



# Islamic Finance Achievements and Prospects

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- Islamic banking and economic development questions
- Financial widening and deepening in a *Shari'ah* context

# Supply side versus demand side effects of Islamic finance

## Demand

- Most Islamic banking retail
- Focus on consumer finance for vehicles and Islamic mortgages

## Supply

- Trade finance for wholesalers and retailers of imported goods
- Minimal finance of investment
- Project finance mainly for residential construction rather than industry

# Aims & 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 & 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 Kuveyttürk 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

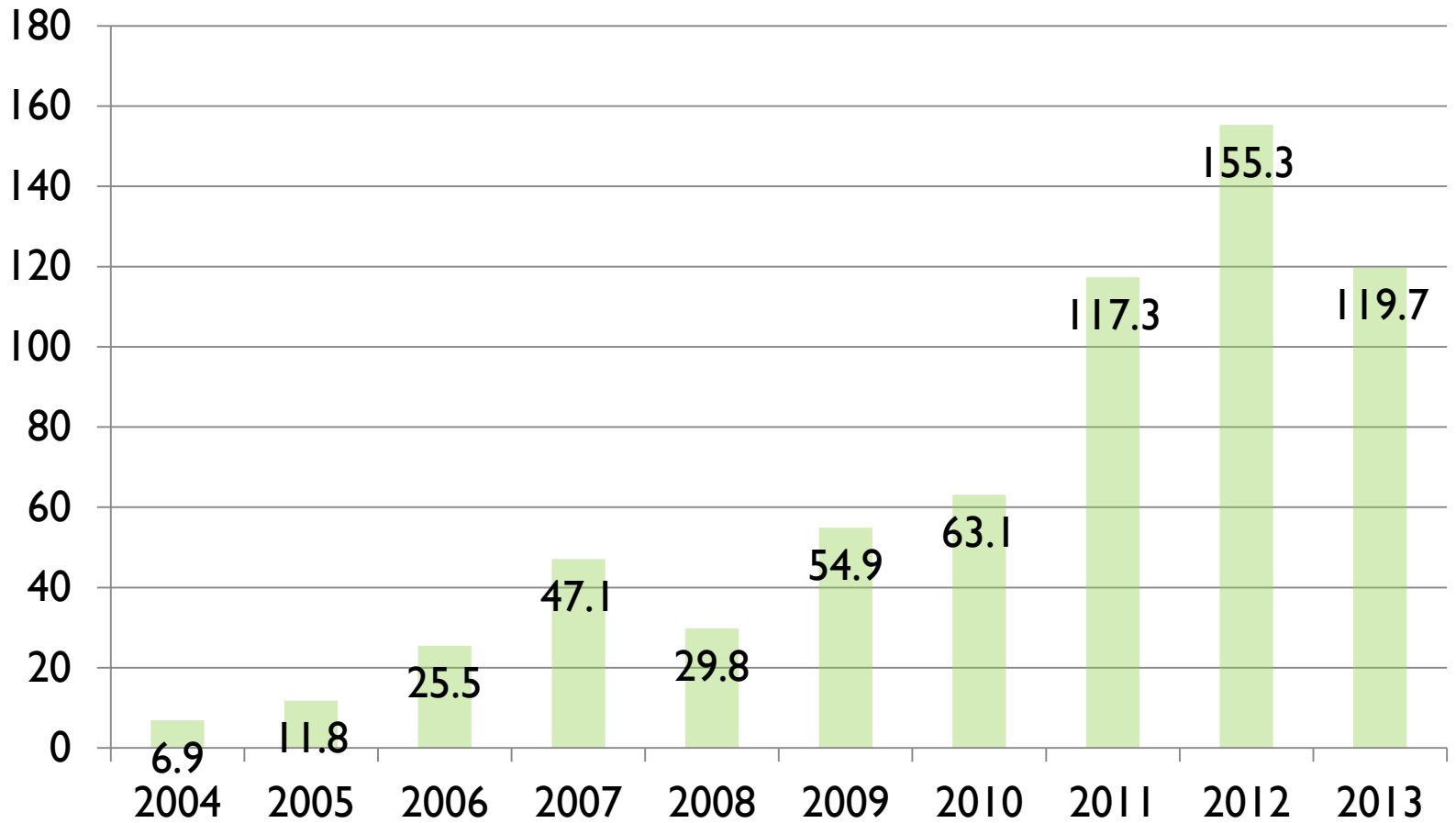
- Appraisal of viability

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**

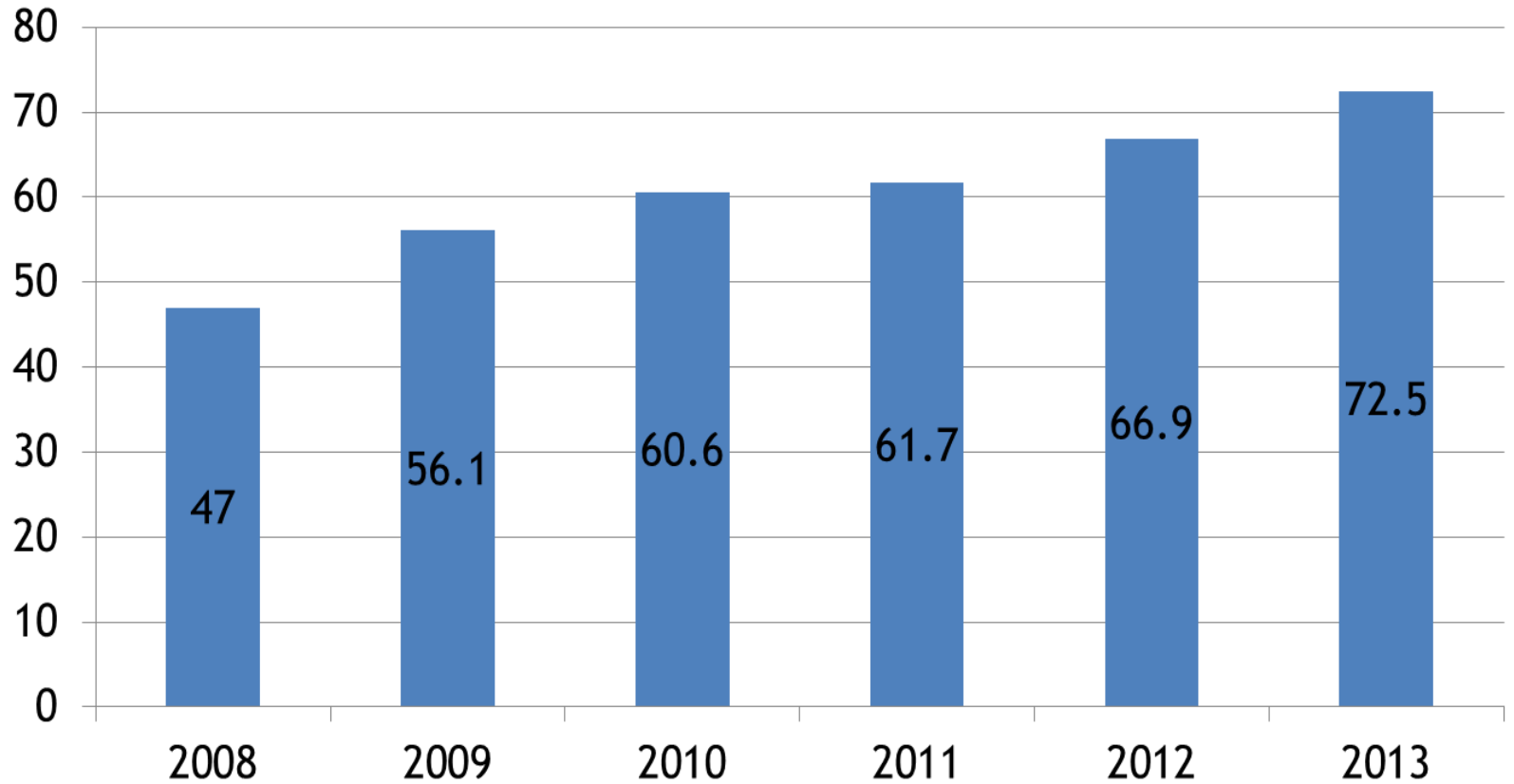
- Tax advice and *zakat* liability
- Islamic inheritance law and establishment of *waqf*

## **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



# Development experiences of countries with a substantial Islamic financial sector

- Is Islamic banking market penetration related to development?
- Does development come first increasing demand for Islamic finance or vice versa?
- What do we mean by development, per capita GDP or human development?



# Islamic banking and development questions

## Financial widening and deepening

- Relationship between bank asset growth and GDP
- Intermediation and disintermediation

## Causality questions

- Does retail Islamic banking enhance economic growth?
- How dependent is Islamic banking on oil and gas prices
- Is the growth of Islamic banks an outcome of development rather than an input

## Islamic micro-finance

- Funding for the financially excluded
- Provision by banks, credit unions or cooperatives

# Financial widening and deepening

## Financial widening

- Extending the range of financial services
- Moving beyond *murabahah*
- Offering more deposit facilities

## Financial deepening

- Bank asset to GDP ratio which increases with development
- Intermediation and disintermediation
- Bank deposits substituted for cash holdings
- With disintermediation capital market funding replaces bank credit

## Financial repression

- Low interest rates discourage savings
- Low cost funding undermines the efficient allocation of credit and supports zombie businesses: the living dead

# Causality questions

Does retail Islamic banking enhance economic growth?

- Can increase consumer spending hence increasing demand
- High leakages into imports reducing local multiplier effects
- Adds to inflation if local supplies limited

How dependent is Islamic banking on oil and gas prices?

- Most Islamic banking in GCC and Iran, oil dependent regions

Is the growth of Islamic banks an outcome of development rather than an input?

- Focus on consumer rather than business finance
- More interest in infrastructure finance through *istisna'a* and *sukuk*

# Islamic micro-finance

## Funding for the financially excluded

- Low and middle income self employed may have little access to bank finance
- Micro-finance less expensive than money lenders
- Subsidy element, but issue of sustainability

## Provision by banks, credit unions or cooperatives

- Too risky and unprofitable for banks with depositors and shareholders
- In credit union *qard hassan* deposits and financing
- Credit unions and cooperatives can use a *wakala* or *musharakah* structure