



THE VIABILITY OF A FULLY-INTEGRATED ISLAMIC
FINANCIAL AND INVESTMENT INSTITUTION
CONCEPT TOWARD THE ACHIEVEMENT OF
MAQASID AL-SHARI'AH: A CASE STUDY OF
MALAYSIA

BY

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ABSTRACT

The fully-integrated Islamic financial and investment institution concept (“the FIIFII concept”) is basically an integration of all the functions and activities of Islamic banking, Islamic insurance and Islamic capital market under the one roof concept. This concept is similar to the “Islamic Universal Banking” concept whereby such an integrated institution has the capability to provide its customers with a wide range of financial and/or capital market products and/or services within the confinement of the Shari’ principles that provide the equity objective and the Tabi’ principles that provide efficiency objective. The concept is being formulated toward achieving the main components of maqasid al-Shari’ah (“the higher objectives and intents of Islamic laws or the Shari’ah”) namely; the justice, the wisdom, the mercy and the benefits. To-date, there has been no fully-integrated Islamic financial and capital market institutions in existence anywhere in this world. Therefore, it would be difficult to make performance comparisons with the conventional counterparts. The principal objective of this research is to study the viability of the FIIFII concept toward achieving maqasid al-Shari’ah in the case of Malaysia. There are two quantitative aspects in this research that had been undertaken by using the secondary information sources gathered from Malaysia’s conventional financial and capital market groups. There are also two qualitative aspects in this research that had been undertaken by using the primary information sources gathered through the survey techniques vide the use of questionnaires and/or interviews with the experts comprising the Shari’ah and Islamic financial scholars, the Islamic financial practitioners, the regulators, the advisers and the politicians and these experts would come from the local universities, Islamic financial institutions, Bank Negara Malaysia, the Securities Commissions, Bursa Malaysia and the federal and state religious institutions. The research on the viability of this FIIFII concept had been done in three parts. The first part had been to measure and compare the financial and efficiency performances of three fully-integrated financial and capital market groups with those of the other three semi-integrated counterparts by using the respective Conventional Financial Analysis (“the CFA”) and Data Envelopment Analysis (“the DEA”) techniques. The second part had been undertaken vide the surveys to ascertain that the FIIFII concept could operate better should maqasid al-Shari’ah act as the guiding principles in its operations. The third part had been undertaken vide the surveys to study on the viability of the FIIFII concept toward the achievement of maqasid al-Shari’ah. The findings and analysis from the use of the CFA and DEA techniques had shown that the three fully-integrated financial and capital market groups have on a 10-year period to the 2011 financial year, performed better financially and efficiently than their semi-integrated counterparts. The surveys undertaken had found that all the functions and activities of the FIIFII concept would be inseparable from those components of maqasid al-Shari’ah and should be aimed at achieving the maqasid. The surveys undertaken on the viability of the FIIFII concept had found that the FIIFII concept would be feasible in the context of Malaysia and would be a better alternative to the country’s existing Islamic financial and capital market system. It is therefore, recommended that Malaysia should seriously consider developing the FIIFII concept of the Three-tier structure whereby the FIIFII Foundation would act as the policy decision entity, the FIIFII Holding Company as the coordinating entity, and the FIIFII Main Subsidiaries as the implementing entities. It is proposed that the FIIFII concept should be operating in a competitive environment and in parallel to the country’s existing Islamic institutions in order to be profitable, efficient and more importantly, the FIIFII should be able to achieve the maqasid. It is also proposed that the FIIFII should not be owned or controlled by the Government as its intervention would not necessarily bring success. In the final analysis, it is felt that the FIIFII concept should be a viable financial alternative to Malaysia’s existing Islamic financial and capital system and this FIIFII concept should urgently be developed in stages to meet the challenges of the twenty-first century.

ملخص البحث

يعد مفهوم مؤسسة التكامل الإسلامي للاستثمارات المالية هو في الأساس، وهو عبارة عن دمج جميع المهام والأنشطة الخدمية المصرفية الإسلامية والتأمين الإسلامي وأسواق رأس المال الإسلامي تحت مفهوم إطارى موحد. هذا المفهوم هو مشابه للمفهوم "العالمي للمصارف الإسلامية"، حيث إنه يمثل مؤسسة متكاملة لديها القدرة على تزويد عملائها بمجموعة واسعة من المنتجات أو الخدمات المالية أو أسواق رأس المال داخل نطاق مبادئ الشريعة "التي توفر الهدف والعدالة ومبادئ التابعين لها" والتي بدورها توفر هدف تحقيق الكفاءة. ويجري حالياً صياغة مفهوم نحو تحقيق هذه المكونات الرئيسية لمقاصد الشريعة ("الأهداف العليا والمقاصد للقوانين الإسلامية أو الشريعة") وهي تشمل: العدل، الحكمة، الرحمة، الفائدة أو المنفعة. ولكن حتى الآن، لم يكن هناك أي وجود لأي نوع من أنواع المؤسسات المالية وأسواق رأس المال الإسلامية المتكاملة في هذا العالم. ولذلك، فإنه سيكون من الصعب إجراء مقارنات مع نظيراتها التقليدية. ولذلك يكمن الهدف الرئيسي من وراء هذا البحث هو دراسة جدوى مفهوم مؤسسة التكامل الإسلامي للاستثمارات المالية نحو تحقيق المقاصد المتوافقة مع الشريعة الإسلامية باتخاذ دولة ماليزيا نموذجاً. علماً بأن هناك نوعين من الجوانب الكمية في هذه البحوث التي أجريت باستخدام مصادر المعلومات الثانوية التي تم جمعها من المجموعات المالية وسوق رأس المال التقليدية في ماليزيا. هناك أيضاً صنفان من الجوانب النوعية في هذا البحث الذي تم إنجازه باستخدام مصادر المعلومات الأولية التي تم جمعها من خلال تقنيات المسح باستخدام الاستبيانات أو المقابلات الشفوية مع علماء الشريعة وخبراء المال في الدول الإسلامية، بالإضافة إلى المتفرسين في شئون المال والمنظمين، والمستشارين والسياسيين وكل هؤلاء الخبراء يمثلون مجموعة بحثية متنوعة من الجامعات المحلية والمؤسسات المالية الإسلامية، مثل بنك نيجارا ماليزيا، وهيئات الأوراق المالية في بورصة ماليزيا والمؤسسات الدينية في الدولة والاتحادية. قد أجرى البحث لمعرفة جدوى مفهوم مؤسسة التكامل الإسلامي للاستثمارات المالية في ثلاثة محاور. المحور الأول كان لقياس ومقارنة الأداء المالي والكفاءة لثلاث مجموعات مالية سوق رأس مالها متكامل تماماً مع نظيراتها الثلاثة الأخرى شبه المتكاملة أي التي تستخدم الأساليب التقليدية للتحليل المالية منها مثل ("تحليل الاستثمار التوافقي") ووفقاً لتحليل البيانات. تم إجراء المحور الثاني بمسح المعلومات للتأكد من أن مفهوم مؤسسة التكامل الإسلامي للاستثمارات المالية يمكن أن يتم بشكل أفضل لو أنه طبق مقاصد أحكام الشريعة كمبادئ توجيهية في العمل. تم تنفيذ المحور الثالث بتوصية المسوحات لدراسة حول جدوى مفهوم مؤسسة التكامل الإسلامي للاستثمارات المالية نحو تحقيق المقاصد الشرعية. وكانت النتائج التي تم تحليلها باستخدام تقنيات التحليل الاتفاقي وكالة مكافحة المخدرات، أظهرت أن مجموعات السوق المالية، ورؤس الأموال المتكاملة الثلاثة خلال فترة العشرة سنوات وصولاً إلى السنة المالية للعام 2011م، كان أداءها أفضل من الناحية المالية ومن حيث الكفاءة مقارنة بنظيراتها شبه المتكاملة. وبناءً على الاستقصاءات التي وجدت تبين أن جميع مهام وأنشطة مفهوم مؤسسة التكامل الإسلامي للاستثمارات المالية سيكون جزءاً لا يتجزأ من مكونات مقاصد الشريعة ويجب أن تهدف إلى تحقيق هذه المقاصد. إن الاستقصاءات التي أجريت بغرض معرفة جدوى مفهوم مؤسسة التكامل الإسلامي للاستثمارات المالية وجدت أن مفهوم مؤسسة التكامل الإسلامي للاستثمارات المالية سيكون ممكنة في سياق دولة ماليزيا، وسيكون أفضل بديل للنظام المالي وسوق رأس المال الإسلامي الموجودة في البلاد. ولذلك، توصي الدراسة بأن ماليزيا يجب أن تنظر بجدية في تطوير مفهوم مؤسسة التكامل الإسلامي المالي للاستثمار بحيث تتم هيكلة من ثلاث طبقات بموجب مفهوم مؤسسة التكامل الإسلامي للاستثمارات المالية وذلك سيكون بمثابة كيان بقرار سياسي، ومفهوم مؤسسة التكامل الإسلامي للاستثمارات المالية القابضة بمثابة هيئة تسييرية، والشركات التابعة لمؤسسة التكامل الإسلامي للاستثمارات المالية الرئيسية مثل الهيئات المنفذة. ومن المقترح أن مؤسسة التكامل الإسلامي للاستثمارات المالية يجب أن تعمل في بيئة تنافسية، وبالتوازي مع المؤسسات الإسلامية القائمة في البلاد من أجل أن تكون مرحة وفعالة، والأهم من ذلك، يجب أن تكون مؤسسة مؤسسة التكامل الإسلامي للاستثمارات المالية قادرة على تحقيق تلك المقاصد. ومن المقترح أيضاً أن مؤسسة التكامل الإسلامي للاستثمارات المالية لا ينبغي أن تكون مملوكة أو مسيطراً عليها من قبل الحكومة، وتدخلها لأن ذلك لا يحقق بالضرورة النجاح. في التحليل النهائي، يرى أن مفهوم مؤسسة التكامل الإسلامي للاستثمارات المالية ينبغي أن يكون البديل المالي السليم للنظام المالي، رؤوس الأموال الإسلامية الموجودة في ماليزيا، وينبغي على وجه السرعة أن يتم تطوير مفهوم مؤسسة التكامل الإسلامي للاستثمارات المالية على مراحل مختلفة لمواجهة تحديات القرن الحادي والعشرين.

APPROVAL PAGE

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DECLARATION

I hereby declare that this dissertation is the result of my own investigation, except where otherwise stated. I also declare that it has not been previously or concurrently submitted as a whole for any other degrees at IIUM or other institutions.

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This dissertation is dedicated to my beloved parents and family members

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CHAPTER ONE

INTRODUCTION

This chapter is divided into three parts. The first part analyzes both the global and local trends of financial and capital markets and provides the possible justifications for reforming the various Islamic financial and capital market institutions in Malaysia. The second part clarifies the preliminary concept of the research with the title namely; “The Viability of a Fully-Integrated Islamic Financial and Investment Institution Concept toward the Achievement of Maqasid al-Shari’ah: A Case Study of Malaysia.” The third and final part explains the organization of the research which comprises statement of the problem, thesis statement, research objectives, research questions, significance of the research, scope and limitations of the research, and proposed chapters of the research.

1.1 FINANCIAL AND CAPITAL MARKET TRENDS AND THE POSSIBLE JUSTIFICATIONS FOR REFORMING THE VARIOUS ISLAMIC FINANCIAL AND CAPITAL MARKET INSTITUTIONS IN MALAYSIA

This part analyses the recent trends of both the global and local financial and capital markets and provides the possible justifications for reforming the various Islamic financial and capital market institutions in Malaysia and covers the following sub-topics:

1.1.1 Analysis of the Trends of both the Global and Local Financial and Capital Markets

Since the early twenties, the world has been witnessing an evolutionary transformation of her financial and capital markets. This transformation process is still ongoing and

judging from the prevailing trends, the financial and capital markets worldwide are characterized by globalization of operations, liberalization of markets, integration of institutions, one-stop shop, and more product flexibility. These trends of the global financial and capital markets are seemingly leading towards the highly competitive environments amongst the market players as characterized by the growing operational efficiencies of such markets. The growing operational efficiencies are the result of economies of scale brought about by the critical mass markets of myriads of gigantic financial and capital market institutions.

The world has also recently been witnessing many restructuring and reorganization exercises undertaken on the components of financial and capital markets and as a result, there exist a wide range of financial and capital market products with better product flexibility and the existence of comprehensive network on information technology. Malaysia is no exception to this phenomenon. The country's various conventional banking/financial institutions, insurance companies, and securities/investment houses are currently undergoing the process of restructuring and reorganization through various mergers and acquisitions so as to be in line with the global trend.

1.1.2 The Possible Justifications for Reforming the Various Islamic Financial and Capital Market Institutions in Malaysia

The current performances of Islamic banks, Islamic insurance companies, and Islamic capital market institutions in Malaysia are still considered to be unsatisfactory, as most of these Islamic institutions are considered to be quite insignificant in terms of capitalization and operations but are observed to be growing rapidly. Perhaps if no efforts are made to reform these Islamic institutions in line with the reforms that are

currently being undertaken for Malaysia's conventional banks, insurance companies and securities/investment houses, then the process of Islamizing the country's financial and capital markets would not materialize, and those Islamic institutions would definitely be marginalized. In view of this, the Islamic financial and capital market institutions in Malaysia are felt to be in a dire need to reform, while contributing to the attainment of maqasid al-Shari'ah ("the higher objectives and intents of Islamic laws or the Shari'ah"). It is in this direction that the research is being undertaken.

In 2008, the world had witnessed the severe financial crisis arising from the failures of the internationally-renowned specialized financial institutions such as AIG, JP Morgan, Citicorp, Barclays Bank, National Westminster Bank and Royal Bank of Scotland in their financing policies and practices, especially in the field of real estate investment and properties financing. With an exception of Union Bank of Switzerland that had suffered badly from its US bond transactions, and DG Bank of Germany that had been negatively affected by the rising energy prices, most of the renowned universal banks in Switzerland, Germany, France and Spain had survived from this crisis. This financial crisis had shown the superiority in performance of the universal banks as compared with that of the specialized banks. It has been observed by financial scholars and writers such as Jordi Canals¹, and Anthony Saunders and Ingo Walter² that the attributing factors to this superior performance can be articulated around the following points:

- a) The presumed advantages for any universal bank arise from economies of scale and scope - any universal bank offers two major types of cost

¹ Canals, Jordi, "*Universal Banking: International Comparisons and Theoretical Perspectives*," (Oxford University Press Inc., New York, 1997).

² Saunders, Antony and Walter, Ingo, "*Universal Banking in the United States*," (Oxford University Press, New York, 1994).

advantage. There are prevalent advantages arising from possible economies of scale: the larger the volume of operations in a certain activity for a given level of overhead or investment, the greater the organization's effectiveness. There are also the advantages arising from sharing costs between different business units, so that the total cost of offering these activities by different units is greater than the cost incurred when they are offered together: these are the so-called economies of scope;

- b) The ability of any universal bank to attract or retain customers on the basis of offering a broad range of financial products – a universal bank offers a wide range of financial products and services to its customers, so that they do not depend on different financial firms. Being a one-stop supplier for various financial services, a universal bank may hold a greater appeal for the customers than any specialized bank due to the comprehensive services it can offer; and
- c) The universal bank runs a lesser risk of substitution than any specialized bank for the simple reason that the universal bank with several, more or less interrelated and services that is able to rebalance its various business depending on internal resources and the dynamics of competition in each financial product, has an option to penetrate the more quickly emerging segments within the financial services industry – the impact on financial innovation of a universal bank and its diversification activities has contributed towards a lesser substitution risk that a specialized bank runs when facing with a drastic change in the demand for financial services.

1.2 PRELIMINARY CONCEPT OF THE RESEARCH

This part clarifies the preliminary concept of this research namely; the viability of a fully-integrated Islamic financial and investment concept (“the FIIFII concept”) toward the achievement of maqasid al-Shari’ah in the case of Malaysia, and covers briefly several sub-topics namely; the FIIFII concept, the maqasid al-Shari’ah, the scope of activities under the FIIFII concept, and the structure of the proposed model of the FIIFII concept for Malaysia.

1.2.1 The FIIFII Concept

The FIIFII concept refers to that of a fully-integrated Islamic financial and investment institution. The FIIFII concept is basically an integration of all the functions and activities of Islamic banking, Islamic insurance, and Islamic capital market under the one roof concept. It is being formulated by incorporating the Islamic universal concept and Islamic guiding principle towards achieving the mission statement of “Delivering innovative and mutually beneficial financial and investment products, for our investors and borrowers that free them from the shackles of riba’ (“the interest in all its various forms”), maisir (“the gambling”) and gharar (“the ambiguities”) and in the fulfillment of maqasid al-Shari’ah”.

The FIIFII concept can be equated to the term “Islamic Universal Banking” concept whereby such Islamic integrated institution has the capability to provide its customers with a wide range of financial and/or capital market products and/or services within the confinement of both the Shari’ and Tabi’ principles, and in cognizance with the maqasid al-Shari’ah. Shari’ principles provide equity objective whereas Tabi’ principles provide efficiency objective. Shari’ principles in financial transactions are: the prohibition of riba’, the application of al-bay’ (“the trade and

commerce”), the avoidance of gharar in contractual agreement, the prohibition of maisir, and the disengagement from production of prohibited commodities.

1.2.2 The Maqasid Al-Shari’ah of the FIIFII Concept

The maqasid is simply the interests that are obtained by persons in this world and in the hereafter, either by means of obtaining benefit or through prevention of harm. The interest refers to an attribute, deed or action that brings benefits to the general public or individuals at all times or most of the time. The prevention of harm refers to an attribute, deed or action that would result in destruction or harm to the general public or the individuals either all times or most of the time. The maqasid in a general sense is the essence, and the ruling of the Shari’ah or the command that is conspicuous in all circumstances or in the majority of the cases. The Shari’ah is inseparable from its maqasid. The maqasid are an integral part of the commands and prohibitions of the Al-Mighty Allah Swt. (“the Lawgiver”).³

According to Al-Shatibi in his Al-Muwafaqat, the maqasid al-Shari’ah is divided into the primary purpose and the complementary purpose. The primary purpose is the necessary benefits for the public, which aims at the protection of religion, life, mind, progeny and property. The complementary purpose fulfills the wishes and desires of the competent person, and at the same time, he is allowed to participate in determining it for his needs and desires, such as getting food, shelter, marriage, clothing, etc. that facilitate his life.⁴

The FIIFII concept is very much inseparable from the maqasid al-Shari’ah as all the functions and the activities of the FIIFII are aimed at achieving the main

³ Sharif, Samsuri Bin, “*Consolidation of Multi-Contracts in the Islamic Financial Transactions*”, (IIUM, 2003).

⁴ Al-Raysuni, Ahmad, “*Imam Al-Shatibi’s Theory of the Higher Objectives and Intents of Islamic Law*”, (The International Institute of Islamic Thought, Hendon VA, USA, 2006).

elements or components of the maqasid namely; the hikam (“the wisdom”), the adl (“the justice”), the maslahah (“the interests”), and the rahmah (“the mercy”) of the Islamic financial and capital market institution. These elements of maqasid al-Shari’ah are general and can be applied in the structure and development of the FIIFII concept.

1.2.3 The Scope of Activities under the FIIFII Concept

The FIIFII concept which provides its customers with a wide range of financial and capital market services within the confinement of both the Shari’ and Tabi’ principles and in cognizance with the maqasid al-Shari’ah, shall encompass all activities pertaining to Islamic Commercial Banking, Islamic Investment Banking, Islamic Development Banking, Islamic Insurance or the Takaful, and Islamic Social Banking as elucidated below:

- a) Islamic Commercial Banking will encompass all the Shari’ah-compliant activities pertaining to corporate banking such as lending, trade facilities and deposit-takings; retail banking such as personal credits and savings, debit card facilities, housing and motor financing; general commercial banking services such as automated telling machine (“the ATM”) facilities for electronic banking, custodian services and foreign exchange (“the FOREX”) transactions; and trustee services such as nominee-ship and trusteeship.
- b) Islamic Investment Banking will encompass all the Shari’ah-compliant activities pertaining to corporate finance advisory that shall cover mergers and acquisitions, listings of securities and debt-structured financing and advisory; wealth management that shall cover all forms of investment management; securitization and trading that shall cover capital market