ISLAMIC FINANCE & INVESTMENT PRODUCTS

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AGENDA

UNDERLYING PHILOSOPHY

TECHNICAL ASPECTS

KEY UPDATES ON IFSI PERFORMANCE

STRATEGIC OUTLOOK

UNDERLYING PHILOSOPHY

FACTORS INFLUENCING FINANCIAL & INVESTMENT PRODUCTS?

F&I products depend very much on the culture & 'ideological' belief of any given society

↓

Example: Apart from credit sales & equity financing, riba was so prevalent in Arab society before the coming of Islam (culture of greed & materialism)

↓

In modern time – factors such as legal framework, taxation regime, as well as societal norms & appetite matter a lot in shaping F&I products

↓

All in all – no perfection or absoluteness with regard to products to satisfy socio-economic needs of the society

↓

Islamic F&I products	
Religious: Shari'ah compliant	Economic: Viable & competitive

ISLAMIC VS CONVENTIONAL PRODUCTS

Islam never prohibits something without offering a corresponding alternative

e.g. Islam prohibits riba but allows trading

However – some product features are very conventional

e.g. Credit Card vs Charge/Debit Card

In some cases, we have alternatives – but they may defeat the purposes of Islamic law

Issue of substance vs form – due to the desire to fit the alternative into the conventional framework / mindset

Conventional aim/worldview vs Islamic aim/worldview (maqasid al-shari'ah)

DISCUSSION: ISLAMIC ALTERNATIVES FOR EACH & EVERY CONVENTIONAL PRODUCT?

Theoretically	Practically
YES	X always YES

Conventional worldview vs Islamic worldview

Alternatives for Prohibitions

Substance vs form

ISLAMIC WORLDVIEW / PHILOSOPHY

Islamic economic paradigm

Rabbani (divinely guided)	Insani (human)	Akhlaqi (ethical)	Wasati (balanced)

Compatible with human nature (fitrah) + Islamic character

Fully Islamic (end-to-end)

Piecemeal approach vs integrated approach

Outcome

Peace (salam)	Cure (shifaa’)	Mercy (rahmah)

QUR’ANIC & PROPHETIC GUIDANCE

Fussilat:46 – Whoever does what is just & right, does for his own good, and whoever does evil, does so to his own hurt, and never does Allah do the least wrong to His servants

Hadith: Verily Allah has prescribed the limits, so do not transgress them, He has ordered certain matters, so do not neglect them, He has prohibited something, so do not indulge in them…

Al-Nahl: 97 – Whoever work righteousness, man & woman and he is faithful, verily to him will We give a good life (hayaatan tayyibah) and to him will We reward with the best recognition of what they have worked for

The notion of righteous work (`amal salih) includes proper economic & financial activities based on Islamic precepts as a pre-condition to a good life (hayaatan tayyibah)

TECHNICAL ASPECTS

FINANCIAL PRODUCTS: AN OVERVIEW

Financial products are packaged solutions for customers' financial needs

Major categories

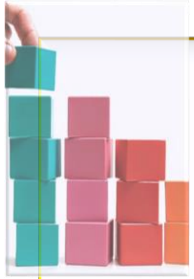
- Personal/Retail/Consumer Banking
- Corporate Banking
- Investment Banking
- Wealth management
- Treasury & capital market
- Structured finance
- Takaful or insurance

SALIENT ASPECTS OF PRODUCT DEVELOPMENT

Focus on customers & solutions

Product mix – normally reflective of FI's vision & strategies

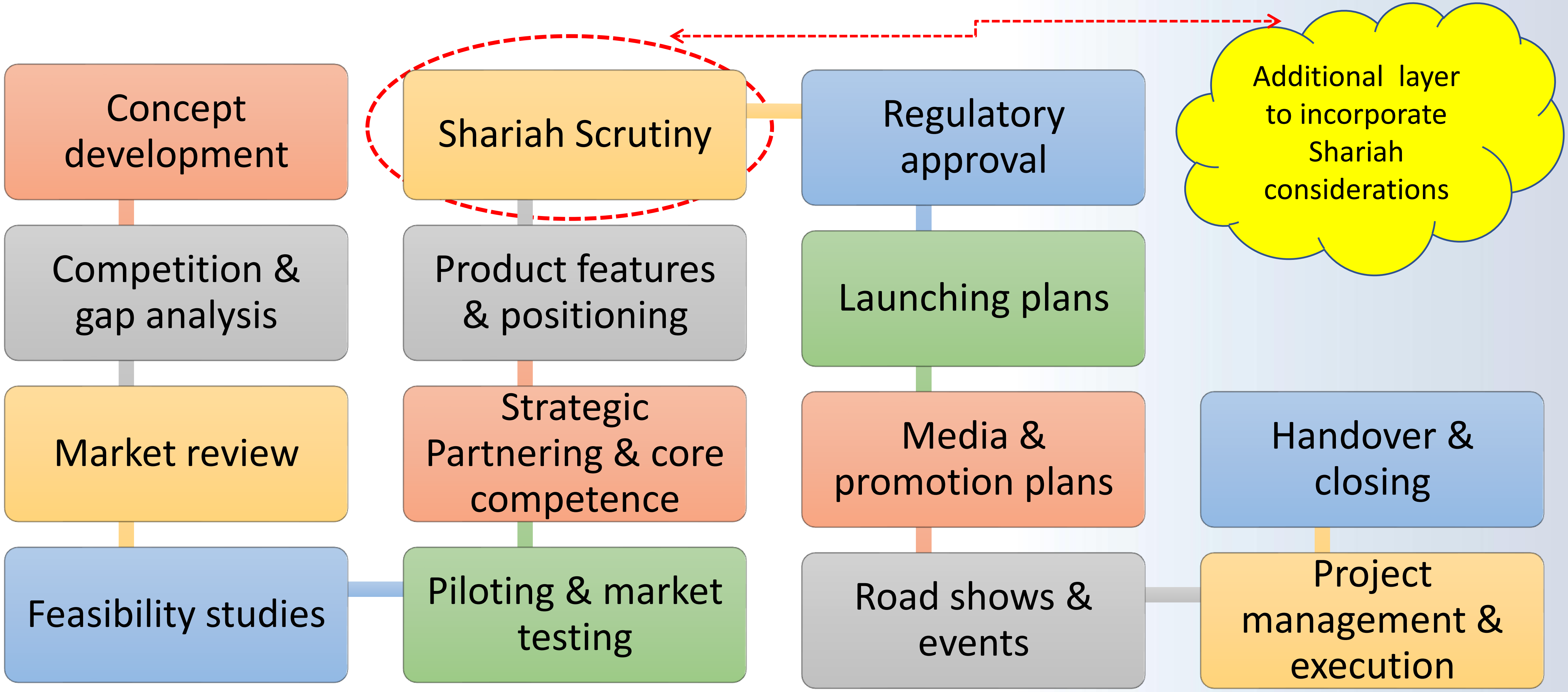
Product-centric vs customer-centric



Building blocks or Menu on offer

Catering to different market segments

ISLAMIC PRODUCT DEVELOPMENT PROCESS



NOMINATE CONTRACTS VIS-À-VIS INNOVATION

Are we confined to contracts already known & defined by the jurists in the past – nominate contracts?

No, because the contracts being sanctioned in the past were the discoveries of the past that suited their circumstances then.

The nominate contracts need not be applied as they are, but their principles might be re-used to meet our purpose, e.g., sale and lease back for the purpose of liquidity

OPPORTUNITIES

Need for new contracts & formulation of new rulings in the absence of any precedents

Shari`ah framework accommodates innovations & product developments via the mechanism of ijtihad – dynamism of analogy & ratiocination – tool for innovation

Islamic theory of contract – principle of permissibility & freedom to contract

Potential to innovate new contracts not previously known	Provided: do not contradict any established principles of Islamic law

PRODUCT DEVELOPMENT: PROPHETIC EXAMPLES

Endorsement & Islamization

- Endorse existing contracts
- Eliminate unlawful elements eg. riba & gharar
- Acknowledge the need & convenience of people
- Examples: Ijarah, Mudarabah, Bay’ al Salam

Introduction of New Contracts

- Innovate new contracts to meet the needs of people
- Give facilities & eliminate hardship & harm
- Examples: Hiwalah, Ibra’, Muqasah, Da’ wa Ta`ajjal

PRODUCT DEVELOPMENT IN VARIOUS MADHHAB

EXAMPLES

- **Bay' al `Uhdah** Shafie School
- **Bay' bima yanqati' Bihi al Si`r** Hanbali School
- **Bay' al `Inah** Shafie School
- **Ijaratan** Shafie School
- **Mursad Loan & Hawalah al-Mursad** Hanafi School
- **Daman Contract** Hanbali School
- **Tawarruq** Hanbali School
- **Bay' al Wafa'** Hanafi School
- **Forward Lease** view in Hanbali School

PRODUCT DEVELOPMENT: MODERN EXAMPLES

EXAMPLES

Islamic Hedge Funds
Salam, `Urbun, Khiyar al Syart

Debt Securitization
Bay' al Dayn
(Sale of debt with Discounting – M'sian)

Equity / Shareholding
Musharakah

Lease-based Securitization
Sukuk al Ijarah
(Buy / Sale & lease-back)

Securitization of Usufruct
Sukuk al Intifa'
(Time-sharing basis)

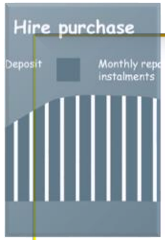
Capital-Protected Investment
(3rd party guarantee, Islamic derivatives)

Islamic Futures/ forward

Mixed-Asset Securitization
Sukuk al Istihmar/ Wakalah
(Assets + Debt)

Islamic Money-Market Instruments

OTHER EXAMPLES OF CONTEMPORARY PRODUCT DEVELOPMENT & ENHANCEMENT



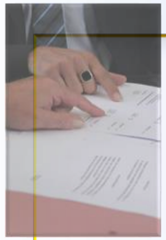
Islamic hire purchase (lease then sale)

Limited recourse collateral in equity financing

Islamic insurance

Security Deposit in Islamic financing

Set-off clause



Early maturity of installments upon default

Late payment charges (ta`wid/gharamah clause)

Wadi`ah yad damanah for Islamic deposit, etc.

PECULIAR TECHNIQUES OF IJTIHAD IN MU`AMALAT

Making analogy (ratiocination – ta`lil)		
shareholding & musharakah		

Tracing the contract to the principles:	
Profit is associated with risk/liability	Loss bearing in musharakah vs priority in capital return for PS

Introducing new contracts combining several lawful features	
Bay’ al-wafa’ (jual janji)	Buy & lease back (sukuk al ijarah)

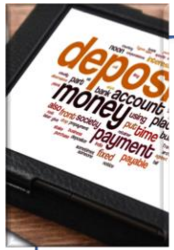
Islamization of conventional products by eliminating elements that are unlawful		
stock selection criteria	forex	PS – preference shares

SHARI'AH CONSIDERATION IN PRODUCT DEVELOPMENT – CONTRACT CLASSIFICATION

Contract of exchange – sale (many different types)

Contract of usufruct – lease (operating, financial & forward)

Contract of security (rahn, kafalah & hiwalah)



Contract of safe custody – wadi'ah

Partnership contract – mudarabah & musharakah

Contract of gratuity – gift, will, waqaf, donation, etc

Multiple contract / hybrid

New contracts… must be free from any of the prohibitions

SHARI'AH CONSIDERATION IN PRODUCT DEVELOPMENT

Case Study 1 :

Forward Market in Currency

Case Study II :

Charges for late payment

Case Study III

Floating rate financing

CHALLENGES & CONSTRAINTS

Legal & Regulatory	Taxation	Accounting
Risk management	Risk weightage	Risk appetite
Rating	Market condition	Human factor

CONSIDERATIONS IN PRODUCT DEVELOPMENT

Risk return Matrix

Low Risk

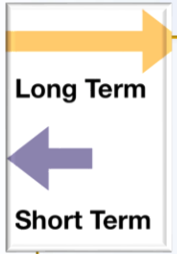
- Murabaha & MM
- Sukuk
- Real Estate Income Fund/vehicles
- Capital protected funds

High Risks

- Speculative growth equities
- Private equities
- Venture capital

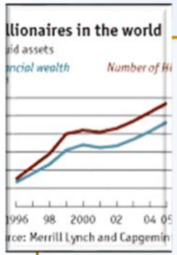
Medium Risk

- Equity income
- Hedge funds
- Structured products
- Asset backed securities



Long-term vs short-term

Liquidity & secondary market



Segment targeted (Mass – HNW)

THE CONSEQUENCE…

Islamic instruments tend to concentrate on debt-related products

Equity-based products fail to take off

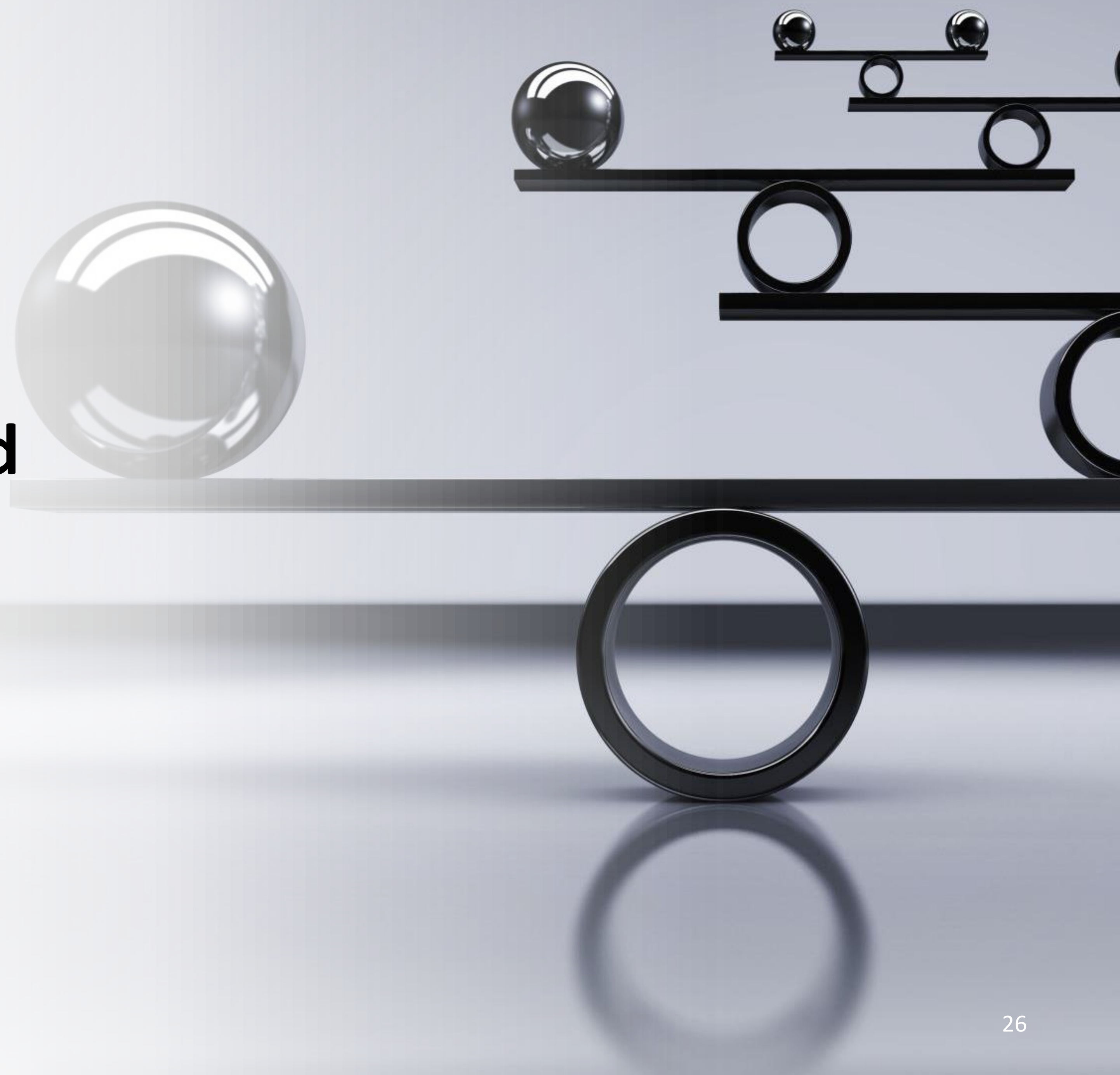
Depth & breadth of Islamic market – lagging behind the conventional counter-part

Lesser liquidity due to lack of secondary market

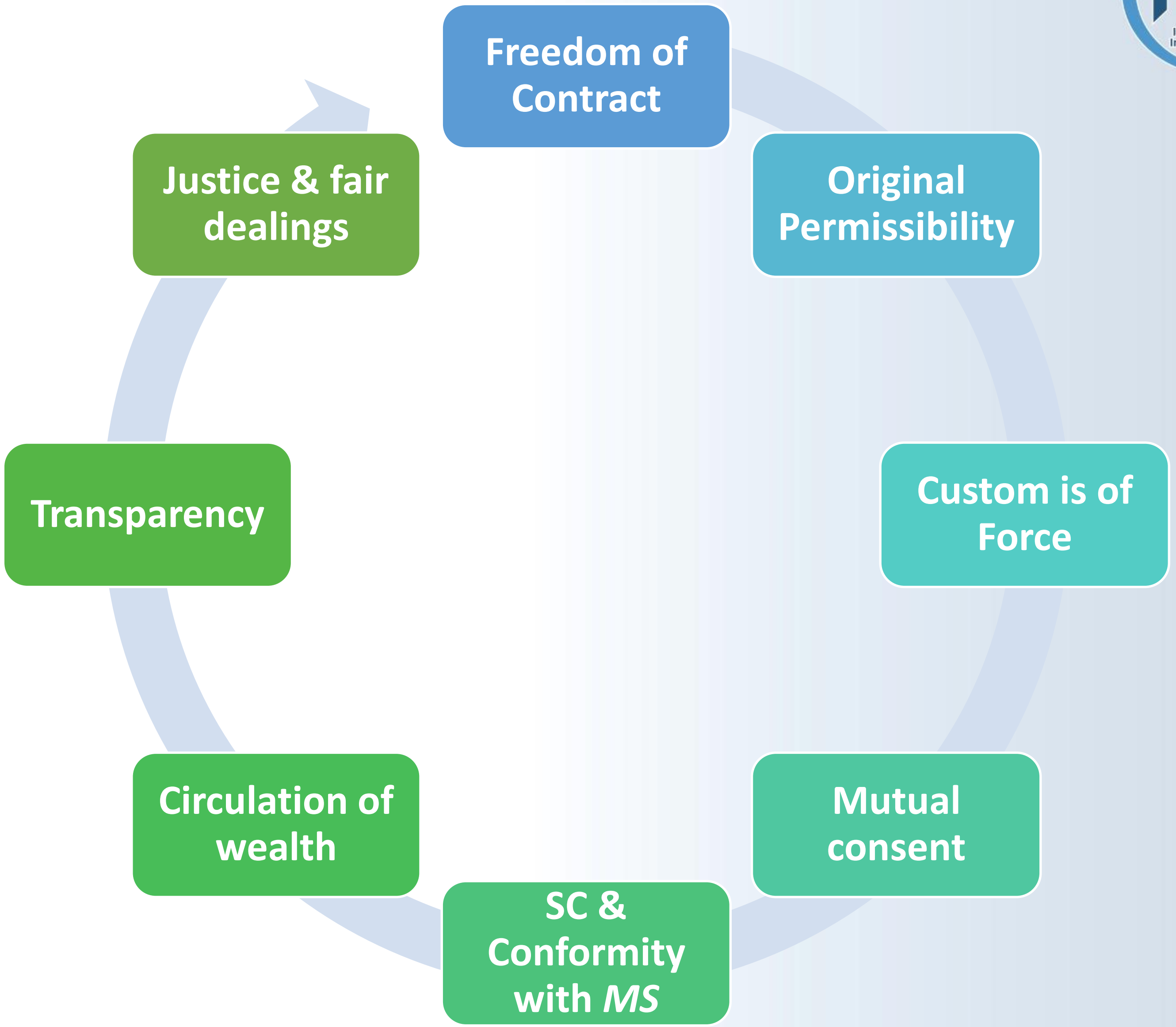
ISLAMIC FINANCE PRODUCTS: THE BIG PICTURE

- **Islamic Financial Products**
  - **Islamic Banking**
    - Financing
    - Deposit & Investment
  - **Islamic Capital Market**
    - Equity
    - Sukuk
    - Funds & Unit Trust
    - REITs
    - Derivatives
    - Private Equity & Venture Capital
  - **Takaful**
    - Takaful
    - Retakaful

Balancing Principle-Based vs Rule-Based Shariah Requirements



SOME GUIDING PRINCIPLES IN MU'AMALAT MALIYYAH



INHERENT SHARI'AH PRINCIPLES IN ISLAMIC FINANCE

SAC of BNM clarified key Shariah principles that are intrinsic to Islamic finance & should be embedded in Islamic financial services (BNM Annual Report 2019)

SHARIAH COMPLIANCE

Profit is justified through bearing & sharing of risk	Money is only store of value & medium of exchange	Wealth creation is balanced with wealth transfer & circulation	Assurance of transparency & traceability

Fairness & attainment of Ihsan

Prevention of harm & attainment of benefits

PRINCIPLES-BASED VS RULE-BASED REQUIREMENTS

PRINCIPLE-BASED

- Macro/broad
- Value-based (spirit of the law)
- Consistent but open for deduction & adaptive to new circumstances

RULE-BASED

- Micro/specific
- Detail/methodological (letter of the law)
- More rigid & may result in unintended anomaly (e.g. used as a mere legal stratagem)

CAN RULES DIVERGE FROM PRINCIPLES?

Generally – Shariah Rules (details) are developed from Shariah Principles (broad-based)

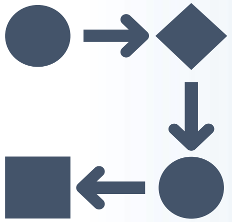
Shariah Rules should ideally & naturally be aligned to the Shariah Principles

Shariah Principles & Shariah Rules must be in harmony so that the real objectives of the Shariah can be achieved

But sometimes application of rules can be inadvertently superficial & detached from the principles – must be corrected & realigned

Principles give soul to revive a rule that becomes too superficial & detached

Go back to the principles – re-draw the rules to match the principles



💡 Prompt: "How can BKRM innovate responsibly within the principle-based framework?"

REGULATORY UPDATES: HIGHLIGHTS FROM SCF DISCUSSION PAPER 2024

SHARIAH CONTRACT FRAMEWORK DISCUSSION PAPER

BNM's 14 Shariah contract-based PDs (SC-B PDs) – promote end-to-end Shariah compliance & provide clear guidance in operationalising Shariah contracts

Shariah Requirements	Operational Requirements

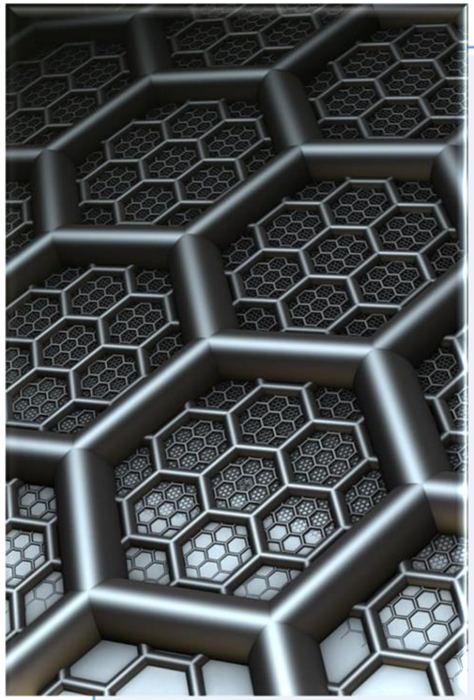
SC-B PDs + SAC rulings = source of ref. for SCs & functions in IFIs to ensure Shariah compliance

Product Development	Internal Control Functions

BNM envisages that – full potential & value proposition of IF can be further realised with application of more diverse Shariah contracts – better meet consumer & economic needs

SCF DP – issued by BNM on 11 Nov 2024 & feedback to be submitted by 10 Feb 2025

SUMMARY OF PROPOSED ENHANCEMENTS TO SHARIAH CONTRACT-BASED PDS (SC-B PD)



Framework Design – simplified & more practical framework

- Consolidate the 14 SC-B PDs into a single document (SCF)
- Outline universal & specific Shariah requirements based on type/ nature of Shariah contracts
- Outline universal & specific operational requirements based on type/ nature of Shariah contracts
- Complement with Implementation Guide ("IG") – practical guidance in structuring IF products & services using various Shariah contracts

SHARIAH CONTRACT FRAMEWORK DP

Explore potential approaches in recalibrating & enhancing the effectiveness of SC-B PDs to ensure a conducive regulatory environment for the application of diverse Shariah contracts

Examine corresponding challenges faced by the industry in applying various Shariah contracts effectively

Outlines strategies to support alignment of Shariah contract application with objectives of Shariah & Shariah contract, as well as promote the application of diverse Shariah contracts

DISTINCTIVE APPROACH IN SCF DP IN RELATION TO MS

The SCF not only look at the general MS, but into the specific contracts & specific maqasid that apply to them (Maqasid al-'aqd)

1st step towards achieving MS is to identify them, not only at general level (maqasid `ammah), but also specific (maqasid khassah) & detail objectives (maqasid juz`iyyah) for each contract

Identifying specific & detail maqasid allows us to go beyond the general – able to relate better to specific practices of IF & align them to the specific purpose of the underlying contract in the product

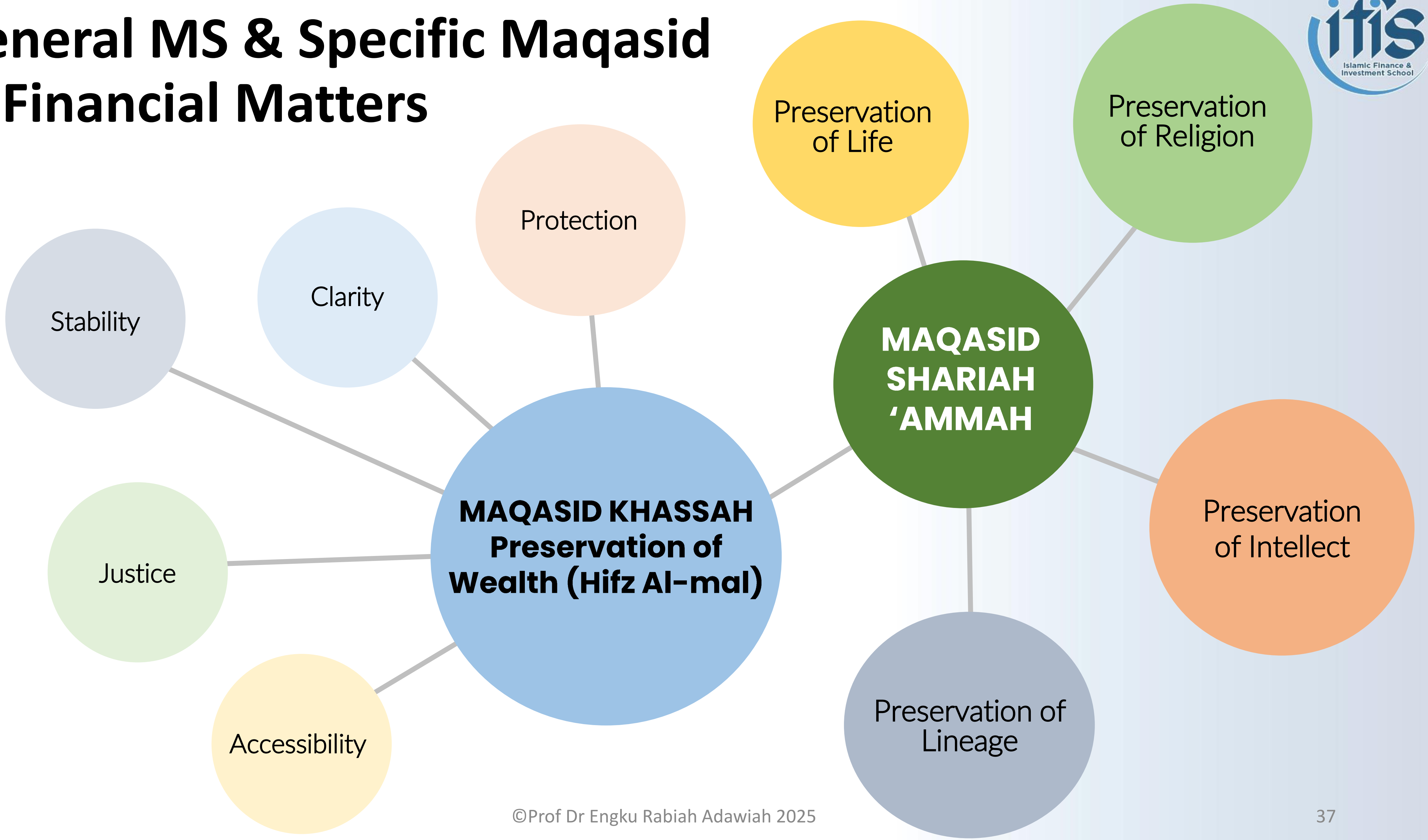
VARIOUS LEVELS OF MAQASID SHARIAH (MS)

Levels of MS

- General Objectives (Maqasid `Ammah)
- Specific Objectives (Maqasid Khassah)
- Detail Objectives (Maqasid Juz'iyyah)

The 3 levels of maqasid are individually distinguishable, though there are obvious overlaps among them. Al-Raysuni noted that although these levels of maqasid are distinctive, they are inter-related, whereby the general objectives are formed from the specific objectives; and the specific objectives are formed from the detail objectives

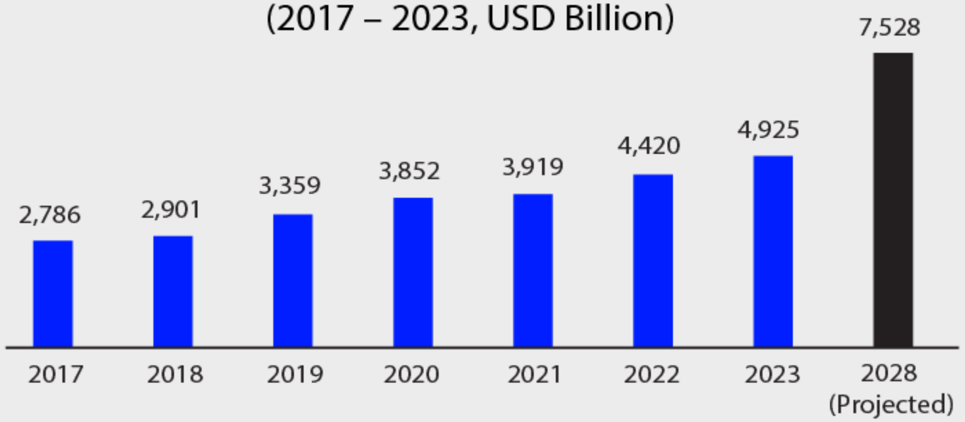
General MS & Specific Maqasid in Financial Matters



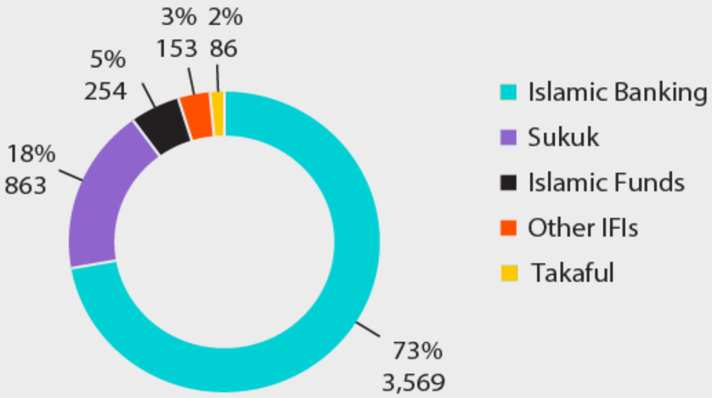
KEY UPDATES ON ISLAMIC FINANCIAL SERVICES INDUSTRY (IFSI)

Islamic Finance Industry in 2023

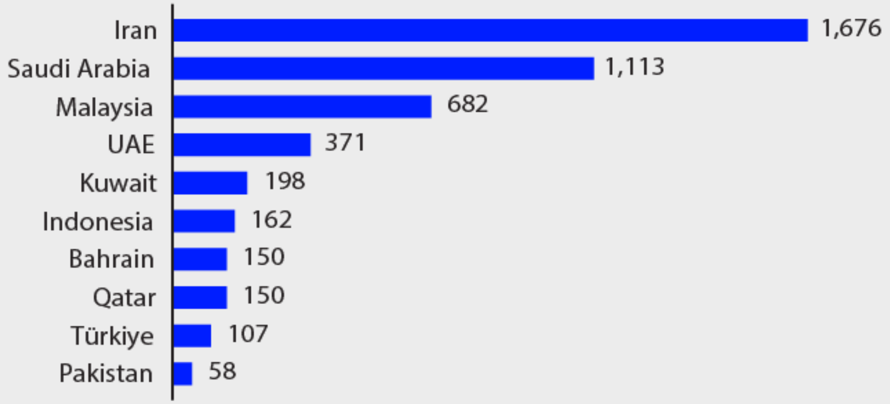
Islamic Finance Assets Growth
(2017 – 2023, USD Billion)



Islamic Finance Assets by Sector and Asset Class
(USD Billion, 2023)



Islamic Finance Assets by Top Countries and Regions
(USD Billion, 2023)



Most Developed Countries in Islamic Finance According to IFDI 2024

ICD - LSEG Islamic Finance Development Report 2024

Islamic Finance Industry and its Supporting Ecosystem in 2023

Financial Performance

Total Islamic Finance Assets	YoY Growth of IF Assets	Islamic Financial Institutions
US$4.9 Trillion	11%	1,981

Governance

Countries with at Least One Type of Islamic Finance Regulation	Countries with FinTech Sandbox	Number of Countries with Centralised Shariah Committee	Average Disclosure Index by Public Islamic Banks	Scholars Representing Shariah Boards
57	72	23	69%	1,512

Sustainability

Total Value of ESG Sukuk Outstanding (USD Billion)	Total Value of ESG Islamic Funds Outstanding (USD Billion)	Number of Countries with Sustainability Guidelines	Average Sustainability Reporting Index by Public Islamic Banks	Total CSR Funds Disbursed (USD Billion)
35.9	8.0	50	48%	1.3

Awareness

Number of Islamic Finance In-Person Events	Islamic Finance Virtual Events	Number of Islamic Finance News
531	387	10,534

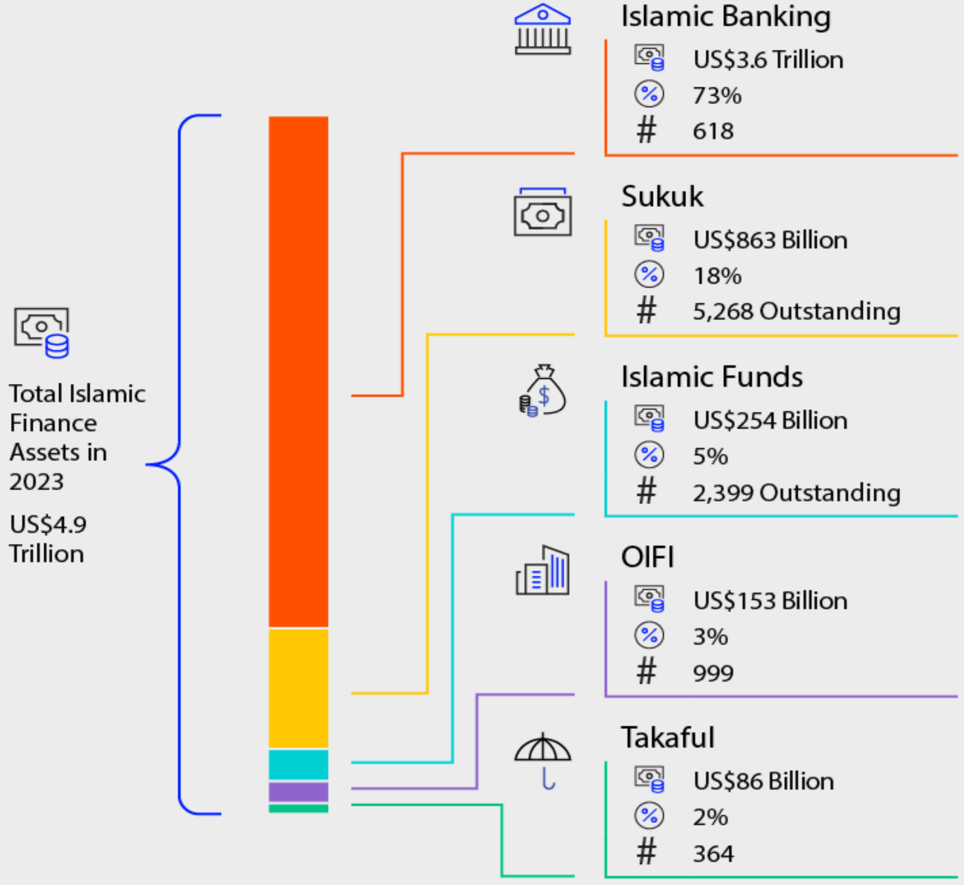
Knowledge

Islamic Finance Education Providers	Islamic Finance Research Papers Produced	Islamic Finance Journals
1,007	5,162	347

ICD - LSEG Islamic Finance Development Report 2024

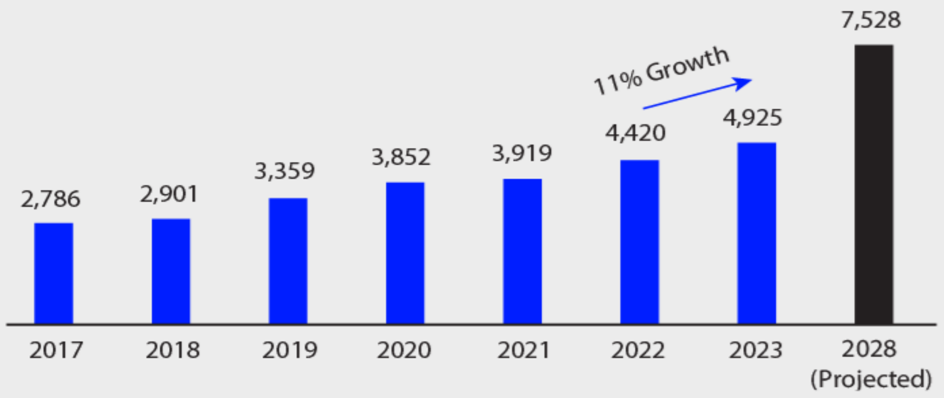
Global Overview of the Islamic Finance Industry

Islamic Finance Industry Breakdown
(2023)

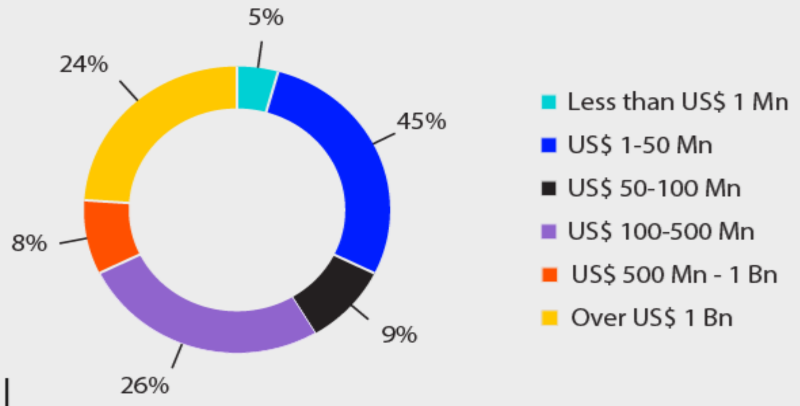


| Total Assets | Share of IF Assets | # Number of Institutions / Instruments |

Islamic Finance Assets Growth
(2017 – 2023, USD Billion)



Breakdown of IFIs by Total Reported Assets
(2023)



ICD - LSEG Islamic Finance Development Report 2024

Islamic Banking

US$3.57 Trillion

Total Islamic Banking Assets in 2023

12%

Growth in Islamic Banking Assets in 2023

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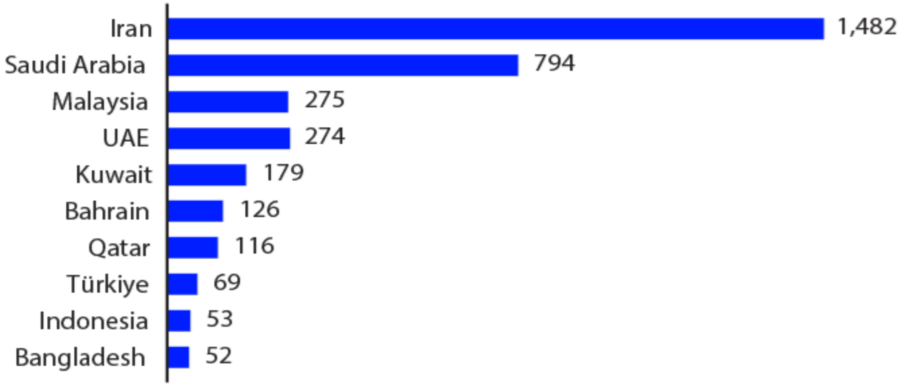
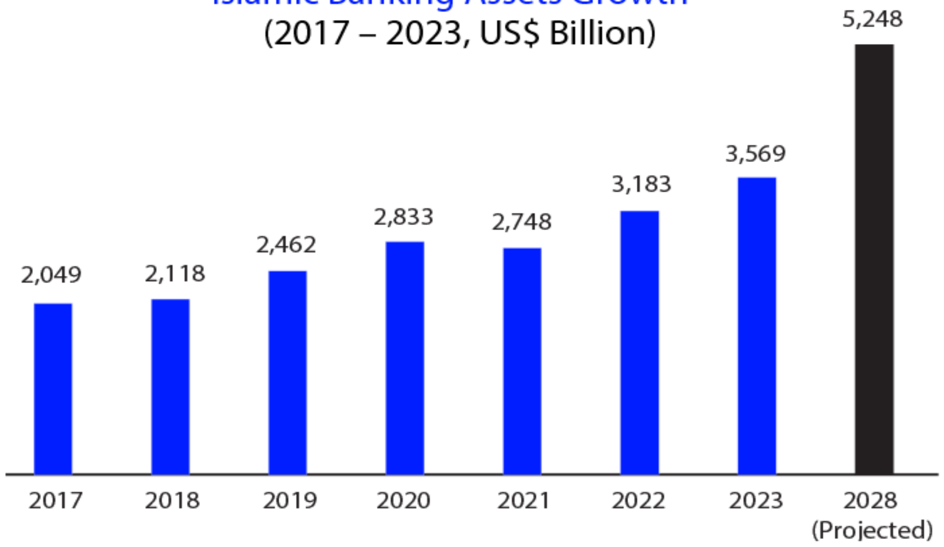
618

Total Islamic Banks

Top Countries in Islamic Banking Assets
(USD Billion, 2023)



Islamic Banking Assets Growth
(2017 – 2023, US$ Billion)



Islamic Banking Assets by Region
(2023, US$ Billion)

Other MENA	1,557
GCC	1,506
Southeast Asia	337
South Asia	85
Europe	78
Sub - Saharan Africa	4
Americas	0.75
Other Asia	0.61

ICD - LSEG Islamic Finance Development Report 2024

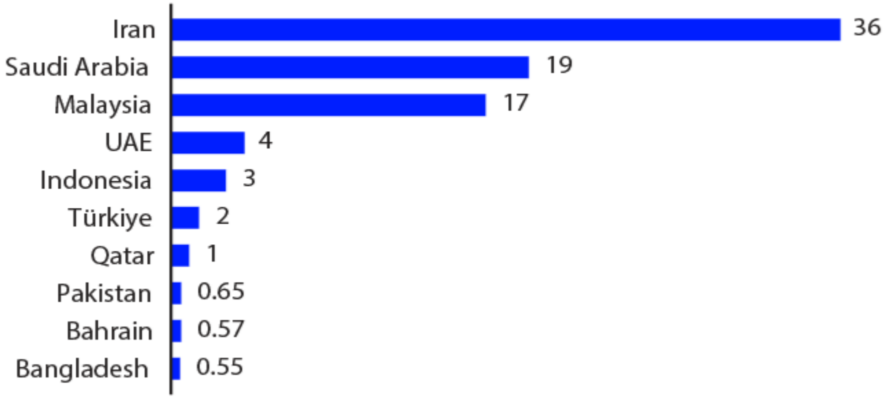
Takaful

US$86 Billion
Total Takaful Assets in 2023

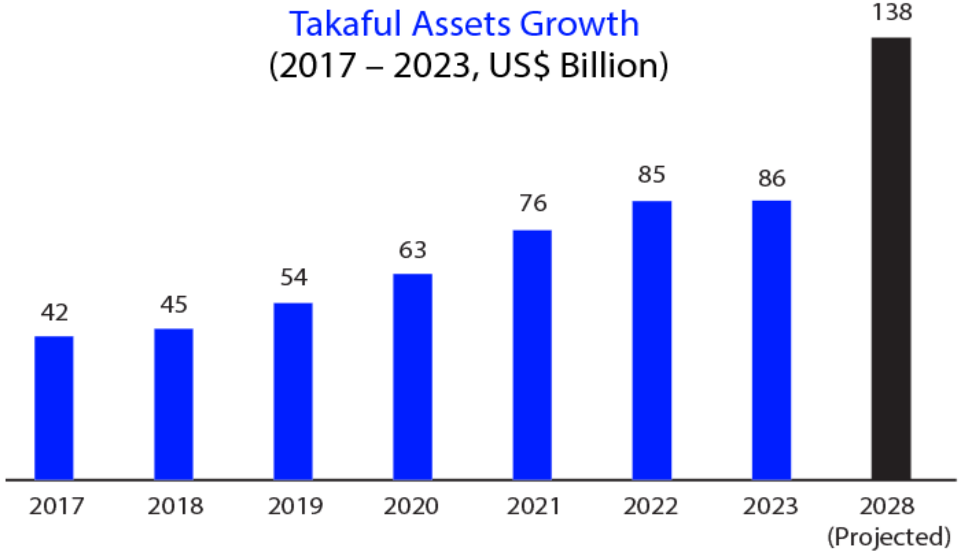
1%
Growth in Takaful Assets in 2023

364
Total Takaful Operators

Top Countries in Takaful Assets
(US$ Billion, 2023)



Takaful Assets Growth
(2017 – 2023, US$ Billion)



Takaful Assets by Region
(2023, US$ Billion)

Other MENA	36
GCC	25
Southeast Asia	20
Europe	2
South Asia	1
Sub - Saharan Africa	0.01
Other Asia	0.00

ICD - LSEG Islamic Finance Development Report 2024

Sukuk

US$863 Billion

Total Sukuk Value Outstanding in 2023

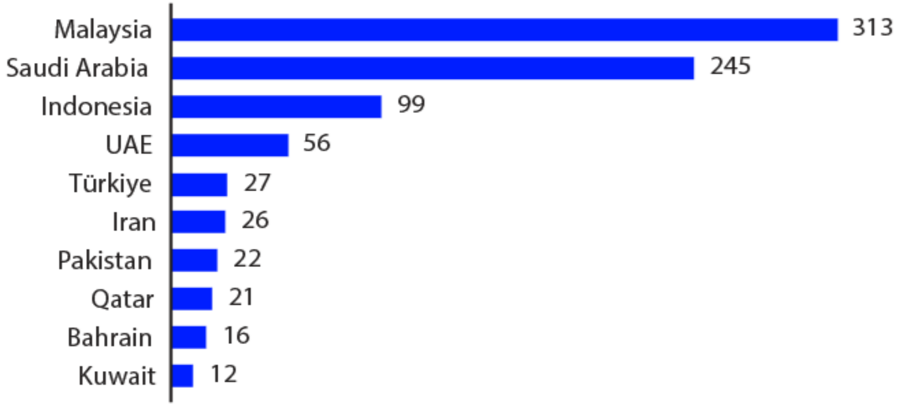
9%

Growth in Sukuk Value Outstanding in 2023

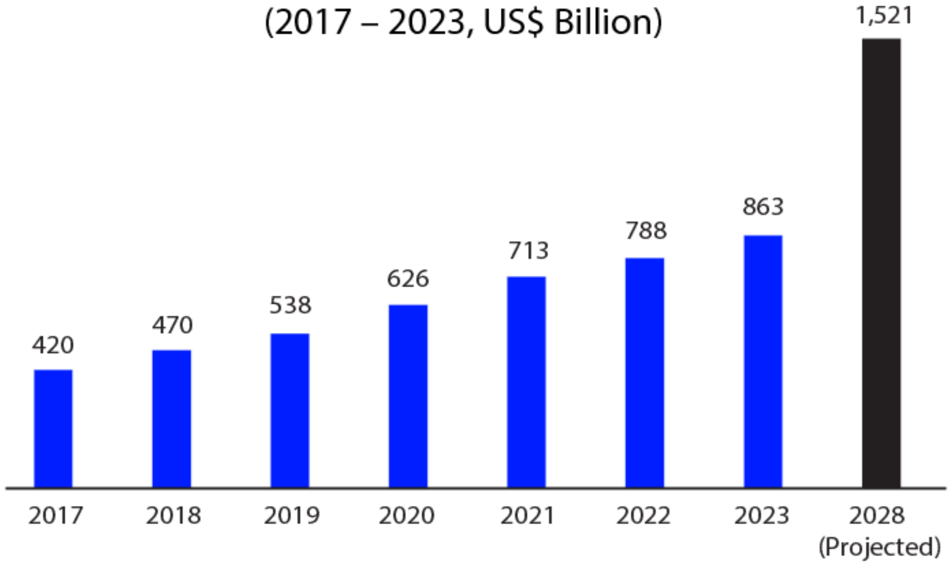
5,268

Number of Sukuk Outstanding

Top Countries in Sukuk Value Outstanding
(US$ Billion, 2023)



Sukuk Value Outstanding Growth
(2017 – 2023, US$ Billion)



Sukuk Outstanding by Region
(2023, US$ Billion)

Southeast Asia	414
GCC	359
Other MENA	30
Europe	28
South Asia	25
Sub - Saharan Africa	5
Other Asia	1
Americas	0.85

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Islamic Funds

US$254 Billion

Total Islamic Funds AuM Outstanding in 2023

16%

Growth in Islamic Funds Outstanding in 2023

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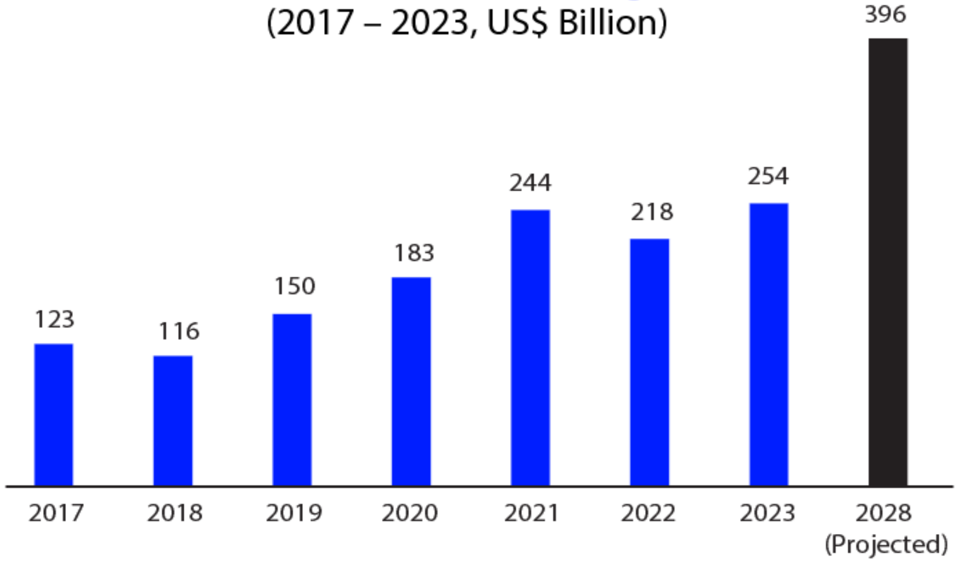
2,399

Number of Islamic Funds Outstanding

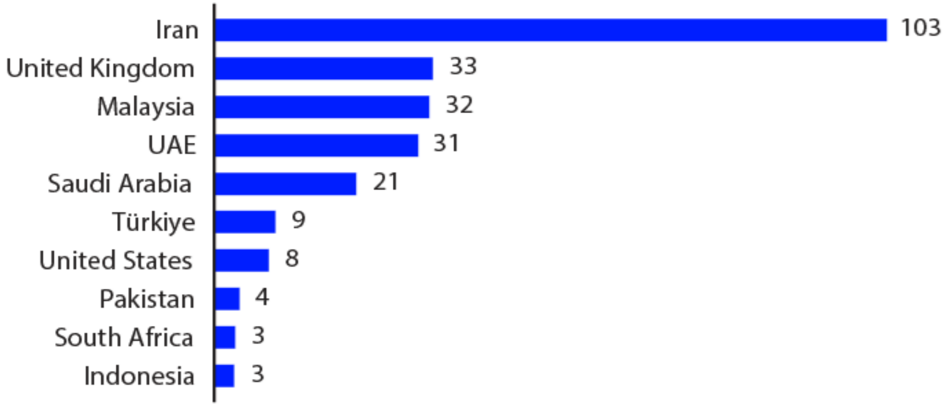
Islamic Funds AuM Outstanding Growth

(2017 – 2023, US$ Billion)



Top Countries in Islamic Funds AuM Outstanding

(US$ Billion, 2023)



Islamic Funds Outstanding by Region

(2023, US$ Billion)

Other MENA	103
Europe	46
GCC	54
Southeast Asia	36
Americas	9
South Asia	4
Sub - Saharan Africa	3
Other Asia	0.3

ICD - LSEG Islamic Finance Development Report 2024

Sustainability

US$35.9 Billion	US$8.0 Billion	50	48%	US$1.3 Billion
Total Value of ESG Sukuk Outstanding in 2023	Total Value of ESG Islamic Funds Outstanding in 2023	Number of Countries with Sustainability Guidelines	Average Sustainability Reporting Index Score by Public Islamic Banks	Total CSR Funds Disbursed in 2023

Top Countries in Sustainability Metrics (2023)

	CSR Funds		Sustainability Disclosure Index by Public Islamic Banks		ESG Sukuk		ESG Islamic Funds	
Ranking	Country	Amount Disbursed (USD Million)	Country	Score	Country	Value Outstanding (USD Million)	Country	Value Outstanding (USD Million)
1	Saudi Arabia	804	Malaysia	91%	Saudi Arabia	10,131	United States	6,665
2	Jordan	219	Oman	74%	Malaysia	9,851	Malaysia	830
3	Qatar	74	Pakistan	72%	Indonesia	7,362	Saudi Arabia	243
4	UAE	65	Indonesia	72%	UAE	6,904	United Kingdom	93
5	Kuwait	51	Sri Lanka	70%	Bahrain	900	Türkiye	56

ICD - LSEG Islamic Finance Development Report 2024

STRATEGIC OUTLOOK

SELF-EVALUATION…

IBF – has developed by leaps & bounds

Products	Market players	Asset size	Types of markets, etc.

But – criticism – it fails to achieve Maqasid Al-Shariah at the macro level

Is this true? Ideal vs Reality: IBF – works within conventional eco-system

Market infrastructure	Rules & regulation	Market norms & culture	Philosophies & value system

Lots of constraints & challenges in attaining its objectives

Commercial	Competitiveness	Attainment of MS

IBF is not perfect – lots of room for improvement

Islamic Finance Long-term Goals

To generate and develop equitable & just economic / financial system for the well-being of humanity & the world as a whole

VBI Initiative by BNM

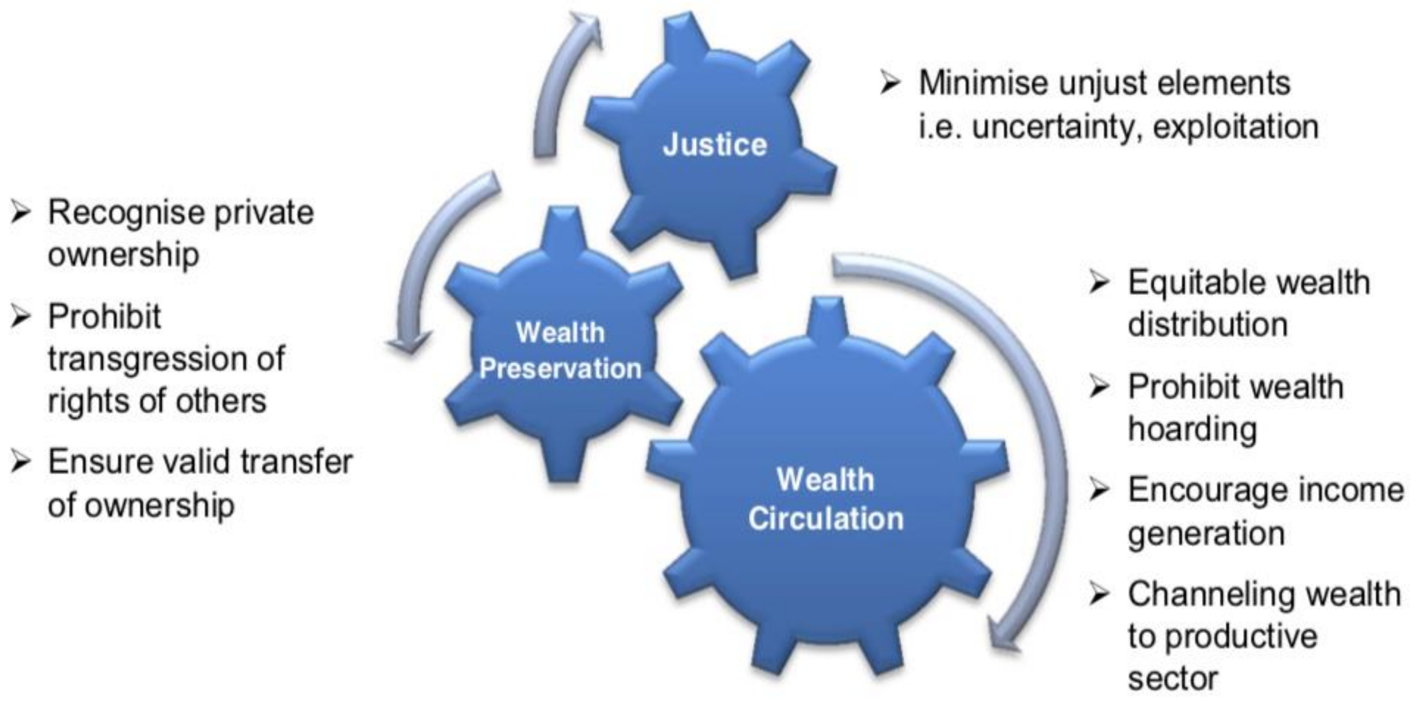
July 2017 – BNM issued a strategy paper on VBI

Further revised on 12 March 2018

Strategy Paper sets out the underpinning thrusts of VBI and proposed implementation approach & strategies in advancing **VBI as the next strategic direction** for Islamic banking industry

The Aspiration Underlying VBI

"An intermediation function that aims to deliver the intended outcomes of Shariah through practices, conduct and offerings that generate positive and sustainable impact to the economy, community and environment, without compromising the financial returns to shareholders"



The Intended Outcome of Shariah in Finance & Economics

VBI envisages Convergence Between Shari`ah & Commercial Goals

COMMERCIAL GOALS

SHARI`AH GOALS

VBI: A Paradigm Shift & Behavioral Concern

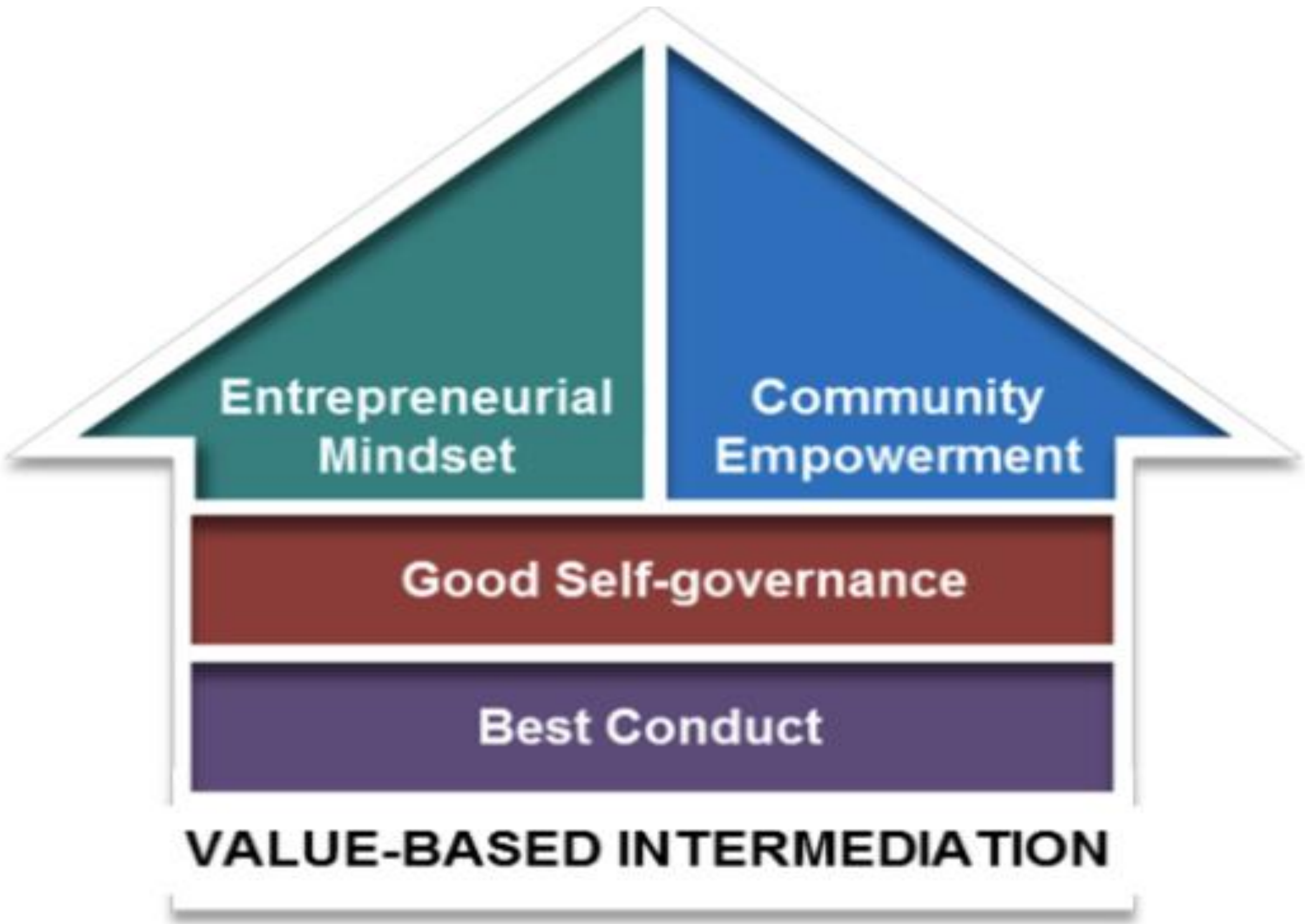
VBI – relook at the strategic future for IF – it is not just about profit – ethical dimension & responsible behaviour

VBI – integrate ethics into the behaviour of IF players:

- Establish guidelines & code of ethics
- Ensure application of code of ethics
- Develop ethical culture in IF

VBI is FINANCE 4 GOOD – positive impacts on economy, community & environment (3Ps)

Underpinning Thrusts of VBI: Blended with MS



Maqasid Shariah

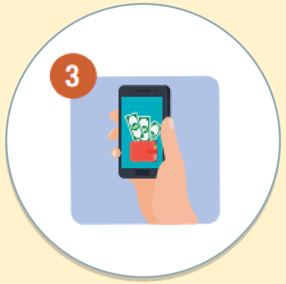
Sustainable way of providing financial services

Social Impact
vs
Profit Maximisation

5 Strategic Thrusts for 2022 – 2026

Fund Malaysia's Economic Transformation

Elevate Financial Well-being of Households & Businesses



Advance Digitalisation of The Financial Sector

Position Financial System to Facilitate An Orderly Transition to A Greener Economy

Advance Value-based Finance Through Islamic Finance Leadership

(Reference: BNM Financial Sector Blueprint 2022-2026)

The Expectations….

IF to help address economic challenges faced by the people & country

Focus – enhancing contribution of IF towards

facilitating economic recovery	building social resilience	promoting climate resilience	empowering trade, business & digital economy

Inclusive & diverse financial solutions

Source: BNM Annual Report 2020

MyWAKAF (2020)

A form of Islamic Blended Finance

Partnership with State Islamic Religious Councils (SIRCs) and social enterprises & NGOs

Unique Expertise	Knowledge	Resources

MyWakaf – digital cash waqf platform

Piloted by 6 Islamic banks	Involving 8 SIRCs	Raise funds totalling RM7.6 million by end of 2020

To finance impactful projects nationwide

Healthcare	Education	Community Empowerment

PRODUCTS FOR UNDERSERVED SEGMENT (2020)

- Benevolent microfinancing for B40 entrepreneurs – funded by donations (e.g. iTEKAD, BangKIT)
- Affordable financing programmes to build houses for zakat recipients
- Financial protection for hardcore poor families in the form of takaful riders using donation

ISLAMIC FINANCE PROMOTING CLIMATE RESILIENCE (2020)

Islamic finance driving sustainability & climate resilience agenda

Consistent with Shariah values – preventing harm & promoting attainment of benefits

Develop sectoral guides (finalised in 1Q 2021)

palm oil	renewable energy	energy efficiency

Financial system that supports sustainability & transition towards a low carbon economy

NEW PRODUCTS / SOLUTIONS: TAKAFUL

Adoption of VBI by Takaful Industry

↓

Innovative product offerings & services

Upgraded self-service customer touchpoints	Digitised system infrastructures

↓

Expansion of digitally-enabled health care & preventive services

Telemedicine	Wellness Apps	Wearables

↓

Digital offerings for traditionally excluded segments

Children with learning disabilities	Usage-based protection	Micro SMEs on e-commerce platforms

INHERENT SHARIAH PRINCIPLES: SUPPORTED BY UNIVERSAL VALUES IN ECONOMY & FINANCE

Economic & social aspirations towards SHARED PROSPERITY:
balanced, sustainable & inclusive economic growth

Other core values – e.g. Key thrusts of the VBI initiative

Best conduct & good self-governance	Entrepreneurial mindset & community empowerment

Facilitate the attainment of the intended objectives of the Shariah (Maqasid al-Shari’ah)

Justice	Wealth preservation	Wealth circulation

Realising the Specific Maqasid of Hifz Al-Mal

Protection
(حفظ الأموال)

Clarity (الوضوح)

Stability (الثبات)

Justice
(العدل في الأموال)

Available/ Accessible
(الرواج)

CONCLUSION: REPOSITIONING ISLAMIC FINANCE

Clear Value Propositions

Sustainable Policies & Actions

Positive impact on:

- Economy
- Community
- Environment

Attainment of Maqasid Al-Shariah