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The Role of Islamic Financial Technology in Fostering Digital Financial Inclusion:
The Malaysian Experience as a Model

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Abstract:
This research paper aims to examine the role of Islamic financial technology (Fintech) in promoting digital financial inclusion. The study concludes that the Islamic financial industry in Malaysia has undergone a significant transformation driven by digital technology. These technologies offer vast opportunities to enhance and develop Islamic financial services, improve transparency, facilitate transactions, and enrich customer experience. They provide optimal platforms for Islamic Fintech companies that offer alternative funding solutions for investments—yielding high returns at minimal costs—while delivering digital financial services that reach underserved populations facing financial hardship and funding delays. Furthermore, these innovations strengthen the financing ecosystem for small and medium-sized enterprises (SMEs), establishing Malaysia as a robust ecosystem and regulatory framework supporting digital economic growth.
Keywords: Islamic Financial Technology, Digital Financial Inclusion, Digital Finance, Islamic Fintech Companies

1. Introduction

Digital transformation is a cornerstone of the modern financial and banking sector. Customers increasingly rely on electronic applications and smart solutions to execute banking transactions. Financial technology possesses a genuine capacity to alter the traditional financial structure by rendering services faster, cheaper, safer, transparent, and accessible—particularly to large unbanked populations.

Access to financial services is vital for economic and social development. It enables individuals to secure funding for micro, small, and medium enterprises (MSMEs) and manage payments and transfers through formal accounts. According to the World Bank, 1.4 billion adults worldwide lack bank accounts, yet approximately 1.1 billion of them own mobile phones, highlighting an urgent need for digital financial inclusion to spur economic growth and job creation.

Malaysia stands out as a leading Islamic nation that has innovated financial products by leveraging rapid advances in Fintech. The country has digitized banking operations, created digital platforms, and designed tailored financial solutions.

1.1 Research Problem and Main Question

Based on the aforementioned context, the main research question is formulated as follows: Does Islamic financial technology play a role in promoting digital financial inclusion in Malaysia?

1.2 Research Hypotheses

- **H1:** Islamic financial technology innovates financial products and services by leveraging rapid advances in technology.
- **H2:** Islamic financial technology contributes positively to digital financial inclusion by enabling timely access to appropriate funding.

1.3 Significance of the Study

The importance of this research paper lies in exploring how Islamic Fintech fosters digital financial inclusion through faster, cheaper, and safer banking services that reach financially excluded populations, referencing Malaysia as a practical model.

1.4 Objectives of the Study

- **Analyze** the global Islamic Fintech landscape using the GIFT index.
- **Examine** the startup experience in Islamic Fintech and its core offerings.
- **Highlight** key Malaysian Islamic Fintech innovations within digital financial inclusion.
- **Determine** the specific impact of Malaysian Islamic Fintech on digital financial inclusion.

1.5 Research Methodology

This paper employs a descriptive-analytical methodology to collect and analyze data regarding major Islamic financial innovations in Malaysia that provide alternative investment funding, foster a regulatory ecosystem, and support digital economic growth.

1.6 Organization of the Study

To cover all relevant dimensions, this paper is divided into five sections:

- **First:** Conceptual Framework of Financial Technology
- **Second:** Islamic Fintech Startups and the GIFT Index
- **Third:** Principles and Mechanisms of Digital Financial Inclusion
- **Fourth:** Key Innovations in the Malaysian Islamic Fintech Industry
- **Fifth:** The Impact of Islamic Fintech on Digital Financial Inclusion in Malaysia

First: Conceptual Framework of Financial Technology (Fintech)

1. Definition of Financial Technology (Fintech)

• Digital Research Institute: Defined as the aggregate of modern technological inventions and innovations in finance, encompassing digital software used in banking operations, fund transfers, currency exchanges, interest/profit calculations, and investment yields (Goujil & Kerziz, 2021, p. 249).

• Basel Committee: Defined as technology-enabled financial innovation that could result in new business models, applications, processes, or products with a material effect on financial markets, institutions, and the provision of financial services (Meryem & Iman, 2021, p. 07).

• Financial Stability Board (FSB): Defined as technology-driven innovation in financial services resulting in new business models, applications, processes, or products with an associated material effect on the provision of financial services (Noureddine, 2020, p. 118).

2. Definition of Islamic Financial Technology

Islamic Fintech refers to modern Shariah-compliant digital financial applications and products deployed within financial institutions to create new tech-based business models, achieve Shariah objectives in finance, and improve banking services for Islamic banking clients (Alaa El-Din, 2022, p. 04).

3. Current Global Status of Islamic Fintech

According to the Global Islamic Fintech Report 2023/2024, the global transaction volume of Islamic Fintech was estimated at $138 billion (2022/2023) and is projected to reach $306 billion by 2027, representing a Compound Annual Growth Rate (CAGR) of 17.3% (Abdul Haseeb & Harri, 2022, p. 05). This outperforms the overall global Fintech industry projected CAGR of 12.3% over the same period. Reports from IFN Fintech indicate that over 417 Islamic Fintech companies currently operate globally across various emerging technologies.

Saudi Arabia, Iran, Malaysia, the UAE, Indonesia, and Kuwait represent the top six market drivers within the OIC, each exceeding $5 billion in market size and collectively accounting for 85% of the global Islamic Fintech market volume.

Second: Islamic Fintech Startups and the GIFT Index

1. Definition of Islamic Fintech Companies

Islamic Fintech companies are newly established ventures offering Shariah-compliant digital products and services. They focus on user needs and leverage technology to expand financial access efficiently and cost-effectively (Abdul Haseeb & Harri, 2022, p. 02). Emerging regional hubs leading in company counts include Indonesia (61 companies / 20%), the UK (45 / 15%), the UAE (42 / 14%), and Malaysia (37 / 12%) out of a tracked sample of 17 major markets (INCEIF University, 2022, p. 03).

2. Global Islamic Fintech (GIFT) Index

Developed by DinarStandard and Elipses, the GIFT index evaluates country performance across 64 nations using 19 indicators divided into 5 categories: Talent, Infrastructure, Islamic Fintech Market, Ecosystem, and Capital (Reem, 2022). Top-tier countries include Malaysia, Saudi Arabia, Indonesia, the UAE, and the UK. High-growth ecosystems include Bahrain, Bangladesh, Egypt, Iran, Jordan, Kuwait, Nigeria, Oman, Pakistan, Qatar, and Turkey.

3. Services Offered by Islamic Fintech Startups

Across 417 tracked firms, services are categorized into three main clusters (Abdul Haseeb & Harri, 2022, p. 08):

- **a. Giving and Protection (31 firms):** Includes Social Finance (Zakat, Waqf, Sadqah) and Insurtech / TakafulTech.

- **b. Savings and Investment (103 firms):** Includes Wealth Management (Robo-Advisory, Pensions, Asset Management) and Deposits/Lending (Personal finance, Mortgages, Student loans).
- **c. Financing (224 firms):** Includes P2P financing, Crowdfunding, Payments/Remittances, Capital Markets (Sukuk, Trading), Digital Assets, and Alternative Finance (MSME/Trade finance).

Note: Fundraising, deposits, lending, wealth management, payments, and alternative finance constitute 77% of all Islamic Fintech activities.

Third: Principles and Mechanisms of Digital Financial Inclusion

1. Definition of Financial Inclusion

• World Bank: Universal access to and use of affordable, formal financial services (payments, savings, credit, insurance) delivered responsibly (World Bank, 2020).

• Arab Monetary Fund (AMF): Availability and usage of formal financial products across all social segments, particularly marginalized groups, at competitive prices while protecting consumer rights (AMF, 2017).

2. Definition of Digital Financial Inclusion

Digital access to and usage of formal financial services by excluded or underserved populations, provided affordably and sustainably within an adequate regulatory framework (Talha & Al-Quran, 2020, p. 01).

3. Principles of Digital Financial Inclusion

Grouped into four main pillars (Souriya & Said, 2018):

- **1. Infrastructure:** Promote secure digital infrastructure, interoperable payments, and low-cost digital financial products compliant with AML and digital identity standards.
- **2. Policy Making:** Enhance data accuracy regarding access/usage and integrate digital financial inclusion into national strategies.
- **3. Regulation:** Implement regulatory reforms to reduce access inequalities and establish sandboxes for public/private digital innovation.
- **4. Literacy & Protection:** Build digital financial literacy and strengthen customer data protection tailored for youth, women, and MSMEs.

4. Operational Mechanism

Financial institutions deploy digital platforms and leverage big data analytics to offer tailored, low-cost savings, credit, insurance, and investment products, thereby expanding client bases while reducing operational costs (Al-Arabi, 2020, p. 03).

5. Drivers of Islamic Fintech Growth in Malaysia

Key factors establishing Malaysia as a global hub include (INCEIF, 2020, p. 03):

- • **A mature dual-banking framework** supported by Shariah advisory bodies.
- • **Proactive regulatory guidelines** issued by Bank Negara Malaysia (BNM).
- • **Strategic leadership** by the Malaysia Digital Economy Corporation (MDEC).

- • **National initiatives** positioning the Islamic Digital Economy as a Key Economic Growth Area (KEGA). The digital economy contributed 20% to Malaysia's GDP in 2020 (MYR 289 billion in 2019).

Key institutional initiatives include:

- • **AFAC (2015):** Alliance of Fintech Community launched by Securities Commission Malaysia.
- • **FTEG (2016):** Financial Technology Enabler Group formed by BNM.
- • **FAOM (2016):** Fintech Association of Malaysia.
- • **DFTZ (2017):** Digital Free Trade Zone for e-commerce.
- • **Malaysia Digital Hub (MDEC):** Provides co-working spaces (Orbit), scaling platforms (Titan), and Shariah advisory services.

Fourth: Key Innovations in the Malaysian Islamic Fintech Industry

1. Islamic Crowdfunding Platforms for SMEs

- **Nusa Kapital:** Founded in 2017 (operated by Ethis Kapital Sdn), it is a licensed Shariah-compliant P2P platform regulated by SC Malaysia and advised by ISRA. It utilizes Murabaha (cost-plus financing) structures for property and SME funding without charging interest (Habibah et al., 2021).
- **Global Sadaqah:** Founded in 2018, this platform manages Corporate Social Responsibility (CSR), Zakat, and Waqf funds. It raised MYR 450,000 via Ethis Malaysia to expand services like Qard Hasan (benevolent loans) for micro-enterprises and integrates with 11 payment gateways, including e-wallets, Bitcoin, and digital gold (Polly Jean, 2021).
- **Zakat Crowdfunding:** Initiatives guided by online models (such as pitchIN, MyStartr, and Ethis) streamline Zakat campaign submission, institutional vetting, donor funding, and automated progress updates.

2. Digital Insurance and Takaful Licenses (DITOs)

BNM issued frameworks in November 2022 to support embedded insurance and Insurance-as-a-Service, planning to issue up to five DITO licenses in 2024 (Rafi Uddin & Abdul Hassib, 2024, p. 01).

3. Digital Banking Licensing

Digital banking accounted for 4.6% of GDP in 2022. Key licensed entities include:

- • **GXBank:** Joint venture between Grab and Singtel; first to launch in November 2023.
- • **Boost Bank:** Axiata and RHB Banking Group joint venture launched in June 2024.
- • **Upcoming Consortia:** YTL-Sea and KAF Investment Bank.

Internet banking penetration stands at 98%, with account ownership at 92%. Mobile e-payment transactions grew by 31.5% in 2022 to 9.5 billion transactions.

4. Electronic Payment Platforms

Per capita e-payment transactions reached 343 in 2023. DuitNow QR (launched in 2019) serves as the unified national standard across banks and e-wallets (Rafi Uddin & Abdul Hassib, 2024).

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5. Digital Finance Adoption & Robo-Advisors

• Digital remittance transactions doubled (+106%) in 2022 to $5.54 billion.

• The Malaysia Co-Investment Fund (MYCIF) expanded its capital pool to MYR 300 million ($65.34 million) to support P2P and Equity Crowdfunding (Mordor Intelligence, 2024).

• Robo-Advisors: Digital wealth management assets reached MYR 1.6 billion across 1 million accounts in 2024. StashAway Malaysia serves over 50,000 clients with over MYR 1 billion in AUM.

Fifth: The Impact of Islamic Fintech on Digital Financial Inclusion in Malaysia

1. SME Empowerment Initiatives

- **MAD Cash:** Provides interest-free micro-loans to female entrepreneurs in weekly installments over 10 months.
- **microLEAP:** SC-regulated P2P platform offering micro-financing from MYR 1,000 to MYR 50,000. As of August 2023, it funded 27 projects totaling MYR 75.4 million (Nurul & Mastura, 2024, p. 344).
- **CapBay:** Supply chain Fintech providing working capital. By August 2023, it funded MYR 2.5 billion across 1,600 SMEs in 20 industries.

2. Key Contributions to Financial Inclusion

- **Product Innovation:** Launch of retail digital Sukuk and paperless SME digital financing (e.g., Maybank Islamic).
- **Consumer Adoption:** Over 90% of Malaysian bank customers regularly use digital banking services.
- **Regulatory Sandbox:** BNM's sandbox allows safe live testing of fintech solutions.

Conclusion, Findings, and Recommendations

Conclusion

Malaysia's comprehensive ecosystem—comprising regulatory support, Shariah expertise, digital infrastructure, and innovative platforms—makes it a global benchmark for Islamic Fintech and digital financial inclusion.

Key Findings

- **1.** Digital financial inclusion directly advances Sustainable Development Goals (SDGs).
- **2.** Islamic Fintech effectively reaches unbanked and underserved populations through tailored, low-cost digital platforms.
- **3.** Alternative financing mechanisms (P2P, Crowdfunding) bridge the funding gap for micro-enterprises and women entrepreneurs.

Recommendations

- **1.** Continuously update regulatory frameworks to accommodate fast-evolving digital business models.
- **2.** Invest in human capital and digital financial literacy programs.

- **3.** Expand institutional backing for Shariah-compliant digital platforms to improve credit access for MSMEs.

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