



Standing Committee
for Economic and Commercial Cooperation
of the Organization of Islamic Cooperation (COMCEC)

Infrastructure Financing Through Islamic Finance in the OIC Member Countries—Part 2

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Presentation Plan

- Background and Methodology
- Country Case Studies—Results
- Key Issues and Policy Recommendations

Introduction

- Infrastructure investments needs are huge
 - Total investment needs per OIC member country per year USD 22.1 billion (2016-2040)
 - Investment gap per member country per year USD 4.9 billion
- There is a need to look for alternative sources of financing
- One option is to tap into Islamic finance
 - Over USD 2 trillion in assets
 - Key features of risk-sharing and direct linkages with the real economy
 - Ideological standing of ethical, social and legal ethos compatible with infrastructure financing



Objectives of the Presentation

- Analyse the prospects and challenges facing infrastructure financing using Islamic finance in selected OIC member countries
- Identify policy recommendations to enhance the role of Islamic finance in promoting investments in infrastructure sector





Case Studies and Methodology

- Criteria used for choosing countries for case studies
 - Ensure regional diversification (Africa, Arab and Asia)
 - Countries with different levels of development in terms of income group classifications of World Bank (lower-middle income, higher-middle income and higher income groups)
 - Size of the Islamic financial industry
 - Diversity in legal systems (Islamic law, common law and civil law)
- The study examined
 - Five OIC countries (Indonesia, Malaysia, Nigeria, Saudi Arabia and Sudan)
 - One non-OIC country (United Kingdom)



OIC Member Countries Used for Case Studies

Country	Region	Legal System Family ^e	Income Grouping	Size of IF sector: % of National Banking Assets ^a
1. Indonesia	Asia	Civil Law	Lower Middle Income	5.6
2. Malaysia	Asia	Common Law	Upper Middle Income	30.0
3. Nigeria	Africa	Common Law		0.28
4. Saudi Arabia	Arab	Islamic/ Civil Law	High Income	51.1
5. Sudan	Africa	Islamic/ Common Law	Lower Middle Income	100

[Table 1.3] Sources IFSB (2017); OJK 92017); BNM (2017); Central Bank Nigeria; World Bank (2004)



Framework of Analyses

1. Infrastructure Related Strategy and Policies
2. Legal and Regulatory framework
3. Government and Government Linked Companies
4. Islamic Banks
5. Islamic Nonbank Financial Institutions
6. Islamic Capital Markets
7. Islamic Social Sector
8. Multilateral Development Institutions



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Infrastructure Investments & Islamic Finance: Indonesia

Infrastructure Investments	2016-2040 (USD Bn)	Average/ year (USD Mn.)
Current trends (CT)	1,642.00	65.68
Investment need (IN)	1,712.00	68.48
Gap between IN and CT	70.00	2.80

Dec 2017	Size (USD billion)	Infrastructure Financing (USD bn.)
Islamic Banks	30.30	2.55
Takaful	2.89	
Sukuk Outstanding	40.63	
Total	73.82	



Infrastructure Investments & Islamic Finance: Malaysia

Infrastructure Investments	2016-2040 (USD Bn.)	Average per year (USD Bn.)
Current trends (CT)	383	15.32
Investment need (IN)	460	18.40
Gap between IN and CT	77	3.08

Sector	Size (USD bn.)	Infrastructure Financing (USD bn.)
Islamic Banking	204.4	8.95
Takaful	7.2	
Sukuk Outstanding	187.1	
Total	398.8	

Infrastructure Investments & Islamic Finance: Nigeria

Infrastructure Investments	2016-2040 (USD Bn.)	Average per year (USD Bn.)
Current trends (CT)	657	26.28
Investment need (IN)	878	35.12
Gap between IN and CT	221	8.84


Sector	Size (USD bn.)	Infrastructure Financing (USD bn.)
Islamic Banking	0.298	0
Takaful	-	0
Sukuk Outstanding	0.340	0.340
Total	0.648	0.340



Infrastructure Investments & Islamic Finance: Saudi Arabia

	2016-2040 (USD Bn.)	Average per year (USD Bn.)
Current trends (CT)	499	19.96
Investment need (IN)	613	24.52
Gap between IN and CT	115	4.60

Sector	Size (USD bn.)	Infrastructure Financing (USD bn.)
Islamic Banking	371.23	13.884
Takaful	15.12	
Sukuk Outstanding	52.55	
Total	438.90	



Infrastructure Investments & Islamic Finance: Sudan

Infrastructure Investments	2016-2030 (USD Bn.)	Average per year (USD Bn.)
Current trends (CT)	-	-
Investment need (IN)	50.967	3.185
Gap between IN and CT	-	-

Sector	Size (USD bn.)	Infrastructure Financing (USD bn.)
Islamic Banking	11.765	0.422
Takaful	0.292	0
Sukuk Outstanding	0.578	
Total	12.63	

Infrastructure Related Strategy and Policies



- Long, medium and short term plans to identify projects most beneficial to the economy
 - Indonesia: Five-year Medium Term National Development Planning
 - Malaysia: Vision 2020 (1991); 10 year policy documents; five year plans
 - Nigeria: National Integrated Infrastructure Masterplan 2014-2043
 - Saudi Arabia: Vision 2030
 - UK: National Infrastructure Commission; Infrastructure and Projects Authority



PPP Framework

- National level policy framework to facilitate investments by the private sector
 - Indonesia: PPP Directorate of Indonesia, Ministry of National Development Planning; Committee for the Acceleration of Priority Infrastructure Delivery (KPPIP)
 - Malaysia: PPP Unit under the Prime Minister's Department
 - Nigeria: Infrastructure Concession Regulatory Commission
 - Saudi Arabia: National Centre for Privatization and PPP
 - Sudan: Set up a PPP Unit in 2018 with support from World Bank



Status of PPP Procurement Regimes

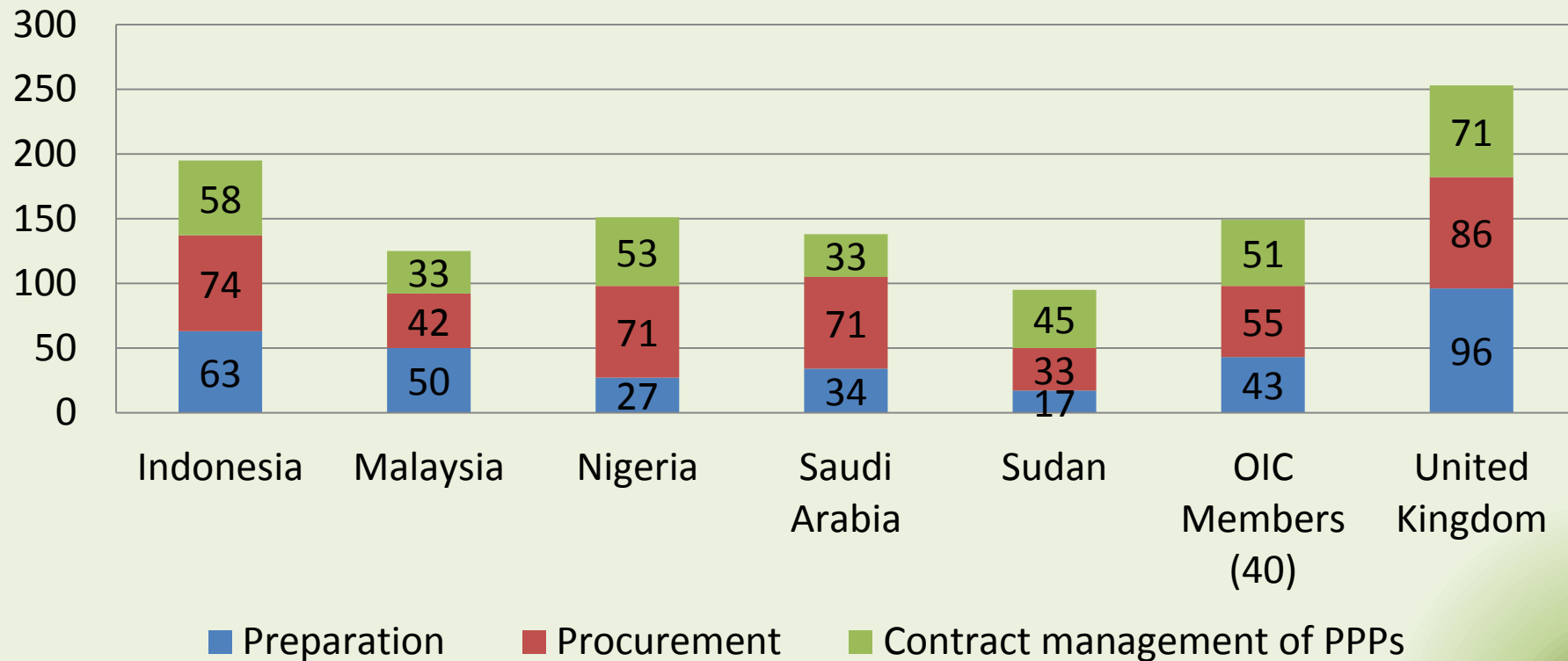


Chart 5.2

Legal Environment for Islamic Finance

- Legal and regulatory environment for Islamic finance necessary for growth and contribution to infrastructure sector
 - Indonesia: Islamic banking law 2008; Sukuk Act 2008.
 - Malaysia: Islamic Financial Act 2013; Capital Markets and Services Act 2007;
 - Nigeria: Islamic financial sectors accommodated in conventional finance laws
 - Saudi Arabia: No specific laws for Islamic finance
 - Sudan: Islamic financial laws support the industry



GLCs to Support Infrastructure Development

- Government-linked investment companies (GLICs) provide financing for infrastructure projects
 - Malaysia: Lembaga Tabung Haji own significant stakes in Axiata Group Berhad (provider of mobile telecommunications)
- GLICs raise funds for infrastructure projects
 - Malaysia: DanaInfra Nasional Berhad (wholly-owned by the Ministry of Finance) has issued sukuk for construction of infrastructure projects
 - Indonesia: PT Sarana Multi Infrastruktur (PT SMI) provides funding for infrastructure projects in the form of equity, debt and securities
- Provide Support Services
 - Indonesia: Infrastructure Guarantee Fund (IIGF) provides guarantees for fulfilment of the contractual obligations in PPP projects
 - Malaysia: Danajamin Nasional Berhad provides guarantees and insurance for bonds and sukuk to investments in infrastructure sector



Islamic Banks Assets and Financing of Infrastructure Sector

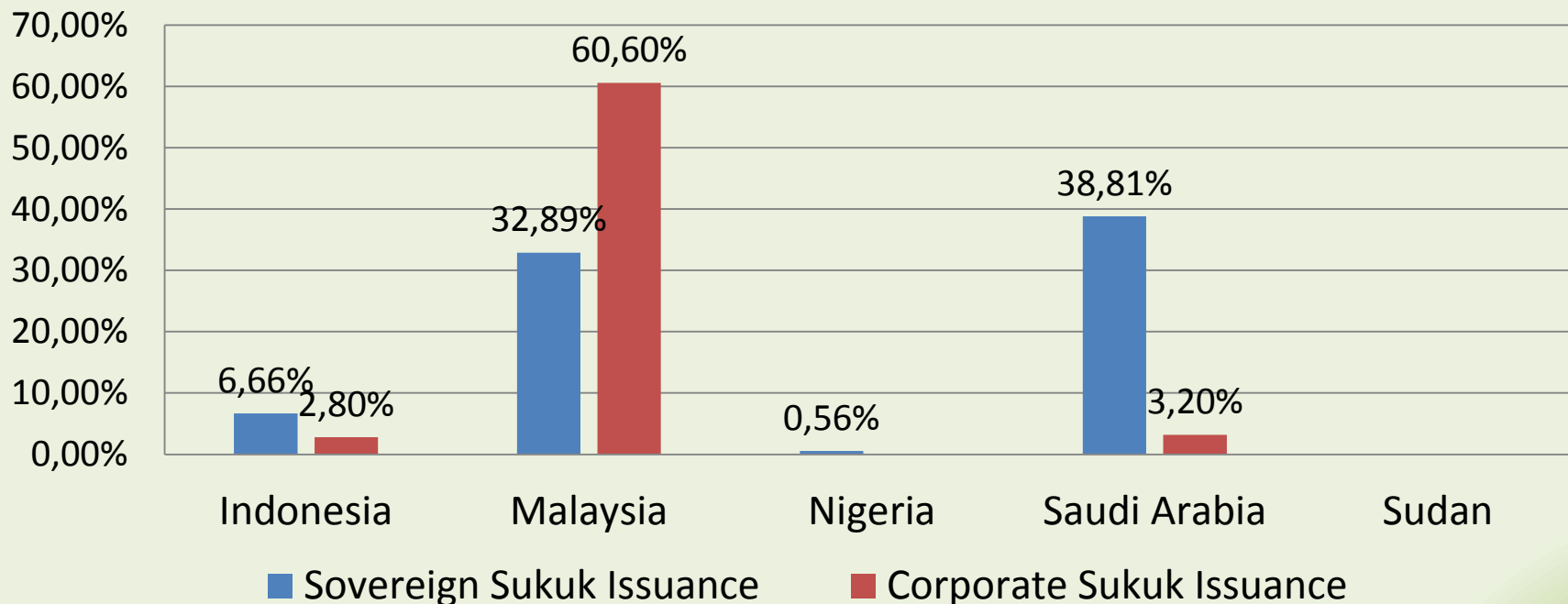
Countries	Islamic banking assets (USD Million)	Percentage of total banking assets	Percentage of investments in Sukuk	Infrastructure financing (USD Million)	Percentage of investments in Infrastructure Sectors
Indonesia	21,374.84	5.6	9.0	1,791.51	8.4
Malaysia	172,265.39	30	13.1	7,538.21	4.38
Nigeria	327.20	0.28	6.8	-	-
Saudi Arabia	159,131.82	51.1	8.6	5,955.90	3.74
Sudan	10,440.64	100	7.0	374.88	3.59

Islamic Nonbank Financial Institutions

- Insurance/takaful sectors and Shariah compliant component of pension funds and sovereign wealth funds is relatively small
- Investments in infrastructure by the sector is little
 - Sudan: Takaful sector does not have any investments in infrastructure sector
 - Malaysia: 45% of AUM (RM266.5 bn.) of largest retirement fund EPF was Shariah-compliant
 - Saudi Arabia: Sovereign wealth fund Public Investment Fund (PIF) invests in many infrastructure-related companies (power, water utility and sewerage, telecommunications and transportation sectors)



Islamic Capital Markets: Percentage of Global Sukuk Issuances



Sukuk issuance by the infrastructure sectors was 11.57% of the total

Islamic Capital Markets and Infrastructure Development

- Governments and corporates have issued sukuk to raise funds for infrastructure projects
 - Indonesia: Government and infrastructure entities issued sukuk for budgets and infrastructure projects
 - Malaysia: Extensively used sukuk for infrastructure projects
 - Nigeria: USD 289.33 million raised by issuing two sukuk by federal and state governments (for roads and education)
 - Saudi Arabia: government raised USD 19.2 billion domestically in 2017 by issuing bonds and sukuk to cover budgetary deficits
 - Sudan: Government Investment Certificates (Sarh) used to finance infrastructure projects; Sudan Financial Services Company Ltd. (SFSC) provides advisory services, designs and executes marketing policy for the issuance of sukuk

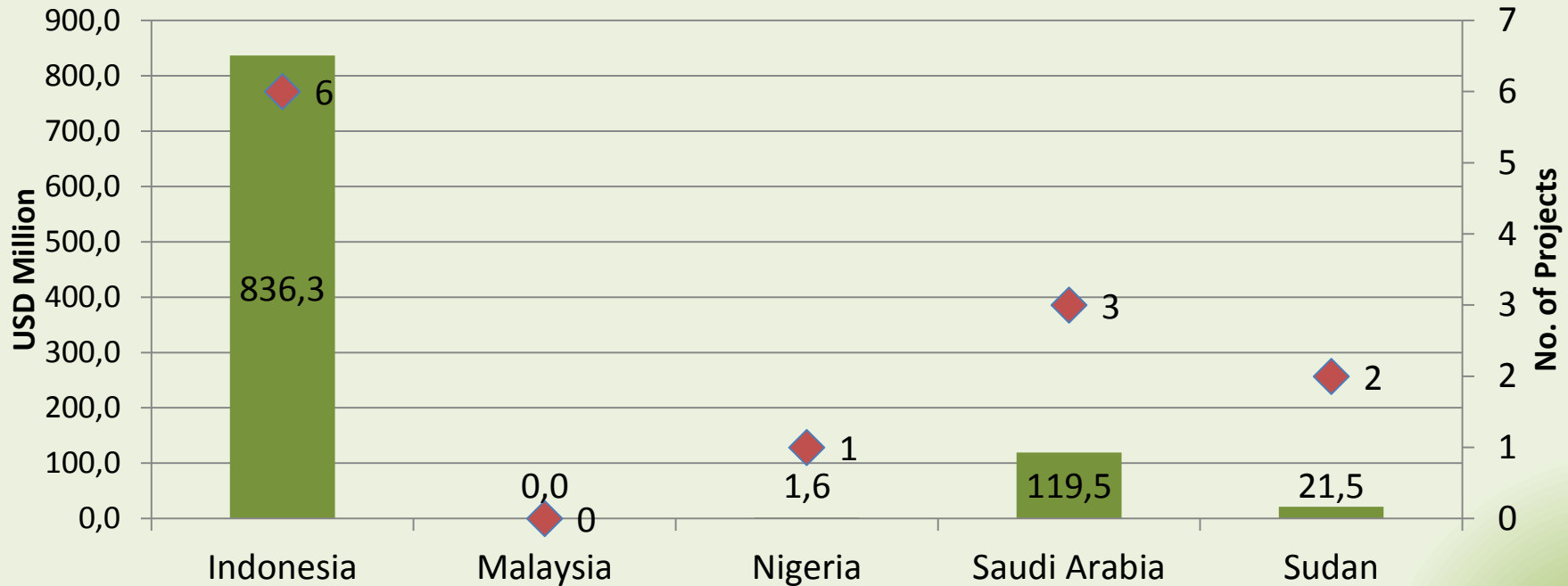


Islamic Social Sector

- Islamic social sector (*zakat* and *waqf*) can contribute to providing certain infrastructure services
- Malaysia and Saudi Arabia: *Waqf* has been used to provide medical services to the needy
- Indonesia: BAZNAS and UNDP used *zakat* funds to provide a Micro Hydro Power Plant to provide electricity to 803 households in four remote villages



Multilateral Development Institutions: Financing by IDB 2016+




Source: <https://isdbdata.github.io/monograph2017.html>



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- **Key Issues and Policy Recommendations**



Key Challenges & Issues in Infrastructure Financing facing OIC Member Countries-1

Infrastructure Related Strategy and Policies

- 1 Infrastructure needs and gaps are huge—need to identify key projects and attract alternative funding sources
- 2 Long-term investments in projects are large with long gestation periods and introduces various risks that inhibit investments (need for guarantees)

Legal and Regulatory Framework

- 3 A stable and supportive legal environment is needed to mitigate risks and attract investments
- 4 Infrastructure projects and PPP contracts are complex and new to Islamic finance—need for a sound legal/regulatory framework PPP framework
- 5 Regulatory framework for capital requirements discourages banks from investing in long-term projects



Key Challenges & Issues in Infrastructure Financing facing OIC Member Countries-2

Financial Institutions

6. Investment by Islamic banking sector in long-term infrastructure projects is small partly due to their short-term and liquid liabilities
7. Lack of underdeveloped money market instruments and markets increases liquidity risks
8. Need for a sound legal and contractual framework for Shariah compliant syndicated financing to enable financing with other Islamic banks and conventional banks
9. Islamic nonbank financial institutions are not contributing to infrastructure investments due to their small size




Key Challenges & Issues in Infrastructure Financing facing OIC Member Countries-3

Capital Markets

10. While sukuk can raise large amounts of funds from different sources, its issuance is complex and costly
11. Need to diversify sources of funds to meet the huge demand for infrastructure investments—retail sukuk can be explored

Islamic Social Sector

12. Traditional sources of Islamic social finance have huge potentials to provide social infrastructure services—in most countries these are not utilized




Key Challenges & Issues in Infrastructure Financing facing OIC Member Countries-4

International Sources

13. Shariah compliant funds from international sources for infrastructure sector is limited—IDB providing Shariah compliant project financing, but has other mandates

Reduce Knowledge Gap and Capacity Building

14. Since Islamic infrastructure investments are new and complex, stakeholders lack the knowledge and expertise on Islamic infrastructure contractual arrangements



Policy Recommendations According to Themes

No.	Themes	No. of Recommendations
1	Infrastructure Related Strategy and Policies	3
2	Legal and Regulatory framework	4
3	Government and Government Linked Companies	3
4	Islamic Banks	2
5	Islamic Nonbank financial institutions	2
6	Islamic Capital Markets	3
7	Islamic Social Sector	2
8	Multilateral Development Institutions	4
	Total	23



Key Recommendations, Responsible Stakeholders & Rationale: Public Sector

No.	Recommendations	Responsible Stakeholders	Rationale
1.	Identify a pipeline of innovative sustainable projects that are essential for long-term economic growth	Relevant government ministries or a specialized public body	Infrastructure investments are large and long-term and require appropriate forward looking planning, policies and implementation frameworks
2.	Develop standardized Shariah compliant contract templates for infrastructure projects	Government agencies and regulators in collaboration with the Islamic Development Bank	Shariah compliant contracts are complex and new to most stakeholders which inhibit financing
3.	Establish a National Islamic Infrastructure Bank (NIIB)	Government establishes and provides the initial equity and then raises funds from market and other stakeholders	Large investments needed for infrastructure projects and relative newness and smaller size of the Islamic financial sector



Key Recommendations, Responsible Stakeholders & Rationale: Private Sector

No.	Recommendations	Responsible Stakeholders	Rationale
4.	Adapt Islamic banking law to establish restricted investment accounts for use in longer-term investments	Relevant government ministry and bank regulators	Liabilities of banks are short-term and liquid and infrastructure projects are long-term and illiquid Capital adequacy requirements impose higher capital charges on long-term unsecured investments
5.	Establishment of a Shariah compliant infrastructure fund	Government can form a GLC or NIIB will drive the establishment and operations of the fund	Most Islamic banks and nonbank financial institutions are small. A specialized fund can raise resources for infrastructure investments from different stakeholders
6.	Establish a GLC that can advise on the structuring and issuance of sukuk	Government can form a GLC that will provide such services	Sukuk structures are complex and new to most stakeholders which increases costs and discourage their use



Key Recommendations, Responsible Stakeholders & Rationale: Islamic Social Sector

No.	Recommendations	Responsible Stakeholders	Rationale
7.	Develop innovative models of using zakat and waqf for providing social infrastructure services	Zakat institutions, waqf institutions, government bodies and international organizations	Islamic social finance has huge potentials, yet is untapped. Given the large investment needs to achieve the SDGs, these sources can be tapped in to provide social infrastructure services



Key Recommendations, Responsible Stakeholders & Rationale: International Stakeholders

No.	Recommendations	Responsible Stakeholders	Rationale
8.	Establish an International Islamic Infrastructure Bank (IIIB)	Multilateral organizations and/or large private sector organizations can take the lead OIC member countries can provide the initial capital for establishing the IIIB.	IDB is the only Islamic MLB with mandates beyond project financing Since Investment needs for infrastructure sector of member countries is large, IIIB can mobilize funds from different international sources
9.	Build capacity and human capital for implementing Islamic infrastructure financing	Multilateral development organizations such as IDB, COMCEC or the proposed IIIB can provide the technical assistance for training professionals of Islamic financial sector	PPP projects are multifaceted and new for many Islamic financial institutions Knowledge gap exists on how Islamic finance can be used for PPP projects



QUESTIONS??