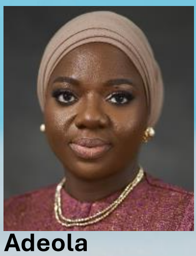
Islamic Finance in Nigeria:
2024 Year in Review and 2025 Outlook



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Nigeria, home to the largest Muslim population in Africa, with Muslims comprising 53% of its total population, presents a compelling landscape for the growth of Islamic Finance.

Rooted in Islamic principles of ethical and socially responsible investing, Islamic finance offers an alternative to conventional banking that adheres to Sharia law, prohibiting interest (riba), uncertainty (gharar), and investments in businesses considered as haram (forbidden).

Although still developing, Islamic finance in Nigeria has made significant strides over the past decade, garnering interest from both Muslim and non-Muslim investors. This growth reflects the increasing appeal of ethical and sustainable investment opportunities within the ecosystem.

According to the *State of Enterprise Report 2024*[1], Nigeria's Islamic finance industry grew to NGN2.5 trillion in 2023, up from NGN1.5 trillion in 2022. Islamic banking led the sector with NGN1.36 trillion in total assets, followed by sukuk (outstanding) at NGN1.09 trillion, while the remainder comprised Islamic (mutual) funds and takaful.

Deposits in Nigerian Islamic banks surged by 92.5%, reaching NGN971.53 billion in 2023 compared to NGN504.6 billion in 2022. Loans facilitated by these banks also increased by 60.7%, from NGN265.67 billion in 2022 to NGN426.86 billion in 2023.

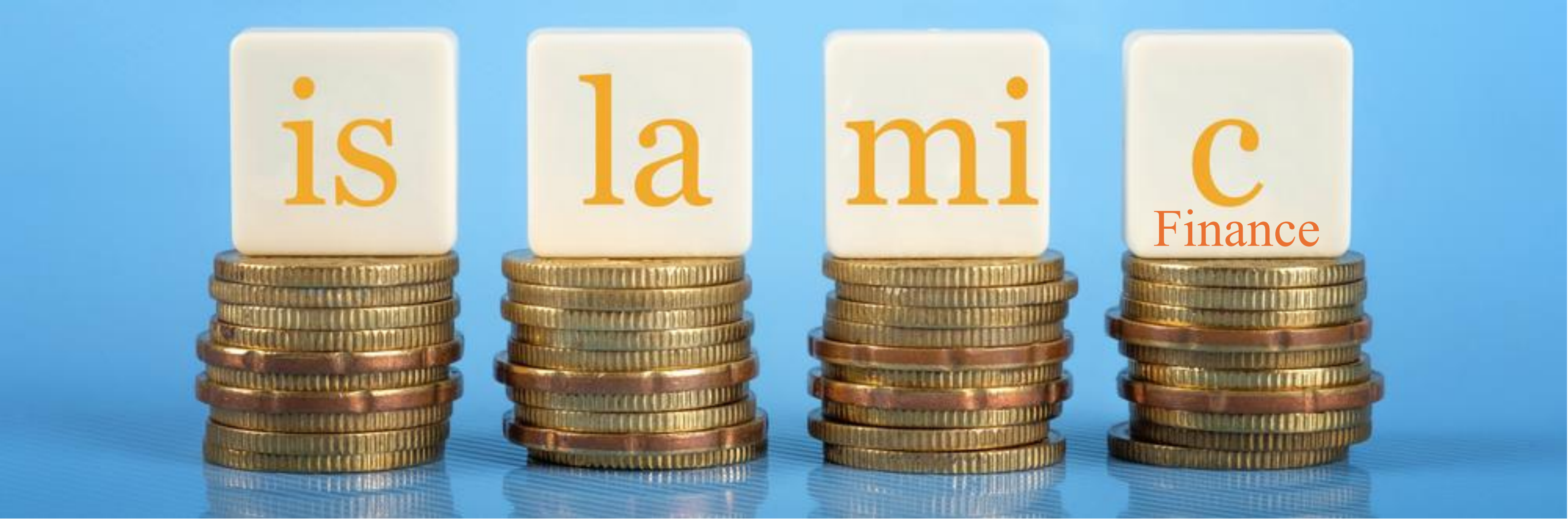
A Review of 2024

The year 2024 has been a pivotal year for Islamic finance in Nigeria, marked by several notable developments that have bolstered its position within the Nigerian financial sector.

Review of Minimum Capital Requirements

One of the key developments this year was the introduction of higher capital requirements for Islamic banks by the Central Bank of Nigeria (CBN) in March 2024. The CBN through its circular titled "Review of Minimum Capital Requirements for Commercial, Merchant and Non-Interest Banks in Nigeria" set a new minimum capital thresholds for Islamic banks, alongside conventional commercial and merchant banks, to be achieved by the end of the first Quarter of 2026.

[1] https://enterprisengr.com/wp-content/uploads/2024/08/State-of-Enterprise-2024-Report.pdf



This policy follows the sharp devaluation of the Nigerian Naira since May 2023, which has strained banking capital ratios and heightened credit concentration risks.

Capital Markets

Regulators have been instrumental in advancing Islamic finance within the year as the Securities and Exchange Commission (SEC) has intensified efforts to position Nigeria as a hub for Islamic capital market products as indicated in the SEC's 'Nigerian Capital Markets Master Plan 2021-2025.' The SEC has an ambitious target to list 50 Sharia-compliant products with a combined market capitalisation of at least NGN5 trillion (USD 11 billion) by 2025.In a recent move to strengthen investor awareness and collaboration within the sector, the Nigerian Exchange Limited partnered with the Islamic Development Bank Institute. The partnership aims to promote Islamic financial products and increase understanding of Islamic finance among investors, underscoring Nigeria's ambition to establish itself as an Islamic finance hub in Africa.

Non-Interest Commercial Paper Program

Another major development for Islamic finance in 2024 was achieved within the Capital Markets space. The sector witnessed the approval by the FMDQ Securities Exchange Limited of Nigeria's first non-interest commercial paper program. This development marked a significant milestone for Nigeria's Islamic finance options, particularly in the debt capital market, offering Sharia compliant, and non-interest bearing investments option to a growing pool of ethical investors.

Sukuk

Sukuk issuances in the private sector remained relatively low, in 2024, primarily due to the complexities and evolving Shariah requirements that come with issuing Sukuk. Several factors contribute to these challenges:

1. **Complex Structure**: The structure of Sukuk transactions is more intricate when compared to conventional debt instruments. They require the underlying assets to be Sharia-compliant, which often involves detailed legal and financial structuring to ensure that the transaction adheres to Islamic law. Private companies consider the process to be time-consuming and costly.
2. **Sharia Compliance**: Issuing Sukuk involves rigorous Shariah compliance processes. Companies must ensure that the assets backing the Sukuk are free from non-compliant activities, such as earning interest or dealing in prohibited items. The process of constituting, and obtaining approval from, a Shariah board can add complexity and delay to the issuance process.
3. **Lack of Familiarity**: Many private companies in Nigeria lack familiarity with the requirements and benefits of Sukuk, making them hesitant to explore this form of financing. As the market for private sector Sukuk is still developing, many companies prefer more conventional financing options that are easier to navigate and would rather adopt a 'wait and see' approach with sukuk issuances.
4. **Market Size and Demand**: The private Sukuk market is not as developed as the sovereign Sukuk market. As such, the perception is that there will be limited demand from investors, particularly if the size of the issuance is not

substantial or if there is insufficient understanding of Sukuk products in the broader investment community.

Despite these challenges, a few private sector companies issued Sukuk during the year under review. More issuances by private companies will grow over time, particularly as the market matures and more investors become familiar with the benefits of Sukuk as an alternative to conventional debt.

In the public sector, the issuance of Sukuk remained a driving force behind the growth of Nigeria's Islamic financial market in 2024. The Federal Government of Nigeria (FGN) has continued to leverage Sukuk to fund essential infrastructure projects, with the most recent issuance being a NGN350 billion sovereign Sukuk issued through the FGN Roads Sukuk Company 1 PLC. These issuances not only addressed solutions to infrastructure deficits but also showcased how Islamic finance products present a viable alternative to conventional debt instruments.

Having commenced the Sukuk program in 2017, the Federal Government of Nigeria (FGN) has diligently applied the proceeds from these sukuk issuances to fund the development of major infrastructure projects, including the construction and upgrade of highways and other road networks across the country.

The Federal Government of Nigeria (FGN) recently proposed issuing its first dollar-denominated Sukuk, valued at US$500 million. This proposal was approved by lawmakers as part of President Bola Tinubu's broader plan to borrow US$2.21 billion from foreign investors to help address the country's budget deficit[2].

Following the successful oversubscription of Nigeria's recent Eurobond, highlighting strong investor demand for Nigerian sovereign debt, however, the issuance of the dollar denominated Sukuk has been postponed.
The 2025 Appropriation Bill[3] which was signed by President Tinubu, excludes the proposed foreign currency denominated Sukuk issuance. This indicates that the government plans to delay the Sukuk issuance until 2025, possibly due to adjustments in its fiscal strategy or changes in market conditions and the FGN's ongoing efforts to manage its borrowing and financing needs more effectively.

Insurance Sector

In the insurance sector, there has been notable growth in ethical insurance products, particularly Takaful. Earlier this year, the National Insurance Commission approved Crown Takaful Insurance to begin operations, marking a significant step in providing Sharia-compliant risk underwriting alternatives. Crown Takaful introduced a range of products designed to cater to the uninsured, offering secure, ethical options for customers. Other pioneering organizations in the Takaful market, such as Hilal Takaful, Jaiz Takaful, and Noor Takaful, have continued to expand their customer base by offering Sharia-compliant solutions, further driving the growth of ethical insurance products in the country.

[2] https://www.islamicfinancenews.com/sovereign-securities-nigeria-to-issue-us-dollar-sukuk.html

[3] file:///C:/Users/TEMP/Downloads/2025%20Draft%20Bill.pdf

Islamic Funds/ Halal Funds

Islamic/Non-Interest Funds have also gained significant traction in Nigeria over the past year. The National Pension Commission (PenCom) initially launched the Non-Interest Fund in September 2021, accompanied by an Operational Framework for Non-Interest Fund[4], to provide a Sharia-compliant investment option. This fund is designed to be managed by licensed pension fund administrators, offering a sustainable and ethical investment avenue for Nigerian pension contributors seeking non-interest-based alternatives.

The growing interest in these funds reflects the increasing demand for ethical and Sharia-compliant investment solutions within the country's financial sector, as well as the broader push for financial inclusion. By offering alternatives that align with ethical principles, these funds are helping to ensure that more individuals have access to financial products that meet their values, while also promoting greater participation in the formal financial system.

Since its inception, the Fund has witnessed remarkable growth, demonstrating increasing acceptance among pension contributors and retirees. For example, the Fund's assets expanded from NGN7.79 billion in September 2021 to NGN 54.27 by the end of January 2024, marking an impressive increase of over five hundred percent. This growth trajectory highlights the effectiveness and growing appeal of the Non-Interest Fund among pension stakeholders, reinforcing its position as a preferred ethical investment option. On its part, the SEC has also played a crucial role in fostering the growth of Islamic Funds by approving and authorising the establishment of Halal Funds by registered and licensed Fund/Portfolio Managers. These Halal Funds adhere to Islamic finance principles, offering ethical investment opportunities for stakeholders. Notable examples of such funds include the One17 Halal Fund and the Marbel Halal Fund, both of which received SEC's approval within the year.

A Preview- 2025
Equity Investments

The outlook for the Nigeria's Islamic Finance sector in 2025 is optimistic, with significant developments anticipated to sustain its growth trajectory. A report released by Fitch Ratings on12th June 2024, projects continued expansions over 2024-2025, primarily driven by the anticipated increase in equity issuances for Islamic banks to comply with the CBN significantly increased capital requirements.

At the 2024 Islamic Development Bank annual meetings in Saudi Arabia, Jazi Bank PLC and the Islamic Corporation for the Development of the Private Sector signed a $20 million memorandum of understanding targeted at boosting its capital base in compliance with the CBN's new minimum capital requirements. In 2025, similar strategic agreements are likely to emerge as Islamic financial institutions explore diverse options to meet the CBN minimum capital requirements.

Commercial Papers

The issuance and approval of additional non-interest commercial papers is expected to be a key area of growth in 2025, providing organizations with an alternative method of securing short-term financing in line with Sharia principles. We also foresee ongoing support from key regulators, such as the CBN and SEC, in fostering a favorable regulatory environment for Islamic finance.

[4] https://www.pencom.gov.ng/wp-content/uploads/2021/06/OPERATIONAL-FRAMEWORK-FOR-NON-INTEREST-FUND.pdf

Sukuk Issuances

Another key driver for the growth of Islamic finance products and instruments in 2025 will be the Nigerian government's focus on addressing fiscal challenges, particularly the difficulty in aligning public spending with revenue. This issue, compounded by inflation, disruptions in crude oil production, low tax collections, and slow-paced economic diversification, has placed significant strain on the country's fiscal health.

To address these challenges, the FGN is likely to explore innovative solutions, of which issuing a dollar-denominated Sukuk could be a strong strategy for several reasons:

1. **Diversification of Funding Sources**: A dollar-denominated Sukuk would provide Nigeria with access to international investors, broadening its sources of funding beyond the domestic market.
2. **Appeal to Foreign Investors**: The success of Nigeria's recent Eurobond issuance highlights the strong appetite for FGN-backed instruments within the international investment community. A dollar Sukuk would further attract global investors seeking Sharia-compliant investment opportunities.
3. **Hedge Against Currency Depreciation**: Given the ongoing depreciation of the Naira, a dollar-denominated Sukuk would help the government mitigate the risks associated with currency fluctuations, offering a relatively stable investment option in US dollars.
4. **Supporting Infrastructure Development**: Historically, Sukuk proceeds in Nigeria have been used to finance key infrastructure projects, such as roads. A dollar-denominated Sukuk would continue this trend while attracting the capital needed for large-scale projects that could drive economic growth.
5. **Boosting Investor Confidence**: Issuing a dollar-denominated Sukuk would help reinforce investor confidence in Nigeria's fiscal management and reform efforts, demonstrating a commitment to diversifying funding sources and improving financial stability.

Despite these advantages, the success of a dollar Sukuk issue will depend on several critical factors, including the prevailing global financial environment and international investor sentiment toward Nigeria's economic and political stability. These elements will be key in determining the overall success of the initiative, as they influence investor confidence and the attractiveness of Nigeria's debt instruments on the global stage.

In the private sector, there is expected to be an increased appetite for Sukuk issuances as a means of funding infrastructure projects. Long-term financing is crucial for funding infrastructure projects, and Sukuk offers a viable solution for financing infrastructure projects over extended periods. The tenors of Sukuk can be tailored to provide the necessary duration for large-scale infrastructure development, ensuring that the repayment schedule aligns with the project's cash flow and development timeline.

As the market matures and awareness of Sukuk benefits expands, private sector participation in Sukuk issuances is likely to grow, supporting the financing of critical infrastructure projects.

Collaboration

To accelerate the growth of Islamic finance in Nigeria, we expect a significant increase in awareness and education about its principles and benefits among policymakers, businesses, investors, and other key stakeholders. By prioritising the sharing of knowledge and understanding of Islamic finance, its potential can be fully realized across various sectors. Additionally, fostering greater collaboration between Islamic financial institutions, regulators, and industry stakeholders will be essential in advancing the sector. This cooperative approach will help address challenges, streamline regulations, and unlock new opportunities, ultimately contributing to the further development and growth of Islamic finance in Nigeria.

Conclusion

As Nigeria's Islamic finance sector continues to mature, its development will hinge on a blend of regulatory reforms, market innovation, and strategic partnerships. By capitalising on these opportunities, Nigeria's Islamic finance sector can solidify its position as a vital component of the broader global financial ecosystem, contributing to economic development and financial inclusion.