



Islamic trade finance: Perfect platform for halal market

Trade finance is a specialised area of finance that deals with short term financing of import and export transactions. Islamic trade finance has benefited from the shifting preference towards Shariah compliant banking and would serve as one of the key growth drivers to help the existing US\$2 trillion Islamic finance industry to double in size.

Despite this positive development, total trade flow using Islamic Trade Finance is still low. In 2016 for example, of the total trade flow of RM1.48 trillion in Malaysia, only 30.3 percent used Islamic Trade Finance.

In trade transactions, there are cases where both importers and exporters are unknown to each other, which may raise concern on the assurance of payment and delivery of the goods to be made on time and with the expected qualities.

This is where trade finance comes into the picture and where banks act as

What is trade finance?

an intermediary to facilitate the trading transaction occurred between both parties, and at the same time providing comfort to both parties as the transactions are handled by a trustworthy bank.

Generally, products offered by Islamic and conventional trade finance are similar, however there are elements in conventional trade transaction that are prohibited in Islam for example when

it involves usury, uncertainty, and gambling. There are also goods that cannot be financed by Islamic banks such as pork, wine and any other prohibited items as listed in Bank Negara Malaysia (BNM) Guidelines of Accepted Bills-i. To the discerning customers, the transaction used in Islamic trade finance is more appealing to them since it needs to observe and comply with tenets and requirements of Shariah contracts.

VALUE PROPOSITION IN ISLAMIC TRADE FINANCE

By choosing an Islamic trade facility, companies can attract investors who are very particular on Shariah-based transactions. There are companies who prefer to choose Islamic trade finance as it promotes a transparent and fair dealing with prohibited elements of usury, gambling, uncertainty, deception and betrayal.

Customers also can benefit from the following prohibitions: early settle-

ment fees, compounding late payment charges (LPC), extension fees and any compounding financing rate or any hidden charges.

In dealing with payment to third parties, customers can choose two methods for their mode of payment, namely Letter of Credit-i (LC-i) or open account basis. LC-i refers to the undertaking given by banks to the beneficiaries as a guarantee of payment if terms and conditions are complied with. It is the most secure instrument for exporters in managing their trade transactions.

On the contrary, customers that have good relationship and trust with the beneficiary may prefer to use open account basis as their mode of payment.

As mentioned above, LC-i is a mode of payment guaranteed by bank to the seller. Nevertheless, if the customer requests for financing, LC-i can be converted into a trust receipt-i (TR-i) which is a financing product against LC-i for the buyer. TR-i is used to enable importers to possess the trading goods without a need to pay until the end of period.

For guarantee-based product, there are Bank guarantee-i (BG-i) which refers to the bank's obligation to pay the beneficiary in the event of customers' failure to pay. Since BG-i is not allowed in some countries, as a solution, Standby Letter of Credit-i (SBLC-i) can be issued. Another guarantee-based product is Shipping Guarantee-i (SG-i) that focuses on bank's guarantee during shipment.

CONCLUSION

To sum, Islamic trade finance offers various type of facilities to assist customers in their trade transactions. In line with the substantial progress in trade transactions, statistics indicate a significant growth within the halal export industry in recent years. Malaysia's Halal Industry Development Corporation for one has stated that the global Halal market in 2016 had reached US \$2.8 trillion in 2016.

As halal industry is moving on the same direction, the incorporation with Islamic trade facilities as their trade platform is highly encouraged. By doing so, customers will have more confidence in halal certified companies as the end-to-end process involving supply, process, manufacture and import/export of the goods are Shariah compliant.

Besides, if halal industry that promotes the same principles as Islamic Trade Finance does not support each other, who else will? 🤖

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