

Islamic Asset Management Dr Natalie Schoon, CFA

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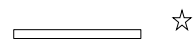


Agenda

- Islamic asset management marketplace
- Sharia'a compliance
- Asset management processes
- Types of funds

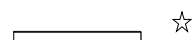


Islamic asset management market place



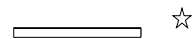
Investment

- Purchasing any form of property and keeping it for a relatively long period to generate a return
- Often offered via asset and fund management vehicles
- Investor Objectives
 - Capital preservation
 - Maximisation of yield
 - Ensuring balance between liquidity and profitability

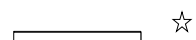
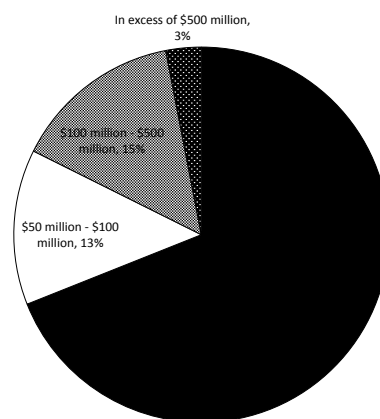


AAOIFI definition of a fund

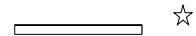
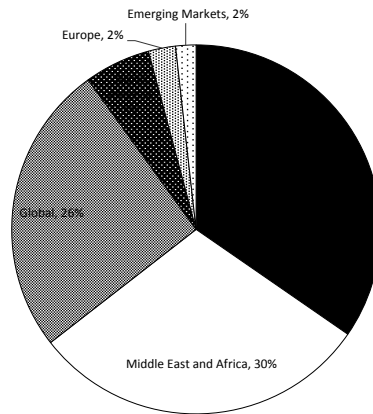
'Funds are investment vehicles, which are financially independent of the institutions that establish them. Funds take the form of equal participating shares/units, which represent the shareholders'/unitholders' share of the assets, and entitlements to profits or losses. The funds are managed on the basis of either a mudaraba or wakala contract.' (AAOIFI Financial Accounting Standard 14, appendix B)



Assets under management



Geographical spread

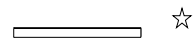


Sharia'a compliance

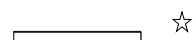
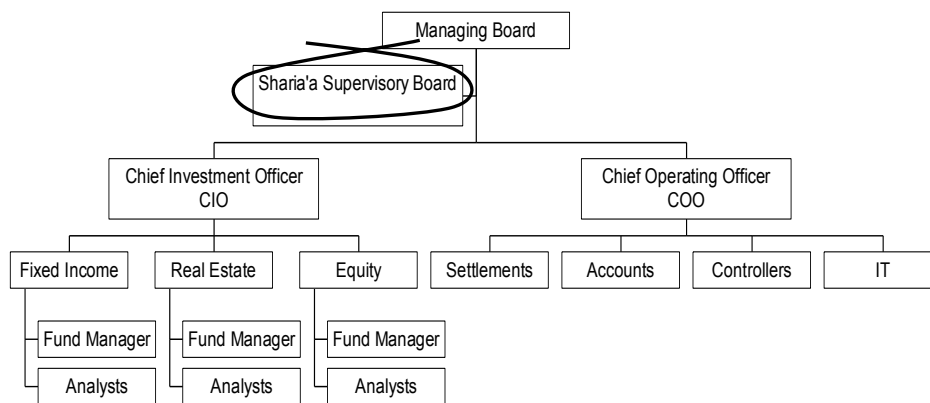


Sharia'a compliance

- How is it achieved?
- Approval process?
- Sharia'a Board?
- Role and responsibilities
- Non-compliant investments

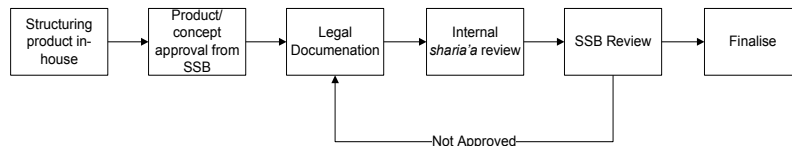


Islamic asset management structure



Sharia'a Supervisory Board (SSB)

- Typically 3 – 5 members, meeting (semi) annually
- Responsible for Sharia'a compliance at inception (investment mandate) and on-going
- Approval process:



- Non-compliance of investments



Screening Criteria

Industry screen

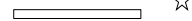
- Conventional banking and insurance
- Alcohol
- Pork
- Defence
- Gambling
- Adult Entertainment
- Other non accepted activities as defined by the *Sharia'a* Board

Financial Screen

- Total Debt / Total Market Cap < 30%
- (Cash + interest bearing deposits) / Total Market Cap < 30%
- (Interest + non-compliant income) / Total Revenue < 5%

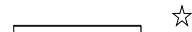


Asset management processes



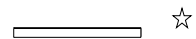
Asset management processes

- Subscriptions, redemptions and switches
- Payment and receipts
- Settlement, accounting and reporting
- NAV calculations
- Prospecting and marketing
- Liquidity and risk management



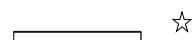
Fund management structures

- *Mudaraba*
 - Investor is *rab al mal*
 - Fund manager is *mudarib*
 - Profits are shared, losses distributed
- *Wakala*
 - Investor is *rab al mal*
 - Fund manager is *wakil*
 - Fund manager is paid a fee

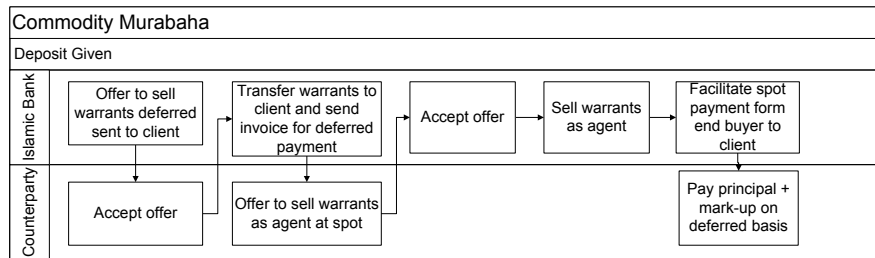


Liquidity

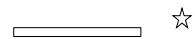
- Why liquidity?
- Which instruments?
- How to manage?



Interbank liquidity (commodity *murabaha* and *tawarruq*)



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Types of funds

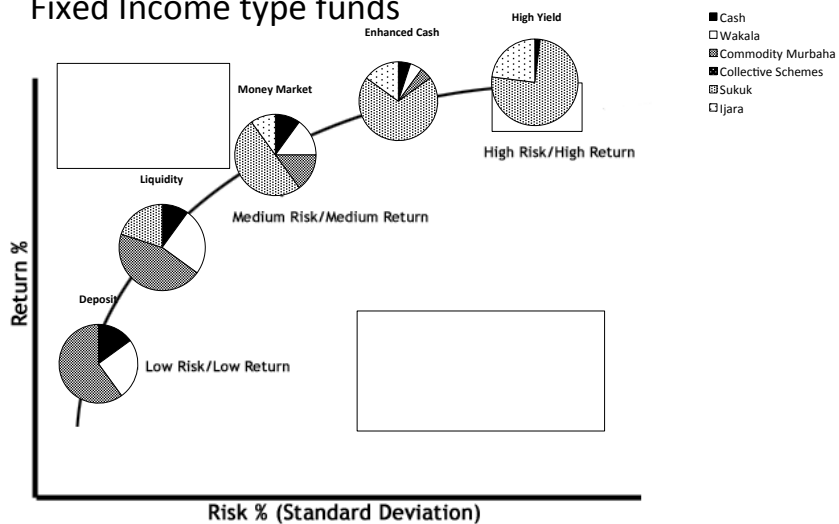


Types of funds

- Range?
- Instruments?
- Challenges?



Fixed Income type funds

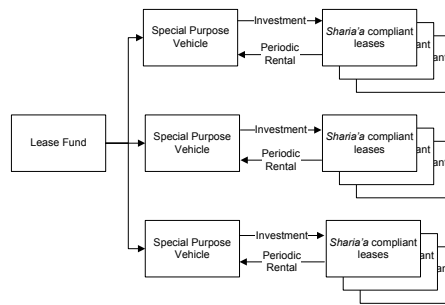


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Lease funds

- Higher risk, higher return potential
- Lessor owns the asset
- No residual risk on the asset
- Daily amortisations or accruals



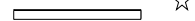
Commodity funds

- Commodity must meet acceptability criteria
- Seller must have physical or constructive possession
- Commodity must be owned by the fund
- No forward selling or buying
- Sale price must be determined with certainty



Real Estate funds

- Commercial and residential real estate
- Income from rental and increase in value
- Non-compliant use may lead to disposal



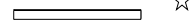
Equity funds

- Private Equity
- Public Equity
- Equity Index
- Exchange Traded Funds



Private equity

- Screening criteria apply
- *Sharia'a* compliance possibly easier to achieve
- Venture capital
- Direct investments
- Diversification



Public equity

- Screening criteria apply
- *Sharia'a* compliance less easy to achieve
- Monitoring of non-compliance
- Purification of non-compliant income



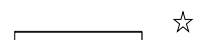
Index trackers

- Apply modelling techniques to reduce transaction cost
- Diversification
- Track a conventional or *Sharia'a* compliant index
 - FTSE Shariah Global Equity Index Series (1998)
 - Dow Jones Islamic Markets Indexes (DJIM – 1999)
 - S&P Shariah Indices (2006)
 - MSCI Islamic Index Series (2007)
 - Russell-Jadwa Shariah Index (2009)



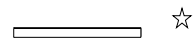
Exchange Traded Funds

- Track an index, commodity, or basket of assets
- Trade on an exchange
- Fully invested
- No NAV required
- Variety of *Sharia'a* compliant ETFs available



Hedge funds

- Risk diversification
- Long-short strategies not permitted
- Use of *salam*, *wa'd* and *arbutun* to mimic optionality and short selling
- Limited traction



Questions

