Where is Islamic Finance Going? Ethical Investment Strategies

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Opportunity often arises out of chaos. That has never been more true than it is today in the international financial markets. However, creating Middle East investor confidence in American-based projects will depend on a U.S. business's ability to establish and retain a reciprocal level of trust built on transparency, collaboration, harmonious cross-cultural contracts and clear systems of operational control.

56 EXCLUSIVE INTERVIEW WITH MR. DAVID FIDDLE (CFO, UNICORN INVESTMENT BANK)

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60 THE WORLD ISLAMIC BANKING CONFERENCE 2008

Rajesh Nair explores the potential for a breakthrough event behind the suspicious event in the Islamic finance industry. One of the most important events at the WIBC was the launch of the 2008/2009 McKinsey competitiveness report in Islamic finance, which was eagerly discussed in an interactive session which took off the event as a whole.

66 ISLAMIC INVESTMENTS 2008 GLOBAL SURVEY

Investment globally are being made a safe haven from subprime debt, emerging equities, out of control inflation and central bank meddling, but not if you’re talking to Islamic investors. Produced by terrains, you’ll find an inclusive detailed overview of Islamic Investments for 2008.
“Islamic banking and finance is underdeveloped in India, due largely to political sensitivities, but current global conditions may change this landscape.”

Douglas Clark Johnson
(CEO & Chief Investment Strategist for Colyn Financial)

“Experts at the Treasury Department have been learning about the important features of Islamic banking.”

Robert Kimmitt
(The US Deputy Secretary of the Treasury)

“With many new projects coming into the pipeline, and reduced competition from conventional finance, now could be the perfect time for Middle Eastern investors to consider Canadian infrastructure investments structured as Shariah-compliant PPFs.”

Guy Currie
(Partner & Head of Islamic Finance, Gowling WLG (Canada) LLP)

“The Shariah indices have generally outperformed their conventional counterparts in the year to June 2008. This is another little-known secret and a major competitive advantage for Islamic investors.”

Quazi Reza
(Chairman of the BLN Umbrella Fund & Founder, Westminster Asset Management)

“Almost every discussion of financial affairs these days needs to have some mention of the sub-prime crisis and the accompanying credit crunch, and a discussion of Islamic finance is no different. Could the sub-prime types of problems occur in the Islamic finance space?”

Ismail Salih
(Senior Finance Partner, King & Spalding’s New York & Dubai offices)

“Many GCC investors will increasingly only invest in Islamic instruments, so if you do Sukuk, the advantage is that you have to whole world to sell to, as conventional banks buy Sukuk, as well as Islamic banks, whereas Islamic buyers don’t buy bonds.”

David Pace
(CFO, Unicorn Investment Bank)

“Opportunity often rises out of chaos. That has never been more true than it is today in the international financial markets. However, creating Middle East investor confidence in American-based projects will depend on U.S. businesses’ ability to establish and maintain a reciprocal level of trust built on transparency, collaboration, harmonized cross-cultural contracts and clear systems of operational control.”

Dr. Steven R. Weiss
(President, Zurich Global Consulting Group)

“Sensible risk management is built into Shariah-compliant financial structures, as the Islamic finance institution pays special attention to both the asset being financed and the individual receiving the funds.”

Dr. Karrn Hunt-Ahmed
(Assistant Professor of Finance & Management, DePaul University)
What Does Islamic Finance Want to Be When It Grows Up?

By Karen Hunt-Almed

During his opening remarks at the Islamic Finance World Summit in New York last October, Mike McMillen challenged us to consider how our industry will move forward and develop in today’s market and in the future. He urged us to engage in constructive self-criticism and to assess the industry’s strengths and opportunities as we face the challenges of building a world-class industry based on combining the principles of international finance and Shariah law. I would like to use this opportunity to step back and reflect on the industry as a whole and to think about how we can establish the solid authenticity of an ethical Islamic finance industry in the global marketplace.
Dr. Karen Sue Anderson is Assistant Professor of Finance and Management at DePaul University. Before receiving her PhD from the University of Chicago, she worked as an operating partner in Chicago and for J.P. Morgan Capital in Tokyo. She currently chairs the Finance and Real Estate Office at DePaul University's College of Commerce and is also on the advisory committee of DePaul's Center for Financial Services.
A 11terred and speak as various industry con-
éferences around the world, I am always
streed by how many people define the industry as
being in its "infancy" and remind about the indus-
tory's "youth" as a way to think about how to struc-
ture and market Shariah-compliant products
globally. It is helpful to think about the industry as
being an "infant" as we work out the kinks and estab-
lish a solid base of current and potential practitioners and innovative financial products.
However, although I am always happy to hear that the industry being described as "young" (it was, after all, establishe in its lifetime), I would like to posit that the industry has actually moved past its infancy stage and may now be considered an "adult.

Adolescence is a time during which a person (or an industry) must look to the future and figure out what kind of adult he or she wants to be. It is a time for consolidating the values learned from family and society and deciding which of those values to integrate into the psyche in order to formulate a meaningful and successful approach to life. In other words, an adolescent asks: "Who do I want to be when I grow up?" It is time for us as an industry to step back and reflect on who we want to be when we grow up.

During my research into the Islamic finance industry in the GCC countries and in the United States, I have had the privilege of talking to numerous industry executives. The overriding theme I have uncovered in these conversations is that of social justice, the dimension of Islamic finance that I think is most crucial to establishing the worldwide legitimacy of the industry. From its inception, the Islamic finance industry has been built on the concept of Adalat, or social justice.

The goal of Islamic finance is to maintain "bal-
dance, distributive justice and equality of opportu-
nities" amongst all people, as Sehaj Muhammad Taqi Ur Rehman has written.

However, although there is a lot of talk about social justice, there is less action as we become entranced by the big-money, internationally recognized deals. Much attention has been paid to proving that investing in Shariah-compliant prod-
ucts is a worthy and profitable investment choice. This is good. It is necessary, even, to put our industry on the worldwide map of legitimate and powerful investment alternatives in a competitive world market. We absolutely need to focus on high-profile opportunities as one way of authenti-
cating our industry.

However, it is time to authenticate our industry from another angle: that of grassroots economic development. Remembering and paying homage to the ethical principle of Adalat will not only justify the industry's legitimacy in the interna-
tional financial markets, it will provide us with the competitive advantage we need in order to prove

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Ethical Investment Strategy

Now we must ask two questions: "What have we done to position ourselves as an ethical investment vehicle?" and "What can we do to take the industry to the next level of maturity as an ethical industry?" To answer the first question, we have begun to build a strong base of ethical investment strategies. Rabih Siddiqi and his colleagues at Dow Jones introduced the first Islamic Index Screening process for stocks in 1999. Now virtually all of the major rating agencies have a compara-
ble index. Invested investors can turn to one of hundreds of funds to meet their personal Shariah-
compliant investing needs. Most, if not all, Islamic financial institutions (IFIs) collect and distribute a
daili  Business models promoting environmentally and ethically sustainable business practices fit naturally into the Islamic finance industry's com-
imment to purifying and improving upon a con-
ventional business model.

Now that the industry has established its creden-
tials both as an ethical business model and as a powerful and flourishing financial markets, it is time for us as researchers and practitioners to take a more active role in building sustainable economic development models that will benefit underserved and underbanked populations in our own communities. I am not talking about giving away money or distribution of zakat funds — although they may certainly be used for what I am proposing — but of investing in growth opportunities that will build and sustain our communities in good and bad economic times.

One way to assist communities in developing a business base is to offer microfinance opportuni-
ties for entrepreneurs. German Bahn is the lead-
ing example of this kind of program that offers
small amounts of interest-based, or conventional,
financing to entrepreneurs in less-developed com-
unities around the world. Shariah-compliant
products such as modarabah, murabaha and jumla had themselves metadically well to a consolid-ated model, and are already being used by many NGOs and non-profit organizations in the United States and around the world. There is yet reason why this kind of business model could not be used as a profit-making investment vehicle. The kind of model I envision could advance the industry’s current agenda of social justice and still provide a profit for investors.

Businesses in the industry are blessed with relatively high liquidity. In the current economic climate, it might seem inappropriate to talk about investing in relatively risky small businesses. But I argue that investing in the community—both the Muslim community and our broader community—will improve our financial model at exactly what is needed to build a better sustainable economic environment for the future. Secure business and property ownership provides stability and sustainable economic growth and can serve to illustrate a community that is vulnerable to the escalating effects of economic crises. This is not to say that Islamic financial institutions are immune to the challenges of conventional finance. The Islamic finance model is sound and viable way to mitigate the risks inherent in small businesses and thus we might avoid undesirable situations such as the subprime mortgage crisis that is deemed to be responsible for our current situation. Our investment into community development will not only make us “feel good,” but is a smart business strategy that will be an ally in our struggle to grow our industry. Let us invest wisely in our prosperity, in building an economically viable community, in all income levels, and in all communities. One of the great strengths of our industry is the clear and obvious way we pay it forward. We are not an industry that advances one group at the expense of another. Instead, we are truly the best at creating a virtuous cycle of prosperity and growth. We are great at the principles upon which our industry was built. Our current task is to determine a good look at our founding principles and decide what we want to be when we grow up. We are well on our way to being a great competitor, ethical, and competitive with conventional finance. Only then can we move toward providing justice for all and truly be able to say we are a legitimate and growing industry with a truly ethical competitive advantage.