



# Impact of the Global Financial Crisis on the Islamic Banking Industry

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Corporate Finance ▪ Capital Markets ▪ Private Equity ▪ Asset Management ▪ Strategic M&A ▪ Treasury

## Impact of the market crisis on financial institutions globally

- No bank is completely immune
- Direct exposure:
  - Toxic assets, mortgage securities, CDO's, SIV's
  - Counterparty exposure to distressed financial institutions
  - Fair value losses on investment securities & financial instruments
- Indirect exposure:
  - Increased cost of funding and/or lack of funding
  - Tightening liquidity
  - Credit crunch
  - Global recession



## Regional impact

- GCC equity markets have fallen dramatically in 2008
  - 49.4% drop in MSCI Gulf Countries Index (ytd, 21/11/08)
  - 59.9% drop in Saudi Tadawul All Share Index (ytd, 22/11/08)
  - 66.1% drop in DFM Index (ytd, 20/11/08)
  
- Direct subprime exposure of GCC banks still not clear; approx. US\$2.6 billion has been announced so far, but actual figure likely to be significantly higher
  - Direct exposure of US and European banks is over US\$500 billion
  - Exposure of GCC sovereign wealth funds likely to be higher than that of banking sector
  
- Region is beginning to see effects of increased funding costs and tighter liquidity; project finance and real estate industry will be particularly affected



# Impact on Islamic banks

- Impact on Islamic banks has been limited so far because of lack of direct exposure to the subprime crisis & underlying risky instruments
  - Renewed global focus on Islamic Finance industry & inherent advantages of asset-backed banking
  
- However, Islamic banks **ARE** affected
  - Slowdown in funding (equity and/or leverage) to support business growth
  - Asset depreciation (particularly real estate)
  - Limited debt financing to support PE deals
  - Slowdown in Sukuk & syndicated facilities (largely dependent on participation of international banks)



# How can Islamic banks protect themselves?

- Comprehensive due diligence on potential deals
- Effective risk management
- Product diversification
- Geographic expansion
- Strong liquidity management
- Expand & diversify funding sources: equity, short-term bank lines, medium and long-term debt, deposits (on and off-balance-sheet)
- Strong capital base



**CONSOLIDATION WITHIN THE INDUSTRY IS ESSENTIAL**

# Opportunities

- Crisis has created buying opportunities
- Climate particularly conducive to private equity transactions
  - Emphasis on smaller deals that are not overly dependent on leverage & debt financing
  - Valuations have fallen while sellers have become more realistic about what they expect from a PE partner
- Renewed focus on inherent advantages of Islamic banking provides opportunity to demonstrate how far the industry has come & to pitch Islamic finance as viable complement & alternative to conventional banking
- The current circumstances provide an unprecedented opportunity for the industry to move to the next level



**ISLAMIC BANKING IS NOT THE SOLUTION TO THE GLOBAL FINANCIAL CRISIS, BUT IT OFFERS AN IMPORTANT & GROWING ALTERNATIVE WAY OF PROVIDING FINANCIAL SERVICES**

Thank you



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