

## THE AK BARS BANK DEBUT ISLAMIC SYNDICATION

THE UNFOLDING OF A TRANSACTION; OR A TALE OF SOME INCREDIBLE PEOPLE AND ANDY WARHOL

### A STORM IS COMING

"THE GOLDMAN SACHS STORM IS COMING!" SHOUTED THE SHIP CAPTAIN. "BRACE FOR IMPACT!"

## SHARI'AH-COMPLIANT RESIDENTIAL FUNDS IN CENTRAL LONDON

PROPERTY INVESTMENT FUNDS: PRIME LONDON CENTRAL

# THE AK BARS BANK DEBUT ISLAMIC SYNDICATION

THE UNFOLDING OF A TRANSACTION; OR A TALE OF SOME INCREDIBLE PEOPLE AND ANDY WARHOL



On 17 December 2010, at 4.30 in the morning, I was standing outside my hotel in Kazan in the middle of a snowstorm waiting for Anatoly, my driver, to take me to the airport. I had to board the early flight heading back to Moscow's Sheremetyevo airport to catch my connection that would take me back to my much coveted wandering life as an Islamic finance consultant in the Middle East.

Three hours of sleep and a temperature of minus 29 degrees centigrade did nothing to dampen my elated mood. The phone call I had received very early the previous morning was still echoing in my ears. I could finally see the light at the end of the tunnel ... my efforts to open up the Russian market to Islamic finance were almost coming to fruition.

It had been a long journey. For almost two whole years, I had pounded the road striving to raise awareness and drum up a consensus on the feasibility of Islamic finance in Russia. The number of conferences and public debates I had spoken at, the articles and interviews, the research and data gathered, though encouraging, showed a quite fragmented and at times controversial picture. It produced evidence of the existence of a lively and passionate Muslim civil society that wanted to bank Islamically which, in a bid to assert its own identity and citizenship rights, was populating dozens of websites dedicated to Islamic social and economic issues. Also, there was evidence of attempts by the big Russian players, the VTBs, the Gazprombanks, the Sberbanks, the influential Association of Regional

Banks of Russia as well as the City of Moscow, Russia's largest municipal borrower, to venture into this new market with its fuzzy edges, although bursting with opportunities. And then there was the Kremlin that, in a bid to reposition itself favourably in the emerging 21st century new world order, had intensified its diplomatic engagements in the Islamic world with Putin calling Russia a "Muslim power that wants to play a role as such among Muslim countries".

The political elite was indeed showing a benign attitude towards Islamic finance, giving its blessing to the granting to Russia of permanent observer status by the OIC, and pleased by the efforts displayed by the IDB to facilitate Islamic finance in their country. Yet, nobody seemed to be able to connect the dots,

*By: Alberto Brugnoli*

assemble the pieces of the puzzle, take that leap forward and make it happen! Marginal transactions had indeed been happening since 2006, when the first Murabahah facility had been arranged for a Russian trading house and for the last couple of years the market had been buzzing with rumours of Sukuk on the verge of being issued by a prime domestic bank teaming up with an international player, but the transaction that would turn the tables had yet to materialize.

A few days prior to my snowy early start, I was in Moscow. Madina Kalimullina, the enthusiastic young lady heading the Department of Economic Programmes of the Russian Muftis Council, had proudly shown me the Russian translation of the AAOIFI Shariah standards in her office. This is an initiative unparalleled in most non-Muslim countries. The 'Sociological Research on Islamic Finance in Russia' has confirmed that a pent-up demand exists for Murabahah and Ijarah financing from SMEs and family businesses across the country. Yet, on that very same day, the middle management of the Central Bank of Russia attended my lecture at the Finance University in Moscow and expressed skepticism on the applications of the principles of Islamic finance.

Yes, the value of the proposition was compelling and the 20 million strong indigenous Russian Muslim community was certainly entitled to bank Islamically, but the proper regulatory framework simply was not in place. Besides, many of the key senior officials at the Russian Central Bank were diehard monetarists and were dismissive of the developments of Islamic finance in some western European countries as being whimsical efforts. The introduction of tax neutrality measures was also needed, as it was in all other

European jurisdictions, but this tedious and lengthy process had not even begun to push any possible transactions into the foreseeable future. And certainly, I was advised, banks were not allowed to get involved in any trading activity; a fundamental condition to provide them with Islamic monies through the Islamic financing structure that I had in mind.

In fact, the sense of disillusionment that pervaded the market had infected me as well. I started wondering whether it was preposterous to think that a consultant, though considerably well-known in the market, could succeed where other much bigger players had stumbled. And was not the Islamic finance fraternity supposed to graze in more suitable pastures, where Arabic was spoken and the chant of the muezzin heard? Skepticism and fatigue definitely began to have the upper hand!

But help was close by. Roustam Vakhitov, an internationally recognized tax adviser – an authority on the intricacies of Russian tax and banking regulations and the editor of the Russian version of the AAOIFI standards – had invited me to dinner two days beforehand in a cozy Ukrainian restaurant. The conversation had soon drifted towards my frustration at being unable to put together, under the current regulatory and legal framework, a syndicated financing that for the first time would have given Russian SMEs access to Shariah-compliant funds. Roustam had listened attentively, smiling wryly from time to time, and obligingly promised to delve into this seemingly thorny issue that very night. The phone call came. Roustam kept his promise and found a way out of my conundrum. He virtually pulled a rabbit out of a hat! He had found that an obscure and often neglected

clause of the banking regulations did in fact authorize Russian banks to trade precious metals for their own account, provided they had been granted a proper authorization by the Central Bank.

Not only that, but if the trading was made abroad this would not trigger any VAT, an issue that had killed many transactions in countries where the tax laws had yet to accommodate Islamic finance. This simple finding – later to be met with skepticism by the very same players that had tried for years to start the Islamic finance process in Russia – made it possible even for a conventional bank to tap the Islamic markets in the Gulf, channel the capital raised to its own balance sheet through a commodity Murabahah and use it to provide Shariah-compliant financing, predominantly through the Ijarah contracts, to Russian SMEs.

In due time, the generated Islamic financial assets could be securitized through the issuance of a Sukuk al-Wakalah bil-Istithmar thus putting Russia on the Islamic capital market map.

Anatoly, the driver, was late. I passed the time reflecting on my second visit to the capital city of the Republic of Tatarstan. A city of 1.5 million people that gently spreads between the imposing white Kremlin – with its surreal Qol-Sharif, the mosque named after the national poet who died there defending the city from the forces of Ivan the Terrible and one of the most important symbols of Tatar aspirations – and the banks of the Volga river, so central to many important events of glorious Russian history. I had singled out Tatarstan as a possible enabler for the debut transaction I had in mind, as it possessed the features that would help me create an enticing selling proposition in the Gulf.

Its strong Islamic identity can be traced back to AD 921, when the Abbasid caliph al-Muqtadar had sent the Muslim writer and traveller Ibn Fadhalan as his ambassador to the king of Volga, who was eager to know how a religion that had grown out of the heart of the desert had succeeded in establishing an empire rivalled only by Alexander the Great. Tatarstan has evolved into a modern and vibrant society.

The Republic has indeed become a model of tolerance and harmony, where Tatars (ethnically Turkish and mostly Muslims), Russians (usually Christian Orthodox), sizeable ethnic minorities of Ukrainians and Chuvash, and small Jewish, Buddhist and Hindu communities all live together and where mosques, churches and temples sit literally side by side.

Kazan is home to the Russian Islamic University, founded in 1998 by Tatarstan's Spiritual Board of Muslims, the Tatarstan's Academy of Sciences and Russia's Council of Muftis, and is the only place in Russia where Muslims can receive a top-notch formal Islamic education in Shariah, theology, Islamic Sciences and Law, the Koran, and Islamic economy. The government, eager to enhance Tatar identity, has shown a keen interest in expanding its relationship with the Islamic world and in 2010, Ekmeleddin Ihsanoglu, the Secretary-General of the OIC, was made a foreign member of Tatarstan's Academy of Sciences – due to start publishing an English-language publication called 'Tatar History and Civilization'.

Besides that, the government was fully backing the development of Islamic finance in the Republic and signing Memorandums of Understanding with Islamic finance players around the world. Linova, the renowned advisory company headed by Malaysian-trained Linar Yakupov, was the only body in Russia and

CIS countries to have the status of observer member at the Islamic Financial Services Board.

The day before I was due to fly out, I had had long meetings at the AK BARS Bank's headquarters. I shared with them the happy news of Roustam's findings and discussed in detail the structure of the debut Islamic syndication that could possibly place this leading Russian bank as a trendsetter in the domestic banking market. In order to push boundaries you need visionary leaders; Robert Minnegaliev, the Chairman of AK BARS Management Board, certainly was one. A well-trained economist and a man of humor.

During my first visit in June, he had started our preliminary discussions by saying that, as he was coming down from his office to the boardroom to meet me, he had lost a button from his shirtsleeve – a very good omen in the Tatar tradition! Aware of the economic importance of Tatarstan, one of the most prosperous oblasts in Russia and strategically positioned along the Western Europe-Western China transcontinental transport corridor, he had a clear understanding of the long term contribution that Islamic finance could make to its sustainable development. Robert was confident that my long experience in Islamic finance and the vast array of relationships that I had built up over the years in the Arab world, could be combined with the strong balance sheet of his bank and the respect it commanded in the international conventional capital markets. He knew these factors would blend well together and help to successfully position AK BARS as the conduit of choice to convey Islamic money to the region.

But, the fulfillment of the mandate he gave me threw up unexpected challenges. In the subsequent months I crisscrossed the Gulf

countries making presentations to practically every single Islamic finance institution on the structure that I had put together. But, I found myself more in an explanatory and capacity building role with regards to Islam in Russia, rather than commenting on the merits and strategic value of the proposed transaction.

Few of the potential participants to the syndication had, in fact, ever heard of the Volga Tatars, the Bashkirs, the Chechenians, the Avarians and the Lezginians of Dagestan, the Kabardinians, the Darginians, the Kumiks, the Ingushs, the Karachais, the Adigians, the Balkarians, the Cherkessians and the Ossetians, who together formed a lively community of more than 20 million Muslims. Few knew that, after Istanbul, Moscow was the largest Muslim city in Europe and the hub for some 100 to 120 million Muslims living in the CIS and Eastern Europe countries. And very few knew that some of the most important Russian businessmen were Muslims. The appeal was certainly there, but also a sense of fear that we experience when confronted with the unknown. A newer and smarter way of communicating was certainly required to convey the image of a proudly Islamic yet modern country and of a well-balanced multi-faith, multi-racial, multi-language country offering enticing business opportunities.

In the middle of last century, Vladimir Propp, the Russian philologist and formalist, had identified the basic plot components of Russian folk tales and by doing so founded modern narratology. This science is the basis of contemporary storytelling, an ensemble of communication techniques used nowadays even in marketing, as they are deemed to be a more compelling and effective way to share ideas and business propositions than using dry facts and numbers.

## История дебютной сделки ОАО «Ак Барс» Банка по привлечению синдицированного финансирования по исламским принципам

Казань. 17 декабря 2010 г.. 4:30 утра.

Я стою у отеля в ожидании водителя Анатолия, который отвезет меня в аэропорт. Метель. Я собираюсь вылетать ранним рейсом в московский аэропорт Шереметьево, чтобы успеть на рейс, который вернет меня к столь любимому и привычному «кочевому» образу жизни в роли консультанта по исламским финансам в странах Ближнего Востока.

Ни три часа сна ночью, ни температура в минус 29 °С не влияют на мое приподнятое настроение. Ранний телефонный звонок прошлым утром продолжает звучать в моем сознании. Я, наконец, могу различить свет в конце туннеля... Мои попытки открыть российский рынок навстречу исламским финансам практически начинают приносить свои плоды.

Это был долгий путь.

Почти два полных года я протоптал эту тропинку, исполненный желанием

повысить информированность среди населения и добиться всеобщего признания реалистичности исламских финансов в России. Все те конференции и публичные дискуссии, в которых я принимал участие, изученные мною многочисленные статьи и интервью, исследования и статистическая информация, хотя и впечатляли, но в то же время представляли достаточно обрывочную и порою противоречивую картину. Было заметно, что в России имеется активное и энергичное мусульманское гражданское общество, заинтересованное в ведении банковских операций по канонам ислама и которое в своем стремлении отстоять свою идентичность и гражданские права, заполняет десятки интернет-сайтов, посвященных исламским социально-экономическим вопросам. Нельзя и не упомянуть таких крупных российских игроков как ВТБ, Газпромбанк, Сбербанк, влиятельную Ассоциацию региональных банков России, Правительство Москвы (кстати сказать, крупнейшего муниципального



заемщика), которые предпринимали неоднократные попытки войти на этот новый рынок с неясными очертаниями, но в то же время полный возможностей.

Find this article in Russian on "The economic portal of the Mufti Council of Russia". (<http://www.muslimeco.ru/opubl/174/>)

I decided to take a leap in the dark and took advantage of Propp's ground-breaking work to produce a short video clip that would narrate an illustrative and easily memorable story portraying the potential investors as leading characters, with AK BARS slightly in the background. I hoped that by building the whole story around the viewer of the video and taking into account his wishes and dreams, it would empower him, calm his uneasiness, tickle his curiosity and create strong emotional bonds with Tatarstan.

And, in the end, this would facilitate the transaction. Paola Trapani, professor of communication at the 'Politecnico di Milano' generously wrote the storyboard. Andrea Perugini put together the animation that was produced in no time at all by Abdul Halim, the head of Damask Media in London. Then David Evans, the ex-BBC World Service presenter and member of the UK actors' union, lent his voice to the story.

The clip, widely distributed across the Gulf, proved to be a blessed initiative as it helped to smooth out the rough edges, allay some fears and became an integral part of my standard business presentation.

From that point forward, I focused on the appointment of the lead managers and hastened on with the search. My goal was to find two iconic Islamic finance institutions representing different sets of stakeholders that could distribute the syndication in areas wide apart not only geographically, but also culturally. The values proposed by Islamic finance are indeed consistent with universal values and if properly presented they can certainly contribute to a healthier approach to finance than the one followed by Western societies – who seem to have lost the plot – and help build bridges between civilizations and societies.

And what better opportunity to send out this message than an Islamic syndication originating from a country that had been at the crossroads of Bagdad and Byzantium and part of the Golden Horde? A Christian Orthodox country, whose ties with the Arabs and the Muslim world have been in place longer than that of the life of many nations and empires.

Here, again, frustration was lying in wait for me as some banks declined the transaction on the grounds that AK BARS was a conventional bank, thus showing a surprisingly narrow understanding of the real purpose of Islamic finance and its role in the international arena.

Hulusi Horozoglu, is the Turkish director of Global Islamic Banking at Citi Dubai and a refined professional used to proactively fostering Islamic finance in non-Islamic jurisdictions. He is well-acquainted with Eastern Europe and Central Asia, and is the banker behind some of the



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most important Islamic finance transactions in Turkey. As soon as I talked him through the AK BARS deal in early February 2011, he understood the strategic importance of this syndication for the whole area. He put together a task force sourced from the Dubai, London and Moscow offices that proved quite effective in the coming months. A few weeks later in Istanbul on 1 March, I met Khaled al-Aboodi the CEO and General Manager of the Islamic Corporation for the Development of the Private Sector of the IDB group.

He is another professional with a keen desire to use the funds of the multilateral organization he runs to help kick start Islamic finance around the world. He gave his invaluable support to the project by agreeing to become the other lead manager of the syndication thus adding credibility to the whole proposition.

Andy Warhol, the acclaimed pop art icon of the 1980s, once said that “being good in business is the most fascinating kind of art.” Meaning that the production of income in the real world touches so many aspects of life, strikes the innermost chords of human personality and entails such a variety of social interconnections, that combining them together in a well-balanced and harmonious manner is equivalent to the production of a work of art.

And the unfolding of AK BARS debut Russian syndication certainly proved Warhol right. This transaction would never have happened if so many people from different cultures and coming from diverse walks of life had not contributed, in their respective capacities, to the final output with an acumen and a drive well beyond their professional remit. They were all able to sidestep their own individualities, cross the boundary into the unknown and venture out into new pastures. And they did so only because Islamic finance was perceived as a smart conduit to channel their sincere desire to do the ‘right thing’ and spread the values of sound finance, financial inclusion, social empowerment, sustainable development and wealth redistribution – values which were, in any event, their own.

This small adventure also taught me that Islamic finance is too important to be left to Islamic bankers alone as there is a necessity to access different disciplines and tools that are usually outside the reach of banking. Islamic finance is a thorough proposition that stretches the religious, ethical and societal areas, and very often happens in jurisdictions alien to Islamic law with recurring legal and tax issues.

Hence, there is a need for consultancies that can span different disciplines, are able to encompass the whole picture, think outside the box and use lateral thinking to its utmost. The understanding of the role of capacity building, communication and the implementation of a mutually creative network between all parties is, indeed, critical in putting together a proposal where stakeholders carrying different interests can find value. If this is achieved, then the frustrations, the hurdles, the fatigue and the unexpected skepticism encountered along the way will suddenly melt away and leave only a sense of accomplishment, a sense of having done the ‘right thing’.

Until the next deal...

#### *About the Author*

*Alberto Brugnoli is managing director of ASSAIF. ASSAIF is a unique proposition in the international Islamic finance landscape as it aims to bridge the gap between Islamic and ethical finance. Its associates structure and develop Shariah-compliant products and instruments and offer professional consultancy and training in legal, fiscal, administrative, financial engineering and marketing areas. At the same time ASSAIF is a not-for-profit think tank at the forefront of the research in some key areas, such as the nature of money and the monetary system, accountancy, Islamic social design, takaful and microfinance.*