

THE ROLE OF SHARIAH INVESTING IN THE NEW NORMAL

Discover how Shariah investing offers resilience, ethical alignment and diversification benefits, emerging as a sustainable path for building long-term wealth.

As we step into 2024, global markets are poised to enter yet another 'new normal' regime marked by higher interest rates and the onset of a fresh economic cycle. Against this backdrop, investors are actively looking for strategies to diversify their portfolios and optimise risk-adjusted returns.

Simultaneously, societal shifts are taking shape, and financial gains are no longer the sole imperative of investors. More investors are now seeking to align their portfolios with their own values as sustainability considerations become mainstream.

Enter Shariah investing, which stands out as a compelling choice to bridge this gap by providing a unique mix of resilience, ethical screening and diversification benefits that can appeal to a broad spectrum of investors.

STEADFAST IN UNCERTAINTY

Historically, Shariah equities have displayed resilience in the face of market volatility. The inherent screening process in Shariah-compliant investments contributes to the defensive nature of the underlying assets. This is achieved by focusing on companies with strong balance sheets while excluding those burdened with high levels of debt.

This resilience was evident in markets during the Covid-19 pandemic, when economies were shuttered and supply chains were under strain. The MSCI World Islamic Index posted a total return of 43.80% over a period of 3 years, outpacing the MSCI World Index, which recorded a return of 34.00%¹. Notably, sectors such as technology, energy and healthcare, which carry heavier weights in Islamic indices, played a pivotal role in driving these gains.

While valid concerns about a potentially smaller investment universe exist, Shariah investing has proven its ability to not only keep pace with its conventional counterparts but in some cases, even surpass them in terms of performance despite such limitations.

By prioritising quality over quantity, Shariah investing zeroes in on businesses with robust financials. This emphasis on quality contributes to the resilience of the portfolio, even within a potentially smaller universe.

Moreover, Shariah investing has steadily expanded its global

reach and embraced innovation over the years. This has led to an enhancement of the breadth and depth of the Islamic capital market, coupled with increased access to international markets. As such, the globalisation of Shariah investing not only broadens the scope of investment opportunities but also enhances its adaptability.

Subsequently, this expanded reach has contributed to the versatility of Shariah investing, allowing it to cater to a wide range of investment objectives, encompassing both growth and income strategies.

In many ways, Shariah investing also inherently encourages investors to practise a long-term investment horizon due to its principles. By avoiding speculative and high-risk ventures, Shariah-compliant investments align with the patient capital approach. A deliberate focus on long-term sustainability contributes to the resilience of Shariah investments in weathering short-term market fluctuations.

DRIVING POSITIVE IMPACT

The pandemic has helped push the reset button on sustainability and forced many businesses to rethink the ways they operate. But is it here to stay?

In our view, as long as social and environmental imbalances remain and the world population demands greater action, sustainability trends will persist and become structural. Indeed, it has now become a global movement that has compelled asset managers and investors to align with these principles.

By virtue of its position as an Islamic finance hub, Malaysia sits in a strategic spot to seize opportunities in this landscape. A growing convergence between Shariah and sustainability principles provides us with a distinctive advantage to capitalise on demand for more purpose-driven solutions or value-based offerings.

While sustainability and Shariah investing are often viewed as separate universes, in truth both

share many similar parallels, such as their emphasis on good governance, social responsibility as well as preservation of life and the environment.

The myth that sustainable investing leads to lower returns has been debunked over the years, with numerous empirical studies showing a positive correlation between the two. By avoiding companies operating in unethical industries that are not well positioned for the future, investors reap the benefits of enhanced risk management, with sustainability factors increasingly becoming performance drivers.

For example, we have seen the share price of companies with poor Environmental, Social and Governance (ESG) scores being punished as global fund managers shun these companies. Conversely, companies with higher scores could

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have more ethical business practices, leading to improved stakeholder engagement that drives value creation over the long term.

SEA OF OFFERINGS

By leveraging on its status as an Islamic finance hub and its extensive Shariah expertise, Malaysia has cemented its position in the Shariah wealth landscape. According to data from *Morningstar*, Malaysia alone accounts for nearly 50% of the total number of Shariah-compliant funds available globally².

Strides in technology have further democratised access, making it easier and more convenient for investors to tap into distinct Shariah investment strategies to meet their goals.

For investors navigating this vast realm, it can be overwhelming to decide what or where to invest. Hence, a fund-of-funds (FoF) structure offers a convenient gateway to tap into the best-in-class Shariah investment strategies through a single solution.

While a FoF structure is more common in the conventional space, the Shariah investment landscape is also seeing similar leaps in terms of


product innovation. This has provided investors with more efficient ways to optimise returns and diversify risk.

By harnessing the expertise of multiple asset managers and selecting the best ideas across various markets, investors can access global opportunities in a seamless and efficient manner through a FoF. This approach minimises concentration risks and enhances diversification by transforming a bucket of Shariah funds into a broadly diversified portfolio.

Furthermore, through its screening process, there is a deliberate focus on companies with lower gearing ratios. This not only enhances the resilience of the funds, making them less vulnerable to economic shocks, but also aligns with Shariah principles by promoting risk-sharing among all the stakeholders involved.

AIIMAN Asset Management, alongside our parent company AHAM Asset Management have played a notable role in advancing the FoF product landscape in Malaysia. Our Smart Invest FoF series are designed to cater to a wide range of risk profiles and investment objectives including investors with a preference for a Shariah-compliant option.

As investors traverse a new normal landscape in 2024, Shariah investing offers a more sustainable path for investors to build long-term wealth while aligning their portfolios with ethical or sustainable considerations.

Fortunately, starting one's investment journey has never been easier today with a plethora of Shariah-compliant offerings available, coupled with ease of accessibility due to technological advancements. 

Sources

1. *Bloomberg*, as at 30 November 2023, in MYR terms
2. *Morningstar*, *Shariah-Compliant Funds Gain in Popularity and Outperform*, 2023



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Akmal Hassan is the Managing Director of AIIMAN Asset Management. As one of the pioneering members in the establishment of the company since 2010, Akmal has steered AIIMAN to becoming one of the fastest-growing Shariah-compliant asset managers in Malaysia, with a clear focus on delivering performance and building people.