How to measure the financial performance of investment portfolios in an Islamic financial framework?

Abstract:
With the rapid growth of Islamic finance in recent years, this system is facing a number of problems that now threaten its future development. One of the biggest problems is the lack of tools and models that can effectively assess, measure and rank the financial performance of investment portfolios tailored to the specific nature of Sharia. Indeed, all the tools and models used today by Islamic financial institutions were developed through modern portfolio theory without taking into account the principles of Islamic finance. If we observe the most often used tools like the Sharpe ratio, the Traynor ratio and Jensen's Alpha, we find that they are based on the existence of free risk assets which are not supposed to exist in Islamic finance. We think that the use of these tools as part of Islamic investment analysis is inconsistent and irrelevant. For this reason, we intend to develop a model to measure investment performance while taking into account the specific character of Islamic investment.