

# Islamic Finance in Tanzania: Success or Failure?



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# 1.0 Introduction



- Since 1975, when the first Islamic commercial bank was established in Dubai, Islamic finance has come a long way.
- It has grown rapidly in recent decades and its global assets have been estimated to be around US \$2.1 trillion across the banking sector, capital markets, and [\*takaful\*](#), or Islamic insurance. (See **S&P Global Ratings 2017 Edition**)
- Islamic finance remains concentrated primarily in some oil-exporting countries, with the Gulf Cooperation Council (GCC) countries, plus Malaysia and Iran, accounting for more than 80% of the industry assets,

# Introduction



- That being the case, there have been downside in this rather young industry of lately. These include negative impact of policy responses to low oil prices in the industry's core countries, as well as a lack of standardization in a sector that is still a collection of local small industries rather than a truly global industry.
- Offsetting these negatives are the efforts deployed by major stakeholders; -
  - to increase the standardization of legal documentation and Sharia interpretation
  - the continuous interest from an increasing base of customers
  - the potential contribution of the industry to the financing of the United Nations' Sustainable Development Goals (UN SDGs) and
  - the expected new opportunities created by countries looking to tap or return to the Sukuk market.

# Introduction



- ***Second***, there is a natural connection between the principles of Islamic finance and some of the UN SDGs. Both of them want to achieve more responsible, equitable, and real-economy-oriented financing.
- ***Finally***, there are several success stories in Islamic finance and new players can leverage the experience of more advanced ones in their strategy to develop Islamic finance locally (**In Tanzania, Amana Bank** being a typical example)

# Introduction

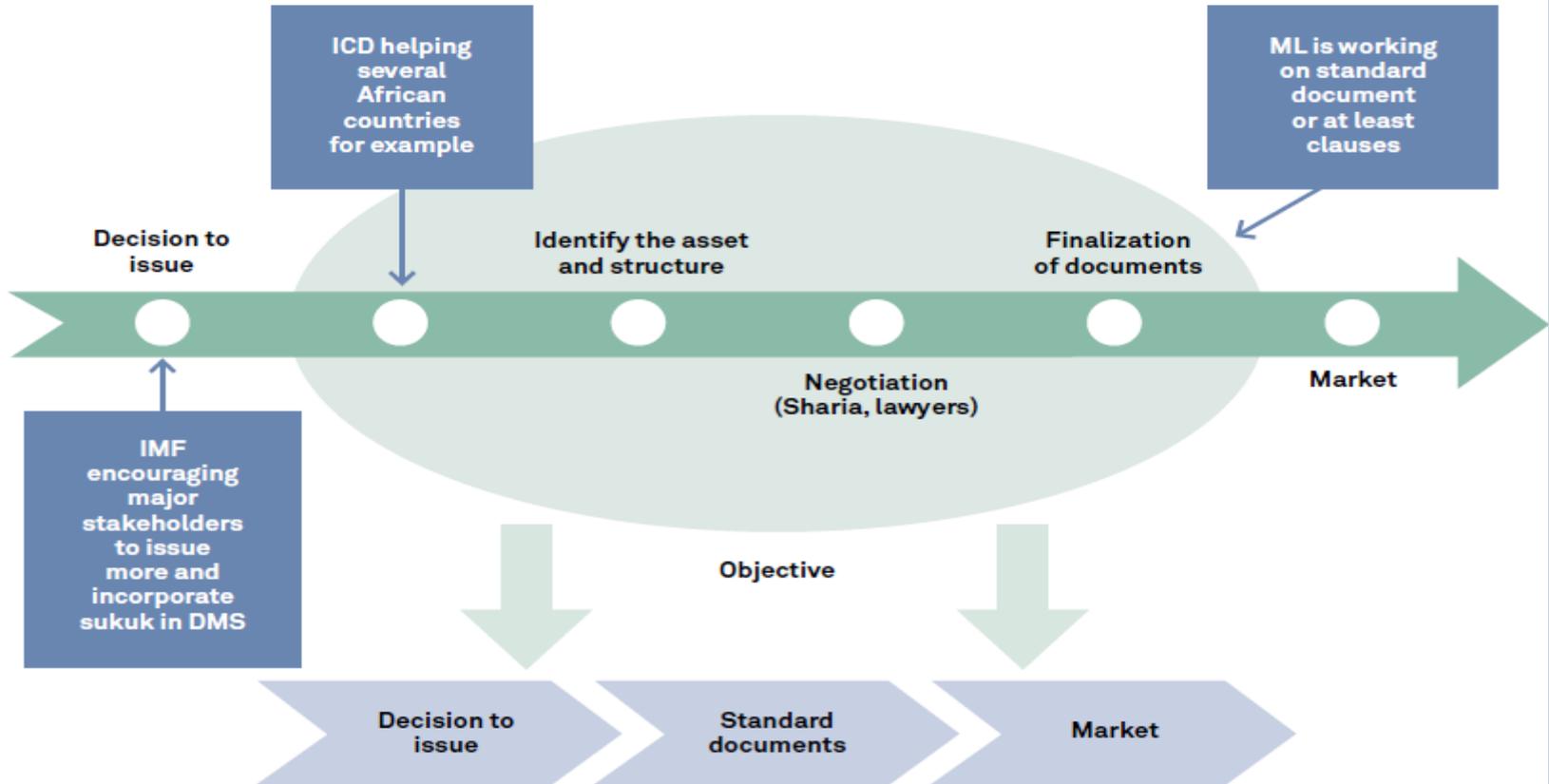


- On a positive note, there are some opportunities that could put the industry back on track for strong growth and continued globalization.
- *First*, stakeholders are getting more serious and aggressive about standardization of documents and Sharia interpretation.
- Some players are working on standard legal structures to be used by sovereign issuers to shorten and ease the process of Sukuk issuance.

# Introduction



Chart 6 - Standardization Objective

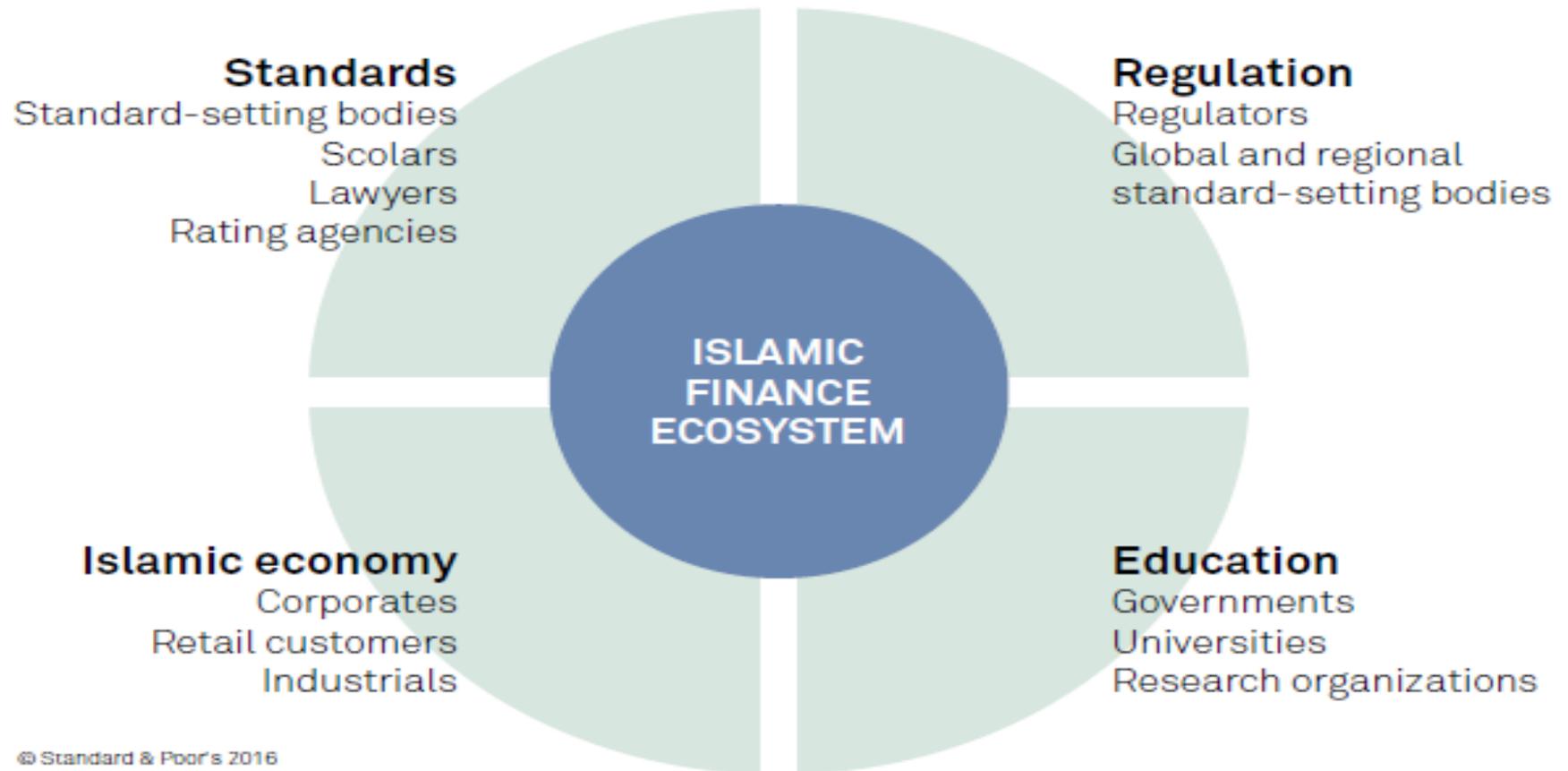


IMF: International Monetary Fund, DMS: Debt Management Strategy, ICD: Islamic Corporation for the Development of the Private Sector  
MLIs: Multilateral Lending Institutions

# Introduction



**Chart 7 - Islamic Finance Industry Consolidation**



## 2.0 What they Say About Islamic Banking?



- Given ten year or so of Islamic Finance in Tanzania, how do public opinions characterize the development of this most prominent form of faith-based finance? And what criteria do they use?

### *Islamic Finance is “Sharia Arbitrage”*

- Meaning what is prohibited in conventional finance becomes permissible when deemed “**Shari’a compliant**” despite having similar, if not the same, economic substance.(The Salafis, Hizb Tahrir etc)

# What they Say About Islamic Banking?



## “*A social Failure*”

- They claim that Islamic finance does not share the actual aspirations or the foundational claims of Islamic moral economy (*Christians and non-Muslims alike*)

## *Not serving Average Muslims*

- Islamic finance, especially the financing side, is not so well received and enjoyed by average Muslims who lack the required conditions to receive financing

# What they Say About Islamic Banking?



- Opportunities in Islamic finance are great and despite current growth for Islamic financial products portfolio, there is still room for further expansion (SME's, Sukuk etc)
- In 2009, Bloomberg quoted the Vatican's official newspaper, *L'Osservatore Romano*, as saying, **“The ethical principles on which Islamic finance is based may bring banks closer to their clients and to the true spirit which should mark every financial service”**

### 3.0 The Current Environment *Vis a Vis* Islamic Finance in Tanzania

- So far Islamic finance has probably been more successful in offering an alternative perspective on finance and banking rather than in providing a ***substantively*** effective way of financing
- The emphasis on the theory of Islamic finance on social consciousness, risk-sharing, redistribution of wealth and opportunity, and making finance the servant and not the master of the real economy are what many of its players focus upon

## The Current Environment *Vis a Vis* Islamic Finance in Tanzania



- But Islamic finance in Tanzania has found it hard to put the theory into proper practice. Why?
- The list of reasons ranges from historical, legal, political, regulatory, taxation, consumer behaviour, lack of creativity, lack of researches, lack of aggressive marketing and beyond
- *An important reason is that, like in any secular country, Islamic finance is generally made to fit into a system designed for conventional finance, and in the process of making concessions, it seems to lose what its critics regard as its substance i.e. its **ethical values***

## The Current Environment *Vis a Vis* Islamic Finance in Tanzania



- Islamic finance, being an integral part of an Islamic economic system, can be practiced more effectively in an environment which conforms with the tenets of Islam
- However, in Tanzania by the *rule of thumb*, there isn't such an environment. Thus, let us together use some essential requirements to gauge whether Islamic finance in Tanzania has been a success or failure
- With this gauge, we can indeed draw a conclusion “has Islamic Finance in Tanzania been a success or failure?”

## 4.0 The Post Mortem



- *A Supportive Legal Framework and Swift Judicial System*
  - An effective legal framework ensuring speedy justice is essential for a good society, it is more so for the success of Islamic finance in a country
  - This is because its investment risk is more than that of a conventional interest-based bank as its dealings are often based on profit and loss portfolios

# The Post Mortem



- *Disciplined Entrepreneurship*

- It would minimize cases of malfeasance and mismanagement. Besides, a banker must extend from being merely a financier to a role-player in business.
- Although a **Murabaha** transaction in Islamic banking does provide an opportunity to a banker to share in business, the Islamic banks generally limit themselves to being inactive partners for their credit risk only.

**Example:** An Islamic Window selling its products alongside conventional products, attendants claiming that the same interest rate will be but *you can have Islamic loans*

# The Post Mortem



## *Conceptual Change from Credit Risk to Overall Risk Management*

- While it is difficult to predict, with any degree of certainty, the operating results of an enterprise and the magnitudes of profit and loss, all the same, it seems unjust if the party providing the capital is guaranteed a fixed and predetermined rate of return, and the other party undertaking the enterprise is made to bear the uncertainty alone.
- Under the circumstances, an Islamic financial institution has religious, moral and ethical obligation not only to focus on credit risk but also view all the business risks of the entrepreneur in which he has invested the bank's money.

# The Post Mortem



## *Strong Ethical Values*

- The success of Islamic finance in a society is related to the extent of acceptability the doctrine of trusteeship transformation of the self-interested profit-oriented behaviour of non Islamic financial system into altruistic and value-oriented behaviour of Islamic finance

## *Presence of Supreme Country Sharia Council*

- The function of Sharia Council in maintaining Islamic banking and finance activities in a country within orbit of Islamic injunctions is dependable on its legal status and the extent of implementation of its opinion

# The Post Mortem



- The opinions of Sharia Councils/Boards of different Islamic financial institutions in the country may not necessarily be unified
- There is, therefore, a need for a Supreme Country Sharia Council representing Islamic finance customers all over the country to deal about various issues confronted by Islamic financial institutions in Tanzania

# The Post Mortem



## *Uniform Accounting Standards*

- There is need for harmonization of operations of Islamic financial institutions in respect to accounting standards
- There is a dire need on having significant accounting policies in the country on which the Islamic financial institutions statements are based

## *Committed Management*

- If the management of an Islamic financial institution is determined to get into the business of Islamic finance, it can easily evolve a strategy for the same, formulate a plan for a specific time-frame and implement it accordingly
- There has been lack of clear commitments on some financial institutions running Islamic finance (No funds for marketing Islamic finance products, no respect for Sharia Board etc)

# The Post Mortem



## *Progressive and Modern Outlook*

- To ensure successful management in Islamic financial institutions, there is need to apply all the modern tools of managing corporate business, including management of human assets, offices, information resources, marketing etc
- One SME Islamic financial institutions has run into big problems due to failure to implement this important tool of trade

# Conclusion



## *Body to Evaluate Islamic Financial institutions*

- In order to; -
  - ensure quality and standards in management of Islamic financial institutions and
  - to build confidence of the general public in Islamic financial system, there is need to establish some professional body responsible to define professional standards and ethics and other aspects of Islamic financial institutions.
- It also certifies the level of financial health and such institutions. In Tanzania still CIFCA has no mandate. It has to be the like of AAOIFI and IIFSB



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