

Intellectual Capital: How Do Islamic Ethics Rejuvenate It?

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Abstract

In this era of knowledge-based economy, intellectual capital (IC) is considered as a critical component in an organizational effort to emphasize on accomplishing competitive advantages and enhancing value added for the organization. Besides concentrating only on new product innovations, small and medium enterprises should also be engaged in managing IC in accordance to Islamic teachings. An understanding to Islamic ethics and its upshots for superior performance facilitates entrepreneurs in managing IC strategically. This paper aims to re-scrutinize several contributions in Islamic ethics and IC in SME entrepreneurial researches, ascertain the main elements of IC as well as Islamic work ethics (IWE); and thus show how IWE is relevant for research in the area of IC.

Keywords: Islamic work ethics (IWE), intellectual capital, knowledge-based, small and medium enterprises

1. Introduction

Knowledge-based economy relies heavily on intellectual competences than on physical capitals (Powell & Snellman, 2004). There has been a change in business environment caused by the usage of information technology (IT) in which knowledge and technical skills have the priority over natural resources (Brinker, 2000). The knowledge entrenched in people and organizations are known as intellectual capital (Ramezan, 2011; Cortini & Benevene, 2010; Bontis, 2004; Demediuk, 2002; Stewart, 1997). In this era, there is a growing importance of IC which is attributed to organizational wealth and gross domestic product (GDP) (Abramovitz & David, 1996; Abramovitz & David, 2000). For that reason, business success depends on organizational strategic management of intangible assets or intellectual capital (IC). Leveraging IC would lead to business success as it contributes substantially to organizational value (Keenan & Aggestam, 2001).

2. The Skandia Intellectual capital Value Scheme Theory

Many definitions of intellectual capital have been proposed by academics and practitioners. However, all of them decide that IC entails particular and systematized information usable for firm's successful business activities (Edvinsson & Sullivan, 1996). Basically, according to intellectual capital theorists, intellectual capital consists of three sub-domains: human capital (HC), organizational (or structural) capital (OC), and relational (or customer) capital (RC) (Stewart, 1997), Sveiby (1997), Bontis (1998), Dzinkowski (2000), Ramirez, Lorduy & Rojas (2007), Cortini and Benevene (2010). A clearer illustration has been done by Roos, Roos, Dragonetti and Edvinsson (1997) through the Skandia IC model as shown below:

Despite no concrete agreement on what IC is, there is still broad consensus on its definition. Mostly, IC comprises intangible assets, like knowledge, skills, customer's satisfaction, faith, loyalty, intellectual property, policies, procedures, social value, industrial property and ethics. (Edvinsson & Malone, 1997; Sveiby, 1997; Bontis, 1998; Bueno et al., 2004; Ismail & Songip, 2006). The concept of IC has been extended into two more new important elements: spiritual capital and technological capital (Ismail & Songip, 2006; Wu & Tsai, 2005) that have positive impacts on organizational performance. Ramezan (2011) described IC components as human

capital, organizational capital or structural capital, social capital technological capital and business process capital or customer capital. On the other hand, Khalique, Isa, and Shaari (2013), Khan (2014), Hashim, Osman and Alhabshi (2015) with Ullah and Hassan Yousaf (2016) synthesized IC elements into human capital, customer capital, structural capital, social capital, technological capital and spiritual capital. In spite of its multidimensionality, this study has defined IC as encompassing; (i) Human Capital (HC), (ii) Organizational Capital (OC), (iii) Relational Capital (RC), (iv) Spiritual Capital (SpC) and (v) Technological Capital (TeC).

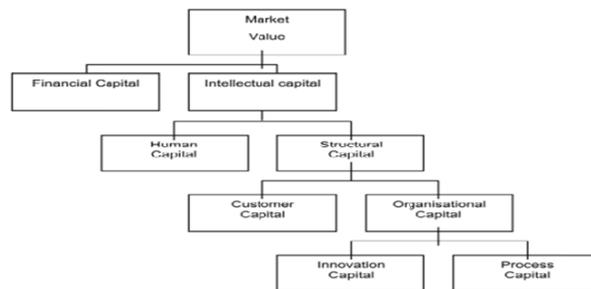


Figure 1. The Skandia Intellectual capital Value Scheme (Source: Roos et al., 1997)

2.1 Measuring Current Values

In the new economy, achieving competitive advantages is crucial for business success and in order to do so, organizations have to exploit both tangible and intangible resources i.e. IC. IC is a key successful feature for all kinds of organizations (Lonnqvist & Mettanen, 2002), including small and medium enterprises (SMEs). Hence, SMEs need to comprehend the concept of IC as to be equipped with effective and efficient management of IC. SMEs should transform their identity through the integration of the IC (Volpel, 2000) by providing employees a favorable environment to innovate, use the capability freely, and act intelligently and responsibly (Wiig, 1999). This is due to the fact that compared to large firms; SME labour productivity (measured by real GDP per worker) is rather small. As indicated in SME Annual Report 2013/2014, labour productivity of Malaysian SMEs was 2.73 times smaller than that of large firm in year 2013. Moreover, in term of labour quality, Malaysia displays a shrinking measure for the period of 2006-2012 compared to the selected developed countries (Japan, Singapore, South Korea and Finland) (MPC, 2014). Malaysia has the number of skilful and talented workers which are a smaller amount of than the average of high-income countries. It is unfortunate that the country is experiencing a deficiency of skilled workforce, weak productivity development due to lack of creativity and innovation in the labour force, and an over-dependence on unskilful cheap foreign labours (National Economic Advisory Council, 2010). These concerns must be resolved to avoid SME entrepreneurs from being bankrupt (Omar & Azmi, 2015).

What could be the reasons for these issues? Is it because of deficit in intangible assets which are considered as crucial capitals in building firm's capacity and capability to compete effectively? Or is it due to lack of understanding of Islamic ethics which is then hinders the opportunity for SME entrepreneurs to maximize their efficacy in ensuring the profitability and performance? Based on the above situation and problems arisen, a research study needs to be conducted in an attempt to know to what extent IC will assist in creating competitive advantages among SME entrepreneurs. Accordingly, below are the main problems that are necessary to be studied;

- i. SME entrepreneurs are unaware of the role of IC as a strategic tool to increase business performance.
- ii. SME entrepreneurs need to understand the impact of Islamic ethics on IC of SMEs and their business performance.

Specifically, this paper offers groundwork to researches on Islamic ethics and IC; therefore determine IWE as well as the key components of IC. It is expected that the results of this paper will contribute to the prevailing body of knowledge by providing an enhanced understanding of Islamic ethics and its outcomes for superior performance facilitates entrepreneurs in managing IC strategically. In order to postulate IC within the comprehensive area of Islamic business studies, the first section begins by explaining what is meant by IC and its main elements as well as Islamic ethics. Then the paper endeavors to elucidate the integration of Islamic work ethics (IWE) in IC by showing how it is pertinent for research in the expanse of IC.

2.2 IC and Its Sub-Domains Study

- i. Intellectual Capital (IC)

IC refers to intellectual materials - knowledge, experience, information, intellectual property, organizational technology, customer relationships and professional skill that provide the firm with competitive advantages (Stewart, 1997; Edvinsson & Malone, 1997). IC is intangible and needs to be discovered and exploited since it may offer a new resource-base to an organization in enhancing its value (Bontis, 1996).

IC sub-domains are categorized into five basic components; human capital, organizational capital, relational capital (customer and social), technological capital and spiritual capital (Khalique, Isa & Shaari, 2013; Khan, 2014; Hashim, Osman & Alhabshi, 2015; Ullah & Hassan Yousaf, 2016). Therefore, organizations ought to get the most out of its assets in these parameters so as to obtain high competitiveness in the market. The sub-domains of IC possibly will deliver further understanding of IC concept and its impact on business accomplishment (Marcin, 2013).

ii. Human Capital (HC)

Human capital represents the stock of knowledge in an organization (Bontis, Crossan & Hulland, 2002). Bontis (1998) defines human capital as the capability of firm to get the best solutions from the knowledge of its employees. Moreover, human capital is genetic inheritance, education, experience, attitudes (Hudson, 1993), skill, the relationship between ability and achievement and knowledge (Edvinsson & Richtner, 1999). Bontis (1999) claims that human capital is an imperative source for firm's strategic renewal and innovation. Indeed, human capital is the capability of intellectual in the company.

iii. Organizational Capital (OC)

Organizational capital is the infrastructure supports for human capital to work in a company. The supports consist of organizational work procedures, programs, systems, processes, and philosophies that organizations need to operate the business (Kannan & Aulbur, 2004). Specifically, organizational capital covers all the non-human knowledge in organizations, such as databases, process manuals, organizational charts, strategies, routines and whatever thing whose value to the business is higher than its physical value (Bontis, 1999). Bontis (1998) argues that organizations with weak systems and procedures to track its activities, the company's IC will not be able to be at its peak. The supportive culture in a firm with strong organizational capital will let people go for and learn new things, and not afraid to fail; thus encourage the organization to reach the fullest potential.

iv. Relational Capital (RC)

Relational capital refers to the organization's relationship with the outside environment such as alliances, suppliers, customers, partners, competitors and delivery networks. In other words, relational capital represents the organization's relationships with external parties (Jardón & Martos, 2009) such as customers, suppliers and other stakeholders (Cohen & Kaimenakis, 2007). Normally, relational capital is through SMEs' personal linkages (Adler & Kwon, 2002) that aid them to identify business prospects (Bhagavatula, Elfring, Van Tilburg & Van De Bunt, 2010).

v. Spiritual Capital (SpC)

Spiritual capital contains religious outlooks and ethical beliefs (Khalique, Bontis, Abdul Nassir & Hassan, 2015). Al-Ghazali believes that spirituality (ruhaniyyah) is what creates belief and faith for religion (Al-Ghazali, 1983, Book 3). In line with this contention, spiritual capital is based on spirit, power, influence and knowledge resulted from religion (Berger & Hefinar, 2003; Liu, 2008), moreover, it can enhance organizational performance (Ismail, 2005).

vi. *Technological Capital (TeC)*

Technological capital is an intangible capital established on innovation process and technical exercise. It comprises of research and development (R&D) and protection rights (Khalique, Bontis, Abdul Nassir & Hassan, 2015). Ramezan (2011) and Ramirez (2010) stressed that the term technological capital comes from technical knowledge and is considered as an essential component of intellectual capital. The technical knowledge refers to the usage of production innovation methods and product technology that generates firm's competitive advantages (Fernandez, Montes & Vasquez, 2000), therefore turn out to be a powerful drive for high profitability.

2.3 Islamic Ethics

Religion controls human comportment through entrenched customs and principles (Roundy, 2009). Quddus, Bailey and White (2009) highlighted that religious background and beliefs influence individual values and ethical understanding. As asserted by Othman and Hariri (2012), Christianity, Islam and Judaism have divine guidelines for their adhered followers. Consequently, people imitate their religious thoughts in practicing ethic and values in everyday and business life. Islamic principles consist of both the law and ethics associated with work, thus Muslims are obligatory to work and operate business consistent with these principles (Obaid, 2005). Work ethics assist in economic development (Congleton, 1991), besides contributing to the organizational

success (Yunus, Abdul Rahim, Shabuddin & Mazlan, 2011). Kazempour, Ashrafi and Taheri (2012) highlighted one of the main variables in organizational success is observing ethics. Most organizations pay significant attention to this matter due to positive consequences and applications of ethics and morality (Ahmadi, 2011). Abeng (1997) pointed out that organization may work more effectively and efficiently by upholding an ethical outline that monitors and aids to organize their exertion. Moreover, Islamic ethics offer the fundamentals for impartiality and tolerance to various needs, difficulties and challenges faced by an organization (Mohamed Aslam & Hafas, 2009). Islamic ethics is the ethical system molded by the teachings of the Quran and expounded by the Prophet (SAW) through actions and words (Hashi, 2011). The Quran sets the underpinning of ethical principles and the sunnah (way of Prophet's life) covers the real practices of the concepts. As mentioned in chapter 68 (Al-Qalam) of the Quran, verse 4:

"You (Prophet Muhammad) are on an exalted standard of character".

Equally, reported by Muslim (Qudsi Hadiths, 2012), hadith no.746:

"When asked about the character of the Prophet (SAW), his wife, Aishah (RA), replied: it was a reflection of the Holy Quran".

Indeed, ethical concepts taught by the Quran are personified in the Prophet's way of life, thus both the Quran and sunnah are the foundations of the Islamic ethics. To gain the pleasure of Allah (SWT), Muslims should apply the essential values of Islamic ethics (Ahmad, 2006). Furthermore, Islamic ethics encourage confidence and reinforce social business responsibilities (Ali, 2005). It is work-orientation in human life virtue (Rizk, 2008). In business, as the servants of Allah (SWT), Muslim entrepreneurs should discern and engage in Islamic ethics (Beekun & Badawi, 2004) through hard working, avoidance of wealth accumulation, commitment, dedication, work creativity, collaboration and competitiveness (Yousef, 2001). Specifically, as agreed by Muslim scholars, entrepreneurs need to practice Islamic teachings and incorporated them in their entrepreneurial activities (Ghazanfar & Islahi, 1998, Faizal, Ridhwan & Kalsom, 2013; Hoque, Mamun & Mohammad Ahshanul Mamun, 2014; Rohaiza, 2014) for the sake realizing Allah's pleasure and achieving the betterment in this world and hereafter. According to Imam Al-Ghazali, Islamic ethics comprise of four basic qualities: i) wisdom, ii) courage, iii) patience, iv) justice (Al-Ghazali, 1983, Book 3). Islamic ethics is recognized by Al-Ghazali as spiritual practice of man, imbedded in his soul and exhibited over the actions. Encompassing of the right actions towards God, family members, and the public (Muhammad, 1983). Islamic ethics will guide people, especially entrepreneurs, in securing the righteous deeds and refraining from evils. Additionally, it is moral filler of thorough business activities and enhanced firm performance (Rice, 1999). Ali (1988) mentioned that hard work and competition are encouraged to improve quality of a business. Concisely, Islamic work ethic (IWE) contends that life will be meaningless for someone who is not working; and involvement in business activities is a responsibility. Below is a summary of the IWEs' items as recommended by Ali (1988) and the reference in Al-Quran.

| Subject | Verses in Al-Quran |
|------------------------------------|---|
| 1. <i>Agreements and promises</i> | <i>Ar-Rad 13:25, Al-Qasas 28:28, Yunus 10:71</i> |
| 2. <i>Consideration for others</i> | <i>An-Nisaa' 4:36, Al-Mumtahina 60: 9</i> |
| 3. <i>Consultation</i> | <i>Ash-Shura 42:38, Taha 20:103, Al-Kahf 18:22</i> |
| 4. <i>Continuous improvement</i> | <i>Al-Araf 7:42. Cooperation. Al-Hujraat 49:9, Maryam 19:9</i> |
| 5. <i>Equality and unity</i> | <i>Al-Isra' 17:35</i> |
| 6. <i>Fairness in dealings</i> | <i>Al-Anaam 6:152, Al-Mumtahina 60:8, An-Najm 3:32, Al-Maida 5:8</i> |
| 7. <i>Fairness in wages</i> | <i>Al-Imran 3:57, Saba' 34:37</i> |
| 8. <i>Hard work</i> | <i>Al-Baqara 2:62; 82, Al-Anaam 6:135</i> |
| 9. <i>Helping others</i> | <i>As-Saff 61:14, An-Nahl 16:97, Yunus 10:41</i> |
| 10. <i>Honesty and justice.</i> | <i>Al-Baqara 2:177, Az-Zumar 39:2; 3</i> |
| 11. <i>Humble</i> | <i>Hud 11:23</i> |
| 12. <i>Patience</i> | <i>Hud 11:11</i> |
| 13. <i>Righteous/Intention</i> | <i>Al-Baqara 2:25; 225, Al-Baqara 2:62, At-Taubah:105, As-Saff 61:8, Al-Qasas 28:19</i> |

14. *Social order*

Al-Imran 3:110, Al-Baqara 2:273

15. *Truth*

Al-Anfal 8:27, Yunus 10:61, An-Nur 24:8

Source: Ali (1987)

Previous studies (Al Habtoor, 2001; Yousef, 2001; Ali, 2005; Ali & Al-Owaihian, 2008) have approved on the adoption of the IWE in management, business operations and economic undertakings. IWE measurement scales constructed by Ali (1988) has been used by many business scholars (Yousef, 2001; Rahman, Muhamad, & Othman, 2006; Ali & Al-Kazemi, 2007; Kumar & Rose, 2010; Rafiki & Wahab, 2014). Hence, this study shall be using the same scales in the expanse of IC.

3. Materials and Methods

Qualitative research is chosen to do this study which deal with ethic issues. Ethic issues are subjective and regarded as less easily measured and chartered. They touch on the search for meaning behind actions and also to understand rather to measure (Hammersly, 1992). Hence, in this context, it concerns with what and how entrepreneurs are capable to sustain their work ethics.

4. Result and Analysis

4.1 *Should Islamic Work Ethics (IWE) Be Integrated in Intellectual Capital (IC)?*

Islam is a complete way of life (ad-Din), covering every single aspect to guide all human activities and business operations, and so Muslim entrepreneurs' values should perpetrate Islamic teachings; ruled by Al-Quran and Sunnah. Muslim entrepreneurs should capitalize their organizational assets in IC and strive to meet religious goals in order to acquire high competitiveness in business. Specifically, they must focus on the management of IC fore mostly on pleasing Allah (SWT), consistent with the moral and Islamic ethics, fulfilling religious obligations and profiting the public as a whole; besides increasing value creation capabilities and competitiveness of the organizations.

It is indeed a plus factor for them as Islamic ethics and spirit infuse the qualities of dynamism in being good Muslims (Solaiman & Hillaly, 1997); which possibly refining dynamic competencies in global competitiveness orientation. As IC supports an organizational competitiveness advantage (Phusavat, Comepa, Sitko-Lutek, & Ooi, 2011), good Muslim entrepreneurs, possessing IC-related conducts such as diligence, commitment, devotion, creativeness, cooperation and competitiveness (Yousef, 2001) shall definitely strengthen a firm's value-creation. This is due to the fact that individual development in Islamic approach not only accommodates central human needs, but also provides opportunities for better material life applied for an organizational success (Zangoueinzhad & Moshabaki, 2011). Accordingly, in managing IC of a firm, entrepreneurs have to foster Islamic ethics such as prayer, patience, gratitude, reliance on Allah, faith, gratification, self-composure, mildness, modesty, knowledge, sincerity, modesty, loyalty, self-respect, silence and deliberateness (Al-Ghazali, 2004). As a result, these merits will endorse decent demeanor, leading to submission and salvation (Al-Ghazali, 2004). Besides, an entrepreneur who endeavors to improve the business performance as a means of piety to Allah (SWT), he is actually worshipping according to the Prophet's teachings (Al-Ghazali, 1983, Book 2).

4.2 *Should Islamic Work Ethics (IWE) Be Integrated in Human Capital (HC)?*

Incorporating ethics into HC management would significantly augment the quality of organizational performance (Mehralian, Rajabzadeh, Sadeh, & Rasekh, 2012). Sakinah and Ahmad Azrin (2016) have agreed that HC and Islamic ethics would encourage initiatives among entrepreneurs in making their businesses successful. Further, Moghaddam, Akhavan and Mehralian (2015) have listed several ethics such as trust, devotion, commitment, hard-work, responsibility, and just that can inspire employees to have greater HC and work at their full capability for business development. Moreover, a prominent scholar and teacher, Imam Al-Ghazali had appreciated HC in which he promoted Muslims to pursue the needed knowledge (Al-Ghazali, 1983, Book 1). Hence, in capitalizing in HC, Al-Ghazali asserted that entrepreneurs should adopt IWE and integrate it in their entrepreneurial undertakings. The assimilation of IWE in HC will definitely offer a balance guiding principle as it has complete means to achieve success in this world and hereafter.

4.3 *Should Islamic Work Ethics (IWE) Be Integrated in Organizational Capital (OC)?*

One of the connotations of ethics given by Solomon (1984) is the social rules administer and bound our behavior, especially the critical procedures about right and wrong. The procedures are also known as morality. Hence, in operating a business, organizational work procedures, programs, systems, processes, and philosophies should be implemented in accordance to appropriate ethical rules or IWE. SME entrepreneurs ought to integrate ethical contents or IWE in OC and monitor its execution from time to time. Jalil, Azam and Rahman (2010) suggested

that business organizations need to have business ethical code which stipulates the ethical contents. Proper implementation of IWE can promise customer satisfaction and business profitability. Supported by Yesil, Sekkeli and Dogan (2012), IWE values influence firm performance positively.

4.4 Should Islamic Work Ethics (IWE) Be Integrated in Relational Capital (RC)?

Issues on business ethics, sustainable business practice, integrity and corporate governance have received tremendous interests (Waddock, Bodwell, & Graves, 2002). For instance, Ahmad Azrin (2015) has highlighted the issue of organizational corporate social responsibility (CSR) measurement that should be implemented with the insertion of spiritual values and considered Islamic ethics as the priority. It is a requisite to implement IWE in the company to put up with the international market. IWE will build trust in the organization, from outside environment. As mentioned by Holme (2008), suppliers will be willing to supply to companies that they can trust. So, an organization will create better relationship with suppliers whom they gain higher level of trust from. In consequence, better business reputations will be formed. IWE helps companies generate values in business operations. The value supports organizations in developing good relationship with various types of external parties, thus facilitates the companies in achieving high business performance.

4.5 Should Islamic Work Ethics (IWE) Be Integrated in Spiritual Capital (SpC)?

IWE will take entrepreneurs to higher circumstances of spiritual illumination. As mentioned by the Prophet (SAW) "Act in accordance with what you know for what you do not know (will) be unveiled to you (by Allah SWT)" (Al-Ghazali, 2004). Al-Ghazali (2011) asserted a person will achieve the uppermost satisfaction when he or she is capable to know Allah SWT closely. To attain higher level of job satisfaction, individuals should have work-life balance (material and spiritual) which would make them perform better (Sudarsono, 2010; Muafi, 2003). IWE will be able to improve the quality of life besides contributing to the economic development, thus it should be emphasized in entrepreneurial undertakings by incorporating it in spiritual capital.

4.6 Should Islamic Work Ethics (IWE) Be Integrated in Technological Capital (TeC)?

In order to survive in this era of turbulent economy, organizations need to innovate (Shan, Pan, & Zhang, 2009; Yeşil & Kaya, 2012). Business success is greatly influenced by organizational capability to indulge in production innovation methods and product technology; which are also called as technological capital. IWE will be able to enhance innovation competency of the organizations (Awan & Akram, 2012; Kumar & Rose, 2010). Abbasi, Rehman and Afsar (2009) claimed that IWE helps organization to capitalize human resources better. Positive qualities of entrepreneurs derived from IWE such as hard work, commitment, enthusiasm to work, work creativity, cooperation and just (Kumar & Rose, 2010) will enhance organizational propensity in its innovation process and technical exercise, thus attain competitive advantage.

5. Conclusion

Islam has provided guiding principles for all human activities and also advocates and enlightens business ethical values. Thus, the integration of IWE in IC will uphold the Islamic teachings and warrant success in the business organization. IC is accepted as one of the most essential assets for organization to obtain competitive benefit. Above all, SME Muslim entrepreneurs should understand that they are required to carry out IWE as inculcated in Al-Quran and Hadith. Proper integration of IWE in IC can ensure satisfaction of all stakeholders of the business organization as their ultimate desire is to gain competitive advantage and business profitability.

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