

CHAPTER VII

CONCLUSIONS AND RECOMMENDATIONS

7.1 Introduction

This chapter is devoted to providing a good explanation of the conclusions and recommendations drawn from the study and the findings. Based on the research question and objectives, and thus the findings from the interviews, the following conclusions and recommendations are made. This chapter also presents the implications for the practitioners and possible areas for future study.

7.2 Conclusion

The Islamic banking industry has come to stay but must consider all the dimensions of credit risk since there are different types of contract used with different types of exposure towards risks, because, if not, it will affect the whole performance and efficiency of the bank. While carrying out their daily business activity, they cannot have any lack of management of credit because it can lead to a total disaster for the bank as well as affect the customers. Islamic banks are still underperforming and still developing, therefore, it is good for this study to explore in advance how Islamic principles are used in credit risk management in the credit evaluation process, and thus the results from the interviews are useful to implement parameters from the credit evaluation process.

To extend this further, before the study provided a standpoint to write up this thesis, the study only knew what credit risk was, its importance towards credit risk

management in conventional-based and Islamic-based approaches theoretically. However, after the interviews with the selected banks to study the current practices and to identify the different practices between conventional practices and Islamic practices in the credit evaluation process, and thus after the interviews with the *Shariah* advisers to explore how Islamic principles are used, and how to implement good parameters for the credit evaluation process in Islamic banking approach, the study believes that there is a degree of credit risk management which is well thought out, which is important when banks, globally, and in Malaysia, particularly, are carrying out their financing decisions.

After the findings are drawn, the study still found that credit risk management really has a great role to play because it makes financing decisions less risky. It also helps banks to have a secure system of two-dimension credit risk management with different types of contract because Islamic banks are unique in terms of principles, which enhances the trust that banks might develop. It also helps to diminish the concept of risk to interest rates that the conventional banking approach apply. In addition, the study also came to realize that the commencement of credit risk management commences before the financing decisions until when it receives repayment from the customers.

Moreover, during the time of making financing decisions, the information needed and the most important elements collected are both valued differently by the different banks. Even though the trust is always borne mind, they must be aligned to avoid asymmetric information. No matter what the strategies used in attaining a good credit risk management, four (4) doctrines should be followed: The Day of Justice (Surah Al-Hijr, 15: 35), the Day of Evaluation (Surah Ghafir, 40: 32), the Day which

is Promised (Surah Al-Buruj, 85: 2) and the Day of Judgement (Surah Al-Mursalat, 77: 14).

To sum up the above discussions, the study has answered the research questions and achieved the objectives of the research.

7.3 Theoretical Contribution

The knowledge that the study contributed is based on the present challenges of bank officers in the banks that practice Islamic window of finance, also known as the dual-banking approach, and in banks that practice the full-fledged Islamic banking approach in Malaysia. Based on the previous theory regarding this topic of study, guarantees and collateral have been mentioned as being there to make up for a credit if a customer is unable to fulfill the payments within the specified time.

However, from the results of the interviewees' responses, one of them believed that Islam provides rules for good credit management. According to him, good credit management is based on the management during the lifetime and after death. During the lifetime, if customers are unable to make payments, he/she should appoint a guarantor. The contracts used are *kafalah*, *rahn*, *hawalah* and *muqassah* contracts. In addition, after the death of the customer, the bank may collect the financing from wealth heritage, or from their heirs, or from *baitulmal*, or, the financing will be brought to *akhirat*, as he/she must pay with rewards and sins.

practicing good deeds or *akhlak* with Islamic ethics in business, make a *syura* as well as discuss with customers constantly, place trust in Allah s.w.t. as practicing the conception of *taqwa*, and, lastly, schedule and re-schedule for financing if needed to extend the financing until the customer is able to pay. In addition, while evaluating all these elements, it does so while appraising its norms, policies, philosophy, practices and strategies.

For customers to have an effective knowledge for good credit management in line with Islamic principles they should make sure that two (2) main beliefs of credit/financing in Islam – *daruriyyat* (necessity) and *hajiyyat* (wants) – are aligned with the principles. Then, it will also be in line with the three (3) conditions for financing, which embraces *niat* (intention), *ghardu* (purposes) and eligible rate/amount for financing.

Furthermore, Islam also gives guidelines in respect of Islamic credit management with which the individual should be acquainted and applies in their daily routine of business activity. This includes during lifetime and after lifetime. In respect of reducing the credit risk arising during the lifetime, Islam gives rules for the use of *kafalah*, *hawalah*, *ar-rahnu* and *muqassah* contracts. These may also reduce the burden for customers in making payments. If not, Islamic banks may charge *ta'widh* or *gharamah* at 1 percent; the compensation being channeled for *sadaqah* (charity) purposes. Furthermore, in respect of after the lifetime, Islam gives rules for the use of wealth heritage to fulfill the financing, or take it from heirs, or take from *baitulmal*, or, if not, the financing will be brought to *akhirat* and will paid from rewards and sins.

However, after the validation process, there are four (4) issues stated which includes of Islamic elements, five C's and CAMPARI, sources of documents and

lastly, software documents. First, how these Islamic elements to be applied in practical? To solve this issue, banks may incorporate these elements in its Product Disclosure Sheet (PDS), the elements has to be explained to the customer at the time of signing the acceptance of the letter of offer and the financing documentation. Second, what is the significant of Islamic elements over five C's and CAMPARI? It is positive or negative consequences? To explain this issue, of course it is positive when Islamic banks and customer practice the Islamic elements. The Islamic elements add value over the five C's and CAMPARI but the terms should be synchronized as mention in findings in this research study. Third, how Islamic banks get sources of documents in making financing decisions by using these Islamic elements stated in parameter? To explain this issue, Islamic banks has to rely on the client for his financial and business information. Additionally, Islamic banks can source client's credit/payment history from Bank Negara Malaysia (BNM) and other reliable sources such as referral from the customer's existing financier(s). For instance, if the customer is found to be a bad paymaster of his/her existing bank (whether conventional or Islamic bank), then his *akhlak* is questionable. In this case, his/her application with Islamic banks may be rejected. Lastly, do Islamic banks need to develop software as aim of implementing this parameter? To solve this issue, for sure, having the necessary software will definitely help the Islamic banks to perform their credit evaluation process effectively. For instance, Islamic banks may have already installed Financing Origination System (FOS) or any similar system to track the status of the clients' business financing application.

To sum up from the above discussions, the study found that any development to strengthen credit risk is always welcome. As already mentioned, the parameter

provides the value add mechanism in achieving a thorough financing evaluation process. However, Islamic banks must be mindful that moving forward, the financing or credit officers must have the necessary skills and experience to handle the proposed parameter and they have to be well trained. As a result, it is good to implement this parameter if the clients are ready to embrace this parameter and the bank personnel have the necessary experience and skills.

7.4 Recommendations for Further Research in Credit Risk Management

The study recommends that for the Islamic banking industry to have a developed industry with Islamic principles that are well-practiced, as well as to accomplish greater success, they should continuously ensure an ability to value all the information regarding the customer's business operation, physically and spiritually of customers, with a high level during the financing decisions. The reason of being that the information that they might consider as being not very important might possibly lead to a miscarriage in their financing decision process or the capacity from which customer's default arises.

Bank practitioners should be duty-bound to bear in mind that the two dimensions of credit risk management in the line of the pre- and post-approval stages of financing is not to be acquainting with or stopped at a particular stage of the business banking activity, but should be a continuous process. Therefore, the study believes that this will lead to greater attainment or success since credit risk, which leads to supplementary to the key activity of the banks and cannot be avoided.

In addition, to sustain in the banking industry, bank practitioners should follow the step-by-step process in managing credit risk, policy guidelines and make sure their

customers know them well. Both should have a continuous relationship as well as share the risks. The study believes that these may avoid some problems and the issue of confusion in the case of the absence of the predecessor.

The study also believes that for a good relationship with customers, as in the business financing activity, both should be aligned from the beginning in making financing decisions, and throughout the business to make it easier to identify, and, if possible, solve problems in time before they get out of hand. This can diminish the issues beforehand, and automatically lead to good solutions.

In addition, bank practitioners should always bear in mind “*what if*” questions in making financing decisions. This is because they are operating banking business in a very unstable and dynamic environment. To extend this further, as proposed by the responses from the respondents in this study, Islamic banks should be more pro-active in making financing decisions, the implementation of Islamic principles in the pre- and post-approval stages of financing decisions as well as collaborate more with *Pusat Zakat* and *Majlis Agama Islam Negeri* in handling issues arising from high default cases.

7.5 Practical Implications

The study puts forth the following practical implications:-

1. Bankers should learn to document all the financing decisions that they take even if they are from personal reasoning and keep discussing (*syura*) with customers to have good values to ensure a tight relationship with Islamic banks so that they are able to fulfill their obligations.
2. The values are more important than cash. Thus, banks and customers, as both of them are in a partnership in doing business, are based on a series of values and all acts that the system form should be based on the considered values. The reason being is that the values have a special place in Islam. This refers to the Islamic ethic principles of good *akhlak* in business activity.
3. As a continuous relationship (*ukhwah*) is the key to success in business activity, Islamic banks and customers should be conscious and *Istiqamah* on individual obligation to fulfill it within time. Both should bear in mind that wherever there is a plan to fulfill obligations, there should also be a plan to fulfill it within the agreed time. This is how both of them should be to have a good way of evaluation to determine the rate of achievement by scheduling and re-scheduling the financing to ensure that the time-line of financing is the correct way to achieve the goal.
4. The banks should be fair and just (*'adl*) in making financing decisions, which means there should be no asymmetric information and that customers should know clearly the Islamic financing contracts used. In addition, putting trust in Allah s.w.t. (*tawakkal*) is good when making financing decisions.

5. By thinking about the principles of the Islamic religion, this study raises the awareness of the readers about the importance that Islam places on evaluation and this study found unique credit risk management methods derived therefrom. Bank practitioners and customers should believe in resurrection and good things, and avoiding the bad things, and, hence, extra elements instead of the five Cs and CAMPARI elements can be applied in the evaluation.

7.6 Suggestions for Future Research

Credit risk and credit risk management of customers defaults have been examined by various studies, such as Vodová (2003), Nor Hayati Ahmad & Mohamed Ariff (2007), Smith and Fischbacher (2009), Imbierowicz and Rauch (2014), Gavalas and Syriopoulos (2014) and other researchers. However, there are still some areas of interest for future research that may perhaps be considered. For example, future research will look at part of the equity-based system in financing (*Mudharabah* and *Musharakah*) in terms of how the Islamic banking approach plays an important role when it comes to financing activities with different types of exposure towards risk. In reality, is the debt-based approach still applied in Islamic banks?

Therefore, for future works on PhD research, the researcher will apply mixed-methods research (qualitative and quantitative), by conducting interviews and collecting the questionnaires from Islamic bank practitioners to identify what reality is reality towards an equity-based system and how well this system is applied, as well as to determine their point of view concerning different types of risk exposure towards an equity-based system. Hence, the assumptions will clearly open the eyes of

practitioners to an extent and lay them more work for better achievement to be accomplished.

7.7 Limitations

The study believes that the consequences and outcomes of this study would have been more elaborate, or more dissimilar, if the study had more interviewees since the business financing officers and *Shariah* advisers who were interviewed were few in number, and the banks and *Shariah* committees were from a specific geographical area.

Honestly, it was in the beginning of all very stressful to ought to the ones which the study interviewed and contacts with respondents yielded no results. Thus, the results and recommendations should not be considered as expert or professional advice but as a mere academic exercise to take along forward what have the study found out in the progression of this work and what have the study contemplate which based on the exploration, analysis and previous theory read that banks practitioners be duty-bound to do in order to improve their results.

7.8 Chapter Summary

This last chapter further discussed the conclusions and recommendations after the work in this research was completed. Section 7.2 explained the supplementary conclusions. Section 7.3 discussed some of the recommendations pertaining to the banking industry as well as the Islamic banking approach to sustain better. Section 7.4 discussed the practical implications. Section 7.5 discussed some of the good

suggestions for future research, and, lastly, in section 7.6, the study discussed the limitations of the study.

