



Development of Islamic finance in Kazakhstan: Reality or myth?



Shaimerden Chikanayev is a partner and **Dinara Otegen** is the associate at Grata Law Firm. They can be contacted at schikanayev@gratanet.com and dotegen@gratanet.com.



The question of whether or not there is any Islamic finance development in Kazakhstan is not easy to answer. There is definitely strong support from the government of Kazakhstan for Islamic finance as an alternative source of funding for infrastructure, SMEs, agriculture and such. But although Kazakhstan adopted relevant legislation for domestic Islamic banking transactions such as the governed Kazakh law more than ten years ago and established the Astana International Financial Center (AIFC) based on the Dubai International Financial Center's model three years ago, Islamic finance is still in the early stages of its development and Islamic products are rarely used.

According to the National Bank of Kazakhstan (NBK), as of 2019, the share of Islamic banking assets account for only 0.21% of the total banking sector assets in Kazakhstan. One may argue that there is more talk about Islamic finance rather than real business all these years and that there is no real market demand for Shariah compliant finance in Kazakhstan. Thus the big question of whether there is any real development of Islamic finance in Kazakhstan or not.

Recent developments

In efforts to become the Islamic financial center of the Eurasian Economic Union and Central Asia, Kazakhstan has so far adopted three sets of legislative amendments in 2009, 2011 and 2015. The AIFC that was established in 2018 adopted the Master Plan (Roadmap) for the development of Islamic finance in Kazakhstan, which provides measures for developing Islamic finance activities in the country in terms of further legislative changes and such. Because of the aforementioned initiatives of the government of Kazakhstan that created a specific legal and regulatory framework for Islamic finance, there are two fully operating Islamic banks in Kazakhstan – Al Hilal Bank and Zaman Bank, which was previously a commercial bank but received permission from the National Bank of Kazakhstan (NBK) in 2016 to convert into an Islamic bank.

In addition, an Islamic leasing (Ijarah) company – Kazakhstan Ijarah Company; an Islamic mutual insurance company – Mutual Insurance Company Takaful; and a multifunctional Islamic financial organization – Al Saqr Finance are all present in Kazakhstan. Importantly, there is no unified Islamic finance law in Kazakhstan. Instead, domestic Islamic finance transactions are regulated by Kazakhstan's general banking, securities, insurance and other relevant legislations. Foreign Islamic financial institutions are not allowed to offer regulated Islamic banking and capital market services in Kazakhstan (for example, they cannot be treated as a Kazakh Islamic bank or a Kazakh insurance firm), but they can, generally, engage in cross-border Islamic finance transactions, such as cross-border Sukuk. Generally, Kazakh law treats Islamic products equally with their corresponding conventional products so that there is a level-playing field for Islamic finance. For instance, so-called Kazakh Islamic banks incorporated in Kazakhstan are treated more or less in the same way as Kazakh conventional banks.

Islamic banking

The principal authority charged with the oversight of Islamic and conventional banking, capital markets and insurance products is the NBK, ie there is no specific supervisory authority for Islamic financial institutions.

A Kazakh Islamic bank is a Kazakh commercial bank (ie it shall be incorporated as a Kazakh joint stock company), created as such but with an Islamic banking license issued by the NBK.

An Islamic banking license authorizes a Kazakh Islamic bank to conduct, inter alia, the following specific operations: accept interest-free demand deposits, and finance commercial operations through the purchase/sale of goods or by way of participation in projects, leasing and such. In February 2016, the first project in the framework of Islamic finance using the Ijarah product (Islamic leasing) was implemented in Kazakhstan by Development Bank of Kazakhstan. In addition, Islamic Bank Al Hilal expanded its range of services by launching Islamic banking products for individuals in 2017. Islamic insurance Kazakhstan law specifically provides for such concepts as Takaful and Takaful operators. Islamic insurance under Kazakh law is a system of mutual protection where one policyholder pays to reimburse the losses of another policyholder, the pool for which is managed by a Takaful operator. Takaful must be carried out by Kazakh Takaful operators only.

Islamic capital market

Kazakh Islamic securities certify the right of their holder for the portion of the material assets and the right to the disposal of such assets and the income derived from such assets, services and other assets of the particular projects for financing of which Islamic securities have been issued. Kazakh Islamic securities include shares and units of Islamic investment funds, Islamic lease certificates, Islamic participation certificates and other securities recognized as Islamic securities by Kazakh law. Importantly, Kazakh Islamic securities may be paid only in cash. The prospectus of Islamic securities shall be approved by the so-called council on the principles of Islamic finance that may be engaged by the issuer based on the agreement.

In 2012, the Development Bank of Kazakhstan issued a RM240 million (US\$53.87 million) 5.5% Sukuk Murabahah facility under its RM1.5 billion (US\$336.66 million) Islamic medium-term note program. To the best of our knowledge, however, these Sukuk facilities were issued on a cross-border basis and were governed by foreign rather than Kazakh law (issued in accordance with Malaysian law) and therefore cannot be considered as Kazakh Islamic securities. Interestingly, the board of directors of the Development Bank of Kazakhstan, on the 23rd February 2017, decided to annul this RM1.5 billion program with full satisfaction of current liabilities by the 31st December 2017. According to the Ministry of Finance, Kazakhstan plans to place Sukuk on the AIFC exchange in the next two years. The placement of sovereign Sukuk will be the huge step forward to the development of the Islamic finance in Kazakhstan, and a sign to the investors that the government of Kazakhstan is particularly interested in Islamic finance.

Conclusion

Taking all of the aforementioned points into account, Kazakhstan, evidently, already has a decent legal and regulatory framework for both the domestic Islamic finance industry and for cross-border Islamic finance transactions and, therefore, it seems that there is a real development of the Islamic finance in Kazakhstan. Such developments, however, are made in small steps. ☺