

Zakat and SDGs : The Impact of Zakat on Economic Growth, Consumption and Investment in Malaysia

Eko Suprayitno

Universitas Islam Negeri Maulana Malik Ibrahim

Malang, Indonesia

suprayitno@pbs.uin-malang.ac.id

Abstract—This study aims to look at the impact of zakat distribution on macroeconomic in Peninsula Malaysia by using OLS, 2-SLS and ECM analysis. This research is initially undertaken because many economists today believe that zakat does not influence the economy at the macro level because the zakat rate of 2.5 per cent is not significant. This issue has motivated us to conduct this study on the impact of zakat distribution in Malaysia. In Malaysia zakat is recognized as a fiscal tool whereby a rebate is given to income taxpayers who pay zakat. This study finds that zakat has a positive and significant relationship with economic growth, consumption and investment respectively. This means that an increase in the amount of zakat distribution will cause an increase in economic growth, consumption and investment. Lastly, the result of the ECM analysis shows that distribution of zakat have influence significant and positive impacts on economic growth. The long-run elasticity of the zakat variable is positive and significant. Empirical evidence in Malaysia support that zakat can influence economic growth, investment and consumption. Hence the Malaysian model of zakat administration and fiscal instrument can influence the economy at the macro level. Such fiscal policy can be applied in other countries.

Keywords—*Zakat, Economic Growth, Consumption, Investment.*

I. INTRODUCTION

As a socio-economic institution born in the 7th century Zakah is the first fiscal system in the World which has a remarkable completeness of rules, ranging from the subject of zakat payments, the object of zakat property and its respective tariffs, the limit of ownership of minimal property is not exposed to zakat (*Nisab*), the period of ownership of the property (haul), to the allocation of the distribution of the recipient of zakat (*mustahik*). If applied systematically in the economy, especially the rule-based economy and the Compellent Islamic spirit, zakat will also have important and significant economic

characteristics and implications that make it socially cool.

In the scope of the economy, zakat has a broad meaning both macro and micro scale, given the zakat in the realm of Macro Economy can be as a fiscal policy instrument in a country or into the public sphere of Islam, then in the field of micro zakat also can play an essential role in the allocation of zakat or distribution of zakat to the recipient. In Nash Al-Qur'an Surat at-Taubah verse 60 already determine the eligible group to receive zakat funds. One of them is poor, and the needy will get the share of zakat as a process of distributing income more evenly.

In Malaysia, the collection and distribution of zakat are organized by the central organization per state central and Community, either collecting or collecting and distributing. Thus under this system all religious matters are under the jurisdiction of each state in this country. Hence, the administration of *zakat* in Malaysia lies with the respective Islamic council of each state and the federal territories also have their own. Due to that, the quality of services provided by the respective Islamic Council in *zakat* administration is different from one state to the other. The practice of *zakat* is based on the *Shariah* while the taxation practice is based on the Malaysian Income Tax Act, established in 1999.

Many efforts have been done to increase *zakat* collection. These includes the privatization of *zakat* collection centres, increasing transparency in the collection and distribution and widening of the *zakat* base especially on the “unconsensus” wealth. Currently all states have agreed that personal income (for example salary) is subjected to *zakat* except for Perak [1]. And most important is support by the fiscal policy system, whereby the payment of *zakat* can reduce income tax payment. The amount of *zakat* paid is entitled to be claimed as rebates pursuant to Section 6A

(3) of the Income Tax Act 1967. In addition to that, any payment, which is related to Islamic religion due such as *zakat* fitr, is also entitled for rebates under the same section. However, if the amount of *zakat* paid is more than the final tax due, no refund will be granted by the Inland Revenue Board (IRB). This meant that *zakat* paid can reduce tax payment up to 100 percent.

The problem of *zakat* is not only in the collection of *zakat*. The problem of *zakat* distribution. *zakat* is even critical today. In al-Qur'an there is more guidance on the distribution of *zakat* compared with the collection of *zakat*. However, the most important problem that has been solved until now is the implication of the distribution *zakat* to the *asnaf*. Many research just look at the influence of *zakat* on poverty elimination and income distribution. Many economist do not believe that *zakat* have an impact on macroeconomic variables, especially economic growth. The question is how can *zakat* at 2.5 per cent rate influence economic growth? This research will examine how *zakat* distribution can influence macroeconomics, especially economic growth, consumption and investment.

The institution of *zakat* has implications for micro and macro-economic variables. In the former *zakat* is said to result in favorable effects on saving and investment behaviors of individuals without affecting work efforts. Favorable macro-economic effects are expected to cover several dimensions including allocative efficiency, economic growth, distribution of income and wealth, poverty eradication, social security and stabilization [2].

Some writers has opinion that collected and distribution *zakat* will contribute to micro and macroeconomics, such consumption, income distribution, economic growth. etc. See [3][4][5]. *Zakah* has important economic implications such as aggregate consumption, national saving, investment and aggregate production. In the Islamic Economy where *zakat* is applied, the society will be divided into two income groups namely the payer of *zakat* and the recipient of *zakat*. The obligatory group of *zakat* (*Muzakki*) will transfer a certain proportion of their opinion to a group of people receiving *zakat* (*mustahik*). This will obviously make the revenue ready to spend from of facilities and infrastructure for the community, increase productivity, and improve income society in general. If *zakat* is managed with good and trustworthy, it will increase the welfare of the people, increase the

mustahik will increase. Increased incomes will increase consumption and simultaneously allow the *mustahik* to start forming savings over the long term, *zakat* transfers will make income expectations and the level of wealth impossible to increase which in turn makes their consumption even higher.

Zakat will increase consumption, particularly consumption of basic goods and services, and will likely change consumption from the use of luxury goods and services to the consumption of staple goods and services. The distribution of *zakat* to the poor and the needy enables their income to increase. Because of the low level of their wealth and income, it is probable that the income and income (share) of the *zakat* are used for the consumption of essential goods. Vice versa, *zakat* will reduce wealth and income of the rich. With the loss of wealth and income of the rich, it is possible to reduce the consumption of luxury goods and services [6].

Several studies have shown that *zakat* can reduce the poverty gap, income gap and poverty level. Patmawati says that in Selangor, Malaysia found *zakat* succeed in reducing poverty [7], research [8] in Malaysia shows that the *zakah* distributed has an impact on aggregate consumption, but the impact is very small although theoretically states that the tendency of consumption *mustahik* is greater than *muzakki*. The small impact of the distribution of *zakah* on consumption may be caused by use of data on aggregate consumption of Muslims and non-Muslims, while *zakat* which are collected are distributed to meet the needs of Muslims only.

These studies only analyze the effect of *zakat* on consumption directly, whereas *zakat* also has an indirect effect to consumption through income. Productive *Zakah* is distributed in the form of business capital will increase production factor in the form of capital (capital) in the activity a *mustahik* effort so as to increase the output and income *mustahik*. In the end this increase in income will increase household consumption *mustahik*.

That earning productive *zakat* from BAZNAS of Kebumen District shows that productive *zakat* has a significant effect on income, consumption, savings, and infak *mustahik* [9]. *Zakat* can maximize the quality of Human Resources (HR) through the provision ethos work, and become a means of distribution of the economy of society [10].

Furthermore, the consumption of the rich is often the relatively unimportant consumption of goods and services. As income increases,

consumption patterns shift from primary goods and services, which are generally still in harmony with a completely non-primary, utility-based, and utility-based utility that generally leads to a livelier life.

Zakat also has important implications for saving, economic theory postulates that saving is a residue of after consumption, in determining the income allocated for current consumption and how much is saved for future consumption, conventional theory explains in the perspective of positive time preference theory. The current level of consumption and the saving rate will be determined by matching the rate of time preference and rate of interest. In other words, the interest rate will affect the current level of consumption through its relationship with savings [11]; [12]; [13]; [14]; [15]; [16].

In the Islamic perspective, saving is not a residual activity, but a rational action that has a certain positive purpose, not to be stockpiled or used to speculate. Savings for future preparation are allowed even recommended. At the same time Islam prohibits the exaggeration.

In macro terms, the implementation of zakat will have a positive impact on the national saving rate. Since zakat is also imposed on accumulated wealth, not only on income alone, the payment of zakat will encourage muzakki to increase the saving ratio to prevent the level of wealth declining. Meanwhile, as the taxation system of zakat is a friendly tax system to the business world so it is believed will have a positive impact on

aggregate production. Zakat has a low tariff and fixed and never changing because it is set in the Shariah [11]; [12]; [13]; [14]; [15]; [16]; [17]

II. METHOD

A. Sources Data

Data obtained from Statistical Department of Malaysia, Government Financial Statistic, International Financial Statistic (IFS), PPZ (Institution of Zakat Malaysia), Central Bank of Malaysia (BNM), the Economic Planning Unit, and such reports which may be applied as reference.

The data collected is Consumer Prices Index, (CPI) for goods and basic service, the other government revenue, other consumption of government, Small and medium enterprises (SMES), public consumption, Real Production Aggregate, Total government revenue, Prices of Basic need, Individual income, collection and distribution of zakat.

B. The Model.

The model is developed from the link between zakat and other macroeconomics variables such income, consumption and investment. This model is developed from the simple model [18] and [19] with application in Malaysian economic and with the any alteration. The estimation of structural equation is applied a Dynamic Linear Model (MLD) is Partial Adjustment Model (PAM), here in after it is estimation by Simultaneous Equation Model and Error Correction Model (ECM). The Research model is like Table 1.

Table 1. Research Model

1.	$Y_t = a_0 + a_1 Y_{dt} + a_2 C_t + a_3 GE_t + a_5 Zk_t + a_6 Zk_{t-1} + a_5 f_t + \varepsilon 1_t$	Growth Equation	(1)
2.	$C_t = b_0 + b_1 Y_t + b_2 Y_{dt} + b_3 GE_t + b_4 Zk_t + b_5 Zk_{t-1} + b_6 \pi_t + \varepsilon 2_t$	Consumption Equation	(2)
3.	$I_t = c_0 + c_1 Y_{dt} + c_2 Zk_t + c_3 C_t + c_4 Zk_{t-1} + c_5 GE_t + c_6 Y_t + \varepsilon 3_t$	Investment (SMEs) Equation	(3)
4.	$Y = C + I$	Identity Equation	(4)

Endogenous variable:

Y_t	=	Real National Income (1987=100)
C	=	Public Consumption Total
I	=	Small Medium Enterprises Investment (SMEs) Total

Exogenous variable:

Zk	=	Collected Zakat by the Zakat Institution
Y_d	=	Individual Income
GE	=	government expenditure total
π	=	Inflation $\pi_t = (P_t - P_{t-1} / P_{t-1}) * 100$ in percent (%)

$\varepsilon 1_t, \varepsilon 2_t, \varepsilon 3_t$, is error term equation 1 to 3.

III. RESULT AND DISCUSSION

A. Error Correction Models

The error correction model, however, is particularly powerful since it allows an analyst

to estimate both short term and long run effects of explanatory time series variables. The standard way to derive the error correction model is to show that if X and Y are linear

functions of a latent integrated process, the residuals of Y regressed on X should be stationary. This derivation of the error correction model starts with the assumption that both Y and X are integrated and demonstrates that the error correction model captures the equilibrium causal movements between these two cointegrated processes. Occasionally, however, some authors derive the error correction model from a different and more promising starting point [20];[21]; [22]. In this research, the *error correction model* derived by [18]; [19]) with any alteration to Malaysian Economic. The model is :

$$LYr_t = a_0 + a_1LYd_t + a_2LC_t + a_3LGE_t + a_5LZkt_t + a_6LZkt_{t-1} + a_5LI_t + \mu I_t \quad (5)$$

LYd = Log (Yd)

LC = Log (C)

LGE = Log (GE)

LZkt = Log (zkt)

LZkt_{t-1} = Log (Zkt_{t-1})

From the basic model in equation (5), we can obtained the *error correction model* is:

$$DYr_t = \alpha_0 + \alpha_1DLYd_t + \alpha_2DLC_t + \alpha_3DLGE_t + \alpha_4DLZk_t + \alpha_6DLZk_{t-1} + \alpha_6DLI_t + \alpha_7LYd(-1)_t + \alpha_8LC(-1)_t + \alpha_9LGE(-1)_t + \alpha_{10}LZk(-1)_t + \alpha_{11}LZk(-1)_{t-1} + \alpha_{12}I(-1)_t + \alpha_{13}ect(-1) + \alpha_{12}\mu_t$$

(6)

Where:

DLYd_t = LYd_t - LYd_{t-1}

DLC_t = LC_t - LC_{t-1}

DLGE_t = LGE_t - LGE_{t-1}

DLZkt_t = LZk_t - LZk_{t-1}

DLZkt_{t-1} = LZk_{t-1} - LZk_{t-2}

DI_t = LI_t - LI_{t-1}

Ect = LYd_t + LC_t + LGE_t + LZk_t + LZk_{t-1} + LI_t - LY

The long term ECM model is derived by:

$$LYr_t = a_0/a_{13} + (a_7+a_{13})/a_{13}LYd_t + (a_8+a_{13})/a_{13}LC_t + (a_9+a_{13})/a_{13}LGE_t + (a_{10}+a_{13})/a_{13}LZk_t + (a_{11}+a_{13})/a_{13}LZk_{t-1} + (a_{12}+a_{13})/a_{13}LI_t$$

$$LYr_t = \beta_0 + \beta_1LYd_t + \beta_2LC_t + \beta_3LGE_t + \beta_5LZk_t + \beta_6LZk_{t-1} + \beta_5LI_t$$

B. Empirical Implementation of The Model

1. Stationerity Test

The test of stationarity in this research will applies the *Dickey Fuller Unit Root test*. The result of this is test on the variables of the equation can be summarized at Table 8 and 9. From the output analyze can be estimated that estimation of the variables have difference integration. In the table 8 we can explain that the Yr, C, Inv, and Yd is significant at $\alpha = 1$ percent and in level second difference (2nd differences) And in table 9 Zkt is significant at $\alpha = 1$ percent at level first difference, inflation (inf) and GE is significant at $\alpha = 1$ percent and $\alpha = 10$ percent at level second difference. Thus the variables is significant at 2nd difference of test for unit root.

Table 2. The Stationerity test
Yr, C, INV, Yd

Lag	Yr		C		INV		Yd	
	DF	ADF	DF	ADF	DF	ADF	DF	ADF
(-2)	-4.099*	-3.86*	-3.989*	-3.94*	-4.411*	-4.106*	-3.53*	-3.51*
(-1)	1.16	1.10	1.59	1.65	2.559	2.388	1.05	1.21

Source: Output Analyze Data,

* significant at $\alpha = 1$ percent

Table 3. The Stationerity Test
INF, ZKT, GE,

Lag	ZKT		INF		GE	
	DF	ADF	DF	ADF	DF	ADF
(-2)	-5.41*	-5.16*	-4.99*	-4.59*	-2.24***	-2.11***
(-1)	3.02**	2.89**	1.25	1.23	-0.35	-0.33

Source: Output Analyze Data

* significant at $\alpha = 1$ percent.

** significant at $\alpha = 5$ percent.

*** significant at $\alpha = 10$ percent.

2. Error Correction Models Analyze

The Analysis of Error correction model will be done for see the impact of zakat on economic growth in long-term analysis. In this analysis will be studied by the input the of the deviation on a long term and short term dynamics. In this model, short term dynamics is input the *first difference*. And the long term adjustment is done by the input of the *error correction* which appraised.

The result of the ECM on the table 10 shows that the coefficient of *error correction*

term lag one or ECT (-1) in the model is significant. With the significant of the coefficient of ECT (-1) its means that between economic growth, public consumption, small medium enterprises investment, inflation, government expenditure, disposable income, collected zakat and collected zakat years before (the distribution zakat), have co-integration, the correct specification model, the correct theory, and any causality relationships (at least there is any one way relationship), so there is no reason to refuse ECM model.

Table 4. Result the ECM Model

Dependent Variable: DYR
Method: Least Squares
Date: 03/28/08 Time: 10:28
Sample(adjusted): 1992 2006
Included observations: 15 after adjusting endpoints

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	1427.103	604.3429	2.361412	0.0455
DLNC	26.36338	51.83596	0.508593	0.7005
DLNGE	-8.400220	18.10409	-0.463996	0.7234
DLNINV	2.315446	1.181274	1.960126	0.3003
DINF	-2.391657	1.066407	-2.242725	0.0698
DLNZk	0.510860	3.802771	2.328468	0.0487
DLNYd	4.597410	55.00819	0.083577	0.9469
BLZK	0.287657	10.67593	2.694179	0.0263
BLINV	-2.079123	1.704849	-2.792535	0.0192
BLGE	54.16133	24.71693	-2.781265	0.0201
BLC	-150.5137	61.80418	-2.435332	0.0480
BINF	-2.177975	0.953628	-2.283884	0.0627
BLYK	158.3686	57.67647	2.745809	0.0223
ECT(-1)	0.913335	0.781355	3.508250	0.0068
R-squared	0.996495	Mean dependent var		0.093333
Adjusted R-squared	0.950925	S.D. dependent var		2.894691
S.E. of regression	0.641259	Akaike info criterion		1.107849
Sum squared resid	0.411213	Schwarz criterion		1.768696
Log likelihood	5.691131	F-statistic		21.86742
Durbin-Watson stat	2.504597	Prob(F-statistic)		0.166015

The variables in the form of first difference is showing existence of significant at $\alpha = 1\%$ is ECT (-1), significant at $\alpha = 5\%$ is C, Zk, and significant at $\alpha = 10\%$ is Inf. And all the variables in the form of level shows relationship existence of significant at $\alpha = 5\%$ and $\alpha = 1\%$, The variable in first difference is showing the short term influence. while variable in the form of level (first difference) like BLZK, BLINV, BLGE, BLC, BINF, BLYK is shows influence in the long-term.

The value of coefficient of determination (R^2) is 0.996495 is showing that the variation of economic growth can be explain by public consumption, small medium enterprises

investment, inflation, government expenditure, disposable income, collected zakat and collected zakat years before (the distribution zakat) is equal to 99.65 percent, and 0.35 percent explain by the others variables of outside the model. The influence of independent variables in simultaneous model is significant at $\alpha = 1\%$.

In the table 11 can be explain of the short term and long term influence or impact of public consumption, small medium enterprises investment, inflation, government expenditure, disposable income, collected zakat and the distribution zakat to economic growth. In the short term the variables of public

consumption, small medium enterprises investment and disposable income have significant at $\alpha = 10\%$ to influence of economic growth in the short term.

In the long term the variables public consumption, small medium enterprises investment, government expenditure,

disposable income and collected and the distribution zakat have significant at $\alpha = 5\%$ and $\alpha = 10\%$ to influence of economic growth, while the inflation has a negative impact and significant to influence the economic growth.

Table 5. Influence the independent variable on dependent variable in the short term and the long term

Independent Variables	Short Term	Long Term
LC	2.664487***	2.998654**
LGE	1.133228	1.975289***
LINV	2.439418***	2.275289***
INF	-0.161049	-1.907057***
LZk	1.638422	2.105210***
LYd	2.584804***	2.248918***

Source: Output Analyze Data

* significant at $\alpha = 1$ percent.

** significant at $\alpha = 5$ percent.

*** significant at $\alpha = 10$ percent.

Short term: effect shock without lag in the observation period

Long term: the equilibrium effect after shock in the next period (from old equilibrium to new equilibrium)

Zakah which is distributed in the form of consumptive assistance alone has been able to provide a significant multiplier effect, let alone be given in the form of productive assistance such as venture capital or revolving funds, will certainly produce more multiplier effects large in an economy due to zakat in the form of productive assistance gives a greater effect than zakat in the form of consumptive assistance [23]. Zakat is channeled to people in need will have a greater effect on aggregate demand (aggregate demand) because the consumption needs of this group is relatively larger, however it should be realized that the strategic role of zakat will be realized if the Muslims really believe and perform zakat properly. In addition, it is necessary to implant a strong conviction about the importance of zakat obligations, both in order to establish vertical relationship with Allah SWT, as well as realize welfare fairly in community life [24].

Based on the above explanation it can be concluded that zakat has an important role in the economy, both in micro and macro, both within forms of consumptive and productive assistance, as well as for muzakki and mustahik [25].

Implementation of zakat worship in a systematic and organized model will be able to provide a multiplier effect that is not small to

increase the national income of a country due to the acceleration of money circulation that occurs in the economy. What is the mechanism of this zakat multiplier effect. Economically, this can be explained as follows assuming the aid of zakat is given in the form of consumptive:

Zakat in the form of consumptive aid given to mustahik will increase the income of mustahik, which means the purchasing power of mustahik on a product that becomes its needs will increase as well. Increased purchasing power of a product will impact on increasing demand for a product. Increased demand means that there will be an increase in production of a company, the impact of increased production is the addition of production capacity which means the company will absorb more labor. This means the unemployment rate will decrease. Meanwhile, on the other hand increased production will result in increased taxes paid to the state, whether corporate tax, value added tax or income tax.

If the state revenue from taxes increases, then the state will be able to provide facilities and infrastructure for development and able to provide public facilities for the community, and if zakat can be collected significantly will be able to provide free investment and health for the community. From the description above it

can be seen that from zakah payments can produce multiplier effect - in economic language this is known as multiplier effect-in consumptive assistance alone is able to provide a significant multiplier effect, let alone zakat given in the form of productive assistance such as working capital or revolving funds, then of course the multiplier effect will be gained even greater in an economy, due to zakat give the effect is twice as much as in zakat in the form of consumptive assistance [25].

IV. CONCLUSION

It is compulsory for a Muslim to pay zakat if he is eligible under the stipulated criteria pronounced by the *Shari'ah*. It is no less important as well for a Muslim citizen to pay tax since both zakat and tax could be used by the government to develop this nation. Since the administration of zakat is under authority of each state, thus there are differences in zakat practice among states in Malaysia. Every state have a differences policy administration zakat because every state have a different problem. This thing will give the different implication and it is possible that more applicable for every state, because the state more knowing the condition of each states. So administration of religious obligation can more optimal.

From the result of analyze this thing proved that in Malaysia zakat can influence economic growth, consumption and investment. The other result of analysis OLS express that zakat have a positive influence to economic growth. Zakat have a positive influence to consumption and investment, although it is (the value still be small that is equal 0.0932 for influence economic growth, 4.406 for influence consumption and 0.186 for influence investment (small medium enterprises)).

According the OLS analysis, the analysis of TSLS and ECM also gives the same result, where the zakat will influence economic growth. either in short term and also on a long term. therefore the management of zakat in Malaysia can be made example for the same nations is including Malaysia where zakat can be applied to individual reduced income tax. Beside also shelf distribution system of zakat done that more improved especially for investment and legal capital help to all ever greater unemployment in Malaysia.

Because, distribution zakat for cost financing like self capital, capital for small and medium enterprises and training for unemployment have been a short term and long

economy, which in the end will indirectly also impact to us. Assistance given in the form of

term effect on economic growth, beside have a multiplier effect.

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