WIEF-UiTM OCCASIONAL PAPERS

DECEMBER 2012

WIEF
WORLD ISLAMIC ECONOMIC FORUM
FOUNDATION

UNIVERSITI TEKNOLOGI MARA

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FOREWORD

The fields and the practice of Islamic financial services, business and economics have developed tremendously over the years. With the emergent convergence of business activities that recognise Halal economy, the need for Islamic financial models and practices have become imperative.

This has been further underscored by the establishment of the Organisation of Islamic Cooperation (OIC) that advocates global implementation of Islamic financial models. OIC provides important access and platforms for practical application and implementation of programs aimed at increasing business, economic and financial cooperation among member countries. OIC countries have become an integral component of the world's economy and these countries' collaboration and synergies could promote sustainable models that will bring improvements to the livelihood and socio-economic status of the Muslims in particular, and the world community at large.

The World Islamic Economic Forum (WIEF) Foundation and Universiti Teknologi MARA (UiTM) are proud to present and publish this first edition of the Occasional Papers series. The publication of this Occasional Papers series compiles academic papers in a wide spectrum of topics from Islamic Finance, Agricultural Micro-Insurance, Exchange Rates, Islamic Studies, Tourism, Business Economics, Women Entrepreneurship to Informal Labour – just to name a few. The series will serve not only to reassess past practices and performances, but to also explore possible directions to follow in the future, at both theoretical and policy levels.

This document is yet another collaborative initiative between WIEF Foundation and UiTM. Earlier, both organisations have collaborated in the coordination of WIEF-UiTM Global Discourse Series under the WIEF Education Trust (WET). The publication of the Occasional Papers complements our earlier initiatives to serve as an important reference literature.

I would like to record my appreciation to all who have put in tremendous efforts in ensuring the successful publication of this first edition.

Tan Sri Dato' Dr Wan Mohd Zahid Mohd Noordin
Chairman, Universiti Teknologi Mara
Chairman, WIEF Education Trust

ABOUT THE WORLD ISLAMIC ECONOMIC FORUM (WIEF) FOUNDATION

The World Islamic Economic Forum (WIEF) Foundation, a not-for-profit organisation based in Kuala Lumpur, organises the annual World Islamic Economic Forum, a world-class business platform showcasing business opportunities in the Muslim world. The Foundation also runs programmes under the WIEF Businesswomen Network (WBN), WIEF Young Leaders Network (WYN), the WIEF Education Trust (WET), and the WIEF Roundtable Series, aimed at strengthening people partnership and knowledge exchange between Muslim and non-Muslim communities across the globe. Some of the Foundation's initiatives include the roundtable discussion series, leadership programmes, knowledge transfer and skill development workshops, business networking forums, internship and scholarship programmes, the Young Fellows Programme and the Marketplace of Creative Arts festivals.

ABOUT THE WIEF EDUCATION TRUST (WET)

The WIEF Education Trust (WET) was established in 2006 on the premise that education is the most important pillar in every society and that the fate and future of a community lies in the availability, access and quality of education for its people. The WET is aimed at garnering support and resources from the Muslim world to provide education opportunities to the people at large. To assist the implementation of the WET initiatives, the WIEF-UiTM International Centre was established in collaboration with the Universiti Technology MARA.

ABOUT THE WIEF-UITM INTERNATIONAL CENTRE

The WIEF-UiTM International Centre was set up in 2007 during the 3rd WIEF to undertake the vocational training and capacity building programmes, in tandem with the objectives of WIEF Education Trust. Its flagship event, the WIEF-UiTM Global Discourse, seeks to bring together distinguished scholars, business leaders, industry practitioners and academia to discuss and lecture on current and critical global economic, business and technological issues, with the ultimate aims of enhancing understanding and building bridges between various factions of the global community.

The Centre has also mooted several new initiatives for the students of UiTM, in particular, the WIEF-UiTM Young Leaders Series, WIEF-UiTM Entrepreneurial Talk Series, WIEF-UiTM Young Entrepreneurship Workshop, Women as Global Entrepreneurs Workshop (WAGE), WIEF-UiTM CEO Talk Series, WIEF-UiTM Career Awareness Series as well as WIEF-UiTM CSR Programs. As part of the on-going efforts in strengthening linkages between UiTM and the industry, the WIEF-UiTM International Centre also initiated programs on Leadership Development and Team Building, as well as Industry Visits for our students.

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SOCIO-HISTORICAL CONTEXT AND BUSINESS IMPLICATIONS OF A FEW ECONOMIC GUIDELINES OF THE QUR'AN

ABSTRACT

The Holy Qur'an contains guidelines and injunctions for a just administration of economic affairs in personal and social spheres of life. This paper focuses on four economic guidelines, which have direct or indirect implications for the management of business enterprises. The selected guidelines are: (1) do not indulge in usury *(riba')*, (2) do not drink intoxicants, (3) do not commit corruptions in trade and (4) do leave trade for Friday Prayer.

The description of socio-historical context of these guidelines precedes the examination of how they can have, at least theoretically, a significant bearing upon the business conduct of a Muslim. System view of an organisation and the concept of business processes are employed to systematise the examination. Each economic guideline is treated as symbolising a particular category of guidelines and its possible influence is identified in reference to three business processes; exception is the last guideline, which does not fit the process framework. Hence, its influence is located directly in relation to the business owner. The implications of the guidelines pervade the whole gamut of the business processes once a Muslim owner takes his business to be truly instrumental to secure his true self-interest which transcends the fleeting benefits of this material world.

KEYWORDS

Shariah business conduct, Usury, Intoxicant, Corruption, Jumu'ah prayer

INTRODUCTION

In an Islamic vision of life, economy occupies a significant position. Islam takes economic wellbeing to be an important instrumental goal of human life. One way to recognise the importance Islam attaches to economic aspect of life is to consider Qur'anic concern for the preservation of wealth. In fact, the literature on 'higher objectives and intents of Islamic Law' (Maqasid al-Shariah) identifies preservation of wealth as one of the five key purposes of the Law. Imam Al-Ghazali, for example, finds evidences of the purpose of preserving people's wealth in the prohibition against taking others' possessions, the command to offer a guarantee, and amputation of the thief's hand (al-Raysuni, 2006, p.19). Imam al-Shatibi's (d.1388) theory of higher objectives of the Law also substantiates this. For him, preservation of material wealth is ensured in the Qur'an by means of prohibition against injustice, depriving of orphans of their property, wastefulness, envy, giving short measure and weight, and corruption in the land (al-Raysuni, 2006, p.138).

Since economic wellbeing is a key instrument to serve the ultimate purpose of life, naturally the Qur'an contains many guidelines and instructions for proper economic administration at various levels ranging from individual to governmental, regional to global. One can easily appreciate the pervasiveness of such principles and instructions by only skimming through the indexes of a text like Khan's (1995) *Economic Message of the Qur'an*. The purpose of the paper, however, is not to reproduce the list of Islamic principles and prohibitions concerning the preservation of wealth or economic administration; rather the paper focuses on few economic instructions to achieve two-fold purposes. Firstly, to describe the socio-historical context of a few selected Qur'anic instructions, which carry with them either direct or indirect implications for the regulation of economic activities; and secondly, to examine how these instructions can influence the business operations of a Muslim.

ECONOMIC GUIDELINES

Prohibition on Usury

According to recorded history, the practice of usury and its intense criticism on moral, ethical, religious and legal grounds have coexisted in various parts of the world for at least four thousand years (Visser and McIntosh, 1998). That Arabia was not an exception to this fact is reflected in the deformed and crooked mentality of usurious mercantile people of Arabia. The holy Qur'an records their attitude: "They say: "Trade is like usury" (al-Baqarah 2:275). The verses of Surah al-Baqarah which declare usury unlawful and command Believers to relinquish their claim to outstanding usury or otherwise put their lives and possessions at stake are as follows.

> [Declaring usury unlawful:] "Those who devour usury will not stand except as stands one whom the evil one by his touch hath driven to madness. That is because they say: "Trade is like usury," but Allah hath permitted trade and forbidden usury" (al-Baqarah 2:275). [*Ordering to forgo accrued but unrealised interests*:] "o ye who believe! Fear Allah, and give up what remains of your demand for usury, if you are indeed believers" (al-Baqarah 2:278). [*Enforcing the order by utmost force*:] "If you do it not, take notice of war, from Allah and His Messenger: but if you turn back, you shall have capital sums; deal not unjustly, and ye shall not be dealt with unjustly" (al-Baqarah 2:279).

Two points deemed worthy of consideration to see the Qur'anic prohibition on usury in its socio-historical context. In the Qur'an, the injunction against usury or interest (riba') – any excess on the capital, i.e., on loan either for consumption or for trade – follows an elabourate account on charity (al-Baqarah 2:261-273) which is markedly contrasted with usury. The second point is that usury, unlike wine which had been banned during the initial years of Medina period, had been declared unlawful almost at the end of the Prophetic mission. Consideration of these points requires reviewing certain events which spread over a period from the *Hijrah* of the Prophet to the conquest of Mecca.

Continuous hostility of Meccan disbelievers towards the Believers had made their co-existence extremely vulnerable, if not impossible. By the thirteenth year of the Prophetic mission, Medina had emerged as a land supportive of this mission. The Prophet and his Companions had left Mecca for Medina. Now, in Medina there were two groups of Companions: Muhajirin, emigrants from Mecca and Ansar, helpers of the Prophet from Medina. As long as the Muhajirin were in Mecca, notwithstanding their Faith and brotherly feelings for each other, "the clan remained the basic social link.

Now with the move to Medina a new form of social organisation was required (Kennedy, 1986, p.34)." Moreover, the Muhajirin "had no means to sustain themselves" since they had left their possessions behind in Mecca (Choudhury, 1993, p.65). The Prophet worked out his plan to address these pressing socioeconomic needs. He took initiative to establish brotherhood between the Muhajirin and the Ansar which was unprecedented in the history of humanity. Ibn Ishaq (1964, p.78) reports, "Soon after the arrival in Medina, the apostle of Allah established 'brotherhood in Allah' between the companions of the Emigrants and the Helpers, saying, 'Become brothers in Allah! Two by two!'" Thus, a new society came into being the basic foundation of which was the Qur'anic principle: "The Believers are but a single Brotherhood" (al-Hujurat 49:10).

The essential requirement for the formation of such a society of unmatched brotherhood, its maintenance and its thriving was an exemplary sharing and sacrificing of economic resources for fellow brothers in need. This requirement brings us to the issue of charity, since meeting others' needs by sharing and

sacrificing own resources is a mere imagination if the people in view lack a strong impetus to charity, which can propel them to be dedicated to the cause of others. Deeply influenced and encouraged by the Qur'anic invitations to charity, the Companions, particularly those who were comparatively well-off, did their utmost to make the small society of the Believers grow "from strength to strength until they [the Muhajirin] were able to stand on their own resources and greatly to augment the resources of their hosts [the Ansar] as well" (Ali, 1992, p.1472).

The relevance of the issue of charity to the discussion on usury prohibition becomes evident when charity and usury are found to be diametrically opposite to each other. While charity implies unselfish giving of one's self or one's goods towards the fulfilment of others' needs, usury is characterised by the selfish grasping greed against those in need or distress. While charity breeds brotherhood, usury – being the opposite of charity – ruins brotherhood. This is why the Islamic prohibition on usury is considered to be the negative formulation of brotherhood (Orman, personal communication, 2007),[1] and charity the positive formulation. Now, the pertinent question is: When the Prophet worked out the plan to establish brotherhood between the Muhajirin and the Ansar in his early days in Medina, why had not usury, which stands out against the spirit of brotherhood, been forbidden until as late as 8th A.H.?

In the advent of the Prophet in Medina, two of its main Arab tribes, the Aws and the Khazraj, from whence arose the Helpers of the Prophet, eked out their living primarily from agriculture in their oasis. In addition to these two main groups, there were three small tribes of Jews or Judaised Arabs, the Banu Qurayza, the Banu al-Nadir and the Banu Qaynuqa" (Kennedy, 1986, p.33) Trade was dominated by these Jewish tribes (Kallek, 1995, p.2). "The Banu Qaynuqa, the silversmith," for example, "controlled much of the commerce of the town" (Kennedy, 1986, p.36) In early years in Medina, the community of the Believers – the Muhajirin and the Ansar– as opposed to the collective body of the pagan Arabs, the Hypocrites and the Jews was small and its presence was not commanding in its immediate vicinity. The economy of this community – the Muhajirin being striving hard to obtain means of subsistence and the Ansar being eking out their living mostly from agriculture – was, in all likelihood, hardly any more than a subsistence economy. Having such a socio-political and economic state, the Muslim community of Medina could not afford to dictate the financial rules of game in the market where usurious transactions were a commonplace.

It is important to note that Islamic injunction concerning usury was not just to inhibit future usurious deals; it had to invalidate retrospectively the claims on accrued but unrealised interests. Moreover, this injunction, if not voluntarily complied with, was to be enforced by legitimate force. In consideration of all these, before the enactment of the regulation against usury, it was necessary for the Muslim community to stand out as an authoritative socio-political entity which

1. Sabri Orman is now the Rector of Istanbul Commerce University, Istanbul, Turkey.

could inspire a sense of respect and loyalty among all disbelieving folks and tribes who were in contact, at least economically, with Muslims and to achieve a sizeable economy which could stipulate the course and terms of trade of its own preference. For the fulfilment of these necessary conditions, the Muslim community had to wait until the conquest of Mecca which was closely followed by another equally important and decisive victory over the Hawazin at the battle of Hunayn (Ibn Ishaq, 1964, p.156; Kennedy, p.43-45).

Usury was now banned. No sooner had usury been declared unlawful, Muslims stopped usurious transactions on their part. However, dispute arose. Banu Makhzum and Banu Thaqif were involved in usurious deals. The former, after their conversion to Islam, declined to pay outstanding interests claimed by Banu Thaqif, who were still disbelievers. This happened in Mecca. The then Governor of Mecca wrote to the Prophet for necessary guidance. In this background, Qur'anic instruction was sent down which demanded interests, accrued from previous usurious deals, to be relinquished; otherwise, the Qur'an posed a formidable threat of war against those who showed unwillingness to comply with the order. In worldly calculation, writing-off outstanding interests was a great loss to disbelievers. For the sake of equity, relinquishing claims on interests could not be one sided. In the Pilgrim of valediction, the Prophet, on behalf of the Muslim Community, relinquished interest claims of Muslims on non-Muslims first; then, on the ground of equitable treatment, he asked non-Muslims to give up their similar claims on Muslims.

Gradual Prohibition on Intoxicants

Drinking wine was a mundane affair in everyday life of Muslims in Mecca, even in Medina for sometime after the migration of the Prophet. The prohibition of wine (khamr) came in a series of steps. If sakar is taken in the sense of fermented wine, the first step was then implicitly stated in verse 67 of Surah al-Nahl revealed in Mecca. "And from the fruits of date palm and grapes, you derive strong drink [sakar] and a goodly provision. Verily, therein is indeed a sign for people who have wisdom" (al-Nahl 16:67). In this verse, sakar is contrasted with a goodly provision (rizqan hasana). Thus, the verse "would imply a subtle disapproval of the use of intoxicants and mark the first of a series of steps that in time culminated in total prohibition" (Ali, 1992, p.654) Based on the exegesis of Qur'an by Muhammad Shafee (1413 A.H.), we describe here three successive events concerning the prohibition of wine.

Although drinking wine was not forbidden since the inception of Islam and it was a routine act in the society, the Prophet and some of his Companions had never ever touched wine. In Medina, a few of such Companions felt the injurious aspects of drinking and they, including Umar Ibn Al-Khattab and Muadh Ibn Jabal, went to the Prophet and beseeched: "Wine and gambling fog human mind and damage properties. What is your command about this?" The following verse of the Qur'an was revealed in response to this question. "They ask thee concerning wine and gambling. Say: "In them is great sin, and some profit, for men; but the sin is greater than the profit" (al-Baqarah 2:219).

The verse did not clearly put restriction on drinking wine, but succinctly and forcefully highlighted its harms. Thus, the verse implied an advice against drinking. Some of the Companions shun drinking by virtue of this advice, although the tradition of drinking in the community of Believers continued since the permissibility of it was not nullified.

One day, a Companion of the Prophet invited some of his friends from among the Companions. Drinking session, as usual, followed with the meal. It was by then the time for Maghrib Prayer and they stood for it. While leading the Prayer with a mind befogged, the imam repeatedly made mistakes in reciting Surah Al Kafiroon. This event was followed by the third step in the process of prohibiting wine. "O ye who believe! Approach not prayers with a mind befogged, until ye can understand all that you say" (al-Nisa'4:43).

This verse put indirect restriction on wine consumption through disallowing those who are in a state of intoxication to come for prayer – an obligation that the people under consideration cannot dispense with. At this stage, therefore, they were left with two choices: either to shun drinking wine totally or, at the least, to confine drinking to a limited time of the day. Many Companions chose the former option and the rest the latter.

There was yet another event to occur for the process of prohibition to complete. This was again a case in which some of the Companions were attending an invitation by a Companion. Drinking competition began after the meal. In social drinking, it was the tradition among Arabs to compete in reciting poetry and eulogise own tribe and predecessors with arrogance and vanity. Following the tradition, a Muhajir Companion recited a poem which extolled his own people and disparaged people of the Ansar. As a result, an Ansar youth became angry and had the Companion's head severely wounded by throwing a camel's jaw bone. The Companion complained to the Prophet against the youth. The Prophet invoked Allah: "O Allah! Ordain for us a clear ordinance as to wine." The following verses were then revealed as a response to this invocation.

> "O ye who believe! Intoxicants and gambling, (dedication of) stones, and (divination by) arrows, are an abomination - of Satan's handiwork; eschew such (abomination), that ye may prosper. Satan's plan is (but) to excite enmity and hatred between you, with intoxicants and gambling, and hinder you from the remembrance of Allah, and from prayer: will you not then abstain?" (al-Ma'idah 5:90-91)

Wine became categorically unlawful in Islam. The decree as to the unlawfulness of drinking wine was officially announced. Companions, who were in the state of drinking, threw their wine the moment they heard the announcement. Moreover, they spill their individual storage of wine kept at home. As to the commercial storage of wine at the market, all were brought together at a certain place upon order and their containers were broken. The case of a Companion,

who was a wine trader, is noteworthy. He was in Syria to import wine when drinking wine was declared unlawful. Before entering Medina, he came to know about the declaration. Leaving his costly merchandise at a place outside the city, he met the Prophet to know what he should do with it. The Prophet ordered to spill it by breaking the containers. The Companion did so without any objection. His merchandise, which would otherwise have generated a handsome profit, was thus sacrificed for a permanent and superior gain in the life after. A better deal indeed!

It should be noted that the injunction initially and directly address consumption of wine; by implication, however, all activities that make such consumption possible are also forbidden. In fact, the Prophet has cursed ten categories of people who are involved in wine production, distribution, consumption, or sharing its financial gains (Sunan al-Tirmidhi). Moreover, the prohibition applies not only to wine (khamr), which is literally understood to mean the fermented juice of the grape. By analogy all fermented liquor, and by further analogy any intoxicating liquor or drug, come under this prohibition.

Warnings against Corruption in Trade

- **Corruption of Madyan Trading Community**

Being a great-grandson of Madyan (a son of Abraham), the prophet Shuaib was in the fourth generation from Abraham (Ali, 1992, p.368). Accordingly, he had come earlier than Moses. He was sent to Midianites – the people of Madyan – who were a commercial people and trafficked from land to land (Ali, 1992, p.995). The Midianites were perhaps "in the path of a commercial highway of Asia, viz., that between two such opulent and highly organised nations as Egypt and the Mesopotamian group comprising Assyria and Babylonia" (Ali, 1992, p.369). "The Midianites, when the prophet Shuaib was sent, fraud and immorality had corrupted their commercial conduct". Their trades were seriously infested by vices like giving short measures and weight, general deceptions that violate the rights of others, and jealousy of other people's prosperity. He urged them to be righteous in their commercial dealings.

> "To the Madyan people (We sent) Shuaib, one of their own brethren: he said: "O my people! Worship Allah: ye have no other god but him. And give not short measure or weight: I see you in prosperity, but I fear for you the Penalty of a Day that will compass (you) all round. And O my people! Give just measure and weight, nor withhold from the people the things that are their due, commit not evil in the land with intent to do mischief. That which is left you by Allah is best for you, if ye (but) believed! But I am not set over you to keep watch!" (Hud 11:84-86)

His repeated sympathetic and prudent advices were responded in unpleasant and arrogant manners. They slandered him and challenged him to bring them immediate punishment if he was truthful (al-Shu'araa 26:185-187). They also

made mockery out of his advices (Hud 11:87) and showed superiority and arrogance (Hud 11:91). They threatened either to expel him and his followers from the city or to bring them back to their (corrupted folks) own ways and religion (al-A'raaf 7:88); otherwise, the threat extended to say, the only thing before them is none but ruin (al-A'raaf 7:90). When prophet Shuaib's gentle and persuasive advices and arguments went abortive and the Midianites proved themselves persistent in their wrongdoing, the Divine punishment became inevitable.

> "When Our decree issued, We saved Shuaib and those who believed with him, by (special) Mercy from Ourselves: but the (mighty) Blast did seize the wrongdoers, and they lay prostrate in their homes by the morning – as if they had never dwelt and flourished there! Ah! Behold! How the Madyan were removed (from sight) as were removed the Thamud!" (Hud 11:94-95)

- **Corruption of Saba' Trading Community**

Saba' was a city and territory in Yemen, approximately 50 miles away from the city of Sana'a. During the time of the prophet Sulayman and Queen Bilqis, it achieved prosperity and high degree of civilisation by means of the famous dam of Ma'rib (Ali, 1992, p.943) This is referred to in the Qur'an. The Hoopoe (al-Hudhud) reported to Sulayman: "I have come to thee from Saba' with tidings true. I found (there) a women ruling over them and provided with every requisite" (al-Naml 27:22-23). Some centuries after Solomon, Saba' "was still a happy and prosperous country, amply irrigated from the Ma'rib dam. … It produced fruit, spices, and frankincense, and got the name of Araby the Blest for that part of the country" (Ali, 1992, p.1088) The prosperous civilisation of Saba', however, was torn into pieces by a mighty flood and thus thrown into oblivion. The destruction occurred only after the people of Saba' had become arrogant of their prosperity and perversion of faith in Allah had taken place (Saba' 34:16-17).

Corruption in commercial conducts of Saba' people was one of the reasons for the destruction. The holy Qur'an alludes to the perversion of monopoly in the following verses.

> "Between them and the Cities on which We had poured Our blessings, We had placed Cities in prominent positions, and between them we had appointed stages of journey in due proportion: "Travel therein, secure, by night and by day." But they said: "Our Lord! Place longer distances between our journey-stages." But they wronged themselves (therein). At length We made them as a tale (that is told)." (Saba 34:18-19)

Yusuf Ali (1992, p.1089) explains that the Yemen-Syria road was a much frequented route. It was studded in the days of its prosperity with many stations (cities) close to each other, on which merchants could travel with ease and safety, "by night and by day." The close proximity of stations prevented the inroads of highwaymen. The covetous people of Saba', however, attempted to reduce drastically the number of way-stations. They did so in order to get more profit

from travellers supply by concentrating them on a few stations which they could monopolise. Their attempt boomeranged on them, as it tended to choke off traffic and ruin the big trade.

Two above accounts of Madyan and Saba', in terms of both geography and chronology, are evidently distant. Nonetheless, they carry a common factor: corruptions in trade, which pulled them together for the current purpose. In case of Madyan people, deception in a broader sense signifies their corruption; for Saba' people, monopoly symbolises their corruption. No doubt, both of them were envious of the prosperity of other people and causing anarchy and disorder on the earth. In other words, their commercial conduct was in opposition to a general principle of no harm. They remained heedless of the prophetic advices and wise ordinances of true Faith and did not mend their conduct to be righteous in their commercial dealings in particular. Consequently, they made themselves deserving of Divine Wrath and were utterly ruined.

Temporary Cessation of Business

English lexicon places Christian Sunday, Jewish Saturday and Muslim Friday under the same rubric of the Sabbath day. This day, according to the lexicon, is the day for rest and worship for some religious groups (Cambridge Advanced Learner's Dictionary). Equating Friday of Muslims with other two days on the alleged common ground of 'day for rest and worship' is problematic, because "the idea behind the Muslim weekly "Day of Assembly" is different from that behind the Jewish Sabbath (Saturday) or Christian Sunday" (Ali, 1992, p.1469) Despite the profound differences, Muslim Friday and Jewish Saturday show a significant similarity to each other when they are seen from the perspective under consideration. Worldly activities, especially economic activities, were forbidden for Jews on the whole Saturday. Prohibition, which is similar in nature but lesser in intensity in terms of the period of suspension of work of worldly interests, came to influence the community of Muslims almost since the inception of the foundation of Islamic Medina by the Prophet (pbuh).

> "O ye who believe! When the call is proclaimed to Prayer on Friday (the day of Assembly), hasten earnestly to the Remembrance of Allah, and leave off business (and traffic): that is best for you if ye but knew. And when the Prayer is finished, then may ye disperse through the land, and seek of the Bounty of Allah: and celebrate the Praises of Allah often (and without stint): that ye may prosper. But when they see some bargain or some amusement, they disperse headlong to it, and leave thee standing. Say: "The (blessing) from the Presence of Allah is better than any amusement or bargain! And Allah is the best to provide (for all needs)" (al- Jumu'ah 62:9-11).

The above verses revealed against the background of a particular incident on Jumu'ah day in Medina. As Muhammad Shafee (1413 A.H.) explains, People of Medina were facing scarcity of daily necessities. A commercial caravan, which used to carry all daily necessities, arrived at the market of Medina at a time when the Prophet was delivering the sermon of Jumu'ah Prayer. It should be noted that up to that time the tradition was to deliver the sermon after the Prayer, as followed for mid Prayers until today. Anyway, the beating of drum well circulated the arrival news of the caravan, and people, anxious that they would not get anything if late, immediately dashed for the caravan. The lion share of the Musalleen (the performers of prayers) attending the Jumu'ah sermon left the mosque – not knowing the sermon is an essential part of Jumu'ah Prayer and being propelled by the dare necessity of getting some goods of daily usages – for the caravan too. Allah disapproved this conduct and prohibited business deals for a specified period on Friday. The Believers are asked to leave off business when call for Jumu'ah Prayer is proclaimed and they are permitted to resume it only when the Prayer is finished.

Lessons pertaining to spiritual training for due compliance with the regulation of temporary suspension of business activities are noticeable in the verses. Believers are after all human beings. Lest worldly interests deflect their human minds from solemn observance of Friday Prayer and tempt them to violate the regulation, each of the three verses ends up with the fact of immense spiritual significance. Allah asks Believers to leave off business and hasten earnestly for His Remembrance and tells them, "That is best for you if ye but knew" (verse 9). They should know that "the immediate and temporal worldly gain may be the ultimate and spiritual loss, and *vice versa*" (Ali, 1992, p.1469). The next verse allows them to resume worldly work and says, "celebrate the Praises of Allah often (and without stint): that you may prosper." The lesson is that "prosperity is not to be measured by wealth or worldly gains. There is a higher prosperity – the health of the mind and the spirit" (Ali, 1992, p.1469). The last verse (11) disapproves the conduct of leaving the Prayer, fully or partially, to attend to the matter of worldly interests, and reminds, "The (blessing) from the Presence of Allah [that which Allah has] is better than any amusement or bargain! And Allah is the Best to provide (for all needs)." This is to caution Believers that "do not be distracted by the craze for amusement or gain. If you lead a righteous and sober life, Allah will provide for you in all senses, better than any provision you can possibly think of" (Ali, 1992, p.1469).

BUSINESS IMPLICATIONS

The previous section describes socio-historical context of four guidelines, which can take a simplified expression as follows: do not eat *riba'* (i.e., prohibition on usury), do not drink intoxicants (i.e., gradual prohibition on intoxicants), do not violate rights of others (warnings against corruptions in trade), and do leave trade for *Jumu'ah* Prayer (temporary cessation of business). For examining the

influence of these guidelines on the business operation of a Muslim, we take each of them to be representative of a broader category of guidelines for fair conduct of business dealings as shown in the Table 1 below.

Table 1: A specific guideline symbolising a broader category instruction

Specific Guideline	Broader Category of Guidelines
Prohibition on usury	Acquisition and use of lawful financial resources
Prohibition on intoxicants	Avoiding business of unlawful and objectionable products or services
Warnings against corruptions in trade	Not harming or hurting people connected – directly or indirectly – to one's business
Temporary cessation of business	Readiness to leave or sacrifice material possessions for the cause of Allah

Keeping this categorisation in mind, we can now proceed to exhibit the major influences of these guidelines on a Muslim's business by employing a simple system view of organisation, which is depicted below.

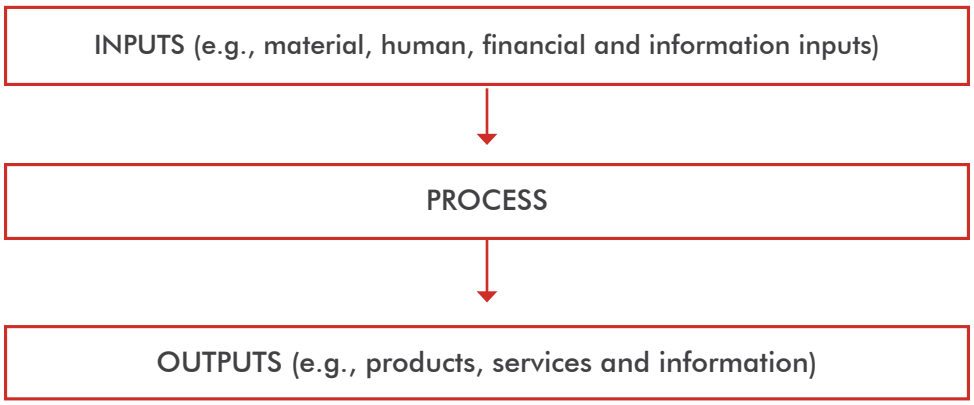

Fig. 1: Simple system view of organisation

According to the system view, organisation for its survival and growth collects various inputs from its environment, processes certain inputs by other inputs to produce what it sends back to the environment as its outputs. This view of organisation offers a frame to conceptualise business as consisting of three key processes: supply management process at the input side, demand management process at the output side and value adding conversion process that links the supply to the demand. Now we can attempt to locate the influence of the economic guidelines in reference to these business processes.

Table 2: Examples of the areas of influence of economic guidelines in reference to business processes

	PROCESSES		
ECONOMIC INSTRUCTIONS	Supply management process	Value adding conversion process	Demand management process
Prohibition on usury	Financial inputs		Financial investment
Prohibition on intoxicants	Material inputs	Production of goods and services	Sale of goods and services
Warnings against corruptions in trade	Rights of suppliers	Rights of employees	Rights of customers

A business owner needs money to start his business. Money as a financial input is subject to the prohibition of usury. Note that this prohibition, taken as symbolising the category of *financial guidelines*, demands a business to start with lawful capital, and acquire and use lawful financial resources in its course of operation. For a Muslim business owner, therefore, the very first condition is lawfulness of his money or capital. If he fails to meet this condition, his business also will fail to serve his true self-interest in the Hereafter irrespective of the fairness in other aspects of his business.

After capital, the second issue of importance is what the business in question is. To put it differently, the essential question is what are the goods or services that the owner deals in? Prohibition on intoxicants is relevant here since we take it as a symbol of the category of guidelines concerning legally objectionable products or services. In accordance with this instruction, business goods or services in question must be lawful. This means that, as shown in the above table, materials to be collected and products to be produced and sold must be an issue of serious deliberation for a Muslim business owner. He cannot engage himself just in any business. He must refrain from the business of forbidden goods and services. His failure in this regard will make his business merely a worldly game even if he starts his business with lawful capital. In other words, because of the wrong use of right capital, the power of pure money will cease to yield him true benefit.

The third instruction, as shown in the table, is warning against corruptions in trade. We take it as a symbol of the category of guidelines as regards the maintenance of the rights of people who are connected with one's business - directly and indirectly. The table shows only three categories of people who are directly connected: suppliers (providers of inputs), employees (carriers of conversion process) and customers (buyers of outputs). The warning implies that the business of lawful products or services with lawful money must be conducted by maintaining the legitimate rights of people – customers, suppliers and employees at the least. Indeed, the Holy Qur'an asks the Believers to conduct their business on mutual goodwill or mutual consent *(taradin minkum)*. "O ye who believe! Eat not up your property among yourselves in vanities; but let there be amongst you *traffic and trade by mutual good will*: nor kill (or destroy) yourselves: for verily Allah hath been to you most Merciful!" (al-Nisa' 4: 29). Short weights and measures, manipulation of market information, misrepresentation of products, taking undue advantage of the abundant supply of labour, non-compliance with safety and quality standards and externalising costs[2] are only a few examples of the violation of mutual consent in business and hence the violation of others rights. No doubt, the benefits of pure money and permissible products evaporate when a Muslim business owner violates the legitimate rights of people, i.e. he does not give what is their due.

What is missing in the above table is of crucial and ultimate importance: the guidelines as regards leaving trade for *Jumu'ah* Prayer. To reiterate, we take this instruction of temporary cessation of business to signify the demand placed on Muslims for their constant readiness to leave or sacrifice material possessions for the cause of Allah. It is necessary for a Muslim to comply with the first three categories of guidelines discussed above. It is, however, not sufficient to guarantee that his business is truly instrumental to secure his true self-interest – the eternal bliss in the life after. For this, his business-sound in terms of finance, products and maintenance of people's rights, must not hinder him in his remembrance of Allah. If it hinders, the soundness of business may generate some temporary material benefits, but it will not be able to save the owner from utter loss in the eternal life. The Qur'an warns us: "O you who believe! Let not your properties *(amwal)* or your children divert you from the remembrance of Allah. And whoever does that, then they are the losers" (al-Munafiqun 63: 9).

2. "An externality," says economist Milton Friedman, "is the effect of a transaction … on a third party who has not consented to or played any role in the carrying out of that transaction." See, Joel Bakan, The corporation: the pathological pursuit of profit and power, New York: Free Press, 2004, p.61

CONCLUSION

The four economic guidelines of the Qur'an considered above are evidently distant from each other in reference to their socio-historical context of revelation. The discussion of their business implications, however, explores a thread of their interconnectedness. This interconnectedness points to the fact that fatal flaws in the observance of one guideline make the observance of others, although sound in isolation, worthless. This fact of interconnectedness, if it becomes an object of profound reflection, can turn to be a provocative issue for a Muslim business owner. And this is the main thrust of this paper.

Another observation of these guidelines from the perspective of regulative standard is noteworthy. Guidelines concerning usury, intoxicants and corruptions in trade – each of them taken as representing a category, not just a single issue – offer scope for the formulation of standards, which are primarily legal and moral. Infringements of these types of standards can be restrained largely through socio-legal and moral sanctions. In other words, primary force to exact compliance is positional authority or legitimate human authority and relevant socio-cultural norms. On the other hand, the temporary cessation of business is an issue of spiritual standard, which in the main does not admit of legal and social measures. The primary force to exact compliance with this kind of standard is the awe of God and love for Him that induce the owner to transform his business – apparently a mundane job – into a form of the veneration of God.

A final note is in order. Qur'anic statements are words of God. Each of the statement of the Qur'an, being Divine words, contains immeasurable depth of meanings. Hence, the meanings of the Qur'anic statements considered here for the discussion of economic guidelines and their business implications cannot claim to be exhaustive and comprehensive.

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IN SEARCH OF IDENTITY: ISLAMIC FINANCE AND MUTUALITY

ABSTRACT

A hotly debated yet scarcely explored issue is the growing divergence between the aspirations of Islamic economics and the realities of the Islamic finance industry. This issue is emerging at a critical junction of Islamic finance development and is key to further enhancements of the whole industry.

Rather than being part of the Islamic political economic thought, Islamic finance has been pursuing policies away from the theoretical underpinnings of Islamic economics and has located a surrogate financial framework in neo-classical economics. Islamic finance institutions aiming at efficiency have ignored and relegated the importance of social dimension and failed to internalise social justice into their own operational function.

They are also mimicking conventional financing tools. In that predicament, Islamic finance is best described as heterogeneous financial products deprived of their value systems and is nowadays suffering from the perception that it is simply a rebranding of conventional finance and not truly reflective of Islamic principles. A new specialised institutional set up is required to promote Islamic economic values.

KEYWORDS

Islamic Finance; equity financing; riba'; waqf; microfinance

GENERAL BACKGROUND OF THE PROBLEM

Centuries-old Islamic economics provides axioms and values that propose an ethical system of economics and finance based on the twin sources of Islam: the Qur'an and the hadiths. Its foundational claims are social justice, poverty alleviation and prevention of exploitation, while at the same time emphasising needs' fulfillment, wealth redistribution and avoidance of wealth concentration. It also postulates socio-tropic individuals. Though market exchanges are its main feature, they are filtered through an Islamic process to produce a socially-concerned and environmentally-friendly system. To allocate resources, Islamic economics strongly recommends equity-based modes of financing – mostly through the *Mudarabah and* Musharakah contracts – that hinge on profit-loss-sharing (PLS), wherein reward-sharing is related to risk-taking (and not risk-shifting as it happens in conventional finance) between transacting parties. The so-called Islamic 'debt' – which needs to avoid foul play with the prohibited ribà and predetermined rate of return – becomes in reality credit obligations arising from trade contracts such as Murabahah or indebtedness arising from leasing contracts such as *Ijarah*.

A critical analysis of today's Islamic finance institutions indicates that the pragmatic approach adopted by the industry has led to a non-implementation of the values and modes of financing postulated by Islamic economics. The emerging wealth in the Muslim world and the staggering rate of growth of the Islamic finance institutions' asset-base, coupled with the weak development of the contemporary discourse of Islamic economics (due to a lack of interest and perhaps scarce intellectual resources) have forced Islamic finance to blindly adhere to the well-known precepts of a neo-classical paradigm of managing wealth. These precepts, needless to say, conflict with the axioms upon which an Islamic ethical economic system is founded. In other words, the methodological framework of Islamic finance nowadays ignores the intrinsic social-welfare emphasis of Islamic economics that requires both individual and societal well-being maximisation. One of the consequences of this neglect is Islamic financial institutions that deliberately and systematically avoid the profit-loss-sharing modes of financing and de *facto* mimicking lender-borrower relation.

A REALITY CHECK

The realities of financial markets, which prioritise economic incentives rather than religious, ethical or social or environmental behavioural norms, have forced Islamic finance to become part of the international financial system by adopting the commercial banking model, its banks' lending criteria, contractual terms and costs of financing, with the primary objective of profit maximisation and efficiency and renouncing its own value-system. In its latest development, Islamic finance represents hybrid financial products in the international financial system and it is accepted that this particular hybridisation requires religious not

secular construction. Thus, the difference with conventional finance has been reduced to a technicality (conducting financial activities according to Shariah-compliant contractual norms) in which the value system is referred to only in describing the Qur'anic prohibition of *ribà,* Gharar and maysir.

This tendency has led to a number of disturbing consequences, such as:

- The avoidance of equity financing (i.e.: *Mudarabah and* Musharakah*)* to the extent that 'debt contracts' (i.e.: *Murabahah, Bay' bi-thaman ajil and Ijarah thumma al-bay'*) represent more than 90 percent of the Islamic market. Nearly all Islamic banks, investment companies, and investment funds offer trade and project finance on mark-up, commissioned manufacturing or on leasing bases. PLS instruments have especially been marginalised in favour of Murabahah - which originally is a trade contract and used as a mode of financing only in contemporary Islamic finance - to mimic conventional fixed income instruments, allow Islamic banks to ensure that they avoid risk almost altogether in their transactions and earn predictable and relatively high returns. While developmental financing, with the objective of economic growth (agriculture, industry and manufacturing, infrastructures) necessitates long-term equity financing, the majority of Islamic banks' financial transactions are directed away from agriculture and industry and toward retail or trade financing through debt-like financial instruments which, by definition, are short-term. The avoidance of equity financing therefore casts a doubt on the industry's interest in economic development and social welfare and on the fulfillment of the aspirational stand of Islamic economics.
- Huge market distortions – Most of the transactions earmarked as Murabahah are in fact not real Islamic fixed-income instruments, but are investments in the so called 'commodity murabahah' transactions with non-Islamic banks. This practice has allowed the siphoning of Islamic funds out to the conventional market, which in turn utilises them for conventional *riba'*-based activities, thus distorting the demand and supply parameters of the Islamic fixed income market. According to Badlisyah Abdul Ghani, CEO of CIMB Islamic, there are about USD1.5 trillion worth of Islamic deposits or funds globally, but there are only about USD130 billion debt papers or Sukuk assets and USD700 billion banking assets in Islamic financial institutions, with the majority of them in the form of commodity murabahah with conventional banks. This accounts for only half of the total Islamic deposits and funds. One can rightfully ask himself where the other half is. This situation ultimately weakens the Islamic capital market and dampens its growth potential. Worse, the incident actually strengthens the conventional *riba'*-based capital market.
- Financial exclusion – The lives of common Muslim individuals have not significantly benefited from Islamic finance. This appears clearly in the SMEs and microfinance sectors. With regards to the former, it is known that Islamic banks rarely offer long-term financing to entrepreneurs seeking for capital. Paralleling personal banking, entrepreneurs excluded from conventional banking are excluded from the use of Islamic finance as well. The needs of those entrepreneurs who cannot provide collateral are not met by the Islamic

finance industry and this, once again, is in contradiction with the principles of Islamic economics. But nowhere the issue of financial exclusion has become apparent as in the microfinance sector with the notable absence of Shariah-compliant products aiming at poverty alleviation and the empowerment of micro-entrepreneurs. Microfinance products have indeed been quite successful in majority of Muslim countries with large microfinance banks operating in Indonesia, Bangladesh, Pakistan, Morocco, Egypt and India; but few of them, if any, are Shariah-compliant. Though 44 percent of conventional microfinance clients worldwide reside in Muslim countries, the overall penetration of microfinance in these countries is indeed irrelevant as conventional products do not fulfil the needs of many Muslim clients. Shariah compliance in some societies may indeed be less a religious principle than a cultural one with even the less religiously observant preferring Shariah-compliant products. A secondary objective is to enable financial inclusion of Muslims in countries where they are a minority; thus contributing, for instance, to a new definition of citizenship in Western societies.

- The constraining of social dimension within zakat*, sadaqah* and other charitable activities that have never been targeted by Islamic finance as a 'natural' area for the deployment of its contractual structures. As a result, these activities, though sizeable, have ignored systematic economic development and social justice. With regards to zakat, for example, the literature review reveals that it has failed to achieve its socio-economic objectives and that many pockets of the Muslim population contribute to the world underdevelopment, poverty and economic inequalities. The use of best-in-class asset management and Islamic finance practices in the management of zakat as well as linking its distribution to community-based development programmes should go a long way to address this particular issue.
- Leaving the enormous amount of capital embedded in the *waqf* structures dormant. Today's *waqfs* are indeed asset rich and cash poor and therefore of little help to the Ummah across the Muslim world. The permissibility, recently recognised by a number of fatwas, of selling the commercial or residential units of the *waqf* on a leasehold basis thus leaving intact the freehold property, has opened the door to a more advanced and progressive approach. For instance, leveraging on the *waqf* properties by using the creative and innovative solutions provided today by Islamic finance such as *Sukuk* al-Musharakah *or Sukuk al-Intifa'* or through the use of the Real Estate Investment Trusts (REITs) will certainly prove a milestone in fighting poverty issues.
- A credibility issue – The overuse of debt-financing transactions has exposed Islamic finance to criticism that the pricing of its products offered as Shariah-compliant parallels too closely to the pricing of conventional products and that interest appears to be disguised as a cost mark-up or administration fee. The distinction from a mere loan is indeed compelling in theory but in practice Islamic banks often employ various stratagems to reduce their risks in Murabahah to almost zero, particularly in international trade.

THE WAY FORWARD

The first best solution having failed to realise the ameliorative goals of Islam economics, Islamic finance should look to foster its values within a more specialised Islamic institutional set up, in line with the recent global developments where an array of institutional structures exist. Extensively cooperative participation, for instance, must be explicitly introduced to reflect the organisational and management processes involved in such participatory enterprises. This will provide for institutional corrective mechanisms that will ensure the second best solution yields the expected social outcome alongside commercial banking.

The brand name of Islamic finance should emphasise issues such as community banking, microfinance, socially responsible investment, and the like. To achieve this aim, a collective effort is needed to rearrange the instruments and contractual structures used by Islamic finance in light of the goals of Islamic economics. The addressing of this stalemate and the exploration of possible ways out of it, are indeed instrumental to help move Islamic finance forward and foster its damaged credibility.

Building on the scarce contemporary literature existent on this specific issues, Islamic finance should, on the one hand, have a look at classical works to find guidance and, on the other, activate an action-research process aiming to increase collaboration between financial and Shariah scholars of the four different schools of thought on product authenticity. The participation of practitioners, such as CEOs of Islamic banks, Private Equity funds and Sovereign Wealth Funds will also add credibility to the whole adjustment process.


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CURRENCY TRADING AND THE APPROPRIATE EXCHANGE RATE REGIME FOR AN ISLAMIC ECONOMY

ABSTRACT

This paper looks at the main forms of currency trading in foreign exchange (forex) and discusses whether these transactions are in line with Shariah, the Islamic law. The paper outlines fundamental principles for a Shariah compliant currency trading and argues that since the development of an Islamic forex discourages currency speculation, it will contribute positively towards providing stability in the exchange rate. Further, an increased adoption of Islamic Banking and Finance instruments including those for currency trading will contribute towards the financial market stability as the reduction and eventual elimination of interest bearing assets will reduce volatility since capital movement will no longer be sensitive to changes in global interest rates and therefore helps to prevent sudden inflows and outflows of hot money.

The research also examines some Shariah compliant alternatives of currency trading and the implications these instruments would have on the exchange rate stability. The paper highlights the experience of Malaysia during the 1998 Asian currency crisis and suggests an appropriate exchange rate regime for an Islamic economy guided by the principles of Maqasid al-Shariah.

KEYWORDS

Forex, Exchange rate, Currency trading, Malaysia

INTRODUCTION

The last two decades, particularly after the 1998 Asian Financial crisis and into the new millennium, saw tremendous growth in Islamic Banking and Finance (IBF) the world over. IBF as part of the bigger Halal industry is now recognised as the new global market force that will change the form and substance of the way business is being conducted.

While the subject on Islamic banking has been taking centre stage in Islamic finance, the issue of exchange rate policies and regimes has not attracted a lot of research. Apart from the subject of the gold dinar which became popular following the Asian crisis when the then Prime Minister of Malaysia Tun Dr Mahathir Mohamad suggested that Muslim countries adopt the gold dinar to avoid dependence on the US dollar[1], there is scant literature on what constitutes an Islamic system of exchange rate. Is there an appropriate exchange rate regime for an Islamic country? Is it fixed or floating? Or in between? Is government intervention in the foreign exchange market justified from the Islamic perspective? And what is the Islamic view on the existing forms of currency trading?

This paper looks at Foreign Exchange (forex) trading and discusses whether these are in line with Shariah principles. The paper then examines the Islamic viewpoint on what constitutes an Islamic forex and argues that the development of an Islamic forex in an economy that increasingly uses Shariah compliant banking and financial products would discourage currency speculation and would contribute positively towards an exchange rate stability.

This paper also discusses the elements of an Islamically appropriate exchange rate regime and examines the implications of an increased adoption of IBF on the exchange rate stability of an Islamic economy.

BACKGROUND TO FOREX

In the forex markets, traders of foreign currencies trade with one another in what seems to be a very efficient and perfect market. These markets help to facilitate foreign trade, raise capital for foreign markets, transfer risks between participants and speculate on currency values. Historically, trading in foreign currency was the result of international trade as buyers and sellers needed foreign currencies to settle transactions. Now currency trading has little to do with international trade, which accounts for only two percent of global currency movements (Singh 1999).

While the New York Stock Exchange averages about $16 billion in trading volume per day, and the London Stock Exchange averages around $11 billion, their combined daily dollar volume represents only a little over three percent of what the foreign exchange market averages. With a daily turnover in the area

of USD1.5 trillion, forex is the world's largest and most influential market in terms of both size and liquidity. It is an immense global market with no central exchange. As a result, forex can neither be controlled nor regulated by any one country. In addition, around 90 percent of its transactions involve the seven major currency pairs.

The last decade prior to the new millennium saw a number of currency crises. There are many theories that try to explain the phenomena. The use of fiat money and the global movement from the gold standard to a more flexible system since the 1970s had resulted in the increases of currency speculators. In previous centuries where gold and silver were more commonly used as currencies and right up to the last century where currencies were backed up by the gold standard, the value of the currency (or its purchasing power) was tied to the real activities of the economy. With the collapse of the gold standard and the rise of the floating exchange rate system where the US dollar became the vehicle currency, the values of currencies across the world are now determined less by real activities and more and more by capital flows of which a greater part of this is influenced by currency speculators and financial investors rather than traders.

MAIN FORMS OF TRADING IN FOREX

Exchange rate is defined as the price of one currency in terms of another. It can be quoted as price of foreign currency in terms of domestic currency units as in 1 USD equals RM 3.8 or as price of domestic currency in terms of foreign currency units as in RM1 equals 0.26 USD.

There are basically three groups in the foreign currency market:

1. Traders
2. Investors and
3. Speculators.

Traders are exporters and importers who use foreign currencies to facilitate transactions in international trade. A Malaysian importer would have to pay an American exporter using US dollars so he needs to change his ringgit to US dollars. Similarly exporters receive payment in foreign currencies which they need to change to ringgit for use in Malaysia or some exporters may insist that they be paid in the local currency (this depends on what currency the business is quoted in; the US dollar is still regarded as the main vehicle currency because in Malaysia alone over 80 percent of business transactions involving trade are quoted in US dollars).
Investors make either long term investments - financial dealings through the capital market through the purchase of government bonds, equities or real investment as in foreign direct investments for setting up subsidiaries and manufacturing plants; or short term investments in the money market, or in bank deposits.

Speculators on the other hand, buy and sell currencies with the objective of getting profits from the expected changes in exchange rate movements. Funds from currency speculators represent large sums of money globally and these funds used for short term financial investments subjected to fast withdrawals represent hot money, the movement of which often results in currency volatility.

In short, while traders are exporters and importers involved in trading of goods and services, investors invest in assets that are both real and financial and speculators are traders who enter the futures market in search of profit and by doing so willingly accept increased risks (Kolb 1997:96 as cited in Ahmed 2001:12). While a hedger uses forward, futures, options and swaps to reduce his exposure to risk, a speculator uses the same instrument to expose himself to risk to make profit (Salvatore 1993:398 as cited in Ahmed 2001:12).

Foreign currency is traded in the spot and forward markets. In the former, currencies are traded on the spot while in the forward markets, contracts are signed in the present time for a transaction that takes place in future. The details of future transactions such as time, price and quantity are specified in the contract. The demand and supply in these markets determine respectively the spot and forward exchange rates.

Other than forward and spot, there are futures, options and swaps. Futures are forward contracts in standardised currency traded in organised markets. Options are financial contracts of standardised amounts that give buyers (sellers) the right to buy (sell) without any obligation to do so.

As an example, a company can reduce transaction risk exposure of exchange rate fluctuation by establishing a short position in the foreign currency forward or option market to hedge the domestic cash flow from their export sales receipt. For example, if an American company, Rexo Equipment had a sales contract with their German dealers for future delivery in 2006 of € 5 million of office equipments. Rexo has risk exposure to a decline in the value of these export receipts. In order to offset this exchange rate risk, in 2005, Rexo might have sold a euro forward contract in the Forex derivative markets to establish a hedge. Rexo's transaction is described as a covered hedge because Rexo anticipates euro receivables (from their German dealers) equal to the amount of their short forward position. In other words, their contract sales receipts "cover" their obligation to deliver as a seller of euro forward contracts.

Let's say Rexo enters into a forward market by agreeing to deliver €5 million at some pre-specified forward price (say $1.00/€) and future settlement in 2006 would make money for REXO if the dollar actually appreciated and the euro declined in value. For example, if euro declined to $0.85/€, Rexo would be entitled to receive $1.00/€ deliverable by purchasing the Euro in the spot market for only $0.85. Therefore, Rexo cancels its position and can collect $0.15/€ x 5 million euros - equivalent to $750,000 on their forward contract. This cash is just sufficient to cover their $1.00 to $0.85 per euro loss in the value of their 5 million euros export receipt from their German dealers.

EXCHANGE RATE DETERMINATION & IMPLICATIONS FOR THE CHOICE OF EXCHANGE RATE REGIME

Just like any other market, exchange rate being the price of currency is determined, in the absence of intervention by market forces of demand and supply of the particular currency. Demand for ringgit for example arises when foreigners buy our goods and services or assets, either financial or real. The supply of ringgit comes from Malaysian importers of foreign goods, services and assets.

The balance of payments places the flow of goods and services under the current account (CA) and the flow of assets (financial and real) under the capital account (KA). The central bank official reserves transaction (ORT) balances the account. The sum of the current account and capital account is called the official settlement balance (OSB). When the Central Bank acquires (sells) foreign currency reserves ORT is negative (positive).

$$BOP = CA + KA + ORT = 0 \qquad (1.1)$$

or

$$CA + KA = -ORT \qquad (1.2)$$

The issue of what kind of an exchange rate regime should be adopted by any economy has been debated for quite some time. An exchange rate regime means a system that is adopted by the monetary authority (the central bank) of any government to determine the exchange value of the domestic currency against other currencies in the world. Basically, there are two main exchange rate regimes: the fixed exchange rate regime where the exchange rate is not allowed to vary and the floating exchange rate system where the value is determined by market forces.

In practice, there are many kinds of exchange rate regimes that are in between, including those that allow some kind of flexibility into an otherwise fixed system and others which are "managed floats" allowing some degree of stability into a floating system. There are very few completely free floaters around, even those economies that claim to have a floating system such as the United States would have its central bank intervene inside the foreign exchange market whenever they deem it to be necessary to do so.

In a completely free floating system the exchange rate of the domestic currency is being determined by market forces - the supply and demand for the currency. A supply of a currency, ringgit for example, can arise when Malaysians demand foreign currencies to pay for their imports. Similarly a demand for ringgit arises when importers of Malaysian products require ringgit to pay to Malaysian exporters or when exporters who are paid with foreign currencies exchange these with ringgit. Thus, current account surplus tends to be associated with currency appreciation, while a current account deficit with depreciations.

But demand and supply of currency does not come only from trading of goods and services. As equation 1.1 suggests demand and supply also arises from the sale and purchase of assets that are both real and financial.

In the last few decades, financial liberalisation across the globe has meant the opening up of markets and capital moves in search of higher returns. As interest rates are returns to financial investment, the global capital is attracted to interest rate differentials across the globe. This has increased the capital mobility and capital now moves from one country to another very fast, faster than the movement of goods, services and labour. The ability to short sell in the forward market has meant greater speculation and much volatility in the currency market. Elhiraika (1999) argues that speculation and volatility contributed much to the many currency crises that happened towards the end of the last century.

There is no unambiguous answer to the question "which is better, fixed or floating?' At any particular time in the history of the modern world, one of these two regimes may prove to be more politically popular. The Great Depression in the 1930s, saw the collapse of one of the most rigid fixed exchange rate systems ever used -the Gold Standard. The fixed exchange rate system was thought to be too rigid to meet the demands of expanding economies. The system that followed was "the Bretton Woods System which was essentially a system of pegging with a small degree of flexibility.

By the early 1970s, that system was under intense pressure as major currencies started to float, with the pound sterling being floated in June 1972 and the US dollar in 1973. Since the collapse of Bretton Woods, the world witnessed what was to be called a generalised floating system. With major currencies now floating, developing countries tended to follow suit, or at least it was thought to be "politically correct" to claim to have an exchange rate regime that was "flexible." In practice, many of the countries which claim to be using a flexible or floating system are in fact "peggers."

A floating exchange rate system has its own advantages. One of it is to relieve the government of constant intervention and the burden of having to have a large supply of foreign currency reserves to support the par-value if it is fixed. The system also has an automatic mechanism to correct problems in the balance of payments – if currency depreciates, then exports would be cheaper and thus more competitive and this helps the current account deficit to improve. However, post 1973 developments indicate that volatilities in exchange rate movements can be severe. Increased volatility can create an environment that is not conducive for trading and economic growth by making pricing and investment decisions difficult in the face of exchange rate uncertainty. The end of the 20th century also witnessed many countries that went into crises because of huge fluctuations or severe depreciations in the domestic currencies, including the Asian 1997-98 crisis.

Historically, trading in foreign exchange was the result of international trade as buyers and sellers need foreign currencies to settle transactions. Now, ironically, currency trading has little to do with international trade, which accounts for only about two per cent of currency movements. This is why if everything is left to market forces, the exchange rate could be very volatile. In a speculative environment, currency traders' perceptions about the market may not always be influenced by market or economic fundamentals and this could lead to market instability. Since there are many factors that can influence speculators to react one way or the other, an economy adopting a floating exchange rate is very much at the mercy of the market. The Forex is so huge that in the advent of a one way speculation (say of a currency devaluation), no central bank in the world has reserves which are huge enough to offset the market forces.

As an example, during the 1997-98 financial crisis, the ringgit depreciated from RM2.47 to the USD in mid-1997 to the lowest RM4.88 to the USD in early 1998, a depreciation of about 80 percent. This happened despite claims that the Malaysian economic fundamentals were good. Although there is a limitless number of explanation to the crisis, one of the more popular ones being offered is the "contagion effect" theory. The Malaysian ringgit was attacked by virtue of the fact that speculators perceived the Malaysian economy to be in a similar situation as that of Thailand and Indonesia and holders of ringgit quickly made the exit.

Thus, a floating regime may expose the local currency to many factors that can make its value unstable. A small open economy like Malaysia would be more vulnerable because it is exposed and influenced by so many factors at the global level. The Asian crisis probably brought different lessons to different people. Prior to the crisis, countries like Indonesia, Malaysia, Singapore and Thailand were unofficially pegging their currencies to the US dollar. The official regime may state that the exchange rate is being determined by a basket of currencies but many observers such as McKinnon (2001) argue that the monetary authorities in these countries were essentially pegging the currencies to the US dollar. Those who favour the floating system argue that the Asian crisis was due to the weaknesses of pegging, Thailand for example could not maintain the peg and had to float the baht in July 1997 marking the beginning of the Asian crisis.

Another view of the causes of financial crises like the Asian financial crisis is due to the inherent weaknesses in the western based financial system which relies on interest-based activities. Easy debt financing has resulted in over investment in real estate and projects with low returns. Failing to achieve the expected returns, the large capital inflows into these Asian countries saw a sudden reversal which worsened the already falling currency markets and led to the worst financial crisis in the history of the region. Elhiraika (1999) puts forward the argument that the solution to the problem lies in adopting Islamic principles in debt financing.

DEVELOPMENTS IN ISLAMIC ECONOMICS AND ISLAMIC FINANCE

Islamic Finance dates back more than a thousand years when Muslim traders who could easily be among the pioneer players in the process of what we now call "globalisation"--developed the financial tools to meet the requirements of Islamic law or the Shariah. The principles laid down in Qur'an and the practices as illustrated in the words and actions of the prophet (hadith) in relation to commerce and business provided early guidelines to Muslims and these were developed to become a comprehensive set of laws governing Muslims' commercial conduct.

More recently, there are scholars who have developed what is referred to as Islamic Economics, which provides for an alternative view to mainstream or conventional economics and challenging the relevance of many of its theories and principles in particular the notion of value free economics. [2]Even though early Islamic evidence from the life and practices of Prophet Muhammad indicates that Islamic practices resemble that of free market, especially when the prophet himself discouraged interference in the price mechanism, many traditions confirm the principle that the government has the right to intervene in an economy to make sure that justice prevails[3].

Islamic Economics rest on the notion that gives emphasis on moral values and social justice. Chapra argues that if conventional economics progresses in the direction of shredding its secularism and value neutrality and injecting moral values and justice, this might ultimately lead to a convergence (Chapra, 2000). As global financial and economic crises become more acute, the search for an alternative or a remedy that incorporates "values and ethics" into the current system, the convergence argument may prove to be real.

The revival of Shariah based modes of financing and commercial transactions and the development of Islamic financial Institutions as we see today started to take place in the 1960s, when some Muslims in various parts of the world started to look for alternatives to the conventional interest based system as they became more aware of their religious obligations and of the strong prohibition in Islam for the use of riba'. Important milestone includes the set up of the Islamic Development Bank in 1975 and the first private Islamic Commercial bank, the Dubai Islamic Bank in 1975. Malaysia, a country that is leading Islamic finance in many aspects has now one of the most comprehensive Islamic banking and finance systems in the world. Its first Islamic bank, Bank Islam Malaysia was set

1. Idea mooted by Malaysian Prime Minister Mahathir Mohamad at OIC Summit Doha Qatar 2002
2. See for example M. Umer Chapra (2000), Mohd. Jalaluddin (1991)
3. Narrated by Abu Hurairah, the prophet once came upon a stack of food. He inserted his hand and the fingers reached something moist "What is this? "Said he., and the merchant said" It has been affected by the weather , O messenger of Allah." "Then why not put it on top of the stack so that people can see it? He who defrauds us is not of us. " Al-Hadith , Sahih Al-Muslim (Mohd Jalaluddin 1991).

up in 1983, but its first Shariah based organisation can be traced back to the Malaysian Pilgrims Fund, which began operation in 1963.

Initially, Islamic finance then came about more as a response to Muslims looking for alternatives to interest based system especially in part because of Islamic revival and fueled by the new oil wealth in the Gulf. Since then, Islamic banking in the Middle East is growing and becoming important in mobilising local and regional saving, as well as providing an important source of capital.

But in the last 20 years, Islamic banking and finance has emerged as a strong and viable alternative to the conventional system. Its clients comprise not only Muslims but people from all religions. In many countries like Malaysia, IBF has moved from serving the narrow niche market of Muslims to more "high street" existence serving everyone who prefers to opt for its services. In fact, some Islamic banks in Malaysia like Maybank and the new foreign Islamic Bank of Al Rajhi, the Non-Muslims form a bigger proportion of the banks' clients.

FOREX AND EXCHANGE RATE REGIME FROM AN ISLAMIC PERSPECTIVE

How does Islam view the current practices of foreign currency trading? It is easy to see that the spot buying and selling of currencies are similar to any other forms of business transactions but how about the more sophisticated derivatives market of forward futures and options?

There are very few indications about the concept of exchange rates from the earlier writings of Islamic scholars. The exchange rates of the silver coins (Dirham) and the gold coins (dinar) were determined by market forces. According to (Ahmed, 2001) the earlier writers (Islahi, 1988, 1992) report that Ibn Taimiyah and Ibn Qayyim emphasised the importance of keeping the value of money stable. (Siddiqi, 1992) maintains that in an Islamic currency market, exchange rate is determined by market forces of demand supply. However, Central banks can intervene on the basis of Maslahah that is to protect and promote public interest (Saiful Azhar Rosly 2005, Siddiqi 1992).

Most Islamic writings on the principles of currency trading *(bai a- sarf)* are guided by the following hadith:

> "Gold for gold, silver for silver, wheat for wheat, barley for barley, dates for dates, salt for salt, like for like, equal for equal, hand to hand. If these types differ, then sell them as you wish, if it is hand to hand (Muslim)."

This has been taken to mean that when commodity money is exchanged (like gold and silver) they should be of equal amounts regardless of quality and the transactions should be completed on the spot. The exchange of different units

of one kind for another for example, gold for silver is allowed with different amounts at an agreed exchange rate as long as the transaction takes place on the spot. Khan (1991) discusses the different types of transactions in Forex –spot, forward, futures, and swaps) and concludes that the conventional system in the forward, futures and swaps are not in line with Islamic principles.

The spot market is allowed and is clearly based on this hadith of the Prophet. The spot market is used mainly for traders, people who can be argued to have "real" needs for the currencies. In the case of forward, futures, swaps and options, these can be used by hedgers in order to protect them against loss of value as a result of exchange rate changes or by speculators who speculate on currency movements in order to get profits. Thus, hedgers move into currency markets to avoid or to reduce risks, but speculators expose themselves with risks in order to get profit.

There seems to be a consensus that speculation using the currency derivatives market through the forward, futures, swaps and options transactions are not Shariah compliant as they involve elements of Gharar (uncertainty) and Maysir (gambling). All these transactions involve both differed payment and differed delivery of a commodity which goes against the hadith. In addition because speculation in currencies is done with a view to profit and not to facilitate trading, actual delivery of the currencies seldom occur. Many of the traders (in this case, speculators) would sell their futures contracts prior to maturity. This kind of speculation can be highly destabilising for exchange rate movements and results in the now too common phenomena that exchange rates are no longer tied to real activities (trading of goods and services) but more to speculative activities which makes exchange rates more volatile.

In a discussion whether the main forms of trading in Forex are allowed in Islam, (Khan, 1991) concluded that while trading in the spot market is allowed, the conventional forward, futures and swaps trading contradict Islamic principles.

Ahmed (2001) quoted Siddiqi (1992: 20) on the Islamic rules pertaining to currency trading:

1. The government/central bank can interfere in the foreign exchange market to protect public interests (the principle of Maslahah)
2. Riba'-based transactions are prohibited. Besides interest on debt transactions, prohibition of riba' has other implications in Forex. As fiat money is ruled to be the same as commodity money (silver and gold), the rules of riba' relating to gold and silver apply to currency. This means that only spot transactions between two currencies are deemed to be Shariah compliant. Thus, current contracts that involve future transactions are prohibited. A transaction which involves future delivery of currencies is prohibited as it amounts to riba'-nisaa or delayed-payment riba' (Hamoud, 1985). The prohibited partial future transactions that may occur in the currency market may be the following:
   a) Taking delivery of foreign currency now and at a future date

b) Paying for foreign currency now and taking delivery at a future date. Note that transactions in the form of deferred payment (Bai-muajjal) and deferred delivery (Bai-salaam) involving goods are permitted even though in an international transaction the price shall be quoted in a foreign currency. However there are now Shariah scholars who agree to extend Bai-salaam to financial products and this is regarded as an Islamic alternative to using short selling as a mechanism for hedging (Saadiah Mohamad and Tabatabaei 2008).

3. Transactions involving Gharar are prohibited. Gharar refers to the doubtfulness arising from insufficient knowledge of the quantity and quality of goods by one or both parties in the transaction. In currency trading, transactions which amount to Maysir (gambling) is prohibited in Islam. Pure speculation not based on economic fundamentals may fall under this category of Gharar because of excessive uncertainty as well as elements of gambling. The following transactions are forbidden on the grounds of Gharar:
   a) future sale (of goods or currency) in which both delivery and payment are postponed to a future date
   b) selling something not in one's possession
4. Selling Dayn (debt or obligation) for debt or money is prohibited
5. In the absence of Islamic alternatives the maxim of necessity making the prohibited lawful, is used.

In conclusion, there seems to be a consensus from Shariah scholars[4] that currency trading in forward, futures, swaps and options under current conventional forms are not Islamic as they violate conditions put forth by the Islamic principles for currency trading and may involve all or some of elements of riba', Gharar, Maysir or the sale of assets not in possession.

What about hedging? Would this also be prohibited? Hedging provides some complications for Shariah scholars as hedging is used by traders–importers and exporters-- to reduce risk of exchange rate exposures. The purpose is to reduce risk as opposed to speculators who expose themselves to risk in order to gain profit which amounts to elements of gambling. Shariah scholars argue that hedging is allowed if the sole purpose is to hedge (protect) against loss of value as a result of currency fluctuation in the transaction of real assets. But speculation is disallowed because speculators go into the market not for real transactions, and so speculation is divorced of real activities and contain elements of riba', Gharar, Maysir which are prohibited in Islam as discussed above.

The problem is when hedgers enter the market they certainly do business with the speculators. For example a Malaysian exporter sells Malaysian products at a quoted price at USD10 million but expects to get paid in six months. If currently

4. See for example the decisions by shariah panel of advisors of Accounting and Auditing Organisation for Islamic Institutions (AAOIFI shariah standard). See also discussions on this matter from http://www.zaharuddin.net

the exchange rate is RM3.5 to 1 USD, at the present exchange rate he should get RM35 million. However if ringgit is expected to depreciate to RM3.0 in six months' time he might just get RM30 million, a loss of total RM5 million simply because of currency value changes over which he does not have control. In order to protect against this loss he could enter a forward market now by buying ringgit at say RM3.5 for 1 USD. In six months if his guess is correct and ringgit does increase to RM3 to 1 USD, he uses 1 USD to buy RM3.5 in the forward market. He would then use ringgit to sell to get USD. For every 1 USD, he gets a profit of RM 0.5, for 10 million USD, he gets RM5 million, enough to cover him for the loss of RM5 million from his export earnings.

However his involvement in the forward market necessarily involves the party of speculators, who would sell ringgit because he speculates that the ringgit will appreciate. Without the speculators, and with only the traders who would want to do forward trading, the market would be impaired.

Rosly (2005) argues that this problem can be avoided with the use of the dinar system. In the Islamic dinar system, an export of RM38 million can be contracted and quoted in Islamic dinar say 10 million Islamic dinar but payments settled in ringgit. In case there is volatility in the dinar value certain things can be done. Let's say the exports are payable in six months and after six months the 10 million worth of dinar is now worth RM40 million, the exporter will pass the RM2 million gain to the buyer as a discount (Wadhiah). Likewise if the dinar is worth RM36 million the exporter shall be awarded an additional RM2 million as an Ibra from the importer. In this way they cancel the risks both parties face.

Another form of Islamic alternative for currency trading to be used for hedging is the use of unilateral wa'd or promises. These are one-way promises similar to forward contracts, but since they are promises and not contracts they do not violate Shariah prohibitions for conventional forward or short selling. This involves one party (a commercial bank client) making a promise to buy a certain amount of currency in future at a certain rate agreed with the bank now.

According to Shariah Advisory Council (SAC) of Bank Negara Malaysia (2010), Islamic financial institutions are allowed to enter into a forward foreign currency transaction for hedging purposes based on Wa'd Mulzim which is binding on the promissory and the compensation for breaching of promise could be implemented. Nevertheless, no fee is allowed to be charged on the promisee because the upfront cash payment for forward currency transaction would lead to a bilateral wa'd which is not allowed by Shariah. In Islam, the bilateral wa'd is not allowed to be used in forward currency exchange since it is akin to contract, thus riba' will occur. However, binding unilateral promise does not violate any basic tenet of Shariah. Hence, the importers or exporters can use wa'd in the contract of forward involving currencies.

This is in line with the view of the majority of jurists who opine that unilateral binding wa'd without any consideration is permissible in a forward currency

transaction (Bank Negara Malaysia 2010). In 2004, a fatwa was obtained from a prominent Saudi cleric to allow the application of wa'd on foreign exchange (currency option), but only for hedging purposes. Meaning that, the importers of exporters can take foreign currency forward to cover for genuine business activities on the basis of wa'd and simultaneous exchange of the currencies at the agreed time (Muhammad Ayub 2007).

However, another Shariah alternative which is the use of Bai-salaam in currency trading remains controversial. If currencies are treated as money in its conventional form and function primarily as a medium of exchange then a strict interpretation of the hadith requires exchange of money (either of same or different type) be made in spot. Hence Bai-salaam contracts cannot be used in currency trading. Other scholars might want a more "liberal" interpretation so that it can be used in currency trading in a similar way that this contract has been extended to other financial products. Bai-salaam has many advantages compared to the conventional short selling and while providing a mechanism for hedging, it can reduce elements of speculation (Saadiah Mohamad and Tabatabaei 2008).

SHARIAH COMPLIANT FOREX AND IMPLICATIONS TO EXCHANGE RATE STABILITY

The argument for an Islamic Forex is that firstly, the system would be a natural extension that would support the development of an Islamic economy that strives for a riba'-free system. Secondly, it will allow for the introduction of Islamic alternative products. In an Islamic economy where there is wide application of Islamic banking and finance and where Islamic Forex prohibits conventional forms of currency trading, speculative activities will be reduced. This will in turn prevent shocks occurring in the currency market, reduce its volatility and stabilise the exchange rate.

There will be an absence or reduction of interest based activities (such as saleable interest bearing debt and the flow of hot money) and this will also reduce variability in the exchange rate. The movement in short term capital for speculative reasons and the attractiveness of interest rate differentials across the globe have been cited as the main reasons for the volatility of exchange rates. As the flow of speculative short term capital is discouraged in Islamic economies the focus will be on long term capital. Even though there is a need for a money market in Islamic economies the characteristics of Islamic financing would mean that contracts are sensitive to rates of return (instead of interest rates, but the elasticity will be smaller than that of conventional economies (Ahmed, 2001). This stems from the basic differences between a debt contract in the conventional economy and an Islamic one. In the conventional system, debt transaction is purely financial while in the Islamic system it is tied to real transactions. As such it cannot be liquidated as the rate of returns changes. There is a built-in lag in

the change in the rate of return and its effects on the capital market. As a result the disturbance arising from capital mobility due to rate of return changes will happen less frequently in an Islamic currency market making the exchange rate relatively stable. Furthermore as the sale of debt is prohibited, the sale and purchase of bonds will not occur as a result of interest rate changes.

However Ahmed (2001) argues that even though eliminating saleable interest bearing will decrease the volatility of exchange rates, without Islamic alternatives the overall volume of international transactions in an economy will be reduced. Islamic economies, most of which are developing, require capital especially long term capital to facilitate economic growth. Some of the gaps in capital can be filled with funds from abroad.

According to al-Ghazali, (cited in Chapra 2000), the objective of the Shariah *(Maqasid al*-Shariah*)* is to promote the well-being of all mankind, which is, safeguarding their faith *(*Deen*)*, their human self *(*Nafs*)*, their intellect *(*Aql*)*, their posterity *(Nasl)* and their wealth *(*Mal*)*. Hence whatever ensues that safeguard these five serves public interest and is viewed as desirable from the Islamic perspective.

The stability of the value of money is an important goal fundamental to the Islamic economic system. The goal of price stability and reducing the rate of inflation is certainly in line with this. Since exchange rate is price of one currency in terms of another and that maintaining stable exchange rates would ensure stability of the value of money hence its purchasing power vis-a-vis other currencies, the goal of exchange rate stability should be in line with the Maqasid al Shariah of safeguarding people's wealth.

While the floating exchange rate is closer to Islamic principle of being market driven, the high volatility observed in modern economies justifies government intervention on the basis of Maslahah or public interest. Fixed exchange rates while offering stability, do not reflect market forces and may not be sustainable in the long run. As such a system of managed float where the exchange rate is determined primarily by market forces but with government intervention as and when necessary is an appropriate system for an Islamic economy. This middle of the road system, requires a crafty management of the exchange rate, and calls for an appropriate balance between exchange rate stability and other macroeconomic objectives.

CONCLUSION

This paper discusses how an Islamic Forex in an Islamic economy with its wide range of Islamic banking and finance applications will contribute towards exchange rate stability because of the reduction in speculative activities. Furthermore, the reduction and eventual elimination of interest bearing assets will reduce volatility as capital movement will no longer be sensitive to changes in global interest rates and therefore, helps to prevent sudden inflows and outflows of hot money.

However, one should not forget that Forex is such a huge market and if players of Islamic Forex are limited to local investors and other international Islamic players the effects on exchange rate stability will be negligible[5] if Islamic economies are open economies which receive international capital flows of both kinds, conventional and Islamic. And yet, in the absence of a good range of Islamic products as alternatives, prohibiting conventional forms of currency trading and other forms of debt financing will reduce the flow of both short and long term capital. Even though short term capital may contribute to volatility and a reduction in the flow is not a bad idea altogether, a healthy money market for short term capital is necessary in any economy. Similarly long term capital is necessary for economic growth and to fill the domestic investment-saving gap.

Thus it is important that Islamic economies are able to offer viable Islamic products for both short and long term funds to replace interest bearing capital and the current forms of currency trading which are based on speculation. This is because as our discussion shows, Islam does not prohibit activities which are conducted to reduce risks of loss on the part of traders, but, if these activities are inextricably linked with excessive speculative activities and contain elements prohibited in Islam then they are deemed to be non-Shariah compliant.

There is clearly a need to come up with more Shariah-compliant products especially with regard to risk management and hedging to meet the demands of the modern day economy.

Finally, the lack of institutions that provide and support Islamic modes of financing across borders is clearly the main obstacle to the Islamisation of international transactions. The Islamic dinar market which acts as an international money market to provide short term funds to Islamic countries and businesses on modes of Islamic financing, needs to be developed. The main players should be Islamic financial institutions or commercial and investment banks, across the world. Other needs include a development of secondary markets for Islamic financial instruments so that investors can invest their savings across borders and for Islamic Finance to move towards more equity based financing which promotes more risk sharing rather than the present day dependence on debt based financing which still benchmarks interest rates and thus make funds sensitive to changes in the global interest rates. Central banks in Islamic countries need to play a more active role in monetary and fiscal policies in both the primary market in terms of issuance of Islamic instruments as well as in the conduct of open market operations involving Islamic instruments as part of their monetary policies. As more Islamic instruments are used across borders which involve use of different currencies, Shariah screening in currency trading can contribute towards reduced speculation and reduced exchange rate volatility.

5. The assets owned by the world Islamic banking are still small. The total assets owned by all Islamic banks in the world are not even matched by the smallest top 60 conventional banks in the world. Even the assets of Al-Rajhi Bank which is the world's largest Islamic bank, stand at only about 1 percent of the world's largest bank, Bank of Tokyo-Mitsubishi UFJ. (Utusan Malaysia 24 Feb 2007 p21.)

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ISLAMIC BANK CONSUMERS IN JAVA: THE HERO, THE DUPE, THE SNOB OR THE SOCIALLY RESPONSIBLE

ABSTRACT

In the early 2000s, Islamic banking evolved as a new model of Indonesia's financial institutions. However, in practice, there have been significant differences between countries that have been successful in applying Islamic banking and those that have not. This article is aimed at exploring the applicability of Islamic banking in a particular cultural context. In particular, the study analyses the applicability of Islamic banking in Indonesia, mainly in East Java where most Muslims are found. A cultural theory is presented whereby Islamic banking is depicted as a culturally dependent strategy. The study proposes that the successful implementation of Islamic banking requires complementarities between the reform strategies that are adopted and the particular cultural characteristics of the country in which they are implemented.

KEYWORDS

Islamic Banking; Cultural Context; Javanese Indonesian

INTRODUCTION

Wouters (2007) in his article 'Islamic banking in Turkey, Indonesia and Pakistan: A Comparison with Malaysia' argues that Islamic banks in Indonesia are not growing due to the fact that only 1.7 percent of the total population is putting their money in banks which operate under Shariah concept. He argues that Muslims in Indonesia are lagging behind in the percentage of savings in the Islamic banking system. The Javanese are the largest and most dominant group in the country, followed by Sundanese (15 percent), Madurese (3.3 percent), Minangkabau (2.7 percent), Betawi (2.4 percent), Bugis (2.4 percent), Banten (2 percent), Banjar (1.7 percent), others or unspecified (29.9 percent) (CIA, 2009). The Chinese may dominate the Indonesian economy, but the Javanese, with their numerical superiority and political influence, set the tone in which business is conducted. It would, however, be misleading to perceive of the role of the Javanese in purely political terms.

The Javanese are basically hard to understand. Most of them do not say what they really think if it might cause trouble for themselves or for others. The non-Javanese frequently accuse the Javanese of being slow and unwilling to speak honestly (even for a good purpose), preferring to hide their real intentions behind a facade of words. The Javanese are also often accused of being hypocrites due to their habit of saying 'yes' when they really mean 'no', a habit embodied in the traditional saying 'nggih-nggih ora kepanggi', which means saying yes but not doing it. Javanese are also accused of being clannish, reluctant to adapt to the ways of the non-Javanese. They frequently differentiate themselves from the non-Javanese using the terms dudu bangsane (not our people), *ora nJawa* (not Javanese), *wong sabrang* (people from overseas), etc. (Sutarto, 2006).

Though the majority of Indonesians are Muslims, Indonesia is not an Islamic country. In Indonesia, Pancasila (the five pillars that eventually became the state foundation: Belief in one God, Humanitarianism, National Unity, Representative Democracy and Social Justice) is basically a compromise between secularism, where no single religion predominates in the state, and religiosity, where religion (especially Islam) becomes one of the important pillars of the state. An Islam-inspired agenda is welcome to the extent that it corresponds with, and does not contradict, Pancasila. In other words, it is a common belief that Indonesia is neither a secular nor an Islamic state.

The rejection of the Islamic state status rooted back to August 1945 when, at the last moment, seven words were removed from the Preamble to the Indonesian Constitution (known as the Jakarta Charter or *Piagam Jakarta*). These seven words were '*dengan kewajiban menjalankan syariat Islam bagi pemeluknya*' (with the obligation for adherents of Islam to follow Shariah or Islamic law). The omission of the seven words in the Preamble has acted as a point of contention

for many Islamic groups in Indonesia, and has influenced their relationship with the government since Independence. During the last half century, Indonesian Islamic-based parties have periodically attempted to have the seven words reinstated, but without success (Hosen, 2005). It is worth noting that for more than half a century, Indonesia has been unable to conduct an uninterrupted dialogue concerning the position of Shariah in the Constitution.

In 1945 and 1955, efforts were hampered by the pressure of time and political manoeuvring by Sukarno and the military. Under Soeharto, debate on the issue was forbidden due to its disruptive potentials. Under the rule of Soeharto in the 1970s and 1980s, the social and political role of Islam was repressed. The party system was simplified and all Islamic parties were forced to fuse into the PPP (Partai Persatuan Pembangunan - United Development Party). Several laws – on marriages and the equalisation of state and Islamic courts - restricted Islam further.

In 1984, the Nahdatul Ulama (NU) left the PPP and, in this way, emancipated itself from state dominance. Around 1990, a turnaround in state policy occurred and, against the opposition from army circles, Soeharto began to court Islam to strengthen his own power base. In 1990, ICMI (Ikatan Cendekiawan Muslimin Indonesia – Indonesian Muslim Scholars Association) – a modernist organisation led by state officials – was founded. Islamic religious, financial and educational institutions were financially supported by the government and, in official context, Islamic rules of behaviour were respected.

Yet Soeharto's policy to domesticate Islam for his own political ambitions failed. The NU, led by Abdurrahman Wahid, remained aloof. Besides a tiny minority of fundamentalists who wanted to establish a theocratic state, the major groups belonged either to the modernists or the neo-modernists. The latter are more positive towards influences from the West, concentrate less on political issues and are more interested in furthering the social and economic advancement of the Muslims. The modernist approach seeks a compromise between traditional Islam, the universality of the *Ummah* and the model of the nation-state. Leaders of both NU and Muhammadiyah assert that even without formal acceptance of Shariah in the Constitution, the Muslims' demands can be met by the state. In the words of Anies Rasyid Baswedan, the current Rector of Paramadina University, a university based on Islamic ethics in Jakarta, "The focus is no longer on how to bring Islam into the foundation of the State, but how to bring Islamic values into policies of the State" (Hosen, 2005).

In explaining the lack of growth, Snodgrass (1980) proposed two schools of thought: the structural hypothesis and the cultural hypothesis. The structural hypothesis blamed the structural impediments erected by the current government, while the cultural hypothesis proposed that values were instrumental in obstructing the economic advancement.

However, when the government allowed the operation of banks under the Shariah law, the progress has not been as expected. Even after the fatwa that prohibits bank interest was announced by the Ulama Council of Indonesia or *Majelis* Ulama *Indonesia* (MUI) at the end of 2003, the number of customers and the amount of money that shifted to Islamic banks are not significant compared to those who choose to remain. At this point, it is obvious that there is limitation in explaining the phenomenon using the structural hypothesis.

The second hypothesis analysed is the cultural hypothesis, which proposes that Javanese values are instrumental in obstructing their economic behaviour. According to Max Weber's *Religions-Sociologie*, the relationship between religious commitment and economic behaviour has been an important theme both in economic history and in the sociology of religion (Geertz, 1956). The broad relationship he postulated between certain kinds of religious ethics and certain types of economic practices has proved stimulating. It is in such a context that this paper is presented: it is an attempt to lay the ground work for an analysis of religious belief and economic behaviour in a given town in East Java, Indonesia.

ISLAM IN EAST JAVA

With some 88.7 percent of its 250 million people professing Islam, Indonesia is the world's most populous Muslim nation. Almost half of the country's Muslims reside on the island of Java. Until the Islamic resurgence of the 1980s, however, the Islam to which the majority of Javanese subscribed to was a spiritualistic blend of Javanese traditions and normative Islam (Geertz, 1960; Wright, 1991). Many Javanese Muslims admit that a generation ago, they were lax in their performance of the pillars of Islam, including daily prayers, the annual fast, and the payment of religious alms. Few Javanese Muslim women covered their heads. Those who did tended to be older women from the ranks of rural traditionalists or the Muslim merchant class. On college campuses, as well as in banks, government offices and business establishments, Western-style skirts or dresses and short-sleeved blouses were the norm (Hefner, 2007).

Religion has a deep and paradoxical relationship to culture. Religion and culture are cut from the same cloth in that both are psychologically rooted and socially transmitted belief-systems (Atran and Norenzayan, 2004). In this way, the Islamic practices in Java manifest varying combinations of symbols and conventions, reflecting local and global understandings of Islamic authority. The different approaches in practicing Islam in Java occupy varying positions between two poles. One pole is characterised by a preoccupation with ritual practice based on local understandings of ritual efficacy. The other is characterised by a need to display affiliation with the formalised system of beliefs and obligations known as Islam. In the former, signs of Islamic convention may be partial or lacking because outward conformity with its scheme of beliefs and doctrines is not of

pressing concern. What is important to this group is achieving ritual efficacy. By contrast, Muslims at the latter pole ensure that ritual practices can be understood in the greater scheme of formalised Islam. These poles are described with varying nomenclatures. The best known is *Clifford Geertz's* dichotomy between *abangan* and santri. He notes that *'abangans* are fairly indifferent to doctrine, but fascinated with ritual detail, while among the santris, the concern with doctrine almost entirely overshadows the already attenuated ritualistic aspects of Islam' (Geertz, 1960).

The typical Javanese is not so much a Muslim as Muslim-minded. Though nominally a *Shafiite*, the intricacies of traditions, hadiths and doctrines of duty, *fikh* and the differences between *fikh* schools, madhabs and even the major passages of the Koran may be unfamiliar to him. Nevertheless, many Javanese regularly attend their mosque, submit – at least outwardly – to the five fundamental requirements of the faith, Islamic laws of marriage and inheritance, and revere mosque officials and *hadjis*. But for the rest, Islam has been adapted to existing traditions and its doctrinal requirements have been strangely observed. The precepts of Animism, Hinduism and ancient class distinctions have been blended with Islam. This aspect of Javanese mysticism, variously called *kebatinan* (mysticism, spiritualism) or *kejawen* (Javanism), have been studied and admitted by Dutch and other Western scholars since the colonial era (Wright, 1991).

The *wayang* and the *gamelan*, which are to some extent cultural products of the Hindu-Javanese periods, are incorporated into Islamic feasts. Early Muslim leaders apparently deliberately introduced *gamelans* (because of their past popularity) at the sacred feast of the Prophet's birth in order to draw people. Thus, the Javanese's identification with Islam is not so much in its religious doctrines, but in the demonstrative participation in such cultural aspects which blend Animism, Hinduism and Islam, such as various feast days, most of which are Muslim in origin.

Despite the large number of Javanese who embrace Islam, they will remain Javanese and the endeavour to be truly Javanese has never flagged. It frequently happens that groups seeking to maintain a traditional Javaneseness operate secretly so as not to collide with the interests of religion or the Indonesian state (Sutarto, 2006).

THE HERO, THE DUPE, THE SNOB, OR THE SOCIALLY RESPONSIBLE?

Two images of the consumers have long dominated the socio-economic pattern on consumption. The core to economic theory is that of the consumer as an active, calculating and rational actor: someone who carefully allocates scarce resources to the purchase of goods and services in such a manner as to maximise the utility obtained. The other is that of the passive, manipulated and exploited subject of market forces: someone who, as a consequence, is largely constrained to consume in the way that they do. Don Slater has referred to these two images

as *'the hero'* and *"the dupe"* (Campbell, 2005).
However, over recent decades, a third image has come to the fore, largely as a consequence of the impact of post-modern philosophy upon social thought. This represents the consumer as neither a rational actor, nor as a helpless dupe, but rather as a self-conscious manipulator of the symbolic meanings that are attached to products: someone who selects goods with the specific intention of using them to create or maintain a given impression, identity or lifestyle (Featherstone, 1991; Campbell, 2005). Hermawan Kertajaya, an Indonesian Marketing Guru, applied the term of *'the Snob'* for this type of costomers. Contemporary Indonesian society can be described as a society that consumes commodities not only to satisfy needs or wants, but also to build a social identity and structure interpersonal interactions. In this context, consumption has become, for many, a fundamental aspect of daily life verified by the latest model of Nokia and Blackberry, which are frequently launched in Indonesia.

However, there is growing evidence that some consumers' purchases, as well as post purchase behaviours and intentions, are influenced by their strong social consciousness (Ogle *et al*, 2004). These consumers – who demonstrate concern about such issues as labour practices, production conditions, environmental impacts and trends toward materialism – have been described as socially responsible, ethical, culturally creative, green, and/or environmentally responsible. The philosophy underlying the establishment of Islamic Banking in Indonesia is in line with these trends.

As in some Islamic countries, more and more people are concerned with the non-Shariah compliant practices by the conventional banks, such as bank interests, resulting in their avoidance in saving their money in conventional banks.

The history of Islamic banks in Indonesia can be traced back to 1990, when the conference of MUI was held in Cisarua, West Java, Indonesia. The conference was motivated by the increase in Indonesian Muslims who started demanding for interest-free banking products and services, in line with the requirements of the Shariah. It was at this conference that the proposition to establish an Islamic bank was made. Thus, it can be seen as an important milestone in Islamic resurgence in the area of economics, banking and finance in Indonesia. Following the conference, continuous efforts have been made to put the idea into practice.

It is important to note that, at the early stages, the Ulama (Islamic scholars) and academicians were the initiators of the idea of Islamic banking. However, the concept of Islamic banking was still unfamiliar to bankers and regulators. Having struggled on a long journey, on November 1992, the first Indonesian Islamic bank, Bank Muamalat Indonesia (BMI), was inaugurated. Yet, it is important to note that even under the new Banking Act No. 7/1992, BMI was actually recognised as a 'profit-sharing bank', and not an 'Islamic bank'.

This study argues that the Muslims in East Java are neither , *'The Snob'*, nor 'The Socially Responsible'. They are *'The Hero'* – the active, calculating and rational consumer who carefully allocates scarce resources to the purchase of goods and services in such a manner as to maximise the utility obtained. This notion was proven with the result of two consecutive researches conducted by Triyowono, *et al.* (2000) and Soenarmi (2006) from the Faculty of Economics, University of Brawijaya, who found that Islamic Banks do not represent the needs and demands of the people, as they view it as no different from conventional banks and that bank interest is not forbidden or *haram* even though some of them know that the Holy Qur'an explicitly mentions prohibition of interest in *ayah* 2:278 to 279.

Surprisingly, among sampled respondents, only 32.6 percent preferred Islamic banking, while the remaining preferred conventional banking. The research further showed that from those who preferred Islamic banking, only 3 percent are using their products and services. Only 26 percent felt the need for Islamic banking, while the rest tend to be neutral and felt that they would not use Islamic banking if they don't have to.

The main finding of the research was that those who are consumers of Islamic banking do not necessarily believe that conventional banks' interest rate is *riba'*, which makes it forbidden or *haram*. This means that the choice of using Islamic banking is not driven by Islamic values, but rather because of its convenience, for example due to the locations, services provided, etc..

The fatwa (which are decrees on specific issues issued by Islamic scholars or authority) that proscribes interest or *riba'* issued by the MUI seemed to have little effect. MUI is an independent non-governmental organisation, established on 26 July 1975, in Jakarta. The members of MUI consist of Ulama and other Muslim scholars from various Muslim organisations in Indonesia, including the two largest organisations, which are NU and Muhammadiyah. On 16 December 2003, the Fatwa Commission of MUI, based on *ijtima* or consensus, agreed that the bank interest was *haram*. Following that, on 24 January 2004, MUI issued fatwa number 1/2004, which is still valid, that stated that interest charged by conventional banks and other financial institutions for loan was categorised as *riba' al nasi'ah and haram*. Along with this fatwa, Muslims in Indonesia were urged to use Islamic financial institutions.

The issuance of this fatwa led to a debate amongst the Muslim society in Indonesia (BNI Syariah, 2005). This fatwa was welcomed particularly by Muslims who wanted a formal statement from MUI with regards to the prohibition of interest in the transaction for borrowing money *(al-Qardh)* or lending money

(al-Dayn). On the other hand, other Muslims questioned the effectiveness of this fatwa. This fatwa was issued without any coordination with the Indonesian Central Bank. Moreover, they were worried that this fatwa would trigger a mass run on conventional banks. People would withdraw their money from the conventional banks and deposit it in Islamic banks. Thus, the deposits of Islamic banks would increase drastically, whereas Islamic banks may not have the capability to distribute their funds to the real economic sectors. As a result, according to this side of the debate, the increase of deposits would more likely influence the liquidity of Islamic banks.

Regardless of the debate on the fatwa, the fact is that Islamic banking has grown significantly in 2004, a year after the issuance of the fatwa (Widagdo and Ika, 2008). However their findings indicated that the financial performance of Islamic banks in Indonesia is not associated with the fatwa issued by MUI. It seemed that the macro-economic indicators, such as interest rate, might have affected the performance of Islamic banks in Indonesia. This supports the findings of previous studies (Gerard and Cunningham, 1997; Metawa and Almossawi, 1998; Haron and Ahmad, 2000; Ghafur, 2003; Rahmatina & Salina, 2009) that indicated the motivation of depositors of Islamic banks is the rate of return on the savings (welfare maximisation premise).

CONCLUSION

Structural and cultural perspectives determine the predicament of Islamic banks in Indonesia, mainly in the Muslim-dominant East Java. Though MUI's fatwa reaffirmed that bank interest is *haram*, this fatwa is not legally binding on society. Therefore, those who disobey the fatwa are not punished socially or legally, as Indonesia is not an Islamic State. However, the fatwa does provide a clear guidance for Indonesian Muslims in dealing with conventional banking services. For Islamic banking, this fatwa is an additional weight that provides moral advantage and support.

Culture influences consumer behaviour (Schiffman and Kanuk, 2010). The core element in culture is *values*, which are broad tendencies to prefer certain states of affairs over other. They are about evil vs. good; dirty vs. clean; immoral vs. moral; and irrational vs. rational. Relationships between people in a society are always affected by the values that form part of the collective programming of people's minds in that society (Hofstede, 2007). By this analogy, one of the most important indicators of consumer belief towards an Islamic bank is his/her preference regarding an Islamic bank. This belief represents the values in his/her overall Islamic value system. If this person highly values Islamic banking, in line with his/her overall Islamic value system, then he/she will tend to choose Islamic Banking. On the other hand, if this value is relatively weak within his/her overall Islamic value system, the motivation to use an Islamic bank will be low.

Since the typical Javanese is not so much a Muslim as Muslim-minded, it is common to find on one extreme a few who believe that the interest rate used in conventional banking as *riba'*, making it *haram*, while on the other extreme those who believe that interest rate is not *riba'* and, therefore, not *haram*. By using Geertz' taxanomy, those whose see the interest rate as *riba'* are then identified as belonging to the santri segment, while those who do not believe that the interest rate is *riba'* is in the *abangan* segment. In between, there is the *floating mass segment*. Under this very small segment, it is very naïve to conclude that only 1.7 percent of the total population is interested in putting their money in a shariah-compliant banking concept. This figure could be bigger if proper segmentation method is applied. Further segmentation based on spectrum of values regarding whether placing funds in the Islamic banks are regarded as *Sunnah* or not is needed.

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ORGANISING INFORMAL LABOUR IN INDIA AND INDONESIA: A DISCUSSION OF BARRIERS AND BEST PRACTICES OF OVERCOMING THEM

ABSTRACT

The majority of global workers are engaged in vulnerable, informal work that offers very little (if any) welfare protection. While there are many possible ways to improve the conditions of work in the informal sector, this paper focuses specifically on organising as an agent for change. We undertake an exploratory analysis of two Asian countries with particularly high proportions of informal sector employment – Indonesia and India. In so doing, we highlight the variety of possible strategies for successfully organising informal sector workers; we also show that similar barriers to organising the informal sector may be manifested differently across countries according to country-specific institutional structures and cultural norms.

KEYWORDS

Trade union; Informal sector employment; Decent work; Labour law

INTRODUCTION

Around the world, most labour market statistics reflect formal sector work—work which is standard, typical, and permanent (in either the public or private sphere). This is the work we know the most about, because it is regulated, taxed, and measured in a variety of ways. In the developed world, informal work (often characterised as non-standard, atypical, and temporary) is atypical in the sense that it represents a minority of the work performed. Yet in the developing world, the opposite is true; informal employment comprises one-half to three-quarters of non-agricultural work (ILO 2002), and the majority of agricultural labour as well. Informal workers generally fall outside of the government net of tax, social contributions, and labour laws (De Ruyter el at. 2009), so it is difficult to track these workers or protect them in the usual (legal) ways.

Although exceptions exist, informal employment is largely vulnerable employment, and because of this informal work is generally not considered 'decent work'. Decent work, as conceptualised by the International Labour Organisation (ILO), promotes "inclusivity and productivity in the workplace" by requiring decent wages, safe working conditions, and regulated working hours, among other things (ILO 2010a). As such, decent work "is a source of personal dignity, family stability, peace in the community, democracies that deliver for people, and economic growth that expands opportunities for productive jobs and enterprise development" (ILO 2010a); it fosters positive economic freedom; i.e., enabling capabilities to better participate in market economies, in accordance with Sen's capability endowment approach (see Warnecke and De Ruyter 2010).

While there are many possible ways to improve the conditions of work in the informal sector (see De Ruyter *et al*. 2009), this paper focuses on one particular method: organising workers in the informal sector. Organising can result in significant gains for informal sector workers; however, organising this sector is difficult. Our overarching goal is to elucidate common barriers to organising the informal sector, and discuss best practices for overcoming them. We undertake an exploratory analysis of two Asian countries with particularly high proportions of informal sector employment in their societies - Indonesia and India. In so doing, we highlight the variety of possible strategies for successfully organising informal sector workers; we also show that similar barriers to organising the informal sector may be manifested differently across countries according to country-specific institutional structures, culture, and other factors.

THE INFORMAL SECTOR AND THE GLOBAL ECONOMY

By providing cheap labour to sustain profitable economic activity, the informal sector supports economic growth (De Ruyter *et al*. 2009). Yet it often does so invisibly, unassisted by economic policies aimed at the formal sector. The diversity of the informal sector should not be understated; it encompasses a wide range of market activities that reside outside the conventional scope of labour practices. Informal sector workers can be employed by unregistered informal enterprises, or can be owner operators, self-employed, or unpaid family workers. They can be temporary or part-time workers, casual day workers, contract workers, industrial outworkers, or unregistered workers (ILO 2002). They are located in rural and urban areas, and can be members of a variety of demographic groups - though women constitute the majority of informal sector workers in most developing countries (ibid.).

What most informal workers do share, though, is vulnerability - vulnerability to harsh working conditions, low wages, and limited upward mobility. This vulnerability disempowers informal workers and erodes their personal dignity; it prevents them from achieving their full potential in their family, community, society, and economy. Yet vulnerable employment has comprised more than half of all global employment over the last decade (as shown in Table 1). As defined by the ILO, vulnerable employment refers to select informal sector groups - contributing family workers or own-account workers who are less likely to benefit from safety nets that guard against loss of incomes during economic hardship (ILO 2009).

While informal work is often considered entrepreneurial (thus having a positive connotation), common practices of evading taxes and avoiding labour regulations are ultimately a detriment to the state (and society as a whole). Furthermore, many informal workers occupy their positions due to economic desperation and lack of alternatives. Perhaps this helps to explain why informal sector workers comprise a significant portion of the working poor (Heintz and Vanek 2007). An informal sector job may be better than no job at all (monetarily-speaking), but the fact that nearly half of all global workers still live on less than $2 US per day (see Table 1) shows that this is not a sufficient argument for maintaining the status quo. For both social and economic reasons, it is crucial to improve the quality of daily life for the millions of people working in the informal sector around the world[1]. Organising informal sector workers is one possible strategy for improving labourers' socio-economic welfare.

1. We realise that formal sector workers also comprise part of the working poor; this is an issue for future research.

Table 1 Global Employment Trends, selected years from 1998-2009

World Vulnerable Employment as share of total employment (percent)		
Year	Total	Female
1999	53.3	55.9
2007	50.6	52.6
2009	52.8	54.3
World Working Poor (millions)		
	US$1.25 per day	US$2 per day
1998	945	1429
2008	633	1185
2009	849	1368
World Working Poor (percent share of total employment)		
	US$1.25 per day	US$2 per day
1998	37.5	56.7
2008	21.2	39.7
2009	28.3	45.6

Source: ILO (2010b, 2010c)

ORGANISING THE INFORMAL SECTOR

Because informal labour lies outside the scope of formal regulation, individual informal sector workers have very little bargaining power over their wages or work conditions. Much informal labour is unskilled, and unskilled workers are often considered interchangeable - so employers are more likely to fire a worker for protesting than to take the worker's concern seriously. In many (but not all) cases, the informal worker's lack of power corresponds to his or her isolation from others; many types of informal work (particularly piece-work in one's home, but also scavenging for metal scraps, domestic work, etc.) occur in environments where there is no interaction between informal workers (Wikramasekera 2002; ILO 2003). It is precisely because of this correlation between powerlessness and isolation that the organisation of informal workers can help; there is strength in numbers.

The goal of organising the informal sector is to improve the daily life of informal sector workers, by increasing wages, reducing work hours, providing health insurance or education, or guaranteeing a street vendor a space from which to sell (among other things). Even small improvements can make a big difference to the lives of informal workers. Yet many attempts to organise workers focus only on the organising process itself - the first step of which is identifying and assembling people who share common goals or needs. While this task is crucial (and difficult in and of itself, as discussed in the following section), successful organisation of the informal sector requires an external program in addition to an internal one (Global Labour Institute 1999). The internal program "focuses on what the labour movement itself has to do to improve its capacity to organise and represent informal sector workers", while the external program "consists of the demands directed outside of the labour movement (to employers, public authorities, international organisations, etc.)" (Global Labour Institute 1999: 7-8).

In other words, successful organising needs to ensure the building of networks at multiple levels - local, national, and international - so that the informal sector group not only recognises itself, but also is recognised by policymakers (if the group is not recognised, it will not be able to effectively bargain for change). Networks can include government bodies, non-governmental organisations (NGOs), international policy-making organisations and private sector organisations. So that the organisation can better meet the multifaceted needs of the working poor, networks should also include educational institutions (Marshall 2010). Effective organising of the informal sector is thus more complicated than it might first appear.

BARRIERS TO ORGANISING THE INFORMAL SECTOR

Perhaps the most fundamental barrier to organising the informal sector is the sheer lack of data on informal sector workers. Since most official labour market statistics do not include the informal sector, basic questions about these workers (who and where are they? How many are there?) are not straightforward to answer. Yet in order to organise a group of workers, there must be an identifiable group to organise.

Even if one can identify informal sector workers, in order to organise them some sort of collective identity must be present. While it is often taken for granted that this exists among workers, this is a mistake, particularly in the informal sector. Informal workers "go where the work takes them, which means such workers are constantly on the move" (Handique 2009: 2). Most informal work is not associated with a particular address in the same way that - for example - a bank teller in the formal sector is likely associated with a particular bank branch. As a result, many informal sector workers do not have a specific 'workplace' they identify with, or 'co-workers' with whom to discuss their jobs. Some informal

sector workers do not even consider their activities to be 'work' at all (Wulandari 2008); instead, they simply see their activities as part of their daily existence. As De Ruyter *et al*. (2009) point out, "Why would someone join a union if s/he does not believe s/he is a worker?"

The ability to establish a collective identity is also impeded by the great diversity within the informal sector. Informal sector workers can be domestic helpers, scrap collectors, or street vendors; they might work in a factory or a small, unregistered business. These groups of workers do not always share the same needs. Some informal sector jobs are considered 'better' than others, and these jobs often are distributed according to existing racial, ethnic, gender-based, and religious hierarchies (Menon 2010). So labour markets, particularly those in developing countries, are highly characterised by internal divisions - divisions not only between formal and informal sector workers, but also between different types of informal sector workers. This complicates efforts to organise the sector. Is it better to organise one segment of the informal sector (e.g. one 'profession') at a time?

A variety of governmental barriers can also hinder workers' attempts to organise. For example, states may wish to court foreign direct investment by enabling least-cost production to occur (without bargaining over wages, etc.). The proliferation of export-processing zones (EPZs) throughout the developing world is one case in point; EPZs are entitled to several government concessions, including evasion of wage and labour laws, so that they can better contribute to short-run economic growth (Engman *et al*. 2007). Even where organising is legally permitted, the lack of enforcement capacity (and/or the lack of will to enforce regulations) in many developing countries facilitates egregious violations from employers (Elliott 2004). Therefore, legalistic solutions alone cannot adequately support labour organising (in either the formal or informal sector).

Finally, there are territorial issues involved in organising, since the task of organising workers has long been dominated by trade unions focused on formal sector employees. These trade unions have long "neglected the informal economy for several reasons…[including] the ease of organising formal sector workers…the high costs of organising workers in the informal sector and the perception or expectation that over time informal sector will be absorbed into the formal sector" (Sundar 2010: 4). However, the wage differentials for union members led to the shift of job creation in favor of informal, contractual labour that was less easily unionised (Sundar 2003). The immense (and lasting) growth of the informal sector and the "trade unions' dwindling numbers in the formal sector" have led to a sort of identity crisis for traditional trade unions (ibid.). Tensions thus emerge between traditional trade unions and the newer groups or unions attempting to organise informal sector workers (Sundar 2009). Should informal sector workers be absorbed into traditional trade unions or have their own organisations for representation and bargaining? These are important questions without a simple answer.

COUNTRY STUDIES OF INFORMAL LABOUR: INDIA AND INDONESIA

It is also worth asking whether the barriers to organising are the same across countries, or whether the barriers differ depending on cultural or institution-specific factors. A related question is whether best practices for organising are universal or differ across countries. To investigate these issues, we conducted an exploratory analysis of two developing countries with a high proportion of informal workers as a proportion of all workers - India and Indonesia. As shown in Table 2, in 2009 62.1 percent of all workers in Indonesia were informal workers (ILO 2010d). The incidence of informal labour is even higher in India; in 2009, 86.1 percent of total employment was located in the informal sector (ILO 2010e). Organising the informal sector could thus benefit a massive number of people; 432 million Indians and 64.8 million Indonesians worked in the informal sector in 2009 (ILO 2010d, 2010e).

Table 2: Informal Employment, India and Indonesia

Country	Informal employment as percent share of total employment in 2009
India	86.1
Indonesia	62.1

Source: ILO (2010d, 2010e)

Only 9 percent of all workers are unionised in India, though 66,000 trade unions are registered in the country (Handique 2009). Since the Indian Supreme Court affirmed that trade unions do not have a guaranteed right to effective bargaining or right to strike (Laxmikanth 2010), this means that most workers currently rely solely on protections granted to them under the law. Yet most of the country's workforce is not covered by national labour laws; laws relating to social security or work conditions only apply to firms with at least 10 or 20 workers, and laws relating to terms of employment and procedures for disciplinary action and layoff compensation only apply to larger firms, with 50 or 100 workers (Sankaran 2007). By simply tailoring their firm size, it is easy for employers to avoid being hampered by labour regulations.

Sundar notes that the Indian federal government "is under pressure to not effect labour reforms concerning the organised sector and at the same time design policies to ensure welfare of millions of workers in the informal economy" (Sundar 2010: 2). One response has been to shift most labour reforms from the federal government to state governments, since "the state governments are in a position to make its own labour laws on certain matters and make amendments

to central laws (owing to distribution of powers under the Constitution of India)" (ibid.). This means that different states in India have vastly different regulatory systems for labour.

Some states (such as Kerala) are known for intervening on behalf of informal sector workers (Waite 2001). Others do the opposite, relaxing labour inspection systems, exempting certain economic sectors from labour laws, or reclassifying certain occupations so that they fall outside the purview of existing labour laws (Sundar 2010). In Delhi, for example, unions were barred from the expansive construction site for the Commonwealth Games Village in 2009, as the administration feared unionisation could delay completion of the project (Handique 2009). Workers at that site were also rotated every two months so that labour laws could not be applied (ibid.). Without access to the construction workers, unionisation is nearly impossible in these locations, and it is clear that labour regulation is needed; a survey of more than 18,000 construction workers in the Delhi region showed that less than 10 percent of them earn the regional minimum wage (Handique 2009).

Indian trade unions have tried to pressure state and national authorities to improve the system of labour laws and enforcement of those laws. Also, in recognition that their main 'consumer' base (formal sector) was quickly eroding, the major trade unions began to reach out to informal sector workers in the 1980s (Sundar 2003). For example, in Orissa, the Building and Woodworkers International union formed self-help groups and cooperatives; in Bangalore and Hyderabad, the Union Network International offered information technology training (Ahn 2008). Other plans aimed "to create organising units in the union federation for informal sector workers … [to extend] legal aid to informal sector workers … [and to] organise various forms of public demonstrations to sensitise the societal agencies about the problems of [informal] workers" (Sundar 2003: 7). While not all efforts were successful, membership in traditional trade unions doubled in India in the early 2000s, primarily due to the increasing unionisation of informal agricultural and rural workers (Sundar 2010: 4).

One might argue that non-traditional unions (such as those focused primarily on informal workers) have been even more successful at pressuring Indian policymakers for change, with SEWA (Self-Employed Women's Association) playing the strongest role. SEWA's roots can be traced to the Textile Labour Association (TLA), the largest and oldest union of textile workers in India. The TLA formulated a 'women's wing' in 1954, and by the late-1960s, TLA had developed training programs for the wives and daughters of mill workers, focusing on embroidery, weaving, and typing, among other activities (SEWA 2009b). In the early 1970s, Ela Bhatt - an attorney and the head of the Women's wing of TLA - learned of a survey probing the exploitation of women workers, revealing "the large numbers [of workers] untouched by unionisation government legislation and policies" (SEWA 2009a). After visiting groups of female cart-pullers, head-loaders and used-garment-sellers and hearing their stories, Bhatt founded SEWA in 1971 in response to appeals from the women (SEWA 2009a).

It was a struggle for the workers' association to gain status in India as a trade union; "the Labour Department refused to register SEWA because they felt that since there was no recognised employer, the workers would have no one to struggle against" (SEWA 2009a). However, persistence paid off and in 1972 SEWA was recognised as a trade union. In 1973 the organisation had 370 members, but membership grew quickly since there were so many workers unrepresented by traditional trade unions such as TLA. While the divergence of interests of formal and informal sector workers led SEWA to an acrimonious split from TLA in the 1980s, this spurred even more growth for SEWA, as the organisation was able to create its own 'brand' of organising.

SEWA's early struggles for higher wages were largely unsuccessful since there were few jobs but a seemingly unlimited supply of individuals wanting to work; this led to a strategy shift, wherein SEWA focused on developing more employment opportunities for rural workers as well as supporting "long-term, structural and social changes needed to seriously change women's lives" (Rose 1992: 22; see also Wakai 1994).

With this multidimensional approach SEWA has been successful on many fronts, particularly in terms of cultivating and supporting a collective identity among its members. It organises a wide variety of occupations, from home-based workers to vendors, from service providers to farmers (ibid.). It has successfully blurred class identification, organising "both self-employed women (part of the petty bourgeoisie) and wage-worker women (part of the working class)" (Selcuk 2005: 4). It has even overcome religious differences (members come from a variety of minority groups with different beliefs) by promoting rehabilitation, education, and "mutual helping" among members since most are discriminated against in some way (Marshall 2010). These achievements should not be understated since the caste system in India still plays a major role in determining the division of labour within the society; among other things, this restricts mobility for workers within the informal sector and influences the interaction among workers from different castes (United Nations Development Programme 2009).

SEWA's success in bringing such disparate individuals together can be linked to three factors. First, the organisation focuses on women (a highly marginalised worker group). Ninety four percent of the female labour force in India works in the informal sector (SEWA 2009b), and many studies show that targeting women for assistance brings the largest positive feedback effects for the family and community (Padgett and Warnecke 2010). Second, the organisation emphasises self-reliance and community-building; this enables individuals to connect by developing locally-run and sustainable provision of services, rather than remaining isolated and relying solely on external assistance. Finally, SEWA approaches organisation holistically, "linking different levels, organising, building skills, developing institutions that serve the poor, bringing the resources of modern knowledge to bear, focusing on systems, and finding the kinds of partners and partnerships that can allow members to move forward" (Marshall 2010: 2).

The organisation is now the largest union in India, with 1.2 million female members; as it has grown, it has increased the variety of services it provides to attract a diverse body of informal labourers (Marshall 2010). In its home state of Gujarat, SEWA is associated with a host of cooperatives, rural producers' groups, and social security organisations (see Table 3), in addition to a plethora of microfinance and microcredit groups to serve members' financial and credit needs.

Table 3. SEWA service networks in Gujarat

Type of Organisation	Number of Organisations and Number of Members per Organisation
Cooperatives	
Dairy cooperatives	53 with 5,182 members
Artisan cooperatives	10 with 1,200 members
Service and Labour cooperatives	10 with 130,000 members
Land-based cooperatives	7 with 192 members
Rural Producers' Groups	
Craft-based groups	142 with 2,106 members
Land-based groups	21 with 395 members
Forest producers based groups	11 with 220 members
Food, grain and essential items distribution groups	10 with 120 members
Nursery-raising groups	7 with 140 members
Social Security	
Health and/or child care organisations	6 with 7,207 members, reaching 117,119 SEWA members and their families

Source: SEWA (2009c)

SEWA has also taken networking to a new level; it helped to create international networks like WIEGO (Women in Informal Employment Globalizing and Organising) and played an important role in the ILO adoption of the Home Work Convention in 1996, which promoted the equality of treatment of home workers with other wage earners, in terms of remuneration, maternity protection, work safety, right to organise, and many other benefits (Sundar 2010; ILO 1996). SEWA has also been instrumental in the creation of StreetNet (an international network of national street vendor organisations) and the National Alliance of Street Vendors of India; the group's lobbying played a major role in the Indian government's 2009 revision of the National Policy for Street Vendors (Sundar 2010). All of these successes can be traced to SEWA's ability - honed over time - to redefine the term 'worker' in India.

Similar to the Indian case, Indonesia's trade union movement in recent years has shown significant growth. In Indonesia, however, this can be linked to the fall of Suharto's regime in 1998. During Suharto's reign, only one trade union federation was permitted, with strict regulation by the government. In many cases, union members did not bargain with employers but simply begged. However, with the collapse of the dictatorship, the right to organise freely and openly was restored (van Klaveren et al. 2010). The resulting trend toward democratisation then enabled the number of trade unions to expand from one large umbrella organisation under state control to over 80 private unions, as of 2004 (ICTUR 2004)[2].

However, unions must continue to fight for fair representation and recognition by Indonesia's reformed government. The new unions initially began as underground organisations that focused on social rights (e.g. freedom of speech) and freedom to organise (wherever, whenever), attracting mass support from a loyal following of informal workers. As these unions expanded their objectives to include economic and social equality in the workplace, the newly democratic Indonesia attempted to meet these pressing demands by ratifying ILO labour regulations and incorporating them as government mandated laws. Nonetheless, these changes remained ineffective as they largely targeted formal sector workers, disillusioning informal workers and causing their union membership to decline (Social Alert 2003:15).

Older trade unions - those existing before 1998 - focus on traditional, more formal styles of bargaining by colluding with employers. Their main purpose is not necessarily for socio-economic equality but simply to gain the ability to collectively bargain. While initially these older unions were solely comprised of formal workers, they extended membership to a large percentage of informal workers after democratisation took place, assuming that increases in numbers would garner greater negotiating potential. Older unions are also favoured

2. ICTUR stands for International Centre for Trade Union Rights.

by authorities, who appreciate the unions' "personal links with vested interest groups" (such as the Ministry of Manpower), alliances with employers, and connections to security forces; this enables the older unions to be "very good at discrediting the new unions" (Social Alert 2003:17). Such factors ensure that older unions' demands are ranked higher than those of the newer, more liberal thinking ones.

Instead of working together toward a common goal, the new and old organisations force their members to compete against one another for the same jobs and positions. Such infighting propagates the notion that trade unions are, in and of themselves, ineffective, keeping many informal workers from becoming members and thus organising in the first place. The actual percentage of workers affiliated with unions remains low, with some 3.4 million workers unionised constituting a mere 4 percent of the total workforce and 14 percent of the formal work sector (ITUC 2007:3)[3].

Although these numbers seem debilitating, changes in the laws surrounding unions instill hope. Indonesia has ratified all ILO core conventions and has committed to changing all standing laws that contradict ILO statements. The Indonesian government's chief focus has been on the Worker's Union / Labour Act (No. 21 of 2000), the Manpower Act (No. 13 of 2003) and the Industrial Dispute Settlement Act (No. 2 of 2004). The Trade Union Act allows workers from the private sector to organise, but trade unions must have a minimum of ten members and must register with the Ministry of Manpower in order to be officially recognised by the government as a legitimate confederation (ITUC 2007:5).

Unions do maintain the right to collective bargaining, but union leaders must first recruit or receive support from more than 50 percent of the total workforce in that specific sector of the economy (ITUC 2007:5). The government's Manpower Act affirms workers' right to strike, but only under a restricted set of conditions. More often than not, strikes lend themselves to violence, giving employers the opportunity to intervene using the military or police forces in an attempt to quell all forms of resistance (ITUC 2007:6). Informal sector union members thus lose credibility as a respectable group worth bargaining with and are instead showcased as violent extremists with unrealistic demands.

Although discouraging unions from collectively bargaining is legally subject to a fine or even imprisonment, in reality this ia often not enforced. Like their Indian counterparts, Indonesian employers often discriminate against union workers and simply ignore standard legal procedures for hiring. While the unions may take their case to courts to be heard and tried, the process is lengthy in Indonesia,

3. ITUC stands for International Trade Union Confederation.

taking up to six years - assuming that small informal sector groups can afford to pay the fees charged by most lawyers and judges, who are often bribed by the employer to rule in the company's favour (Social Alert 2003:13). Consequently, when informal workers attempt to unionise they are terminated on the spot, being replaced by new low-skilled labourers resigning themselves to the tasks at hand, no matter the pay.

The Industrial Relations Dispute Settlement Act of 2004 attempted to remedy such corrupt practices rampant in the judicial system by creating a bipartite system for negotiation. As of 2006, union leaders from the informal sector and company heads are required to first attempt to reach an agreement on their own accord. If this process fails, a mediator is brought in to act as an intermediary. Ultimately, the dispute may be brought before the Industrial Relations Court with a verdict given within 50 days (ITUC 2007:6). However, even when union demands are granted via a court-ordered sentencing, a common practice is for employers to simply declare bankruptcy. In doing so, the company itself is dissolved and then reformed a few days later under a newly registered name. This in turn ensures that informal workers' rights, while granted in court, are simply circumvented in practice (ITUC 2007:7).

The Indonesian government has proved effective at being the first Southeast Asian country to successfully ratify all ILO conventions, yet the international trade union community along with the International Monetary Fund (IMF) encourage stricter adherence to these changes. It is the role of the State to not only mandate new laws, but also ensure they are being enforced. In doing so, the IMF along with NGOs have promised to keep a steady stream of foreign investment flowing into Indonesia to spur economic development, especially for the informal sector (ICTUR 2004).

One way that NGOs help to organise the informal sector is by funneling capital into Indonesia through a proven method of small, community-based micro-lending institutions (World Bank 2001). These services are crucial for informal workers, given that 88 percent of Indonesia's workforce relies on some form of capital loans in order to meet daily family and work demands (Social Alert 2003: 10). In gaining access to resources (as well as proper training on using those resources effectively and efficiently), individuals are able to identify with one another and in turn collectively increase awareness about their specific needs and goals. While the Indonesian government initially branded NGOs as foreign "watchdogs" and expressed concern over their ability to organise informal sector labourers, policymakers have since changed their view (Antlov *et al*. 2005).

In seeing the effectiveness of microfinance initiatives, the Indonesian government attempted to support the informal sector with its own National Bank (Bank RI) and the Social Credit Bank (Bank Perkreditan Rakyat); however, poor management practices and high expenses linked to corruption and legal restrictions caused the system to buckle.

Apart from their role in micro-lending, though, NGOs remain influential by raising awareness of the injustices associated with informal labour practices. NGOs have been particularly helpful for Indonesian home-based workers, most of whom are women; the average earnings of home-based workers are lower than any other (paid) informal worker group (Chen 2003). In Indonesia, 42 NGOs collaborate with MWPRI[4] (the National Network of Friends of Women Homeworkers), altogether serving more than 19,000 homeworkers in nine provinces (Pineda Onofreo 2007). Approximately two-thirds of these homeworkers are subcontracted, with the remainder being self-employed (ibid.).

Founded in 1999, MWPRI aims "towards a better life for the women home-based workers…which is humane, just, gender-sensitive, and progressive" (ibid.). Specifically, the organisation aspires to offer social protection comparable to what those in standard (formal) wage employment positions receive (MWPRI 2008). While in 2004 the Indonesian Parliament approved a National Social Security System Law, the law did not include detailed provisions for transitioning to this system (ILO 2008). Implementation and enforcement have thus been lacking so home-based workers (along with many other groups) have not received any benefits. While MWPRI continues to pressure the government on this matter, the network has also developed indigenous social protection schemes offering health, savings and loan services (Pineda Onofreo 2007).

MWPRI's work is facilitated by its linkages with Homenet, a transnational network of NGOs focusing on the social welfare of home-based workers. Homenet "is able to provide local homeworker unions with links to global organising"—including advocacy within ASEAN, the Association of Southeast Asian Nations (Hale 2004:159; see also HomeNet Southeast Asia 2010). The organisation has been known to intervene on legal matters as well. While homeworkers are not technically mentioned in the new laws introduced as part of Indonesia's recent ratification of the ILO declarations, Homenet Indonesia "claims that these laws can be interpreted to cover the workers or labourers in the putting out system" (MWPRI 2008). Accordingly, the organisation rallies around government declarations and ensures informal workers are up to date on recent changes in regulations. In this way, MWPRI is able to effectively combat injustices against women workers in the informal sector.

Ultimately, the organisation has been able to promote the visibility of female home-based workers, encourage the establishment and collaboration of local unions[5], and foster belief in the emancipation of female workers as powerful and contributory Indonesian citizens. Most of this is mainly attributable to MWPRI's collaborative efforts with governmental organisations, international activists, academicians, and NGOs - all in the hopes of encouraging a united front in the fight against home-based worker injustices.

4. MWPRI stands for Mitra Wanita Pekeria Rumahan Indonesia.
5. MWPRI played a major role in establishing an independent association of female homeworkers in Indonesia (Himpunan Wanita Pekerja Rumahan Indonesia, also known as HWPRI).

DISCUSSION

While the process of organising informal workers faces an array of barriers, the potential benefits from overcoming these obstacles far outweigh the costs. By tapping into the strength of numbers, organising can diminish day-to-day vulnerability for the majority of workers around the globe. This empowers individuals to bring about positive changes in their lives and those of their families.

While most informal labourers experience similar barriers to organising, it should be noted that country-specific factors such as political history, cultural norms, and economic and political structure influence the entire organisational process. Such was the case with our exploratory analysis of India and Indonesia, where India's lingering caste system and Indonesia's recent democratisation played a large role in dictating how informal workers effectively organised and communicated with one another. It is crucial to think about a country's individual characteristics in order to implement appropriate and relatable methods of surpassing organisational barriers. Because of this, it becomes difficult to make broad, sweeping claims regarding "proven" methods associated with overcoming these barriers and successfully uniting groups of people.

Although there is not a one-size-fits-all approach to organising informal workers, we did observe general trends for empowering those within the informal sector. For example, successful organisation of the informal sector requires an external program in addition to an internal one (Global Labour Institute 1999). To accomplish this, networks at multiple levels - local, national, and international - need to be utilised to their fullest capacity in order to ensure that informal sector workers not only recognise themselves, but also are recognised by others.

In focusing internally and locally, communities need to come together to begin the process of identifying their fellow informal workers and exchanging information. In doing so, these groups are able to unite on the principle of commonality of circumstance and thus make a stand to gain the attention of national policymakers who have all but forgotten about this sector of the economy.

In amassing large numbers of people, these collectives court both internal national attention and external international organisations. Informal workers thus raise awareness and spur the international community to act on their behalf in their struggle for socio-economic justice. Often times, external NGOs not only have access to capital funding but can promote the upholding of ILO declarations in all countries that operate and trade in international markets.

This two-pronged approach grants informal sector workers a heightened degree of bargaining power in terms of affecting change within their respective countries. The national government, feeling compelled not only by its citizens but also by international organisations, feels pressured (at least) to acknowledge the issue facing the 'invisible' sector of its economy or (at most) ratify laws that align with ILO core conventions. It is also crucial that the national government, not merely state-run legislatures, uphold these regulations to ensure that the laws manifest universally across the entire citizenry. This promotes the centralisation of labour lawmaking and further develops enforcement capacity within the informal sector. Such measures also facilitate the organising process, enabling informal workers to become a recognised entity with certifiable claims toward socio-economic welfare - which many of their formal sector counterparts already enjoy.

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CHALLENGES FACING MUSLIM WOMAN ENTREPRENEURS IN THE HOSPITALITY AND TOURISM INDUSTRY IN MALAYSIA

ABSTRACT

This qualitative study looks at the challenges, issues as well as the business strategies adopted by the Muslim woman entrepreneurs who either own or manage the hospitality and tourism business in Malaysia. The questions asked were: (1) What are the challenges and issues faced in their day-to-day operations of the hotels/tourism business? (2) What are their business strategies in facing the stiffer competition from bigger names in the hospitality and tourism industry? The findings show a few commonality areas among these Muslim woman entrepreneurs. They believe that they are not badly affected by the influx of international chains. Rather than becoming victims to globalisation, they have come up with creative responses to the onslaught of the MNCs by providing complementary roles and having a different target market. Findings also suggest that they hold strong Islamic values which they instil in their day-to-day operations. They operate in an Islamic manner by providing Halal food and services, hence contributing to the development of "Halal hospitality". This new market niche and a unique market positioning strategy may very well cushion the impact of the current economic slowdown and may be replicated to enhance women's participation in small businesses in many Muslim communities the world over.

INTRODUCTION

The growing number of women in businesses has become a worldwide phenomenon. In Malaysia, the involvement of women, especially Muslim women, particularly in the hospitality and tourism industry, is not being studied thoroughly and systematically. Research conducted in the 1980s identified challenges specific to female entrepreneurs and these include difficulties in obtaining start-up funds, financial management and development of effective marketing and advertising. Financial barriers remained a key problem for women wanting to establish and grow their businesses. Major barriers to woman entrepreneurship include lack of access to (i) credit; (ii) formal business and social networks; (iii) opportunities to gain management experience and exposure; as well as (iv) the limitations of combining household and family care responsibilities with those running the enterprises, all of which could lead to negative impacts on the growth of woman entrepreneurs in the development of SMEs in Malaysia.

This research was conducted via in-depth and face-to-face interviews with 12 selected Muslim woman business owners or managers in the hospitality and tourism industry in the areas of Penang, Negeri Sembilan, Melaka and Johor. An open-ended structured questionnaire was used to conduct the interviews to enable the researcher to compare and contrast each component of the issues. Interviews, observations, and archival document studies, being the most popular qualitative research methods, were used in this study. Detailed data was gathered through open ended semi-structured questions that provided direct quotations from the respondents and through corroboration. It helped the researchers to increase their understanding of the probability that their findings would be seen as credible or worthy of consideration by others (Stainback & Stainback, 1988). All interviews had taken place at the owners' properties, thus the respondents felt very comfortable, secured and at ease to speak openly about their point of view.

Background

A 'new tourism' has emerged in the developed and industrialised countries resulting from a series of developments in the world economy, socio economic changes, technological revolution and innovation processes and new management practices. The new tourism is giving rise to sustainable and a more responsible tourism and basically refers to diversification and market segmentation and developing new market niche. Market segmentation as seen in ecotourism, cultural tourism, cruise tourism, education tourism, medical tourism, spa and wellness tourism, sports tourism, religious tourism, adventure and nature tourism, theme park tourism and rural tourism, are increasingly on the rise and becoming more popular amongst travellers in this age. Today, the new-age consumers are influencing the pace and future direction of the industry. They are more experienced and 'seasoned' travellers who would demand for a better quality and value-add holiday experience as well as 'customised

holidays'. So the creation and exploitation of niche markets as such have proven to be a good source of revenue within this new tourism, suggesting that further diversification and customisation or 'personalised niche market' can be expected in the years to come.

According to the Malaysian Tourism Promotion Board, if the trend of growth for all tourist groups continue in Malaysia, an overall growth of 14 percent per year can be expected and this could mean that the total tourist spending would reach about RM80 million in 2012. However, the long-term success of the tourism industry in Malaysia hinges on the country's ability to develop sustainable tourism that can attract repeat visitors. Currently in Asia, Malaysia leads the way with 68 percent increase in tourist arrivals and 70 percent increase in tourism receipts in 2010. Cheap and promotional airfares that are sometimes packaged with accommodation and meals especially offered by the low cost carriers and at times 'zero' fares promotion all gave rise to the amazingly significant increase of inbound travel to Malaysia. Meanwhile, domestic travel is also fast growing due to the cheap promotional accommodation and F&B prices especially during the school holidays and festive seasons. However, for any country to succeed long-term in this industry, it must develop the ability to sustain tourism and more importantly to attract repeat visitors.

In Malaysia, the tourism sector ranks second as a generator of foreign exchange after oil and gas production. This industry has been growing rapidly in the country over the past few years. Ecotourism is becoming the fastest growing form of tourism in Malaysia, currently making up about 10 per cent of the country's tourism revenue (Vasanth, 2005). A high fiscal commitment is also contributed by the Tourism Ministry for its development. For instance, a total of RM1,367 million was allocated for the development of the tourism industry during the Ninth Malaysia Plan [9 MP]. Malaysia has a wide range of natural assets that make tourism a highly beneficial and sustainable over the long-term.

Problem Statement

Globalisation has brought about a range of opportunities and challenges which have put additional pressures on SMEs. In addition to having to cope with the effects of globalisation, they need to adapt to new business conditions in terms of product positioning and product development facilitated by information technology. The potential for SMEs in achieving economies of scale is very limited and the use of computer reservation systems (CRSs) has not spread significantly in Malaysia among the SMEs. They are forced by market conditions to install new systems and train their staff to use tourism-related technology but find it difficult to invest in training or staff development, mainly because of limited investment resources and the fact that the many SMEs in the hotel, tourism and catering sector are managed by a generation of staff who have had no formal training in the sector. In a globalised market, these SMEs need to pursue new survival strategies.

The tourism industry in Malaysia also has to cope with the increasing problem of seasonality encountered by many coastal resorts. The competitive advantage then depends on their organisational competencies and capabilities. The new-age travellers are always looking for a different, unique, quality, value-added, flexible and customised vacations.

In addition, lack of professionalism and inadequate management and marketing skills, the absence of economies of scale and limited access to the necessary capital, human resources, marketing expertise and technology, over-reliance on a limited number of distribution partners and inadequate formal education or business training are among the other deficiencies which put them at a competitive disadvantage.

SMEs are highly reliant on existing distribution channels such as intermediaries like tour operators, travel agencies, travel information centres and tourist guides. It can be argued that the gradual reduction of SMEs' reliance on intermediaries will enable them to become more profitable, flexible and adaptable and to produce customised tourism products in order to satisfy niche markets. This will also require a rethink of all strategies and operational practices with regard to SME development, as well as development of entrepreneur's managerial skills and professionalism, training in marketing and management and on the use of information technology.

Research Objectives

The objectives of this study are:

- To identify the challenges and issues faced by Muslim woman entrepreneurs in this industry with the growth of globalisation.
- To find out their business strategies in facing the increasing challenges of the industry.
- To provide recommendations to the relevant authorities in improving and developing further the Muslim women entrepreneurship in the hospitality and tourism industry in Malaysia.

Scope of Study

This study was limited to specific areas which are popular tourist destinations in the Northern (Penang), Central (Negeri Sembilan and Melaka), and Southern (Johor) – parts of Malaysia where woman business owners in the hospitality and tourism industry were identified and located. Data on woman business owners in this economic sector is scarce and due to its small number, therefore, the scope of this study was constrained to the mentioned areas.

LITERATURE REVIEW

According to the Secretary-General of the Association of Southeast Asian Nations (ASEAN) Development Blueprint for SMEs (2004-2014), SMEs employ about 75-90 percent of the domestic workforce, especially adult persons and women (Lim, 2008). These enterprises play strategic roles in private sector development, especially in the aftermath of the 1997 Asian Financial Crisis. In some member countries, as their economies modernise or industrialise, SME provide the much-needed inter-firm linkages required to support LEs to ensure that they remain competitive in the world markets. In this region as well as in East Asia (e.g. China and South Korea), the total number of SMEs account, on average, for more than 99 percent. SMEs' contribution to total value added or gross domestic product (GDP), on the other hand, are much smaller than their share in total employment. This is indeed a general characteristic of SMEs in developing countries, his also a potential tool of poverty alleviation by creating self-employment avenues. In Southeast Asian countries alone (Indonesia, Malaysia, Thailand, Singapore, the Philippines, Brunei Darussalam, Laos, Cambodia, Vietnam, and Myanmar), by combining all sources which are available (Tambunan, 2008; Wattanapruttipaisan, 2003; Lim, 2008) there is an estimated total of around 52 million SMEs, with Indonesia as the largest contributor.

Malaysian woman entrepreneurs are increasingly recognised to play an important role to the unprecedented rate of growth of the SMEs and indirectly to the Malaysian economy. The number of women in Malaysian SMEs in 2003 was 1,122,000, or 36.8 percent of the total employment in SMEs. A proxy for woman entrepreneurs obtained from Population Census in 2000 indicates that 30 percent of them are working proprietors and active business partners. It is not surprising that the number of woman entrepreneurs in Malaysia has increased in the past three decades due to the emphasis on industrialisation, and growing interests in privatisation, self-employment and business-oriented employment. All of these have been facilitated by the growth in various sectors such as banking and financing, food manufacturing, general trading, personal and public services, education, training and consultancy, and others. Malaysian women have been involved in various enterprises that were formerly male-dominated. According to The Department of Statistics of Malaysia, there were 518,000 companies involved in services, manufacturing and agricultural sectors, of which 99.1 percent were SMEs. About 16 percent were women-owned companies with 89.5 percent involved in the services sector, 7.5 percent in manufacturing and 3 percent in the agricultural sector.

Issues in Women Entrepreneurship

Researchers have made attempts to distinguish an entrepreneur from a bread-winning businessperson. They consider an individual to be an entrepreneur if he/she exhibits a high propensity for growth. They view growth propensity as one's desire to grow and change in future as well as his/her self-perceived power to achieve the same. As such, size and growth are typically used as criteria for evaluating organisational success. Women, however, conceive their businesses differently from the way men do. Women have different socialisation experience which might shape varied strategic choices among themselves such as their prior professional experience and social network affiliation. This leads to different approaches to venture creation and business growth expectancies. Some studies show that women-owned businesses are no more likely to fail than men-owned. Cliff and Fasci and Valdez, however, reported that women perform less well on quantitative measures such as job creation, sales turnover and profitability since women do not enter business for financial gain but to pursue intrinsic goals (for example, independence, and the flexibility to run business and domestic lives). Implicitly, women are deemed to assess success in relation to their achievement in attaining personal goals (i.e. self-fulfilment, goal attainment etc.). Other researches found that differences in initial capital and goals explain the poorer performance in growth and survival of women-owned businesses.

While businesses need more women in order to capture the full benefit of diverse thinking and problem solving, decisions making and managing strategies, some significant barriers especially financial barriers remain for women in establishing and growing businesses. Some of the difficulties included obtaining start-up funds, financial management and development of effective marketing and advertising. The root causes of limited financial success were often attributed to early management practices of the woman entrepreneurs. Female owners tended to prefer internal to external sources of financing. In addition, women used smaller amount of capital at the start-up phase and that they are less likely to use financial instruments such as overdrafts, bank loans, and supplier credit. Indeed, women were more likely to use their banks for a source of advice, but men were more likely to respond to that advice. Specifically, women-led businesses that used bank loans as a primary source of start-up capital outperformed those that used alternative funding sources. Therefore, Haynes and Helms stressed the importance of having a relationship with a bank in place at the time of the business launch. This is because having access to financial resources and emphasising the financial aspects of the business had stronger effects on growth than did intention or choice.

But one of the biggest obstacles facing woman entrepreneurs is the discrimination they suffer from the banking and finance communities. So they prefer to rely on their own personal funds. In Malaysia, many woman entrepreneurs feel that there is a huge barrier for them to obtain capital at banks and lending agencies. It is therefore crucial for the government agencies, banks and lending agencies and women associations especially Women SME Association of Malaysia (WSME) to assist these entrepreneurs in terms of their credit access.

Social network

Networks have long been hailed as essential to the survival of female-run establishments. It is a critical element for entrepreneurs in gaining access to capital/loans, advice and information needed for initiating and operating a new venture easily. Entrepreneurs make use of social relations and contacts as channels to gain access to information, customers, suppliers, and to the sources of finance. They make use of family networks to access unpaid family work as well as emotional support. Support from personal network improves survival and growth chances of new ventures. Specifically, support from strong ties (spouse/life partner, parents, friends and relatives) is more important than from weak ties (business collabourators, acquaintances, former employers and former co-workers) which influence the success of new ventures. Besides, active help and emotional support from spouse is more important for success in case of the woman entrepreneurs.

Men and women, however, have different priorities in establishing networking relationships. Men's motives are often more instrumental (seeking personal gain) while women have more affective considerations in social relationships. Their management style is not seen as being relevant and thus, women are often excluded from the male networks which are very effective. Women do not have the same tools, assets, and chances than men in the small business arena. This phenomenon seems to be applicable to Malaysian woman entrepreneurs. Woman entrepreneurs faced a shortage of peer support networks compared with men although various woman entrepreneurs and industry associations have been formed (i.e. FEM, NAWEM, USAHANITA) which generally serve as a platform for these entrepreneurs to establish networks and exchange information and experiences as well as to conduct training programmes, seminars and workshops on motivation, leadership and entrepreneur development and to provide other means of support. This is due to the fact that women may not join these associations as they might be overloaded with business and family responsibilities. This limits their ability to seek informal advice and peer-financing as well as the information networks needed for survival and growth. This might pose a challenge to woman entrepreneurs in establishing networks which are helpful to the survival of their businesses.

Education, Training and Counselling

The combined impact of globalisation, changing patterns of trade, and evolving technologies such as ICT, call for skills that woman entrepreneurs do not for a large part possess, as many more women than men lack the requisite level of education and training, including business and technical skills and entrepreneurship training. Nevertheless, women are often disadvantaged in terms of access to training. They are often unaware of training opportunities and are less likely to be able to afford the cost of training provided by the private sector (and subsidisation of training is limited by the willingness of donors to support this).

According to the International Labour Office, African Development Bank and Private Sector Department, even if women could afford to pay for training, they have difficulty in travelling to central locations to participate in training programmes, and quite often cannot afford time away from their enterprises and family responsibilities to attend weeklong programmes – even assuming their husbands give them permission to be away from home. In fact, some husbands often object to training offered by men in certain countries. In addition, most entrepreneurship training programmes are too general in scope and do not offer a growth strategy orientation. Many of them focused on the start-up process with very limited effort on the part of the training providers with regard to doing any post-training follow-up. In addition, women tend not to use supporting government programmes including the training programmes provided. This might be a problem pertinent to Malaysian woman entrepreneurs as generally there is a lack of entrepreneurship training and skills development in Malaysia, where most woman entrepreneurs acquired their skills and experience through their family members, friends and previous experiences. Efforts are therefore needed to increase the level of awareness among these entrepreneurs of existing training opportunities.

Usage of ICT

The use of ICT is crucial and arguably unique in allowing small businesses and their entrepreneurial owners to sharpen their strategies in order to achieve success. The wide-reach of technology provides businesswomen with greater access to the market, networking opportunities, and greater promotional capabilities which will undoubtedly augment the competitive advantages for their businesses. However, most of the local SMEs do not have internal IT infrastructure installed in their premises such as the Local Area Network, and fewer than 20 percent of SMEs have access to the Internet. Besides, there exists a "digital gap" between urban and rural women and between women of different economic status even though the government and NGOs have jointly organised many training programmes and seminars on ICT. Between 1995 to 2000, about 10,000 women benefited from these courses which are relatively few compared to the population of female entrepreneurs in Malaysia. This problem should be addressed by policy, particularly policy aimed at providing entrepreneurial skills to women.

The travel and tourism industry has grown globally by 500 percent in the last 25 years. It is estimated that by the year 2020 there will be 1.6 billion annual international tourist arrivals worldwide and collectively, they will spend USD2 trillion. More importantly, there is a major shift of travelling to the Asia Pacific region and Malaysia is still one of the 'hot' tourist destinations in this region. One of Malaysia's biggest revenues is from the tourist arrivals from the Middle East between the period of July to September every year coinciding with the school holidays. In 2007, about 200,000 Arab tourists visited Malaysia, a significant increase from the 147,646 in 2006. In light of this great potential to tap from the Arab tourists, the government must step up efforts to attract more arrivals into

Malaysia and the hospitality and tourism industry must be prepared to take on this great opportunity. If the trends of growth for all tourist groups continue, an overall growth of 14 percent per year can be expected and this could mean that the total tourist spending would reach about RM80 million in 2012.

In Malaysia, SMEs represent more than 90 percent of business establishments, 56 percent of total employment and 32 percent of GDP. A study conducted by Asia Pacific Economic Cooperation has divided the SMEs market into three main group: those who are already internationally competitive or able to become internationally competitive; those who are less likely to be able to adapt and are considered to be 'at risk'; and those that are insulated from the effects of globalisation, such as those providing services for the local market. There are over 50 percent of SMEs in the third category and about 20 percent to 30 percent in the second category whose current business model is not sustainable in the longer term. Malaysian hospitality and tourism industry is highly supported by the SMEs where women are also players in this field owning or operating hotels and accommodation, tour operations, travel agencies, entertainment and more so in the cottage industry.

Malaysian women are important contributors to the country's economic and social development and this can be seen in an increasing trend in the participation of women in the formal workforce and in a range of economic activities. The female labour force participation rate increased from 32 percent in 1957 (when Malaysia gained Independence) to 47 percent in 2000 but has remained relatively unchanged in the last 9 years. The changing attitudes of the family was one of the significant reasons which influenced more women participating in paid labour. (Don, 1993). However, most of the women were concentrated in the labour intensive operations, in the manufacturing sector. (Ariffin,1994). As Malaysia moves from labour intensive manufacturing to more capital intensive and high technological industrialisation, more women have gained employment and made strides into male dominated and more challenging sectors such as in the business arena. This has seen the increasing trend, though at a very slow rate with more woman entrepreneurs, especially among Muslim women entering the global playing field.

The number of women in Malaysian SMEs in 2003 was 1,122,000, or 36.8 percent of the total employment in SMEs. (Wendy & Siong, 2008). The Population Census in 2000 indicated that 30 percent of them are working proprietors and active business partners. Recognition of women as potential contributors has resulted in a major shift over the past 20 years towards women as a key target group for programmes using SME development, as a way to achieve wider economic development targets. Southeast Asia where Malaysia is part of has longer history in tourism development compared to other developing regions and is more integrated into world tourism circuits. But despite being a matured tourism destination which saw tremendous growth in the industry for the past three decades, there has been no comprehensive view of social, economic, cultural, environmental and political issues of processes and problems

associated with tourism development in Southeast Asia (Hitchcock, King and Pamwell 1993, Wall 1998). Analysis of women's experiences have been even more partial (Kindon 2001), despite increasing calls to recognise the gendered nature of tourism globally (Kinnaired and Hall 1994, Richter 1995, Wall 1996, Sinclair 1997).

Despite having a big potential in creating new market niches, small businesses in tourism often have problems in financing, fluctuations in demand, high staff turnover, capacity constraints, underdevelopment of infrastructure and facilities, and because of limited funds and low skills and knowledge levels are often badly positioned and fail to maximise their unique potential in the global market (Thomas and Augustyn 2007, Saprunova 2007). The findings from this study is evidence that further supports all the previous studies and literatures discussed in this chapter and thus, enhanced the significance of this study and put its findings to greater emphasis with the government agencies, ministries, NGOs and women business associations and other relevant stakeholders.

RESEARCH METHODOLOGY

The researchers decided on a conceptual framework to work on: (i) secondary desk research to examine previous research work done so that we could understand better the critical issues and to map out our questions for the primary research, (ii) primary field research which involved a small sample of 12 Muslim woman entrepreneurs in this industry. In this respect, the researchers chose an exploratory and a descriptive qualitative methodology which was most suitable and deemed appropriate for answering the research questions that had been identified. The reason why this methodology was chosen is due to the main strength of qualitative methodological approach in which the behaviours and interactions of the research subjects can be directly observed, and the respondents are encouraged to tell their own stories and reflect on their day-to-day experiences where such reflections have become very useful qualitative data for the researchers.

Samples

A total of 12 respondents were interviewed in the following regions:

- 3 in Desaru, Johor (Southern region)
- 1 in Johor Bahru, Johor (Southern region)
- 1 in Kota Tinggi, Johor (Southern region)
- 2 in Port Dickson, Negeri Sembilan (Central region)
- 2 in Melaka (Central region)
- 3 in Penang (Northern region)

All of the respondents are Muslim women and out of the 12 respondents, it is interesting to note that only 1 has a direct experience in the hospitality industry. The other 11 Muslim woman entrepreneurs entered into the hospitality and tourism business by 'chance' (Dass 2000. Refer to the Literature Review in Chapter 2). Because of their very deep passion and interest in the Hotel and Tourism business, the respondents ventured into it with great enthusiasm, belief and strong faith in God. Thus, the other 11 respondents have never worked or had any first-hand experience with the hospitality and tourism industry before. These respondents were leads given by the Tourism Malaysia office, Malaysia Tourism Action Council (MTPB now known as JPN), a few Women Business Associations, and referrals from the respondents themselves.

The profile of the 12 respondents is as follows:

- All 3 respondents in Desaru are married with children, aged between 35 to 50, with spouses as their full-time business partners. All 3 respondents are operating the beach front hotels/chalets on a management contract of 5 years from KEJORA.
- The 1 respondent in Johor Bahru is married with children, aged over 50, with a retired spouse from the military who is in full support and together with their oldest daughter, is assisting the respondent with the day-to-day operations. This respondent is operating and running a city hotel as a franchisee on a 5-year contract from the Government. She is the only respondent who has direct experience in the hospitality and tourism industry for 17 years prior to setting up her own hotel business as her parents used to own a resort on one of the beautiful islands in Johor and from her younger days, she has been helping her parents out at that island resort.
- The 1 respondent in Kota Tinggi, aged 50, is married with children, is running her own business (wholly-owned enterprise) in travel & tours specialising in Umrah and Haj packages for the Muslims. Her daughter is helping her full-time and her husband is in full support with the business and assists her on a part-time basis.
- The 2 respondents in Port Dickson, Negeri Sembilan, aged between 45 – 55, are married with children, and their husbands are their full-time business partners. One respondent together with her husband, are operating and running the beach Hotel on a franchise business with 5 years contract from the Government. The other respondent together with her military retiree husband are running and operating the beach front hotel as a wholly-owned enterprise now. They started this hotel business (a time-sharing apartment/ hotel on the beach front) as a management contractor from the Singaporean owner and gradually bought over the entire property from the owner. The owners are also opening another Hotel in downtown of Port Dickson soon.
- One respondent from Melaka, aged 45, is single, and running a city hotel in downtown of Melaka under a management contract from the Government. The other respondent from Melaka, aged 52, married with children, owns a Batik printing business using a very unique technique of dyes from fresh flowers, leaves and plants. She designs her own Batik and clothing line. Her husband is her full-time business partner.

- The 3 respondents in Penang are all married with children, aged between 35 to 48, with spouses in full support of their business. One respondent is running two (2) properties in Penang, one is a colonial-styled city hotel under a management contract from the Government, and the other is at a very strategic location nearby the University Sains Malaysia and Penang Airport where she wholly-owns it. On top of these two properties, she also wholly-owns another guest house property in Kulim, Kedah. The other one respondent is running and operating a cross between a Malay and a Balinese-styled Hotel on Batu Ferringhi Beach, also under a management contract from the Government. Her husband is the General Manager of a 4-star international hotel on Batu Ferringhi Beach. And she is the only Malay woman entrepreneur to operate and run a mid-sized hotel amidst all the other 3-5 star hotels/resorts on Ferringhi, where mostly are foreign players. And finally the last respondent from Penang (a Muslim Filipino but is a PR of Malaysia), married with 8 children, is running and operating a wholly-owned Guest House on the beach front of Batu Ferringhi Beach with her husband as a full-time business partner. Aside from owning the Guest House, they also own an Internet Café and a small car rental service for their guests on Batu Ferringhi Beach.

It is interesting to note that out of the 12 Muslim woman entrepreneurs, 7 are operating and managing beach front hotels, while 5 others are running and operating city/town hotels/businesses.

FINDINGS

The findings of this study are divided into two (2) themes - Weaknesses in the Hospitality and Tourism Business in Malaysia, and Business Strategies. However, in this paper, the researchers are only going to discuss one finding under the 'Challenges and Issues' and one more finding under the 'Business Strategies'.

Challenges and Issues

The question asked was *"What are the challenges and issues faced in their day-to-day operations of the hotels/tourism business?"*

(1) Taking-Over problems.

Eight out of the 12 Muslim woman entrepreneur respondents are running and operating their hotel/chalet business on a management contract basis (2 are hotel franchisees), 2 respondents are running and operating a wholly-owned hotel/guest house properties, 1 respondent is running and operating her wholly-owned travel and tours agency and finally the other 1 respondent is running and operating her wholly-owned Batik printing business. When the 9 woman entrepreneurs in the hotel business first took over the properties from the Government after the properties were handed over by the previous operators, either by way of management contracts or franchise agreement, they were faced

with the obvious challenge that the properties were in a pathetic state. The properties were poorly maintained with lots of wear and tear and damages and run-down facilities, furniture and fixtures. This was especially true for the beach front properties as the process of wear and tear and damages are greater due to (i) the salty air, (ii) the usage of facilities are greater and more 'heavy-duty' because these properties are frequent more by the holiday makers rather than business travellers, (iii) over-crowded number of guests who stay in one room at these properties because holiday makers usually travel in large families. As such, a few of the respondents had to spend between RM100,000 to RM200,000 for renovations and refurbishments which were conducted in a staggered manner over the period of their first to second year of their tenure.

One respondent from Johor Bahru said, *"taking over business from somebody is not easy because of bad stigma, old place was dirty, run down in terms of building, furniture, poor quality of food, staff was not motivated, no infrastructure, I had to re-do everything from re-training of staff to décor to preparing the menu and even cooking!". She further said, "I must turn this place from a blacklisted place to a place where people want to come and for that continuous job of upgrading is required."*

Another respondent from Desaru said, *"my biggest problem when I first started out this business was the renovation because this resort was in a really terrible shape when we took over. The renovation and refurbishment exercise took a lot of time and money of over 1 year but we did it in stages."*

Another respondent from Desaru said, *"the cleaning process of this place took us 6 months as this place was very dirty and unorganised when we took over."*

Another respondent from Desaru said, *"when we took over this place from Kejora, we put in a deposit of RM30 but had to spend RM200K for renovation and refurbishment."*

Another respondent from Penang said, *"I came here (to this hotel) and spent around RM1.8 million just to make it look good."*

Turn-over exercise had really posed a great challenge to them because they still had to operate the properties for cash turnover purposes, and at the same time to put back the properties in good and presentable order. Hence, in order to do both, they had to sell rooms and food & beverages (F&B) and concurrently closed certain sections for renovations and refurbishments. That gave rise to some inconvenience and discomfort problems to their guests. On top of that, as they were only having a small property of below 200 rooms (with the exception of the owners in Port Dickson and Johor Bahru where they have more than 200 rooms), they were also faced with the challenge of not being able to cope with the demands from the market due to insufficient rooms and facilities as a result from the temporary partial closure.

Moreover, being small operators, they were constantly faced with the challenge of insufficient funds, tight budget and small capital to roll into their businesses. Obviously, for these reasons, they had a lot of constraints in investing for renovation and refurbishment exercises. The wear and tear problems in their properties were greater compared to the others as theirs are located by the beach front and at the very least, the air conditions need to be serviced every six months (as mentioned by one respondent in Desaru, *"Beach resort has a very high maintenance, the air-conditioners must be serviced once in every 6 months"*.

Some of the other 'taking over' problems were:

- Bad image or bad stigma from the previous operator. They had to rebrand and reposition their properties and embark on an active publicity and promotional campaign to change the perceptions of the market about their properties. This exercise had caused them a lot of money. As mentioned by one respondent from Desaru, *"When we first took over from Kejora, we had to do a lot of repair works because Kejora didn't maintain this place well. We also changed the Resort's brand name and had to do rebranding exercise, changed logo, change name, did a lot of promos at Expos, tourism exhibitions, and marketing costs was high but we had to do it."*
- Dirty, smelly and infested facilities with roaches, rodents and ants, damaged building and run-down furniture and fixtures (cited by one respondent from Johor Bahru).
- 'Inherited' unmotivated staff who were demoralised, un-trained, lazy, having bad attitude, uncultured with 'kampong' mentality, and their spirits were very low from the previous operators. (Cited from one respondent from Desaru). She further commented, *"Main problem is the cleanliness of the Resort and many guests make their complaints and the staff are very lazy, has a 'kampong' attitude, like to gossip, not professional and the Malay culture is deeply rooted in them."*
- No modern and internationally standard facilities and infrastructure, especially true in Desaru as there is no internet accessibility. One respondent from Desaru said, *"One problem here is that we don't have internet service and some guests get disappointed."*
- Renovation and refurbishment exercises took a very long time and is a very costly affair. One respondent from Penang said, *"I had to spend about 1 year to make good this place and it cost me a lot of money. My advice is don't overdo (your renovation and refurbishment) as this isn't your own property."*

(2) Business strategies

The question asked was *"What are their business strategies in facing the stiffer competition from bigger names in the hospitality and tourism industry?"*

The respondents had shared one of their business strategies that had proved to work effectively especially during the economic trying times:

- Islamic management giving rise to Islamic tourism.

All the 12 respondents operate their hotels/resorts in an Islamic manner as they all hold very strong Islamic values and they embrace and instil these Islamic values in their day-to-day operations. They embrace honesty, integrity, and transparency in operating their business. They believe that the more Islamic values they adopt in their business and day-to-day operations, the more blessings and greater fortune Allah will grant upon them and the more they can share the good fortune and profits with their staff. They also commented that being Muslim business women, they must not be greedy as the industry is huge and it is more than enough for everyone to make a good living out of it. They do not condone to having a karaoke centre or pub or selling liquor in their resorts, including those giving accommodation to unmarried couples. They allow their female staff, including working at the public areas, to wear the head covers which is quite not the case with the other hotels/resorts that are run by non-Muslim management or owners. They frequently organise and host Islamic gatherings and activities for the staff to remind each other to stay close to Allah and to offer their thanks to the Al-Mighty. Their hotels/resorts serve 100 percent Halal food with the Halal certification. Thus, giving rise to Islamic tourism and creating a new market niche and successfully cushioning the impact of the current economic slowdown onto their business.

One respondent from Kota Tinggi said, *"I have always wanted to open up a business that is meaningful to me as a Muslim and so I chose to open up a tour agency focussing on Umrah and Haj packages and I practice giving all my clients a 'personalised' service."*

Another respondent from Port Dickson said, *"doing business must be transparent and following Islamic teachings. My staff are my asset. As a Muslim woman, I follow Islam and I practise honesty when dealing with customers. I work hard and Allah will help and I am not greedy in business. Also I am always truthful and transparent with my staff, if they are right I will compliment them, if my business makes more profits, I share them with all my staff because Islam teaches me to be so."*

Another respondent from Penang said, *"Islamic is very clean concept. I asked many of my non-Muslim guests locally and from overseas why do they like to come to our Hotel as we are an Islamic Hotel. They said they felt very safe here, no hanky panky, no disco, so they feel very comfortable". She added, "60 percent of my guests are foreigners, they come through internet booking, and when I asked what they think of my hotel that runs on Islamic values and we don't sell beer and liquor. They said that is not a concern as they are very happy here because our service is excellent and if they feel like drinking they will go to other parts of the Ferringhi Beach."*

Another respondent from Penang said, *"my business is 100 percent* Halal*, so that now people come here and go to the terrace to eat, they are not suspicious if this hotel is* Halal *or not. We don't serve liquor. Honestly, I tell you if the Muslims want to travel, they prefer to go to hotels that are owned by the Muslims because it is easier to eat and they are not worried if it's* Halal *or not." She added, "We don't serve any liquor or beer inside the hotel, but I do rent out a small space in front of the hotel to a Chinese operator who runs and operates a karaoke pub and when they pay me their rent, I make sure that I don't include that money to pay my staff's salaries."*

CONCLUSION

As mentioned earlier, capital, social networks affiliation, education, training and counselling, limitations of combining household and family care responsibilities and usage of ICT are important factors in influencing the growth of woman entrepreneurs in the development of SMEs in Malaysia. The other studies also suggested that Malaysian small business entrepreneurs rely heavily on personal savings including family funds or loans as their main source of initial capital and working capital. And the lack of collateral, guarantors, or the inability to furnish financial documents required by financing institutions are mostly the main reasons for that.

The 12 Muslim woman entrepreneurs surveyed are no different as they share the same limitations in all those mentioned areas. However, these Muslim businesswomen must be acknowledged for playing critical roles in bringing their fresh and vibrant ideas and capabilities into their business strategies and enhancing the successful development of SMEs in the hospitality and tourism sector in Malaysia. Despite the challenges and constraints they have and are still facing, with such positive and strong-willed minds, they have brilliantly turned these challenges into opportunities in their business. And for them, Halal hospitality business is the answer to create that product differentiation and new market niche and positioning to cater to the unique market. They have produced a customised tourism product as a new survival business strategy, in order to satisfy niche markets and now more and more non-Muslims customers prefer Halal products and services, so much so that it has now become 'the in-thing'.

On top of creating a new market niche in the Halal hospitality business, they have also decided to position themselves in the industry by being and remaining small. In that way, they are not directly competing with the big boys in the industry, instead they are complementing the big players by offering cheaper alternative of accommodation especially to the budget conscious travellers, backpackers and long-stayers. At the same time, by being and remaining small, they are in the better position than the international and local big boys in providing and extending a warm and 'personalised' hospitality and value-added service to all their guests. This special bonding relationship with their guests will attract repeat guests and travellers to their hotels.

RECOMMENDATIONS

From this study, we have earmarked certain areas which the government and NGOs may want to address in order to develop further our Malaysian woman entrepreneurs, especially the Muslim woman entrepreneurs in the hospitality and tourism industry:

- Policy recommendations - the findings point out that financial assistance, networking, training, education and counselling, and to a certain extent the usage of ICT are quite lacking and is hampering the further growth and bigger success of these women entrepreneurs.
- Ministries as well as NGOs and Women Business Networks/Associations must organise social and business networking sessions and conduct more affordable training and development programmes to increase human and skill capacity among them.
- The government can also provide special assistance on a continuous basis on the financial perspective - they must be made to understand on the advantages of external sources of financing for their businesses. The government should increase grants allocation, or encourage more banks and micro institutions through tax incentives to provide a wider range of financial services with flexible terms and conditions, or encourage banks/financial institutions to expand their range of financing products and delivery mechanisms to the SMEs. Beside that, NGOs can also play some important roles in providing credit schemes to women entrepreneurs.
- Some form of incentives could be provided to the women entrepreneurs in developing their internal IT infrastructure, such as tax relief for equipments bought.

This study is a small part of an on-going bigger study on the Muslim woman entrepreneurs in the hospitality and tourism industry in Malaysia. There will be more findings along the way. But with some of the findings which we are highlighting in this paper, we hope that the relevant parties will be able to revisit some of the existing women entrepreneurial training and development programmes as well as policies and improvise them as time goes by to ensure the effectiveness of the programmes and policies so that Muslim woman entrepreneurs are able to propel their business to the next level. Obviously, for them to go to the next level, they need all the help and strong support from the government agencies, Ministries, NGOs and woman business associations at both state and federal levels.

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ENTREPRENEURSHIP AND DEVELOPMENT INSTITUTIONS IN NIGERIA: PROSPECTS AND CHALLENGES

ABSTRACT

This paper examines the prospects and challenges of entrepreneurship and development institutions in Nigeria. The paper is essentially conceptual but has been enriched with secondary data from researches conducted by the Business Environment and Enterprise Performance Surveys (BEEPS) and the findings of scholars of entrepreneurship in Africa and beyond. The paper examines the meaning of entrepreneurship, history of entrepreneurship in pre- and post-independent Nigeria, prospects of entrepreneurship to national development and employment creation. The paper also makes deliberate attempt to uncover plethora of problems and challenges affecting established and potential entrepreneurs in their genuine quest to develop entrepreneurship activities in Nigeria. The role of government legislations and its agencies coupled with support by the community-based NGOs, commercial banks, cooperative societies, investment clubs and micro-finance institution are also show-cased in the paper. The paper concludes clearly that support for SMEs in Nigeria is limited and quite inadequate and that there is the dire need for government and its relevant agencies to create enabling environment for entrepreneurship to thrive.

KEYWORDS

Entrepreneurship, Development and Employment Creation

INTRODUCTION

Entrepreneurship is not a new phenomenon in Nigeria, as the profile of the country encouraged entrepreneurial culture, attitude and behaviour. Nigeria is a Federation of thirty-six (36) States and a Federal Capital Territory in the heart of Abuja. It was under Colonial rule for years, until 1960 when it gained independence from Britain with pomp and pageantry. This largest black African nation has a population of approximately 140 million, by 2006 national census, 150 million by CIA fact book and more than 250 ethnic groups. It is the most populous country in Africa, accounting for about 47 percent of West Africa's population, with a growth rate of 2.4 percent per annum (Ukaejiofo, 2009). It is referred to as the giant of West Africa in that; one in every two West Africans is a Nigerian. The country's GDP is larger than that of all countries in the African continent with the exception of South Africa (Adaya, 1998).

Traditional entrepreneurship in pre-independent Nigeria started when people produced more products than they needed in the villages, as such; they had to exchange these surpluses with those who needed them within their immediate and neighbouring communities. The exchange of goods for goods or services was based on trade by barter initially, until commodity money was developed and used. Exchange encouraged specialisation among producers, and the communities came to realise that they can concentrate on the areas of production they are best fitted. Consequent on the above, the culture of entrepreneurship started (Nicks, 2008).

Early entrepreneurship in Nigeria was characterised by the simple production of essential products and agricultural produce. The producer (most often farmers and artisans) started with a small capital, most of which is sourced from personal savings and gifts from relatives. At inception, business was carried out through an exchange process called trade by barter, even before the advent of any form of money. This classical era as enunciated above, marked the beginning of entrepreneurship in all local communities within the enclave that later became Nigeria. Entrepreneurship development is therefore not a new phenomenon in Nigeria, as wrongly opined by scholars like Miranda Elizabeth. According to her, Nigeria does not have a large or very detailed history when it comes to entrepreneurship (Miranda, 2010). In fact, the Yoruba and Hausa ethnic groups are great entrepreneurs in pre- and post- independent Nigeria. The Ibo ethnic group particularly is recognised internationally for its culture of entrepreneurship and enterprise development (Dana, 1995).

Entrepreneurship also flourished among the major ethnic groups in Nigeria because of the availability of able-bodied men and women, who are often mobilised for specific community projects and programmes through informal process of recruitment or on a free-will arrangement by community leaders and constituted authorities. Those recruited through this informal medium for entrepreneurial activities comprises of skilled, unskilled, old, young, experienced

and inexperienced individuals of various age grades, gender statuses and tribal affiliations. This entrepreneurial and developmental engagement is prevalent in Yorubaland in western Nigeria, Hausaland in the northern Nigeria and among the Igbo people of eastern Nigeria.

Ananaba (1969) lends credence to the above assertion that:

"The economy of the various states which make up modern Nigeria was basically a subsistence economy and customs had established the practice that people serve their parents, village heads and the community without remuneration. On a given day, people went and work for a particular individual. Through the day, the man they serve was responsible for their food and drink. On another day, the man returned the service and it went on until everybody in the group was served."

The above statement typically explains the enterprising nature of Nigerians in the traditional communities prior to colonialism. It is therefore incorrect to say that entrepreneurship is recent and a modern practice. On this note the arrival of the colonial masters slowed down rather than developed Nigeria's entrepreneurship development.

One of the factors that slowed down entrepreneurship development is the value system brought about by formal education. For many decades, formal education has been the preserve of the privilege few in the country. With formal education, people had the opportunity of being employed in the civil service, because in those days the economy was large enough to absorb the educated into the prestigious occupation, usually referred to as "white collar jobs". As such, the system destroyed self-reliance, self-employment and entrepreneurial skills of Nigerians; they thus became permanently dependent on the colonial masters (Nicks, 2008).

Another factor that slowed down the pace of entrepreneurship development was competition between Nigerian and foreign entrepreneurs. The competitive cut-throat business strategy of the foreign entrepreneurs was against the moral standards established by the communities. The foreigners did not adhere to the theory of "live and let live". For instance, the United African Company (UAC) that was responsible for a substantial percentage of the import and export trade, had the policy of dealing directly with producers and refused to make use of the services of indigenous entrepreneurs. The refusal of the expatriates to utilise the services of local businessmen inhibited their expansion and acquisition of necessary skills and attitude. Because of this, many eventually folded up. Those that folded up built up resentment against business which became very demoralising to other prospective entrepreneurs. As a result, the flow of entrepreneurship in the country was slowed down (Nicks, 2008).

Modern entrepreneurship however started with the coming of the colonial masters who brought their merchandises and made Nigerians their middlemen and supplier-clients. The products traded during this golden period were gold, silver, sugar, cocoa, cotton, tobacco rum, and coffee and later sale of Black Slaves who are preferred to Red Indian slave. (Popovic, 1976).

In the modern times, the pace of growth of entrepreneurship has increased in leaps because people, tertiary institutions and government at all levels take great interest in entrepreneurship activity because of the immense benefits therein. This interest is evidenced in the increasing research on the subject, the increased number of courses in entrepreneurship development, and the increased coverage by the media on a daily basis of the challenges of cottage, small and medium scale enterprises. On account of encouraging entrepreneurial initiatives, the country has experienced exponential growth in the number of private firms. However, majority of these businesses are very small when their operations are measured in terms of capital, employment and revenues (Attahir and Minet, 2000).

CONCEPTUALISATION OF ENTREPRENEURSHIP

Literature that explores entrepreneurship in Nigeria is limited. It is therefore necessary to rely on materials from developed and developing countries in order to have a deep insight into the impact of entrepreneurship on socio-economic development.

The discussions on the term "entrepreneurship" are traceable to authors such as Richard Cantillon and Jean Baptiste Say; who attempted at different times gave economic definitions to the concept of entrepreneurship (Binks and Vale 1990, Phuc 2006, Kanothi, 2009). Other influential theorists in 20th century who have contributed immensely to the understanding of entrepreneurship and its role in economic development include Knight in 1921, Schumpeter in 1934, Leibenstein in 1968, Kirzner in 1973 and Baumol in 1990 (Minniti and Lévesque 2008, Kanothi, 2009). Their various definitions subsequently encouraged a wide range of comments and reactions on the concept of entrepreneurship in academic circle up till the contemporary periods.

Kanothi (2009) quoting Binks and Vale (1990) defined entrepreneurship as 'an unrehearsed combination of economic resources instigated by the uncertain prospect of temporary monopoly profit'. Entrepreneur is also the 'instigator of entrepreneurial events for so long as they occur'. These definitions represent the views of Joseph Schumpeter and Harvey Leibenstein (Kanothi, 2009).

Entrepreneurship also entails the act of risk-taking, innovation, arbitrage and co-ordination of factors of production in the creation of a new products or services for new and existing users in human society (Acs and Storey 2004, Minniti and Lévesque 2008, Naudé 2007, Kanothi, 2009). The deliverable of entrepreneurship is making or doing things differently; making or providing new products or services; or organising how the products are made or supplied.

According to Acs and Szerb (2007) entrepreneurship revolves around identification, realisation and commercialisation of the opportunities harnessed in the environment by starting a new firm. This is what Thornton (1999) describes as demand and supply perspectives of entrepreneurship discourse. Likewise an entrepreneur is the person who is innovative and coordinates other factors of production in the creation of new products or services for societal benefits and wellbeing (Kirzner 1997, Mcquaid 2002, Phuc 2006, Praagt and Cramer 2001). Whereas, Casson (1999) argues that the enviable skill of an entrepreneur is to make prompt judgmental decisions about the best allocation of the ever scarce resources with the view to maximising gains from the venture created.

OBJECTIVES OF ENTREPRENEURSHIP

According to Tijani-Alawiye (2004) entrepreneurship objective is to increase the supply of entrepreneurs or adding to the stock of existing small, medium and big enterprises available to a country by creating and promoting many capable entrepreneurs who can successfully run innovative enterprises, nurture and sustain their growth, with a view to achieving broad socio-economic development goals. Furthermore, Igbo (2005) is of the view that entrepreneurship objective is the creating, building and distributing something of value from practically nothing to individuals, groups, organisations and society. The process involves planning and organising small business ventures through the mobilisation of people and resources to meet their needs.

To Chigunta (2002) the thrust of entrepreneurship is the conscious attempt to create jobs for the unemployed, facilitating empowerment and economic dynamism in a rapidly globalising world. Furthermore, Garavan and O'Cinneide (1994) noted that the major objectives of entrepreneurship are to develop enterprising people and inculcate an attitude of self-reliance using appropriate learning processes. In other words, entrepreneurship development and training programmes are aimed at stimulating independent small business ownership or the development of opportunity-seeking managers within companies.

However, Shepherd and Douglas (1997) noted that the essence of entrepreneurship is the ability to envision and chart a course for a new business venture by combining information from the functional disciplines and from the external environment in the context of the extraordinary uncertainty and ambiguity which faces a new business venture. It then manifests itself in creative strategies, innovative tactics, uncanny perception of trends and market mood

changes and courageous leadership. Furthermore, 'entrepreneurship', when treated as 'enterprise-creation' helps develop new skills and experiences that can be applied to many other challenging areas in life.

The need for promoting entrepreneurship culture among the youth in all societies becomes imperative because of the sterling qualities of youthful population such as resourcefulness, initiative, drive, imagination, enthusiasm, zest, dash, ambition, energy, boldness, audacity and courage which are all valuable traits for entrepreneurship development (Schnurr and Newing, 1997). Failure to direct all these entrepreneurial traits to positive endeavours is responsible for the high wave of crimes, vandalism, gangsterism, kidnapping and militancy in Niger-Delta and other trouble spots in Nigeria (Raimi, 2010). Bennell (2000) also supported this assertion that governments, NGOs and international bodies seeking to improve youth livelihoods could best pursue their empowerment objective by tapping into the dynamism of young people and build on their strong spirit of risk-taking through entrepreneurship development.

Entrepreneurship has also led to employment generation, growth of the economy and sustainable development. The current number of colleges and universities offering small business management and entrepreneurship development programmes has grown from one university in 1947 to over 1600 in the 1990s (Solomon and Fernald, 1991; Solomon *et al.*, 1994; Solomon, *et al.,* 2002). White and Kenyon (2000) also found a 'flourishing youth enterprise culture' in the United Kingdom among young entrepreneurs aged 18-24 years.

A popular survey from Zambia shows that a quarter of the youths (precisely 25 percent) is self-employed and is owners of businesses (Chigunta, 2001). Most of these young people, especially younger youths, tend to be concentrated in marginal trading and service activities. These findings are supported by evidence from Ghana where a survey of small scale enterprises revealed that young people owned almost 40 percent of the enterprises (Osei *et al*., 1993).

Similar evidence from South Africa suggests that the probability of self-employment among young people rises with age (Chigunta, 2001). When Nigerians especially unemployed youths are mentored and provided the needed resources for starting business ventures, the illegal acts of hostage taking, kidnapping, bombing and vandalism would become less attractive.

The theoretical foundation for entrepreneurship is the psychological theories of entrepreneurship. According to the proponents of these theories, the internal attitude, ability to make good judgment and forecast the desired situation leads an individual or group to become successful entrepreneurs despite the avalanche environmental/ecological challenges. Specific strands of the psychological theories include David McClelland's psychological theories of entrepreneurship, otherwise called need for achievement theory (NAT). This psychological theory emphasised the relationship between need for achievement to economic development through entrepreneurial activities. He opined that "the presumed

mechanism by which an Achievement level translates itself into economic growth is the entrepreneurial class. If the Achievement level is high, there will presumable be more people who behave like entrepreneurs…" (Islam,1989; Raimi, 2010). According to McClelland, one would expect a relatively greater amount of entrepreneurship in a society if the average level of need achievement is relatively high. Nigerians have zeal for following ideas to success, but on account of lack of enabling environment, an average Nigerian is disillusioned and developed hatred for the state. The frustration manifests in the forms of armed robbery, gangsterism, kidnapping, vandalism, sabotage and violence, etc..

The second theory is Richard Cantillon and John Stuart Mill's psychological theory of entrepreneurship, otherwise called the "risk taking theory" (RTT). The theory considers entrepreneurship as a mentality to take moderate or calculated risk, because people taking a very big risk also have a great responsibility (Alam and Hossan, 2003; Raimi, 2010). This fact can be observed in the avalanche of misplaced risky undertakings of Nigerian youths in the forms of hostage taking, kidnapping, vandalism, bombing, cultism, sabotage etc. The traits of creativity, risk-loving, innovation, strategic thinking and constructive engagement against the government by discontented Nigerians could as well be directed to entrepreneurship development.

LEGAL FRAMEWORK FOR BUSINESS IN NIGERIA

All business enterprises (small, moderate or large) must statutorily be registered with the Registrar-General of the Corporate Affairs Commission (Registrar of Companies in Nigeria). Therefore, any investor, be it local or foreigner, planning to set up any type of business, either service-oriented or product-oriented, should take all steps necessary to obtain local incorporation of their companies, as this process would afford the investors many opportunities and incentives apart from the benefit of legality that incorporation confer.

Business activities may be undertaken under the following models:

- Private or Public limited liability company;
- Unlimited liability company;
- Company limited by guarantee;
- Foreign Company/Subsidiary of foreign company;
- Partnership/Firm;
- Sole Proprietorship; and
- Incorporated trustees and Representative office.

To formally register any of the above-mentioned business enterprises, the promoters must meet the provisions of Companies and Allied Matters Act (CAMA), 1990. The Companies and Allied Matters Act, 1990 is the principal law regulating the incorporation of businesses. The administration of the Companies Act is under-taken by the Corporate Affairs Commission (CAC) and its functions include:

- the regulation and supervision of the formation, incorporation, registration, management and winding up of companies.
- the maintenance of Companies Registry;
- the conduct of investigation into the affairs of any company in the interest of share-holders and the public.

PROSPECT OF ENTREPRENEURSHIP DEVELOPMENT

Small enterprises are the leading force in the development of African economies. They are essential for economic growth in many developing countries. Entrepreneurial activities such as innovation, risk bearing, employment creation, finding new opportunities and the commercialisation of their inventions have been contributed to the prosperity in all regions of the world (Ukaegbu, 2000; Chu, Kara and Benzing, 2008). Report indicates that even in Europe, the private sector organisations employs 60 percent of the workforce, thus, it is a vibrant creator of massive employment (Wintermantel, 1999, Chu et al., 2008). Similarly, Japan, an industrialised nation in the Asian continent has six million small-and medium-sized enterprises (SMEs) which account for 99.7 percent of all businesses subsisting in the country, and interestingly, these SMES absorbed 70 percent of the total labour force in Japan (Chu *et al.* 2008). Similarly in Taiwan, 96 percent of all functional small businesses are SMEs employing 78 percent of the nation's work force (Lin, 1988). In other survey conducted, it was reported that cottage, micro-firms and medium enterprises are vital but neglected sector of the economy; however, they are making significant contributions to Africa's economic growth. Ghanaian micro-enterprises employ less than 5 people, yet it proudly accounted for 70 percent of country's workforce. This confirms the vibrancy of SMEs as employment and income generators (Government of Ghana, 2003; World Bank, 2006). The prospect of SMEs as prime mover of the economy is visible in Kenya, where the private sector alone in 2003 employed 3.2 million people and contributed 18 percent to the nation's GDP (OECD, 2005). The impact of small businesses on the Nigerian economy is difficult to accurately measure, but it is believed to be highly dynamic and promising. It has been estimated that between 45 and 60 percent of the urban labour force work for private enterprises (Chu et al., 2008). Ariyo (2005) like other scholars across Africa, reported that in Nigeria, the private sector provides 50 percent of the country's employment and 50 percent of its industrial output. On the strength of the plethora of evidences presented above, the importance of entrepreneurship as employer of labour, driver of GDP and income earner is justified.

PROBLEMS AND CHALLENGES OF ENTREPRENEURSHIP

Common operational problems and environmental challenges facing entrepreneurship without reference to any particular nation according to the views of Kisunko, Brunetti & Weder, (1999) are high taxes and tax regulations, inadequate infrastructure, inflation, labour regulations, and regulations governing the starting and running a business. In Sub-Saharan Africa, the most critical problems identified are wide-spread corruption, tax regulations and high taxes, inadequate infrastructure, inflation, crime, theft and financing. The laws governing private enterprise, especially business registration and taxation systems, are believed to be overly complex and difficult to understand. Contract and private property laws are often poorly designed and/or enforced. As suggested by Kiggundu (2002), Pope (2000), and Stevenson (1998) the unfavourable institutional/regulatory environment in the various countries is often accompanied and compounded by the added expenses of corruption and bribery. Other problems encountered by entrepreneurs in transition economies include poor macroeconomic policies, limited access to short-term and long-term financial capital, and a lack of managerial experience.

Entrepreneurship can be described as suffering from plethora of problems and challenges. Nigerian entrepreneurs in some surveys reported that they were frequently harassed by government officials who extorted money from their businesses. Poor infrastructure including bad roads, water shortage, erratic supply of electricity, and poor telecommunication system represent additional challenges faced by small business owners (Mambula, 2002; Chu, Kara, Benzing, 2008). Difficulty in gaining access to bank credits and other financial institutions proved to be a major obstacle hindering the process of entrepreneurial development, but the most serious and damaging problem threatening the state of entrepreneurship is a lack of government interest in and support for SMEs (Ariyo, 2005; Chu *et al.*, 2008).

Another pressing challenge facing entrepreneurs is that they experience difficulties in establishing and maintaining effective business networks and clusters in their areas of domicile (Barr, 1999; Kiggundu, 2001; Ramachandran & Shah, 1999). This is corroborated by the atomistic outlook of small firms which prevent them from accessing credits. Barr (1999) specifically lends credence to this by emphasising that size is important because small firms were less able to manage risk and uncertainty by gaining membership in networks and clusters.

Lack of joint action is another challenge facing small firms. Ramachandran and Shah (1999) found that African-owned firms lacked joint action, and networking, which kept them out of the loop for information on valuable resources, capital and markets. In fact, they prefer to remain as sole proprietors rather than engaging in partnerships and limited company organisations. Kallon (1990) reported that 73.4 percent of the firms studied were single proprietorships, 10.9

were general, and 9.4 were limited partnerships and only 6.3 were corporations. Also, the productivity, survival and growth of the small entrepreneurial firms are fundamentally bound up with the fortunes of the economy as a whole (McGrath & King, 1999). It is therefore reasonable for these small enterprises to restructure themselves in such a way as to manage these interdependences to their advantage (Kiggundu, 2002). The empirical evidence from 2007 Business Environment and Enterprise Performance (BEEP) as shown in the diagrams below present the problems and challenges of entrepreneurship.

Table 1: Problems and Challenges of Entrepreneurship in Nigeria

Problems/Obstacles	Nigeria (percent)	Small (percent)	Medium (percent)	Large (percent)
Access to Finance	15.55	17.01	11.52	3.90
Access to Land	2.85	2.70	3.38	2.85
Licenses & Permits	0.57	0.58	0.60	0.00
Corruption	1.87	2.13	1.12	0.00
Courts	0.00	0.00	0.00	0.00
Crime, Theft & Disorder	2.07	1.64	3.40	4.33
Customs & Trade Registration	1.31	1.09	2.23	0.00
Electricity	63.63	62.66	65.50	78.78
Inadequately educated workforce	0.31	0.32	0.32	0.00
Labour regulations	0.09	0.07	0.20	0.00
Political instability	0.70	0.79	0.45	0.00
Practices Informal Sector	1.05	0.92	1.66	0.00
Tax Administration	0.28	0.12	0.49	3.48
Tax Rates	2.24	2.11	2.70	2.49
Transportation	7.49	7.88	6.42	4.16

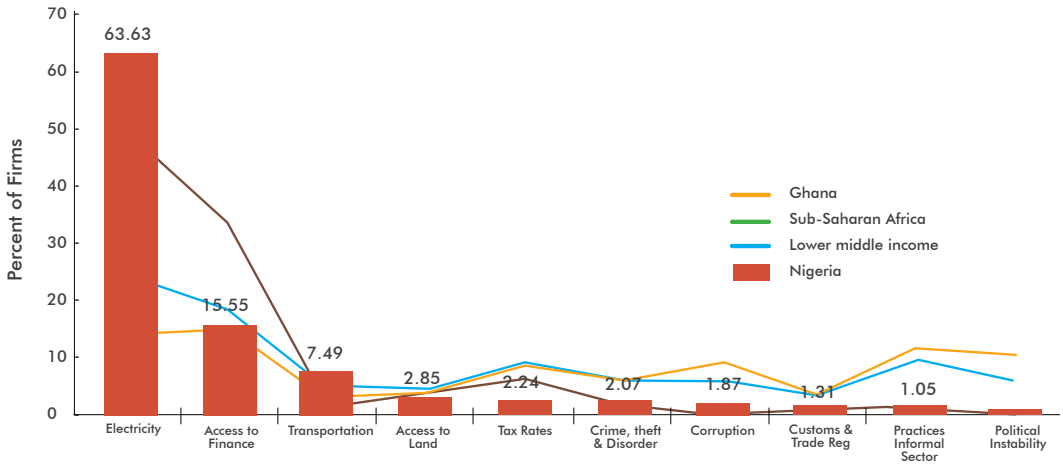
Source: Business Environment and Enterprise Performance Surveys (BEEPS)/World Bank, 2007.

The Enterprise Surveys above identified fifteen (15) problems/challenges as militating against entrepreneurship development in Nigeria. These include: access to finance, access to land, licenses/permit, corruption, courts, crime/theft/disorder, customs/trade registration, electricity, inadequately educated workforce, labour regulations, political stability, practices informal sector, tax administration, tax rates and transportation. The responses of the firms (in percentages) have also been clearly analysed according to operational sizes (small, medium and large).

The problems faced by entrepreneurs in Nigeria in comparison with other Sub-Saharan African countries are provided by BEEP/World Bank 2007. These are shown in figure 1 below.

Figure 1. Pressing Challenges/Constraints Facing Entrepreneurs according to 2007 survey

Top 10 Business Environment Constraints for Firms



Source: BEEP/ World Bank, 2007

ENTREPRENEURSHIP DEVELOPMENT AGENCIES

Modern entrepreneurship with specific reference to Nigeria became formal and organised after the Nigerian civil war. At the end of the war, the focus of the Second National Development Plan was on sustainable development embedded in the 3Rs objectives of Reconstruction, Re-development and Reconciliation. The activities in the plan and government legislations in support of enterprise development reinforced the ingenuity and inventive skills of the individuals and groups to be wealth creators, self-employed and self-reliant rather than seekers of white collar jobs. Specific government legislation that gave vitality to entrepreneurship was the promulgation of the Nigerian Enterprise Promotion Decree of 1972. Amendment of the indigenisation decree in 1977, 1987 and the introduction of privatisation and commercialisation decrees in 1988, 1989 and 1995 further boost the development of indigenous entrepreneurship. Besides that the government, local communities and non-governmental institutions also set up support agencies in order to promote the entrepreneurship culture. These support agencies include the following:

Traditional Microfinance Institutions

Before the emergence of formal microfinance institutions, informal microfinance activities flourished all over the country. Informal microfinance is provided by traditional groups that work together for the mutual benefit of their members. These groups provide savings and credit services to their members. The informal microfinance arrangements operate under different names: 'esusu' among the Yorubas of Western Nigeria, 'etoto' for the Igbos in the East and 'adashi' in the North for the Hausas. The key features of these informal schemes are savings and credit components, informality of operations and higher interest rates in relation to the formal banking sector (Raimi, 2007). The major challenges facing the traditional microfinance institutions are inadequacy of credits to go round, lack of government support, embezzlement, default etc.

Community-based NGOs

There are some well established community-based NGOs providing micro credits to their members, these are: Farmers' Development Union (FADU) Ibadan; Community Women and Development (COWAD) Ibadan; Country Women Association of Nigeria (COWAN) Akure; Life Above Poverty (LAP) Benin; Justice Development and Peace Commission (JDPC) Ijebu-Ode; Women Development Initiative (WDI) Kano; Development Education Centre (DEC) Enugu; Development Exchange Centre (DEC) Bauchi; Outreach Foundation (OF) Lagos; and lastly Nsukka Area Leaders of Thought United Self-Help Organisation (NLTNUSHO), Nsukka.

National Directorate of Employment (NDE)

The National Directorate of Employment (NDE) was established to give training opportunities to the unemployed, especially the youth, by providing guidance, finance and other support services, to help them create jobs for themselves and for others. A major problem of the programme has been inadequate funding. Nearly two million people have benefited from the NDE programmes (NBTE, 2008). Evawoma-Enuku and Mgbor, (2005) in their evaluation of the NDE scheme noted that the master craftsmen and women teach trainees using the traditional apprenticeship system. Also, there are no Saturday Theory classes for trainees due to lack of funds. The apprentices under NDE have low educational backgrounds, receive no evaluation and certification at the end of training; they get an equivalent of about three apprentices a month and are paid in arrears of three to six months. NDE scheme also suffers from a shortage of tools and drop-out rate is high.

National Poverty Eradication Programme (NAPEP)

This programme which commenced in 2002, is aimed at poverty eradication and empowerment. There are four major intervention schemes in Nigeria's current poverty eradication programme. One of them is targeted at youth – the Youth Empowerment Scheme (YES). The brochure describing the YES programme emphasises that YES is more than an employment scheme as it is aimed at the provision of training opportunities, skill acquisition, employment opportunities, wealth creation through enhanced income generation, improved social status and rural development. It is primarily aimed at the economic empowerment of youth. Despite the massive tax payers' money appropriated to NAPEP, poverty and destitution is still waxing stronger in Nigeria.

Micro Finance Institutions (MFI)

These are set up to meet the credit needs of the rural and urban poor, artisans, farmers, petty traders, vehicle mechanics, etc.. The Central Bank of Nigeria gave a directive to all erstwhile Community Banks to convert to MFI, latest by December 2006, by recapitalising to meet the new guidelines for setting up of MFI. Today, there are many MFI or MFB providing easy and cheap microcredits to small business owners. The Nigerian microfinance industry has come a long way; it boasts of all the four well-known models in the industry. A CBN study identified, as of 2001, 160 registered MFIs in Nigeria with aggregate savings worth N99.4 million and outstanding credit of N649.6 million, indicating huge business transactions in the sector (Anyanwu, 2004).

Institutional structures for the provision of microcredit vary and may be any of the following: government or public sector-oriented, NGO supported, traditional or a mixture of two or more of these. One of the challenges microfinance currently faces in Nigeria is for the MFIs to reach a greater number of the poor. The CBN survey indicated that their client base was about 600,000 in 2001, and there were indications that they may not be above 1.5 million in 2003. The existing microfinance in Nigeria serves less than 1 million people out of 40 million potential people that need the service (Mohammed and Hasan, 2008). Also, the aggregate microcredit facilities, account for about 0.2 percent of GDP and less than one percent of total credit to the economy. The effect of not appropriately addressing this situation would further accentuate poverty and slow down growth and development (Mohammed and Hasan, 2008).

Community banks

This is a defunct institution. While operational, the community banks were designed around the informal mutual savings and loan associations operating in rural areas. Organised by the government-sponsored National Board of Community Banks (NBCB), these financial institutions were meant to be self-sustaining and managed by communities to provide credit and deposit banking facilities. These banks used the strong local networks present in many rural areas of Nigeria and community boards generally drawn from respected leaders within the community (Ibid).

Small and Medium Industries Equity Investment (SMIETS)

The Bankers' Committee took a decision that 10 percent of the funds accruing to the Small and Medium Industries Equity Investment (SMIEIS) should be channeled to microenterprises through registered microfinance institutions. Under the SMIEIS arrangement, banks agreed to set aside 10 percent of their pre-tax profit annually for equity investment in small and medium industries. In December, 1999, the Small and Medium Industries Equity Investment Scheme (SMIEIS) was initiated, conceived and designed by the Bankers' Committee at its 246th meeting. The scheme has not been very successful as conditionalities for accessing credit were extremely discouraging. As laudable as the scheme was, it has a lot of conditionalities attached. Hence, the utilisation rate of the accumulated fund is only 3 percent (Inegbenebor, 2006).

Contribution of development partners – UNDP

The United Nations Development Programme (UNDP) is on the ground in more than 400 communities in all the 36 States of Nigeria and the Federal Capital Territory. It is assisting to build capacity to manage the economy and to fight

poverty. One of the four programmes supported by the UNDP is Job Creation and Sustainable Livelihood. The microcredit delivery aims at increasing the access of communities to small loans and other productive inputs to empower them and expand their livelihood opportunities. UNDP has trained 37 Microfinance Institutions (MFI) in different States in loan disbursement to communities supported by the UNDP.

Manufacturers' Association of Nigeria (MAN)

This body was formed as a company limited by guarantee to perform important roles on behalf of its members, as well as for the development of the country. Its sectoral groups include: food, beverages, and tobacco; chemicals and pharmaceuticals; domestic and industrial plastic, rubber and foam; basic metal, iron and steel, and fabricated metal products; pulp, paper and paper products, printing and publishing; electrical and electronics; textile, wearing apparel, carpet, leather and leather footwear; etc. The Manufacturers' Association of Nigeria (MAN) performs many functions. The body encourages a high standard of quality for members' products through the collection and circulation of useful information and the provision of advice.

This Association encourages the patronage of Nigerian-made products by Nigerians and by consumers in foreign countries. It develops and promotes the contribution of manufacturers to the national economy. Furthermore, it provides the manufacturers in the country with information on industrial, labour, social, legal, training and technical matters (NBTE, 2008). The Association, since its establishment in 1971, has made giant strides in the areas of policy advocacy, business information and development, as well as outright direct intervention.

MAN has successfully positioned itself as a leading business Association recognised and respected by the Government. There is a very high level of consultation between the Federal Government and the Association, and the views of the Association are sought at the conception stage of policy formulation. The relevance of MAN has been appreciated through invitations to serve on many committees set up by government and other organisations, namely: Commonwealth Head of Government Meeting - Abuja 2003; Business Support Group; Presidential Committee on Lagos Explosion Disaster Relief Fund; Specialized Committee of Stakeholders to Review the Status of the Pre-shipment Inspection Scheme Preparatory to the Introduction of Destination Inspection Scheme; House of Representatives Committee on World Trade Organisation (WTO) Agreements; Presidential Committee on Modalities for Engaging Nigerian Professionals in the Execution of Project; MAN-NPA; Fast Track Delivery Committee on Consignment of Raw Materials; Regional Organising Committee on 3rd ECOWAS Trade Fair and National Organising Committee on the 8th OAU Trade Fair (MAN 2010) .

CONCLUSION

From the foregoing discussion, it is clear that support for SMEs is limited and quite inadequate. The government should therefore increase its support for entrepreneurial development in the forms of trainings, logistics and fundings for trained graduates of entrepreneurship programmes.

Entrepreneurial discoveries and innovations should also be linked up with SMEDAN and Industrial Associations for support. In the final analysis, the government should guarantee and remove the bottlenecks in accessing loans by entrepreneurs from microfinance banks and grants promising SMEs reasonable grace period before loan repayment starts. Lastly, government should facilitate easy business registration, tax holiday and basic infrastructures in order to boost the growth and expansion of enterprises and industrial organisations.

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MALAYSIAN FARMERS' MICROFINANCING AND MICRO-ISLAMIC INSURANCE MODEL: INSPIRATIONS FROM A MULTI-COUNTRY STUDY

ABSTRACT

The agricultural sector in Malaysia is particularly susceptible to food crisis and spiral increase of the price of staple food. These factors justify the need to strengthen the foundation of the Malaysian agricultural sector and place the sector at the forefront of the Malaysian economy. The inability to secure rice imports from the neighbouring countries, particularly Thailand, Indonesia, Vietnam and the Philippines, has led to the country's focus on food production for better sustenance and control on the food bill, which peaked in 2004. The farming community, which represents approximately 12-13 percent of the national work force and 11.6 percent of the population, makes up the majority of the hard core poor in the country. Without serious financial and ancillary support, their living condition is bound to deteriorate in the near future. This situation is especially true for the paddy growers who produce 70 percent of the national rice consumption. Evidently, many of them are leaving the agricultural sector for greener pasture, i.e. the service sector, to ensure income stability.

In this paper, a micro-Islamic insurance model is proposed for the agricultural sector, with adoption and adaptation from models used in various countries. This model is put forward to be considered by the Malaysian Government towards uplifting the livelihood of the farmers and the poor residing in the rural areas of Malaysia.

KEYWORDS

Islamic insurance, family takaful, general takaful, zakah, tithe, Shariah, musharakah, Baitulmal, microfinance, micro-insurance

Malaysia is situated in South East Asia and almost all nations in this region are rice producers. While Thailand and Vietnam produce more than they require for home consumption, Malaysia has been, since Independence, importing between 30-40 percent of its rice. Rice is a staple diet of its population. Therefore, Malaysia has been moving towards increasing the local rice production through a sectoral transformation plan so as to be less dependent on food imports. Among the strategies outlined to achieve this objective are: to maximise land use; to increase productivity through integrated farming; to create collective offering of credit facilities; to adopt use of high technology; automation; to develop human resource in food production; and to strengthen the agricultural institutions (Transformasi Pertanian, 2001). However, to date, not much increase has been recorded in agricultural output since 2001 (Table 1).

Table 1: Production of Agricultural Products

Year	2001	2002	2003	2004	2005	2006	2007	2008
RM	12,800.8	13,709.1	13,304.1	14,159	13,305.5	13,188	14,005	15,085

Source: Economic Report, Ministry of Finance, Malaysia

THE NEW AGRICULTURE, THE 3rd ENGINE OF GROWTH FOR MALAYSIA

Public spending and economic growth

In the last two decades, the agriculture sector in Malaysia had not been a well-sought out industry and one that is very much dependent on government assistance. Public spending in the form of various incentives and subsidies had been offered by the government to improve productivity and returns. For example, mechanisation was thought to be the solution to this issue and one of the crops that benefited from this is paddy. Nevertheless, mechanisation is only feasible and economically efficient if there are large masses of land. However, most paddy growers are small landowners and have limited access to financial assistance. The past efforts by the government resulted in a negative impact as food import bill peaked (increased by 40 percent) at RM18,478 billion in 2004, compared to food exports of RM34,085 billion (Table 2) (normal average increase per year is about 12 percent). A number of similar studies done in

other parts of the world, cited by Heller & Roman (2008) and supported by their own research found that an increase in real level of public spending in European Union countries, in fact, saw a decrease in the Gross Domestic Product growth rate. This is especially true when more funds were allocated towards agriculture, but did not achieve the desired level of growth. This is also true where staple food is concerned. 2004 and 2006 was the most critical year when import of rice increased exceptionally high, at 38 percent and 43 percent respectively (Table 3). This is a disturbing development considering Malaysia's dependency on imports for at least 30 percent of its consumption. On top of that, Thailand, Vietnam, (the two largest exporters), as well as Cambodia and Myanmar hinted at establishing a cartel to curb exports when the production fell drastically after the occurrence of numerous natural and man-made disasters and the price of rice shot up unexpectedly.

Farmers' predicament: agriculture v. nature

The agriculture sector is an industry very much affected by nature, fluctuation in prices and yields, government policies and foreign markets. These factors have all posed as challenges to the industry and caused wide swings in farm income. Managing risks in this sector is in itself a risky business, partly due to the factors that cannot be regulated and the potential for catastrophic losses. Natural perils brought about by meteorological factors, such as extreme changes in weather, droughts and floods, as well as biological threats, such as diseases and pests, are among the causes of large losses to this sector. For individual farmers, this may be hard to bear as they may lose their livelihood from the impact of even one major calamity. To rebuild their livelihood would be costly and to experiment with new methods of farming is a big gamble. Statistics have also shown that many farmers in Malaysia belong to the hardcore poor group, some of which are the result of these very factors, as well as the farmers' inability to rebound financially.

The renewed interest in agriculture in Malaysia was spurred partly by the agro-biotechnology revolution, as well as the increase in hypermarkets and supermarkets bringing processed agricultural products to the end consumers. Agriculture is envisaged to be a mechanism to eradicate poverty and preserve the environment. In eradicating poverty through agriculture, it became clear that after rapid urbanisation took place, the rural folks (who are badly affected by the high cost of staples) were left in the lurch, hence, providing little choice to the government except to embark on poverty eradication programmes to bring the hardcore poor, especially the farmers, into the economic mainstream (Wong, 2007).

Table 2: Malaysia's food & beverages 2000-2008 (RM million)

	2000	2001	2002	2003	2004	2005	2006	2007	2008a
Exports	17,531	17,771	23,698	30,731	34,085	33,160	36,468	50,033	15,764
Imports	10,593	12,078	12,678	13,162	18,478	18,411	21,136	24,435	7,219
Percent Increase (Imports)		14	5	4	40	-0	15	16	

a estimate

Source: Economic Report: Ministry of Finance, Malaysia

Table 3: Malaysia's import of rice, 2000-2008

	2000	2001	2002	2003	2004	2005	2006	2007	2008
RM '000	689.3	529.7	510.1	398.7	548.1	688.7	1,048.9	1,072.9	189.3a
'000 tons	594.1	516.6	495.5	365.4	506.0	581.1	836.1	796.0	123.6
Percent Increase (tons)		-13	4	-26	38	15	43	-5	

a estimate (not a yearly data; available at the time of print)

Source: Economic Report, Ministry of Finance, Malaysia

TRANSFORMATION FROM AGRICULTURE TO MANUFACTURING, AND BACK TO AGRICULTURE

Prologue to the manufacturing sector

The manufacturing sector has played a dominant role in Malaysia's economic growth in the last 30 years. Up until the decline of the manufacturing sector beginning from 1997, a lot of emphasis, backed by several development plans and projects, were given to the sector to achieve the many national economic targets. The continued slump in the manufacturing sector caused the shift of interest towards the agriculture sector. The former recorded its first lowest growth in 2007, at 1.9 percent compared to 7.5 and 5.1 percent in 2006 and 2005, respectively (Central Bank of Malaysia Annual Report, 2007). Although it is the sector commanding the highest labour use, contribution to GDP and other positive developments in the supply chain presently, it was the Government's view that more focus should be given to the food industry, which has been

neglected for too long, particularly to agriculture. Being a country with one of the highest rate of biomass production in the world, where "almost anything can grow here", it was felt that it is a wasted opportunity that the country is not able to grow enough to be self-sufficient and remains a net importer of food (Loh & Bedi, 2008).

The shift towards the agricultural sector

With an additional allocation of RM5.6 billion in 2010, Malaysia made a commitment to increase the national rice production up to 86 percent. Both short and long term measures, such as stockpiling and expansion of planting areas, were suggested. Private and public sector funds are required to speed up projects towards achieving this end (The Star, 2009). The commitment was in response to the need to reduce the income gap between the urban and rural population. Statistics showed that 1.5 percent of the rural population earns less than RM300 (US86) per month, compared to 0.2 percent of the urban folks in 2004 (1US dollar = RM3.50) (Tables 4 & 5). Many of the rural population are directly or indirectly involved in agriculture and statistics indicate that the labour force in this sector, which started out at 14 percent in 2003, had decreased to 11.6 percent in 2008 (Table 6). Although small in terms of percentage decline, there are indications that people are moving on to other sectors that could provide for a more stable income, especially the services sector (Statistics Department of Malaysia, 2008).

Positive agricultural development plans

More research and development projects should be carried out on the agricultural sector to boost productivity and, ultimately, increase the income of this sector. There is the need for the agricultural workforce to undergo transformation and paradigm shift in the way things are done in this sector. Banks and financial institutions are also encouraged to provide agro-financing. The emphasis placed by the government towards upgrading this sector is strong evidence that it is serious about transforming and modernising the agriculture sector.

Under the 9th Malaysia Plan (9MP), several initiatives were introduced to increase domestic food production. These included exploration of new areas for cultivation with the introduction of the Permanent Food Production Park in 2003 (1,540 hectares); resource optimisation; introduction of technology as a boost to increase productivity; as well as provision of incentives and encouragement for private sector involvement via investment. To date, these objectives have not been achieved, with very minimal increase recorded, as well as a decline in agriculture's share in GDP contribution from 2006 onwards (Table 7). Another initiative that has been long-awaited by the farming community is the development of an insurance scheme for the agricultural sector, which would act as a safety-net against major calamities, whereby compensation from the insurance are given during times of economic hardship, which would certainly reduce the losses faced by the farmers, hence, stabilising their income.

Table 4: Percentage of poor and hard core poor (monthly income)

Geographical Area	Poor Household (RM)	Per Capita	Hard Core Poor Household (RM)	Per Capita
Peninsula Malaysia	660.00	150.00	400.00	90.00
Sabah (East Malaysia)	900.00	170.00	500.00	100.00
Sarawak (East Malaysia)	770.00	170.00	450.00	100.00

Source: Majlis Taklimat Pemantapan Jentera Penyelarasan Program Pembasmian Kemiskinan Selangor, (Council for the Eradication of Poverty Briefing in Selangor) December 13, 2007

Table 5: Groups of poor & hard core poor (percentage)

Year	1990	1997	1999	2004
Poverty Rate	16.5	6.1	7.5	4.3
Urban	7.1	2.1	3.4	1.6
Rural	21.1	10.9	12.4	9.6
Poverty Rate for Hard Core Poor	3.9	1.4	1.4	0.7
Urban	1.3	0.4	0.5	0.2
Rural	5.2	2.5	2.4	1.5

Source: Majlis Taklimat Pemantapan Jentera Penyelarasan Program Pembasmian Kemiskinan Selangor, (Council for the Eradication of Poverty Briefing in Selangor) December 13, 2007

Table 6: Employment by agriculture sector (millions)

Year	2003	2004	2005	2006	2007	2008
Total Labour Force	10,150.0	10,587.7	10,926.6	11,544.5	11,775.1	11,985.8
Agriculture Labour Force	1,402.6	1,396.8	1,385.6	1,392.4	1,391.2	1,389.7

Source: Economic Report, Ministry of Finance, Malaysia

Table 7: Share of gross domestic product by sector - agriculture

Year	2001	2002	2003	2004	2005	2006	2007	2008a	2009b
Percent	8.7	8.4	8.2	8.5	8.5	7.9	7.6	7.5	7.4

a estimate, b forecast

Source: Economic Report, Ministry of Finance, Malaysia

In 2001, the Central Bank of Malaysia or Bank Negara Malaysia (BNM), together with the insurance bodies, proposed an insurance plan to provide protection against certain major agricultural risks. Uncertainties in prices, poor yields due to natural disasters, escalating fuel price, government policies and pressure from foreign markets are some of the risks faced by the agricultural sector. What this plan hoped to achieve is to put a comprehensive and integrated risk management programme in place, so that corrective and timely decisions could be implemented. To date, this plan has not taken off.

Elements of theory of spending

Economic growth is the foundation for improvement of living conditions and general welfare of the population. Its growth is also predicated by improved economic status of the poor. In Malaysia, individuals and households that are categorised as poor are given minimal subsistence allowance by the Ministry of Social Welfare and state agencies concerned. An increase in public spending to provide support for this group sometimes goes beyond basic government function, resulting in ineffective redistribution of income. For example, subsidies sometimes cause beneficiaries like farmers to act ineffectively because their dependence on public funds results in less effort on production capacity. The principles expounded by Schaefer (2006) on the effect of public spending on economic growth are:

- A need for a certain amount of public spending necessary to support basic socials, legal and economic structures of the economy
- A need for reasonable public spending transfer of resources from private sector to stimulate economic growth

Hence, the cost of state activities must not exceed the benefits because, if it did, it would result in the "dead weight loss" concept, which in economics is termed as "ineffectiveness of state financed projects." Agricultural growth is hampered largely due to the uncertainty of external natural forces in the form of natural, human, as well as economic perils, compounded by the lack of private sector participation to encourage growth. Therefore to counter this, a reasonable government intervention, aided with private sector help is necessary to protect them. Experts in the field view that the agricultural sector requires concerted efforts in the form of financial incentives from both the public and private sector (namely, the government, banks and insurance companies). The former to prepare the infrastructure as well as partial funding or subsidies, while the latter, to provide the financing for pre-, during and post-production periods.

It has been documented that the world's main areas for agricultural production insure both their livestock and crops. Many forms of catastrophe exposure have created affordable premiums, while hail insurance for crops and disease insurance for livestock has been in existence for the last 150 years. Although governments' premium subsidies worldwide have increased and extended the scope of agricultural insurance cover, this remained at a modest amount of between 2-3 percent, while the agricultural sector in the U.S. is subsidised up to 10.5 percent (depending on crops). Crop producers insuring under the Actual Production History (APH) insurance plan received up to 100 percent government subsidy of the APH premium at the lowest yield level to 38 percent for the maximum coverage level (Edwards, 2009). Globally, growth opportunities in this area have been high. Factors prompting this positive development are high agricultural commodity prices increase, growth in population, increased buying power in emerging markets and increase in biofuel demand (Heintz, 2008).

ISSUES TO BE ADDRESSED

In wanting to bring some changes to the scenario faced by the agricultural sector, it is necessary to design a model that depicts both the extent of public and private sector intervention into the agricultural sector in Malaysia.

RESEARCH DESIGN

A work-study visit was initiated to gain some insights from other countries. Morocco in North Africa was chosen because its economy depends a great deal on agriculture, (18 percent of GDP; 33 percent of GNP), while in Europe, Spain was selected (agriculture is 8 percent of GDP) due to its heavy leanings on government intervention in the agricultural insurance policy offerings. The other reason is partly because they have produced very encouraging results from both the insurance and financial sectors. While the choice of other countries' experience, such as Pakistan, Jordan, Kuwait, Egypt and Sudan, is due to the State intervention in poverty eradication programme using their zakat (tithe) entities and microfinancing respectively, forming the basis of the model to be proposed for the Malaysian farmers who account for 14 percent of the total work force in the country. With wide income fluctuations and production that is highly susceptible to by changes in economic and socio-political factors, this sector certainly deserves immediate attention and some incentives must be provided to the workers for them to remain in this sector.

A two-tiered research project funded by Universiti Teknologi MARA was undertaken to visit Spain and Morocco, while another research was conducted to look into the plight of the Malaysian farmers from many aspects. Initially, with the assistance from the Malaysian embassies in Spain and Morocco, data was collected in the form of interview with various institutions and bodies directly related to agriculture. These included both the private and public (various ministries) sectors, as well as bodies relevant to the sector, such as agricultural associations. The time frame to commit to the international and national research began from 2002 right up to 2004 (when data was collected) and 2005 when the findings were analysed and report submitted to the relevant authorities for their consideration. This is later used to assist in the agricultural development plans announced by the government.

RESEARCH FINDINGS

Agricultural sector in Morocco (extracted from Abdul Rahman, 2006)

The government of Morocco appointed the Mutual Agricultural Assurance of Morocco (MAMDA) to provide a comprehensive insurance cover within the agricultural sector, which is lacking in most African nations' agricultural policies. MAMDA is owned by the private sector (including the farmers as co-owners) and the public sector (Moroccan government). The setting up of MAMDA is in itself an encouragement to the farmers to boost their income through the annual dividends and bonus payout received as co-owners of the entity. The incentive from these returns is the initiative towards an effective risk management of their land to ensure high returns every year. Up to 2002, only cereal farmers were covered under this scheme, which by then had run for 7 years. MAMDA also aggressively undertook researches in collabouration with the World Bank Program to initiate the introduction of newly created insurance products for the agricultural industry. Studies conducted thus far included:

- Conceptual and Practical Considerations for Sharing Catastrophic Risks
- Designing and Rating Area Yield Crop Insurance Contract
- An Expected Indemnity Based Approach to the Measurement of Moral Hazard in Crop Insurance
- An Empirical Analysis of the Demand for Multiple Peril Crop Insurance
- New Approaches to Crop Yield Insurance in Developing countries

As part of the incentives from the government, premium subsidy is given up to 50 percent for 5 years and this support is reduced gradually to encourage independence.

Other institutions supporting MAMDA

The Caise National Credit Agricole Bank of Morocco (CNCA) was established in 1961 to provide financing facilities in the Agribusiness sector. It has been aggressively promoting its credit facilities services both to the general public and farmers, covering small, medium and large farmers. Both CNCA and MAMDA worked jointly to ensure the success of the national insurance scheme. In 1996, the bank used a common criterion for all its outlets, providing credit based on the presence of some form of assets as collateral from the farmers. This format proved to be ineffective, and in 1997, refocusing its objectives, the credit was extended based on a grouping of farmers having similar financial standing. The concentration on the rural farmers saw a decline in the number of clients but weeds out the ineffective farmers.

For the small farmers, usually having high composition of women of approximately 10 people in a group, involved in homemade agricultural produce (e.g. sauce, chips etc.), a tontine type of financing is provided. Small credit facilities were given out individually. Each participant takes turn to receive the credit and it is only extended once the earlier participant has completely settled the loan. For

the medium to large farmers, a larger credit facility is allowed, but subject to an effective risk management programme in place to ensure productive use of the land. To oversee this function, an advisor is selected from among the villages, a person known to the bank and the farmers. The advisor checks on the credit worthiness of the farmers, determines who is eligible for credit and ensures that repayment is completed. With the current credit scheme, many farmers in 18 provinces are insured. Indemnity is provided by the insurance company and the state (government) steps in during occurrence of catastrophe, as in the 1993 drought.

Other than the CNCA, other institutions working closely with the agricultural sector include the various Fruits Producers' Association, Educational Institutions and the Ministry of Agriculture. The institutions involvement in the Morocco's agriculture sector is depicted in Tables 8 & 9.

AGRICULTURAL SECTOR IN SPAIN

The scenario of the Spanish agricultural insurance system before 1978 and after 1978 changed a great deal. Before that year, insurance was handled by the private insurance institutions and this system proved to be unsuccessful. The reason for this failure include the insurance system being too profit-driven and the premiums charged were too high, therefore the farmers could ill-afford to participate in the scheme. The Spanish government took control and established itself as state insurer and this also was not successful because the government was too sympathetic towards the farmers. After 1978, a consensus was reached between the three parties, namely the state (ENESA), private insurance institutions represented by their association (AGROSEGURO) and the farmers which result in the co-participation of all three.

The state performs the task of overseeing and monitoring the insurance activities, while the private insurers manage and handle all insurance related activities due to their wide experience and knowledge in the field. The basic objective for this insurance framework is to stabilise the earnings of the farmers after experiencing a loss, as well as to prevent mass migration to the urban areas and resorting to debts. The participation of the insurance scheme is not mandatory, and the farmers could purchase insurance individually or as a group through the farmers associations. The Government support comes in the form of subsidy for the cost of insurance and insurance companies can claim the subsidy directly from the government. The agricultural insurance contract is an annual contract and rates, conditions and others are decided after every annual meeting held between the three parties. The government sets aside allocated budget specifically for the agricultural insurance plan and coordination efforts are entrusted to the state organisation of agricultural insurance (ENESA), which is directly controlled by the Ministry of Agriculture. Besides acting as a signatory body, while at the same time monitoring the development of the annual agricultural insurance plan, it also investigates damages to agricultural productions. Other roles include

promoting and disseminating insurance information to the relevant bodies, acting as arbitrator in times of disputes between the insured and the insurer, as well as reporting to the government on special conditions and imposition of loadings for specific classes of insurance by the group of insurer (Che Idris, 2002).

In 1980, they started out with only five lines of insurance, covering 12 agricultural products. By 1990, these have expanded to 36 lines, covering 58 agricultural products and cattle rearing. By the turn of millennium, they have 63 lines covering 130 agricultural products, three cattle rearing and five aquaculture products. Summary of governmental, private sector and farmers' association support is depicted in Tables 7 & 8.

AGRICULTURE IN MALAYSIA

Malaysian farmers also faced a number of unpredictable losses and disasters in the last 10 years. The most affected crops due to flood damage were paddy, followed by tobacco. The Malaysian government had initiated many programmes to prop up the sector in order to stabilise the farmers' income, as well as food production. The continued and vigorous growth of this sector faces setback partly due to the lack of commercial loans or financing and insurance protection. In 1992, only one local insurer took the bold step to provide crop, livestock and aquaculture insurance and this was soon terminated after a few years due to poor claims experience. Bank Pertanian Malaysia (BPM), established in 1969 under the directive of the World Bank to oversee the function of providing credit facility solely to the agricultural sector, accomplished its role to a certain extent, but did not reach its full potential because the small farmers were left out. In 2003, under the BPM banner, government funding came through the Fund for Food (3Fs) programme, which provided a maximum loan of 75 percent of project costs to Small Medium Enterprise (SMEs). A microcredit scheme, a joint effort between BPM and Bank Simpanan Nasional (BSN), provides small loans in the amount of RM20,000 (USD5,000-6,000) for small businesses and enterprises in the agricultural sector. Although all these efforts were deemed worthwhile, insurance involvement is seen as the key factor before banks and financial institutions would be keen to come forward to offer their services. Otherwise, financial aid must come from the government, which is seen through the BPM and BSN. In 2002, Tani Pool Malaysia was set up, comprising general insurers interested in a joint indemnity programme, initiated by the Central Bank of Malaysia (BNM) for the agricultural sector. But to date, this initiative was put on hold and it is not known whether it would be revived in the near future.

Data gathered from the nationwide survey of Malaysian farmers found various techniques, approaches and mechanisms were introduced and supported by the government. The results of the interviews conducted in all three countries, namely Morocco, Spain and Malaysia, are depicted in the Tables 8 to 9 below.

Table 8: Governmental & financial institution support (premium subsidy)

	Morocco	Spain	Malaysia
Farmers Associations	50 percent	Minimum	None
Government	50 percent	Yes, varies with types of crops, range 8 percent - 65 percent	None
Financial Institutions	credit extended	n/a	None

Table 9: Summary of comparison for 3-countries categorised into 3-perils - x risk exposed to

Country/ Continent	Morocco Africa	Comments	Spain Europe	Comments	Malaysia Asia	Comments
NATURAL PERILS	× × ×	Govt. & private sector intervention	× × ×	Govt. & private sector intervention	× × ×	Partial Govt. intervention
Drought Disease/Virus		Risk financing		Risk financing technique -		Risk control techniques -
• Floods • Frost • Hail • Fire • Fire on equipment, building & goods • Change in weather condition • Pests • Storms • Death/ disablement • Forced termination of production • Death of animals	× × ×	technique – insurance	× × × × ×	insurance	× × ×	Crop scheduling Water drainage Dig trenches Use biological & chemical Retain own risks
MAN-MADE PERILS		"		"		Individual initiatives
Machinery & equipment b/ down Political risks Farm leasing risks Environmental risks, pollution, pesticide Health impairment of consumers Accidents at work	× × × × × ×	Risk financing technique – insurance	× × × × × ×	n/a	× × × × × ×	Risk control techniques -Govt. aid & use of retention fund

Country/ Continent	Morocco Africa	Comments	Spain Europe	Comments	Malaysia Asia	Comments
Theft & robbery Contamination of water supply Insurance for stationery vehicle Transportation of merchandise					×	
ECONOMIC OR BUSINESS PERILS		"		"		Individual initiatives
Oversupply of production Price risks Change in govt. policy Lack of infrastructure & technology Exportation problem Civil responsibility Loss of production Retirement	× × × × × × ×		× × × × × × ×	Minimum or ceiling price	× × × × × × ×	Risk control techniques - Short cycle plant; depend on innovati-veness & own creativity

The abovementioned findings provided insights into both the plight of the farmers and the mechanisms employed to address them. While Morocco and Spain clearly have their government intervening in addressing their exposures via introduction of a risk financing scheme, they also have in place a form of national agricultural insurance scheme, which has been successfully implemented with cooperation and commitment from the private sector. To some extent, the Moroccan private sector has more or less tackled the poverty problem among its poor by embarking on the financing scheme for the low income and the farming community in general. After studying both Morocco's and Spain's experience in managing their national insurance scheme, Model 1 is emulated from both country's experience, which is anticipated to provide some financial assistance to the low income groups, particularly the farmers.

SECONDARY RESEARCH FROM VARIOUS COUNTRIES FINANCING SCHEME FOR THE POOR

Microfinance in Sudan

A look at various microfinancing services from around the globe provided a somewhat mix practice overview. In Sudan, for example, the products of microfinance are highly in demand due to the high level of poverty. Although there is no national policy, nor any market studies undertaken to study the problem, achievements in the implementation of the Microfinance Unit, Central Bank of Sudan, is exceptional with a joint-venture or musharakah (equity

financing) contract with eight specialised banks, reaching out to 25,000 of the economically active poor and 23 percent of funds handed out to women (Dirar, 2009). Dirar (2009) reported that even though there is no commonly accepted definition of the target group of the poor and the destitute, commercial banks must still channel their loans to at least 10 percent of the productive families, artisans and small professionals, on top of being gender sensitive. The poor are normally located in remote areas, where banks have difficulty in reaching out to them. Therefore, linkages between the banks and the informal credit systems that exist could tap into the needs of the poor and the latter being able to identify them and their character strengths. One of the ways for banks to achieve their target population is by opening up microfinance windows in geographical locations where they are represented by their branch offices. Due to the non-collateralised nature of the transaction, the banks' pricing took into account the higher risk exposure (delayed payments, delinquent and doubtful debts and writing-off bad debts), where a cost sharing formula is worked out between the banks and their clients.

ALTERNATIVE FINANCING SCHEME - ZAKAT DISTRIBUTION UTILISED BY OTHER COUNTRIES

Zakat is obligatory upon a Muslim with surplus assets or wealth to give to the poor. The belief among Muslims is that the act of paying zakat purifies and cleanses wealth, and the Almighty will ensure that the individual is rewarded extensively in return (Abdul Rahman, 2009).

A study by Kahf (2000) on zakat management in four countries - Egypt, Jordan, Kuwait and Pakistan - saw some similarities in the findings on how the funds accumulated from the payer of the tithes is distributed to the poor. These distributing organisations, although different in features especially in its physical make up, a bank; (Nasir Social Bank and Faisal Islamic Bank) in Egypt, use of tithe collection agencies and volunteers from the local zakat committees; in Pakistan, and government agencies; in Kuwait and Jordan, have played a prominent role in disbursing funds to the poor. To this end, the most effective is the one in Pakistan, where the percentage of zakat receipts is 4-15 times of its GDP, with the ability to reach approximately one million individual and family recipients annually. The "system of funds (zakat) distribution" provides for contacts and relations with a large segment of the population. The Nasir Bank in Egypt managed to collect from a half million voluntary payers and reaching about 700,000 recipients, also using voluntary workers and committees. The government assisted zakat directorate in Jordan and Kuwait does not reach to that many recipients because they are basically provided assistance by the government.

Based on the above experiences of various countries in assisting the poor through a number of financing schemes, this research uses several agencies in order to create a combined micro-Islamic insurance and micro-Islamic finance scheme suitable for Malaysian farmers and the poor. Figure 1 below outlines the model syndicated by various financing institutions complementing an integrated risk financing and investment scheme using the Islamic financing and Islamic insurance models to appeal to the farmers and the poor who are majority Muslims.

MODUS OPERANDI OF THE MICRO ISLAMIC FINANCE AND MICRO ISLAMIC INSURANCE SCHEME

This scheme is a Malaysian-made innovative risk financing, serving both as an investment mechanism, as well as insurance cover to the agricultural sector. Since the majority of the farmers are Malays who are Muslims, conventional insurance could be replaced with Islamic insurance or takaful and, similarly, conventional banks are replaced with Islamic banks. The implementation of the scheme is elabourated below. To be eligible, one has to be a farmer and a member of a farmers' association or cooperative.

Administration of the scheme (involvement of 3 parties):

The Players: The Bank – Islamic Bank

1. The bank must ensure that each participant is a member of a farmers' association.
2. The bank sells units and issues a certificate on the amount purchased. The bank matches each unit purchased with its own funds (in compliance with Islamic law or Shariah, the financing institution partners with the participants (farmers) on their agricultural project, creating a joint venture relationship called Musharakah (the Islamic equivalence of joint venture agreements), where profits or losses will be shared equally or according to a fix predetermined proportion for both parties (Usmani, 2007).
3. Partial amount of the units purchased will go towards covering the bank's administrative expenses (estimated to be 10-20 percent of the amount) and 25 percent-30 percent as contribution (premium) to be remitted to the Islamic Insurer or Takaful Operator.
4. To enable the disbursement of the tontine values or loans, the amount to be received by the members must exceed a certain number of units purchased. If the client is deficient in funds contribution, he/she could approach the Baitul Mal (Tithe collection agency in Malaysia), which has ready funds collected from individuals who have profited from their business activities and meant for distribution to the poor and the needy.
5. The bank will also pay a fee to the monitoring body (farmers' association for keeping a record of its members, which ensures the latter service their loans and continue to purchase the tontine units and monitor members' eligibility criteria, as well as farm risk management).

Islamic Insurer or Takaful Operator

1. The takaful operator will receive the contributions* (premium), which is deducted from the units purchased for the coverage by the farmers from the bank.
2. The type of takaful coverage provided are:
   - Term Life insurance or Family Takaful – to cover premature death due to any causes, disability and injuries due to accidents and illnesses (small sums insured; recommended at RM1,500 for contribution of RM10/year and increases if the unit purchased increased accordingly),
   - General insurance or general takaful – agricultural losses due to 'natural perils only' at the beginning and later to be expanded to cover other perils after the fund stabilises (sums insured begins at RM2,000/acre for each paddy grower).
3. Benefit amounts will commensurate with the contribution (premium) amount remitted by the bank, which consequently will depend on the units purchased.
4. The takaful operator will provide the coverage based on the contributions (premium) received, which largely depend on the farmers' affordability or the sum contributed by the Baitul Mal (zakat institution) on their behalf.

*contribution is used in place of premium

Monitoring Body – Farmers' Association/Cooperative

1. Keeps a record of members eligible to join the scheme.
2. Ensures members service their loans and continue to purchase units from the scheme. Penalties imposed or members are barred from the scheme if loans are not repaid; ensure the members are credit-worthy, and economically active.
3. Receives a fee for their effort.
4. Provides farm risk management activities, as well as monitor validity of claims.

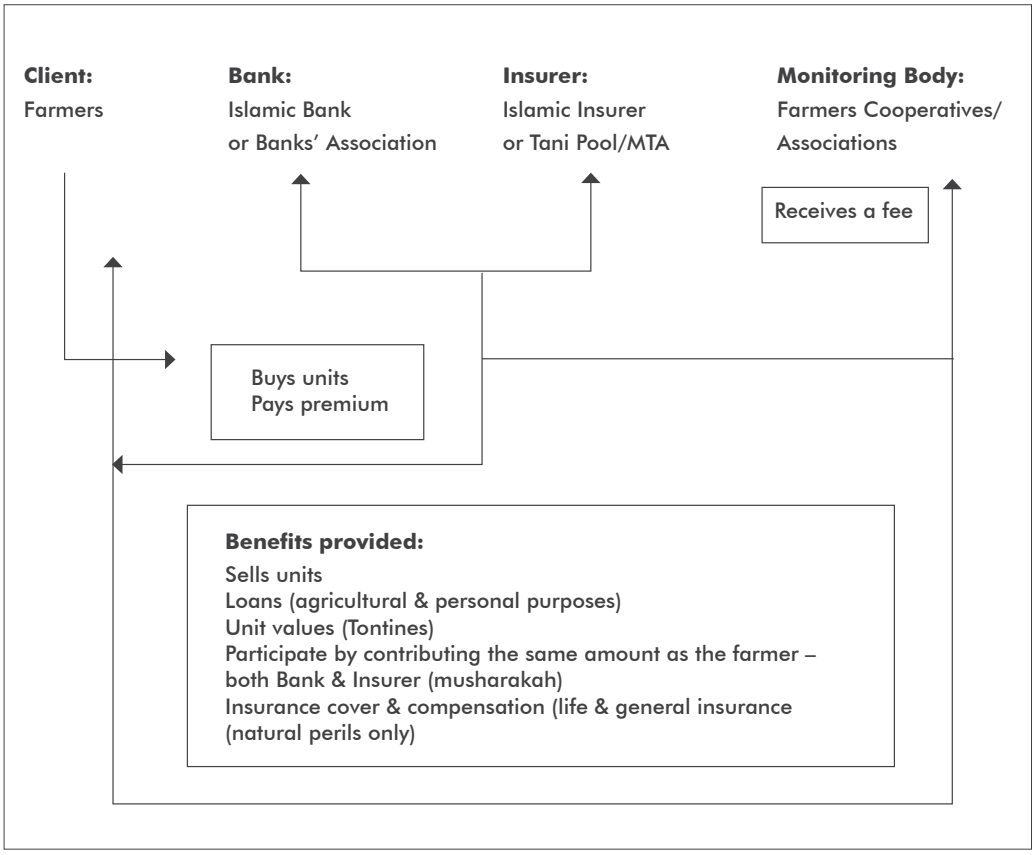
Collaborating Institutions

- Central Bank of Malaysia (Bank Negara Malaysia) as regulator of the scheme
- Tani Pool Malaysia (Members from the National Insurance Association of Malaysia or members from the Malaysian Takaful Association), representing individual insurers or takaful operators
- Ministry of Agriculture & Agro-based industry as a watchdog
- Baitul Mal or Zakah Malaysia (tithe collection agency of Malaysia) disbursing funds to the identified poor

Novelty

- To improve the socio-economic status of the farmer & the poor,
- To initiate collabouration between financial institutions and the farmers association forming an integrated network of suppliers or funds providers to reach out to the recipients, who demand them and the various entities monitoring the whole scheme,
- To support the government's policy of acknowledging the agricultural sector being the third engine of growth in Malaysia, and
- To encourage the set-up of a cooperative scheme where all parties stand to make potential financial gains.

Figure 1: Integrated risk financing & investment scheme for the low income and farmers in Malaysia – model 1



MTA: Malaysian Takaful Association

SUMMARY AND CONCLUSION

In many aspects, the Malaysian agriculture sector is technically lagging and this has impacts on the livelihood of the low income group and the hardcore poor. Appropriate and adequate measures need to be developed to ensure the rights of the small farmers, the destitute and the poor are protected. The farmers must continue to produce and the government must prevent their migration to other sectors to ensure the food supply is given top priority in the 10th Malaysia Plan.

These initiatives would require concerted efforts from many parties in order for it to materialise. Both the public and private sectors must collabourate for the sake of improving lives economically. The main thrust is to reduce dependency on food imports, especially rice; improve the marketing and production of the paddy growers who are the majority of poor in the society; and make the agricultural sector more profitable and sustainable. Profitability can only be achieved if losses are curbed. To achieve this, a form of risk financing technique, in this case through insurance, is recommended as a way to provide assistance to the agriculture sector, thus enabling it to be further developed. The setting up of Islamic insurance as a form of cooperative bodes well for the existence of the all familiar agricultural cooperatives. The scheme combines various microfinance models currently in use in many countries around the world. Other than emulating these models, the ingenuity in bringing the farmers' association and zakat institutions into the fold will accelerate the popularity of using this mechanism since these bodies have a structured and identified list of farmers and the poor and be able to reach out to as many potential recipient of the funds. On top of that, zakat institutions are critical in the network chains due to the availability and ready funds for disbursements. The central bank and the Agricultural Ministry form the regulatory body and watchdog respectively, overseeing the implementation of the scheme and to ensure transparency.

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INTERNATIONALISATION OF EDUCATION AND TOURISM GROWTH IN NEW ZEALAND: AN ANALYSIS FROM STUDENTS' PERSPECTIVE

ABSTRACT

The purpose of this paper is to examine the link between international education and the growth of tourism in NZ from the students' perspective. The study encompassed a survey which was conducted from the months of March to May 2009. Respondents for this survey were selected from the four universities in the Auckland region. The study found that there is a positive link between the internationalisation of education and the growth of tourism. The study further found that low cost tourism and shorter duration trips were preferred by international students and their relatives and friends. The study concludes that international education and tourism are significant industries for New Zealand and therefore necessary means should be taken to keep them sustainable. Findings of the study might be of interest for policy makers and researchers.

KEYWORDS

Exporting education; International students; Tourism; Family visits

INTRODUCTION AND BACKGROUND OF THE STUDY

The number of international students in New Zealand (NZ) is increasing every year. Their total number stood at 79,030 in 2001, 110,817 in 2004 and 90,934 in 2007 (Ali, 2010). There has been a remarkable growth of 15 percent between 2002 and 2007. A majority of international students in NZ come from China with 24,776 in 2007, or about 27 percent of the total number. International education generates $1.9 billion foreign exchange earnings and tourism generates $8 billion foreign exchange earnings each year. The key strengths of international education in NZ are its peaceful environment, worldwide recognition, and English language (Ali and Abbott 2010; Ali, 2010 and Ali 2008).

Tourism is also one of the fastest growing industries in NZ, contributing 9 percent to the GDP. New Zealand being a small country needs more awareness measures in order to popularise its tourism industry. Various campaigns are run from time to time in order to attract more international visitors.

In January 2009, the largest number of international visitors was from Australia at 82,684, followed by USA at 20,916. The number of international visitors in the friends and family category was also highest from Australia at 33,124 in January 2009 (International visitor arrivals to New Zealand, January 2009). International visitors who come under Visiting Friends and Relatives (VFR) category spend around $1,189 million in NZ.

Both international education and tourism are very important export sectors for the New Zealand economy. Ritchie (2003) states that as countries become more interdependent their growth and prosperity will mainly depend upon these two industries. As little research has been done in this field there is a need for further research. For the development of tourism strategy, it is vital to recognise the relationship between international education and tourism. International education is also included in the strategy to generate further awareness about tourism (Ali, 2010). It also sets the direction for government's role in various areas of international education. The growth in international education will in turn further contribute to the tourism industry.

The organisation of this paper is as follows: Section 2 describes an overview of the international education in NZ, while an overview of tourism in NZ is presented in Section 3. Section 4 describes the link between international education and tourism; Section 5 describes the field survey; Section 6 presents the findings; Section 7 presents statistical analysis; and Section 8 gives the conclusion and policy implications.

OVERVIEW OF INTERNATIONAL EDUCATION IN NEW ZEALAND

The demand of international education is increasing rapidly in NZ. By changing the immigration laws and exporting education, New Zealand has attracted a huge number of international students. Data from the Ministry of Education (2009) showed the number of international students in 2007 at 90,934.

NZ is preferred over other countries due to the ease of getting students visa, English language requirements, and also because it is easier to get permanent residence (PR) status. Parker (2009) states that by exporting education, NZ earns around $2.3 billion in foreign exchange in a year. The international education industry employs around 32,000 people. In 1990, there were less than 1,000 international students in NZ (Abbott & Xiaoying, 2009). Table 1 shows the enrolment of international students for the period of 2001 to 2007.

Table 1: International enrolments of students from 2002-2007 by provider groups

Providers	2001	2002	2003	2004	2005	2006	2007
Schools	10,555	15,259	17,448	14,477	11,984	13,933	15,207
PTEI	20,405	30,714	39,009	43,047	40,706	35,261	31,143
PTE	6,345	9,443	10,475	9,876	5,807	44,662	44,584
ELP	41,725	71,503	50,689	43,417	35,749	NA	NA
Totals	79,030	126,919	117,621	110,817	94,246	93,856	90,934

Source: Education Counts, 2008 cited in Ali 2010. Private Tertiary education institutions (PTEI); Private Training establishments (PTE); English language providers (ELP)

Table 1 shows that the number of international students increased sharply from 79,030 in 2001 to 126,919 in 2002. A large number of international students were in the ELP category but this figure was available till 2005 only. In 2001, out of a total of 79,030 international students, 41,725 or 53 percent of the total were studying in the ELP category. The total number of international students has been increasing from 2001 to 2003 but it started dropping from 2004 and reached 90,934 in 2007.

According to the Education Review (2009), international students are spending $600 million in terms of tuition fees and another $1.6 billion on living costs per year in NZ. Living costs include accommodation, groceries, entertainment, etc. The large presence of international students in Auckland boosted its economy by about $800 million, annually Living cost per student also varies by their country

of origin; Chinese spend around $17,870, compared to South Koreans who spend $22,898 per student. Korean students are spending higher than Chinese students ("Export education economics revealed," 2009). Though the data shows the living cost of international students, it fails to reveal the exact amount of tourism expenditure by international students.

In New Zealand, the level of contribution to GDP by international education is rising due to other factors like high home stay costs by primary school students, high spending on entertainment by English language students and high tuition fees by university students. According to a new research by the Education Review (2008), export education contributes around $2.1 billion to New Zealand's GDP. Export education also helps in employment as it employs one in 10 New Zealanders. Around 35,000 full time jobs were directly or indirectly linked to export education. Education is one of the highest value added industries of New Zealand, whose end product is knowledge, spreading directly to students. This shows the importance of international education to the economy.

OVERVIEW OF TOURISM IN NEW ZEALAND

The international tourism data from 2007- 2009 gives an idea of international visitor arrivals to NZ. It also tells about visitors' length of stay, purpose of visit and expenditure incurred by them. Table 2 shows that the number of international visitor arrivals to NZ fluctuates every year. Every year, the highest number of international visitors comes from Australia. In 2007, the number of international visitor arrivals from Australia was 74,676 and this figure has risen to 82,684 in January 2009. USA is the second highest international market for NZ, with 20,916 visitor arrivals in January 2009.

Table 2: International visitor arrivals for the years January 2007- January 2009

Country	2007	2008	2009
USA	22,624	25,984	20,916
Australia	74,676	80,881	82,684
Japan	12,236	10,121	7,532
Korea	14,028	10,846	6300
China	9,576	10,817	14,252
Singapore	1,652	1,537	1,680
Malaysia	812	870	980
India	1,204	1,595	1,596
Other	4,704	4,930	4,452

Source: Ali, 2010

Table 3: International visitor arrivals by purpose in March 2009

Purpose of visit	No of visitors
Holiday	1,159,534
Visiting Friends & Relatives (VFR)	743,424
Business	247,040

Source: Tourism News, 2009

Table 3 shows international visitor arrivals to NZ by purpose in March 2009. In March 2009, the number of international visitors under VFR category was 743,424. However, the highest number of visitors was under the holiday category. In the VFR category, the most number of days stayed was by Indians, who stayed for a period of 52 days, followed by Fijians, who stayed for 31 days. The length of stay was more in the VFR category as compared to the holiday category, except for Australians, who made 10 days in the holiday category and in VFR it was 9 days (Tourism News, 2009).

Table 4 shows total expenditure by purpose of visit in March 2009. As explained in the earlier tables, the largest number of visitors come under the holiday category, hence, the expenditure incurred by this category was $3,263 million. Expenditure incurred by the VFR category was $1,189 million.

Table 4: Total Expenditure on Tourism by purpose of visit in March, 2009

Purpose	Exp in $(millions)
Holiday	3,263
Visiting Friends & Relatives (VFR)	1,189
Business	808
Education	378
Other	309

Source: Tourism news, 2009

LINK BETWEEN INTERNATIONAL EDUCATION AND TOURISM GROWTH IN NEW ZEALAND

From the previous discussions on international education and tourism, it is assumed that there is some relationship between international education and tourism. Extensive literature is available on international education and tourism, but literature on examining the relationship between the two is far less extensive. Globalisation is one of the most important factors for growth of international education and tourism. Both international education and tourism have grown rapidly in recent decades. The main question is how does the international education contributes towards tourism. While there are studies carried out in the field of international education and tourism, the contribution of international education to tourism is still largely understudied.

For a small country like New Zealand, export education and tourism play major roles in getting a skilled labour force. According to New Zealand tourism strategy 2015, international education and tourism help the economy in getting skilled labour force. Tourism works in partnership with international education in order to get more skilled migrants. Both the industries are working together for the growth of the economy.

International education has become one of the country's biggest export earners, contributing $2.3 billion to the economy every year. An increase in the number of international students is a boost for the tourism industry as their friends and families often visit them. But there is a need for further research in order to study the relationship between both.

THE SURVEY

The main purpose of the study was to investigate the link between international education and tourism growth in NZ. To achieve this objective, a survey was conducted in 2009 by collecting data on the number of international students, their friends and relatives visiting them and the amount they spend on tourism. As a large number of tertiary education providers, both in private and public sector, is located in Auckland, and the international students are also concentrated in this region, this survey was conducted in the Auckland region.

A sample of 150 international students was taken for this study. Valid responses were 139, 93 percent of the total. Data was collected from four universities: Auckland University, Auckland University of Technology, UNITEC and Auckland Institute of Studies. The survey was done in four universities due to the concentration of international students in them. It was not possible to include more institutions due to the time frame and resource limitations. Questionnaires were distributed in the following manner: 36 questionnaires to the students of AU; 30 to the students of AUT; 30 questionnaires to the students of UNITEC; 40 questionnaires to the students of AIS; and 3 questionnaires were filled by those from other universities. The survey was conducted between the months of March and May, 2009.

The questionnaire comprised 17 questions, which were divided into two main sections. The first section was on demographics, which consisted of six questions. This section comprised questions like the age of respondents, countries of origin and the name of universities. It also integrated some other questions, like the level of study, and the duration of their stay and study in NZ. The main purpose of this section was to collect some information on the profiles of international students.

The second section was on tourism by family and friends, which consisted of seven questions. It collected some information on family and friends visiting the international students by asking their frequency of visit, the countries they often visit and the amount they spend on tourism. However, questions 4-5 were on international students only, in order to know how often they travel and contribute towards tourism. The main purpose of this section was to investigate the contribution of international education to the growth of tourism in NZ.

FINDINGS

The findings of the study are summarised according to the questions we asked the respondents. The first question was on the age of the international students. It was found in the survey that the highest numbers of international students in NZ were in the age group of 21-25, i.e. 55 percent. These findings were similar

to Ritchie (2003) who states that international students are youngsters. Twenty four percent were in the age group of 26-30; 15 percent were in the age group of 15-20; 5 percent were in the age group of 31-35; and only 1 percent was above 36. One of the respondents in the survey was only 16 years old; it is very interesting to see an international student of such a young age.

The second question was on the country of origin of international students. Response to this question revealed that the most numbers of international students were from China, followed by India. According to our survey, 26 percent of the respondents were from China, and this figure is also very similar to the data released by the Ministry of Education; The survey also showed that 21 percent were from India, and only 11 percent were from Korea.

The next question was on level of study. We found that the highest number of international students was studying in the Bachelor's course. Forty five percent respondents came to study in the Bachelor's programme, with only 21 percent in postgraduate studies. It is assumed that most of the international students start their career with a bachelor degree first. That is why the most number of international students was in the age group of 21-25. Sixteen percent of the students were in level 6 courses, with 11 percent in level 5 courses. This shows that besides bachelor and postgraduate degrees, international students study other courses like diploma, as well.

Respondents' length of stay while studying has been presented in Table 5.

Table 5: Length of stay in NZ

Length	3-6 months	6-9 months	1 year	2 years	3 years	4 years	5 years or more
No of Res	25	17	28	32	6	1	30

Source: Field survey

Table 5 shows the length of stay of international students in NZ. It can be seen from the above table that 23 percent of the respondents' length of stay in NZ was two years. Twenty-two percent of the respondents have been in NZ for a period of five years or more. There were 20 percent of the respondents who were here for one year only. A fairly large 18 percent of the respondents' length of stay was less than six months. The length of stay in NZ depends on the course which they are studying. But most of the Chinese students study in English level courses first, then do further business studies.

The last question of this section was on the duration of study in NZ. It has been found that 33 percent of the respondents' duration of study in NZ was three years and 32 percent was one year. As most of the international students were doing

Bachelor's degrees, the highest number of international students' duration of study was three years. Some 18 percent of the international students' duration of study was two years and 7 percent whose duration of study was four years. Another 4 percent of the respondents' duration of study was 6 years or more. Only 3 percent of the respondents' duration of study was less than a year. There was another 3 percent whose duration of study was five years. The duration of study depended on the course taken. As explained earlier, some international students do additional courses and that is why the duration of study is longer for them.

Section two of the questionnaire was on tourism by family and friends, which consisted of seven questions. The first question was on whether or not their family and friend visited. The second part of this question was, "if yes, who visited - friends, family or both?" Figure 1 shows whether family or friends visited NZ. It has been found in the survey that about 51 percent of international students indicated that their friends and family have visited them during their study in NZ, while 48.92 percent said that they never been visited. Some of the respondents said that their family and friends were planning to visit in future. There was only a small difference between the two responses and the reason for not visiting may be the cost of tourism, the country of origin of international students or the immigration policies of NZ.

The subsequent question was "Who visited NZ - friends, family or both?". Only 71 of the respondents answered this question. About 42.25 percent of the respondents who answered said that their family visited them during their study. Approximately 34 percent was of the view that both friends and family visited them and 23.9 percent said that their friends visited them in NZ. It is clear from the above figures that the highest contribution was from the family category. Most of the international students' parents come to visit their children in NZ, thereby contributing towards tourism. We asked the 'yes' respondents, how long did they stay in NZ? It was found that out of 71 respondents who said that their friends and family visited them, most of them stayed for four weeks. Twenty-four percent of the respondents said that they stayed for a period of four weeks. Twenty-two percent hold the view that their VFR stay was a maximum of five weeks and 15 percent said that they stayed only for three weeks. Eight percent said that their VFR stay was two weeks. It was different for everyone as respondents were from different countries. It depends on the visitors' countries of origin. If they are visiting from India, the tendency is to stay longer.

The next question was on the frequency of visits of friends and relatives. Out of the 124 respondents who answered this question, 29 percent were of the view that their friends and relatives have visited only once during the course of their study, and 18 percent said that their friends and relatives visit them once a year. Nine percent said they visit them twice a year. Only 2 percent said that they visit them once in every 2 years. Twenty-nine percent said they had not visited

so far and 14 percent said they were planning to visit. The frequency of visitors to international students, again, depended on their countries of origin. But according to the survey, most of the friends or family of international students visit only once during the course of their study and this may be due to high cost or other immigration policies.

In response to a question regarding the purpose of visit, we found that about 50 percent of the respondents' main purpose of visit was holiday and 17 percent of them visit other parts of NZ to meet their (VFR) friends and relatives. Nine percent of the respondents' main purpose of visit was recreation and 7 percent went outside Auckland for sightseeing and tourism. Only 4 percent of the respondents' main purpose was exploring. There was only 1 respondent who said that his main purpose of visit outside Auckland was for employment, which falls under the business category. Hence, significant contribution was from the holiday category.

The next question was on average expenditure incurred by international students on tourism. The number of respondents in this case was only 43. Approximately 63 percent of the respondents spent between $121 - $1,120 on tourism and 14 percent spent between $1,121 - $2,120. Nine percent spent between $2,121 - $3,120 and only 2 percent spent between $3,121 - $4,120. Five percent spent between $4,121 - $5,120 on tourism and only 2 percent spent more than $5,121. There were only 5 percent who spent less than or equal to $120. As the majority of international students travelled between 1-5 days, consequently 63 percent spent between $121 - $1,120 only. Hence, it shows that international students prefer low cost tourism as the maximum contribution came from the second category, i.e. $121-$1,120. As international education is vital for the NZ economy, the government should follow some measures to reduce cost of tourism for them.

We asked respondents, while their friends/ relatives come to Auckland, whether they visit other parts of the country? The survey showed that out of a total 71 respondents, 66 percent said yes and only 34 percent said that their friends or relatives stay only in Auckland and don't visit other parts. Most of the family or friends who visit international students go outside Auckland for holiday in order to enjoy the beautiful scenery of NZ or visit friends and relatives living outside Auckland. Some of the family or friends don't visit other parts. This may be due to high costs of travelling.

In response to a question regarding the purpose of visit, it is seen that out of the 47 respondents, only 31 answered this question. Twenty-nine percent of the friends or family's main purpose of visit was holiday and 26 percent was tourism. Nineteen percent of the respondents said that the main purpose of visit was to meet friends and relatives and 13 percent visit other parts for sightseeing. Six percent of the respondents said that the main purpose of visit of friends or relatives was recreation and 3 percent visit other parts for skiing. The highest number of friends or relatives main purpose of visit was holiday.

We asked respondents how many days they travel and the results are shown below.

Table 6: How many days of travel by friends or family?

Days	1-5	6-10	11-15	15-20
No of Res	12	22	1	1

Source: Field survey

Table 6 shows the number of days travelled by friends or family of international students. Only 36 respondents answered this question and most of the visitors travelled between 6-10 days. Sixty-one percent said that their friends or family travelled for 6-10 days and 33 percent travelled for 1-5 days only. Three percent travelled for 11-15 days and another 3 percent travelled for15-20 days also. Most of the friends or family travelled to other parts for 6-10 days only. This may be due to high cost of tourism. Hence, friends or family visiting international students also travelled for fewer days.

Our last question to respondents was while their family or friends stay in NZ, how much do they spend? The number of respondents in this case was 43 and the highest contribution was 65 percent of the respondents who said that their friends or relatives spent between $151 - $1,220 on tourism and 14 percent said that they spent between $1,221- $2,290. Seven percent said that they spent between $2,291 - $3,360 and only 5 percent said that they spent between $4,431- $5,500, as in the first category. Two percent said that they spend between $3,361- $4,430 and another 2 percent spent between $5,501- $6,570. The findings are again similar to figure 6. It is evident from the above figures that the low cost tourism is preferred by visitors of the international students.

STATISTICAL TEST

As the main objective of the study is to explore the link between international education and tourism growth in NZ, we wanted to see the strength of the link. In doing so, we have used the Spearman correlation method. It has been found that there is some relationship between international education and tourism growth, but to further verify the study some statistical analysis was carried out. The results of the analysis are given as follows:

The link between friends or family visits to international students and how often they visit is perfectly positive. The correlation coefficient ($r = .737$) and level of significance ($p = 0.01$). It can be seen from the above results that there is a strong positive relationship between the two variables. If the number of friends or family visits increases there will be increase in the frequency of visit of visitors also. Hence, it will help NZ's tourism growth.

The link between cities often visited by international students and their friends or relatives is perfectly positive ($r = .639$, $p = 0.01$). As the number of visits by international students to other cities besides Auckland increases, there will also be increase in the visits of the visitors. If the international students travel outside Auckland to other cities, their visitors will also prefer to visit other cities. This helps in tourism growth because both international students and the visitors visiting them travel to other cities besides Auckland. Hence, if more international students travel outside Auckland, it will lead to an increase in the number of visitors, as well as higher contribution towards tourism growth.

The link between days travelled, while visiting other cities and average expenditure incurred by friends or relatives on tourism is significant to some extent. The results of the statistical analysis are ($r = .481$, $p = 0.01$). Although the relationship is not that strong there is some positive relationship between the two. As the number of days travelled increases, the expenditure on tourism also increases, but only to some extent. If they travelled for more days then they would spend more and contribute strongly towards tourism growth. It is clear from the above analysis that international students contribute towards tourism growth but only to some extent.

The link between days travelled while visiting other cities and expenditure incurred by international students on tourism is significant to some extent. The results of the correlation were ($r = .405$, $p = 0.05$). As the number of days travelled by international students increase, the average expenditure also increases but only to some extent. The relationship between the two is positive but it is not strong enough. This is because 59 percent of the international students travelled for 1-5 days only. The results would have been stronger if they travel for more days because if they travel for more days, they will spend more on tourism. Hence, from the above results it is clear that there is a relationship between international education and tourism growth but it is limited to some extent.

CONCLUSION AND POLICY IMPLICATIONS

The main purpose of this study was to examine the link between international education and tourism growth in NZ from the students' perspective. The data was collected from four main universities AU, AUT, UNITEC and AIS, between the months of March and May 2009.

The results of the study were divided into two parts, descriptive statistics and correlation. The findings of the first part revealed that low cost tourism is preferred by international students and their friends or relatives. A majority of international students in NZ are from China and come to do their Bachelor programmes here. Most of the international students in NZ are in the age group of 21-25. A majority of the family or friends of international students visit them but nearly 49 percent never visited and were planning to visit in future. The reason for not visiting may be high cost of tourism or immigration policies of NZ. Family or friends' maximum stay in NZ was nearly four to five weeks, which again depended on the country from where they were coming from. Most of the family or friends visited international students only once during their study.

According to the survey, a majority of respondents go outside Auckland and visit other cities but there were some respondents who remained in Auckland, which again depended upon the financial stability of the international students. Most of the international students went to Queenstown for holiday and the main purpose of visit was holiday. This data was quite similar to the data released by the government. International students travelled for a maximum of one to five days and most of them spent between $121- $1,120. It can be seen from the above results that international students travelled for very few days and spent very little. Hence, low cost tourism is preferred by international students and the government should take some steps to reduce the cost of tourism for them as international education is vital for NZ's economy.

Most of the family or friends also visited other cities outside Auckland but there were some who stayed in Auckland only. The main destination of visitors was also Queenstown and they travelled for a maximum of 6-10 days. Their main purpose was also holiday and most of them spent between $151 - $1,220. Hence, it shows that visitors visiting international students also prefer to travel for fewer days and spend lesser money on tourism. In order to protect the tourism and international education industry government should take some steps to reduce cost of tourism for them.

NZ is one of the main destinations for tourists and Auckland is declared one of the fourth most beautiful cities in the world. As international education is vital for NZ's economy, the government should follow some measures to reduce cost of tourism for international students. Most of the international students don't travel due to their financial conditions. The friends or family who visit international students also prefer low cost tourism. As international students are contributing towards tourism growth, these sectors need further attention to maintain its sustainability.

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