

Zeti Akhtar Aziz: Raising the bar for the next phase of growth and development – sustaining transformative momentum

Welcoming address by Dr Zeti Akhtar Aziz, Governor of the Central Bank of Malaysia, at the 10th IFSB (Islamic Financial Services Board) Summit 2013 “The future of the Islamic financial services industry – resilience, stability and inclusive growth”, Sasana Kijang, Kuala Lumpur, 16 May 2013.

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It is a great pleasure to welcome you to this 10th IFSB Summit, on the “***The Future of the Islamic Financial Services Industry: Resilience, Stability and Inclusive Growth***”. Bank Negara Malaysia is most honored to host this year’s summit, which is held in conjunction with the 10th anniversary of the Islamic Financial Services Board (IFSB). It was here in Kuala Lumpur 10 years ago that we witnessed the momentous occasion of the IFSB inauguration, that was the culmination of international collaboration among the founding member countries with the support of several key international and multilateral institutions. Its landmark establishment in 2002 as the international prudential standard setting body for the Islamic finance marked a major milestone in the effort to strengthen the international infrastructure for the Islamic financial system, steering the path for its successful integration as a viable component of the global financial system. A decade on, the work of the IFSB in ensuring a cohesive cross-border regulatory framework and the international best practices that are attuned to the intrinsic characteristics and peculiarities of Islamic financial intermediation, have served to underpin the development of a sound and stable Islamic financial system, ushering in a phase of rapid growth and greater internationalization of the industry.

Indeed, 10 years since the founding of the IFSB have been a period of significance, during which the Islamic financial services industry has grown impressively with its landscape dramatically evolved. This growth acceleration has been accompanied by the widening of its geographical reach transcending its traditional borders in Muslim majority countries to the more established financial centres. In addition, Islamic finance has evolved as a comprehensive system of intermediation servicing all segments of society, including governments, businesses and households regardless of scale of businesses and income levels. In this decade, Islamic finance has also evolved from being domestic-centric to become increasingly internationalized, intermediating funds across borders and becoming a new vehicle that bridges economies and fostering closer financial linkages, particularly among emerging and developing markets.

As a form of financial intermediation that is well anchored to serve the real economy, Islamic finance offers distinct potential to achieve the goals of inclusive growth and financial stability. Its foundations have been strengthened with the setting up of the IFSB and before that, the Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI), have taken the lead in setting the prudential and accounting standards for the industry. Combined with continuous capacity building initiatives and institutional development, it has resulted in the opportunity to achieve scale and has allowed the Islamic financial services industry to transition into a dynamic, fast growing and competitive form of financial intermediation for the global community.

The IFSB today is celebrating its tenth anniversary in a world which is changing profoundly. A new growth and development agenda is unfolding before us. Given the severe damage and devastation caused by the global financial crisis and the ensuing economic downturns, the road to an enduring recovery and lasting prosperity demands a global policy response that brings about a new economic trajectory built on a strong, more inclusive and more sustainable growth path. Common challenges that have also come to the forefront, such as poverty, increasing inequality and the imperative for greater social cohesion, have also called for the construction of policy objectives and strategies that can enhance stability, social well-

being and environmental sustainability. In the wake of the global financial crisis, there is consensus on the need for a return to financial systems that serve the real economy, and the demands for more responsible financial practices from the financial sector, that also includes the commitment to achieve socio-economic goals.

In response, the international community is prioritizing financial stability by strengthening financial regulation. This includes financial reforms aimed at protecting depositors from excessive risk-taking, over-leveraging and unfettered innovation. The reform initiatives have also focused on enhancing capital and liquidity standards, reinforced by moves to strengthen the macro-prudential orientation of regulation to complement micro-prudential supervision to manage the risks arising from the interdependencies within the financial system. Whilst the breadth of regulatory changes being considered collectively endeavor to strengthen financial system resilience, the key challenge for policymakers and regulators going forward is also to achieve *inclusive* and more sustainable *growth*, whilst ensuring *financial stability*.

Whilst Islamic finance has benefited from a well-developed, more competitive and well regulated eco-system, it needs to build on and reinforce the solid foundations that has been achieved in this decade. As the industry transitions into a new era of growth and development in this post-crisis world, the competitive financial landscape is being redrawn by the evolving international regulatory reforms, changing operating models, rising consumer expectations and increased competition. In this more challenging environment, the success of sustaining the momentum of Islamic finance as a transformative agent for the economy, will hinge on the ability to ***keep raising the bar in the pursuit of an effective functioning and sound Islamic financial system.***

Post-crisis, the increased emphasis for inclusive and sustainable products as well as responsible corporate behavior provides clear potential for Islamic financial players to demonstrate leadership by capitalizing on core value propositions of Islamic financial intermediation. There is also scope for greater leverage on the advances of technology and new institutional arrangements that can enhance operational excellence, particularly distribution channels for extending outreach to the range of users from households to microenterprises and small and medium scale enterprises.

In addition, innovations in Islamic financial solutions will need to take into account the higher regulatory expectations for more transparency, and the need for the effective management of risks and capital. This involves strengthening the resilience of the Islamic financial system in alignment with the evolving international regulatory developments thus raising the bar of industry performance. The IFSB has made significant advancements in leading the efforts to review specific measures put forward by the Basel Committee for possible adoption in Islamic finance. Further to this is the imperative to cultivate a strong risk culture within institutions. Reinforced by a robust shariah governance framework, it will ensure that innovation for furthering the development of Islamic finance is harnessed within the boundaries of the Shariah, which would avert overzealous innovative activities that could undermine financial stability.

Let me conclude my remarks. Much has been achieved, both in terms of the role and contribution of the IFSB, and the advancement made by Islamic finance in this recent decade. This has been an outcome of cumulative efforts to strengthen the foundations of the Islamic financial system. As the industry gears itself for the next phase of growth in the more challenging environment, our commitment and strategies to keep raising the bar to bring Islamic finance to a new level will enhance its prospect to contribute to achieving our shared vision of inclusive growth in an environment of financial stability.