Integration of Islamic Finance with ESG Sustainability Efforts Evidence in Malaysia

Nurul Afzan Najid[1*], Amirul Afif Muhamat[2], Mohamad Nizam Jaafar[3]

[1]Faculty of Accountancy, UiTM Cawangan Pahang Kampus Raub,Malaysia

[2]Faculty of Business and Management, Shah Alam, Malaysia

[3]Faculty of Arshad Ayub Graduate Business School, Universiti Teknologi MARA Shah Alam, Malaysia

***Corresponding author**

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ABSTRACT

This paper studies the integration of Islamic banking into worldwide sustainability initiatives, which in turn underlines the special role of Islamic financial principles in the process of achieving environmental, social, and governance (ESG) goals. Islamic finance, which is built upon ethical principles such as the ban on interest (riba), uncertainty (gharar), and investments in harmful businesses (haram), by default, promotes the goals of sustainable finance. The research was based on qualitative approaches, mainly the grounded theory to examine the feedback from different people in the Islamic finance field. This technique helps in the determination of important themes, which are Principles and Ethics, Financial Products and Services, Sustainability and ESG, Global Integration and Education, and Challenges and Opportunities. The findings show that Islamic finance has a vast potential on global sustainability to be increased by the introduction of innovative financial instruments, for instance, Green Sukuk and Islamic microfinance. However, the obstacles which include the lack of standardization and the inadequate knowledge beyond the areas with a Muslim majorities keep on existing. The paper presents the methods to address the problem, such as the creation of better regulatory frameworks and the project of educational programs to encourage a more effective integration of Islamic finance with the global sustainability projects.This paper also aims to propose framework on the aligning Islamic finance and the global sustainability efforts. Future research should give the highest emphasis to the development of the quantitative methods for evaluating the influence of Islamic financial products on the sustainability outcomes. Besides, it should also check the effectiveness of the particular laws that are certain to increase the acceptance of the same phenomenon in the non-Muslim markets. The Islamic finance may overcome these problems and research these chances, thus, making its contribution to the global sustainability to increase, and also becoming an example for the ethical and socially conscious investing.

Keywords: IslamicFinance,Sustainability,ESG,sustainable finance framework

INTRODUCTION

Lately, there has been a worldwide rise of the awareness of sustainable finance as it is realized by the stakeholders of different sectors that there is a strong need to tackle the environmental, social, and governance (ESG) issues. The ESG component consists of 3 aspects: the following standards can be mentioned: environmental, social, and governance. In the light of the knowledge with the help of the study of Steblianskaia et al. (2023), it is understood that, ESG is a system that is used in the assessment of organisation's non-financial performance regarding sustainability and ethical concerns. ESG is a structure used in measuring a company's mode of working with reference to the environmental, social and the governance structures. In this regard, ESG investors use strategies of quantitative management of risks through equity risk reduction to avoid loss-making situations or get maximum profit for the investor, rather than for the business. ESG-screened investments are thought of as interesting investments because they are concerned about companies that have a higher chance of long-term success and they can also reduce the risks for investors (Li et al. , 2021). The change implies an increasing consciousness of the lasting consequences of the financial decisions on the society and the planet. As part of this broader trend, sustainable finance has gained prominence as a key approach to addressing global challenges such as climate change, inequality, and corporate governance. Sustainable finance encompasses financial strategies that integrate ESG criteria into business or investment choices with the aim of advancing environmental preservation, social equity, and efficient governance. Malaysia, which has been the leader in the Islamic finance field, is now at the point where it can use its huge Islamic financial sector to help the sustainable development to be achieved. The Islamic finance, which strictly adheres to the Sharia principles, including the prohibition of interest (riba) and the focus on the ethical investment, naturally is in line with the goals of the sustainable finance. These principles not only ban the investments in the industries that are harmful to the community but also regulate the investments that are useful for the community and hence, encourages the greater sustainability goals. Hence, the funding of the illegal sectors, for instance, alcohol, tobacco, and gambling, is not at all put on the list.

Even though these synergies are inherent, the actual integration of Islamic finance with ESG-oriented initiatives in Malaysia is still limited. As per Harahap et al. (2023), the connection between Islamic finance and ESG goals is still not well explored and is unclear. This gap is considerable considering the fact that Islamic finance can finance large-scale sustainable projects through the introduction of new products such as green Sukuk and Islamic microfinance. The integration challenges are multi-layered, consisting of regulatory obstacles, market readiness, and a lack of harmony in the application of sustainability standards in Islamic financial practices (Hammod, 2022; Pengally, 2022). The main problem that lies behind the combination of ESG and Islamic finance is the possible differences in their methods of risk management and the investment decision-making. Although ESG investing deals with the evaluation of investments based on environmental, social, and governance risks, Islamic finance concentrates on the principles of risk-sharing and the avoidance of excessive uncertainty and speculation. The different views on risk management of the two frameworks may be the reason for the difficulties to combine them and to have a smooth integration. This, in turn, will increase the cost and complexity of the investment process (Lawrence & Hewitt, 2022). Besides, research has shown the low usage of active ESG integration and ownership practices in Islamic finance institutions compared to the conventional ones. This indicates a split between the degree of ESG considerations that are being given priority and being implemented in the Islamic finance sector, although they have the same values and the potential synergies between them. This, in turn, can restrict the growth potential of ESG investments in Islamic finance (Pengelly, 2022).

In order to address these problems and the gaps, further qualitative and quantitative analysis is needed to identify the further implications, prospects and challenges, which Islamic finance means when adopting ESG principles. Studying this crossing allows researchers to contribute to the development of such approaches in constructing a more holistic interrelated cross connecting these two systems of finance based on their shared values and principles. Some researches concerned with ESG and Islamic finance are Al Adawiyah et al.(2023) who investigated the bibliometric computational mapping for sustainability publications and Islamic finance; Kashi & Shah (2023) who conducted a bibliometric review of sustainable finance; Hassan et al.(2021) who described the literature on The role of Islamic finance to sustainability is very significant, so the discussion on the two topics is vital as how far and deeper Thus, the aim of this research is to discover how improvements could be made to the synchronization between the principles of Islamic finance and the sustainability objectives in Malaysia.. It is designed to reveal the mechanisms by which Islamic finance can contribute to sustainable development and to assess the current challenges and opportunities in this process. Thus, the research will offer the understanding of the ways to improve the regulatory frameworks and the strategies for the promotion of the Islamic finance to the sustainable development of Malaysia. The importance of this research is not only in the filling of the academic gap but also in the influence on the policy-making and the practical applications in the financial industry. Malaysia keeps on being the leader in the Islamic finance market and with this, the understanding and utilization of this alignment will make the country a world center for sustainable Islamic finance and hence, a model for other countries that have a similar economic and financial situation.

LITERATURE REVIEW

Islamic Finance and Environmental,Social and Governance (ESG)

Islamic Finance, the alternative to the financial system, has appeared since 1970s and is now developing rapidly because of its unique principles that aim for justice and other ethical and religious goals (Warde, 2014). The principle of Islamic finance is based on its ethico-faith which is derived from the Islamic law, the prohibition of riba (unjustified increase), gharar (uncertainty, risk and speculation) and aims to promote economic and social justice without being solely profit maximization in conducting a business. This feature is connected with the promotion of sustainability, which in Islamic finance, the promotion of social welfare, social inclusion, and being environmentally friendly are part of Islamic finance’s goals which thus makes Islamic finance principles also aligned with the ESG concepts. The comparison between these entities is clear because of their common values, their agreement with sustainability, their possible overlap, and their similar investment methods (Fadzillah, 2023; PWC, 2022; CFA Institute, 2019). It is evident that, the principles of Islamic finance, which are based on the Maqasid al-Shariah, are very much aligned with the aims and objectives of the ESG goals. Moreover, inclusion of ESG criteria in Islamic finance can bring a number of benefits, for instance, the promotion of sustainability and ethical behavior, diversification of risks and revenue sources, and compliance with the general principles. This area is very likely to have substantial global potential both in terms of growth and "Green" credentials (Hammod, 2022).The Islamic finance industry is pushing the companies that are connected to the sectors or industries that add value to the real economy. The investments in the fixed-income financial instruments, for example, preferred stock, bonds, and some derivatives are not allowed, as they promise a fixed rate of return and do not give voting rights. Moreover, Islamic investors are not permitted to buy shares of companies whose main business activities are alcohol, gambling, conventional financial services, entertainment, products related to pork, tobacco, and weapons. Islamic finance, the one which is founded on the principles of Shariah law, has also been studying the incorporation of ESG principles into its activities.ESG was first created in 2005 in a research paper named Who cares Wins by the UN Global Compact.

ESG investments are a type of sustainable investment which is a term for investment portfolios that, in addition to seeking positive returns, also evaluate and consider the long-term impact of business practices on society, the environment and the business performance alone. The Schroders Environmental, Social and Governance Policy includes a number of activities that recognize the links between companies, the communities and the environment in which they operate and also the relationship between companies and their controlling shareholders (Miskam & Abdullah, 2021). According to Shen (2023) the international ESG concept and evaluation system represent a holistic approach made up of three aspects: Countries have also international organizations that establish regulations on ESG disclosure and reporting, corporate ESG ratings issued by rating agencies, and ESG investment guidance issued by investment institutions. Through the introduction of these elements, the system wants to facilitate the transparency, accountability and long term value creation for the companies and their stakeholders.Kumar’s research in 2022 informs that there are seven main research themes of sustainable finance, such as socially responsible investment, climate finance, impact investment, carbon finance, energy financing, and governance of sustainable financing and investment. The corporate events in the sustainable finance are yet to be greenwashed and the study of this issue is in the very beginning stage. Greenwashing is a deliberate process in corporate events. This will ultimately lead to a decrease of investor confidence in the companies that follow ESG principles (Kumajas, et. al. , 2022). Though looking at emerging markets, it is proved that the introduction of ESG in Malaysian listed companies adds the value. Thus, the inclusion of ESG factors in Islamic finance can help in meeting the demand to that effect and, at the same time, attract more investors. Moreover, the global standards and initiatives like the UN's Sustainable Development Goals (SDGs) which aim at promoting sustainability and social responsibility are the examples of the alignment with the global standards. ESG factors can be integrated into Islamic finance, which can be in congruence with these global standards and initiatives. Moreover, the integration of ESG factors into Islamic finance can not only boost the industry's reputation but also increase the reputations. Islamic finance can be seen as something that is acting responsiblely and ethically towards the environment and the society because by promoting sustainability and social responsibility, Islamic finance can be the alternative to the conventional finance (Jawad & Abdulla, 2022)

RESEARCH METHOD

In this paper, a qualitative research method was employed, which concentrated on the feelings and opinions of the stakeholders in the Islamic finance sector. The study uses a qualitative research design to examine the linkage between Islamic finance and the worldwide sustainability projects. This design is the basis to perceive the Islamic finance in all the aspects, the principles, challenges and opportunities, and how they can be united with the global ESG (Environmental, Social, and Governance) goals. The empirical investigation is the step of the study which is carried out by the method of interviewing the stakeholders and the analysis of their answers to discover the patterns, themes, and the frameworks.

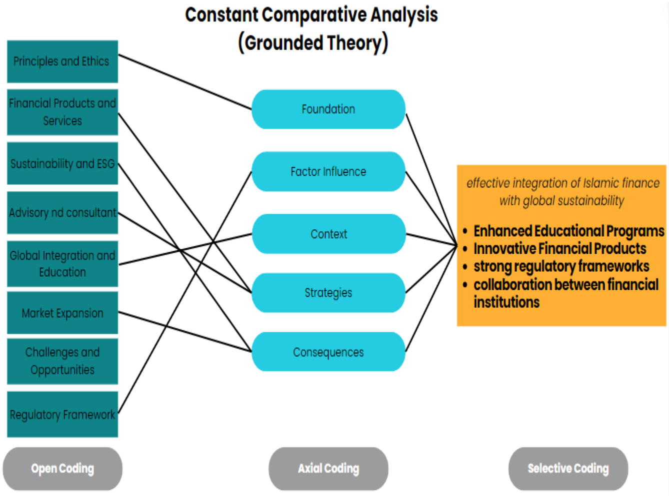

Figure 1.0 :Grounded Theory

Data was collected through a selection of semi-structured interviews conducted with key stakeholders in the Islamic finance industry. The semi-structured interviews were selected because of their flexibility that allows the interviewers to tailor the questions according to the respondent's answers, but at the same time, they still cover the topics that interests the researcher. The investigation of this technique helped in getting rich, detailed responses and also made it possible to compare the responses of the participants. The participants were chosen by a sampling technique that is designed to be best for the purpose (Creswell,2014). This approach involves focusing on individuals who possess the necessary expertise and experience, as it is a strategy that prioritizes concentration in this regard. Besides, it was best to choose the people who best matched the criteria for the interview. (Kumar,2011). For key participants,preference was given to those from the senior management level as it is suitable and credible source in providing relevant information for the study (Falses and Johansson,2015). The criteria of the participants are: 1) expertise in Islamic finance; 2) over 10 years of professional experience 3) variety of viewpoints and 4) wide range of experience with ESG practices. The session of the interview lasted for around 1 hour. The participants' names were not disclosed and were denoted as participants 1-4 in the study to ensure their privacy as per Table 1.

Table1:Interview participants

BIL.	PARTICIPANT	MANAGEMENT LEVEL
1	Participant 1	Executives in islamic banking
2	Participant 2	Sharia advisor
3	Participant 3	Senior Officer Financial Authorities
4	Participant 4	Senior Academician,expert in Islamic Finance

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The data was examined through the grounded theory technique which is illustrated at Figure 1. 0. The grounded theory research process consists of three stages of coding: Open coding, axial coding, and selective coding are the main components of the grounded theory method. These coding stages were the reason for the identification of the key themes and connections in the qualitative data. The first phase is the open coding, which is the process of the interview responses of the participants being cut into a few codes that aid in the identification of the key themes and concepts. These approaches are used to unveil the main themes like principles and ethics, financial products and services, sustainability and ESG, advisory and consultant, global integration and education, market expansion,regulatory framework and challenges and opportunities. Then, the given research uses axial coding. In this stage, the links between the codes were pointed out and sorted out into bigger categories which exposed the relations between the principles, products, and ESG goals. In the last phase, selective coding is done with the main aims of disseminating and developing the theory. The main result in this case is the effective integration of Islamic finance with the global sustainability.

DISCUSSION

The link between Islamic finance and global sustainability illustrates that Islamic finance and the principles of sustainability are both based on ethics. This agreement is not a coincidence but it is the basic principle of Islamic finance that puts ethical, social, and environmental issues as the first thing in financial activities.Through grounded theory analysis it reveals several key dynamics in order to integrate Islamic Finance with global sustainability efforts.

Foundational principles and ethics

The participants underlined the fact that Islamic finance is based on the ethical principles that determine the way of doing business. These principles are not merely suggestions, but rather obligatory practices that ensure all financial activities comply with Sharia law, which prohibits interest (riba) and emphasizes risk sharing and fairness. This ethical base is the key factor since it makes Islamic finance different from the regular one and thus helps to build trust among its stakeholders. This natural compatibility can be used in the development of standardized practices that clearly set ESG compliance according to Islamic law.

Influential factors

The effect of the financial products that are designed in accordance with Islamic law and the emphasis on sustainability and ESG principles is huge. These aspects are very vital as they bear the two-fold dimensions of affective perception about Islamic finance and its utility in various economic contexts. By passing ESG policies that conform to Islamic ethical standards, Islamic finance remains in a vantage position to champion sustainable economic activities required by a wider populace of environmentally conscious and socially responsible clients. The Islamic finance institutions are creating new products for example; the Green Sukuk which is Shariah compliant as well as having sustainability features. Islamic microfinance is another important product within this portfolio. It also benefits the community in enhancing social justice and act as an economic enabler.. The comprehensive evaluation of these products' impact on sustainability renders it innovative by providing an authentic perspective on the effectiveness and areas for enhancement within the realm of Islamic finance.

Contextual elements

Guidance and consultancy together with international education about Islamic finance are the keys to its wider acceptance and global integration. Education is the tool that enables Islamic finance to be understood and accepted by non-traditional markets and consequently, it can be integrated worldwide. Correspondingly, the role of expert advisors is of utmost importance in guaranteeing that Islamic financial products are properly designed and that they are in accordance with both local and international regulations. These services will assist investors in the Sharia compliance process while at the same time giving them the necessary information about global regulatory frameworks. The appropriate advice thus guarantees that the investments are ethical and in line with international standards.

Strategies

The market expansion tactics and the methods of overcoming the obstacles are important factors for the development of Islamic finance. Thus, along with the generation of new markets also the adaptation to the evolving financial landscape which is influenced by the technological advancements and the changing regulations is also required. The difficulties that are being faced now and how to overcome them through proactive and innovative ideas are the main causes of the Islamic finance becoming relevant and competitive again.

Consequences

The regulation of Islamic finance is the key to its sustainable future development. These frameworks are the ones that make sure that financial practices are not only complied with the Sharia law but also with the international financial regulations. This double compliance is the key to be recognized as credible and trustworthy, which are the main reasons of the collaboration between Islamic and non-Islamic financial institutions. These collaborations can give rise to the development of more creative financial products that are in line with the cal standards and are liked by a wide range of investors.

From the key dynamics explained above, it is clear that the connection of Islamic finance with worldwide sustainability efforts is a promising field with natural correspondences. The challenges that Islamic finance has to overcome, such as standardization and awareness, and the opportunities that it has, such as innovative financial products and principles can significantly increase its role in global sustainability initiatives. Besides, the relationships between categories show the complex and dynamic interplay that is the basis for the widespread and big-market expansion of Islamic finance as an ethical and sustainable financial model.

Challenges and opportunities in the integration of Islamic Finance and global sustainability efforts

Islamic finance, rooted in Sharia principles, is exclusively used for investments that promote the well-being of individuals while avoiding any unlawful practices. The sustainable finance sector is gaining popularity worldwide, especially as the objectives of Environmental, Social, and Governance (ESG) principles are assuming a prominent role. Muslim finance is now recognized as being uniquely positioned to integrate both aspects. Despite of considerable effort put in, there are also challenges that should be addressed in assessing the effectiveness of the integration.

Lack of standardization

The absence of universal benchmarks for ESG compliant investments within Islamic finance hinders the development of consistent and widely accepted definitions. This, in turn, creates different interpretations of compliance that cause inconsistencies and problems in establishing a univocal framework. The study carried out by Pathan et al. (2022) was in line with the issues where Islamic finance is capable of funding green projects, but there are issues that need to be addressed, like the regulatory framework and the market misunderstandings for full integration of Islamic finance with sustainability. The participants highlighted the importance of this problem. Participants noted the critical nature of this issue.

"There is a need to unify standards for ESG-compliant investments in Islamic finance. Without this, we face varying interpretations that hinder the development of cohesive products and frameworks. It results in confusion among stakeholders and diminishes investor confidence." (Participant 1).

Therefore, the disparity in the interpretation of compliance results in confusion which in turn causes investor confidence in sustainable Islamic finance products to drop downwards. Besides, it may end up fragmenting markets thus constraining global integration and scaling up. To overcome these difficulties, standardization bodies and regulatory authorities, together, are working on the process of unification. Furthermore, the cooperation among Islamic finance institutions and international organizations is considering the joint standards of Sustainable Islamic financial products.

Awareness and Education: Awareness and education are crucial aspects that shape the successful integration of Islamic finance with sustainable finance and ESG goals. One of the participants mentioned that:

"It is very important for people di negara barat to learn more about and understand Islamic finance." So apa yang kita kena buat adalah we do come out with educational materials and programmes that not only explain what Islamic banking is and how it works, but also show how it can work with modern financial systems. " (Participant 1)

Even so, the general public is still unaware of the fundamental relationship that exists between Islamic finance and environmental sustainability. There are misconceptions about the suitability of Islamic finance as a tool in the sustainable investment agenda as a result of this cross-sectional approach. In many parts of the world, the population lacks exposure to Islamic finance practices due to the prevalence of conventional financial systems. Consequently, people are unfamiliar with the practical applications of Islamic finance or how its products, like green sukuk, are uniquely positioned to promote sustainable projects. Many people agree with the view claiming that Islamic finance is almost the same as conventional finance, with only slight modifications to adhere to Shariah laws. This view omits the fact that Islamic finance is built on ethical and social premise which fits into ESG approach because it shuns activities that may have negative impact on society and environment. Raising public awareness of the general compatibility between Islamic finance and sustainable investment will help the sector gain more credibility and interweave itself more with ESG practices. It is also important to note that there is scarcity of extensive and widely accessible educational materials and training that specifically deal with the intersection of IF and sustainable finance. While the majority of curricula presently focus on Islamic finance or sustainable finance, few integrate both subjects into their syllabi. A study conducted at Georgetown University Medical Center and Virginia Commonwealth University by Jamil et. al (2019) states a lot on the direction in trying to integrate sustainability to Islamic Accounting and Finance education. It especially calls for a deeper level of integration in order to adequately meet industry needs. Secondly, another issue emerging in the field of Islamic finance is the scarcity of knowledge and specialization in the area of sustainable finance. Islamic finance professionals may lack a comprehensive understanding of the specific criteria and execution of Environmental, Social, and Governance (ESG) principles. Similarly, ESG investors may lack comprehension of the intricacies of Sharia compliance, which encompasses restrictions on interest (riba) and unethical investments, guaranteeing equity in agreements, and advocating for social and environmental equity.

Regulatory Frameworks

Sustainably integrated Islamic financial products face challenges in terms of standardization and integration due to inadequate rules and regulations from the government. As mentioned by one of the paraticipant:

.............developing a robust regulatory framework and educating stakeholders about the synergies between ESG and Islamic finance are essential for better alignment..........."(Participant 3)

The regulatory frameworks in Malaysia play a significant role as they act as a connector for integrating Islamic finance with sustainable objectives such as the ESG. It will have to restructure in order to enable the harmony between Islamic finance and ESG features. Although Malaysia is a leading Islamic Fintech hub in the world, it, nevertheless, faces various challenges, both regulatory and policy wise, in regard to sustainable finance . Consequently,it is important to articulate such effective policies that Islamic finance may effectively contribute to the sustainable development in the whole world considering both the Islamic and ESG regulations. Even though the government has a proactive role in developing Islamic finance through the Central Bank of Malaysia (Bank Negara Malaysia) as well as the Securities Commission Malaysia, the absence of unified frameworks aimed specifically at the sustainability of Islamic financing remains one of the main obstacles. There are different understandings of the principles under Sharia and the different levels of ESG adoption among financial institutions lead to discordantness.

The divergence in approaches to sustainability poses a challenge in establishing a consensus on the definitions and standards of sustainable products in the context of Islamic finance. Despite Bank Negara Malaysia's implementation of the Value Based Intermediation (VBI) framework to align Islamic banking operations with

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sustainable practices, many financial institutions still struggle with ambiguity regarding its implementation. Also, the current level of adoption of ESG indices in banking still stands at a remarkably low level. Moreover, the guidelines derived are mostly voluntary, and therefore, one may find a wide disparity in how the different banks pertain to it. The understanding of rules and regulations complied with International Environmental, Social and Governance Standards, accompanied by covering all-round guidelines that includes incentive aspects, puts us in a competitive edge being a leading and well-recognized hub for Sustainable Islamic financing. Nonetheless, market complexities standardization or retarding regulatory measures make Islamic finance a worthy market proposition. This goal can be attained through inherent features, focused product development, and by obtaining government support in the case of Islamic finance in order to fully participate in addressing universal ENVSSG targets, and play our part in achievement of sustainable development.

Natural Alignment with ESG Principles

ESG is analogous to Islamic finance standards based on the law of fairness, transparency, and social justice. In Habib (2023), the author argues that Islamic finance can effectively drive ESG goals by releasing shariah compliance to cover ethical, social, and environmental objectives. This is possible if organisations assume a stakeholders' interested view and broaden the definition of value to include social goods. At this point, the ESG framework incorporates these ethical concepts through environmental sustainability and social responsibility supported by appropriate governance. It also adheres to ethical finance where practices of interest (riba) and in the businesses prohibited (haram) are prohibited. This is why Riba is seen as inequitous and as becoming exploitative between the creditors and the debtors. Instead, Islamic finance encourages profit-and-loss sharing mechanisms that distribute risk equitably among stakeholders. The prohibition of riba aligns with the ESG objective of ensuring financial inclusion and promoting socially responsible lending practices. Furthermore, excluding industries such as gambling, alcohol, and arms manufacturing ensures that investments have positive societal impacts, directly aligning with ESG goals. Hence, the natural alignment between Sharia-compliant investing and ESG goals offers considerable potential for expanding the sustainable finance market. Prohibiting unethical practices, emphasizing social justice, and fostering transparency position Islamic finance as a compelling option for socially responsible investors. By harnessing this alignment, Islamic finance can broaden its global reach and significantly contribute to sustainable financial practices.

"......islamic finance contributes to ESG goals through its structured compliance with ethical standards,...(Participant 1)

Product Innovation

The introduction of new financial instruments like green sukuk (Islamic bonds) and Islamic microfinance provide opportunities for growth in sustainable finance. Panagopoulos, (2023) highlighted that sustainable bonds and green loans borrow social implications and generate financial rewards by fusing the two in the capital market. Thus, Green sukuk can be used to cover the financing needs of the projects so that their social and environmental sustainability requirements are respected. They will appeal both to conventional and Islamic investors. However, the green Islamic sukuk is not the only tool that the Islamic microfinance institutions are deploying because they are also working hard to support the marginalised groups and to pursue the social justice agenda through financial inclusion. The innovations in these instruments have the likelihood of sparking the imagination of inventors who will form new products dedicated to addressing the urging demand for environmental sustainability.

'we have to focus on the innovative financial product ni. cthnya Green Sukuk. UiTM Solar Energy, then we have Microfinance. Cth: Amanah Ikhtiar,TEKUN. These products actually assist on achieving sustainability .... (Participant 1)

Malaysia is the pioneer in the issuance of green sukuk globally. In 2017, the Securities Commission Malaysia launched the world's first green sukuk framework, which made it possible for environmentally friendly projects to be financed while complying both with Sharia principles and with global ESG standards. The success of initial issuances resulted in forthcoming issuance that showed strong investor appetite attracting both Islamic and conventional investors. Malaysia's experience with green sukuk confirms that issuance of these sustainable securities attracts a wide range of investors that include Islamic financiers as well as global institutional actors. facilitates the way of financing the renewable energy investment, sustainable agriculture, and other environmental-friendly projects which need a lot of money. Regarding Islamic microfinance, such platforms offers Sharia-friendly loaning options to unbanked and poor communities, they facilitate fight against poverty and inequality. Microfinance organizations are based on a system of both profit and loss sharing model, which ensure that the results are even and fair. It enables the development of entrepreneurs that have problems with accessing traditional banking services. With a strengthened social justice and economic empowerment the institutions stand to have a great investment opportunity for those global impact investors that finance for sustainable development.

Government and Institutional Support

Supportive government policies and institutional frameworks are crucial in harnessing the potential of Islamic finance. Malaysia's Value-Based Intermediation (VBI) framework demonstrates how integrating ESG goals within Islamic financial institutions can be institutionalized. The introduction of VBI by Bank Negara Malaysia (BNM) in 2017 aimed to enhance the congruence between Islamic finance practices and sustainability objectives. This framework is, however, all about value creation through banking activities with the integration of fair, responsible, and transparent banking practices in line with the ethical values that are born out of Islamic faith. The ESG integration of VBI into Islamic financial institutions ensure the observance of sustainable finance practices throughout the institution. It provides the guideline and strategy starting to integrate ESG enabling the Sharia-compliant financial products. Such policies can be spread by the authorities to construct a robust policy atmosphere which will encourage the entry of ESG compliant Islamic finance products in the market.. Tax incentives, grants, and government-backed guarantees for green sukuk issuances and Islamic microfinance institutions can encourage more financial institutions to pursue sustainable investments. Along with that, international collaboration ventures that link regulators, financial institutions and global bodies for framing universal standards and benchmarks for sustainable Islamic finance is of cardinal importance. Organizations like the Islamic Financial Services Board (IFSB) and the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) can work with national governments to harmonize Islamic finance standards with ESG criteria. This international collaboration will help align practices, boost transparency, and foster trust among stakeholders. Such efforts will also reduce compliance costs for financial institutions, making ESG-compliant Islamic finance more accessible and attractive.

Shariah compliance makes government stronger because it requires all deals to be open, honest, and fair. This makes sure that Islamic financial institutions not only follow the rules when it comes to money, but also follow moral guidelines ....” (Participant 3)

The ESG principles are at the heart of Islamic finance and therefore this type of finance is perfectly matched for the sustainable finance projects. Natural synergy in tandem with innovative financial products and government backing generates ways for sustainable development. Through such opportunities, the contribution of Islamic finance to ethical, transparent, and socially responsible global investment becomes a transformational role.

Framework Aligning Islamic Finance with Global ESG Goals

This proposed framework aims to synchronize Islamic finance with global Environmental, Social, and Governance (ESG) goals. By doing so, it can establish a more all-encompassing and enduring financial system that adheres to Islamic principles while tackling worldwide challenges. It involves several critical sub-processes I will discuss later in this essay. First, the concept of Maqasid al-Shari'ah or the objectives of Islamic law as a primary determinative tool employed in Islamic law means that the decision-maker needs to pay attention to the overarching goals of theShariah in the sphere of Islamic finance, as these include protection of faith, life, intellect, offspring, and property. Based on the above objectives of Islamic finance, it is important that practices in the financial system achieve the aims of the shariah while allowing for ethical and sustainable transaction. In addition, the two frameworks also place emphasis on what is referred to as public interest or Maslahah. This is a key concept that is central to many Islamic finance practices. Concerning concepts and features linking it to other theories, it focuses on the welfare of others and the absence of aggression. Investments should focus on caring for the well-being of the society; protecting the environment and the development of the economy in a manner that is less prohibitive to those at the lower end of the society. In addition, it can be achieved through the introduction of fresh financial instruments like Green Sukuk and Islamic micro-finance. I concur with the research done by Sadiq & Mushtaq (2015) that opines Sukuk (Islamic bonds) as a financial tool that aligns itself with the ESG framework and will greatly enhance the consideration of the environmental, social, and governance factors in the investment process. Third, the highlights the need for sound legal structures also known Shari'ah governance structures so that compliance is maintained and organizations transparency and accountability developed in Islamic finance. This creates confidence and increases the likelihood of being trust when undertaking financial activities. This framework also emphasizes the importance of engaging all the relevant stakeholders including the customers, investors, regulators, and the community so as to discover ways through which the Islamic Finance Industry can adapt to the current global ESG goals. Involvement of all stakeholders ensures that everybody is part of the decisive procedure which adds value to the decision-making process. In view of these findings, it is imperative to build and conduct capacity and training programs that would focus on the improvement of competencies of Islamic finance workforce in the area of integrating ESG factors into research and practice. Ideally should be well equipped to incorporate ESG factors into their framework and be in a position to point out sustainability issues within an organization. Last, the framework especially focuses on reporting and disclosures because these practices can help to ensure that Islamic finance is in sync with the ESG objectives across the world, and contribute to vested interest among the stakeholders. Therefore, the intention of including these key elements in the structuring of Islamic finance practices is in line with the goal of the framework to design and implement a stable and responsible financial environment as it contributes to the realization of global ESG objectives subject to the principles of Islamic finance. The framework in question was designed to bring Islamic finance regulation in line with the conventional worldwide Global ESG targets, so that the financial transactions are ethical, sustainable, and transparent. When there is better alignment of its goals, the contribution of Islamic finance in addressing the world challenges in developing a fair economy, becomes more effective.

CONCLUSION

Integrating Islamic banking and ESG is the best way to work towards sustainable development in the banking system. This paper reveals how both Islamic finance and ESG programs are inherently compatible, and the elements that create a framework in which these principles can be adopted. The alignment is a function of the principles of Islamic finance and its cardinal principles of fairness, transparency and the ban on Gharar and Riba. As such it provided and supports ESG initiatives like: environmental preservation, fairness in society, and responsible management. Additionally, there are some perennial barriers, to wit: relating to the implementation of consistent standards for inadequate performance, parity of regulations and the level of awareness. There is no correct benchmark for good and improved sustainable Islamic financing yet so most of the time there are differences resulting to unconnected market segments. Further, lack of a proper legal framework from the government side and general lack of knowledge about how Islamic finance is compatible with sustainable development goals restrains the market. But there are other opportunities which can be used while relying on natural occurrence, introducing a new product, and enjoying the support of the institution. Sukuk green and Islamic micro finance are the examples of innovative instruments for Islamic finance which meet the sustainability requirements within Sharia guidelines. Organizational changes at the regulatory level, for example Malaysia's Value-Based Intermediation Framework, will help support more ESG goals. This framework provides official and constructive purposes to establish ESG. Thus, ESG investing along with Islamic finance can create a synergy that may lead to legitimization, higher performance, and consistencies with sustainable development. The rising global demand for sustainability-driven investment will be hugely influenced by the ongoing enhancement of environmental, social, and governance (ESG) criteria in Islamic finance to advocate for the ethical future of business. Global societies' demand for sustainable investments will be highly influenced by constant development of Islamic ESG criteria, which stand at the frontier of business evolution. Implementation of the legal guidelines in an Islamic finance environment that follows ESG standards of the global world helps in delivery of ethical and sustainable financial services that are mutually beneficial for investors, beneficiaries, and society as a whole. Regarding the above findings, it is recommended that future studies focus on the construction of more robust annual performance devices based on the impact of IFS on sustainability performance. The intentional comparison analysis of Islamic and conventional ESG investing possesses a strong chance of offering insights. Further, it should examine how some of these legislative changes has helped to promote higher acceptance of similar ideas in markets still largely non-Muslim. Through challenging these challenges and exploring these opportunities, Islamic finance holds the key to extend its impact on global sustainability contributing the best example of sustainable and responsible investing.

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