Foreword

Zeti Akhtar Aziz

International optimal portfolio diversification has long been considered the gold standard for long-term savings. It is practiced by the leading investors of the world, from international SWFs (sovereign wealth funds) to the major public employees' retirement funds.

This golden rule is also known to individual investors: diversify your savings portfolio not only by the type of investments but by regions too. As a result, we have seen the intensification of the globalization of financial flows; cross-border portfolio investments now account for hundreds of trillions of dollars, with the amount in the global asset management industry now reaching \$100 trillion.

Up to now, however, we have yet to see the emergence of a well-defined, industry-wide practice in Islamic asset management, which also includes wealth management. There seems to be an absence of incentive or focus from the world's major asset management institutions to deliver asset management offerings which adhere to the principles being followed by a quarter of the world's population.

Of importance, however, is the significant growth in ethical and socially responsible investment activities. Large numbers of endowments, pension funds and family offices worldwide have now signed up to the protocols for ESG and SRI investing, redirecting their investments toward those stocks, bonds, mutual funds and ETFs (exchange-traded funds) that are certified as either doing good or, at the least, doing no harm. Ethical investment activities are said to have now achieved a 20% penetration into the global asset management universe.

Because there is much in common between investing according to sharia and ethical investing, both can be considered to be in the same league. Studies have shown that these forms of finance focus on their positive impact on the economy and their long-term growth and sustainability. Recognizing that these similar elements are embedded in these respective forms of finance, the case is made in this book that the rigorous and robust professional practice in asset management can therefore be matched to the funds that adopt the principles of Islam to thereby support the development of the Islamic asset management industry.

Asset managers are fastidious in general. They apply modern portfolio theories and analytics that feature cutting-edge knowledge of statistics, data generation and comparative analysis in their approach to asset management. Supporting their efforts are the eminent works of several Nobel Laureates who have been some of the most celebrated contributors to financial market theory. Perhaps in no other industry has professional best-practice been so thoroughly enjoined with scholarship.

This has produced clarity on the path toward global diversification, risk management and optimized returns. Thus, one should not consider Islamic asset management without having the required knowledge and discipline needed to meet these tough professional standards and rigorous theoretical constructs, while at the same time looking over one's shoulder to comply with contemporary regulatory standards.

This book achieves the goal of simultaneously examining financial market theory—those concepts that have been proven over the decades to support responsible and optimal asset allocation—and then applying these rules of investing within the context of sharia. At the same time, it takes into consideration the prudential requirements imposed by regulatory authorities.

This book contributes something new, something that has yet to surface among the academic or professional literature. It applies the theoretical foundations, professional discipline and regulatory standards adopted in conventional asset management to the sharia-compliant investible universe. This is an exemplary contribution of this book. Prior to constructing optimal portfolios there has to be an understanding of where to find the securities needed for investment. The book provides readers with the manner in which to extract the data for over 1,000 Islamic mutual funds and ETFs, while also providing detailed guidance for sorting and filtering this universe of securities, thereby providing a list of funds that meet the required professional and regulatory standards.

The authors have made a major contribution in their efforts to align Islamic finance to the exigence of modern financial intermediation and portfolio asset management, while respecting the requirements of sharia to ensure that this form of financial activity stays true to its core values.

Finance, however, covers several sectors that include banking, insurance and asset management. We have long known that economic efficiency is improved when savers can effectively and efficiently channel their savings to the users of capital. In highly developed markets we see the intensive financialization of savings, starting with the growth of the banking sector, before progressing to higher penetration rates in the insurance sector and to increasingly massive volumes of funds that now come under professional asset and wealth management.

While being exemplary in banking and insurance (takaful), asset management in Islamic finance has yet to experience much growth. Contemporary numbers indicate the relatively very small size of the Islamic asset management industry, with only about 1,000 investment products and just over \$60 billion in total AUM (assets under management). These numbers themselves represent not only a small fraction of total assets in Islamic finance but an even smaller fraction of the total assets under the conventional asset management industry worldwide.

There needs to be new efforts toward spurring the further advancement of the Islamic asset management industry. Indeed, we know that Muslims do not differ from those from other faiths when it comes to savings. Anecdotally, many of them have higher household savings rates than their peers in other parts of the world.

Much needed, therefore, is the development of vehicles for their savings that match their spiritual requirements. The global asset management industry has not yet addressed this mismatch between the potential demand and supply. This is perhaps in part because until now there has been no practical guide for Islamic asset management, one that is deeply rooted in the theory embraced by conventional asset managers.

This book has aimed to do just that. It provides the global Islamic asset management business something that may be used as guidance; it has provided a formal, rigorous, professional framework for such guidance. For this, the authors should be commended for their work.

I hope academics, industry players and policymakers will benefit from reading this book.

Zeti Akhtar Aziz
Former Governor, Bank Negara Malaysia, Malaysia
20 August 2020