

Journal of Management & Muamalah

Jurnal Pengurusan & Muamalah

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Journal of Management & Muamalah

Jurnal Pengurusan & Muamalah

NORZALINA BINTI ZAINUDIN
Lecturer

Faculty of Business Administration

Universiti Kebangsaan Malaysia

43000 Kajang, Selangor Darul Ehsan

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Jurnal Pengurusan & Muamalah 2009 merupakan jurnal berwasit terbitan Fakulti Pengurusan & Muamalah, Kolej Universiti Islam Antarabangsa Selangor (KUIS). Adalah menjadi hasrat jurnal ini untuk menjadi suatu wadah bagi perkembangan ilmu pengetahuan dan penyelidikan khususnya dalam bidang pengurusan dan perniagaan. Artikel di dalam jurnal ini meliputi pelbagai disiplin dalam bidang pengurusan dan perniagaan seperti pemasaran, pengurusan, kewangan, perakaunan, perbankan, ekonomi, pembangunan sumber manusia dan muamalah (transaksi perniagaan Islam) dan daripada disiplin-disiplin ilmu yang lain yang berkait rapat dengan perniagaan dan pengurusan konvensional mahupun Islam sama ada dalam Bahasa Melayu atau pun Inggeris.

The Journal of Management & Muamalah 2009 is a refereed journal which is the second publication of the Faculty of Management & Muamalah, Selangor International Islamic University College. This journal is devoted to advancing scholarly research, knowledge and innovations in all areas of business. Contributions of articles are sought from all functional areas of business such as marketing, management, finance, accounting, economics, human resource development and muamalah (Islamic commercial transaction) and from other disciplines of conventional and Islamic business and management either in Malay or English.

Alamat Surat-Menyurat:

Correspondence Address:

Chief Editor

Journal of Management & Muamalah

Faculty of Management & Muamalah

Selangor International Islamic University College (SIUC)

Bandar Seri Putra

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Malaysia.

E-mail Address: mmj200910@yahoo.com

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Views expressed in this journal are not necessarily reflect views of the editor or publisher. Authors are fully responsible towards their articles.

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Sidang Editor merakamkan ucapan jutaan terima kasih kepada semua yang terlibat dalam menjayakan penerbitan jurnal ini.

Special thanks to all involved in the publication of this journal.

Para penulis

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Selangor.

BUSINESS STRATEGY AND PERFORMANCE OF MALAYSIAN EXPORTING SMES

Mohd Khairuddin Hashim & Sa'ari Ahmad*

Abstract

The linkage between business strategy and performance of exporting small and medium-sized enterprises (SMEs) has been emphasized in the literature. In the Malaysian context, however, the review of the small business literature reveals the relationship between business strategy and performance of exporting SMEs has not received much research attention. This study initiated an attempt to investigate this issue by examining the relationships between six business strategies and the performance of 73 exporting SMEs in Malaysia. On the basis of the analyses of the data gathered from the 73 exporting SMEs, the findings of the study indicate significant positive relationship between business strategy and the performance of the exporting SMEs.

Keywords: *Business Strategy, SME.*

Introduction.

Throughout the world, as economic globalisation intensified, business firms are increasingly been forced to expand their business operations by seeking opportunities in the international marketplace. As a matter of fact, survival and success in the global business system require large firms, as well as small and medium-sized enterprises (SMEs) to adopt international perspectives (Namiki, 1988; Litvak, 1990; and Wright and Ricks, 1994; Dana and Etemad, 1995; Acs, Morck and Yeung, 1997; Karagozoglu and Lindell, 1998; and Crick and Barr, 2007).

Exporting represents one of the internationalization options for firms to expand their business activities globally. Terpstra and Sarathy (1994) indicated that exporting can provide individual firms a competitive advantage by improving their financial position, increasing their capacity utilisation, and raising their technological standards. Furthermore, according to Wheelen and Hunger (2002), exporting is becoming increasingly popular for businesses because of the Internet, fax machines, 800 numbers, and overnight air express services, which reduce the once formidable costs of going international.

Although exporting is increasingly seen as an internationalization option for growth and profitability among SMEs, findings of past studies on export entry decisions of small businesses showed lack of agreement among researchers concerning the factors that can help small firms to penetrate foreign markets (Bilkey, 1978; Bilkey and Tesar,

* Lecturers at College of Business, Universiti Utara Malaysia

1977; Reid, 1981 and 1984; Kaynak *et. al*, 1987; Axinn, 1988; Malekzadeh and Navajamdi, 1985; Ortiz-Buoafina, 1990; Ogbuchi and Longfellow, 1994; Julien *et. al*, 1997 and Zou and Stan, 1998; and Burpitt and Rondinelli, 2000).

Apart from the disagreement concerning the factors that contribute to the process of internationalization among SMEs, the small business literature further indicates that limited research attention have been given to examine the linkage between small firm business strategies and internationalization (Namiki, 1988; Baird, Lyles and Orris, 1994; and Bell, Crick and Young, 2004). Although competition in international markets has become an important issue for exporting SMEs, little research has been conducted to examine the relationship between business strategy and the performance of SMEs involved in exporting. The lack of information and knowledge concerning the important relationship between business strategy and performance of exporting SMEs, specifically in the Malaysian context suggests the need for more research in this area. This study was conducted to address this issue. The objective of the study was to examine the relationship between business strategy and performance of exporting SMEs in Malaysia.

The Literature.

The literature highlights the importance of business strategy to organizations operating in a competitive business environment. Business firms need to develop effective business strategies to help them compete effectively. Business strategy has been characterized as the way in which a firm decides to compete, pursue, achieve and maintain its competitive advantage in an industry (Walker and Ruekert, 1987; Rue and Holland, 1989; and Varadarajan and Clark, 1994).

Firms can gain their competitive advantage by producing value to their customers. More specifically, Porter (1980) indicated that a firm can develop its competitive advantage by performing the chain of strategically important activities (such as production, marketing, sales, service, human resource management, technology development, procurement activities) cheaply or better than its competitors. According to Porter, business strategies that focused on these activities are called generic strategies. The three generic business strategies include; low cost, differentiation, and focus or niche. In a low cost strategy, the firm strives to lower its costs, increase profit and sales by adopting economics of scales, scope and technology. In a differentiation strategy, the firm emphasizes on making its products appear unique and different.

Finally, in and marketing eff advantage. Namiki small-sized expor in the United Sta differentiation st strategy, and prod strategy is focused advertising and in strategy stressed o Innovation differe technologically su strategy stressed o customers. More i a differentiation f performance than

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Finally, in a niche or focus strategy, the firm stresses on product development and marketing efforts in a particular market segment that it has a cost or differentiation advantage. Namiki (1988) identified four patterns of competitive strategy adopted by small-sized exporting firms in a study of 393 small computer hardware manufacturers in the United States of America. Among the competitive strategy include; marketing differentiation strategy, differentiation focused strategy, innovation differentiation strategy, and product-oriented strategy. According to the study, marketing differentiation strategy is focused on competitive pricing, brand development, control over distribution, advertising and innovation in terms of marketing techniques. Differentiation focused strategy stressed on the ability to offer specialized products to specific customer groups. Innovation differentiation strategy was developed on the basis the firm's ability to offer technologically superiority of products and new product development. Product-oriented strategy stressed on the quality of the products and high levels of services provided to customers. More importantly, the findings of the study showed that the firms that adopted a differentiation focused or innovative differentiation strategy achieved higher export performance than those firms that used a marketing differentiation strategy.

The studies by De Noble, Castaldi, and Moliver (1989) and Cavusgil and Knight (1997) further indicated small firms faced competition in exporting markets developed business strategies based on a variety of factors. Among these factors include; business opportunities and market research, promotion of the business and products, selection of and collaboration with agents and distributors, development of local contacts and provision of services after sales, pricing, sales force management, credit risk analysis, knowledge of business practices, awareness of the competition, and product research, development, and adaptation.

In a study that attempted to examine the international strategies of small firms, the relationship between international strategy and firm performance, and the attributes associated with the adoption of an international strategy, Baird, Lyles, and Orris (1994) found three types of international strategies being adopted by small firms. The findings of the study indicated that among the three international strategies used by the small firms included; international strategy (which emphasized on exporting, foreign equity investment, and foreign alliances to develop new products and enter new markets), domestic alliances strategy (which focus on domestic alliance formation, using domestic alliances to enter new markets, develop new products), and domestic solo strategy (the firm entering new markets and developing new products on its own). Further, the results

of the study showed that international strategy was positively related to return on sales but negatively related to growth in sales.

Lages and Montgomery (2004), in a more recent study, found product strategy, promotion strategy, price strategy, and distribution strategy as the four common strategies adopted by exporting firms. In product strategy, the firm stressed on differentiating the products offered in the domestic market and the products sold in the export markets in terms of brand name, design, labeling, variety of main exporting product line, and quality. The promotion strategy focused on adjusting the domestic promotion program towards the export market in areas such as advertising idea and theme, media channels for advertising, promotion objectives, budget for promotion, public relations emphasis, and direct marketing and mailing. In pricing strategy, the firm used concession of credit, price discount policy, and margins to offer products at different prices across national boundaries. Distribution strategy involved selecting the distribution system, transportation, budget for distribution, and distribution network to the export market.

Research Methodology.

Sampling Frame and Procedure.

The sample of the study was confined to selected small and medium-sized enterprises (SMEs) operating in the Malaysian manufacturing sector. In this study, a small and medium-sized enterprise is defined as a manufacturing firm with an annual turnover of less than RM25 million and as one which employs not more than 300 full time employees. On the basis of this definition, 400 firms were identified and selected from the listing obtained from the Malaysian External Trade Development Corporation (MATRADE). The data for this study was gathered through the mail survey. Structured questionnaires were sent to the senior managers of the 400 firms selected. Out of the total number of 400 questionnaires mailed, 73 usable questionnaires were returned, yielding a response rate of 18.3 percent.

Questionnaire.

The structured questionnaire-adopted in this study consisted of three sections. The first section of the questionnaire which consisted of nine items was used to obtain the general information concerning the background of the respondents. The items in section two of the questionnaire focused on getting the information on the characteristics of the

firms such as industry in which they operated, years involved in exporting, and the number of employees were designed to

These items were used in the study, to gauge the business strategies adopted by the firms, to rate the importance of various factors (1) Extremely Important

The Results.

Profile of the Respondents.

Of the 73 respondents, 13 were owners/managers, 50 were Indians. Fifty-two were married, and 21 had between one and three children. The respondents obtained 25 respondents

Characteristics of the Firms.

The profile of the firms includes; legal status, age, and net profit margin. The majority of the firms' involvement in exporting was more than four years. The number of firms to more than ten ranged from less than

firms such as legal form of the firm, number of full time employees, age of firm, the industry in which the firm operates, total sales of the firm, percentage of export sales from total sales, net profit before tax of the firm, countries of export, and number of years involved in exporting activities. The items in section three of the questionnaire were designed to capture the business strategy adopted by the firms.

These items contained brief descriptions of each the six business strategies. In the study, to gather the information on the six common business strategies emphasized by the firms, the respondents were requested to rate the importance of each of the six business strategies with respect to their firms' export success. The respondents were asked to rate the importance of each business strategy based on a five point scale ranging from (1) Extremely Important to (5) Not Important At All.

The Results.

Profile of the Respondents.

Of the 73 respondents, 46 were managers, 14 were owners and managers, and 13 were owners and CEOs of their firms. Forty were Malays, 28 Chinese, and five were Indians. Fifty six of the respondents were males and 17 females. Sixty respondents were married, eleven never married, one remarried, and one widowed. The respondents had between one to more than 20 years of work experience. In terms of education, 22 respondents obtained bachelor degrees, 14 master's degrees, 11 had school certificates, 25 respondents had diplomas, and one respondent earned a PhD degree.

Characteristics of the Sample Firms.

The profile of the sample firms is presented in Table 1. The information in Table 1 includes; legal forms of the firms, number of employees, age of the firms, total sales, and net profit before tax for the year 2006. Following Table 1, Table 2 summarizes the firms' involvement in exporting. As shown in Table 2, 41 firms had been exporting for more than four years. Thirty-eight firms exported to less than three countries and 35 firms to more than four countries. The percentage of export sales to the firms' total sales ranged from less than 10% to more than 30% of their total sales.

Table 1: Characteristics of the Sample Firm

Firm Characteristics (n=73)	Frequency	Percentage (%)
Legal Form:		
Sole Proprietorship	19	26.0
Partnership	11	15.1
Private Limited	43	58.9
Number of Employees:		
1-100	41	56.2
101-200	4	5.5
201-300	28	38.3
Age of Company:		
<5yrs	7	9.6
6-10 years	0	0
11-15 years	27	37.0
16-20 years	13	17.8
> 20 years	26	35.6
Total Sales in 2006 (Ringgit Malaysia):		
<RM1 million	18	24.7
RM1,000,001-RM5 million	12	16.4
RM5,000,001-RM10 million	9	12.3
RM10,000,001-RM15 million	3	4.1
RM15,000,001-RM20 million	3	4.1
RM20,000,001-RM25 million	28	38.3
Net Profit in 2006 (before tax):		
<RM100,000	15	20.5
RM100,001-RM200,000	7	9.5
RM200,001-00,000	8	11.0
RM300,001-RM400,000	4	5.5
RM400,001-RM500,000	3	4.1
RM500,001-RM600,000	2	2.7
>RM600,000	34	46.6

Business Strategies

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Business Strategies Emphasized by the Firm.

Table 3 presents the mean scores and standard deviation of the business strategies as recorded from the respondents. The mean scores ranged from 1.80 to 2.77, suggesting that in general, majority of the firms viewed the six business strategies to be important to their firms' export success.

Relationship between Business Strategy and Performance.

Table 4 presents the results of the correlations between the six business strategies and the performance of the exporting SMEs as measured in terms of sales, net profit, and number of employees. The results in Table 4 indicate significant positive relationships between the six business strategies (niche, product differentiation, marketing differentiation, service differentiation, innovation and low cost) and the performance (sales, net profit, and number of employees) of the exporting SMEs. However, the correlations between niche, product differentiation, innovation and number of employees were found to be not significant.

Business Strategy	Mean Score	Standard Deviation
Niche	2.15	0.85
Product Differentiation	2.25	0.95
Marketing Differentiation	2.35	1.05
Service Differentiation	2.45	1.15
Innovation	2.55	1.25
Low Cost	2.65	1.35

Table 2: Firms' Involvement in Exporting

Firm Characteristics (n=73)	Frequency	Percentage (%)
Number of years involved in exporting:		
<3 years	32	43.8
4-6 years	8	11.1
7-9 years	15	20.5
10-12 years	10	13.7
>13 years	8	10.9
Number of countries exported to:		
<3 countries	38	52.2
4 to 6 countries	12	16.4
7 to 9 countries	12	16.4
10 to 12 countries	2	2.7
>13 countries	9	12.3
Percentage of export sales to total sales:		
<10%	28	38.4
11% to 15%	11	15.1
16% to 20%	8	11.0
21% to 2%	3	4.1
21% to 2%	4	5.5
>30%	19	26.0

Table 3: Business Strategies As Emphasized by the Firm

	Mean	SD
Niche Strategy:		
Focus on specialty products	2.22	1.06
Focus on a specific range of products	2.25	0.85
Focus on a specific foreign market	2.17	0.87
Focus on specific foreign customers	2.33	0.93
Focus on new product	2.42	1.06
Product Differentiation Strategy:		
Product quality	1.80	1.04
Packaging	2.14	1.09
Design and style	2.13	1.08

Product uniqueness
Maximize perceived value
Marketing Differentiation
Adopt competitive pricing
Create new distribution channels
Increase advertising
Increase advertising
Brandbuilding
Update product line
Use market research
Use personal selling
Develop new markets
Service Differentiation
Quick product development
Prompt response to customer needs
Offer extensive customer service
Personal contacts
Provide quality service
Innovation Strategy
Technological superiority
Focus on new innovations
Use advanced technology
Improve existing products
Improve product quality
Low Cost:
Purchase materials in bulk
Mass produce products
Limited range of products
Maximize economies of scale
Sell product at low prices

(1)Extremely Important At All

Product uniqueness	2.07	1.05
Maximize perceived value of product	2.10	0.89
Marketing Differentiation Strategy:		
Adopt competitive pricing	2.10	0.94
Create new distribution channel	2.23	0.97
Increase advertising and promotion	2.33	1.01
Increase advertising and promotion	2.33	1.01
Brandbuilding	2.25	1.17
Update product line	2.41	0.97
Use market research	2.26	0.93
Use personal selling	2.57	0.98
Develop new market for product	2.58	1.06
Service Differentiation Strategy:		
Quick product delivery	2.04	1.04
Prompt response to customers' orders	1.93	1.00
Offer extensive customer service	2.16	0.98
Personal contacts with overseas distributors	2.22	0.94
Provide quality service	1.90	1.03
Innovation Strategy:		
Technological superiority of product	2.13	0.95
Focus on new innovative product	2.17	0.98
Use advanced communication technologies	2.22	1.00
Improve existing product	2.04	0.91
Improve product process	2.16	0.90
Low Cost:		
Purchase materials in large volumes	2.36	1.06
Mass produce products	2.52	1.04
Limited range of products	2.77	0.97
Maximize economies of scale	2.20	1.01
Sell product at budget price	2.55	1.08

(1)Extremely Important; (2) Important; (3) Fairly Important; (4) Not Important; (5) Not Important At All.

Table 4: Correlations between Business Strategy and Performance

Business Strategy (N=73):	Sales	Net Profit	No. of Employees
Niche	0.415**	0.443**	0.209
Product Differentiation	0.366**	0.359**	0.185
Marketing Differentiation	0.361**	0.323**	0.252*
Service Differentiation	0.400**	0.324**	0.245*
Innovation	0.341**	0.260**	0.189
Low Cost	0.295**	0.315**	0.239*

* Correlation is significant at the 0.05 level (2-tailed). ** Correlation is significant at the 0.01 level(2-tailed).

Discussion and Conclusion.

This study attempted to examine the relationship between business strategy and the performance of exporting SMEs. At the general level, the results of the correlation analysis as presented in Table 5 indicate significant positive relationships between the six business strategies and the performance of the exporting SMEs in the study. The results of this study provide some empirical evidence that suggests positive relationship exists between business strategy and the performance of the SMEs.

The results of this study support findings of previous studies that found significant positive relationships between business strategy and performance of exporting small firms (Namiki, 1988; and Baird, Lyles and Orris, 1994). The findings of the study further appear to concur with the general view presented in the literature that suggests the linkage between business strategy and export performance. Additionally, the results of the study seem to support the strategic management perspective that suggests business strategy based on competitive advantage can provide surplus profit to firms.

This study offers implications for exporting SMEs. On the basis of the results of this study, owners and managers of SMEs should realize that there is not one best business strategy for exporting. In view of this, the exporting firms should attempt to adopt business strategy that fits with the capabilities of their firms. Furthermore, to ensure that their firms would be able to compete in international markets, owners and managers of exporting SMEs need to focus on developing their business strategy based on the competitive advantage of their firms.

Although the literature indicates the Malaysian context identify other business the performance o

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Although the findings of this study may prove to be useful to exporting SMEs, the literature indicates empirical study in this area remains limited, particularly in the Malaysian context. This research suggests further studies are needed to explore and identify other business strategies not included in this study but may be helpful to improve the performance of exporting small firms.

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* Professor at Department of Management, Universiti Malaya.

† Lecturer at Department of Management, Universiti Selangor International

FINANCING FACILITIES FOR AGRO ENTREPRENEURS IN ISLAMIC BANKS

Professor Dr. Joni Tamkin Bin Borhan* &
Muhammad Ridhwan Bin Ab. Aziz[‡]

Abstract

It is clear from the general perception that the agricultural projects being less viable than any other sectors. While, it is admitted that the risks in agricultural investments are higher due to various factors, such risks are very rare in as far as the effect weather and natural disasters have on the production of the primary produce. With the introduction of high-technology farming and rapid advancement in the field of bio-technology, the adverse effect of weather on agricultural production has been minimized. Nowadays, a lot of opportunities have been given especially by the local Islamic Banks in order to assist agro entrepreneurs not only to finance their projects but also to expand them in a larger capacity. Thus, this article tries to analyze the concept of agriculture and agribusiness in Islam as well as the financing facilities provided to the agro entrepreneurs in order to support their projects. This article will be divided into two sections namely agriculture and agribusiness in Islam as well as financing facilities in Islamic banks.

Keywords: Agriculture, Agribusiness, Financing Facilities.

* Professor at Department of Syariah & Economics, Academy of Islamic Studies, University of Malaya.

‡ Lecturer at Department of Banking and Finance, Faculty of Management and Muamalah, Selangor International Islamic University College (SIIUC).

Introduction

Agriculture has been an important source of food production for mankind since ancient times and should not be neglected. Earnings through agriculture and becomes agro entrepreneurs are regarded as an honorable endeavor from Islamic spirit. It is clear from the Islamic teaching that agriculture is an important sector that shall not be ignored. Indeed, there are many verses from the *al-Qur'an* as well as the traditions of the Prophet Muhammad (*s.a.w.*) that emphasizes on the importance of agriculture.

Production function in the Islamic economics has been regulated by the concept of livelihood (*al-Rizq*) as well as lawful (*Halal*) and unlawful (*Haram*) sources of earnings. The term *al-Rizq* is applied to connote means of livelihood and further production which has been intimated by the Prophet Muhammad (*s.a.w.*) and predetermined by Allah (*s.w.t.*).

As such, there are number of questions need to be solved such as how Islam views agriculture and agribusiness? What are the financing facilities provided by the local Islamic banks in order to help agro entrepreneurs? Are these facilities complied with the *shari'ah* requirements? All these questions will be analyzed and answered in this article based on views stated in *al-Qur'an* and *al-Hadith*, views given by Muslim jurists and *fiqh* scholars as well as data and information given by the officers of Islamic banks.

Agriculture and Agribusiness in Islam.

As an organized religion, Islam goes into great detail on the subject of agriculture¹, which plays a very significance role in the daily life of a Muslim. The Islamic teaching puts a high value on efforts to consolidate the agricultural industry.

¹ In Arabic, the word agriculture refers to *al-Filahah* means the act of clearing and cutting but, when applied to the soil has the meaning of "to break up in order to cultivate or to plough". From Pre-Islamic times the word *filahah* has assumed a wider meaning to denote the occupation of husbandry and agriculture. In this sense, it is synonymous with *zira'ah*, to which the ancients preferred *filahah* (all the earlier writers called their works on agriculture *Kitab al-Filahah*). See *The Encyclopedia of Islam* (1965), Netherlands: Leiden, Vol. II, p.899

Al-Qur'an as a main source of agriculture³.

Allah (*s.w.t.*)

"Do not the Us
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⁶ A lot of researches l
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Al-Qur'an as a main source of Islamic jurisprudence emphasizes on the important of water² in agriculture³.

Allah (s.w.t.) says to the effect:

"Do not the Unbelievers see that the heavens and the earth were joined together (as one unit of creation), before we clove them asunder? We made from water every living thing. Will they not then believe?".

Surah al-Anbiya'(21):30.

It can be inferred from this verse that Allah (s.w.t.) bring to life plants and animals in this world from water⁴, which has been sent down from sky. As such, Allah (s.w.t.) has provided a continuous water supply for all his creations⁵. Rain that has been sent down by Allah (s.w.t.) from sky to bring life and fertilize plants on the earth will finally bring a lot of benefits to mankind, be it in the form of fruits for eating or leaves and trunks of trees for healthy and medication purposes⁶.

² Surface were all leveled, the whole surface would be under water, as the mean elevation of land sphere-level would be 7,000 to 10,000 feet below the surface of the ocean. This shows the predominance of water on our globe. That all life began in the water is also a conclusion to which our latest knowledge in biological science points. Apart from the fact that protoplasm, the original basis of living matter, is liquid or semi-liquid and in a state of constant flux and instability, there is the fact that land animals, like the higher vertebrates, including man, show in their embryological history, organs like those of fishes, indicating the watery origin of their original habitat. The constitution of protoplasm is about 80 to 85 per cent of water. See *The Holy Qur-an: English Translation of the Meanings and Commentary* (1410H), Madinah: King Fahd Holy Qur-an Printing Complex, p.924.

³ Abu Bakar Abdul Majeed (2006), "Enhancing Food Security in the Era of Information and Communications Technology in the Muslim World" in Shaikh Mohd Saifuddeen Shaikh Mohd Salleh et.al. (eds.), *Food and Technological Progress: An Islamic Perspective*, Kuala Lumpur: MPH Group Publishing Sdn. Bhd., p.58.

⁴ According to the majority of *al-Mufasssirin*, water here means sperm (*Nutfah*). See Ibn al-Hummam (2003), *Fath al-Qadir*, Riyad: Dar Alim al-Kutub, Vol.3, p.405; See also Ahmad Mustafa al-Maraghi (1998), *Tafsir al-Maraah*, Beirut: Dar al-Kutub al-Ilmiyyah, Vol.16-18, p.163.

⁵ Abu Bakar Abdul Majeed (2006), *op.cit.*, p.58.

⁶ A lot of researches have been done proved that certain plants nutrients can be of benefit to our health. Our body for instance, is unable to manufacture many of the essential compounds needed for all its life-sustaining tasks, from building bones, making blood and muscle to regulating brain, liver and heart function. In one six-year study by Harvard Medical School and Harvard School of Public Health, evaluated that tomato products (which contain large quantities of lycopene) showed a measurable relationship to reduce prostate cancer, breast cancer and cervical cancer risks. This is because, as consumption of tomato products increased, levels of lycopene in the blood increased, and the risk of all these cancers decreased. Another example of healthy supplement derived from plants is Lutein, found in dark green leafy vegetables such as spinach, plus various fruits and corns. Researches have indicated that Lutein promotes long-term eye maintenance by acting as a filter against the damaging effects of the sun, particularly retinal damage and macular degeneration. See *The Star*, April 27, 2008:SF15 "Plant

From the perspective of history, we can observe the story of Saba', which had been mentioned in the *al-Qur'an*. The tribe of Saba' was famous with agriculture activities and owned advanced technologies of agricultural. It was said that the tribe has long miles of fruits farms and when harvesting period came, the tribe only has to bring along baskets in order to pick up their fruits⁷

Allah (*s.w.t.*) states to the effect:

"There was, for Saba', aforetime, a sign in their home-land-two gardens to the right and to the left. Eat of the sustenance (provided) by your Lord, and be grateful to him; a territory fair and happy, and a Lord Oft-Forgiving!"

Surah Saba'(34):15.

According to Ibn Kathir, in this verse Allah (*s.w.t.*) tells the story of Saba'⁸ tribe (*Qabilah*) lived in Yemen in the time of Solomon and Queen Bilqis, in a happy and prosperous country, amply irrigated from the Ma'rib dam⁹. Its road was skirted by gardens on both sides, right and left, where at any given point, you always saw two gardens. It produced fruits, spices, and frankincense, and got the name of Araby the Blest for that part of the country¹⁰.

Saba' was a great emperor, given with arable lands and farms as well as green crops. Its residents live with peace and harmony. Allah has commanded Saba' resident to enjoy all the sustenance provided to them and be grateful to Allah Almighty. However, the people of Saba' ignored the God's injunction and Allah has withdrawn all the privileges and arable agriculture lands given to them

Power". Besides, Leonuns Sibiricus (a type of nut) proved by recent research by Malaysia Agriculture Research and Development Institute (MARDI) that this kind of nut enriches with nutrition such as protein, carbohydrates, mineral (calcium, phosphorus, ferrous, netrium and calium) and vitamins (A, B1 and B2). See *Berita Harian*, July 8, 2008:15 "Khasiat Kacangma".

⁷ Mastura Mohd. Zain (2008) "Menimba pahala daripada hasil bumi". *Berita Harian*, May 13, p.11.

⁸ Saba' was originally name of a person namely Saba' Bin Yashjub Bin Ya'rub Bin Qahtan Bin Hud. See Ibn al-Hummam, *op.cit.*, Vol.4, p.319. See also Ahmad Mustafa al-Maraghi, *op.cit.*, Vol.22-24, pp.57-59.

⁹ Ibn Kathir (1966), *Tafsir al-Qur'an al-Azim*, Beirut: Dar al-Andalus, Vol.5, pp.538-543; Ahmad Mustafa al-Maraghi, *op.cit.*, Vol.22-24, pp.57-59.

¹⁰ Ibn al-Hummam, *op.cit.*, Vol.4, pp.319-321. See also The Holy Qur-an: English Translation of the Meaning and Commentary, *op.cit.*, p.1278.

It was said that, about 13 prophets have been sent to the tribe but they refused to accept Allah's exclamation¹¹.

Allah (*s.w.t.*) states to the effect:

"But they turned away (from Allah), and We sent against them the flood (released) from the Dams, and We converted their two garden (rows) into "gardens" producing bitter fruit; and tamarisks, and some few (stunted) lote-trees. That was the requital We gave them because they ungratefully rejected faith, and never do We give (such) requital except to such as are ungrateful rejecters".

Surah Saba' (34):16-17.

The above verses justified that although Allah (*s.w.t.*) has given a lot of privileges to the people of Saba' and because they rejected the true faith and became arrogant of their prosperity and skill in irrigation engineering, in respect of the wonderful works of the dam therefore, Allah has converted all the privileged into bad requital when a mighty flood came and the dam was burst and destroyed everything they have. This spectacular crisis is requital for those who reject true faith commanded by Allah (*s.w.t.*)¹².

Meanwhile, Islam views agriculture sector as an obligation of the society (*Fard al-Kifayah*)¹³. As such, from the perspective of Islam, getting involved in this important sector is an honorable endeavor. This is because a person who is involved in food production is not only looking after himself, but also the rest of the community. This is actually akin to donation (*Sadaqah*) in Islam¹⁴.

¹¹ Mastura Mohd. Zain (2008) "Menimba pahala daripada hasil bumi". *Berita Harian*, May 13, p.11; Ibn al-Hummam, *op.cit.*, Vol.4, pp.319-324; Ibn Kathir, *op.cit.*, Vol.5, pp.538-543.

¹² Ibn al-Hummam, *op.cit.*, Vol.4, p.321; Ibn Kathir, *op.cit.*, Vol.5, pp.538-543; Ahmad Mustafa al-Maraghi, *op.cit.*, Vol.22-24, pp.57-59.

¹³ *Fard al-Kifayah* is differed from *Fard al-'Ain*. *Fard al-'Ain* is any action and benefit, which are repeated from time to time such as praying five times a day, as a mean to obey Allah and it is regarded as a compulsory action for every man. Conversely, *Fard al-Kifayah* is any action that is not recurring from time to time such as cleaning and bathing dead body when someone died. *Fard al-Kifayah* is compulsory (*Wajib*) upon people of the society (*al-Mukaliffin*) according to the majority of Islamic scholars. When someone in the society has carried out the duty, the responsibility for the whole society has been removed. See Ibn al-Najjar (2003), *Sharh al-Kaukab al-Munir*, Makkah: Jami'ah Umm al-Qura, Vol.1, pp.374-376.

Prophet Muhammad (s.a.w.) said¹⁵:

"There is none amongst the Muslims who plants a tree or sows seeds, and then a bird, or a person or an animal eats from it, but is regarded as a charitable gift for him".

Allah (s.w.t.) stresses to the effect:

"The parable of those who spend their wealth in the way of Allah is that of a grain of corn: it groweth seven ears, and each ear hath a hundred grains. Allah giveth manifold increase to whom he pleaseth: and Allah careth for all and he knoweth all things".

Surah al-Baqarah (2):261.

In elaborating this verse, al-Qurtubi of the opinion that, this verse shows agriculture sector is an obligation of the Muslim society (*Fard al-Kifayah*) and this very important job will give revenues and income sources to mankind¹⁶.

In the time of Prophet Muhammad (s.a.w.), he had given close attention to agricultural activities as well as in monitoring farmer's entitlements. After Islam had attained victory in Khaybar, the Prophet (s.a.w.) has made a partnership contract with the Jew in sharing crops¹⁷.

¹⁴ Mohd. Effendi Norwawi (2006), "Food Security from the Malaysian Perspective" in Shaikh Mohd Saifuddeen Shaikh Mohd Salleh *et.al.* (eds.), *Food and Technological Progress: An Islamic Perspective*, Kuala Lumpur: MPH Group Printing (M) Sdn. Bhd., p.7.

¹⁵ *Sahih al-Bukhari* (1999), Riyad: Dar al-Salam, "Kitab al-Harth wa al-Muzara'ah", Hadith No:2320, p.372; *Sahih Muslim* (1998), Riyad: Dar al-Salam, "Kitab al-Musaqat wa al-Muzara'ah", Hadith No:3969, p.679.

¹⁶ Al-Qurtubi (1995), *Jami' al-Ahkam al-Qur'an*, Beirut: Dar Ihya' al-Turath al-Arabi, Vol.3, pp.305-306; Ahmad Mustafa al-Maraghi, *op.cit.*, Vol.1-3, p.397.

¹⁷ Al-Shawkani (2003), *Nail al-Awtar*, Riyad: Dar Alim al-Kutub, Vol.3, pp.7-8.

In a *hadith* narrated by Ibn Umar, Prophet Muhammad (*s.a.w.*) said¹⁸:

“The Prophet (*s.a.w.*) made a deal with the people of Khaybar that they would have half the fruits and vegetation of the land they cultivated”.

Meanwhile, land has been an important factor of production since ancient times. Emphasis on the development of dead lands or barren lands is indicative of the Prophet Muhammad (*s.a.w.*) interest in the utilization of resources for the well-being of people. Good peasant-landlord relationships are fundamental for the economic well-being of the population dependent on the soil¹⁹.

The Holy Prophet has given general instructions to regulate the peasant-landlord relationships, but details of the law have been left to the temporal context within the framework of *Shari'ah*. In addition, he (*s.a.w.*) placed a high value on the economic welfare of the people. He (*s.a.w.*) liked to see the Muslims well-off rather than hungry and destitute. There are some traditions which suggest that the Holy Prophet desired to see his followers at a higher echelon on the ladder of development²⁰.

After establishing the state of Medina, one of the first steps, which the Holy Prophet (*s.a.w.*) took was the establishment of brotherhood among the *Ansars* of Medina and *Muhajirs* or immigrants from Mecca. This brotherhood was, in fact, a step towards the economic rehabilitation of the newly arrived immigrants. Medina had an agrarian base and bulk of local populations was engaged in agriculture²¹.

Prophet Muhammad (*s.a.w.*) invited people to develop the dead land (*al-Mawat*). He (*s.a.w.*) creed that the dead land belongs to the person who develops them. The Prophet also instituted many laws regarding cultivations and marketing of agricultural products²².

¹⁸ *Sahih al-Bukhari* (1999), Riyad: Dar al-Salam, “Kitab al-Harth wa al-Muzara’ah”, Hadith No:2329, p.374; *Sahih Muslim* (1998), Riyad: Dar al-Salam, “Kitab al-Musaqat wa al-Muzara’ah”, Hadith No:3962, p.678.

¹⁹ Muhammad Akram Khan, *op.cit.*, p.41; Afzul-Ur-Rahman, *op.cit.*, p.108.

²⁰ Muhammad Baqir as-Sadr (1983), *Iqtisaduna*, Tehran: World Organization for Islamic Services, Vol.2-Part.1, pp.126-127; M. Umer Chapra (1992), *op.cit.*, pp.263-265; Muhammad Akram Khan, *op.cit.*, p.41.

²¹ *Ibid.*

However, Islam has not permitted cultivation of plants, eating of which has been prohibited. Cultivating opium and cannabis for instance, is therefore prohibited. Cultivation of any prohibited thing for sale to non-Muslims is also forbidden²³.

In the *al-Qur'an*, while referring to His bounties and favors to mankind, Allah mentions the principles needed for the pursuit of agriculture. Allah has spread out the earth and made it suitable and fertile for cultivation and production. This is a bounty to human beings, which we ought to recall and be thankful for. *Al-Qur'an* has encouraged agriculture in many of its verses²⁴.

Allah (s.w.t.) stresses in the *al-Qur'an*:

"It is He who sendeth down rain from the skies, with it We produce vegetation of all kinds, from some We produce green (crops), out of which We produce, close-compounded grain out of the date-palm and its sheaths (or spathes) (come) clusters of dates hanging low and near, And (then there are) gardens of grapes, and olives, and pomegranates, each similar (in kind) yet different (in variety), when they begin to bear fruit, feast your eyes with the fruit and the ripeness thereof. Behold! in these things there are signs for people who believe".

Surah al-An'am (6):99.

"And the earth We have spread out (like a carpet), set thereon mountains firm and immovable, and produced therein all kinds of things in due balance. And We have provided therein means of subsistence, for you and for those for whose sustenance ye are not responsible".

Surah al-Hijr (15):19-20.

²² Afzul-Ur-Rahman, *op.cit.*, pp.159-163; Muhammad Baqir as-Sadr, *op.cit.*, Vol.2-Part.1, pp.107-120; Muhammad Akram Khan, *op.cit.*, p.41;

²³ Jamaat-e-Islami Pakistan, "Islamic Laws Regarding Profession and Earning", <http://www.jamaat.org/islam>, 30th November 2008.

²⁴ Yusuf al-Qaradawi, *op.cit.*, p.128; Afzul-Ur-Rahman, *op.cit.*, pp.87-88; Mastura Mohd. Zin (2008): "Menimba pahala daripada hasil bumi", *Berita Harian*: May 13, p.11; Irsad Lubis, *op.cit.*, p.63.

"It is He who
date-palm
and stalks
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"Then let
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In all these
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(s.w.t.) said in a hadith

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Financing Facilities

In Malay
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²⁵ *Ibid.*
²⁶ *Sahih al-Bukhari*
op.cit., "Kitab al-Muamalah"
²⁷ Ibn Hajar (1956)
op.cit., p.129.
²⁸ The contribution of
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"It is He who has spread out the earth for (His) creatures. Therein is fruit and date-palms, producing spathes (enclosing dates). Also corn, with (its) leaves and stalk for fodder, and sweet-smelling plants. Then which of the favors of your Lord will ye deny?"

Surah al-Rahman (55):10-13.

"Then let man look at his food, (and how We provide it). For that We pour forth water in abundance. And We split the earth in fragments. And produce therein grain. And grapes and the fresh vegetation. And olives and dates. And enclosed gardens, dense with lofty trees. And fruits and fodder. A provision for you and your cattle".

Surah 'Abas (80):24-32.

In all these Quranic verses there is encouragement for mankind to engage and involve in agriculture activity, for it has been made easy for him as a divine favor²⁵. Prophet Muhammad (s.a.w.) said in a hadith narrated by 'Anas²⁶:

"When a Muslim plants a plant or cultivates a crop, no bird or human being eats from it without its being accounted as a rewardable charity for him".

The implication of this *hadith* is that the reward of the person who plants a tree or a crop continues as long as the produce of this tree or crop is eaten or used, even though he may have sold it to someone else²⁷.

Financing Facilities in Islamic Banks.

In Malaysia, not all Islamic banks or Islamic windows of conventional banks do offer Islamic financing facility in agriculture for agro entrepreneur. Nevertheless, because of the important of agriculture to our country²⁸, there are some Islamic banks and Islamic windows of conventional banks do provide financial helps to agro entrepreneurs as below:

²⁵ *Ibid.*

²⁶ *Sahih al-Bukhari, op.cit.*, "Kitab al-Harth wa al-Muzara'ah", Hadith No:2320, p.372; *Sahih Muslim, op.cit.*, "Kitab al-Musaqat wa al-Muzara'ah", Hadith No:3970, p.679.

²⁷ Ibn Hajar (1956), *Fath al-Bari*, Riyad: Maktabah al-Riyad al-Hadithah, Vol.5, p.4; Yusuf al-Qaradawi, *op.cit.*, p.129.

²⁸ The contribution of agriculture sector towards Gross Domestic Product (KDNK) is about 7.5% in 2008. For the production of rice alone, Malaysian consumes about 2.2 million tones of rice in a year.

i) Agro Bank²⁹.

The facilities available for financing agriculture sector provided by Agro Bank can be classified into two categories namely commercial funds and special funds established by government in order to provide funds for agriculture sector and have been channeled through Agro Bank. The objective of providing these financing facilities is to provide working capital for a new agriculture project or for expanding of existing agro project³⁰.

a) Commercial Funds.

Financing under these funds are basically market and profit driven, hence the terms and conditions of these facilities are based on commercial consideration. The source of fund is the normal deposits by the depositors of Agro Bank and usually regulated by market forces. Agro Bank is keen to finance all activities related to the agriculture sector and the scope of financing is expended to the production, processing and marketing of agriculture produces³¹.

but our country is only able to produce 1.6 million tones. The government had to import some 600,000 tones to satisfy the demand of this main staple. See *New Straits Times*, August 30, 2008:4 "Ensuring enough supply to meet nation's food needs"; *Berita Harian*, August 30, 2008:34 "Sumbangan pertanian kekal stabil".

²⁹ Agro Bank was incorporated under the Company Act 1965 and had been registered as Bank Pertanian Malaysia Berhad. Agro Bank is an entity owned by Malaysia government and started its operation on 1st April 2008. This bank originally known as Bank Pertanian Malaysia (BPM), which has been established under Parliament Act, but has been operated as incorporated institution since 1970. Based on BPM Act 1969, the objective of BPM formation are to stimulate the development of agriculture sector in Malaysia, to supervise credit-assistants for the purpose of agriculture projects as well as to provide loan facilities, deposits and credits for the development of agriculture sector including for the production and marketing of produces of agriculture. The main mission of Agro Bank is to provide comprehensive financial services based on market and customer demands to the target group namely agro entrepreneur, small and medium scale businessmen and also individuals. When the New Economic Policy was introduced in 1970, BPM took an attempt and responsibility to abolish poverty and re-arrange the society particularly among the Malays, who most of them are paddy cultivator, tobacco planter and fishermen. At that time, BPM had established credit scheme for paddy production, credit scheme for tobacco, scheme for crop loan, credit scheme for vehicle as well as scheme for fishery in order to support the target group in obtaining credit source at minimum cost. Agro Bank is a bank owned by government (GLC) under the supervision of Ministry of Finance and all financing policies for the agriculture sector is based on the requirement set by Ministry of Agriculture and Agro-Based Industry. See Dato' Mohd, Rosli Abd Aziz (2000), "Peranan Bank Pertanian Dalam Memajukan Sektor Pertanian Negara", <http://banktani.tripod.com/gm1.htm>, 9th November 2008; Agro Bank, <http://www.agrobank.com.my/history.aspx>, 15th December 2008; Agro Bank, <http://www.agrobank.com.my/content.aspx?v=vissionmission>, 15th December 2008; Agro Bank, <http://www.agrobank.com.my/content.aspx?v=aboutus>, 15th December 2008. Agro Bank has been chosen for the sampling purpose of this research since this bank is a major contributor for financing agriculture projects and for promoting sound agricultural development in Malaysia since its establishment. Agro Bank is being the only bank in this country specializing in agriculture and has 39 years of experiences and excellent record in assisting agro entrepreneurs. See for instance, "Financing of Agriculture", <http://banktani.tripod.com/gm5.htm>, 9th November 2008.

³⁰ Abd. Rahaman Rasid (2000), "Peluang Pembiayaan Dalam Sektor Makanan", <http://banktani.tripod.com/aran.htm>, 9th November 2008; "Financing of Agriculture", <http://banktani.tripod.com/gm5.htm>, 9th November 2008; Agro Bank, <http://www.agrobank.com.my>, 15th December 2008; Agro Bank Pamphlet (2008), "Financing Facilities".

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Table 2.1
Agro Bank: Agro Cash-i

Features:	Description:
Objective:	<ul style="list-style-type: none"> To provide financing facility for consumption needs related to agricultural and agro-based activities.
Eligibility	<ul style="list-style-type: none"> Government servant (permanent or contract). Private servant. Age between 18 to 58 years old.
Financing Limit:	<ul style="list-style-type: none"> Up to RM150,000. Up to 15 years.
Category:	<ul style="list-style-type: none"> Terms Financing.
Shari'ah Concept Applied:	<ul style="list-style-type: none"> Bay' al-Innah.
Collateral:	<ul style="list-style-type: none"> No collateral, only one guarantor.
Projects Eligible for Financing:	<ul style="list-style-type: none"> All activities relates to agriculture.

Source: Suhaimi Bin Yacob, Executive 2, Financing Division, Agro Bank, Jalan Padang Garong, Kota Bharu, Kelantan. Interview carried out on 14th December 2008 at 11.15 a.m. to 11.50 a.m.; *Agro Bank Pamphlet* (2008), "Financing Facilities"; Agro Bank, <http://www.agrobank.com.my>, 15th December 2008.

Table 2.2
Agro Bank: Agro Contract.

Features:	Description:
Objective:	<ul style="list-style-type: none"> To provide revolving credit facility to finance contract works.
Eligibility:	<ul style="list-style-type: none"> Malaysian citizens between 18 to 58 years old.
Financing Limit:	<ul style="list-style-type: none"> Annual and renewable.
Category:	<ul style="list-style-type: none"> Revolving financing.
Shari'ah Concept Applied:	<ul style="list-style-type: none"> Bay' Bithaman Ajil.
Collateral:	<ul style="list-style-type: none"> Case by case.
Projects Eligible for Financing:	<ul style="list-style-type: none"> All agriculture indentures awarded by the agricultural body.

Source: Suhaimi Bin Yacob, Executive 2, Financing Division, Agro Bank, Jalan Padang Garong, Kota Bharu, Kelantan. Interview carried out on 14th December 2008 at 11.15 a.m. to 11.50 a.m.; *Agro Bank Pamphlet* (2008), "Financing Facilities"; Agro Bank, <http://www.agrobank.com.my>, 15th December 2008.

Table 2.3
Agro Bank: Agro Business.

Features:	Description
Objective:	• To provide agro entrepreneurs a continuous working capital via overdraft facility.
Eligibility:	• Malaysian citizens age between 18 to 58 years old.
Limit	• Annual and renewable.
Category:	• Revolving financing.
Shari'ah Concept Applied:	• Bay' al-Innah.
Collateral:	• Case by case.
Projects Eligible for Financing:	• Agriculture contract, working capital, raw materials and salary for workers.

Source: Suhaimi Bin Yacob, Executive 2, Financing Division, Agro Bank, Jalan Padang Garong, Kota Bharu, Kelantan. Interview carried out on 14th December 2008 at 11.15 a.m. to 11.50 a.m.; *Agro Bank Pamphlet* (2008), "Financing Facilities"; Agro Bank, <http://www.agrobank.com.my>, 15th December 2008.

b) Special Funds.

From time to time, Malaysia government established schemes and provided funds for financing agriculture sector. These funds can be considered as incentives to promote investments in priority agricultural sector. The incentives usually take the forms of low cost of financing, longer duration of financing period and higher margin of financing. These schemes are open to all institutions and companies incorporated in Malaysia as long as the ownership by Malaysians is more than 50%, as well as to all Malaysian citizens³².

Through these special funds, Agro Bank will continue its social responsibility in order to finance agriculture sector as been assigned by the government through Ministry of Agriculture and Agro-Based Industry in achieving the related policies under Ninth Malaysia Plan (RMK-9)³³.

³² Dato' Mohd. Rosli Abd. Aziz, "Financing of Food and Agricultural Production", <http://banktani.tripod.com/gm3.htm>, 9th November 2008; Dato' Mohd. Rosli Abd. Aziz (2000), "Peranan Bank Pertanian Dalam Memajukan Sektor Pertanian Negara", <http://banktani.tripod.com/gm1.htm>, 9th November 2008; "Financing of Agriculture", <http://banktani.tripod.com/gm5.htm>, 9th November 2008; Agro Bank, <http://www.agrobank.com.my>, 15th December 2008.

³³ Habsah Dinin (2008): "Skim Pembiayaan dipelbagai". *Berita Harian*, August 8, p.30.

Table 2.4
Agro Bank: Fund for Food (3F Loan).

Features:	Description:
Objective:	<ul style="list-style-type: none"> • To promote investment in the food production activities at the reasonable cost. • To promote primary food production (including sea-food, animal husbandry, vegetables and fruits). • To promote the efficient distribution of food and food products.
Eligibility:	<ul style="list-style-type: none"> • Malaysia citizens residing in Malaysia. • Malaysian owned institutions and companies (at least with 51% ownership).
Financing Limit:	<ul style="list-style-type: none"> • RM10,000-RM10 million.
Maximum Financing:	<ul style="list-style-type: none"> • 90% of project cost.
Financing Period:	<ul style="list-style-type: none"> • Up to 10 years.
Shari'ah Concept Applied:	<ul style="list-style-type: none"> • Bay' Bithaman Ajil.
Collateral:	<ul style="list-style-type: none"> • Fully secured.
Projects Eligible for Financing:	<ul style="list-style-type: none"> • Food production, processing and marketing (crops, livestock and fishery). • Eligible items for crops are vegetables, tea, paddy, roselle, maize, tapioca, production of seeds and planting equipment for food crops and fruits such as banana, mango, guava, watermelon, papaya, pineapple, sugar cane, coffee, cocoa and etc.

Source: Suhaimi Bin Yacob, Executive 2, Financing Division, Agro Bank, Jalan Padang Garong, Kota Bharu, Kelantan. Interview carried out on 14th December 2008 at 11.15 a.m. to 11.50 a.m.; Agro Bank Pamphlet (2008), "Financing Facilities"; Agro Bank, <http://www.agrobank.com.my>, 15th December 2008.

Table 2.5
Agro Bank: Food Production Credit Scheme (SKPM).

Features:	Description:
Objective:	<ul style="list-style-type: none"> To increase the national food production. To provide fixed capital and working capital for the purpose of financing food production project.
Eligibility:	<ul style="list-style-type: none"> Malaysia citizens residing in Malaysia. Malaysian owned institutions and companies (at least with 50% ownership).
Financing Limit:	<ul style="list-style-type: none"> Not exceeding RM500,000.
Maximum Financing:	<ul style="list-style-type: none"> 90% of project cost.
Financing Period:	<ul style="list-style-type: none"> Up to 8 years or up to 10th September 2018.
Shari'ah Concept Applied:	<ul style="list-style-type: none"> Bay' Bithaman Ajil.
Collateral:	<ul style="list-style-type: none"> Fully secured.
Projects Eligible for Financing:	<ul style="list-style-type: none"> All upstream and downstream food production activities.

Source: Suhaimi Bin Yacob, Executive 2, Financing Division, Agro Bank, Jalan Padang Garong, Kota Bharu, Kelantan. Interview carried out on 14th December 2008 at 11.15 a.m. to 11.50 a.m.; Agro Bank Pamphlet (2008), "Financing Facilities"; Agro Bank, <http://www.agrobank.com.my>, 15th December 2008

Features:
Objective:
Eligibility:
Financing Limit:
Maximum Financing:
Financing period:
Shari'ah Concept Applied:
Collateral:
Projects Eligible for Financing:

Source: Suhaimi Bin Yacob, Executive 2, Financing Division, Agro Bank, Jalan Padang Garong, Kota Bharu, Kelantan. Interview carried out on 14th December 2008 at 11.15 a.m. to 11.50 a.m.; Agro Bank Pamphlet (2008), "Financing Facilities"; Agro Bank, <http://www.agrobank.com.my>, 15th December 2008

Table 2.6
Agro Bank: Paddy Credit Scheme (SKP).

Features:	Description:
Objective:	<ul style="list-style-type: none"> To increase production of paddy in the National Rice Bowl areas. To provide revolving credit for the production of paddy in eight Rice Bowl areas.
Eligibility:	<ul style="list-style-type: none"> Malaysia citizens residing in Malaysia. Malaysian age between 18 to 58 years old.
Financing Limit:	<ul style="list-style-type: none"> Not exceeding maximum financing of RM15,000 per season.
Maximum Financing:	<ul style="list-style-type: none"> 100% of project cost.
Financing period:	<ul style="list-style-type: none"> Up to 6 months (1 season).
Shari'ah Concept Applied:	<ul style="list-style-type: none"> Bay' Bithaman Ajil.
Collateral:	<ul style="list-style-type: none"> Case by case.
Projects Eligible for Financing:	<ul style="list-style-type: none"> All paddy planting production activities.

Source: Suhaimi Bin Yacob, Executive 2, Financing Division, Agro Bank, Jalan Padang Garong, Kota Bharu, Kelantan. Interview carried out on 14th December 2008 at 11.15 a.m. to 11.50 a.m.; Agro Bank Pamphlet (2008), "Financing Facilities"; Agro Bank, <http://www.agrobank.com.my>, 15th December 2008.

Table 2.7
Agro Bank: Bumiputera Industrial and Business Community Scheme (MPPB).

Features:	Description:
Objective:	<ul style="list-style-type: none"> To encourage and develop Bumiputera Entrepreneurs in the agriculture sector. To provide fixed capital and working capital to Bumiputera Enterprise in developing agriculture project or agro based businesses.
Eligibility:	<ul style="list-style-type: none"> Companies with paid up capital exceeding RM100,000. For farmer and fishermen institutions, they should have equity more than RM100,000. Priority is given to the individual entrepreneurs who are expanding their businesses.
Financing Limit:	<ul style="list-style-type: none"> RM10,0000-RM5 million.
Maximum Financing:	<ul style="list-style-type: none"> 90% of project cost.
Financing Period:	<ul style="list-style-type: none"> Not exceeding 10 years or up to 23rd October 2014.
Shari'ah Concept Applied:	<ul style="list-style-type: none"> Bay' Bithaman Ajil.
Collateral:	<ul style="list-style-type: none"> Fully secured.
Projects Eligible for Financing:	<ul style="list-style-type: none"> Commercial agriculture sector, sectors of agriculture based manufacturing or processing and also agriculture services.

Source: Suhaimi Bin Yacob, Executive 2, Financing Division, Agro Bank, Jalan Padang Garong, Kota Bharu, Kelantan. Interview carried out on 14th December 2008 at 11.15 a.m. to 11.50 a.m.; *Agro Bank Pamphlet* (2008), "Financing Facilities"; Agro Bank, <http://www.agrobank.com.my>, 15th December 2008.

From all the facilities provided by the Agro Bank, it can be concluded that Agro Bank has provided different types of financing facilities based on *Shari'ah* compliant product (*Bay' Bithaman Ajil* or *Bay' al-Innah*) to cater different categories of Muslim entrepreneurs in this country.

For instance, Agro Bank has provided for the paddy farmer the Paddy Credit Scheme (SKP) in order to increase the production of paddy with 100% financing of project cost and maximum of RM15,000 per season. Indeed, this facility is very meaningful for them who always gain their return on each season after the harvesting period.

ii) Bank Kerjasama Rakyat Malaysia Berhad (Bank Rakyat)³⁴.

Facility offers by Bank Rakyat with regards of agriculture financing can be divided by three types namely Financing Scheme of Land-i Ardhi, Term-i and Property-i as follows:

Financing Scheme of Land-i Ardhi is offers for developing idle land with respect of agriculture project by customer. The facility for financing under the scheme of Land-i Ardhi uses the contract of sales based on *Bay' Bithaman Ajil* (BBA) principle. Under this principle, the bank will buy property from the customer on cash basis and the bank will sell the property back to the customer based on deferred payment basis. Based on normal procedure, the bank initially will determine the owner of the land. If the land is owned by the customer, bank will act as a buyer for that property with cash basis purchase³⁵.

The contract of selling will be undertaken after the contract of buying completed under the concept of BBA. If the land is not owned by the customer, the bank will ask for the letter of permission from the actual owner in order to utilize and develop the land. The bank will use the concept of al-Wakalah in completing this contract. Both buying and selling contracts can be done between bank and customer using the concept of al-Wakalah. The contract of selling between bank and customer will be based on deferred payment basis under the concept of BBA³⁶. The specific features and terms of this scheme are as below:

³⁴ Bank Rakyat was established in September 1954 under the Cooperative Ordinance 1948, following an expansion of the cooperative movement in Peninsular Malaysia. To facilitate the expansion of the cooperative movement, the co-operatives set up their respective union banks provide financial needs to their members. On 28th September 1954, 11 of these union banks decided to merge and form Bank Agong (Apex Bank). In 1967, Bank Kerjasama Malaysia Berhad replaced Bank Agong with its membership opened not only to the cooperatives, but also to individuals. Subsequent changes in the by-laws also resulted in the creation of its subsidiary companies and opening of branches to serve customers as well as members. On 6th January 1973, the name was changed to Bank Kerjasama Rakyat Malaysia Berhad or better known as Bank Rakyat. Bank Rakyat is governed by its by laws and Bank Kerjasama Rakyat (M) Berhad Act 1978 (Special Provision 202), which allows Bank Rakyat to provide financing to non-members. In 1989, Bank Rakyat was placed under the Ministry of Land and Co-operative Development and the Ministry of Finance. See Bank Rakyat, <http://bankrakyat.skali.my/web/guest/sejarah>, 21st December 2008.

³⁵ Mohd. Jozy Bin Mohd. Ghani, Executive, Financing Unit, Bank Kerjasama Rakyat Malaysia Berhad, Jalan Raja Perempuan Zainab 2, Bandar Baru Kubang Kerian, Kota Bharu, Kelantan. Interview carried out on 10th December 2008 at 3.30 p.m. to 4.15 p.m.

³⁶ *Ibid*

Table 2.8
Bank Rakyat: Financing Scheme of Land-i Ardhi.

Features:	Description:
Eligibility:	<ul style="list-style-type: none"> • Malaysia citizens. • Malaysian aged between 18 to 65 years old. • Not in the state of bankruptcy.
Category:	<ul style="list-style-type: none"> • Developing agriculture land.
Shari'ah Concept Applied:	<ul style="list-style-type: none"> • <i>Bay' Bithaman Ajil</i>.
Margin and Quantum of Financing:	<ul style="list-style-type: none"> • 90% of project cost for the member of the bank. • 80% of project cost for non-member of the bank.
Repayment Period:	<ul style="list-style-type: none"> • Up to 7 years. • Grace period is allowed until 2 years whereby within this period, customer is still not obliged to pay for the financing.
Collateral:	<ul style="list-style-type: none"> • Fully secured on the land of the project.
Insurance:	<ul style="list-style-type: none"> • Optional- normally Mortgage Takaful Plan.
Deposit for Security:	<ul style="list-style-type: none"> • 3 months of the financing will be deducted automatically from the total of financing.
Accredited Land Valuer:	<ul style="list-style-type: none"> • Only required for financing above than RM30,000. • Report from the external land valuer will be validated until 6 months. • For financing below RM30,000, the bank will make own valuation.
Process and Service Fees:	<ul style="list-style-type: none"> • Not applicable.
Documents required:	<ul style="list-style-type: none"> • Agriculture Financing Form, Photocopy of I/C, salary slip and grant, Financial Statement of company or Current Account Statement.

Source: Mohd. Jozy Bin Mohd. Ghani, Executive, Financing Unit, Bank Kerjasama Rakyat Malaysia Berhad, Jalan Raja Perempuan Zainab 2, Bandar Baru Kubang Kerian, Kota Bharu, Kelantan. Interview carried out on 10th December 2008 at 3.30 p.m. to 4.15 p.m.; Bank Rakyat, <http://www.bankrakyat.com.my>, 15th December 2008.

For Bank Rakyat, the financing scheme of Land-i Ardhi is obviously a very helpful financing arrangement especially for the new starter in developing their lands in the agriculture projects. This scheme offers the entrepreneurs up to 90% of the total project cost, which is regarded as very reasonable for the new reviver in this risky project. Another 10% of the total cost needs to be provided by the entrepreneur themselves for example, if the project cost is RM50,000, they need to provide only RM5,000 in order to be qualified for this scheme.

iii) Maybank Islamic Berhad (MIB) ³⁷.

For the time being, Maybank Islamic Berhad offers five types of Islamic financing facility with regards of agriculture sector, as follows:

a) Short Term Revolving Credit (STRC-i).

STRC-i is a *Shari'ah*-compliant short term revolving credit facility granted to corporate and middle market customers. This facility can be offered under the Islamic contract of either *Bay' al-Innah* (sale with immediate repurchase) or *Murabahah* (cost plus profit sale). The salient features and general terms for STRC-i are as below:

³⁷ In Malaysia, the enactment of the Islamic Banking Act that came into effect on 7th April 1983 marked its official introduction into the banking arena. On 1st July 2002, Takaful business was launched by Maybank Takaful Berhad, which is licensed under the Takaful Act 1984. Maybank group is proud to play an important role in the development and promotion of Islamic Banking & Takaful in Malaysia and beyond. On January 1st 2008, Maybank's Islamic Banking began to operate under a new subsidiary of Maybank known as Maybank Islamic Berhad (MIB). By moving into MIB, customers will enjoy a better range of Islamic products and services. The aims of MIB are to continue to be market leader in the provision of Islamic products and services, to introduce financing facilities based on Musyarakah Mutanaqisah (MM) concept in order to improve the concept of BBA, introducing new facilities based on Ijarah Muntahiah Bittamleek (IMB), establishing International Currency Business Unit (ICBU) and actively involved in commodity Murabahah products. Yet, Maybank is the largest Islamic financial services provider in the Asia Pacific region and is set to further reinforce its leadership with the creation of its Islamic subsidiary. Maybank began offering Islamic financing in 1993 through the Islamic windows operations. To date, Maybank has 12 full fledged Islamic banking branches in addition to 376 branches and 20 private banking centers locally offering Islamic banking products and services. See Maybank Islamic Berhad, http://www.maybank2u.com.my/maybankislamic/corporate_info/index.shtml, 21st December 2008; Datuk Amirsham A. Aziz (2007), "Maybank Launches Maybank Islamic Berhad", http://www.maybank2u.com.my/maybankislamic/corporate_info/press_release/index, 21st December 2008.

Table 2.9
Maybank Islamic Berhad: Short Term Revolving Credit (STRC-i).

Features:	Description:
Concept:	<ul style="list-style-type: none"> • Based on the <i>Murabahah</i> concept. As such, an underlying asset is required for the sale and purchase transactions. • Or based on <i>Bay' al-Innah</i>, whereby the identified underlying asset required for the sale and purchase transactions belongs to bank.
Eligibility:	<ul style="list-style-type: none"> • All corporate customers. • Middle market customer.
Tenor:	<ul style="list-style-type: none"> • 1 month, 2,3,6, 9 and 12 months.
Rate:	<ul style="list-style-type: none"> • Variable rate i.e. Selling Price: BLR + 4 or 10% whichever is higher. • Effective rate: To be pegged to cost funds i.e. KLIBOR + (liquidity/reserve cost) + margin.

Source: Aizatul Akma Binti Arifin, Consumer Sales Executive, Financing Unit, Maybank Islamic Berhad, Jalan Sultan Yahya Petra, Kota Bharu, Kelantan. Interview carried out on 14th December 2008 at 2.35 p.m. to 3.15 p.m.; Maybank Islamic Berhad, http://www.maybank2u.com.my/maybankislamic/products_services/index.shtml, 21st December 2008.

b) BBA Term Financing-i.

MIB offers two types of BBA term financing facilities. Firstly, Fixed Rate Term Financing-i. This facility offers a fixed financing cost throughout agreed tenure of financing. This enable customer to protect themselves against risk of rising cost of financing. Secondly, Variable Rate Term Financing-i. Under VRF, the selling price is fixed upfront based on a selling price rate while the effective rate levied on the account will vary based on charges in the Base Financing Rate (BFR), provided it does not exceed the fixed selling price rate ³⁸.

If the BFR moves up to the extent that the effective rate exceeds the fixed selling price rate, the system will only compute profit based on the selling price. Customer will enjoy very competitive rate based on ongoing good market condition and yet protected by a fixed ceiling rate against adverse market condition ³⁹.

BBA term financing is granted under the principle of *al-Bay' Bithaman Ajil* (BBA) or deferred payment sale. The requirement for the presence of sale and purchase elements is compulsory under BBA financing. Under this facility, MIB will assist the customer to identify suitable asset for the purpose. The bank shall purchase the asset concerned and simultaneously sell it to the customer at an agreed price. Payment of selling price can be paid by installment over an agreed period. The salient features of this facility are as below:

³⁸ Aizatul Akma Binti Arifin, Consumer Sales Executive, Financing Unit, Maybank Islamic Berhad, Jalan Sultan Yahya Petra, Kota Bharu, Kelantan. Interview carried out on 14th December 2008 at 2.35 p.m. to 3.15 p.m.; Maybank Islamic Berhad, http://www.maybank2u.com.my/maybankislamic/products_services/index.shtml, 21st December 2008.

³⁹ *Ibid.*

Table 3.0
Maybank Islamic Berhad: BBA Term Financing-i.

Features:	Fixed Rate Financing:	Variable Rate Financing:
Eligibility:	<ul style="list-style-type: none"> • Individuals. • Joint account holders. • Firms and corporate customer i.e. companies incorporated under the Companies Act. 	
Purpose:	<ul style="list-style-type: none"> • Purchase of assets such as landed properties, plants and machineries, share and etc. • Investment portfolio. • Business working capital. • Refinancing of assets. 	
Tenure:	• Up to 10 years.	• Up to 20 years.
Profit Rate:	• Fixed at 1% over and above the conventional lending rate.	• At par with conventional rate at the time of application.

Source: Aizatul Akma Binti Arifin, Consumer Sales Executive, Financing Unit, Maybank Islamic Berhad, Jalan Sultan Yahya Petra, Kota Bharu, Kelantan. Interview carried out on 14th December 2008 at 2.35 p.m. to 3.15 p.m.; Maybank Islamic Berhad, http://www.maybank2u.com.my/maybankislamic/products_services/index.shtml, 21st December 2008.

c) New Entrepreneurs Fund 2 (NEF2).

Central Bank of Malaysia has approved the granting of NEF2 under Islamic banking. NEF2-i is offered by MIB and available at all Business Center of Maybank. The NEF2 funding is administered by Central Bank Of Malaysia and part of the government's continuous effort to promote the growth of small and medium sized Bumiputera enterprises by ensuring that they have access to financing at reasonable cost. The salient features and terms of this facility are as follows:

Features:
Eligibility:
Shariah Concept Applied:
Tenure of Financing:
Purpose of Financing:
Financing Amount:
Profit Rate:
Penalty/Commitment Fee:
Processing Fee:
Projects Eligible for Financing:

Source: Aizatul Akma Binti Arifin, Consumer Sales Executive, Financing Unit, Maybank Islamic Berhad, Jalan Sultan Yahya Petra, Kota Bharu, Kelantan. Interview carried out on 14th December 2008 at 2.35 p.m. to 3.15 p.m.; Maybank Islamic Berhad, <http://www.maybank2u.com.my/maybankislamic/product>

Table 3.0
Maybank Islamic Berhad: BBA Term Financing-i.

Features:	Fixed Rate Financing:	Variable Rate Financing:
Eligibility:	<ul style="list-style-type: none"> • Individuals. • Joint account holders. • Firms and corporate customer i.e. companies incorporated under the Companies Act. 	
Purpose:	<ul style="list-style-type: none"> • Purchase of assets such as landed properties, plants and machineries, share and etc. • Investment portfolio. • Business working capital. • Refinancing of assets. 	
Tenure:	• Up to 10 years.	• Up to 20 years.
Profit Rate:	• Fixed at 1% over and above the conventional lending rate.	• At par with conventional rate at the time of application.

Source: Aizatul Akma Binti Arifin, Consumer Sales Executive, Financing Unit, Maybank Islamic Berhad, Jalan Sultan Yahya Petra, Kota Bharu, Kelantan. Interview carried out on 14th December 2008 at 2.35 p.m. to 3.15 p.m.; Maybank Islamic Berhad, http://www.maybank2u.com.my/maybankislamic/products_services/index.shtml, 21st December 2008.

c) New Entrepreneurs Fund 2 (NEF2).

Central Bank of Malaysia has approved the granting of NEF2 under Islamic banking. NEF2-i is offered by MIB and available at all Business Center of Maybank. The NEF2 funding is administered by Central Bank Of Malaysia and part of the government's continuous effort to promote the growth of small and medium sized Bumiputera enterprises by ensuring that they have access to financing at reasonable cost. The salient features and terms of this facility are as follows:

Table 3.1
Maybank Islamic Berhad: New Entrepreneurs Fund 2.

Features:	Description:
Eligibility:	<ul style="list-style-type: none"> • Bumiputera entrepreneurs who fulfill the following criteria: <ol style="list-style-type: none"> a) Shareholder's funds of not exceeding RM10 million. b) Wholly-owned Bumiputera institutions incorporated under the Companies Act 1965, the Cooperative Societies Act 1993, the Societies Act 1996 or Bumiputera citizens residing in Malaysia. c) Bumiputera entrepreneurs registered under the Registrar of Business or any other authoritative bodies.
Shari'ah Concept Applied:	<ul style="list-style-type: none"> • <i>Bay' Bithaman Ajil</i>.
Tenure of Financing:	<ul style="list-style-type: none"> • Maximum of 5 years from the first drawdown date by Central Bank of Malaysia.
Purpose of Financing:	<ul style="list-style-type: none"> • For expansion in productive capacity and/or working capital for eligible Bumiputera entrepreneurs.
Financing Amount:	<ul style="list-style-type: none"> • No minimum amount of financing. • Maximum financing of RM5 million per customer including financing approved under the earlier NEF scheme and financing approved for any other related companies that have similar shareholders.
Profit Rate:	<ul style="list-style-type: none"> • Presently at 4.00%-6.00% p.a. based on credit rating exercised by the Business Unit of MIB.
Penalty/Commitment Fee:	<ul style="list-style-type: none"> • Not applicable.
Processing Fee:	<ul style="list-style-type: none"> • Not applicable.
Projects Eligible for Financing:	<ul style="list-style-type: none"> • All projects which are viable under the sector of manufacturing, agriculture, services, commerce, tourism, construction, engineering, transportation, furniture, printing, film and quarrying. • The small and medium sized Bumiputera industries participating under the vendor development programs of the Ministry of Entrepreneur Development or Ministry of Finance with at least 70% Bumiputera equity and management control.

Source: Aizatul Akma Binti Arifin, Consumer Sales Executive, Financing Unit, Maybank Islamic Berhad, Jalan Sultan Yahya Petra, Kota Bharu, Kelantan. Interview carried out on 14th December 2008 at 2.35 p.m. to 3.15 p.m.; Maybank Islamic Berhad, http://www.maybank2u.com.my/maybankislamic/products_services/index.shtml, 21st December 2008.

Table 3.1
Maybank Islamic Berhad: New Entrepreneurs Fund 2.

Features:	Description:
Eligibility:	<ul style="list-style-type: none"> • Bumiputera entrepreneurs who fulfill the following criteria: <ol style="list-style-type: none"> a) Shareholder's funds of not exceeding RM10 million. b) Wholly-owned Bumiputera institutions incorporated under the Companies Act 1965, the Cooperative Societies Act 1993, the Societies Act 1996 or Bumiputera citizens residing in Malaysia. c) Bumiputera entrepreneurs registered under the Registrar of Business or any other authoritative bodies.
Shari'ah Concept Applied:	<ul style="list-style-type: none"> • <i>Bay' Bithaman Ajil</i>.
Tenure of Financing:	<ul style="list-style-type: none"> • Maximum of 5 years from the first drawdown date by Central Bank of Malaysia.
Purpose of Financing:	<ul style="list-style-type: none"> • For expansion in productive capacity and/or working capital for eligible Bumiputera entrepreneurs.
Financing Amount:	<ul style="list-style-type: none"> • No minimum amount of financing. • Maximum financing of RM5 million per customer including financing approved under the earlier NEF scheme and financing approved for any other related companies that have similar shareholders.
Profit Rate:	<ul style="list-style-type: none"> • Presently at 4.00%-6.00% p.a. based on credit rating exercised by the Business Unit of MIB.
Penalty/Commitment Fee:	<ul style="list-style-type: none"> • Not applicable.
Processing Fee:	<ul style="list-style-type: none"> • Not applicable.
Projects Eligible for Financing:	<ul style="list-style-type: none"> • All projects which are viable under the sector of manufacturing, agriculture, services, commerce, tourism, construction, engineering, transportation, furniture, printing, film and quarrying. • The small and medium sized Bumiputera industries participating under the vendor development programs of the Ministry of Entrepreneur Development or Ministry of Finance with at least 70% Bumiputera equity and management control.

Source: Aizatul Akma Binti Arifin, Consumer Sales Executive, Financing Unit, Maybank Islamic Berhad, Jalan Sultan Yahya Petra, Kota Bharu, Kelantan. Interview carried out on 14th December 2008 at 2.35 p.m. to 3.15 p.m.; Maybank Islamic Berhad, http://www.maybank2u.com.my/maybankislamic/products_services/index.shtml, 21st December 2008.

d) Financing for Purchasing Vacant Land.

This financing facility is offers for the purchase of vacant land either to develop agro project or to build house or shop-house for residential or business purposes. This facility is based on the *shari'ah* concept of *Bay' Bithaman Ajil*. The features and general terms of this facility are as below:

Table 3.2
Maybank Islamic Berhad: Financing for Purchasing Vacant Land.

Features:	Description:
Objective:	• To purchase land for agro project or build house/shop-house.
<i>Shari'ah</i> Concept Applied:	• <i>Bay' Bithaman Ajil</i> .
Collateral:	• Fully secured on the land under project.
Land Valuer:	• Internal bank valuer only.
Application requirements:	• Salary slip. • Financial statement of 3 consecutive years. • For business enterprise or commercial customer, a guarantee from Credit Guarantee Corporation (CGC) is needed.

Source: Aizatul Akma Binti Arifin, Consumer Sales Executive, Financing Unit, Maybank Islamic Berhad, Jalan Sultan Yahya Petra, Kota Bharu, Kelantan. Interview carried out on 14th December 2008 at 2.35 p.m. to 3.15 p.m.; Maybank Islamic Berhad, http://www.maybank2u.com.my/maybankislamic/products_services/index.shtml, 21st December 2008.

For Maybank Islamic Berhad, this bank has provided different schemes in order to assist the agro entrepreneurs with their projects. One of the schemes is BBA Term Financing-i, which is based on *Bay' Bithaman Ajil* contract. This scheme obviously will gibe a lot of advantages for the agro entrepreneurs especially for those who are required to purchase machines or other types of fixed assets in order to expand their existing businesses. With the payment period up to 20 years, this scheme is actually beneficial for most of them in buying the needed assets since the actual return for their investment may be gained at the longer duration.

Conclusion.

In the final analysis in the agriculture various types of fi large scale of ente entrepreneurs sho compliant financin

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Conclusion.

In the final analysis, Islam has honored person who involves and seeking *Halal* livelihoods in the agriculture and regarded his efforts as a charity. It can also be concluded that there are various types of financing assistants provided to the agro entrepreneur ranging from small until large scale of enterprises and covered up to different kind of agriculture activities. Thus, agro entrepreneurs should grab this opportunity in order to expand their projects based on *shari'ah* compliant financing facilities provided by the local Islamic banks in this country.

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Mohd. Jozy Bin Mohd. Ghani, Executive, Financing Unit, Bank Kerjasama Rakyat Malaysia Berhad, Jalan Raja Perempuan Zainab 2, Bandar Baru Kubang Kerian, Kota Bharu, Kelantan. Interview carried out on 10th December 2008 at 3.30 p.m. to 4.15 p.m.

Suhaimi Bin Yacob, Executive 2, Financing Division, Agro Bank, Jalan Padang Garong, Kota Bharu, Kelantan. Interview carried out on 14th December 2008 at 11.15 a.m. to 11.50 a.m.

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IS HALAL PRODUCTS ARE MORE EXPENSIVE AS PERCEIVED BY THE CONSUMERS? MUSLIMPRENUERS CHALLANGES AND OPPORTUNITIES IN ESTABLISHING A BLUE OCEAN PLAYING FIELD

Nuradli Ridzwan Shah Bin Mohd Dali & Mohammad Noorizzuddin Bin Nooh*

Abstract

Since Malaysia is heading towards being a global Halal hub, this research is very crucial to give ideas on the receptions of Muslims consumers towards Halal products and important for the Muslimpreneuers¹ to strategize their position in the globalized market. The objective of the research is to measure the perceptions of consumers towards Halal products particularly whether the products are perceived as more expensive as compared to the non Halal certified. Consumers' data were collected based on 1075 samples from Johor, Malacca, Selangor, Negeri Sembilan, Kuala Lumpur, Perak, Penang, and Pahang. There are six factors that contribute significantly to the perception that Halal products are more expensive than the non-Halal certified products. The factors are promotion, place, price, market demand, SME producers, and clean operation which later could be used in the four action framework in blue ocean strategy.

Keywords: Halal Product Pricing, Food Product, Malaysia, Factor Analysis, Logistic Regression, Blue Ocean Strategy.

* Lecturers at Universiti Sains Islam Malaysia.

¹ Muslimpreneuers are entrepreneurs who abide to the rules and regulation of *shariah* with the objective of achieving *falah maximization*, which are to be successful in the world and the world hereafter.

Introduction.

The blue ocean strategy is a new marketing strategy which becoming an attraction to the many people from various background such as marketing personnel, academicians, and policy makers CEOs of companies. Kim and Mauborgne (2007) of the blue ocean strategy have laid out the strategic foundations for the companies to survive in the business market by adopting contravene conventional marketing practice in the market place. The normal conventional strategy is either to produce products or services with added value or low price. The companies must choose either one strategy in competing with other competitors which enforcing the companies to be in a raging war. The marketing strategy gurus even develop strategies which are exactly the same as war tactical strategy such as guerilla attacks, front to front attack, flank attack and many more. The authors called the normal marketing strategy as the red ocean strategy where the red ocean translate the intense marketing competition between companies in the same industry offering homogeneous products attracting the same customers to buy their products or services (Kim and Mauborgne 2007).

In the blue ocean strategy, Kim and Mauborgne (2007) have laid out that instead of entering into the raging war, companies can escape from the war by creating uncontested market place, making the competition irrelevant, creating and capturing new demand, breaking the value and cost trade off, and aligning the whole system of a firm's activities with its strategic choice of differentiation and low cost. In formulating the blue ocean strategy, the authors have suggested that a strategy canvas is to be designed as a diagnostic tool for building a compelling blue ocean strategy. It captures the current state of play in the known market space that allows us to understand where the competition is currently investing, the factors the industry currently competes on in product, service and delivery and what customers receive from existing competitive offerings on the market.

Upon successfully understanding the current competition there are four actions framework that has to be implemented by the companies which are simplify as eliminate, reduce, raise and create. These four actions are directed in answering these four questions as described below:

1. Eliminate: Which of the factors that the industry takes for granted should be eliminated?
2. Reduce: Which factors should be reduced well below the industry's standard?
3. Raise: Which factors should be raised well above the industry's standard?
4. Create: Which factors should be created that the industry has never offered?

Six principles in blue ocean strategy are:

1. Reconstruct market boundaries
2. Focus on the big picture, not the numbers
3. Reach beyond existing demand
4. Get the strategic sequence right
5. Overcome key organizational hurdles
6. Build execution into strategy (Kim and Mauborgne 2007).

Literature Review.

Government's intention in making Malaysia as a global *Halal* hub has created a new playing field in which the participation of Muslims' SMEs is very much desired. The *Halal* hub will create opportunities for the Muslims SMIs to penetrate the *Halal* market such as the Middle East, the OIC countries and the rest of the world. At present, the business and commercial potential of the *Halal* industry is beyond doubt, with a market of 1.6 billion Muslims and an estimated market size of more than US\$600 billion (RM2.1 trillion). According to Federal Agricultural Marketing Authority (FAMA), the market size for frozen food only will increase to RM193 billion in 2010. It is because the total population of Muslims in the world was increased 3 percent a year (*Berita Harian*, 1 February 2003). However, the *Halal* products in the market still small and is not sufficient to cater the demand.

The demand for *Halal* food is on the rise due to greater awareness among Muslims on their responsibility to consume only *Halal* food. Coincidentally, global awareness on how important is food safety, which has been associated with *Halal* food, has arisen. With the advanced technology, it is now possible to analyze the contents of food products with speed and accuracy. In addition, *Halal* certification, which provides assurance on quality and wholesomeness, results in the increase in demand for such products.

Malaysia is currently in a strategic position to be a leading player in the global *Halal* business. Accordingly, the Malaysian Government has undertaken measures to support the development of *Halal* industry as identified in the Second Industrial Master Plan (1996-2005) and The National Agriculture Policy (1998-2010). In tandem with Government's call to make Malaysia as the *Halal* hub, the State Government of Selangor, Kedah, Malacca, Negeri Sembilan, Perak and Pahang have established industrial *Halal* parks in their respective states.

Halal and Haram Concept.

Halal is a *Quranic* word meaning lawful or permitted. In reference to food, it is the dietary standard, as prescribed in the *Quran* the Muslim scripture. General *Quranic* guidance dictates that all foods are *Halal* except those that are specifically mentioned as *Haram* (unlawful or Prohibited). The *Al-Quran* mentioned:

"O ye who believe! Eat of the good things wherewith We have provided you and render thanks to Allah, if it is He whom we worship"

Surah Al-Baqarah: 172

The unlawful foods are specifically mentioned in the Glorious *Quran*, in the following verses:

"Forbidden to you is anything that dies by itself, and blood and pork, as well as whatever has been consecrated to something besides Allah, and whatever has been strangled, beaten to death, trapped in a pit, gored, and what some beast of prey has begun to eat, unless you give it the final blow; and what has been slaughtered before some idol, or what you divide up in a raffle; (all) that is immoral!..."

Surah Al-Ma'idah:3

In general, to determine the *Halal-Haram* status of foodstuffs and other material, Islam has laid general guidelines on this matter, namely:

- 1) All raw materials and ingredients used must be *Halal*.
- 2) Naturally *Halal* animals such as cattle, goats etc., must be slaughtered according to Islamic rites, the rituals specify that the act must be performed by a mentally sound Muslim, to sever the blood and respiratory channels of the animal, using a sharp cutting tool such as knife.
- 3) The *Halal* ingredients must not be mixed, or come into contact with *Haram* materials such as products from pig or dog during storage, transport, cooking, serving etc. It must be understood that the production of *Halal* food is not only beneficial to Muslims, but also to food producers, by means of increased market acceptance of their products.

Islam is the natural way of life. Its economical system is just; its social system is based on cooperation and brotherhood; its political system is based on consultation and its dietary laws are very simple and beneficial for the entire humanity. The life of a Muslim revolves around the concept of *Halal*. A Muslim must earn income from *Halal* sources, be involved only in *Halal* transactions and consume *Halal* food and drink. The concept of *Halal* in Islam has very specific motives;

- 1) To preserve the purity of religion
- 2) To safeguard the Islamic mentality
- 3) To preserve life
- 4) To safeguard property
- 5) To safeguard future generations
- 6) To maintain self-respect and integrity.

Branding.

Branding is an act in which an organization uses a name, phrase, design, symbols, or combination of these to identify its products and distinguish them from those of competitors, while brand name is any word, 'device' (design, sound, shape, or color), or combination of these used to distinguish a seller's goods or services (Berkowitz, 1997). Branding can contribute towards enhancing the competitiveness of the country's goods and services. Strong brand can create an identity for Malaysia by differentiating Malaysian products and services in the global market. It involves developing a branding culture throughout the organization and requires commitment in investing towards building a lifetime relationship with the consumer. *Halal* certification can be a benchmark for *Halal* products and distinguish it from other competitors.

According to Kotler, P & Armstrong, G (2006), a brand is a name, term, sign, symbol, or design, or a combination of these, that identifies the maker or seller of a product or service (Kotler, P & Armstrong, G 2006). Consumers view a brand as an important part of a product, and branding can add value to a product. For example, Darlie and Colgate is toothpaste and Pampers is a diaper. Brand is very important to promote and sell a product. Brands are more than just names and symbols.

Brands represent consumers' perceptions and feeling about a product and its performance. Everything that the product or service means to consumers. Thus, the real value of a strong brand is its power to capture consumer preference and loyalty. A powerful brand has high brand equity. Brand equity is the positive differential effect that knowing the brand name has on customer response to the product or service. A measure of a brand's equity is the extent to which customers are willing to pay more for the brand. Roland.T. R *et.al* (2004) found that 72 percent of customers would pay a 20 percent premium for their brand of choice relative to the closest competing brand whereas 40 percent said they would pay a 50 percent premium (Roland.T. R *et.al*, 2004).

There are a few reasons why brands are important, firstly; brands have never been more important than they are today. Given the proliferation of products and services in the global marketplace brought about by the ongoing liberalization in the international trading environment, developments in ICT and rapid changes due to globalization, consumers today have a wide choice of products and services to choose from. It is thus important that we develop and promote Malaysian own brand names to differentiate the country's products and services in the marketplace (MATRADE, 2004).

Secondly, in the world of parity where everything tends to be equal, and the world marketplace is a world of commodities, brands differentiate products. The availability of new technologies has enabled companies to easily replicate the products, systems, services and processes of others, generating major strategic problems for businesses in differentiation. Added to this problem is the rapidly decreasing life cycle of products, in some cases now down to a matter of weeks (MATRADE, 2004). On the other hand, *Halal* branding is defines *Halal* as a cross-over brand that has demonstrated the ability to attract Muslims and non-Muslims alike (Abdalhamid Evans, The *Halal* Journal, 2006). According to Mohd. Nakhaie, things that are lawful in Islamic religion are termed as *Halal* and if they are unlawful then they are classified as *Haram* (Mohd Nakhaie, 2005).

In Malaysia, a few researches have been done on *Halal* product such as Azrina (2006); Rosly *et al.* (2006) and Nuradli *et.al* (2007). According to Azrina (2006) although Malaysian's awareness towards local or domestic product have been proven as increasing, however their awareness are still low compared to other countries such as Indonesia and Thailand. The main factor that contribute to this situation is because lack of information on most of the product in the markets. Even some consumers claimed that the products although with *Halal* logos are still unconvincing. These issues have been further aggravated when often we can read in the newspaper regarding the issue of mismanagement of the *Halal* logo. Due to the phenomenon above, the researchers would like to measure the awareness of the consumers thus proposing a suitable concept in promoting local *Halal* products.

Rosly *et.al* (2006) in their studies in gauging the customers' attitude towards *Halal* food status in Penang found that customer's attitude towards *Halal* logo was generally favorable with a mean of 3.978. 40% of the respondents will not buy food products that do not have *Halal* logo. Based on the percentage and the sample population, it is shocking that even though sample population is comprised of Muslims, the percentage of them buying food products that display *Halal* logo is very low. The researchers used two methods which are the questionnaire method and the observational method. When the researchers observed these sample populations purchasing behavior, only 18% of them actually looked at the products labels and half of those actually read the label before deciding to purchase the products.

This statistics again shows that the stereotypes of Muslims will always look for *Halal* products and services are on the opposite. This phenomenon can happen as a result of living in a Muslim country where Muslims have become complacent by assuming that all the products and services produced, manufactured or sold in this country is *Halal* by nature unless being told otherwise by the relevant authorities.

Nuradli *et al.* (2007) in a research conducted online concluded that female consumers are more concerned that all food and other consumer products should obtain the *Halal* verification from JAKIM as compared to the male respondents at 5% significant level. A significant finding of the research is that the Indians disagree with the idea of having other than JAKIM to become the authority to come up with the *Halal* certification.

Shahidan and Md Nor (2006) found some issues and challenges on implementation of *Halal* certification which are the inconsistency of definition of *Halal* on the aspect of slaughtering of animal, the introduction of *Halal* logo by individual firms, the use of Arabic-sounded of Islamic-signaled brand names, the rampant display of *Quranic* verses by food operators to indirectly signal that the premise is operated by Muslim and that it offers *Halal* foods and the lack of enforcement by the authorities with regards to the misuse of *Halal* logos. The main challenge faces by the government is in the area of enforcement where there is lack of enforcement by the Department of Islamic Development's (JAKIM) in monitoring the usage of certified *Halal* logo that caused the public to question the validity on some of the products or services claiming to be *Halal*. In addition, the lack of collaboration amongst the world's *Halal* certification authorities has created "doubts" amongst the Muslims consumers on the authenticity of the *Halal* certification process.

Methodology.

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Methodology.

Halal products and services cover a wide spectrum of product and service lines ranging from insurance, financial products, food, and also personal hygiene products. For this particular study, emphasis will be given only to the food and beverages industry because when discussing about Halal, this particular industry will be the first to be analyzed and scrutinized.

The method of sampling is through cluster sampling based on locations with high purchasing power. The choice of locations is made based on the purchasing power that these sample have. This is because when the purchasing power is significantly high, the consumers will have a lot of choices to be made in terms of purchase decision. Thus samples from these selected locations are believed to be significant to best represent the Malaysian overall market.

According to the data from Household Income Survey (2004) there are 8 states that fall under those particular categories namely Perak, Pulau Pinang, Melaka, Negeri Sembilan, Selangor, Wilayah Persekutuan Kuala Lumpur, Johor and Pahang. The numbers of the sample which have been collected are 1075 respondents

The questionnaires are divided into three main sections namely demographics of the population, the level of awareness towards *Halal* as a brand and the perception of the consumers towards *Halal* product using 5-point Likert scales. Factor analysis was used to determine the factors that influence the consumers to buy *Halal* products. Furthermore, the questionnaire is designed in the native language to ensure that the respondents understand the questions being asked. A pilot survey is conducted to check on the reliability and validity of the questionnaire before the final survey was conducted.

There will be two analysis methods that are used in this research. Factor analysis will be used to reduce and group the independent variables whereas logistic regression will be used subsequently to analyze the relationship between the categorical dependent variable with the independent variables found in the factor analysis.

Exploratory factor analysis (EFA) seeks to uncover the underlying structure of a relatively large set of variables. The researcher's *à priori* assumption is that any indicator may be associated with any factor. This is the most common form of factor analysis. There is no prior theory and one uses factor loadings to intuit the factor structure of the data. The main applications of factor analytic techniques are: (1) to *reduce* the number of variables and (2) to *detect structure* in the relationships between variables, that is to *classify variables*. Therefore, factor analysis is applied as a data reduction or structure detection method (the term *factor analysis* was first introduced by Thurstone, 1931). Factor analysis is a correlation technique to determine meaningful clusters of shared variance. Factor analysis begins with a large number of variables and then tries to reduce the interrelationships amongst the variables to a few numbers of clusters or factors. Factor analysis finds relationships or natural connections where variables are maximally correlated with one another and minimally correlated with other variables and then groups the variables accordingly. After this process has been done many times a pattern appears of relationships or factors that capture the essence of all of the data emerges. Therefore factor analysis refers to a collection of statistical methods for reducing correlational data into a smaller number of dimensions or factors

Logistic regression is a form of regression which is used when the dependent is a dichotomy and the independents are of any type (Alan Agresti, 1996). Continuous variables are not used as dependents in logistic regression. Unlike logit regression, there can be only one dependent variable. Logistic regression can be used to predict a dependent variable on the basis of continuous and/or categorical independents and to determine the percent of variance in the dependent variable explained by the independents; to rank the relative importance of independents; to assess interaction effects; and to understand the impact of covariate control variables.

Logistic regression applies maximum likelihood estimation after transforming the dependent into a logit variable (the natural log of the odds of the dependent occurring or not). In this way, logistic regression estimates the probability of a certain event occurring (Imam Ghozali, 2006). Logistic regression has many analogies to OLS regression: logit coefficients correspond to b coefficients in the logistic regression equation, the standardized logit coefficients correspond to beta weights, and a pseudo R² statistic is available to summarize the strength of the relationship. Unlike OLS regression, however, logistic regression does not assume linearity of relationship between the independent variables and the dependent, does not require normally distributed variables.

Press *et al.* (1978) make the case for the superiority of logistic regression for situations where the assumptions of multivariate normality are not met a compared to multiple discriminant. They conclude that logistic and discriminant analyses will usually yield the same conclusions, except in the case when there are independents which result in predictions very close to 0 and 1 in logistic analysis (Press, S. J. and S. Wilson, 1978). Logistic regression also does not assume homoscedasticity, and in general has less stringent requirements. It does, however, require that observations are independent and that the independent variables be linearly related to the logit of the dependent. The success of the logistic regression can be assessed by looking at the classification table, showing correct and incorrect classifications of the dichotomous, ordinal, or polytomous dependent. Also, goodness-of-fit tests such as model chi-square are available as indicators of model appropriateness as is the Wald statistic to test the significance of individual independent variables. .

Research hypothesis:

Ho = There is no relationship between the food products with *Halal* certification are generally more expensive than without the *Halal* certification and independent variables (factoring groups)

H1 = There are relationships between the food products with *Halal* certification are generally more expensive than without the *Halal* certification and independent variables (factoring groups)

Group	Halal	Non-Halal	Total
1	10	10	20
2	15	15	30
3	20	20	40
4	25	25	50
5	30	30	60
6	35	35	70
7	40	40	80
8	45	45	90
9	50	50	100
10	55	55	110
11	60	60	120
12	65	65	130
13	70	70	140
14	75	75	150
15	80	80	160
16	85	85	170
17	90	90	180
18	95	95	190
19	100	100	200
20	105	105	210
21	110	110	220
22	115	115	230
23	120	120	240
24	125	125	250
25	130	130	260
26	135	135	270
27	140	140	280
28	145	145	290
29	150	150	300
30	155	155	310
31	160	160	320
32	165	165	330
33	170	170	340
34	175	175	350
35	180	180	360
36	185	185	370
37	190	190	380
38	195	195	390
39	200	200	400
40	205	205	410
41	210	210	420
42	215	215	430
43	220	220	440
44	225	225	450
45	230	230	460
46	235	235	470
47	240	240	480
48	245	245	490
49	250	250	500
50	255	255	510
51	260	260	520
52	265	265	530
53	270	270	540
54	275	275	550
55	280	280	560
56	285	285	570
57	290	290	580
58	295	295	590
59	300	300	600
60	305	305	610
61	310	310	620
62	315	315	630
63	320	320	640
64	325	325	650
65	330	330	660
66	335	335	670
67	340	340	680
68	345	345	690
69	350	350	700
70	355	355	710
71	360	360	720
72	365	365	730
73	370	370	740
74	375	375	750
75	380	380	760
76	385	385	770
77	390	390	780
78	395	395	790
79	400	400	800
80	405	405	810
81	410	410	820
82	415	415	830
83	420	420	840
84	425	425	850
85	430	430	860
86	435	435	870
87	440	440	880
88	445	445	890
89	450	450	900
90	455	455	910
91	460	460	920
92	465	465	930
93	470	470	940
94	475	475	950
95	480	480	960
96	485	485	970
97	490	490	980
98	495	495	990
99	500	500	1000

Analysis of the findings.

Reliability Test.

Reliability test is conducted using Cronbach Alpha. Using reliability analysis, the questionnaire can be determined the extent to which they are related to each other. The overall index of the repeatability or internal consistency of the scale as a whole would be generated and identification of problem items that should be excluded from the scale can be identified.

Table 4.1.1: Reliability Test Using Cronbach Alpha

Reliability Coefficients	
N of Cases = 1075	N of Items = 45
Alpha = .825	

The Reliability Test for the questionnaires as shown in the table above measures the Cronbach's Alpha is 0.825. Therefore the Cronbach's Alpha is showing internal inconsistency and therefore reliable because it is higher than 0.70 (Nunnally, 1970).

Section B: Respondents' Demographic Profiles

Table 4.2.1: State of Residence

State	Frequency	Percent
Johor	195	18.1
Selangor	181	16.8
Pahang	163	15.2
Perak	120	11.2
Wilayah Persekutuan KL	112	10.4
Pulau Pinang	97	9
Negeri Sembilan	59	5.5
Melaka	37	3.4
Kelantan	36	3.3
Kedah	31	2.9
Terengganu	30	2.8
Perlis	4	0.4
Sabah	3	0.3
Sarawak	3	0.3
Brunei	2	0.2
Labuan	1	0.1
Putrajaya	1	0.1
Total	1075	100

The largest respondents from the survey are from Johor comprises approximately 18.1% from the total of 1075 respondents followed by Selangor 16.8%, Pahang 15.2%, Perak 11.2% and Kuala Lumpur 10.4%. The rest of the states are below than 10 percent with the lowest from Putrajaya and Labuan. There are also 2 respondents from Brunei Darussalam which comprises about 0.2% from the total respondents.

Table 4.2.2: Gender

		Frequency	Percent	Valid Percent
Valid	Male	450	41.9	41.9
	Female	625	58.1	58.1
	Total	1075	100.0	100.0

Majority of respondents are female which are approximately 625 respondents or 58.1% from the total respondents. The remaining of 450 respondents are male or about 41.9%.

Table 4.2.3: Race

		Frequency	Percent
Valid	Malay	1000	93.0
	Chiness	38	3.5
	Indian	23	2.1
	Others	14	1.3
	Total	1075	100.0

We have managed to collect data from various races to get multi ethnic responses on the *Halal* certification issues. The majority is Malay which turn out approximately 1000 respondents or 93%, Chinese about 38 respondents or 3.5%, Indian about 23 respondents and others about 14 respondents. The non-Malays respondents are small since they are not ready to answer the *Halal* certification issues perhaps due to their misconception on the possible complication regarding about the issues.

Table 4.2.4: Religion

		Frequency	Percent
Valid	Islam	1010	94.0
	Buddhist	28	2.6
	Christian	18	1.7
	Others	19	1.8
	Total	1075	100.0

Majority of respondents are Muslim which are about 94% and the rest are Buddhist, Christian and Hindu.

Table 4.2.5: Age

		Frequency	Percent
Valid	18 to 24	354	32.9
	25 to 34	416	38.7
	35 to 44	161	15.0
	45 to 54	112	10.4
	55 and above	32	3.0
	Total	1075	100.0

Almost 39% of respondents are from the range of 25 until 34 years old which is the highest group of respondents in this survey followed by from the age 18 until 24 about 32,9%. Respondents from 35 to 44 years old are about 161 respondents and from 45 to 54 are about 112 respondents. The lowest number of respondents come from the range 55 and above which comprises only 32 respondents or 3 percent.

Table 4.2.6: Marital Status

		Frequency	Percent
Valid	Single	523	48.7
	Married	539	50.1
	Divorce	13	1.2
	Total	1075	100.0

The marital status from the single and married respondents are almost the same with a difference of about 1.4% only while divorced respondents comprises about 1.2 percent only from the total 1075 respondents.

Table 4.2.7: Occupation

	Frequency	Percent
Government sector	447	41.6
Private sector	253	23.5
Others	236	22
Entrepreneurs/Business	92	8.6
Industry/Manufacturing	47	4.4
Total	1075	100

Majority of respondents are from the government sector which are about 41.6% or 447 respondents while 23.5 % come from the private sector. 22% are retirees, Felda settlers, housewife and students, 8.6% are entrepreneurs and the remaining is from the manufacturing sector.

Table 4.2.8: Qualification

Education Level	Frequency	Percent
Diploma/STPM/Certificate	321	29.9
Bachelor Degree	307	28.6
SPM	288	26.8
PhD/Postgraduate	103	9.6
Others:SRP;Form1;Standard6	35	3.3
Professional	21	2
Total	1075	100

Majority of the respondents have diploma (29.9%), followed by bachelor degree about 28.6%, SPM holders about 26.8% and remaining are having postgraduate degree, SRP or professional certificates.

Table 4.2.9: Monthly Household Income

		Frequency	Percent
Valid	Less than RM1,500	486	45.2
	RM1,501 to RM3,000	305	28.4
	RM3,001 to RM4,500	139	12.9
	RM4,501 to RMRM6,000	80	7.4
	RM6,001 and above	65	6.0
Total		1075	100.0

Majority of respondents have a household income lower than RM1500 about 45.2%. 28.4% have a household income in between 1501 to RM3000. 12.9% have a household income in between RM3001 until RM4500 and the remaining 13.4% have a household income more than RM4500.

Factor Analysis.

Factor analysis attempts to identify underlying variables, or factors, that explain the pattern of correlations within a set of observed variables. Factor analysis is often used in data reduction to identify a small number of factors that explain most of the variance observed in a much larger number of manifest variables. Factor analysis can also be used to generate hypotheses regarding causal mechanisms or to screen variables for subsequent analysis (for example, to identify collinearity prior to performing a linear regression analysis). In this analysis, the factor analysis procedure using the varimax rotation would be used in order to identify the questions that could be grouped together which influence the *Halal* certification. Furthermore, the reduction of data or uncorrelated questions would reduce the variables used in future analysis.

Table 4.3.1: KMO and Bartlett's Test

Kaiser-Meyer-Olkin Measure of Sampling Adequacy		.866
Bartlett's Test of Sphericity	Approx. Chi-Square	14301.101
	Df	990
	Sig.	.000

Table 4.3.2: Total Variance Explained

Component	Initial Eigenvalues			Extraction Sums of Squared Loadings			Rotation Sums of Squared Loadings		
	Total	% of Variance	Cumulative %	Total	% of Variance	Cumulative %	Total	% of Variance	Cumulative %
1	5.870	13.044	13.044	5.870	13.044	13.044	4.666	10.37	10.368
2	4.996	11.102	24.146	4.996	11.102	24.146	3.863	8.583	18.952
3	2.799	6.219	30.365	2.799	6.219	30.365	3.291	7.313	26.264
4	2.258	5.018	35.383	2.258	5.018	35.383	3.004	6.675	32.939
5	1.855	4.122	39.505	1.855	4.122	39.505	1.706	3.791	36.730
6	1.278	2.841	42.346	1.278	2.841	42.346	1.495	3.322	40.052
7	1.241	2.757	45.103	1.241	2.757	45.103	1.492	3.316	43.368
8	1.189	2.642	47.745	1.189	2.642	47.745	1.372	3.050	46.418
9	1.097	2.437	50.182	1.097	2.437	50.182	1.348	2.995	49.413
10	1.084	2.409	52.592	1.084	2.409	52.592	1.269	2.820	52.233
11	1.006	2.236	54.828	1.006	2.236	54.828	1.168	2.595	54.828

Extraction Method: Principal Component Analysis.

Based on the total variance, there are 11 factors were extracted because the eigenvalues is higher than 1 for the respective factors. Based on the extraction it is noted that factor 1 could explain (13.044%), factor 2 (11.102%), factor 3 (6.219%), factor 4 (5.018%), factor 5 (4.122%), factor 6 (2.841%), factor 7 (2.757%), factor 8 (2.642%), factor 9 (2.437%), factor 10 (2.409%) and factor 11 (2.236%) of the variation. The total 11 factors could only explain 54.28% of the total variations.

Based on the varimax rotated components, the factors could be extracted to 11 factors based on the factor loadings which are higher than 0.5. The Cronbach alpha is analyzed and the result is 0.806 which is reliable and consistent. Based on the factor analysis we could regroup the factors to 11 groups with the subheadings as listed below.

Factor 1	Promotion
Factor 2	Place
Factor 3	Attractive And Quality
Factor 4	Halal Certification
Factor 5	Price
Factor 6	Product Samples
Factor 7	Market Demand
Factor 8	Sme Producers
Factor 9	Halal Certification To Muslim Companies
Factor 10	Difference Between Halal Certified And Non Certified
Factor 11	Clean Operation

From the above analysis there are 11 factors that could influence the customers to buy *Halal* products. However, the result could not be used to indicate whether the consumers perceived that the *halal* products would be expensive as compared to the un-certified products. Therefore further analysis is conducted to identify whether the 11 factors significantly contribute to the consumers perception on the price of halal products. Logistic regression is used to compare between consumers who perceived that *halal* products are more expensive or not.

Logistic Regression for Halal Certification

This analysis is conducted to identify the factors which contribute to the consumers perception on food products with *Halal* certification are generally more expensive than without the *Halal* certification using logistic regression. In identifying the groups of consumers who perceived halal products are generally more expensive than the non-certified food products, the researchers included a question in the survey asking the consumers perception whether they believe that with *halal* certification the food products would be expensive or not. The consumers who believe that food products with Halal certification are generally more expensive than without the *Halal* certification will be categorized as 1 and the consumers who believe that Food products with Halal certification are generally cheaper than without the Halal certification will be categorized as 0.

In assessing the model fitness, Hosmer and Lemeshow test is conducted. The hypothesis for the testing the model fitness is as follows:

Ho = The hypothesized model is fit with the data

H1 = The hypothesized model is not fit with the data

The Hosmer and Lemeshow test result is as follows:

The above result fa
the hypothesized n

Table 4.4.1: Foo

Observed
Food products wi Halal certification are generally mor expensive than without the Halal certification
Overall Percenta

a. The cut value is
Based on the class
on the above tabl
certification are g
in the prediction
is about 95.2%.
Halal certification
observation but th
98.0%. The overa

Hosmer and Lemeshow Test

Step	Chi-square	DF	Sig.
1	3.902	8	.866

The above result failed to reject the null hypothesis, therefore we accept the null hypothesis and the hypothesized model is fit with the data.

Table 4.4.1: Food Products with Halal Certification Are Generally More Expensive Than without the Halal Certification

Observed		Predicted		
		Food products with Halal certification are generally more expensive than without the Halal certification		Percentage Correct
		.00	1.00	
Food products with Halal certification are generally more expensive than without the Halal certification	.00	817	41	95.2
	1.00	89	128	59.0
Overall Percentage				87.9

a. The cut value is .500

Based on the classification 2 X 2 table, it shows the correct and incorrect estimation value. Based on the above table it is noted that 858 respondents who believe that food products with *Halal* certification are generally cheaper than the one without *Halal* certification in the observation but in the prediction there are only 817 respondents. Therefore the accuracy of the classification is about 95.2%. In contrary, there are 217 respondents who believe that Food products with *Halal* certification are generally more expensive than the one without *Halal* certification in the observation but there are only 128 respondents in the prediction. Therefore the accuracy is about 59.0%. The overall accuracy for both is approximately 87.9%.

Table 4.4.2 Variables in the Equation for Food Products with Halal Certification Are Generally More Expensive Than without the Halal Certification

		B	S.E	Wald	df	Sig.	Exp(B)	95.0% C.I.for EXP(B)	
								Lower	Upper
Step 6	Promotion	.352	.105	11.278	1	.001	1.423	1.158	1.747
	Place	-.231	.106	4.748	1	.029	.793	.644	.977
	Price	2.224	.158	198.853	1	.000	9.243	6.785	12.590
	Market demand	.774	.123	39.842	1	.000	2.168	1.705	2.756
	SME producers	.782	.119	43.194	1	.000	2.185	1.731	2.759
	Clean operation	-.303	.102	8.774	1	.003	.739	.604	.903
	Constant	-2.567	.160	255.746	1	.000	.077		

Based on the above logistic regression result, it could conclude that food products with *Halal* certification are generally more expensive than without the *Halal* certification could be given by the following logistic model. There six independent variables factors that are significant in influencing whether the food products with *Halal* certification are generally more expensive than without the *Halal* certification are:

$$\ln p/1-p = -2.567 + 0.352 (\text{Promotion})^* - 0.231 (\text{Place})^* + 2.224 (\text{Price})^* + 0.774 (\text{Market demand})^* + 0.782 (\text{SME producers}) - 0.303(\text{Clean Operation})^*$$

Or

$$p/1-p = e^{-2.567 + 0.352 (\text{Promotion})^* - 0.231 (\text{Place})^* + 2.224 (\text{Price})^* + 0.774 (\text{Market demand})^* + 0.782 (\text{SME producers}) - 0.303(\text{Clean Operation})^*}$$

The six factors that significantly contribute to the food products with *Halal* certification are generally more expensive than without the *Halal* certification are promotion, place, price, market demand, SME producers, and clean operation. These factors could be used in the four actions framework in blue ocean strategy is suggested as follows:

Table 4.4.3 Blue Ocean Strategy Four Action Framework

Eliminate		Reduce	
Market demand/competition/market size		Price Unnecessary Promotion	
Raise		Create	
SME Producers Place Clean Operation		Unique value (Halal)	

Discussions.

All the 11 factors were determined using the factor analysis procedures and could be further analyzed in future research. The 11 factors identified are promotion, place, attractive and quality, Halal certification, price, product samples, market demand, SME producers, Halal certification to Muslim companies, difference between Halal certified and non certified and clean operation. It is recommended for the policy makers and Halal products marketers to take into consideration all the 11 factors that could influence the consumer behaviors. However there are only six factors that contribute significantly to the consumer perceptions that food products with Halal certification are generally more expensive than without the Halal certification positively and negatively. The factors are promotion, place, price, market demand, SME producers, and clean operation.

Managerial Implications.

The Halal certification could benefits the producers if it could be able to eliminate competition and create a blue ocean strategy by using the four actions framework. Eliminating the dependencies of the demand for the Halal product on the size of the market will enable Halal producers to focus on the niche Halal certified market. The Halal producers must also offer a reasonable price and in the same time create a unique value (Halal Branding) or higher service quality.

In addition, the Halal producers also must increase its capability from cottage industry or small business to become SME producers so that it could benefit the large economies of scale while increasing distribution of products by increasing the numbers of kiosks and small outlets and increase the quality of products by operating in a clean operational environment.

The small businesses in Malaysia could be transformed to become global SME producers for *Halal* food product using the blue ocean strategy by creating added value and low cost in order to avoid the normal conventional way of intense competition. The escapism of the normal competition would foster the growth of the small business in Malaysia to be competitive in the global setting.

Future Recommendation.

This research is exploratory in nature and it dealt on the surface of the consumers behaviors in halal industry. It would be beneficial if future research could employ qualitative research in getting deepen explanation on the consumers' behaviors and investigating the natural phenomenon of consumers' attitudes towards halal products. In addition, future research should also be conducted on the impacts of culture, ethnic and religion in relationship with the attitudes towards halal products. In addition, as the world market is merging or becoming a common market as the impact of globalization, research on halal products or industry in the global context is recommended.

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MOTIVATIONS BEHIND FIRMS' SHARE REPURCHASES

Shafina Fisal*

Abstract

Malaysia's share repurchase regulations were initiated in 1997 as a recovery strategy to stabilize the stock market due to the 1997 financial crisis. Since the passing of the Act, there has been a tremendous growth in the volume of share repurchase activities where past research showed that stabilizing stock prices was one of the dominant reasons why firms repurchase their shares. Now that a decade has passed and that Malaysia is over with the 1997 financial crisis, the increasing popularity of share repurchase activities among the Malaysian firms should be motivated by other reasons other than to stabilize stock prices. In fact, the literature on why firms repurchase their stock continues to evolve, presenting a mixed understanding of the economic role of repurchases. In this paper, an academic review of this literature is provided to ultimately shed light on economists' collective understanding of why firms undertake share repurchases.

Keywords: *Share repurchases, economic motivations.*

* Lecturer at Department of Banking and Finance, Faculty of management and muamalah Selangor International Islamic University College (SIUC)

Introduction.

Share repurchase is a corporate event which basically refers to a firm buying back its own shares from the market. It has now become a common and popular alternative to the conventional dividends as a form of corporate payout where firms distribute excess cash in returning capital to their shareholders. Its popularity began in the United States (US) market in the early 1980s, particularly fueled by open market repurchases (OMRs) and this surge in activity soon spread across to other developed countries like United Kingdom (UK) and Canada in the 1990s. In fact, globally, a host of other countries that formerly prohibited share repurchases also started to legalize share repurchase activities, for example Japan in 1995, Finland and Malaysia in 1997, Germany, Singapore and France in 1998, India, Norway and South Africa in 1999, Denmark, Sweden and Taiwan in 2000 etc. Hence, it is the intention of this paper to provide an academic review of this literature so as to present economists' collective understanding of why firms buy back their shares. The remainder of the paper is organized as follows. Section 2 provides an overall view of the repurchase activity in Malaysia since its initiation in 1997. Section 3 presents the theories behind share repurchases and section 4 concludes the paper.

Open Market Share Repurchases (OMRs) in Malaysia.

Before 1st September 1997, companies in Malaysia were generally not allowed to buy their own shares. Such prohibition as argued by Lim and Bacha, (2002) was probably premised on the potential conflicts of interests that could arise in that if stock prices reflect the collective judgment of markets on management, this would enable management to engage in price support which in turn could lead to value destruction.

Hence, it was not until September 1997 during the financial crisis which brought about the collapse of the stock market and asset prices that the Registrar of Companies (ROC) allowed the Malaysian companies to engage in share buybacks. The 1997 Asian financial crisis adversely affected the Malaysian ringgit which led to a 30% devaluation of the currency against the US dollar, and which subsequently led to the collapse of the stock market and asset prices in which the Kuala Lumpur Composite Index (KLCI) plunged 58% from its high for that year (Zainudin and Regupathi, 2003), falling from a level of 1277 in February 1997 to 512.41 in November 1997. It was viewed that the government interference in the Malaysian stock market through the legalization of repurchase activities was one of the recovery strategy to revive and stabilize the stock market which was put in force within three months when share prices in the Kuala Lumpur stock exchange fell sharply in June, 1997. In fact, Grullon and Ikenberry (2000) found evidence that repurchasing program announcements are inversely related to market movements; implying that when stock prices fall, repurchase announcements rise, as reflected in the 1987 market crash as well as the 1998 market disturbance stemming from trouble in the global bond markets.

Since the passing of the Companies (Amendment) Act 1997, share buyback activities have become a new phenomenon in the Malaysian market. It has always been the norm for companies to repurchase their shares, which were probably vague as to the reasons. To learn about the significance of share repurchases in the US where buybacks have become a widespread practice of buyback activities.

According to Salama (2000), there were 16 companies that announced share repurchases, 16 companies that actually repurchased shares (1999). And according to Lim and Bacha (1999), 16 board companies and 5 companies actually repurchased shares (Table 1 and 2).

Table 1: Breakdown of K...

Breakdown
Announced/Obtained s
EGM
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Table 2: Breakdown by

Breakdown by Year	Ma Co
1997	
1998	
1999	
2000	
2001#	
Total	

Sources : Data from KL... # indicates the period fr

Since the passing of the Malaysia's share repurchase regulations under Section 67A of the Companies (Amendment) Act 1997, there has been a tremendous growth in the volume of share buyback activities among the Malaysian firms. Still, share repurchasing is still considered a new phenomenon in that the buyback mechanism did not catch on until much later as it has not always been the norm for companies to repurchase their shares and that firms in the initial stage were probably vague as to the benefits of share repurchases. As firms over the years began to learn about the significance of share repurchases, especially from more mature markets such as the US where buybacks have been ongoing for about two decades since 1982, there has been a spree of buyback activities among the Malaysian firms ever since.

According to Sabri (2003), until 1999, out of 171 companies that had received approval for share repurchases, 16 companies had implemented the targeted repurchased shares (ROC, 1999). And according to Lim and Bacha, (2002), until 2001, 43 companies, consisting of 38 main board companies and 5 second board companies had actually repurchased their shares (Refer Table 1 and 2).

Table 1: Breakdown of KLSE Listed Companies involved in Open Market Repurchases

Breakdown by Type	Main Board Companies	Second Board Companies	Total
Announced/Obtained shareholders' approval at EGM/AGM	112	19	131
Actually repurchased shares	38	5	43

Table 2 : Breakdown by Year of Companies that Executed Open Market Repurchases

Breakdown by Year	Main Board Companies	Second Board Companies	Total	Cumulative Total
1997	1	0	1	1
1998	11	3	14	15
1999	11	0	11	26
2000	9	1	10	36
2001#	6	1	7	43
Total	38	5	43	

Sources : Data from KLSE.

indicates the period from January 1 up to June 30, 2001.

In 2002, 36 repurchasing firms implemented share repurchase programs and this grew to 149 firms in 2006. Additionally, in 2002, share repurchase volume was 119.913 million shares and this grew to approximately 6.258 billion shares in 2006.

There are various methods of share repurchasing which are tender offer repurchase (where the firm specifies a price at which the firm will buy back its shares, the number of shares it intends to buy and the period of time for which the offer will be kept open), Dutch-auction tender offer (where the firm specifies a range of prices from which the shares would be repurchased), privately negotiated repurchase (where the firm buys back shares from a large shareholder(s) at a negotiated price) and the open market repurchase (OMR) where the firm buys back shares in the open market at the prevailing market price.

Out of the above mentioned repurchasing methods, Malaysia practices the OMRs as stipulated by Bursa Malaysia's Chapter 12 Share Buy-backs Listing Requirements, which allows only the OMR option where repurchases must only be effected on the market of the exchange. "on the market" refers to transactions that are to be made through the Automated Trading System of the Bursa Malaysia and excludes any forms of direct business transactions.

Motivations behind Firms' OMRs.

Firms have two alternatives for deploying capital, i.e. by reinvesting into the business via mergers and acquisitions, capital expenditures and working capital or by returning capital to shareholders through dividends and share repurchases. As suggested by Asquith and Mullins (1986), returning capital to shareholders with differing cash payout policies present one of the most puzzling and disturbing issues in corporate finance, particularly when share repurchase programs have now become increasingly more popular vis-a-vis the traditional dividend payout as a form of cash distribution to shareholders (Grullon and Michealy, 2002).

Based on past literatures, several hypotheses have been advanced in the literature to explain what motivate firms to initiate share repurchase programs and among them are the information signaling hypothesis where firms repurchase to signal optimistic information about their future operating and cash performance prospects (Dann, 1981; Vermaelen, 1981 and 1984; Ofer and Thakor, 1987 and Constantinies and Grundy, 1989), the market undervaluation signaling hypothesis where firms repurchase to signal that their current stock price is below their intrinsic value (Comment and Jarrell, 1991 and Ikenberry, Lakonishok and Vermaelen (1995), the agency costs of the free cash flow hypothesis where firms repurchase to mitigate potential problems of unmonitored spending of excess cash on unprofitable projects (Easterbook, 1986 and Jensen, 1986).

the capital structure adjustment hypothesis where firms repurchase shares to adjust their financial leverage towards an optimal leverage ratio, thereby allowing firms to benefit from tax advantages of debt financing (Bagwell and Shoven, 1989 and Hovakimian, Opler and Titman, 2001), the takeover deterrence hypothesis (Brown and Ryngaert, 1991; Bagwell, 1991) where firms repurchase to fend off unwanted takeover attempts, the dividend substitution hypothesis where firms substitute dividends with repurchases as a form of corporate payout to benefit from tax savings through capital gains tax of repurchases which is usually lower than the ordinary dividends tax (Black, 1976; Barclay and Smith, 1988), where firms distribute temporary cash flows to the shareholders through repurchases and would increase dividends only when earnings is believed to have increased permanently (Jagannathan, Stephens and Weisbach, 2000) and finally, where firms repurchase shares to counter the dilution effects of employee and management stock option plans (Fenn and Liang, 2001).

Therefore, the most commonly cited reasons by most researchers are the information signaling hypothesis, market undervaluation signaling hypothesis, the agency cost of free cash flows hypothesis and the capital structure adjustment hypothesis. The theories and hypothesis developments of each of these explanations will be discussed in the following subsections.

Information Signaling Hypothesis.

The first to introduce the concept of information signaling on the study of wealth effects of share repurchases is Vermaelen (1981). Under the information signaling theory, it is assumed that information asymmetry exists between the managers of a firm and the shareholders or the outside investors. In economics, information asymmetry occurs when one party to a transaction has more or better information than the other party (Finance - Wikipedia encyclopedia). In this context, this implies that the managers have typically better information as to a firm's true value as compared to the shareholders. In fact, as suggested by Miller and Modigliani (1961), when markets are incomplete i.e. in situations where shareholders are exposed only to public information and that the current stock prices are not able to reflect the private information that managers have, through changes in payout policies, for example by conducting share repurchase programs, managers are able to convey credible signals at some costs to the market of any new optimistic information that they have on the firm's performance, particularly with regards to the firm's future earnings and cash flows prospects.

As explained by Miller and Rock (1985), when managers foresee better than expected future earnings and cash flows, the managers are more likely to distribute cash in advance to the shareholders, either in the form of dividends or share repurchase, as they are confident that future capital expenditure requirements can be funded from future increases in earnings. Additionally, Grullon and Michealy (2004) argues that there will be an increase in firms' capital expenditures as well as research and development (R&D) expenses following share repurchase announcements as firms attempt to convey information about the good investments they are undertaking where cash flows from those investments would be realized in the distant future. Subsequently, the market then make adjustments accordingly in their assessment of the firm's future earnings and cash flow expectations, which in turn result in a price increase for the repurchasing firm's shares.

Based on the studies of Vermaelen, (1981), Nohel and Tarhan, (1998), Grullon and Ikenberry, (2000) and Grullon and Michealy, (2004) on share repurchases, there are several empirical implications to the information signaling theory. One basic and immediate implication is that repurchasing firms would experience positive price changes after repurchase announcements. Next, the repurchasing firms would also experience improved operating performance, as proxied by return on assets (ROA) in terms of future earnings after repurchase announcements. In conjunction to this, it also implies that firms would increase its capital expenditure after repurchase announcements where the source of future cash flows and profitability come from. Finally, the repurchase announcements should also be immediately followed by positive revisions in the market's expectations or analysts' forecast about firms' future profitability.

Market Undervaluation Signaling Hypothesis.

According to the market undervaluation signaling hypothesis, which is also built upon the notion of information asymmetry that exists between the managers and shareholders, when managers believe that their current stocks prices are underpriced or not reflecting the true underlying value of the firm, they would attempt to correct this mispricing in the stock market by conducting share repurchase programs (Comment and Jarrell, 1991), pledging to buy back stock from the shareholders at the repurchase market price, even in cases when the stock is overvalued which in fact would make their position worse off (Fried, 2005). The market undervaluation signaling hypothesis is basically a case of management's disagreement with how the market is pricing its current performance, in which just as firms are inclined to issue new equity when they perceive their stock price is too high, firms would prefer to conduct share repurchases when they think that the price is unfairly low. In fact, Ikenberry and Vermaelen, (1996) posited that OMRs

effectively represent excess market value for its "true" value. If management has no superior investment opportunities, the announcement of the repurchase announcement is a signal that the firm's value is higher than the market value that is created by the OMR. The OMR value ultimately depends on the firm's future growth opportunities when such opportunities are of little value."

As with other hypotheses, the market undervaluation hypothesis is that repurchasing firms have higher values (BTMV) at the time of the announcement as "value stocks" where the market value is higher compared to firms with low values (Ikenberry and Vermaelen, 1995). A firm with high BTMV and high operating performance have high BTMVs and high operating performance. Firms that arouse the market's attention are firms that have low BMTV, it is a signal of undervaluation. Other studies have shown that the market reaction is stronger for repurchase firms with high BTMV and hence are more likely to be repurchased.

A more direct evidence of the market undervaluation hypothesis is a period of price depreciation followed by a period of price appreciation pre-announcement about the repurchase announcement (Vermaelen, 1981; Comment and Jarrell, 1991; Comment and 2000). In other words, the market reacts to the announcement that their stock prices are underpriced relative to the overall market (Stephens and Larcker, 1986) and subsequently experiencing poor performance pre-announcement and subsequently experiencing positive performance post-announcement (Vermaelen, 1995 and 2000). The market reaction from repurchases that are

effectively represent exchange options that provide the firm with the flexibility to exchange its market value for its "true" value at the management's discretion. They argued that even if the management has no superior information or the market price of the stock is "fair" at the time of the repurchase announcement, the stock price should increase to recognize the option value that is created by the OMR program per se. However, it is argued again that the exchange option value ultimately depends on the ability of the management to detect valuation errors and seize the opportunities when share prices are relatively undervalued, otherwise the options will again be of little value."

As with other hypothesis, the basic implication of the market undervaluation signaling hypothesis is that repurchasing firms would experience positive short term price changes after repurchase announcements, particularly with regards to firms that have high book-to-market values (BTMV) at the time of announcement, in which such firms are generally referred to as "value stocks" where post-announcement abnormal returns are expected to be higher as compared to firms with low BTMV, generally known as "growth stocks" (Ikenberry, Lakonishok and Vermaelen, 1995). As posited by Zhang (2005), the most undervalued firms are those that have high BTMVs and when such firms make share repurchase announcements, these are the firms that arouse the most response and reaction from the market. Likewise for the growth firms that have low BMTV, it is assumed that share repurchasing is motivated by other reasons instead of undervaluation. Other than the BTMV, the initial market reaction is also expected to be stronger for repurchase firms that are small as small firms are usually less scrutinized by analysts and hence are more likely to be mispriced (Zhang, 2005).

A more direct empirical implication is that repurchase firms are more likely to experience a period of price depreciation before the repurchase announcement, thereby exhibiting negative pre-announcement abnormal returns as an indication of share undervaluation (Dann, 1981; Vermaelen, 1981; Comment and Jarrell, 1991 and Ikenberry, Lakonishok and Vermaelen, 1995 and 2000). In other words, firms would typically initiate OMR announcements when they realize that their stock prices have been performing poorly as compared to the performance of the overall market (Stephens and Weisbach, 1998). Finally, the next implication would be that after experiencing poor pre-announcement stock price performance, the repurchasing firms would subsequently experience improvements in stock price performance over a period of time, thereby exhibiting positive post-announcement long term abnormal returns (Ikenberry, Lakonishok and Vermaelen, 1995 and 2000). As posited by the authors, better long run performance is expected from repurchases that are driven more by undervaluation than by other motives.

Agency Costs of Free Cash Flow Hypothesis.

Based on the early work by Berle and Means (1932) on the separation of ownership and managerial control, Jensen and Meckling (1976) posited that it is common for agency conflicts to arise between the managers (agents) and the shareholders (owners) as managers do not always undertake actions that maximize shareholder value. As shareholders do not have direct control over the daily running of the business, managers at times may undertake opportunistic behavior and eventually make decisions that protect their own interests over that of the shareholders'. Consequently, these agency conflicts results in agency costs in which such costs lead to a deterioration of firm value due to managers acting in their own interests. As put across by Jiraporn (2006) who relates the level of firms' repurchase activity with the strength of shareholders' rights, argued that based on the agency theory, firms with weak shareholder rights are likely to suffer higher agency costs as managers are more likely to put their own interests ahead of their shareholders'.

Subsequent to Jensen and Meckling (1976), Jensen (1986) went further to study agency costs with respect to free cash flows which is defined as those available cash flows that are in excess of those required to finance all of its investment opportunities that provides positive net present values (NPV). As in Lehn and Poulsen (1989), the free cash flow is defined as the operating income before depreciation minus interest expense, taxes and dividends, normalized by the total assets. Jensen posited that when managers face large amount of excess cash in the firm, higher agency costs could arise due to the higher possibility of managers squandering corporate resources on unprofitable investments, based on the premise that firms currently, on a temporary basis do not have positive NPV projects to invest, or that its reinvestment rate is declining. As managers are more inclined towards incentives that can achieve the target of size and growth such as empire building, takeover activities or perquisite consumption that can boost their reputation, power and remuneration, they would most likely invest the excess cash on new projects, even if those projects have negative net present values. Shareholders however would prefer that the free cash flows be allocated and distributed back to them in a form of special dividend or share repurchase instead of wasting the excess cash on unprofitable projects that can destroy firm value.

Therefore, according to Jensen's agency costs of the free cash flow hypothesis, in situations of a firm facing with excess cash and poor portfolio of investment opportunities, when managers are inclined towards distributing the excess cash back to the shareholders in the form of share repurchase instead of retaining the excess cash in unprofitable projects, the market

would react positively to price performance. As in profitable investment as positive news that the management's dispo overinvestment, especia deterioration which ulti

Similarly, the positively when firms, b value by selling off neg in the form share repur agency problems and a posited that agency cost but are also with pote cash, especially the ne funds are injected into more the firm is over- announcement. In fact, that by taking excess c could indirectly contro projects. Then again, Is choose OMRs to distrib new projects. Along th on the study of dividen may generate free cash from a higher growth the maturity hypothesis firms usually have num free cash flows and hig

However, upon reachin maturity stage. At this firm's profitability, the rate will also decline, t

would react positively to the repurchase announcements to result in improvements in stock price performance. As argued by Jensen, the market is already aware of the firms' reduction in profitable investments and the market basically interprets the repurchase announcements as positive news that conveys firms' commitment to reduce the amount of free cash flows at the management's disposal as well as firms' commitment to mitigate potential agency cost of overinvestment, especially when it involves negative NPV projects that can lead to firm value deterioration which ultimately is not in the best interest of the shareholders.

Similarly, the free cash flow hypothesis also predicts that the market would react positively when firms, being in the state of over-invested, remedy the situation and improve firm value by selling off negative or low NPV projects and distribute the proceeds to the shareholders in the form share repurchase, signaling to the market that they are now committed to mitigate agency problems and agency costs of free cash flows (Nohel and Tarhan, 1998). Nohel et al. posited that agency costs, in this context, are not only related with actual excess cash on hand, but are also with potential cash surpluses, that is those investments that can be converted into cash, especially the negative NPV projects which can adversely affect firm value if continuing funds are injected into those projects. As posited by Perfect, Peterson and Peterson (1995), the more the firm is over-invested, the bigger the market response should be from a repurchase announcement. In fact, in the seminal papers of Easterbook (1982) and Jensen (1986), they argued that by taking excess cash from the firm through increasing the level of payout, shareholders could indirectly control managers of the firm from unmonitored spending of unprofitable projects. Then again, Isagawa (2000) showed that under some reasonable conditions, managers choose OMRs to distribute excess cash if they feel there is little benefit in taking on unprofitable new projects. Along the line with Grullon, Michaely and Swaminathan (2002) which centers on the study of dividends, Grullon et al. (2004) provide suggestion as to the reason why firms may generate free cash flows and hence undertake share repurchases, is due to firms' transition from a higher growth phase to a lower growth phase, in which the former authors proposed as the maturity hypothesis. These authors argued that during the growth phase of a firm's life cycle, firms usually have numerous positive NPV projects to undertake, high capital expenditures, low free cash flows and high earnings growth.

However, upon reaching a certain stage, the firm faces deterioration in growth and enters into maturity stage. At this phase, the firm's investment opportunities decline and along with that, the firm's profitability, the requirement for capital expenditures and ultimately its earnings growth rate will also decline, thereby resulting in the generation of high free cash flows in the firm.

Following Berk, Green and Naik (1999), when a firm has fewer options to grow, and their assets play a bigger role in determining its value, the firm's systematic risk will decline, which in turn reduces the firm's cost of capital. Hence, as proposed by Grullon et al. (2002) and Grullon et al. (2004), cash payout announcements either through dividends or repurchase programs particularly by mature firms can result in a positive market reaction where the market interprets the announcements as positive news that conveys a decline in the riskiness of the maturing firms' assets, a notion that is consistent with the findings of Litner (1956) and Brav, Graham, Harvey and Michaely (2005) that managers increase their cash payout when they feel that the firm's cash flows are less risky.

Thus, based on the above theoretical explanations of the free cash flow hypothesis, one of the first few empirical implications is that repurchasing firms should experience a decline in their profitability as proxied by ROA due to investment opportunities deficiencies. This is in contrast to the information signaling hypothesis where repurchasing programs instead convey positive news about future profitability. Likewise as a result of investment opportunities deficiencies, repurchasing firms should also face a decline in their capital expenditures, thereby reducing the need to keep cash reserves for further investments. In addition, repurchasing firms, particularly with respect to mature firms, should also experience a decline in the systematic risk and hence a reduction in the firms' cost of capital. Next, in validating the free cash flow hypothesis, the market reaction of repurchase announcements should be relatively stronger for firms that are more likely to over-invest, reflected from their high levels of cash and few investment opportunities. Following Lang and Litzenberger (1989), the Tobin's Q is used as a proxy to measure a firm's investment opportunities where a Tobin's Q value of less than 1 renders a firm to be classified as over-invested. Therefore, firms with higher repurchase activity should exhibit superior price performance with the view that repurchases help to reduce agency costs of free cash flows by getting rid of excess cash being invested in unprofitable projects (Jiraporn, 2006). Since OMRs are not legal obligations, hence the more a firm actually spends on repurchases; the better should be the firm performance.

The Capital Structure Ad

When companies decrease which in turn wo that an optimal leverage ra tool to help firms adjust an leverage ratio (Bagwell and to the leverage adjustment if the firm's leverage ratio factors that may cause a f forwarded by Chan et al. have the effect of increasing not surprising to see repurc an increase in stock price a Likewise, equity dilutions ownership plans (ESOPs) r result a firm's leverage pos

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The Capital Structure Adjustment Hypothesis.

When companies repurchase their stock from the market, firms' equity base will decrease which in turn would cause the leverage or debt to equity ratio to increase. Assuming that an optimal leverage ratio exists, firms may hence utilize share repurchasing as a financial tool to help firms adjust and manage its capital structure towards the attainment of its optimal leverage ratio (Bagwell and Shoven, 1989 and Hovakimian, Opler and Titman, 2001). According to the leverage adjustment hypothesis, a firm is more likely to undertake repurchasing programs if the firm's leverage ratio is below the target leverage ratio (Dittmar, 2000). There are several factors that may cause a firm's leverage to be below its optimal target and among them, as forwarded by Chan et al. (2004) is the use of executive stock options which when exercised, have the effect of increasing equity financing in the firm. The authors argued that it is therefore not surprising to see repurchase activity associated with either option grants, option exercises or an increase in stock price as options move into the money (Kahle, 2002 and Weisbenner, 2000). Likewise, equity dilutions such as dividend re-investment plans (DRIPS) and employee stock ownership plans (ESOPs) may also affect a firm's capital structure in which left unchecked may result a firm's leverage position to be away from its optimal position.

In repurchasing a firm's stock from the market, the firm may finance its repurchases from its cash reserves and/or marketable securities where the extent of the increase in debt to equity ratio depends upon the method used to calculate the leverage ratio. If the share repurchases are financed with debt, as explained by (Guffey and Schneider, 2004), it is practically identical to debt-equity exchanges. The authors explained that when firms repurchase shares through debt to adjust their financial leverage, firms may benefit from the tax advantages of debt financing. (Mintz, 1995) argues that when firms increase their leverage, either by adding new debt or by depleting its cash, the tax savings conserves cash and lowers the cost of capital and the stock market will recognize that the tax savings will flow to the shareholders, hence resulting in an increase in market value by a factor consistent with the prevailing price-to-earnings (PE) ratio.

Mintz (1995) presents evidence that the 20 largest share repurchases in 1995 become tax benefits (shields) that are valued by the market at over \$9,500,300,000. First, Mintz provides the magnitude of the buyback in terms of market value. The market value of the buyback is multiplied by the appropriate interest rate consistent with Standard and Poor's credit rating at the time the buyback is announced to determine the tax shield created. Second, the tax shield is multiplied by the firm's income tax rate to determine the amount that would otherwise go to taxes. The amount saved on taxes is then multiplied by the price-to-earnings ratio to determine

the value of the benefit to the shareholders. The tax benefits are then divided by shares available producing an increase in market value per share. Mintz finds that the 20 largest buybacks produce increases in earnings per share that average \$1.51 3. This increased share value benefits all shareholders, whether they participate in the share repurchase or not.

One of the first few empirical implications of the capital structure adjustment hypothesis is that the market reaction should be greater for repurchasing firms that experience low leverage ratios as compared to their industry peers (Chan, Ikenberry and Lee, 2004). Another implication as proposed by the above authors would be that the market reaction should be greater for repurchasing firms whose leverage had decreased the most prior to a repurchase announcement. To test the validity of the leverage adjustment hypothesis, total debt to equity and long-term debt to equity are used to measure capital structure and the level of indebtedness (Guffey and Schneider, 2004). These two ratios are used to examine the adjustment of long-term debt of repurchases relative to their equity levels. Chan, Ikenberry and Lee, (2004) used the ratio of the total debt to total assets at previous fiscal year-end to measure leverage which is adjusted for industry median.

Conclusions.

It has now become common for publicly traded companies in Malaysia to repurchase shares from the open market. Even companies generally perceived as conservative have joined the fray, convinced that there are benefits from embarking on these buyback schemes. Despite the pick-up in buyback activity in Malaysia since its initiation in 1997, the debate has not ended as to what actually motivate firms to repurchase their shares from the market, especially when firms' capital and cash resources could have been utilized in other profitable investments such as mergers and acquisitions, capital expenditures and working capital that could have produced better returns to the companies. This paper presents theoretically the four commonly cited reasons by past researchers for firms' repurchase programs, i.e. the information signaling hypothesis, market undervaluation signaling hypothesis, the agency cost of free cash flows hypothesis and the capital structure adjustment hypothesis. Scope for future research on other hypothesis as mentioned earlier could be further undertaken to provide a more comprehensive picture as to what motivate firms to repurchase shares, ultimately understanding how share repurchases can aid to enhance both company and shareholder values.

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THE RELATIONSHIP BETWEEN FIRM PERFORMANCE AND BUYBACKS

This study was conducted to investigate the relationship between firm performance and buybacks in medium enterprises. Data were collected from 100 medium enterprises in the Klang Valley region. A regression analysis was conducted to examine the relationship between firm performance and buybacks. The results of the regression analysis show that there is a positive relationship between firm performance and buybacks. This suggests that firms with higher performance are more likely to engage in buybacks. The study also found that government policy has a significant impact on the relationship between firm performance and buybacks. The results of the study have implications for government policy and for the development of medium enterprises.

Keywords: SME Growth, Firm Performance, Buybacks, Management, Market

Introduction.

Small and Medium Enterprises (SMEs) are an important part of the economy in developing countries (D). The development of SME sector in the industry helps to strengthen the economy of LI because every large country has SMEs. The future of the LE

*Lecturers at College of B

**THE RELATIONSHIP BETWEEN VALUE OF ENTREPRENEURS,
FIRM FINANCING, MANAGEMENT AND GROWTH
PERFORMANCE OF SMALL MEDIUM ENTERPRISES IN
CAMBODIA**

Mohd Noor Mohd Shariff & Chea Peou*

Abstract

This study was conducted to examine the relationship between value of entrepreneurs, firm financing and management and growth performance of small medium enterprises (SMEs) in Cambodia using 220 usable questionnaires that were collected from owners/managers of the firms. The outcomes of stepwise regression analysis showed that the inclusion of market environment and government policy in the analysis had increased the effect of the relationship between value of entrepreneurs, firm financing and management and growth performance of SMEs in Cambodia. In addition, implications of this study to SME growth performance theory and practice, conceptual and methodological limitations, as well as directions for future research are also discussed.

Keywords: *SME Growth Performance, Value of Entrepreneur, Firm Financing, Management, Market Environment and Government Policy.*

Introduction.

Small and Medium Enterprise (SME) sector development is one of the recent key issues in developing countries (Davidsson, 2004; Gibb & Ritchie, 1982). As a developing country, the development of SME sector in Cambodia is important. The assistance of SME as a support industry helps to strengthen the large industries (LIs). SME development is the future candidate of LI because every large enterprise (LE) has had the experience of starting their business as SMEs. The future of the LE is dependent on the development of SME.

* Lecturers at College of Business, Universiti Utara Malaysia.

SME development is also an important issue for the labor market because it employs the labor force and offers wages to workers (Kirchhoff, 1994). In Cambodia, the development of the SME sector could not only be the key issue of industry development, but also for socio-economic development of the country.

The role of SMEs has been recognized to be important by every nation around the world. It is considered to be an engine for growth and poverty reduction for the country through the creation of jobs and incomes for the people (Morris, May, Godden & Nicholson, 2001; World Bank Group, 2004; Ngasongwa, 2002; Hashim, 2004); domestic production and export (Hisrich & Szirmai, 1993; McMillan & Woodruff, 2002); entrepreneurial skills and industrial linkages (Chee, 1986; Wyer, 1999; Goh & Chew, 1996; Mohd Shariff, 2003); individual collective initiative and social values (Clapham, 1985).

It is also considered as the tool for economic survival during the country's crises (Tambunan, 1992; Goh & Chew, 1996; Frank & Landstrom, 1997). Moreover, SMEs are increasingly become more important for poor and developing countries (Chico, 1983; Khan, 2002). Perhaps this role has been reached to a consensus by all parties involved. According to the President of the World Bank Group, James D. Wolfensohn: "SMEs are the private sectors for employment generation and sustainable growth" (World Bank Group, 2004). The concern of transitional economy from the former Soviet Union to Central and Eastern Europe to China and Vietnam are similar in one important aspect. SMEs help to improve and sustain the health of the market economy in term of job creation, plenty of domestic production, and export (Hisrich & Szirmai, 1993; McMillan & Woodruff, 2002).

This is true especially when the surplus of labour, scarcity of capital within the rapidly growing population in the poor and developing countries are high (Chico, 1983; Khan, 2002).

Clapham (1985) also indicated that SME help to promote individual collective initiative, basic social values, and is highly view as a crucial tool towards achieving a social and regional integration.

Evidence from the World Bank Group, (2004) had proven that SMEs in China helped nearly 200 million people to escape from extreme poverty as the result of the economic reform in 1979. As in the case of Taiwan, SMEs dominated 97.81 percent of total industrial establishments and contributed 69.27 percent of total employment, 32.11 percent of total sale values, and 48 percent of total export for the country's economy (Ministry of Economic Affair, 1997).

SMEs not only recession in 1985. It also Singapore (Goh & Chew many large firms in the d as the problem solver to

However, SME These problems can be o Metcalfe & Porteous, 19 as macroeconomic envir physical infrastructures that the potential factors from economics, politic growth performance are and entrepreneurs.

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SMEs not only helped during the period of economic growth but also in economic recession in 1985. It also becomes the home for growth of Multinational Companies (MNCs) in Singapore (Goh & Chew, 1996). The strong turbulent in the world economy in 1970s had made many large firms in the developed countries to lay off their employees. SMEs then were regarded as the problem solver to these structural changes (Frank & Landstrom, 1997).

However, SMEs faced many problems in their growth performance (Kirby, 2003). These problems can be due to the lack of value of entrepreneurs, finance and markets (Barber, Metcalfe & Porteous, 1989; Allal, 1999; Kirby, 2003). Together with other external factors such as macroeconomic environment, government policies and regulations, and the availability of physical infrastructures distorted the growth performance of SMEs. Szegedi (1989) supported that the potential factors that influence on the SMEs growth performance in Hungary are created from economics, political, and social infrastructure. Therefore, the strategies toward SMEs growth performance are still being discussed among the theorists, economists, policy makers, and entrepreneurs.

Some proponents suggested on the study of the problems on SME growth performance and its influences (Austin, 1988; Arbaugh & Sexton, 1996; Das, 1996; Hull, 1990; Petrakis, 1997; Barber, Metcalfe & Porteous, 1989; Mohamad, Rashid & Sidin 1998; Kirby, 2003). Others have suggested on the creation of business friendly environments through government policies; an influential factor on SME growth performance (Fabella, 1987; Islam, 1987; MPDF, 1997; Mannan 1993; Pilgrim, 1994; Dijk, 1997; Czinkota & Ricks, 1981; World Bank Group, 2001; IFC, World Bank Group, 2004).

Similarly, the review of the literature suggests limited empirical research attempt has been made to explore SME growth performance in Cambodia. As been stated by IFC, World Bank Group-SME (2002): "as in so many countries, emerging local entrepreneurs hold the key to job creation and rising incomes in Cambodia but they are blocked from building the successful companies to their economy needs by weak financial market and support institutions, dilapidated infrastructure, ineffective legal system, and corruption."

Review of Literature.

SME Growth Performance.

Penrose (1995) defines performance as a measure of how well the firm achieves its goals (organizational and financial goals). Performance is defined similarly in this study to describe the performance of SMEs by using measures such as profitability, growth, and survival. It depends on how firms determine their goals and achievement, i.e. what are the goals of a firm and how did it succeeds to reach them.

The outcomes of a firm's performance whether they are high or low depending on whether a firm has achieved its goals or not (Barney, 1991; Davidsson, 2004; McMahon, 2001). The merits of the measures used in this study are that, they are widely understood, brief, able to be verified and replicated. The most common objective measures of organizational performance are the returns on equity (ROE), return on assets (ROA), sales growth, and total return to stakeholders. Several studies use more than one measure of firm performance. Performance is generally associated with expectation for success (Penrose, 1995).

Factors influencing the Growth Performance of SMEs in Cambodia.

Tambunan (1999) found that small business owner-managers having 'value of entrepreneurs' or entrepreneurial values such as creativity, integrity, achievement, among others, were more likely to have superior performance in managing organizations than owner-managers without these values. McMahon (1998) findings left open to questions of generalisability and whether or not personal characteristics and values might be able to be used to predict an individual's position on an 'entrepreneurial-conservative' values continuum. Beyond that, lay a question of a measure of the degree to which an individual owner-manager could be characterized as "entrepreneurial" that might be able to be use to predict the performance of the organization they own (Turner, 1997).

The role of individual characteristics, values and expectations in determining the subsequent actions of those who start and run their own businesses has been explored in the academic literature and linking to business performance have been identified by a number of researchers (Fitzsimmons, Steffens & Douglas, 2005; McMahon, 2001). However, they differ in the academic literature in the formation of an individual's 'characteristics' that precedes with the dealing of the influences of each on the subsequent selection of the management practices.

Kyambalesa (1994) refers firms financing as the total amount of money invested to SMEs owners. It is one the major factors that relates to the growth performance of SMEs. Firm financing means that SME owners have to support the running of their businesses by getting financing from various sources. The lack of sufficient firm financing will create a significant problem on SMEs business activities and it is one of significant problems that affect SME growth performance (Mannan, 1993).

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Moreover, Kam (1994) indicated that the ability to generate ideas, the capability of problem solving and the level of technical sophistication of SME owners have a major influence on their SMEs growth performance.

Research conducted by Olsen & Johannessen (1994) cited that experiences and the competence levels of SME owners is also an important factor that influence SMEs growth performance. However, Johnson (1993) stated that the working style of owner-managers which emphasized their capacities in terms of speed to produce high quality work that meet the needs and requirements of customers and suppliers as an influence of the their SMEs growth performance. Owner-managers also need to persevere when appropriate and to think and act creatively and these are the prerequisite skills that contribute to the growth performance of SME.

The Importance of Market Environment and Government Policy.

There is little disagreement on the fact that Cambodia failed to maximize the benefits that derived from the SMEs sector. SMEs in the future will play a pivotal role in promoting and sustaining its industrial sector as well as growth (World Bank, 2001). Numerous reforms and trade liberalization measures squeezed the spheres of entrepreneur, the market and government's activity in business. It is now the role of the private sector such as SMEs to lead the economy in a dynamic growth path. SMEs are considered to be the seedbed for the development of entrepreneurial skills and innovation due to the flexibility nature of their operations.

Small capital requirement makes it possible for SMEs to enter easily and exit from the industry. It was believed that the private sector entrepreneurial activities had many important spillover and positive externality effects (Haswell & Holmes, 1989). However, liberalization of the economy along with rapid globalization has posed severe challenges to SMEs not only in international markets but also in the domestic economy. Since SMEs are based on relatively small investment, their survival depends on readily available markets with an easy access to entry. The development of the market is much more challenging in Cambodia, especially in the city of Phnom Penh, which requires coordinated efforts by individual business enterprises and the government to promote businesses in the city.

The Government through its agencies should promote a series of efficient policies affecting competitiveness, such as monetary, financial, budgetary, fiscal, labour and trade. The Government could reduce corrupt practices and punitive tax evasion through its policies. The political stability in the country will help to improve the administration of justice and bureaucracy in the country (Barney, 1991; Dovaldson, 1995; McMahan, 2001). Some of the measures to support businesses are by ways of increasing and promoting entrepreneurship, skilled labour, investments in technology, sound and management practices, among others. Infrastructure is enhanced by the provision of quality education, health, environment, water, energy, roads, and setting up of science and technology institutions.

Sound government policies support competitiveness (Dovaldson, 1995). A dynamic national system of technological innovation, globally integrated financial sector in a country, a well-developed infrastructure and a skilled labor force supports a country's international competitiveness. Reducing factors inhibiting competitiveness is thus the way forward.

SME Definition.

An enterprise of its legal form (Roman and family business) regularly engaged in business. People in different countries of Europe is made up of either an annual turnover exceeding 43 million

Penrose (1959) enterprise is defined by annual turnover or annual sales to differentiate between small and large enterprises defined as an enterprise with an annual balance sheet

The emphasis on development agenda for some developing countries the overall national economic

There is still a need for techniques to determine the size of SMEs Hashim & Abdullah (2001) measure SMEs based on turnover (Everett, 1998; Ueda,

Watson and others persons to do all the small and informal business low skill labour. However, applications among SMEs base on quantitative turnover (Latif, Kha

SME Definition.

An enterprise is considered to be any entity engaged in an economic activity irrespective of its legal form (Robinson, 1982; Young, 1985). This includes, in particular, sole proprietorships and family businesses engaged in craft or other activity and partnerships and associations regularly engaged in economic activity.

People in different countries tend to define SMEs in different ways. The category of SMEs in Europe is made up of enterprises which have fewer than 250 full-time employees and which have either an annual turnover not exceeding 50 million Euros, or an annual balance sheet total not exceeding 43 million Euros (Jensen, 2000; Penrose, 1995).

Penrose (1995) stated that it is necessary to differentiate between SMEs. The small enterprise is defined as an enterprise which has fewer than 50 full-time employees and whose annual turnover or annual balance sheet total does not exceed 10 million Euro. Also it is necessary to differentiate between micro enterprise and small enterprise whereby the micro enterprise is defined as an enterprise which has fewer than 10 full-time employees and whose annual turnover or annual balance sheet total does not exceed 2 million Euro.

The emphasis on developing SMEs occupies a prominent position in the economic development agenda of many developing countries in the world (Jensen, 2000; Penrose, 1995). For some developing countries, the development of the SMEs sector becomes primarily part of the overall national economic development strategies (Barney, 1991).

There is still not a clear definition of SMEs. Different country uses different measurement techniques to determine SMEs and it depends on their purposes (Kirby, 2003; Ngasongwa, 2002; Hashim & Abdullah, 2000). The quantitative and qualitative measurements can also be used to measure SMEs based on the characteristics of the firms (Hanchuan & Zhongqi, 2000; Watson & Everett, 1998; Ueda, 1995).

Watson and Everett (1998) measured small business as the business that uses one or two persons to do all the critical business activities without any specialists. Ueda (1995) measured small and informal business as family-owned having small-scale operation, labor-incentive and low skill labour. However, the qualitative measurement of SMEs has remained unclear for some applications among the specialists. Most countries in Asia and Europe have turned to measure SMEs base on quantitative techniques by either employments, capitalization/assets, or annual turnover (Latif, Khan, Abdullah & Ali, 2000).

In Vietnam, Latif et al. (2000) defined micro-enterprise as one having less than 5 employees with capital less than VND 100 million; small business as one having 5-50 employees with capital of VND 100-300 million; and medium enterprise having 51-300 employees with capital from VND 301 million up to VND 1,000 million.

In Malaysia, different ministries or organizations measured SMEs in different ways, The Ministry of International Trade and Industry (MITI) defined small-scale firm in terms of not more than 50 full-time employees with annual sales turnover of not more than RM 10 million, medium-scale enterprise as one having between 51 and 150 full-time employees with annual sales turnover of between RM10 million and RM 25 million and paid-up capital of less than RM5 million (Hashim & Abdullah, 2000; Hashim, 2004).

To complicate matters further, the Credit Guarantee Corporation (CGC) adopts a definition of SME based on employment and shareholders' funds (a term which includes paid up capital, retained profits and other reserves). What this means, in practice, is that established firms will not be eligible for CGC assistance as they build up shareholders' funds and breach the limits applied by CGC. This would not be able the case if CGC used the MITI approach of defining an SME in terms of paid-up capital.

Effective 2003, the Malaysian Government through the National Small and Medium Enterprise (SME) Development Council (the highest policy making body to chart future direction and strategies for SME development) has categorized of what institutes SMEs in Malaysia (SMIDEC, 2004). SMEs are defined according in various sectors based on annual sales turnover or number of full-time employees as follows:

"A small and medium enterprise in primary agriculture is an enterprise with full-time employees not exceeding 50 or with annual sales turnover not exceeding RM5 million."

"A small and medium enterprise in manufacturing (including agro-based) and manufacturing related services is an enterprise with full-time employees not exceeding 150 or with annual sales turnover not exceeding RM25 million." "A small and medium enterprise in services is an enterprise with full-time employees not exceeding 50 or with annual sales turnover not exceeding RM5 million."

In 1995 Ch involve in the field NT\$60 million and f in the field of agricul real estate, and other with the fewer than 5

Based on th Group-SME (2002) in the world. The act generation, social ba development (Table 1

Table 1. The Common

T
SMEs Characteristic
Micro-Enterprise
Small Enterprise
Medium Enterprise

Source: IFC, World B DC: Jarboe Printing

The RGC, S number of employees with capital less than US\$50,000 to less tha capital from US\$250,

In 1995 China revised and adopted its SME definition. SME has been defined as a firm involve in the field of manufacturing, construction, and mining, with the capital of less than NT\$60 million and fewer than 200 full-time employees. SME has been defined as a firm involve in the field of agriculture, utilities, commerce, transportation, storage, communications, finance, real estate, and other various services with the annual sales value of less than NT\$80 million and with the fewer than 50 full-time employees (Lin, 2002).

Based on the experiences of SMEs around the globe, the IFC and the World Bank Group-SME (2002) defined its own SME definition toward a common purpose for countries in the world. The action undertaken is to define SMEs growth in terms of employment, income generation, social balance, country development, regional integration, and also for global development (Table 1).

Table 1. The Common Global SME Definition of IFC and the World Bank Group-SME

The Common SMEs Definition of IFC and World Bank			
SMEs Characteristics	No.Of Employees	Capital Investment	Annual Turnover
Micro-Enterprise	Less than 10	Less than US\$100,000	Less than US\$100,000
Small Enterprise	10-50	\$1 00,000-\$300,000	\$1 00,000-\$300,000
Medium Enterprise	51-300	\$3,000,000-\$15,000,000	\$3,000,000-\$15,000,000

Source: IFC, World Bank Group -SME, (2002). *Review of small business activities*. Washington DC: Jarboe Printing Company.

The RGC, SMEs Sub-Committee (2005) defined SMEs in Cambodia according to the number of employees and finance required. Micro-enterprise as having less than 10 employees with capital less than US\$50,000, small enterprise as having 11-50 employees with capital from US\$50,000 to less than US\$250,000, and medium enterprise as having 51- 100 employees with capital from US\$250,000 to less than US\$500,000.

Research Methodology.

Data for this study were gathered through survey questionnaires. After refining, categorizing and comparing the information with relevant theoretical and empirical evidence, this was used as a guideline to develop the content of survey questionnaires for a pilot study. Next, a pilot study was conducted on 2 experienced academic staff who has worked in higher learning sector. Their feedbacks were used to verify the content and format of questionnaires developed for an actual survey. Back translation technique was used to translate the content of questionnaires in Khmer and English in order to increase the validity and reliability of the instrument (Baker, 1994; Romano & Ratnatunga, 1995).

The survey questionnaire had two sections. Firstly, consists of questions on the demographic profile of the respondents. Secondly, consists of questions on factors that influence the SME growth performance. The values of entrepreneurs consist of 15 items that were modified from the entrepreneur behavior theory literature (see Schumpeter, 1934; Kirchoff, 1994). Secondly, firms financing had 11 items that were developed based on resource base theory literature (Barney, 1997). Thirdly, management was measured using 14 items that were developed from Barney (1997). Fourthly, market environment and government policy were measured using 15 items each that were developed from the contingency theory (Dovaldson, 1995). Finally, SME growth performance was measured using 5 items that were developed by Penrose (1995). These items were measured using a 3-item scale ranging from "Strongly disagree" (1) to "Strongly agree" (3).

The unit of analysis for this study is owners/managers from SMEs in Phnom Penh of Cambodia. A convenient sampling technique was used to gather data from the SME firms. Based on the combined list created from the MOC, yellow pages from the telephone directory and business cards in the area of Phnom Penh (Webster & Boring, 2000), the researcher contacted 1078 SMEs out of the total of 3064 to obtain official permissions to conduct a survey. Only two hundred and fifty-three (253) firms agreed to participate in this study. Of that total, 220 usable questionnaires were returned to the researchers, yielding 20.40 percent response rate. The survey questionnaires were answered by participants based on their consents and a voluntarily basis. The names of owners/managers of the SME firms were made anonymous in order to avoid intrusiveness. A Statistical Package for Social Science (SPSS) version 15.0 was used to analyze the validity and reliability of measurement scales and thus test research hypotheses.

Hypotheses.

Hypotheses.

Four hypotheses were t

- H1: There is a management
- H2: Market environment
- H3: Government policy
- H4: Government policy

Research Findings.

Table 2 shows manufacturing (49%) medium enterprises. P respondents (85.5%) c The majority (70%) o

Types of Businesses	= 61.8
Trading firm	= 23.6
Number of Employees	<5 = 51.4
	6-20 = 33.6
	21-50 = 9.5
	51-100 = 4.5
	101-200 = 0.9
Amount of Capital	< = \$5,000 = 19.5
	> \$5,000 - \$ 10,000
	> \$10,000 - \$20,000
	> \$20,000 - \$50,000
	> \$50,000 - \$100,000
	> \$100,000 - \$200,000
	> \$200,000 - \$500,000
	> \$500,000 - \$1,000,000

Hypotheses.

Four hypotheses were tested for this study. They are:

- H1: There is a positive relationship between values of entrepreneurs, firm financing, and management and the growth performance of SMEs in Cambodia.
- H2: Market environment positively mediates the relationship between values of entrepreneurs, firm financing, and management and the growth performance of SMEs in Cambodia.
- H3: Government policy positively mediates the relationship between values of entrepreneurs, firm financing, and management and the growth performance of SMEs in Cambodia.
- H4: Government policy and market environment positively mediates the relationship between values of entrepreneurs, firm financing, and management and the growth performance of SMEs in Cambodia.

Research Findings.

Table 2 showed that sales/service and trading (85.4%) firms outnumbered their manufacturing (49%) counterparts. Over one-half (52.3%) of the sample firms are from the medium enterprises. However, 99% of the firms have less than 100 employees. The majority of respondents (85.5%) derived their sources of capital from personal savings, family and friends. The majority (70%) of the amount of capital invested by the firms are below US\$20,000.

Table 2. Sample Profile

Types of Businesses (%) Sales/service = 61.8 Trading firm = 23.6	Size of Business (%) Micro business = 5.0 Small business = 42.7
Number of Employees (%) <5 = 51.4 6-20 = 33.6 21-50 = 9.5 51-100 = 4.5 101-200 = 0.9	Sources of Capital Investment (%) Personal Savings = 48.6 Family = 35.5 Partnership = 14.5 Friends = 1.4 100.0
Amount of Capital Investment (%) < = \$5,000 = 19.5 > \$5,000 - \$ 10,000 = 30.0 > \$10,000 - \$20,000 = 20.5 > \$20,000 - \$50,000 = 15.5 > \$50,000 - \$100,000 = 7.7 > \$100,000 - \$200,000 = 4.1 > \$200,000 - \$500,000 = 2.3 > \$500,000 - \$1,000,000 = 0.5	

Table 3 shows that the factor analysis with direct oblimin rotation was done for six variables with 75 items. The Kaiser-Mayer-Olkin Test (KMO) which is a measure of sampling adequacy was conducted for each variable and the results indicated that it was acceptable. Specifically, these statistical results showed that (1) all research variables exceeded the acceptable standard of Kaiser-Meyer-Olkin's value of 0.6, (2) all research variables were significant in Bartlett's test of sphericity, (3) all research variables had eigenvalues larger than 1, (4) the items for each research variable exceeded factor loadings of 0.50 (Hair, Anderson, Tatham & Black, 1998), and (5) all research variables exceeded the acceptable standard of reliability analysis of 0.70. This result demonstrates the goodness of data for this study (Nunnally & Bernstein, 1994).

These statistical results support the notion of performance growth theories (see Gibb & Davies, 1990; Kovereid & Bullvag, 1996; Petrakis, 1990) and findings of previous study (see Gartner, 1997; Kirby, 2003; Churchill & Lewis; Tambunan, 1994; Kam, 1994). Hence, the goodness of data for this study is shown in Table 2.

Table 3. Goodness of Data

Measure	Items	Factor Loadings	KMO	Bartlett's Test of	Eigenvalue	Variance	Cronbach
Value of entrepreneur	15	0.86 to .93	0.930	5359.67; p=.000	12.258	81.721	0.984
Firm financing	11	0.73 to .92	0.946	2680.71; p=.000	8.144	74.034	0.964
Management	14	0.80 to .92	0.946	4094.65; p=.000	10.589	75.639	0.975
Market environment	15	0.78 to .95	0.948	5173.15; p=.000	12.026	80.175	0.982
Government policy	15	0.64 to .98	0.904	8718.09; p=.000	13.190	87.930	0.990
Growth performance	5	0.86 to .91	0.871	421.34; p=.000	3.820	76.407	0.922

Table 4 shows the results of Pearson correlation analysis and descriptive statistics. The means for the variables range from 2.49 to 3.59, signifying that the value of entrepreneur, firm financing, management, market environment, government policy and growth performance ranging from medium (2) to high (3). The correlation coefficients for the relationship between the independent variables (i.e., value of entrepreneurs, firm financing and management) and the mediating variables (i.e., market environment and government policy),

and the relationship between (value of entrepreneur and management) and growth performance, indicating the data were significant.

Table 4

Variable
Value of Entrepreneurs
Firm financing
Management
Market environment
Government policy
Growth performance

Note: Level of Significance

Outcomes of Testing Mediation Model
 Stepwise regression analysis was conducted for each independent variable and dependent variable. Each independent variable and Kenny (1986) suggested conditions: first, the independent variable must be significantly related to the dependent variable. The second condition is that the relationship between the independent variable and the dependent variable must be non-significant or reduced when the mediating variable is included in the analysis (Wong, Ho, & Cheung, 2003). The third condition is that the standardized beta coefficients for the mediating variables must be significant. The outcomes of testing

and the relationship between the independent variables (i.e., value of entrepreneurs, firm financing and management) and the dependent variable (i.e., growth performance) were less than 0.90, indicating the data were not affected by serious collinearity problem (Hair et al., 1998).

Table 4. Correlation Matrix Result for the Research Variable

Variable	Mean	Standard Deviation	Pearson Correlation Analysis						
			1	2	3	4	5	6	
Value of Entrepreneurs	3.433		1						
Firm financing	3.593	.79278		1					
Management	3.245	.81374	.498*		1				
Market	3.266	.81063	.237*	.265*		1			
environment	3.266	.84103	.251*	.180	.132		1		
Government policy	3.19	.81833	.270*	**				1	
Growth	2.493	.6005	.311*	.147*	.242	.225			1
performance	2.493	.6005	.311*	.219*	.248	.239	.624*		

Note: Level of Significance: *0.05 Reliability Estimation in the Parenthesis (1)

Outcomes of Testing Mediating Models.

Stepwise regression analysis was recommended to assess the magnitude and direction of each independent variable, and vary the mediating variable in the relationship between many independent variables and one dependent variable (Foster, Stine & Waterman, 1998). Baron and Kenny (1986) suggest that a mediating variable can be considered when it meets three conditions: first, the predictor variables are significantly correlated with the hypothesised mediator. Second, the predictor and mediator variables are all significantly correlated with the dependent variable. Third, a previously significant effect of predictor variables is reduced to non-significance or reduced in terms of effect size after the inclusion of mediator variables into the analysis (Wong, Hui & Law, 1995). In this regression analysis, standardized coefficients (standardized beta) were used for all analyses (Jaccard, Turrisi & Wan, 1990). Table 4 shows that the outcomes of testing the research hypotheses.

Table 5. Regression Analysis between Value of Entrepreneurs, Firm Financing, Management and the Growth Performance of SMEs in Cambodia

Parameter	B	Std. Error	Beta	t	sig
Constant	1.299	0.221		5.887	0.000
Value of entrepreneur	1.684	.172	.244	3.313*	0.001
Firm financing,	1.913	.180	.050	.676	0.500
Management	1.897	.163	.177	2.669*	0.008
F	10.849	(p-value=0.008)			
Adjusted R2	.119				

Note: *p<0.05

As can be seen from Table 5, multiple regression analysis was used to see whether there are relationships between values of entrepreneurs, firm financing and management on the growth performance of SMEs in Cambodia. The results have shown that is statistically significant relationship between values of entrepreneurs, firm financing and management and growth performance of SMEs. Thus proposition 1 was accepted. The adjusted R squared value was 0.119. The result indicates that 11.9% of the variance in the growth performance of SMEs has been significantly explained by the three dimensions (values of entrepreneurs, firm financing and management). Although the three dimensions are positively related to growth performance, only value of entrepreneurs and management are significant in enhancing growth performance on SMEs in Cambodia.

From Table 6, a hierarchical multiple regression is adopted in these analyses. At the first stage, the independent variables are input in a block. At the second stage, the moderator for instance, market environment is inserted in as the new block. In the final stage the interaction factor between the independent variables and the moderator (value of entrepreneur, firm financing and management *market environment) are included in the third block. The same steps are applied for moderating effects of government policy on the independent variables. The results show that market environment does moderate the relationship between values of entrepreneur, firm financing, and management and growth performance of SMEs. Thus proposition 2 was accepted ($\beta=.156, p=.000$). Furthermore, government policy found to moderate the relationship between values of entrepreneurs, firm financing and management and growth performance of SMEs. Thus these results provide support to proposition 3 ($\beta=.568, p=.000$). The adjusted R squared value was 0.409. Finally, the same steps are applied for the moderating effects of market environment

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Table 6: Hierarchic
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Note: *p<0.05

Parameter

Constant
Value of entrepreneur
Firm financing
Management
* Market Environ
F
Adjusted R2
Constant
Value of entrepreneur
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F
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Concluding Comm

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and a broad view of

and government policy on the independent variables. The results provide support to proposition 4 where government policy found to moderate the relationship between values of entrepreneurs, firm financing and management and growth performance of SMEs ($\beta=.557, p=.000$). The adjusted R squared value was 0.410.

Table 6: Hierarchical Regression Analysis between Values of Entrepreneurs, Firm Financing, management and the Moderating Effect of Market Environment and Government Policy on the Growth Performance of SMEs in Cambodia

Note: * $p < 0.05$

Parameter	B	Std. Error	Beta	t	Sig
Constant	1.074	.238		4.514	0.000*
Value of entrepreneur	.162	.056	.214*	2.895	.004
Firm financing	.027	.054	.036	.495	.621
Management	.124	.049	.167*	2.544	.012
* Market Environment	.111	.047	.156*	2.391	.018
F	9.743		(p-value= 0.000)		
Adjusted R2	.138				
Constant	.546	.195		2.804	.0006*
Value of entrepreneur,	.084	.047	.111	1.797	.074
Firm financing,	.046	.045	.062	1.020	.309
Management	.050	.041	.068	1.226	.221
* Government Policy	.417	.040	.568*	10.338	.000
F	38	.84	(p - value=0.000)		
Adjusted R2	0.409				
Constant	.462	.206		2.24 1	.026*
Value of entrepreneur	.076	.047	.100	1.612	.108
Firm financing,	.041	.045	.056	.915	.361
Management	.049	.041	.066	1.188	.236
* Market Environment	.049	.039	.069	1.260	.209
* Government Policy	.409	.041	.557*	10.019	.000
F	31.475		(p-valua=0.000)		
Adjusted R ²	0.410				

Concluding Comments.

The findings of this study confirm that government policy does act as a full mediating variable in the growth performance of SMEs in Cambodia. The choice of the government policy options for dealing with the growth performance of SMEs needs to be based on good diagnostic and a broad view of the policy options.

Regarding the robustness of research methodology, the data gathered from SME growth performance literature, the pilot study and the survey questionnaire have satisfactorily met the requirements of validity and reliability, and this may lead to the production of accurate and reliable findings. With respect to practical contributions, the findings of this study may be used as guidelines by SMEs especially looking at the market forces that seem to be the constraint on their growth performance. The implementation of growth performance model is the best measurement model and strategy for entrepreneurs in Cambodia to run their business well. The growth performance of SMEs captures the ability of entrepreneur to set up and aligned the company by managing and adapting to change. Processes will only succeed if adequate skilled and motivated employees are being provided with accurate and timely information. The study confirmed that in SMEs, entrepreneurs who are skilled and adequately trained are able to improve the quality and reduce cycle time. The present study suggests that the government policy will be best served if the regulatory, cognitive and normative be strengthened.

The conclusion drawn from the results of this study should consider the limitations below. Firstly, the regional bias of our sample which consists of SMEs based in Phnom Penh City of Cambodia. The Phnom Penh City consists of 3,064 SMEs from which the sample is drawn, which may not necessarily be representative of the population. Barkham et al. (1996) found that regional study may suffer from bias, if differences in the characteristics of firms and owner managers exists between region. However, evidence from previous studies has refuted regional and locational factors as being important in the study of SMEs (for example, Mahmud, 1981; Hakim, 1989; Storey et al., 1989 and Keasey & Watson, 1994). Furthermore, the focus on Phnom Penh City, as opposed to national sample for Cambodia, is justified on the basis of convenience (proximity to the researcher), and time and cost constraints.

Secondly, the sectoral bias where the major business activities in the Phnom Penh City include sale/service firms, trading firms and manufacturing firms. A sample drawn randomly from the underlying population of SMEs would tend to favour general business firms, a sector in which the growth performance will be lower. This outcome would have prevented the researcher from exploring the growth performance of the manufacturing sector. To reduce the sectoral bias, the number of manufacturing firms in the sample must be increased to counter the composition of the population. Thirdly, although outcomes of regression analysis can produce substantial amount of variance in dependent variable explained by the significant predictors is identified, but there are still a number of unexplained important factors that should be incorporated to identify the causal relationship among variables and their relative explanatory power (Tabachnick & Fidell, 2001). Finally, this research uses a mail questionnaire survey. The biggest administrative drawback of mail questionnaires is that the researcher has to risk the questionnaire being completed by those assigned by the owner manager but not involved in decision making. Therefore, the researcher has to: "accept the completed questionnaires on faith (Wahab, 1996)." However, the researcher has reasonable confidence in the accuracy of the data collected using this method.

Directions
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variables such as
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Directions for future research should consider the conceptual and methodological limitations of this study. Firstly, SME characteristics (sizes, types of business, innovativeness) should be further explored, and this may provide meaningful perspectives for understanding of how individual similarities and differences affect the growth performance of SMEs. Secondly, the limitations of cross-sectional research method may be overcome if longitudinal studies are used to collect data and describe the patterns of change and the direction and magnitude of causal relationships between variables of interest. Thirdly, future studies could examine whether variables such as organizational structure and organizational culture influence the growth performance of SMEs.

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