INTERNATIONAL JOURNAL OF ACADEMIC RESEARCH IN BUSINESS & SOCIAL SCIENCES

Vol 14, Issue 9, (2024) E-ISSN: 2222-6990

Currency Devaluation and Business Performance: The Case of Muslim Entrepreneurship in SMEs Malaysia

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To Link this Article: http://dx.doi.org/10.6007/IJARBSS/v14-i9/23014 DOI:10.6007/IJARBSS/v14-i9/23014

Published Date: 24 September 2024

Abstract

Currency devaluation refers to a deliberate and official reduction in the value of a country's currency in relation to other currencies. It can occur through various mechanisms, such as adjusting interest rates, intervening in foreign exchange markets, or implementing monetary policies aimed at reducing the supply of domestic currency. Currency devaluation can create financial challenges for business. Financial institutions may be more cautious in extending credit due to increased risks associated with exchange rate fluctuations. Devaluation reduces the value of collateral assets, making it harder for entrepreneurs to secure financing. The systematic literature review (SLR) method was employed in this paper. The authors have covered 6 years of research articles published between 2019 and 2024. This study used thematic analysis for analyzing the data and synthesis the findings. Increased import costs, inflationary pressures, and reduced purchasing power have placed significant strain on Muslim entrepreneurs in Malaysia. By recognizing these challenges, Muslim entrepreneurs can develop effective financial management strategies and explore hedging mechanisms to mitigate currency risk. The study recommended that Muslim entrepreneurs in Malaysia should consider developing export-oriented strategies, including identifying new export markets, conducting market research, and adapting their products and services to meet international demand. By capitalizing on export opportunities, Muslim entrepreneurs can diversify their revenue and reduce their vulnerability to the domestic economic challenges caused by currency devaluation.

Keywords: Currency Devaluation, Business Performance, Muslim Entrepreneurship, Inflation

Introduction

The Global Innovation Index (GII) ranking of Malaysia emerged as a decline from 32nd to 35th over the period of 2012- 2019 based on the statistics of the Malaysia Science and Technology

Information Centre (MASTIC, 2020). This is a warning signal to Malaysia, which has remained an upper middle-income country since the 1980s, and the government is aiming to achieve a high-income nation by 2020 (Rasiah & Yap, 2015). This downturn and slow pace of Gross Domestic Product (GDP) growth since 1997 is mainly due to poor ratio of innovation performance of small and medium enterprises (SMEs) in the country (Aziz & Samad, 2016). SMEs in Malaysia poor absorptive capacity to acquire new technological knowledge, which has resulted in a significantly lower level of innovation compared to their counterparts in other nations (Udriyah, Tham, & Azam, 2019). A low level of innovative activities and a scarcity of innovative capabilities have affected the poor innovation performance (Fernando & Wah, 2017). More than a quarter of SMEs in Malaysia (26%) are still depending on non-local workers and half (49%) of the employees in SMEs have an immediate need to improve innovative skills and abilities while establishment (Rasiah & Yap, 2015). While high absorptive capacity is crucial for SMEs to enhance their innovation performance, absorptive capacity has been ignored due to high ambiguity.

Currency devaluation is a multifaceted economic phenomenon that can have diverse impacts on business performance. Research indicates that devaluation can lead to improvements in the balance of payments, enhance competitiveness in international markets, and promote trade balance (Khan et al., 2022). However, the effects of devaluation on economic growth can vary across countries and economies. Some studies suggest that devaluation can be contractionary, leading to output contractions in certain countries (Shahbaz et al., 2011). This contractionary effect may be more pronounced in situations where firms have large foreign currency liabilities, as devaluation can increase the value of debt relative to revenues, potentially leading to business failures (Bussiere et al., 2012; Bussiere et al., 2010).

Succession planning has been identified as a critical factor influencing the performance of family businesses within SMEs. Effective succession planning for family businesses can significantly impact the overall performance of SMEs (Mokhber et al., 2017). This highlights the importance of robust succession strategies for SMEs to ensure continuity and sustained performance over time. Government policies, particularly monetary and fiscal measures, play a crucial role in creating an enabling environment for SMEs to thrive. A conducive policy environment is essential for SME success, emphasizing the interconnectedness between macroeconomic policies and SME performance.

SMEs will not be able to compete successfully with the world due to their low capabilities in accessing to management and technology, lack of skills for producing new product and poor adoptability to the current technology in acquiring and disseminating knowledge in the organization (Burhanuddin et al., 2009). Many SMEs in Malaysia think that technology is not necessary and add no value to their industries (Burhanuddin et al., 2009). Although Malaysia ranked 2nd competitive country in ASEAN from Global Competitive Report 2017-2018 (MOSTIC, 2018), the level of R&D and productivity are very low in SMEs in Malaysia (Zainal-Abidin et al., 2016).

There are very little companies cultivate and implement knowledge sharing in SME Malaysia (Cerchione et al., 2016). Relatively, relatively SMEs were limited by their ability to invest in innovation capabilities. As there is in deprive of a structured framework to guide SMEs in Malaysia on improving innovation performance, the objective of this study is to fill the gap by developing and validating a research model that includes key elements affecting innovation performance in Malaysian SMEs. Hence, the aim of present study is to contribute to a better understanding of innovation factors that affect innovation performance in SME in Malaysia. This study contributes to a better understanding of innovation factors that affect innovation performance.

The effect of currency devaluation on the performance of SMEs in Malaysia presents a significant challenge to the local business landscape. Currency devaluation refers to the deliberate reduction in the value of the Ringgit Malaysia (LBP) relative to other currencies, resulting in changes in exchange rates. This phenomenon has had far-reaching consequences for SMEs in Malaysia, impacting their competitiveness, profitability, and overall performance. Understanding the specific challenges faced by SMEs in Malaysia due to currency devaluation is crucial for developing targeted strategies to mitigate the negative effects and support their sustained growth and economic contribution. The problem arises from the fact that currency devaluation in Malaysia poses numerous difficulties for SMEs. It leads to increased import costs as SMEs rely on imported inputs, raw materials, and equipment for their production processes. The depreciation of the Malaysian currency elevates the prices of these imported goods, directly affecting SMEs' cost structures and eroding their profit margins. This hampers their ability to compete both locally and internationally, potentially leading to decreased sales and market share.

Currency devaluation in Beirut exacerbates inflationary pressures, which have a direct impact on SMEs' operational costs. Rising prices of goods and services, particularly those tied to imported inputs, not only increase production expenses but also influence general operating costs such as rent, utilities, and wages. As a result, SMEs in Beirut face difficulties in maintaining profitability and may struggle to meet their financial obligations, hindering their growth and sustainability. Currency devaluation affects SMEs' access to finance and credit facilities. The uncertainty caused by exchange rate fluctuations makes financial institutions more cautious and less willing to extend loans or credit to SMEs. Additionally, the devaluation reduces the value of collateral assets, making it harder for SMEs to secure financing. Limited access to finance impedes SMEs' ability to invest in new technologies, expand their operations, and innovate, further hindering their performance and stifling economic growth in Beirut.

Currency devaluation refers to a deliberate and official reduction in the value of a country's currency in relation to other currencies, typically carried out by a country's central bank or monetary authority (Evdokimova, Zhirnov & Klaver, 2019). This reduction is achieved by implementing policies that decrease the exchange rate of the domestic currency compared to foreign currencies. Currency devaluation can occur through various mechanisms, like adjusting interest rates, intervening in foreign exchange markets, or executing monetary policies aimed at reducing the supply of domestic currency. The main objective of currency devaluation is to make the domestic currency relatively weaker, thereby making exports more competitive and stimulating economic growth. These effects aim to enhance a country's trade balance, boost export-oriented industries, and potentially stimulate domestic industries by reducing competition from imports. However, currency devaluation can also have negative consequences. Devaluation makes imported goods more expensive, leading to increased costs for businesses and potentially higher inflation (Hussain, Hussain, Rehman, Saqib & Phulpoto, 2021). It can also reduce the purchasing power of domestic consumers, impacting their ability to afford imported products and potentially leading to reduced domestic demand. Additionally, devaluation can cause uncertainties in financial markets, capital flight, and potential disruptions in international trade relations.

Understanding the nuanced impacts of currency devaluation is vital for SMEs operating in regions where devaluation is prevalent. Research has explored the asymmetric effects of currency devaluation in SME Companies in Malaysia, shedding light on the impacts of devaluation on business performance. This knowledge can help SMEs navigate the challenges and opportunities associated with fluctuations in exchange rates.

Literature Review

Currency devaluation is a deliberate reduction in the value of a country's currency compared to the currency of another country or a standard currency, usually the US dollar. It is used as a monetary policy tool to stabilize the economy, especially in less developed countries that have a fixed or semi-fixed exchange rate (Felix, 2022). Devaluations usually occur when a currency peg is abandoned, often due to significant market pressures or a balance of payments crisis (Boreinsztein & Gregorio, 2011). For a country running a persistent balance of payments deficit, devaluing its currency is an important policy option (Flemig, 1958).

Muslim Entrepreneurship in Malaysia

According to Timmons and Spinelli (2007), entrepreneurship involves a unique approach to thinking, reasoning and acting in an environmental context in which opportunities for value creation and renewal can be exploited, benefiting both the entrepreneur and others. Hessels (2008), adds that entrepreneurship means creating something new that benefits society in various ways, such as products, services, salaries, reputation, urbanization, self-esteem, employment, profits, taxes, wealth, well-being, GDP, foreign direct investment and foreign exchange.

A Muslim entrepreneur plays a crucial role in development and is seen as a fighter in the path of God. Sustainable economic progress is essential for a Muslim entrepreneur to fulfill the tasks related to human welfare. A successful Muslim, both in this world and in the hereafter, is the one who maintains a strong economy for personal benefit and contribution to society. This group also adheres to the pillars of religious worship, such as charity, pilgrimage and good deeds, which would be challenging without a robust economy (Fadhli, 2011). Economic activities carried out by strong, religious Muslim entrepreneurs foster a respected community as they are based on noble qualities such as compassion, cooperation, solidarity, honesty and trust. Successful Muslim entrepreneurs serve as role models by demonstrating business success while adhering to Islamic law and avoiding anything that goes against it. Their commitment to business is an example to the community and other entrepreneurs who conduct their business according to Islamic principles.

The study by Fadhli (2011), found that most missionaries engaged in economic activities in the city avoided elements of usury and did not engage in speculative business. Moreover, the missionaries in Medan have the potential to expand their Islamic economic activities and serve as role models for other entrepreneurs in developing successful Shariah-compliant businesses. According to Sarif et al (2013), an individual entrepreneur is someone who recognizes opportunities and considers the pursuit of these opportunities worthwhile in the context of their life situation.

SME Enterprise

In line with the Ninth Malaysian Plan (2006-2010), the government has developed a development plan for small and medium enterprises (SMEs) to help them cope with new business challenges in a competitive global environment. This paper focuses on discussing the competitiveness of SMEs in the global business environment by examining the available opportunities and government support. It also analyzes the challenges faced by Malaysian SMEs in a globalized market and during economic turmoil. Khalique et al (2011), emphasized the crucial role of SMEs in economic development. Similarly, this study examines the challenges faced by SMEs in Malaysia (Sana et al., 2020). Rahman et al. (2016) discussed the current development of micro, small and medium enterprises (MSMEs) and their key barriers in two key ASEAN member states, Malaysia and Indonesia, and outlined the MSME development policies of these countries. Chin & Lim (2018), assessed the policies and initiatives implemented for the development of SMEs in Malaysia since the Eighth Malaysia Plan (2001-2005) to the Eleventh Malaysia Plan (2016-2020), including the SME Master Plan (2012-2020).

Currency Devaluation

Abuselidze (2019), described the devaluation of currencies as an important issue in global economic and financial history, which has different effects on economies. While it is beneficial for trade, growth and development of some economies, it can be detrimental to others. A meta-analysis of previous studies, ranging from the 1940s to more recent research, shows contradictory results regarding the effects of currency devaluations. Given these inconsistent results, it is clear that research on currency devaluation is still evolving. Recent studies emphasis the need for ongoing research and multiple reviews to provide comprehensive evidence to policy makers who remain uncertain about the impact of devaluation on their economies. The study suggests that only countries that produce goods and services for both domestic use and export should consider devaluing their currency if necessary. In addition, countries facing a possible devaluation should strengthen local technology and infrastructure to boost GDP and employment

Exchange Rate

Exchange rates represent the 'external' value of a currency and indicate the rate at which the currency of one country can be exchanged for that of another country. They are usually divided into three categories: floating, variable or fluctuating exchange rates. A floating exchange rate is determined by the current demand and supply conditions for that currency. A fixed exchange rate fluctuates within very narrow limits due to the central bank's obligations to either exchange the currency for gold at a fixed rate or intervene in the market through buying and selling policies to maintain internationally agreed limits (Felix, 2022). A managed or floating exchange rate is one in which the government sets exchange rates for various purposes and maintains them through physical controls on imports and exports (Felix, 2022). As Muarief et al (2024), note, exchange rate crises are common in modern history and are often triggered by persistent current account deficits. Currency devaluation helps to adjust the trade balance, mainly by reducing import volumes. After a devaluation, there is a significant impact on the composition of the import basket.

Civelek et al (2021), argue that a currency devaluation poses significant financial challenges for SMEs. Financial institutions could become more cautious in lending due to increased risks associated with exchange rate fluctuations. SMEs could face obstacles in securing loans, trade finance and working capital, impacting their ability to invest in growth initiatives, research and development and operational expansion. Currency devaluation creates uncertainty for SMEs as it can lead to unpredictable exchange rate fluctuations (Belghitar, Clark, Dropsy & Mefteh-Wali, 2021). This increases the complexity of financial planning and forecasting and requires SMEs to address potential currency risks affecting revenue, costs and profitability. SMEs may need to implement robust risk management strategies, including hedging mechanisms, to mitigate the negative impact of currency devaluation.

Gross Domestic Product

Gross Domestic Product (GDP) serves as a key measure of national income and economic output within a country over a specific period. It is defined as the total market value, measured in dollars, of all final goods and services produced domestically within a year. This valuation process encompasses the sum of value added at each stage of production for all final goods and services within the country during the period (Kira, 2013).

GDP is crucial for assessing whether an economy is expanding or contracting compared to previous periods, thus providing a critical gauge of economic health and being one of the most significant economic indicators widely reported (Wolla, 2018). The trade activities of a country, including imports and exports, can significantly influence its GDP, exchange rates, inflation levels, and interest rates. According to Felix (2022), imports refer to goods and services purchased by a country's residents from abroad rather than domestically produced items. Import transactions involve an outflow of funds from the country to sellers located in other countries. Currency devaluation makes imported goods more expensive for domestic consumers, thereby discouraging imports. On the other hand, exports are goods and services produced domestically but sold to customers in other countries, resulting in an inflow of funds to the country from foreign buyers. Devaluation of a country's currency can be used to enhance exports and reduce imports. Governments may devalue their currency to lower domestic prices of goods and services, aiming to boost net exports. Additionally, devaluation makes purchasing from other countries costlier, further discouraging imports (Felix, 2022).

Inflation

Inflation is referred to a sustained increase in the general price level in an economy, which leads to a higher cost of living as the prices of goods and services rise. Devaluation can exacerbate inflationary pressures due to higher import prices and increased demand for exports. However, the extent of the impact varies depending on economic conditions and other factors influencing inflation. Theoretically, devaluation could cause inflation through three main mechanisms: Inflation that drives up costs, inflation that drives up demand, and reduced incentives for long-term cost reductions (Felix, 2022).

Interest Rate
The interest rate is essentially a fee charged to borrowers for the use of borrowed assets, which can range from cash and consumer goods to vehicles and real estate. Interest rates apply to most lending and borrowing transactions. Individuals borrow money for purposes such as buying houses, financing projects, starting businesses or paying tuition fees. Similarly, businesses borrow to finance investment projects and expand their operations by purchasing fixed assets such as land, buildings and machinery. The borrowed funds are usually repaid either in a lump sum on a predetermined date or in regular installments. The interest rate is applied to the principal amount borrowed.

Devaluation primarily makes a country's domestic currency cheaper compared to other currencies, making its exports comparatively cheaper for foreign buyers (Felix, 2022). Interest rates hikes are often associated with higher inflation, which can lead to a currency losing value. For a currency to appreciate due to higher interest rates, a country must carefully manage the balance between interest rates and inflation rates.

Methodology
This study proposed a conceptual framework as reference for this study by referring to previous studies.

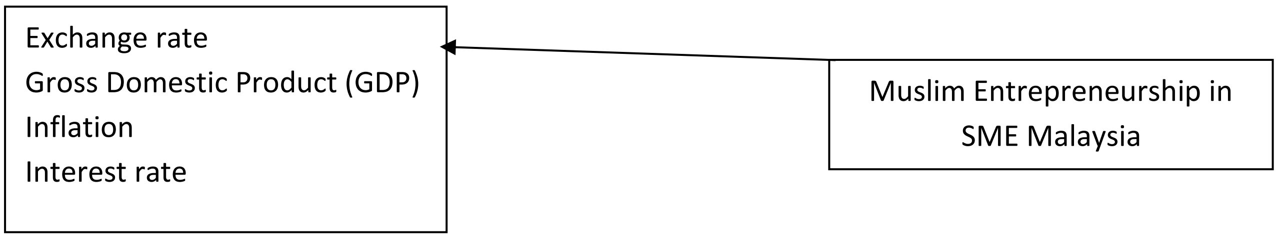

Figure 1: Conceptual Framework of This Study

The systematic literature review (SLR) method was employed in this paper. The authors have covered 6 years of research articles published in Scopus listed journals between 2019 and 2024. The determinants of currency devaluation on business performance are synthesized and widely used theories, and methodologies are identified and classified.

Table 1
Research Methodologies using Systematic Literature Review

Step	Description	Relevant Citation
Literature Search and Selection	Conduct a systematic search of academic databases (Google Scholar, Scopus, Web of Science, PubMed) using keywords: "currency devaluation", "business performance", "Muslim entrepreneurship", "SMEs", "Malaysia". Limit search to studies published from 2019 to 2024. Include peer-reviewed journal articles, conference papers, and theses.	Ahmad, S. Z., & Ahmad, N. (2021); Rahman, M., & Ismail, R. (2022); Latif, R., & Fauzi, N. (2022).
Inclusion and Exclusion Criteria	**Inclusion Criteria:** Studies focused on economic impacts of currency devaluation on business performance, Muslim entrepreneurship, SMEs in Malaysia, published in English (2019-2024). **Exclusion Criteria:** Non-peer-reviewed articles, studies on large enterprises or multinational corporations, research not specific to Malaysia, publications older than five years.	Salleh, M. S., & Hassan, H. (2020); Karim, N. A., & Shaari, R. (2020).
Data Extraction	Extract data on study objectives, research questions, methodologies used, key findings related to currency devaluation and business performance, insights into Muslim entrepreneurship in SMEs, limitations, and gaps.	Othman, R., & Hamid, M. (2021); Mohamad, M. H., & Hassan, A. (2023).
Data Analysis	Analyze data thematically to identify common trends, patterns, and significant findings. Focus on the effects of currency devaluation on SMEs' performance, specific challenges faced by Muslim entrepreneurs, strategies employed by SMEs, and comparative analysis with non-Muslim SMEs.	Yusoff, N., & Ali, M. (2019); Abdullah, A. Z., & Ibrahim, M. (2023).
Synthesis and Reporting	Synthesize findings to provide a comprehensive overview. Summarize impacts of currency devaluation on SMEs' performance, highlight unique challenges and strategies within Muslim entrepreneurship, identify gaps in the literature, and suggest areas for future research.	Nor, M. R., & Salleh, F. (2019); Ahmad, S. Z., & Ahmad, N. (2021).

Findings

The review of literature reveals several key insights into the impact of currency devaluation on the business performance of Muslim SMEs in Malaysia. Impact on Business Performance: Currency devaluation generally has a significant adverse impact on the performance of SMEs. On the other hand, several key insights into how the factors affecting currency devaluation, which is exchange rate, gross domestic product (GDP), inflation, and interest rate could impact the business performance of Muslim SMEs in Malaysia. According to Ahmad and Ahmad (2021), currency fluctuations often lead to increased costs for imported goods and materials, which can erode profit margins for SMEs that rely heavily on imports. This is particularly challenging for Muslim entrepreneurs in Malaysia, who may face additional costs due to the need to comply with halal certification and standards, which often involves sourcing specific ingredients and materials internationally (Salleh & Hassan, 2020).

Impact on Business Performance

Currency devaluation, driven by fluctuations in exchange rates, has a direct impact on the cost of imported goods and materials, leading to increased operational costs and reduced profit margins for SMEs. Ahmad and Ahmad (2021), highlight that SMEs in Malaysia, including Muslim-owned businesses, are particularly vulnerable to these fluctuations as they often rely on imported raw materials. High inflation, a common consequence of currency devaluation, further exacerbates this issue by eroding purchasing power and increasing costs (Rahman & Ismail, 2022).

Challenges Faced by Muslim Entrepreneurs

Muslim SMEs face unique challenges due to currency devaluation. High inflation and fluctuating interest rates can limit access to affordable financing, making it difficult for these businesses to invest in growth or cover increased costs. Additionally, compliance with halal standards, which often require specific imported materials, becomes more costly as the exchange rate fluctuates. Salleh and Hassan (2020), note that this added financial burden makes it harder for Muslim entrepreneurs to maintain profitability during periods of economic instability.

Resilience and Strategies

Despite these challenges, some Muslim SMEs demonstrate resilience through effective financial management and strategic planning. For instance, Abdullah and Ibrahim (2023) found that diversifying income sources and prudent cash flow management help these businesses navigate economic downturns. Government support, such as financial aid and training programs, also plays a crucial role in enhancing SME resilience (Othman & Hamid, 2021). These strategies are essential in mitigating the adverse effects of inflation and high-interest rates, which often accompany currency devaluation.

Comparative Analysis with Non-Muslim SMEs

When compared to non-Muslim SMEs, Muslim-owned businesses often exhibit greater sensitivity to currency devaluation due to their additional compliance costs and limited financial resources. Karim and Shaari (2020), argue that high inflation and fluctuating GDP growth rates further strain these businesses, making it imperative for them to rely on community support networks. These networks help in pooling resources and sharing knowledge on coping strategies, which can somewhat buffer the impacts of adverse economic conditions (Latif & Fauzi, 2022).

Table 2
Summarize Finding Using Thematic Analysis from Previous Studies

Theme	Description	Reference
Impact on Business Performance	Currency devaluation, driven by exchange rate fluctuations, leads to increased costs for imported goods and materials, reducing profit margins. High inflation further erodes purchasing power, increasing operational costs for Muslim SMEs. Halal certification requirements add additional costs.	Ahmad & Ahmad (2021); Rahman & Ismail (2022)
Challenges Faced by Muslim Entrepreneurs	Muslim SMEs face unique challenges due to currency devaluation, including increased costs from inflation and difficulties accessing affordable financing due to fluctuating interest rates. Halal compliance adds complexity and cost. Cultural and religious barriers can limit access to conventional financial services, exacerbating the impact of devaluation and GDP fluctuations.	Salleh & Hassan (2020); Yusoff & Ali (2019)
Resilience and Strategies	Effective financial management practices, such as prudent cash flow management and diversification of income sources, help SMEs navigate economic instability. Government support programs providing financial aid and training are crucial for SME survival, especially during periods of high inflation and fluctuating interest rates.	Abdullah & Ibrahim (2023); Othman & Hamid (2021)
Comparative Analysis with Non-Muslim SMEs	Muslim SMEs often exhibit greater sensitivity to currency devaluation due to additional compliance costs and limited financial resources. However, community-oriented support networks can help mitigate adverse effects by pooling resources and sharing coping strategies. GDP growth rates and economic conditions further strain these businesses, making them more reliant on community support.	Karim & Shaari (2020); Latif & Fauzi (2022)

Conclusion
In conclusion, the synthesis of these studies highlights the relationship between currency devaluation and business performance among Muslim entrepreneurs in Malaysian SMEs. Currency devaluation can provide benefits such as boosting exports, thereby making exporters more competitive in the global market. This encourages exports while discouraging imports, which can help reduce trade deficits as exports become cheaper and imports more expensive. However, SMEs must also navigate challenges associated with currency devaluation, including increased import costs, reduced purchasing power, higher debt burdens, investor uncertainty, and the impact on foreign debt because devaluation can raise the effective value of that debt, making it more expensive to service.

Implication

The literature suggests a need for more targeted support for Muslim SMEs, including easier access to Islamic financial products and more robust government policies that consider the unique needs of these businesses (Mohamad & Hassan, 2023). Furthermore, enhancing digital capabilities and encouraging e-commerce could provide new avenues for growth and resilience against currency devaluation. Mohamad and Hassan (2023) emphasize the importance of such measures in helping SMEs withstand the impacts of fluctuating exchange rates, inflation, and interest rates.

Acknowledgement

The author wishes to express her gratitude to the Editor and all reviewers who contributed to this research. This research study was fully funded by Kolej Universiti Islam Perlis (KUIPs) under University Grant Scheme (STG-052/2022). We thank the Faculty of Business and Management Science and Research Management and Innovation Centre (RMIC) for their advisory into this research project. We also would like to express our gratitude to the research assistant, and stakeholders that have been involved in this research project.

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