



Fostering Stable and Inclusive Financial Systems

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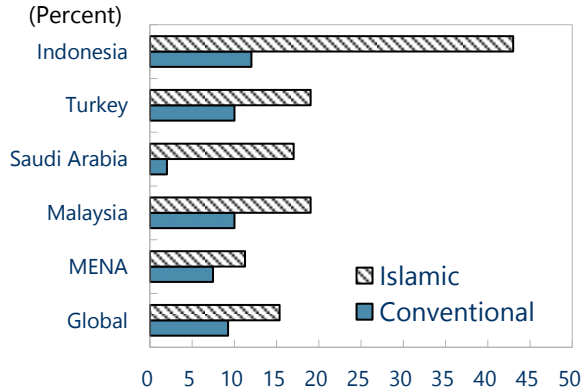
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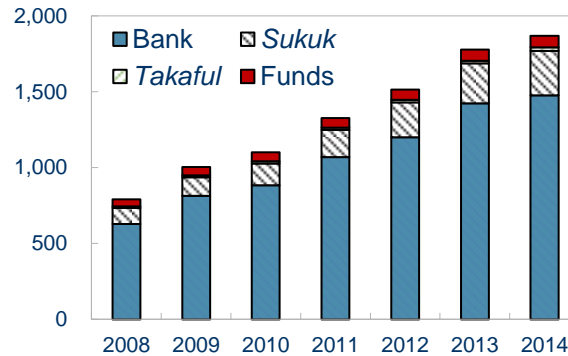
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Islamic finance appears not to have realized its full potential

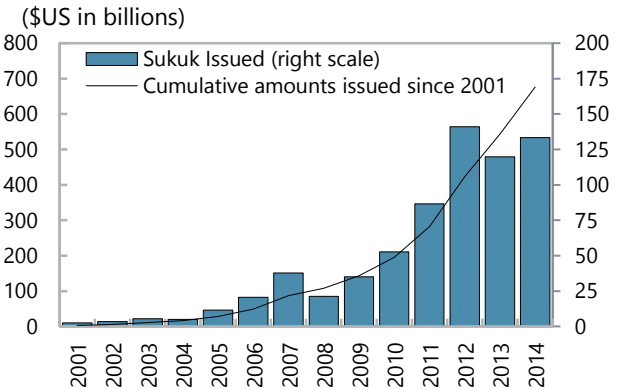
Compound Annual Growth Rate for Banking (2009-13)
(Percent)



Islamic Finance Assets (2008-14)
(\$US in billions)



Global Sukuk Issuance (2001-14)



Source: IFSB, HSBC, Kuwait Finance House Research, IMF and Zaywa.

Islamic finance has the great potential for the development of the financial sector, the SMEs sector and inclusive finance because it helps in fostering co-operation, interdependence and involving everyone in both production and investment. Notwithstanding its potential, Islamic finance appears **not** to have realized its full potential. Islamic finance industry has huge potential but a long way to go in supporting financial inclusion (i.e. challenges of depth and breadth)

Expansion of Islamic finance has the potential to enhance overall financial sector development



Reinforcing Financial Stability

- Its risk-sharing features and prohibition of speculation may pose less systemic risk than conventional finance
- Islamic financial institutions may be more resilient to some unforeseen shocks due to asset-backing for their transactions, avoidance of speculation and avoidance of excessive leverage

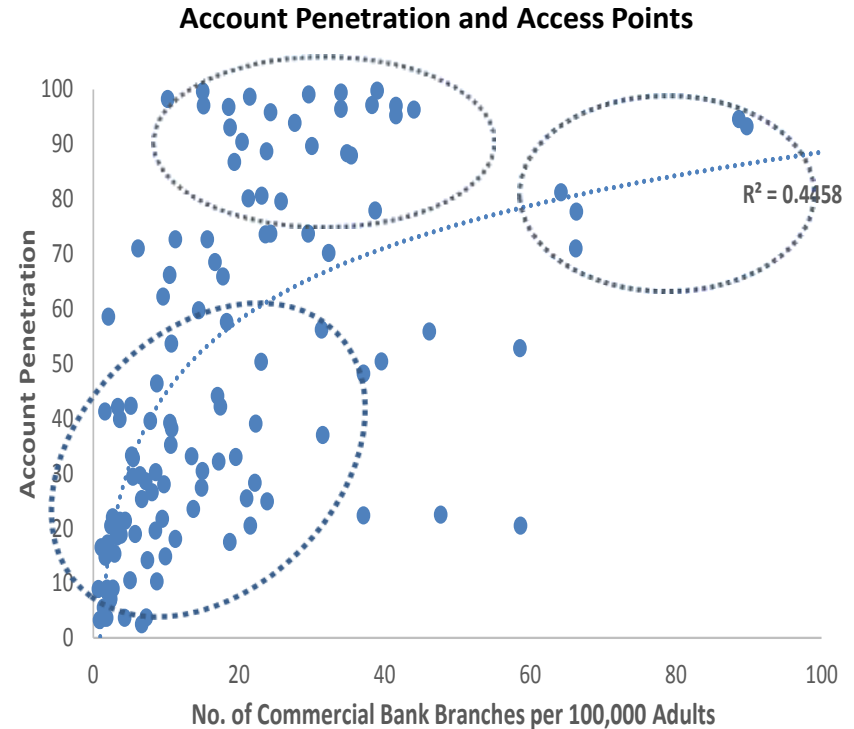
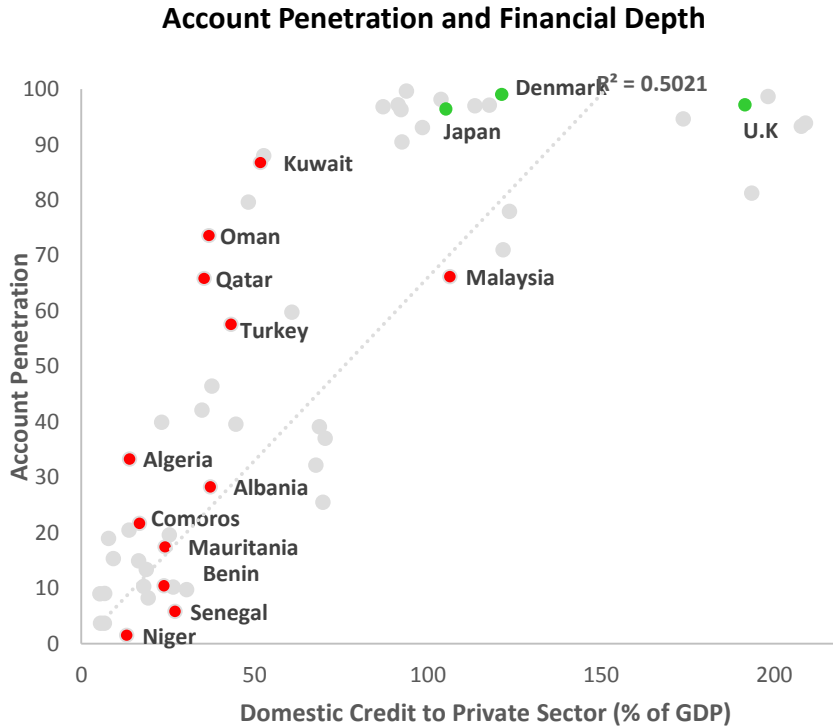
Improving Depth, Breadth and Efficiency

- Islamic finance provides alternative sources of financing for households and businesses
- Potential to provide competition to conventional financial institutions

Enhancing Financial Inclusion

- Emphasis on asset-backed financing and risk-sharing feature means that it could provide support for small and medium-sized enterprises (SME)
- Widening the range of products and services available to businesses and households
- Improving access of the underserved to financial services

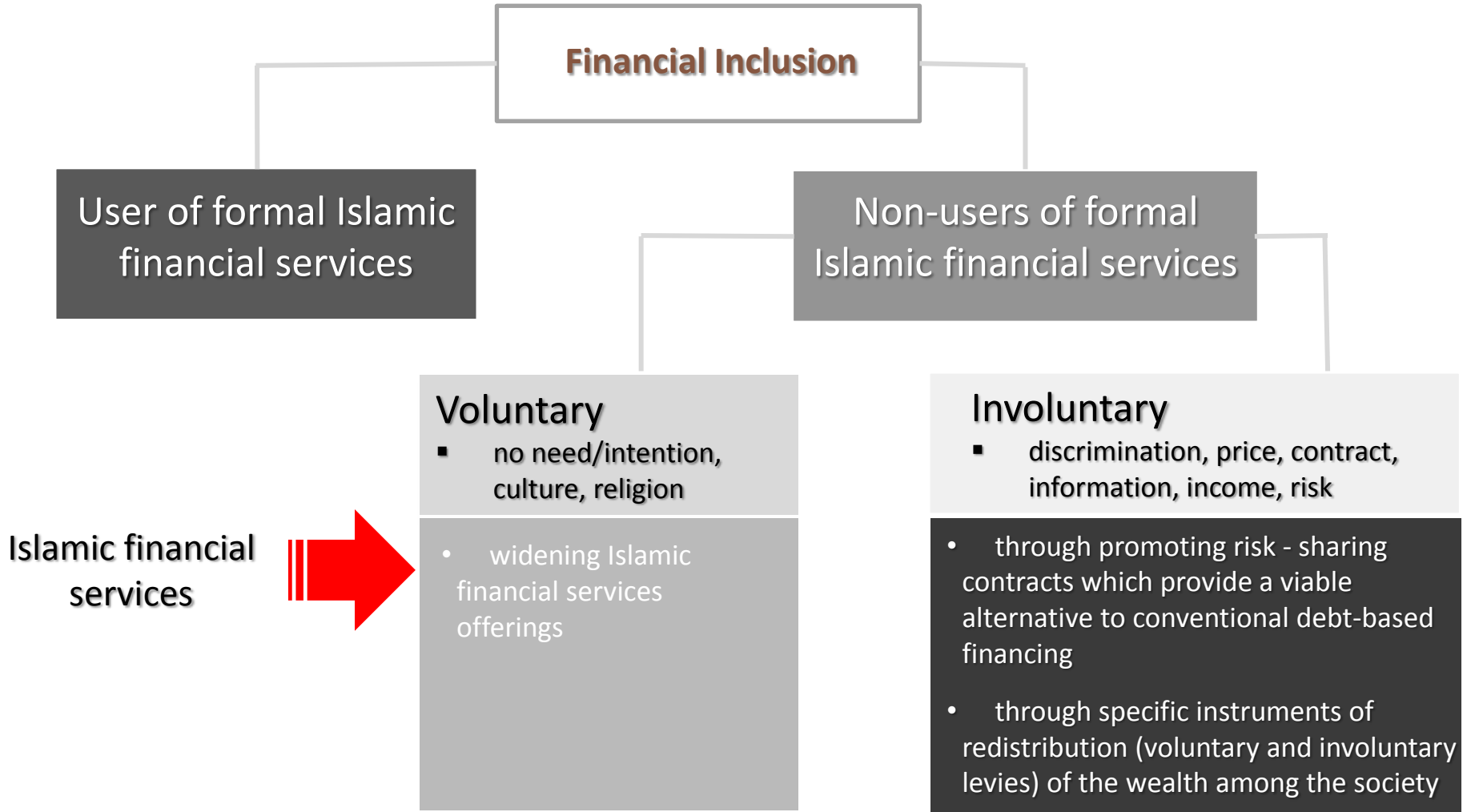
Positive correlation: financial inclusion, financial depth and access points



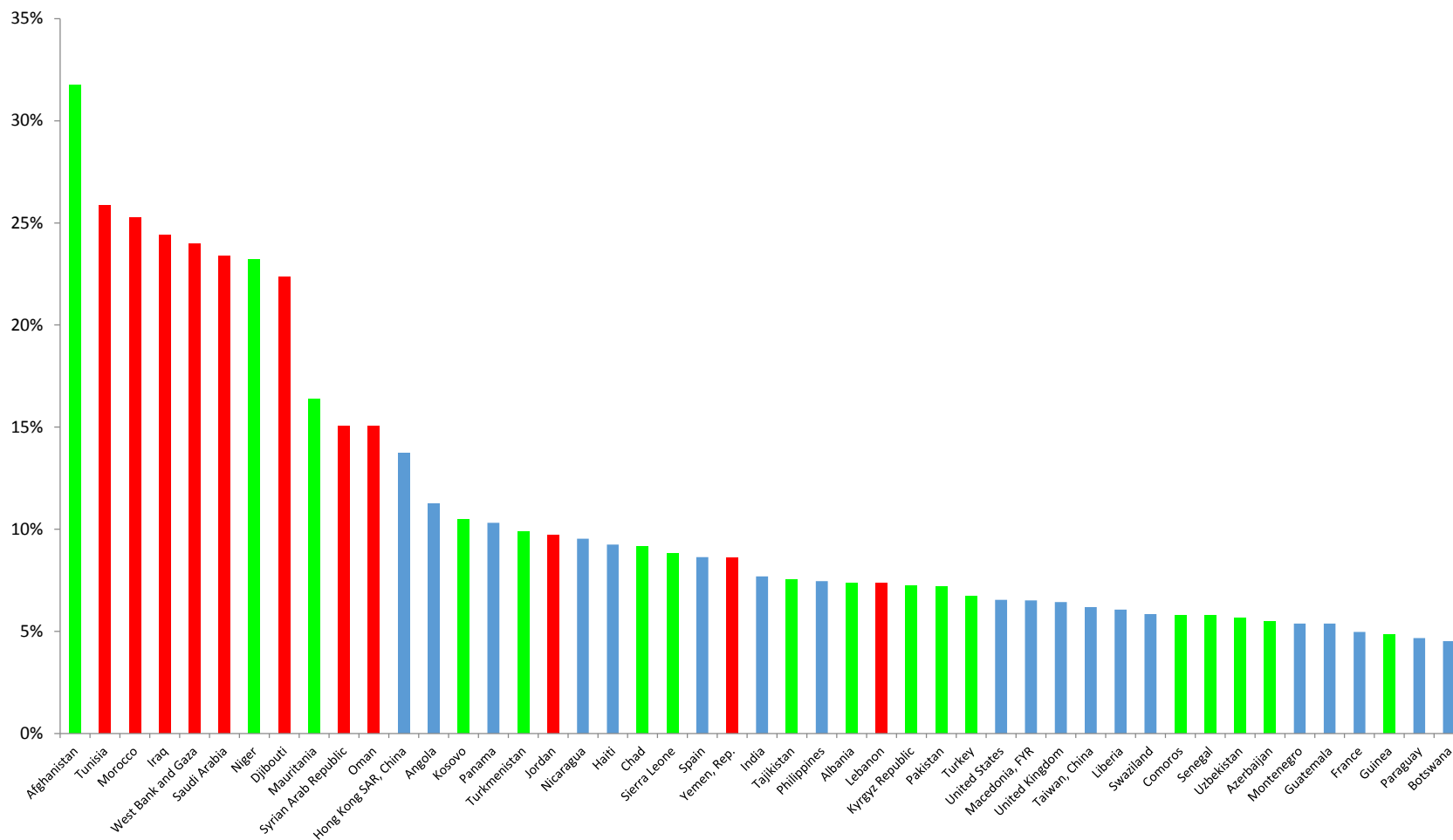
Source: Global Financial Inclusion (Global Findex) Database, World Bank

Depth of financial systems alone is not sufficient to delivering access to all. In addition, often the main barrier is the great distances that residents (rural) must travel to reach a bank branch

The channels: financial inclusion from Islamic perspectives



Although not substantial, many Muslim-headed households and enterprises are voluntarily excluded



Source: Global Financial Inclusion (Global Findex) Dataset; author's Calculation.

Public policy approaches in fostering 'risk-sharing' for inclusive financial system



PUBLIC POLICY ALTERNATIVES



Enhance the capacity of the regulatory and supervisory framework to evolve in greater alignment with the international regulatory and the supervisory standards and best practices

Develop an effective and efficient regulatory framework which provides an enabling environment to support the development of the Islamic financial services industry

Market driven approach in network and product development, fair treatment between IFIs and conventional banks

Create effective and efficient consumer protection and complementing the need for investor protection via effective risk management systems

Ensure the need for institutional soundness of the Islamic financial institutions and their enhanced ability to assess risks in the real sector

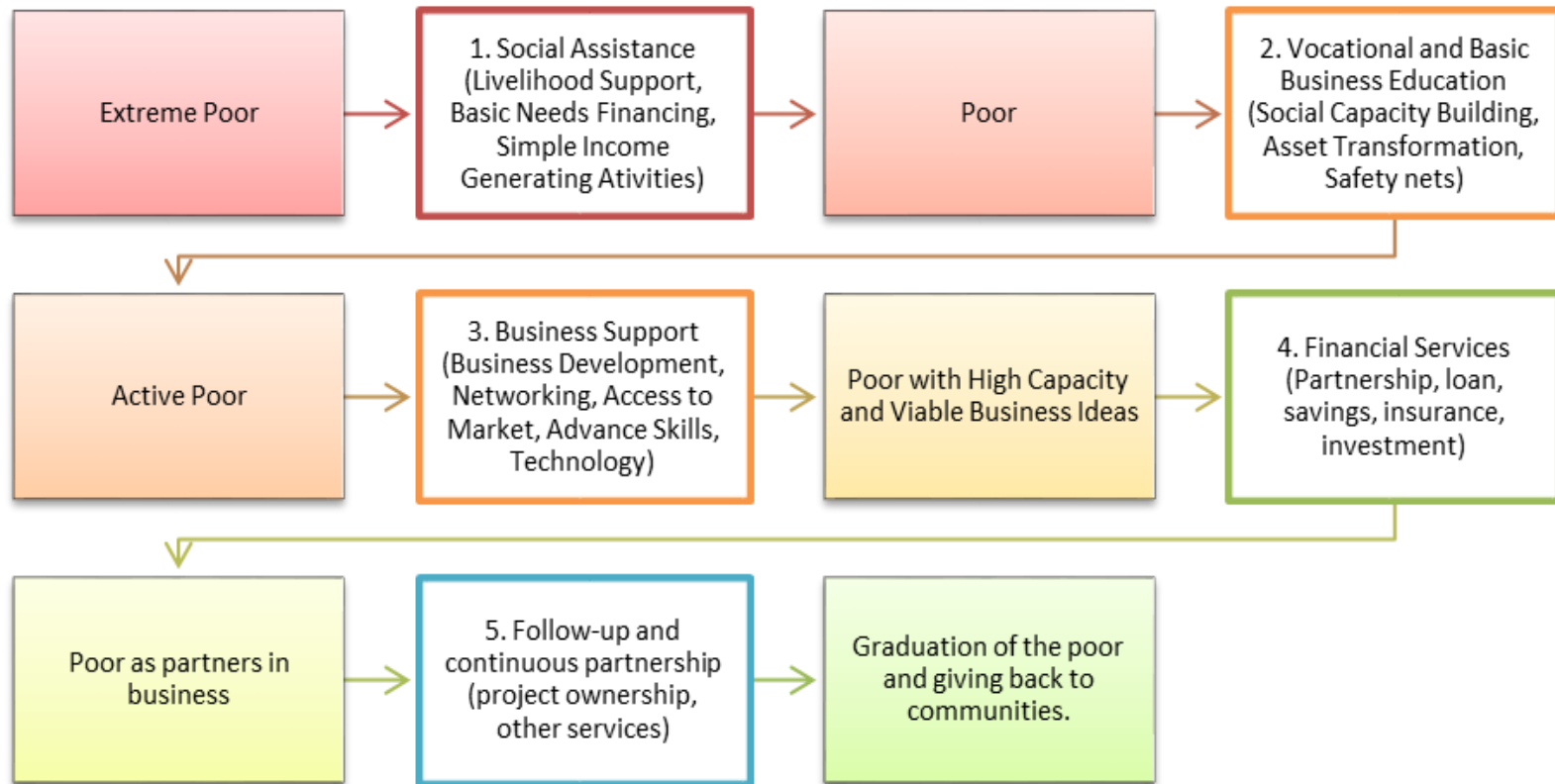
Instill investor confidence in the market, confidence on the Shari'ah compliant process and confidence that Islamic products are truly Shari'ah compliant via transparency and disclosure requirements

Gradual and sustainable development of infrastructure and regulation, applying Islamic universal values for IFIs development initiatives

Adjust the legal, regulatory and supervisory framework to accord greater clarity to the appropriate legal and regulatory treatment

'MARKET DRIVEN' APPROACH VS. 'GOVT. DRIVEN' APPROACH

Economic empowerment under inclusive Islamic finance business model



Source: IRTI Working Paper WP/1437/03

No “one size fits all” financial inclusion strategy and framework



1

- Many of the national financial inclusion strategies have common similarities but differ greatly in the level of detail, breadth of coverage, and degree of specificity,
- There are three difference approaches: (a) stand alone; (b) integrated in financial/development strategy; and (c) specific strategies for specific areas

2

- Many strategies on Islamic microfinance do not properly take into account (or create links to) the broader financial sector
- Integrating Zakah collection or subsidies can work for Islamic microfinance in certain circumstances, but subsidies are best used to build the systems

3

- Financial inclusion strategy and policy must be truly evidence based and so that progress can be effectively measured
- Diagnostics of the sector too often lack breadth and depth and neglect the financial infrastructure or the political economy

4

- None of the national financial inclusion strategy include the role of Islamic financial services
- Important for the government to recognize necessary and sufficient conditions that are needed to maximize the benefits derived from the FI strategy

Promotion


- Take the lead in promoting Inclusive Islamic Finance and 'Smart' Financing solutions including conducting Solidarity Group and Value Chain Project Group Financing


Capacity


- Take the lead in developing the capacity of MFIs keen on Islamic MFIs by providing templates for collecting data, a repository of manuals, and tools and strategies


Advocacy

- Take the lead in advocating that every financial institution should allocate a proportion of their lending portfolio to the poor as part of the efforts of contributing to inclusive finance and poverty alleviation

- 

develop a comprehensive Islamic financial inclusion operational framework beyond microfinance and facilitate transfer of best practices, knowledge and resources on financial inclusion
- 

intensify support on the effort in developing technological (i.e. mobile/digital payments) and institutional innovation (i.e. fintech) in particular to improve usage and access to Islamic financial services
- 

develop a comprehensive information/database for Islamic financial services, Islamic microfinance and solidarity-based institutions (Zakat, Awqaf etc)
- 

undertake in-depth analytical work on Islamic financial services and Islamic social finance to further understanding the issues of Islamic financial inclusion



Thank You

Some observations for Islamic financial industry

- 1
 - Cost, distance, documentations, trust and religious belief are important obstacles for financial inclusion
- 2
 - Contributions of Islamic finance have been limited to only a small segment of the population, failed to reach underserved segments
- 3
 - Islamic microfinance is small by international standards, limited coverage and lack of cost-efficient service model
- 4
 - Islamic finance industry has huge potential but a long way to go in supporting financial inclusion (i.e. challenges of depth and breadth)
- 5
 - Islamic finance can play an important role in reaching the segment of consumers who are reluctant due to religious reason