

## **Zeti Akhtar Aziz: Into the next chapter – transformative changes to strengthen industry linkage with the real economy**

Keynote address by Dr Zeti Akhtar Aziz, Governor of the Central Bank of Malaysia (Bank Negara Malaysia), at the Global Islamic Finance Forum 2014 “Into the Next Chapter: Transformative Changes to Strengthen Industry Linkage with the Real Economy”, Kuala Lumpur, 2 September 2014.

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It gives me great pleasure to welcome you to this fourth Global Islamic Finance Forum. In this new era of great transformative change in the world, the growth and evolution of Islamic finance has continued to be very much part of the changing configuration of the global financial system. An important part of this ongoing change, is the growing internationalisation of Islamic finance, that has resulted in greater cross-border financial flows which has in turn facilitated greater and more diversified economic inter linkages between countries. With this increased pace of the internationalisation of Islamic finance, the total global financial assets of the Islamic financial industry is now estimated to be more than US\$2 trillion. The growth has continued to gain scale with its geographical outreach now extending beyond Muslim countries to the more established international financial centres and to other emerging economies. Across continents, Islamic finance is therefore having an increasing role in intermediating funds across borders and creating greater financial and economic inter-linkages.

The increasing international dimension of the global sukuk market, in particular, affirms its offering as a distinct platform upon which international inter-linkages are fostered. The upcoming debut sovereign issuances from established financial centres and emerging markets and the increasing diversity of the composition of sukuk investors across continents, in addition to the growing trend for multi-currency sukuk issuances, cumulatively contribute towards strengthening the dynamism of the sukuk as a global product for fund raising and investment activities in the international financial markets. Malaysia, has witnessed an increasing trend of issuances of foreign currency denominated sukuk in our domestic sukuk market, reinforced by an increasingly wider investor base as reflected by the increased and more diversified foreign investor participation in such issuances.

In parallel with this rapid growth of cross-border financial flows has been the increased attention to the development of the international financial architecture relating to financial stability in the Islamic financial system. With the important two international institutions already well established, that is, the accounting standards setting organisation, AAOIFI, and the prudential standard setting body, the IFSB, concerted global efforts have been directed towards the progressive implementation of the recommendations in the eight building blocks identified in the Islamic Finance and Global Financial Stability Report 2010. In particular, the efforts have been focused on the adoption and operationalisation of the prudential standards and the development of the potential for effective liquidity management as part of the efforts to safeguard financial stability. It is encouraging that there has been a higher adoption of the prudential standards issued by the IFSB, with implementation by 13 regulatory and supervisory authorities worldwide with indications that there are more in the pipeline. Taking into account the distinct characteristics and specificities of Islamic finance, the effective implementation of these standards will contribute towards maintaining the soundness and stability of Islamic financial institutions.

Liquidity management in the international Islamic financial system has also been strengthened with the establishment of the International Islamic Liquidity Management Corporation (IILM) in 2010 that will contribute towards facilitating efficient liquidity management and cross-border flows by Islamic financial institutions. On the domestic front, in Malaysia, the upcoming issuance of a ringgit denominated Mudharabah Certificate for

liquidity management purposes by the central bank is the introduction of a new profit sharing instrument that is expected to contribute towards increasing the range of instruments in the global Islamic short term securities market. With returns that are linked to the performance of the underlying asset and tradability in the secondary market, it is expected to draw significant interest of international investors.

### **Moving forward: transformative changes to grow beyond numbers**

The efforts taken to strengthen the global financial infrastructure of Islamic finance thus far have provided a solid foundation for the growth and internationalisation of the industry that is underpinned with soundness and stability. While the rapid growth of Islamic finance, attests to its resilience and competitiveness, the challenge before us is also to enhance its capacity to contribute towards inclusion and more balanced economic growth. Statistical numbers and projections are important performance indicators and benchmarks for the industry. However, the growth of the industry has to extend beyond the numbers to sustain its growth momentum. This is of particular importance in today's environment of growing global uncertainties and when considerations that prioritise the linkage of finance to the economy, justice and fairness, and sustainability and inclusion and which have been regarded as essential elements of a modern financial ecosystem. Islamic finance, with these inherent features and ethical dimensions, therefore has an immense potential role as a transformative agent in the economy, particularly in serving the requirements of the real economy and the broader society. Of importance is thus the role of the global Islamic financial marketplace in facilitating greater linkages with the real economy and inclusion and thus balanced growth.

In evolving into the next growth phase, it remains an imperative for the Islamic banking industry in the global marketplace to reinforce meeting the very objective of its existence as an effective form of financial intermediation that serves the real economy and that complies with the requirements of the Shariah. As an extension to this, Islamic banks have the potential to extend its role to also include the role as an investment intermediary. This would require the diversification of banking business to expand beyond credit intermediation to investment intermediation, in which the alternative modes of risk sharing contracts can be applied. In performing investment intermediation, Islamic banking institutions not only strengthen further the linkage of finance and real economic activity, but also contribute towards more inclusive and more balanced growth.

In the Malaysian Islamic finance marketplace, the changes associated with the modernisation of laws facilitate the maturing of the Islamic finance industry, with the enactment of the new Act in 2013. It includes new provisions that strengthen the potential role of Islamic financial institutions as investment intermediaries for risk-sharing to effectively take place. Legal recognition of investment accounts provides differentiation from deposits, which thereby opens up the avenue for Islamic financial institutions to further explore the various modes of operationalising such investment accounts.

In advancing this quest, technological advances need to be leveraged upon to develop new innovative platforms that can facilitate the implementation of investment accounts. Aimed to assist Islamic financial institutions in performing this investment intermediary function more efficiently, a multi-bank platform is currently being developed in Malaysia to effectively and efficiently match funds from potential investors with industries and ventures in the real sector. The platform would facilitate efficient mobilisation of private sector funds, both from individuals and corporates to finance targeted industries and ventures that are in need of funding. The platform would also be positioned to spur international connectivity as its outreach will also extend to international participation from foreign Islamic financial institutions and investors, through the offering of multi-currency financing options for foreign projects.

The potential for Islamic banks to progressively chart into this new territory would need to be supported by a state of readiness in terms of the capabilities of the industry to venture into a

diversification into such business offerings. In preparing for a business landscape with different complexities, talent development in Islamic finance will need to be accorded with an even greater priority. Existing talent needs to be equipped with the necessary skills to support the expansion into areas of specialisation that include investment intermediation. Stronger knowledge in the value propositions of the investment instruments require a greater understanding on the risks associated with business ventures in the respective growth areas, including in the non-traditional markets. This would require determining the viability of such business and investment proposals. Additionally, at the management level, and the directors and Shariah scholars of Islamic financial institutions need to be adequately equipped with the necessary knowledge so as to have an understanding important for steering the business to the new directions of the industry.

To realise the vision of a highly competent and high performing workforce in the Islamic financial sector, of equal importance is the standards of quality of the education programmes in Islamic finance and to raise the level of professionalism of Islamic finance practitioners. The Finance Accreditation Agency, an international and independent quality assurance and accreditation body for the financial services industry that was established in Malaysia in 2012, has raised the bar for Islamic finance talent and professionals. The introduction of its Finance Qualifications Structure that will be launched today has strategic significance, as it aims to link the various qualifications relevant to financial practitioners under a cohesive framework which will allow for greater mutual recognition on qualifications and provide clear and systematic learning path for financial professionals. Complementary to this initiative is the launch of the Learning Standard to ensure more global consistency for learning contents across the financial services industry in line with international industry benchmarks.

Technology can also be explored to remove barriers or impediments in promoting greater interconnectedness in Islamic finance as we aim to create stronger linkage with the real sector. As a catalyst to improve market access and enhance outreach, technology has the potential to disseminate information more efficiently, to promote greater market transparency and price discovery. Today, the launch of the digital application for Islamic finance is a further pioneering platform to facilitate sharing of information and for greater engagement, including between industry players that transcend borders. Such innovation is an impetus for raising greater awareness on benefits of Islamic finance as a form of financial intermediation.

### **Realising cross-border business opportunities for greater linkages**

The next frontier of Islamic finance beckons the global Islamic finance marketplace to evolve its business models to that which would strengthen the nexus of Islamic finance with the real economy. This is an important consideration in our strategies, in parallel with the efforts to further increase the internationalisation of Islamic finance that can cumulatively contribute towards strengthening economic linkages and thus enhance international economic connectivity.

Themed “Marketplace for Global Linkages”, with the presence of more than 1000 participants from various industries across the globe, this year’s Global Islamic Finance Forum brings unique opportunities for industry players to realise cross-border business opportunities for growth. It is our hope that this international platform would also provide the opportunity for intellectual engagement that would generate new thinking and knowledge as the industry ventures to new frontiers. On that note, I declare GIFF 2014 open and I wish you a productive and successful Forum.

Thank you.