

Ways to Attract Islamic Compliant Investors to Funds and Products

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www.klgates.com

The demographics

- 26.4% of the global population will likely be Muslim by 2030
- Currently 23% in 2012
- Percentage of Muslims in Europe is around 5%

- Source: Deutsche Bank, Global Islamic Banking, November 2011

Islamic asset management industry

- 2010: 7.6% increase in assets; 23 new islamic funds; 46 funds liquidated
- Large number of relatively small, equity-heavy funds
- Focus on banking industry
- Islamic fund universe: c. 100 fund managers, managing 765 global islamic mutual funds (versus c. 60,000 conventional funds)
 - Source: Ernst & Young Islamic Funds & Investments Report

Islamic fund sizes

- Just over half of Islamic funds <\$50m under management
- Almost 70% <\$75m under management
- Conventional funds of \$22,000bn versus Islamic funds of \$52.3bn
 - Source: E&Y, Islamic Funds & Investment Report, 2010

Islamic fund composition

- 54% equities
- 17% money markets
- 15% mixed assets
- 7% real estate
- 5% seed capital
- 2% others

□ Source: Maybank Islamic, 2009

What is Shariah?

- A means of conducting business through a distinct set of rules designed to facilitate fairness
- High correlation between Shariah compliant investing and socially responsible investing

Shariah terms

- *Halal* – that which is permitted or compliant
- *Haram* – that which is not permitted
- *Riba* – charging of interest
- *Gharar* – uncertainty/ambiguity
- *Maysir* – gambling; one party receives the other's loss
- *Sukuk* – Shariah compliant debt
- *Ijara* – Shariah compliant lease
- *Takaful* – Shariah compliant form of insurance
- *Mudaraba/Musharaka* – forms of partnership
- *Murabaha* – sale of commodity with the payment being deferred, the mechanism being used as a fixed income substitute

Industry prohibitions

- Gambling
- Pork production or consumption
- Adult Entertainment
- Conventional banking and finance
- Alcohol production or consumption
- Tobacco production or use

Where are Shariah rules codified?

- Interpretations of the Qur'an from various Islamic schools of thought
- Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI)
- The fact remains: Shariah mandates are not always consistently applied from Scholar to Scholar. Information is asymmetric, and Shariah Advisers and lawyers skilled in the area become useful to work through the counter-intuitive results

Islamic finance themes

- Connection to underlying assets
- Commercial risk taking by all parties (including financier)
- Entrepreneurship
- Returns linked to actual investment outcomes
- Sharing profit and loss

Islamic asset management challenges

- Scholars and schools of thought
- Lack of standardisation
- Transaction costs
- Asset ownership by financier involves potential liability e.g. environmental, warranty claims
- Insurance / *takaful*
- Tax treatment



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Ways to Attract Islamic Compliant Investors to Funds and Products

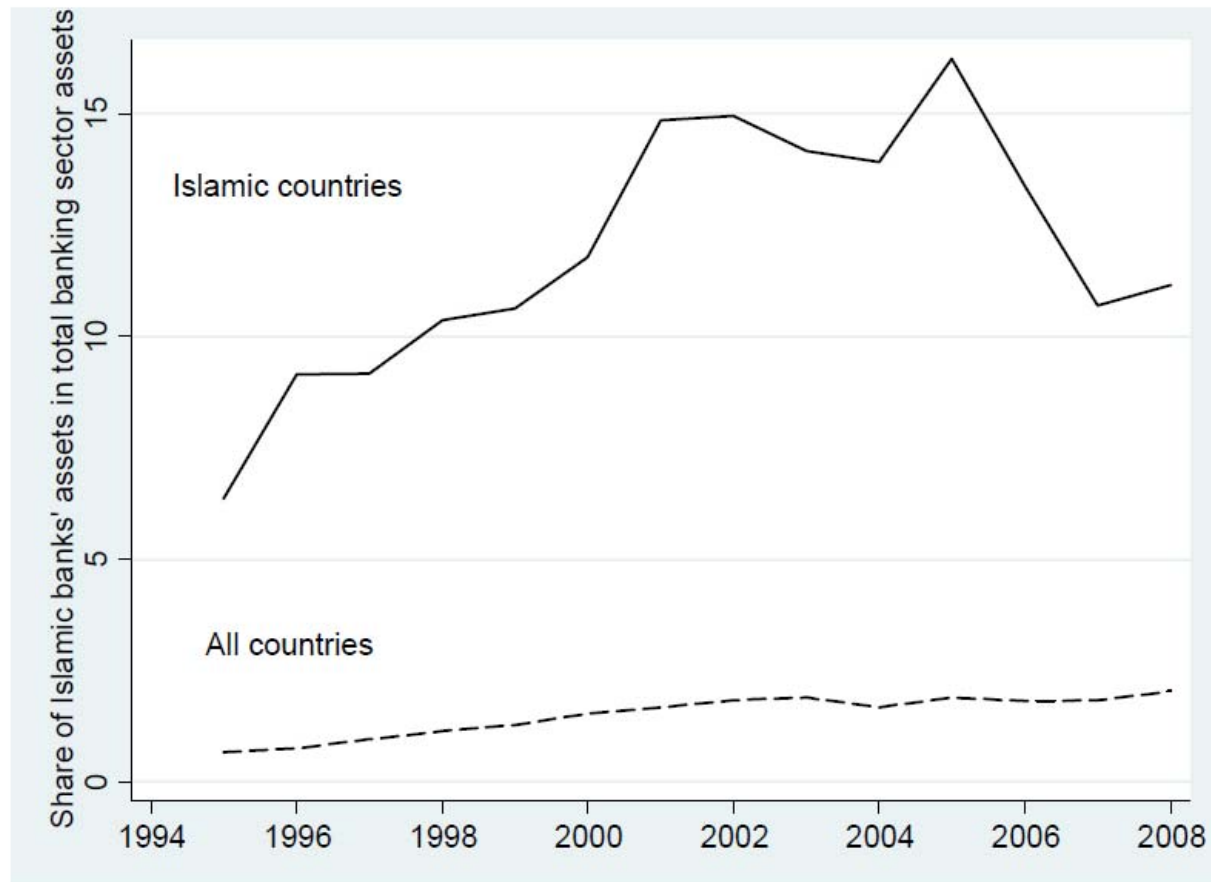
Fares Mourad, Head Islamic Finance
London 27th. June 2012

Numbers speak by themselves

- In 2010 about 23.4% of world's population are Muslims, and expected to reach 26.4% by 2030*
- In numbers, this means an increase from 1.6 billion to 2.2 billion*
- Muslims currently have a 7.7% share of global GDP which is expected to grow to 8.7% by end 2017
- 50% of the Islamic Banking is in the GCC, while GCC Muslims with a population of 38 million are a minority within the Muslim population.

Source: * The Economist, A waging crescent, 27th Jan 2011

Expansion of Islamic Banking 1995 - 2008



Source: World Bank, Policy Research working paper 55446

To attract, you need to know the motives

- Identity and faith
- Economic considerations

Competition on products

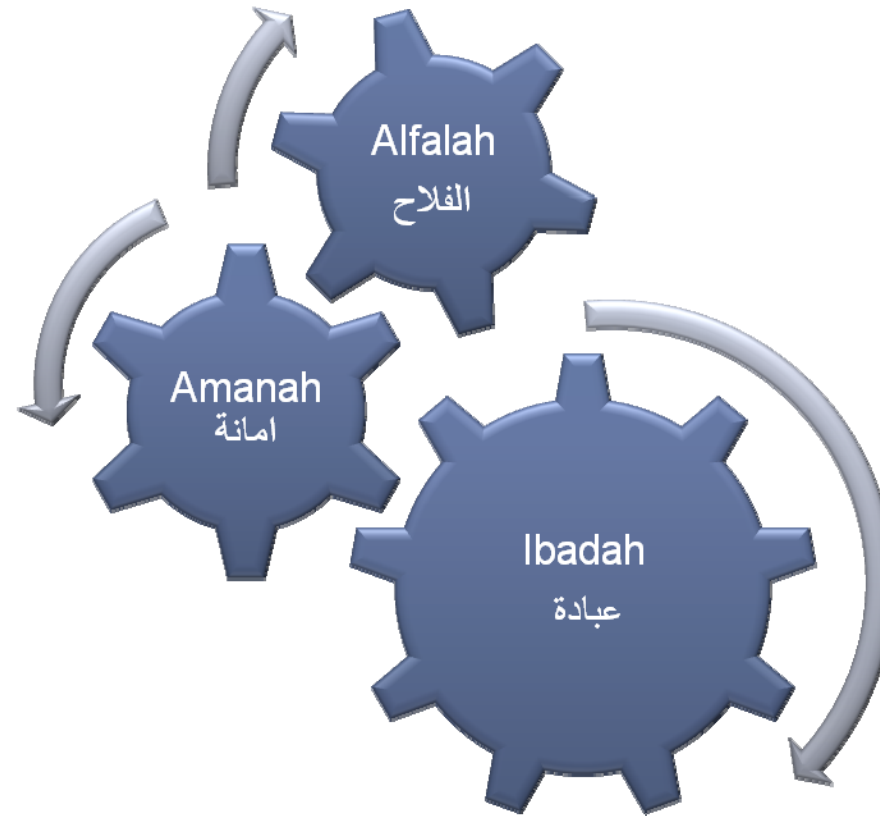
- Unless the product is unique, competing on products, is ultimately a competition on pricing
- it is better to create an added value to the client



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Islamic Financial Planning / Estate and Succession Planning

Islamic world views on Financial Planning



Practical example I/III

- Abdullah, enquired about his Zakat obligation, the zakat awareness arose on the wake of his decision to perform the hajj. In addition to the recent preparatory hajj course that he has been attending, he found out that he has to pay back past dues (i.e. zakat not paid from his wealth in the past). Further, he believed that zakat is only obligatory during the month of Ramadan, namely zakat el fitr, which he never missed. of course his financial plans have not neglected the hajj requirements and have always been within the ambit of his savings and investment plan. To make this scenario more interesting, Abdullah has just divorced his wife of 25 years and is planning to remarry later in the year. His ex-wife is holding on the company directorship and has successfully claimed her rights to their matrimonial assets via the assistance of an established law firm.

Practical example II/III

- The plot thickens, The wife-to-be is also divorced with three children under her grace. with hindsight, Abdullah wants to plan his estate distribution firstly, to ensure his present children (his own flesh and blood) are provided for sufficiently from his wealth, and secondly to make sure that his present assets are not claimable by his future wife. Matrimonial assets would only be accumulated from the date of marriage onwards. Abdullah plans to transfer specific assets to be given to his wife-to-be via hibah (هبه) or living gift.
- to complicate things even more, Abdullah has only daughters, hence according to the laws of faraid, this is the case of missing independent agnate exposing the balance of the distribution to his living brothers or uncles or nephews.
- Thus a detailed Islamic Estate Plan is required to meet his goals, especially in the light of diverse locations of his assets. We already know that he has properties in UK,USA and Australia and his daughters are currently studying.

Practical example III/III

- Abdullah knows that the distribution of his estate is provided by faraid, however, he is not particularly sure of the rights of his soon-to-be-step children on his assets. Nor does he want to be unfair in providing for the needs of all his dependents, whether they are blood children or by marriage.
- thus he seeks full advice, on the matter including available options. Also planning ahead, he would like to explore the idea of waqf or charity in perpetuity as recommended in Islam.
- Last but not least, issues related to pension, health insurance...etc should be considered as well when planning.

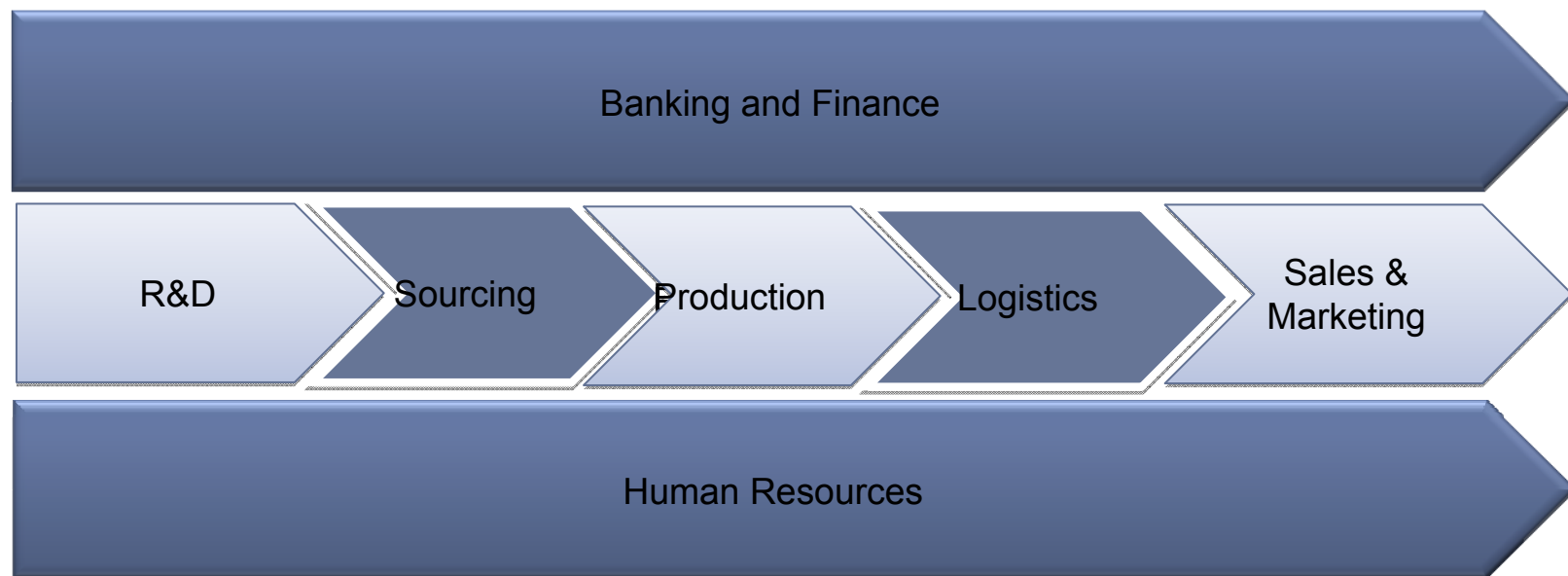
Islamic and Conventional Financial Planning

- Time horizon: the Muslim will live in the hereafter.
- Sharia is the guide in creating strategies to achieve life goals.
- Objective: Achieving Alfalah (الفلاح).



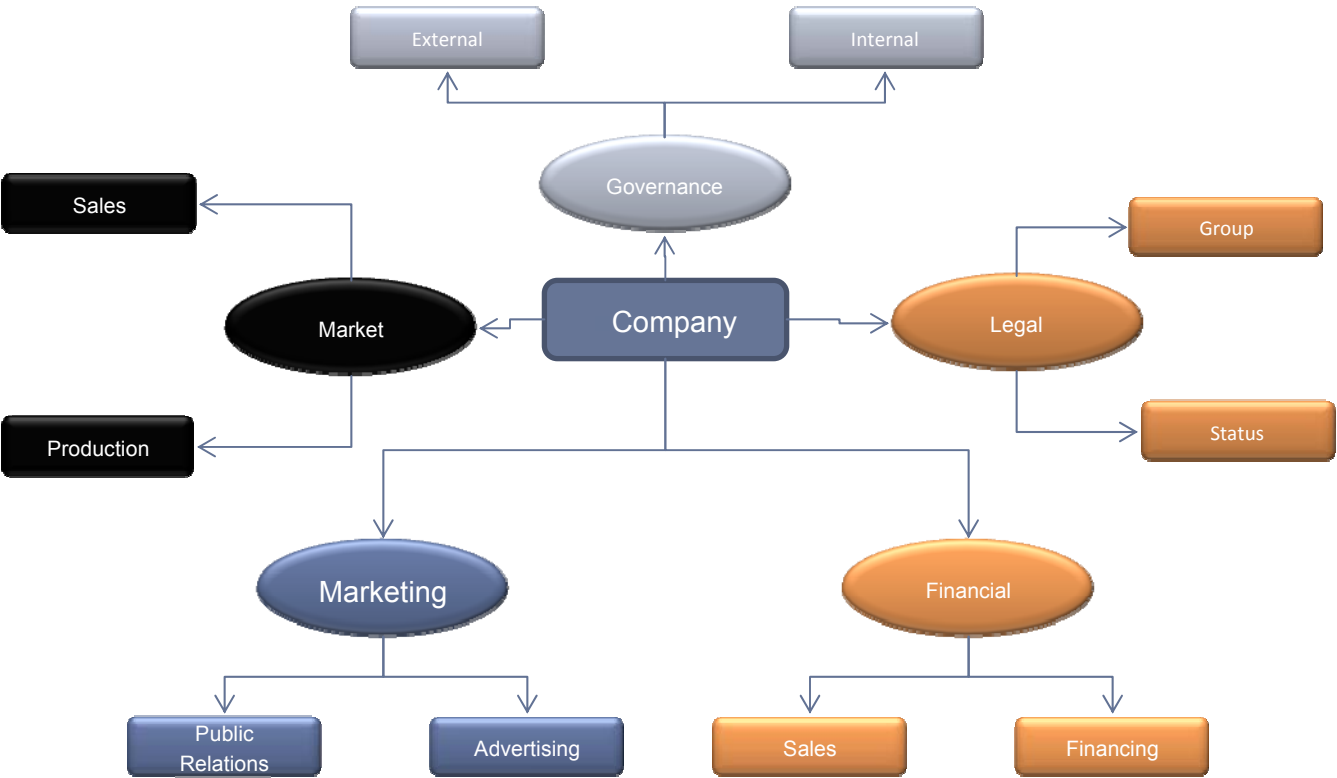
Business conversion

Conversion requires a holistic approach



Source: Bank Sarasin, A.T. Keaney

Corporate conversion means that a web of issues need to be considered



Source: Bank Sarasin

Purpose of conversion

If a company wishes to be Islamic, it cannot focus only on the business, but on making business right in the eyes of Allah.

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