

CHALLENGES FACING MALAYSIA IN EXPANDING ITS ISLAMIC FINTECH LANDSCAPE & POSSIBLE REMEDIES

Abubakar Ilyas

International Center for Education in Islamic Finance (INCEIF)
Kuala Lumpur, Malaysia

Kinan Salim, Ph.D

International Center for Education in Islamic Finance (INCEIF)
Kuala Lumpur, Malaysia

Email : kinansalim@gmail.com

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Abstract

Despite being a dynamic hub for the Islamic financial products and services, Malaysia's Islamic fintech landscape does not meet expectations. With a number of challenges such as stringent regulations, lack of adequate funding, shortage of a skilled workforce, fierce conventional competitors etc. the future growth and progress might only remain an unfulfilled dream if they are not addressed timely. This paper is aimed at critically discussing these challenges faced by such companies. Also it aims at proposing potential measures to overcome the highlighted issues. But in order to validate the mentioned challenges and the potential remedies, an interview based approach is employed. The top and middle management of five full-fledged Islamic fintech companies were interviewed with the aim of ensuring whether the mentioned challenges actually exist or not. And whether the proposed solutions are practicable. Based on the findings from the interviews, it is observed that almost all the mentioned challenges are recognized by the companies. Although not all were in consensus regarding every issue, but in general they saw the challenges as legitimate. The proposed solutions were also well received and recognized as beneficial for the companies. Another finding from the interviews was additional challenges the companies saw as worrisome, such as lack of awareness and technological ignorance among the masses. The paper concludes with the recommendation for the relevant authorities to address the highlighted issues with seriousness. Further research may be carried out to provide solutions for the additional issues pointed out by the companies.

A. INTRODUCTION

Those times are far behind us when a simple banking activity took a substantial amount of our time. Rapid technological advancements have drastically affected the financial services and are continuing to do so. Financial technology, known more commonly as 'Fintech', has totally transformed the traditional banking activities and has

made it possible for the banks' customers to bank with their smart devices. But this is just the tip of the iceberg as apart from the traditional banking activities, there are actual fintech companies and startups dedicated to provide advanced financial services to their customers in an extremely convenient manner. To put it in a very general way, fintech is reaching everywhere. From platforms to send and receive investments to takaful operations. From mobile payment applications to digital currencies, fintech is clearly thriving with all its might and changing the landscape of financial services. Despite the evident benefits of fintech and the obvious fact that it is here to stay and make many other financial services become extremely convenient, we see the Islamic finance industry lagging behind in this area. This could become a huge problem for the industry in the near future.

Malaysia, that is rightfully considered to be the global leader in Islamic finance, serving home to a number of dedicated Islamic banks and even more Islamic windows offered by conventional banks, having an attractive Islamic capital market and a wide Takaful landscape, also does not seem to be progressing in Islamic fintech the way it is expected to, given its leading position in the Islamic finance industry as well as the wide array of conventional fintech companies already operating in the country. Upon dwelling deep into this matter, it could be said that the industry is facing some serious challenges in progressing in the fintech arena. For starters the regulation of such companies is not helping it to flourish. Then the companies face the lack of adequate funding and generous investments. Then of course, the unavailability of the required knowledgeable and skillful workforce is also a major concern. And not to forget, there are the fierce conventional competitors that are quite hard to compete with. These issues among a few others are the major reasons behind the not-so-good performance of Malaysia in the fintech landscape.

This paper aims to address these issues thoroughly and to propose practical and appropriate remedies in order to avert them. An interview based approach is adopted for this matter and a few Islamic fintech startups are interviewed for primarily two purposes; to validate the challenges faced that are elaborated in this paper and then to validate whether the given remedies could actually help them grow and flourish. The paper is organized as follows: The second section following the introduction elaborates the major challenges faced by the Islamic fintech companies in Malaysia and the remedies to avert them. The third section sees the interviews conducted and explains whether the challenges and their remedies are actually valid or not. The fourth section states the conclusion and the way forward followed by the references for the paper.

B. LITERATURE REVIEW

Since its inception, the Islamic finance industry has been prone to multiple challenges and hurdles. Apart from a fierce competitor in the form of conventional financial institutions, there was a serious problem of the scant human resources in the Islamic financial services. Then there were the regulatory aspects and the effective supervision of the Islamic financial institutions (IFIs). Naturally, they required a supportive and conducive environment to work in, an atmosphere that allows them to grow and flourish with minimum unnecessary strings attached. And then there is always the ever-reluctant public that has, and still is, skeptical to the concept of Islamic

finance altogether. In short, the entire Islamic finance industry has been facing challenges since its birth and it still is.

Likewise, the Islamic fintech is also no exception to this. It is facing similar issues that are clearly impeding the progress of Islamic fintech. As mentioned, even Malaysia, the global leader of Islamic finance, has not yet come up with an attractive Islamic fintech landscape. According to the Fintech Malaysia Report 2019, there are only 6 Islamic fintech companies out of a total of 198. That is just 3% of the total fintech landscape. On the other hand, according to Datuk Nor Shamsiah Mohammad Yunus, governor of Bank Negara Malaysia; “Islamic banking is not slowing down; rather, it has been growing. The industry is propelling growth on its own, penetrating new markets and increasing market share” (The Star 2019). Thus, the overall popularity and constant growth of Islamic finance in the country does not positively correspond with its own Islamic fintech avenue. So obviously it is clearly facing some serious challenges. This section is divided into two parts with the first one aiming at highlighting and elaborating those challenges and the second, proposing remedies to avert them.

a. Major Challenges facing the Islamic Fintech Companies in Malaysia

Out of a number of different challenges, the most important ones that seem to be a major hurdle for the Islamic fintech companies are listed below.

1. Lack of Regulations or Extra Regulations?

According to the global head of Islamic finance, Fitch Ratings, Bashar Al-Natoor; “Regulatory limitations and concerns could hinder the ability of Islamic finance institutions like Islamic banks, Takaful, and fintech companies to forge ahead in adopting new models linked to various fintech themes such as P2P, crowdfunding and big data” (Sokhi). The need for the hour for the Islamic fintech companies in Malaysia is that they are efficiently supervised. But that does not necessarily mean that they are regulated to such an extent that it becomes hard for them to perform in a friendly environment. Appropriate regulation provides direction and vision, while a presence of too many regulations discourages the investors. Robin Lee of HelloGold, a digital platform for trading in gold, is of the opinion that there must be a balance that is maintained by the regulators (Whitehead 2018). How much control is too much control and can the regulators find a perfect balance between regulating the fintech companies and supporting them is the million-dollar question here.

It is understandable from the regulators’ part that they intend to ensure that all the security threats are mitigated, risks are efficiently managed, money laundering is minimized, there is hundred percent Shariah compliance etc. But doing that at the cost of a minimum fintech landscape might not be a good idea. Cryptocurrency is still not recognized as a legal tender in Malaysia, but surprisingly, blockchain solutions are legal which means that the business offerings are correct but its medium of exchange (coins) are not, which leads to a big dilemma. Then there is the regulatory sandbox under the Bank Negara Malaysia’s (BNM) framework with quite stringent restrictions that has raised quite some eyebrows within the fintech fraternity.

All these regulatory issues are shared alike by conventional and Islamic fintech companies alike, what is specific to Islamic fintech companies is that there are a lot of grey areas that are bringing uncertainty for such startups. Azleena Idris, Director of Corporate Services, PayNet says that the Islamic fintech startups are struggling to grow as there exists uncertainty on the regulatory side for such businesses and giving a clear direction would help them grow substantially (MDEC 2019). Umer Munshi, Co-Founder of Ethis venture also opines that a direction is the need of the hour and till now there is not much clarity (MDEC 2019). Dr. Habib from the International Shariah Research Academy (ISRA) also opines that the current guidelines are not comprehensive enough (Pikri 2019).

2. The Scarce Knowledgeable & Skillful Workforce

A specialized human resource has been the missing component in the entire Islamic finance industry since the beginning. A number of reasons could be attributed to this particular shortage, but there is no denying that there is a significant shortage. Either there are Shariah scholars or the finance specialists, but a fusion of both is indeed scant. The avenue of Islamic fintech is also facing the same dilemma, but this avenue, on top of the two mentioned specializations, also requires a technologically skillful workforce. Although Malaysia has a very impressive portfolio of successful educational institutes providing education in Islamic finance and based on the Global Islamic Finance Education report of 2013 by (Yurizk 2013), it actually ranks second, just behind Pakistan as the highest Islamic finance education provider. But providing knowledge specific to financial technology is still lagging behind. Mr. Ridzuan, one of the founding members of the Fintech Association of Malaysia, says: “What we have is pockets of people who know about Islamic finance on one side, and financial technology on the other side, and there is a gap in between. That’s the biggest problem” (Fintech Summit 2018).

(Jamil and Seman 2019) discuss in their studies that although many universities are providing theoretical knowledge on Islamic finance, but there still is a lack of relevant skills to work and innovate in the area of fintech.

Similarly, the students of classical Shariah although are equipped with in-depth theoretical knowledge of classic Islamic jurisprudence, but again lack the applied and innovative part which is actually required. As far as the modern finance and financial technologies are concerned, they do not even exist in institutions providing classical knowledge of Islamic jurisprudence. This leads to debate between the Shariah scholars that ultimately ends up with a confused and skeptical public. There is no denying that Shariah compliance is the most important aspect of any financial product that is stamped with ‘Islamic’, but in order to give a ruling on a latest technology, it is imperative that it is thoroughly understood. This part is actually what is missing. If a Shariah ruling is given after this process of thorough comprehension, then it must be given the utmost importance. Therefore, there is a serious mismatch between the demand and supply of people that are specialized in all three areas of Shariah, finance and technology not only in terms of knowledge, but also in practical skills and innovation.

3. Lack of Substantial Funding

This is another issue that is shared by both conventional and Islamic fintech startups and that is the unavailability of substantial funds for fintech companies. There is a reason why the economically thriving neighbor of Malaysia, Singapore is far ahead of Malaysia in fintech. According to Mr. Lee from HelloGold, Singapore will always have a competitive advantage over Malaysia as it able to attract more tech startups due to the generous availability of funds, and that the entrepreneurs naturally go where the money is (Whitehead 2018). Actually there are two issues under discussion here; the funding needs of Islamic fintech startups are not met and, because of that, they do not have any option but to move to other jurisdictions like Singapore where they are funded substantially, which results in the exit of domestic potential from the country.

A major reason behind this could be the volatile situation of the Malaysian economy over the past few years. Although, it is moving upwards, but definitely not playing up to its potential. The deputy economic minister, Mohammad Radzi, announced at the start of last year that the country is expected to experience moderate growth due to the challenging external factors (The Star 2019). Those factors are still alive, plus the fatal Co-vid 19 outbreak that has forced the whole world in a global lockdown. The lockdown in Malaysia started from the third week of March in 2020 and is still underway while the country enters the month of May. The disastrous economic impacts of this are evident and are likely to pull back the investors a whole lot more. Then there is the situation with India over palm oil trade. Plus the sudden and unexpected crash in the oil market in April in which for the first time the world saw oil prices dropping below zero. Thus all these external factors suggest that the volatility may remain for a while. Naturally, situations such as these discourage investors and keep them on a back foot. Then funding fintech startups, specifically Islamic fintech startups in such situations, is a tricky endeavor that most are unwilling to take. Shankar Kanabiran, partner and Malaysia Financial Services Banking & Capital Markets Advisory leader at Ernst & Young Advisory Services SdnBhd further explains; “As with most start-ups, fintech firms may find themselves limited by funding options. Venture capitalists and banks are often the first port of call for fund-seekers, although most will not take on the credit risk of companies with a track record of less than three years” (New Strait Times 2018). And speaking of venture capital firms, according to the Islamic fintech report of the Malaysia Digital Economy Corporation, the venture capital environment in Malaysia is not mature enough to meet the financial needs of Islamic fintech startups (MDEC 2019).

If lack of funds is a challenge facing fintech startups, then it is even bigger for Islamic fintech startups as they have to prove more to the fund providers. The business plan, feasibility reports, risk aversion plans, Shariah compliance and most importantly, how are they any different from the conventional fintech companies are all areas that need to be satisfied by the Islamic startup.

4. The Fragmented Eco-System of the Islamic Finance Industry

Although the overall growth of the Islamic finance industry in such a small period of time is nothing less of phenomenal, but the industry within itself is quite fragmented instead of being one single

integrated unit. Mr. Mohamed Damak, the global head of Islamic finance at Standard & Poor's, is of the view that the fragmented nature of the Islamic finance industry is what is actually holding it back, there is no integration between the different players from multiple areas of the same industry and there is limited interaction between them (Fintech Summit 2018). The fragmentation is naturally due to different legal regulations and local laws and norms, but the *raison d'être* behind the fragmentation is probably the different opinions of the Muslim scholars in different areas and sometimes in one single area. There is no denying that these differences in opinion are a blessing in disguise for the general masses, but in order to elevate the bar of Islamic finance and bringing it forward as a worthy competitive force to the conventional finance, standardizing the issues related to *Muamalaat* might not be a bad idea. The problem right now is that scholars are giving diverse opinion regarding Islamic financial products, it cannot be said that they are wrong as all of them could be right in their own way, but there is no denying the fact that it impacts the global Islamic finance industry in a negative manner. This is also the main reason why quite a substantial amount of Muslims are even skeptical to the whole concept of Islamic finance. Mr. Craig Moore, founder and CEO of Beehive, a Dubai-based peer to peer finance platform, is of the opinion that an eco-system that consists of two layers; regulatory and scholarly, impedes the progress and growth (Fintech Summit 2018). Although this is not much of an issue inside Malaysia after the establishment of Shariah Advisory Council (SAC) on Islamic finance by the BNM in 1997, but in other Muslim countries such as Pakistan and Bangladesh, this is an issue which has confused thousands of people over the whole concept of Islamic finance. Therefore, this could prove problematic for the fintech companies in Malaysia when they try to extend their operation outside the country.

5. Fierce Conventional Competitors

This is the same challenge that the entire Islamic finance industry still faces. The conventional finance industry has been around for ages and is naturally way more established. Fintech is not a very old avenue but still the conventional finance has a strong hold there as well looking at the number of conventional financial institutions. As mentioned before, the Islamic fintech companies just make up 3% of the total fintech landscape in the country, the rest is in the hands of its fierce conventional competitors. This is because the conventional financial institution and fintech startups have very little to prove. As long as they satisfy their clients with huge profits and the regulators with abiding by the laws, they are good to go. IFIs and Islamic fintech startups come with a lot of strings attached. The most difficult thing for them to do is to compete with their conventional competitors while staying Shariah compliant plus they have to give solid switching reasons to people who are accustomed to the conventional financial setup.

Ibrahim Khan, the founder of the popular IslamicFinanceGuru.com, clearly says that the Islamic fintech companies have two main challenges, first they have to convince someone to switch from a traditional bank to a digital one then they have to convince the same person to not go to the conventional digital bank but the Islamic digital one, which is smaller than the former (Woodford 2020). Thus, the Islamic fintech startups in Malaysia have a lot on their plate, if they cannot satisfy the people and fail to

give them attractive incentives in order to switch from a conventional to an Islamic startup, people have a strong reason and a rich portfolio of 192 conventional fintech startups to turn to. Hence, the competition is literally intense.

The challenges listed above are, in the author's opinion, the ones heavily impeding the growth of the Islamic fintech startups. Apart from the ones mentioned, there are numerous others as well; ethical issues regarding the digital working mechanisms such as data sharing, educating the already reluctant public on how Islamic fintech companies are different and better than their conventional counterparts, ensuring 100% Shariah compliance etc.

b. Ways to Handle the Challenges Successfully

The challenges elaborated in the previous section have shed enough light on why the Islamic fintech landscape in Malaysia is not up to par. As the reader may have observed, the challenges discussed are even a hurdle in the way for conventional fintech companies with the exception of the last one, thus they become even more challenging for the Islamic fintech startups due to reasons we mentioned while explaining the challenges. Now the obvious question that naturally comes to mind after the last discussion is; '*How to survive in such unfriendly conditions?*'

This section aims at answering this question. Fintech is, without a shadow of a doubt, the present as well as the future. It is quite evident that the situation we see today is going to be much more advanced in terms of technology in the very near future. Therefore, the Islamic fintech companies must find their way through these challenges soon in order to stay strong and competitive today and tomorrow. Possible ways that these challenges are faced and avoided are discussed one by one.

1. Striking the Accurate Regulatory Balance

It was mentioned clearly while elaborating the regulatory challenges face by the country's Islamic fintech companies that it is imperative for the regulators to hit the bull's eye in their regulations. Moderation is the key word here, neither too many regulations for the sake of consumer protection and illegal activities, nor too less regulations for the sake of promoting the industry. It cannot be claimed that the Bank Negara Malaysia (BNM) is neglecting this area as it is among those countries which have introduced the regulatory sandbox frameworks to cater the development of the fintech industry, and it is taking several initiatives with multiple entities such as the Malaysian Digital Economy Corporation (MDEC) and the Securities Commission to conduct regular fintech workshops (IMF 2020). However, more work must be done to efficiently supervise, eradicate the grey areas, promote Islamic fintech companies specifically and build the confidence level of such startups. In 2018, a fintech census was conducted by EY among the ASEAN countries inquiring them of the challenges they were facing while operating in the market. 87% of the respondents were of the view that it was either moderate or difficult to conform to local regulations. 78% believed that the government should increase its funding, give tax rebates for the development of the fintech landscape (Bellens, Liew, Thung 2020).

Therefore, the only way to solve the regulatory issues for the Islamic fintech startups is, as we suggested, 'striking the accurate regulatory balance'. Malaysia is already a champion in the Islamic finance industry with such a vibrant Islamic finance landscape. It must adopt similar strategies for the fintech startups as well. Malaysia could also learn from Singapore, a country where entrepreneurs and startups are most attracted to work in. The same census of 2018 shows that the Singapore based firms finds the regulatory environment relatively easier to conform to.

2. Equipping the Youth with the Required Knowledge & Skills

This is another issues which needs to be handled by the state-level policies and Islamic fintech companies can only hope that this issue is resolved and they are able to get the required manpower at the soonest. The issue could be addressed through a two-way solution; a long-term knowledge and skills based solution and a short-term knowledge based solution.

The long-term solution is basically changing the curriculums of the academic institutions. As we are living in the industrial revolution 4.0, the future generations must be equipped with the necessary tools to survive. However, strictly in terms of Islamic finance and fintech, the appropriate knowledge in different levels of education must be taught. The primary and elementary levels of education could include the basic knowledge of Shariah, finance and technology, while the advanced levels could include the knowledge related to Islamic finance and fintech. Specializations in Islamic fintech, along with hands-on experience, must also be introduced just like specializations in Islamic finance. Malaysia already has the advantage in this area. Bank Negara Malaysia (BNM) has even established a dedicated institute for the production of human capital in Islamic finance; International Centre for Education in Islamic Finance (INCEIF), which is the only Islamic finance university to be honored with an AACSB accreditation. Therefore, Malaysia can definitely capitalize on this and must focus on equipping the students not only with the required knowledge but with the required skills as well. Seminaries must also not be excluded from these reforms. Recently, students from a notable seminary in Pakistan; Jamia Baitul Salam, won a robotics competition conducted by HITEC University Taxila (Pakistan), by beating competitors belonging to 20 other universities (Rabbie 2019). This proves their remarkable potential even though the seminary students in Pakistan are often stereotyped with being orthodox and old-fashioned. If anything, they could contribute even more as they are the ones studying classical Islamic jurisprudence.

As far as the short-term knowledge based solution is concerned, as Malaysia currently has a number of students graduating with degrees in Islamic finance, the state, the student's own university or even the fintech companies could sponsor them in taking short online courses in Islamic finance. Prestigious universities such as Harvard, Duke and Columbia are providing short online courses on fintech with certifications spanning from six weeks to six months. Such short courses will help the graduates to get a quick in-sight with the current happenings in the fintech universe. Likewise, Islamic scholars well-versed with Islamic finance could also be sponsored for such courses.

Both these solutions must be given serious thought by all the players in the Islamic finance industry, as looking at the fast pace of technological advancements, it will become even more strenuous to deal with this problem in a few years' time.

3. Bringing in the Money

As mentioned earlier, Malaysia's neighbor Singapore, has quite a competitive advantage over Malaysia in terms of generating substantial funds for tech startups and businesses in general. Singapore's business-friendly policies is one of the main reasons why it is considered as a paradise for entrepreneurs. For more than ten years, World Bank has ranked Singapore in the top three countries among a total of 190 countries for its ease of doing business. Singapore ranked number 2 out of a 190 countries in the year 2019 (Doing Business 2019). Recently, CorporateServices.com conducted a survey of more than 100 startup founders from five countries; India, Poland, UK, USA, and Ukraine. The survey was to find out the destination these startups would prefer to operate in terms of various factors. Singapore was ranked number 1 in all those factors. Apart from its ease of doing business policies, a major reason for those startups to set up in Singapore was 'Access to Startup Resources' (Corporate Services).

The Singapore government provides various types of assistance such a cash grants and equity financing services to local tech startups in the country. After qualifying the eligibility criteria, startups receive the necessary grants. The criteria to qualify is also not that stringent. Many resources are available just be incorporating a startup. Apart from government assistance, there are other sources of funds such as 'Angel Investing Networks', individual who invest in startups at their seed stage, venture capital firms, private equity firms etc (Startup Decisions, n.d.). Moreover, Singapore market allows the free movement of international capital. The cherry on top would be that it highly encourages foreign investment through convenient policies. Foreigners do not need local shareholders, there are no restrictions on the amount of capital brought inside the country, no restrictions on foreign currency movements and no restrictions on repatriation of profits(Startup Decisions, n.d.).

Now the question is, can fintech companies in Malaysia solve their funding problems similarly? It would be unfair and unrealistic to say that Malaysia should incorporate all the steps Singapore is taking in order to solve its funding crisis as there is quite a difference between the economies of the two countries. However, Malaysia can definitely take a leaf or two out of Singapore's book.

Malaysia is already open to foreign investors with free inflow and outflow of capital. The country is already at par with Singapore in this matter. What it can do more is provide attractive packages and incentives to foreign players investing in specifically the country's Islamic fintech startups. Malaysia can also capitalize on its status as the global leader in Islamic finance and attract funding for Islamic fintech companies. Once the foreign funding starts pouring in this sector, local investors may be automatically encouraged to invest themselves.

Apart from the government playing its part in providing assistance, the involvement of private entities is equally crucial. Islamic banks can play a very important part here. AlBarakaGaraj Islamic bank of Turkey has built the world's first startup acceleration center. It aims at providing all types of assistance to Islamic fintech companies from mentorship, financial assistance and even an opportunity for the company to be acquired by the bank itself. Then there is the B2B (bank to bank) collaboration adopted by Bahrain as the Islamic banks of the country are pooling resources for research and development in Islamic fintech solutions. Their aim is to launch 15 fintech platforms by the year 2022 (MDEC 2019).

Therefore, these are a few areas on which Malaysia can work and solve the financial issues faced by the Islamic fintech companies. Already open to international investment and having a substantial number of quality Islamic banks, it is not an impossible feat. Apart from this, there must be separate research to find out the reasons behind reluctance of the private investors in investing in fintech companies, especially in Islamic fintech companies despite the evident situation that fintech is the present and the future.

4. Integrating the Scholarly & Regulatory Layer

This particular issue in the whole Islamic finance industry is not just faced by Malaysia but by a significant number of countries. The industry was, and still is being labeled as nothing but a provider of the same services as the ones provided by the conventional institutions with the exception of an Islamic name attached to it. Even if the regulatory authorities allow a certain practice and deem it Shariah compliant, a different opinion from a revered Shariah scholar would pull back a substantial number of people from availing that particular service.

This is a very serious issue indeed and cannot be tackled in a year or two. It requires a serious effort from the relevant authorities of the Muslim majority nations. Just like Malaysia did by establishing SAC.

A long term solution of this challenge is to reform the curriculums of all educational institutes as mentioned earlier. In this regard, students at the seminaries must be provided with adequate knowledge of the modern financial services as they are the scholars of tomorrow. They could critically analyze the Shariah compliance of the available services during their learning tenure. And it is very likely that they come up with better alternatives with even more Shariah compliance. But that will only be possible if they are educated in a specific manner.

The scholars themselves should equip themselves with the latest on goings in the Islamic finance world. Instead of taking a very strict approach without a thorough insight might be doing the whole Muslim ummah more harm than benefit. Islam teaches us to make ease for each other instead of difficulties. The Quran says: ***“Allah intends (to provide) ease for you and does not intend (to create) hardship for you.”*** (Al-Baqarah: 186). The Prophet (pbuh) says to his two companions, Mu'adh and Abu Moosa, while sending them to Yemen; ***“Treat the people with ease and do not be hard on them; give the***

people glad tidings and do not fill them with aversion; and love each other, and do not differ” (Sahih Bukhari: 3038). Of course, all this is subject to limitations prescribed by Shariah, and one cannot go against an explicit ruling of Quran and Sunnah in order to provide ease. But where there is a space for allowances, the Muslims living in the challenging world today do deserve it more than ever.

Thus, if every stakeholder plays their role effectively, the fragmented ecosystem of the Islamic finance industry can definitely become a single and united ecosystem with one regulatory and scholarly layer.

5. Competing Bravely & Smartly with the Arch Rivals

This challenge is something that is going to stay for quite a while looking at the ultra-strong conventional finance industry and its loyal customers, among Muslims and non-Muslims alike. As mentioned earlier, the total number of full-fledged Islamic fintech companies in Malaysia is six, which makes up only three percent of the total fintech landscape. This number alone suggests the fierce competition.

Now what the Islamic fintech startups must do is not only to compete bravely but also smartly. It would be very difficult for them to come at par with the other startups by providing the same service in a Shariah compliant manner due to a number of reasons mentioned while elaborating on this challenge. If we look at the available fintech companies, they are providing the same services as their conventional counterparts. EthisKapital is a crowdfunding platform, PayHalal is an e-payment service etc. What Islamic fintech companies must realize is that their conventional counterparts are already strong in these avenues. While we cannot deny the need for the Shariah compliant alternatives for such fintech products, at the same time it is also necessary for the Islamic fintech companies to come up with products specific to them in order to get that competitive advantage and acquire a significant market share. One of the recommendations presented in the Islamic Fintech Dialogue organized by MDEC earlier this year was to form an Islamic fintech niche (MDEC 2019). It was stressed upon to begin the digitalization of Zakat, Sadaqah, and other Islamic financial social services in order to create that niche in the market where the Islamic fintech companies can capitalize and gain an advantage over their conventional counterparts. This would allow such companies to sustain themselves in the market and when they have gained the confidence of the public, they could definitely start offering the basic services of fintech as well such as e-wallets, crowdfunding platforms etc.

C. FINDINGS FROM INTERVIEWS WITH THE ISLAMIC FINTECH COMPANIES

As mentioned in the introduction, this paper's aim is not merely to list down the challenges faced by the Islamic fintech companies in Malaysia, and suggesting a handful of remedies. Rather, this paper aims to see if the mentioned challenges are existent or not. And to see whether the suggested remedies will be really helpful in the country's context or not. Therefore, in order to achieve these two targets, interviews were conducted with the top

management of five Islamic fintech companies in Malaysia to validate the challenges as well as the suggested remedies. Due to the ongoing covid-19 crisis, the interviews were carried out online. Following are the companies which were interviewed:

For the purpose of maintaining the confidentiality of our interviewees and their thoughts, the interviewees will be referred to in the coming sub-sections as Participants A, B, C, D and E.

a. Validating the Challenges

The challenges mentioned in section 2.1 are validated here one by one with the same sequence.

1. Regulatory Issues

There were mixed opinion regarding the highlighted regulatory issues. Two of the participants considered it as a major challenge. According to participant A, registering the company and obtaining a license was the biggest challenge the company faced. Participant D also confirmed this as one of the main challenges faced. Both the participants agreed that the regulatory aspect of fintech companies is a bit unclear and insufficient. Participant A also opines that fintech companies do not want to be heavily regulated, they just want to be treated normally as a tech company. Regarding the regulatory sandbox framework of the BNM, both the participants criticized it for its stringent requirements and quite a lot of red tapes to go through.

On the other hand, participants B and C had a different view. Both were of the opinion that the regulations are satisfactory in general. Even though both recognized the issue of the lengthy procedure of obtaining a license, but gave a satisfactory nod to the overall regulatory aspect of the fintech companies in the country.

Participant E did not comment much on the regulations as they did not have much impact on the nature of his company's business model. He also was satisfied with the sandbox framework.

It must be noted here that the participants who did recognize the regulatory aspects as a challenge for their company were in fact the CEOs of their companies. And the ones who did not see it as much of a challenge were people a bit lower in the management hierarchy. Therefore, it could be deduced that the mixed opinions were due to the difference in the perspectives of the top and middle managers.

2. Human Resources

Regarding the issue of the lack of a knowledgeable and skillful workforce in the Islamic fintech industry. There were more or less similar opinions from our participants. Participants C, D and E validated this challenge, and all of them agreed that the area in which the workforce is lagging behind in terms of skills, is the technological area. Participants D and E also stressed upon the fact that a workforce that is good at multi-tasking is the workforce that is actually required. Participant E further added that the industry would surely progress at a faster pace if this issue is taken up. Participant C made a very

interesting comment and said: “*Our graduates are good for corporates but not good for startups. For startups, a dynamic workforce with a mindset to grow is required.*”

On the other hand, participants A and B did not see this as a significant challenge, and were of the view that there is no lack of talent in the country. And that they can always outsource the operation in which there is a problem regarding a talented workforce. Participants A and D have already outsourced some of their operations and have overcome this challenge.

3. Funding Issues

Three participants validated the highlighted challenge of acquiring funding from different institutions. Participants A, C and D were all of the opinion that it is challenging to get the required funding from investors as well as the government. According to participant A, there are only a handful of Islamic VCs in Malaysia to get funds from. Participant C also confirmed this and recognized the lack of *Shariah* compliant instruments in the country. All these participants also agreed that it is even harder to acquire funds with the ‘Islamic’ label. Many of the VC firms are of the view that the company will only be targeting the Muslims, which is far from truth. But that is why they are reluctant in investing. Participant D told that due to the lack of funding, their company is self-funded up till now.

Only participant B was satisfied by the funding so far, but did recognize the lack of funding and support from the government.

Participant E did not comment much on the matter due to the company still being in its early stages, but did recognize the fact that the investors are apprehensive when they see that the company is ‘Islamic’.

4. The Fragmented Eco System

There was almost a consensus on the non-recognition of this issue and four participants, except for participant A, agreed that there is no such issue in existence. All agreed that there are no such diverse opinions from the scholars in Malaysia plus the regulatory bodies make it easy for the public and the companies to wipe out any *Shariah* related ambiguities.

Participant A himself did not face any challenge related to this, but validated this issue in general and that it does hinder the overall progress of the Islamic finance industry.

5. Competition

Most of the participants invalidated this challenge as well and did not consider this much of an issue. Participant A was quite optimistic in competing with the conventional competitors and welcomed all sorts of competition.

When asked whether being ‘Islamic’ makes it hard for them to compete, all were of the opinion that it only provides them with an opportunity and an extra competitive edge. As they have something which

their conventional competitors don't, and that they can cater to the Muslim markets in a better manner than them. According to participant C; *"being Islamic only puts you ahead of your competitors."*

However, participant E had a mixed opinion and recognized the fact that due to the fact that they are an Islamic company, the non-Muslim customers think that they only cater to the Muslims. But overall, he also invalidated this issue in general.

b. Validating the Proposed Solutions

The proposed measures to tackle the challenges mentioned in section 2.2 are validated one by one in the same sequence.

1. Balanced Regulations & Incentivizing the Islamic Fintech Companies

As only two participants; A and D validated the regulatory challenges, both of them agreed to the proposed measure of provision of a balanced set of regulations for the Islamic fintech companies. Participant A explicitly said: *"Leadership and guidance from the regulators is what we require now. Regulators should play their part and build an effective eco system. And building an eco-system without regulations could take years."* Participant D also approved of this and said that a proper regulatory balance would definitely stimulate innovation. Participant E, despite not considering it as much of a challenge, did validate the fact that balanced regulations are required, otherwise the scenario could be chaotic.

Interestingly, two out of the other three participants who do not consider the regulatory aspects challenging; B and E, validated that there should be some extra incentives for the Islamic fintech companies per se. Participant B reasoned his suggestion by saying that most of the Islamic fintech companies are going bankrupt after four or five years due to the lack of incentives. Participant E agreed to special incentives for Islamic fintech companies for the overall growth of the Islamic finance industry. And even if it projects biasness from the regulators part.

However, participant C did not like the idea of special regulatory incentives for such companies as it would disrupt the level playing field. He suggested that it is up to the Islamic fintech companies to compete and up their game.

2. Overcoming the Human Resource Challenge

Participants A and B did not have much to say regarding the proposed measures to overcome this challenge as both of them did not consider it to be challenging. As far as the other three participants are concerned, all of them agreed that knowledge regarding technology and *Shariah* should definitely be provided from an early stage of education.

When asked whether the students of seminaries should be equipped with the required knowledge of modern techniques of finance and latest technology, all participants strongly supported this idea.

Participant C even went on saying: “*without it those students are merely a waste of resource.*” Participant E also suggested that those students should be equipped with the required technological skills as well.

As far as the short online courses provided by universities regarding fintech are concerned, most of the participants did not consider it as an appropriate solution as such courses mainly provide an ‘understanding’ of fintech. They do not help much on enhancing the technological skills which is the actual problem. However, participant E recognized the short courses as helpful for the workforce.

3. Enhancing the Provision of Funds

Participant A did not comment much on the proposed measures to enhance funding. And as participant B did not consider it as much of a challenge, the solutions were not properly addressed.

When asked whether the government should come forward to fund such companies, Participant C was of the opinion that govt. has already taken a few initiatives which are good. Although their company did apply for funds but were not approved. Participant D was in strong favor of this measure.

When asked whether Islamic banks should partner with the Islamic fintech companies to solve this dilemma, participant D saw it as a good solution but added that the Islamic banks see them as competitors so that is unlikely to happen. Participant E also had the same reservation and said that the chances of getting funds from Islamic banks are quite bleak as they consider us as competitors.

When asked about attracting and encouraging foreign investment, participant D strongly supported the idea.

4. Integrating the Fragmented Eco System

As almost all the participants refused to recognize this as a challenge hindering their progress and growth, the proposed measures to solve it were left unaddressed. Only participant A, who saw this as a general threat for the Islamic fintech companies, agreed that if the overall curriculum of the early stages of education is changed to incorporate the discipline of *Shariah*, the problem is likely to be addressed in the future.

When asked whether it is feasible to invite scholars holding a different opinion and providing them with an insight of the operations, and holding dialogues and healthy discussions could work to solve this issue, participant A saw it as a very healthy and positive approach.

5. Competing with the Conventional Rivals

Even though almost all the participants did not consider competing with the conventional competitors as a big challenge, some of them did have thoughts on the measures proposed in this paper. Participants B and E agreed to the proposed measure that finding untapped markets, focusing on the Islamic social financial services and finding a niche is a wiser and preferable way to go for the Islamic fintech companies than replicating the conventional services already provided. Speaking on providing common financial services provided by the conventional fintech companies with just an Islamic label,

Participant E went on saying: *“It’s better to specialize and excel in that rather than being jack of all trades and master of none. It is also not logical to ‘halalize’ everything.”*

However, participant C had different thoughts. He said: *“no financial service should be left by the Islamic fintech companies, as even the simplest fintech product such as an e-wallet could be subject to Shariah non-compliance practices without the knowledge of its Muslim clients.”*

c. Finding out Other Challenges

Apart from validating the issues and their proposed solutions from the interviewees, they were ultimately asked other challenges which they see as major hurdles and they have or still are facing. Following are what they mentioned:

1. Tech Ignorance in Senior Citizens

Participant B was of the opinion that they cannot target a very large segment of the population i.e. the elderly, due to them not adapting to tech based financial services.

2. Lack of Subsidy Initiatives for Foreigners

Participant C highlighted a very important issue i.e. all the government initiatives and funding packages are only available for locals. This discrimination hinders the residents of other nationalities from giving reality to their dreams.

3. Lack of Awareness

Participants D and E pointed out that a major challenge that they are facing is the lack of education and awareness among the general masses. Thus, they first have to run awareness campaigns, educate their clients about their services and then comes the actual marketing part.

D. CONCLUSION & THE WAY FORWARD

This research aimed at highlighting the major challenges being faced by the Islamic fintech companies in Malaysia. It was necessary to do so as the Islamic fintech landscape in the country does not match well with its dynamic Islamic finance industry. Challenges were elaborated thoroughly, and some measures were proposed in order to overcome them. The challenges and the remedies were then put in front of five full-fledged Islamic fintech companies for their validation. Upon doing so, it was observed that the biggest challenge the companies were facing was of acquiring adequate funds from the private and public sectors. This was followed by the regulatory challenges they faced such as obtaining a license, unclear regulations etc. Issues related to human resource and competition received mixed reviews with some of the participants recognizing it as something problematic, while others not much worried about it. And the issue regarding the fragmented eco-system was discarded as a challenge altogether. It was encouraging to see that most of the measures proposed in this research were validated by the participants. A balanced regulatory framework, encouraging foreign investment and government coming forward to fund such

companies in order to solve the regulatory and funding challenges were validated as sound measures to promote the Islamic fintech companies. Even the participants who did not recognize the challenges relating to human resources and competition, agreed that the proposed measures will bring good anyways to their companies.

Therefore, it can be concluded that the challenges highlighted in this research, along with the ones pointed out by the interviewees, are actual challenges faced by the Islamic fintech companies. Thus, they should be addressed seriously. And in order to solve them, taking up the proposed measures in this paper are most likely to produce favorable results based on the opinions of the companies that are presently working in the industry. There is no doubt that the future of financial services is already here upon us. And with the covid-19 entrapped global economy, fintech will be receiving tremendous attraction from all segments of the society. Hence, now is the time to act and improve the fintech landscape in general, and the Islamic fintech landscape in particular in order to benefit from the fruits of the future.

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