Takaful Investment Portfolios
A Study of the Composition of Takaful Funds in the GCC and Malaysia

ABDULRAHMAN KHALIL TOLEFAT
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Islamic finance emerged as an alternative financing method in the post-colonial period with the objective of developing an Islamic moral economy system in accordance with the norms, values, and principles of Islam. This constructivist strategy produced its first institution in the form of an Islamic social bank (Mith Ghamr Bank) in the early 1960s in Egypt. However, the development trajectory of Islamic finance is marked with the establishment of the first Islamic commercial bank in 1975, which defined the model to be followed in the future of Islamic banking and finance (IBF). Since then, IBF has made important inroads in mainstream banking and the global financial centres. Once considered a “voodoo economy” by BBC, it is now an everyday news subject. With over 500 IBF institutions, the asset base of the industry has passed the trillion-dollar threshold to US$1.2 as reported by The Banker (2011). While IBF has compromised on its value proposition due to the observed convergence between IBF and conventional finance, it has managed to get the attention of bankers, financiers, and business people all over the world. The product development and diversity provide a great opportunity for IBF to sustain its growth, as evidenced with the modest yet positive performance it has shown during the global financial crisis.

An important aspect of Islamic finance is the insurance, for which takaful as an Islamic alternative has been functioning in civil society on the peripheries of the Muslim world for a long time. However, the institutionalisation of takaful operating companies is also a new phenomenon limited to only about three decades.

The scepticism regarding insurance in the Muslim world can be considered an important factor in the slower growth and late development of Islamic insurance or takaful in the Muslim world. However, in particular in the GCC region and Malaysia, the takaful industry has shown a robust growth in the recent years, and its development has been possible with the facilitatory regulations and standards issued by these countries. The developments in IBF also contributed to its expansion, growth, and development. Ernst & Young’s World Takaful Industry Report 2012 states that the takaful industry will reach the US$12 billion threshold by the end of 2012. Such impressive growth is expected to continue with a positive attitude being developed.
in the Muslim world to overcome the observed skepticism toward insurance in general and *takaful* in particular.

The efficiency and effectiveness of the *takaful* industry is directly related to the way the companies manage the funds collected. The diverse *Shari’ah* complaint products available paved the way for the efficient investment of these funds, which will further contribute to the development of the *takaful* industry. It is observed that there is a gap between the ideal or the expected asset allocation of *takaful* operating companies and their actual investment or asset portfolios. As Asaria (2012) suggests, the ideal asset allocation should be: “cash, 10–15%; debt securities, 60–70%; equity, 10–20%; and alternative assets, 5–10%.” However, the experience and observations demonstrate that the asset allocation of *takaful* companies is approximately: “cash, 40–45%; debt securities, 10–15%; equity, 25–30%; and alternative assets, 10–20%” (Asaria, 2012). Thus, there is a gap between the desired and actual asset or investment portfolios of *takaful* operating companies, which was more visible in the last decade.

This observed gap provided the motivation for this study on the emergent years of the *takaful* industry in the middle of the past decade. The research presented in this study aims to explore, examine, and analyse the investment behavior and hence the asset composition of the *takaful* operating companies in the GCC and Malaysia with the objective of identifying the observed gap between the desired and actual asset allocation or portfolios of the *takaful* companies from 2002 to 2005. While the research was completed in 2009, the availability of the data and also the low willingness of *takaful* operating companies and their managers for disclosure necessitated focusing on the period for which better data was available, and hence the scope of the research is limited to 2002–2005. It should be noted that this was the expansionary period for IBF industry as well, which has had implications for the development of the *takaful* industry.

The findings, implications, and recommendations of this research should, therefore, be understood and contextualised within this period, namely 2002–2005. Despite being historical, this will help to reveal the behaviour of the *takaful* companies in the emergent period. Therefore, it is suggested in the conclusion chapter that this research can be repeated with a larger sample within a more matured *takaful* industry to search for the change that has taken place in the asset allocation or the investment behaviours of the *takaful* companies.

The subject matter, method of analysis, and findings presented in this study should be considered an important and early contribution to the nascent literature on *takaful* and on the performance and operations of the *takaful* operating companies. It is hoped that the subject matter can be taken up by other researchers to examine more recent years so that the
development trajectories in the asset allocation and investment behaviours of *takaful* companies can be located.

This book is not on *takaful* itself, and therefore does not aim to discuss *takaful* as a financial instrument and institution. It is a book developed out of research based on the exploration and analysis of the investment behaviour and portfolio composition of *takaful* companies. Hence, it should be considered an empirical research–based book.

We hope that the material and the findings presented in this book can shed some light on our understanding of the portfolio composition and investment behaviours of *takaful* companies, which are also related to the development of and product diversity in the IBF industry.

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