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# ISLAMIC FINANCE WEBINAR SERIES 2: INNOVATION IN ISLAMIC BANKING

Presenters:

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# PART 1: ASSET/ FINANCING - Introduction



## The role of Islamic Bank:

Trader, partner/ Wa'd Undertaking



# PART 1: ASSET/ FINANCING

## CONCEPT OF FINANCIAL ASSETS AS PER IFRS 9

Any asset that is:

(a) cash;

(b) an equity instrument of another entity;

(c) a contractual right:

- to receive cash or another financial asset from another entity; or
- to exchange financial assets or financial liabilities with another entity

(d) a contract that will or may be settled in the entity's own equity instruments and is:

- a non-derivative for which the entity is or may be obliged to receive a variable number of the entity's own equity instruments; or
- a derivative .....



# PART 1: ASSET/ FINANCING

## FINANCIAL ASSETS - A SHARIAH PERSPECTIVE

- Shariah recognizes the concept of financial assets.
- Shariah, however, sets certain rules to trade financial assets.
- Shariah restricts the trade of financial assets representing cash or debt, to par value only.
- Financial asset to be traded should represent any tangible asset, usufruct or services or a combination of these with cash/debt.



# PART 1: ASSET/ FINANCING

## INNOVATION – RUNNING MUSHARAKAH

- Running Musharakah was conceived as a Shariah compliant alternative to the Running Finance/Over Draft facility offered by conventional banks.
- A partnership in the operating activities based on profit/ loss sharing.



# PART 1: ASSET/ FINANCING

## INNOVATION – RUNNING MUSHARAKAH

### KEY FEATURES

- Enables the clients to draw and repay funds against an approved limit.
- Can be offered to finance any Shariah Compliant Financing need of the client.
- Leverages the concept of profit ceiling and dual profit/loss sharing ratios.
- The product marked a paradigm shift from trade based financing products to an equity based financing model.
- One of the most widely used financing products by Corporate clients in Pakistan.



# PART 1: ASSET/ FINANCING

## RUNNING MUSHARAKAH - CONCEPT

- The Bank enters into a partnership with Client by investing cash in the ongoing business operations of the Client for a set period e.g. quarter, half year, year, etc.
- Partnership is restricted to Operating Activities and Bank does not participate in the Investing and Financing Activities.
- Operating Activities of a manufacturing or trading concern comprises of purchase, production and sale of goods.
- Drawdowns by the Client are considered as Bank's investment and repayments are considered as redemption.



# PART 1: ASSET/ FINANCING

## RUNNING MUSHARAKAH - CONCEPT

- Total Investment in Musharakah = Avg. Inventories + Avg. Receivable
- Bank Investment is the weighted average of daily outstanding balance (drawdowns less repayments) in Client's account.
- Client Investment = Total Investment – Bank's Investment.
- Musharakah Profit and loss is calculated on the basis on the quarterly or annual financial statement of the client.
- Musharakah Profit is arrived by excluding certain fixed assets related expenses (e.g. depreciation, repair & maintenance etc.) from Gross Profit.
- Musharakah Profit above a pre-agreed Profit Ceiling goes to Client.
- Musharakah Profit up to Ceiling are shared in the Investment Ratio.
- Loss, if any, is also shared in Investment Ratio.
- Profit Ceiling is set as a Percentage of Total Musharakah Investment at the beginning of Musharakah period.





# PART 1: ASSET/ FINANCING

Adjusted Cost of Goods Sold (ACOGS)		
Figures in PKR "000"	Audited Accounts	For Musharakah
Raw and packing material consumed	15,330,843	15,330,843
Salaries, Wages and other benefits	1,212,579	1,212,579
Utilities	1,580,937	1,580,937
Packing material consumed	267,012	267,012
Stores and spares consumed	454,109	454,109
Repairs and maintenance	39,286	-
Insurance	30,112	-
Rent, Rates and taxes	2,297	-
Depreciation	568,734	-
<b>Total</b>	<b>19,485,909</b>	<b>18,845,480</b>

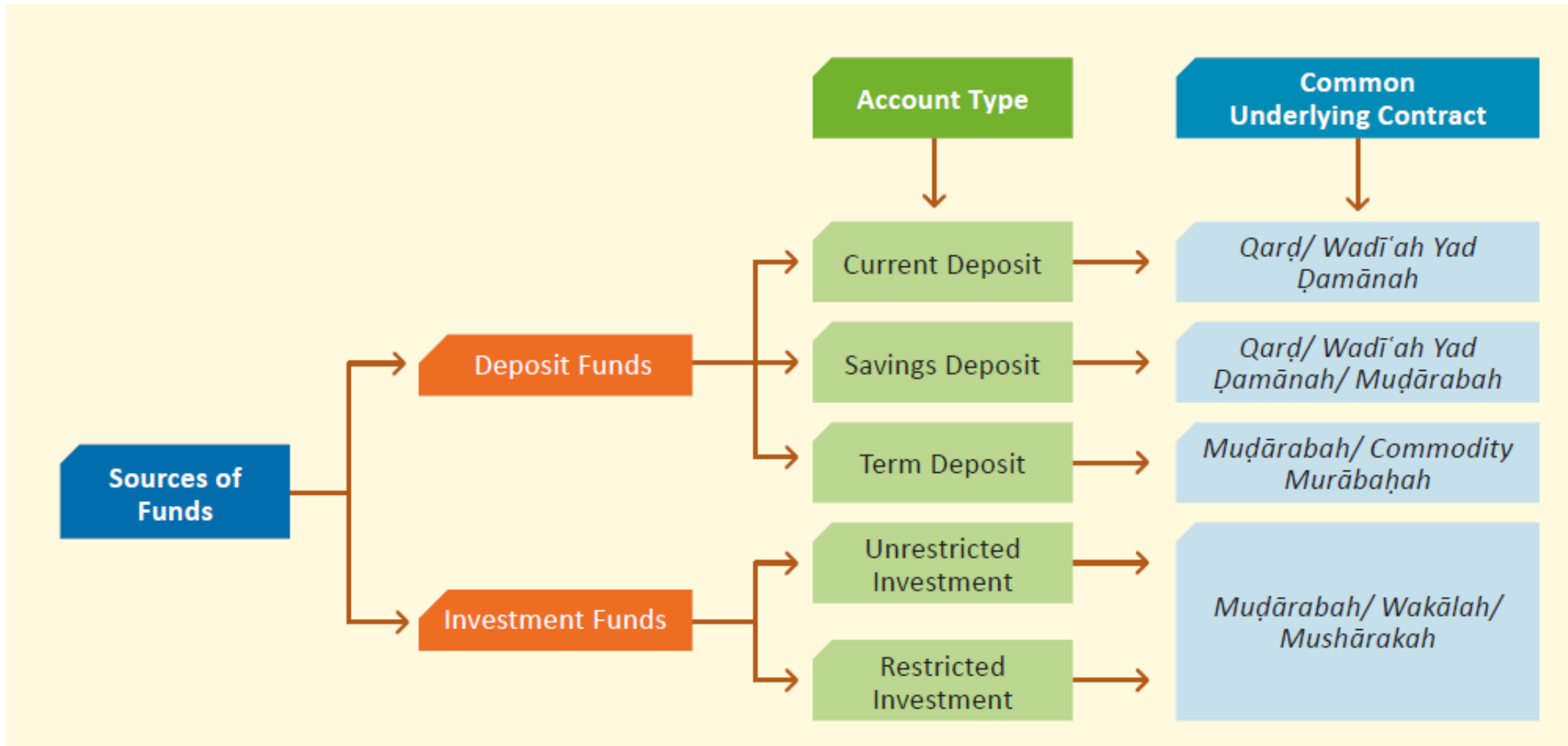
Musharakah Profit		
Figures in PKR "000"	Audited Accounts	For Musharakah
Net Sales	22,090,427	22,090,427
Adjusted Cost of goods sold	19,485,909	18,845,480
Gross Profit	2,604,518	
<b>Musharakah Profit</b>		<b>3,244,947</b>



# PART 1: ASSET/ FINANCING

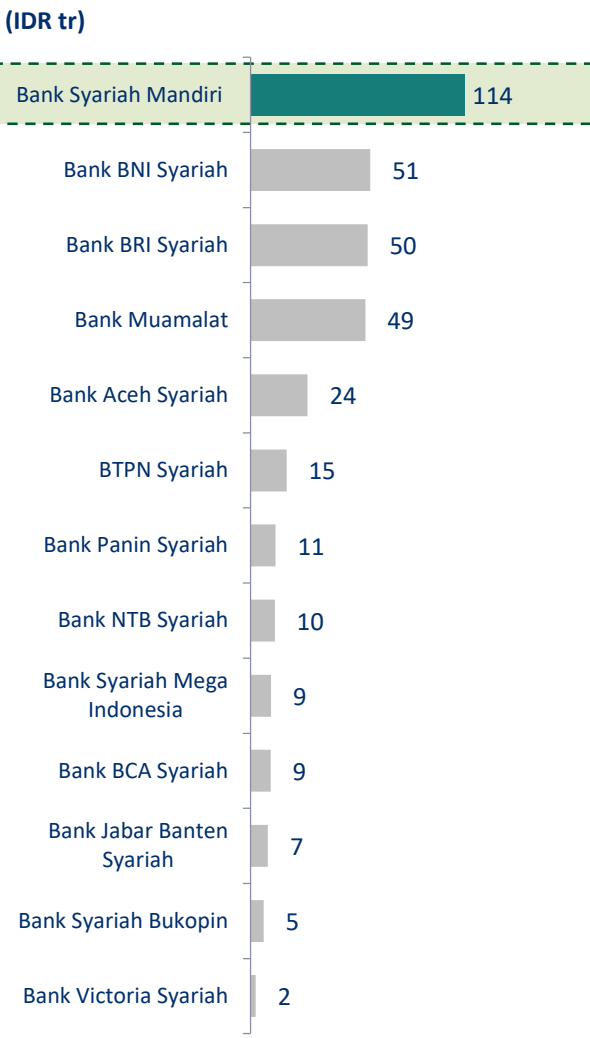
Profit/ Loss Sharing			
Running Musharakah Tenure	365 days		
Customer's Running Musharakah Limit (in PKR "000")	400,000		
Profit Ceiling Rate (% p.a.) (KIBOR based)	7.35%		
<b>Figures in PKR "000"</b>	<b>Total</b>	<b>Bank</b>	<b>Customer</b>
Running Musharakah Investment	4,082,169	279,758	3,802,411
Investment & Profit/(Loss) Sharing Ratio		6.85%	93.15%
Profit Sharing Ratio above Profit Ceiling		0.001%	99.999%
Profit Ceiling Amount	300,039		
Running Musharakah Profit	3,244,947		
Running Musharakah Profit upto Profit Ceiling Amount	300,039	20,562	279,477
Running Musharakah Profit above the Ceiling Amount	2,944,908	29.45	2,944,878
<b>Total</b>	<b>3,244,947</b>	<b>20,592</b>	<b>3,224,355</b>
<b>Difference between Desired &amp; Actual Profit (in PKR "000")</b>			
Bank's Desired Profit	20,562		
Bank's Actual Share in Running Musharakah Profit	20,592		
<b>Difference</b>	<b>29.45</b>		

## PART 2: LIABILITY/ FUNDING - Introduction

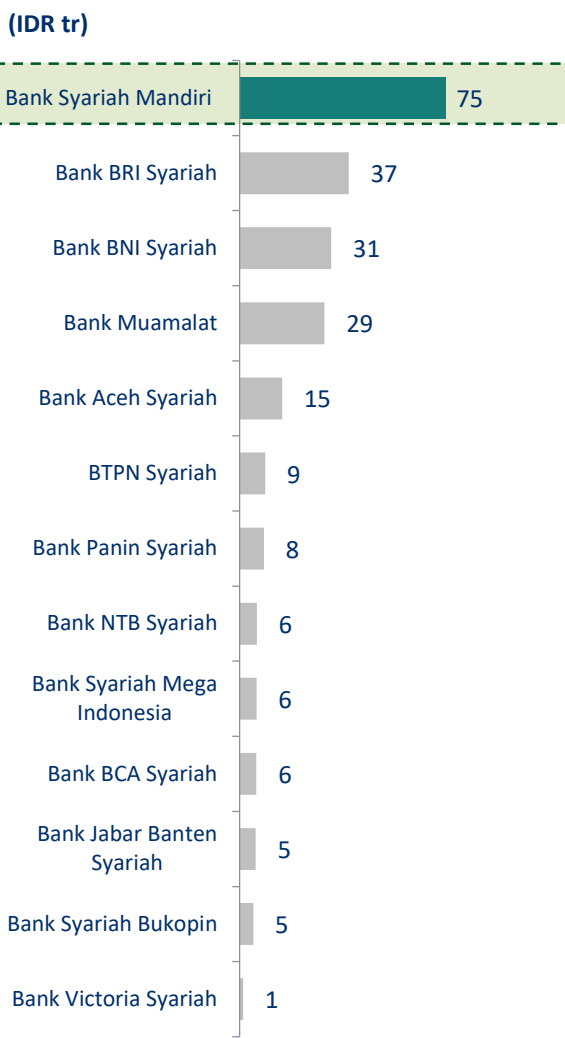


# MANDIRI SYARIAH IS THE LARGEST SHARIA BANK IN INDONESIA WITH HUGE SAVINGS ACCOUNT

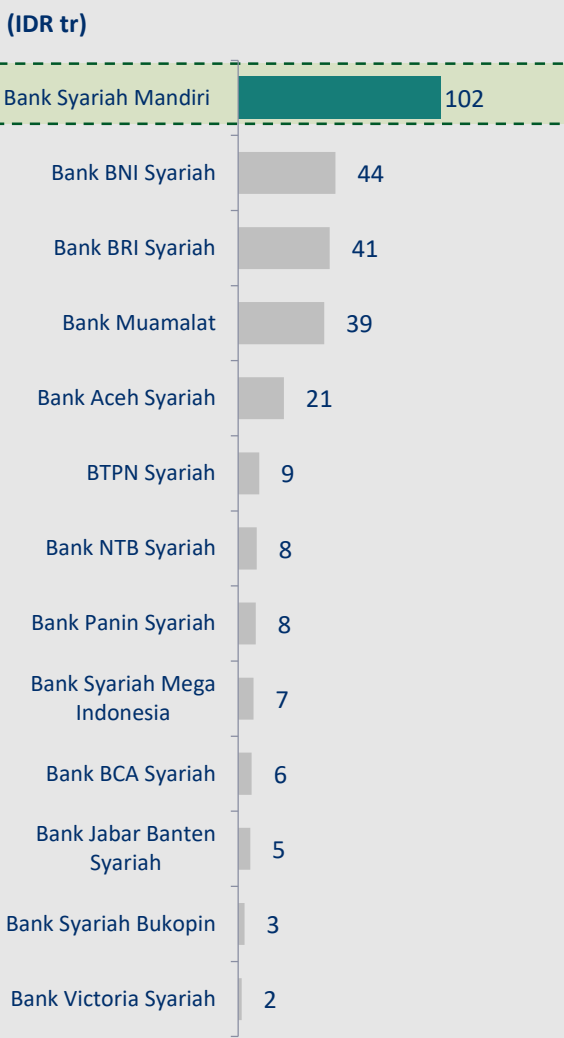
Largest Total Assets



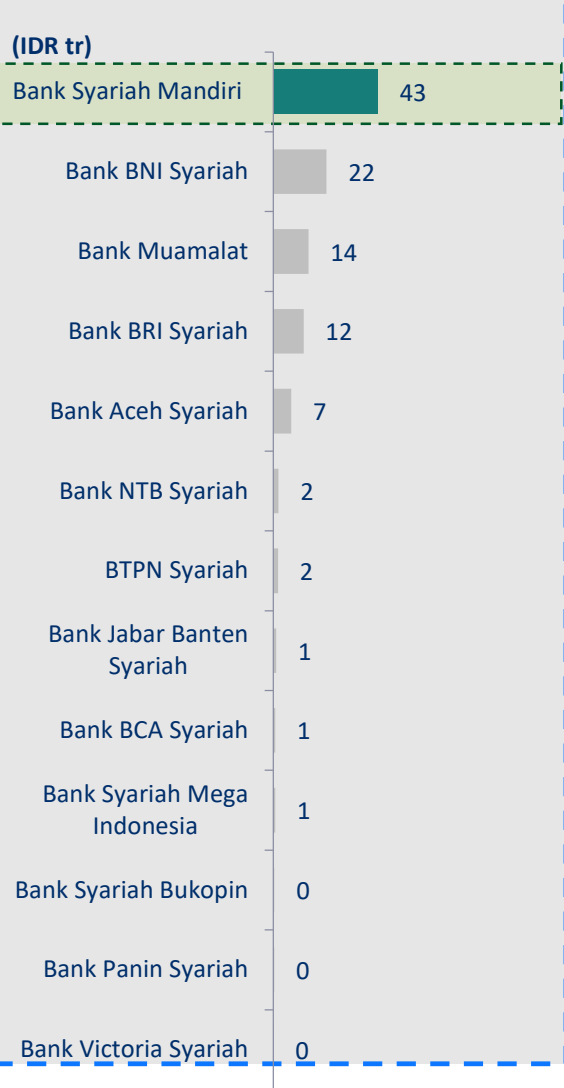
Largest Financing Portfolio



Largest Deposits Base



Savings

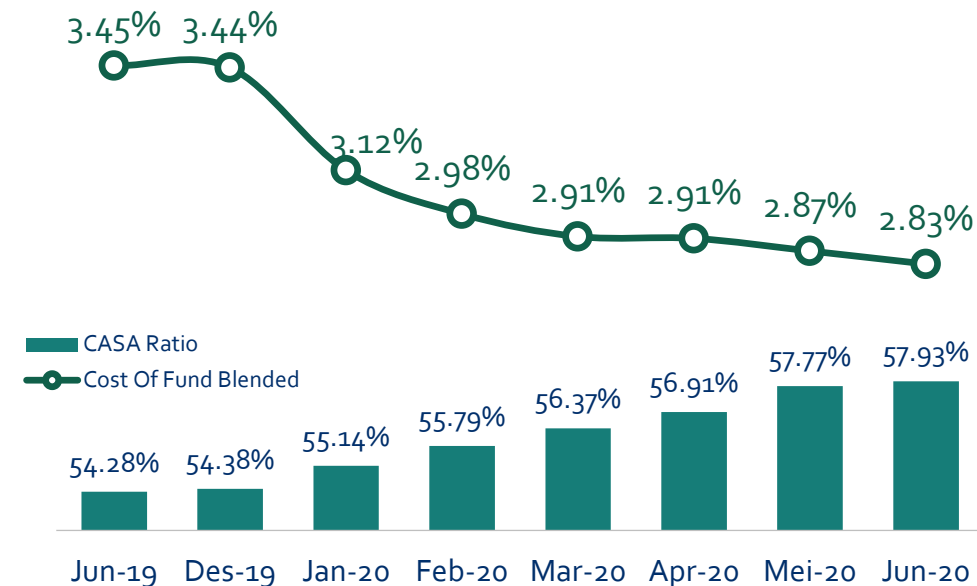


# #6 IN INDONESIAN BANKING INDUSTRY, WITH STRONG CASA RATIO

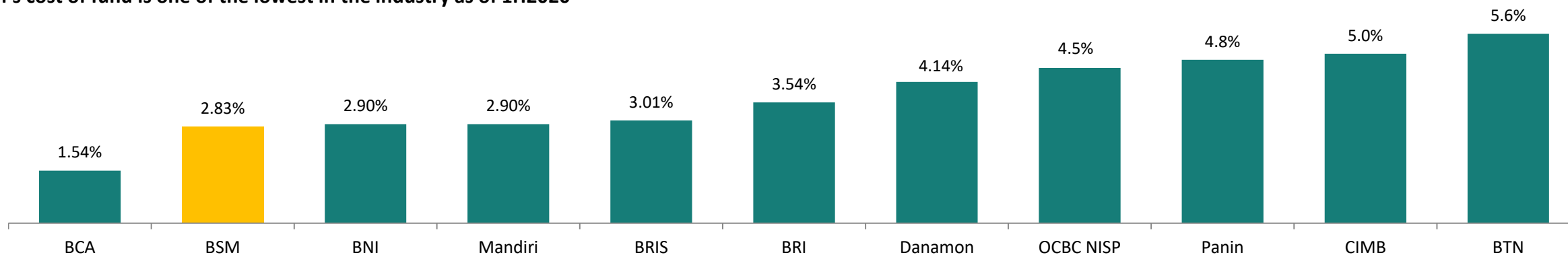
Not only a leader in sharia segment, Mandiri Syariah is also competitively positioned against conventional banks, especially in low cost funding

...with a growing CASA composition resulting to a lower Cost of Funds

Rank 1H2019	Rank 1H2020	Bank	Savings 1H2019 (Rp Bn)	Savings 1H2020 (Rp Bn)
1	1	BRI	365,826	401,092
2	3	BCA	337,195	380,207
3	2	Mandiri	303,196	311,328
4	4	BNI	177,983	187,844
5	5	CIMB Niaga	49,175	56,956
8	↑6	<b>Mandiri Syariah</b>	<b>36,331</b>	<b>42,523</b>
6	7	Panin	38,593	40,663
9	8	Danamon	35,164	38,874
7	↓9	BTN	37,064	34,160
10	10	OCBC NISP	24,259	28,275

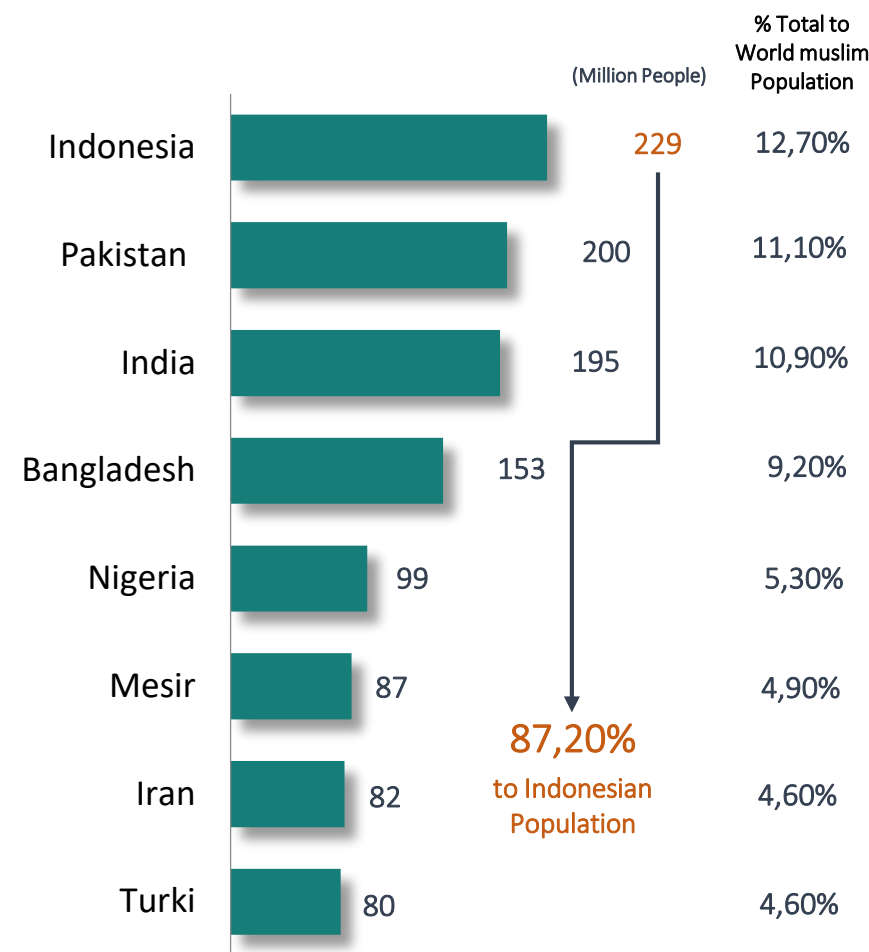


BSM's cost of fund is one of the lowest in the industry as of 1H2020

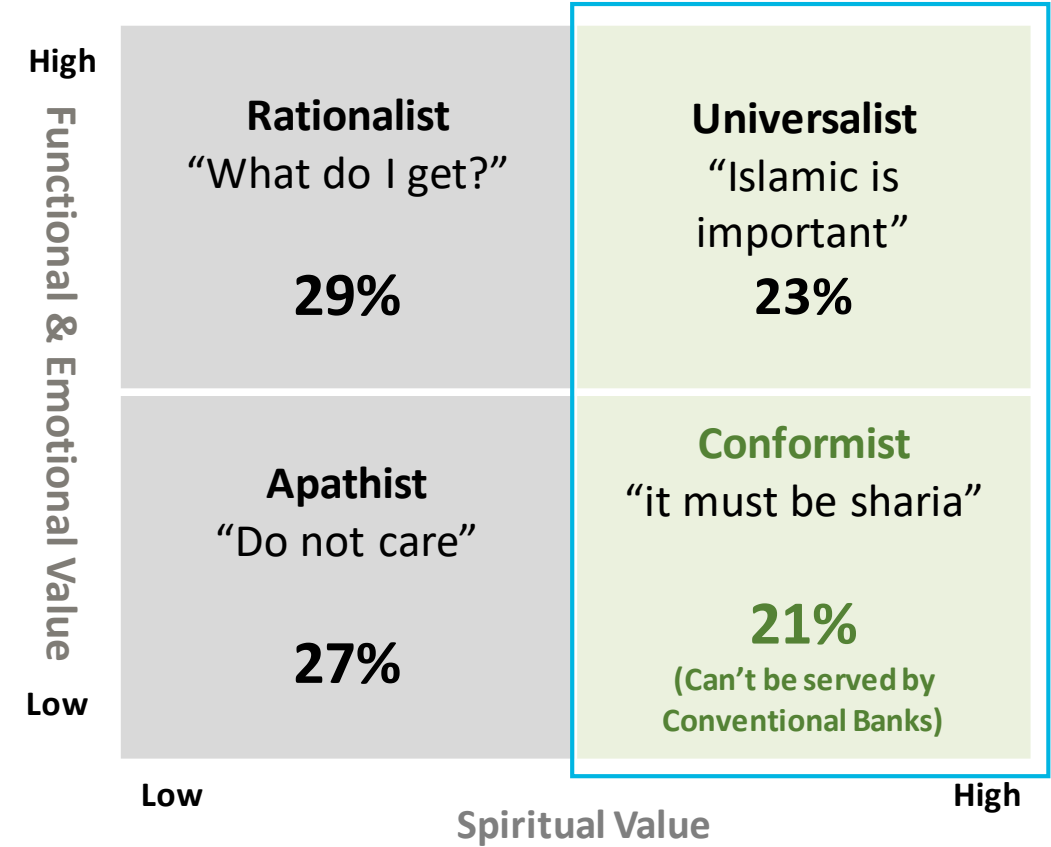


# INDONESIA IS A POTENTIAL MARKET FOR THE DEVELOPMENT OF SHARIA BANKING

Indonesia has the biggest moslem population in the world which contributes 12,7% to the total world moslem populations

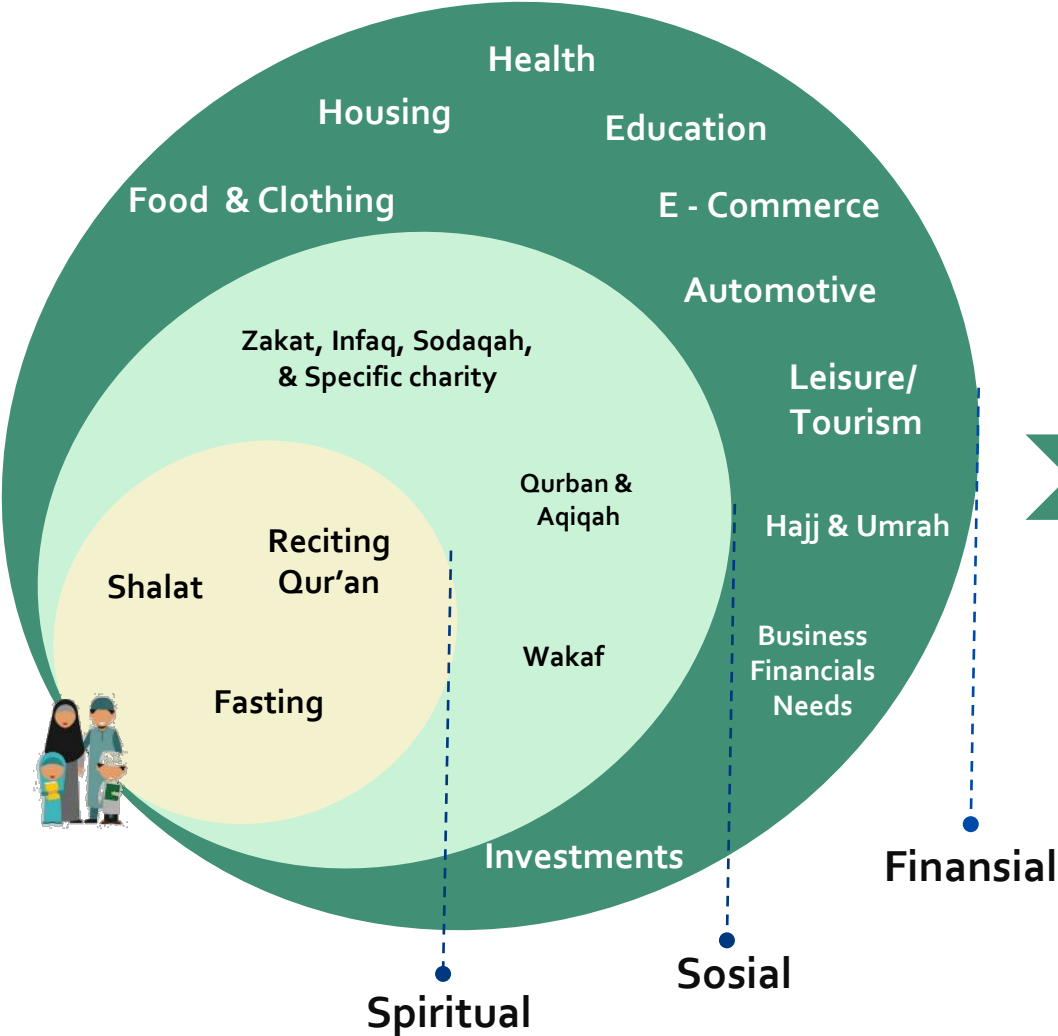


Our strategy starts from understanding the characteristic of moslems in Indonesia who have very diversified preferences

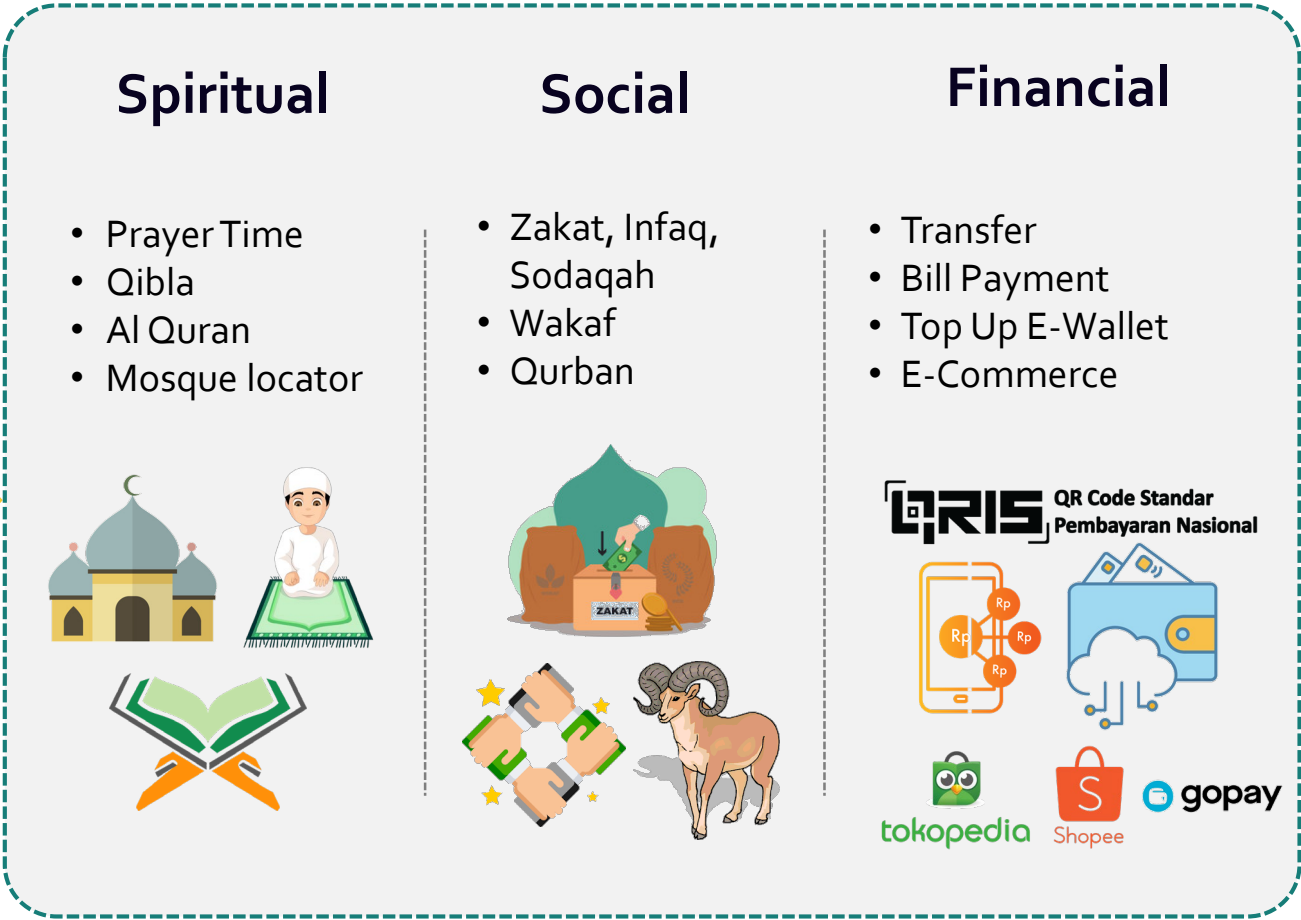


# WE SERVE OUR CUSTOMER NOT ONLY FINANCIAL NEEDS BUT ALSO SOCIAL AND SPIRITUAL

Customer Needs and Activities

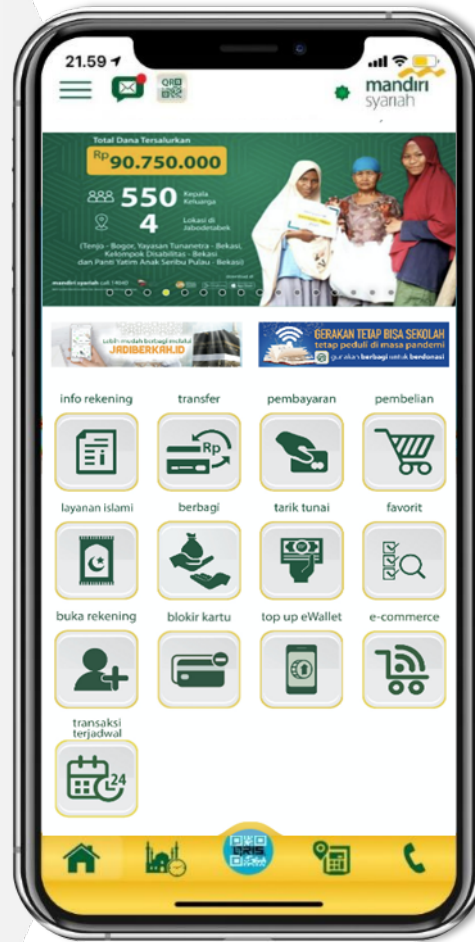
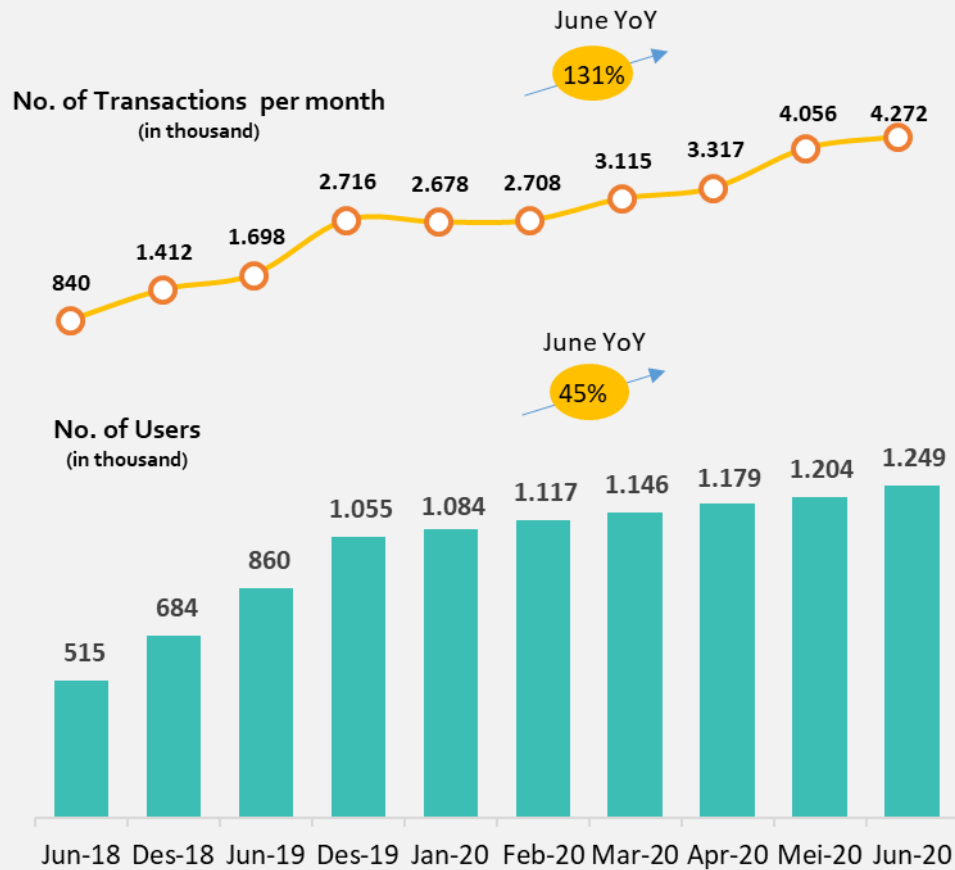


Customer Solution through Mandiri Syariah Mobile



# THE STRATEGY HAS PROVEN RESULT

Number of Mandiri Syariah Mobile Users and transactions has increased significantly



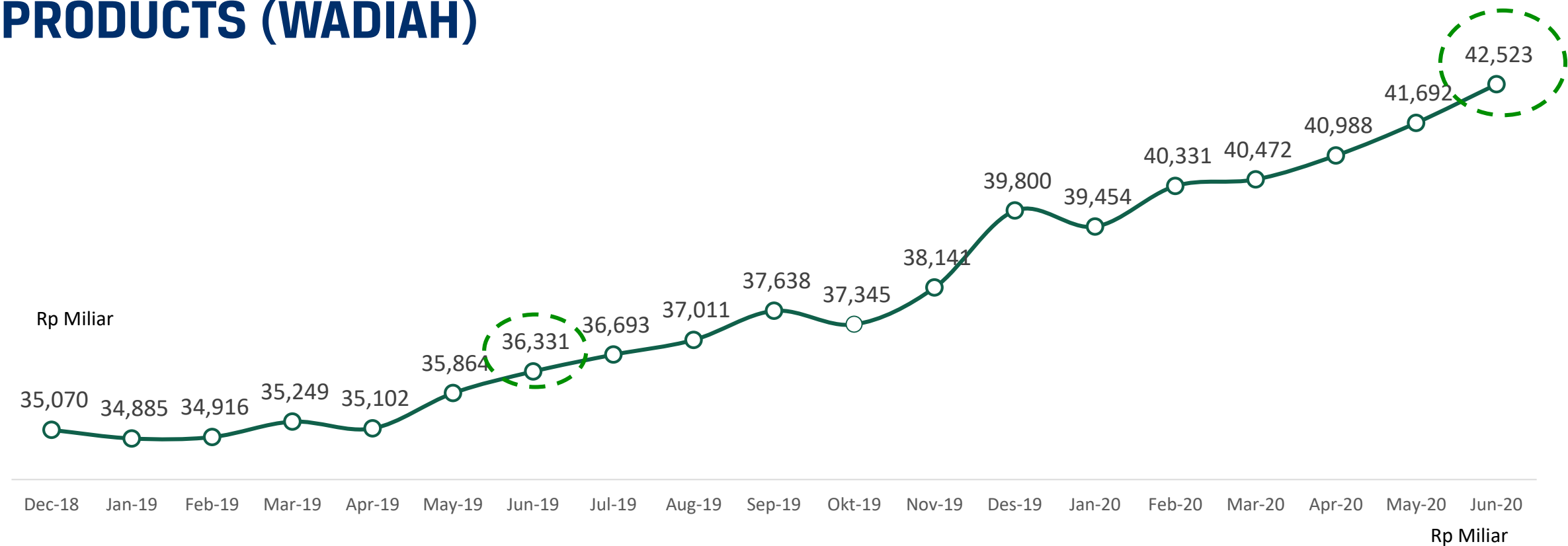
... number of transactions which related to donations has increased also significantly

No. of Transactions (in thousand)	Jun-19	Jun-20	YoY
Interbank Transfer	4,532	7,438	64.1%
Overbooking	2,242	4,256	89.8%
Phone credit	1,266	1,698	34.1%
<b>Zakat, Infaq &amp; Sadaqoh*</b>	879	1,467	67.0%
Payment OVO	93	1,052	1031.0%
Electricity	390	717	83.9%
Top Up Gopay	77	515	567.1%

\* donation for charity in moeslem term

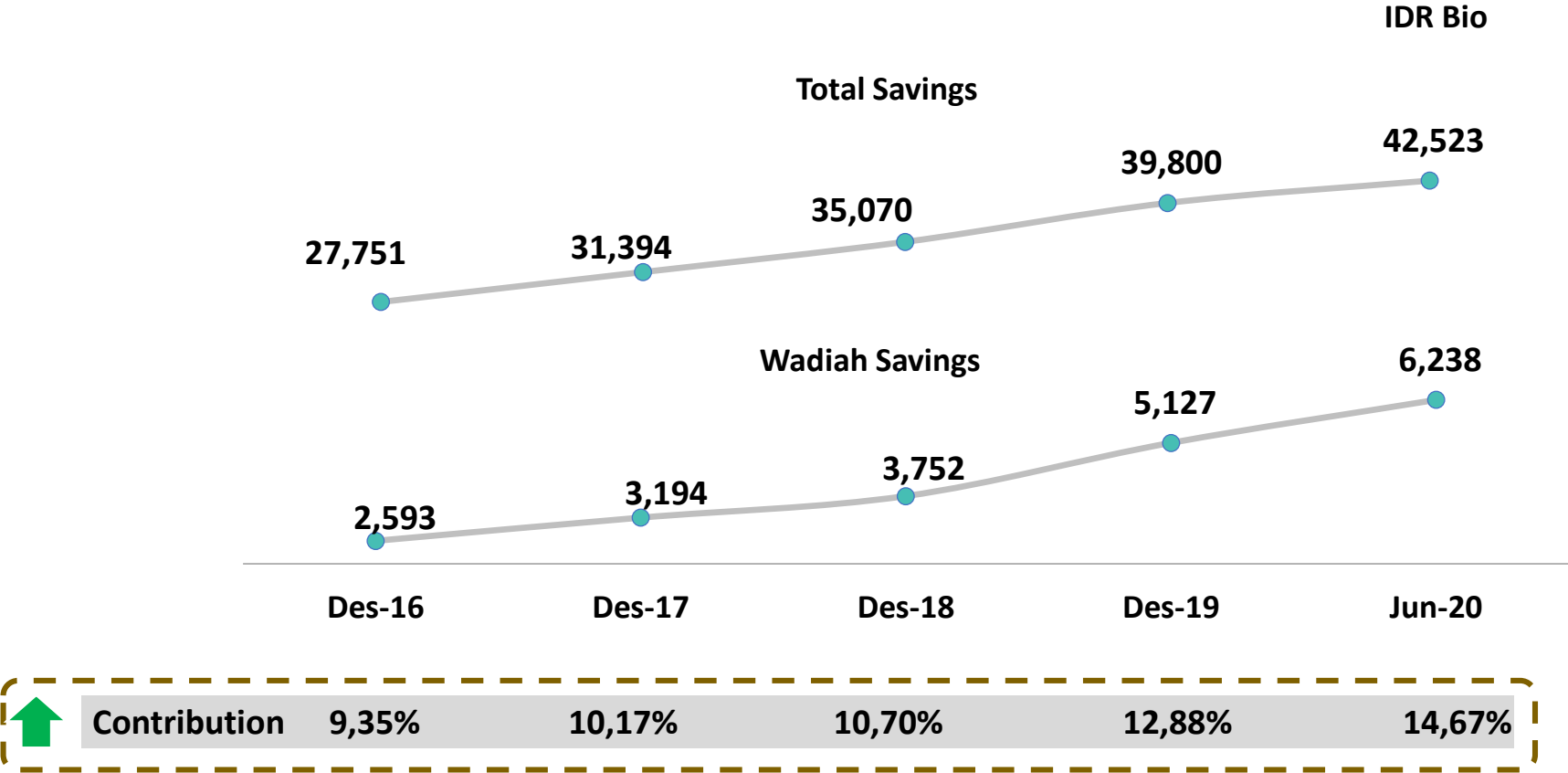


# NUMBER OF SAVING INCREASE, ESPECIALLY FOR SPECIFIC SHARIA PRODUCTS (WADIAH)



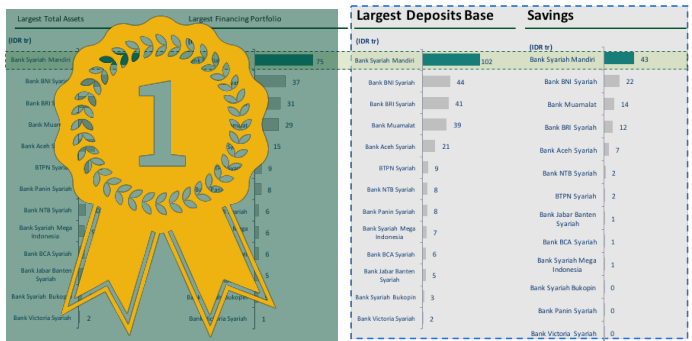
Keterangan	Dec-18	Mar-19	Jun-19	Sep-19	Des-19	Jan-20	Feb-20	Mar-20	Apr-20	May-20	Jun-20	Growth YtD	Growth YoY
Tabungan BSM	23,911	23,948	24,475	24,887	26,530	26,178	26,657	26,796	27,112	27,728	28,207	6.32%	15.25%
Tabungan Mabrur	4,531	4,452	4,481	4,743	4,954	5,038	5,121	4,963	4,869	4,893	4,923	-0.63%	9.87%
Wadiah	3,752	3,858	4,230	4,514	5,127	5,199	5,330	5,499	5,734	6,070	6,238	21.67%	47.47%
Lainnya	2,877	2,991	3,145	3,493	3,189	3,039	3,224	3,214	3,273	3,001	3,155	-1.07%	0.32%
Total	35,070	35,249	36,331	37,638	39,800	39,454	40,331	40,472	40,988	41,692	42,523	6.84%	17.04%

# CONTRIBUTION OF WADIAH TO TOTAL MANDIRI SYARIAH SAVINGS ALSO CONTINUE TO INCREASE

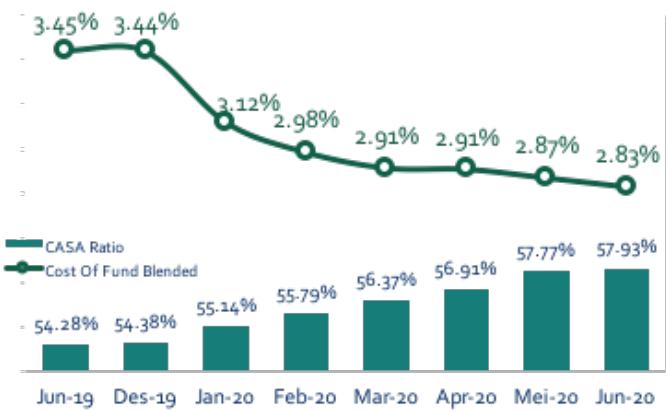


# KEY TAKEAWAYS

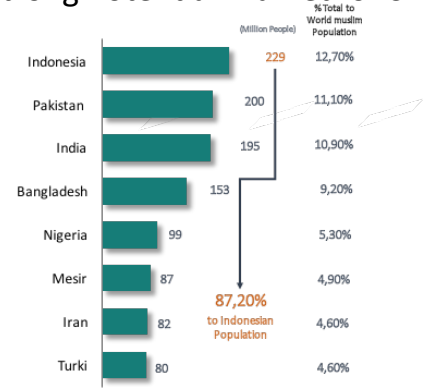
## 1 Largest Sharia Bank In Indonesia Asset, Financing, Deposits



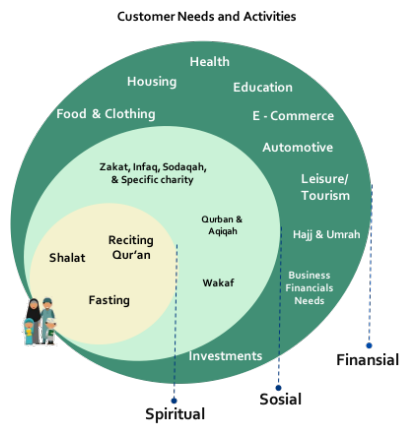
## 2 Growing CASA Ratio Competitive Cost of Funds



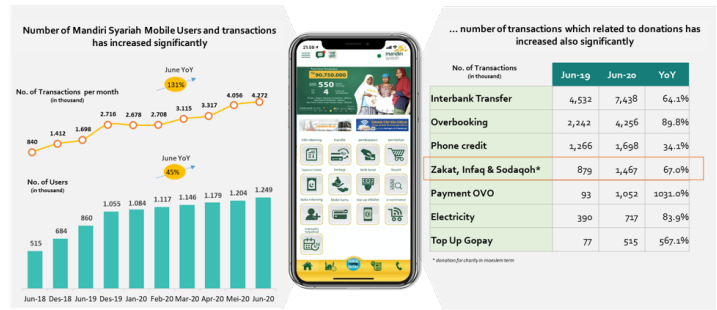
## 3 Indonesia: Largest moslem population in the world Strong Potential Market for Sharia Banking



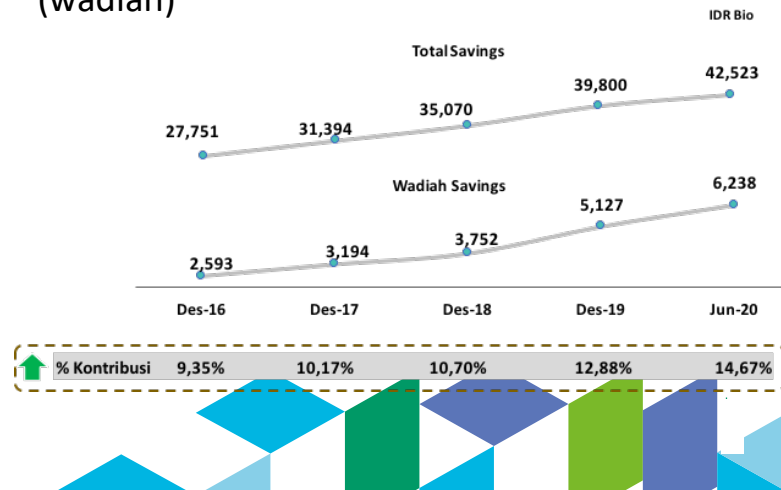
## 4 Customer Solution with sharia value Serve not only for financial needs, but also social and spiritual



## 5 Number of transaction has increase significantly ... especially transactions which related to donations

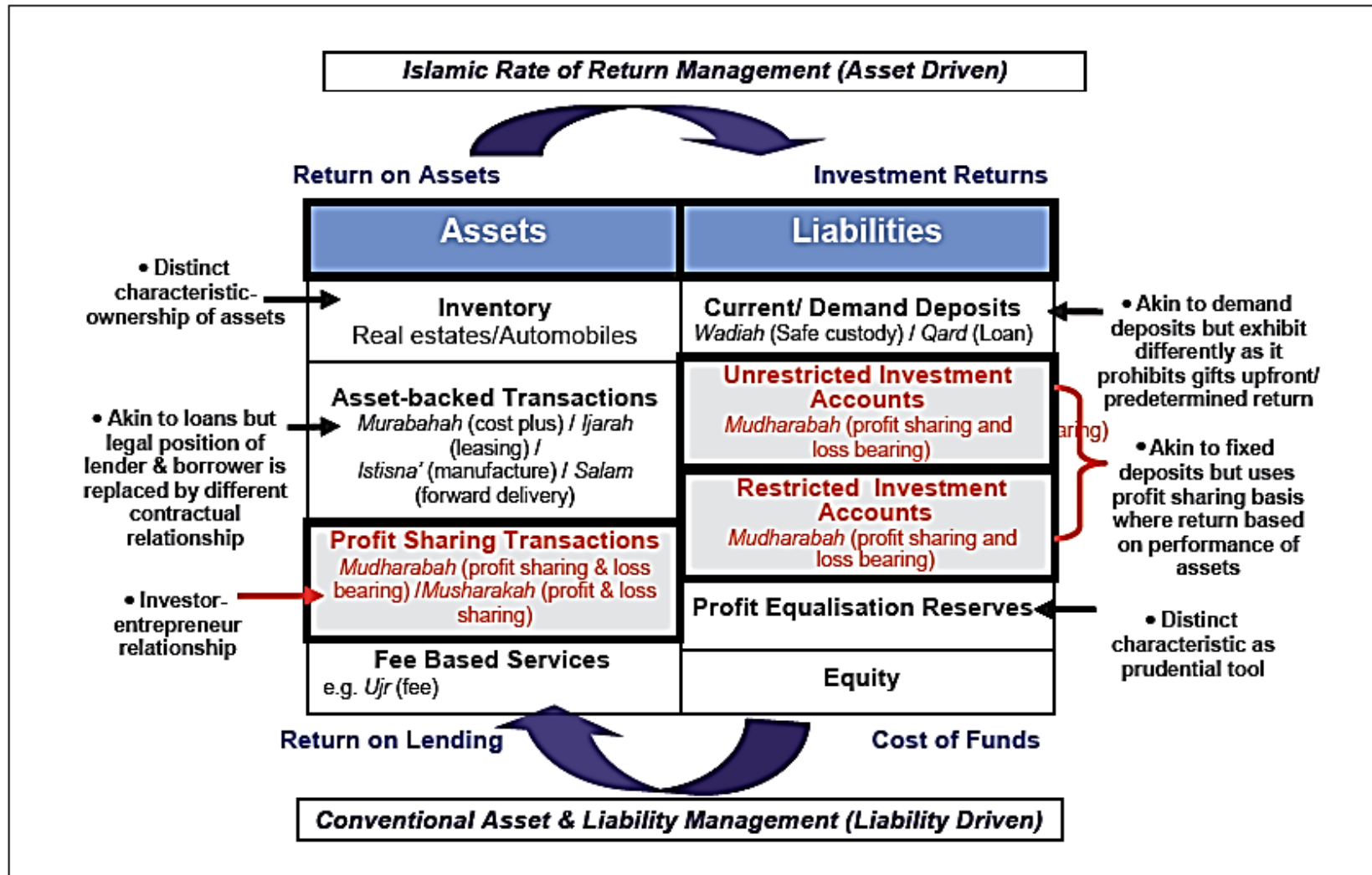


## 6 Number of saving increae ...especially for specific sharia products (wadhah)



% Kontribusi	9,35%	10,17%	10,70%	12,88%	14,67%
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# PART 3: ISLAMIC BANKING MODEL - Introduction



## PART 3: "BINIOG SATHI" – A NEW INVENTION IN ISLAMIC BANKING

- **"Biniog Sathi"** is a new generation banking model that solves the default problem of the banking industry.
- **"Biniog Sathi"** is a Bangla word. It means "Friend in Investment". A true friend can never let the life of his friend to ruin if he goes into trouble. We believe that a true financing institution should stand beside its borrowers in both good and bad times. This is the main essence of this model.



# THE PROBLEM OF CREDIT DEFAULT

- The problem of default is common in all the present banking models, i.e., both Conventional and Islamic
- Although default rate is low for Microfinance Institutions, but it achieves this at the cost of beneficiary's reducing their standard of living
- High risk of default is inducing Banks and MFIs to leave ultra-poor section of the society
- Under present banking system, a true defaulter loses everything to the Bank whenever he defaults on his debt



# FEATURES OF "BINIOG SATHI"

- The model incorporates Zakat and Charity with the present banking model.
- The model is based on Islamic Banking Principles and it makes Islamic banking more competitive
- It offers a solution to the Problem of Credit Default for the clients and the Banks.
- The model unleashes the power of Zakat and Charity



# THE CONCEPT OF ZAKAT

"Zakat" or alms giving is a pillar of Islam. Every Muslim is obligated to pay 2.5% of his wealth every year to eight categories of people, who are:

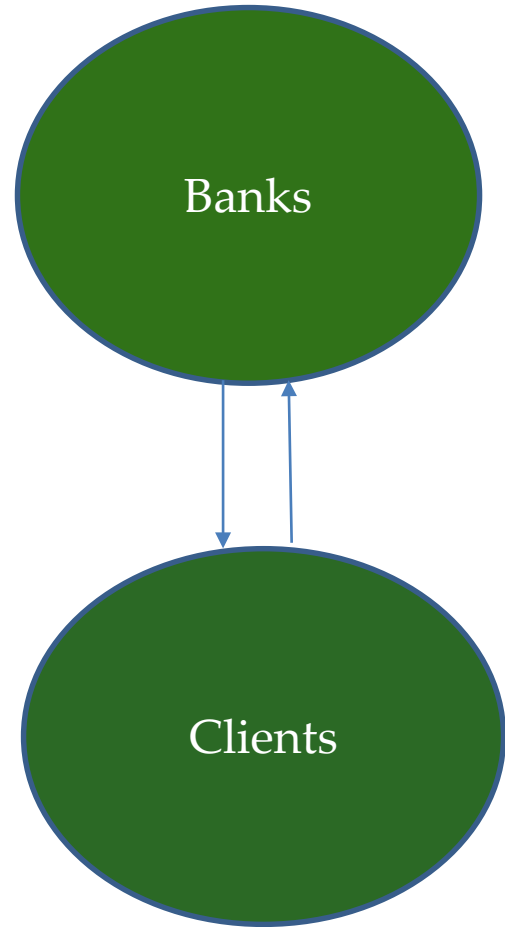
- Poor people
- Needy people
- Zakat Collectors
- Whose hearts are to be won over
- Captives needed to be free
- **Debt Defaulters**
- For the cause of Allah
- Distressed travelers

**Muslims now a days concentrate on poor and needy people only for the utilization of their Zakat. The other six categories of people are largely ignored**





# PRESENT BANKING MODEL



Poor clients are getting finances from Banks and MFIs and repaying them. In case of default, Banks file claims in the court and liquidates the collateral. For Microfinance Institutions (MFIS), they deduct savings of the borrowers to write off the debt

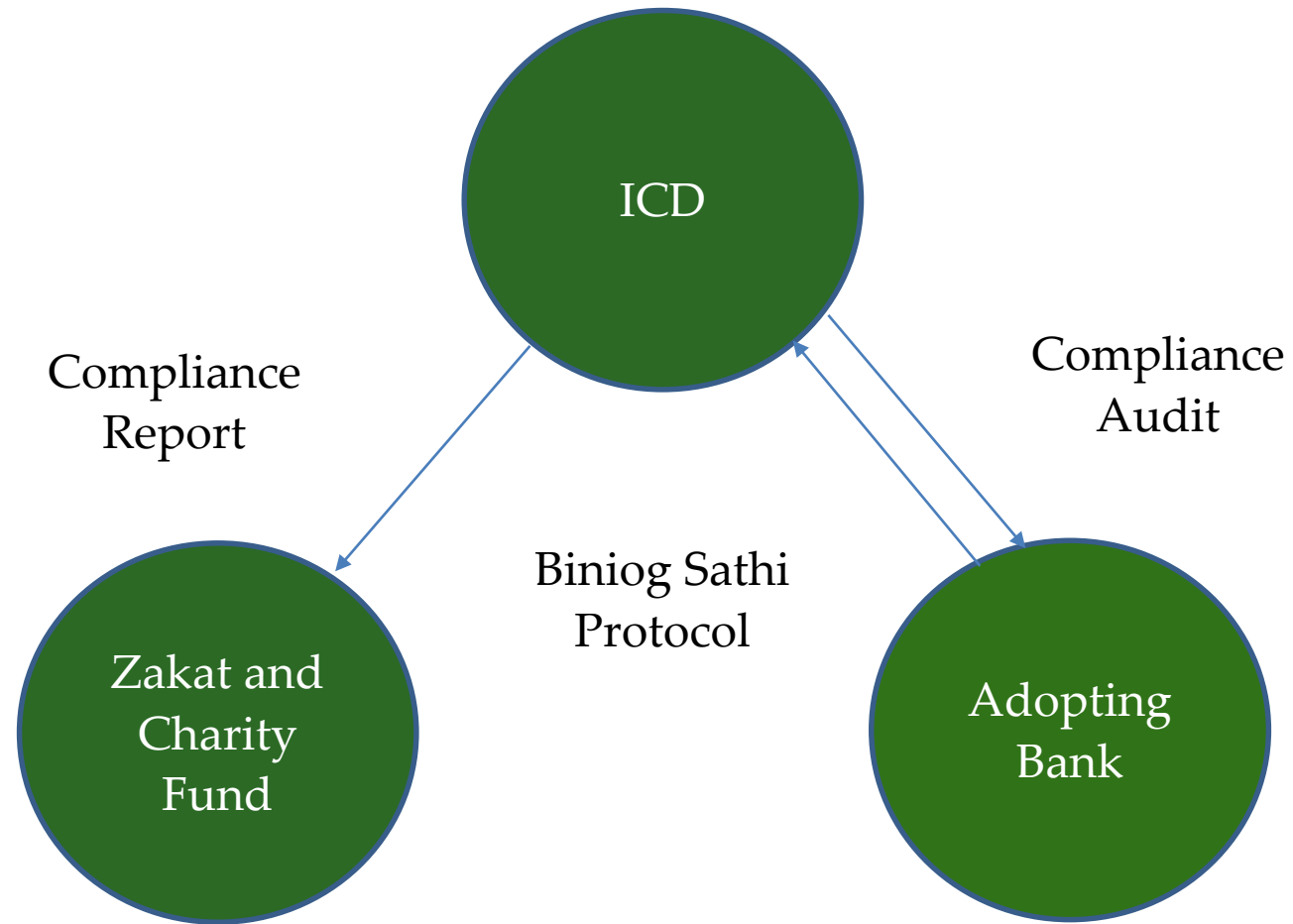


# BINIOG SATHI BANKING MODEL

<https://www.youtube.com/watch?v=DViPoDfZBDU>



# ADDRESSING MORAL HAZARD



# PROGRESS OF THE MODEL

- The model is now an official initiative of ICD. It is under the process of obtaining approval for becoming an official product
- The model received "**Best Innovative Product**" Award at Global Islamic Microfinance Forum in 2017
- ICD has entered into an MOU with AlHuda CIBE of Pakistan to market the model globally
- The model has been featured in Islamic Finance News (IFN) of Malaysia, CNBC Arabia, etc.
- Collaboration efforts are underway to form relationships with various Zakat Funds



# POTENTIALS FOR ZAKAT COLLECTION

- Zakat is much less explored area in the field of Islamic Finance but the potentials are enormous
- Theoretically 2.5% of yearly GDP of a country can be collected as Zakat if efficient marketing and administrative process is followed
- Pakistan, Bangladesh, Indonesia and Malaysia have a combined GDP of 2,064 billion USD. So potential for Zakat collection in these four countries only is **USD 52 billion** a year
- If only 10% of this Zakat (USD 5.2 billion) is distributed to Debt Defaulters on a yearly basis, then the problem of credit default will be greatly reduced and the poor defaulters will be benefited the most



# DEVELOPMENT IMPACT

- This model is a blessing for Islamic Micro Finance Institutions (I-MFIs) and micro clients
- The model will provide incentives to the poor beneficiaries to continue their productive activities without any fear of being in default
- This model will help Islamic MFIs to reach the ultra-poor section, which is a challenge due to increased cost
- The model will help Zakat and Charity Funds to be connected with the real economy
- Due to the positive impact on the poor beneficiaries, Donors will tend to pay more Zakat and Charity. Joint effort between I-MFIs and Zakat and Charity Funds will accelerate poverty reduction





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## Q & A SESSION



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**THANK YOU**

