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Asset Management

An introduction to Shariah investments

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Unconventional thinking. Superior performance

Contents

Islam, Islamic Law and Shariah Law

Term	Meaning
1. Islam	• Peace, Submission • Way of life
2. Muslim	One who believes in Islam
3. 5 pillars of Islam	• Belief • 5 daily prayers • Fasting • Obligatory charity • Pilgrimage
4. Shariah	• Literally means a water source • Refers to Islamic law

Shariah Law = Islamic Law

Sources of Shariah Law

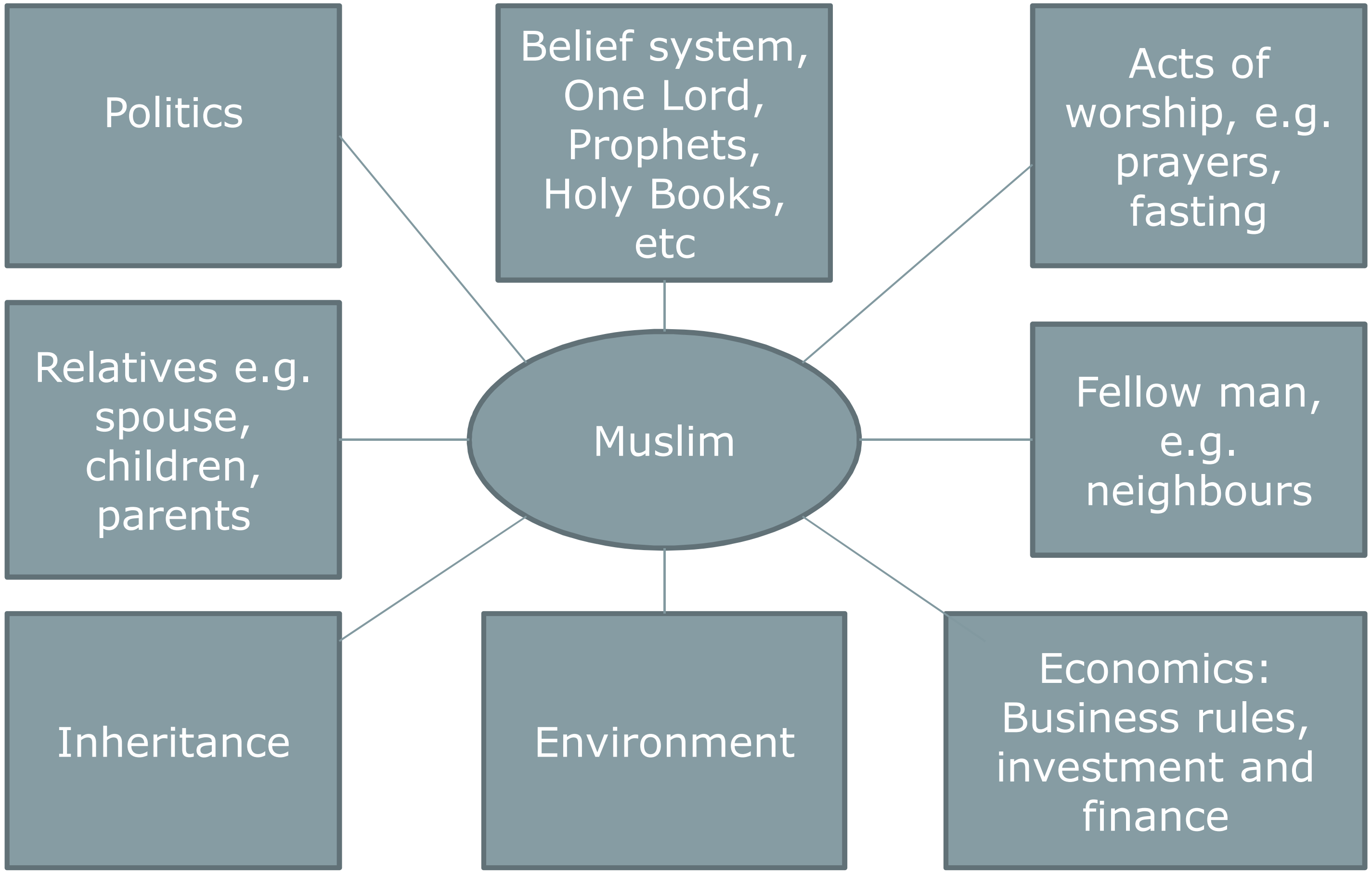
Shariah Law refers to the legal framework that governs the entire life of a Muslim

4 Sources of Shariah Law

Primary
- 1. Quran
- 2. Sunnah

Secondary
- 3. Ijma’
- 4. Qiyaas

Shariah laws covers every aspect in the life of a Muslim



Major restriction

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Interest – major sin

- “And Allah has permitted trade and prohibited Interest” – Quran
- The Holy Prophet (Peace be upon him) has cursed these people with regards to interest, the giver, the taker, the scribe and the two witnesses, and said, ‘They are equal (in sin).’ Saheeh Muslim

Basis for Shariah investments

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Shariah compliance (type of investment, risk, etc.)

- Core difference between Shariah and non-Shariah investments
- A non-Shariah compliant return has absolutely no worth to a muslim investor. Such investor may not derive any benefit from non-Shariah compliant returns/profits

Prohibited industries

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Conventional banks

Conventional insurance and re-insurance companies

Casinos and gambling institutions

Manufacturing/processing/Sale/transporting/marketing of pork, alcohol, non-halaal foods, all intoxicating food and drink

Entertainment based companies such as night clubs, pornography, etc.

Shariah models of asset management

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Wakaalah (Agency)

- A fixed fee as a percentage of net asset value of assets under management is levied for performing investment functions
- A performance based fee may also be included, if the manager meets specific pre-determined targets

Mudharabah (Profit share)

- The manager does not charge a fee
- Profits earned are split between investor and manager on a pre-agreed profit sharing ratio

Shariah ruling for investing in shares

- Islamic Fiqh academy of Jeddah
- Islamic Fiqh academy of India
- Both have ruled on the permissibility of investing in shares subject to certain conditions

Basis of this ruling

- An investor, by virtue of purchasing shares of the company, becomes a partner of the company. He owns equity in the company and his equity is exposed to risk. Hence, he is entitled to share in the profits and losses of the company

Shariah processes (screens and NPI)

Process for checking Shariah compliance of shares

- Qualitative (Industry) screen
- Quantitative (Financial) screen

Shariah processes (screens and NPI)

Qualitative (Industry) screen

- This refers to checking the main business activities of the company to ensure that the company we invest in does not primarily earn its income from impermissible activities
- If the main business of the company involves dealing in impermissible activities then it would not be permissible to invest in such a company
- Example: A conventional bank deals in lending and borrowing on interest. Hence, it would not be permissible to purchase shares of a conventional bank

Shariah processes (screens and NPI)

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Quantitative (Financial) screens

- Impermissible income to total income < 5 %
- Total interest bearing debt < 30 % of total assets
- Cash and interest bearing assets < 30 % of total assets
- Liquid assets (cash and receivables) < 70% total assets

Shariah processes (screens and NPI)

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Purification process

- Non-permissible income earned should be donated to charity
- The method of calculating the value of non-permissible income is:
  - Total value of non-permissible income divided by the profit before tax to obtain a percentage of non-permissible income included in the profit
  - This percentage is then multiplied by the value of dividends received

Shariah governance

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Internal Shariah department

- Day to day Shariah compliance
- Implements decisions made by the Shariah Supervisory Board
- Shariah audits / review

Shariah Supervisory Board

- Issuance of Shariah rulings and opinions
- Product certification
- Shariah audits / review

Q & A