GLOBAL BUSINESS MANAGEMENT REVIEW
http://e-journal.uum.edu.my/index.php/gbmr

How to cite this article:
Muhmad, S. N., W. Ismail, W. N. S., A. Rahim, N. A. A., & Ahmad, S. N. (2020). Islamic financing for small medium enterprises: Challenges and opportunities. *Global Business Management Review, 12*(2), 50-64. https://doi.org/10.32890/gbmr2020.12.2.12527

ISLAMIC FINANCING FOR SMALL MEDIUM ENTERPRISES: CHALLENGES AND OPPORTUNITIES

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Received: 26/10/2020 Revised: 8/12/2020 Accepted: 30/12/2020 Published: 31/12/2020

ABSTRACT

This study attempts to discuss the challenges and opportunities of Islamic financing for Small Medium Enterprise (SMEs), as the Islamic finance industry's growth and SMEs are stimulated in this recent year. The government has introduced Islamic SME financing since 2012, and Malaysia has promoted it by granting a rebate for the participated parties, especially Islamic financial institutions. However, the government's opportunities are still in the slow mode to be grabbed by SMEs. With selected literature related to SMEs and Islamic financing, this study discussed SMEs and Islamic banks' practices in Malaysia. Based on the literature, several issues had to be highlighted, such as SMEs' readiness to have the opportunity with larger firms, SMEs' behaviours, and attitudes when dealing with external supports, as well as their awareness of business financing. Thus, this study highlights the challenges and real issues among SMEs and points out the opportunities for improvement that are expected to benefit SMEs and Islamic financial institutions in Malaysia.

Keywords: Small Medium Enterprises (SMEs), Islamic financial institutions, SME financing, Islamic finance.

INTRODUCTION

Small and medium-sized enterprises (SMEs) have been key drivers that contribute to the economic system and economic growth. In developing countries, SMEs hold the largest shares of employment (Ayyagari Demirgüç-Kunt & Maksimovic, 2011), with a contribution to the global labour market of 43.5 percent. With their capabilities in various business and operations and large networking within different sectors, SMEs can dominate sub-sector businesses such as computer services, marketing, and human resources (OECD, 2000). SMEs also contribute to gross domestic product (GDP) (Al Balushi, Locke & Boulanouar, 2019) with the contribution of 50 percent of global GDP (World Trade Report, 2016).

Small Medium Enterprises (SMEs) show excellent performance and growth in the Malaysia context by representing 97.3 percent of registered businesses and 57.5 percent of total employment in 2015 (Chin & Lim, 2018). The performance of SMEs has improved in the last 14 years since 2004 after the establishment of the National SME Development Council (NSDC). The SME Masterplan 2012-2020 (the Masterplan) aims to take SMEs to the next development level by increasing SMEs' participation in the national economy. Under the Masterplan, SMEs' contribution to growth is targeted in a way to reach 41 percent increase of the country's total GDP by 2020. To achieve this target, SMEs' GDP growth needs to be sustained at 9.3 percent per annum, against the current 'business as usual' average of 6.3 percent per annum (BNM, 2013).

Although SMEs are found to have improvement in financing their capital (OECD, 2018), SMEs still have face constraints in their operations as they lack external financing and face larger credit limit compared to large companies (Beck & de la Torre, 2007). In Malaysia, SMEs' access to financing is provided in various institutions of both Islamic and conventional. However, SMEs have high rejection rates as they might lack documentation, insufficient cash-flows and vague business plans (Kandasamy, Lee & Jer, 2018). A survey conducted by SMEs Corporation Malaysia reported that 44.8 percent of SMEs' respondents have difficulties in sustaining their business due to liquidity problems and demand for financing their capital from financial institutions that decreased to 36.3 percent in 2016. Moreover, SMEs' owners are doubting themselves to make loan repayment as financial institutions providing higher financing costs that do not meet their small business capital requirement (Wassiuzaman & Nordin, 2019; Kandasamy et al., 2018).

Malaysia is categorised as the most comprehensive halal ecosystem in the world. However, there is still inadequacy to meet the world demand for halal-certified products from local producers, and 98 percent of it is from SMEs that scarce in mentoring, money, and markets (SMECorp, 2019). However, most demand financing in developing countries is Islamic financing (Elasrag, 2016). The preference and demand for sharia-compliant products from a financial institution are very high. Besides, the application of a diverse spectrum of Sharia contracts by Islamic financial institutions continues to trend upward in recent years.

According to The Star (2017), SME corporation, as the agency of the Ministry of International Trade and Industry (MITI) has approved funding for Sharia-compliant SME Financing Scheme (SSFS), about RM1,595 billion in total since 2012. It shows that Islamic SME financing is become trending and received encouraging demand among SMEs in Malaysia. Additionally, the preference for the sharia-compliant product is very high based on the report by Ozkan (2015). However, according to Ying (2019), the facilities provided by the Islamic financial institutions and governments, especially about the availability of Islamic financing for business, have not been fully aware by SMEs due to the misconception of surrounding eligibility.

Additionally, most SMEs has adopted conventional financing. Some of them are still confused about Islamic finance that is said to be specific only for Muslims. Hasan (2015) also highlighted several challenges faced by SMEs, including adverse legal and regulatory framework, insufficient strategies for products and services branding, and insufficient bank policies that utilise movable collaterals. Various directions of the problem that arose show space for improvement in Islamic SME financing, specifically in Malaysia. According to Iqbal (2014), the nation needs to develop a national-level policy and strategy that enables Islamic finance's regulatory framework for SME financing. It is essential to strengthen the Islamic framework for SME financing and increase the visibility of Islamic SME financing. Thus, this study highlights the challenges and strategies and develops a framework of Islamic SME financing for Islamic financial institutions. The rest of this paper discusses the literature review related to SMEs and Islamic finance, the discussions on challenges and opportunities of Islamic financing to SMEs in global and Malaysia, the recommendations, and the conclusion.

LITERATURE REVIEW

An Overview of SMEs and Islamic Finance in Malaysia

The development of SMEs in Malaysia which started from 1957 to 1970 were mostly involved in agricultural and small services. Since then, the accelerated growth of SMEs cannot be denied (Chelliah, Sulaiman, & Yusoff, 2010; Hashim, 2007) when it contributes a massive impact to the Malaysian economy by offering job opportunities and, most notably to the development of multinational companies (Madanchian, Noordin, Hussein, & Taherdoost, 2016). The SME sector in Malaysia shows remarkable growth and has become the key driver of accelerating economic growth in the nation. According to the World Bank, SMEs account for 97 percent of businesses and 67 percent of employment, thus contributing up to 36 percent of Gross Domestic Product (GDP) in Malaysia. Department of Statistics Malaysia revealed that about 98.5 percent of businesses established in Malaysia are from SMEs across all sizes and sectors. Figure 1 and 2 illustrate the classification of SMEs by size and sector (Sources: Economic Census 2016, Department of Statistics Malaysia).

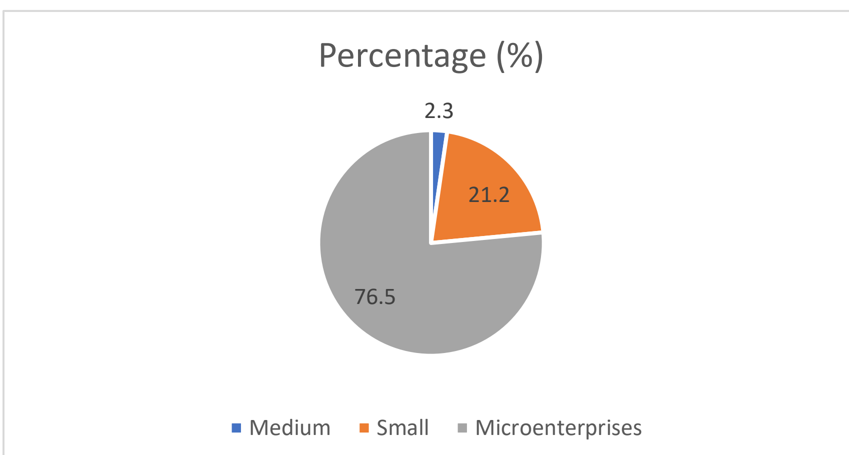

Figure 1: *Percentage of SMEs by Size*

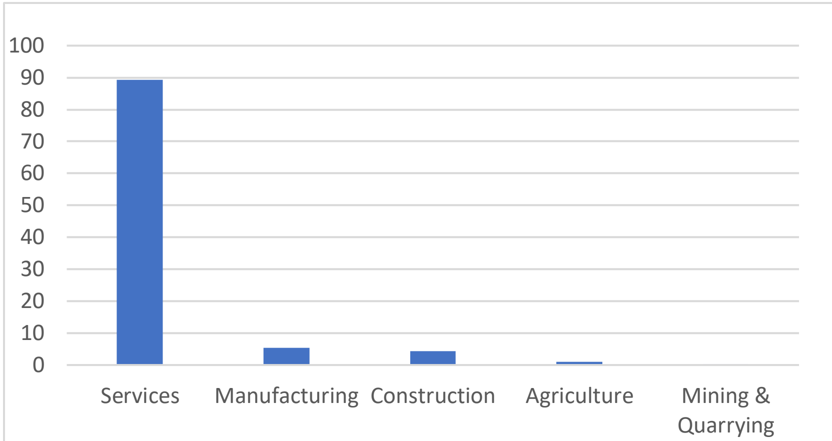

Figure 2: *Percentage of SMEs by Sector*

The total number of SMEs, which is 907,065, shows the remarkable growth of businesses in Malaysia. The high contribution of SMEs towards the Malaysian economy cannot be denied since SMEs' function is seen as having a vital role in the development of the country's economy. A vast number of SMEs have led to increased funding and seek of capital through institutions involved in providing finance (Ramlee & Berma, 2013). The funds are made available by government agencies, venture capital companies, financial institutions, and non-financial institution lenders. The competitiveness and continuous growth of SMEs need to have a well-developed financial infrastructure in order to meet SMEs' needs in offering the diverse financing model (BNM, 2013). The specification of qualified SMEs is highlighted in Table 1 through the total sales turnover or full-time employees.

Table 1

Definition of SME by sector and size of the operation

Sector	**Small**	**Medium**
Manufacturing	Sales turnover between RM 300,000 to less than RM 15 million or full-time employees between 5 and 75	Sales turnover from RM15 million to not exceeding RM50 million OR full-time employees from 75 to not exceeding 200
Services & Other Sectors	Sales turnover between RM 300,000 to less than RM 3 million or full-time employees between 5 and 30	Sales turnover from RM3 million to not exceeding RM20 million OR full-time employees from 30 to not exceeding 75

Source: SME Corporation Malaysia

The massive number of SMEs that operate in Malaysia leads to the demand for access to finance. The World Bank also revealed that microfinance and SMEs is lack access to credit in emerging markets (Elasrag, 2016). The famous institutions in Malaysia that offer loans to SMEs are Amanah Ikhtiar, Tekun

Nasional, and financial institutions. However, due to the accelerated development of the Islamic finance industry and the establishment of Islamic SME financing offered by Islamic financial institutions, it is seen as an opportunity for all entrepreneurs to grab the facility. The largest Islamic financing providers for SMEs are Islamic banking, entrepreneur development institutions, and the private trust body. Table 2 illustrates the list of Islamic financial institutions that offer Islamic SME financing in Malaysia.

Table 2

List of Islamic financial institutions that offer Islamic SME financing

Affin Islamic Bank
Alliance Islamic Bank
AmIslamic Bank
Bank Islam Malaysia
Hong Leong Islamic Bank
Bank Muamalat Malaysia
CIMB Islamic Bank
Bank Kerjasama Rakyat Malaysia
Public Islamic Bank
RHB Islamic Bank
HSBC Amanah Malaysia
Maybank Islamic
Agro Bank
Al-Rajhi Bank

Source: Bank Negara Malaysia

According to Masuduzzaman, Akther, and Ara (2018), SMEs financed under Islamic banks are more efficient than those financed under conventional banks. However, the main practical problem confronting SMEs is the lack of knowledge and awareness towards Islamic financing product that suits their requirements (Elasrag, 2016). According to Ying (2019), SMEs are not fully aware of Islamic business financing facilities as financial institutions due to misconception of eligibility in the application process. Islamic financing is not just focusing on Muslims entrepreneur, but it is comprehensive, and all people are eligible to apply for its service. Additionally, the conventional bank's cost of credit is lesser than Islamic banking for the same sector. Lack of suitable Islamic finance offerings, poor management, and complicated application flow has led to SMEs' unsatisfactory response towards Islamic financing products (Alam, 2015).

The halal industry's continuous growth that focuses on the SMEs sector has also led to the increasing demand for Islamic financing products. Thus, Malaysia should offer a more competitive product in order to compete with the conventional financial player. On the other hand, Islamic finance's focus should be comprehensive to be competitive for all consumers rather than cater solely to Muslims' needs (Yusof, 2018). There is an urgent need to improve Islamic SME financing as SMEs' role is significant and getting stronger day by day. A proper framework for Islamic SME financing is crucial and should be illustrated in the best way to improve the facilities and services provided by Islamic financial institutions.

THE PRACTICES OF ISLAMIC FINANCING FOR SMES IN OTHER COUNTRIES: CHALLENGES AND OPPORTUNITIES

There are various practices in Islamic financial Institutions related to Islamic SME financing in various countries. For example, the study in Indonesia has explored current practice problems by Islamic financial institutions and proposed a better scheme (Huda, 2012). The study suggests the act of overcoming asymmetric information through a proper database of SMEs in every region and creating a valuation of SME for scoring an innovative credit. The Indonesian Islamic banks are about to charge a higher margin for its financing. Plus, banks prefer short-term financing, and more than 70 percent of their local funding is in the form of micro, small and medium-sized loans. The non-performing financing for SMEs in Indonesia has been recorded as higher than non-performing loans from conventional banks. The result of the evaluation helps the banks to assess the business's risk quickly. Therefore, this step helps the bank study SMEs' potential, and the study offers a framework in which Islamic financing schemes could thoroughly solve SME financing problems.

In Sultanate of Oman practice, SMEs' perception towards Islamic banking is not so positive, yet it is not too hostile. This is due to the lack of awareness and promotions by financial institutions in proposing Islamic finance as an alternative banking system to SMEs. Besides, Islamic banking in Oman is considered new since the first Islamic bank of Oman in 2011. Most SMEs' owners used their capital to inject into their enterprise (Subramaniam & Kumar, 2014). However, another recent study by Al Balushi et al. (2019), which focuses in Oman, has found that knowledge on Islamic financing of SMEs' managers influences their decision to used Islamic financing products. Although SMEs' managers intend to use Islamic finance to leverage their business capital, their business characteristic does not influence their decision. This implies that SMEs in Oman are still in development stages where Omani regulators require more time to have mechanism that can match Islamic financing requirement for SMEs in Oman (Al Balushi et al., 2019).

A study by Mumani (2014) investigates the SMEs' perceptions in Jordan towards the performance of Islamic financing and understanding of Islamic financing concepts. The Islamic banking system starts the developmental role to reduce the rates of unemployment. Therefore, by offering adequate resources through Musharaka (partnership), the new policy was implemented in order to assist the craftsmen, experts, and unemployed participation in SMEs. The programme also evolved to become a single programme called finance craftsmen. SMEs and professionals with the following characteristics: i) the borrower and bank, ii must bear both profit and loss) the required needs, which include financial skills, administrative and experience, should be provided by the bank to the borrower, iii) the monthly installment payment is not obligated by the borrower, iv) allocates the net income into three shares: a) the effort of entrepreneur b) bank that invested the money, c) a share allocated to the business owner to buy the bank's shares, and v) service provides by the bank to the owners of SMEs. The results showed the SMEs to believe that Islamic financing is holding an essential role in developing SMEs. To achieve better performance, the Islamic banks suggested on having a separate department to support and look after all related SMEs issues.

In South Afrika, the first bank was established in 1989, which is South Africa Albaraka Bank. It performs the zero-interest loan, and as an intermediaries business, where the profit and loss are shared in their business practices (Hove, Sibanda, & Pooe, 2014). The practice in Egypt is based on a report by International Finance Corporations. According to takaful, the rule and element in Islamic banking practices need to fulfill the obligation for Islamic banks in order to indemnify customer deposits. Additionally, all outlines of the processes for conventional banks to open Islamic banking windows must be kept in separate accounts from conventional ones. In order to oversee all activities of Islamic banks, the formation of an independent Sharia authority must have no less than three Sharia advisors that registered with the central bank (IFC, 2017).

Hachimi, Salahddine, and Housni (2017) compared conventional to Islamic banking and finalised SME financing by stating Islamic financial institutions as can be studied according to three criteria: the amount of investment and the profit of the enterprise, and the risk. These criteria summarise the features of participatory banks compared to conventional banks. A study from Turkey shows that Islamic banks are more inclined to finance SMEs than conventional banks (Aysan, Disli, Ng, & Ozturk, 2016). While in Pakistan, Hasan Raza, Ahmed, Osama, and Ahmed (2017) reported that 11 percent of the SMEs feel well-served, and 22 percent claimed to be underserved. The other 67 percent agreed that they remain un-served by the bank sector either in Islamic or conventional. It is because the majority of the SME entrepreneurs tend to avoid this financing opportunities due to religious reasons. Therefore, the researcher proposed the potential Islamic financing market for SMEs as it complies with Sharia compliance and align with the entrepreneur's beliefs.

In Saudi Arabia, most of the entrepreneurs in SMEs are still not in favour with Islamic finance's environment despite the development and recent growth of new Islamic financing products. The problem arises from the weakness in Islamic financing infrastructures regarding trade development and its capabilities (Saaid, 2013). A study in Sudan has been done related to Islamic finance is found to have biases towards SMEs that relatively smaller, less of asset, income, and skill. To balance bias and improve SMEs' facilities and access to Islamic finance, the measurement of policy reform should take place (Magbul & Hassan, 2017). Elasrag (2016) agreed that SMEs are vital to developing countries, especially when it represents most employment for a particular country. Therefore, to ensure the SMEs' sustainable growth, each financial institutions mustt attain a strong financial support and become reliable for the entrepreneurs.

According to Matarneh and Almanaseer (2015), Bahrain's government has introduced Islamic financing instruments for small and medium-sized enterprises known as *Tamkeen*, which refer to fostering enterprises' creation and development and providing supports to enhance the productivity and growth of both enterprises and individuals. The result extracted from the study proved that the development of Islamic modes of financing is directly reflected in the growth of the Bahraini economy.

Shaban, Duygun, and Fry (2016) have investigated the growth of SME lending by Islamic banks. In terms of market share competition, the result has revealed a decrease of the amount of SMEs lending through Islamic banks. However, from the side of price competition, the variety of product range has led to an increase of market share. A lending framework is an integral part of encouraging SMEs to lend with Islamic financial institutions and raise borrowers' number. Additionally, a lending framework should be transparent to the borrower, especially in exposing the transaction cost and taxes that include for an involved transaction. Clear information about the cost can convince SMEs to choose the funding for their business. In Islamic financial institutions, apart from raising money from the borrower, it could intensify lenders' transparency and credibility.

Haque (2016) highlighted the form of Islamic Finance in Morocco Conference in 2016 that changed the tax policies for Value Added Tax into Direct Tax to help Islamic financial institutions raise more money through revenues. Thus, Islamic financial institutions always have a strategy to earn money while maintaining a good practice for both sides of benefits. Meanwhile, the recent study in Morroco conducted by Ziky and Daouah (2019) has found that SMEs in Morroco are aware of Islamic financial products, especially those that can help them keep operating their business. Based on the Theory of Planned Behaviour (TPB), costs, risk, and suitability of financial products become the important determinants for SMEs' owners to adopt Islamic financing products (Ziky & Daouah, 2019). Badaj and Radhi (2018) also conduct a study in Morocco, in a way to investigate the perceptions of SME toward profit and loss sharing financing in Morocco. SMEs' owner behaviour, attitudes, family, and external supports also play their role in determining SMEs' intention to adopt the financial product. This implies that Islamic banking should take every possible opportunity to serve the small and medium companies by offering financing products according to the SME's requirement. Moreover, understanding SMEs' behaviours in taking financing products for their business could provide a significant insight for the banks to innovate financial products that can meet SMEs' needs.

In this rapid competitiveness, depositors and bank customers tend to look for a versatile bank that meeting their financial needs and entertain all inquiries. Therefore, advisory services are crucial to improve profitability, expand the market share, and be survive the tough competition. Business management is crucial to SMEs as this business development is intensely stimulating in recent years. SMEs' knowledge is still in starting mode to learn about new businesses. Thus, sufficient knowledge should become the primary agenda to the Islamic financial institution by providing sufficient knowledge about finance, management, business skill, and government's regulations and guidelines that directly and indirectly impactable to the operation of their business (Elasrag, 2016). Furthermore, to achieve customer satisfaction in Islamic financial institutions, Janahi and Almubarak (2015) and Ali and Raza (2015) highlighted the qualities of customer service, specifically on compliance, responsiveness, empathy, tangibility, reliability, and assurance.

Islamic banking product is a standard yet new knowledge to future customer, and the information of it need to be delivered accurately, especially on product offering and eligibility. Hence, regular promotions and active knowledge sharing should be undertaken to facilitate the transfer of knowledge, penetrate the market, and prepare future customers with comprehensible products' understanding and the functions of other Islamic banking (Rhanoui & Belkhoutout, 2017). A platform for knowledge sharing among practitioners may help in promoting interactions, information sharing, and spread the standard of Islamic financial documents (Abuazoum, Azizan, & Ahmad, 2013; MIFC, 2016). According to Hasan (2015), financial institutions should create campaigns to improve business and bank policy in a way to promote information sharing. Information sharing mechanisms should be established and improved by Islamic financial institutions in order to ensure the targeted person or customers can reach the information created.

THE PRACTICES OF ISLAMIC FINANCING FOR SMES IN MALAYSIA: CHALLENGES AND OPPORTUNITIES

The Islamic finance industry's growth nowadays cannot be denied when it operates Islamic financial institutions globally. Besides, in the greater and global visibility of Islamic finance, SMEs should take an opportunity to stand out as Islamic finance, which can help boost the industry of SME (Bizhive, 2015). Based on the speech by Bank Negara Governor, Datuk Nor Shamsiah Mohd Yunus, the statistics of Islamic financing from Islamic financial institutions is currently accounted for 34.1 percent of total financing (2008: 14.9 percent) (Bernama, 2019) and continued to expand at a faster pace. Banks' participation is seen to have an essential role in SMEs' growth by providing greater access to financing (Rahman, 2017).

A study conducted by Selvanathan et al. (2018), found that religious, bank reputations and the cost-benefits are factors that can influence customers to choose Islamic bank product and its services in Malaysia. Therefore, those factors can be applied to the framework in attracting SMEs' to choose Islamic banks to finance their business. However, Md Azmi (2020) argues that SMEs in Malaysia depend too much on attitudes that influence their networking opportunities and daily business routine. Negative attitudes, such as reluctance to seek support, demotivation, and lack of financial support, could bring bad performance on both owners and their business (Md Azmi, 2020).

Wasiuzzaman and Nordin (2019) highlight that SMEs' business characteristics (i.e, credit history) influence the decision to apply for financial loans. The researchers also found that SMEs with poor credit history are posited among the highest applicants of financial loans. This indicates that SMEs actually have low knowledge and awareness about the Malaysian marketplace. The researchers also imply that banks particularly should create awareness and knowledge for SMEs to understand the financing policies and create equal opportunities for them to emerge their potential in the marketplace. Having business networking with other large firms also determines SMEs' financial access (Wasiuzzaman, Abdullah & Vinayan, 2020). Wasiuzzaman et al. (2020) argue that SMEs' financing access depends on their character, collateral, and other larger firms. This implies that lenders (i.e, banks) seek more information regarding SMEs' characteristics before providing loans to them.

Study regarding customers' perceptions of Islamic banking in Malaysia is mostly derived from the Theory of Planned Behaviour. It is important for the Islamic bank to understand customers' behaviour before engaging them with their products and services (Ibrahim, Fisol & Haji-Othman, 2017). Ibrahim et al. (2017) studying the customer intention to purchase Islamic home financing products by applying Theory of Planned Behaviour (TPB). It is worth noting that customers who are aware of Islamic financial products and attain sufficient knowledge of it would have a higher intention of choosing Islamic financial products. Moreover, religious factors play a vital role in determining customers' behaviours. Therefore, Islamic banks need to understand the issues and challenges faces by SMEs before offering financial products to the public.

Due to SMEs' growth in the marketplace, fund availability and accessibility have become debatable (Ramlee & Berma, 2013). The issues have been around for a long time in academic research. It becomes crucial when Sustainable Development Goals (SDGs) is established in 2015 and highlighted SMEs as a leading role to boost economic growth in every country (United Nations, 2015). According to Hamilton and Beck (2016), SMEs can create a significant source of jobs across all economical and geographical areas that focus on public service to high and low-skilled people. Thus, governments and related parties should focus on SMEs' needs to ensure SMEs' growth is supported and sustained in the long run. This is important for the sake of the performance of the country's income and helping the citizens by providing job opportunities.

Malaysia has promoted Islamic SME financing by providing rebates to 874 SMEs under Sharia-compliant SME Financing Scheme (SSFS) that is participating by Islamic banks amounting to RM20 million in total, which is a 2 percent profit rate charged on the financing will be borne by the government (Tuah, 2013). Bank Negara assistant governor Adnan Zaylani Mohamad Zahid has mentioned at the "Islamic Finance Rendezvous Series" in January 2019: Islamic finance can act as an enabler of growth SMEs in related areas, which provides an alternative form of financing for SMEs.

However, according to Bank Negara Malaysia (BNM), there is a misconception about Islamic financing facilities among SMEs in Malaysia (Ying, 2019). Thus, the access to finance of SMEs provided by Islamic financial institutions becomes complicated when it is having unclear information and awareness among the SMEs. Some of them still have the misconception that Islamic finance is dedicated only to Muslims. The confusing information that speculated among SMEs has led to a decrease in Islamic financial institutions' awareness and its financing facilities for both Muslim and non-Muslim.

Thaker and Khaliq (2016) suggested a framework that focuses on service quality comprising Sharia requirement, reliability, assurance, responsiveness, website efficiency, and tangibility. This is because Malaysia practices a dual Islamic banking system, and the selected attributes will help in maintaining a competitive edge over conventional banks. To improve SMEs' access to finance, the lending framework should have a reliable mechanism and offers adequate resources (Mumani, 2014) to deliver lending information in the best way. Magbul and Hassan (2017) suggest making some policy reform measurements to balance bias in lending parts.

RECOMMENDATIONS

The rapid growth of Islamic finance in Malaysia is aligned with the vision and missions of the government. Thus, creating a wise banking environment that retains the aspired ethical banking and instills professionalism is hopefully helpful in producing a prudent Islamic finance hub for this region. After a thorough literature review about the practice of Islamic SME financing in Malaysia and other countries, there are many rooms for improvement to enhance SMEs in terms of its efficiency and performances. Entrepreneurs should grab the opportunities provided by the governments as well as Islamic financial institutions.

The review of the different countries and methods are the main points to be concluded. There is also a need for a new framework to solve the problem that arises among SMEs worldwide, which are affecting SMEs' performance and growth. Inefficient management and strategy to boost the SMEs has become the main reason for performance volatility. SMEs should be managed by separating the department for SMEs in every Islamic bank so that all problems would be focused within one centre. The standardisation of documentation and contracts that compatible with Sharia's requirement should be practiced to improve people's sensitivity and awareness of SME financing. Additionally, some entrepreneurs avoid grabbing Islamic financing opportunities due to religious reasons. Thus, to balance the bias and enhance Islamic SME financing in all parts, some policies reform (Magbul & Hassan, 2017) should be done, and the proper framework should be developed thoroughly (Huda, 2012).

Standardisation in contracts, accounting, and documentation, must be practiced, and information technology needs to be compatible with Sharia requirements. These practices shall enhance financial returns and performance as well as improve governance. The standardisation of Sharia compliance must be extracted from four primary sources, which are the interpretation of Al-Qur'an, interpretation of *hadith*, *Ulama' Ijtima'* which is the consensus amongst scholars, and lastly using *Qiyas*, which is the analogical deduction or individual reasoning for specific problems (Ullah, 2014). Besides, the main activities must be aligned with Sharia compliance; Majeed & Zainab (2017) firmly suggest that Islamic finance's business must prohibit from interest because it represents the money earned without putting any effort. Proper Islamic financing systems that align with shariah compliance is based on a fair risk-sharing. The pre-determined ratio of risk between lender and borrower needs to be involved in Islamic financial contracts and transactions.

The businesses also need to focus only on legal business and not included all immoral and socially harmful activities. The practice of asset-backed finance and easy access to *Qard-ul Hassan* is also one of the best ways to properly practice Islamic financing. The criteria highlighted must be parallel with the guideline established by the central bank, securities commissions, and authorities responsible so that the standardisation could be done and centralised to all standards needed. On the other hand, a separate account for Islamic transactions should be practiced by Islamic banking windows rather than conventional ones (IFC, 2017). Additionally, a registered Sharia advisor must be up to three persons to ensure that all Islamic transactions run properly.

To pursue the Islamic financial system's perfect practice, human resources have to be well-prepared with the basic of Islamic finance that aligns with Sharia compliance. Ullah (2014) and MIFC (2016) suggest that every Islamic institution need to hire a Sharia expert, prepare a proper training to do the task related to Islamic finance, and have a strong fundamental of Sharia background. According to Rahman (2017), an expert plays a significant role in strengthening the bank's participation in the SMEs business. The central bank also has to create special supervision that only focuses on Islamic banking and related issues. Besides, to boost human resources' better practice in the Islamic financial system, study tour and on-the-job-training can be beneficial tools. Even in a more developed market like Dubai, human resources is still a real problem; therefore, this issue has to be taken care of by proposing an appropriately skilled employee that work within the industry and offering globally recognised qualifications to properly train the qualified human to understand the requirements for Sharia compliance and deal with the difficulties of Islamic Commercial Law (Rhanoui & Belkhoutout, 2017).

Apart from strengthening the documentation and better practice of human resource, government and the owner of SMEs should be aware of the promotions of Islamic banking products that offered by Islamic financial institutions (Alam, Magboul, & Raman, 2010). The problem arises about misconception among SMEs is due to the lack of promotion, guidelines, and framework that need to be provided by all related parties. Thus, government and Islamic financial institutions should provide a framework, graphical flyer for promotion and flowchart on eligibility, and apply for Islamic business loans at Islamic financial institutions.

ACKNOWLEDGEMENT

Universiti Malaysia Terengganu supports this work under the research grant entitled Talent and Publication Enhancement – Research Grant (TAPE-RG - 55174).

CONCLUSIONS

The steadfast growth of the Islamic finance industry has led to the demand for Islamic financing including SMEs, which are managed by Islamic financial institutions as the largest lender. In the growth and raises of the number of SMEs, some challenges should be tackled to improve the development. Islamic SME financing is seen to have poor management due to the report and news exposed by the government and SMEs. Although SMEs are knowingly to be the backbone of economic growth in country, however there are seemingly have limited sources to grow their business. Industries with such important role in national economic should grab every opportunities to grow their business and maintaining their individual business operations for long terms. Islamic banks particularly could take opportunities to provide financing products toward SMEs and help them operates. The individuals characteristics and behaviours of SMEs' owners are recognised by previous studies as one of the important factors that determine their financing decision. Explanation of such behaviour mostly derived from TPB, where attitudes, religiousity, and external factors influence the decision of SMEs owners to take financing products. However in Malaysia, SMEs' owners' attitudes, and their lack of readiness to take opportunity become barrier for them to grow. Such barriers created within SMEs' owners would hold them from receiving financial leverage by financing companies and banks. Moreover, the concept of Islamic banking is seemingly misunderstood by SMEs, due to the lack of understanding upon Islamic financing. This misunderstanding should be encountered by Islamic bank and regulators through training, seminars and education to SMEs regardless their status or religions. Thus, to have a proper framework for Islamic SME financing is through an urgent agenda that held by the government and practitioners.

There are limitations that worth to highlight in this paper. This study only discussed the literature review related to the Islamic financing on SMEs. The discussion on this issues cannot be confirmed since the empirical evidences are yet to be conducted. It is recommended in the future that more precise and sounded theoretical framework should be done in order to gain more evidence regarding the concept of Islamic financing to SMEs.

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