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EMBRACING NEW WORLD OF ISLAMIC FINTECH IN MALAYSIA: MOVING TOWARDS DIGITALISATION ERA

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Abstract

Driven by the Fourth Industrial Revolution force, the wave of FinTech has swept across the whole universe including Malaysia. Nowadays, more people begin to believe that FinTech could offer all-time solution for financial problems. As Malaysia is leading the world of Islamic finance, it is the best time to embrace this technology in catching up the worldwide competition. Many financial services providers from other Islamic nations such as Bahrain and United Arab Emirates are aggressively making use of FinTech in their financial products and services. The utilisation of Islamic FinTech in those countries creates a new era of digitalisation when existing system is made to serve better via the technology. The digital transformation changes the traditional view of living and doing business. Analysing the significance of the FinTech, it is crucial to undergo the process of digitalisation for the survival of Malaysia's Islamic finance industry. Hence, in conjunction with the spirit of digital transformation, this paper aims to explore the potential and opportunity lies beneath the Islamic FinTech which should be maximised to boom the Islamic finance industry in Malaysia. Besides that, this research would identify the risks and implications derived from the implementation of Islamic FinTech as a preparation in order to face the future of the digitalisation era.

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Keywords: Islamic FinTech, Islamic finance industry, Malaysia, digitalisation.

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1. Introduction

The popular buzzword of 'FinTech' is used globally to combine two prevailing words namely 'finance' and 'technology'. It is not unusual to sync this term of FinTech with the digitalisation of Islamic financial services and products because both of them are interwoven together nowadays. The digital transformation is resulted from billions of online connections between individuals, societies, communities, organisations, businesses, institutions, companies, devices and machines via mobile technology and the Internet of Things (IoT) (Lau, 2019). The exertion of technology is neutral in Shariah so long it does not contradict its principles. Therefore, to make it applicable in Islamic finance industry, certain FinTech solutions need to observe the Shariah guidelines. Once the elements of Islamic teaching are satisfied, the concept of 'Islamic FinTech' emanates. The adoption of Islamic FinTech has reformed the classical offerings of Islamic financial products into easier and cost-effective offerings through the process of digitalisation. Due to this convenience, the consumers particularly the savvy millennials and digital natives show their favour towards the FinTech alternatives (Global Islamic Financial Report [GIFR], 2017). This industry strives to prosper without compromising on Islamic rules and this points to promising opportunity to collaborate further with FinTech in driving the Islamic finance industry farther in the era of digitalisation (Alam & Gupta, 2017).

2. Islamic FinTech in Malaysia

At the end of 2017, Malaysia was ranked top in global Islamic finance industry due to its production of Shariah-compliant financial assets amounting to RM2.05 trillion (Pikri, 2019). This achievement clearly proves the significance of the nation's role in boosting the growth of the concerned industry. Even if Malaysia is acknowledged as a preeminent contributor in this industry, it is yet considered quite lagging behind in terms of developing Islamic FinTech. The practitioners and the regulators are still in early process to properly understand the mechanism of FinTech and its appropriateness to current landscape Islamic finance (Islamic FinTech Summit, 2018)

Undeniably, there are initiatives demonstrated by the industrial key players to encourage the adoption of FinTech into Islamic financial transactions, products and services. For instance, EthisCrowd as an Islamic crowdfunding online platform has been established with the objective of collectively funding in business, trade, entrepreneurial, real estate activities in Southeast Asia (Global Sadaqah, 2019). Islamic crowdfunding is guaranteed to invest in permissible (halal) projects/products/services by Shariah law in the absence of an interest rate (Biancone et al., 2019). Furthermore, Malaysian Government Advisory Committee (MPM) has entered into a Memorandum of Understanding (MOU) with IncuBlock, a South Korean blockchain lab for the development of Shariah-compliant blockhain (Zuckerman, 2018).

The Investment Account Platform (IAP) is launched as the first FinTech platform for Islamic banking to serve as a hub marketplace in funding the Small and Medium Enterprises (SMEs). The consortium members are Bank Rakyat, Affin Islamic, Bank Muamalat, Bank Simpanan Nasional, Maybank Islamic and Bank Islam (Abdullah, 2017). Apart from that, the local government has established the Malaysian Digital Economy Corporation (MDEC) as an entity which is liable to develop Malaysia's digital business ecosystem. This organisation also earnestly engages with halal ecosystem by giving Shariah

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certification. In addition, a remarkable stride was witnessed when a gold-backed cryptocurrency by HelloGold which is founded by a Malaysian co-founders Robin Lee and Ridwan Abdullah, obtained Shariah-compliance certification from the Shariah supervisory board of Amanie Advisors (HelloGold, 2019; Islamic Finance News, 2018).

However, all these efforts seem to be insufficient due to lack of regulator advocacy. Leaving FinTech without proper regulation will disrupt the whole digitalisation process with the possibility of deceptions, abuse and misapplication of the technology (Oseni & Ali, 2019). Malaysia has a robust framework to cater Islamic finance-related activities, however the progress on the technology part cannot be seen much from the authorities (Whitehead, 2018). Although the Central Bank of Malaysia (BNM) and the Securities Commission (SC) have issued the FinTech Regulatory Sandbox and the guidelines on crowdfunding, there is no adequate action taken in order to coordinate the component of Shariah-compliant in the extant FinTech solutions (Abdullah, 2017). Thus, this regulatory restraint shall frustrate the potentials of Islamic finance institutions to improve their products and services in adopting up-to-date models related to the FinTech solutions like cryptocurrency and blockchain technology (Islamic FinTech Summit, 2018). While in fact, the usage of RegTech would lessen the risk associated to probable breaches of Shariah prerequisite (Qatar Financial Centre, 2018).

3. Islamic FinTech opens new world of digitalisation

The phrases of digitalisation, digital Islamic revolution and digital transformation are habitually mentioned in this last decade (Mohamed & Ali, 2018). Particularly in Islamic finance industry, the process of digitalisation involves the modification of a financial business model by adopting the digital technology (IGI Global, 2019). The technologies are used to upgrade the said business model into a greater form. In this scenario, the technologies included are the big data, artificial intelligence, robotics, blockchain, cryptocurrency and mobile phones. Until this moment, there are more than 100 FinTech companies offering Shariah-compliant products all over the world. And out of this number, about 21 firms are in Malaysia. (Qatar Financial Centre, 2018)

Over the last decades, FinTech is changing the way of Islamic financial system operating by creating tremendous opportunities (Jamil & Seman, 2019). In the past, people need to personally walk and go to the physical bank in order to perform any financial transaction. But nowadays, common financial transactions such as transfer of funds, bill payment and online purchase can be carried out anytime anywhere so long the internet connection does exist. Islamic financial transaction becomes more automated and user-friendly. At the same time, this shall direct to a secured, transparent and efficient Islamic financial market for the key players (Islamic Finance News, 2018). This phenomenon has evolved a new mechanism of financial transactions i.e., smart contracts compared to the traditional contracts typically used in the past (Rahim et al., 2019).

The fruitful arrangement of Islamic FinTech solutions such as blockchain technology would immensely increase the sum of financed Small and Medium Enterprises (SMEs). Moreover, phone-based biometric identity applications via fingerprints and voice or facial recognition could equip the unbanked individuals with a digital identity. Ingrained in the blockchain, this digital profile would comprise unchangeable birth record, educational background and medical history, voter registration and property

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titles, bringing the customers into the financial cycle (Qatar Financial Centre, 2018) In July 2018, Stellar has been reported to become the first Shariah-compliant blockchain licensed by the Central Bank of Bahrain, the Shariyah Review Bureau (SRB) (Alexandria, 2019). All activities ventured by Stellar and its subsidiaries are unquestionably regarded as Shariah-compliant. This recognition indicates a large-scale improvement as the cryptocurrency sector counters much ambiguity and negative suspicion by the public. Presently, the Islamic world begins to look at blockchain technology in a positive manner (Cromley, 2018).

In 2018, the Blossom Finance, a United States firm has announced the first SmartSukukTM platform. It is composed with end-to-end Shariah compliance details. The company assures that all 'smart contracts' would use the only approved Shariah structures including asset-based lease (Ijarah) and profit-sharing (Mudarabah) (Blossom, 2019). The shareholders will be capable to participate in the digital sukuk by using the Ethereum blockchain, which will then be used to fund Shariah-compliant microfinance enterprises in Indonesia. From the situations aforementioned, the blockchain technology manages to boost the Islamic trade finance through various financial activities.

Besides that, Islamic FinTech can effectively captivate higher percentage of possible customers including the non-Muslims through digital channels by requiring the new customers to sign up for a digital wallet account which normally authorises bill payments, micro credit and fund transfers in shorter duration of time compared to prior traditional mean of transaction (Qatar Financial Centre, 2018). This digital wallet feature facilitates the consumers to carry out financial transactions only by using their electronic gadgets such as smart phones, tablets or laptop. Even those who do not own a bank account including the illegal immigrants and refugees can actively engage in the services and products offered which originally remain out of their reach if not for this FinTech solution (Todorof, 2018).

Furthermore, Algebra has been invented to fulfil the market demand for Shariah-compliant investments as the Asia's earliest artificial intelligence-based Islamic financial robo-advisor (Noordin, 2017). It is reported that this retail reached $60 billion assets of clients by the end of 2015 and it expects to hit $2 trillion in 2020. The policy which is Shariah-compliant applied by the platform has been certified by the Amanie Advisors (Fazmi, 2019). All in all, more flexible alternatives are offered in comparison with the traditional banking and payment systems via the operation of Islamic FinTech exceptionally in Malaysia.

In contrast, the opportunities aforementioned can be viewed as a peril to the Islamic finance institutions (IFIs) from different angle. As it is still at early stage, the Islamic finance institutions might be intimidated from the evolution of Fintech. According The 2016 Global Consumer Banking survey warned that 40% of customers reduced their reliance on the bank as their primary financial services provider. Instead, they likely prefer to depend on FinTech providers (Hasan, 2017). With low costs and rapid expansion, Islamic FinTech could also threaten the traditional banking market (Digital News Asia, 2016). Alerting the expected threat in the future, it is necessary for the Islamic Financial Institutions (IFIs) to embed themselves into the digital strategies and expansion to maintain their spot in this industry.

4. Future of Islamic FinTech in Malaysia

In 2020, the digital banking consumers in Asian region are foreseen to attain more than 1.7 billion in total (Fong, 2017). It is worth noting that there is consequential margin for production across the Islamic

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FinTech ecosystem (Dinar Standard, 2018). Nonetheless, the market for FinTech-based Islamic finance is gigantic in Malaysia even though it is still at its early stage. The financial technology is no longer an option but fundamental for those who are the Islamic finance industry players (Noordin, 2017).

Dr Farrukh Habib said that Islamic FinTech may hold some promise for Malaysia, unless and until the authorities keep their attention and find ways to entice new entrepreneurs to their jurisdiction (Whitehead, 2018). There is a need for regulatory mechanism enforced to administer Islamic FinTech affairs (Oseni & Ali, 2019). Obviously, Malaysia shall provide big number of opportunities for more Islamic FinTech platforms to emerge which cater their desire to heed their belief and religion (Pikri, 2019). As of 2018, Muslim population reaches at least 69.1% in Malaysia (Malaysia Department of Statistics, 2019). This percentage signifies that Islamic finance industry would be more favourable by this nation. Increasing demand for Shariah-compliant financial products/services must be met (Firmansyah & Anwar, 2019). Even the non-Muslims have begun converting their interest to Shariah-compliance finance because Islamic financial institutions banned the payment of interest i.e. usury. So, it is rational for them to opt for this service to avoid the payment of unlikely interest. Obviously, this illustrates the positive viability of Shariah-compliant market products and services in Malaysia.

Whereas in 2017, the sukuk market was $422 billion. Ensuing to tap all possible segments in sukuk market, digital sukuk is essential to that (Williams, 2018). As a response to this need, Malaysian government and Islamic finance institutions affiliated with other FinTech providers should provide the alternatives. Thus, Islamic FinTech would expand and extend larger in Malaysia's Islamic finance sector due to the integration of initiatives and incentives carried out by the concerned parties.

Along with stronger penetration of mobile phone and internet, this occurrence triggered the FinTech implementation as there are an expected 50,000 3G subscriptions for every 100 inhabitants by the end of 2022 (Asian Banking & Finance, 2018). As reported by Findex, 78% of the globe's non-banked adults accepting wages use a mobile phone (Yan, 2019). It becomes a world phenomenon for the digital-savvy consumers to transfer money through their smartphones. As Malaysia aims to succeed in digital economy, the government has introduced e-payment looking at the upward trend of smartphones by year to year. The direction for this online platform is bright as more consumers are using this service from time to time.

It is hopeful that the future of Islamic FinTech is encouraging globally (Wintermeyer & Basit, 2019). Supposed Malaysia intends to sustain its sound excellence in Islamic finance space, the industry players such as the banks and FinTech providers are highly encouraged to collaborate together.

5. Conclusion

Technology evolves very fast; thus it is vital for the financial key players to act faster in order to avoid the risk of losing market share. The existing Islamic finance industry has started to embrace the aeon of digitalisation as a mean to thrive and get ahead, however it is somewhat slow. Since Islamic FinTech is still at its infancy phase, it is gradually trying to catch up the rapid development of the worldwide FinTech landscape which has been broadened in recent years. Still, it is evident to say that the Islamic FinTech has been progressing consistently by looking at the market demand and innovations applied in the products and services of Islamic finance. The industrial revolution has precipitated the changes of our way of working, living and socialising with others. Undoubtedly, this revolution would induce a big impact against the finance industry as a whole. Since Islamic finance industry operates in digital age, it cannot elope the FinTech revolution in order to outlast. The future of Islamic FinTech appears to be auspicious as Islamic finance industry keeps growing and embracing the utilisation of mobile and internet banking day by day. Thus, this opens up to the new world of Islamic FinTech in Malaysia to fit the involved industry key players in the age of digitalisation.

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