

# SUKUK

(ISLAMIC SECURITIZATION)

October 2021



# OUTLINE

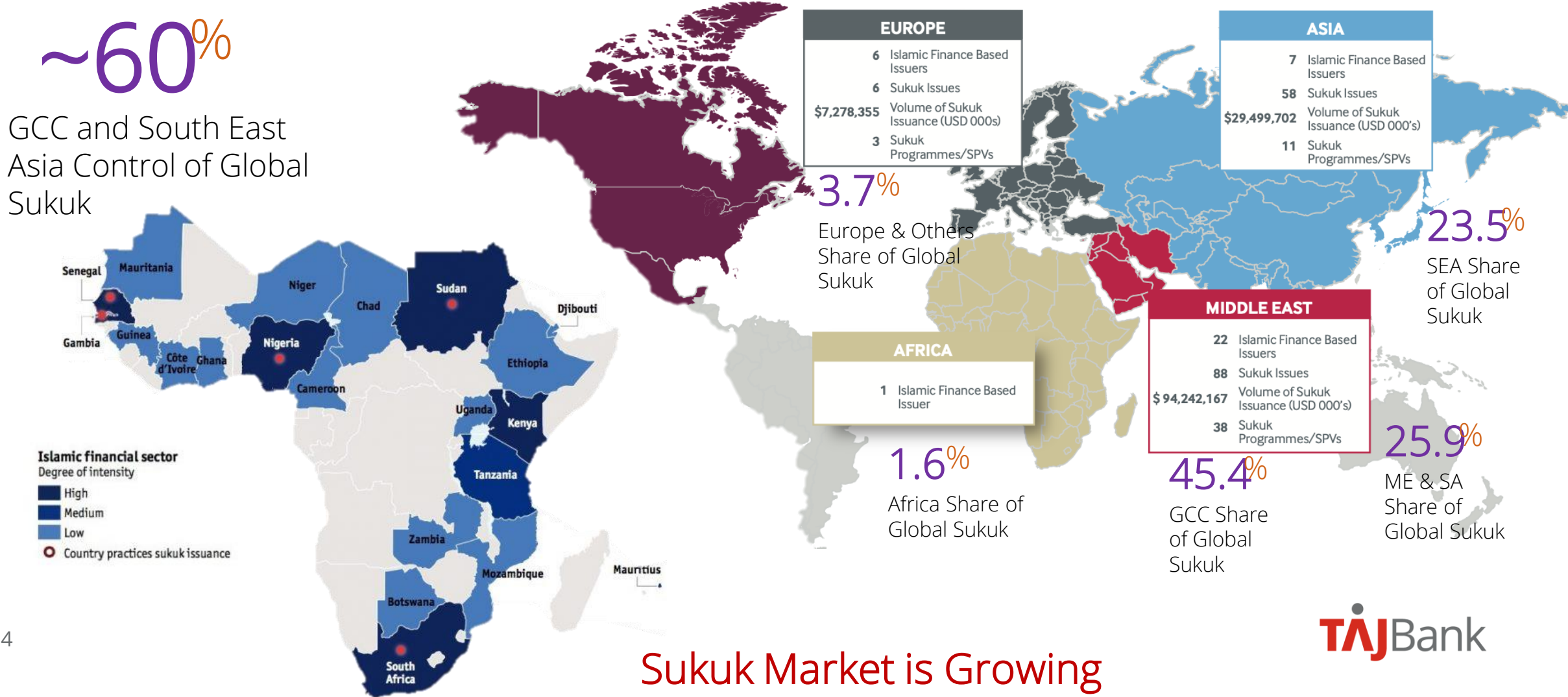
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- Overview of Global Sukuk Market
  - Definition, History & Evolution
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- Sukuk Structures
  - Sukuk Instruments in Comparison
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# Overview of Global Sukuk Market



# Overview of Global Sukuk Market



# Overview of Global Sukuk Market

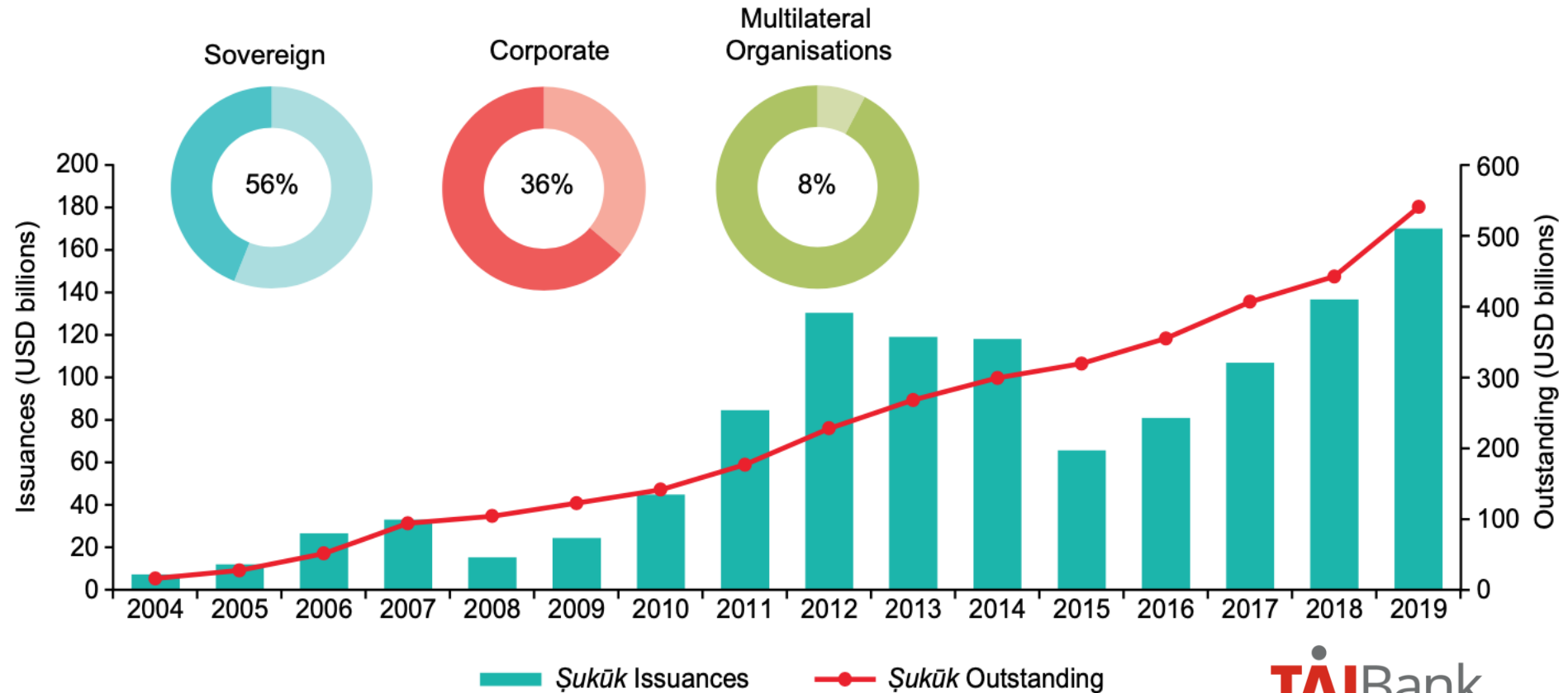
## Global Sukuk Issuances and Sukuk Outstanding Trends (2004–19)

\$543. Billion

Global Sukuk Outstanding

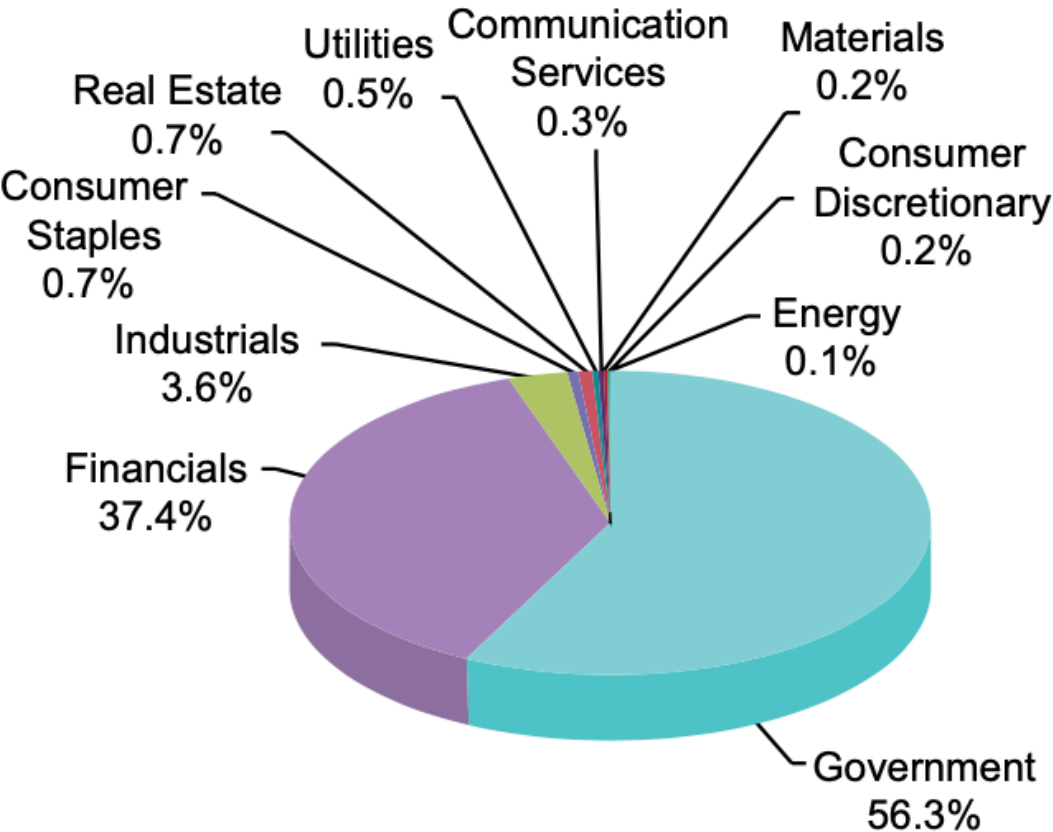
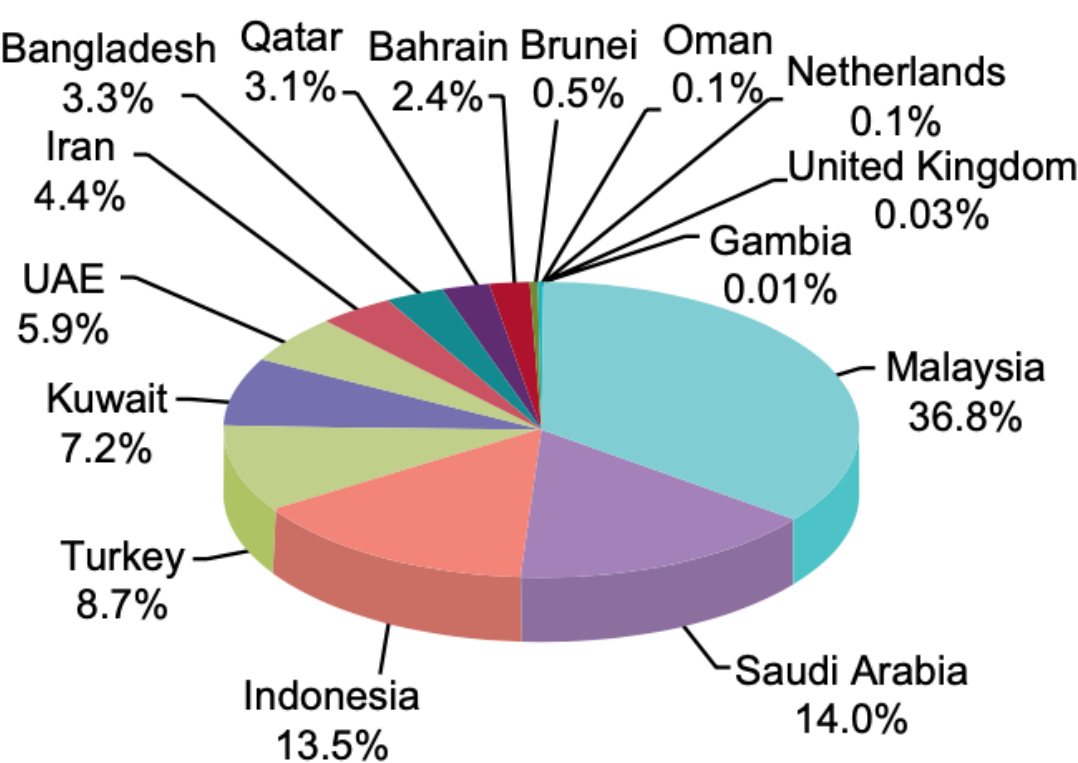
22.3%

Share of Global IF Industry



# Overview of Global Sukuk Market

Which Countries are most active in Sukuk



To which Sectors have Sukuk been deployed?

# Definition, History & Evolution

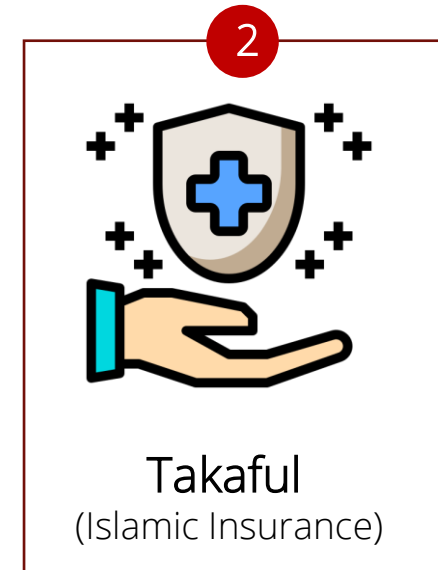


# Definition & History

What is Sukuk?



Islamic Financial System



Each segments have a distinctive set of products and services



# Definition, History & Evolution

What is Sukuk?

**ANS:** Literally, Sukuk is an Arabic term.

It is the plural of another Arabic term – **Sakk**.

**Sakk** = **Certificate of Investment**

Hence...

**Sukuk** = **Investment Certificates**

Technically, Investment Sukuk are **certificates of equal value** representing **undivided shares in ownership** of tangible assets, usufruct and services or (in the ownership of) the assets of particular projects or special investment activity.

[AAOIFI -17(2), 2015]



Sukuk

# Definition, History & Evolution

## What do we know of its Origin?

The origins of sukuk can be traced back to the classical Islamic period. Around 1st Century AH (700-1300 AD) during the Umayyad Caliphate.

It took place in Damascus, Syria.

At that time, papers representing financial obligations originating from trade and other commercial activities were issued in conformity with verse 2:282 of the Holy Qur'an, which encourages fixing contracts in writing term.

يَا أَيُّهَا الَّذِينَ ءَامَنُوا إِذَا تَدَايَنْتُمْ بِدَيْنٍ إِلَىٰ أَجَلٍ مُّسَمًّى فَاكْتُبُوهُ ۚ وَلْيَكْتُبَ  
بَيْنَكُمْ كَاتِبٌ بِالْعَدْلِ ۚ وَلَا يَأْبَ كَاتِبٌ أَنْ يَكْتُبَ كَمَا عَلَّمَهُ اللَّهُ ۚ

*"O believers! When you contract a loan for a fixed period of time, commit it to writing. Let the scribe maintain justice between the parties. The scribe should not refuse to write as Allah has taught them to write."*



Marwan I (623-7 May 685)

Caliph of the [Umayyad Caliphate](#) (684 to 685,)  
Succeeding [Muawiyah II](#) & preceding [Abu-al-Malik](#).



# Definition, History & Evolution

What about its evolution in modern day finance?

## Who did it first?

1st Global Sukuk by Shell  
MDS



A non-Islamic Oil  
Company

## Where did first happen?

1st Global Sukuk in  
Malaysia



An Ethno-Religious Diverse  
Country

## When did first happen?

The Year 1990

199

0  
31 Years  
Ago

## What amount was the 1<sup>st</sup> Issue

125 Million Malaysia  
Ringgit

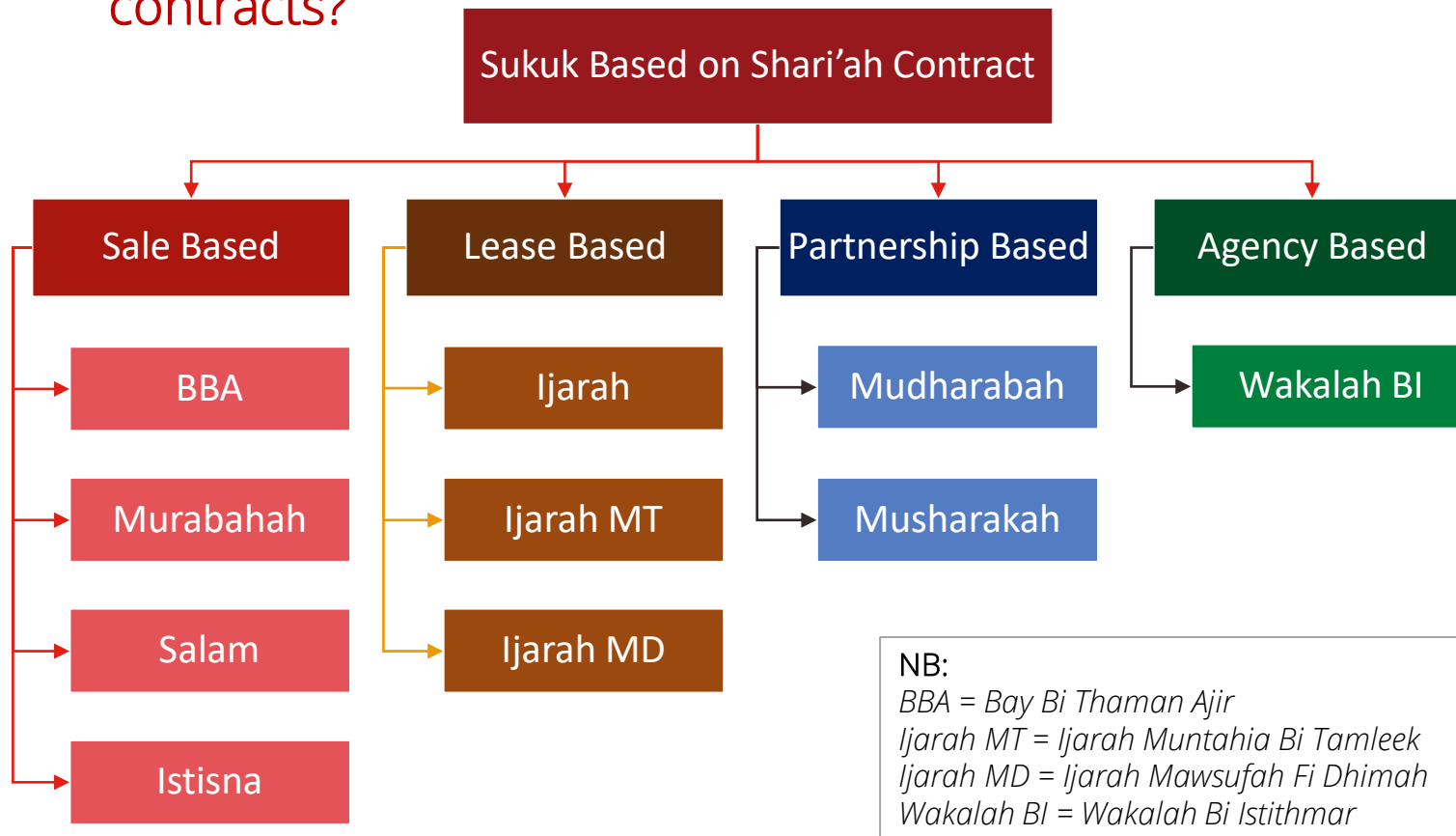
\$33  
Millio

n  
N1.65 Billion on N500/\$

# Sukuk Structures

# Sukuk Structures

What are the categories of Sukuk by Underlying contracts?



How are sukuk structured?

❖ Sukuk are structured based on nominate Islamic financing contracts.

*Example:  
Ijarah, Murabaha, Musharakah, Istisna*

❖ The class and category of each Sukuk is determined by its underlying Islamic Financing contract.

*Example:  
Lease-base or sale-based contract categories*

# Sukuk Structures

Are there other Sukuk

## ASSET-BACKED SUKUK

- ❖ Reliance on the underlying assets to generate returns and to recover the investment of Sukuk holders
- ❖ In case of non-payment, Sukuk holders can sell the

## ASSET-BASED SUKUK

- ❖ Reliance on the credit worthiness of the issuer or obligor
- ❖ In case of non-payment, Sukuk holders can recourse to the obligor.

Tradability

## TRADABLE SUKUK

- ❖ Sukuk that represents tangible assets or proportionate ownership of a business; can be bought and sold on the capital markets

Example: Sukuk al-Ijarah, Sukuk al-Musharakah, Sukuk

## NON-TRADABLE SUKUK

- ❖ Sukuk that represents receivables of cash or goods; their sale would be like trading in debt which is prohibited in Shariah

Example: Sukuk al-Murabahah, Sukuk al-Salam

Asset Class

```
graph LR; SB[Sale Based] --> BBA[BBA]; SB --> Murabahah[Murabahah]; SB --> Salam[Salam]; SB --> Istisna[Istisna];
```

Sale Based

BBA

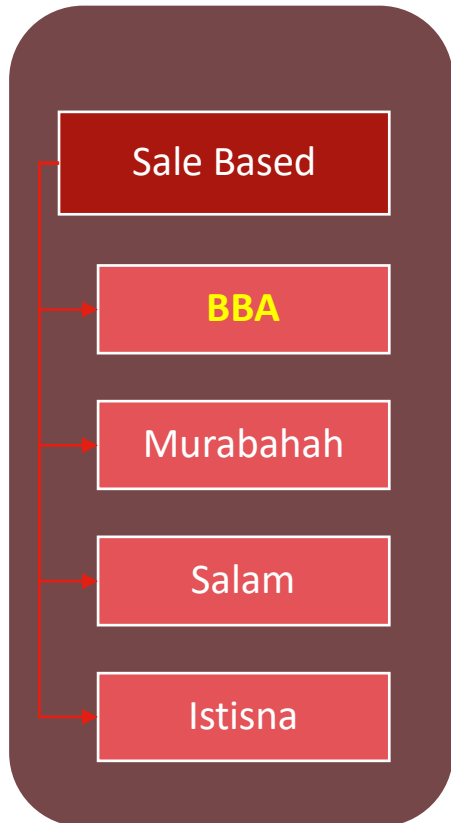
Murabahah

Salam

Istisna

# Sukuk Structures: Sale Based Sukuk

## Sukuk Structures – Sale Based Sukuk

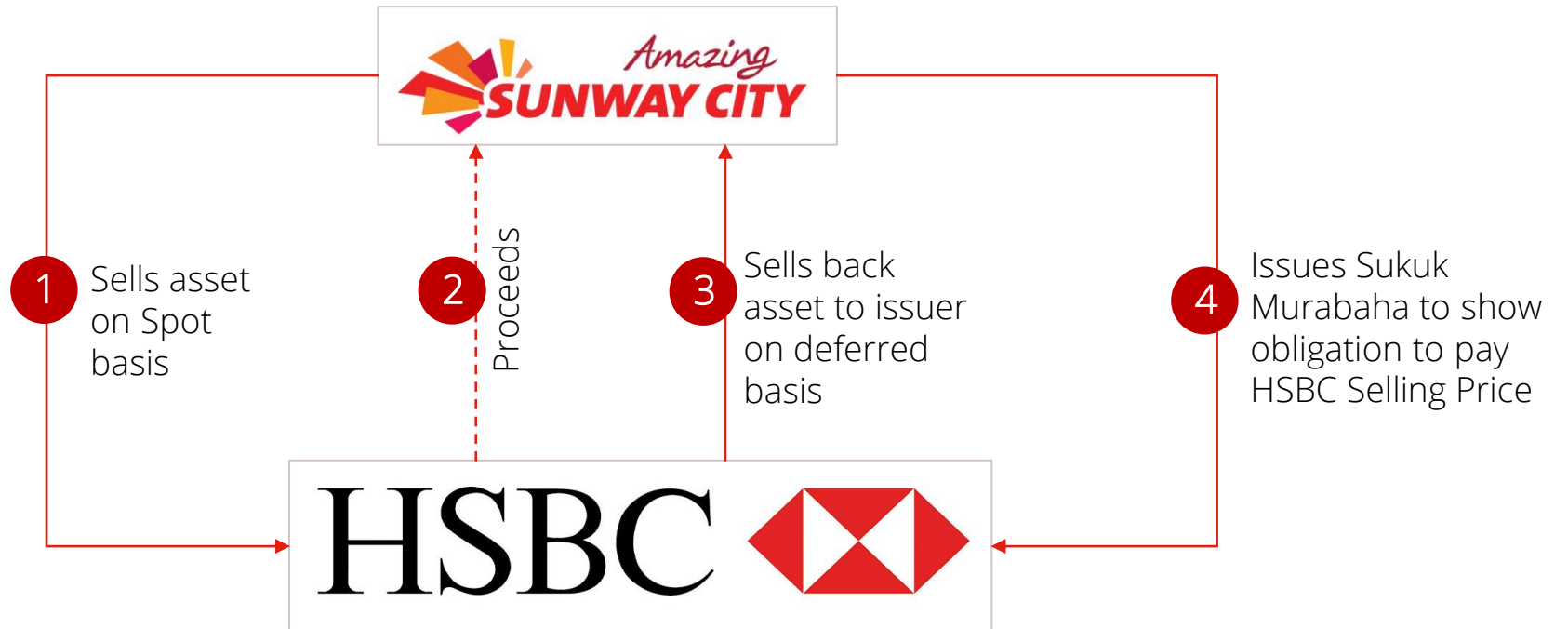
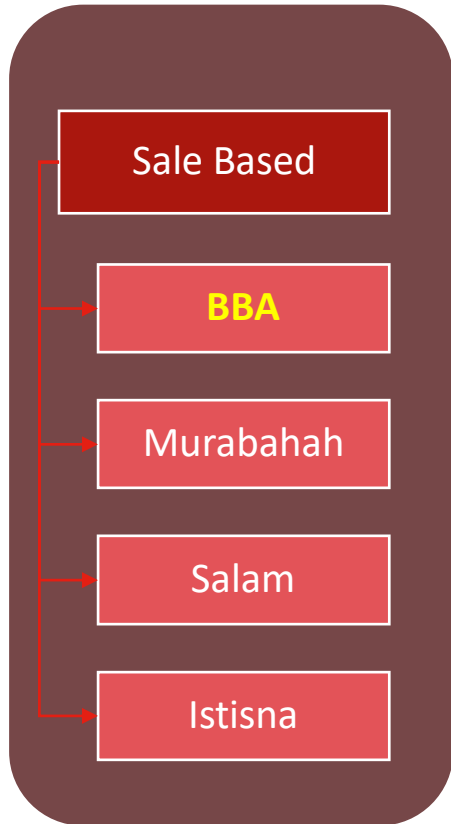


| Murabahah Certificates<br>(Sale with immediate repurchase) |                                                                                                                                                                                                                                                  |
|------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Purpose                                                    | General / various specific Shariah compliant purposes                                                                                                                                                                                            |
| Main Concept                                               | <ul style="list-style-type: none"><li>- Based on a mark-up selling price on a deferred payment basis.</li><li>- Investors purchase the underlying asset from the commodity supplier/seller and sell it to final buyer at higher price.</li></ul> |

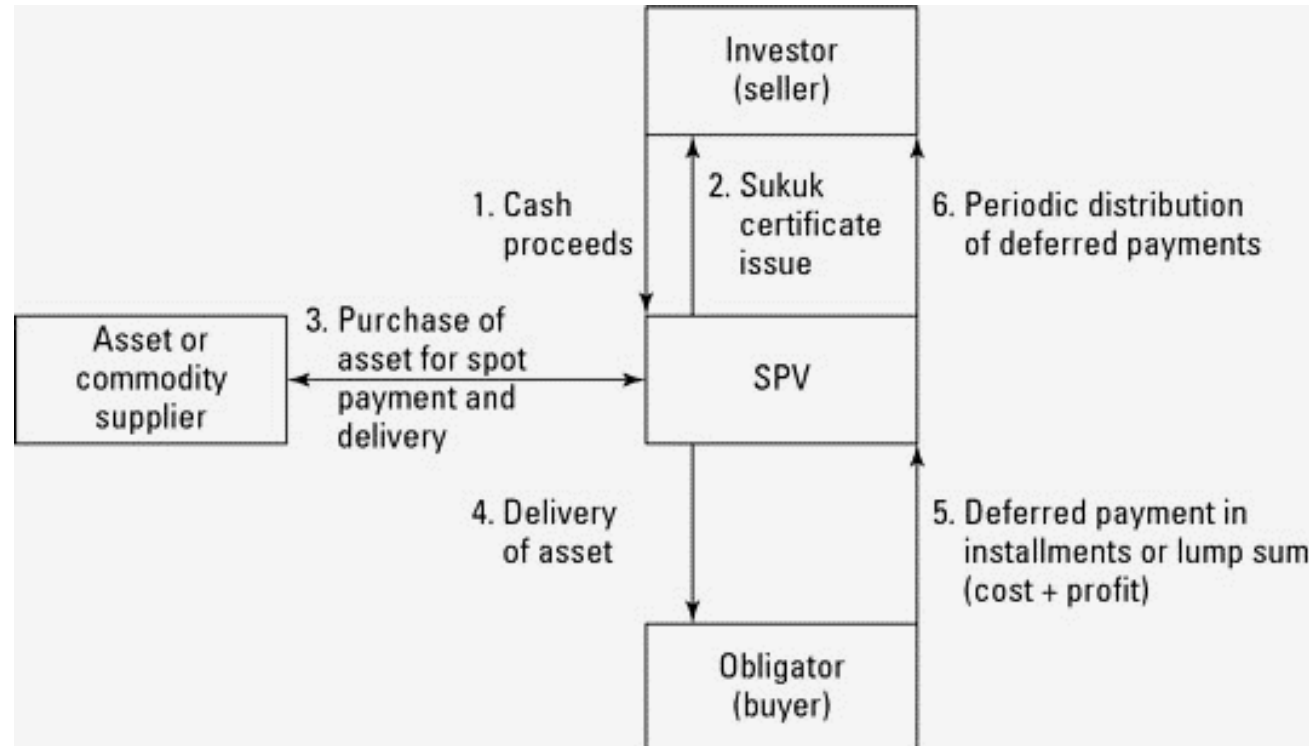
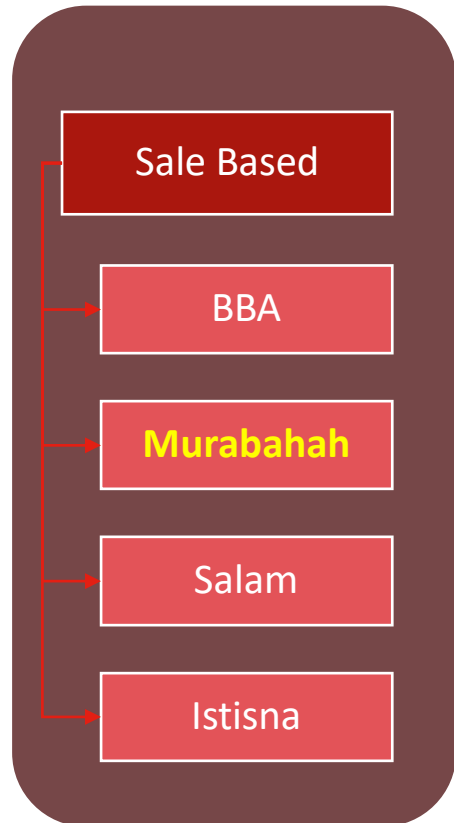


# Sukuk Structures – Sale Based Sukuk

## Case Study: BBA Sukuk (Issued by Sunway city – Malaysia)



# Sukuk Structures – Sale Based Sukuk



Murabahah  
(Murabahah

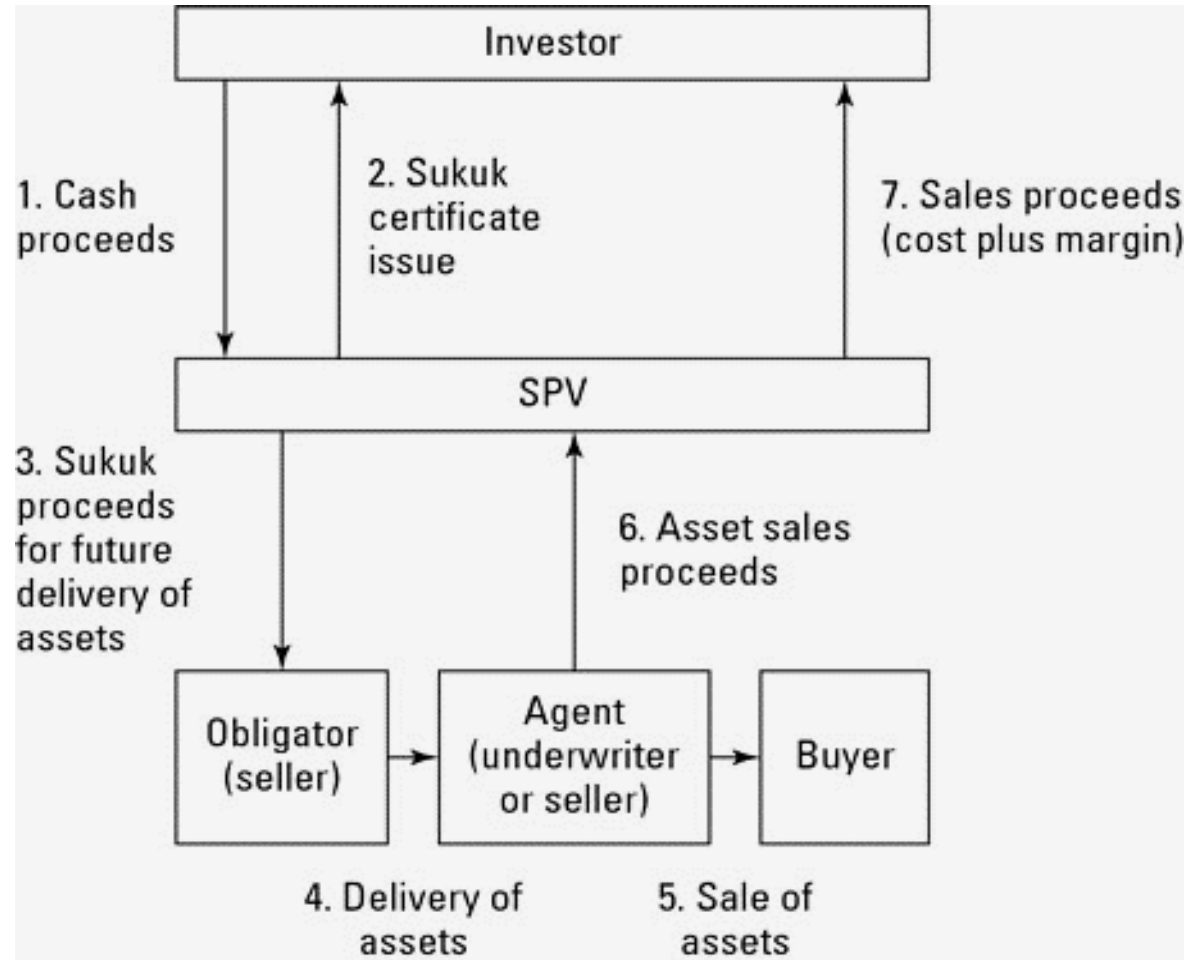
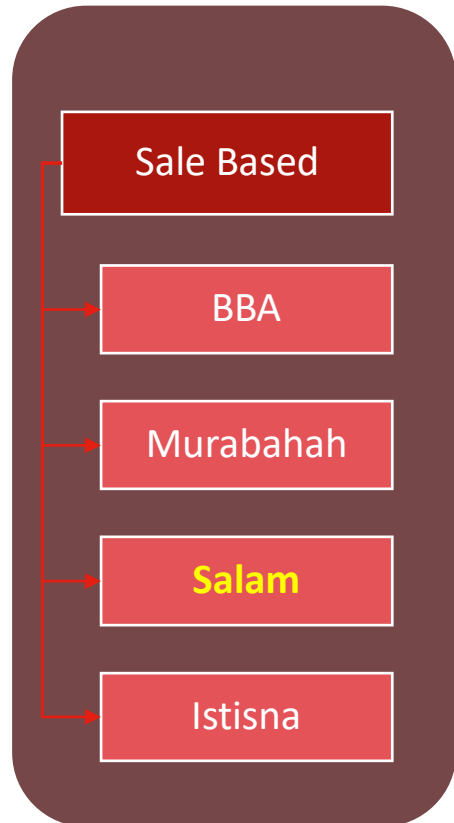
Certificates  
Sukuk):

These are certificates of equal value issued for the purpose of financing the purchase of goods through Murabahah so that the certificate holders become the owners of the Murabahah commodity.

It is not permissible to trade in Murabahah certificates after delivery of the Murabahah commodity to the buyer.

However, trading of Murabahah certificates is permissible after purchasing the Murabahah commodity and before selling it to the buyer.

# Sukuk Structures – Sale Based Sukuk

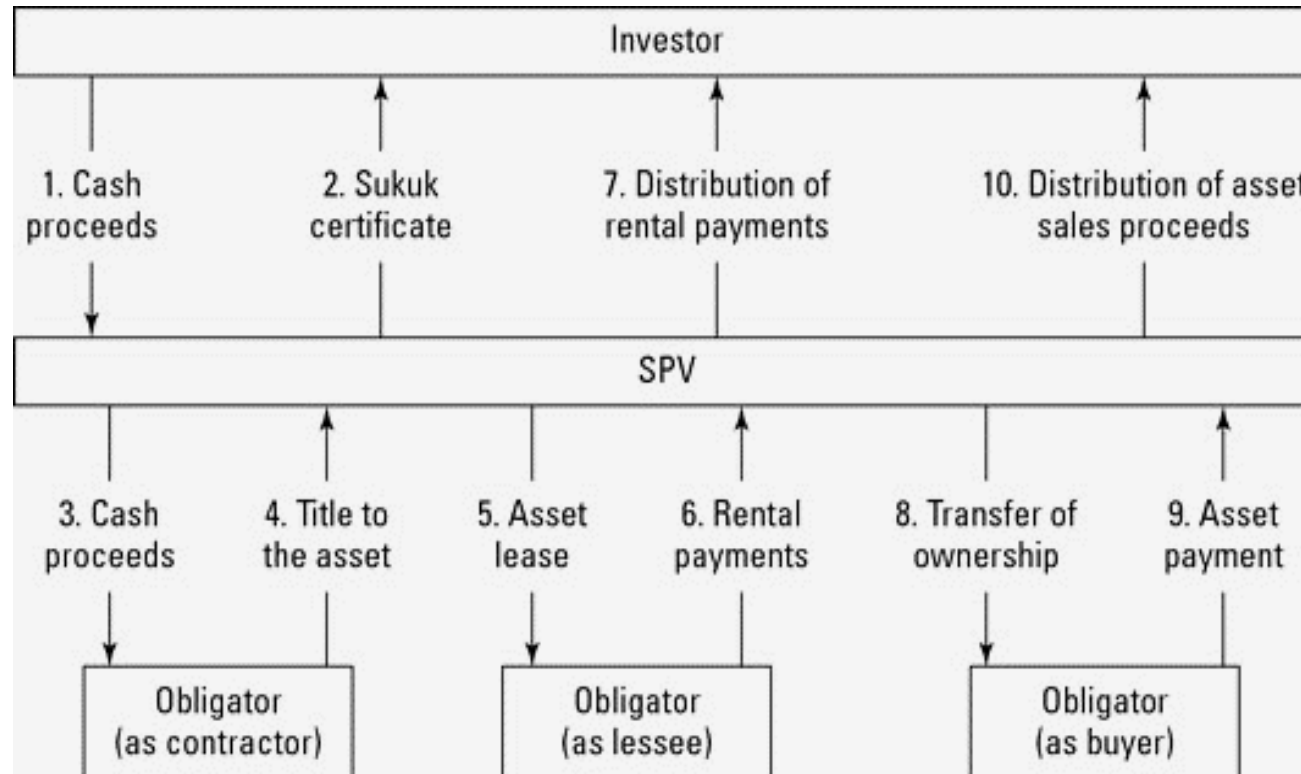
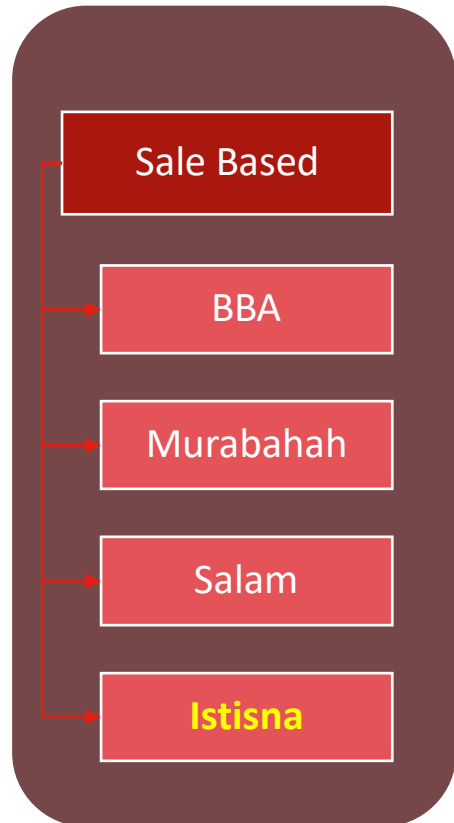


## Salam Certificates (Salam Sukuk):

These are certificates of equal value issued for the purpose of mobilising Salam capital so that the goods to be delivered on the on the basis of Salam come to be owned by the certificate holders.

It is not permissible to trade in Salam certificates.

# Sukuk Structures – Sale Based Sukuk



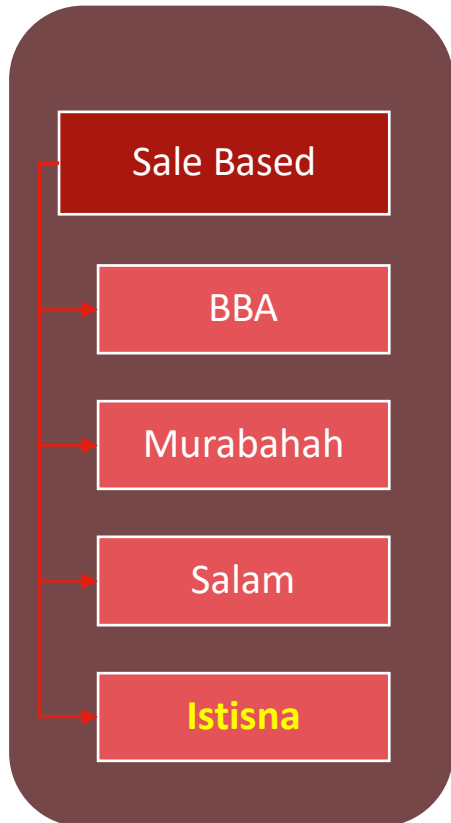
## Istisnah Certificates (Istisnah Sukuk):

These are certificates of equal value issued with the aim of mobilising funds to be employed for the production of goods so that the goods produced come to be owned by the certificate holders.

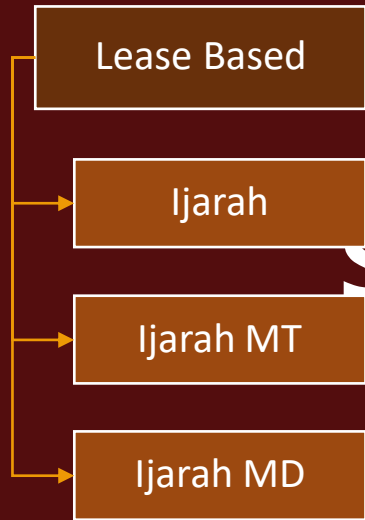
It is permissible to trade in or redeem Istisnah certificates if the funds have been converted, within the period of the Istisnah, into assets owned by certificate holders.

If the realised funds are immediately paid as a price in a parallel Istisnah contract or the manufactured item is submitted to the ultimate purchaser, then trading in Istisnah certificates must follow the rules of trading in debt.

## Sukuk Structures – Sale Based Sukuk

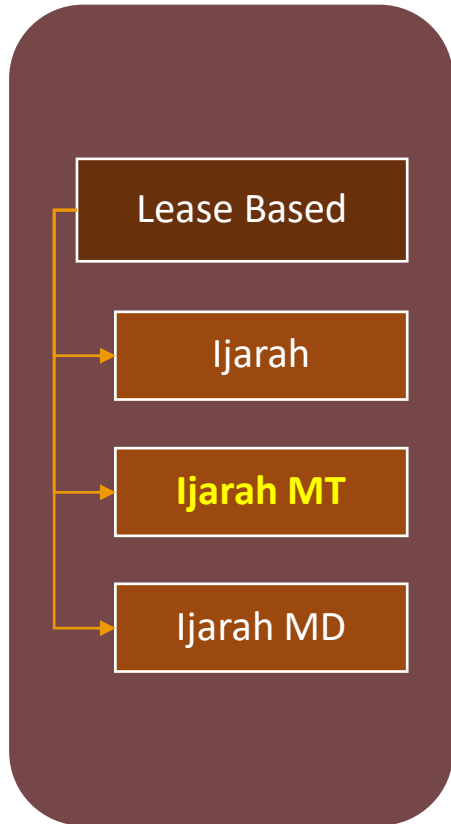


| Istisna' Certificates<br>(Construction Contract) |                                                                                         |
|--------------------------------------------------|-----------------------------------------------------------------------------------------|
| Purpose                                          | Financing construction of asset                                                         |
| Main Concept                                     | Investors fund Issuer for construction of asset via back-to-back construction contract. |



# Sukuk Structures: Lease Based Sukuk

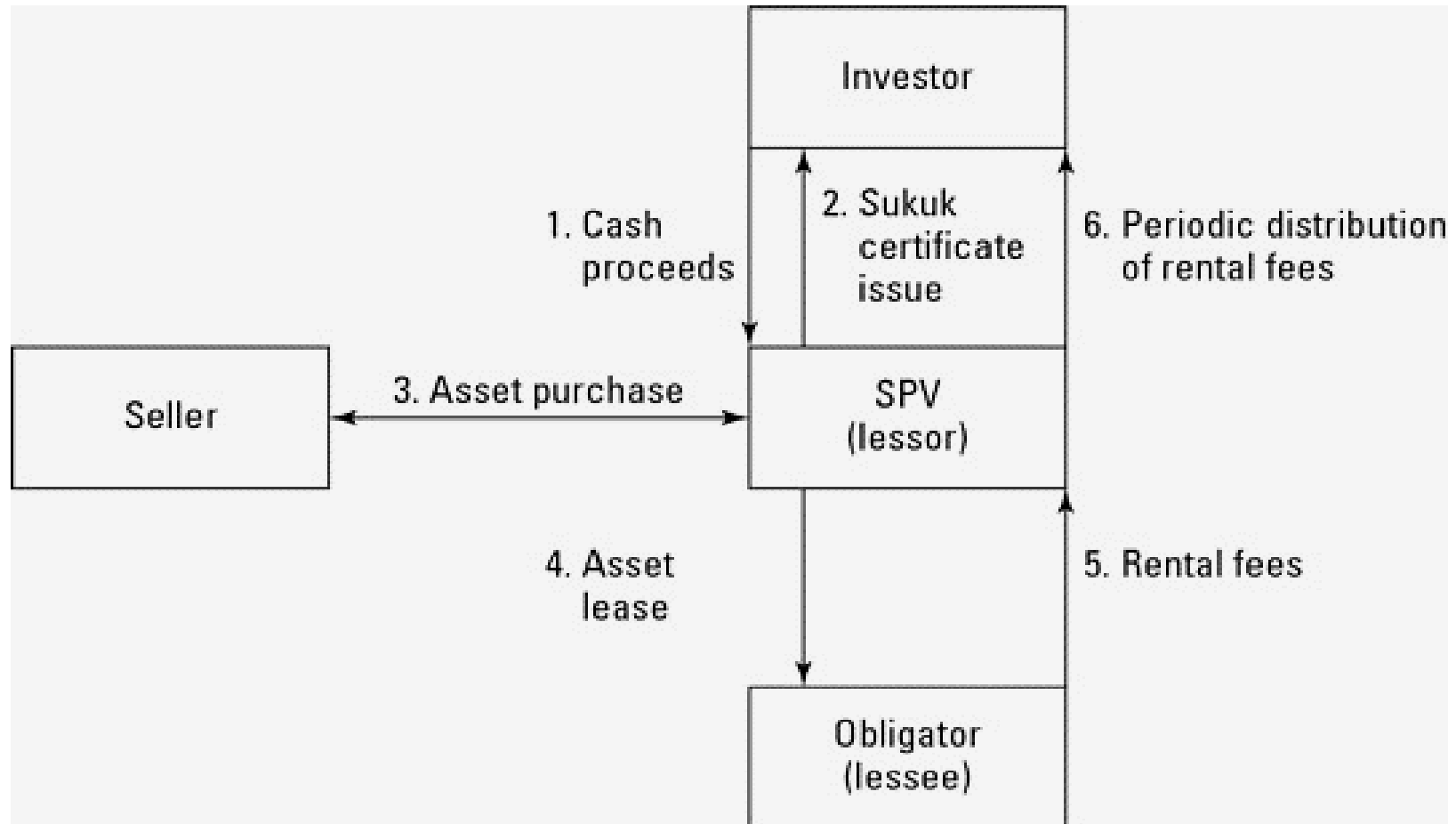
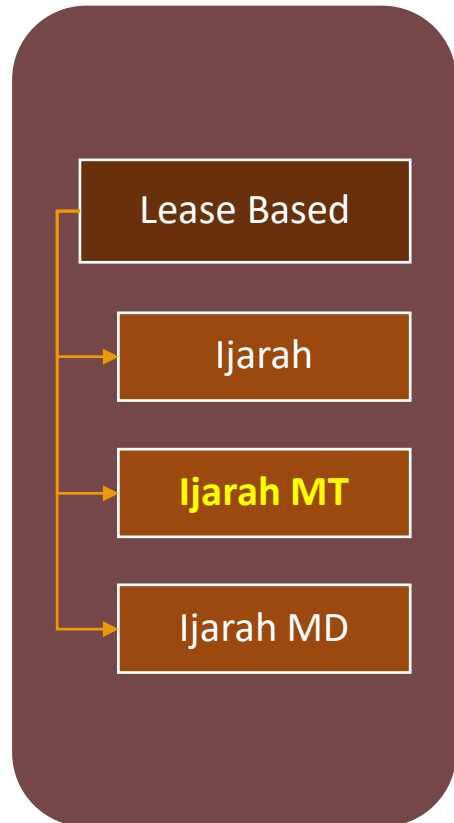
## Sukuk Structures – Lease Based Sukuk



| Ijarah Certificates<br>(Leasing / Renting) |                                                                                                                                                                                                                                                                                                                  |
|--------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Purpose                                    | Acquisition of asset or general / various specific Shariah compliant purposes                                                                                                                                                                                                                                    |
| Main Concept                               | <ul style="list-style-type: none"><li>- It is coupled with a right of the Issuer as lessee to acquire the asset at the end of lease period.</li><li>- Issued based on asset identified on the Issuer's balance sheet.</li><li>- Rental payments to Investors represent profit &amp; principle payment.</li></ul> |

# Sukuk Structures – Lease Based Sukuk

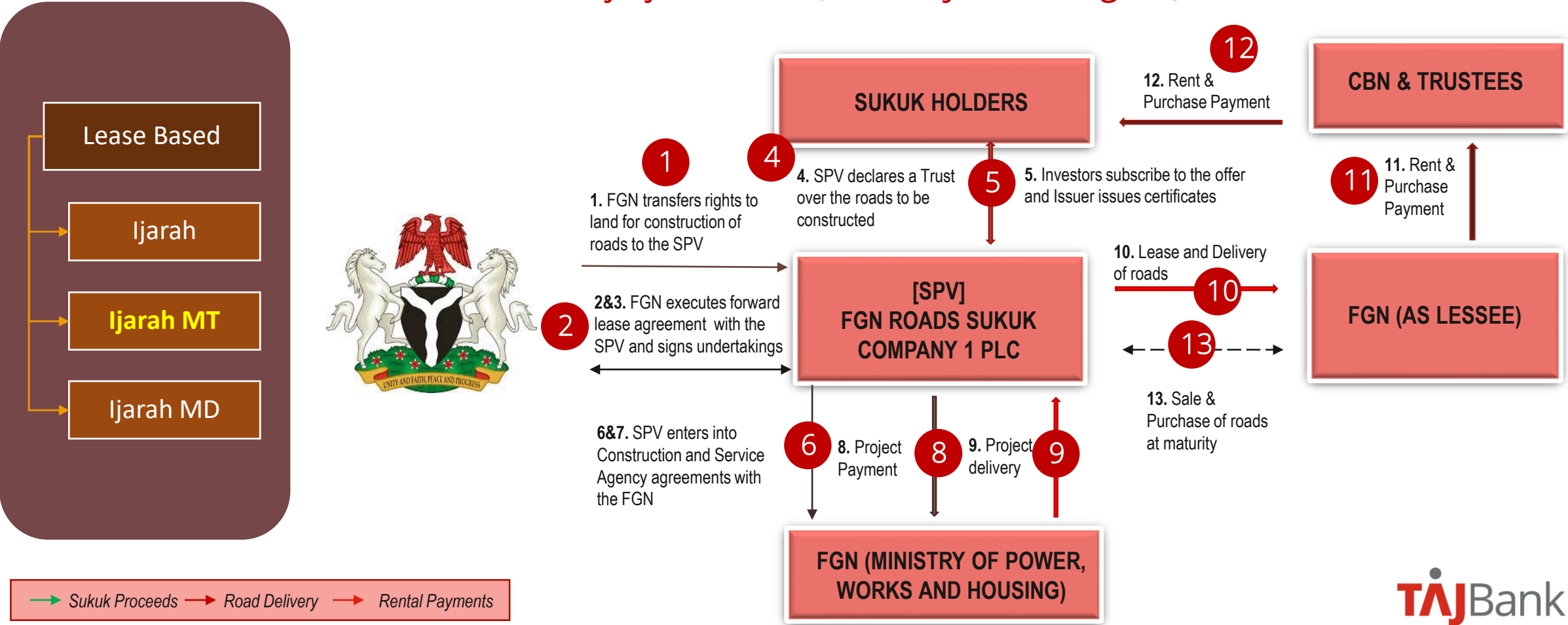
## Process flow of an Ijarah Sukuk





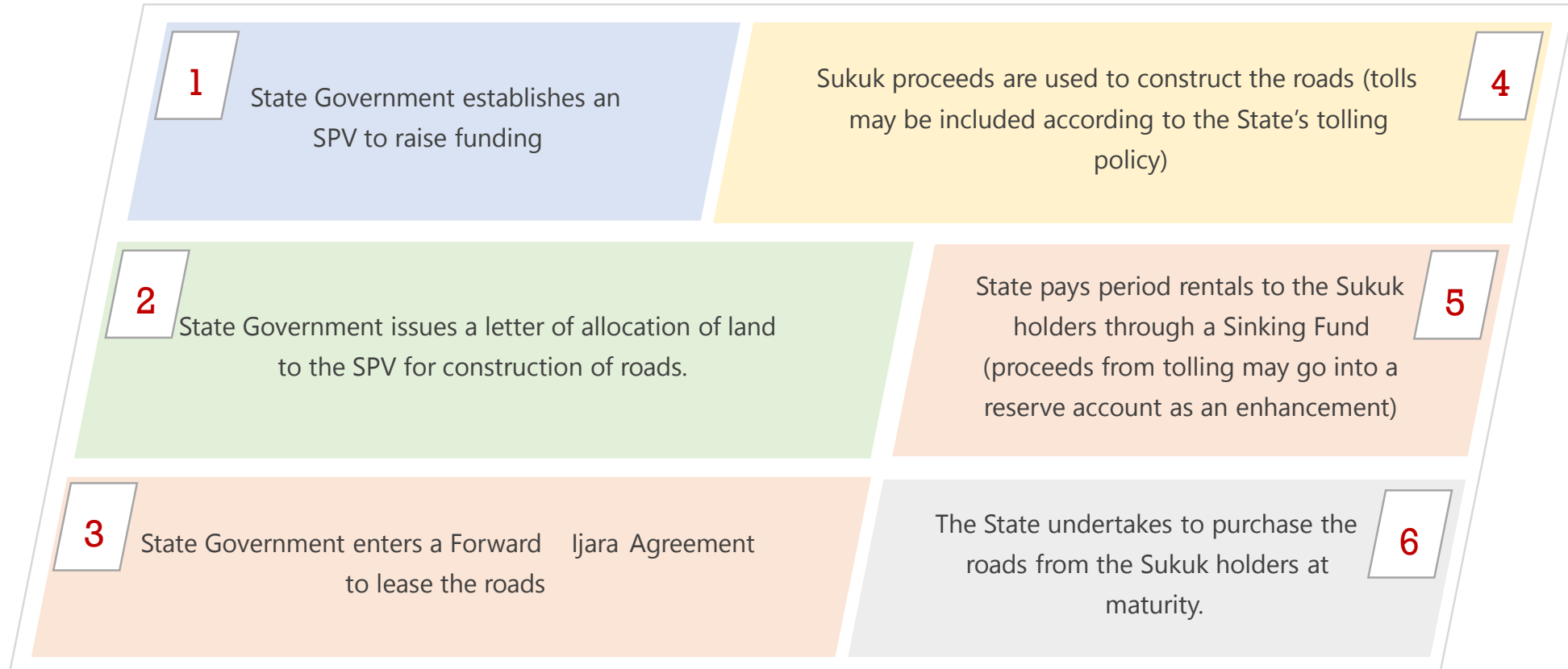
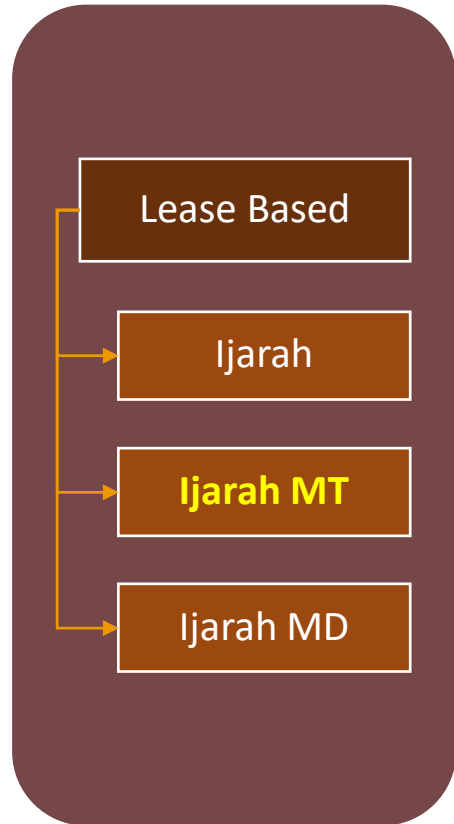
# Sukuk Structures – Lease Based Sukuk

## Case Study: Ijara Sukuk (Issued by FGN – Nigeria)



# Sukuk Structures – Lease Based Sukuk

## Case Study: Ijara Sukuk (*Issued by FGN – Nigeria*)



# Sukuk Structures – Lease Based Sukuk

## Case Study: Ijara Sukuk (Issued by FGN – Nigeria)

Lease Based

Ijarah

**Ijarah MT**

Ijarah MD

Port Harcourt - Enugu



Sukuk Road

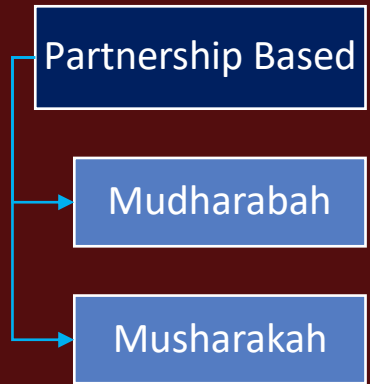
Nigerians need **affordable housing/buildings**  
Sukuk has successfully constructed and equipped school buildings



Ilesa Grammar School

There is a significant deficit of **roads** in Nigeria and Sukuk is already helping to bridge the gap.

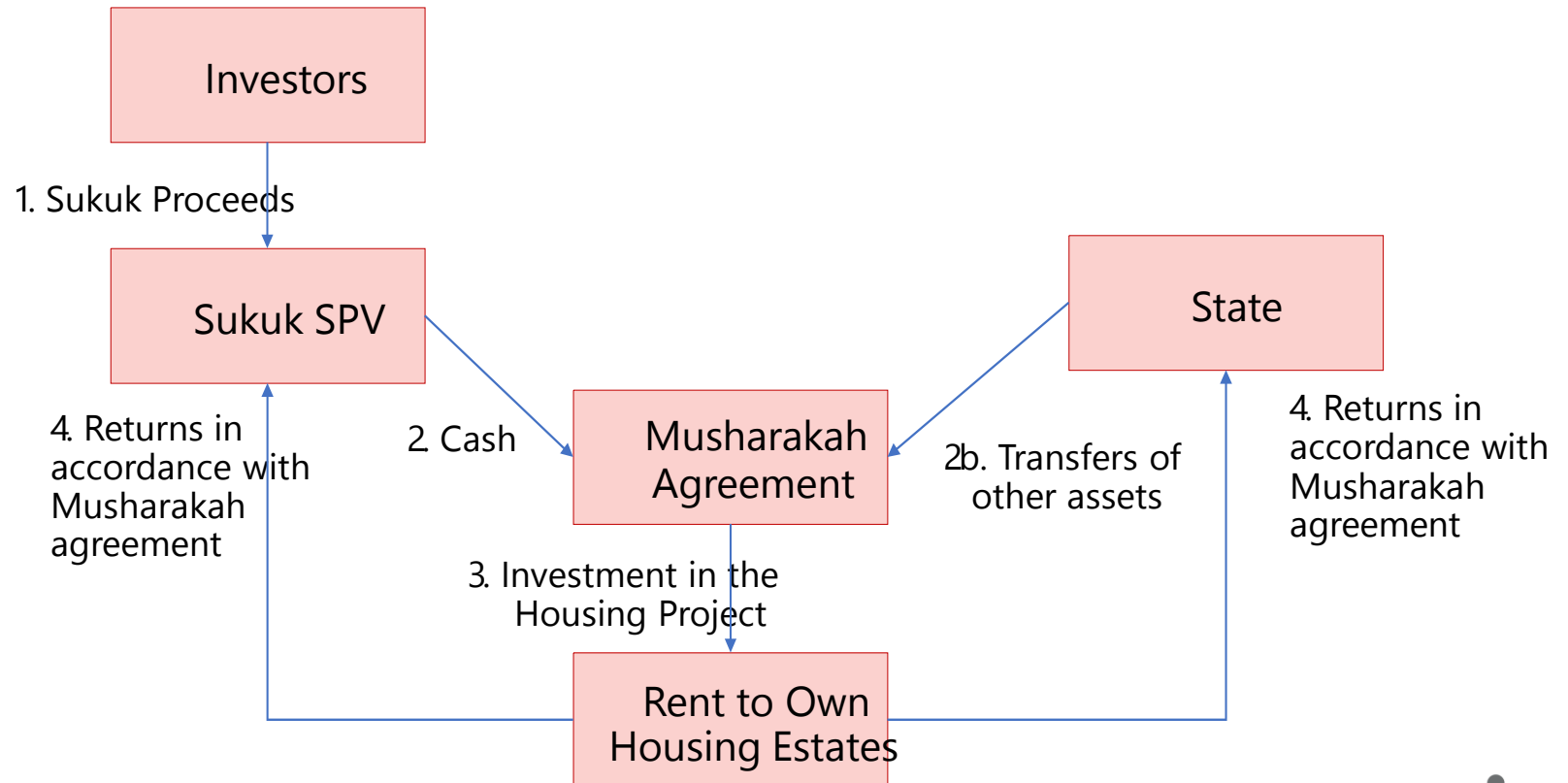
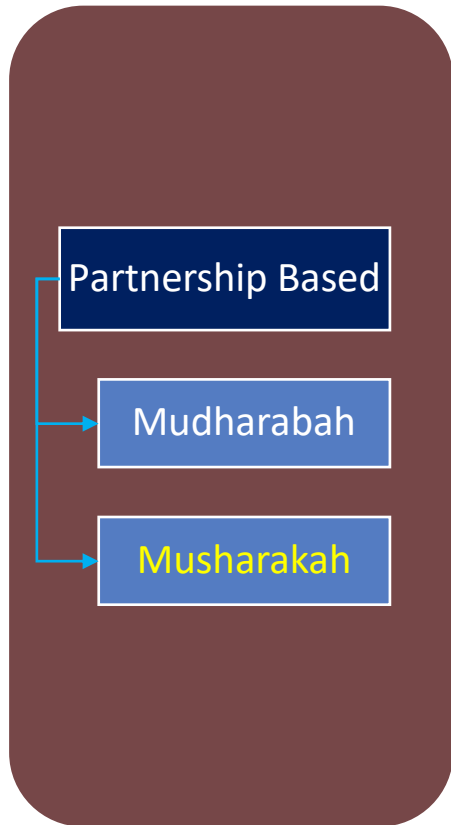
Sukuk Building



# Sukuk Structures: Partnership Based Sukuk

# Sukuk Structures – Sale Based Sukuk

## Case Study: Using Musharakah Sukuk to provide mass housing estates



# Sukuk Structures – Sale Based Sukuk

## Case Study: Using Musharakah Sukuk to provide mass housing estates

Partnership Based

Mudharabah

Musharakah

**1** State Government establishes an SPV to raise funding

Musharakah assets are invested in a **Rent to Own** housing project

**2** State Government and the Special Purpose Vehicle (SPV) enter into Musharakah Arrangement for a fixed period and an agreed profit sharing ratio.

The profits are shared between State and the SPV

**3** Originator (a Musharik) contributes land or other physical assets, SPV (a Musharik) contributes cash i.e. the Sukuk proceeds

The State undertakes to buy Musharakah shares of the SPV on periodic basis to cover shortfall risk.

## Sukuk Structures – Sale Based Sukuk

Partnership Based

Mudharabah

**Musharakah**

### Musharakah Certificates (Profit & Loss Sharing)

#### Purpose

Financing general / specific venture(s) managed on Musharakah basis

#### Main Concept

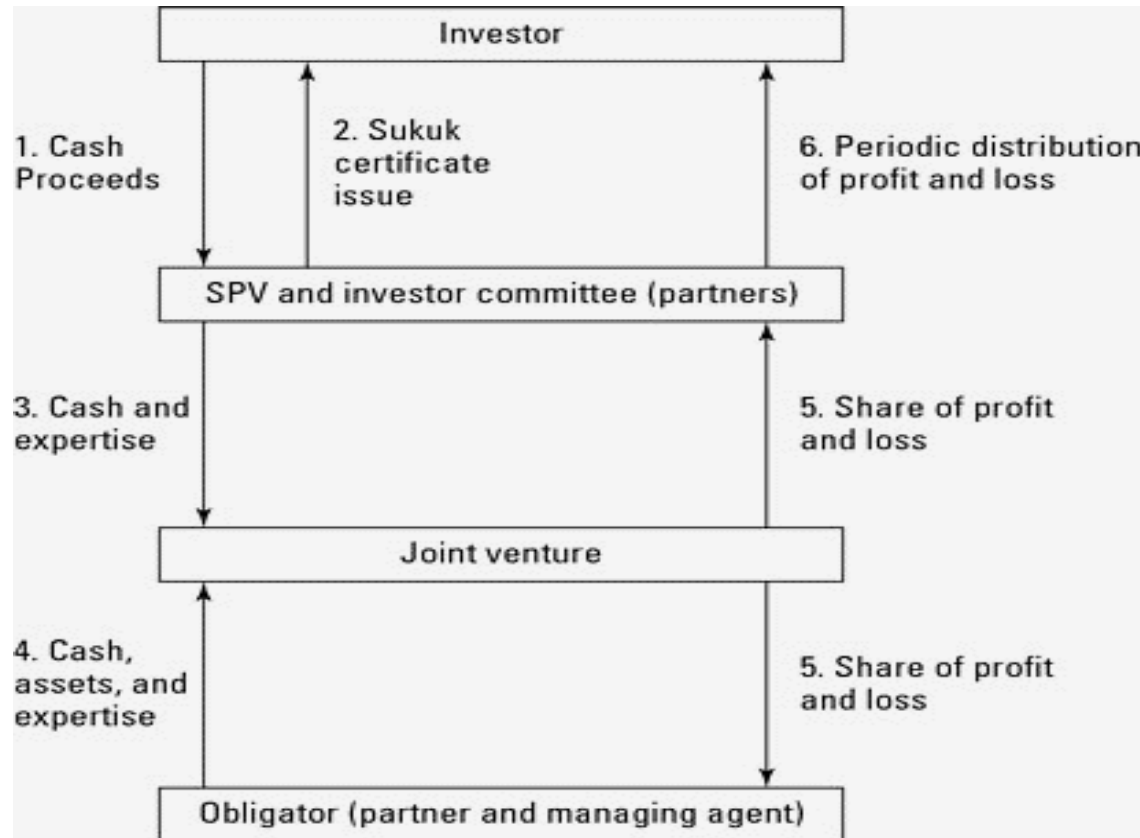
- Requires both parties (Investors and Issuer) to provide capital to the project.
- If loss, both parties will lose in proportion to the size of their investment.

# Sukuk Structures – Sale Based Sukuk

Partnership Based

Mudharabah

Musharakah



## Musharakah Certificates (Musharakah Sukuk):

These are certificates of equal value issued with the aim of using the mobilised funds for establishing a new project, developing an existing project or financing a business activity on the basis of any of partnership contracts so that the certificate holders become the owners of the project or the assets of the activity as per their respective shares, with the Musharakah certificates being managed on the basis of participation.

It is permissible to trade in Musharakah certificates after closing of subscription, allotment of the certificates and commencement of activity with respect to the assets and usufructs.



## Sukuk Structures – Sale Based Sukuk

Partnership Based

Mudharabah

Musharakah

### Mudharabah Certificates (Profit Sharing)

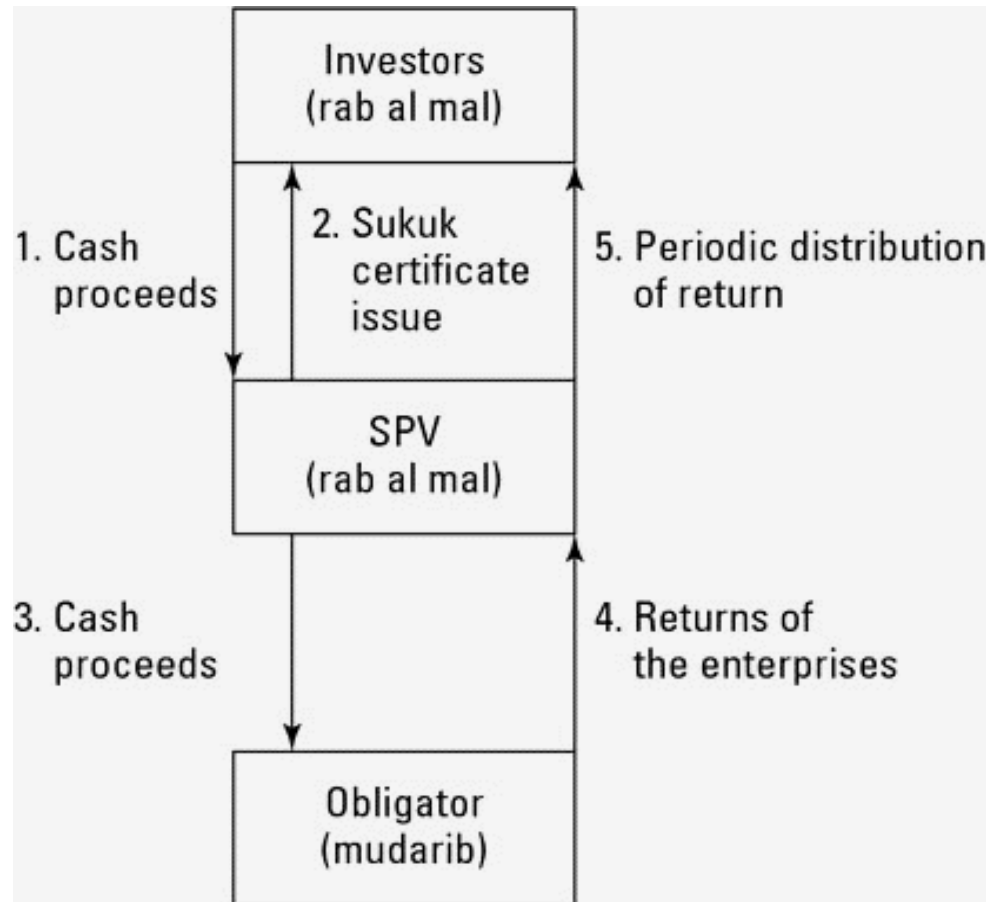
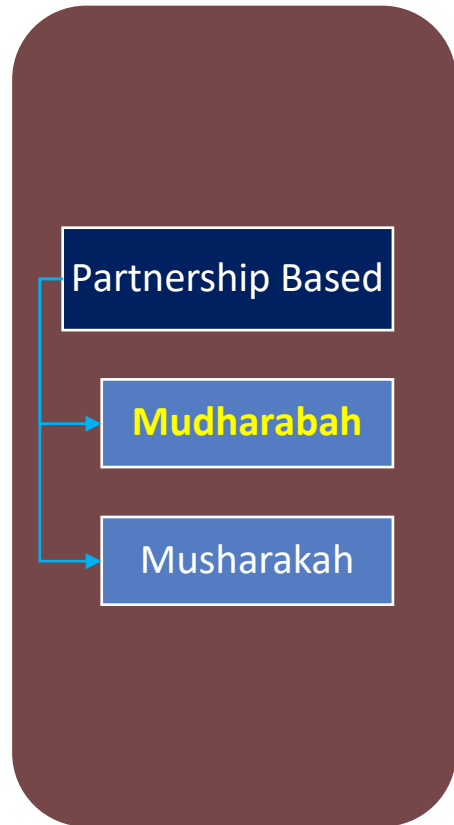
#### Purpose

Financing general / specific venture(s) managed on Mudharabah basis

#### Main Concept

- Contract between two parties to enter business venture.
- Investors as capital provider provides the capital and venture will be managed by Issuer as entrepreneur.
- Profit will be distributed based on pre-agreed ratio.
- If loss, it will be solely borne by capital provider.

## Sukuk Structures – Sale Based Sukuk



### Mudarabah Certificates (Mudarabah Sukuk):

These are certificates of equal value issued with the aim of using the mobilised funds for establishing a new project, developing an existing project or financing a business activity on the basis of any of partnership contracts so that the certificate holders become the owners of the project or the assets of the activity as per their respective shares.

The sukuk holders are the silent partners, who don't participate in the management of the underlying asset, business, or project. The working partner is the sukuk obligator.

It is permissible to trade in Mudarabah certificates after closing of subscription, allotment of the certificates and commencement of activity with respect to the assets and usufructs.

## Sukuk Structures – Sale Based Sukuk

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Other types of Sukuk includes:

1. **Sharecropping certificates (Muzara'ah Sukuk):** used for financing a project on the basis of Muzara'ah so that the certificate holders become entitled to a share in the crop according to the terms of the agreement.
2. **Irrigation certificates (Musaqat Sukuk):** used for irrigation of fruit bearing trees, spending on them and caring for them on the basis of a Musaqat contract so that the certificate holders become entitled to a share in the crop as per agreement.
3. **Agricultural certificates (Mugharasah Sukuk):** used for planting trees and undertaking the work and expenses required by such plantation so that the certificate holders become entitled to a share in the land and the plantation.



Partnership Based

Mudharabah

Musharakah

# Sukuk Instruments: **Comparison**

# Sukuk Instrument – Asset backed vs Asset Based

| CATEGORIES               | ASSET BACKED SUKUK                                                                           | ASSET BASED SUKUK                                                                      |
|--------------------------|----------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------|
| Issuer                   | SPV                                                                                          | SPV or Company                                                                         |
| Process                  | Securitization of Tangible Assets                                                            | Securitization of Receivables                                                          |
| Characterization         | Equity-Like                                                                                  | Debt-Like                                                                              |
| Sources of Payment       | The revenues generated by the underlying asset                                               | The originator/obligor's cash flow                                                     |
| Sukuk holder's Ownership | <b>Legal ownership</b> with rights to dispose of underlying assets                           | <b>Beneficial ownership</b> with no rights to dispose of underlying assets             |
| Recourse                 | Sukuk holders cannot recourse to the originator ( <b>recourse only to underlying asset</b> ) | Sukuk holders can recourse to obligor (originator) if there is a shortfall in payments |
| Funding Cost             | Mainly based on the strength of the asset cash flow                                          | Market driven mainly depending on originator/issuer credit rating/standing             |
| Presentation/Disclosure  | The asset is separated from the originator's book                                            | The asset stays on the balance sheet of the originator/obligor                         |
| Example                  | Mudarabah Sukuk                                                                              | Murabahah Sukuk<br>Ijarah Sukuk (FGN Sukuk)                                            |



**Thank You!**