

Sukuk – An Important Asset Class

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Plan

- An overview of the Sukuk market
- Sukuk: an Islamic capital market instrument
- Sukuk : some basics and the secondary market
- Sukuk structures: the journey so far and some recent innovations
- Issue of purchase undertaking in some of the Sukuk structures

Overview of the Sukuk market: 2008 figures (as of October)*

Total Announced	59 Nos. (\$20 billion)
Total issued	140 Nos. (\$15 billion)
Total sovereign issues	40 Nos. (\$6 billion)
Total corporate issues	100 Nos. (\$9 billion)
Size	30 over \$100 million Largest \$1.3 billion (SABIC), May
Most popular type	Ijara (42) BBA / Murabaha (41) Musharaka (30) Mudaraba (10) Salam (9)

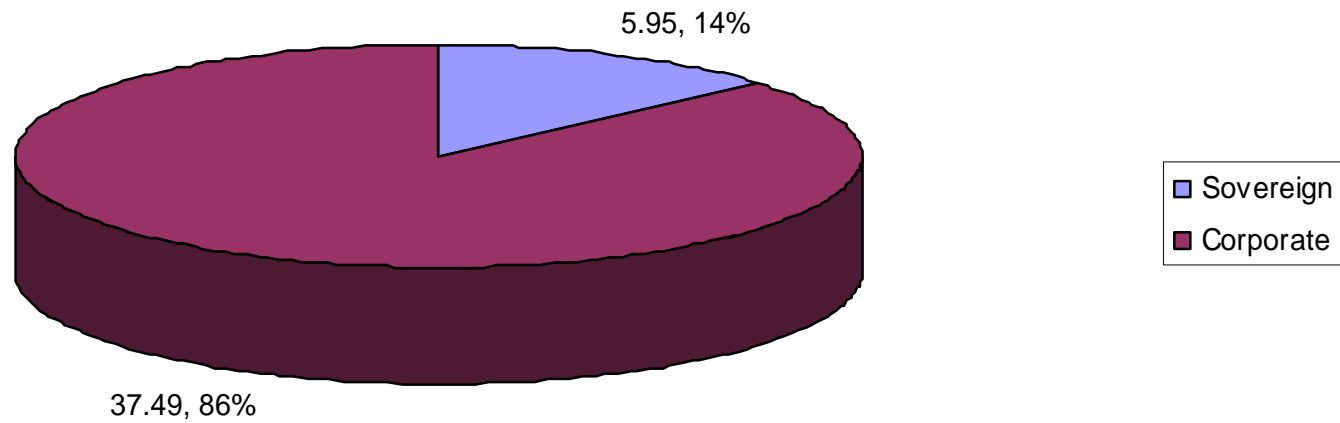
* Source: IFIS Database

Overview of the Sukuk market: 2007 figures

Total issued	206 Nos. (\$47 billion)
Total sovereign issues	51 Nos. (\$10 billion)
Total corporate issues	155 Nos. (\$37 billion)

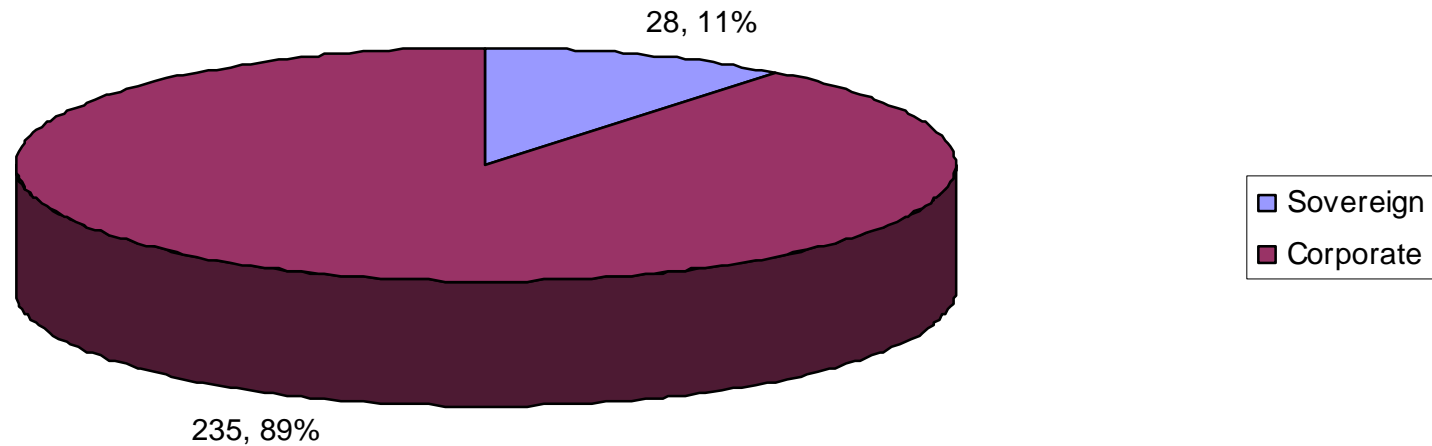
Overview of the Sukuk market

Size of Sukuk Issued (2000 - 2006) in bil \$



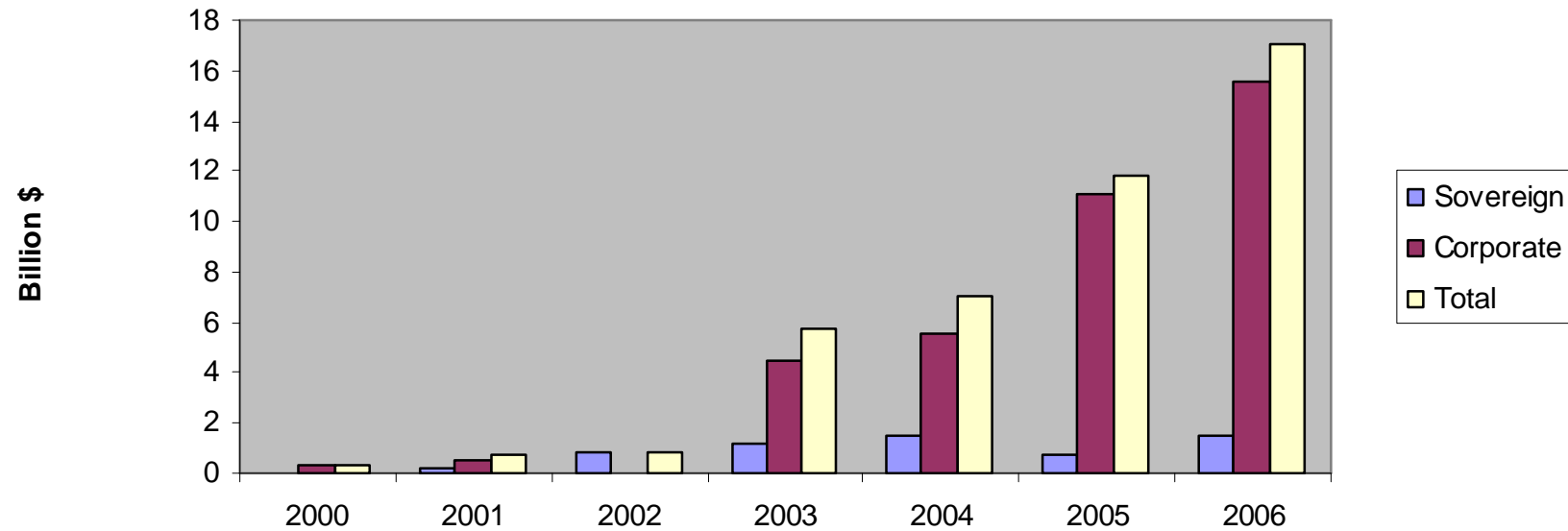
Overview of the Sukuk market

Total Number of Sukuk Issues (2000 - 2006)



Overview of the Sukuk market

Sukuk Issues: Year and Issuer Breakdown

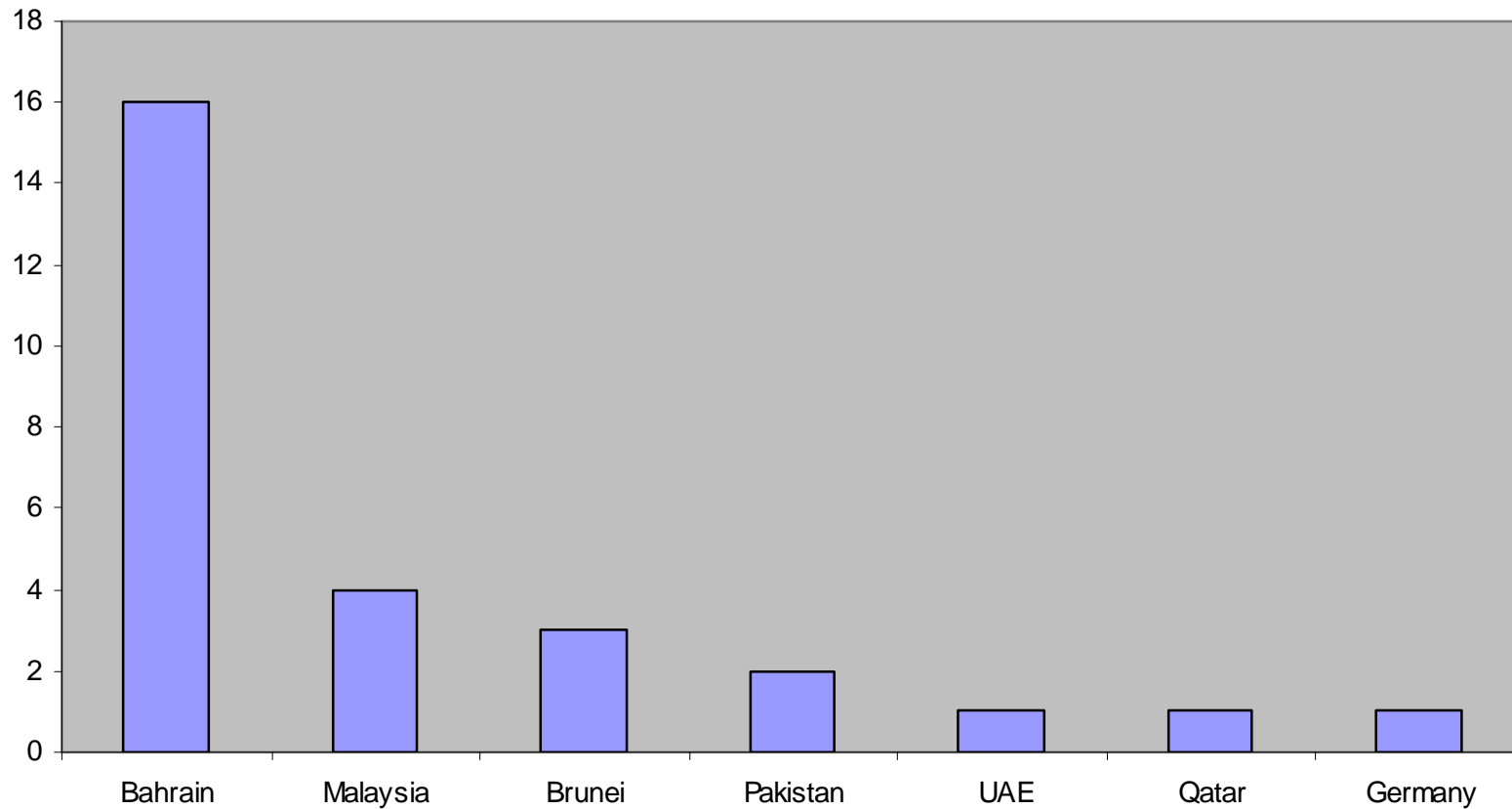


	2000	2001	2002	2003	2004	2005	2006
■ Sovereign	0	0.25	0.8	1.2	1.5	0.7	1.5
■ Corporate	0.34	0.53	0.02	4.5	5.5	11.1	15.5
■ Total	0.34	0.78	0.82	5.7	7	11.8	17

Years

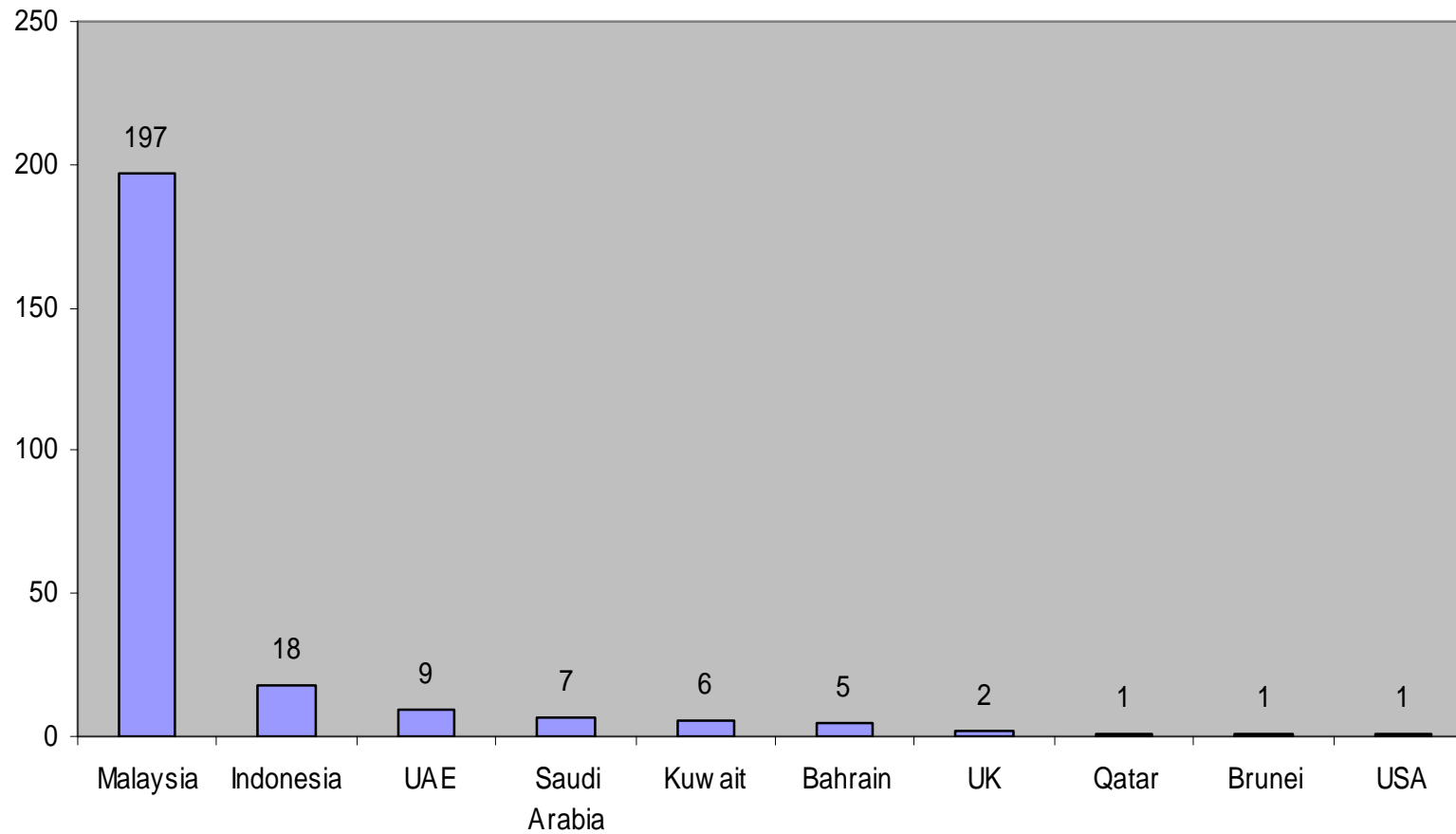
Overview of the Sukuk market

Leading Sovereign Issuers



Overview of the Sukuk market

Leading Corporate Issuers



Overview of the Sukuk market

- Some of the leading Lead Managers are:
 - Commerce International Merchant Bank Berhard (CIMB)
 - HSBC Amanah
 - Dubai Islamic Bank
 - AmMerchant Bank Berhard
 - Aseambankers Malaysia
 - Central Bank of Bahrain
 - Citigroup

Sukuk: an Islamic Capital market instrument

- Capital market is the market for securities, where companies and governments can raise long-term funds.
- Capital market includes in it the stock market and bond market, where equity and debt securities are traded.
- Islamic capital market also needs to have equivalent capital market instruments.
- While there is a good number of equity securities available, Sukuk is by far the only (commodity Murabah is another exception) Islamic instrument that translates the features of debt securities.

Sukuk: some basics

- In classical sense;
 - The singular word “Sakk” is derived from classical Arabic and means ‘a document representing a contract or conveyance of rights, obligations and / or monies’.
- Contemporary use of word Sukuk mean;
 - Financial securities of equal denominations represented by a portfolio of eligible tangible assets and/or services.
 - Hence, Sukuk represent Islamic Investment instruments registered in the name of their holders and are based on principles of sale (Murabaha, Salam and Istisna’), leasing (Ijara) or partnership (Mudaraba and Musharaka), whereby investors mix their funds with other investors to make profit.

Sukuk: some basics

- In a conventional framework, asset monetization is achieved through the process of 'Securitization', a structured finance process which involves pooling and repackaging of cash-flow producing financial assets.
- In Islamic finance, monetization of assets is achieved through the process of 'Taskeek' (process of Sukuk issuance).
- All assets can be securitized so long as they are associated with cash flow. Hence, the securities, which are outcome of securitization processes, are termed as Asset backed Securities (ABS).
- Hence, Sukuk are also considered similar to ABS.

Similarities of Sukuk with conventional securities

- Marketability: Sukuk are monetised real assets that are liquid, easily transferred and traded in the financial market.
- Ratability: Sukuk are easily analysed by international and regional rating agencies which facilitates their marketability.
- Enhancement: Different Sukuk structures may allow for credit enhancements or wraps that broaden their appeal to risk-averse investors in the Islamic investor sphere as well as conventional investors outside the Islamic market.
- Versatility: Versatility of Sukuk structures allows:
 - structuring across legal and tax domains of products that meet diverse financing needs;
 - offering fixed or variable income options;
 - cross listing capabilities; and
 - compatibility with global bond regulations.

Sukuk vs conventional debt securities

•Sukuk

- Participation in ownership of the company issuing the sukuk
- Right to profits & bear the loss
- Evidence of ownership transfer or beneficial ownership transfer
- Maturity corresponds to an underlying project
- Sukuk prospectus includes all Sharia rules related to the issue
- Sukuk Manager to abide by Sharia rules
- Manager of the Sukuk represents Investors & works for their benefits
- Manager invests proceeds in accordance with the approved terms listed in the bye-laws of the issue
- Under the management administration contract, investors could demise the manager

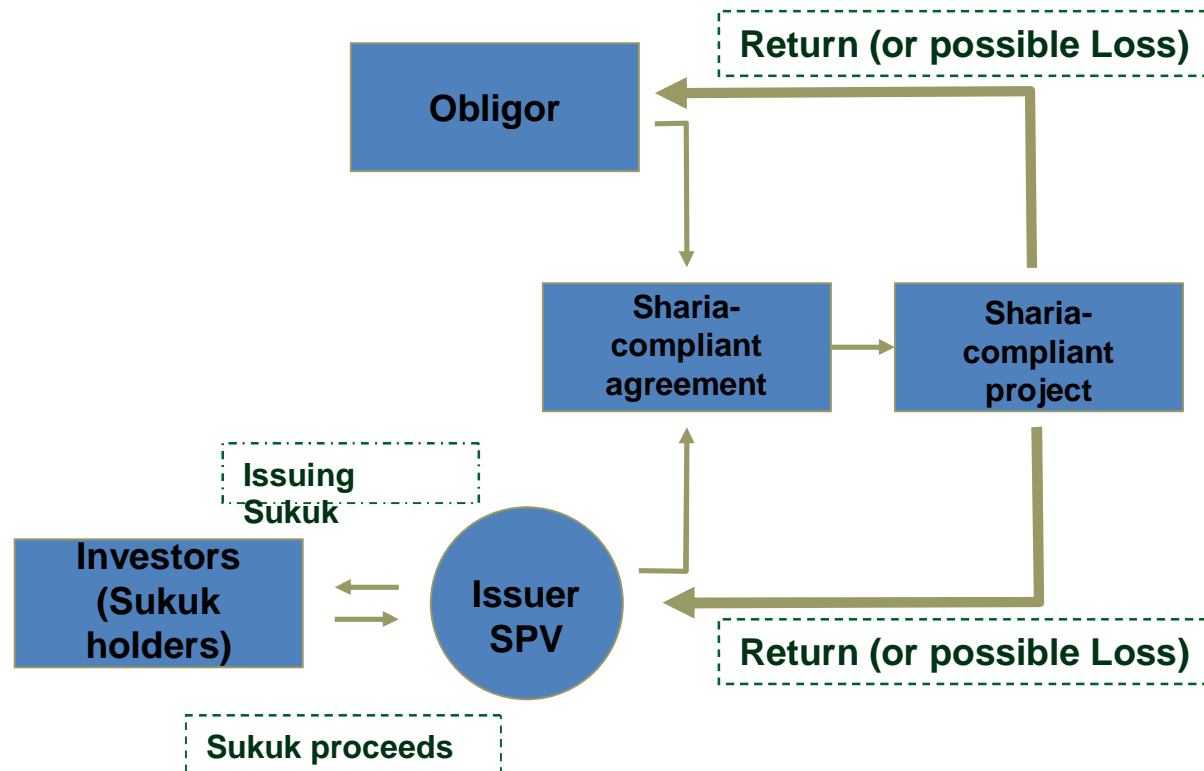
• Conventional securities

- No damage for loss
- Share in a financing process through usurious practices
- Term of securities does not match with the term of the underlying asset
- No Sharia constrains
- Manager has the absolute right to dispose of the proceeds
- Holders of the securities have no control over the manager's investment decision
- Investors are only concerned with the coupon

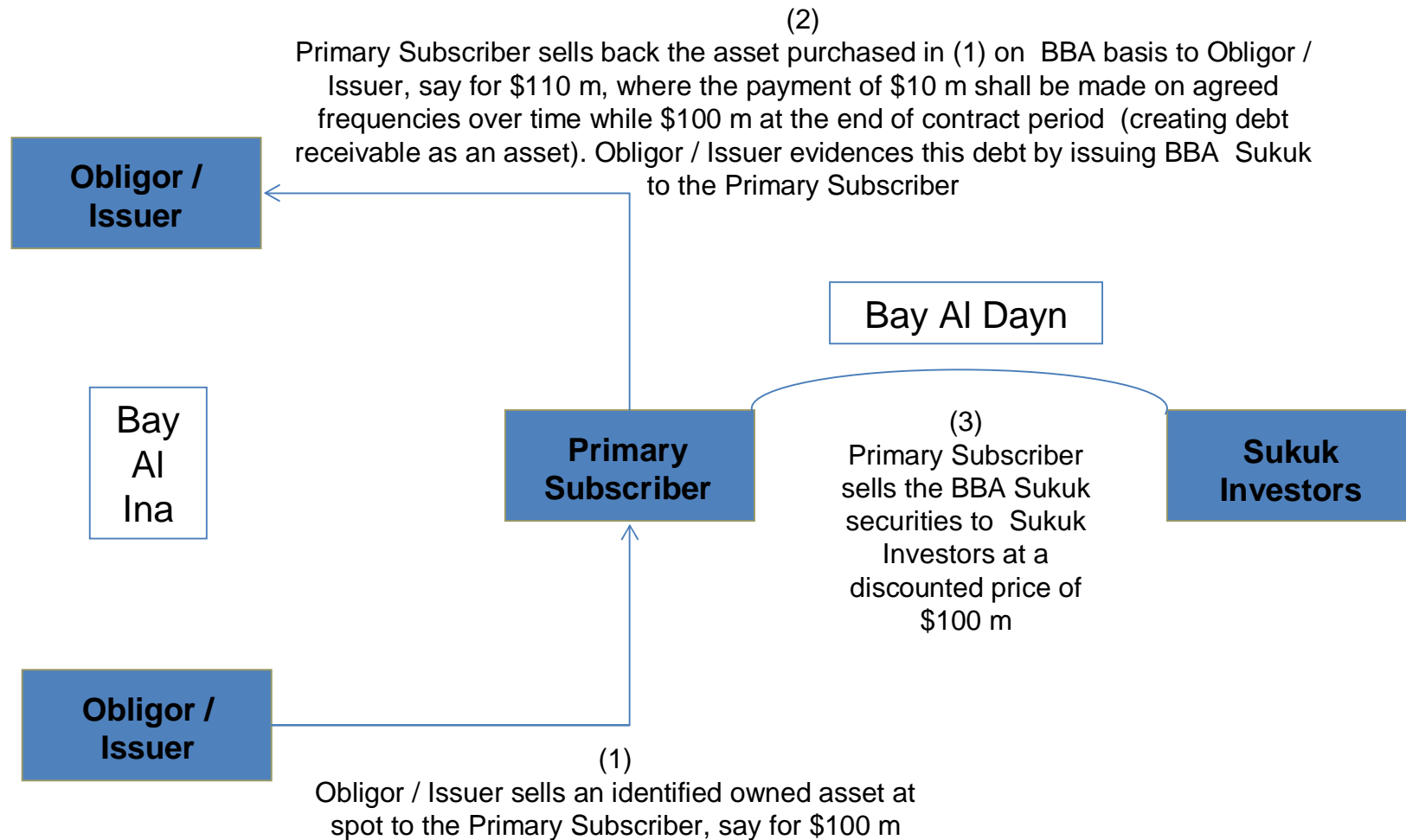
Secondary market for Sukuk

- It has largely been a buy and hold culture so far
- However, recent flurry of Sukuk in recent years has made trading of Sukuk more common, e.g.,
 - Barclays Capital on average it trades sukuk worth an average of \$20 million on the secondary market daily; and
 - Dubai Islamic Bank trades between \$100 million and \$250 million of sukuk on the secondary market every month.
- The changing profile of sukuk buyers (more western investors, not necessarily Islamic, are emerging).
- Liquidity Management Centre (LMC) in Bahrain as well, together with a handful of regional banks, has been offering

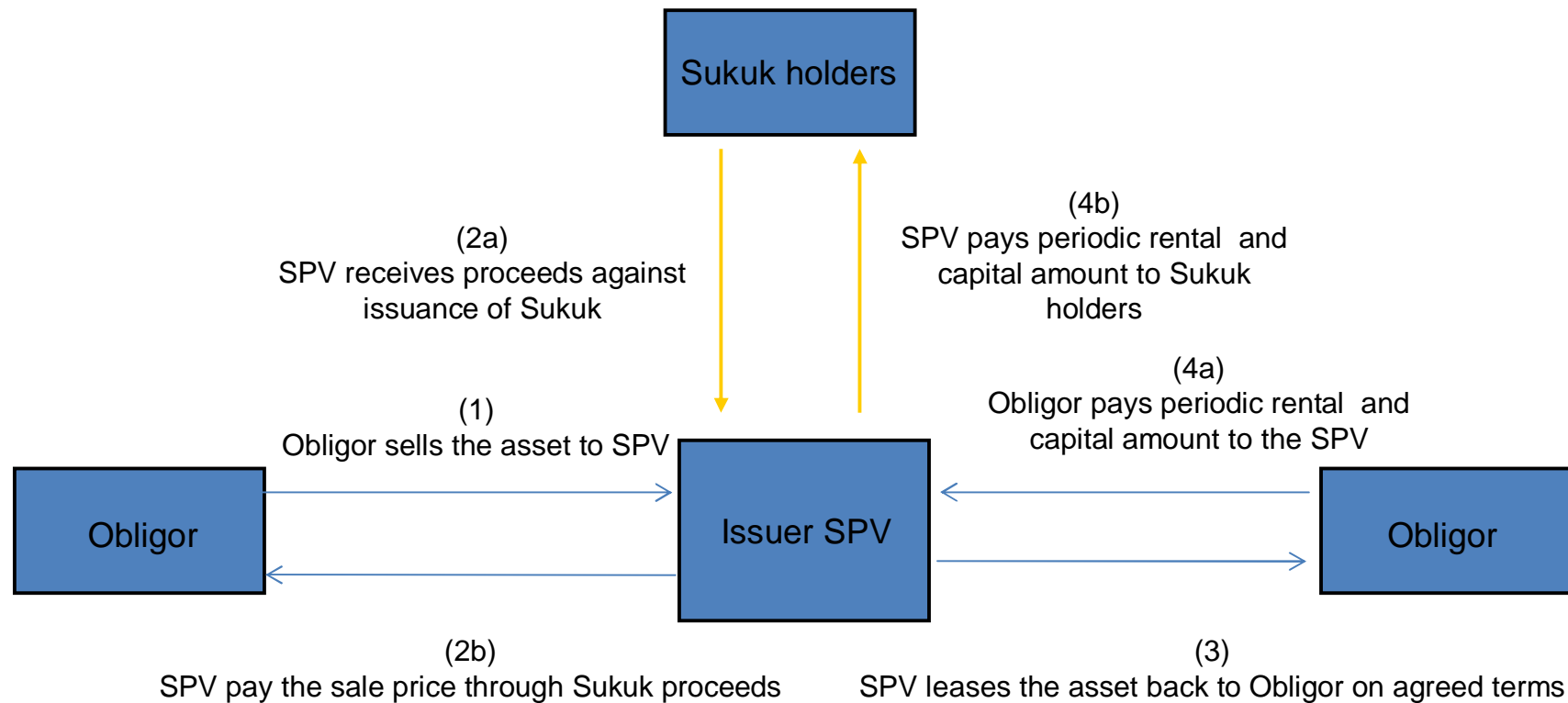
A basic Sukuk structure



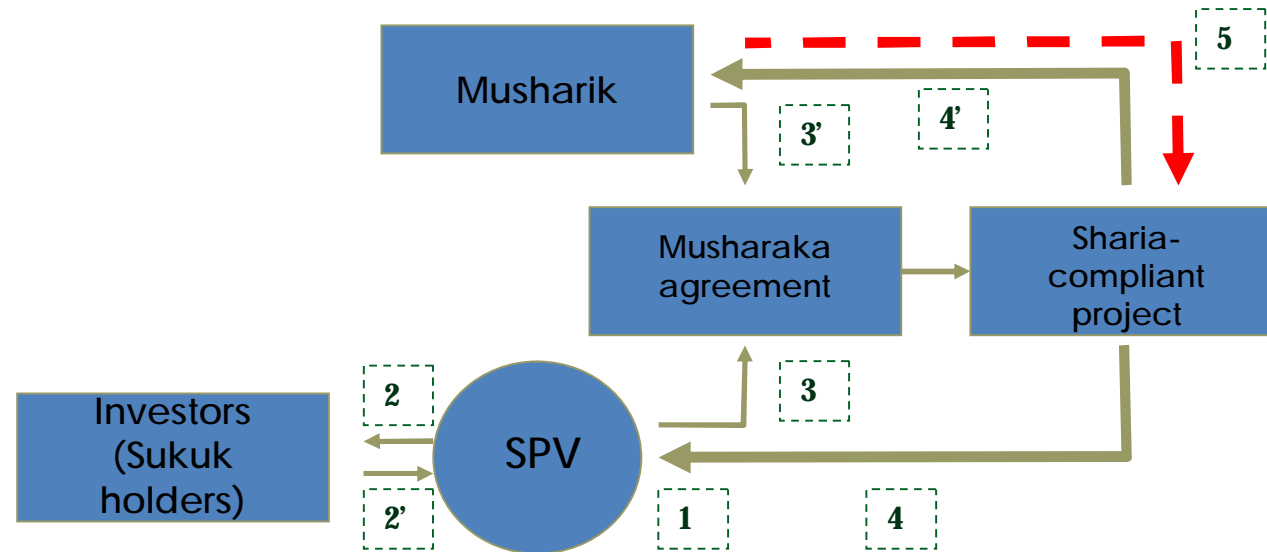
Initial phase: BBA / Murabaha structure



Initial phase: Ijara structure



Further development: Musharaka structure



- 1- Establishment of the SPV
- 2 -Issuing Sukuk to investors
- 2'- collecting proceeds from Investors
- 3 - Musharaka agreement - SPV (provides capital)
- 3'- Musharaka Agreement - Musharik (manager of the underlying project) contributes (usually in kind e.g., land)
- 4 - Profit distributed (or possible loss) according to the Musharaka agreement
- 4'- Profit distributed (or possible loss) according to the Musharaka agreement
- 5- Musharik Undertaking at Maturity to buy back the Sukuk & redeem investors the Notional value + last profit amount

More recent innovations: exchangeable Sukuk structures

- Exchangeable Sukuk structures are a unique innovation initiating from Malaysia and making significant inroads into the Middle East.
- While the primary Sharia structure usually is based on Ijara Sukuk, the flexibility that Sukuk holders do have an option of exchanging their Sukuk securities with ordinary shares of the Obligor is indeed very attractive for many investors.

More recent innovations: convertible Sukuk structures

- Convertible Sukuk structures is yet another unique innovation initiating from the Middle East.
- These structures, although primarily based on either Musharaka or Mudarabah, offer the Sukuk holders a right / option to convert part of their invested capital into shares of a designated entity of the Obligor.

Purchase undertaking in case of Mudaraba and Musharaka Sukuk

- An undertaking to purchase Sukuk assets at face value is considered a guarantee for the capital thus eliminating the possibility of profit and loss – an essential element of Islamic investment products
- Solution??????????????