



**BRIEF ON FINANCE**

**OIC/COMCEC-FC/29-13/D(25)**



**COMCEC**

# **CCO BRIEFS**

# **FINANCE**

**COMCEC COORDINATION OFFICE**

**MAY 2013**



## BRIEF ON FINANCIAL COOPERATION

Over the last few decades, the global financial system has become more and more integrated. The economic and financial fragilities emerging in a part of the world have the potential to effect the entire global economy and financial system. Recent financial crisis demonstrated the extent of this interconnectivity and highlighted the need for international cooperative action by financial institutions and regulatory authorities.

Financial system has a vital role in economic development. One of the basic functions of the financial system is the transfer of savings to entrepreneurs. The weaknesses in the financial system negatively effect the ability of entrepreneurs to access finance which, in turn, leads to delays in required investments and decreases in production levels. On the other hand, a powerful financial system contributes to the economic growth by effective allocation of resources.

Despite its essential role in the progress of efficiency and equality in a society, 2,7 billion people (70% of the adult population) in emerging markets still have no access to basic financial services, and a great part of them come from countries with predominantly Muslim population<sup>1</sup>.

A significant number of Islamic countries has a considerable capital surplus that can be channeled to investments in line with the development needs and capital export requirements of the member countries. Through its one of the core principles, namely Strengthening Solidarity, the COMCEC Strategy, adopted by the 4<sup>th</sup> Extraordinary Islamic Summit in 2012, aims to enhance financial cooperation among the Member States.

### SOME FINANCIAL FIGURES

Except for 2009, the COMCEC Countries recorded high real GDP growth rate from 2007 to 2011 (*see Table 1*). They had a much better performance than the developed countries and the world, and their performance was almost as good as the developing countries' (excluding China). However, GDP Growth rates in COMCEC countries fell below the rates of emerging economies.

**Table: 1 Real GDP growth rates** (%)

ECONOMY	2007	2008	2009	2010	2011
World	4,04	1,37	-2,33	4,03	2,72
Developing economies	7,91	5,08	2,52	7,48	5,79
Developed economies	2,58	-0,09	-3,97	2,66	1,38
Developing economies excluding China	6,13	3,71	0,37	6,46	4,54
The COMCEC Countries	5,66	3,96	0,61	5,38	4,51

Source: UNCTAD, UNCTADstat

The total GDP of the COMCEC Countries was USD 6,9 trillion in 2007, and it increased approximately by 5,5% between 2007 and 2011, and it is expected that the total GDP of the COMCEC countries in 2012 and in 2013 will be USD 9,04 and 9,06 trillion, respectively<sup>2</sup>. The COMCEC Countries' share in the World GDP has increased constantly in parallel with the Emerging and developing countries share in the World total GDP.

<sup>1</sup> Mahmoud Mohieldin, Zamir Iqbal, Ahmed Rostom, Xiaochen Fu, *The Role of Islamic Finance in Enhancing Financial Inclusion in OIC Countries*, The World Bank December, 2011, p:2

<sup>2</sup> GDP in PPP, International Monetary Fund, World Economic Outlook Database, October 2012

After the recent global economic crisis, there has been a dramatic decrease of 39,4 percent in total global FDI Flows between 2007 and 2009. Along with the recovery in the global economy, although FDI flows could not reach the pre-crisis level in all economies as indicated in table 2, there has been a slight recovery in global foreign direct investment flows. There was a remarkable FDI Flow to the COMCEC countries in 2008 reaching to USD 171,6 billion in total. However it declined to USD 133 billion in 2009 in parallel to the global decline. There was a fractional increase in 2010 up to USD 135 billion followed by a slight decline in 2011 to USD 134 billion (*see Table 2*).

**Table: 2 FDI Flows**

(Current US Dollars in Billion)

ECONOMY/YEAR	2007	2008	2009	2010	2011
World	1.975,5	1.790,7	1.197,8	1.309,0	1.524,4
Developing economies	574,3	650,0	519,2	616,7	684,4
Developed economies	1.310,4	1.019,6	606,2	618,6	747,9
The COMCEC Countries	145,8	171,6	133,1	135,2	134,0

Source: UNCTAD, UNCTADstat

FDI flows to the COMCEC Countries were concentrated in a few numbers of them. FDI flows to ten top COMCEC Countries accounted for 77 per cent of the total FDI flows to all of COMCEC Countries<sup>3</sup>.

Table 3 indicates that there had been a notable increase of 57% in total global reserves from 2007 to 2011. The world total reserves (including gold) were equivalent to USD 10,7 trillion in 2011 and 70% of this amount was recorded in the developing countries. Their total reserves rose significantly reaching to USD 7,4 trillion in 2011. Although this can be explained, in part, by the increasing trade flows and the large surpluses of some developing countries, such as China, the newly industrialized Asian countries and the oil exporting countries in the Middle East, it is more likely due to efforts for financial reforms in some developing countries with chronic current account deficits to improve their reserves position<sup>4</sup>.

**Table: 3 Total reserves (including gold)**

(Current US Dollars in Trillion)

ECONOMY/ YEAR	2007	2008	2009	2010	2011
World	6,9	7,5	8,6	9,7	10,7
Developing economies	4,5	5,2	5,9	6,8	7,4
Developed economies	1,8	1,8	2,1	2,4	2,7
The COMCEC Countries	1,2	1,4	1,4	1,5	1,7

Source: UNCTAD, UNCTADstat,

The total reserves (including gold) of the COMCEC Countries amounted to USD 1,7 trillion in 2011. Although there was an increase in the amount of total reserves, the share of the COMCEC Countries in total reserves of developing countries showed a decrease from 27% in 2007 to 22% in 2011. As was the case in the FDI Flows, ten COMCEC Member countries had 82 percent of the total reserves of the COMCEC Countries. Furthermore, Saudi Arabia itself (USD 541 billion) had 33 percent of the total reserves<sup>5</sup>.

According to World Bank statistics, the amount of domestic credit provided by the banking sector was 165% of GDP in the world in 2011 and this increase in high income countries was

<sup>3</sup>UNCTAD, FDI Statistics, (Indonesia, Saudi Arabia, Turkey, Kazakhstan, Malaysia, Nigeria, UAE, Iran, Lebanon, Turkmenistan)

<sup>4</sup>SESRIC Annual Economic Report 2012

<sup>5</sup>UNCTAD, UNCTADstat

203% of GDP. This amount was only 42% of GDP in the COMCEC countries which is almost the same as low income countries (40%). Only Lebanon has a ratio of above the world average with 174 percent.

According to “*World Islamic Banking Competitiveness Report 2013-Ernst&Young*” Islamic Banking assets-including commercial bank assets- grew by an annual average of 19% in the period 2008-2011 (2011: 24%). Total assets reached to USD 1,3 trillion in 2011, and in some countries having an advanced Islamic Banking system, this sector grew 50% faster than the overall banking sector. It is expected that the global Islamic Banking assets (including commercial bank assets) will reach USD 1,8 trillion and USD 2 trillion in 2013 and in 2014, respectively.

The Islamic Banking Assets also concentrate in a few COMCEC Countries. The top four markets in the COMCEC Region account for 84% of industry assets. Top 20 Islamic Banks constituted 55% of the total Islamic banking assets and are concentrated in 7 countries, namely Saudi Arabia, Kuwait, the United Arab Emirates, Bahrain and Qatar, Turkey and Malaysia<sup>6</sup>.

Despite its high potential in financial cooperation, The COMCEC region has various challenges regarding implementation of financial cooperation. The main challenges of financial cooperation among the COMCEC Members are as follows<sup>7</sup>:

- *More integration with the global markets rather than with themselves*
- *Lack of sound financial institutions*
- *Huge diversity in financial sector development across the region*
- *Lack of reliable data*
- *Small size of financial markets*
- *Lack of differentiated products*

### Cooperation Efforts under the COMCEC

Finance is one of the significant cooperation areas of the COMCEC. The ideas for enhancing financial cooperation under the COMCEC date back to its initial meetings. The Financial and Monetary issues were defined as one of the cooperation area by the Former Plan of Action. The Cooperation efforts in this area have been intensified and deepened in recent years. The Ongoing efforts for the COMCEC in this field have been carried out under the cooperation among the Stock Exchanges Forum, COMCEC Capital Markets Regulators Forum and Central Banks and Monetary Authorities.

Furthermore, The COMCEC Strategy, adopted by the 4<sup>th</sup> Extraordinary Islamic Summit in 2012, determined the finance as one of the cooperation areas of the COMCEC and the Strategy. The Strategy determines “*deepening financial cooperation among the member countries*” as the strategic objective of the COMCEC in this field. The Strategy identifies, “*Regulatory and Supervisory Cooperation*”, “*Capital Flows*”, “*Visibility of Financial Markets*”, “*Training, R&D Activities and Statistics*” as output areas in its finance section and specifies several expected outcomes under each of them.

For the realization of its objectives and expected outcomes in its finance section, the Strategy envisages the establishment of COMCEC Finance Working Group which will provide a regular platform for the experts from Member Countries to discuss their common issues in

<sup>6</sup>World Islamic Banking Competitiveness Report 2013-Ernst&Young

<sup>7</sup> COMCEC Strategy

finance sector and share their knowledge and experiences. The Finance Working Group will hold its 1<sup>st</sup> meeting this year.

### **Ongoing Efforts under the COMCEC:**

– **Cooperation among the Stock Exchanges:** The Cooperation among the Stock Exchanges was launched in 2005 by the COMCEC in line with the decision taken by the 20<sup>th</sup> Session of the COMCEC. Accordingly, the OIC Stock Exchange Forum was established for the harmonization of the rules and regulations governing market operations, for opening communication channels for the stock exchanges of the COMCEC Member Countries and relevant institutions. The Forum has held 6 meetings so far. The 7<sup>th</sup> Meeting of the Forum will be held in September 2013 in İstanbul.

S&P OIC/COMCEC 50 Shariah Index which is the Forum's one of the most important projects was introduced on 22<sup>nd</sup> June 2012 in İstanbul. The official launching ceremony of the Index was held during the 28<sup>th</sup> Session of the COMCEC. The Index was designed to measure the performance of 50 leading companies from the 19 Member States.

The Forum also works on the introduction of sukuk and other Islamic capital market instruments and continues to facilitate and coordinate the work of the Task Forces and project groups formed under the Forum.

– **Cooperation among the Capital Markets Regulatory Bodies:** In line with the relevant resolutions of the 25<sup>th</sup> and 26<sup>th</sup> Sessions of the COMCEC, Capital Markets Board of Turkey (CMB) organized COMCEC Capital Markets Regulatory Authorities Conference and Roundtable on 16-17 September 2011 in İstanbul. Accordingly, the “COMCEC Capital Market Regulators Forum” was established among the COMCEC Member Countries to increase coordination and cooperation in regulatory and legal infrastructure with a view to achieving more harmonized policies and regulations among the Member Countries. The Main focus of the Forum is to support market development and reinforce capabilities of regulatory authorities in the COMCEC Region.

The 1<sup>st</sup> Meeting of the COMCEC Capital Markets' Regulators Forum was held on September 27<sup>th</sup> 2012 in İstanbul. The meeting decided the formation of the Task forces on “Capacity Building”, “Market Development”, “Islamic Finance” and “Financial Literacy”. The 2<sup>nd</sup> Meeting of the COMCEC Capital Market Regulatory Forum will be held in September 2013 in İstanbul.

– **Cooperation among the Central Banks and Monetary Authorities:** In line with the relevant resolution of the 24<sup>th</sup> Session of the COMCEC, cooperation among the Central Banks and Monetary Authorities of the Member Countries has been revitalized. Since then the Central Banks and Monetary Authorities of Member Countries have been convening annually. The Central Banks and Monetary Authorities in their meeting in October 2009 agreed to meet regularly to share experiences in enhancing the payment systems and capacity building in the member countries. So far, several capacity building programs have been successfully implemented in various member countries.

The Central Banks and Monetary Authorities have convened twelve times till now. The 12<sup>th</sup> Meeting of the Central Banks and Monetary Authorities was held on 14-15 May 2012, in İstanbul. The meeting decided to establish working groups to prepare technical background papers in the following areas: Payment Systems, Macro-Prudential Regulations, and Liquidity Management in Islamic Finance. The next meeting will be held in the Kingdom of Saudi Arabia in 2013.