

Luis M Linde: Islamic finance – growing importance and regulatory challenge

Welcoming remarks by Mr Luis M Linde, Governor of the Bank of Spain, at the European Forum on Islamic Finance, organized by the Islamic Financial Services Board (Madrid), Madrid, 24 May 2016.

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Mr. Jaseem Ahmed, Secretary-General of the Islamic Financial Services Board (IFSB); Mr. Guillermo de la Dehesa, Chairman of the International Advisory Board of IE Business School; colleagues, ladies and gentlemen:

It is a pleasure for me to welcome you all to the European Forum on Islamic Finance. This is the fifth European Forum since 2005, after the previous fora in Luxembourg, Germany, France and Italy.

Following the tradition established by other European central banks, we are glad to support this event, organised by the IFSB. I would also like to thank the IE Business School for their hospitality in hosting the Forum in Madrid today.

The purpose of this European Forum is to gain a better grasp of the specifics of Islamic Finance and its development, which has been particularly noticeable in the last decade. In this respect, I would like to stress two relevant aspects of Islamic Finance in my opening remarks: FIRST, its growing importance in international finance; and SECOND, the ongoing regulatory efforts to facilitate its insertion in international markets.

The growing importance of Islamic finance

Indeed, Islamic Finance has grown most significantly in the last decade, posting double-digit rates since 2007, at close to 20%, compared with growth of 4% in the “conventional” financial sector. It has now reached a volume of US\$ 2 trillion, which is a very significant figure that represents around 1% of total global bank assets.

The surge of Islamic Finance is apparent both in Islamic countries and also, in European markets, with the establishment of Islamic banks and the development of the Sukuk market for private and official issuers under some European jurisdictions.

The prospects for Islamic finance are also positive, given the extensive scope for the financial inclusion of a population in a number of countries, with very low rates of bank access and usage.

The regulatory challenge of Islamic finance

The further development of Islamic finance will nonetheless depend on implementing the necessary financial reforms to ensure its integration into the wider financial system. Here, I think that the challenges are twofold:

FIRST, in Islamic jurisdictions the challenge is to continue developing the architecture of Islamic finance in areas such as payment systems and supervisory and resolution regimes. In particular, it would seem vital to advance towards the standardisation of Islamic finance regulation, breaking the existing jurisdictional heterogeneity, in order to take advantage of a wider international market.

The SECOND challenge refers to the integration of Islamic finance into the wider financial system. In this area, Islamic finance instruments will have to comply with conventional or general financial regulation, while maintaining their specificities. In particular, the contract-based nature of Islamic finance normally linked to an underlying asset poses challenges in areas such as risk weight analysis and the fiscal treatment of Islamic-type instruments.

Financial instruments have to be carefully calibrated to take due account of the risks linked to the underlying asset and its liquidity. In taxation, there are problems of double or multiple taxation and equality of treatment with interest-based instruments that also need to be addressed. Several European countries are adapting their legislation in this respect.

In addressing these regulatory challenges, the IFSB is playing a very important role by providing a forum for coordination and dissemination of better international practices. It is also contributing to the integration of Islamic finance into the general framework of conventional finance regulation, as established by international bodies, such as the FSB itself and the Basel Committee on Banking Supervision.

In parallel, other institutions such as the G20, the IMF and the World Bank are stepping up their efforts to further the analysis of Islamic finance and to identify the necessary reforms to its insertion in the international financial system.

Many of these issues will be dealt with in the different sessions of today's Forum. The agenda includes four technical sessions on regulatory aspects and the specific challenges regarding Sukuk markets, equity-based financing and financial inclusion. We have a diverse audience with well-known experts on Islamic finance and market participants who, I am sure, will provide us with a fruitful encounter.

Let me thank the IE again for hosting the event and the IFSB and Mr. Jaseem Ahmed for bringing this initiative to Madrid.

I wish you all a very successful Forum.