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International Conference on Islamic Capital Markets
Towards a Reselinet, Robust and Competitive Islamic Capital Market
Jakarta, Indonesia 19-20 June 2012

The Islamic Capital Markets Conference themed "Towards a Reselinet, Robust and Competitive Islamic Capital Market" was held during 19-20 June 2012 in Jakarta, Indonesia. Its purpose was to deliberate on the ways and means to further develop Islamic capital markets at local and global levels. The conference was jointly organized by the Indonesian Capital Market and Financial Institutions Supervisory Agency (Bapepam-LK) and Islamic Research and Training Institute IRTI-IDB.

Her Excellency Ibu Any Ratnawati, Vice Minister of Finance, Republic of Indonesia inaugurated the conference which was attended by over 250 national and international participants. The conference program was organized around four main themes:

1. Islamic Capital Market Development and Prospects;
2. Market Reform and Infrastructure Development;
3. Regulatory Aspects;
4. Strategy for Developing Capital Market Products for Public Sector Financing.

In these four sessions 15 research papers were presented and four panel discussions were held. Individual scholars, regulatory organizations from various countries and international financial infrastructure organizations participated.

Given the current turmoil in the global financial system and global imbalances the conference was very stimulating in its purpose and theme. The sustainability of finance has become an important issue besides increasing the market capitalization and enhancing market growth. The conference discussed these issues from both the practitioners' and the academician's views. The interaction between academics, practitioners, regulators and policy makers was the unique dimension of the conference that provided new perspectives and practicable approaches to the issues faced in development of Islamic Capital Markets.

A communique making five important recommendations was issued at the end of the conference.

Conference Communique and Recommendations

Based on the presentations and panel discussions during the conference, the participants issued a communique making five recommendations:

1. Though Islamic capital markets are much stable due to avoidance of interest based instruments and moral values in its trading principles, these markets are not immune from possible financial disturbances which may be transmitted through slightly different channels. This vulnerability increases as markets expand and get integrated with global markets and become more exposed to the global financial shocks. Therefore, in addition to relying on operational peculiarities of Islamic finance, the Islamic capital market should also impose good corporate governance. The higher the quality of the implementation of good corporate governance, the higher the public confidence will be achieved, hence the market would be more resilient and robust. This calls for applying well designed regulatory framework and allowing the market participants to get right incentives for performance. Since the transparency and good performance are mutually reinforcing, the capital market regulators should give particular attention to this dimension.
2. Risk assessment of products and markets are also important for regulators, issuers and investors in Islamic capital markets. Appropriate techniques should be developed for risk assessment of Islamic products, regulatory bodies should build this internal capacity, and methods should be created to educate investors on the returns and risks involved in Islamic capital market products.
3. In the area of product and market development, some papers analysed the comparability of the Islamic capital market products to other conventional capital market products such as socially responsible investment and the possibility of developing the ETF compatible to Sharia principles. The challenge is, how we can enrich the market with capital market products that maintain the strong tie with projects and real economy and improve

the liquidity of the market while keeping compliance with the Sharīʿah principles.

4. Besides the product development, the expansion of the Islamic capital market also depends upon efforts of the industry in educating the public. Misperception on the Islamic capital market products does exist which may lead to reluctancy in investment decision. The Islamic capital market needs a well-designed marketing program capable of introducing the Islamic products to the public in a more friendly way. The introduction of retail sukuk in Indonesia is one of the examples on how the Islamic market products can be popular and become a success story for public sector financing. The fact shows that the retail government sukuk has become an effective tools for public fund mobilization particularly in strengthening the fiscal policy of the government.
5. A proper and strong legal foundation for Islamic capital market is very important to achieve market efficiency since it could minimize the uncertainty and subsequently improve the public confidence. An important aspect discussed was the possible revision of the governing law clause in sukuk issuance. The adoption of asset-backed or asset-based instruments could bring different legal consequences that should be clearly reflected in the governing law.
6. The potential for growth of Islamic capital markets is very high, but this will not be realized by private demand and good wishes alone, active regulatory support and political will is mandatory.

In short

The development of the Islamic capital market requires comprehensive support covering human capital development, improved legal environment, supporting infrastructure, well-developed risk management, and finally market expansion. Despite the successes achieved so far, much still remains for us to do. Researchers, academic institutions, regulators, bankers, financial institutions, lawyers, capital market players and policy makers should all work towards these at their respective levels.

In Indonesia, the development of the Islamic capital market could serve as an important gateway for the international investors to participate in the Indonesian economic development in a mutually benefitting manner.

Further, the contents of this conference should be broadcasted to the capital market community to bring their attention upon the importance of continuous development of the market.

(Summarized by Salman Syed Ali and Dadang Muljawan)

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IRTI Lectures by Eminent Scholars during the year 1433H (2012)

IRTI organized two lectures by eminent scholars during the year 1433H (2012). One was given by an IDB Prize Laureate, Prof. Khurshid Ahmad on behalf of the Islamic Foundation, UK, the winner of IDB Prize in Islamic Economics for 1432H. The other was given by a Sharīʿah Scholar, Sheikh Yousuf Al-Shubaily. These lectures were attended by a large number of participants from across the various entities and departments within the IDB Group and from other institutions such as the Islamic Economics Institute, King Abdul Aziz University, Jeddah, Umm-Al-Qura University, Makkah Al-Mukarramah, Organization of Islamic Cooperation and Dallah Al-Barakah, Jeddah. Below are brief summaries of these lectures.

Global Financial Crisis and the Role of Islamic Economics

PROF. KHURSHID AHMAD
(Chairman of the Islamic Foundation, Markfield, UK)

IDB Prize Laureate delivered this lecture on 29/05/1433H (21/04/2012). Professor Khurshid Ahmad started his lecture by presenting the most important contributions of the Islamic Foundation UK in the field of Islamic economics for which it was awarded the IDB Prize in Islamic economics. Then he spoke of the economic and political scenarios that characterized the economic and social changes of the 57 Muslim countries during the 19th and 20th centuries, paying particular attention to the endogenous and exogenous factors that have delayed their development. This was followed by an analysis of the excesses of the capitalist system that has been the cause of the recent global financial crisis that resulted in an increase in bankruptcy, mass unemployment, inequality, and poverty.

According to him, there have been five major delinks that have given modern capitalist economy and the mainstream science of economics their distinct character, identity and ethos. They lie at the root of the crisis, which can be identified as follows:

1. A delink between religion, ethics, the moral and spiritual dimensions of life and the economy, society and state.
2. A delink between economics and other social disciplines and aspects of human thought and life.
3. A delink between economy and society was not the end of the story. What happened to the economy itself is no less devastating. It was reduced to what is called market-mechanism, which was assigned the task of decision-making in respect of all matters relating to production, exchange and consumption. It is this tragic transformation that has been rightly described by some of the leading economists, like Nobel Laureate Joseph Stiglitz and the financial wizard, George Soros, as “Market Fundamentalism”.
4. The above delinks have led to a fourth delink, both in the economic science and in the economy and all areas of economic policy-making - the delink between efficiency and equity.
5. A delink between money and production activity. This has led to the emergence of two parallel economies, a money economy and other the real physical economy.

Finally he proposed the development of a new paradigm based on Islamic economics that is not a reform of capitalism, socialism or welfare state but as an alternative to them.

(Summarized by Abdelkader Chachi)

Financial Intermediation in the Light of *Maqāṣid* Al-Sharīʿah

SHEIKH YOUSUF ABDULLAH EL SHUBAILY

(Professor of Shari’ah, Higher Institute of Justice, Riyadh, Saudi Arabia.)

The lecture was delivered by Sheikh Yousuf bin Abdullah al-Shubaily on 21/06/1433H (12/05/2012) at IDB, Jeddah. He discussed some of the modern applications of financial intermediation by contemporary Islamic banks and financial institutions from an Islamic perspective of *Maqāṣid* al-Sharīʿah. The conventional banks as well as Islamic banks are financial intermediaries in the sense that they link depositors (who provide money) with investors (entrepreneurs who employ the money). However, the main difference between them is that the conventional banks use debt contracts to borrow from depositors and lend to the seekers of funds and make their own earnings from the difference between the borrowing rate and the lending rate. Whereas Islamic banks mobilize money through *muḍārabah* or *shirākah* or *wakālah* contracts and provide finances through *murābaḥah*, *ijārah*, and *istiṣnāʿ*. There are also investment banks which are different only in that they intermediate between investors as agents without taking ownership of the money raised.

The lecture focused on clarifying the objectives of the rules and laws of Sharīʿah pertaining to regulating financial intermediation. Five key aspects of the law were highlighted that Sharīʿah distinguishes between:

1. (*Himayah*) protection and (*ḍamān*) guarantee.
2. Social needs that necessitate particular contracts and the needs that do not require those contracts.
3. Mediation intended for economic investment and the mediation for speculative purposes.
4. Legitimate risk and the prohibited risk.
5. Commutative contracts and non-commutative (or gratuitous) contracts as well as cooperation.

These distinctions have clear implications in defining permissible and prohibited kinds of financial intermediation.

1. The objective of the rules to keep a distinction between (himayah) protection and (daman) guarantee

Protection of wealth or money means to safeguard against losses or destruction of the capital through care and prudential behavior, this is desired by Sharīʿah. While, ‘guarantee’ is a binding commitment that puts the liability of making good any losses or capital destruction on the guarantor.

The legal implication of the objective of protection is that it is not permissible for the bank (or the *muḍārib*) to risk the money of the depositors (or the fund provider) without authorization, nor to borrow against this money without authorization; neither to buy and sell using the commodities that people usually do not trade, nor to buy and sell for itself, and not to indulge in acts that will lead to damage or bring harm to the capital. If it does, then the bank is liable for the damages.

The Sharīʿah position on liability of loss is also very clear. As long as there is no breach of fiduciary responsibility of protection and care in investment contracts, whether it is *muḍārabah*, or commission based agency, the loss from capital depletion is to be borne by the capital provider alone, whereas the loss of the worker is unrewarded efforts.

In the current practices of investment and financial intermediation institutions the concept of fiduciary responsibility of 'protection' and the concept of 'guarantee' as liability are often been mixed and confused. Some examples of the misapplication of these concepts are: (i) Imposing of a condition on the asset management company or on the *ṣukūk* issuer to guarantee the expected return, as if a shortfall in attaining the expected returns is a kind of transgression. (ii) Putting in a binding promise from the asset management company that at the time of dissolution they will buy the merchandise from the capital provider at a price covering the cost and profit equivalent to the expected profit. (iii) Making it binding to buy back *ṣukūk* assets at their original price. Effectively, this guarantees the principal in investment.

2. *Distinction between social needs that necessitate particular contracts and the needs that do not require those contracts*

There are many instances of contracts and mutual dealings in which the law giver has provided leniency due to the real human needs and others where a strict stance has been taken due to non-essential nature of the need. Examples include prohibition of sale of yet to born camel and sale of to be planted crop but allowing of *salam*. Similarly, prohibition of sale of debt with debt (*bayʿ al-kāli bil kāli*) but allowing of *istiṣnāʿ* which itself initiates a debt while the price is not fully paid. The permissibility here is due to existence of genuine needs. In light of this the lecture discusses and evaluates permissibility and non-permissibility of many modern day practices in currency exchange, stock exchange trades, trading on margin etc.

3. *Distinction between intermediation intended for economic investment and the mediation for speculative purposes.*

Looking at the legal provisions one notices that the law giver has directed the traders and brokers towards value creating investment and away from speculative undertaking. For example, the insistence of Sharīʿah on acquisition and ownership (*qabz*) of goods before their trade and re-trade. Imposition of *zakāh* on all goods kept in inventory for trade to get speculative gains, while these goods are not originally *zakātable* items. All these point to the above mentioned purpose.

4. Distinction between legitimate risk and the prohibited risk

It is known that any investment whether it is mediation or financing or insurance or any other type is not without risk. All kinds of investments, despite all the measures undertaken to protect them, are subject to varying degrees of risk depending upon the type of contract used, its duration, nature of the investment, location, time and other factors. In general, the risk in debt contracts is higher than risks in spot contracts; and risk in partnership contracts are higher than the risk in debt contracts. Sharīʿah's position is that not all risks are prohibited nor all are permitted. According to the classification of Ibn Taimiyyah risks are of two types: Permitted risks such as the entrepreneurial risk undertaken by a producer or trader. And prohibited risks such as that originate from lack of information and uncertainty about the commodity or time or wording of the contract etc. Such risks are called *gharar*. The extreme form of this risk is gambling where the motive is to gain at the loss of the other.

Some kind of *gharar* or uncertainty is tolerated in contracts as exception to the rule due to (i) its unavoidability or (ii) its smallness or (iii) it being not an objective of the contract. However, in the current practices of financial intermediaries we find many wrong applications of the above mentioned exception. Financial derivatives like options, futures and swaps all fall under prohibited types due to their speculative use. Similarly, promise and counter promise arrangements and trading of promises all fall under the same category.

(Summarized by Salman Syed Ali)

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Ninth International Conference on Islamic Economics and Finance (ICIEF)
Growth, Equity and Stability: An Islamic Perspective

The Conference will be held for three days on 9-11 September 2013, in Istanbul, Turkey, under the theme "Growth, Equity and Stability: An Islamic Perspective".

The Ninth ICIEF at a Glance

Recovery from the global financial crisis and subsequent economic downturn remains fragile. Persistent risks to financial and economic development include sluggish growth in developed countries – which is now spilling over into developing economies as well; increasing income and wealth inequalities; and still-unrestored financial, economic and political stability in many regions. High poverty and unemployment rates, large macroeconomic imbalances, deteriorations in sovereign credibility, increasing food price volatility and food shortages, and lack of access to basic infrastructure further intensify and magnify these risks – particularly for the underprivileged segments of the world population. As a result, for many countries it has become even more challenging to achieve the Millennium Development Goals (MDGs) set by the United Nations.

The existing structure of the economic and financial system is also continuing to be questioned at the highest level of intellectual and political discourse. The growing emphasis on ethics and morality in economic and financial transactions highlights the structural problems undermining the confidence in the current system and, in turn, the pressing need for more durable alternatives.

To highlight some and more of these issues, the Ninth ICIEF is being jointly organized by the Statistical, Economic & Social Research and Training Centre for Islamic Countries (SESRIC), a subsidiary organ of the Organization of Islamic Cooperation (OIC), the Islamic Development Bank (IDB) Group through its Islamic Research and Training Institute (IRTI), the International Association for Islamic Economics (IAIE), and the Qatar Foundation’s Hamad Bin Khalifa University through its Qatar Faculty of Islamic Studies (QFIS), with the support of other stakeholders.

Focus Areas

The Ninth Conference will provide a platform for dialogue and discussions between policy-makers, academics, researchers, graduate students, and practitioners to address the problems of poverty alleviation, inclusive economic growth, and macroeconomic stability from the perspective of the Islamic economics and finance discipline.