

# Successful Drivers for Islamic Finance in the U.S.

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The history of contemporary Islamic finance is quite brief, and its history in the United States is even shorter. Yet the factors that have driven its establishment and successes in the U.S. are quite similar to those in Muslim nations, despite the very different contexts. Nearly all of the many practitioners surveyed for this article seem to agree that the key drivers for the success of Islamic finance in the U.S. have been, and are, the American Muslim demographic, the depth and sophistication of the U.S. as a marketplace, and a general increase among members of various faiths, not only Muslims, in engaging in socially responsible or faith-based investing.

Studies regarding American Muslims have shown them to be a sizable, well-educated, responsible, wealthy population segment in the United States. As this population has aged, it has “spiritually matured to seek Islamic alternatives to its financial activities,” according to Monem Salam of Saturna Capital. Adnan Durrani, chief halal officer at American Halal Co., which aims to become the major provider of halal foods nationwide, sees a number of parallels between the growth and success of socially responsible investing and Islamic alternatives, having himself been actively involved in both.

“Looking after society, the environment, shareholders and employees in a responsible, just and holistic manner are broadly appealing virtues,” Durrani says. As one might expect, many financial institutions have come to appreciate the virtues of the American Muslim demographic, seeking to educate themselves about this market’s needs and the opportunity presented by serving it.

#### On the Grow

Responding to their faith first and foremost, and then recognizing the significant market potential, American Muslims over the past 20 to 25 years have elected to address their own demand for Islamic retail products. These efforts have largely been pointed towards home and auto financing and then to investment vehicles. With the passage of time and the maturation of this demographic, these efforts have increased and gained not only in momentum, but in capability and sophistication as well.

Efforts to establish an Islamic bank within the U.S. are well under way with various governmental and regulatory support efforts, such as those of the U.S. Treasury generally and the Federal

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Home Loan Mortgage Corporation (Freddie Mac) in the realm of mortgage financing.

Most recently, the market has witnessed the success of Guidance Financial as well as University Bank, LaRiba and Devon Bank in the realm of residential financing across numerous states. Michigan-based University Islamic Financial Corp., a subsidiary of University Bank, currently lays claim to having the first unit wholly devoted to Islamic banking, offering home financing and deposit products and expanding its operations. Chicago-based Devon Bank also offers mortgage and business financing as well as lines of credit on an Islamic basis. Zayan Finance is currently establishing itself as one of the first Islamic financiers to provide standardized commercial real estate financing.

Investment vehicles for American Muslims remain few. However, one of the most important developments for Islamic equity investments globally comes from within the U.S.: the issuance (and

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subsequent revision) of a fatwa by the Dow Jones Islamic Indexes' Shariah Board, outlining parameters for permissible equity investments and leading to the establishment of Islamic indices by Dow Jones and, subsequently, FTSE, MSCI and Standard & Poor's. These parameters are often followed by money managers and also serve as guideposts in the realm of private equity and real estate investing. Such parameters are similar but not necessarily identical to those relied upon by Saturna Capital (the activities of which preceded the Dow Jones fatwa) and Azzad Asset Management in managing well-regarded Islamic mutual funds in the U.S.

Significant demand for additional investment vehicles (for both accredited and nonaccredited investors) remains unaddressed. Funds that allow for diversification and open other markets to American Muslim investors on an Islamic basis, such as real estate, will be important contributions to the U.S. Islamic marketplace.

Islamic insurance appeared during the 1990s and then disappeared; nonetheless, demand for it remains and will likely begin to be addressed in the short term. Most recently, American Muslim efforts at providing small- and medium-sized business financing have begun to coalesce. The significant local demand for property construction-financing products in the residential and commercial realms exists but is only beginning to be addressed.

Having begun to appreciate the vast potential of the American Muslim market, some foreign

financial institutions, namely, United Bank of Kuwait and HSBC, have offered home mortgage products. Other prominent banks, both foreign and domestic, are expected to contribute to the fur-

ther development of the market, as they too come to appreciate its potential. American Muslims will look to see a long-term commitment from financiers; anything less appears to further the skepticism surrounding Islamic finance, which will be remedied by persistent education and practice that meets principles.

#### Outside Looking In

The bulk of Islamic finance activity in the U.S. comes from foreign institutions transacting for themselves or for their non-U.S. investors. They structure investment opportunities in real estate projects and equipment and also make a variety of



private equity investments, whether as

full-fledged funds or single transactions. For those foreign buyers with sophisticated diversification strategies, U.S. assets (and, perhaps, distressed assets in the current market in particular), remain an important portfolio constituent for a variety of reasons.

There appears to be a general consensus among foreign investors with whom we spoke that "the U.S. stands as one of the largest, deepest and most mature markets of any single nation with a broad array of well-developed industries, assets and opportunities," according to Tariq Malhance, president of Chicago-based UIB Capital Inc., which is engaged in Shariah-compliant private equity.

Motivated by the current rise of petrodollar-fueled liquidity, local institutions have become and will continue to be responsive to this significant foreign Islamic institutional demand. These U.S. or domestically located institutions, especially in light of the current credit crisis, "must be flexible and creative, particularly with legal and Shariah structures, if they are to successfully engage investors from these regions," according to Naveed Siddiqui, chief executive officer of Zayan finance. Within this credit crisis, some institutions have come to appreciate the "discipline of many Islamic investors with respect to the utilization of debt," Malhance said. Creativity with product offerings, such as vehicles enabling investments in distressed assets that might be of particular interest in the current climate, is also likely to be important as well in order to continue the flow of foreign Islamic investment.

None of those surveyed thought U.S. regulations, particularly those applicable to investments by foreign persons into the U.S., posed an obstacle to the success of Islamic finance. This is consistent with our experience; foreign investors are keen on doing business, respecting boundaries and building the relationships necessary to do so. In fact, when asked about challenges, most in the industry seem to focus on the need to continue educating financial institutions, regulators, American Muslims and the market generally in the spirit of information sharing, education and dialogue. "Finance and food are great uniting forces," Mr. Durrani offered, "by which we bring communities together."

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