3rd International Conference on Finance Business and Banking
Fakultas Ekonomi dan Bisnis Islam, Universitas Islam Negeri Mataram
Mataram, 27th - 28th November 2023
Available Online at http://proceeding.uinmataram.ac.id

Green Islamic Finance for SMES to Achieve Sustainable Development Goals

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ABSTRACT

Purpose — *We provide a framework for green Islamic finance for impactful small and medium companies (SMEs) to accomplish the Sustainable Development Goals (SDGs) in this study. Green Islamic finance emerges from a discussion of the relevant ideas that underpin charity, private sector initiatives, and public sector facilitation. The agreement of these three parties on the impact criteria is a necessary precondition for financing to occur. As a result, we first created the 4Zeros & SS (zero-waste, zero-emissions, zero-interest, zero-foreclosures, and service to society) green-based impact criterion for SMEs. Following that, we used a financial engineering method to build green products that included the three motivations. If these three incentives are identified and brought together, financial contracts may be incentive compatible and effective.*

Method — *We use (a) Values Creation Shariah Accounting, (b) the pillars of sustainable human development (equality, productivity, empowerment and sustainability) as SDGS and (c) ESG and circular economy concerns as green based Islamic finance.*

Result — *This study design will help to achieve multidimensional human development as envisioned by the Value Crehariah Accounting and the SDGs. Environmental, social, and governance best practices, as well as national development goals, must be integrated into impactful businesses.*

Novelty — *This study answer phenomenon occurs for businesses must be aware of environmental, social, and governance challenges, as well as other global activities, if we are to achieve sustainability.*

Keywords: *Green Islamic Finance, SMEs, SDGs*

INTRODUCTION

Climate change has implications which interferes with social welfare and development economic and financial stability of current and future generations front (Evans et al., 2017). Concerns about the future impact of all these worrying changes and needs to overcome current problems has prompted various global initiative to meet the threat of climate change and environmental crises such as the Sustainable Development Goals (SDGs) United Nations (UN) and Agreements Paris(Cordova & Celone, 2019). We assume it is general information that small and medium-sized firms (SMEs) are a viable and long-term means of achieving multidimensional development (MD). The MD concept is included in Maqasid Al-Shariah (local ambitions in Muslim community), Qatar National Vision 2030 (as an example of national priorities), and the Sustainable Development Goals (SDGs). However, there are worries about funding costs and collateral requirements as hurdles to SMEs getting loans (Kota et al., 2021). This study proposes to remove barriers to funding for SMEs using a hybrid Islamic structure. The concept of green Islamic finance is not new. However, its significance has recently grown in the context of the SDGs. The basic concept is straightforward.

In spite of ecological fragmentation, there is no unified definition for green Islamic finance(Soundarrajan & Vivek, 2016). While some definitions explicitly emphasize on resource mobilization for SDGs in emerging economies (Williams & Parker, 2010) (WEF & OECD, 2015; Green Finance Task Force, 2017), others are reflective of the blended institution's purpose. Green Islamic finance was defined by the OECD as "the strategic use of development finance for the mobilization of additional finance towards sustainable development in developing countries" (OECD, 2018b, p. 13).

Green Islamic finance refers to the use of grant and, in most cases, concessionary development funding to entice commercial finance into unappealing development initiatives (Khan & Badjie, 2022). Samans and Solheim's notion of green Islamic financing supports this. Green Islamic finance, according to (Kayani, 2023) is "the strategic use of development finance and philanthropic funds to mobilize private capital flows to emerging and frontier markets." These definitions make it clear that the common and overriding goal of blending is to use scarce development funds in a way that encourages private sector participation in development impact projects(Chien et al., 2021).

Another advantage of green Islamic financing is the ability to overcome market barriers by altering the risk-return relationship in order to catalyze capital flows to projects with high development effect that would otherwise be unachievable(Kumar et al., 2022). Shifting the risk-return profile, sharing local knowledge, developing local capacity, and shaping policy and regulatory reforms are some of the characteristics of green Islamic finance that attract private players to sectors with explicit social impact, financial viability, and sustainability but are hesitant to enter due to market barriers (Samans and Solheim, 2015). Overcoming these constraints is critical for closing development gaps, particularly in SMEs sectors in desperate need of resources.

The study expects that this framework of green Islamic finance will be useful in providing capital for SMEs. Proposed green Islamic finance Murabahah line of credit model in which the charitable entity offers a social subsidy to cover the markup while the SMEs pay only the cost, resulting in a win-win situation for all parties. While financial institutions use green contracts to boost profitability, green Islamic finance entity reduces the amount of grant by only delivering a portion grant to support the markup. SMEs can get interest-free loans to boost their productivity.

METHOD

This research, driven by the literature, used a concise case study approach to examine use (a) Value Creation Shariah Accounting , (b) the pillars of sustainable human development (equality, productivity, empowerment and sustainability) as SDGS and (c) ESG and circular economy concerns as green based Islamic finance. The case study approach was chosen to discuss the research topic because of its suitability. A general advantage of the case study research methodology is that it provides the study unit with a rich contextual insight at a level of qualitative detail that can not be reproduced.

This analytical approach is useful for addressing "why" and "why" of questions (Saldaña, 2013). The study examined how sustainability-oriented technology is applied inside Interface in this instance?"The co-innovation process was the unit of study for this research; a global interface mechanism designed to facilitate and systematize development initiatives within the organization for the purpose of this study. In this study, researchers obtained main data by making direct observations to the research object, interviewing management and stakeholders, and interacting directly with the management of the research object. Observations were made directly at the location of the object of research with the aim of getting a picture of the reality of the actions taken by each individual and reinforced by interviewing the object. This observation lasted for a relatively long period of three (3) months, starting at the time the researcher first observed general office conditions. Based on the scheme of green based Islamic finance development is carried out with six stages: (1) Identification of problems; (2) Formulation of development models; (3) Preparation of models and development of syntax prototypes, model scenarios; (4) Trials of syntax prototypes and model scenarios; (5) Evaluate the feasibility of the prototype syntax; (6) Refinement and communication of results. The green Islamic finance model design is carried out by an iteration process between researchers, as well as stakeholders.

RESULT AND DISCUSSION

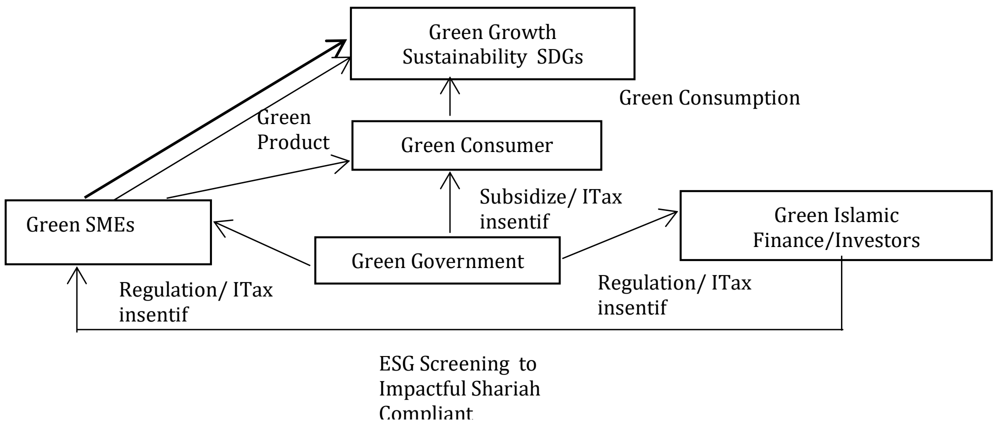
Result

The Rationale of Green Islamic Finance

The rationale is to create a win–win for all green Islamic finance e parties and to mobilize more com- mercial capital through financially viable projects. The outcome of the green Islamic finance transaction is a benevolent loan (qard) to the SMEs, Murabahah for a financial institution and partial grant for the blended entity. The win–win for the three entity is Financial Institutions: expanding into untapped and scalable market segments which were impossible due to high perceived risk and market barriers. Blending Murabahah adjust the risk-return profile, the lower operating cost compared to sharing contracts, guaranteed a fixed stream of cash flow through Murabahah contract[5] and most impor- tantly, portfolio diversification and profitability for the commercial investor development funds.

Small Medium Enterprises: Murabahah is beneficial to SMEs because it smoothens access to finance by overcoming key bottlenecks such as cost of funds, infor- mation symmetry,[6] and high operating cost (Asmanto et al., 2016) . The provision of social subsidy does not only eliminate the cost of funding but also incentivise commercial investors into SMEs financing. Philanthropic entity: also save funds by just financing the markup component instead of providing full grant which could have to consume more resources. Murabahah blended unlike another financing mechanism, minimizes the utilization of limited.

Figure: Relationship between Green Growth Sustainability SDGs and Green Islamic Finance



Source: Modified Soundadarrajan 2016

The explanation in figure 4 is as follows:

Green SMEs : The emphasis has switched to implementing appropriate (alternative technologies) industrial methods in order to maximize energy conservation (Verdolini et al., 2018). Reduce (waste), reuse, and recycle are now emerging as focal points for a variety of activities.

Green Government: Governments should encourage and regulate green industrial markets in order to spread green products and increase green consumption(Sadiq et al., 2022).

Green Consumer: Ethical consumerism, increasing affluence, digital connectivity, growing population, increasing religious affinity.

Green Islamic Finance: Green financing is critical in green growth since it provides enterprises.If green finance is inadequate, the green industry will not be adequately activated, and green products will be phased out of the market, leaving customers unable to acquire green items.Product green financing: financing for energy efficiency (Kayani, 2023),

Discussion

As a result, traditional financial institutions can also be accessed through this way, broadening finance alternatives for SMEs. Green Muarabahah is also replicated in various exchange contracts. The entity can pay the rent and markup element in Ijarah, Salam, and Istisna contracts, respectively. Except for Ijarah concluding with ownership, in which SMEs will contribute toward the purchase (Chebab et al., 2021), SMEs can use the asset for free. Musharakah, Muz'arah, and other sharing contracts Islamic Social Funds (ISFs) can provide Kafala for Mudarabah money in socially responsible and influential SMEs (Chien et al., 2021).

Instrument & Structure Green Finance	Instrument Green Finance	Market Segment	Additional Information
Grants	*Waqf, Sadaqah, Zakah* penalty fees	Preparing Ready for Leading	Instead of depending on constrained funding for development, the faith-based society is tapped to equip the economically active of society through skills training and capital to establish a business.
Repayable Grants	*Qard*	Get Ready Pioneering Facilitating	It is used to help new businesses get started, existing small enterprises, and even medium-sized organizations. The loan can be used to fund operating capital, the purchase of a fixed asset, and the expansion of the business.
Guarantees	*Kafala* (third party quarantee)	Pioneering, Facilitating Anchoring	For many years, the use of guarantees dominated the green finance sector. The same may be said for Kafala. However, the amount guaranteed is a source of contention.
Debt (conces-sional loans)	*Murabahah line* of credit, Sukuk, Salam, Istina	Preparing Pioneering Facilitating Anchoring	It should be mentioned that for Islamic Green Funds, the interest payment is replaced with a make-up/return that is lower than the market rate. This is appropriate to help new businesses get started and existing businesses grow.
Debt (market rate)	*Murabahah* line of credit, *Sukuk, Salam, Istina*	Anchoring Transitioning	The make-up/returns are in line with current market rates and conditions. This form of loan is typically appropriate for a mature company.
Equity (first loss absorber/ risk capital)	Unrestricted *Mudarabah, Musharakah, Muzarah*	Preparing Pioneering	This is based on profit and loss sharing in Islamic finance. As a result, the varied contracts can be based on the investors' preferences. Although Mudarabah capital is not guaranteed, Mudrib can provide hibah to lessen misplaced commercial risk..
Market-based equity	*Musharakah* (diminishing), *Mudarabah*	Anchoring Transitioning	Similarly, equity can be supplied at market rates based on the company's life cycle. For example, an established company that has already crowd-in commercial can be funded at market rates comparable to private investors.
Technical Assistance	*Waqf, Sadaqah, Zakat*	All stages of the life cycle	

Explanation of the Green Murabahah line of credit

1. The intermediary signs a mater Murabahah contract with a multilateral bank, for example, at a rate of 6.5%.
2. In addition, the intermediary bank engages into another Murabahah with SMEs that collect the invoice from the Supplier.
3. Banks purchase from suppliers, and SMEs on Wakala accept delivery on their behalf. The makeup is then charged by the bank based on the Libor and the anticipated profit, which is typically 17-20%.
4. The Entity pays the mark-up (17-20%) and the SMEs pay the cost. 1b) toTo be cost-effective and efficient in fund management, the Entity may negotiate directly with multilateral banks to pay a composition of 6.5% rather than 20%.

Green finance is the green growth infrastructure (Asmanto et al., 2016). Finally, green growth is an orchestra that includes a SDGs development SMEs, a financial company, the government, and the consumer. The elements should be harmonized together in order to avoid cacophony. There are several things that need to be included to harmonize all these roles, consits are: (1) Leverage: the strategic use of development funding and charity to attract greater private investment into development-impacting projects (Abduh & Azmi Omar, 2012). This increases the limited capacity for development finance.(2) Impact: By pooling development money, we may achieve long-term social, environmental, and economic benefits that would not be feasible otherwise (Pepinsky, 2013).(3) Profitability refers to ensuring attractive, risk-adjusted returns for private actors in order to stimulate their and long-term wealth creation (Abduh & Azmi Omar, 2012).

CONCLUSION

The study proposed a concept and set of criteria for influential green Islamic finance. If we are to achieve sustainability, SMEs must be aware of environmental, social, and governance challenges, as well as other global activities. Evidence from the literature suggests that incorporating ESG principles into enterprises increases profitability, mitigates environmental risk, decreases costs, and ensures sustainability. Furthermore, ESGs integration has global prospects to tap into diverse funding sources and attract investors who want to do well while doing good, as well as donors who are primarily influenced by social and environmental considerations.However, one of the major challenges is the funding these types of SMEs, due to the incompatibility of their business model with current banking culture and functions. Hencethe funding costs are exorbitant for them to bear. The governments' resources are limited and under pressure, and no public subsidy could be sustainable.

The concept of green finance is used to create an institutional framework for social subsidies in this article. The paper reviewed conventional finance and expanded on its faults to introduce the concept of Islamic green money, which might potentially use Islamic social institutions of compassion such as Zakah, Sadaqah, Waqf, and so on. Integration of Islamic principles to encourage private sector participation and economic activity in society in order to enhance wealth generation and resource mobilization.

The study expects that this framework of green Islamic finance could be essential in providing capital for the SMEs. The proposed Green Murabahah and Murabahah line of credit model, in which the charitable entity offers a social subsidy to pay the markup while the SMEs covers the cost, is a win-win situation for all parties.

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