

Islamic Finance news

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Revolution brings renewal

The tectonic plates have shifted, albeit metaphorically. Nations in the Middle East and North Africa are caught up in a whirlwind of revolution moving across the region, and the world waits to witness the full impact of the political crisis. If the domino theory has its way, the global economy will bear the brunt of this catastrophe even before it has completely healed from the wounds of the financial crisis.

However distasteful, this might be a good moment to pay heed to the adage that behind every crisis lies great opportunity. At least that is how NBD-Abu Dhabi Islamic Bank (Egypt) chooses to look at things in its report. The bank asserts that the best time to start an Islamic finance business is now, in post revolution Egypt, particularly in the light of the political will that comes with a new regime.

Not far from the political unrest lies Syria which has made incremental steps to facilitate Islamic finance in recent years. However, there are many opportunities for improvement in Syria as put forward in a report by The Scandinavia University, including injecting new blood into Islamic financial institutions, and the rehabilitation of Islamic finance education.

While not immune to the recent political protests, both Yemen and Oman stand in good stead as far as Islamic finance opportunities are concerned. Although the development of the Islamic microfinance industry in Yemen has been a governmental priority for a while, the country now needs an Islamic microfinance sector development project, says a report by Tadamon International

Islamic Bank. And in Oman, while not explicit in its laws for facilitating Islamic banking and finance, Shariah as the primary source of law precludes the need for separate Islamic finance legislation, according to BankMuscat's report.

Ever intertwined with the fate of the Middle East economies is the US, where opportunities for Shariah syndicated finance are plenty. Patton Boggs writes in their report that unless US based financial institutions expand their knowledge and comfort level with Islamic finance structures, opportunities to originate and participate in Shariah financings will go elsewhere in the global financial marketplace.

One strategic approach which may help the US market is to concentrate on the high net worth individual market as suggested by ADCB Meethaq. Their report proposes that the HNW market be given top priority, so focus is kept on best of breed Islamic banking offerings. This will in turn ensure that quality service is the key strategy for growth.

In our IFN reports, Uganda, Nigeria and Ethiopia are steadily harnessing the potential of Islamic finance; Thailand's upcoming Sukuk are detailed; Korea is on the verge of a make or break decision on allowing Islamic finance into its shores; and the fate of the much touted megabank is considered.

In Meet the Head, we feature Najmul Hassan, CEO of Gulf African Bank, one of the banks poised to enter the Ugandan market this year, and Senai Desaru Expressway's Islamic medium term notes is detailed in our Termsheet.^(f)

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FORWARD BANKING CIMBISLAMIC

Islamic Finance Features In Syria

By Dr Samer Mazhar Kantakji

The monetary corrective movement in the Syrian economy began in 2006 when an independent directory about the fiscal policy was granted which activated the monetary policy by implementing indirect monetary tools. The financial stock market was then established and called Damascus Securities Exchange.

The law of private banks was issued in 2001 followed by Decree 35 which permitted the establishment of Islamic banks in 2005. Although the introduction of Islamic banks in Syria was delayed, the abovementioned decree can be considered one of the best laws in the world as it started from the point where all others had stopped.

Decree 43 followed in the same year, allowing Takaful companies to be established. The laws for exchange companies and small financing establishments were then followed by Law 17 of 2010 concerning bank secrecy, in addition to issuing executive decisions aiming at correcting the monetary malformations resulting from the Syrian market's separation from the market economy.

In 2010, there were three licensed Islamic banks, two Takaful operators and one Islamic brokerage. There were 19 Islamic bank branches.

An organizing decree for lease (Ijarah) and lease to buy (Ijarah Muntahia Bitamlik) were issued permitting further freedom for the Islamic banks to deal in these financing forms. The resolution has allowed Islamic investment companies to act according to this financing form as well.

Surveying some of the official indicators up to 2009 may help us to investigate the Syrian market revealing the importance of Islamic financing. The indicators include –

- GDP per capita of US\$2574
- The Syrian pound exchange versus special withdrawal rate of Syrian pound SYP against SDR = 72
- Foreign currency exchange Rate (SYP / US\$) = 46.7
- Current account balance (in billions of SYP = -54.2)

Between 2004 and 2009:

- The central bank's assets increased by 136%. The unified assets of the local banks (without the central bank) increased by 156%
- The unified assets of the public banks increased by 120%
- The unified assets of the private banks increased by 1500%
- The unified assets of the Islamic banks increased by 157%
- A growth in the local deposits from 8.23% to 12.44% between 2004 and 2009

The Islamic banks' investments in Murabahah amounted to SYP1.7 billion (US\$36 million) in 2007, SYP1.9 billion (US\$40 million) in 2008, SYP2.1 billion (US\$445 million) in 2009, but until June 2010 it amounted to SYP3.3 billion (US\$700 million); besides financing in the form of Istisnah and other forms at very moderate rates. It is observed that the growth of Murabahah financing has reached 12 folds in half year only, on the supposition the number doubled at the end of 2010. This shows an increase up to 25 folds.

Although the rate of subscription for Cham Islamic Bank reached 628% and of Syrian Islamic Bank reached 336%, we find that the Islamic financing does not represent more than 2% to 3% of the Syrian market's finance. This can be attributed to the weak formula used which is Murabahah that does not meet the needs and requirements of the Syrian market.

The structures of the Syrian market are distributed formally according to the international criteria where agriculture forms 14%, mining and manufacturing and utilities 8%, building and construction 14%, while trade and its services exceed 65% (with wholesale and retail trade make up 50% and other activities 15%).

But the Islamic banks' insistence in using Murabahah system only made them defective in meeting the Syrian market's need resulting in turning customers (suppliers) toward other banks to secure their financing requirements.

“The structure and diversity of the Syrian market provides a further impetus to activate all forms of Islamic financing”

The diversity in Islamic financing forms permit meeting the needs of all sectors and levels of society, but sticking to the Murabahah system alone may lead to lowering the Islamic banks' performance, by decreasing the return on equity (ROE) to less than 4%, thus lowering their efficiency in the macro-economic by lower return on assets (ROA) which is less than 0.004.

As for the suppliers, the cost of finance, which is very high compared to those at traditional banks, leads suppliers to find dealing with Islamic banks unacceptable.

In my opinion, as an observer of the Islamic market in general and the Syrian market especially, I find the Syrian market promising for Islamic finance provided directors of Islamic banks in the country adopt the correct Islamic financing thought ensuing from the principles of sound Islamic economy.

These principles depend on the sources of legitimate Islamic Fiqh which permit deducing the forms and financing tools which tend to verify the divine or religious aims before the doer's, and adopt the resolution and licenses. The principles do not rely on tricks which disfigure the picture of the Islamic financing and spoil its right economic force.

The use of diversity in financing forms aids in risk management and does not centralize on a definite form or sector of the market, leading to the lowering of financing costs as well.

The central bank's aims to establish a central legislative board in Syria may embitter the situation. The board shall also guide investment *continued...*

Islamic Finance Features In Syria (continued)

policy and restrict credit forms, which may be used to raise Islamic banking efficiencies, before the classic competitors.

The structure and diversity of the Syrian market provides a further impetus to activate all forms of Islamic financing – in addition to pushing the Islamic financial institutions toward direct investments to verify good gains for them and clients where the total benefit results in lowering the financing costs.

This attitude affords the local human resources to be either technical or legitimate. These local human resources may be good learners and skillful enough to develop experience, whereas imported workers of traditional banks may lack the efficiency required, and also view their learning and development as negative.

Syrian universities have been criticized in this respect. They are seen as not supplying enough study in the field of Islamic economy and financing, mainly because they are still unconvinced of the efficacy and success of Islamic finance establishments in both Muslim and non-Muslim states.

In some universities the study of Islamic finance is restricted to one chapter. The professors are not experienced enough practically nor theoretically, which leads to graduates with poor knowledge of Islamic finance, thus forcing them to look for other ways of education.

The central bank must cooperate with Syrian universities to allow graduates to practice and further their experience at Islamic banks via internship programs.

This will eliminate the need for graduates to obtain 'experience certificates' to make them more preferable than other graduates when Islamic banks recruit their staff. This may lead to a confusion of concepts and differing education at the Islamic financial establishments.

We find that Islamic finance faces several challenges in general and particularly in the Syrian Islamic market. These challenges may be resolved by adopting the following:

1. Rehabilitation of the Syrian universities for teaching economics and Islamic banking.
2. The adoption of policies by the central bank that bridges the gap between universities and the Islamic financial institutions.
3. A directive from the central bank for Islamic banks to diversify Islamic financial products.
4. Change the education of the boards of directors when planning banking strategies, to follow policies to achieve Islamic banking in core, not in appearance.
5. For higher, medium and lower staff to choose executive directors and staff who believe in Islamic finance as a strategy which depends on the divine and welfare for all people.
6. Introducing new elements of support for legitimate staff in view of new blood who are more active, energetic and ready to work in Islamic financial institutions and by not allowing them into more than two or three boards.
7. Establishing scientific research centers in universities and more to develop financial innovation in Islamic financial engineering to enable these products to move further into active services of the economy.
8. Developing accountants and accounting auditors in collaboration with the CPA institutions, universities and expert bankers
9. Supporting formation of external legitimate auditors compared with the external accounting auditors
10. Supporting establishing financial study and analysis bureaus interested in Islamic financial institutions. (3)

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