

Box Article

Social finance as an enabler of social development in Malaysia

Social finance has the potential to narrow remaining inclusion gaps

Social finance is envisioned to play a greater role in Malaysia's financial landscape, with Islamic finance leading the way – complementing public sector finance and commercially-driven financial solutions to promote greater social resilience. Importantly, social finance has three unique qualities that can advance financial inclusion in a way that is transformative and addresses constraints typically associated with traditional finance.

First, social finance instruments can be designed for greater flexibility, thereby increasing the level of risk absorbency (in contrast with traditional debt-based finance). These range from allowing more flexible repayment terms that accommodate irregular income streams and not imposing repayment obligations on beneficiaries (e.g. financing funded by *zakat* funds). For donation-sourced financing, there is usually minimal or no financing cost attached (e.g. beneficiaries are only required to repay the benevolent financing provided). Social finance can thus improve access to funding for segments that face challenges in accessing commercially-driven finance. The use of more flexible, innovative financial structures can also avoid deepening existing financial vulnerabilities (e.g. indebtedness) faced by such individuals or businesses.

Second, implementation partners generally supplement funding with structured programmes that upskill beneficiaries in financial management, business acumen, and other key areas (e.g. digital capabilities). These enhance their financial literacy, foster entrepreneurial behaviour, and empower the beneficiaries to generate a more sustainable income and improve their quality of life.

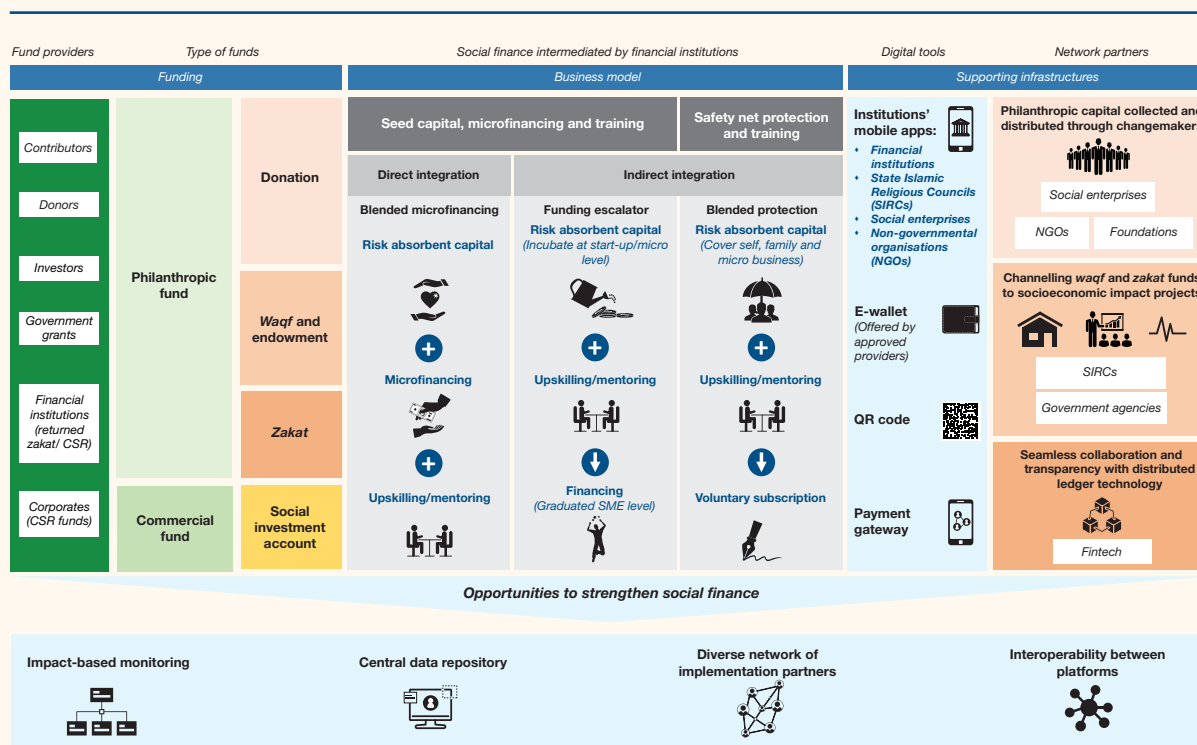
Third, social finance initiatives are often supported by impact monitoring and “pay-it-forward” mechanisms. Effective implementation of these mechanisms can build trust among the fund providers and target groups, as well as foster a virtuous cycle that encourages past beneficiaries to be part of efforts to support future ones – potentially creating a valuable network of support, thereby strengthening the upsides of social finance solutions.

The landscape of social finance solutions is becoming more vibrant and diverse

Over the past decade, several financial institutions have been exploring different ways to deliver social finance, refining their offerings over time (Diagram 1). While most ventures have been pursued as part of CSR initiatives, some players are developing social finance as a viable business proposition. Encouragingly, VBI-aligned financial institutions have begun to adopt a blended finance approach in social finance offerings, thus improving the target segments' access to capital and protection.

There is also greater collaboration among the diverse stakeholders and implementation partners. These partnerships can optimise the strengths of various actors in the ecosystem (e.g. collection/distribution agents, platform providers, payment facilitators, fund managers, and underwriters), thereby improving efficiency and outreach, augmented by the increased adoption of digital tools.

Diagram 1:
Common characteristics of social finance offerings in Malaysia



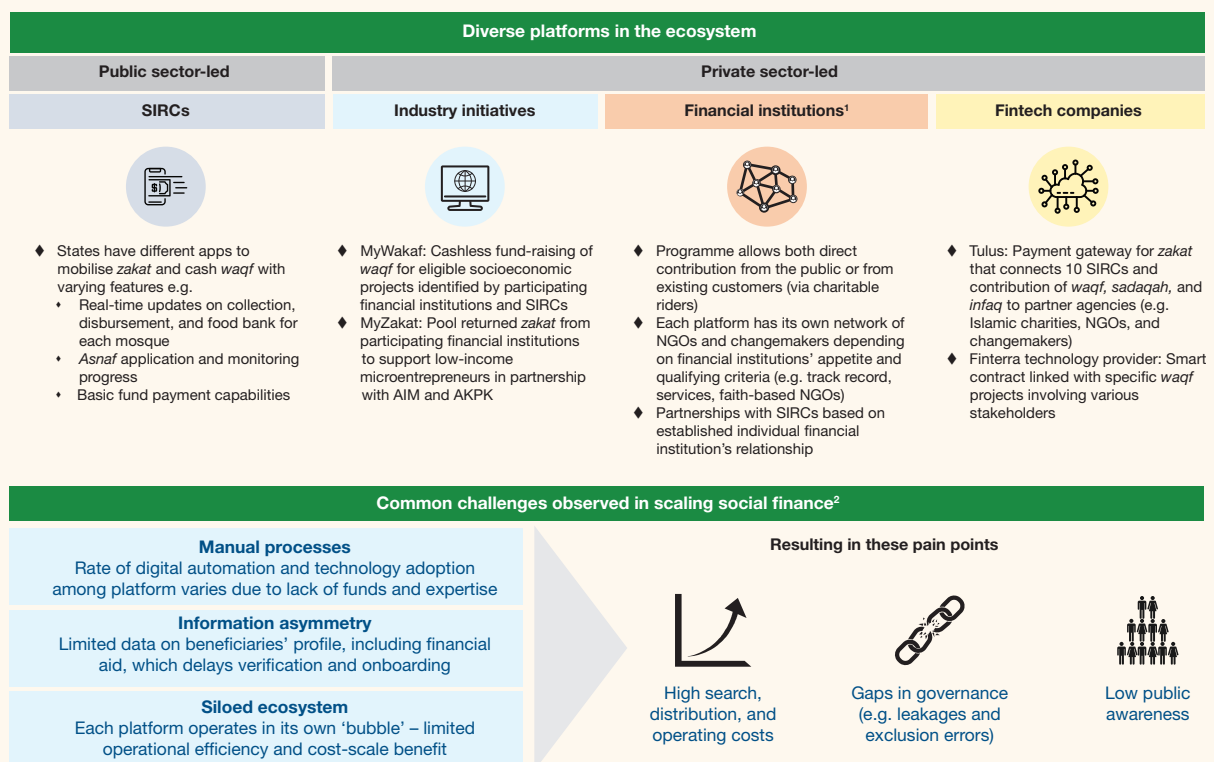
In 2020, iTEKAD was launched – a social finance pilot programme that blends financial and non-financial components. The first phase of the pilot has provided useful insights for participating banks to design more flexible offerings, as well as for diverse implementation partners to support training, business mentorship, and impact monitoring. Since then, we have seen the launch of more social finance solutions that are consistent with iTEKAD components to support pandemic affected micro-SMEs. These offerings combine philanthropic funds (such as grants, donations, and *zakat*¹) with low-cost or benevolent microfinance, supplemented with structured financial and business training. Ultimately, we are working towards nationwide expansion of iTEKAD and similar social finance offerings by various financial institutions. These programmes require close collaboration with diverse range of implementation partners and stakeholders such as government agencies, SIRCs, fintech companies, NGOs, social enterprises, and foundations.

Moving forward, multi-stakeholder efforts are key – including to promote shared infrastructures and to support national developmental priorities

As social finance gains traction, multi-stakeholder coordination and collaboration are critical to lower search and distribution costs, as well as to promote greater public confidence in the disbursement and governance of funds (refer to Diagram 2).

¹ Financial institutions as *zakat* payers may apply to participating SIRC to distribute a portion of the *zakat* paid (returned *zakat*) or partner directly with SIRC to distribute a certain portion to eligible recipients on behalf of the SIRC, subject to predefined criteria.

Diagram 2:
Overview of the diverse social finance platforms available



¹ The examples cited are social finance platforms established by financial institutions under the direct integration model.

² These challenges are not in relation to any specific platform and are based on observations across the social finance ecosystem.

These efforts include developing shared infrastructures – or making better use of existing ones, such as by making them interoperable – to reduce barriers to social finance offerings. Examples of such infrastructures include:

- A shared data repository of target groups for social finance programmes, which can support better risk-informed profiling of beneficiaries and the channelling of funds to unmet groups.
- A network of credible implementation partners – that are vested in social outcomes and have strong relationships with 'at-risk'² communities – can act as support system to build trust and encourage participation in the financial system.
- An integrated dashboard optimising mobile-based interfaces that facilitates real-time funding updates and impact disclosures. This can address key information gaps on the social finance landscape, including on readily available opportunities for willing stakeholders to contribute funds or volunteer other resources.

Another important thrust is to align social finance initiatives to national priorities, thereby amplifying the impact of social finance. These priorities include improving income generation potential for entrepreneurs as well as providing funding support for the provision of cost-effective education, healthcare services and facilities for common non-communicable diseases. Suitable financing and protection solutions can be designed to support these sectors in line with Malaysia's long-term focus on sustainable economic growth and entrepreneurial drive towards a high-income society and shared prosperity for all.

² These target groups, among others, are budding entrepreneurs and community groups with the ability to generate productive income when supported by small financing and protection value.

