



Faculty of Economics and Business

**THE PERFORMANCE OF SHARI'AH INDEXES BETWEEN  
MALAYSIA AND INDONESIA**

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Bachelor Degree in Finance (Honours)  
2014

# **HUBUNGAN ANTARA SHARI'AH INDEKS DI MALAYSIA DAN INDONESIA**

**CHU WEI FATT**

Projek ini merupakan salah satu keperluan untuk  
Ijarah Sarjana Muda Kewangan dengan Kepujian

**FAKULTI ECONOMI DAN PERNIAGAAN  
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**THE PERFORMANCE OF SYARI'AH INDEXES BETWEEN  
MALAYSIA AND INDONESIA**

CHU WEI FATT

This project is submitted in partial fulfillment of  
The requirements for the degree of Bachelor Degree of Finance with Honours

FACULTY ECONOMY AND BUSINESS  
UNIVERSITY MALAYSIA SARAWAK  
2014

## ABSTRAK

# HUBUNGAN ANTARA SHARI'AH INDEKS DI MALAYSIA DAN INDONESIA

*Oleh*

**Chu Wei Fatt**

Objektif kajian ini adalah untuk mengkaji prestasi pelaburan dalam indeks Shari'ah di Malaysia (*Dow Jones Islamic Malaysia, DJIMY*) dan Indonesia (*Jakarta Islamic Stock Exchange, JAKIS*) dari tempoh 2 Januari 2003 sehingga 31 Januari 2013. Kajian dibahagikan kepada tiga tempoh iaitu Tempoh Keseluruhan (2 Januari 2003 – 31 Januari 2013), Tempoh *Bullish* (2 Januari 2003 – 31 Januari 2008) dan Tempoh *Bearish* (1 Februari 2008 – 31 Januari 2013). Prestasi indeks Shari'ah ini diukur dengan mungumpul data harian indeks Shari'ah dari Malaysia dan Indonesia, dan menggunakan nisbah *Sharpe*, nisbah *Treynor*, *Modigliani & Modiglioni (MM)* dan *Jensen-alpha*. Selain daripada itu, kajian ini menggunakan statistik deskriptif, analisis korelasi, ujian kepegunan *Augmented Dickey Fuller (ADF)* dan *Phillips-Perron*, ujian kointegrasi *Johansen-Juselius (JJ)* dan ujian sebab-menyebab *Granger*. Keputusan kajian telah menunjukkan bahawa prestasi *JAKIS* lebih baik berbanding dengan *DJIMY* dan *DJIMWORLD* (penanda aras kajian) dalam semua tempoh masa yang dipilih. Di samping itu, keputusan juga menunjukkan bahawa tidak ada hubungan jangka panjang di antara *DJIMY* dan *JAKIS*. Walaubagaimanapun, ujian sebab-menyebab *Granger* menunjukkan bahawa prestasi *JAKIS* mempengaruhi prestasi *DJIMY*. Oleh itu, pelabur tempatan dan pelabur asing boleh melabur dalam kedua-dua Indeks Shari'ah di Malaysia dan Indonesia untuk memperoleh faedah menerusi portfolio pelaburan antarabangsa.

## **ABSTRACT**

# **THE PERFORMANCE OF SYARIAH INDEXES BETWEEN MALAYSIA AND INDONESIA**

*By*

**Chu Wei Fatt**

The main objective of this study is to investigate the performance of ethical investment or known as a Shari'ah - compliant investment in Malaysia (Dow Jones Islamic Malaysia, DJIMY) and Indonesia (Jakarta Islamic Stock Index, JAKIS) during the period from 2 January 2003 until 31 January 2013. The studied period is further divided into overall period (1 January 2003 – 31 January 2013), Bullish Period (January 2003 – January 2008) and Bearish period (2 February 2008 – 31 January 2013). Collecting the daily data of the Shari'ah indices from Malaysia and Indonesia, the performance of Shari'ah indices is measured by using Sharpe ratio, Treynor ratio, Modigliani and Modigliani (MM) measure and Jensen-alpha measure. Apart from that, this study employed the descriptive statistics, correlation analysis, Augmented Dickey-Fuller (ADF) and Phillips-Perron (PP) Unit Root Tests, Johansen-Juselius (JJ) Cointegration Test, and Vector Autoregression (VAR) Granger Causality test to examine the long-run and the short-run relationship between the DJIMY and JAKIS. Firstly, the result shows that JAKIS is outperformed DJIMY and DJIMWORLD (benchmark of this study) during all the selected periods. Secondly, the result also shows that there is no long run relationship between DJIMY and JAKIS. However, the Granger causality test had shown that JAKIS granger causes DJIMY during all the three study periods. Therefore, the local and foreign investors can invest in both Malaysian and Indonesian Islamic Index to gain profit through international portfolio investment.

## Pengesahan Pelajar

Saya megakui bahawa Projek Tahun Akhir bertajuk  
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ini adalah hasil kerja saya sendiri kecuali nukilan, petikan, huraian dan ringkasan  
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## Statement of Originality

The work described in this Final Year Project, entitled  
**“THE PERFORMANCE OF SYARIAH INDEXES BETWEEN  
MALAYSIA AND INDONESIA”**  
is to the best of the author’s knowledge that of the author except where due reference is  
made.

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Date Submitted

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## **PENGHARGAAN**

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## **CHAPTER ONE**

### **INTRODUCTION**

#### **1.0 Introduction**

Islamic investment or more commonly known as ethical investment and Socially Responsible Investment (SRI) are an investment tool that is socially responsible by investors due to the nature of the business conducted by the company. Islamic investment is the buying or selling of Islamic securities or funds in accordance to the principles of Islam. As stated in a study conducted by Hussein (2004), the number of investors showing an increasing trend and seeking to align their investment with their principles through socially responsible investment.

The stock market of the Muslims' world is an ideal destination for Islamic ethical investment as Muslim investors always seen this as promoting their business activities which may help other Muslims. Malaysian stock market, Bursa Malaysia and Indonesia stock market, Jakarta Stock Exchange are classified as emerging market that attract the attention of wealthy investors all over the world. Wilson (1997) mentioned that the alternative way to construct an Islamic investment product is by investing in quoted companies by Shari'ah compliant in Muslim countries. He also said that such pragmatic strategy is appealing to Muslim investors as the quoted companies are subject to the limitations of the Islamic environments on their operations which do not involve in halal business activities. The basic rules of Islamic investment are providing a platform for Muslim and encourage them to invest their assets to reflect the Islamic principles that govern their dairy life.

The ethical investment getting more interesting and popular topic of discussion, especially when there are many researchers start involving themselves in Islamic research, organizing Islamic forum, conferences and conducting empirical study related to Islamic investment published on international journal. Based on a research conducted by Nathie (2008), Islamic equity fund investments are becoming increasingly popular due to the avoidance of prohibited goods and services, doubtful transactions and speculative financial dealing bordering on gambling.

However, there are evidences argued that ethical investment underperformed over longer periods as ethical investment lack of sufficient diversification in the investment market. However, the result is different on the performance of ethical investment and conventional investment and hence shows a gap from the studies conducted by some scholars and researchers. Some researches show ethical investment performs well during the bearish and financial crisis period as the risk exposed to the market is lower and underperformed during the bullish period as the return is less compared to conventional investment (Merdad, Hassan & Alhenawi, 2010; Snoussi, Saleh & Rigobert, 2013).

## **1.1 Background of the Study**

### **1.1.1 Ethical Investment in Malaysia**

Malaysia had more than 30 years' experience and solid fundamentals in Islamic finance development. This is due to its strategic location that acts as the hub between the East and West, South East Asia and Middle East. Foreign investors found Malaysia as a good gateway to seize the opportunity of the fastest growing emerging markets (Securities Commission, 2007). As fast growing and expanding of emerging country's economics, Malaysia plays an important role as a financial hub and gateway for foreign investment and fund sourcing.

According to Jamal, Hambali and Ali (2010), an Islamic equity market must be free from any form of unethical or immoral investments and transactions. It is characterized by the absence of interest-based investment, doubtful transactions and unlawful stocks of companies which deal with Shari'ah non-compliant activities or items. The main thrust of Islamic Capital Market in Malaysia is governed by the Securities Commission Malaysia (SC) which acts as a statutory body with the responsibility of regulating and systematically developing the Malaysia's capital markets. Security Commission Malaysia established a Shari'ah Advisory Council (SAC) with the mission of advising the Commission on all matters which related to the wide-ranging development of the Islamic Capital market issues. SAC also responsible for listing all of the Shari'ah-compliant securities which as traded in the Bursa Malaysia (Securities Commission, 2007).

**Table 1.1.1a: Number of Shari’ah-compliant securities listed on Bursa Malaysia**

	November 2013	May 2013
Number of Shari’ah-compliant securities	653	801
Total listed securities	914	910
% total listed securities	71%	88%

Source: Securities Commission Malaysia, as at 25 November 2013.

Up to November 2013, Shari’ah-compliant securities hold 653 out of 914 or 71% of the total listed securities which are traded on Bursa Malaysia, which are 653 out of 914 total securities. The latest Shari’ah-compliant securities list is updated in May and November every year. This list is useful in assisting ethical investors to identify their investment is according to Shari’ah-compliant and hence avoid them to invest in non-compliant securities. This is due to the reclassified of Shari’ah-compliant securities to Shari’ah non-compliant securities are different from time to time.

**Table 1.1.1b: Market Capitalization (RM billion) of Shari’ah-compliant securities**

	December 2012	December 2011
Shari’ah-compliant securities	942	806
Total market capitalization	1466	1285
% total market capitalization	64%	63%

Source: Securities Commission Malaysia, as at December 2012.

As shown in the Table 1.1.1b above, the market capitalization of Shari’ah-compliant securities increased by RM 136 billion or 16.87% from RM 806 billion in December 2011 to RM 942 billion in December 2012. The market capitalization of Shari’ah-compliant securities has increased by 1% to 64% of total market capitalization as of December 2012 from 63% in December 2011.

### **1.1.2 Ethical Investment in Indonesia**

Indonesia had a total population of 237 million as stated in Country's Census Indonesia 2010 and it ranks number 4 biggest population countries in the world. Besides, Indonesia is the world largest Muslim majority country in the world at 86% of their total populations are declared as Indonesians Muslims. Population of Indonesia is expected to grow to 366 million by 2050 with the total annual growth rate of 1.04%. Therefore, Indonesia offers better opportunities in the development of the Islamic financial industry.

Indonesia take the opportunity to establish an Islamic based capital market called Jakarta Islamic Index (JII) in 2000 which aims to provide a guideline for ethical investors who want to invest funds and securities accordance with Islamic principles (Antonio, Hafidhoh & Fauzi, 2013). The Islamic investment instruments in the capital markets are growing rapidly and governed by Badan Pengawas Pasar Modal & Lembaga Keuangan (Bapepam-LK). Islamic securities are a collection of securities that included all Islamic stocks and Sukuk. They must not contrary with Shari'ah principles in the capital market (Regulations of Bapepam-LK Rule No IX.A.13). Bapepam-LK is assisted by the National Sharia Supervisory Board (DSN-MUD) to set on the screening criteria and categorized all the Islamic securities.

**Table 1.1.2a: Number of Shari’ah-compliant securities listed on Jakarta Stock Exchange (JII)**

	March 2013	November 2012
Number of Shari’ah-compliant securities	321	317
Total listed securities	464	459
% total listed securities	69.18%	69.06%

Sources: Indonesia Stock Exchange Fact Book 2013, Indonesia Stock Exchange (IDX), May 2013

Up to May 2013, there are 69.18% of the total listed securities on the Indonesia Stock Exchange (IDX) are Shari’ah-compliant securities. Table 1.1.2a shows 321 out of 464 securities had been screened through by the Bapepam-LK and DSN-MUI. The latest list of Shari’ah-compliant securities can be divided into two types, Periodic Shari'ah Securities List (PSSL) and Incidental Shari'ah Securities list (ISSL). PSSL is updated twice a year in May and November while ISSL is issued irregularly. These lists are the guidance for ethical investors to invest in Shari'ah securities portfolios.

**Table 1.1.2b: Market Capitalization (RP billion) of Shari’ah-compliant securities**

	December 2012	November 2011
Jakarta Islamic Index	1,671,004.23	1,414,983.81
Jakarta Composite Index	4,126,994.93	3,537,294.21
% total market capitalization	40.49%	40.00%

Sources: Sharia Capital Market Statistics, Indonesia Financial Services Authority 2013.

As shown in the Table 1.1.2b above, the market capitalization of Shari’ah-compliant securities increased by RP 256,020.42 billion or 18.09% from RP 1,414,983.81 billion in December 2011 to RP 1,671,004.23 billion in December of 2012. The market capitalization of Shari’ah-compliant securities in Jakarta Stock Exchange is slightly increased from 40% in December 2011 to 40.49% in December 2012.

## 1.2 Problem Statement

Shari'ah-compliant securities are strictly obeying Islamic principles. Shari'ah screening criteria which forbidden in investing companies that producing or selling addictive substances allow Muslim investors to choose their securities carefully. Hassan and Antoniou (2010) stated that screening criteria or Qualitative Screening are the general rules followed by Islamic stocks and funds because these investment needs to be investigated whether the industries or companies they invested is permissible according to Islamic principles. These companies with their core business related to gambling, conventional banking (interest-based activity), manufacturing of liquor, tobacco, conventional insurance, pork production or related and activity that offensive to the principles of Islam will not be considered and invested.

Besides qualitative screening, quantitative screening method is also important in ethical investment. According to Bellalah, Abdul Rehman and Masood (2013), the quantitative screening method involve the numerical calculation of the company financial ratio which their non-permissible activities do not exceed the maximum allowance threshold. For instance, debt and asset ratio are calculated based on the amount of the company's capital, which is financed by debt instead of assets. Based on the Shari'ah compliant, a company with a debt financing that is more than 33% or above are considered as impermissible investment and hence should be excluded in the investment or portfolio investment (Jamal, Hambali & Ali, 2010).

The existence of a Shari'ah screening process in the capital market allows investors to invest in companies that operating in permissible business activities that

are according to the fair Shari'ah principles (Bellalah, Rehman & Masood, 2013). Nevertheless, there are some researches on the Shari'ah investment screening process. Dusuki and Abdullah (2006) mentioned in their research that the concern for ethical investment and socially responsible investment has become popular since the mid-1970s in the United Kingdom. After that, there are significant development and growth in Islamic investment no least within the financial sectors. Many companies also took this as a chance to get their companies' securities listed as Shari'ah-compliant securities to strengthen their brand, enhance corporate reputation with customers, suppliers and attract more Muslim investors to invest in their company.

The Islamic screening process provides an investment tool which is acceptable by the Muslim investors to invest in. However, this also excluded some sectors like conventional banking sectors which have high profitability and return and preferences for investment that create some negative view on the ethical investment. There are some mixed results about the ethical investment. Albaity and Ahmad (2008) stated that the pessimistic view of the ethical investment is that an investor is more likely to receive a lower return or return which is below the market return. Setiawan and Oktariza (2013) also commented that this pessimistic view in Islamic investment is based on the fact that Shari'ah compliant stocks or companies experience limited opportunities for two reasons. First, a Shari'ah compliant company is limited and restricted to use external financing and this might lead to a gradually low company's sustainable growth and the second reason is Shari'ah restrictions limit the company's income as the investment opportunities are limited.

The Securities Commission (SC) of Malaysia and National Sharia Supervisory Board (DSN-MUI) of Indonesia has the responsibility to carry out the