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Finance & Markets

Global Islamic Finance Center

Global Sukuk Market Trends

Workshop on Developing Sukuk Markets

Arab Monetary Fund

World Bank Group

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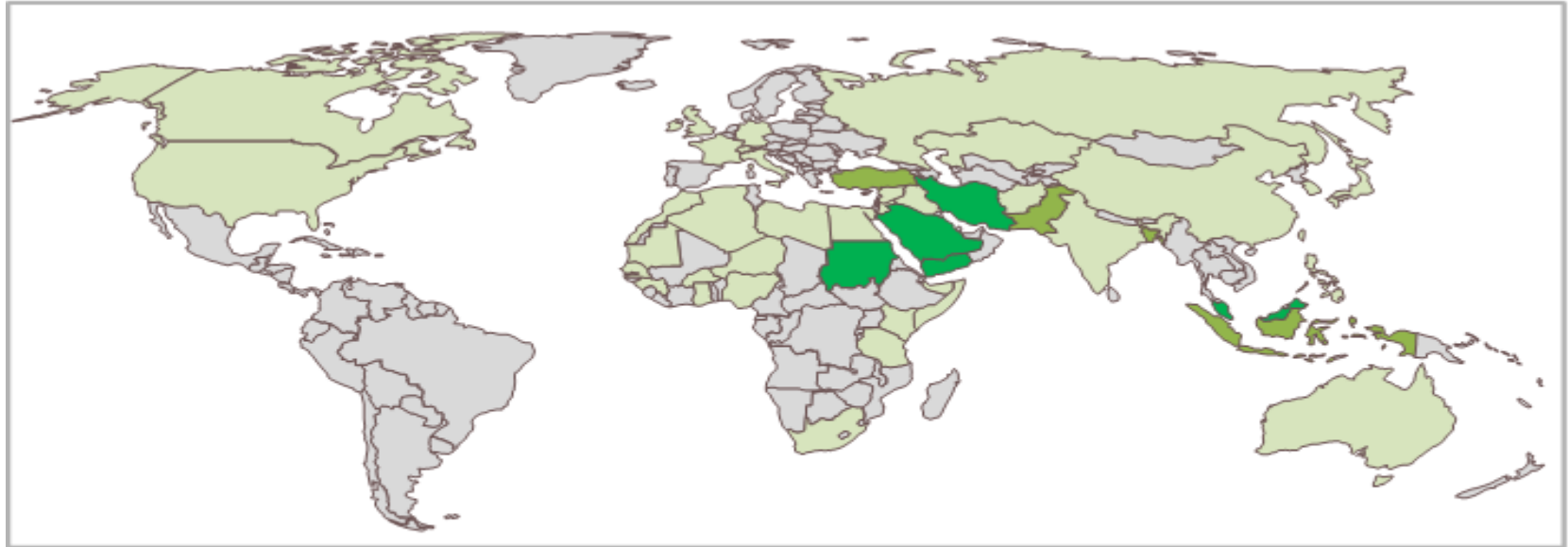
Roadmap

- I. BRIEF OVERVIEW
- II. STYLIZED FACTS & TRENDS ABOUT GLOBAL *SUKUK* MARKET



I. Brief Overview

Globalization of Islamic Finance...



- Systemic Importance
- Potential Systemic Importance in Mid-term Given Current Growth
- Minimal Systemic Importance

Source: IFSB Financial Stability Report 2014, KFHR, IMF

Islamic Finance makes into G-20 agenda

2015- The G20 group of major nations has included discussion of *Sukuk* (Islamic bonds) as an infrastructure financing tool in its annual agenda, a move that could potentially spur the use of project-based *Sukuk*. In addition, Islamic Finance is subject of study under G20 themes of long-term investments and Financial inclusion.

...there is increasing interest in Islamic finance from non-Muslim countries

Recent transactions include sovereign issuance by United Kingdom (UK), South Africa, Hong Kong, and Luxemburg.

UK

- **2010** – The Financial Services and Markets Act 2000 Order 2010 was introduced by Treasury to support Islamic finance and the issuance of corporate *sukuk* within the UK
- **2012** - The UK Government launched an Islamic Finance Task Force with the aim of securing London's status as the Western hub for Islamic finance
- **2013** - London hosted the World Islamic Economic Forum during which the UK Prime Minister announced plans to issue a *Sukuk* in 2014 and to turn London into a global center of Islamic finance.

France

- **2009** - The amendment of Article 2011 of the French Civil Code relating to the formation of trusts was interpreted as an important step towards permitting the issuance of *sukuk* out of France
- **2010** - Revision of specific tax regulations covering *Sukuk*, *ijarah*, *istisna* and *murabaha* with a view to removing discrepancies

Luxembourg

- **2010** - The Luxembourg Tax Authority published a circular to clarify the tax treatment of murabahah and sukuk transactions, to ensure that they benefit from the same tax treatment as conventional products
- **2011** - Luxembourg's CSSF published a note that clarified that no specific legislation was required for Shariah compliant investment funds, since Luxembourg's current law contains no obstacles to it.

Germany

- **2012** - German banking regulator hosted an Islamic finance conference in Frankfurt during which the tax treatment of different Islamic finance products was discussed.

Hong Kong

- **2014**- Hong Kong has raised \$1bn in its debut Islamic bond issue.

South Africa

- **2014**- \$500m sale was more than four times subscribed, with an order book of \$2.2bn according to the SA Treasury

What is *Sukuk* (Islamic Bond)?

- The word *Sukuk* (plural of Arabic word *sakk*, meaning “certificate”) reflects participation rights in the underlying assets.
- *Sukuk* represent proportionate beneficial ownership of an asset for a defined period when the risk and the return associated with cash flows generated by underlying assets in a pool are passed to the *Sukuk* holders (investors).
- Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI) Standard 17 defines Investment *Sukuk* as being:
 - “Certificates of equal value representing after closing subscription, receipt of the value of the certificates and putting it to use as planned, common title to shares and rights in tangible assets, usufructs and services, or equity of a given project or equity of a special investment activity”

Types of *Sukuk*

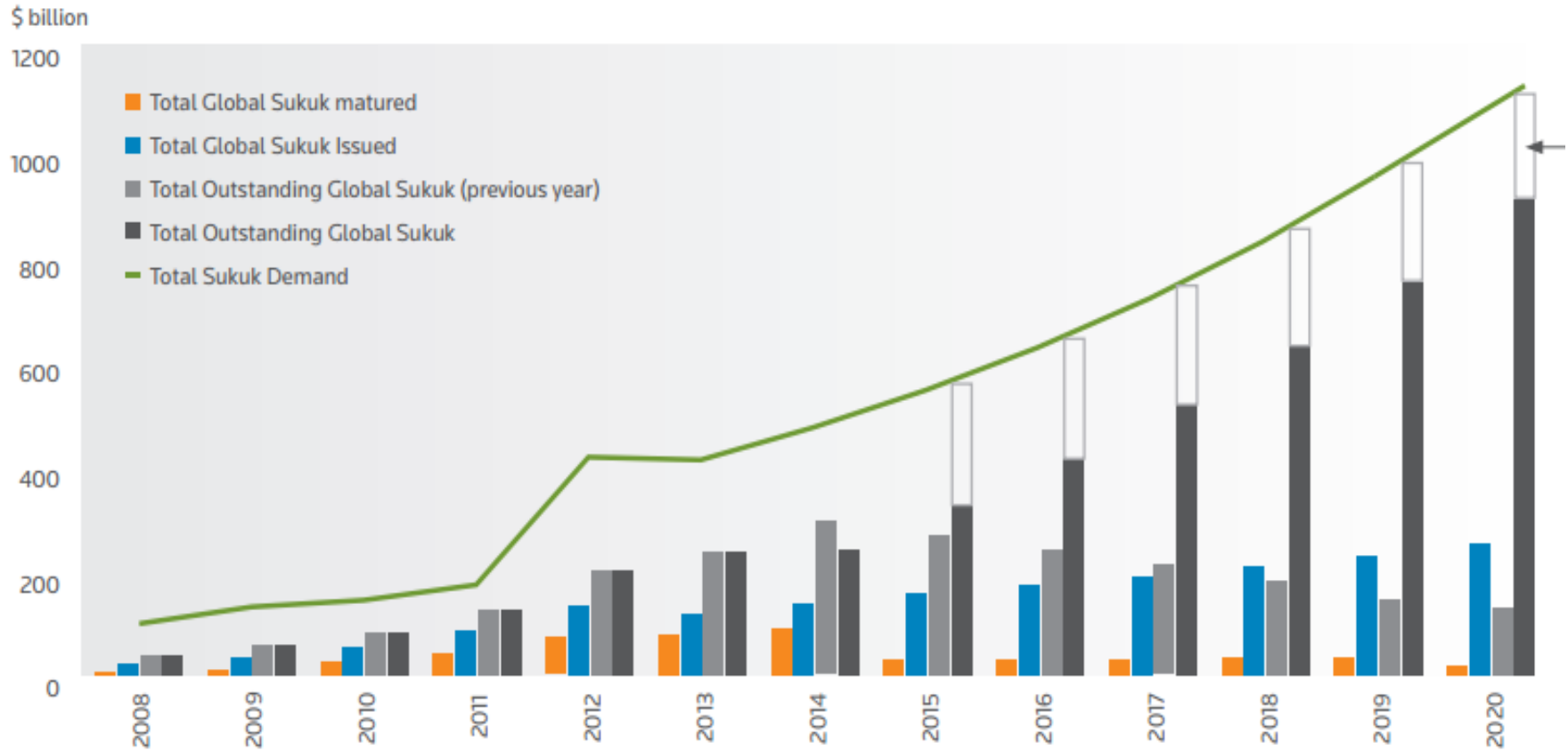
AAOIFI recognizes the following different types of *Sukuk*:

1. Certificates of ownership of leased assets (*Ijarah Sukuk*)
2. Certificates of ownership of right to use; (i) of existing assets, (ii) of described future assets, (iii) of services of specified party, and (iv) of described future services
3. *Salam* Certificates
4. *Istisna'* Certificates
5. *Murabahah* Certificates
6. *Musharakah* Certificates
7. *Mudarabah* Certificates
8. *Muzaraah* (share-cropping) Certificates
9. *Musaqah* (irrigation) Certificates
10. *Mugharasa* (agricultural/seed planting) Certificates

I. Stylized Facts & Trends about Global *Sukuk* Market

Sukuk market is growing fast

SUKUK DEMAND & SUPPLY LEVELS (2014 - 2020)

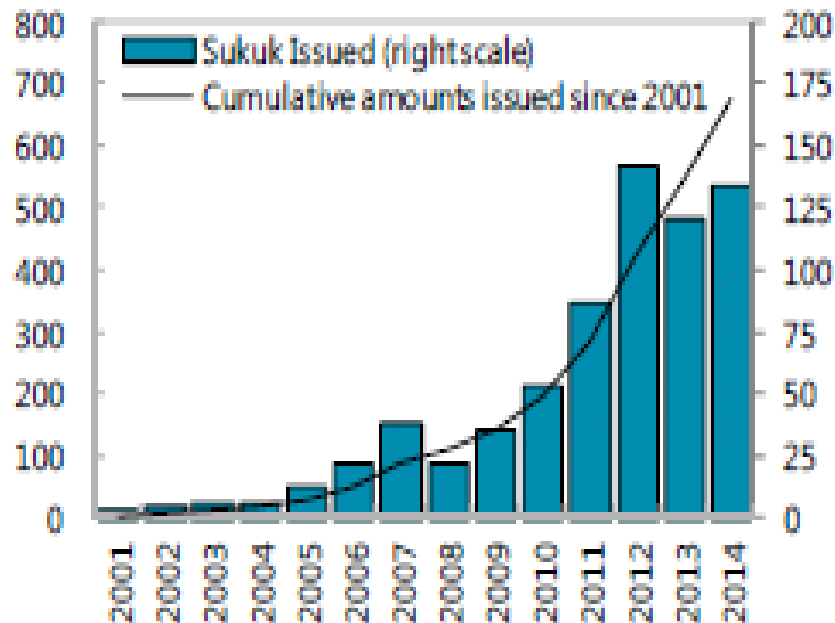


Demand for *sukuk* has been surpassing the level of *sukuk* issuances worldwide.

Sukuk market is growing fast

Global Sukuk Issuance

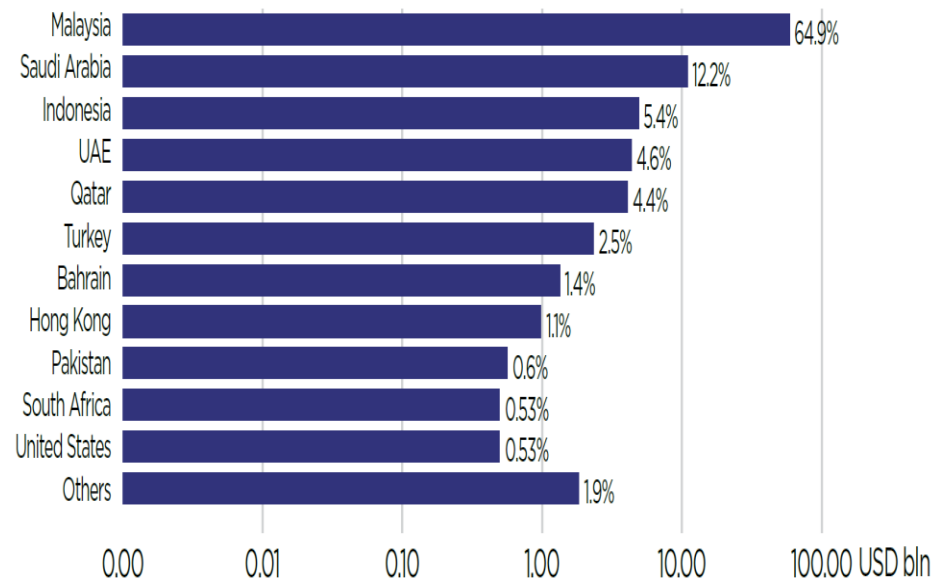
(\$US in billions)



IMF 2015, "Sukuk Capital Markets Surveillance"

Sukuk issuances by domicile in 9M14 YTD - Volumes and Market Share

Source: KFH Research Limited

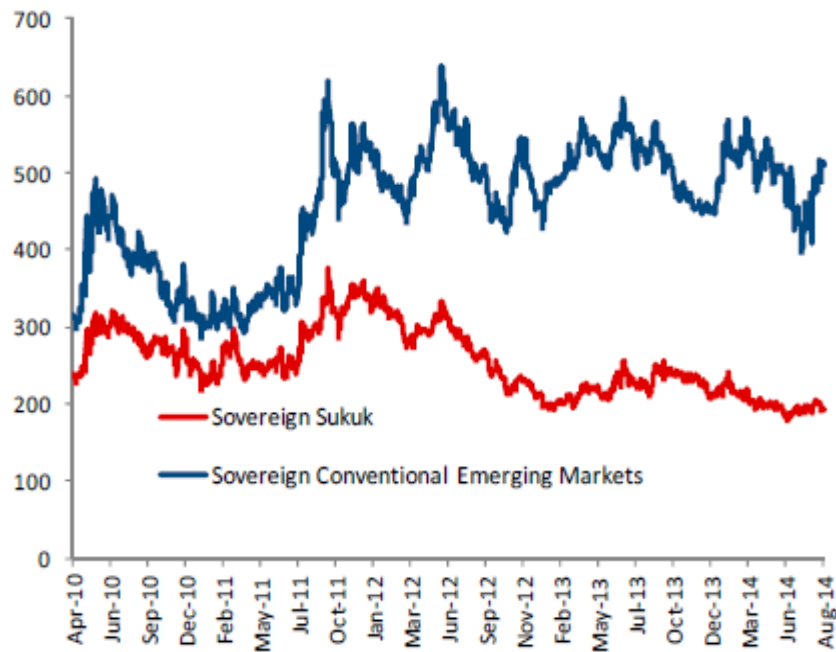


*Numbers in percentage indicate share of total issuances for each domicile (based on obligors' domicile)

Source: "Sukuk Market: Continues to Expand in 3Q14" retrieved from <https://www.mifc.com>

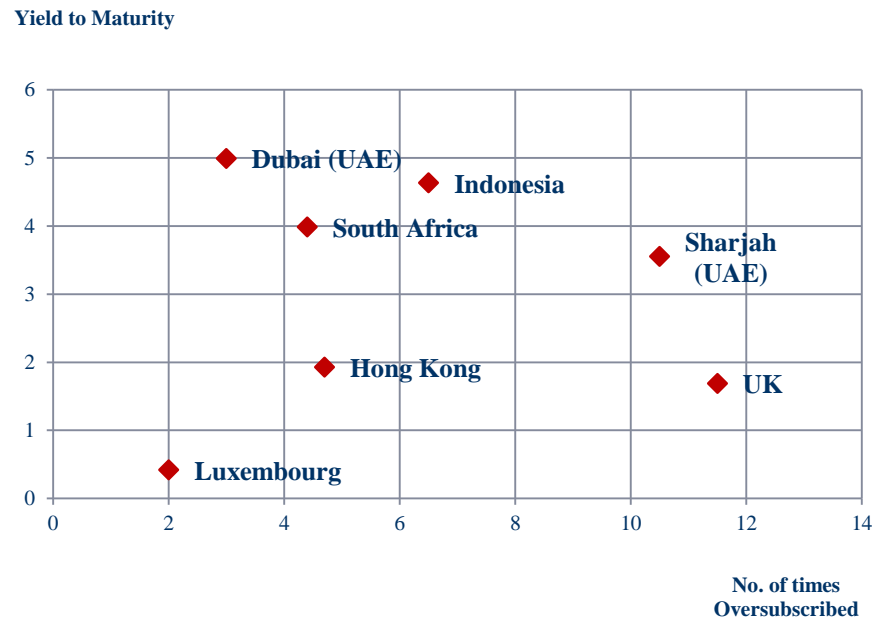
The global *Sukuk* outstanding market reached USD294.69bln as at end-3Q14, a 9.4% expansion YTD from the USD269.4bln as at end-2013 and a 18.2% growth y-o-y since 3Q13.

Sukuk Yields



Strong demand is compressing Sukuk yields...

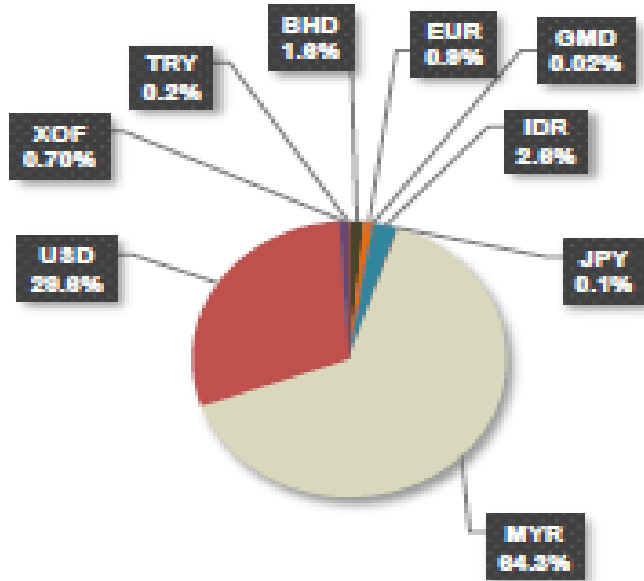
Oversubscriptions Vs. Yields to Maturity
Jan. - Sep. 2014



Source: Bloomberg, accessed September 30th, 2014

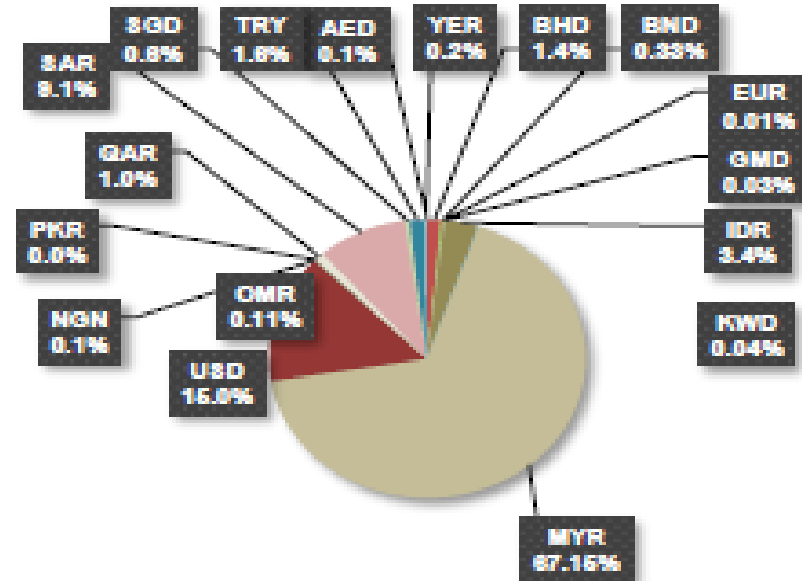
Global *Sukuk* Market by Currency

Sukuk Issuances by Currency (3Q14)



Source: Bloomberg, IFIS, Zawya, KFHR

Sukuk Issuances by Currency (2013)



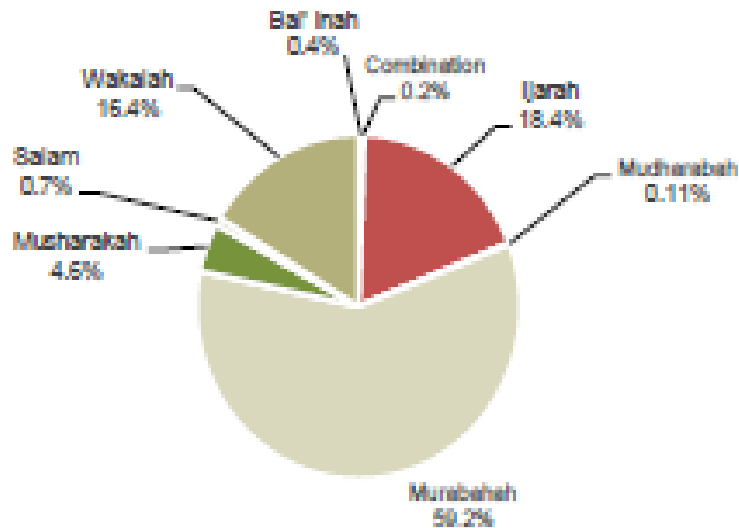
Source: Bloomberg, IFIS, Zawya, KFHR

Source: "Quarterly Global Sukuk October 2014", Rasameel Structured Finance Co.

Sukuk are issued mostly in Malaysian Ringgit (%65) and US Dollar (30%). However, *sukuk* denominated in other currencies are also being issued in recent years.

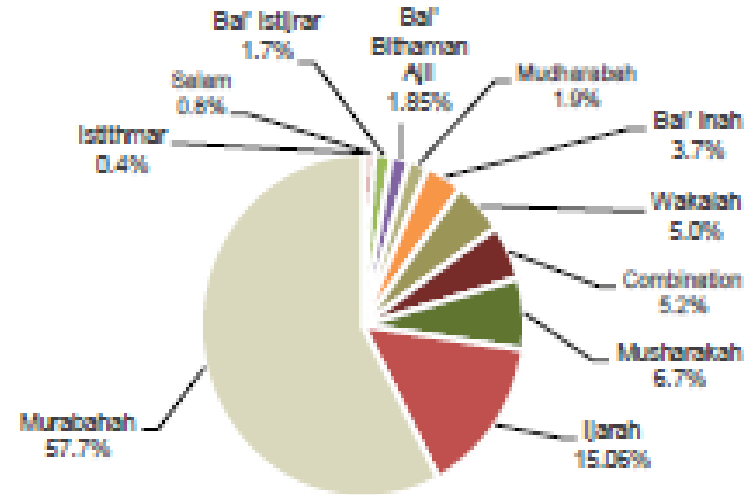
Global *Sukuk* Market by Structure

Sukuk Issuance by Structure (3Q14)



Source: Bloomberg, IFIS, Zawya, KFHR

Sukuk Issuance by Structure (2013)



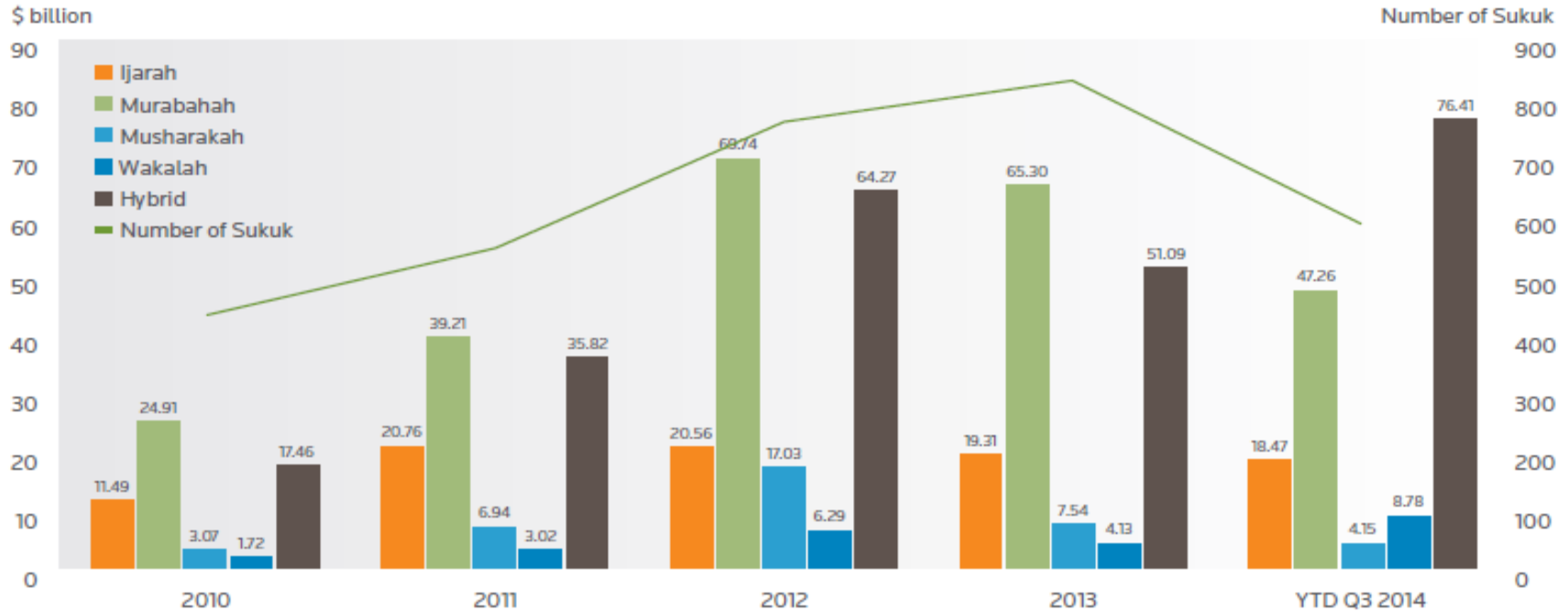
Source: Bloomberg, IFIS, Zawya, KFHR

Source: "Quarterly Global Sukuk October 2014", Rasameel Structured Finance Co.

Murabahah sukuk and *Ijarah sukuk* are the most common forms of *sukuk* structures prevalent in the sector.

Sukuk Issuance by Structure: Time Series

GLOBAL SUKUK HISTORICAL TREND TOP SUKUK STRUCTURES (2008-YTD Q3, 2014)

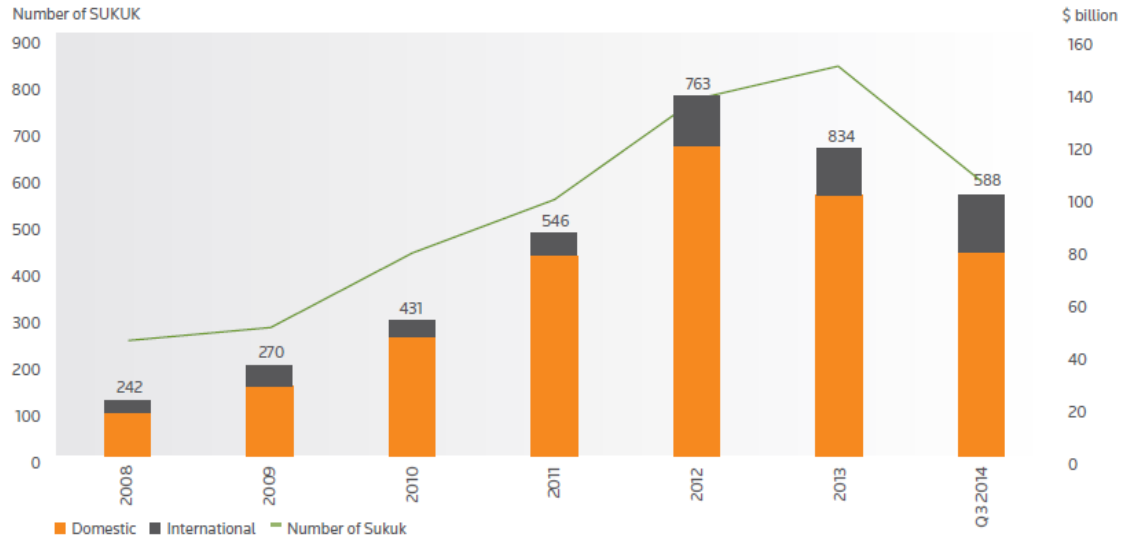


Murabahah type *sukuk* structure, although not allowed to be traded in Middle East countries, is the dominant structure of *sukuk*. However in first 9 months of 2014 hybrid *sukuk* have outpaced *murabahah* *sukuk*.

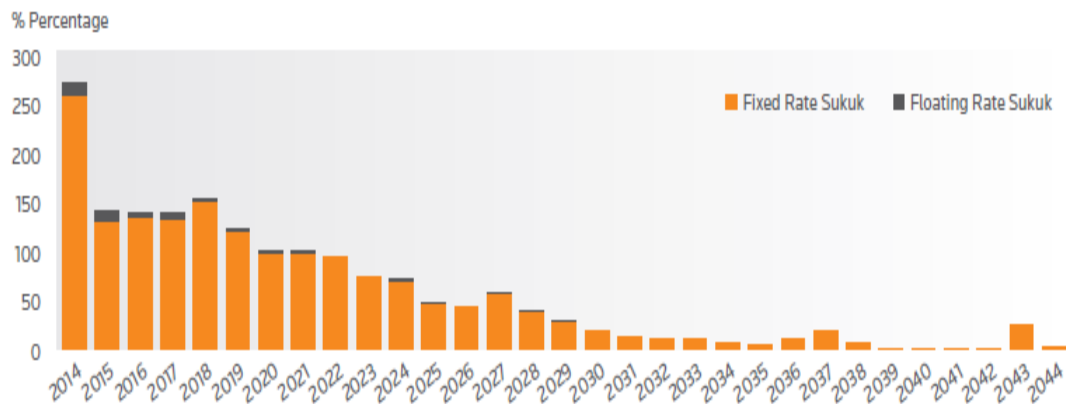
Global *Sukuk* Market: Market of Issuance and Type of Coupon

Domestic markets are dominating mainly due to domestic Malaysian Ringgit issuance.

GLOBAL SUKUK HISTORICAL TREND BREAKDOWN BY MARKET OF ISSUANCE (2008 - Q3, 2014)



GLOBAL OUTSTANDING SUKUK MATURITY PROFILE BREAKDOWN BY TYPE OF COUPON

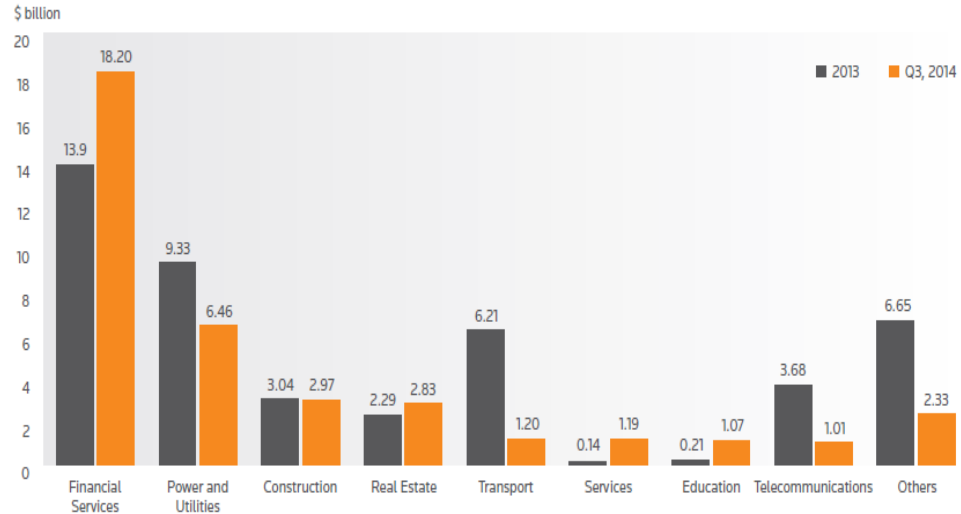


Sukuk offering fixed rate are more widespread than floating rate *sukuk*.

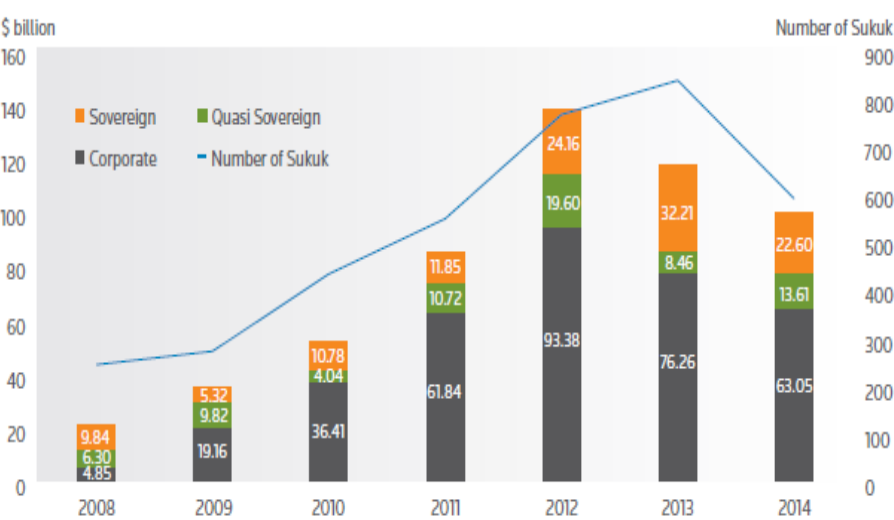
Global Sukuk Issuance by Sector and Issuer Type

The bulk of *sukuk* issuances during first 9 months of 2014 were in Financial Services sector (due to Tier-I *Sukuk*). Four sectors (Financial Services, Real Estate, Services and Education), experienced increased issuances compared to 2013.

GLOBAL CORPORATE SUKUK GROWTH COMPARISON (2013, Q3, 2014)



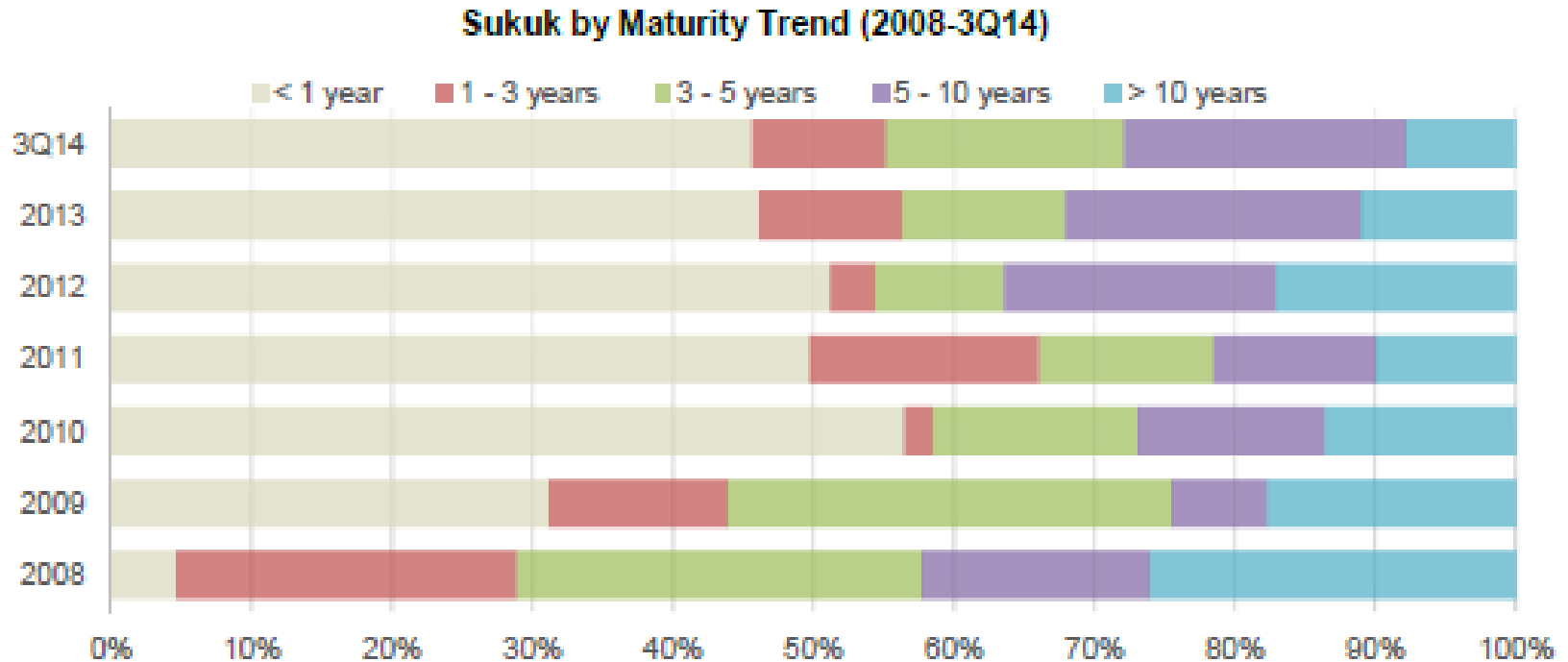
GLOBAL SUKUK HISTORICAL TREND BREAKDOWN BY ISSUER (2008 – YTD Q3, 2014)



In the first 9 months of 2014, total sovereign *sukuk* issuance was \$63.05 billion compared to \$13.61 billion quasi-sovereign and \$22.60 billion corporate issues. In the whole of 2013, total sovereign *sukuk* amounted to \$76.26 billion, and quasi-sovereign and corporates totaled \$8.46 billion and \$32.21 billion, respectively.

Source: "Sukuk Perceptions & Forecast: 2015", Thomson Reuters .

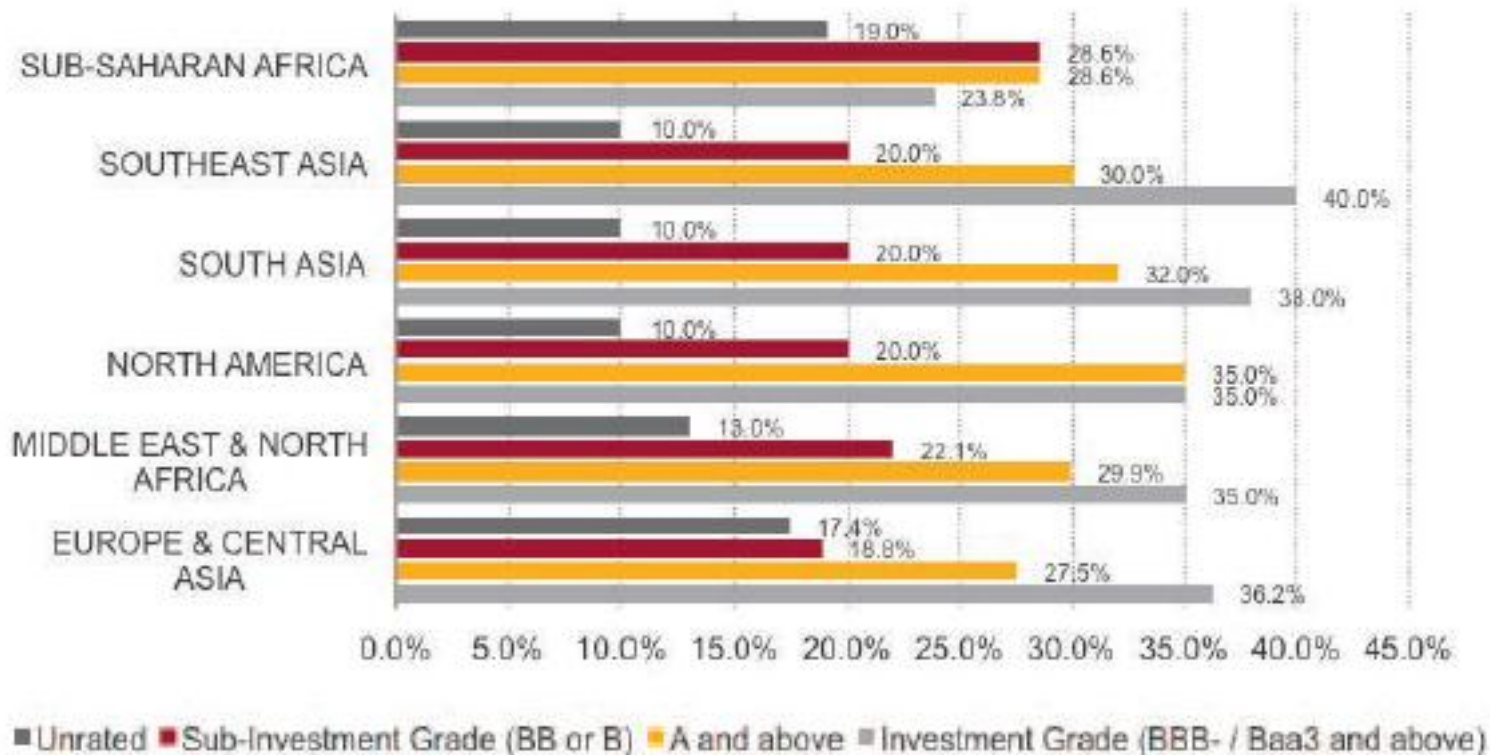
Sukuk by maturity trend



Source: Bloomberg, IFIS, Zawya, KFHR

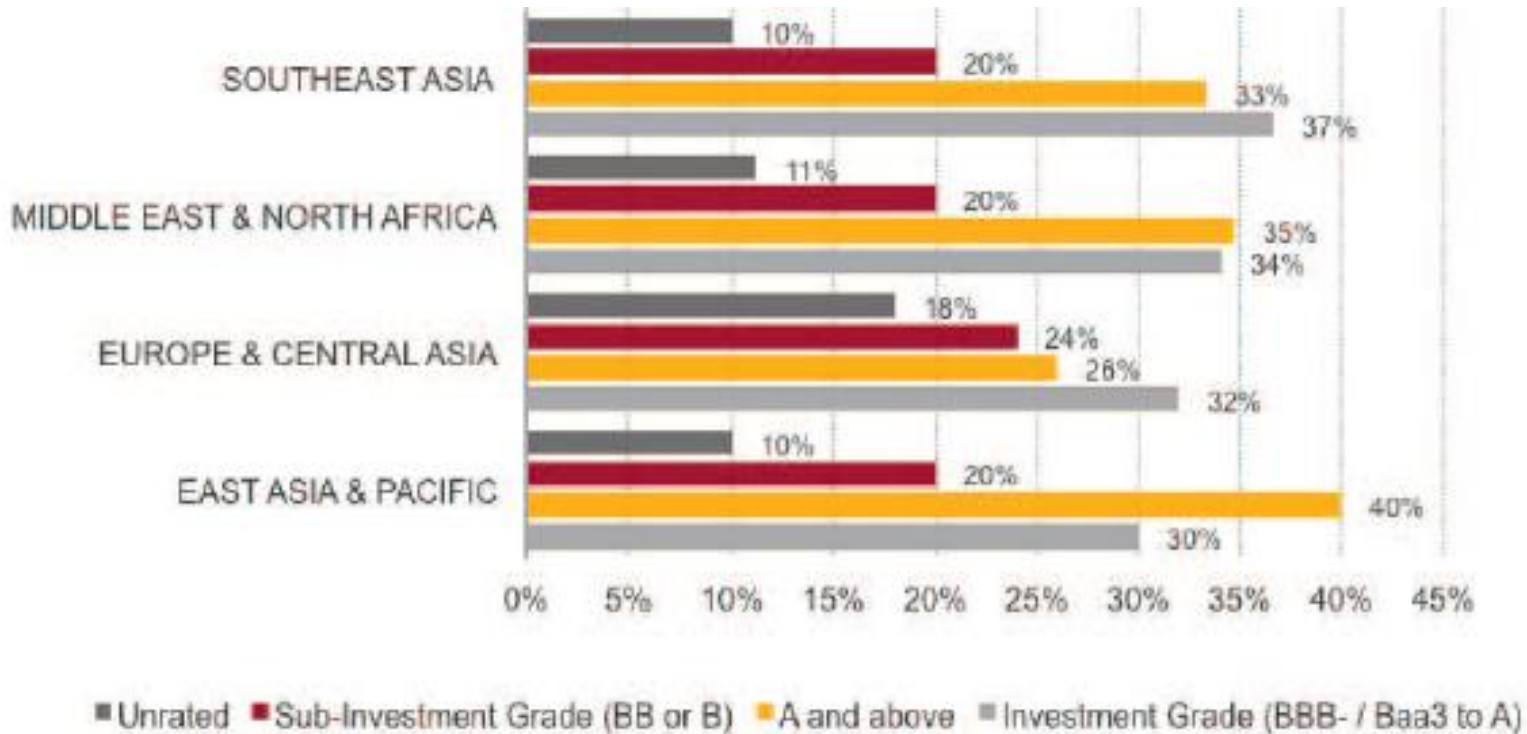
In recent years the *sukuk* market has moved to issuing *sukuk* with shorter maturity. One can argue that investors are reluctant to take long term risks in the *sukuk*. Hence if we are to advance *sukuk* as sound alternative to conventional bonds in long term infrastructure projects better risk management policies should be developed to address the concerns of investors.

Buy Side: Regional Break Down by ratings



From buy side perspective the top rated *sukuk* are concentrated in North America region but other regions are not lagging far behind in this metric.

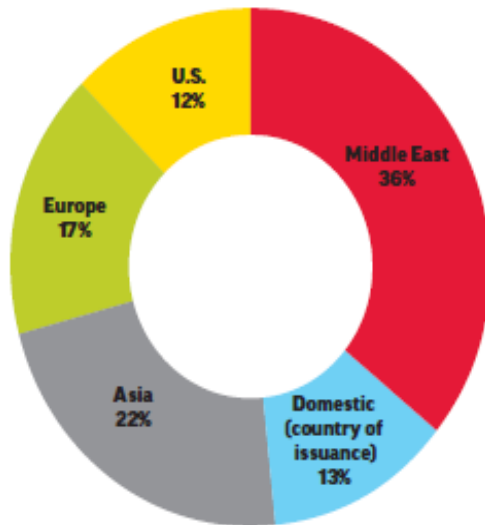
Sell Side: Region Break Down by ratings



From sell side perspective the top rated *sukuk* are concentrated in East and Southeast Asia regions.

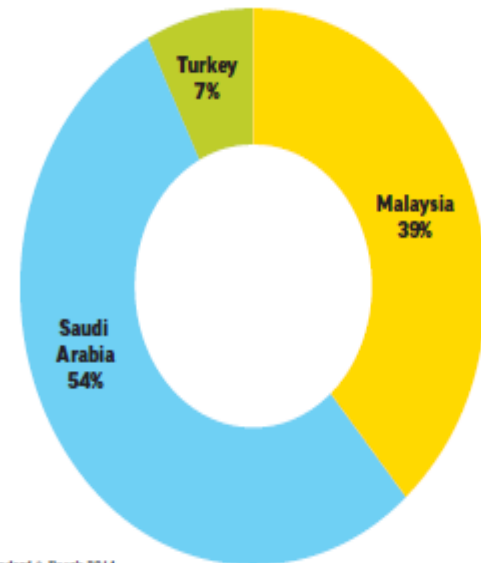
Investors Profile

CHART 3
INVESTOR LOCATIONS WEIGHTED BY INVESTMENT SIZE



© Standard & Poor's 2014.

CHART 2
DISTRIBUTION OF TIER II INSTRUMENTS BY COUNTRY



© Standard & Poor's 2014

Issuers of Tier 2 sukuk claim that they qualify as Additional Tier 1 (AT1) capital under Basel III.

THANK YOU...

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