Nasser Saidi: Economics & Governance

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Islamic Finance is coming of age: IFC lists Sukuk on the DIFC

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On 4 November, 2009 the International Finance Corporation, an affiliate of the World Bank listed an Islamic bond, a Sukuk on the DIFC's international exchange, Nasdaq-Dubai. The IFC Hilal Sukuk is a dollar-denominated $100 million issue, AAA rated, with a five-year maturity. While this is a symbolic amount compared to some of the mega-Sukuk, the Hilal Sukuk offered by the IFC sets a milestone for Islamic Finance and for financial markets in the GCC. It is the first time that a non-Islamic financial institution issues a Sharia compliant security for term funding, a fact all the more important, considering that the IFC, the private sector arm of the World Bank, is a leading multilateral financial institution, founded in 1956, with a strong reputation on international markets and impeccable credentials. By issuing a Sukuk, the IFC and the World Bank have recognised Shari'a compliant finance and securities as bona fide, valid, and acceptable financial instruments.

It is also the first time that a sizeable Sukuk will be listed exclusively in the Gulf, i.e. on Nasdaq Dubai and the Bahrain Stock Exchange, which represents an acknowledgment of the progress made by the emerging financial sector in the region, in terms of liquidity, but more importantly in terms of the trading, clearing & settlement, and the legal and regulatory environment. In fact the contractual terms of this IFC Sukuk are established under DIFC law (based on English common law), which receives, by a leading issuer, an implicit endorsement as a sound framework on par with those of other well-established jurisdictions. Confirming the maturing of our regional market, the Hilal Sukuk was arranged by a regional syndicate including Dubai Islamic Bank, Kuwait Finance House Bahrain, HSBC Amanah and Liquidity Management House. With such a high profile precedent the investment banking community and the legal profession will take notice and rest assured that every aspect has been thoroughly tested and can be duly replicated.

Hence, in practice the IFC Sukuk represents a historic benchmark for all future Shari'a compliant financing operations by sovereign and corporate entities and sets a standard for the whole Islamic finance sector, too often hindered by a lack of standardisation, the absence of uniform rules and structures. The IFC Sukuk listing documents will provide reference documentation for other issuers from the region and internationally, thereby lowering the cost of issuing Sukuk, making them more competitive with conventional debt.
Two additional aspects are noteworthy. First, the Hilal Sukuk will raise funds for IFC infrastructure and health projects in Yemen and Egypt, stressing the ideal suitability of Islamic finance for the financing of tangible, real assets. In a region where the pipeline of infrastructure is estimated at around USD 2 trillion over the next years, the IFC has clearly indicated a direction which others would be persuaded to follow. Second, so far a liquid Sukuk secondary market in the region has struggled to emerge in part because there is a shortage of high quality securities compared to the demand by a host of Islamic institutions (which typically buy and hold most of the supply). The IFC Sukuk, rated AAA and likely to commanded a narrow spread with a profit rate of 3.0379%, highlighting the appetite by investors in the region for an issue which was strongly oversubscribed and is likely to attract the attention of the international financial community. It will provide a benchmark for pricing sovereign and corporate Sukuk, being considered essentially "risk free".

In conclusion the IFC Sukuk has demonstrated that Dubai has the required trading, settlement & custody, physical and legal infrastructure to attract prominent issuers and investors and is ready to accommodate the needs of the Islamic finance community. It is now up to the governments and the large state owned companies to take advantage of this breakthrough and tap the immense pool of wealth owned in the region, but invested in distant locations. Such a course of action would be even more warranted and urgent at a time when the domestic banking system is struggling to extend credit and large international banks, mired in the aftermath of the financial crisis, are focused on regaining their balance and rebuilding their balance sheets. Given the ease with which capital market products transcend geographical borders, Shari'a compliant financing projects which originate in one country can source investors globally. The current infrastructure projects in the MENA and the Asia regions are an unprecedented opportunity to create an Islamic financial market. Infrastructure should be financed through the debt markets and no longer rely on oil & gas revenue. The IFC Sukuk has opened the way to mainstreaming Shari'a compliant finance. Indeed, the time is ripe for action on two broad fronts: the mainstreaming of Islamic financial services and products, and the integration of Shari'a compliant securities into international markets, to become an internationally recognised asset class. The egalitarian nature of Islamic finance, investment disclosure, corporate governance and risk-sharing characteristics are an antidote to the uncertainties generated by the ongoing global financial crisis. Islamic finance has come of age and is a viable and credible alternative to conventional financing. DIFC's strategy and policy measures have succeeded in creating the enabling environment for the establishment of a sound, well-functioning Islamic financial system and achieve banking and financial deepening. Islamic finance is coming of age and is now part of the international financial architecture of markets and products.

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