

CAPITAL ADEQUACY FOR ISLAMIC BANKS & FINANCIAL INSTITUTIONS



21st - 22nd October 2019, KUALA LUMPUR

In the advent of the global financial crisis of 2007-9, Islamic banking practitioners are under significant pressure to comply with capital adequacy standards. The hope of regulators is that compliance will reduce the chance of individual bank failure, and also contagion within the financial system. The IFSB's capital adequacy framework for Islamic banks establishes minimum levels of capital which Islamic banks should maintain in order to remain solvent in the face of unexpected losses. As this framework has developed to keep track of evolving international standards for the regulation of banks set by the Bank for International Settlements (Basel Accords), they have become increasingly voluminous and technically challenging to understand. One of the biggest challenges for practitioners is knowing and understanding the relevant standards concerning capital requirements, and the determination of capital adequacy based on the capital charges of a multitude of risk types, and financial products. This not only impacts risk managers, but anyone whose financial and business decisions change the composition of the balance sheet on a forward-looking basis, for example Islamic asset origination teams and treasury managers.

This course has been developed for Islamic finance practitioners who need in-depth knowledge of the capital adequacy requirements of Islamic banks. The course provides a valued opportunity to know and to understand the IFSB's capital adequacy standards in detail, and to develop meaningful insights into practical implementation and how to overcome implementation challenges. The course also covers the development and use of the Internal Capital Adequacy Assessment Plan (ICAAP), which is an essential capital management tool used to ensure that capital adequacy is properly managed taking into consideration future changes in an institution's risk profile. The course provides an indispensable resource not only for Islamic bankers, but also Islamic bank supervisors and regulators needing expert knowledge of regulation.

The course will also include a high level of interactive discussion, practical case studies, and thorough instruction in capital adequacy regulations as they apply to Islamic banks, which can be used in practice to meet regulatory governance and reporting requirements.

KEY HIGHLIGHTS

- Know and understand Basel III as it relates to Islamic banks
- Know and understand IFSB standards for Islamic bank capital adequacy
- Understand how these standards are implemented in practice
- Understand how banks manage capital using economic capital planning
- Develop and use the Internal Capital Adequacy Assessment Plan
- Understand the treatment of complex financial instruments from a capital adequacy viewpoint

AGENDA

Day 1

Session One: Overview and Basel III changes

Basel Regulatory Standards

- From Basel I to Basel III
 - How have the Basel standards evolved over time?
- What are the changes introduced by Basel III?
 - Capital quality
 - Capital buffers
 - Liquidity ratios
 - Leverage
- What is the impact of Basel III on Islamic banks?

Capital Adjustments, Deductions and Buffers

- Capital deductions from Common Equity Tier 1
- Capital conservation buffer
- Countercyclical buffer

Other Regulatory Changes

- Leverage ratio
- Islamic windows
- Systemically important banks

Session Two: IFSB-15 Revised Capital Adequacy Standard

How Credit risk arises in Islamic Financial Instruments

- Murabahah accounts receivable
- Salam counterparty risk
- Istisna accounts receivable and counterparty risk
- Ijarah lease payments receivable
- Sukuk held in the banking book

How Market Risk arises in Islamic Financial Instruments

- Equity trading positions
- Sukuk trading positions due to changes in market price of benchmarks
- FX risk
- Commodities and inventory risk (held for resale in Murabahah, or Ijarah)
- Exposures from hedges which are MTM

Capital Calculation by Risk Type

- Market Risk
- Credit Risk and credit risk mitigants
- Operational Risk
- Risks arising from Profit Sharing Investment Accounts

Quiz 1: Capital Adjustments and Buffers; Capital Adequacy by Risk Type

Session Three: IFSB-15 Revised Capital Adequacy Standard

Minimum Capital Requirement by Financial Instrument

- Murabahah and Murabahah for the Purchase Orderer (MPO)
- Commodity Murabahah Transactions

- Salam
- Istisna
- Ijarah and Ijarah Muntahiyah Bittamleek
- Musharakah and Diminishing Musharakah
- Mudarabah
- Qard
- Wakalah

Quiz 2: Capital Charges by Financial Instrument

Day Two

Session One: Sukuk and other Assets

- Treatment of Sukuk
 - Rated Sukuk
 - Unrated Sukuk
- Treatment of real estate
- Treatment of Islamic derivative contracts
 - Credit risk equivalents
 - Islamic Forwards and Islamic Profit Rate Swaps
- Mapping IFSB-15 to BNM's Capital Adequacy Framework for Islamic Banks (issued March 2017)

Session Two: Internal Capital Adequacy Assessment Plan

- What is an ICAAP and what is it used for?
- What is the difference between regulatory capital and economic capital?
- Application of the value-at-risk methodology to economic capital adequacy
- How to determine which lines of business or products utilize the most economic capital
- Stress-testing economic capital adequacy
- What management actions are needed if capital is deemed inadequate?

Session Three: Implementation and Models

- Implementation and related challenges
 - Regulatory treatment of asset-based financing
 - Technology: to build or to buy?
 - Policies: embedding capital adequacy into decision-making
 - Reporting: making the capital adequacy information internally useful
- Calculation models for capital adequacy
 - Which are the most important capital adequacy models to have?
 - Who should develop and maintain a model?
 - How sophisticated should a model be?
 - How should the institution audit a financial model?
 - What is the role of the regulator in the financial modelling process?

Closing Discussion and Wrap-Up

SPEAKERS



Dr. Ken Baldwin
Former Director
*Financial Policies &
Planning, Islamic
Development Bank*

Dr. Ken Baldwin has worked as a practitioner in banking and finance for over 25 years in senior positions spanning the front and middle offices. Having graduated from Oxford University with a first-class honors degree in Physics in 1989, he qualified as a Chartered Accountant with PWC, before joining UBS, and then later Credit Suisse, in derivatives risk and control functions based in London.

He gained a PhD in the microeconomic theory of risk sharing in Islamic contracts, and worked in the GCC for 15 years in Islamic retail and Islamic investment banks. Whilst at Abu Dhabi Islamic Bank, Dr. Ken built an ALM analytic technology platform capable of capturing liquidity and interest rate risks inherent in the many varied Islamic financing products used at retail and corporate levels. He then moved to take up the position of MENA Regional Head of Quantitative Analysis for Citigroup. At Citicorp, Dr. Ken worked on structuring complex products used by Gulf-regional corporations to hedge FX and interest risks. Still residing in Bahrain, Dr. Ken then joined Investcorp, where he worked on the risk due diligence of corporate private equity and real estate private equity transactions and portfolio management. After leaving Investcorp, he set up the risk management department for venture capital bank, providing Basel III compliance and deal analysis for the bank. He then operationalized a new Islamic investment bank as its Chief Operating Officer for 3 years, before his most recent industry role at the Islamic Development Bank, where he set up and ran a new department tasked with developing Financial Policies and Planning underpinned by robust financial analytic tools and methodologies designed specifically for the IDB. Dr. Ken is currently a senior university lecturer in finance in the UK. He has published quantitative finance articles in peer-reviewed academic journals including the Journal of Risk, and during his earlier career, taught CFA and FRM professional certifications as a pastime for the Bahrain Institute of Banking and Finance.

Ken is a British Muslim.

Who Should Attend?

- Board members with risk and audit responsibilities
- Risk officers, risk managers, risk analysts
- Asset origination teams and treasury managers
- Compliance, legal, IT, finance and risk management support personnel
- Central bank supervisors and analysts
- Rating agency analysts

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