General Council for Islamic Banks and Financial Institutions

CIBAFI

المجلس العام للبنوك والمؤسسات المالية الإسلامية

Global Islamic Bankers' Survey 2019

Sustainability, Growth Drivers, and the Regulatory Challenge

Executive Summary

May 2019

STATEMENT BY THE SECRETARY GENERAL

Welcome to the fourth annual CIBAFI survey. We hope this survey will serve as an industry tool to provide both the background context for the Islamic financial industry and the framework to progress in the coming years.

The theme for this year's survey is "Sustainability, Growth Drivers, and the Regulatory Challenge." It addresses the issues facing financial institutions in the coming years, the necessary factors for business growth and the regulatory restraints that constrain them. The data collected by the survey create a clear picture of the Islamic financial industry's current state, region-to-region.

This year it also addresses particularly the contribution that Islamic banking is making to sustainable development as embodied in the United Nations Sustainable Development Goals (UN SDGs). The report features a special article by the UN outlining the current financing gap of the UN agenda and the role of Islamic finance as an alternative mode of financing. This reinforces CIBAFI's interest in further enhancing collaboration with the UN and other stakeholders to promote the role of Islamic finance as a viable tool for the financing of sustainable development and the attainment of economic growth.

This year's survey had the largest response yet, with 106 responses from Islamic banks in 33 different countries. Because of the wide range of countries responding, the survey includes a geographic breakdown in order for the reader to see how certain regions are faring compared to others and the unique issues that certain regions are facing that will affect their business.

It is more important now more than ever for banks to adapt to new challenges and use the tools at their disposal. Technology remains a vital asset to the finance industry, and the banks who use it will reap the benefits: increased geographical reach, expansion of the offering of products and services and the ability to streamline the bank's processes. However, it comes with its share of threats including cybersecurity breaches. Adaptation to the digital age is the key to banks' survival.

For Islamic banks in particular, it is important to display the values that make Islamic finance distinctive and place it at the service of human society. This includes thinking about how sustainability and human development can be embedded in all they do.

These issues and many more, are addressed in the survey by the top banking officials who shared their opinions in detailed written responses. We extend our warm thanks to the banking officials who took the time to share their views.

We hope the information within will help paint a clearer picture of the Islamic finance industry as we forge ahead into the coming years.

Abdelilah Belatik

Secretary General

EXECUTIVE SUMMARY

Although 2018 began on an optimistic note, buoyed by global manufacturing and trade success, the market hit a downturn in the later months of the year. The implementation of tariffs, such as those levied by the United States, and retaliatory measures undertaken by economic powerhouses such as China caused widespread uncertainty in the minds of economists and a subsequent slowing of investments. Despite this, the US Federal Reserve raised its policy interest rate by 3%, although 10-year bond rates increased by more modest proportions.

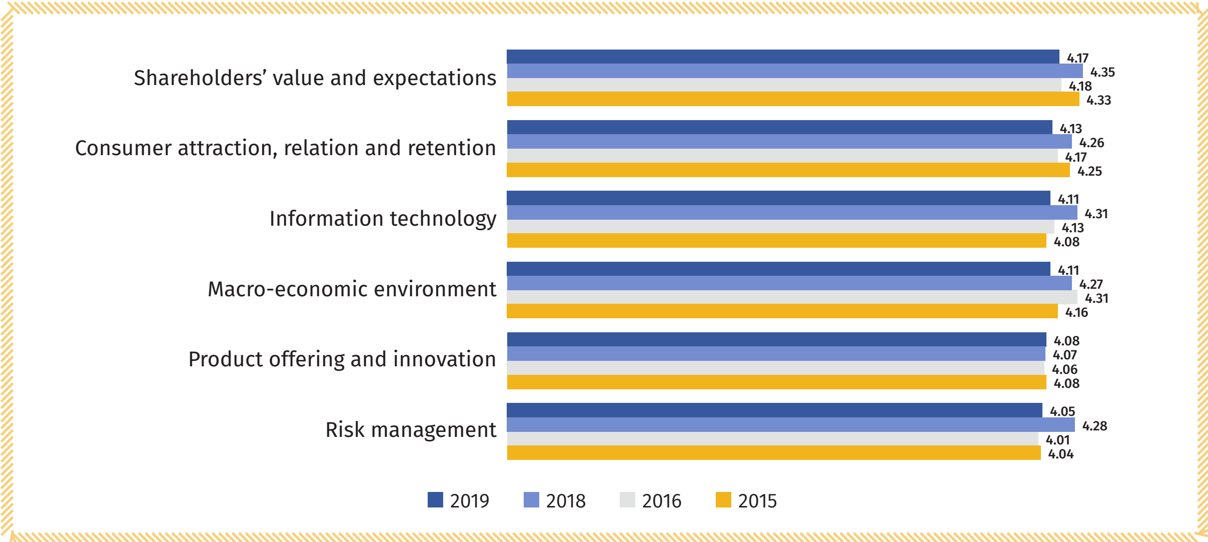
This strengthening of the US dollar put a strain on some of the world's more vulnerable economies and coupled with the political issues occurring both globally and locally, it remains a concern for many Islamic banking institutions. Inflation concerns are ever-present for the upcoming year. The prospect for 2019's macroeconomic environment is uncertain, but as new developments unfold, leaders of banks in the Islamic financing sector seem confident to meet these challenges head on.

Our survey for this year fittingly is titled, "Sustainability, Growth Drivers, and the Regulatory Challenge." Growth drivers are an issue we have covered before, and it is interesting to see how much – or how little – banks' views of them have changed. However, this year we looked also at the contribution that Islamic banking can make, and is making, to wider objectives, particularly those embodied in the SDGs. The results are heartening, though there is still more to be done. We also looked at the regulatory challenges that the industry is facing, especially those that are unique to the Islamic financing sector.

Industry leaders from all regions have projected the same air of confidence as in 2018 for the years to come, expressing sustained confidence in both the future of Islamic finance in their jurisdictions, as well as the banking and finance sectors in general. The optimism is a cautious one, but it is optimism, nonetheless.

They also shared with us their top concerns for the near future. It is understandable that the respondents cited concern for meeting shareholders' expectations. Islamic banking officials who responded demonstrated that they are not only positive, but also prepared; many banks were ready to share the plans they had implemented during the downturn of 2018 and had identified the obstacles they will likely face in coming years. Furthermore, they seemed equipped to address issues of shareholder expectations and capital adequacy in the face of possible economic stagnation. Banks are now facing competition from not only conventional and other Islamic banks, but also from the emergence of unconventional, technology-enabled business models. The publication of this survey will allow banks to compare their strategies with their peers' and glean new information that could prove to be helpful for their situations.

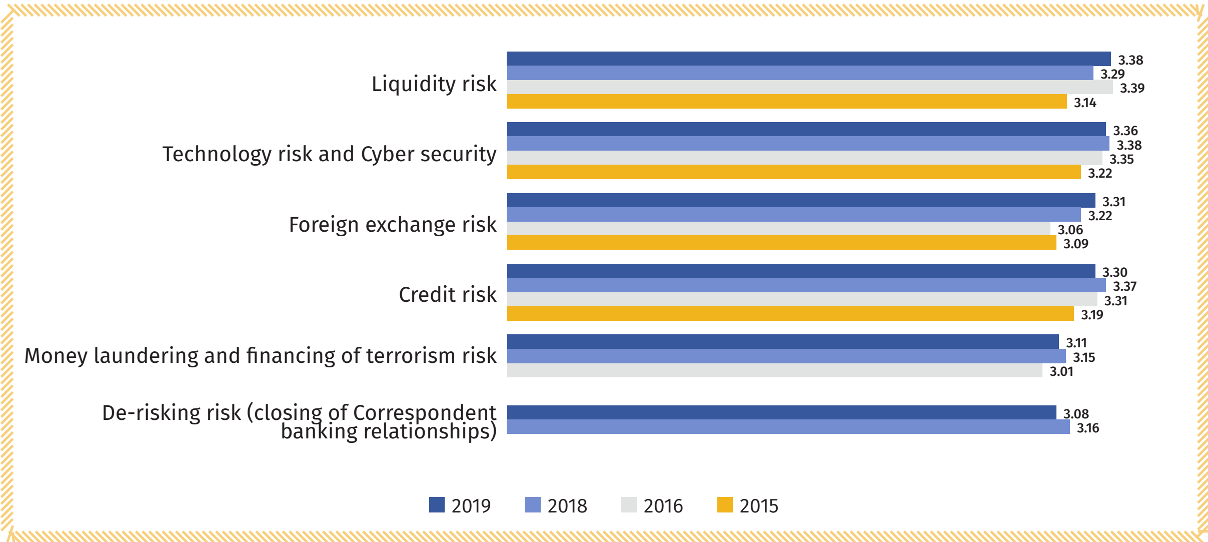
Global Islamic Banking Top Concerns



1: Extremely not Important; 2: Not Important; 3: Fairly Important; 4: Very Important; 5: Extremely Important

Survey respondents are likewise cognizant of the risks they will face in the next few years. The advent of new technology is naturally followed by increased cybersecurity risks such as malware and hacking, and Islamic banking officials are well aware of these risks. In addition, liquidity risk is a feature risk that banks are taking into account in the near future. The report outlines the proposed strategies of the top banking officials that will weather these possible risks.

Global Islamic Banking Top Risks



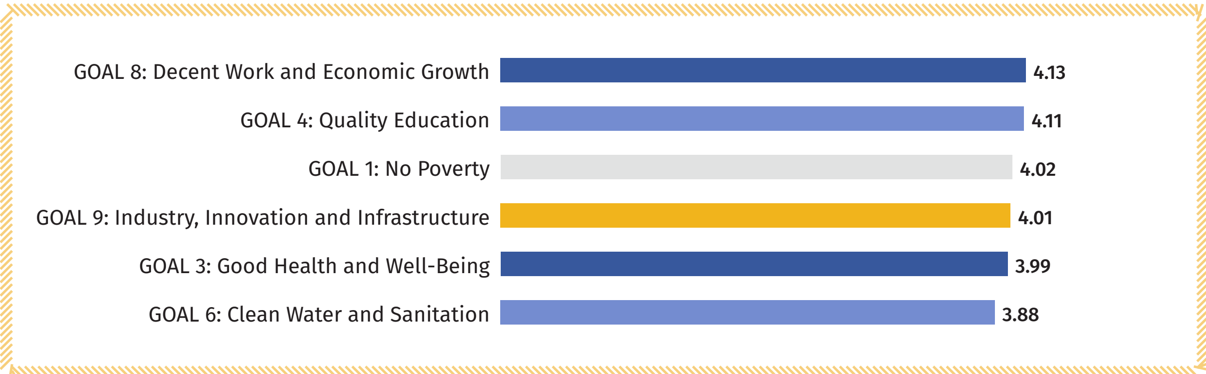
1: No Risk at All; 2: Low Risk; 3: Medium Risk; 4: High Risk; 5: Extreme Risk

Growth drivers are key to financial institutions' success as we move ahead. The Islamic Banking Key Growth Drivers' Monitor asked banking officials to identify the factors they perceived to be important for facilitating growth. Respondents across all regions identified product innovation and market penetration as drivers for advancement. Banks are eager to improve systems already in place, as well as innovate new products that will give them an edge. Also acknowledged is the fact that business growth needs not to be just physical – in the new digital age, "expansion" could also mean pushing one's electronic presence.

Islamic institutions not only have to manoeuvre around these risks while keeping in mind how to promote growth, but they also must deal with regulatory challenges. Some banks adhere to jurisdictional standards, but the bigger picture of international standards should be taken into account as well. While there are clear international standards from the BCBS, AAOIFI, IFSB and FATF, which are implemented in many jurisdictions, some areas of bank business conduct are handled with minimal regulatory guidance. Additionally, banks must operate in accordance with Shariah, often in jurisdictions with no Shariah frameworks of their own and, indeed, often within regulations which do not reflect the distinctiveness of Islamic banking. Some banks, because of their size, have limited ability to influence regulatory bodies, whether local or international, and this survey underlines the responsibility that falls on representative bodies like CIBAFI to engage actively in the regulatory dialogue.

There is increasing concern internationally that banking should contribute to wider developmental aims. We found a heartening level of engagement with the SDGs, not only in the obvious areas of economic growth and industry but also in education and the elimination of poverty. However, while some banks saw this engagement as something that should pervade their whole business, others focused it within more limited areas of charitable giving.

Top Six UN SDGs institutions plan to promote as part of their Business Growth Plan



1: Extremely not Important; 2: Not Important; 3: Fairly Important; 4: Very Important; 5: Extremely Important

The banks' growth, tampered by the need for compliance to Shariah, adherence to regulatory boundaries, and the risks they will face in the years to come, appears to be a hefty task in some jurisdictions. However, this survey allows all banks to reflect on procedures that have worked in the past, while facilitating collaborative strategic efforts looking to the future. It allows a comparison to bring the different struggles and approaches of the various jurisdictions into perspective. More importantly, it puts data results into the context not only of the global image, but time as well: where we were, what we are dealing with now, and where we want to go.

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ABOUT CIBAFI

CIBAFI is an international non-profit organisation founded in 2001 by the Islamic Development Bank (IDB) and a number of leading Islamic financial institutions. CIBAFI is affiliated with the Organisation of Islamic Cooperation (OIC).

CIBAFI represents the Islamic financial services industry globally, defending and promoting its role, consolidating co-operation among its members, and with other institutions with similar interests and objectives. With over 130 members from more than 34 jurisdictions from all around the world, CIBAFI is recognised as a key piece in the international architecture of Islamic finance.

Its mission is to support the Islamic financial services industry as the leading industry voice in advocating regulatory, financial and economic policies that are in the broad interest of its members and that foster the development of the Islamic financial services industry and sound industry practice. CIBAFI is guided by its Strategic Objectives, which are 1) Advocacy of Islamic Finance Values and related Policies & Regulations; 2) Research and Innovation; and 3) Training and Professional Empowerment.