



Global Achievements and Prospects for Expansion in Islamic Finance

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Challenges

- Widening the market with less geographical concentration
- Ensuring risk sharing has substance

Aims And Achievements of Islamic Banks

- **Aims**

- Product range compatible with conventional offerings
- Current, savings and investment accounts available
- Major focus on vehicle financing and Islamic mortgages

- **Achievements**

- Shari'ah compliant assets exceed \$1.54 trillion worldwide
- 38 million customers, of which over 4 million Maybank Islamic (Ernst and Young)
- Islamic banks account for 18-48% of deposits in Malaysia and the GCC

Islamic Banking Assets and Market Share

Country	Assets \$ billion	Domestic market share %
Saudi Arabia	237	48.5
Malaysia	170	24.0
UAE	97	17.9
Kuwait	94	43.3
Qatar	52	23.1
Bahrain	19	13.4

Case Study: United Arab Emirates

- Dubai Islamic Bank, established 1975, first commercial Islamic bank
- Monopoly of Islamic finance until Abu Dhabi Islamic Bank founded, 1997
- Dubai Islamic Bank Pakistan established 2006
- Sharjah Islamic Bank, converted from National Bank of Sharjah, 2002
- Middle East Bank converted to Emirates Islamic Bank, 2004
- Noor Bank, formerly Noor Islamic Bank, established 2008



Case Study: Kuwait

Kuwait Finance House

- Founded 1977
- Regulated initially by Finance Ministry, not Central Bank
- Brought under Central Bank in 2004
- Focus on Kueyttürk Participation Bank since 2002
- Interest in Malaysia since 2005

Boubyan Bank

- Established 2004 following amendment of banking legislation
- Majority shareholding acquired by NBK in 2010

Kuwait International Bank

- Conversion of Kuwait Real Estate Bank in 2007



Case Study: United Kingdom

Islamic Bank of Britain (IBB)

- Opened 2004 and now has over 50,000 customers
- 5 branches in London (2), Birmingham, Leicester and Manchester
- 3 agencies in Luton, Tooting and Blackburn
- Retail bank with focus on home finance using diminishing musharaka and ijara
- Islamic asset managers

Bank of London and the Middle East (BLME), 2007

Gatehouse Bank, 2008

European Islamic Investment Bank, 2007

Qatar Islamic Bank (UK)

Standard Chartered Saadiq



Providing a Comprehensive Range of Retail Services

Offering most of the financial services provided by conventional banks but ensuring *Shari'ah* compliance

Deposits

- Current accounts identical but deposits segregated
- Profit sharing investment accounts alternative to savings accounts

Financing

- *Murabaha*/BBA continues to be dominant
- *Ijara* operational leases popular
- Diminishing *musharaka* for mortgages
- Some methods such as sale and buy back arrangements (*Bai' 'Inah*) rejected by most scholars

Money transfer and foreign exchange services the same as for conventional banks

Islamic Investment Banking

Arrangement of *sukuk* issuance

Advice on market listing

- Guidance on script dividends, rights issues and preference shares

Private equity financing

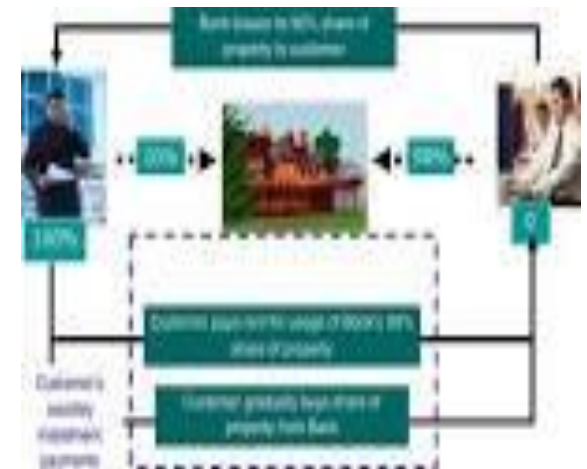
- *Musharaka* structures

Mergers and acquisitions

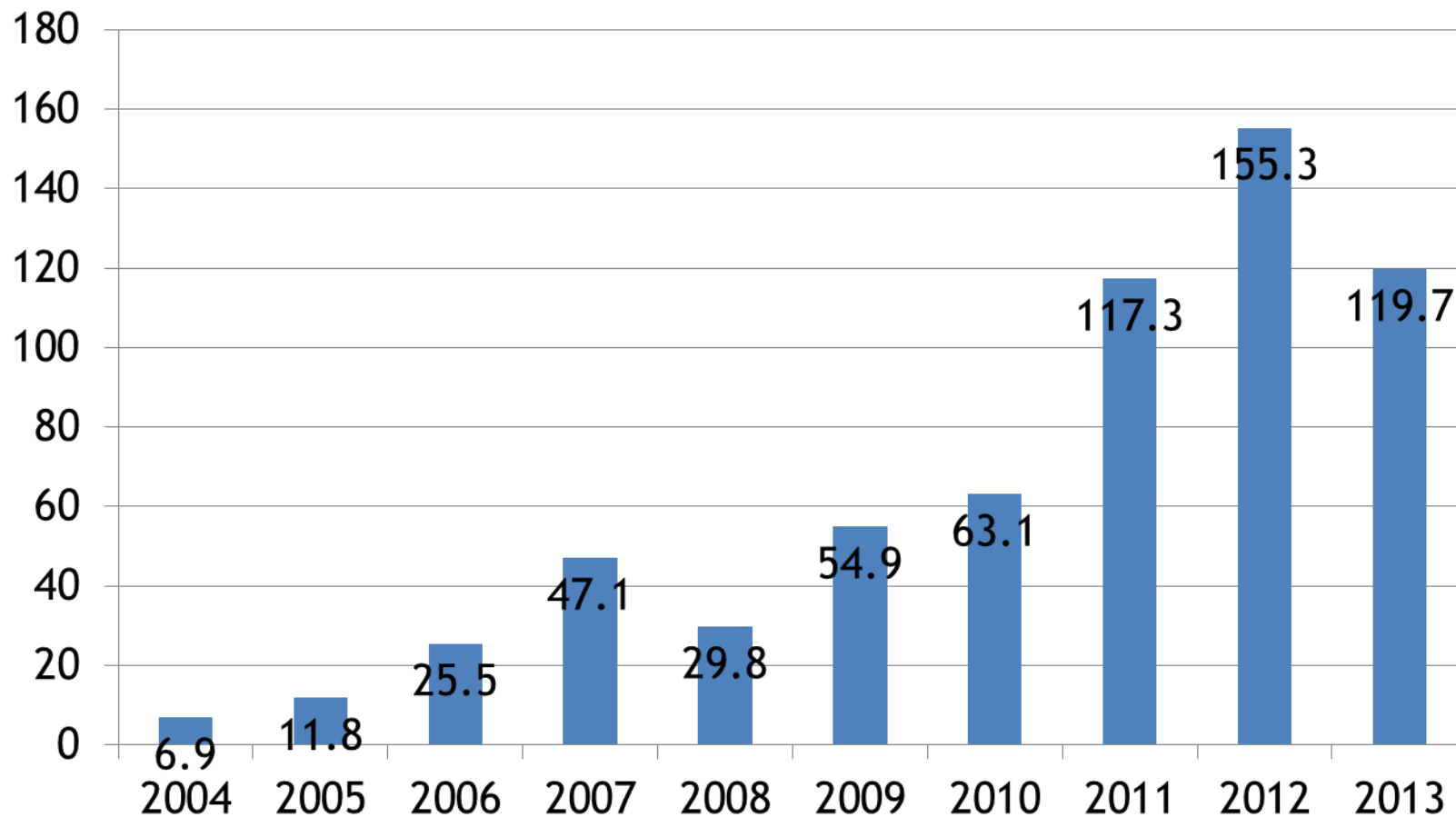
- Appraisal of viability

Disintermediation

- Capital market funding rather than bank finance



Value of New *Sukuk* Issuance, \$ billion



Shari'ah Compliant Wealth Management

Islamic equity fund offerings

- Sector and financial screening

Advice on portfolio management

- Assessment of risk preferences

Succession and inheritance planning

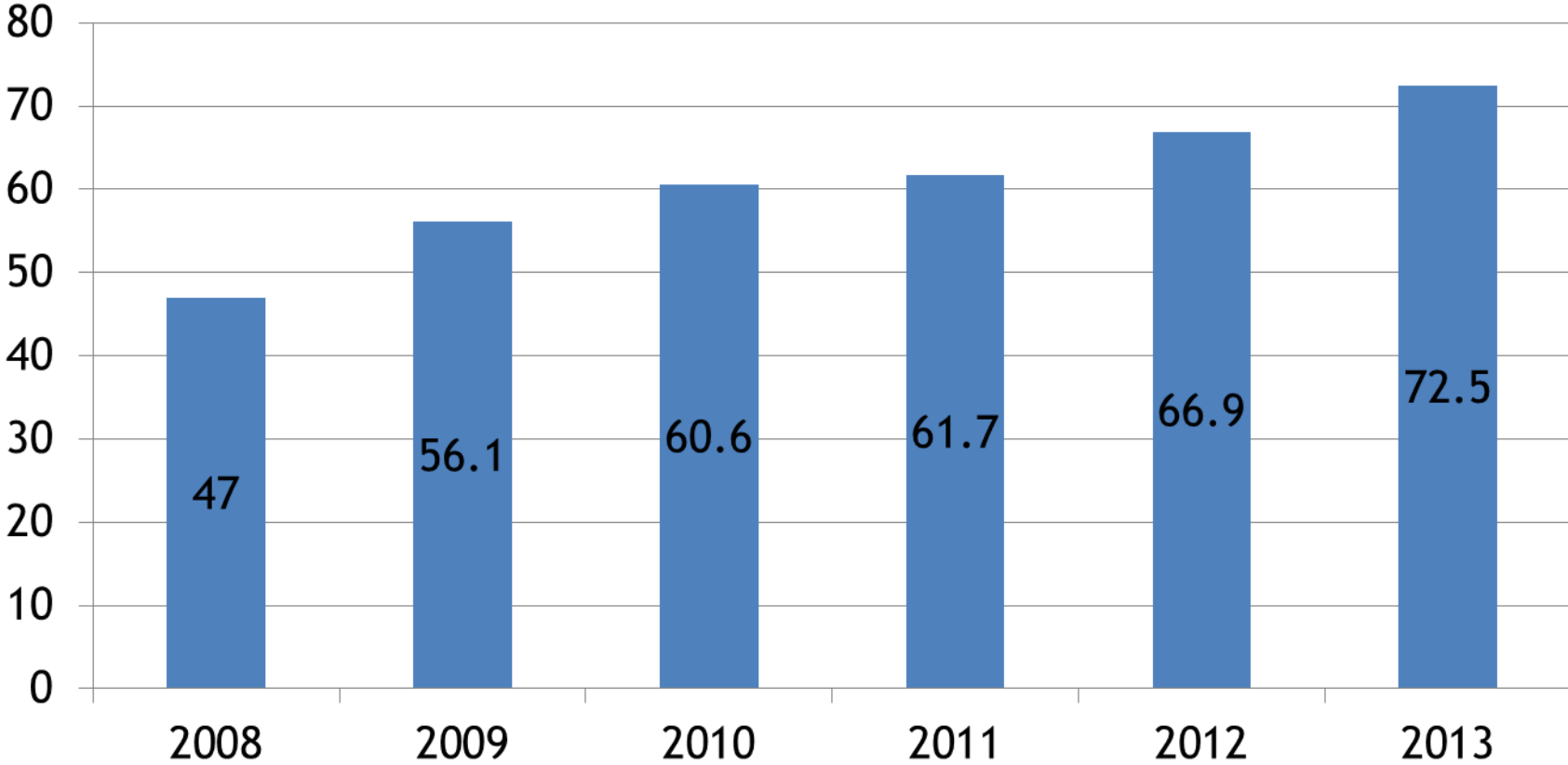
- Tax advice and *zakat* liability
- Islamic inheritance law and establishment of *waqf*

Treasury management and custodian services



Islamic Fund Assets, \$ billion

\$ billion



Demonstrate How *Shari'ah* Compliance Enhances the Product Offering

Peace of mind

- Customer has assurance that financial dealings in accordance with *Shari'ah*
- It is *Shari'ah* scholars who have ultimate accountability
- *Shari'ah* board ensures product integrity
- Reputation depends on *Shari'ah* authenticity



Social responsibility

- Banking with a moral purpose
- Ethical practices and branding
- Engagement in *halal* activities



Obstacles to Islamic Banking Expansion

Political sensibilities

- Islamic finance viewed in political terms in regions such as North Africa
- Islamist political parties associated with Islamic finance, often wrongly
- Flourishes best when seen as a business opportunity



Dependence on oil and gas pricing

- Economies of GCC, where Islamic finance most developed, oil and gas dependent
- Initial expansion of Islamic finance in the 1970s helped by high oil prices



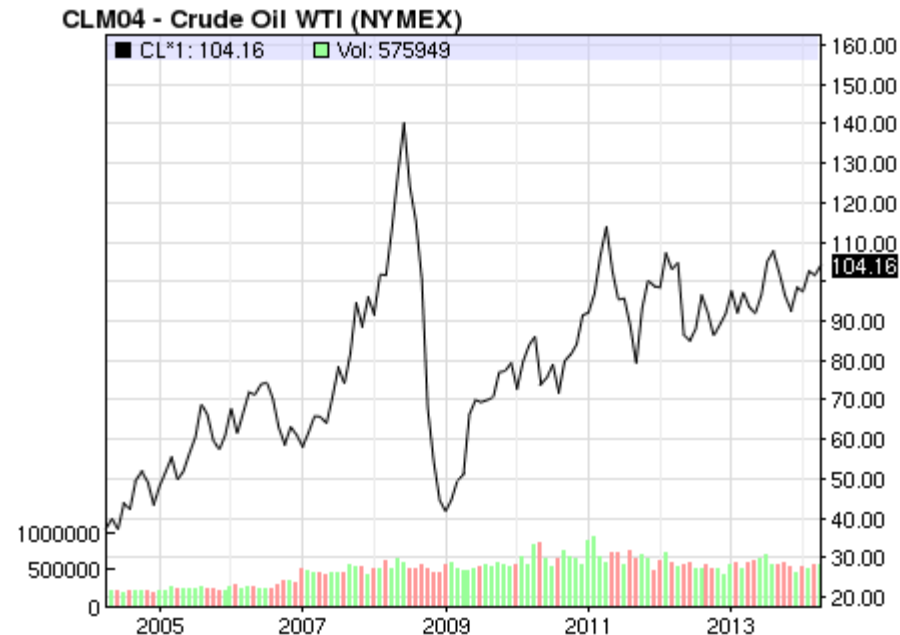
Scenario: Impact of a collapse of oil and gas prices on Islamic finance

Short term

- Negative impact on government revenue and expenditure on new projects
- Less *istisna* and *sukuk* issuance
- Minimal impact on Islamic retail banking
- KFH and Dubai Islamic Bank derive significant income from outside GCC

Long term

- UAE, Qatar and Kuwait less affected as large sovereign wealth funds
- Saudi Arabia more affected as a larger population to support
- Negative effect on Al Rajhi Bank



Legal and regulatory issues

Shari'ah, civil and common law

- Islamic financial contracts more easily enforceable in common law jurisdictions such as Malaysia

Legislative approached to Islamic finance

- Law to convert entire financial system as in Iran
- Comprehensive Islamic finance legislation as in Malaysia and Indonesia
- Addition and amendments to banking law as in Kuwait and UAE or changes to tax laws as in United Kingdom

Regulatory provision only

- Separate rulebook for Islamic finance as in Bahrain
- Special treatment in instructions to banks as in Qatar



Case Study: Iran's Law on Usury Free Banking, 1983

Article 1 provides for the establishment of a monetary and credit system based on rightness and justice as delineated by Islamic jurisprudence

Article 2 and 3 provide for *qard hasan* current account deposits and the granting of interest free loans

Article 3 provides for term investment *mudarabah* and *musharakah* deposits, hire purchase and installment transactions

Article 6 covers depositor benefits including bonuses in cash or in kind for *qard hasan* depositors, exemption from commissions and fees for all depositors as well as priority in receiving financing

Article 9 provides for *mudarabah* financing

Article 20 provides for Bank Markazi to set minimum and maximum profit ratios with respect to different sectors and activities and provides for minimum and maximum bonuses for depositors to be determined by the Central Bank

Client Perceptions

Scepticism regarding Islamic financial products

- Viewed as little different from conventional savings deposits and loans
- Returns to depositors and financing costs little different or worse
- The only differences with Islamic financial products are the Arabic names



Misunderstandings

- Clients cannot identify benefits from risk sharing
- Failure to comprehend the details in Islamic financial contracts



Remedies

Education and training

- Enhanced training for bank employees with emphasis on communication skills
- Education and certification for Islamic financial advisors



Shari'ah board responsibilities

- Provide more information on their work
- Explain rationale for *fatwa* issued



Treatment of investment depositors

- More information on how profit pay-outs calculated
- Explain benefits of profit equalisation reserves
- Stress on relationship banking and long term loyalty



Strategic Challenges

Product development

- Review contracts to determine what risks are shared
- Islamic mortgages to be based on diminishing *musharaka*
- Explore scope for parallel *salam* and *istisna*



Geographical focus

- Domestic, regional or global market focus



Cross selling

- Family, medical and general *takaful*
- Promote in-house or third party Islamic funds
- Private banking including legal and financial advisory services



Building global business

Bank	Assets \$ billion	Deposits \$ billion	Overseas focus
Al Rajhi	74.6	61.6	Malaysia
Kuwait Finance House	57.3	35.8	Turkey
Maybank Islamic	38.0	25.3	Indonesia, Singapore
Dubai Islamic Bank	30.8	21.6	Pakistan

Source: Bank Annual Reports and Financial Statements, December 31st 2013

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