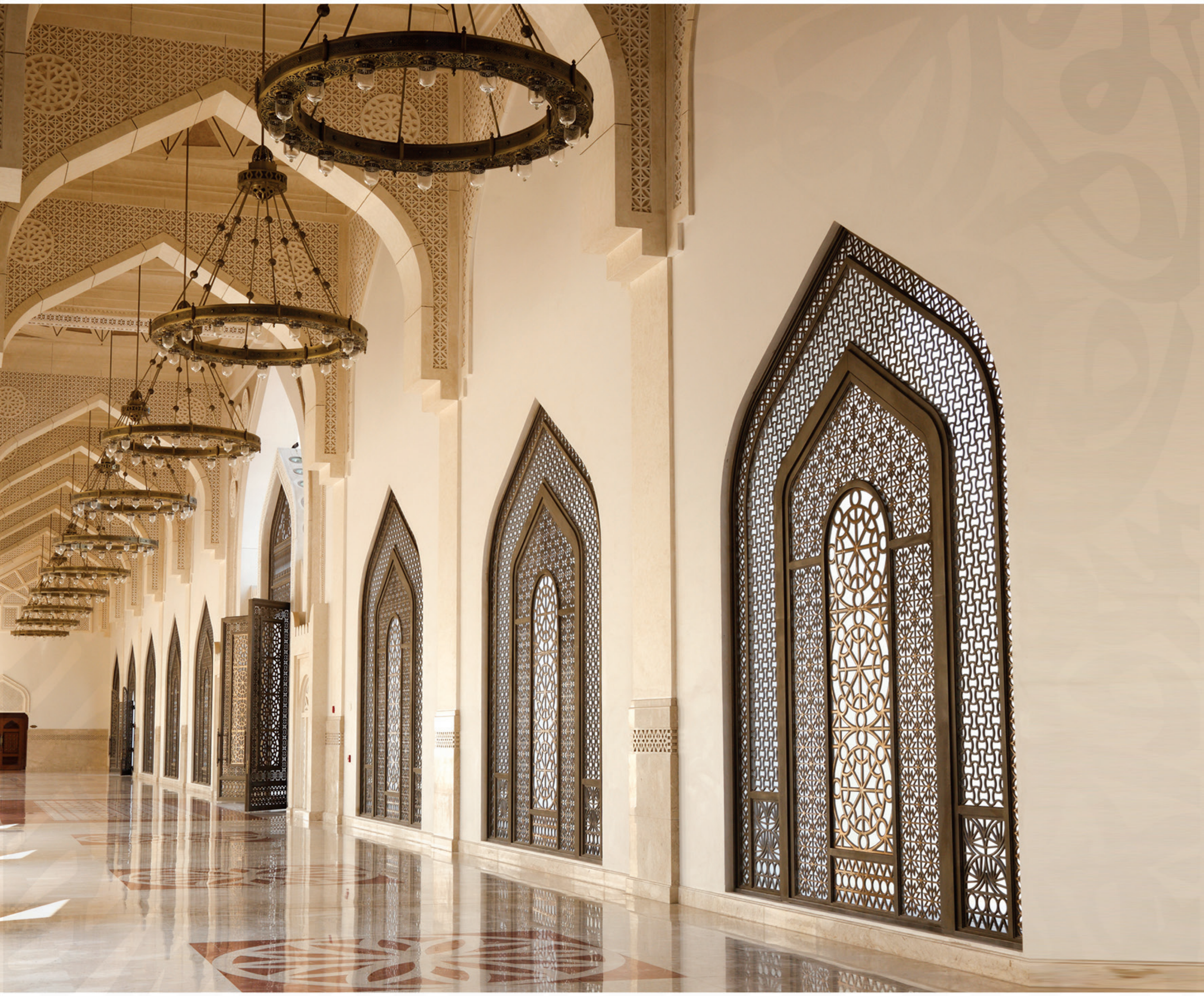
Bait Al-Mashura Journal

مجلة بيت المشورة

International Academic Refereed Journal On Islamic Economics and Finance

Issue (14) State of Qatar - October 2020



Published by

Bait Al-Mashura Finance Consultations

ISSN : 2409-0867 إلكتروني

ISSN : 2410-6836 ورقـــي

mashurajournal.com

بسم الله الرحمن الرحيم

In the Name of Allah the Most Gracious the Most Merciful

رقم الإيداع بدار الكتب القطرية : ٢٠٢٠/٥٥٦
الرقم الدولي (ردمك) : ٩٧٨/٩٩٢٧/٤٠٧٩/١/٨

(البحوث المنشورة تعبر عن رأي كاتبيها)

مجلة بيت المشورة

مجلة دولية محكمة في الاقتصاد والتمويل الإسلامي

الجهة المصدرة

Published by:

بيت المشورة للاستشارات المالية

الدوحة - قطر ص.ب: 23471

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- Once the research is published, the researcher will be provided with a letter of gratitude along with an electronic copy of the journal in which the research has been published.

الفهـرس

تقديم

بسم الله الرحمن الرحيم

الحمد لله رب العالمين، والصلاة والسلام على نبينا محمد، وعلى آله وصحبه أجمعين، أما بعد:

لقد أولت قواعد ومبادئ الشريعة الإسلامية اهتماماً كبيراً بشأن العلم والبحث العلمي، ودعت إلى التفكر والتدبر في الآيات الكونية والحقائق العلمية، وحثت على بذل الجهد ودراسة العلوم الفلكية والطبيعية والاجتماعية بفروعها، وتوجيه الطاقات إلى البحث الدقيق في كافة مجالات وأمور الحياة من أجل الوصول إلى نتائج تفي بحاجة المجتمع وتسهم ببنائه وتطوره، وبهذه الدافعية نشطت وازدهرت فنون العلم والمعرفة في ظل الحضارة الإسلامية وأصبحت منارة يستضاء بها ومرجعاً للحركة العلمية والنهضة المعرفية.

وإن المتتبع لمسيرة التطور والازدهار في عالمنا اليوم والسباق التكنولوجي في تشكيل بنية وصورة المستقبل يدرك يقيناً أثر البحث العلمي المتخصص وإسهامه الكبير في تحقيق ذلك الارتقاء، وأهمية ارتباط المجتمع بكافة قطاعاته الصحية والصناعية والاقتصادية وغيرها بالبحث العلمي المنهجي الرصين، وضرورة تبني الحركة البحثية ودعمها للنهوض بنتاجها وتحقيق أهدافها.

ولقد سعت «مجلة بيت المشورة» إلى نشر النتاج العلمي المميز ضمن تخصصها إسهاماً منها في تطوير ونهضة علوم الاقتصاد والتمويل الإسلامي، ودعماً لمؤسساته التطبيقية، وتنمية المجتمع من خلال إتاحة محتواها المعرفي للباحثين والقرّاء، وتجويده وفق معايير الضبط العلمي المعتمدة دولياً.

ويطيب لنا أن نقدم لكم العدد الرابع عشر من «مجلة بيت المشورة»، والذي تضمن بحثًا حول مؤشرات الحوكمة في دول منظمة التعاون الإسلامي،ودراسةً لعقد الـتأمين التعاوني وتكييفه الفقهي، بالإضافة إلى دراسةٍ لتعليمات الحوكمة الشرعية لمؤسسات الصناعة المالية الإسلامية في الكويت، كما ضم العدد دراسةً لضوابط الاجتهاد في النوازل الوقفية متناولاً جائحة كوفيد 19 نموذجاً، وبحثًا حول معايير فرز الاستثمار الحلال متناولاً حالة أسواق الأسهم الخليجية. ونؤكد للسادة الباحثين والمتخصصين اهتمامنا وترحيبنا بآرائهم ومقترحاتهم، وحرصنا على كل ما فيه تطوير وازدهار المجلة، لتحقيق رسالتنا وأهدافنا النبيلة، سائلين الله تعالى التوفيق والسداد والهداية والرشاد.

هيئة تحرير المجلة

Studies and Researches

Revisiting the Halal screening investments: the case of GCC stock markets

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Abstract
This study provides a critical review of the issues associated with the screening of Islamic funds in the Gulf Cooperation Council (GCC) and questions the concept of Shariah-compliant (Halal) equity investment. Unlike prior relevant studies, the paper attempts to provide evidence as whether there is a necessity to invest in commingled Halal (CH) for a Halal diversified portfolio post the global financial crisis (GFC). This paper aims to explore how participants define and screen Shariah-compliant (Halal) investment, it particularly investigates whether pure Halal (PH) and commingled Halal (CH) equity investments are distinct or similar type of investments. The paper reports the findings of the semi-structured interviews with key participants in the Islamic funds industry mainly in Kuwait and other GCC countries. The findings from the interviews reveals that the Shariah-compliance equity investments are split into two different categories, namely: pure Halal (PH) and commingled Halal (CH) investments not as reported in the literature when measuring their screens or performance. Some interviewees seriously questioned the Shariah-compliance of CH stocks and thought that the fatwa that allows CH stocks should be revisited. The interviews findings highlight the need for harmonizing the Shariah screening criteria, and the development of accounting standards based on Islamic values rather than western ones to reflect the unique characteristics of Halal investments.

Keywords: Islamic investment funds, Halal Investments, Shariah screening, Shariah-compliance investment, pure Halal stocks (PH), commingled Halal stocks (CH)

مراجعة معايير فرز الاستثمارات الحلال، دراسة حالة أسواق الأسهم الخليجية

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(سلّم البحث للنشر في 16/ 3/2020م، واعتمد للنشر في 21/ 6/ 2020م)

https://doi.org/10.33001/M011020201479

الملخص

تهدف هذه الدراسة إلى مراجعة المعايير الشرعية المطبقة في فرز أسهم الشركات الحلال التي تستثمر بها الصناديق الإسلامية في دول مجلس التعاون الخليجي عموما والكويت خصوصا. خلافا للدراسات السابقة، تبحث الدراسة مدى حاجة الصناديق الإسلامية للاستثمار في الشركات المختلطة (المتوافقة مع المعايير الشرعية) لتنويع مخاطرها بعد الأزمة المالية العالمية. كما تنظر الدراسة في مفهوم الشركات الحلال وتصنيفها إلى شركات نقية (إسلامية) أو مختلطة (المتوافقة مع المعايير) والفرق بينهما. وذلك من خلال استطلاع آراء الأطراف الرئيسية ذات الصلة بصناعة الاستثمارات الحلال عبر مقابلات شبه منظمة.

تشير نتائج المقابلات إلى تقرير فروق جوهرية بين أسهم الشركات النقية والمختلطة

باعتبارهما صنفين مختلفين من الاستثمارات خلافا لما تذكره كثير من الأدبيات السابقة التي تضعهم في بوتقة واحدة عند دراسة الأداء أو معايير فرز الاستثمارات. أظهرت الدراسة أن هناك دعوات جادة لمراجعة الفتوى الشرعية التي أجازت الاستثمار في أسهم الشركات المختلطة حتى بعد الأزمة المالية حيث إن الحاجة لهذا النوع من الاستثمارات لم تعد كالسابق عندما أجيزت. كما أكد المقابلون على أهمية توحيد معايير فرز أسهم الشركات الحلال وتطوير المعايير المحاسبية بما يتناسب مع القيم الإسلامية التي تعكس خصائص الصناديق الإسلامية لا القيم الغربية.

الكلمات المفتاحية: صناديق الاستثمار الإسلامية، الاستثمارات الحلال، معايير الفرز الشرعية، الاستثمار المتوافق مع الشريعة، الشركات النقية، الشركات المختلطة

1. Introduction

This research is motivated by the significant growth of the Islamic (Halal) investment funds industry in the GCC countries and particularly in Kuwait. Most previous studies on Halal investment funds used quantitative techniques to understand their characteristics. This research, however, adds to the extant body of knowledge by exploring the practical issues surrounding the Islamic equity investments industry via qualitative methods, using in depth semi-structured interviews. Interviews were conducted with 58 stakeholders from a wide variety of groups in the Halal investment funds industry in Kuwait and the GCC countries. This is because there is a scarcity of data and literature about Shariah-compliant screening in Kuwait and GCC, and the difficulty in quantifying some of the Shariah issues related to the Halal investment industry. The paper investigates interviewees' perceptions regarding the concept of Islamic, Shariah-compliant or Halal (permissible) investments, the motivations and drivers for the industry's growth, and Shariah issues underpinning such investment practices, related to screening and asset allocation.

In practice, it is common to find GCC Islamic funds and investors investing in both 'pure' Halal (PH) and 'commingled' Halal (CH) stocks that contain some 'sin' element based on certain Shariah screening criteria. In addition, some Halal funds and Halal seeking investors invest only in pure Halal stocks. This is because investing in CH stocks was established by a fatwa (a Shariah opinion) at a time when pure Halal stocks were scarce, and hence, this was granted as an exception, and is not an ideal Halal investment option (Al-Shubali, 2005; Al-Tunaji, 2009; Al-Nifasa, 2010). Thus, voices have been raised to revisit this fatwa[(1)] with current information and empirical evidence (Al-Tunaji, 2009) to see whether Islamic funds (and investors) still need to invest in CH investee companies. Therefore, contrary to most academic research on Islamic equity investments, this paper responds to these calls and, hence, bridges this significant gap in the literature.

Hence, contrary to other Islamic fund studies, this research paper aims to provide empirical evidence as to whether there is still a need to invest in CH stocks in Kuwait, as a case study of the GCC, considered a hub of Islamic finance and investment, triggered by their mounting oil wealth and economic growth. Moreover, the paper bridges the gap between the professional and academic research by focusing on practical issues that are not well addressed

(1) A religious opinion, ruling or provision regarding an incident that has occurred or is expected to occur (AAOIFI, 2010).

in the literature. It challenges the definition and screening of Sharia-compliant equity investments. The findings of this paper will support SSBs, regulators, and policy makers in deciding whether to revisit the current Shariah screening criteria of CH stocks.

In order to achieve these research objectives, the study attempts to answer the following two main research questions:
(1) How do participants define and screen Shariah-compliant (Halal) investment? are PH and CH equity investments distinct or similar type of investments?
(2) Do participants believe that CH stocks are still necessary for a Halal diversified portfolio?

2. Literature Review

Halal investment funds must eliminate the stocks of companies that indulge in 'sin' activities as their core business; (e.g. manufacturing or distributing alcohol). Shariah scholars allow investments in the stocks of companies that fully conform to Shariah guidelines, which do not borrow or keep surplus cash in interest-bearing accounts (Usmani, 2010). However, investment in companies whose core business is Halal, but that sometimes borrow or receive small amounts of interest or sin revenue is widely debated by Shariah scholars from different schools of thought (Abdul Rahman et al., 2010). These companies are usually called "commingled" investee companies, as their core businesses are Halal but may include some earnings generated from Haram (unlawful) non-operating activities (Usmani, 2010). The term 'commingled' investee companies is not found in the academic literature that empirically investigates the screening or performance of Islamic funds, as Islamic equity assets are described as Shariah-compliant equity investments. Hence, the literature does not distinguish between commingled Halal stocks (CH), commingled sin stocks (CS), or pure Halal stocks (PH) as separate investment categories. The difference between CH and CS is that the former complies with certain screening criteria, while the latter ones fail to comply with such criteria.

The debate about commingled companies is elaborated only in the Arabic fiqh (Islamic Jurisprudence) literature (see Al-Nashmi, 1998; Al-Salaami, 1998; Al-Manea, 1998; Al-Qurdi, 2001; Al-Birwari, 2001; Al-Quradaqi, 2002; Al-Khalel, 2005; Al-Shubali, 2005; Al-Nifasa, 2010). These studies discuss the legitimacy of investment in such stocks from a Shariah point of view, based on the premise that it is common for companies in a global interest-based financial system to borrow from conventional financial institutions to finance their activities (Abdul Rahman et al., 2010). Many Islamic international bodies have contributed to the development of the Shariah-compliant equity investment industry, including: The Organization of Islamic Conferences (OIC); the Fiqh Academy; the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI)(2); the Islamic Development Bank (IDB); and the Islamic Financial Services Board (IFSB). This issue was first discussed at the seventh conference of the OIC Fiqh Academy in Saudi Arabia on 9-14 May 1992, then subsequently at a conference held by the Kuwait Finance House in Kuwait on 2-4 November 1998 (Al-Quradaqi, 2002). During that period, very few Islamic financial institutions (IFIs) existed that offered Shariah-compliant financing to large companies or could be invested in by Islamic fund managers or even by individual Muslim investors. However, since then, the number of IFIs has increased. For instance, it is more popular nowadays in the GCC countries to find Islamic funds and investors who invest only in 'pure' Halal stocks that have SSB. Indeed, it is the role of the SSB to continue to ensure that such investee companies do not engage in any Haram transactions (Abdul Rahman, 2010; Kasim and Sanusi, 2013).

Some Shariah scholars forbid investments in the stocks of companies with any degree of involvement in Haram activities (see: Al-Qurdi, 2001; Al-Nashmi, 1998). Therefore, some investors avoid investing in 'commingled' stocks, even if the Haram element is a minor component of the business, such as airlines, hotels and supermarket chains that sell alcohol or pork (Wilson, 2004; Al-Qurdi, 2001; Al-Tunaji, 2009).

Shariah scholars who forbid investments in any CH companies do not differentiate between a large or small Haram element, and thus do not consider the financial screening. This, nevertheless, may result in a limited selection of potential securities to include in a Halal investment portfolio.

On the other hand, another group of Shariah scholars, who form the majority of SSBs of Islamic funds, permit investment in CH stocks (Al-Birwari, 2001). This group of scholars who allow investment in CH stocks argue that the existing global financial system is dominated by the tenets of capitalism. Hence, finding fully Shariah-compliant securities is difficult within the pervasiveness of interest transactions (Al-Quradaqi, 2002; Khatkhatay and

(2) AAOIFI Shariah Standard No. 21

Nisar, 2007; Derigs and Marzban, 2008; Usmani, 2010; Hutchinson et al., 2018). Thus, investing only in PH investee companies may create a hardship for Muslim investors, because most listed stocks are CH companies (Al-Shubali, 2005; Al-Nifasa, 2010), including leading stocks in the markets. Henceforth, Shariah scholars tolerate investments in CH stocks as an exception in certain conditions (Kamal, 2001; Al-Quradaqi, 2002; SAC, 2007), until a reasonable number of pure Halal stocks becomes available (Al-Tunaji, 2009; Al-Nifasa, 2010). They argue that investing in certain companies (e.g. utilities, infrastructure industries) has importance and general benefit for Muslim nations and countries, given that the Haram element is very small (Al-Quradaqi, 2002; Al-Shubali, 2005; SAC, 2007). This group of Shariah scholars argue that, if a company's primary business is Halal but it keeps its surplus income in an interest-bearing account, for instance, the fact that it receives a small incidental (non-operating) interest income will not render all of the company's business Haram (Usmani, 2010), based on the fiqh legal that mixing an immaterial proportion of Haram with a majority of Halal does not render the whole entity Haram (Al-Quradaqi, 2002). Therefore, some Shariah scholars relax different screening criteria for commingled equity investments, which are discussed extensively in the literature. These criteria are divided into two types of screen: (i) qualitative (sector or business) screens; and (ii) quantitative (financial) screens (see: Siddiqui, 2007; Khatkhatay and Nisar, 2007; Derigs and Marzban, 2008; Abdul Rahman, 2010; Marzban and Asutay, 2012; Ho et al., 2012; Pok, 2012; Mahfooz and Ahmed, 2014; Rahman, 2015; Ho, 2015; Hutchinson et al., 2018).

The debate among Shariah scholars, especially among those who seek to discourage investment in CH stocks, had made Muslim involvement in the stock markets very scant during the past few decades. Nevertheless, changes which took place in the 1990's, due to the development of more open jurisprudential views, led to the emergence of several Islamic indices (Hassan and Lewis, 2007) and attracted more interest in Islamic equity investment.

Nonetheless, allowing investments in CH stocks is not ideal, and is rather, a contemporary stage, and thus, further steps should be taken to encourage Islamic funds and investors to move towards investing in only pure Halal investee companies (Al-Tunaji, 2009). Therefore, these Shariah views on CH stocks have led some to call for the fatwa on investing in commingled companies to be revisited, considering the growth of these purely Islamic companies (Al-Tunaji, 2009) especially in the GCC region. This is because the fatwa allowing CH stocks is restricted to the need and necessity for such investment (Al-Shubali, 2005; Al-Tunaji, 2009) which may no longer exist nowadays.

3. Research method and Sample

Semi-structured interviews were chosen for this research to generate rich insights into practical Shariah issues underpinning Halal equity investments in GCC counties in general and in Kuwait in particular.

Hence, during 2012, 58 semi-structured interviews were conducted mainly in the state of Kuwait, while six interviews out of the total were conducted in other GCC countries, namely in Saudi Arabia, Qatar, Bahrain, and UAE. Interviews were conducted in 2012, following the recovery of economy from the GFC in 2008-2009, to investigate the underpinning issues facing the industry post the GFC period. To address the main objective of this study is explore whether to revisit the current Shariah screening criteria practice of Halal stocks, that did not change since 2006 (AAOIFI).Therefore, the findings of key stakeholders interviewees will help to see the issue from a different perspective post the GFC as market capitalization that is an element of screening criteria has dropped severely. Consequently, even though the interviews take place in 2012, the findings still hold today.

Besides, the number of pure Islamic companies (PH) in the GCC, grew rapidly until the GFC and Kuwait accommodates most PH companies (according to Al-Muthanna Islamic index(3)). Hence, it is interesting to understand the reasons for this growth during this period and how is this is impacted post the GFC. Moreover, as of September 2011, the supervision of investment companies and investment funds was transferred from the Central Bank of Kuwait (CBK) to the Capital Markets Authority (CMA), and the role of the CBK became limited to supervising the financing activities of investment companies (CBK annual report, 2012). Further, CMA introduced new regulations in 2011-2012 to increase transparency, protect the rights of shareholders and investment fund holders, and enhances market performance and efficiency. Hence, the interviews included participants from both CMA and CBK regulatory bodies to explore their role after the GFC in supporting the industry.

One interviewee was from the largest Islamic index provider in the Middle East, based in Egypt but whose head office is in the USA. The researchers

(3) The Al-Muthanna Islamic index (MUDX) is a weighted index that tracks the performance of 57 PH listed on the KSE. The index was launched on the 1st of March 2009 (see https://www.kfhcapital.com.kw/Islamic_fund_detail_page2_en.cms).

had no difficulty in arranging this large number of interviews, compared to other studies, as the researchers worked in the industry and had access to participants. This adds to the significance of this study, since it contributes to the lack of comprehensive in-depth investigation with this wide range of practitioners in the field of the Islamic funds industry. Being at the forefront of the Islamic fund industry is highly valuable for a thorough understanding of the examined issues, some of which are investigated for the first time, contributing to our knowledge.

The broad themes were highlighted at the beginning of each interview and interviewees were asked to talk freely about the issues. The interviews were conducted in Arabic, apart from three which were conducted in English, as the participants were non-Arab speakers.[4] Each interview session lasted 30-45 minutes. Interviews were recorded with the permission of the interviewees and were then transcribed in Arabic, relevant parts also being translated into English. Since the number of interviews was large, Excel templates were used to summarize and analyze interviewees' responses.

The interview questions were established based on the literature review including the fiqh literature in Arabic, and modern portfolio theory, and from the prior pilot interviews with several practitioners in the Islamic funds industry. (See appendix for the interview questions.)

Table 1 provides background information about the interviewees, namely: fund managers (FM), Shariah supervisory board members (SSB) and Shariah auditors, and Others, which includes investors, index providers, and regulators. The interviewees were assigned codes so that their identity would remain anonymous.

(4) They are FM10 and FM14 who are from the US and Other 2 (index provider) is from India (see Table 1).

Table 1: Interviewees' Summary Details

No.	Interviewee	Gender	Qualification	Invest in GCC	Organization	Location	No.	Interviewee	Gender	Qualification	Position	Organization	Location
1	FM1	Male	Masters	Yes	Con. Inv. Comp.	Kuwait	**24**	SS1	Male	PhD	SSB	AAOIFI	Kuwait
2	FM2	Male	Bachelors	No	Con. Inv. Comp.	Kuwait	**25**	SS2	Male	PhD	SSB	Kuwait University	Kuwait
3	FM3	Male	Masters	Yes	Con. Inv. Comp.	Kuwait	**26**	SS3	Male	PhD	SSB	Kuwait University	Kuwait
4	FM4	Male	Masters	Yes	Con. Inv. Comp.	Kuwait	**27**	SS4	Male	PhD	SSB	Kuwait University	Kuwait
5	FM5	Male	Masters	Yes	Con. Inv. Comp.	Kuwait	**28**	SS5	Male	PhD	SSB	Kuwait University	Kuwait
6	FM6	Male	Masters	Yes	Con. Inv. Comp.	Kuwait	**29**	SS6	Male	PhD	SSB	Kuwait University	Kuwait
7	FM7	Male	Masters	Yes	Islamic. Inv. Co.	Kuwait	**30**	SS7	Male	PhD	SSB	Kuwait University	Kuwait
8	FM8	Male	Master	Yes	Islamic. Inv. Co.	Kuwait	**31**	SS8	Male	PhD	SSB	*Shariah* Consulting Co.	Kuwait
9	FM9	Male	Bachelors	No	Islamic. Inv. Co.	Kuwait	**32**	SS9	Male	PhD	SSB	HCCAS*	Kuwait
10	FM10	Male	Masters	No	Islamic. Inv. Co.	Kuwait	**33**	SS10	Male	PhD	SSB	*Shariah* Consulting Co.	Kuwait
11	FM11	Male	Masters	No	Islamic. Inv. Co.	Kuwait	**34**	SS11	Male	PhD	SSB	Islamic Development Bank	K.S.A
12	FM12	Male	Masters	No	Islamic. Inv. Co.	Kuwait	**35**	SS12	Male	PhD	SSB	HCCAS*	Kuwait
13	FM13	Male	Masters	Yes	Islamic. Inv. Co.	Kuwait	**36**	SS13	Male	Masters	S.A	Islamic Inv. Co	Kuwait
14	FM14	Male	PhD	No	Islamic. Inv. Co.	Kuwait	**37**	SS14	Male	Bachelors	S.A	*Shariah* Consulting Co.	Kuwait
15	FM15	Male	Masters	No	Consulting Co.	Kuwait	**38**	SS15	Male	Masters	S.A	*Shariah* Consulting Co.	Kuwait
16	FM16	Male	Masters	Yes	Islamic. Inv. Co.	Kuwait	**39**	SS16	Male	Masters	S.A	Islamic Bank	Kuwait
17	FM17	Male	Masters	No	Consulting Co.	Egypt	**40**	SS17	Male	PhD	S.A	Islamic Bank	Kuwait

18	FM18	Male	Bachelors	No	Institutional Inv.	Kuwait	**41**	SS18	Male	Bachelors	S.A	*Shariah* Consulting Co.	Kuwait
19	FM19	Male	Masters	No	Institutional Inv.	Kuwait	**42**	SS19	Male	Masters	S.A	Islamic Inv. Co.	Bahrain
20	FM20	Male	Bachelors	Yes	Institutional Inv.	Kuwait	**43**	SS20	Male	PhD	S.A	Islamic Inv. Co.	Qatar
21	FM21	Male	Masters	Yes	Institutional Inv.	Kuwait	**44**	SS21	Male	Bachelors	S.A	Islamic Bank	UAE
22	FM22	Male	Bachelors	No	Institutional Inv.	Kuwait	**45**	SS22	Male	Masters	S.A	Islamic Inv. Co.	KSA
23	FM23	Male	PhD	No	Institutional Inv.	K.S.A	**46**	Other1	Male	Masters	Index Provider	Islamic Inv. Co	Kuwait
							47	Other2	Male	Masters	Index Provider	Islamic Inv. Co	Kuwait
							48	Other3	Female	Masters	Index Provider	Islamic Inv. Co	Kuwait
							49	Other4	Female	Masters	Index Provider	Conventional .Inv. Co	Kuwait
							50	Other5	Male	PhD	Index Provider	Consulting Co	Egypt
							51	Other6	Male	PhD	Investor	Kuwait University	Kuwait
							52	Other7	Male	Masters	Investor	Islamic Inv. Co	Kuwait
							53	Other8	Male	PhD	Investor	Kuwait University	Kuwait
							54	Other9	Male	Bachelors	Investor	Ministry of Education	Kuwait
							55	Other10	Male	Bachelors	Investor	Ministry of Islamic Studies	Kuwait
							56	Other11	Male	Bachelors	Regulator	CBK	Kuwait
							57	Other12	Male	PhD	Regulator	CMA	Kuwait
							58	Other13	Female	Bachelors	Regulator	KSE	Kuwait

*Note: This table displays summary background information about the interviewees. The interviewees were assigned codes in order that their identities remain anonymous; these codes are reported in the interviewee column. The codes used express the category of the participant. FM represents fund manager or an institutional investor. SS is used to describe Shariah Supervisory board member (SSB) or Shariah Auditors, while Other is used to describe Index providers, investors, and regulators. An * HCCAS is the abbreviation of Higher Consultant Committee for Application of Shariah law in Kuwait.*

An inspection of Table 1 reveals that only 3 interviewees were females, because most fund managers, investors, and Shariah scholars are men; however, more women are getting involved in the industry as noted by some of the interviewees. Most interviewees had a higher education (either master's or PhD degrees) and are in Kuwait. Although the findings of the interviews cannot usually be generalized, the interviews of this study reflect a high proportion of the Islamic equity industry population in Kuwait, and thus the findings can, to some extent, be generalized. For instance, the fund managers interviewed represent 85% of the Islamic equity fund managers in Kuwait (22 out of 26), including all (100%) of the six pure Islamic equity funds offered by the largest Islamic and conventional investment companies in Kuwait. In addition, the interviews cover all five Islamic index providers in Kuwait and the largest Islamic index and screening provider in the Middle East. The interviews also cover all (100%) four Shariah list providers in Kuwait, including the largest two Shariah consulting companies in Kuwait. This captures 100% of Islamic indices and list providers. Furthermore, interviews were conducted with the twelve most active Shariah scholars in the GCC, who are also SSB members across the globe. Three of them are ranked among the top ten scholars in the world; these top ten scholars hold 450 out of 1141 SSB positions and represent 40% of the Islamic finance industry worldwide (Ünal , 2011). These twelve SSB members are also members in the Higher Consultant Committee for Application of Shariah law in Kuwait (HCCAS), the AAOIFI in Bahrain, the S&P Global Islamic Index, the Islamic Development Bank in Saudi Arabia, and the international Islamic fiqh academy. Indeed, they represent the bulk of the Shariah scholars' population in Kuwait and the GCC. The same applies to the ten Shariah auditors working in six Islamic institutions in Kuwait, while the other four Shariah auditors are in UAE, Qatar, Bahrain, and Saudi Arabia. Furthermore, interviews were conducted with representatives from the three regulatory bodies in Kuwait, the CBK, Kuwait Stock Exchange (KSE), and the CMA which started to operate in March 2011. Therefore, the interviews reflect nearly all the institutions involved in Halal investing in Kuwait, and to some extent these findings are generalizable.

4. Interviews Findings

4.1 The Concept of Pure and Commingled Halal Equity Investments

In order to establish levels of understanding of Islamic funds screening criteria, it is crucial to identify precisely the concept and classification of Halal investments in the stock markets, particularly that of the Shariah scholars as they are responsible for defining such criteria. Hence, the interviews examined the understanding of these terms and whether they mean different things to different stakeholders.

The interviewees were first asked to classify and define the term "*Halal stocks*". Although the word *Halal* means lawful or permissible in *Shariah* law and is opposite to the word *Haram* that means unlawful or prohibited, there are different interpretations of a *Halal* equity investment and the *Shariah* classification of stocks. As noted by some interviewees, under Shariah only Allah has the authority to legislate what is *Haram* and what is *Halal*; human beings, regardless of their religious position, including the prophet, are not allowed to do so (see: Al-Qaradawi, 2005). Nevertheless, the interviewees indicated that investing in the stock market is a contemporary practice that is not directly covered in the holy Qur'an or the Hadith (see Al-Shubali, 2005). Hence, many interviewees in Kuwait classified Halal stocks into (i) Islamic stocks (IS) and (ii) Shariah-compliant stocks (SCS). Some interviewees described *Halal* stocks as (i) PH stocks and (ii) CH stocks to clearly differentiate between commingled *Halal* stocks (CH) from commingled sin (CS) stocks that are not permissible. Thus, CH and SCS denote the same thing, but interviewees from Saudi Arabia, Qatar, and Bahrain call them CH, while those in UAE and most of the interviewees in Kuwait describe them as SCS.

More strictly, 8 interviewees classified Halal stocks to be only PH, not commingled with any Haram proportion, even when the Haram proportion was minimal. This strict definition of Halal equity investment is only adopted by a minority of Islamic funds in the GCC. However, many interviewees indicated that a growing number of individual investors also consider only PH as Halal stocks.

The interviewees' classifications of Halal stocks are close to the contemporary fiqh literature such as Al-Manea (1998), Al-Quradaqi (2002), Al-Shubali (2005), Al-Khalel (2005) and Al-Nifasa (2010). This fiqh literature classifies stock of investee companies into three groups; PH, sin, and commingled stocks, indicating that CH and CS are reported under commingled stocks depending or their compliance with certain Shariah financial screening criteria.

The classification of Halal stocks that will be used throughout this paper will be the two investment classifications of PH and CH (and not IS and SCS). Although this classification is not used widely in Kuwait, it has been chosen to be consistent with other GCC countries and is more precise from a Shariah perspective, as deemed by some SS, and was understandable to most of the interviewees. For instance, IP3 rejected calling any company an “Islamic” company and stated:

> *“I refuse to call them Islamic companies or Islamic products just because they do not contradict Shariah. For example, if chocolate does not contain in its ingredients any alcohol, will that make it Islamic chocolate? Certainly not! If you call it a Halal chocolate, that means it is permissible for Muslims and anyone else to consume it, the same logic applies to equity investments; similar to the food industry, as we have for example Halal meat or chicken. Muslim and non-Muslim investors can invest in such stocks or products.”*

This differentiation of PH and CH is not addressed in the literature (e.g. Siddiqui, 2007; Khatkhatay and Nisar, 2007; Derigs and Marzban, 2008; Derigs and Marzban, 2009; Abdul Rahman et al., 2010; Ho et al., 2012; Marzban and Asutay, 2012) where the two Halal investment groups are always combined and called Shariah-compliant stocks or Halal investment equity funds. Nevertheless, some fund managers in the GCC have: (i) Islamic funds that invest only in PH stocks; and (ii) Islamic funds that invest in both CH and PH stocks. In addition, strict religious-based investors do not include CH stocks in their portfolios, while other religious investors diversify their portfolios across PH and CH stocks. Conventional funds and investors invest in all stocks in the market regardless of whether they are Halal or not.

Furthermore, unlike the relevant literature, the interviewees explicitly classified the non-Halal or Haram stocks into two groups as ‘sin’ and ‘commingled sin’ (CS), while others called them all sin stocks. This study will use both terms (‘sin’ and ‘CS’) to differentiate between non-Halal equity investment groups. This is because it is important to separately examine the screening of companies that operate in sin industries, and those that only fail to meet the Shariah financial screening criteria.

The interviewees were asked to define each type of stocks that they perceived as Halal as demonstrated in Table 2.

Table 2: Definition of PH Stock

	FM	SS	Other	Total
Shariah- compliant article of association and SSB	19	16	9	**44**
Shariah- compliant article of association and not Sure of SSB	4	2	2	**8**
Shariah-compliant article of association only	0	1	1	**2**
Other definitions	2	2	2	**6**

Note: this table presents the interviewees' definition of PH stocks.

Table 2 shows that the vast majority of the participants required a pure Halal stock (PH) to satisfy two conditions: (i) the company has an article of association that states clearly that all its transactions are governed by Shariah principles, or that the company's activities do not contradict Shariah provisions; and (ii) the company has a SSB that oversees its transactions and submits an annual Shariah-compliant report at the end of financial year. According to these 44 interviewees, PH stocks cover not only IFIs like Islamic banks, Halal investment companies, and Islamic insurance companies, but also non-financial investee companies such as manufacturing firms, if they meet the above two conditions.

A minority of the participants defined PH stocks exclusively as having a Shariah-compliant article of association but were not sure whether those companies should have SSB monitoring their activities or not, especially for non-financial companies. Many of these interviewees were fund managers and Others.(5)

In Kuwait, Qatar, Bahrain, and the UAE, Shariah-compliant articles of association prevent companies from operating in sin activities by law, even when they do not have an SSB, and if they violate their articles of association, regulatory bodies can penalize them. Therefore, the article of association is a safeguard over companies adhering to Shariah principles. However, the

(5) Five Fund Managers: FM5; FM7; FM14; FM15; and FM19, an investor (Other 8), and a regulator (Other 13).

interviewees admitted that there was a regulatory gap in the Halal investments industry, whereby the central bank only oversaw investee IFIs and investment funds. No regulatory body oversees whether Islamic companies in non-financial sectors meet Shariah guidelines. Some interviewees noted that CMA in Kuwait will address this gap. Nonetheless, the interviewees assumed that such companies remained Islamic in accordance with their articles of associations.

When the interviewees were asked if they accepted the claim that a company was Islamic or whether they investigated further, most of them took it as a fact without further investigation. Nevertheless, three interviewees (FM23, SS11, and SS22) did not trust these claims and investigated further. These three interviewees, who were in Saudi Arabia, stated that there was a bigger regulatory gap in their country regarding the Islamic finance industry compared to other GCC countries. For instance, they noted that only Islamic banks and Takaful companies could be described as PH stocks, as only they were required to appoint SSBs. Furthermore, in Saudi Arabia, unlike other GCC countries, there are no companies with Islamic articles of association that are overseen by a regulatory body such as the central bank or the CMA. This was also confirmed by nine interviewees (FM16, Other1, FM22, Other7, SS1, SS2, SS7, SS12, and SS13). Thus, in Saudi Arabia, nothing, apart from Islamic banks and Takaful companies (that have SSBs), stops a company from borrowing interest-based debt or earning interest-based revenues. Interviewees from Saudi Arabia[(6)] viewed this as a significant drawback, as investors must keep an eye on their stocks as these might move from being PH to CH or even to non-Halal stock from one period to another. In Kuwait, it is rare for a company to convert from PH to CH or to a non-Halal stock since they are governed by their Islamic articles of association. However, a CH could become a non-Halal stock (CS) if a fund manager's pre-determined financial screening criteria was breached. In addition, nine of the interviewees said that they had to check if there was an active Shariah board governing the operations of the investee companies and ensuring it was compliant in the case of non-financial companies. However, Other 5 said that:

> *"You still have to check their financials, especially for Islamic banks converted from conventional banking. But if their Shariah board is governing its operations and approves it as compliant, it should be a positive indication."*

(6)Interviewees: Inst. Inv.6; SS11; and SA10.

In addition, some SSs called for an active Shariah auditing system to support SSBs in Islamic funds and investee IFIs; for example, SS5 asserted that:

> "Not only Shariah supervisory boards are required but also regular independent Shariah auditors and a clear Shariah auditing system is needed to ensure the effectiveness of Shariah supervision."

Other 4, who had worked for the first Islamic index provider in the GCC region since 1999, said that:

> "We do not take the existence of the Shariah supervisory board in consideration when screening the universe to be included in our pure GCC Islamic Index. We only base our decisions on their articles of Association; if the company claims that it will follow Shariah law or will not contradict Shariah law, we accept that without going beyond it."

At the other extreme, SS3, SS6, and Other 10 had a strict definition of PH stocks; an investee company that has a strict SSB which does not allow them to invest in any CH stocks and considers them as sin stocks. This view is consistent with strict classification of Halal stocks outlined in the previous section.

Further, interviewees FM17, Other 5 and SS22 defined PH stocks as those companies that had no interest-bearing debt, interest-bearing investments, or any non-Halal income. SS8 and SS11, however, held the strictest definition of PH stocks; for instance, SS8 defined a PH stock as:

> "…a company that focuses on Islamic morals and social values, not on profit maximization, offering a sustainable and ethical alternative away from not only interest-based instruments but also from mimicking existing conventional financing instruments, such as organized Tawarruq(7), in order to provide effective solutions and added value to the economy. Because if interest is only substituted by Tawarruq or other weak Shariah backed instruments that are based on debt, not on profit and loss sharing

(7) Organized Tawarruq is a way of financing in which the seller, a financial institution, arranges a transaction by selling a commodity to the client for deferred payment. The institution then sells the commodity, as an agent on behalf of the client to a third party, in the market and then credits the price to the account of the client (Al-Suwailem, 2009).

instruments, it would represent a change just in name rather than in substance".

Some argued that what are described as PH or 'Islamic' by many, do not follow the true Islamic finance model. This is supported by Al-Suwailem (2009) who indicated that Tawarruq, for instance, should not be used in IFIs because it creates debts far larger than the cash received, like interest-based instruments, and it shifts the economy from an asset market towards a debt market, and the underlying equilibrating mechanisms are no longer linked to the real market. Most interviewees, especially SSs, admitted that investee IFIs should promote Islamic ethical norms and values to achieve the economic objectives as prescribed by Shariah rather than being solely profit driven. This finding is consistent with the literature; for example, Dusuki (2007), and the International Council of Fiqh Academy (ICFA), as the ICFA[(8)] recommends that IFIs should avoid all dubious and prohibited financial techniques in order to ensure that general Shariah objectives (Maqasid al-Shariah) are achieved (see Ziqaba, 2010; Rosly, 2010).

However, several interviewees[(9)] argued that PH stocks with the narrow perspective of SS8 and SS11 rarely existed in the market, arguing that many corporate practices have deviated from the general social and moral objectives, as affirmed by Kurran (2004), El-Gamal (2006), and Kamla (2009).

All interviewees agreed that investing in companies that operated in 'sin' industries as their core businesses, such as conventional financial services that are based on interest, or companies that operate in alcohol, tobacco, gaming (gambling), pork, pornography, and weapons businesses, was strictly prohibited. This is consistent with Al quradaqi (2002), Al-Manea (1998), Al-Shubali (2005) and Sultan (2007). However, there was a middle ground of the two extremes of pure Halal stocks (PH) and sin stocks. These are what were described by the interviewees as commingled stocks which could be commingled Halal (CH) or commingled sin (CS) stocks depending on the size of the sin element not related to their main operations. Examples of CH companies are those that operate in industries such as energy, technology, telecommunications, transportation, oil and gas, food, and real estate (Al-Shubali, 2005).

All the interviewees believed that Shariah-compliant stock-screening

(8) In their meeting: 26 – 30 April 2009 in their resolution 179.

(9) Those interviewees are: FM15, Inst.Inv.1, Individ.Inv.5, SS5, SS8, SS11, SS13, SS16, and SS18.

providers used slightly different criteria to screen the sin element for CH stocks. The interviewees indicated that, if a company failed to meet certain screening criteria then it would be considered as CS and not a CH anymore. Accordingly, some investee companies may be Shariah-compliant (CH) at a certain time period but non-Shariah-compliant (CS) in another time period due to the violation of the pre-determined Shariah-screening criteria. For instance, having interest-bearing debt of less than 30%, if breached, requires the stock to be removed from an Islamic fund's investment portfolio. This is because, as many interviewees noted, CH companies do not usually have articles of association that restrict them to following Shariah in their non-operational financing or operational activities. For example, CH companies can have conventional loans to finance their operations or invest their surpluses in interest-bearing accounts or have deposits in conventional banks.

Overall, two thirds of the interviewees, most of whom were FMs, accepted that Islamic funds could invest in CH stocks, while the other third, most of whom were SSs, believed that CH stocks should not be permissible in Islamic funds' portfolios, believing that companies had to be pure Halal (PH) investments and not commingled or involved in any non-Halal activity at all. These contested views should be reflected in the design of future empirical quantitative research in this field.

4.2 Asset allocation and the inclusion of commingled Halal Stocks

It is argued in the literature that the stricter the adherence to screening requirements, the more restrictions there are on stock selection, the less diversification is expected as suggested by modern portfolio theory. Hence, interviewees were then asked whether there is a need to include CH stocks in Islamic funds' portfolios and impacts on the diversification of Islamic funds; excluding CH stocks yields a restricted and smaller investment universe, which could have an adverse impact on their diversification and hence performance. Table 3 summarizes the respondents' perspectives toward this crucial question.

Table 3: The Need to Include CH Stocks in Islamic Portfolios

Is there a Need to include CH stocks?	FM	SS	Other	Total
Yes	16	5	4	25
No	3	11	3	17
Not Sure	4	5	7	16
Total	23	21	14	58

Note: This table summarizes all the interviewee groups' responses on whether it is necessary to include CH stocks in Islamic funds' portfolios.

Table 3 reveals divergent views regarding this issue. 25 out of 58 interviewees agreed that there is still a need to include CH stocks. The FMs were the group most likely to agree to include CH stocks from Islamic funds, as they have an interest in including them, as indicated by FM10:

> "Fund managers are not eager to talk to Shariah supervisory board members about this topic, because the more stocks they can play with the better for them"

FMs and Index providers in the Others group argued that if they were restricted to investing in PH only, their portfolios would be exposed to concentration risks, since most PH stocks are currently financial companies; hence this would not allow a well-diversified portfolio across all sectors. For example, Other 3 indicated that:

> "This an embarrassing question because I personally prefer pure Halal stocks, however, we have to offer Islamic funds that also invest in commingled Halal stocks as we have a wide range of customers including: government, institutional and individual investors, who prefer commingled Halal stocks. We think that limiting ourselves to pure Halal stocks is not sufficient to create a well-diversified and optimal risk-adjusted return portfolio,

> because we are a leading Islamic company that launched the first Islamic Fund and first Islamic index in Kuwait and our Shariah supervisory board has the same members as the Islamic Dow Jones."

Therefore, several interviewees, especially FMs, investors, and Index providers believed that banning CH stocks totally in Kuwaiti Islamic funds' portfolios would not be a good resolution, especially after GFC when financial companies were the most affected by the crisis. As a result, some interviewees, including some SSs, declared that investing in CH stocks was a necessity, referring to the old fatwa that allowed CH stocks under 'the law of necessity' or the concept of 'Umumbalwa', which refers to unfavorable widespread situations affecting most people which are difficult to avoid (SAC, 2007). Moreover, these interviewees argued that Islam had encouraged Muslims to invest their wealth, engage in business and share in economic prosperity. For example, SS11 stated that:

> "According to Islam, capital has a role to play in the economy. Hence it should not be hoarded but rather circulated to allow people to benefit from it. And investing in the stock market is a venue to achieve that, especially in operational industries that benefit the economy. In addition, small investors do not have any other opportunities other than the stock market. However, if all investors invest exclusively in pure Halal stocks, as they are a minority in the market, then their prices will be inflated beyond their actual value causing a bubble in the market and eventually leading the market to collapse and possibly a recession in the economy. Thus, investing in commingled Halal stocks is necessary to maintain a balance in the market."

Furthermore, SS20 added that:

> "Investment in stocks is a contemporary issue that did not exist in the early years of Islam and has not been stated directly in the primary sources of Shariah and is not like a regular partnership relationship but rather a special form of partnership. Thus, it requires a new Ijtihad[10] from Shariah scholars to control the

(10) The application of the faculty of reasoning by qualified Shariah scholars for forming an opinion with respect to an issue on which there is little or nothing in the Qur'an or the Sunnah (Bakar, 2008).

sin element and close a wide door of Halal investment that is commingled with a small amount of non-Halal."

In addition, interviewee SS11 highlighted that:

> "No one dare to say that receiving or giving interest is Halal, the screening criteria are Ijtihad to limit interest and other Haram activities, not to make it legitimate. For example, does restricting smoking rooms in public places make smoking permissible in Shariah or in law?! certainly not, it is only to limit the harm of smoking in society and the environment and to control it as much as possible. The same concept applies to investing in commingled investee companies."

These three quotes are in accordance with the literature (see for example: Al -Manea, 1998; Al quradaqi, 2002; Usmani, 2010). Practically, the Shariah Advisory council (SAC, 2007) in Malaysia, the SSB of Al-Rajhi Islamic Bank in Saudi Arabia(11), and most of the SSBs of Islamic index providers and Islamic funds follow the same logic, as noted by the interviewees.

On the other hand, 17 of the interviewees, notably SSs and individual investors, had the opposite view as they argued that those who allowed CH stocks should do so as an exceptional case, not as a norm. This was because when the fatwa was released, PH stocks were very rare as only a few Islamic banks and Halal investment companies were listed on GCC stock markets, leading Shariah scholars to agree on a minimum level of compliance to allow Muslim investors to invest in the stock market (see Quradaqi, 2002; Al-Shubalia, 2005; Al-Tunaji, 2009). Furthermore, some SSs indicated that a fatwa was different from Shariah law, in that a fatwa refers to how the rules of Shariah are to be applied from the point of view of the jurists, which can change from time to time as circumstances surrounding them change. Thus, many interviewees, including some FMs and investors, asserted that Shariah scholars should revisit this fatwa. For example, FM 20 said that:

> "Unfortunately, Shariah supervisory board members did not have enough commitment to take the initiative to revisit this

(11) The SSB of Al-Rajhi Islamic bank in Saudi Arabia has discussed the legitimacy of CH stocks in their Shariah resolution no. 485 in 23/ 8/ 1422 H (according to the Islamic calendar) that corresponds to 8/11/2001 and approved the investments in such stocks given that they were compliant with their screening criteria (similar to AAOIFI's screens) but restricted this approval to the necessity of such investment (Al-Tunaji, 2009).

> fatwa as they sit on multiple boards and are very busy doing that. However, things have developed and changed and thus this fatwa allowing commingled Halal stocks is 10-15 years old now, thus Shariah supervisory board members should not wait until they are asked to respond to it!"

Among these 17 interviewees who were against investing in CH stocks, some argued that investing in CH stocks had been strictly prohibited from the beginning and that the law of necessity was not applicable, as SS16 noted:

> "I do not believe that there is a necessity to include commingled Halal stocks because fund managers and investors seek to maximize their wealth only, not anything else! Hence, if there was a strict prohibition from the beginning, then we could have seen these companies converting to Islamic companies, like many conventional banks in the GCC that converted to fully fledge Islamic banks. Because if we want to build a real Islamic economy, we must sacrifice some profits in the short run, as in the long run the investment environment will improve, and awareness will increase."

Other SSs supported this, such as SS4 who pointed out:

> "Investors are shareholders or owners in the company, therefore if they know about any sin element in the company such as interest, but still decide to continue investing in their stock, then this means that they have implicitly approved the existence of that sin element, hence they would be held responsible and share the sin with them. And interest is one of the major sins in Islam. In addition, investing in the stock market is not a necessity that makes forbidden things, such as interest, permissible. Necessities should be evaluated carefully and in a proper manner"

This view is consistent with the Standing Committee for Scholarly Research and fatwa in Saudi Arabia, the SSB of Kuwait Finance House, the SSB of Dubai Islamic Bank, and the SSB of Sudan Islamic Bank (Al-Shubali, 2005; and Al-Khalel, 2005).

Between these two extreme views, 16 interviewees were not sure if CH stocks had still necessarily to be included in Halal equity portfolios. Some were SSs and acknowledged that they did not have enough information and empirical evidence to answer this question or issue a new fatwa in this regard. For instance, SS13 stated that:

> "Although pure Halal stocks and Islamic financial companies particularly have experienced a tremendous increase and growth, this fatwa has never been examined any more neither by practitioners nor by academics, and unfortunately we do not have active research centers that play this role, since it is not an easy task to make a fatwa that requires detailed information, especially after the global financial crisis."

Other 6, however, took in a middle standpoint, saying that:

> "I personally do not invest in commingled Halal stocks since they are questionable from a Shariah point of view, and also I believe that pure Halal stocks are sufficient for a well-diversified portfolio in the GCC stock markets but could be slightly difficult if limited to Kuwait only if you manage large Islamic funds, because most pure Halal stocks in Kuwait are financial companies and few companies work in industrial sectors such as petrochemicals or services. Therefore, combining all GCC pure Halal stocks will create a reasonable universe. But meanwhile, this commingled Halal stocks fatwa certainly deserves revisiting toward Islamizing those companies gradually."

Although Other 5 agreed that CH stocks were still needed for a well-diversified portfolio nowadays, he suggested that:

> "Commingled Halal stocks should still be eligible, but we should over time put more and more constraints on them, reducing the screening thresholds, handling companies in Islamic countries like the GCC states differently from global countries and so on."

The last two quotes and other interviewees' feedback suggest that more constraints should be placed progressively as a compromise to investing in CH stocks. As noted by some interviewees, this could be achieved by reducing the screening thresholds by 30% or 50% and continuing to revisit and reduce them through time, until a time comes when Islamic funds and investors can find enough PH stocks enough for a well-diversified PH portfolio.

Additionally, almost all SSs and the other interviewees agreed that the financial screening criteria should be re-evaluated, and that companies in Islamic countries should be different from western countries.

It was mainly the SSs group who knew and elaborated on the rationale underpinning the financial screening ratios; for instance, the SSs indicated that if the assets of an investee company were highly liquid it would be not permissible to invest as riba would occur.(12) A significant minority of interviewees including FMs, investors, and regulators were not fully aware of the rationale of the screening criteria. This is because most FMs and investors depended on screening providers; hence, they were not engaged in any screening process. Few interviewees reported that they were not aware of such criteria because they only invested in PH stocks. The majority said that such financial screens are a respectable form of Ijtihad conducted by Shariah scholars and they do not know much more about their rationale.

Nevertheless, some interviewees criticized the above argument determining financial ratios, indicating that there was no evidence from the Qur'an or the Hadith to back this Ijtihad, which they deemed as weak and not convincing. For example, interviewee SS16 said that:

> "Indeed, Ijtihad is a secondary source of Shariah and gives the fiqh flexibility; however, it should be based on strong evidence based on divine guidance and other secondary sources which I do not think it is the case here. I might have accepted it 15 years ago as it was a necessity at that time and we are required to apply the Shariah law gradually, but it should not be accepted anymore as the number of Islamic stocks has increased dramatically in most GCC stock markets, thus using those financial ratios is not justified anymore."

From this quote, it seems that not all practitioners in the industry are convinced of investing in CH stocks or the Shariah rationale underpinning financial screening. In fact, some voices are calling for intervention to control such investments, consistent with Al Tunaji (2009) and others.

In terms of asset allocation, the interviews findings reveal that Islamic fund

(12) According to principles of jurisprudence, money cannot be traded for money, as exchange should be for exact value in cash otherwise it would be riba (Usmani, 2002; AAIFIO Shariah standards, Alquradaqi, 2004; Alquradaqi, 2005). There is a consensus among Shariah scholars regarding this rule, however, applying it in the case of trading stocks remains debatable (Abdul Rahman, 2010). This screening ratio is mostly used in Pakistan and India.

managers who invest only in PH stocks are concentrated in the stocks of Islamic banks, investment and real estate companies. This is because most PH stocks operate in such industries, and few in other non-financial sectors. Those who could invest in both PH and CH stocks were more diversified across financial and non-financial sectors. Some interviewees, especially FMs, argued that it is hard to find 7-10 fundamentally robust PH stocks, especially after the GFC. However, individual investors, SSs and regulators believed that investors were able to pick up good PH stocks from different sectors and obtain reasonable returns. This could be because FMs manage large capitalized portfolios and need to allocate investments across a wider range of stocks to avoid concentration in certain sectors. 32 % of the interviewees indicated that they only needed 10-15 stocks to diversify away the systematic risk of their portfolios, whereas 14% said that they needed 15-20 stocks, while 12% mentioned 20-30 stocks. SSs were not aware of the asset allocation or any of the investment decisions, indicating that they are not involved in the technical aspects. This may suggest that there is a separation between Shariah experts and FMs, as noted earlier.

All research participants agreed that there were diversification benefits by investing in more than one GCC stock market to enhance the performance of Islamic funds, especially those that only invested in PH stocks. This is similar to that findings of Balli et al. (2013) who find that portfolios diversified across GCC stock markets perform better than those within local markets. The participants believed that it would be a diversification advantage if Halal portfolios were constructed across the GCC markets. In addition, most interviewees also confirmed that there will be diversification benefits for foreign investors of ethical and socially responsible investment SRI to invest in Halal equity investments, as ethical and SRI are very close to Halal investment (Haniffa and Hudaib, 2007).

4.3 Source of Information Used in Screening and Harmonization the Criteria

The interviewees were then asked about the sources of information employed when evaluating investee companies from a Shariah perceptive to classify them into PH, CH, CS and Sin. About 27% of the interviewees only examined the articles of association to confirm if they had SSB and looked at their annual report to see the names of the SSB members as well as their Shariah report, but not the financial statements. However, 38% of the interviewees, who invested in CH stocks, indicated that they used the financial statements and attached notes. One quarter of the interviewees noted that list providers used financial reports and obtained information directly from the investee companies themselves, in some cases by speaking directly to them, because they believed that published available information was not sufficient to decide if certain stocks were Halal or not. The interviewees agreed that the financial reports with their notes were the most important source of information for evaluating CH stocks, while the articles of association and the existence of SSBs were the most important sources of information for evaluating PH stocks. 61% of the interviewees felt that the level of disclosure in the annual reports was enough to determine (to some extent) Halal investments; however, 34% of them highlighted that there is a lack of Shariah-related disclosure. They noted that annual reports and financial statements are not prepared for Halal-seeking investors as they are based on western accounting standards. This is consistent with Azmi et al. (2017) who indicated that this disclosure deficiency creates several challenges for Shariah screeners. Some interviewees asserted that the degree of disclosed information, the terminology used, the explanatory notes and accounting policies used were diverse. They pointed out that the annual financial disclosure practices of Islamic companies within the same country and among other GCC countries were inconsistent, and incomparable in some cases.

Many interviewees pointed out that PH and CH investee companies' annual reports were very similar to conventional annual reports. This accords with Derigs and Marzban (2008), as it was unclear in this study whether certain items were Halal (e.g. other income, cash in banks, debt, other investments, investment in securities, and other liabilities). For instance, interviewee SS16 reported that:

> "When we screen the annual and financial reports, it is our job for example to find out whether the item debt in the balance sheet refers to an interest-based debt or a Halal based debt such as Murabaha! Hence, there is a need for accounting information and terminology to be regulated in order to enhance the credibility and comparability of the annual reports and the screening process for Halal-seeking investors, why not follow central banks that have adopted AAOIFI's Islamic accounting standards for Islamic companies?"

Interviewee Other 3, for instance, reported that:

> "We, as an Halal investment company and Islamic Index and screeners, maintain good relationships with most investee companies to facilitate any information required for screening but this consumes time and effort. Thus, it is essential that the regulatory bodies intervene in this regard, compelling all listed companies to report certain accounting items to facilitate Shariah screening. I expect companies would respond positively because many investee companies are interested in being targeted by Islamic funds and investors as they think that this will raise their stock price in the market."

Ideally, a comprehensive Islamic accounting and auditing framework and disclosure system that underpinned Islamic values is preferable, as suggested by some interviewees. For instance, interviewee SS13 noted that:

> "Islamic companies in different countries use disclosure systems that are based on the western capitalistic accounting standards. Indeed, such disclosure systems do not reveal full compliance with Shariah. Therefore, it is hard to claim that such a company is 100% purely Islamic. Hence, there is a need to develop accounting standards and a disclosure system [framework] based on Islamic values, in order to cater for the unique characteristics of Islamic companies' products (e.g. Musharakah, Mudarabah, Murabahah) and social values (e.g. Zakat), or at least Islamic companies should offer additional disclosure that address these Shariah concerns. However, since commingled companies are not governed by Shariah, they are not obliged to disclose such additional information, which again is challenging for Shariah list providers"(13)

This view is consistent with that of Karim (2001), Lewis (2001), Harahap (2003), Kamla et al. (2006), Maali et al. (2006), Haniffa and Hudaib (2007), Kamla (2009), Yaacob and Donglah (2012), Kasim and Sanusi (2013), Sarea and Hanefah (2013), and Azmi et al. (2017). Some interviewees argued that AAOIFI Islamic accounting standards offer a good model for adoption, which

(13) Musharakah (partnership) is a partnership contract in which both parties contribute capital and may form a joint Management, while a Mudarabah is a partnership contract in which one partner contributes capital and the other partner invests time and effort (Bakar, 2008).

is consistent with Kamla (2009) who criticized AAOIFI's role by imitating western capitalistic driven accounting bodies. Kamla (2009) indicates that AAOIFI's accounting standards draw on the most dominant accounting and auditing practices, with emphasis on technical issues related to interest prohibition and Zakat calculation rather than holistic Islamic and social values. Lewis (2001), El-Gamal (2006), Hassan and Lewis (2007), and Kamla (2009) argue that Islamic accounting standards should be based first on Islamic values and teachings, and then consider western accounting standards. However, the interviewees pointed out that such an approach is difficult to implement, due to western influences on business and culture in Islamic countries (also see Maali et al., 2006). The interviewees revealed that regulators are not interested in playing an active role in this regard. For example, Other 12 (a CBK officer) provided the following argument:

> "I have to confess that the Islamic fund industry in Kuwait is self-regulated; we left it in the hands of the Shariah boards who are qualified and trustworthy people, because we are not experts in this field, and there was a sudden rapid growth in this industry, and we had to respond to the strong demand. Thus, the market itself is capable of producing sound and qualified individual and institutional Shariah experts, because our intervention could deprive the market from good brains and limit the flexibility and innovation of the industry if we have one unique Shariah authority here at the central bank."

On the other hand, many interviewees blamed the regulatory authorities for being ineffective and passive, compared to their role towards conventional counterparties. The interviewees affirmed that in Kuwait, Qatar and Saudi Arabia, the Islamic fund industry is self-regulated with no central Shariah authority at the central bank or any other regulatory body. Nevertheless, in Bahrain and UAE there is Shariah authority as a reference. The interviewees noted that the CMA in Kuwait has started to fill this gap by constructing a regulatory Shariah governance system for the Islamic finance industry. For instance, interviewee Other 11 stated that:

> "… [T]he good news is that the awareness in the regulatory level of the importance to develop better regulations for the Islamic finance and investment industry has improved. For example, the newly emerged regulatory body in Kuwait, the Capital Markets

> Authority, has established recently a fully independent central Shariah Council that will work on a full-time basis to address all these issues you have just presented and is expected to publish detailed codes in this regard"

Therefore, the regulators need to put more emphasis to develop a comprehensive financial infrastructure for Islamic finance and investment that includes Islamic accounting practices and appropriate disclosure requirements, valuation standards, and a Shariah governance framework.

Furthermore, interviewees noted that for commingled investee companies, that are not governed by Shariah, additional disclosures were required to purify the non-Halal income. Interviewees reported that the concept of 'purification' was applicable when the non-Halal revenues of a stock is 5% or less of the total revenues or total income; if the non-Halal revenues exceeded this tolerance level, then the stock is considered to be non-Halal (MS) and should be filtered out and removed from the portfolio if it was part of it, even though it was compatible before that, as noted earlier. FMs asserted that the SSBs did not allow them to use purified amounts for tax or Zakat, but rather they to be given away for charitable purposes. These findings are supported by the literature (Derigs and Marzban, 2008; AAOIFI 2010[14]; Mulcahy, 2014; Rahman, 2015; Hutchinson et al., 2018). Interviewees stated that the non-Halal earnings purification of funds was calculated annually when the audited financial information of the investee companies became available and the purification amount was deducted prior to the Islamic funds' profit distributions. The interviewees highlighted that the purification process was conducted on a stock by stock basis, not for the entire portfolio. Interviewees asserted that PH stocks do not require any purification as they are already pure from Haram earnings.

Participants were then asked if there is a need to harmonize Shariah screening criteria to produce one unique list of Shariah-compliant stocks of for all Islamic funds and for individual investors in the market. The majority agreed to such harmonizing of screening criteria. For example, interviewee FM14 highlighted that:

> "At some point of time, it will be healthier and beneficial to harmonize the various screening criteria because you do not want to have unfair competition where you are arbitraging

(14) AAOIFI Shariah Standard No. 21

> Shariah rules; secondly it is inexpensive in terms of cost and effort in duplicating the screening process, and finally it would not confuse individual investors"

Furthermore, interviewee SS9 added the following to support the above argument:

> "Shariah encourages unity among Muslim nations and harmonizing the screening criteria across Muslim countries and globally would accelerate and strengthen investment and economic cooperation among Muslim communities, and this will also attract foreign investors to invest in our countries as it will not create confusion for them"

This outcome seems to be consistent with other studies, such as Karim (2001), El-Hawary et al. (2006), Derigs and Marzban (2008), Abdul Rahman et al. (2010), Ghoul (2012), Marzban and Asuty (2012), and Ho (2015). However, some interviewees argued that there were valid reasons why diverse screening criteria were used. For instance, interviewee Other 12, a regulator in CBK, noted that:

> "Harmonization is difficult, and Islam is diversified in the sense that we have four different respectable schools of thought, where this should enhance the creativity and competition between different Halal service providers and funds. Furthermore, it allows for more flexibility to adjust for specific conditions faced by some countries or industries in different environments. And even if we, as a central bank, intervene to harmonize the screening criteria in Kuwait, we cannot do so in other countries such as Malaysia, Pakistan, or Sudan. Therefore, we would rather let people and the market decides."

Different schools of thought did not seem to have much role to play in defining screening criteria as they are based on contemporary Ijtihad or fatwa that did not exist before. However, many interviewees noted that Islamic funds' SSBs came from the different schools of thought. Some SSs outlined that harmonizing Shariah standards in general may contradict the fundamental premise of Ijtihad that provides Shariah a dynamic ability to be applied in different circumstances over time. Some interviewees rejected the idea of harmonizing the screening criteria simply because they thought that Islamic indices and screening providers offer such services as a marketing strategy to promote themselves and as a source of revenue. Hence, a single screening list in the market would diminish this opportunity. Furthermore, other interviewees refused the idea of harmonization because they argued that harmonizing accounting information should come first, and it was more important and challenging as reported earlier than harmonizing the screening criteria. Many interviewees believed that AAOIFI carried significant weight in Muslim countries, especially in the Middle East, enabling it to create a harmonized framework to encourage Halal investments in the region. This harmonization would improve the usefulness of accounting information for Halal screeners and investors.

5. Conclusion

In contrast to prior relevant literature, all the interviewees distinguished PH stocks from CH stocks, and most interviewees noted that there is a growing number of Islamic funds and individual investors in the GCC who invest merely in PH stocks, driven by religious motivation. However, the findings reveal a gap between the motivations of Islamic investors and fund managers, as investors are concerned about religious and economic motives, while fund managers are concerned mostly with profit maximization. This gap should motivate Halal investment funds to differentiate themselves from conventional ones based on religious and ethical values. This finding may explain why some Islamic fund managers resist restricting their investments in commingled Halal stocks based on the current screens or only PH stocks, as this step may reduce diversification and hence hinders Islamic funds' performance. However, this remains a research question that need to be further investigated.

Many interviewees agreed that the financial screening criteria needed to be re-evaluated toward being more Shariah-compliant and that companies in Islamic countries should be different from western countries. Hence, calls were raised suggesting imposing "tighter" screening criteria for classifying CH stocks as some interviewees seriously questioned the Shariah-compliance of CH stocks. They argued that the current financial screening criteria do not have a robust Shariah-based rationale underpinning them, and that the fatwa that they are based on should be updated. Yet, other interviewees doubted that any changes to the financial screening criteria would occur, due to the influence of the GFC.

Interestingly, interviewees agreed that the financial and annual reports with their notes were the most important source of information for evaluating CH stocks, while the articles of association and the existence of SSBs were the most important source of information for evaluating PH stocks. Some interviewees, however, asserted that the level of disclosure in companies' annual reports was low and were not prepared for screening purposes and Halal seeking investors. Thus, many of the interviewees asserted the importance of harmonizing Shariah screening criteria to produce one unique investment list for all individual investors and Islamic funds. Hereafter, some interviewees called for the establishment of an Islamic accounting and auditing framework underpinned by Shariah values, in conjunction with AAOIFI standards.

Future research on the issues discussed in this paper could be extended to extensively cover all GCC and some MENA countries and empirically investigate whether there are diversification benefits from investing in PH equity portfolios over several Muslim countries' stock markets, using advanced quantitative research methods.

Another avenue for future research is exploring the disclosure practices of investee companies to assess the quality of Shariah screening relevant information, using a disclosure index as a benchmark.

Finally, a behavioral finance research might examine the non-monetary satisfaction that may be achieved through making investment decisions, especially by PH investors. Non-monetary satisfaction means meeting investors' utility preferences not just in terms of financial returns, which may include pleasure, or religious beliefs (see Beal et al., 2005; Statman, 2005; Statman, 2017).

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Appendix: Interview Questions

Background information:

Participant: Fund managers (FM), SSB or Shariah auditors, and Others (investors, index providers, and regulators)
Age:

Years of experience:

Professional Qualifications:

Educational background:

1. How do you classify and define Halal stocks?
2. Have the number of pure and commingled Shariah-compliant companies increased over the last ten years in GCC stock markets? If so, what have been the main drivers to such growth?
3. Given the fact that the number of IFIs has increased in the GCC stock market over recent years, should it still be permissible to invest in commingled stocks?
4. How do you allocate your investments across sectors or markets?
5. Are there any diversification benefits of Islamic investing in different GCC markets? Are there any diversification opportunities for western ethical investors or Islamic investors?
6. What do you use for screening; annual accounts, information providers, or company managers?
7. To include an investee company in an Islamic fund, is it sufficient to accept its claim that is Islamic, or do you investigate further? For example, KFH (Islamic Bank).
8. Do all your funds follow the same screening criteria?
9. What happens if a Halal stock becomes non-Halal; what do you do?
10. Are there enough Halal stocks to diversify and achieve a profitable and efficient portfolio?
11. What is the Shariah rational behind the financial screening criteria and thresholds?
12. Is there a need to harmonize Shariah screening criteria? Should there be one

unique list for all Islamic funds?

13. If you invest in commingled companies, do you purify your portfolio earnings, and when and how (on cash dividend or capital gains)? And where does this amount go to?

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مجلة بيت المشورة

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العدد (14) دولة قطر - أكتوبر 2020م

تصدر عن

بيت المشورة للاستشارات المالية

إلكتروني ISSN : 2409-0867
ورقــي ISSN : 2410-6836

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