

## THE IMPORTANCE OF SUKUK IN THE DEVELOPMENT OF ECONOMY: AS AN EXAMPLE OF ITS IMPACT ON THE INCOME OF THE MALAYSIAN POPULATION.

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### Abstract

As we know, in recent years, Islamic finance has been increasing rapidly. Despite a very small share in the global financial system, it attracts all specialists in the field with an average annual growth rate of 20%. It is noteworthy that Islamic finance can be used not only in Muslim countries but also in non-Muslim countries.

In this article has been investigated the impact of sukuk development on the economy which is the second largest sector of Islamic finance and used data from Malaysian indicators for 2006-2018 years. There are provided some ideas for the future researches at the end of the paper based on obtained positive results of the study.

**Key words:** Islamic finance, Islamic Bank, sukuk, GDP per capita.

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### INTRODUCTION

In the last years, Islamic finance shows a positive tendency. Islam financial assets reached to USD 2.4 trillion in 2017 [GIFR, 2018]. According to the calculations, by the end of 2024, it will be reached up to USD 3.4 trillion [IFDI, 2019]. Also, its including in G20 agenda [Smaoui & Nechi, 2017] increases its importance. Second largest sector of Islamic finance – sukuk is growing rapidly. By the end of 2018, emissions for the all period amounted to 1.1 trillion US dollars, including in 2018 - 123.15 billion US dollars. [IIFM, 2019].

The interest for Islamic finance increased after the global financial crisis in 2008. Scientific research has shown that Islamic finance is more stable and resistant to crisis than traditional finance [Chapra, 2008; Hasan & Dridi, 2010; Beck, Demirgüç-Kunt & Merrouche, 2013]

According to the Accounting and Auditing Organization for Islamic Financial Institutions, "Sukuk are certificates of equal value representing undivided shares in ownership of tangible assets, usufruct and services or (in the ownership of) the assets of particular projects or special investment activity, however, this is true after receipt of the value of the Sukuk, the closing of subscription and the employment of funds received for the purpose for which the Sukuk were issued" [AAOIFI, 2017].

This Islamic finance tool is used not only in Muslim countries but also in non-Muslim countries. Sukuk is used as one of the most convenient instrument for securing liquidity for institutional investors such as banks, investment funds and insurance companies.

This article deals with the issues how the growth of sukuk emissions influences the economy. We consider that it will have a positive impact on the economy due to the following factors:

- Firstly, from the point of view the Shari'ah, the Muslim savings, which cannot invest in traditional bonds, will be effectively utilized because of such factors as ribo and maysir.
- Secondly, it is a convenient instrument for risk reduction by diversifying the investment portfolio.
- Thirdly, the principle of risk sharing motivates the issuer to make more investment projects.
- Fourthly, the development of the securities market promotes competition between the financial sectors.

Even though there have been an increasing number of scientific research related to Sukuk, it still remains low compared to other areas. There are a small number of studies on the impact of Sukuk on the economy.

The study analyzed the effect of sukuk on the Malaysian economy in 2006–2018. The study gave the expected result. Finally, there recommended some questions that need to be explored to expand the sukuk market.

The remainder of the paper is organised as follows: Part two is an overview. Part tree discusses literature review. Part four describes data and variables. Part five explains our model. Section six analyzes results. The last section provides conclusions.

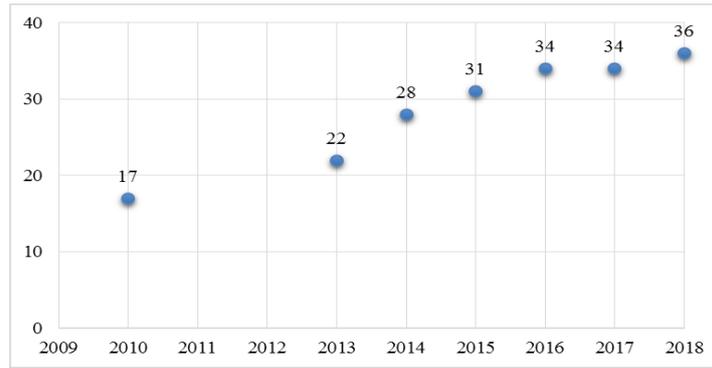


Figure 1. Growth trend of number of sukuk issuing countries  
Source: IIFM

### OVERVIEW OF SUKUK MARKETS

Historical documents indicate that the issue of sukuk was first covered by Imam Malik's work in Al-Muwatta [Echchabi, Abd.aziz & Idriss, 2016]. This mechanism was used in the VII century during the Umayyad Caliphate. Attempts were made in Jordan in 1978 and in Pakistan in 1980 for modern sukuk emissions. On the other hand, these works have failed because of inadequate infrastructure and transparency in the market [Ali & Falahi, 2014].

The first sukuk, which was recognized successful, was in Malaysia in 1990 with a total of MYR 125 million - USD 32.9 million [Paltrinieri et al., 2019]. After that, the sukuk was not issued until 2001.

In 2018, two countries issued their first sukuk and the number of sukuk issuing countries in the world reached 36 (figure 1). However, according to the annual report of IIFM 2019 Iran is not listed among the sukuk issuing countries. In fact, in 2018 and earlier reports this country was included.

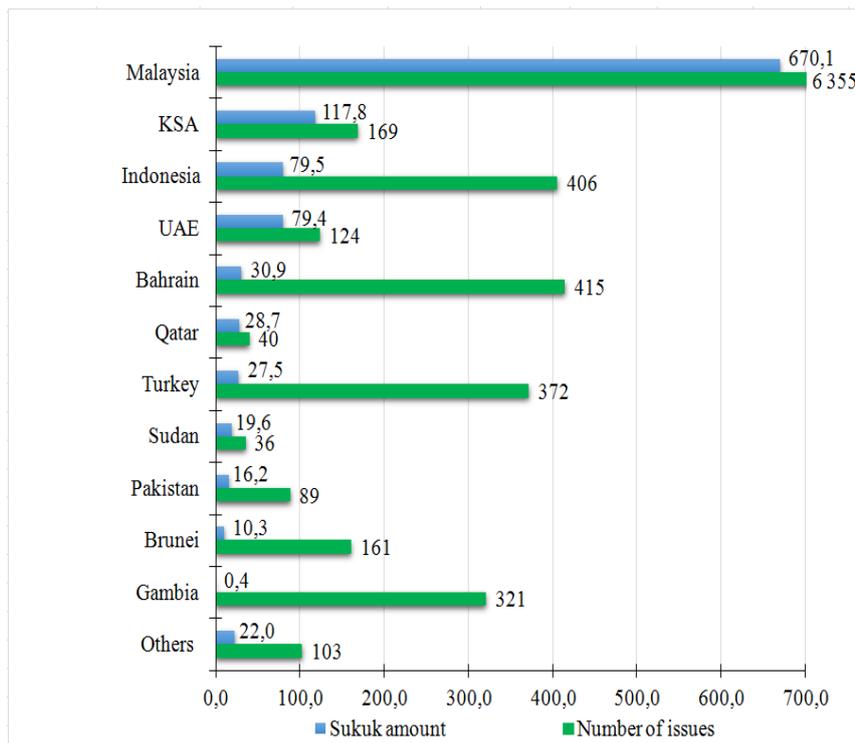


Figure 2. Sukuk issuance in some countries of the world (2001-2018, USD billions)  
Source: IIFM

Malaysia is a leader among sukuk issuing countries with a market share of 60.8% at the end of 2018 [IIFM, 2019]. Figure 2 shows the largest sukuk issuing countries in the world.

dominating over the years. The average share of the local sukuk in total issues during the 2001-2018 years shows 77.1%.

Figure 3 shows the trends in the international and local sukuk share till 2018, by years. The size of local sukuk has been

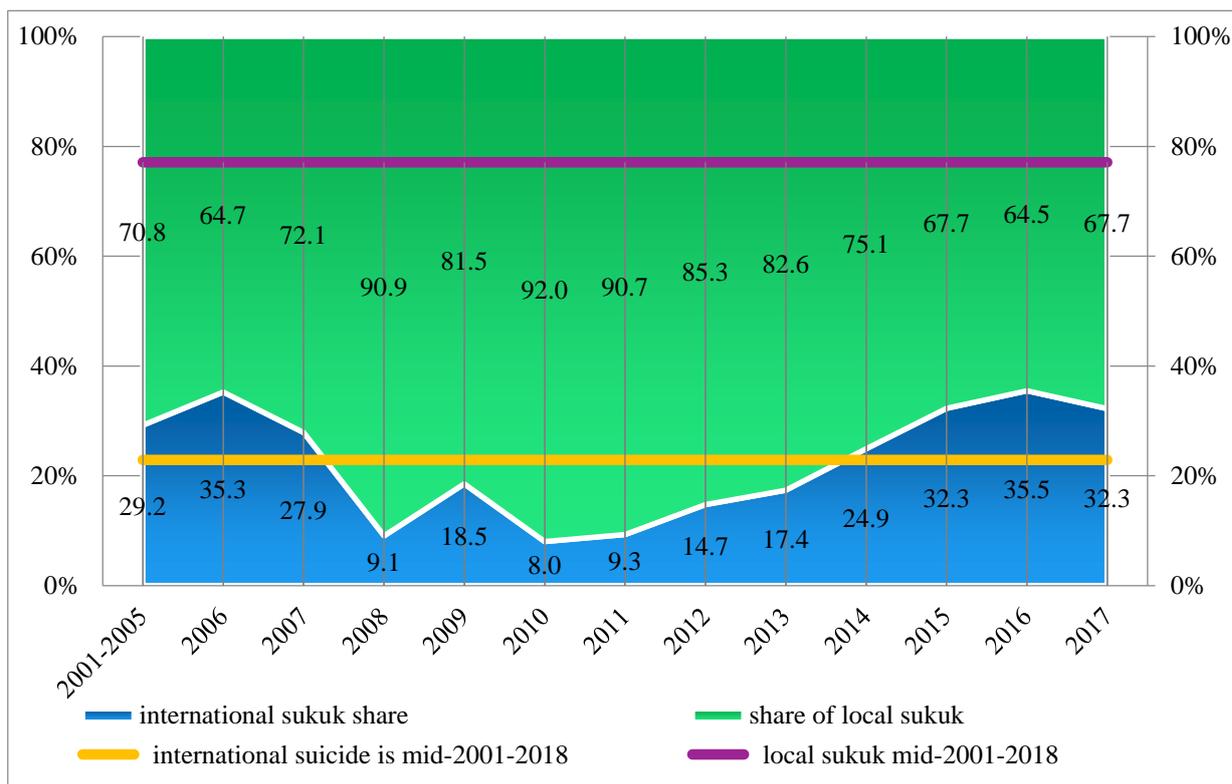


Figure 3. Dynamics of changes in the share of international and local sukuk in global issuance  
Source: IIFM

#### LITERATURE REVIEW

If Islamic finance is seen as a new system of our time, sukuk is the newest tool in this system. There is a growing number of scientific studies related to Islamic finance and Islamic banks. More on this can be found in the work of Zaher & Hassan, 2001 and Hassan et al, 2018.

Although the increasing number of scientific studies related to Sukuk, it still shows less number compared to other areas. Its main part remains dependent on theoretical aspects, organizational issues and the mechanism of its functioning. But, the researches based on the connection between sukuk and economic development is rare [Zulkhibri, 2015].

Ibrahim & Minai, 2009 made a research on the importance of sukuk in attracting investments to enterprises. The results show that for small enterprises with high investment potential it is advisable to issue sukuk. As well as, the government's support of the sukuk market has a positive impact.

Researches indicate that macroeconomic factors have an influence on the development of the sukuk market [Ahmad, Daud & Kefelia, 2012; Said & Grassa, 2013]. But, some macroeconomic indicators, such as inflation and the size of the banking sector are not significantly influenced by this type of Islamic financial instrument. Additional important aspect is that whereas the Muslim population has a positive impact on the development of the sukuk market, ethnic division has been found to be unimportant [Said & Grassa, 2013].

As there are some researches on the impact of sukuk on the economy, the first attempt was based on the effect of sukuk emissions on GDP, gross capital growth and trade processes

[Echchabi, Abd.aziz & Idriss, 2016]. Even though the results have not been as expected, there some actions that's significant with their attempting to a new direction. The next researches in this field had significant results [Smaoui & Nechi, 2017]. This work differs from the previous one by the different factors and methods. Sukuk supports the long term economic developing. Here, corporate and state sukuk has equal importance.

In this article, as continuing the current direction, the impact of sukuk emissions on population income was studied based on the study within 2006–2018 in Malaysia.

#### DATA AND VARIABLES

Sukuk outstanding (so) is the amount of the annual sukuk outstanding of Malaysia. One of the key indicators of the Sukuk market has been chosen as an independent variable for our model.

Gross national income per capita (gnipc) is an index of Malaysian gross national income per capita. This dependent variable serves to define the standard of living of the population.

All of the aforementioned variables are in constant 2010 national currency for the period 2006-2018. All the data was obtained from World Bank, IIFM, and SC Malaysia. Table 1 summarizes the data about indicators.

**Table 1. Definition of variables**

Variable	Label	Measure	Source
Sukuk outstanding	<i>so</i>	The amount of the annual sukuk outstanding of Malaysia	IIFM, SC Malaysia
Gross national income per capita	<i>gnipc</i>	Malaysian gross national income per capita	World Bank

**MODEL**

In order to determine the effect of Sukuk on the economy, we construct the following model by using our data from table:

$$y_t = \beta_1 + \beta_2 x_t + \varepsilon_t \quad (1)$$

$y$  represents gross national income per capita (*gnipc*) as the dependent variable,  $x$  is sukuk outstanding (*so*) as the dependent variable and  $t$  is the period within 13 years (1, 2, ...,

13). We test our linear regression model by the help of tests. We check our linear regression model with various tests.

**RESULTS**

It was known that correlation indicator between the amount of sukuk in circulation and the national income per capita is 0.97. It means that there is a strong relation between these two factors.

**Table 2. Regression results**

Source	SS	df	MS	Number of obs = 13		
Model	179597315	1	179597315	F( 1, 11) =	217.77	
Residual	9071632.35	11	824693.85	Prob > F =	0.0000	
				R-squared =	0.9519	
				Adj R-squared =	0.9475	
Total	188668947	12	15722412.3	Root MSE =	908.13	

gnipc	Coef.	Std. Err.	t	P> t	[95% Conf. Interval]	
<i>so</i>	17.90821	1.213525	14.76	0.000	15.23726	20.57916
<i>_cons</i>	23976.31	540.0549	44.40	0.000	22787.66	25164.96

Our simple linear regression analysis shows that sukuk have a positive impact on the economy. In other words, increase in the amount of sukuk outstanding by MYR 1 billion in Malaysia in 2006-2018, contributed to the increase the gross national income per capita by MYR 17.9. In this regression model, we identified them in all criteria and on the basis of it we found that they were statistically significant, the parameters of this model are reliable and the absence of autocorrelation and heteroskedastic errors as well as determined the normal distribution of residuals.

**CONCLUSION**

In this research the hypothesis of the positive effect of sukuk on the economy has been confirmed. According to this it is desirable to use sukuk emissions as a factor in increasing incomes in Muslim countries. Here, mid-term and long-term sukuk are more effective in macroeconomic context. We consider that it is a sufficient opportunity to stimulate the economies of countries that have not implemented the sukuk or have little use of this financial instrument.

As Sukuk's development has short historical period, there are much research that should be done. Furthermore, we recommend to study study in the future the sukuk effect on changes in the size and components of the stock market and the impact of international sukuk on international integration processes.

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