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Key Factors influencing customers to use Ar Rahnū (Islamic Pawn Shop) in Malaysia: Evidence from Bank Rakyat

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Abstract

The objective of Ar-Rahnū scheme is to establish an alternative channel of financing especially to a conventional pawn broking. The operational of Ar-Rahnū scheme is more transparent, ethical and at the same time, satisfying the Shariah requirements. Beside, the scheme is hope to contribute to the development of the Malaysian economic-socio (including all races and religions) through micro credit finance and to increase the Islamic banking products in parallel with the government goals to develop an Islamic financial system which cover all financial aspects including banking, insurances and capital market. This research aim to investigate the key factors influencing customers to use Al Rahnū. Quantative research through survey questionare was conducted to achieve objective. The frequency analyses of demographic for 107 respondents involved in this survey. Finding showed that the factor of 'Shariah View' dominated the choices of the respondents as their preferences on the Ar-Rahnū scheme. Elements of "Al Quran and Sunnah as a souce of business", "operations based on Islamic law and principle", "interest free", and "uncertainties free" ranked in the top tenth place as important to the respondents. Others factors are 'Customer Service': "issuance of receipt", "security of transactions", "fair treatment upon all religion", and "customer's confidentiality"; and the factor of 'Pledge Asset': "pawner's belongings" and "all type of gold".

Keywords: Ar Rahnū, Islamic Pawn Shop, Malaysia, Bank Rakyat

1. Introduction

Pawn shop could be assumed as a one-stop financial centre for women and men minority to obtain quick and convenient way to borrow money (Amin et al, 2007). A pawn broking services was introduced by the Chinese traders during the Malacca Sultanate in 15th century. Since then, it started to grow especially after the 19th century when tin mining were found in Larut (Johari et al, 2006). A pawn broking provide faster cash services to customers who need cash without having to face a long processing period. However, these pawn broking are based on the conventional system involves with elements of usury (*riba*) and uncertainties (*gharar*). The introduction of Islamic banking system in 1983 has encouraged the implementations of *Shariah* regulation in other finance institution such as insurance, trust unit and Islamic pawn broking (*Ar-Rahnū*). Previous study has shown the important of the Islamic pawn broking to the Muslim community (Sanusi and Johari, 2006; Mohammed et al, 2005; and Ismail and Sanusi, 2005). The establishment and development of the Islamic pawn broking (*Ar-Rahnū*) scheme provide an

alternative for Muslim community in the country to use a '*halal*' and more appropriate pawn system suit to the *shariah* needs and requirements. It is a short term fund that is free from the elements of usury (*riba* ') and uncertainties (*gharar*).

2. Concept of *Ar-Rahnu*

The *Ar-Rahnu* scheme provide a financial product for small traders and lower income group which usually have some difficulties to gain such facilities from conventional financial system. It is an Islamic collateral-based financing system, introduced as a *shariah*-based alternative and easier source of financing, with gold as collateral in exchange for cash. The Islamic pawn broking is based on four concepts that is *Qardhul Hassan* (benevolent loan), *Wadiyah YadAmanah* (trustworthiness), *Al-ujrah* (safekeeping), and *Wadiyah Yadhomanah* (safekeepingwith guarantee) (Bhatt and Sinnakkannu, 2008).

- (a) *Qardhul Hassan*: A benevolent loan (interest-free) will be granted by the financial institutions to the applicant who wishes to pawn his valuable item. The loan issued under this concept requires the borrower to pay the same amount borrowed to redeem the valuable item at the maturity of the agreed period.
- (b) *Wadiyah Yad-Amanah*: Returnable collateral is required to be produced by the borrower to guarantee the repayment of the loan. The borrower gave his trust to the lender to look after his belongings during the loan period. If something happens to the collateral item which is not in the lender's negligence, then, he should not have to replace the item.
- (c) *Al-ujrah*: This is a concept where the lender is allowed to charge a reasonable fee for the services rendered in order to keep the pawned items safe and in good condition. The financial institution normally accepts a custody of the valuable asset on a *Wadiyah* concept whereby such institution promises to keep the valuable asset in a safe place and return when the time comes. A precautionary measure such as providing security and insurance shall be taken by the lending institution to ensure its safe returns once the customer pays his debt. Under the *Wadiyah* concept, the bank will charge the customer for the services rendered in keeping the valuable asset.
- (d) *Wadiyah Yadhomanah*: The lender will be responsible to replace the missing or stolen items to the owner if lender fails to keep the agreement due to own negligence.

3. *Ar-Rahnu* Scheme in Malaysia

Since the establishment of the scheme in 1992 by MGIT, followed by PKB and Bank Rakyat in 1993, the scheme has expands tremendously giving access for the small traders and lower income group for an easy financing. However, the market penetration of Islamic pawn broking in the country was still less than 50 per cent. According to Barjoyai (1999), the amount of pawning value under the conventional pawn broking system covered almost 82 percent with a loan amounted to RM1.5 billion compared to 15 percent share of Islamic pawn broking with a value of RM275 million.

The objective of *Ar-Rahnu* scheme is to establish an alternative channel of financing especially to a conventional pawn broking. The operational of *Ar-Rahnu* scheme is more transparent, ethical and at the same time, satisfying the *Shariah* requirements. Beside, the scheme is hope to contribute to the development of the Malaysian economic-socio (including all races and religions) through micro credit finance and to increase the Islamic banking products in parallel with the government goals to develop an Islamic financial system which cover all financial aspects including banking, insurances and capital market.

Usually, the *Ar-Rahnu* scheme is a source of fund for those who need financing facility in an urgent manner for a particular period of time. Most of the users of *Ar-Rahnu* scheme have no access to other source of fund from other institutions or lack of capacity to gain loan from the financial institutions. Here, *Ar-Rahnu* scheme could provide funds for such needs as it used an easy, flexible and fast system and procedure. A survey by Ragayah (1986) showed that housewife, private employee and government's supportive category of employees could not borrowed from the premier financial institutions due to a credit worthiness (Ragayah, 1986). It was also mentioned by Barjoyai that a pawn broking scheme help the small businesses and traders in the Klang Valley, Kuala Terengganu and Kota Bharu gained an additional capital, and the same goes to a business financing for many small-scale entrepreneurs (Barjoyai, 1999). A field study by *YaPEIM* revealed that a majority of the respondents feels that the *Ar-Rahnu* scheme is good because it imposed a lower service charge, easy, faster and comply with *Shariah* requirements.

Another interesting part of the *Ar-Rahnu* scheme is in term of the cost of borrowings which is said to be lower compared to the conventional pawn broking. The graph in Figure 1.1 shows the annual cost of borrowings for the *Ar-Rahnu* scheme compared with the annual cost of borrowings for the conventional pawn broking scheme. For this purpose, it is assume that the item's pawned have an equal value and the loan margin is assumed to be 60 percent of the asset's value. The safekeeping charges are adopted from Bank Rakyat *Ar-Rahnu* scheme, and the conventional pawn broking interest rate is two percent per month (Bhatt and Sinnakkunna, 2008).

The graph shows that the Islamic pawn broking scheme (*Ar-rahnu*) have lower cost in percentage to loan amount than the conventional pawn broking scheme. The annual cost of borrowing in the *Ar-rahnu* scheme is just about half the cost of the conventional pawn broking scheme which has a flat rate of 24 percent. It is also evident that the cost of borrowing in the *Ar-rahnu* scheme is only 11 percent per annum when the collateral value is RM500.00, and it rises as the collateral value increases. However even at the collateral value level of RM 10,000.00 the cost is only 15 percent per annum while the conventional pawn broking has a flat rate of 24 percent per annum at all levels of collateral value (Bhatt and Sinnakkunna, 2008)

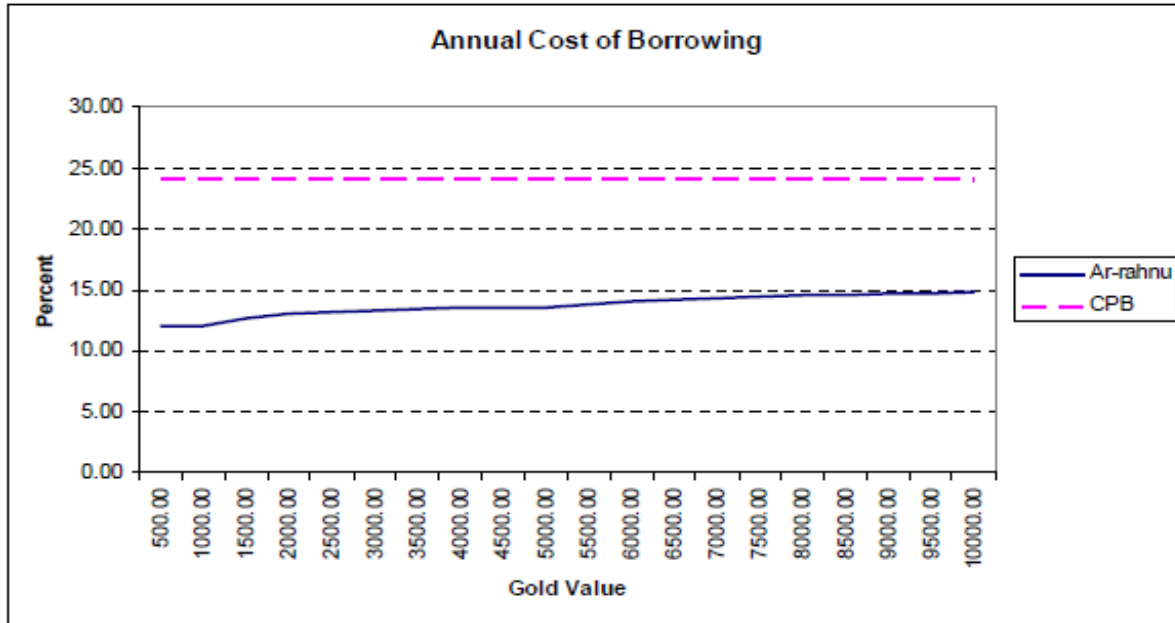


Figure 1.1: The annual cost of borrowings in *Ar-Rahnu* scheme and conventional pawn broking

Source: Bhatt and Sinnakkannu (2008)

The establishment of the *Ar-Rahnu* scheme in banking institution with an intention to provide *shariah* compliance and better alternative of financing method for Muslim community however may not be consumed at a good level of usage due to two reasons that is; A perception that banking institutions are always associate for those who has money and not suitable with a low income group with only a few gold as a pledge assets; And a possibilities that those who want quick cash may found that they are not eligible since there are red tapes in getting financing or loan from these institutions (Amin et al, 2007).

Therefore, this is one of the reasons why this studies being held. The motivation is to provide an overview on the empirical aspects towards the acceptance of *Ar-Rahnu* scheme especially the one provided by Bank Rakyat. Bank Rakyat’s *Ar-Rahnu* scheme is chosen in this study as it is the first banking institutions to introduce the scheme in 1993 after *Kedai Ar-Rahnu* being established in 1992 by Terengganu’s Islamic Pawnshop Corporation (*Muassasah Gadaian Islam Terengganu* or *MGIT*) followed by *Permodalan Kelantan Berhad (PKB)* which formed the *Ar-Rahnu* shops in Kelantan in the same year. Bank Rakyat, with the cooperation of Bank Negara Malaysia and Malaysian Islamic Economic Development Foundation (*YPEIM*) has introduced the *Ar-Rahnu* scheme in 1993. It was first introduced in six branches and the number keep increasing and as in the year of 2008, there are 112 branches (including *Kedai Ar-Rahnu*) operating throughout Malaysia (Razak, 2010).

Bank Rakyat’s *Ar-Rahnu* scheme is open to Malaysian resident age between 18 to 65 years old. It accepts gold jewellery as collateral and fees imposed for safekeeping the goods are collected based on the value and the pawning period. The rate of safekeeping charge by the *Ar-Rahnu* counters is shown in Table 1.1 below.

Table 1.1: The fees of *Ar-Rahnu* scheme in Bank Rakyat

Type of Scheme	Financing Amount	Safekeeping fee for every RM100.00 of gold value per month
<i>Ar-Rahnu</i>	RM100.00 - RM1,000.00	RM0.65
	RM1,001.00 - RM10,000.00	RM0.75
<i>Az-Zahab</i>	RM10,001.00 - RM100,000.00	RM0.75

Source: www.bankrakyat.com.my/arrahnu

A financing value is not more than 70 percent of the pawned goods value and a maximum loan is RM10,000 per day with a cumulative amount of not exceeding RM50,000 for each customer. A financing tenure is six months with extending tenure of another three months.

The scheme is more of social oriented and not for profit which would benefit the customers. It is very important to really understand the perceptions of customers towards *Ar-Rahnu* scheme in order to increase the level of acceptance among customers. In this research, factors influencing individual and customer acceptance on *Ar-Rahnu* scheme especially the scheme provided by Bank Rakyat is studied to identify the significant influences on the acceptance towards the scheme.

4. *Ar-Rahnu* Scheme in Bank Rakyat

Bank Rakyat's *Ar-Rahnu* scheme was established in 1993 when it was introduced in six branches. As on January 2011, the scheme has been offered at all 126 branches of the bank and 23 outlets of its owned *Ar-Rahnu* Exchange. The cumulative financing for the *Ar-Rahnu* market as in August 2010 is RM5.8 billion, with more than 4.5 million people having benefited since the establishment. It is estimated that the *Ar-Rahnu* industry will grow by 20-30 per cent in the next five years.

As October 2010, the present share of Bank Rakyat in the country's market of Islamic pawn broking is 25 percent with a yearly loan disbursement of RM1.2 billion. The bank has planned to control about 50 percent of the country's market of Islamic pawned broking with an estimated RM2 billion and more of its outlets would be opened to achieved the goal (Business Times). As reported in November 2010, the loan disbursement from January to September of the year is RM849 million and the loan balance until August 2010 is RM1.02 billion. The bank use only 18k – 24k gold jewellery as collateral with a financing value up to 70 percent of the pawned item and open to Malaysian residents aged 18 to 65 years old. The loan which is based on *al-Wadiah* and *Qardhul Hassan* concept with a minimum loan amount of RM100.00 to a maximum of RM10,000.00 . Table 2.3 shows the comparisons of the available loans of total collateral value for Bank Rakyat and the other Islamic pawn broking in Malaysia. The customer would be charge with a safekeeping fees ranging from RM0.65 to RM0.75 per month of every RM100.00 according to the amount of the loan with a maximum loan of RM10,000.00 each time or a cumulative value of RM50,000 for each customer.

5. Research Objective

- To identify the factors influencing individual and customer acceptance on *Ar-Rahnu* (Islamic pawning) scheme.
- To specifically examine individual and customer acceptance on *Ar-Rahnu* scheme provided by Bank Rakyat.

6. Literature Review

Shariah View

“Those who devour usury will not stand as stands one whom the evil by his touch driven to madness. That is because they say: “Trade is like usury,” but Allah has permitted trade and forbidden usury” (Al Quran 2: 275). The citation of the holy Quran shows that the *shariah* aspects especially involves with usury, should not be taken less in any transactions and any acts of business. The important of *shariah* rules in the implementation of Islamic pawn broking system was studied by Ismail and Sanusi who have argued that the Islamic principles such as *wadiah*, *qardhul Hassan* and *ujra* ought to be given a careful consideration in establishing Islamic pawn broking (Ismail and Sanusi, 2005; Bhatt and Sinnakkannu, 2008; Amin et al, 2007). The *Ar-Rahnu* become clearly different from the conventional pawnshop by the implementation of the principles of *wadiah*, *qardhul Hassan* and *ujra* that eliminated the elements of *riba* and *gharar* in *Ar-Rahnu* system. (Mohammed et al, 2005; Amin et al, 2007; Bhatt and Sinnakkannu, 2008). It was founded that the *Shariah* view has a very strong relationship with the acceptance on the Islamic based pawnshop (Amin et al., 2007).

Pricing System

The important of pricing associated with the pawnshop transactions have been examined in the study by Mohammed et al (2005) and Ismail and Ahmad (1997). The service charge imposed by *Ar-Rahnu* is comparatively low, compared to conventional pawn broking system that required an interest of about two percent (Mohammed et al., 2005). A low charge by *Ar-Rahnu* contributes to a lower cost of “loan” and help to reduce the cost burden by the customer. This is consistent with the findings by Ismail and Ahmad (1997) that the cost of getting cash from MGIT is cheaper than the conventional based pawnshop that imposed a cost of two percent for the pawned item. These findings showed that it is important for the *Ar-Rahnu* shop to offer a competitive rate that reflects the average pricing system in the market. A study by Amin et al. (2007) however showed that the pricing system is insignificant with the acceptance of the Islamic-based pawnshop. It was argued that the pricing system is the main problem in introducing Islamic-based pawnshop (Amin et al., 2007).

Pledge Asset

Gold and jewellery are valuables that always accepted merchandised by the pawnshop (Amin et al., 2007). Previous studies on pawnshop have documented that the pawned item have to be valuable (Sanusi and Johari, 2006; Mohammed et al, 2005 and Ismail and Ahmad, 1997). MGIT only accepted valuables such as gold and jewellery as pawned items (Sanusi and Johari, 2006). Comparatively, conventional pawnshop accepts items beyond the gold and jewellery, including

expensive watch such as Rolex and diamonds. The Ar-Rahnu scheme that is offered by Islamic banking institutions including the one offered by Bank Rakyat only accept gold as a pawned item. Presently, these institutions are silent on the usage of other materials as pledge assets (Amin et al., 2007). Gold, as a collateral item have several advantages over other items. It is easy for resale, easy determination of purity, little space for storage and generally, retained a personal ownership (Skully, 2005; Razak, 2010). There is no evidence that there have institutions that have accepted any other valuable items as a pledge asset for short term loans (Bhatt and Sinnakkannu, 2008). The finding is also similar with the studies that mentioned gold and platinum as a pawned item (Mohammed et al., 2005). Beside jewellery, electronics assets also being mentioned as a pledge assets (Ismail and Ahmad, 1997). The gold items are highly accepted as pawned item because it maintain their value over a reasonable period of time and gained higher in liquidity. In term of pledge asset, Amin et al. (2007) suggested that it should be diversified and should not be limited to gold, but open to other valuable assets such as silver and Rolex watch, which are expensive in the contemporary business (Amin et al., 2007).

7. Findings and Data Analysis

The frequency analyses of demographic for 107 respondents involved in this survey are shown in the Table 1.2. From the analyses, most of the respondent is not a customer of *Ar-Rahnu* scheme, only 43 respondents (40.2 percent) are the user of *Ar-Rahnu* scheme. Among the users, 40 respondents (93 percent) are the customer of *Ar-Rahnu* Scheme provided by Bank Rakyat. Most of the user have been used the scheme for less than a year (62.8 percent), with only two (4.7 percent) respondents used the scheme for more than five years. About 55.8 percent of the user have been visited the *Ar-Rahnu* scheme for two to three times and 37.2 percent of them (16 respondents) just pay a one-time visit to the *Ar-Rahnu* scheme. Only one respondent (2.3 percent) have been visited the *Ar-Rahnu* scheme for more than five visits. The analysis also showed that the respondents are quite balance in gender, with male constituting 52.3 percents (56 respondents) of all respondents, while the female constitute 47.7 percents (51 respondents). In relation to age, 13.1 percents of respondents aged between 18 to 25 years old, while majority of them aged between 26 to 40 years old with 65.4 percents. There is one respondent age above 55 years old participated in the survey contributed about 0.9 percent of the respondent, and the balance with 20.6 percents aged between 41 – 55 years old. In terms of race, 98.1 percents of respondents are Malay, followed by Chinese respondents with 1.9 percents. There are no respondents from Indian and other races take part in the research. The feedbacks from respondents also showed that most of respondents are Muslim in religious with 98.1 percents followed by Buddhist with 1.9 percent. This is co-related with the aspects of races where 105 respondents of this survey are Malays where the religion of Malays are Islam, and two of the respondents are Chinese, where they are mostly Buddhist.

The result reported in Table 1.2 also indicate that in terms of respondents' education background, majority of them or about 82.2 percents had get the tertiary education level with 34 respondents or 31.8 percents have a diploma while 30 respondents (28 percents) hold a degree and 24 respondents (22.4 percents) had undergo and have a post graduate qualifications. For type of profession, about 47.7 percents of respondents are Government employee, private sector employee and self employed contributed about 18.7 percents of respondents respectively, while 15 percents are from other types of employment such as students and housewives. As depicted in Table 1.2, the majority or 41.1 percent of the respondents earn a monthly income between

RM2,500 to RM5,000, followed by 35.5 percents of the respondents with monthly income group below than RM2,500. A total of 21.5 percents of the surveyed respondents earn between RM5,000 to RM10,000 per month, while another 1.9 percents or two of the respondents earn more than RM10,000 per month.

Table 1.2 : Profile of the respondents

No.	Profile	Description	Frequency	%
1.	Status	Customer	43	59.8
		Not a Customer	64	40.2
2.	<i>Ar-Rahnu's</i> (customer)	Institution Bank Rakyat	40	93.0
		Other Institution	3	7.0
3.	No. of Years Involve	< 1 Year	27	62.8
		2 – 3 Years	14	32.6
		4 – 5 Years	-	-
		> 5 Years	2	4.7
4.	No. of Visit	Only Once	16	37.2
		2 – 3 Times	24	55.8
		4 – 5 Times	2	4.7
		Above 5 Times	1	2.3
5.	Gender	Male	56	52.3
		Female	51	47.7
6.	Age	18 – 25 years	14	13.1
		26 – 40 years	70	65.4
		41 – 55 years	22	20.6
		56 years and above	1	0.9
7.	Race	Malay	105	98.1
		Chinese	2	1.9
		Indian	-	-
		Others	-	-
8.	Religion	Muslim	105	98.1
		Buddhist	2	1.9
		Hindu	-	-
		Christian	-	-
		Others	-	-
9.	Education	Secondary	19	17.8
		Diploma	34	31.8
		Graduate	30	28.0
		Post Graduate & above	24	22.4
10.	Profession	Government Employee	51	47.7
		Private Employee	20	66.4
		Self Employed	20	85.0
		Others	16	100.0
11.	Monthly Income	< RM2,500	38	35.5
		> RM2,500 – RM5,000	44	41.1
		> RM5,001 – RM10,000	23	21.5
		> RM10,000	2	1.9

Descriptive Analysis

The mean, standard deviation of 10 highest ranked customer preferences items is showed in the Table 1.3. This is to look on the important of these elements to the respondents relating to the customer preferences and the acceptance of the *Ar-Rahnu* scheme or the Islamic pawn broking system. The result shows that the factor of ‘*Shariah View*’ dominated the choices of the respondents as their preferences on the *Ar-Rahnu* scheme. Elements of “*Al Quran* and *Sunnah* as a souce of business”, “operations based on Islamic law and principle”, “interest free”, and “uncertainties free” ranked in the top tenth place as important to the respondents. Others factors are ‘Customer Service’: “issuance of receipt”, “security of transactions”, “fair treatment upon all religion”, and “customer’s confidentiality”; and the factor of ‘Pledge Asset’: “pawner’s belongings” and “all type of gold”.

Table 1.3: Ten highest ranked influence factor by respondent

Elements	Factors	N	Mean	Std. Deviation	Rank of Mean
Issuance of a Receipt	CS	107	4.45	.676	1
Al Quran and Sunnah as a Source of Business	SV	107	4.36	.706	2
Operations based on Islamic law and principle	SV	107	4.34	.713	3
Security of Transaction	CS	107	4.26	.664	4
Interest Free	SV	107	4.23	.875	5
Pawner's Belonging	PA	107	4.17	.771	6
Uncertainties Free	SV	107	4.13	.825	7
Fair Treatment upon all religion	CV	107	4.10	.752	8
Accept All Type of Gold	PA	107	4.09	.759	9
Customer's Confidentiality	CS	107	4.06	.787	10
Valid N (listwise)		107			

Note: CS: Customer Service, SV: *Shariah View*, PA: Pledge Asset

Table 1.4: Acceptance on *Ar-Rahnu* scheme ranked item by the respondents

Elements	N	Mean	Std. Deviation	Rank of Mean
Awareness on BR's <i>Ar-Rahnu</i> Scheme	107	4.33	.877	1
Highly Accepted	107	4.08	.826	2
<i>Ar-Rahnu</i> Scheme is Good	107	3.96	.686	3
Readiness to use BR's <i>Ar-Rahnu</i> Scheme	107	3.82	.899	4
High Quality Standard of Service	107	3.79	.789	5
Recommend to Friends & Families	107	3.73	.842	6
Valid N (listwise)	107			

This study has examines the impact of those possible influence factors towards the acceptance on *Ar-Rahnu* scheme and observed whether there are relationships between *Shariah* views, pledge assets, customer service, locality (where the *Ar-Rahnu* scheme is offered), social and advertisement factors with the acceptance on *Ar-Rahnu* scheme. The Table 1.4 showed the mean value for each influence factor's dimensions and acceptance on *Ar-Rahnu* scheme after perform transformation. The table showed that the means scale for all of the influence factors and the acceptance on the *Ar-Rahnu* scheme are between 3 (neutral) and 5 (strongly agree). In term of ranking among the influence factors, the "*Shariah View*" is ranked in the first place with a mean scale of 4.27, followed by "Pledge Asset" (4.10), "Customer Service" (4.05), "Social" (3.96), "Pricing System" (3.94), "Advertisement" (3.65) and "Locality" (3.47).

8. Conclusion

The result showed that the "*Shariah view*" have the highest mean score indicate that it is key criteria that all customer emphasis when they choose the services of *Ar-Rahnu* Scheme instead of others as they think that it is the most important factor in choosing the service. Therefore, the management of *Ar-Rahnu* institution should maintain this high level of *Shariah* compliance.

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