

COVER STORY

Bahraini insurers to begin due diligence exercise for proposed merger...7

Two Libyan banks establish units to serve SMEs with Shariah compliant financing...7

Indonesia generates multimillion-dollar Islamic economy deals over three weeks as part of Halal drive...8

Ballooning inflation makes cryptocurrencies ever so appealing to Iranians...11

4th November 2020 (Volume 17 Issue 44)

IFN Turkey: Time to shine?

Turkey is a crucial market for Islamic finance (which it calls participation finance) and has made both substantial efforts to develop its sector and significant strides in moving it forward. Up until now, it has struggled to raise awareness and build market share beyond 5% of the banking market, but recent events have shown that progress is most certainly being made. Last week, IFN was delighted to present its annual IFN Turkey Forum, in which leading regulators, practitioners and stakeholders came together to discuss the challenges, opportunities and insights of the Islamic finance industry in 2020. LAUREN MCAUGHTRY writes.

Despite the huge diversification of all alternative financial instruments, the banking sector still accounts for 90% of the financial industry. Turkey hopes to raise the share of participation finance in total banking assets to 15% as of 2025, but how can it achieve that — and in particular, how can it leverage and benefit from the growth of sustainable and responsible finance to support this growth?

The country is starting from a strong footing, with a 99.8% Muslim population. Although there is no dedicated legislation for Islamic banking, the law

takes Shariah compliance into account when it comes to Islamic transactions. Out of 53 banks in Turkey, six are fully-fledged Islamic banks, including several high-profile state conversions. The capital markets are also gradually developing. The Turkish government regularly auctions gold-based Sukuk and issues Islamic lease certificates, while in 2019 both Turkish Airlines and ferrochrome producer Eti Krom announced plans to issue Sukuk. There are also three fully-fledged Islamic asset managers in Turkey.

Movement is now afoot. In January 2020, the European Bank for Reconstruction and Development said it would explore opportunities in Turkey, and expects issuances from Turkish entities to grow. Also in January 2020, AAOIFI and the Participation Banks Association of Turkey signed an MoU to collaborate in enhancing the awareness and promotion of Islamic finance in Turkey, and in February 2020 the Halal Accreditation Agency of Turkey and Pakistan's National Accreditation Council signed an MoU with a view to developing uniform standards within the Halal sector.

But are these steps enough to propel the country

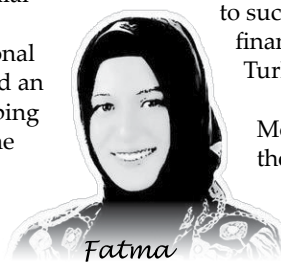


onto the world stage and fulfill its potential both on a domestic and global level?

Back to basics

How can participation finance mobilize to address the imminent challenges of the real economy and provide not just liquidity support, but solvency support to the vital Turkish SME and corporate sector? Can participation finance in Turkey and the region use this opportunity to become truly responsible, inclusive and ethical, while at the same time contributing to the country's growth and development? How can we as an industry ensure this is substance over form on a permanent basis? We asked a respected panel for a new roadmap to success for participation banking, finance and capital markets in Turkey.

Moderated by Fatma Cinar, the manager of international relations at the Participation



Fatma

continued on page 3



HONORING THE VERY BEST IN ISLAMIC FINTECH

Submissions are now open

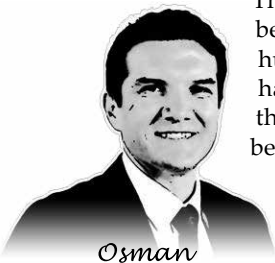
Closing date :
30th November 2020

IFN Turkey: Time to shine?

Continued from page 1

Banks Association of Turkey, the discussion ranged across a wide landscape of complex issues, with plain-speaking and frank, honest admissions from all participants — especially when it came to the challenges of handling the current coronavirus crisis.

“The pandemic has been a disaster for human lives, and it has changed a lot of things in the world — behaviors, economies and government approach”



Osman

“The pandemic has been a disaster for human lives, and it has changed a lot of things in the world — behaviors, economies and government approach,” admitted Osman Karakutuk, the executive

vice-president at Ziraat Katilim. “The growth rate in the economy has decreased very rapidly, and financial institutions have decreased their facilities. Our country has been impacted, but I think participation banks — especially state banks — have come through this well. We have not seen much interruption in our business activities during the pandemic. As a public bank, our focus has been on meeting the needs of the Turkish people, in order to help them withstand that negative economic consequences of the pandemic. Branches have continued their services and successfully used alternative channels like internet and mobile banking.”



Dr Kinan

The central bank has introduced a substantial raft of measures to support the economy during the crisis, including reducing the policy rate from 10.75% to 9.75%, providing banks with as much liquidity as needed through intraday and overnight standing facilities, raising the liquidity limits of primary dealers of open market operations and lowering foreign exchange reserve requirement ratios by 500bps and offering banks with targeted additional liquidity facilities to secure uninterrupted credit flow to the corporate sector.

“The main issue is liquidity and financing of corporate customers,” explained Osman. “That’s why we accelerated our financing to SME and corporate clients, to ensure that sufficient liquidity with reasonable profit rates could be provided to support the real economy. We’ve provided a business support package of TRY5 billion (US\$594.03 million), as well as restructuring the existing facilities of corporate clients and providing them with additional finance as needed to support their cash flow.

But, pointed out Fatima, the pandemic could also be an opportunity for SMEs, as the banks look to support them strongly and lots of additional measures are made available. Is it a risk issue converted into an opportunity?

Asst Prof Dr Kinan Salim, the head of Islamic digital economy at the International Centre for Education in Islamic Finance, believes so. “COVID-19 has shown the fragility of our economies,” he said. “One big shock has had a huge impact on all businesses across the world. First, we see disruption in the supply chain, and the second is the drop in market demand. And we are seeing that SMEs are far more financially fragile when market demand is down. They still need to pay their bills and salaries, so they are accumulating losses. Some banks are trying to help by postponing payments, but that doesn’t solve the real problem. This crisis shows the need to create more resilient economies and businesses. This is everyone’s responsibility. But it gives an opportunity for participation banks to develop

new solutions to fix these systematic problems. This can be achieved through sustainable and responsible banking that can make a positive impact on society: driven by profit, but always keeps an eye on social and environmental performance.”

“This crisis shows the need to create more resilient economies and businesses. This is everyone’s responsibility”



Ahmet

Sustainable finance is of course a key trend for this year, and Turkey demonstrates some unique opportunities within the space. Ahmet Ilyas Collu, the vice-president and head of international banking for the Treasury and Strategy Group of Vakıf Katilim Bankası, urged the importance of building on the momentum within the responsible finance sector, particularly around sustainable energy. “We are importing a lot of energy and we want to produce our own renewable energy within Turkey,” he explained. “We also support the municipalities in their investment in technology, building smart cities, smart car parking, smart transportation, smart agriculture and waste recycling. Based on our investments in sustainable energy, we plan to issue a green Sukuk down the line, possibly a local or an international Sukuk. Green Sukuk is an attractive concept — we’ve only seen one green Sukuk issuance in Turkey this year, from an investment bank, and as a state-owned participation bank we want to be active in this sector so we are preparing for this.”

continued on page 4

IFN Turkey: Time to shine?

Continued from page 3



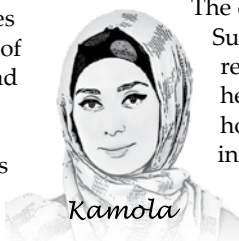
Omer

Omer Cekin, the head of the Participation Banking Unit at the Banking Regulation and Supervision Agency, gave a comprehensive summary of the

agency's achievements in recent years in developing a constructive environment for Islamic finance in Turkey. "The regulatory framework is very important, and we are a sophisticated country when it comes to infrastructure," he concluded.

“The regulatory framework is very important, and we are a sophisticated country when it comes to infrastructure”

And finally Kamola Bayram, an assistant professor at KTO Karatay University, raised the point of Islamic finance education as a focal point of the wider ecosystem, particularly as a means of developing the human resource capacity for the participation banking sector in Turkey. "We have six participation banks in Turkey and 16,000 people employed in this sector," she noted. "But when we look at the share of Islamic finance in the banking sector it is still just 5%, and Islamic finance education is very important as a means of reaching the desired market share of 15–20%. Research shows that increasing the number of banks and branches alone is not enough. We need to increase public awareness, which comes with education. I receive a lot of questions from students abroad who want to continue their studies — of course Malaysia and the UK and Gulf countries are popular, but today in



Kamola

Turkey we also have the infrastructure, with 10 universities, to invite students to come here to continue their Islamic finance studies. In Turkey, we need to promote these opportunities more, perhaps through an initiative like the FAA [Finance Accreditation Agency] in Malaysia, to help it flourish."

“Research shows that increasing the number of banks and branches alone is not enough. We need to increase public awareness, which comes with education”

"As of today, the market share of participation banks has reached 7% with assets of more than US\$53 billion," revealed Fatima at the end of the session, noting that growth is continuing despite the challenges.

Funding, fintech and responsible finance

With the Republic returning to the market via euro and dollar issuances in May 2020, the second panel of the IFN Turkey Forum, moderated by Tarik Akin, the division director (Islamic finance) at the Finance Office of the Presidency of the Republic of Turkey, looked at the capital markets, funding, fintech and responsible finance aspects of the market.

The discussion explored what role Sukuk could play in supporting recovery, how technology can help promote innovation, and how sustainable and responsible investment can make further progress within Turkey.



Tarik Akin

Dr Sutan Emir Hidayat, the director of the Islamic Economy Supporting Ecosystem at the National Committee for Islamic Economy and Finance, gave his experience from an Indonesian perspective on the current outlook for the global industry — particularly the downside risk in 2021 and the respective repercussions for the Islamic financial industry in Turkey. "When it comes to 2021, I expect the global growth of the Islamic financial industry will continue to slow," he predicted. "We foresee an expected mild recovery, and low to middle single-digit growth. Notably, COVID-19 vaccination should be a priority, and Sukuk are likely to be a solution to finance the procurement of these vaccines."



Dr Sutan

“When it comes to 2021, I expect the global growth of the Islamic financial industry will continue to slow”

A key element of the discussion was Turkey's target of a participation banking market share of 15% by 2025 — is this goal realistic?

"There are only three OIC countries that are G20 members, and Turkey is one of them. It plays a vital role in regional economic development, including Islamic finance," stressed Dr Sutan. "But there are several challenges that need to be tackled. These include literacy and awareness — there is a clear positive relationship between literacy and financial inclusion. There is still a lack of a clear Islamic financial legislative framework and infrastructure. There is a need for more product innovation — this

continued on page 5

IFN Turkey: Time to shine?

Continued from page 4

is limiting participation banks because of a lack of products. A more active secondary market for Sukuk is also needed. The previous issue of double taxation of Sukuk has been resolved, but more companies need to be encouraged to issue. Currency risk is another issue. Dollar-denominated Sukuk is a risk because the lira is so volatile. If you can tackle all these things, with a clear master plan for Islamic finance in Turkey, then Inshallah you can achieve the 15%."

“There is clearly room for further growth in Turkey for participation banks. I think to achieve this, capitalization, a larger labor force and digitization are key drivers”



Tarik Borekci

But not everyone was as optimistic. Tarik Borekci, the vice-president and head of treasury in the Treasury & Strategy Group of Vakif Katilim Bankasi, gave a detailed

financial analysis of the specific figures involved. "There is clearly room for further growth in Turkey for participation banks. I think to achieve this, capitalization, a larger labor force and digitization are key drivers," he concluded. "But from a financial point of view, capitalization is the main issue if the sector is to reach 15%. There is a TRY60 billion [US\$7.13 billion] gap between the projected and the required total liquidity



Leilya

figure that is needed to drive the balance sheet to reach a 15% market share. I don't think the banks necessarily have a capital plan to inject this much, so it might not be a realistic figure. But if new players join into the market, then these figures and projections could change."

Tarik Borekci was also optimistic about the potential to develop a local Sukuk market. "Sukuk gives us a change to access the longer capital markets and diversify our funding sources. Participation banks already actively issue Sukuk in the local market, and with the improvement of the pension fund system, where participants choose Islamic funds, the local Sukuk market certainly has the potential to grow further," he noted.

“The first pillar the government should focus on is increasing awareness. This is crucial in the development of Islamic fintech”

Islamic fintech is another promising growth area for Turkey. Leilya Shamel, the associate director of DDCAP, explored the opportunities within the sector. "Turkey has great potential here. First, because of its geographical position lying between Europe and Asia, which opens up a bigger market of both users and providers. And second, the population of Turkey, which is very entrepreneurial and majority Muslim.

The first pillar the government should focus on is increasing awareness. This is crucial in the development of Islamic fintech. Second is building trust so that market participants feel secure, followed by government support,

building a regulatory framework and supporting it through sandboxes, accelerators and so on. Then the third pillar is the availability of funding. The developers of fintech usually come from small start-up companies and they struggle with access to funding forces. A bigger role could be played by venture capital, private equity and investment funds to develop this sector."



Alaa

Alaa Alaabed, the chief research officer at Wethaq Capital Markets, highlighted more developments within the capital markets, particularly the growing focus on a more inclusive and sustainable path to recovery out of the global pandemic. "We are seeing the growth of ESG [environmental, social and governance] funds outperforming, and there is an increasing interest from both issuers and investors for green and sustainable issuers," she explained. "In the Islamic space, we have seen a number of initiatives that are very relevant here, including in Turkey. The IDB issued its first-ever sustainability Sukuk in June 2020. A catalyst like this could really, it is hoped, encourage and spur on green and social sustainable issuance going forward. Another point is the increasing focus on Waqf as a funding instrument for societies."

Finally Wail Aaminou, group CEO at Al Maali Group, discussed how Turkey could apply the UN Sustainable Development Goals to its participation finance activities.



Wail

"The most important element is bringing together Islamic finance and impact finance under the same umbrella," he urged. "It's an interesting value proposition, but marketing is vital. We need to bring capital, we need to bring talent and we need to bring lots of different players on board to make it happen."

To hear the full discussion and derive full value from these cutting-edge debates, you can view the complimentary event recording [here](#). ☺