Islamic fintech survey results 2021

From April to June 2021, 200 founders, CEOs and senior executives of Islamic fintech start-ups were invited to share their thoughts and projections on the most pressing issues and trends of the global Shariah fintech market. Responses came in from Europe, Southeast Asia, the Middle East, North America and Africa.

Key highlights:

- Alternative finance predicted to be the fastest-growing Islamic fintech vertical of 2022 followed by challenger banking and crowdfunding and peer-to-peer (P2P) finance
- Slow growth expected for Islamic insurtech or Takatech
- Funding remains the biggest hurdle faced by Islamic fintech start-ups while lack of Islamic finance awareness and regulatory barriers continue to be a challenge to growth
- Almost 70% of respondents plan to raise funds by the first half of 2022
- Despite more than two-thirds of respondents having secured a Fatwa for their businesses, about 55% of respondents view official Shariah pronouncements as unnecessary to their businesses, with about 67% of those without an official Fatwa confirming they intend to secure one in the future
- Islamic fintech founders and CEOs perceive Malaysia as the most conducive and supportive ecosystem for Shariah compliant fintech service providers, leading over the UK and Saudi Arabia by a comfortable margin
- Among factors to encourage Islamic fintech growth include raising market awareness, more robust regulations and access to venture capital
- More than half of respondents believe Islamic fintech start-ups are disadvantaged compared with conventional fintech firms
- Southeast Asia and the GCC are seen as the most lucrative Islamic fintech markets, and
- Indonesia and Malaysia are the most popular jurisdictions for expansion, with almost 35% of respondents highlighting those markets as their next preferred market to enter.

Industry outlook

Growth opportunities — alternative finance most attractive

In a surprising turn of events, alternative finance catapulted itself from one of the least promising Islamic fintech verticals for growth in 2021 to being the segment Islamic fintech leaders think will exhibit the strongest growth in 2022, unseating P2P and crowdfunding. With only 4% of respondents last year opining that alternative finance would be the fastest-growing Islamic fintech vertical, this year almost a quarter (24%) believe the vertical will top the rest.

Despite falling two spots, P2P and crowdfunding (14%) remain one of the most promising growth areas after challenger banking (15%). Islamic insurtech or Takatech came in last two years in a row. It is worth noting that the Takatech vertical remains the smallest vertical by number in the IFN Islamic Fintech Landscape as at the end of August 2021. This suggests that momentum is low for Takatech.

Most conducive ecosystems — Southeast Asia in the lead

Southeast Asia remains the undisputed regional hub for Islamic fintech, housing two major powerhouses, with one representing a conducive Islamic finance ecosystem and the other embodying immense latent market potential. Nearly 40% singled out Malaysia as having the most robust and supportive regulatory architecture and Islamic finance infrastructure for Shariah fintech activities. The next most conducive Islamic fintech ecosystem is the UAE (almost equally split between Dubai and Abu Dhabi but the former is slightly more favored), followed by the UK, Saudi Arabia and Indonesia.

Interestingly, while Indonesia may not be perceived as the most supportive market when it comes to Islamic fintech, it is nonetheless the market most Islamic fintech entrepreneurs want to expand into. This is unsurprising considering the commercial opportunities Indonesia's 270 million-strong Muslim population provides coupled with the Republic's affinity for Shariah as well as the government's aggressive drive for Islamic finance over the last five years. Such unrivaled market prospect overshadows any potential market barriers that may be faced by foreign Islamic fintech start-ups in expanding into Indonesia.

Malaysia is a very close second for obvious reasons. The country is one of the most sophisticated Islamic financial markets in the world and in recent years has focused on bolstering its Islamic fintech ecosystem. Malaysia has been touted as an ideal gateway for Islamic fintech start-ups to launch into the wider Southeast Asian region. It is worth noting that the top five favored jurisdictions for expansion are Muslim-majority markets except for the UK, underscoring the appeal of the UK as an Islamic fintech destination. With a robust financial regulatory architecture, thriving fintech community and international repertoire as a financial center as well as the title of 'the Islamic finance hub of the western world', the UK is attracting related start-ups — both homegrown and foreign — seeking to capitalize on unmet domestic Muslim demand as well as to use the UK to tap the European market.

Chart 1: Most promising Islamic fintech verticals in 2022

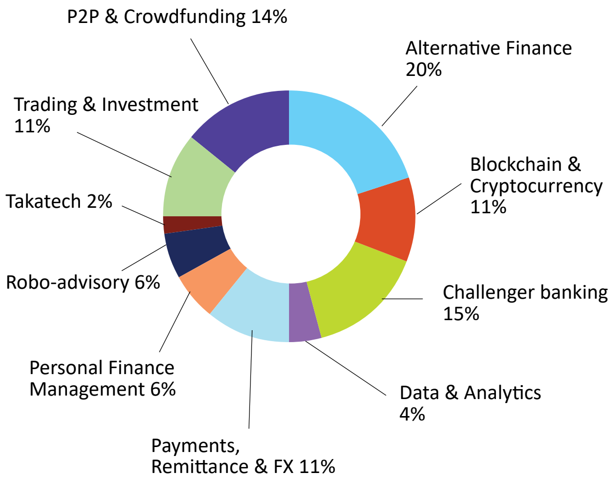


Chart 2: Which market do you think has the most supportive and conducive ecosystem for Islamic fintech?

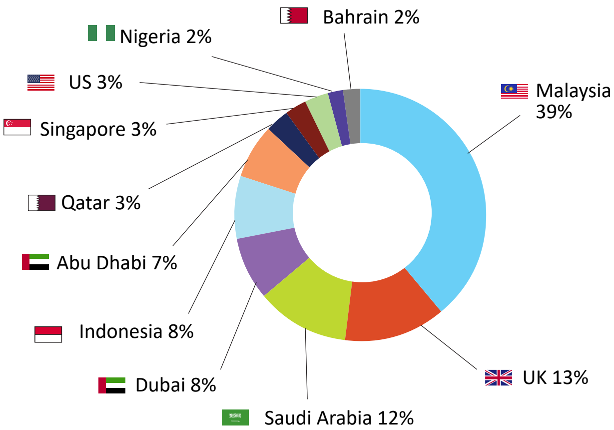
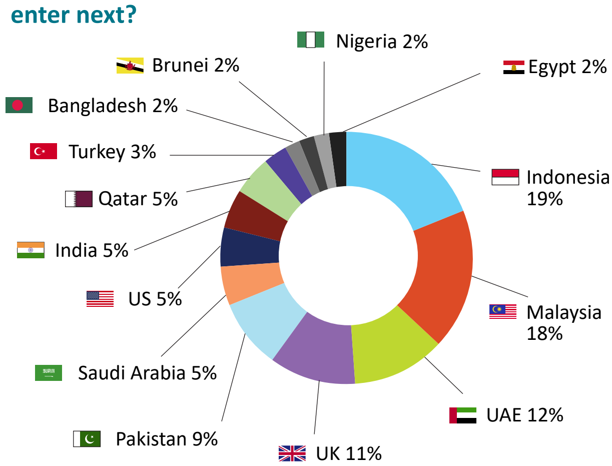


Chart 3: Ideally, which market would you like to enter next?



Competitive advantages

A majority of respondents (62.5%) believe that taking the Islamic route puts a start-up at a rather disadvantageous position compared with conventional firms. Founders and CEOs provide more color to this in the discussion about challenges they face in expanding their market share. These include access to Halal capital, regulatory and tax hurdles, negative perceptions toward Islam, as well as the lack of human capital sufficiently well-versed in fintech and Islamic finance.

"Yes, I think any restriction or parameter puts you at a disadvantage aside from catering to a customer base that prefers dealing with Islamic laws," a Dubai practitioner shared. This sentiment is echoed by another market leader based in the UK: "Earning customer trust when it comes to Shariah approval is an additional friction point when compared to other fintech firms."

Yet, almost 30% viewed Islamic fintech and conventional fintech start-ups as being on par, with different value propositions and ethos.

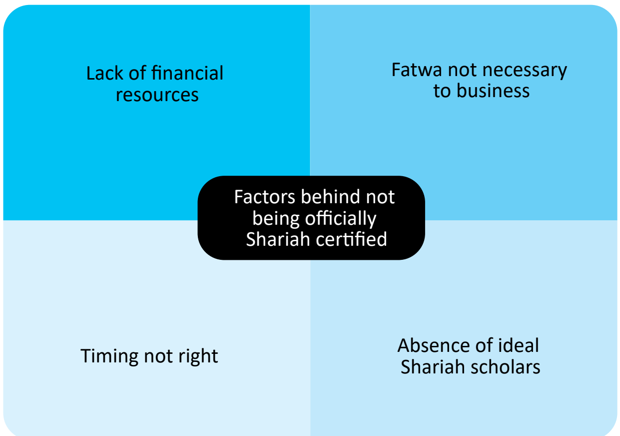
A small minority, about 8%, was of the view that being Shariah compliant does not necessarily hold a start-up back. "A financial services company can operate in any way it sees fit — charging an interest is prohibited in Shariah law, whereas specialist Shariah mortgages provide the same outcome just structured differently. If Islamic finance products were wrapped up and marketed as something available to the whole market, then these funds would see a huge boost. Whereas Islamic finance products are currently only being marketed to Muslim investors — then other cultures perhaps see them as 'not suitable' because they do not follow Shariah law personally," one UK-based Islamic finance director at a fintech firm shared.

Shariah compliance

Yet, despite the additional challenges that come with being Shariah compliant and the fact that 56% of respondents do not view a Fatwa as necessary for their business model, an overwhelming majority had pursued or are planning to secure an official approval from Shariah scholars.

About 71% of the start-up respondents had officially received Fatwas while 67% of those not certified yet are planning to get a Fatwa for their business within the next 12 months. This underscores the importance of an official Shariah approval in building integrity as an Islamic fintech service provider which would ease business growth and market expansion. For those not certified yet, 44% did not see certification as essential, while about one-third are being held back by unfavorable market conditions and waiting for an opportune time to get certified. Budget constraints were a factor of consideration for 17% of the respondents with about 6% still on the hunt for the right Shariah scholar.

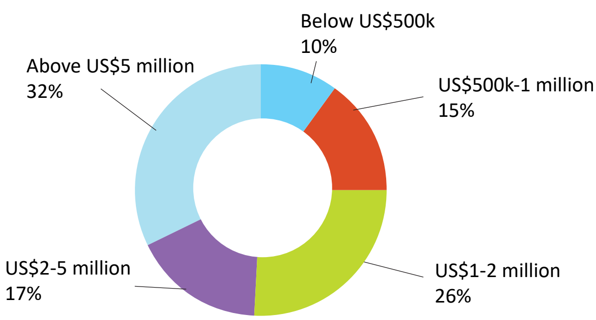
Chart 4: Factors behind not being officially Shariah certified



Funding

Despite tougher market conditions triggered by the global coronavirus pandemic, only 15% of the start-ups surveyed are holding off fundraising plans, while another 10% are mulling the decision in light of market conditions. In total, 76% intend to raise investments over the next 12 months.
This year, a greater number of start-ups are seeking bigger funding — 32% intend to raise over US$5 million over the next 12 months, up from 26% in 2020. This signals the maturity and market readiness of the Islamic fintech sector. US$1–2 million is still a sweet spot for 26% of Shariah fintech start-ups (versus 29% in 2020).

Chart 5: How much are you looking to raise?



Challenges

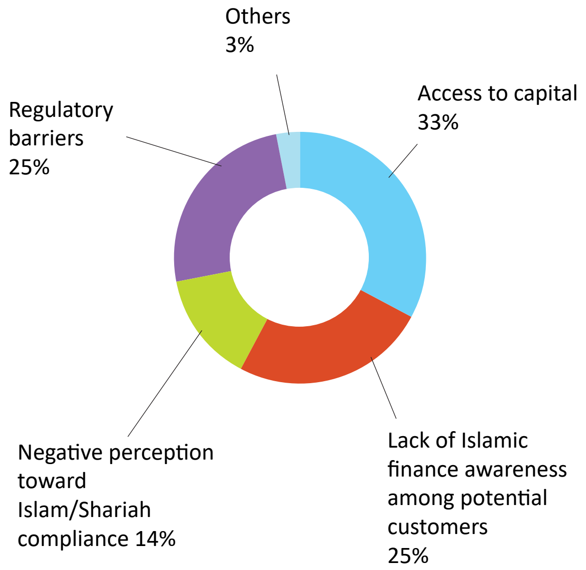
As far as challenges are concerned, Islamic fintech practitioners maintain that access to capital remains the biggest hurdle Islamic fintech start-ups face in scaling up, followed by the poor Islamic finance literacy among target market segments and unsupportive regulations.

These concerns are pervasive and persistent, as reflected from the IFN Fintech study conducted last year.

When asked about what is needed to drive the industry forward, a majority of the CEOs and founders expressed the need for regulatory enhancement to better facilitate and support Islamic fintech start-ups in navigating the local environment, greater Islamic and digital finance awareness among users and stakeholders as well as the need for a larger pool of capital for Shariah fintech ventures.

"Regulatory framework needs to be improved to create a level playing field. Big banks need to be constrained from creating barriers to entry," explained one practitioner. Others echoed the sentiment, also calling for streamlined regulatory approval processes as well as joint awareness campaigns to improve Islamic financial literacy.

Chart 6: What are the biggest challenges you face in scaling up?



Future

Optimistic growth potential

Despite severe economic challenges triggered by the global pandemic, the CEOs and founders surveyed were optimistic on the growth potential and demand for Shariah compliant fintech services over the medium term. Almost half believed that the value for the global Islamic fintech market would double by 2025, with a quarter of the total respondents opining that the market would quadruple over the same period.

"I think the market is ripe for an exponential growth as a result of the aftermath of the COVID-19 pandemic. The opportunity for growth lies in people seeking financing that is more equitable, impact-driven and is void of exploitation," one market leader commented.

Another echoed a similar sentiment.

"The market will grow naturally with there being more access to funds via online platforms and the ability to invest across the globe from the comfort of your own home. The potential for growth is huge but it needs to be carefully structured," one industry leader shared.

A handful also held the opinion that initiatives post-pandemic, particularly those centering around financial inclusion and sustainable finance, taken by governments could contribute to driving the demand and value for Islamic fintech products and services.

Chart 7: Factors for a conducive Islamic fintech environment