



**ISTANA ISKANDARIAH  
KUALA KANGSAR**

**KEYNOTE ADDRESS  
BY  
HIS ROYAL HIGHNESS  
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**AT THE  
FRANKLIN TEMPLETON INVESTMENTS  
2018 ISLAMIC FORUM**

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*Seizing the Moment for the Islamic Investment Industry:  
The Evolving Case of the Sukuk Market*

*Bismillahirrahmanirrahim.*

*Assalamualaikumwarahmatullahiwabarakatuh.*

1. Good morning and a very warm welcome to all of you, particularly those who have travelled long distances to be here with us today.

2. My congratulations to Franklin Templeton Investments for putting together this Forum at what is, I think, a pivotal moment for global Islamic finance. I am delighted that Kuala Lumpur is hosting this prestigious forum, which I last spoke at in Dubai back in 2014.<sup>1</sup> My hope is that this Forum

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<sup>1</sup>Sultan Nazrin Shah, "Building Greater Inter-Connectivity Through Islamic Investing", Keynote Address at the Franklin Templeton Investments 2014 Islamic Forum, Park Hyatt, Dubai (27 October 2014).



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will continue to play an important role in the increasingly vibrant and successful Islamic finance industry in the years to come.

3. Permit me to begin with a brief and, no doubt, familiar definition. At the broadest level, the term “Islamic finance” describes any financial products or mechanisms which have been developed according to the principles outlined in the Qur’an and the Sunnah. Islamic finance is thus as old as Islam itself, and has existed for over 1,400 years. Central to Islamic finance are the key principles of sustainability, responsibility, risk-sharing and generosity. These key principles are manifested in a variety of Islamic finance instruments, including *zakat*, our compulsory alms-giving, *sadaqah* or charitable giving, and *waqf*, the donation of endowments. While all of these Islamic finance instruments have a crucial role to play, however, we are here today to consider the ongoing development of Islamic finance within the global finance industry. As such, it is on Islamic investments, and in particular, on *sukuk*, which I intend to focus in my address this morning.

4. It is only in recent years that we have witnessed the Islamic investment industry emerge as a viable and important contender on the world stage. The opening of the world’s first Islamic bank, the Dubai Islamic Bank, in 1975 may be regarded as a milestone in the global development of Islamic investing, but even 40 years ago, no one would have expected the industry to grow so rapidly, or to become as prominent within a global context as it now undoubtedly is. Indeed, we may look back on the global financial crisis of 2007-2008 as a turning point for Islamic investments, a period of economic turbulence during



which the key Islamic finance principles of responsibility and sustainability were, surely, more than vindicated. A 2010 report by the International Monetary Fund found that Islamic banks, on average, demonstrated stronger resilience during the financial collapse. In fact, the report goes so far as to conclude that “Islamic banks contributed to financial and economic stability during the crisis”.<sup>2</sup>

5. The global economy has, for the time being, stabilized, and following a period of uneven growth, we are at last witnessing synchronized growth in most regions. But the global financial crisis has sent shockwaves throughout the world, acting as a much-needed wake-up call to the global finance industry. I hope that the crisis has alerted banks, investors and experts to the urgent need for more responsible and sustainable financial practices, in order to safeguard against future recurrences. For this reason, I believe that the present financial climate may represent an unprecedented opportunity for Islamic investing. Islamic finance is synonymous with investments that are ethical, equitable, social, and sustainable – all qualities which the global finance industry desperately needs. In the true and generous spirit of Islamic finance, therefore, I hope that we may witness the Islamic investment industry expand over the coming years, in ways which benefit not just its own investors, but also the world population and, indeed, the planet as a whole.

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<sup>2</sup>“IMF Survey: Islamic Banks: More Resilient to Crisis?”, *IMF Research* (4 October 2010); cf. Jemma Dridi and Maher Hasan, “The Effects of the Global Crisis on Islamic and Conventional Banks : A Comparative Study”, *IMF Working Paper* 10:201 (Washington, DC: IMF, 2010).



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6. The Islamic investment industry has already registered remarkable growth in the years since the financial crisis. The industry's total assets reached US\$1.9 trillion globally in 2016, with the domestic share of Islamic banks increasing in 18 countries. I am delighted to say that Malaysia continues to set the pace for the rest of the world in this area. The share of Islamic assets in total assets quadrupled here between 2001 and 2016, while we are also leaders in the global *sukuk* market, with more than 50 per cent market share. Malaysia maintained its leadership as the world's largest *sukuk* issuer in 2017. Its issuance of US\$36.5 billion accounted for more than one third of global *sukuk* issuance. Malaysia also topped the global *sukuk* arena in 2016, with issuance of US\$29.9 billion.

7. Beyond our borders, meanwhile, there are also promising signs for Islamic investments. Al Rayan Bank in the United Kingdom became the first British Bank to issue a *sukuk* earlier this year, worth GBP250 million. This *sukuk* was oversubscribed at 155 per cent, reflecting the strong demand that exists for Islamic financing instruments even in Western Europe. In other countries, too, the thirst for Islamic investments is fast developing: South Africa is now considering a local-currency *sukuk*, after becoming the first African nation to issue a US\$500 million sovereign Shariah-compliant bond in 2014.

8. From the point of view of investors the world over, it is not difficult to understand the growing appeal of *sukuk*. From a choice of only 7 industries in the year 2000, *sukuk* issuances are now offered across 27 industries, with the



issuance amount growing from US\$1.5 billion to more than US\$440 billion. This is an almost 300-fold expansion, providing investors – Muslims, and non-Muslims alike – with vastly increased and improved investment opportunities.

9. Moreover, since the inception of the Dow Jones Sukuk Index – the global index that tracks Islamic fixed income securities – *sukuk* has consistently outperformed Global Fixed Income in 7 out of 10 calendar years, and in 5 of the last 6 calendar years. Over this period, *sukuk* returns were 50.3 per cent, as against 38.2 per cent for Global Fixed Income.

10. *Sukuk* returns have a low correlation with other conventional asset classes, such as Emerging Market Equities, Global Property, Developed Market Equities and Global Bonds. This makes *sukuk* a good portfolio diversifier. Given these low correlations and its consistent performance, *sukuk* should be considered as a mainstream asset within both Shariah-compliant and conventional portfolios.

11. Yet, in spite of these recent successes, Islamic investing is not without its challenges of course, and these challenges must be addressed if the industry is to continue to thrive in a global context. The first challenge is one of scale. While the overall *sukuk* market has posted growth in recent years, the resilience of Islamic equities and funds cannot be taken for granted, as most of them lack scale. Close to three-quarters of the 1,100-plus Islamic funds in existence have less than US\$25 million in Assets Under Management. This is in stark contrast to conventional funds, which have an average size of US\$394 million. This



scale issue has serious implications, including the risk that Islamic funds may be less competitive than conventional ones, as they miss out on scale economies. This could result in the closure of smaller, struggling Islamic funds.

12. Another potential concern is that global Islamic-listed equity markets, as measured by the performance of Islamic equity indices, have been experiencing greater volatility of late, due to international developments, as well as more region-specific events. For the first time in many years, Islamic equity indices have recently been yielding lower returns as compared to identical conventional equity indices. This goes against the pattern of Islamic equities generally outperforming conventional instruments. Whether or not this becomes a trend remains to be seen, but it is certainly something that we need to take note of.

13. There is also the question of ensuring that Islamic finance retains its relevance to global finance, while remaining steadfastly anchored to Shariah principles and values. A crystal-clear roadmap of proper governance is essential to maintaining the integrity of Islamic assets. The Islamic market has an added layer of regulatory processes, related to the Shariah compliance of the underlying securities and business operations. So players in the Islamic funds industry do have to comply with an additional set of transparency and disclosure requirements. For investors of other faiths and belief-systems, the ultimate proof of the value of Islamic investment assets is not in their religious intentions, but rather in their inherent practical soundness. This places a heavy responsibility on



the governing institutions of Islamic finance to set high standards for risk management, operations, auditing, and financial reporting.

14. New realities such as changing client demographics and the growing preference for modern and digitized distribution methods, must also be recognized. The global asset management landscape is being pushed to embrace new online investment platforms in order to meet the needs of an evolving client base that favours these new distribution channels. Growing demand for low-cost and passive investment strategies, as well as for greater transparency, poses unique sales and execution challenges. Failure to keep up with these changing structural dynamics could put the industry at an even greater disadvantage than at present.

15. In summary, there are four key areas that need to be addressed for Islamic finance to move forward. First, the Islamic equity asset class needs to explore solutions to the challenge of scale, with the aim of achieving critical mass volume in order to remain competitive. Second, returns to Islamic funds must be stabilized in order to reinvigorate investor confidence. Third, an unparalleled benchmark for governance must be established that balances financial and ethical considerations. And finally, Islamic finance must embrace the modern era of disruption, with a continued strong focus on product innovation.

16. I am delighted that this Forum is dedicated to exploring the very issues that I have highlighted, at what is, as I have suggested, a pivotal moment in the



Islamic finance industry. Before I conclude, I would like to reflect on the last of these issues – the question of innovation – to consider how Islamic investing might, as it were, *carpe diem* and seize this moment. For I believe that innovation represents a challenge and an opportunity for the industry. Indeed it seems that there are ways in which recently developed financial products might actually have a certain synergy with the key principles of Islamic finance.

17. The rise of Socially Responsible Investing(SRI), which is based on a similar rationale as the fundamental tenets of Islamic finance, broadens the appeal of Islamic finance instruments to encompass ‘socially responsible’ investors who are also guided by an ethical code. This overlapping of core values provides an opportunity for Islamic finance to access the growing amount of SRI funds available in global markets, which already amount to US\$22.9 trillion. With a 30 per cent share, Malaysia is the largest SRI market in the Asia region (excluding Japan).

18. A related area of innovation on which Islamic investing might also capitalize is the emerging field of “green” or environmentally-friendly finance. Late last year, Malaysia took the lead in this area, when the country launched the world’s first Green *Sukuk*, aimed at financing sustainable, climate-resilient growth. A collaboration with the World Bank, this first-of-its-kind Green *Sukuk* is the culmination of years of work on how best to address the current global gaps in Shariah-compliant green financing. It provides a blueprint for pioneering fundraising instruments that serves the growing global need for more sustainable and responsible financing.





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19. Sustained innovation is essential for progress, and Malaysia constantly strives to be at the forefront in this area. We must keep ahead of the technological disruptions that are reshaping the way we live. Given this context, Islamic finance should embrace fully the new and emerging approaches to finance, while at the same time maintaining the core principles that set it apart from conventional finance.

20. I note with interest the relevance of the selected themes and issues that will be under discussion at this Forum. While Islamic investing has made significant progress in recent years, both domestically and globally, the next phase of growth will require players within the industry to reflect, recalibrate, and rethink their approaches to certain aspects of conducting business, in order to respond to the challenges of the present financial climate. Just as Islamic finance itself is considerate, open and honest, so must our discussions of these challenges be if we are to overcome them.

21. To see so many of the best minds in Islamic finance gathered here today gives me great confidence that we will discover new perspectives, and develop exciting, innovative ideas about the global role of Islamic investments going forward. Following a period of terrible financial uncertainty on an international level, I truly believe that the world now needs Islamic finance, and the sustainable, responsible financial practices enshrined at its spiritual core. This, ladies and gentleman, is the moment for Islamic investing to realize its full,



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global potential, and I am in no doubt that the discussions taking place over the next two days will help us to achieve this. I very much look forward to hearing about the many positive outcomes of the Forum, and I wish everyone here a meaningful, insightful, and even, an enjoyable event.