

Muhammad bin Ibrahim: The “Islamic Finance Country Report for Malaysia 2015”

Keynote address by Mr Muhammad bin Ibrahim, Deputy Governor of the Central Bank of Malaysia (Bank Negara Malaysia), at the launch of the “Islamic Finance Country Report for Malaysia 2015”, Kuala Lumpur, 30 June 2015.

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Thank you for the invitation today to officiate the launch of the “Islamic Finance Country Report for Malaysia 2015” published by IRTI, the research and training arm of the Islamic Development Bank. This country report is the fifth in its series and features Malaysia’s ongoing initiatives and prospects in transforming into a high income economy and the contribution of Islamic finance in this endeavour. Islamic finance in Malaysia has undergone three decades of progress and its current state of development is the reflection of the collaborative effort between the industry and the government. While Malaysia has achieved a number of successes, a lot needs to be done still. Islamic finance needs to advance from domestic-centric growth and expand beyond our borders. The next phase of achievement would very likely hinges on our ability to collaborate successfully with others and harness our capabilities to ensure that Islamic finance will progress and expand transactional activities across borders to remain competitive and dynamic.

Progressive development of Islamic finance in Malaysia

As part of the strategy to sustain balanced economic growth, Malaysia has developed Islamic finance as one of the sectors that not only adds value to the economy but offers an alternative to businesses and the public. Our approach has been holistic, yet focused on specific outcomes. The focused approach has led to the exponential growth of the industry and contributed towards the diversification of the Malaysian economy.

The future and continued progress of Islamic finance in Malaysia would very much depend on the industry resourcefulness to build and maintain an innovative, competitive and inclusive Islamic financial industry. Empirical evidence shows the importance of an enabling environment for Islamic finance to flourish, with tax incentives, business-friendly policies and initiatives, as well as an appropriate and robust regulatory and supervisory framework. It is these ingredients that enable Islamic banking assets to consistently record double-digit annual growth rate since year 2000 and now representing 25% of domestic banking assets. In terms of customer base, it is estimated that non-Muslims make up over 50 percent of the customer base of Islamic banks in Malaysia. Growth numbers are also most evident for the Islamic capital market, with the sukuk market commanding a 57 percent market share and attracting global issuers and investors. From 2006 to end-2014, foreign issuers have issued sukuk amounting to an estimated RM28 billion in various currencies – US dollar, Yen, Renminbi and Singapore dollar – in the Malaysian marketplace. These indications show that businesses are seeing the economic and business merit of Shariah-compliant products and services and that its appeal extend beyond the traditional captive market. However, growth of the magnitude that Islamic finance experienced over the last decade would increasingly become more difficult if the industry does not continue to be nimble and agile in its approach.

Innovation is therefore a key priority for Islamic finance players to keep expanding and gain market share. As indicated by the results of the retail consumer banking and insurance survey in the country report, the demand for Islamic banking by survey respondents far exceeds that for its conventional counterpart. This should be an encouragement for Islamic banks to boost its innovativeness in meeting customers’ needs. The Islamic Financial Services Act 2013 is already paving the way for the development of Islamic banking solutions that are differentiated from conventional products by allowing funds to be mobilised either through deposits or investment accounts. This classification brings greater options for the

public and reflects an enhanced risk-sharing approach to Islamic banking. It also gives the industry additional options to create creative solutions for its customers.

Greater engagement and collaboration between industry and academia would also ensure mutually-reinforcing efforts in driving innovation through the development and implementation of new research findings and breakthroughs. Towards this end, the upcoming inaugural Islamic Finance Innovation Symposium aims to build the necessary linkage for a stronger partnership between industry and academia, of which may be of interest to IRTI. The symposium seeks to promote applied research that would spark industry innovation and act as a testbed for breakthrough ideas. Another designed takeaway from the symposium is the creation of a network for more effective business matching between the industry and academia to explore and implement specific innovative ideas. As Islamic finance has gained a strong foundation, competitive pressure would demand us to further strategise and refine the offerings of Islamic finance to ensure that the products and services needed by the customers are met and deliver the unique value propositions of Islamic finance.

As we look ahead, future Islamic banking growth will be very much driven by the industry's ability to continuously tap the opportunities to finance the activities of the real economy. Judging by the data to date there is positive indication that we are on track to meet the 40 percent target of total financing by the year 2020. Furthermore, our continuous efforts to initiate cross-border dialogues and interactions between regulators and industry, as well as between regulators and international bodies would further expand cross-border activities given a steady and strong regulatory and supervisory framework already put in place.

The launch of The Islamic Finance Country Report for Malaysia 2015 is a much welcomed initiative. The report aims to provide insights to our stakeholders, namely investors, analysts and the business community on the current state and future potential of the Islamic financial sector in Malaysia. In documenting our journey, the report also seeks to present the lessons learned. Its in-depth information, featuring Islamic banking, takaful, Islamic capital market and education; and independent due diligence position the report as a potential beacon for interested investors.

While we hope that the strong value propositions of Islamic finance in Malaysia are self-evident, today's global markets would require accurate, timely and objective information that would enhance the confidence of businesses to use the services offered by this sector.

The publication of the five Islamic finance country reports by IRTI would certainly add greater depth to the wealth of information available for the global community. In highlighting the Islamic finance prospects and opportunities across regions, it is my hope that trade and business linkages would further expand in the future.

I would like to highlight a specific issue in my remarks today. The need to elevate Islamic finance to another notch; intensifying cross-border linkages among jurisdictions that practise and promote Shariah compliant financial services. An ambitious undertaking; but a necessary initiative that I thought would spearhead the next exponential growth of the industry. There are many prerequisites, but I would like to touch on four of them. Firstly, the global supply of a wide range of high-quality, competitive and innovative Islamic financial products and services that meet the requirements of international businesses. These include environmentally friendly and ethical product offerings. While international transactions are on the rise, Islamic finance players also need to introduce mutually acceptable and comprehensive Shariah compliant financial solutions that can serve differentiated market needs. The availability of diversified offerings can be tailored to the financial needs on a regional scale and serves as an important stimulus for expanding cross-border investments.

Secondly, the need to have diverse and dynamic intermediaries and market participants including auxiliary service providers with a global focus. As the phase of globalisation expands, industry players from various sectors including Islamic banking, takaful and capital market including service providers need to further widen their outreach internationally in

capitalising market opportunities. Towards meeting this prerequisite, businesses should forge partnership and strategic alliance to penetrate markets.

Also of importance is the offering of multidisciplinary practices under one roof. For instance a consortium of service providers from legal and accounting disciplines with global linkages that enable seamless offering of clients' services. To do so, a culture of knowledge sharing across borders and greater collaboration between the industry, regulators and the academia; including Shariah scholars need to be intensified to provide the linkages for effective knowledge building and informational flow.

Thirdly, the need for business enablers, particularly in the areas of legislation, taxation and regulation that facilitate effective linkages and connections between global financial markets. The new global landscape of growing cross-border financial flows between regions that have national and cultural differences also underscores the need for enhanced recognition and understanding of practices in the different jurisdictions. This imperative translates into high demands on the use of standardised documents and agreements among Shariah compliant financial market players. Standardised documents and agreements increase market efficiency, transparency and uniformity, as well as reduce the cost of transactions as we strive towards seamless global interlinkages.

The fourth prerequisite is the catalytic role of Shariah scholars in expanding cross-border Islamic financial transactions. Given the prominence of Shariah in the industry's advancement, greater internationalisation will require the capacity and capability of Shariah scholars in offering practical solutions to Shariah issues faced by various global participants. Equally important is the efficiency and agility of Shariah scholars in responding to these matters. This calls for continuous discussions and active dialogues involving scholars across the globe. Of importance is also the need for mutual respect and common understanding within the international Shariah fraternity to enable productive and effective deliberations that will facilitate cross-border businesses.

Many can indeed benefit from learning and leveraging on these country reports. To better disseminate the information, an idea is for the IDB Regional Office here in Kuala Lumpur to act as a focal point for member countries seeking further information or clarification on the reports. As a measure to further develop Islamic finance, the Regional Office can also expand its scope to include capacity building programmes for member countries. An example is a structured programme with the opportunities for other countries to have a one-to-one engagement with the countries featured in the reports. In this spirit, IRTI, can explore the opportunity through the Regional Office to jointly collaborate with the International Shari'ah Research Academy for Islamic Finance (ISRA), Islamic Banking and Finance Institute Malaysia (IBFIM) and International Centre for Education in Islamic Finance (INCEIF) for greater synergy in international research and training, as well as capacity building.

In concluding, I wish to congratulate the IRTI team, that has worked diligently with the Council of Islamic Banks and Financial Institutions (CIBAFI) and Thomson-Reuters in producing this report. It is my hope that there is further continuity in developing such country references that can showcase the offerings of Islamic finance to the global community. With this, more jurisdictions can contribute towards advancing Islamic finance as an alternative financial system that adds diversity and vibrancy to the economy.

Thank you.