

Realising the Value-based Intermediation Vision: Five Years After Introduction

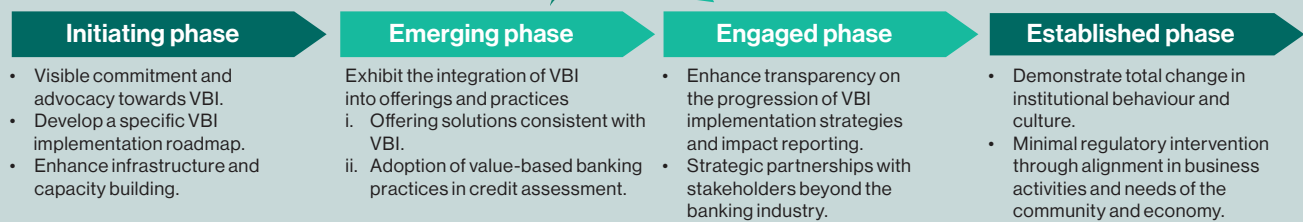
The Value-based Intermediation (VBI) strategy was initiated by Bank Negara Malaysia (BNM) in 2017.¹ It aims to strengthen the role and effectiveness of Islamic financial institutions in delivering the intended outcomes of Shariah, which is premised on balancing wealth creation and wealth circulation as well as promoting social justice, among others. This is achieved through practices, conduct and solutions that generate positive impact on the economy, community and environment, while maintaining returns for the shareholders of the Islamic financial institutions. VBI is different from Corporate Social Responsibility (CSR) programmes as CSR is carried out separately from business operations. VBI is a collaborative effort with the Islamic financial industry, driven by the VBI Community of Practitioners (CoP).²

Progress and Impact to Date

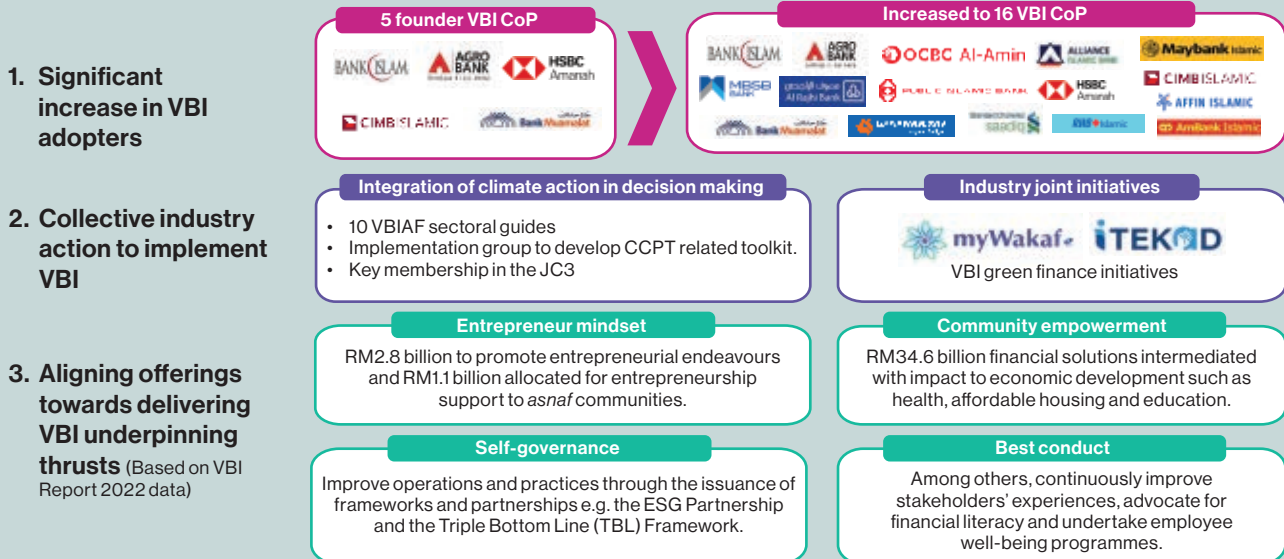
The integration of VBI into business strategies of Islamic banks has contributed positively to individuals, households and businesses, including micro-enterprises. Islamic banks intermediated RM433.8 billion in VBI-aligned initiatives between 2017 and 2022.³ The Islamic banking industry remains committed to aligning their activities with the VBI strategic thrusts to further amplify the positive impacts (Diagram 1).⁴

Diagram 1: Evolution and Outcomes of VBI Journey Thus Far

Four phases of VBI implementation



Transition towards 'Engaged' phase is supported by developments in three areas:



Source: Bank Negara Malaysia, Implementation Guide for Value-based Intermediation and AIBIM (2021) Value-based Intermediation Full Report, (2022) Value-based Intermediation Report: Emerging to Engaging

¹ The Strategy Paper on 'Value-based Intermediation: Strengthening the Roles and Impact of Islamic Finance' was issued on 12 March 2018 following consultation with the industry.
² VBI CoP is a collaborative platform initiated by Islamic banks spearheading VBI industry initiatives. The founding members consist of Bank Islam Malaysia Berhad, CIMB Islamic Bank Berhad, Bank Muamalat Malaysia Berhad, HSBC Amanah Malaysia Berhad and Bank Pertanian Malaysia Berhad (Agrobank), and the CoP has grown to 16 members to date.
³ The data collection by VBI CoP initiated earlier in 2017, when the founding members of VBI CoP were established and the concept paper for VBI was at the consultation stage.
⁴ VBI-aligned initiatives refer to deposits and investment accounts, financing, investment and social finance activities.

VBI encourages Islamic banks to offer more innovative products and services that are impact-driven. This is evident in three areas:

- First, greater focus on net zero and green financing to ensure a sustainable path towards a high-value green economy. Based on the latest VBI report released during the Joint Committee on Climate Change (JC3) conference in October 2023, Islamic banks have disbursed a total of more than RM16.5 billion to net zero and green financing in 2022, a growth of over 2.3 times from 2021. The financing was disbursed, among others, to fund green buildings and renewable energy projects. Currently, it stands at 6.5% of total financing by Islamic banks and is expected to grow further given the rise in financing needs in these sectors.
- Second, more avenues have been explored to support financing needs for Small and Medium Enterprises (SMEs) and micro-SMEs (MSMEs). As of 2022, Islamic banks disbursed RM3.4 billion of net zero and green financing as well as RM24.1 billion of financing for socio-economic development⁵ specifically for SMEs and MSMEs.
- Third, mobilisation of philanthropic and social finance funds (*zakat* and *waqf*), via blended finance solutions has been a growing focus. Social finance provides the opportunity to build financial resilience among the *asnaf*⁶ and the poor. From 2017 to 2022, RM411.8 million was intermediated for various alms (*zakat*), donations (*sadaqah*) and charity programmes including iTEKAD and myWakaf initiatives. iTEKAD, for example, has assisted more than 6,000 low-income microentrepreneurs, comprising *asnaf* and B40 individuals.⁷ Various programmes initiated by Islamic banks to empower microentrepreneurs include financial advisory, access to microfinance, training and business coaching as well as halal certification assistance.

Diagram 2: Examples of Impact-driven Offerings by VBI CoP

Financial solution anchored on creating positive impact

A growing number of Islamic banks are offering various solutions to generate sustainable impacts on the economy, community and environment while delivering financial returns.

An impact investment account invests in renewable energy, green financing, clean transportation, clean water and sanitation as well as other sectors that contribute to creating sustainable cities and communities. In addition, 2.5% of the investment return will be contributed to *zakat*.

A low carbon transition facility provides financial support for both capital expenses and operational funding to enforce sustainable practices for SMEs across various industries.

A financing facility for solar installation is offered to SMEs to facilitate the purchase and installation of solar on business premises.

Source: AIBIM (2022) Value-based Intermediation Report: Emerging to Engaging and Bank Islam Malaysia Berhad website

Progressive Efforts Undertaken by Industry Players

An important demonstration of VBI's collective effort is the issuance of the Value-based Intermediation Financing and Investment Impact Assessment Framework (VBIAF) Sectoral Guides⁸ to facilitate the implementation of an Environmental, Social and Governance (ESG) impact-based risk assessment. So far, three cohorts of sectoral guides have been issued to provide sector-specific guidelines that assess the impact of financing and investment activities on ten sectors.⁹ These sectoral guides are also in line with BNM's Climate Change and Principle-based Taxonomy (CCPT). Effective implementation of VBI, complemented by a better understanding and measurement of climate and environment has the potential to address contemporary issues that the financial system and the world are facing.

⁵ Refers to financing extended to sectors that will improve the impact on social aspects under this category, such as education, public infrastructure, MSMEs, etc.

⁶ A group of people worthy of receiving zakat contribution such as the destitute and poor.

⁷ For more information, please refer feature article on 'iTEKAD: An Ecosystem Approach in Scaling Up Social Finance'.

⁸ VBIAF Sectoral Guides serve as an in-depth impact-based risk management toolkit to guide financial institutions in implementing VBIAF in the sectors.

⁹ First cohort (palm oil, renewable energy and energy efficiency) and second cohort (oil and gas, construction and infrastructure and manufacturing) were issued in 2021 and 2022, respectively. The third cohort (agriculture, mining and quarrying, road transportation and waste management) were released for consultation in May 2023 and is pending finalised issuance in the first half of 2024.

VBI has also expanded its relevance to the takaful industry. The Malaysian Takaful Association (MTA) introduced the Value-based Intermediation for Takaful (VBIT) framework and roadmap in 2021 and 2022, respectively. VBIT carries the aspiration to achieve inclusive protection for the underserved and unserved segments of society. Efforts to improve the quality and value of offerings are already taking place, such as widening affordable coverage to the poor at a lower price and introducing the *sadaqah* feature as part of product design.

As part of its VBIT priorities, the takaful industry also aims to improve its impact measurement practices. For this, MTA is currently developing a Maqasid al-Shariah Scorecard (MSS). MSS will identify key performance indicators and outcomes in line with the intrinsic values of Islamic finance. The scorecard is expected to be piloted with several takaful operators in 2024.

VBI is also consistent with the global movement towards a more sustainable economy. The goals of inclusive economic development, environmental conservation and social advancement are part of Shariah principles. These goals are universal in nature, consistent with the UN Sustainable Development Goals 2030 and aligned with the 'Ekonomi MADANI' framework. New developments such as the introduction of the Maqasid Al-Shariah Guidance by the Securities Commission Malaysia in 2023 and the call among Islamic finance community to adopt the '*Tayyib* (good) concept' further reinforce the importance of increasing adoption of VBI within the financial sector. These developments provide a strong and clear impetus to accelerate its implementation.

Increasing Adoption of VBI Requires Enduring Industry Commitment

While these positive steps have been encouraging, challenges such as a lack of understanding of VBI principles and application among key stakeholders, the need for group-wide strategy alignment and data limitations to accurately measure impact still exist and may continue to impede further progress of VBI. As such, more efforts need to be made by the industry to address these challenges. Among others, this includes assessing the need for longer-term investment in shared infrastructure and technology, such as leveraging on fintech and artificial intelligence to make impact-driven data gathering or analysis easier and more effective. Increase in public disclosures in various reports will demonstrate the industry's leading role in serving the needs of society and the broader economy. Diagram 3 summarises the roles of shareholders in advancing VBI implementation.

BNM is committed to provide an enabling environment to support the growth of VBI. This includes developing a more conducive regulatory environment that will also facilitate the application of diverse Shariah contracts. At the same time, BNM will continue to facilitate the industry's efforts to innovate and develop new value-based business models, solutions and practices.

Diagram 3: Roles of the Stakeholders in Advancing VBI Implementation



Regulatory bodies

- Provide the appropriate regulatory facilitation for value-based finance implementation to better support innovations, such as the novel application of Shariah contracts.
- Facilitate improvements in the quality and usefulness of impact-based disclosures.



Implementation partners

(including professional services and talent entities)

- Enhance collaboration with financial institutions to provide training and financial assistance to vulnerable communities.
- Continuously enhance talent capabilities through upskilling and learning infrastructures.



Financial institutions

- Integrate corporate value intent into Islamic financial institutions' business operations and practices.
- Improve comparability and quality of disclosures including exploring pertinent infrastructure and capacity building to improve impact-based reporting.
- Continue innovation efforts in developing new value-based business models, solutions and practices.



Institutional investors and shareholders

- Transition towards impact investing that creates positive environmental and social benefits.
- Explore VBI-aligned investment opportunities offered by financial institutions.



Government and state agencies

- Leverage VBI-aligned products and services in realising national agenda and priorities to improve Malaysia's long-term economic prospects.

Source: Bank Negara Malaysia