

THE AUSTRALIAN

Islamic finance a chance to connect

STIRLING LARKIN THE AUSTRALIAN AUGUST 30, 2014 12:00AM



In the early 1960s, the convergence of political and socio-economic factors ignited interest in Islamic financial practices. Source: AFP

T.E. LAWRENCE, also known as Lawrence of Arabia, said that all the revision in the world would not save a bad first draft — for the architecture of the thing comes or fails to come in the first conception and revision only affects the detail and ornament.

These wise words hold deep truth and carry merit for us in wealth management, where it is not only imperative that we achieve meritorious returns for our clients, but also that we guide them down an enlightened path.

As often stated in this column, investing without an established world view is unwise.

Consequently, any such approach or world view that does not respect the importance and gravitas of Islamic finance in the contemporary global investment mix is both flawed and shortsighted and is surely destined to not only underperform, but also show its Achilles heel when challenged.

Experienced Australian ultra- high-net-worth investors are well aware that the conversation surrounding Islamic finance is far more than just one about Australia's potential to rival Qatar as the world's largest LNG exporter or the nuances of doing business in Malaysia, Brunei or Indonesia.

They know that this alternative framework has to be understood, respected and engaged when met along the many touchpoints throughout the Australian economy and Asia-Pacific regional markets.

Also, events of recent weeks have made this conversation timelier than ever before.

On August 21, the Saudi Capital Markets Authority announced it would be finally allowing foreign investors the opportunity to invest in the Kingdom's stockmarket.

Up until now, many keen to invest in sharia-compliant indices looked to international ETF index trackers such as NewFunds Shari'ah Top 40 Index ETF (NFSH40: SJ) in Africa, Deutsche Bank's S & P Europe 350 Shari'ah UCITS ETF (XSHE: GR) or Goldman Sachs' CNX Nifty Shariah Index Exchange Traded Scheme, incorporated in India.

But even more relevantly than solely focusing in on any single isolated capital market investment, it is firstly important to grasp that Islamic finance and sharia-compliant standards produce a far larger footprint across many parts of our "real" economy here in Australia than first thought.

Whether in the Gulf, Africa, Europe, Southeast Asia or domestically within Australia, Islamic finance is often the linchpin of many existing investments, transactions and trade agreements.

Further still, these relationships are only set to grow and more deeply immerse themselves into our existing and future commercial and investment lives.

Innes Willox, CEO of the Australian Industry Group and vice-president of the Australia-Saudi Business Council, believes that "as our trade with the Middle East grows and diversifies, an awareness of Islamic finance is going to be increasingly important to Australian exporters, if not for their own use then certainly for a better understanding of their market and customer base."

It is thus essential to take a step back and ask what is Islamic finance? What are their guiding principles and what is its relationship with Islam itself?

In answering that, the following needs to be discussed.

Firstly, economics generally makes the assumption that human behaviour is rational and therefore presumes rationality as a given.

Religion, by contrast, considers humans to be fallible, thus potentially irrational, and aims to influence our behaviour.

Bringing religion into our economic lives, then, means bringing moral values into what is supposed to be free of such values.

Some would think the two, religion and economics, never shall meet, but in reality they do.

Moral values, often derived from the major religions, are increasingly being introduced into our economic lives in the form of environmental concerns, protection of the rights of labour and promotion of fairness in trade.

In finance, for instance, the increased level of interest in socially responsible investments is a sound case in point.

It is in Islamic finance, however, where economics and religion truly come together. Of paramount importance, the principles of Islamic financial transactions are that they do not involve any activities prohibited by Islamic law. These transactions must not involve "riba", which is the giving or receiving of interest, and should avoid "gharar" which is considered to be uncertainty, risk or speculation.

In essence, riba includes interest charged on lending money whereas gharar includes excessive uncertainty regarding essential elements of a contract, such as a price in a contract of sale.

The inclusiveness of Islamic finance therefore promotes sharing of risk and reward between contracting parties, but it does not allow for the perception of speculation or unjustified risks.

Contemporary Islamic finance incorporates these principles and other doctrines of the Muslim faith

in a wide variety of products to meet the growing global demand for sharia-compliant investment and financing.

In the early 1960s, the convergence of political and socio-economic factors ignited interest in the revival of faith-based Islamic financial practices, including the prohibition of usury or the giving or receiving of interest.

Today, this interest is seen again across the Gulf, Africa and Australia's nearest neighbours in Indonesia, Malaysia, Brunei, Pakistan and India.

Africa, in particular, is an important case study for Australian companies and investors.

This is due to the rising popularity of these compliant investments combined with the increasing presence of our largest trading partner, China.

Numerous Australian mining and exploration companies that are listed in Australia on the ASX are already heavily engaged in Africa and are increasingly competing with the Chinese, who have taken the time and diligence to better educate themselves on the principles and expectations of Islamic finance.

Accordingly to Ernst & Young, "Africa, with its Muslim population of approximately 500 million people, represents a huge untapped market for global banks and insurance companies to grow their markets."

They also suggest that the "key to the continued growth of the African sharia industry will be its ability to develop financial products that provide sharia-compliant substitute solutions that match conventional financial products and instruments".

During a time when a small few are making a lot of noise about the isolation of Islam, the conversation surrounding the inclusiveness of Islamic finance across communities and its benefits for many should be warmly welcomed by all.

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