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### THE RACE TO BECOME THE HUB OF ISLAMIC FINANCE

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#### **ABSTRACT**

This study investigates which of London, Dubai or Kuala Lumpur is the most qualified city to become the hub of Islamic finance. Qualitative method is the methodology that going to be used in this research in order to investigate the result. Also, SWOT analysis is a useful technique to compare the Strengths, Weaknesses, Opportunities, and Threats between these three cities. The outcome of the research has shown that Kuala Lumpur is the most qualified city to become the hub of Islamic finance. It shows more strength points than London and Dubai. Also, it shows less weakness points than the other two cities. In the other hands, Dubai shows more strength, opportunity and less weakness than London. Also from the interview analysis, the experts emphasized that Kuala Lumpur is the strongest in Islamic finance. The competition between London, Dubai and Kuala Lumpur stressed that Islamic finance system become more and more strong. People have started to understand the important of this financial system and how it can improve their economic positions.

#### **INTRODUCTION**

Islamic finance is an activity that consistent with the principles of sharia and its practical application through the development of Islamic economics [1, 2]. The difference between Islamic and capitalist finance is that in capitalist finance; business decisions for making and raising profits are made without principles or rules. This kind of finance lead to some issues in society such as interest rate, gambling, and producing immoral or harmful products just to control the market under any condition. Islamic finance prohibits the fixed or floating payment or acceptance of specific interest or fees for loans of money. Also, investing in businesses that provide goods or services considered contrary to Islamic principles is prohibited. On the other hand, Islamic finance

has balanced between the business and human rights with sharia principles and rules in order to protect all stakeholders that are included in the business [3]. Now days, Islamic finance is growing 50 per cent faster than the traditional banking sector, and it has huge growth potential [4]. Islamic Finance has become a significant global force in directing transactions of financial activities with sharia principles and its tools have become one of the most important tools in the global financial system. After the global recognized of the importance of Islamic finance, London, Dubai and Kuala Lumpur are in three ways fighting for becoming the hub of Islamic finance [5, 6].

London has long been the default center for international firms to issue sharia-compliant bonds. However, few years ago, everything changed. In year 2013, the World Islamic Economic Forum was in London. There were more than 1,000 investors from more than 100 countries and 15 global leaders are gathering for the ninth world Islamic Economic Forum and Britain is honoured to play host [7]. London already is a major home of Islamic finance outside the Islamic world. Britain has more sharia-compliant banks than any other western European country. In March 2013, Britain launched a publicity campaign involving government junior ministers and private sector executives to burnish London's Islamic credentials [8]. The City of London is the home to fast-growing new markets. However, it faces a mounting challenge from two canters: Dubai and Kuala Lumpur.

Dubai, at the heart of the wealthy Gulf, announced a push into Islamic finance year 2013. It has an entrepreneurial culture which has already made it the Middle East's top conventional banking center and big state-run firms which can be expected to support the government's strategy. Dubai laid claim to Islamic business in January 2013 when its ruler, Sheikh Mohammed bin Rashid al-Maktoum, announced a drive to develop the emirate as an Islamic financial center [5].

In addition, the Malaysian capital has a great reputation for efficient regulation of Islamic finance and a huge domestic market for local-currency Islamic bonds, which is starting to attract foreign issuers [5]. In May and June 2013, Malaysia took steps to strengthen its regulation of the industry while making it easier for its Islamic insurers to invest their money overseas. The final result of the three cities' rivalry may not be known for years, but thousands of jobs and large amounts of direct investment in companies and real estate are likely to depend on the outcome. Therefore, this research going to investigate with of London, Dubai or Kuala Lumpur is the most qualified city to become the hub of Islamic finance.

## **METHODOLOGY**

This study used qualitative method. The research is concerned in doing an analysis of social trends, or policy implications. However, it also introduces a 'human touch' by conducting interviews with experts in Islamic finance, in order to know expert's opinion about the topic. The fieldwork was conducted between 2006- 2014, which supported from many resources that have related information to the cultural, educational, geographical, financial situations and governmental rules for London, Dubai and Kuala Lumpur.

### ***Data Collection***

The research material collected its resource from primary and secondary data. The primary data refers to data being collected or obtained from a first-hand experience such as the interview. While secondary data refers to data gathered in the past or obtained from other party such as journals, web sites, videos and newspaper.

### ***SWOT Analysis***

This study conducted the SWOT analysis, which is useful technique for understanding the tree cities Strengths and Weaknesses, and for identifying both the Opportunities open to them and the Threats they face. SWOT analysis is a framework for identifying and analysing the internal and external factors that can have an impact on the viability of a project, product, place or person. SWOT analysis determines what may assist London, Dubai and Kuala Lumpur in accomplishing their objectives, and what obstacles must be overcome or minimized to achieve desired results.

## **RESULT AND DISCUSSION**

### ***SWOT Analysis For LONDON***

#### ***Strenght***

UK is the 6<sup>th</sup> largest economy by nominal GDP. The Britain launched a publicity campaign involving government junior ministers and private sector executives to burnish London's Islamic credentials. UK is the European Islamic finance center. More than 20 international banks operating in the UK are working in Islamic finance, 6 of which are fully Sharia compliant. The London Stock Exchange has raised a total of US\$34 billion through 49 issues of Sukuk. London's sheer size gives it an advantage in Takaful. UK has a very good and long experience in banking system. The UK is a global leading provider of sector specific education and research with world class academic institutions offering a range of specialist courses and qualifications in Islamic finance. Strong universities offer Islamic finance courses for PHD and other levels, such as university of east London, Cambridge, university of Durham and university of Salford Manchester.

#### ***Weakness***

London is not located within a natural pool of Sukuk issuers. European customers will remain a limited group. There are conventional staff works in Islamic banks. There is shortage of skilled Islamic finance professionals and Sharia scholars. Islamic banks and their clients are not treated any differently to their conventional counterparties. For example: they don't remove double tax on Islamic mortgages. Islamic banking assets only marks at \$19 billion.

### *Opportunity*

London has led in attracting issues by big international companies because of its massive experience in financial markets. London has globally respected legal system. Britain is becoming the hub of Sukuk in western countries. The UK tax authorities have been working for some time with the Islamic finance. The tax treatment of Sharia compliant securitization has been put on the same footing as traditional securitizations. The presence of a Sharia compliant securitization is a real possibility in London. The Muslim population in Europe is growing. New standards and qualifications in Islamic finance are being offered by professional institutes, universities and business schools across the UK. GCC oil rich countries make their investment in Europe and US, so if UK offers Sharia compliant investment; it will attract them more than any other western countries.

### *Threats*

Sukuk is the highest profile and the most sensitive area of competition between the three centers is arranging Sukuk. The small number of Muslims citizen in the UK could lead to delay the progress of Islamic finance. There are some political reasons such as, right wing parties BNP against Sharia and Islamic finance.

## **SWOT ANALYSIS FOR KUALA LUMPUR**

### *Strenght*

The Malaysian capital has a great reputation for efficient regulation of Islamic finance and a huge domestic market for local-currency Islamic bonds. K.L. is now starting to attract foreign Sukuk issuers. The government took steps to support its regulation of the industry while making it easier for its Islamic insurance companies to reinsure overseas. About 60% of populations in Malaysia are Muslims. Kuala Lumpur has accounted for about two-thirds of all Sukuk issued globally in year 2013. Kuala Lumpur benefits from its location in a vast, predominantly Muslim area of Southeast Asia help in huge increase in Takaful. Malaysia is centered between Indonesia, Singapore and Thailand those are countries have good number of Muslim populations. Malaysia has been influential because of its centralized model of regulation, which minimizes disputes among different boards of Islamic scholars. The Islamic banking assets are about \$135 billion. There are 50 institutions offering industry courses and 18 universities offering degrees in Islamic finance.

### *Weakness*

It is holding the 35 position by nominal GDP. Malaysia is more focusing in domestic market rather than international market.

### *Opportunity*

Malaysia has the advantage of a vibrant market in local-currency Sukuk. The convergence of expertise is becoming all the more critical as Islamic finance grows in size and gains popularity in certain jurisdictions.

### *Threats*

Some Gulf scholars view Malaysian regulation as too liberal, arguing that it permits structures which too closely mimic conventional finance. Sukuk is the most competing issues between the three cities. Economically, KL and the surrounding regions are not strong as counterparts.

## **SWOT ANALYSIS FOR DUBAI**

### *Strength*

Dubai situated at the heart of the wealthy Gulf countries. The government announced a push into Islamic finance in 2013. Dubai has an entrepreneurial culture which has already made it the Middle East's top conventional banking center. Dubai is a big state-run firm which can be expected to support the government's strategy. Dubai Islamic Bank has been named as the Best Islamic Bank in the region. DIB has been proactive in creating partnerships and alliances at both the local and international level. DIB has strong financial stability and strong capitalization. Islam is the main religion in Dubai. And it's ruled by completely Muslim government. UAE has numbers of qualified universities offer Islamic finance and banking courses, such as Hamdan Bin Muhammad University, Canadian university, UAE University.

### *Weakness*

Progress in Islamic finance has been slow and it will take a few years to reach the level of Malaysia. There is need for human capital with high experience in Islamic finance field. The last economic depression has hit Dubai extremely hard, due to its dependence on tourism and building but not on strong financial system.

### *Opportunity*

Dubai holds the 30 position by nominal GDP. Dubai's government is now convincing its companies to issue at home, and could attract business from firms in neighboring Gulf States. The ruler of Dubai Shekh Mohamad bin Rashed plan to make Dubai the capital of Islamic economy. Takaful firms were forced to transfer some of their risk to conventional re-insurers. That creates a window for Dubai to set up Islamic re-insurers. Dubai will issue Sukuk standards that are more detailed and comprehensive than others, hopefully resolving conflicts between the regions. Dubai is becoming the hub of International Corporation, so, their seeking for more financial funding are

increases. Islamic banking assets are about \$75 billion in retail banking assets across United Arab Emirates.

### ***Threats***

Sukuk is the most critical issue between the three cities. Dubai lists relatively few Sukuk on its exchanges; traditionally its state-owned companies have gone to London to issue. Intense competition among Islamic and conventional banks may keep profit margins at minimum. The regulatory changes concerning to the global financial crisis are going to be stricter.

### **INTERVIEW ANALYSIS AND EXPERTS' EXPECTATION**

The interview was conducted with some professors and experts in Islamic finance and high position people in the market.

#### ***What Progress Step Can Malaysia Take In Order To Be The Hub Of Islamic Finance?***

The first respondent said that Malaysia already has reached high certain situation in Islamic finance. The most important thing is the amount of Islamic finance they offer. More people do transaction, insurance and intermediaries because of their seeking of funds. In order to be the hub, Malaysian's government has to make the transaction easy for the international people. Also, they should make the priority in providing the facilities for easy transaction.

The second respondent claims the analysis about the progress step can Malaysia shown to become the hub was that Malaysia has done enough. Even if it doesn't do more it stills the best between its competitors. These days, Kuala Lumpur is so far ahead of London and Dubai. In his opinion, Malaysia should take steps to maintain its situation. The infrastructure is perfect, man power is available, educational institution is good, rules and regulation is set and it already has plane for 10 to 15 years ahead. If Malaysia keeps on those entire elements it goes to be the hub.

The third respondent believes that Malaysia is already the hub of Islamic finance. There could be few improvement steps that can lead to increase the progression of Malaysia's level by open the market for more international investors. And find a way to standardize Islamic finance product development (the way of design).

#### ***What The Most Innovation Era In Islamic Finance Make The UK Involve In Sharia Product?***

The first respondent mentioned that London has already strong infrastructure. The nature of wealth in Muslims hands, capacities and economic growth, make London more insistence to continue to sustain its position as a finance leader. UK tries to accommodate the need of Islamic shareholders and investors.

The second respondent outlines the financial interest and political interest are the elements that make UK involve in entering the Islamic finance market. London doesn't want to be left behind. However, Islamic finance is booming and there is a great possibility to become the second in the world after the capitalism system. It is now acknowledged by even non-Muslim investors. In addition, many experts have talked that Islamic finance could be the solution for the global financial crisis. This show that there is a great future for the Islamic system and Britain must be there. From the political aspect, many of the Muslim countries (Arab, African and Asian and other Muslims) who are going to accept this system are alliance and friends to UK for that reasons Britain want to be there.

The third respondent highlights that Sukuk is the most innovation area involving the UK to participate in Islamic finance. London wants to be a part of Sukuk issuers to attract rich Muslim's people who seek to invest in Sukuk.

### ***What Are The Main Challenges When It Comes To Offering New Islamic Finance Instrument In London, Dubai And Kuala Lumpur?***

The first respondent's opinion was, the number of Islamic products not that much to offer. There are suppliers and there are demanders, but the demanders are not able to find those products. One other challenge is faced by London, Dubai and Kuala Lumpur is that the standardisations of Sharia rules. They should all work under certain Sharia regulation (whatever accepted in one accepted n the others).

The second respondent claims the challenging in all the countries is legal set up. Its common low and British low. There for, when Islamic finance comes, there will be a challenge, because they have to know how to accommodate this system which is more towards ethics. Islamic finance system is ethical financial system and that is different than the existing system, for example, the capitalist. The capitalism is the financial governing body. So, there is a conflict between the two systems. As an example, capitalism is interest based while Islamic is not. So, any of those capitalist systems want to adapt Islamic finance, their legal system does not allow. They have made change, create new lows to have room for this system.

The third respondent said follows the country rules and regulations and follow Sharia guidance such as make sure the product that they offer is profitable, also make sure it is transparent and understood easily by Sharia scholar and end-users.

### ***How Important Is Having Sharia Compliant Business In London, Dubai And Kuala Lumpur?***

The first respondents on the importance of having Sharia complaint in London, Dubai and Kuala Lumpur is because of the strong presence of demand. So that they have to be able to accommodate demand by offer Sharia compliments. Also they need to attract funds from the investors. However, the

economy of any city is affected by the Macro economy in addition to money supply.

The second respondent said, if look back to Islamic finance system; it was helping the people, improving the society, helping the poor people. Islamic system encourages Zakat, Awqaf, Sadaqah and Qurd Al-Hassan. So that is mean Islamic financial system is for everybody. The capitalism is only for the rich. Capitalism makes the rich richer and the poor even poorer. However, Islamic finance is very equitable system which gives everybody his rights. So that's why having this kind of system in any of this country is going to actually help the whole society and the whole economy. It makes everybody inclusive. In the other hand, in capitalism not everybody is inclusive; only those who have the capital are included. While, in the Islamic finance everybody is included. The poor people are included, they are given Zakat, so they can go and open their own business. So for that reasons we can understand why the Islamic finance is very important.

The third respondent claims that it is very important to have Sharia compliant product, for instance, Malaysia has stock index (Sharia screening method). It has its own criteria to going in. If a company fulfil its rules, this company going to be listed in the stock index. As a result, the companies listed earn and desire good reputation in the Islamic market as well as attracting more investors. However, Dubai and London work on Islamic finance in terms of generating more money by engaging more investors.

***What Is The Most Qualified City To Become The Hub Of Islamic Finance From Your Expectation As An Expert?***

The first respondent mentioned that even Singapore is competing, because of the attractiveness of Islamic product. London, Dubai or Kuala Lumpur sustainability is regarding to provide the facility in the way that allows any investor to invest in. Fundamentally, London is the financial hub. It already has the infrastructure. With the intention, London can easily add the Islamic product and its exponential growth is faster than Dubai and Kuala Lumpur. However, as now Kuala Lumpur gain the first position, because of it is huge history in Islamic finance and it is the central bank of it.

The second respondent without any doubt said Malaysia is the most qualified city to become the center of Islamic finance. Regardless of the strong infrastructure of commercial finance in London, Malaysia long time ago has the infrastructure of Islamic finance. UK could be the second after Malaysia. At the moment there no way Britain can compete.

The third respondent approved that Malaysia is the center of Islamic finance and it will be. He mentioned many reasons to ensure his answer, such as Malaysia has the most develop Islamic finance product. Malaysia has the most develop Islamic finance rules and regulations. Malaysia has the most develop Islamic finance education institutions. Kuala Lumpur is the largest Sukuk issuance in the world. Also, Malaysia is the most comprehensive frame work for Islamic finance. However, London has great history in commercial



finance, but it has just try to inter the Islamic once. Now days, Bahrain could be better than UK in this field as he said.

### **OVERALL DISCUSSION**

In the United Kingdom the Financial Services Authority has played a proactive role with respect to Islamic banking and finance and been broadly supportive, but that has not been the position elsewhere in Europe, where central banks and other regulatory authority have shown little interest. There is also a negative perception of Sharia, especially amongst right wing and national politicians, which potentially inhibits the spread of Islamic finance in the UK. However, Kuala Lumpur has an old reputation for efficient regulation of Islamic finance and a huge domestic market for local-currency Islamic bonds, which is now starting to attract foreign issuers. Malaysia has the advantage of a lively market in local-currency Sukuk, thanks to a Muslim-majority population; Kuala Lumpur has accounted for about two-thirds of all Sukuk issued globally this year [9]. While Islamic finance in Dubai may be growing at approximately twice as the conventional, there is still no visible race since Shariah-compliant funding represents a measly 1% of global banking assets [10]. At the same time, the growing economies of several Islamic countries, especially those in the GCC, are building up momentum in Islamic finance, which is expected to reach USD 2 trillion globally by 2015 according to Standard & Poor's. Dubai sees this as an opportunity to further diversify its economy. In addition, aside from offering world class infrastructure, Dubai is home to the world's oldest Islamic bank (Dubai Islamic Bank), has a proven track record, political stability, existing expertise and ability to attract larger pool of experts - one of the top primary Sukuk issuance source [10]. It also has a wide network of companies such as rating agencies, internationally recognized scholars and auditing companies that offers Islamic services.

### **CONCLUSION**

The research study had shown deep analyses related to the three competing cities, it also studied their past, present and future situations in Islamic finance. This study helped to show and expect the ranking of the three cities regarding to the study done, interview analysis and SWAT analysis. The expected position is; Kuala Lumpur then Dubai after that London. From the research finding, Kuala Lumpur is the most qualified city to become the hub of Islamic finance. It shows more strength points than London and Dubai. Also, it shows less weakness points than the other two cities. In the other hands, Dubai shows more strength, opportunity and less weakness than London. According to the interview, the expert's analysis and opinions emphasis that Kuala Lumpur is the best city in Islamic finance. They mentioned several convincing points about the three cities. However, they ensure that the priority is for Malaysia to become the Islamic finance center.

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