

GOVERNOR'S SPEECH



Governor	: Mr. Tariq Bajwa
Title	: Governor SBP's Address to the Launching Ceremony of AAOIFI Shariah Standards – Urdu Version
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- Shaikh Ebrahim Bin Khalifa Al Khalifa, Chairman, Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI)
- Mufti Taqi Usmani, Chairman Shariah Board, AAOIFI
- Distinguished speakers, ladies and gentlemen

Assalam-o-Alaikum and Good Morning!

- I feel honored to be here on this important occasion of launch of Urdu version of AAOIFI's Shariah Standards. We are all aware that national language is an important ingredient of any culture and most effective mode of communication in a country. With this in perspective, translation of global standards into our national language is an important milestone, as it would remove language barriers to understand Shariah Standards. I believe this Urdu version of the Shariah Standards will be instrumental in improving awareness about Islamic finance especially amongst the Shariah scholars, academia and practitioners of Islamic finance. The scholars and all other experts involved in this project deserve great appreciation for their commendable role.

As we are all aware, Islamic Finance Industry is relatively new to the Global Financial Landscape. Events like these are important not only for dissemination and awareness but also reinforce the emerging significance of fast growing Islamic Finance.

Ladies & Gentlemen!

- Islamic banking started initially as a niche market for the faith sensitive clientele and is now increasingly becoming an integral component of global financial system. Islamic finance industry has grown at a fast pace. The development of Islamic banking industry especially beyond Muslim jurisdictions is a recognition of its viability as a competitive alternate to the conventional banking. According to Financial Stability Report 2018 issued by Islamic Financial Services Board (IFSB), its asset base has grown by 8.3 percent to surpass US\$ 2 trillion mark. With expanding scope and size of Islamic finance, and emerging global challenges, it is gaining importance from financial stability perspective. Inherent strengths of being asset backed and prohibition on speculative activities in Islamic finance lead to better resilience of Islamic banking institutions against excessive risks. However, these strengths alone may not be sufficient to immunize the Islamic finance from risks associated with deficiencies in due diligence, inadequate buffers, lack of transparency and weak risk management practices. The well thought out international standards issued by the global standard setting bodies like AAOIFI and IFSB facilitate in managing the challenges facing the Islamic finance and harmonizing the industry practices.
- Against the backdrop of growth of Islamic banking globally, our domestic industry is also demonstrating quite impressive headway. The industry has posted a healthy annual growth of over 20 percent during the last five years. The market share of Islamic banking industry stands at 13.6 percent in terms of banking assets and 14.7 percent in total deposits. Islamic banking industry has expanded its network to over 2700 branches in 111 districts across the country.
- Given the potential of Islamic finance to support broad based economic growth and our constitutional obligation to make available Islamic financial services in the country, Islamic banking has remained a priority area for State Bank of Pakistan (SBP).
- I feel pride in sharing that the sound foundations of legal and regulatory environment laid down by the State Bank of Pakistan has played a key role in sustained high growth of Islamic banking in the country. Our Shariah compliance environment is considered amongst

the best in the world. It encompasses a comprehensive Shariah Governance framework consisting of establishment of Shariah Board, Shariah compliance department and Shariah internal audit in Islamic banking institutions supported with Shariah external audits and SBP regular inspections. Let me also apprise you that SBP regularly reviews the regulatory framework to make sure that it is aligned with international standards and best practices and at the same time caters to the evolving needs of the industry.

- State Bank of Pakistan also believes that growth and development of other elements of Islamic finance ecosystem i.e. capital markets, mutual funds and takaful, is essential not only for Islamic banking industry but also for the overall growth and development of the country. In this regard, SBP regularly collaborates with Securities and Exchange Commission of Pakistan (SECP), the capital market's regulator, to promote Islamic finance. We appreciate and acknowledge key steps taken by SECP in last few years including establishment of Islamic Finance Department, introduction of all share Islamic Index, issuance of Takaful rules and Sukuk guidelines. We believe that these measures shall facilitate the diversity and outreach of the Islamic finance.

Ladies & Gentlemen!

- At this stage, let me highlight few potential risks and challenges that Islamic banking industry need to address for its sustainability and stability. Effective liquidity management has been the key challenge of Islamic banking industry. This issue has gained more prominence owing to factors like dearth of Shariah compliant investment opportunities, limited availability of Shariah compliant money market instruments and absence of Shariah compliant SBP standing facility. In Pakistan, sovereign sukuk being issued since 2008 provide the key liquidity management avenue to the domestic industry, however, demand for such instruments far surpasses their supply. Being cognizant of this challenge, SBP, in consultation with industry is working to develop alternate solutions for liquidity management for Islamic banking industry.
- The inherent advantage of Islamic financial industry to fund projects on equity participation and profit sharing basis enables it to cater to the huge, unmet demands of underserved sectors such as agriculture and SMEs. However, like conventional industry, Islamic banks are also not effectively serving these sectors. KAP (Knowledge, Attitude and Practices of

Islamic Banking in Pakistan) survey based study of SBP, also indicates these areas as potential growth avenues for Islamic banking industry. SBP is persuading the industry to capitalize on its innate strengths to cater to the needs of these underserved sectors.

- Housing finance is another attractive avenue for Islamic banks. Increased focus of incumbent government on this sector provides Islamic Banks an opportunity to diversify their asset portfolio. I am confident that present conducive environment provides opportunity to Islamic banking industry to tap potential in low income housing through Diminishing Musharaka instruments. This would also pave the way towards the ultimate objective of Islamic finance. i.e. Maqasid-e- Shariah.
- Another major issue restraining Islamic banking from realizing its true potential is lack of qualified and trained Islamic bankers. To tackle this issue, SBP is not only offering training courses on its own and through its training subsidiary-National Institute of Banking and Finance (NIBAF), but is also supporting industry in such initiatives. We have also collaborated and sponsored three Centers of Excellence in Islamic Finance Education (CEIFEs) at well renowned educational institutions- IBA Karachi, LUMS Lahore, and IM Sciences Peshawar. These institutions are fully operational and they are providing regular supply of trained human resource as well as conducting training programs for enhancing capacity of the existing human resource of the industry.
- Another important challenge for the Islamic finance industry, as identified in the KAP study, is lack of awareness among masses on demand side. As such a robust awareness campaign about Islamic banking is necessary for promoting Islamic banking. SBP is focusing on addressing this challenge through multipronged strategy; it is conducting various mass awareness programs and focused group discussions all over the country and supporting the industry and other related stakeholders for such initiatives. However, this is one area in which Islamic banks have also to play a far more proactive role.

Ladies & Gentlemen!

- As I mentioned earlier, standardization in Islamic finance is essential for addressing various issues facing the Islamic finance in addition to promote disclosure, transparency and integration into global financial system. I think the rapid growth of Islamic banking and

finance requires further strengthening of its financial infrastructure. This will augment the ongoing efforts to bring the infrastructure of Islamic financial industry up to the international standards. The alignment of Islamic finance industry with the global best practices would not only help supervisors in their tasks but will also foster the integration of Islamic financial institutions into the international financial community.

- I would like to highlight here the commendable role AAOIFI has played in development and promotion of Shariah, accounting and governance standards to facilitate the growth of Islamic financial services industry. AAOIFI has also been instrumental in enhancing awareness of Islamic banking and finance globally through knowledge sharing and organizing capacity building programs, workshops, conferences, and seminars. Considering the constant changing dynamics in financial sphere, AAOIFI also reviews and updates its standards to keep them relevant. AAOIFI's enhanced coordination with relevant stakeholders and increased collaborative efforts help Islamic financial services industry to grow on sound footings.
- The AAOIFI role in capacity building through offering Shariah based certifications in the area of Auditing, Accounting and advisory services is laudable. Such certifications provide the much needed qualified resources for effective implementation of the Shariah standards.
- SBP has long standing association with AAOIFI. As a member of the AAOIFI's Board of Trustee, State Bank contributes in the overall oversight and supervision of its operations. Our officials participate as both speakers and participants in different knowledge sharing and capacity building initiatives. So far SBP has adopted 6 of the AAOIFI's standards while another 8 to 10 standards are in the final stages of implementation. Besides, SBP has advised the banks to refer the AAOIFI's standards for guidance in different areas of Islamic finance.
- Given the commitment and concerted efforts of all stakeholders, I am optimistic that Islamic banking and finance is likely to maintain its positive growth trajectory. The growth of Islamic finance on its distinct strengths would bring more stability to the financial system, improve equitable distribution of economic gains, and support overall economic development. I believe events and steps like these are vital steps towards achieving this goal; hence, we should not stop here and but continue to work towards establishing an ethical financial system.

- At the end, I would like to reiterate that State Bank of Pakistan will continue to extend its full cooperation and play due role for achieving our shared vision of a vibrant and sustainable Islamic banking sector in Pakistan.

- Thank you!
