

GOVERNOR'S SPEECH



Governor	: Mr. Jameel Ahmad
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Theme: "ICM development with ecosystem completion: innovation, growth, and transformation"

- *Senator Muhammad Ishaq Dar, Minister for Finance and Revenue*
- *Mr. Ashfaq Tola, Minister and Chairman, Reforms and Resource Mobilization Commission*
- *His Excellency Shaikh Ebrahim Bin Khalifa Al-Khalifa, Chairman, AAOIFI Board of Trustees*
- *Mr. Akif Saeed, Chairman, SECP*
- *Distinguished speakers, ladies and gentlemen;*

Assalam o Alaikum and Good Morning;

It gives me a great pleasure to be here today to address this distinguished audience. At the very beginning, I would like to extend my appreciation to the AAOIFI and SECP for jointly arranging this international conference on development of Islamic capital markets. This indeed is a commendable initiative to bring together stakeholders from public and private sectors, multilateral institutions, and prominent experts to deliberate issues pertaining to the development of Islamic capital markets. I hope that the insights and knowledge exchange in this conference will help us build a roadmap for development of a sustainable, diversified, and inclusive Islamic Capital Market in Pakistan.

Without a doubt, the capital market is one of the most crucial indicators reflecting an economy's health. The development and deepening of Islamic capital markets is

imperative to support economic growth, mobilize savings, improve resource allocation, and provide diverse funding sources to economic agents. Today, Islamic finance as a global industry has crossed the USD 3 trillion mark. Islamic capital markets account for around 31 percent share of this growing pie. The Islamic Capital Market has registered substantial growth over the years, mainly due to the significant increase in Sukuk issuances particularly the sovereign sukuk.

Despite their growing importance, Islamic capital markets are generally in nascent stages of development in most jurisdictions, compared to conventional counterparts. In my assessment, the main impediments to the growth of Islamic Capital Markets include: (a) gaps in institutional, legal and regulatory frameworks, (b) lack of efficient ways for price formation and discovery, (c) lack of diversity in Islamic capital market instruments and investor base, and (d) gaps in investor education and awareness.

Looking at the developments in Pakistan, Islamic banking has grown into a systemically important sector in Pakistan. Its assets have grown by an average of 24 percent per annum over the past decade, to stand at 20 percent in terms of current market share of the overall banking industry. SBP has put in place a comprehensive legal, regulatory and Shariah governance framework for the Islamic banking industry.

As many of you already know, a fresh impetus has been provided to Islamic finance by the Federal Shariat Court (FSC) judgment for elimination of Riba from the economy by 2027. We are committed to transform the financial sector into a system based on Shariah principles. In this regard, the Government of Pakistan has constituted a Steering Committee for providing strategic guidance regarding the implementation of the FSC's judgement. To this end, SBP and SECP, as a part of this Steering Committee, are playing their role in achieving the aligned goals for the transformation towards Islamic economic system.

Let me highlight few key issues and challenges pertaining to the development of Islamic capital market, particularly of Islamic Debt Market. One of the biggest challenges in implementing the FSC judgment is the conversion of public debt into equivalent Shariah compliant modes. Lack of adequate sovereign assets has remained a major impediment to regular issuance of asset-based Sukuk by the government until recently. While Sukuk issuances are now being auctioned regularly, the size of issuances needs to be scaled-up massively. Currently, out of total government domestic debt obligations of nearly Rs 35 trillion, the volume of outstanding Sukuk stands at Rs 2.8 trillion only. Thus, there exists a huge gap between the overall

financing requirements and Shariah compliant financing through Sukuk. Also, despite regular issuances, the secondary market of GOP Sukuk is less diversified.

Meanwhile, the size of Pakistan's Corporate Debt Market (both conventional and Islamic) remains very small, equivalent to less than 1% of GDP. The secondary market is also not developed and deep. The slower-than-expected development of the corporate debt market is mainly attributed to high issuance costs, lack of short-term securities, complex documentation (more so for Shariah based instruments), and lack of required skill-set with investment banks and support financial services.

A cross-cutting issue for Islamic finance is a lack of harmonization in some existing Islamic products and difference of opinion among various Shariah Scholars is a hindrance in building investors' confidence. This is notwithstanding the tremendous role played by AAOIFI in the development and issuance of global standards.

Ladies and gentlemen;

Despite the impediments to Islamic capital market development that I have alluded to, I am convinced that the solutions are well within our grasp.

First, in terms of conversion of government debt to Islamic mode, the regular issuances of Sukuk with higher volumes and varying tenures is required. In this respect, State Bank, under the guidance of the Steering Committee, has constituted a high-level working group to develop practical solutions on alternate Shariah compliant structures, especially Asset Light Sukuk Structures. I believe that Asset Light Sukuk has the potential to propel Islamic Finance and provide much needed liquidity management tools that Islamic Financial Industry needs, apart from helping the government to fulfil its financing requirements.

Second, to develop the corporate Sukuk, coordinated and sustained efforts on multiple fronts are needed. It is essential to provide an enabling tax, regulatory and policy environment, coupled with additional incentives for issuers and investors. This needs to be augmented with raising awareness level amongst the corporates about the potential of raising Shariah-compliant funding through capital market.

Third, retail investors can also play an important role in the growth of the Islamic debt and capital market, particularly in jurisdictions with younger populations like Pakistan. Sukuk can be used for creation of Sukuk funds for retail distribution, which can increase the demand for Sukuk exponentially, if they gain traction. In this regard, investor education programs can play a vital role in raising awareness and

understanding of Islamic finance. Also, Islamic finance through digital offerings can help in inclusion of a rural unbanked population into the formal financial system.

Fourth, strengthening the market infrastructure is of utmost importance. Development of Shariah Compliant hedging instruments, and establishing the appropriate benchmarks and yield curve for Islamic capital market instruments will play an important role. This will allow investors to hedge their risks and measure performance of their investments, increasing their appetite for investment in Islamic capital market and portfolio diversification. By focusing on improving trading platforms, clearing systems, and other market infrastructure, we can enhance efficiency, liquidity, and accessibility within our Islamic capital markets.

Fifth, collaboration among regulators, financial institutions, industry players, and Shariah scholars is essential to harmonize their views. It will help enabling standardization of Islamic financial contracts and simplifying the processes. Further, this collaboration will foster knowledge sharing and exchange of best practices. Centralized Shariah bodies can ensure consistency in Shariah rulings and instill greater confidence amongst the general public. International integration is also key to the global visibility and competitiveness of our Islamic capital markets.

Sixth, investing in research, talent development, and specialized training programs is also crucial for building a skilled workforce. This entails capacity building of Islamic investment banks, providers of supporting financial services, such as credit rating agencies, and qualified professionals and Shariah Scholars. Making all these players well-versed with capital market issues will help efficient structuring, arranging and execution of Islamic capital market transactions.

Last but not least, we must also delve deeper on how to further embrace Islamic fintech, digital finance, climate finance, and innovation with a futuristic view to achieve holistic and sustainable development of an inclusive Islamic capital market.

Ladies and gentlemen;

Going forward, I envision Pakistan's Islamic Capital market to be a fair, modern, efficient and globally competitive market, responsive to the needs of its stakeholders, and based on sound regulatory principles. It should provide the impetus for sustainable economic growth and be a major facilitator for investment activity and fund-raising in the country. However, this cannot be achieved without strong political backing, pro-active regulatory support in the form of conducive laws and regulations, investment in research and development, and capacity building of human resource.

We must strive to provide the necessary infrastructure to Islamic markets as has been available to conventional markets since decades.

I would like to end by thanking the finance minister for his commitment, guidance, and continuous support in this challenging journey of transforming our financial system on Islamic principles. I want to reiterate that State Bank of Pakistan assures its relentless and constant support for development and transformation of the different areas of Islamic finance in Pakistan. We would continue to work with SECP, government bodies and academia and all relevant stakeholders, such as AAOIFI, to foster development of Shariah compliant capital market to realize the full potential of Islamic finance.

In conclusion, I would like to thank the organizers for inviting me to address this august forum. Thank you all for your attention.
