# Title: An Integrated Model of Islamic Social Finance Towards Sustainable Funding

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**Abstract:**

*This paper explores the evolving landscape of Islamic social finance and its crucial role in alleviating the socio-economic repercussions. Islamic social finance, sharing similarities with conventional social finance, constitutes a four-part ecosystem involving social welfare initiators, social finance providers, social ecosystem coordinators, and beneficiaries. However, Islamic social finance incorporates principles aligned with Shariah, featuring instruments like zakat, sadaqah, and waqf, which have gained prominence, particularly after the Mywakaf initiative by Bank Negara Malaysia and the Association of Islamic Banking and Financial Institutions Malaysia in 2017. Effective coordination among stakeholders is essential to achieve projects with significant social impact, demanding a robust Islamic social finance ecosystem rooted in Shariah principles. While the concept is still predominantly theoretical, a call exists to develop and adopt an integrated Islamic social finance model. This paper aims to discuss Islamic social finance tools and propose adopting such an integrated model.*

**Keywords**: *Islamic social finance, Zakat, Waqf, Integrated model, Sustainable funding*

## 1. Introduction

Islamic social finance is becoming a more popular product offered by almost all Islamic financial institutions in Malaysia as it fulfils the Maqasid Shariah, preserving the benefits and preventing harm. Although it carries a nearly similar objective and element to conventional social finance, the Islamic social finance sector has its institutions and instruments aligned with Shariah principles (IRTI, 2014). *Zakat*, as one of the instruments, has already been embedded as part of the Islamic banking primary obligation, while *sadaqah* and *waqf* only started to be widely marketed after the establishment of the Mywakaf initiative spearheaded by Bank Negara Malaysia through the Association of Islamic Banking and Financial Institutions Malaysia (AIBIM) in 2017. The emergence of the novel severe acute respiratory syndrome coronavirus 2 (SARS-CoV-2) epidemic, also known as COVID-19, in December 2019 caused massive impacts on society's socioeconomics. The prolonged lockdown has devastated economic activities while unemployment and retrenchment continue to increase. The closure of all business premises greatly impacted the individuals and the companies' cash flow, especially those involved in micro and small & medium enterprises (SMEs). This situation affected their ability to fulfil the financial institutions' monthly obligations. To alleviate their financial hardship, zakat, waqf, and sadaqah provide their beneficiaries access to "quick cash" through Islamic social finance on top of the government stimulus package. *Zakat* distribution will focus on the eight beneficiaries mentioned in the Quran. Meanwhile, the beneficiaries for *waqf* and *sadaqah* can be categorised more broadly.

Since then, more projects with more significant social impact have been carried out by financial or non-financial institutions to ease the burden of those impacted. It is found that boosting those projects requires coordination between all stakeholders. Also, there is a pressing need to mobilise financial resources effectively to ensure maximum financial returns and social benefits are delivered to the entire community. This can create a sound economic equilibrium that requires a robust Islamic social finance ecosystem consisting of specific instruments in terms of funding and investment that align with Shariah principles. Hence, based on the above background, the integrated model of Islamic social finance is proposed to form a dynamic ecosystem in achieving the maximum impact of Maqasid al-Shariah through Islamic Social Finance initiatives. According to Widiastuti et al. (2022), the development of integrated Islamic social finance is theoretical and has not yet reached the empirical stage. Therefore, the objectives of this paper are (1) to discuss the tools of Islamic social finance and (2) to propose an adoption of an Integrated Islamic Social Finance Model.

## 2. Review of Literature

### *2.1 Definition and Tools of Islamic Social Finance*

Islamic social finance has excellent potential in combatting the issue of financial distress and poverty, especially during the pandemic in Malaysia or elsewhere. The study from Rahman et al. (2022) recommends that Islamic social finance be further enhanced with the help of diverse fintech applications, such as blockchain technology, e-wallets, digital platforms, and so forth. To the best of the author's knowledge, not much literature defines the term 'Islamic Social Finance'. When describing Islamic Social Finance, most of them will always associate it with traditional philanthropic tools. A Rehman (2019) refers to Islamic social finance as finance modes rooted in Islamic ethics and intended for social benefit. These include zakat (almsgiving), waqf (endowments), Sadaqa (charity), and Qard Hasan (interest-free loans), which are more suitable to be categorised as Islamic Social Finance tools. This statement is further supported by Kuanova et al. (n.d), who defined zakat (almsgiving), sadaqah (voluntary), waqf (endowment) and Islamic microfinance as social tools that can be used to empower socio-economic well-being. Rosman et al. (2022) and Mohd Zain et al. (2017) mentioned that among the Islamic social instruments that are widely adopted are *zakat, sadaqah* (donation), waqf, *qard hassan* (benevolent loan) and Islamic microfinance. IRTI (2014) added on top of philanthropic-based (*zakat, sadaqah, waqf*) and cooperative-based (qard and *kafalah*), the contemporary Islamic microfinance institutions may be integrated to develop a more effective social finance ecosystem.

Therefore, in a nutshell, Islamic Social Finance can be categorised as a not-for-profit sector that engages with philanthropic instruments (IRTI, 2020). Nevertheless, Syed Azman et al. (2019) opined that the definition of Islamic social finance should be extended beyond just zakat, waqf and Islamic microfinance. A Rehman (2019) wrote with the development of green sukuk, SRI sukuk, vaccine sukuk and socially impactful Islamic crowdfunding, there is always room to widen the definition of Islamic Social Finance by integrating the element of Islamic Capital Market and takaful. Islamic Social Finance definition is not limited to only traditional philanthropic tools but extended to other socially impactful Islamic instruments to address humanitarian needs and thus should be considered as part of the ISF agenda.

### *2.2 Integrated Islamic Social Finance*

The process of integrated Islamic social finance components cannot be separated from the supporting ecosystem that may consist of, among others, (1) qualified human resources, (2) sustainable Islamic social finance research and development, (3) regulations supporting Islamic social finance development, (4) branding or introduction of Islamic social finance institutions to the community, and (5) adopting technology infrastructure to support the operational convenience of benefactors and recipients (Widiastuti et al., 2022). Since the underlying principle of Islamic social finance is value-oriented, it is easily blended with the Shariah principles that preserve the Maqasid Shariah in protecting human rights and preventing poverty. Its various philanthropic instruments may provide a great opportunity to deliver social and environmental impacts. Microfinance is now widely recognised as a significant tool for poverty reduction and women's empowerment and as a prospective financing method for banks, financial institutions, and non-governmental organisations (NGOs). Countries with a robust microfinance system have significantly reduced poverty and improved women's socio-economic conditions. Widiastuti et al. (2022) illustrated one of the examples of an integrated model of Islamic Social Finance conducted by Rumah Gemilang Indonesia (RGI), whereby the integrated models combine the roles of zakah and waqaf in developing the educational sectors. She mentioned that Zakat funds are generated to improve skills and knowledge in this case, while waqf funds are used to provide educational infrastructure.

Previous studies have developed a few integrated Islamic Social Finance models by combining more than one philanthropic instrument in providing microfinancing to people in need to combat poverty. As an example, a study conducted by Raimi et al. (2014) has proposed an integrated model of corporate social responsibility (CSR), Waqf system (WS) and Zakat system (TZS) as faith-based- model (FBM) for poverty reduction, enterprise development and economic empowerment. On the other hand, Hassanain (2015) and Hasan (2010) developed the integrated instruments of Islamic Social Finance between zakat, waqf and Islamic Microfinance for poverty alleviation. Hassanain (2015) proposed the new innovative waqf instruments referred to as monetary or cash waqf as capital to provide Islamic microfinance to the needy who are expected to repay their future earnings. On top of that, he also proposed the integration of zakat and waqf into one framework. He opined the integration between these two will be able to overcome the issue of fund insufficiency for the poor and later create a stable income stream through various microfinance schemes and services. This was supported by Hasan (2010), who also believed that this integrated model is reliable in reducing the risk of loan default. To make the model more reliable, he added the proposed financial management framework, which includes three main elements, namely i) fund management principles, ii) sources of funds and iii) usage of funds.

Haneef et al. (2015) developed an integrated waqf-based Islamic microfinance model (IWIMM) that involves components such as i) waqf/endowment which can be collected from various sources like waqf donors, government, charitable bodies and others, ii) Islamic microfinance, iii) project financing, iv) takaful and v)human resource development where the fund is utilised to develop more productive human resource by providing business training to the poor entrepreneur. He opined that in this integrated model of Islamic Social Finance, an educational and training program is vital to the borrowers in ensuring successful business operations, thus increasing their capability to repay the loan. An adequate loan amount is also essential to ensure the sufficient borrowed amount is utilised productively and efficiently. All those studies on the integrated models have shared objectives of poverty alleviation that touch on the conceptual basis only without mentioning the impact measurement. Therefore, Widiastuti et al. (2022) took the initiative to expand earlier research by constructing a sustainable integrated model of Islamic social finance through 4ER (Economic Rescue, Economic Recovery, Economic Reinforcement, and Economic Resilience) impact measurement model by integrating the Islamic social finance fund in a cooperative project scheme. The 4ER refers to the distribution mechanism that supplies a fundamental need to strengthen the welfare contribution of the community. Sulistyowati (2018), on the other hand, developed an integrated model for disaster recovery management. Even though the purpose differs from the other integrated model, the integration tools engaged are the same: waqf and zakat. Zakat is considered an empowerment tool, whereas waqf carries an investment element. Widiastuti et al. (2022) categorised zakat between consumptive and productive zakat, whereby consumptive zakat will be distributed directly while productive zakat will be given through some business training. In conclusion, previous studies developed the integrated models only by incorporating the tools of Islamic Social Finance, whether the integration took place between two traditional philanthropic tools or a combination of the traditional and modern tools of Islamic Social Finance. In some integrated models, they inserted the synergy element between institutions that took place between zakat/waqf institutions and Islamic microfinance institutions.

## 3. Analysis / Discussion

This section summarises the findings and discussion outlined in the literature reviews and the secondary data derived from the library research. The findings have been categorised into two (2) significant themes as follows:

### *3.1 Theme 1: Definitions and Overview of Islamic Social Finance Instruments*

Most of the literature reviews mentioned the instruments highly engaged in structuring Islamic social finance, which is philanthropic-based and not-for-profit, except to cover certain costs through microfinancing schemes. The use of these instruments triggered an activation of real economic activities, especially concerning waqf and zakat, compared to conventional debt-based financing. This was supported by Rosman et al. (2022), who found that most respondents did not provide a definitive meaning of Islamic social finance when asked about the definition of Islamic social finance. Instead, they were elaborating on the instruments. Some researchers were only comparing Islamic Social Finance with other philanthropic agendas such as sustainable development goals (SDGs), corporate social responsibility (CSR), and value-based Intervention (VBIs). Mohd Zain et al. (2017) described Islamic social finance as an ecosystem that combined traditional philanthropic tools with modern financial services such as Islamic microfinance, Sukuk, and takaful integrated with the element of cooperation that aims to solve societal challenges. It seeks to achieve the common good and ensure fair distribution of wealth among the society.

Furthermore, it bans the exploitation elements in economic activities such as financial speculation, gambling, imposition of interest, *gharar*, and others. As an alternative, it promotes fair financial dealings based on the principles of Shariah. The writer opined that the word "finance" is used to signify the probability of an element of profit imposed while providing the facility. Still, only to the extent of covering the operational cost of Islamic Banking, the word "social" is to differentiate it between the commercial Islamic Finance features, which the earlier is meant to provide global social and economic well-being through the involvement of various stakeholders by engaging different Shariah instruments. So, this is where Integrated Islamic Social Finance comes into the picture. Figure 1 below displays the instruments of Islamic Social Finance that could be enhanced further in future research.

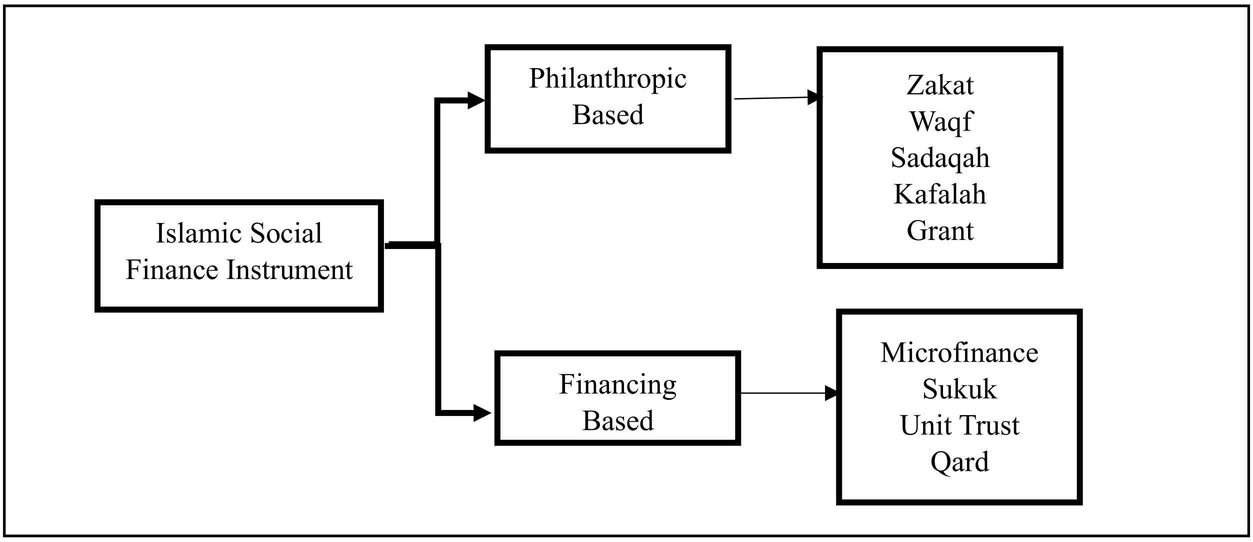



**Figure 1: Instruments of Islamic social finance**

Each of the above instruments carries different features and characteristics and focuses on different target segmentations. Zakat, for example, has a broader scope than sadaqah as it is not only given in the form of wealth but also the form of non-wealth (Tahiri Jouti, A. 2019).

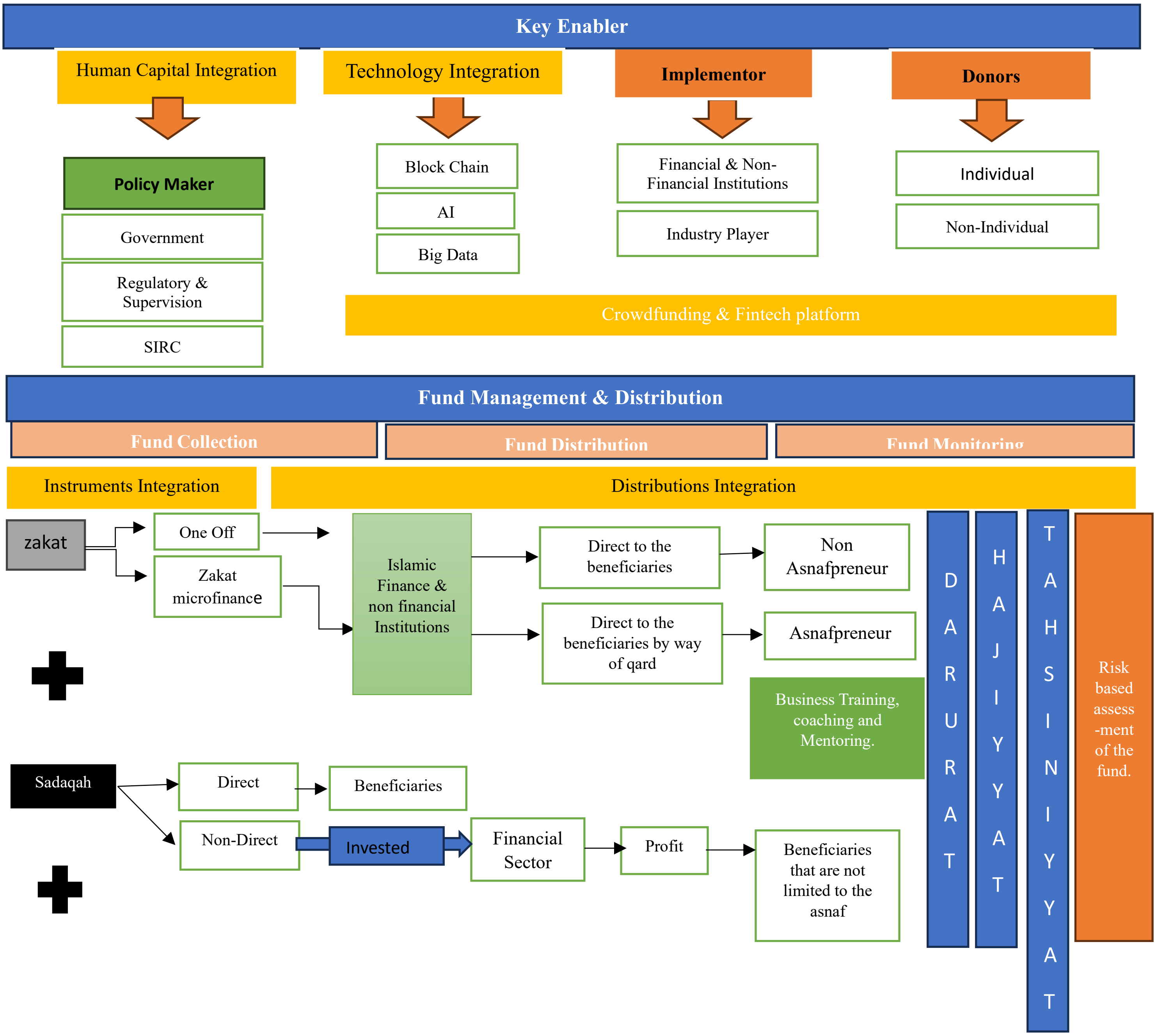
### *4.2 Theme 2: Proposed Model of Integrated Islamic Social Finance*

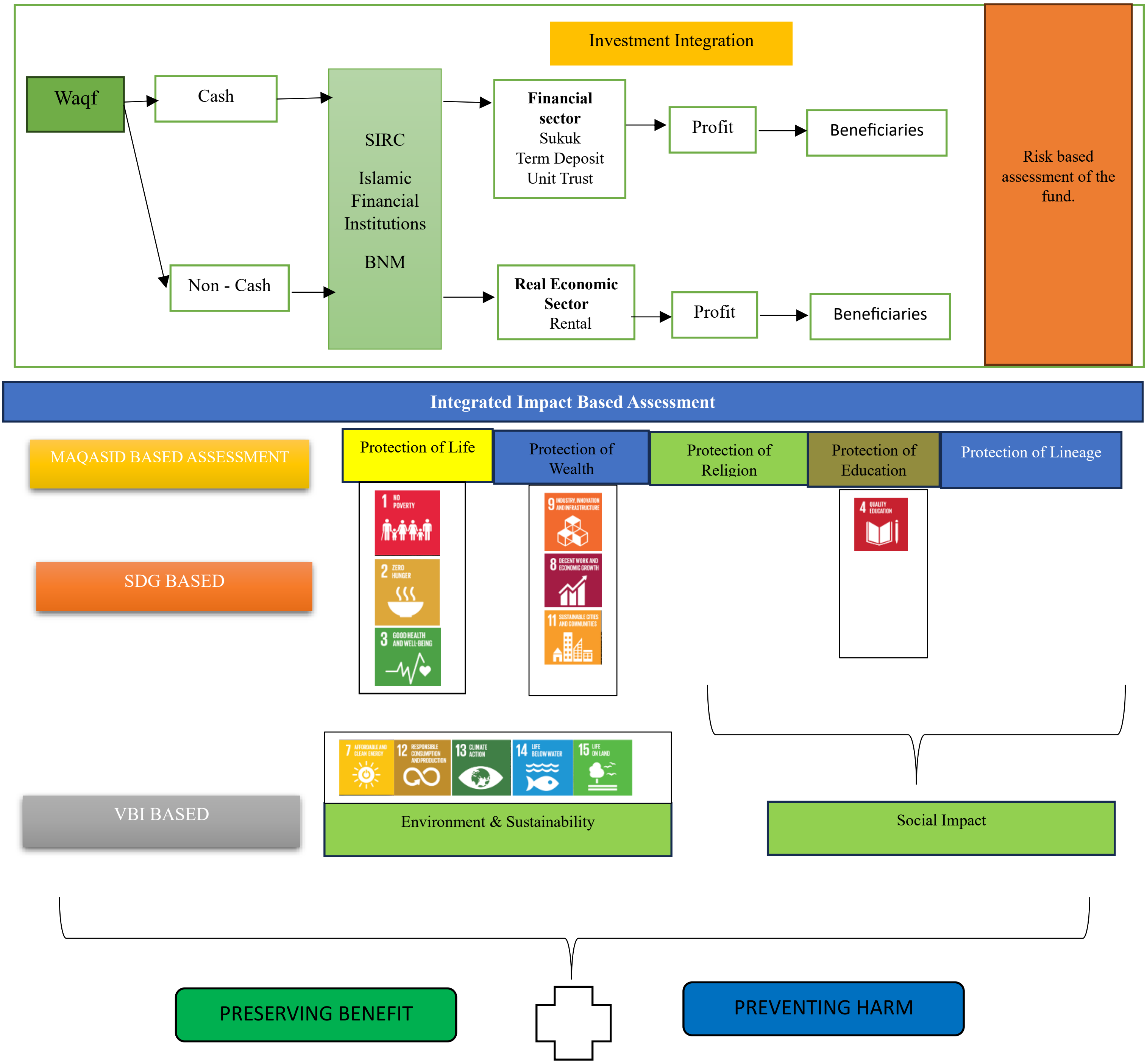
This study develops an integrated model of Islamic social finance, as in **Figure 2,** that suits Malaysia's regulatory requirements. This model adopts the proposed integrated model of social finance developed in Indonesia with some modifications to the structure following the regulatory requirements, funders' appetites, and many more. The integrated model proposed consists of 4 main elements, which are i) Enabler, ii) Source of fund, iii) Distribution of fund and iv) Impact assessment. All those elements will have an integration features as follows:

1) **Technologies Integration**: It involves synergy collaboration between multiple fintech providers in terms of data collection and analysis to simplify the collection and distribution process. Disruptive technologies avoid overlapping distribution and concentration of segmentations (Widiastuti et al., 2022). Technology helps in terms of data profiling of donors and lists of beneficiaries.
2) **Human Capital Integration**: It illustrates the synergy between all the relevant stakeholders, such as academicians and researchers, policymakers, financial and non-financial institutions, the States Islamic Religious Council (SIRC) and others.
3) **Instruments Integration**: Innovative philanthropic instruments that leverage modern Islamic Finance tools and integrate between the elements of funding and investment to maintain the fund's sustainability, thus creating a higher impact on the community.
4) **Management & Distribution Integration:** Integrates between direct and non-direct distribution**.** Some philanthropic tools such as waqf and sadaqah will be invested to generate more economic activities before distributing their profit to the beneficiaries.

5) **Impact-based Integration**: The integration element indulges between impact assessment based on the linkages between Maqasid Shariah, VBI based as well as SDG

**Figure 2: Integrated Model of Islamic social finance**






*4.3 Discussion on Integrated Model of Islamic Social Finance in Malaysia Human Resources Integration*

**Human Capital Integration**

The Integrated model must evolve into one complete ecosystem that comprises human resource support as the main players that consist of the policymakers such as the State Islamic Religious Council (SIRC) as a sole trustee of waqf, Bank Negara Malaysia as regulators for banking institutions, Securities Commission Malaysia as a regulator for Capital Market, government representatives as policy maker, researchers, financial and non-financial institutions as market players and others. For example, banking institutions are currently not allowed to be the mutawalli for waqf assets. This is among the challenges that we may need to look into to facilitate the investment activities of the cash waqf asset.

**Technology Integration**

The second support system in the ecosystem is the technology providers to facilitate the infrastructure. The implementation of technology helps in terms of data collection, data analysis as well as data segmentation and monitoring so that the following can be ensured: (1) identification of new donors and classification of the existing donors (2) identification of new potential beneficiaries and classification of the existing beneficiaries (3) Monitoring the zakat recipient that has elevated themselves to zakat giver and (4) the most significant is, to ensure proper management and disclosure of the fund for instant no overlapping of distribution to the same recipients.

**Instruments Integration**

As Widiastuti et al. (2022) mentioned, waqf will act as an investment instrument, while zakat is utilised to empower skills and business capital through productive distribution offered via a microfinancing scheme. Using zakat as a funding source will reduce the cost of funds for Islamic banking institutions and increase the productivity of real economic activities through microfinance businesses. As the model proposed, the zakat fund will be utilised in two ways, namely (1) non-productive and (2) productive. The former is by giving a one-off absolute amount to the specific eight beneficiaries mentioned in Surah Al-Taubah verse 60, while the latter is by utilising the zakat fund as a source for microfinancing. According to Muhd Adnan et al. (2021) research, zakat funds seem to have the potential to become one of the instruments to micro-credit the poor. Microfinancing using the zakat fund can prevent people from being involved in riba-based loans. According to Al-Qardawi (2020) a special committee need to be established to monitor the zakah fund that will be used for microfinancing purpose. He added that the financing can be structured based on Qard al-Hassan as an interest-free loan.

On the other hand, waqf and sadaqah can be an investment tool to generate more income before distribution to people experiencing poverty. The distribution can be made directly and indirectly, where only the profit portion will be distributed to the poor. The distribution can be made to individual or specific economic segments such as education, health, economic empowerment, agriculture, etc. Takaful and kafalah can be designed as part of the guarantee or assurance engaged in protecting in case of default or else. Waqf instruments can be extended to the Islamic Capital market as Sukuk Waqf and Waqf unit trust.

**Management and Distribution Integration**

The management and distribution could be challenging without proper profiling and monitoring. Zakat is obliged to be distributed to asnaf, but for integrated distribution, the one-off zakat will be given to individual asnaf who are non-entrepreneurial. As for the zakat microfinance, the fund will be distributed to the asnaf entrepreneur. This target segment will undergo proper monitoring, business skills training and many more to ensure their business performs well. They need to repay the zakat money lent to them under the microfinance scheme. As for waqf and sadaqah segments, the beneficiaries could be from M40-B40 households or targeted projects meant for the well-being of the society and the fair distribution of wealth for the ummah. The distribution amount and target segmentation will also be based on three categories, which are i) Daruriyyat, ii) Tahsiniyyat and iii) Hajiyyat.

**Impact Based Integration**

The impact-based assessment was integrated between the three elements overarching by the ultimate objective of Shariah. The writer has aligned each maqasid element with the objective required under SDG and VBI. For instance, the maqasid of life protection is aligned with the first three SDGs and meets the VBI element of environmental protection that includes animal life. The maqasid of wealth protection is aligned with SDGs 8, 9 and 11. On the other hand, the protection of education is in line with the SDG no 4. As mentioned by Value-Based Intermediation Full Report (AIBIM) 2021, nothing on the SDG concerned the protection of religion. This is evidence *of* their ideology that separated the world and Akhirah's affairs. That also exemplifies the (Shumuliyyah) element inherent in Islam that preserves every single aspect of both lives.

## 4. Conclusion

The proposed integrated Islamic social finance model is enhanced from previous studies of enriching more impacts towards social development and community empowerment. It is also aimed to accelerate the poor enrichment initiatives more effectively and efficiently through synergy collaborations between all parties. This study has several implications for the relevant stakeholders; for instance, the Islamic banking institutions must be ready for collaborations with other non-profit organisations. The regulators and government may have to revisit their existing guidelines or establish new regulatory policies to pave the way towards an integrated model of Islamic Social Finance. Lastly, all involved institutions must spark mutual synergy and initiatives to promote global social well-being that align with Maqasid Shariah through integrated Islamic Social Finance.

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