WORLD BANK GROUP
Finance & Markets
Global Islamic Finance Development Center

Recent Developments in Global Financial Architecture and Implications for Islamic Finance

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Road Map

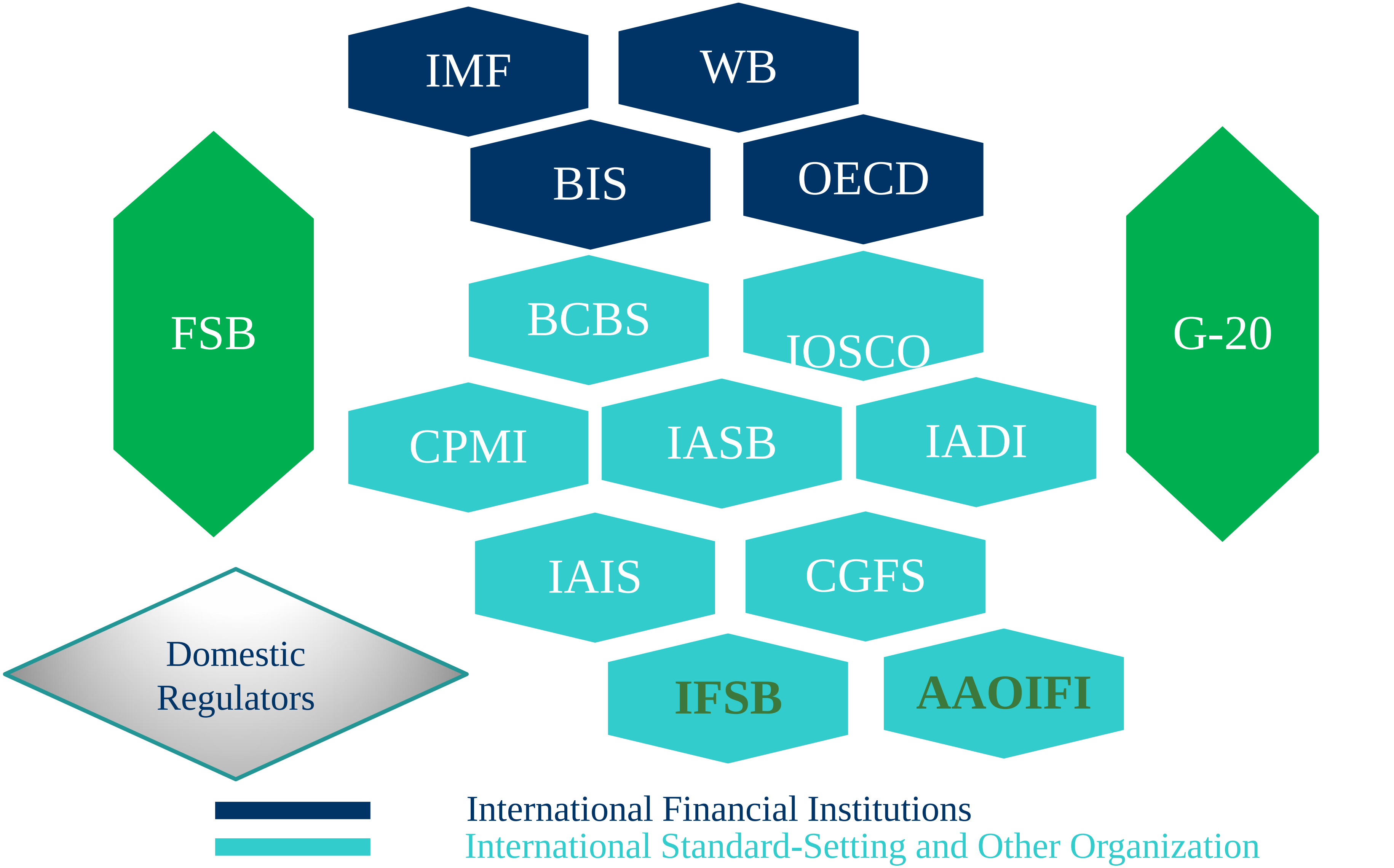
I. Global Financial Architecture

II. Recent Developments in Global Financial Architecture

III. Implications for Islamic Finance

I. Global Financial Architecture

Players of Global Financial Architecture



Role of World Bank in Global Financial Architecture

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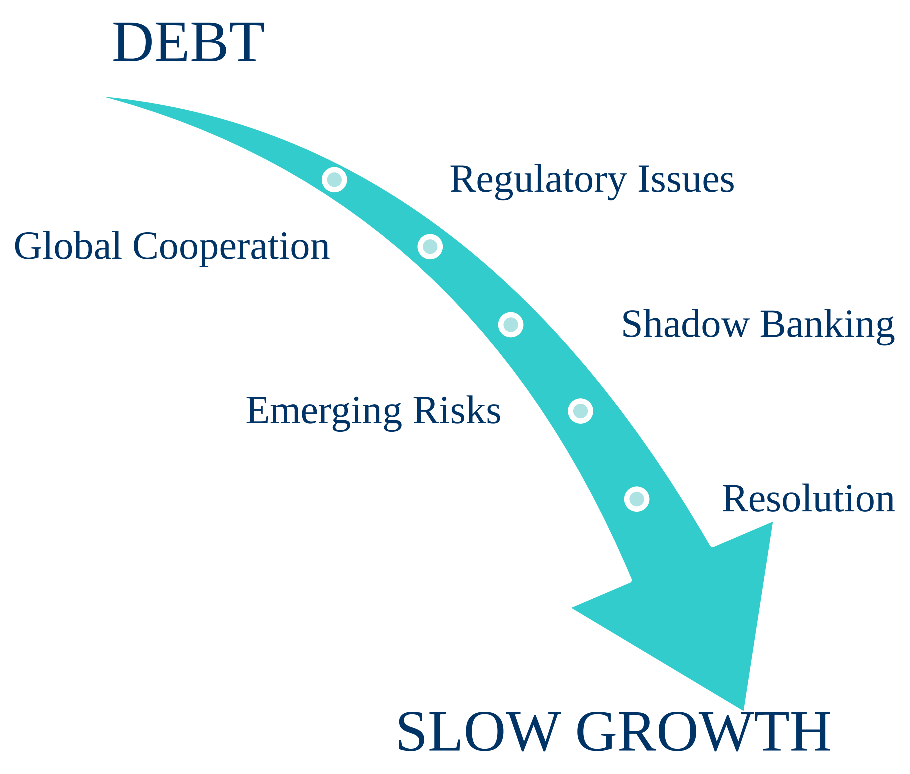
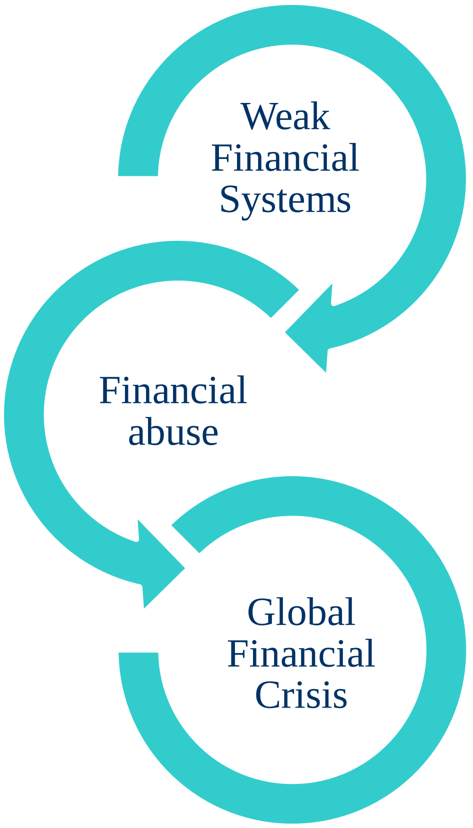
- **Ending extreme poverty**

- **Boosting shared prosperity**

I. Recent Developments in Global Financial Architecture

Global Financial Architecture – Current Issues





Macro-Prudential Regulation

- **Macro-Prudential Framework**
  - Deals with systemic risk "the risk of widespread disruptions to the provision of financial services"
  - Time dimension (pro-cyclicality) and cross-sectional dimension (concentration and interconnectedness)
  - Basel III

  - **Main challenges**

    - Institutional and governance arrangements: need for clearly defined mandate, powers and accountability. Two trends:
      - Integrated regulatory framework (macro and micro under central bank)
      - Inter-agency financial stability committee (e.g., ESRB, FSOC)
    - Designation and calibration of instruments (policy toolkit): many instruments already exist but re-oriented
    - Shadow banking risks
    - Potential cross-border effects

Micro-prudential Regulation (Basel III)

- **Strengthened global capital framework**
  - Definition of capital
    - Redefined criteria for inclusion in regulatory capital; phase out of innovative hybrid instruments; capital deductions strengthened; all capital instruments absorb losses
  - New capital requirements
    - Common equity tier 1 of 4.5% of RWA (from 2%) and minimum Tier 1 of 6% of RWA (from 4%)
    - Improved counterparty credit exposures on derivatives, repo and securities activities (beyond Basel II.5) and review of trading book to improve market risk exposure (reduce arbitrage, VAR/tail risk, etc.)
    - Capital conservation buffer from 0.625% up to 2.5% in 2019
    - Leverage ratio (initially set at 3%) and countercyclical capital buffer

- **New global liquidity framework**
  - Liquidity coverage ratio (LCR)
  - Net Stable Funding Ratio (NSFR)

- **New studies: Simple and comparable models (IRB)**

Innovative Financial Inclusion

- G20 Initiative and WB Goal
- Fintech
- De-risking
  - Risk of De-risking
  - WB studies
- Financial Literacy&Consumer Protection

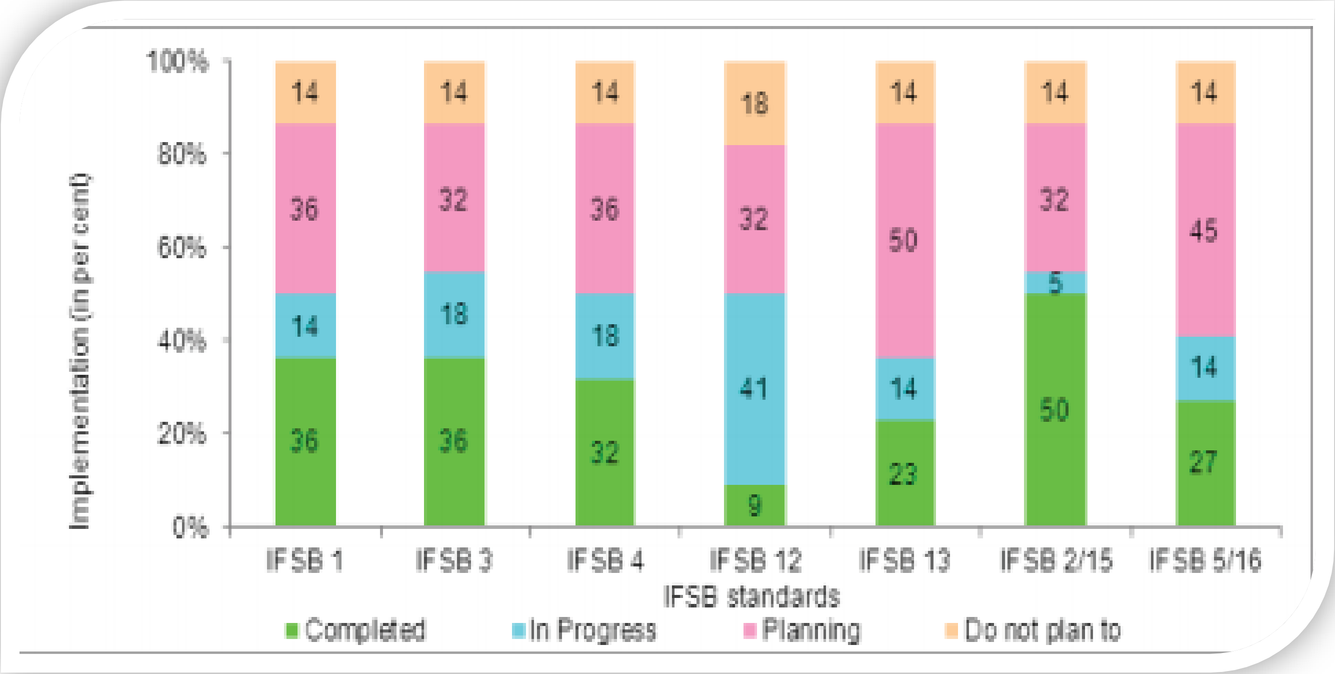
III. Implications for Islamic Finance

Implications for Islamic Finance

- Adoption and Implementation of the Standards
- Supervisory governance and reforms
- Shadow Banking
- Basel III Implications
- Collaboration
- Inclusion

Adoption of IFSB Standards

- Number of Countries which adopted IFSB Standards



Source: Comparative Study on the Implementation of Selected IFSB Standards, IFSB Working Paper Series, WP-04/10/2015, October 2015

Adoption of AAOIFI Standards

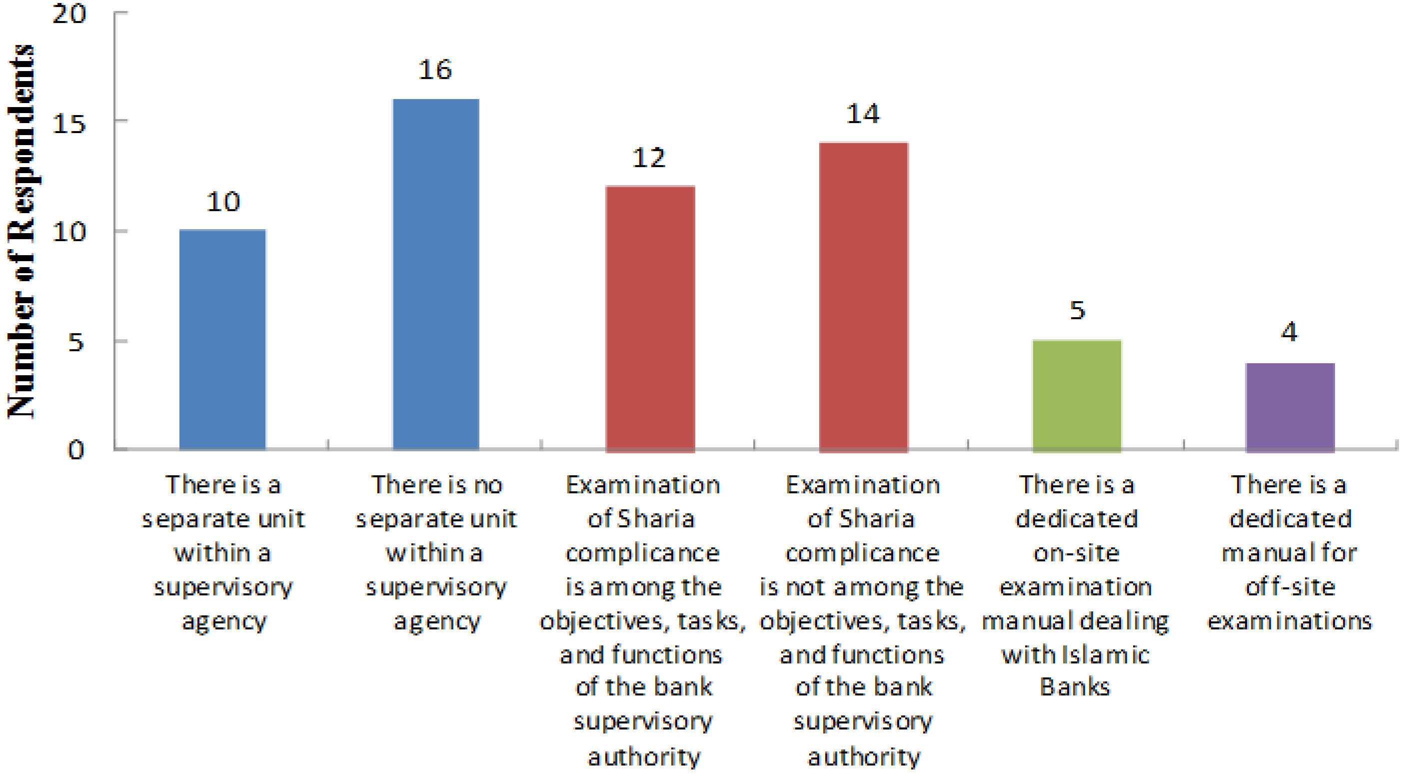
Mandatory regulatory requirement in jurisdictions		As basis of of national accounting standards in jurisdictions	
Shari'ah Standards	***Accounting Standards***	***Shari'ah Standards***	***Accounting Standards***
Bahrain	Bahrain	Indonesia	Indonesia
Oman	Jordan	Malaysia	Pakistan
Pakistan	Oman		
Sudan	Qatar		
Syria	Qatar Financial Centre		
Islamic Development Bank	Sudan		
	Syria		
	Islamic Development Bank		

In other jurisdictions including Brunei, Dubai International Financial Centre, France, Egypt, Jordan, Kuwait, Lebanon, Saudi Arabia, Qatar, Qatar Financial Centre, South Africa, United Arab Emirates and United Kingdom as well as in Africa, Central Asia and North America, AAOIFI Shari'ah standards and/or AAOIFI accounting standards have been used voluntarily as basis of internal guidelines by leading Islamic financial institutions.

AAOIFI auditing, governance and ethics standards are not part of mandatory regulatory requirement for Islamic finance. Instead, these standards are used voluntarily by leading Islamic financial institutions across all major Islamic finance jurisdictions.

Source: AAOIFI website

Islamic Banking Regulation and Supervision

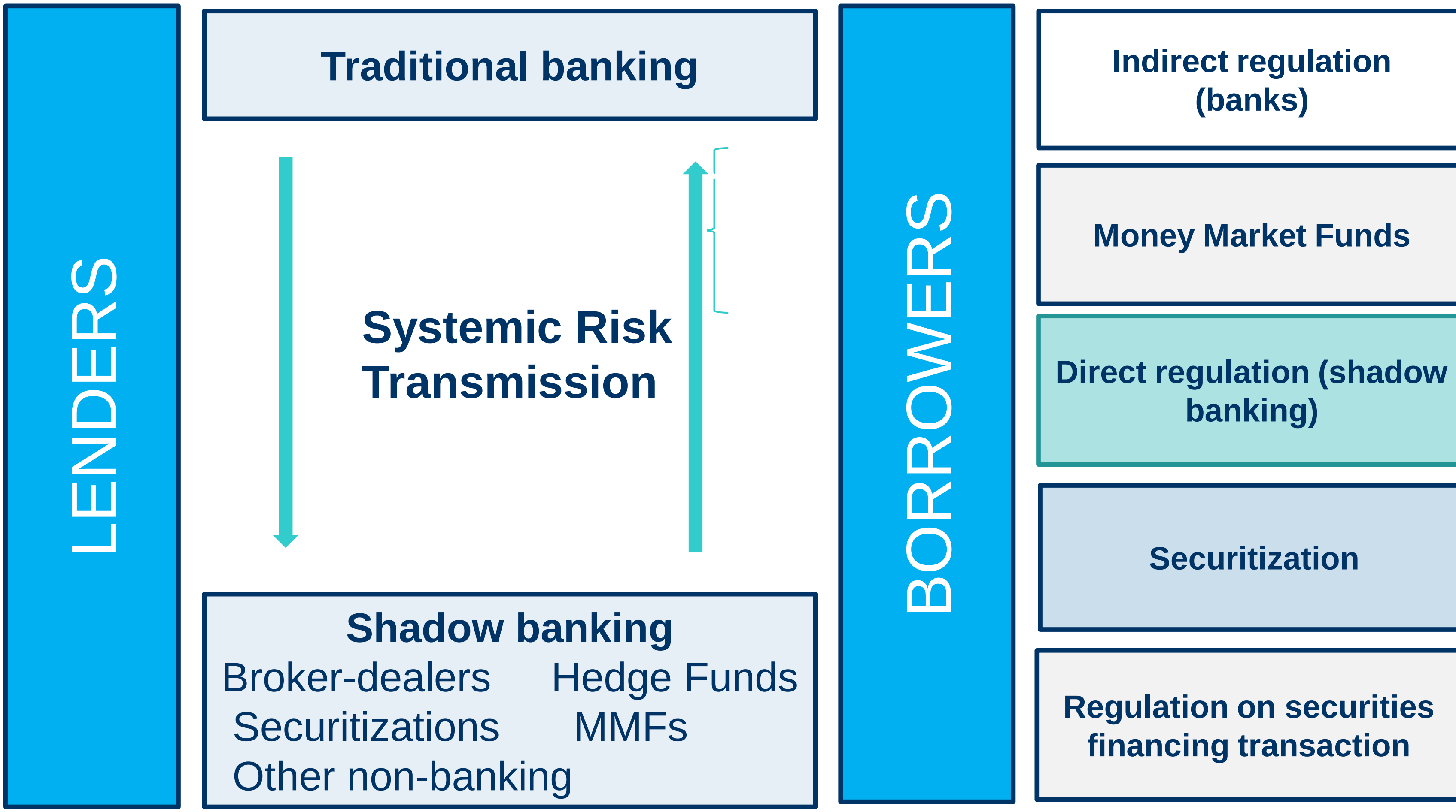


Source: Song, Inwon and Carel Oosthuizen 2014, "Islamic Banking Regulation and Supervision – Survey Results and Challenges," IMF Working Paper No. 14/220 (Washington: International Monetary Fund).

Basel III implications on IFIs

- The supervisory authorities` discretionary role
- Capital
- Liquidity
- Leverage
- Risk and Cost
  - Increased exposure to operational risks
  - Increased operational cost for monitoring and reporting
  - New approach to the risk management and internal control
- Growth

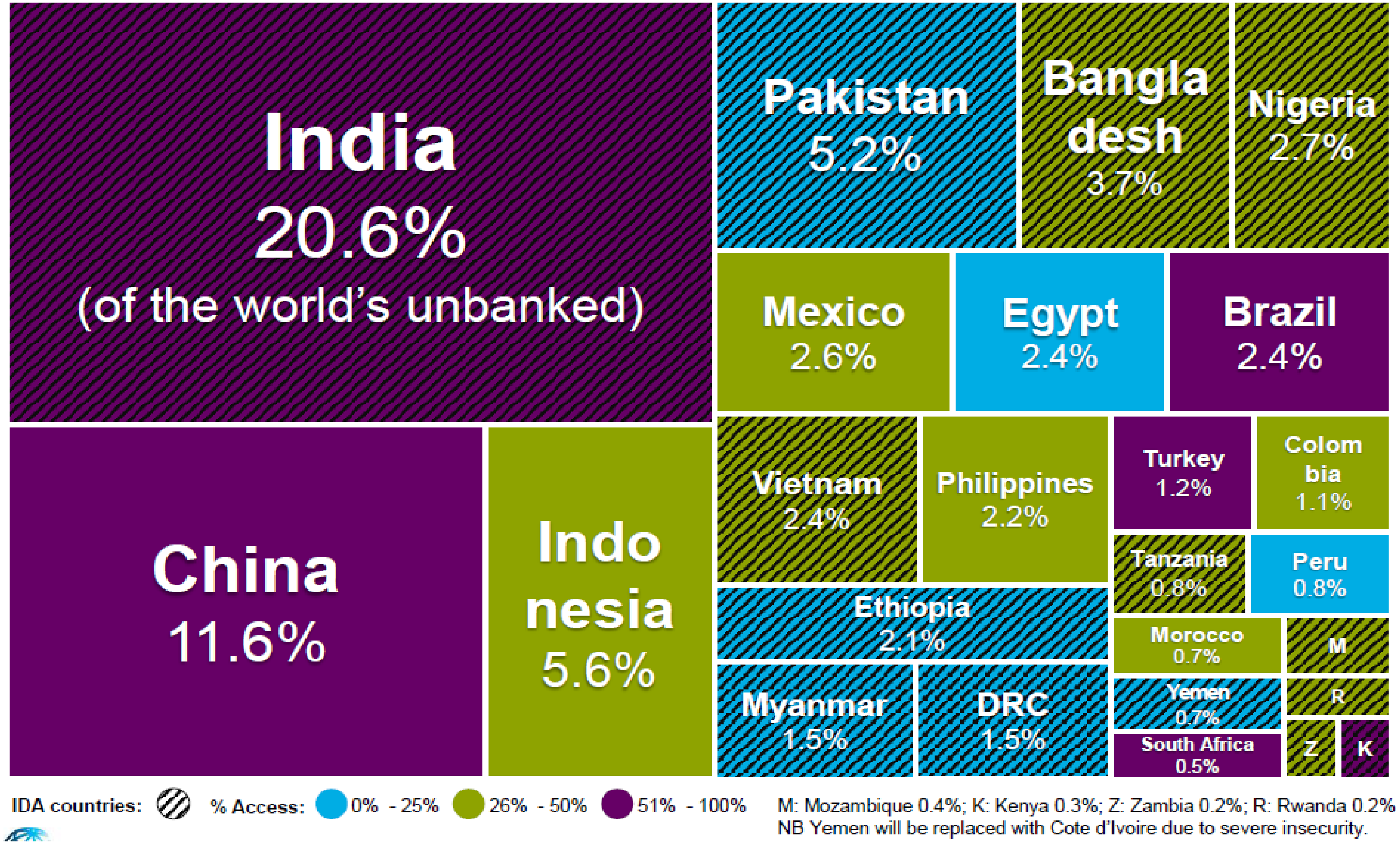
Shadow Banking: Islamic Finance



Financial Inclusion

Out of 73% of the world's unbanked, 22.2% are Muslim countries.

Countries prioritized based on share of unbanked, IDA, and FCS: 2014 FINDEX



Sources: Global Findex 2014

Financial Inclusion - Fintech

- New Business model, new emerging risks
- Regulatory arbitrage
- Consumer protection

Need for close collaboration...

- Islamic Finance on G-20 agenda provides both opportunities and challenges.

- Close collaboration of IFSB and AAOIFI with international and multilateral institutions

- Increased activities in capital markets with cross-border investors and borrowers call for coordinated efforts by capital markets regulators.

- Establishment of World Islamic Infrastructure Bank (Mega Bank)

Thank You

For your further questions please contact:
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