



# -CAPITAL FOR THE FUTURE- Towards a Sustainable Financial Sector Development

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Sustainable Finance for Sustainable Development

**MARTIN RAISER  
COUNTRY DIRECTOR  
WORLD BANK**

# Outline

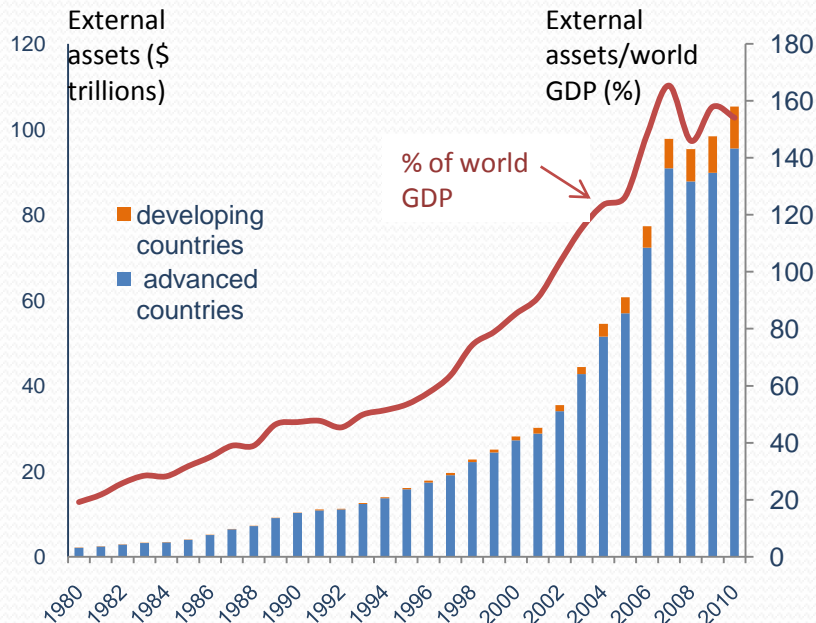
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## *Issues for a Sustainable Financial System and Implications for Islamic Finance:*

- 1- Post-crisis Trends in Financial Regulation and Risk Management and the Potential Contribution of Islamic Finance
- 2- Shifts in the Share of Emerging markets in Global Savings and Investment and Implications for Islamic Finance
- 3- Financial Inclusion and the Possible Role for Islamic Finance

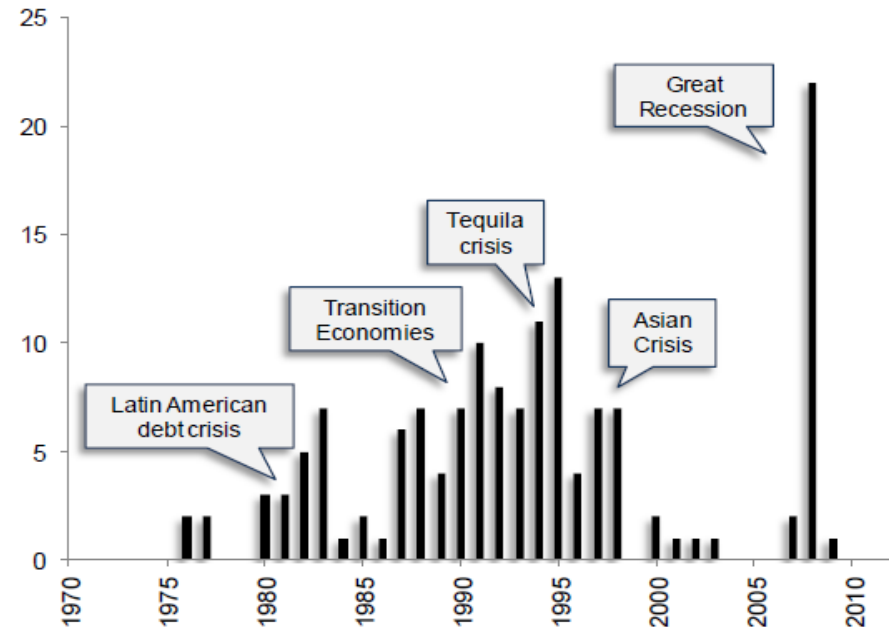
# Financial Integration has been deepening, and with it the risks of crises and contagion...

## International Investment Positions and Increasing Financial Globalization:



World Bank Global Development Horizons and IMF International Financial Statistics

## Number of Systemic Banking Crises Starting in a Given Year:



Systemic Banking Crises Database: An Update, - Luc Laeven and Fabián Valencia 2012

# Implication: improved risk management, stronger buffers, strengthened corporate governance...

## Islamic finance can play a role

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### **What Triggered the Global Financial Crisis ?**

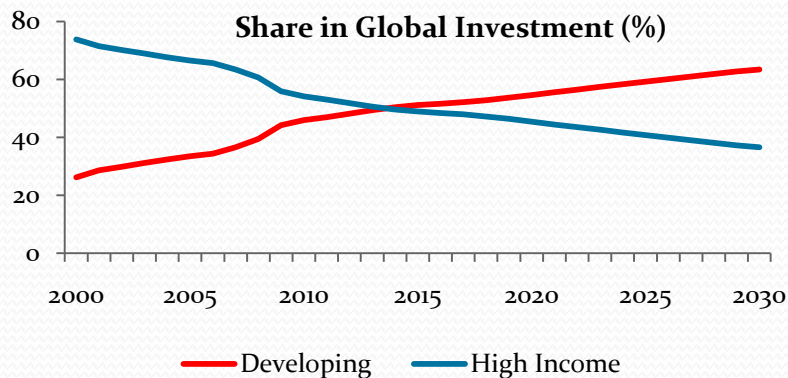
- Macroeconomic imbalances
- Boom-bust credit cycles, fueled by lax monetary policy in developed countries
- An asset price bubble and excess investment in real estate (poor overall assessment of risks)
- Regulatory weaknesses and poor risk management, weak supervisory and corporate governance frameworks
- Financial innovation and increased opaqueness (Reckless use of collateralized debt obligations; growing reliance on the originate-to-distribute business model/poorer risk assignment)
- Financial integration (much larger capital flows /cross-border positions and resulting contagion)

### **Can Islamic Finance Play a Role in Reducing Risks in Future?**

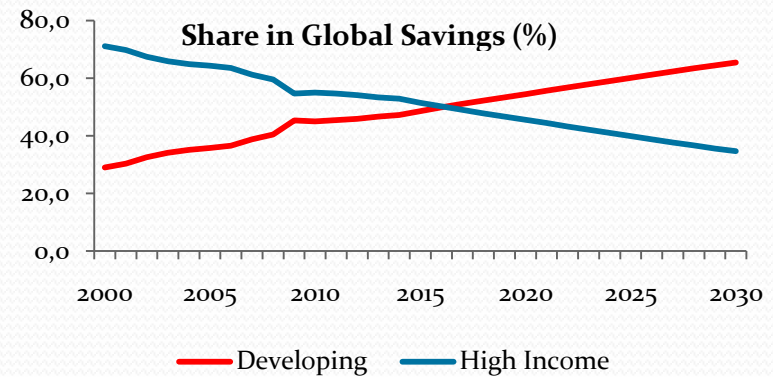
- Islamic finance emphasizes asset backing and principle risk sharing
- Profit and loss sharing encourages risk-sharing between banks and their clients
- Ensures a direct link between financial sector transactions and real sector activities
- Reliance on equity-type financing arrangements helps restrain excessive leveraging
- Sharing of losses reduces the probability of contagion to the rest of the financial system
- Consistent evidence of higher capitalization among Islamic banks

# Major shift in the share of emerging markets in global savings, investments and capital flows

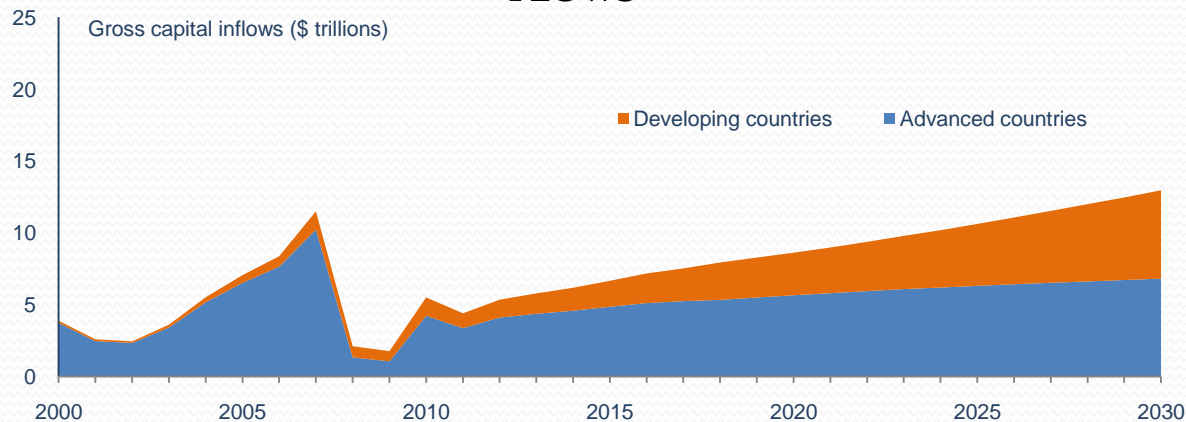
## INVESTMENT



## SAVINGS



## CAPITAL FLOWS



# Implication: enhanced coordination is essential

## Islamic finance needs more standardization

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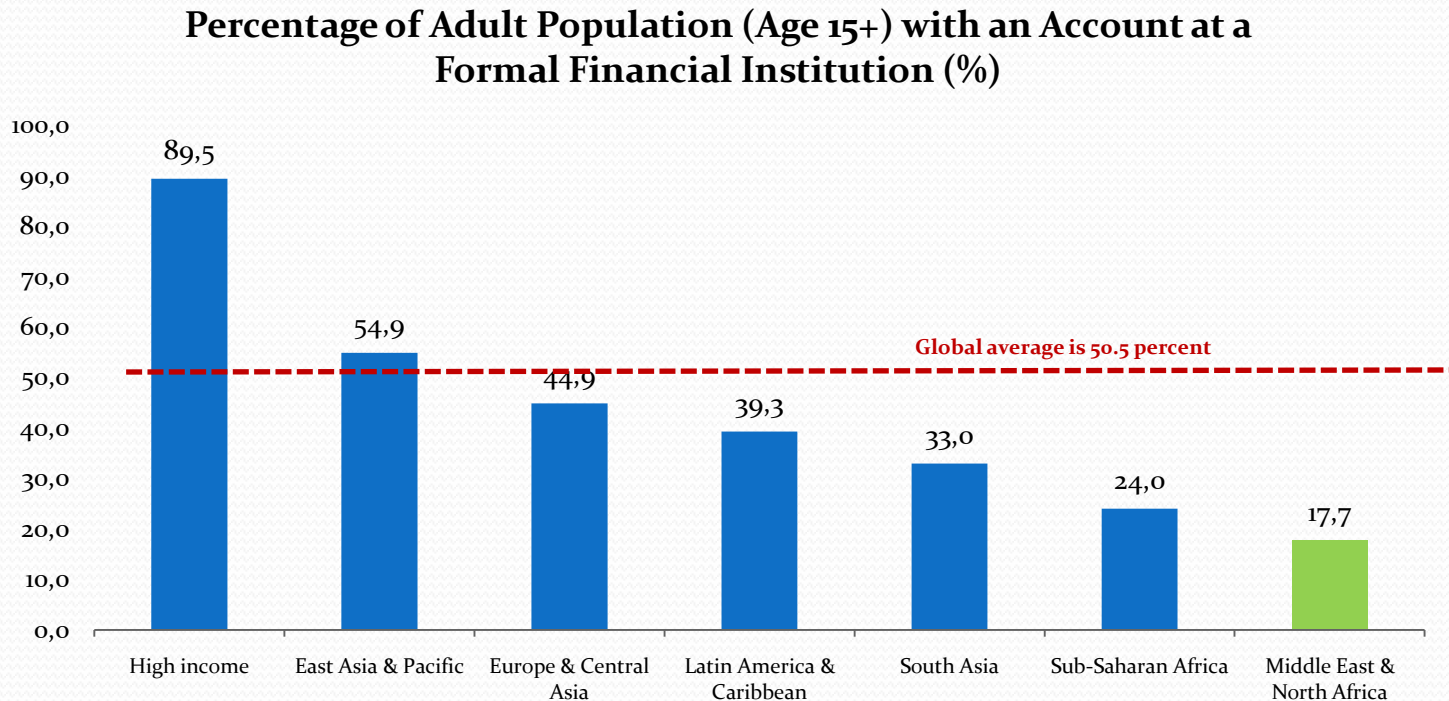
### **How can emerging markets benefit from the shifts in global financial heft?**

- Emerging markets will rely less on flows from developed countries - but will need to develop financial systems that can mobilize domestic and international savings effectively and intermediate these funds efficiently
- Global monetary and financial policy coordination will need to strengthen as developing countries become responsible for an expected half or more of the world's capital outflows – and thus much more dependent on each other

### **What implication for Islamic Finance?**

- Islamic finance can play an important role in this transformation, as the rising market share in non-traditional Islamic finance markets shows
- However to realize the full potential of Islamic finance more standardization and harmonization of the regulatory framework is needed
- Some other challenges that Islamic finance industry faces are: improving regulatory and supervisory oversight; rebalancing tax treatment of Islamic finance instruments; strengthening insolvency frameworks; establishing sound risk-management practices (e.g. Basle III compliance); and ensuring adequate liquidity in the fixed income market

# Financial Inclusion is important for sustainable financial development



World Bank Global Financial Inclusion Data

# Implication: Islamic finance can play a major role in expanding financial inclusion

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## Why is financial inclusion important?

- Enhancing the access to and quality of basic financial services such as availability of credit, mobilization of savings, insurance and risk management can help reduce poverty and boost productivity
- More than 2.7 billion people (70 percent of the adult population) in emerging markets still have no access to basic financial services, and the share is highest in countries with a predominantly Muslim population (in part because Muslims may “opt out” of traditional financial services for religious reasons)

## How can Islamic finance help?

- (i) through providing financial instruments for those uneasy about traditional finance; (ii) through risk-sharing that may overcome collateral constraints among SMEs and micro-borrowers, and (iii) through non remunerated capital contributions and other explicit redistribution mechanisms (Zakah, Waqf, Qard-al-Hasan)





Thank You  
Tesekkur Ederim