“MOBILIZING ISLAMIC FINANCE FOR SHARED PROSPECTIVITY
AND POVERTY”
WORLD BANK SEMINAR
OCTOBER 9, 2014
EVENT BRIEF

This high level seminar brought together more than 80 government officials, regulators, market players, academia, WB and IMF staff to discuss ways by which Islamic Finance can contribute to the World Bank Group’s twin goals, as well as explore the potential of using Islamic financial instruments to provide microfinance, support SME growth, expand infrastructure finance, and finance climate-friendly and socially responsible investments.

As Gloria Grandolini, Senior Director of Finance and Markets Global Practice at World Bank, emphasized “We at the World Bank, recognize the potential of Islamic finance and its core values. There is a cross-cutting relevance across the range of development solutions that the Finance and Markets Global Practice delivers and a strong linkage with the Bank’s twin goals of eliminating extreme poverty and promoting shared prosperity. Therefore, we are committed to expanding the use of Sharia-compliant modes of financing in Bank Operations, particularly for financing SMEs, infrastructure, business innovation and “green” investments.”

The seminar was moderated by Abayomi A. Alawode, Head of Islamic Finance, Finance and Markets Global Practice at World Bank. The panel convened leading experts on Islamic Finance, namely Aamir Rehman, Managing Director of Fajr Capital (Dubai), Jamel Zarrour, Chief Economist at Islamic Development Bank (TBC), Khaleel Ahmed, Chief Investment Officer, IFC, Michael Bennett, Head of Structured Finance, World Bank Treasury, and Khalid Howladar, Global Head of Islamic Finance, Moody’s.
Value Proposition of Islamic Finance

The Islamic Finance industry has expanded rapidly over the past decade with annual growth rates of 10-15 percent. Today, Shariah-compliant financial assets are estimated at over US$1.3 trillion, covering bank and non-bank financial institutions, capital markets, money markets and insurance (Takaful).

Islamic finance is a collection of modes of financing that already exist. When put together and followed correctly, those modes of financing can create a broader tangible value to society and community as a whole. Islamic finance is equity based finance, asset-backed finance, ethical, sustainable, environmentally and socially responsible finance. It is the exclusion of debt financing, and the promotion of modes of financing that discourage excessive leverage and immoral profits, and that encourage risk sharing and distribution of wealth.

Four basic principles guide Islamic Finance: 1) you cannot profit from something that is immoral or ethically problematic (i.e. arms manufacturing or weapons of mass destruction), 2) if you want a reward you have to take a risk, 3) you cannot sell what you don’t own, and 4) you have to be very specific about what you are buying or selling.

Islamic Finance and Socially Responsible Investment

There is a huge demand in conventional finance for ethical bonds where the proceeds have to be invested in ethical investments. This is somehow lacking in Islamic Sukuk, which despite being ethically structured, are not necessarily examined and tracked to the proceeds. The World Bank is now trying to promote the idea of ethical Sukuk where the proceeds are targeted to specific purposes, so that not only the Sukuk structure is Islamic but also the proceeds are in line with Islamic principles.

In 2006, the World Bank acted as treasury manager for an institution that funds immunizations to the poorest countries in the world, and issued the first bonds for that immunization facility, and saw a whole new group of investors that target socially and ethically responsible investors. The World Bank also issued green bonds to use for environmentally beneficial projects. The World Bank sees a great opportunity to put together these SRI investors who are suffering from the lack of supply of products, and the Islamic investors, where we create a product where the proceeds and not only the structure are supporting Islamic principles. This can result in a new market that benefit both groups of investors in terms of market size liquidity and the underlined projects from pricing efficiency and project diversity. The World Bank can achieve this by bringing the immunization facility mentioned above to the Sukuk market.

The World Bank is also trying to shift focus of banks and financial institution to financing SMEs, microfinance, affordable housing, education system, and encouraging those banks and financial institutions to issue Sukuk along those same lines.
**Islamic Finance and Infrastructure Finance**

There is a big complementarity between infrastructure finance and Islamic finance for a number of reasons: 1) Islamic finance seeks real assets to be financed and infrastructure finance provides those tangible assets for financing, 2) the way that infrastructure finance can be structured is that investors can have ownership in assets, and the cash flow generated from those assets flow back to investors, and 3) the ethical dimension based on which money has to be allocated to its best use and to help communities and societies as a whole.

The current Sukuk market is not completely conforming to the Islamic finance principles as mentioned above. Sukuk fall under the fixed income market and they are considered credit instruments. Infrastructure Sukuk is still a bank dominated market, with Islamic banks high on liquidity. Project finance Sukuk market hasn’t yet taken off yet, but given the high demand for infrastructure funds, the market is expected to take off during the next 18-24 months.

**Islamic Finance & Financing Innovation**

In order to increase its economic role and become more main stream and efficiently compete with conventional finance, Islamic Finance needs new innovative and forward looking instruments to complement the traditional ones. In addition, Islamic finance needs to move its focus from real estate and commodity sectors to broader real sector. Building capacity and developing risk management and governance are essential in this matter.

**Takeaway Messages**

*Risk has no religion.*

*Best practices come from common sense.*

*You cannot sell what you do not own.*