

## GLOBAL ISLAMIC FUND INDUSTRY GROWTH DESPITE CHALLENGING AND VOLATILE MARKET

Despite a challenging global macroeconomic environment and volatile performances in the world financial market, the Islamic funds industry has demonstrated impressive growth and a four-fold increase in the number of funds available. This growth has been supported by the surge in availability of Shariah-compliant capital market instruments including listed equities, fixed-income instruments, money market instruments and other structured investment products. Further opportunities are expected to come from untapped markets in Asia-Pacific and North-America.

**23 December 2013**

## Global Islamic funds industry – Achieving growth under challenging times

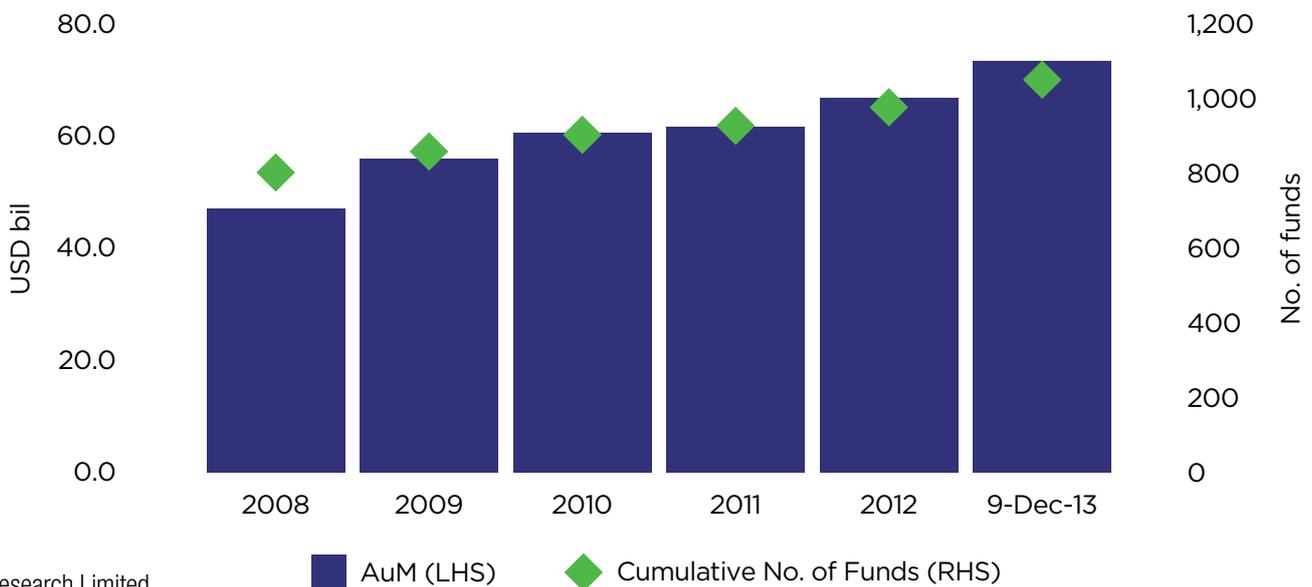
The global assets under management (AuM) for Islamic funds are estimated to have reached USD73.7bn<sup>1</sup> as at 9th December 2013 at a CAGR of 9.41% during the past five years and the number of funds has grown four folds, demonstrating the vast potential of the Islamic wealth management industry.

The global Islamic funds industry has progressed tremendously having grown from a USD29.2bn AuM market in 2004 to an almost USD73.7bn market as at 9th December 2013. The number of funds in the industry has also grown four-folds from approximately 285 funds in 2004 to an estimated 1053 funds in the same time period. Despite the challenging global macroeconomic environment and volatile performances in the world financial markets, the Islamic funds

industry has managed to post an impressive 2013 YTD growth of 10.2% in AuM, having witnessed the introduction of more than 78 new Shariah-compliant funds in this period ending 9th December. The growth in the Islamic funds sector has been supported by the surge in availability of Shariah-compliant capital market instruments including listed equities, fixed-income instruments, money market instruments and other structured investment products which essentially provide fund managers a wide range of Shariah-compliant financial instruments for fund portfolio management. Moreover, there are now four major global Islamic indices providers, namely Dow Jones Islamic Indices, S&P Shariah Indices, FTSE Islamic Indices and MSCI Islamic Indices, which track a global universe of Shariah-compliant stocks in various financial markets, thus providing fund managers with options to vary their fund offerings according to geographical focus.

### Islamic Funds Industry – Assets under Management (AuM) and Number of Funds

Source: Bloomberg, Eurekahedge, KFH Research Limited



<sup>1</sup> KFH Research Limited

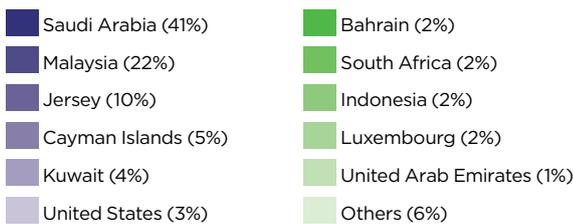
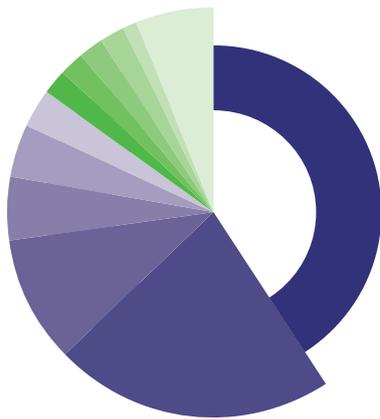
**GLOBAL ISLAMIC FUND**  
**INDUSTRY GROWTH DESPITE CHALLENGING**  
**AND VOLATILE MARKET**

In terms of assets by domicile, Malaysia and Saudi Arabia represent the two largest Islamic funds markets having combined total Islamic funds AuM of USD46.5bn or 63.1% of the total industry AuM as at 9 December 2013. In terms of number of funds by domicile, once again Malaysia and Saudi Arabia lead the market with nearly 48% of the total number of Islamic funds domiciled in these two countries. The leading position of Malaysia as an Islamic funds domicile can be attributed to the availability of a wide range of Islamic capital market instruments and ready pool

of various institutional and retail investors investing in Shariah compliant financial products. Moreover, Malaysia’s well-developed regulatory framework and accommodative policies which encourage the growth and development of Islamic capital market, make it an attractive market to originate Islamic funds from the country. Similarly, in the case of Saudi Arabia, the availability of a ready pool of Islamic investors and high net-worth individuals (HNWIs) factor in as reasons for the jurisdiction to be a preferred domicile for Islamic funds.

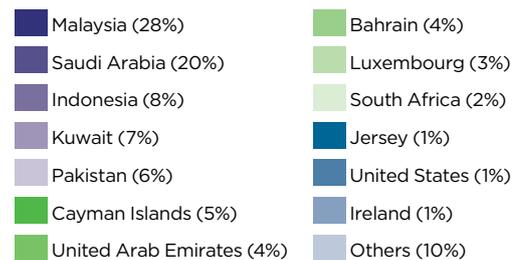
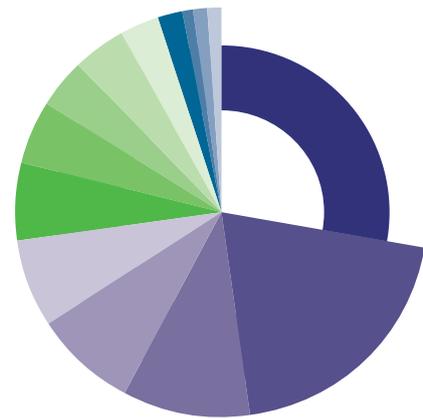
**Islamic Funds Assets – by Domicile**  
**(9th December 2013)**

Source: Bloomberg, Eurekahedge, KFH Research Limited



**Number of Islamic Funds – by Domicile**  
**(9th December 2013)**

Source: Bloomberg, Eurekahedge, KFH Research Limited



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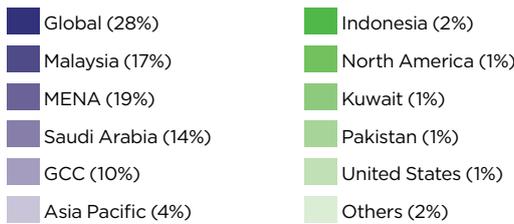
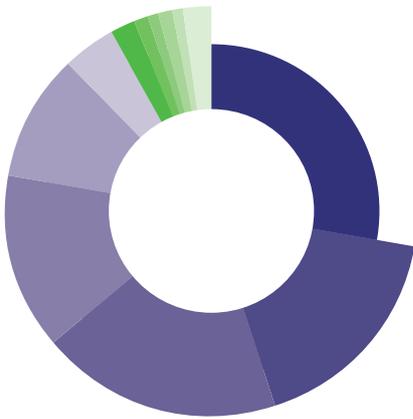
As at 9th December 2013, funds with a global geographical focus remain the most popular as 28% of total Islamic AuM were invested under a global mandate with global geo-focus strategy to achieve diversification of risks by investing in various financial markets. Malaysia and Saudi Arabia represent the two key individual country focus markets which attract the most AuM of Islamic funds (17% and 14% respectively as at 9th December) given the large market capitalisation of Shariah-compliant equities in

these markets. Furthermore, bulk of the Islamic funds raised locally in these two jurisdictions are channelled into the domestic Islamic capital markets, thus raising their profile as focus countries for funds.

By asset class, equities constitute 34% of the total AuM of Islamic funds as at 9th December, followed by money market instruments (19%) and then commodities (15%) as the second and third largest Islamic funds assets by asset class.

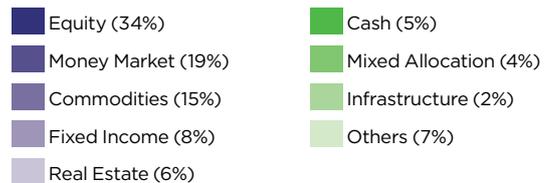
**Islamic Funds Assets – by Geographical focus (9th December 2013)**

Source: Bloomberg, Eurekahedge, KFH Research Limited



**Islamic Funds Assets – by Asset Class (9th December 2013)**

Source: Bloomberg, Eurekahedge, KFH Research Limited



The concentration of Islamic funds in Malaysia and Saudi was attributed by the large size of funds domiciled in the two countries. Among the top 20 Islamic funds by asset size, Malaysian and Saudi Arabian domiciled-funds dominate the list with 8 and 10 funds respectively along with one fund each from the United States and Kuwait. Half of these funds have investment focus on equity, followed by five money market funds and three having commodities as their asset focus.

In terms of returns on Islamic funds, Top 10 best total equity funds returns in 2013 are domiciled in United Arab Emirates, Pakistan, Malaysia and Saudi Arabia, with more than 45% in total YTD returns as at 9th December 2013. In comparison, the mixed allocation funds, yielded average total YTD returns of 32% across the

Top 10 best total mixed allocation fund returns as at 9th December 2013. The top 10 best performing mixed allocation funds in terms of returns are domiciled in Pakistan, Saudi Arabia, Kuwait, Malaysia and the United Arab Emirates.

As for money market and fixed-income funds, funds domiciled in Pakistan and Indonesia generally yielded higher returns given the higher Islamic interbank profit rates and Sukuk return rates in these countries. The total YTD returns among the Top 10 money market funds averaged 6.2% while among the Top 10 fixed-income funds averaged 10.1% as at 9th December 2013. The returns on commodity funds however remained stagnant given the declining commodity prices in the global markets as the world macroeconomic conditions remain challenging.

### Top 20 Islamic Funds by Asset size as at 9th December 2013

Name	Domicile	AuM Size (USD mil)	YTD Returns (%)	Fund Asset Class
Al-Ahli Saudi Riyal Trade Fund	Saudi Arabia	3,994.94	0.64	Money Market
Al-Rajhi Commodity Fund	Saudi Arabia	2,668.77	1.13	Commodity
Samba SAR Intl Trading Fund	Saudi Arabia	2,324.60	0.97	Money Market
Al-Ahli Divers SAR Trade	Saudi Arabia	1,939.33	0.64	Money Market
Amana Income Fund	United States	1,592.19	27.42	Equity
Public Islamic Dividend Fund	Malaysia	1,289.44	8.41	Equity
CIMB Islamic Dali Equity Growth Fund	Malaysia	1,204.42	18.6	Equity
Hwang Aiman Cash Fund	Malaysia	1,172.04	2.72	Money Market
HSBC Saudi Companies Equity Fund	Saudi Arabia	879.74	34.72	Equity
Public Islamic Select Enterprises Fund	Malaysia	775.49	9.22	Equity
Samba Al Raed Saud Equity Fund	Saudi Arabia	669.06	28.37	Equity
Public Islamic Equity Fund	Malaysia	658.33	9.51	Equity
Riyad Commodity Trading SAR Fund	Saudi Arabia	579.97	0.93	Commodity
ARNB SAR Trade Fund	Saudi Arabia	473.93	1.04	Fixed Income
ANBI Al Mubarak SAR Trade Fund	Saudi Arabia	473.93	N.A.	Fixed Income
Amanah SAR Trading Fund	Saudi Arabia	446.29	0.67	Commodity
PB Islamic Cash Plus Fund	Malaysia	430.46	2.67	Money Market
Al Wataniya Fund	Kuwait	428.85	8.01	Equity
Public Islamic Optimal Growth Fund	Malaysia	426.19	11.13	Equity
Public Islamic Select Treasures Fund	Malaysia	415.31	18.02	Equity

Source: Bloomberg, KFH Research Limited

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## Malaysia's Islamic Funds and Asset Management Industry

Malaysia's Islamic capital market is one of the most dynamic markets globally and the industry has led many product innovations in the global Islamic capital markets. Malaysia leads the global sukuk sector in terms of number of issuances and sukuk outstanding since the inception of the sector in the year 2000. In terms of funds and asset management, the domicile has nearly two decades of experience in Islamic funds having established two Islamic unit trust funds way back in 1993. Since then, the country has been driving the Islamic asset management industry's innovation with milestones among others the launching the world's first Islamic Real Estate and Investment Trust (REIT) in 2006 and the Asia's first Islamic Exchange Traded Fund (ETF) in 2008. Malaysia is now the second largest Islamic funds market by domicile (largest number of funds globally) and is centrally located in the ASEAN region which is home to a population of more than 570mln. As at 31st October 2013, Malaysia has 175 active Islamic funds with a net asset value (NAV) of RM40.7bln while there are a total of 39 asset management companies which offer Islamic and conventional unit trust funds.

Gradual financial liberalisation undertaken by the Malaysian government has attracted a number of market players to establish their operations in the country's Islamic financial market place. In terms of flexibility of funds operation, Malaysia allows Islamic fund management companies to offer funds in both local and foreign currencies while further allowing fund managers to invest 100% of the capital abroad. In addition, the foreign exchange administration rules of Malaysia now allow free mobility of inward and outward movement of funds. Dynamic Islamic capital market with ready pool of Islamic financial players provide abundant opportunities for various Islamic financial institutions, including the Islamic asset management industry, to participate in the growth of Malaysia's Islamic finance sector.

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## Outlook and Challenges

The global Islamic funds industry has managed to achieve growth despite the challenging economic conditions. Moving forward, the Islamic funds sector is expected to continue this growth. As more jurisdictions introduce Shariah-compliant indices in their capital markets, for example United Kingdom's recent announcement of listing a Shariah-compliant index on the London Stock Exchange, the Islamic fund managers have wider stock universe to choose from for their portfolios management. The phenomenal growth rates in

world sukuk issuances further provide avenues for Islamic fixed-income and mixed-allocation funds to blossom. Similarly, growing efforts to introduce short-term Shariah-compliant instruments for liquidity management of Islamic financial institutions will allow more funds be directed to Islamic money market type of funds. These developments will further spur growth of the Islamic funds industry which eventually will appeal more asset managers to tap into the market.

From the demand side, the rise in the number of HNWI (having investable assets over USD1mIn) in key Islamic finance markets represents further potential for the Islamic funds industry to expand its market base. Based on 2012 statistics, 6.8% of global HNWI were located in Middle East and Africa, with

“From the demand side, the rise in the number of HNWI in key Islamic finance markets”

GCC having the majority share in the cluster. Meanwhile, Asia-Pacific, which has witnessed growing interest in Islamic financial services among its various jurisdictions, is home to 30.4% HNWI as at 2012, overtaking North America and other regions to become home to the most number of HNWI. As a result, the Islamic funds industry has vast opportunities to profile the HNWI in such regions in order to offer them Islamic wealth management products based on their investment objectives and risk appetites.

Nonetheless, challenges remain in the sector's growth and development as volatile global economic performances have caused smaller-scale Islamic fund managers to restructure and at times, exit the industry in the light of competition from larger-scaled and more developed conventional fund managers. Under such circumstances, opportunities for Islamic fund managers exist in the form of attracting investments from institutional investors that can help shore up the AuM of Islamic funds, which may lead to achieve efficiency benefits through scale for the fund managers. Further opportunities for fund managers exist in the form of penetrating into untapped markets in the rising Asia-Pacific and developed North-America, targeting high-net-worth individuals in such markets. In conclusion, the Islamic funds sector needs are expected to grow beyond its traditional strongholds of GCC and Malaysia and will attract more conventional fund managers to tap into this thriving Islamic funds industry.

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