

THE PANEL



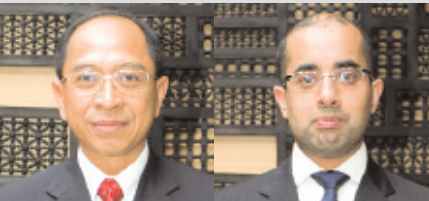
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CEO, Standard Chartered
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Vince Cook
CEO, Islamic Bank of
Asia

A TEMPLATE FOR AVERTING DISASTER?

Round table

As turmoil in the banking industry intensifies, the appeal of Islamic finance and its risk-sharing approach is growing. Yet to bring Islamic structures into the mainstream, a workable infrastructure must be established. The Banker brought together a panel of industry experts to discuss the key considerations.

■ THE KEY ISSUE ISLAMIC FINANCE



As the global financial crisis shakes up the banking industry, Islamic banking is faced with a great opportunity to build improved structures and to strengthen its international market role, but it will also face some stiff challenges in the process. Stephen Timewell, editor-in-chief of *The Banker* and round table chairman, asked a panel of industry experts to share their views.

Speaking at *The Banker's* recent Islamic Banking Round Table in Dubai, Dr Nasser Saidi, chief economist at the Dubai International Financial Centre (DIFC), said: "This is the moment for the industry to really grow and develop; we'll never have as much liquidity in the region and this is a prime opportunity to develop the Islamic securities markets."

But while Dr Saidi and nine other chief executives and Islamic banking experts at the round table could see the possibilities, they were also well aware of key challenges involving the convergence of regulations, lack of transparency and standardisation of Islamic products. While *The Banker's* Top 500 Islamic Financial Institutions listing in November showed that global sharia-compliant assets had grown by 27.6% since November 2007 to reach \$639.1bn – a healthy growth rate – Vince Cook, chief executive of Islamic Bank of Asia, was adamant that the industry needed to follow a better roadmap to move forward.

He explains: "The Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI) and the Islamic Financial Services Board (IFSB) have no legislative clout and Western models were

largely still being followed." The 10 participants clearly shared concerns about accounting and regulatory issues. "We are not going to make an impact on the conventional banking world while bankers are still largely following Western or BIS [Bank for International Settlements] standards."

While Sohail Zubairi, chief executive of Dar Al Sharia, spoke positively of the "beauty of Islamic structures", others were concerned about the 'untested' aspect of insolvency laws and about bringing Islamic laws into the mainstream.

Khalid Howladar, senior credit officer for asset-backed and sukuk (Islamic bond) finance at rating agency Moody's, was emphatic that Islamic finance did not need new structures, but Islamic structures needed to be brought into the existing structures. He explained: "Parallel systems are not the way, integration is the key." While Mr Zubairi advocated teaching the Islamic rules of AAOIFI from an early age, Mr Howladar was keen for Islamic expertise to be integrated into overall training and that the skills of conventional banking and Islamic banking were combined. "The International Accounting Standards Board (IASB) needs to incorporate Islam rather than create separate, parallel systems," he said.

The lack of an Islamic voice in the international financial arena was demonstrated by the fact that there was not one single member from the Middle East region or Middle East bank on the IASB. As participants noted, how can Islamic banking be recognised if it has no membership in the IASB?

The complexity of having dual systems was raised by Jamil Hassan, principal consultant for Islamic banking at Oracle Financial Services. He cited a recent court case in Malaysia which referred to the problem of the two operating laws: conventional banking law and Islamic banking law. Because of

the complex legal system, decisions need to be made in court, and this complexity and the need for court decisions is said to create unwarranted issues and difficulties.

Others, such as Afaq Khan, chief executive of Standard Chartered Saadiq, emphasised the need for closer co-operation between industry bodies, such as AAOIFI, so that there could be moves towards standardisation and standardised products.

Another key challenge facing all economies in the region is infrastructure but, as Dr Saidi explained, Islamic public finance has yet to be fully explored and was a major opportunity for the industry. It was suggested that development of securities markets should be a priority, especially with the abundance of liquidity in the region. Yet Dr Saidi warned: "Islamic banking is not immune from the current crises." But he said that in trying to create risk models for the Islamic industry, Western risk models and data were irrelevant. He also noted that the absence of a lender of last resort in Islamic finance was an issue needing to be solved.

Addressing the issue of regulation, Dr Saidi put forward a few ideas. First, he suggested that the multiple number of free trade agreements should include recognition of Islamic financial products so that they could be recognised in law by various countries and get wider transmission and traction. Second, he mentioned the issuance of a financial passport that would give mutual recognition across a variety of countries for various Islamic products. Third, he stressed the use of double taxation agreements to recognise Islamic banking principles, emphasising that if the Gulf's oil-rich countries were being sought by heavily debt-ridden countries in the West for help, they should make sure that Islamic banking products are recognised in these agreements.

While participants were aware of the rather small size of the Islamic banking market, others stressed that, unless there was mutual recognition in various free trade agreements made, Islamic financial products would never get proper recognition from major developed markets.

Participants were keen to see recognition and reciprocity from conventional banking mechanisms and states. It was noted that the UK government was planning to issue a sukuk in the future but this was being delayed by certain factors. As Qudeer Latif, head of Islamic finance and partner at Clifford Chance, said: "Double taxation agreements are not the biggest obstruction to the issuance of a UK sukuk, the key issues remaining include stamp duty,



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Vince Cook ●●

the secondary market and value-added tax."

As the round table concluded, it was stressed that the moment was opportune for Islamic finance to play a key role in the international financial infrastructure. The time was right for central banks and finance ministers to tap into the liquidity available, to develop the relevant infrastructure and projects in their region, and also to develop the Islamic securities markets.

Dr Saidi concluded that three ingredients are needed. First, standardisation of laws and procedures, and second, convergence of regulatory structures across the Islamic finance arena. But he also added that in this positive environment for Islamic banking, reliable data – sadly lacking at present – was essential if progress were to be made.

But differences existed between the panel's viewpoints, as Mr Cook questioned the need for too much standardisation: "We need to be careful about standardisation: conventional banking still has a variety of different models so why should Islamic banking be any different?" Clearly, the debate over Islamic banking continues. **1B**

THE ISSUES

- **INTEGRATING ISLAMIC STRUCTURES INTO THE MAINSTREAM**
- **PROMOTING CLOSER CO-OPERATION BETWEEN INDUSTRY BODIES**
- **ESTABLISHING INFRASTRUCTURE AND DEVELOPING ISLAMIC SECURITIES MARKETS**
- **MAPPING OUT A WORKABLE ACCOUNTING AND REGULATORY SYSTEM**
- **INTRODUCING ISLAMIC FINANCIAL PRODUCTS TO DEVELOPED MARKETS**

