Market Analysis

Following last year’s success, 2015 poses several challenges and opportunities for the Islamic financial industry. One potential challenge is the market response to the rapid deterioration in the price of oil, likely tightening of US Fed monetary policy and the development of innovative financial products to meet excess liquidity in the market. The rapid decline in the price of oil threatens to decrease the liquidity in Gulf countries as revenues from petrodollars fall. This decrease in liquidity could have adverse effects on sukuk issuances. On the other hand, the decline in oil revenues might result in higher budget deficits in Gulf countries which rely heavily on oil revenues to finance government spending. Higher budget deficits might force the countries to issue more sukuk to finance their budget deficits. In addition, the increasing interest from international financial markets in issuing sukuk might improve the liquidity of sukuk markets. Recently Barclays bank announced that Malaysian sukuk were to be included in its global fixed income index. Furthermore, Pemex, Mexico’s national oil company is considering raising funds through its sukuk while the Russian central bank is showing interest in the sukuk market to overcome the liquidity shortages following Western sanctions. In terms of developments in Islamic capital markets, the Saudi Stock Exchange (Tadawal) has announced it is opening up to international investors. This new development might give further support for the development of international Islamic capital markets as Saudi Arabia has the largest and most liquid stock exchange in the Region.

In addition, harmonization of standards and development of innovative financial products is highly desirable for Islamic finance to grow further. Moving from a reliance on sale-based financing like Murabahah as the preferred financing instrument to more risk shared financing is a major hurdle for Islamic banks to overcome. In this respect, the Malaysian government’s initiative to establish an Investment Account Platform is a major step in encouraging Islamic financial intermediaries to move away from debt-based contracts to equity-based products. Finally, there is more realization of the tendency of Islamic financial intermediaries to give less priority to social welfare as opposed to the principles of Islamic Finance. From this standpoint, the recent remarks by central bank governors suggest that the challenges facing Islamic banks should find ways to reward their customers according to high profit rates in the banking system and efforts to enhance the importance of microfinance in alleviating poverty among Muslim societies are important developments.

World Bank Global Islamic Finance Development Center’s Inaugural Symposium to be held on September 8-9th, 2015 in Istanbul with the theme of “Islamic Finance: A Catalyst for Shared Prosperity?”

The inaugural Symposium is a 2-day event and will be held in Istanbul. The theme of the symposium is “Islamic Finance: A catalyst for Shared Prosperity?” The papers presented at the symposium will be published in an edited book. The organizers have the full rights to publish the papers.

Submission of extended abstract March 15, 2015
Acceptance of abstracts March 31, 2015
Full Paper Deadline 15 July 2015
Acceptance Notification 30 July 2015

For more information please visit: http://submit.confbay.com/conf/idbwbs2015

World Bank publication entitled “Economic Development and Islamic Finance” has been translated into Turkish

A World Bank publication entitled “Economic Development and Islamic Finance” has been translated into Turkish in a collaborative effort of the World Bank, Borsa Istanbul and INCEIF. Although Islamic finance is one of the fastest growing segments of emerging global financial markets, it is often stated that the market is far below its true potential. At the same time, the concepts of Islamic finance are not fully explained and exploited, especially in the areas of economic development, inclusion, access to finance, and public policy. This volume attempts to highlight some of the key features of Islamic finance relevant to economic development. The objective of the volume is to improve understanding of the perspective of Islamic finance on economic development, social and economic justice, human welfare, and economic growth. We hope that the translation of “Economic Development and Islamic Finance” is going to pave way for future research in this field.
Barclays has given a boost to the fast-growing market for sharia-compliant bonds by including emerging market local currency sukuk in its indices for the first time. A total of 36 Malaysian ringgit-denominated sukuk, with a combined par value of Rm264bn ($73bn), issued by the Malaysian government, will be added to Barclays indices as of March 31. The move, which is expected to trigger inflows of $2.5bn to $3bn into the bonds, will virtually double Malaysia’s weighting in Barclays’ Global Aggregate and Emerging Market Local Currency Government indices to 0.38 per cent and 8.7 per cent respectively. Jan Dehn, head of research at Ashmore Investment Management, an emerging markets house, said the move was an important precedent. “This is very good news. Sukuk have been a fast growth area for external bond issuance in emerging markets,” said Mr Dehn. “The most commonly used external debt benchmark index, the EMBI Global Diversified index from JPMorgan, does not include sukuk. This is one of the reasons why this index only captures about 47 per cent of the emerging market external debt universe.”

The International Finance Facility for Immunisation Co. (IFFI), for which the World Bank acts as treasury manager, has launched a $500 million Islamic bond issue. The International Finance Facility for Immunisation Co. (IFFI), for which the World Bank acts as treasury manager, has launched a $500 million Islamic bond issue.

The three-year sharia-compliant floating rate note has been priced at 15 basis points over the three-month London interbank offered rate, the document showed. This compares with a range of 15 to 17 basis points over three-month Libor in pricing details issued on Wednesday.

Three trends in the global financial market are converging to make sukuk, the Islamic financial instrument most similar to a conventional bond, a potentially viable form of finance for green investments: (1) banks are reluctant to finance infrastructure due to stricter capital requirements; (2) an increasing number of investors are interested in ‘environmentally sustainable investing’ (in other words, investing to promote activities seen as positive for the environment); and (3) the market for sukuk is growing significantly. While these three trends are distinct and not obviously related, taken together, they create a market opportunity for sukuk to be used as a tool to finance environmentally sustainable infrastructure projects.

Barclays has given a boost to the fast-growing market for sharia-compliant bonds by including emerging market local currency sukuk in its indices for the first time. A total of 36 Malaysian ringgit-denominated sukuk, with a combined par value of Rm264bn ($73bn), issued by the Malaysian government, will be added to Barclays indices as of March 31. The move, which is expected to trigger inflows of $2.5bn to $3bn into the bonds, will virtually double Malaysia’s weighting in Barclays’ Global Aggregate and Emerging Market Local Currency Government indices to 0.38 per cent and 8.7 per cent respectively. Jan Dehn, head of research at Ashmore Investment Management, an emerging markets house, said the move was an important precedent. “This is very good news. Sukuk have been a fast growth area for external bond issuance in emerging markets,” said Mr Dehn. “The most commonly used external debt benchmark index, the EMBI Global Diversified index from JPMorgan, does not include sukuk. This is one of the reasons why this index only captures about 47 per cent of the emerging market external debt universe.” The Bank for International Settlements, which in September warned of the dangers of “herd behaviour” in emerging markets, cited the problem of “clustering” by western investors in the securities covered by major indices. Broadening the scope of these indices would help ameliorate this problem.
**Islamic Finance Bulletin**

**AAOIFI Standards go digital with Thomson Reuters**

In an unprecedented move in the development of the Islamic finance industry, the Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI) standards will be made available online through Thomson Reuters’ range of digital information platforms, including Zawya Islamic.

AAOIFI Shari’a standards are approved and developed under the guidance of its Shari’a Board, which comprises the world’s leading Shari’a scholars on Islamic finance and internationally regarded as the ultimate authority on Shari’a for Islamic finance. The standards on accounting, auditing, ethics and governance are approved and developed by AAOIFI Accounting and Auditing Standards Board comprising senior representatives from major Islamic financial institutions, central banks and regulatory authorities, and international accounting and auditing firms. The standards represent the broadest consensus of rules that govern the Islamic finance industry and cover Shari’a, accounting, auditing, governance and ethics.


**Mexico eyes sovereign sukuk**

Mexico is considering issuing an inaugural sukuk bond, an official in the ministry of finance has told Euromoney. Pemex may follow. The deal, which would be a regional first, would further enhance Mexico’s reputation as the region’s most innovative sovereign issuer. Pemex, Mexico’s national oil company, also confirmed interest in a sukuk, although it is believed the company will probably wait for the sovereign to open the market first.

However, international DCM bankers say that a Mexican foray into this market would fit the sovereign’s debt strategy, which is to open new markets and aggressively diversify funding sources.

http://www.euromoney.com/Article/3394391/Mexico-eyes-sovereign-sukuk.html

**Japan’s FSA explores opening market to Islamic finance**

Japan’s Financial Services Agency (FSA) is considering relaxing rules to allow banks to provide Islamic financial products in its domestic market for the first time.

The financial regulator said in a statement on its website it was asking for public comments until March 27 and would present results of the consultation a month afterwards.

Japanese lenders are already allowed to provide Islamic financial products through their overseas subsidiaries, and Bank of Tokyo-Mitsubishi UFJ (BTMU) recently became the first Japanese commercial bank to issue Islamic bonds, or sukuk.

Non-Muslim countries like Luxembourg, Britain and South Africa also issued sukuk last year as the structure gains acceptance beyond its core markets of the Middle East and Southeast Asia, making it more useful as a funding tool.

A move to allow sukuk and similar products to be bought and sold in Japan, Asia’s largest bond market, would give the sector a further boost.

http://www.reuters.com/article/2015/02/26/islam-financing-japan-idUSL5N0W3Z420150226


**Russian Banks Warm to Shariah as Crisis Looms**

Russian lenders would like to tap Islamic finance just as international sanctions and a low oil price brings their country to the brink of a recession. The Vnesheconombank is currently seeking advice from Middle East lenders on how to sell Islamic bonds. Banks and companies are seeking Shariah financing after the Russian currency recently weakened to an all-time low.

Adopting Islamic finance would mark a sea change for the predominantly Russian Orthodox nation. Alexei Ulyukayev, who was first deputy chairman of the central bank until last year and is currently economy minister, said in 2011 the industry isn’t of “primary, secondary or even tertiary importance,” Gazeta.ru reported.

The central bank is now considering legislature for Islamic finance following requests from lenders, Governor Elvira Nabiullina said on Nov. 26.

"Due to Sharia Law restrictions, Islamic financial products do not follow traditional financial models; however, it was interesting to note that with Hong Kong's first USD1 billion sukuk issuance, two-thirds of the investors came from outside the Muslim world."


**Fitch affirms 11 Saudi Arabian banks**

Fitch Ratings has affirmed 11 Saudi Arabian banks as part of a peer review of the Saudi banking sector. Fitch has also affirmed and withdrawn SAMBA Financial Group’s (SAMBA) EMTN Program rating. The program no longer exists and there is no outstanding issuance.

The affirmation of the banks’ Support Ratings and Support Rating Floors reflects the extremely high probability of support available from the Saudi authorities if required. Fitch’s opinion of support is based on the strong ability and willingness of the authorities to support the banking sector.

Support has been demonstrated by the Saudi authorities’ long track record of supporting domestic banks, as well as close ties and ownership links with the government at a number of banks. Fitch’s view of support is also underpinned by the sovereign’s strong capacity to support the banking system, underpinned by its sovereign wealth funds and ongoing revenues mostly from its hydrocarbon production, and the moderate size of the Saudi Arabian banking sector in relation to the country’s GDP.
Bahrain sukuk battered amid oil drop

Tumbling oil prices are battering Bahrain’s Shariah-compliant bonds. The Gulf nation’s dollar-denominated sukuk that mature in 2018 have dropped 1.3% since the end of September, compared with an average 0.8% gain for more than 30 Islamic sovereign dollar bonds tracked by Bloomberg. Only the five-year $1bn sukuk issued by Pakistan have performed worse.

The decline underscores how oil’s 45% slide since last year is hurting a country where Standard & Poor’s estimates crude accounts for 65% of fiscal revenue and yet has oil reserves that are less than 0.1% of neighbouring Saudi Arabia’s. The retreat threatens to jeopardise some of the $30bn of infrastructure projects the government is planning to sustain economic growth, according to Commerzbank.

Bahrain requires an average oil price of about $120 a barrel to balance its budget, according to S&P. The smallest crude oil producer in the Gulf, Bahrain witnessed some unrest in the region amid turmoil triggered by revolutions in Tunisia and Egypt.


Kenya to issue its debut sukuk next financial year

Kenya will issue its debut sukuk in the next financial year, not this one as some had expected, after it option to borrow an additional $750 million from its maiden $2 billion Eurobond issued in June, its finance minister said on Monday.

Parliament is set to consider a recommendation by its finance committee to double the government’s external debt ceiling to $28 billion to fund the construction of a new railway, port, roads and power plants.

There were expectations in the market the government would issue a bond compliant with Islamic law or shariah this financial year, partly to reduce domestic borrowing and lower interest rates.

Henry Rotich, the cabinet secretary for the Treasury, told Reuters on phone, without indicating the potential size of the bond. He said it would be issued in the financial year in the financial year ending June 2016.

http://af.reuters.com/article/investingNews/idAFKCN0JF1L820141201

Indonesia Pushes Ahead With $8 Billion Shariah Megabank

Indonesian authorities are pushing ahead with a plan to create an $8 billion Islamic megabank, even after a similar proposal fell through in Malaysia. A potential merger of the shariah-compliant units of government-controlled Bank Mandiri, Bank Rakyat Indonesia and Bank Negara Indonesia could happen as soon as this year, Financial Services Authority (OJK) chairman Muliaman Hadad said. Talks are ongoing with the State-Owned Enterprises Ministry, which first proposed the merger in May 2013. The megabank could help drive a quadrupling in Islamic banks’ market share to 20 percent by 2018, compared with 10 percent without it, the Indonesia Islamic Banking Association predicts. That would approach the 21 percent level in Malaysia, where a planned combination of CIMB, RHB Capital and Malaysia Building Society was called off last month as oil prices damped the economic outlook. “If the shariah banking sector is left to evolve and progress on a purely organic basis, it may experience a long-drawn process with a marginal growth rate,” Alhami Abdan, head of international finance and capital markets at OCBC Al-Amin Bank, said last Thursday in Kuala Lumpur.

Malaysia's $40 billion sovereign wealth fund Khazanah Nasional plans to issue a sukuk worth up to one billion ringgit ($279.17 million) to help fund schools, its managing director said on Thursday.

Speaking to Reuters on the sidelines of an Islamic finance event in London, the fund's head Azman Mokhtar said the planned "social impact sukuk" is awaiting regulatory approval from Malaysian financial regulators.

The move is aimed at opening funding for education to a broad pool of investors rather than financing it out of its own reserves, he added.

http://www.reuters.com/article/2015/02/26/sovereign-wealth-malaysia-idUSL5N0W06KH20150226

Bahrain looks for regional edge with central sharia board

Bahrain's central bank is drafting legal documentation to set up a sharia board of scholars that would oversee the kingdom's Islamic finance sector, in a step that could help the market compete with regional rivals. The central bank already has a sharia board but its scope is limited to vetting its own products. A country-level approach - which is so far rare in the Gulf - could help to limit differences between products, speed the design of new products and boost investor confidence. A "legal instrument" is now being prepared that would set out details of the sharia board, Khalid Hamad, the central bank's executive director of banking supervision, told Reuters. He did not specify a timeframe. Oman’s central bank set up a sharia supervisory board last October but unlike Oman, Bahrain has positioned itself as a regional financial centre, with historical links to Saudi and Kuwaiti financial institutions, a status that in recent years has seen growing competition from Dubai and Doha.

https://www.zawya.com/story/Bahrain_looks_for Regional_edge_with_central_sharia_board-TR20150204ln6N0VE048X2/

Indonesia plans Islamic repo rules, separate deposit insurance

Indonesia's central bank plans to introduce rules for Islamic repurchase agreements, allowing lenders to use a wide range of sovereign and corporate assets to manage their liquidity, deputy governor Halim Alamsyah told Reuters.

Efforts to develop substitutes for conventional repos are increasing across Islamic finance, as the industry looks to plug a hole in the financial tools available to Islamic banks so they can cope better during times of market stress.

Conventional repos allow institutions to lend out assets for short periods to generate liquidity. But this is problematic in Islamic finance as it entails charging interest. The central bank already has in place repurchase facilities for Islamic money market instruments, but the new rules would allow Islamic banks to make better use of their longer tenor fixed income portfolios.

"This will relate not only to local currency, but also foreign currency backed by sovereign sukuk, corporate sukuk and supranational sukuk," Bank Indonesia's Alamsyah said on the sidelines of an industry conference in Bahrain.

He declined to give a specific timeframe for when the regulations would be in place, adding that other Islamic financial instruments were also being developed.

Separately, the Indonesian Deposit Insurance Corporation or Lembaga Penjamin Simpaman (LPS) plans to create a separate scheme to guarantee Islamic bank deposits, LPS chairman Heru Budiargo told Reuters.

Work will start next year on the procedures with the separation of funds to take place in 2016, Budiargo said.

The lack of Islamic deposit insurance has been a longstanding problem in the industry, which is set to aggravate due to incoming requirements from Basel III regulatory standards.

For bank deposits to be deemed stable under Basel III, they need to be protected by an insurance scheme. Currently, LPS guarantees all bank deposits under a single fund.

Analysts believe creating a separate fund to cover Islamic deposits would also improve customer perception of the industry.

http://www.reuters.com/article/2014/12/03/indonesiaislam-banks-idUSL3N0TN2FD20141203
<table>
<thead>
<tr>
<th>Name</th>
<th>Location</th>
<th>Date</th>
</tr>
</thead>
<tbody>
<tr>
<td>Islamic Finance: What the Future Holds</td>
<td>London, United Kingdom</td>
<td>06 Mar</td>
</tr>
<tr>
<td>Global Forum on Islamic Finance (GFIF) 2015</td>
<td>Pakistan, Lahore</td>
<td>10-11 Mar</td>
</tr>
<tr>
<td>The World Takaful Conference (WTC 2015)</td>
<td>UAE, Dubai</td>
<td>13-14 Apr</td>
</tr>
<tr>
<td>12th Islamic Financial Services Board (IFSB) Summit</td>
<td>Kazakhstan, Almaty</td>
<td>19-21 May</td>
</tr>
<tr>
<td><a href="http://www.ifsb.org/event_detail.php?e_id=244">http://www.ifsb.org/event_detail.php?e_id=244</a></td>
<td></td>
<td></td>
</tr>
<tr>
<td>IFSB-FIS Workshop Series (Turkey)</td>
<td>Turkey, Istanbul</td>
<td>25-26 May</td>
</tr>
<tr>
<td>IFN Asia Forum 2015</td>
<td>Malaysia, Kuala Lumpur</td>
<td>25-26 May</td>
</tr>
</tbody>
</table>
Dow Jones Sukuk Index: The Dow Jones Sukuk Index is designed to measure the performance of global Islamic fixed-income securities—also known as sukuk. The index includes U.S. dollar-denominated investment-grade sukuk issued in the global market that have been screened for Shari‘ah compliance according to the index methodology. The index was created as a benchmark for investors seeking exposure to Shari‘ah-compliant fixed-income investments. The Dow Jones Sukuk Index follows the same consistent, quantitative methodology as the Dow Jones Islamic Market™ (DJIM) Indices, which are monitored to ensure their continued adherence to Shari‘ah principles.

Bloomberg USD Emerging Market Composite Bond Index: The Bloomberg USD Emerging Market Composite Bond Index is a rules-based, market-value weighted index engineered to measure emerging market debt. The index includes U.S. dollar-denominated investment-grade bonds issued in the global market that have been screened for Shari‘ah compliance according to the index methodology. The index is constructed to provide a benchmark for investors seeking exposure to Shari‘ah-compliant emerging market debt.

LIBOR USD 6 Month: London - Interbank Offered Rate - ICE Benchmark Administration Fixing for US Dollar. The fixing is conducted each day at 11am & released at 11:45am (London time). The rate is an average derived from the quotations provided by the banks determined by the ICE Benchmark Administration. The top and bottom quartile is eliminated and an average of the remaining quotations calculated to arrive at fixing. The fixing is rounded up to 5 decimal places where the sixth digit is five or more.

Dow Jones Islamic Market World Index: The Dow Jones Islamic Market World Index is a global index of companies that meet Islamic investment guidelines. The index is quoted in USD.

Dow Jones Global Index: The index measures the performance of stocks that trade globally, targeting 95% coverage of markets open to foreign investment. It is float market cap weighted. It is quoted in USD.

MSCI World Islamic Index: The MSCI World Islamic Index is a free-float weighted equity index. It was developed with a base value of 1000 as of May 31, 2007.

MSCI World Index: The MSCI World Index is a free-float weighted equity index. It was developed with a base value of 100 as of December 31, 1969. MXWO includes developed world markets, and does not include emerging markets.

MSCI Emerging Markets Index: The MSCI Em (Emerging Markets) Index is a free-float weighted equity index. BLOOMBERG Takaful Index: Bloomberg Takaful Index is a capitalization-weighted index of all globally listed Takaful-recognised companies. Takaful is an Islamic term meaning mutual support, which is the basis of the concept of insurance or solidarity among Muslims. This is a form of insurance based on mutual assistance. The index was developed with a base level of 100 as of April 15, 2009.

Murabaha Deposit Rates: Murabaha Deposit An agreement that refers to the sale and purchase transaction for the financing of an asset or project whereby the costs and profit margin (mark-up) are made known and agreed by all parties involved. The settlement for the purchase, which can be done in cash or in installments, will be specified in the agreement. Use all prices available in the terminal and updated within the last three working days. Banks that do not price for

Glossary Of Key Terms

Sukuk
An Islamic financial certificate, similar to a bond in Western finance, that complies with Sharia, Islamic religious law. Because the traditional Western interest paying bond structure is not permissible, the issuer of a sukuk sells an investor group the certificate, who then rents it back to the issuer for a predetermined rental fee. The issuer also makes a contractual promise to buy back the bonds at a future date at par value.

Sharia Board
An independent body set up by an Islamic bank with the mandate of ensuring that the Islamic bank achieves and maintains compliance with Sharia.

Takaful
The term ‘takaful’ is derived from an Arabic word which means solidarity, whereby a group of participants agree among themselves to support one another jointly against a defined loss. In a takaful arrangement, the participants contribute a sum of money as wholly or partially taburru’ (donation) into a common fund, which will be used for mutual assistance for the members against a defined loss or damage, according to the terms and conditions of the takaful.

Murabaha
A sale contract whereby the institution offering Islamic financial services sells to a customer a specific kind of asset that is already in its possession, whereby the selling price is the sum of the original price and an agreed profit margin.

Contact Info:
Phone: +90 212-385-3442
E-mail: rmutlu@worldbank.org