



FIFTH HARVARD UNIVERSITY FORUM ON ISLAMIC FINANCE  
HARVARD LAW SCHOOL - APRIL 6-7, 2002

## ISLAMIC FINANCE IN THE GLOBAL MARKET: A SHORT REPORT

The Fifth Harvard University Forum on Islamic Finance was held at Harvard University on 6-7 April 2002. The Forum, titled "Islamic Finance: Dynamics and Development" and originally scheduled for October of 2001, had been postponed after the tragic events of September 11. It came at a time of a significant upsurge in interest in Islamic finance by Muslims and non-Muslims alike. In the days preceding the Forum, WBUR (Boston public radio) aired a feature about the growth of Islamic Finance in the West. Increased awareness of the Islamic Finance industry, coupled with a widespread desire to better understand Middle Eastern financial systems, made this year's forum the best attended ever. The U. S. Treasury Department, impressed by the quality of the presentations at the Forum, has asked HIFIP to organize an "Islamic Finance 101" seminar in Washington, D. C. on April 26 for Treasury Department officials and congressional staff.

### Saturday, April 6

Thomas Mullins, Executive Director of the Harvard Islamic Finance Information Program, welcomed the guests to the Forum. Mr. Mullins stressed the important role of the Islamic Finance industry in creating dialogue between Islam and the West, a role made especially relevant after September 11. Forum Chairperson, Samuel Hayes, Jacob Schiff Professor Emeritus at Harvard Business School, in his opening remarks commended the industry on the many strides it has taken in the past decade and outlined the areas where it still must improve. Saif Shah Mohammed, president of Harvard Islamic Society, in his introduction suggested that the industry should provide relevant services to students such as *shari'a*-compliant educational loans and young professional programs.

As in past years, the keynote speeches of the Fifth Forum were delivered by high-level practitioners, regulators, academics, and *shari'a* scholars in the field of Islamic Finance and Economics. The Fifth Forum Address, delivered by Ahmad Mohamed Ali, President of Islamic Development Bank (IDB), was titled "The Emerging Islamic Financial Architecture: The Way Ahead." In his remarks Dr. Ali detailed the measures that IDB has taken to strengthen the international Islamic financial architecture by establishing the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI), the Islamic Financial Services Organization, an International Islamic financial market, and an Islamic rating agency.

In his well-received keynote address, Ahmed Bin Mohammed Al-Khalifa, Governor of the Bahrain Monetary Agency (BMA), discussed "The Progress of Islamic Banking and Finance in Bahrain." In his remarks Mr. Al-Khalifa explained that Islamic institutions have long recognized the need to establish a regulatory regime that is industry specific but constructed to a standard that compares favorably with international best practice in the regulation of conventional financial institutions. He also stressed the importance of human resource development, arguing that the industry must make this issue a priority if it hopes to successfully compete with conventional institutions. Frank Vogel, Adjunct Professor and Director of Islamic Legal Studies Program at Harvard Law School, delivered a keynote address entitled "Ijtihad in Islamic Finance." In his speech, Professor Vogel pointed to Islamic Finance as the field in which *ijtihad* had been most successfully carried out in the modern age.

The remaining sessions of the Fifth Forum carried on with numerous topics discussed in past years, including Legal and Structural Issues in Islamic Finance, Strategic Trends, Product Development, and Islamic Finance for Newcomers.

The Strategic Trends session brought together an impressive cast of top Islamic Finance executives and academics. M. Nejatullah Siddiqi, president of the International Association for Islamic Economics and a visiting Fellow at UCLA, discussed the emerging advantages of Islamic finance and banking. In his remarks Dr. Siddiqi posited that three reasons help explain the continued progress in Islamic banking and finance: deficiencies in the current system that make people search for alternatives, the association of the Islamic financial movement with the recent resurgence in Islamic societies, and the strong moral orientation of Islamic finance. Monzer Kahf, a former research economist with the IDB, looked at the economic-cum-political alliance between bankers and Islamic religious scholars, arguing that the newfound alliance introduces much-needed ethical standards into investing. Hazim Al-Mutairi, sitting in for Adnan al-Bahar, discussed the prospects and implications of consolidation within the Middle East Islamic banking sector, drawing on the experience of the recent merger between The International Investor and Dallah Albaraka. Jassar Al Jassar, General Manager of Kuwait Finance House, discussed how *shari'a* compliance mechanisms have helped institutions navigate through the regulatory environment as Islamic financial institutions rapidly grow in sophistication. Ramzi Abu Khadra, CEO of iHilal.com, highlighted his company's innovative efforts to use the Internet as a global platform to aggregate and streamline the market for Islamic financial market, which, while growing at double-digit rates, remains quite fragmented.

After lunch, the Legal and Structural Issues session, chaired by Frank Vogel, featured interesting presentations from Michael J.T. McMillen, Mudassir Siddiqui, and Robert Toan & Monir Barakat. Mr. McMillen, Partner at King and Spalding in New York, discussed the development of the first *istisnac-ijara* structure for the construction and mini-perm financing of U.S. residential and commercial real estate. Mr. Siddiqui, Independent Shariah Consultant, delivered a speech entitled "The Principle of the Shariah vs. its application," wherein he argued that Islamic products should not merely camouflage the interest element contained in traditional products; but that they should rather conform to the letter and spirit of *shari'a* concerns. Mr. Toan and Mr. Barakat, both of Wafra Investment Advisory Group, examined several types of credit support in conventional finance and corresponding or similar arrangements in Islamic *Ijara* (leasing) transactions. Fatima Iliasu read a summary of Engku Rabiah Adawiah Bt Engku Ali's paper "Re-defining Property and Property Rights in the Islamic Law of Contract," which looked at the varying *shari'a* positions on the trade of intangible assets such as intellectual property and rights to receivables.

The final session on Saturday featured a panel discussion about Islamic Finance in the Contemporary Context, which aimed to review the challenges and opportunities facing the Islamic financial industry since September 11 and the market downturn, crises, and bankruptcies that followed. The four panelists, Fred Crawford, James Godec (replacing Khalid Abdulla-Janahi), Iqbal Khan, and Abdulkader Thomas, and the session chair, Mahmoud El-Gamal, each delivered short presentations, which were followed by an extensive question-and-answer session. While acknowledging that 9/11 and its fallout have placed the Islamic Finance industry under a good deal of scrutiny, many panelists argued that the industry has come through the current crisis unscathed or even strengthened. The new focus on transparency will force the industry to upgrade its bookkeeping, while know-your-customer strategies were posited as the best way to prevent terrorist-tainted money from passing through Islamic banks.

## Sunday, April 7

Sunday morning witnessed one of the most eagerly anticipated sessions, namely Community Banking in the West. Designed to address the growth of Islamic finance in the West, three of the presentations focused on the burgeoning Islamic home financing market in the United States. Tariq al-Rifai, Vice-President of Islamic Banking at HSBC USA, focused on the extensive research carried out by HSBC when designing a range of products that would satisfy consumer needs, meet sharica guidelines, and conform to New York's regulatory environment. Saber Salam, Vice-President of Freddie Mac, discussed his firm's efforts to open doors for Muslim families in America by purchasing home financing contracts from Muslim homebuyers, and approving new Freddie Mac Sellers/Serviceirs that specialize in providing financing to Muslim consumers in the U.S. Yahia Abdul-Rahman and Mike Abdelaaty, Founder and President of LARIBA American Finance House, gave a presentation detailing their long experience in the Islamic finance field in America, and arguing that, as Islamic home financing becomes more developed and better publicized, it will be in great demand by Muslims and non-Muslims alike. Rushdi Siddiqui, Director of the Dow Jones Islamic Index, argued that developing 'Islamic windows' within conventional financial institutions constitutes the immediate future for Islamic banking in the West.

Shaykh Nizam Yaquby, an Independent Shari'ah Consultant from Bahrain, again returned to Harvard, where he delivered a keynote address on Sunday morning entitled, "What can Islamic Banks Do Besides Eliminating Riba." In his remarks Shaykh Nizam sought to combat the notion that the mandate of Islamic banking is simply to eliminate usury. He posed a number of questions, asking what are the social implications and larger economic benefits of an Islamic financial system? What are Islamic banks doing to eliminate poverty? Has Islamic finance become the roost of the few, or has it been able to address the needs and aspirations of the general populace? Shaykh Nizam's

answers to these questions indicate that while the industry has made enormous progress in the last decade, it still has a long way to go.

After Shaykh Nizam's keynote address the Forum divided into two parallel sessions. Monzer Kahf chaired a session devoted to Case Studies, while Munawar Iqbal chaired a session on Product Development next door.

Opening up the Case Studies session, Tariq Hassan, Advisor to the Finance Minister of Pakistan, looked at Pakistan's efforts to abide by a Supreme Court decision to take the necessary legislative and executive measures to transform the current interest-free banking system into a genuine Islamic financial system. Mulya Siregar and Nasirwan Ilyas, Researchers from Bank Indonesia, highlighted the strategies undertaken by Bank Indonesia, the central bank, to develop *shari'a*-compliant banking capabilities. Kabir Hassan, Associate Chair at the University of New Orleans, employed an empirical approach to examine the market efficiency of the Dow Jones Islamic Index and to see whether Islamic investors must suffer lower returns because of their ethical concerns. Hulusi Inanoglu, PhD candidate at Rice University, compared the efficiency during the 1990-2000 period of 31 conventional banks with that of 4 Islamic banks in Turkey. His surprising conclusions are that Islamic banks are no less efficient than their conventional counterparts, and are more efficient when controlling for size of operations.

In the Product Development session, Omar Fisher and Dawood Taylor, both of Takaful Tacawuni at Bank Aljazira, explored the viability of *takaful* (Islamic insurance) to hedge against medium- to long-term risk in an Islamically acceptable way. Zafar Sareshwala of Parsoli UK used his firm as a case study to analyze Islamic investment objectives, performance benchmarks, investment restrictions, purification methodologies, composition, and the role of the *shari'a* supervisory board. Norafifah Ahmad of Northern University of Malaysia undertook an analysis of why major corporate customers either chose or did not choose an Islamic financial system in Malaysia where both the conventional and Islamic systems exist side-by-side. Dadang Muljuwan of Loughborough University presented his joint paper, titled "Synchronization of Investors' Risk Aversion and Managers' Risk Taking." Specifically Mr. Muljuwan argued that a capital adequacy requirement must be established which both protects risk-averse depositors and gives correct incentives to shareholders which promote prudent behavior.

After lunch in the adjoining Greenhouse Café, the Forum resumed with two more parallel sessions: Investing and Trading Islamically chaired by Fred Crawford, and a Workshop on Islamic Finance for Newcomers coordinated by Ibrahim Warde.

Michael Swingler and Nazeem Ebrahim, both of Oasis Asset Management in Cape Town, delivered a presentation detailing their firm's success in managing *shari'a*-compliant mutual funds in a volatile equity environment. Stressing the necessity of active fund management, the two speakers showed how Oasis has been able to minimize losses during the bear market, allowing them to outperform their rivals. John Lightstone, Adjunct Professor of finance at Pace University, delivered an interesting lecture explaining his innovative model to allow managers to back-test their *shari'a*-compliant funds. Mr. Lightstone argued that his model can be used to determine how well an Islamic index would have performed in the early 90s before the creation of the Dow Jones Islamic Index. Like Oasis, Mr. Lightstone concluded that actively managed *shari'a*-compliant funds would have historically outperformed passively managed ones. Mahboob Hossain of Credit Suisse First Boston discussed private equity in Islamic finance, arguing that venture capital and real estate investment trusts (REITs) provided the most potential for growth in the Islamic private equity market.

For the second year, the Harvard Forum offered a free Workshop on Islamic Finance for Newcomers. The session aimed to introduce Islamic Finance to the members of the audience who had had little to no previous exposure to the field by describing Islamic finance from a theoretical, *shari'a*, and practitioner's perspective. Ibrahim Warde, Course Director of Euromoney Training in London, coordinated the session and described the theory underlying Islamic Finance. Omar Fisher of Takaful Ta'awuni at Bank Aljazira presented Islamic finance from a practitioner's perspective, while Taha bin Hasan Abdul-Basser, PhD. candidate in Near Eastern Languages and Civilizations at Harvard University, described the shariah principles underlying Islamic finance. An engaging question-and-answer session followed their short presentations.

The final session of the conference featured the unveiling of the New HIFIP Portal and iDataBank. Mr. Abdul-Basser, who is also the Coordinator of Software Development at HIFIP, described how the new remote Data Entry System (DES) will allow researchers from around the world to contribute to the iDataBank. Mr. Abdul-Basser also stressed that by providing online access to the iDataBank, information would instantaneously be made available to HIFIP sponsors, thus eliminating the lag time of publishing the DataBank CD-ROM.

As in past years, S. Nazim Ali, HIFIP Director of Operations, closed the forum by thanking all of the spon-

sors, speakers, and participants. He also commented that the benefits of the Forum would extend far beyond the two days of the conference, noting one the great strengths of this Forum is the publication of proceedings, remarking, “It is difficult to let this knowledge go away with out recording it in a permanent form.” Further, Dr. Nazim Ali mentioned that the 300-page Proceedings of the Fourth Harvard University Forum on Islamic Finance, widely recognized as the leading scholarly publication within the field, had just been published and are available for purchase from HIFIP.