Short Term Sukuk and Islamic Liquidity Management

John Weguelin
January 2007
Islamic Finance Today

• Islamic banking assets heading towards 20% of total banking assets in several GCC states, over 10% in Malaysia

• Improving regulatory, fiscal and political landscape, particularly in the UK

• Greater demand for Sharia’a compliant products

• Nascent but growing Islamic finance market in Europe, with Muslim population of 88 million (including Turkey)

• Ethically and environmentally friendly nature of Islamic finance increasingly attractive to non-Muslim
Parallels

- Parallels with other markets
- Speed of transition is quicker
- Change/innovation happening all the time:
  - Mortgage Backed Sukuks
  - Exchangeable Sukuks
  - IIFM/ISDA working on documentation
  - Move to improve liquidity in the Sukuk market
  - Work on standardising documentation
  - 1st Sharia’a Compliant Islamic Investment Bank to receive FSA authorisation
Functions of Sukuk Market

- Risk Management
- Liquidity Management
- Balance Sheet Management

<table>
<thead>
<tr>
<th>Short Term Islamic Instruments</th>
<th>Medium-Long Term Islamic Instruments</th>
<th>Conventional Financial Instruments</th>
</tr>
</thead>
<tbody>
<tr>
<td>Murabaha</td>
<td>Murabaha</td>
<td>Credit Default Swaps</td>
</tr>
<tr>
<td>Short Term Sukuk</td>
<td>Musharaka</td>
<td>Negotiable Certificates of Deposit</td>
</tr>
<tr>
<td>Wakala</td>
<td>Ijara</td>
<td>Repos</td>
</tr>
<tr>
<td></td>
<td>Istisna’a</td>
<td>Interest Rate Swaps</td>
</tr>
<tr>
<td></td>
<td>Salam</td>
<td>Basis Swaps</td>
</tr>
<tr>
<td></td>
<td>Sukuk</td>
<td>Senior &amp; Subordinate Debt</td>
</tr>
</tbody>
</table>
Drivers for Liquidity

- Market Centres
- Transparency
- Credit Ratings
- Consistency of interpretation
- Ease of Access
- Size of Issues
Government & Corporate Organisations Role

- **Governments and quasi-governmental institutions:**
  - Critical to development of liquid secondary market
  - Help develop legal and regulatory framework
  - Standardisation of documentation
  - Are regulators, issuers and investors

- **Program Issues – volume and consistency**
EIIB’s Role

Short Term Liquidity Management
• Commodity Murabaha
• Wakala

Long Term Sukuk Investment / Trading
• Active participation in the primary Sukuk market
• Active role in the secondary Sukuk market
• Active participation in the Syndicated Term Financing
• Trade Finance
• Asset Management
• Partnerships with local banks
Way Forward

- Need to recognise that the Sukuk market is only 5 years old
- Evolution thus far has been exponential
- Develop the entire short end of the yield curve
- Sharia’a compliant derivatives