

P.R.I.M.E. Finance

Panel of **R**ecognized **I**nternational **M**arket **E**xperts in **F**inance



Islamic Finance & Sustainable Development

Salahuddin Manzoor

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Discussion Points

- ❖ UN Sustainable Development Goals 2030
- ❖ Understanding "Sustainable Development"
- ❖ The Basis for Sustainable Islamic Finance
- ❖ Islamic Finance in Action at the Grassroots Level - Microfinance
- ❖ Islamic Finance & Capital Markets: Green Sukuk
- ❖ Governance Challenges in Green & Islamic Sukuk Markets
- ❖ Conclusions..





- The scale and ambition of the 2030 Agenda for Sustainable Development, as embodied in the 17 goals and 169 targets, call for substantial financial and technical resources
- The annual funding gap is estimated to be close to \$3 - 5 Trillion per year for the next 11 years *
- These sums are far beyond the scope of individual governments and the multilateral funding agencies to supply
- Private sector funding, capabilities and know-how need to be mobilized to sustain the new development agenda
- Islamic Finance can play a crucial role in at least leading Muslim countries towards a greater sustainable future and perhaps even helping mobilize global resources for the benefit of Muslim and non-Muslim states

* “Unleashing the potential of Islamic finance and impact investing for the SDGs,” -

[Gülçin Salıngan](#)

Deputy Director, UNDP Istanbul International Center for Private Sector Development (ICPSD), Posted Sept 26, 2018



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Understanding Sustainable Development – What does that mean?

- Sustainable development has been defined as “development that meets the needs of the present without compromising the ability of future generations to meet their own needs” (The Brundtland Commission) [Hiecki Cantell’s PRIME Finance 2019 Presentation]
- “Development is only sustainable when it takes into consideration both human needs and long-term ecological sustainability. The point then becomes specifically one of not establishing a hierarchy of values between the two, but one of excluding development paths which do not take both into consideration” [World Commission on Environment and Development, (1987), p.13]
- Four primary dimensions can be derived from the Brundtland Report: safeguarding long-term ecological sustainability, satisfying basic human needs, and promoting intra-generational and inter-generational equity.
- However, there remains confusion about how to distill this understanding of SDG into actionable criteria which can qualify a development project as sustainable at a global, national or firm level – and the much needed regulatory guidance is largely missing
- Since ultimately development requires investment, it also remains unclear if there is a hierarchy or simply an overlap between “impact investment”, “sustainable investments” and “green investments” – and, again, how do regulators both incentivize and police these overlapping deployments
- Nonetheless, Islamic Finance lends itself well, by its very structure in both sources and uses of funds having to meet ethical standards, and can play an increasingly larger role in addressing SD challenges in both Muslim as well as non-Muslim countries



The Basis for Sustainable Islamic Finance*

- In Islamic tradition, the concept of Khilafah underpins thinking on SD:
 - raises the stature of human beings as moral beings with inbuilt and active conscience which provides the ability to differentiate moral from immoral acts.
 - It inculcates the responsibility of custodianship, trusteeship and stewardship in human beings with regards to the use and ownership of physical property and environmental resources.
- In Islamic Finance there is complete clarity regarding both its sources and uses with clear definitions for both
- The main sources are Zakat and Waqf which contribute towards scaling up efforts in socially vital projects and programs:
 - **Zakat:** is the financial obligation that an Muslim has to donate a certain proportion of wealth each year to charitable causes. Payer of Zakat and the receiver of Zakat belong to two different income classes. The payer of Zakat is non-poor with surplus wealth above Nisab.
 - **Waqf:** an owner donates and dedicates a movable or immovable asset for perpetual societal benefit. The beneficiaries enjoy its usufruct and/or income perpetually. Waqf can be established either by dedicating real estate, furniture or fixtures, other movable assets and liquid forms of money and wealth like cash and shares.
- But to complement these sources of charity, Islamic Finance is successfully making forays in both Microfinance to alleviate poverty at the grassroots level while also entering the global Green Bond market to finance large sustainable development projects

* Role of Islamic Economics and Finance in Sustainable Development Goals, Abdul Ghafar Ismail & Salman Ahmed Sheikh, 2017 (Research Gate)



Islamic Finance in Action at the Grassroots Level: Akhuwat, Pakistan – World’s Largest Islamic Microfinance Institution* (An Update)

- Established in 2011:
 - *Akhuwat provides interest free loans to the economically poor so that they may acquire a sustainable livelihood*
 - *Being Sharia-compliant, the organization sees interest as a barrier to widespread proliferation of capital.*
 - *In keeping with the principles of equity and social justice, burdening the poor with exorbitant interest rates is also viewed as undermining the overarching goal of poverty alleviation.*
 - *Akhuwat believes in an inclusive society without any discrimination on the basis of caste, color, creed, gender, politics or faith. Akhuwat is a non-political and pro-poor organization*
- Currently Akhuwat Islamic Microfinance (AIM) has 800+ branches across Pakistan
- AIM has a work force of 7045 volunteers, 90073 donors and 4.5 million directly benefiting families
- Having started by extending two PKR 10,000 interest free loans in 2011, AIM crossed the PKR 100 Billion disbursement milestone in 2019 from PKR 76.5 Billion in 2018.
- Akhuwat’s collection percentage remains close to 100%
- *In its collection process, disputes are managed through Counselling (Nasiyah) and Sulh (Negotiation, Mediation)*

* <https://www.akhuwat.org.pk>



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Islamic Finance in Action at the Grassroots Level: Akhuwat, Pakistan – World’s Largest Islamic Microfinance Institution* (An Update)

- **Higher Education:** Apart from assisting 4.5 million families financially (impact on 20 million under-privileged people, this microfinance institution is setting up the first completely free world class residential university - Akhuwat University (having successfully set-up Akhuwat College)
- **Clothes Bank:** “Despite the fact that we are cut from the same cloth, the fabric that binds us is ripping at the seams.” Providing adequate clothing to the poor is high on Akhuwat’s priority list.
 - Akhuwat Clothes Bank - an extension of Akhuwat Micro-finance - applies the same philosophy.
 - Established in May 2014. Clothes collected from affluent families are repaired, washed/dry-cleaned and packed. The packed clothes are then distributed in the underprivileged communities with due respect and honor.
- **Health Care:** The aim of Akhuwat Healthcare Services is to educate people to maintain a healthy lifestyle promoting behaviors for sustained well-being.
 - It intends to provide inclusive health care experience in order to improve the health conditions of the unprivileged as well as the middle class community.
 - AHS aims to provide preventive, primary and curative health services that are accessible at affordable cost along with focusing on the physical well-being.
 - AHS strives to improve the mental and social well-being of the people, which are as important as the physical health.

* <https://www.akhuwat.org.pk>



Islamic Finance in Action at the Grassroots Level: Akhuwat, Pakistan – World’s Largest Islamic Microfinance Institution* (An Update)

- **Akhuwat’s** most amazing work is for the **Transgender Community of Pakistan**

- The community is not only deprived of the basic necessities of life, but has, traditionally, been dispossessed from the vital and most fundamental rights such as identity, self esteem, dignity and most importantly, sense of self worth.
- Khawajasiras (Transgender) have been relegated to the lowest level of society. At the fringes, they have been painfully left dependent on alms (most resorting to begging) and have remained vulnerable to societal cruelty and brutality.



- The Khawajasira Support Program (KSP) was initiated in 2011 Akhuwat’s aim to painstakingly restore their sense of self worth and establish their positive presence in the society.
- Akhuwat does not wish to reform or recreate their culture, traditions or identity, however, it plans to uplift this marginalized community by initiating and implementing sustainable efforts and programs that will guarantee self reliance, income generation and alleviate societal exclusion.
- KSP has become a symbol of strenuous efforts, unparalleled activism and truly a beacon of joy and hope for the Khawajasira community.
- Members of this extremely marginalized community have registered and opened accounts at Akhuwat.
- The community has become more aware, empowered and employed since Akhuwat’s positive intervention.
However, there is still long way to go....

* <https://www.akhuwat.org.pk>

Islamic Finance & Capital Markets: Green Sukuk

- **In November 2019, The Islamic Development Bank has successfully finalized a Sustainable Finance Framework and become the first AAA-rated institution to issue a USD 1 Bn Green Sukuk***
 - Through the new Framework, the /green Sukuk will be the first of its kind in Europe following the very first globally seen green Sukuk launched in Malaysia in 2017.
 - The Sukuk will be issued to reflect the IsDB's ambitions to help leverage greater funds from capital markets into specifically green development projects by unlocking the necessary funds through Islamic financing, a method that places great importance on improving the quality of life, social equity and fair-trade relations and; forbids profiteering at the expense of others, or investment in businesses that damage society.
- **In March 2018, the Government of Indonesia through MoF issued the very first Sovereign Green Sukuk of USD 1.25 Bn**



- The five-year issuance raised US\$1.25 billion and reached a broad range of investors including conventional, Islamic and green investors.
- In fact, the issuance was oversubscribed, signaling the growing market demand for sustainable and responsible Islamic investments.

* <https://www.isdb.org/news/isdb-announces-plans-to-launch-first-green-bond>

** <https://www.sukuk.com/article/indonesia-raises-3bn-in-sovereign-sukuk-including-1-25bn-green-sukuk-6835/>



Governance Challenges in Green & Islamic Sukuk Markets

Green & Satisfying SDG? *Development of Regulatory & Legal Framework is Critical*

- Green Bonds are clearly playing a vital role in responding to the existential threat and enormous costs posed by climate change.
- However, government regulators seem to be largely missing from this emergent market, especially so in emerging markets and Islamic countries.
- “Instead, its governance is decentralized and primarily shaped by private governance regimes (such as investment standards, certification schemes, ratings, and third-party assessment), which compete or collaborate with each other for market adoption.
- In comparison to public regulation, private governance is often faster to implement and more responsive to the needs of market participants ***but may suffer from a lack of legitimacy, accountability, and consistency and be susceptible to greenwashing.*****

Green & Satisfying Shariah? *A Framework for Ongoing Governance is Critical*

AAOIFI Governance Standard - GS 12 – Sukuk Governance Objectives of the Standard (Jan, 2020)**

- The objective of this standard is to set out a framework for governance of Sukuk issuances for the entire lifecycle of such instruments.
- Implementation of such framework, in turn, shall result in enhanced confidence of the Sukuk-holders and other stakeholders on Sukuk, and Sukuk market, particularly with regard to the compliance with Shari'ah principles and rules, fair and equitable treatment of stakeholders and transparency
- GS12, in six parts, sets out the Key Pillars & Principals of Sukuk Governance, Organs & Management Structure for Governance, Pre-Issuance Considerations, Considerations During Continuity of Sukuk, Before Intended Maturity & At Maturity or Termination and other considerations..

* Investors as Regulators: Green Bonds and the Governance Challenges of the Sustainable Finance Revolution, *Stanford Journal of International Law*, Vol. 54, No. 1, 2018, University of Connecticut School of Business Research Paper No. 18-1

** AAOIFI Governance Standard (GS) 12, Sukuk Governance, <http://aaoifi.com/sukuk-governance/?lang=en>



Conclusions

- It is clear that Islamic Finance can help bridge the large annual resource gap of \$3 - 5 Trillion in our quest to achieve the 2030 Sustainable Development Goals
- This is already being done, however modestly, through Islamic Finance mechanisms ranging from grassroots-level Islamic microfinance institutions to Green Sukuk issuance tapping the global capital markets
- One major impediment keeping Islamic Finance from growing at an even faster pace – lack of a comprehensive sukuk governance standard – has recently been removed by AAOIFI through their issuance of GS12 in January 2020
- This will provide international investors greater confidence in Islamic Finance structures and produce the required increase in investment flow for realization of SDG
- More work, however, needs to be done globally on developing a robust legal and regulatory framework for SDG qualifying financings (including one for green instruments) and regulators must play a more visible role in promoting/policing SDG investments
- Perhaps PRIME Finance can play a critical role in setting up an Islamic Finance Arbitration Panel by inviting top Islamic Law Experts as well as Sharia Experts in an effort to create a globally accepted Islamic ADR panel (in close coordination with IsDB & AAOIFI)
- Once this step has been taken, the panel can be enhanced to include SDG experts to ensure investors in Green Islamic Debt structures are provided a comprehensive ADR venue..



Thank you



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