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”Après nous, le déluge” towards a shock theory of Islamic green finance

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"Après nous, le déluge"

towards a shock theory of -Islamic green finance

Salim REFAS & Ezzedine GHLAMALLAH



CONTENT

- 1. INTRODUCTION: GLOBAL AGENDAS, FINANCING GAPS AND MACROECONOMIC RISKS**
- 2. THE BIRTH, DEVELOPMENT AND EXPECTED FUTURE OF ISLAMIC GREEN FINANCE**
- 3. A SHOCK THEORY FOR THE DEVELOPMENT OF ISLAMIC GREEN FINANCE**
- 4. CONCLUSION, A MATTER OF URGENCY FOR THE WHOLE ISLAMIC FINANCE SECTOR**

1- INTRODUCTION : GLOBAL AGENDAS, FINANCING GAPS AND MACROECONOMIC RISKS

GLOBAL AGENDAS adopted in 2015 but issues in implementation and new systemic risks to be faced

- **SDG and Paris agreement financing needs are not met.**
- **Major climate catastrophes are disrupting development of poor nations.**
- **COVID-19 pandemic** has erased decades of economic progress, poverty reduction, and gains in human development
- **Dramatic global political, economic, financial and potentially direct military confrontation** between NATO countries and Russia causing rising inflation and supply shocks in global supply chains.



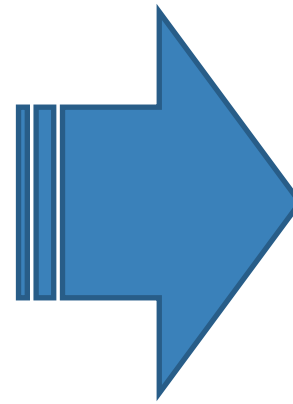
THE RECESSION SHOCK IS COMING and SEEMS UNAVOIDABLE



1- INTRODUCTION : GLOBAL AGENDAS, FINANCING GAPS AND MACROECONOMIC RISKS

RAISING AWARENESS and mobilization for global action but the world is ill-prepared for major shocks

- Total annual investment in developing countries is \$1.4 trillion, **leaving an annual investment gap of \$3.1 trillion to achieve the SDGs** (IsDB, 2019).
- The **macroprudential policies under development** are **welcome but are not commensurate and radical enough** to rapidly adapt the regulatory frameworks to new macroeconomic contexts.



THE TRANSFORMATION
TOWARDS GREEN, RESILIENT
and INCLUSIVE DEVELOPMENT
PATHWAYS is only
“INCREMENTAL” where it should
be RADICAL AND IMMEDIATE.



During the shock:
**DISASTER
MANAGEMENT &
RESILIENCE**

After the shock:
**RECOVERY AND
RECONSTRUCTION**

Before the shock:
**MITIGATION AND
ADAPTATION**



WHAT TO DO ?

Refas. S & Ghلامallah. E

"Après nous, le déluge" towards a shock theory of Islamic green finance

2- THE BIRTH, DEVELOPMENT AND EXPECTED FUTURE OF ISLAMIC GREEN FINANCE

ISLAMIC FINANCE has developed rapidly since 1970s but has started adopting principles and tools of responsible finance and climate only since 2009

Islamic finance is one of **the fastest growing segments of the global financial system** growing since its debuts in the 1970s to an industry of \$2.88 trillion globally by the end 2019 and forecasted to grow to \$3.69 trillion by end 2024 (ICD-REFINITIV, 2020).

The adoption in 2009 by the International Fiqh Academy **of a *fatwā* prohibiting, according to the principle of removal of corruption (*dar' al-mafasid*), environmental damage that harms the ecological balance or uses resources in an unsustainable way and do not take into account the interests of future generations** was a decisive act.




PROTECTION OF THE ENVIRONMENT AND MITIGATION OF CLIMATE CHANGE becomes a RELIGIOUS OBLIGATION and A PARADIGM CHANGE for the whole Islamic Finance industry is CALLED UPON

2- THE BIRTH, DEVELOPMENT AND EXPECTED FUTURE OF ISLAMIC GREEN FINANCE

Perspectives of Islamic green finance (IGF) development under current market conditions

Islamic green finance now represents about **1-2% of IF industry**, so it's a niche of niche industry. One main reason pertains to the process of development of IGF:

- IGF is developing through **policy transfer** from conventional green finance policies => the policy outcomes and the success of IGF is dependent on the success of conventional green finance policies;
- The **process of policy transfer does not initiate from market demand** and carries a heightened risk of negative market perceptions
- Due to the **lag in transferring relevant policies from conventional finance**, combined with the lag for evaluation of Shari'ah compatibility of the new policies and instruments before implementation, IGF will be developing at a reduced pace and is exposed to **risks of institutional obsolescence**




The window of opportunity is expected to be largely missed without radically different policy formulation and market development

3. A SHOCK THEORY FOR THE DEVELOPMENT OF ISLAMIC GREEN FINANCE

Despite the alignment of ethical principles of Islamic finance with the principles of Green finance and climate action, **a central assumption of this paper is that a massive transition from the current consumption-driven and unsustainable Islamic finance industry cannot happen unless a major economic, social or political shock triggers this transition.**

- 1. First assumption:** only systemic risks can provoke the magnitude of change needed to effectively transform the Islamic economies towards sustainable and climate-resilient pathways
- 2. Second assumption:** by transferring and adopting a package of reforms and policies from different contexts (developed economies, pre-shock context), **the IF industry is actually missing the preparation needed for this transformation**

3. A SHOCK THEORY FOR THE DEVELOPMENT OF ISLAMIC GREEN FINANCE



What are the critical conditions and policy directions to build back better after a systemic change and effectively develop an IGF sector that would support the economy for a sustainable and equitable future for all?

3. A SHOCK THEORY FOR THE DEVELOPMENT OF ISLAMIC GREEN FINANCE

Critical conditions for the development of Islamic Green Finance in the aftermath of a systemic shock

- **Critical condition 1:** Government stability;
- **Critical condition 2:** Mass urban relocations;
- **Critical condition 3:** De-commoditization of consumption;
- **Critical condition 4:** state control over unsustainable industries;
- **Critical condition 5:** dematerialization of the economy through technology and state planning;
- **Critical condition 6:** a large-scale reconstruction financing program tied to mobilization of human capacities and natural resources;
- **Critical condition 7:** an interventionist policy to salvage and consolidate the banking sector and transition to Islamic Green Finance.

4. CONCLUSION, A MATTER OF URGENCY FOR THE WHOLE ISLAMIC FINANCE SECTOR

The world is waking up from the shock of the COVID-19 with a firm and resolute global commitment: **“Build Back Better.”** But COVID-19 was probably “just a severe warning” to a much deeper crisis forthcoming.

The next major global crisis will arguably determine the fate of most vulnerable nations in the next decades and of the NEXT TWO GENERATIONS of human beings at least.

The current global IF institutions are not equipped with capabilities and resources to adopt packages of reforms radical enough to bring rapidly enough the sector back on track before the crisis hits.

Seven conditions are identified and more research is needed to better explore and prepare the aftermath of the next global shock.

Thank you!

Questions?



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