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Financing Product Innovation through Sharia Fintech in Supporting the Development of Halal UMKM

Inovasi Produk Pembiayaan melalui Fintech Syariah dalam Mendukung Pengembangan UMKM Halal

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Abstrak

Kata Kunci: Produk Pembiayaan; Fintech Syariah; UMKM Halal; Inovasi; Literasi.

Inovasi produk pembiayaan dalam industri fintech syariah telah menjadi faktor penting dalam mendukung pertumbuhan dan pengembangan Usaha Mikro, Kecil, dan Menengah (UMKM) yang berorientasi pada prinsip-prinsip syariah. Dalam konteks globalisasi ekonomi dan peningkatan kesadaran akan pentingnya patuhan syariah, UMKM halal memainkan peran yang semakin penting dalam ekonomi modern. Penelitian ini menyelidiki bagaimana inovasi produk pembiayaan platform fintech syariah dalam mendukung pengembangan UMKM halal. Dengan menganalisis karakteristik produk pembiayaan yang sesuai dengan prinsip syariah, serta mempertimbangkan kebutuhan dan tantangan yang dihadapi UMKM halal, penelitian ini mengeksplorasi berbagai model pembiayaan yang dapat diterapkan oleh fintech syariah untuk mendukung pertumbuhan sektor UMKM halal. Menggunakan pendekatan studi literatur untuk memberikan pemahaman yang lebih dalam tentang bagaimana inovasi produk pembiayaan fintech syariah dapat berperan dalam mendukung pertumbuhan dan pengembangan UMKM halal dan memberikan panduan bagi pelaku industri, dan pemangku kepentingan lainnya dalam memperkuat ekosistem pembiayaan UMKM halal melalui fintech syariah.

Abstract

Keywords: Financing Products; Islamic Fintech; Halal UMKM; Innovation; Literacy.

Financing product innovation in the Islamic fintech industry has become an important factor in supporting the growth and development of Micro, Small and Medium Enterprises (UMKM) oriented towards sharia principles. In the context of economic globalisation and increased awareness of the importance of sharia compliance, halal UMKM play an

increasingly important role in the modern economy. This study investigates how the innovation of Islamic fintech platform financing products in supporting the development of halal UMKM. By analysing the characteristics of sharia-compliant financing products, as well as considering the needs and challenges faced by halal UMKM, this study explores various financing models that can be implemented by Islamic fintech to support the growth of the halal UMKM sector. Using a literature study approach to provide a deeper understanding of how sharia fintech financing product innovation can play a role in supporting the growth and development of halal UMKM and provide guidance for industry players, and other stakeholders in strengthening the halal UMKM financing ecosystem through sharia fintech.

INTRODUCTION

An encouraging development in the 20th century was the rise of Muslims in various aspects of life. In the field of finance, the idea emerged to overhaul the financial system by eliminating its main instrument, interest. This step was taken to achieve consistency in applying the fundamental principles of Islamic teachings, such as justice, honesty and benevolence. Discussing the role of something cannot be separated from its function and position.

One of the financial institutions that operate with a profit-sharing system today is Sharia Bank, Sharia Insurance, Sharia Money Market, Sharia Capital Market, Baitu Maal Wattamwil, and Sharia Pawnshop. The presence of these financial institutions is expected to reach the lower strata of society, introduce, and utilise their financial services. The essence of economic activity is how humans can fulfil their needs to achieve prosperity in this world and the hereafter (falah).

Indonesia, as a country with a majority Muslim population, has great potential to restore its economic condition through the development of the Sharia Economic System. By implementing Islamic economic strategies, Indonesia can improve its economic stability (Amrin, 2022). Islamic economics shows good and rapid growth in the midst of the global economic downturn and turmoil due to the economic and monetary crisis. This is evidenced by the growth and development of economic and financial institutions that are guided by Islamic values, namely the Qur'an and Hadith. Islamic economics not only offers solutions that are in accordance with Islamic principles, but can also strengthen the foundations of the national economy.

The rapid advancement of digital technology has encouraged the Ministry of Tourism to formulate a new strategy by offering 100 digital destinations and nomadic tourism to achieve the target of foreign tourist visits (Maritim, 2019). The presence of e-marketing based on

Financial Technology (Fintech) is able to bring new nuances to the tourism sector in Indonesia. In the midst of various tourism performance challenges, e-marketing can strengthen the attractiveness of foreign tourism, while Fintech facilitates financial transactions with a wide range and high efficiency.

In addition, Fintech can provide great benefits to UMKM players, including halal UMKM, which can be empowered through the tourism sector. Shariah-compliant fintech is also emerging, offering funding solutions and financial transactions that comply with shariah law, especially for Muslims. This is important so that economic activities remain based on sharia principles and values.

The presence of financing institutions such as banks plays an important role in providing financing products, both for consumptive and productive purposes, for the community and the business world. This role can be seen from the dominance of banks in the Indonesian financial industry, with the demand for financing products continuing to increase. This increase has encouraged the emergence of other institutions with similar functions, such as multifinance institutions, pawnshops, and venture capital.

The development of technology today, provides innovation in the distribution of financing continues to grow. People can now apply for financing online without having to come to the office of a financial institution. This innovation is behind the emergence

of Financial Technology (Fintech) institutions. The realisation of financing by fintech showed an increasing trend from December 2018 to April 2022. OJK noted that in April 2022, the distribution of fintech financing reached IDR38.68 trillion, up 181.3% compared to the previous year. This increase shows that the fintech sector has bright business prospects, supported by technological advantages that facilitate access to financial services, including financing applications.

OJK data shows that there are 102 fintech institutions in Indonesia, consisting of 95 conventional fintechs and 7 sharia fintechs. As of March 2022, the total assets of all fintech institutions reached Rp4.52 trillion, with conventional fintech holding the largest assets of Rp4.43 trillion, while sharia fintech had total assets of Rp91 billion.

Although the total assets of sharia fintech are relatively low, this institution is still able to compete in the distribution of financing to the public. The majority of Indonesia's Muslim population is a great opportunity for Islamic fintech to expand financing. In addition, technological advantages provide a significant impetus for the development of Islamic fintech in the future. The market potential of Islamic fintech is also large, supported by the sizeable halal industry in Indonesia.

According to the 2019 Global Islamic Report, the potential of the halal industry in Indonesia is estimated to reach IDR3,000 trillion. The largest potential is in the halal food sector with

a value of IDR2,422 trillion, followed by the fashion sector with IDR294 trillion, and tourism with IDR154 trillion. Other sectors such as media, pharmaceuticals, beauty equipment, and Hajj Umrah have potentials of around Rp140 trillion, Rp70 trillion, and Rp56 trillion, respectively.

This huge business opportunity can have a significant impact on the national economy. Therefore, synergy between industry players and financial institutions is essential to maximise these opportunities. The contribution of Islamic fintech is crucial, especially with the use of technology that facilitates access to financing for business actors. Innovation in financing models is also an attractive alternative choice for business actors.

Islamic fintech business models emphasise various types of products such as crowdfunding, microfinancing, investment, and digital payment systems. Most of the Islamic fintech industry registered with OJK focuses on microfinancing, offering financial products such as working capital financing, services, and consumption. Islamic fintech operations are based on DSN-MUI fatwa No. 117/DSN-MUI/IX/2018 on information technology-based financing services that follow sharia principles. This fatwa, along with other fatwas on Islamic financial products, serves as the basis for Islamic fintech in developing financing products for businesses, especially to accelerate the development of the halal industry ecosystem in

Indonesia. Financing distribution by the fintech industry is aimed at small and medium enterprises (SMEs).

The stable performance of Islamic fintech can support the acceleration of business actors in the halal industry, such as UMKM. Rahmawati et al (2020) stated that the existence of Islamic fintech in Indonesia is closely related to the increase in UMKM businesses. Hasan, Rabbani, and Daouia (2021) state that the Islamic financing model is an important instrument in optimising the role of the Islamic financial industry in the development of the halal industry. Khan et al (2021) gave an example of a fintech financing model for the agricultural industry using waqf funds, where Islamic fintech can cooperate with waqf agencies in providing business funds which are then channeled to business actors such as farmers, using Islamic financing contracts such as mudharabah.

However, Islamic fintech institutions also need to develop technology to expand access to financing. Glavina, Aidrus, and Trusova (2021) stated that Islamic fintech should develop application-based technology to facilitate industry players, including in the distribution of financing. This application can be a literacy tool for industry players to choose a financing model that suits their business characteristics. This will support easy access to financing, make sharia fintech products an alternative for UMKM to meet capital needs, and support the acceleration of economic recovery

because UMKM are the main contributors to economic growth.

The number of UMKM that have been integrated with the digital ecosystem reached 12 million as of June 2021, or around 19% of the total national UMKM. The government targets 30 million digitally integrated UMKM by 2024. This condition creates opportunities for collaboration between UMKM and fintechs as financing providers. Chua, Yua, and Aye (2018) stated that the variety of financing products is one of the advantages that can encourage the competitiveness of fintech financing distribution, providing alternatives for people to choose financing models and contracts that suit the characteristics of their businesses.

This research aims to optimise the role of Islamic fintech in supporting the development of the halal industry by providing Islamic financing models and developing technology. The goal is to create a strong collaboration in the Islamic financial ecosystem, especially for the development of the national halal industry through UMKM businesses.

RESEARCH METHODOLOGI

This research method is structured with a literature review approach to explore the role of Islamic fintech in improving financial inclusion for halal UMKM. In addition, this method can incorporate exploratory studies.

This research uses a type of literature study with various sources as its main method. The nature of this research is descriptive qualitative,

which aims to explain the benefits, innovations and problems that arise from the use of fintech towards the development of UMKM in Indonesia. This research focuses on describing and explaining the findings regarding the benefits felt by UMKM and the challenges faced by the existence of sharia fintech in accordance with Islamic teachings.

This research uses secondary data, which is data taken by researchers to support scientific research through various sources such as journals, magazines, the internet, scientific papers, articles, and other sources. Data collection is carried out with several methods of literature study, which aims to find theoretical foundations relevant to the workings and concepts of fintech that are growing rapidly in this modern era, ensuring its suitability with Islamic principles, as well as understanding the benefits and obstacles faced in the development of fintech to help improve UMKM in Indonesia.

The data generated in this research is descriptive, coming from oral statements, writings, as well as observations of a situation. By combining these various approaches, this research aims to provide a comprehensive understanding of how financing product innovation through Islamic fintech can effectively support the growth of halal UMKM.

RESULTS AND DISCUSSION

This section will discuss micro, small and medium enterprises, the role

of Islamic fintech in the halal industry ecosystem, challenges and opportunities in the development of Islamic fintech, and innovation in Islamic fintech financing products.

Micro, Small and Medium Enterprises (UMKM).

According to Law No. 20/2008 on Micro, Small, and Medium Enterprises (UMKM), the classification of UMKM businesses consists of three categories, namely: 1) Micro enterprises are productive businesses owned by individuals or individual business entities that fulfil the criteria as micro enterprises in accordance with the provisions stated in this law; 2) Small enterprises are productive economic businesses that stand alone, conducted by individuals or business entities that are not subsidiaries or branches of companies affiliated with medium or large enterprises, and qualify as small businesses in accordance with the provisions in this law; 3) Medium-sized enterprises are productive economic businesses that stand alone, conducted by individuals or business entities that are not subsidiaries or branches of companies affiliated with small or large enterprises, and have a total net worth or annual sales results in accordance with the provisions in this law.

According to BPS data from the SE2016-Continuation results, the percentage of micro enterprises (MSEs) in Indonesia reached 98.68 per cent of the total number of businesses in the country. MSEs are spread across

various non-agricultural categories, with Wholesale and Retail Trade, Repair, and Maintenance of Cars and Motorcycles (Category G) being the most dominant, accounting for almost half of the total. Accommodation and Food Service Enterprises (Category I) and Manufacturing Enterprises (Category C) also contributed significantly, at more than 16 per cent each.

The main advantages of MSEs include their ease of adopting business innovations, especially in technology. Smaller scopes allow for better employee relations, while the flexibility to adapt the business to dynamic market changes is also an important factor. From 2009 to 2017, the number of UMKM in Indonesia increased from 52.21 million businesses to 64.19 million businesses. This represents a growth of 116 per cent from 2012 to 2018.

Based on Law No. 20/2008 on Micro, Small, and Medium Enterprises, UMKM play an important role in expanding employment, increasing GDP, and providing an economic safety net, especially for low-income communities. BPS data from SE2016-Lanjutan shows that UMKM contribute up to 89.2 per cent of the total workforce, 99 per cent of employment, 60.34 per cent of national GDP, 14.17 per cent of total exports, and 58.18 per cent of total investment. UMKM in Indonesia need to adopt business innovation, especially

in technology, as digital technology is expected to increase.

However, UMKM businesses still face challenges in accessing digital financial services, with key constraints including competitors and liquidity. Although the government has issued policies to provide UMKM with access to credit, only a small percentage utilise it, citing reasons such as high interest rates, lack of knowledge about procedures, and difficulties in the lending process. However, the Indonesian government has given great support to the development of the digital economy, including through the UMKM Go Digital programme. The fintech sector is a promising financial solution for UMKM, as it provides easy access and online service processes. The support of affordable smartphones and downloadable applications also facilitates UMKM' access to fintech services.

The Role of Islamic Fintech in the Halal Industry Ecosystem

Fintech is a new financing model that has changed the business model from conventional to digital. Previously, transactions had to be done face-to-face, but now they can be done online in a very short time without the need to meet in person. According to fintech observer Hasnil Fajri, since the beginning of 2018, smartphone users in Indonesia are estimated to reach around 177.9 million people, with 132.7 million of them being internet users. This condition

makes fintech the new favourite in digital financial transactions.

Data from the Indonesian Fintech Association (Aftech) shows that the majority of fintech service users are young millennials aged 25-35 years, with a monthly income between Rp5 million and Rp15 million. This group is already tech-savvy, making it easier to adopt fintech services. Another fact shows that while sharia finance is often considered old-fashioned and complicated, the presence of sharia fintech can change that stigma. Islamic fintech makes transactions easier and, over time, the Islamic finance industry is predicted to develop with technological innovations on par with conventional fintech.

However, in 2019, the financial inclusion index was still below the target of 75 per cent, indicating low financial knowledge among Indonesians. This needs to be improved with financial technology innovation. The presence of fintech and its innovations brings fresh air to Indonesians who have been struggling to access financial services. Fintech can connect UMKM players with financial services that were previously unreachable by banks. Access to financial services is no longer a luxury; money transfers, searching for bank and non-bank financial products, and applying for loans can now be done remotely in a short time. This convenience further strengthens the role of fintech in supporting the national economy and the transformation from

conventional models to the digital era (Ariyanti, 2019).

The presence of Fintech provides alternative funding to UMKM players who have difficulty getting support from traditional financial institutions. The approach is done online through an online contract or contract using a smartphone, by complying with the regulated sharia principles.

Article 21 of Supreme Court Regulation Number 2 of 2008 concerning the compilation of sharia economic law mandates that contracts must fulfil a number of requirements, such as voluntary, trustworthy, prudential, unchanging, mutually beneficial, equality, transparency, ability, convenience, good faith, and halal cause. Sharia Fintech provides easy funding to UMKM players with a spirit of partnership, not through the debtor and creditor approach commonly taken by conventional Fintech. This approach provides greater potential for Islamic Fintech to be accepted by the community because it promotes economic transactions as a joint effort for the benefit of the people, not just to achieve individual business goals.

Challenges and Opportunities in the Development of Islamic Fintech

One of the main challenges in the use of fintech in Islamic banking is ensuring Shariah compliance. The use of this technology requires special attention to data security and customer privacy and faces challenges related to relevant regulations and legal frameworks. Islamic banking should

work closely with Shariah experts to ensure that the technologies and products implemented are compliant with the principles of Islamic finance, while maintaining a high level of security to protect customer information from cybercrime threats. Adequate regulatory clarity is also needed to support fintech innovation while ensuring compliance with Shariah principles and protecting customer interests. It is also important to raise the level of education and awareness about fintech among the public and Islamic banking customers to address any misunderstandings and concerns that may arise regarding the use of technology in the context of Islamic banking.

The opportunity for the development of Islamic economics and finance, including Islamic fintech in Indonesia, is enormous. This is because Indonesia has the largest Muslim population in the world. Functionally, there is no difference between Islamic fintech and conventional fintech, both provide financial services. The difference lies in the contract used, where sharia fintech follows the rules of Islamic law. The legal umbrella is the same, which is based on the Financial Services Authority Regulation (POJK) number 77 of 2016 concerning Information Technology-Based Money Lending and Borrowing Services. In addition, sharia fintech also refers to the Fatwa of the National Sharia Council of the Indonesian Ulema Council No. 117 of 2018 concerning Information

Technology-Based Financing Services Based on Sharia Principles.

Apart from regulations, there are other aspects that need to be considered to develop Fintech in Indonesia, namely:

1. Licensing;
2. Company bylaws;
3. Agreement/contract;
4. Proof of asset ownership;
5. Legal dispute;
6. Taxation.

These six things are important points that need to be considered by Fintech business developers in Indonesia so that Fintech business operations run smoothly. There are a number of benefits offered by Sharia Fintech, including:

- a. Helping UMKM players by providing funding that is easier, cheaper, faster, and more efficient than the complicated requirements often proposed by banks;
- b. Prioritising sharia principles that are free from usury, with funding based on the principle of profit sharing so that it is safer for UMKM players;
- c. Becoming a bridge between fund owners and those who need funds, thus providing economic benefits not only for the upper middle class but also for UMKM activists;
- d. A transaction process that is easily accessed online through smartphones and the internet; and
- e. Higher security because there is no interest that harms other parties and

is regulated by regulations from DSN-MUI and OJK.

Seeing the importance of the contribution of Islamic Fintech, OJK officially approved the Indonesian Islamic Fintech Association (AFSI) as an Islamic Fintech association supervised by OJK for the Islamic financial technology industry. This move is expected to support the development and innovation of Sharia Fintech in the face of the digital market in Indonesia, as well as ensure stricter supervision of financing practices and financial transactions. It also brings clarity in the regulation of the Islamic financial technology industry in Indonesia, enabling Islamic Fintech to better compete with conventional Fintech.

Sharia Fintech Financing Product Innovation.

The hope for Small, Micro and Medium Enterprises (UMKM) entrepreneurs in developing their business includes easy access to financing. Fintech such as Peer-to-Peer (P2P) lending is a solution for UMKM activists who find it difficult to gain access to traditional financial institutions.

Through Fintech, UMKM that were previously difficult to access by financial institutions become more accessible. In the long run, Fintech has the potential to increase the capacity and growth of UMKM. The government also supports UMKM through a number of programmes, including Kredit Usaha

Rakyat (KUR), which has been launched since 2007. To accelerate the development of UMKM, the Financing Policy Committee for UMKM decided to change the KUR policy by lowering interest rates, increasing the total KUR ceiling, and increasing the Micro KUR ceiling per debtor.

Nonetheless, according to the latest data from OJK, only a small fraction of the total registered Fintech startups are Islamic Fintechs. Technology development has made financial services more affordable, faster, and easier, and Fintech has an important role in providing solutions for UMKM players. One of the main challenges for Fintech in supporting UMKM in the future is to increase Indonesians' access to financial services, with surveys showing that there is still a large proportion of people who have not used financial products.

Innovation in business models and product development is a key element in maintaining business sustainability, as stated by Evans and colleagues (2017), who assert that innovation supports future business development. Intense competition in the financial sector encourages financial institutions, both banks and non-banks, to continue to innovate to maintain their existence and competitiveness.

Islamic fintech plays an important role as an intermediary between fund owners and those who need funds, especially UMKM. To perform its role effectively, Islamic fintech needs to develop financial products that can

support the acceleration of its role in channelling funding. Some common products offered by Islamic fintech institutions include multipurpose financing, community-based business capital, service-based financing, and financing and accounts receivable collection services. For example, the multipurpose financing model uses a murabaha contract, while the community-based financing model uses a musyarakah scheme.

Islamic fintech also provides service-based financing, where the institution will receive a service fee for the financing provided. For financing and accounts receivable collection services, fintech assists in funding as well as issuing invoices that will be billed to third parties. Nonetheless, despite these innovative products, the asset growth of Islamic fintech is still lower than that of conventional fintech, despite its positive impact in driving the acceleration of Islamic fintech financing in Indonesia.

An increase in fintech financing to the UMKM sector has occurred in recent months, supported by the domestic economic recovery that fuelled growth in economic activity. This phenomenon has a positive impact on the demand for UMKM financing to fintech.

This situation opens up opportunities for Islamic fintechs to expand their market share and contribute to the development of UMKM within the national halal industry ecosystem. There are several

Islamic fintech products currently available that need to be further developed to provide wider funding alternatives to UMKM players. Hashfi & Zusryn (2019).

Highlighting several types of contracts that can be used as alternatives to be developed as Islamic fintech funding contracts, such as Ijarah Muntahiyah Bit'Tamlik (IMBT) and hawalah.

The implementation of the IMBT contract can allow fintech to provide working capital equipment to UMKM businesses with a rental system that will end with a handover to UMKM businesses. On the other hand, Alam, Sukmana, and Melani (2021) revealed that the implementation of IMBT can also be an alternative contract to manage risks for microfinance institutions in handling financial risks in the distribution of financing products. Therefore, Islamic fintech can optimally utilise this contract as an anticipatory step against risky financing.

Another contract that can be implemented by Islamic fintech is Musyarakah Mutanaqishah (MMQ), which is commonly used by Islamic banks for takeover financing products, such as houses and cars. However, this contract can also be implemented by other Islamic financial institutions, including fintech.

The MMQ agreement can be used in takeover financing products for UMKM players, such as working capital financing. For example, if an UMKM player has financing at a

conventional financial institution and wants to switch to sharia fintech financing services, the fintech can use a takeover scheme by paying off all UMKM financing at the previous institution. Then, sharia fintech and UMKM will enter into an agreement with the MMQ contract, where both will conduct a joint venture or share ownership of the shophouse. UMKM will pay in instalments as a gradual takeover of sharia fintech's ownership of the shophouse.

In addition, another alternative contract that can be utilised by Islamic fintech is based on productive waqf. Waqf contracts are becoming a trend in the Islamic financial ecosystem because they can be a new innovation in improving community welfare through community social funds. The implementation of waqf contracts in financing Islamic fintech institutions can be done in certain sectors, such as agriculture. The way it is implemented is by financing equipment for farmers. To obtain waqf funding, Islamic fintech can collaborate with the national waqf agency, where fintech is responsible for channelling funds collected by the waqf agency to communities or UMKM players who need capital assistance.

The integration of financing platforms is done to make it easier for UMKM players to access financing from Islamic fintech. UMKM will apply for financing through the websites of institutions that have collaborated with sharia fintech, so that it will facilitate the process of applying for and

administering financing. On the other hand, this can support the increase in financial inclusion of Islamic financial products and accelerate the distribution of more financing in the future.

Writing Tables and Figures

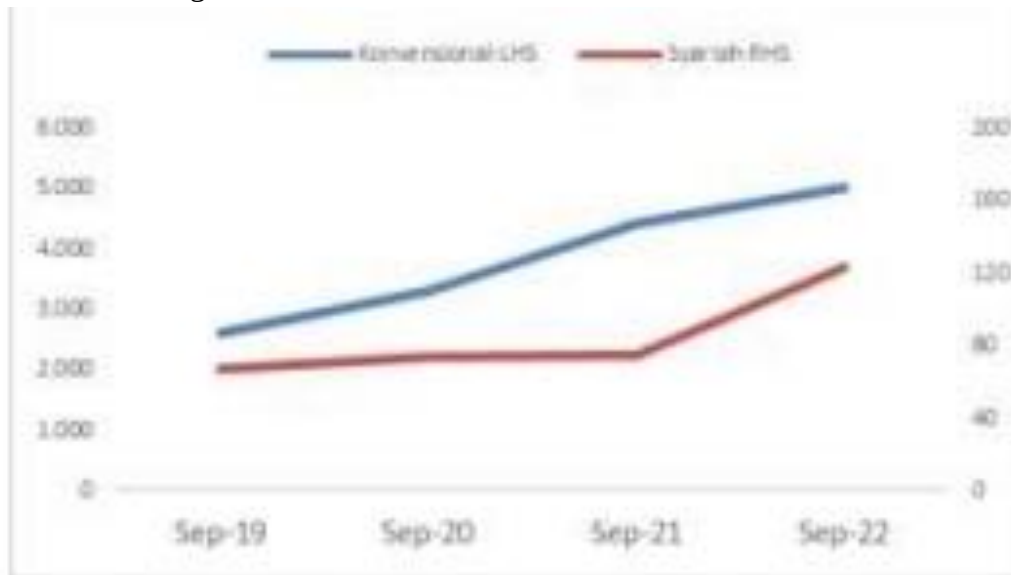


Figure 1: Development of Fintech Assets in Indonesia

Source: OJK (2022)

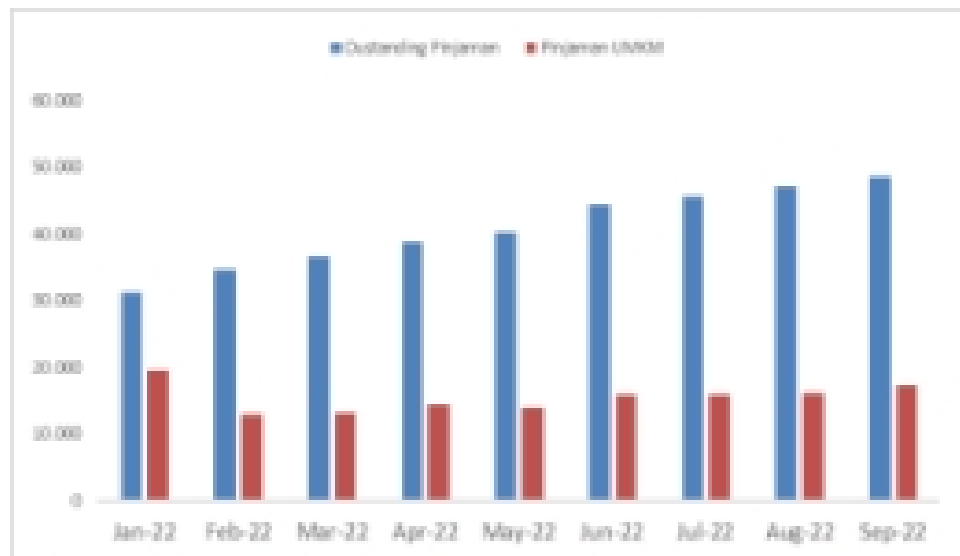


Figure 2: Financing Distribution by Fintech in Indonesia

Source : OJK (2022)

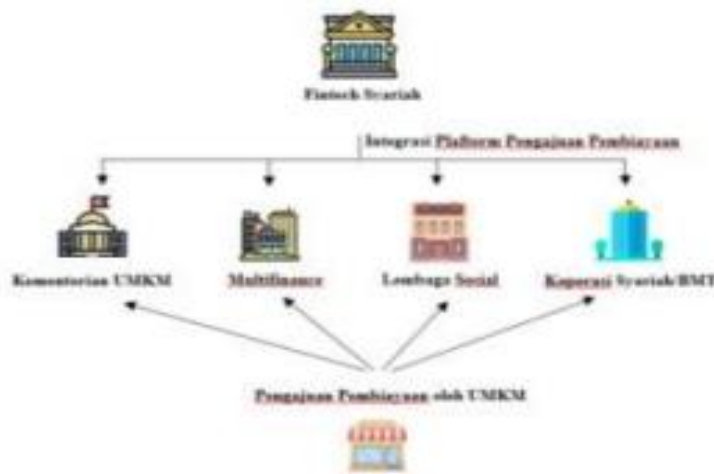


Figure 3: Development of Sharia Fintech Financing Technology Access Through Platform Integration.

Source: Lilis (2022)

CONCLUSION

Based on the research results, it can be concluded that the existence of Islamic fintech in Indonesia has an important role in increasing the inclusion of Islamic financial products for the community, especially UMKM businesses. Innovation in financing models aims to provide alternatives to UMKM businesses so that they can choose products that suit their business needs and cash flow. In addition, this innovation also helps Islamic fintechs to expand the variety of financing products they offer, thereby encouraging the growth of this industry in the future.

Several alternative contracts, such as IMBT, MMQ, and waqf, can be an option for Islamic fintech in developing financing products for UMKM players. The development of this financing model needs to be supported by expanding access to technology through platform integration

with various institutions, such as the Ministry of UMKM, multifinance companies, social institutions, and sharia cooperatives/BMTs. This aims to facilitate UMKM players in accessing financing from Islamic fintech institutions.

The development of Islamic fintech also needs attention from regulators in the future, especially considering the increasing trend of financing distribution to the UMKM sector after Covid-19. Regulations that can facilitate Islamic fintech in providing financial products that support the business development of UMKM players need to be drafted. This is expected to have a multiplier effect on the national economy through the growth of UMKM businesses and increased Islamic financial inclusion.

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