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Islamic finance needs ‘real transformation’

The Islamic finance industry needs to undergo a ‘real transformation’ if it is to grow and compete internationally.

This was the message from Mr. Rasheed Mohammed Al Maraj, Governor of the Central Bank of Bahrain (CBB), to over 1,300 delegates attending the 20th annual World Islamic Banking Conference (WIBC), which took place in Bahrain from 3 to 5 December 2013.

Held under the patronage of His Royal Highness Prime Minister Prince Khalifa bin Salman Al Khalifa, and supported by the CBB, the theme of the event was ‘Industry Transformation to Improve Global Competitiveness’ across key areas of the Islamic finance sector, including regulatory, strategic, Shari’a, operational and risk transformation.

In his opening address, Mr. Al Maraj said Islamic finance had come a long way in a relatively short space of time.

However, there is a need to identify practical, constructive, and sustainable frameworks for improving the competitiveness of Islamic finance.

“The ability to compete requires financial strength and a wide constituency of stakeholder confidence. Financial strength requires banks to have larger balance sheets to enable them to compete at the top table. That is reliant upon an increase in the capital of institutions,” said Mr. Al Maraj.

“A major influx of funds to the industry is required, underpinned by a deep understanding of the changing financial landscape to invest wisely for the future.”

Stakeholder confidence is built upon demonstrably effective frameworks, he pointed out.

The industry, thus, needs a consistent interpretation of Shari’a, linked with an acceptance of the principles of Shari’a into the judicial system of major financial centres; standardised product documentation; and changes to the business model to facilitate diversification of products and services to provide a more attractive proposition to customers.

“These initiatives are vital if we are to compete internationally, attract better skilled resources, and participate as equals with existing regional financial institutions,” said Mr. Al Maraj.

Extending the reach of Islamic finance into new and developing markets is also extremely critical. Many countries have now recognised the potential of Islamic finance, and a recent conference in London has ignited serious interest in many parts of the Western world.

“All of these developments are positive, but we must be ready to optimise the opportunities at hand if the industry is to grow sustainably,” he said.

“These are laudable, although extremely challenging objectives. The road map is complex; it varies in detail from one institution to another; and from one jurisdiction to another.”

A successful road map will take into account the dynamically changing landscape facing the industry as a whole, and the Islamic finance industry in particular.

“Put in simple terms, the Islamic finance industry requires a transformation,” said Mr. Al Maraj.

“I urge everyone with an interest in Islamic finance to work together to make the transformation real.”

According to the World Islamic Banking Competitiveness Report 2013-14, presented at WIBC 2013, global Islamic banking assets with commercial banks are expected to reach US$1.72 trillion in 2013, from US$1.54 trillion in 2012. Islamic banks today serve approximately 38 million customers globally.

The report, published by EY, finds there is increased demand on established and new reference centres, including Bahrain and Malaysia, to provide leadership for the next phase of the industry’s development.

“We believe that the future success of Islamic banks will be measured less by the growth of assets and more by the quality of this growth,” said Mr. Gordon Bennie, Partner and MENA financial services leader at EY.

“Banks with strong connectivity across key markets and sectors are set to gain.”

Mr. Ashar Nazim, Partner, Global Islamic Banking Center, at EY, said the biggest challenges for Islamic banks are how to become a mainstream form of banking in their home markets, diversification to build regional brands, and taking a more socially responsible approach to differentiate themselves from conventional banks.

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Regulators support industry transformation

Regulators in Bahrain and around the world are working to support the Islamic finance industry achieve its much needed transformation, said Mr. Rasheed Al Maraj, Governor of the Central Bank of Bahrain (CBB).

Rules to strengthen banks' capital bases, and promote transparency and better governance are among the actions being taken by the CBB and its peers, he said at the 20th annual World Islamic Banking Conference, held in Bahrain from 3 to 5 December 2013.

Over 1,300 delegates from 50 countries attended the milestone event, held under the theme 'Industry Transformation to Improve Global Competitiveness' across key areas of the Islamic finance sector, including regulatory, strategic, Shari'a, operational and risk transformation.

"No transformation of the industry can be fully achieved with any confidence unless it is underpinned by an appropriate, well founded, globally accepted, regulatory framework and agreed upon international standards of practice," said Mr. Al Maraj.

"A framework of this nature must be sufficiently robust to bring consistency of approach, whilst at the same time it must be sufficiently flexible to accommodate the regional and local environment. This presents a major challenge, but more importantly offers the opportunity for sustainable and significant success."

Enumerating some examples of what financial regulators are doing to facilitate this transformation, he said best practice corporate governance, including transparency of operations, lies at the heart of all successful business frameworks.

"After the onset of the global financial crisis, the Basel Committee initiated consultation in respect of governance and Board sub-committee structures, including the extremely sensitive but absolutely key area of the remuneration structure," said Mr. Al Maraj.

"Many regulators have accepted the challenge, and this will change the culture of the industry to one which provides a clear link between remuneration and performance, with an emphasis on long-term performance measures rather than short-term personal gain."

He said the CBB had recently issued new directives for sound remuneration practices for all licensed banks in Bahrain.

Transparency and disclosure standards are being strengthened in order to make financial reporting more easily and readily understandable, as well as to provide a greater amount of more useful data to stakeholders.

Basel III requires banks to hold more Tier 1 capital, incorporating the lessons of the recent past which have clearly demonstrated the need for banks to have adequate liquidity, in addition to regulatory capital, to sustain operations during any crisis. The composition of balance sheets is changing and, as a result, both conventional and Islamic banks are making fundamental changes to their business models.

"The overall outcome is that Islamic finance is benefiting from these changes. The over-reliance on real estate and infrastructure projects is being systematically replaced with a recognition that revenue-generating assets, which in turn provide identifiable, sustainable profits for the future, is the way forward," said Mr. Al Maraj.

The new models will both encourage and support the introduction of increased venture capital. If this is used to help small and medium enterprises (SMEs) to grow and develop, the potential is clear.

"An upward spiral is within our grasp; transformation is key; exponential growth is attainable. The question is – are we up to the challenge?" asked Mr. Al Maraj.

Risk management practices continue to be highlighted and incrementally improved, including the implementation of more easily understood risk/reward methodologies, and a demonstrable link between successful management of risk and a successful business outcome.

The growing sophistication of stakeholders will demand best in breed internal audit, compliance, and risk management principles and practices to be implemented, he said.

Integral to all of these initiatives is the importance of Shari'a. A greater number of Shari'a scholars are required; Shari'a reviewers must be further trained and provided with career development opportunities.

"Consistency of approach and understanding should be the watchwords. Islamic financial institutions need to quickly address these issues," said Mr. Al Maraj.

Moving specifically to Bahrain, the CBB's financial sector development strategy has been, and shall continue to be, focused on the following areas:

- Maintain and enhance the CBB's leadership in the development of Islamic finance through a continuous programme of providing thought-provoking ideas and suggestions; and dialogue with the industry;
- Maintain our robust regulatory standards, and to continue to develop these in line with international standards;
- Work closely with the industry, the Waqf Fund and the Bahrain Institute of Banking and Finance on further developing human capital which is vital to future success;
- Encourage mergers and acquisitions aimed at strengthening the resilience of locally incorporated banks in the Kingdom; and
- Encourage our licensees to adopt best practices in every avenue of their work, with an emphasis on corporate governance practices, transparency of reporting, risk management, internal audit and compliance.

WIBC awards presented to Islamic banking leaders

Achievements, innovations and excellence in the international Islamic banking and finance industry were recognised at the awards ceremony held on the sidelines of the 20th World Islamic Banking Conference.

The annual WIBC Awards recognise individuals and institutions that have made significant contributions to the Islamic banking and finance industry.

The award for Islamic Banker of the Year went to Mr. Afaq Khan, Chief Executive of Standard Chartered Saadiq.

The WIBC Institutional Excellence Award was presented to Kuwait Finance House - Bahrain.

The WIBC Outstanding Contribution Award – recognising outstanding contributions by an individual in the global Islamic finance industry – was awarded to Shaikh Saleh Abdullah Kamel, Chairman and Founder of Dallah Al Baraka Group.

The ceremony also featured a number of special awards categories that recognised pioneering initiatives in the global Islamic banking and finance industry looking back over the past two decades.

The WIBC industry innovator award was presented to Mr. Rushdi Siddiqui, Adviser, Thomson Reuters. The WIBC Shari'a leadership award was presented to Dr Hussain Hamed Hassan. The WIBC human capital development award went to Tamkeen for institutionalising new concepts within Bahrain's private sector. The WIBC thought leadership award was given to EY.

Industry must support standardisation efforts

The Islamic finance industry must support efforts aimed at harmonising and standardising practices, to facilitate the industry's growth across geographic and regional boundaries.

Such growth is vital for Islamic financial institutions to become truly global and become more competitive, said Mr. Khalid Hamad, Executive Director, Banking Supervision, at the Central Bank of Bahrain (CBB) and Chairman of the International Islamic Financial Market (IIFM).

He was speaking at IIFM's 4th Industry Briefing Seminar on Islamic Capital & Money Market, which was held as a preconference event of the World Islamic Banking Conference 2013. The topic of the seminar was 'Development of Islamic Capital & Money Market: The way forward and required ideal strategies'. The event attracted more than 300 participants, a record preconference event.

The following critical issues were discussed:

- Global Sukuk Market development and Potential for Market Standardisation;
- Collateralisation of Islamic Securities as a liquidity management tool and IIFM Standard;
- Development in Tahawwut (Islamic Hedging) segment, Product documentation standards and Law reforms; and
- IIFM Inter-bank Unrestricted Wakala Standard.

The pragmatically focused executive briefing was led by a number of experienced and respected industry practitioners who provided valuable insight into the technical aspects of Islamic hedging, sukuk and liquidity management alternatives which resulted in creating a deeper knowledge of the critical issues. The seminar was also able to provide a better understanding of IIFM standards and its mechanics which will assist in the implementation of the documentation and product standards at a global level.

The experts stressed on the need for high standards of disclosure, transparency and governance to ensure sufficient levels of investor confidence that will lead to development of a robust and credible market.

It was also stressed that the major challenge in the development of Islamic finance is the need for it to be integrated within the global architecture. The twin approaches of ensuring strict compliance with the principles of Islamic commercial jurisprudence and with internationally acceptable standards of conduct and discipline are critical to success.

IIFM's ultimate objective is to facilitate unification, Shari'a harmonisation and legal reforms in Islamic financial markets, the true potential of which can be achieved by providing support to IIFM in its Islamic industry unification efforts by all stakeholders, particularly by Islamic financial institutions.

Support from the regulators is also key as the standards are of a voluntary nature but are equally beneficial to regulators as well.

IIFM holds sukuk restructuring seminar

The International Islamic Financial Market (IIFM) organised an Industry Consultative Seminar on 'Sukuk Restructuring', as part of its efforts to deliberate on key issues and challenges relating to sukuk.

The specialised seminar was supported by the Islamic Research and Training Institute (IRTI) of the Islamic Development Bank Group and hosted by Bahrain-based Al Baraka Banking Group.

The diverse gathering of over 100 participants included a number of regulators, Shari'a scholars, senior representatives from event of the World Islamic Banking Conference accounting firms, researchers, standard-setting and infrastructure bodies, including Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI), General Council for Islamic Banks and Financial Institutions (CIBAFI), and the International Monetary Fund (IMF).

The consultative seminar deliberated on the sukuk market in general and sukuk restructuring issues in particular. The main objective was to assess the standardisation requirements in this very important Islamic capital market instrument as well as highlight the lessons learnt from limited sukuk defaults and subsequent restructuring undertaken.

The presentations and discussions provided direction to IIFM and other standard-setting organisations in addressing several pertinent issues concerning the sukuk market as well as providing leads for further development of this key Islamic instrument.

IIFM provided sukuk analytical details of international sukuk issuances till the year 2007 and impact on sukuk due to the global financial crisis in the year 2008. According to IIFM-verified sukuk data, the international sukuk market was in growth trend till 2007. However, sukuk was directly impacted by the financial crisis and the 2008 to 2010 period saw a very low volume of issuances.

Several issues ran into difficulty and initially the amount of sukuk facing difficulty was US$7.4 billion, out of US$37 billion outstanding international sukuk, i.e. 17 percent of the market. However, one of the larger sukuk from Dubai was eventually paid off, and the remaining US$3.1 billion (7 percent) have been either restructured or are currently in the midst of restructuring. Only a couple of sukuk are in default with no restructuring in sight.

Due to the improvement in the market environment led by sovereigns, the demand factor and some repayment and restructuring of international defaulted sukuk, the market regained its confidence in 2011 and the following year, 2012, saw a record global sukuk issuance of US$137 billion. This growth trend continued in 2013.

The key issues discussed at the consultative seminar were:

The key issues discussed at the consultative seminar were: Asset Backed & Asset Based Sukuk; Minority Interest Rights; SPVs & Trusts Responsibilities & Rights; Information flow between Lead Manager & Paying Agent; Private Placement & related issues; Tenor of restructured Sukuk; and Role of Chapter 11 in Islamic Finance.

Mr. Khalid Hamad, Chairman of IIFM, said that despite the global financial crises and European sovereign debt problems, Islamic capital and money markets have shown resilience over the past few years. The discussions at the seminar will help in enabling sukuk standardisation, thus, allowing for sukuk defaults and restructuring to be handled properly.

Mr. Ijlal Alvi, Chief Executive of IIFM, said the objectives of the consultative seminar were met and the findings will assist IIFM in developing guidelines for minimising risk of sukuk default as well as developing comprehensive standardised documents on sukuk for use across the globe.

The sukuk restructuring consultation was the first part of IIFM's sukuk standardisation assessment. A final consultation on sukuk standardisation covering broader issues, including documentation requirements, will be held in the coming months, following which IIFM will initiate its sukuk standards and guidelines development process.

Islamic banks need to be true to Shari'a

Islamic banks need to adhere more closely to the tenets of the Shari'a, the very basis of Islamic finance, says Mr. Rasheed Mohammed Al Maraj, Governor of the Central Bank of Bahrain (CBB).

Speaking at an annual conference on Islamic banking and finance, held in Bahrain on 18 and 19 November 2013, Mr. Al Maraj also emphasised the importance of risk management and standardisation of Islamic banking products.

The event, organised by the Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI) in partnership with the World Bank, was held under the auspices of the CBB.

Conference discussions focused on issues related to the development and adoption of international accounting standards for Islamic finance, dynamics of auditing and risks, incorporation of Shari'a principles in legal documentation, further innovation on takaful (Islamic insurance) operations and products, and continuing development of Islamic venture capital.

The annual event is part of AAOIFI's on-going consultative process with the international Islamic finance industry on the development and review of its standards on Shari'a, accounting, auditing, ethics and governance. Delegates included senior representatives of Islamic financial institutions, accounting and auditing firms, legal firms, universities and higher learning institutions from across the world.

"The Islamic banking industry has grown significantly in recent years and we are also seeing increasing global interest in Islamic finance. The question that now arises is whether Islamic banking regulations and products are keeping pace with the rapid growth of the industry," said Mr. Al Maraj in his opening address.

For their part, Islamic financial institutions (IFIs) need to become bigger in terms of their capital base, to take advantage of the growth opportunities.

Industry-support institutions, such as AAOIFI, also need to play their part in enabling the industry by developing appropriate standards for the industry to follow. Importantly, regulators of IFIs should adopt and implement the standards, to promote harmonisation of Islamic banking practices, globally.

Mr. Al Maraj highlighted a number of issues that need to be addressed. These include:

- The need for IFIs to adhere more closely to the principles and provisions of the Shari'a;
- The need for accounting standards on venture capital, to support the development of small and medium enterprises;
- Development of procedural controls to promote Shari'a-compliance, in order to promote consumer and investor confidence in Islamic banking;
- Expansion of the powers and scope of the regulators, to provide proper oversight of special purpose vehicles (SPVs) by Islamic banks;
- Development of systems of governance and risk management in IFIs.

"The CBB is committed to working with the Islamic finance industry on all of these important issues," said Mr. Al Maraj.

Shaikh Ebrahim bin Khalifa Al Khalifa, Chairman of AAOIFI's Board of Trustees, said the international Islamic finance industry, currently, is composed of a few major components, i.e. Islamic banking, sukuk, funds asset management, and takaful.

Islamic banking is the largest component, with assets currently estimated at US$1.3 trillion, while outstanding sukuk are an estimated US$230 billion, funds assets about US$70 billion, and takaful contributions around US$17 billion.

In recent years, discussions and debates about the further growth of the international Islamic finance industry have highlighted a number of key themes, said Shaikh Ebrahim. These include:

- First, the need for Islamic finance to contribute towards real economic development, including entrepreneurship development;
- Second, the need for Islamic finance to deliver real benefits to the end-consumers, including through Islamic insurance protection; and
- Third, the need for Islamic finance to strengthen operational processes, including Shari'a compliance, risk management, auditing and accounting.

"It has been argued, and well accepted, that Islamic finance must always be linked to economic development. And, one of the most fundamental objectives of economic development is the provision of 'life-sustaining' necessities, including food, shelter, and health care," said Shaikh Ebrahim.

"Another objective is to raise the standard of living of the population in general, which would naturally require expansion of employment and entrepreneurial prospects."

Additionally, economic development also relates to ensuring the expansion of economic activities and creation of diverse economic sectors.

The fundamental objectives of economic development can be achieved through a number of specific aims, such as building hospitals, developing affordable housing, and promoting entrepreneurship.

"It is noteworthy that these fundamental objectives and specific aims of economic development echo the Islamic principles for the advancement of the Ummah and mankind, and for the attainment of social harmony. In addition, the fundamental objectives and specific aims of economic development can also actually be supported by Islamic finance mechanisms," said Shaikh Ebrahim.

Beyond the Islamic banking sector, the Islamic funds or assets management sector also has a critical role to play in terms of economic development, he said.

"Within the Islamic funds management sector, venture capital and private equity investments are perhaps ideally suited to make a real contribution towards economic development, especially relating to entrepreneurship development," said Shaikh Ebrahim.

The real benefits of Islamic finance can also be meaningfully extended to the end-consumers through Islamic insurance. Indeed, the Islamic insurance sector, which is currently considerably smaller than the Islamic banking sector, has much potential to grow.

"In order to support further growth of the Islamic insurance sector, and to ensure real benefits for the end-consumers or policyholders of Islamic insurance, perhaps it will be useful for us to reflect on further innovation of Islamic insurance operations and products," said Shaikh Ebrahim.

Meanwhile, improving operational processes is also key to achieving further growth of the international Islamic finance industry, he said.

"For Islamic finance in general, in order to achieve and support further growth, there is a need to continuously strengthen operational processes as this will help Islamic finance to be efficient in delivering products and services," said Shaikh Ebrahim.

Of paramount importance is to ensure that operational processes support and uphold compliance to Shari'a, including through incorporation of Shari'a principles in Islamic financial contracts and documentation.

In addition, Islamic finance operations also need to pay attention to the dynamics of risk management, auditing, and accounting, in strengthening the operational processes, he concluded.

Islamic Venture Capital – What, Why and How

What do Microsoft, Apple, Google, Skype, Starbucks, Fedex and Electronic Arts have in common? All these recognised global brands are venture capital (VC) funded companies. In its essence, VC is a true Musharaka that is immensely beneficial for entrepreneurs, investors, the economy and society. Speaking at the AAOIFI-World Bank annual conference on Islamic banking, EY Executive Manager Sohaib Umar, a former VC practitioner, presented the key factors necessary to create an enabling environment for VC in a country and made a case for targeted government intervention to kick-start the VC industry in Bahrain and the GCC region.

Venture capital (VC) is financial capital provided to early-stage, high-potential, high-risk, start-up companies. A VC fund makes money by owning equity in the companies it invests in, which usually have a novel technology or business model in high technology industries. VC is a subset of private equity. But, it is not just about providing money. VC brings financial discipline, hands-on management support, industry expertise and business contacts. VC is a thriving business in the US, Europe, Japan and a number of other developed and emerging countries. The US is the biggest and most successful VC market with about US$25 to 30 billion investment annually.

Why venture capital?

A 2002 study commissioned by the National Venture Capital Association, titled, 'Measuring the Importance of Venture Capital and its Benefits to the United States Economy,' analysed all VC-financed companies over the period 1970-2000. The study found that a VC-backed company generates 2x sales and exports, pays 3x more taxes and invests 3x more in R&D than a non VC-backed firm in the US. Moreover, 11 percent of US GDP and one out of every 9 jobs are generated by an originally VC-backed company. VC has played a significant role in creating industry clusters (software, biotechnology, Internet companies, etc.). The study also found a strong correlation between VC activity in a state and its GDP and average annual wages.

Here is an interesting statistic. Since 1995, VC investment in the US has totaled about US$550 billion, funding thousands of companies. The market value of just three of these VC-funded companies – Apple, Google and Microsoft – is twice that much.

Besides financial returns, the VC industry generates numerous economic and social benefits. It results in GDP growth, job creation, technological growth (since high technology industries have been the focus of VC activity), payment of more taxes eventually when the companies become successful and creation of industry clusters. A number of VC-backed companies have gone on to become global players. There are important social returns as well, although these are difficult to quantify.

Most importantly, VC encourages entrepreneurship, transforming the mindset from one of a job seeker to a job provider. It encourages a culture of risk taking, innovation and research. It creates hope, optimism and a positive mindset about the future. Thousands of "rags to riches" success stories exist in the Silicon Valley of the US, thanks to the VC industry.

Islamic VC vs. conventional VC

Unlike most Islamic banking products, VC is Shari'a-compliant in spirit but needs some adjustments to the structure. Specifically, the nature of business and the capital structure have to be Shari'a-compliant (preference shares are typically employed to raise VC money and sometimes interest-based loans are also used). VC is truly aligned with the objectives of Shari'a (Maqasid-e-Shari'a) where the intellectual genius of a person is financially supported in a risk-return sharing structure.

Enabling environment

What does it take to create a thriving VC industry in a country? What are the ingredients of success? The IESE Business School of theUniversity of Navarra, Spain attempted to answer this question by creating a country attractiveness index. The Global Venture Capital and Private Equity Country Attractiveness Index 2012 covers 116 countries and ranks them on six factors: economic activity; depth of capital markets; taxation; investor protection and corporate governance; human and social environment; and entrepreneurial culture and deal opportunities.

No Muslim country is among the top 10 or even 20 countries in the world on VC attractiveness. Malaysia (ranked 25), Saudi Arabia (28) and Turkey (35) score better than others. Israel has the highest VC investment per capita in the world.

Of the eight regions that the study has divided the world into, the Middle East ranks as the 5th most attractive after North America, Australasia, Western Europe and Asia. The areas where the Middle East is lagging significantly behind the highest ranked region, North America, are depth of capital markets and entrepreneurial culture and deal opportunities.

Promoting VC

While the VC model of the US is successful, it is not advisable to simply replicate it in its entirety in the GCC. Some measures that may be considered by Bahrain and the GCC to promote VC are:

- Government should establish VC funds focused on SMEs and specific sectors;
- Government can launch a "matching funds" scheme to encourage global VCs to come to the region;
- Universities should encourage entrepreneurship among students and offer courses on the subject;
- Stock markets should be opened up to international investors, listing major government entities to create depth;
- Government should establish industry clusters and incentivise VC funds to invest;
- Media should highlight role models – individual success stories from the Middle East and GCC region; and
- Islamic banks, pension funds, takaful companies and Awqaf/endowments can provide long term institutional risk capital for VC, which is best undertaken in a non-banking structure.

The views expressed in the article are not necessarily those of the CBB.

Takaful industry urged to address challenges ahead

The Central Bank of Bahrain (CBB) is revising the regulatory framework for takaful (Islamic insurance) business, to further advance the fast-growing industry.

The revisions are also aimed at protecting the interests of all stakeholders, i.e. participants (policyholders), shareholders and takaful operators, said Mr. Abdul Rahman Al Baker, Executive Director, Financial Institutions Supervision, at the CBB.

He was speaking at the second annual Middle East Takaful Forum (METF), held in Bahrain on 7 and 8 October 2013. More than 250 delegates attended the event, held under the patronage of the CBB.

In his opening address, titled 'Reforming the Regulatory Regime – Key Initiatives to Ensure the Long Term Profitability of Takaful Industry in the Middle East', Mr. Al Baker highlighted the tremendous growth of the takaful industry, globally and in Bahrain.

"The global takaful industry has continued to demonstrate strong growth momentum and is increasingly being recognised as one of the major components of the Islamic financial system," he said.

Surging Ahead

Citing the World Islamic Insurance Directory 2012, he said global takaful contributions (premiums) amounted to US$13.7 billion in 2010, a significant increase of 23 percent over the previous year. The GCC market represented 41 percent, or US$5.7 billion, of the total contributions, while contributions from South East Asia stood at US$1.9 billion.

During the past eight years, the takaful industry has recorded growth rates of around 20 percent annually, indicating high growth potential in the years to come, due partly to the current low rate of takaful market penetration.

In Bahrain, the takaful industry is one of the fastest growing segments of the insurance sector. Gross contributions (of takaful firms operating in Bahrain) grew 22 percent to BD53.7 million (US$142.4 million) in 2012, from BD43.9 million (US$116.4 million) in 2011.

"Overall, the takaful market has grown by almost 12 times, in terms of contributions, since 2003," said Mr. Al Baker.

Public Demand

He attributed the growth to the increasing demand for Shari'a-compliant insurance, increasing public awareness about takaful, entry of international players in the local market that offer takaful business and the existence of enabling legislation that promotes the development of takaful in Bahrain.

"Currently, takaful contributions represent almost 22 percent of total gross premiums of the insurance industry in Bahrain," said Mr. Al Baker.

"During the past three years, we have observed positive changes in the mix of takaful contributions, as the family takaful line of business has gained ground. Family takaful constituted 20 percent of total takaful contributions in 2012, compared to 10 percent in 2009."

The growth was not only due to increased public awareness about the importance of family takaful, but also reflected a change in the appetite of clients towards life products that are linked to investment.

As a regulator, the CBB believes in continual enhancement and improvement of its regulatory infrastructure to support the growth and betterment of the industry, said Mr. Al Baker.

"The current work towards revision of the existing takaful model is one step in reaffirming Bahrain as the jurisdiction of choice for all takaful and retakaful companies," he said.

Mr. Al Baker

"The objective of modifying the existing takaful rules is to facilitate faster growth of takaful business in Bahrain while protecting the interest of all stakeholders, vis-à-vis participants, shareholders and takaful operators. It is also expected that the changes to the model will attract new entrants to the market and will foster competition for the betterment of consumers."

The takaful industry has also benefited from the remarkable growth of the Islamic banking industry in the Middle East and North Africa (MENA) region and other parts of the world.

Furthermore, the low penetration of insurance in the Islamic world makes it possible to achieve significant growth for takaful, especially in the MENA region.

Strong economic growth in the region during the past decade, as well as growth of the Muslim population, which represents almost a quarter of the world's population, have helped further enhance growth of the takaful industry.

Mr. Al Baker also pointed to the regulatory frameworks that are tailored to suit takaful business as a critical factor that has helped advance the industry globally.

Challenges Ahead

However, there are several challenges facing the industry that need to be properly addressed in order to further enhance the long term profitability and soundness of the takaful industry, he said.

The first of these is the issue of corporate governance, especially as it relates to participants rights. In contrast to policyholders of conventional mutual insurance firms, who are the owners of the company, participants in general meetings, and have the right to remove the management, takaful policyholders have no such governance structures or rights, although in principle they are exposed to similar insurance risks.

In fact, takaful participants seem to have no more governance rights than the policyholders of a conventional proprietary insurer, and must rely on market competition to get a fair deal and good value for money in their dealings with the takaful operator.

A second challenge is the issue of standardisation of takaful accounting standards and disclosure, especially those related to capital adequacy and solvency, disclosure of Qard Hassan, and regulatory framework, said Mr. Al Baker.

"Another challenge is the lack of human talent that have the necessary exposure and experience in takaful business, as well as those mastering Shari'a compliance," he said.

However, a critical challenge facing the takaful industry is the issue related to the limited availability of the Islamic instruments, such as sukuk, which are the most suitable type of the investment for takaful companies.

Another challenge is with respect to offering micro-takaful to address the needs of lower income individuals, as well as finding the appropriate distribution channels to offer takaful-assurance services through banks.

"The future prospects of the takaful industry will hugely depend on the combined efforts of all relevant parties – regulators, market players and the community at large – to chart a strategic direction for the industry. Collective effort is critical in order to maximise the potential for the takaful industry," said Mr. Al Baker.

GCC region driving global takaful momentum

The takaful industry in the GCC region, including Bahrain, grew by an estimated 15 percent in 2012, with total gross contributions (premiums) amounting to US$7.4 billion, according to a key report published by EY.

The GCC takaful industry generated 67 percent of global gross takaful contributions, which are estimated to have reached US$11 billion in 2012 (from US$9.4 billion in 2011), according to EY's inaugural issue of Global Takaful Insights 2013. Findings from the report were presented at the Middle East Takaful Forum, held in Bahrain on 7 and 8 October 2013 under the patronage of the Central Bank of Bahrain (CBB).

More than 250 senior decision-makers from 100 organisations attended the event, which was held under the theme 'Adapting to Change: Fresh Thinking to Boost the Efficiency, Profitability and Scale of Islamic Cooperative Insurance Players'.

"In recent years, the GCC region continued to record stable industry growth with buoyant performance in some countries," Global Takaful Insights 2013 points out. Saudi cooperatives alone account for approximately 51 percent of the global contributions in 2012.

The growth lever in Saudi Arabia and the UAE (specifically Abu Dhabi) was the implementation of the compulsory National Health Insurance policy.

Globally, the silver lining for the industry is the development of the family takaful sector, which continues to show positive growth momentum.

Key findings of the report are:

- Regional structural differences remain. Key markets continue to offer growth prospects with low market penetration rates, but wider opportunities beckon in emerging markets.
- The Islamic insurance industry, or takaful in most markets, is still in its infancy. Its potential to replace conventional insurance in leading Islamic finance markets is untapped.
- Despite significant regional differences, key markets that are largely underinsured continue to offer growth prospects; these include near developed and emerging rapid growth markets. Meanwhile, regulatory enhancements in rapid growth markets are presenting new opportunities in tapping latent underlying demand and propelling the takaful industry forward so the industry can realise its optimum growth potential.

However, despite the strong performance in 2012, it was a deceleration from the 22 percent annual average growth rate seen from 2007–2011, says the report. Beyond the large markets of Saudi Arabia and Malaysia, most takaful operators are struggling.

It says significant changes in operating models and technology utilisation are the only way to address the inflated, legacy start-up costs that managements of takaful operators are burdened with.

Shareholders, for their part, need to have a clear strategy and capital plan with options ranging from organic and inorganic growth, maintaining and refining segmentation or exit or acquisition strategy.

"And perhaps most importantly, authorities need to simplify regulatory frameworks across borders, as well as support development of larger, regional players. Regulators need to be watchful on how shareholder capital is being eroded. Some need to take a proactive approach to encourage consolidation where within a short time frame, minimum capital requirements will be breached due to ongoing underwriting losses," says the report.

"Unless these issues are addressed as a matter of urgent priority, we believe the takaful industry will find it challenging to maintain its growth trajectory."

Speaking during a session at the Middle East Takaful Forum, Mr. Adeel Mushtaq, Senior Mnager, Audit & Advisory, at KPMG, said takaful is less understood by customers than Islamic banking and most customers are unable to distinguish between a takaful policy and a conventional insurance policy.

He also said that takaful products are inherently expensive compared to conventional ones due to premium nature of service and higher compliance requirements. Hence, replicating conventional products or takafulisation of conventional products may not be sustainable in the long run for the sector.

Mr. Mushtaq said takaful products were initially launched with 'takaful wrapper' with some resemblance to wakala or mudaraba model, together with conventional insurance policy terms and conditions. Although takaful products have come a long way since then, a lot more is needed to be done.

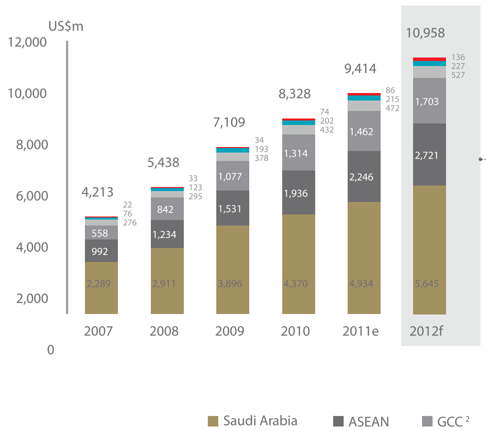
There is also a need to create greater customer awareness about takaful, said Mr Mushtaq, who also chairs an Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI) working group, set up to review guidance and accounting standards for takaful firms.

"I believe review of takaful accounting standards should help companies enhance quality and transparency of entities to support investing in businesses and capital markets," he said.

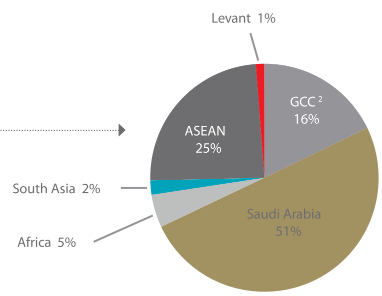
Despite the many challenges the takaful industry faces, he said he is optimistic about the future.

He said takaful firms need to invest in research and development, in understanding Shari'a principles and they need to compete in the development of products that best meet customer needs as well as Shari'a requirements.

Global gross takaful contributions by region, 2007-12f



Share of global gross takaful contributions by region, 2012f



Bahrain insurance market grew by 9% in 2012

The Bahrain insurance market rebounded strongly during 2012, according to the Bahrain Insurance Market Review 2012, issued recently by the Central Bank of Bahrain (CBB).

Total gross premiums underwritten by the domestic insurance industry, including takaful (Islamic insurance) operators, grew to BD239.05 million (US$634.1 million) in 2012, an increase of 9 percent over the previous year's revised figure of BD218.7 million (US$580.1 million).

A significant part of this increase was due to a surge in long-term insurance (life and savings) products, which grew by 14 percent. Gross premiums from this class of business amounted to BD60.2 million in 2012, compared with BD52.6 million in 2011, representing almost 25 percent of the total gross premiums in 2012.

Motor insurance also constituted a significant portion of insurance business written in Bahrain, representing almost 26 percent of the total premiums written in the insurance market in 2012. Gross premiums from motor insurance increased from BD55.6 million in 2011 to BD62 million in 2012, an increase of around 11 percent.

Total assets of insurance and takaful firms (including shareholders and participants funds) in 2012 stood at BD1.6 billion, compared to BD1.4 billion in 2011, an increase of almost 10 percent.

Total net profit of conventional insurance firms amounted to BD47.9 million in 2012, compared to BD54.8 million in 2011, a decrease of 13 percent. Similarly, the underwriting profit decreased by 28 percent to BD14.4 million in 2012, from BD20 million the previous year. On the other hand, net investment income increased by 14 percent to BD25.9 million in 2012, from BD22.7 million in 2011.

For the takaful industry, net investment income of participants funds increased significantly to BD678,000, from BD57,000 in 2011. Participants funds registered a deficit of BD1.9 million in 2012 compared to a deficit of BD5.1 million in 2011. On the other hand, shareholders funds registered losses of BD1.4 million in 2012 compared to a profit of BD1.3 million in 2011.

In a message in the Bahrain Insurance Market Review, Mr. Rasheed Mohammed Al Maraj, Governor of the CBB, noted the strong growth of the insurance industry in 2012.

"Long-term business and motor business have displayed a growth of 14 percent and 11 percent respectively from the year 2011. The growth in medical, fire, property and liability businesses has also been quite strong in 2012 from the previous year. Insurance penetration has increased from 1.99 percent in 2011 to 2.09 percent in 2012," said Mr. Al Maraj.

The takaful industry continues to expand with overall gross contributions (by firms operating in Bahrain) increasing from BD43.9 million in 2011 to BD53.7 million in 2012, a growth of around 22 percent, he said.

"The CBB is currently in the process of enhancing its operational and solvency framework for the takaful and retakaful (Islamic reinsurance) industry in consultation with the industry and Shari'a scholars," said Mr. Al Maraj.

Pointing to key highlights, he said: "I am particularly pleased to mention that the appointed representative scheme (that prescribes minimum requirements for tied agents in dealing with potential policyholders) that was introduced in March 2010 has been a success and the number of appointed representatives, registered under the scheme, by the CBB, has grown to 15 corporates and 41 individuals."

The CBB issued a new legislation on clients' money which came into effect in July 2012. The rules include requirements that must be met by insurance brokers and appointed representatives with regard to holding clients' money.

"The rules are aimed at ensuring proper protection of clients' money to minimise the risk of clients' money being used by insurance brokers and appointed representatives and to prevent the commingling of clients' money with the assets of insurance brokers and appointed representatives," said Mr. Al Maraj.

The CBB, in collaboration with the insurance industry, launched an 'Insurance Day' in March 2012, with the objective of increasing insurance penetration levels in Bahrain by educating the public about insurance services. The event was also held to recognise the achievements and contributions of the market leaders in the industry.

The CBB has set up licensing requirements for Third Party Administrators (TPAs) to safeguard the interest of customers and to ensure the well-being of licensed insurance firms. Licensed TPAs provide requisite protection to licensed insurance firms and customers.

At the end of 2012, Bahrain's domestic insurance market comprised 26 locally incorporated firms and 11 overseas insurance firms (branches of foreign companies) carrying out insurance, reinsurance, takaful, retakaful and captives business in the Kingdom of Bahrain.

Main Highlights

	Gross Premiums			Gross Claims		
BD' 000	2012	2011	% Δ	2012	2011	% Δ
Long-term	60,159	52,591	14%	21,892	20,180	8%
Fire, Property & Liability	41,748	38,645	8%	10,236	12,767	-20%
Miscellaneous Financial Loss	4,464	4,043	10%	1,700	1,190	43%
Marine & Aviation	7,013	7,064	-1%	853	717	19%
Motor	61,994	55,627	11%	54,409	41,855	30%
Engineering	15,188	16,456	-8%	3,467	3,513	-1%
Medical	37,165	34,844	7%	29,321	24,636	19%
Other	11,320	9,387	21%	3,246	1,957	66%
Total	**239,051**	**218,657**	**9%**	**125,124**	**106,815**	**17%**

Note:Certain items have been restated, reclassified or recalculated and have been retrospectively adjusted in 2012.

The locally incorporated firms consisted of 14 conventional insurance firms, seven takaful operators, two reinsurance firms, two retakaful firms and one captive insurance firm, while overseas insurance firms comprised eight conventional insurance firms and three reinsurance firms. In addition, there are a substantial number of firms restricted to business outside Bahrain and insurance ancillary services.

The insurance sector employed a total of 1,659 people in 2012, compared to 1,661 employees in 2011. Of the 2012 insurance sector workforce, 64 percent (or 1,056 people) were Bahrainis.

Promising prospects of Bahrain insurance sector

Bahrain's insurance sector holds tremendous promise for growth, as demonstrated by the industry's strong performance not only during 2012 but also during the past five years, said Mr. Abdul Rahman Al Baker, Executive Director, Financial Institutions Supervision, at the Central Bank of Bahrain (CBB).

In remarks to coincide with the release of the Bahrain Insurance Market Review 2012, Mr. Al Baker said the Kingdom was fast becoming a hub for major regional and international reinsurance and retakaful firms, as evidenced by the increasing number of such firms that are established in the Kingdom.

"We expect the insurance sector to continue its growth in the coming years, mainly due to the increase in public awareness of the importance of insurance products in general, as well as due to the surge in the economic growth of the Kingdom and the soundness of the regulatory and supervisory framework for the insurance sector in Bahrain," he said.

According to CBB data, gross premiums generated in the domestic insurance market amounted to BD239.05 million (US$634.1 million) in 2012, an increase of 9 percent over the previous year's revised figure of BD218.7 million (US$580.1 million).

Following are highlights of the performance of the different classes of business, as provided in the Bahrain Insurance Market Review 2012, which is available on the CBB website at www.cbb.gov.bh:

Long term insurance

Coverage under this class of business includes group life assurance; group credit life assurance; level and decreasing term assurance; unit-linked assurance; participating with profit policies; and children's education policies. This is in addition to the ancillary benefits that are normally attached to such types of life assurance.

During 2012, long-term insurance premiums increased by 14 percent to BD60.2 million, compared with BD52.6 million in 2011. Long-term insurance premiums represented 25 percent of total premiums written by the insurance market in 2012, with a 93 percent retention ratio for the year.

Gross claims increased by around 8 percent to BD21.9 million in 2012, compared to BD20.2 million the previous year. The loss ratio for this class of business was almost 52 percent in 2012 (26 percent in 2011).

Fire, property & liability

Gross premiums generated by this class of business represented around 17 percent of the insurance market in 2012. Fire, property & liability insurance premiums grew by 8 percent to BD41.8 million in 2012, from BD38.7 million in 2011. The retention ratio of this insurance class reached almost 21 percent in 2012 compared to 20 percent in 2011.

Fire, property & liability insurance gross claims decreased by 20 percent to BD10.2 million, compared to BD12.8 million in 2011. The loss ratio for this class of business was almost 29 percent in 2012.

Marine and aviation insurance

Marine and aviation insurance premiums totaled BD7.01 million in 2012, a decrease of 1 percent over the 2011 figure of BD7.06 million. This class of business has a relatively low retention ratio, reflecting a heavy reliance on reinsurance arrangements. In 2012, the retention ratio was around 27 percent (26 percent in 2011).

Gross claims amounted to BD853,000 in 2012, compared to BD717,000 in 2011, with a loss ratio of around 15 percent in 2012.

Motor insurance

Motor insurance business represented a significant portion of insurance business written in Bahrain, representing almost 26 percent of the total gross premiums written in 2012.

Motor insurance premiums grew by 11 percent during 2012 to BD62 million, from BD55.6 million in 2011. Insurance firms continued to retain a high level of motor insurance premiums, with a retention ratio of 90 percent in 2012.

Premiums from comprehensive insurance policies and third party insurance represented 64 percent and 36 percent, respectively, of total motor insurance premiums in 2012.

Gross claims totaled BD54.4 million in 2012, compared to BD41.9 million in 2011, with a loss ratio of around 70 percent in 2012.

Medical insurance

Gross premiums from medical insurance policies amounted to BD37.2 million in 2012, compared to BD34.8 million in 2011, an increase of 7 percent. Medical insurance premiums represented 16 percent of total premiums underwritten in the Bahrain market in 2012. The retention ratio of this class of business was 62 percent in 2012.

Gross claims amounted to BD29.3 million, compared to BD24.6 million in 2011, with a loss ratio of around 78 percent in 2012.

Other classes of insurance

Other classes of insurance business includes engineering, miscellaneous financial loss, and others. Gross premiums from this portfolio increased by 4 percent to BD31 million in 2012, from BD29.9 million in 2011. The premiums represented around 13 percent of the total premiums in 2012.

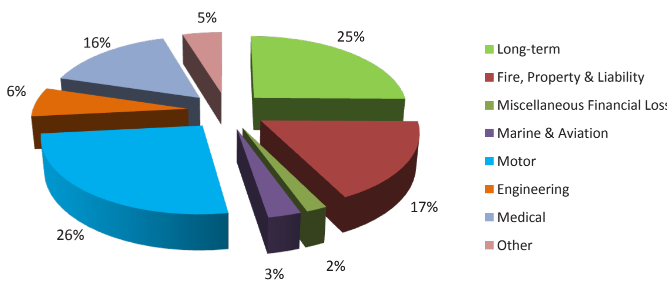
Gross claims amounted to BD8.4 million, up from BD6.7 million the previous year.

Reinsurance

Gross premiums of reinsurance and retakaful firms decreased by 11 percent to BD312.1 million in 2012, from BD349.53 million in 2011. Retakaful business constituted approximately 20 percent of the total reinsurance and retakaful premiums/contributions in 2012. Reinsurance and retakaful firms retained around 83 percent of the gross premiums in 2012, compared to 81 percent in 2011.

Gross claims also decreased, by 19 percent, to BD220.3 million in 2012, from BD272.8 million the previous year.

Gross premiums of firms operating in Bahrain, 2012



Demand emerging for professional liability insurance

The Central Bank of Bahrain (CBB) has developed comprehensive rules governing professional liability insurance, a top CBB official told delegates attending a major insurance seminar.

The CBB rules apply to insurance brokers, insurance consultants, and investment firm licensees that offer professional liability insurance cover. The rules ensure the necessary maintenance of coverage acceptable to the CBB and specify a minimum limit of indemnity for different professionals, said Mr. Abdul Rahman Al Baker, Executive Director, Financial Institutions Supervision, at the CBB.

Recent global and local developments had made the need for insurance against malpractice increasingly important for professionals offering advisory and other services, he said at the Professional Liability Insurance seminar, held in Bahrain on 21 and 22 October 2013.

The event was organised by the General Arab Insurance Federation (GAIF) in cooperation with the Bahrain Insurance Association (BIA) and under the patronage of the CBB. Over 300 delegates attended the two-day event, which was the first of its kind to be held in Bahrain.

Discussions focused on issues related to the development of the professional liability insurance market and the need to address the emerging demand for liability insurance in the region. It also provided an opportunity to explore the importance of professional liability insurance and its role in business continuity and the protection of a company's financial and human capital.

Mr. Al Baker pointed to the importance of professional liability insurance in providing comprehensive protection for firms' assets against claims for financial losses, injury or damage arising from certain acts, errors or omissions in the performance of the professional services. It protects professionals such as accountants, lawyers, medical practitioners, engineers, architects, brokers, bank managers, etc. against negligence and other claims initiated by their clients.

"This kind of insurance is required for professionals who have expertise in a specific area because general liability insurance policies do not offer protection against claims arising out of business or professional practices such as negligence, malpractice or misrepresentation. Some charities and other nonprofits/NGOs are also insured against professional liability," said Mr. Al Baker.

"There is a lot of potential for insurance firms to provide and strengthen professional liability insurance products and to cater them to the needs and requirements of the different industries."

Mr. Abdul Khaliq Al Raouf, Secretary General of GAIF, said insurance premiums in the Arab world totaled US$27 billion in 2012. Of this, the GCC region generated $16.5 billion, which was an increase of 11.7 percent over the previous year.

He urged the insurance industry and regulators to modernise in tune with rapidly changing consumer requirements. Insurance providers should also venture into specialised classes of business, such as professional liability insurance.

Mr. Younis Jamal, Chairman of BIA, said Bahrain needed legislation that regulated professional liability, specifying the nature of such errors.

"Bahrain's insurance market is experiencing all-round growth, reflecting the dynamic nature of the economy," he said.

Nouriel Roubini attends Bahrain forum

Globally famed economist Nouriel Roubini, who predicted the global financial and economic crisis, attended the Interarab Cambist Association's 38th annual conference, held in Bahrain from 14 to 17 November 2013.

The event also featured David Blanchflower, a former member of the Bank of England's Monetary Policy Committee, and Mr. Rasheed Mohammed Al Maraj, Governor of the Central Bank of Bahrain (CBB). The event was sponsored by the Bahrain Economic Development Board (EDB).

Mr. Abdullah Al Ahmadi, Chairman of ICA, said the Bahrain event was a continuation of the ICA's review of the global economic crisis. ICA conferences, held since 2010, have focused on different aspects of the crisis and its aftermath.

"It has now been almost six years since the onset of the global financial turmoil. What many at first saw as a temporary disruption escalated into a systemic shock that is fundamentally reshaping business models and attitudes while redefining economic realities for a whole generation," he said.

The theme for the Bahrain event was 'Adjusting to a new economic order'. A line-up of prominent speakers traced the contours of this new emerging order and discussed its implications for financial services.

The discussions also focused on assessing the challenges of investing successfully in an environment of unprecedented volatility and uncertainty. A special session on Islamic finance highlighted the growth of resilience of this sector during the crisis.

"The ICA annual conference has a longstanding reputation for informed discussion on the global economy," said Mr. Kamal Ahmed, Minister of Transportation and Acting Chief Executive of the EDB.

Bahrain Bourse extends trading hours

Trading hours at Bahrain Bourse (BHB) have been extended by 30 minutes each day. As of 1 December 2013, the trading session starts at 9.30am and ends at 1pm each trading day.

BHB has also reduced the levy on online trading activities, with effect from 28 November 2013.

Brokers' commission on online trading has been set at 0.2 percent of the value of each transaction, while the commission between a client and broker remains negotiable with a maximum of 0.2 percent of the value of the transaction.

The Bourse's commission from brokers for online trading transactions is 15 percent of the broker's commission and is calculated based on the broker's total buy and sell deals on each trading day.

The reduced levy is applicable for two years. The commission on online trading is 30 percent lower than that on conventional trading, and it is expected to maximise returns generated from online trading.

The move is part of the "online trading incentive programme", launched to boost trading activity and enhance liquidity.

New Islamic bank launched in Bahrain

A new Islamic bank, resulting from a merger of three Bahrain-based Islamic banks, was launched in Bahrain.

Ibdar Bank announced on 2 December 2013 that it was open for business. The new entity, which has resulted from the merger of Capital Management House, Capivest and Elaf Bank, has a paid up capital of US$300 million, $329 million in equity and assets of $360 million.

The launch follows a period of consolidation and the integration of the assets, resources and operations of the three merged banks.

"Leveraging a 30-year combined track record and the complementary strengths of the merged entities, Ibdar will engage in private equity, capital markets and real estate," said Mr. Paul Mercer, Chairman of Ibdar Bank.

"The merger, which has already provided significant value to shareholders, has brought forth a more competitive institution with the foundations for leadership in Islamic banking."

He said the bank has a strong deal pipeline. Areas of focus are aviation, maritime, infrastructure, oil and gas, and real estate, among others.

"Ibdar's strategy also calls for the rationalisation of its existing portfolio across these sectors and others," he said.

The bank is working to bolster and add value to core assets within the portfolio whilst also preparing for the strategic exit of non-core businesses and investments.

Geographically, the bank's focus will be on the GCC and the wider Middle East and North Africa region, as well as Turkey and Southeast Asia. It will also consider select opportunities in developed markets. Ibdar is not leveraged and will retain Elaf Bank's licence in Malaysia to support its geographical scope.

"With significantly enhanced investment and underwriting capacity, the bank is well-positioned to undertake deals and to more effectively participate in capital markets," said Mr. Mercer.

The three-way merger of Ibdar's legacy banks, effected in January 2013, was amongst the first mergers of banks to take place in Bahrain.

In September, Islamic lender Al Salam Bank said it had agreed to merge with fellow Bahraini lender BMI Bank, an affiliate of Oman's Bank Muscat, through a share swap.

Khaleeji Commercial Bank, 47 percent owned by Gulf Finance House, said in June it was evaluating a potential merger with local lender Bank Al Khair and in March, National Bank of Bahrain and a local pension fund bought a 51.6 percent stake in Bahrain Islamic Bank from Kuwait's Investment Dar in a deal worth around US$92.6 million.

The consolidation of Bahrain's banking industry is being encouraged by the Central bank of Bahrain (CBB).

Perpetual sukuk holds promise

The Waqf Fund, a Bahrain-based special fund to support Islamic finance training, education and research, hosted its third Shari'a Scholar session, featuring leading Islamic finance scholar Shaikh Nizam Yaquby.

The topic under discussion was "Perpetual Sukuk – Shari'a Considerations". Over 25 Shari'a practitioners from 13 financial institutions attended the session, which was held on 13 October at the premises of the Central Bank of Bahrain (CBB).

Shaikh Nizam explained that the concept of perpetual sukuk, or no redemption bonds, is very old in the conventional financial industry – dating back to 1700s when the UK government introduced them. Due to their attractive features (low rate of interest, non-dilutive, no redemption, etc.) they have been popular amongst issuers.

With the oncoming of Basel III, which classifies perpetual bonds/sukuk as Tier 1 capital, Islamic banks have an incentive to issue perpetual sukuk.

From a Shari'a-compliance perspective, Shaikh Nizam hailed the financial innovation as a welcome development for Islamic banks, large corporates and governments interested to finance infrastructure projects. This is because of risk participation and no purchase undertaking (which has been criticised by scholars as a questionable practice).

He also identified some common concerns about the structure of perpetual sukuk but concluded that those can be easily addressed.

Bahrain is tops in economic freedom in Arab world

Bahrain has topped the list of the most economically free nations in the Arab world.

According to the annual Economic Freedom of the Arab World report, published by the Fraser Institute, an independent Canadian public policy think tank, the UAE and Jordan shared first place with Bahrain.

The report is published in partnership with the Egypt-based Friedrich Naumann Foundation for Liberty and the International Research Foundation of Oman.

It focuses on the role of economic freedom in increasing prosperity, creating jobs and reducing poverty. The report compares and ranks Arab nations in five areas of economic freedom: size of government, including expenditures, taxes, and enterprises; commercial and economic law and security of property rights; access to sound money; freedom to trade internationally; and regulation of credit, labour, and business.

It highlights Bahrain's role as a leading financial centre, and the Kingdom scores particularly high in freedom to trade internationally and in the regulation of labour, credit and business.

"Bahrain's ranking reflects the Kingdom's commitment to maintain a liberal business environment and strengthen its core business fundamentals, offering an attractive base for accessing the wider GCC market," said Mr. Kamal Ahmed, Minister of Transportation and Acting Chief Executive of the Bahrain Economic Development Board.

With a mature, well-established business environment and a trusted and transparent legal and regulatory environment, Bahrain is uniquely positioned as the natural gateway to the GCC market, with a combined GDP of over US$1.5 trillion.

Bahrain is committed to sustaining and strengthening its core business fundamentals: a highly skilled workforce, stable and transparent regulation, an open business environment and sustainable growth.

Financial Sector Fact Sheet

Regulator: Central Bank of Bahrain
Financial Institutions: 402 (Nov 2013)
Financial Sector Workforce: 14,009 (2012)
Bahraini nationals 9,253 (66%)
Foreign nationals 4,756 (34 %)

Key Economic Indicators

GDP (Current) US$30.4 billion (2012)
Growth 4.1% (2012)
GDP (Constant) US$27.1 billion (2012)
Growth 3.5% (2012)

Financial Sector contribution to GDP 16.8%
Sovereign Rating
BBB (S&P Dec 2011) with stable outlook
BBB (Fitch Dec 2011) with stable outlook
Population 1,195,020 (2011)

Banking Sector

Assets US$186.1 billion (Oct 2013)
No. of institutions 111 (Nov 2013)
Retail banks 28
- Locally incorporated 13
- Branches of foreign banks 15

Wholesale Banks 71
Representative Offices 11
Bank Society 1

Islamic Banks (included in left):
No. of banks 24 (Nov 2013)
Assets US$23.1 billion (Oct 2013)

Insurance Sector

Total No. of Insurance Companies & Organisations Authorised in Bahrain 159 (Nov 2013) * excluding Appointed Representative
Domestic market
Gross premiums US$615 million (December 2012)
No. of insurance firms 36
- Locally incorporated insurance firms 25
  - Takaful & Retakaful Firms (included above) 8
  - Captives (locally incorporated, included above) 1
- Overseas insurance firms 11

Insurance Brokers 31
Insurance Consultants 5
Insurance Managers 2

Representative Offices 5
Loss Adjusters 11
Actuaries 31
Insurance Ancillary Services 6
Insurance Pools & Syndicates 2
Insurance Society 1
Insurance Licensees Restricted: 29
- Insurance Firms restricted: 23
- Insurance Brokers restricted: 4
- Insurance Consultants restricted: 2

Insurance Appointed Representative 17
- Corporate 12
- Individual 5

Investment Business Firms

No. of firms 57 (Nov 2013)
No. of Investment Business firms 49 (Nov 2013)

Representative Offices 7
Bahrain Asset Manager Association 1

Specialised Licensees

Total no. of institutions 47 (Nov 2013)
Money Changers 18
Fund Administrators License 1
Registrar License 1
Registered Administrators 1

Financing Companies 8
Microfinance Institution 2
Trust Service Providers 3
Ancillary services 12
Registered Professional Body 1

Capital Markets

Market Capitalisation US$17.88 billion (Nov 2013)
No. of firms 28 (Nov 2013)
Licensed Exchanges 2
Licensed Clearing, Settlement and Central Depository Systems 1

Licensed Securities Brokers 4
Licensed Securities Dealers 1
Licensed Securities Clearing Member 7
Licensed Securities Broker Dealers 13

Funds Industry

Authorised Funds 2,833 (Nov 2013)
NAV US$7.46 billion (June 2013)

Local Funds (CIUs) 103
- NAV US$4.49 billion (June 2013)
- Conventional-Local 57
- Islamic-Local 46
- Locally Incorporated (PIUs) 1

Foreign Funds-Offshore 2,729 (Nov 2013)