

Muhammad bin Ibrahim: Malaysia and Turkey – the new silk route in Islamic finance – strategies for collaboration, cooperation and smart partnership

Opening remarks by Mr Muhammad bin Ibrahim, Deputy Governor of the Central Bank of Malaysia, at a business seminar on Islamic finance Istanbul: “Malaysia-Turkey Islamic finance cooperation: new solution – preferred partner”, Istanbul, 29 September 2011.

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I have the honour today to welcome distinguished guests to the Business Seminar organised by Bank Negara Malaysia, held in this beautiful and historic city of Istanbul. The theme “Malaysia and Turkey: The New Silk Route in Islamic Finance – Strategies for Collaboration, Cooperation and Smart Partnership” was chosen as a reflection of our desire to strengthen economic and business ties for the mutual benefits of both countries. The emergence of the “Silk Route”, a term coined by Governor Dr Zeti in 2006 opens up exciting prospects for countries and businesses. The new “Silk Route” not only carries traditional trade of goods and services of old but also manufactured goods, technological innovation and know-how, portfolio flows, private equity investment and mobility of human capital and knowledge. Today, Islamic financial products and services are truly “new” additions to this trade.

Let me first express our heartfelt appreciation to His Excellency Tun Dr. Mahathir Mohamad for accepting our invitation to speak at this event, sharing his thoughts on Islamic finance. Tun Dr. Mahathir needs no introduction. Among his many achievements was the time he steered the country during the 1997 – 98 Asian crisis. His unorthodox policies then have become mainstream now. Under his leadership, Malaysia experienced modernisation and economic prosperity, a development most profound for my generation. That modernisation included the early development of Islamic financial system. From the seeds planted during Tun Mahathir’s time, we are now seeing the maturing of the Islamic financial system in Malaysia that is innovative, competitive and increasingly internationalised. What was once a novelty has become an alternative means of conducting business. We owe this very much to Tun Dr. Mahathir’s foresight and wisdom. Not many people today realised that one of the first actions that Tun Dr. Mahathir took when he came to office in 1981 was to set up a National Steering Committee to implement Islamic banking in Malaysia. The report of this committee on the viability and strategy of the Islamic banking, was the impetus for the creation and robust development of the Islamic financial industry in Malaysia. The rest they say is history.

Global economic challenges and Islamic finance

The world is transforming and its transformation is way beyond what we had seen before. This is an era of radical change, new rules are being formulated, standards and best practices that were in vogue hardly 5 years are now considered insufficient. It is changing at a scale and speed we had never experienced before, that require us to accelerate our own pace of transformation, to enable us to survive and prosper under this “new normal” operating environment. The world is currently faced with wide-ranging challenges that include among others – excessive indebtedness, at household businesses and at sovereigns. Many are grappling at finding the solutions to overcome the complex issues facing them today. Some of the problems look uncannily similar to what we had faced in the 1990s, but the solutions might be different this time. But whatever that solution might be, we must never discount any probable answers including unorthodox measures. Experience during the Asian Financial Crisis had shown that unconventional measures could very well be the future best practices. But then, yesterday’s solution may no longer be adequate to address today’s challenges. Therefore, we must endeavour to search for new alternatives

and embark on new ventures that could mitigate the contemporary issues and challenges confronting us. And this is where Islamic finance can fit in and play a meaningful role.

As an objective, we need to build the foundations for a stronger and more inclusive global economy with sustainable growth and greater shared prosperity by all. This objective is in fact fundamentally in line with the role and relevance of Islamic finance. Islamic finance emphasises on attainment of socio-economic goals espoused on Shariah objectives. It emphasises on a strong linkage to productive economic activity to generate legitimate income. It also emphasises on accountability, fairness and transparency. All these reflect the fundamental values propagated in Islamic finance that could serve as a stable and resilient form of financial intermediation. When Islamic finance is applied in an appropriate and structured manner, it has a strong prospect to serve as a contributor to a sustainable global economic growth and financial stability.

The infrastructure already established in Islamic finance today is ready to serve as an effective intermediary for the conduct of global business including promoting greater intra-regional trade not only within Asia but between the various regions of emerging markets. With more than 600 Islamic financial institutions that now operate in more than 75 countries, growing at an annual rate of about 15 per cent, Islamic finance can be a platform to strengthen economic ties between East and West Asia in trade and investments flows. The sukuk market in particular, has evolved as an important avenue for international fund raising and investment activities, generating significant cross-border flows. Sukuk issuances have grown in diversity and sophistication. The diverse sukuk structures of Ijarah, Istisna, Murabahah, Musyarakah and Mudharabah have expanded to form hybrid sukuk which include exchangeable and subordinated sukuks, thus increasing its usability and compatibility to fund various forms of financing. For example, huge amount of funds could be raised, via sukuk, for the purpose of financing large infrastructure projects. It is this substantive advancement in Islamic finance that we believe greater business and investment ties could be built upon to enhance economic relationship between Turkey and Malaysia.

Turkey-Malaysia vast growth opportunities

For Turkey and Malaysia, a productive partnership could be created when both parties are able to harness the strengths of each other. Turkey is Malaysia's eighth largest trading partner among the OIC member countries, has had a significant growth in terms of its trade with Malaysia, which has expanded at an annual average rate of 22.4 percent since 2006. While the volume of trade and investment between the two countries is still relatively small, where Malaysia's trade with Turkey accounts for 0.3 percent of Malaysia's total trade and Malaysia's investment in Turkey totalled to USD56.2 million as at end-2010, the figures also reflect the enormous opportunity for further growth. Turkey's Prime Minister The Honourable Recep Tayyip *Erdoğan*, during the recent visit by the Malaysian Prime Minister to Turkey, has suggested a leadership aspiration for trade volume between Malaysia and Turkey to grow from USD1.3 billion to USD5 billion. With commitment and hard work, this target is certainly not impossible to achieve. I believe with a Strategic Framework Agreement that is planned to be signed later this year between our two Governments would further strengthen cooperation between the two through identification of important areas where we could focus and work on.

Opportunity to enhance trade and financial linkages between Turkey and Malaysia is immense. Collaboration between the two countries could be in many forms; for instance Turkish investors and financial institutions could use Malaysia as a gateway to the Asean region. Malaysian financial community could use Turkey as a base to Central Asian region and Europe. In the area of Islamic finance, Malaysia is committed to be a partner with Turkey to further promote the business prospect in this country. Malaysia being an Islamic financial hub in Asia is willing to share with Turkey our 30 years of experience in developing its Islamic

financial industry and our knowledge and insights in operating an Islamic financial system that runs parallel with its conventional counterpart.

Potential Turkey-Malaysia partnership in Islamic finance

There are vast opportunities for Turkey-Malaysia bilateral cooperation, however let me mention five key areas of possible cooperation that could increase cross-border activities between our two countries. These are in the area of sukuk issuance, promoting cross-border activities, Islamic fund management, partnership in innovation and in education and research.

Firstly, in the area of sukuk issuance, we welcome Turkish financial and business community to use Malaysia's comprehensive and tested infrastructure with its extensive investors network as a platform to raise funds such as sukuk and Islamic syndication financing. The multi-currency sukuk market in Malaysia is well developed and active with over 60% of the outstanding sukuk in the world originating from Malaysia. There is also the opportunity to list the sukuk on Bursa Malaysia, the Malaysian bourse, which has emerged as the largest exchange for sukuk listing in the world. This gives the listed sukuks greater profiling, visibility and transparency in the global bond market. Collaboration in issuance of sukuk would indeed benefit Turkey, as Turkey's aggressive diversification of its industrial base and services sectors will require huge financing needs that could be partially met through the Islamic financial markets. Large infrastructure projects such as building the Bosphorus shipping canal, the new railway lines and highways might require funding via issuing sovereign sukuk as an alternative source of funding. The extensive privatisation in basic industry –transportation, communication and banking – would also offer the corporates and alternative source of financing that is competitive and innovative.

Secondly, in promoting cross-border financial activities, the Turkish financial community could network with Malaysian-based investors, and practitioners to facilitate more business opportunities. Malaysia has diverse domestic and international players that engage in international currency business. There are now 150 entities in Malaysia's Islamic financial system which offer a wide spectrum of Islamic products and services. There are also more than 150 funds in Malaysia including real estate investment funds (REITs) and ETFs that practise ethical investments. These entities have the capabilities to structure funds for investment abroad, including into the emerging markets. Additionally, there are opportunities for ethical investments as more than 80% of equities listed on the Malaysian stock exchange are shariah compliant. As one strategy to enhance cross-border financial activities, Turkish banks and relevant entities might wish to consider being members of Bursa Suq Al Sila' to facilitate liquidity management in the Islamic financial market. The Bursa Suq Al-Sila' is the world's first end-to-end Islamic multi-currency commodity trading platform to enhance liquidity management for Islamic financial institutions. This fully-electronic platform facilitates sukuk structuring, Islamic financing and investment transactions including inter-bank placements and customer deposits, by applying the concept of murabaha and tawarruq. Since its establishment in 2009, 23 Commodity Trading Participants from Malaysia, the Middle East and Europe have been registered in Bursa Suq Al-Sila', contributing to the growth in its trading volume where 1370 trades were recorded in Q1 2011 with a total value of USD18 billion as compared to 728 trades in the final quarter of 2010 that totalled to an estimated USD11 billion.

Thirdly, opportunities to collaborate in the area of Islamic fund management. Following the launch of the first Participation Bank Index by the Istanbul Stock Exchange earlier this year, the investment products introduced in the Turkish market have been expanded to include Islamic equity funds and products. Through collaboration and strategic alliances between Malaysian Islamic fund management companies and the participation banks in Turkey, the development and distribution of Shariah compliant funds across borders could be made possible and new investment options to divest the savings of retail clients, as well as in the

development of investment strategies to meet the needs of high net-worth individuals or sovereign funds.

Fourthly, partnership in innovation – where the Malaysian and Turkish financial community could jointly develop innovative products and investment instruments, provide consultation and advisory services on complex legal, accounting, tax and Shariah matters as well as developing human talent to support the development of Islamic finance. Joint Shariah research could also be conducted with International Shariah Research Academy, dedicated research in applied Islamic finance based in Kuala Lumpur.

And finally, on the education and research front, possible collaboration can be explored between the International Centre of Education in Islamic Finance or INCEIF and Turkish universities to give opportunities for Turkish students to enrol in professional and post-graduate programs. Students from Turkey intending to deepen their knowledge in Islamic financial industry are encouraged to consider learning opportunities offered by Malaysia including possible attachments with Malaysian financial institutions. As I speak, efforts to develop human capital are already taking place now, as a team from the Malaysian financial community led by the Central Bank of Malaysia is conducting a capacity programme on Islamic finance in Ankara. This programme is held in collaboration with the Islamic Development Bank. The programme offers wide ranging topics for Islamic finance and caters to the needs of a group of central bankers, regulators and Government officials. We wish to thank the Central Bank of the Republic of Turkey for their support for making this training initiative possible.

Before I end my remarks, I would like to take this opportunity to re-emphasise our commitment to strengthen strategic collaboration with Turkey. With me is a delegation of the Malaysian financial institutions, investment institutions and professional firms ready to explore, engage and leverage on each other's market opportunities. There is much that can be done by both sides to jointly explore and realise the potential for mutual benefits. I strongly believe that today's event will end on a positive note, with both Turkish and Malaysian delegation able to identify on the next steps. It is our fervent hope that the business and financial community of both countries would establish regular contacts to further strengthen collaborative network and to follow through on some of the understandings reached today.

I take this opportunity to offer for the next follow meeting or seminar to be held in Malaysia. It is always useful to see first-hand the opportunities and prospect that Malaysia has to offer. I wish to thank you all for your participation in making this event a success and to His Excellency Tun Dr. Mahathir Mohamad and the panel of speakers for the ideas, pointers and suggestions that you would share to make this event a successful one.