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Screening Criteria for the Indonesian Sharia Stock Index: An Analysis Based on Monzer Kahf's Paradigm

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Abstract

Introduction: The topic in this journal is related to the Indonesian government's policy in providing categorization of Sharia stock indices which have criteria for debt levels below 45% compared to total assets. It has a big difference compared to the major stock exchanges in the UK, USA, Malaysia, Qatar and Pakistan which have a debt ownership limit of 30%-33%. **Research Methods:** This study uses a qualitative approach method, this study focuses on hypothesis testing. Experimental research is used in a quantitative method because the financial ratio data obtained from IDX will be controlled and manipulated by the author so as to obtain the effectiveness of one of the variables. **Results:** There is a difference of 21% of the number of Sharia shares in Indonesia when using the rule of debt ownership of a maximum of 30% of assets. **Conclusion:** Hopefully, this research can give an overview of the IDX that Indonesia is still permissive so that if it is enforced, it can provide peace of mind for Muslim investors in Indonesia.

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INTRODUCTION

Stocks are one of the investment instruments in the capital market, with a high level of liquidity, causing so many investors to be interested in investing in the stock market (Handini & Dyah, n.d., p. 11). In Indonesia, stock buying and selling transactions can be done through securities listed on the Indonesia Stock Exchange (IDX). As a country with the largest Muslim population in the world ('10 Negara dengan Populasi Muslim Terbesar Dunia Menurut RISSC (2021)', n.d.) The existence of sharia stocks is an absolute necessity in the Indonesian stock market. The development of the sharia stock market is so large that the government provides a legal Law no. 19 of 2008 concerning State Sharia Securities(Siregar, 2020). Currently, in the IDX there are 936 listed companies (go public)('Profil Perusahaan Tercatat', n.d.) Spread across various sectors such as energy, raw materials, industrial, primary consumer goods, non-primary consumer goods, healthcare, finance, property and real estate, technology, infrastructure and transportation/logistics(*Saham*, n.d.). From various sectors and all stocks contained in the IDX, there is also a classification of sharia stocks or commonly known as sharia stock indexes. Where sharia stocks themselves are securities in the form of shares that do not contradict sharia principles in the Indonesian capital market. The criteria for sharia shares are contained in the Financial Services Authority Regulation (POJK) no. 35/POJK.4/2017 concerning the criteria and issuance of sharia shares('IDX Islamic', n.d.).

The stock index is a collection of various stocks in certain criteria, for the sharia stock index in Indonesia there are 4 parts, namely: ISSI (Indonesian Sharia Stock Index), JII (Jakarta Islamic Index), JII70, IDX-MES BUMN 17. ISSI is an index of sharia stocks contained in the main board and development board in the Indonesian stock exchange, JII is 30 sharia stocks in ISSI that have the best capitalization and liquidity value, JII 70 is 70 sharia stocks that have the best market capitalization and liquidation value (Dwiyanti et al., 2023) , while IDX-MES BUM 17 is 17 sharia stocks owned by SOEs and their affiliates that have the best fundamentals('IDX Islamic', n.d.).

After the Covid-19 pandemic, there has been a lot of increase in the number of investors trading on the Indonesia Stock Exchange, as summarized by the author from a publication published by the Indonesian Central Securities Depository (KSEI) that on December 26, 2018 the number of investors in the stock market was 1.6 million(Yusuf, 2019). There has been an increase of 28% compared to the data in 2017 where there were "only" 1.1 million investors. Meanwhile, data on the Indonesia Stock Exchange in February 2022 has more than 8 million investors(*Statistik Pasar Modal Indonesia*, n.d.). The increase in the number of investors in the stock exchange shows the great passion for investment among the Indonesian people, but such a great enthusiasm needs a balance for Muslim investors who transact in sharia stocks.

Currently, the practice of stock transactions by investors in buying sharia stocks does follow the release of sharia index data, but out of a total of 936 issuers that list shares, there are a total of 637 issuers labeled sharia('IDX Islamic', n.d.). This has been in accordance with OJK regulations with various qualitative provisions for company operations that do not violate sharia rules such as: *gharim* or *gharar*, *riba*, *maysir* and do not commit tyranny(Andriani, 2022) as well as quantitative provisions such as various financial ratios in a company such as the ratio of total debt to assets of a company which does not exceed 45% and total interest income and non-halal income compared to the total company income of no more than 10% (‘IDX Islamic’, n.d.).This financial ratio policy when compared to sharia stock indices in various countries tends to be permissive. A Muslim scholar named Monzer Kahf in his journal (Kahf & Al-Hajjaji, 2019) has collected various criteria in the sharia stock index screening process.

The screening process for the Sharia stock index involves both qualitative and quantitative evaluations. The first one is qualitative screening which is related to the main business of a company's operations, the main objectives and activities or business sectors in which a company is located. Companies with businesses that pass this screening process are companies that do not violate sharia rules. However, a company that produces or offers services that violate sharia does not pass this test. This criterion includes production bases or services that sell pigs and alcohol. This includes companies with an operating base that offers *interest, gharar, riba and maysir*.

Second one is quantitative screening consists of screening companies based on quantitative data, this data contains 3 aspects of financial ratios in a company, namely: debt ratio, non-permissible income ratio and liquidity ratio(Kahf & Al-Hajjaji, 2019). In this study, the author emphasizes the goal that the Indonesian Sharia Stock Index is too permissive so that many issuers have passed this index. On the basis of prudence as in QS Al Baqarah verse 275 which means: "... *And Allah has legalized buying and selling and prohibited riba*...(‘Qur’an Kemenag’, n.d.), so it is necessary for the author to provide input to the OJK to review the rules for limiting financial ratios in the quantitative criteria for an issuer to pass the sharia category. So that in the future Muslim investors will be more confident in making sharia stock transactions in Indonesia.

RESEARCH METHOD

This study adopts a mixed-method approach to evaluate the permissiveness of the Indonesian Sharia Stock Index (ISSI) in comparison to international Sharia stock indices. The data using in this paper based on International Sharia index guidelines, including those by AAOIFI, Dow Jones Islamic Market Indices, FTSE Shariah Global Equity Index, and others. Relevant academic literature, reports, and journal articles.

The step of this study is that the author screens all members of the Indonesian Sharia Stock Index following Monzer Kahf's thinking where he gives limits on several financial ratios such as debt levels, liquidity levels, and non-halal income from a company. This implementation process can be done directly through the IDX website (https://www.idx.co.id/id/investhub/stock-screener/).

RESULT AND DISCUSSION

Stock screening is a way to filter a stock based on certain criteria or indicators by investors(‘Gunakan Aplikasi Gratis Ini Untuk Screening Saham’, 2022). An investor can choose stocks with income, market capitalization, as well as various financial criteria as he wants. The sharia stock screening method is carried out in 2 main stages, namely qualitative and quantitative screening. The author overrides the qualitative screening method because the author feels that the OJK's policy in providing qualitative criteria in sharia stocks in Indonesia has been good. The author will focus on screening stocks through financial statements. The process of sorting sharia issuers quantitatively is sure to have passed the qualitative criteria. The financial ratio criteria used to assess the 3 main criteria of an issuer in the financial aspect, namely: the ratio of dependence on debt, the ratio of interest-based or non-halal income, and the liquidity ratio of an issuer(Kahf & Al-Hajjaji, 2019).

Debt Level Ratio (Leverage)

For business continuity, a company can use debt as one aspect of financial solutions. This is used to carry out the process of expansion, investment and business acquisition. A concept of riba is not only in receiving interest, but also the use of interest-based capital is also included in it. So that the use of capital from third parties with the concept of prohibited loans will certainly be against sharia law, which of course is included in the non-sharia category. Some opinions from Muslim scholars provide a certain level of flexibility in the use of conventional banking capital. The loan limit of a company is no more than 33% of its market value or of its total assets. Meanwhile, if a company uses interest-based loans above this level to finance its activities, whatever a company produces is included in the haram category. So as Muslims, it is better not to own stocks with criteria like this.

Levels of income that are not allowed

The meaning of income that is not allowed here is the income of a company from non-sharia activities such as interest from cash assets stored in banks, securities or all things that interest income. The limit of this revenue is 5% of the total income of a company(Kahf & Al-Hajjaji, 2019).

Liquidity Levels

The liquidity level here is the liquidity ratio of a company, the liquidity ratio is a measure to measure a company's ability to pay obligations that have matured and to meet unexpected needs(Al. Haryono Jusup, 2014). The level of each parameter is not in writing in the Qur'an, but all the limitations on these parameters come from the ijtihad of sharia scholars. The results of this ijtihad are published in various sharia index policies from various countries that issue sharia index categories. The majority limit of the debt ratio of a sharia company in various countries is 30% or one-third of the share. This ijtihad comes from the hadith of the Prophet narrated by Muslims "*One third, one third is quite a lot*" (Muslim bin al-Hajjaj, n.d.). Monzer Kahf is a Muslim scholar who was born in Damascus, Syria in 1940(Adhari & dkk, 2021), he gave a lot of input and thoughts on Islamic economics, Monzer Kahf's works and thoughts include the fields of zakat, waqf, government including stocks. His thoughts on stocks are written in a study on the analysis of sharia stock screening in Qatar(Kahf & Al-Hajjaji, 2019).

Comparison of Sharia Stock Index Criteria

To illustrate the differences as well as the similarities of various sharia indices, the author presents various criteria data from five sharia indices from different providers. These five indices were chosen because they are widely known and use the AAOIFI (Accounting and Auditing Organization for Islamic Financial Institutions) standards. AAOIFI is a non-profit organization for Islamic financial institutions. AAOIFI was born in Bahrain in February 1990 and is responsible for setting standards in the world of Islamic finance(‘Accounting and Auditing Organization for Islamic Financial Institutions’, n.d.). The criteria of AAOIFI itself were released in standard no. 21 of 2004 (AAOIFI, 2017, p. 568). In addition, the indices used as a comparison are “Dow Jones Islamic Market Indices”(‘S&P Dow Jones Indices’, n.d.), *screening* from FTSE *Shariah Global Equity Index*(‘FTSE Russel’, n.d.)*, Al-Rayan Islamic Index* is a sharia stock index in Qatar (‘Qatar Stock Exchange’, n.d.), Meezan Index (Pakistan)(‘Al Meezan Investment Management Ltd.’, n.d.), Bursa Malaysia (Malaysia)(‘Bursa Malaysia’, n.d.), and ISSI (Indonesian Shariah Stock Index)(‘Indonesia Stock Exchange’, n.d.). Sharia information and criteria from each index are taken from each website in August 2024.

Qualitative Screening

The following is a selection of business criteria from a company seen from a qualitative perspective, the author agrees with what is in ISSI.

Table 1. Prohibited Business Criteria from Various Indexes

Index	Prohibited Business Criteria
AAOIFI	The company does not state in the agreement, bylaws or articles of association that one of its purposes is to deal with interest, or in prohibited goods or materials such as pigs and the like (AAOIFI, 2017, p. 563).
DJIM (USA)	1. Conventional banking services 2. Alcohol 3. Products related to porks 4. Entertainment (hotels, casinos/gambling, cinemas, pornography, music etc.) 5. Tobacco 6. Weapons and defense

FTSE (UK)	1. Conventional banking 2. Alcohol 3. Products related to pigs and non-halal food production, packaging, or other activities related to pigs/non-halal food 4. Entertainment (casino, gambling and pornography) 5. Tobacco 6. Weapons production and defense
Al-Rayan (Qatar)	1. Conventional banking and insurance 2. Alcoholic beverages 3. Pork-based production 4. Pornography or related matters 5. Tobacco 6. Weapons 7. Casinos/gambling 8. Music Hotels (except sharia) 9. inemas
Meezan (Pakistan)	1. Conventional banking and insurance 2. Alcoholic beverages 3. Pork-based production 4. Tobacco 5. Weapons production
Bursa Malaysia	1. The main activities of the company do not go against the principles of sharia 2. Public perception of business activities seen from Islam must be good 3. The main business activities must be mashlahah to Muslim countries, and elements that are not allowed must be few

ISSI (Indonesia)	6. Gambling or the same as gambling 7. Trading prohibited by Islam (false demand/offer, trading without the delivery of goods) 8. Ribawi financial services 9. Buying and selling risks that contain uncertainty (gharar) and/or gambling (maysir) such as conventional insurance 10. Conducting transactions that contain elements of bribery Producing, distributing or trading goods or services of haram substances (haram li-dzatihi); Goods or services are haram not because of the substance (haram lighairihi) stipulated by DSN MUI; Goods or services that are morally damaging and/or harmful;

Source: Data processed by the author

Table 2. Screening Based on Prohibited Activities

Index	Prohibited Income Level
AAOIFI	Revenue generated from prohibited components must not exceed 5% of total revenue
DJIM (USA)	Income from prohibited activities **must not exceed 5%** of income
FTSE (UK)	Total interest income and non-compliant activities **must not exceed 5%** of total income.
AL-Rayan (Qatar)	-
Al Meezan (Pakistan)	The ratio of non-compliant revenue to total revenue **must be less than 5%**

Bursa Malaysia (Malaysia)	The limit on the profit of companies and group companies from non-sharia activities is a **maximum of 5%,** this is in the income category (conventional banking; conventional insurance; gambling; liquor and liquor-related activities; activities related to pigs and pigs; non-halal food and beverages; Entertainment that is not in accordance with sharia; interest income from conventional accounts and instruments; tobacco). **The 20% limit** on income such as: stockbroking business, rent from non-halal things, and other things that are not in line with sharia.
ISSI (Indonesia)	Total interest income and non-conforming activities compared to total maximum income of 10%

Source: Data processed by the author

Screening by Liquidity Level

Liquidity is the ability of a company to settle short-term debt obligations using current assets such as cash, accounts payable or other assets of the company (AI. Haryono Jusup, 2014). In table 2 the author tries to collect screening information based on the company's liquidity level, AAOIFI does not provide a special screening record, but for DJIM, Al-Rayan and Bursa Malaysia it provides a limit of 33%. The only difference is in the calculation method where the divisor in DJIM uses the average market capitalization in the last 24 months. The FTSE (UK) provides a limit of less than 50%. While ISSI in Indonesia does not provide a specific record for the company's liquidity level, the liquidity level is in JII, JII 70 and IDX-MES BUMN 17.

Table 3. Screening Based on Liquidity Level

Index	Liquidity Level	
AAOIFI	There is no special screening, just a note that the company's total assets, rights, and profits should not be less than one-third of the total assets('Accounting and Auditing Organization for Islamic Financial Institutions', n.d.)	
DJIM (USA)	$\frac{\text{Accounts receivables}}{\text{Average Market Capitalization (24 month average)}}$	< 33%
FTSE (UK)	$\frac{\text{Accounts receivables + Cash}}{\text{Total Asset}}$	< 50%

Al-Rayan (Qatar)	Accounts receivables + Cash / Total Asset	< 33,3%
Meezan (Pakistan)	Illiquid Assets / Total Asset	More than equal to 25%
Bursa Malaysia (Malaysia)	Cash / Total Asset	< 33%
ISSI (Indonesia)	There is no record regarding the company's liquidity requirements, the liquidity level is used for other sharia indices in ISSI	

Source: Data processed by the author

Screening based on Debt Ratio (Debt/Leverage)

In the next screening is based on the level of debt that a company has, the information that the author has collected is that AAOIFI as the parent of Islamic financial standards in the world suggests at the level of 30%. This is also followed by various other country indices such as DJIM, FTSE, Al Rayan and Bursa Malaysia by providing a threshold at the level of 33%. It is slightly different when viewed at Meezan, which is 37%. ISSI Indonesia provides a higher limit, which is 45%. At this level, the author focuses on the Indonesian index providing a looser limit on a company's debt level.

Table 4. Screening Based on Debt Level

Index	**Debt Level**	
AAOIFI	Total Debts / Market Cap	<30%
DJIM (USA)	Total Debts / Average Market Capitalization (24 month average)	< 33%
FTSE (UK)	Debts / Total Asset	< 33,33%

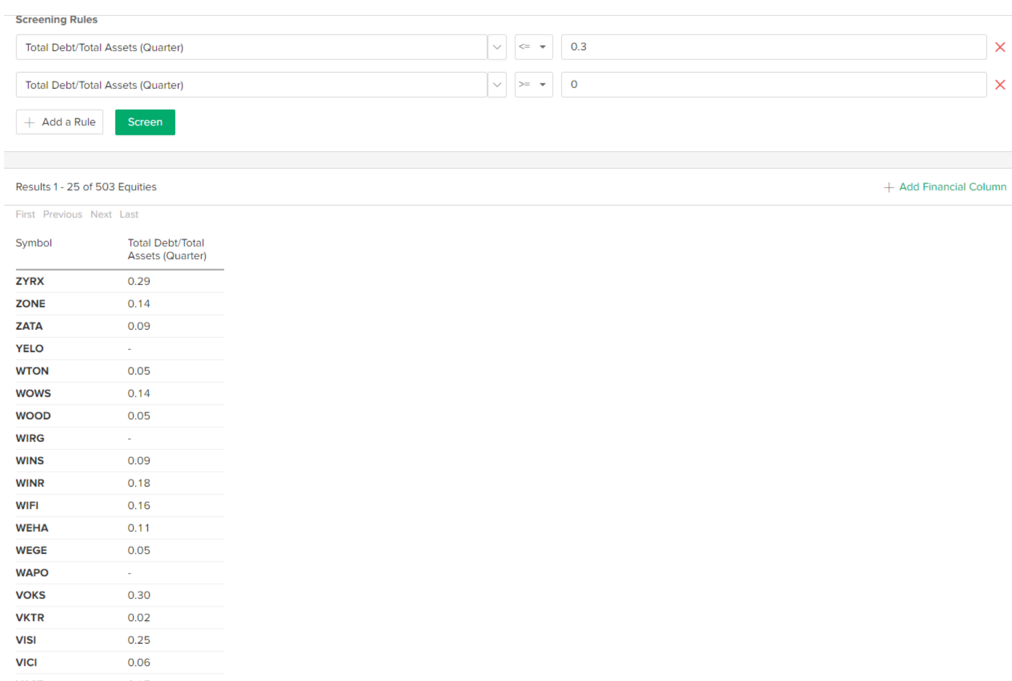
Al-Rayan (Qatar)	Total Debts / Total Assets	< 33,33%
Meezan (Pakistan)	Debts / Total Asset	< 37%
Bursa Malaysia (Malaysia)	Debts / Total Asset	< 33%
ISSI (Indonesia)	Total Debts / Total Asset	**< 45%**

Source: Data processed by the author

Results of the Screening Process of Stocks in the Sharia Category

As a result of the comparison of various sharia stock indices in the world compared to Indonesia, the author concludes that the debt ratio is the main quantitative thing in the sharia stock screening process. The author tries to use an average benchmark of 30% as the maximum threshold in the sharia stock screening process. Meanwhile, the author also added a figure above 0% because there are companies that have a negative ratio value. This is because there are companies whose total assets are lower than their total debts.

Figure 1. Screening Based on Debt Level



Source: Data processed by the author

Figure 1 shows a stock screening process in the ISSI index, where the screening results show a total of 503 equities compared to a total of 637 issuers labeled with sharia labels in the ISSI index category. The screening process has reduced as many as 134 issuers or around 21%. The results of the screening are a process carried out on the stock screener feature on stockbit securities (https://stockbit.com/screener) on September 26, 2024.

CONCLUSION

Stock screening is a process of screening stocks with certain criteria, in the stock index in Indonesia there is ISSI, namely the Indonesian Sharia Stock Index. This index is a collection of various issuers that have passed the sharia category. The process of screening shares in the sharia category is qualified in terms of qualitative, where a company does not conduct a business that violates sharia. Where this category includes not in the context of ribawi financial services, not trading things that are prohibited by sharia, gharar (uncertainty), maysir (gambling) and making transactions that contain elements of bribery('IDX Islamic', n.d.). In the quantitative screening method, emphasis is placed on the ownership of a company's debt. The average sharia stock index provides a limit of 30%. This is also in accordance with Monzer Kahf's(Kahf & Al-Hajjaji, 2019) writing as the focus of writing this article. The results of the ISSI index re-screening to 503 issuers decreased by 134 issuers from a total of 637 or around 21%. Hopefully, this research can provide confidence for Muslim investors in Indonesia and provide input to the OJK as an institution that issues sharia indexes.

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