



FOURTH HARVARD UNIVERSITY FORUM ON ISLAMIC FINANCE
HARVARD LAW SCHOOL - SEPTEMBER 30 - OCTOBER 1, 2000

ISLAMIC FINANCE: THE TASK AHEAD: A SHORT REPORT

The Fourth Harvard University Forum on Islamic Finance was held at the Harvard University campus in Cambridge, Massachusetts, on Saturday and Sunday, September 30 and October 1, 2000. The Forum, organized by the Harvard Islamic Finance Information Program in cooperation with the Harvard Islamic Society, enjoyed the participation of over 250 banking and financial industry professionals, *shari'a* scholars, academics, and students of the growing field of Islamic finance. The conference's broad theme "The Task Ahead" embodied the aims of the Forum: to discuss the opportunities and challenges facing Islamic finance while keeping a keen and critical eye on the achievements and performance of the industry in the last quarter century. To this end, over 35 speakers presented their papers at the Forum on aspects ranging from the *shari'a* and theoretical issues in Islamic economics to business, legal, and regulatory perspectives on Islamic finance. In its focus on both the progress and potential of Islamic finance and in covering a wide variety of topics in the field, the Fourth Forum built on previous Harvard University Forums on Islamic Finance.

Saturday, September 30

After the welcoming introduction by Thomas D. Mullins, Executive Director of HIFIP, Samuel L. Hayes, III of the Harvard Business School, Chairman of the Forum, formally opened the first session on Saturday morning. He spoke about necessary changes and opportunities in the Islamic finance industry. Noting that the sector had grown rapidly in since its inception, he found further room for improvement, as well as areas into which the industry and its participants can evolve. Mahmoud A. El-Gamal of Rice University then spoke on Islamic economics, presenting his paper "The Economics of 21st Century Islamic Jurisprudence," in which he constructed a simple model to explain the differences between Islamic finance and Islamic economics. Looking to the future, he noted that jurists and firms can gain an advantage by being in the avant-garde of Islamic financial innovation, but if others do not follow suit, they risk error or the loss of credibility. El-Gamal modeled the tension between competition and cooperation and explained the small number of active participants on the financial and juristic sides.

The second keynote speaker, Stephen Green of HSBC Investment Bank, underlined "Challenges Facing the Islamic Financial Industry." Green, speaking from the perspective of one of the most active institutional participants in the sector, noted the challenges of the years ahead: the emergence of new models, the opportunities afforded by the Internet, and the need for size and scalability in this growing market. In these respects, Green concurred with many of the points put forward by Hayes. The final keynote speaker, Yusuf Talal DeLorenzo, an experienced and noteworthy *sharica* advisor, addressed "Changing Perspectives in Sharica Supervision." He pointed out that *shari'a* supervision-in addition to its usually quoted role as a religious audit-is also a form of consumer advocacy.

After the keynote speeches, the second session, Critical Issues in Islamic Finance, brought together individuals with a wealth of experience and working knowledge of the field. Jassar Al Jassar of Kuwait Finance House (of one of the largest and most successful institutions in the field) noted some successes, prospects, and neglected areas in Islamic finance. Fred Crawford of The National Commercial Bank (NCB) in Saudi Arabia discussed the development of financial products in Islamic finance. In introducing results from NCB's market surveys in Saudi Arabia, Crawford ensured that his conclusions led to far-reaching implications because they were grounded in practicality. Mabid Ali Al Jarhi, of the Islamic Research and Training Institute at the Islamic Development Bank, compared transactions in conventional and Islamic economies, exploring whether transactions in the latter could be more efficient than in the former. The last speaker in this session, Omer Ahmed of Crescent Capital Management in Chicago, canvassed Islamic investment from an institutional investor's perspective, incorporating old concepts in capital management into a new paradigm of Islamically managed assets in a more mature Islamic financial mindset.

The third session of the day, Islamic Finance: Sharica Perspectives, featured noted jurists and *shari'a* consultants. Mohamed Ali Elgari spoke about the critical issue of the purification of Islamic equity funds. He elaborated on the *shari'a* foundation as well as the methodology for such purification, a process central to the acceptability of an equity fund as Islamic. In a similar vein, Nizam Yaquby spoke about *shari'a* perspectives on trading in equities, offering an overview of the literature on the topic, with a detailed survey of the pros and cons, as well as his own opinion on the issue. Yusuf Talal DeLorenzo then dealt with "Shari'a Supervision of Mutual Funds," stressing the importance of the competence of *shari'a* supervisors for the credibility of mutual funds as well as of the Islamic financial sector in general. This session has been described as the "gem of the Fourth Forum." The audience took full advantage of the depth of knowledge panelists possessed of the *shari'a* and its interaction with finance. Questions ranged from the permissibility of investing in 401K's to the issue of a universal *shari'a* board.

The Forum broke into two parallel sessions following the sharica session. In order to increase understanding of Islamic finance by newcomers to the field, particularly students, this year HIFIP set up a Workshop for Newcomers to Islamic Economics and Finance, chaired by Mahmoud El-Gamal of Rice University. The session was open to the public for free. El-Gamal presented a general introduction to Islamic economics, debunking some of the myths and misconceptions that surround the field. He was followed by Mohammad Fadel of the U.S. Court of Appeals for the 4th Circuit, who compared and contrasted the approaches of Islamic law, the common law, and modern regulations to the regulation of risk in financial markets. Fadel demonstrated that Islamic law was consistent when its approach was properly understood, and examined how differences affect the practice of Islamic finance in the field, particularly with regard to regulation. Finally, Iqbal Ahmad Khan of HSBC Amanah Finance spoke about Islamic finance from the viewpoint of the practitioner, noting its achievements to date and its current challenges. A lively question and answer session followed. The session in fact lasted an hour longer than expected due to the large number of questions from interested attendees.

Parallel to the workshop was a session on Current Research in Islamic Banking and Finance. Sudin Haron and Norafifah Ahmad of the Northern University of Malaysia looked at the Islamic banking sector in Malaysia, which forms a feasible alternative to the conventional sector. Zamir Iqbal of the World Bank examined the scope of off-balance sheet transactions in Islamic finance and posited that they may be able to improve liquidity as well as portfolio diversification and risk management in the industry. Shaikh Abdul Hamid of New Hampshire College discussed corporate debt in Islam, contending that the harmful effects of debt outweigh its advantages. Aamir Khan of ABN AMRO and Tariq Al-Rifai of The International Investor highlighted the conspicuous lack of venture capital in contemporary Islamic finance models.

Sunday, October 1

Among the speakers in Islamic Finance: Business Perspectives, the first session on Sunday, were Yahia Abdul-Rahman and Mike Abdelaaty of American Finance House-LARIBA, who catalogued the challenges that no-interest finance companies in America face in capitalization. Iqbal Ahmad Khan of HSBC Amanah Finance identified a potential trade-off between reach and richness in Islamic finance and attempted to find a balance between the two. John Bauer and Richard Keigher of SAMBA Capital Management (a division of NCB) described opportunities and challenges for Islamic equity fund managers, addressing questions of *shari'a* supervision, marketing and distribution. Essam Mahmoud of King Fahd University of Petroleum and Minerals and Gillian Rice of the American Graduate School of Management jointly presented a paper raising the issue of marketing leadership in Islamic financial institutions. They argued that intelligence must be emphasized at all employee levels and departments so that employees can build and share both managerial and Islamic knowledge within the organization in order to develop truly competitive Islamic products.

The Forum then broke up into two parallel sessions. The first approached the issue of law and regulation from three separate perspectives. W. Donald Knight, Jr. of King & Spalding and Henry Thompson of First Islamic Investment Bank raised a number of legal, tax and regulatory issues in structuring Islamic investment funds in the United States. Jameel W. Aalim-Johnson of the Office of Representative Gregory Meeks surveyed the legislative process for regulation of the financial industry and the role of the financial industry in influencing the development of these regulations. Andrew Cunningham of Moody's Investors' Service urged regulators to recognize the "otherness" of Islamic finance as not just a technical inconvenience to be "fixed" on the path to standardization but as a quality valued by the industry and its investors. He questioned whether the constraints on Islamic finance were more cultural or based on real accounting problems.

The second parallel session, Contemporary and Historical Views on Islamic Economics and Finance, featured speakers such as M. Kabir Hassan of the University of New Orleans, who provided an econometric analysis of

economic stability and Islamic finance. He hypothesized that such non-interest systems may indeed be more stable, and then tested his hypothesis with a battery of econometric tests. Ibrahim Warde of the University of California at Berkeley provided an assessment of Islamic finance in the last quarter century. He noted achievements as well as finding significant room for improvement. In suggesting new areas of research, he pointed to areas that he claimed have traditionally been shunned, such as the moral economy of Islam, Islamic economic cultures, and the Islamic moral hazard. Muqtedar Khan stringently criticized the direction of Islamic economics in concentrating solely on *riba*. He claimed that equity considerations demanded similar, if not greater, notice.

The final session, Islamic Funds and Indices, featured players such as Naseeruddin Khan, who asked whether the performance of Islamic funds can measure up to their hype and presented a case study of his own institution. Tom Gainor presented “A Practical Guide to Product Development,” addressing the question of how best to design Islamic funds and indices. Scott Valpey of Azzad Asset Management treated similar issues in his paper on structuring Islamic equity funds, which covered topics such as the selection and place of *shari’a* boards, purification, and practical questions of portfolio management and performance. Laurent Chappuis of Pictet & Cie measured the impact that *shari’a* guidelines are having on Islamic funds, pinpointing the differences between conventional and Islamic funds in terms of sectoral and regional allocation and thus on performance. He identified the companies whose exclusion from the universe of Islamic funds has the largest impact in the comparison.

Taha bin Hasan Abdul-Basser, Chief Technology Officer of HIFIP, described the Harvard Islamic Finance Information Program’s iDataBank project, which will take the HIFIP DataBank online to enable easier data retrieval as well as entry. Finally, S. Nazim Ali, HIFIP’s Director of Operations of HIFIP, announced that the Fifth Forum would be held on October 6 and 7, 2001. Thanking the speakers and attendees, Ali invited Thomas D. Mullins, Executive Director of HIFIP, to formally close the Fourth Harvard University Forum on Islamic Finance.