

The conventional pawn broking finance essay

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CHAPTER 1

INTRODUCTION

This chapter discusses on the study background by providing overview for both pawn broking in Malaysia which are conventional pawn broking and Ar-Rahnu. Next section describes the problem statement, followed by research questions, objectives of the study, and significance of the study. Finally, in this chapter summary the whole section in this chapter.

RESEARCH BACKGROUND

In the current economy landscape, there is no doubt that financial institutions especially banks play an important role in generating the economic and financial growth for a country. The individuals, business communities and organizations are relying on the banks as their main investment and financial resources. Therefore, the financial institutions have developed various innovative financial instruments in order to meet their customers need in the forms of financing and investment. Besides the formal financial institutions, there were informal financial providers such as moneylenders or pawn broking that have played a complementary role in providing credit to the communities. However, the informal financial providers tend to be hidden from view because their loans are relatively small and the sensitivity attached to credit on lenders and borrowers (Abdul Razak, 2011). Among informal financial providers, pawn broking business has grown importance as a main source for the low income communities. In Malaysia, there are two types of pawn broking business which are conventional pawn broking and Al-Rahnu is normally known to Islamic pawn broking.

Conventional Pawn Broking

In Malaysia, the conventional pawn broking business is business tradition brought by Chinese Hakka from China. According to Abdul-Razak (2011), the business was introduced by the Chinese merchants in the 15th century during the sultanate of Malacca. The business became more popular after the tin mining in Larut in the 19th century. In the early stage, the business was not bounded to any laws. However, during the British colonial, the Pawnbrokers Ordinance 1871 was introduced and enforced in the Straits Settlements for the purpose of business licensing and regulating the pawn broking business activities. This is the first formal regulation for pawn broking business in Malaysia and this ordinance was enforced until it was repealed by the Pawnbrokers Ordinance of 1898 (Wan Abdullah, 1999).

During that time, the state government started to introduce their own law to regulate the pawn broking business in their state. Initially, there are thirteen (13) enactments, ordinance and rules have been introduced and enforced by the states governments (KPKT). This situation happened because at that time the states in Malaysia are separated under their own administration and have not yet been consolidated under a single federation. Finally, in 1973, the Malaysian government has taken an initiative to standardise and harmonies the pawn broking business in Malaysia including Sabah, Sarawak and Labuan by introducing the Pawnbrokers Act 1972 and Pawnbrokers Regulation 1972. The administration of this act is under supervision of the Ministry of Housing and Local Government (KPKT). This act provides the basic guidelines for both pawnbroker and pawner to ensure healthy pawn broking business and to protect the consumers' interest. This act still exists until today with the latest amendments done in 2006. According to Abdul

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Razak (2011), as at 2010, there were 259 licensed conventional pawn broking operated in Malaysia (refer table 1. 1) and the business is still monopolized by the Chinese communities. Their business is governed under the Pawnbrokers Act 1972. Table 1. 1: The Number of Pawn Broking in Malaysia in 2010

States

Conventional Pawn Broking

Ar-Rahnu (Islamic Pawn Broking)

Total

Selangor 394079 Perak 403171 Johor 343064 Kelantan 115061 Kedah 292756 Pulau Pinang 271744 Pahang 142640 Kuala Lumpur/ Putrajaya 142236 Terengganu 72835 Negeri Sembilan 181634 Sabah 71421 Melaka 12719 Sarawak 31518 Perlis 4610 Total 259329588 Source: Abdul Razak (2011)

Ar-Rahnu

In Malaysia, Ar-Rahnu is operating in parallel with the conventional pawn broking business. Ar-Rahnu has been introduced in order to give an alternative to the muslim community due to majority of muslim are afraid to do business with conventional financial institutions as they deal with interest (riba), which is forbidden in Islam and their management of profits is not based on Islamic principles (Nor Mohamed, 1996). Therefore, in an effort to eliminate riba and gharar in conventional pawn broking business, there was initiative to introduce Ar-Rahnu as an alternative financing for the society especially to muslims' communities which is not involve riba, more

transparent and their scheme is complies with Shari'ah principles. According to Yaacob (2012), the first Ar-Rahnu was Muassasah Gadaian Islam Terengganu (MGIT), which was set up by the Council of Islamic Religion and Malay Customs Terengganu (MAIDAM) in 1992. The establishment of MGIT is to provide easier and faster secured loan facility for the individual that having cash flow based on the Shari'ah principles. The borrower (Al-Rahin) will pledge an item which is jewelry from gold or diamonds for pawning to the lender (Al-Murtahin) as a collateral from which the borrower receives an interest free loan amounting to 80% of the pawned item or not exceeding RM5, 000 (MGIT, 2013). The collateral item is held by the lender and the storage fee is charged to the borrower during the period of loan. The period of loan is six months and can be extended to another four months. Upon the maturity, the borrower has to pay back the loan and the lender must return back the item to the owner. After that, Ar-Rahnu scheme was introduced in Kelantan by Permodalan Kelantan Berhad (PKB) through establishment of Ar-Rahn shop in Kota Bahru and subsequently followed by the Malaysia Islamic Economic Development Foundation (YaPEIM). However, the foundation faced problems as it was against the Pawnbrokers Act 1972. Since there is a need of Islamic pawn broking in Muslim community, Bank Negara Malaysia (BNM) which is the Central Bank of Malaysia has requested Bank Kerjasama Rakyat Malaysia Berhad (Bank Rakyat) to collaborate with YaPEIM in implementing Ar-Rahnu. This suggestion was taken seriously by Bank Rakyat who was interested to use their present platform as a starting point for exploring in Ar-Rahnu in order to expand their Islamic financial product and services. As such, in 1993, the Minister of Finance announced the introduction of Ar-Rahnu scheme through the collaboration between Bank Rakyat with YaPEIM.

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Under this collaboration, Ar-Rahnu was growing and expanding more rapidly. The next financial institution to launch the Ar-Rahnu product and services was Bank Islam Malaysia Berhad (BIMB) in 1997 followed by EON Bank and Bank Pertanian Malaysia (Agro Bank) in 2002 and also by other cooperatives. Now, Ar-Rahnu can be categorized into three main groups which are: (i) state-linked company such as MAIDAM and PKB, (ii) cooperatives under foundation for example YaPEIM, Koperasi Pos, and (iii) subsidiaries of banking institutions such as Bank Rakyat, Agro Bank, BIMB (Maamor et al., 2010). According to Abdul Razak (2011), as at 2010, there were 329 Ar-Rahnu operated in Malaysia (refer to table 1. 2). From the table we noted that the Ar-Rahnu service is dominant in Kelantan, Terengganu and Sarawak as compared to the conventional pawn broking. Table 1. 2: The Breakdown of Ar-Rahnu in Malaysia in 2010

States**Ar-Rahnu****Total****Conventional Pawn Broking****MGIT****PKB****Bank Rakyat****YaPEIM****Agro Bank****BIMB****Co-operative**

Selangor234854039Perak1161223140Johor149613034Kelantan2289821501

1Kedah98912729Pulau Pinang7551727Pahang107722614Kuala Lumpur/

Putrajaya132522214Terengganu106561287Negeri

Sembilan64511618Sabah1031147Melaka43712Sarawak105153Perlis22264T

otal10221335984219329259Source: Abdul Razak (2011)

PROBLEM STATEMENT

In the middle of current economic slowdown, those in financial problem are looking for the various avenues in order to get easy cash. For people who are desperate for money, they may approach for loan shark and in Malaysia loan shark is synonym with Ah Long. Ah Long derived from Cantonese phrase which is a common term for illegal loan sharks in Malaysia and Singapore and they lend money to the people who are unable to obtain loans from financial institutions or other legal sources (Wikipedia, 2013). Statistic from <https://assignbuster.com/the-conventional-pawn-broking-finance-essay/>

PDRM shows that 213 Ah Long cases have been referred to PDRM from last January to May 2012 (Utusan Malaysia, 17/06/2012). MCA public complaint bureau highlighted that they have received eleven (11) complaints regarding Ah Long which involve the total loans amounting to RM500, 000 across all the races in Malaysia in the first seven days this year (Bernama, 8/01/2013). In the early this year also, Malaysia has been shocked with the report regarding Ah Long issue involving Royal Malaysian Navy (TLDM). The report highlighted that TLDM successfully solved Ah Long debts amounting RM139, 000 which involving 102 their staffs (Utusan Malaysia, 8/1/2013). This Ah Long issue is not a new issue in Malaysia. Statistics recorded by Malaysiakini highlighted that 503 cases in 2006, 539 cases in 2007, 636 cases in 2008, 487 cases in 2009 and 302 cases in 2010 (Malaysiakini, 29/04/11). By taking the loan from Ah Long, the borrowers were burdened with high interest rate imposed on the loan and exposed them to inhuman treatment of ah long. Besides that, they have an option to go to conventional pawn broking if they have valuable accessories such as gold, diamond, or any jewelry that can be pawn to loan some cash. Conventional pawn broking is very popular as it is require simple producers that do not cause too much hassle to borrower as compared to the formal financial institution. However, the borrowers were burdened with the high interest rate imposed on the loans. Due to this problem, effort were taken to make forward the Islamic approach in micro credit financing more feasible. In this context, Ar-Rahnu is one of the most appropriate mechanisms as it provides financial assistance especially for those who have difficulties in obtaining loan from financial institutions. Therefore, in the 2010 budget speech by YAB Dato' Sri Mohd. Najib Tun Abdul Razak, the Prime Minister and Minister of Finance highlighted that Ar-

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Rahnu is an important instrument to assist those unable to secure financing from financial institution to obtain business capital. Malaysian people have been encouraged to take the opportunity to improve their socio-economic by engaging in Ar-Rahnu. The Ar-Rahnu plays an important role as a fair, transparent and cheap microcredit financing in meeting the different customer requirements. Ar-Rahnu can use as credit channel to those who want to obtain easy cash to meet their financial requirement such as educational need and also can be a credit channel to those who require temporary working capital especially for small and medium size businesses. Realizing the increasing popularity and recognizing the usefulness and contribution of Ar-Rahnu as one of important medium for financial assistance, this study will be conducted to explore more on the factors that can influence the intention of customers whether to engage or not to engage in Ar-Rahnu.

RESEARCH OBJECTIVES

This study attempts to investigate the determinants that influence customers' acceptance to pursue Ar-Rahnu. Specific objectives of this study are: To determine the relationship between customers acceptance and social influence. To determine the relationship between customers acceptance and pricing. To determine the relationship between customers acceptance and location of Ar-Rahnu. To determine the relationship between customers acceptance and advertisement.

RESEARCH QUESTION

The following research questions are proposed as part of this study: Is there a significant correlation exists between social influences on customers' <https://assignbuster.com/the-conventional-pawn-broking-finance-essay/>

acceptance to choose Ar-Rahnu? How significant is the relationship between pricing and customers' acceptance to choose Ar-Rahnu? How location of Ar-Rahnu can influence the customers' acceptance to choose Ar-Rahnu? Is there are a positive relationship between advertisement and customers' acceptance to pursue Ar-Rahnu?

SIGNIFICANCE OF THE STUDY

This study will provide a better understanding to the community about Ar-Rahnu which is the services that offered by the Ar-Rahnu service providers such as MAIDAM, PKB, Bank Rakyat, YaPEIM, Agro Bank, Co-operative and other cooperation as well. The researcher expected that the result from the study finding can provide additional information and knowledge to the community on the concept and structure of Ar-Rahnu businesses. By knowing this, the community especially non muslim will expose to the advantages of Ar-Rahnu as one of the alternative for funding facilities as it offers better valuation for pawned items compared with other similar forms of financing and the monthly payment was much lower, affordable and not burdensome. In addition to contribute to the increase of the knowledge on Ar-Rahnu, this study also expected to contribute to increase the number of literature in this area for helping future researcher to get more references and information on Ar-Rahnu. This study is also useful for the Ar-Rahnu services provider to have clear view, understanding and knowledge on the factors that influence the community acceptance towards Ar-Rahnu, so that they can enhance their performance and develop an effective strategy to attract more customers in order to penetrate their market.

SUMMARY

This chapter provides an overview of the overall study by explaining the background of the study, emphasizing the problem statement, highlighting the research objectives and research question and also the significance of the study. This study is important to provide a better understanding on the Ar-Rahnu services, expose to public on the opportunities of Ar-Rahnu as one of the better alternative for funding facilities, increase the number of literature in this area and give advantage to the Ar-Rahnu service providers to enhance their performance and develop an effective strategy to attract more customers in order to penetrate their market.