

Muhammad Al-Jasser: Overview of the Islamic banking industry

Speech by Dr Muhammad Al-Jasser, Governor of the Saudi Arabian Monetary Agency, at The Fifth Conference for Islamic Banks and Financial Institutions, hosted by the Central Bank of Syria, Damascus, 15–16 March 2010.

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In the Name of Allah, the Most Gracious, the Most Merciful

Let me first thank the Central Bank of Syria, the official sponsor of the Fifth Conference for Islamic Banks and Financial Institutions, and, in particular, I would like to thank the Bank's Governor, His Excellency Dr. Adeen Mayalah.

Ladies and Gentlemen,

Islamic banking has grown widely in recent years and has extended to several international financial centers, which invested in this field, reflecting an increasing interest in financial Islamic products and services. Because of this interest, some of the international markets indices such as "Dow Jones" and "FTSE" have been launching indices for Shari'ah-compliant activities since 1999. According to the latest available data, the Islamic financial institutions' assets exceeded \$822 billion by end of 2009, and they are expected to exceed \$1 trillion by end of 2010. In addition, issuance of Islamic Sukuk has risen fourfold over the last four years, exceeding \$100 billion by end of 2009.

Islamic banks and financial institutions account for 15 percent of the Middle East top 30 banks' assets. There are more than 430 Islamic banks and financial institutions in more than 75 countries and about 191 conventional banks have Islamic windows. By the end of the third quarter of 2009, the total assets of Islamic investment funds were estimated at about \$ 27 billion, spread across 478 Islamic investment funds worldwide.

Dear audience

Islamic banking contributes to **social and economic development** through investment in areas related to the real economy such as production of goods and services and commerce. In addition, Islamic Banks and Institutions have proved their success in attracting savings, fulfilling customer's needs and achieving their interests. Moreover, Islamic banking has made great strides in boosting banking business by **introducing innovated products and tools** and by adopting new financing forms such as Ijarah (leasing), Istisnaa and Salam, along with Mudarabah (profit and loss sharing) and Musharakah (partnership). Furthermore, a variety of Islamic Sukuk (Islamic bonds) has emerged, and some Islamic banks have started to arrange for syndicated financing transactions in accordance with Islamic forms, and others are managing Shari'ah-compliant investment funds. Every tool of the Islamic banking has its own contractual nature and features, which differ from other tools in terms of risks, guarantees and pricing.

Islamic banking services have not been confined to the activities mentioned earlier, but the scope of their transactions has been extended to include **other services** such as: providing joint finance, issuing banking bonds and opening letters of credit. Islamic institutions and banks provide a variety of finance and insurance methods for enterprises, management of financial portfolios, and Tawarruq assets (assets securitization). Moreover, Islamic institutions and banks have played an effective role in supporting economic reforms and privatization programs in countries where they work by purchasing shares in listed companies and financing some private activities, thereby helping in supporting the basic infrastructure and financing of housing projects for low and middle income people. They have

also contributed to supporting small and craft projects, and indirectly helped in creating many job opportunities for citizens.

Ladies and Gentlemen,

The achievements of the Islamic banking industry over the last three decades have necessitated the **establishment of relevant institutions that support Islamic banking** such as: the Accounting and Auditing Organization for Islamic Institutions (AAOIFI) and the Islamic Financial Services Board (IFSB). All these organizations aim at creating a sound environment for collaboration and communication among Islamic banks and financial institutions by introducing and applying International standards to improve the Islamic banking industry and ensure its soundness.

Let me briefly talk about **the necessary requirements to ensure the sustainability, stability and soundness of Islamic banking. The Islamic Financial Services Board (IFSB)** plays an effective role in abiding by supervisory requirements for sustainability through issuing supervisory and control standards for the Islamic banking system, based on the best supervisory practices in line with Basel II standards, focused on: capital adequacy, risk management, internal control, institutions management controls, transparency and market discipline.

The IFSB has urged the Islamic institutions to follow specified procedures for assessing their capital adequacy in terms of the nature of risks and pursue strategies to maintain their capital at required levels. It has also required supervisors to review and assess internal assessment measures of these institutions' capital adequacy and ensure their compliance with the required capital level and take supervisory measures in case of non-compliance. In addition, the Board has urged supervisory authorities to take prudential measures to prevent the decrease of capital to lower than minimum level, and stipulate quick correcting measures in case of such a decrease. Stress tests are considered one of the prudential measures that the Islamic Financial Services Board (IFSB) is keen to emphasize, and it urges Islamic financial institutions to apply them, including the assessment of prudential and control steps to reduce qualitative and quantitative risks, apart from applying transparency and accounting disclosure in financial reporting.

In the realm of **coordination with the national supervisory authorities**, the IFSB seeks to enhance work in the area of consolidated and effective supervision and ensure the stability of the Islamic financial system by abiding to best practices for risk management and transparency. In this vein, the IFSB organizes conferences and symposiums for supervisory authorities and those interested in this industry. The IFSB also endeavors diligently to work with international and regional institutions, research centers and educational institutes to promote this significant industry.

Dear audience,

In Saudi Arabia, we are aware of the importance of Shari'ah-compliant banking products and services. The Saudi Arabia Monetary Agency (SAMA) encourages banks operating in Saudi Arabia to meet market demands and provide those services. Currently, all banks operating in Saudi Arabia provide Shari'ah-compliant services, and this activity is rapidly growing. The size of this activity differs from one bank to another. Some banks only provide Shari'ah-compliant products and services, and others provide such services and products through some specific branches or units.

We, at SAMA, supervise and regulate Shar'iah-compliant activities in accordance with the same practices applied to conventional commercial banking businesses. Hence, standards of capital adequacy, liquidity, and other supervisory and monitoring requirements apply on Shari'ah-compliant institutions and banks. SAMA, in cooperation with Saudi banks and

financial institutions, has deep-rooted international standards (such as those set forth in Basel II and those prescribed by the IFSB) for risk management, corporate governance and internal controls.

Dear audience,

There are many ***challenges posed to Islamic banking*** such as finding new and various opportunities for development, innovation of new tools, boosting its human resources in all fields including in risk and liquidity management, promoting customer service level, improving skills and expertise for promoting the understanding of Shari'ah teachings and applying them in new banking and finance areas. In addition, it is appropriate for Islamic Financial Institutions to increase efforts to train human resources scientifically to enhance their capabilities and to conduct further studies to update Islamic services and products and improve Islamic banking in the long run.

Moreover, it is necessary to use uniform accounting and auditing standards to ensure safety and stability of Islamic banking. It is also encouraged that Islamic financial institutions merge to increase their capital and have more liquidity to finance their investments. Finally, Islamic financial institutions need to steer efforts towards good corporate governance, good risk management, transparency, and financial disclosure.

I hope that the Islamic banking industry will achieve further prosperity and success in the future. Thanks again to the Central Bank of Syria for hosting this conference and for the interest in Islamic banking, and I think it is timely and wise to choose this topic for the conference. I wish all success for this conference and the participants and I thank you all for your kind attention.

Wassalmu Alikum Warahmatu Allah Wabarakatuhu.