
Islamic Finance: The Way Forward for Japan

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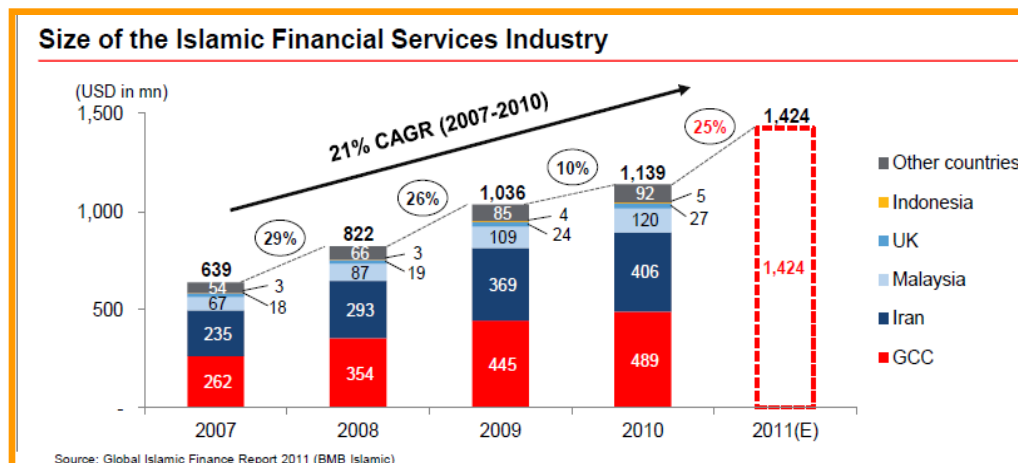
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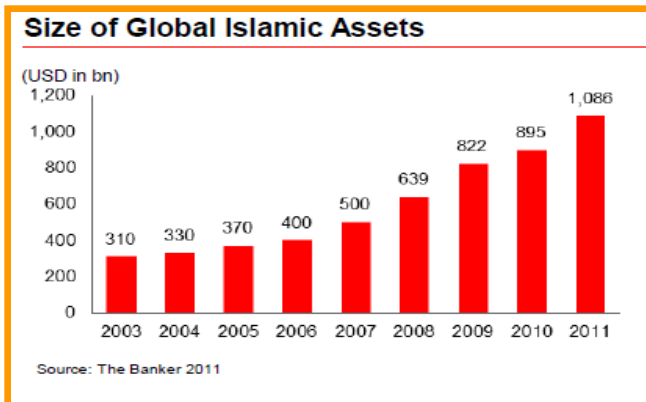
I. Cursory View of Islamic Finance

Islamic Finance Global Development

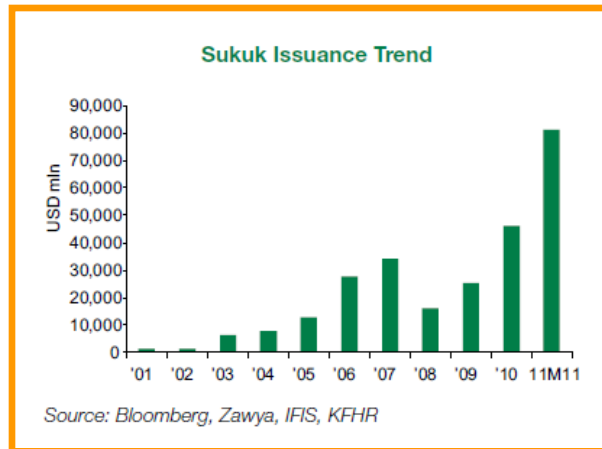


- Total Shariah-compliant assets have surpassed the USD1 trillion mark in 2011.

- Despite challenging global environment, Islamic finance experienced growth of 21% over the last 5 years.



Islamic Finance Global Development



- *Sukuk* market is now well-developed; registering 57% (CAGR) growth since 2001.
- *Sukuk* market has expanded to USD180 billion by end-2011.

Currently, there are more than 600 Islamic financial institutions, operating in more than 75 countries (both Muslim and non-Muslim)

Source : Central Bank of Malaysia

Islamic finance is beginning to establish in key financial areas in the EU region; such as UK, Luxembourg, France.

Source : Central Bank of Malaysia

II. Merits for Japanese Corporations to Utilize Islamic Finance



Diversifying Funding Sources

- Considering the fact the Islamic finance industry is growing at average 21% per annum and significantly growing after the Lehman Shock, the importance of Islamic finance is expected to increase even more under the difficult financial environment in US and Europe. It is beneficial for Japanese corporations to ensure an access to this ever growing Islamic finance market.
- By accumulating experience and know-how in Islamic finance, Japanese corporate can expect a more diversified funding sources through utilizing various Islamic financing schemes and/or Sukuk (Islamic bonds).

Enhancing Corporate Image in Muslim Countries

- Generating positive PR image of a corporation that is progressive in applying leading-edge financing methods, and is deeply rooted in the Muslim society.
 - Muslim population is expected to exceed more than one-fourth of the world population in the future.
 - In Malaysia, as the Government and Central Bank is proactively promoting Islamic finance, corporations utilizing Islamic finance can appeal to the public on their positive stance towards Islamic finance, and at the same time use Islamic finance effectively in their corporate image strategy to create an image of a company that is deeply rooted in the local (Muslim) society.
 - In some countries such as the GCC region, funding for mega projects may need to be procured through a Shariah compliant financing.

III. Development of Islamic Finance in Japan

Japanese Government and Government-Linked Financial Institutions are Committed to the Development of Islamic Finance

Major Development

- 2006 The Islamic Finance Research Group was set up at the request of the Ministry of Finance. Japan Bank for International Cooperation (JBIC) launched a Shariah Advisory Group, and joined IFSB in 2007 as an observer member. Currently, 7 Japanese institutions and corporations including BTMU's subsidiary in Malaysia (BTMU Malaysia) joined as observer members.
- 2008 The amendment of the Order for Enforcement of the Banking Act allows subsidiaries of a Japanese bank to engage in Islamic banking business.

Japanese Government and Government-Linked Financial Institutions are Committed to the Development of Islamic Finance *(continue)*

Major Development

- 2011 Pursuant to the tax reform in 2011, the profit to be distributed to the investors holding quasi-bond beneficiaries under the Asset Securitization Act to be used as J-Sukuk (Islamic bonds) will be exempted from withholding tax.
- 2012 FSA Japan is conducting a study on Islamic banking business by Japanese banks' overseas subsidiaries. It is expected that this will result in the Japanese Banking Act to be amended, earliest by 2013. (Source: Nikkin Newspaper, December 2011)

Development by Japanese Corporations

Major Development

- 2007 The Malaysian subsidiary of Aeon Credit Service Co., Ltd set up a RM400.0 million (approx. JPY13.6 billion) Bank Guaranteed Conventional and Islamic CP/MTN Programme which was arranged by BTMU Malaysia, CIMB Investment Bank Berhad and Maybank Investment Bank Berhad.
- 2008 BTMU Malaysia, a subsidiary of Bank of Tokyo-Mitsubishi UFJ, is the first Japanese-owned bank to obtain the approval to conduct Islamic banking business. The Islamic banking department and an in-house Shariah Committee within BTMU Malaysia was also established in the same year.
- 2008 The Malaysian subsidiary of Toyota Financial Service Co., Ltd set up RM1.0 Billion (approx. JPY 32 billion) nominal value Islamic CP/MTN Programme which was arranged by BTMU Malaysia and CIMB Investment Bank.

Development by Japanese Corporations (*continue*)

Major Development

- 2008 Nomura Asset Management Co., Ltd. established a subsidiary in Malaysia specializing in Shariah compliant asset.
- 2009 Mizuho Securities Co., Ltd. alliances with Maybank Investment Bank in Malaysia in Islamic finance business.
- 2010 Sumitomo Mitsui Banking Corporation announced business alliance with RHB Bank Berhad in Malaysia. Nomura Holdings Inc. announced a full-scale expansion into Islamic finance business, and issued its own Sukuk.

Development by Japanese Corporations (*continue*)

Major Development

- 2011 Mizuho Corporate Bank, Ltd. announced its alliances with Malaysian Banking Berhad (Maybank), and new business deployment including Islamic finance in Malaysia. Mitsui Sumitomo Insurance Company Limited announced its capitalization on takaful business.
- 2012 Mizuho Corporate Bank, Ltd. obtained approval from Bank Negara Malaysia (Central Bank of Malaysia) to conduct Islamic banking business, through its International Currency Business Unit.

IV. Examples of Japanese Corporations Utilizing Islamic Finance

IV. Examples of Japanese Corporations Utilizing Funding Examples Using Islamic Finance

Japanese Corporations in Muslim Countries that is Actively Utilizing Islamic Finance

Company Name	Country	Description	Amount
Sukuk			
Aeon Credit Service	Malaysia	The first Sukuk issuance by a Japanese corporation (2007)	RM 400 million (MTM Programme) (USD 120 million)
Toyota Financial Service	Malaysia	Sukuk issuance by a subsidiary of Toyota Financial Service in Malaysia (2008)	RM 1 billion (MTN Programme) (USD 310 million)
Nomura Holdings	Malaysia	Issuance of Sukuk utilizing leasing of aircrafts (2010)	USD 100 million
Project Financing			
Sumitomo Chemical	Saudi Arabia	Rabigh Refining & Petrochemical Complex Project	USD 600 million (Total construction cost USD 9.8 billion)
Mitsui & Co./TEPCO	UAE (Abu Dhabi)	Umm Al Nar Power & Water Desalination Plant Project	USD 500 million (Total construction cost USD 2.5 billion)
Mitsui & Co./ Chubu Elec./ Shikoku Elec.	Qatar	Ras Laffan Power & Water Desalination Plant Project	USD 250 million (Total construction cost USD 3.9 billion)
Mitsubishi Corp.	Saudi Arabia	Shukeik Power & Water Desalination Plant Project	Unknown (Total construction cost USD 2 billion)

**Japanese Corporations in Muslim Countries
that is Actively Utilizing Islamic Finance (*continue*)**

Company Name	Country	Description	Amount
Bilateral Financing			
Japan Automobile Company	Malaysia	Murabahah Working Capital Financing-i	USD 5 Million
Electronic Distribution Company	Malaysia	Commodity Murabahah Financing	USD 8 Million

V. The Way Forward



Commitment and Support from Government

- Due to the legal lending limit constraints imposed by the Central Bank of Malaysia, Japanese banks' subsidiaries operating Islamic finance in Malaysia face difficulty to participate in mega deals that required Shariah-compliant funding. .
- Hence, this put Japanese banks in unfavorable positions and restricts them from tapping into the growing Islamic finance assets. .
- Therefore, necessary amendments to the Japanese Banking Act to facilitate Japanese banks' overseas strategies are much needed. Such regulatory reform would be regarded as a commitment from the Japanese government to pave the way towards a more robust Islamic finance in Japan. .

3-Tier Strategic Moves

- Considering the current unique position in which only Japanese overseas subsidiaries can engage in Islamic finance, Japanese banks must make strategic adjustments in order to take part and compete as one of the leading Islamic finance service providers in the world.
- There are 3 tiers for Japanese banks to embark:

TIER 1

To support Japanese corporation through its subsidiary engaging in Islamic finance; within the country where the subsidiary is located.

TIER 2

Based on the success in Tier 1, to expand the Islamic finance business into other Muslim countries (or other countries where there is demand for Islamic finance).

TIER 3

To bring back the know-how gathered from Tier 1 and Tier 2 experiences in order to spread Islamic finance in Japan.

Creating Demand and Supply

- In Tier 1, the subsidiary of Japanese banks that engage in Islamic finance would strategically be located in a country where there is conducive environment for Islamic financial system; such as strong support from the government, well developed governance framework and regulatory system, and abundant human capital talents, among others. Generally, the market for Islamic finance in such countries are well developed and there is steady demand for Islamic finance products.
- In the next stage Tier 2, it is expected that the Japanese banks would expand into other countries that would have the same robust environment as the initial set-up country in Tier 1; such as the Middle East and South East Asian regions where the majority are Muslim countries. It may also be strategic to explore into 'younger' markets such as non-Muslim countries where there are increasing awareness and demand for Islamic-based products.

Creating Demand and Supply *(continue)*



In both Tier 1 and Tier 2, the markets for Islamic finance are relatively matured and led by demands with sophisticated needs. In such fierce competition, Japanese banks must create their own competitive edges that are able to attract loyal customers. To achieve this, Japanese banks must stay ahead of the evolving products development, and deliver reliable services that fulfill the s a t i s f a c t i o n s o f customer.

Creating Demand and Supply (*continue*)

However, to achieve Tier 3, the approach might be different. Considering that Japan is a young market for Islamic finance, the approach would have to be supply driven. Japanese banks have the competitive advantage in creating the market for Islamic finance in their own homeland. Hence, they must be creative and inventive so that they can create their own uniqueness.

On the other hand, there must be matching effort to spur the market with demands. This requires strong support from the government to not only create a conducive environment (through legal and infrastructure framework) but also to facilitate the awareness for Islamic finance among its 128 million citizens.



Arigato Gozaimashita

