

ISLAMIC LETTERS OF CREDIT IN MALAYSIA: MAPPING LC-I STRUCTURES AND SHARĪ‘AH CONTRACT APPLICATIONS

MOHTESHAM, M. M. J.^{1*} – MOHAMED, I.²

¹ *Ahmad Ibrahim Kulliyah of Laws, International Islamic University Malaysia, Kuala Lumpur, Malaysia.*

² *School of Graduate and Professional Studies, The International Center for Education in Islamic Finance (INCEIF) University, Kuala Lumpur, Malaysia.*

**Corresponding author
e-mail: Meermoh8[at]gmail.com*

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Abstract. Letters of Credit (LCs) serve as an important mechanism for mitigating risk in international trade. As a leading hub for Islamic finance, Malaysia has developed sophisticated Islamic LCs (LC-i) structures that achieve functional equivalence with conventional instruments while strictly complying with Shariah principles. This article analyses the operational structures and Shariah contracts employed in LC-i by three prominent Malaysian financial institutions: EXIM Bank, Maybank Islamic, and Affin Islamic. Adopting a qualitative approach based on the analysis of product disclosure sheets and institutional data, the study found that Malaysian IFIs demonstrate high level of maturity in structuring LC-i to accommodate diverse needs of customers. This has been achieved by adopting suitable Shariah contracts according to commercial functions of the corresponding LC-i. In standards LC-i, dual-contract has been used, where Wakalah (Agency) is employed for cash-backed 'at sight' settlements and Murabahah (Cost-Plus) is employed for 'usance' transactions requiring financing. Furthermore, Wakalah bil Ujrah is predominantly used for advance LC-i services such as advising, transfer, confirmation, while Kafalah (Guarantee) is used for Islamic Standby Letters of Credit (SBLC-i). Further, the study also uncovers institutional innovations, such as the "Express LC-i," which expedites issuance without prior credit facilities. These insights confirm the maturity of the Malaysian ecosystem and offer a practical takeaway for policymakers and practitioners in other jurisdictions seeking to develop robust Islamic trade finance instruments.

Keywords: *Islamic trade finance, Malaysia, Letter of Credit-i, Shariah contracts, export and import*

Introduction

International trade has been widely recognised as a critical driver of economic activities. Within this context, trade finance plays an essential role and functions as a core enabler of international trade (WBG, 2021). Among the various trade financing instruments, letters of credit (LCs) constitute a fundamental component and play a vital role in international trade financing. LCs function as a secure mechanism that mitigates payment and delivery risks between contracting parties in international trade. Consequently, they are highly valued for their practicality, flexibility, reliability, and enhanced security, and are widely regarded as the lifeblood of international trade (Oseni, 2013). In essence, an LC constitutes a written undertaking by a bank, issued on the request of the importer (applicant) in favour of the exporter (beneficiary). The bank, through the LC, guarantees payment to the exporter upon the fulfilment of stipulated terms and conditions. While the LC safeguards the financial interests of the exporter by ensuring payment against documentary compliance, it also provides the importer with assurance that the seller has fulfilled the contractual obligations, as evidenced through authenticated trade documents (Adam, 2024; Oseni, 2013).

In international trade finance, LCs have been structured in various forms to cater to the specific needs of the relevant parties. For instance, revocable LC allows the issuing bank to alter or cancel the LC unilaterally without prior notice to the beneficiary, whereas an irrevocable LC cannot be amended or cancelled without the consent of all involved parties. This structure provides the beneficiary with an increased level of assurance. Similarly, LCs are also categorised based on the level of payment assurance. While an unconfirmed LC constitutes guarantee of the issuing bank only, a confirmed LC includes an additional payment guarantee from a second bank, usually located in the exporter's country. This additional guarantee protects the exporter from country-specific economic or political risks associated with the issuing bank. Other types of LCs include transferable, revolving, and standby LCs, which further improve liquidity and provide on-going backing for long-term relationships. Ultimately, the selection of a particular type of LC depends on the specific commercial needs of the involved parties (ITF, 2026; Koç, 2025; Adam, 2024; Meynell, 2024).

Given the importance of LCs in international trade finance, LCs have been adapted into Shari'ah-compliant structures within the Islamic banking framework. These structures employ Shari'ah contracts to facilitate the LC process in a Shari'ah compliant manner. Importantly, Islamic banks across various Islamic finance jurisdictions have sought to adopt various forms of LC structures in a Shari'ah-compliant manner, utilising suitable contracts to accommodate the diverse needs of their customers. Nevertheless, the extent and sophistication of such adaptations vary significantly across jurisdictions. Malaysia stands out as one of the most advanced jurisdictions in this regard. Islamic banks in Malaysia offer sophisticated and diversified Islamic LCs (LC-i) instruments that, in many aspects, exceed from other Islamic finance jurisdictions. A World Bank report identifies Malaysia as a leading country among members of the Organisation of Islamic Cooperation (OIC) in the provision of Islamic trade financing instruments (WBG, 2021). Further, Malaysian Islamic banks offer a broad range of LC-i structures with minimal disparity against their conventional counterparts. This reflects the depth and maturity of Malaysia's Islamic trade finance ecosystem and its strong capacity to support complex cross-border commercial activities (WBG, 2021).

In this context, therefore this article seeks to systematically analyse the LC-i structures offered by Malaysian Islamic banks and to critically examine the Shari'ah contracts utilised in offering these structures. In doing so, the study offers insights that may inform policymakers, regulators, and Islamic financial institutions in other jurisdictions seeking to draw lessons from Malaysia's relatively advanced LC-i practices. The article is organised into six sections. Following this introduction, the second reviews the relevant literature. The third section outlines the research methodology employed in the study. The fourth section presents the finding. The following section discusses the findings, while the final section concludes.

Literature review

Letter of Credit

Letter of Credit (LC), also referred to as a documentary credit, is one of the most extensively used instruments in export and import financing due to its practicality, adaptability, reliability, and strong security features. It is often characterised as "the lifeblood of international commerce" (Oseni, 2013). Essentially, it is a written commitment by a bank, acting at the request of an importer, to honour payment to the

exporter once the specified documentary requirements have been met. It guarantees the exporter that payment of the agreed amount will be made within the stipulated period, as long as the necessary documents, such as evidence of shipment, are submitted in proper conformity with the LC requirements. Consequently, the LC not only guarantees payment to the exporter but also protects the importer by ensuring that the goods will be disbursed only after the contractual obligations have been met and evidenced through proper documentation (Adam, 2024; Alwi, 2012). LC encompasses several key participants. Typically, the process begins with the importer (applicant), who requests a bank to issue the LC. The exporter (beneficiary) is the party entitled to receive payment once the stipulated documents are submitted in full conformity with the terms of the credit. The issuing bank, acting on behalf of the importer, formally issues the LC, assumes responsibility for honouring any presentation that meets the prescribed documentary requirements, and arranges payment to the beneficiary or the nominated bank when those conditions are fulfilled (Adam, 2024).

Depending on the structure and configuration, other parties may also include in the LC arrangement. The advising bank, usually situated in the exporter's jurisdiction, verifies the authenticity of the LC and conveys its terms to the beneficiary, but it does not undertake any responsibility for payment. In some cases, the beneficiary requests the involvement of a confirming bank, which adds its own independent guarantee to honour the payment. By doing so, the confirming bank assumes a separate liability to pay the beneficiary if the issuing bank fails to fulfil its obligation. In some cases, the negotiating bank is also involved in the process for scrutinising the documents submitted by the beneficiary, ensuring that they conform to the conditions stipulated in the LC. Once satisfied with their compliance, the negotiating bank may advance funds or effect payment to the beneficiary and subsequently request reimbursement from the issuing bank. When required, the reimbursing bank is also appointed by the issuing bank to facilitate the settlement process by honouring reimbursement claims lodged by the negotiating bank, particularly in transactions which involves multiple currencies. Additionally, some LC arrangements permit the appointment of a second beneficiary, enabling the primary beneficiary to transfer all or part of their entitlement to another party, provided such a transfer is allowed under the terms of the LC (Adam, 2024; Vaze et al., 2022; Alwi, 2012). In practice, it is common for a single financial institution to undertake multiple functions mentioned above. For example, the advising bank may concurrently act as the confirming bank, thereby not only authenticating the LC issued by the importer's bank but also extending an independent payment guarantee to the exporter. *Figure 1* illustrates the operational sequence of an LC in a real transaction facilitated by Mizuho Bank, and also highlights the bank's dual function within one transaction.

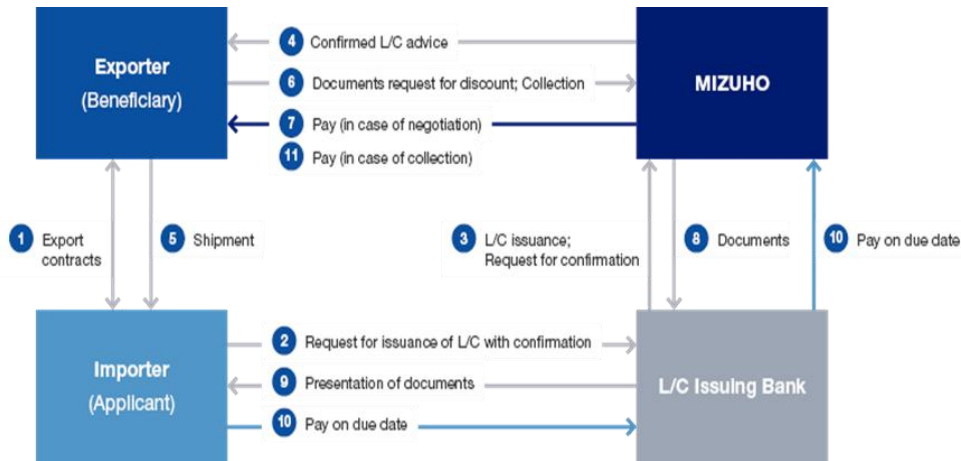


Figure 1. The operational flow of a Letter of Credit (LC) in a real application involving Mizuho Bank.

The process begins with the exporter and importer entering into a sales contract, after which the importer requests the issuance of an LC, together with a request for confirmation, from the issuing bank. The issuing bank then issues the LC and forwards it to Mizuho Bank for authentication and confirmation. Once confirmed, Mizuho advises the LC to the exporter. The exporter subsequently ships the goods and submits the required documents to Mizuho. If Mizuho also acts as the negotiating bank, it makes payment to the exporter upon receiving the documents. Otherwise, it examines the documents and forward them to the issuing bank for payment. Upon receiving compliant documents, the issuing bank forwards them to the importer, who reimburses the bank on the maturity date. The issuing bank then fulfils its undertaking by making payment to Mizuho, which subsequently remits the proceeds to the exporter, thereby completing the LC cycle.

Types of LC

As discussed previously, LCs have been structured in various forms to address the specific needs of the involved parties in international trade. The applicants select particular type of LC depending on the nature of transaction and their specific commercial needs. The following section discusses the important types of LCs and highlights the functions and purposes they serve in international trade financing.

Irrevocable vs. revocable LCs

An irrevocable LC is a type of LC which constitute a binding commitment from the issuing bank to honour the payment given that the beneficiary submits documents in full compliance with the LC terms. Irrevocable LC cannot be amended or cancelled without the consent of the involved parties. In other words, it provides beneficiary with a high level of payment assurance, as it can only be cancelled or modified with the consent from beneficiary and, if one is in place, the confirming bank. Under UCP 600 (Uniform Customs and Practice for Documentary Credits), all LCs are deemed irrevocable by default (Meynell, 2024). By contrast, a revocable LC permits the issuing bank to alter or cancel the credit unilaterally without prior notice to the beneficiary. Due to the lack of security for beneficiary, revocable LCs are rarely practiced and no longer exist under current UCP 600 (Meynell, 2024).

Confirmed vs. unconfirmed LCs

An unconfirmed LC is an LC where the beneficiary relies solely on the issuing bank's commitment to pay upon the presentation of compliant documents. In contrast, a confirmed LC includes an additional undertaking from a confirming bank, typically located in the beneficiary's country, which assumes payment responsibility if the issuing bank defaults. Confirmation is often sought in high-risk environments to enhance payment security. It offers added assurance in transactions where credit or country risk is a concern (Meynell, 2024). In some instances, confirmation may be added by the advising bank without any information to the issuing bank. This usually occurs in a private arrangement between the advising bank and the beneficiary and thus called silent confirmation. Such a situation arises where the issuing bank considers their undertaking to be sufficiently creditworthy and sees no justification to add any confirmation to it (Meynell, 2024).

LC at sight vs usance LC

At sight LC is a facility where the exporter receives the payment immediately upon presentation of compliant documents. Once the issuing bank receives the documents from the advising bank, the importer is obliged to pay immediately to obtain the shipping documents and take possession of the goods. In contrast, a usance (or deferred payment) LC offers flexibility to the importer and allows him to pay at a later agreed date while enabling him to collect the shipping documents and clear the goods immediately (ITF, 2026; Adam, 2024).

Revolving LC

A revolving LC is a facility where the credit amount automatically reinstates after use for subsequent transaction over a period of time. A revolving LC eliminates the need for issuing new documentation for each transaction and particularly suited for ongoing trade relationships between the bank and the customer. It provides consistent cash flow for exporters and facilitates a continuous, reliable supply chain for importers. This LC reduces administrative costs and enables payment for multiple, recurring transactions under a single, aggregate limit. The credit limit is either restored on a time or value basis. Time-based revolving credits restore the amount at regular intervals (e.g. monthly), while value-based revolving credits reset after previous amount has been used and paid (Adam, 2024; Meynell, 2024).

Transferable LC

A transferable LC is a type of LC that allows the first beneficiary to instructs the issuing bank to transfer all or part of the payment to a second beneficiary who is an actual supplier of the goods. It is commonly used in trade transactions which involves a middleman or intermediary. In such cases, the first beneficiary (middleman) does not supply the goods directly, rather secure the goods from the actual supplier and export them to the importer. Because the intermediary may not have enough funds to pay the supplier in advance, a transferable LC allows them to rely on the buyer's credit to ensure payment to the actual supplier. While this type of LC eliminates the needs for

intermediaries to open their own credit line, it also provides the actual supplier with the payment security (Koç, 2025; Adam, 2024; Meynell, 2024).

Back-to-Back LC

A back-to-back LC is a type of LC where two distinct but interrelated LCs are issued for the same trade transaction. Similar to transferable LC, this LC is also used where an intermediary or middleman is involved between the importer and the actual supplier. The intermediary typically does not own sufficient funds to purchase goods from the supplier. Instead, the intermediary uses the LC received from the buyer as security and purchase the goods. In this LC, the importer's bank first issues a master LC in favour of the intermediary. Then, using that master LC as backing, the intermediary's bank issues a second LC, called the back-to-back LC, to the actual supplier. Unlike a transferable LC, where the original LC is simply passed on, a back-to-back LC uses two distinct LCs, one to pay the intermediary and one to pay the supplier. The second LC is usually paid from the money received through the first LC. Unlike a transferable LC, back-to-back LC arrangement facilitates separate payment assurance to the intermediary and the supplier, adding an extra layer of the security to the transaction (Koç, 2025; Adam, 2024; Meynell, 2024).

Standby Letters of Credit (SBLCs)

A standby LC is similar to a bank's guarantee, where the bank undertakes to pay the beneficiary if the importer fails to make payment according to the agreement. Although it is used globally, this type of LC is especially prevalent in the United States. Unlike a documentary credit, which facilitates payment upon the completion of specific actions such as the shipment of goods, a standby letter of credit allows the beneficiary to claim payment in cases of non-performance or breach of contract (Adam, 2024; Meynell, 2024).

Materials and Methods

This paper adopted a qualitative method and employed an analytical approach to examine the operational structures of LC-i offered by Malaysian Islamic banks, with the objective of deriving practical insights for other Islamic finance jurisdictions. The data was collected primarily from the secondary sources, including books, journal articles, institutional reports, Islamic banks' official websites, and product disclosure sheets (PDS). Selected Malaysian Islamic banks were examined, and their publicly available documents i.e. PDS and websites were analysed to identify the types of letters of credit offered, the Shari'ah contracts employed in structuring these instruments, and the specific commercial purposes they serve. The selected banks included EXIM Bank, a government-owned development financial institution (DFI) with a special focus on cross-border trade financing; Maybank Islamic, a leading Islamic bank offering sophisticated trade finance products; Affin Islamic, recognised as best trade finance bank in 2025; and Bank Islam, a full-fledged Islamic bank with Islamic trade finance offerings. This method enabled a detailed mapping of LC-i structures as applied in practice within the Malaysian Islamic banking system. Through this approach, the study sought to produce important findings that may inform policymakers, practitioners, and

researchers concerned with the development and implementation of Islamic trade finance instruments.

Results and Discussion

EXIM Bank

Export-Import Bank of Malaysia (EXIM Bank) is a government backed development financial institution in Malaysia with a mandate to support Malaysia’s cross-border trade and overseas investments. The Bank plays a specialised role in facilitating export and import activities through trade finance, guarantees, and credit support etc. As part of its developmental mandate, EXIM Bank offers various Islamic trade finance instruments, including LC-i. The table below presents the range of LC-i products offered by EXIM Bank, together with a brief description of their operational mechanisms and the Shari’ah contracts employed in structuring these instruments (*Table 1*).

Table 1. *EXIM Bank’s LC-i offerings, mechanisms, and Shari’ah contracts.*

Product	Shariah Contract	Mechanism
Letter of Credit-i	Wakalah (“Agency”) If only trade settlement is needed/Murabahah (“Cost-Plus”) If financing is included	Issued at the request of importer to pay the exporter. The bank purchases the goods from exporter and consequently sells it to the importer on cost-plus basis. In case, customer doesn’t need financing, the bank will use Wakalah contract. The customer will be needed to place 100% of the amount with the bank.
Letter of Credit Advising-i	Wakalah bil Ujrah (Agency with fees)	The bank advises the LC received from the issuing bank and notifies and authenticates it for the customer. The bank acts as an agent and charges an agency fee
Letter of Credit Collection-i	Wakalah (Agency)	The bank handles export documents on behalf of the customer and presents them to the issuing bank for payment or acceptance. The bank charges either a commission or a flat fee for this service.
Letter of Credit Confirmed-i	Wakalah (Agency)	The bank adds its confirmation to the LC issued by the importer’s bank. Confirmation constitutes undertaking from bank to make payment upon the presentation of compliant documents. The bank acts as an agent of the issuing bank and charges a fee (ujrah) for the confirmation service.
Back-to-Back Letter of Credit-i	Wakalah bil Ujrah (Agency with fees)	Issued using master LC from importer’s bank. Help the applicant to procure shariah compliant goods from ultimate supplier. Bank as an agent (wakil) of applicant perform the task and charges the fees to the customer.
Letter of Credit Transfer-i	Wakalah bil Ujrah (Agency with fees)	Allows the first beneficiary to transfer all or part of the LC amount to another supplier (second beneficiary). The bank acts as an agent and charges a fee for the service.
Standby Letter of Credit-i	Kafalah (guarantee)	Payment guarantee issued by the bank on behalf of the customer if the customer fails to meet its obligation to beneficiary. The bank acts as a guarantor by assuming responsibility for the customer’s specified liability.

Source: EXIM Bank Malaysia (2026).

As evident from the table above, EXIM Bank offers a wide range of LC-i products. These products are specifically structured to cover key dimension of trade finance and address diverse needs of the customers. For instance, in its standard LC-i offering, the bank uses two different contracts based on the customer’s liquidity needs. If a customer is a cash rich and approaches the bank only for trade settlement without requiring financing, the bank uses Wakalah (Agency) contract, where bank acts solely as a payment agent. However, if the customer requires financing, the structure adopts Murabahah (Cost-Plus) contract, where the bank purchases the goods from exporter and subsequently sells them to the customer at a marked-up price, allowing the customer to

pay at a later date. Further, the table shows that the bank has structured a wide range of LC services in a Shari'ah-compliant manner, including advising, collection, confirmation, transfer, back-to-back, and standby LC facilities. Agency-based contracts, namely Wakalah and Wakalah bil Ujah, predominates these structures as the bank act as an agent and charges the fees for the services rendered. In Standby LC-i (SBLC-i), where the product is based on guarantee, the bank applies Kafalah contract. The bank offers SBLC-i in two forms. A financial SBLC-i where the bank provides financial safety to the customer to ensure smooth operation of the business and enhance creditworthiness of the customer. In contrast, a non-financial SBLC-i enhances the customer's credibility with relevant stakeholders by providing assurance that contractual obligations will be fulfilled.

Maybank Islamic

Maybank Islamic Berhad is one of the largest Islamic banks in Malaysia and a key subsidiary of the Maybank Group. The bank plays a significant role in facilitating domestic and cross-border trade through a wide range of Islamic trade finance products. Similar to EXIM bank, Maybank Islamic also offers a wide range of LC-i products. The table below presents LC-i products offered by Maybank Islamic, together with a brief description of their mechanisms and the Shari'ah contracts employed (*Table 2*).

Table 2. *Maybank Islamic's LC-i offerings, mechanisms, and Shari'ah contracts.*

Product Name	Shariah Contract	Mechanism
letter of Credit-i (LC-i)	Wakalah ("Agency") If only trade settlement is needed/ Murabahah ("Cost-Plus") If financing is included	Issued at the request of importer to pay the exporter. Where financing is required, the bank purchases the goods from the exporter and subsequently sells them to the importer on a cost-plus basis. In case, customer doesn't need financing, the bank will use Wakalah contract. The customer will be needed to place 100% of the amount with the bank.
Inward Letter of Credit-i (ILC-i)	Wakalah (Agency)	The bank authenticates the LC received from the issuing bank and advises to the exporter (customer). The bank act as agent to the customer to advise and charges the fee.
Confirmed Letter of Credit-i (CLC-i)	Wakalah (Agency)	Confirmation is added by the bank to the LC received by the exporter/beneficiary. Mitigates The Risk of non-payment from the Issuing Bank. The bank acts as an agent on behalf of the issuing bank to add confirmation to the LC and subsequently charge the fee to the customer for the service.
Transferable Letter of Credit-i (TLC-i)	Wakalah (Agency)	Allows the first beneficiary of the LC to transfer either partial or full of the credit to another party (second beneficiary) after approval from the issuing bank. The bank act as agent to customer (first beneficiary) to transfer the LC to the second beneficiary
Standby Letter of Credit-I (SBLC-i)	Kafalah Bi Ujah (Guarantee with Fee)	Guarantee by bank of payment if customer (applicant) fails to honour the commitment to beneficiary. The bank charges a fee to the customer for guarantee.

Source: Maybank Islamic (2026).

The table shows wide range of LC-i products offered by Maybank Islamic to address key trade finance functions, including import settlement, advising, confirmation, transferability, and guarantee-based arrangements. Overall, the LC-i offerings of Maybank Islamic are largely similar to EXIM Bank offerings. In its standard LC-i structure, Maybank Islamic similarly employs two types of contracts, where Wakalah is used for cash-backed transactions involving trade settlement, while Murabahah is employed where financing is required. Under the Murabahah structure, the bank

initially purchases the goods from the exporter and subsequently sells them to the importer on a cost-plus basis to be paid at later date. Similar to EXIM bank, Agency-based structures are dominant in service-based LC-i, including advising, confirmation, and transferable LC-i, where the bank acts as an agent and charges a fee for its services. For guarantee-based SBLC-i, the bank uses Kafālah bi al-Ujrah, under which the bank assumes the customer’s liability in return for a fee. However, unlike EXIM Bank, Maybank Islamic does not offer Back-to-Back LC-i or LC-i for collection. In addition, while EXIM Bank explicitly distinguishes between financial and non-financial SBLC-i, such differentiation is not evident in Maybank Islamic’s SBLC-i offerings.

Affin Islamic

Affin Islamic Bank Berhad is an Islamic banking subsidiary of the Affin Bank Berhad that offers a diverse range of Sharī’ah-compliant products and services, including trade finance. The bank provides Islamic trade finance facilities to support both domestic and cross-border activities, including LC-i. Affin bank was recognised as the Best Trade Finance Bank and Fastest Growing Trade Finance Bank in Malaysia at the Global Banking & Finance Awards in 2025. The table below presents the LC-i products offered by Affin Islamic, together with a brief description of their operational mechanisms and the Sharī’ah contracts employed (*Table 3*).

Table 3. *Affin Islamic’s LC-i offerings, mechanisms, and Sharī’ah contracts.*

Product Name	Shariah Contract	Mechanism
Letter of Credit-i (LC-i)	Wakalah (“Agency”)/Murabahah (“Cost-Plus”)	Issued at the request of importer to pay the exporter at sight or at the future date. Murābahah LC-i (MLC-i): can be used with or without financing. Upon payment, the customer may opt for financing under Trust Receipt-i (TR-i) or Accepted Bills-i (AB-i), or alternatively use its own funds to settle the payment. Wakālah LC-i (WLC-i): fully cash-backed LC issued without financing, where payment is set off against the customer’s deposit.
Express Letter of Credit-i (Express LC-i)	Wakalah (“Agency”)/Murabahah (“Cost-Plus”)	Designed to expedite the issuance of LC-i with no requirement of any prior facility. Issued in exchange of Cash or Term Deposit-i / Fixed Deposit (TD-i/FD).
Inward Letter of Credit-i (ILC-i)	Wakalah bil Ujrah (Agency with fees).	The bank authenticates the LC received from the issuing bank and advises to the exporter (customer). The bank act as agent to the customer to advise and charges the fee. Confirmation can be added to LC-i upon the request from the customer.

Source: Affin Islamic (2026).

The table above indicates that Affin Islamic offers a more focused range of LC-i products compared to the other banks examined. However, a distinct approach can be observed in Affin Islamic’s LC-i offerings. For instance, Express LC-i is unique among the studied banks as it is specifically designed to expedite and simply the LC-i issuance process. For this LC-i, the applicant doesn’t need any pre-approved LC-i facility to open the LC-i. Rather, this LC-i issued and “secured against 100% cash payment or Term Deposit (TD-i)/Fixed Deposit (FD) plus variance/tolerance (if any)”. However, this facility is only offered to the existing “financing customer or non-financing who maintain Current Account/-i (CA/-i) or Foreign Current Account/-i (FCA/-i) with the Bank.” Further, it was observed that dedicated LC-i for confirmation is not offered by Affin Islamic like other studied banks. However, confirmation can be provided by the bank in Inward Letter of Credit-i (ILC-i) upon the request from the customer. Similarly, in its standard LC-i, EXIM Bank specifically applies Wakālah where financing is not

required by the customer and Murābahah where financing is needed. In contrast, while Affin Islamic also applies Wakālah for non-financing transactions, it offers Murābahah-based LC-i not only where financing is needed but also in situations where the customer does not require financing. Under the Murābahah LC-i (MLC-i), upon payment for the goods, the customer may choose to obtain financing through other facilities such as Trust Receipt-i (TR-i) or Accepted Bills-i (AB-i), or alternatively use its own funds to settle the payment where financing is not required.

The findings reveal that Malaysian Islamic financial institutions (IFIs) provide sophisticated and diversified range of LC-i products and services employing suitable Shariah contracts. It highlights functional similarities between LC-i offered by Malaysian Islamic banks and their conventional counterparts. LC-i structures adopted by examined banks primarily designed to replicate the economic functions of conventional LCs such as trade settlement, risk mitigation, intermediation, and guarantees, through the use of Shari'ah contracts that correspond to the underlying commercial roles assumed by the bank. In standard LC-i, it was observed that if a customer provides full cash (100% deposit), the banks utilise the Wakalah (Agency) contract. In this scenario, the bank acts merely as a payment agent and settle the trade using the customer's own funds. Conversely, if a customer require financing, the bank adopts Murabahah (Cost-Plus) contract, where the bank purchases the goods and sells them to the customer at a markup for deferred payment. This variation demonstrates the operational flexibility of LC-i structures in accommodating both sight and usance transactions. By applying Wakālah to sight settlements and Murābahah to usance, Malaysian Islamic banks are able to serve both cash-rich clients and those requiring credit facilities. Further, it is observed that Malaysian IFIs offer sophisticated and advanced LC-i structures, including advising, transfer, back-to-back and confirmation services. These structures are predominantly structured under Wakālah bil Ujah (agency with fee) contracts. Notably, even in the case of confirmation, where a second bank provides payment guarantee if the issuing bank defaults, the data from EXIM Bank and Maybank Islamic indicates that Malaysian IFIs structure such LC-i under Wakālah, framing confirmation as an agency service performed on behalf of the issuing bank in exchange for a fee, rather than as a standalone guarantee contract. However, in Standby Letter of Credit-i (SBLC-i), which specifically function as a guarantee in the event of non-performance, the IFIs utilizes the Kafalah (Guarantee) contract. The study also highlights differences in in the LC-i offerings by the banks. EXIM Bank, as a DFI with a trade-specific mandate, offers the comprehensive range of LC-i products. In contrast, Affin Islamic tends to focus on demand and profitability. Specifically, Affin Islamic "Express Letter of Credit-i" provides an efficient model that may serve as a practical alternative for IFIs globally, particularly those seeking to streamline LC-i issuance without requiring pre-approved credit facilities.

Conclusion

This study has systematically analysed the LC-i structures offered by three Malaysian banks and critically examined the Shari'ah contracts utilised in offering these structures. The study found that Malaysian IFIs demonstrate high level of maturity in structuring LC-i to accommodate diverse needs of customers. This has been achieved by adopting suitable Shariah contracts according to commercial functions of the corresponding LC-i. For emerging Islamic finance jurisdictions, this study offers key

practical insights for regulators and Islamic financial institutions to develop or enhance LC-i offerings within their respective markets. While this study systematically analysed LC-i structures in Malaysia, it is subject to certain limitations. First, the research relies primarily on secondary data derived from product disclosure sheets (PDS) and official websites of the selected banks. While these documents provide the formal Sharī'ah structures and mechanisms, they may not fully capture the operational nuances or private variations that occur during the actual execution of complex trade transactions. Second, the scope of the study is limited to three selected institutions—EXIM Bank, Maybank Islamic, and Affin Islamic. While these banks represent different segments of the market (DFI, commercial bank), a broader sample size including more Islamic financial institutions would provide a more comprehensive representation of the entire Malaysian banking system. Future research should aim to bridge these gaps by incorporating primary data through interviews with the practitioners. This would offer deeper insights into the subject matter. Finally, comparative studies could be conducted to assess the feasibility of adopting such structures in other jurisdictions.

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Conflict of interest

The authors confirm that there is no conflict of interest involve with any parties in this research study.

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