



Islamic Banking Prospects for Future Cooperation

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Enhancing "ShamGen" Banking Turkey, Syria, Lebanon, Jordan
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Your Excellencies, Distinguished Guests, Ladies and Gentlemen,

It is a real pleasure for me to be here in Istanbul to address such a distinguished audience and I would like to thank the Central Bank of the Republic of Turkey and Al Bank Wal Mustathmer group for this invitation.

Today, I would like to share with you some thoughts on the Islamic Banking prospects for a future ShamGen cooperation.

Let me first evoke three important points pertaining to economic and financial cooperations in general:

- 1- The ultimate purpose of strengthening economical and financial ties is to achieve financial development, which in turn supports economic growth and social welfare. The more efficient is the allocation of our economic resources the better our long-run economic performance will be.
- 2- Economic and financial cooperations should proceed in parallel and reinforce each other, meaning that significant advancement in the banking cooperation aside would be more difficult in the absence of an increase in the economic cooperation.

- 3- Economic and financial cooperations results from the effective interplay between public and private actions. While public authorities and regulators' roles is to ensure that basic conditions are in place for market participants to expand their cross-border activities through an adequate regulatory and supervisory framework, the effective cooperation rests eventually on the initiatives of market participants to exploit the opportunities.

In the case of the ShamGen countries, we witnessed an enhancement of the economic cooperation with the increase of the trade exchanges following the bilateral free trade agreements and we are confident that it will further develop in the future with the establishment of a free trade zone. Nevertheless, we are mindful that as of today the ShamGen financial cooperation is lagging behind.

Ladies and Gentlemen,

In order to explore prospects for future cooperation among the ShamGen Islamic Banks, it is worth assessing the current status of this industry in the four jurisdictions and its potential.

Across the ShamGen countries, the banking sector is still heavily dominated by the conventional banks in terms of market players' number and market share. Although still in its infancy, the Islamic banking sector has enjoyed rapid growth in recent years, fuelled by the large Muslim community. In Turkey, the share of the four participation banks from the total assets went up from 2.13% in 2000 to 4.13% as of end July 2010¹. According to the Islamic Financial Centres Competitive Review conducted by the Kuwait Finance House Research, which measures the competitiveness of 20 selected countries across the Globe, Turkey ranked ninth. The successful launch of the first Sukuk created interest within the Turkish investment community to consider raising capital through Sukuk issuances in international markets. In Jordan, the share of the two Islamic banks from the total assets went up from 7.59% in 2000 to 11.38% at the end of 2009² and the central bank granted a third bank the license to operate in the kingdom; In Syria, the market share of the two Islamic Banks from the total assets went up from 2.67% in 2008 to 4.48% in September 2010³; and in Lebanon, the market share of the four Islamic Banks from the total assets has been only around 1%⁴.

In the aftermath of the global financial crisis, it has become increasingly clear that the Islamic financial industry has a great potential to grow, if it can overcome the infrastructural challenges that it is facing such as the establishment of the lender of last resort facility, the availability of short term financial instruments for liquidity management ...

¹ Source: Participation Banks Association in Turkey

² Source: Central Bank of Jordan – Financial Stability Report

³ Source: Central Bank of Syria

⁴ Source: Central Bank of Lebanon

Ladies and Gentlemen,

ShamGen direct cross-border banking, conventional and Islamic alike, could be fostered through further convergence in the banking legislation in order to ensure a level playing field for the financial institutions within the ShamGen. In particular, this convergence would reduce the compliance costs resulting from the multiplicity of rules. For the Islamic Financial industry, the convergence of specific prudential regulations such as the capital requirements, the governance, the distribution of profits and the emphasizing on a common reporting and disclosure frameworks would be favorable. The alignment of the applied Shariah principles in order to avoid Shariah arbitrage opportunities is an additional level of requirement for the enhancement of the cross-border operations. Among the ShamGen countries, only Syria has allowed for the establishment of a central Shariah board which ensures a “national” standardization of the Shariah principles. If we are looking for an increase in the cooperation between the ShamGen Islamic banks, we should take into account that this can be achieved in a context of a minimum consistency among the Fatwa ruling such as a common ban of the sale of debt.

Aside from the direct cross-border provision of banking services, banking cooperation could take place indirectly via foreign establishment, either branches or subsidiaries. We may want to explore the possibility to allow the financial institutions, which satisfied minimum requirements, to branch freely throughout the ShamGen and offer financial services cross-border.

The provision of cross-border banking services implies a greater coordination among the supervisors to ensure financial stability. Apart from the determination of roles and responsibilities for home and host supervisors through formal arrangements such as MOUs, several initiatives can be explored in that respect such as the specification of common actions to be taken by supervisors in a cross-border emergency situation.

Other areas which offer opportunities for cooperation among the ShamGen regulators and supervisors in the Islamic Finance field pertain to the development of arrangement for the exchange of expertise across jurisdiction.

From the market participants’ perspective, the increasing ShamGen trade exchanges are an important opportunity on which ShamGen Islamic banks should capitalize to grow the industry. Since Islamic banks have a basic orientation towards trade, they are in a better position to handle the counter-trade operations between the ShamGen countries.

Contrary to conventional interest-based banks, the Islamic banks are allowed under law to enter into direct equity participation, which can be used with great advantage for exploring the long-term investment opportunities. In order to counteract the fierce competition in the banking sector, Islamic

banks should seek consortium financing for large-scale investment opportunities.

Ladies and Gentlemen,

The prospects are wide open for a ShamGen cooperation in Islamic finance. The path might be challenging but the benefits are worth the effort!

Thank you.