Growth and Development of the Malaysian Islamic Capital Market

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Capital markets play a very important role in modern economies. Being a part of the financial sector, which they share with the banking system, capital markets have become the focus of many a government's development plans. Most developing countries' financial sector tends to be dominated by the banking system. As countries develop, capital markets begin to take on a bigger role. In most developed markets, the capital market is far larger than the banking system. In the case of Malaysia, the real impetus to capital market development began after the 1997–1998 Asian financial crisis. The crisis laid bare the vulnerabilities of a bank-dependent system. Policymakers saw the need for a well-functioning capital market, especially a bond market. Accordingly, capital market development in Malaysia owes much to two encompassing plans undertaken by the government. These are the Capital Market Masterplans 1 and 2. The first Capital Market Masterplan covered the period from 2001 to 2010 while the second will run from 2011 to 2020. Implemented by the Securities Commission although under the purview of the Ministry of Finance, these two ten-year masterplans were launched with the objectives of providing both the synergy and focus needed in building well-functioning markets and creating a globally competitive capital market and a vibrant Islamic finance hub. While the first plan was focused on establishing and developing the markets, the second plan is aimed at enhancing quality. Its stated objective is growth with governance.

Today, the Malaysian capital market is probably the most developed in the Muslim world. Like most other Muslim countries, Malaysia operates a dual model, with both conventional and Islamic components of the capital market operating in tandem. As is the case in banking, the two systems operate in parallel. Malaysia however, has been able to bring to bear Shari’ah compliance on all the components of a fully developed capital market. Thus, the equity, debt/bond, money/interbank, derivative and foreign exchange markets all have Shari’ah-compliant equivalents. This makes Malaysia unique, in that, no other Muslim country has been able to replicate all key components of a conventional capital market in a Shari’ah-compliant capital market. Aside from the strong government support and a deliberate strategy to make Malaysia a hub for Islamic finance, several other factors like better rule of law, a greater degree of openness and a sound institutional setting have helped to position the country as a leading global market in Islamic finance.