

ISLAMIC SME FINANCING IN MALAYSIA: AN ANALYSIS OF PRODUCT OFFERINGS BY ISLAMIC BANKS

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Abstract: *Small and Medium Enterprises (SMEs) are vital to Malaysia's economic growth, yet many faces persistent challenges in accessing suitable financing. Islamic finance, grounded in Shariah principles, presents an ethical and inclusive alternative to conventional financial systems, particularly for SMEs operating in the halal economy. This study aims to examine the Islamic SME financing products provided by Islamic banks in Malaysia. Using a qualitative content analysis approach, data were collected from annual reports, product disclosure sheets, and official websites of 16 Islamic banks operating in Malaysia for the year of 2025. The findings reveal that while most banks offer financing products such as term financing and working capital facilities, primarily structured around Tawarruq and Commodity Murabahah. There is limited use of equity-based or risk-sharing instruments like Musharakah or Mudarabah. Larger and more established banks tend to offer more diversified and specialized products, while others offer limited SME-focused services. The study concludes that although Islamic banks have made progress in serving SMEs, their offerings remain predominantly debt-based and conventional in structure. There is a need for greater innovation and customization to fully align Islamic SME financing with Shariah principles and the diverse needs of SMEs.*

Keywords: Islamic finance, SME financing, Shariah-compliant products.

1. Introduction

Small and Medium Enterprises (SMEs) are recognized globally—and in Malaysia in particular—as essential contributors to economic growth, job creation, and innovation (World Bank, 2019; SME Corp Malaysia, 2024). As of 2023, SMEs comprised 96.9% of all business establishments in Malaysia and contributed 39.1% to the national GDP while employing 48.5% of the labour force (DOSM, 2024).

Despite their economic significance, SMEs often struggle to access adequate financing, particularly from formal institutions. Studies have highlighted that access to finance remains a top barrier to SME growth, largely due to issues such as high collateral requirements, limited credit history, and information asymmetry (Albertazzi et al. (2025); Wasiuzzaman & Nurdin (2019); Yuan et al. (2019). This situation applies not only globally but also within Malaysia's dual banking system, where Islamic banks coexist with conventional banks.

Islamic banks, while offering products aligned with Shariah principles, have historically focused on corporate clients rather than developing customized solutions for SMEs. This is attributed to difficulties in assessing SME creditworthiness and designing suitable financing structures (Kandasamy et al., 2018). However, increasing demand from the SME sector has prompted Islamic banks to expand their offerings.

By 2023, Islamic financial institutions accounted for 12.5% of financing disbursed to microenterprises and SMEs, suggesting growing involvement in SME development (DDCAP Group, 2024). However, detailed information about the specific Islamic SME financing products remains scarce.

Given this context, the study aims to examine the types of Islamic SME financing products offered by Islamic banks in Malaysia, addressing a significant gap in both literature and practical understanding.

2. Literature Review

The literature emphasizes Islamic finance as a vital alternative for SMEs, particularly those aiming to align with Shariah principles. However, despite Malaysia's leadership in Islamic finance, there is a persistent gap in integrating halal operations with Shariah-compliant financing. As Awang et al. (2020) highlight, only 17.4% of SMEs have successfully obtained financial support, pointing to a weak financing ecosystem for halal-focused businesses.

One major challenge is the institutional disconnect between halal regulators like JAKIM, who focus solely on raw materials and operational compliance, and Islamic financial institutions, which manage funding aspects separately (Hassan et al., 2023). This lack of coordination leads to fragmentation where SMEs must navigate halal certification and Shariah-compliant finance independently, with limited support (Ahamat, 2017).

Moreover, the products offered by Islamic banks are often generic and not tailored to the unique needs of halal SMEs, causing a mismatch between supply and demand (Antara et al., 2015; Awang et al., 2020). Many Islamic banks design products based on risk-averse, profit-driven motives, which differ from the ethical and operational goals of halal SMEs (Jaffar & Musa, 2014; Muhamed et al., 2014).

Further, SMEs are often left out of policy and regulatory dialogues, leading to a lack of guidance in implementing Islamic finance (Awang et al., 2020). Awareness and knowledge gaps continue to hinder adoption, as many SME owners lack understanding of the benefits and processes involved in Shariah-compliant financing.

Overall, while Malaysia has a strong Islamic finance system and a mature halal certification framework, integration between the two remains limited. There is also limited academic focus on specific product offerings of Islamic banks to SMEs. Therefore, there is a pressing need to examine the range, structures, and Shariah principles underlying Islamic SME financing products in Malaysia (Muhmad et al., 2020; Abdullah & Oseni, 2017).

3. Research Methodology

The study employs a qualitative content analysis approach in examining the Islamic SME financing products provided by Islamic banks in Malaysia. The data for this analysis was collected from secondary sources, primarily the annual reports of 16 Islamic banks in Malaysia, along with official product disclosure sheets, bank websites, and regulatory publications such as those from Bank Negara Malaysia and SME Corp Malaysia.

A systematic coding framework was developed to extract and categorize key information, including the types of products and the underlying Shariah contracts (e.g., *Tawarruq*, *Murabahah*, *Wakalah*). The aim was to create a comprehensive overview of the range, structure, and variation of Islamic SME financing products offered by each bank.

This content analysis allowed to identify patterns in product offerings, innovation levels, and institutional priorities across different banks, forming the basis for evaluating how well Islamic banks align with the financing needs of SMEs.

4. Findings and Analysis

The findings reveal that Islamic banks in Malaysia offer a diverse range of SME financing products, though the level of variety and complexity differs significantly across institutions.

| NO. | BANK | ESTABLISHED (Hamzah et al., 2024) | PRODUCTS | SHARIAH PRINCIPLE |
|-----|---|---|--|--|
| 1. | Affin Islamic Bank | 2006 | Tawarruq Term Financing-i Tawarruq Cash Line-i (CL-i) | Tawarruq, Wakalah & Wa'd |
| 2. | Al-Rajhi Banking & Investment Corporation (Malaysia) Berhad | 2006 | Cashline-i | Commodity Murabahah (via Tawarruq arrangement) & Wakalah |
| 3. | Alliance Islamic Bank | 2006 | Commodity Murabahah Term Financing-i Cashline Facility-i | Commodity Murabahah (via Tawarruq arrangement) |
| 4. | AmBank Islamic Bank | 2006 | Cash Line Facility-i (Small Medium Enterprise (SME)) SME Term Financing-i | Tawarruq, Wa'd, Murabahah & Wakalah |
| 5. | Bank Islam Malaysia Berhad (BIMB) | 1983 | Business Cash Line-i Term/Business Financing-i | Tawarruq |

| | | | | |
|-----|--|------|---|---|
| | | | Multi Trade Facility-i | Murabahah Purchase Order (MPO) & Bay' Al-Dayn |
| 6. | Bank Muamalat Malaysia Berhad | 1999 | Term Financing | Tawarruq, Murabahah, Wakalah, & Wa'd Mulzim |
| | | | Mcash (Cashline) | |
| | | | Mcash (Invoice) | |
| 7. | CIMB Islamic Bank Berhad | 2003 | Term Financing-i | Commodity Murabahah |
| 8. | Hong Leong Islamic Bank Berhad | 2005 | Commodity Murabahah (CM) Flexi Term Financing-I | Tawarruq |
| | | | CM Cashline-i | |
| 9. | HSBC Amanah Malaysia Berhad | 2008 | Cash Line-i | Commodity Murabahah |
| | | | Commodity Murabahah Financing-i | Commodity Murabahah |
| | | | Business Premises Smart-i | Diminishing Musharakah |
| | | | Industrial Hire Purchase-i | Al-Ijarah Thumma Al-Bai (AITAB) |
| | | | Revolving Financing-i | Commodity Murabahah |
| 10. | Kuwait Finance House (Malaysia) Berhad | 2005 | N/D | N/D |
| 11. | Maybank Islamic Berhad | 2008 | Commodity Murabahah Term Financing-i (CMTF-i) | Murabahah via Commodity Murabahah/Tawarruq |
| | | | Cashline Facility-i | Tawarruq |
| | | | Tradeline-i | Murabahah via Commodity Murabahah/Tawarruq, Wakalah, Wa'd, Bay' al-Dayn & Kafalah |
| 12. | MBSB Bank | 2005 | Term Financing-i | Tawarruq/Istisna' & Ijarah |
| | | | Cashline-i | Tawarruq |
| | | | Revolving Credit-i | Tawarruq |
| | | | Bank Guarantee-i | Kafalah |
| | | | Letter of Credit-i | Murabahah/Wakalah |
| 13. | OCBC Al-Amin Bank Berhad | 2008 | Cash Line-i | Commodity Murabahah & Tawarruq |
| 14. | | 2008 | Cash Line Facility-i | Bai' Inah & Murabahah |

| | | | | |
|-----|----------------------------------|------|----------------------|---|
| | Public Islamic Bank Berhad | | Term Financing-i | |
| 15. | RHB Islamic Bank Berhad | 2005 | Term Financing-i | Commodity Murabahah, Tawarruq & Wakalah |
| | | | Overdraft-i Facility | |
| 16. | Standard Chartered Saadiq Berhad | 2006 | Cashline-i | Tawarruq |

Notes: N/D – Not disclosed in website

The analysis of Islamic SME financing products provided by Islamic banks in Malaysia revealed a substantial variety of offerings, though the range and complexity differed notably between institutions. From the 2025 data across 16 Islamic banks, two categories of financing products were found to be the most commonly offered: term financing and working capital facilities. Term financing products such as *Term Financing-i* and *Commodity Murabahah Term Financing-i*, along with working capital solutions like *Cash Line-i* and *Business Cash Line-i*, were widely available. These products reflect a strong emphasis on fixed-return instruments tailored to support the capital and operational needs of SMEs.

A smaller number of banks extended their services into more specialized areas of SME financing. For instance, institutions like Bank Islam, MBSB Bank, and Maybank Islamic offered trade and multi-purpose facilities such as *Multi-Trade Facility-i*, *Letter of Credit-i*, and *Vendor Financing-i*. HSBC Amanah and Bank Islam also provided niche offerings like *Industrial Hire Purchase-i* and *Business Premises Smart-i*, indicating efforts to diversify beyond basic financing tools and cater to specific SME requirements.

Regarding the underlying Shariah principles, the most frequently applied contracts across these products were *Tawarruq*, *Commodity Murabahah*, *Wakalah*, and *Murabahah*. These contracts support structured and asset-backed financing, commonly used in cashline and term financing arrangements. Less frequently used were contracts such as *Bay' al-Dayn*, *Musharakah*, and *Ijarah*, which are more aligned with equity-based and partnership models of financing.

Notably, banks with longer operating histories and larger Islamic portfolios, such as Bank Islam, Maybank Islamic, Bank Muamalat, and HSBC Amanah, demonstrated more diversified and innovative product offerings. In contrast, some banks, particularly those with foreign ownership or newer Islamic banking divisions, provided limited or non-disclosed information on their SME products. Kuwait Finance House, for example, did not disclose sufficient information on its SME financing offerings, highlighting gaps in transparency and public accessibility of product data.

Overall, the findings indicate that while Islamic banks are actively involved in supporting SMEs, their product strategies still largely rely on debt-like structures that mirror conventional financing. This accentuates a need for further innovation in product development, especially in introducing more risk-sharing and equity-based instruments that are more aligned with Shariah principles, and the unique financing needs of SMEs in Malaysia.

5. Discussion and Conclusion

The examination of Islamic SME financing products offered by Islamic banks in Malaysia reveals meaningful progress in the development and provision of Shariah-compliant financial tools for SMEs. Most banks have responded to the financing needs of SMEs by offering a range of products centered around working capital and term financing. These products are often built upon the Tawarruq and Commodity Murabahah contracts, which are widely used for their compatibility with structured debt-like instruments. This reflects the banks' focus on providing stable, asset-backed financing solutions within the constraints of Shariah law.

However, the findings also indicate that the majority of Islamic SME financing products are concentrated around conventional-style structures, primarily replicating the risk-averse lending practices seen in traditional banking. While these instruments provide a degree of access to financing, they do not fully utilize the potential of Islamic finance, which offers broader models such as profit-sharing (Musharakah, Mudarabah) that may better suit SMEs facing uncertain cash flows or needing long-term investment support. The limited use of such equity-based contracts highlights a conservative approach among Islamic banks in Malaysia, which could be due to regulatory preferences, operational challenges, or risk management concerns.

Another notable point is the variation in product offerings across banks. More established Islamic banks such as Bank Islam and Maybank Islamic tend to provide a wider and more diverse set of products, including trade finance and niche facilities. This suggests that institutional maturity, market positioning, and strategic priorities influence the degree to which banks invest in developing SME-specific offerings. In contrast, some foreign or smaller institutions offer only a limited suite of SME financing options, and in certain cases (e.g., Kuwait Finance House), product details are not publicly disclosed. This inconsistency in transparency and depth of offerings may hinder SME owners from making informed financial decisions, especially those new to Islamic financing.

In conclusion, while Islamic banks in Malaysia have made commendable strides in catering to the SME segment, there is room for further innovation and diversification. The current landscape is dominated by Tawarruq-based products, and the low adoption of more inclusive, risk-sharing instruments limits the distinct value proposition of Islamic finance. For Islamic SME financing to fully realize its potential, banks must explore and scale products that align more closely with both the ethical foundations of Shariah and the dynamic needs of SMEs. This may involve not only new product development but also regulatory encouragement, improved financial literacy among SMEs, and closer collaboration with halal industry stakeholders to ensure a comprehensive Shariah-compliant ecosystem.

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