

ISLAMIC FINANCE INDUSTRY OUTPERFORMS IN 2013

The global Islamic finance industry has sustained impressive double-digit growth in 2013 despite challenging global economic conditions, such as the emerging markets funds outflows in the light of tapering in US quantitative easing programme, the US public sector shutdown over its budget deficit fiscal cliff, as well as slow recovery in the Eurozone.

15 January 2014

2013: Another profound year for the global Islamic finance industry

Despite the global economic and financial challenges, Islamic finance has once again demonstrated its resilience by continuing to grow at double-digit growth rates across all sectors of banking, sukuk, funds and takaful to reach an estimated USD1.8tln in assets as at end-2013, reflecting an impressive y-o-y growth of 18.6%¹.

The global Islamic financial industry has sustained its tremendous growth momentum in 2013 to reach an estimated USD1.8tln in assets as at end-December 2013, witnessing double-digit growth rates across all sectors

of the Islamic financial industry. Following 2013's profound performance, the growth of total Islamic financial assets has managed to achieve a CAGR of 17.07% during 2009-2013. Spearheading this impressive growth has been the Islamic banking sector which continues to dominate the global portfolio of Islamic financial assets with a 79.8% contribution to total assets in 2013. The amounts of new sukuk issuances in 2013 once again surpassed the USD100bln mark, although the volume of issuances fell 8.77% short of the 2012's record amount. The funds and takaful sectors also posted double digit growth rates of 10.2% and 15.5% respectively in 2013, although in recent years, both sectors have been experiencing lower y-o-y growth rates².

Global Islamic Finance Assets by Segment (2013E)

Source: IFIS, Zawya, Bloomberg, KFH Research



¹ KFH Research Limited

² ibid

Global Islamic Banking “2013 Review”

The Islamic banking sector is tipped to be the fastest growing segment for the year 2013 with forecasts indicating Islamic banking assets has surpassed USD1.4trn as at end-Dec 2013. Based on these estimates, the Islamic banking sector records a y-o-y growth of just over 19%, slightly edging out the sukuk outstanding growth rate for 2013. Driving the tremendous growth in Islamic banking assets

during 2013 are jurisdictions in MENA and Asia particularly Saudi Arabia, Malaysia, United Arab Emirates, Kuwait, Qatar, Indonesia, Pakistan and Turkey where Islamic banking institutions have seen remarkable growth rates surpassing conventional banks in recent years. In terms of key markets, Iran, Saudi Arabia and Malaysia remain the top three jurisdictions for Islamic banking assets in 2013.

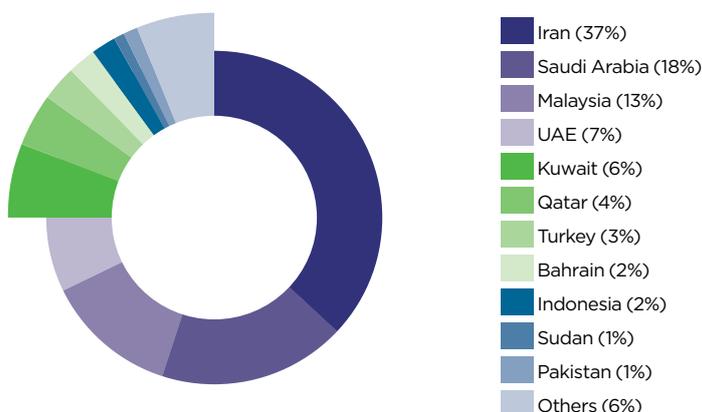
Malaysia Islamic Banking Market Snapshot - 2013

The Malaysian Islamic banking sector continues to outperform the conventional banking sector with average annual asset growth rate of 18.6% during 2008-2012, in comparison to the conventional banking growth of 9.3% during the same period. During 11M13, the Islamic banking assets have already grown at a rate of 14.5% based on latest statistics available. Excluding the Development Financial Institutions (DFIs), the Islamic banking assets in Malaysia are over USD132bln as at end Nov-13.

On a global level, Malaysian Islamic banking assets (including DFIs) represent 13% share of the total global Islamic banking assets, behind only to Iran and Saudi Arabia. Regionally, Malaysian Islamic banking assets represent over 85% of the total Islamic banking industry in Southeast Asia.

Domicile of Islamic Banking Assets (1H13)

Source: Central Banks, KFH Research

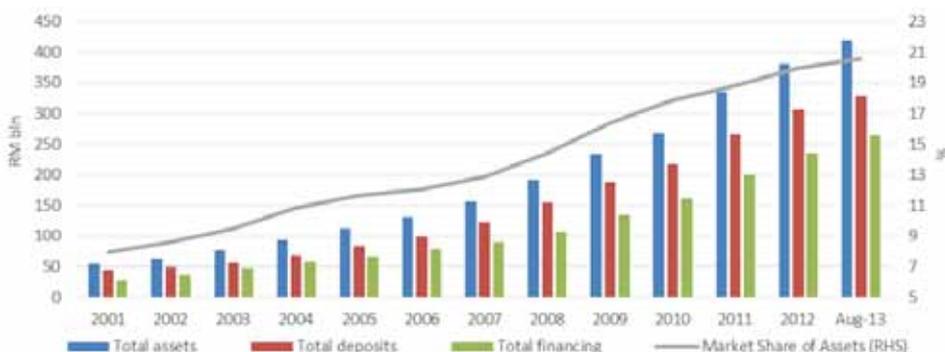


Malaysia Islamic Banking System* - Key Financials

Source: BNM Monthly Statistical Bulletin, KFH Research

2008-2012 Banking Assets* Growth
 Islamic Banking = 18.6%
 Conventional Banking = 9.3%

*Excluding DFIs



Global Sukuk Market “2013 Review”

The global sukuk industry once again surpassed the USD100bln mark in terms of new issuances during the year 2013. Having witnessed a slowdown in the second half of 2013, particularly in 3Q, the global sukuk issuances closed with a total of USD119.71bln in issuances, falling 8.77% short of the record issuances amount of USD131.2bln in 2012. The slowdown in global sukuk issuances were largely driven by the indication of a cut-back in the US monthly stimulus program by the Federal Reserve (Fed) in May-2013. This announcement by the Fed had a profound effect on the global bond market which saw prices of fixed-income instruments (including

sukuk) to fall sharply as fears spread that the Fed’s reduction in bond purchases would move investors out of the safe asset to higher yielding assets on an improving US economy. In particular, the hard hit was the corporate sukuk market in the 3Q immediately after Fed’s announcement, which fell to their lowest level in two years with issuances at a mere USD2.68bln as compared to USD8.1bln and USD7.4bln issuances in 1Q13 and 2Q13 respectively. Nonetheless, sovereign sukuk issuances sustained the momentum throughout 2013 steering the global sukuk outstanding level to expand by 17.8% y-o-y to close at USD270.2bln as at end-2013.³

Malaysia Sukuk Market Snapshot - 2013

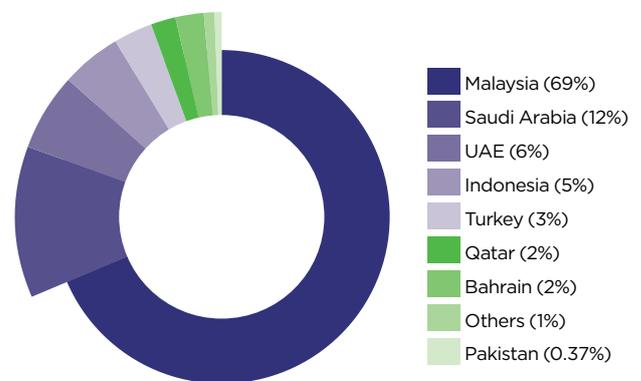
Malaysia’s sukuk market is recognised as the most vibrant and active in the world. During 2013, Malaysia maintained its top position as the largest sukuk issuer with a 69% share of total issuances in 2013 amounting to almost USD82.4bln.

By currency, Malaysian Ringgit sustained its domination representing 67% of total sukuk issuances for the year 2013 worth USD80.4bln.

By structure, Murabahah is the most popular instrument in Malaysia representing 75% or USD61.8bln of total Malaysian sukuk issuances.

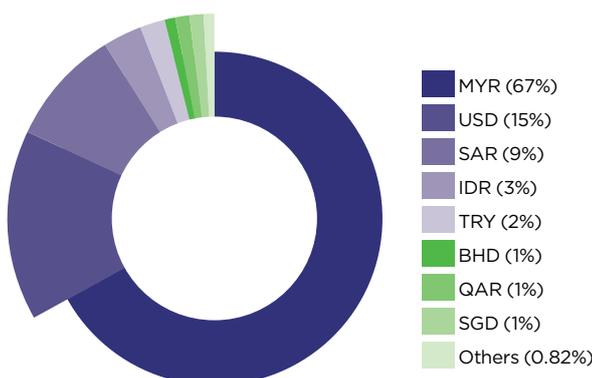
Global Sukuk Issuances by Domicile (2013)

Source: IFIS, Zawya, Bloomberg KFH Research



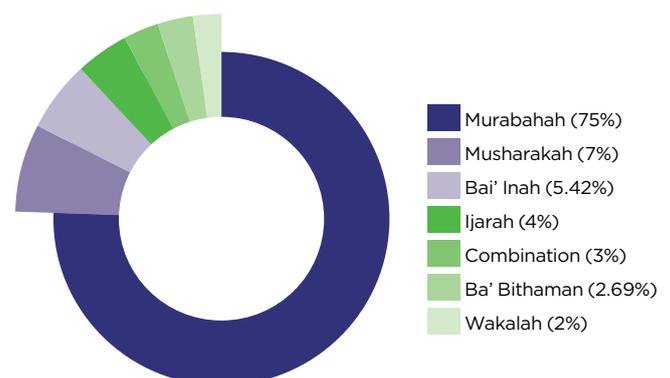
Global Sukuk Issuances by Currency (2013)

Source: IFIS, Zawya, Bloomberg KFH Research



Sukuk Issuances by Structure - Malaysia (2013)

Source: IFIS, Zawya, Bloomberg KFH Research



Global Islamic Funds Industry “2013 Review”

The global Islamic funds sector witnessed a 10.2% y-o-y expansion in assets under management (AuM) to close at an estimated USD73.7bln as at 9th December 2013. Post the global financial crisis, the Islamic funds sector had witnessed subdued growth on the back of falling prices and stagnant volume in the global equity markets. However, improved global economic outlook and growing demand

for Shariah-compliant investment avenues contributed towards the year 2013 y-o-y growth in Islamic funds AuM which comes at a rate higher than the CAGR of 7.86% for the years 2009-2013. The number of funds in this sector have also grown four-folds from approximately 285 funds in 2004 to an estimated 1,053 funds as at end-2013.⁴

Malaysia Islamic Funds Market Snapshot - 2013

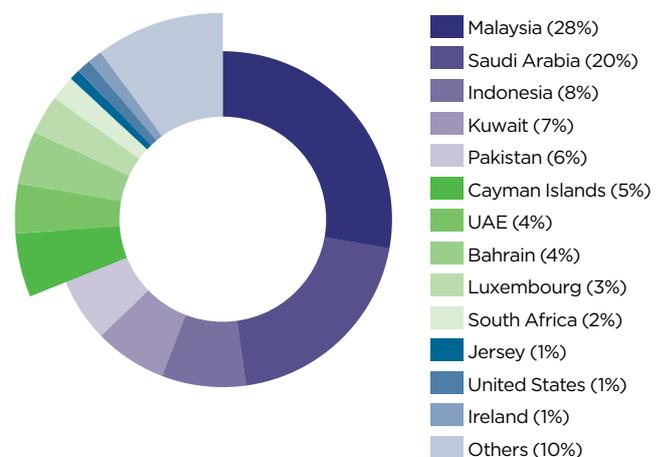
In terms of number of funds by domicile, Malaysia retains the top position in 2013 with nearly 28% of the total number of Islamic funds domiciled in Malaysia as at 9th December 2013.

In terms of Islamic funds assets by domicile, Malaysia represents the second largest Islamic funds markets having total Islamic funds AuM of USD16.3bln or 22% of the total industry AuM as at 9th December 2013.

In terms of geographical focus of Islamic funds assets, Malaysia represents the largest individual country focus market with almost 17% of Islamic funds having geographical focus on Malaysia.

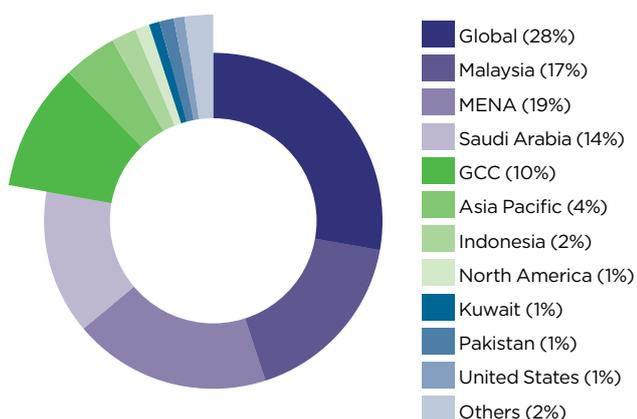
Global Number of Islamic funds - by Domicile (2013)

Source: IFIS, Zawya, Bloomberg KFH Research



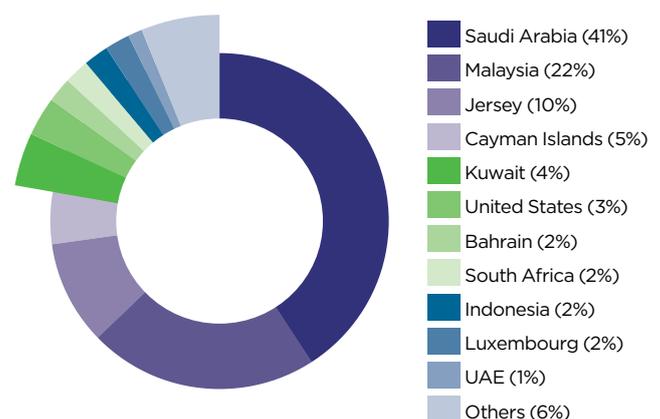
Islamic Funds Assets by Geo Focus (2013)

Source: IFIS, Zawya, Bloomberg KFH Research



Global Islamic Funds Assets by Domicile (2013)

Source: Bloomberg, Eurekahedge, KFH Research



Global Takaful Industry “2013 Review”

The global takaful industry experienced a strong y-o-y growth rate of over 15% to reach an estimated USD19.87bln in gross takaful contributions as at end-2013. Nonetheless, in spite of the impressive double digit growth rates in recent years, the global takaful industry remains a small segment representing a 1.13% share of the global Islamic financial industry as estimated at end-2013. The stagnancy in the share of the takaful segment in the global Islamic finance industry during the last few years is a result of comparatively faster growth in other

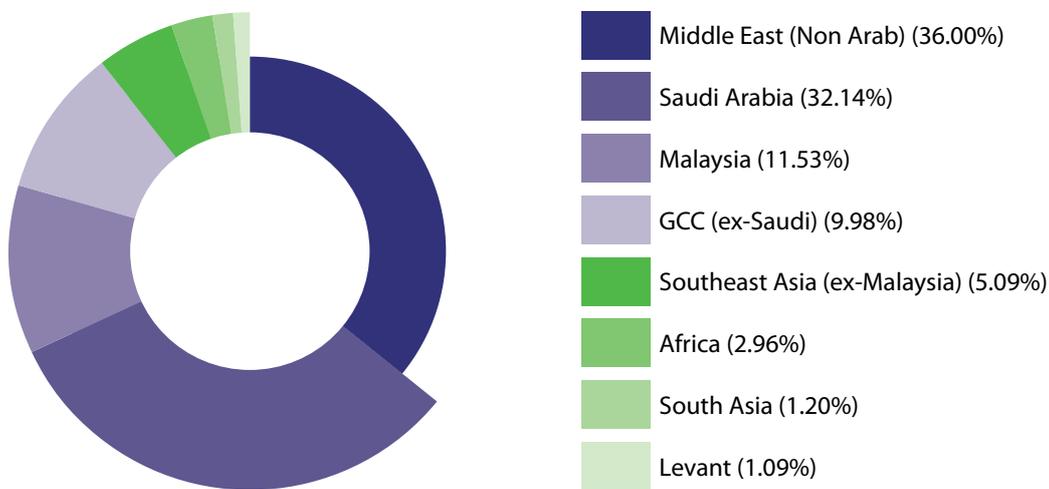
Islamic financial sectors such as banking and sukuk. Notwithstanding this, the growth in the other Islamic financial sectors are bound to spur expansion in the takaful sector as a holistic Shariah-compliant system entails use of Islamic financial products including takaful. Therefore, with the double digit growth rates of Islamic financing of various projects through Islamic banking and capital markets, takaful sector also has potentials to expand by providing the necessary coverage for the projects utilising Islamic financing.⁵

Malaysia Takaful Market Snapshot - 2013

Malaysia is the second largest takaful market (excluding Iran) in terms of gross takaful contributions, estimated at over USD2.2bln as at end-2013. The takaful market in Malaysia, which is served by 11 takaful operators, has maintained its growth momentum in recent years at a CAGR of 18.69% (2009-2012), mainly on account of an increasing awareness among the demographics regarding the benefits of insurance products that have helped boost demand for the sector’s products in the country.

Global Gross Takaful Contributions by Region (2013F)

Source: World Islamic Insurance Directory, EY, KFH Research



⁵ KFH Research Limited

2014 Prospects

The global Islamic finance industry has managed to sustain its impressive double-digit growth rates in 2013 despite various challenging economic conditions such as the emerging markets funds outflows in the light of tapering in US quantitative easing programme, the US public sector shutdown over its budget deficit fiscal cliff, as well as slow recovery in the Eurozone. Moving forward, the Islamic financial industry is expected to continue its robust performance in 2014 particularly with more jurisdictions penetrating into the Islamic financial industry.

By the end of the year 2014, the Islamic financial industry is expected to surpass the USD2tn mark⁶. Islamic banks financing growth remains robust and positive, supported by aggressive government spending on infrastructure projects and domestic consumption. Mega infrastructure projects in GCC countries and Asia are poised for Islamic banks to tap into these investment opportunities. Sukuk market will also benefit from these trends. The sukuk segment is expected to experience an increase in momentum in 2014 as there are a number of jurisdictions and entities looking to tap into the global pool of Shariah compliant funds through sukuk for their various economic, business and infrastructural spending needs. Particularly for sovereign sukuk issuances, 2014 will witness a number of debut issuances including from the United Kingdom, South Africa, Oman and Senegal among others. The new participations in the Islamic financial system, e.g. Oman, Philippines and China, and potential expansion in niche markets to the likes of Sri Lanka, Maldives, Singapore, United Kingdom, Hong Kong, Azerbaijan, Kazakhstan and Afghanistan are bound to spur growth in all sectors of the Islamic financial industry in 2014. Notably, United Kingdom's efforts to issue sovereign sukuk and to list an Islamic index in the London Stock Exchange are likely to encourage

other European nations to follow suit including France, Ireland and Germany, among others. Luxembourg is already known to soon realise the launch of EU's first Islamic bank in 2014 known as Eurisbank. From the demand side, the rise in the number of HNWI's (having investable assets over USD1mln) as well as general increase in the affluence of the population in key Islamic finance markets represents further potential for the Islamic financial industry as whole to expand its market base.

The development of sukuk and money markets are also expected to contribute to the growth of Islamic funds industry. Furthermore, the global Islamic funds industry is expected to benefit from the steady global economic recovery which will bolster investor confidence and performance of underlying invested assets. Growing number of new Islamic financial institutions e.g. Islamic pension funds, takaful companies and Islamic trusts (or awqaf), as seen in recent years, would naturally create greater demand for Islamic investments including funds. Attracting institutional investors, therefore, is of the essence for active progression of the Islamic funds sector. The global takaful industry is expected to have surpassed the USD20bln mark with gross takaful contributions forecasted to range between USD22bln and USD23bln as at end-December. Moving forward, the growth opportunities for the global takaful industry in 2014 and beyond are bright on the backs of several economic, financial and socio-demographic trends.

These prospects, coupled with growing preferences for Shariah-compliant financial solutions and instrumental support by various multilateral organisations and regulatory bodies, are among the key drivers of the Islamic finance industry in 2014.

⁶ KFH Research Limited

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