

## Barriers of Islamic Transactions Among Halal SME Owners in Malaysia

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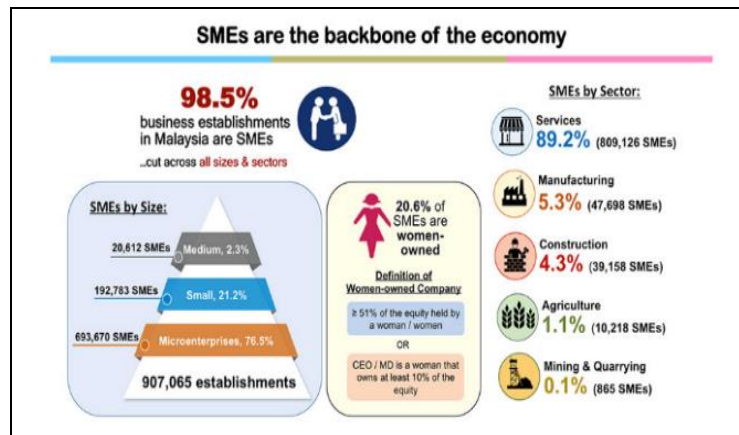
**Abstract:** The Halal supply chain landscape in Malaysia is ever growing, with Halal small and medium-sized enterprises (Halal SMEs) as its backbone. However, just like other businesses, Halal SME owners also face barriers in internal and external factors management. This paper aims to study the barriers in conducting Islamic transactions among Halal SME owners in Malaysia. It aims to investigate the current use Islamic transaction among SMEs globally and issues related to Islamic transaction that arises in Malaysia, specifically amongst Halal SME owners. This paper uses qualitative methods in round-table interviewing Halal knowledge Experts, SME Owners, SME Experts, and Technologists. From the expert discussions, it is found that the main barriers in conducting Islamic transactions among Halal SME owners in Malaysia are divided into 8 internal and external factors to manage. From these results, suggestions were given by the expert on how to overcome it.

**Keywords:** Malaysian SMEs, Halal Transactions, Halal supply chain

### 1. Introduction

Barriers are obstacles or circumstances that keep people and their field or area of expertise from progressing. Islamic transactions are transactions that prohibit interest, ambiguity, gambling, and the involvement of prohibited activities such as monopoly, manipulation of scales, false advertisement, selling fake products, treason, embezzlement, and bribery (Firdaus & Fauziah, 2019; Mohammed Masih et al., 2012; Osman et al., 2019). Halal SME owners are SME owners that are in the Halal industry and are compliant to its rules of Islamic or sharia law (Halal Industry Development Corp, 2019).

According to the latest statistics from the third Quarter of 2019 Malaysian economy, 98.5% of Malaysia's Gross Domestic Product (GDP) comes from SMEs while large enterprises contribute to only 1.5%, with 24.5% of that GDP is from the Selangor state alone (Department of Statistics Malaysia, 2019). The records also show that these numbers have increased since 2018 with a growth of 38.3%, which is RM521.7mil, an increase from the previous year where the total GDP is RM491.2mil (SMEBIZ, 2019). This exponential growth is due to the allocated budgets each year given by the government upon learning that SMEs are the backbone of the country with the highest import and export percentages. Subsequently, SMEs are expected to continue to contribute to the overall national GDP by the end of year 2020 as much as 41% and 50% by 2030 (Ministry of Entrepreneur Development, 2019).



**Figure 1.** SMEs by Size and Category (SME Corp. Malaysia, 2019a)

In the Malaysian Halal ecosystem, 98% are SMEs (SME Corp. Malaysia, 2019b). Certifications and standards are all done by Department of Islamic Development Malaysia (JAKIM), with constant efforts to incorporate information and communications technology (ICT) into the ecosystem. There is also the Halal Directory under JAKIM which ensures SMEs and other Malaysian Muslim consumers have access to all companies that have their products and services certified Halal. The Halal ecosystem in Malaysia is very comprehensive and is considered the global Halal leader by all Muslim countries around the world. This is due to the quality and certification of Halal in Malaysia being in compliance with Good Manufacturing Practices (GMP) (SMEBIZ, 2019) and is also recognized as the leader of Global Islamic Economic Indicator by Dubai’s Islamic Economy Development Centre in October 2018 report (Jayamanogaran, 2019).

In its efforts to be at the forefront in Halal branding, Malaysia has been striving towards being the Global Halal Hub by taking the initiative to implement the Halal Park since 2016 (Halal Industry Development Corp, 2019). The park is to accommodate all halal productions, sources, development, logistics, and traceability into one comprehensive system. This is compliant to the Halal Compliance Critical Control Point (HCCCP) that is needed to be adhered in order to assure the integrity of each product and services across the whole supply chain locally and globally.

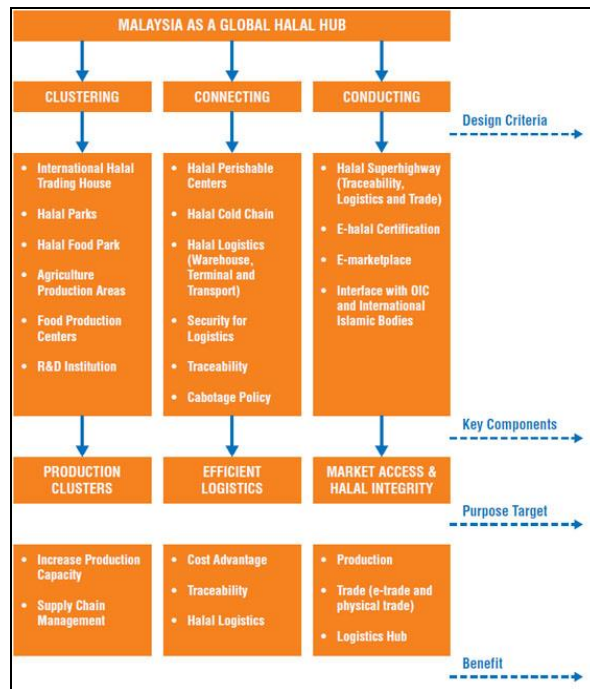


Figure 2. Malaysia as Global Halal Hub (Halal Industry Development Corp, 2019)

## 2. Current Use of Islamic Finances Among SMEs Around The World

The main principles of Islamic transactions are profits without interest, sharing risks, monetary source as only potential capital, prohibition of speculative behaviour, contracts that are sanctioned, and Islamic activities. These are all done using tools such as trades with cost-up sales, leasing, profit-sharing agreement, equity participation, and sales contracts which includes deferred-payment sale and deferred delivery sale (Iqbal, 1997). According to Islamic laws, these transactions are protected using either investigations or restrictions that are Islamic (Hasan, 2007; Osman et al., 2019). However, even when Islamic countries have banking initiatives to support SMEs, there is still no Islamic banking strategy, business transaction strategy, credit bureau, risk sharing instruments, and many other important tools that can better aid SMEs in performing Islamic transactions services across the supply chain (Aysan et al., 2016; Maswadeh, 2015).

## 3. Islamic Transaction Challenges in Malaysia

Just like other businesses, Halal SME owners also face challenges in transactional management such as Islamic financial literacy, attaining affordable business model, and consistently paying a two-yearly-paid Halal certification. The global Halal Market value until January 2020 is at RM7tril (Jayamanogaran, 2019). In the challenge of Islamic financial literacy, a financially literate owner will manage their finances well to maintain their sales transaction. Therefore, to become financially literate, SME owners need to have complete knowledge of their company's whole supply chain, especially in terms of financial management and financial strategies in order to take advantage of this market value. They must understand the basics of Islamic finances and its advantages, especially in terms of transparency in conducting each transaction, which will allow the owners to maintain halal integrity even during procurement. If a business is inherited, then business succession plans and exit strategies must be made so that past and current knowledge and information of the company can be passed down to the business owner's successor. This is especially true for

SMEs, as 76.5% are microenterprises which are more susceptible to business successions (Yusof, 2017).

Besides that, affordable Halal Business Analytics model, framework, or plan for SMEs are scanty, especially one that can provide forecast and analysis across the whole supply chain and is Islamic. Business Analytics models are models that can analyze data from multiple sources from large datasets and detect real-time changing trends, predict future patterns, and relay crucial information for decision management (Aysan et al., 2016). Therefore, to apply a Halal Business Analytics model into the Halal industry would be beneficial in aiding SME owners manage their transactions with real-time facts to aid in their decision making management. However, current applications that provide halal procurement with a Halal Business Analytics model is PayHalal, which not many SME owners know of. Other banks also do not have Halal Business Analytics models, just financial strategies to aid SMEs such as RHB Islamic purchasing card in March 2019 (Digital News Asia, 2019), CIMB Bank halal-ready financial aid (The Edge Markets, 2019), and Alliance Islamic Bank Halal One Program (NST Business, 2020).

Other than that, Halal SME owners face challenges in consistently paying a two-yearly-paid Halal certification. This is an issue as Halal certification is a means for these owners to engage in business transactions safely and securely with consumers without the consumers backing down due to fear of them being non-Islamic or non-Halal compliant. However, by the end of 2019, 90% of SMEs still do not have proper Halal certification (Azizi, 2019). The certification fees only need to be renewed every two years. However, Halal SME owners prefer to run their business using traditional means and do not see the benefits of obtaining halal certification, especially when it involves more licensing fees (Sallem et al., 2017). The current Malaysian trend shows more non-Muslims business owners accepting and entering the Halal market at increasing rate (Malek, 2020). Malaysian consumers on the other hand have equipped themselves with Halal verification apps in order to scour the market for products and services (Ismail, 2017). If SME owners do not apply for Halal certification, consumers will assume that their product is not Islamic and refuse to buy it. This will reduce their business transactions and cripple the performance of these non-Halal certified SMEs.

#### **4. Methodology**

This paper uses qualitative approach, where a round-table interview session was done with 1 Halal knowledge Experts (HE), 3 SME Owners where 1 owner represents manufacturing (SM) and 2 owners represents services (SS1, SS2), 1 SME Experts (SE), and 3 Technologists (T1, T2, T3). SME Owners and Expert validates the Supply Chain elements, Halal Knowledge and Islamic Finance Expert validates the Halal elements in each transaction, and Technologists validates the technological part and whether an analytical business model is practical to be used in the Halal industry. The research has also been limited to SMEs in Halal Supply Chain only. The data will be collected through open-ended feedback forms with each topic grouped into main points, discussed, and then reviewed again with all the experts in order to conclude the final points together. The final points are then tabulated and analysed, before writing down the solutions suggested.

The data collection session begins with a discussion and handing out open-ended feedback forms for each expert to fill in within their own field of expertise. From the discussions, it is found that the main barriers in conducting Islamic transactions among Halal SME owners in Malaysia are divided into 8 internal and external factors to manage, which are capital and financing barriers, productivity and technological barriers, labour force barriers, company management barriers, raw materials barriers, competitiveness barriers,

relationship barriers, and location barriers. From these barriers, several comments and suggestions were given by each expert on how to overcome it.

## 5. Discussion

The barriers of Malaysian Halal SME owners in conducting Islamic transactions are divided into internal and external factors to manage. Internal factors are capital and financing barriers, productivity and technological barriers, labour force barriers, and company management barriers. External factors include raw materials barriers, competitiveness barriers, relationship barriers, and location barriers. The following are the tabulation and its overall description of the solutions based on the data collection session, which shows that most barriers to manage are internal than external factors.

**Table 1.** Analysis of Barriers by Experts Involvement

| Barriers         |   | Experts Involved in Suggestion |    |     |     |    |    |    | Total (%) |      |
|------------------|---|--------------------------------|----|-----|-----|----|----|----|-----------|------|
|                  |   | HE                             | SM | SS1 | SS2 | SE | T1 | T2 |           | T3   |
| Internal Factors | Capital and financing barriers          | /                              | /  | /   | /   | /  |    | /  |           | 75.0 |
|                  | Productivity and technological barriers | /                              | /  | /   |     |    | /  | /  | /         | 75.0 |
|                  | Labour force barriers                   |                                | /  | /   | /   | /  |    | /  | /         | 75.0 |
|                  | Company management barriers             | /                              | /  | /   | /   | /  |    | /  | /         | 87.5 |
| External Factors | Raw material barriers                   | /                              | /  |     |     | /  |    |    |           | 37.5 |
|                  | Competitiveness barriers                | /                              | /  |     |     | /  | /  |    | /         | 62.5 |
|                  | Relationship barriers                   |                                | /  |     | /   |    | /  | /  |           | 50.0 |
|                  | Location barriers                       |                                |    | /   | /   | /  |    |    | /         | 50.0 |

**Table 2.** Barriers by Ranking

| Barriers                                | Category | Total (%) |
|---|----------|-----------|
| Company management barriers             | Internal | 87.5      |
| Capital and financing barriers          | Internal | 75.0      |
| Productivity and technological barriers | Internal | 75.0      |
| Labour force barriers                   | Internal | 75.0      |
| Competitiveness barriers                | External | 62.5      |
| Relationship barriers                   | External | 50.0      |
| Location barriers                       | External | 50.0      |
| Raw material barriers                   | External | 37.5      |

### 5.1 Capital and financing barriers

In order to solve this barrier, T2 suggests that there should be more opportunities, crowdsourcing, re-investment plans, and other Strategic Financial Plans with the main financial body in Malaysia, which is Bank Negara Malaysia (BNM). T2 explain that the barrier that occur is due to not having a standardized basic financial plan that specifically

caters across the whole Halal supply chain by BNM. When the main financial body sets a standard, all financial institutes will follow suit with the new regulation. HE, SM and SE states that the standard should include cooperation between BNM and the main Islamic affairs institute in Malaysia, JAKIM, and Standard and Industrial Research Institute of Malaysia (SIRIM). HE, SS1, SS2 agrees with the justification that public awareness on these plans must be commercialized especially regarding Islamic transactions, Islamic loans, and the importance of data policies and knowledge.

## **5.2 Productivity and technological barriers**

According to SM, low productivity is caused by lack of skills. Due to not having a stable financial status, SM explains that Halal SME owners do not have the knowledge to attain affordable management and financial courses. Therefore, SM suggests that this barrier can be tackled by providing digitalized platforms to upgrade skills and training that are affordable for the average public and SME owners. T1, T2, and SS1 agrees with the justification that this way, there is integration of the knowledge in a digitalized environment, creating more accessibility and less complexity in attaining those knowledge and skills. T3 and HE also agreed, further noting that digitalized platform training will increase the productivity rate of Halal SME companies both internally and externally.

## **5.3 Labour force barriers**

SM and SE explains that low skilled labour forces are crucial to an industry. However due to financial barriers, SM and SE states that labourers lack quality training and are given lower salaries. A proposition by SE is for better quality training to be provided for these labourers and giving them higher impact incentive will encourage the labourers to increase their skills, knowledge, and service. This is further agreed by SS1 and SS2 with justification that this will lead to higher quality products and services amongst the labour force. A good framework for this is the TVET (Technical and Vocational Education Training) programme, which was suggested by SM, T2, and T3.

## **5.4 Company management barriers**

According to SS1, SS2, SM, and HE, the main barrier that arise from inherited SME businesses is that there are no models to understand past data from the customer for the next generation that inherited the business. Therefore, a business model may help in that area, where each data can easily provide predictions and annual visualizations for the current business owner. T2 and T3 that it is feasible and practical if the model can summarize internal and external business factors such as SWOT Analysis and financial plans. SE adds that the model should also cater many other knowledge expertise as well in the form of Knowledge Management from previous owners.

## **5.5 Raw material barriers**

Barriers that arise in this area, according to SM, is usually due to boycott by suppliers, the monopoly of raw materials, and the supplies being controlled by foreign bodies. SE suggests that these barriers can be addressed by improving logistics, storage unit, and distributor relationship amongst the Halal SME companies. However, HE commented that these barriers are only specifically towards SME companies, not applied generally towards the Halal industry.

## **5.6 Competitiveness barriers**

When SE and SM mentioned competitiveness barrier, HE quickly suggests that Halal Marketing can easily solve this it. HE along with agreement and justification from T1 and T3 says that the import and export of Halal products can be done through common sales international hubs and assistance platforms, such as the Halal Hub created by JAKIM.

## **5.7 Relationship barrier**

SS2 states that there is a barrier in the relationship between heavy industry and Halal SME owners. SS2 further explains that any solution suggested must place it focus on the main supplier in the Halal supply chain tier. SM, T1, and T2 describes further in their assessment, stating that the areas that need to be explored to solve this barrier includes Halal storage, Halal packaging, Halal logistics, and Halal supplier relationship. This way, the heavy industry chosen in the tier will also be halal compliant industry, in which most barriers regarding support and biased will be on par.

## **5.8 Location barrier**

SS1 and SS2 states that placement or location is another important barrier. However, T3 suggests that strategic location can be found by using e-Commerce Platforms. These platforms usually have cost database and provide market focused geo-analysis for the users. Noting this, SS1, SS2, and SE also suggest for SME owners to join Virtual Malls and e-Shops that can also provide seasonal trend analysis and business growth data.

## **5.9 Other Suggestions and Comments**

SS1, SS2, and SM suggest that these barriers need to be scoped into the direction of Halal Market and SME growth. This can be done by understanding SME Financial Charter, MS1900 by JAKIM, and SIRIM. However, HE and SE suggests that these discussed issues are only referring to SME Halal owners, not multinational Halal owners. Therefore, all the experts agree that the general Halal industry may produce different discussion results.

## **6. Conclusion**

The barriers faced by Malaysian Halal SME owners are due to their lack of internal and external factor management. Malaysian Halal SME companies have grown over the last 20 years. Therefore, there will be more challenges that they will face. In order to fully reach the National Entrepreneurship Policy 2030 target of 50% GDP for SMEs, more research should be done in managing each barriers practically across the whole Halal supply chain and amongst Halal SME owners. Perceptions of customers, suppliers, distributors, retailers, and wholesalers should be explored in detailed separately as to understand the extent of each barrier, and the procurement documents needed in order to conduct sharia compliance across each HCCCP. Future researches can also conduct SWOT Analysis on the internal and external factors management discussed so that the strengths, weaknesses, opportunities, and threats of Malaysian Halal SME owners can be identified and better managed.

Besides that, further studies can be done on Halal large enterprises, Halal multinational organizations, and halal heavy industries. Halal large enterprises and Halal multinational organizations have their own frameworks to maintain company and financial stability. Therefore, the study of those frameworks can be minimized and made to fit a smaller scale for the SMEs to reference in terms of business and financial strategies. The relationship heavy industries have with Halal SME companies should also be further investigated, as it is crucial for the survival of Halal SME companies in the local Halal Market.

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