

THE INTERNATIONAL



ISLAMIC FINANCE FORUM

Dubai

13 - 17 April 2008 • Jumeirah Beach Hotel, Dubai, UAE

**Innovation in Islamic Retail Products
- A Comparative Update Between
Malaysia and GCC**

Ruslena Ramli

www.iiff.com



Innovation in Islamic Retail Products

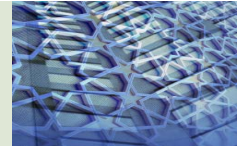
- A Comparative Update Between Malaysia and GCC

Presented to The International Islamic Finance Forum 2008

Presented By Ruslena Ramli

April 14, 2008

Presentation Outline



The Malaysian Banking Scene

3 - 6

What is Islamic Retail Banking?

7 - 9

Types of Islamic Contracts Applied in Retail Products

10 - 33

Challenges and Sustainability

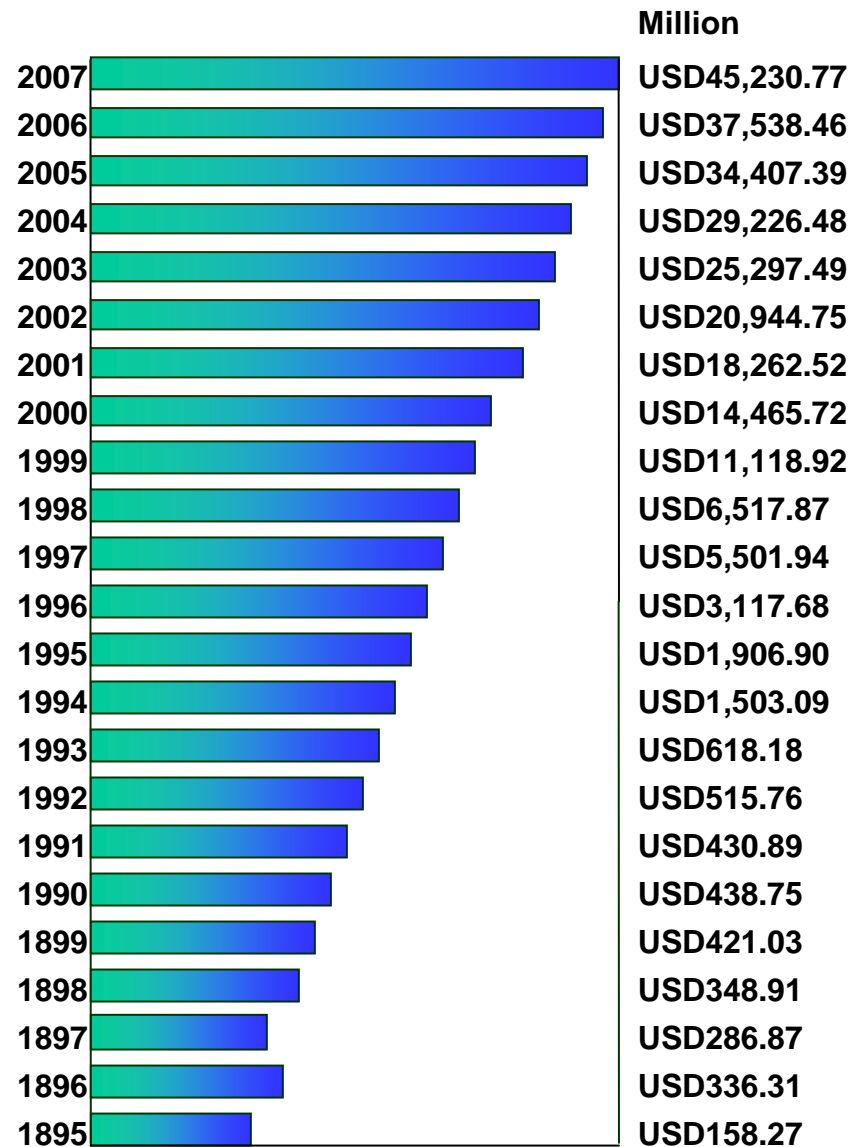
34 - 35



The Malaysian Retail Banking Scene

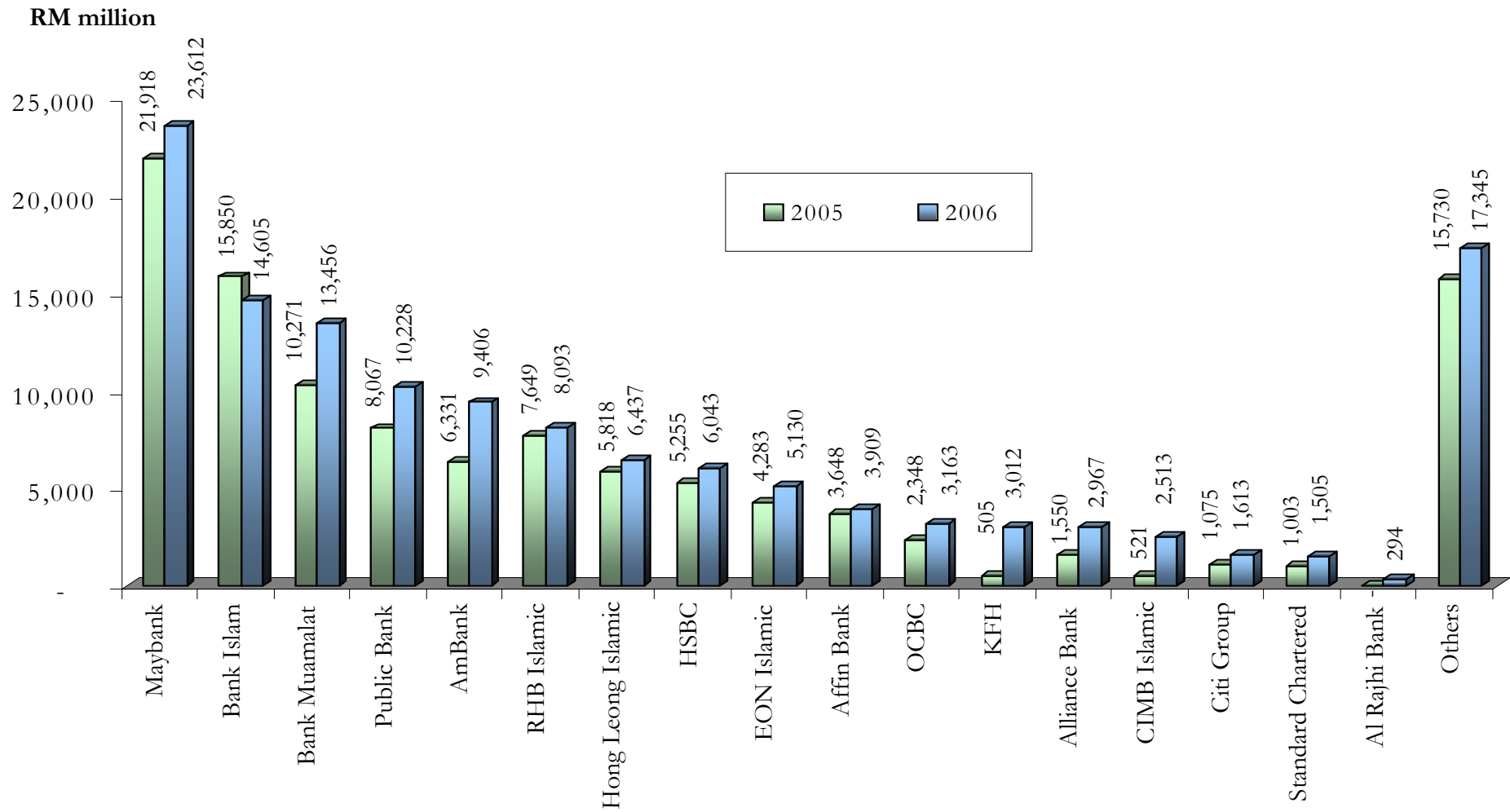
1

Overview of Growth in Islamic Banking Assets



“From a modest start of USD158.27 million in 1895, Islamic banking assets in Malaysia is increasing at an average rate of 33% to USD45.23 billion by 2007”

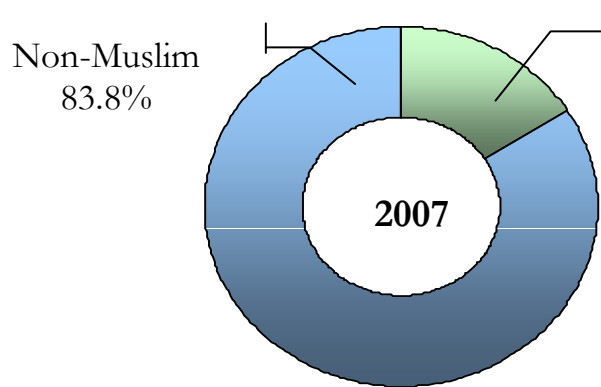
Growth of Islamic Assets by Malaysian Banks



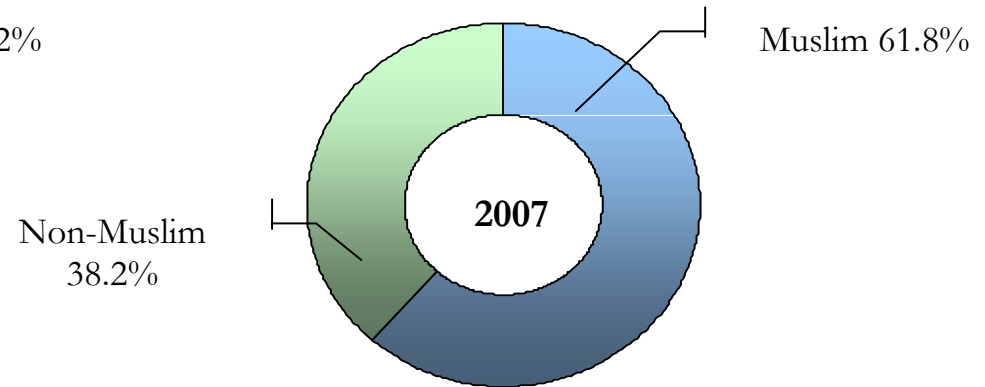
Source: BNM, Annual Reports

Profile of EONCAP Islamic's Banking Assets

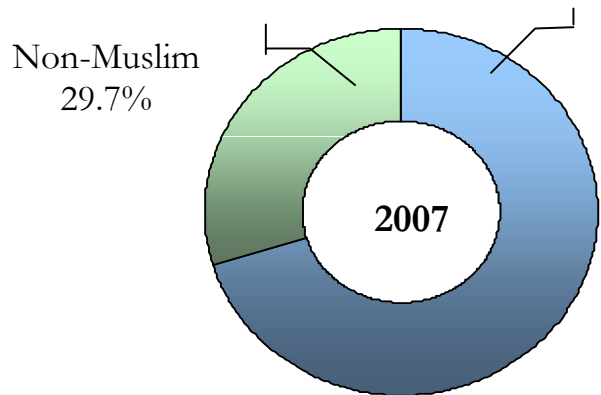
“Islamic banking today is no longer restricted to race or religion”



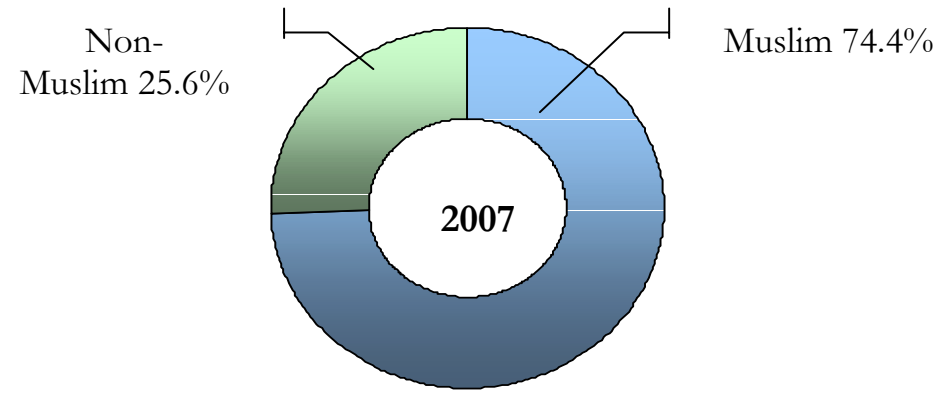
Current Deposits



Saving Deposits



Home Financing



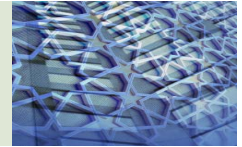
Motor Vehicle Financing

A decorative banner with a dark green background on the left and a blue geometric pattern on the right. The text is white and centered.

2

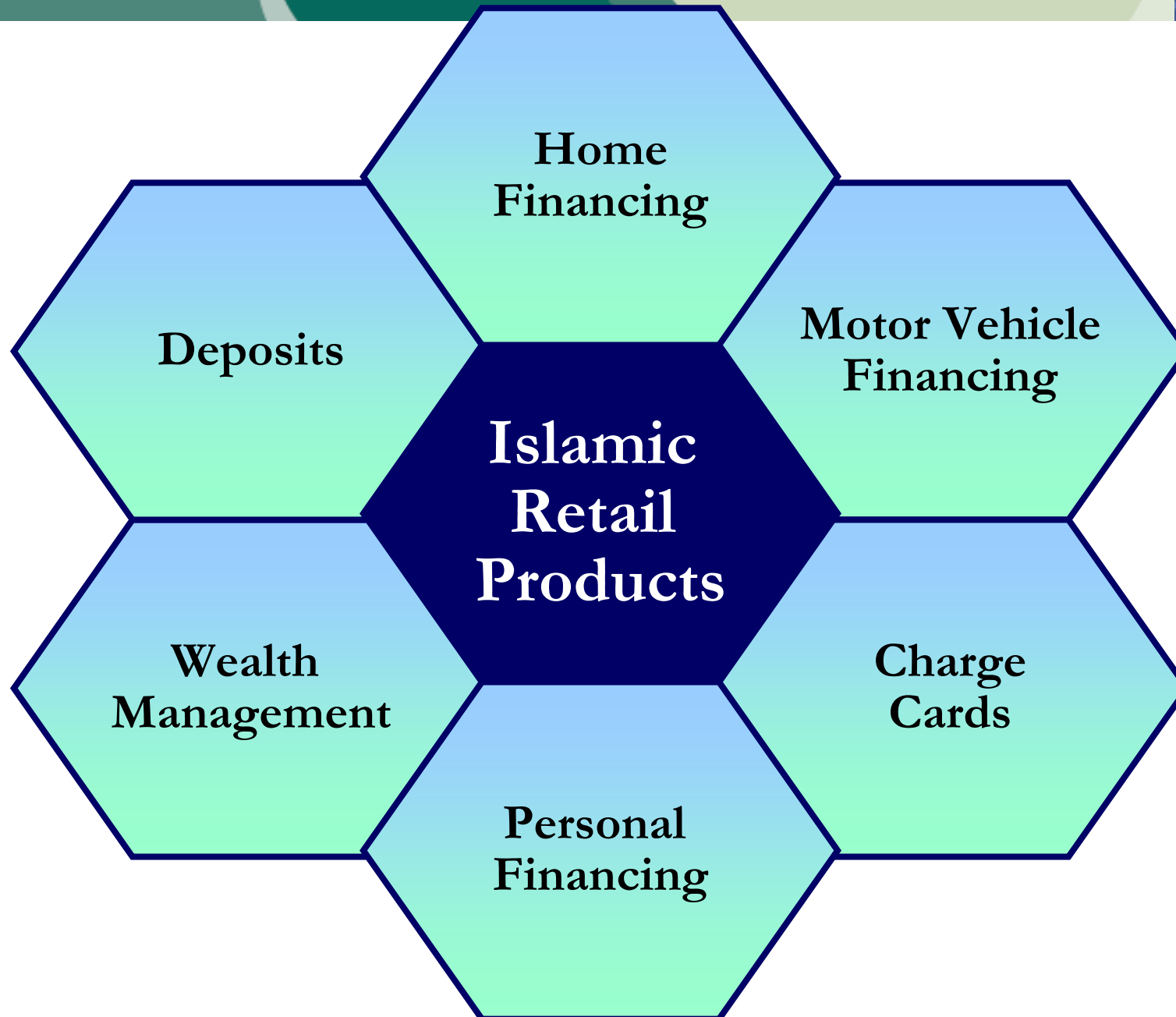
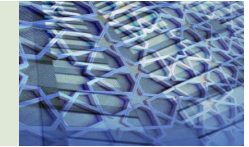
What is Islamic Retail Banking?

Brief Summary



- **Mass-market banking** where products cater to individual needs of customers and is typically performed in local branches of larger commercial banks.
- **Common products** include deposit accounts, home financing, car financing, personal financing, charge cards, etc.
- **Scope of services** have evolved to address the entire financial solution of a customer, from growing and protecting customer's assets to planning retirement and passing wealth on to future generation.

Types of Islamic Retail Products



3

Types of Islamic Contracts Applied in Retail Products



3a

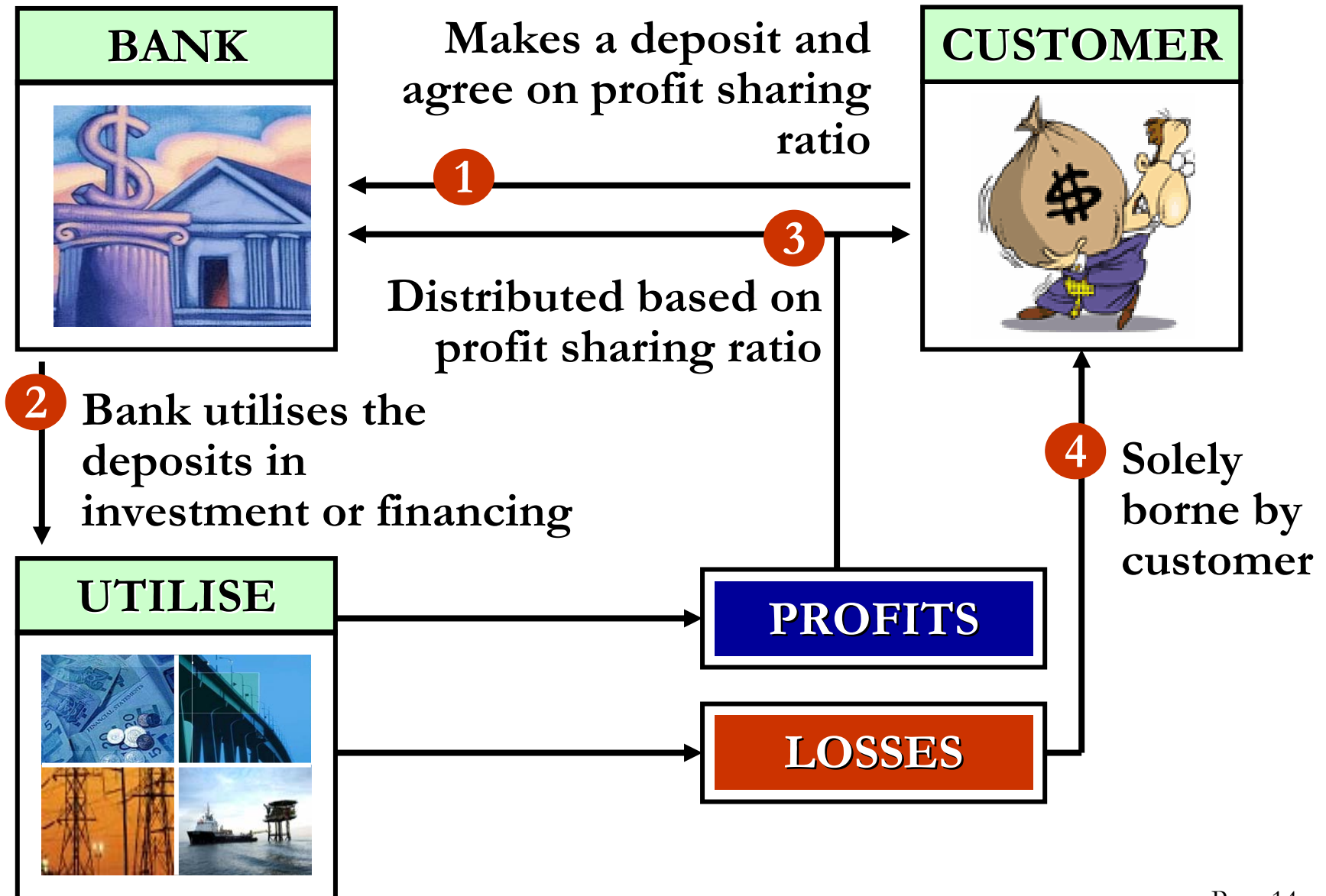
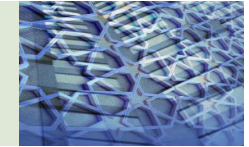
Islamic Deposits

Application of Islamic Contracts - Comparison

Products	Shariah Principles (Malaysia)	Shariah Principles (International)
Saving/Current	Wadiah Yad Dhamanah/ Mudharabah	Wadiah/Qard Hasan/ Mudharabah
GIA/SIA	Mudharabah	Mudharabah
Deposit		Tawarruq/Wakalah

- In Saving Accounts, most Banks adopt the principle of Wadiah (guaranteed safe custody) and Mudharabah (joint venture) for Current Accounts.
- Other Islamic banks use the contract of Qard Hasan especially in Iran.
- Alternative principles are Tawarruq and Wakalah.

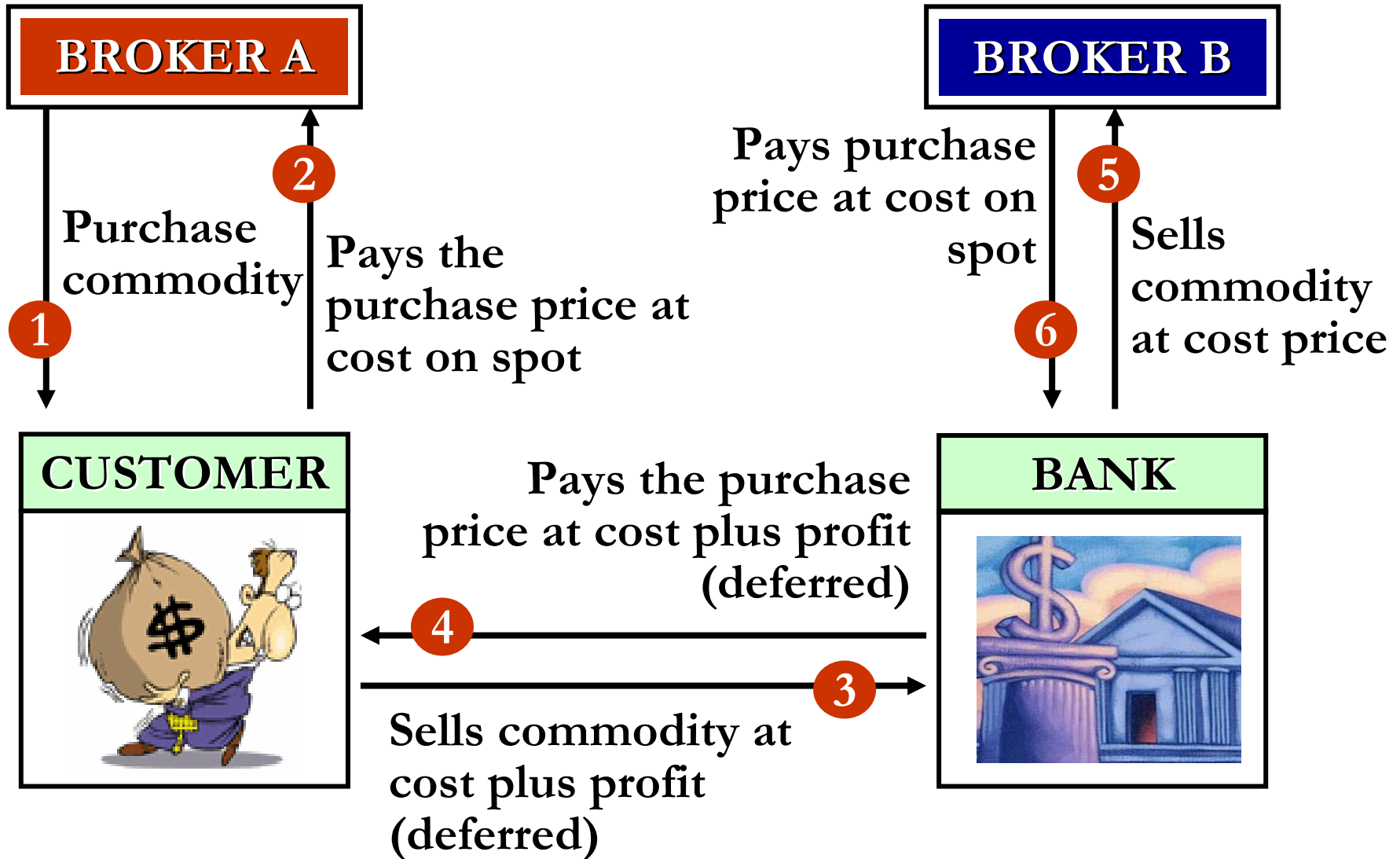
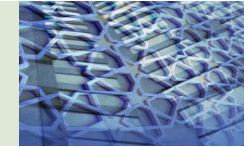
Mudharabah Based Deposits



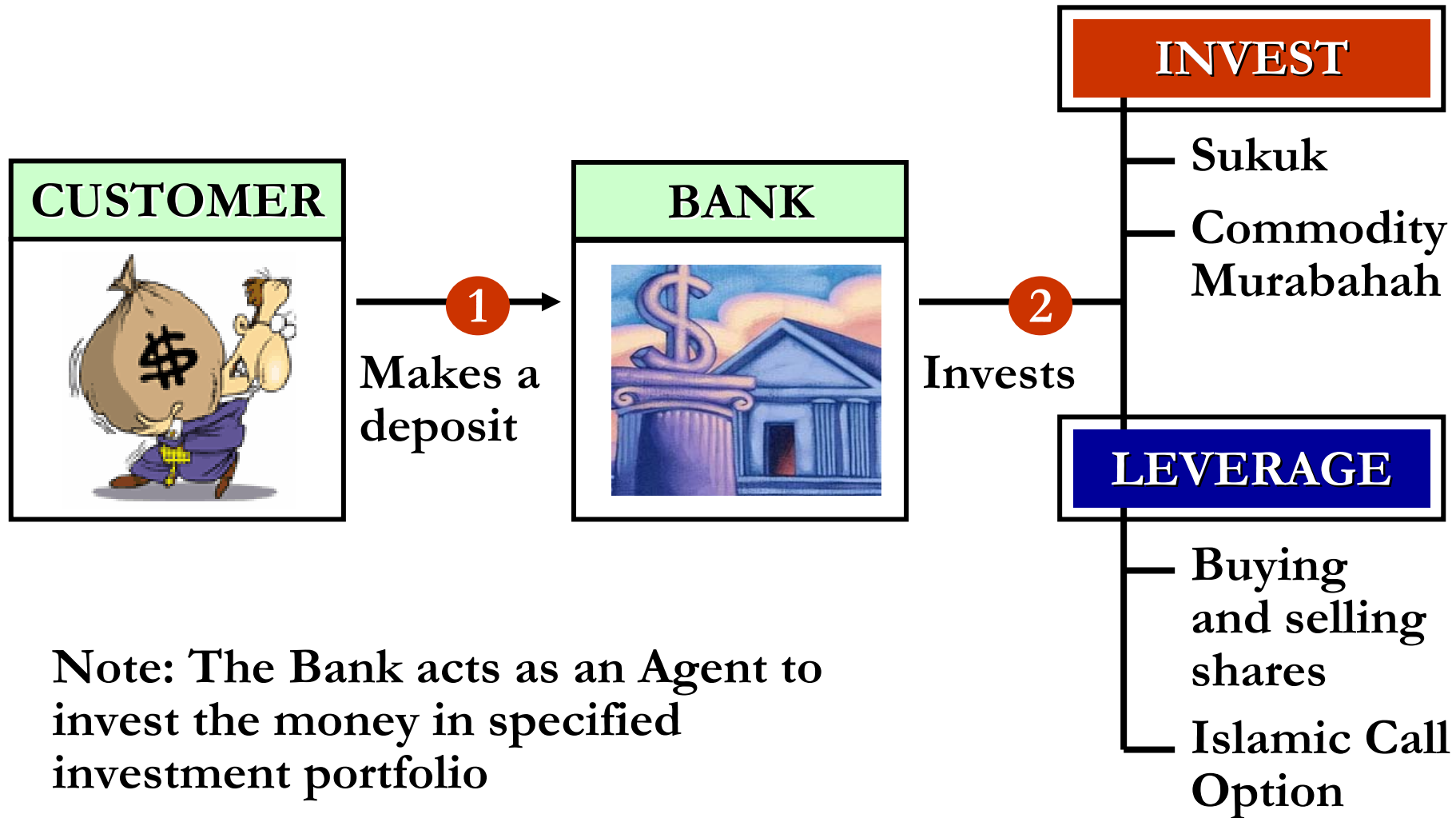
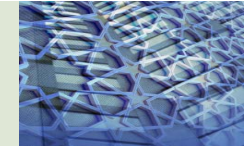
Innovation and Issues in Product Development

- Establishment of an effective rate of return framework, which provides a standard methodology for deriving the rate of return on deposits – “Profit Equilisation Reserve”.
- In a dual banking system, level of competitiveness is important in retaining customer and deposits.

Alternative : Tawarruq Based Deposits



Alternative : Wakalah Based Deposits





3b

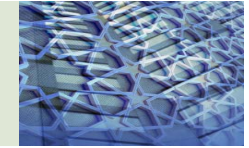
Home Financing

Application of Islamic Contracts - Comparison

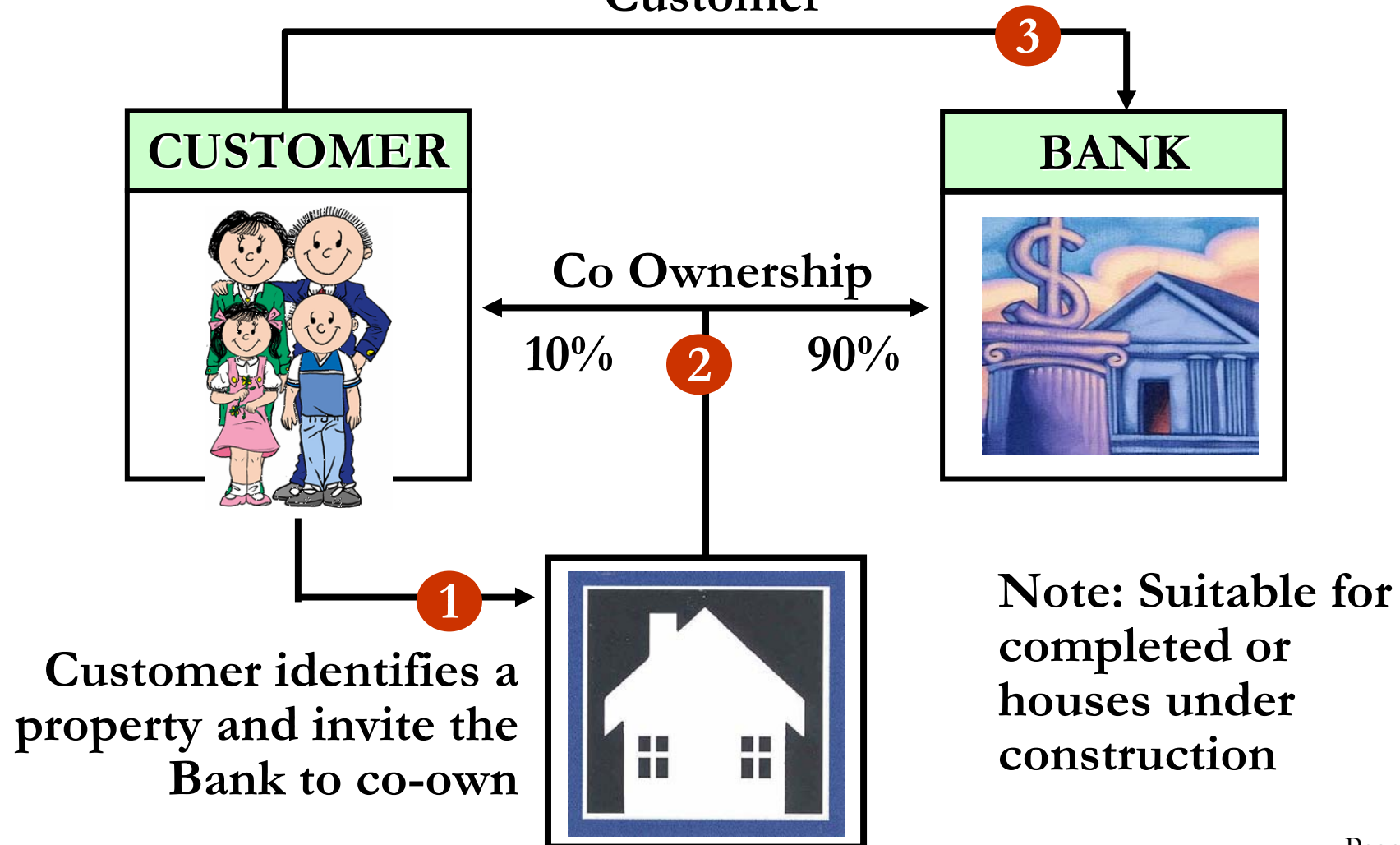
Products	Shariah Principles (Malaysia)	Shariah Principles (International)
Home Financing /Refinancing	Bai Bithaman Ajil (Bai Inah)/ Musyarakah Mutanaqisah/Istisna	Musyarakah Mutanaqisah/ Murabahah/Ijarah Muntahiyah Al Tamluk/Istisna

- Almost all Malaysian Islamic Banks adopt the principles of Bai Bithaman Ajil (sale and purchase).
- Initiatives are underway to promote utilisation of Musyarakah Mutanaqisah (diminishing ownership).

Musyarakah Mutanaqisah Home Financing



Over time the Customer purchases the Bank's stake in the property until all ownership remain with the Customer

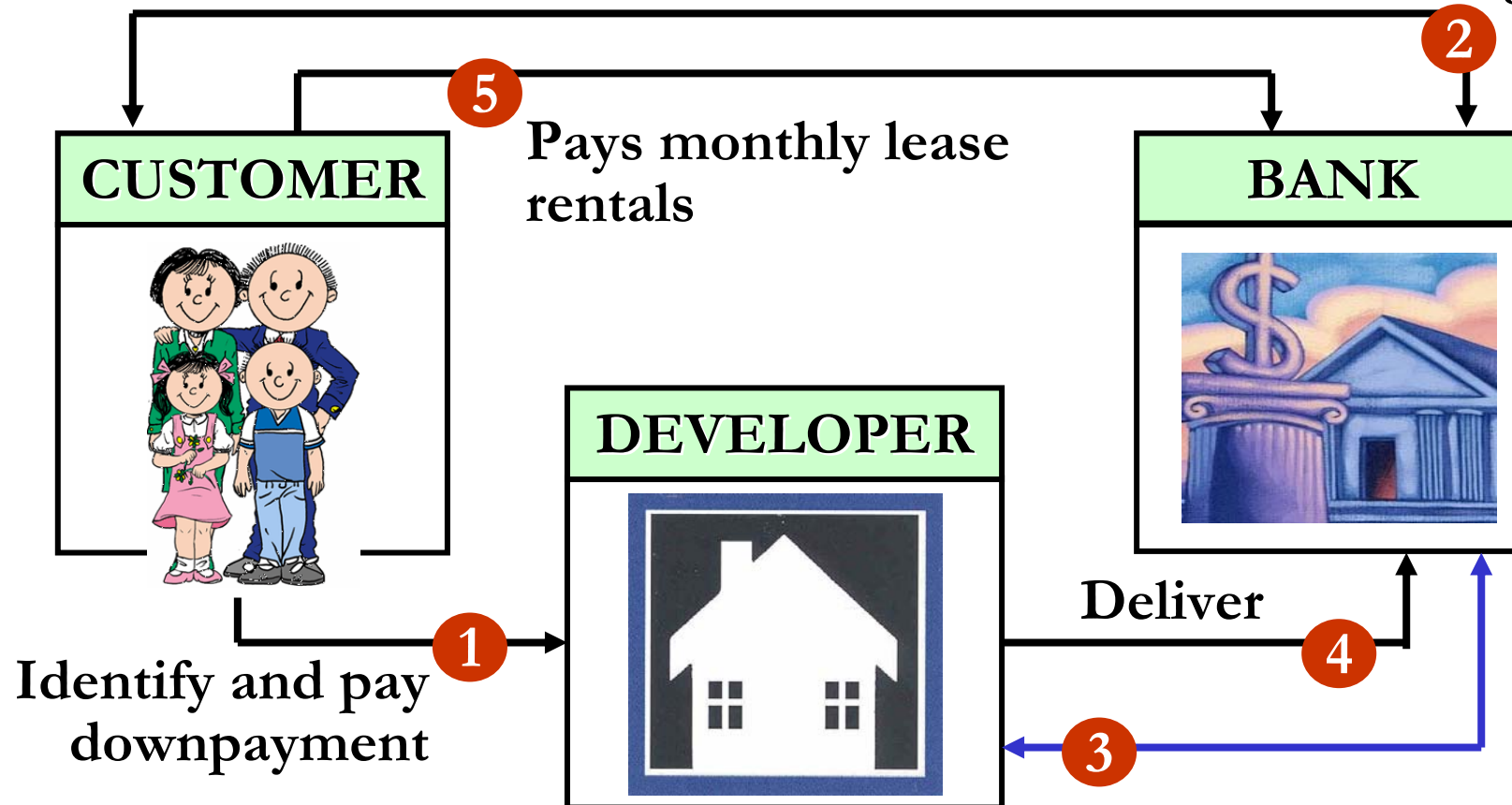


Innovation and Issues in Product Development

- **Waiver on double stamp duty for the transfer of Asset from the Bank to the Customer.**
- **Enhancing IT System and reducing legal documentation for Customer.**
- **Benchmark of sale price at the end of the Musyarakah Mutanaqisah period. Market value or a price that is agreed upfront? In Malaysia, the price is agreed upfront.**
- **How to recognise Musyarakah Mutanaqisah in the Bank's books?**
 - **The Bank as owner of the Asset; or**
 - **The Customer (legal possession) as owner of the Asset but the Bank has charge over the Asset (actual possession)**

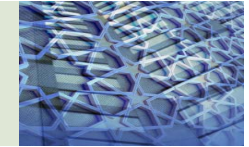
Ijarah Home Financing

Customer enters into a Lease Agreement (or Forward Lease Agreement) to lease the house for an agreed lease rental with a transfer of the asset to the Customer at the end of financing

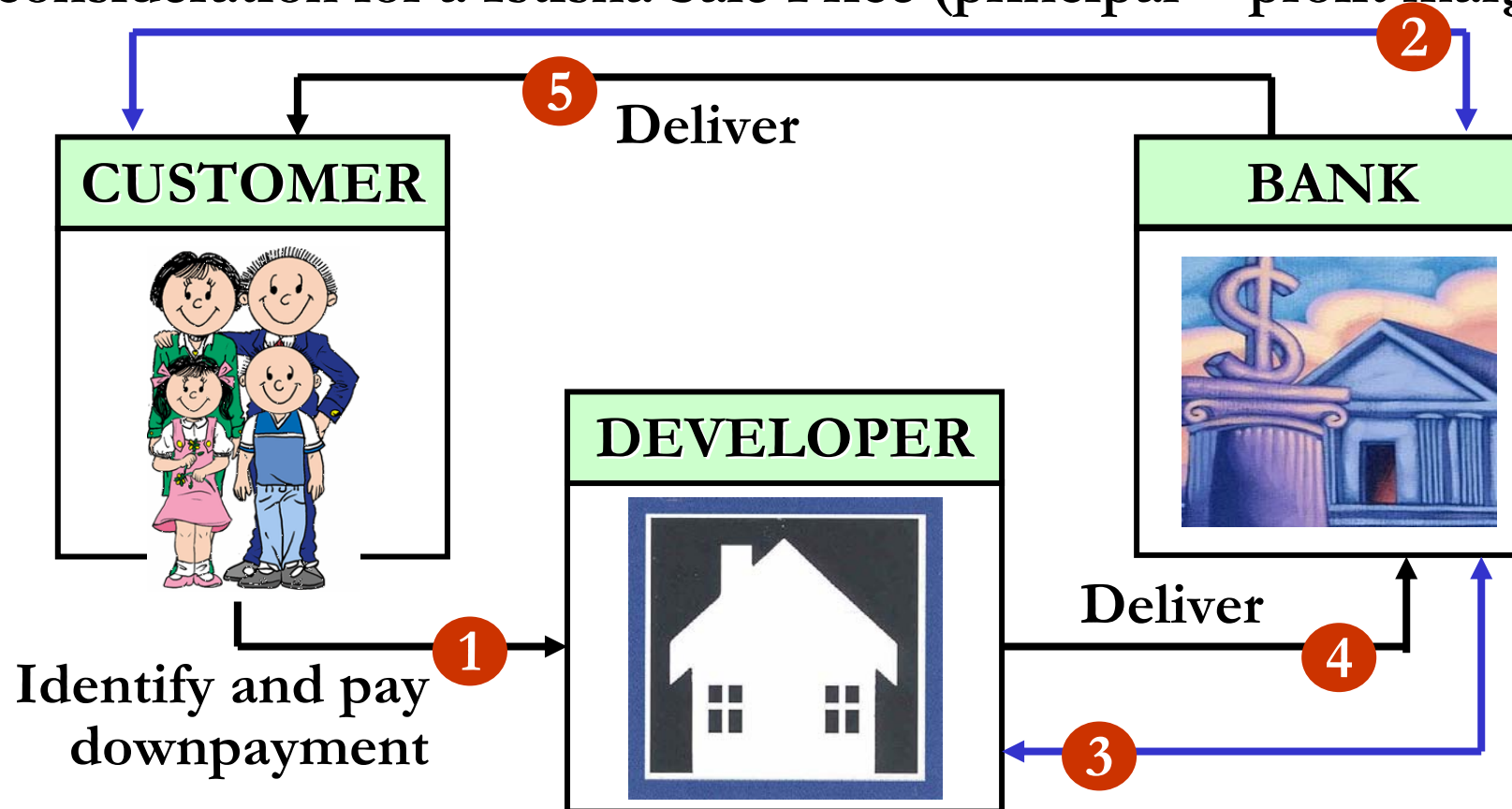


The Developer enters into a Parallel Istisna Agreement with the Bank to construct and deliver the house in consideration for a Istisna Purchase Price (principal)

Parallel Istisna Home Financing



Customer enters into 1st Istisna Sale Agreement where the Bank agree to construct and deliver the house to the Customer in consideration for a Istisna Sale Price (principal + profit margin)



The Bank enters into 2nd Istisna Purchase Agreement where Developer agree to construct and deliver the house to the Bank in consideration for a Istisna Purchase Price (principal)



3c

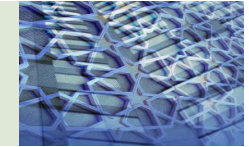
Motor Vehicle Financing

Application of Islamic Contracts - Comparison

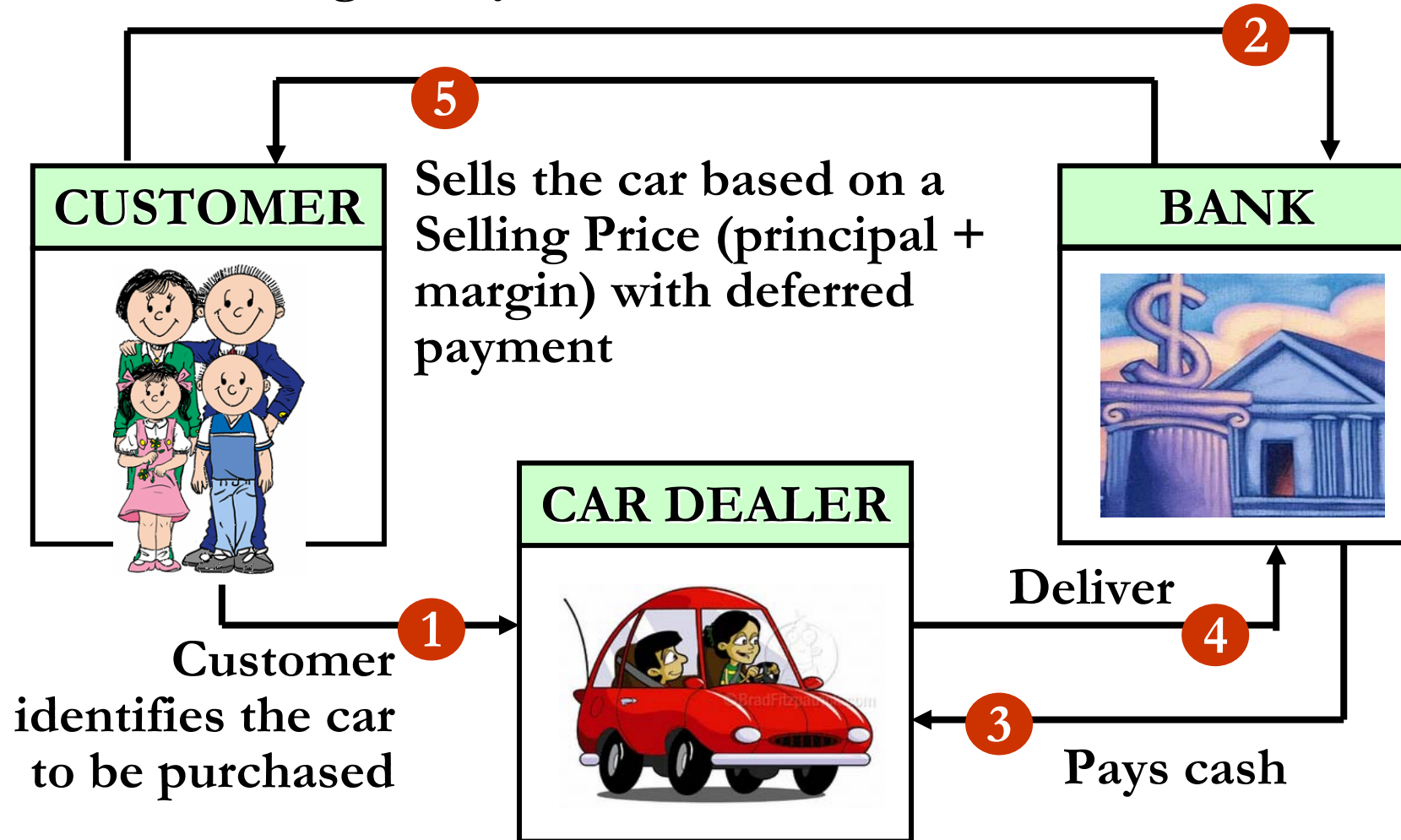
Products	Shariah Principles (Malaysia)	Shariah Principles (International)
Motor Vehicle Financing	Ijarah Thumma Al Bai/Bai Bithaman Ajil (Bai Inah)/Murabahah	Musyarakah Mutanaqisah/Murabahah/Ijarah Muntahiyah Al Tamlik/ Ijarah Wa Iqtina

- Various Islamic contracts are being practised by Islamic Banks in offering car financing. Ijarah Thumma Al Bai is widely adopted in Malaysia.
- Product innovation underway to utilise Murabahah.
- Standard Chartered Bank (Pakistan) adopts the Musyarakah Mutanaqisah principle for its car financing.

Murabahah Vehicle Financing



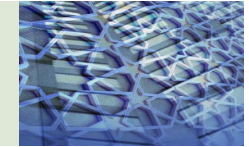
Customer approaches the Bank and obtain Murabahah financing to buy the car based on a Purchase Price



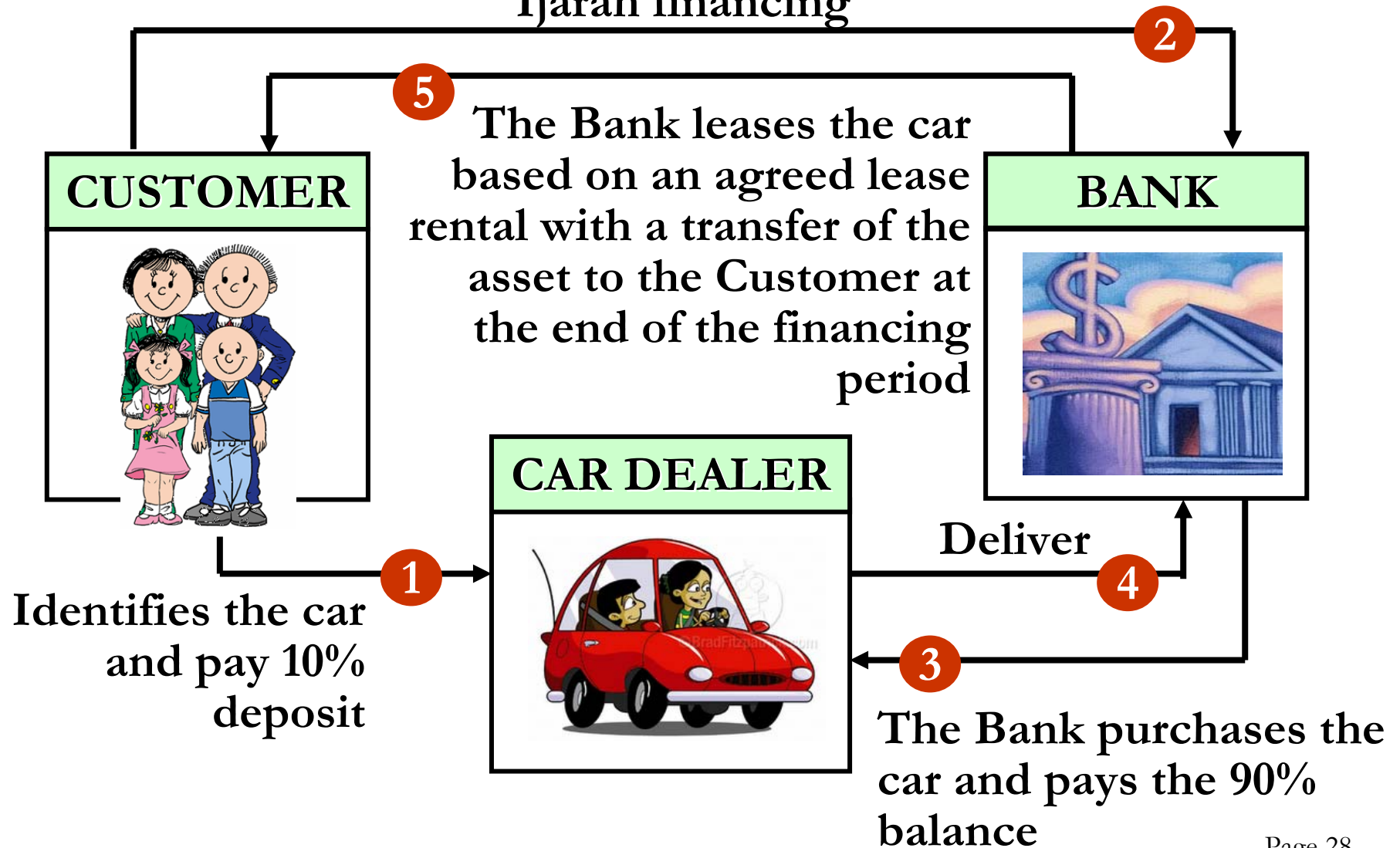


- Under Murabahah ownership is with the Customer. In the event of default, the Bank would exercise its Power of Attorney or assignment to auction the car but this would involve the Bank going to Court which is tedious.
- In Malaysia, car financing under Ijarah Thumma Al Bai is govern under HP Act 1967. There is currently, no Islamic HP Act. Currently in the process of being developed.

Ijarah Vehicle Financing



Customer approaches the Bank and obtain Ijarah financing





3d

Charge Cards

Application of Islamic Contracts - Comparison

Products	Shariah Principles (Malaysia)	Shariah Principles (International)
Charge Cards	Bai Bithaman Ajil (Bai Inah)/ Wadiah/Qardh Hasan	Tawarruq/Ijarah

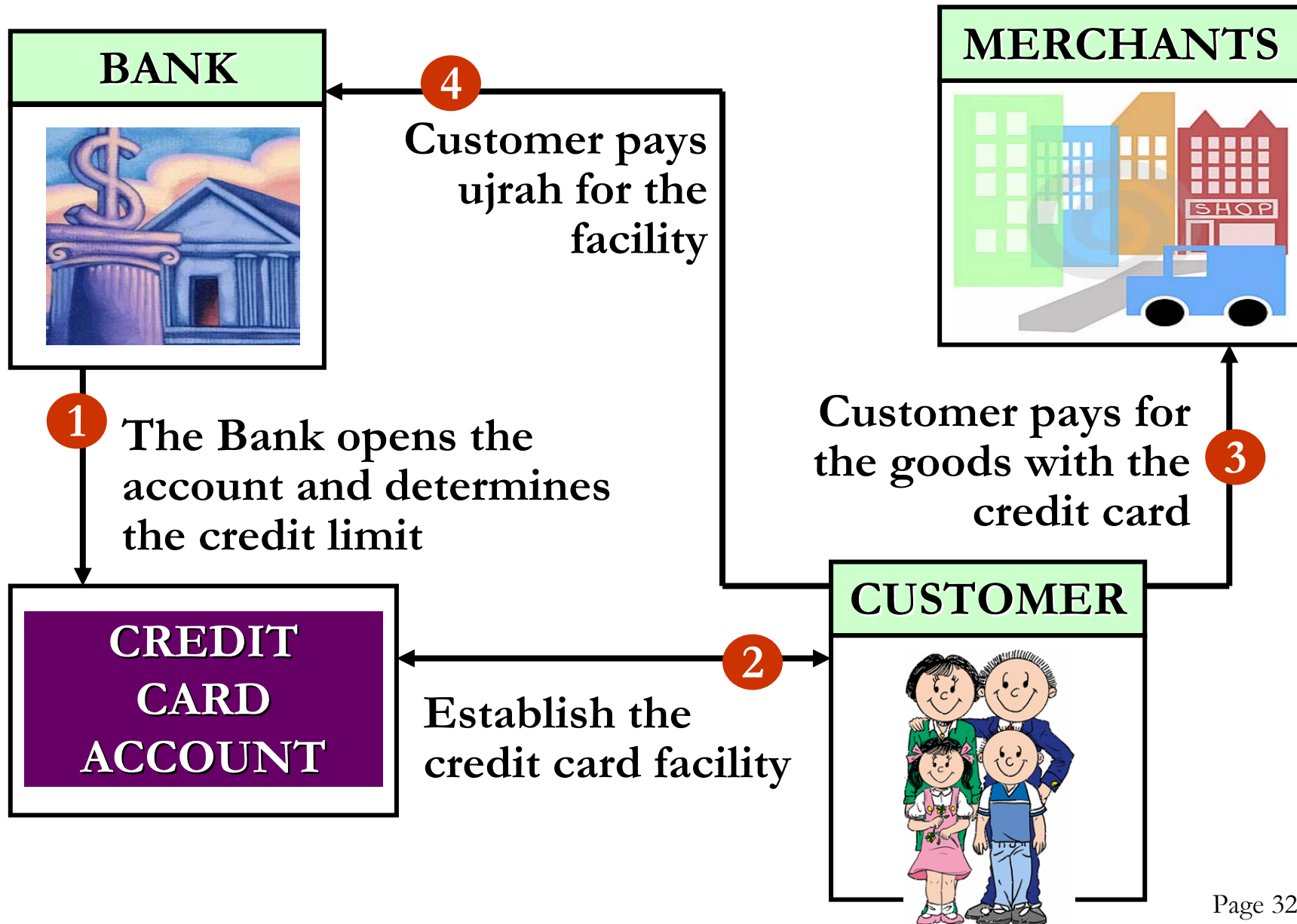
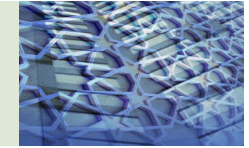
- Some Malaysian Islamic Banks use a combination of Bai Inah, Wadiah and Qardh Hasan (benevolent financing) in providing the service.
- Most International Islamic Banks uses the contract of Tawarruq.
- KFH adopts the contract of Ijarah Muntahiyah Bi Tamlik for its credit cards. However, purchases are confined to purchase of goods which are leaseable.

Innovation and Issues in Product Development

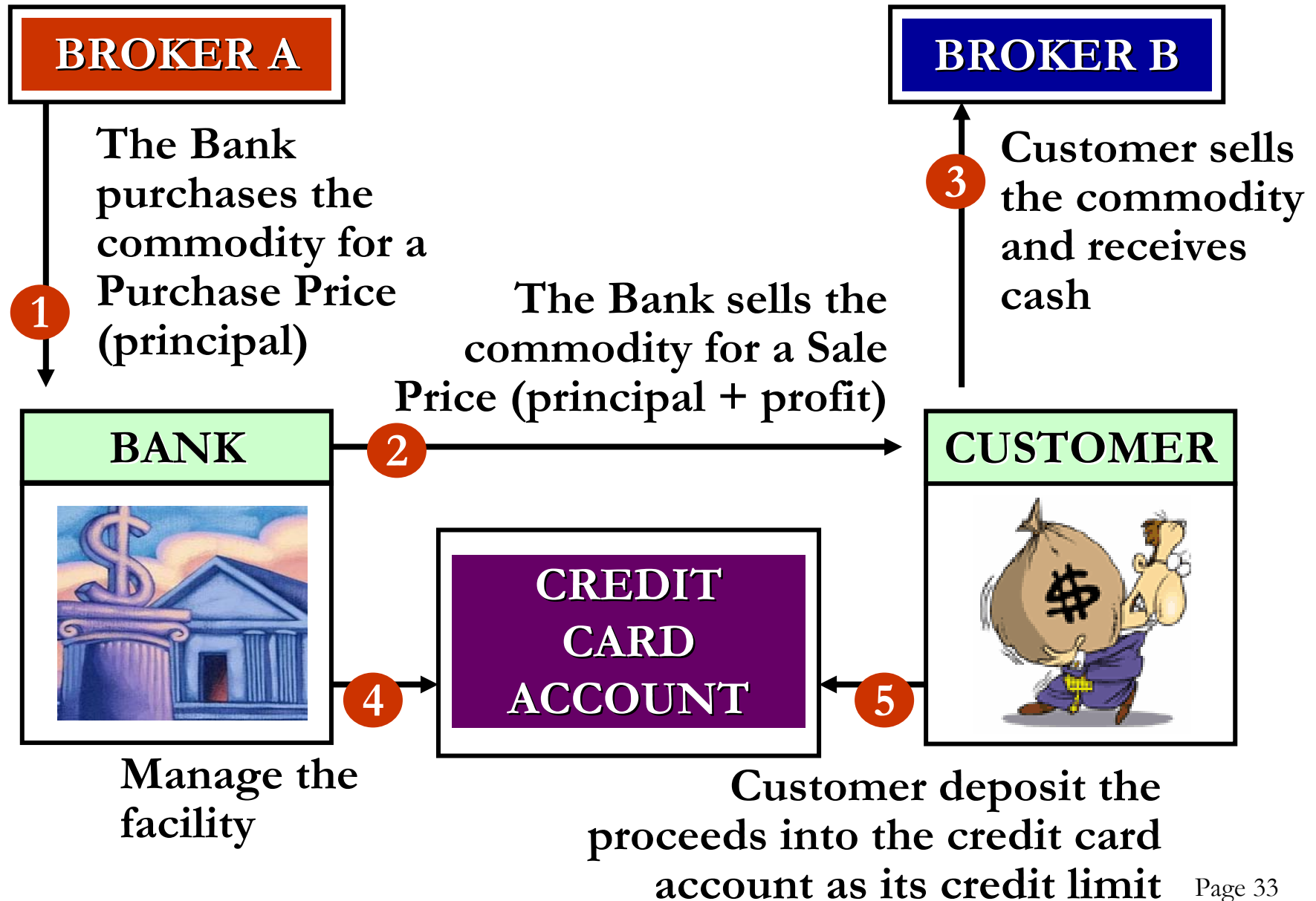
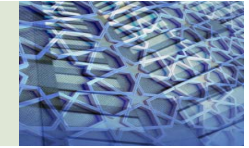


- Interest free.
- No charging of late payment is allowed.
- Some of the structures that have been adopted are debt free.
Concept of debit card.
- Alternative principle is to base the card on “Ujra” or service charge. An annual service charge is levied depending on the credit size payable in installments (monthly/quarterly).
- The concept of Tawarruq is used to solve issues pertaining to purchases of intangibles such as services, cash withdrawals and consumables.

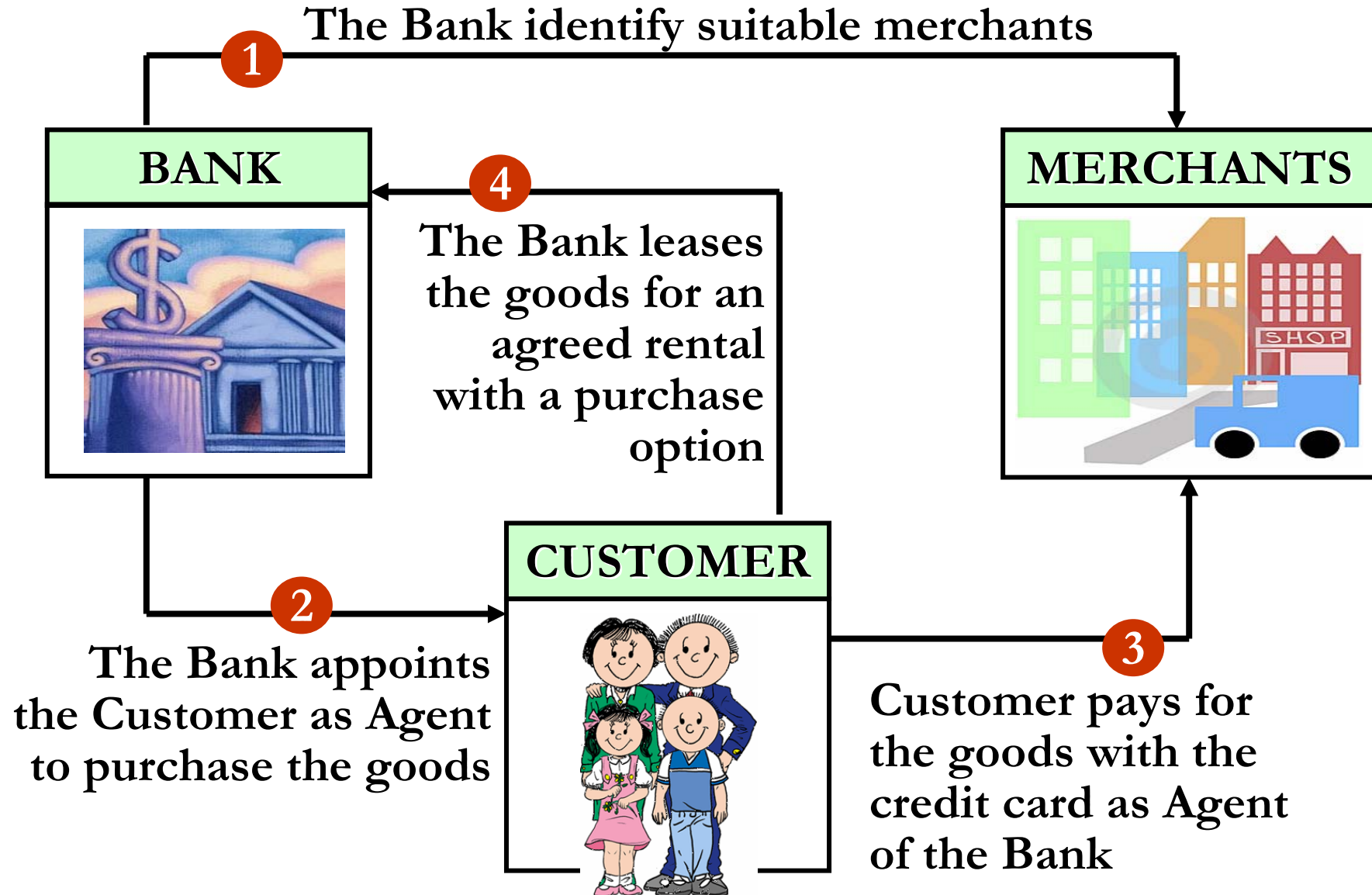
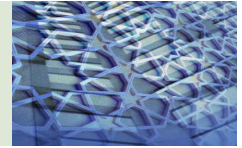
Alternative : Ujrah Based Credit Cards



Tawarruq Based Credit Cards



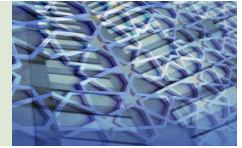
Ijarah Based Credit Cards





Challengers and Sustainability

4



- **What are the constraints and challenges faced by Islamic retail product providers and those who have successfully launched their products?**
- **Why is there a need to grow retail products?**
- **What are the critical success factors?**



EONCAP Islamic Bank Berhad

17th Floor, Menara EON Bank

288 Jalan Raja Laut

50350 Kuala Lumpur

Tel: +603-2694 1188

Fax: +603-2694 8688

www.eoncap-islamicbank.com.my