

IDB PRIZE LECTURE

Challenges of Regulation and Supervision of Islamic Banks

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Abstract

The Lecture argues that Islamic bank should be supervised using a cross-sectoral approach. However, whilst such an approach appears to suit the investment and banking services offered by Islamic banks, the Lecture highlights the challenges faced by the IFSB in implementing this approach over the eight years of my work as its Secretary-General. The Lecture further highlights the implications of these challenges for the future development of the regulation and supervision of Islamic banks. In particular, it draws attention to the special situation of Unrestricted Profit Sharing Investment Accounts, as a type of investment product used as a Shari'ah-compliant substitute for conventional deposit accounts, a banking product, and the resultant regulatory issues.

Policy Dialogue on Monetary Policy in Islamic Perspective

One of the very important roles that the government in any country needs to play is to monitor the movement of macroeconomic variables, such as inflation, growth, employment and to try to improve them by using efficient policy tools. These policy tools include fiscal and monetary policies, direct control of prices, incomes and taxation, etc.

In conventional economics, interest-based instruments are widely used to realize the objectives of these macroeconomic policies. However, according to the basic fundamentals of Islamic economics that are based on the Islamic Shari'ah rules,

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Muslims are not allowed to use interest-based instruments for monetary policy. Hence many Muslim scholars have suggested profit-based instruments or credit ceilings should replace interest-based instruments in Islamic economic framework. While some Muslim countries try to apply Islamic Monetary policy that is based on either profit-based instruments or credit ceiling instruments, the gap between theory and practices is still very wide. IRTI, by conducting policy dialogues in member countries, tries to find way and means to bridge this gap between theory and practice in Islamic monetary policy. IRTI invites a group of experts and policy makers from different Muslim countries to contribute to dialogue, discuss thoroughly the constraints, the opportunities and the challenges of applying Islamic monetary policy by referring to specific Islamic countries as cases studies, in line with its objective of facilitating dialogue among major stakeholders on important policy issues, IRTI organized a policy dialogues on Monetary Policy in Islamic Perspective in Iran involving central bankers from Iran, Pakistan and Sudan during 1432H.

The Monetary and Banking Research Academy (MBRA) of the Central Bank of Iran (CBI) played an instrumental role as a collaborating institution in arranging the programme. More than 300 participants, including government officials, financial institutions managers and university professors attended the workshop.

The two-days workshop comprising four sessions each day, resulted in thorough discussion of the issues. In addition to the theoretical papers which covered theory of Islamic and conventional monetary policy, three-country cases in Islamic monetary policy of Iran, Pakistan and Sudan were presented. The second day witnessed a presentation on the role of the IDB in promoting Islamic Monetary Policy in Muslim countries.

(Extracted from IRTI Annual Report 1432H)

International Conference on Inclusive Islamic Financial Sector Development, Khartoum, Sudan, 9-11 October 2011

Three days international Conference on Inclusive Islamic Financial Sector Development: Enhancing Financial Services for Regional Microfinance was held in the Sudan Academy for Banking and Financial Science (SABFS). The conference was jointly organized by IRTI- a member of the IDB Group, and SABFS. In three days, 25 papers were presented, covering different areas on microfinance including case studies and experiences of microfinance in different countries, performance of MFIs, policies and regulatory framework of

microfinance. More than 150 participants including foreign experts, leaders of the banking and financial industry in Sudan, the academicians, practitioners, stakeholders and students regularly attended three-day conference. A panel session was held on the third day, the last day, of the conference. It was addressed by the experts in microfinance who highlighted the various issues related to three days' discussions on microfinance.

The focus of the discussion has been on importance of MFIs in poverty alleviation, social development, performance of MFIs, capacity building of the stakeholders and the facilitative role of the governments for the development and strengthening of MFIs. The conference discussed the diversification in microfinance products that suit the beneficiaries in each region of different countries. It has been stressed that central banks may allocate at least 12 percent of their funds for the MFIs. The conference recommended that there is a need to learn from the best practices and experiences of microfinance in other countries, particularly the implementation of Profit-Loss Sharing schemes, poverty alleviation and youth employment. The creation of an efficient and effective Islamic microfinance business model was highly recommended. Microfinance institutions should ensure successful outreach policies. It is highly necessary to establish special credit rating agencies for microfinance activities and to set up Sharīah rating agencies. Governments should enhance microfinance activities to create more jobs and employment opportunities, especially among the poor segments of the society.

Orientation Seminar on Islamic Finance and Workshop on Morality and Finance in UK, 4-6 October, 2011

Two events (1) an Orientation Seminar on Islamic Finance and (ii) a Research Workshop on Morality and Economics were held at the Markfield Institute of Higher Education (MIHE), The Islamic Foundation, UK during 4-6 October, 2011.

The Orientation Seminar was designed to disseminate knowledge on important issues of Islamic finance. For example, the rationale behind investing in Shari'ah compliant funds, issuance of *sukūk* and operations of sovereign funds etc. The Research Workshop on Morality and Finance was held with the purpose to sensitize graduate students and researchers to the new area integrating morality and values with economics and finance.

These two events were jointly organized by MIHE and IRTI, and attended by over 70 participants. The role of moral and ethical behavior has acquired greater

focus among the financial institutions after the global financial crises. This workshop addressed the foundations of Islamic finance and showed how the macro and micro principles of Islamic finance provide a moral framework and helps him creating cooperation and healthy competition. Scholars from Durham University, Aston Business School, University of Stockholm, Business School, University of Hull, Markfield Institute of Higher Education and IRTI presented their views.

**Training and Orientation Program on Islamic Finance
in Astana, Kazakhstan, July, 2011**

A ten day program was organized by IRTI and the local counterpart organization to train teachers of Islamic economics and finance as well as the bankers on the theory and practice of Islamic finance.

The Training Division and the Research Division of IRTI both contributed by providing program design and speakers. The program was attended by more than 50 participants from universities, government and financial sector.