

Participation asset management: A long way to go



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As it offers a totally different model than conventional finance, it has got to have a different name; however, neither 'Islamic finance (or Shariah compliant finance)' – the term commonly used – nor 'non-interest bearing (interest-free) finance' are necessarily the right terms. This is because:

- 1) The alternative is not Judeo-Christian finance. There is no need to put a religious tag as it is not meant for Muslims only, nor does it mean that non-Muslims cannot utilize this financial system. Although this one is affirmative, it is like using the term 'Islamic terrorism'! The very reason why we reject the 'Islamic' tag in Islamic terrorism may well be asserted for 'Islamic finance'.
- 2) The only differentiating feature of this system is not just being 'interest-free'. There is much more to it, with the main ones being:
 - (i) sharing risks and rewards (sharing 'Rizq' with 'Rizq' meaning 'everything given by God for livelihood; according to some linguistics, it is believed to be derived from the word 'risk')
 - (ii) not engaging in forbidden transactions or investments such as gambling, alcoholic beverages, drugs, etc, that are detrimental to society
 - (iii) avoiding unclear terms in contracts that may end up in a hazardous sale or deception
 - (iv) being environment-friendly, and
 - (v) decent corporate governance.

The essence is participating in risks and rewards, hence the term 'participation'. It is by definition embracing all people whether Muslim or not and it is already gaining traction in financial jargon.

Finance stands on four pillars: banking, asset management, insurance and other financial intermediations (such as leasing, forfaiting, factoring and so on). There are clear differences between participation and conventional alternatives of banking and insurance systems. Other intermediation is kept out of discussion as they have to be discussed one by one which is beyond the scope of this article, for example, leasing is in essence compliant with participation principles whereas factoring is not at all by its nature.

However, it is not the case when it comes to asset management. We need to establish the participation alternative of asset management together with its distinguishing principles, institutions, products and services.

Notwithstanding the current stagnant outlook, there is quite an interest and potential in participation asset management. Muslim countries' sovereign wealth funds (SWFs) are larger than US\$2.5 trillion – the demand.

Meanwhile, emerging markets such as Turkey, Malaysia and Indonesia offer high yields in vast amounts of investment opportunities – the supply. The match between the two would not only serve the economic purposes but would also strengthen ties between Muslim nations. On the other hand, lucrative investment opportunities in emerging markets are of interest to all investors in the world, especially the developed world craving for returns. Also

environmental, social and governance investors are very comfortable with participation finance, creating additional demand.

Review of 2017

2017 has been a year of cooperation among participation finance firms in setting up new equity and real estate investment funds. The two prevailing issues of financial illiteracy and complex regulations do not seem to be resolved yet resulting in slow growth of assets under management (AuM) in participation asset management.

Financial illiteracy is in fact a general problem within the finance sector, and even a more severe one within the participation part. Nevertheless, we have seen initiatives to train students and teachers about finance led by NGOs in Malaysia and Turkey.

Regarding the regulatory environment in general, the lack of one universal standard-setting body for the whole participation finance industry remains a major challenge in its global recognition and acceptance. Although there are bodies like AAOIFI (Bahrain) and the IFSB (Malaysia), there can also be a higher authority, say at the Committee for Economic and Commercial Cooperation of the Organization of Islamic Cooperation (COMCEC) level, playing the joint role of the Basel Committee and the International Organization of Securities Commissions.

Meanwhile, there are new regulatory developments in Morocco and Turkey to develop participation finance institutions and products. Morocco started Shariah compliant banking in early 2017 and Turkey enacted an auto-enrolment private pension regulation whereby participation pension funds have to be made available by all pension companies. Turkey also set up a sovereign wealth fund and stated bolstering participation finance as one of its main objectives.

Preview of 2018

In 2018, participation asset management will be more popular due to the rise in IPOs in the Muslim world triggered by the upcoming IPO of Saudi Aramco. In addition, low oil prices will lead some oil-rich Muslim investors to utilize products and services in participation asset management, further leading to increased AuM.

There are also initiatives to improve cooperation among the exchanges of COMCEC member states which may facilitate the cross-listing of stocks and easy access to a wider investor base.

Another initiative, based on the fact that investors in Muslim countries have a tendency to invest in real estate, is to set up a real estate exchange whereby properties in COMCEC member states would be traded. Real estate investment funds can also play a significant role in attracting foreign investors into the property markets.

The world economy is finally expected to get into a growth stage in 2018. Therefore, we may expect private equity deals to increase and hence, an opportunity for participation asset managers to set up private equity investment funds (PEIFs) and provide investors with potential high returns derived directly from the growing businesses.

Conclusion

As the title of this article suggests, there is a long way to go for participation asset management. Improving financial literacy, developing international standards, engaging SWFs and private pension systems so that they are encouraged to move into the industry, launching new venues of close cooperation among Muslim countries via joint exchanges or PEIFs are all the very first steps to be taken to bolster participation asset management. ☺