

## **KNOWLEDGE AND APPLICATION OF ISLAMIC FINANCIAL PLANNING AMONG SMALL AND MEDIUM ENTERPRISES HALAL OPERATORS IN PENINSULAR OF MALAYSIA**

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### **ABSTRACT**

Malaysia plays an important role in halal industry at national and international level. In the Eleventh Malaysia Plan, 2016–2020, the halal industry was emphasised by the Prime Minister to ensure that the halal industry is highly and persistently competitive. In Asia, Malaysia is considered as a leader in the development of halal hub centre. However, halal industry is not only about halal food production but also covers the Islamic finance services that prohibit riba, gharar (uncertainties), and maysir (gambling). Islamic financial planning is one of the important parts of Islamic finance because it plays a big role in providing Shariah-compliant funds and investment opportunities especially to halal SME operators. The holistic approach of halal industry should also covers not only halal food production but also the Islamic financial planning that includes activities such as creating, increasing, purifying, and protecting wealth from the Islamic perspective. Thus, this study has conducted a survey on knowledge on Islamic financial planning among halal SME operators in Peninsular Malaysia. The findings of this study revealed that the knowledge of Islamic finance was significantly correlated with the application of Islamic financial planning among halal SME operators. This finding indicated the importance of integration between knowledge on halal food production with Islamic financial planning activities. This relationship recognises the importance of knowledge and practice of Islamic financial planning among halal SME operators in promoting halal products and services and boosts demand for Malaysian halal products at the international level.

**Keywords:** Halal industry, Halal SME operator, Islamic financial planning

## **PENGETAHUAN DAN APLIKASI PERANCANGAN KEWANGAN ISLAM DI KALANGAN OPERATOR HALAL PERUSAHAAN KECIL DAN SEDERHANA DI SEMENANJUNG MALAYSIA**

### **ABSTRAK**

Malaysia memainkan peranan penting dalam industri halal di peringkat kebangsaan dan antarabangsa. Dalam Rancangan Malaysia Kesebelas, 2016-2020, industri halal ditekankan oleh Perdana Menteri untuk memastikan bahawa industri halal kekal berdaya saing. Di Asia, Malaysia dianggap sebagai pemimpin dalam pembangunan pusat hub halal. Bagaimanapun, industri halal bukan sahaja tentang pengeluaran makanan halal sahaja tetapi juga meliputi perkhidmatan kewangan Islam yang melarang riba, ketidakpastian, dan perjudian. Perancangan kewangan Islam ialah salah satu bahagian penting dalam kewangan Islam kerana ia memainkan peranan besar dalam menyediakan dana patuh Syariah dan memberi peluang pelaburan terutamanya kepada pengusahahalal PKS. Pendekatan secara holistik dalam industri halal juga harus meliputi halal keseluruhan bukan sahaja pengeluaran makanan tetapi juga perancangan kewangan Islam yang termasuk aktiviti seperti mencipta, menambahkan, menyucikan, dan melindungi kekayaan dari perspektif Islam. Maka, kajian ini telah menjalankan penyiasatan tentang pengetahuan perancangan kewangan Islam antara pengusaha halal PKS di Semenanjung Malaysia. Hasil kajian ini menunjukkan bahawa pengetahuan perancangan kewangan Islam nyata sekali berhubung kait dengan permohonan perancangan kewangan Islam di kalangan pengusaha halal PKS. Hasil kajian ini juga menunjukkan kepentingan integrasi antara pengetahuan dalam pengeluaran makanan halal dengan aktiviti perancangan kewangan Islam. Hubungan yang signifikan ini menjelaskan kepentingan pengetahuan dan amalan perancangan kewangan Islam antara pengusaha halal PKS dalam mempromosikan produk dan perkhidmatan halal dan seterusnya merangsang permintaan untuk produk halal Malaysia di peringkat antarabangsa.

**Kata kunci:** industri halal, pengusaha halal PKS, perancangan kewangan Islam

### **INTRODUCTION**

Small and medium-sized enterprises (SMEs) in Malaysia are expected to contribute more than 40% to the gross domestic product (GDP) of the country by 2020. High demands for halal products and services further increase the role of SMEs in the economy of the country. Thus, SMEs are urged to get a certified halal certification to seize lucrative opportunities in the global halal sector. To ensure

that the process of the whole production is halal, halal SME operators are recommended to apply the Halal Standards in the sales production process. However, there is still a gap in applying for Islamic financial planning in the business activities such as financing and investing activities which involve prohibited elements such as *riba*, *gharar*, and *maysir*.

Halal Standards (HS) set by government authorities such as Halal Industry Development Corporation (HDC) and Jabatan Kemajuan Islam Malaysia (JAKIM) are responsible to conduct halal certification and auditing processes which are based on good quality value, safe, and trust as a precondition to achieve HS in implementing strategies for the development of the industry. The HS is also capable in enhancing good governance in several sectors, business activities, halal supply chain, and halal experts. The terms used in HS are crucial in promoting Malaysia as a global halal hub centre. The development of halal industry can also contribute to good business environments such as a business-friendly ecosystem and network collaboration between related government and private agencies. Therefore, to achieve a holistic view of the HS, there is a need to integrate halal industry with Islamic finance.

## **HALAL SME OPERATORS**

The definition of SME is mainly based on annual sales turnover and total number of full time occupied by an enterprise (Hashim and Abdullah, 2000; Small and Medium Enterprises Corporation Malaysia [SEMCORP], 2008). According to Hashim, M.K (2000), SME in Malaysia can be categorised into three main sectors which are general business, manufacturing, and agriculture. In Malaysia, according to SMECORP (2008), enterprise that employs 50–150 full-time employees is considered as a medium enterprise, while enterprise that employs 5–50 employees is called small enterprise and less than five employees of employment is considered as a micro enterprise. Mohani Abdul (2008) suggested that incentives should have been formulated to encourage more businesses to go into halal and financial institutions that have targeted SME in particular to achieve halal certification. Table 1 shows the statistic information on financing sources obtained from the 2011 Economic Census (Profile of Small and Medium Enterprises). In 2010, more than half of the SMEs use their own internal generated funds or funds raised from shareholders to finance their business operations. 21.9% of SMEs obtained funds through micro credit and from financial institutions such as banks and developed finance corporations. Financial aids obtained from other sources such as grant or fund from government agencies and financial cooperatives were at 28.5%. Based on the size of organisation, the statistic revealed that the fund from financial institutions is the major financing source (51.7%) for medium-sized SMEs. However, small and micro enterprises rely mainly on internally-generated

funds. Only 17.4% of micro enterprises had secured financing from financial institutions.

The development of halal industry will become more competitive with the involvement of the Islamic finance and banking industry. Although the Islamic finance and banking in Malaysia has been established since 1960s, the system is not yet integrated with halal industry. Today, there are many views from halal experts and political leaders to integrate halal products and Islamic financial system. This information is relevant to be used to show the importance of expanding the halal concept to cover the planning for financing aspect. Therefore, the concept of halal products and Islamic financial planning should go hand in hand.

There are 56 verses of the Qur'an that mention the word 'Halal' and its root words and 21 verses stress on food consumption. In addition, there are many *hadith* of the Prophet mention about Halal in different contexts and meanings according to the treaties of the *Sunnah* of the Prophet Muhammad (peace be upon him). There are some indicators that can help to understand the importance of integrating Halal products industry with Islamic banking and finance (Irfan et.al., 2016). For instance, a hadith stated by the Prophet (peace be upon him), "*those who eat Riba even a dirham, it is as the sin of 33 times of adultery, one that grows out of the meat from illegal sources, then the hell is the key for him*" (At-Thabarani, 1983). This hadith shows us that Allah prohibits anyone from committing Riba in total and a very ultimate consequence will occur to those who involve in Riba. Meanwhile, Allah has ordered Muslims to accept Islam as the way of life in total as mentioned in a verse of surah al-Baqarah, "*O you who believe, enter into Islam completely (and perfectly...)*" (Surah Al Baqarah, verse 208). This verse shows us that Allah has brought his order for the people to implement their affairs of life as a holistic system and not separately. Thus, halal concept should also be integrated with the sales operation and also the financing and investing activities through business firms. From the investing activities, halal SME operators should be aware and occupy knowledges in saving, financing, and investing money based on the Shariah requirement that prohibits interest, gharar, gambling activities, and production of prohibited products.

Daud Vicary Abdullah, the Chief Executive Officer of the International Centre of Education in Islamic Finance (INCEIF) stated, "to ensure that the whole production process is halal, the source of financing should also be from a halal source, i.e. by using Islamic banking services."

These spirits become a reality through the halal SME operators in Malaysia via the Eleventh Malaysia Plan, 2016–2020 (11MP). If all of the halal SME operators are required to apply Islamic financial plan in their business activities, this will guarantee a tremendous increase in demand for halal products and halal industry will continue to grow and resembles the holistic view of halal standards in Islam.

Table 1. Sources of Financing for SME According to Size of Enterprise In 2010

Profile Company	Financial Resources				
	Banking, Microcredit, And Developed Institutions	Finance	Internally Generated	Friends And Family	Other Sources
Total	21.9		56.1	14.3	28.5
Micro	17.4		58.1	15.0	27.5
Small	33.0		49.8	12.8	31.4
Medium	51.7		47.8	8.7	32.0

Source: 2011 Economic Census (Profile of Small and Medium Enterprises)

## ISLAMIC FINANCIAL PLANNING

Being prudent and sensible in managing money and wealth are crucial for every individual, family, and organisation. A previous study done by Hilgert and Beverly (2003) found that there was a positive connection between financial knowledge and the behaviour to practice financial planning. The results of the study indicated that those with basic financial knowledge were able to prepare savings for future retirement.

Meanwhile, Gitman and Joehnk (2002) had arranged the process of financial planning that involved six steps as mentioned below;

- i. Define financial goals,
- ii. develop financial plans and strategies to achieve goals,
- iii. implement financial plans and strategies,
- iv. periodically develop and implement budgets to monitor and control progress toward goals,
- v. use personal financial statements to evaluate results of plans and budgets, taking corrective action as required, and
- vi. redefine goals and revise plans as personal circumstances change.

In comparison, the dimension of Islamic financial planning is grounded based on the demand of Shariah. Islamic financial planning is defined as the process of meeting life goals through the management of finances in accordance with the Shariah such as how to increase, create, protect, purify, and distribute wealth based on Shariah guidelines. Shariah rules and principles are incorporated into the process of financial planning and form the core position in the application of Islamic financial planning (Lahsasna, 2010). Hence, Shariah decree has to be observed and adhered throughout the process. Lahsasna (2010) further defined Islamic financial planning as a process of determining financial goals, priorities,

and resources to be met optimally within the parameters stated by the Shariah. The crux of Islamic financial planning is the planning itself in pursuit of meeting the individual goals through execution and monitoring of the financial plan. The Islamic teachings always urge Muslims to plan and take necessary actions to ensure they succeed in life.

Thus, the six-step process of financial planning seems to be similar in both practices as individuals would set their financial objectives and as well as to strive in achieving those objectives. However, the intention to conduct a financial planning based on Shariah and its underlying principles of permissible (halal) transactions distinguishes the implementation measures in both practices. In wealth protection aspect, the Muslims are recommended to apply for a *Takaful* scheme and to finance halal business operations, while the halal business operators are recommended to use financing products offered by the Islamic financial institutions or apply microfinance from an Islamic pawnbroker (*Ar-Rahn*). Nevertheless, wealth should be kept or invested in products and services provided by Islamic financial institutions.

According to the Islamic teachings, any Muslim who is also a halal SME operator is obliged to pay *Zakat* according to the wealth obtained. *Zakat* is very important in the economic development process of the Muslim community (*ummah*). According to Shofian and Amir Husin (2002), the wisdom of *zakat* or alms can be categorised into two main aspects which are social and economic. From the social view, *Zakat* can purify the soul of the owner from being arrogant, stingy and individualistic. Nevertheless, the concept of *Zakat* is able to grow and build close relationship within the community and produces individuals who are gracious and generous. *Zakat* also plays an important role in the community as agents of social security. Economically; the *zakat* can increase the purchasing power of the society. *Zakat* is the only form of welfare that is pure that the owner offers sincerely without expecting anything in return other than the consideration of the God Almighty (Shofian and Amir Husin, 2002). This form of sincerity produces healthy activity in the economy as there is no oppression, fraud, usury, and monopoly. In addition, *zakat* is a mean of social security and it is not meant to gather properties but to redistribute the wealth in immediate assistance to those who are eligible and in need.

Ajzen and Fishbein (1980), Amin et al. (2011), and Jaffar and Musa (2013) suggested that the attitude towards the behaviour refers to the favourable or unfavourable evaluations of the behaviour of an individual and they stated that attitude is positively related with the intention to make use of Islamic personal financings and the attitude is measured using five determinants of attitude which are; awareness and knowledge, religion obligation, cost benefits, business support, and reputation. These attitudes may influence the intention behavioural of entrepreneurs to adopt Islamic methods of finance in business.

## DATA AND METHODOLOGY

The primary data for this study were obtained from survey questionnaires that were distributed to 200 halal SME operators in Peninsular Malaysia using random sampling technique. Social Package of Social Science (SPSS) software was used to analyse the relationship between knowledge of Islamic finance and application of Islamic financial planning among the halal SME operators.

Reliability means ability to measure consistency of an instrument. According to McMillan and Schumacher (2006), the reliability level of a certain research tool can be projected by using five methods; namely deciding stability, equivalence, stability and equivalence, internal consistency, and agreement.

Almost all previous researchers tested the reliability of data based on the value coefficient of Cronbach's alpha to valid the data (McMillan and Schumacher, 2006). According to Cates, W.M. (1990), the validation process that the data should achieve is more than 0.85 ( $\alpha > 0.85$ ). However, this value sometimes is very difficult to obtain for this particular study, therefore, a coefficient with  $r$  value more than 0.60 is acceptable (Cates W.M., 1990). On the other hand, coefficient value between 0.6–0.8 can be considered as acceptable. Table 2 shown below is the scales used in this study with their reliability analysis.

Table 2 : Reliability Analysis of Scales

Scale	Number of Item	Cronbach's alpha
Knowledge	35	0.68
Application	22	0.83

To enable the analysis of parameters that have been carried out, statistical data must be in normal distribution (Bhasah, 2007). In this study, Kolmogorov-Smirnov test and Plot Normal Q-Q were used to determine the normal distribution of data obtained. According to Gravetter and Wallnau (2000) and Bhasah (2007), certain data were considered scatter by normal if its distribution were not significant and the Kolmogorov-Smirnov test showed value that exceeded 0.05. This study achieved the acceptable value that exceeded 0.05 as the normal distribution as shown in Table 3.

Table 3 : Test of Normality

Variable	Kolmogorov-Smirnov <sup>a</sup>		
	Statistic	df	Sig.
Knowledge	.051	200	.200*
Application	.062	200	.061

\* This value is a lower bound of true significant.

<sup>a</sup> Lilliefors Significance Correction

Furthermore, measurement scale intervals from the lowest (0.00) to the highest (1.00) (Majid, 2000) were used in this study. Pearson coefficient was used to seek relationship between two variables. The function of Pearson coefficient measurement is to determine the type and strength of mutual relationship between variables ('Knowledge' and 'Application'). A positive Pearson coefficient value determines direct correlation between two variables studied, while, negative value determines an inverse relationship between the variables (Majid, 2000). The strength of relationship between two variables was determined using Majid (2000) as shown in Table 4.

Table 4: Strength of Relationship According to Correlation Value

Correlation Index Value	Interpretation
0.00–0.20	Very weak
0.21–0.40	Weak
0.41–0.70	Medium
0.71–0.90	Strong
0.91–1.00	Very strong

Table 5: Correlations Between The Knowledge of Islamic Finance and Application of Islamic Financial Planning Among Halal SME Muslim Operators

	Knowledge	Application
Knowledge Pearson Correlation	1	.436**
Application Pearson Correlation	.436**	1

\*\*Correlation is significant at the 0.01 level (2-tailed).

The Pearson correlation ( $r$ ) and significant value ( $p$ ) for this study are shown in Table 5.

H1: The knowledge of Islamic finance has significant and positive relationship with application of Islamic financial planning among halal SME Muslim operators.

The statistical findings showed that the proposed hypothesis is supported. The knowledge of Islamic finance showed positive correlation and significantly correlated at medium level with the application of Islamic financial planning among halal SME operators ( $r = 0.436, p = .000$ ).



## **CONCLUSION**

The knowledge of Islamic finance is important to SME operators in order to implement the Islamic financial planning process. However, not all halal SME operators apply Islamic financial planning in their business managements. This leads the implementation of this study in giving general exposure to SME operators about the importance of the knowledge in halal food production industry. The policy makers such as government agencies, JAKIM, and HDC should give more exposures to SME operators in the form of training or courses about Islamic finance or Islamic financial planning because of the integration between the knowledge of Islamic finance and application of Islamic financial planning is strongly and positively correlated. This study also suggests that the Malaysian government should conduct a number of workshop and training to integrate the halal food production concept with Islamic finance knowledge to enhance the understanding about the holistic view of halal certification concept among the SME operators. This study also recommends that the Islamic financial planning should be practiced by everybody especially Muslim businessmen. Thus, policy makers such as the Ministry of Education and other authorities such as HDC and JAKIM should enhance their roles in promoting the awareness and knowledge among halal SME operators in order to fully integrate the Islamic finance system with halal products and service industry.

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