

# SUSTAINABLE ISLAMIC INVESTING IN DEMANDING TIMES



Nida Raza, Director in Advisory and Asset Management at the Islamic Corporation for the Development of the Private Sector (ICD), is a senior capital markets banker with over 18 years of global investment banking experience. She leads the teams that provide advisory and asset management solutions to FIs corporates and governments on Islamic Banking, Sukuk, Enabling Environment and Liquidity Management. During her career she has led capital market transactions for over 100 clients, helping to raise over US\$115 billion in financing. She specializes in origination, structuring, and execution of conventional and Islamic capital market instruments. She has advised FIs, NBFIs and Family offices on risk management enterprise solutions and led the introduction of complete Islamic pension solution one of the largest public pension funds in Asia. She holds a first class BSc (Hons) in Physics and Space Science from University College London as well as an MSc in International Securities Investment and Banking from the University of Reading in the UK. She has Islamic Finance Qualifications (IFQ), Series 7 & 63-qualified as well as a registered Financial Services Authority (FSA) general representative.

In this article, Umair Hameed, Director and Melda Salhab, Consultant in Monitor Deloitte Middle East meet with Nida to discuss her views on ICD, its funds strategy, and the outlook for the region.



**1) Many people may not be familiar with ICD, so could you please tell us a bit more about the organization, its stakeholders and its overall mandate?**

ICD is a multilateral development financial institution with authorized capital of US\$4 billion and it is part of the Islamic Development Bank (IDB) Group. Currently, ICD's shareholders are IDB, 52 member countries and five public financial institutions. ICD fosters sustainable economic growth in its member countries by:

- Promoting Islamic finance channels
- Providing finance for private sector projects
- Promoting competition and entrepreneurship
- Providing advisory services to governments and private companies
- Supporting the development of capital markets
- Encouraging cross-border investment

In November 2014, Fitch rated ICD "AA/F1+" with a stable outlook. In April 2015, Moody's assigned an "Aa3/P-1" rating to ICD with a stable outlook. In December 2015, Standard & Poor's Ratings Services assigned its "AA" rating to ICD with a stable outlook.

**2) As Head of Advisory and Asset Management for ICD, what sorts of sector and region are you currently focusing on?**

Our focus is diverse both in terms of geographical scope and target sectors.

Initially, the Middle East and North Africa region (MENA) accounted for many of our project

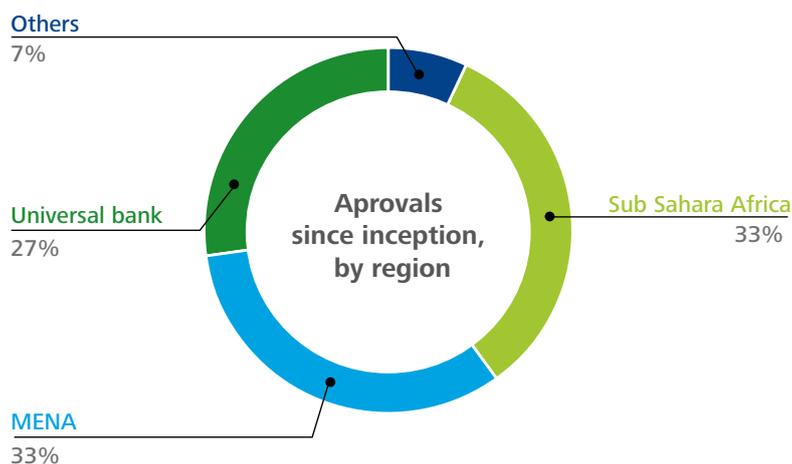
approvals. However, in 2014 we shifted our focus toward sub-Saharan Africa, mostly because of an ICD strategy to provide more support to the least-developed of our member countries. Sub-Saharan Africa now accounts for 27 percent of our total project approvals since inception.

In terms of sector focus, most of our work has been focused on finance, industry and mining, and real estate. We have also been working to increase our presence in underrepresented sectors by providing advisory services to a range of other core infrastructure industries such as telecoms, energy and transportation, as well as, the general private sector by promoting privatization, Industry and Business Environment Support programs (IBES).

**3) How are you finding the quality of the underlying assets in such turbulent markets?**

As a multilateral development financial institution our role is particularly crucial in turbulent times. Many of our member countries face dire economic circumstances. This is partly as a result of oil prices and a global economic slowdown but often political or security issues are to blame.

Being a strategic but developmental institution, it is our fiduciary duty to continuously support our member countries. We believe that financial inclusion is key—this is why we target Small and Medium enterprises (SMEs) and the financial services sector. This allows us to strengthen the backbone of emerging economies and to assist in improving the Islamic finance banking model as an alternative form of banking, both of which, if monitored and implemented correctly, have proven resilient in turbulent times across the globe.



Despite the challenging times, ICD has been successful in identifying and investing in high-quality assets. Our net income increased from US\$9.5 million in 2012 to US\$26.3 million in 2014. In parallel, the return on average assets almost doubled, while our total assets increased by approximately 50 percent.

**4) As it is a non-traditional fund, could you give us more insight about the investment strategy of ICD? How important are factors such as socio-economic impact, contribution to employment, etc. when considering investment opportunities?**

The ultimate aim of ICD is to support and boost the economic development of our member countries. Our commitment to this goal permeates our strategy, as well as, our existing products and services. ICD's commercially viable financing projects are selected based on their potential impact with regard to economic development, accounting for factors such as job creation, Islamic finance development, technology transfer, etc. Priority is usually given to projects that contribute to intra-regional trade, represent cross-border investments and have a strong export potential.

The volume of financing for a project ranges from US\$5 million to US\$20 million with average repayment periods of between five and eight years. We do not invest less than US\$2 million in any one project or more than 50 percent of the total project cost. Also, we typically do not hold more than 33 percent equity in our investments. Our target companies for investment are private sector firms or startups and privatized public sector projects or financial institutions.

**5) To what extent are fund management activities undertaken by ICD in house, rather than in collaboration with third-party service providers?**

While the majority of our processes, particularly strategic decision-making, do take place in house, we recognize the value of collaborating with other organizations. We often work with other fund managers to sponsor or create special purpose vehicles. The ideology behind this is to accelerate the launching of specialized funds based on member country (MC) requirements without compromising on the quality of ICD assessment or investment. Collaborating with local experts in addition to our Islamic structuring and access to funds provides a winning combination for our clients.

ICD identified that, in recent years, the biggest challenge faced by IFIs in our member countries has been short-term liquidity management. We reacted by launching an internally managed Money Market Fund (MMF). Our MMF has monthly liquidity and provides Islamic short-term excess liquidity investment solutions. The fund has exhibited returns of approximately 3.5 percent over the last 24 months through a combination of bank placements, as well as, investments in highly rated sukuk. Our access to and relationships with Islamic banks give us the leverage to be able to secure above-average returns on short-term investment funds.

The ICD Food and Agribusiness Fund is an excellent example of how we partnered with Rabobank, as a third-party service provider. A specialized asset

management company was established with ICD as the institutional advisor and Rabobank as the technical advisor. A team of experts was hired, including individuals on temporary placements from ICD and Rabobank. The strategic advantage of the partnership is the combined skill set—ICD offers a strong Islamic banking track record, while Rabobank provides international food and agriculture expertise. Extensive investment experience is a trait shared by both parties.

Similarly, our SME funds are typically established with a local financial institution/fund manager who has contextual expertise and a strong knowledge of the investment environment in the specific jurisdiction. Theemar and Afaq, our Tunisian and Saudi SME funds, are excellent examples. Joint GP structures provide a platform for knowledge sharing, as well as, opportunities to upskill the member country labor force. We aim to achieve this by investing in SMEs and providing them with educational and technical support (e.g., mentorship, Islamic finance education, accounting, strategy planning etc.).

**6) Would you consider alternate investment funds/private equity players to be your competition?**

There is definitely competition in the market, particularly given the presence of national investment authorities in the region and their efforts to shift away from a reliance on natural resources.

However, it is important to note that while alternative investment funds and private equity funds do compete with us in some spaces, the market is far from being overcrowded. Over the past decade, private equity capital raised in the region was equivalent to 1 percent of GDP as compared to 11 percent in the US.

Considering our other locations, there seems to be an upward trend in terms of potential competition. While historically foreign funds focused on developed or emerging markets, recent lackluster economic trends in those countries have shifted focus to regions that the ICD is heavily involved with, specifically Africa



and many parts of Asia. We do have a significant advantage by providing Sharia-compliant finance products, which appeal to many clients in many regions.

Also, most players seem to be focusing on Africa, which has extensive infrastructure requirements. This has resulted in many PE players, as well as other DFIs, which have launched funds centered on infrastructure; however, these typically only address large and mega projects. ICD's plan is to address the often neglected but highly necessary smaller infrastructure projects, which have a more immediate impact on the country but also a smaller investment horizon. These types of projects are typically not associated with the large PE and alternative investment players.

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## Most Gulf Cooperation Council (GCC) countries have established financial centers to provide easier access for international FIs to launch their Middle Eastern offices

### **7) How are the low oil prices likely to affect the fund management business for the Middle East region and for ICD's donors?**

There are two ways to view the drop in oil prices in terms of its impact on the region. The most obvious result is the sudden decrease in GCC government budgets and the spillover effect that this has on the private sector and other regions. The second interpretation is that the past year has been a long overdue stress test and wake up call. Governments have been forced to re-evaluate their financing strategies and expenditure patterns. Overall, oil-exporting countries in the region were able to sustain positive GDP growth levels, while consumers in MENA oil-importing countries benefited from the decrease in petrol prices.

As an organization, ICD remained committed to supporting member states with their diverse needs throughout this period of uncertainty. In fact, the majority of our MENA project approvals in 2014 were in oil-exporting nations. There is greater need for government financing when resource rent is unreliable. An example is a mandate for Sukuk issuance for the Hashemite Kingdom of Jordan. ICD, together with the Japan International Cooperation Agency (JICA), is helping the Jordanian government create an Islamic money market. This will help

the Islamic banks in Jordan invest their short-term excess capital and obtain suitable returns on their investment, putting them on a level playing field with their conventional counterparts. In the past they had to forgo interest on conventional investment. On the sovereign side, Jordan is able to use this liquidity for its own resource requirements, providing a win-win for all parties.

Low oil prices mean that all players will find it harder to raise additional funds for typical fund management products; however, new industry or sector-focused funds are still attractive to investors. We believe funds focused on Africa, or industry-specific financing funds (e.g., focused on Islamic infrastructure, healthcare, or education), will remain attractive. They typically remain resilient to short-term economic volatility while providing long-term stable cash flows, especially if there is a government led or sponsored private sector initiative.

### **8) Asset management across the GCC remains generally underdeveloped compared to other regions. Have you noticed higher levels of interest from various stakeholders (banks, investors, companies) in this industry? What role does ADGM play and what is its impact on the region's asset management business?**

You are absolutely correct in saying that asset management in the region is underdeveloped as a whole when compared to mature markets. For example, in developed countries, mutual funds account for the majority of Assets under Managements (AuM). Here, the trend is the exact opposite. Mutual funds represent only a tiny proportion of the industry, while separately managed portfolios for governments, big companies, and wealthy families account for billions of dollars of AuM. This is largely a result of many years of high oil prices that helped build large sovereign wealth funds and many high net worth individuals.

Most GCC countries have established financial centers to provide easier access for international FIs to launch their Middle Eastern offices. I believe that this will be further accelerated by partnerships between global AM players and regional FIs.

Consolidation and inorganic growth will be the only catalyst that will bring the Islamic AM industry into the mainstream from a GCC perspective.

Abu Dhabi Global Market (ADGM) is a welcome advance in the GCC that will help to accelerate the development of various aspects of the financial sector. The recent announcement by ADGM that it will champion the FinTech sector will help spur innovation that will benefit the general IFI industry and specifically the asset management industry, which is still very fragmented and small-scale.

I believe that we will start seeing new trends emerge. The drop in oil prices, the creation of institutions like ADGM, the opening of the Saudi market to foreign investors and the general maturing of capital markets in the region will all have a significant effect. As independent asset managers start entering the market, banks may have to begin innovating and offering more competitive products. We will also probably see a rise in multichannel distribution, especially given the digital penetration rates in the region.

The large expatriate population in the region still remits a considerable portion of surplus savings overseas for investment purposes. This, of course, represents another opportunity for the industry although it clearly needs to be accompanied by further capital market development.

Some big regulatory changes are coming soon. There has been talk about developing a unified GCC system that would ease cross-border investment. It will be similar to the European Undertakings for Collective Investment in Transferable Securities (UCITS). If this succeeds, it will help the industry develop exponentially.

### **9) *What is it like to be a female in a senior leadership position with a prominent institution in the KSA?***

One of ICD's key performance indicators is to be inclusive. ICD is clearly sending a message that being "inclusive" translates to inclusivity across all its functions, including the work force. ICD's success in this field is a testament to its leadership team, who have been recruiting and developing female senior leaders within its management.

Research has shown that female representation within boards and executive management in international companies has led to higher financial performance (see the Catalyst research report on Fortune 500 companies). Furthermore, we are also working toward supporting female populations in our MCs as they are undoubtedly an essential part of the economy. Our efforts extend from SME financing and Islamic banking to human capital development through training and education.

Personally, it is inspiring to see that ICD, as an Islamic multilateral institution, embodies the vision and mission that it promotes globally.

