Islamic Treasury Application (IPD 04)

Course Synopsis:

Objective: To examine the key Islamic instruments utilized in treasury operations and explain *Sharia'a* limitations on these instruments

This course main focus areas are deposit instruments used to manage liquidity in the Islamic money market activities and Islamic equivalent to forward contract in forex operations. It seeks to describe the key Islamic instruments utilized in treasury operations and explain Sharia'a limitations on these instruments.

This module is suitable for: Treasury team members, audit, Sharia'a and sales team members selling treasury products.

Chapter 1: Key Concepts applied in the Islamic Treasury. In our first session, we review the prohibition of riba. We will focus on riba al fadl and its implications for forward foreign exchange transactions. We also examine how contracts, promises, and the rules of possession affect the money markets and FX practices? Then, we review the Islamic contract forms and how these shift our practice from a Money Market to an Asset Market.

Chapter 2: The Islamic "Money Market" Part 1: In this session we start with common liquidity management issues and look at differences in regional business practices. We then examine simple murabaha and musawama "placements" through trading games. Having understood how Murabaha placements work, we examine operational issues like breakage and back valuations in Murabaha placements. We wrap up session 1 by examining the usage of listed and over the counter commodities to facilitate Murabaha placements and brokerage issues.

Chapter 3: The Islamic "Money Market" Part 2: In this session we examine another treasury instrument; cash Murabaha. We will first examine Tawarruq. International Islamic Financial Market (IIFM), discusses two Tawarruq structures in its master hedging (tahawwut) agreement. The first structure uses agency while in the second structure there is no agency. We examine both the structures and highlight the one preferred by AAOIFI. Having examined Tawarruq Al-Munazzam(Organized Tawarruq) we then discuss the structure of Original

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Tawarruq (Tawarruq Al-Asli). We will play a number trading games to see how these concepts are applied and the implication on treasury positions. We also clarify if there is any difference between Murabaha, commodity Murabaha and Tawarruq.

Chapter 4: The Islamic "Money Market" Part 3. In this session we compare Tawarruq to Bai al-Ainah. We will also examine how Tawarruq is applied for breakage and its implication on Treasury positions. We wrap up session 4 by examining how the Malaysia market developed and implemented the Mudaraba interbank placement. We will highlight how the Central bank regulated to calculation of the profit rate to manage moral hazard issues.

Chapter 5: Islamic "Money Market" Part 4. In this session we will examine how a wakala placement is different from a Mudaraba placement. We also look at "Wakala to do Murabaha" structures and discuss the issue of leakage or application of proceeds. We revisit the issue of Back Value and Back Date in the context of Wakala. We wrap this session by looking at Wadia placements. We examine the Wadia for point system and review how Wadia may be used for placements with Central Banks as applied in Malaysia and Indonesia. Finally we review all interbank deposit instruments we have covered in the money market segment.

Chapter 6: Islamic "Forward FX" Part 1. In this session we review the function of FX operation in Islamic banks and the rules of Sarf. We will deconstruct how a traditional forward transaction works and examine the Sharia'a issues. We will then examine how a cross currency deposit is structured to replicate the forward solution in the Islamic market. We will also look at Salam structures as a possible solution.

Chapter 7: Islamic "Forward FX" Part 2. In this session we will focus on the application of Tawarruq to structure a forward solution. As we will fund the client in this structure, it is close to FX Swap structure. We will review the options that the client has with this funded structure. Finally we contrast the Tawarruq structure to a Bai al-Inah structure. We wrap up this session by comparing how the tawarruq and Salam structures for forward are different.

Chapter 8: Islamic "Forward FX" Part 3. In this session we will examine how a promissory forward structure works. Following this, we will review how the bank may hedge

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itself by either using a Long Murabaha strategy or using a Back to Back promises structure. We will wrap up this session by reviewing the exit strategy for treasurer under the promise and Murabaha forward structures.

Chapter 9: Islamic “Forward FX” Part 4. In this session we will deconstruct how a traditional options transaction works including the exercise of the option and the premium collection. We will then contrast the traditional option to an Arbun optionally solution in the Islamic space. We will also review how an Islamic bank may use a Back to Back Arbun structure to hedge its position. Finally we wrap up the course by reviewing all the FX instruments we have discussed.