Islamic Finance news

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FRANCE

BNP Paribas push into Middle East

BNP Paribas has announced a retail banking drive in the GCC and neighbouring markets, with the aim of doubling assets under management in three years to US$10 billion.

Director of BNP Paribas Private Bank and Chairman of the Foundation BNP Paribas, Francois Debiesse, said the company was expanding its operations in Islamic finance: "We have got to become excellent professionals in Islamic banking. It is absolutely necessary and we think that without that we wouldn't be able to succeed in this region."

BNP will tie up with Islamic finance firms to develop Shariah compliant products, as well as using currently available instruments. BNP is using a Bahrain-based operation to run its foray into Islamic banking.

This expansion in the Middle East forms part of BNP's strategic expansion plan in the neighbouring region and Asia. The bank plans to have 381 branches in the Mediterranean Basin and the Gulf region and 58 in China.

SINGAPORE

SCB in first Shariah transaction

In Singapore's first Islamic financing transaction since the Monetary Authority allowed banks to offer Murabahah financing, Standard Chartered Bank (SCB) has concluded a US$96 million Islamic financing (Murabahah) facility for Baitak Asian Real Estate Fund I (Labuan) (BAREF).

BAREF is a US$600 million real estate fund launched by Kuwait Finance House Group, as fund manager and Shariah advisor, and the Singapore-based real estate investment, fund management and asset-management company Pacific Star Group, which provides investment management and asset management services.

Proceeds of this Murabahah facility will be used to fund the joint venture's first investment into a property development project in Kuala Lumpur.

BAHRAIN

Global Islamic accounting program

Bahrain-based Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI)'s global certification programme for accountants involved in the Islamic finance industry will open for registration soon.

The Certified Islamic Professional Accountant (CIPA) will be introduced in Malaysia and Bahrain, before going global. AAOIFI Senior Financial Analyst Syed Alwi Mohamed Sultan commented: "The program is structured to provide practitioners, mainly practising accountants, with a good grounding in areas such as Islamic economics and financial system, financial reporting for Islamic transactions, Islamic accounting and auditing standards, Islamic commercial law and Shariah standards."

It is hoped that the certification program will lead to a more highly skilled workforce in the Islamic finance industry

A similar certification program for Shariah advisers – the Certified Shariah Advisor (CeSA) – is planned for later on in 2006.

Inside Islamic Finance News:

NEWS BRIEFS

UAE (Dubai)

Omniyat Properties sells 50% stake to IIB

Almasa Holdings' newly launched property development arm – Omniyat Properties –has sold a 50% equity stake in its debut freehold property project to Bahrain-based International Investment Bank (IIB).

Omniyat Properties is to focus on creating the most technologically advanced properties in the Middle East region. Its first project is an US$80.04 million (Dh294 million) 30-storey high-tech commercial tower in Dubai's Business Bay.

QATAR

QIIB to enter Arab countries

The Qatar International Islamic Bank (QIIB) is examining the possibility of establishing Islamic banks in several Arab countries.

At the 9th Arab Business Forum QIIB's General Manager, Abdulbasit Al Sheibi, said Islamic banking was growing swiftly worldwide. The total assets of institutions providing Islamic products and services reach US$250 billion, or US$350 billion if Islamic banking windows are included.

BAHRAIN

Financial Trustees Bill delayed

Bahrain's Financial Trustees Bill, which will legalize trust funds and fund managers to attract Arab and foreign investments, has been postponed by the Chamber of Deputies.

It is hoped the bill, which will replace the regulations for trustees set by the Bahrain Monetary Agency (BMA), will enhance Bahrain's position as the regional hub of international financial and banking services.

MALAYSIA

Sime Darby's issuance attracts interest

Sime Darby issued the second offering from its existing Al Murabahah Commercial Paper and Medium-Term Notes Program, set up in December 2002. This US$132.32 million (RM500 million) 4-year Al Murabahah Medium Term Notes was sold with an Islamic profit yield of 4.30% pa.

CIMB and HSBC Bank Malaysia are joint lead managers/bookrunners for the issuance, which was very well received by investors, with final orders reaching US$555.75 million (RM2.1 billion).

BAHRAIN

US$1.5 billion development

Shariah compliant investment bank Arcapita has joined up with a Bahrain-based investment group to form Bahrain Bay Development, a joint venture which will oversee a US$1.5 billion development in Bahrain Bay.

The centrepiece of Bahrain Bay will be the Kingdom's first Four Seasons hotel in what is expected to be the tallest building in Bahrain. The 1.1million metre square project will contain a mixture of commercial, residential and retail space on the Manama waterfront.

NEWS BRIEFS

BAHRAIN

Fashion group lists IPO

Jawad International Fashion (JIF) is to offer 40% of its shares in an Initial Public Offering (IPO) to raise US$29.18 million (BD11 million).

A total of 10 million shares at US$2.92 (BD1.1) will be offered from the 19th December until the 8th January 2006, ahead of the company listing on the Bahrain Stock Exchange.

JIF, whose brands include BHS, Mango, Adams, Shoe City and Hush Puppies, has appointed Ahli United Bank, Bahrain Islamic Bank and Standard Chartered Bank.

PAKISTAN

Islamic financing for Ranhill project

Ranhill Power has received financing from the Asian Development Bank and Islamic Development Bank for its US$120 million hydropower joint venture project in Pakistan, the country's first private sector hydropower project.

Ranhill Power CEO, Wong Keng Cheong, confirmed that the IDB and ADB financing facilities (of US$37.3 million each) have been approved by the respective boards.

The IDB's Shariah compliant facility will be utilized to finance the project's plant and equipment on an Ijarah basis.

MALAYSIA

Al Rajhi enter Malaysia

Al Rajhi Banking & Investment Corporation, the largest Islamic bank in West Asia, will offer Shariah compliant banking services in Malaysia by April 2006.

Abdullah Sulaiman Al Rajhi, CEO of Al Rajhi revealed that: "The first branch will be operating by the second quarter of next year."

The first nine months of 2005 saw sales of Islamic bonds by Malaysian companies reach US$5.84 billion (RM21.9 billion). The country is opening its Islamic financial industry to overseas banks and has awarded Islamic banking licences to Islamic investment firm Kuwait Finance House, as well as a group of investors led by Qatar Islamic Bank.

PAKISTAN

Islamic IAS ready

International Accounting Standards (IAS) for the Islamic banking and financial reporting system will be issued by the Institute of Chartered Accountants of Pakistan (ICAP) on the 1st January 2006.

Chairman of ICAP Syed Mohammad Shabbar Zaidi said that the IAS, the first ever issued by a Muslim country, represents a landmark in the history of Islamic banking and finance.

The transparent standards incorporate international reporting standards and requirements to make them acceptable to professionals and regulatory bodies worldwide.

MALAYSIA

New credit guarantee scheme

Credit Guarantee Corp Malaysia (CGC) expects its Islamic guarantee scheme – Direct Access Guarantee Scheme-Islamic (DAGS-i) – to guarantee US$133.3 million (RM500 million) in 2006.

Datuk Wan Azhar Wan Ahmad, Managing Director of CGC said: "The RM500 million target is conservative but achievable as we want to give time for small and medium-sized enterprises (SMEs) to get acquainted with the scheme. Moving forward, we hope the amount will double or even triple."

DAGS-i was launched in Kuala Lumpur by the Deputy Governor of Bank Negara, Datuk Zamani Abdul Ghani, who commented that the scheme was a significant step to further promote growth of the country's Islamic finance system.

DAGS-i is the second Islamic guarantee scheme that CGC has offered. The first was its Islamic Banking Guarantee Scheme, introduced in 1997, which has accumulated total guarantees of US$60.59 million (RM227.2 million) to date.

NEWS BRIEFS

BAHRAIN

WIBC concludes with PowerTable

The 12th Annual World Islamic Banking Conference (WIBC) ended with an interactive "PowerTable" debate, which discussed new developments, challenges, risks and benefits of Islamic banking.

David McLean, Executive Director of WIBC, said that the PowerTable took dialogue between the audience and specialist panel to a new level: "The use for the first time of polling technology facilitated the unprecedented level of interactivity between the audience and the PowerTable panel."

The snapshot of the issues, priorities and effectiveness of the Islamic banking industry provided by the PowerTable resulted in an action list for next year, to be reviewed at the WIBC 2006.

A record-breaking number of delegates attended this 12th WIBC – over 700 from more than 30 countries were in attendance.

McKinsey Competitiveness Report

Islamic banks continue to grow much faster than their conventional counterparts, but their overall profitability is still lagging behind their conventional peers.

The McKinsey Competitiveness Report, revealed at the pre-conference briefings for the 12th World Islamic Banking Conference in Bahrain and entitled "Tracking an Industry in Transition," said 2004 had been yet another great year for Islamic banks, but these banks will have to meet high expectations to continue their strong growth and bridge their profitability gap.

Islamic banks will have to develop more sophisticated offerings and appeal to a broader consumer base in order to capture the consumer banking market. The report stated: "So far Islamic banks have managed to capture customers who have a strong preference for Shariah compliant products. Going forward, they will have to broaden their appeal to customers who are interested in Shariah compliant products but are not ready to sacrifice returns, service or convenience."

Islamic banks must, therefore, improve their service levels, network convenience and staff knowledge while developing critical enablers such as operations, risk management and people management.

The objective of the McKinsey Competitiveness Report is to examine trends in Islamic banking and chart ways to help the industry sustain its momentum.

Investment in resources key

Islamic finance institutions must invest resources in infrastructure development if they are to continue to encourage further growth and innovation across the industry.

Abdulhakeem Alkhayyat, the General Manager of Kuwait Finance House (KFH), addressed the audience at the 12th Annual World Islamic Banking Conference (WIBC) in Bahrain about the opportunities for financial institutions, highlighting areas of focus to ensure ongoing innovation and growth across the entire industry.

"By nature, Islamic financial instuitions must be innovative. Not only is this a new industry, in relative terms, but Islamic banks have also had to learn to operate and adapt in regulatory and other environments that are not necessarily tailored to meet their needs and methods of operation and furthermore and importantly we must always operate within the confines of Shariah standards. With this in mind, Islamic financial institutions have had to be extremely innovative in order to meet these challenges and thus bring the industry to where it is now.

"Nevertheless, while we have seen significant progress to date, it is critical that today banks in our industry also look at a number of internal factors and dedicate the necessary resources to further developing their infrastructure so that there are strong engines in place that are capable of driving further growth and innovation across the industry for the benefit of investors, shareholders and the economies in which we invest and operate."

IRAN

Murabahah for Esfahan Steel

ABC Islamic Bank and Emirates Islamic Bank have announced the joint mandate for a US$70 million, three-year Murabahah Financing Facility for Iranian Esfahan Steel Company.

Guaranteed by the Iranian Mines and Mining Industries Development and Renovation Organization, the facility has a margin of 3.48% per annum with the top ticket fees of 1%.

The proceeds from this facility will be utilized to finance the purchase of raw materials, machinery and equipment for the completion of the Coking Coal Production Expansion Project.

BAHRAIN

US$150m real estate fund launched

Bahrain-based Unicorn Investment Bank (UIB) and Abu Dhabi Holding Company have joined to launch a new US$150 million real estate fund: the three-year, closed-ended, Shariah compliant Gulf Springs Real Estate Fund.

UIB and Abu Dhabi Holding Company will be founding investors in the fund and will select banks in each GCC country to assist with distribution, as well as linking up with real estate companies in each GCC country to invest in real estate projects.

The fund's strategy is to mix real estate projects and sectors across the GCC to gain diversified income generation. At least 80% of asset allocation will be made inside the GCC region, including low to middle income residential developments in Saudi Arabia; tourist developments in Abu Dhabi, Sharjah and Oman; office developments in Bahrain; infrastructure projects in Qatar and retail space and offices in Kuwait.

MALAYSIA

Japanese financing through RHB Bank

RHB Bank has signed a memorandum of understanding with the Japan Bank for International Cooperation (JBIC) to receive US$100 million (RM375 million) in financing for the small and medium industries (SMI) sector in Malaysia.

JBIC, the second largest financial institution in the world after the World Bank, will extend the Two-Step Untied Loan to RHB Bank, which will then disburse the loan to Malaysian SMIs.

Deputy Chairman of RHB Bank, Dato' Abdullah Mat Noh, commented: "The new facility will further strengthen the SMI sector and help boost Malaysia's exports in the long term."

NEWS BRIEFS

UAE (Dubai)

DIFC Council to develop Islamic benchmarks

An Islamic Finance Advisory Council comprising key industry figures has been established to work with the Dubai International Financial Centre (DIFC) to develop Islamic finance in general, and to develop international benchmarks for the industry.

The Council will provide strategic advice on the development of the industry; forecast future trends; and highlight the impact of legal and regulatory initiatives on the Islamic finance market within the DIFC.

Omar Bin Sulaiman, Director General of the DIFC, stated: "One of the challenges for Islamic finance today is that it doesn't have international benchmarks. You have different models, you have a Bahrain model, you have the rest of GCC and you now have the western model."

Sulaiman expressed doubts as to whether the recent growth in Islamic banking could be sustained in the event of a downturn: "Islamic finance is not just for Muslims, it is for everybody. For this industry to grow in the future, you need to create one model so that non-Muslims know how to deal with it," Sulaiman said.

The DIFC is hoping to attract Islamic finance firms to it, as well as the top international securities firms such as HSBC, Deutsche Bank and Credit Suisse, who have been attracted by the international regulation of the DIFC.

SAUDI ARABIA

Prince calls for more Islamic banks

Prince Salman, the Governor of Riyadh, has emphasized the need for more Shariah based financial institutions to be established. The Prince was speaking at the official opening of Bank Albilad, Saudi Arabia's 14th bank.

Bank Albilad obtained a licence to operate as a Saudi joint stock company by a royal decree in 2004 with a capital of US$799.88 million (SR3 billion). Last year the bank offered half of its 60 million shares for public offering in the Kingdom's largest IPO offering.

BAHRAIN

Centre for Islamic Finance Studies

A new centre for Islamic finance education, training and research has been launched in Bahrain.

"The centre's mission, which will start operations in January 2006, is to be a leader in providing training, education and research in the Islamic banking and finance field, in order to better serve the global Islamic finance industry and further strengthen Bahrain's position as the world's Islamic finance hub," said Governor of the Bahrain Monetary Agency Rasheed Mohammad Al Maraj.

It is hoped that the degree programmes will lead to a new generation of professionally and technically qualified Islamic bankers and professionals. Key educational initiatives of the centre include specialized professional programmes such as the Certified Shariah Scholar, the Certified Shariah Auditor and the Certified Islamic Accountant. An international accreditation board is planned, in conjunction with Islamic finance industry organizations, to set standards for and endorse these professional programs.

In terms of research, the centre aims to stimulate product innovation by concentrating on the practical aspects of Islamic banking and finance.

BAHRAIN

Islamic clearing firm licenced

A licence for an Islamic broking company has been granted by the Bahrain Monetary Agency (BMA) to Global Islamic Clearing Company (GICC), a joint venture between Bahrain-based Islamic Finance Consultants (IFC) and UK-based financial services firm, Dawnay Day Global Investment.

GICC, based in Bahrain, will undertake Islamic assets facilitation and liquidity clearing in the region. At present liquidity management by Islamic banks is largely completed via brokers in London.

Ahmed Al Bassam, Director of Licensing and Policy at the BMA said: "The establishment of the GICC will add greater sophistication to the Islamic banking industry and will add value to the development of Bahrain as a well-rounded and mature centre for Islamic banking and finance."

The BMA has also granted a licence for an Islamic investment advisory/consultancy firm specializing in structuring Islamic commodity funds. The proposed firm will offer technical support relating to the structure and acceptability of trade and commodity transactions in compliance with Shariah principles.

BAHRAIN

ABG solid growth

The Albaraka Banking Group (ABG) has posted strong growth in assets, operating income and net profit for the first nine months of 2005.

Total operating income rose to US$275.1 million for the first nine months of 2005, reflecting an increase of US$68.8 million (33.4%) in the total operating profit during the third quarter of this year.

Net operating income was US$69.2 million during the first nine months of 2005, up 15.1%, as against US$60.1 million for the whole of 2004. Total assets at the end of September 2005 were US$5.8 billion, compared to US$5.1 billion as at the end of December 2004 (a 13.7% increase).

Shaikh Saleh Kamel, Chairman of the Board of Directors, said that ABG planned to expand its shareholder base through an Initial Public Offering early in 2006. The group's shares will then be listed on the Bahrain stock exchange, amongst others.

MALAYSIA

Dana Ikhlas distribution

Mayban Unit Trust's Islamic Balance Fund – Mayban Dana Ikhlas – has declared an annual gross distribution of US$0.0066 (RM0.025) per unit, representing a gross distribution of over US$1.1 million (RM4.12 million) to 5,580 unit holders for the year ended on the 30th November 2005.

Chief Executive Officer of Mayban Unit Trust, Shamsuddin Bahari, said the gross distribution represented an annualized yield of 5.45% for Dana Ikhlas, a good yield when compared with its peers.

The distribution entitlements will be given to all unit holders on the register and tax vouchers will be dispatched with the annual report in January.

Dana Ikhlas aims to achieve a mixture of regular income stream and possible capital growth through investments in listed equities, debt instruments and other assets which comply with Shariah principles.

NEWS BRIEFS

BAHRAIN

Standards for Islamic banking

The Governor of the Bahrain Monetary Agency Rasheed Al Maraj has made calls for greater standardization and regulation so that Islamic banks can maintain the stability and integrity of the financial system, protect customers from fraud and improve the efficiency of the financial system.

In his opening address to the 12th World Islamic Banking Conference, Al Maraj stressed that Islamic banks cannot match conventional banking without implementing greater standardization.

On the sidelines of the conference Al Maraj also said that the GCC monetary union would be established according to schedule by 2010: "All GCC countries have been working very hard to meet the set deadline. However, given the sensitivity of the subject, all countries are working closely to reach a consensus on various issues. The GCC monetary union and single-market concepts will usher in a new era of development in the region."

BAHRAIN

Bahrain exception to the rule

Bahrain's Islamic banking industry is growing at a slower pace than the banking sector as a whole, in contrast to Islamic banking in other countries.

The McKinsey Competitiveness Report – "Tracking an Industry in Transition" – undertook research comparing the growth of major Islamic banks in Bahrain, Indonesia, Jordan, Kuwait, Malaysia, Qatar, Saudi Arabia and the UAE, with that of banking in general. In each country Islamic banks were growing at an increased rate, except in Bahrain, where Islamic banks were found to be growing at a slower rate than the 9.9% asset growth of the sector for 2000–2004.

Partner at McKinsey and Company Nasr Benaissa said that: "Islamic banks have a higher penetration rate in Bahrain than they do in most other countries. The fact that the Islamic banking sector is already established here rather than still penetrating the market may be a factor."

MALAYSIA

Market to all sectors

Malaysia's largest bank, Maybank, has stressed the need to market its products and services for Islamic as well as conventional banking.

Deputy President of the bank Agil Natt stressed the need of marketing the Islamic designed products in different markets across the world: "The notion that the Islamic products are only meant for the Muslim customers is not based on fact as currently 45% of Islamic banks' account holders are non-Muslims showing the appetite of the market."

"In Malaysia, when we launched various deposit products, there was a huge response from all communities showing a real need of Islamically designed products to bridge the huge gaps between the products and customer needs."

Agil Natt continued: "We need to concentrate on three areas namely regulatory regime, legislation and structure – the combination of these three pillars are required to provide a strong platform for the Islamic banking industry. The issue of universal acceptability is also very important."

UAE (Abu Dhabi)

Proposed risk management standards

New international standards for better risk management in Islamic banking are set to be approved, according to the Chairman of Dubai Islamic Bank's Shariah Board, Dr Hussain Hamid Hassan.

"There will be new standards for risk management, new standards for capital adequacy ratio and the new role of the Central Banks in regulating Islamic banks. The proposals, prepared by the Islamic Financial Services Board in Malaysia are ready for approval and will be put up before the Central Bank governors of Islamic countries in Jeddah later this week," he said, expressing his confidence that the proposals will be approved.

NEWS BRIEFS

MALAYSIA

Islamic banks urged to seek international rating

Obtaining an international rating may help Islamic banks in Malaysia to dispel the perception that Islamic banks lack transparency.

Director for Asian Financial Institutions at Fitch Ratings, Ambreesh Srivastava, has stated that even though Malaysian banks may not suffer from the lack of supervision and regulations of Islamic banks elsewhere, an international rating may still prove useful, as it results in increased investor confidence.

Ambreesh said: "For the moment, none of Malaysia's Islamic banks have sought a rating from us," although being rated is gaining momentum among Islamic banks in the region.

UAE (Dubai)

EIB branches out with priority banking

Emirates Islamic Bank (EIB) has launched Ethmar, its new priority banking service targeted at wealthy clients.

Ethmar will provide high net worth individuals with an exclusive, personalized service with superior standards of reliability and confidentiality. It comes with a package of benefits tailored individually to each Ethmar customer. A dedicated relationship manager will oversee the client's account and help manage their finances.

Ethmar customers will also benefit from perks such as access to the first class lounge at Dubai International Airport and limo transfers.

EIB also has plans to double its branch network, with 12 new branches within a year, in the hope of extending its market share and luring Muslim customers away from conventional banks

Customer deposits at the bank have grown 100% in the past year, compared to industry growth of just 30–40%. EIB reported a 51.6% rise in net profit in the nine months to September to US$8.79 million (Dh32.3 million), with total income over doubling to US$33.24 million (Dh122.1 million).

The bank has called an extraordinary shareholders' meeting for the 21st December to discuss a 10-for-one stock split and a 30% bonus share issue.

UAE (Dubai)

PCFC Sukuk to list on DIFX

Dubai's Ports Customs and Free Zone Corporation (PCFC) will list a US$2.72 billion (Dh10 billion) Sukuk issue on the Dubai International Financial Exchange (DIFX) in the coming months.

The last issue of *Islamic Finance News* reported how PCFC's bid for the British ports, ferries and property group P&O includes a US$2.8 billion Sukuk issue, which is expected to raise between US$4 billion and US$5 billion and will be listed on the DIFX in two months.

Lead-managed by Dubai Islamic Bank (DIB) and Barclays Capital, the Sukuk has received an excellent response from investors, and is predicted to be oversubscribed by at least 50–75%.

Last week there was thought to be uncertainty over the bid, due to speculation over a possible rival bid from Singapore's Temasek Holdings.

UAE (Abu Dhabi)

Governor calls for transparency

The Governor of UAE's Central Bank – Sultan bin Nasser Al Suwaidi – has warned that despite the strong growth of Islamic banking, its exposure to real estate, leasing and trading also poses serious concerns to the regulators for their "inherent and liquidity risks."

"The regulating authorities also require more transparency about the institutions' strategy and performance for effective and prudent regulation," he stated.

Over the last quarter of a century Islamic banks have grown tremendously, with assets now exceeding US$250 billion: "The Islamic financial services industry is growing at 15% against less than 10% by the conventional banks," the Governor said. However, lack of consistency among Islamic scholars shows a need to standardize the rules and regulations based on the Shariah.

BAHRAIN

Islamic repo for secondary Sukuk mart?

Bahrain-based Noriba Bank is developing an Islamic version of a repurchase agreement which it hopes will stimulate the secondary market for Sukuk and thus help Islamic banks to create liquidity.

Repurchase agreement contracts let investors borrow money by selling securities and simultaneously promising to buy them back at a higher price, at a specified time. Some Shariah scholars see the speculation involved in such agreements as highly un-Islamic. The price difference between the transactions (repo rate) is seen to contravene the Islamic ban on borrowing and lending on interest.

Ismail Dadabhoy, Head of Institutional Banking at Noriba, said repos were essential if banks were to deepen the secondary market for Islamic bonds. He added that Noriba was trying to get a repo contract approved by its Shariah Advisory Board by 2006.

MALAYSIA

Islamic banking retains integrity

Malaysia's Islamic banking industry will not be damaged by minor setbacks such as Bank Islam Malaysia's recent losses, according to Dr Mohd Ishak Ismail, Chief Executive of the Malaysian Institute of Corporate Governance.

The sound Islamic banking system and good industry supervision points towards a good future for the sector: "Bank Negara, the Securities Commission and Bursa Malaysia have played their regulatory roles effectively."

Malaysia's first Islamic bank, Bank Islam, made losses of US$120.93 million (RM456 million) for the year ending on the 30th June 2005. Dr Mohd Ishak Ismail commented that these losses "could have happened because of factors beyond the jurisdiction of the bank's management and the industry's watchdog."

NEWS BRIEFS

SYRIA

ICS partners Arab Bank-Syria

Arab Bank-Syria, part of the international Arab Bank Group, has named International Computer Systems (London) (ICS) as its technology partner to provide the bank with a complete banking solutions.

ICS is a leading International IT Solutions company providing complete IT services project cycles from initial consultancy to design, development, implementation, and ongoing maintenance and support. ICS has been chosen because of the strength and sophistication of the solutions they offer to a wide range of countries and regions.

BAHRAIN

Ithmaar to launch IPO

Ithmaar Bank, a wholly-owned subsidiary of Daar Almaal Islami, will launch its Initial Public Offering (IPO) early in 2006.

The Chairman of Ithmaar Bank's Board of Directors, Khalid Abdullah Janahia, said: "Ithmaar's strength comes from its subsidiaries and affiliates engaged in Shariah compliant finance, investments and insurance through a range of businesses including retail, commercial and investment banking as well as Takaful, leasing and asset management. The IPO would help establish the bank as a major player in the GCC market."

Ithmaar also proposes to reconstitute itself as a Bahrain shareholding company, issuing an additional 150 million shares, at US$1 per share par value, through one of the largest IPOs by any investment bank in Bahrain and listing itself on the Bahrain Stock Exchange.

MALAYSIA

Banks: tap Islamic finance mart

The Governor of Bank Negara Tan Sri Dr Zeti Akhtar Aziz has urged merchant banks to take advantage of the opportunities that the expansion of Islamic finance and the demand for Islamic financial assets has brought about, both nationally and internationally.

Speaking at the 26th annual dinner of the Association of Merchant Banks in Kuala Lumpur, Zeti said that although Malaysia had a head-start in the Islamic banking industry, Malaysian financial players had still not made the most of the unprecedented growth in the industry.

"As Islamic financial products increase in sophistication, a higher level of competencies, skills structuring abilities of the merchant banking community would be needed. If Malaysia could emerge as a supplier of these high-end services, the nature of merchant banking would change significantly," the Governor commented.

UAE (Abu Dhabi)

Khorfakkan branch for ADIB

Abu Dhabi Islamic Bank (ADIB) has added to its 19 branches across the Emirates with a new full service branch in Khorfakkan.

The Khorfakan branch will offer the full range of Shariah compliant banking services, including its Shariah compliant covered credit card, car loans and a 24-hour ATM.

NEWS BRIEFS

BAHRAIN

IIB invests in Business Bay

Bahrian-based International Investment Bank (IIB) has announced it will take a 50% equity stake in an US$80 million investment in a yet to be constructed office tower in the swiftly developing Business Bay district of Dubai.

IIB is currently placing a portion of this investment with GCC investors, where it has so far received a positive response.

Acting CEO of IIB Aabed Al Zeera commented that this transaction is an example of the Bank's range of Shariah compliant investments that are diversified by asset class and location. The office real estate market in Dubai offers attractive growth potential.

IIB was established in October 2003 with an authorized capital of US$200 million, of which US$43 million has been issued and fully paid. Its shareholders are leading business houses and institutions from across the GCC.

BAHRAIN

Al Basha'er Fund record-breaker

The Al Basha'er GCC Equity Fund has broken all records for funds of its kind, exceeding its target by US$140 million, and raising more than US$540 million from regional investors.

The Shariah compliant open-ended fund was jointly launched by Gulf Finance House, Kuwait Finance and Investment Company and Qatar Islamic Bank on the 9th October 2005, closing on the 24th November. It will now re-open in January, offering monthly subscriptions and redemptions.

The minimum initial subscription in the fund, which offers investors the opportunity of participating in the growth of the region's capital markets, is US$10,000, followed by subsequent investments of US$1,000.

QATAR

New HSBC office in QFC

HSBC Bank Middle East will open an office in the Qatar Financial Centre early in 2006, according to Chief Executive of the HBME unit David Hodgkinson.

MALAYSIA

CIMB seeking partners

CIMB Private Banking head, Alan Inn, has announced it is looking to form more strategic partnerships.

CIMB Private Banking, which currently manages assets worth US$688.2 million (RM2.6 billion), also wants to add to its existing product range with more innovative products.

UAE (Dubai)

Rasmala Investments joins DIFC

Rasmala Investments has been licensed by the Dubai Financial Service Authority (DFSA) as an authorized firm in the Dubai International Financial Centre (DIFC). The investment firm is awaiting approval to operate as a regulated subsidiary.

QATAR

QIIB takes on SMS services

Qatar International Islamic Bank (QIIB) has formed an agreement with the provider of electronic payment solutions Arab Financial Services (AFS) to provide the bank's cardholders with AFS's Smart Alert Card SMS Service.

The Smart Alert Card SMS Service will enable QIIB to communicate information, such as authorizations, fraud alerts, customer service, billing, payment and marketing to its cardholders efficiently.

This meets the customer's requirement for instant access to information and will also help QIIB to minimize fraud, provide enhanced customer services, improve customer loyalty and increase sales.

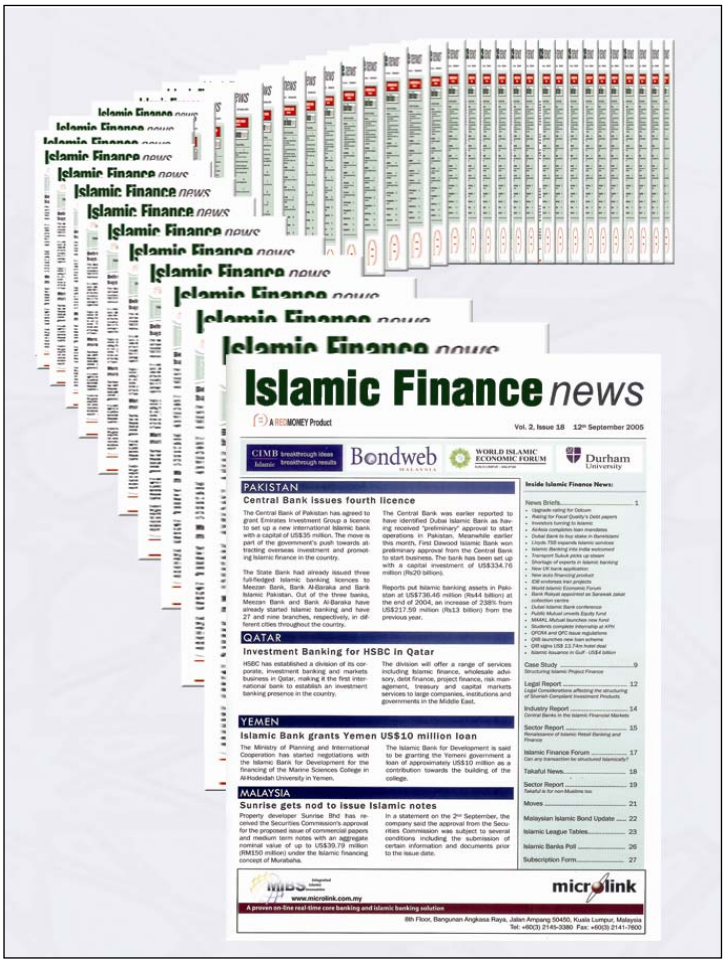
KUWAIT

Investment Dar 5-year plan

Investment Dar has almost completed a 5-year company strategy for 2004–2008.

Investment Dar CEO Adnan Al Musalem has indicated that the 5-year plan will state that the company's investments will be distributed on qualitative, sectorial and geographic bases.

Al Musalem said that Investment Dar had recently purchased 30% of the Rahal Company for logistical back-up. Since 2003 Investment Dar has taken over the Al Mal Islamic company, which became the Al Madar company. In addition, it has acquired 30% of the Bahrain Islamic Bank and 40% of the Withaq Takaful Insurance company.



NEWS BRIEFS

Ratings Update

MALAYSIA

RAM rates Touch Matrix's Islamic debt

Touch Matrix's proposed US$16 million (RM60 million) Murabahah Islamic Medium-Term Notes (IMTN) Programme has been assigned a long-term rating of AA3 with a stable outlook by Rating Agency Malaysia (RAM).

Touch Matrix, a provider of telecommunication infrastructure facilities, has been licensed by Maxis Broadband, Celcom (Malaysia) and Digi Telecommunications to construct and license the use of towers to these companies.

The rating reflects Touch Matrix's envisaged ability to comfortably meet all its financial commitments under the proposed IMTN Programme. Moderating the rating is Touch Matrix's short operating track record and the (low) pre-completion risks involved in the project.

Ingress Sukuk's rating affirmed

Ingress Sukuk has had the rating of A+ID on its US$42.65 million (RM160 million) Sukuk Al Ijarah issuance affirmed by MARC.

Ingress Corporation's track record as a leading local automotive component manufacturer with a good financial profile has influenced this rating. Moderating the rating were the susceptibility of the automotive industry and the manufacturing sector to economic changes, in addition to the growing competition from trade liberalization.

The Group supplies Perodua and Proton in Malaysia, as well as General Motors/Isuzu, Ford/Mazda, Mitsubishi and Honda.

Amat Suria's MUNIF rated

A short-term rating of P2 has been given by RAM to Amat Suria's proposed US$10.67 million (RM40 million) Murabahah Underwritten Notes Issuance Facility.

Amat Suria was established to facilitate the purchase of MCB Industries from its current owner, Regal Horizon. Therefore the debt servicing ability of Amat Suria depends on MCB. MCB manufactures integrated lime, primarily producing calcium carbide, and holds a 95% share of the calcium carbide market in Malaysia.

MCB's strong market position, coupled with the high regional demand for calcium carbide and a guaranteed supply of raw materials from the company's own limestone quarry, have influenced this rating.

RAM reaffirms Nestle's ratings

The long-term rating of AAA and short-term rating of P1 have been reaffirmed by RAM for Nestle Foods (Malaysia)'s US$186.68 million (RM700 million) Al Murabahah Commercial Papers/Medium-Term Notes Programme (CP/MTN), with a stable outlook. The issuance is backed by a corporate guarantee from the parent company of Nestle Foods – Nestle (Malaysia) Group.

Although Nestle Foods have ceased manufacturing operations following the consolidation of the group's wholly owned manufacturing subsidiaries, because the CP/MTN is backed by Nestle Malaysia, this has no impact on the company's ratings or credit profile. Thus the AAA/P1 ratings continue to reflect the credit profile of Nestle Malaysia.

Vastalux Capital Islamic securities rated AA-IS

Malaysia Rating Corporation (MARC) has assigned a rating of AA-IS to Vastalux Capital (VC)'s Musharakah Mutanaqisah (Sukuk Musharakah) US$26.63 million (RM100 million) Islamic securities.

VC is a special purpose company wholly owned by Vastalux and incorporated in order to provide financing to Vastalux. Under this proposed transaction, VC will act as an agent (wakil) for potential Sukuk investors in order to invest their capital contribution on their behalf in identified contracts.

This rating mirrors: the strong credit risk of Petronas Carigali, the offtaker; a protective issue structure; Vastalux's reliability; and the manageable performance risk of the contracts.

MARC rates Guthrie's CPs

Kumpulan Guthrie's proposed US$39.99 million (RM150 million) Underwritten Murabahah Commercial Papers have been given a short-term rating of MARC-1ID.

The group is a leading plantation player/property developer in Malaysia, with a sound financial profile based on its large asset base and good financial flexibility. One factor moderating the rating is the cross-border implications of the group's operations in Indonesia.

Emas Kiara's MUNIF/IMTNs rated

The US$21.33 million (RM80 million) Partially Underwritten Murabahah Notes Issuance Facility/Islamic Medium-Term Notes Issuance Facility (MUNIF/IMTN) Programme of Emas Kiara Industries has been assigned a rating of A+ID/MARC-2ID by MARC.

Emas Kiara Industries is an investment holding company with subsidiaries involved in manufacturing and trading geosynthetic and industrial textile products and providing design and installation services to customers. It is now the domestic leader in manufacturing geosynthetic products, with continuing revenue growth.

MARC's rating reflects Emas Kiara Industries' leading market position; the stable, foreseeable increase in demand for its products both domestically and regionally; stable operating margins and low debt leverage position. Factors moderating the rating include the competition within the industry; end users' receptiveness to the products and the potential increase in the price of resin.

Encorp Systembilt downgrade

Further to the story in the last issue of *Islamic Finance News*, RAM has announced that the US$349.45 million (RM1,321 million) Al-Bai Bithaman Ajil Notes Issuance Facility (ABBA Notes) (Tranche 1), US$134.91 million (RM510 million) ABBA Notes (Tranche 2), US$66.14 million (RM250 million) ABBA Notes (Tranche 3) and US$176.46 million (RM667 million) ABBA Notes (Tranche 4) of Encorp Systembilt have been downgraded from AA2(s) to A1(s). The negative outlook on the ratings has been maintained.

The rating watch was the result of irregularities in the concession payments from the Government of Malaysia. This downgrading reflects the uncertainty surrounding the company's claims on additional works, which has heightened the credit risk of the company.

INDUSTRY REPORT

Governance Issues and Islamic Banking

By Professor Bala Shanmugam

Introduction

Corporate governance refers to the method by which a corporation is directed, administered or controlled. It includes the laws and customs affecting management, as well as the company's goals. Corporate governance mechanisms and controls are designed to reduce the inefficiency that results from moral hazard and adverse selection. It is also a process of monitoring performance by applying appropriate counter-measures and dealing with concepts such as transparency, integrity and accountability.

Corporate governance requires corporations to exercise accountability to their shareholders and the public, and also monitors management. Corporate governance is normally divided into two categories: self-governance and statutory regulation. Self-regulation involves the aspects of corporate governance that are difficult to legislate for, especially those involving a human element, such as the independence of the Board of Directors, its relationship with management and appraisal of directors' performance (Nordin, 2002). Statutory regulation is the framework of corporate governance that can be explained in legal terms. Legislative and regulatory rules include:

(a) Duties, obligations, rights and liabilities of directors, controlling shareholders and company officers.
(b) Disclosure and transparency.

In Malaysia, statutory regulations covering corporate governance are:

(a) Companies Act 1965.
(b) Securities Industry Act 1983.
(c) Securities Commission Act 1993 and Securities Commission Policy & Guidelines.
(d) KLSE Listing Requirements.

Good corporate governance is considered essential because it promotes morality, honesty, integrity, trust, openness, performance orientation, responsibility and accountability, mutual respect and commitment to the organization from everyone involved. Corporate governance does not only apply to directors and executives, but to all players in an organization.

Banks and corporate governance

Having established a broad understanding of the concept of corporate governance, let us attempt to fit this into an Islamic banking paradigm. Even within the conventional system corporate governance is a thorny issue, as banks have certain characteristics unique to them, including first, banks are generally more opaque than other financial institutions, which intensifies the agency problem. Secondly, banks are exposed to extreme regulations; and thirdly, government ownership makes the governance of banks different from other types of organization (Levine, 2003).

When banks employ sound governance mechanisms, they efficiently mobilize and allocate funds, thus lowering the cost of capital to firms, boosting capital formation and thus stimulating productivity growth. In contrast, weak governance of banks reverberates throughout the entire economy, with negative ramifications for economic development. (Claessens, 2003).

Islam and corporate governance

Strong corporate and bank governance are essential ingredients for the development of a vibrant and sound Islamic finance industry. Corporate governance is not new to Islam. As pointed out by Mustapha and Salleh (2002), the Islamic concept of corporate governance emphasizes the three main areas of accountability, transparency and trustworthiness (Mustapha and Salleh, 2002).

The Holy Prophet Muhammad (Pbuh) said (as related by Bukhari and Muslim): "Each one of you is a guardian and each guardian is accountable to everything under his care." This underlines the importance of people being accountable for their actions.

As for transparency, Surah Al-Baqarah (verse 282) of the Holy Qu'ran states:

> "O you who believe! When you contract a debt for a fixed period, write it down. Let a scribe write it down in justice between you. You should not become weary to write your contract down, whether large or small, for its fixed term, that is more just with Allah, more solid as evidence and more convenient to prevent doubts among yourselves ... Take witness whenever you enter into a commercial contract."

This verse emphasizes the need to record every transaction in order to avoid injustice and to conceal any details that might lead to further injustice.

In highlighting trustworthiness, the Qu'ran states in Surah Al-Anfal (verse 27): "O ye that believe! Betray not the trust of God and the Apostle, nor misappropriate knowingly things entrusted to you."

Islam looks into the essence of responsibility, the concepts of work, dedication to work and vicegerency or trusteeship. This gives Islamic corporate governance a very comprehensive coverage. Responsibility not only involves being responsible towards other people, but also in performing one's role in life. This role is given as an amanah (trust) from God and should this responsibility be neglected, it is a form of khianat (betrayal) to God. The concept of work and dedication to work is a form of ibadah (worship) and amal salih (virtuous act). In addition, khilafah (trusteeship) emphasizes that the qualities of a good Islamic manager are also the qualities of a practising Muslim.

The need to follow these corporate governance requirements is given greater weight, especially for god-fearing persons, by linking the practices to God.

In relation to trusteeship, the Holy Prophet Muhammad (Pbuh) once said:

> "Every one of you is a keeper or a shepherd and will be questioned about the well-being of his fold. So, the Head of the State will be questioned about the well-being of the people of the State. Every man is a shepherd to his family and will be answerable about every member of it. Every woman is a shepherd to the family of her husband and will be accountable for every member of it, and every servant [employee] is a shepherd to his master [employer] and will be questioned about the property of his master." (Abod, 2002)

Another commandment for Muslims is the concept of tawhid, which promotes the need to submit fully to God. It highlights the unique and distinguished relationship between man and Allah and also prevents men from behaving in a way that is harmful to other living things.

Continued...

INDUSTRY REPORT

Governance Issues and Islamic Banking *(continued...)*

By enforcing full submission to the Creator (tawhid) and by insisting that the Creator expects trustworthiness, transparency and responsibility in all dealings, corporate governance is given a spiritual backing.

Elements of corporate governance in Islamic banking

The statutory corporate governance in Islam involves Islamic financial institutions abiding to a set of rules called the Islamic law, or Shariah. The Shariah governs the bank's operations and transactions in accordance with Islamic principles derived from the Qu'ran and Hadith.

Three basic elements of faith provide the foundation for Islamic banking (Haron and Shanmugam, 1997):

(a) Aqidah: concerns all forms of faith and belief in Allah.
(b) Shariah: concerns practical actions taken by a Muslim in manifesting his faith and belief.
(c) Akhlaq: covers all aspects of a Muslim's behaviour, attitude and work ethics.

Corporate governance within Islamic banking is therefore covered by Shariah, which has a crucial role not only in governing bank transactions and operations, but also in monitoring and supervising the roles of all players within the banking system.

Shariah

The concept of Shariah governs the way a man conducts his life and behaviour, including the spiritual, mental and physical. Shariah is a blueprint for Islamic banks to operate in accordance with the laws outlined, for instance, in eliminating riba (interest) in all its forms and ensuring that banking procedures do not exploit nor do injustice to the bank's shareholders.

To ensure that Islamic banks comply with the appropriate Shariah rulings, the services of religious committees known as Shariah boards are employed. The boards comprise Shariah scholars or a committee of ulamas (religious scholars) and play the dual role of supervision and consultation.

Governance structures

Islamic banks must have regard to the pronouncements of Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) and Islamic Financial Service Board (IFSB).

The Islamic scholars or ulamas employed by Islamic banks have played a crucial role in the movement of Islamic finance and investment. They derive the principles of Islamic finance and investment from sources of Islamic law, which include:

(a) The Qu'ran.
(b) Hadith texts (statements and practices of the Prophet Muhammad (Pbuh)).
(c) Ijma (consensus of ulama).
(d) Qiyas (analogies from the Qu'ran and Hadith texts).
(e) Ijtihad (scholar's own reasoning).

The Shariah board is responsible for ensuring that financial institutions comply with the Shariah rulings in two phases. In the first phase, the religious board reviews the operations of the financial institution to ensure its Shariah compliance. The second phase involves answering queries, whether proposals for new transactions or products conforming with Shariah. The board also offers constructive and creative recommendations in all matters pertaining to Shariah.

Discussions with economists and bankers are also held to develop new Shariah compliant financial products. These dialogues are important so as to keep Islamic banking in line with market demands. Strict adherence to the Shariah and frequent dialogues with financiers will also assist in minimizing agency problems, as discussed below.

Financial governance

Like a conventional bank, an Islamic financial institution is an intermediary and trustee of other people's money, with the difference that it shares profit and loss with its depositors. Therefore Islamic banks should act as "responsible" trustees to shareholders and investors. "Responsible" in this context means managing the business according to the principles of Shariah. Therefore application of the concept of amanah to a business situation demands that the business be managed by those responsible as a trusteeship for the stakeholders. By relying on amanah, financial governance is ensured and unethical behaviour avoided.

Islamic banks operate on the concept of interest-free banking, with Shirkah or Musharakah (partnership) and Mudarabah (profit-sharing) as its basic products. Mudarabah financing involves projects managed by a client and the bank shares the risk with the client. The bank acts as a partner and is entitled to monitor, supervise and access books and records. Thus an ethical dilemma can arise when the management of Islamic banks is faced with a conflict of interest between shareholders and Mudarabah "partners". However, the company's management still has the authority to conduct the company's affairs.

However, in a Musharakah set up, losses are borne in proportion to the capital invested, with Islamic banks providing funds that are combined with the funds of the enterprise. Profits are distributed in predetermined ratios among the partners and contributors have the option to be involved in the project management.

Agency theory

In Islamic banking, the stakeholders are shareholders, account holders, Musharakah financing partners, Mudarabah investment account holders, its employees and the Islamic community (ummah). Agency problems arise from differences in economic interests between the agent (bank's management) and the principal (bank's investor). However, conscientious adherence to the Shariah can counter agency problems, allowing Islamic banks to maintain investors' confidence and assist in the establishment of a stable and secure financial system.

Corporate governance in selected countries

Corporate governance principles and codes in Islamic banks have been developed in different countries and issued from stock exchanges, corporations, institutional investors, or associations of directors and managers with the support of governments and international organizations. As a rule, compliance with these governance recommendations is not mandated by law, although the codes linked to stock exchange listing requirements may have a coercive effect. There is no single recognized best model of corporate governance.

Malaysia model

On the 30th July 1981, a 20-member National Steering Committee of Islamic Banks was established and proposed recommendations to the government on the 5th July 1982:

Continued...

(a) An Islamic bank should operate on Shariah principles.
(b) The Islamic bank should be incorporated as a limited company under the Companies Act 1965.
(c) The Central Bank should monitor and supervise the Islamic bank.
(d) The Islamic bank should have a Religious Supervisory Council to ensure that the bank's operations are in accordance with the Shariah.

Following these recommendations, the Islamic Banking Act 1983 was promulgated. Under this Act it became compulsory for Islamic banks to have their own Religious Supervisory Council with a minimum of three and a maximum of seven Muslim religious scholars. The Council's role is to advise the Islamic banks on its operations and transactions.

The first Islamic bank in Malaysia, Bank Islam Malaysia, was established in July 1983. The distinct Islamic principles that govern its operations are as follows:

(1) Prohibition of riba: the profit–loss sharing concept replaces interest as the central mechanism governing the deposit taking and loan making transactions.
(2) Muamalah (Islamic transaction): all banking transactions and management efforts must comply with Shariah.
(3) Avoidance of contradictory activities.

The Shariah Board holds a prominent role in the management of Bank Islam, assuring customers that good corporate governance will be followed.

Bahrain model

Bahrain has over 30 Islamic financial institutions offering a wide range of activities, including Islamic insurance. Bahrain is a major player in the world of Islamic banking and finance. To maintain the strong, stable and secure financial systems, all Islamic banks in Bahrain need to comply with Shariah supervisions.

All Shariah boards conduct annual reviews and produce reports to shareholders. The shareholders in turn provide input on the satisfaction level of their investments and the manner in which projects were handled by the bank. Should a bank breach the Shariah tenets, the board will:

(a) find Shariah compliant alternatives to the transactions;
(b) if no alternative is found, the transaction will not be allowed to proceed further; and
(c) if the transaction has already been executed and the breach is found at a later stage, the board will advise the management and shareholders to distribute the income generated from the breached transaction to a charity account.

In addition to the Shariah board, the AAOIFI was established to define Islamic financial instruments and design accounting standards. This organization set up a 15-member Central Shariah Board in 1995 to harmonize and converge concepts and applications amongst boards of various Islamic financial institutions, preventing inconsistencies and assisting with the development of new products. By establishing these bodies Bahrain has moved ahead of many other countries offering Islamic banking services.

Bangladesh model

It has been reported that of the 39 Islamic banks in Bangladesh, only five operate according to stringent Islamic principles, with Shariah Councils to guide their operations. These Councils consists of fuqahas (Islamic jurists), Islamic economists and lawyers (Sarker, 1999). The monitoring and supervisory roles of these Shariah Councils ensure that all activities operate according to the tenets of Shariah, thus maintaining good corporate governance. In some instances the Councils conduct audit operations and produce a report to highlight any deviations and make suggestions for the further purification of banking transactions.

Saudi Arabia model

The Saudi Arabian Islamic banking scene is dominated by the Islamic Development Bank (IDB), which was established in 1974. The IDB is an international financial institution, similar to the World Bank or the Asian Development Bank, set up to encourage member countries and Muslim communities to implement policies leading towards Islamic economic development and social progress (Mannan, 1998). It also participates in equity capital and grants loans for project and enterprises. The IDB has diverse operations that are governed by the following Shariah principles.

(1) Dynamic use of resources without riba
Interest charges on loans are strictly prohibited in line with the Holy Qu'ran: "Allah has permitted trade and forbidden riba (interest)." The IDB prides itself for being involved in trade and not in riba.

(2) Constant use of financial resources
Resources should not be wasted, as Islam encourages owners to put resources in a productive process to enable distribution throughout society.

(3) Equitable sharing of risk and gains
As mentioned in the Holy Qu'ran: "Let it be a trading among you by mutual agreement," financial contracts such as Mudarabah, Musharakah and Murabahah are all based on profit–loss sharing arrangements.

(4) Securing due benefits/income for owner
IDB emphasizes the ethical use of financial resources in a manner that secures maximum benefits in the form of a return or mark-up.

(5) Benevolent loans
The Holy Qu'ran stresses the importance of Qardhasan (benevolent loans) in Surah Al-Mozammil, verse 20: "Attend your prayers, pay your alms and grant benevolent loans." It is also mentioned in Surah Al-Taghabon, verse 17: "If you grant benevolent loans, we multiply them for you and forgive you." The IDB provides Qardhasan to achieve Islamic social, moral and spiritual goals for member countries and for Muslim communities of non-member countries.

(6) Lawful investment
The Shariah does not recognize profit maximization as the solitary goal of an enterprise that neglects social and ethical principles. In Islam, operations involving financial profit may need to be sacrificed in the interest of the community at large. Morals and ethics are given greater weight than profit.

Complication in corporate governance of Islamic banks

The law states that corporations and their management owe fiduciary duties to their shareholders only, whereas Islamic banks owe fiduciary duties towards their shareholders and stakeholders. It is the stakeholders rather than the shareholders whose rights might be compromised. This is not due to the governance of the Mudarabah contract, but rather to the context in which it is used.

Recommendations

Islamic banks all have Shariah supervisory boards to deal with both self and statutory regulation. These boards may have to extend their jurisdiction to cover corporate governance issues.

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INDUSTRY REPORT

Governance Issues and Islamic Banking *(continued...)*

Shariah board members must be knowledgeable in the Arabic language to interpret the Holy Qu'ran and Hadith correctly. It may be a good idea to establish a central board to oversee the rulings of independent boards, regulate differing interpretations and advise individual boards as needed.

As for self-regulation, the Shariah boards play an important role in raising awareness on concepts such as tawhid and other Islamic ethics within Islamic financial institutions. Directors, shareholders and staff must all remember that performing their tasks honestly is a form of worshipping God.

Islamic banks should establish training centres where prospective clients are taught to observe aspects of good governance, especially with respect to providing full and honest disclosures of their business dealings and also to run their business in an ethical manner.

Establishing some sound corporate governance rules may help Islamic banking to fulfil its mission.

Conclusion

The need for good corporate governance practice is vital in all banking sectors and especially so within Islamic banking. Governance issues are currently well placed in all aspects of Islamic banking operations. However, they are not yet so sophisticated to meet the ever increasing changes in Islamic business dealings and the Shariah Council needs to play an even more crucial role in monitoring and ensuring a well-adapted governance practice in Islamic banking. The responsibility of practising ethical governance in Islamic banking falls to the Shariah Council, but also to all other parties involved such as directors and shareholders.

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LEGAL REPORT

Different Acts for Similar Islamic Services and Products – The Dilemma

By Sherin binti Kunhibava

Islamic banking business in Malaysia is conducted by Islamic banks and conventional banks offering Islamic banking services. This article examines the laws which govern these two services provided to customers wishing to practise Islamic banking. One pertinent question that arises is should these services be governed by the same laws?

Introduction

In recent years there has been a welcome renaissance in the area of Islamic banking and finance. To support the tremendous activity in this sector a proper legal infrastructure is required. This article will highlight one dilemma facing the current legal infrastructure that governs Islamic banking and finance.

In Malaysia, the first Islamic bank was established in 1983, and 10 years later – in 1993 – commercial banks, merchant banks and finance companies were permitted to offer Islamic banking products and services under the Islamic Banking Scheme (IBS), known as "Islamic windows". This system, also known as the dual banking system, was seen to be the most efficient way of increasing the number of institutions offering Islamic banking services at the lowest cost and within the shortest time frame.[1] In 1999 a second Islamic bank, Bank Muamalat Malaysia (BMMB) commenced operations. Another five years down the road and Islamic subsidiaries have been introduced, with RHB Islamic Bank and Hong Leong Islamic Bank being launched this year. Islamic subsidiaries are for all purposes treated as fully fledged Islamic banks.

Therefore, in Malaysia there are generally two types of banks where a customer can engage in Islamic banking:

- Islamic banks (including Islamic subsidiaries) that offer purely Islamic products and services.
- Conventional banks who are allowed to offer Islamic banking products and services under the IBS, known as "Islamic windows."

Different Acts

There are two main statutes governing banks in Malaysia: the Banking and Financial Institutions Act 1989 (BAFIA), which governs conventional banks; and the Islamic Banking Act 1983 (IBA), which governs Islamic banks. BAFIA does not apply to Islamic banks and IBA does not govern conventional banks. However, conventional banks that offer IBS or Islamic windows are governed by BAFIA, under section 124.

Section 124 of BAFIA provides:

> "(1) Except as provided in section 33, nothing in this Act or the Islamic Banking Act 1983 shall prohibit or restrict any licensed institution from carrying on Islamic banking business or Islamic financial business, in addition to its existing licensed business, provided that the licensed institution shall consult the bank before it carries on Islamic banking business or any Islamic financial business.
>
> *(2) For the avoidance of doubt, it is declared that a licensed institution shall, in respect of the Islamic banking business or Islamic financial business carried on by it, be subject to the provisions of this Act.*
>
> ...
>
> *(5) Any licensed institution carrying on Islamic banking business or Islamic financial business shall be deemed to be not an Islamic bank.*
> *(6) This Act shall not apply to an Islamic bank."* (emphasis added)

Thus conventional banks offering IBS and Islamic banks are governed by different legislation.

Are Islamic banks offering products and services that are different from Islamic windows?

To answer this question, the definition of products and services offered by both types of bank offering IBS needs to be looked at under both BAFIA and IBA.

Section 124(7)(b) of BAFIA reads:

> "'*Islamic* banking business' has the meaning assigned thereto under the Islamic Banking Act 1983; and
> (c) 'Islamic financial business' means any financial business, the aims and operations of which, do not involve any element which is not approved by the Religion of Islam." (emphasis added)

Section 2 IBA reads:

> "'Islamic banking business' means banking business whose aims and operations do not involve any element which is not approved by the Religion of Islam."

In summary, both Islamic banks and Islamic windows offer "Islamic banking business," as stipulated under section 124(7)(b) of BAFIA and section 2 of IBA. This means conventional banks offering IBS conduct Islamic banking business, as defined under the IBA. Thus both Islamic banks and conventional banks offering IBS conduct the same or at the very least similar Islamic banking business, and yet they are governed by separate acts.

Different laws

Since both Islamic banks and conventional banks offering IBS are governed by different Acts, does this mean that they are governed by different laws or standards? The licence for an Islamic bank can only be achieved after compliance has been achieved with the requirements under IBA, section 3, whereas conventional banks obtain their license under BAFIA. The requirements for obtaining a licence before a bank can operate as an Islamic bank are set out below:

Continued...

IBA, section 3(5)

"The Central Bank shall not recommend the grant of a license, and the Minister shall not grant a license, unless the Central Bank or the Minister, as the case may be, is satisfied:

(a) that the aims and operations of the banking business which it is desired to carry on will not involve any element which is not approved by the Religion of Islam; and

(b) that there is, in the articles of association of the bank concerned, *provision for the establishment of a Shariah advisory body*, as may be approved by the Central Bank, to advise the bank on the operations of its banking business in order to ensure that they do not involve any element which is not approved by the Religion of Islam." (emphasis added)

However, under BAFIA a licensed conventional bank can carry on Islamic banking business and Islamic financial business as long as the following conditions are satisfied:

BAFIA, section 124(1)

"Except as provided in section 33, nothing in this Act or the Islamic Banking Act 1983 shall prohibit or restrict any licensed institution from carrying on Islamic banking business or Islamic financial business, in addition to its existing licensed business, provided that the licensed institution shall consult the bank before it carries on Islamic banking business or any Islamic financial business.

(3) Any licensed institution carrying on Islamic banking business or Islamic financial business, in addition to its existing licensed business *may, from time to time seek the advice of the Shariah Advisory Council established under subsection (7)*, on the operations of its business in order to ensure that it does not involve any element which is not approved by the religion of Islam.

(4) Any licensed institution carrying on Islamic banking business or Islamic financial business *shall comply* with any written directions relating to the Islamic banking business or any other Islamic financial business, carried on by such licensed institution, issued from time to time by the Bank, *in consultation with the Shariah Advisory Council*." (emphasis added)

Therefore from looking at the BAFIA and IBA, it can be seen that it is mandatory for Islamic banks that an internal Shariah Advisory Body is set up and approved by the Central Bank. There is no requirement for conventional banks offering IBS to establish a Shariah Advisory Body in order to obtain a licence to carry out Islamic banking, as long as they seek the consultation of the Shariah Advisory Council.[2]

To elaborate on this point, all the provisions in the IBA only apply to Islamic banks, whereas conventional banks offering IBS are governed by the BAFIA, even though both conduct the same Islamic banking business. So provisions in IBA which differ from the BAFIA, such as section 55, do not apply to conventional banks offering IBS, only to Islamic banks.

IBA, section 55 – application of other laws

"An Islamic bank which is incorporated under the Companies Act 1965 (Act 125) shall be subject to the provisions of that Act as well as to the provisions of this Act, save that where there is any conflict or inconsistency between the provisions of that Act and the provisions of this Act shall prevail."

So conventional banks offering IBS would not be exempted from the provisions of the Companies Act 1965. If there is a conflict between the Companies Act 1965 and the IBA, an Islamic bank must follow the IBA, whereas conventional banks offering IBS would continue to follow the Companies Act 1965.

It is possible that there are other sections in the BAFIA and IBA which are at cross-purposes, resulting in Islamic banks following a different set of laws from conventional banks offering the same Islamic banking business.

Recommendations

In light of the above, it is the author's opinion that to avoid any possible conflicts between Islamic and non-Islamic banks offering the same services, it is time for change in the legal infrastructure, to enable both Islamic banks and Islamic windows to be governed by one law, which means one Act.

The first recommendation would be to change all Islamic windows (even if they are operating within a conventional bank) from being governed by BAFIA to IBA. If all Islamic windows and the products and services they offer are governed by the IBA, as Islamic banks are, there will be no possibility of conflict. (This may, however, cause practical problems when a conventional bank is subjected to two different laws – BAFIA for conventional products and services and IBA for Islamic windows).

A second plausible solution would be for all Islamic windows to be converted to Islamic bank subsidiaries.[3] This would result in all Islamic banks and subsidiaries being governed by the IBA.

A further suggestion is to review and combine all the laws on banking in Malaysia, whether Islamic or non-Islamic, whether conducted by a fully fledged Islamic bank or a conventional bank, into one comprehensive BAFIA. There should be two sections within the new comprehensive BAFIA, one on conventional banking business – perhaps section A – and a section B for Islamic banking business, whether conducted by Islamic banks or through Islamic windows.

This has been done before, for example when BAFIA repealed the Finance Companies Act 1969 and the Banking Act 1973 to provide one comprehensive Act on banking and financial institutions. Jordan,[4] Kuwait[5] and the Phillipines[6] have all incorporated Islamic banking and finance matters within one regulatory framework by introducing new sections to their existing laws on banking and finance.

A prominent scholar has made the following statement on incorporating laws applicable to Islamic banks within laws governing conventional banking and finance:

> "This approach places the emphasis on the regulation of Islamic finance within the established legal framework, seeking to minimize points of possible conflict, and maximize a level regulatory playing field. From a systemic viewpoint, it places Islamic banks within the context of the financial system as a whole."[7]

Continued...

LEGAL REPORT

Different Acts for Similar Islamic Services and Products – The Dilemma *(continued...)*

Conclusion

Islamic banking business in Malaysia is currently governed by two different Acts and therefore two different laws: there is no standardization. Uncertainty in the legal framework in any country only translates to problems, more litigation and a loss of consumer confidence.

This dilemma can be overcome by ensuring that all Islamic banking business in Malaysia is governed by the same Act. Legislative amendments is one solution; converting all Islamic windows to Islamic banking subsidiaries would also solve the dilemma.

The author is a Lecturer at the University Tunku Abdul Rahman (Utar), email: sherinali34@hotmail.com.

1 "Why Islamic Banking? The Emergence of Islamic Banking," Association of Islamic Banking Institutions: http://www.aibim.com.my/aibim/dsp_page.cfm?pageid=230, retrieved in September 2005.

2 However, it should be noted that even though there is no mandatory requirement that conventional banks offering IBS have a Shariah Advisory Body, it would seem that they do in practice have Shariah Advisory Committees or Consultants: see http://www.bankinginfo.com.my, retrieved in September 2005.

3 See Saiful Azhar Rosly, "Islamic Banking Windows Transform to Subsidiaries" *Star Newspaper*, StarBiz, 31 October 2005, p 6. In this article the author stated that: "Transformation of Islamic banking windows into Islamic banking subsidiaries is mandatory."

4 Banking Law, Law No 28 of 2000, Jordan, Articles 50–59 contain the regulatory framework for Islamic banking. The law states the objectives of Islamic banking, permissible activities and restrictions. It also contains provisions on investment risk funds, deposit insurance and Shariah compliance supervision: www.worldbank.org, retrieved in September 2005.

5 "Central Bank of Kuwait Law 32/1968, Central Bank of Kuwait." Section 10 of the revised law refers to regulation of Islamic banking. It touches on various issues on the set-up of Islamic banks and the creation of Supervisory Shariah Boards: www.worldbank.org, retrieved in September 2005.

6 "Manual of Regulations for Banks – Central Bank of the Philippines" (Appendix 44, scroll to p 625). The Manual contains regulations on Islamic banking approved by the Monetary Board through Resolutions 161 and 244 on the 14th February and the 6th March 1996. The regulations touch on several issues: the purpose of the bank, the functions of the Shariah Advisory Council, the powers of the bank, return on investment funds, authorized operations, investment risk funds, accounting and training of personnel. The section on Islamic banking is at pp 625–645 (Appendix 44): www.worldbank.org, retrieved in September 2005.

7 William Blair, "Legal Issues in the Financial Services Industry," 1st–2nd March 2005, Sheraton Hotel and Towers, Kuwait City: http://www.combar.com/Default.aspx?sID=17, retrieved in September 2005.

How important a role does Takaful play in the development of a liquid and efficient Islamic capital market?

PROFESSOR RODNEY WILSON

Director

University of Durham

At present Takaful companies play a minimal role in Islamic capital markets. Such markets are in their infancy in the Gulf, where most Sukuk securities are held to maturity rather than traded, partly because there is a shortage of available Sukuk relative to the demand by Islamic banks and financial institutions for liquid Shariah compliant instruments. Furthermore, in the Gulf the Takaful industry itself has only just developed during the last five years, and most of the companies offering Takaful are small in comparison to conventional insurance companies.

Malaysia has the most developed domestic market in Sukuk securities and these are extensively traded, especially the corporate Sukuk. Takaful companies are amongst those holding and trading ringgit denominated Sukuk, but in Malaysia Takaful companies remain small in terms of premium income and capitalization in comparison to conventional insurance companies.

The potential role for Takaful companies in the development of Islamic capital markets is, however, enormous. Conventional insurance companies hold up to 50% of their assets in bonds because the fixed maturity date, certain capital value on maturity and predictable income stream make bonds the safest form of asset to offset against liabilities to those insured. Similarily as Takaful companies grow, they can be expected to have a comparable asset profile, with a high proportion of assets in the form of Sukuk securities that should encourage the growth of the market.

SAMI MATRAJI LLM

Takaful and Islamic capital markets play different yet complementary roles in terms of the development of a sound Islamic financial system.

In order to clarify the above statement, one should begin by illustrating the way in which the conventional system operates. It is well established that insurance companies, known as the "institutional investors," substantially contribute in the development of any capital market, given that their investments are significant compared to other investors. However, this is not a one-way benefit system in favour of public companies or capital markets generally. As a matter of fact, insurance companies, by investing in the capital markets, are securing a constant income for their shareholders.

Turning now to the Islamic system, it is incumbent on Takaful companies to ensure, on the one hand, long-term profits for both the company's shareholders and the participants and, on the other hand, liquidity to cover all claims, through the development of a secure investment system which could be formed by diversifying the risk of loss.

The latter objective is achieved by investing in a well-structured Islamic capital market comprising all classes of assets: equity, bond, derivatives and offshore markets. Moreover, the market should contain companies with different sizes and specializing in a huge variety of sectors. More importantly, the capital market should establish a Shariah Board which will impose a screening system with various qualitative and quantitative parameters based on Islamic principles. This screening system will determine which companies or debt securities issues are allowed to be listed.

Hence, the existence of an Islamic capital market with the abovementioned requirements will constitute an incentive for Takaful companies to invest and, undoubtedly, contribute in the development of a liquid and efficient Islamic capital market.

Therefore, one might contend that Takaful companies do not play a salient or core role in the development of a liquid Islamic capital market because they are committed to protecting certain internal interests (ie shareholders' and participants' interests). Yet, they could contribute by maintaining and developing such an Islamic market as long it satisfies the above requirements. Conversely, the existence of an Islamic capital market with a developed infrastructure, such as the Bursa Malaysia or, recently, the Gulf capital market, constitutes an essential investment target for any Takaful company seeking to satisfy its internal interests.

Continued...

Islamic Finance forum *(continued...)*

ADNAN AZIZ
Research Analyst
Dar Al Istithmar
London

Islamic capital markets have emerged as a natural progression of the growth of Islamic finance industry, playing a vital role in developing liquidity management mechanisms and offering a range of asset classes to invest in. Following the principle of supply creating its own demand, investable capital of the Takaful industry, like that of Islamic banking sector, has played a significant role in the development of the Islamic capital market.

Sukuk, Shariah compliant equity products, and a variety of Islamic investment funds, are now representing a flourishing market to attract Islamic capital from all Islamic financial sectors, including Takaful. Though contributing greatly to the development of the Islamic capital market, the available asset classes are yet not as liquid and efficient when compared to the conventional capital market. The need is more pressing in case of Islamic investment funds and Sukuk. Hence, Takaful and other Islamic financial sectors need to press on the relevant industry players to come up with more innovative, liquid and efficient instruments.

Most commonly used operational models of Islamic insurance rely on the concept of Takaful based on Mudarabah or Wakala. These two and other variants of Takaful models have a number of limitations. For example, in a conventional set up, insurance providers become owners of the premiums and are at liberty to invest in assets of their own choice. This is not the case for existing Takaful models, who cannot benefit from this principle of separation of ownership. Hence, there is a need to come up with alternative models for Islamic insurance.

In short, the current role of Takaful in development of a liquid and efficient Islamic capital market is rather limited. Takaful may play a much larger role, however, if alternative models of Islamic insurance are considered and explored.

Dato Mohd Fadzli Yusof
Chief Executive Officer
Takaful Malaysia

Like insurance, Takaful as custodian of participants' funds has to strive for as high returns as possible on these funds without compromising on its safety and security. Hence, investment of these funds is one of the key functions of a Takaful operator. Obviously, investment must be in avenues that are Shariah compliant.

In this respect, Takaful would certainly play a crucial role in the development of the Islamic capital markets. More importantly, if instruments developed by the market would be able to match the liability of these funds.

MS BALJEET KAUR GREWAL
Chief Economist
Asembankers Berhad

Takaful, as a system of Islamic insurance, is based on co-operation and mutual help for the good of the society at large. Although Takaful has been in the market for more than two decades, it has yet to make significant inroads. It should be noted that although the conventional insurance market is deeply entrenched in several Muslim countries, the percentage of the Muslim population that are insured is relatively low. Hence the market penetration level is very low, at less than 5% in many Muslim countries. In Malaysia, the level of market penetration of Takaful relative to the total population is only 3.8%, versus a market penetration for conventional insurance of 34.6%. Therefore, there is enormous potential to be tapped.

The Takaful industry represents an important component in the overall Islamic financial system, given its role in the mobilization of long-term funds, provision of risk protection, development of the Islamic capital market, an important institutional investor as well as supporting the overall economic growth and development. As both the mobilizers of long-term funds and fund managers to the policy holders, Takaful operators' ability to generate returns to fulfill the obligation to the policy holders depends very much on the range of financial instruments available in the market place. Demand from Takaful players, coupled with an enabling regulatory environment, speeds up the development of innovative Islamic structured products.

The development of a comprehensive Islamic financial market in Malaysia that includes Islamic banking, Islamic money and capital markets has reinforced the development of the Takaful business. As of today, the Takaful industry in Malaysia has emerged as a fast growing industry within the insurance sector since its introduction in 1985. From total assets at a mere US$0.5 million in 1986, it has reached more than US$1.33 billion in 2004, constituting 5.1% of the total assets of the insurance sector.

Continued...

Islamic Finance forum *(continued...)*

CHRIS COOK
Principal
Partnerships Consulting LLP, London

The future of Islamic capital markets lies in distinguishing between investment on the one hand and credit on the other, ie between asset-based and deficit-based finance.

The former is concerned with revenue sharing and new asset-based financing tools such as the "capital partnership," as opposed to the inequitable limited liability company. A "capital partnership" is essentially Musharakah achieved within a new partnership-based corporate legal "wrapper."

The latter is concerned with the sharing of risk and essentially comprises a mutual guarantee of bilateral "trade" credit (ie "time to pay") between a seller and a buyer. Such a "guarantee society or "clearing union" is essentially "Takaful" again within a partnership legal wrapper. There is no place for credit creation by banks, which are disin-termediated.

The role of banks changes to:

(a) appraising investments and providing liquidity by bringing investors together with investments or "making a market;"
(b) maintaining an accounting system and risk management in respect the mutual guarantee of credit creation.

Next Forum Question

During the past year we have witnessed numerous new and exciting Shariah compliant products. Quite simply, what new products and advancements do you expect we will see during the course of 2006?

If you would like to air your views on the next Islamic Finance Forum Question, please email your response of between 100 and 300 words to Christina Morgan, Islamic Finance News Manager at: Christina.Morgan@IslamicFinanceNews.com before Wednesday 4th January.

EVENTS DIARY

International Leadership Summit in Islamic Finance
Kuala Lumpur
Tuesday, 17th –18th January 2006
Organized By: IFSB

5th Annual Islamic Finance Summit
Millennium Hotel, London
Tuesday, 24th – 25th January 2006
Organized By: Euromoney

The 2nd International Conference on Islamic Banking: Risk Management, Regulation & Supervision
Le Meridien, Kuala Lumpur
Tuesday, 7th – 8th February 2006
Organized By: Bank Negara Malaysia, IDB, IRTI Jeddah, IFSB

The Fundamentals of Islamic Finance & its Applications in Modern Commercial Transactions
Princeton Club, New York City
Wednesday, 16th – 17th February 2006
Organized By: Infocast

Islamic Finance Singapore 2006
Hilton Hotel, Singapore
Tuesday, 21st – 22nd February 2006
Organized By: IQPC Worldwide

2nd Seminar on the Regulation of Takaful
The Andaman Langkawi, Malaysia
Thursday, 23rd – 24th February 2006
Organized By: IFSB

Hedge Funds World Middle East 2006
Madinat Jumeirah Hotel, Dubai
Monday, 6th – 8th March 2006
Organized By: Terrapinn

The 1st Islamic Banks & Financial Institutions Conference in Syria: "Islamic Banking's Horizions"
Le Meridien Hotel, Damascus
Monday, 13th – 14th March 2006
Organized By: Al Salam for International Conferences & Exhibitions

International Islamic Finance Forum Middle East
Dubai, UAE
Sunday, 19th – 22nd March 2006
Organized By: IIR Middle East

3rd Islamic Financial Services Board Summit: Aligning the Architecture of Islamic Finance to the Evolving Industry Needs
The Phoenicia Intercontinental Hotel Beirut, Lebanon
Wednesday, 17th – 18th May 2006
Organized By: IFSB

Takaful news
www.islamicfinancenews.com


NEWS BRIEFS

MALAYSIA

Takaful-ready Triton software

3i Infotech, a global leader in IT solutions for insurance, banking and retail industries, has signed a multi-million dollar deal with Hong Leong Bank for the implementation of Triton Loan Origination application software.

Triton is a retail banking solution that has proved successful in global markets that require banking solutions for both conventional and Islamic banking principles. Triton is designed to support Takaful lending across various retail products (mortgages, personal finance, project finance, auto finance).

Islamic lending offerings such as Al Bai Bithaman Ajil, Bai Istisnah and Al Ijarah are all built into the application and Triton's flexibility allows for the development of new products and services.

BAHRAIN

Regional insurance hub

The Executive Director of Financial Institutions Supervision at Bahrain Monetary Agency (BMA), Anwar Khalifa Al Sadah, believes that Bahrain is ready to act as a regional insurance hub, through its provision of the best regulatory framework for companies, stake holders and policy holders.

Addressing the Takaful Summit at the pre-conference briefings of the 12th World Islamic Banking Conference, Khalifa Al Sadah said that the BMA will issue guidelines to implement the Wakala model for the Islamic insurance industry in the Kingdom.

He said: "Keeping in view the interest of policy holders, the BMA has set solvency margins as we feel that it is rightful for the policy holders to know the performance of any company. The BMA's emphasis on corporate governance, transparency and professionalism at every stage in the insurance sector are few but important steps being implemented by the Agency. There is a need for concerted effort to develop the Islamic insurance industry in line with the future needs of the market."

The Takaful summit, which was facilitated by Solidarity, focused on "Assessing the Appropriate Takaful Model in Today's Business Environment" and a panel discussion on the perspectives of shareholders, policy holders, regulators and Shariah scholars was held on key issues and opportunities facing the Takaful market.

MALAYSIA

Joint venture for Takaful licence

Bahrain-based Solidarity has signed a joint venture agreement with Malaysia's largest composite insurance provider MAA Assurance. The partnership hopes to win one of the four new Takaful licences to be awarded by Bank Negara in January 2006.

The announcement to set up the as yet unnamed US$25 million joint venture firm was made at the 12th annual World Islamic Finance Conference's "Takaful Summit" in Bahrain.

Solidarity, one of the world's largest Islamic insurers, which currently sells its Shariah compliant family Takaful savings, investment and protection plans for retirement, wealth accumulation and education throughout the GCC, will obtain access to MAA's customer base of 2.71 million people, 76 branches and 25,000 agents through this partnership. It will also put the company in a good position to move into MAA's markets in Thailand, the Philippines, Indonesia and Sri Lanka.

MALAYSIA

Global expansion for Takaful Nasional

Once Takaful Nasional's consolidation exercise with Mayban Fortis Holdings is completed, the company plans to accelerate its expansion plans, with the next targets being China and India.

President and CEO of Takaful Nasional Aminuddin Md Desa commented: "Before the end of 2006, we should be actively going into either China or India. We should start operations by 2007." There are no Takaful operators in either of these huge markets at present.

Aminuddin Md Desa said the company would like to make more inroads into foreign shores after 2010: "Mayban Fortis will bring the necessary resources and network it has to further our expansion plans," he said.

Takaful Nasional recently joined with Pakistan's Pak Kuwait Investment to form the joint venture company Pak Kuwait Takaful, in which it holds a 25% stake. Pak Kuwait Takaful started operations in the last few weeks.

MALAYSIA

Maphilindo's profits to rise

Maphilindo International is expecting to see a 25% increase in profit and revenue for the financial year ended September 2005. The company is set to post a US$4.63 million (RM17.5 million) net profit on the back of US$6.62 million (RM25 million) revenue, securing its place as Malaysia's leading loss adjuster.

The company put its improved results down to the introduction of new products and its success in handling large losses in the country this year.

In the last issue of *Islamic Finance News* it was reported that Maphilindo International's loss adjusting Takaful licence had been approved by Bank Negara. This would make the company Malaysia's first provider of Shariah compliant loss adjusting services.

MALAYSIA

Takaful Nasional claims ratio up

Takaful Nasional has improved its overall claims ratio to 48.2% last year (from 79.5% in 2001) by adopting a more proactive approach to enterprise risk management. This strategy has led to savings of US$793,983 (RM3 million) in 2004; reducing its policy issuing timeframe from three months to three days; improved returns on equity; and greater overall efficiency.

Takaful Nasional commissioned Roots Consulting to automate risk management procedures and provide a structured approach to risk management. Takaful Nasional President and CEO Aminuddin Md Desa commented that he was determined that risk management should not be seen merely as a compliance exercise at Takaful Nasional, but should be translated across the organization to minimize risks and yield efficiencies.

An additional benefit relates to the Board: "The additional transparency we get from ERM and the automated Risk Scorecard have made our Board more comfortable with risk-related issues, such as extending our operations to Pakistan, for example."

TAKAFUL REPORT

The Concept of Takaful and its Place in our Economies

By Rob King

The global Takaful market, despite having been around for over 30 years, is still in its infancy. Some markets across the globe are more developed than others, but in general the industry has further to go. The development of Takaful offers over 1 billion Muslims the opportunity to plan for their financial future with the knowledge that it is Shariah compliant. The principle at the heart of Takaful is to provide protection to those individuals who need it most; a principle in line with the fundamental tenants of Islam.

Regional economic growth and a greater understanding of Takaful should see the industry expand exponentially, as people come to appreciate the virtue of fairness in this Shariah compliant system.

There are a number of key factors driving demand in the market today. The economic outlook, for both the short and long-term, is very favourable. There is a greater awareness, from every social class, of the need for financial planning and a cultural resistance towards conventional planning makes Takaful the preferred option.

Relationship marketing

To take advantage of this positive climate, financial services providers – especially Takaful companies – need to approach the market in a professional manner and create consumer confidence through the genuineness of their products and services. Educating the public about the concept, products and benefits of this unique Islamic financial system will allow it to rise to the challenge of global competition by unleashing the creativity and entrepreneurial flair of financial services manufacturers who share and believe in the Islamic financial system in general, and Takaful in particular.

Marketing through relationship building is paramount to the success of the industry. Relationship marketing is based on network interaction, and recognizes that marketing is rooted in the total management of the networks of the financial institution, the market and society. It is directed to a long-term, win–win relationship with clients and distributors, a value which is jointly created between the parties involved. It transcends boundaries between specialist functions and disciplines. The success of relationship marketing will be mirrored in the global Takaful industry, which is forecasted to grow at a rate of 15–20% per annum. Takaful products are in huge demand because they rely heavily on the virtue of fairness and are concurrent with the teachings of Islam. Many conventional products, while being dynamic and diverse, do not fulfill the requirements of Shariah, and thus a need for products and services that are Shariah compliant is created. This is reflected in the confidence of investors and shareholders in Islamic financial institutions. Financial institutions have to provide solutions through a variety of means that people can trust and understand.

Planning for the future

Both Islamic and conventional financial institutions are rapidly approaching a crossroads. In order to develop, Islamic institutions need to understand and accept the views of what predominantly Muslim clients require for their future financial well-being. The products and plans supplied, the distribution channels employed, as well as the rules and regulations adhered to, are not the only solution. Employing an approach of relative simplicity underlined with shrewd diversity and intensity, through specialist financial planning and management advice within appropriate financial wealth generation and risk cover offerings will also help to build self-sustaining protection for the aged, infirm and less fortunate members of society.

Financial products of any kind are sold, rather than bought. This enhances the added value that Takaful companies must bring to the market in providing, along with creative and innovative products and services, individual consumer education, based on the important task of planning for the future. It is not an easy task to accomplish, and is often the reason many individuals – of varying race, creed, colour and religion – are reluctant to face impending financial crises in their lives. These individuals may realize that they are able to take such responsibility only with our help and with the guidance of Shariah. Once this realization takes place, potential clients will come to understand that they need proper Islamic financial planning, leading financial professionals to create the added demand which will lead to further growth, increased sophistication and a movement towards a self-protecting, self-financing, self-sufficient ageing population, which is not reliant on social largesse.

It is important that consumers understand the need for financial planning and its influence on protecting our societies. Economic statistics, especially from the Middle East, indicate that many countries are reducing their social security benefits, leaving people exposed if they become unable to work. Takaful has its own niche which is being developed and nurtured, as companies are beginning to take notice of this growing global trend. A company's size, scope and backing are major assets in expanding this market.

A key to the continuing success of the Takaful market is its ability to rapidly develop human resources with the knowledge and skills not only in managerial, financial and technical fields, but also in the principles of Shariah. Financial services must be provided through educational methods to assist clients with their personal financial estate analysis and planning. For instance, clients need to be advised on the selection of appropriate products to be used to meet future needs, and staff members will be required to manage this entire process according to the tenets of the Islamic Shariah.

The increase in money supply would generate an increase in individual purchasing power, which is then applied to both financial and non-financial industries and market sectors. An increase in purchasing demand will then spur the capital growth of these countries. This capital growth will in turn further increase living standards in society. Islamic financial institutions will grow together, as an industry, prosper and continue to be pillars of community financial well-being.

Looking to the future

Takaful is indeed a prospect for the future, and as we look forward its massive potential for both the industry and consumer can be realized. The necessity of understanding the client's requirements and preferences is paramount in implementing a successful strategy. For instance, realizing the need for protection and a diverse range of Shariah compliant savings and investment plans will motivate clients to think specifically about the future of themselves and their families.

This can all be achieved once financial professionals come to believe in the shared responsibilities that represent the key element of Takaful. At present, Takaful remains a market with very low penetration.

TAKAFUL REPORT

The Concept of Takaful and its Place in our Economies *(continued...)*

The potential of a market which covers more than 1 billion Muslims (over 20% of the global population) is immense. There is not only a need to create market awareness of Takaful, but also to develop products which meet clients' needs. Developing fully fledged Shariah compliant savings, investment and protection plans, alongside re-Takaful, is the duty of any financial professional who is seeking a better and more stable financial future for our economies.

Takaful strongly emphasizes shared responsibilities and its core principles are based on fairness to all – the individual participants, stakeholders and the community at large. Working in partnerships allows the use of savings, investment and protection Takaful plans supplied through a variety of distribution methods to suit particular markets. Currently it is expected that annual contribution growth will be 15–20%. With its superior features as compared to conventional insurance and assurance properties, it is almost impossible for Takaful to be out of the mainstream. Takaful, both family and general, allows individuals to plan for their future and helps to provide them with assurance and financial security.

The author is General Manager at Solidarity, based in Bahrain.

MOVES

Emaar – SAUDI ARABIA

Emaar Properties, the world's largest property development company by market capitalization, has made two key appointments.

Issam Galadari will take on the role of Managing Director of Saudi Arabia. Mr Galadari has two decades of experience, most recently holding the role of Executive Director of Projects at Emaar Dubai. He holds a BSc in Civil Engineering and a postgraduate diploma in Structural Engineering from the University of Southampton, UK.

Ahmad Thani Al Matrooshi will take on the role of Managing Director for the UAE operation. Mr Matrooshi comes to Emaar from the government-run Dubai Development Board, where he was Chief Executive Officer for almost a decade, and holds a wealth of experience in property and real estate development.

UIB Capital – USA

The global Islamic investment bank, Unicorn Investment Bank, has appointed Tariq Malhance to be Senior Vice-President of Private Equity and President of UIB Capital in Chicago.

Mr Malhance comes to UIB Capital from the City of Chicago, where he worked for 25 years. He is a graduate of the University of Karachi, Pakistan and has a BS BA in Finance from Roosevelt University in Chicago, as well as two graduate degrees.

Mr Malhance, who is highly experienced in bonds and private equity, will take responsibility for originating and facilitating senior loans for private equity deals in North America.

CITIGROUP – HONG KONG

Citigroup has appointed Andrew Stotz as Head of Research in Thailand. Mr Stotz comes to Citigroup from TMB Macquarie, where he was Head of Equity Research. Previously he has worked at SG Asia and WI Carr and Peregrine. He holds an MBA from California State University.

SG CIB – ASIA

Sandra Lee has been appointed Managing Director, Head of Retail, Marketing and Product Development for the retail structured products business in Asia (excluding Japan).

Prior to joining SG CIB, which is part of Société Générale, Lee worked at HSBC Investments as Head of Retail, Marketing and Product Development. She has 10 years of experience in sales and financial business development.

Islamic Finance Advisory Council – DUBAI

The newly created Islamic Finance Advisory Council, formed by the Dubai International Financial Centre, has appointed six honorary members to sit on its board for two years:

- Saad Abdul Razak, CEO of Dubai Islamic Bank.
- Hussain Al Qemzi, CEO of Sharjah Islamic Bank.
- Aref A Al Kooheji, EVP, Dubai Islamic Bank.
- Mohsin A Nathani, Managing Director and CEO, Citi Islamic Investment Bank EC.
- Iqbal Khan, CEO of HSBC Amanah Finance.
- Abdul Wahid Al Ulama, Legal Consultant and Advocate, Al Tamimi & Co.

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Bondweb MALAYSIA

MALAYSIA ISLAMIC BOND UPDATE

Bondweb MALAYSIA

RINGGIT ISLAMIC DEBT MARKET: FORTNIGHTLY SNAPSHOT

AS AT 14th Dec 2005

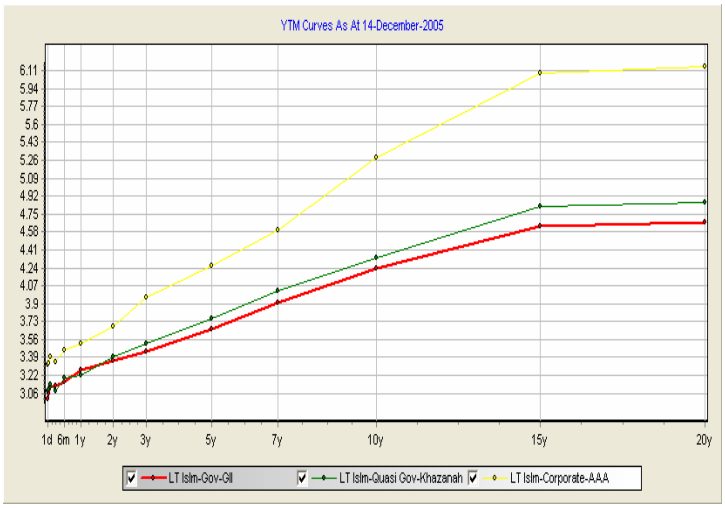
Key Benchmarks Trend (by volume)	Rating	This week close (RM)	7/12/2005 (RM)	30/11/2005 (RM)	23/11/2005 (RM)
Private Debt Securities					
PLUS PRIMARY BONDS SERIES 6 - 30.05.2008	AAA (RAM)	103.77	103.77	104.27	104.27
PLUS 0.00000% 16.06.2017 - SERIES 2	AAA (RAM)	50.94	50.60	50.50	50.50
CELCOM 0.00000% 15.04.2008	AA1 (RAM)	109.94	110.74	110.74	110.74
PLUS PRIMARY BONDS SERIES 7 - 29.05.2009	AAA (RAM)	106.17	106.08	106.55	106.56
PFK 4.55000% 31.03.2011	AAA ID (MARC)	100.00	101.65	101.65	101.65
Government Investment Instruments					
PROFIT-BASED GII 24/2005 08.12.2010	n/a	100.14	83.25	83.25	83.25
GII 1/2003 0.00000% 31.03.2008	n/a	92.62	92.62	92.62	92.81
GII 3/2004 0.00000% 29.10.2009	n/a	87.51	87.38	87.38	87.38
Quasi Government					
KHA1/99 IB 0-CP 7Y 17/3/2006	n/a	99.22	99.22	99.22	99.17
KHA1/01 700M 0-CP 5YR 20/3/2006	n/a	99.20	99.18	99.18	99.18
KHA1/05 1B 0-CP 5Y 18/01/2010	n/a	86.20	86.16	85.80	85.80
KHA2/03 1B 0-CP 5Y 18/9/08	n/a	90.73	90.73	90.73	90.85
KLIA 0.000% 30.01.2016 PN	n/a	124.37	124.37	124.37	124.37

SPREAD VS GII (in b.p)

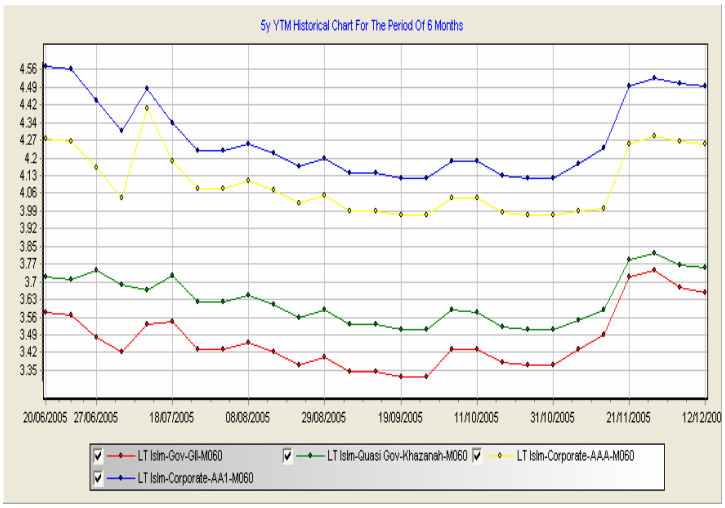
	TENURE					
	1-Year	2-Year	3-Year	5-Year	7-Year	10-Year
GII	3.27	3.36	3.45	3.66	3.91	4.24
Cagamas	0.1	0.23	0.31	0.23	0.26	0.23
Khazanah	-0.05	0.04	0.07	0.1	0.12	0.1
AAA	0.26	0.33	0.51	0.6	0.69	1.05
AA1	0.32	0.54	0.83	0.83	0.92	1.21
A1	1.01	1.24	1.51	2.23	2.7	2.81

MYR ISLAMIC DEBT YIELD CURVES

YTM Curves



5-YEAR YTM Historical Charts (weekly closing, over last 6 months)



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ISLAMIC LEAGUE TABLES

TOP 20 ISSUERS OF ISLAMIC DEBT — June 2005 – Dec 2005

	Issuer or Group	Nationality	Instrument	Amt US$ m	Iss.	%	Share Manager
1	Cagamas MBS	Malaysia	Asset-backed Sukuk Musharakah Islamic Bond	542	6	13.7	CIMB, HSBC, ABN AMRO, AmMerchant Bank
2	Islamic Development Bank	Saudi Arabia	Islamic Bond	500	1	12.6	Deutsche Bank, HSBC
3	PLUS Expressways	Malaysia	Serial Bai Bithaman Ajil Islamic Securities	349	4	8.8	CIMB
4	Syarikat Bekalan Air Selangor	Malaysia	Bai Bithaman Ajil Commercial Papers/MTN	273	4	6.9	CIMB, Bank Islam Malaysia, HSBC Bank (Malaysia)
5	Maybank	Malaysia	Islamic Subordinated Bond	265	1	6.7	Aseambankers Malaysia
6	Senai Desaru Expressway	Malaysia	Bai Bithaman Ajil Islamic Debt Securities	249	26	6.3	Aseambankers Malaysia, Standard Chartered Bank
7	DRB-HICOM	Malaysia	Bai Bithaman Ajil Islamic Debt Securities/Murabahah CP/MTN Facility	209	11	5.3	AmMerchant Bank, Malaysian International Merchant Bankers
8	Konsortium Lebuhraya Utara-Timur (KL)	Malaysia	Redeemable Secured Serial Sukuk Istisnah	207	9	5.2	CIMB
9	Ranhill Power	Malaysia	Islamic MTN Program	142	12	3.6	Aseambankers Malaysia
10	Antara Steel Mill	Malaysia	Al-Bai Bithaman Ajil Islamic Debt Securities	133	6	3.3	AmMerchant Bank
11	Sime Darby	Malaysia	Al-Murabahah CP/MTN Program	133	1	3.3	CIMB, HSBC Bank (Malaysia)
12	Cagamas	Malaysia	Bithaman Ajil Islamic Securities	132	1	3.3	AmMerchant Bank
13	Golden Crop Returns	Malaysia	Sukuk Al Ijarah	117	15	3.0	Affin Bank
14	Konsortium Lapangan Terjaya	Malaysia	Bai Bithaman Ajil MTN	101	9.0	2.6	Alliance Merchant Bank, United Overseas Bank (Malaysia)
15	Bayu Padu	Malaysia	Istisnah Serial Bonds	66	8.0	1.7	United Overseas Bank (Malaysia)
16	Konsortium Lebuhraya Butterworth-Kulim	Malaysia	Bai Bithaman Ajil Islamic Debt Securities	66	25	1.7	Bank Muamalat Malaysia
17	Sarawak Gateway	Malaysia	Redeemable Secured Serial Sukuk Ijarah	64	6	1.6	CIMB, RHB Sakura Merchant Bankers
18	Harum Intisari	Malaysia	Murabahah Commercial Paper/MTN Program	53	1	1.3	HSBC Bank Malaysia
19	Sweetwater SPV	Malaysia	Serial Bai Bithaman Ajil Islamic Securities	52	3.0	1.3	Avenue Securities
20	Focal Quality	Malaysia	Sukuk Al Ijarah	50	8.0	1.3	OCBC Bank (Malaysia)
	Total of issues used in the table			3,962	197	100.0	

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ISLAMIC LEAGUE TABLES

TOP 20 ISSUERS OF ISLAMIC DEBT — YEAR-TO-DATE

	Issuer or Group	Nationality	Instrument	Amt US$ m	Iss.	%	Share Manager
1	Pakistan International Sukuk	Pakistan	Sukuk Al Ijarah Sovereign Islamic Bond	600	1	9.4	Citigroup, HSBC
2	Wings FZCO	UAE	Islamic Sukuk Al Musharakah Issue	550	1	8.6	Dubai Islamic Bank, Standard Chartered Bank, HSBC
3	Cagamas MBS	Malaysia	Sukuk Musharakah Islamic Bond	542	6	8.5	CIMB, HSBC, ABN AMRO, AmMerchant Bank
4	Islamic Development Bank	Saudi Arabia	Islamic Bond	500	1	7.8	Deutsche Bank, HSBC
5	PLUS Expressways	Malaysia	Serial Bai Bithaman Ajil Islamic Securities	349	4	5.5	CIMB
6	Syarikat Bekalan Air Selangor	Malaysia	Bai Bithaman Ajil Commercial Papers/MTN	273	4	4.3	CIMB, Bank Islam Malaysia, HSBC Bank (Malaysia)
7	Maybank	Malaysia	Islamic Subordinated Bond	265	1	4.1	Aseambankers Malaysia
8	Senai Desaru Expressway	Malaysia	Bai Bithaman Ajil Islamic Debt Securities	249	26	3.9	Aseambankers Malaysia, Standard Chartered Bank
9	Jimah Energy Ventures	Malaysia	Istisnah Islamic MTN Facility	245	10	3.8	AmMerchant Bank, RHB Sakura Merchant Bankers, Malaysian International Merchant Bankers, Bank Muamalat Malaysia
10	Cagamas	Malaysia	Bithaman Ajil Islamic Securities	238	5	3.7	Cagamas/ AmMerchant Bank
11	DRB-HICOM	Malaysia	Bai Bithaman Ajil Islamic Debt Securities	209	11	3.3	AmMerchant Bank, Malaysian International Merchant Bankers
12	Konsortium Lebuhraya Utara-Timur (KL)	Malaysia	Redeemable Secured Serial Sukuk Istisnah	207	9	3.2	CIMB
13	Gold Sukuk dmcc	UAE	Islamic Sukuk Al Musharakah Issue	200	1	3.1	Standard Bank, Dubai Islamic Bank
14	International Bank for Reconstruction & Development – World Bank	Supranational	Bai Bithaman Ajil Islamic Debt Securities	200	1	3.1	ABN Amro Bank, CIMB
15	Musyarakah One Capital	Malaysia	Asset-Backed Sukuk Musharakah Issuance Program	176	7	2.8	CIMB
16	Special Power Vehicle	Malaysia	Bai Inah Islamic MTN Facility	163	13	2.6	Malaysian International Merchant Bankers, AmMerchant, RHB Sakura Merchant Bankers, Bank Muamalat Malaysia
17	Ranhill Power	Malaysia	Islamic MTN Program	142	12	2.2	Aseambankers Malaysia
18	Antara Steel Mill	Malaysia	Al-Bai Bithaman Ajil Islamic Debt Securities	133	6	2.1	AmMerchant Bank
19	Sime Darby	Malaysia	Al-Murabahah CP/MTN Programme	133	1	2.1	CIMB, HSBC Bank (Malaysia)
20	Golden Crop Returns	Malaysia	Sukuk Al Ijarah	117	15	1.8	Affin Bank
	Total of issues used in the table			6,396	264	100.0	

ISLAMIC LEAGUE TABLES

ISLAMIC DEBT		YEAR-TO-DATE	
Manager or Group	Amt US$ m	Iss.	%Share
1 CIMB	1,323	47	20.7
2 HSBC	1,224	18	19.1
3 Aseambankers Malaysia	531	39	8.3
4 AmMerchant Bank	506	50	7.9
5 Standard Chartered Bank	316	28	4.9
6 Citigroup	300	1	4.7
7 Dubai Islamic Bank	283	2	4.4
8 Deutsche Bank	275	3	4.3
9 EON Bank	246	47	3.8
10 RHB Bank	201	45	3.1
11 Bank Muamalat Malaysia	168	48	2.6
12 United Overseas Bank	117	17	1.8
13 Affin Merchant Bank	117	15	1.8
14 Cagamas	105	4	1.6
14 ABN AMRO	100	1	1.6
16 Standard Bank Group	100	1	1.6
17 Bank Islam Malaysia	91	4	1.4
18 Oversea-Chinese Banking Corp	88	19	1.4
19 Bahrain Monetary Agency	80	1	1.2
20 Avenue Securities	52	3	0.8
Total of issues used in the table	6,396	264	100.0

ISLAMIC DEBT	JUNE 2005 – DEC 2005		
Manager or Group	Amt US$ m	Iss.	%Share
1 CIMB	1,074	41	27.1
2 HSBC	741	16	18.7
3 Aseambankers Malaysia	531	39	13.4
4 AmMerchant Bank	383	21	9.7
5 Deutsche Bank	275	3	6.9
6 Standard Chartered Bank	125	26	3.1
7 United Overseas Bank	117	17	3.0
8 Affin Merchant Bank	117	15	3.0
9 EON Bank	104	11	2.6
10 RHB Bank	99	22	2.5
11 Bank Islam Malaysia	91	4	2.3
12 Oversea-Chinese Banking Corp	88	19	2.2
13 Bank Muamalat Malaysia	66	25	1.7
14 Avenue Securities	52	3	1.3
14 Alliance Merchant Bank	51	9	1.3
16 Andalan Artha Advisindo	30	1	0.7
17 OSK Asia Securities	13	4	0.3
18 Bank BNI	6	1	0.2
Total of issues used in the table	3,962	197	100.0

ISLAMIC DEBT BY COUNTRY		YEAR-TO-DATE	
	Amt US$ m	Iss.	%Share
Malaysia	4,205	255	65.7
UAE	750	2	11.7
Pakistan	600	1	9.4
Saudi Arabia	500	1	7.8
United States	200	1	3.1
Bahrain	80	1	1.2
Indonesia	61	3	1.0
Total	6,396	264	100.0

ISLAMIC DEBT BY COUNTRY	JUNE 2005 – DEC 2005		
	Amt US$ m	Iss.	%Share
Malaysia	3,426	194	86.5
Saudi Arabia	500	1	12.6
Indonesia	36	2	0.9
Total	3,962	197	100.0

ISLAMIC DEBT BY CURRENCY		YEAR-TO-DATE	
	Amt US$ m	Iss.	%Share
Malaysian ringgit	4,405	256	68.9
US dollar	1,850	4	28.9
Bahraini dinar	80	1	1.2
Indonesian rupiah	61	3	1.0
Total	6,396	264	100.0

ISLAMIC DEBT BY CURRENCY	JUNE 2005 – DEC 2005		
	Amt US$ m	Iss.	%Share
Malaysian ringgit	3,426	194	86.5
US dollar	500	1	12.6
Indonesian rupiah	36	2	0.9
Total	3,962	197	100.0

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