Abdul Rasheed Ghaffour: Keynote address - Third Fitch Ratings Islamic Finance Symposium 2024

Keynote address by Mr Abdul Rasheed Ghaffour, Governor of the Central Bank of Malaysia (Bank Negara Malaysia), at the Third Fitch Ratings Islamic Finance Symposium 2024, organised by Fitch Ratings, Kuala Lumpur, 6 March 2024.

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It is my great pleasure to be part of this Symposium, and my thanks to Fitch Ratings for the invitation. This gathering offers an excellent platform for us to continue important conversations about the growth prospects for Islamic finance against the current environment of tight global financial conditions.

Growth prospects for the global Islamic financial system

Global Islamic finance assets are estimated to have reached USD4.5 trillion in 2022 and are projected to reach USD6.7 trillion in 2027.[1] The industry has grown more than twofold compared to a decade ago. Almost 60 countries now have Islamic finance regulations,[2] with several new markets in Asia and Africa exploring to introduce Islamic financial services.

The prospect for expansion of the global Islamic economy remains promising. Furthermore, the intrinsic values of Shariah that promote a balanced distribution of wealth and value of ihsan (the act of doing good and performing one's duty in the best possible way) are imperatives to achieve inclusive growth. Strong demand for halal industry and impact-driven finance, offer significant opportunities for the industry to play a bigger role in intermediating investments across markets. Deepening the development of Islamic financial markets will be an integral component to this aspiration. There are three important priorities that will unlock a stronger role of Islamic finance in supporting global financial intermediation:

a. First, to strengthen the vibrancy and depth of Islamic financial markets. This includes ensuring regulatory clarity and industry coherence, as well as instrument diversification are in place;

b. Second, to advocate for system-wide alignment to value-based finance and universal principles of Shariah for sustainability across all sectors. And this needs to be supported by clear demonstration of measurable impact; and

c. Third, is to unlock impactful innovation via diverse Shariah contract structures including deployment of blended finance, supported by an enabling ecosystem and circle of expertise.

Islamic finance a driving force in shaping Malaysia's sustainable economic growth

These priorities are also very much aligned with Malaysia's Financial Sector Blueprint.

In strengthening Malaysia's global position as an Islamic finance gateway, efforts are intensified in strengthening the vibrancy of the Islamic financial markets via instrument diversification and providing regulatory clarity. These aim to widen the range and volume of Shariah-compliant investable assets including to international investors. Over the past half-decade, Malaysia's sukuk market has grown about USD70 billion (RM332.3 billion) or 35% to an outstanding amount of USD267.5 billion (RM1.27 trillion). Foreign participation in Malaysia's sukuk market now stands at total investments of USD12.6 billion (RM59.6 billion).[3] Building from this progress, the Islamic Financial Market Subcommittee (IFMC) set-up by the Central Bank has also been tasked to explore strategies to enhance foreign investors participation in domestic sukuk issuances. We look forward to welcoming increasing participation from around the globe in the times ahead. One key progress of the IFMC is in the area of hedging. This has led to a Shariah Advisory Council ruling on the permissibility of anticipatory hedging, subject to specified conditions. This is aimed at further developing the Islamic derivatives market, ensuring that it aligns with both Shariah principles and prudent risk management practices. We are also establishing a stronger collaboration with the GCC and Asian countries to advance mutual development in Islamic finance. These efforts will strengthen Malaysia's position to be the Islamic finance gateway to the GCC and OIC markets.

Global investors stand to benefit from investing in Malaysia and participating in sustainable economic prospects

This brings me to Malaysia's broader growth prospects, and the investment opportunities it presents in the area of sustainability.

The Malaysian economy is projected to grow at 4-5% in 2024, supported by robust domestic demand and an improvement in the external sector. The improving global economy together with the tech upcycle are benefitting our exports, especially since Malaysia is a dominant player in the global semiconductor industry.

In 2023 alone, a total of about USD70 billion (RM329 billion) investment was approved with foreign direct investment accounting for 57%. Almost 74% of the projects approved between 2021 - 2023 have also been realised.[4] Last year, Malaysia's National Energy Transition Roadmap (NETR) and the New Industrial Masterplan (NIMP) were introduced, solidifying further our focus on the sustainability agenda and our commitment to bolster the nation's manufacturing sector. These will place Malaysia on a solid ground for its sustainable growth path. The NETR detailed ten flagship catalytic projects and initiatives to transition the energy sector. Given its scale, the implementation of these two plans is estimated to require both public and private financing of about USD210 billion (over RM1 trillion) by 2050. Part of this financing will be met through Islamic finance product offerings including Shariah-compliant ESG in the Malaysian sukuk market. More broadly, the ASEAN region has significant financing needs for the sustainability agenda. New investors to the region can use Malaysia as a base to meet the financing demands of the region, given our comprehensive Islamic finance ecosystem.

A key strength of Malaysia is our external sector resilience. This is contributed by a current account surplus, a manageable level of external debt, a net external asset position and an adequate level of international reserves. This has enabled Malaysia to weather the volatile global financial conditions from a position of strength, and has ensured the domestic financial markets continue to remain orderly.

The Government is committed to ensure fiscal sustainability through several fiscal reform initiatives. This includes The Public Finance and Fiscal Responsibility Act (FRA) and the Medium Term Fiscal Framework (MTFF) which will support the paring down of the fiscal deficit to between -3.0% and -3.5% of GDP by 2025. This will be supported by both revenue enhancements and expenditure optimisation, including broadening the tax base.

Notwithstanding this, the Malaysian ringgit has been under pressure since 2022, largely influenced by the aggressive policy rate adjustments by the US Federal Reserve. This phenomenon is not specific to Malaysia but reflects broader currency market dynamics. Given our positive growth prospects, the current ringgit level is undervalued. This is unwarranted, as the ringgit is also supported by sustained investor confidence, evidenced by the stable long-term government bond holdings by non-residents at around 22%, and recent foreign inflows into domestic equities.

We are highly resolved to ensure that the ringgit remains stable. The Government of Malaysia and Bank Negara Malaysia are undertaking coordinated actions to further increase flows into the foreign exchange market on a sustained basis. Specifically, we have elevated our engagements with our Government-Linked Companies (GLCs) and Government-Linked Investment Companies (GLICs) to encourage more consistent repatriation and conversion of their foreign investment income. We are also stepping up our engagements with international investors, such as yourselves, to showcase the positive prospects of Malaysia and that Malaysia remains highly attractive for investment and business.

Thus, with the current ringgit undervaluation and ongoing and forthcoming investment opportunities, global investors stand to reap the benefits from participating in Malaysia's growth prospects.

Ladies and gentlemen,
Malaysia looks forward to collaborating with other markets and international stakeholders, as the transition to a sustainable economy requires a global collective act. I trust this Islamic Finance Symposium will provide us invaluable insights and outlooks of the market that will undoubtedly contribute to our roles within our respective domain. In May this year, Malaysia will also be hosting a global forum focusing on applications of Islamic economics and finance in shaping a more resilient, sustainable and equitable global economy. Further details will be announced soon and all are welcome to join. Continued intellectual discourses on pertinent issues and forward-looking ideas, will InsyaAllah, pave us for continuous improvement. On this note, I wish you all a productive discourse ahead.

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[1] Source: ICD-LSEG Islamic Finance Development Report 2023.

[2] Refers to the number of countries with at least one type of Islamic finance regulation. Source: ICD-LSEG Islamic Finance Development Report 2023.

[3] Source: BNM FAST and Securities Commission Malaysia, data as of end December 2023.

[4] Source: MIDA, February 2024.