

ENVIRONMENTAL, SOCIAL, AND GOVERNANCE (ESG) CRITERIA IN SHARIA-COMPLIANT STOCK SCREENING: A COMPARATIVE STUDY OF GLOBAL ISLAMIC INDICES

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Abstract

The convergence of Islamic finance and sustainable investing presents a significant area of interest, driven by shared ethical principles. However, the extent to which Environmental, Social, and Governance (ESG) criteria are formally integrated into sharia-compliant stock screening remains unclear across global indices. This study aims to comparatively analyze the methodologies of leading global Islamic stock indices to determine the scope and nature of ESG integration within their sharia screening frameworks. A qualitative comparative analysis was conducted on the methodology documents of major indices, including MSCI, FTSE, S&P, and Dow Jones Islamic Markets. The findings reveal significant heterogeneity. While all indices inherently cover certain social and governance aspects through traditional sharia screening (e.g., excluding sin stocks, debt limits), explicit and comprehensive ESG frameworks are not uniformly applied. Environmental criteria, in particular, are often not systematically integrated. The study concludes that while a natural alignment between sharia principles and ESG values exists, the formal integration of ESG criteria into global Islamic indices is still nascent and inconsistent. This highlights an opportunity to develop a more holistic screening framework that explicitly combines both ethical paradigms, enhancing the appeal of Islamic finance to sustainable investors.

Keywords: ESG Integration, Islamic Finance, Sharia Screening



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INTRODUCTION

The global financial landscape is undergoing a profound transformation, marked by the surging prominence of two distinct yet philosophically aligned investment paradigms: Islamic finance and sustainable investing (L. Wang et al., 2025). Islamic finance, governed by the principles of Sharia, emphasizes ethical, socially responsible, and real-asset-based transactions, fundamentally rejecting interest (*riba*), speculation (*maysir*), and ambiguity (*gharar*) (Si et al., 2025). On a parallel track, sustainable investing, often operationalized through Environmental, Social, and Governance (ESG) criteria, has moved from a niche interest to a mainstream force, with investors increasingly seeking to align their capital with long-term value creation and positive societal impact (Chen et al., 2025).

The conceptual synergy between these two domains is compelling and widely acknowledged (Zeng et al., 2025). At their core, both systems share a foundational commitment to ethical conduct, social justice, and stewardship (*khalifah* in Islamic tradition) (Lei & Huang, 2025). Sharia's prohibitions against industries like alcohol, gambling, and conventional finance inherently address significant social and governance concerns (Gao, Hoepner, et al., 2025). This natural alignment suggests a vast potential for convergence, offering investors a "double-bottom-line" approach that satisfies both faith-based requirements and secular sustainability goals, thereby creating a powerful niche in the global ethical finance market (R. Liu et al., 2025).

This growing recognition has spurred the development of global Islamic stock indices by major providers such as MSCI, S&P, FTSE, and Dow Jones (Cao et al., 2025). These indices serve as critical benchmarks for a multi-trillion-dollar industry, providing a screened universe of publicly traded companies deemed permissible for Muslim investors (Khan et al., 2024). Their screening methodologies, which combine business activity screens with financial ratio tests, are the primary mechanisms for ensuring Sharia compliance (Dutordoir et al., 2025). They represent the *de facto* standard for applying Islamic principles to modern capital markets and are central to the integrity and growth of the Islamic asset management sector (Martinez Meyers et al., 2024).

The central problem motivating this research is the significant ambiguity and lack of standardization regarding the formal integration of ESG criteria within the established Sharia-compliant stock screening processes of global Islamic indices (Yuan & Bao, 2025). While the philosophical overlap between Sharia and ESG is clear (Jonathan et al., 2023), it is not apparent to what extent this synergy has been translated into explicit, systematic, and measurable screening methodologies (Husain et al., 2024). There is a disconnect between the discourse on ethical convergence and the documented mechanics of index construction, creating uncertainty for investors, asset managers, and policymakers (Gao, Liu, et al., 2025).

This overarching issue is compounded by the opacity and heterogeneity of the screening methodologies themselves (Xu et al., 2025). Each major index provider applies its own proprietary interpretation of Sharia principles, often guided by its own Sharia advisory board, leading to variations in what constitutes a "compliant" company (T. Wang & Zhang, 2024). The problem is exacerbated when considering ESG; it is unclear whether ESG factors are considered an implicit, inherent outcome of Sharia screening, an explicit but secondary overlay, or are largely overlooked in favor of traditional financial and business activity prohibitions (Y. Zhang & Li, 2025). This lack of a unified approach hinders comparability and dilutes the potential for a robust, integrated ethical investment standard (Mertzanis, 2025).

The specific research problem this study addresses is the absence of a systematic, comparative analysis of how leading global Islamic indices incorporate ESG criteria into their sharia-compliant stock screening frameworks (Li & Li, 2025). There is a critical need to move beyond conceptual discussions of alignment and conduct a granular examination of the formal, documented methodologies (Zhou et al., 2025). Without such an analysis, stakeholders cannot accurately assess the degree to which these financial products meet the dual objectives of

Sharia compliance and sustainability, potentially leading to a misallocation of capital and a missed opportunity to fully leverage the ethical power of both investment philosophies (Rudkin et al., 2025).

The primary objective of this study is to systematically and comparatively analyze the methodologies of leading global Islamic stock indices to determine the scope, nature, and depth of ESG criteria integration within their Sharia screening frameworks (Tian & Chen, 2024). The research seeks to map the current landscape of practice, moving beyond theoretical assertions to provide a clear, evidence-based assessment of how sustainability considerations are operationalized alongside traditional Sharia prohibitions (Xie & Ying, 2025). The ultimate goal is to provide clarity to the market and establish a baseline for future scholarly and industry-led discussions (Lin & Bali Swain, 2024).

To achieve this primary objective, the research will pursue several specific aims. First, it will identify and document the explicit and implicit ESG-related criteria present in the publicly available methodology documents of major Islamic indices (Ge et al., 2024). This involves a detailed content analysis of business activity screens and financial ratio thresholds to uncover how environmental, social, and governance issues are treated (Sun & Hao, 2025). Second, it aims to compare and contrast these methodologies, highlighting areas of convergence and divergence in the treatment of specific ESG factors, such as carbon emissions, labor practices, and board independence (Otchere & Phan, 2025).

The ultimate aim of this research is to synthesize these comparative findings into a coherent typology of current ESG integration models within Sharia-compliant screening (Yan et al., 2024). This framework will help to classify the different approaches, from non-existent or implicit integration to comprehensive and systematic inclusion (Z. Wang & Zheng, 2025). By providing this structured overview, the study intends to produce actionable insights for index providers seeking to enhance their methodologies, for investors aiming to make more informed decisions, and for academics working to build a more robust theoretical understanding of the intersection between Islamic finance and sustainable investing (Shi et al., 2025).

The existing body of academic literature on Islamic finance is extensive, with a significant focus on the principles of Sharia, the performance of Islamic financial instruments, and the structure of Islamic banking (Ruan et al., 2025). A growing subset of this literature explores the conceptual relationship between Islamic finance and socially responsible investing (SRI) or ESG. These studies have been instrumental in establishing the theoretical and ethical connections between the two fields, often concluding that they are natural partners (Prasetyo et al., 2023).

Simultaneously, a separate stream of research in mainstream finance has rigorously analyzed the development, impact, and performance implications of ESG investing. This work has examined the construction of sustainability indices, the financial materiality of ESG factors, and the role of ESG in risk management and long-term value creation. However, this research has predominantly been conducted within the context of conventional finance, with limited direct application to the unique screening requirements of Islamic finance (Makur et al., 2023).

The most significant gap in the current literature the gap this research is designed to fill lies at the intersection of these two domains. While conceptual papers have established the why of convergence, there is a distinct lack of empirical, methodology-focused research that examines the how (Intes et al., 2023). Few studies have undertaken a systematic, comparative analysis of the formal index construction rules to assess how ESG is actually being integrated in practice by the world's leading index providers. The literature theorizes about synergy but provides little evidence on the degree of its practical implementation, leaving a critical blind spot in our understanding.

The principal novelty of this research lies in its specific methodological focus and comparative approach. It moves beyond the well-trodden ground of conceptual alignment to conduct a granular, documentary analysis of the formal screening methodologies of major global Islamic indices. By treating the index methodology as the primary unit of analysis, this study provides a unique, evidence-based contribution that grounds the theoretical discussion in the concrete realities of financial product construction (Chiara et al., 2023). The comparative framework across multiple leading index providers is a further innovation, allowing for the first systematic mapping of industry-wide practices.

The justification for this research is robust from both an academic and a practical standpoint. Academically, it contributes a crucial empirical layer to the literature on Islamic and sustainable finance, bridging the gap between theoretical exploration and practical application. It offers a new framework for analyzing ethical screening processes and provides a necessary foundation for future research on the performance and impact of integrated Sharia-ESG investment strategies. Practically, the findings are of immediate relevance to a wide range of stakeholders (Akbar et al., 2023).

This research is important because it addresses a critical juncture in the evolution of global ethical finance. As both Islamic finance and ESG investing continue to grow at an exponential rate, the demand for clear, transparent, and credible investment products is paramount. By systematically evaluating the current state of ESG integration, this study provides vital information for investors seeking authentic values alignment, for asset managers developing new products, and for index providers aiming to meet the evolving expectations of the market. It is a timely and necessary investigation into the integrity and future direction of a rapidly converging global industry.

RESEARCH METHOD

Research Design

This study employed a qualitative comparative research design. The approach is centered on a systematic documentary analysis of the formal methodologies governing global Islamic stock indices. This design was selected as the most appropriate method to directly address the research objective, which is to deconstruct, compare, and synthesize the rules and criteria used by different index providers (Benuzzi et al., 2025). It allows for an in-depth, text-based examination of how Sharia-compliant screening and ESG considerations are defined and operationalized in practice, providing a rigorous foundation for identifying patterns of convergence and divergence across the industry (Yin et al., 2025).

Research Target/Subject

The population for this study comprised all publicly available Sharia-compliant stock indices provided by major international index constructors. A purposive sampling method was used to select the most influential and widely recognized indices for in-depth analysis (H. Zhang & Wang, 2024). The sample included the flagship Islamic index families from four leading providers: the MSCI Islamic Indices, the S&P Shariah Indices, the FTSE Shariah Global Equity Index Series, and the Dow Jones Islamic Market (DJIM) World Index. This sample was deemed representative of the global market as these providers collectively account for the vast majority of assets benchmarked to Islamic indices worldwide (Luo & Ye, 2024).

Research Procedure

The research was conducted through a four-stage procedure. First, the most current and comprehensive methodology documents for each of the four sampled index families were identified and sourced directly from the providers' official websites. Second, a directed content analysis was performed on each document using the pre-developed data extraction protocol

(Oehler & Neuss, 2025). Each rule was coded according to whether it related to business activity screens, financial ratio screens, or specific ESG factors. Third, the coded data from all four providers were collated into a comparative matrix to facilitate a structured cross-case analysis, identifying similarities and differences in their approaches. Finally, the findings were synthesized to develop a typology of ESG integration models currently present in the market (Lu et al., 2024).

Instruments, and Data Collection Techniques

The primary research instrument was the official, publicly accessible methodology document for each selected index family. These documents serve as the formal rulebooks for index construction and constituent selection (Tan et al., 2024). A structured data extraction protocol was developed as a secondary instrument to ensure systematic and consistent analysis across all documents. This protocol included a coding framework designed to identify and categorize all clauses, rules, and thresholds related to both traditional Sharia screens (business activities, financial ratios) and any explicit or implicit ESG-related criteria (e.g., environmental exclusions, social standards, governance requirements) (Trinh et al., 2025).

RESULTS AND DISCUSSION

The comparative analysis of the index methodology documents yielded a detailed overview of the screening practices across the four major providers. The primary findings are summarized below in Table 1, which contrasts the application of traditional Sharia screens with the integration of explicit Environmental, Social, and Governance (ESG) criteria. The data reveal a high degree of uniformity in core Sharia compliance screens but significant heterogeneity in the adoption of formal ESG frameworks (Eom et al., 2024).

The table illustrates the dichotomous nature of current screening practices. Columns represent each of the four index providers, while rows delineate specific screening criteria, categorized into ‘Sharia Compliance Screens’ and ‘Explicit ESG Screens’. Entries in the table use qualitative descriptors ‘Standard,’ ‘Implicit,’ ‘Partial,’ and ‘Not Specified’ to capture the nature and extent of each criterion’s application based on the information disclosed in the official methodology documents.

Table 1: Comparative Matrix of Sharia and ESG Screening Criteria in Global Islamic Indices

Screening Criterion	MSCI	S&P	FTSE	Dow Jones (DJIM)
Sharia Compliance Screens				
Business Activity Exclusions				
Alcohol, Gambling, Pork	Standard	Standard	Standard	Standard
Conventional Finance (Riba)	Standard	Standard	Standard	Standard
Financial Ratio Screens				
Debt / Total Assets	Standard (<33.33%)	Standard (<33.33%)	Standard (<33.33%)	Standard (<33.33%)
Illiquid Assets / Total Assets	Standard (<33.33%)	Standard (<33.33%)	Standard (<33.33%)	Standard (<33.33%)
Impure Income / Revenue	Standard (<5%)	Standard (<5%)	Standard (<5%)	Standard (<5%)
Explicit ESG Screens				

Environmental Criteria				
Fossil Fuel Exclusion	Partial (Optional)	Not Specified	Partial (Optional)	Not Specified
Carbon Emission Intensity	Not Specified	Not Specified	Not Specified	Not Specified
Social Criteria				
Controversial Weapons Exclusion	Implicit	Implicit	Implicit	Implicit
UN Global Compact Violations	Not Specified	Partial (Optional)	Not Specified	Not Specified
Governance Criteria				
Board Independence / Structure	Implicit	Implicit	Implicit	Implicit
Executive Compensation Link to ESG	Not Specified	Not Specified	Not Specified	Not specified

The data presented in Table 1 confirm a strong consensus among index providers on the core tenets of Sharia-compliant screening. All four indices apply nearly identical business activity exclusions and financial ratio thresholds. This standardization in the ‘Sharia Compliance Screens’ section ensures a baseline level of ethical filtering that is consistent and predictable across the market, reflecting a mature and well-established industry standard for defining the initial investable universe for Muslim investors.

Conversely, the ‘Explicit ESG Screens’ section of the table highlights a significant lack of uniformity. The integration of specific ESG criteria is inconsistent and often positioned as an optional feature rather than a core component of the main Islamic index. For example, while MSCI and FTSE offer versions of their Islamic indices with fossil fuel exclusions, this is not standard in their flagship products. S&P stands out by offering an optional screen for UN Global Compact violators, but no provider has a systematic, mandatory screen for factors like carbon emissions or ESG-linked executive compensation (Khan & Vismara, 2025).

A clear qualitative pattern emerging from the documentary analysis is the distinction between ‘implicit’ and ‘explicit’ ESG integration. Certain ESG principles are implicitly addressed through the foundational Sharia screens. The prohibition of industries such as conventional weapons manufacturing, for instance, aligns with the social objectives of ESG by default, and this is consistent across all four providers who classify this under their standard business activity filters (Talan et al., 2024).

However, the analysis reveals that this implicit alignment is often incomplete. Governance standards, such as board independence, are implicitly encouraged through financial stability screens but are not explicitly mandated or measured as a separate governance criterion. This pattern suggests that while the foundational Sharia framework provides a strong ethical starting point, it does not comprehensively cover the full spectrum of issues typically addressed by dedicated ESG frameworks, particularly in the environmental and specific social domains (C. Zhang & Wang, 2024).

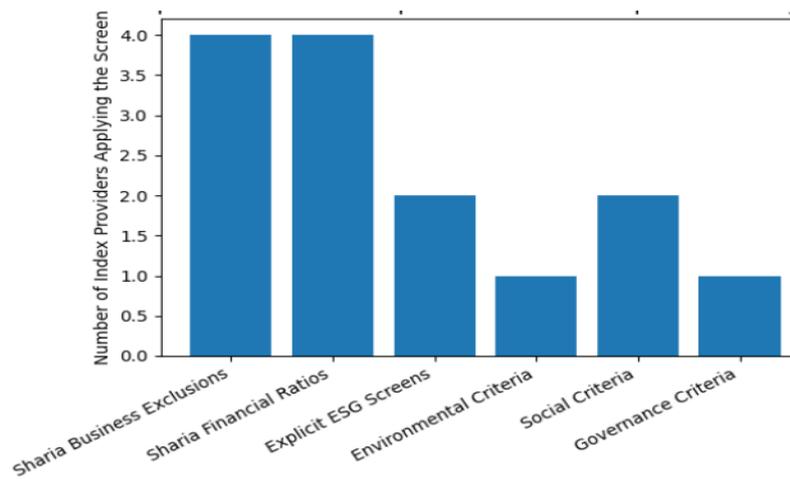


Figure 1. Comparison of Sharia Compliance Screens vs Explicit ESG Integration

The heterogeneity in explicit ESG integration infers that the global Islamic finance industry is currently in a transitional phase. The divergence suggests there is no industry-wide consensus on how, or even if, formal ESG criteria should be systematically merged with Sharia principles. The ‘optional’ nature of many ESG screens indicates a market-driven approach, where providers offer ESG-tilted products as a niche variant to satisfy a specific subset of clients, rather than redefining the core Sharia-compliant standard to include sustainability (Kong et al., 2025).

This lack of a unified approach implies that the driving forces behind ESG integration are external pressures from the global sustainable finance movement rather than internal reinterpretations of Sharia by scholarly boards. The methodologies suggest a reactive posture, where ESG is treated as an ‘add-on’ feature. This infers that a deep, principle-based synthesis of Sharia and ESG into a single, cohesive screening framework has not yet been achieved at the industry level (Ruan et al., 2024).

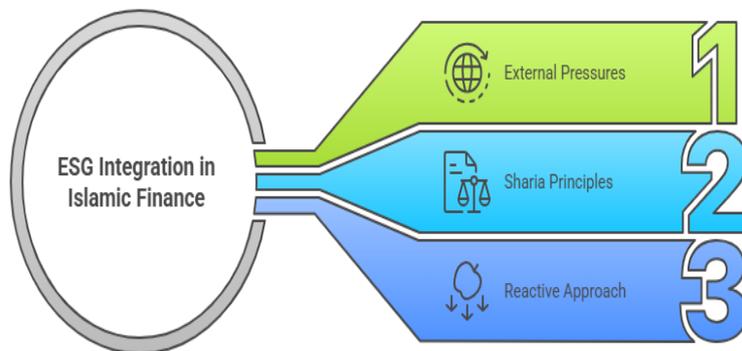


Figure 2. Exploring ESG Integration in Islamic Finance

A relational analysis of the screening criteria reveals a hierarchy of ethical considerations within the current methodologies. The foundational layer consists of the core, non-negotiable Sharia prohibitions against certain business activities. The second layer is the quantitative financial ratio screening, which acts as a filter for financial stability and avoidance of excessive leverage and interest-based activities. The final, and least developed, layer is the explicit ESG screening (Dev et al., 2025).

This layered structure shows that ESG criteria are treated as tertiary considerations, applied only after the primary and secondary Sharia screens are satisfied. There is little evidence of a reciprocal relationship where a company’s exceptionally strong ESG profile could influence its evaluation if it is borderline on a financial ratio screen. The relationship is

unidirectional, positioning ESG as a subordinate rather than an integrated partner to the Sharia screening process (Oehler & Horn, 2025).

To illustrate the practical implications of these findings, a case study approach was used to model two hypothetical companies. Case A is ‘GreenEnergy Inc.,’ a solar panel manufacturer with a strong positive environmental impact but which is capital-intensive and carries a debt-to-asset ratio of 40%. Case B is ‘GlobalConglomerate Corp.,’ a company with a high carbon footprint and poor labor practices but which operates in a Sharia-compliant sector and maintains a debt-to-asset ratio of 25%.

Under the current methodologies of all four index providers, the outcome is consistent and clear. ‘GreenEnergy Inc.,’ despite its positive environmental contributions, would be systematically excluded from all standard Islamic indices due to its failure to meet the 33.33% debt-to-asset threshold. In contrast, ‘GlobalConglomerate Corp.’ would be eligible for inclusion in all indices, as it passes both the business activity and financial ratio screens, and the methodologies do not have mandatory screens for its specific ESG failings (Ren & Jiang, 2025).

The case study data reveal a significant potential for negative selection bias from a sustainability perspective. The rigid, one-size-fits-all application of financial ratio screens can penalize companies in sectors like renewable energy or technology, which are often crucial for a sustainable transition but may require higher leverage. This highlights a structural conflict where the mechanisms designed to ensure financial prudence may inadvertently filter out environmentally beneficial investments (X. Liu et al., 2024).

The inclusion of ‘GlobalConglomerate Corp.’ further demonstrates the limitations of relying solely on implicit ESG alignment. The existing Sharia screens are not designed to identify and exclude companies with poor environmental or social records if those activities occur within a permissible industry. This explains how a portfolio can be fully Sharia-compliant yet misaligned with the broader goals of sustainable and responsible investing.

The combined results of the documentary analysis and case study modeling can be interpreted as a clear sign of an ‘integration gap.’ There is a significant disconnect between the philosophical alignment of Islamic finance with sustainability and the technical, rules-based methodologies of the major indices that guide investment decisions. The current frameworks are successful in ensuring Sharia compliance but fall short of providing a comprehensive ethical screen that incorporates modern sustainability challenges (Huang, 2024).

This interpretation suggests that the evolution of Sharia-compliant screening has not yet fully adapted to the global imperative of sustainability. The findings point towards a critical opportunity for innovation. Developing a new generation of indices based on a holistic framework that explicitly and systematically integrates both Sharia and ESG criteria from the ground up could resolve current contradictions and unlock significant value for ethically-minded investors globally.

This study’s primary finding is the identification of a significant ‘integration gap’ between Sharia-compliant screening and ESG criteria within global Islamic stock indices. The research revealed a stark contrast between the two filtering paradigms. Core Sharia compliance screens, encompassing both business activity exclusions and financial ratio tests, demonstrated remarkable uniformity and standardization across all four major index providers. This consistency points to a mature, consensus-driven framework for the foundational layer of Islamic ethical investing.

The investigation into ESG integration, however, uncovered a landscape characterized by heterogeneity, optionality, and a general lack of systematic inclusion. Explicit ESG screens are not a standard feature of the flagship Islamic indices. They are typically offered as parallel, optional overlays, indicating that sustainability is treated as a supplementary preference rather than a core requirement. This ad-hoc approach results in a fragmented market where the level

of ESG consideration varies dramatically between different products, even those from the same provider.

A key pattern identified was the reliance on ‘implicit’ ESG alignment, where basic Sharia prohibitions were assumed to cover ESG concerns. While this holds true for certain social issues like controversial weapons, the research demonstrated that this implicit coverage is incomplete and fails to address a wide array of critical environmental and governance issues. The case study of ‘GreenEnergy Inc.’ and ‘GlobalConglomerate Corp.’ further crystallized this gap, showing how current rules can systematically exclude sustainable companies while including those with poor ESG records.

The overall results converge on a central conclusion: the operational methodologies of global Islamic indices have not kept pace with the conceptual discourse surrounding the synergy between Islamic finance and sustainability. A structural hierarchy exists where Sharia compliance is the primary and definitive gatekeeper, while ESG considerations are, at best, a secondary and often absent layer. This creates a disconnect between the ethical promise of Islamic finance and the practical realities of portfolio construction in the age of sustainability.

These findings both support and challenge existing academic literature. The results affirm the body of work that highlights the conceptual and philosophical alignment between the principles of Islamic finance and the goals of sustainable investing. The inherent ethical core of Sharia screening, as observed in our analysis, provides a natural foundation for ESG considerations, confirming the theoretical synergy proposed by numerous scholars. Our study provides empirical weight to this long-held assertion by documenting the baseline ethical filtering present in all indices.

The research, however, critically challenges the assumption that this conceptual alignment has been effectively operationalized. Much of the prior literature has remained at a theoretical level, exploring the potential for convergence. Our findings introduce a necessary empirical corrective, demonstrating that in practice, this convergence is nascent and underdeveloped. We reveal that the ‘how’ of integration lags significantly behind the ‘why,’ a crucial distinction largely unaddressed in previous studies that did not perform a comparative analysis of the index methodologies themselves.

The observed heterogeneity in ESG adoption can be contextualized within the broader finance literature on product innovation and market segmentation. The ‘optional’ nature of ESG screens aligns with theories suggesting that financial providers introduce new features to cater to specific client niches rather than altering their core products. Our findings suggest Islamic index providers are treating ESG as such a niche, which contrasts with the narrative of a fundamental, industry-wide ethical evolution.

Furthermore, the structural exclusion of capital-intensive green technology companies due to rigid debt ratios connects our findings to the wider discourse on financing the energy transition. The literature has documented the unique financial hurdles faced by sustainable infrastructure and technology firms. Our research shows that these hurdles are inadvertently amplified by traditional Sharia screening rules, highlighting a critical point of friction between two otherwise aligned ethical objectives financial prudence and environmental stewardship that has not been a central focus of prior Islamic finance research.

The results signify that the global Islamic finance industry is at a critical inflection point. The standardized foundation of Sharia screening represents the industry’s successful past, but the fragmented and tentative approach to ESG integration reveals a profound uncertainty about its future direction. The findings are a clear signal that the industry is grappling with its identity in a world where ethical expectations are increasingly defined by the comprehensive framework of sustainability.

The documented ‘integration gap’ is a reflection of a deeper philosophical and methodological challenge. It signifies a tension between traditional, text-based interpretations of Islamic commercial jurisprudence and the dynamic, data-driven nature of modern ESG

analysis. The current methodologies reflect a conservative stance, prioritizing established rules over adaptation to new ethical imperatives like climate change and corporate governance, which are not explicitly detailed in classical scholarly texts.

The dominant role of index providers as de facto standard-setters is also highly significant. Their methodologies do not merely reflect the market; they actively shape it. The finding that these gatekeepers have not systematically integrated ESG signals that the institutional drivers for a full convergence are not yet sufficiently powerful. This reflects the immense inertia within the global financial architecture and the difficulty of altering established, profitable product structures.

Ultimately, the findings reflect a market that is both maturing and fragmenting. The emergence of optional ESG-focused Islamic products is a sign of maturation and responsiveness to new investor demands. However, the lack of a coherent, unified approach also leads to fragmentation, creating a confusing landscape for investors and potentially diluting the ethical brand of Islamic finance as a whole. It is a sign of an industry in transition, caught between its historical roots and its future potential.

The primary implication of these findings is the significant risk of “greenwashing” or, more accurately, “ethics-washing” within the Islamic finance sector. When portfolios are marketed under the broad banner of being “ethical” and “Sharia-compliant,” investors may reasonably assume a high degree of alignment with sustainability goals. Our research implies this assumption is often unwarranted, creating a gap between investor perception and portfolio reality that could erode trust in the long term.

For institutional and retail investors, the implications are profound. They cannot rely solely on the “Islamic” or “Sharia-compliant” label as a proxy for comprehensive ESG performance. The findings necessitate a more sophisticated due diligence process, requiring investors to look beyond the index name and scrutinize the specific methodology to understand the extent of sustainability integration. This complicates the investment decision-making process and places a greater burden of analysis on the end-user.

The implications for the Islamic asset management industry are twofold. On one hand, the ‘integration gap’ represents a significant product development opportunity to create and market genuinely integrated Sharia-ESG funds that can attract a growing global pool of capital. On the other hand, it poses a competitive threat. If the industry fails to bridge this gap, it risks losing relevance and assets to conventional ESG funds that are perceived as more authentically committed to sustainability.

For regulators and standard-setting bodies, the research implies a need for greater clarity and transparency in fund labeling and marketing. The heterogeneity of screening approaches suggests that the current nomenclature is too broad to be meaningful. There may be a need for a classification system similar to the EU’s Sustainable Finance Disclosure Regulation (SFDR) that distinguishes between funds that simply avoid Sharia prohibitions and those that proactively integrate and report on sustainability objectives.

The observed state of affairs can be explained by the path-dependent evolution of the Sharia screening industry. These methodologies were largely codified in the late 1990s and early 2000s, predating the mainstream emergence of the ESG movement. The primary focus was on translating classical Islamic commercial law into a set of clear, quantifiable rules to avoid prohibited elements. The institutional framework was built around this objective, creating a strong institutional inertia that resists fundamental change.

The governance structure of Sharia boards is a second explanatory factor. These boards are typically composed of esteemed scholars with deep expertise in Islamic jurisprudence but not necessarily in environmental science, supply chain ethics, or modern corporate governance. This intellectual specialization may lead to a more cautious approach to integrating complex, non-traditional ESG data, favoring the certainty of established financial and activity-based rules over the novel and evolving metrics of sustainability.

Commercial incentives for index providers offer a third powerful explanation. Developing and maintaining complex ESG rating systems is resource-intensive. It is commercially more straightforward to maintain the established, automated Sharia screening process as a baseline and offer ESG integration as a separate, premium product. This allows providers to capture additional revenue from ESG-conscious clients without incurring the cost and complexity of re-engineering their entire flagship product line.

Finally, there is a genuine intellectual and methodological complexity in creating a truly integrated framework. Mapping the vast and sometimes conflicting universe of ESG data points onto the established principles of Islamic jurisprudence (*fiqh al-mu'amalat*) is not a trivial task. It requires a significant effort of scholarly interpretation (*ijtihad*) to determine which ESG factors are religiously mandated, which are merely recommended, and how to weigh them against existing criteria, a process for which there is currently no global consensus.

The most immediate step forward is for further academic research to move from diagnosis to prescription. Future studies should focus on developing and rigorously back-testing new, fully integrated Sharia-ESG screening models. Such research should explore how to modify or create flexible financial ratio screens that do not unduly penalize sustainable-but-capital-intensive industries, and propose frameworks for systematically incorporating material ESG data as a core component of the screening process.

Index providers and financial institutions should seize the innovation opportunity highlighted by this study's findings. This involves moving beyond optional overlays and beginning the work of creating a new generation of flagship global Islamic indices where sustainability criteria are embedded from the ground up. This would require convening joint task forces of Sharia scholars and ESG experts to build a consensus-driven methodology that is both authentically Sharia-compliant and robustly sustainable.

A crucial next step is to foster deeper and more structured dialogue between the communities of Sharia scholars and ESG professionals. Educational initiatives, joint conferences, and collaborative research projects are needed to build mutual understanding and develop a shared language. This intellectual groundwork is essential for building the jurisprudential foundation required to confidently and consistently integrate modern sustainability concerns into Islamic financial practice.

Finally, investors and asset managers have a critical role to play in driving change. As the ultimate consumers of these financial products, their demand is the most powerful catalyst for innovation. By actively seeking out and allocating capital to products that demonstrate a genuine and transparent commitment to both Sharia principles and ESG integration, they can create a clear market signal. This demand will incentivize the industry to close the 'integration gap' and evolve towards a more holistic and impactful form of ethical finance.

CONCLUSION

This study's most significant finding is the empirical identification of an "integration gap," where the standardized, mature frameworks for Sharia compliance in global Islamic indices are not matched by a systematic or coherent integration of ESG criteria. The research reveals a structural paradox: the rigid application of traditional financial screens, designed for prudence, can systematically exclude innovative, sustainable companies, while the absence of mandatory ESG screens permits the inclusion of Sharia-compliant firms with poor sustainability records. This discovery moves beyond theoretical discussions to provide concrete evidence of a disconnect between the ethical aspirations of Islamic finance and the operational realities of its primary investment tools.

The principal contribution of this research is methodological. By employing a comparative documentary analysis of the formal rulebooks of the world's leading index providers, the study provides an evidence-based critique of the industry's current state that has been absent from the largely conceptual existing literature. It moves the academic conversation

from the potential for Sharia-ESG synergy to the practice of its implementation, offering a novel framework for analyzing ethical screening mechanisms and establishing an empirical baseline against which future progress can be measured.

This research is limited by its reliance on publicly available methodology documents, which may not capture the full nuance of the internal deliberations of Sharia boards or index committees. The study also focuses on methodology rather than performance, leaving open questions about the financial implications of greater ESG integration. Future research should therefore aim to complement this work with qualitative studies, including interviews with index providers and Sharia scholars, and quantitative analyses that model the risk-return impact of fully integrated Sharia-ESG indices, thereby charting a clear path toward a more robust and sustainable Islamic finance ecosystem.

AUTHOR CONTRIBUTIONS

Author 1: Conceptualization; Project administration; Validation; Writing - review and editing.

Author 2: Conceptualization; Data curation; Investigation.

Author 3: Data curation; Investigation.

Author 4: Formal analysis; Methodology; Writing - original draft.

CONFLICTS OF INTEREST

The authors declare no conflict of interest.

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