General Council for Islamic Banks and Financial Institutions

المجلس العام للبنوك والمؤسسات المالية الإسلامية

CIBAFI

Global Islamic Bankers' Survey

SEPTEMBER 2024

Islamic Social Financing:

Assessing Islamic Banks' Current Initiatives and Potential Impact

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About the General Council for Islamic Banks and Financial Institutions (CIBAFI)

CIBAFI is an international organisation established in 2001 and headquartered in the Kingdom of Bahrain. CIBAFI is affiliated with the Organisation of Islamic Cooperation (OIC).

CIBAFI represents the Islamic financial services industry (IFSI) globally, defending and promoting its role, consolidating co-operation among its members, and with other institutions with similar interests and objectives.

With over 130 members from more than 30 jurisdictions, representing market players, international intergovernmental organisations, professional firms, and industry associations, CIBAFI is recognised as a key piece in the international architecture of Islamic finance.

Its mission is to support the IFSI's growth by providing specific activities and initiatives that leverage current opportunities while preserving the value proposition of Islamic finance. CIBAFI is guided by its Strategic Objectives, which are,

1) Advocacy of Islamic Finance Values and Related Policies & Regulations;

2) Sustainability and Innovation Integration;

3) Industry Research and Analysis; and

4) Professional Development.

Contents

Acronyms

AI	Artificial Intelligence
CIBAFI	General Council for Islamic Banks and Financial Institutions
OIC	Organisation of Islamic Cooperation
IFC	The International Finance Corporation
IFSI	Islamic Financial services Industry
GIBS	Global Islamic Bankers’ Survey
MSMEs	Micro, small, and Medium Enterprises
FinTech	Financial Technology

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Statement by the Secretary General

It is with great pleasure that I introduce the ninth edition of the CIBAFI Global Islamic Bankers' Survey (GIBS) Report. Throughout its various editions, the GIBS Report has consistently offered valuable insights into the key concerns, practices, and emerging trends within the Islamic banking sector, establishing itself as a vital benchmark for assessing Islamic banking executives' perspectives on the industry's future. The report has explored factors influencing growth, including sustainability, financial technology (FinTech), regulatory changes, women's empowerment, and talent management.

This year's edition of the GIBS Report highlights the role of the Islamic banking sector in contributing to global social welfare. It emphasises the importance of Islamic banking in advancing social causes, advocating for the integration of cutting-edge technologies, improved governance practices, and global collaborations to enhance its impact.

The report investigates the opportunities and challenges faced by Islamic banks in leveraging these instruments to mobilise funds for socially oriented initiatives, such as supporting vulnerable groups, financing micro, small, and medium enterprises (MSMEs), and promoting social development projects. Furthermore, it examines how innovation and technology can elevate the role of Islamic banking in social finance and foster inclusivity.

Amid escalating geopolitical conflicts and ongoing economic challenges, this year's findings underscore Islamic banks' commitment to navigating an increasingly complex landscape. Balancing technological advancements, shareholder expectations, and risk management while amplifying their social impact remains crucial. Continuous emphasis on strategic partnerships and innovative approaches to social finance will be essential for sustaining growth and reinforcing the principles of Islamic finance.

We trust that this report provides a comprehensive perspective on social finance within the Islamic banking industry and serves as a valuable reference for understanding the forthcoming challenges and opportunities. Our goal is to equip industry leaders with the knowledge and insights needed to navigate the complexities of today's global economic environment and make informed decisions for a successful future.

Dr. Abdelilah Belatik
Secretary General

Acknowledgements

The Secretariat would like to extend its deepest gratitude to all the member and non-member banks and financial institutions who took the time to participate in the survey and share their valuable insights.

We would also like to express our sincere appreciation to the individuals who have played an instrumental role in the success of this report. Our sincere thanks go to the CIBAFI Secretariat, and Mr. Peter Casey, CIBAFI Consultant, for their efforts in the different phases of this report's production.

In addition, CIBAFI extends its gratitude to its partners, Albaraka Türk Katılım Bankası A.Ş. "Knowledge Partner"; and DDCAP "Supporting Partner", for their support in the launch of the GIBS 2024 Report.

We are hopeful that the report will provide valuable insights on the prospects for the Islamic banking industry as we strive together for its development and growth.

Dr. Abdelilah Belatik
Secretary General

Executive Summary

In light of escalating geopolitical tensions and persistent economic challenges, the urgency for initiatives that positively impact society and alleviate individual hardships has never been greater. Mobilising the necessary funds can be achieved through social financing, which is crucial due to its scale and inclusiveness.

This year's edition of the GIBS report explores the role of Islamic banks in social financing, examining both the benefits and challenges. The aim is to highlight the importance of Islamic banking in advancing social causes and to deepen stakeholders' understanding of how Islamic banks actively engage in Islamic social finance. This includes shedding light on the associated challenges, innovative strategies, and collaborative partnerships. Ultimately, the report seeks to inform and inspire strategies that integrate sustainability, financial inclusion, social welfare, and economic development, all while upholding the ethical values intrinsic to Islamic finance.

The first and second parts of the report provide a comprehensive view of Islamic banking executives' perspectives on the industry's current and future landscape, as well as the key concerns and risks facing Islamic banks in the coming years. Despite ongoing turbulence, the sector's outlook remains stable and optimistic, reflecting its resilience and adaptability in a volatile environment.

Findings in Part 1 reveal a notable sense of confidence among Islamic banking executives regarding their sector's future prospects. This positive outlook suggests that while the severity of most risks remains stable, Islamic banks are effectively managing these challenges. However, this stability in risk levels could also be attributed to a potential underestimation of emerging risks. It is important to consider whether some risks may be downplayed, which could impact the sector's resilience in the long term.

Information technology continues to be a critical focus for Islamic banking institutions. The swift evolution of technology, which encompasses innovations such as generative AI, offers both prospects and obstacles. These developments influence consumer behaviour and expectations, which are of utmost importance to Islamic banks. Upholding a customer-oriented strategy is crucial for ongoing expansion.

Meeting shareholder expectations has emerged as a significant focus for Islamic banks. Balancing financial performance with the ethical principles of Islamic banking is increasingly vital. This emphasis on shareholder value underscores the sector's commitment to aligning profitability with ethical standards, ensuring long-term success while adhering to core Islamic principles amidst global issues such as the macroeconomic environment, which remains a significant concern. Global economic slowdowns and geopolitical tensions pose ongoing challenges, requiring banks to stay informed and responsive to global trends to sustain stability and competitive advantage.

The risks reported by Islamic banks in the second part of the report indicate confidence in their ability to manage risks, with most risks showing no increase in severity. This aligns with the perceptions reported in the first part. This confidence is consistent across global and regional contexts, underscoring the sector's resilience amidst increasingly complex economic conditions worldwide. Nonetheless, some risks have seen slight increases while others have decreased. These shifts suggest that Islamic banks are adapting their risk management approaches in response to evolving global economic dynamics, aligning their strategies with current market challenges and opportunities.
Technological risks are at the forefront, with Islamic banks also prioritising credit risk due to economic and geopolitical factors. Risks related to extreme disruptive events and climate change have experienced minor shifts in severity, prompting continued vigilance and action plans to manage these emerging threats.

The concluding part of the report examines the role Islamic banks play in Islamic social finance, underscoring their approaches, prospects, and difficulties. The results show that microfinance is regarded by most respondents as an essential tool for social finance, yet regional variations impact the efficacy of Islamic financial offerings. Savings accounts are commonly utilised; however, there's less participation in Zakat and Waqf financing models. Opportunities exist for greater engagement in sectors like Zakat funding and Islamic crowdfunding. Banks are advised to enhance their focus on healthcare and eco-friendly initiatives.

Islamic banks are perceived as better suited for social finance compared to conventional banks, driven by goals such as sustainable development and enhanced reputation. Challenges include a lack of awareness, a shortage of qualified professionals, and unclear regulatory frameworks. Despite these obstacles, Islamic banks have made progress in social finance, leading to improved branding, customer attraction, and economic impact. Many banks are forming partnerships with government bodies and NGOs to boost their social finance efforts.

The report ends by offering strategic recommendations for Islamic banks to manage economic unpredictability. It advocates for the development of digital frameworks using emergent technologies such as AI and big data, which can increase operational efficiency and enrich the customer journey. Cultivating an environment that values consistent learning and innovation is crucial for maintaining market competitiveness. Moreover, reinforcing social finance activities with a focus on sustainability and inclusivity, and engaging in cooperative endeavours with relevant stakeholders and industry peers, will amplify the influence and proficiency of Islamic financial institutions.

Through the various sections, the GIBS report presents insights from Islamic banking leaders regarding the future of the industry, focusing on the role of Islamic banks in advancing social finance.

CIBAFI's Global Islamic Bankers' Survey

Introduction

The Global Islamic Bankers' Survey (GIBS) Report, now in its ninth edition, continues to serve as an essential benchmark for evaluating Islamic banking executives' views on the industry's trajectory. The report, in its previous editions, examines various factors shaping growth, such as sustainability, financial technology (FinTech), regulatory developments, women's empowerment, and talent management.

In light of the ongoing global uncertainties, which include economic volatility and political upheaval, supporting social initiatives and causes through financing has become increasingly crucial. These challenges exert significant pressure on many individuals, highlighting the urgent need for robust financial mechanisms to address social issues and foster resilience. The GIBS Report underscores the importance of Islamic banking in advancing social finance, reflecting its role in mitigating these global pressures and driving positive change.

We are delighted to report that once again, we have received a significant number of responses to the survey, with 95 Islamic banking executives from 30 countries participating. The analysis of the report thus covers responses from various backgrounds and markets, allowing a comprehensive overview of the experiences of Islamic banks across different regions. It also permits displaying a diversity of practices based on each market's development. Together with the results of previous years, readers can draw a clear picture of the evolution of Islamic banking executives' views on various concerns and risks facing the industry.

The table below outlines more details on this year's respondents.

Table 1. Respondents by Regions and Countries

Group	Region	Countries of respondents	Number of respondents in this group
Group 1	GCC	Bahrain, Kuwait, Oman, Saudi Arabia, UAE	19
Group 2	Middle East ex-GCC	Egypt, Iraq, Jordan, Palestine, Syria	24
Group 3	Southeast Asia	Malaysia	6
Group 4	West, Central, and South Asia	Afghanistan, Bangladesh, Pakistan, Sri Lanka	11
Group 5	North Africa	Algeria, Libya, Morocco, Sudan, Tunisia	16
Group 6	Sub-Saharan Africa	Burkina Faso, Djibouti, Kenya, Mauritania, Nigeria, Somalia, South Africa	11
Group 7	Europe, Türkiye, US & Others	Bosnia Herzegovina, Türkiye, Suriname	8
Total number of countries and respondents		**30 Countries**	**95 Islamic Banks/Financial Institutions**

The survey respondents for this year's edition comprised a diverse range of Islamic financial institutions, including full-fledged Islamic banks (around 77%), Islamic bank subsidiaries (around 13%), Islamic banking windows of conventional banks (around 8%), and other Islamic financial institutions (around 2%). It is worth noting that compared to the previous year, the sample of participating institutions has decreased. This could be due to significant mergers and acquisitions in the GCC region, as well as the inability of some banks to participate in this year's survey due to communication difficulties caused by the war situations in their respective countries.

The main business of these respondents varied, with 40% focusing on both retail and wholesale banking, 20% primarily on retail banking, about 14% on wholesale banking, about 22% on investment banking and around 4% focused on other areas. More than half of the respondents reported total assets of less than one billion USD (around 51%), with the remaining distributed among those with total assets of one to five billion USD (around 25%), five to ten billion USD (around 12%), and over ten billion USD (around 13%).

Figure 1. Type of Islamic Banking Operation

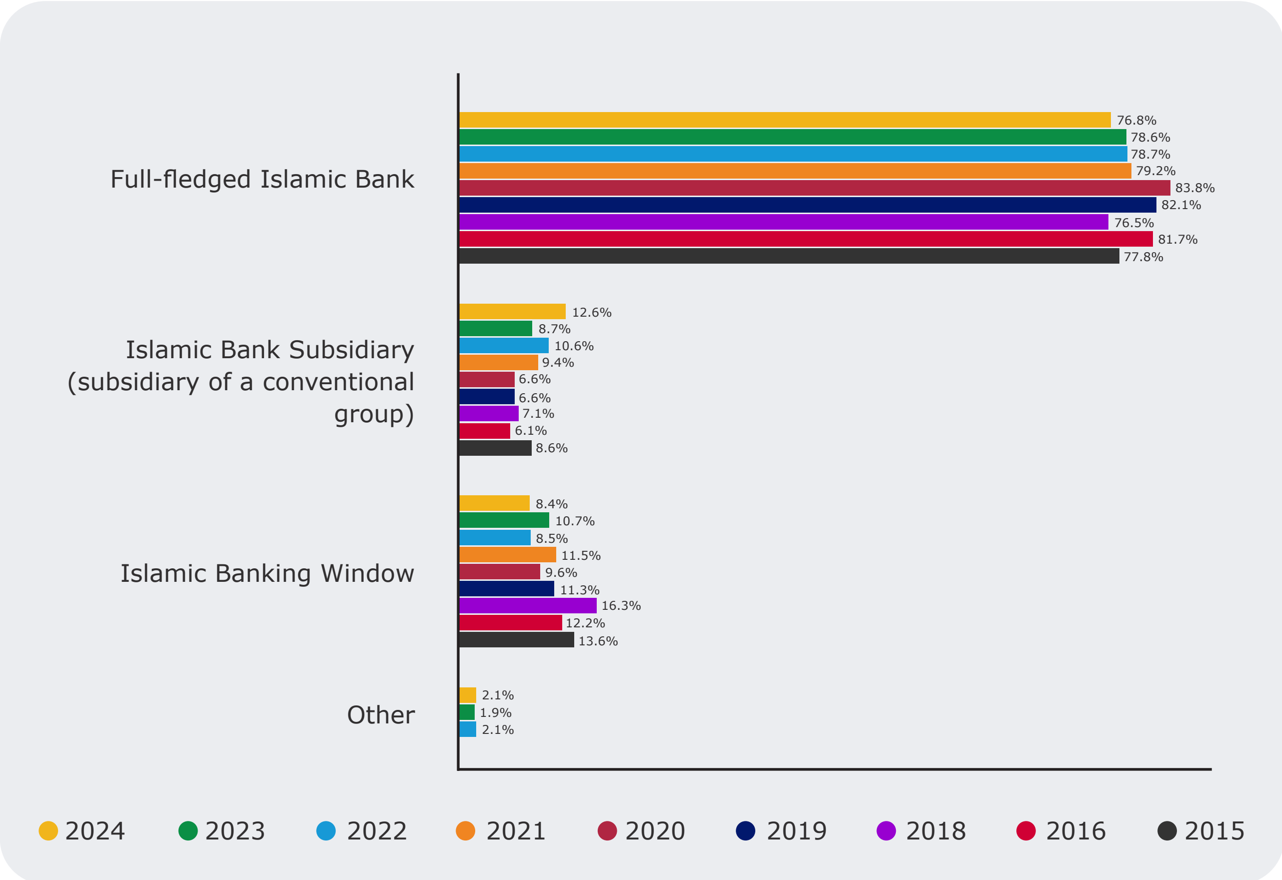


Figure 2. Core Business

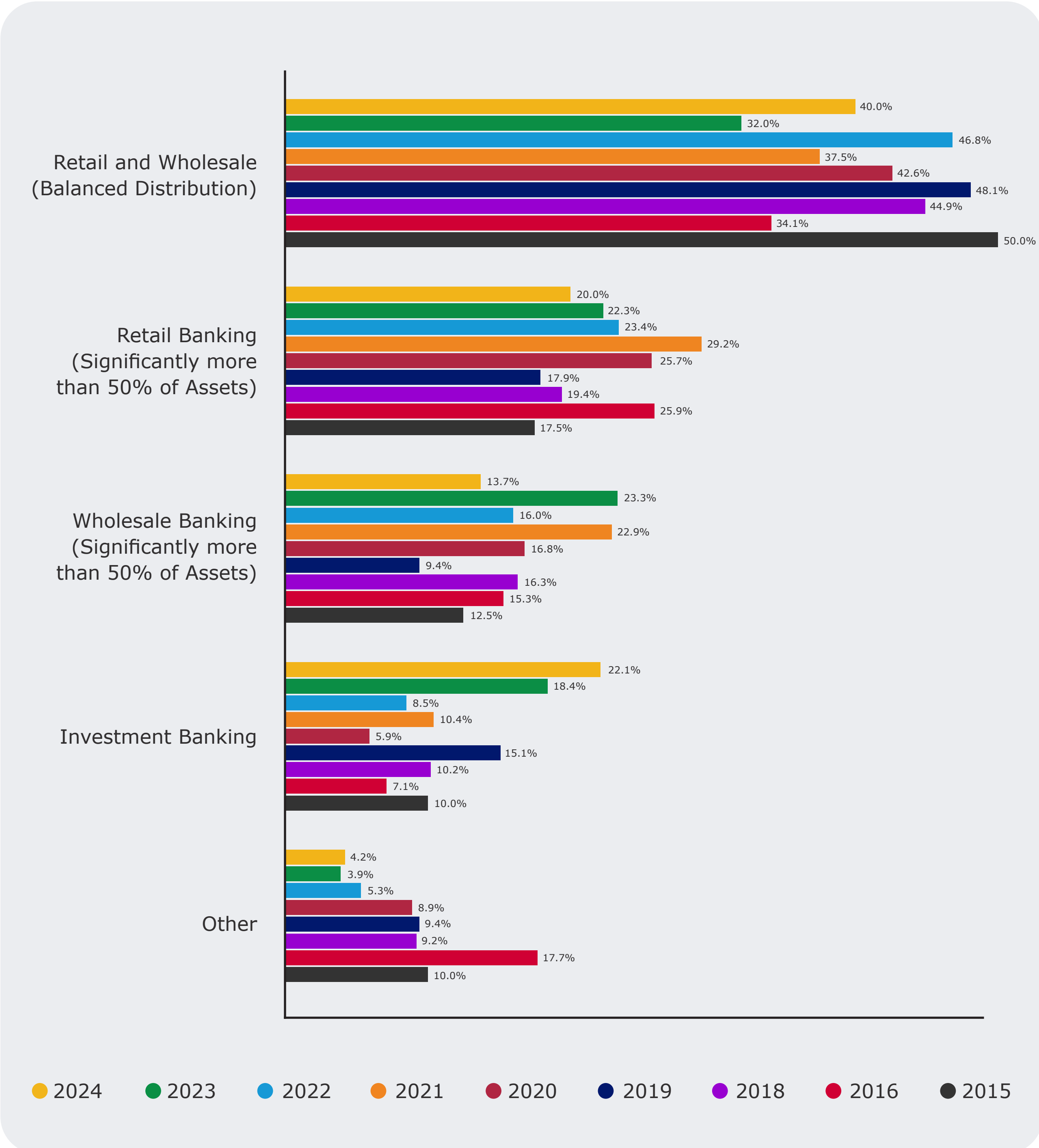
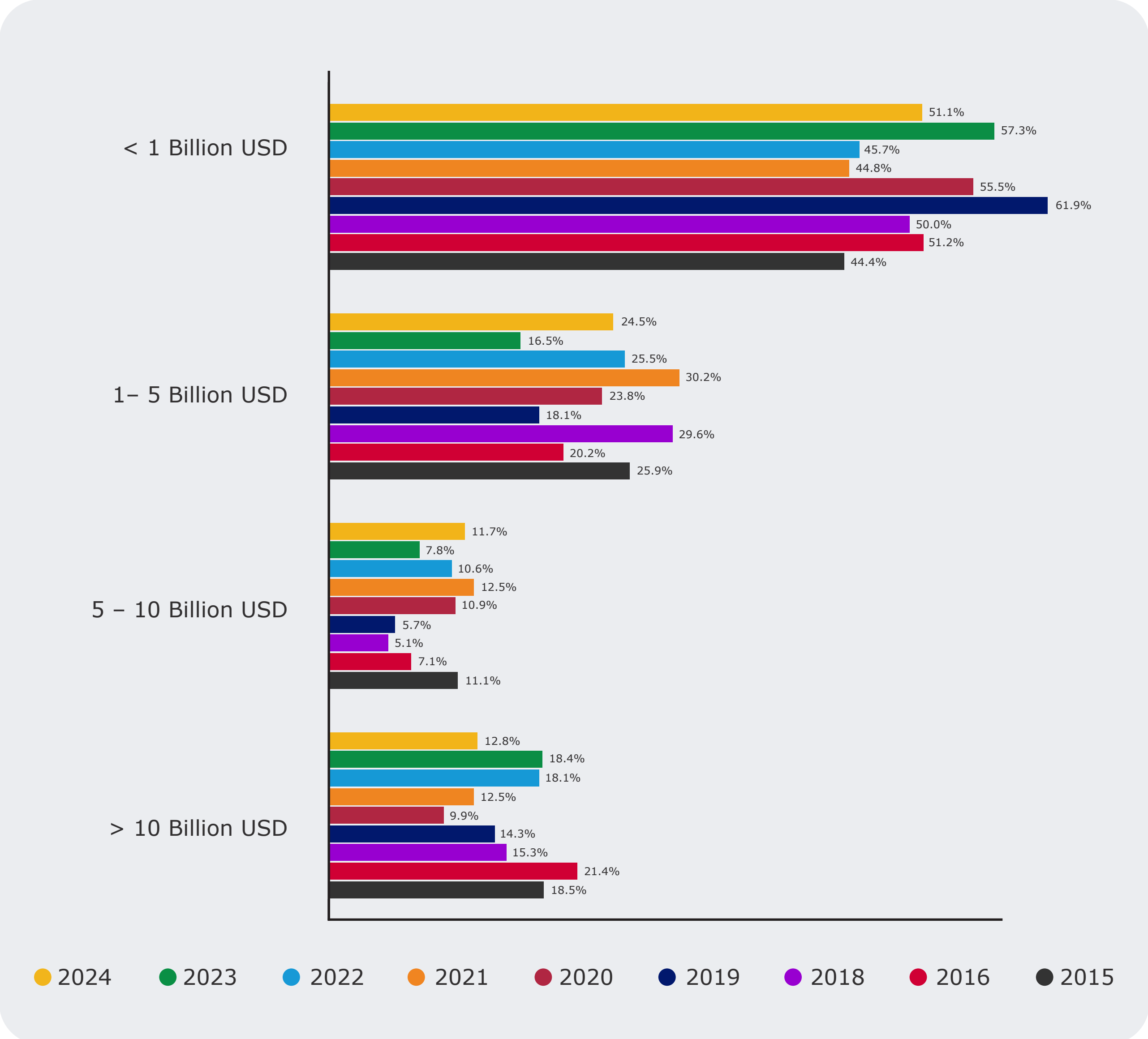


Figure 3. Size of Total Islamic Assets



Compared with the previous year, changes were observed in the composition of the survey respondents. Notably, the proportion of Islamic bank subsidiaries of conventional groups increased, while the number of respondents representing Islamic banking windows declined. Furthermore, there was an increase in respondents focused on a balanced distribution of retail and wholesale banking, as well as those primarily focused on investment. Conversely, the number of respondents primarily focused on wholesale banking and primarily on retail banking decreased. In terms of bank size, there was a decrease in respondents with total assets of less than one billion USD and total assets above ten billion USD, while the number of participants with total assets between one and ten billion USD increased. However, it is worth noting that these changes may be attributed to the sample rather than indicative of broader industry trends.

The outcomes presented in this report were derived from a questionnaire distributed online to the offices of chief executive officers (CEOs) of both CIBAFI's member and non-member financial institutions in mid-December 2022. The final responses were collected by June 2024. Consequently, the analysis reflects the viewpoints of the Islamic banking community towards the beginning of 2024 and the beginning of the second quarter of 2024. Consistent with previous years, the survey included both "closed" and "open-ended" questions, providing industry leaders with the opportunity to provide detailed and nuanced written feedback to express their observations.

It is our hope that this report will shed light through its various sections on the perspectives of Islamic banking executives towards the future of the industry, specifically on the practices and emerging trends of Islamic social finance.

PART I:

CIBAFI ISLAMIC BANKING CONFIDENCE INDEX

Part 1. CIBAFI Islamic Banking Confidence Index

The CIBAFI Islamic Banking Confidence Index is a permanent part of the GIBS report aiming to assess the level of confidence of Islamic bankers in the future of the industry on a yearly basis. It determines the key concerns facing Islamic banks in upcoming years and outlines the strategic initiatives taken in response. Over the past eight years, the index provided pertinent results on the industry's growth dynamics, identifying key development areas, both globally and within the contexts of jurisdictions in various regions.

Optimism Levels for Islamic Banking Growth

The first section of the confidence index covers the optimism of Islamic banking executives towards the future of the industry and its revenue growth. Respondents were asked to rank their optimism levels from a scale of 1.0 to 5.0, where 1.0 indicates extreme pessimism and 5.0 indicates extreme optimism.

The global optimism level for the banking sector remains unchanged from 2023.

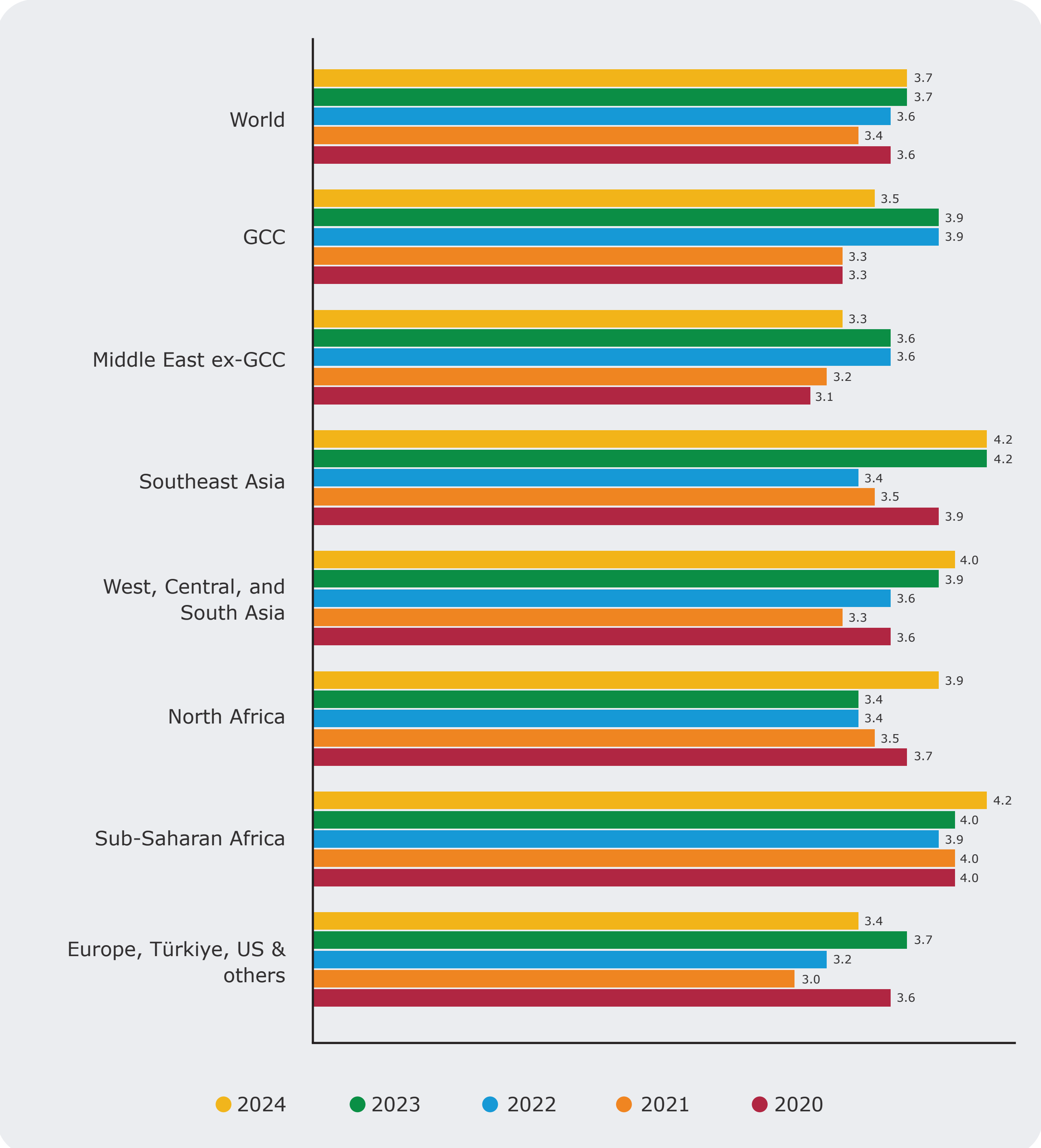
A stable optimism level for the future of banking

The findings of this year's survey suggest a stable optimism level towards the future of the banking sector, with a reported global score of 3.7 in 2024. This unchanged score compared to 2023 indicates a stable optimistic view for the future of the industry despite global challenges.

On a regional level, many regions experienced an increase in their optimism level towards the future of banking compared to 2023. The West, Central, and South Asia, North Africa and Sub-Saharan Africa regions all reported a noteworthy increase in optimism levels, with scores of 4, 3.9 and 4.2, respectively in 2024 compared to 3.9, 3.4 and 4.0 in 2023. Southeast Asia reported a score of 4.2, the same score as 2023.

On the other hand, GCC, Middle East ex-GCC and, Europe and Türkiye, US & Others experienced a slight decrease in the optimism level towards the future of banking compared to 2023, with scores of 3.5, 3.3 and 3.4 respectively in 2024 compared to 3.9, 3.6 and 3.7 in 2023.

Figure 4. Overall Banking Industry Optimism Level



The perception of the future of Islamic banking remains unchanged from the last two years

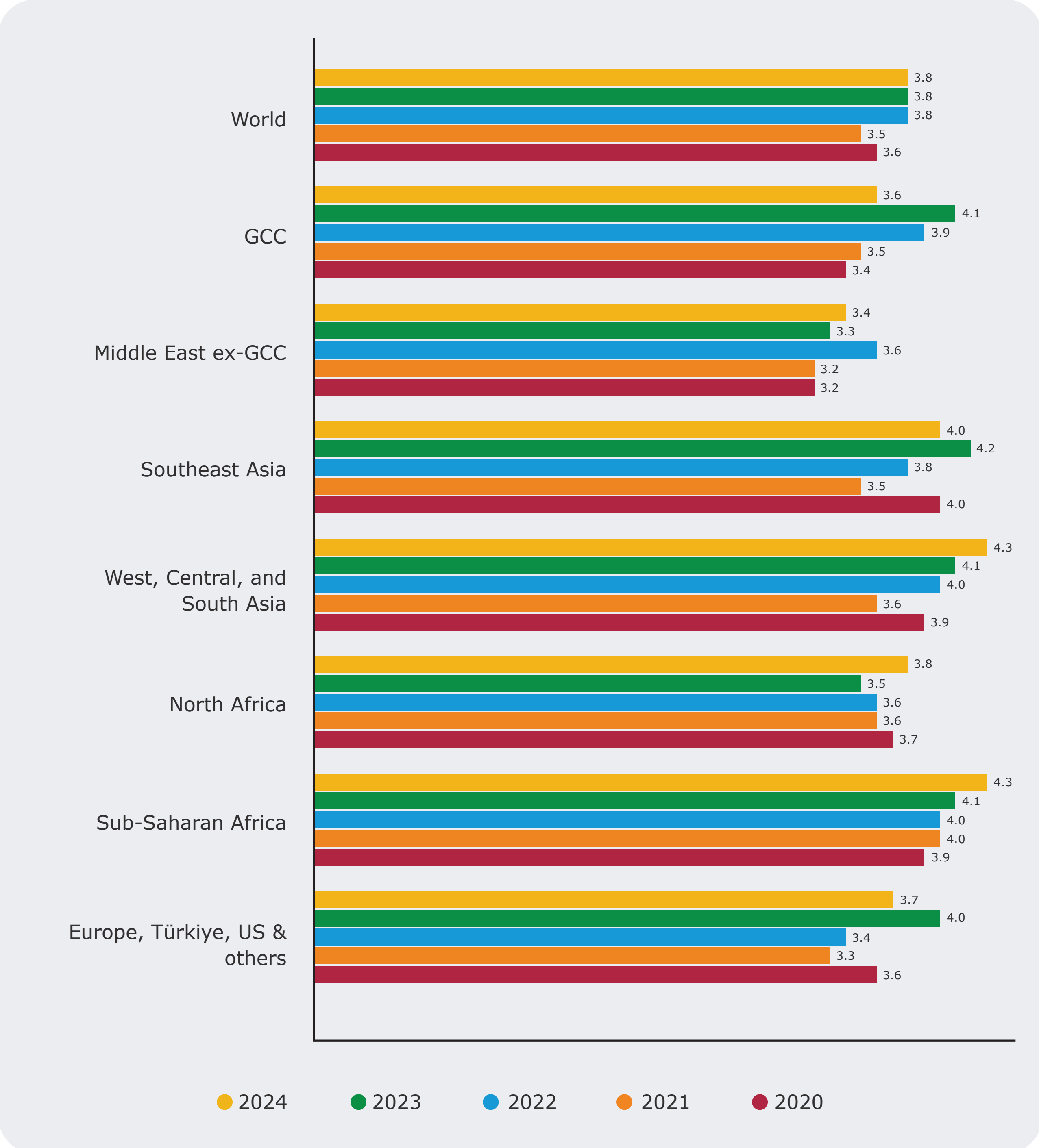
The future outlook for Islamic banking remains positive, with the global optimism score holding steady at 3.8 in 2024, the highest reported across the overall banking industry and consistent with the previous two years. This sustained optimism among Islamic bankers can be attributed to several factors, including favourable economic indicators in many countries with Islamic finance.

Although the global score remained unchanged, there were noticeable changes in optimism across regions. Several regions recorded a decline in optimism levels. The GCC, Europe and Türkiye, the US & Others, and Southeast Asia reported a decrease, with scores of 3.6, 3.7 and 4 in 2024 compared to 4.1, 4 and 4.2 in 2023, respectively. These declines could be attributed to uncertainties due to geopolitical conflicts directly affecting some regions and economic challenges such as inflation faced by certain countries. Despite these declines, the overall view remains positive.

Conversely, Sub-Saharan Africa, North Africa, the Middle East ex-GCC, and West, Central, and South Asia reported slight increases in their optimism for the future of Islamic banking.

The global optimism score for Islamic banking remains steady at 3.8, the highest in the overall banking industry and consistent with the previous two years.

Figure 5. Islamic Banking Industry Optimism Level



Slight Increase in optimism for Islamic Banks' revenue growth compared to conventional counterparts

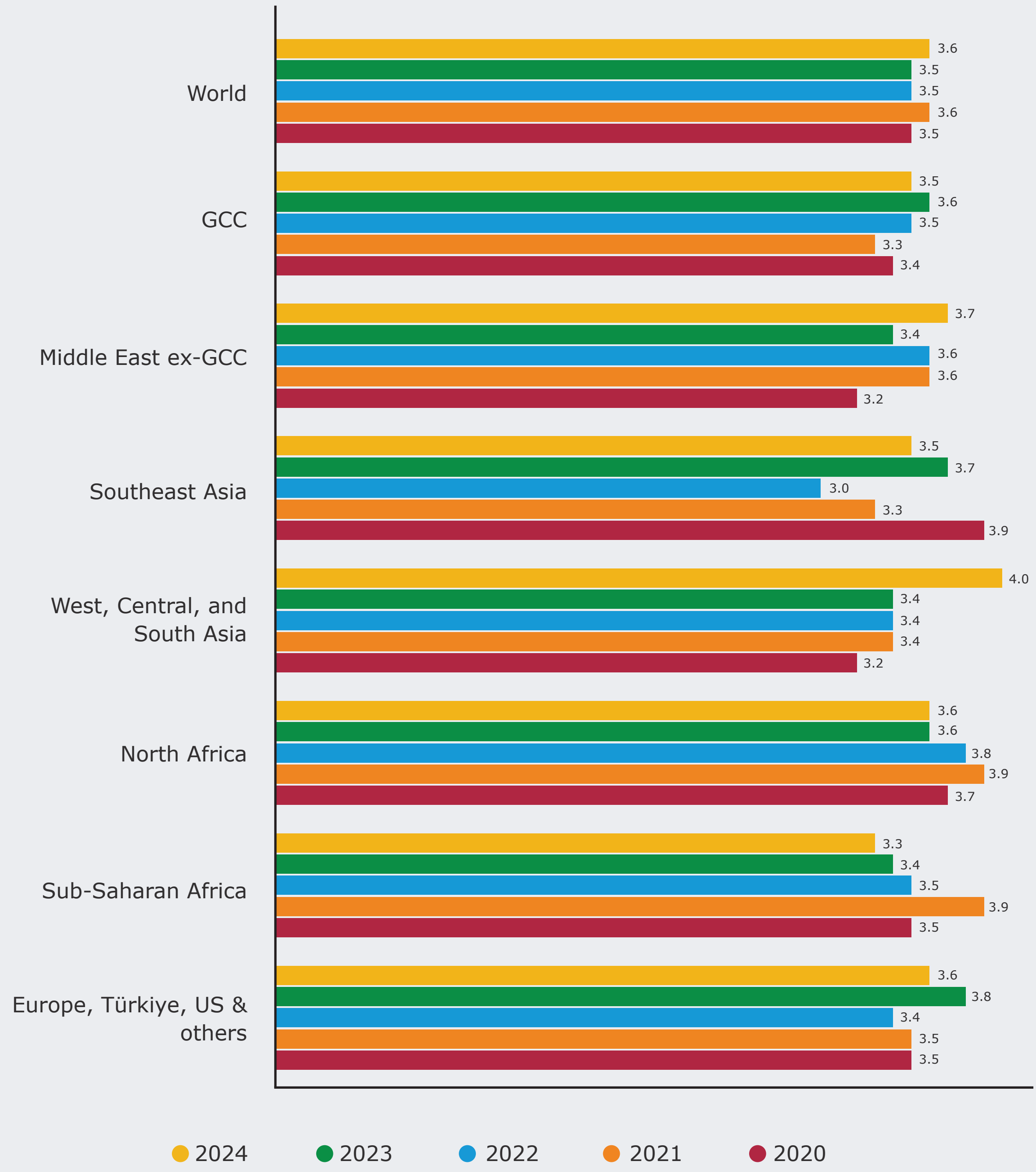
Optimism about revenue growth compared to conventional banks rose slightly in 2024, the highest score recorded over several years.

The optimism of respondents regarding their revenue growth compared to conventional counterparts experienced a slight increase in 2024, with a score of 3.6 compared to 3.5 in 2023. This is the highest score recorded over the years, occurring three times: in 2019, 2021, and this year. This supports the assumption made in last year's report that this high score could be due to a sampling effect across years or may reflect Islamic banks' perceptions of better performance in times of market turbulence. This year is also characterised by geopolitical conflicts and uncertainties. Despite these challenges, Islamic banks maintain a positive outlook on their revenue growth potential.

From a regional perspective, optimism levels for revenue growth showed both increases and decreases. The most significant increase was in the West, Central, and South Asia region, which recorded a score of 4 in 2024, up from 3.4 in 2023. This was followed by the Middle East ex-GCC, which scored 3.7 in 2024, compared to 3.4 in 2023. North Africa maintained the same score as last year.

Conversely, four regions showed a decrease in optimism for revenue growth: the GCC, Sub-Saharan Africa, Europe and Türkiye, US & Others, and Southeast Asia, with scores of 3.5, 3.3, 3.6, and 3.5 in 2024, respectively, compared to 3.6, 3.4, 3.8, and 3.7 in 2023. This could reflect the economic and political conditions in these regions or the nascent development of Islamic finance in some jurisdictions within these regions.

Figure 6. Expectations of Islamic Banking Revenue Growth Compared to Conventional Banking



Islamic Banking Concerns for the Upcoming Years: A Global Perspective

The second section of the confidence index highlights the key concerns of Islamic banking executives for the upcoming years. The survey provided Islamic banking leaders with a list of 25 potential challenges and asked them to rate the severity of each challenge their institution might face in the next one to three years. The scores ranged from 1.0 to 5.0, with 1.0 indicating "not at all important" and 5.0 indicating "extremely important."

This year's results reveal many of the same concerns reported in the previous year, although most concerns have continued to decline in severity. This may suggest that banks are becoming more adept at adapting to and managing these challenges.

Information technology remains the foremost challenge for Islamic banks in the future

Information technology continues to be a major concern for Islamic banks. The focus is on balancing technological advancements with operational and cybersecurity challenges.

In today's rapidly evolving landscape, the banking industry is at the forefront of disruptions from cutting-edge technologies like generative AI to redefine customer experiences and operational efficiencies. These advancements bring immense potential for innovation and optimisation within financial institutions. However, they also introduce new complexities and challenges, particularly in the automation of operations and cybersecurity. Balancing these challenges, Islamic banks and their counterparts must prioritise robust digital technology strategies to harness the transformative power of these technological trends while safeguarding against any challenges.

The score of information technology saw a slight decrease from 4.3 in 2023 to 4.2 in 2024, yet it continues to remain a critical priority for banks aiming to maintain leadership amidst technological advancements and manage any related challenges.

Rising concerns over meeting shareholder expectations in a dynamic market

In an era of evolving market dynamics, Islamic banks must navigate the complex terrain of meeting shareholder expectations while ensuring sustainable growth and profitability. The focus on shareholder value necessitates a strategic balance between delivering consistent financial performance and aligning with the ethical and social principles inherent in Islamic banking.

Shareholders’ value and expectations share the top position with information technology as a primary concern this year, with a score of 4.2 compared to 4.1 in 2023. This increase reflects the growing emphasis on addressing this concern.

Attracting and retaining consumers will remain a central focus for Islamic banks

While still a priority, the severity of consumer attraction and retention concerns has decreased slightly. This indicates a reduction in urgency but still highlights the need for effective strategies in a changing market.

Consumer attraction, relations, and retention remain a top priority for Islamic banks, even as the perceived severity of this challenge has slightly diminished. The score has decreased from 4.4 in 2022 to 4.3 in 2023, and now stands at 4.1.

This gradual decline reflects a modest reduction in the urgency of addressing consumer attraction, relations, and retention. However, the need for robust strategies in this area remains critical. Emerging technologies such as generative AI, industry convergence, embedded finance, open data, and digitisation of money are fundamentally transforming how banks operate and address customer needs. As these innovations advance, their influence will intensify, necessitating continuous adaptation and innovation from banks.

Islamic banks must persist in evolving their approaches to meet changing consumer expectations while striving for sustainable growth and profitability. Maintaining a focus on these areas is essential for sustaining a competitive edge and ensuring long-term success in a dynamic market landscape.

Addressing risk management challenges: a core concern for Islamic banks

Risk management remains a prominent concern for Islamic banks in the coming years. Although the severity of this issue has seen a slight decrease, with the score shifting from 4.2 in 2023 to 4.1 in 2024, it continues to demand significant attention.

The year 2024 is characterised by a set of challenges for financial institutions, including compliance risks, interest rate fluctuations, credit instability, AI-enhanced fraud, and geopolitical shocks. The rising frequency of unexpected events, often termed "unknown unknowns," compounds these challenges and underscores the complexity of effective risk management. In this context, a proactive and strategic approach is essential. Islamic banks must develop and implement robust risk management frameworks to navigate these multifaceted threats successfully.

Prioritising human resources and talent development in Islamic banking

Human resources and talent development remain a significant focus for Islamic banks. Although the score has slightly decreased from 4.2 in 2023 to 4.1 in 2024, its ranking among the top concerns has risen.

The rapidly changing environment and diverse challenges underscore the need to prioritise workforce development to stay competitive and effectively address these issues. The human resources landscape is shaped by several factors, including the demand for specialised skills in emerging technologies, evolving regulatory requirements, and shifting market dynamics. The responses emphasise that investing in talent development and cultivating a strong organisational culture are crucial for maintaining operational excellence and achieving strategic goals.

Responding to global economic shifts is a focus for Islamic banks

The macro-economic environment continues to be a significant issue. This highlights ongoing concerns about global inflation, trade disruptions, and geopolitical tensions.

The macro-economic environment remains a top concern for Islamic banks, although its severity has slightly decreased, with the score moving from 4.2 in 2023 to 4.0 in 2024. This shift also reflects a drop in its placement among the top concerns compared to the previous year.

Despite this decrease in urgency, the macro-economic landscape continues to present significant challenges. A slowing global economy coupled with a divergent economic landscape will test the banking industry. While recent efforts to combat inflation are showing signs of success in many countries, risks from supply chain disruptions, rewiring of trade relationships, and ongoing geopolitical tensions may complicate global economic growth. Additionally, extreme weather-related events, such as floods and earthquakes, could cause severe economic disruption.

Islamic banks must adapt their strategies to effectively address evolving macroeconomic challenges, such as global inflation, interest rates, and geopolitical changes. Staying informed about global economic trends, adjusting financial models, and implementing risk mitigation measures are essential for maintaining stability and growth. By focusing on these areas, Islamic banks can manage the impacts of economic changes and sustain their competitive edge in a dynamic financial environment.

Strategic focus on sustaining AML/CFT compliance and growth in Islamic banking

In 2024, Islamic banks maintain a steadfast focus on two critical areas: the implementation of AML/CFT (Anti-Money Laundering/Counter Financing of Terrorism) regulations and business growth and expansion. Both areas have consistently scored 4.0 in 2023 and 2024, underscoring their ongoing importance.

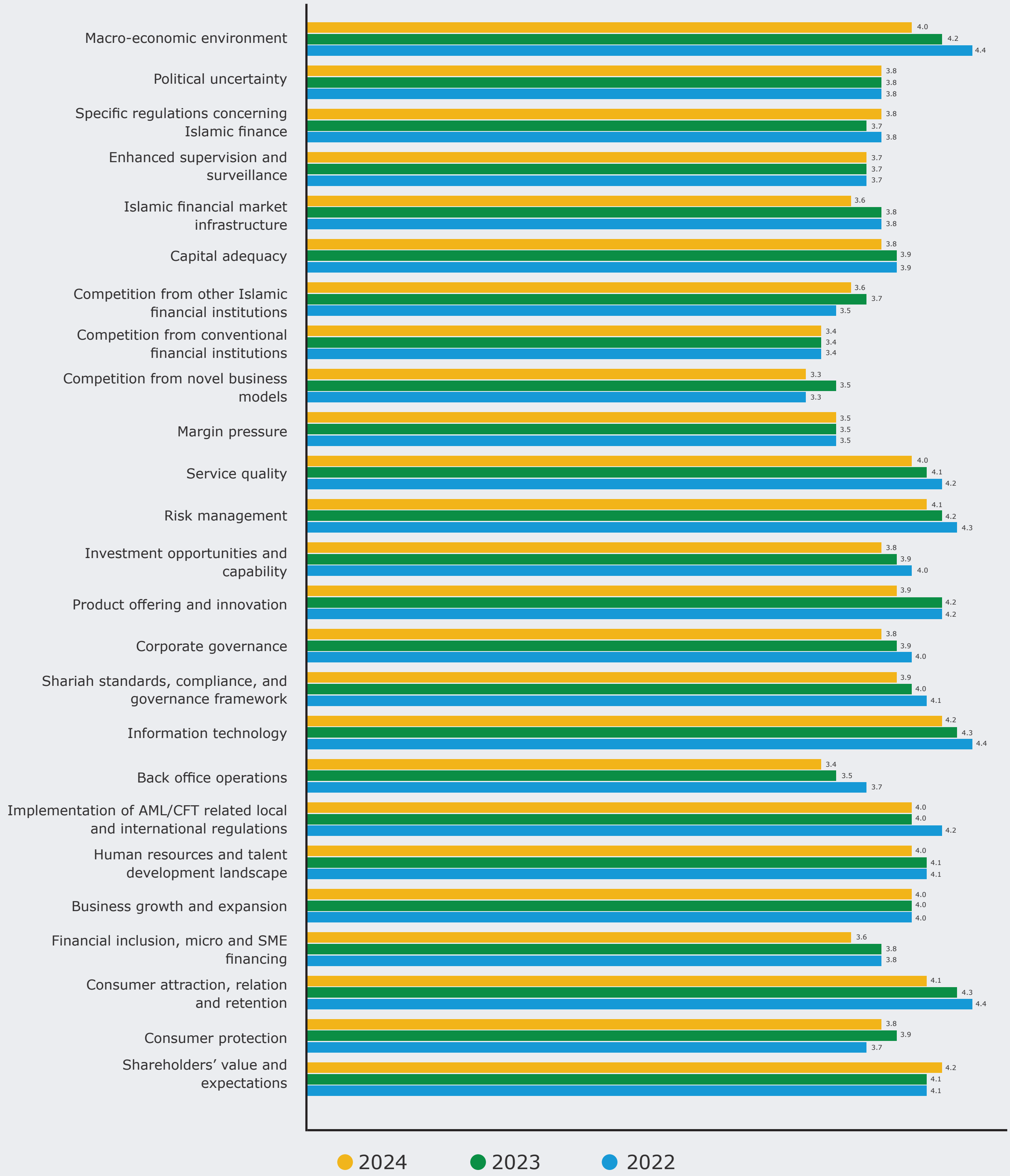
The persistent score for AML/CFT regulations reflects the banks' commitment to adhering to stringent compliance standards, which are vital for preventing financial crimes and ensuring regulatory integrity. Similarly, the steady score for business growth and expansion indicates a continued emphasis on exploring new opportunities and broadening market presence, essential for long-term success and resilience.

Islamic banks must carefully balance these priorities by upholding rigorous AML/CFT compliance amid rising financial crime concerns while also pursuing strategic growth initiatives. Managing these areas effectively is crucial for navigating the complexities of the financial landscape and achieving sustainable development.

Decreasing concerns in Islamic banking

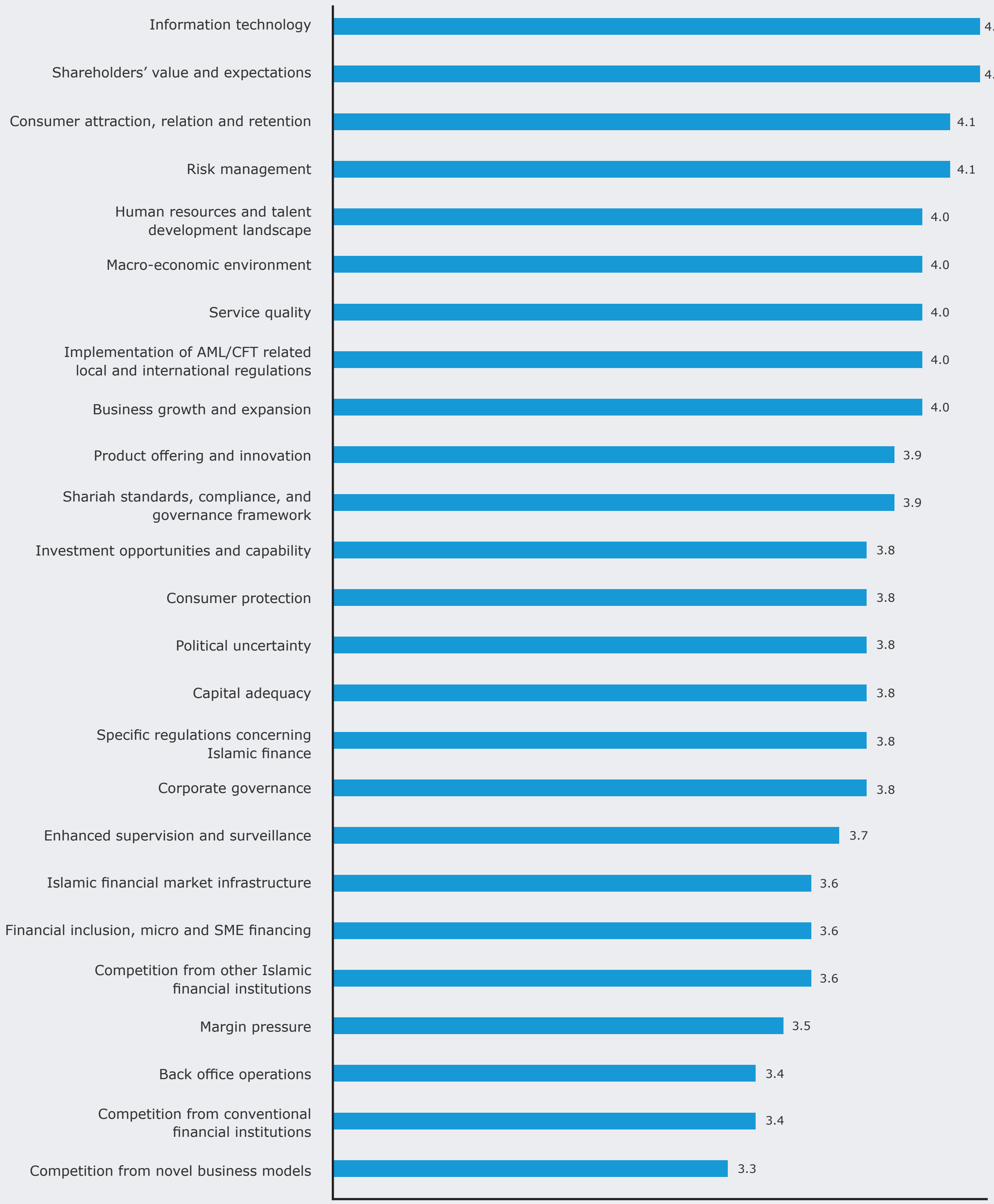
Looking at the lower end of the list of concerns, the reduction in the severity of certain issues compared to the previous year suggests that banks are becoming more adept at addressing these challenges. For instance, financial inclusion, micro, and SME financing scored 3.8 in 2023, but this year it has decreased to 3.6. Another concern that has seen a decrease in severity is Islamic financial market infrastructure, which scored 3.4 in 2024 compared to 3.6 in 2023. Additionally, Islamic banks are less concerned about competition from novel business models, as reflected in this year's scores compared to last year.

Figure 7. Global Islamic Banking Top Concerns



1: Extremely unimportant; 2: Not important; 3: Fairly important; 4: Very important; 5: Extremely important

Figure 8. Global Islamic Banking Top Concerns (2024)



1: Extremely unimportant; 2: Not important; 3: Fairly important; 4: Very important; 5: Extremely important

Regional Concern Variations

In addition to reporting Islamic banking concerns from a global perspective, it is important to recognise the differences that may arise based on specific regional conditions. Thus, this section outlines concerns specific to each region. Many of these regional concerns align with global issues, although the underlying causes may differ across regions.

There are common global concerns but also different regional priorities.

Across all regions, banks face unique challenges but share common concerns, particularly in information technology and human resources. Notably, the top four global concerns are absent from the list of primary concerns in the GCC. This could be attributed to the development level of banks in this region concerning technology adoption and customer attraction. It is also important to note that while banks are prioritising other issues, the significance of concerns such as information technology and consumer matters remains significant.

In terms of common concerns, a bank from the Middle East ex-GCC said: "The rapid advancement of information technology and the growing demand for digital banking require significant investments in technological infrastructure." A bank from Europe, Turkey, the US, and other regions highlighted the crucial role of information technology in enhancing customer satisfaction and providing a competitive advantage. Another bank from the same region linked IT concerns to new technologies, fintech, and new entrants to the sector. A bank remarked: "Besides IT infrastructure development, retaining the best talent will be a core issue for the bank." Similarly, a bank from West, Central, and South Asia mentioned that the lack of trained staff is critical for Shariah compliance. Another bank from Sub-Saharan Africa emphasised the importance of both technology and human resources.

Consumer-related concerns across different regions focus heavily on improving customer experience, leveraging technology to meet customer needs, and maintaining strong relationships. A bank from the Middle East ex-GCC said: "The banking sector generally restored consumer trust after there was a significant gap between banks and consumers." Another bank from the same region said: "The bank faces many concerns regarding attracting customers, building strong relationships, and maintaining them." In a similar vein, a bank from Sub-Saharan Africa noted the challenge of meeting consumer expectations and keeping up with evolving needs.

Concerns about macroeconomic conditions and political instability, particularly in the Middle East ex-GCC and North Africa, affect investment opportunities and banking operations.

Banks across diverse regions express significant concerns about macroeconomic and political instability. These factors are seen as having wide-ranging impacts on the banking sector and the broader economy.

A bank from the Middle East ex-GCC region articulated this concern succinctly:

"Macroeconomic environment and political instability are the most significant concerns facing our bank and the local banking sector in general, due to the negative repercussions of these conditions on the economy as a whole and banking in particular, which limit investment opportunities, increase uncertainty, and raise risk."

Another institution from the same region reported facing multiple global shocks, citing challenges related to foreign exchange, high inflation rates, higher interest rates, and import restrictions. These factors, the bank noted, directly affect its banking activities and operations.

Similar sentiments were echoed by banks in North Africa. One institution identified the macroeconomic environment and political instability as its top concerns. Another bank from the region emphasized: "One of the most important concerns is political instability, which affects economic development and, consequently, the profitability of the bank."

These statements highlight the interconnected nature of macroeconomic conditions, political stability, and banking sector performance across different regions.

Margin pressure was also highlighted by banks in certain regions as a top concern. For instance, a bank from the GCC said: "Generally, Islamic banks will always experience margin pressure compared to conventional banks." Likewise, a bank from North Africa said: "Islamic banks struggle with return margin risk because they cannot raise profit margins if payments are delayed, unlike traditional banks, especially with recent payment extension rules from the Central Bank."

Table 2. Major Concerns of Islamic Banks across Regions[1]

Group	Top Concerns	Score
Group 1 GCC	Service quality Human resources and talent development landscape Business growth and expansion	4.5 4.2 4.2
Group 2 Middle East ex-GCC	Information technology Macro-economic environment Implementation of AML/CFT related local and international regulations	4.2 4.2 4.1
Group 3 Southeast Asia	Information technology Corporate governance Human resources and talent development landscape Shareholders' value and expectations Consumer attraction, relation and retention Shariah standards, compliance, and governance framework	4.8 4.6 4.5 4.5 4.5 4.5
Group 4 West, Central, and South Asia	Shareholders' value and expectations Human resources and talent development landscape Consumer attraction, relation and retention Business growth and expansion	4.2 4.1 4.1 4.1
Group 5 North Africa	Consumer attraction, relation and retention Shareholders' value and expectations Product offering and innovation	4.4 4.4 4.3
Group 6 Sub-Saharan Africa	Consumer attraction, relation and retention Human resources and talent development landscape Shareholders' value and expectations Risk management Macro-economic environment Information technology Business growth and expansion Implementation of AML/CFT related local and international regulations Financial inclusion, micro and SME financing	4.0 4.0 3.8 3.8 3.8 3.8 3.8 3.8 3.8
Group 7 Europe, Türkiye, US & Others	Information technology Shareholders' value and expectations Shariah standards, compliance, and governance framework	4.7 4.6 4.4
Global	Information technology Shareholders' value and expectations Consumer attraction, relation and retention Risk management	4.2 4.2 4.1 4.1

1: Extremely unimportant; 2: Not important; 3: Fairly important;
4: Very important; 5: Extremely important

[1] For every group, the top three concerns are identified, including all concerns with the same score, even if that means that more than three are listed in total.

Strategies Adopted by Islamic Banks to Overcome Top Concerns

To further explore how Islamic banks are addressing the concerns, the survey asked respondents to expand on the steps and strategies taken to overcome the challenges reported. The responses covered different aspects and initiatives, which we outline below.

Initiatives to address information technology concerns

Islamic banks are addressing IT concerns by investing in technological advancements, upgrading infrastructure, adopting AI, and enhancing cybersecurity. They are also exploring fintech and diversifying into new business areas to maintain competitiveness.

As a major concern globally, banks provided several deployed strategies to overcome challenges associated with IT. This includes investments in technological advancements and improving banks' operations. A bank from Middle East ex-GCC said:" Bank used advanced technology to improve banking operations and facilitate communication with customers. For example, using smart banking apps and self-support services to deliver a seamless customer experience".

Another bank stated: "The rapid advancement of information technology and the growing demand for digital banking require significant investments in technological infrastructure for banks.

Consequently, the bank is launching a promising digital transformation strategy to adapt to the rapid changes in fintech and deliver an excellent customer experience while maintaining the highest cybersecurity standards". A bank from West, Central, and South Asia highlighted the use of advanced technologies, such as AI, to assist customers with simple tasks like making payments, as well as employing tech-based services to automate and secure internal operations. Another bank from the same region highlighted a set of measures to manage the concerns related to IT and these include:

- Invest in upgrading and modernising IT infrastructure to ensure efficiency, security, and scalability.
- Implement robust data management and cybersecurity measures to protect sensitive information.
- Foster a culture of continuous learning and development to keep up with technological advancements.
- Explore emerging technologies such as artificial intelligence and automation to streamline processes.

A bank from Sus-Saharan Africa said:" The bank is diversifying into a holding company with fintech as one of its subsidiaries, in order to capitalise on business opportunities and address competition".

Strategic adaptations of Islamic banks to political and economic instability

In response to global challenges faced by many jurisdictions, banks have adopted strategies to adapt to disruptions affecting the macroeconomic environment and mitigate potential risks from political instability. In this context, a bank from the Middle East outside the GCC stated, "Political stability is fundamental to economic stability, creating a safe and stable working environment and allowing for the development of strategic plans for the medium and long term without significant deviations from expectations. This type of uncertainty is a major concern for countries experiencing political and social conflicts." To address these challenges, the bank added, "We prepare and review three-year strategic plans and an estimated one-year budget at the end of each fiscal year, analysing completion ratios to develop strategies for the following year."

Another bank from the same region mentioned implementing various measures to tackle macroeconomic challenges, such as focusing on financing promising economic activities, ensuring safe investments with high credit quality, and expanding digital services to attract more customers. The bank is also significantly funding SMEs, co-financing national projects to support development and reduce unemployment, and increasing zakat resources to aid those affected by current economic conditions. A bank from the GCC commented, "Management is pushing for local market outperformance through expansion strategies to ensure that the USD return on investment is not significantly impacted by economic or political instability."

Strategic initiatives for enhancing human capital in Islamic banking

Islamic banks across different regions have highlighted the importance of human resources. A bank from Middle East ex-GCC shared several actions including:

- Promote the training and continuous development of employees to enhance their skills and knowledge in relevant areas.
- Invest in online and distance learning programs to provide continuous learning opportunities for employees.
- Encourage the organisation's learning culture by supporting employee participation in training courses, workshops, and knowledge-sharing activities.
- Forge partnerships with universities and educational institutions to develop tailored educational programs that meet the bank's needs and cultivate the necessary skills for the banking industry.
- Use technology effectively to facilitate recruitment processes and select employees with the required skills.
- Develop specific training programs aimed at cultivating skills needed for the banking industry and its new technologies.
- Foster a culture of innovation and development within the bank to encourage employees to expand their skills and explore new ideas.
- Provide leadership support and career development programs for promising employees to enhance the bank's leadership capabilities.

Additionally, a bank from Sub-Saharan Africa said:" The Bank is establishing an academy and will collaborate with leading Islamic finance training Organisations in order to produce enough professionals for the Bank and Industry at large".

Strategies for handling customer issues in Islamic banking

Banks are enhancing services, personalising interactions, and investing in security to address customer concerns, while focusing on innovation and adapting to evolving needs.

Customer concerns are a major issue for Islamic banks. Due to their importance, banks have implemented various initiatives and strategies to manage related challenges. Understanding customer needs is the first step towards addressing them. In this context, a bank from Sub-Saharan Africa stated that one of its strategies to manage customer concerns is to conduct surveys to measure client satisfaction and identify their needs.

Additionally, the bank is developing a CRM system to improve customer communication and provide customised services. Another bank from West, Central, and South Asia is focusing on strengthening customer relationships through personalised experiences and excellent customer service. Additionally, a bank from Middle East ex-GCC said: "The banking sector has generally restored customer trust through modern and innovative services and streamlined techniques and procedures. However, any emergency can still disrupt this relationship, causing lingering effects even after the issues are resolved".
Another bank from the same region highlighted the following actions that consist of multiple aspects to improve the relationship with customers:

- Providing a premium customer experience: The bank provides innovative and flexible services that meet customers' expectations and contribute to improving their overall experience.
- Focus on Personal Service: The bank has worked to strengthen the relationship with customers by providing a unique personal service and responding quickly to their individual needs and requirements.
- Enhancing Trust and Security: Invest in security and privacy technologies and provide strong safeguards to protect customers' data.
- Customer Listening: The bank's communication channels are open to customer feedback and demands and utilise them to improve its services.
- Training and Employee Empowerment: The bank's team is an important factor in building strong relationships with customers. The bank provided appropriate training for employees to enhance their communication skills and provide quality service.
- Innovation and continuous development: The bank is ready to adapt to changes in customer needs and the banking sector in general. This can be achieved by investing in research and development and applying new and innovative ideas.

By implementing these strategies, Islamic banks are proactively addressing major concerns, enhancing their operations and services, and driving sustainable growth.

PART II:

CIBAFI
Islamic Banking
Risk Dashboard

Part II. CIBAFI Islamic Banking Risk Dashboard

The CIBAFI Islamic Banking Risk Dashboard continues to offer a unique perspective on the potential risks Islamic banks might face over the next one to three years. This dashboard remains a crucial tool for assessing the challenges that banks encounter globally and regionally, tracking their evolution over time. While the Islamic Banking Top Concerns in Part I address global issues within their respective environments, the Islamic Banking Risk Dashboard focuses primarily on operational risks faced by banks. Political, macroeconomic, and other broad risks have been excluded to better understand the operational risks impacting banks in the coming years.

Each bank was requested to score 22 categories of risks on a scale from 1.0 (no risk at all) to 5.0 (extreme risk). The risk dimensions remain consistent with previous years to maintain comparability.

Islamic Banks' Global Top Risks

The 2024 survey indicates that Islamic banks are confident in their ability to manage risks, with most risks showing no increase in severity. This confidence is observed consistently across global and regional contexts, highlighting the sector's resilience amidst increasingly complex economic conditions worldwide. However, it is important to consider that this perceived stability may also reflect an underestimation of certain risks. While some risks have slightly increased and others decreased, these shifts suggest that Islamic banks are adapting their risk management approaches to align with current market challenges and opportunities. Nonetheless, a cautious approach is necessary to ensure that emerging risks are not overlooked.

Islamic banks remain confident in their risk management abilities, with most risks showing no increase in severity.

Technological risks at the forefront

This year, technology-related risks have once again emerged as the primary concerns for Islamic banks, maintaining their top position on the risk dashboard. Cybersecurity risk was ranked first, scoring 3.7, followed closely by technology risk at 3.6 (see Figure 9). The banks continued their efforts to accelerate their digitalisation initiatives and online banking services after the COVID-19 pandemic, aiming to sustain operations and attract and retain customers. However, this rapid digital transformation has also brought about significant operational and technological challenges, particularly heightened cybersecurity risks associated with the integration and deployment of new systems. As technology continues to advance and customer expectations rise, concerns related to technology and cybersecurity are expected to remain paramount for banks striving to enhance customer engagement and stay competitive.

Some banks have expressed concerns about increasing technology risks. A bank from GCC stated that "With the banking sector becoming increasingly dependent on modern technology, technology risks may become one of the most important challenges to its stability and growth, for example, service outages, data loss, disruption of banking operations, cybersecurity violations involving cyberattacks and data penetration, wire fraud or, for example, the Bank's inability to adapt to new technological developments which could result in the Bank losing market competitiveness." The Bank further added "To mitigate these risks, more investment has been made in cybersecurity solutions to detect and respond to threats in real time. Stronger data encryption has been implemented and training is provided to staff on best cybersecurity practices and emerging technology to reduce human error, which is an important source of technology risk."

A bank from the North Africa region outlined a comprehensive approach to mitigating cybersecurity risks. Their strategy encompasses several key components:

i. Governance: Implementation of strong cybersecurity governance, including a specific security policy, controls, operations, administrative supervision, and periodic reporting.
ii. Risk Analysis: Systematic identification and assessment of threats and vulnerabilities.
iii. Staff Training: Continuous awareness-raising and training programs for staff on best Internet security practices.
iv. Technical Defenses: Enhancement of technical safeguards through measures such as:
    - Encryption of sensitive data
    - Multi-factor authentication
    - Firewalls
    - Intrusion detection systems

v. Security Testing: Regular security audits, penetration tests, and attack simulations, followed by remediation of identified gaps.
vi. Continuous Monitoring: Ongoing surveillance of the technological environment to detect new threats and adapt defenses accordingly.

This multi-faceted approach demonstrates the bank's commitment to maintaining a robust cybersecurity posture in the face of evolving digital threats.

Cybersecurity and technology risks are top concerns for Islamic banks, leading to heightened investment in security and staff training.

Slight increase in credit risk

With a slight increase, credit risk has resurfaced as a second top concerning risk for Islamic banks this year, ranking second on the risk dashboard alongside technology risk. In 2023, the credit risk score was 3.5, while this year that number increased to 3.6. The looming threat of a global economic slowdown, the Russia-Ukraine conflict, the political instability in some regions, and rising inflation rates are all making it more difficult for borrowers to meet their debt obligations. Consequently, Islamic banks are facing increased risks of non-performing debts and non-payment, making credit risk a significant focus for the upcoming years. A bank in the GCC region expressed concerns and stated that "Credit risk remains a top priority for Bank and counterparty-credit-risk management is becoming more challenging and complex, reflecting a disrupted global economic, political, and regulatory environment, together with historically high levels of volatility. The Bank aims to further enhance the credit selection/due diligence/governance criteria of customers to minimise non-performing financing that leads to lowering credit risk."

Another bank from the Middle East ex-GCC region highlighted its strategy to mitigate credit risk, "The Bank has a flexible and renewable staffing and investment policy to accommodate changes in the surrounding environment that are supported by practical references that support detailed steps of application. The terms of credit include criteria for accepting and dealing with customers as long as they enjoy the facilities granted, as well as reliance on global credit risk measurement systems, creditworthiness assessments for clients, appropriate pricing policy for all of the above and adequacy. In all, the minimum acceptable risk tolerance threshold is set, and the exams of pressure on the portfolio are periodically examined within the framework of an accurate, graded risk retention policy and the unit approved by the Board of Directors under the supervision and consideration of the supervisory authority."

Similarly, a bank from West, Central, and South Asia shared several measures to mitigate credit risk, "The Bank's management has taken effective actions to mitigate credit risk that are: Strengthen credit assessment and underwriting processes to ensure thorough evaluation of borrowers' creditworthiness; Implement effective risk management systems and tools to monitor and manage credit exposures; Diversify the loan portfolio to reduce concentration risk and exposure to specific industries or sectors; Regularly review and update credit policies and procedures to align with changing market conditions and regulatory requirements; and Enhance collection and recovery processes to minimise potential losses from defaulting borrowers."

Credit risk has become a major concern for Islamic banks due to economic challenges and rising non-performing debts, prompting banks to enhance their credit assessment and risk management strategies.

Risk related to extreme disruptive events and climate change risk

This year there has been a slight increase in perceived risk related to extreme disruptive events, such as the COVID-19 pandemic. The score has increased from 3.3 in 2023 to 3.4 making it positioned as the third most concerned risk on the dashboard. Banks remain concerned about risks related to extreme disruptive events, such as the COVID-19 pandemic, even though the world has returned to normalcy with the reopening of businesses and economic activities. This ongoing concern perhaps stems from the recognition that such events can have severe and unpredictable impacts on financial stability, operational continuity, and customer trust. The COVID-19 pandemic highlighted vulnerabilities in global supply chains, digital infrastructures, and workforce management, making banks more aware of the need for robust contingency planning.

Climate change risk held steady at a score of 2.8 out of 5, unchanged from last year. While this score might suggest moderate concern, the open-ended responses tell a different story. Many Islamic banks are actually very aware of climate risks and are taking steps to address them.

For example, a bank from West, Central, and South Asia highlighted their vulnerability: "Our country faces real threats from climate change and extreme events. We're surrounded by sea, with limited land, making us especially at risk." This bank isn't just worrying - they're taking action. They're putting together a solid Business Continuity Plan and using cloud solutions to keep things running even if disaster strikes.

Other banks shared similar concerns and actions. It's clear that while the number hasn't changed, Islamic banks are far from complacent about climate risks. They're recognizing the threats and actively working on solutions to protect their operations and customers. A bank from Europe, Turkey, and the US region highlighted the significant role of regulatory and supervisory bodies in promoting sustainability and developing guidelines to mitigate climate change in the financial industry.

The bank reported that their regulator is gradually implementing practices such as climate change measurement, auditing, transparency requirements, and green asset ratio assessments. Specifically, the regulator recently published draft regulations on green asset ratios and guidance on the effective management of climate-related financial risks for banks. These guidelines are scheduled for implementation in 2025.

In response to these regulatory developments, financial institutions, including this bank, have accelerated their sustainability efforts. The bank emphasized the need to recruit personnel with expertise in sustainability to adapt to these changes. They noted that failure to take necessary precautions could result in difficulties complying with upcoming sector regulations. Consequently, the bank has initiated capacity development efforts related to sustainability.

This example illustrates how regulatory actions are driving concrete changes in banks' approaches to climate-related risks and sustainability, influencing both strategic planning and human resource development in the sector.

Foreign exchange risk remains significant

Foreign exchange risk remains in the top five concerns for Islamic banks, with a consistent score of 3.3 from last year. This is likely due to the ongoing state of the global economy and rising geopolitical risks in various regions, leading to increased market volatility and a “flight to safety” behaviour among international investors. These factors are putting pressure on foreign exchange rates. The fluctuation in foreign exchange rates can have adverse effects on banks’ asset returns and increase their vulnerability to other risks, including liquidity risk, transaction risk, credit risk, and inflation risk.

To address foreign exchange risk, banks are developing and implementing various strategies. For example, a bank from the West, Central, and South Asia region shared its approach: “[Bank] developed a comprehensive foreign exchange risk management strategy that includes hedging techniques and tools that monitor and analyse foreign exchange market trends to identify potential risks and opportunities; Establish clear guidelines and policies for managing foreign currency exposures; Consider using financial instruments such as forward contracts or options to hedge against currency fluctuations; Provide training and education to employees to ensure proper understanding and execution of risk management strategies.”

Similarly, a bank from North Africa shared its strategy for mitigating foreign exchange risk: “[Bank] reduce risks by strengthening the Bank’s financial position with respect to foreign exchange, retaining existing correspondents, and expanding the outreach by adding new correspondents according to clients’ trading heavyweights.”

Rise in misconduct and fraud risk

The increase in misconduct and fraud risk, due to new technological vulnerabilities, has led Islamic banks to improve fraud detection systems and invest in staff training.

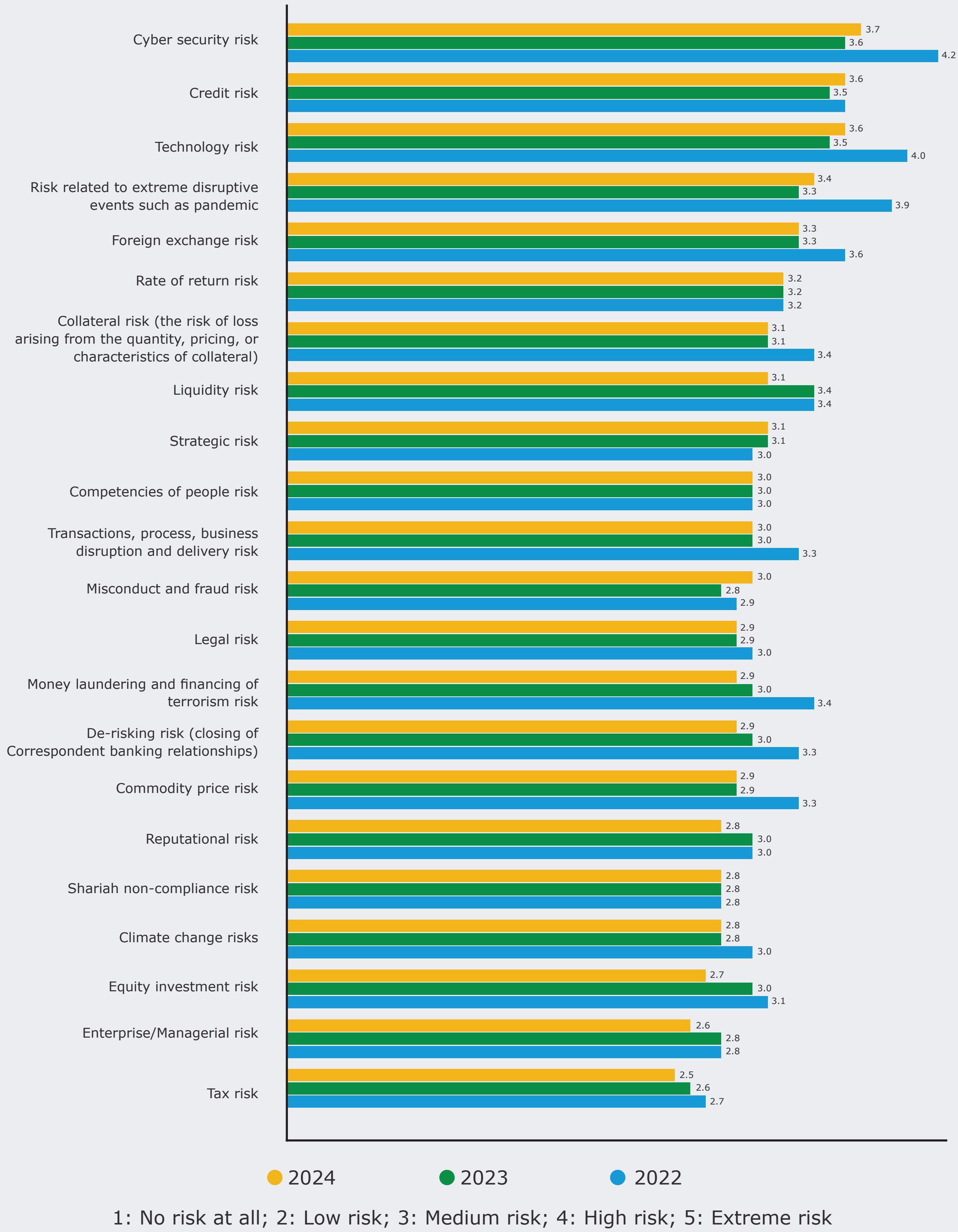
A slight increase in misconduct and fraud risk has been observed, with a score of 3.0 compared to 2.8 in 2023. This rise in misconduct and fraud risk in Islamic banks can be attributed to several interconnected factors. Technological advancements, while beneficial for efficiency and customer convenience, also introduce vulnerabilities to cyberattacks and data breaches, which malicious actors exploit for fraudulent purposes.

Regarding fraud risk, banks across regions reported increasing challenges and their strategies to address them. A bank from the Middle East ex-GCC region highlighted the evolving nature of financial crimes, noting the emergence of new security vulnerabilities in financial products and services, as well as an increase in synthetic identity fraud. The bank emphasized that the growing use of artificial intelligence by criminals necessitates new risk mitigation strategies. In response, the bank is developing a comprehensive fraud prevention program to proactively address various fraud scenarios.

Similarly, a bank from West, Central, and South Asia detailed its approach to mitigating fraud risk. This institution has upgraded its systems and implemented enhanced processes for monitoring cybersecurity and fraud issues. The bank also emphasized its investment in human capital, including ongoing training for key employees in techniques and tools related to critical IT services.

These examples illustrate the multifaceted approach banks are taking to combat fraud risk, encompassing technological upgrades, process improvements, and human resource development.

Figure 9. Global Islamic Banking Risk Dashboard (2022-2024)



A Closer Look at Different Geographical Regions

The regional data breakdown allows an in-depth look at the top risks cited by Islamic banks in different geographical regions. However, in this year's survey, the similarities are more prominent than the differences. Information technology risk appeared in the top three in all regions except West, Central, and South Asia and Sub-Saharan Africa regions (see Table 3).

Cybersecurity risk is ranked among the top three risks in five regions and only just outside that list in the West, Central, and South Asia and Europe, Türkiye, US & others. Given the banking sector's growing reliance on technology for essential functions like customer transactions, data management, and communication, these concerns are unsurprising. The ongoing digital transformation of the banking industry has introduced new and emerging risks, such as cyber-attacks and data breaches, that banks must address to remain competitive and maintain their customer trust.

Similarly, credit risk is identified as one of the top three risks in five regions. In the Middle GCC group and Europe, Türkiye, US & others, it is ranked as the fourth and tenth most significant risk, respectively. Notably, in the North Africa region, credit risk received the highest score of 4.1, which can be attributed to the challenging economic conditions prevalent in the area. Additionally, geopolitical tensions in some North African countries further contribute to increased credit risk for banks operating in the region.

Foreign exchange risk makes the top three in the West, Central, and South Asia, Sub-Saharan Africa and Europe, Turkey, & others regions; but, given the fact that it comes fifth overall, this is in itself hardly surprising. The notable high score of 4.2 in the Sub-Saharan Africa region perhaps can be attributed to these economies' heavy reliance on commodity exports, making them vulnerable to global price fluctuations. Additionally, political instability, geopolitical conflicts, and high levels of external debt further exacerbate investor uncertainty, leading to capital flight and currency volatility and putting pressure on foreign exchange.

This year, major disruptive events, such as the COVID-19 pandemic, appeared in the top five risks of all regions. Islamic banks from the West, Central, and South Asia region rated it as the top risk with the highest score of 3.7. This indicates ongoing apprehension due to concerns about pandemic-like events in the coming years. These concerns highlight the need for robust risk management strategies to mitigate the adverse effects of such disruptive events on financial stability.

Table 3. Major Risks of Islamic Banks Across Regions[2]

Group	Top Risks	Score
Group 1 GCC	Technology risk Cyber security risk Rate of return risk	3.7 3.6 3.4
Group 2 Middle East ex-GCC	Cyber security risk Technology risk Credit risk	3.8 3.6 3.6
Group 3 Southeast Asia	Cyber security risk Technology risk Credit risk Collateral risk (the risk of loss arising from the quantity, pricing, or characteristics of collateral)	4.0 4.0 4.0 4.0
Group 4 West, Central, and South Asia	Risk related to extreme disruptive events such as pandemic Credit risk Foreign exchange risk	3.7 3.6 3.4
Group 5 North Africa	Cyber security risk Credit risk Technology risk	4.3 4.1 3.8
Group 6 Sub-Saharan Africa	Foreign exchange risk Credit risk Cyber security risk Rate of return risk	4.2 3.8 3.6 3.6
Group 7 Europe, Türkiye, US & Others	Technology risk Foreign exchange risk Strategic risk	3.5 3.3 3.3
Global	Cyber security risk Credit risk Technology risk	3.7 3.6 3.6

1: No risk at all; 2: Low risk; 3: Medium risk; 4: High risk; 5: Extreme risk

[2] For every group, the top three risks are identified, including all risks with the same score, even if that means that more than three are listed in total.

Islamic banks across various regions consistently face top risks related to technology, cybersecurity, and credit, with global disruptions like the COVID-19 pandemic also remaining a significant concern.

A Comparison of Small and Large Banks

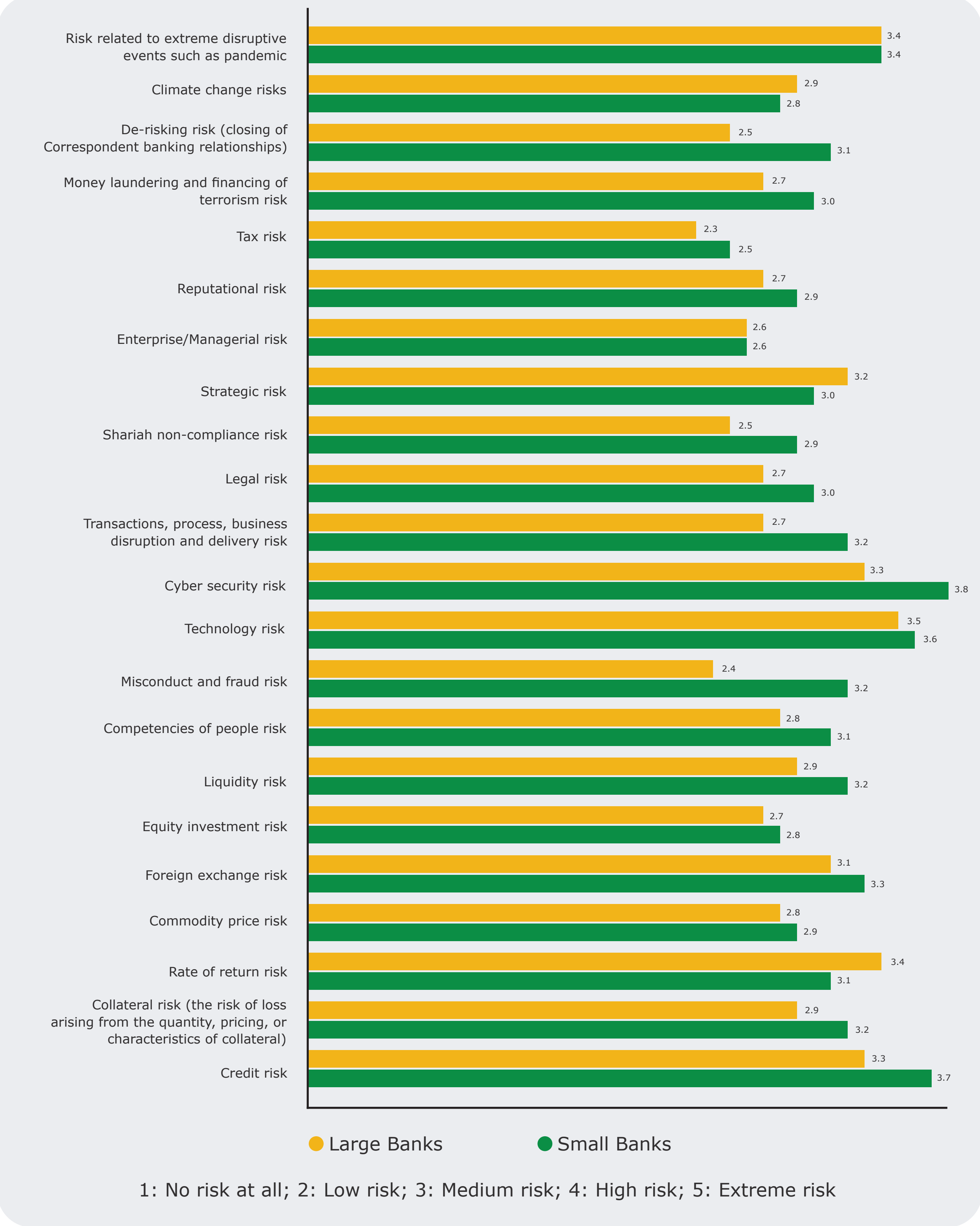
For referencce, small banks are defined as those with total Islamic assets not exceeding USD 5 billion, while large banks are those with total Islamic assets exceeding USD 5 billion.

This year's survey reveals both similarities and differences in risk perceptions between small and large banks. Small banks generally scored risks higher than large banks, reflecting their limited resources and higher vulnerability (see Figure 10). Smaller institutions often lack the extensive capital and technological infrastructure that larger banks possess, making them more susceptible to various risks and less able to absorb financial shocks. For instance, the heightened concern for cybersecurity risk (3.8) and technology risk (3.6) among small banks could be attributed to their comparatively less robust security frameworks and IT capabilities. Whereas the larger banks scored slightly less for technology risks (3.5) and cybersecurity risk (3.3).

Despite these differences in scoring intensity, the overall ranking of risks was quite similar for both groups, with cybersecurity, technology, and credit risks being the top three concerns for both small and large banks. This similarity underscores a common recognition of the critical challenges posed by the digitalisation of financial services and the ongoing economic uncertainties affecting credit quality. Large banks, while better equipped to manage these risks, still prioritise them due to their potential impact on operational continuity and financial stability.

Additionally, the alignment in risk rankings indicates a shared understanding across the Islamic banking sector of the key areas requiring vigilant risk management. Both small and large banks are increasingly focusing on enhancing their cybersecurity measures, adopting advanced technologies, and implementing stringent credit risk assessments to navigate the evolving financial landscape effectively.

Figure 10. Global Islamic Banking Risk Dashboard – Small and Large Banks



PART III:

Role of Islamic Banking in Islamic Social Finance

Part III. Role of Islamic Banking in Islamic Social Finance

In today's rapidly evolving world, addressing global challenges such as climate change, resource depletion, and social inequality has become increasingly urgent. This urgency has elevated the importance of social finance in overcoming these challenges and facilitating future market growth. Effective implementation of social initiatives with a significant positive impact depends on the coordinated efforts of all stakeholders and the mobilisation of adequate financial resources. Islamic banks play a critical role in this process, funding social welfare initiatives through a diverse range of tailored Islamic financial instruments, from donations to commercial financing, ensuring essential social projects receive the necessary support to thrive.

Islamic social financing, rooted in the principles of inclusivity and sustainability, is vital in promoting social trust, cooperation, and solidarity in the fight against poverty and hunger. This encompasses traditional instruments such as annual obligatory almsgiving (Zakat), charitable donations (Sadaqa), endowments (Waqf), and microfinancing instruments.

In this section, we explore the theme of Islamic social finance, focusing on the role of the Islamic banking industry in contributing to global social welfare. The section aims to underscore the significance of Islamic banking in advancing social causes, advocating for the integration of cutting-edge technologies, enhanced governance practices, and global partnerships to amplify its impact.

We will delve into the opportunities and challenges surrounding the role of Islamic banks in deploying these instruments to mobilise funds for various socially oriented initiatives, including financing for vulnerable groups, micro, small, and medium enterprises (MSMEs), and social development projects. Additionally, we will explore how innovation and technology can enhance the role of Islamic banking in social finance and promote inclusivity.

Our goal is to deepen stakeholders' understanding of how Islamic banks actively engage in Islamic social finance, highlighting the associated challenges, innovative strategies, and collaborative partnerships. Ultimately, this section seeks to inform and inspire strategies that advance sustainability integration, financial inclusion, social welfare, and economic development, while upholding the ethical values intrinsic to Islamic finance.

Section 1: Islamic Banks' Engagement in Philanthropy and Risk-Sharing Financing

In this section, we asked respondents a series of closed-ended questions to rate their views on various aspects related to the topic, from a scale of 1.0 (not at all) to 5.0 (to a very great extent). We also gave them the opportunity to share more details through open-ended questions.

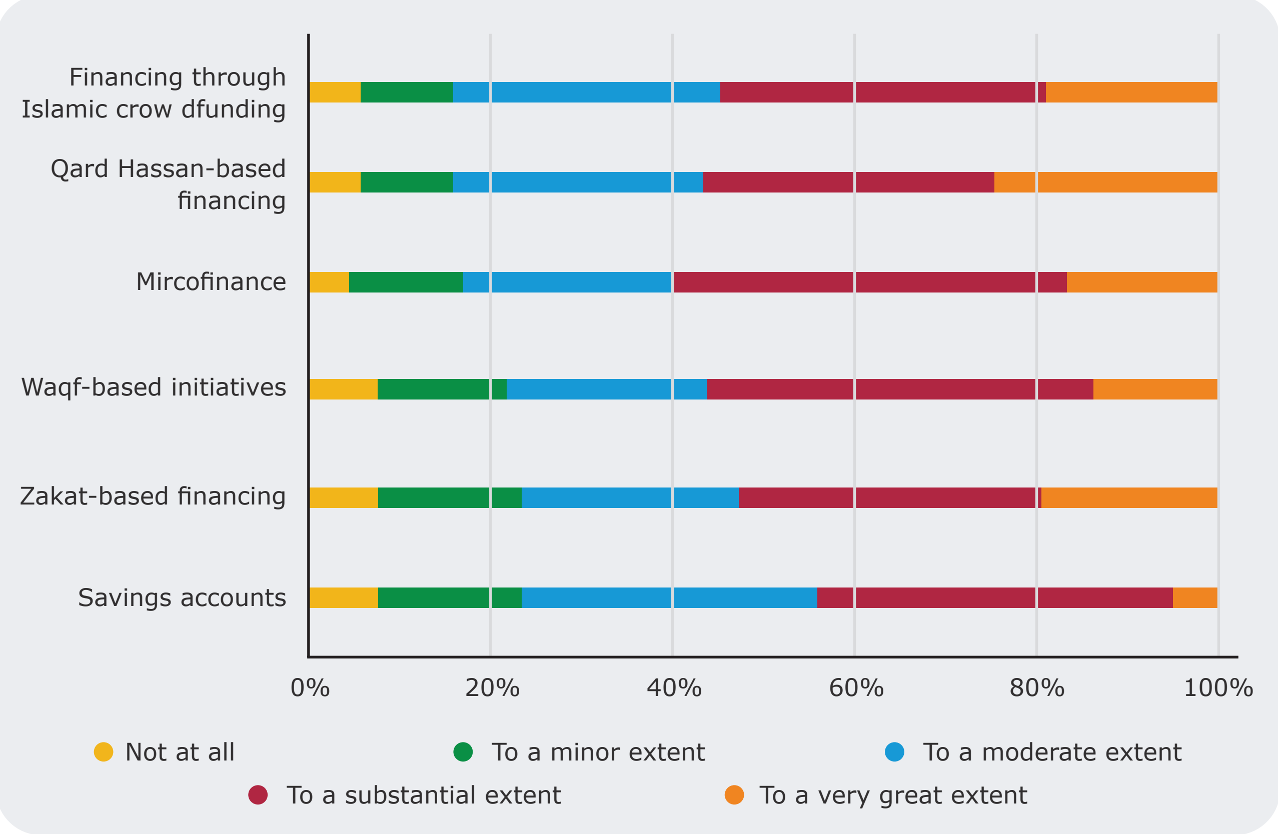
Potential of Islamic banking mechanisms in advancing social finance

To gauge the perceived potential of various Islamic banking products in advancing social finance, respondents evaluated six mechanisms (see Figure 11). With the exception of savings accounts, most respondents believe that these mechanisms have substantial or very great potential for advancing social finance.

Microfinance is perceived to have the highest potential for advancing Islamic Social Finance, with 60.3% of banks indicating that it has the potential "to a substantial extent" or "to a very great extent." This reflects its critical role in providing financial services to the underserved and promoting economic empowerment. Qard Hassan-based financing is rated second, with significant support from 56.5% of respondents who view it as having substantial or very great potential, highlighting its effectiveness in fostering social equity through interest-free loans. Islamic crowdfunding ranks third, with 53.7% of banks indicating it has the potential "to a substantial extent" or "to a very great extent," suggesting its growing importance in raising funds for social projects and supporting community participation in social finance.

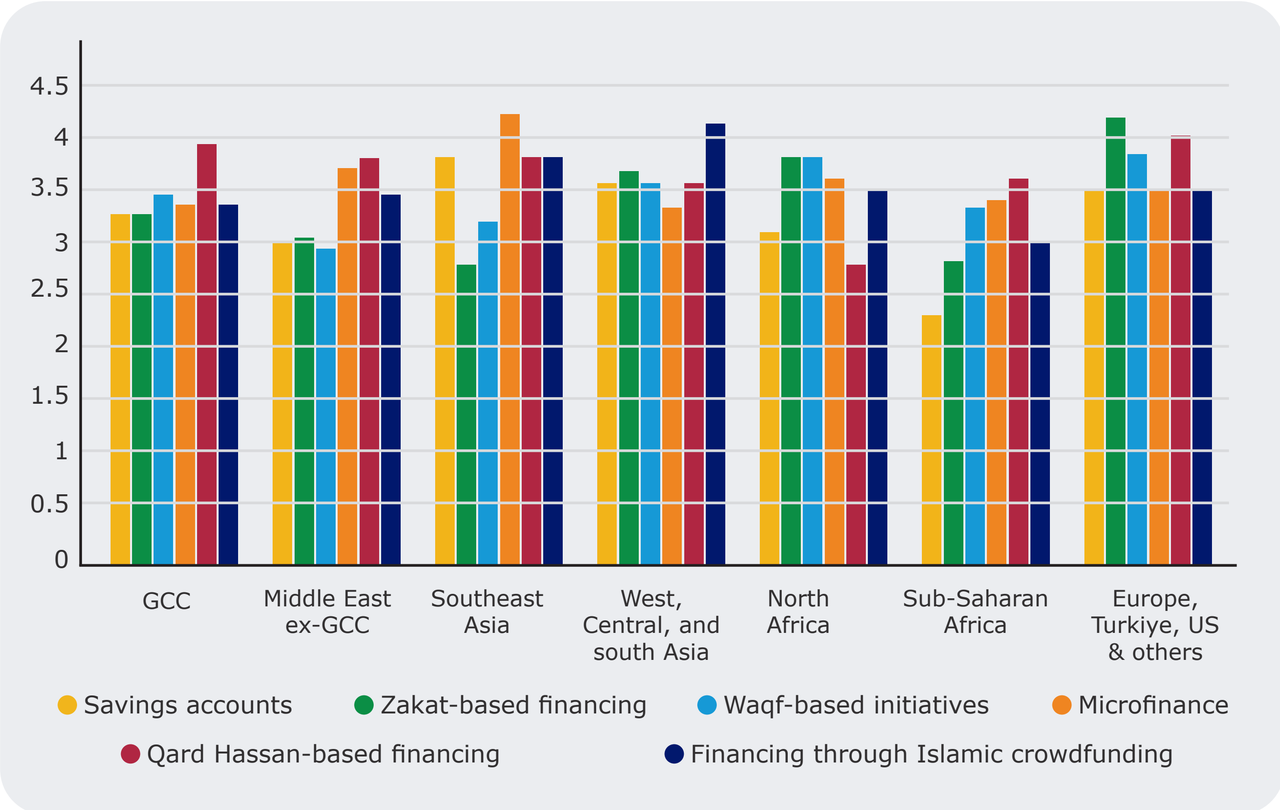
Microfinance is seen as having the highest potential for advancing Islamic social finance, especially in Southeast Asia and North Africa.

Figure 11. Islamic Banking Products or Services with the Most Significant Potential to Advance Islamic Social Finance



The analysis reveals significant regional variations in the potential of the proposed financial products or services to advance social finance. Southeast Asia, represented by banks from Malaysia, shows the highest potential in microfinance, with a score of 4.2, followed by Qard Hassan-based financing, Islamic crowdfunding, and savings accounts, each scoring 3.8. Banks from this region, alongside those from North Africa, placed less importance on Zakat-based financing. In contrast, Europe, Türkiye, and the US & Others regard Zakat-based financing and Qard Hassan-based financing as highly effective for social finance, with scores of 4.17 and 4.0, respectively. Islamic crowdfunding is seen as a major driver of social finance in West, Central, and South Asia, with a score of 4.11. Savings accounts ranked lowest in Sub-Saharan Africa and the GCC, with scores of 2.3 and 3.3, respectively.

Figure 12. Islamic Banking Products or Services with the Most Significant Potential to Advance Islamic Social Finance – Regional Breakdown



Engagement levels of Islamic banks in social finance products and services

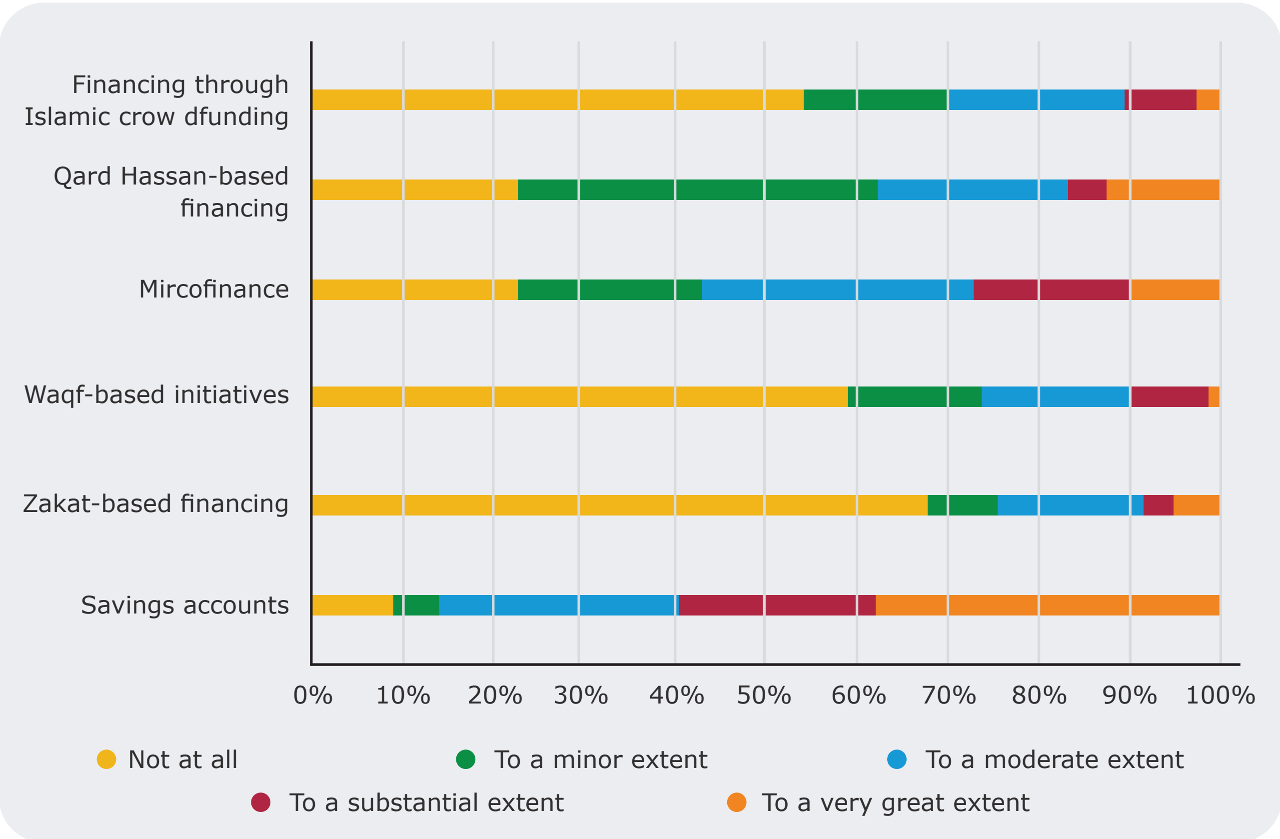
To understand the results further, we asked Islamic banks about their level of engagement in providing the proposed list of products and services.

Engagement levels are generally low to moderate across many Islamic social finance products, with savings accounts being the most widely adopted.

The data analysis reveals varying levels of engagement across different financial products and services. A general observation is that, despite acknowledging the importance of these products and services for advancing social finance, banks demonstrate only low to moderate levels of engagement. This may explain why banks are not prioritising financial inclusion, microfinance, and SME financing as major concerns, as highlighted in Part 1 of this report.

Savings accounts are the most widely adopted, with 59.4% of respondents involved to a substantial extent or more, highlighting their key role in financial service offerings. Microfinance shows moderate engagement. Conversely, Zakat-based financing and Waqf-based initiatives exhibit low participation, with 66.2% and 59.4% of respondents, respectively, not involved at all. Islamic crowdfunding similarly shows limited engagement, with over half of the respondents not participating. These findings suggest that while traditional financial products like savings accounts and microfinance are commonly offered, there is significant room for increased engagement in Islamic finance instruments such as Zakat-based financing and Waqf-based initiatives.

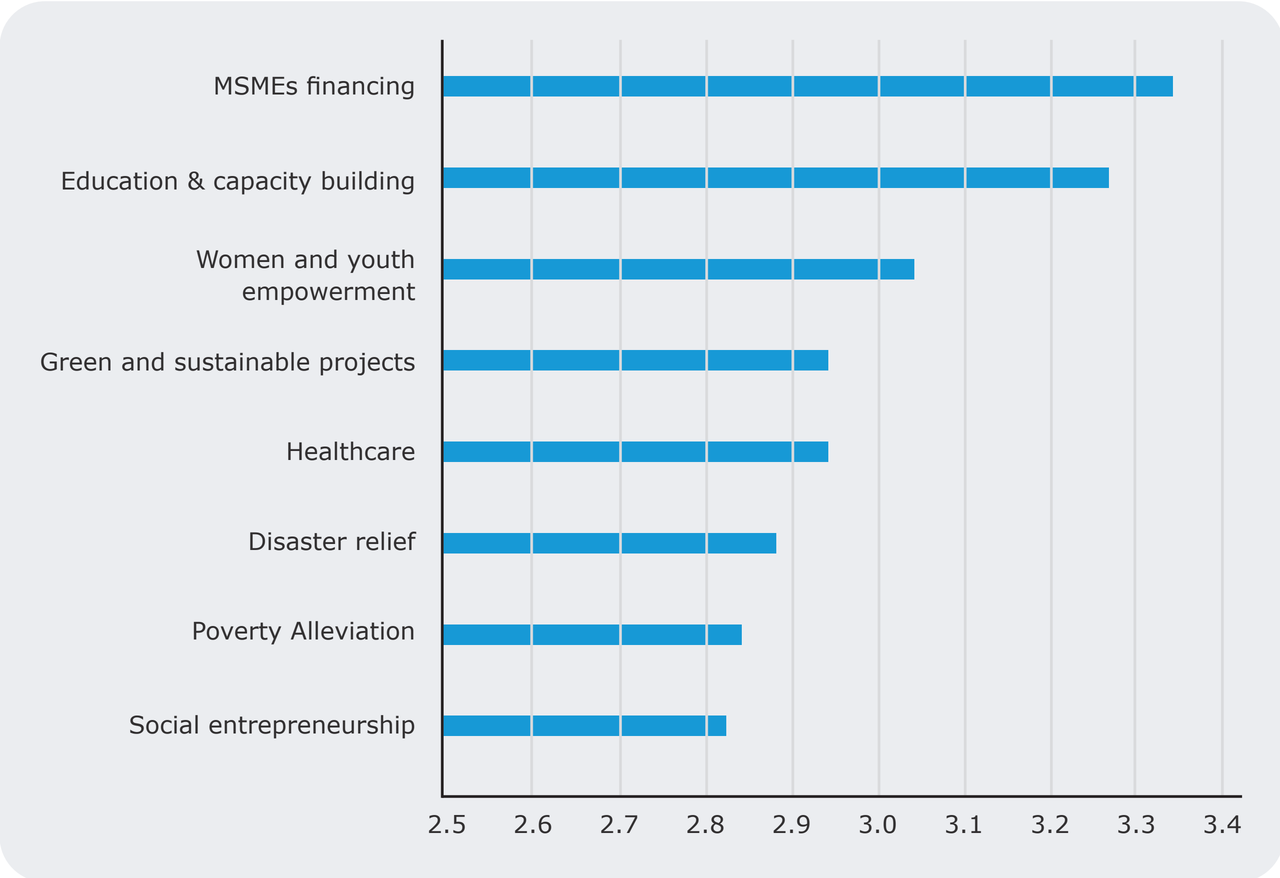
Figure 13. Islamic Banks' Engagement in Providing Specific Products and Services



For more insights, we asked banks to indicate to what extent they are involved in supporting specific segments through Islamic social financing.

The results indicate that respondents are moderately to substantially involved in various segments through Islamic social finance, with the highest engagement in MSMEs financing and education & capacity building. However, there is potential for increasing involvement in areas like healthcare, poverty alleviation, and sustainable projects to better fulfil the social objectives of Islamic finance.

Figure 14: Islamic Banks' Involvement in Supporting Specific Segments through Islamic Social Finance



Islamic banks are actively involved in MSME financing and education across regions, with varying regional focuses.

The regional analysis reveals that different areas prioritise various segments based on local needs and challenges. These findings are also supported by the open-ended responses of banks about how they deploy Islamic social finance instruments to support the most important segments.

Banks from GCC focus on social entrepreneurship, education, and healthcare, which may reflect their commitment to innovation and human capital development. A bank mentioned leveraging partnerships with international organisations, such as the United Nations, to channel Islamic social finance into humanitarian efforts. Another bank indicated offering affordable financing for medical and educational needs, with some offering rates as low as 1%.

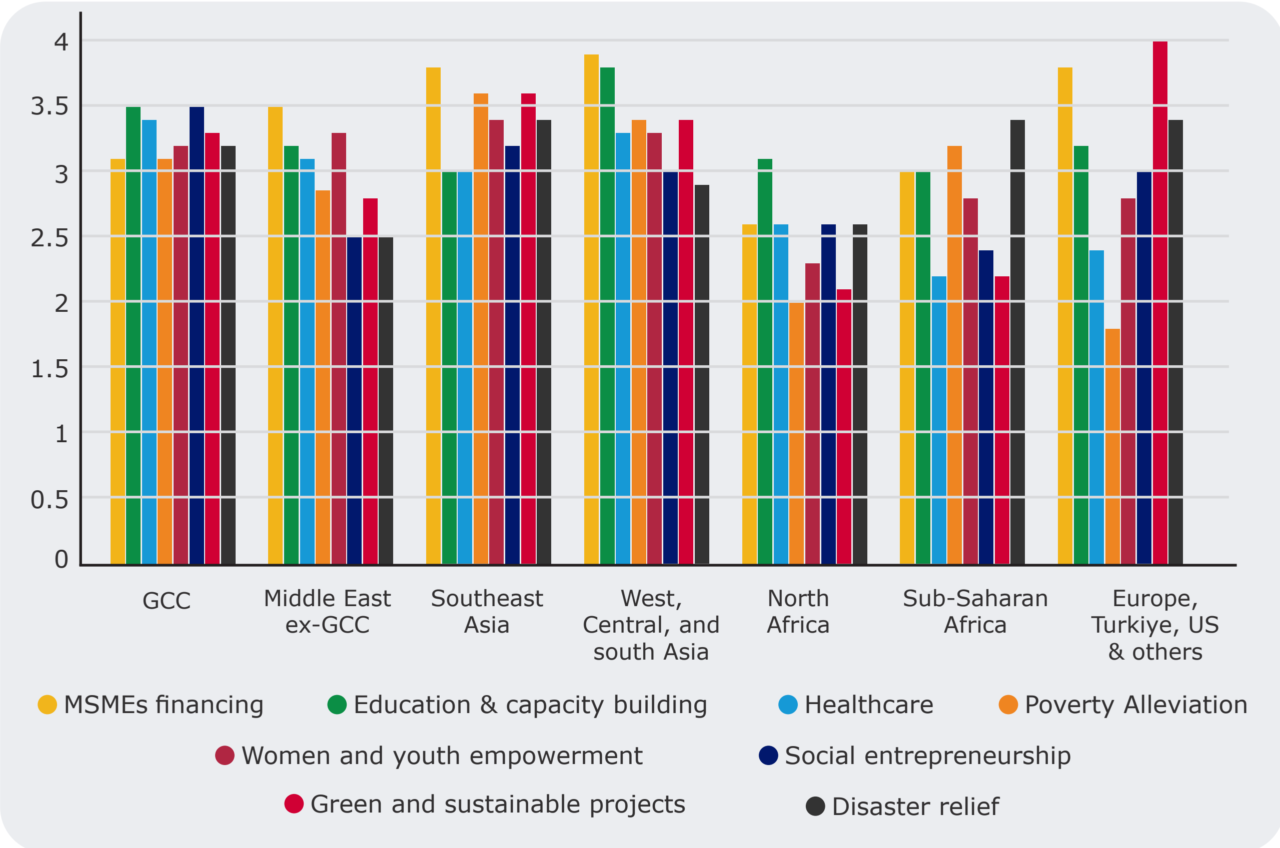
In the Middle East ex-GCC, there is support for MSMEs financing and women empowerment, highlighting efforts towards economic growth and social inclusion. To support these segments, banks from this region are deploying a broad array of Islamic finance instruments such as Qard Hassan, Murabaha, and Ijarah, targeting sectors such as industrial projects, women's and youth empowerment, and educational programmes. Banks from Southeast Asia emphasise MSMEs financing and green projects, indicating a dual focus on economic development and sustainability, using instruments like waqf and zakat to directly support social and economic development. A Bank indicated using cash waqf and zakat for direct community support, such as distributing funds to beneficiaries and crowdfunding for social projects. Another bank from the same region stated: "There is a significant focus on supporting micro-entrepreneurs through microfinance, investment, and free training".

Banks from West, Central, and South Asia prioritise MSMEs financing and education, underscoring the importance of economic support and skills development. Two banks from this region indicated deploying funds for small borrowers and participating in state schemes for clean financing.

North Africa's main focus is on education and MSMEs financing, with less emphasis on sustainability. Sub-Saharan Africa emphasises disaster relief and poverty alleviation, essential for resilience and improved livelihoods. In this context, a bank indicated its involvement in microfinance, particularly in rural areas, to empower women and support small businesses through partnerships with government and non-profit organisations. Another bank stated allocating funds for youth and women empowerment, skill acquisition, and disaster relief.

Lastly, Europe and Türkiye, US & Others show commitment to sustainability and MSMEs financing, reflecting global environmental goals and economic diversity. A bank mentioned developing products for social finance, including social sukuk and supporting women entrepreneurs, highlighting a blend of economic and social development objectives.

Figure 15. Islamic Banks' Involvement in Supporting Specific Segments through Islamic Social Finance – Regional Breakdown

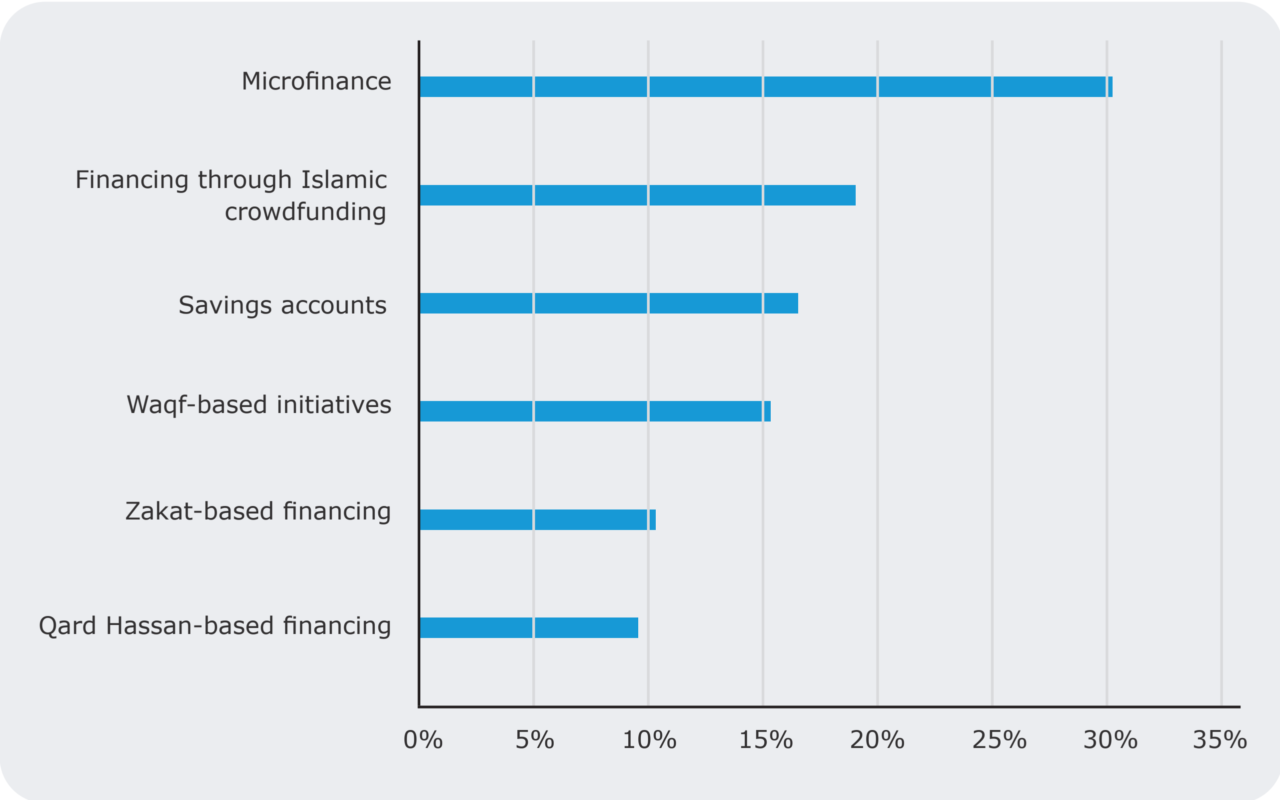


Key areas of potential and strategic integration in Islamic social finance

Islamic social finance encompasses a variety of instruments and initiatives designed to promote economic and social well-being in accordance with Islamic principles. Each area within Islamic social finance offers unique opportunities and holds varying levels of potential for development. Islamic banks were asked to identify the areas that hold the greatest potential for development.

The results show that microfinance is viewed as the most promising, receiving 30.3% of the responses. Islamic crowdfunding follows with 18.2%, indicating potential interest in using digital platforms to mobilise funds for various social and business initiatives. Savings accounts and Waqf-based initiatives are also seen as important, with 16.7% and 15.2% respectively, reflecting an interest in traditional saving methods and sustainable funding for community projects.

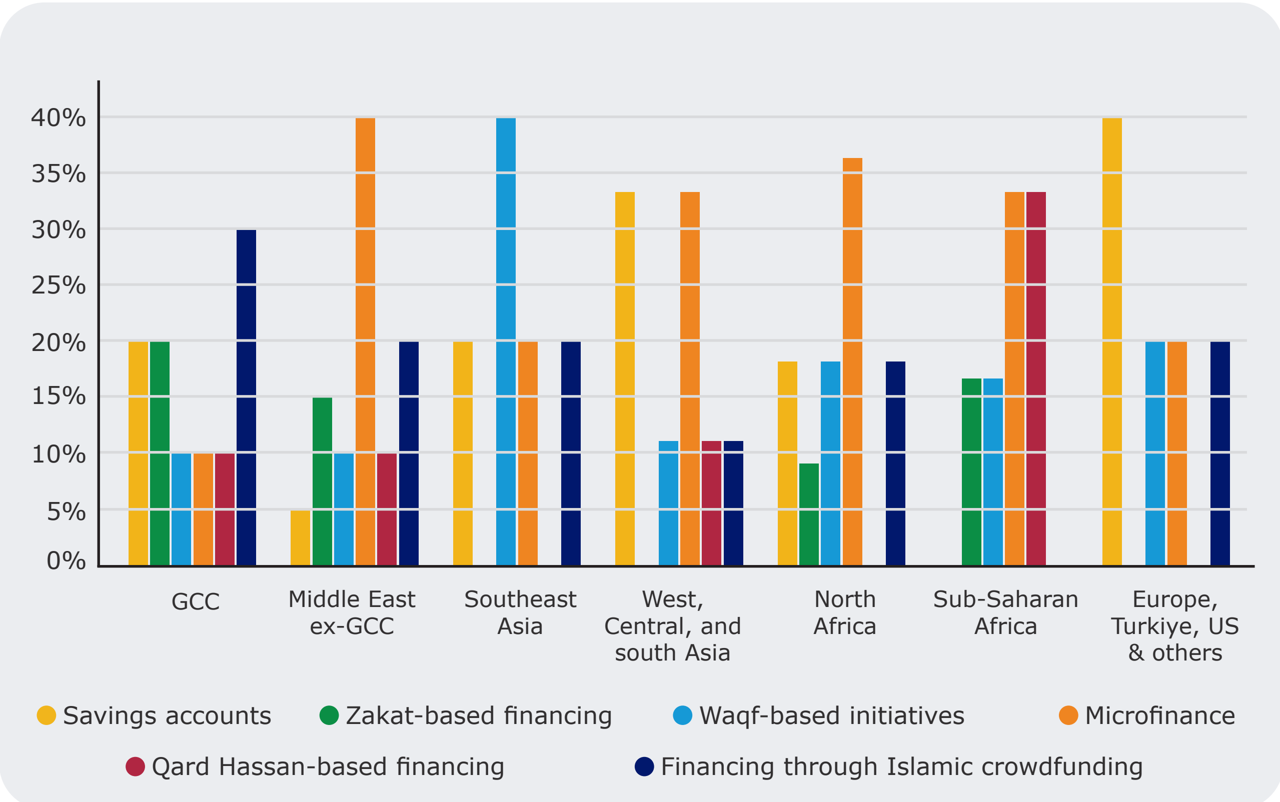
Figure 16: Islamic Social Finance Areas that Hold the Greatest Potential for Development



The regional analysis highlights Microfinance as the area with the greatest perceived potential for development across multiple regions, especially in the Middle East ex-GCC, West, Central, and South Asia, and North Africa. Savings Accounts are particularly important in the West, Central, and South Asia, and Europe, Türkiye, US & others, reflecting a preference for traditional saving methods. Islamic Crowdfunding shows considerable interest in the GCC and Southeast Asia, indicating a trend towards using digital platforms for funding and this aligns with the advancements of these segments in particular countries from these regions. Qard Hassan-based financing initiatives have significant potential in Southeast Asia, while viewed with lower potential in other regions.

Banks are increasingly integrating philanthropic activities into their core business strategies, balancing social and financial objectives through strategic planning and community-focused initiatives.

Figure 17: Islamic Social Finance Areas that Hold the Greatest Potential for Development - Regional Breakdown



Islamic banks were next asked to indicate how they balance their commitment to philanthropic activities, often framed under "Corporate Social Responsibility" (CSR), with their core financial objectives. This focus on CSR rather than on the use of various financial instruments aligns with some findings from previous surveys. The results showed the following trends:

Integrated Philanthropy: Across multiple regions, there is a trend towards integrating philanthropic activities within the core business model of financial institutions. Banks from GCC stated adopting strategies like setting budgets and leveraging dedicated funds such as Zakat funds to balance philanthropy with financial goals. In Europe, Turkey, US & Others, a bank is adhering to Islamic finance principles and channels donations towards community needs, promoting profit-sharing and charitable practices as part of its regular business operations. Similarly, a bank from West, Central, and South Asia stated: "The bank actively participates in philanthropic activities across sectors such as education, healthcare, and environmental care".

Strategic Planning: Institutions emphasise the importance of strategic planning and regular evaluation to balance social and financial objectives effectively. In this context, a bank from the Middle East ex-GCC stated: "We develop a clear strategy that defines both financial and charitable objectives. We leverage internal resources and expertise to effectively balance these goals and continuously evaluate their performance to ensure both are achieved". Another bank from the same region stated adopting an active CSR strategy and setting aside specific amounts annually to support philanthropic activities, aligning these efforts with its financial goals through a planned and structured approach.

A bank from North Africa stated: "As the bank's activities improve, we plan to integrate social responsibility more actively into the strategic operations."

Community Focus: A strong focus on community welfare, financial inclusion, and sustainable development is evident, with tailored initiatives to meet local needs.

A bank from North Africa stated: "The bank supports financial inclusion through a microfinance product for artisans and women, providing savings accounts, microfinance, and additional services like training and e-commerce opportunities to empower marginalised groups".

In the same context, a bank from West, Central, and South Asia indicated focusing on the economic upliftment of low-income individuals by investing in projects that create employment opportunities and support halal businesses, aligning their financial activities with the needs of society. From Middle East ex-GCC, a bank stated: "The bank provides developmental contributions through a Sustainable Community Responsibility Programme, supporting critical sectors like health and education, thus directly benefiting the community and aligning with social objectives".

Value-Driven Practices: Values such as social justice, equitable distribution of wealth, and adherence to Islamic finance principles are central to the approach of these institutions. A bank from North Africa mentioned integrating charitable activities as a core part of its business philosophy, ensuring that all business decisions reflect values of social justice and community support. Another bank from West, Central, and South Asia stated: "The bank prioritises wealth maximisation alongside significant investments in social well-being, establishing institutions like universities and hospitals to support community development in line with Islamic principles".

Section 2: Opportunities and Challenges in Islamic Social Finance

The next section of the survey aimed to explore the perceived opportunities and challenges within Islamic social finance from the banks' perspective. It also examines the strategies deployed by banks to overcome these challenges.

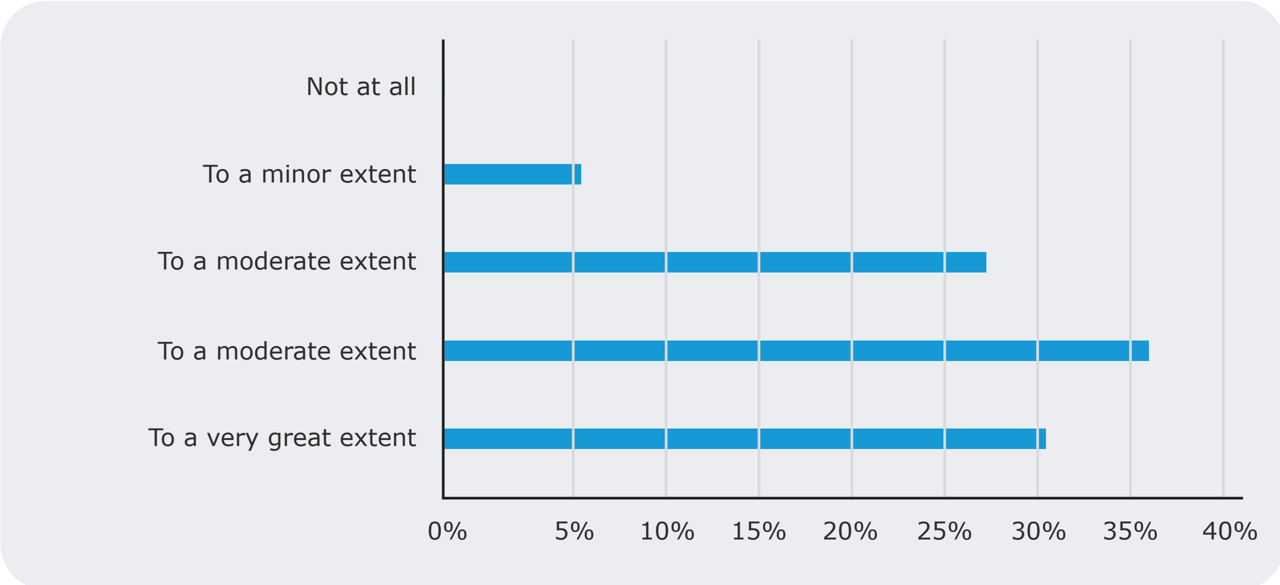
Comparative suitability of Islamic and conventional banks for social finance

First, banks were asked to what extent Islamic banks are more suitable for social finance compared to conventional banks. The responses reveal a general consensus that Islamic banks are more suitable for social finance than conventional banks. A combined 66.6% of respondents view Islamic banks as either substantially or very greatly more suitable for social finance. The 27.5% of respondents who see a moderate advantage suggest that while they recognise the potential of Islamic banks in social finance, they may also acknowledge the role of conventional banks, or the challenges faced by Islamic banks in implementing social finance effectively.

The lack of any responses indicating "Not at all" suggests that the inherent principles and operations of Islamic banks are perceived to align well with the goals of social finance.

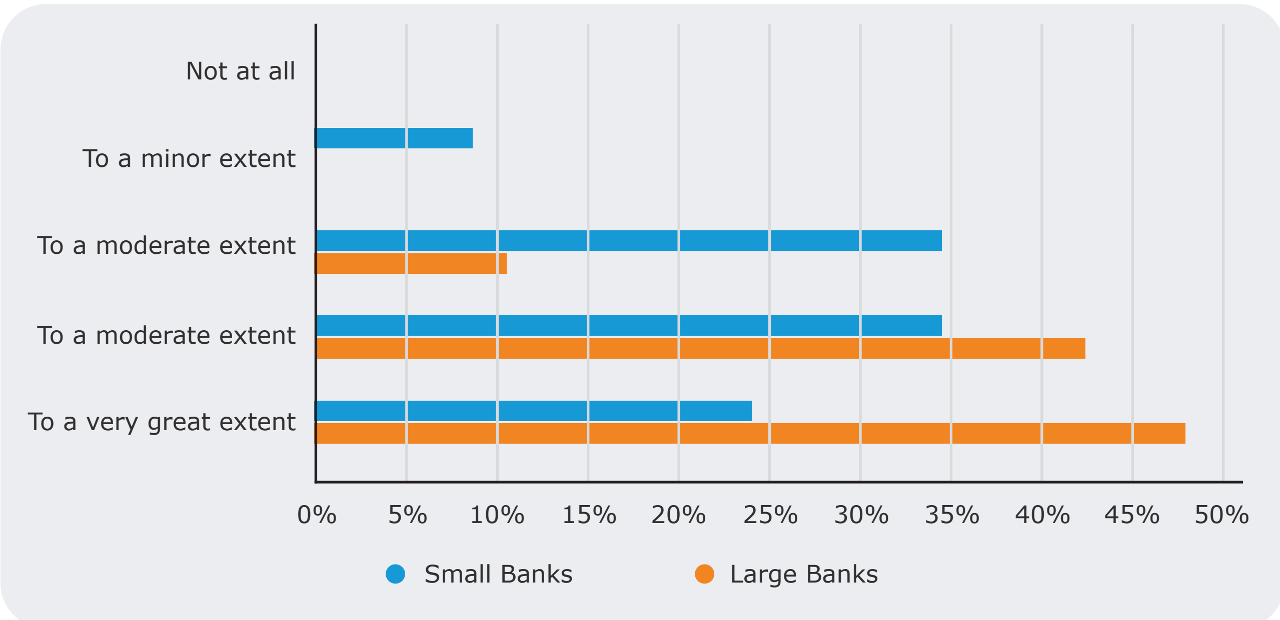
A majority (66.6%) of respondents believe Islamic banks are more suitable for social finance than conventional banks, with large banks showing stronger confidence in this suitability compared to small banks.

Figure 18: Suitability Level of Islamic Banks for Social Finance Compared to Conventional Banks



The results suggest a strong belief, among large banks, in the suitability of Islamic banks for social finance compared to small banks. An impressive 89.5% of large bank respondents view Islamic banks as either substantially or very greatly more suitable for social finance compared to 58% among small banks.

Figure 19: Suitability Level of Islamic Banks for Social Finance Compared to Conventional Banks - Small and Large Banks

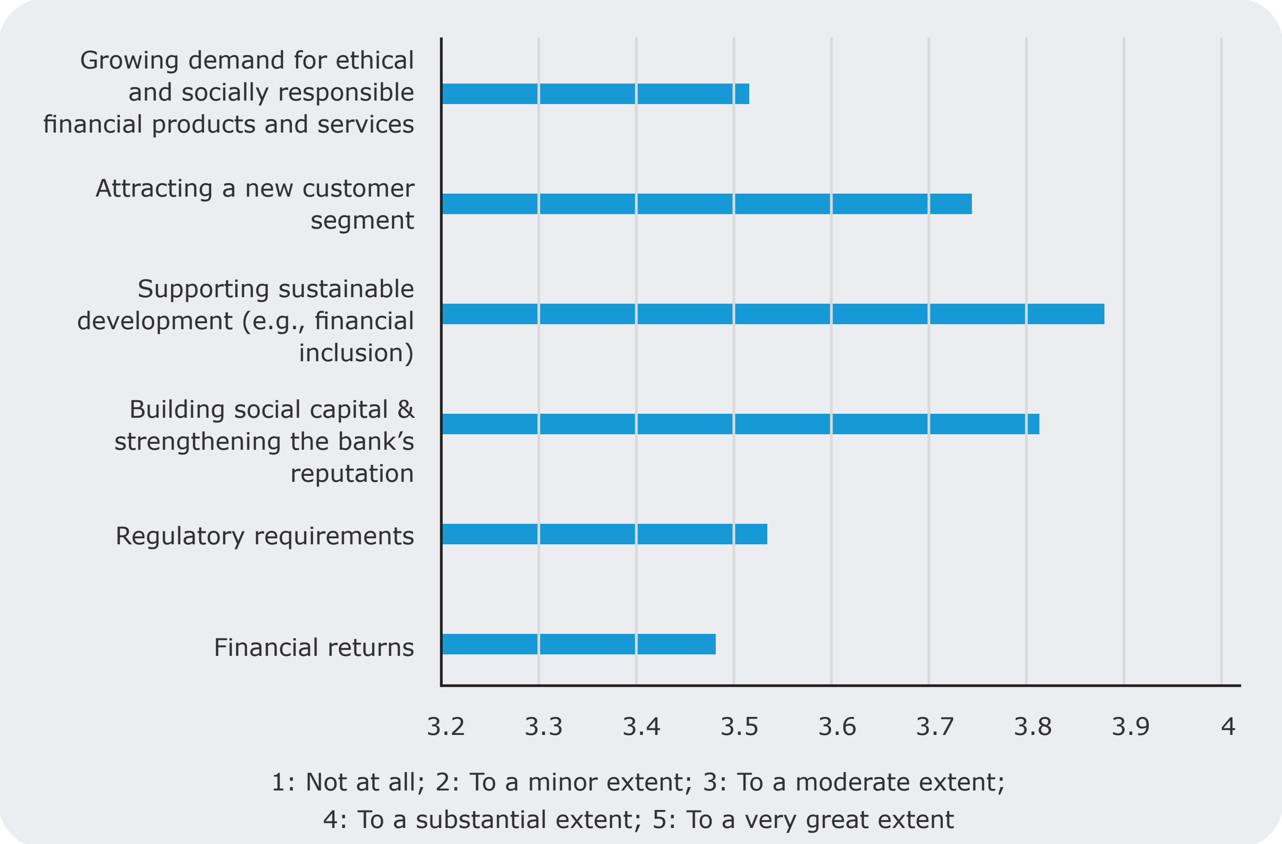


Motivating factors and obstacles in islamic banks' involvement in social finance

Islamic banks are primarily motivated by goals such as supporting sustainable development and building social capital, with financial returns being less of a focus.

We next asked Islamic banks which elements they consider as motivating factors in order to be involved in social finance. All elements ranked high with closed scoring. However, the two factors receiving the most focus were supporting sustainable development (e.g., financial inclusion), as well as building social capital & strengthening the bank's reputation. Financial return ranked last.

Figure 20: Motivating Factors for Islamic Banks' Involvement in Social Finance



It is worth noting that the analysis of the results based on the banks' size shows that both small and large banks consider all the factors to be important for involvement in social finance.

Figure 21: Motivating Factors for Islamic Banks' Involvement in Social Finance - Small and Large Banks

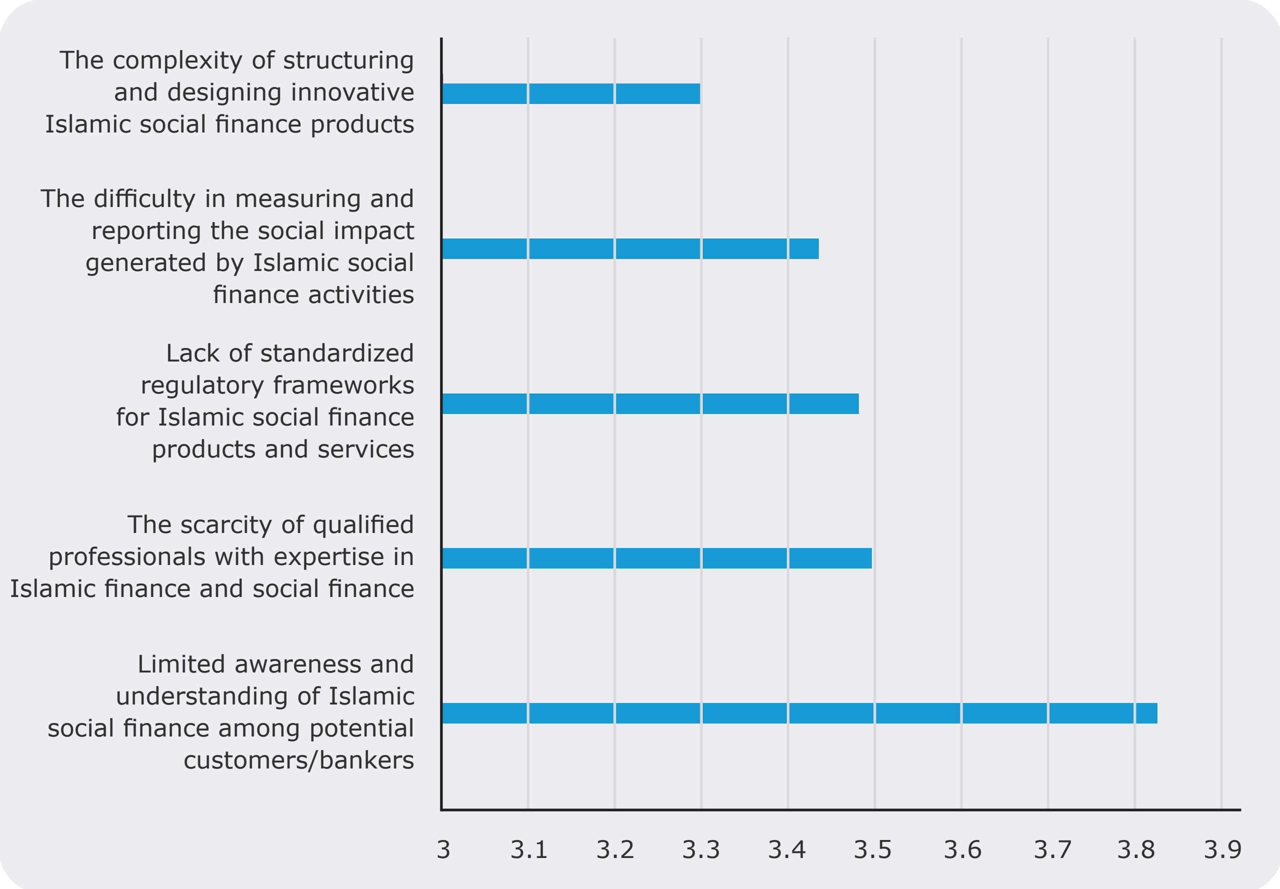
We also asked about the various obstacles banks face in engaging in Islamic social finance practices.

The results indicate that the scores for all the obstacles were relatively close to each other. The primary obstacles for banks in engaging in Islamic social finance are the lack of awareness and understanding among stakeholders, the shortage of qualified professionals, and the absence of standardised regulatory frameworks.

Addressing these challenges requires concerted efforts in education, capacity building, and regulatory development to foster a more conducive environment for Islamic social finance.

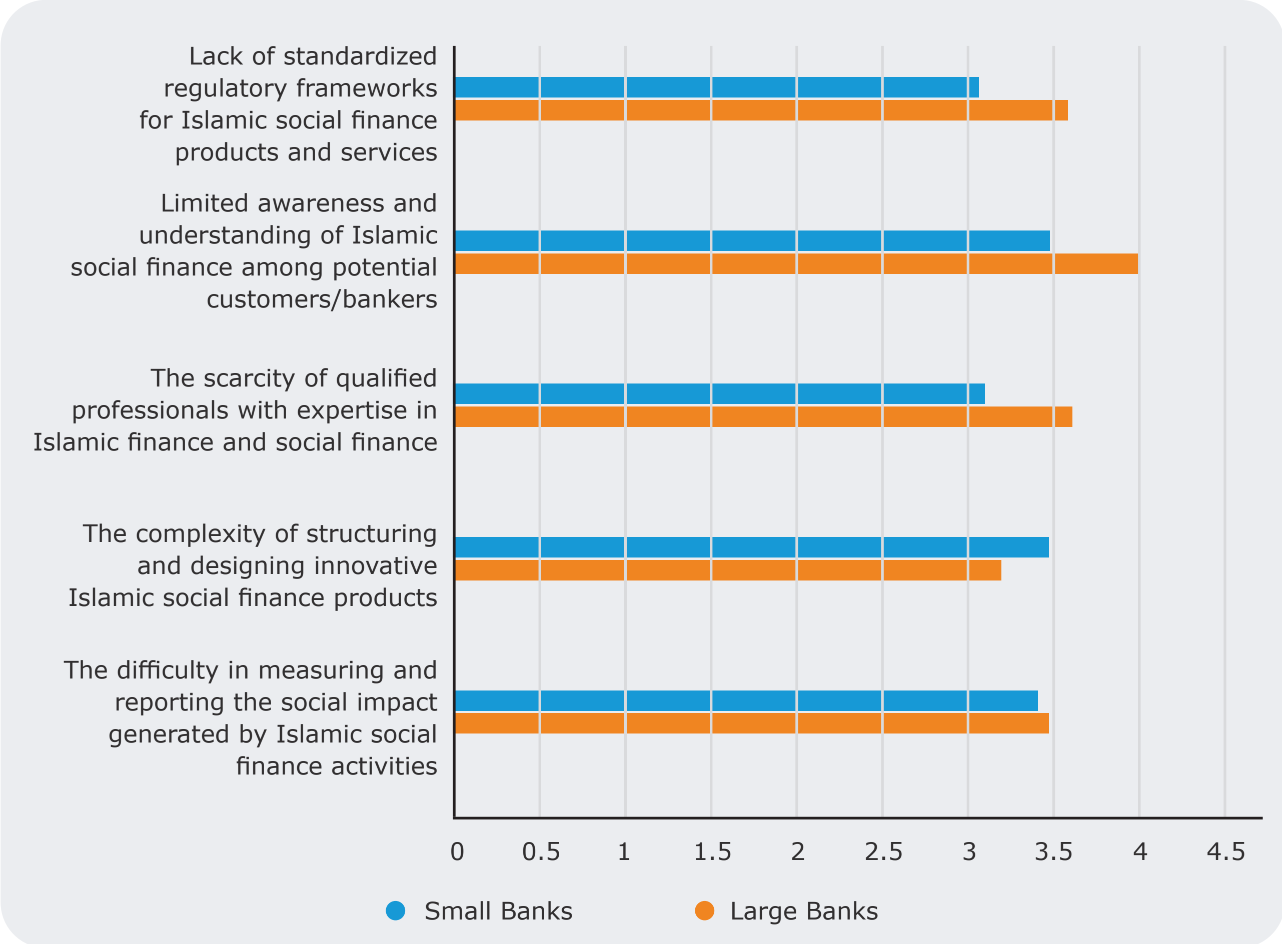
Key obstacles for Islamic banks in engaging with social finance include a lack of awareness, a shortage of qualified professionals, and the absence of standardized regulatory frameworks.

Figure 22: Obstacles to Islamic Bank's Engagement in Islamic Social Finance Practices



Looking at the rankings by bank size, Small Banks perceive the lack of standardised regulatory frameworks, limited awareness and understanding, and the scarcity of qualified professionals as more significant obstacles compared to Large Banks. These challenges suggest that small banks may need more support in navigating regulations, educating stakeholders, and building expertise in Islamic social finance. Conversely, Large Banks find the complexity of designing innovative products to be a more substantial obstacle, reflecting their involvement in more complex financial activities.

Figure 23. Obstacles to Islamic Bank's Engagement in Islamic Social Finance Practices – Small and Large Banks



The open-ended responses highlighted some common legal and institutional barriers that may hinder the advancement of Islamic social finance. The most common barriers include:

- Regulatory and legal gaps pose significant barriers to the advancement of Islamic social finance, characterised by a lack of comprehensive and uniform frameworks tailored to Islamic finance principles. These gaps hinder the innovation and effective implementation of Islamic financial products and services. For instance, banks from West, Central, and South Asia mentioned struggling with the absence of robust legal frameworks specifically designed for Islamic social finance, limiting the sector's growth and operational clarity. In North Africa, a bank stated: "The absence of legal frameworks governing essential aspects like Zakat and Waqf impedes the development of Islamic social financing initiatives. Similarly, banks from Middle East ex-GCC stated facing challenges due to the absence of legislation for specific Islamic financial instruments, crucial for expanding the scope of Islamic finance.

In Europe, Turkey, US & others, banks also highlighted the lack of specific regulations that would facilitate the development of innovative Islamic financial products, thereby restricting the sector's ability to diversify and meet evolving market needs.

- Bureaucratic and documentation challenges present formidable obstacles to the advancement of Islamic social finance, characterised by extensive documentation requirements and complex bureaucratic processes that impede swift implementation.

In GCC, a bank said: "Stringent regulatory requirements and intricate documentation procedures delay the deployment of Islamic financial initiatives, complicating operational efficiency".

Banks from West, Central, and South Asia face similar challenges, where regulatory complexities contribute to difficulties in navigating legal documentation and contract processes, creating barriers to executing Islamic social finance projects smoothly.

Meanwhile, a bank from North Africa said: "Fragmented regulatory oversight across various financial activities exacerbates bureaucratic hurdles, making it challenging to streamline processes and ensure compliance within the Islamic finance sector".

- Weak financial infrastructure poses significant challenges to the development of Islamic social finance, characterised by inadequate financial systems and a lack of specialised institutions capable of supporting its growth.

In Middle East ex-GCC and Sub-Saharan Africa, banks highlighted that the insufficient financial and banking infrastructure limits the capacity to effectively implement and expand Islamic finance initiatives, hindering broader financial inclusion and economic development.

In North Africa, a bank said: "The absence of specialised financial institutions capable of delivering microfinance products under Islamic principles restricts access to financing options tailored to Islamic social finance objectives.

In Southeast Asia, a bank stated that the limited guidelines and infrastructure for crowdfunding and social investment products constrain the sector's ability to innovate and meet the diverse needs of stakeholders.

Steps to overcome barriers in advancing Islamic social finance

Advancing Islamic social finance requires supportive regulations, heightened awareness, innovation, strategic partnerships, and effective impact measurement.

Next, we asked banks about the steps to surmount barriers in advancing Islamic social finance. Overall, the responses highlight a multifaceted approach involving:

Regulatory alignment: Banks from GCC emphasised the importance of regulatory support and the development of appropriate legal frameworks tailored to Islamic finance. A bank from the Middle East ex-GCC highlighted the importance of coordinating with government supervisory authorities to establish regulatory frameworks that incorporate a social dimension.

Awareness and capacity building initiatives: Banks across various regions stress the need for increasing awareness and education about Islamic finance principles among both customers and banking personnel.

This involves launching awareness campaigns, organising workshops, and integrating Islamic social finance into training programmes to enhance understanding and adoption. Banks from the Middle East ex-GCC highlighted the need for public and banking awareness about Islamic finance principles.

They advocate for educational campaigns, workshops, and seminars to raise awareness and understanding among clients and employees.

A Bank from Southeast Asia recommends roundtable discussions with regulators, academicians, and stakeholders to address challenges and promote awareness about Islamic social finance. Likewise, a bank from Sub-Saharan Africa stresses the importance of awareness campaigns to enlighten the public about the benefits and principles of Islamic social finance.

Innovation in product offerings: Several banks underscore the importance of innovation in developing new Islamic financial products that meet the diverse needs of communities. This includes designing Shariah-compliant products like microfinance and crowdfunding initiatives to address specific social and economic challenges.

A bank from Southeast Asia advocates for developing specialised Islamic financial products tailored to meet the needs of different customer segments.

The bank suggests creating new departments focused on Islamic microfinance and innovating products to cater to specific market demands.

Similarly, a bank from Europe and Türkiye, US & Others said: "There is a necessity of developing innovative Islamic financial products such as Islamic microfinance, social sukuk, and ethical investment funds. These products can attract a broader customer base and meet various financial needs".

Strategic partnerships: Collaboration emerges as a key strategy across regions like Southeast Asia and North Africa. Banks suggest forming partnerships with regulatory bodies, NGOs, and international organisations to leverage resources, share expertise, and foster a supportive ecosystem for Islamic social finance initiatives.

A bank from Southeast Asia proposes building partnerships with academicians and regulatory bodies to foster a collaborative approach in addressing challenges and promoting Islamic social finance.

This helps in pooling resources and expertise for better outcomes. In this context, a bank from North Africa said: "Cooperation among stakeholders is critical to the success of Islamic microfinance. Governments, financial institutions, non-governmental organisations and other actors should work together to create an enabling environment for Islamic microfinance and strengthen partnerships that promote knowledge-sharing and resource mobilisation.

For example, partnerships between Islamic microfinance institutions and traditional banks can facilitate access to a wide range of financial services and expertise, benefiting both parties and the communities they serve."

Technological integration: Some responses advocate for leveraging technology to improve the efficiency of financial processes and expand outreach, particularly to underserved populations.

This includes investing in digital solutions and expanding electronic networks to facilitate access to Islamic finance services. A bank from Southeast Asia suggests enhancing infrastructure for crowdfunding and social investment products, which can improve accessibility and efficiency.

Similarly, a bank from Sub-Saharan Africa said: "Islamic banks and financial institutions can invest in technology to make Islamic social finance more accessible and accessible to all. Technology can help improve process efficiency and reduce costs".

Impact measurement: Some responses stress the importance of measuring the social impact of Islamic social finance activities. They advocate for transparent reporting practices to build trust among stakeholders and demonstrate the tangible benefits of Islamic social finance in community development.

A bank from Europe and Türkiye, US & Others highlights the need for transparency in operations and financial reporting. The bank said: "Clear and ethical financial practices can build trust among customers and investors".

A bank from the Middle East ex-GCC suggested measuring the social impact of Islamic social finance activities". Likewise, a bank from West, Central, and South Asia said: "Impact assessment methodology should be formed and made public bi-annually. There is a need to move beyond financial impact assessment and focus on ground-level structural impact due to social finance".

The responses from various regions highlight diverse approaches and priorities that Islamic banks adopt to adapt to local interpretations of Shariah and institutional contexts. These approaches aim to develop a flexible framework for Islamic social finance that aligns with both financial and social objectives. Some banks provided detailed approaches consisting of various aspects.

A bank from the Middle East ex-GCC described an approach that consists of five elements:

- Adherence to Shariah standards: Islamic banks and financial institutions must follow Shariah standards and consult with Shariah scholars to ensure all financial activities comply with Islamic principles.
- Strong institutional structures: Islamic banks need robust structures to manage their operations effectively. This includes developing internal policies and procedures for Islamic social finance and enhancing transparency and accountability.
- Compliance with local laws: Islamic banks must ensure their activities align with local financial laws and regulations, understanding both the regulatory environment and Islamic financial laws in the country they operate.
- Financial and social sustainability: Islamic banks should balance financial and social objectives, financing projects that promote sustainable development and provide social benefits.
- Stakeholder communication: Islamic banks should engage with stakeholders, including the local community, customers, and investors, through forums, meetings, and feasibility studies to understand and meet societal needs.

Similarly, a bank from West, Central, and South Asia stated: "For developing a flexible framework for Islamic social finance which need to address the following:

- Understanding local Shariah variations
- Customising products based on cultural and social contexts
- Collaboration with local Shariah scholars
- Flexibility in contract structures
- Educating stakeholders: incorporating social and ethical values
- Community engagement and participation
- Ethical investment screening
- Legal and regulatory alignment"

According to a bank from North Africa, Islamic banks can create a flexible framework for Islamic social finance, achieve financial and social objectives, adapt to changes in Shariah interpretations, and commit to transparency and accountability by following seven steps:

- Establishing a Shariah body: Form a body of religious scholars from various Islamic schools to advise on local Shariah interpretations and ensure adherence to Islamic principles.
- Community engagement: Involve communities in designing Islamic social finance programmes to ensure they meet local needs and align with cultural values.
- Developing compatible products: Create products and services compatible with local Shariah interpretations by consulting religious scholars.
- Building relationships with religious institutions: Foster relationships with local religious institutions to build trust and enhance cooperation.
- Leveraging technology: Use technology to make Islamic social finance more accessible and efficient, reducing costs and improving processes.
- Raising awareness: Promote Islamic social finance through awareness campaigns and educational programs to highlight its benefits.
- Sharing best practices: Exchange best practices among institutions to improve the quality and impact of Islamic social finance programmes.

Similar steps were shared by a bank from Europe and Türkiye, US & Others with an additional step focusing on implementing monitoring and evaluation systems to assess the impact of financial products and social initiatives, refining strategies based on data.

Alongside these responses that provided a holistic view of the approaches that will facilitate the development of a flexible framework for Islamic social finance that aligns with both financial and social objectives, other responses focused on particular aspects. For instance in the context of working with regulators and adopting international standards, a bank from GCC stated: "Islamic banks must engage with regulatory authorities to advocate for a supportive regulatory environment that encourages flexibility and innovation in Islamic social finance". In terms of adopting international standards, a bank from the same region emphasised relying on regulatory standards such as Shariah, accounting, and governance standards issued by AAOIFI.

There is also a focus among responses on communication and consultation with various stakeholders. A bank from Sub-Saharan Africa stated: “Islamic banks and financial institutions can engage communities in designing Islamic social finance programmes. This can help ensure that these programmes meet communities’ needs and are in line with their culture”. In line with the same point, a bank from Middle East ex-GCC stated:

“Islamic banks and financial institutions must promote communication and consultation with stakeholders, such as the local community, customers, investors and other participants in Islamic social finance”. The bank also suggested conducting Forums, meetings and feasibility studies to understand society’s needs. Experience sharing was also highlighted by a bank from GCC as a key point to foster collaboration and community engagement.

Corporate governance for Islamic social finance

Strong corporate governance is crucial for Islamic banks to enhance trust, transparency, and ethical practices, which support effective social finance initiatives and sustainable development.

We followed with questions to understand the relationship between corporate governance and Islamic social finance.

We asked firstly about how corporate governance can impact the role of Islamic banks in supporting social finance. Overall, the responses indicate a strong consensus on the critical role of corporate governance in enhancing trust, transparency, ethical practices, and sustainable development in social finance. The responses highlight the need for robust governance frameworks, effective stakeholder engagement, and tailored governance practices to support the unique aspects of Islamic finance.

A bank from GCC stated: “Corporate governance in Islamic banks can impact their ability to support social finance by ensuring transparency, accountability, and ethical practices. Strong governance mechanisms can help Islamic banks align their operations with social finance goals, such as promoting financial inclusion, supporting community development, and adhering to ethical investment principles in line with Islamic finance principles. Effective governance can enhance stakeholder trust, attract socially responsible investors, and foster sustainable growth in the social finance sector”. A bank from the same region highlighted several points as follows:

- Enhance social responsibility: Maintain the bank's financial strength and support the community and government campaigns to meet the needs of various societal segments.
- Strengthen transparency and accountability: Apply the highest standards of good governance and sustainable development to build confidence among customers and investors.
- Guide and control for strategic objectives: Achieve investment and business goals while supporting social financing and sustainable development across the economy, environment, and society.
- Balance economic and social decisions: Make decisions that balance economic dimensions and the investment environment to promote sustainable development

In addition to these points, a bank from Sub-Saharan Africa added two more points:

- Ensuring financial sustainability: It sets rules and procedures for financial sustainability, ensuring long-term availability of social finance programmes.
- Attracting qualified personnel: It ensures a good working environment, helping to attract qualified professionals to work in Islamic social finance.

Moreover, a bank from Southeast Asia said: "Good corporate governance in Islamic social finance activities plays a crucial role in mitigating risks such as Anti-Money Laundering and Counter-Terrorism Financing (AML/CFT). Furthermore, effective corporate governance helps shape a well-trained staff in the field of Islamic social finance, as it encompasses both support and business elements. A well-versed staff can design programmes and products that comply with banking requirements, further enhancing the bank's operations and reputation".

Key challenges in corporate governance for Islamic banks include ensuring transparency, adherence to governance standards, balancing profitability with social responsibility, and addressing conflicts of interest.

Next, we asked banks about challenges related to corporate governance that an Islamic Bank could overcome to further advance Islamic social finance. Key challenges include the need for transparency, awareness, adherence to governance standards, and the balance between profitability and social responsibility.

A bank from Sub-Saharan Africa stated: "Conflict of interest, identification of the right beneficiaries, effective mechanism for monitoring the beneficiaries and availability of a comprehensive and robust framework by the regulators on the Islamic social finance". Another bank from the same region provided a list of challenges including:

- Lack of governance awareness.
- Lack of clear governance rules.
- Absence of independent boards.
- Lack of specialised governance committees.
- Ineffective communication with investors and society.

In the context of conflict of interest, a bank from West, Central, and South Asia stated: "Balancing stakeholder interest is important. Shareholder interests are sometimes prioritised over other stakeholder interests". The bank continued by suggesting a solution that consists of promoting stakeholder-oriented governance models to strike a balance between profit maximisation and social responsibility.

In terms of transparency, a bank from GCC provided an example related to the lack of trust in fund allocation. The bank stated: "There are innovative social finance models that can achieve a 100% donations-for-intended-purposes policy without any funds being diverted for administrative purposes. Islamic banks need to instil confidence that the social finance funds are not being used to cover the administrative costs of the bank".

Section 3: Strategies for Advancing Islamic Social Finance

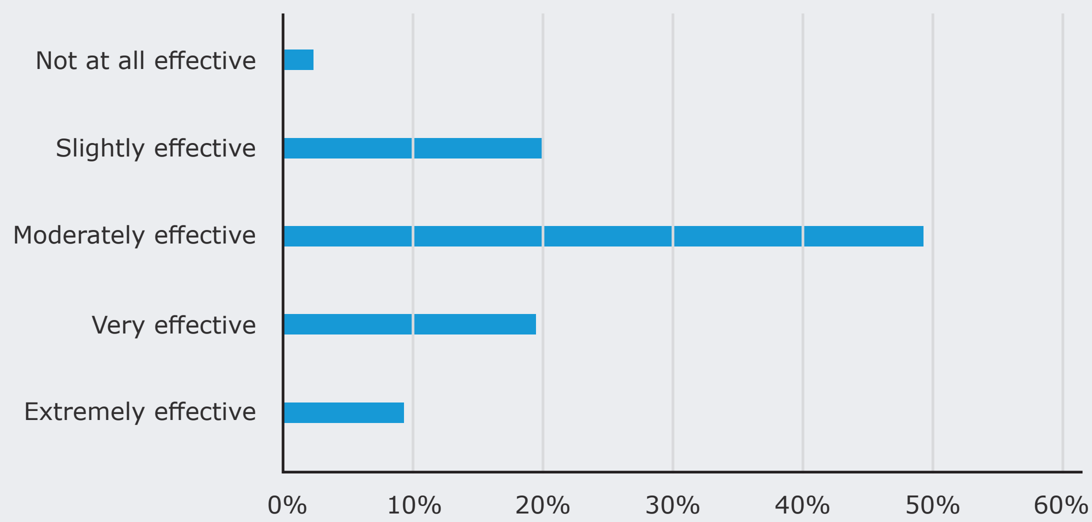
The aim of this section is to assess and explore the effectiveness of current efforts by Islamic banks in promoting Islamic social finance. Through a series of targeted questions, we will evaluate the strategies, initiatives, and innovations being employed by Islamic banks.

Perceptions and innovative practices in Islamic social finance

There is a generally positive perception of Islamic banks' efforts in promoting Islamic social finance, with large banks rated more effective than small banks.

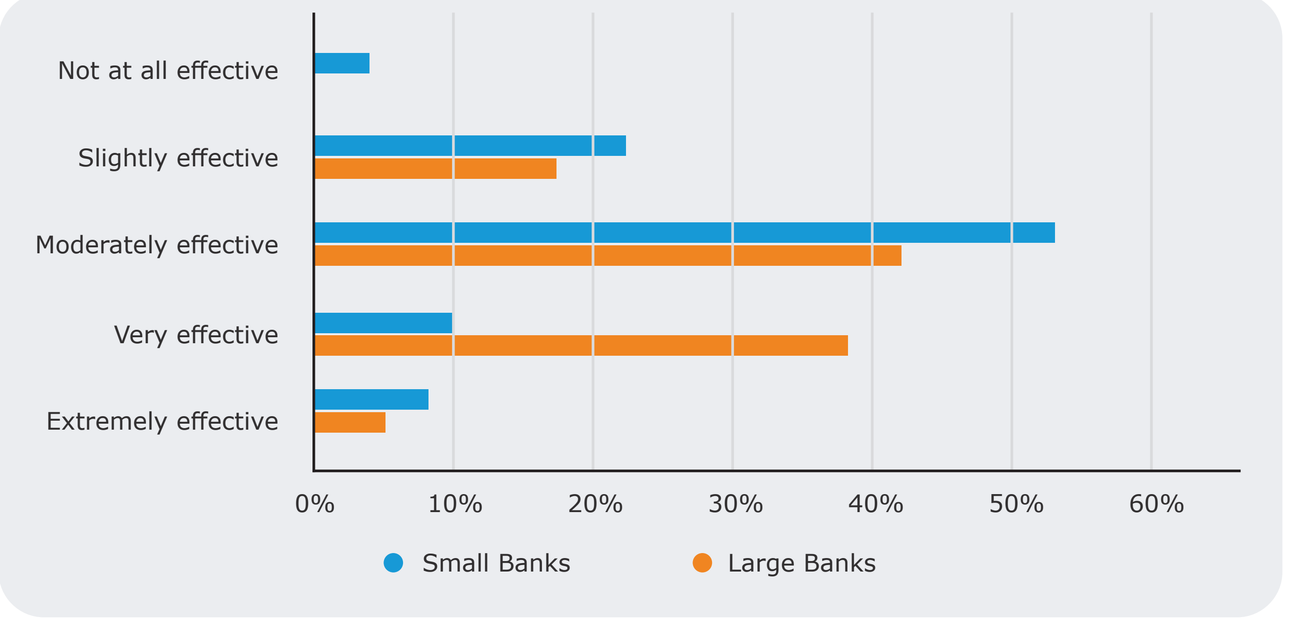
First, we asked the participants about how they would rate the current efforts of Islamic banks in promoting Islamic social finance. The results indicate a generally positive perception of the effectiveness of Islamic banks in promoting Islamic social finance. A significant portion of respondents (49.3%) consider the efforts to be moderately effective while over a quarter of respondents (27.5%) perceive the efforts as "very effective" or "extremely effective".

Figure 24: Level of the Current Efforts of Islamic Banks in Promoting Islamic Social Finance



Looking at the perceptions based on banks' size, the results show that large banks have a more positive perception compared to small banks, with 42.1% of respondents considering Islamic banks to be "very effective" or "extremely effective" in promoting Islamic social finance, compared to 22% for small banks.

Figure 25: Level of the Current Efforts of Islamic Banks in Promoting Islamic Social Finance - Small and Large Banks



Islamic banks are adopting various innovative practices such as Social Impact Sukuk, digital platforms for Zakat and Waqf, and microfinance initiatives to enhance sustainability and financial inclusion.

For the purpose of sharing experiences, we asked the banks to provide examples, if any, of innovative practices within Islamic social finance that they are adopting. Respondents across various regions are adopting various innovative practices aimed at promoting sustainability, financial inclusion, and community support. A bank from Europe and Türkiye, US & Others shared a list of innovative practices such as:

- Social impact Sukuk.
- Zakat and Waqf digital platforms.
- Microfinance initiatives.
- Sadaqah crowdfunding.
- Socially responsible investment funds.
- Islamic microinsurance.
- Digital Waqf platforms.
- Blockchain for transparency.

Many responses focused on supporting SMEs, women, and underserved segments through targeted financial products and initiatives. In this context, a bank from Southeast Asia said: "We have an entrepreneurship programme based on Mudarabah for micro-entrepreneurs and an in-house crowdfunding platform for charity/social projects". Similarly, a bank from North Africa listed the following initiatives:

- Crowdfunding of smallholder farmers.
- Financing projects for small artisans and industrialists.
- Microfinance project for poor groups in society.

Another bank from the same region added establishing a crowdfunding entity to support underserved communities. From GCC a bank indicated offering financing through Qard Hassan in partnership with a guarantor broker to support microenterprises for productive families. In addition to providing financing, a bank from Europe and Türkiye, US & Others said: "We established an entrepreneurship center to enable entrepreneurs with technology-oriented, scalable business ideas to turn their project ideas into commercial activity in a sustainable model and quickly. We support entrepreneurs by offering more than 30 years of banking experience to them through all channels". In terms of financial support, the bank said: "For this purpose, we support ideas with investments by establishing our own Venture Capital Investment Fund".

Some banks mentioned introducing innovative financial products. For instance, a bank from Sub-Saharan Africa highlighted that the bank is introducing Cash Waqf Account. The bank explained how this product works: "Cash Waqf Account is an innovative perpetuity deposit that will encourage the Public to participate in Waqf activities. Under the scheme, funds will be accepted. as endowments in the form of cash that will be invested by the institution on behalf of the customer. The profit generated from the investment will then be channelled to the charitable activity (s) specified by the customer at the point of opening the account from a list of pre-approved charitable activities". A bank in North Africa is offering a microfinance product developed in collaboration with charities, foster companies, and experienced e-commerce sites. This collaboration leverages their geographical reach and ability to support marginalised groups in economic entrepreneurship.

The microfinance product aims to provide a comprehensive package of financial and non-financial services to small entrepreneurs.

The financial services package includes savings, credit, and takaful insurance, all in accordance with Islamic Shariah principles. The non-financial services package focuses on training, consulting, and technical support.

Impact and measurement of Islamic social finance initiatives

Banks use a range of KPIs, including financial returns, job creation, education, health, and environmental sustainability to measure the impact of their social finance initiatives.

Next, we asked about the impact resulting from the main strategies and initiatives that the banks have undertaken to promote Islamic social finance. Some of the responses highlighted the internal impact such as improving the bank's branding and attracting new customers while others mentioned external impact such as contributing to economic development and financial inclusion. In this context, a bank from Sub-Saharan Africa said: "The bank has empowered over 1000 women entrepreneurs and some of them now have capital for their business and are financially included". Similarly, a bank from West, Central, and South Asia said: "We have been able to reach thousands of small borrowers by providing funding to different microfinance institutions".

Some banks highlighted the impact that their initiatives had on specific economic sectors such as agriculture. In North Africa, a bank indicated that its initiatives focused on financing small-scale producers' and farmers' associations helped in expanding production affecting the size of the agricultural sector by increasing and growing. Social benefits were also highlighted by some banks, for instance, a bank from the Middle East ex-GCC said: "Funding for several projects under the Bank's community responsibility programme contributed to strengthening the capacities of educational and health institutions, providing clean water, and fighting poverty".

A bank from Europe and Türkiye, US & Others said: "Since the inception of the [bank] microfinance programme, we provided microcredit to 521 micro-entrepreneurs". The bank stated: "Positive effects were identified, including the expansion of the social environment, increased purchasing power, improvement in family relationships, increased self-confidence, improved emotional well-being, enhanced professional well-being, better social life quality, and the ability to cope with financial problems.

To understand how this impact is measured, we asked banks to highlight various KPIs and indicators used to measure the impact of their social finance initiatives. For instance, from the GCC, a bank mentioned key metrics like ROA/ROE/ROI of Waqf properties, the number of jobs created, and the number of education and healthcare beneficiaries. Furthermore, another bank indicated that specific KPIs are monitored by the board as part of business activities rather than setting distinct metrics.
In the Middle East ex-GCC, a bank highlighted indicators encompassing social, economic and environmental dimensions. The indicators cover the following:

a- Economic indicators:

- Financial return: focuses on the initiative's financial return and its ability to generate profits or provide financing.
- Employment and economic opportunities: Measures the initiative's ability to create jobs and improve the economic status of the target community.
- Economic growth: Measures the initiative's impact on domestic and regional economic growth.

b- Social indicators:

- Education and training: Measures the initiative's impact on promoting educational and training opportunities in society.
- Health and well-being: Measures the initiative's impact on improving the health and well-being of individuals and target communities.
- Equality and justice: Measures the initiative's ability to promote equality and social justice in society.

c- Environmental indicators:

- Environmental sustainability: Measures the initiative's impact on natural resource conservation and sustainable development.
- Pollution reduction: Measures the initiative's ability to reduce carbon emissions and environmental pollution.

Another bank from the same region noted that the impact of social finance initiatives is reflected in the increase in partners and the volume of annual social funding.

From Southeast Asia, a bank tracks the number of beneficiaries and projects, alongside the individual impacts such as increased income, job creation, and business expansion. In the West, Central, and South Asia region, banks measure the number of borrowers impacted, financial and social KPIs, stakeholder feedback, and specific targets for new customer acquisition and account openings.

In North Africa, a bank uses a comprehensive set of KPIs, including the number of beneficiaries of Islamic financial products, the size of financing for socio-economic projects, successful payment rates, and the growth of charitable accounts. Banks from Sub-Saharan Africa focus on the number of financially included women, the amount of capital advanced, and the profit saved.

In Europe and Türkiye, US & Others, a bank said: "We track the number of green projects financed, the number of students supported, and the number of entrepreneurs aided, aligning these with our strategic goals".

While banks reported various impacts of their social finance initiatives, it is important to note that the metrics for measuring these impacts are not standardised across the industry. Banks use a range of indicators, from the number of beneficiaries to financial metrics such as increased income or business expansion. Future research could focus on developing more standardised frameworks for measuring the impact of Islamic social finance.

Technology deployment in Islamic social finance

Banks are increasingly leveraging technology, including digital platforms and AI, to improve the efficiency, transparency, and reach of their social finance activities.

Technology deployment is a critical component for banks to support and expand social finance initiatives. The following question explores how banks across various regions are utilising technology to streamline processes, improve transparency, and maximise the impact of their social finance efforts. The open-ended answers highlighted the diverse ways in which banks are deploying technology to support their involvement in social finance. For instance, a bank from the GCC region has adopted a web-based platform for the application of social finance projects and requests for financial disbursements. Another bank indicated using an online platform to follow up with beneficiaries.

Similarly, a bank from the Middle East ex-GCC is leveraging an electronic platform for crowdfunding and digital social finance, mobile applications for social finance and digital payments. Advanced technology such as AI is deployed by a bank in Southeast Asia for marketing activities. In the same context, a bank from Europe and Türkiye, US & Others mentioned using advanced analytic models with AI to streamline social finance processes. Another bank said:" We have recently initiated IT efforts to filter and report on the financing related to social finance conducted through our system".
Banks in Southeast Asia are using social media and AI for marketing activities, setting up crowdfunding platforms, and integrating charity features into Internet banking. Meanwhile, in West, Central, and South Asia, a bank developed a digital supply chain finance platform to support small distributors. Another bank ensures its IT infrastructure is frequently updated to facilitate smooth operations linked to social finance.

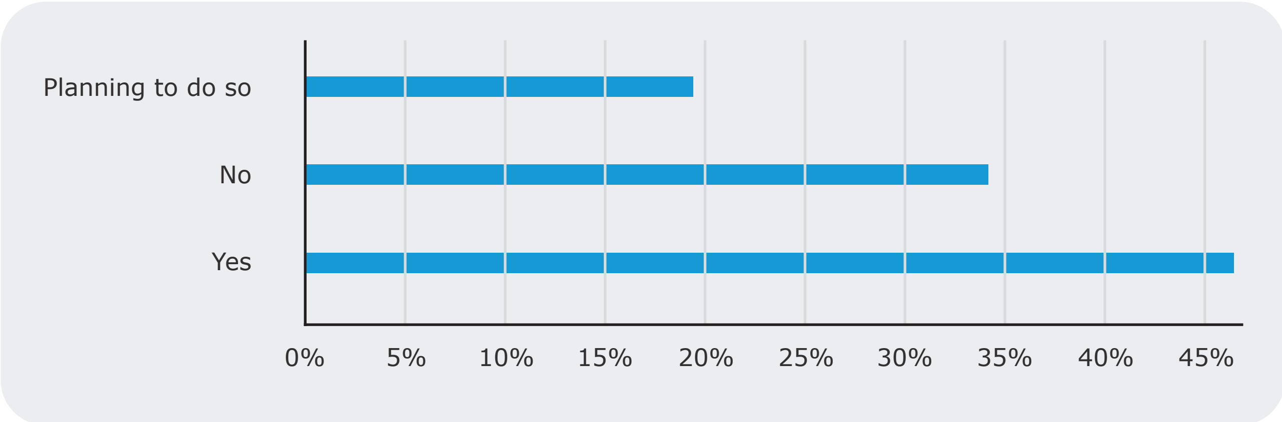
In North Africa, banks are also harnessing technology to enhance social finance. For instance, a bank uses a mobile application for donations. Another bank offers a suite of e-services, including Internet and mobile banking for SMEs.

Although the responses highlight the awareness of banks about the role of technology in supporting social financing, the examples provided are still basic and indicate an infancy phase of deployment.

Section 4: Collaborative Ventures and Partnerships for Enhancing Islamic Social Finance

The following section focuses on the role of partnerships and collaborations in advancing Islamic social finance. The first question is inquiring if institutions have engaged in such collaborative efforts to enhance their role in this domain. The responses show that the majority of respondents (65.7%) are either involved or planning to do so.

Figure 26: Engagement Status in Partnership or Collaborations to Enhance Islamic Banks' Role in Islamic Social Finance



A significant majority of institutions (65.7%) are either involved in or planning to engage in partnerships to advance Islamic social finance, with regional variations in current engagement and future plans.

When banks indicated they were 'planning to' engage in partnerships for social finance, this generally refers to plans within the next 1-3 years. However, the specific timeframes may vary between institutions and should be interpreted as indicative of intent rather than firm commitments.

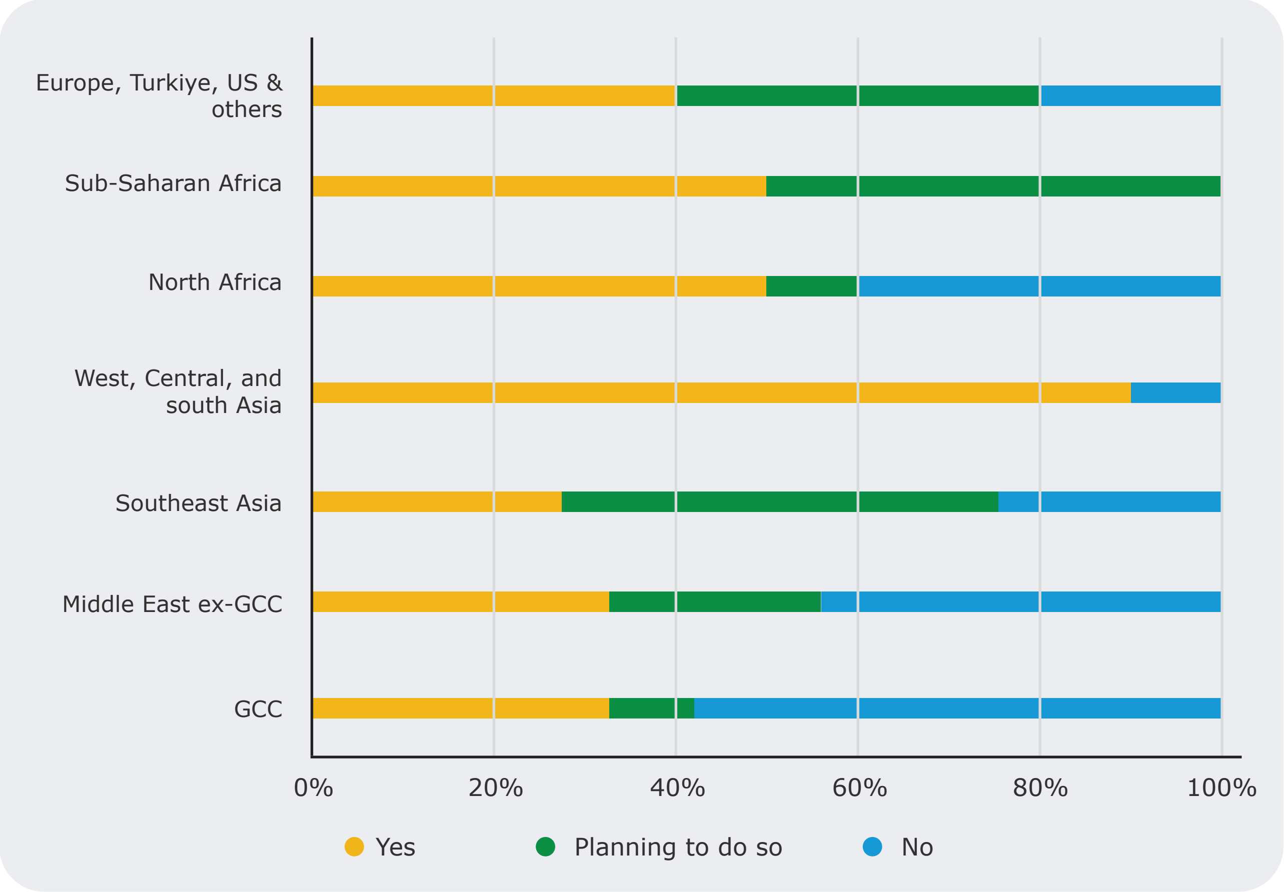
The regional breakdown reveals significant regional differences in the engagement and plans for partnerships in Islamic social finance, with some regions showing strong current engagement and others indicating substantial future plans for collaboration.

In the GCC and Middle East ex-GCC, a similar percentage (33.3%) of institutions have already engaged in such partnerships. However, the proportion of institutions planning to do so is higher in the Middle East ex-GCC (23.8%) compared to the GCC (8.3%). Additionally, more institutions in the GCC (58.3%) have not engaged in any partnerships compared to those in the Middle East ex-GCC (42.9%).

In Southeast Asia, only 25% of institutions have engaged in partnerships, but a significant portion (50%) are planning to do so, indicating a growing interest in future collaborations. The remaining 25% have not engaged in any partnerships.
In West, Central, and South Asia, a notable majority of institutions have engaged in partnerships, which is the highest among all regions. North Africa shows that half of institutions have engaged in partnerships, and 10% are planning to do so, leaving 40% that have not engaged. Sub-Saharan Africa has an equal split with half of institutions already engaged and the other half planning to do so, indicating a commitment towards partnerships in Islamic social finance.

In Europe, Türkiye, US and Others, 40% of institutions have engaged in partnerships, and another 40% are planning to do so, with only 20% not engaged.

Figure 27. Engagement Status in Partnership or Collaborations to Enhance Islamic Banks' Role in Islamic Social Finance – Regional Breakdown

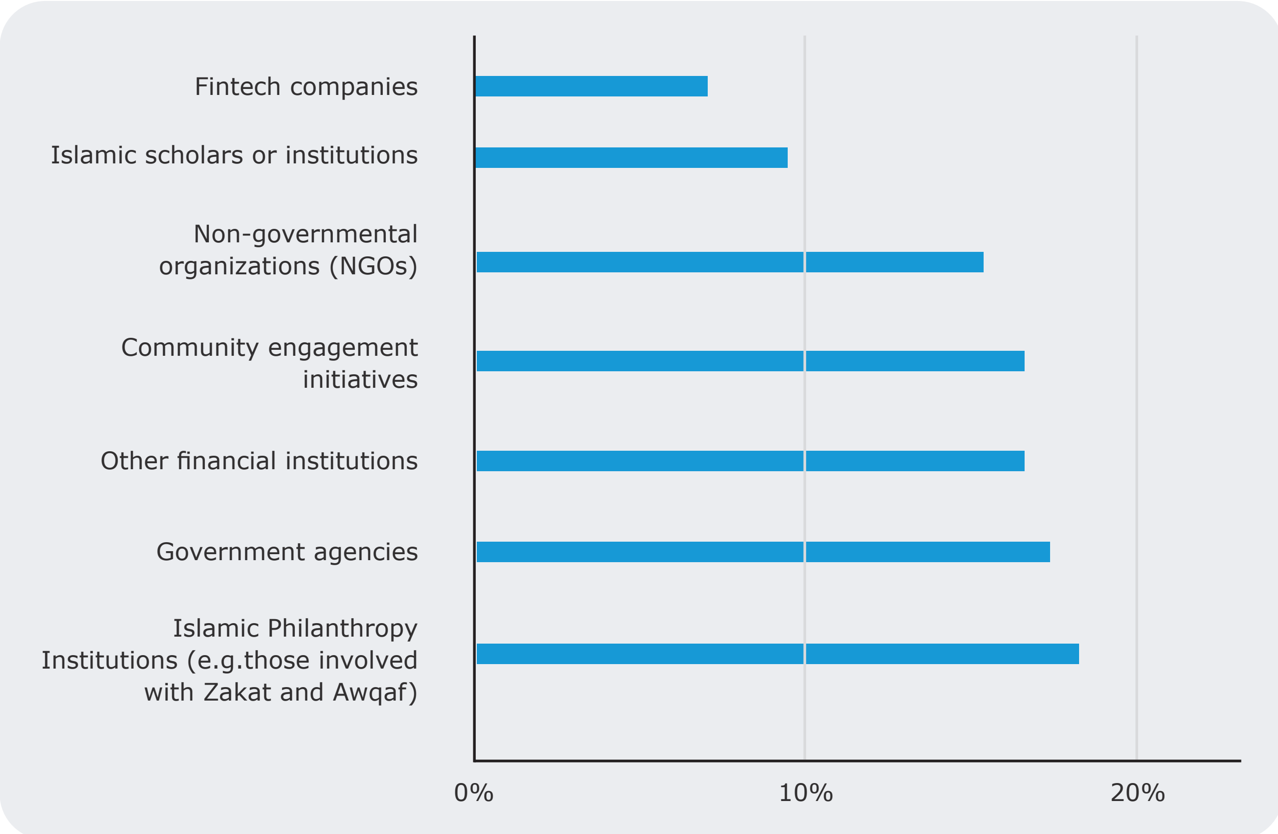


Next, we asked those engaged in, or are planning to engage in, partnerships and collaborations to enhance Islamic social finance to identify the partners or stakeholders involved. Islamic Philanthropy Institutions, such as Zakat and Awqaf organisations, are the most common partners (17.7%), highlighting the importance of traditional Islamic charities in social finance. Government agencies follow closely at 16.9%, emphasising their crucial role due to regulatory support and potential large-scale impact.

Community engagement initiatives and other financial institutions each constitute 16.2% of the partnerships, underscoring the importance of grassroots involvement and inter-financial cooperation. NGOs account for 15.4%, showcasing their support and implementation capabilities. Islamic scholars or institutions make up 9.6%, ensuring religious alignment and credibility. Lastly, fintech companies, at 8.1%, highlight the growing role of technology and innovation in Islamic social finance.

Overall, the data shows a diverse range of partnerships with a balanced involvement of traditional Islamic institutions, government agencies, financial institutions, community initiatives and NGOs

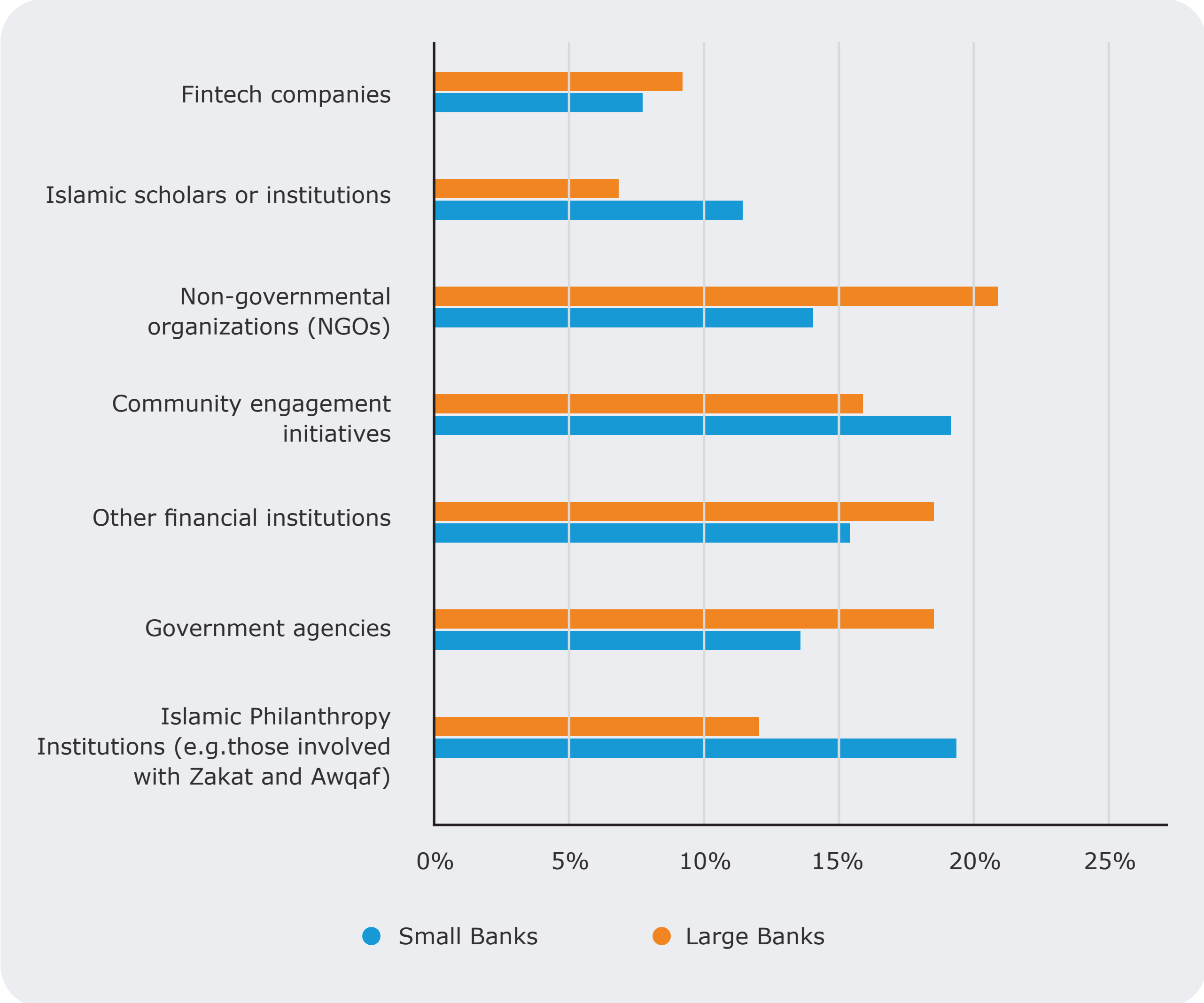
Figure 28: Partners or Stakeholders Involved in Collaborations to Enhance Islamic Social Finance



Institutions are forming partnerships with a range of stakeholders, including Islamic Philanthropy Institutions, government agencies, community initiatives, NGOs, and fintech companies, reflecting a broad and varied approach to enhancing their social finance efforts.

The results reveal distinct differences in partnership preferences based on bank size. For small banks, government agencies are the most frequent partners. This suggests that small banks rely significantly on government support for their Islamic social finance initiatives. Islamic philanthropy institutions, such as those involved with Zakat and Awqaf, follow closely. For large banks, community engagement initiatives are the most prominent partners followed by NGOs and other financial institutions.

Figure 29: Partners or Stakeholders Involved in Collaborations to Enhance Islamic Social Finance - Small and Large Banks



The open-ended responses revealed that the collaborative ventures and partnerships related to Islamic social finance have yielded benefits for banks across various regions, enhancing their capabilities, expanding their outreach, and reinforcing their social and economic missions.

In the GCC region, a bank stated, "Partners have enabled the expansion of field outreach in diverse regions and countries." Another bank reported an impressively low default rate of less than 1% in the social projects they financed, while a third bank highlighted the expansion of its financing capabilities and emphasised its contributions to social finance over financial gains.

In the Middle East ex-GCC region, a bank mentioned several benefits such as expanding its customer base, diversifying products and services, promoting positive images and social responsibility, accessing funding and support, and achieving social impact. Similarly, another bank reported enhanced orientations towards Islamic social finance, strengthening its reputation and highlighting the importance of Islamic banking in social and economic development. A bank from West Central and South Asia shared similar benefits including improving banks' images, promoting Islamic social finance ideas and strategies, and generating fee-based income.
A bank from Southeast Asia benefited from shared responsibilities, catering to more beneficiaries, and sharing knowledge and expertise, which expanded its networking opportunities. In the same context, a bank from Europe and Türkiye, US & Others said: "We have developed deep relationships with partners, benefiting from shared experiences and enhancing their reputations and market awareness".

The partnerships also benefited banks in developing innovative solutions. In this context, a bank from West, Central, and South Asia said: "We have partnered with technology providers to develop innovative solutions for supply chain finance and SME finance".
In North Africa, a bank said: "These partnerships have expanded social finance initiatives, contributed to increased agricultural, industrial, and animal production, and achieved social and economic objectives". Likewise, a bank from Europe and Türkiye, US & Others said: "Collaborations with local NGOs have supported small-scale entrepreneurs in rural areas despite the lack of legal infrastructure".

The successful partnerships and collaborations established by banks to advance Islamic social finance showcase a variety of initiatives across different regions, reflecting diverse approaches and impacts. The initiatives span various sectors, including education, health, housing, and SME support.

In the GCC region, a bank engaged in Islamic Philanthropic Ecosystem and cooperation with the International Committee of the Red Cross (ICRC) on Islamic philanthropy. These collaborations are aimed at bridging the humanitarian and development gap. Another bank has partnered with numerous local associations and organisations focusing on various social welfare projects. In the same context, a bank from the same region said: "We collaborated with the Ministry of Housing for the social housing financing demonstrating a strong commitment to social finance". Similarly, a bank from Southeast Asia has collaborated with State Islamic Religious Councils on cash waqf initiatives, emphasising community support and social welfare.

In the context of supporting MSMEs, a ban from Middle East ex-GCC region has partnered with the IFC Organisation[5] and participated in projects supporting SMEs and residential loan initiatives. Likewise, another bank has also formed multiple partnerships, such as a safety fund for Orphans and the bank's scheme for Islamic MSME financing, which have significantly supported social finance and community welfare.

In West, Central, and South Asia, a bank said: "We have launched an Islamic supply chain financing portal with a local B2B FinTech provider to provide microfinance solutions. Partnerships with the federal government and the Ministry of Finance have further supported this initiative. Another bank from the same region collaborated with a development bank and has agreements with a local insurance company to support micro-enterprise investments".

Also, a bank from North Africa said: We have partnered with civil society institutions, NGOs, and e-commerce platforms to support small enterprises and microfinance operations, aiming to reduce the likelihood of failure and accelerate business innovation". In Europe and Türkiye, US & Others, banks have launched, with local foundations, impactful projects to support education and to provide microcredits to micro-entrepreneurs.

The diversity in the nature and maturity of these initiatives indicates that while some regions have made substantial progress, others are still in the early stages of deploying Islamic social finance solutions.

The effectiveness and nature of partnerships in Islamic social finance are influenced by regional regulatory frameworks, socio-economic contexts, and institutional sizes, leading to diverse strategies and stages of development across different areas.

[5] IFC — a member of the World Bank Group — is the largest global development institution focused on the private sector in emerging markets.

The diverse range of partnerships and collaborations in Islamic social finance highlights significant regional variations and underscores the importance of adapting strategies to specific operational environments. These variations are influenced by factors such as regulatory frameworks, local charitable practices, and the socio-economic contexts in which institutions operate.

1. Regulatory frameworks: The regulatory environments governing charitable activities, such as Zakat collection and distribution, play a crucial role in shaping collaboration opportunities. In regions where Zakat is managed by government bodies, such as some GCC countries, Islamic banks may find it beneficial to align their initiatives with government strategies and leverage state-sponsored programmes. In contrast, in regions where Zakat is left to private individuals or community organisations, banks may need to develop partnerships directly with these entities to effectively channel resources and support.

2. Socio-economic contexts: The nature of social finance initiatives often depends on the socio-economic environment. For example, urban settings in GCC countries may present different needs and opportunities compared to the predominantly rural settings in other regions. Urban areas may benefit from partnerships focused on technological innovations and infrastructure projects, while rural areas might see more value in collaborations that address basic needs and community development.

3. Institutional size and capacity: The scale and scope of partnerships also reflect institutional size and capacity. Smaller banks, which may have limited resources, often rely on government agencies and philanthropic institutions for support. Larger banks, with greater resources and a broader reach, tend to engage in more diverse collaborations, including those with community initiatives, NGOs, and fintech companies.

Conclusion and Recommendations

Conclusion and Recommendations

Conclusion

Amidst the backdrop of rising geopolitical conflicts and ongoing economic challenges, this year's survey provides valuable insights into the perspectives of Islamic banking executives on various crucial aspects of the industry. These perspectives offer insights into market conditions, strategic priorities, and the dynamic landscape of Islamic finance.. They highlight how these leaders are navigating through uncertainty, addressing risks, and seizing opportunities within the sector.

The findings from the CIBAFI Islamic Banking Confidence Index indicate a stable and optimistic perception of the future of Islamic banking. Despite ongoing global economic volatility and geopolitical tensions, Islamic banking executives remain confident in their sector's resilience and ability to thrive. This confidence is further underscored by the CIBAFI Risk Dashboard, which shows stability in the severity of most risks, suggesting that Islamic banks are adept at managing these challenges. The consistent risk severity levels indicate that Islamic banks are successfully navigating uncertainties and adapting their strategies to maintain stability and growth in a complex economic environment.

Information technology remains a foremost challenge for Islamic banks. In a rapidly evolving landscape, the banking industry faces disruptions from technologies like generative AI, which redefine customer experiences and operational efficiencies. These advancements offer immense potential for innovation but also introduce new complexities, particularly in operations automation and cybersecurity. Misconduct and fraud risk has slightly increased, driven by technological advancements that introduce new vulnerabilities. Despite a slight decrease in concern levels, IT remains a critical priority for maintaining leadership and competitiveness in an increasingly digital world, underscoring the need for ongoing investment in technology infrastructure to overcome related risks such as cybersecurity.

Rising concerns over meeting shareholder expectations have become a primary focus for Islamic banks. In a dynamic market, balancing consistent financial performance with the ethical principles of Islamic banking is crucial.

The emphasis on shareholder value reflects the growing importance of addressing this concern. By doing so, banks can maintain market leadership and ensure long-term success, demonstrating a commitment to both profitability and ethical standards, which are core to Islamic banking principles.

Consumer attraction, relations, and retention remain top priorities for Islamic banks, although the urgency has slightly diminished. The shift in customers' needs and emerging technologies like generative AI, embedded finance, and digitisation are transforming banking operations and customer interactions. Islamic banks must evolve their approaches to meet changing consumer expectations, ensuring sustainable growth and a competitive edge in a dynamic market. The slight decrease in the perceived severity of this challenge reflects a modest reduction in urgency, yet the need for robust strategies in this area remains critical for long-term success and customer satisfaction.

Risk management remains a prominent concern for Islamic banks. Although the perceived severity of this issue has slightly decreased, this does not necessarily indicate an actual reduction in risk. Islamic banks continue to face significant challenges from compliance risks, interest rate fluctuations, AI-enhanced fraud, and geopolitical shocks. It is crucial for banks to recognise that the diminished perception of risk may obscure underlying threats. A more cautious and proactive approach to risk management is essential, with robust frameworks needed to navigate these multifaceted and potentially underestimated risks, ensuring long-term stability.

Human resources and talent development are significant focuses for Islamic banks. Despite a slight decrease in concern levels, the priority of this issue has improved. The rapidly changing environment necessitates workforce development to stay competitive. Investing in talent development and cultivating a strong organisational culture are crucial for operational excellence and achieving strategic goals.

The macro-economic environment remains a top concern for Islamic banks. The slowing global economy and ongoing geopolitical tensions pose significant challenges. Staying informed about global trends and addressing these evolving macro-economic challenges is crucial to maintain stability and growth, sustaining a competitive edge in a dynamic financial environment and ensuring long-term resilience.

Islamic banks are prioritising AML/CFT (Anti-Money Laundering/Counter Financing of Terrorism) regulations and business growth, both of which remain critical. Credit risk continues to be a significant concern due to economic slowdowns, geopolitical conflicts, and rising inflation rates, all of which heighten the risk of non-performing debts. The risks associated with extreme disruptive events, such as the COVID-19 pandemic, have increased slightly, prompting banks to stay vigilant and recognise the severe impacts on financial stability. Additionally, climate change risk remains a concern, though its severity has stabilised, suggesting a growing awareness of the need for action plans to manage risks from future disruptive events.

In the report's third section, we examined the role and engagement of Islamic banks in Islamic social finance. The analysis looked at the opportunities and challenges inherent in Islamic social finance, as perceived by the banks, and the strategies these banks employ to capitalise on the opportunities while effectively addressing the associated challenges.

In the assessment of Islamic banks' engagement with philanthropy and risk-sharing financing, several key findings emerged. Microfinance was highlighted as the most promising mechanism for advancing Islamic social finance. Regional differences in the perceived effectiveness of Islamic finance products were notable. Despite the recognised importance of various social finance products, actual engagement levels among Islamic banks varied. Savings accounts were the most widely adopted, while Zakat-based financing and Waqf-based initiatives saw lower participation. There is a general opportunity for increased engagement in underutilised instruments like Zakat-based financing and Islamic crowdfunding. Banks reported a significant involvement in segments like MSMEs financing and education but indicated a need for greater involvement in areas like healthcare and sustainable projects to enhance their social impact.

There is a recognition among the majority of participants in this year's survey that Islamic banks are more suitable for social finance compared to conventional banks. The top motivating factors for engaging in social finance include supporting sustainable development (e.g., financial inclusion) as well as building social capital and strengthening the bank's reputation. The primary obstacles faced by banks in Islamic social finance include a lack of awareness and understanding among stakeholders, a shortage of qualified professionals and the absence of standardised regulatory frameworks.

There is a generally positive perception regarding the effectiveness of Islamic banks in promoting Islamic social finance. The efforts and initiatives of Islamic banks in social finance have led to various impacts, including improved branding, customer attraction, economic development, and enhanced financial inclusion. Most banks have reported current or planned engagements in partnerships and collaborations to support social finance. Key partners in these collaborations often include government agencies, philanthropic institutions, and NGOs. These established partnerships have provided Islamic banks with numerous benefits, such as enhanced capabilities, expanded outreach, and reinforced social missions.

The findings underscore Islamic banks' commitment to navigating a complex landscape, balancing technological advancements, shareholder expectations, and risk management while enhancing their social impact. Continued focus on strategic partnerships and innovative approaches to social finance will be crucial for sustaining growth and reinforcing their role in promoting Islamic finance principles.

Recommendations

The unstable global economic outlook and rapid market developments require Islamic banks to take strategic steps to navigate seamlessly through looming concerns and risks in the coming years, including leveraging talent for organisational performance and business continuity.

With the continuous technological developments and shifts in customer behaviours, Islamic banks should prioritise continuously upgrading their digital infrastructure to enhance operational efficiency and customer experience. This includes implementing advanced technologies such as AI, to streamline processes, enhance security, and offer innovative financial products. By investing in a robust digital infrastructure, banks can improve transaction speed, reduce operational costs, and ensure compliance through automated compliance checks. Additionally, adopting cloud computing and big data analytics can provide valuable insights into customer behavior and market trends, enabling banks to tailor their services to meet evolving customer needs and preferences.

To stay competitive in the rapidly evolving financial landscape, Islamic banks must cultivate a culture that embraces continuous learning and innovation. This involves providing regular training and development programs for employees to keep them updated with the latest technological advancements and industry trends. Encouraging a mindset of innovation can lead to the development of innovative products and services that cater to the unique needs of Islamic banking customers.

Islamic banks must focus on building resilience and adaptability into their operational frameworks. Emphasising robust risk management practices and dynamic business strategies will enable these institutions to better navigate the ongoing global challenges, such as geopolitical conflicts and economic uncertainties. A proactive stance is needed to manage external shocks.

Islamic banks should strengthen their marketing strategies and product offerings that emphasise their resilience and ethical banking principles. Highlighting the stability and ethical grounding of Islamic finance during economic uncertainties can attract customers seeking safer and more principled financial options.

In the specific area of Islamic social finance, Islamic banks should enhance their strategies and initiatives in promoting Islamic social finance by focusing on high-impact areas such as sustainability and financial inclusion. Islamic banks could amplify their impact by increasing their investments in innovative financial products and social initiatives. Expanding successful programmes such as Microfinance initiatives can further drive positive outcomes in communities and improve the overall effectiveness of their social finance efforts.

It is important for Islamic banks to tailor their strategies according to their size. Large banks, which have shown a higher perception of effectiveness, should leverage their resources to support smaller banks in their social finance endeavours. Conversely, smaller banks could benefit from forming strategic alliances with larger institutions to gain access to broader networks and expertise. This collaboration can help bridge gaps in capabilities and enhance the collective impact of social finance initiatives across different bank sizes. By fostering cross-regional knowledge exchange, Islamic banks can accelerate the implementation of effective strategies, improve outcomes in their respective areas, address local challenges and maximise the impact of social finance initiatives, leading to more effective and widespread support.

To maximise the benefits of partnerships, Islamic banks should regularly evaluate and communicate the outcomes of their collaborative ventures. Sharing success stories and impact metrics can help build credibility, attract new partners, and demonstrate the value of partnerships in advancing social finance. Banks should also address any challenges faced during collaborations to continuously improve and optimise their partnership strategies.

In addition, to better assess the impact of social finance initiatives, infrastructure organisations such as CIBAFI, AAOIFI, and IFSB should develop and standardise comprehensive measurement and reporting frameworks. This includes establishing standardised metrics to track both internal and external impacts, such as improvements in branding, customer acquisition, and contributions to economic development. Developing clear KPIs and regularly reporting on these metrics will enable banks to refine their strategies, demonstrate their value, and attract further support for their social finance programmes.

Building on these internal efforts, partnerships should be fostered between industry leaders, academic institutions, and governments. These partnerships can serve multiple purposes. They can raise awareness about Islamic finance and the career opportunities it offers. They can design specialised programmes to develop the necessary skills for the industry.

They can also create a supportive ecosystem for the growth of Islamic finance talent, for example, through scholarships, internships, or research initiatives.

Banks need to adapt their strategies based on local regulatory and socio-economic contexts. In regions with government-managed zakat, aligning with state initiatives and exploring public-private partnerships is crucial. In areas with decentralised zakat, banks should focus on collaborating with local charities and community leaders.

Engaging with local experts and stakeholders can provide valuable insights into regional needs, helping banks develop effective, contextually relevant initiatives.
Banks should explore innovative solutions tailored to local contexts. Urban areas may benefit from fintech-driven financial inclusion, while rural areas might see greater impact from grassroots programmes and community-based initiatives.

Adopting flexible partnership models allows banks to adapt to changing regulatory conditions and community needs, enhancing the effectiveness of their social finance initiatives.

General Council for Islamic Banks and Financial Institutions

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