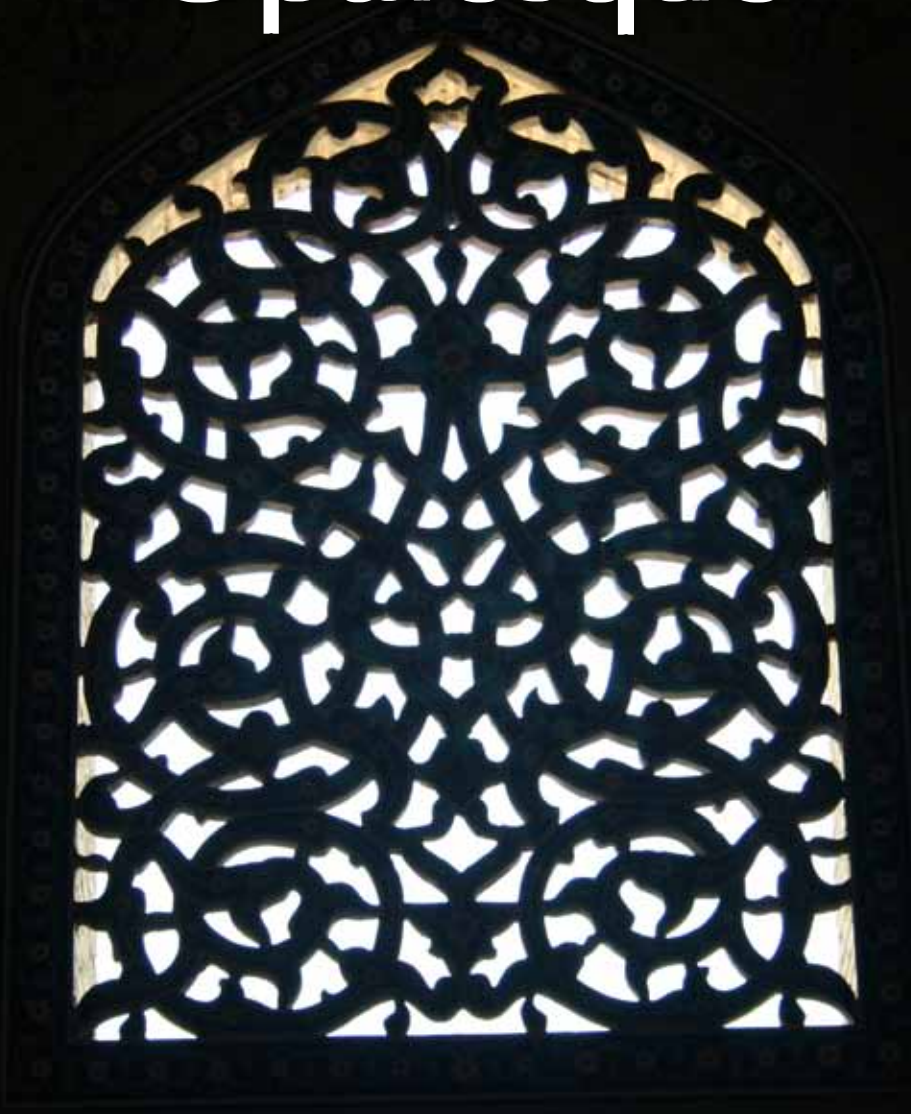


ISLAMIC FINANCE

INTELLIGENCE

šaffaafiyya Opalesque



Featured Structure

Maslaha and the Permissibility of Organized Tawarruq
Mohammed Khnifer

Lex Islamicus

Universality and Codification of Islamic Contracts
Khalil Jarrar, J.D.

Kulliyyah Korner

Measuring the Performance of Islamic Banks by Adapting Conventional Ratios
Ahmed Mohamed Badr-Eldin

The eight issue of Opalesque Islamic Finance Intelligence is here, the underlying thread uniting all the content for this month is looking at Islamic finance from a fresh and open perspective. This month's editorial outlines how Islamic finance is being developed/ introduced in new markets - and whether the industry's long term future is being mortgaged for some short term gains. This is complemented in the Featured Resource (with a list of studies that look at Islamic finance from a global or macroeconomic point of view) as well as the Industry Snapshot (with an analysis of the recent report by the IFSB, IRTI and the IDB).

The Featured Structure section welcomes Mohammed Khnifer as he takes a novel approach as to the permissibility of organized tawarruq. Lex Islamicus takes on Islamic commercial contracts as Khalil explores the issues of good faith and fair dealing. The Kulliyah Korner hears from Ahmed Mohamed Badr-Eldin and profiles his research on adapting conventional ratios to measure the performance of Islamic banks.

Furthermore, the Opinion Column hears from Edib Smolo, from the International Shari'ah Research Academy (ISRA), and his take on the future prospects of the industry. As part of our ongoing industry survey (The Islamic Window), Joy Abdullah provides an overview of the initial findings and some of the most striking signals from consumers.

Welcoming your comments & suggestions and a reminder that you can check the ever-growing archive of Opalesque Islamic Finance Briefing and Opalesque Islamic Finance Intelligence, all available free. In addition, we continue to expand the reach of our industry survey (see [reference link](#)) and appreciate it if you can help us disseminate it further.

Thanks & Regards,
Bernardo
Editor, Opalesque Islamic Finance Intelligence

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Photography by: Kelly Lemon, Robert Seabrook

Disclosure, Due Diligence & Death Spirals

By Bernardo Vizcaino, CAIA

Much has been said about what is right and what is wrong within Islamic finance, but every so often one must admit that while we scrutinize the current events and immediate developments (mostly in the short term) we tend to lose sight of the long term objectives of the industry (i.e. where it is heading). It is our hope that we can provide (and receive) constructive criticism while simultaneously promoting the positives that this industry has to offer. At times however it seems that not everyone is on the same page.

Not long ago I attended a particular industry event where various practitioners took to the stage to talk about Islamic finance (or to be more precise to sell us their services). The whole episode left me with much to think about in terms of who is representing Islamic finance. This wouldn't surprise the seasoned industry veteran (advertorials are an almost daily occurrence), but this takes on greater importance when we place this in the context of the new markets where Islamic finance is nascent and gradually opening up.

It begs the question - what are the priorities of these individuals/institutions? While I run the risk of being accused of naiveté (we all have to look after our business interests), it appears that their short-term financial/business gain takes priority at the expense of the long-term viability of the industry. A few things to consider:

Disclosure

Most of the presentations during this event had nothing new: sukuk, tawarruq, riba, Shariah boards, etc. What was conspicuously missing was any mention of some rather significant issues that should be discussed openly (if not candidly): but not a word about Nakheel, Blom Bank, OIC rulings, or the huge magnifying glass that is currently set on top of asset-based sukuk. Everyone has the right (and professional duty) to market their products and services, but we should encourage the disclosure of these various industry issues (at the very least to illustrate that we have learned from these bumps in the road). One thing that has remained constant in our discourse is the need to be open, frank, and practical in our comments and suggestions. Some will argue it is transparency and eventually this leads to something equally important: credibility.

Another aspect of disclosure pertains to which Islamic finance model (if any) does a particular country follow (again this is much more important for frontier markets where Islamic finance is just taking hold). Nonetheless, very little was shared in this regard but it comes down to whether a country follows one of these:



1) An umbrella SSB model - be that at the country level or at the industry level. The umbrella SSB has proven successful in Malaysia, Pakistan and Indonesia to name a few. Some of the key benefits are market recognition, volume of transactions and low-cost product development. Overall, the umbrella SSB is tasked with providing substantial direction (for instance in the shape of product standards and/or guidelines). This requires strong government - as well as political - support so it is not as easy to implement (but not impossible either).

2) An individual SSB model - whereby each market participant can choose their own path to compliance. This is usually illustrated when regulators take a hands-free approach and signal market participants to respond to 'market forces' when selecting the Shariah advisors or scholars whom they employ (in other words, no signal or direction is given except in the broadest sense). The individual SSB model can work well in offshore jurisdictions (say Luxembourg, Ireland, Jersey), where financial transactions are often not high in volume or are structured as pass-through vehicles (think special purpose vehicles and the like), or where Islamic finance remains a niche segment.

There is absolutely nothing wrong with either one of these, but they cater to very different markets and situations. One might work for Brazil while the other might work for Bermuda. Similarly, there are various exceptions such as the vibrant London and UAE markets (for the individual SSB model) which exhibit volume and visibility (although at the expense of higher costs). Again, it should be left to the policy makers to make these decisions, although what

Editor's Note

is necessary is for them to hear from all viewpoints (this is often not the case).

For the record, my preference is for the umbrella model mentioned above. It might be more elegant and cost-effective but what is far more enticing is how it engages the entire community of capital market participants. Hence Islamic finance is not privy to a few specialized funds houses, instead it is open to any financial institution that wishes to explore this 'alternative' finance. It simply makes more sense, especially when one deals with markets that contain significant capital market activity.

Due Diligence

There will always be a learning curve and we are not advocating placing an undue burden on service providers for them to educate governments, regulators or new entrants at large. These new market participants need to do their homework as well. Even a superficial analysis of the industry would yield many of the issues that have been highlighted earlier but unfortunately this is lost when hearing from industry experts that are advocating one point of view and this can have an undue influence on policy makers (some are often not the most industry savvy individuals out there). A balanced presentation of the industry would be most refreshing, alongside an objective digest from the audience. Hence due diligence is vital and it is a two way street - it is not just about asking questions (even if they are simple ones) it is about asking them to the right sources and on the overall quality of the answers.

To illustrate, the following points (or rather incomplete arguments) were made during the event:

- "Lack of Scholars": This bottleneck was argued both in terms of quantity and quality (and this might well be the case). This could support the use of an umbrella SSB; Nevertheless, the lack of Scholars argument is used to suggest that some Scholars are not up to standard and that preference should be given to the more 'progressive' ones. However this could make the bottleneck even worse. What needs to be addressed is the nurturing of new Scholars and/or ensuring proper training is given to the younger generation of Scholars.
- "Priority to issue sovereign sukuk": Again this is partly true, having a government issuance is a widely accepted positive (as it provides a pricing benchmark for the market), but this requires the private sector to follow suit (i.e. sovereign sukuk is followed by private issuances). This would also suggest that most would issue the same type of sukuk (cue product convergence), hence this would benefit tremendously from having an industry guideline and/or standard for such a product. Once again, these points were missed altogether.
- "More bang for your buck": The argument was made by another presenter that a sovereign sukuk or an educational program would provide maximum market visibility (not surprisingly he represents an educational service provider). Nevertheless, there are other equally noticeable initiatives: a country level SSB, publishing an industry roadmap, issuing a product guideline/directive. Any of these could be equally powerful signals.
- "Musharaka is a beautiful but impractical concept": This particular gem came from an actual AAOIFI board member, and I really don't have much to say except that if we are dissing musharaka while marketing organized tawarruq we have really lost sight of things. The truth is that one is not better than the other, but what we should advocate is a balanced approach.
- "Industry immunity to the global financial crisis": This point has been covered extensively by many but it was curious to see presenters quoting Singapore and Korea as examples of markets where Islamic finance has flourished. The fact is that Islamic finance has stagnated in the former and is barely taking off in the latter. They are both prime examples of the struggles faced by new markets (in terms of high costs, lengthy timelines, etc) and at the same time they can prove to be excellent examples of what actually is needed by market participants (Singapore's recent product guideline on Istisna financing is an acknowledgment that leaving things to 'market forces' does not always work).

Death Spirals

It is very clear, and overtly encouraging, that in the next few years we will have Islamic finance springing in various new markets. In some cases this will be at great expense to the first movers in those markets and various other service providers and market participants will follow suit. The risk is that these costs will be overtly high, the obstacles numerous and the benefits limited. Hence we might not see Islamic finance endure after this short honeymoon period.

I am not advocating spoon-feeding and/or baby-sitting these new entrants, yet we want to see the industry expand in a sustainable fashion. At the moment it seems that certain service providers are engaged in short term tactics at the expense of long term viability. In fact some seem to have a love affair with complexity (the more moving parts the better), giving priority to SPV-rich instruments and promoting commission-laden structured products, while simple and perhaps more efficient products are sidelined. A more pragmatic approach should be expected, especially from those individuals who we deem as guardians and representatives of the industry.

Your feedback and comments are very important to us, please feel free to contact the author [via email](#).

The Macro Perspective

 **Blogger** [As Featured in the Islamic Finance Resources Blog](#)

This is an overview of various papers on global and/or regional issues as pertaining to Islamic finance from a macroeconomic or structural point of view. Featured below a short selection of some of these papers:

Internationalization of Islamic Financial Institutions: Challenges and Paths to Solution

By Samy Nathan Garas, Al Baraka Center for Islamic Economics

Islamic Financial Architecture: Risk Management and Financial Stability

By Tariqullah Khan, Dadang Muljawan

Islamic Finance: Global Financial Stability IFSB, IRTI, IDB

Islamic Financial Services Industry Development : Ten-Year Framework and Strategies IRT1, IFSB

Towards Developing a Successful Islamic Financial System by Professor Sudin Haron, KLBS

The development of Islamic finance in the GCC

By Professor Rodney Wilson, The Kuwait Programme on Development, Governance and Globalisation

Regulatory challenges posed by Islamic capital market products and services

By Professor Rodney Wilson, IOSCO Task Force on Islamic Capital Market

Maslahah and the Permissibility of Organized Tawarruq

By Mohammed Khnifer

Mohammed Khnifer is regarded as part of a 'second generation' of Islamic banking practitioners who have a solid academic background in Islamic finance. He is a holder of an MSc in Investment Banking & Islamic Finance from Reading University and is a Chartered Islamic Finance Professional (CIFP) from INCEIF. He is one of the most prolific and well-known journalist specializing in Islamic Finance today. For the past six years he has been in charge of the editorial content for the Islamic Banking section of Al Eqtisadiyah (Kingdom of Saudi Arabia).

The principle of Maslahah (public interest) may be used to determine the desirability of a particular Shariah interpretation in such matters as the use of Murabahah-based structures in Islamic finance.



Respecting, understanding and implementing Shariah are the backbone of the trillion dollar Islamic finance industry. Shariah scholars are deemed to be the gatekeepers for the Islamic finance sector. With their guidance, legitimacy can be fulfilled and confidence in the industry achieved. While Shariah advisors themselves come from four prominent Sunni schools of thought, or fiqh, they together attempt to achieve Ijtihad and Maslahah, that is, finding common ground over their respective rulings on some of the controversial financial instruments of our time.

Within this framework we argue the need of favouring Maslahah with Murabahah-based structures in spite of the landmark 2008 ruling by the OIC (Organization of Islamic Countries) Fiqh Academy, a ruling that declared organized Murabahah (Tawarruq) as non-compliant with the principles of Shariah.

Maslahah can be defined as the “unrestricted” public interest, which is one major component of the framework of Islamic law, or Shariah. The objectives of Shariah are commonly defined in Imam Ghazali’s classification of “unrestricted” public interest in terms of the protection and preservation of religion, life, intellect, property and progeny (Dar, 2009). Thus, Islamic financial products based on (the objectives of) Shariah must attempt to enhance “unrestricted” public interest.

In reality there is a disagreement between liberal and conservative scholars over the necessity of applying Maslahah on some Islamic banking products. This disagreement (i.e., on when to apply Maslahah with specific products such as Murabaha) has moved from closed doors meetings to the public, resulting in creating the biggest Shariah risk this industry has ever seen.

Featured Structure

In 2009, the OIC, and through its powerful line-up of senior Shariah scholars, sent shock waves across the industry. The OIC Shariah committee, comprising more than 50 scholars, of which few are directly involved in Islamic banking, disregarded the public interest of Islamic financial institutions by declaring organised Tawarruq impermissible as it has elements of interest-based lending. So rather than clarify issues and state what steps needed to be taken in order to ensure compliance, the entire practice was at once ruled non-compliant (Firoozye, 2009).

Nonetheless, it is imperative to hear their justification over the ruling. The OIC considered it a “trick” to get cash now for more cash paid later, which is prohibited in Islam. While it may be considered a hiyal (legal stratagem or ruse to circumvent Islam’s most basic prohibition on riba) the combination of purely legal strategies as a means of arranging financing was sufficient to legitimize it (under very specific circumstances according to the majority of jurists) (Firoozye, 2009).

What makes this ruling especially injurious is that Tawarruq and commodity Murabahah have become essential financial instruments in wholesale banking. The OIC ruling implies that the banks are not really interested in delivery of underlying assets, which in any event has questionable overlapping ownership by brokers.

To illustrate, Muddassir Siddiqui (2009) defines organised Tawarruq as the purchase of commodities from local or international markets and their onward sale (on a deferred payment basis) to the customer. The seller then (as agent for the customer) on-sells the commodities (to a person who must be different from the first supplier) for a price that is lower than the deferred payment obligation owed by the customer. The result is the customer gets a cash amount for his required business or personal purposes.

The OIC scholars made it clear that even though organized Tawarruq may comply with the letter of Sharia, it does not comply with the spirit of Sharia. That is, commodity Murabahah is legitimate because it involves the sale of assets, rather than a lending operation. But what if the assets are just an entry to the broker’s book? It begs the question: is anyone interested in the actual assets?

Firoozye (2009) capitalizes on this point by saying that banks themselves are not generally equipped to take delivery of tons of palladium or gold; rather, they use the services of brokers & custodians. These same custodians can potentially make all necessary changes of title in milliseconds before the price of the underlying can actually change, and before either the bank or customer might take much in the way of market risk.

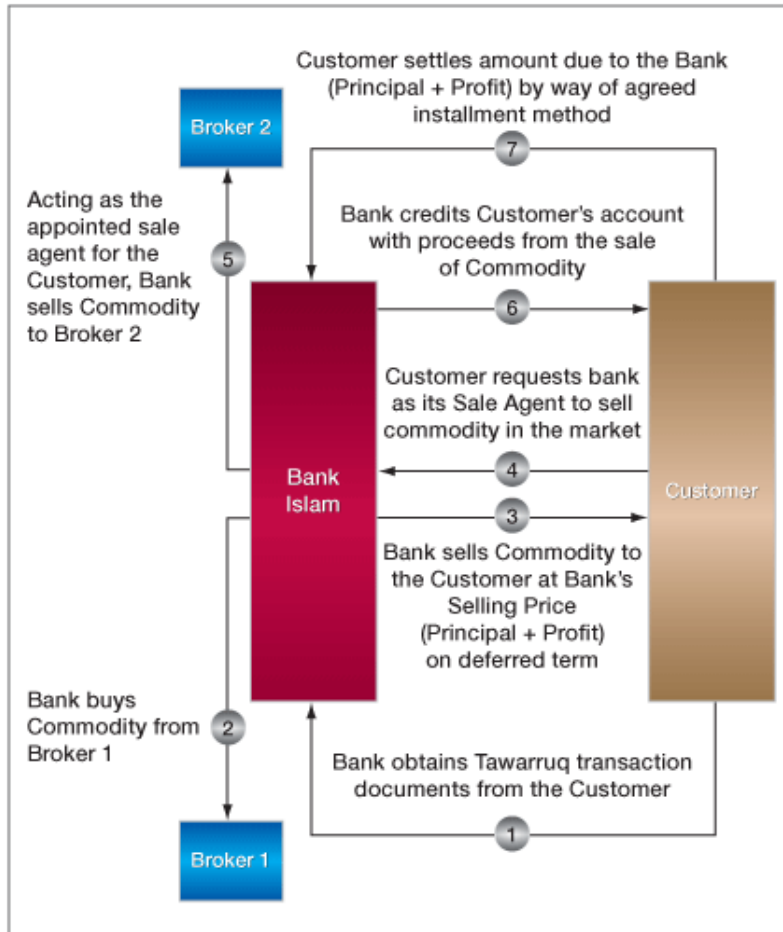
Before embarking on the argument favouring Maslahah and ignoring the OIC ruling, one should take a profound look at the wide utilization of Murabahah within the Islamic banking industry. It is the basis of many credit card transactions (primarily in the GCC region). It is used in covered drawings, in top-up facilities, in mezzanine financing, in liquidity management and in working capital finance (among other things) (Firoozye, 2009). Furthermore, modern Shariah supervisory boards (SSBs) have engineered and approved a host of hybrid nominates, using a single nominate such as Murabahah in different configurations (such as parallel Murabahah, reverse Murabahah, back-to-back Murabahah, and reverse parallel Murabahah contracts) (DeLorenzo, 2007).

Having witnessed their young industry being shaken up with the OIC fatwa, a group of prominent scholars, led by Nizam Yaquby, stood up and challenged the establishment’s ruling. These scholars went public and appealed to the principle of Maslahah. They made an argument that commodity Murabahah is the backbone of the industry and it should be legitimized on the basis of social usefulness or social needs of the Islamic Ummah.

To compliment the above view, other observers profess that OIC scholars had a narrow view on the usage of commodity Murabahah. That is, the product can be used to serve customers in the retail banking. Further, the product itself can be used in the wholesale banking. OIC fatwa on the impermissibility of organized Murabahah takes into consideration that this product is used mainly in the retail division. Thus, it ignores the use of this product as a liquidity management in the wholesale banking division. Islamic banks can not function properly without inter-bank transactions. Banks use Murabahah to borrow and lend from each other from as short as overnight to as long as one year and even more. Murabahah is a fundamental element in the liquidity management process. If you condemn Murabahah as non-Shariah compliant, then the Shariah inter-bank market might collapse, forcing these banks to channel their excessive funds to the conventional system, which would essentially be the end of Islamic banking as we know it. In addition to that, Murabahah is one of the Lender of Last Resort facilities. All in all, the benefit of continuing using Murabahah contracts, despite some Shariah reservations, outweighs the call for its impermissibility as they fulfil a useful purpose.

Featured Structure

Organized Tawarruq Structure Diagram:



Source: Bank Islam

Organized Tawarruq Step by Step

1. The customer applies financing product based on Tawarruq concept from the Bank. Bank obtains Tawarruq transaction documents from the customer
2. Bank will buy the commodity at London Metal Exchange (LME) through Broker 1
3. Under the Murabaha contract, Bank then sells the commodity to the customer at Bank's Selling Price (Principle + Profit) on deferred payment term
4. Under the Wakalah contract, customer requests Bank to sell the commodity in the market
5. Acting as the appointed sale agent for the customer, Bank sells the commodity to Broker 2
6. Bank then credits the Wariq (proceed) from the sale of commodity to the customer's account
7. Finally, customer pays amount due to the Bank (Principal + Profit) by way of agreed instalment method

How can Islamic financial institutions manage the risk of non-compliance with Shariah ?

Over the past decade the Islamic finance industry was increasingly exposed to the risk of creating banking products that might be deemed not in compliance with established Shariah principles, thus losing customers and profits in the process. This is what we now term Shariah compliance risk.

A heated debate among practitioners over some of the more innovative products (which sometimes mimic conventional ones) led to the creation of the term "Shariah risk." In recent years banks and other Islamic finance institutions (IFIs) have become increasingly sensitive

Featured Structure

to Shariah risk as more and more respected Islamic scholars began to openly criticize certain types of Islamic banking practices (Firoozye, 2009). Indeed, the short history of Islamic finance is embedded with anecdotes of high-Shariah-risk products such as commodity Murabahah and to some extent asset-based Sukuk.

Recognizing and mitigating Shariah risk, which is sometimes not understood very well even by some industry experts, is not especially different from managing market risk, credit risk, liquidity risk and operational risk. Shariah supervisory boards (SSBs), which certify finished products with a fatwa, play a vital role in managing such risk. Also critical to managing Shariah risk is the active role played by an IFIs Chief Risk Officer (CRO). The concept of mitigating Shariah risk rests jointly on the shoulders of the CROs and SSBs. With the increasing recognition of Shariah risk among IFIs over the last decade, there have been concerted efforts to understand, analyse and control Shariah risk within every jurisdiction that Islamic finance is active.

Shariah risk management is identical in process and procedures to general risk management, of which there is an abundance of professional reference works to refer to for guidance. Basel II, the ultimate risk-management system, is now nearly universal in identifying, measuring, and protecting against any and all risks that affect a bank's operations.

Shariah risk management begins ex-ante from the actual products that ultimately receive fatwa. It can be controlled early in the development of any new Islamic product or service. It starts prior to SSB certification, i.e., at the stage when a bank is engineering a new product and designing its relevant contracts for later approval by the SSB. The Shariah compliance process for any given product comprises many steps, such as research, design, modelling, legal analysis, fiscal analysis, market analysis, and other steps (Laldin, 2009). Within these early stages of development, an IFI averse to Shariah risk is expected to consult with members of its SSB long before the product is presented for SSB approval. It is hoped that Shariah risk can be identified at the early stages of product development. For example, Shariah risk could involve issues like improper structuring that does not meet Shariah tenets, or a haram process of implementing the product in the market, or miscommunication by people who are involved in the whole process from product initiation until the post implementation product review (Ibrahim, 2009).

Furthermore, at the ex-ante Shariah compliance stage, a developer may incur considerable costs for a new product, including costs directly related to Shariah compliance and, in order to retain first-to-market status for the business, will insist on keeping the fatwa out of the public eye for a time (DeLorenzo, 2007).

Shariah risk is also managed ex-post compliance, i.e., after a product is approved and launched. Shariah risk management involves, at this stage, continuous monitoring and testing of the rationale originally used to issue the product's fatwa. As we know, opinions can change within the community of respected Shariah scholars, and when enough opinions change there can be a sizeable shift in attitude toward one type of product or service. Staying close to the community of Shariah scholars and their professional dialogue is critical to proper Shariah risk management.

Some industry observers believe non-compliance risk is more likely with ex-post shariah compliance. In response to such potential risk, many Islamic banks try to strengthen their Shariah risk management, i.e., controlling the functions where identification and assessment of Shariah risk would be systematically monitored and controlled to avoid non-compliance of Shariah (Ibrahim,2009).

Shariah compliance is a shared responsibility, where both CROs and SSBs must be involved ex- and post-compliance. All IFIs are encouraged to set up dedicated Shariah compliance risk divisions (Ibrahim, 2009). Within this division, there should be a Internal Shariah Compliance Unit (ISCU) which comprises a Shariah Compliance Officer and staff well trained in and with knowledge of Islamic finance. To compliment the ISCU role, the Internal Shariah Review Unit (ISRU) should operate like other typical internal audits, but report to the SSB (Hussain, 2009). The objective here is to provide checks and balances in ensuring all operations of a full-fledged Islamic financial institution are Shariah compliant, achieved through an effective Shariah review and audit (Ibrahim, 2009).

It is often the case that Shariah advisors possess little knowledge of advanced accounting and auditing. In some cases, Shariah auditors are recognized as a second line of defence in the process of managing Shariah risk. As an example, Aznan Hasan, the well-known Malaysian scholar, demonstrates how these auditors once managed to uncover non-Shariah practices by brokers on the London Metals Exchange (LME). In his interview with the Saudi newspaper Al Eqtisadiyah (Khniifer, 2009), Hasan exposed what he termed "Fictitious Murabahah" activities undertaken by some LME brokers. He discovered the frequent overlapping ownership of underlying assets. After a Shariah audit he illustrated how commodity broker (A) when selling a commodity, involved multiple and simultaneous ownership, meaning one particular commodity was sold to more than one buyer (Khniifer, 2009). Indeed such non-Shariah activities may not have been discovered and eliminated if it were not for the Shariah auditors.

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Do these risk management methods lead to desirable outcomes in line with the public interest?

Given a heightened sensitivity among banks to be socially responsible generally, whether Islamic or not, it appears that a bank can manage Shariah risk and try to simultaneously attain Maslahah. Every bank has what we term its own internal micro-Shariah risk. That is the risk that can be confined and eliminated through the process of ex ante and post-shariah compliance described above. Hence, if a bank properly applies Shariah risk mitigation, then most risks will likely be eradicated during the process to create Sharia-compliant products, and then during the management and administration of those products.

Like a canary in a coal mine, Shariah risk management is meant to spot risks before they occur, or at least before they become a problem. The result of a committed effort to plan and implement a Shariah risk management program is directly and indirectly a public good. Not only are bank customers enjoying increased protection from non-compliant products and services, they are equally protected by a bank whose own capital is better protected from failures in the risk management process. There is in fact no difference in the outcome of good Shariah risk management than credit risk, information risk, property risk and regulatory risk management. Thus, Maslahah is definitely being served by banks that adopt methods to manage Shariah risk as a fundamental part of overall risk management.

The correlation between managing the risk and Maslahah can be appreciated more if we assume a scenario where a bank fails to mitigate such risk. Just because other banks are better or worse in credit management, other banks can be better or worse in Shariah risk management. Nobody wants to see an Islamic bank violating Shariah principles as this will create chaos and confusion, which ultimately erodes shareholder capital and the bank's ability to function efficiently. For example, if a Muslim community has concerns regarding religious compliance of a banking product, it will definitely reflect on the other related products in the same category, thus affecting the profitability of the bank. The consequence of such spillover is that depositors will withdraw their funds, as they take this issue just as seriously as rumors of bad credit. With that in mind, it is noteworthy that any bank that prudently and proactively manages Shariah risk, and better than other banks, is performing a public service as it is increasing customer confidence. Therefore, ensuring the complete implementation of Shariah risk management can lead, from the micro-level on up, to a desirable outcome.

At the same time, banks need to simultaneously consider macro-Shariah risk. This risk arises when an established entity such as the OIC issues a fatwa which might lead customers think that a bank's already issued fatwa on certain product has been overturned by a higher authority. No bank can overturn an OIC ruling on Tawarruq, for example. This controversial OIC ruling exposed Islamic banks to the most significant Shariah risk in recent history, significant as it had the potential to nullify hundreds of billions of dollars of yearly transactions (Firoozye, 2009). In this scenario, a bank formerly comfortable with its own Shariah risk management system, and the interaction of its CRO and SSB in managing the bank's internal Shariah risk, would find itself potentially losing large volumes of formerly stable revenue because an outside authority, such as the OIC or AAOIFI (the Accounting and Audit Organization for Islamic Financial Institutions), delivered a ruling that at once undermined one major form of its conventional Islamic banking. To illustrate such macro Shariah risk, Muhammad Taqi Usmani, chairman of the AAOIFI board of scholars, brought the Sukuk industry to its knees when he declared in early 2008 that about 85% of Sukuk in the GCC region did not comply with Islamic law because of a then-standard repurchase undertaking agreement. Following his pronouncement, sales of sukuk plunged to US\$13.9 billion in 2008 from a record US\$31.0 billion a year earlier, according to Bloomberg's data (Khniifer, 2009). Any bank that had counted on revenue from new Sukuk issuances would have been sorely disappointed.

Being now aware of the potential magnitude of losses from macro-Shariah risk, bank managements must establish contingency plans in order to counter or minimise the effect of such risks. In order to manage such risks prudently, banks need to measure exposure to macro Shariah risk on an ongoing basis. This requires both a bank's CRO and its SSB to proactively maintain close tabs and constant surveillance of the body of Shariah scholars and organizations that make rulings that might affect a bank's operations.

The business of risk management at banks is well established, and there is abundant literature available to support a conventional, acceptable risk management system inside any bank. Just as CROs constantly evaluate "what if" scenarios, mapping out for example the potential loss of customer deposits if the failure of a certain product or service causes reputation risk, so can CROs duplicate this process for Shariah risk, both from internal and external sources.

In conclusion, a desirable outcome can be achieved through managing Shariah risk at the micro level, but Islamic financial institutions also need to include macro Shariah risk in their planning. The results will be a stronger, more stable banking enterprise, which over time fulfils the public good.

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In Good Faith

By Khalil Jarrar, J.D.

Khalil has a diverse educational and professional experience in both Information Technology and International Law. Working as a senior IT consultant for a range of multi-national corporations, he holds a law degree from the US (J.D.) in addition to International Law training at the Hague Academy and Strasbourg International Institute of Human Rights. He is a Bi-lingual and Bi-Cultural Arab-American with extensive knowledge of the MENA region. Khalil currently hold a position as an International law consultant for a Geneva based foundation.



Imagine, in a perfect world, that you found an Islamic bank that is fully compliant with Shari'a law. The Jurists have done their homework; no loopholes are to be found, and created instruments that meet your high moral standards. The choice is yours, said the bank manager, we have developed instruments in accordance with Shari'a law. These instruments are easy to understand and our bank is strictly Islamic therefore funds are not commingled with Riba money. We only implement sound investments with low risk or uncertainty avoiding Gharar. You narrowed down your choices to modern Murabaha or a diminishing Ijara, and for an added assurance the bank manager states that a local index is used to calculate the profit, not LIBOR. You contemplate these options and you tell the bank manager that you are ready to close the deal. Not too fast, the bank manager said, we have to exchange promises today, nonbinding he adds, and we will see you tomorrow to sign a contract.

Assuming you are a novus buyer and do not know what a contract is, so you rush home to your computer and lookup few definitions of what a contract is and you finally find a definition that sounds simple enough to understand; A contract is an agreement between two or more entities to do, or to refrain from doing, a particular thing in exchange for something of value. Contracts generally can be written, using formal or informal terms, or entirely verbal. If one side fails to live up to his/her/its part of the bargain, there's a "breach" and certain remedies for solving the differences are available (see [reference link](#)).

You contact a lawyer friend to validate your newly acquired legal knowledge and she adds, to your surprise, the most important element of a contract is not mentioned in the contract so be careful. How can the most important element of a contract not be mentioned you ask? She explains that it is the implied covenant of good faith and fair dealing, a general assumption of the law of contracts, that people will act in good faith and deal fairly without breaking their word, using shifty means to avoid obligations, or denying what the other party obviously understood, she replied.

This is an Islamic bank you answered and the principle of good faith is required by the Qur'an. As stated: "Woe to the fraudulent dealers. "Good faith is always presumed as long as the contrary is not proven." Not to confuse you the lawyer adds that good faith is universal. The concept of good faith is considered especially important in both the common law tradition and the lex mercatoria (international customary law) and, as a result, was codified in the 1980 Convention of Contracts for the International Sale of Goods or CISG (see [reference link](#)).

Law and religion throughout history have been trying to create a balance in protecting contracting parties. They both agree that both parties to the contract must be able to have an arms length negotiation, if one party has a major advantage then the contract is voidable and classified as a contract of adhesion. With this note from your friend, sounding more confused than before, you end the phone call, go to sleep and walk to the bank the next morning. You sign a one page contract that includes no excessive penalties in case of default on your end.

But wait! It is not a perfect world we live in nor there an Islamic finance Utopia, so wake up and face reality. As I mentioned in previous articles (see [reference link](#)), thumping through samples of Islamic finance contracts, most are long enough to earn you a law degree by the time you are done with reading it or trying to comprehend it. Some of the offered instruments are confused and confusing not to mention excessive remedial fines and the tilted playing field favoring the bank over the customer. The future of modern Islamic finance globalization relies on the short market history. No matter how long or brief the contract terms are, the implied covenants of good faith and fair dealing are paramount to the enforcement of such contracts. Doing some market research and interviewing few customers who bank with Islamic financial institutions made me realize that such customers know very little about the basic principles of Islamic finance. When pressed, they answer, I do it in good faith and the burden is on the bank to be accountable before God!

Most patrons of Islamic finance institutions presume that avoiding major prohibitions in Islam deems a contract valid. The prohibitions, against *riba* and *gharar*, have led jurists of Islamic law to focus on the objective elements of the contract, such as its implementation and its subject matter, instead of more subjective elements like intent. Keeping this in mind, there are two rules: (1) property in the object of sale passes as soon as the contract is concluded (after offer and acceptance) and; (2) There cannot be unfair exploitation. Speaking of exploitation, here are a couple of examples of such practices: An Islamic bank that has branches through out the Arab world finances appliances on one condition; a cosigner is required for every \$500 of equipment purchased to guarantee the client would not default. If leaving a person who is pressed for need to go find a minimum of two cosigners to buy a decent appliance is not exploitation, what is?

The Holy Qur'an equates unjust dealing with *Riba*, verse 278 of Surah Al- Baqarah states: "O ye who believe! Fear Allah and give up what remains of your demand for *riba*, if ye are indeed believers." and verse 2: 279 says "If you do it not, take notice of war from Allah and His Messenger. But if ye turn back, ye shall have your capital sums. Deal not unjustly and you shall not be dealt with unjustly. Another example is requiring two cosigners who are bank customers for a home purchase, although the home is still technically mortgaged to the bank. The same guarantee is never offered for the loan applicant in case the bank defaults or goes out of business. Maybe the inadequacy in my perception to see fair dealings such practices or is it?

Not to generalize, the notion above does not mean that all *Islamic* finance houses apply unconscionable practices. I am mindful of many banks that employ the best and the brightest to perfect the process of producing fully *Islamic* compliant instruments with an audit mechanism to perfect their application. The fact remains that a substantial minority is tainting the image of the conformant majority, abusing the trust of their clients under the veil of Islamic banking. The time is now to create an auditing entity that certifies any institution that claims to practice Islamic laws with an auditing arm to protect their clients who bank with them in good faith. The Accounting and Auditing Organization for *Islamic* Financial Institutions, has come a long way to create standards, however such organization needs to have the force of law to certify and audit existing and new institutions to conform and adhere to acceptable standards and best practices of *Islamic* finance.

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Measuring the Performance of Islamic Banks by Adapting Conventional Ratios

By Ahmed Mohamed Badr-Eldin

Ahmed is an Assistant Lecturer at the German University in Cairo (GUC), he graduated from the GUC with Double Majors of Finance and International Business and took his Masters in Economics with a thesis in Islamic Finance. He has been working as a teacher for several years and recently published his paper on “Measuring the Performance of Islamic Banks by Adapting Conventional Ratios” (see [reference link](#)).

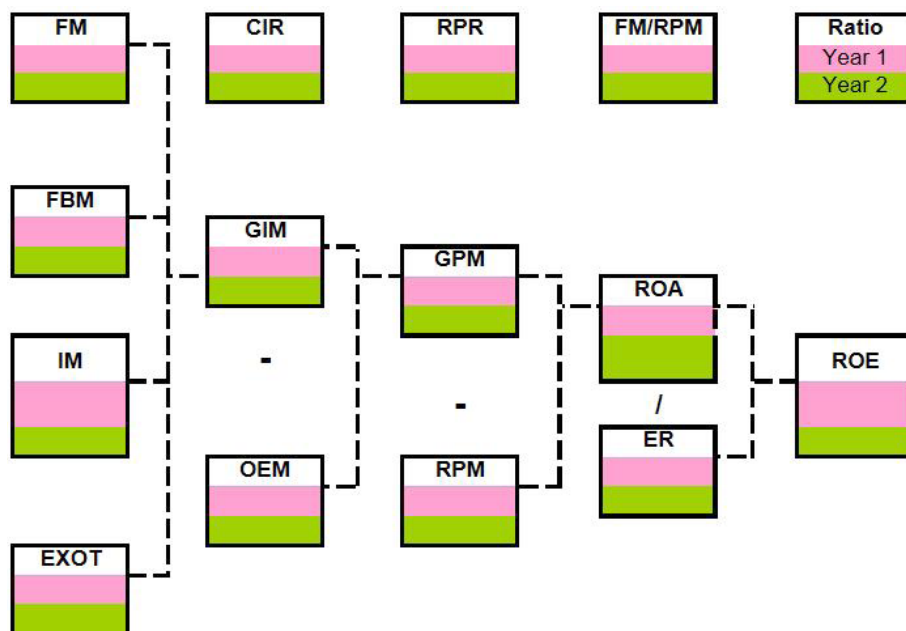
Before discussing the paper I would like to highlight that I have witnessed the huge potential of students in the Finance majors with special focus on Islamic Studies but at the same time almost all my students have highlighted these two significant barriers: The first is that they have a very hard time finding resources and information about Islamic Finance and cannot find any centers or companies that are able to help them. Secondly, they feel that their research and work in the Islamic Finance area is useless because there are no well known journals that can communicate their findings to the practical world, since most of the research around Islamic Finance is very practical and can be applied, but “there is no one to listen”.

A key driver for developing this paper was to gain a better understanding of the Islamic Banking sector, as I had already realized that the industry is still growing and is missing many aspects which have been covered in the conventional banking sector. Beginning with Performance Measurement, I decided that Islamic Banks need their very own custom-made performance measurement tools in order to have better insights and greater understanding of how these banks (and their balance sheets) are performing and how to compare them, which I believed would be very useful academically for more progress in studying the sector, identifying how they are performing and finally in comparing it to conventional banks. Similarly, it would be very useful for the actual mainstream users (whether bankers, government entities or even financial analysts) in order to have a more solid basis for making their decisions and investment calls.

The abstract of the paper provides a brief but concise summary of the complete paper: “One consequence of the current financial crisis is that many countries began to reevaluate their financial systems and recognize its flaws and drawbacks. They also began the search for alternative systems for their economies; one of the proposed systems is the current Islamic financial model. This model is still in its infancy and many modifications and additions are required. It also lacks the necessary financial performance measurement tools similar to those used by conventional banks for managers and investors alike. This paper evaluates this lack of performance measures. It then adapts a currently applied ROE Analysis Tool used in conventional banks, to the currently established model of Islamic Banks and tests its applicability and evaluates its usefulness. The findings suggest that such an adapted model would be quite successful for use in Islamic banks and would offer much better analysis and basis of comparison within the Islamic financial system. It also suggests that much of the previously measured performance of Islamic Banks is unsound and should be revised for accuracy and reliability because of the flawed methods used for measurement in the first place.”

Furthermore, the attached graph provides an illustration of the process that is developed in the paper itself, outlining the tracing procedure used to adapt the Return on Equity of Islamic banks in order to make them comparable to conventional banks. When these changes are taken into consideration then “it becomes possible to use the Adapted ROE Scheme to measure performance of Islamic banks fairly and accurately without any loss of information, discrepancies in intended meaning or incorrect categorization of funds, deposits or income”.

Explaining the Tracing Procedure of the Adapted ROE Scheme



Ratios and Abbreviations used in the Adapted ROE Scheme

Ratio	Abbreviation Used		
Financing Margin	FM	Gross Profit Margin	GPM
Fee-Based Margin	FBM	Risk Provision Margin	RPM
Investment Margin	IM	Return on Assets	ROA
Extraordinary and Other Income Margin	EXOT	Equity Ratio	ER
Gross Income Margin	GIM	Return on Equity (Pre-Tax)	ROE
Operating Expenditure Margin	OEM	Cost-Income Ratio	CIR
		Risk Provision Ratio	RPR

It must be said that there were several obstacles faced (and can be found in the limitations section of the paper) which mainly revolved around the diversity in accounting standards used by Islamic banks across the world, as well as the actual sub-items presented in the financial statements. These need to be more uniformly prepared in order to ensure a complete and transparent understanding of the financial positions of these banks. Another great obstacle was the availability of data on Islamic banks, most of the data collected has been downloaded directly from each and every bank’s annual report and website. Such a method is very time consuming (even if ensuring complete accuracy and liability of information falls on the banks themselves and not on some other database supplying the data), as well as limited in scope as not all banks have published their statements online, or might not have enough historical reports available for download.

I believe a good step now for Islamic banks would be to first adopt the Islamic Accounting Standards in their preparation of financial statements, this can be followed by more accurate performance measurement which can in turn allow people to make more secure investment decisions which might show Islamic Banks to be much more superior to other investments and will definitely improve and prosper the sector and allow it to take its real and significant position among the global banking sectors.

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Islamic Finance Practices at the Crossroads

By Edib Smolo

Edib Smolo is Associate Researcher at the Islamic Banking Unit, International Shari'ah Research Academy (ISRA) for Islamic Finance. He obtained his undergraduate double-degree in Economics and Islamic Revealed Knowledge with Honors as well as Master in Economics from International Islamic University Malaysia (IIUM), Malaysia.

Prior to joining ISRA, Mr Edib worked for an insurance company in Bosnia and Herzegovina and at the same time he was Assistant Professor at Faculty of Economics, Sarajevo School of Science. He participates in conferences and seminars related to economics, business and finance. He published several papers on Islamic microcrediting, economics, and finance. His interests and areas of specialization are in Islamic banking and finance, microcrediting, fiqh muamalat, risk management, and Islamic capital market products, among others.

Islamic finance is at the crossroads. On one side the global economic crisis provides a golden opportunity for the Islamic finance industry to establish itself better and prosper due to its conservatism towards speculation (maysir) and interest (riba). However, on the other side, the Islamic finance industry is also faced with numerous challenges.

A recent legal ruling in Malaysia regarding the validity of BBA (bay' bithaman ajil) is one example. Initially, the High Court of Malaysia ruled out that ten Bank Islam Malaysia Bhd (Bank Islam) contracts were structurally faulty and that defaulters did not have to pay more than the original financing amount, thus depriving Bank Islam of the profit arising from the transaction. Following the appeal filed by Bank Islam, the Court of Appeal held that the BBA facility offered by Islamic financial institutions is valid and legally binding. This decision was unanimously made by judges of the Court of Appeal, namely Datuk Md Raus Sharif, Datuk Abdul Hamid Embong and Datuk Ahmad Maarop, on 31 March, 2009.

The said decision reaffirmed that Bank Islam's practices in relation to BBA contracts are Shari'ah-compliant and valid. The Court of Appeal also reiterated that a BBA contract is a sale transaction and therefore, it must not be compared to a loan transaction. The unanimous decision in the appeal in the Bank Islam Malaysia Bhd



v Ghazali Shamsuddin & two others, and nine other cases would mean a certain relief to local Islamic banks that had earlier feared a potential avalanche in defaults of Islamic contracts, especially for home financing. Although the Court of Appeal approved the practice of BBA, this practice is still overshadowed with a lot of issues, the most important being its application of bay'inah (buy-back) contract.

In addition to this case in Malaysia, a recent ruling by the OIC Fiqh Academy, in its 19th session held in Sharjah, United Arab Emirates from 26-30 April 2009, against organized tawarruq practices delivered another shock to the Islamic finance industry. According to the Fiqh Academy, organized tawarruq is "when a person (mustawriq) buys merchandise from a local or international market on a deferred-price basis. The financier arranges the sale agreement either himself or through his agent. Simultaneously, the mustawriq and the financier execute the transactions, usually at a lower spot price." Reverse tawarruq, they argued, is similar to organized tawarruq. However, in this case, the mustawriq is the financial institution, and at the same time it acts as a client.

In its Resolution 179 (19/5), the Fiqh Academy stated that "it is not permissible to execute both tawarruq (organised and reversed) because simultaneous transactions occur between the financier and the mustawriq, whether it is done explicitly or implicitly or based on common practice, in exchange for a financial obligation. This is considered a deception, i.e. in order to get additional quick cash from the contract. Hence, the transaction is considered to contain the element of riba."

Raising issues about current practices within the Islamic finance industry should be welcomed and addressed with the true intention of improving them. The time is ripe for Islamic finance to step forward and find its way out of the chains of the conventional finance domain. An attempt should be made by both practitioners and scholars to come up with genuine products that are free from controversies and based on Islamic principles stipulated within Islamic law, Shari'ah. Current issues and problems with BBA and tawarruq arise from their similarity to conventional practices explicitly based on riba. Many scholars as well as sincere practitioners see them as ruses (hila) to provide legal justification for interest.

To continue replicating conventional products and practices will lead to the convergence of Islamic finance with the conventional sector. If this is the case then Islamic finance is doomed to fail, as it will be following in the footsteps of its stepmother, interest-based financing. Islamic finance, being currently a part of a larger, more sophisticated and better established conventional system, will face huge resistance if it tries to distinguish itself and change the rules of the game. The recent resolution issued by the Fiqh Academy is going to put more pressure on Islamic banks, as they will have fewer instruments for their operations. At the same time, it will put more pressure on them to come up with a new product(s) that will (hopefully) be Shari'ah-based so as to avoid further misunderstanding and problems.

One thing is for sure: as long as Islamic finance is dressed and breast-fed by the conventional financial system and covered by an artificial "hijab" it will not be able to realize its full potential until and unless it frees itself of the conventional system's chains. Both the financial crisis and recent fatwas are timely in order to awake the Muslims and provoke new solutions for the financial industry. Shari'ah is (and should remain) a backbone of Islamic finance, and it should be better merged with the practices of Islamic financial institutions. Without solid Shari'ah backing, Islamic finance will be just one more market player bound for failure.

Your feedback and comments are very important to us, please feel free to contact the author [via email](#).

Preliminary Findings

By Joy Abdullah

Joy Abdullah, Brand Strategist, has more than 20 years of experience across ASEAN & the Indian sub-continent in developing and managing national, regional and international brands in a wide variety of industries covering Islamic Financial services, tourism, B2b Halal, telecommunications, beverages, real estate, tobacco, hospitality and healthcare.

In the March issue of Opalesque Islamic Finance Intelligence (“The Islamic Window: Consumer Perception and Market Research in Islamic Finance”) we presented a rationale as to why a market survey across consumers would help the Islamic Finance Industry, specifically:



“there is scant research available on the consumer perception and understanding of Islamic finance, from product specifics (i.e. what is ijara?) to the overall perception of the industry’s value proposition (i.e. do consumers actually care?). Such critical analysis would be invaluable to the industry, specifically as input for the design of Islamic finance products that serve a real need amongst retail consumers. Such consumer perception studies could provide the Islamic Finance industry with a platform to:

- I. Develop basic financing products adhering to Shariah, which are applicable across geographical boundaries, thereby providing globally-operating IFI’s a common product pool to use across markets and jurisdictions.*
- II. Support global standards as opposed to country-specific or even company-specific SSB certification/approvals.*
- III. Encourage the industry to innovate on areas of brand identity through service improvements, technology inputs and consumer wealth development.”*

We launched the survey (see [reference link](#)) in a collaborative manner and with a concerted effort to understand the level of awareness and overall understanding of consumers towards the Islamic finance industry (and its products and services). In this regard the survey is a continuous effort, a sort of consumer ‘barometer’ as to how Islamic finance is viewed and accepted. It could even be argued that once we have built enough historical data we can then create an Islamic finance ‘confidence index’ or even a Muslim consumer ‘confidence index’, or we would equally welcome a more impartial body to develop it using a far more rigorous scientific approach.

Nonetheless, we zoom in on our initial findings. We expect to broaden the geographical mix as the survey matures, although the current mix is very healthy: the majority of responses come from the UK (13%), India (11%), Pakistan (10%), the US (10%), Kuwait (7%) and Malaysia (6%). While these represent more than half of all respondents we aim to expand the survey in other markets. The only demographic bias we observe that needs to be addressed is the male/female response rate (currently 84% to 16% respectively), whereas age and household income exhibit a normal distribution.

A segway on professional background is also useful. Only 22% of respondents are Islamic finance practitioners, 35% relate their work to Islamic finance, and 41% are not related to Islamic finance. It might be counter-intuitive, but this is a very positive indicator that the results reflect consumers and industry outsiders (for lack of a better word). This provides validity to the results while of course we acknowledge the importance of having responses from practitioners. A future investigation remains in terms of analyzing the comments and suggestions provided within the survey.

Summary of findings:

- 1. Awareness:** Whilst awareness levels are overall high, the need that comes out is the lack of easily available industry and product information. Significantly only 9% of respondents strongly agree that this is sufficient, whereas over 70% are either neutral or negative. Therefore, there is an opportunity area for the industry to collaborate within itself and with regulatory and standard-setting bodies to have a more open communication and the sharing of information (whether this is on product development, standardisation and/or regulatory developments).
- 2. Industry Perception:** Industry practitioners and consumers (as respondents to this survey) clearly show the 'split' that exists in terms of 'sharia-compliant' and 'sharia based'. This dissonance clearly shows that there are strong doubts about true Sharia adherence of the products in the market. The survey highlights that 43% of the respondents remained neutral (non-committal) on the statement that "the current products are true to the teachings of Islam", and this neutrality is mirrored in other responses within this section of the survey. While this may raise concerns, there is an equally strong perception that Islamic finance is a good way to promote Islamic values (56% on agreement, only 16% disagree).
- 3. Product Perception:** In terms of product perception, the data supports product innovation being possible and Islamic finance products are not inferior to conventional instruments (close to 40% of respondents feel this way). Furthermore, the response numbers also justify that the industry can establish itself outside of SEA and GCC (a solid 78%). However, perception on institutional products is split with 30% of respondents preferring to remain neutral - this can be interpreted as 'a need to have more product choices for the institutional category'. On the retail front, 33% remain neutral in this regard (however depth and width of product range would need to be checked). In both cases, responses are skewed towards neutrality (with very low marks on strongly agree and strongly disagree).
- 4. Product Knowledge:** Of the products listed the knowledge levels are good across the board with the 3M taking the top spots (Murabaha, Musharaka, Mudaraba). The early responses showed strongly for Ijara but this has since dissipated although it remains as one of the most familiar products. On the other end of the spectrum: Istijar (32% poor, 21% neutral), Arbun (31% poor), Wa'ad (27%), Tawarruq (25% poor) and - surprisingly - equity screening (23% poor). With the exception of the last one this exhibits a clear knowledge gap for those geared towards derivative contracts.
- 5. Acceptance:** A substantial 72% of the respondents show a desire for a fully compliant investment portfolio, followed with 74% claiming that Islamic finance products are now a necessity in their financial planning. However, respondents were strongly divided on the statement of whether current products are serving their requirements as Muslims & faith in current products - with 33% strongly agreeing and 33% remaining neutral. This split clearly indicates a perceived doubt in acceptance of current products as being 'truly' Islamic.
- 6. Brand Values:** 61% of the respondents stated that an open, transparent and honest business culture is overwhelmingly important. This is in conjunction with 82% have rated a strong brand promise as an important "must have" in order for the product to succeed. This clearly shows the need for strong marketing in order for the industry to develop brands through which consumer relationships are grown. In addition, 53% of the respondents stated that they would be willing to pay a higher price (or price premium in comparison to conventional products) for fully compliant products. In terms of brand values, the respondents clearly sat on the fence with 43% indicating that IFI's are not reflecting the values in which they are based and that Islamic brands providing more value has not yet been 'perceived' as 35% of respondents were neutral with 26% strongly agreeing and 24% disagreeing.

Your feedback and comments are very important to us, please feel free to contact the author [via email](#).

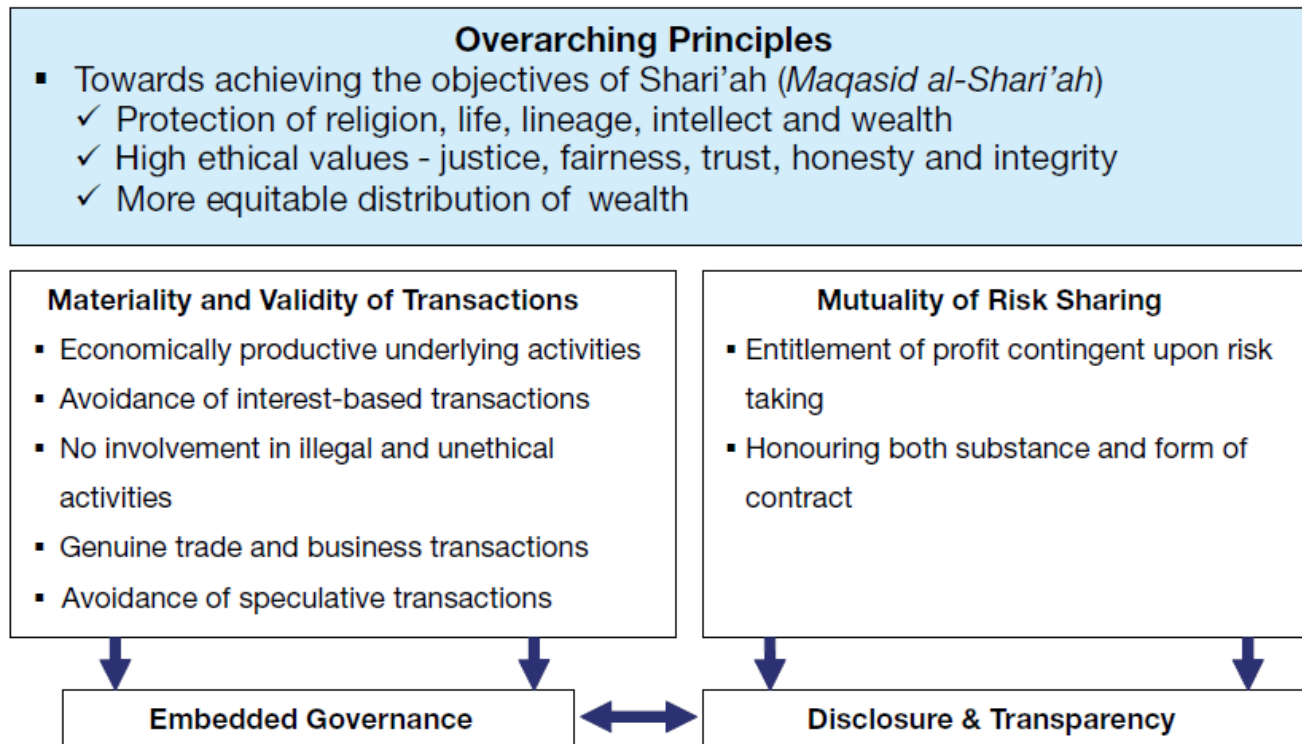
IFSB-IRTI-IDB Islamic Finance and Global Stability Report

This particular report (see [reference link](#)) has been published very recently (April of this year) and is a joint collaboration between the ISFB, IRTI and the IDB. We felt a desire to further scrutinize this study since it seems that not enough attention has been given to its findings. Even their own press release failed to include a link to the actual report and almost every media outlet (in particular those that claim to be internet savvy) could not - or would not - bother to include a simple hyperlink to the online document. In any case, the output can be easily described with one word: lucid. It provides a concise, refreshing and pragmatic overview of the Islamic financial industry today and provides poignant signals as to its future.

The report itself is in fact the amalgamation of work performed by three different task forces that worked on the following areas:

- A. Appreciating the Islamic Finance Model
- B. The State of Islamic Financial Services Industry
- C. Challenges and Strategies for Strengthening Financial Stability in the Islamic Financial System

Essential Features of Islamic Finance



Industry Snapshot

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All three sections deserve attention, for instance the attached graph from the first area (Appreciating the Islamic Finance Model) provides a succinct overview of Islamic finance. Nevertheless, it is the third area (Challenges and Strategies for Strengthening Financial Stability in the Islamic Financial System) that provides very useful indicators in terms of governance. The report takes a predominantly forward looking perspective and it identifies three key areas of priority that warrant greater attention from policy makers and regulators, so as to strengthen and enhance the “Islamic finance ecosystem”:

1. Strengthening the infrastructural building blocks of the Islamic financial services industry to further enhance the industry’s resilience. The report identifies a set of 8 building blocks required for strengthening industry infrastructure., and this incorporates a strong governance approach that is closely aligned with the efforts of the IFSB:

- a. Comprehensive set of cross-sectoral prudential standards
- b. Development of a liquidity management infrastructure
- c. Strengthening financial safety nets
- d. Effective crisis management and resolution framework
- e. Accounting auditing & disclosure standards
- f. Macro-prudential surveillance
- g. Strengthening rating processes
- h. Capacity building and talent development

2. Accelerating the effective implementation of Shari’ah and prudential standards and rules to facilitate the creation of a more stable, efficient and internationally integrated Islamic financial services industry. Here the report zooms in on the need for 1) a better implementation of prudential standards (i.e. IFSB guidelines, etc); 2) encouraging mutual understanding of Shari’ah views on key issues across different jurisdictions (i.e. communication) ; and 3) emphasis for Islamic finance to be a more inclusive system (i.e. integration). The main takeaway is that there is a clear understanding that industry cohesion is necessary and this can occur despite the various schools of thought and the different stages of market maturity.

3. Creating a common platform for the regulators of the Islamic financial services industry to enhance constructive dialogue. The most significant recommendation put forward by the report is for the establishment of a platform for constructive dialogue which is termed the “Islamic Financial Stability Forum” (IFSF). This is expected to take the form of a task force within the IFSB that will be “a strategic platform for conducive and constructive dialogue among the regulators of the international Islamic financial system”. While this will be a significant undertaking it would benefit from having the input of practitioners and active market participants as well (some represented within the IFSB membership).

The overall recommendations are focused on macroeconomic issues, policy concerns, as well as crisis management. Nevertheless, it also suggests that increased attention will be given to “issues of coherence and convergence, and on opportunities to increase the efficiency, integrity and stability of Islamic financial markets”. If these can be developed within an aggressive timeframe and if they have the implicit buy-in of IFSB members (regulatory bodies in particular) then we are looking at a governance initiative that could have far reaching consequences for the industry.

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