

number of other Western financial institutions have followed suit by offering Islamic mutual funds and other investment products in an attempt to attract liquidity from this growing market. The growing sophistication of Islamic banks is leading an increasing number of Muslims to invest money in them.

The Islamic financial system is founded on the absolute prohibition of the payment or receipt of any predetermined, guaranteed rate of return. This closes the door to the concept of interest charges and precludes the use of debt-based instruments. The system encourages risk-sharing, promotes entrepreneurship, discourages speculative behaviour, and emphasizes the sanctity of contracts. Some banks that are not entirely "Islamic" do have an Islamic window to accommodate Muslim clients.

Islamic banks operate through Islamic financial instruments described below, being equity (same as conventional mutual funds), commodity and leasing. The future of Islamic finance seems bright, partly owing to the privatization trend under way in some Muslim countries such as Egypt, Jordan and Morocco, and in high-growth Islamic countries such as Malaysia and Indonesia, where the demand for Islamic financial products is growing rapidly.

While Islamic finance meshes well with project finance, observers don't expect projects costing more than \$200 million to be financed by Islamic funds alone. Given the capital requirements of many deals, especially in the Middle East's oil and gas sectors, most will need to combine Islamic financial products with conventional financing. Islamic finance is relatively inexperienced when it comes to project finance and privatization financing which implies a long-term commitment not characteristic of Islamic banking. In terms of participating in project finance deals, perhaps the most perplexing challenge facing Islamic banks lies in the Islamic investors' preference for investing their money short-term, whereas BOT projects, for example, are for the long-term.

Despite the mounting competition in the market and the gradual number of ground-breaking deals, further development of Islamic finance depends on how successful the Islamic banks can develop their ability in finding solutions to their shortcomings. They still are faced with a slow pace of innovation, new instruments are needed, a uniform regulatory environment and legal framework have yet to be developed. The development of an interbank market is another challenge, and, finally, there is a lack of uniformity in the religious principles applied by different Shariah Boards. Nevertheless,