مصرف الإمارات العربية المتحدة المركزي
CENTRAL BANK OF THE U.A.E.

UAE ISLAMIC FINANCE REPORT 2023

THE YEAR OF SUSTAINABILITY

Table of Acronyms

AAOIFI	Accounting and Auditing Organization for Islamic Financial Institutions
ADGM	Abu Dhabi Global Market
CBUAE	Central Bank of the UAE
CIBAFI	General Council for Islamic Banks and Financial Institutions
COP 28	Conference of the Parties of the UNFCCC
DFSA	Dubai Financial Services Authority
DIFC	Dubai International Financial Centre
ESG	Environment, Social and Governance
FSRA	Financial Services Regulatory Authority
GSSS	Green, Social, Sustainability and Sustainability-Linked
HSA	Higher Shari'ah Authority
IFDI 2023	Islamic Finance Development Indicator 2023
IFSB	Islamic Financial Services Board
ISSCs	Internal Shari'ah Supervisory Committees
IsDB	Islamic Development Bank Group
MOCCAE	Ministry of Climate Change and Environment
SCA	Securities and Commodities Authority
SDGs	UN Sustainable Development Goals
SFWG	Sustainable Finance Working Group

Table of **Contents**

Message from the **Governor of the Central Bank of the UAE**

H.E. Khaled Mohamed Balama

Governor, Central Bank of United Arab Emirates

The Central Bank of the United Arab Emirates (CBUAE) is pleased to launch the UAE Islamic Finance Report 2023: The Year of Sustainability. We mark the theme of sustainability in this report as the UAE hosts the 2023 UN Climate Change Conference (UNFCCC COP 28) this year. This study showcases our approach to support the development of Islamic finance within the UAE. It is also in line with the vision of the UAE's leadership and its strategy to promote sustainable growth within the financial sector—Islamic finance included—and encourage sustainable development.

The UAE is the home to the world's first modern commercial Islamic bank, which was established in Dubai in 1975. Since then, the Islamic banking sector has become an integral part of the UAE's financial industry, accounting for 23% of total banking assets within the UAE in 2022, equivalent to AED 845 billion. The growth in Islamic banking assets in the UAE is supported by strong funding conditions of Islamic banks and Islamic windows. Recent growth has also been driven by the economic activities of retail and corporate consumers despite the increases in benchmark rates. As a systemic component of the banking sector, Islamic banks play an important role in developing and implementing sustainable finance plans and aligning with sector-wide sustainability objectives in support of the initiatives of the Year of Sustainability. Other than the banking sector[1], the UAE is also supporting the takaful sector and sukuk issuances, served by a strong presence of Islamic financial institutions and an enabling industry ecosystem.

This report provides an overview of the performance of the different Islamic financial sectors that shape the industry as a whole. The study also covers the diverse ecosystem of the industry, including the legislative, regulatory and Shari'ah governance landscape, as well as human capital development and innovation within Islamic financial institutions. These contributions and sectors are important for the holistic development of the Islamic finance industry.

As the industry increasingly aligns itself with sustainability practices, we see the strategies and operations of Islamic financial institutions following suit, as indicated by our UAE Islamic Finance Sustainability Survey. This survey was developed to capture the sustainability strategies and practices of the Islamic finance industry in the UAE. The results illustrate that all Islamic banks in the UAE have sustainability strategies in place a key foundation to support the transformation required by the Islamic finance industry to support a more sustainable future.

This is further strengthened with the release of the Guiding Principles Regarding Sustainability in Islamic Financial Institutions by the Higher Shari'ah Authority. The Guidance adds to the Central Bank's sustainability agenda, which is a key focus area of our strategic plan, and covers regulatory, supervisory and risk management aspects.

We will continue our efforts to support the development of Islamic and sustainable finance sectors in the UAE and we hope the findings of this report will provide a meaningful impact towards achieving a sustainable future.

Message from the **Higher Shari’ah Authority Chairman, CBUAE**

H.E. Eminence Sheikh Dr. Ahmed Bin Abdulaziz Al Haddad

Higher Shari’ah Authority Chairman, Central Bank of United Arab Emirates

The principles of Islamic law and Shari’ah are inseparable from the ethical and social values of Islam with regards to the objectives relating to the protection of life, wealth, intellect, progeny and faith, all of which span across generations. The fundamental alignment of Shari'ah principles with the concepts that have been embedded in sustainability provides Islamic finance with a clear rationale to lead on the sustainability front.

In 2023, the UAE Higher Shari'ah Authority issued guidance concerning the application of sustainability within Islamic financial institutions. The document roots the responsibility for action on environmental and social impact in the requirements associated with ownership of assets. We believe that this provides a strong starting point for Islamic financial institutions to adopt sustainability and engage in sustainable finance as best practice in alignment with Shari'ah principles. Such guidance and other initiatives on Islamic sustainable finance are reflected upon in this report.

We are pleased to launch this report during the Year of Sustainability and coinciding with the UAE hosting COP 28. We ask Allah that it serves as a meaningful reference for the market to align Shari'ah principles with sustainable finance.

Message from the **Assistant Governor of the CBUAE, Banking & Insurance Supervision**

Ahmed Al Qamzi

Assistant Governor, Banking and Insurance Supervision, Central Bank of United Arab Emirates

The UAE Islamic Finance Report 2023 provides an overview of the development of Islamic finance sectors and supporting ecosystem alongside recent UAE initiatives focused on ESG and sustainable finance.

The report showcases the evolution of Islamic finance in the UAE and supporting regulatory and Shari'ah frameworks. The report also denotes the sustainability practices and strategies are being increasingly adopted and instruments such as green financing and green sukuk are becoming available to support the scaling of sustainable finance and to combat climate change.

These are further supported by a robust ecosystem. For instance, to solidify our efforts towards developing Islamic finance, the Commercial Transactions Law (Federal Decree-Law No. 50/2022) was introduced, and this will be supported by the CBUAE and HSA by the issuance of by-laws related to the Articles of this law.

This study also exclusively reports on the findings of the UAE Islamic Finance Sustainability Survey, which gives insight into the adoption and outlook of sustainability practices and strategies by Islamic financial institutions. The survey covers responses by Islamic banks, Islamic banking windows, and Islamic financing companies that capture their ESG and sustainability strategies. Among the key findings of the survey is that 83% of Islamic banks have planned financial commitments for sustainability in the coming three to five years, while 68% of Islamic banks and Islamic windows implement an ESG impact-based risk assessment framework when deciding extending financing or investment. This indicates strong sustainability alignment and positive steps towards the future of sustainable Islamic finance.

We are confident that this report will further support the development of the sustainable Islamic finance industry in the UAE.

Islamic **Finance and Sustainability** Overview

Global and UAE **Islamic Finance Overview**

The Islamic finance industry continued to grow in 2022, expanding a further 11% to AED 16.5 trillion. The industry has grown 69% over the past five years and 163% over the past ten, according to the Islamic Finance Development Report 2023 (IFDI 2023), produced by the Islamic Corporation for the Development of Private Sector (ICD), and the London Stock Exchange Group (LSEG).

Growth is being chiefly driven by Islamic banking, which accounted for around 72% of total Islamic finance industry assets in 2022, followed by Sukuk. The main Islamic finance markets are to be found within the GCC, Southeast Asia and South Asia. The UAE is the world's fourth largest Islamic finance market.

Figure 1.1 Global Islamic Finance Assets in 2022 **(AED Billion)**

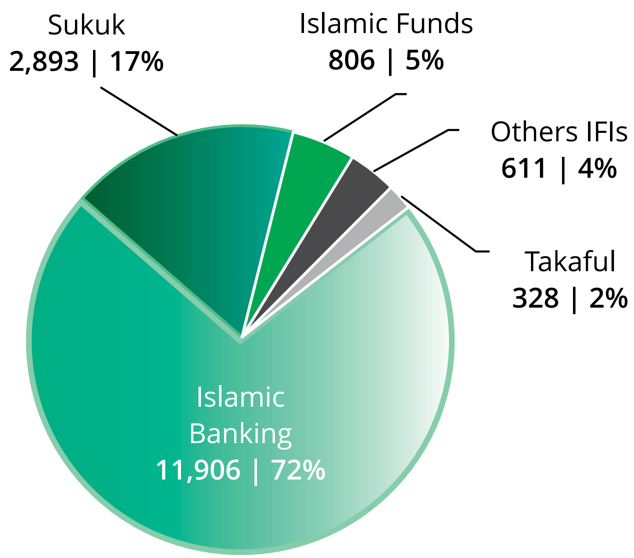
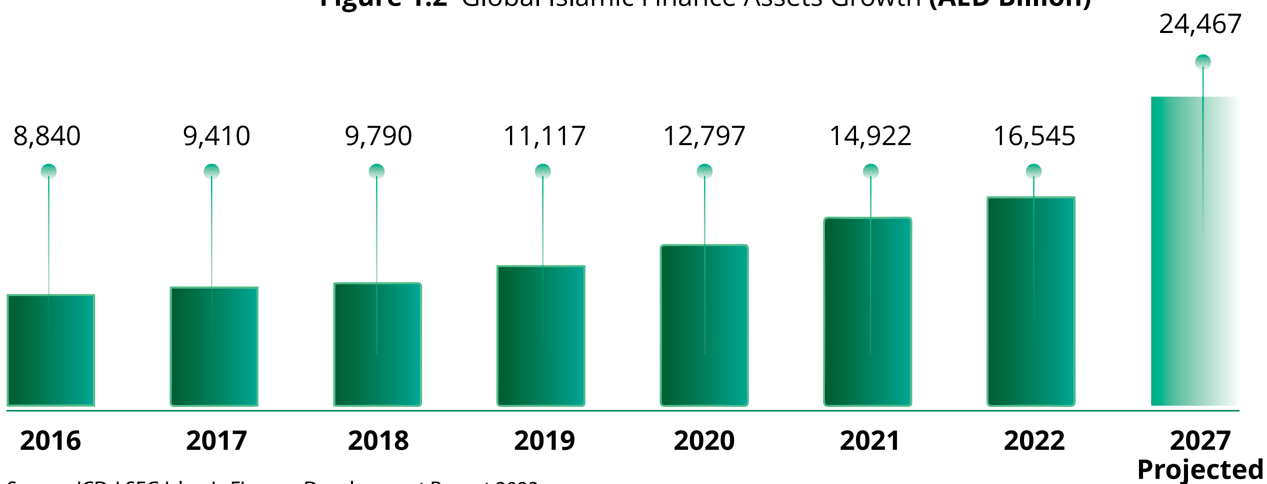


Figure 1.2 Global Islamic Finance Assets Growth **(AED Billion)**



Source: ICD-LSEG Islamic Finance Development Report 2023

The UAE's **Islamic finance landscape and governance ecosystem**

Since the establishment of the first Islamic bank, the Islamic finance industry in the UAE has developed across a range of areas including Islamic banking, finance, takaful and sukuk. The industry has become an integral part of the UAE's financial industry, and is supported by a robust and conducive regulatory environment, with harmonised Shari'ah and legal requirements.

The Islamic banking sector—consisting of Islamic banks and Islamic windows at conventional banks—currently accounts for 23% of the UAE's total banking assets, having grown 16% over the past five years. The UAE's sukuk market is also expanding, and the introduction of local-currency Treasury sukuk by the Federal Government has the potential to encourage the issuance from other players in the market.

The industry in the UAE has witnessed a number of initiatives pertaining to the introduction of conducive legislation and Shari'ah standardisation. These initiatives are aimed at enhancing the stability of the Islamic financial system and enabling the development of innovative products and services. A key development in this area was the issuance of the UAE's Commercial Transactions Law (Federal Decree-Law No. 50/2022), which provided the market with the greater legal certainty it required to grow and innovate.

The UAE's Islamic finance ecosystem, including the Shari'ah governance landscape, is discussed in further detail in **Chapter 1**.

Figure 1.3 Islamic Finance Landscape in the UAE

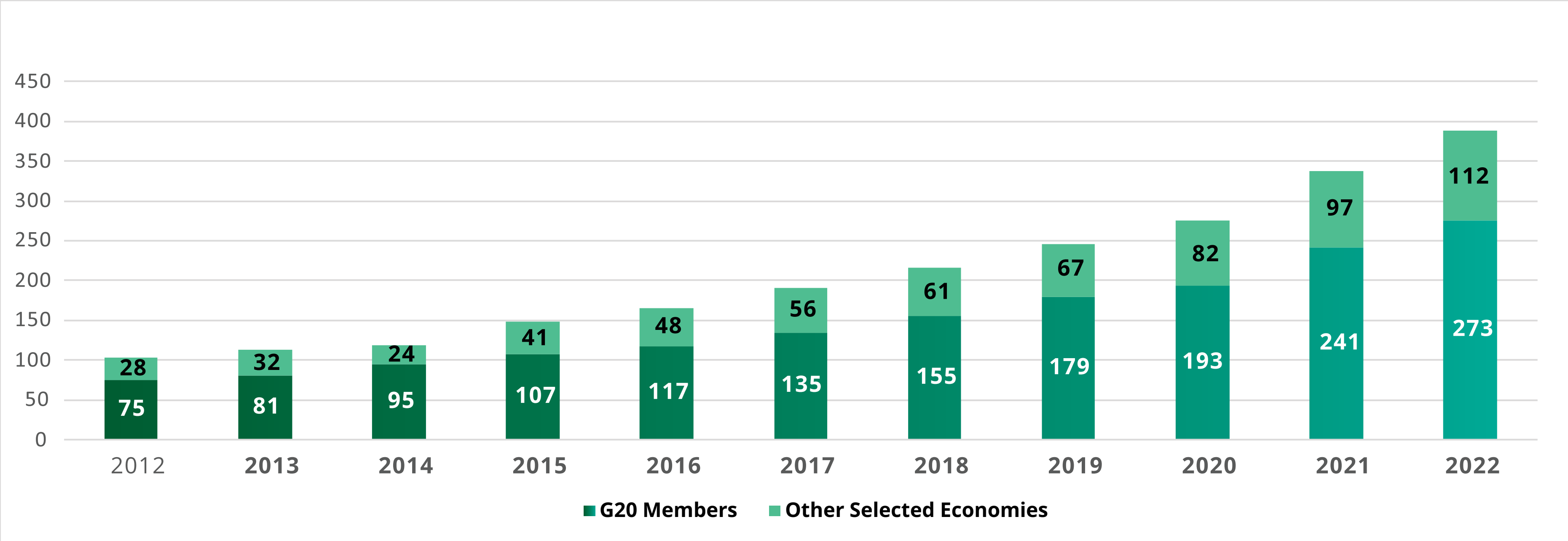
Islamic Banking	Islamic Finance Companies	Takaful Insurance	Sukuk
24 Number of Islamic banking institutions (including Islamic windows) in 2022	**9** Number of Islamic finance companies	**10** Number of takaful insurance companies in 2022	**17** Number of sukuk issued in H1 2023
AED 845 billion Total Islamic banking assets in 2022		**AED 4 billion** Total gross written contributions in 2022	**AED 217 billion** Sukuk outstanding by H1 2023

These and other statistics on the growth of the Islamic finance industry in the UAE are detailed in **Chapter 2**.

Expanding **Regulatory Drive for Sustainability**

Growing global focus on sustainability: Sustainable finance and the financing of sustainable projects are vital tools for achieving the UN Sustainable Development Goals (SDGs). Governments and regulators around the world have over the past decade launched a series of national, regional and international policies and regulations supporting sustainable finance. According to the United Nations Conference on Trade and Development (UNCTAD), in 2022, there were 388 such measures in force in 35 developed and developing economies and country groupings—between them accounting for 93% of global GDP—with 50 introduced in 2022 alone and more than 50 in development.

Figure 1.4 Number of Sustainable Finance Policy Measures and Regulations



Source: United Nations Conference on Trade and Development (UNCTAD) World Investment Report 2023

The UAE's approach towards sustainability: In 2016, a year after the signing of the Paris Agreement, the UAE hosted the UN Environmental Programme Finance Initiative's (UNEP FI) Global Roundtable, which was an important milestone in the development of sustainable finance in the region. The highlight of this event, which included a dedicated session on Islamic finance, was the launch of the Dubai Declaration on Sustainable Finance. With this declaration, 11 UAE financial institutions committed to support the UAE Vision 2021, Paris Climate Accord, and UN Sustainable Development Goals in line with the UAE Green Agenda 2015-2030.

After this, sustainable finance working groups in Abu Dhabi and Dubai worked with local stakeholders to produce their own sustainability initiatives. Abu Dhabi Global Market (ADGM) hosted the first Abu Dhabi Sustainable Finance Forum in 2019 and launched the Abu Dhabi Sustainable Finance Declaration, under the auspices of the CBUAE, ADGM , Ministry of Climate Change and Environment (MOCCAE), and the SCA.

The Declaration was followed a year later by the Abu Dhabi Sustainable Finance Guiding Principles, which included explicit reference to Shari'ah principles and the role of Islamic finance.

The UAE adopted its national Net Zero target ahead of the COP 26 conference in Glasgow in 2021. Abu Dhabi Securities Exchange and Dubai Financial Market also developed voluntary ESG guidance, and became part of the Sustainable Stock Exchange Initiative.

COP 28 is to be hosted by the UAE in 2023. Its presidency calls for increasing the overall levels of ambition, and the UAE in July accordingly announced that it had approved under the Third Update of its Second Nationally Determined Contributions that it had raised its target for emissions to 40% below business as usual by 2030, from a previously targeted 31%.

Sustainability and Islamic finance in the UAE: The world's environmental and social efforts have grown rapidly since the United Nations first introduced the concept of sustainable development in its Brundtland Report of 1987. The Islamic finance industry has been able to play an increasingly active part in this global movement because of the broad intersection of Shari'ah requirements with the aspirations of the SDGs. One indicator of the rapid development of the Islamic sustainable finance industry is how quickly ESG-related sukuk issuance has grown, having totalled AED 120.3 billion in issuance by H1 2023.

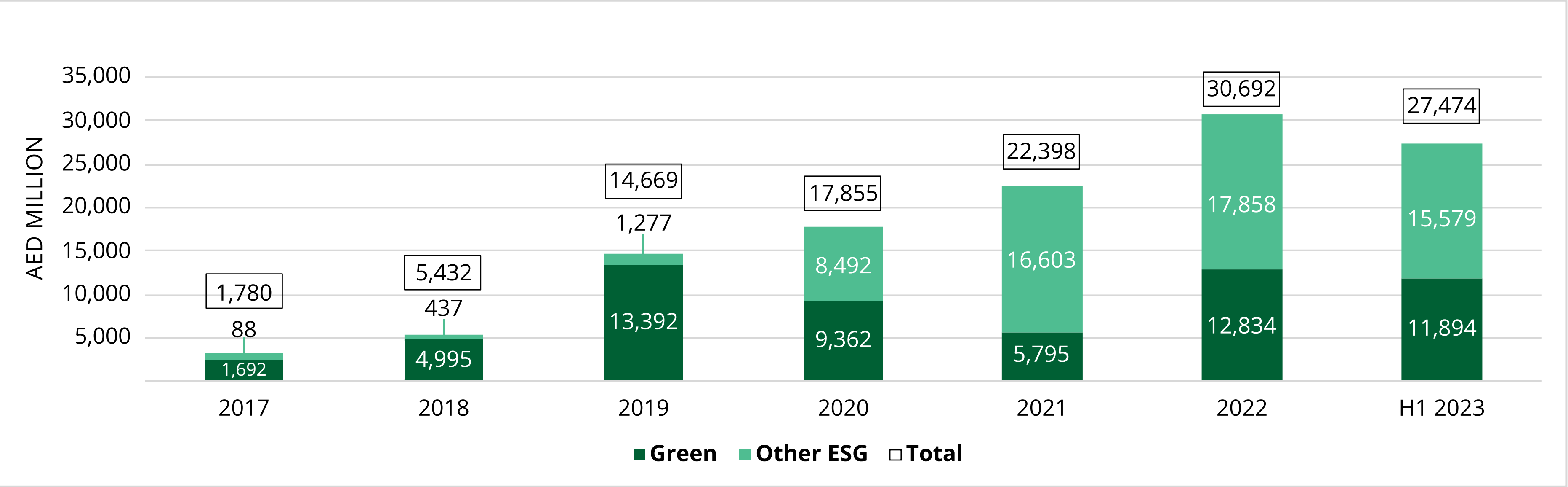
Sustainable finance has also seen rapid growth in the UAE since the country's first green sukuk was issued in 2019, whether through Islamic capital markets or Islamic financing. A breakdown of key transactions and Islamic sustainable finance initiatives by UAE institutions is detailed in **Chapter 3**.

In addition, **Chapter 1** of this report outlines the supporting Islamic finance environment for enabling sustainability as it looks into initiatives towards encouraging digital innovation, enabling Emiratisation, and developing human capital.

Chapter 3 presents a comprehensive picture of the UAE's sustainable finance efforts and initiatives.

In **Chapter 4**, we present the findings of an industry-wide survey on sustainability, which show a clear commitment to sustainability from Islamic banks and Islamic banking windows.

Figure 1.5 Global ESG Sukuk Issuance



Source: LSEG Islamic Sustainable Finance Monitor H1 2023

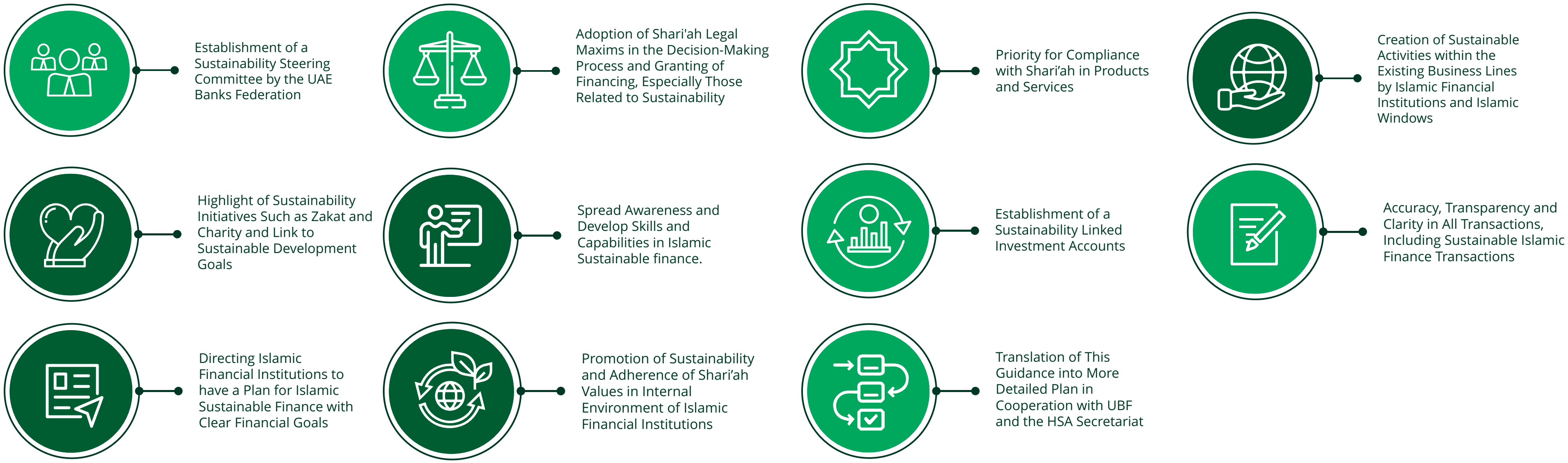
The role of the UAE Higher Shari'ah Authority: The CBUAE's Higher Shari'ah Authority has encouraged Islamic finance institutions to play an active role in sustainable finance through a balanced approach looking at both its environmental and social aspects.

In 2023, the HSA issued guiding principles on the application of sustainability within Islamic financial institutions. The document underlines the Shari'ah foundations of Islamic sustainable finance and the Fiqh approach towards it. The guiding principles integrates the responsibility for action on environmental and social matters within the requirements and the responsibilities assigned to ownership of property rights.

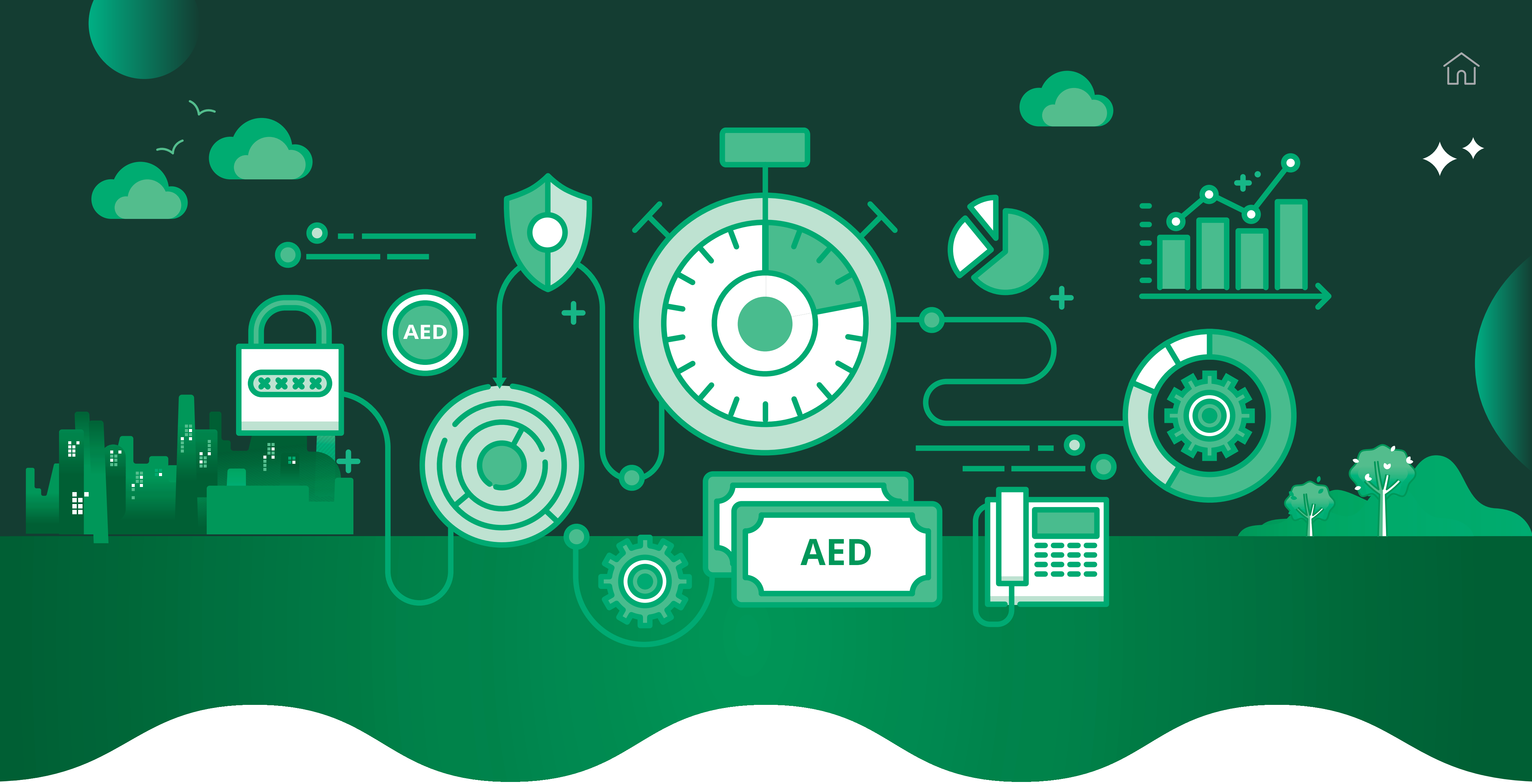
The HSA's central message for Islamic financial institutions in the UAE is that achieving sustainability goals is not only recommended (Mandoob) by Shari'ah; it may be a matter of obligation (Wajib). Therefore, the HSA stated that preventing environmental and social issues is not only recommended, but doing otherwise is highly discouraged or forbidden (Makrooh or Haram).

In order to meet these objectives, the CBUAE is actively working with the Islamic finance industry in the UAE to develop Islamic sustainable finance through HSA directives and other means. In the final quarter of 2022, the UAE Banks Federation established a sustainability steering committee composed of CEOs of Islamic financial institutions and Islamic windows. The Federation will lay out practical and strategic foundations for Islamic sustainable finance and devise a general framework as a basis for a unified and common approach to sustainability and its initiatives among Islamic financial institutions.

Figure 1.6 Summary of the Guiding Principles Regarding Sustainability in Islamic Financial Institutions



Source: Guiding Principles Regarding Sustainability in Islamic Financial Institutions, 2023



CHAPTER ONE: **DEVELOPMENT OF THE ISLAMIC FINANCE SECTOR IN THE UAE**

Evolution of the **Islamic Finance Industry** in the UAE

The UAE's Islamic finance journey: Islamic finance in the UAE started almost 50 years, with the establishment of the world's first Islamic commercial bank in 1975. This was followed by the launch of the first takaful insurance company in the country four years later. Since then, The UAE saw a number of industry firsts, with recent years being characterised by new initiatives in Islamic sustainable finance.

Figure 2.1 UAE Islamic Finance Key Milestones

1970s

1975: UAE and world's first Islamic commercial bank established: Dubai Islamic Bank (DIB).

1979: UAE's first takaful insurance company, Islamic Arab Insurance Company (SALAMA), established.

1980s

1985: UAE Islamic banking law and Higher Shari'ah Authority introduced under Federal Law 1985.

1988: Establishment of UAE's second Islamic bank: Abu Dhabi Islamic Bank (ADIB).

2000s

2002: UAE's second takaful insurance company, Dubai Islamic Insurance and Reinsurance (Aman), established.

Establishment of first Islamic bank, through conversion of conventional bank: Sharjah Islamic Bank.

2004: Sovereign sukuk issued by Government of Dubai and corporate issue by Emaar Properties.

2010-2015

2010: Issuance of CBUAE's Certificate of Deposit.

2014: Government of Sharjah debuts sukuk.

2015: Conversion of Arabian Scandinavian Insurance to a full-fledged takaful insurance company.

2016-2019

2018: DP World receives first sustainability-linked financing in the Middle East to include an Islamic facility.

Establishment of Higher Shari'ah Authority.

2019: First corporate green sukuk issuance in the Middle East, by Majid Al Futtaim.

DFM Launces DFM Shari'ah Index (DFMSI), the first of its kind in the UAE.

2020-2022

2020: Consolidation between two Islamic banks: DIB and Noor Bank. Also, merger between different Islamic finance companies including takaful insurers.

Etihad becomes first airline to issue transition sukuk globally.

2022: Debut sustainable sukuk by Islamic bank in the UAE, DIB.

Enactment of Commercial Transactions Law.

2023

Launch of UAE government domestic Treasury sukuk to develop domestic sukuk market.

Securities and Commodities Authority exempts registration fees for green or sustainability-linked sukuk.

First Abu Dhabi Bank issues first local currency green sukuk.

Higher Shari'ah Authority issues guidance for sustainability at Islamic financial institutions.

Islamic Sustainable Finance Milestones

Islamic Finance **Regulatory Landscape**

Regulatory oversight for Islamic finance: Islamic finance industry began with the 1985 Federal Law on Islamic Banks, Financial Institutions, and Investment Companies. This was the country's first law to introduce the concept of centralised Shari'ah oversight via the HSA and to allow Islamic financial institutions to take part in commercial and real economy activities that differentiated them from their conventional counterparts.

Table 2.1 Milestones in the UAE's Regulatory Journey for Islamic Finance

2004	2010	2014	2018	2020	2022
Law Regulating Islamic Financial Business. By Dubai International Financial Centre (DIFC).	Promulgation of Resolution No. 4 of 2010 concerning takaful insurance by UAE Insurance Authority Board.	Sukuk regulations introduced by Dubai Financial Market and Securities and Commodities Authority.	Adoption of Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) Shari'ah standards by the CBUAE.	Issuance of Shari'ah Governance Standard and the first independent standard for Islamic windows by the CBUAE.	Enactment of Commercial Transactions Law

The current regulatory scope for Islamic financial institutions covers several different areas of the industry in the UAE, including Islamic banking, Islamic finance companies, takaful insurance companies and asset managers, along with sukuk and Islamic funds. These sectors and asset classes are regulated and supervised by the CBUAE as well as others as outlined below:

Table 2.2 Islamic Finance Regulators in the UAE

Regulator	Central Bank of the UAE (CBUAE)	Securities and Commodities Authority (SCA)	Dubai Financial Services Authority (DFSA)	ADGM's Financial Services Regulatory Authority (FSRA)
Regulated Sectors	Islamic banks, takaful insurance companies and Islamic finance companies as well as Islamic windows	Sukuk and Islamic funds	Islamic finance entities* and Islamic funds	
Scope of Regulation	Onshore Regulation		Regulation of DIFC, the Financial Free Zone in Dubai	Regulation of Abu Dhabi Global Market (ADGM), the Financial Free Zone in Abu Dhabi

*Islamic banks, takaful insurance companies, and other Islamic financial institutions

Federal Law 50 of 2022 enhances the UAE's regulatory landscape in Islamic finance: A key milestone for the Islamic finance industry in the UAE was the Commercial Transactions Law (Federal Law 50 of 2022) issued on October 3, 2022. The legislature took into consideration several industrial and technological developments affecting commercial transactions and commerce. It was the first commercial law to recognise and govern Islamic financial transactions in a chapter dedicated to the subject. To further enhance the legal certainty, the law requires reference to the standards and resolutions issued by the HSA for interpreting the articles within that particular chapter of the law (Chapter VI of Book 3 - Banking Operations). The CBUAE and HSA will issue by-laws related to the articles of the law.

The law in meant to provide legal ground for innovative products and services while safeguarding the interests and rights of different concerned parties. It includes several provisions around the main structures used in Islamic finance, such as murabaha (cost-plus financing), istisna (construction and manufacturing financing), salam (forward sale), and ijara (Islamic lease).

Table 2.3 Islamic Finance Areas Covered by Federal Law 50 of 2022

Chapter	Articles	Some Areas Covered
Chapter 1: General Provisions	**Articles 474 - 468**	• Recognition of Shari'ah controls issued or adopted by the HSA as per Federal Law 14 of 2018. This will serve as reference for interpretation of provisions outlined in the Commercial Transactions Law. • The board of directors of the CBUAE shall issue regulations that include controls of the commercial transactions of the Islamic financial institutions that transact their business according to Islamic Shari'ah provisions, having been approved by the HSA. • Covered transactions are: deposits, investment accounts, takaful insurance, finance forms, investments, and any transactions governed by Shari'ah principles.
Chapter 2: Special Provisions of Certain Types of Contracts and Obligations to Which the Islamic Financial Institutions are a Party	**Articles 496-475**	• Promise of Contracting • Sale in Instalments • Murabaha • Toll Manufacturing* • Forward Sale • Lease
Chapter 3: Islamic Banking Operations	**Articles 497**	CBUAE will issue decisions on Islamic banking operations, administrative sanctions and penalties in case of breach of regulations

*Toll manufacturing is a manufacturing contract where the seller sells a described item to the purchaser to be manufactured against a fixed total price and a determined term for future delivery.

Source: Federal Decree Law 50 of 2022, The UAE's Ministry of Economy

Establishment of Higher Shari'ah Authority: The HSA was established to harmonise and standardise the Shari'ah practices of Islamic financial institutions within the UAE. The Authority determines the rules and principles applicable to Islamic finance activities and supervises the internal Shari'ah supervisory committees (ISSCs) of Islamic financial institutions. It also approves monetary and financial tools to manage Shari'ah-compliant monetary policy operations.

Table 2.4 Shari'ah Governance Key Milestones

1985	2016	2017	2018	2022
HSA introduced under Federal Law No.6 of 1985	UAE Cabinet approves establishment of the HSA	Appointment of HSA members by Cabinet Resolution No. (31/6) of 2017	HSA commences work	Takaful included as part of HSA's Charter

Source: CBUAE

Table 2.5 UAE's Shari'ah Governance Landscape in 2022

51	41	6
Number of Members in Shari'ah Committees of Islamic Financial Institutions	Number of Islamic Financial Institutions with Shari'ah Committees	Number of Higher Shari'ah Authority Members

Source: CBUAE

Table 2.6 Comprehensive Shari'ah Governance Standards and Resolutions by HSA

Overarching Standard	Example Regarding Type of Institutions	Example Regarding Disclosure
Standard Re Shari'ah Governance for Islamic Financial Institutions	**Standard on Regulatory Requirements for Financial Institutions Housing an Islamic Window**	**Guidance Note on Annual Shari'ah Report of Internal Shari'ah Supervision Committee**
This standard requires Islamic financial institutions to have Shari'ah governance policies covering all their operations and objectives. It should incorporate three lines of defence comprising the business line, support and control functions, and internal Shari'ah audit function.	This standard articulates the minimum requirements for financial institutions with Islamic windows to ensure strong governance for Islamic activities and to contribute to financial stability and consumer protection.	This guidance outlines the general requirements for issuing an annual Shari'ah report, including its submission to the HSA for approval. The guidance also provides a template for the report.

Source: CBUAE

Governance and Shari'ah-compliance: The CBUAE has introduced initiatives and regulations to promote harmonisation and standardisation of Shari'ah-compliant practices within the Islamic finance industry. The CBUAE and HSA align the UAE's regulatory and Shari'ah requirements with internationally recognised standards such as IFSB prudential standards and AAOIFI Shari'ah standards, which serve as a minimum requirement for Shari'ah compliance among Islamic financial institutions. The HSA has also addressed several issues impacting Islamic financial institutions through its guidance regarding the Shari'ah aspects of sukuk, syndicated financing, and repo transactions. It has also provided guidance on innovative products and services offered by Islamic financial institutions and targeted guidance on the transition from Libor to risk-free rates.

One standard issued by the CBUAE to strengthen the prudential aspects of Islamic finance is the risk management standard for Islamic banks, which elaborates on aspects that were not already covered in other regulations issued by the CBUAE. Specifically, the risk management standard for Islamic banks lists the types of risk that are associated with the operations of Islamic banks, such as displaced commercial risk*, rate of return risk, and Shari'ah non-compliance risk.

The CBUAE also issued its Profit Equalisation for Islamic Banks regulation in 2022 in order to set appropriate risk management and governance requirements and safeguard the interests of investment account holders.

Table 2.7 Number of CBUAE Regulations**

	Banking	Insurance
Regulations and standards for Islamic financial institutions only	3	2
Shari'ah standards for Islamic financial institutions	7	1
Regulations and standards for both conventional and Islamic financial institutions	26	22

Table 2.8 Number of Regulations Issued by Other Regulatory Authorities***

Regulations for Islamic financial institutions	5
Regulations for both conventional and Islamic banks	24

Source: CBUAE

* Displaced commercial risk is a risk where an Islamic bank may be under pressure to voluntarily pay a market return on funding that is higher than the rate earned on assets financed by Investment Account Holder when the return on assets is under-performing compared to competitors' rates.
**This does not cover guidance, notices issued by the CBUAE and resolutions issued by the HSA and other regulations and standards issued for other LFIs (e.g. Finance Companies, Exchange Houses etc.).
*** SCA, DFSA, and ADGM's FSRA

Collaboration with standard-setting bodies: The UAE adopted AAOIFI Shari'ah standards in September 2018 following an HSA resolution. AAOIFI Shari'ah standards are considered the reference point for the Islamic finance industry worldwide. They can be adopted voluntarily by Islamic financial institutions and jurisdictions or be enforced by a regulator. There are currently 17 jurisdictions which have adopted AAOIFI standards whether fully, partially, or as guidance, along with three financial centres (including Dubai International Financial Centre) and Islamic Development Bank Group (IsDB). With the adoption of AAOIFI Shari'ah standards, all Islamic financial institutions in the UAE are required to review their products and services to ensure that they are in compliance. In addition, the HSA builds on these standards and modifies them based on the needs and practices of the UAE market.

Given the UAE's substantial share of the world's Islamic finance assets—the country is ranked fourth globally in this respect, according to the Islamic Finance Development Indicator 2023—CBUAE's efforts towards standardisation will help reduce fragmentation within Islamic finance markets.

The CBUAE is also a full member of the Islamic Financial Services Board (IFSB), which promotes the soundness of the Islamic financial services industry through its role as an international standard-setting body for regulatory and supervisory authorities. The CBUAE has voting rights as a member of the IFSB Council. The Dubai Financial Services Authority (DFSA) is also a full member, while ADGM is an associate member. As of December 2022, 11 UAE-based financial institutions were observer members.

Both AAOIFI and IFSB are working on standards covering Islamic sustainable finance as outlined in the table below.

Table 2.9 AAOIFI and IFSB's Contribution to Islamic Sustainable Finance

Issuing Body	Standard
AAOIFI	Governance Standard 7: Corporate Social Responsibility, Conduct and Disclosure for Islamic Financial Institutions
	Governance Standard: Responsible Financing
IFSB	IFSB-25: Disclosures to Promote Transparency and Market Discipline for Takaful/Retakaful Undertakings
	IFSB-22: Revised Standard on Disclosures to Promote Transparency and Market Discipline for Institutions Offering Islamic Financial Services
	TN-3: Technical Note on Financial Inclusion and Islamic Finance
	GN-4.12 :8 Integrating Sustainability into Legal and Regulatory Frameworks for ICM Considering the Associated Risks and Opportunities

Source: AAOIFI and IFSB

Collaboration with other Islamic finance organisations: Apart from adopting AAOIFI and IFSB standards, the HSA continues to work with other Islamic finance standard-setters and organisations such as the General Council for Islamic Banks and Financial Institutions (CIBAFI) to advance Islamic sustainable finance. The role of sustainability and collaboration in achieving sustainability goals was among the key themes addressed during the meeting of Centralised Shari'ah Authorities in October 2022. This was hosted by the CBUAE and the HSA, with the participation of AAOIFI, IFSB, CIBAFI and the IsDB, as well as the International Fiqh Academy. The meeting also discussed strategies to adopt green and sustainable finance standards for Islamic financial institutions, with a specific focus on social aspects.

Supporting the Islamic Finance Environment **in the UAE to Enable Sustainability**

Sustainable development of Islamic finance human capital in the UAE: An important consideration for sustainability development in the UAE Islamic finance industry is human capital. For example, there is often a gap between what graduates have studied and the skills they will need once they enter the industry. This issue is being actively addressed by Islamic financial institutions in the UAE.

Table 2.10 Training and Development by Islamic Financial Institutions in the UAE in 2022

33	20,156	82,877	66	235	1,847
Number of workshops for senior management and boards of directors	Number of training courses for employees	Total number of hours spent on training courses & workshops	Number of training courses delivered to students and academics	Number of training courses or workshops for other participants (technical assistance)	Number of e-learning courses

Source: CBUAE

Apart from professional training and development, the UAE provides a comprehensive education landscape for preparing upcoming and existing human capital for the Islamic finance industry. The country has 56 Islamic finance education providers, the third highest number in the world, according to the ICD – LSEG Islamic Finance Development Indicator 2023.

Other aspects considered by Islamic financial institutions with regard to the development of human capital include:

Figure 2.2 Human Capital Considerations by Islamic Financial Institutions

Diversity & Inclusion

- Emiratisation
- Disability Inclusion
- Gender Diversity
- Grievance Procedures

Talent Management

- Training and Development
- Performance Management System
- Structured Development Programmes

Health & Wellbeing

- Work / Life Balance Support including Hajj Leave
- Takaful and Parental Leave Policies
- Staff Finance Policies
- Health & Safety

Source: Annual and Sustainability Reports of the Largest Fully Fledged Islamic Banks in the UAE, 2022

Talent development through Emiratisation initiatives: One way in which the Islamic banking industry is investing in local talent is through compliance with the CBUAE's Emiratisation requirements. Aligning with the UAE's 'Projects of the 50' economic development initiatives, the requirements are aimed at boosting Emiratisation within the private sector. Accordingly, UAE-based institutions have developed internal Emiratisation plans and initiatives to not just retain talent but provide meaningful job opportunities that can serve the Islamic finance industry.

Figure 2.3 Initiatives by Islamic Financial Institutions to Support Emiratisation

Emirati graduate programmes to develop needed skills	Specialised development journeys for UAE nationals for future critical roles	Targeted recruitment programmes and participation in career fairs	Partnerships with the Ministry of Human Resources and Emiratisation and the Emirates Institute of Finance (EIF)

Source: Annual and Sustainability Reports of the Largest Fully Fledged Islamic Banks in the UAE, 2022

In addition, the HSA has issued a resolution to support Emiratisation within Islamic finance, especially in relation to Shari'ah governance at financial institutions. The resolution requires one third of Shari'ah board members to be Emirati. The HSA has also issued a resolution to appoint Emirati trainee members to the ISSCs of Islamic financial institutions. The results of these initiatives are reflected in the growing proportion of Emiratis working in internal Shari'ah control and internal Shari'ah audit departments and similar functions.

Table 2.11 Employment in Islamic Financial Institutions

	Islamic Banks	**Takaful***
Number of Employees	**7,802**	**1,410**
Emiratisation	**40%**	**9%**

* June 2022
Source: CBUAE

Table 2.12 Employment in Shari'ah Control and Shari'ah Audit Departments in UAE-Based Islamic Banks

Number of Employees	**175**
Emiratisation	**29%**

Source: CBUAE

Islamic banks embracing digital innovation: Innovation and digitalisation are having a major impact on economies and are an essential tool for achieving the transformations needed to reach sustainability goals. Following the global lockdown caused by the Covid-19 pandemic, the financial industry looked much more urgently to digital innovation to find ways to better serve its customers. Islamic banks in the UAE have similarly looked to digitally transform their services.

Figure 2.4 Customer Service-Related Digital Initiatives Reported by Islamic Banks in the UAE in 2022

Online Finance and Contactless Payments	Online Chat	Dedicated Application	Upgrading Automatic Teller Machines (ATMs) and Cash Deposit Machines (CDMs)	Digital Umbrella Brand	Social Media
Customers can easily approve and sign financing contracts without the need to visit branches. Contactless technology allows payments to be made through devices such as smart watches.	Consumers can chat with agents on a bank's website or use other digital channels such as WhatsApp.	Customers can bank in a simple manner using apps and other digital channels.	Upgrading existing ATMs and CDMs allows customers to update their information without visiting physical branches.	A digital umbrella brand allows a bank to offer all its digital offerings under one roof, such as opening an account, applying for cards, or sending remittances.	Social media channels allow banks to engage better with clients, create awareness, and acquire new customers.

REPORTED OBSERVED IMPACT BY ISLAMIC BANKS

- Increase in the Number of Online and Mobile Transactions
- Increase in Share of Digitally-Active Customers
- Increase in Number of Customers Overall
- Increase Uptake of Mobile Wallets

OTHER MECHANISMS USED IN DIGITAL TRANSFORMATION

Artificial Intelligence (AI) and Robotics	E-Learning	Blockchain
AI can be used for facial recognition in account openings and used in Know Your Customer (KYC) identity verification, while robotics allow all kinds of processes to be automated.	Employees can have access to custom-curated content with a library of thousands of courses on topics spanning business and technology, as well as certifications.	Use of blockchain is being seen in trade finance, where it can allow transparency, privacy and trust between organisations.

Source: Annual and Sustainability Reports of the Largest Fully Fledged Islamic Banks in the UAE, 2022

CHAPTER TWO: **ISLAMIC FINANCE LANDSCAPE AND FINANCIAL PERFORMANCE**

Islamic Banking

Islamic banking sector in the UAE: The UAE is the world's fourth largest Islamic banking market, according to the Islamic Finance Development Report 2023 (IFDI 2023). The country has a dual banking sector in which Islamic banks—comprising standalone Shari'ah-compliant banks and Islamic banking windows of conventional banks—operate alongside conventional banks.

In 2022, there were a total 24 Islamic banking institutions in the UAE, eight of which were standalone and 16 were Islamic windows of conventional banks. Breaking these numbers down, there were six locally incorporated standalone Islamic banks and two branches of foreign Islamic banks, and 11 local and five foreign banks with Islamic windows. These numbers were down from nine standalone Islamic banks and 18 Islamic windows in 2018 due to the acquisition of Noor Bank by Dubai Islamic Bank in 2020 and other mergers.

Asset growth driven by investments and financing: Assets held by the UAE's Islamic banking sector totalled AED 845 billion in 2022, having grown a compound annual growth rate (GAGR) of 3% over the previous five years. Assets held by Islamic banks totalled AED 631 billion while Islamic windows held AED 214 billion, showing respective growth of 8% and 49% from 2018. Islamic windows now account for 25% of total Islamic banking assets in the UAE. Islamic banking assets accounted for 23% of total banking assets in the UAE in 2022.

Figure 3.1 Islamic Banking Assets **(AED BILLION)**

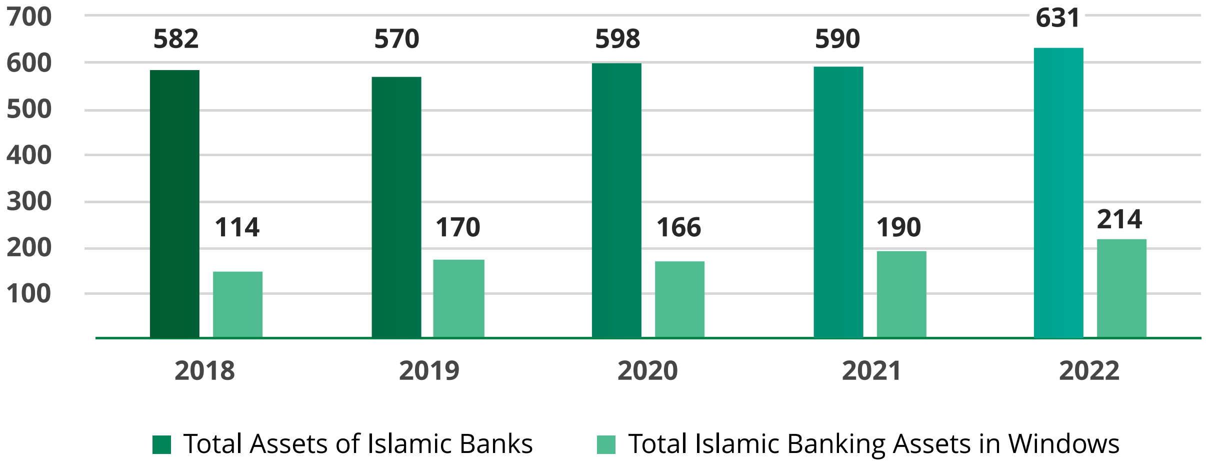
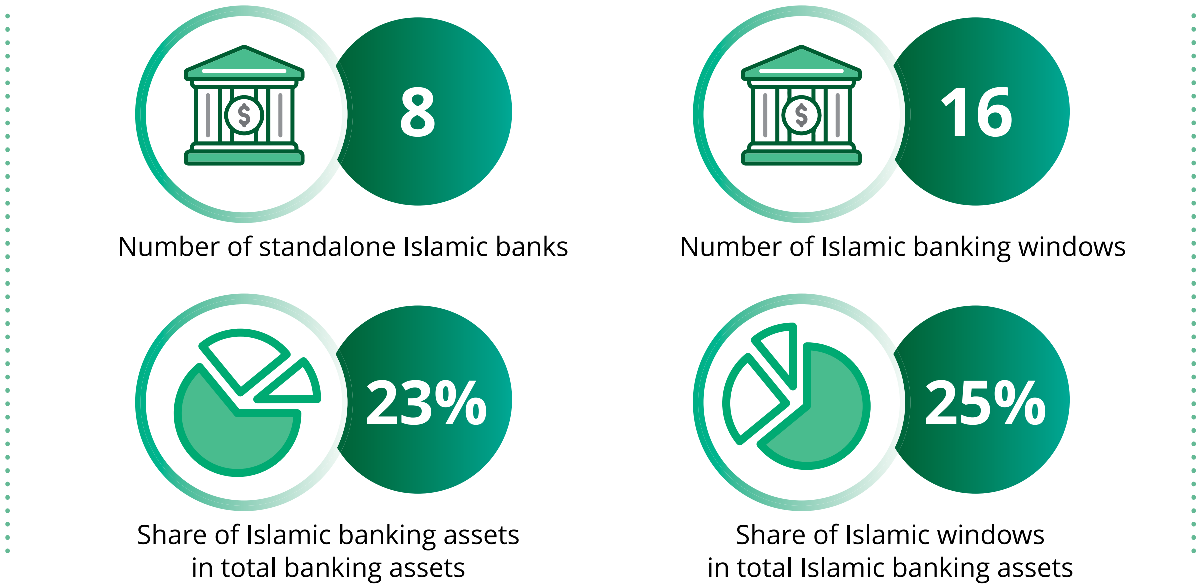


Figure 3.2 Islamic Banking in the UAE Snapshot (2022)



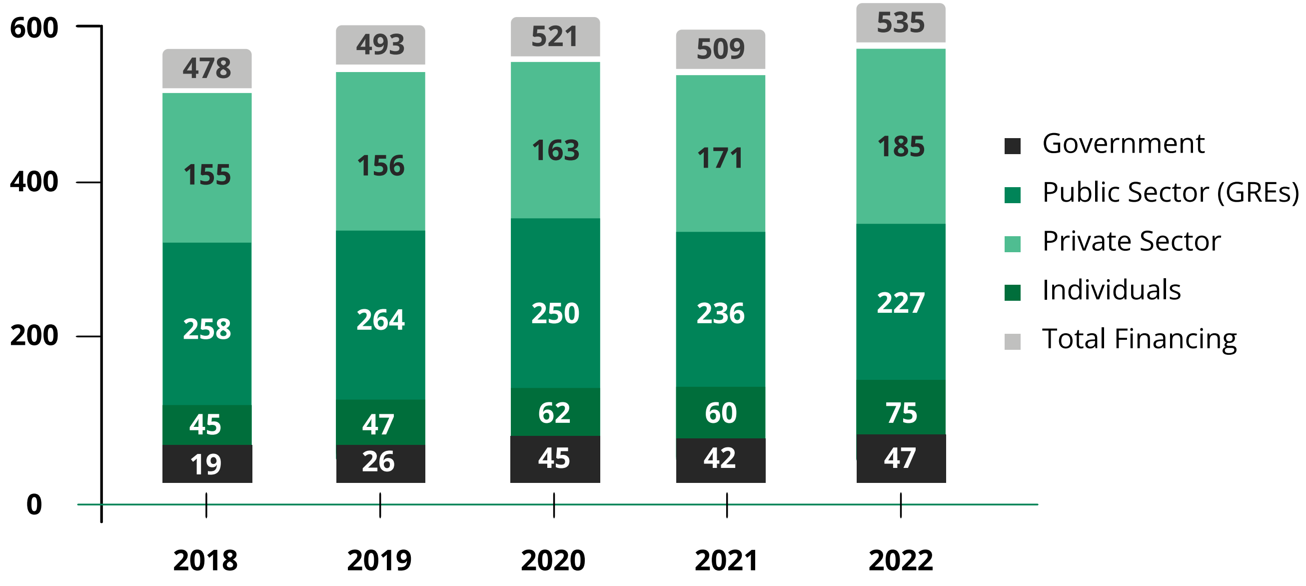
Source: CBUAE

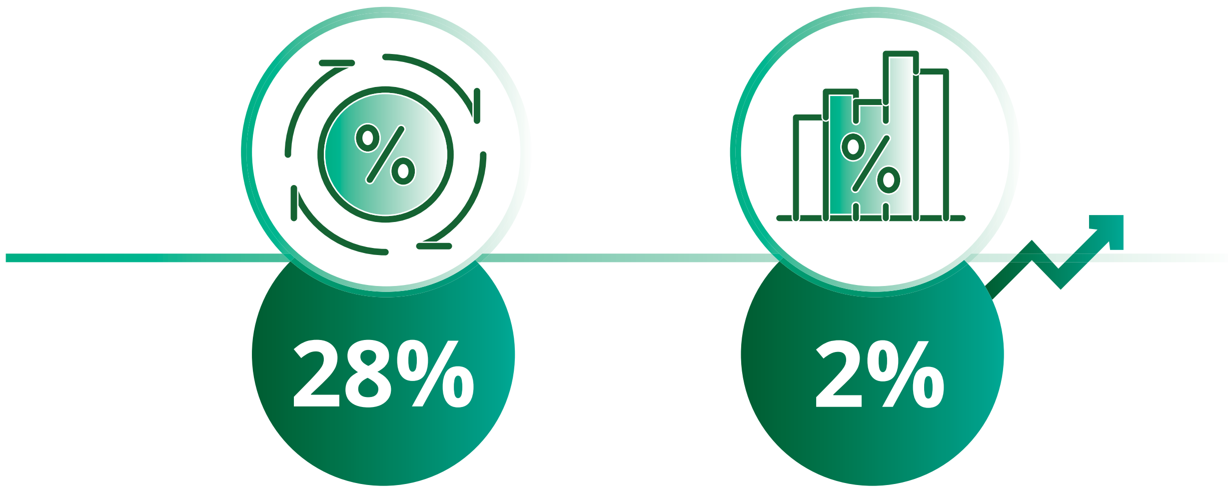
Continued growth in financing consistent with post-pandemic economic: Financing to the corporate sector and individuals makes up a large part of Islamic banks' portfolios, at 43% and 35%, respectively. Financing extended to the corporate sector has decreased since 2020 while financing to government and individuals has edged up from the onset of the Covid pandemic in 2020. The personal consumer segment was the main growth driver of retail financing, followed by mortgage and vehicle financing.

Overall growth in financing extended by the Islamic banking sector points to a continued rise in economic activities for both retail and corporate consumers post-pandemic, despite increases in benchmark rates. According to the CBUAE's quarterly Credit Sentiment Survey Q2 2023, strong economic conditions are offsetting the impact of higher rates on financing demand. Growth in financing was also supported by strong funding capacities at Islamic banks.

Ijara and murabaha were the most employed financing asset structures by Islamic banks in the UAE. Ijara is a lease contract used for fixed assets such as homes, other real estate, and equipment and machinery financing. Murabaha financing is a structure that works as a sales contract used to purchase goods such as vehicles at a pre-agreed profit margin. The profit and loss-sharing mechanisms that were most used for financing asset structures were wakala, mudharaba and musharaka.

Figure 3.3: Financing Extended by the Islamic Banking **(AED BILLION)**





Share of Islamic banking financing in total banking loans and financing

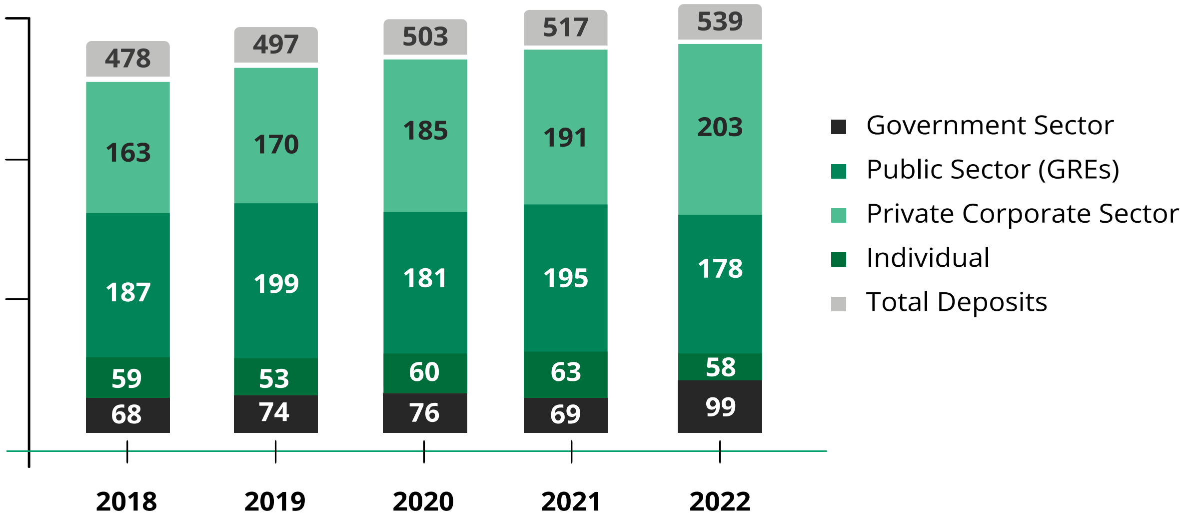
CAGR in financing extended by the Islamic banking sector since 2018

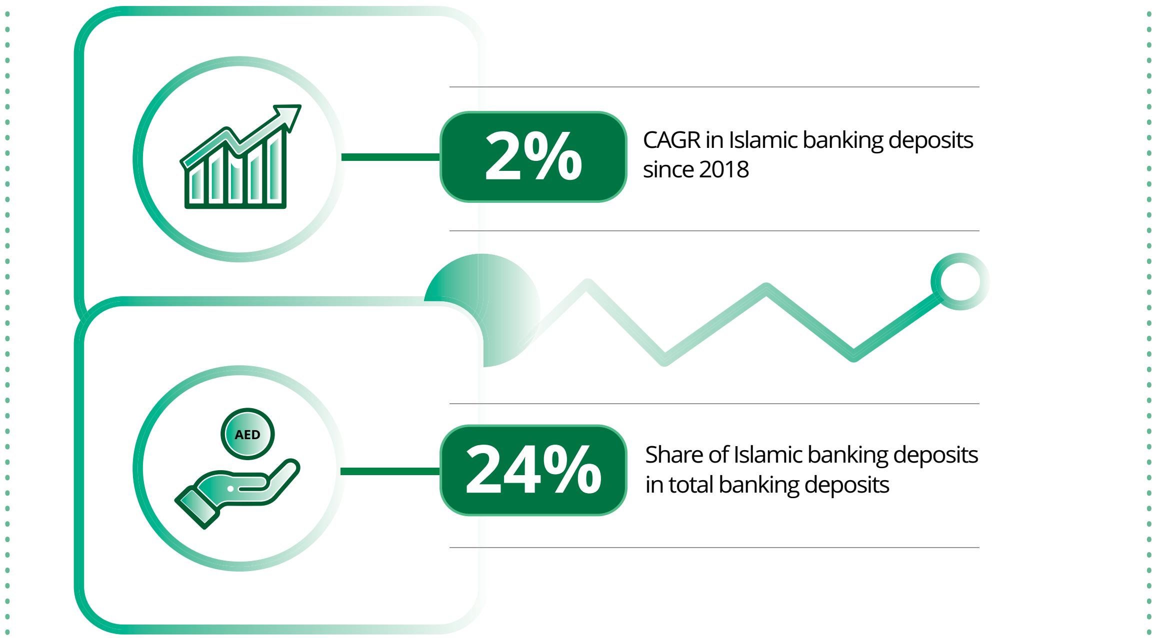
Source: CBUAE

Growth of Islamic banks' funding base: In 2022, the UAE's Islamic banking industry posted its highest growth in deposits since 2019. This was in line with the macroeconomic recovery in the UAE two years after the onset of the pandemic. Deposits increased in parallel with financing, by 4% in 2022, and this continued to improve Islamic banks' credit capacity while supporting liquidity. On the liabilities side, deposits account for 66% of total liabilities for Islamic banks, followed by Islamic capital market funding at 5%.

Individuals and the corporate sector contributed the largest shares of deposits, at 38% and 33%, respectively. While making up a large proportion of total deposits, the private corporate sector contribution was 9 percentage points lower than in 2021. At the same time, Islamic banks saw growth in government sector deposits. As reported by Islamic banks in the UAE, profit-sharing investment accounts such as mudharaba and wakala deposits accounted for most of the deposits. Mudharaba is a profit partnership between a bank and client for an agreed period, while wakala is an agency contract under which the account holder appoints the bank to carry out investment activities on the client's behalf.

Figure 3.4: Deposits in Islamic Banking **(AED BILLION)**





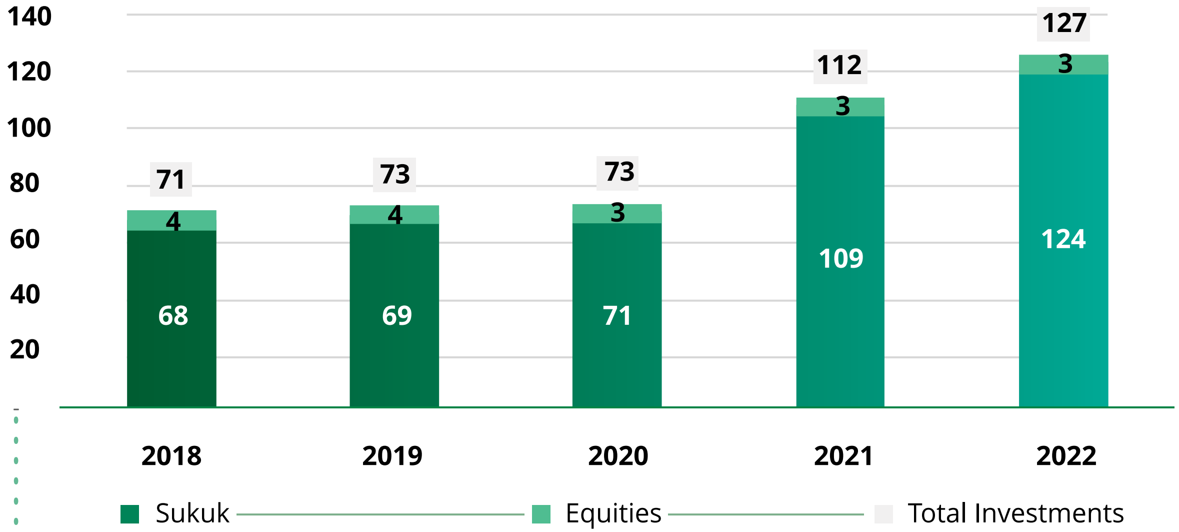
Source: CBUAE

Sukuk dominate investments for Islamic Banks: Following growth of 52% in investments by banks in the Islamic banking sector in 2021, when there was a particularly sharp rise in investment in sukuk, growth moderated to 14% in 2022, to AED 127 billion. The rise in rates of return from the middle of 2022 boosted investment in sukuk during the second half.

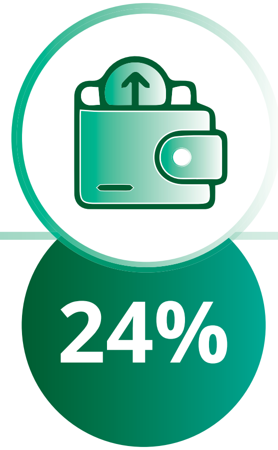
While sukuk dominate investments, Islamic banks have sought to ensure there is sufficient risk management for these exposures as they watch for signs of global financial market volatility following a rapid series of increases in global benchmark rates. A large proportion of sukuk are held to maturity. Equity holdings accounted for just a 2% share of investments by the Islamic banking sector.

There has been strong growth in sukuk supply, whether locally or from international issuers outside of the UAE. The introduction of local-currency Treasury sukuk by the UAE Federal Government in 2023, which was reviewed and approved by the HSA prior to its issuance, can support the mid-term yield curve development. This will be a key enabler for further growth in sukuk issuance. Given their role as investors as part of their liquid assets portfolio, this has the potential to further increase the sukuk holdings of the UAE's Islamic banking sector.

Figure 3.5: Investments by Islamic Banking Sector **(AED BILLION)**



CAGR in investments in Islamic banking sector since 2018



Share of Islamic banking investment in total banking investment

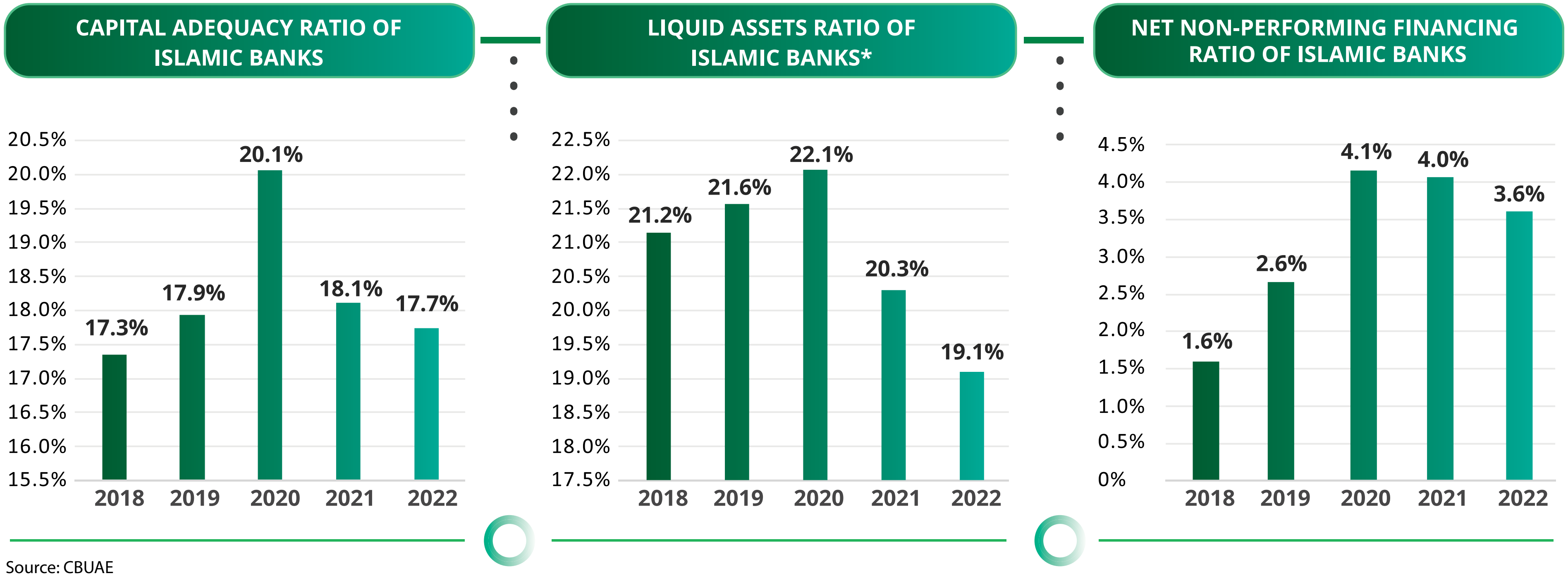
Source: CBUAE

UAE Islamic banking shows resilience across different metrics: The UAE Islamic banking sector performed relatively well across all key financial stability metrics in 2022. The capital adequacy ratios of Islamic banks averaged 17.7%. This was well above CBUAE requirements, which are based on the Basel III capital standards. The figure compares to 17.4% for the UAE banking sector as a whole. The slight decline in capital adequacy ratio (CAR) since 2020 is due to an increase in credit losses caused by higher defaults in the corporate and retail sectors following the Covid pandemic.

In terms of liquidity, Islamic banks held the same average eligible liquid asset ratio (ELAR)* of 19.1% as the overall UAE banking sector. This is markedly higher than the CBUAE's requirement of 10%. In terms of profitability, the average return on asset ratio (ROA) improved by 0.5 percentage point to 1.8%, largely due to an increase in net financing income, improved cost efficiency and lower impairment charges. This is slightly higher than the overall banking ROA of 1.4%.

The asset quality of the financing portfolio improved with a reduction in net non-performing financing to 3.6% in 2022 from 4.0% in 2021. This compares with 3.0% for the overall banking sector. The net non-performing financing ratio (NPF) continued to drop from 2020 as the overall economy recovered following the pandemic and despite the increase in benchmark rates.

Figure 3.6: Key Financial Stability Metrics for Islamic Banking in the UAE



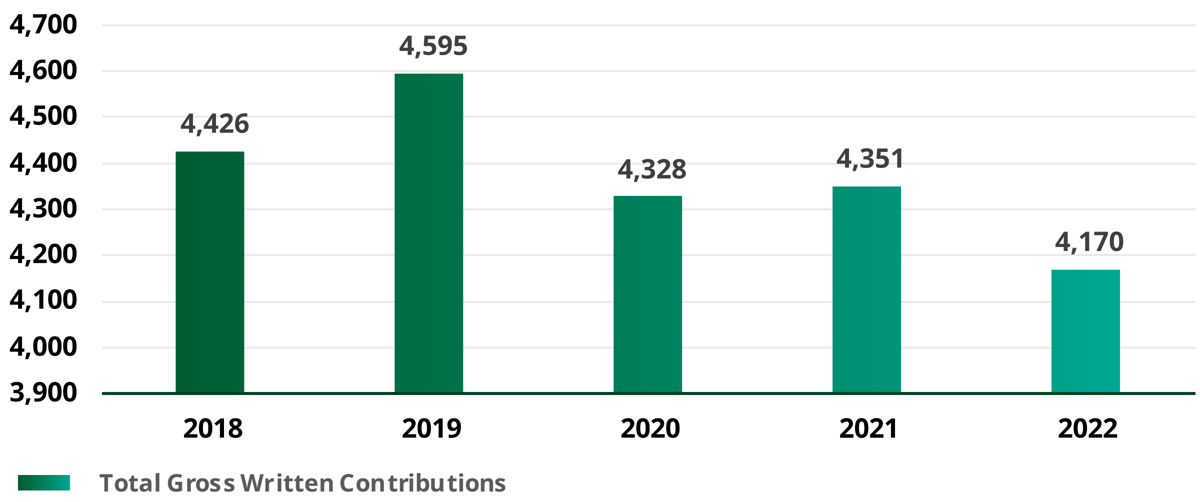
Source: CBUAE

* ELAR calculation excludes domestic systemically important banks.

Takaful Insurance

UAE takaful sector landscape is reshaping due to consolidation: Out of the 62 insurance companies in the UAE in 2022, 10 are takaful operators. Takaful insurance companies are fully Shari'ah-compliant. Unlike the equivalent in banking, conventional insurance operators are not permitted to operate Islamic windows in the UAE. In addition, there are two retakaful insurance companies in the UAE, both operating from the DIFC.

Figure 3.7: Takaful Growth in the UAE **(AED MILLION)**



9%

Share of takaful gross written contributions in total insurance gross written premiums in UAE

10

Number of takaful insurance companies in UAE

Source: CBUAE

Property and liability drive takaful gross written contributions in the UAE: The property and liability sector was the largest takaful business line in 2022, contributing 45% to gross written contributions (GWC), compared with 31% in 2021. Motor business line was the biggest contributor to the business, accounting for 47% of the total property and liability. Motor contributions have been increasing since 2020 due to heavy Covid discounts allowed on insurance operators since that year by the Insurance Authority. With regard to annual growth, marine and aviation lines saw the biggest increase, by 75%, on 2021, following the travel industry's return to pre-pandemic activity.

A potential contributor to the growth of the property and liability line is the Unemployment Insurance Law introduced in September 2022. The new law provides an insurance scheme under which private and federal government employees receive compensation payments in case of unemployment, in exchange for a contribution. This was signed with nine insurance companies, including two takaful insurance companies.

Health takaful was the second largest business line by GWC, holding a 38% share. Family takaful accounted for 16% in GWC, down from 32% in 2021. In terms of net written contributions (NWC), health takaful recorded 43% of such contributions. It is followed by property and liability which accounts for 41%. This is mainly driven by the motor business line, which makes up 76% of contributions to property and liability.

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Figure 3.8: Gross Written Contributions by Type of Business **(AED MILLION)**

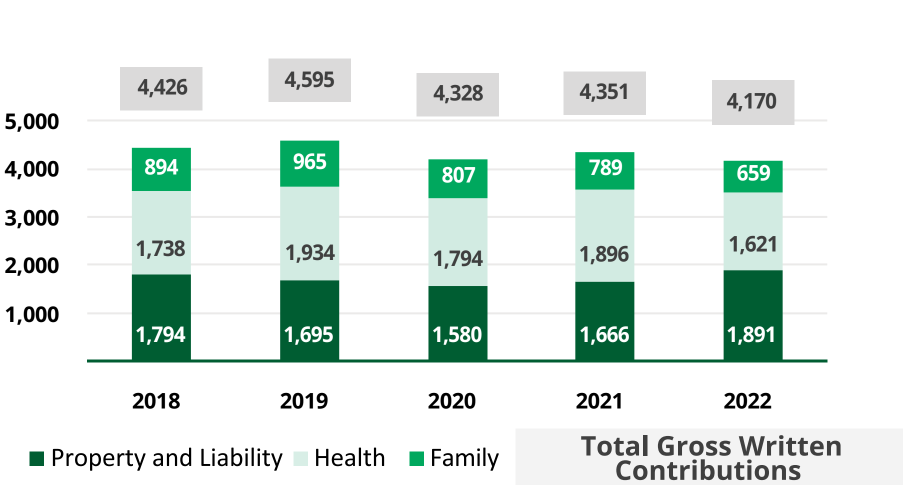
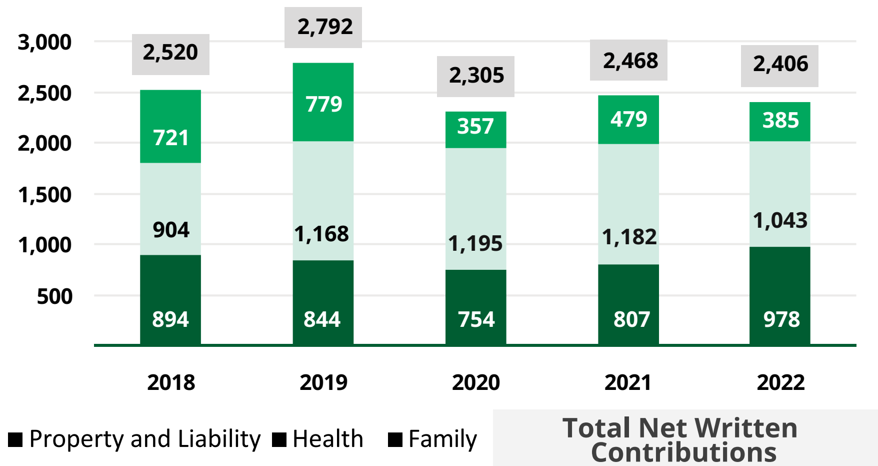


Figure 3.9: Net Written Contributions by Type of Business **(AED MILLION)**



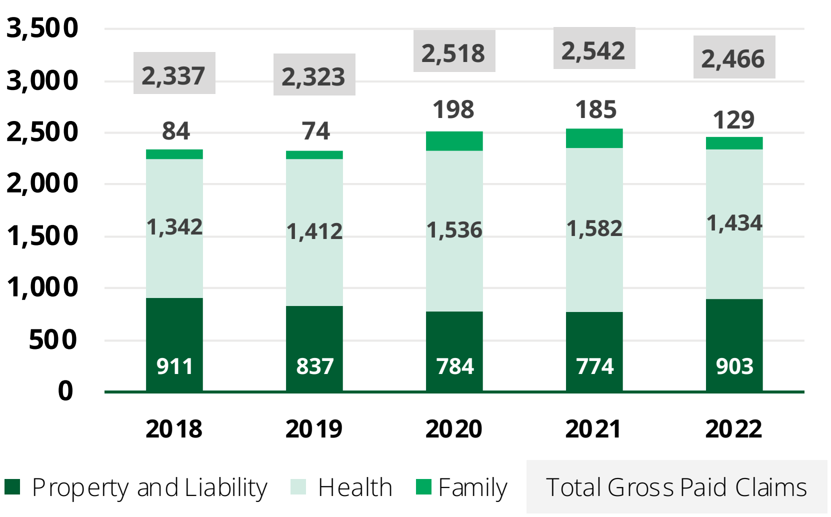
Source: CBUAE

Claims paid decline by takaful insurance companies in the UAE: For General Takaful, total gross claims paid (GCP) and net claims paid (NCP) each dropped 3% from 2021. The highest share of claims paid in 2022 was in the health takaful business line, at 58% for GCP and 64% for NCP. Health takaful has paid out the most in claims in the 2018 – 2022 period.

The second-highest contributor to claims is the motor and transportation business—part of the property and liability sector—which accounted for 27% of total overall takaful GCP and 33% of NCP. With vehicle activity on the roads returning to pre-pandemic levels, there has been an increase in both frequency and severity of claims on motor insurance. In addition, the high inflation environment has contributed to the increased costs, for example new vehicle parts, related to such claims.

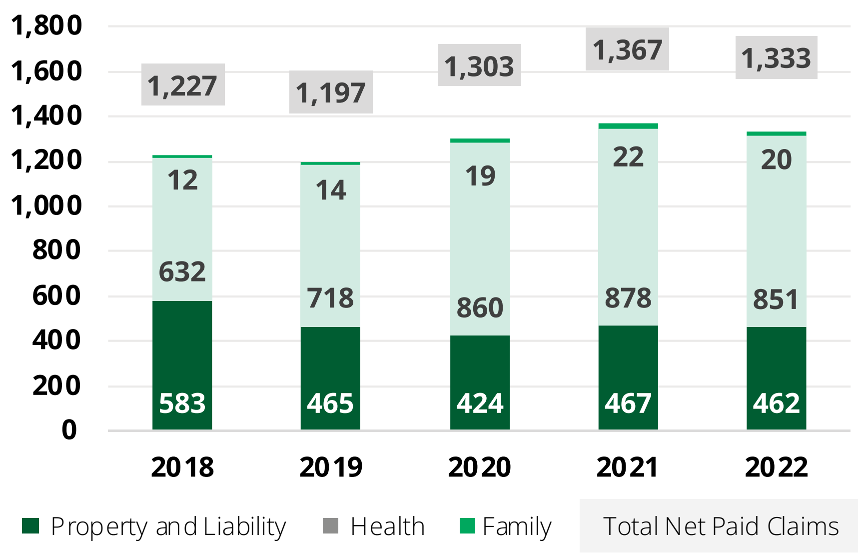
Family Takaful saw an annual decrease of 30% in GCP and 8% in NCP following a rise in family cover claims during the pandemic. The biggest segment driving such takaful claims in 2022 was group credit life takaful, which covers the outstanding principal amount to a lender in case of death or disability of the borrower.

Figure 3.10: Gross Written Paid Claims by Type of Business **(AED MILLION)**



Source: CBUAE

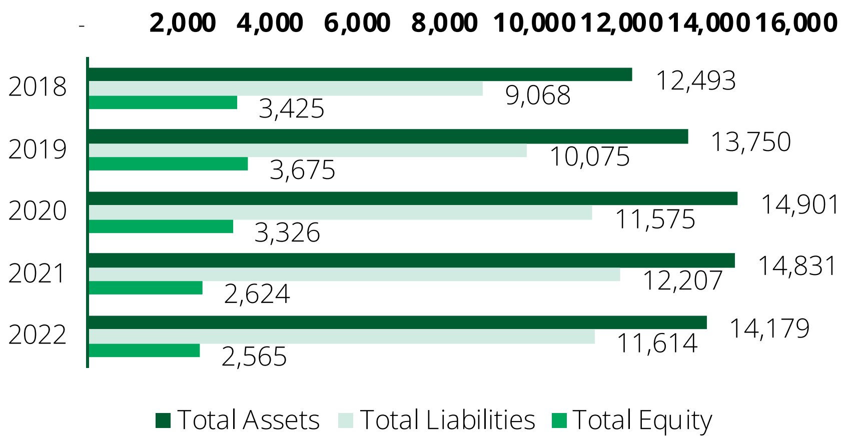
Figure 3.11: Net Paid Claims by Type of Business **(AED MILLION)**



Profits impacted by a drop in gross investment income: Takaful insurance companies posted an overall loss of AED 14 million in 2022, contrasting with a profit of AED 93 million in 2021. They reported an overall increase in net underwriting income to AED 205 million in 2022 from AED 3 million in 2021. However, gross investment income dropped 32% in 2022, due mainly to a decrease in net unrealised gains on investments and weaker stock market performance while investment expense rose 32% over the same period.

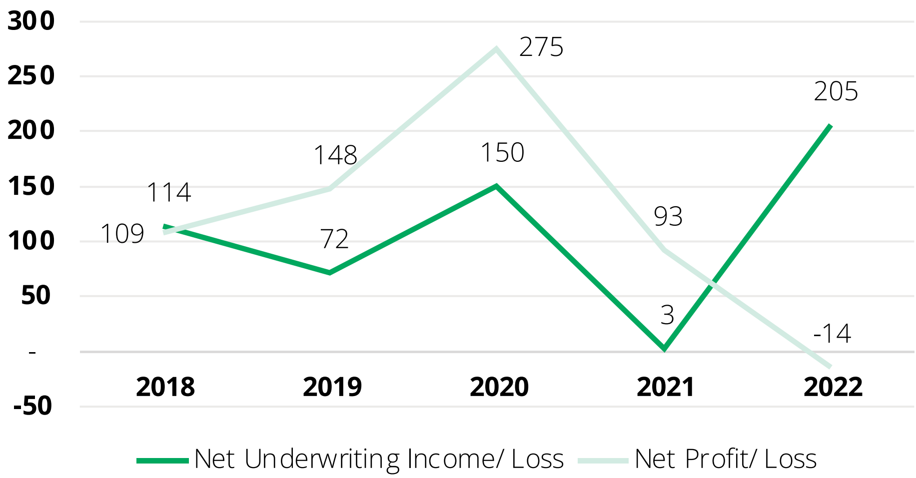
Total assets of takaful insurance companies have reduced by 4% since 2021 to AED 14.2 billion. Invested assets accounted for 53% of total assets in 2022, down 10 percentage points since 2021. Similarly, liabilities reduced by 4% since 2021 to AED 11.6 billion. Technical provisions accounted for 55% of total liabilities in 2022, down 9 percentage points since 2021.

Figure 3.12: Balance Sheet Structure of Takaful Insurance Companies **(AED MILLION)**



Source: CBUAE

Figure 3.13: Profitability by Takaful Insurance Companies **(AED MILLION)**



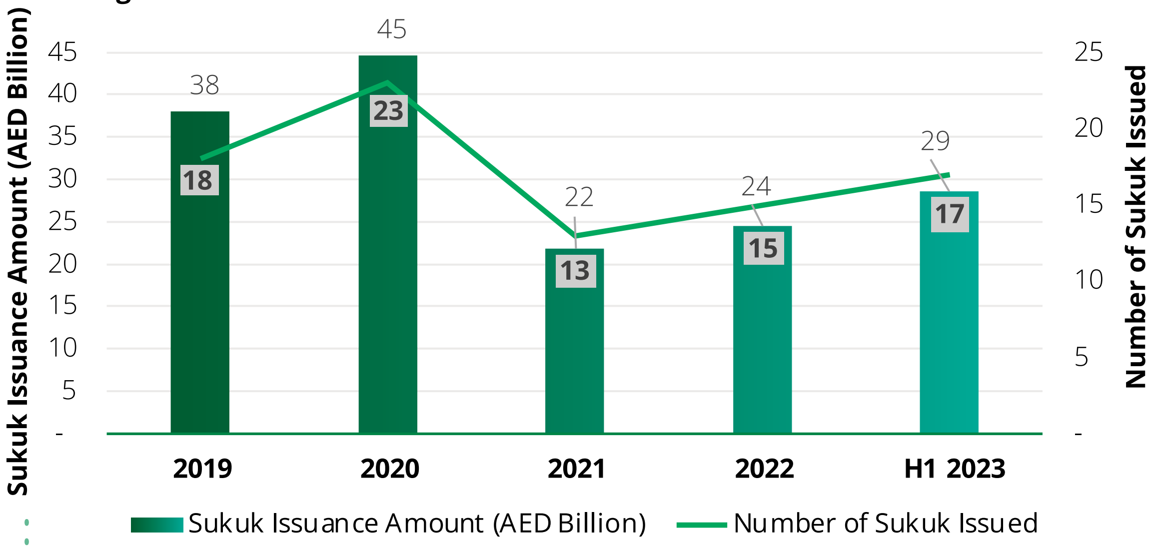
Sukuk

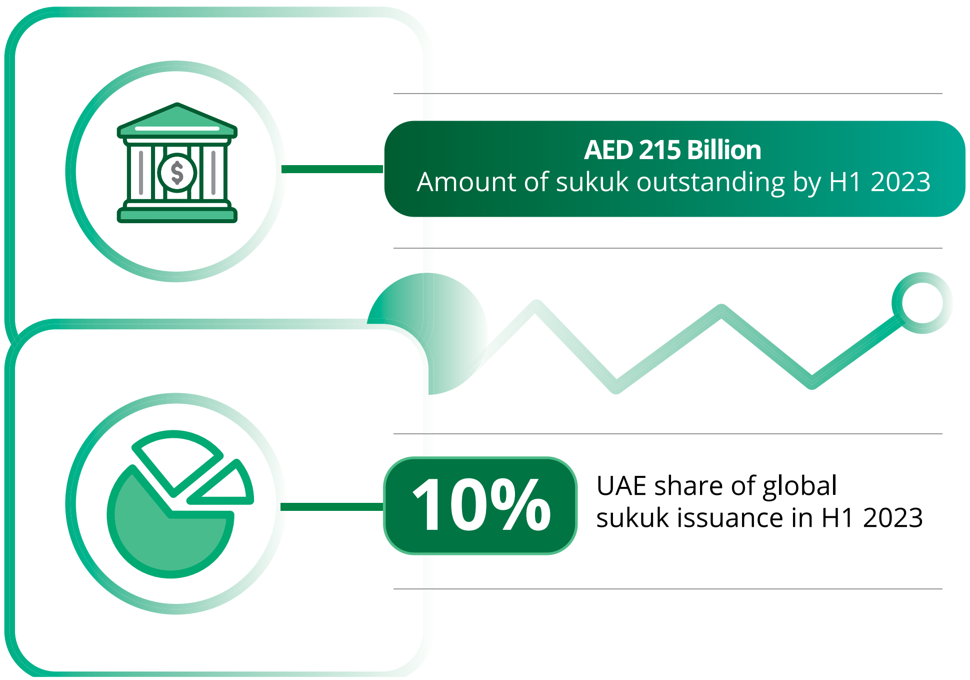
Sukuk issuance in the UAE sees strong growth in first half of 2023: The UAE is the world's fourth largest market in term of sukuk issuance and outstanding, according to LSEG data, supported by the presence of its Islamic financial institutions.

The UAE saw more active sukuk issuance in the first half of 2023 than in each of the full years 2021 and 2022. Issuance reached AED 28.7 billion in the first half of 2023, compared with AED 24.6 billion over the whole of 2022. Sukuk outstanding grew 15% from AED 187.0 billion in 2022 to AED 215.24 billion in the first half of 2023.

The Government of Sharjah issued the highest amount of sukuk over the past five years, followed by Dubai Islamic Bank and Abu Dhabi Islamic Bank. Collectively, these three entities accounted for 74% of total sukuk issuance in the UAE.

Figure 3.14: Sukuk Issuance in the UAE





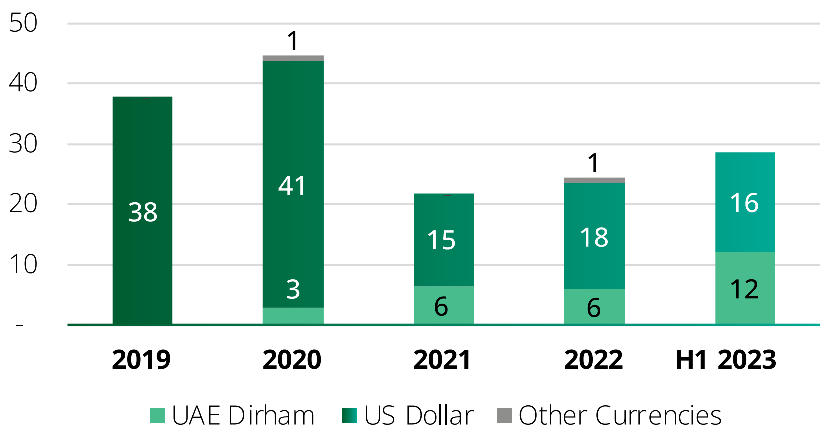
Source: LSEG Workspace Platform

Domestic sukuk issuance gaining traction with introduction of UAE Treasury sukuk: Most of the UAE's sukuk issuance over the past five years has been in US dollars. However, locally denominated issues are growing in popularity. One reason for this is the debut issuance of a local-currency Treasury sukuk, in the second quarter of 2023, by the Federal Government with approval from the HSA. The domestic dirham-denominated sukuk aimed to diversify funding structures while supporting growth of the local Islamic capital markets through the development of its mid-term yield curve. The issues were in 3, 5 and 10-year tranches.

Other issuers of AED sukuk during the first half of 2023 included Emirates Islamic Bank (EIB), which was the first bank in the UAE to issue a local-currency sukuk. Other currencies in which UAE-issued sukuk have been denominated over the past five years include the Malaysian ringgit, Kuwaiti dinar, and Saudi riyal.

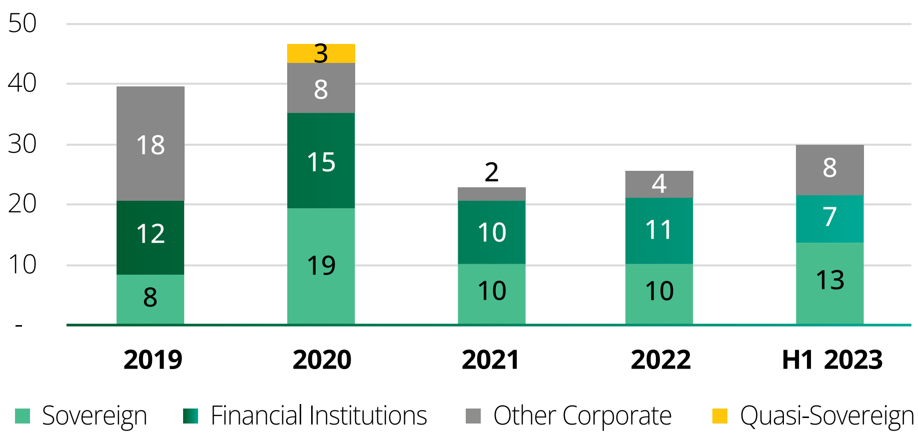
Corporate and sovereign issuers are both active in the UAE. Corporate issuers in the past five years have been mostly banks, both conventional and Islamic. Active corporates from other sectors include business conglomerate, logistics, airlines, and real estate development.

Figure 3.15: Sukuk Issuance in the UAE by Currency **(AED BILLION)**



Source: LSEG Workspace Platform

Figure 3.16: Sukuk Issuance in the UAE by Issuer Type **(AED BILLION)**



CHAPTER THREE: **SUSTAINABILITY DEVELOPMENTS AND INITIATIVES IN THE UAE**

Sustainability Agenda by **the Government of the UAE**

Sustainability is embedded within the UAE government agenda: The primary governmental framework for sustainable finance in the UAE is the Ministry of Climate Change and Environment's (MOCCAE) Sustainable Finance Framework 2021-2031. The Framework includes three pillars: mainstreaming sustainability in financial decision-making; enhancing the supply and demand of sustainable finance products; and strengthening the enabling environment for sustainable finance practices. This strategy interlinks with the UAE Green Agenda 2015-2030, the National Climate Change Plan of the UAE 2017-2050, and the UAE Net Zero by 2050 strategic initiative.

Figure 4.1 MOCCAE's UAE Sustainable Finance Framework

Pillar 1: Mainstream sustainability in financial decision-making and risk management

- Embed sustainability in policies, legislation and directives
- Supervisory oversight of climate-related risks by existing supervisory authorities
- Regulatory guidelines relating to ESG- and climate-related risk exposures
- Environmental stress-testing tools
- Standardised guidance on ESG- and climate-related disclosures in line with TCFD

Pillar 2: Enhance supply and demand for sustainable finance products and green investment projects

- Establish a nation-wide, common taxonomy for sustainable finance
- Incentives for green finance including tax, refinance schemes, guarantees ,and other risk-sharing instruments
- Incentivise financial institution by development of green finance products
- Assess readiness for sovereign green bonds
- Develop climate and green investment product pipeline and support implementation of pilot projects

Pillar 3: Strengthen enabling environment for promoting sustainable finance practices

- Forge partnerships for research and development of green finance, technology and innovation
- Skills development in sustainable finance for next generation of financial professionals
- Accreditation schemes for sustainable finance training programmes, with incentives for professionals and project developers
- Promote entrepreneurship and innovation through concessional funding, venture capital, grants, and technical assistance.

Source: UAE Sustainable Finance Framework 2021 - 2031

UAE declares 2023 Year of Sustainability: As host of the COP 28 climate conference, the UAE government has declared 2023 as the 'Year of Sustainability', with the country drawing on its heritage and the legacy of its Founding President, the late Sheikh Zayed bin Sultan Al Nahyan, to promote sustainability practices under the theme of 'Today for Tomorrow'.

The aim of the Year of Sustainability is to make a positive impact to ongoing work in this area through initiatives involving both the public and private sectors. It aims to build awareness across the three themes of sustainable consumption, conservation, and climate action. This will be promoted through media campaigns and the release of a 'Sustainability Guide' by the Sustainability Experts Network for individuals and businesses wishing to play their part in wider sustainability goals.

UAE Sustainable Finance Working Group advancing sustainability in capital markets: The Sustainable Finance Working Group (SFWG) was established in 2019 to bring together a core group of UAE authorities support the development of sustainable finance and facilitate regulatory cooperation on frameworks that can enable the financial institutions to deliver on identified needs in this area. Its work follows national policies relating to sustainability, the green agenda, action on climate change, and the Net Zero by 2050 strategic initiative. The SFWG now includes representatives of the CBUAE, SCA, ADGM, DIFC, the Ministries of Finance and Economy, and the UAE's Special Envoy for Climate Change. The working group also includes the Abu Dhabi Exchange, Dubai Financial Market and Nasdaq Dubai.

The SFWG's first deliverable was its Guiding Principles on Sustainable Finance. These were complemented by two public statements that covered three specific deliverables for the Working Group relating to the consistency of ESG disclosure; strengthening corporate governance to support the sustainability agenda, and the development of the UAE taxonomy of sustainable activities.

Figure 4.2 UAE Sustainable Finance Milestones

2020

- Guiding Principles on Sustainable Finance adopted as voluntary guidelines for the development of policies to encourage financial institutions to incorporate ESG in their business decision-making and risk frameworks, and to identify new opportunities.
- Recognition of the importance of sustainability taxonomies and referencing several international taxonomies and processes relevant to capital markets issuance.
- Explicit incorporation of considerations relating to Islamic finance for financial institutions, investors and issuers with specific reference to AAOIFI accounting and Shari'ah standards in the Guiding Principles on Sustainable Finance.

2021

- SFWG issues its first high-level statement on sustainable finance following national announcement of 2050 Net Zero ambition.
- The high-level statement outlines a roadmap to progress the Guiding Principles via the three key deliverables: examining sustainability disclosure standards in the UAE, with a view to promoting standards aligned with best practice, reviewing corporate governance practices and helping embed sustainability in them; and agreeing to develop a UAE taxonomy of sustainable activities.

2022

- Reiteration of the roadmap to implement the Guiding Principles on Sustainable Finance and progress update on the three workstreams relating to ESG disclosure, sustainability-focused corporate governance, and designing the UAE Sustainable Finance Taxonomy.
- Extensive benchmarking and fact-gathering exercises of best practice from regulators, international organisations, industry standards-setting bodies. This included developments at the Basel Committee on Banking Supervision, International Sustainability Standards Board, and IOSCO, as well as the G20 Sustainable Finance Roadmap.

2023

- The SFWG issues the "Principles for the Effective Management of Climate-related Financial Risks", which are designed to apply to all UAE-based financial services firms.
- HSA produces guiding principles regarding sustainable Islamic financial institutions.
- The UAE Banking Federation forms the Steering Committee on Islamic finance to define a unified vision on sustainability for Islamic financial institutions.

The SFWG launched the Principles for the Effective Management of Climate-related Financial Risks in November 2023. The Principles constitute a declaration of common understanding among the SFWG members, including the CBUAE's and the other financial sector regulatory bodies in the UAE, on the minimum expectations for the management of climate-related financial risks by financial sector institutions operating in the UAE.

The Principles set the expectations for governance and risk management of climate-related financial risks, and firms will be expected to establish and maintain appropriate oversight and allocation of responsibilities for these risks, and integrate them within the processes and systems for strategy-setting, risk management framework, capital and liquidity planning, and scenario analysis exercises. The Principles currently apply to all banks and insurance companies within the CBUAE's purview, including Islamic banks and takaful insurance companies.

Other parties have also been implementing steps to progress sustainability within the domains they oversee, such as SCA in capital markets. The SCA's sustainable capital markets initiative, which follows the Master Plan for Sustainable Capital Markets issued in 2019, seeks to enhance sustainability disclosures and the use of ESG considerations within risk management and decision-making processes in order to improve capital allocations.

The DFSA has also provided market guidance on ESG capital markets products and disclosures using a voluntary approach to drive adoption of best practice. The guidance is supported by DFSA's rules concerning deceptive marketing practices such as greenwashing.

The Financial Services Regulatory Authority at ADGM has issued regulations in 2023 which cover requirements for investment funds and capital markets issuance, including for green, social, sustainability, and sustainability-linked (GSSS) bonds and sukuk.

Table 4.1 Initiatives on Sustainability by Regulatory Authorities in the UAE*

Securities and Commodities Authority (SCA)	Dubai Financial Services Authority (DFSA)	ADGM's Financial Services Regulatory Authority (FSRA)
Sustainable Capital Markets Plan 2019 • Taxonomy • Legal framework • Market platform and investment instruments • Corporate governance • Disclosure	**DFSA Best Practice Guidelines on ESG Bonds** • ESG bond guidelines • Additional guidelines for sustainability-linked bonds	**Sustainable Finance Regulatory Framework** • 'Green' and 'Climate Transition' funds label • 'Green' and 'Climate Transition' portfolio • Requirements for green, social, sustainability and sustainability-linked debentures and sukuk

*The CBUAE's sustainability initiatives are covered on the following page

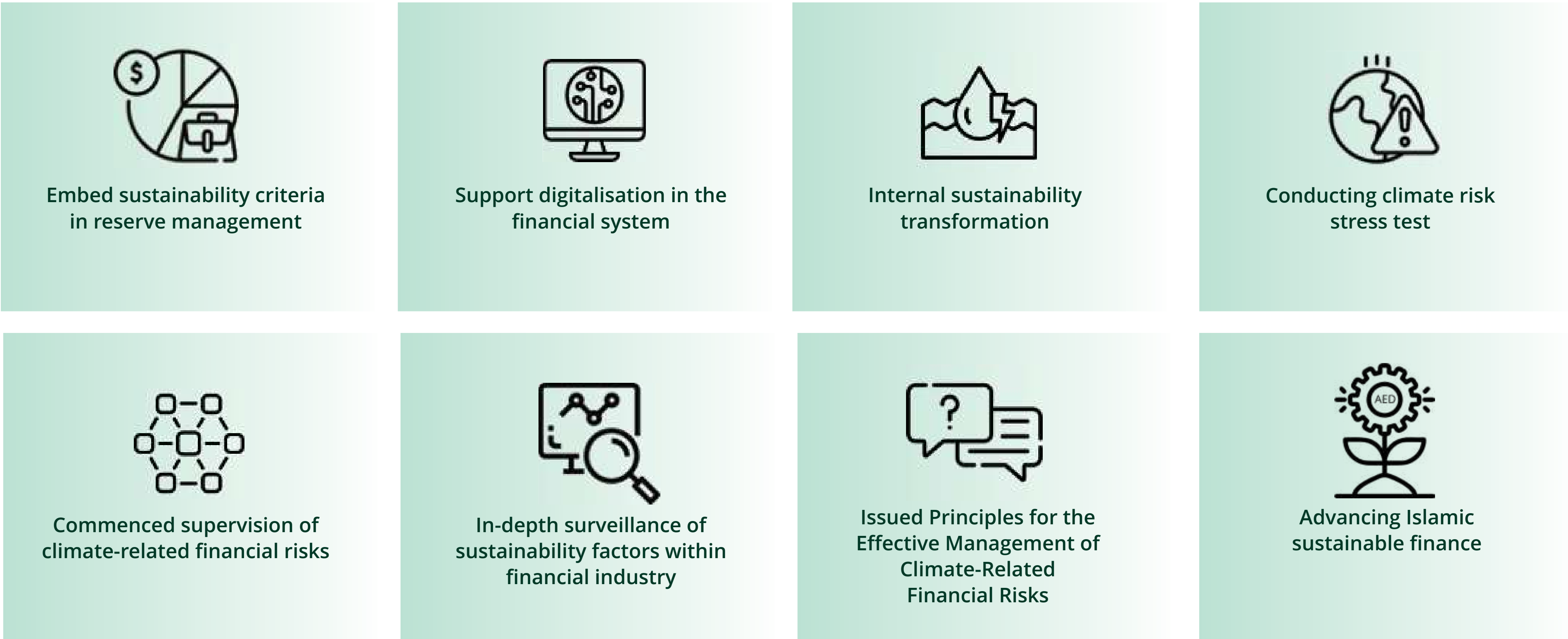
Central Bank of the UAE **Sustainability Agenda**

Sustainability and sustainable finance commitments implemented by the CBUAE: The CBUAE in 2021 produced a new strategic plan for the years 2023-2026 that incorporate sustainability as one of five strategic focus areas. The CBUAE also undertook a range of operational sustainability initiatives to reduce its own environmental footprint and to practise sustainability as an employer. It also took proactive steps during the 2023 HSA's annual meeting to highlight the importance of sustainable finance, which served as a prelude to the guidelines issued by the HSA to Islamic financial institutions.

The CBUAE added green and sustainable financial assets as eligible reserve assets in its own investment policy and holds ESG financial assets as part of the capital market tranche of its reserve portfolio. It began conducting climate risk-risk stress-testing and scenario analysis. The CBUAE also commenced with the supervision of climate-related financial risks in banks and insurance companies.

The CBUAE promotes green and sustainable finance in the UAE, advances Islamic sustainable finance, and conducts in-depth surveillance of sustainability factors in financial markets and institutions. The CBUAE is a member of the Network for Greening the Financial System (NGFS), a network of central banks and financial supervisory bodies that advocates a more sustainable financial system.

Figure 4.3 Selected CBUAE Initiatives on Sustainability and Sustainable Finance UAE



Source: CBUAE

HSA's Shari'ah-based approach to sustainable finance: The regulatory approach of Islamic financial institutions has been largely characterised by treating them on an equal footing with conventional financial institutions while increasing consistency within the Shari'ah governance process through the HSA. The HSA is the main body within the UAE tasked with providing a consistent Shari'ah governance framework and providing Shari'ah rules for Islamic financial institutions' operations that are supervised under the CBUAE. The HSA has also issued guidelines for decision-making processes that embody sustainability considerations.

The supervisory structure for Shari'ah governance in Islamic finance is extensive and well established. Islamic finance has had decades of development in relation to standardisation, regulation, and ecosystem development, starting with the formation of AAOIFI in 1990. Governance structures have been designed to ensure compliance of all of an institution's operations with Shari'ah. To the extent that this responsibility includes sustainability, ISSCs must include sustainability aspects in their decision making by applying Shari'ah legal maxims that weigh harm and benefits and by taking into consideration the consequences of financing projects. In addition, although it does not provide oversight for all financial institutions' activities, the HSA has required that sustainable financial activities should be segregated from other assets in order to provide greater transparency and lessen the possibilities of greenwashing.

Sustainable Finance and Sustainability at Islamic Financial Institutions in the UAE: Sustainable capital markets in the UAE have grown rapidly since the debut of the first green sukuk issuance in 2019. The market has expanded and diversified as businesses recognise the opportunities such instruments present, particularly within the Islamic capital markets. Along with a growing number of issuers, there has been an array of new types of issuance such as green sukuk, sustainability sukuk, sustainability-linked loans and Islamic financing, as well as transition sukuk. Much of the development in Islamic capital markets follows the introduction of international guidelines and principles covering green, social, sustainable and sustainability-linked (GSSS) issuance.

Added to this are localised guidelines such as the UAE taxonomy of sustainable activities to be delivered by the SFWG. Alignment with international guidance such as Green Bond Principles by the International Capital Market Association will result in greater mobilisation of financial resources for companies and projects that are not only Shari'ah-compliant but also have positive impact on the environment and society. The international guidance, principles and frameworks reduce market friction and increase the ability of issuers and their advisors to mobilise funding internationally, including from dedicated green or sustainable investors who do not typically invest in sukuk.

Figure 4.4 UAE ESG Sukuk (Issuance and Arrangement)

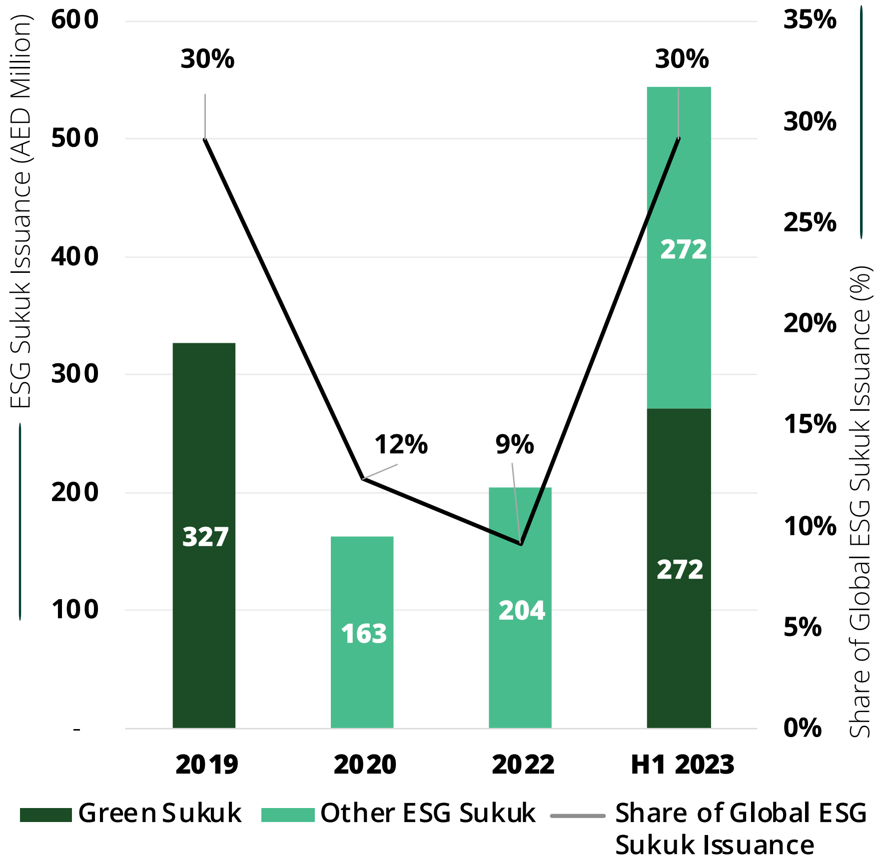
AED 1,239 Million
Amount of ESG Sukuk Outstanding by H1 2023

15%
UAE's Share of Global ESG Sukuk Outstanding in H1 2023

UAE-based Lead Arrangers for International ESG Sukuk*

	Proceeds Amount + Over-allotment Sold	Market Share of Total Proceeds (%)	Number of UAE-based Managing Underwriters
2022	AED 218 Million	12	4
H1 2023	AED 413 Million	28	7

*The table covers UAE-based banks arranging for ESG sukuk which include arrangements for sukuk issued by local and foreign issuers that are not based in the UAE.



Source: LSEG Workspace Platform

CHAPTER FOUR: OUTLOOK ON SUSTAINABILITY ADOPTION BY ISLAMIC FINANCIAL INSTITUTIONS IN THE UAE

Outlook on Sustainability Adoption **by Islamic Financial Institutions in the UAE**

This chapter covers the UAE Islamic Finance Sustainability Survey. It has been developed to assess the strategies, practices and outlook for sustainability within the Islamic financial system of the UAE. The responses were collected and aggregated to build a broad market perspective.

The survey covers responses by Islamic financial institutions consisting of both Islamic banks and Islamic banking windows, whether of domestic or foreign banks. The survey also sought input from Islamic finance companies on their ESG and sustainability strategies. Meanwhile, similar information from takaful insurance companies' was collected as part of the UAE Takaful Sustainability Survey presented in the **CBUAE Takaful Insurance Report 2022**

The survey was conducted in the third quarter of 2023 by the CBUAE. Responses were collected from 19 Islamic banking institutions, six Islamic banks, and 13 conventional banks with Islamic windows. Five Islamic finance companies also participated.

The survey covers a number of areas considered key for sustainability development by Islamic financial institutions in the UAE:

- Sustainability Strategy and Governance
- Sustainability / ESG Criteria
- Sustainability Roadmap
- Sustainability Financial Goals
- Sustainability in Product Offerings
- Opportunities and Challenges in Implementing Sustainability
- Sustainability Disclosures

The CBUAE requires Islamic financial institutions to adhere to the highest degree of disclosure and transparency regarding the sustainability and ESG standards they adopt. However, adopting a particular sustainability or ESG standard is the responsibility of Islamic financial institutions and the CBUAE does not interfere in their choices as long as they disclose them in a transparent manner to their clients.

Sustainability Strategy **and Governance**

All full-fledged Islamic banks in the UAE have sustainability strategies: A survey of the UAE Islamic banking sector, covering local and foreign full-fledged Islamic banks and Islamic banking windows of conventional banks, revealed that 79% have a sustainability strategy, while 74% reported that their strategy has been approved at the board level.

All of the Islamic banks said they have sustainability strategies in place, however this was not the case for conventional banks with Islamic windows, where some strategies were under development or waiting to be formalised for publication in the coming year.

In addition, more than half of respondents said they were conducting sustainability awareness campaigns or implementing an ESG risk-assessment framework. Also, 37% of respondents said they have a dedicated budget for sustainability, although this proportion drops to 17% when considering Islamic banks only.

Figure 5.1: Sustainability Strategy

79%
Share of Islamic banks and Islamic windows with a sustainability strategy or approach

74%
Share of Islamic banks and Islamic windows with board approval for their sustainability strategy

Figure 5.2: Directions to Strengthen Sustainability Strategy and Governance

68%
Conduct sustainability awareness capacity-building sessions

68%
Implement an ESG impact-based risk assessment framework for financing and investment decision-making

37%
Make a clear priority for sustainability in bank budgets

The role of governance bodies in overseeing and enabling sustainability: Although ultimate responsibility and oversight for sustainability lies with boards of directors, 79% of the Islamic banking entities in the survey indicated that executive committees and senior management are a vital part of ensuring implementation of banks' sustainability strategies while 74% have indicated that the board of directors is part of the main parties responsible for this. Driving sustainability can take the form of building awareness or of improving the integration of sustainability within business functions.

One mechanism used by boards is to devise a multi-year ESG plan with their strategy committees, under which objectives are set out and updates on material developments are provided on a quarterly basis. The survey showed that 63% of Islamic banks and Islamic windows look to their risk management committees to incorporate ESG within their enterprise risk management frameworks. Some Islamic banks also reported having both a sustainability committee and a sustainability officer.

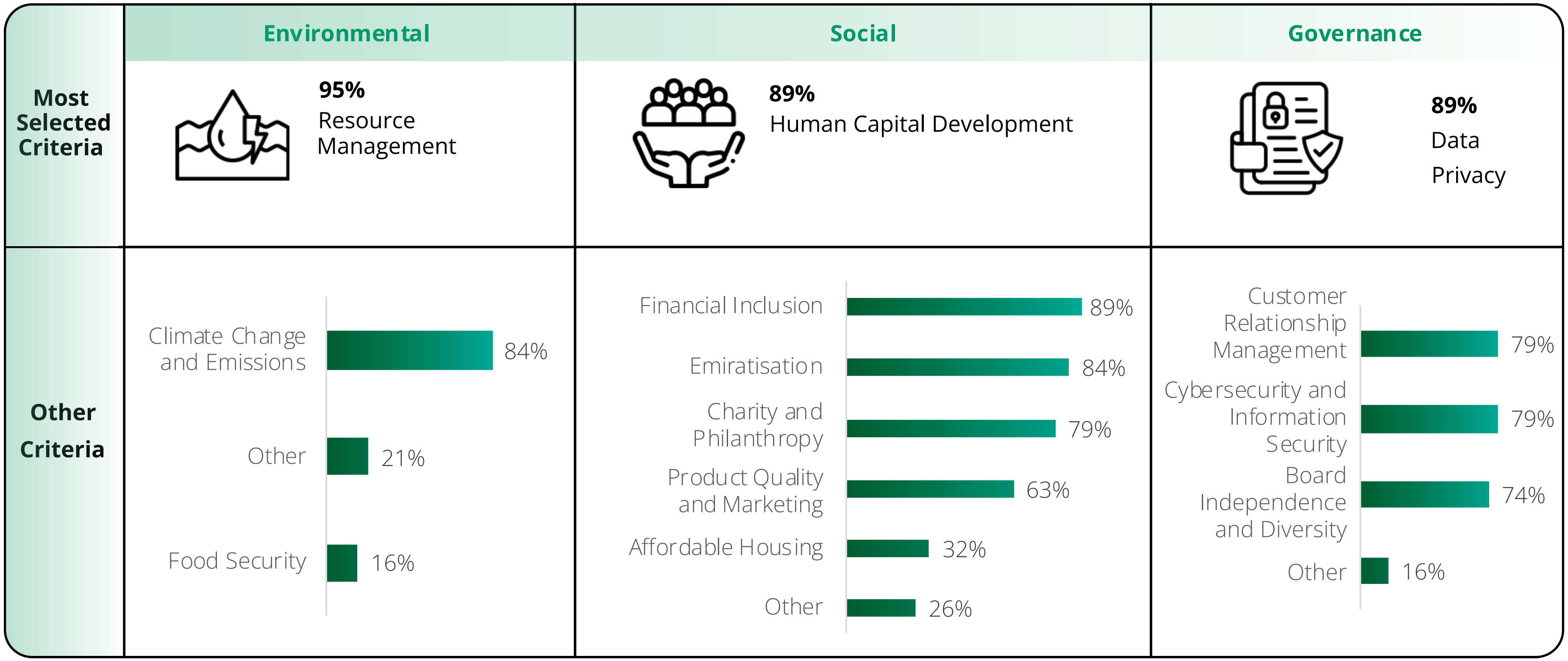
Figure 5.3: Main Parties Responsible for Driving Sustainability Strategy

Sustainability and **ESG Criteria**

Environmental considerations given priority by Islamic financial institutions: The UAE Islamic banking sector considers ESG criteria in its strategies, with resource management such as energy efficiency, water consumption, and waste management cited as the most widely adopted Environmental criteria. These criteria are considered by all fully-fledged Islamic banks with respect to the efficiency of their business operations.

Social and Governance criteria, which are covered by 100% of Islamic banks, focus on human capital development, charity, product quality and marketing, financial inclusion, board independence and diversity, data privacy, and customer relationship management. Other criteria considered by Islamic banks and Islamic windows include transparency, accountability and reporting under 'Governance'; green building standards under 'Environmental'; and financial literacy and attention to special needs under 'Social'.

Figure 5.4: Selected ESG Criteria by Islamic Banking Sector ESG Strategies



Sustainability **Roadmap**

Risk management and compliance are chief drivers of sustainability: Most Islamic banks and Islamic windows reported that regulatory requirements and risk management are the key drivers of their sustainability agenda. These drivers are followed by the desire to meet consumer demand and ensure alignment with Shari'ah principles. The latter factor was cited by 67% of full-fledged Islamic banks.

In terms of policy considerations for implementing ESG, 79% of Islamic banks and Islamic windows identify ESG issues such as emissions by their borrowers in their financing and investment models in a way that is sector- or country- specific.

In addition, 63% of respondents have considered UN Sustainable Development Goals in their sustainability frameworks. For Islamic banks, this proportion rises to 83%.

However, there is room for greater incorporation of metrics in policies. Only 53% of the Islamic banking sector discloses ESG portfolio metrics and just 37% use ESG impact-measured metrics of their product offerings when making decisions.

Figure 5.5: Key Driving Force in Embracing the Sustainability Agenda in the Islamic Banking Sector

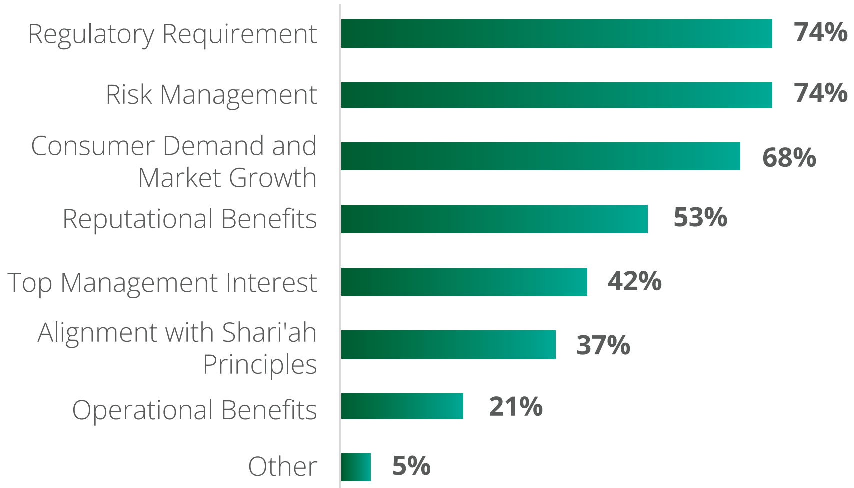


Figure 5.6: ESG Policy Considerations for Islamic Banking Sector

79% Take sector- or country-specific approach to identifying ESG issues

37% Have impact-measured metrics for decision-making

63% Consider UN Sustainable Development Goals

53% Disclose ESG portfolio metrics

Sustainability **Financial Goals**

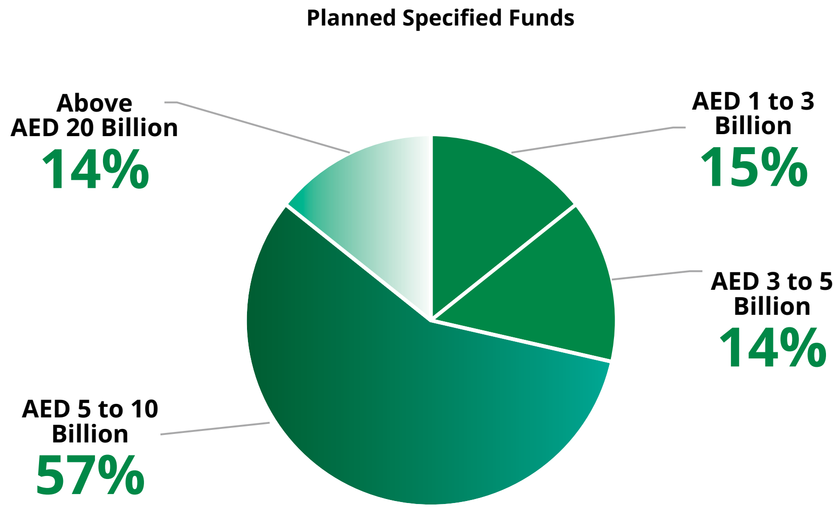
Over half of Islamic banks have made funds available for sustainability uses: Looking ahead, 58% of Islamic banks and Islamic windows have specified funds dedicated to sustainability in their medium-term plans. Of these institutions, 83% of full-fledged Islamic banks have made such commitments.

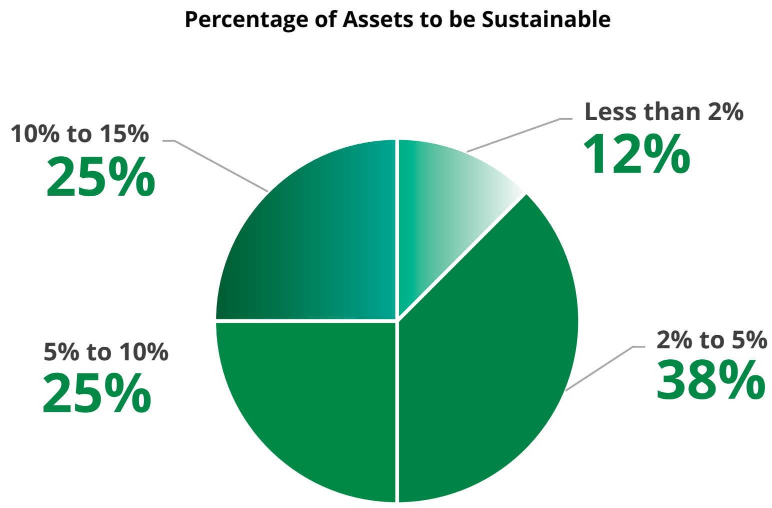
Also, 53% of Islamic banks and Islamic windows apportion a defined share of their assets for sustainability. This increases to 83% for full-fledged Islamic banks. Most UAE Islamic banks plan to allocate up to a 5% of their assets to sustainability linked projects within the next 3-5 years.

Figure 5.7: Planned Financial Commitment to Sustainability by Islamic Banking Sector in the Coming 3-5 Years

58%
Plan to commit specified funds

53%
Target a certain percentage of assets to be sustainable





Sustainability in **Product Offerings**

Sustainable products offered by the Islamic banking sector are mostly in financing activities: By product offering in the Islamic banking sector, 89% of banks take into account sustainability considerations in their financing activities while 100% of full-fledged Islamic banks do the same. For instance, some Islamic banks indicated that they are developing an ESG Due Diligence Toolkit to be used by credit, wholesale banking and investment business lines to assess the ESG performance of projects.

Most of the Islamic finance banks offer green products such as electric and hybrid vehicle financing, home financing that can be discounted for green-certified properties, green sukuk, or sustainability-linked financing, which is an arrangement where the borrower's costs are tied to the borrower meeting a certain set of green targets. The second-most chosen sustainable finance product offering is financing to SMEs, which could be in the form of working capital, small business financing, or financing for female entrepreneurs.

Other sustainable products include social financing in the form of government housing schemes, liability settlement financing, education, and Qard al Hasan financing. As for sustainability-linked deposits, these can be in the form of accounts used for sustainable projects aligned with a bank's sustainability framework. Other sustainable financing products include carbon trading and carbon derivatives.

Figure 5.8: Product Offerings with Sustainability Considerations

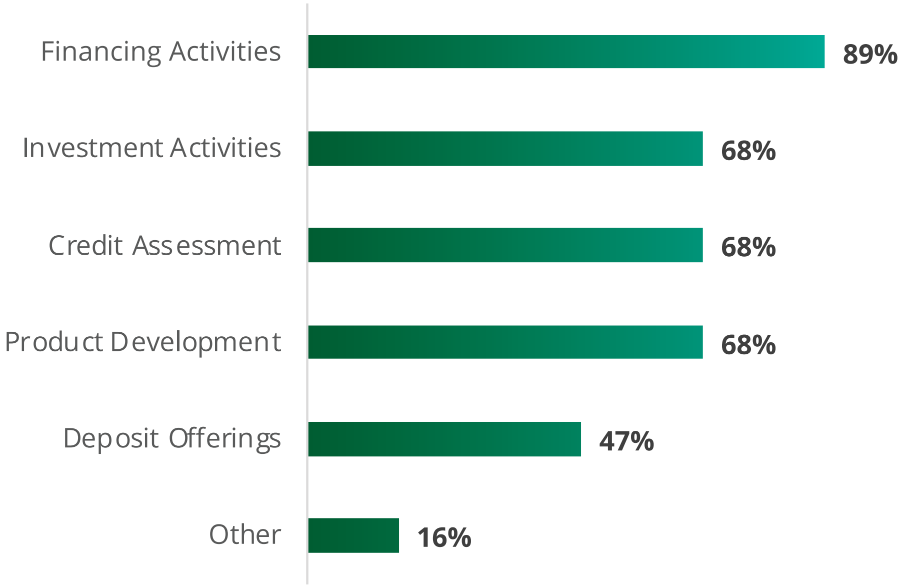
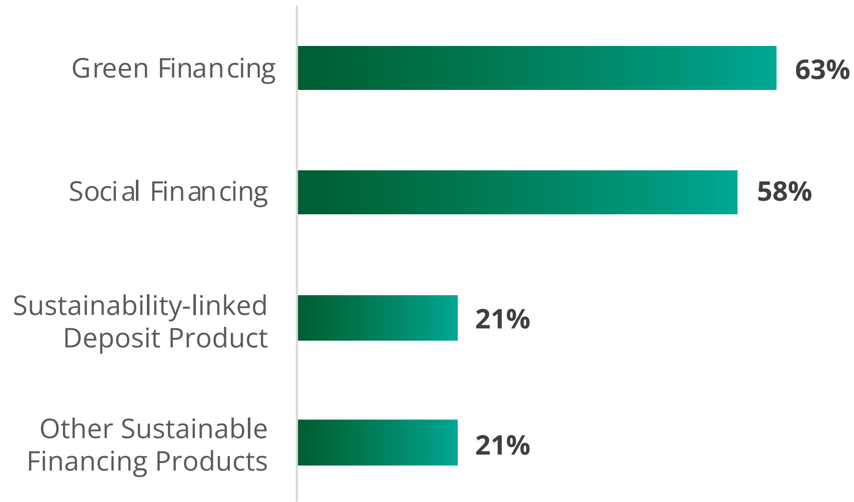


Figure 5.9: Sustainable Finance Product Offerings

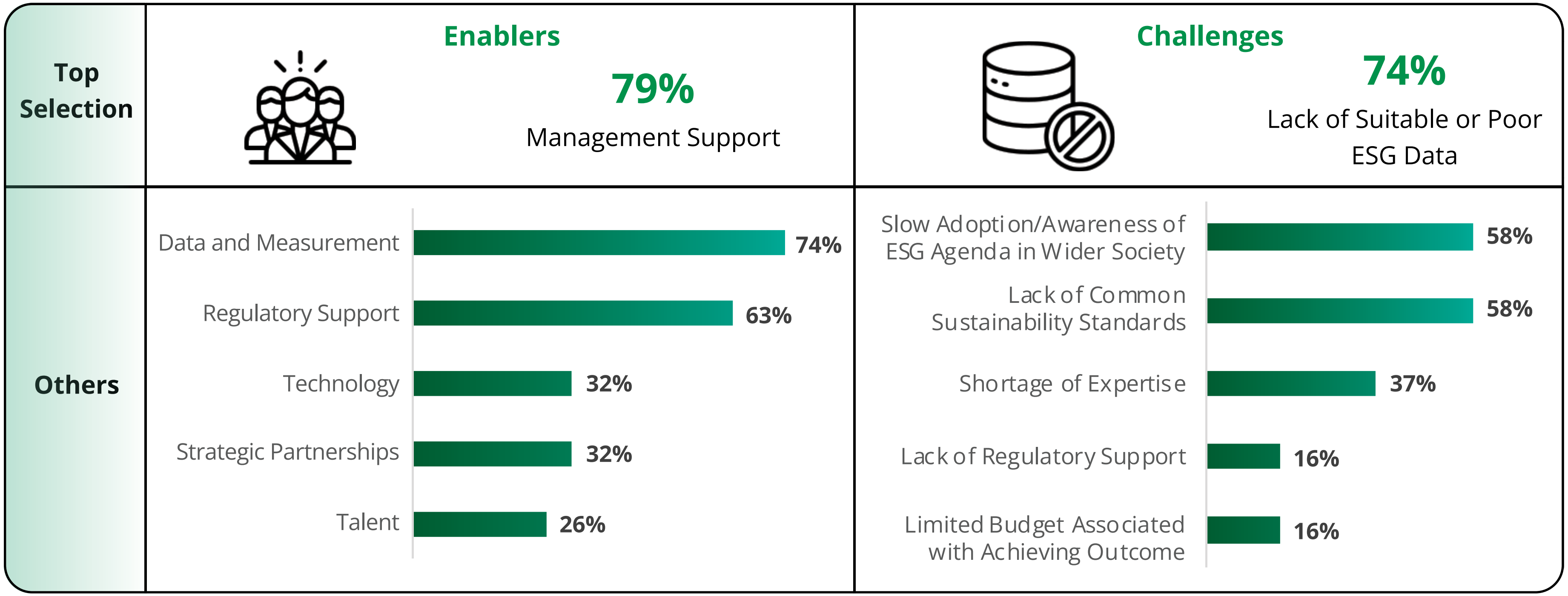


Opportunities and Challenges **in Implementing Sustainability**

Data is the biggest challenge for UAE's Islamic banking sector: Most of the banks operating within the UAE's Islamic banking sector cite Board and management support as the chief enabler of sustainability. Other enablers highlighted by a smaller number of banks include support from the UAE Banks Federation and internal Shari'ah departments.

Availability of data and measurement is both the second-most important enabler and, where there is a lack of such data, the biggest challenge to enabling sustainability. As we have seen, few banks are incorporating metric-driven considerations within their policies. Another challenge, although reported by a smaller number of banks, is conflicting internal policies.

Figure 5.10: Opportunities and Challenges in Implementing Sustainability by Islamic Banking Sector

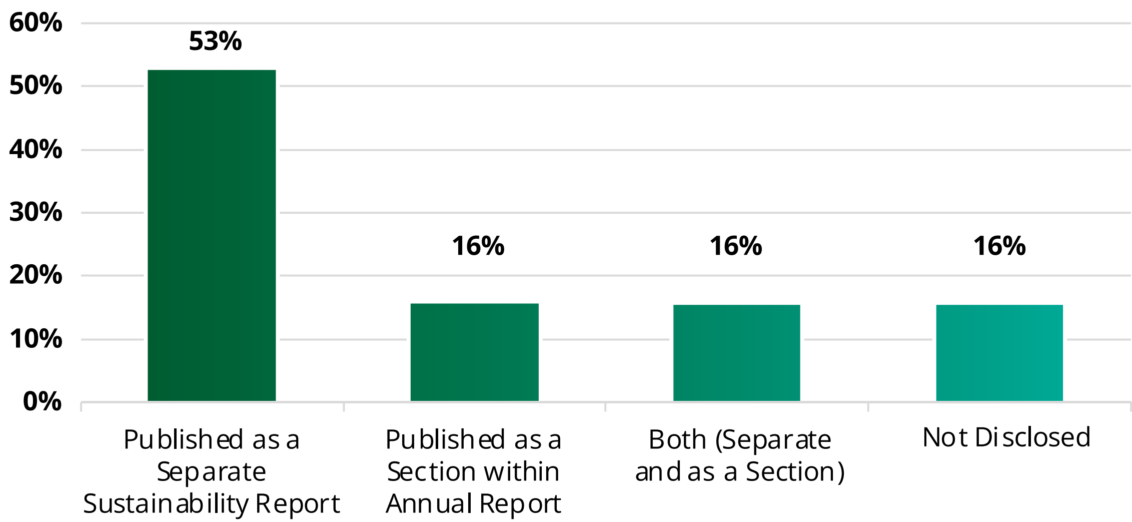


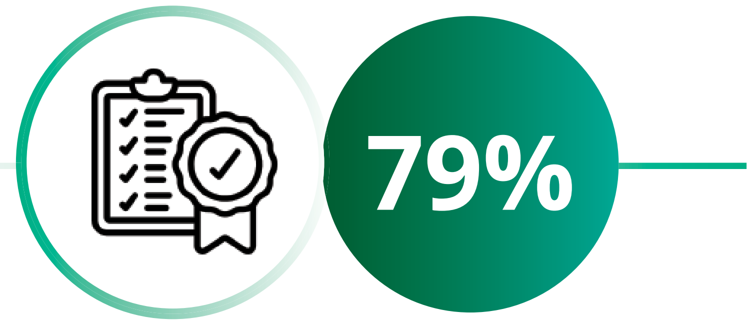
Sustainability **Disclosures**

Majority of Islamic banks align disclosure with internationally recognised ESG reporting frameworks: 85% of banks in the UAE Islamic banking sector report their sustainability activities. These banks either produce a separate sustainability report, include sustainability reporting in their annual financial reports, or do both. Sustainability reports by Islamic banks for 2022 included sections covering initiatives towards governance, customers, employees, and the wider community.

In addition, 79% of Islamic banks and Islamic windows align their reporting with internationally recognised ESG reporting frameworks such as Global Reporting Initiative (GRI) standards. All Islamic banks surveyed follow this method, though fewer Islamic banking windows. Some of the Islamic banks include in their sustainability reports an appendix covering a GRI table of information or GRI Content Index, which lists all applicable GRI standards and where this information is covered in the report

Figure 5.11: Disclosure of Sustainability Activities





Confirm their reporting is aligned with internationally recognised ESG reporting framework or standard

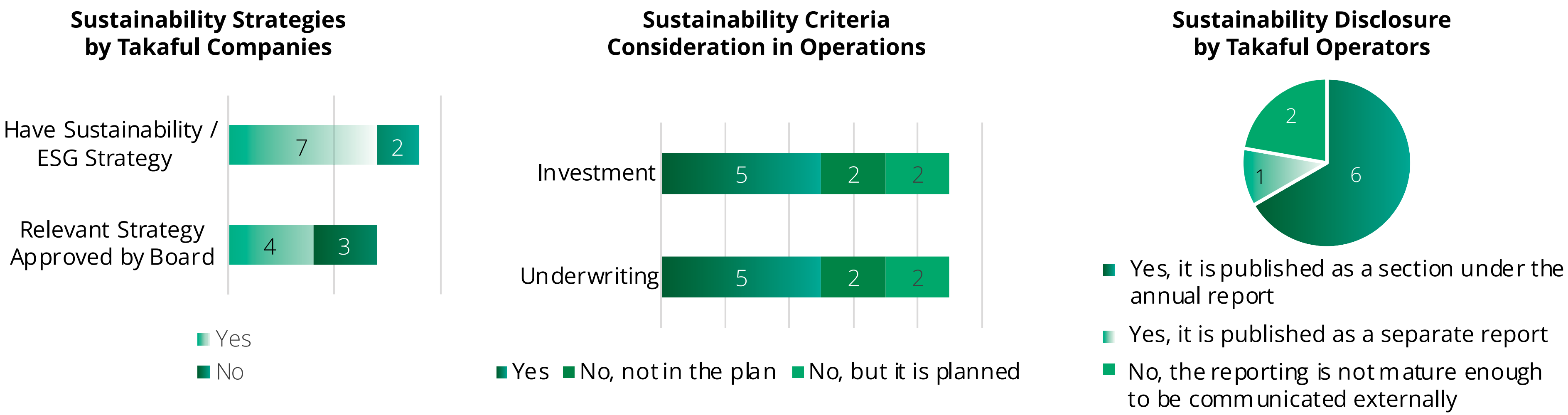
Takaful **Insurance Companies**

UAE takaful market's approach towards incorporating sustainability: Takaful is not unique among forms of insurance that can benefit from a developed approach to sustainability and climate risk. The CBUAE has been assessing the types of climate-related risks that could affect both conventional and takaful insurers.

In 2022, the CBUAE surveyed nine takaful insurance companies on their sustainability practices and found significant progress had been made across a number of areas, although more work remains to be done to deal with market challenges. Seven takaful insurance companies said they had a sustainability strategy and of those, four had been approved by the Board. The survey also showed seven companies had sustainability disclosure policies, with most such reporting included as a section within their annual reports. Five of the takaful insurance companies surveyed already integrated ESG into their investment operations and underwriting processes, while two were preparing to do so.

Many institutions are now able to incorporate ESG, including climate-related risks, into their core operations in certain ways, but they still face challenges stemming from the lack of sustainability guidelines specific to the takaful business model.

Figure 5.12: UAE Takaful Sustainability Survey Insights



Source: CBUAE Takaful Insurance Report 2022. To read the report:

Visit: CBUAE | Takaful Insurance Report 2022 (centralbank.ae)

Islamic **Finance Companies**

Islamic finance companies' approaches for sustainability: The survey reveals that fewer Islamic finance companies based in the UAE have sustainability agendas than do Islamic banks and Islamic windows. These companies rely on senior management and their boards of directors to drive sustainability, but none has appointed a specific sustainability officer.

Islamic finance companies' sustainable products mostly comprise financing channelled to SMEs such as financing related to solar power and energy projects dedicated for SMEs. Compared to banks, a lower percentage—40%--of Islamic finance companies said they published separate sustainability reports and 20% included sustainability reporting within their annual reports.

Figure 5.13: Sustainability Survey Results for Islamic Finance Companies

60% share of Islamic finance companies have sustainability strategy or approach

60% have their sustainability strategy approved by their board

60% have committed funds on sustainability and a targeted share within next 3–5 years

Chief Parties Responsible for Driving Sustainability Strategy

- Senior management
- Board of directors
- Risk management committee
- Human resources department

Leading Enablers

- Technology
- Management support
- Strategic partnerships

Main Challenges

- Slow adoption/awareness of ESG agenda in wider society
- Conflicting internal priorities
- Lack of common sustainability standards

Leading Selected ESG Criteria

- Resource Management
- Emiratisation
- Human Capital Development
- Data Privacy
- Customer Relationship Management
- Cybersecurity and Information Security

Figure **Appendix**

Table Appendix

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