



Rania Abdelfattah Salem. *Risk Management for Islamic Banks*

Edinburgh: Edinburgh University Press, 2013, 222 Pages

Ahmet Suayb Gundogdu

The eight chaptered book entitled “Risk Management for Islamic Banks” is kind of a review of literature on the subject of risk management in Banks, particularly Islamic banks. Chapter 5 and chapter 6 are the main parts of the book. In chapter 5, the book supposedly introduces various risk mitigation methods for Islamic banks. However, this chapter is primarily a review of existing literature. In chapter 6, the book supposedly demonstrates how to adopt an integrated risk management framework to fit Islamic banks, by presenting a hypothetical case of an Islamic bank and adopting suggested risk management procedures. While developing the argument, the book assumes, with reference to the literature, that Islamic banks’ business models and products are homogenous. While such assumptions are made in conventional economics and finance and any results can be derived with these assumptions, they are not deemed scientific and acceptable in Islamic economics and finance which looks for reality instead not assumptions in order to have scientific inferences. For example, conventional economics and finance assumes that Riba is same as mark-up in trade transactions and such an assumption is reprimanded in the Holy Qur’an.

Aim

The book aims to bridge the existing risk management gap between conventional and Islamic banks. However, the book assumes that Islamic banks are different due to ownership risk and such risk necessitates modification of conventional risk

@ Assoc. Prof. Dr., Istanbul Sabahattin Zaim University. ahmet.gundogdu@izu.edu.tr



management practices. The book assumes that Islamic banks expose themselves to price fluctuation risk since they don't transfer such risk to their loan seekers. The book's assumption pertaining to ownership risk is unjustified in real life, so do the results.

Interpretation

The treated subjects are not well connected. The book claims that Islamic banks have different risks, yet, it proposes a framework that is equally applicable to conventional and Islamic banks. The book's statements are not reasonable and consistent. In order to avoid logical fallacy, the book should either consider that Islamic banks are not different from conventional banks in practice or propose a different risk management framework for Islamic banks. There are major wrong statements in the book which would mislead those who are not familiar with Islamic finance. For example, the book claims "non-existence of a lender of last resort" function for Islamic banks. Besides, the book claims, pertaining to liquidity risk, that "there is no interbank market for Islamic banks". In practice, Islamic banks have access to such non-Shari'ah compliant platforms. In another part, the book mentions the availability of organized Tawarruq and Liquidity Management Company for Islamic banks and contradicts with the previous statements. The book refers to literature, yet, does not verify the authenticity of such information. Besides, the book even makes untrue statements without any reference: "conventional banks heavily depend on rating systems, specifically external rating, Islamic banks have limited access to external ratings. Therefore, in the absence of rating agencies, Islamic banks depend on internal rating systems, in which a client's creditworthiness is assessed through historical data – by evaluating past performance measures of the client's track record".

Context

The book assumes complying with government regulatory framework and BASEL system is enough to develop a risk management framework for Islamic banks. There is no out-of-the-box thinking. Hence, the ideas and facts expressed are not put into a wider context. The book does not adequately concentrate on the proposed subject. The book's perspective provides an understanding of existing bank risk management habitat to the reader. However, the book does not question the soundness of the BASEL system, neither does it mention the convergence of Islamic banks to conventional. Should conventional banks and Islamic banks fail in the next global financial crisis, the book would totally be irrelevant.

Silence

The book does not dwell on the practice of Islamic finance and instead conveys the reflection of other researchers regarding the theory of Islamic finance. The book's claim of Islamic banks having financing facilities backed up by physical assets is untrue. . The financing of Islamic banks is not actually backed by real assets and in many instances, there does not even exist any asset-based financing in real life. The book is silent about non-Shari'ah compliant liquidity management practices of Islamic banks vis-à-vis liquidity risk management. Such silence takes away from the book's appeal and casts doubt about the soundness of the models proposed by the book. Nevertheless, the book broke the silence, to some extent, towards the conclusion and highlighted the importance of central Shari'ah board for Islamic banks to avoid Shari'ah compliance risk. The book also rightly identifies the fact that having central Shari'ah board is not enough to avoid Shari'ah compliance risk and central Shari'ah audit function is needed as well.

Form

It might be discerned that the book is written in a Ph.D. thesis format but lacks the quality of a book as the author refrains from expressing his personal opinion and instead refers to other researchers without checking the accuracy of information. For example, on page 87, the book states that "It is known that Islamic Principals agree with conventional finance in terms of the risk-return principles, highlighted by Markowitz, where an increase in the expected return can only be released with an increase in the portfolio risk". Markowitz theories stemmed from Bachelier's book entitled "Theory of Speculation". The very basics of Islamic finance relate to the prohibition of such practice of speculation based financial engineering. Such fundamental mistakes alongside literary style do not add to the book's appeal and it is misleading for those are not familiar with Islamic finance.

Sources

The book refers to miscellaneous material related to Islamic finance. The major sources are mentioned, yet, due to silence on real-life examples with interviews, the authenticity of the information in the literature is not verified. Hence, the book is disconnected from real life. The book is rather a compilation of literature and could not bring the subject to life.

Literature

The book is another academic endeavor relating to other academic works in the field. It does not break new ground and/or modify the general perspectives, it rather locates itself within the established perspectives. It would be an overstatement to claim that the book introduces a novel methodological or theoretical approach and/or raise controversy. The book was published in 2013 and could not lead a debate following its publication since finance practitioners would immediately discern its disconnect from the real life.

Background

The structure and the style of the book imply that the origin of the text is a Ph.D. thesis. It is clear that the book is written by an academician with no substantial Islamic banking experience.

Overall, the book is misleading due to material information mistakes. Hence, it is neither appropriate as a textbook for any course in Islamic finance nor for casual reading. The reliance on official regulatory framework and the BASEL system suggests that the author has full confidence in the established system. The future of the established system might reveal the weakness of the book by itself in due course.