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Media Release

Series of Alternative financing articles by RAM Ratings Lanka:

ALTERNATIVE FINANCING DEMYSTIFIED

The credit crisis has unveiled myriad risks inherent in western countries' regulatory architecture. Although no system is perfect, there is growing consensus that alternative finance ("AF") or financing based on Islamic principles provides some degree of effective safeguarding against the risks faced by its conventional counterparts.

Interest in this form of AF has been rapidly gathering momentum in the last few years, from various corners of the globe. This industry is estimated to have charted an impressive annual growth rate of more than 25% over the past 5 years. According to Moody's estimates, the global AF industry has the potential of reaching USD5 trillion. Not surprisingly, even economies such as the United Kingdom, France and Hong Kong are keen to participate in this expanding market, and have made provisions to nurture their respective AF segments.

This is not to say, however, that sukuk (alternative debt instruments) are impervious to the global downturn. In fact, the general decline in property values has also affected these instruments. Nonetheless, they possess key features that address some of the underlying causes of the current credit turmoil. Perhaps the most popular aspect of AF is the prohibition of interest; rather, AF is based on risk-sharing contracts. Consequently, profits are shared and losses are divided or borne by the capital provider, as specified in the respective contracts. This implies that the lender has to be convinced of the viability of the project, and hence discourages excessive risk exposures. Apart from prohibiting business activities that are deemed harmful to society, *Shariah* law (or Islamic jurisprudence) also ensures that contracts promote fairness and justice. This is an environment where everyone can invest and receive returns based on their morals, ethics and risk appetites.

All said, Sri Lanka has a unique opportunity to position itself as the AF centre of the SAARC region. An increasing number of institutions are already offering *Shariah*-compliant financial services/instruments. On the other hand, this should also be complemented by a corresponding accounting, tax and supervisory framework to protect the interests of the investing public and stakeholders.

Analyst Contact

Prakash Jerome
prakash@ram.com.lk