Islamic Finance *news*

2007

GUIDE

January 2007

Note from the publisher

As we enter 2007 Islamic finance will continue to develop and reach out to the world's issuers and investors regardless of their faith, religion and location. We will continue to see major advancements in innovation and product development and new players will amaze us with bigger and better offerings.

New markets will emerge following the likes of China, Japan and Kenya in 2006. However, the focus will again be on the current dominant players and this is where we're likely to see the major growth. Malaysia, currently boasting the world's largest Islamic bond market, will continue to set the pace but the United Arab Emirates, Saudi Arabia and Kuwait are all expected to reduce the gap if not reverse it. The UAE is a bustling haven for Islamic finance with Abu Dhabi, Dubai and Sharjah claiming almost every major financial institution with Islamic capabilities between them.

Malaysia may have the upper hand on the quantity of Shariah compliant issuances, but the UAE can certainly claim the biggest with the likes of PCFC and Nakheel amounting to a combined US$7.02 billion. These are the deals which raise eyebrows in Europe and the US. Indonesia will witness a major transformation with the proposed new regulations and standards for issuing Islamic paper in the world's most populous Muslim country. Up to US$10 billion needs to be raised over the next ten years for necessary infrastructure projects. The Islamic Development Bank has already announced US$1.5 billion of investment this year.

Singapore, which is yet to issue a Sukuk but continues to vigorously promote its Islamic banking capabilities, may find its niche in the Islamic funds and wealth management sectors.

With the usual array of nations claiming to be the global centre for Islamic finance we will surely witness an abundance of sovereign paper hitting the market. Or perhaps it will be yet another case of not walking the walk. London, Dubai, Singapore, Qatar, Kuwait and Saudi Arabia take note.

Islamic REIT's will almost certainly be an interesting market to watch in 2007 with Al-`Aqar KPJ REIT being the world's first last year and winning numerous plaudits including one in Islamic Finance news' Deals of the Year Awards.

We're probably not too far away from seeing the first fund of Islamic funds entering the market now we have Islamic hedge funds. And it's also likely we'll witness the first true Islamic securitization this year. Will 2007 be the year we see the secondary market pick up, increasing the attractability of Islamic paper in yet the relatively untapped markets? Although, with 40% of the recent Nakheel Sukuk (US$3.52 billion) investor base coming from Europe we're on the way.

As mentioned we've recently witnessed some large deals, but what would a Hutchison, Temasek, Boeing or US sovereign issuance do for the industry? Well perhaps we'll find out this year.

We've seen a number of traditionally local banks launch operations in new markets. A trend likely to continue! However, would more joint ventures like that of CIMB-Kanoo be more enticing? Ultimately though, with the necessity for greater capitalization amongst the majority of today's Islamic banks true consolidation will win the day.

In this the second edition of the Islamic Finance news Guide, we provide you with the industry's most comprehensive and authoritative review of 2006 and preview of 2007. With 32 exclusively authored industry sector and market reports you can be assured there's plenty to read. We also have the full results of the Islamic Finance news Deals of the Year and Best Islamic Banks Poll for 2006, both of which were carried out during December. League tables, a full review of the stories from 2006, the industry's largest terminology glossary and much more are all contained within these pages.

I would like to thank Professor Rodney Wilson who has again kindly authored the introductory industry overview and all the other contributors from around the world for sharing their insights and predictions. My thanks also goes to the editorial, marketing and production teams here at Redmoney who have worked endlessly to ensure this reaches you.

Finally, thank you, our readers for your continued support. On behalf of the entire team at Islamic Finance news and Redmoney, I'd like to wish you a very happy and prosperous 2007.

Very best regards,

Andrew Morgan
Managing Director & Publisher

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Government of Dubai, Department of Civil Aviation
USD 1 Billion Sukuk - Government of Dubai's inaugural Sukuk issue
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USD 550 Million Sukuk - First ever airline Sukuk
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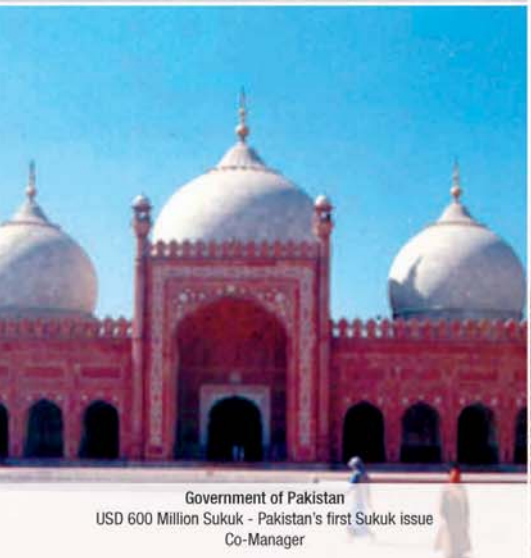

Government of Pakistan
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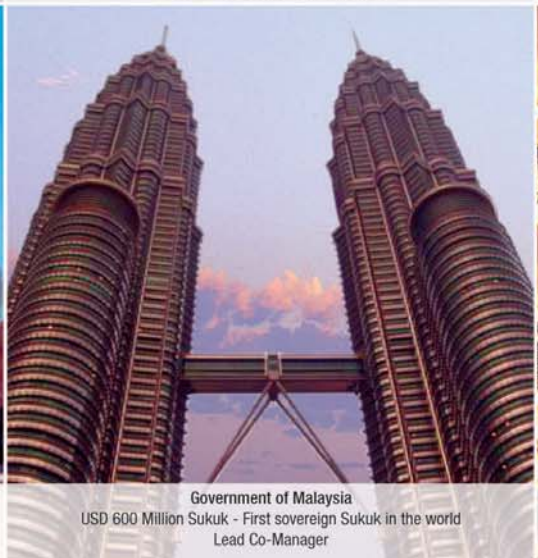

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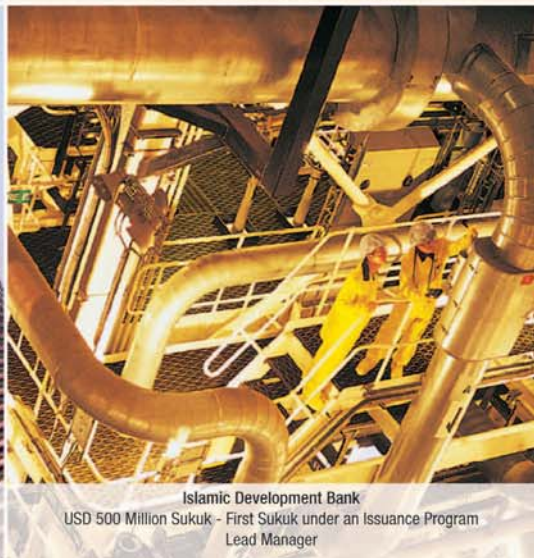

Islamic Development Bank
USD 500 Million Sukuk - First Sukuk under an Issuance Program
Lead Manager

Global Islamic Capital Markets

By Professor Rodney Wilson

The last year witnessed mixed results from Islamic capital markets, usually defined as including the issuance and trading in equities that are Shariah compliant and Islamic Sukuk securities. The conventional equivalents are equity and bond markets and the institutions that invest in these markets, namely investment banks, managed funds and insurance companies.

Shariah compliant equity investments

Just because securities are Shariah compliant does not imply that they necessarily under-perform or out-perform conventional market instruments. In 2006 there was little sign of significant divergence between the returns on Shariah compliant assets and their conventional equivalents, and it is unlikely that there will be much divergence in 2007. Specifically with equity investments, the major factor explaining the differences between the performance of the Dow Jones Islamic Indices and their mainstream indices is the performance of the shares of conventional banks, as other shares screened out (such as those of brewers and distillers) are not significant enough to affect the markets. Generally if conventional bank shares do well, Shariah compliant investors lose out, but if they fare less well, Shariah compliant investors do better. Globally 2006 was a good year for bank shares, but by no means outstanding, and therefore Shariah screening made little difference to performance.

Of greater significance for Shariah compliant equity investment was the performance of the home markets of the investors. Following the Gulf equity markets boom of 2003–2005, price–earnings ratios became distorted, and it became obvious to most observers that a significant correction was likely, even if its timing could not easily be predicted. The inevitable downturn came in February and March, with Gulf markets losing almost half of their value over the remainder of the year. Saudi Arabia in particular – the largest equity market in the Islamic world in terms of capitalization – fared especially badly, with most investors losing substantial amounts. Islamic managed funds focused on local market investments could not escape the downturn, and all suffered capital depreciation in 2006.

Despite the setback in Gulf stock markets, the more prudent Shariah compliant investors, with diversified international portfolios, were only marginally affected. Indeed, many saw the correction coming, realized their gains, and looked to invest elsewhere, especially in Asian markets, although there was also some movement into euro-denominated stock, encouraged by concerns about the depreciation of the US dollar. It was therefore a good year for marketing Shariah compliant funds focused on Europe and Asia to Gulf investors, who in 2005 viewed such markets unfavorably, given the phenomenal returns in their own home markets.

"If conventional bank shares do well, Shariah compliant investors lose out, but if they fare less well, Shariah compliant investors do better"

The wider impact of the stock market correction in the Gulf appears to have been limited, partly because of continuing high oil prices, as GDP growth in Saudi Arabia again exceeded 6.5%, with the figure for the UAE being nearer 10%, and the economy of Dubai growing significantly faster. As a consequence, private wealth continued to grow rapidly, including that of those high net worth families who have a strong preference for Shariah compliant investment. Although oil prices are expected to be lower in 2007, with an inevitable slowing down in GDP growth rates in the Gulf, any impact on private wealth is likely to be marginal, which should mean another good year for private bankers focusing on Islamic investors of high net worth.

Although many Gulf Islamic investors appear to have an appetite for risk, the stock market correction has resulted in some seeking capital protected products, which raises challenging Shariah compliance issues. There can of course be no guarantee for investment Mudarabah deposits with Islamic banks or conventional banks offering Islamic "windows," as the aim of Mudarabah contracts is to justify reward through risk-sharing. For equity investments there are no contractual obligations after the initial share purchases, the risk being entirely borne by the investor, rather than shared with entrepreneurial partners. Consequently, seeking capital protection in equity markets can be viewed as permissible, including even the use of derivatives to provide the protection, as the Shariah concern is with trading derivatives far removed from the underlying assets.

Purchasing a "put" option with the intention of buying the stock can be compared with the Islamic contract of Arboun, a deposit for the delivery of a specified quantity of a commodity on a pre-determined date. The new Shariah compliant capital protected funds offered in 2006 all referred to Arboun

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Global Islamic Capital Markets *(continued...)*

contracts. Options and futures contracts cannot be traded under Shariah, as they are too remote from the underlying assets, but that is not to say they can not be purchased, with the investor enjoying a constant, if not increasing, financial reward. The central issue is the nature of the contracts themselves. There is inevitably a relationship between risk and return, which Islam does not see as problematic, but rather an inevitable consequence of the real world with its business cycles. The concern in Islam is with gharar (contractual uncertainty) but not with trying to eliminate other uncertainties, such as those in equity markets, which are inevitably a fact of life.

Islamic securities markets

Trading in Sukuk or Islamic securities was largely confined to Kuala Lumpur until recently, but the last year has seen the start of significant Sukuk trading in the Gulf, a development that is likely to become of increasing importance in 2007, as Dubai and Bahrain compete to become the leading global market, Kuala Lumpur's potential role being limited by the Sukuk being local currency denominated, which deters international investors. Sukuk are the Shariah compliant counterpart of conventional bills, floating rate notes and bonds, the pre-requisites for Shariah acceptability being that they must be asset-backed and structured using an Islamic financing instrument so that there are no riba payments. The most popular and standardized structure is based on Ijarah contracts, which makes the Sukuk equivalent to a floating rate note in terms of its financial characteristics. The majority of new Sukuk issuance in 2006 was of this type, the main alternatives being Salam and Murabahah Sukuk, which yield a fixed return, the former typically for three months, corresponding to a treasury bill, while the latter, usually running from three to seven years, corresponds to a bond. It was the Bahrain Monetary Authority (renamed as the Central Bank of Bahrain in 2006) that pioneered Salam Sukuk five years ago, and in 2006 there were two further offerings worth US$40 million each and paying 2.34%, a similar rate to that on the Central Bank's conventional treasury bills.

Sukuk issuance has increased substantially over the last six years, and 2006 was a record year, with over 170 new Sukuk issues worth over US$27 billion. The year started with the then world's largest ever Sukuk, which was worth over US$3.5 billion. The issuer was the Dubai Ports Authority and DPI Terminals and the managers were Dubai Islamic Bank (DIB) and Barclays Capital. The issuance was to finance Dubai Ports' take-over of P&O Ports' worldwide interests. The Sukuk was based on an innovative Musharakah structure, with the investors receiving certificates of partnership giving them a pre-determined share of any profits or losses, the actual profit distribution being linked to performance indicators. Hitherto most of the large Sukuk issues had been managed by international banks such as HSBC Amanah and Citigroup, but DIB has tried to diversify beyond its retail banking business in recent years, and this deal marked a turning point in its investment banking operations. Partly as a result of its business diversification strategy, DIB enjoyed a 26% rise in profits in 2006, with gross profits amounting to US$600 million, and the value of its assets rising to over US$14 billion. Net profits after dividends to shareholders and profit-sharing with depositors rose to US$280 million, and the attractive product offerings to customers resulted in a 60% rise in deposits to US$11.24 billion.

"The majority of new Sukuk issuance in 2006 was Ijarah contracts with the main alternatives being Salam and Murabahah Sukuk"

Subsequently, DIB was able to build on its experience as a Sukuk manager to win the mandate later in the year – again with Barclays Capital – for the largest ever Sukuk, that issued by the Nakheel Group of Dubai, the second largest construction and development group in the Middle East after Emaar, also of Dubai. The Nakeel Group Sukuk was valued at US$3.52 billion, used an Ijarah structure and the variable returns were benchmarked to LIBOR, as is usual with Ijarah Sukuk, the actual return being LIBOR plus 120 basis points. However, to make the financing cheaper for Nakheel, and to add an incentive for investors, holders of the Sukuk certificates will have the right to buy shares at a discount in any Nakheel Group initial public offering (IPO). As the Nakheel Group is developing The Palm, there is likely to be an IPO during the three years of the Sukuk issuance as the group seeks to replace debt capital with equity. The Sukuk therefore provides medium-term bridging finance for Nakheel, and at the same time delivers what could be regarded as captive investors for any future IPO, which should undoubtedly help to ensure that any new equity offered is fully subscribed.

Dubai as a market for Sukuk

As the Nakheel Sukuk has been listed on the Dubai International Financial Exchange (DIFX), investors are able to sell their certificates at any time. The value of the certificates will depend on the rating of the issuer, which reflects Nakheel's ability to meet its financial obligations, the probability of an IPO and the expected terms and the period to maturity. Assuming Nakheel is able to meet its commitments, certificate holders should receive the nominal face value of their holdings in 2009 when the Sukuk matures, but in

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Global Islamic Capital Markets *(continued...)*

2007 and 2008 the market value could vary significantly from the maturity value. The major risk for Sukuk holders is that there is a major correction in the real estate market in Dubai in 2007, and therefore a downgrading in the value of Nakheel. As there is a substantial amount of new residential and commercial property coming onto the market in 2007, estimated by some to be as much as one-fifth of the total property stock, the risk of a downturn is real. However, real estate analysts have made gloomy predictions in previous years that have proved unfounded, and Nakheel itself has become more international in terms of its operations, and therefore less dependent on Dubai.

"There have been no defaults on any Sukuk, but it is likely that 2007 could see the first ever default"

There are good prospects for a rapid expansion in Sukuk trading on the DIFX in 2007, not least because with Gulf equity markets likely to continue to be volatile, the demand for Shariah compliant liquid instruments with a defined maturity value is anticipated to be strong. Furthermore, the Dubai Ports and Nakheel issues are only the start for high value Sukuk, as DIB itself has announced its intention of raising US$11 billion through a Sukuk issuance in 2007, partly to fund its ambitious expansion plans in Pakistan and elsewhere. Aldar Properties of Dubai has also announced plans for a Sukuk worth US$3.5 billion, and the Dubai Civil Aviation Authority plans for a Sukuk worth US$1.64 billion.

The real test for the international credibility of the DIFX will, however, not come from trading local Sukuk issuance, but rather that of Saudi companies. The Al Marasi Company of Saudi Arabia is planning a Sukuk worth over US$1 billion, which will be Saudi riyal denominated, and Aramco and Conoco Phillips of Saudi Arabia are planning US dollar denominated Sukuk issuance, the latter to be managed by Riyadh Bank, but it remains to be seen whether either Sukuk will be listed and traded in Dubai. The most likely listing could be by SABIC, the Saudi Arabia Basic Industries Corporation. SABIC issued a riyal denominated Sukuk for US$800 million in 2006 which was managed by HSBC Amanah of Dubai, and it is looking to raise a further US$4–6 billion through Sukuk and Islamic financing in 2007 in order to part-finance the construction of the Saudi Kayan Petrochemical Complex on the Gulf coast near Jubail. This will be one of the world's largest petrochemical complexes, costing over US$10 billion. If some of this is financed through traded Sukuk, this may help to lower financing costs, as investors in the Sukuk will accept a lower return if their assets are liquid. As DIFX has been accepted as a correspondent member of the World Federation of Exchanges, and since June 2006 has been an affiliate member of the International Organization of Securities Commissions (IOSCO), it has a unique status in the Gulf, which should help its aspiration to become the region's preferred trading exchange.

Malaysian Sukuk listings

While Sukuk trading in the Gulf is new, trading in Kuala Lumpur dates back over a decade, although the market is essentially domestic, with most of the issuance local currency denominated. Rantau Abang Capital had two major Sukuk issuances in 2006, the first being worth US$790 million and the second US$2.6 billion, both managed by Malaysia's leading investment bank, CIMB. These Sukuk were based on Musharakah partnership structures involving profit and loss-sharing. Other Malaysian Sukuk have been based on Murabahah mark-up structures, notably that by Bank Pembangunan Malaysia – worth US$921 million – and the Sukuk for Putrajaya Holdings – worth US$578 million. Although the Malaysian market continued to account for the largest number of Sukuk issuances by volume, it has been overtaken in 2006 for the first time by the value of Sukuk issuance in the UAE. Given the issuances in the pipeline, the lead of the UAE is set to increase in 2007.

Malaysia may also lose out to other markets in 2007, notably to Singapore, which has aspirations to become a center for Sukuk trading as part of its bid to become the international Islamic financial hub of South-East Asia. Singapore is well positioned to play this role as an international financial market for conventional instruments, with most trading in US dollar denominated securities. Singapore has only a small local Muslim community, and therefore offers little scope for Islamic retail products such as the managed Sukuk funds offered by RHB Bank in Malaysia, but it has the potential to serve as an inter-bank market for Sukuk. The Monetary Authority of Singapore, which has been an enthusiastic participant in several recent Islamic finance conferences, is keen to see the island play this role, as it helps diversify product offerings and attract new classes of investors, notably those who wish to be Shariah compliant.

Malaysia's Labuan International Offshore Financial Center also has ambitions to be a trading centre for Sukuk, but although there are now 31 instruments listed, with a market capitalization of US$13.5 billion, trading is limited, and some of the issuance is of investment funds rather than Islamic notes and debt securities. Most of the listings are of Malaysian rather than international securities, and the anticipated business from nearby Brunei never materialized, the latter preferring to maintain its links with Singapore, to which its currency is pegged. Labuan is to unveil a re-branding strategy in 2007 to help boost its position, but it

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Global Islamic Capital Markets *(continued...)*

is unclear what its real rationale is, apart from offering tax advantages to Malaysian companies and dollar rather than Malaysian currency issuance. The government of Brunei's first ever sovereign Sukuk in 2006, worth US$96 million, was denominated in Singapore dollars and largely taken up by local banks, as well as some Gulf investors hoping that the Singapore dollar might appreciate against the US dollar.

To date there have been no defaults on any Sukuk, but it is likely that 2007 could see the first ever default, opening the possibility that some Sukuk might fall into the "junk" bond category. The prime candidates for this dubious distinction are the Sukuk issued by Peremba Jaya Holdings, valued at RM200 million (US$57.04 million). These Sukuk were downgraded by the Malaysian Rating Corporation (MARC) in February 2006 and there was a further downgrade in December to BBB- grade with a negative outlook. Peremba Jaya is the developer of precinct 11 in Putrajaya, but because of a weak financial position its construction subsidiary, Arif Cerah, was served with a termination notice by Putrajaya Holdings, the governmental organization managing the development. As the proceeds from the government contracts are the ultimate repayment source for the payment of the Sukuk investors, Peremba Jaya Holdings is unlikely to be able to meet its commitments unless it can convince Putrajaya Holdings to lift the termination notice, which seems unlikely. If the Sukuk holders take Peremba Jaya Holdings to court it should provide a precedent to determine exactly what their rights are to the underlying assets. Given the complexity of the contractual arrangements, however, it could take years for the legal outcome to be known.

Gulf–South East Asian links

There was much talk of increasing Shariah compliant financial links between the Gulf and South-East Asia in 2006, despite some differences in interpretation of what is acceptable under fiqh by the more liberal Shafi'e School of Islamic jurisprudence that prevails in Malaysia and Indonesia and the more conservative interpretations of fiqh in the Gulf. These differences did not preclude Islamic banks from the Gulf seeking to expand in South-East Asia, with Al Rajhi Bank of Saudi Arabia – the largest retail Islamic bank in the world – opening nine branches in the Klang Valley surrounding Kuala Lumpur. Al Rajhi Bank was originally given a license to operate in Malaysia in 2004, but it was only two years later that its expansion plans were clarified. The issue for 2007 will be whether it can expand through organic growth; or whether it will seek to take over an established Malaysian Islamic bank. It is not clear whether Bank Negara Malaysia would permit such a foreign takeover.

Kuwait Finance House (KFH) also obtained a license from Bank Negara Malaysia to operate in Malaysia, but so far it has focused on putting the plans in place to develop a piece of real estate it was granted by the government of Malaysia in the Golden Triangle in downtown Kuala Lumpur. The intention is to build luxury serviced apartments for sale to Kuwaitis and other Gulf Arabs who wish to acquire a second home in a lush tropical environment very different from the deserts of Arabia. To finance its expansion in Asia, KFH launched a real estate fund in July 2006 worth US$250 million to invest in both commercial and residential property, including the Kuala Lumpur project. KFH anticipates that the return to investors should be between 8% and 10% for the five-year life of the fund. Reimbursement at the end of the five-year period will be covered by the sale of the assets once construction is completed.

Of course, not all the traffic is one-way from the Gulf to South-East Asia, as some flows from the east to the west of the Indian Ocean. Maybank, Malaysia's largest conventional bank, opened an offshore unit in Bahrain in 2004. The bank offers Islamic "windows," although none have yet opened in the Bahrain branch. Of greater interest was the agreement between the Malaysian investment bank, CIMB, and Bahrain's Yusuf bin Ahmad Kanoo Holdings to distribute specialized Islamic investment products in the Gulf. These include managed equity funds and capital market instruments, as well as asset management, corporate banking and treasury services. Another significant development was the offering in April 2006 by Shamil Bank of Bahrain of its Shamil China Reality Mudarabah, the first ever Shariah compliant fund focused on China. Under an agreement with Shamil Bank, the Xuan Huang China Reality Investment Fund is to invest in residential, commercial and industrial property in prime locations in Chinese cities. The Mudarabah matures after four years, with an anticipated return to investors of 18% annually, which some believe may be hard to achieve, despite China's booming real estate sector.

The largest link-up of all involves Singapore real estate development company, CapitaLand, which is to raise US$630 million through a Shariah compliant fund. The finance is to be used for the development of a large site of 43,000 square meters of land in Bahrain, which has been designated Raffles City after the famous Singapore hotel and boutique shopping complex. The plan is for an integrated up-market residential and retail development, in which CapitaLand will invest US$800 million. However, CapitaLand only intends to retain a 20–30% share in the longer run, as it is placing a major share of the assets in the Shariah compliant fund, the aim being to attract external investment. The majority of fund subscriptions in 2007 are expected to come from the Gulf, although there may also be some indirect investment through Singapore, both from Islamic banks and Takaful (Islamic insurance) companies.

continued...

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RAM League Awards - Lead Manager Awards 2005 No.1 in Number of Islamic Deals, No. 3 in Issue Value, Islamic Deals

Kuala Lumpur Islamic Finance Forum
KLIFF 2005 Islamic Banking Awards - Most Innovative Islamic Financial Product

Project Finance International
PFI Awards 2005 - Bond Deal of the Year - Asia Pacific

Project Finance
Project Finance Asia (2005) - Project Bond Deal of the Year

FinanceAsia
FinanceAsia Achievement Awards 2005 - Best Domestic Securitisation/ Best Islamic Finance Deal

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AsiaMoney Domestic Bank Awards 2005 - Best Bond House

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Global Islamic Capital Markets *(continued...)*

Islamic investment banking

Most Islamic banks primarily serve the retail market, but with the development of equity markets in Muslim countries and the increase in Sukuk issuance, some have started to play an investment banking role. The Islamic financing affiliate of Commerce International Merchant Bankers, CIMB Islamic, is undoubtedly the leader in this field, as during 2006 it managed 36 Sukuk issues, accounting for almost 30% of the global Sukuk issuance, with the value of these operations exceeding US$7.5 billion. CIMB Islamic investment banking business includes Shariah advice on the structuring, documenting and trading of Sukuk securities, as well as advice on Islamic funds and Shariah compliant asset management. CIMB Islamic also provides Islamic debt fund services and can arrange commercial paper, medium-term notes and floating rate notes using an Ijarah structure, as well as syndicated Islamic financing.

CIMB Islamic has become the most experienced provider of Shariah compliant treasury services, with its short to medium-term facilities including negotiable Islamic debt certificates structured using Bai Bithaman Ajil (BBA) and Islamic Treasury Bills (i-TB) issued by the government of Malaysia. It also trades in Bank Negara Malaysia Negotiable Notes with tenure of up to six months, structured on a Bai Inah basis, as well as Islamic accepted bills, structured on the Murabahah principle. Its activities encompass the issuance and trading of Islamic commercial papers and it can make available to clients wanting medium to long-term investment instruments Bank Negara Malaysia Ijarah Sukuk notes and Islamic private debt securities.

During 2006 CIMB Islamic also developed Islamic financing facilities for share purchases and trading. These Murabahah margin financing arrangements use asset purchase and sales agreements secured on the underlying assets of the transaction. Finance is also available to finance purchases in Shariah compliant IPOs, shares made available through rights issues and preference shares, although the latter are unacceptable for most Shariah scholars in the Gulf. Further refinement and a greater use of these facilities is likely in 2007, further strengthening the CIMB Islamic position in Malaysian capital markets.

In the Gulf, international banks such as HSBC, Citigroup, Deutsche and UBS accounted for most of the investment banking business up until last year, including Shariah compliant investment banking, partly reflecting the limited capacity and experience of the local banks. However, as Gulf capital markets have developed, DIB made the strategic decision to enter the investment banking arena, initially in co-operation with a new Gulf entrant rather than an existing player, Barclays Capital, an institution with much investment banking experience elsewhere, notably in Europe and South Africa. DIB subsequently became the second largest arranger of Sukuk globally after CIMB, with issuance worth over US$3 billion in 2006. It has learnt much from this exposure, and although it may be premature for it to go it alone in 2007 without an external partner, this is certainly likely in the future.

Much of this review has focused on the Gulf and South-East Asia, as that is where most of the Islamic finance activity is concentrated, and will continue to be concentrated in 2007. Longer term however, Iran, Pakistan, and possibly Indonesia are likely to be much more in the news. These are all more populous countries; indeed Indonesia has the largest Muslim population in the world, although Islamic finance there remains in its infancy despite some official encouragement, with Islamic bank deposits accounting for less than 1% of the total. However, Iran is the country to watch. All its banks are Shariah compliant under its 1983 law, with Bank Melli being the world's largest Islamic bank. Despite US sanctions, the Iranian economy grew by 5.4% in real terms in 2006, and growth is predicted to exceed 6% in 2007. The Islamic Republic is increasingly confident politically, and this may be matched by increasing economic confidence, including in the Islamic finance arena, where it has already 23 years of experience.

The author is Director, Islamic Finance Studies, Durham University, UK.

Islamic Debt as the Global Propeller

By Badlisyah Abdul Ghani and Shamsun A. Hussain

Islamic debt is the real missing link in the Islamic finance industry, as at present the global regulatory legal framework has designed debt to be interest-based.

Differing regulatory and tax regimes, diverse legal frameworks and disparate banking rules all influence effective communication between Islamic financial centers and market players on how to manage the business. Complying with Shariah is the easy part of the industry; sorting out the intricacies of undertaking the Shariah compliant nature of Islamic debt is a more interesting challenge. As a result, Islamic debt transactions are not as cost-effective as they should be in many jurisdictions. Institutions in Malaysia and the Middle East have been trying to bridge this gap, and 2006 saw the largest number of Islamic debt transactions brought to the market thus far.

Some of the activity that has been seen in the market includes Malaysia's tax neutrality announcement in 2004, which has proven how critical the tax issue is to the development of the industry. After this announcement, the market share of Islamic debt securities shot up to more than 70% of Malaysia's total corporate bonds issuance. Singapore, a budding Islamic finance jurisdiction, also announced some tax neutrality when the country entered the industry. Many other jurisdictions have made similar proactive moves, including the UK, the US state of New York and Queensland in Australia. Tax neutrality allows Islamic banking products or debt securities to be treated in the same manner as their conventional counterparts. No extra tax or stamp duties will be imposed. Equity instrument contracts, whether conventional or Islamic, are similar. As a result, the development of Islamic equity is a lot simpler.

The success of the Islamic debt market will have a direct impact on the developmental success of the Islamic finance industry. Thus all Islamic finance players, including Islamic bankers, Shariah advisors or Shariah committee members, regulators and other key industry players must pay extra attention to issues other than Shariah, particularly tax, legal and regulatory frameworks, which will become a tipping point to the development of Islamic finance industry globally.

Background

A successful financial market requires all industry components to be present – debt market, equity market, banking industry, non-banking sectors (e.g. trusts, waqf, etc...), baitulmal and zakat. Some people argue that Islamic finance is all about equity instruments, not about debt instruments. Nevertheless, the same people will also agree that activities such as Murabahah sale (where the price is paid in the future) and Ijarah (where the purchase undertaking is in the future) are also Shariah compliant financial instruments. The Islamic finance industry will never be relevant and significant to the national economic agenda of a particular jurisdiction until all components of the industry are developed.

This article attempts to address the complexities in dealing with the challenging status of Islamic debt to be developed as a key component of a nation's Islamic finance industry and the financial market as a whole, operating on a par with, and being as convenient as, the conventional debt market. In this article, for the purpose of clarity, Islamic debt is defined to include all banking products, as well as Islamic fixed-income securities products.

Islamic debt?

"Debt" has always been interpreted to be loans with riba (interest), which makes any discussion on Islamic debt sound very odd indeed. All finance students and bankers have been trained in debt transactions based on riba.

Conventional debt is a financial obligation arising from borrowed monies that a customer takes from a financier/investor, while Islamic debt is a financial obligation arising from a plethora of trade relationships entered into between a financier/investor and a customer/issuer. Many Shariah principles can be used for this trade relationship, such as Murabahah (installment sale), Bai Bithaman Ajil (deferred payment sale), Ijarah (lease/hire), Mudarabah (partnership), Musharakah (joint venture), Inah (buy and sell transactions), Salam (forward sale), Istisnah (sale by order), etc... A loan can also take place under the Shariah principle of Qard – the only loan permissible under Shariah because it is interest free.

Why is the Islamic debt market important?

To determine how important the Islamic debt market is to the well-being and growth of the Islamic financial market, we must look at the composition of a successful and sound financial market. The debt securities market in developed countries such as the US or the UK is mature and is widely used as a means of fundraising. In the US, 72% of its fundraising is done via the debt capital market, which is worth about US$23.84 trillion, as compared to bank loans of US$9.34 trillion in 2005.

For emerging market countries, particularly Asia (excluding Japan) there was a 27% market share in 2005, which increased from 24% in 2004. On the other hand, in the

continued...

Islamic Debt as the Global Propeller *(continued...)*

Middle East, supposedly the home of Islamic banking, there was a mere 7% of total fundraising in the form of debt in 2005. Banking assets still dominate the Asian and Middle Eastern markets. In order to have a sound financial market, both these markets need to develop their debt capital market including their Islamic debt capital market.

Issuers will be more likely to tap the debt capital market to raise funding for projects and assets acquisition. Investors needs are becoming more sophisticated and they are demanding more debt securities products.

A debt transaction is not necessarily a loan transaction!

An Islamic debt transaction may be entered into to meet various requirements, arising from personal, business or societal needs. When someone plans to buy a home, a need to own a house is identified. A mature Islamic financial market should be able to facilitate this need effectively by providing an Islamic debt facility from an Islamic bank by way of a loan or by way of trade. Whether it is an equity participation or an interest-free loan or a trade, the Islamic bank's only purpose for undertaking the transaction is to facilitate the home buyer's needs. A debt transaction is not tantamount to an interest-bearing loan.

Islamic debt is critical to business and economy

Project finance, corporate finance and asset finance are all key business needs, and an Islamic banking practitioner must understand these key needs and understand how to optimally meet them. The optimum level objective plays a significant role in appreciating and understanding the applicability of Islamic debt transactions for a project or an investment. Below is an illustration:

Here, project finance is being contemplated. What would be the optimum financing model as far as debt to equity requires? First of all, the key consideration is meeting and matching the needs and objectives of equity investors and the needs and objectives of debt investors. Generally, equity investors are driven by return on equity (ROE). Certainty of ROE will be subject to performance of the project at residual level as it ranks junior to debt investors. At the same level of project Internal Rate of Return (IRR), ROE will be able to earn different return levels depending on composition of debt. At the same level of project IRR, the higher the debt level, the higher ROE is expected and vice versa. Any upside return on the project will go straight to equity investors. Thus, equity investors would be looking forward to have the lowest equity contribution to a project and have the highest portion possible on debt financing part.

Three cases below demonstrate the above scenarios:

Case A

Project Cost	100
Debt	90
Equity	10
Profit before Debt cost	15
Debt cost (i.e. ijarah rate - 10%)	9
Net Profit after Debt Cost	15-9 = 6

Based on the above, ROE to equity investors is **60%** (based on 6/10)

Case B

Project Cost	100
Debt	50
Equity	50
Profit before Debt cost	15
Debt cost (i.e. ijarah rate - 10%)	5
Net Profit after Debt Cost	15-5 = 10

Based on the above, ROE to equity investors is 20% (based on 10/50)

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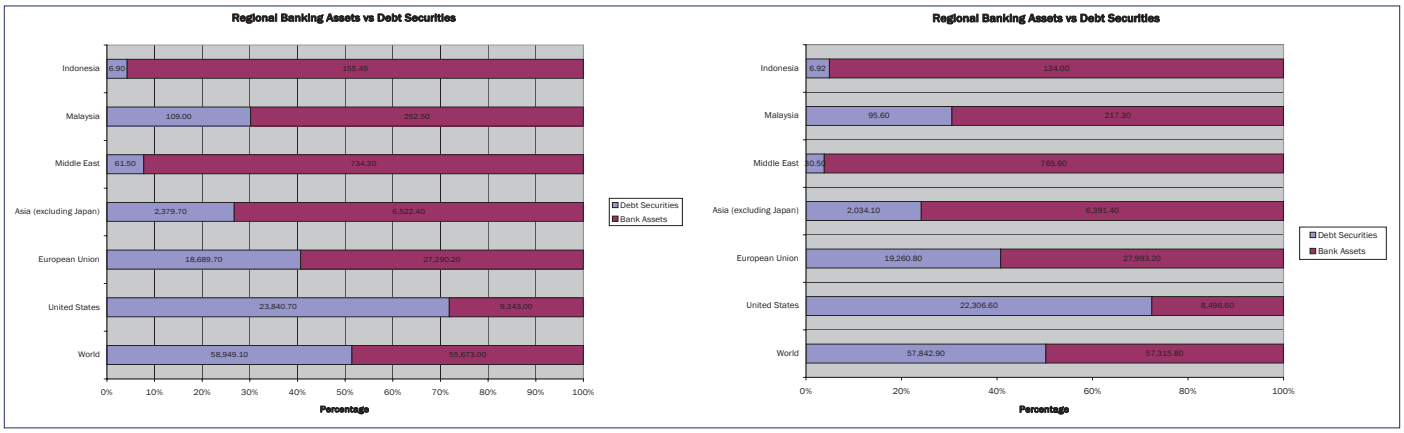
Diagram 1: Regional debt securities vs bank assets



Source: International Monetary Fund, Bank Negara Malaysia, Bank Indonesia, & Bursa Efek Surabaya

Islamic Debt as the Global Propeller *(continued...)*

Case B

Project Cost	100
Debt	50
Equity	50
Profit before Debt cost	15
Debt cost (i.e. ijarah rate - 2%)	5
Net Profit after Debt Cost	15-1 = 14

Based on the above, ROE to equity investors is 28% (based on 14/50)

Based on the above 3 cases, Case A will be the most attractive return to equity investors. Despite the fact that Case C has a lower Debt Cost i.e. 2% compared to 10% in A and B, C does not give the best ROE because of the low debt composition. Structuring a capital structure for a project will be based on the market condition of the debt market at one particular time. Assuming the above is the market condition the project promoter is facing, option A will be selected easily.

From the above scenario, if an effective Islamic debt market is absent many Islamic equity investors will not achieve an optimum ROE. The only way for them to achieve an optimum ROE is to opt for the project to be financed via Riba based financing, which will cause these Islamic investors to do something haram. If an Islamic debt market is effectively developed, business activities can be facilitated optimally.

Shariah flexibility

Shariah contract choices are available for any type of debt transactions and reaffirm that Shariah is the easiest thing to deal with in the industry. Islamic banking practitioners across the globe deal with many different banking products but utilize only one Shariah principle, such as Ijarah. Ijarah can be used for hire purchase, for term financing and for leasing products. These three banking products, although using a similar Shariah principle, are treated differently in accounting treatments and risk-weighted capital ratios. A term financing can also be undertaken in the form of Murabahah, Bai Bithaman Ajil, Salam, Inah, Mudarabah and Musharakah. The accounting treatment and risk-weighted capital ratio in this case would still be the same as term financing using Ijarah, as the product is a term financing.

Term financing could be also structured as a floating rate financing. The same Ijarah term financing can also be done as fixed rate financing. Typically, a term financing under the principle of Murabahah, Bai Bithaman Ajil, Inah or Salam would be done as a fixed rate debt transaction but with some Shariah compliant techniques. These principles could also accommodate floating rate financing features, even though this would be slightly more tedious operationally. A Musharakah and Mudarabah can also be used for debt transactions as long as the identified underlying productive activity provides either a variable or fixed cash flow.

As can be seen from the above, Shariah is very flexible in addressing financial needs as long as riba is avoided. If we cannot apply Mudarabah, we could apply Murabahah or Bai Bithaman Ajil. If we cannot apply Musharakah because of the underlying nature of the financing requirement, we can always apply other Shariah compliant contracts such as Ijarah. For example, the acquisition of leaseable assets could be best structured in the form of Ijarah, but if a lease cannot be done due to the legal framework in the jurisdiction in question, then a Murabahah or Inah principle can be used.

Inah, Tawarruq and Commodity Murabahah

When we discuss Islamic debt transactions, we cannot avoid dealing with the hullabaloo of Inah transactions in several of the major Islamic financial markets including Malaysia. The alternatives to Inah are the Tawarruq and Commodity Murabahah which was developed and popularized in the GCC amongst the Islamic financial institutions there.

Though Commodity Murabahah has received wide Shariah endorsement in the GCC and in the western financial market, Tawarruq has not been fully accepted by some GCC Shariah advisors or Shariah committees as they would argue that Tawarruq is a sister of Inah. Commodity Murabahah as it is practiced in the GCC and western financial markets has not been approved in Malaysia, Indonesia and several other markets. Tawarruq is fully accepted in markets that accept Inah. If one accepts Inah, then one would definitely accept Tawarruq and vice versa.

The pertinent question is does everyone in the Islamic financial markets share similar meanings, understanding and usage of these three terminologies? To illustrate, below are the relevant meanings and usages:

Inah or Einah: Refers to a sale and a buy-back arrangement from the same party. Purchase Agreement Price is paid spot and Sale Agreement Price will be paid in the future by way of installments or one lump sum.

Example:
Ali wants to transfer his home financing from Bank A to Islamic Bank B. Since he owns the home, he will sell to Islamic Bank B at a price equivalent to redemption amount of Bank A. Islamic Bank B will subsequently sell the home to Ali at a price (including Islamic Bank B profit) to be paid by equal installments over the next 20 years.

Some Islamic home financings in Malaysia have been implemented under the Inah concept but most would carry Bai'

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Dar Al Istithmar
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Shariah advisory services and the role played by Dar Al Istithmar

In general, the principal objectives of **Shariah advisory services** would be firstly, to assess and evaluate whether a financial product or service, or business deal or contract, is in line with Shariah or not, and if not, how could it be made Shariah compliant.

In order to offer a comprehensive Shariah advisory service, the service provider would necessarily need to possess expertise in certain fields. These are listed in the table to the right, as are the ways through which these expertises have so far been obtained by the client financial institution:

Field of expertise	Typical mode of acquiring this expertise, until the present
Sharia law and Islamic jurisprudence (in particular of commercial affairs or **mu'amalaat**)	From direct contact of conventional finance experts with Sharia scholars: Process is often time-consuming, **due to lack of "bridge of understanding"** and limited overlap of expertise between the two parties
Technical expertise, in the workings of the **conventional finance** in general, and specifically with regard to the proposed Sharia compliant product's parallel conventional version (if a parallel exists, as it usually does)	By conventional financial experts, with little or no background in Islamic law
Knowledge of **Islamic banking and financial standards**, to ensure the product follows the established standard	Again through an imperfect and evolutionary mechanism of "learning while doing", by the concerned parties. The imperfection exists as the current (presently non-binding) standards such as the AAOIFI Sharia standards and knowledge of industry practice are often not (well-) known, especially by conventional side.

The necessary "bridge of understanding" referred to above has so far, largely, been sought to be provided by conventional financial experts, who, based on their contact with the Islamic scholars, gradually build up a patchy and barely functional understanding of only certain very specific Shariah rulings through a very slow process of hit and miss.

As a natural consequence, the overall process of developing Islamic financial products has been slow, unplanned, and frankly, inefficient – and has hindered the pace of development, innovation and progress in the Islamic finance industry as a whole.

In order to meet the ever-increasing demand for a consolidated and efficient Shariah advisory service provider, **Dar Al Istithmar (DI)** entered the market recently in 2004.

DI has made stunning progress over a very short period of time, and is increasingly being regarded as the standard-bearer of a new genre of Shariah advisory and Islamic consultancy firms, which can provide all of the above services in a very efficient, streamlined, and compact manner. It is no surprise that in addition to achieving general and widespread recognition, **DI** also won the **Euromoney** award for "Best Islamic Assurance and Advisory Services" for two years running, in 2006 **and** 2007.

DI is able to fulfil this role based on the strength of its staff who possess specialised expertise in all of the relevant fields of Shariah law, conventional financial technical expertise, and knowledge of Islamic financial standards.

It is specifically this dual expertise of DI's team i.e. knowledge of Shariah law as well conventional technical / financial know-how that **enables DI to form a solid bridge of understanding** between the Islamic scholars and the financial world. The DI team profiles can be viewed at http://www.daralistithmar.com.

In addition to the proficiency of the **DI** team, **DI** has a full-time Shariah Supervisory Committee (**SSC**) comprising five of the best-known and highly skilled, and hence highly respected, Islamic scholars across the Islamic financial world:

- Dr Hussain Hamid Hassan (Chairman of **DI's** SSC) - Egypt
- Dr Abdus Sattar Abu Ghuddah - Syria
- Dr Mohamed Elgari – Saudi Arabia
- Dr Ali Al Quradaghi – Qatar
- Dr Mohd Daud Bakar - Malaysia

DI works very closely with its Shariah board throughout the whole process of development of all of its Islamic financial products and services, and all Fatawa (or Shariah approvals/ratifications) of products are achieved only after the Shariah board has properly understood the working of the concerned product and its rationale, and has decided that it is acceptable from a Shariah viewpoint.

All of **DI's** clients would therefore automatically have access to DI's highly competent SSC (by virtue of using DI's as a Shariah advisor), and clients would not need to deal with the extremely cumbersome and financially challenging task of putting together and then maintaining a Shariah board itself. This is another major advantage of using **DI's** services.

Moreover, since none of DI's scholars are among the board of directors for **DI**, conflict of interest is also avoided, thereby increasing the investors confidence in the financial product or service.

Thus, **DI** is a very competent and fully contained **"one-stop shop" for all Shariah advisory services.**

At present, it is a fact that very few firms like **DI** exist, and that **DI's** entry into the market represents a very much needed and long-awaited development.

It is firmly believed that the future will witness a concerted move towards the **DI**-model of service provision by other providers (both existing and new) of Shariah advisory services, to achieve the much desirable goals of efficiency, excellence, and compactness in one go.

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Islamic Debt as the Global Propeller *(continued...)*

Bithaman Ajil label. But not all Bai' Bithaman Ajil is necessarily Inah. During the 1990s, Bank Islam Malaysia offered Islamic home financings that included developers in the whole legal documentation process. After a sale & purchase agreement had been executed by an Islamic home financing client, the Bank would enter into a novation agreement with the developer. Then, the Bai' Bithaman Ajil agreement would be entered between the bank and the client. Other than home financings, South-East Asian Islamic financial institutions also practice Inah for other Islamic financing segments including business banking and corporate banking clients.

Tawarrukh: Always refers to "Tawarrukh Al-Munazzam", which means Tawarrukh with pre-arrangement. Legal documentation reflects the full flow of funds including the ultimate utilization. As such the control to ensure that the fund raised is utilized for Shariah-compliant purposes can be identified upfront.

Example:
Islamic Bank C plans to provide term financing-i to a corporate client. Islamic Bank C will take an undertaking or the pre-arrangement with the corporate client and purchase a commodity from a commodity vendor. The commodity will be subsequently sold to the corporate client with the price to be paid in the future through installments or one future lump sum. Immediately, the corporate client will sell the commodity back to the same vendor or another vendor at spot/cash price. But the whole arrangement is made upfront. By the closing of the transaction, the corporate client receives cash for business expansion or to fund operating expenses.

However, some GCC Islamic banks or Shariah advisors do not accept this type of contract or legal documentation that reflects the full monetization process of the commodity.

Commodity Murabahah: This concept is always referred to as "Tawarrukh bi ghaira Munazzam" which means Tawarrukh without pre-arrangement. This concept is used for Islamic treasury placements and Islamic deposit products with Islamic banks or conventional banks. It is better known as Commodity Murabahah not Tawarruq to differentiate from "Tawarrukh Al-Munazzam".

Example:
Islamic Bank D wants to place short term money i.e. US$1 billion for a right return. Islamic Bank D enters into Commodity Murabahah arrangement with either an Islamic Bank E or XYZ Conventional Bank. Say Islamic Bank D decides to place with Islamic Bank E. Typically Islamic Bank E would need to match the liability it obtained from Islamic Bank D with the right Islamic assets. Islamic Bank E has 2 options whether to use the liability to finance its own Islamic assets or to make an interbank placement or investment in the form of Commodity Murabahah in XYZ Conventional Bank or any other Islamic Bank or conventional bank. Assuming that Islamic Bank E decides to place the same funds it received from Islamic Bank D on a back to back arrangement with XYZ Conventional Bank because the Islamic assets for Islamic Bank E is limited and they are pressured to provide the right return to Islamic Bank D. XYZ Conventional Bank, in its ordinary course of business, invests in interest-bearing loans or Riba instruments. Since the identification of purpose is not required under Commodity Murabahah documentation in some parts of the world, this type of transactions flourishes there.

It has always been argued that since the commodity Murabahah documentation only reflects at the commodity trading level without identifying issues as to what the funds will invest in or how it will be reflected in the conventional banks' balance sheet, certain Shariah boards outside of Malaysia have approved. Below is the illustration.

Balance Sheet of XYZ Conventional Bank

Assets	Liabilities
Riba Instruments US$1 billion	Commodity Murabahah Deposits US$1 billion

At the documentation level, the above relationship might not be identified. However, at balance sheet level, the issue of financing riba instruments by Islamic deposits can easily be established.

Under Malaysia's Islamic Banking Act 1983 and under the excellent and able supervisions of the Central Bank and the Securities Commission, the above arrangement whereby the funds goes to XYZ Conventional Bank and be utilized in riba based transactions has never been allowed and will never be allowed. The Act states clearly that all Islamic banking and finance transactions must not contradict Shariah and it clearly states riba is prohibited directly or indirectly. It must be noted that Inah, Tawarruq and Commodity Murabahah can be done and are being done in Malaysia subject to the Act.

At the end, we may conclude that Tawarruq and Inah is in the same family. The Tawarruq can involve 3, 4 or even 100 contracting parties and it will still continue to be akin to Inah. Unfortunately, both do not seem to be practiced widely in the Middle East particularly the GCC as the market has used Commodity Murabahah for the last 40 years to facilitate practically all their Islamic banking and finance activities. The main beneficiaries of this product are the conventional financial institutions as it facilitates riba based financial transactions using Islamic funds. One of the main reasons why the GCC markets still see a lackluster secondary market for its nascent Islamic debt market is attributed to the existence of Commodity Murabahah in that market as it is currently practiced.

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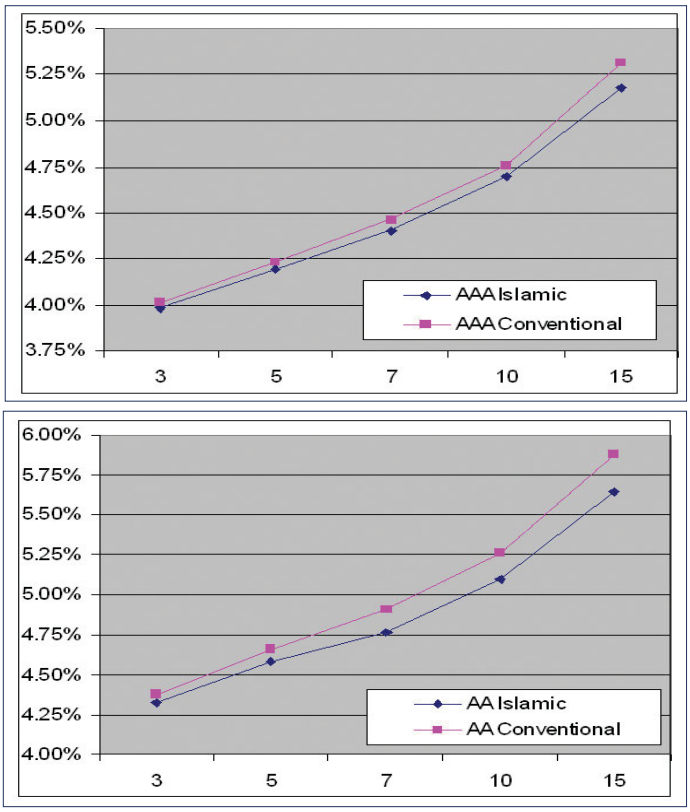
Islamic Debt as the Global Propeller *(continued...)*

The compelling need for Islamic debt

The faster the Islamic debt segment develops, the faster the whole Islamic finance industry will grow – in terms of domestic markets and at a global level.

One only has to look at the development of Islamic debt securities in Malaysia to obtain an insight into how compelling the need for this market is. Traditional Islamic banking products might not be able to reflect the commercial benefits directly to investors and fundraisers or issuers alike. However, Islamic debt securities (or to use the more popular label, Islamic private debt securities) have provided portfolio investors as well as fundraisers with better deals. As a result, both sides would make Islamic debt securities issuance the most cost-effective and the most profitable proposition. This dimension is reflected in the following chart of historical record.

Diagram 2: Yield to issuers



The Malaysian market has been able to achieve the above impact due to its properly regulated Shariah management. We have not seen comparable development in the US dollar market or in the GCC markets as yet. In Malaysia, which is driven by the Islamic Banking Act 1983, Islamic banks or windows will not place funds with conventional banks either in the form of Mudarabah or in the name of commodity Murabahah. As such, Islamic funds are fully circulated in the Islamic financial system and thus create a real demand for Islamic fixed income securities, especially in the secondary market. This rule has allowed issuers and investors to benefit, while by default developing the Islamic debt securities market and ultimately the whole Islamic finance industry.

Diagram 3: Illustrates the return of Islamic papers vs. conventional papers

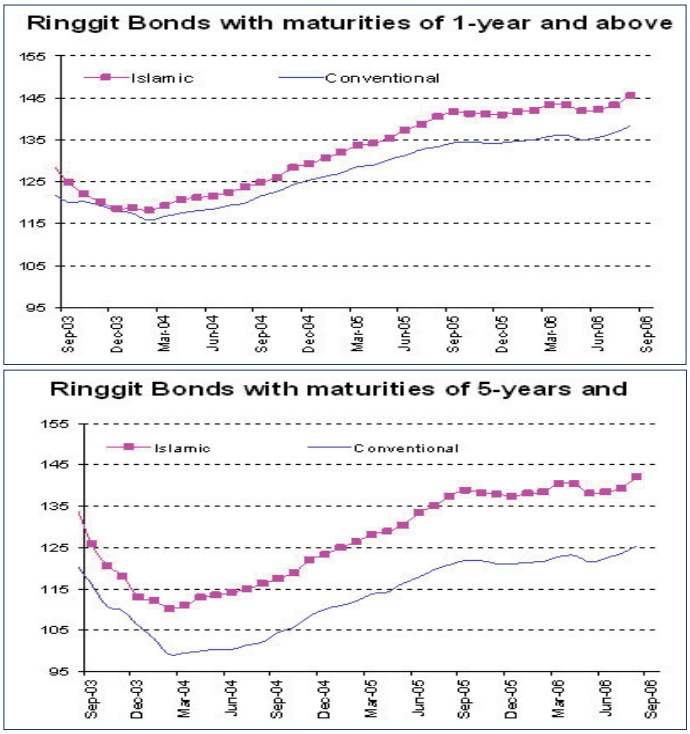
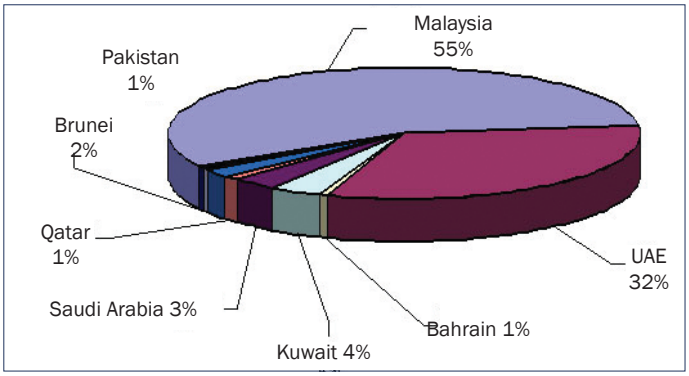


Diagram 4: Global Sukuk issued



Conclusion

Islamic debt instruments, whether in the form of banking products or securities products, must be looked at as the ultimate propeller to develop the Islamic finance industry globally. Recognizing and addressing the challenges faced by Islamic debt implementation will create a new platform for growth.

CIMB ISLAMIC

The authors are the chief executive officer/executive director and director, debt market and corporate finance, respectively, at CIMB Islamic Bank.

Islamic Capital Market Growth and Trends

By Baljeet Kaur Grewal

In an internationally seamless and interconnected financial world, Islamic finance has made headway and continues to expand within a global context. No other financial industry, market or jurisdiction in the last decade has witnessed the staggering financial engineering and innovation of the Islamic finance industry. The extensive assortment of global Islamic products available today not only accentuates the expansion of Islamic finance as a popular financing mechanism, but more crucially it underscores the sustainability of the industry.

It should be recognized from the outset that the Islamic capital market in Malaysia is an essential element of the capital market as a whole. Within a broader context, Islamic finance has effectively functioned as an alternative market for capital seekers and providers, at the same time playing an important complementary role to the Islamic banking and Takaful industry. In short, the broadening and deepening of the Islamic financial market in this country has all three strategic pillars: i.e. banking, Takaful and more distinctively, the capital market. The Islamic capital market complements the conventional market by providing value-added services that meet the needs of the market for a broad range of instruments, and has effectively mobilized and channeled funds to fuel economic growth.

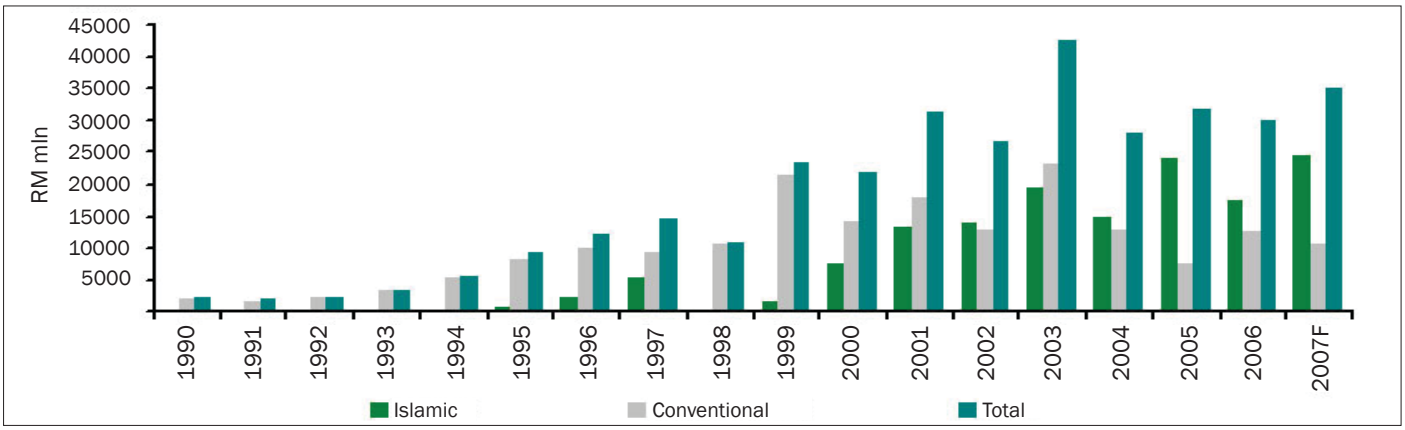
One crucial challenge and pre-requisite to the growth of the Islamic market has been the inculcation of market awareness and understanding of its varied investment opportunities, contributing to the diverse stages of progression in Islamic finance in various parts of the world. Given the rate at which this industry is growing, no global operator targeting clients or businesses can afford to ignore this market without suffering a loss in market share, a loss in global competitiveness, or a foregone opportunity loss.

"For Islamic capital markets to remain competitive, attractive and innovative, indigenous Islamic financial products must be introduced to meet the risk/reward profiles of investors and issuers"

The Islamic capital market accounts for a large proportion of the private debt securities (PDS) market in Malaysia. In the last eight years, the composition of Islamic fixed rate securities has grown unabated and increased in significance (see chart 1). Demand for domestic Islamic debt instruments, which accounted for only 7% of total bonds raised in 1999, grew to 25% in 2000 and subsequently to 58% of total new corporate debt issued in 2006, primarily due to investor awareness of alternative funding sources, i.e. Islamic instruments and the increased number of Islamic funds launched over the years. No less than 53% of outstanding domestic bonds are now Shariah compliant, especially the larger issues, and this proportion continues to grow. The result is that Malaysia's Islamic financial landscape has advanced in terms of diversity of instruments and in terms of its modernity, as well as boasting a dual banking model whereby a developing Islamic financial system exists in parallel to the conventional banking system. To chart the growth of Islamic fixed income securities, total Islamic PDS (IPDS) issued since 1991 (matured and

continued...

Chart 1: Malaysian PDS market (1990–2007F)

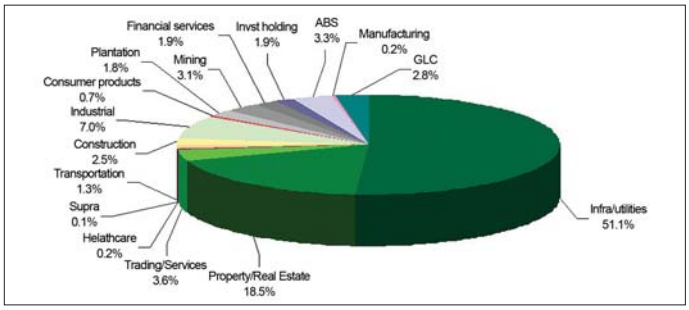


Source: BNM/FAST, RAM, MARC, KFH

Islamic Capital Market Growth and Trends *(continued...)*

outstanding) amounts to RM165.2 billion (US$47.18 billion) at 380 issues. In terms of total number of IPDS issued, the infrastructure/utilities and property/real estate sectors dominate at 51% and 19% respectively, given the large-scale nature of these projects (see charts 2 and 3).

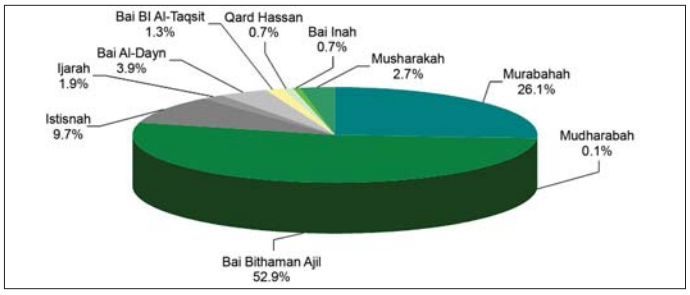
Chart 2: Total value of Islamic corporate bonds issued and rated by sector, as at December 2006 (Malaysia)



Source: BNM/FAST, RAM, MARC, KFH

* Statistics include total of IPDS rated and issued to date (matured and outstanding).

Chart 3: Total value of Islamic corporate bonds issued and rated by instrument type, as at December 2006 (Malaysia)



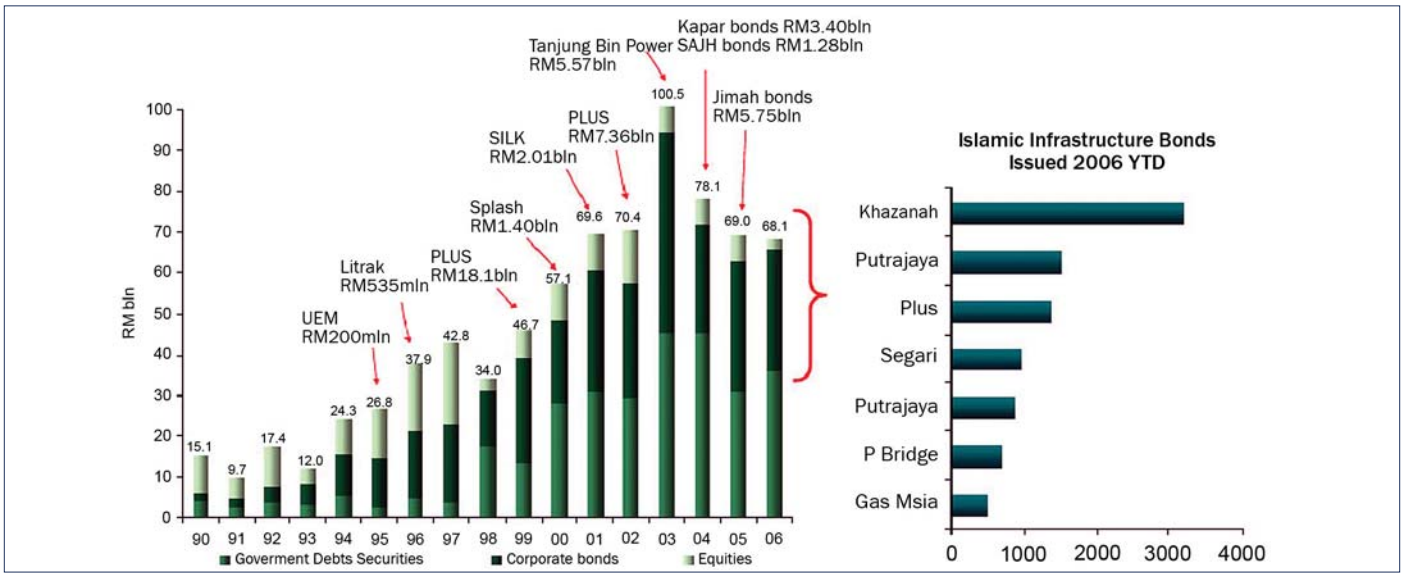
Source: BNM/FAST, RAM, MARC, KFH

In 2007, the Malaysian bond market is expected to continue its aggressive stance with an estimated RM35 billion–RM40 billion (US$10 billion–US$11.42 billion) worth of new debt to be issued, of which 80% of the bonds are expected to be Shariah compliant. A large proportion of these new bonds will be channeled to finance infrastructure projects, given the implementation of the Ninth Malaysian Plan. Project financing via the Islamic route has gained impetus since the late-1990s; some notable projects include the Putra–Star LRT (RM1 billion (US$285.57 million) Istisnah financing), Putrajaya Holdings (RM2.2 billion (US$628.17 million) Sukuk), SAJ Holdings water project (RM680 million (US$194.16 million) Sukuk), toll road operators, as well as other infrastructure and utilities players (see chart 4). The thrust of the Ninth Malaysian Plan will continue to drive demand for Islamic project finance structures, specifically in the areas of infrastructure financing for water projects, education, healthcare, roads, etc...

Meanwhile on the global Sukuk front, new Sukuk issuance stood at US$16.81 billion in 2006, bringing the total amount of global Sukuk outstanding to US$57.4 billion (including local currency denominated Islamic bonds). Among notable varieties of new Sukuk issues were the inaugural Sovereign Pakistan Sukuk of PKR8 billion (US$130 million), Nakheel Development's US$3.52 billion property/real estate and the world's largest issue to date, PCFC Development FZCO's US$3.5 billion (ports/shipping) and SABIC's SR8 billion (US$800 million) in basic industries. For 2007, we expect new Sukuk issuance to move still higher to US$18 billion, dominated largely by huge infrastructure/utilities, property/ real estate and oil and gas financing in Malaysia and GCC countries.

continued...

Chart 4: Malaysia's Islamic infrastructure deals (1990–2006)



Source: BNM/FAST, RAM, MARC, KFH

Islamic Capital Market Growth and Trends *(continued...)*

So why are Islamic bonds becoming increasingly popular? The advantages fundamentally lie in the structure of Islamic finance itself. Islamic bonds provide an avenue for Islamic investors to invest in Shariah compliant investments, thus guaranteeing access to a larger investor base, as well as providing potential lower pricing to issuers via the wider investor pool from the participation of large Islamic investors. Structures employed have also evolved from the traditional Bai Bithaman Ajil (BBA) structure to include more project-specific transactional structures such as Istisnah, Ijarah Sukuk, Musharakah or a combination of the above.

"Strategic partnerships between domestic players and foreign Islamic institutions are imperative for the domestic Islamic industry to face the currents of globalization and change"

By this measure also, Malaysia stands to gain given its multi-faceted approach to Islamic banking. A deep and liquid debt capital market, thriving Takaful and banking sectors, combined with sound regulatory support bode well. The entry of foreign Islamic institutions to the marketplace has also been critical in accelerating liberalization as Malaysia becomes an Islamic financial hub. Among the advantages of foreign participation are globally acceptable Shariah compliant Islamic debt and equity structures, research and development in product development, a knowledge pool of resources and human capital, and more crucially access to GCC investors and their vast funds.

For Islamic capital markets to remain competitive, attractive and innovative, indigenous Islamic financial products must be introduced to meet the risk/reward profiles of investors and issuers, fulfilling all the tenets of the Shariah while remaining sufficiently cost effective and competitive vis-à-vis conventional products. By confining product development to mere evaluation and adaptation of products in the conventional markets, the Islamic capital market will have to play a perpetual catch-up game with the conventional financial system. There will also be a continuous reliance on the expertise in the conventional market in order to take the Islamic capital market forward.

As such, strategic partnerships between domestic players and foreign Islamic institutions are imperative for the domestic Islamic industry to face the currents of globalization and change.

Nevertheless, like all financial mechanisms that are in emerging stages of development, the Islamic industry poses some overreaching challenges. The main hurdle identified is in accessing long-term investors and ensuring the sustainability of the Islamic industry – which can be mitigated by a greater understanding of and familiarity with Islamic structures and a wider skill base. Further to this, creating a deep and liquid secondary market for Islamic instruments through the enhancing of risk management tools and the innovation of new products will ensure that standards remain adaptive and effective in riding the evolutionary waves of financial innovation. The nature of project finance itself, which requires large funding, will enable issuers to tap a wider pool of investors in Malaysia and abroad – simultaneously establishing sizeable Islamic markets and participants, leading to cheaper funding costs. The crux, however, is being able to structure a deal which is not only marketable, but is also able to secure a wide distribution network.

Further prospects exist for Islamic products in the areas of asset origination and asset management. Following on from the theme of innovation, structures that can be explored include the gradual shift to Istisnah, Ijarah and Salam based products, short-term oil and commodity linked products, equity/debt hybrids, as well as internationalizing distribution lines. Continuous research and development in the areas of product development can also enhance growth in Islamic equity funds, cultivate liquidity management of assets and create Shariah based equity benchmarks.

2007 will continue to see robust growth across global Islamic markets. Wide recognition of the need for a variety of shared institutions, as well as regulation to strengthen the industry will see qualitative improvements in terms of diversity and scope. "New" Islamic participants across various jurisdictions (Singapore, Thailand, Indonesia, China, etc...) will also come to the fore in deepening their respective markets and contributing to the development of the Islamic financial architecture.

Kuwait Finance House
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The author is director and chief economist at Kuwait Finance House (KFH) Malaysia. KFH is one of the largest Islamic banks in the world and the first Islamic bank with an Economic and Investment Research team.

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From,
The Chairman, Board of Directors,
Management and Staff of Kuwait Finance House & Kuwait Finance House (Malaysia) Berhad.

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Al Dar Money Market Fund

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Fund Manager Profile

- Al Dar Assets Management Company (ADAM) was set up as a Kuwaiti closed shareholding company on 6 April 2004. It is registered with the Central Bank of Kuwait as an Islamic investment company, with a paid-up capital of KD20m in April 2004. The company specialises in the vast and promising Islamic financial investment field. Besides that, ADAM is a member of the Investment Dar Co KSCC Group, which is one of the pioneering and leading institutions in Kuwait and in the region. It is also the group's investment arm.

Strategy

- The objective of the fund is to achieve competitive financial returns relative to returns from the conventional short- and medium-term financial instruments available in the Kuwaiti market. For this purpose, the fund is to be invested in instruments available in Kuwait and abroad.
- *The fund was previously known as Al Dar Investment Fund.*

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MARKETING ISLAMIC BANKING PRODUCTS
5-6 March 2007 * Malaysia

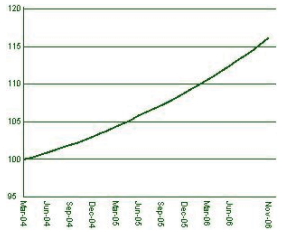
Statistics (as at November 2006)

Summary Data	
Annualised Return (%)	5.76
Best Monthly Return (%)	0.73
Worst Monthly Return (%)	0.23
2005 Return (%)	5.62
2006 Return (%)	6.72
Rise in NAV Since Inception (%)	16.10
Last 3 Months (%)	2.01
One Year Rolling Return (%)	7.29
Two Year Rolling Return (%)	13.18
Five Year Rolling Return (%)	n/a

Select Annual Risk Free Rate 4%

Risk/Return	
Sharpe Ratio (RFR = 4%)	4.20
Annualised Standard Deviation (%)	0.42
Downside Deviation (%) (RFR = 4%)	0.07
Upside Deviation (%) (RFR = 4%)	0.63
Sortino Ratio (RFR = 4%)	26.19
Maximum Drawdown (%)	0.00
Percentage of Positive Months (%)	100.00
VaR (90%)	0.31
VaR (95%)	0.27
VaR (99%)	0.19

Chart



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Performance Tables

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	YTD
2006	0.55	0.51	0.56	0.52	0.61	0.58	0.64	0.56	0.58	0.73	0.68	n/a	6.72
2005	0.43	0.38	0.48	0.40	0.43	0.58	0.43	0.43	0.42	0.46	0.51	0.53	5.62
2004	n/a	n/a	n/a	0.23	0.34	0.31	0.33	0.35	0.33	0.28	0.38	0.41	3.00

Manager Details

Management Company	ADAM
Advisory Company	Burgan Bank S.A.K.
Fund Manager	Mohannad Al-Mesbah
Director of Fund	Osama Al-Musslam, Fahad Albassam, Khalid Alshatti, Adnan Al-Musslam, Yousif Malallah
Investor Contact	Khalid Alshatti
Shariah Advisor	ADAM shariah board
Address	State of Kuwait, Sharq Area, Arraya Centre, Shuhada Street, 30th Floor, PO Box 27965, Safat
Country	Kuwait
Zip	13140
Website	www.adamco.com
Email Address	asset-inv@inv-dar.com
Telephone number	965 888866

Fund Details

Fund Size(US$m)*	49
Fund Capacity(US$m)	171
Firm's Total Asset(US$m)	5,000
Inception Date	Apr 2004
Domicile	Kuwait
Base Currency	KWD
Dividend Policy	No
Hurdle Rate	No
High Water Mark	No
Listed on Exchange	No
Fund Open Close	Open
Minimum Investment Size	3,000 (units of shares)
Subsequent Investment Size	1,000 (units of shares)
Benchmark	Local investment funds

Investment Details

Classification	Mutual Fund / Unit Trust
Investment Geography	Middle East/Africa
Industry Focus	All Sectors
Instruments Traded	Equity, Others

Fee and Redemption Structure

Subscription Frequency	7 days (every Monday)
Redemption Frequency	7 days (every Monday)
Redemption Notification Period	5 days
Lock-up	No
Leverage	No
Penalty	No
Other Fee(s)(%)	None
Management Fee(%)	1.5
Other Fee(s)(%)	0.125 (annual fees)

Service Providers

Auditor	Al-Fahad & Co, Deloitte & Touche
Legal Advisor	Al Markaz Law Center

Limitations

Debt to Equity Ratio	No
Return on Assets Ratio	No
Cash to Market Capitalisation Ratio	No
Income Interest to Sales Ratio	No

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The Next Generation in Islamic Financing

By Arul Kandasamy

It is no coincidence that a pre-IPO structure has been used for the two largest ever Sukuk (Nakheel Development – US$3.52 billion and PCFC Development – US$3.5 billion, both arranged by Barclays Capital and Dubai Islamic Bank). It is a unique structure that offers significant benefits to both borrowers and investors. In fact, not only is the Nakheel Development Sukuk the largest Sukuk ever executed, it was one of the largest convertible offerings ever executed globally.

The pre-IPO Sukuk has heralded a sea-change in investor perception of the Sukuk instrument and has been the single largest contributor to the growth of Sukuk issuance in 2006. As can be seen from the table below, global Sukuk issuance increased 120% from 2005 to 2006. Approximately 43% of 2006 Sukuk issuance was made up of pre-IPO Sukuk transactions.

Global Sukuk Issuance 2002-2007

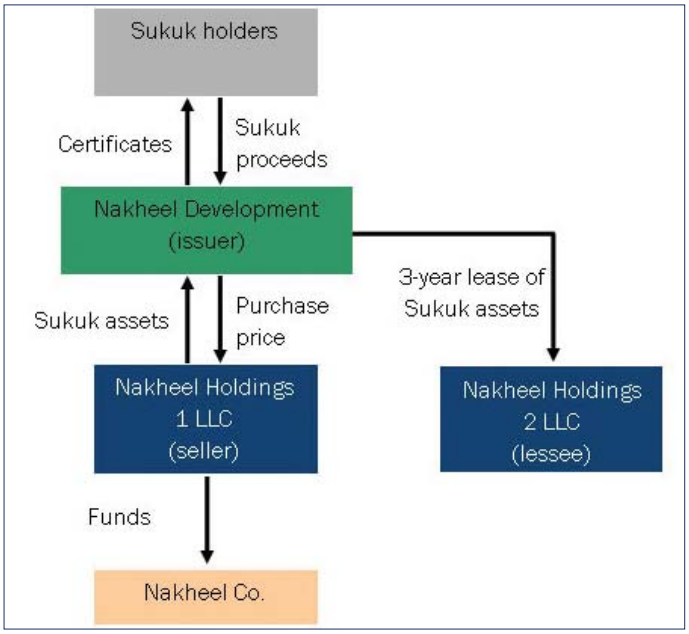
Source: Bloomberg, January 2007

A pre-IPO Sukuk is a debt financing instrument that provides investors with an opportunity to take a view on the equity markets before an IPO has taken place. During the lifetime of the Sukuk, investors receive not only a fixed income return, similar to the one they would expect from a normal bond, but also a guaranteed pre-allocation in shares to be issued in any public offering (initial or secondary) that takes place during the life of the issuance (defined as qualified public offering – QPO). This can happen either through the attribution of subscription rights, or through a commitment of the company to redeem in shares part of the instrument at the time of the QPO. This allows investors to benefit from the appreciation of the shares, which usually takes place immediately after the QPO. In this respect, a pre-IPO Sukuk has the risk/return characteristics of a bond, but with an equity upside potential, the value of which depends on the equity performance at the time of the QPO.

The pre-IPO Sukuk is a relatively new instrument which requires an arranger/lead manager who is at the cutting edge of structuring technology. There is a need to combine the best in financing techniques with legal and Shariah structuring. In particular, transaction structuring expertise and market knowledge are key to being able to balance the requirements of fixed income (i.e. debt) investors with the requirements of convertible (i.e. equity-oriented) investors. Barclays Capital has successfully been able to leverage on its expertise in structuring and distributing conventional financing products in the development and marketing of the pre-IPO Sukuk.

"The pre-IPO Sukuk has heralded a sea-change in investor perception of the Sukuk instrument and has been the single largest contributor to the growth of Sukuk issuance in 2006"

Depending on the particular needs of each borrower, a number of different transaction structures can be used for a pre-IPO Sukuk. As an example, the transaction structure used for the Nakheel Development pre-IPO Sukuk is summarized below.



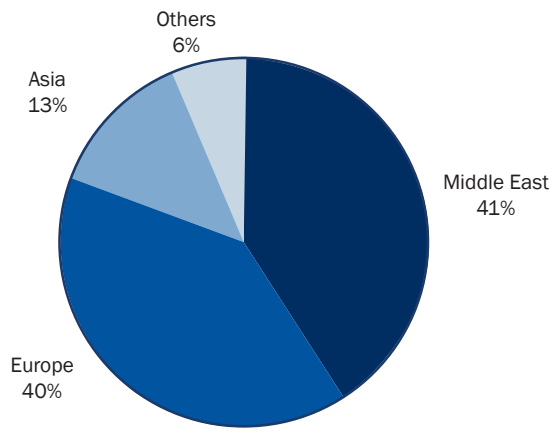
continued...

The Next Generation in Islamic Financing *(continued...)*

At the close of the transaction, Nakheel Development raised US$3.52 billion by issuing trust certificates (Sukuk Ijarah) to a diverse, global investor base. Proceeds of the Sukuk issuance were used to purchase a long leasehold interest on property at Dubai Waterfront (Sukuk assets) from Nakheel Holdings 1 LLC. Nakheel Holdings 1 LLC then injected capital into Nakheel Co., which is the corporate vehicle of the Nakheel Group. Nakheel Development then leased the Sukuk assets to Nakheel Holdings 2 LLC under a three-year lease agreement. Rental from this lease agreement were then upstreamed as returns to Sukuk holders. Pursuant to the terms of a servicing agent agreement, Nakheel Holdings 2 LLC will be responsible for managing the Sukuk assets on behalf of Nakheel Development.

The Sukuk size at launch was US$2.5 billion. Due to the unique transaction structure and aggressive marketing of the Sukuk, the transaction was well received in the global market, with an order book that was oversubscribed nearly two times. This enabled Nakheel to upsize the transaction to US$3.52 billion and to price the Sukuk at LIBOR + 120 basis points (bps) per annum, which was at the mid-point of marketing price talk (LIBOR + 95 to LIBOR + 145 bps). Interestingly, due to greater awareness from the investor base after the PCFC Sukuk transaction, new investors (i.e. those not participating in the PCFC Sukuk) accounted for 33% of the demand and 25% of the allocation in the Nakheel transaction. This was a clear demonstration of increased investor demand for and interest in Sukuk. Another key development was the large number of orders received from investors in Europe and Asia and as a consequence, the allocation of 40% of the Sukuk to European investors and 13% of the Sukuk to investors in Asia.

Nakheel Sukuk Allocation by Region



A key element of investor interest in a pre-IPO Sukuk relates to the option investors have to participate in a future IPO on preferential terms. Whilst this may seem like an expensive option for the borrower to give, the borrower in fact benefits through a lower cost of funding (the value of the option is monetized through a reduction in the margin). In that respect, the pre-IPO is a powerful financing tool which offers a "win–win" solution to all parties involved.

	PCFC Sukuk	Nakheel Sukuk
Issuer	PCFC Development (SPV)	Nakheel Development (SPV)
Obligor	Ports, Customs and Free Zone Corporation	Nakheel
Guarantor	–	Dubai World
Size	US$3.5 billion	US$3.52 billion
Closing Date	January 2006	December 2006
Structure	Musharakah	Ijarah
Tenor	2 years	3 years
QPO Yield	7.125% (LIBOR +200 bps at launch)	6.345% p.a. (LIBOR + 120 bps at launch)
Non-QPO Yield	10.125%	6.345% + up to 2.00% p.a.
QPO Discount	None	5%
Arrangers	Barclays Capital and Dubai Islamic Bank	

At Barclays Capital, we are confident that pre-IPO Sukuk will form an integral part of future Sukuk issuance, particularly in the GCC and South-East Asia, where there are a number of unlisted, fast-growing or mature companies that want to monetize today value that could be raised in the future via an IPO.

The author is head of Islamic Financing Solutions at Barclays Capital. He can be contacted at: Dubai International Financial Centre, Level 9, West Wing, The Gate Building, PO Box 506504, Dubai, UAE. Tel: +971 4 362 1000 or +971 4 362 1013 (direct), Mob: +971 50 553 2011, Fax: +971 4 362 1102.

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Malaysia External Trade Dev. Corp (MATRADE) offices worldwide
Malaysia Embassies worldwide
Malaysian Tourism Promotion Board offices worldwide
Ministry of International Trade Industry (MITI) offices worldwide
Malaysian Industrial Dev. Authority (MIDA) offices worldwide
Trade promotion Centre Offices and Trade Associations
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Project Financings in Saudi Arabia

By Robin Abraham, Mohamed Hamra-Krouha and Qudeer Latif

2006 witnessed three significant project finance transactions in Saudi Arabia that relied heavily on Islamic investors to meet part of their overall financing requirements.

Following the successful close of the financings for the US$9.9 billion Rabigh and US$5 billion Yansab projects, both of which included significant Islamic tranches, as well as funding from conventional banks, export credit agencies (ECAs) and Saudi government agencies, the shareholders of Al-Waha Petrochemical Company also chose Islamic financing for their project. In addition to Islamic finance, the Al-Waha project relied on funding from the shareholders and Saudi government agencies. There was no conventional bank or ECA funding.

This article considers some of the features of the Islamic tranches/facilities that financed the Rabigh, Yansab and Al-Waha projects.

The projects

Rabigh Petrochemical Company

The Rabigh project comprised a US$9.9 billion financing package for an integrated refinery and petrochemicals project. The sponsors were Saudi Aramco and Sumitomo Chemical and financial close was in March 2006.

The Japanese Bank for International Cooperation (JBIC) provided US$2.5 billion alongside the US$1.74 billion provided by 15 commercial banks, US$1 billion from the Public Investment Fund of Saudi Arabia (PIF) and a US$600 million Islamic tranche provided by APICORP, Bank Al Bilad, Calyon, Citibank, Islamic Development Bank, Riyad Bank, Gulf International Bank and the Saudi British Bank.

The Rabigh complex is expected to be one of the world's largest export-oriented refinery and petrochemical complexes, producing 18.4 million tons of petroleum products and 2.4 million tons of ethylene and propylene-based petrochemical derivatives products per year. There will also be a captive independent 380mw oil-fired water, steam and power project to serve the complex.

Yansab

Saudi Arabian Basic Industries Corporation (SABIC)'s US$5 billion Yansab project was signed in June 2006.

The integrated petrochemicals project is the largest greenfield project in Saudi Arabia to date. The US$3.5 billion financing package comprised commercial term and working capital facilities, ECA-backed facilities provided by the Italian ECA (SACE) and the United Kingdom's ECA (ECGD), the largest Islamic facility for a project financing to date (US$846.8 million) and a PIF facility.

Al-Waha

The US$526.55 million Islamic financing for Al-Waha signed on the 14th November 2006.

The financing for the 450kt per year polypropylene plant and a propane dehydrogenation unit is believed to be the first limited recourse greenfield project to be financed without any commercial bank debt, relying on funding from the shareholders and Saudi government agencies, as well as the Islamic facility. The sponsors were Basell and Sahara Petrochemical Company.

The arrangers of the financing were ABC Islamic Bank, Arab Banking Corporation, Bank Al Jazira, Banque Saudi Fransi, Gulf International Bank, Saudi Hollandi Bank and The Saudi British Bank.

Common features

The principal Islamic structure in each of these projects combined the use of: (i) a procurement arrangement (a variation of an Istisnah contract); (ii) a forward lease arrangement; (iii) purchase/sale undertakings; and (iv) a service agency agreement (or service agreement where the servicer is appointed as an independent contractor rather than an agent). The procurement arrangement is used to enable the financiers to disburse the funds required for the construction of the asset and the lease enables the financiers to seek repayment of the principal as well as a return on their funding. The undertakings are necessary to permit the constructed asset (or a part thereof) to be transferred to the project company in either a pre-payment scenario (voluntary or mandatory), or in a default scenario to accelerate the debt outstanding.

Procurement agreement

Under the procurement arrangements, each project company was, either as procurement agent or principal, obliged to procure the manufacture/construction and delivery of the project or asset being financed. The project companies had a direct contractual relationship with the EPC contractors.

The procurement agreement is essentially a variation of the Istisnah contract whereby the project company undertakes

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Project Financings in Saudi Arabia *(continued...)*

to procure the construction of a specific asset according to certain agreed specifications. The price of the asset and delivery date is specified at the outset. However, at the time the procurement agreement is entered into the asset does not exist and the procurer has not been paid. The liability of the financiers to pay and of the procurer to deliver is deferred to a future specified date(s).

Lease agreement (Ijarah)
As is the case with many other project financings, each of the Islamic structures used for these projects incorporated a forward lease arrangement (known as Ijarah Mawsufah Fi Al Thima or Ijaraj Fil Thimma). The forward lease agreement enables the financiers to generate a return on their funding during the period of construction, or in other words permits the financiers to recover a remuneration during construction in a Shariah compliant manner. Additionally, in each case, if delivery of the asset to be leased did not occur (and therefore the lessee is never able to benefit from the usufruct of the leased asset), the lessor must return in full all lease payments that have been made to it by the project company/lessee. (However, through a liquidated damages regime under the procurement arrangements, it is possible for the financiers to be compensated by an amount equivalent to that which they would have to reimburse.)

Sale undertaking
In the event that the project company wishes to pre-pay the financing, it can buy the financed asset from the financiers for a price equal to the outstanding principal plus rental accrued but unpaid. The sale undertaking can also be used to buy part of the financed asset from a single financier should, for example, withholding tax become applicable on payments to be made to it under the lease.

Purchase undertaking
Upon the occurrence of a default by the project company, the Islamic financiers can put the financed asset to the project company for a price equal to the outstanding principal plus accrued and unpaid rental. This effectively enables the Islamic financiers to accelerate the repayment of all amounts outstanding to them.

Service agency agreement/service agreement
Under the forward lease agreement the lessor retains certain obligations which Shariah does not allow to pass to the lessee, such as the obligation to insure the leased asset and the obligation to undertake any structural or major maintenance of the asset. These obligations can, however, be passed by the lessor to an agent or an independent contractor and the agent/independent contractor can be the project company. To the extent that the project company as agent/independent contractor claims any costs and expenses for acting in such a capacity, then the lease rentals will be increased by an equal amount. To mitigate settlement risk, the increased lease rental will often be set off against the costs and expenses claimed by the agent/independent contractor.

"The concept of diminishing Musharakah is often encountered in Shariah compliant residential real estate financing"

Distinguishing features

Incremental purchase of leased assets on Al-Waha
Under the Rabigh and Yansab projects, upon the expiry of the lease agreement at the end of the agreed tenor, the lessor transfers title to the lessee either by way of a gift or for a nominal consideration.

The Al-Waha project incorporated an alternative method for the transfer of asset ownership, with the leased assets being sold in increments by the financiers to the project company on each rental payment date. Accordingly, on each such date, the project company pays: (i) rental under the lease; and (ii) purchase payments, with title to a portion of the leased assets being transferred to the project company. This is similar to the concept of diminishing Musharakah that is often encountered in Shariah compliant residential real estate financing.

From an economic perspective, the lease rental payments are equivalent to interest payments under a conventional facility and the purchase payments are equivalent to principal payments. By structuring the payments in this way, any risk that a Saudi court would consider the lease rental payments to be in excess of the market rental payable for comparable leased assets would be reduced. This would mitigate the risk that the court could either order the rental amounts payable to be reduced, and/or that previous payments be refunded by financiers to the lessee/project company.

Co-ownership structure on Al-Waha
In a typical Ijarah structure the leased asset will be owned entirely by the financiers or by a Special Purpose Vehicle (SPV) (see below). However, in the Al-Waha project, the leased assets were: (i) acquired by Al-Waha as procurer on behalf of itself and the financiers; and (ii) were legally owned by Al-Waha on behalf of itself and the financiers.

The leased assets were co-owned in proportion to the funding provided by the parties for their acquisition and the financiers leased their ownership interest in the underlying co-owned assets to Al-Waha.

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Insya Allah.

*read: Ha-I per - mill
(investment yield per one thousand).

Project Financings in Saudi Arabia *(continued...)*

Use of an SPV in Rabigh and Yansab

To avoid the leased asset appearing on the balance sheet of the Islamic financiers, which may have required regulatory approvals and also due to local law requirements which prohibit non-Saudi nationals from owning real estate assets in Saudi Arabia, an onshore SPV was incorporated for the purposes of owning and leasing the manufactured asset. The SPV was owned by two Saudi Arabian financial institutions participating in the financing. The shareholders were given indemnities by the other Islamic financiers for any losses they may suffer in their capacity as shareholders. This was backed by an indemnity from the project company to the Islamic financiers. The SPV acted as custodian of the asset for the Islamic financiers.

Islamic supplemental agreement on Rabigh

To permit different risk allocations for participating banks within the same tranche, the primary Islamic documents had one risk allocation and were entered into by all Islamic participants. These documents were acceptable to the Shariah committees of all participating banks. For those participants which wished to pass some of the risk allocated to them back to the project company, such as the risk of shortfall of insurance proceeds, a supplemental agreement was entered into between those participants and the project company.

Conclusion

Other project financings are scheduled to close in Saudi Arabia in 2007 using Islamic finance for some or all of their funding requirements. These projects will likely see further distinguishing features being introduced, whilst still retaining the common features of the underlying structure used in the 2006 landmark projects described in this article.

CLIFFORD CHANCE

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Clifford Chance acted as common counsel to the financiers on the Rabigh and Yansab projects and advised the sponsors in relation to the Al-Waha project, including in relation to all aspects of the Islamic structuring.

Rafflesia Capital's Exchangeable Trust Certificates

By UBS

On the 27th September 2006, UBS Investment Bank successfully launched and priced what is believed to be the world's first Shariah compliant exchangeable trust certificates. The Sukuk, exchangeable into the equities of Telekom Malaysia, were issued by Rafflesia Capital, a Labuan (Malaysia) incorporated special purpose company, for Khazanah Nasional, the investment arm of the Government of Malaysia.

This was the largest ever exchangeable issue to come out of Malaysia and the largest exchangeable issue out of Asia – excluding Japan – in 2006. The offering comprised US$750 million of periodic payment trust certificates (due in 2011), upsized from the initial deal size of US$500 million on the back of strong investor demand. The offering was launched with a yield range of 5-year US dollar swap -32.5 bps to +42.5bps (equivalent to 4.925% to 5.675%) and a premium of 17–20%, finally pricing at a tight 5.07% (swap +3 basis points). The final pricing was set at a yield of 5.07% and a premium of 19%, which was above the mid-point of the indicated range.

Unique structure

What was so remarkable about this transaction was its unique and innovative structure – we believe this is the first Sukuk structure to be backed by Shariah compliant financial assets (equities of Telekom Malaysia). Previously, the Sukuk market was predominantly comprised of Sukuk structured as trust certificates, representing ownership of physical assets. This meant that potential issuers with inadequate physical assets – including holding companies and investment firms – were excluded. This deal establishes a structural framework so that these issuers can have access on the basis of their Shariah compliant financial assets.

Another challenging aspect of structuring this transaction was designing the mechanism for payment of coupons on the Sukuk, which were structured as premium redemption instruments paying a coupon of 1.25%. Unlike the redemption amount, which is guaranteed by Khazanah Nasional pursuant to a Unilateral Purchase Undertaking, the periodic Sukuk coupons could not be guaranteed and had to be paid from the dividend income derived from the equities of Telekom Malaysia. Investors' concerns regarding the uncertainty of coupon payments were addressed by creating a sinking fund account for the benefit of the investors, wherein dividends from the underlying equities were accumulated to ensure the availability of funds from which to make payment of periodic coupons over the life of the transaction.

Commitment to Islamic finance

The motivation of Khazanah Nasional for this deal was to reinforce Malaysia's reputation as an international Islamic banking hub; to continue Malaysia's tradition of innovation in Islamic banking; and to tap into Middle Eastern liquidity as an alternative funding source. Therefore, a key performance indicator for Khazanah Nasional was the acceptability of this structure to both conventional and Islamic investors globally, and distribution of the Sukuk to Middle Eastern financial institutions. Given Malaysia's prominent commitment to the development of Islamic finance, it was crucial that UBS Investment Bank structured the transaction in a way that was both Shariah compliant and priced at levels attractive to Islamic and conventional investors.

Extensive pre-marketing

Being the first Shariah compliant exchangeable Sukuk, UBS Investment Bank, along with representatives of the other joint lead managers, undertook an extensive pre-marketing exercise wherein selected Middle Eastern financial institutions in Kuwait, Qatar, the UAE and Bahrain were educated on the various aspects of the Sukuk and encouraged to return their feedback on the product features.

"The issue generated demand in excess of US$3.2 billion, with over 100 investors participating, implying a subscription level of 6.6 times the base deal size"

Great demand

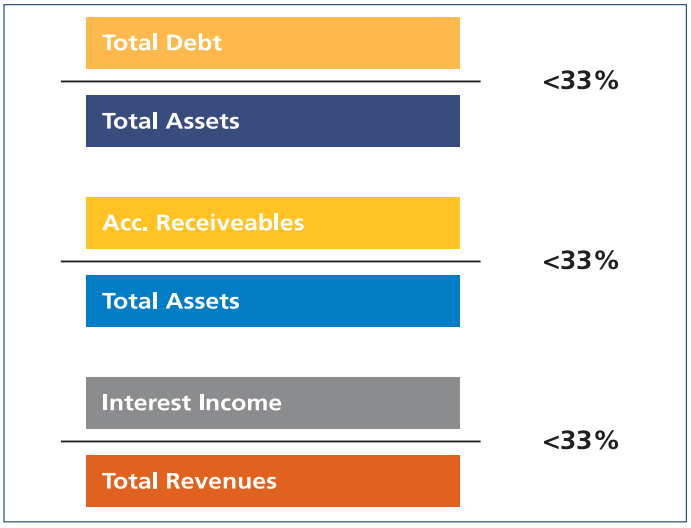
The groundbreaking nature of the deal combined with the investor education conducted during the pre-marketing phase motivated Islamic investors to buy in at below their benchmark investment yield levels. The issue generated demand in excess of US$3.2 billion, with over 100 investors participating, implying a subscription level of 6.6 times the base deal size. UBS Investment Bank generated 57% of this US$3.2 billion demand. Approximately 44% of the Middle East allocation was made to clients of UBS Investment Bank.

continued...

Rafflesia Capital's Exchangeable Trust Certificates *(continued...)*

Shariah compliance of Telekom Malaysia

The Sukuk was structured as exchangeable trust certificates representing the beneficial ownership of the investors in the underlying financial assets (Telekom Malaysia equities). It was therefore imperative from a Shariah compliance perspective that Telekom Malaysia be Shariah compliant at the time of issuance of the Sukuk and remain so throughout the tenure of the Sukuk. For this purpose, the Shariah advisors of the three joint lead managers approved the following criteria for determining the Shariah compliance of the company:



Source: UBS Investment Bank, September 2006

A designated calculation agent periodically applies the above-mentioned tests to the relevant financial statement of Telekom Malaysia and forwards the results to a group of three Shariah scholars appointed by Rafflesia Capital, which issued the Sukuk, on behalf of Khazanah Nasional. If there is a sustained breach of the Shariah compliance tests, the Shariah scholars have the discretion to declare Telekom Malaysia non-Shariah compliant, which gives the investors the right to have their respective Sukuk redeemed by Khazanah Nasional at an agreed price.

Key timing

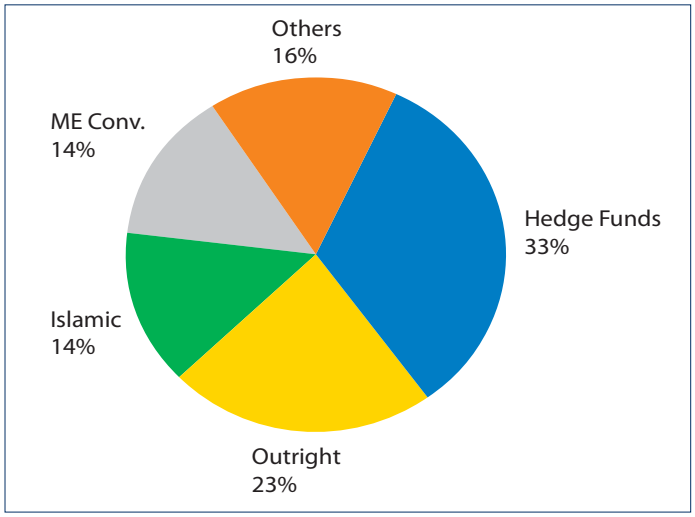
The timing of the transaction and its execution were key factors to the success of the offering. Given the complexity and objectives of the transaction, a detailed timetable was prepared. Adequate time was factored in for investors to understand the new structure and also assess the credit quality of Khazanah. UBS Investment Bank conducted continuous education and feedback sessions with Middle Eastern investors to provide them with comfort. Investors had a week to analyze the underlying asset and participate in the transaction.

The result of this careful planning was significant interest and demand, not only from Islamic and Middle Eastern investors, but also from conventional investors. The Fed Funds rate was widely forecast to remain constant, with the expectation that this would result in tightening of the swap rates as a result of improving sentiments. Over the period of the book building, the US dollar swap rates tightened by around 25 basis points, which was fully captured in the final pricing to the benefit of the issuer.

Strong interest

There was very strong interest from all groups of investors globally; the allocation by investor type is shown below.

Allocation by investor type



Source: UBS Investment Bank, September 2006

Allocation was greatest among hedge funds, which were allocated 33% of the offering; outright investment accounted for 23% of allocation; and Islamic and conventional Middle Eastern investors were each allocated approximately 14% of the total issue size.

Highly successful

In the press the deal was unanimously perceived as a highly successful offering. The Sukuk – and the UBS team in charge of the transaction – gained a number of prestigious awards in connection with the deal and it has also been nominated for a number of other major awards to be announced during the first quarter of 2007.

Islamic Project Finance Returns to the Spotlight

By Neil D. Miller and Paul McViety

With the growth and the popularity of the Islamic finance industry now being beyond question, increasing emphasis is being placed upon the analysis of product innovation in various sectors of the industry; looking at what has been achieved to date and considering areas where there may be scope for a particular product to evolve even further.

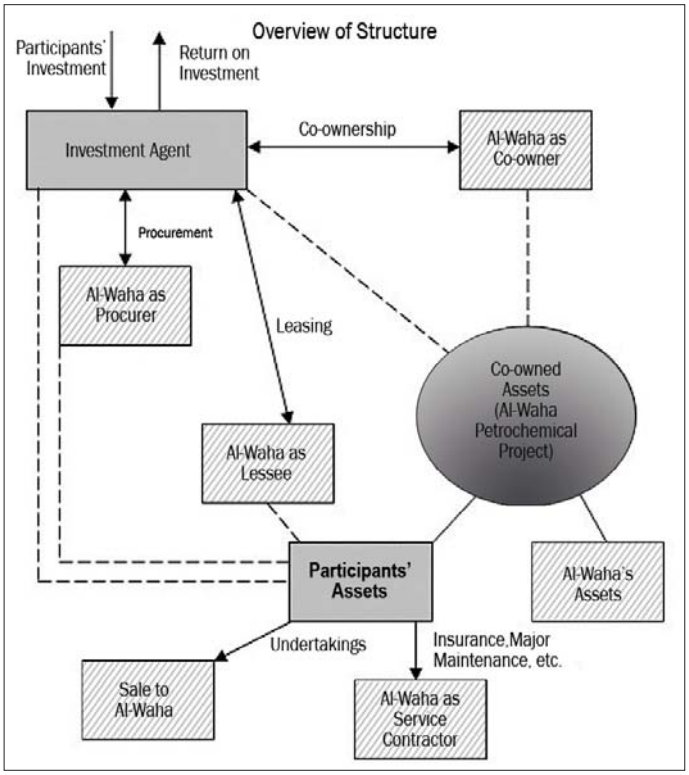
The Islamic financing structure that was developed for the US$1 billion Al-Waha petrochemical project illustrates the progression of Islamic project finance. In a market where the popularity of Sukuk offerings seems to be at the forefront of most people's minds, it serves as a timely reminder of the important role of Shariah compliant financing structures in Middle East projects. Whilst multi-billion dollar capital market deals like the Dubai Ports Sukuk and the recently closed Nakheel Sukuk may hit the headlines, a lot can be learned from studying project finance transactions such as Al-Waha.

"The Islamic financing structure that was developed for the US$1 billion Al-Waha petrochemical project illustrates the progression of Islamic project finance"

Background

The project, whose sponsors are Sahara Petrochemicals and Basell, is located in Jubail industrial zone, Saudi Arabia and, when completed, will comprise of polypropylene and propane dehydrogenation plants. The financing package for the project has been developed around an Islamic facility of approximately US$526 million, comprising a base investment and a standby investment (as two distinct tranches, with different disbursement conditions attached to each tranche). Additional funding for the project will be sought from the Saudi Industrial Development Fund (SIDF) and the Public Investment Fund (PIF), with the Islamic facility being scaled down as PIF funding is successfully injected.

The absence of commercial lenders and export credit agencies is a notable departure from the so-called "multi-sourced" financing model which has been used so successfully on Middle East projects: Al-Waha can therefore be characterized as one of the largest stand-alone Islamic financings in Saudi Arabia to date. The underlying structure, which combines features from a number of different Islamic products and from which one can draw notable parallels with some of the Sukuk structures in the market, is an impressive achievement when one considers the difficulties posed by, and uncertainty within, the Saudi legal framework.



Agreeing to invest – co-ownership

The participating banks, comprising ABC Islamic Bank, Bank Aljazira, Banque Saudi Fransi, Gulf International Bank, Saudi British Bank and Saudi Hollandi Bank, were advised by Norton Rose. The participants appointed an investment agent (one of the Saudi banks), through whom they will make their contributions in the base and standby investments. The financing also benefits from a security package and a hedging strategy, both of which have been structured so as to ensure Shariah compliance.

The investment agent and Al-Waha entered into co-ownership arrangements, based on the principle of shirkah al milk, pursuant to which they have agreed to invest in, and co-own, certain physical assets of the project (referred to as co-owned assets). The beauty of this arrangement is in its simplicity; the injection of the equity into the project is a natural fit within these

continued...

Islamic Project Finance Returns to the Spotlight *(continued...)*

arrangements, with the basis upon which contributions are to be made by the co-owners being agreed upfront (including the order in which these contributions are to be made). The understanding of the parties with respect to delivery and cost overruns is obviously an important component of these construction phase arrangements.

Additionally, certain matters relating to the operating phase of the project are covered under the co-ownership arrangements, such as how title to the co-owned assets will be held and the responsibilities of Al-Waha in relation thereto.

Al-Waha as procurer

The investment agent (as a co-owner) effectively discharges the bulk of its obligations under the co-ownership arrangements by entering into a separate procurement contract with Al-Waha (in its capacity as an independent contractor). Under this particular arrangement, Al-Waha (in its capacity as an independent contractor) has undertaken to procure the delivery of the participants' ownership interest in the co-owned assets (this interest being described as the participants' assets) on time and to specification. Ownership of the participants' assets and all of the associated risks will remain with Al-Waha until the assets are delivered at project completion.

Inevitably, the parameters of these procurement arrangements are fairly basic; it being recognized that Al-Waha would itself be engaging engineering procurement construction (EPC) contractors with the requisite expertise to complete the project. It is ultimately through this procurement role that Al-Waha receives funding from the participants (via the investment agent). This approach is not too dissimilar to that of Istisnah, which has been used for construction phase financing on a number of other greenfield projects. The basic approach was similar to techniques Norton Rose had developed for commercial real estate development projects in the UK over the past five years .

Forward leasing

The participants' assets (i.e. the participants' ownership interest in the co-owned assets) are the subject of a forward leasing arrangement (Ijarah Mawsufah fi al Dimmah), which enables the financiers to receive advance rental payments from Al-Waha during the construction phase. Following the approach taken on a number of recent Islamic structures, the equivalent of a commitment fee forms a component of the calculation for these advance rentals.

Although not universally accepted, a number of Shariah scholars have found forward leasing permissible on the understanding that: (i) advance rentals are taken into account (as rental which has already been paid) when actual leasing commences; and (ii) advance rentals have to be refunded in full where the assets are not delivered for leasing. Such matters are readily addressed in the documentation in order to ensure that the commercial deal is not disturbed: first (in the case of (i) above), by having a notional "gross-up" for the purposes of the first "actual" rental payment; and, for the purposes of (ii) above, by careful calculation of any termination payments that are triggered if a termination occurs pre-delivery (in Al-Waha this is dealt with under the termination provisions of the procurement arrangements).

"Some commentators would argue that the need for innovation is not so great in an industry that has built up so much momentum over the last five years"

Upon project completion, the participants' assets are deemed to have been delivered and actual leasing commences, with Al-Waha being obliged to start making rental payments. As with most Ijarah-based transactions, supplemental rent (equivalent to any charges payable by the investment agent under the service agreement) forms part of the rental during the operating phase.

The leasing arrangements do not, of themselves, include any amortizing payments – from a purely financial point of view, the leasing is in place simply to generate a LIBOR-based return for the financiers. Repayment of the facility is actually dealt with as part of the co-ownership arrangements.

Additionally, potential exposure of the financiers to additional costs (such as increased costs and mandatory costs) are wrapped up as part of the calculation for both advance rentals and rentals. This approach appears consistent with the stance taken on a number of recent projects and marks a retreat from the position taken on a number of earlier projects (where the Shariah scholars had been comfortable with the financiers making a separate claim for such amounts through the indemnity provisions). In shifting these to the rental calculations and removing the stand-alone indemnity, the only drawback is that, in order to avoid uncertainty (gharar), the rental calculation always looks to those costs incurred in (and quantifiable for) an earlier period (i.e. an increased cost incurred during any rental period would form a component of the rental for the next-to-occur rental period). This results in a delay in the ability of the financiers to claim such amounts and also means that any costs incurred in the last rental period cannot be claimed through this approach.

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Islamic Project Finance Returns to the Spotlight *(continued...)*

Service arrangements

An analysis of the risks associated with asset ownership (or, in the case of Al-Waha, co-ownership) is an important part of any Islamic structure. This becomes even more critical where the assets involved form part of a petrochemical project. Of obvious concern to the financiers are potential third party and/or environmental liabilities which may arise during the operating phase (i.e. once delivery has taken place and the co-ownership interest has been created). The risk of any such liability materializing is reduced because Al-Waha will have possession and control of the assets under the leasing arrangements. However, the service arrangements and various indemnities throughout the documentation go further towards ensuring that the financiers are not in any worse position than they would be with a conventional financing.

For the purposes of traditional Ijarah structures, an agency approach is typically adopted whereby the project company is appointed as the service agent of the financiers in order to assume responsibility for certain tasks (e.g. obtaining insurance and requisite authorizations for the project, performing major maintenance and settling ownership taxes) which would otherwise have been the responsibility of the lessor. In order to achieve a stronger footing under Saudi law, it was decided that Al-Waha should be engaged as an independent service contractor and not as an agent. Such strict obligations being placed upon Al-Waha would, at least in theory, ensure that the Saudi courts would look more favorably upon the contractual provisions (including indemnities) intended to operate so as to keep the financiers "whole" in a total loss scenario.

Another interesting feature of this kind of co-ownership arrangement is the replacement asset regime – this unique regime is contemplated as part of the service arrangements. If the participants' assets suffer a loss (other than where a total loss has occurred) and the service arrangements kick in, Al-Waha (as independent service contractor) will procure the transfer of an additional percentage of ownership interest in the co-owned assets (i.e. part of Al-Waha's interest under the

continued...

Islamic Project Finance Returns to the Spotlight *(continued...)*

co-ownership arrangements) to the investment agent, thus ensuring that the leasing arrangements remain unaffected.

Incremental purchase of assets

The repayment arrangements in respect of the facility are reflected through purchase and sale undertakings, pursuant to which Al-Waha will buy proportions of the participants' assets from the investment agent during the operating phase by making purchase payments on certain dates in accordance with an agreed schedule. These dates coincide with rental payment dates, meaning that the financiers will effectively receive a rental payment (profit) and a purchase payment (principal) on each of those dates. The Al-Waha project also contemplates the right to prepay (albeit limited) as well as a mandatory cash sweep, both of which trigger "unscheduled" purchase payments through the operation of these undertakings.

"Al-Waha is required to pay a fixed amount which is deferred until the time at which Al-Waha acquires all of the participants' assets"

Purchase payments of this nature are generally permitted under Shariah as part of co-ownership arrangements; a number of similarities can be drawn with the most favored home financing product based on the principle of diminishing Musharakah, as developed by Norton Rose for several clients in the UK real estate market.

As an additional part of these purchase arrangements, Al-Waha is required to pay a fixed amount which is deferred until the time at which Al-Waha acquires all of the participants' assets (i.e. at scheduled expiry of the lease or upon an early termination). The purpose of this additional amount is to provide a "buffer" to cover certain potential exposures of the financiers (for example, an increased or mandatory cost which has been incurred but which cannot otherwise be passed back to Al-Waha due to termination of the leasing arrangements (as discussed above).

Framework for enforceability

For a project of this size, it would be a rather time-consuming exercise for the draftsman to work through all of the commercial terms relating to the project and ensure (with guidance from the Shariah scholars) that each such term is correctly positioned within the most appropriate underlying Islamic document. Fortunately, this exercise did not have to be performed on Al-Waha – it was accepted by all parties involved that an Islamic facilities agreement should be used as the "framework" for the financing.

The concept of an Islamic facilities agreement is not a new one; albeit usually seen on multi-sourced financings. For the Al-Waha transaction, one of the key benefits of having an Islamic facilities agreement is that the contemplated transactions become more visible as a financing arrangement in respect of which the Committee for the Settlement of Banking Disputes (operating under the aegis of the Saudi Arabian Monetary Agency, the SAMA Committee) would take jurisdiction. In theory, this should ensure that the possibility of ending up before the unpredictable Board of Grievances is even more remote.

Where next?

It goes without saying that extra care needs to be taken when combining so many different products in order to achieve the financing objectives. This inevitably involves a more extensive and potentially protracted dialogue with the Shariah scholars in order to ensure that the Shariah integrity of each product and the overall structure is in no way compromised.

Some commentators would argue that the need for innovation is not so great in an industry that has built up so much momentum over the last five years; however, transactions such as Al-Waha illustrate that innovation is not so much about driving the industry forward as it is about ensuring that the right balance continues to be achieved between the requirements of Shariah scholars and the commercial needs of the parties.

NORTON ROSE

Neil D. Miller is partner and global head of Norton Rose's Islamic Finance Group. Paul McViety is an associate in the Islamic Finance Group. Norton Rose advised the financiers and led the documentation process on the Al-Waha Petrochemical project.

The Evolution of Products in Islamic Finance

By Safdar Alam

The Islamic finance industry continues to develop at a rapid pace which shows no sign of abating. Islamic finance transactions are expanding to new countries and regions, the range of Islamic structures is increasing, and still the huge demand for products and structures is comfortably outstripping the availability of suitable products.

New products are being developed and other (relatively more established) products are seeing development in terms of complexity and innovation – for example we have seen convertible Sukuk, pre-IPO Sukuk and exchangeable Sukuk issues.

Sukuk

The nature of the structures that are being developed and used is naturally playing a key part in the development of the industry as a whole. One way to measure the development of the industry is to assess the evolution of products, and those that are popular will be those that meet the needs of all parties involved. There will be an increase in the utilization of these products, and still further evolution, from vanilla to complex, yet still retaining the same underlying structure. For example, the Sukuk product is developing more varieties, yet they are still Sukuk. As a product and structure, Sukuk appears to be here to stay, and only the direction in which it will continue to evolve is not yet fully certain. Debates have long been underway to discuss a secondary use of Sukuk in terms of liquidity management, and here we see the focus of discussion shifting from analyzing the differences between various Sukuk structures, to focussing on the similarities. Sukuk that are rated and listed will contribute to the eventual liquidity of their trading, hence the aim is to issue more and more Sukuk that are rated and listed.

There are also debates about the development of an Islamic repo, which will presumably involve the use of Sukuk or other Islamically acceptable securities.

So we can see that the debate is evolving from "Is Sukuk an appropriate product for the industry?" to "How can we use Sukuk to further develop the industry?" Once that has happened, it is very difficult to take a step back, for example if in the future the industry decides that perhaps Sukuk is not the best structure to meet the needs of parties in a Shariah compliant manner. Hence it is crucial that analysis of the products and structures takes place at an early stage of their introduction to the market.

Continuing to use Sukuk as an example, the key reason for its current success and popularity is clearly the fact it meets most or all of the needs of the investors and fundraisers. However, another equally important reason is its similarity to conventional bonds. It is generally accepted that Sukuk behave similarly to bonds, and are treated similarly to bonds by both issuers and investors. In fact, this has been a key driver in the acceptance of Sukuk amongst both issuers and investors who also have access to the conventional bond market. For investors, Sukuk can provide benefits that are not achievable by buying bonds, for example access to new markets and regions or to achieve higher spreads than similar credit risk in regions such as Europe.

"As a product and structure, Sukuk appears to be here to stay, and only the direction in which it will continue to evolve is not yet fully certain"

Another key consideration is the fact that Sukuk can generally be booked, risk managed and (eventually) traded like bonds. Most buyers of Sukuk are not Islamic institutions, but conventional institutions that will typically have a large portfolio of bond investments and trading books. As an estimate, Islamic institutions buy between 20–30% of Sukuk issues in the GCC and a lower proportion of Sukuk issues in South-East Asia. Hence it is clear that the success of the Sukuk market is largely due to the presence of conventional banks and institutions buying the paper. It is also clear that these institutions buy Sukuk because they are similar to bonds, and they treat them as bond products for booking and risk management purposes. It is natural to conclude that if Sukuk were significantly different to bonds, then they would not be bought in any real volume by conventional institutions, and the Sukuk product would not have reached the level of prominence it now enjoys.

Investment products

Focussing on this particular issue, the same also applies to investment products. The technology and pricing for many investment products comes from conventional banks, and Islamic investment products are priced in the same way as their conventional equivalents. Shariah compliant capital protected equity investments are booked similar to floating rate notes or equity linked notes. It is this similarity in structure

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The Evolution of Products in Islamic Finance *(continued...)*

that allows conventional banks to price and distribute (and hedge) these products, either direct to the market or on a wholesale basis to Islamic banks for onward distribution to the retail market. Profit rate swaps are booked as interest rate swaps. If there was not this direct similarity in the products, they would not be structured by conventional banks, and if conventional banks did not offer products such as these, then Islamic banks would not be able to offer these products to their own clients – because of course the Islamic banks need to hedge their own exposures with the conventional banks in a Shariah compliant manner.

"Is there anything wrong with cherry picking the best products that conventional banking offers and Islamicizing them?"

This in itself is not a cause for concern, as there is nothing inherently wrong with developing a Shariah compliant product that has strong similarities to a conventional product. Conventional banking has been evolving over a much longer period of time than Islamic finance, and a large number and variety of products have been developed and tested by the market. The more established products are those that continue to meet the needs of the involved parties – and the needs of the parties in Islamic finance are largely the same needs as the parties in conventional finance. Parties in both cases wish to raise funds, invest funds, understand the risks involved – whether it is enterprise risk, credit risk, currency risk, or rate risk – and to be able to manage or control these risks and earn a sufficient return or pay an acceptable cost. These universal needs span both the conventional and Islamic finance industries.

"Islamisizing" conventional products

So the question still remains – is there anything wrong with cherry picking the best products that conventional banking offers and Islamicizing them? This is certainly how the vast majority of Islamic products are developed.

Let us consider the evolution of a certain product in conventional banking. If a client wishes to invest in XYZ company he can buy shares in that company – a simple solution. Eventually, over time, a more efficient way has developed – by using leverage and maintaining upside exposure by using significantly less funds, and at the same time obtaining protection against the downside – by buying call options. Options allow the hedging of risks and also the ability to speculate on markets in a relatively cheap and low-risk (for the buyer at least) manner.

Now imagine an Islamic client with the same requirements, to invest in XYZ. You could take the approach that buying shares is inefficient and old fashioned, in fact options are cheaper and offer more protection. Hence one solution would be to Islamicize a call option, and offer it as an Islamic investment product. It might not suit all Islamic clients, but for certain investors it would meet their needs.

However, options owe their existence to the fact that they use leverage, permit speculation, involve uncertainty and no purchase of the underlying asset (in the case of cash settled options). These are principles that are not Shariah compliant. Clearly, taking such products, which are based on non-Shariah compliant principles, and restructuring them in such a way that the same economics are achieved, albeit in a Shariah compliant product, appears counter-intuitive. Yet this scenario does occur because there is such a great demand for Islamic products, and it is growing rapidly. The products that are most readily developed are those with a strong crossover with conventional products, for reasons mentioned above. Conventional banks are content to sell Islamic call options because they are priced, booked and risk managed the same way as conventional call options – because their economics and risks are the same. At the same time, Islamic investors are largely content to purchase such products (even though with some cosmetic repackaging they can be sold as Shariah compliant investments) because there are not enough alternative suitable products for them to invest in. This is repeated across several product areas – in financing products and investment and hedging products – so that the Islamic finance industry is now heading in a direction that is defined by the nature of products that are in the marketplace.

Developing new Islamic products

This author takes the view that if we use our collective skills and experience, we should be able to develop products without reference to equivalent conventional products that are only possible by following non-Shariah compliant principles. By "we," I mean the Islamic finance industry as a whole. We should still aim to leverage from the experience of conventional banking, but at the same time benefit from the skills and experience of Islamic banks. We can select products from conventional banking that were developed on principles that are not against Shariah. For example an asset-backed bond, with slight modification, becomes a Sukuk. Securitization is built on principles entirely consistent with Shariah – the sale and transfer of assets in exchange for a return based on those assets.

Alternatively we could try to find different solutions to those developed by conventional banking and solutions that are not

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The Evolution of Products in Islamic Finance *(continued...)*

only Shariah compliant but in full accordance with Shariah principles in all aspects, and still meet the needs of all parties. This is an oft-repeated phrase, but we should look beyond the letter of the law and try to comply also with the spirit.

But who should be undertaking this endeavour?
Several participants have key roles to play – Shariah scholars, Islamic banks, conventional banks and also investors. Shariah scholars can refuse to approve products that may appear to be Shariah compliant but are judged to be inappropriate for the development of the industry. A unified body representing the scholars, with the power to enforce its decisions widely in the industry is required – one that has the ability to effectively ban the use of certain types of products and encourage and suggest the development of other, more suitable products.

Islamic banks can stop buying certain products from conventional banks, or better still provide clear guidelines as to what is appropriate and what is not. They could develop their own products, but a lack of technology and skills prevents most Islamic banks from doing so currently. Investors too can encourage such development by not putting their funds in inappropriate products and encouraging Islamic banks to develop more suitable products. However, in a marketplace where demand outstrips supply, we cannot expect the demand side to always put qualitative judgments ahead of the hard need to invest in new and existing products.

Regulating bodies, rather than merely attempting to control and manage current activities, should also be encouraged to have a say in deciding which activities are inappropriate, and perhaps even banning such activities.

Finally, conventional banks also have a role to play. They need to be clearly informed by the industry as to which products are suitable and which are not, and given clear guidelines which cover the spirit as well as the letter of Shariah principles. If investors and Islamic banks stop buying products which contravene these guidelines, then conventional banks will stop developing such products.

All the above market participants have a vital role in this endeavour. The key to success lies in developing real dialogue between the participants – and not just individual banks with individual Shariah boards and their investors, but between authorized bodies that represent each of these groups, empowered to make decisions on their behalf.

The current prevailing attitude – how much can we sell easily in a structure that we can get approval for? – needs to change into an attitude of aiming to develop the most appropriate products that will help the industry as a whole to grow and evolve in a direction that is better for the industry and its key participants. In that way, the credibility of the Islamic industry will be increased. Islamic finance is not an industry that is fundamentally short of credibility, but in some key areas it is facing a challenge on that front.

"Islamic finance is not an industry that is fundamentally short of credibility, but in some key areas it is facing a challenge"

One of the outcomes of such a dialogue as described above would be that the Islamic finance industry accepts and recognizes the best of conventional banking products that meet the needs of all parties, with clear pricing and risk–reward profiles, built on principles that are not contrary to the Shariah. It will also enable the industry to structure and build products that from the onset are built on principles that are fully Shariah compliant, and exclude speculation, uncertainty, leverage – even if it is possible to Islamicize them by cosmetic restructuring.

This would add real value to the industry, to the benefit of all its stakeholders. It would add to the credibility and development of the market, and provide a clear blueprint for future growth and thinking. It would show that there is a clear difference between conventional banking and Islamic banking and not just a cosmetic difference. The Islamic finance industry would develop products that are new and truly innovative (in a good way), whilst also recognizing that it can and should benefit intelligently from the experience of conventional banking and still not compromise the real spirit of Islam.

The author is from global Islamic banking at Calyon.

Cross Border Deal of the Year

By Dubai Financial & Citigroup

The US$330 million Dubai Financial acquisition of a 40% equity stake in Bank Islam Malaysia Berhad (BIMB) was a unique deal in 2006 in which Citigroup acted as the sole advisor and arranger.

Pre-funding was provided by Citigroup through a Shariah compliant bridge facility, hedging the underlying currency exposure with a ground breaking Islamic cross-currency swap. The bank also led the dual-tranche Islamic syndication for the take-out of the bridge facility.

Deal structuring

After 6 months of negotiation and after facing serious competition from the other buyers, in May 2006, the Board of Bank Islam Holding (Malaysia) finally approved the sale of a 49% stake in its wholly owned subsidiary bank to Dubai Financial and Malaysia's Lembaga Tabung Haji through an issue of shares.

Dubai Financial opted to secure financing in Malaysian ringgit to mitigate the currency risk and take advantage of the prevailing lower ringgit interest rates. Dubai Financial chose Citigroup to enable payment of RM828 million (approximately US$230 million) for its portion of the subscription to the share issuance in early October 2006.

Citigroup, as the sole mandated lead arranger and bookrunner, provided a fully underwritten US$ equivalent of the Islamic bridge facility structured as a Murabahah transaction.

As the payment of the acquisition price was to be in ringgit, the whole amount of the US$ Islamic bridge facility was swapped into ringgit through a commodity based Shariah compliant cross-currency swap.

Execution

Citigroup initially bridged Dubai Financial for the acquisition. The syndication was then launched and the senior phase of the syndication was subsequently closed in a relatively short time frame.

The total amount of the syndication is US$330 million which was used to take out the bridge facility, and the balance utilized for general corporate purposes.

This transaction represents the debut Islamic financing facility for Dubai Financial. The facility is structured as a dual-tranche financing to accommodate Shariah structuring requirements of various Islamic banks. Tranche "A" is based on a revolving commodity Murabahah based mechanism commonly used for floating rate Islamic financings in cases where the purchaser does not have underlying tangible assets. Tranche "B" is based on a fixed rate 'Share Murabahah' structure whereby the shares of BIMB have been used as the underlying assets.

Innovative structure

This facility represents the first truly integrated M&A, financing and hedging package structured Islamically which brings together the Middle Eastern and Asian Islamic markets. Various phases of the transaction dovetail seamlessly to provide the client an end to end Shariah-compliant solution.

"This deal represents potentially the most significant cross-border transaction Islamically structured, integrating two hubs of the Islamic market"

Significance for the industry & setting new benchmarks

The transaction establishes the viability of the Islamic financing to be applied as a comprehensive M&A, financing and hedging package.

The acquisition was, at the time, the largest ever investment in an Islamic financial institution by foreign financial and strategic investors in Malaysia and the single largest investment for Dubai Financial in Asia.

This is expected to have a multiplier impact on the growth of Islamic finance in Malaysia as the new capital of RM1 billion will allow BIMB to pursue new growth opportunities in Malaysia's fast-growing Islamic banking sector.

Moreover, through its alliance with Dubai Investment Group, BIMB will tap into Islamic banking opportunities in the Middle East, as well as explore other diversified financial services such as investment banking and asset management.

The acquisition financing deal also underpins Dubai Financial's presence in the international financing arena. The facility was oversubscribed at a sub-underwriting level through seven mandated lead arrangers and attracted a cross-section of investors from different regions.

continued...

Cross Border Deal of the Year *(continued...)*

The facility delivered the same efficiency as expected from a conventional transaction.

This deal represents potentially the most significant cross-border transaction Islamically structured, integrating two hubs of the Islamic market.

As the payment of the acquisition was to be in ringgit, the whole amount of the US$ Islamic bridge facility was swapped into ringgit through the largest Shariah compliant cross-currency swap transaction to date.

Deal	Deal Features	
Dubai Financial acquires Bank Islam and CitiGroup arranges US$ 330 million Islamic Syndication Facility	Acquirer	Dubai Financial LLC
	Target company	Bank Islam Malaysia Berhad
	Amount	US$ 330,000,000
	Tenor	5-year bullet
	Financing Structure	Shariah compliant Bridge Facility with an embedded Islamic US$/RM cross currency swap and taken out through a 5-Year Syndicated Dual-tranche Islamic Facility
	Sole Bookrunner	Citigroup
	Sole Lead Manager	Citigroup
	Islamic Hedging Bank	Citigroup
	Islamic M&A Advisor	Citigroup

Dubai Financial LLC is part of Dubai Group, with a balance sheet in excess of USD 2 billion and focussing on strategic investments in the financial services sector.

Citigroup has been a leader in the Islamic Finance business for more than 20 years and has successfully arranged Islamic transactions for issuers in Europe, Asia, Africa and the Middle East.

Islamic Collateralized Debt Obligations

By Dr Humayon Dar

Collateralized debt obligations – commonly known as CDOs – are generally perceived as a "no-go" area in Islamic finance. This perception is correct.

As the way CDOs are structured and traded in conventional financial markets is certainly Shariah repugnant. The task of an Islamic financial engineer is to design a Shariah compliant structure that can replicate the risk–return profile of a conventional CDO. Doing so requires a good understanding of the Islamic stance on collateral, debt and trading in it. Requiring collateral to secure debt is a recognized and acceptable function in the Islamic theory of contracts. Similarly, while interest-based lending is prohibited, there are a number of Islamic modes of financing that can be used for issuing debt in compliance with Shariah. Discounted trading in debt, however, has limited acceptance: Middle Eastern scholars reject it while the Far Eastern school of thought find it acceptable. Given that there are a number of CDOs that have non-debt underlying assets – like trust preferred (a debt–equity hybrid) CDOs and CDOs of CDOs – the prohibition of trading in debt can be circumvented in structuring Shariah compliant CDOs.

CDOs are a tool to leverage a financial portfolio by issuing securities of different ratings to match the risk appetite and investment policies of investors. Like any financial transaction, a CDO has an asset side (comprising a pool of credit risky instruments like bonds, loans, credit default swaps and asset-backed securities, etc...) and a liability side (consisting of securities tranched in different asset classes). A representative structure of a CDO is sketched in diagram 1. An originator/arranger having exposure to a reference portfolio (underlying assets) creates a mechanism (with the help of a special purpose vehicle (SPV)) to create matching liabilities by issuing tranched securities (senior classes, mezzanines, junior classes, swaps and equity). The structure presented in diagram 1 is an example of the senior-most debt being exposed to the credit risk exposure of the originator. Other notes, however, are made bankruptcy remote through an SPV.

"The prohibition of trading in debt can be circumvented in structuring Shariah compliant CDOs"

While the above-mentioned Shariah issues in terms of collateral and debt trading are important, in the present context the issue of preference shares is probably more relevant to structuring Islamic CDOs. The way the CDO is structured allows for preference/seniority of some notes over others, with the equity being the residual claimant. Although in conventional CDOs, notes (papers representing debt) are issued, an Islamic structure would require issuance of different classes of shares (as mentioned below). It is

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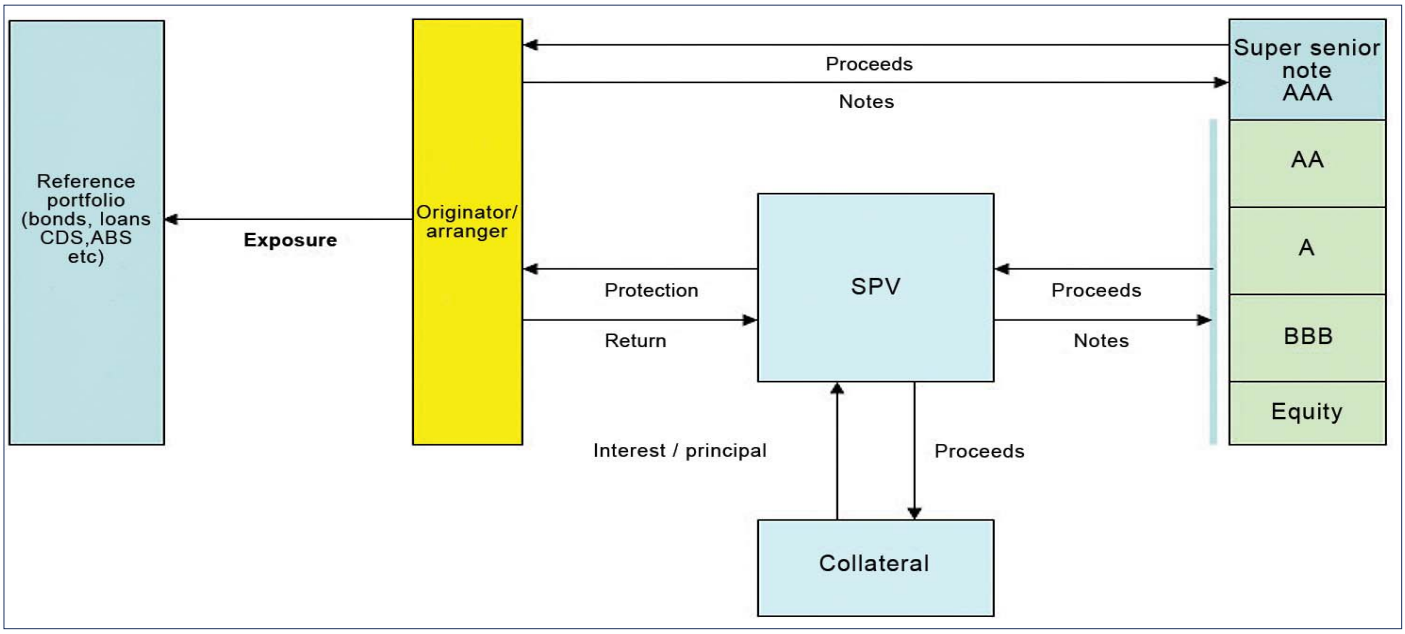
Diagram 1: A representative structure of a CDO



Islamic Collateralized Debt Obligations *(continued...)*

a basic requirement for such a structure to be Shariah compliant that the underlying assets (the reference portfolio) must be in compliance with Shariah. Thus, if the reference portfolio contains some Shariah compliant instruments like Sukuk, Ijarah-based assets and Murabahah receivables, etc, the SPV may issue some shares with different risk–return characteristics.

"There is a growing consensus among contemporary Shariah scholars that a Mudarib can guarantee a return of a benchmark"

Although the majority of Shariah scholars do not endorse preference shares, it is possible to introduce clauses in memorandum and articles of association to give some preferential rights to certain investors over others. For example, if a company has multiple investors, it is not against Shariah that they impose certain restrictions on the manager with respect to the use of their investments and their right to different returns. For instance, if there are two capital providers in a Mudarabah, one may only contribute to the Mudarabah on the condition that his capital would be employed in less risky activities in order to minimize the loss of his capital. In return, the manager may offer him a lower return as compared to the other investor who does not put any restrictions on the use of the capital provided by him.

There are some deeper Shariah issues that must be addressed to make the above structure Shariah compliant.

1. The SPV must not invest the proceeds of notes (Islamic investors' capital) into any Shariah repugnant activity. In the conventional context, the proceeds may very well be invested in an account risk-free (cash equivalent) collateral paying, say, LIBOR flat. In a Shariah compliant structure, this investment must fulfil Shariah requirements.

2. Even if the above investment is in compliance with Shariah, the Islamic investors are as a matter of fact exposed to this LIBOR-linked investment only. How can they be exposed to the risk–return profile of the reference portfolio? There is a growing consensus among contemporary Shariah scholars that a Mudarib can guarantee a return of a benchmark (another indisputable return) if he can unambiguously prove to the investors that his investment strategy is capable of generating such a return in a Shariah compliant way.

3. This takes us to the third Shariah issue in the present CDO structure – the arrangement between the originator/arranger and the super senior note-holders. In the conventional context, the senior-most tranche will be based on interest, just like other notes. However, in a Shariah compliant structure, the relationship between the originator/arranger must be based on a couple of promissory notes, which generates the economic effect of an interest-based transaction. The promises are now widely used in Islamic structured products and are accepted as useful Shariah compliant instruments.

4. It is important that the reference portfolio should comprise Shariah compliant assets. There are a number of Shariah compliant assets like Sukuk, Ijarah and Murabahah portfolios and equities, available for securitization, which may be included in the underlying portfolio. However, the issue arises how such an arranger can have exposure to such a portfolio. In the conventional context, an arranger/issuer may buy a portfolio or sell an instrument like credit default swap to gain exposure to a chosen portfolio, but these options may not be viable given the limited acceptance of trading in debt or conventional swaps. There are different ways of constructing a Shariah compliant swap to have exposure to a reference portfolio. One such technique is called an "Islamic plug," an innovative structure developed by Dar Al Istithmar and used in an increasing number of Islamic funds and structured products.

One possible structure of an Islamic CDO is represented in diagram 2 below. The structure revolves around a Mudarabah in which Islamic investors and the originator invest. The Mudarabah issues different classes of share (like the notes issued by an SPV in a conventional CDO); while fixed return shares are held by Islamic investors, the residual shares are retained by the originator/arranger, who also serves as a Mudarib. The Mudarabah offers different returns linked with the reference portfolio to Islamic investors in accordance with the terms of the shares issued. In addition, the originator may issue a note (based on two unilateral promises) to have liquidity facility to cater for early redemptions and/or shortfall in return to be offered to the shareholders during the term of the CDO.

The originator can have exposure with the help of an "Islamic plug," as mentioned above. Islamic plugs allow a Shariah compliant entity to have exposure to a non-Shariah asset, while observing Shariah requirements. The idea behind Islamic plugs is rather simple. It makes use of the Shariah permission that the two transacting parties can agree on an off-market price and that the price, once paid to a non-Shariah seller, can be used in any activity (including in activities which are not permitted for Muslims).

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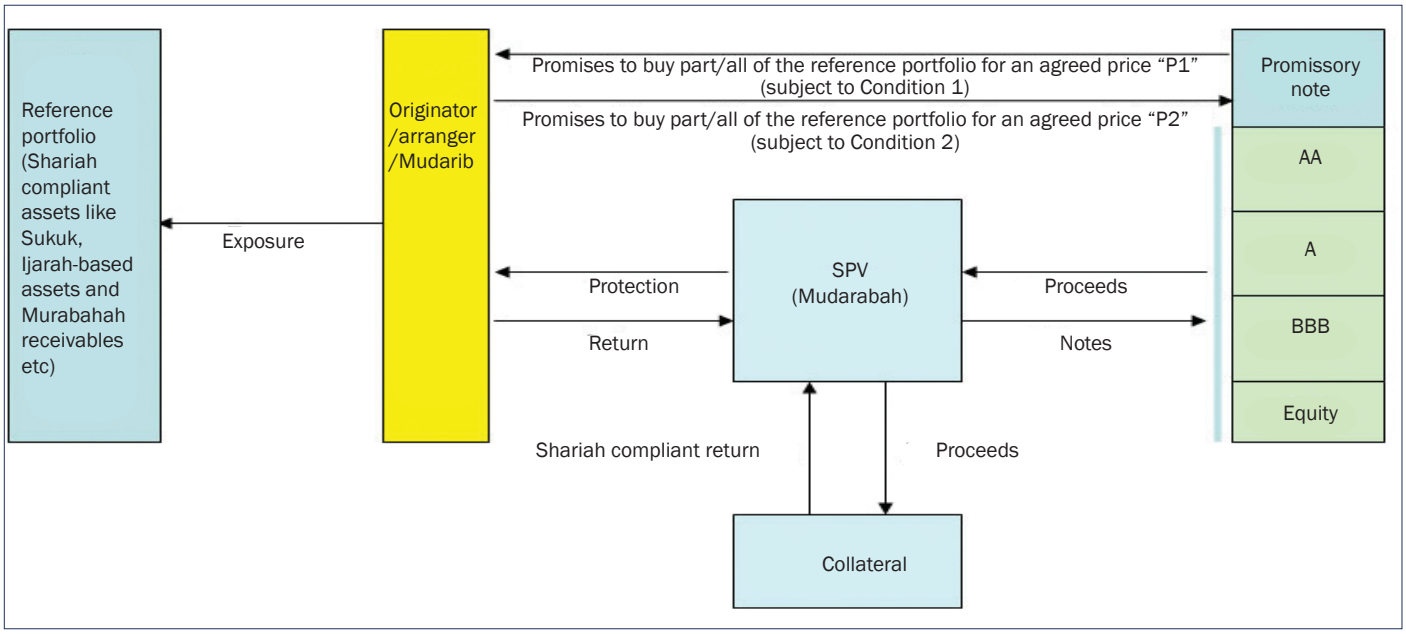
Islamic Collateralized Debt Obligations *(continued...)*

Diagram 2: A possible structure of an Islamic CDO



The above-mentioned structure is rather a purist one. In fact, Islamic plugs can be used to structure an Islamic CDO of CDOs, which allows Islamic investors to have direct exposure to conventional CDOs by investing in shares of a Shariah compliant company. The underlying principle is very simple and those with good structuring minds can very easily unlock a solution!

Dar Al Istithmar دار الإستثمار

Dr Humayon Dar is an Islamic economist currently serving as managing director of Dar Al Istithmar, a joint venture company of Deutsche Bank.

The Evolution of Islamic Hedging Solutions

By Azrulnizam Abdul Aziz

Introduction of commodity Murabahah products

Commodity Murabahah products were introduced to the Malaysian market with the aspiration of offering alternative solutions and to attract more customers. The emergence of these products has meant that customers have greater choice of Shariah compliant products, enabling them to participate and to be competitive in the global banking industry. In addition, the commodity Murabahah modus operandi meets Shariah acceptable standards in most regions and countries.

The development of commodity Murabahah products, particularly in Malaysia and South-East Asia, started with the introduction of commodity Murabahah deposit and financing solutions. Using a similar framework and mechanism, Islamic hedging solutions were then introduced. The Islamic industry has been in dire need of risk management tools and solutions to complement investment, project financing and capital raising requirements. A number of institutions have been trying out different structures and mechanisms to create viable solutions and the development is still ongoing.

This article is written with the intention of sharing information on commodity Murabahah products, including the deposit, financing and Islamic hedging solutions.

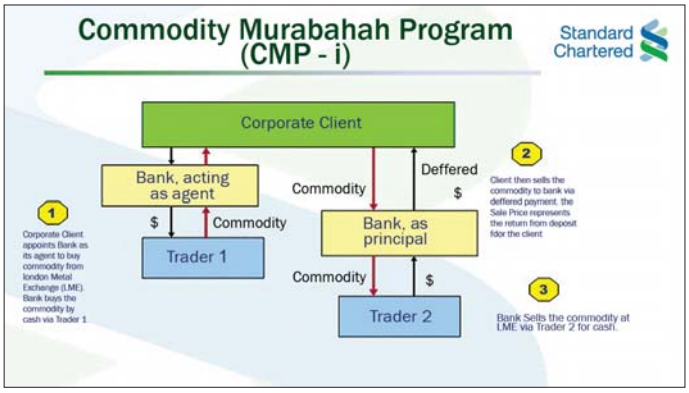
Commodity Murabahah Program-i (CMP)

CMP-i serves as an alternative deposit product for corporate and institutional clients, based on a globally acceptable Islamic structure. Unlike a deposit or loan contract involving a borrower and a lender, the CMP-i product is based on a sale and buy-back contract which complies with the Shariah principles of Murabahah. The product offers features such as fixed return with an unlimited deposit size. The Murabahah transaction involves the purchase and sale of metal commodities such as aluminum, zinc, tin or copper as the underlying assets. The current arrangement is via metal traders based in London. There is no commodity price risk to clients. The modus operandi or the mechanism of the transaction is shown below (see figure 1).

CMP-i documentation required is as follows:

a. Master agency agreement.
b. Schedules of offer and sale.
c. Cost–traders commission.

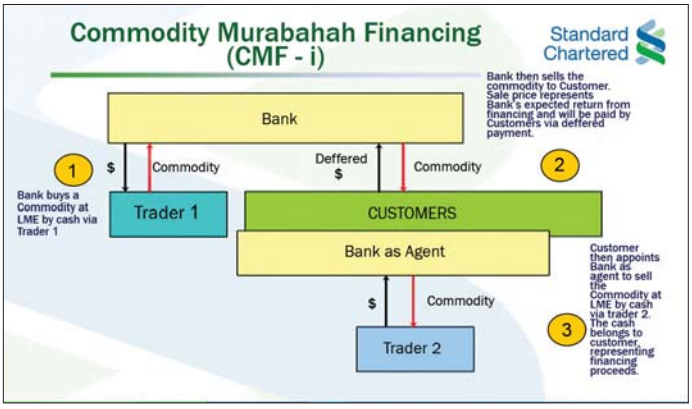
Figure 1



Commodity Murabahah Financing-i (CMF)

CMF-i serves as an alternative financing product for corporate and institutional clients. The product mechanism is basically the reverse of the CMP-i (please see figure 2). This product will provide working capital financing for corporate clients without the client having to have ready assets. Documentation requirements for this product are very much similar to the CMP product.

Figure 2



Islamic hedging solutions

IPRS, ICCS and IFRA

The Islamic Profit Rate Swap (IPRS) was introduced to assist in the management of profit rate risks, thus enhancing cash flows. Profit rate swap is a mechanism structured to allow bilateral exchange of profit streams using two parallel and back-to-back Islamic marked-up sale transactions (Murabahah). It comprises of three possible structures, namely the IPRS, Islamic Cross-Currency Swap (ICCS) and Islamic Forward Rate Agreement (IFRA).

continued...

The Evolution of Islamic Hedging Solutions *(continued...)*

In IPRS, a series of Murabahah sale and purchases are conducted, allowing parties to swap or exchange profit rates from fixed to floating rate or vice versa (see figure 3 below).

In ICCS, the same mechanism can also be applied for the purpose of cross-currency swaps. The Murabahah sale and purchase will be transacted involving one currency in exchange for another. The objective is for the parties to exchange one income stream of currency with another, for example Malaysian ringgit to US dollar.

The IFRA is similar to the IPRS, where there is an agreement between two parties to conduct a Murabahah transaction in a single specified profit period.

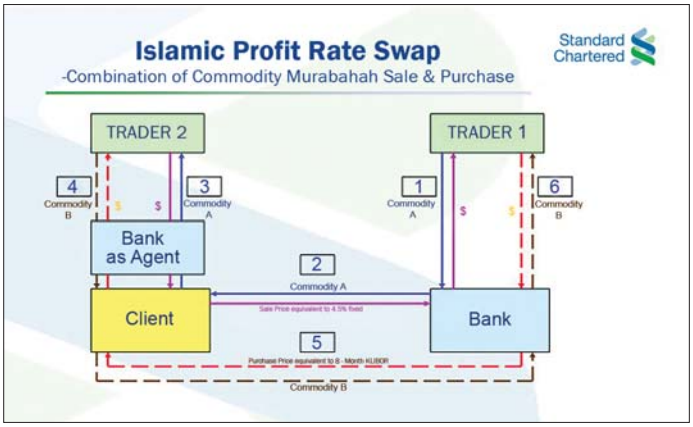
The pricing of all these Islamic hedging solutions depends on the rate of profit, which will be agreed upon by the bank and the client. The period of the swap ranges from one to five years.

Documentation required includes the following:

a. Master agreement between the bank and the clients.
b. Murabahah purchase agreement and Murabahah sale agreement.
c. Murabahah terms and conditions.
d. Agency agreement.
e. Letter of framework.

The products above were designed to have minimal balance sheet implication.

Figure 3



Step 1: Bank (as principal) buys Commodity A from trader 1.
Step 2: Bank sells Commodity A to customer for a price of "P + SFR."
Step 3: Customer sells Commodity A to trader 2 (through bank as its agent).
Step 4: Customer buys Commodity B from trader 2 (through bank as its agent).
Step 5: Bank buys Commodity B from customer for a price of "P + LIBOR."
Step 6: Bank sells Commodity B to trader 2.

"The availability of hedging products is imperative for the industry to compete with its conventional counterparts, especially in the corporate and institutional markets"

Issues and challenges

Islamic hedging solutions are not easy to structure within the framework of Shariah. However, we have seen positive developments among the industry players, and the Shariah scholars have been playing a vital role in providing support and guidance towards the development of these products. In addition, the regulators have been supporting the initiative and have been instrumental in providing direction, supervision and approval for products.

Familiarization and adaptation are another issue faced by all parties, including the bank and the clients. Time was required by all parties involved to understand the product, the processes and procedures. In many instances, parties may have to organize meetings involving personnel from treasury, legal, Shariah and others.

Legal documentation and standardization are also key issues that industry players have to manage and comprehend. Efforts are being made to provide a common platform for the industry to rely on, especially regarding legal agreements.

Conclusion

Islamic banking and finance is still in dynamic mode. The availability of hedging products is imperative for the industry to compete with its conventional counterparts, especially in the corporate and institutional markets. In the case of Islamic hedging, there have been encouraging developments by industry players in introducing different structures with different mechanisms, resulting in global perspective for the industry.

Standard Chartered

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Trading Potential in Sukuk and Equities

By Ijlal Alvi & Dr Azmir Agel

In the development of the Islamic capital and money market industry, an avenue that has gained much interest is the issuance of short-term dated Sukuk that has enabled the increased potential of Islamic cross-border equities trading.

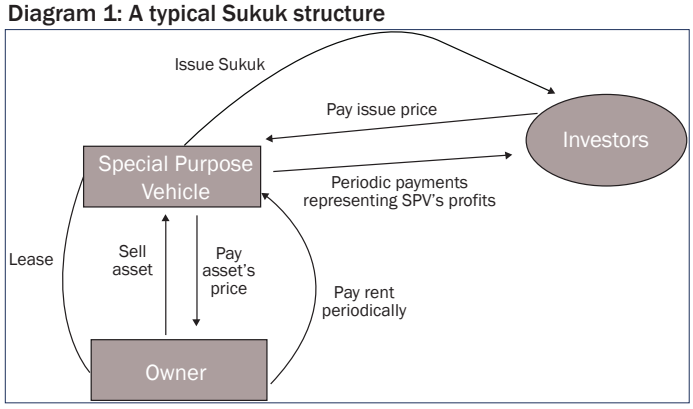
Short-term dated Sukuk

The issuance of short-term dated Sukuk is very much in its infancy stage but there is major growth potential. Lead by countries in the Middle East such as Bahrain and in South-East Asia, such as Brunei and Malaysia, short-term dated Sukuk has managed to offer Islamic investors new financial instruments for investments.

The development of Islamic short-term Sukuk as investment products also means the creation of another asset class, appealing to both Islamic and conventional investment houses and investors at large. The short-dated Sukuk could be a way of mobilizing Islamic funds across jurisdictions and across the globe.

The management of short-term Sukuk can lead to a better form of liquidity management, since there is little risk involved. These short-term Sukuk can assist the process of liquidity management for Islamic financial institutions. However, due to the lack of Sukuk, there is a shortage of these financial instruments in the current market, and this places a limit on investors. The Central Bank of Bahrain (CBB) issued one of the first short-term Sukuk in August 2005. This six-month Sukuk was oversubscribed by more than 200%, which supports the fact that there is a shortage of these financial instruments in the market.

Diagram 1: A typical Sukuk structure



Enhancing liquidity

Currently, Islamic financial institutions are seeking ways to diversify their portfolios and increase their portfolio size of tradable instruments with a fixed income profile. The industry requires Sukuk funds for retail distribution, and once the concept becomes more popular, demand for Sukuk issues will surge exponentially. One way of enhancing liquidity is by issuance and pooling of a constant and large number of investment instruments rather than undertaking one large project issuance, and therefore giving the market many options to actively buy and trade instruments, enhancing capital flows while at the same time reducing the substantial transaction costs that are usually associated with large issuance. A short-term Sukuk money market will be ideal for these institutions, as Sukuk both comply with Islamic law and offer diversity.

Catalyst to an active secondary market

The pre-requisites for the development of an active secondary market start with the basic premise of the structure of the financial instruments and having adequate and consistent documentation that transcends jurisdictions and allows the easy start up of issues. The issuance must be attractive to investors and structured to ensure that it is acceptable to investors. In addition, there must be voluminous issues to allow trading and transactions to take place. This is where short-dated Sukuk can help to proliferate the market.

An active market needs good primary market structure, uniformity and standardization of documents. The short-term dated Sukuk – if structured correctly – would be the vehicle, from the onset, to allow active trading on the secondary market and permit cross-border transactions trading instruments. In short, the starting place for a successful secondary market begins with the structure of the issue itself and the primary market.

Mobilization of funds across jurisdictions

In view of the great growth in Islamic countries and jurisdictions, the refocusing of investment strategies and the fact that Islamic banks, investment houses and corporates have been announcing record-breaking profits, there is now a huge surplus in liquidity from primary investors which could be channeled and mobilized for cross-border investments, especially for short-term Sukuk and equity securities.

Enhancing the mobilization of funds would allow the development of the inter-bank money market, providing an opportunity for short-term Shariah compliant instruments and securities, which are far more flexible than fixed mid to long-term investments. Short-term instruments are also a means by which treasurers can invest their surplus liquidity, especially Shariah compliant instruments and that are fully backed by assets.

continued...

Trading Potential in Sukuk and Equities

(continued...)

Cross-border equities trading

The biggest challenge for Organization of the Islamic Conference (OIC) economies and countries is that of globalization. However, on the positive side, globalization has also brought about an impressive increase in trade and investment flows, technological progress and economic integration among OIC countries.

Islamic cross-border equities trading is presently very much centered on private investments rather than direct equity investments. Much Islamic investment in equities is done through international fund managers who manage based on a mandate from investors and through portfolios. The major issues involving cross-border trading are the availability of a range of Shariah compliant instruments and their sophistication; the attractiveness of the instruments to market investors; acceptable returns for the investments; the awareness of market professionals to transact in the market; the education of investors; and the commitment of the investors themselves.

"One way of enhancing liquidity is by issuance and pooling of a constant and large number of investment instruments rather than undertaking one large project issuance"

Cross-border equities trading for OIC countries

Cross-border equities trading is a necessity for OIC countries. When funds are mobilized and invested in order to fund infrastructure and development projects, industrialization, technology and to provide funds and capital to local start-up companies to enable them to become regional and global market players, cross-border equities trading has been said to be the driving force of a nation's economy. These opportunities have not escaped the mind of the leaders of the OIC.

There is a need for enhancement in the areas of cross-border equities trading. Islamic nations need to improve their investment climate and provide adequate infrastructure to ensure efficient investment flows and thus ensuring sustainable economic growth.

Strengthening the market

Intra-OIC investment flows should be increased, with countries initiating and developing long-term policies and plans to encourage cross-border investments and at the same time lowering barriers to these investment flows. Global Islamic equities cross-border flows are further impeded by the lack of market players. To overcome this, there must be a strengthening of cooperation among specialized institutions to promote cross-border equities flow plans and programs. It is inadequate to merely have listings of Shariah compliant stocks and shares as proof that Islamic cross-border equities are on the rise, while the real measure of tradable volume and the value of those shares is still low, along with the percentages of ownership by Islamic investors.

continued...

Trading Potential in Sukuk and Equities *(continued...)*

Clearing and currency issues

There are also issues of clearing and settlement of Islamic investments and equities flows that need to be taken into consideration, as well as currency denomination issues that are not yet settled in the Islamic finance industry, despite initiatives by institutions such as the International Islamic Financial Market (IIFM) in bringing together some uniformity and standardization in the Islamic finance industry to bring the Islamic finance industry to the next level of growth.

Moving forward in providing solutions to the industry, there is a need for the Islamic finance industry to provide support to one another in international forums, to help strengthen this collective effort and to encourage co-operation between financial institutions to support cross-border projects and to share experiences.

Organization of Islamic Conference Countries GDP

Country	Year	GDP (purchasing power parity (PPP))	Rank	Percent change	Date of information
Bahrain	2006	US$15.9 billion	125	22.21%	2005 est
Bangladesh	2006	US$305.9 billion	31	10.95%	2005 est.
Egypt	2006	US$304.3 billion	32	-3.79%	2005 est.
Indonesia	2006	US$869.7 billion	15	5.11%	2005 est.
Iran	2006	US$569.9 billion	19	10.30%	2005 est.
Jordan	2006	US$26.85 billion	101	5.29%	2005 est.
Kazakhstan	2006	US$125.3 billion	56	5.83%	2005 est.
Lebanon	2006	US$22.78 billion	110	20.98%	2005 est.
Malaysia	2006	US$287 billion	33	25.16%	2005 est.
Morocco	2006	US$135.1 billion	54	0.37%	2005 est.
Oman	2006	US$40.39 billion	86	6.04%	2005 est.
Pakistan	2006	US$395.2 billion	26	13.79%	2005 est.
Saudi Arabia	2006	US$346.3 billion	27	11.64%	2005 est.
Tunisia	2006	US$82.85 billion	63	16.89%	2005 est.
Turkey	2006	US$584.5 billion	18	14.90%	2005 est.
UAE	2006	US$115.8 billion	57	81.88%	2005 est.

Source: CIA World Factbook
https://www.cia.gov/cia/publications/factbook/index.html

OIC equity markets
(Source: Compiled from World Development Indicators -2006)

Country	Market capitalization		Market liquidity	Turnover ratio
	US$ millions 2005	% of GDP 2004	Value traded % of GDP 2004	Value of shares traded % of market 2005
Bahrain	17,240	–	–	4
Bangladesh	3,035	5.9	1.6	32.3
Egypt	79,672	48.9	7.1	42.4
Indonesia	81,428	28.4	10.7	54.8
Iran	46,995	28.8	8.1	21.7
Jordan	37,639	159.6	46.3	85
Kazakhstan	3,941	9.7	2.4	22
Kyrgyz Republic	34	1.5	3	205.3
Lebanon	4,929	10.7	0.9	25.5

Country	Market capitalization		Market liquidity	Turnover ratio
	US$ millions 2005	% of GDP 2004	Value traded % of GDP 2004	Value of shares traded % of market 2005
Malaysia	180,346	160.6	50.6	26.9
Morocco	27,220	50.1	3.4	16.4
Oman	15,269	26	7.4	29.8
Pakistan	45,937	30.2	76.9	375.7
Saudi Arabia	646,104	122.2	188.8	231.7
Tunisia	2,876	9.4	0.8	16.8
Turkey	161,537	32.5	48.7	153.9
UAE	30,363	34.3	4.3	-

(Source: Compiled from World Development Indicators -2006)

This article was co-authored by Ijlal Alvi (chief executive officer) and Dr. Azmir Agel (head of capital market and support services) of the International Islamic Financial Market

Shariah Products - The Road Ahead

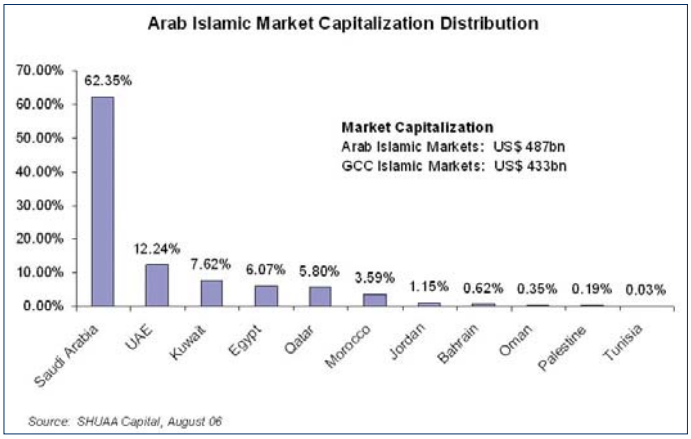
By Sonia Borg

This article aims to provide an overview of the Islamic financial services industry in the GCC and the MENA region. It assesses the potential for future growth and identifies existing challenges to that growth. It also attempts to identify possible solutions for these challenges.

The Islamic financial services industry

Today's Islamic banking world emerged in the early seventies to coincide with the first Middle East economic boom. Simultaneous to the surge in oil revenues was a spread of Shariah compliant banking from the Gulf States to other countries – westwards and eastwards.

In the GCC and the MENA region today we count approximately 63 major banking institutions. In 2006 SHUAA Asset Management* estimated that conventional and Shariah compliant assets under management in the Arab world stood at 7% of combined Arab market capitalizations, reaching approximately US$60 billion. SHUAA Asset Management estimates that 55% of these assets are managed in a Shariah compliant manner with 70% constituting the regional funds sector *(SHUAA Asset Management, September 2006)*.



Future growth

The figures for the growth potential of the nascent Islamic financial services industry are striking, confirming a prominent trend towards Shariah compliant products. SHUAA Asset Management forecasts that combined conventional and Shariah compliant fund assets under management will grow organically to US$160 billion by 2010, representing a compound annual rate of return of more than 23%. Assuming that the Islamic component of 55% remains at current levels, we are expecting Islamic assets under management to grow from US$33 billion today to US$88 billion by 2010.

The more likely scenario is that we will also experience growth in the proportion of Islamic fund assets in comparison to conventional assets. This assumption arises from the perception that popularity of Shariah compliant products is rising amongst non-Muslim populations as well as in Muslim communities both in Muslim countries and in the west. In addition, conventional banks both regionally and internationally have joined the bandwagon and have themselves created Islamic windows to enable them to manufacture and market Shariah compliant products to their clients worldwide.

Challenges and solutions

Such unprecedented growth does not come without its challenges.

If one were to consider the nuts and bolts of conventional financial systems worldwide and transpose those characteristics to a hypothetical Shariah compliant financial system, the essential components necessary for order, progress and development become easily identifiable.

Any established financial system tends to have a central regulator whose principal activities include overseeing market participants according to a set of generally accepted market rules and regulations. These market rules and regulations are developed after in depth consideration of a universally accepted code of market behaviour and based on a set of generally accepted accounting principles. The aim is to ensure transparency and fair play amongst all market participants.

The regulator is also entrusted with ensuring that all participants behave according to those market rules and regulations and, perhaps more importantly, it operates within a legal system which allows it to deter and punish foul play. In cases where it detects foul play, it is normally able to take enforceable action to protect the other participants.

Another very important role of a conventional financial regulator is that it approves new market players and oversees existing participants. It is entrusted with certifying professionals within the industry such that any certified members become accountable to the regulator and, in the case of an individual, to the employer too. Individual certified members are held personally responsible for their conduct when participating in market transactions.

continued...

Shariah Products - The Road Ahead *(continued...)*

The main obstacle in the development of Islamic finance market today is supply of Shariah compliant products and the time required for such products to reach the market rather than demand by investors. For the likes of SHUAA Asset Management – a 'kitchen' for financial products, the process of creating new Shariah compliant products is fraught with bottlenecks, stemming from the absence of certain necessary components for an Islamic financial system.

"The process of creating new Shariah compliant products is fraught with bottlenecks"

Furthermore, varying interpretations of Islamic religious principles mean that the same financial instrument may not be acceptable internationally or across schools of Islamic thought represented by the scholars sitting on various Shariah boards. The resulting difficulty in endorsement and subsequently the inability to distribute such products to clients makes it problematic for financial services institutions to produce 'one size fits all' products.

The absence of a universally approved central religious authority to authorise new products has forced banks and financial institutions to appoint their own Shariah boards. The Malaysian model attempts to circumvent this challenge by requiring only central bank approval of Shariah complian products. This solution has not proven to be successful for the endorsement and distribution by banks and financial institutions in the GCC of most Shariah compliant products approved and regulated in Malaysia.

By way of a solution in the short term, financial institutions could focus on manufacturing tailor made products which stand a better chance of being accepted and approved by the Shariah boards of institutions in countries targeted for distribution.

In the medium to long term, a central council of Shariah scholars would go a long way towards solving the issue of lack of uniformity in the interpretation of Islamic principles. Furthermore, suitable accounting principles – or Generally Accepted Shariah Principles (GASP) which are tailor made to the needs of an Islamic financial system and which are generally accepted by the different schools of Islamic thought are not only necessary but would also set a benchmark for reporting standards across the Islamic markets. This would add weight to the integrity of newly created and existing Shariah compliant products manufactured by institutions worldwide. It would also allow both conventional and Shariah compliant financial services institutions to create innovative products within a shorter timeframe. An added benefit would be the elimination of variables such as choosing the right scholars based on where the product is to be distributed. In addition, it would do away with the need for these same financial 'kitchens' to tailor make the same products to suit their target institutions.

Finally, the industry suffers from a lack of product breadth due to the dearth of financial instruments which are available. The proposed central religious authority would work closely with conventional banking institutions to create flexible solutions and instruments which would be acceptable to the Shariah compliant investment world. It would use a generally accepted code of religious interpretations which would constitute the core of an Islamic regulatory framework. Such a regulatory framework would ideally be approved and recognized by central banks in countries targeted for distribution – thus facilitating endorsement by both Islamic and conventional banking institutions in that country. On the other hand, such products could be easily approved by central banks and regulatory authorities worldwide – enabling financial services institutions and banks to tap the growing Muslim populations in the west as well as other interested investors.

Conclusion

Islamic assets under management are on the rise thanks to the growing populations in Muslim countries and the emerging trend of popularity of Shariah compliant financial products amongst Muslims and non-Muslims alike. Investors were traditionally limited to socially responsible investment as an option for ethical investment. Today they can avail themselves of Islamic products too. This adds weight to the argument for a fully fledged Islamic financial system complete with its own set of regulations and systems. Such a system would ease the training and appointment of much needed additional scholars. It would also ease the grooming of professionals within the Islamic finance industry.

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** SHUAA Asset Management is a division of SHUAA Capital psc. SHUAA Capital psc is licensed and regulated by the UAE Central Bank and by Emirates Securities and Commodities Authority ("ESCA").*

Islamic Wealth Management

By Yousif A. Juma

It has been quite a ride. Pushing harder and harder, Islamic investment banking has been growing at a rapid pace over the past decade. With demand for Shariah compliant investment solutions continually on the rise, investors are encouraging banks in the region to challenge current practices and evolve the system, making for a value added relationship. On the back of record oil prices, the banking sector has prospered in recent times, regardless of the performance of the local equity markets. In reality, the recent correction in the markets has only helped to bolster the roll of Islamic investment banking as a more convenient and lower risk alternative to going it alone.

By emphasizing a customized banking experience, Islamic financial institutions have sprung up all over the region. These banks have seen enormous success as providers of investment products by offering structured products in such diverse areas as real estate development, private equity, venture capital and alternative investments. Islamic products using different structures have been the most popular Shariah compliant investments offered in recent times.

With the record budget surpluses being registered in regional economies, serious money is being made at the local level. Islamic Wealth Management (IWM) is seen as a service that can best cater these growing needs. Banks are trying to shift their clients into a wealth management system which offers Shariah compliant services and products. Even though these services have been available in Europe for many years offering conventional services, the aim now is to shift these clients and their assets back to the Middle East. In order to help this trend, they have turned to IWM.

The total market size of IWM target assets is estimated to be somewhere in the region of US$600 billion. By 2013, the assets of Islamic banks are expected to grow to more than US$1 trillion. This is a sign that local banks need to up their game. In this fast-paced business environment, setting up a Shariah compliant wealth management program is vital in securing major clients. In Bahrain, arguably the premier banking and financial services hub in the Middle East, banks are at the forefront of applying new methods and testing new services to better support their role as a local hub for IWM activity. Centers like Dubai, and more recently Qatar, are introducing new regulations aimed at seriously competing to attract foreign institutions and investors in this field.

> **"This is the time for financial institutions to rise up and challenge themselves"**

Islamic wealth management is the next logical step up from simply providing high yielding investment products. In the past, Islamic investment banks maintained clients on a per product basis. Now, as these products and investments have gained the trust and backing of the biggest investors in the region, banks need to offer a more hands-on approach and look after the investor's assets as a whole. These assets should be fully utilized and a proper balance should be struck in diversifying these assets.

Gulf Finance House (GFH) Investment Bank for one is looking to undertake this initiative, moving its clients into a more dedicated Islamic wealth management program. By transforming the bank's product line using its extensive experience in the region, GFH aims to create a dynamic portfolio for all of its high net worth clients. The aim of its approach is to create a harmony of products and solutions to cater to this growing class of investor. This may be achieved through the client's risk assessment and better asset allocation of client resources.

As an Islamic investment bank, GFH has achieved immense success in structuring products that yield exemplary returns since being established. Real estate projects like the Bahrain Financial Harbor and Al Areen Resort and Spa were all projects financed by our prominent client base. In seven years of operations, we have kept our clients satisfied and optimistic about all our upcoming projects. Now, after gaining the trust and respect that the market demands, GFH is looking to create a better, more prosperous partnership with investors by adding value to their already profitable portfolios.

By analyzing clients' total assets, wealth managers can measure the risks and returns associated in the existing account class, while offering a wide range of customer requirements including wealth generation, preservation and accumulation of that wealth. In order to achieve the greatest possible return, a complete process is needed, developing a thorough understanding of the customer's needs, offering

continued...

Islamic Wealth Management *(continued...)*

innovative solutions, while enhancing customer service delivery.

In order to create returns, wealth managers need to understand what it is the client wants and what his future ambitions are. This, coupled with the bank's extensive resources, will go towards striking a delicate balance between the total risks and the possible returns. Portfolios need to be diversified through equities, Sukuk, Surabaya, structured products, alternative investments like private equity, as well as absolute return products like Islamic hedge funds. Islamic hedging is a modern new method that is still under development which wealth managers can apply to client portfolios.

"Islamic wealth management is the way forward"

The potential of the Islamic wealth management industry is clearly present. This is the time for financial institutions to rise up and challenge themselves. High net worth individuals are on the rise in the region and this is time to capitalize on the change. More and more people are prospering in the Middle East following a successful past few years. World oil prices have reached record prices, pumping more money back into local industrial, construction and manufacturing businesses, stimulating the economy and creating more wealth throughout.

Islamic wealth management is the way forward. For it to move forward, Islamic investment banks need to challenge the culture of ignorance and educate its clientele. The coming years will be testing times for wealth managers as clients learn to accept these new practices and embrace them. The benefits are not just limited to short-term gains, but make for a long-lasting value-added relationship.


Gulf Finance
House

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The Scope of Islamic Investment in Indian Equities

By Shyam Kumar

A relatively new concept a decade ago, Islamic banking and finance has seen explosive growth in recent years. This can be attributed to the fact that many predominantly Islamic nations have seen an increase in financial wealth due to a surge in exports and high oil prices. This increasing income is fuelling an ever-growing demand for Shariah compliant offerings along ethically aware Islamic principles as an alternative to western banking and investment products.

While Shariah compliant investment avenues are now becoming available in most countries, India has not seen large-scale development. Apart from a handful of Shariah compliant funds, currently India offers limited options for investors looking at Shariah compliant investing. However, this should not undermine the scope for Shariah compliant investment opportunities in India.

Since the 1991 liberalization reforms, India's GDP has consistently grown at over 5% and has now crossed the 8% mark. When compared to the US figure of less than 3% and European growth rate of 2% on a 10-year average, this figure is remarkable [1]. In fact, with its population qualifying as a huge yet untapped consumer market and relatively cheap labor, India is expected to be one of the world's two largest economies by 2050[2]. The huge capital inflows into the country mirror the confidence of foreign investors in the Indian economy's ability to match this expectation. Foreign institutional investor flows have shown a consistent upward trend, with the total for the current financial year (ending in March 2007) standing at US$7.99 billion on the 29th December 2006[3].

> **"Out of the 1,000 NSE listed companies, 335 are Shariah compliant"**

India's institutional framework is well suited for the world economy. Corporate India has been performing well and this factor, coupled with strong macroeconomic fundamentals, growing industrial and service sectors, provides great potential for investment in the Indian economy. In fact, India ranks higher than other BRIC nations in the World Economic Forum's Global Competitiveness report. (BRIC refers to the countries of Brazil, Russia, India and China, which are rapidly developing and are expected to eclipse most of the current richest countries of the world by the year 2050). India scored well in innovation, sophistication of firm operations and adoption of technologies[4].

> **" Investors from across the world who are looking at Shariah compliant investment opportunities could find India an attractive destination"**

India is amongst the most developed and organized markets in the world. Two of India's exchanges are amongst the five largest in the world. India has almost 10,000 listed companies, a number second to none. Asia's oldest stock exchange, the Bombay Stock Exchange (BSE), is India's biggest in terms of listed companies (4,853) and market capitalization (US$797 billion) (as at the 30th November 2006)[5]. By number of transactions, the National Stock Exchange (NSE) and the BSE are the third and fifth largest in the world respectively[6].

The Indian benchmarks – the BSE Sensex and the Nifty – have given annualized returns of 57.3% and 67.05% respectively for the period between December 2005 and November 2006. Between March 2001 and December 2006 BSE market capitalization recorded a jump of over 600%, and for NSE it has been over 589%[7]. Such strong numbers only go to confirm that this is the ideal time to take a call on the India story.

To gauge the scope of Islamic investment opportunities in the Indian stock market, it is imperative to examine stocks that conform to Islamic Shariah principles. A thorough study was conducted by Dr Shariq Nisar, an eminent personality in Islamic finance in India. Below are a few facts from his study that go to prove that there is huge potential for Islamic investing in India[8].

> "Out of the 1,000 NSE listed companies, 335 are Shariah compliant. The market capitalization of these stocks accounts for approximately 61% of the total market capitalization of companies listed on NSE. This figure is higher even when compared with a number of predominantly Islamic countries such as Malaysia, Pakistan and Bahrain, where the share of Shariah compliant market capitalization is 57%, 51%, and 6% respectively of the total market capitalization[9]. In fact, the growth in the market capitalization of these stocks

continued...

The Scope of Islamic Investment in Indian Equities *(continued...)*

was more impressive than that of the non-Shariah compliant stocks.

The software, drugs and pharmaceuticals and automobile ancillaries sector were the largest sectors among the Shariah compliant stocks. They constitute about 36% of the total Shariah compliant stocks on NSE."

On examining the BSE 500 (mostly India's Fortune 500), the market capitalization of the 237 Shariah compliant companies hovered between 48% and 50% of the total BSE 500 market capitalization during the period of Dr Shariq Nisar's study.

The table below indicates the number of Shariah compliant companies in India during the period of study.

	Mar-02	Mar-03	Mar-04	Mar-05	Dec-05
NSE					
Total number of companies listed	988	988	988	988	1000
Shariah compliant companies	115	137	185	237	335
BSE					
Total number of companies listed	500	500	500	500	500
Shariah compliant companies	95	112	164	196	237

Source: Centre for Monitoring Indian Economy (CMIE)

There are a few Shariah compliant investment vehicles available in India for foreign investors. The Kotak Indian Shariah fund is one such fund which endeavors to achieve capital appreciation by being invested in the shares and equity-linked instruments of companies which the investment manager believes are Shariah compliant as per the Shariah supervisory board.

Conclusion

India is expected to see stellar macroeconomic performance in the coming years. The Indian equity indices have risen around 49% (Sensex)[10] in the past year on the back of strong domestic growth, the improving global competitiveness of Indian companies and robust foreign institutional inflows into India. The huge spread of listed Shariah compliant companies gives the fund managers a wider spectrum and flexibility to identify and invest in future growth sectors and companies. Investors from across the world who are looking at Shariah compliant investment opportunities could find India an attractive destination. In fact, Indian markets may throw up wider options than many Islamic countries. This is what differentiates the Indian markets. Also, as an investor, one would be investing into a country with 1 billion people, a GDP growth rate in excess of 8% and corporate earnings growing in excess of 15%, predominantly out of domestic consumption rather than export dependence.

There is a strong likelihood of a substantial increase in the funds available for Shariah investment as a result of growing wealth in Islamic countries and communities. Complementing this is the fact that India is becoming extremely important for investors' portfolios and long-term Shariah investors will find this story a difficult one to ignore.

The author is director and CEO of Kotak Mahindra (UK) and can be contacted on: +44 207 977 6900.

[1] *Bloomberg*
[2] *BRIC report - 2003*
[3] *www.bseindia.com*
[4] *http://www.weforum.org/pdf/Global_Competitiveness _Reports/Reports/gcr_2006/top50.pdf*
[5] *www.bseindia.com*
[6] *Economic survey 2004-05 ministry of finance, GOI 2005*
[7] *Bloomberg*
[8] *Dr. Shariq Nisar holds a PhD in Economics with a specialization in Islamic Finance. He is investment advisor to Idafa Investments Pvt. Ltd, a Shariah compliant investment management firm in India.*
[9] *Islamic Capital market products: Developments and Challenges, Islamic Research and Training Institute, Islamic Development Bank, 2005.*
[10] *Bloomberg*

Islamic Banking Technology and Solutions

By Dourria Mehyo

Islamic finance is emerging as the fastest growing industry in the financial services market in the Middle East. It is also a growing services market in non-Islamic countries. Although no one figure has been agreed upon, a routinely quoted estimate of the value of transactions in the Islamic banking market is between US$200 and US$300 billion, with a 10–15% annual growth rate expected over the next five years.

The rules and regulations upon which Islamic finance is based and which govern its operations are significantly different than those of conventional finance. The absence of interest is the most important differentiating aspect; this by itself makes the structuring of Islamic products a complex task.

It is not only the growth in the Islamic banking industry that makes banks strive for efficient IT solutions; the growth in the market, in addition to increasing opportunity for profits, also leads to increased competition. As such, banks are becoming increasingly aware that effective information management within their operating environment represents their best chance to maintain their competitive advantage; and this can only be achieved through advanced IT solutions that allow streamlining procedures, consolidating operations, and efficiently processing transactions. Consequently, Islamic banks need to rely on an efficient IT system which is able to handle their significant transaction nature and volumes, and to make available the necessary information to the bank's management on an accurate and timely basis.

The objective of this article is to present the specifications and characteristics needed in an IT solution to support such a growing industry.

Supporting the Islamic banking industry

For proper and efficient Islamic banking operations, a specialized software is essential in order to support the basic concepts of Islamic banking and the distinguishing aspects of the industry. It is not sufficient for the software just to allow the recording and processing of transactions.

The first essential characteristic of the software is that it must be built on Shariah rules and regulations and have embedded in it the related information capturing features. The captured information must fully cater for the different types of Islamic products; i.e. in order to fully record a commodity Murabahah transaction, the details to be captured must relate to the details of the bought and sold products, and cover details related to the suppliers and down payments.

Legal documents and confirmations are an essential part of Islamic banking operations. As such, the IT solution to be utilized must allow the printing of the Islamic transaction's details, the related confirmations and the related legal documents and contracts. Each type of Islamic financing product has its own legal document, and the system must be able to support these, and this applies to all transactions of the bank (with depositors of restricted and unrestricted investments) and with the funded counterparties.

For the efficient and proper operation of Islamic banks, the system must allow the set-up and tracking of restricted and unrestricted investment accounts of the clients across the system as well as obtaining the information on a timely basis.

Since Islamic banking is based upon shared profits and risks, the operations, simply put, cover pooling clients' funds and then distributing the profits based on the revenues generated from these pools after applying certain computations, costs and revenue allocation criteria that are pertinent to Islamic banking. In light of these transactions, the software must support proper recording, tracking and management of the pools of funds. Each pool must be easily tracked to its component accounts and computations must be made on an efficient and timely basis, and affect clients' accounts and produce reports detailing the results of the computations. As such, the system must also support the complex profit computation method for the unrestricted investment accounts and distribution of the computed profits to each account holder. The system must allow the tracking of the financing transactions, the contributors to these transactions and computations of profit to be received from funded (or partnership) parties and computation of the profit shares to be distributed to the contributors based on each client's invested amount. This is important for the restricted investment account holders.

Since Islamic banks must abide by the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) standards, the system must produce the standard accounting entries and booking methods of the transactions and the bank's profits and investments according to these AAOIFI standards.

In an era of banking operations where customer service management concepts are becoming more and more essential for competitive advantage, customer-centricity is

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Islamic Banking Technology and Solutions *(continued...)*

extremely important the banks need to know, from a single click, the total balance position, transactions and operations completed by any client with the bank. This is important for customer service, sales management, risk management and exposure analysis. The IT software to be utilized should be fully customer-centric in order to provide the bank the needed information in the stated above manner and thus to give the bank the competitive advantage of obtaining such information on an accurate and timely basis.

It is a matter of fact that the legal documents and confirmations are an essential part of Islamic banking operations. As such, the IT solution to be utilized must allow the printing of the Islamic transaction's details, the related confirmations and the related legal documents and contracts. Each type of Islamic financing product has its own legal document, and the system must be able to support the maintenance and management of these documents, and this applies to all transactions of the bank with depositors of restricted and unrestricted investments and with the funded counterparties.

The possibility of being able to keep a copy of the signed contracts as a scanned document or another medium in the system is also an important feature. The logging of dates and times of a transaction is another essential factor, as is being able to keep the signed contracts in their related transaction record, particularly since the Shariah audit will be looking at those details.

Needless to say, the technological software must also have a powerful reporting tool that allows ease of access to data and development of all types of reports for the bank's management and the Central Bank's reporting requirements. The system must also be able to integrate easily with other applications for data mining in order for the bank to obtain the reports needed to support its operations.

Finally, the software must also allow the bank to comply with Basel II requirements and the computation of what is needed for such compliance in a timely manner. The software must also allow the Islamic bank to properly record and monitor its market, credit and operational risks.

Conclusion

The right technology is essential for supporting any growing industry. In the current golden era of Islamic banking, the availability and choice of the right solution is extremely important for accompanying such growth and in order for the operations to be efficient and maximize the benefits of the bank, the depositors, the clients and the bank's shareholders.

path solutions

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Bahrain – The World's Islamic Financial Capital

By Jane Dellar

Bahrain can legitimately claim to have laid the groundwork for the development of Islamic banking as a global financial force. Its innovative and forward-thinking approach to banking and insurance services, both conventional and Islamic, has been instrumental in securing its pre-eminent position as an international financial capital.

Meeting the demands of regional investors

There are now hundreds of Islamic banks and investment funds across the world, all offering an array of Shariah compliant products to attract the Middle Eastern investor. Even the most traditional western private banks are launching new Islamic investment products and opening up offices across the Middle East to boost their presence in the region.

Investors in the Middle East are knowledgeable about financial opportunities globally, and are no longer willing to have all their investment dealings managed remotely. Whilst demanding excellence, high performance and exceptional returns on their capital, they are increasingly looking to achieve this through Shariah compliant investments. These investors are not looking for companies that merely pay lip-service to their requirements; they insist that providers of Islamic finance products understand Islam as well as global finance. A strong and visible presence in the region is essential for any institution targeting this growing customer base.

Bahrain's success in the Islamic finance sphere has come as a direct result of its continued determination to push the boundaries of regulation and business practice. This has resulted in a two-fold benefit for the growth of the sector in the Kingdom. Not only does it reassure individual customers, but it also provides Islamic institutions with recognition within the global banking and finance industry as being committed to best practice and transparency. As such openness correlates directly with the principles of Shariah investments, it has been a successful formula for growth.

Rapid, sustainable sector growth

The recent upsurge in petrodollars is an undeniable factor in the phenomenal expansion of the Islamic finance sector in the Middle East and beyond – and scope for future development remains enormous. The Gulf is home to some of the world's richest individuals and families and the number is growing dramatically. There are 300,000 high net worth individuals in the region – up almost 10% on last year. This group holds an estimated US$1.2 trillion worth of wealth, an annual increase of 19.7%.

It is no coincidence that private wealth management and Islamic finance are two of the fastest growth segments both in Bahrain itself and in the industry. Bahrain's Islamic licensed financial institutions saw 30% growth in revenue between February and August 2006 alone. The value of the Sukuk market now stands at US$41 billion according to Moody's credit rating agency. In the insurance sector, HSBC predicts that Takaful will be worth US$14 billion in 2015 – a five-fold increase on the current size of the industry. And increasingly, European and American investors are understanding the opportunities and returns that can be gained from investment in the sector; between 70–80% of Sukuk are believed to be held by non-Islamic investors, according to the European Islamic Investment Bank.

"Between 70–80% of Sukuk are believed to be held by non-Islamic investors"

Innovation and transparency

The Shariah compliant wealth management industry may still be in its infancy, but it is developing quickly. Historical criticisms regarding transparency, liquidity levels and little standardized regulations have been and continue to be addressed; and important steps have been taken to strengthen the industry. The Islamic Financial Services Board (IFSB) – created in 2002 – has recently issued its first two standards, one on capital adequacy and another on risk management. The IFSB is supported by the Accounting and Auditing Organization for Islamic Institutions (AAOFII), which seeks to standardize regulations and accounting procedures across the Islamic world. Bahrain is taking the lead in the region on ensuring that all of its Islamic financial bodies fully comply with AAOFII guidelines.

The Central Bank of Bahrain (CBB) has also developed a number of industry-leading legal and regulatory initiatives to strengthen the environment for financial services organizations. It was the first Central Bank in the world to develop and issue prudential regulations specifically for Islamic banks – the innovative, and now globally recognized Prudential Information and Regulations for Islamic Banks (PIRI). More recent innovations from the CBB include a comprehensive program to modernize and update the licensing framework for all financial institutions in the Kingdom. In addition, a new trust law was issued in August 2006, providing a legal foundation for the creation of trusts.

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Bahrain – The World's Islamic Financial Capital *(continued...)*

The CBB has also established the Wafd Fund – the first of its kind in the region – to fund research, education and training in Islamic finance.

Creating the optimum business climate

Bahrain's geographical location gives the country an enviable advantage. The Kingdom is centred between the European and Asian markets and time zones, and has unrivalled links with its neighbours in the GCC. With the region's largest market, Saudi Arabia, just a 45 minute drive across the causeway from Bahrain, institutions in Bahrain are uniquely placed to benefit from the estimated US$400 billion to US$500 billion of private wealth there. A second causeway linking with Qatar is also due for completion in 2010, providing another direct road link with a major regional partner. This logistical strength combined with its history as a financial leader makes it the natural choice as a regional hub for any company with its eye on the international markets.

The country's Economic Development Board (EDB) is pioneering a joined-up approach to the continued development of the financial sector as an integral part of the economic diversification of the Kingdom. The board is rolling out a strategy for growth covering all factors relating to the successful and integrated development of the economy: from cutting red tape to forward-thinking on investment in infrastructure; from education and training programs to international trade agreements. In developing relationships with public and private sector partners, it is clearly committed to enhancing what is already the freest and most competitive business environment in the region.

Dedicated resource for financial institutions

In May 2006, the Bahrain Financial Services Development Bureau (BFSDB) was established by the EDB as a dedicated financial sector resource. Its remit is to promote Bahrain's strengths and innovative approach to finance on the global stage, and to further the levels of foreign direct investment into the Kingdom.

The BFSDB is dedicated to working with outstanding regional and international partners from the public and private sectors – including the CBB, ministries and trade associations – to support the needs of more than 320 licensed institutions already based in Manama. Of this group, around 50 are Islamic institutions – a number that is growing rapidly. Using its unrivalled network of contacts, the BFSDB is uniquely placed to support financial institutions looking to build or develop a base in the region. It is also fostering the growth of the support services that international financial corporations rely on – from back-end IT and technology providers to legal and administrative services.

BFSDB managing director Jane Dellar says: "Bahrain's regional lead in conventional finance and world lead in Islamic finance is of real value. This position has been gained and retained as a result of the Kingdom's commitment to transparency; effective and fair regulation; a strong legal system; and the outstanding international reputation of the Central Bank of Bahrain. With increased focus on the financial sector from other nations, it is imperative that we continue to make others aware of our regional pre-eminence in the sector. With more noise than ever in the global marketplace, we must ensure our voice is heard and the message is clear. Our team is committed to doing just that."

As part of its role, the BFSDB is targeting large international and leading regional companies across the financial services sector that have yet to build a base in Bahrain. It is also working to attract the secondary sector companies that are essential to provide support and enhance the working practices of licensed institutions.

Dellar says: "The BFSD's role is to identify and target these growth sectors, because by supporting and growing financial services, both Bahrain and business stand to benefit. Not only does the sector contribute 27% of the country's GDP, it also provides jobs. The workforce in the Kingdom has developed in response to the organic and sustained growth of the financial services sector. This means that the population is geared to meet the demands and high standards required by international financial companies."

Conclusion

Bahrain's key strengths lie not only in having the lowest tax environment in the Middle East – with no corporate taxes, no income taxes and no taxes on personal wealth – but also in continued investment in human resources. This is particularly true when looking at the needs of the financial services sector. A skilled local workforce is an increasingly important factor for any business looking to build a home in the Gulf. With continued investment in skills and training programs, Bahrain is looking to increase and exploit its GCC market lead.

It is this type of commitment to thinking of and investing in the long-term that has seen Bahrain develop its current standing as a financial leader. Its continued dedication to remaining both innovative and influential can only serve to reinforce its status as the world's Islamic financial capital.

The author is managing director of Bahrain Financial Services Development Bureau. She can be reached at bfsdb@bahrain.com.

Islamic Finance Industry in Kuwait

By Global Investment House

The benefits of high oil prices have been omnipotent in Kuwait, helped by the adequate reserves and the relatively small size of the country. It is one of the richer countries in the world, with a per capita GDP of US$27,006. The abundance of oil reserves, as well as the various steps taken to increase oil production and export capacity, has set the economy up for high growth, at least in the short to medium-term. Growth is further aided by petro-dollar generated liquidity and the resultant investments in construction projects.

However, sustaining this growth in the longer term remains a challenge and it is contingent upon a number of structural changes in the economy, which are imperative to reduce the dependence on oil. These changes revolve around a shift towards a market-oriented system so as to improve efficiency on all fronts. Although the current boom period provides an opportunity to bring about such changes, not many changes have been actioned, owing to the lack of incentive to try something new in the good times. Nominal GDP for 2005 increased to KD23.6 billion (US$81.64 billion), 35.1% higher than the previous year, while the real GDP grew by 8.1%.

The Islamic financial services industry – comprising Islamic banking, Islamic insurance (Takaful) and the Islamic capital market – is an area that has grown to become an increasingly substantial segment of the global financial market, and has gained considerable interest as a viable and efficient alternative model of financial intermediation. The growing awareness of and demand for investing in accordance with Shariah principles on a global scale has been the catalyst for making the Islamic financial services industry a flourishing one. This is also a reflection of the increasing wealth and capacity of investors – both Muslim and non-Muslim – to seek out and invest in new investment products that serve their needs.

"Close regulatory supervision and policy measures have catapulted the Islamic financial services sector in Kuwait to be one of the strongest sectors in the region as a whole"

The Islamic financial services industry today stands at an estimated size of US$250 billion, growing at 10–15% per annum and consisting of more than 200 financial institutions. It is a product of the collective efforts of bankers, economists and Islamic legal scholars over the past few decades to develop financial solutions that meet the religious requirements of Muslims. It is a young and growing industry, and continues to evolve and expand both financially and geographically. It is indigenous and community-focused: it caters to devout Muslims in indigenous Muslim societies, as well as to Muslim minorities of non-Muslim countries. Furthermore, it is an inclusive paradigm: non-Muslim individuals and communities

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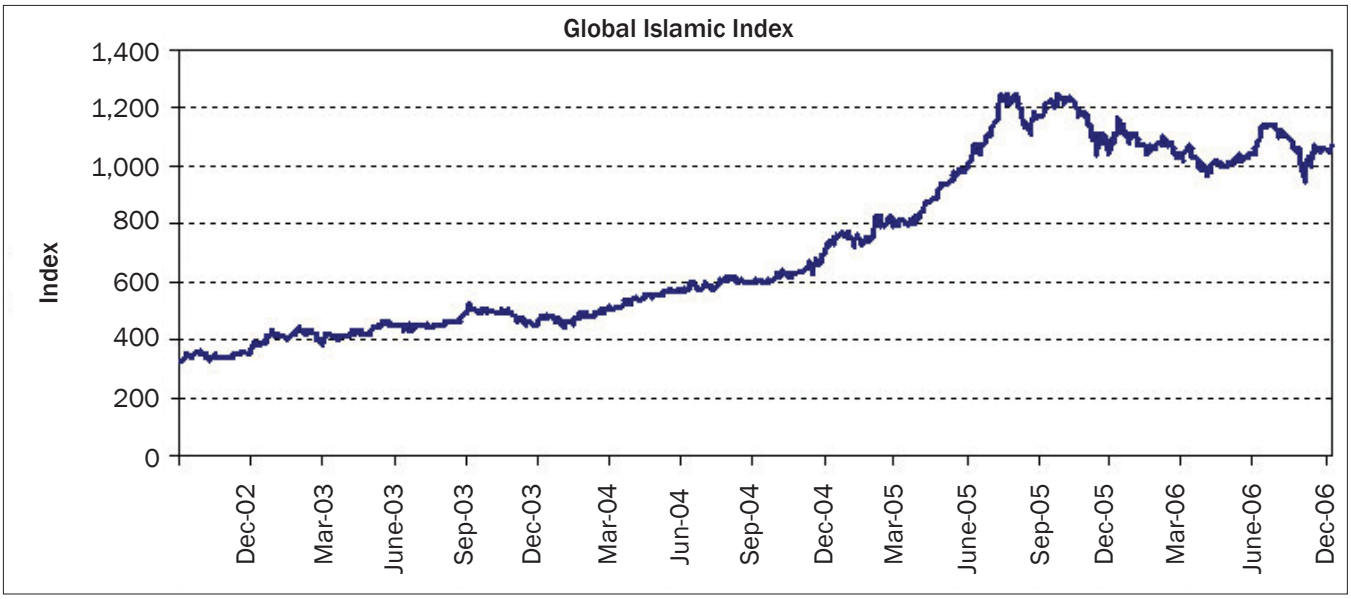

Islamic Finance Industry in Kuwait *(continued...)*

that seek ethical financial solutions have also been attracted to Islamic finance.

The Islamic financial services sector in Kuwait remains one of the important drivers of economic activity, and is expected to gain from the growth of the economy. It continues to benefit from positive business and consumer sentiment, as well as the religious leanings of the country's people. Close regulatory supervision and policy measures have catapulted it to be one of the strongest sectors in the region as a whole.

However, competition in the Islamic financial services arena is increasing. During December 2006, the board of directors of the Central Bank of Kuwait (CBK) approved the application of the Kuwait Real Estate Bank (KREB) to switch entirely to Islamic banking. KREB will become the third Islamic bank in the country, after CBK broke the Islamic banking monopoly of Kuwait Finance House (KFH) in 2004 by licensing the country's second Islamic bank – Boubyan Islamic Bank. The Central Bank has also decided to establish an Islamic bank in 2007 with the government as a major shareholder.

The performance of most banks in Kuwait's banking sector improved during the first nine months of 2006. Net profit growth was led by Islamic bank KFH, which grew by 56.2%. Boubyan Bank reported marginal growth in profitability, growing by 2.6%. The Islamic banking sector in Kuwait will see increased competition with the establishment of new banks and increased pressure on conventional banks to offer Islamic products through their separate divisions. This will require banks to adhere to the latest technological innovations in the banking sector, besides vigorously pursuing the development of new products.

Kuwait banking sector

	Assets		Deposits		Loans	
	9m05	9m06	9m05	9m06	9m05	9m06
NBK	28.5%	26.6%	27.9%	25.6%	27.5%	26.3%
KFH*	19.9%	21.7%	21.9%	21.4%	21.1%	22.4%
GB	11.6%	13.6%	11.6%	16.3%	13.1%	16.1%
CoBK	9.9%	10.3%	9.7%	9.1%	9.7%	10.1%
AA	8.9%	8.3%	9.6%	8.7%	9.5%	8.3%
BB	8.7%	7.9%	8.3%	7.8%	7.1%	6.0%
BKME	7.5%	7.0%	7.1%	7.2%	7.4%	7.1%
KREB*	3.9%	3.0%	3.7%	3.2%	4.3%	3.1%
Boubyan*	1.1%	1.8%	0.2%	0.7%	0.4%	0.6%

Source: Global Research
** Islamic banks*

Kuwait's investment sector contains a large number of companies operating at various scales and levels. There are 70 investment companies registered in Kuwait, of which 30 companies – according to their articles of association – conduct their business in accordance with Islamic Shariah. Islamic companies have been diversifying their asset structure over the last few years to focus and capitalize on the booming investment and real estate market in Kuwait.

"Islamic companies have been diversifying their asset structure over the last few years to focus and capitalize on the booming investment and real estate market in Kuwait"

Kuwaiti companies are spearheading innovation in Islamic bonds (Sukuk), as seen in the US$150 million Musharakah Trust Sukuk issued by The Investment Dar (TID). One of the unique features of the TID Sukuk was that it has both a call and put option for early redemption by either investors or the issuer.

Global Investment House announced the launch of Al Fajer ReTakaful Insurance Company (Al Fajer) as an Islamic reinsurance company with a paid-up capital of KD50 million (US$172.97 million), the first licensed re-Takaful company in Kuwait and the second in the Gulf region. According to Global, international Takaful is expected to grow at a rate of 15–20% per annum over the next 10 years and two to three-fold over the next five to eight years, depending on the industry (although currently not much competition is evident). With the high population growth family Takaful should gain popularity, while the massive projects currently underway in the region will benefit non-life Takaful opportunities.

Islamic funds have played an important role in developing an equity culture among Muslim investors. Out of 79 investment funds, 33 funds operate on Shariah principles. The growth of Islamic funds is improving the market's liquidity and provides risk diversification opportunities for medium and long-term maturity structure, a feature that was lacking in the Islamic capital market. Islamic funds are providing tough competition to their conventional peers in terms of returns and subscription levels. The emergence of Ijarah leasing, as well as privately subscribed real estate funds, has pumped considerable liquidity into the industry and causes no alarm for any abrupt halt in real estate activity.

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Islamic Finance Industry in Kuwait *(continued...)*

Global Islamic Index – constituents

Company	Market capitalization (US$ million)
Kuwait Finance House	9,147.4
The Investment Dar	3,064.0
Boubyan Bank	1,642.9
The Securities House	993.5
Aref Investment Group	826.0
A'ayan Leasing & Investment Co.	764.3
First Investment Company	726.3
Grand Real Estate & Touristic Dev. Co.	684.9
International Leasing & Investment Co.	549.3
International Investment Group	544.8
Alafco Aviation Lease & Finance Co.	440.0
Grand Real Estate Projects	389.0
The International Investor	387.8
Al Safwa Group Holding	376.7
Al-Madar Finance & Investment Co.	353.5
Gulf Petroleum Investment	288.3
Gulfinvest International	284.6
Al-Enma'a Real Estate Company	262.2
Tijara & Real Estate	260.7
Al Shall Consultants & Investment	255.8
Al Dar National Real Estate	253.2
Credit Rating & Collection Co.	251.7
Sokouk Holding Co.	242.5
Haj & Umrah Services Consortium (Mashaer)	227.3

Company	Market capitalization (US$ million)
Osoul Leasing & Financing	214.5
Kuwait Real Estate Holding Company	176.7
Al-Madina for Finance & Investment Co.	167.0
A'ayan Real Estate Company	164.8
1st Takaful Insurance	135.3
Arkan Al-Kuwait Real Estate Co.	125.9
Wethaq Takaful Insurance	94.4
Eyas Higher & Technical Education	94.2
Safwan Trading & Contracting Company	72.8
Al-Muwasat Holding Co.	71.2
National Company for Consumer Industrial	53.4
Excellent Education Company	29.1
Total Market Cap – Islamic	24,615.9
Total Market Cap – KSE	143,857.3

Source: KSE

* Market capitalization as at the 27th December 2006.

The author are from the Global Investment House research department.

Great Demand Ahead for Syria

By Raed Karawani

Following the wide growth in the Islamic banking industry, Syria has issued a special law for Islamic banking which allows Islamic banks to operate and start working in the country.

Syrian banking environment

Syria has recognized the great need to develop and reform its banking and financial infrastructure, allowing the private sector to participate and simultaneously reforming the public sector. Over the past few years a new set of laws and regulations have been issued covering banking law, insurance, the stock market, anti-money laundering and secrecy law, amongst others.

A big demand is expected to materialize for Islamic banking services and products in Syria, as many Syrian corporations have been meeting their Islamic finance needs through neighboring and the gulf countries.

The first Islamic bank in Syria – Al Sham Bank – issued a 25% IPO in December 2006 and saw more than five times oversubscription of the shares offered to the public.

In a survey conducted by Bankakademie International in Syria on more than 650 Syrian enterprises of all sizes in seven governates, it was shown that of the companies that had never requested a bank loan, 34% cited religious reasons for not so doing. Since the Islamic alternative is not yet available in the Syrian market, these people did not then go to conventional banks, because of the prohibition of interest in Islam.

Islamic banking regulation in Syria

After several years of success in the private banking practice in Syria, Legislative Decree No. 35 was issued in 2005, allowing the establishment of Islamic banks in Syria. Many international institutions were keen to invest in this area. Several Islamic banks have already submitted their applications and three of them have received a first approval, with two being licensed officially.

The first two Islamic banks to operate in Syria will be:

1. **Al Sham Islamic Bank**, with a US$100 million capital, and a main shareholder in Al Shall Investment & Consulting Company from Kuwait.
2. **Syria International Bank**: its main shareholder is Qatar International Islamic Bank, with other partners from Qatar and Syria.

The Islamic Banking Law in Syria was issued with a good structure based on the previous experience of other countries relating to their Islamic banking laws and consequent amendments. The law included important issues for Islamic banks in Syria, such as:

- Compliance with the accounting standards issued by the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI).
- Compliance with the capital adequacy standards of the Islamic Financial Services Board (IFSB).
- The law states clearly the requirements for Shariah boards and compliance with all Shariah principles in providing Islamic services and products.

The Syrian Islamic Banking Law requires a minimum capital of S£5 billion (US$100 million), while conventional banks only require a minimum capital of S£1.5 billion (US$30 million). The 49% foreign ownership limit remains the same in Islamic banks as in conventional ones. The law allows Islamic banks to own, sell, invest and rent properties and land and to establish companies and participate in projects under establishment, all in compliance with Islamic rules and principles.

Soon the foreign ownership percentage will increase, allowing more participation from foreign banks in the Syrian market and facilitating banking investment.

"Syria has issued a special law for Islamic banking which allows Islamic banks to operate and start working in the country"

Banking sector reform process

The Central Bank is working on several measures for the year 2007. The Governor of the Central Bank announced a few months ago that several steps will be taken in the year 2007. Some of these important measures are:

- Unifying the exchange rate of the Syrian currency, which has been reduced to only two rates in recent years. Also it has been announced that the currency will be priced according to a basket of foreign currencies, not only the US dollar.
- Central Bank will increase foreign ownership participation in the banks from 49% to 60%, reflecting the big demand from foreign banks and investors to increase their ownership percentage.

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Great Demand Ahead for Syria *(continued...)*

- The issuance of treasury bills, which comes in response to demand from banks to issue treasury bills in order to be able to grant long-term loans and avoid mismatch positions.

Several other measures are in the pipeline and will take place in the coming months. Beside that the Central Bank is training its staff on Islamic banking activities to be able to meet the Islamic banks' needs, as well as for supervision purposes.

"A big demand is expected to materialize for Islamic banking services and products in Syria"

Islamic insurance – Takaful regulation

Reforming the insurance sector will take place along with the bank reform process; the president issued Legislative Decree No. 43 dated 2005 for regulating the insurance market in Syria. The new decree allows private insurance companies to enter the Syrian market, opening the doors to many interested companies from around the world.

The Syrian Insurance Supervision Committee has granted the license for the first Islamic insurance company in Syria to Al Aqila Insurance Company. The capital for this company is about S£2 billion (US$40 million) and the main shareholders are the Kuwaiti Al Aqila for Investment and Finance (taking 32% of the shares), and other investors from Syria and Kuwait. 51% of the shares will be offered in an IPO, and the company will start operations soon.

Another preliminary approval has been granted for two further Islamic insurance companies. These companies are:

- Syrian Qatari Insurance Company
- Al Nour Insurance Company

The law allowed the establishment of Takaful companies, but did not mention any different conditions or procedures for Takaful insurance, except the requirement for clearly stating the type of insurance services on the application, to make clear that the application is for a Takaful insurance company.

The minimum capital required differs depending on how many types of services the company will provide. If the company will provide only general insurance services, the minimum capital required is S£700 million (US$14 million), which is upped to S£850 million (US$17 million) for those providing general insurance services and life insurance. The capital required for reinsurance companies is S£1200 million (US$24 million).

It is expected that Islamic banking and insurance services will give a big boost to the Syrian economy, and increase consumer confidence in the Syrian banking and insurance market.

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Islamic Banking in Jordan

By Professor Said Al Hallaq

Development of the banking system in Jordan

The rapid pace of development in the Kingdom of Jordan has taken place in an environment of strengthening economic growth underpinned by strong fundamentals. The growth has been achieved with relative price stability, moderate unemployment and strong direct investment.

In 2004, the Jordanian economy achieved positive results. Gross domestic profit recorded a high growth rate of 7.7%, doubling its growth rate as compared to 2003, and marking the highest rate since 1992, despite regional instability and a decline in foreign aid. High growth helped to reduce unemployment and boosted public revenues, but the economy also showed signs of overheating, with inflation surpassing 3.4%. On the fiscal side, despite the pressure resulting from the increase in international oil prices and the decline in foreign grants, the general Government budget achieved good results in 2004, with the overall budget deficit declining from 2.5% of GDP in 2003 to 1.9% in 2004. Public debt, notwithstanding the negative valuation effect of the weaker US dollar, also decreased from 98.1% of GDP in 2003 to 89.3% in 2004.

Amid this environment of favorable growth and strong fundamentals, Jordan, under the direct supervision of Head of State King Abdulah the Second King of Jordan, has taken the opportunity to further deregulate and liberalize the Jordanian financial sector, with a view to enhancing its contribution to efficiency and growth. The sector has also continued to be progressively transformed through rationalization among existing financial institutions and the introduction of new institutions. These developments have contributed to the strengthening of the international dimension in the financial system.

The banking and financial services sector is reasonably advanced in Jordan, and foreign institutions are increasingly entering the Jordanian market. Jordan's Arab Bank, however, is still the dominant player in the sector; the Housing Bank for Trade and Finance is the second largest institution.

Jordan has only two Islamic banks, namely Jordan Islamic Bank and The Islamic International Arab Bank. Jordan Islamic Bank started business on the 22nd September 1979 to become the first Islamic bank in Jordan, and has continued its course, conforming to its mission and objectives and enhancing its position in the market. The bank's annual report and financial statements for the year 2005 indicate that Jordan Islamic Bank recorded an increase in profits before tax amounting to JD20.2 million (US$28.51 million), compared to JD4.76 million (US$6.72 million) in 2004, thus recording an increase of JD15.44 million (US$21.8 million) with a ratio of 324.4%, which is the highest recorded ratio since its establishment. The balance of joint investment and financing operations (Mudarabah, Musharakah, Murabahah and other modes of investment) amounted to JD645.5 million (US$911.2 million) in the year 2005, compared to JD536.7 million (US$757.62 million) as 2004, increasing by JD108.7 million (US$153.44 million) with a growth ratio of 20.26%. This growth is very important to emphasize, as the role of Jordan Islamic Bank as the oldest bank in Islamic banking industry in Jordan and as a key player begins to concentrate more on medium and long-term investments.

> **"The role of the Islamic bank in the development of the economy is moving into the right direction"**

This increase shows that the role of the Islamic bank in the development of the economy is moving in the right direction. Jordan Islamic Bank's share of the local market reached 10.8% of the total direct investment facilities of the Jordanian banks for the year 2005. These facilities covered a wide range of economic and social activities and utilities, including hospitals, medical clinics, universities, schools, educational institutions, industrial and real estate projects, in addition to the commercial sector.

The second bank in Jordan is the Islamic International Arab Bank, which was established on the 30th March 1997. The bank recorded an increase in profits before tax amounting to JD2.35 million (US$3.32 million). The balance of financing (Mudarabah and Musharakah) amounted to JD11.18 million (US$15.78 million) in 2005, compared to JD4.085 million (US$5.77 million) in 2004. Total investments financing and receivables amounted to JD165.8 million (US$234 million). The Islamic banking industry has been faced with obstacles and challenges resulting from increased cash surpluses with limited finance and investment opportunities. The Islamic International Arab Bank has proved the ability of its management to cope with new conditions and to dictate wise policies that balance the protection of equity on one hand with the achievement of acceptable dividends for depositors on the other.

The Islamic International Arab Bank is working hard to achieve its goals and to continue to grow, despite the strong

continued...

Islamic Banking in Jordan *(continued...)*

local competition and the difficult circumstances facing the banking industry. To satisfy customer needs, the management is developing new banking services and diversified banking products which are in accordance with the rules and principles of the Shariah.

The Islamic finance industry has grown rapidly, both in terms of the number of institutions and the size of assets. For Jordan, there is strong potential to be a hub for Islamic finance in the area; currently the country has only two Islamic banks, one Islamic insurance company and one Islamic banking window. In order to encourage growth in Islamic finance, regulatory decisions need to be made allowing conventional banks to operate Islamic banking windows alongside their conventional operations, as a first step towards initiating the Islamic banking services industry. At a later stage the Central Bank could change this regulation, requiring conventional banks to open Islamic banking subsidiaries, rather than windows. This move should increase the number of Islamic banks in Jordan.

Why expand Islamic banking services?

There are no accurate statistics about the number of Islamic financial institutions, the volume of business or the growth rate of the sector worldwide. However, rough estimates indicate that there are more than 200 Islamic banks managing about US$300 billion in total assets. This is exclusive of Islamic banking windows and independent funds. The table on the right provides some available statistics about Islamic financial institutions in selected countries. Assets under management by Islamic banks and conventional banks offering Islamic banking services reportedly now exceeds US$400 billion. At present, mutual funds are estimated to stand at over US$300 billion, while issuance of Islamic sovereign and corporate bonds (Sukuk) has reached about US$50 billion.

Islamic finance has demonstrated its viability and competitiveness in the current environment of a more liberalized and globalized financial system, with changing business and technological climates. As a form of financial intermediation it is now becoming increasingly integrated with the international financial system.

The future of Islamic banking in Jordan

A study conducted by the author indicates that the extent to which Islamic banks contribute to the institutionalization of savings has showed positive effects. In this way a positive contribution to development can be made by matching savings with investment needs. Islamic banks encourage those who may not previously have used banks to make use of their services. Many Muslims are hesitant to use riba-based financial institutions; instead keeping their money "under their pillow." The presence of Islamic banks provides

Development in the Islamic finance industry

Country	Islamic banks and finance companies	Islamic insurance companies	Islamic banking windows
Bahrain	26	6	6
Sudan	29	7	–
Qatar	4	1	3
UAE	6	2	3
Kuwait	12	2	–
Saudi Arabia	4	4	6
Egypt	2	–	–
Jordan	2	1	1
Lebanon	3	–	1
Yemen	2	1	–
Iran	9	–	–
Malaysia	2	1	12
Indonesia	6	2	6
Brunei	3	1	–

Muslims with a permissible system of finance, which is in compliance with Shariah principles. Jordan Islamic Bank and the Islamic International Arab Bank have attracted several thousand customers who were not previously bank users. Islamic banking has become an international phenomenon, and now conventional banks are opening new Islamic widows to keep up with the huge demand from customers to enjoy Islamic financial transactions.

Jordan, despite its small size, is one of the most developed Islamic countries, where the majority of the population uses banks. Jordan has one of the best educated and qualified populations in the entire Islamic world. The economy is very open and Jordan's geographical position and economic structure have encouraged more banks and investment companies to come to the country. There is a strong potential for Jordan to become a hub for Islamic financial services in the region.

More effort should be put into recognizing the importance of the Islamic financial services industry across the world, to ensure that the Islamic banking industry is adequately regulated and supervised so as to maintain and enhance banks' confidence in the industry.

The author is Professor of Economics at Yarmouk University, Jordan

Islamic Banking in Lebanon

By Saeb Matraji

The Islamic banking industry is witnessing an unprecedented rise in Lebanon. The Lebanese culture has been a major contributory factor in attracting the necessary funds, in particular from the Gulf area, for the establishment of Islamic banks in Lebanon. A culture which is characterized by an open and multi-faith society, though marked by a Muslim majority, with an economy based on tourism and a robust banking sector. In addition, the industry has received significant support from the well-respected Banque du Liban (BDL), the Central Bank of Lebanon, which has provided the required regulatory, legal and financial framework for Islamic banks and is striving to integrate the Islamic banking sector within the Lebanese financial system.

This article will begin by exploring the current status of the financial sector in Lebanon in the aftermath of the July war. Secondly, it will give an insight into the Islamic banks that are currently operating in Lebanon; and finally it will illustrate the impact of the July war on the activities of the Islamic banks and the policy of the BDL towards the integration of Islamic banking in Lebanon.

The information in this report is based on three exclusive interviews conducted with the general managers of three (Arab Finance House, Al-Barakah Bank Lebanon and the Lebanese Islamic Bank) out of the four (Blom Islamic Bank being the fourth) fully fledged Islamic banks in Lebanon and also on two reports: one prepared by the Economic Research Department at BLOMINVEST Bank SAL at the end of the Israeli attacks, and the other from the Monthly Bulletin, No. 147 of August 2006, prepared by the Department of Statistics and Economic Research at the BDL.

A resilient financial sector

Despite the significant destruction and physical damage caused by the Israeli military strikes, the Lebanese financial system will be able to weather the current period of recession due to the factors summarized below:

1. The Lebanese pound is well supported, as reflected by strong foreign currency reserves of US$13 billion, and the recent support of the Gulf countries, notably Saudi Arabia and Kuwait, who deposited a total of US$1.5 billion with the BDL.

2. The recent significant financial aid and full political support for the Lebanese government by Arab and Gulf countries in particular, reflects a strong implicit financial support by the Arab community.

3. The dollarization of customer deposits with domestic banks has been less significant than in the aftermath of the assassination of former prime minister Rafic Hariri. Foreign currency deposits are believed to have reached around 75% of total deposits, which is far inferior to the 78–80% figures experienced after the Hariri assassination.

4. The strong faith of depositors in the Lebanese banking sector, with total assets estimated at US$60 billion, is a clear indication of the soundness of the system and is reflected in two ways. First, the transfer of deposits out of the country's banking system have been minimal, and have largely been taking place on an inter-bank basis (i.e. from a local bank to its foreign branch or subsidiary in Europe or in the Gulf). Secondly, the amount of deposits in commercial banks has, in fact, increased. This was also the case after the assassination of prime minister Hariri in February 2005, which had a more direct impact on the financial system than the recent hostilities. Therefore, it is widely expected that the deposit level within the system will be maintained.

5. The efficiency of the BDL reflected by the recent liquidity preservation mechanism it has implemented through the purchase and sale transactions with commercial banks of Treasury bills and Certificate of Deposits, which resulted in the exchange of the Lebanon pound liquidity it has with the US dollar liquidity in the market is a strong factor supporting the stability of the national currency and the good health of the banking system.

Nevertheless, the key issue which has been heavily impacted and which really concerns banks is investment. Investment will only occur in a stable, secure and peaceful environment, which is currently lacking in Lebanon. In fact, huge investment projects, especially in the real estate sector, have been either cancelled or suspended because of the political situation. Undoubtedly, the economic ramifications are severe for conventional banks as well as for Islamic banks.

Status and operation of Islamic banks in Lebanon

The first appearance of Islamic banks in Lebanon occurred about a decade ago when the Al-Baraka Bank, a subsidiary

continued...

Islamic Banking in Lebanon *(continued...)*

of Dallah Al-Baraka Group, was launched as a merchant bank operating in compliance to the Shariah, according to Law No. 520, relating to fiduciary contracts, dated the 6th June 1996. A few years later, the Lebanese government sensed the importance of the Islamic banking industry, particularly because of the major success achieved by Islamic institutions in the region, the abundant liquidity due to the boom in oil prices, and the fact that many investors in the GCC states were investing in banks.

As a consequence, the Lebanese Parliament enacted in February 2004 a unique legislation (No. 575) for the establishment of Islamic banks under the supervision of the BDL and governed, unless specified otherwise, by all the regulatory and legal provisions in force in Lebanon, especially the Code of Commerce, the Code of Money and Credit and the Banking Secrecy Law. The law clearly states that the establishment of an Islamic bank or a foreign Islamic bank's branch in Lebanon requires prior authorization from the Central Council of the BDL. Non-Islamic banks operating in Lebanon may establish or take part in the establishment of Islamic banks and may hold shares in Islamic banks established in Lebanon if they fulfill the necessary requirements such as the submission of the names of a credible Shariah board. Moreover, the BDL has been issuing periodical circulars, with the advice of scholars and practitioners in Islamic banking, to organize the functioning of various Islamic structures such as Murabahah, Mudarabah, Salam and Istisnah.

In pursuance to Law No. 575, four Islamic banks are currently operating in Lebanon. The Lebanese Islamic Bank, a subsidiary of Credit Libanais (a conventional bank); the Arab Finance House, supported by Qatar Islamic Bank; Blom Islamic Bank; and Al-Baraka Bank Lebanon. Each of these Islamic banks possesses a distinctive characteristic. The Lebanese Islamic Bank was the first bank to be licensed by the BDL, the Arab Finance House has the largest capital at US$60 million, Blom Islamic Bank is a subsidiary of Blom Bank, Lebanon's largest conventional bank, and the Al-Baraka Bank is the largest in

continued...

Islamic Banking in Lebanon *(continued...)*

terms of the number of branches, with six branches spread across the Lebanese territories.

Impact of the July war and the BDL's policy

As for the impact of the July war, Mr Fouad Matraji, Mr Khodr Temsah and Mr Mutasim Mahmassani, the general managers of the Arab Finance House, the Lebanese Islamic Bank and Al-Baraka Bank Lebanon respectively, hold convergent views in that it will be difficult to realize effectively the budget determined for 2007, given the current economic and political situation.

" The target for the next three to five years is for the market size of the Islamic banking sector to constitute between 5–10% of the total financial market in Lebanon"

The salient argument advanced here is that Islamic banks, unlike conventional banks, have universal banking licenses, which means that they can undertake both retail and investment activities under one license. In the current circumstances, the investment arm has been paralyzed, and thus Islamic banks are not benefiting from the activities which will generate huge profits and are focusing on consumer finance such as car or home finance. Mr Matraji stressed that the key to the success of any Islamic bank is product innovation, as well as the creativity necessary in setting up new Shariah compliant deals and structures within the Lebanese financial system, and this can only be achieved in a secure and stable environment. Mr Temsah, for his part, explained that the main goal of the Shariah through Islamic banks is not confined to the realization of profits, but also relates to the achievement of social prosperity through the implementation of myriad investment projects on a profit and loss-sharing basis, which is not possible at this time.

Despite all the obstacles facing the Islamic banking industry, the market leaders are ambitious with regard to their plans and are relying on the resilient banking sector. Mr Temsah emphasized that whatever the political and economic situation, Islamic banks should do their best to at least preserve their position in the industry, and he is quite confident that in 2007 Islamic banking activities will meet the expectations of the people who established Islamic banks in Lebanon. Mr Matraji confirmed that there is a serious plan to increase the capital of the Arab Finance House from US$60 million to US$100 million in the near future. Similarly, Mr Mahmassani underlined that one of the major resolutions on the agenda of Al-Baraka Bank is to increase its current capital of US$20 million.

With respect to the BDL's policy towards the integration of Islamic banks in the financial system, Dr Ahmad Jachi, first vice-governor of the BDL, confirmed that the target for the next three to five years is for the market size of the Islamic banking sector to constitute between 5–10% of the total financial market in Lebanon. Dr Jachi explained that the BDL plans to have an integrated financial system, which includes fully fledged conventional banks and fully fledged Islamic banks. The Central Bank's policy is not to allow Islamic banking windows at conventional banks. Nor will it follow a dual system of banking. The vision is not to have an Islamic niche banking sector nor a dual system whereby an Islamic system operates side by side a conventional one. The BDL prefers an integrated financial system. It wants to come to a solution where Islamic banking is part of the financial system; and where it can integrate the Lebanese financial system within the global system.

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Turkey 2006 – Looking Ahead With Confidence

By Paul Wouters

Overall 2006 was a good year for the Turkish economy, which has proven to be sufficiently resilient against some monetary re-adjustments that in the past would have caused problems. The present government, tied up with the upcoming elections and the EU accession talks, still manages to master inflation rates and maintain economic growth objectives. Due to ongoing legislative and budgetarian efforts, a reassuring International Monetary Fund (IMF) report and a cautious but positive Organization for Economic Co-operation and Development (OECD) report on corporate governance were obtained.

Foreign direct investment is improving and on the local financial markets, several new international players have established themselves (amongst others Fortis and Dexia). These firms import the required energy, knowledge and expertise, new types of financial instruments and will enhance competition and innovation. Such incentives are much needed by the comparatively inexperienced local financial markets (both conventional and Islamic) that – sometimes also hindered by reluctant regulatory bodies – struggle to innovate.

Islamic finance market – market players

The Islamic finance sector, as of September 2006 was about 340 branch offices (up from 290 branches at the end of 2005), and is projected to grow at a rate of 50 new units per year. Overall, personnel grew from 5,740 at the end of 2005 to 6,340 in June 2006. Compared to 2005, deposits and investment accounts have grown 25%.

Dubai Islamic Bank (which maintains a representative office in Istanbul) encountered a setback in trying to acquire MNG Bank (transaction value estimated at US$160 million), but Kuwait-based The International Investor (TII) succeeded taking over Adabank (formerly owned by the UZAN group) for a total of TL45.1 million (US$32 million). Adabank had been seized by the Banking Supervision and Regulation Agency (BDDK) in July 2003 as part of the Imar Bank investigations and was put up for public tender by the Saving and Deposits Insurance Fund (TMSF). Adabank maintained only one (head) office and 65 personnel.

TII has already filed for a licence as a "Participation Bank." The granting of such licence will bring the total number of Turkish Participation Banks to five. The others are:

Albaraka Turk Participation Bank (Albaraka Turk Katilim Bankasi), part of the Gulf-based Albaraka Banking Group, which met its projected targets last year and is preparing for an IPO in 2007.

Kuveyt Turk Participation Bank (Kuveyt Turk Katilim Bankasi), part of Kuwait Finance House (KFH). Kuveyt Turk was in the newspapers several times last year with important Murabahah financings. It is rumoured that it will redress its balance sheet and – depending on market conditions – could be candidate for an IPO in 2008–2009.

Turkiye Finans Participation Bank (Turkiye Finans Katilim Bankasi), of Turkish origin (Boydak and Ulker). It has absorbed the merger of December 2005 of Family Finans and Anadolu Finans "Finance Houses" (the previous name for Participation Banks) remarkably well and is anticipating further development.

Bank Asya (Asya Katilim Bankasi), also of Turkish origin. In May 2006 Bank Asya conducted probably the most successful IPO in Turkish history: US$150 million raised for 20% of the shares, valuing the bank at US$800 million, with US$7.5 billion offers, making it 50 times oversubscribed. Strong interest from European and Gulf investors was noted, beside strong demand from Turkish retail investors. Following this massive oversubscription, more activity on the equity side is to be expected. Marketing a very modern and contemporary profile (retail, small business, corporate and private banking), Bank Asya will open five new dedicated corporate banking units (3 in Istanbul, 1 in Izmir and 1 in Bursa) in 2007, in addition to the already existing Ankara unit.

Aside from these Participation Banks, a growing number of Islamic finance houses now have a presence in Turkey. In addition to Dubai Islamic Bank and ABC Islamic Bank, institutions such as Amlak Finance, Dubai Bank and the National Bank of Kuwait Capital have established representative offices, formed partnerships or are about to form partnerships in order to take an active role in the development of the sector in Turkey.

In December 2006, the Qatar-based Doha Bank joined the league by officially opening its representative office in Istanbul. This followed the strategic alliance (in March 2006) between Dubai Bank and Turkey's Daruma Corporate Finance to co-operate in structuring, executing and distributing of Shariah compliant corporate finance and merchant banking services.

continued...

Turkey 2006 – Looking Ahead With Confidence *(continued...)*

In light of Qatar's recently announced budget of US$182 billion for infrastructure projects (for the period 2006–2011), Doha Bank is said to have launched a representative office in Turkey in order to forge business opportunities with Turkish companies interested in Qatari projects. Doha Bank has been working with Turkish banks for over 15 years and has a total volume of finance in the country of US$150 million. A free trade agreement between Qatar and Turkey is presently under negotiation.

In addition, international banks such as BNP Paribas, Calyon and Deutsche Bank have joined ABN Amro, Citibank and HSBC in promoting Islamic finance as part of their mainstream product offerings.

Islamic finance market – size

The Islamic financial institutions market (Participation Banks) has grown considerably, especially since 2001 (when Turkey experienced its last economic crisis), at an average annual rate of 40% in terms of asset size, 53% in terms of funds placed and 40% in terms of funds raised.

Assets (US$ millions)

	Banks	Participation banks	Growth	Participation banks (% in total)
1995	68,373	1,416	–	2.1%
2000	155,183	3,372	–	2.2%
2001	149,625	1,634	–	1.1%
2002	129,522	2,413	48%	1.9%
2003	178,991	3,665	52%	2.0%
2004	228,337	5,435	48%	2.4%
2005	294,423	7,378	36%	2.5%
2006–09	307,921	8,482	15%	2.8%

Source: Turkish Participation Banks Association (TKBB)

In addition to the onshore Islamic finance outlined above, a cross-border Islamic finance market has formed, especially during the last decade. Starting out as a funding vehicle for the cash-strapped local banks by way of bank-guaranteed financings to corporations, the market has grown to an estimated annual volume of US$500 million–US$600 million, with corporate risk-based structures often with security packages involving checks, export receivables and credit card receivables.

Historically, HSBC has taken a leading role in this area with its corporate Islamic facilities to Vestel Electronics, together with the Islamic Development Bank (IDB), to the tune of US$25 million, the US$60 million financing for the development of Istanbul Airport International terminal to TAV (2003), and again with IDB a US$100 million facility to Turkcell (2004), the leading mobile telecommunications operator of the country, to finance network equipment purchases.

Funds raised (US$ million)

	Banks	Participation banks	Growth	Participation banks (% in total)
1995	29,061	1,072	–	2.4%
2000	101,849	2,772	–	2.7%
2001	101,949	1,325	–	1.3%
2002	251,150	1,952	47%	0.8%
2003	105,628	2,946	51%	2.8%
2004	147,078	4,463	51%	3.0%
2005	188,073	6,209	39%	3.3%
2006–09	196,755	6,855	10%	3.5%

Source: Turkish Participation Banks Association (TKBB)

Funds placed (US$ million)

	Banks	Participation banks	Growth	Participation banks (% in total)
1995	29,061	1,043	–	3.6%
2000	50,913	2,568	–	5.0%
2001	39,628	741	–	1.9%
2002	34,330	1,280	73%	3.7%
2003	34,422	2,333	82%	6.8%
2004	76,925	3,645	56%	4.7%
2005	113,520	4,891	34%	4.3%
2006–09	136,099	5,823	19%	4.3%

Source: Turkish Participation Banks Association (TKBB)

HSBC still preserves a strong position in cross-border syndicated Islamic finance in Turkey, as evidenced by the US$1.3 billion volume generated over the last few years and the US$80 million transaction of 2006, which was arranged together with KFH Group to ULKER Group, the prime food and beverage company in Turkey.

Another transaction that drew a lot of attention in 2006 was ABC Islamic Bank, Standard Chartered Bank and Gulf International Bank closing a two-year US$200 million Murabahah facility for Kuveyt Turk Participation Bank in December 2006. The facility will allow Kuveyt Turk to serve small and medium-sized enterprises throughout Turkey. It is syndicated by 32 banks, including leading names from across Europe and the Middle East.

Moreover, it is said that ABC Islamic Bank intends to double its financial presence in Turkey – which for the moment mainly consists of bilateral credit lines to financial institutions – over the next year. It is preparing, as are others, for the new Turkish mortgage law (extensive knowledge of which is

continued...

Turkey 2006 – Looking Ahead With Confidence *(continued...)*

Participation Banks in Turkey (US$ millions as of 2006/09)

	Total assets	Funds raised	Funds placed	Equity	PBT	Net profit
Al Baraka	1,586.3	1,378.1	1,106.6	150.3	31.7	30.4
Bank Asya	2,537.7	1,927.1	1,645.3	390.2	88.3	63.9
Kuveyt Turk	1,961.7	1,517.4	1,340.4	157.3	15.0	15.0
Turkiye Finans	2,396.6	2,032.7	1,730.4	250.9	69.7	69.7
Total Participation Banks	**8,482.3**	**6,855.4**	**5,822.6**	**948.7**	**204.7**	**179.0**

Source: Turkish Participation Banks Association (TKBB)

available through their Alburaq diminishing Musharakah) and intends to offer "overnight Murabahah" to Turkish financial institutions through their ABC Clearing Company.

Fitch Ratings – long-term issuer default rating

Albaraka	B	15.11.2006	Stable
Bank Asya	B B	25.09.2006	Stable
Kuveyt Türk	B	19.06.2006	Positive
Türkiye Finans	–	–	–

In July 2006, GAP Guneydogu Tekstil (a subsidiary of CALIK Holding in Turkey) entered into a US$50 million master revolving Murabahah facility with KFH and Kuveyt Turk Participation Bank as mandated lead managers. With a maturity of 4.5 years, the facility has the longest term ever granted by the Gulf group to any Turkish company. It thereby expresses faith in the prospects of the Turkish economy and in the good standing of GAP Guneydogu Tekstil. The signing ceremony was attended by Ahmet Calik, the president of Calik Group, and Emad Yousef Al-Monaya, the president of the international investment department of KFH. Both leaders expressed the signal function of the agreement for other Turkish exporters and the importance of a Gulf presence in the Turkish market.

"By licence, Participation Banks are automatically able to offer leasing"

Islamic finance market – the future

By licence, Participation Banks are automatically able to offer leasing. Therefore mark-up sales (Murabahah) together with leasing (Ijarah) are the primary products available in the Islamic finance industry from onshore Islamic finance institutions. For cross-border syndicated Islamic finance, Murabahah remains the only product, as cross-border leasing is subject to official approvals complicating the process further.

Government Sukuk is not on offer in Turkey yet, mostly due to the lack of regulatory infrastructure. The Turkish treasury department has been looking for some time into the possibility of establishing a framework for this, however it has yet to come to a decision, mostly because of the current abundance of inexpensive funding from the conventional market. Several private issuers are beginning to consider Sukuk and evaluate the market conditions and the regulatory framework for these purposes.

The 2nd Turkish Arab Economic Forum in Istanbul in June 2006, attended by Recep Tayyip Erdogan, prime minister of Turkey, has again evidenced the importance that is accorded to Turkey's relationship with the Arab world and in that context to Islamic finance. Consequently, along with the development of Islamic finance globally and increasing application locally, the market is prone to the introduction of new and more advanced products. The increasing number of international players will certainly help to facilitate the process.

As voiced by the general manager of one of the leading Participation Banks, it is estimated that the assets of Islamic banks in Turkey will exceed US$25 billion, from US$8.5 billion, in the next decade and will make up 10% of the total banking system. Needless to say, there will be growth in the cross-border syndication market at a comparable pace.

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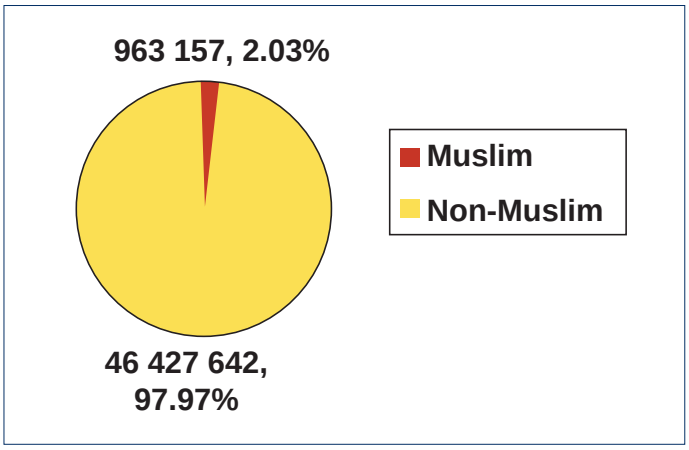
Islamic Banking in South Africa

By Ahmed Moola

The concept of Islamic banking dates back several decades in South Africa. The practical implementation of Islamic banking started in 1989, although the initial take-up was slow. In the late-1990s some asset managers began to achieve success with Shariah compliant products and currently they hold between R35 billion (US$4.9 billion) and R40 billion (US$5.6 billion) in assets. Islamic banking opportunities have also been explored by conventional banks through single product offerings and Islamic windows.

South Africa has a total Muslim population of 1 million people, representing 2.1% of the country's population. While the industry is relatively modest in terms of figures at present, Islamic banking is strategically important for unlocking value in sectors such as high net worth individuals and business banking, as well as in relation to the rest of Africa, where the total Muslim population is estimated at 387 million.

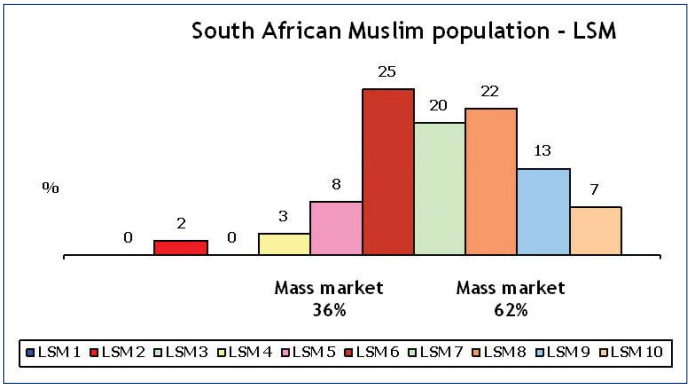
Total South African population – Muslim vs non-Muslim



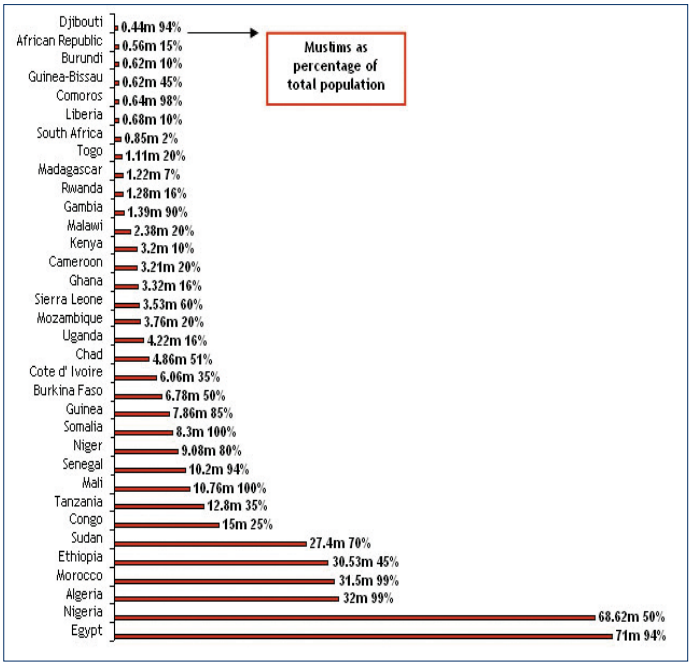
Currently, 58% of the South African Muslim population banks conventionally. Islamic banking is offered by two conventional banks (one of which is Absa) and by one niche market Islamic bank. Other conventional banks in South Africa are intending to launch Islamic banking as part of their strategy, as there is a definite tendency in South Africa for Muslim customers to move towards Islamic banking.

The need for Islamic banking products is not yet being fully met in any sector of the market. The high demand is not yet being matched with appropriate Islamic banking products, leading to limited take up of such products that do exist. Similarly, the need for private banking services has not been appropriately addressed, leading private banking clients to use conventional banking services. As an illustration of this, although all three Islamic banking institutions in South Africa currently offer savings and checking accounts and vehicle and asset finance, only one offers a petrol card, one offers trade finance and two offer mortgage bonds, insurance, Islamic wills and unit trusts. None currently offer an Islamic credit card, personal loans, or finance for working capital.

Asset management companies that offer Shariah compliant products have to some degree been successful in capturing the unit trust/mutual fund market. This success can be attributed to the Islamic population's lifestyle being higher then average.



Total African Muslim Population in Africa



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Islamic Banking in South Africa *(continued...)*

Islamic banks face a number of challenges in the South African market. Competition is expected to increase significantly during 2007, although education and awareness remain major challenges for all institutions in the Islamic banking market. Another challenge for niche players in the market is to create a geographic footprint. This impacts their ability to reach clients, access appropriate staff, as well as their ability to provide banking infrastructure in more than their restricted footprint. The current lack of industry expertise is a result of the fact that this sector is in its infancy in South Africa and, as competition increases, the challenge of satisfying the demand for Islamic banking skills will increase.

Absa Islamic Banking, with less than a year in business, has already leveraged this relationship to create demand for its innovative banking products both in the Middle East and in some African countries. Absa Islamic Banking has grown its business and the early slow uptake of products has developed into a growing demand as more and more customers become aware of the product range and comfortable with the products and the robustness of the process.

"The South African Islamic banking market is set to expand at a rapid rate as new players identify the huge opportunity in the country"

The South African Islamic banking market is set to expand at a rapid rate as new players identify the huge opportunity in the country. Those banks which are already established from a product, skills set and customer relationship perspective are well positioned to lead the field.

The author is head of Islamic banking at Absa Islamic Bank.

Islamic Financial Services in Nigeria

By Femi Sunmonu & Associates

Nigeria is sub-Saharan Africa's second largest economy. Situated on a land mass of 924,000 square miles and with a population estimated at 140 million it is arguably the largest consumer market in Africa and, as the burgeoning growth of the telecommunications services market in the last seven years clearly shows, it holds one of the most attractive outlets for the marketability and profitability of financial services – for example, between 2000 and 2004, average return on equity in the banking sector was 35–40% – without doubt one of the best in the world.

The Nigerian financial services sector comprises the banking, insurance and capital markets and pension funds sub-sectors. In the last 20 years, the whole sector (except the nascent pension funds sub-sector) has witnessed considerable growth, due mainly to the privatization of government-owned corporations, the liberalization of licensing policies and the progressive and proactive evolution of the regulatory regimes for the financial sector.

"It holds one of the most attractive outlets for the marketability and profitability of financial services – for example, between 2000 and 2004, average return on equity in the banking sector was 35–40% – without doubt one of the best in the world"

Under the mandate of two principal legislations – the Central Bank of Nigeria and the Banks and Other Financial Institutions Act – the Central Bank of Nigeria (CBN) serves as the main regulator of the banking sector (with a secondary role being played by the Nigeria Deposit Insurance Corporation).

The banking sector is divided into:

1. Deposit money banks.
2. Discount houses.
3. Community banks.
4. Micro-finance banks.
5. Finance companies.
6. Development finance institutions.
7. Primary mortgage institutions.
8. Bureaux de Change.

Banking sector

In 2005, earnings and total assets of the banking sector represented 5.9% and 49% of GDP respectively (discounting the large informal sector, GDP for 2005 was estimated at US$89.6 billion). The sector has come a long way from the inefficiencies of a largely government-owned and civil service-managed sector of the 1970s.

The northerly trajectory of the Nigerian financial services sector in the last 20 years notwithstanding, there remains a palpable lack of depth and breadth to the variety and quality of services available to the public. This factor may explain why Islamic finance in Nigeria is still in its infancy. Little had been done by the 115 commercial and merchant banks as at 1995, to offer the approximately 69 million Nigerians who profess to be Muslim the opportunity to play a role in the economy in compliance with their belief system. The consequences of this situation were (and remain): first, the perpetuation of informality for a very significant volume of trade – particularly in northern Nigeria where the majority of the populace is Muslim and estimates of money outside the banking system hover around the N250 billion (US$1.95 billion) figure. Secondly, the socio-financial disenfranchisement of large numbers of the population through inaccessibility to capital for trade and home ownership. Thirdly, the curtailment of growth for the capital market due to the limited intervention of the Islamic faithful in the ownership of quoted securities. Fourthly, limited alternatives for the funding of infrastructure and other developmental purposes – particularly in the light of the country's painful experience with the Paris/London Club borrowing for such purposes.

During the licensing liberalization of the early 1990s, the CBN created a window for banks to be licensed under the caption of "profit and loss sharing" banks – this was to find a route around national legislation and banking regulations which forbade the overt espousal of religious norms in businesses such as banks. Despite the willingness of the CBN to allow soft regulation for this niche of the financial sector, there were no takers for the licenses – the ownership class in Nigeria was not only thoroughly enraptured by the outlandish profiteering possible in the conventional banking sector, they also lacked the knowledge, patience and perseverance necessary to nurture institutions based on alternative principles to those of the conventional banking system. Another problem was the

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Islamic Financial Services in Nigeria *(continued...)*

thin spread of integrity in the management class of the financial services industry and the lack of corporate governance on the directing boards of financial institutions. It was not surprising then that the mid-1990s saw the banking sector in a tailspin of bankruptcies and failures. It was inevitable that the CBN as regulator had to switch to heavy-handed regulation and enforcement of prudential guidelines for financial reporting.

Notwithstanding this, by 1999 there remained 89 commercial/investment banks with 3,300 branches nationwide. None of these banks offered any service that could in theory or practice be called Islamic. At best, two of them sought and obtained Central Bank approval to open "Islamic windows." This was a euphemism for banking products designed to allow the banks essentially to take and keep deposits with assurances given to the depositors that no riba would be added to their funds whenever they wished to withdraw. Sentimentalities were exploited by the banks stating that depositors could save towards landmark Islamic events like the Hajj or the Eid al Adha. There was no corresponding offer of Mudarabah, Musharakah, Murahabah or Ijarah wa Istinah. Put plainly, Nigerian Muslims still had no choice but to endure the deprivations of conventional banking.

"The regulatory regimes accommodate a preference to offer services tailored to meet Islamic principles and have consistently shown a willingness to work with promoters and investors to nurture and give best practice regulation to Shariah compliant services"

In July 2004, the CBN announced – as part of a broader 13-point national economy/banking sector reform plan – a new minimum capital base requirement of N25 billion (US$195.1 million). The need to achieve this capital requirement by the 31st December 2005 deadline resulted in an assortment of mergers, consolidations, acquisitions and unfortunately a number of outright failures, which pruned the number of banks at that date back to 25.

Of the 25 "deposit money banks," none of the banks that offered Islamic windows survived as a monolith and none of them currently offers or has projected the offer of Islamic banking services. However, it is noteworthy that a corporation formed in April 2003 by a pool of Nigerian investors with the name Jaiz International had, shortly before the July 2004 minimum capital declaration by the CBN, sought and obtained a license-in-principle to commence operations as a wholly non-interest banking institution. Jaiz has sought assistance and partnerships from the Islamic Development Bank and the Islami Bank of Bangladesh. The terms of agreement with Islami Bank stipulated that Islami Bank would provide five senior management personnel including the CEO for Jaiz, in addition to the transfer of technical and operational know-how. It seems, however, that Jaiz has been slow in commencing business as it has to source the difference between the N2 billion (US$15.61 million) prescribed capital base with which it obtained its license-in-principle, and the N25 billion (US$195.1 million) share capital now mandatory to commence operations.

Insurance sector

The insurance sector is regulated by the National Insurance Commission (NAICOM) and is divided into the insurance (life and non-life) and reinsurance businesses.

As at September 2005, the Nigerian insurance sector comprised 103 direct insurance and five reinsurance companies. The industry was cumulatively capitalized at N34 billion (US$265.35 million). Government, based on a desire to ensure that there was some evenness to the contributory role of the insurance industry to the national economy vis-à-vis the banking sector, directed another bout of recapitalizations by increasing the minimum share capital requirements for the insurance industry as follows:

- Life insurance business: N2 billion (US$15.61 million).
- General insurance business: N3 billion (US$23.41 million).
- Reinsurance: N10 billion (US$78.04 million).

The new capital requirements became effective for new companies on the 1st September 2005, taking effect for existing companies from the 28th February 2007.

As a gale of acquisitions, mergers and consolidations sweeps through the sector, a number of the very creative banks are making direct acquisitions of medium-sized companies to form bancassurance outfits. The strategy, it seems, is to create platforms for massive cross-selling of services and value.

As in the banking sector, insurance companies have been lethargic about structuring their services and products to comply with the Shariah. Following several international conferences on Islamic finance and insurance held in Kano and Abuja between 1999 and 2004, one insurer made an attempt to introduce a Shariah compliant Takaful product

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Islamic Financial Services in Nigeria *(continued...)*

which unfortunately has not caught on – probably due to a combination of poor conceptualization and marketing.

Capital markets

The capital markets sector is regulated by the Securities and Exchanges Commission. This sector is made up of the Nigeria Stock Exchange (Lagos), which trades quoted securities; the Abuja Stock Exchange, which is about to commence operation as a futures/commodities exchange; and the various intermediation parties, such as stockbrokers, issuing houses, etc...

The Nigeria Stock Exchange (NSE) serves as the platform for the introduction and sale of government and corporate securities. Commendably there are a number of mutual funds quoted on the NSE that are tagged "ethical," i.e. they are structured to invest pooled funds only in businesses that align with the ethical preferences of the investors. The only drawback of these funds as they relate to Muslims is that investments are not subjected to the stringency of compliance with the Shariah, and therefore the level of patronage by the Muslim population does not reflect the potential of the market.

Pension funds

The pension funds sector is regulated by the National Pension Commission (PenCom) and includes pension fund administrators, pension fund custodians and closed pension fund administrators. The present structure came into being through the enactment of the radical Pension Act 2004.

At the end of 2005, PenCom had licensed four pension fund custodians, one closed pension fund administrator and 13 pension fund administrators. The value of the Nigeria pension fund sector is estimated at N275 billion+ (US$2.15 billion+), with annual growth projections of at least 12%.

To date no pension fund administrators have made any attempt at marketing pension account holders/contributors on the basis of keeping and investing their pension funds in compliance with the Shariah.

Nigeria – the proposition for Islamic finance services

Given the foregoing overview, and in contrast with trends in the Middle East, South-East Asia and Europe, Nigeria is a long way down on the Islamic finance growth scale. This is paradoxical considering that:

1. The regulatory regimes accommodate a preference to offer services tailored to meet Islamic principles and have consistently shown a willingness to work with promoters and investors to nurture and give best practice regulation to Shariah compliant services.

2. There is a substantial number of consumers available to sustain the beginning and the growth of the Islamic finance niche, representing an enormous potential volume of business from the liability generation side and are ready off-takers for a commensurate volume of the asset generating retail services, home finance, micro-credits, small to medium-scale loans, etc.

"Nigeria is a long way down on the Islamic finance growth scale"

Starting an Islamic finance service in Nigeria

Entry into the financial services sector in Nigeria is based on a similar template for all sectors. Subject to proper professional input and advice, an outline is provided below:

1. Prepare feasibility report for proposed service.
2. Prepare draft incorporation bylaws (articles and memorandum of association).
3. Compile list of shareholders, directors and principal officers of the proposed business.
4. Pay prescribed application fee.
5. Provide such other information and documentation as the sector regulator may request.
6. Deposit equivalent of prescribed minimum share capital with the Central Bank (in all cases).
7. If approval in principle is granted, proceed to incorporation of business under the Companies Act and fulfill all further conditions necessary for the grant of an operating license.

Furthermore, as there are no restrictions on foreign participation in the financial services sector, interested parties could either go it alone or in collaboration with Nigerian partners.

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Islamic Finance in Egypt

By Dr. Reinhard Klarmann

Egypt has played an important role in the development of Islamic finance since its early stages. Host to the first modern Islamic bank, established as early as 1963, Egypt was home to many influential scholars who, since the beginning of the 20th century, largely fuelled the debate on the prohibition of riba, contributing to the creation of what is today's global Islamic finance industry.

In the last decade, however, the Egyptian Islamic finance sector has fallen behind, despite the huge surge in the popularity of Islamic finance in most of its neighboring countries and a tendency towards an increasing Islamization in Egypt. This may be explained by a number of reasons.

On the one hand, many Egyptians still recall all too well the collapse of prominent Egyptian Islamic investment companies in the late 1980s, most notably that of the Al Rayyan Islamic Investment Company, which left investors with total losses of approximately E£1 billion (US$176 million). On the other hand, the Central Bank of Egypt (CBE)'s restrictive policy consisting of preventing the establishment and expansion of Islamic financial institutions has played a significant role in the limited growth of the Islamic finance sector in Egypt.

Despite Egypt's reluctance in past years to revive the Islamic finance sector, the strong international focus on Egypt's banking sector in 2006, which was dominated by several significant mergers and acquisitions of banks, may have created an appetite for investment in the Egyptian Islamic finance sector.

Regulatory framework

A significant milestone for the Egyptian banking sector was laid with the introduction of the new Law No. 88/2003 promulgating the law on the Central Bank of Egypt, the Banking Apparatus and Exchange (Banking Law), which came into force on the 15th July 2003. One of the new Banking Law's main aims was to bring about a number of mergers in the market. To this effect, stringent capitalization and capital reserve requirements were implemented and have indeed forced a number of banks to merge in order to be able to satisfy these requirements.

Despite the introduction of many new elements of banking regulation by the Banking Law, no provisions were introduced to regulate Islamic financial institutions. It is surprising that, in the context of this comprehensive restructuring of the regulatory framework, the legislator chose to leave Islamic financial institutions without a specific regulatory framework, especially given that other countries in the region, such as Syria and Jordan, have enacted specific legislation governing Islamic financial institutions.

Early Egyptian public sector Islamic banks

Mit Ghamr Bank

The Mit Ghamr Bank (MGB) was a government-owned bank, established in 1963 as an adapted model of the German Sparkassen (savings banks) in the Delta town of Mit Ghamr. Unlike other financial institutions, the MGB was not subject to the supervision of the CBE, but to that of an independent public authority, especially created for this purpose. Despite the success of MGB's activities, which essentially consisted of small loans in profit-and-loss-sharing form, in 1968 the Egyptian government found it necessary to close down the bank, mainly for political reasons.

Nasser Social Bank

MGB's successor on the Egyptian Islamic finance stage was the state-owned Nasser Social Bank (NSB), established by Law No. 66/1971. Although NSB cannot be formally considered a bank because it is not registered as such with the CBE, its statutes define it as an Islamic bank which must carry out all its activities in conformity with Islamic Shariah. NSB essentially carries out a wide array of social services. Unlike MGB, NSB still exists, but in recent years there have been several reports that it is distancing itself from its original Islamic character.

"In the last decade, however, the Egyptian Islamic finance sector has fallen behind, despite the huge surge in the popularity of Islamic finance"

Present-day Islamic financial institutions

The Egyptian Islamic finance sector is made up of a few full-fledged Islamic banks, and a number of conventional banks offering Islamic services. Three main Islamic banks currently dominate the sector.

Faisal Islamic Bank of Egypt

Faisal Islamic Bank of Egypt (FIBE) was established by Law No. 48/1977, and is an Egyptian–Saudi joint venture. As the largest Islamic bank in Egypt, FIBE has experienced strong growth in recent years, posting a net profit of E£118.5 million (US$21 million) for the year 2006. FIBE offers the full array of

continued...

Islamic Finance in Egypt *(continued...)*

Islamic services, mainly focussing on commercial operations, including Murabahah, Musharakah and Mudarabah instruments. Investments and shareholdings in other entities are not a main part of FIBE's focus.

"The Egyptian market is ready for new forms of Islamic financial instruments"

Despite FIBE's success, recent attempts to expand its network of branches in Egypt have failed, due to the CBE's refusal to allow the opening of new branches. This has reportedly led to the overcrowding of FIBE's existing branches.

Egyptian Saudi Finance Bank
The second largest Islamic bank in Egypt, the Egyptian Saudi Finance Bank (ESFB) was created on the 21st June 1988, as a result of the takeover of Ahram Bank by the Saudi Dallah Al Baraka group.

ESFB provides a full range of banking transactions and services related to its activities in compliance with the principles and rules of Islamic Shariah through its Cairo-based head office and its 15 branches in Egypt.

Islamic International Bank for Investment and Development
Earlier in 2006, the ailing Islamic International Bank for Investment and Development (IIBID), established by Law No. 43/1974, was acquired by the newly established United Bank, together with the United Bank of Egypt and Nile Bank. Factors leading to the acquisition of IIBID by United Bank were essentially IIBID's inability to curb its high debts and its failure to comply with the new minimum capital requirements introduced by the Banking Law. Whilst it has been reported that United Bank will continue to offer Islamic services, little is currently known about the dimensions which this Islamic window will take.

Finally, a number of conventional Egyptian banks offer Islamic services. The major banks in this field are the National Bank for Development, El Watany Bank and Banque Misr (soon to merge with Banque du Caire).

Shariah compliant activities

The recent launch of the new E£100 million (US$18 million) Islamic fund "Sanabel" by the National Bank for Development and Société Arabe Internationale de Banque is an indicator that the Egyptian market is ready for new forms of Islamic financial instruments. Until recently, the only other Islamic fund in Egypt was the Faisal Islamic fund, launched in 2004.

Outlook for 2007

As more conventional Egyptian banks are looking to offer Islamic services, and Gulf-based Islamic banks are looking at purchasing smaller Egyptian banks in order to gain a foothold in the Egyptian market, 2007 seems to hold much in reserve for Egypt's Islamic finance sector. Just recently, Bahrain Islamic Bank announced that it is looking into the acquisition of the Arab Investment Bank.

The recent large-scale investment of Gulf corporations in Egypt, most notably the UAE's Emaar and Etisalat, has raised expectations in the Egyptian market, which has yet to see its first Sukuk issuance. Further, the establishment last month of a branch of the UAE Islamic mortgage provider Amlak in Egypt may prove to be the first of a series of Shariah compliant home finance providers to begin offering their services on Egypt's relatively virgin real estate mortgage market.

With all these developments, 2007 may indeed prove to be the beginning of a new era for the Egyptian Islamic finance sector.

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Prospects for Pakistan

By Mohammad Shaheed Khan

Islamic finance - commonly defined

Islamic banking – defined as banking in consonance with the values of Islam – is governed, in addition to conventional good governance and risk management rules, by the principles laid down by Islamic Shariah.

Islamic finance is an ethical and equitable mode of finance. The most distinctive element is the prohibition of interest (riba), whether nominal or excessive, simple or compound, fixed or floating. Other elements include the emphasis on equitable contracts, the linking of finance to productivity, the desirability of profit sharing, and the prohibition of gambling and types of uncertainty. It also discourages speculation and precludes short selling, conventional debt instruments and derivatives.

"Of the worldwide Muslim population of approximately 1.6 billion, one-tenth of these live in Pakistan, which has a total populace of approximately 160 million Muslims"

Pakistan market environment

Of the worldwide Muslim population of approximately 1.6 billion, one-tenth of these live in Pakistan, which has a total populace of approximately 160 million Muslims. This growing, religiously cognizant nation has the potential to provide opportunities for Shariah compliant savings, asset and investment products.

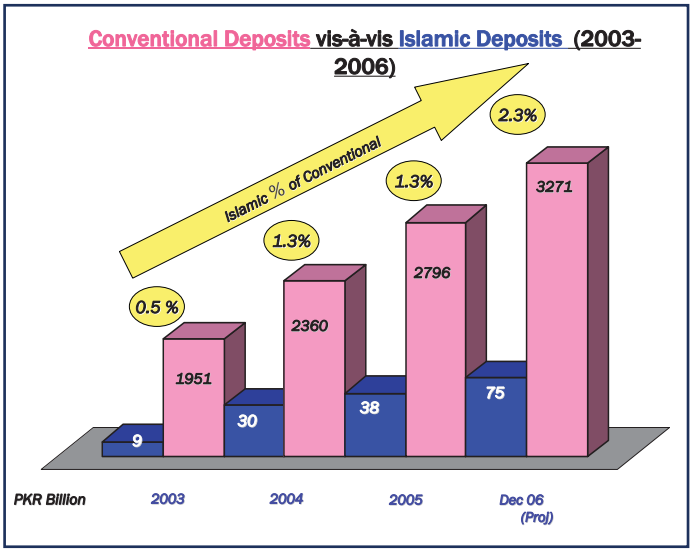
In Pakistan the Islamic banking market is relatively new. There have been a few abortive attempts over the last couple of decades to initiate Islamic banking, for various reasons they have been unsuccessful. However, over the last five years or so there has been a lot of support for Islamic banking from the government and regulators, providing the sector with a boost.

The Islamic banking industry is now emerging from its embryonic stage of development, where it only constitutes 2% of the banking sector's total assets. Although the Islamic sector's share of the market remains miniscule, the growth it has seen relative to itself over the last three years has been exceptionally strong. There are efforts in Pakistan to gradually move away from conventional towards Islamic banking. The regulators have provided a level playing field to the Islamic banking industry, leaving it to the consumer to decide which form of banking to choose.

With Pakistan's economy now moving at a faster pace, the Islamic banks have been aggressively targeting new customers and have grown in size as well as in the diversity of their services over the last few years. The overall deposits in Islamic banks stand at PKR67 billion (US$1.11 billion), while assets constitute around PKR98 billion (US$1.63 billion). It is expected that the industry will see a 40% year-on-year growth for the next 10 years, with Islamic banking deposits projected to reach US$13 billion, or 10% of the market, by 2014[1].

Within the banking sector, deposits and financings continue to dominate the balance sheets of various banks. The share of deposits is 68%, followed by funds from owner's capital. Financings are the dominant component of assets structure of the Islamic banking system and their share is evident by the financings to deposit ratio of almost 87%. Within financings, Murabahah and Ijarah dominate, their collective share in total financings being 70% towards the end of 2006. However, the share of other modes of financing such as diminishing Musharakah, Salam and Istisnah has been gradually increasing, reflecting diversification in the portfolio of Islamic banking institutions and the development of new products based on Islamic modes of financing.

The following graphs[2] compare the asset and liability books of Islamic and conventional banks.



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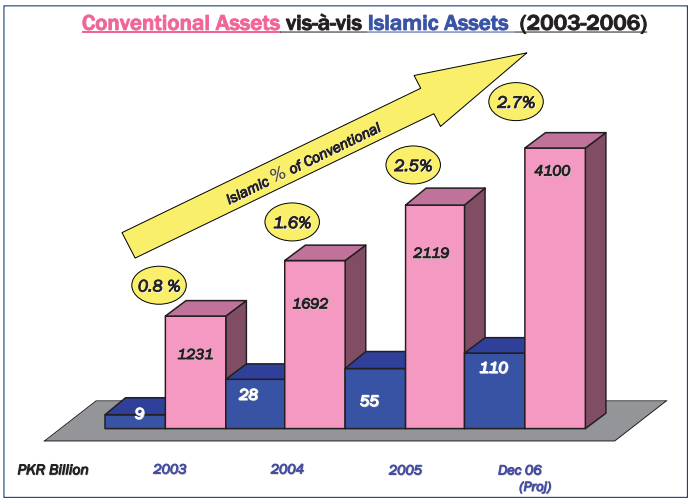
Prospects for Pakistan *(continued...)*



Competition in Pakistan

2003		2004		2005	
Islamic Banks	Branches	Islamic Banks	Branches	Islamic Banks	Branches
Meezan Bank	12	Meezan Bank	16	Meezan Bank	28
Albaraka Islamic	5	Albaraka Islamic	7	Albaraka Islamic	9
		Bank Alfalah	11	Bank Alfalah	14
		Muslim Commercial	5	Muslim Commercial	5
		Habib AG Zurich	1	Habib AG Zurich	4
		Standard Chartered	1	Standard Chartered	2+1in Khi
		Bank of Khyber	3	Bank of Khyber	4
		Metropolitan Bank	1	Metropolitan Bank	1
				Bank Al Habib	1
				Habib Bank	1
				Soneri Bank	1
2 Banks 17 Branches		8 Banks 45 Branches		11 Banks 70 Branches	

Competition in Pakistan

Further evidence of the interest in Islamic banking in Pakistan can be seen from the expenditure institutions are making both in terms of entering the Islamic banking industry, and in setting up distribution networks. Institutions are willing to make that initial capital expenditure and administrative expense, the 144 branches that we see presently are not just windows, but fully fledged Islamic banking branches.

During the last few years the branch networks have experienced exponential growth, in addition to the industry seeing the infiltration of leading local banks and a few multinationals. 2006 has shown the most significant growth in terms of the quality of the players entering the market. In four years the branch network has increased from 17 to 144, demonstrating that people have recognized Islamic banking as a veritable reality.

Products on offer

Islamic banks in Pakistan are using various modes of financing and investment including Murabahah, Ijarah, Istisnah, Salam,

January 2007[3]

Existing Islamic banking providers		Exclusive Islamic branches
1	Meezan Islamic Bank (fully fledged Islamic bank)	62
2	Bank Alfalah	22
3	Dubai Islamic Bank (fully fledged Islamic bank)	10
4	Bank Islami Pakistan (fully fledged Islamic bank)	10
5	Al Baraka Islamic Bank (fully fledged Islamic bank)	9
6	MCB Bank	6
7	Bank of Khyber	5
8	Askari Commercial Bank	4
9	Standard Chartered Bank	4
10	Habib Metropolitan Bank	4
11	Soneri Bank	2
12	Prime Commercial Bank	2
13	Bank Al-Habib	1
14	Habib Bank	1
15	National Bank	1
16	United Bank	1
	Total branches	144
License issued		
17	Emirates Global Islamic Bank (fully fledged Islamic bank)	Paid up Capital PKR2.1 billion (US$34.63 million). Formed by Emirates Investment Group, UAE.
18	ABN AMRO Bank	
In principle approval		
19	Bank Al Zamin (fully fledged Islamic bank)	JV between local group and Saudi based conglomerate. Paid up capital PKR2.2 billion (US$36.28 million).
19	Citibank	
20	Atlas Bank (Formerly Bank Ceylon)	
21	First Dawood Islamic Bank	
Planning phase		
22	Saudi Pak Commercial Bank	
23	Two fully fledged Islamic banks (initial discussions are underway with the Central Bank) to commence operations this year.	

Musharakah and diminishing Musharakah. Employing these modes of financing, Islamic banks in Pakistan are offering a full range of asset and liability products, including current and savings accounts (both rupee and dollar), working capital financing, project financing, car and housing finance, amongst many others.

Presently, the Murabahah and Ijarah structures constitute the bulk of assets portfolio, but as mentioned above their share is decreasing with the gradual growth in product development and the evolving regulatory and economic system.

continued...

Prospects for Pakistan *(continued...)*

Regulatory information[4]

The State Bank of Pakistan (SBP) has offered three options to existing and new banks to present Islamic banking products and services in Pakistan. These options are:

1. to set up a fully fledged Islamic bank in the private sector; or
2. to set up an independent subsidiary for Islamic banking by existing commercial banks; or
3. to set up (a) stand-alone branch(es) for Islamic banking by existing commercial banks.

The following steps must be taken:

- The bank has to apply for in principle approval.
- The bank has to submit a business case to SBP for obtaining a license.
- The bank is required to set up an Islamic finance division (IFD) at the head office in Pakistan in the case of a stand-alone branch.
- Existing conventional banks have to have at least one independent branch dedicated to Islamic banking. Every licensed branch of a bank shall carry a name, prominently displaying it as an Islamic banking branch.
- Conventional banks undertaking Islamic business have to clearly segregate Islamic banking branch(es) funds from conventional banking funds and have to maintain a separate book for Islamic banking branches. The bank must maintain a separate Islamic banking balance sheet within the operations of the bank. SBP has not determined specific disclosure requirements for activities under Islamic banking in the annual accounts of the bank, with a general view that appropriate information should be provided based on current operations, as and when required.
- The bank has to provide details of the organizational structure and training programs to SBP.
- The bank has to devise a Shariah compliant "profit and loss sharing" mechanism to pay out profits.
- The bank is required to maintain a minimum amount of 8% of the risk-weighted assets of Islamic banking in an "Islamic banking fund" as a reserve against potential asset loss on this portfolio. The initial funding requirement for this fund has been set at a minimum of Rs50 million (US$824,511), to be made available through conventional banking resources. Similarly the Islamic banking business will not be considered as an independent legal entity, but a part of the existing bank operations.
- The bank has to open a separate current account with SBP in order to maintain the cash reserve requirement (CRR) for Islamic banking at 7% of Time and Demand Liabilities (TDL). The bank has to maintain a separate SLR (Statutory Liquidity Requirement) for Islamic banking at 8% of TDL. Until the development of Shariah compliant inter-bank securities, the bank will maintain the SLR in the same CRR current account with SBP. Therefore, in all, CRR and SLR will be 13% of TDL. This lies in the current account without any profit, i.e. at 0%.
- The bank has to appoint a local Shariah advisor based on the "fit and proper" criteria of SBP. The Islamic scholar vets product features to ensure they are in line with the Shariah. All relevant documents, agreements and guidelines must be certified by the Shariah advisor.

"Within financings, Murabahah and Ijarah dominate, their collective share in total financings being 70% towards the end of 2006"

Future outlook

Pakistan's recent geopolitical resuscitation and resulting economic fortune is providing a fertile ground for the development of Islamic banking. The future outlook, against a backdrop of the increasing number of Islamic banking participants, expansion in the overall asset base, strengthening of the profitability indicators and contained credit and market risk, is promising.

The year 2007 will witness a lot of activity within the Islamic banking industry as other banks start Islamic banking operations. The merger of Habib Bank AG Zurich and Metropolitan Bank may also mean a further increased number of Islamic branches for these banks.

A number of businesses are becoming increasingly interested in Islamic solutions and are educating themselves on the options. As this trend continues we will see a transition from Shariah compliant products (i.e. the simulation of conventional products) to Shariah based products.

Islamic banks will have to focus their attention on service quality in order to gain customer loyalty. Most of the Islamic banks have yet to prove their mettle within the banking industry by providing superior customer service and quality.

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Prospects for Pakistan *(continued...)*

Uniformity in accounting practices is another major challenge facing the industry and expected implementation of the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) standards may be a vital first step in that direction, although a number of regulatory changes will be required in order to fully implement these standards.

Pakistan provides a good model for Islamic banking, where the government and the regulators have been proactive in creating a parallel system. Islamic finance will continue its strong growth and will become mainstream business in Pakistan. Hence institutions with a strong focus on research and development, innovation and service quality will truly benefit from this growth.

The author is currently working at ABN AMRO Bank Pakistan, looking after the development of Islamic products and businesses. He also serves as the secretary to ABN AMRO's global Shariah advisory board. Previously, he has worked at various large organizations with diversified experience in the fields of Treasury (FX and derivatives), business development (corporate, investment banking and retail) and Islamic product development. He also regularly lectures on Islamic banking at the central banks training institute in Pakistan.

The article above represents personal views of the writer and may not be construed as views of ABN AMRO Bank Pakistan.

[1] *Source: Authors analysis*
[2] *Authors analysis*
[3] *Authors analysis*
[4] *Source: State Bank of Pakistan*

Country Report: Sri Lanka

By Faizal Salieh

The economy

Sri Lanka's economic framework is supported by policies that encourage private sector participation, with low barriers to trade and investment. The Government has strengthened external trade relations by expanding bilateral, regional and multilateral trade arrangements. Of particular significance are the free trade agreements with India and Pakistan. The current account is fully convertible and the capital account is liberalized to a large extent.

The country's economy is dominated by the services sector, which consists of trade, port, telecoms, tourism, financial and business services. The financial sector is one of the fastest growing segments in the economy. There is a sound and modern banking system which dominates this sector. There are 22 licensed commercial banks and 14 licensed specialized banks, including 12 global banks. The Central Bank is actively working towards implementing the Basel II recommendations by 2008 and preparing to tighten controls on the ownership of banks. Monetary policy directions in 2007 are expected to promote the broad basing of shareholdings, reduce ownership concentrations, address conflicts of interest arising from large shareholdings and introduce a mandatory code of governance. New laws relating to debt recovery, asset management, credit information, electronic transactions and computer crimes are expected to be introduced this year. Efforts are also underway to further strengthen the legislative and institutional framework of the financial sector against money laundering, terrorist financing, pyramid-type network marketing, etc...

There are four players in the Islamic financial market in Sri Lanka. Amana leads the pack with unrivalled expertise and market share in Islamic financing, merchant banking, insurance, fund management and stockbroking. Ceylinco Profit Sharing, which is part of a large group involved in diversified businesses, is a recent entrant, followed by Islamic window operations from Union Bank of Pakistan (now acquired by Standard Chartered Bank) and MCB.

2006 was a tough year for the economy. Gross domestic profit growth is estimated at about 7.5%, compared to the targeted 8%, and the 6% achieved in the previous year. This is despite the early promise shown in the first quarter where GDP grew to 8%. High oil prices, inflation averaging 14% (peaking at 19% in December 2006) and increasing defense expenditure following the breakdown of talks with the northern insurgents put the economy under severe stress in the subsequent quarters of the year.

Inflation, on a point-to-point basis, increased from 14.6% in 2005 to 19.3% in 2006. High oil prices have historically caused strain on the financing of imports. The Government has recently resorted to hedging against oil price hikes to mitigate the price and exchange rate risks. The Central Bank has attributed the high inflation to the expansion of private sector credit by banks and has warned the banks of the consequential effects upon credit quality.

Interest rates are now on an upward trend and the local currency dipped by 6% against the US dollar between December 2005 and December 2006 (i.e. from SLR102.04 to SLR107.87). The exchange rate regime has been re-classified by the International Monetary Fund (IMF) as a "managed float" as opposed to a "free float." The recent move by the Central

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Key economic indicators

	2000	2001	2002	2003	2004	2005
GDP growth %	6.0	-1.5	4.0	5.9	5.4	6.0
Agriculture, fishing & forestry	1.8	-3.4	2.5	1.6	-0.3	1.5
Industry	7.9	-2.1	1.0	5.5	5.2	8.3
Services	6.9	-0.5	6.1	7.9	7.6	6.4
Investments/GDP	28.0	22.0	21.3	22.1	25.0	26.5
Inflation	6.2	14.2	9.6	6.3	7.6	11.6
Exports/GDP	33.4	30.6	28.4	28.1	28.8	27.4
Imports/GDP	42.0	37.9	36.9	36.6	40.0	38.3
Budget deficit/GDP	9.9	10.8	8.9	8.0	8.2	8.7
Exchange rate (SLR/US$)	80.0	93.20	96.70	96.70	104.60	102.10

Source: Central Bank of Sri Lanka

Country Report: Sri Lanka *(continued...)*

Bank to curb the imports of classified non-essential or luxury goods by requiring 100% cash margins for such imports has been interpreted as an exchange control measure on current payments.

In 2005, the average per capita income was US$1,197, compared with US$480 in 1980, reflecting a progressive increase in living standards. But this growth rate does not capture the distributional issues arising from it being largely concentrated in the western province and having little impact at regional levels. The western province, which includes Colombo, accounted for 51% of the GDP with only a 28% share of the country's population. That means 49% of the GDP is shared by 72% of the population living outside the western province. The Government is conscious of the regional income disparities and imbalances and their impact on society, and is taking steps to encourage more investments into regions outside the western province.

Although the official unemployment rate is 6.4%, a significant number of households in the country are beneficiaries of Government welfare schemes. 45% of the workforce is employed in the services sector, 31% in agriculture and 24% in industry.

"Sri Lanka has a good track record of foreign debt repayments with no default ratings whatsoever"

Sri Lanka's sovereign risk rating is BB- (Fitch) and BB+ (Standard & Poor's). Standard & Poor's (S&P) has affirmed a B+ rating on long-term foreign currency, a BB- rating on local currency and a B rating on short-term foreign and local currency. A high level of Government debt, weak public finance, a narrow tax base and security concerns regarding the unresolved northern ethnic conflict are the main factors affecting the risk ratings at present. However, S&P has observed that the economy has demonstrated a remarkable resilience, has benign terms of external trade which impose little stress on external liquidity, and has good medium-term growth prospects.

Sri Lanka has a good track record of foreign debt repayments with no default ratings whatsoever and is therefore seen as having sound long-term risk. The stock market, however, is seeing bullish foreign investor interest, particularly in the telecoms, infrastructure development and financial sectors.

Outlook for 2007

The Government's budget for 2007 projects a broad-based economy and a GDP growth rate of 7.5% facilitated by infrastructure development. It also predicts an overall balance of payments surplus of US$200 million, with exports increasing by 10%, imports by 12% and a budget deficit contained at 7% of GDP.

Sri Lanka is a major exporter of tea. Whilst tea prices are projected to be buoyant in 2007, there are critical issues in the tea industry that require early resolution. Rising input costs, declining workforce productivity, the uneconomic age profile of the tea bushes and high social costs are leading to a declining profitability in this industry.

Structure of the economy

Services	55.8%
Industry	27.0%
Agriculture	17.2%

The budget indicates no new revenue sources of a significant nature except for the changes in the existing tax system and revenues from administrative reforms, rather than revenue resulting from a higher economic growth. The Government will be compelled to adjust its expenditure to maintain the budget deficit within the limits specified by the international lending agencies. A high budget deficit will pose a formidable challenge to the country's monetary policy.

The Government needs to increase investments from the current 25% of GDP to 32% in order to attain an 8% GDP growth rate. The challenge for the Government now is to chart the course for a mixed economy with selected but vigorous deregulation and also to unlock more of the economic sectors for private sector investment and participation. It should opt for higher revenue generation from higher economic growth, resulting in lower tax burdens, rather than depending on higher taxes as the main source of revenue. In this regard, the aggressive pursuit of foreign direct investments should be of critical importance for the development of the country.

Sri Lanka's revenue base is dominated by a complex tax system. There are a variety of taxes, levies and surcharges which are introduced or varied from time to time to meet the shortfalls in revenue. Value added tax (VAT) and the economic service charge (ESC) have been subject to changes every year since their introduction a few years ago. This underlines the weak revenue base of the economy.

The Government is alive to the economic realities of the country, but is constrained by the political conditions surrounding it, mainly a weak coalition in parliament and the unresolved ethnic issue. In recent times it has made some concerted moves to address both these factors. It has signed

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Country Report: Sri Lanka *(continued...)*

a historic MoU with the main opposition party in parliament to work together on an agenda which includes certain economic and peace-related initiatives. This move has helped it to marginalize an extreme leftist-oriented coalition partner and look ahead positively towards facilitating economic growth in the immediate future. The practical success of this move will be seen as the days unfold.

On the ethnic issue, the Government is pursuing a course of action which involves keeping the doors open for political negotiations whilst engaging in limited military actions to ward off security threats from the LTTE. The cease fire agreement between the LTTE and the Government is largely holding whilst being occasionally dented by both parties.

"The safety of foreign investments is guaranteed by the constitution and equal treatment is assured for foreign and local investors"

Investment climate

Despite the current political status, analysts see now as an opportune time to invest in Sri Lanka, as most assets in the country are still available at discounted prices. With economic policy directed at rapidly improving the country's infrastructure, Sri Lanka will be able to upgrade the value of its assets and generate substantial dividends in the medium to long-term.

Sri Lanka has positioned itself as the services and trading hub of the South Asian subcontinent and has been progressively opening its economy to trade and investment. Its strategic location as an island with access to major shipping routes in South Asia and the Far East, advanced communication links and the aspiration to become a regional financial center make it one of the best investment locations in the region. It is ranked high on the Human Development Index. English is widely spoken and is the main language of business. The country has already reached several Millennium Development Goals in universal primary schooling, gender equality and infant and maternal mortality.

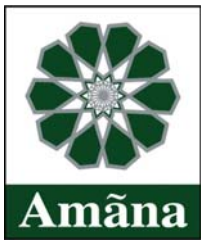
Key social indicators

Literacy Rate %	93
Life expectancy (years)	74
Infant mortality rate (per 1000 live births)	11.7
Maternal mortality rate (per 1000 live births)	0.9
Human Development Index	0.751

Source: Central Bank of Sri Lanka

Potential investment sectors include hi-tech agriculture, deep sea fishing, highways, railways, airport and port development, tourism, petroleum, oil refining and oil exploration, ICT, BPO, health, education and the financial sector.

The safety of foreign investments is guaranteed by the constitution and equal treatment is assured for foreign and local investors under the country's general and investment laws. Bilateral investment protection agreements have also been signed with many countries and a large number of global businesses are present in the country.



The author is the managing director of Amana Investments, the pioneer and largest Islamic financial institution in Sri Lanka.

Development of Indonesia's Islamic Capital Market

By Arlyana Abubakar and Sari Nadia Z. Rizal

As a Muslim-majority country (about 85% of the population of 230 million are Muslim), Indonesia offers bright prospects for the development of the Islamic financial industry. This calls for untiring efforts to build Shariah financial markets in Indonesia so that the Shariah financial system can make a greater contribution to the national economy. The Shariah financial market is currently enjoying rapid growth, marked by the increasing number of Indonesian corporations issuing Shariah financial instruments – structured in various forms – to raise financing, as well as the growing public understanding of Shariah economics, banking and financial instruments. Reinforcing this growth are government initiatives to issue regulations addressing the current constraints on the development of Shariah financial markets in Indonesia. All of these factors offer positive support for the future development of an Islamic capital market in Indonesia.

The Indonesian economy

As Indonesia enters its tenth year following the Asian economic crisis, much progress has been achieved in rebuilding the economy. As of 2006, the Indonesian economy had achieved significant gains, with steady improvement in macro-economic and financial performance. During 2006, the Indonesian economy achieved a 5.5% growth. Inflation was subdued, coming in below the targeted level. International reserves amounted to US$42.6 billion at the end of 2006, with the strong balance of payments performance bringing stability to the rupiah throughout the year. Significant improvements also took place in the financial and operational performance of the national banking industry. Under these conditions, Indonesia's economic growth in 2007 is predicted to improve to about 6%.

International rating agencies have upgraded Indonesia's sovereign rating. Following the sharp downgrading during the crisis period, there has been steady improvement in Indonesia's rating. The latest Indonesia sovereign ratings reported for 2006 are BB- (Standard & Poor's), B1 (Moody's) and BB- (Fitch). Although the sovereign rating has yet to reach investment grade, as it was before the crisis, further upgrading is expected in 2007, which will send a positive signal to foreign and domestic investors regarding investment in Indonesia, including the purchase of securities issued by the government and corporate sector.

The present condition of the economy is a key factor supporting government efforts for further development of the Indonesian capital market as a whole and especially the Islamic capital market.

Development of the Islamic capital market

Islamic finance in Indonesia is relatively new compared to conventional finance, but the sector has nevertheless seen rapid growth. The growth driven by the Shariah banking industry is officially based on the legal provisions of Act No. 7 of 1992 concerning banking, as amended by Act No. 10 of 1998. Bank Indonesia, the Central Bank of the Republic of Indonesia, has developed an initiative for the development of the national Shariah banking system, which is set out in the *Blue Print for Development of the Indonesian Shariah Banking System*. This strategic initiative has been developed within an objective and realistic framework in order to build sustainability and consistency into the Shariah banking development program in Indonesia.

Over time, assets managed by Indonesia's Shariah banks have steadily mounted from Rp7.85 trillion (US$865 million) in December 2003 to Rp26.72 trillion (US$2.94 billion) in December 2006 (*Source: Publication of Shariah Banking Data, Bank Indonesia, December 2006*). Even so, Shariah banking still accounted for a very small share of the national banking system – at only about 1.5% – in October 2006. Furthermore, while the number of Islamic commercial banks (Bank Umum Shariah) in Indonesia remains unchanged at three (no new banks have been established since 2004), there has been considerable expansion in Islamic banking unit (Unit Usaha Syariah) and Islamic rural banks (Bank Perkreditan Rakyat Syariah). Up to 2006, Indonesia's banking system included 19 Shariah divisions and 105 Shariah rural banks. To promote more rapid growth in Shariah banking in the 2007–2008 period, an acceleration program has been launched with the involvement of all stakeholders. This program envisages building the Shariah banking industry to about 5% of the overall banking industry in Indonesia by the end of 2008, while upholding prudential banking and compliance with Shariah principles (*Indonesian Sharia Banking Outlook for 2007*, Bank Indonesia, December 2006).

In line with the development of Shariah banking, the Islamic capital market in Indonesia is also on the rise. Shariah based stocks listed on the Jakarta Islamic Index (JII) soared 54%, climbing from 199.75 at the end of 2005 to 307.62

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Development of Indonesia's Islamic Capital Market *(continued...)*

on the 27th December 2006 *(Source: Bloomberg)*. As can be expected with the rising turnover in Shariah capital market products, there has been growing activity in Shariah mutual funds during recent years. These first came on the market in 1997 and initially received little public attention. Since then, however, Shariah mutual funds have undergone remarkable growth and expansion. In 2003, Indonesia had only three Shariah mutual funds. However, during 2006, this number had risen to 20 mutual funds, representing a combined net asset value of Rp663.7 billion (US$61.6 million). *(Source: Chief of Capital Market Supervisory Agency as cited from Indo Pos Online, 2nd January 2007)*

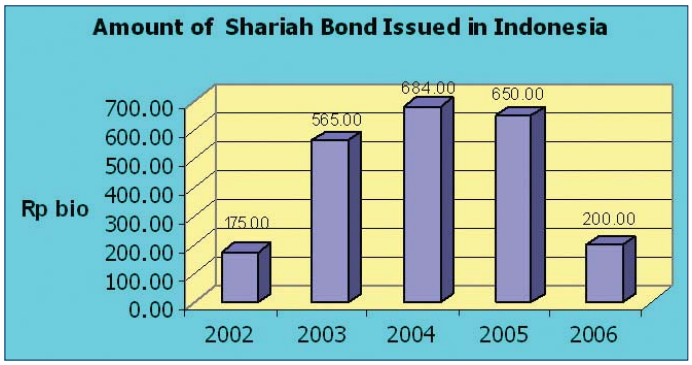
Another growth area is the Shariah bond market, marked by steady expansion in amount of Shariah bond issues (see chart 1). There are two types of Shariah bond issued in Indonesia so far, namely Ijarah accounting for 64% (Rp1.459 trillion) (US$160.6 million) and Mudharabah for 36% (Rp815 billion) (US$189.7 million). The first corporation to launch Shariah bonds in Indonesia was Indosat. In 2002, this telecommunications giant organized a Rp175 billion (US$19.29 million) Shariah bond float shortly after the National Shariah Council (DSN) issued its fatwa on Shariah bonds. This issue was for Mudharabah bonds with variable rate. In subsequent years, other Indonesian corporations have followed suit with flotations of Mudharabah and Ijarah bonds.

In 2003, five corporations issued Mudharabah Shariah bonds, bringing growth in bond issues to 222.86% as compared to 2002. The two leading bond issues were launched by Bank Muamalat and Bank Syariah Mandiri, each valued at Rp200 billion (US$22.01 million). In 2004, corporations began to show keen interest in Ijarah structured Shariah bonds. That year, total bond issues were up only 21.06% from 2003. In 2005, total Shariah bond issues in fact contracted by 4.97%, only three corporations floated Shariah bonds, led by Indosat with an issue worth Rp285 billion (US$31.36 million). The contraction still exists in 2006 where only one corporation issued Shariah Bond.

Up to 2006, however, 17 Indonesian corporations issued Shariah bonds worth almost Rp2.274 trillion (US$250.36 million). Interestingly, the first company to issue Shariah bonds was not one operating under Islamic principles. Even up to 2006, bond issues continued to be dominated by non-Shariah based corporations. This demonstrates that the Indonesian corporate sector, like corporate issuers in the international market, regard Shariah bonds as a potential and feasible alternative for use in overall corporate asset and liabilities management.

Despite this, the financing raised through Shariah bond issues accounted for a mere 3% share of the Indonesian financial market *(Source: Karim Business Consulting)*, which is dominated by conventional financial transactions. In addition, Shariah bonds issued in Indonesia are denominated in Indonesian rupiah; no company has yet issued Shariah bonds in an international currency. Likewise, the government of Indonesia has yet to tap domestic or international Shariah bond markets. So far, the government has confined its bond issuing activity to conventional bond markets.

Chart 1: Shariah Bonds in Indonesia



Source : Bloomberg as of 31/1/2007

Problems, challenges and prospects

Indonesia's Shariah capital market is not showing the same vigorous growth as the Shariah banking system in Indonesia. Furthermore, in terms of presence on the international Shariah capital market, Indonesia lags far behind Malaysia, another Muslim-majority nation, although Indonesia potentially has a tremendous opportunity to build its share of that market.

Shariah bonds, as one of the instruments used on the Islamic capital market in Indonesia, have the potential for open-ended growth as a financing alternative for the corporate sector and for the government of Indonesia itself. The keen and growing interest among Islamic and non-Islamic investors in these instruments, when combined with the steady improvement in economic conditions and a potentially large Shariah bond market, represents strengths and opportunities that need to be seized in order to achieve more robust growth on Indonesia's Islamic capital market in general and the Shariah bond market in particular.

However, the obstacles and challenges confronting Indonesia in the development of the Shariah financial market are indeed formidable. The issues involved are multi-faceted. Most important, however, is the inadequate legal framework, institutional structures, supervision, limitations in human resources, taxation problems, risk management and mitigation, a small market share compared to conventional financial products and the lack of a secondary market. It is important for all stakeholders to take careful note of these weaknesses and threats and to seek out solutions. For these

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Development of Indonesia's Islamic Capital Market *(continued...)*

reasons, the development of the Shariah capital market in support of the Indonesian economy is an effort that calls for the concerted attention of all stakeholders.

"One action taken by the government is the development of a legal framework for Shariah bond issues"

Having analyzed the potential for the market, the government and stakeholders need to work to promote the development of the Shariah financial market in Indonesia in line with international practices. The tasks involved include the following:

- The development of a legal framework for facilitating the development of the Shariah capital market and the creation of Shariah capital market products. To prepare for this, the Capital Market Supervisory Agency (BAPEPAM) has established the development of the Shariah capital market and products as one of its key working priorities for the next five years, as set out in the Indonesian Capital Market Master Plan for 2005–2009. It is also crucial to take immediate action for the development of the legal framework pertaining to taxation issues.

- The development of a global Shariah bond market for issues of sovereign and corporate bonds. The development of the US dollar Shariah bond market (global Shariah bonds) will of course be harmonized with the development of the rupiah Shariah bond market. This market requires the development of a secondary market, one that in essence requires heterogeneity, opportunities, information and expectations on the part of the market players. To this end, the development of the Shariah bond secondary market will include efforts to encourage Indonesian corporations to acquire larger quantities and greater diversity of Shariah financial instruments and to promote the distribution of these instruments to a broader investor base.

- Building the numbers and the qualifications of human resources for the Shariah financial industry. This will take place through education, the introduction of Shariah financial instruments to the public and in investment training to build a more skilled workforce for the Shariah financial industry. The growing numbers of educational institutions in Indonesia offering study and training programs related to the Shariah financial industry reflects the keen interest of many in building the qualifications of those employed in the industry. Higher numbers of more qualified personnel will build the competitiveness of the Shariah financial industry and thus support the development of a fair, efficient and transparent market.

For the government, the rapid development of Islamic financial markets in the Middle East, Europe and Asia, as well as the steady improvement in Indonesia's economic fundamentals, political stability and sovereign rating makes it an ideal time to become active in bond issues on international Islamic capital markets. For this reason, the government of Indonesia is considering the possibility of using Shariah financial instruments as an alternative source of funding for investment and development and to anticipate fiscal needs arising from the financing gap and the savings–investment gap.

The government is currently exploring possibilities for issuing Shariah bonds on international and domestic markets, given the attractiveness of this option for management of government assets and liabilities. One action taken by the government is the development of a legal framework for Shariah bond issues in the Draft Law on Government Shariah Securities. This legal framework is expected to resolve the various problems that have held up the issuance of government Shariah bonds, including issues related to the transfer of underlying assets in Shariah bond issues, the establishment of Special Purpose Vehicles (SPVs) and taxation issues.

With work on the draft law moving steadily forward, the government of Indonesia is expected to begin issuing Shariah bonds on the domestic and international market in the near future. These bond issues are expected to establish a benchmark for corporate rupiah denominated Shariah bond issues, many of which have been launched in past years, and encourage Indonesian corporations to issue foreign currency Shariah bonds on the international market. The active role of the government, corporations and banks in issuing these Shariah financial instruments is expected to promote the development of the Islamic capital market in Indonesia.

The authors are deputy manager and economic analyst in Foreign Debt Analysis and Investor Relations Division, International Directorate, Bank Indonesia.

A Market Economy – Brunei

By Dr Abul Hassan

The principal goal of any country's development policy is to create sustainable improvements in the people's quality of life. After several decades of Muslim countries' preoccupation by the colonialists' power, an increasing number of developing and developed Muslim countries have shifted their economic growth focus to market signals. This is guiding the allocation of resources in which the role of prices is being emphasized, profits are becoming a measure of economic success for enterprises, and financial markets are being promoted to allocate resources to profitable activities within a competitive environment. Deregulation and liberalization in the economic and financial system are carried out in order to nurture competition among various market participants and to enhance the allocative efficiency of the economy.

Planned economy or market economy?

After World War II, the economic development model was inward-oriented in many countries, relying upon government intervention to set pricing signals and promoting strong participation of the state in the production of goods and services. The market economy approach, on the other hand, is outward-oriented through a free market mechanism where market prices play the dominant allocative role. The role of the government in this outward-oriented development model is to provide a level playing field for all market participants through deregulation and liberalization. Here, the existence of a substantial private sector is a necessary but not the only condition for economic development, which also requires open competition.

Advocates of planned economy say that a planned economy can better provide for the material needs of a society. But empirical evidence says that this theory suffered a severe setback with the fall of the Soviet Union and the adoption of China's open economic policy. The planned economy was unpopular with Muslim economists from the beginning. There are numerous traditions that demonstrate that the Prophet Muhammad turned to the marketplace to determine the just price of commodities. On learning that his companion Bilal had traded poor quality dates for high quality dates, the Prophet advised him that buying and selling at market prices rather than bartering avoided the dangers of overcharging (riba) inherent in a barter system. As might be expected from this respect for the market's ability to set just prices, Prophet Muhammad disliked price controls and limited his intervention to the prohibition of practices like fraud and riba (usury).

The Islamic analysis of markets had reached the level of economic science by the time of the great fourteenth century historian Ibn Khaldun. According to him, the fact that the policies mandated by God could be scientifically demonstrated as the best social policies was the natural consequence of the fact that the laws of economics and the laws of good living had the same creator. It is no accident that Muslim countries like Bahrain, Iran, Kuwait, Malaysia, Qatar, Saudi Arabia and Sudan, which all followed a short market economy, have consistently outperformed other countries with central planning and state control of their economy. Without a doubt the market economy possesses many advantages over a planned economy.

Advantages of a market economy

First, a market economy assures more efficient resource allocation as new investment resources are channelled to those sectors and projects that generate the highest possible economic returns. Islamic economic principles support this mechanism. In a planned economy, in contrast, scarce investment resources are allocated based upon various non-economic factors that may be tied to the preferences of the government leaders, thereby leading to lower investment returns. Furthermore, in a market economy, the investors are directly responsible for the risks and returns of a project since their own capital and resources are involved. This leads them to be more careful and thorough in calculating the expected returns from their investments and to pursue only those investments that are likely to reach optimum results.

The Islamic system is a just and equitable system that promotes win–win relationships between economic agents. For example, the relationship between financiers and users of capital is based on co-operation and the equitable sharing of risks and rewards. It abhors oppressiveness and adversarial, asymmetric relationships. It is meant to be efficient in wealth distribution and, perhaps more importantly, the system demands that capital be used for productive purposes. In a planned economy, decision-makers are not utilizing their own resources but rather the state's funds and thus the investment decisions involving state resources would sometimes be less disciplined in nature.

Secondly, in a market economy most resources are raised by the private sector, and the government is not active in raising funds for its own public investment operations. In

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A Market Economy – Brunei *(continued...)*

a planned economy, however, public funds for investments are often raised through government financing activities such as new taxes and/or public borrowings, which push out private investors from the capital market and raise interest rates in general for non-public fundraisers (certainly this is not the case in Brunei). Thus the cost of capital for private sector investors in a planned economy is higher, which tends to discourage new investments by the private sector, leading to chronic shortages and market distortions. In a market economy, less government means less taxes and more funds for private investors at less cost, which increases the returns to investors in general. The core principles of Islamic economics have always favoured healthy competition.

Thirdly, less government in general implies less waste of taxpayers' money, less corruption and more transparency. A market economy implies more private sector initiatives and individual responsibilities. Welfare is limited to those who truly deserve public assistance due to physical or mental handicaps and welfare recipients are expected to follow certain social norms of responsible behaviour in return for public assistance. Since all able-bodied persons are expected to contribute to society through hard work and discipline, there is less room for waste and abuse of taxpayers' money. This is certainly in line with Islamic business ethics. Smaller governance in a market economy means fair regulation and a participatory role of the people in the development process. Since more working people are available in a market economy, the overall production volume of goods and services should be higher than in a planned economy country with a comparable population base.

Fourthly, a market economy frees up the creativity and innovative spirit among people who can expect to benefit from their own creative ventures. A pervasive problem in socialist countries was the lack of motivation on the part of economic participants, as they are protected by the government's "iron bowl." Risks and rewards for one's own efforts are not properly shared in a planned economy where the government elite determine the rewards for members of society based on their own politically motivated criteria. The result is often a complete abdication of initiative and hard work as there are often no rewards for extra effort and instead some risk of being penalized for disturbing the accepted norms of social behaviours and work patterns. The Islamic economic system does not subscribe this system.

Fifthly, in a market economy the private sector generally provides more attractive opportunities for reaping financial rewards. Thus, more gifted and talented persons tend to congregate toward private ventures and initiatives rather than being attracted to a public service career. Of course, there are exceptions, but in general people value the material wellbeing of themselves and their families highly. Since a market economy provides the most opportunities for the advancement of one's material wellbeing through hard work and creativity, more talented people tend to engage in private economic ventures producing those goods and services. This will be in response to demand from the market, rather than in a planned economy where the route for advancement and financial security is mostly found in a public service career. The Quran emphasizes the importance of commerce and productivity.

Finally, a planned economy cannot adequately cope with today's globalized world, which is ever more closely inter-connected through digitalized communication networks and modern transportation links. A planned economy might have fared better in an earlier industrial era when the main economic activities revolved around heavy machinery industries and were measured by annual coal and steel production volumes. Today's economy is more service-oriented and therefore the critical economic signals are more complicated. A market economy possesses the required flexibility and dexterity to understand and respond to the complex modern economic signals emanating from all corners of the globe. It takes a degree of vision, insight and indeed foresight to collect diverse market signals and to organize the most appropriate economic schemes and business ventures to exploit the current and emerging opportunities.

An example: Bahrain

A vivid example of this trend can be seen in the city of Bahrain in the Middle East. Twenty-five years ago, it used to be a sleepy town of less than 200,000 residents toiling in the peoples' communes, but now it has exploded into a dynamic metropolis of over 700,000 (which includes 235,000 non-nationals) people working and living in ultra-modern office buildings and sleek apartments. The city has attracted numerous high-tech and trading companies from all over the world. The transformation of Bahrain into a modern Muslim state is a direct result of Bahrain's adoption of the market economy and the establishment of its offshore international Islamic financial market. Among the many offshore banks, the Arab Banking Corporation provides a wide range of banking services including corporate banking, treasury, Islamic banking and private banking. At present Bahrain hosts 180 financial institutions and more than 100 insurance companies. Its stock exchange listed 41 local and eight foreign companies valued at US$7.04 billion at the end of September 2004. In addition to serving as a regular stock exchange, the Bahrain Stock Exchange acts as a securities regulator and undertakes supervision of the capital market in general. Bahrain's financial sector represents a unique blend of local, regional and international names, and offers

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A Market Economy – Brunei *(continued...)*

a diversity of financial services, products and activities. They include 11 fully Islamic banks, with one of the highest concentrations of Islamic banking assets (some US$2 billion in 2003) and services in the world. The Islamic market strives to create employment opportunities in the country and to establish development opportunities.

A country's financial system and markets constitute an important part of the total infrastructure for the economy. An efficient financial system performs three main tasks: first, it handles payments; secondly, it channels savings to investments with a good return for future consumption; and thirdly, it spreads and reduces economic risks in relation to the players' required returns. The smooth functioning of all these activities facilitates economic growth in that lower costs and risks promote the production of goods and services as well as employment. In this way the financial market contributes to increased prosperity. In a market economy, the establishment of a capital market is very important. Just as it is important that networks for transport and telecommunications function properly, so is it essential that payments can be transacted, capital can be saved and channeled to the most profitable investment projects and that households and firms can get help in handling financial uncertainty and risk.

Islamic finance in Brunei

Brunei Darussalam represents an example of a country where a functioning banking system has been built within only a few years. Given the initial start-up conditions and some deficiencies in the overall economic/legal/institutional framework characteristic to transition economies, the case of Brunei can in many respects be regarded as a success story. Its economy expanded the oil and gas sector into a world class industry. The government has taken appropriate steps to diversify service sectors of the economy. In the second quarter of 2005, the growth of the service sectors (including banking and insurance) reached 9.4%, as compared to the same period in 2004. A quarter on quarter comparison showed that the service sectors had grown by 4.8%. Remaining outstanding issues include the lack of infrastructure within the development of the capital market and institutions, but these issues can only be overcome once the process of formation of the capital market starts.

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A Market Economy – Brunei *(continued...)*

In order to establish a security market in any economy, certain legal, institutional, economic and value-based social conditions must exist. Most important among these factors are the existence of well-defined property rights based on a private property doctrine; the existence of corporate (limited liability) forms of entrepreneurship; the enforcement of contracts; and free price formation based on demand and supply. Brunei is definitely well qualified in respect of the formation of an Islamic securities market.

The following features exist within in the system of Brunei:

- A private property doctrine proceeding legal and institutional reforms (e.g. institutionalization of private ownership and entrepreneurship, ownership reform, initiation of privatization of state-owned enterprises).
- Market economy relevant economic and institutional reforms (e.g. monetarization of the economy, price liberalization, corporatization of businesses and enforcement of contracts).
- The majority of the people in Brunei are practising Muslims and would like to lead their life according to the Islamic teaching which says interest is forbidden but business is halal.

However, there remain critical policy issues relating to the formation of the Islamic securities market and institutions which need to be addressed.

- The creation of an appropriate regulatory framework for securities, the securities market and its participants.
- The creation and development of the appropriate infrastructure for the securities market.
- The development of supervision and monitoring systems with sufficient authority.
- Training of professional personnel and educating the general public in securities investment.
- The promotion of investors' interest in security investments.
- The establishment of foundations for the creation and development of institutional investors.
- Institutionalization of accounting standards and auditing.
- With the development of a security market and shareholder institutions, corporate governance and agency costs issues will need to be tackled. Stocks will provide not only rights for participation in financial proceeds, but will also provide shareholders with the right to participate in company control by voting.
- Appropriate taxation policy is one of the crucial regulatory means through which the development of a securities market can be directed.

With regards the prospect of the establishment of a stock exchange in Brunei, a number of factors within the overall economic, legal, institutional and social infrastructure have been identified. It must be remembered that future economic development may be driven by market forces initiative, as well as by direct and indirect government policies. Keeping this in mind, policy-makers should constitute a taskforce to examine these issues in order to establish an Islamic securities market. For the purpose of buying and selling securities in the primary market, the role of the secondary market is very important. Due to liquidity and pricing reasons, there may be demand constraints from insufficient internal resources. Even if the external financing companies rely predominantly on bank loans, the role of the Islamic securities market should grow gradually. With the expansion of the economy and economic agents, the banking system will make the raising of equity capital imperative.

Brunei's government has focused on industrial development, with an emphasis on the development of small and medium enterprises, which will create an optimum level of employment opportunities in the economy. However, an important reason for the lack of entrepreneurial development in Brunei is the absence of capital being intermediated to the needy, as they lack collateral and banks rarely look at the viability of a project in isolation. In a market economy, this sector will grow by promoting, in a bigger way, equity-based instruments. Even in the case of the debt-based instruments of the Islamic financial market, the emphasis must be on project viability rather than collateral.

Conclusion

Ibn Khaldun stated in his book *Muqaddimah* that social justice, the rule of law, property rights, a culture of tolerance and co-operation among constituents, a willingness to innovate, and economic strategies that target growth and development with equity are all crucial and inter-dependent elements that form the enabling environment to strive for success, both in this world and in the hereafter. If we are to look at the Islamic financial system, it is natural that we look to the core of Islam itself. Unlike many other religious systems, we see Islam as a complete way of life. Beyond basic religious beliefs and practices, Islam shows us how to best conduct ourselves in everyday matters through the Shariah, which is the basis of the Islamic financial market. The establishment of an Islamic capital market through a market economy may be a suitable tool of competitive advantage for the economic success of Brunei Darussalam.

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Singapore Exchange - Islamic Finance Prospects

By Kok Cheang-hung

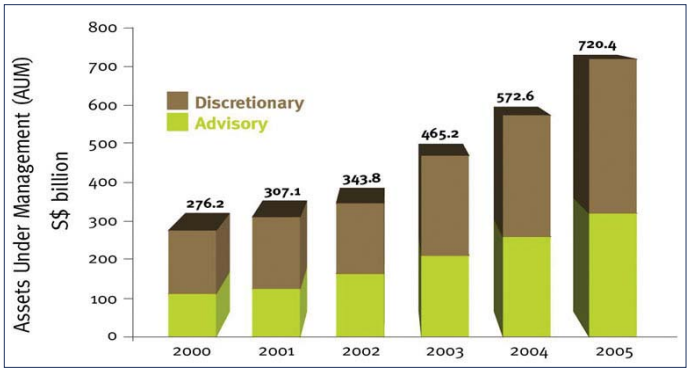
In recent years, the Singaporean government has been pushing the ambition to be an Islamic finance hub. Given such impetus, it has launched numerous initiatives to boost the growth of Islamic finance by encouraging Islamic financial institutions to set up offices in Singapore, and enhancing bilateral ties with various Middle East and North Africa (MENA) countries.

The government is helped by the fact that Singapore is a racially, culturally and religiously diverse island state, where care has been taken to cater to the needs of diverse communities. Muslims in Singapore make up 14.9% of the local population, and as Singapore was formerly a state within the Malaysian Federation, its government is familiar with the uniqueness and attractiveness of Islamic finance.

Today, Singapore is recognized as an international financial center. Its thriving financial services industry serves not only a vibrant domestic economy, but also the rest of the world. There are over 700 local and foreign financial institutions in Singapore, offering diversity in services and products. This attests to the vibrancy, sophistication and attractiveness of the present financial landscape.

Due to Singapore's policy of welcoming foreign companies and the large available liquidity pool from international funds, Singapore is now an internationally recognized fund management center, with total assets of more than S$720 billion (US$467 billion) under management at the end of 2005. This provides ready funding support for the growth of international companies seeking to raise capital, both Islamic and conventional.

Figure 1: Six-year growth of assets under management (AUM) (S$)



Singapore has also earned numerous accolades from various reports and institutions, including being named by the Bank for International Settlements (BIS) as the world's fourth most active foreign exchange trading center after London, New York and Tokyo.

SGX – developing the Asian gateway

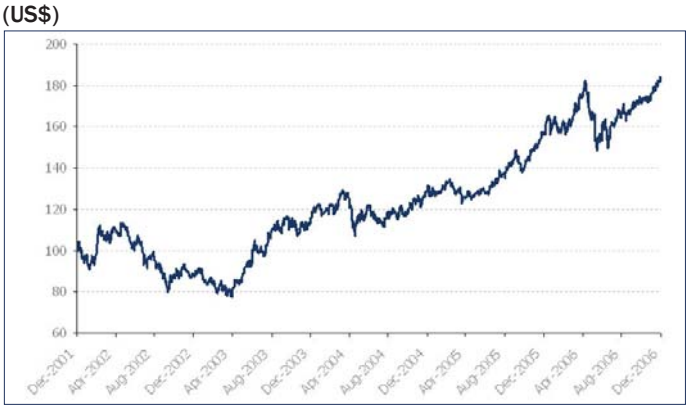
The current surge in and increasing awareness of Islamic finance has also seen a number of major banks and funds domiciled in Singapore offering Shariah compliant instruments and facilities. In this light, as the island state's securities and derivatives market operator the Singapore Exchange (SGX) has embarked on a number of initiatives.

In collaboration with the FTSE Group, SGX launched a series of FTSE SGX Shariah Indices early in 2006. This index series is designed to reflect the stock performance of companies in the Asia-Pacific region whose business activities comply with Islamic Shariah law. The independent Shariah screening is provided by the renowned Yasaar Research.

This index series is calculated in accordance with the Industry Classification Benchmark (ICB), an international standard developed by a partnership between the FTSE Group and Dow Jones. As this series is calculated daily and denominated in US dollars it can be used as the basis of index-linked funds, Exchange Traded Funds (ETFs) and over-the-counter (OTC) products.

The first index of the series – the FTSE SGX Asia Shariah 100 Index – was launched in February 2006 and comprises the 100 Asian largest companies in terms of market capitalization. This index is made up of 50 Japanese companies, with the rest coming from Singapore, Taiwan, Korea and Hong Kong.

Figure 2: Five-year total return on FTSE SGX Asia Shariah 100 Index (US$)



The FTSE SGX Asia Shariah 100 Index is the first of its kind as it reflects the performance of Shariah compliant companies

continued...

Singapore Exchange - Islamic Finance Prospects *(continued...)*

in Asia and enables Islamic investors a unique opportunity to benchmark their Asian Shariah compliant equity funds. The stocks selected are free-float weighted and liquidity is screened to ensure that only the investable-cum-tradable set of stocks is included.

To that effect, SGX is planning to launch an Exchange Traded Fund (ETF) based on the FTSE SGX Asia Shariah 100 Index. The advent of this ETF will allow direct and cheaper access for investors, both Islamic and non-Islamic, to partake in the halal version of the exciting Asia growth story.

Currently, SGX has a comprehensive suite of ETFs that includes regional indices and commodities-related choices such as Gold ETF. The streetTRACKS® Gold Shares is the first gold-backed exchange-traded fund to be listed in Asia. Sponsored by the World Gold Trust Services, the streetTRACKS® Gold Shares are designed to track the price of gold and trade like any stock on the exchange. The Gold Shares are backed by physical allocated gold bullion and are denominated in US dollars. Investors can buy as little as one board lot of 10 shares, with each share priced at approximately one-tenth the spot price for an ounce of gold.

"Singapore can certainly leverage on its advantageous position to develop itself as the Asian gateway for Islamic products and services"

The most recent listing of an ETF on SGX was the Lyxor Commodities ETF. Based on the world renowned Reuters/ Jefferies CRB Index, the Lyxor Commodities ETF offers investors a convenient and efficient way to track the performance of the commodities market. For the first time in Asia, investors can access a basket of 19 commodities, covering energy, precious metals, industrial metals, agriculture and livestock through one simple investment.

In addition, Singapore has also gained popularity as the region's main risk management and derivative trading hub. With the CNX Nifty (India) and FTSE/Xinhua A50 China index futures contracts listed on SGX, international investors can now participate in the two most prolific Asian economies via the SGX gateway. SGX currently offers 23 futures and option contracts. Most of these contracts are quantos denominated in US dollar.

SGX – harnessing the Asian listing platform

To date, the SGX has more than 700 listed companies. Over one-third of the listings are foreign companies. This is testimony to the fact that SGX has emerged as the choice listing venue in the Asia-Pacific for both companies and potential issuers/sponsors of investment products. As at the 31st December 2006, the securities bourse has a total market capitalization of US$386 billion. This is illustrated in the Straits Times Index, which is the benchmark index for the Singapore stock market.

Figure 3: Historical price chart on the Straits Times Index

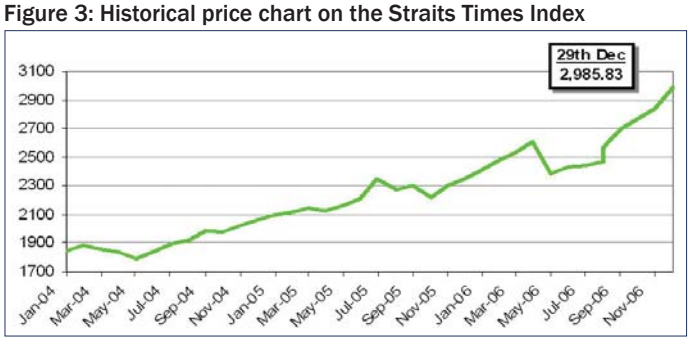


Figure 4: Average IPO proceeds and market capitalization

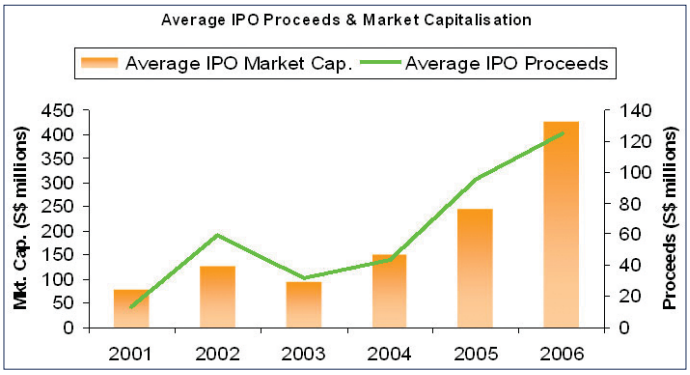
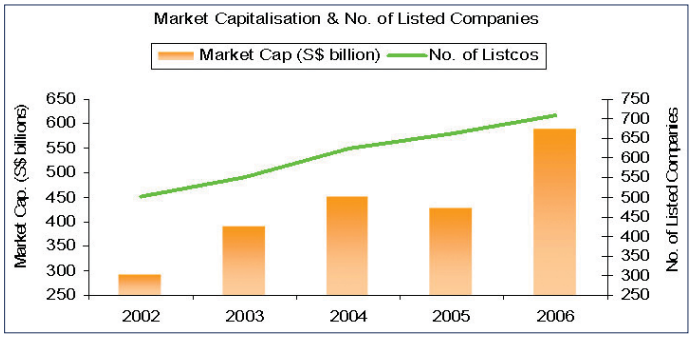


Figure 5: Market capitalization and number of listed companies



Another interesting fact about the securities market in the SGX is that about 10% of the listed firms are deemed Shariah compliant.

Foreign companies are well received by investors and enjoy a higher turnover velocity than local stocks. Such receptivity to foreign companies is a unique characteristic of the Singapore market which foreign companies find appealing

continued...

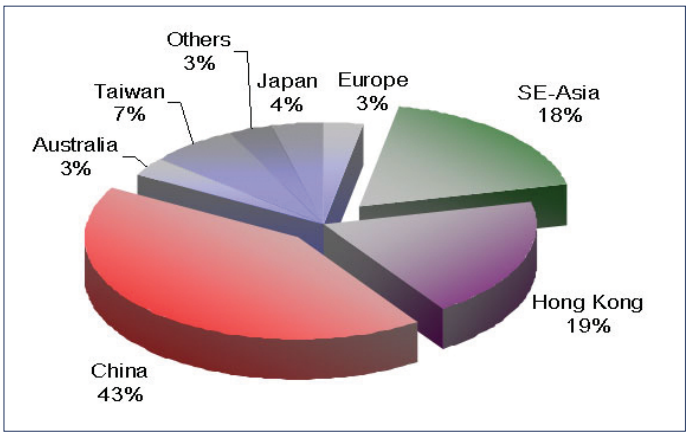
Singapore Exchange - Islamic Finance Prospects *(continued...)*

when choosing SGX as a listing venue. Foreign listings are a major driver of the business at SGX and continue to be a key focus. Apart from Greater China, which forms about 25% of the listings, it has also diversified into attracting companies from South-East Asia, India, Korea, Europe, the US and even the Middle East.

"Singapore can certainly leverage on its advantageous position to develop itself as the Asian gateway for Islamic products and services"

Other than the IPO market, SGX has also been successful in the listing of real estate investment vehicles such as real estate investment trusts (REITs). Singapore REITs have experienced strong growth, with market capitalization increasing by 114% per annum over the last four years. In terms of the number of listings and market capitalization, SGX is second only to Japan. According to numerous market analysts, SGX-listed REITs are presently amongst the most attractive in terms of dividend yield.

Figure 6: Breakdown of foreign listed firms on SGX



SGX – Entering new markets

In May 2006, SGX launched the SGX AsiaClear™, an OTC clearing facility for oil derivatives and dry bulk forward freight agreements (FFA). SGX AsiaClear™ presently clears 21 different OTC trades, and at the end of 2006 it had over 60 counter-party accounts.

Commodities have been the best performing asset class globally over the last few years. In relation to this, SGX has partnered the Chicago Board of Trade (CBOT) to form Joint Asian Derivatives Exchange (JADE), an Asian commodity derivatives market. JADE specializes in Asian-based commodities and has launched its first product, the TSR 20 Rubber Futures Contract, in September 2006. Moving forward, it will be launching a US dollar-denominated Crude Palm Oil (CPO) futures contract.

Given Singapore's strategic location, in addition to a sizeable Muslim population, Singapore can certainly leverage on its advantageous position to develop itself as the Asian gateway for Islamic products and services.

Today, the present size of the global Islamic financial industry is estimated to be in excess of US$500 billion. This number is expected to increase further as the depth and sophistication of these instruments develop. As it is a major finance center, Singapore and the SGX have been at the cutting edge of the finance industry. As such, it offers an attractive value proposition for Islamic finance, be it in Sukuk or equities, for development, trading and listing.

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Islamic Finance in the US

By Stephanie Mumford Brown and Douglas Clark Johnson

Islam in the US dates back to the 18th century, and the first US mosque to the early 20th century. In more recent decades the US Muslim population has achieved sufficient size to have a discernable impact on American culture, economics and politics. The events of 9/11 further raised the media profile of Islam's American adherents, with considerable print and airtime devoted to news and feature stories exploring their lives.

Today, Muslims in the US evidence a diversity that mimics in miniature both the population of the nation as a whole, and the breadth of Islamic populations worldwide. The nation's roughly 6–7 million Muslims represent a spectrum of ethnicities, professions and socioeconomics – from Pakistani physicians to Bosnian entrepreneurs to African–American legislators (such as the first Muslim congressman, Rep. Keith Ellison of Minnesota). They are immigrants, second-generation Americans and converts.

Islamic finance, banking and investing in the US present a similarly diverse story. Here the range extends from boutique banks helping homebuyers to giant financial houses issuing Sukuk. Thus far the history is relatively short and the activity fairly sparse. But we expect this to change rapidly as US institutions both catch the global wave of Islamic finance growth and begin to appreciate the niche market at home.

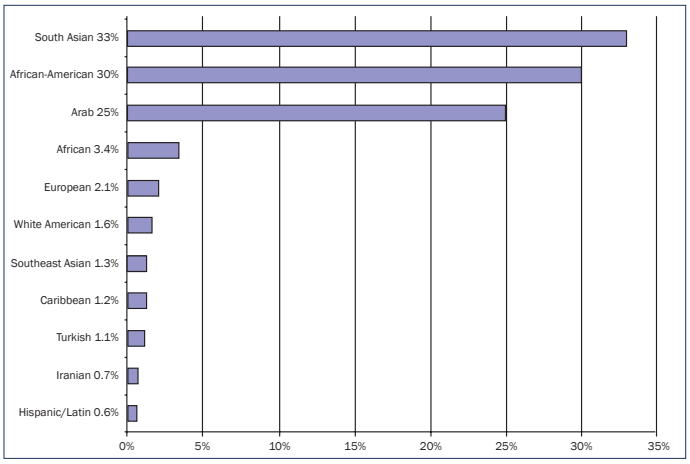
Our discussion here views Islamic finance activity in the US through three lenses: the US as product market, the US as product source, and the US as an investment target.

The US market for Islamic financial products

US Muslims represents a small proportion of the national population, but one that is said to be growing rapidly. Since US law forbids census questions about religion a definitive assessment of the number of Muslims is hard to come by. Indeed, there is some controversy here, involving post-9/11 accusations of political influence in both directions. Our analysis suggests estimates as high as 7 million hold validity.

More reliable is the accounting of US Muslim diversity (figure 1). South Asians make up a third of Islamic Americans, with a broad range of other ethnicities represented. The high proportion of Muslim immigrants who have become US citizens – estimated at 70–80% – speaks to their integration in American society.

Figure 1: Ethnic division among Islamic Americans

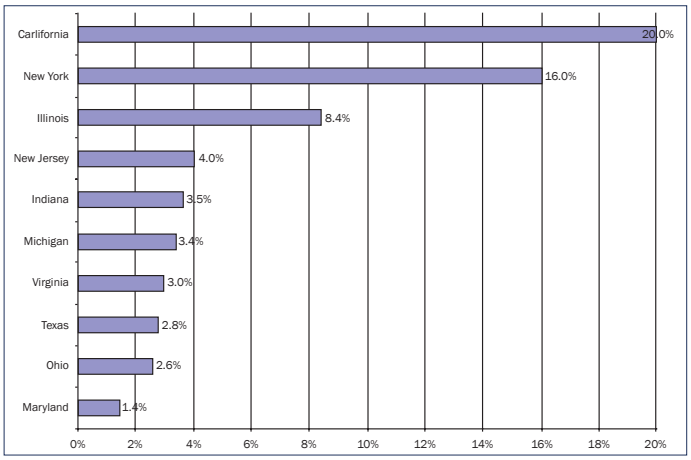


Source: Study of American Mosque Attendance, Hartford Institute for Religion Research, June 2003.

The demographic fact most relevant to the financial services sector is the relative affluence of US Muslims. Examinations of Islamic American earning power indicate average household income higher than the national average, by as much as 25% in one study.

At about 2% of the US population, Muslims constitute a niche market. Nevertheless, their concentration in a handful of geographies makes them relatively efficient to serve, insofar as banking retains a bricks-and-mortar component. Half a dozen states host more than half of the Islamic American population: California (20%), New York (16%), Illinois (8%), New Jersey (4%), and Indiana and Michigan (both about 3.5%) (see figure 2). Further studies indicate these US Muslims overwhelmingly cluster in cities.

Figure 2: Islamic American population by state of residence



Source: American Moslem Council, 2003.

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Islamic Finance in the US *(continued...)*

A handful of companies currently provide individual customers with Islamic depository and credit products. Among them is Devon Bank, a community bank founded in 1945 and headquartered in an ethnically diverse Chicago neighborhood. Devon Bank has earned international recognition for its broad Shariah compliant product set. University Bank in Ann Arbor, Michigan, has established University Islamic Financial Corporation. American Finance House LARIBA of Pasadena, California, and Guidance Financial Group, headquartered outside Washington, specialize in home financing contracts. Most of these institutions operate in multiple states, even nationally, via branch offices and web sites. Among the global institutions serving the US market, HSBC and Citigroup have Islamic capabilities.

"The young but burgeoning Sukuk market saw its first US issuer in 2006, when East Cameron Partners issued an Islamic bond based on its offshore Louisiana gas reserves"

From a US financial perspective, Islamic asset management slots within the field of "ethical investing." Saturna Capital's Amana funds have occupied the US Islamic investing space since 1989, virtually alone for much of the period. We are aware of two other investment firms now catering to Islamic American investors: Allied Asset Advisors and Azzad Asset Management.

Based in Washington state, Saturna created its two Islamic funds as an alternative to Islamic investment clubs. The firm's experience suggests the potential for Shariah compliant products to compete with conventional funds in terms of performance and attracted capital. Indeed, the firm's long-term performance has earned it attention from the US business media, including a recent profile in SmartMoney magazine. Saturna management now aims to expand assets under management aggressively, and recently opened an office in the Washington DC area to serve the east coast.

US regulation of Islamic finance

From a regulatory standpoint, Islamic finance does not require explicit federal governmental permission in order to operate. Fundamentally speaking, US law permits all commercial activities that are not specifically prohibited.

Nevertheless, the entities providing Islamic financial products in the US are subject to oversight by the same network of state and federal regulatory bodies as conventional financial institutions. This has not been much of an issue, since both the economic underpinnings and the consumer protection spirit of Islamic finance seem fairly harmonious with the perspective of US regulators. Thus far Islamic retail product structures have been subject to a handful of case-by-case rulings by the US Treasury Department's Office of the Comptroller of the Currency, all of them positive to date.

Figure 3: Estimated US Islamic assets under management

Manager	Funds	Assets (millions)	2006 price return
Saturna Capital	Amana Trust Growth (AMAGX)	US$329	15.4%
	Amana Trust Income (AMANX)	US$111	21.2%
Allied Asset Advisors	The Dow Jones Islamic Fund, Class K (IMANX)	US$32	12.5%
Azzad Asset Management	Azzad Ethical Mid Cap Fund (ADJEX)	US$4	3.1%
	Azzad Ethical Income Fund (AEIFX)	US$3	4.5%

Data as at the 31st December 2006. Comparative 2006 price returns are S&P 500, 13.6%; Dow Jones Islamic Market World Index, 14.5%.

Source: Saturna Capital, Morningstar.

Several of the 12 regional Federal Reserve Banks have made an effort to promote understanding of Islamic finance tenets and practices through conferences and publications. Thomas C. Baxter Jr., executive vice-president and general counsel of the Federal Reserve Bank of New York, summarized the Fed's regulatory perspective at a March 2005 seminar, "Legal Issues in the Islamic Financial Service Industry":

> "A corollary of the principle of religious freedom enshrined in our constitution is that the secular law should adapt, as much as possible, to accommodate differing religious practices ... As financial regulators, we operate within a statutory framework created by others, namely the United States Congress and the various state legislatures. Yet within that framework we enjoy a considerable degree of freedom to see that our enforcement of those laws (and the regulations we promulgate under them) does not interfere duly with the religious practices of our body politic, including Muslims."

The US as a global provider of Islamic financial products

To transition from the US as product consumer to source, let us review US-based Shariah compliant asset management as a discipline serving global investors. Here, too, the industry is at an early stage but accelerating.

continued...

Islamic Finance in the US *(continued...)*

Two young ventures, Calyx Financial and Shariah Capital, are building bridges between Wall Street investment experience and Islamic needs, albeit through different structures. Based in New York City, Calyx Financial specializes in developing Shariah compliant investment funds for distribution outside the US. The firm is set to launch its first product, a fund of Shariah compliant funds, in early 2007 through a series of banks and investment advisors primarily in the Middle East and South-East Asia.

"Ignoring the world's largest equity market eliminates half of all global investment opportunities"

Shariah Capital, headquartered in Connecticut, offers services to connect western companies with Islamic capital. The new firm listed on the Alternative Investment Market (AIM) exchange in London in late 2006. In an earlier venture, Shariah Capital CEO Eric Meyer focused on setting up a screening process to enable hedge fund managers to transform their strategies into Shariah acceptable vehicles. The current firm expands its purview to Islamic real estate, private equity and Sukuk products, as well as Shariah advisory services.

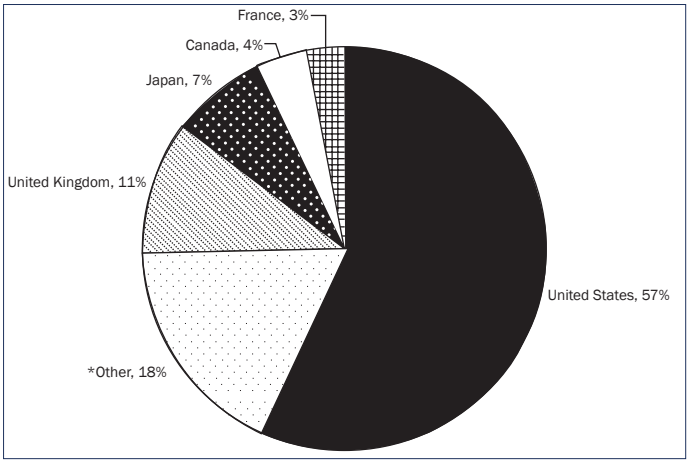
Shariah compliant corporate and investment banking is becoming a two-way street. Bahrain-based Unicorn Investment Bank and Arcapita Bank have US offices for deal sourcing. In turn, the global financial behemoths based in the US are opening Islamic "windows" in the Middle East and Asia for both retail and corporate customers. The young but burgeoning Sukuk market saw its first US issuer in 2006, when a Texas oil and gas exploration firm called East Cameron Partners issued an Islamic bond based on its offshore Louisiana gas reserves, raising US$116 million with the help of Merrill Lynch's London office and Bemo Securitization in Beirut.

Citigroup is a relatively long-time Islamic financial force, with Bahrain-based Citi Islamic dating back to 1996, joined more recently by a Kuala Lumpur operation. Morgan Stanley announced in August 2006 it would double the size of its Dubai office to enable involvement in Islamic finance. Insurance giant American International Group established AIG Takaful in Bahrain in October 2006. Other US-based global Goliaths are reportedly studying how to engage with Islamic markets.

US as an Islamic investment target

While the US is by no means an Islamic nation, as a target for Islamic investment commitment it offers a plethora of Shariah compliant opportunities. The US accounts for almost half of world equity market by capitalization, and an even higher proportion of the Dow Jones Islamic Market World Index (see figure 4). Indeed, relatively few nations with dominant Muslim populations have equity markets represented among the Dow Jones Islamic Market indices: Kuwait, Malaysia, Pakistan and Turkey. Impediments to Shariah compliance generally reflect market immaturity: barriers to foreign investment, lack of transparency in equity reporting and other such issues.

Figure 4: Regional breakdown of Dow Jones Islamic Market World Index



*Data as of April 28, 2006. *Other Include 34 countries with weight less than 3%.*
Source: Dow Jones, Calyx Financial.

"The high proportion of Muslim immigrants who have become US citizens – estimated at 70–80% – speaks to their integration in American society"

We recognize that some Islamic investors may avoid the US capital market as a matter of personal preference. But – capital controls aside – the idea that Middle Eastern or South-East Asian investors can assemble a well-allocated portfolio while avoiding the US capital market in general, and US equities in particular, is tenuous for several reasons:

- **Size**: ignoring the world's largest equity market eliminates half of all global investment opportunities.
- **Quality**: we further question the logic of trying to isolate US stocks from a portfolio, because relatively few large-capitalization companies operate strictly within US national borders. From IBM to Starbucks, these are global organizations whose stocks happen to trade primarily on US public markets.
- **Disclosure**: national standards for corporate transparency and reporting frequency align with the needs of Shariah compliance review.

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Islamic Finance in the US *(continued...)*

Further, we expect that more and more Shariah compliant offerings, beyond traditional equity investments, will rise out of the US. By any one of several objective measures, it is the world's most dynamic capital market. These may be enhancements on existing trade finance, real estate or Sukuk structures. Or they may be developments that we cannot even begin to appreciate today.

Concluding observations

The first North American conference on Islamic finance takes place in Toronto in May 2007. A glance at the sponsor list suggests that the industry is achieving critical mass in this continent. Despite perceptions that the US offers a hostile environment for Islamic finance, the reality is that this discipline fits comfortably within the pluralistic, non-discriminatory traditions that exemplify the best of American society.

The US is not only receptive to Islamic finance, but is actively engaged in it. Important trends are percolating there, supported by factors ranging from the small but economically significant Muslim population, to a sympathetic regulatory environment.

Accordingly, we conclude:

- There is a viable niche market for Islamic financial products in the US.
- Given the size of the local market, financial institutions have done a credible job of serving it thus far, thereby further stimulating its potential.
- Although not part of the Islamic world, the US continues to be highly relevant to investors there, whether they are adhering to Shariah principles or not.

CALYX FINANCIAL

Stephanie Mumford Brown and Douglas Clark Johnson are managing director and chief executive officer, respectively, of Calyx Financial, a New York-based firm that specializes in Islamic asset management for a global clientele. The authors acknowledge the essential research aid of Rasha Al-Aswad and Kirk B. Smith.

Please note that this article is merely a sketch, far from the definitive portrait. But we hope have conveyed the impression of a US Islamic finance industry that is prospering and globally engaged.

THE RESULTS ARE NOW OUT

2006 was a year of record mergers and acquisitions (M&A) in all markets. And, what kicked it off? The Ports, Customs & Free Zone Corporation (PCFC) Sukuk (Dubai Ports World) - the funding issue for DP World to acquire The Peninsular and Oriental Steam Navigation Company (P&O)'s international ports contracts. No better way to highlight the growing sophistication and capacity of Islamic finance and the institutions offering it. But the PCFC Sukuk was not the only ground-breaking high profile Sukuk issuance in 2006. As a result, the entire Deals of the Year selection process was tremendously difficult, as too many deals were closely matched in quality, skill, innovation, and market expansion.

The PCFC Sukuk has been selected as the world's Islamic Finance Deal of the Year in an exciting competition. The sub-categories were as competitive as the Deal of the Year. Typically, quantity and quality are not companions, but the 2006 competition is one in which quantity and quality was matched. And, 2006 opened a variety of new markets, expanded forms of innovation and accelerated co-operation between the Gulf Cooperation Council (GCC) and Malaysia on multiple fronts. What does it all mean? Well, 2007 should produce an even more complicated, voluminous, exciting and excellent competition.

Deal of the Year:	**Ports, Customs & Free Zone Corporation (PCFC) (DP World)**
Size:	US$3.5 billion Sukuk
Arrangers:	Barclays Capital and Dubai Islamic Bank
Lawyers:	Clifford Chance and Denton Wilde Sapte
Rating:	Unrated
Date Closed:	23rd January
Shariah Advisors:	Dubai Islamic Bank

The PCFC Sukuk was the world's first convertible Islamic bond; and it marked the first significant participation of Islamic finance in the global M&A market. Part of the funding for the acquisition of P&O, the Sukuk contributed to elevating DP World to the world's 3rd largest ports operator. Innovative structural aspects included the ability for Sukuk holders to exchange their holdings for shares if DP World carries out an IPO within three years of the Sukuk issuance. As the tenor of the Sukuk is only two years, this required careful structuring, which involved the creation of a "look back" mechanism should DP World go to an IPO within the three-year period, but after the tenor of the Sukuk has expired. Important cross-border elements had to be addressed; including demonstrating to UK authorities that the acquirer of a UK listed company had certainty of funds. A Musharakah structure, the PCFC Sukuk tested a number of relationship elements that caused predictability of income to investors, a bonus mechanism for the DP World, and other complex creative features that helped the PCFC Sukuk serve DP World by drawing conventional and global investors into the Islamic structure. PCFC was an excellent example of cooperation between a leading Islamic bank and international bank showing that the Islamic market players are capable of providing cutting edge services in the complex and time focused global M&A market.

(Also the winner of: Deal of the Year in UAE)

Honorable Mention: The first exchangeable Sukuk: Rafflesia (Khazanah), the first Islamic REIT: Al-Aqar: a dynamic GCC-Malaysian deal: Dubai Financial: and significant tier two capital instruments for Abu Dhabi Islamic Bank and Sharjah Islamic Bank.

continued...

Deals of the Year Result *(continued...)*

Corporate Finance: Kuwait Finance House

Size: US$850 million

Lead Arrangers: BNP Paribas, Gulf International Bank, Calyon, HSBC Amanah, Citigroup, Standard Chartered Bank, Deutsche Bank, West LB

Lawyers: Clifford Chance and Denton Wilde Sapte

Rating: Unrated

Date Closed: March

Shariah Advisors: Kuwait Finance House

Traditionally, the market views Kuwait Finance House (KFH) as a key source of funds. But, in 2006 KFH accessed the syndication market for funding. In early 2006, KFH executed its debut "debt" market, which was one of the largest Islamic deals in Kuwait of the year. This transaction was selected due to its success in attracting a diverse universe of investors. The largest syndicated Murabahah as of its time for a Kuwaiti corporate, this transaction has opened the door to expanding the Kuwait market space, in terms of deal volume and international investor confidence.

Honorable Mention: The Emaar Sukuk issuance, the Dubai Financial funding for acquisition of BIMB, and the MTC syndicated Murabahah all gave close competition to KFH. Preference was given to KFH due the initial launch at a large volume.

Cross Border: Dubai Financial

Size: US$330 million Syndication Facility

Lead Arranger: Citigroup

Lawyer: Denton Wilde Sapte

Rating: Unrated

Date Closed: October

Shariah Advisors: Citi Islamic Investment Bank

This transaction cements the growing co-operation between the GCC and Malaysia, turning the talk about harmonization into a business reality and allowing for greater synergy in Islamic finance. The transaction was a complex blend of bridge funding for Dubai Investment Group's acquisition of 40% of BIMB, the founding Malaysian Islamic bank, and an important capital contribution to bank's capital base and its capacity to grow its domestic business as well as to expand cross-border. The transaction embedded a US dollar Malaysian ringgit Shariah compliant swap. Some cross-border deals were more complex by their components, but Dubai Financial earns precedence for its successful merging of GCC interests with the Malaysian market in a direct investment in an established institution. This investment required a GCC entity to buy into a Malaysian entity with distinct operating methods; and the Malaysian institution to adapt to the GCC style in a way that does not disturb the bank's effectiveness in the local market. But, despite similar home currency pegs to the dollar, the inbound investment was in US dollars and required a five year Shariah compliant hedge, given the next investment in local currency.

Honorable Mention: The Albaraka IPO and PCFC were strong contenders in this same category.

Innovative: Rafflesia Capital (Khazanah Nasional)

Size: US$750 million Exchangeable Sukuk

Joint Managers: CIMB Islamic, UBS and HSBC Amanah

Lawyers: Allen & Gledhill, Clifford Chance and Linklaters

Rating: Unrated

Date Closed: 27th September

Shariah Advisors: CIMB Islamic

In a year of widespread innovation, Khazanah Nasional's debut global Islamic bond wins over impressive competition. The deal represents the world's first Shariah compliant exchangeable bond based on the ownership concept of the underlying

continued...

Deals of the Year Result *(continued...)*

shares, whilst preserving a typical feature of an exchangeable bond. The transaction generated funds for Khazanah whilst creating an opportunity for investors to convert their bond units into shares of an underlying Khazanah controlled company – Telekom Malaysia. The deal creates unique business elements allowing investors to participate in a flagship company, and prospectively to convert into that company's shares, whilst having a direct obligation of Khazanah, yet preserving Khazanah's capacity to buyout the position of the investors. This was not only a highly creative transaction in its own right, but it was the largest exchangeable instrument issued in Asia in 2006. Given the diverse universe of government-linked entities in the Islamic world, this deal established a useful role model for both funding, and government-linked entity risk and portfolio management.

(Also the winner of: Sovereign Deal of the Year & Deal of the Year in Malaysia)

Honorable Mention: The PCFC Sukuk, Dubai Financial, and Abu Dhabi Investment House structured trade Mudarabah by Abu Dhabi Commercial Bank all represented significant and important innovations in the field.

Equity: Abu Dhabi Islamic Bank

Size: US$ 5 billion with US$800 million issued Sukuk program
Lead Manager: HSBC Amanah
Lawyers: Allen & Overy, Maples & Calder and Norton Rose
Rating: A2 Moody's and A Fitch
Date Closed: December
Shariah Advisors: HSBC Amanah and Abu Dhabi Islamic Bank

Traditional banks have long supplemented their tier one capital with tier two issuances via trust certificates. Recent experimentation with Musharakah forms has allowed the development of this Islamic equity model in a manner that is consistent with western-style trust certificate programs. The Abu Dhabi Islamic Bank Sukuk Program for US$5 billion of trust certificates issued the first US$800 million in December 2006. The second program launched by an Islamic financial institution, this program is the largest in scope and the first program to be listed on the London Stock Exchange with investment grade rated certificates. The deal has built-in flexibility to allow redrawing on a periodic basis over the life of the transaction up to the maximum volume of certificates authorized. The scope and structure of this issuance allows for a significant growth of the Islamic market by increasing the capital access of Islamic banks.

Honorable Mention: The Albaraka IPO and the Sharjah Islamic Bank trust certificates also were top drawer equity transactions.

Ijarah: Nakheel Development

Size: US$3.52 billion Sukuk Ijarah
Arrangers: Barclays Capital and Dubai Islamic Bank
Lawyers: Clifford Chance and Denton Wilde Sapte
Rating: Unrated
Date Closed: December
Shariah Advisors: Dubai Islamic Bank

Not only is Nakheel an excellent example of a structured Ijarah transaction, it is the largest ever Sukuk issuance to date. Proceeds are being used to fund Nakheel's landmark real estate projects throughout the UAE. But the Nakheel Sukuk builds on the PCFC Sukuk convertibility model. The Sukuk permits investors to have the option of taking part in any Nakheel IPO, acquiring shares at a preferential price, and allowing investors the option to hold onto the bond. This is an evolutionary step beyond the PCFC Sukuk model. The largest ever Sukuk issuance, and one of the ten largest convertible bond issuances ever globally, Nakheel demonstrates the relative attraction of GCC assets and GCC government-linked companies to global investors, including investment in the GCC real estate sector. The underlying leasehold estate structure gives investors a secure means of participating in Nakheel's core business whilst achieving a predictable, attractive current income.

(Also the winner of: Real Estate Deal of the Year)

Honorable Mention: Were the Nakheel Sukuk not so filled with unique features appended to the lease relationship, a classic aircraft lease deal like Etihad Airways would have stood out.

continued...

Deals of the Year Result *(continued...)*

I-REIT: Al-Aqar KPJ REIT

Size: RM179.25million (US$48.72 million)
Total Market Capital: RM333.2 million (US$90.57 million)
Managing Underwriter: AmImvestment Bank
Lawyer: Abdul Rahman Saad
Rating: Unrated
Issuance Date: July
Issuance Date: August
Shariah Advisors: Hadi Noohdin Gadot, Hj Md Hashim b. Hj Md Yahya, and Prof. Madya Dr. Ab. Halim Muhammad and complies with Securities Commission Islamic REIT standards

After a great deal of talk and many broken promises by bankers, KPJ Healthcare (KPJ) broke through and offered units in the first Islamic REIT. Playing on its existing market position as the largest private healthcare group in Malaysia, KPJ first covered many milestones: first Asian healthcare REIT, first listed Islamic REIT globally, first REIT launched and listed in Malaysia under the Securities Commission's guidelines for Islamic REITs. Generating cash for KPJ's expansion, the REIT allowed KPJ to maintain healthcare management roles as well as to retain its brand. The six properties acquired by the REIT will ddistribute up to 99% of income to investors for the financial years ending 2006 to 2009. KPJ REIT has a solid expansion plan as it is given a first right of refusal to acquire existing local or overseas hospitals managed by the KPJ Group with yield enhancing prospects. Low risk stable rental income streams proven by leading profitable hospital operators based on long-term lease agreements with the KPJ Group for 15 years with an option to renew for another 15 years. In the lease agreements, all the future maintenance costs will be borne by the KPJ Group. With the volume of parties owned by KPJ Group, the REIT may be expanded. This transaction sets a new benchmark and paves the way for future Islamic REITs. At the same time, the successful launch of an Islamic REIT model establishes a platform for regional, international growth for KPJ.

Mudarabah: KNM Capital

Size: RM300 million (US$81.20 million)
Lead Manager: Aseambankers and AmImvestment Bank
Lawyer: Zaid Ibrahim & Co.
Rating: MARC-1ID, A+ ID
Date Closed: October
Shariah Advisors: Aseambankers

KNM's transaction is the first of its kind where a combination of Murabahah and Mudharabah principles were used to facilitate an Islamic Commercial Papers/Medium Term Notes program. The ICP of up to RM150 million (US$40.56 million) issued under the ICP/MTN program are underwritten whilst the MTN are not. This seven-year deal was structured to allow a shelf structure whereby the subsequent tranches are issued without a new prospectus. The proceeds raised from the issuance of the ICP/MTN may be applied by KNMC, KNM's funding entity, to KNM and/or its other subsidiaries for the redemption of existing facilities, to make new industrial investments in China, to make new capital investments, and for general KNM working capital. This transaction applies a blend of the older Malaysian innovations and the latest developments from the Malaysian Islamic bond market.

Honorable Mention: Aabar was an excellent runner up serving for the corporate expansion of Aabar Petroleum in the ASEAN region.

continued...

Deals of the Year Result *(continued...)*

Musharakah: Qatar Real Estate Investment Company (QREIC)

Size: US$270 million Sukuk

Lead Manager: Qatar National Bank Al Islami, Dubai Islamic Bank, Gulf International Bank, and Standard Chartered Bank

Lawyers: Clifford Chance and Denton Wilde Sapte

Rating: Unrated

Date Closed: August

Shariah Advisors: Qatar National Bank Al Islami, Dubai Islamic Bank and Standard Chartered Bank.

The QREIC Sukuk was the first corporate Sukuk in Qatar and the first transaction to be issued by a special purpose vehicle (SPV) domiciled in the Qatar Financial Centre. Unlike the Qatar Global Sukuk, the QREIC issuance benefited from the drafting of specific regulations/exemptions (including a tax letter) to ensure that the SPV had a similar status to issuers located in other offshore jurisdictions. This creates a replicable role model for the Qatar market that meets international standards. In addition to using a procurement agreement to appoint QREIC to construct the project (which is a relatively new concept in Islamic finance), a second purchase undertaking was required in respect of the forward lease agreement, enabling the lessor to sell the leased assets to the lessee on a continuing event of default.. Whilst purchase undertakings in respect of the Musharakah are more common, the concept of a 'lease' purchase undertaking (and any second purchase undertaking) is novel development in this declining Musharakah transaction. The Musharakah is structured to fund in stages, reflecting the needs of the underlying obligor QREIC to fund according to its project needs. The first 10-year issuance in the GCC, the deal enjoys a high degree of security given the control of the properties by the Musharakah.

This issuance is a significant development in the opening of the Qatar market for domestic corporate issuances as well as signaling the formal opening of the Qatar Financial Centre for domestic and global Sukuk.

(Also the winner of: Deal of the Year in Qatar)

Honorable Mention: East Cameron Gas Company represents a very strong competitor, but covers other unique territory for which it is acknowledged below. .

Murabahah: Mobile Telecommunications Company International (MTC)

Size: US$1.2 billion Syndicated Murabahah Facility

Lead Arrangers: ABC Islamic Bank, Arab Bank, Calyon, Gulf International Bank, Kuwait Finance House and National Bank of Abu Dhabi

Lawyers: Clifford Chance and Norton Rose

Rating: Unrated

Date: December

Shariah Advisors: Kuwait Finance House

A traditional participant in the interest markets, Mobile Telecommunications Company (MTC) returned to the Islamic market for the second time. Two important reasons for this were MTC's discovery that Islamic providers can be efficient and deliver on pricing competitively to traditional banks. One of the largest Islamic facilities in the market, the deal was syndicated prior to financial close, demonstrating the attractiveness of the obligor, the Kuwait market, and the Islamic alternatives. The use of Murabahah to access funds from serial sales of commodities and their deferred purchase payment by the obligor is the tried and true method of Islamic finance. When well-executed, it is an excellent tool to draw world class companies like MTC to expand its tapping of the Islamic market space.

(Also the winner of: Deal of the Year in Kuwait)

Honorable Mention: Pertamina US$200 million Syndicated Murabahah.

continued...

Deals of the Year Result *(continued...)*

IPO: Albaraka Banking Group

Size: US$572 million
Lead Arranger: Gulf International Bank
Lawyers: Norton Rose and various domestic counsel in more than ten countries.
Rating: Unrated
Date: September
Shariah Advisors: Albaraka

Once of the founders of the modern Islamic banking movement, the Albaraka Banking Group (ABG) was traditionally a closely held entity with a broad mandate in many Islamic countries. The 2006 private placement of US$450 million and IPO of US$572 million represent both the first true opportunity for the broad Muslim public to participate in the success of this important market participant, and the first dual listing of shares on the Bahrain Stock Exchange and the Dubai International Financial Exchange.

(Also the winner of: Deal of the Year in Bahrain)

Project Finance: Al-Waha Petrochemical Project

Size: $1 billion wholly-Islamically financed project
Lead Arrangers: ABC Islamic Bank, Arab Banking Corporation, Bank Al Jazira, Banque Saudi Fransi, Gulf International Bank, Saudi Hollandi Bank and Saudi British Bank
Lawyers: Clifford Chance (Sponsors) and Norton Rose (Banks)
Rating: Unrated
Date: November
Shariah Advisors: HSBC Amanah

Al Waha, despite many very good entries, was well ahead of the pack. This is believed to be the first limited recourse greenfield project in Saudi Arabia to be financed without any interest bearing commercial bank debt, relying on funding from the shareholders and Saudi government agencies, as well as the Islamic facility. In itself, the Islamic structure is based on co-ownership of certain project assets. Traditionally, project finance structures have required a conventional loan tranche, and have never enjoyed a completely Shariab compliant fund and security package. Moreover, instead of applying Istisnah or a forward lease, a Musharakah method was used, which may recreate more deal flexibility over the long term.

Honorable Mention: Aabar was an excellent runner up serving for the corporate expansion of Aabar Petroleum in the ASEAN region.

Real Estate: Nakheel Development

Size: US$3.52 billion Sukuk Ijarah
Arrangers: Barclays Capital and Dubai Islamic Bank
Lawyers: Clifford Chance and Denton Wilde Sapte
Rating: Unrated
Date: December
Shariah Advisors: Dubai Islamic Bank

There were many entries for this category, but, the sheer scale of Nakheel demonstrates that investors voted with the dollars in the Nakheel company, its UAE real estate vision and its expansion plans. There is an old saying, "money talks, you know what walks." Nakheel is the best real estate deal.

(Also the winner of: Ijarah Deal of the Year)

continued...

Deals of the Year Result *(continued...)*

Sovereign: Rafflesia Capital (Khazanah Nasional)

Size: US$750 million Exchangeable Sukuk
Joint Managers: CIMB Islamic, UBS and HSBC Amanah
Lawyers: Allen & Gledhill, Clifford Chance and Linklaters
Rating: Unrated
Date Closed: 27th September
Shariah Advisors: CIMB Islamic

There were no true Sovereign issuances in the submissions for this competition, but there were many government-linked entries, including the various Dubai transactions and the Malaysian secondary market buyer of mortgages Cagamas. But Khazanah Nasional, with its unique structure and breadth of investor appeal into North Asia through the ASEAN region into the GCC and Europe makes this the strongest sovereign linked deal of the competition. The transaction is also a tribute to the leadership of the issuers' management team in defining creative alternatives to managing the capital structures and exit strategies of the constituent companies controlled by Khazanah.

(Also the winner of: Most Innovative Deal of the Year & Deal of the Year in Malaysia)

Structured Finance: East Cameron Gas Company (ECP)

Size: US$165.67
Lead Managers: BSEC S.A. and Merrill Lynch
Lawyers: Vinson & Elkins and Walkers
Rating: CCC+ Standard & Poor's
Date: July
Shariah Advisors: Sh. Nizam Yaquby and Sh. Yusuf DeLorenzo

This structured deal has everything: a formerly bankrupt obligor, a complicated capital structure to replace, a participation in oil and gas production and the first approval of a traditional hedge for gas prices. It is also the first significant US Sukuk to be issued globally, and to be heavily acquired in the US market. East Cameron is a tribute to the structuring skills of BSEC S.A. and its ability to partner with a global brand to produce a highly structured deal with attractive outcomes for the obligor and the investors.

(Also the winner of: Deal of the Year in US)

Sukuk: SABIC

Size: US$800 million Sukuk
Lead Managers: HSBC Amanah and SABB Amanah
Lawyers: Al-Jadaan, Clifford Chance and Torki Al-Shabaiki in association with Baker & McKenzie (local)
Rating: Unrated
Date: July
Shariah Advisors: SABB Amanah

This was the first ever Sukuk in Saudi Arabia, and has set the benchmark for subsequent Sukuk issuances. SABIC, despite many really good entries, stands out as the deal that opens Saudi Arabia, the largest GCC country. Prior to SABIC's Sukuk issuance, there were no public non-equity capital market issuances by any issuer other than the Central Bank Saudi Arabia Monetary Agency (SAMA). SABIC's decision to issue Sukuk instead of borrowing conventionally related to a desire to diversify financial sources, deepen the Saudi Arabian market and promote Islamic finance in the Kingdom. As the first tradable public issuance of Sukuk in Saudi Arabia, the SABIC deal has defined the challenges to forming an efficient market, as well for the opportunities of issuing Islamic securities for Saudi Arabian corporates.

(Also the winner of: Deal of the Year in Saudi Arabia)

continued...

Deals of the Year Result *(continued...)*

Trade Finance: Pertamina (Persero)

Size: US$200 million Murabahah Syndication
Lead Manager: HSBC Amanah
Lawyer: Clifford Chance
Rating: Unrated
Date: January
Shariah Advisors: HSBC Amanah

Pertamina (Persero), the state-owned oil company, is the first Indonesian company to tap the overseas Islamic finance investor base. Its second syndication attracted participation from several existing banks in the first syndication as well as new participants, representing both Islamic and conventional banks. Competitively priced, the financing for oil imports during a period of high oil prices eased the cash flow burdens of the buyer, and further reinforced interest from the offshore Islamic investor base in Indonesia.

(Also the winner of: Deal of the Year in Indonesia)

Country Deals:

Bahrain: Albaraka Banking Group

Size: US$572 million
Lead Arranger: Gulf International Bank
Lawyers: Norton Rose and various domestic counsel in more than ten countries.
Rating: Unrated
Date: September
Shariah Advisors: Albaraka

Bahrain is truly one of the most import centres for Islamic banking. The Albaraka Banking Group IPO stands out by increasing our opportunities to participate in this market through acquisition of listed shares.

(Also the winner of: IPO Deal of the Year)

Indonesia: Pertamina (Persero)

Size: US$200 million Murabahah Syndication
Lead Manager: HSBC Amanah
Lawyer: Clifford Chance
Rating: Unrated
Date: January
Shariah Advisors: HSBC Amanah

The Indonesian market is newly opening to Islamic finance. The credit worthy state oil company could easily borrow conventionally or issue traditional bonds. But, Pertamina lent credibility to the Islamic market and its tools by choosing to purchase oil by using syndicated Islamic sales transactions. In 2007, Indonesia expects to tap the global Sukuk market with a debut offering. Certainly, Pertamina helped the cause by demonstrating capabilities and efficiency of Islamic banking syndicates, and leading structurers of Islamic deals like HSBC Amanah.

(Also the winner of: Trade Finance Deal of the Year)

continued...

Deals of the Year Result *(continued...)*

Kuwait: Mobile Telecommunications Company International (MTC)

Size: US$1.2 billion Syndicated Murabahah Facility
Lead Arrangers: ABC Islamic Bank, Arab Bank, Calyon, Gulf International Bank, Kuwait Finance House and National Bank of Abu Dhabi
Lawyers: Clifford Chance and Norton Rose
Rating: Unrated
Date: December
Shariah Advisors: Kuwait Finance House

(Also the winner of: Murabahah Deal of the Year)

Malaysia: Rafflesia Capital (Khazanah Nasional)

Size: US$750 million Exchangeable Sukuk
Joint Managers: CIMB Islamic, UBS and HSBC Amanah
Lawyers: Allen & Gledhill, Clifford Chance and Linklaters
Rating: Unrated
Date Closed: 27th September
Shariah Advisors: CIMB Islamic

The maturity of the Malaysian market means that the depth and variety of deals truly makes it a difficult one in which to determine the best and brightest deal in 2006. Rafflesia and Al Aqar stood out above the rest. But, Al Aqar is a fulfillment of the long awaited promise of an Islamic REIT, and a top deal at that. After close consideration, Khazanah's innovation, exchangeable feature, and wide distribution propel it to the top spot.

(Also the winner of: Most Innovative Deal of the Year & Sovereign Deal of the Year)

Oman: Sohar Aluminum

Size: US$260 million Islamic Tranche of US$1 billion project financing
Lead Manager: Citigroup
Lawyer: White & Case
Date: November
Rating: Unrated
Shariah Advisors: Citi Islamic Investment Bank

Sohar is the first Omani obligor to take the Islamic market in a significant way. Oman has long been considered to be the most difficult market for Islamic financial institutions to penetrate. This high profile deal in the local market led by Citibank should provide clear evidence of the benefits of Islamic finance to local corporates.

continued...

Deals of the Year Result *(continued...)*

Pakistan: Sitara Chemical Industries

Size: PKR1.1 billion (US$16.63 million) Sukuk
Lead Manager: Standard Chartered Bank
Lawyer: Mohsin Tayebaly & Co.
Date: June
Rating: Unrated
Shariah Advisors: Standard Chartered Bank

This is the first local currency Sukuk issued by a local corporate in Pakistan and the first Sukuk issue for Standard Chartered in the Pakistan market. This privately placed Sukuk issue is structured on the basis of co-ownership of assets ("Shirkat-ul-milk"), whereby Sitara Chemical Industries (SCI) and the Sukuk holders will jointly own the fixed assets relating to SCI's caustic soda plant. SCI will be appointed as managing co-owner on behalf of the Musharakah, pursuant to the management agreement. Further, SCI will use the Sukuk holders' portion of the Musharakah assets in return for periodic rental payments linked to a known benchmark and agreed threshold level of production, as per the payment agreement.

Honorable Mention: Tuwairqi, WAPDA

Qatar: Qatar Real Estate Investment Company (QREIC)

Size: US$270 million Sukuk
Lead Managers: Qatar National Bank Al Islami, Dubai Islamic Bank, Gulf International Bank, and Standard Chartered Bank
Lawyers: Clifford Chance and Denton Wilde Sapte
Rating: Unrated
Date: August
Shariah Advisors: Qatar National Bank Al Islami, Dubai Islamic Bank and Standard Chartered Bank.

The Qatar Real Estate Investment Company (QREIC) Sukuk represents the debut of both the corporate sector in Qatar and the Qatar Financial Centre. These developments are welcome and the market looks forward to progressive expansion of these two developments as the Qatari corporate and hydrocarbon markets expand, and enjoy cross border investment from multi-nationals and GCC business partners.

(Also the winner of: Musharakah Deal of the Year)

Saudi Arabia: SABIC

Size: US$800 million Sukuk
Lead Managers: HSBC Amanah and SABB Amanah
Lawyers: Clifford Chance, Torki Al-Shabaiki in association with Baker & McKenzie (local) and Al-Jadaan Law Firm
Rating: Unrated
Date: July
Shariah Advisors: SABB Amanah

This was a particularly tough decision given the important project finance deals executed in Saudi Arabia, and the innovation achieved with Al Waha. However, the significant contribution represented in generating the first domestic traded Sukuk, causes SABIC to seize the honor. The SABIC Sukuk demonstrated how the new Capital Markets Authority regulations may be used for the structuring and issuance of Islamic instruments. It also highlights the strong domestic demand for Islamic income oriented instruments. SABIC has paved the way for Sukuk and other publicly issued asset oriented securities to become mainstream tools of corporate finance in Saudi Arabia. Such a development bodes well for the expansion of the domestic economy.

(Also winner of: Sukuk Deal of the Year)

continued...

Deals of the Year Result *(continued...)*

South Africa: Absa

Size: Rand 100 million (US$13.9 million) Murabahah Equity
Lead Managers: Absa Capital and Absa Islamic Banking
Date: December
Rating: Unrated
Shariah Advisors: Moulana Shoayb Joosub

Absa Islamic Banking, in partnership with Absa Capital, has signed a R100m (US$13.9 million) Murabahah Equity conduit deposit with a new business banking customer to the Absa Group. This is one of the largest Shariah compliant business banking investments in the business banking market in South Africa to date. The transaction allowed a client to make a unique Islamic deposit and achieve a successful placement of funds on a short term basis.

Turkey: Garanti Leasing

Size: US$41.5 million Syndicated Murabahah
Lead Manager: Citigroup
Lawyer: Norton Rose
Date: September
Rating: Unrated
Shariah Advisors: Citi Islamic Investment Bank

Turkey has long been viewed as an important market for Islamic finance and many important Islamic investors have long standing projects in the Turkish market. But, convincing leading Turkish finance houses and corporates to seek finance structured on Islamic principals has been challenging. Citibank's arrangement of a corporate financing based on Murabahah for Garanti Leasing is a significant success in this line. Garanti is one of the country's most important financial groups, and their agreement to tap the Islamic market is hoped to be a stepping stone for more widespread Islamic corporate finance in Turkey.

UAE: Ports, Customs & Free Zone Corporation (PCFC) (DP World)

Size: US$3.5 billion Sukuk
Arrangers: Barclays Capital and Dubai Islamic Bank
Lawyers: Clifford Chance and Denton Wilde Sapte
Rating: Unrated
Date Closed: 23rd January
Shariah Advisors: Dubai Islamic Bank

The UAE with its growing issuances of government linked entities provides one of the most challenging markets in which to make a decision. But, the creative structuring of the Ports, Customs & Free Zone Corporation (PCFC) Sukuk and fitting this deal into the modern global M&A framework has to give PCFC Sukuk the lead. With Abu Dhabi and Sharjah based entities joining the fray, one can imagine that the 2007 UAE deal of the year will be even more difficult to select!

(Also the winner of: Deal of the Year)

continued...

Deals of the Year Result *(continued...)*

USA:	**East Cameron Gas Company (ECP)**
Size:	US$165.67
Lead Managers:	BSEC S.A. and Merrill Lynch
Lawyers:	Vinson & Elkins and Walkers
Rating:	CCC+ Standard & Poor's
Date:	July
Shariah Advisors:	Sh. Nizam Yaquby and Sh. Yusuf DeLorenzo

BEMO Securitization, without any branches, was able to rely upon business relationships to originate a niche US market transaction. It then co-operated with Merrill Lynch to refine the structure and achieve a global distribution for the complex transaction. Not only was the transaction a landmark for the service rendered to a niche US corporate, but for its successful distribution to US investors. The East Cameron Gas Company (ECP) deal demonstrates that the US regulatory framework works for the issuance of Sukuk, domestically and cross border: A fact that should open the way for more Sukuk from both traditional American companies as well as the nascent Islamic banking industry in the US.

(Also the winner of: Structured Finance Deal of the Year)

THE RESULTS ARE NOW OUT

Dubai Islamic Bank has been voted the world's Best Islamic Bank for the second consecutive year in the 2006 Islamic Finance *news* Best Islamic Banks Poll.

Kuwait Finance House came second and CIMB Islamic third in this very closely contested category.

Many key players retained their number one status from last year's inaugural poll, including Bahrain Islamic Bank, Bank Muamalat Indonesia, Jordan Islamic Bank, Kuwait Finance House, Al Rajhi Bank (Saudi Arabia) and the US-based Lariba.

The Islamic Bank of Britain was voted the Best Islamic Bank in Europe for the second year running with the European Islamic Investment Bank, also based in the UK, in second place.

In the highly competitive technology sector, Path Solutions beat rivals Microlink in the Best Islamic Finance, Technology Provider category.

In newly created categories Ernst & Young claimed the Best Islamic Finance Advisory Firm mantle and Norton Rose took the Best Law Firm in Islamic Finance accolade.

Bank Negara Malaysia was again comprehensively voted as the Best Central Bank in Islamic Finance, claiming more than half the registered votes in that category. The Central Bank of Bahrain took the runners up spot.

In the sole individual category, and rounding off an exceptional year for the bank, Kuwait Finance House Malaysia's executive director, Salman Younis, was voted Best Individual in Islamic Finance.

Best Islamic Bank

1st	2nd	3rd
Dubai Islamic Bank – 21%	Kuwait Finance House – 19%	CIMB Islamic – 12%

Category	1st	2nd
Best Islamic Bank – Africa	Albaraka Bank – 32%	Faisal Islamic Bank – 21%
Best Islamic Bank – Bahrain	Bahrain Islamic Bank – 25%	Arcapita – 16%
Best Islamic Bank – Brunei	Bank Islam Brunei Darussalam – 73%	TAIB – 13%
Best Islamic Bank – Egypt	Faisal Islamic Bank – 56%	Egyptian Saudi Finance Bank – 19%
Best Islamic Bank – India	Kotak Mahindra – 37%	Al-Barr Finance House – 25%
Best Islamic Bank – Indonesia	Bank Muamalat Indonesia – 48%	Bank Syariah Mandiri – 26%
Best Islamic Bank – Iran	Bank Saderat Iran – 44%	Bank Melli – 22%
Best Islamic Bank – Jordan	Jordan Islamic Bank – 53%	Islamic International Arab Bank – 35%
Best Islamic Bank – Kuwait	Kuwait Finance House – 76%	Boubyan Bank – 13%
Best Islamic Bank – Malaysia	Kuwait Finance House Malaysia – 29%	CIMB Islamic – 23%

continued...

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□ **Sukuk & Islamic Capital Markets: Products & Documentation** 11th – 14th March, Dubai	□ **Structuring Islamic Financial Products** 9th – 12th July, Zurich
□ **Sukuk & Islamic Capital Markets** 2nd – 4th April, Singapore	□ **Legal & Documentary Issues in Islamic Financial Products** 16th – 18th July, Kuala Lumpur
□ **Structuring Islamic Derivatives** 5th April, Singapore	□ **Structuring Islamic Financial Products** 20th – 23rd August, Johannesburg
□ **Structuring Islamic Financial Products** 8th – 11th April, Dubai	□ **Undertaking Effective Shariah Control for Islamic Banking** 27th – 29th August, Kuala Lumpur
□ **Islamic Treasury Simulation** 7th – 8th April, Kuala Lumpur	□ **Legal & Documentary Issues in Islamic Financial Products** 2nd – 4th September, Dubai
□ **Risk Management in Islamic Banking & Finance** 7th – 10th May, Kuala Lumpur	□ **Managing the Shariah Advisory Process** 21st – 23rd October, Bahrain
□ **Islamic Treasury Simulation** 13th – 15th May, Dubai	□ **Managing Islamic Funds** 21st – 22nd October, Dubai
□ **Structured Islamic Real Estate Finance & Investment** 28th – 30th May, Kuala Lumpur	□ **Sukuk & Islamic Project Finance** 26th – 29th November, Kuala Lumpur
□ **Islamic Financial Engineering and Advanced Products** 11th – 14th June, Kuala Lumpur	□ **Islamic Financial Engineering and Advanced Products** 9th – 12th December, Dubai
□ **Essentials of Islamic Finance & Banking** 25th – 18th June, Hong Kong	□ **Legal & Documentary Issues in Islamic Financial Products** 10th – 12th December, Bahrain

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Islamic Finance news Awards Best Islamic Banks Poll 2006

RESULTS *(continued...)*

Islamic Finance news Awards Best Islamic Banks Poll 2006

Category	1st	2nd
Best Islamic Bank – Oman	Bank Muscat – 57%	National Bank of Oman – 29%
Best Islamic Bank – Pakistan	Meezan Bank – 45%	Dubai Islamic Bank (Pakistan) – 21%
Best Islamic Bank – Qatar	Qatar Islamic Bank – 58%	Qatar International Islamic Bank – 19%
Best Islamic Bank – Saudi Arabia	Al Rajhi Bank – 75%	National Commercial Bank – 10%
Best Islamic Bank – Turkey	Albaraka Turkish Finance House – 38%	Kuveyt Turk – 23%
Best Islamic Bank – Europe	Islamic Bank of Britain – 47%	European Islamic Investment Bank – 30%
Best Islamic Bank – UAE	Dubai Islamic Bank – 65%	Abu Dhabi Islamic Bank – 11%
Best Islamic Bank – USA	Lariba – 36%	University Bank – 21%
Best Islamic Retail Bank	Al Rajhi Bank – 17%	Dubai Islamic Bank – 16%

Most Innovative Islamic Bank	Dubai Islamic Bank – 16%	Kuwait Finance House Malaysia – 15%
Best New Islamic Bank	Kuwait Finance House Malaysia – 20%	Al Salam Bank – 12%
Best Central Bank in Islamic Finance	Bank Negara Malaysia – 52%	Central Bank of Bahrain – 25%
Best Individual in Islamic Finance	Salman Younis – Kuwait Finance House Malaysia	

Best Islamic Finance Advisory Firm	Ernst & Young – 27%	KPMG – 10%
Best Islamic Ratings Agency	Islamic International Rating Agency – 29%	Rating Agency Malaysia – 24%
Best Takaful Company	Solidarity – 18%	= Takaful Nasional – 16% = Takaful Malaysia – 16%
Best Islamic Asset Management Firm	National Commercial Bank – 19%	Oasis Asset Management – 14%
Best Islamic Wealth Management Firm	Citibank – 24%	UBS – 18%
Best Islamic Finance Technology Provider	Path Solutions – 47%	Microlink – 27%
Best Law Firm in Islamic Finance	Norton Rose – 27%	Clifford Chance – 18%

Methodology

A record total of 1,232 votes were cast in the 31 contested categories in the Islamic Finance *news* 2006 Best Islamic Banks Poll.

Of these, 143 were rejected owing to irregularities found during the due diligence process. Therefore a total of 1,089 votes counted towards the final results.

Islamic finance issuers, investors, non-banking financial intermediaries and Government bodies from around the world were invited to participate.

Voting took place during December and participants were requested to take only 2006 into consideration when casting their votes.

JANUARY news briefs

Deutsche Bank commenced trading of its four new indices on the DIFX. Cash Return on Capital Invested Islamic Global Certificates – Global Index; the CROCI Islamic US$ Certificates – Islamic Europe Index; CROCI Islamic US$ Certificates – Islamic US Index; and the CROCI Islamic US$ Certificates – Islamic Japan Index. The issue price was US$100 per certificate.

The **Singapore Exchange, FTSE Group** and **Yasaar Research** developed Shariah compliant indices under the FTSE-SGX Shariah Index Series. The stocks were screened against Yasaar Research's proprietary screening methodology for Shariah compliance.

Al Rayyan Bank opened its US$1.13 billion initial public offering on the 15th of January. **Qatar National Bank** was lead arranger and manager. A total of 413 million shares were offered to the public at QR10 (US$2.75) per share.

Emirates Islamic Bank gained approval to raise its capital from Dh500 million (US$140 million) to Dh650 million (US$177 million), through issuance of bonus shares representing 30% of capital. A share split from the shares' original value of Dh10 (US$2.72) to Dh1 (US$0.27) was also approved.

Qatar's banking sector saw an increase in competition with conventional and foreign banks increasing local presence. Qatar's two listed Islamic banks – **Qatar Islamic Bank** recorded 8.6% of the total US$30.6 million banking assets, and **Qatar International Islamic Bank** 6%.

Tameer Holding finalized a strategic agreement with **Emirates Islamic Bank** to facilitate mortgages and finance Tameer's property developments in the UAE.

CapitaLand established **CapitaLand Amanah**, a Shariah compliant unit to develop new real estate services in Asia. The company which offers advisory services for investments plans to bring US$500 million of Islamic compliant investments to investors within two years.

Doha Bank inaugurated its Shariah compliant bank **Doha Islamic** to meet ongoing demand from customers and shareholders.

Sistem Penyuraian Trafik KL Barat (Sprint) gained a US$53.06 million boost from its shareholders, with the initial US$26.53 million invested when the restructured Islamic bonds were issued. Sprint manages the Sprint highways in Kuala Lumpur and its shareholders are **Lingkaran Trans Kota Holdings** (50%), **Gamuda** (30%) and **Kumpulan Darul Ehsan** (20%).

Emirates Islamic Bank signed a memorandum of understanding with **Emaar** to offer Shariah compliant financing for Emaar properties.

Al Baraka Banking Group floated shares in Bahrain and throughout the region in order to boost its capital base by US$600 million to over US$1.2 billion.

Dolphin Energy's US$7 billion natural gas development project saw an increase in the percentage of gas production for the Gulf region. The project was part-funded by one of the largest Shariah compliant oil and gas financing transactions of 2006.

Affin Holdings applied for a license to operate an investment bank through merging **Affin Merchant Bank**, Malaysia's first merchant bank, and its stockbroking arm **Affin Securities**.

Saudi banks began planning for Islamic bond issuance. Talat Zaki Hafiz, assistant general manager of Islamic finance at **National Commercial Bank** commented, "Saudi banks were very late in taking this step. We have no Islamic finance or Sukuk, although most Saudi banks have Islamic units, and our country is home to the holy mosques."

The **Islamic Development Bank** provided funding in excess of US$47 billion for various infrastructure and development projects. The bank also issued US$666 million for the development of imports and exports.

Credit Suisse filed an application for a financial services license with the **Qatar Financial Centre** which would allow it to open a subsidiary in Doha.

Dubai Holding obtained a 70% stake in **Dubai Bank** from **Emaar Properties PJSC**, which retained a 30% ownership of the bank. The purchase occurred ahead of Dubai Bank's conversion from a conventional to an Islamic bank later in the year.

Istithmar signed a deal to buy **Inchcape Shipping Services** for US$285 million from **Electra Investment Trust**. The company was put up for auction in October 2005, with a US$200 million asking price.

The **Bahrain Monetary Agency** approved the establishment of a new Islamic investment bank with a paid up capital of US$100 million. The bank was established by prominent investors from Saudi Arabia, Bahrain, the UAE and Qatar.

The **Bahrain Monetary Agency**'s monthly issue of Sukuk Al Salam Islamic bonds was oversubscribed by more than three times, receiving subscriptions worth US$125.8 million for the initial US$40 million issue.

AmInvestment Group and **ARA Private** signed a memorandum of understanding to form a joint venture company managing real estate investment trusts to be listed on **Bursa Malaysia**. AmInvestment holding a 70% stake and ARA 30%.

BIMB Holdings posted a net loss of US$3.92 million in its first quarter ending on the 30th September 2005. Group revenue was up 35% from 2005 to US$76.02 million. GE

The **Islamic Financial Services Board** council approved two draft standards for Islamic financial services involving the "Guiding Principles of Risk Management Standards" and the "Capital Adequacy Standards". The standards will be issued and fully implemented by the end of 2007.

Gulf Finance House's board of directors recommended a 30% increase in bank capital through the issuance of new shares to registered shareholders.

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The **National Bank of Abu Dhabi** was the highest performing bank in the UAE for the first nine months of 2005, with a profit of US$550 million. **Dubai Islamic Bank** made a profit of US$398 million.

Adeem Investment Company, an Islamic investment and asset management company, lead managed, financed and arranged the purchase of a 45% stake in **Gulf Craft Inc.**

Kuwait Finance House's general manager, Abdulhakim Al Khayat, called for the University of Bahrain to open a course on Islamic banking.

Ann Arbor's University Bank, formed the first ever US Islamic banking subsidiary called **University Islamic Financial Corporation**, with a capital of US$15.5 million in shareholder equity and assets.

Barclays Bank of Kenya became the first bank to launch Islamic banking products in the country.

Iran was allocated a US$350 million facility for 2006 by the **Islamic Development Bank** to assist with financing implementation of Iran's industrial projects and ensure the financial and commercial resources needed by Tehran's trade sector.

32 **Lloyds TSB** branches across the UK rolled out Islamic current account and Islamic home finance services.

Mada'in Real Estate Company was established through a partnership of the **Gulf Investment House** with **Ahmed Ramadhan Juma Group**, with a paid-up capital of US$136.13 million.

Emirates Islamic Bank opened its consumer finance offices in Garhoud, expanding its retail banking initiatives.

Johor's investment arm, **Johor Corporation,** approved a corporate Wakaf fund, involving US$53.06 million worth of shares for a corporate endowment. It was the first fund of its kind to be introduced in the country.

Kuwait Finance House's Landmark One, Phase 2 real estate investment product in Kuala Lumpur was launched.

Dubai Bank implemented riskpro™, an integrated financial analysis infrastructure from **IRIS** ahead of its planned conversion to Islamic banking.

Tamweel opened its first branch in Sharjah.

Dubai Islamic Bank launched Al Islami Personal Finance to meet personal finance needs.

Lloyds TSB's International Private Banking moved its operations to the **Dubai International Financial Centre.**

Excelcomindo Pratama, Indonesia's third largest mobile phone company set an indicative yield of 7.5% for a proposed seven-year bond of up to US$250 million. **CIMB, JPMorgan** and **UBS** were joint bookrunners for the deal which was oversubscribed.

The Sukuk raised by **Dubai Ports, Customs & Free Zone Corporation** was increased from US$2.8 billion to US$3.5 billion due to overwhelming investor response. The oversubscribed three-year bond was lead managed by **Dubai Islamic Bank** and **Barclays Capital** and raised more than US$11.4 billion.

Bank Negara Malaysia tested the bid system for the issue of Islamic debt securities based on the Ijarah leasing arrangement.

Singapore's government-owned **PSA International** approached British firm **P&O** with an offer of US$6.18 billion, trumping the US$5.86 billion previously offered by Dubai's **DP World**.

CIMB and **Bumiputra-Commerce Holdings** completed a restructure involving a new **CIMB Group** management line-up. Nazir Razak was elected group CEO, along with 12 new appointments.

The **Islamic Shamil Bank of Bahrain** signed a US$100 million five year amortizing Murabahah syndicated facility, fully underwritten by **Gulf International Bank**. **Boubyan Bank** and **BNP Paribas** acted as mandated lead arrangers.

MNI Holdings was advised to reject **Maybank**'s takeover offer of US$1.07 per MNI share. Independent directors advised shareholders that the offer was not attractive on a price-to-book valuation.

The **Dubai International Financial Exchange**'s US$750 million Floating Rate Note was listed by the **National Bank of Dubai**. The note was the exchange's first debt security and first UAE issue.

Avenue Capital Resource completed a share sale agreement for the sale of a 60% stake in **Avenue Asset Management Services** to **Bank Muamalat**.

Abu Dhabi Islamic Bank posted a 180% growth in net profit – from US$33.46 million in 2004 to US$93.84 million in 2005.

Al Rayyan Bank launched the Gulf's biggest initial public offering in Qatar at US$1.13 billion, open to Qatari and GCC nationals.

Islamic and conventional Multi-Currency Trade Finance and Indirect Exporter Financing Scheme were made available to banks and small and medium enterprises. The participating banks included **Maybank**, **Bumiputra-Commerce**, **RHB Bank**, **Affin Bank**, **Alliance Bank Malaysia**, **AmBank**, **EON Bank**, **Hong Leong Bank**, **Public Bank**, **Southern Bank**, **Bank Islam Malaysia**, **Bank Muamalat Malaysia**, **RHB Islamic Bank**, **Commerce Tijari**, **Hong Leong Islamic Bank** and **SME Bank**.

Over 43% of **Dubai Islamic Bank**'s employees were made UAE nationals, due to the bank's high focus on Emiratization. This marked one of the highest rates amongst UAE banks with over 1,000 employees.

A **Standard & Poor's** report revealed that fixed income Islamic funds were the highest performers in a loss-making sector in 2005.

The **International Centre for Education in Islamic Finance (INCEIF)** was established to enhance Malaysia's position as a regional centre for Islamic finance and encourage growth in the industry worldwide.

** US$ rates were correct at the time the story was first published.*

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Saudi Arabian company **SIRAJ Capital** joined up with **Johor Corporation** of Malaysia to develop and launch US$500 million worth of Shariah compliant investment funds in the two countries.

The **Dubai International Financial Exchange** listed a Sukuk worth US$3.5 billion from Dubai Ports, Customs and Free Zone Corporation (PCFC). The Sukuk was lead managed by Dubai Islamic Bank and Barclays Capital.

The British port operator **P&O** accepted a £3.9 billion (US$6.93 billion) offer to be acquired by **Dubai Ports World**.

Sheikh Sir Dr Mohamed Aboulkhair Zaki Badawi, a prominent member of the **RHB Group**'s Shariah Committee passed away in London at the age of 83. Sir Dr Zaki Badawi founded the Muslim College in London and was a leading Imam and a progressive religious leader in the UK.

The **State Bank of Pakistan** revealed that banks have been recovering service charges for collecting and disbursing zakat, contrary to the Zakat and Ushur Ordinance Act 1980.

Kingdom Hotel Investments (KHI) launched an initial public offering to list shares on the **Dubai International Financial Exchange (DIFX)** and global depositary shares on the **London Stock Exchange**. The proceeds from the offering were used to finance the expansion of its portfolio of hotel investments through acquisitions and new developments. **Deutsche Bank** and **Morgan Stanley** acted as joint global coordinators and joint global bookrunners.

Saudi Arabian banker Sheikh Saleh Kamil revealed plans for a US$1 billion mega Islamic bank called the **Emaar International Group**.

The **Saudi British Bank** posted a net profit of SR2.5 billion (US$668 million) in 2005, an increase of 52.2% over 2004's SR1.65 billion (US$439 million). Earnings per share also increased to SR50.09 (US$13.36).

Brunei's Ministry of Finance announced the merger of **Islamic Bank of Brunei** with **Islamic Development Bank of Brunei**, creating the nation's largest domestic lender; the **Bank Islam Brunei Darussalam**.

Al Rajhi Investment & Banking Corporation structured and acted as underwriters for the US$210 million Islamic tranche of the US$2.5 billion Shuaibah Independent Water and Power Project, Saudi's first.

EON Bank's deputy chief executive Abdul Jamel Pawanteh revealed plans to launch EON's Islamic banking subsidiary in 2006.

Abu Dhabi Commercial Bank's net profit for 2005 soared to a record Dh1.91 billion (US$520 million), an increase of 139%. The bank's assets stood at Dh57.5 billion (US$15.65 billion) at the end of December 2005, against Dh38.3 billion (US$10.43 billion) in 2004.

Bank Negara Malaysia issued approval for **Dubai Investment Group** to start due diligence on its proposed strategic investment of up to 49% of **Bank Islam** Malaysia's enlarged issued and paid-up share capital. The due diligence was carried out by DIG's subsidiary, **Dubai Financial**.

Bahrain-based **Shamil Bank** launched the first ever Islamic property fund for investment in the Chinese real estate market – the US$100 million Shamil China Realty Mudarabah. The four-year Mudarabah will invest in the Xuan Huang China Realty Investment Fund, a joint venture between Shamil Bank and the state-owned Chinese conglomerate **CITIC Group**.

Qatar was inundated by GCC nationals eager to buy shares in **Al Rayyan Islamic bank**. The bank's initial public offering was open from the 15th to the 29th January to all GCC nationals.

Dubai Islamic Bank (DIB) signed a global agreement with **i-Flex** solutions to supply DIB's global banking operations with FLEXCUBE services; with a common banking platform used to consolidate its worldwide operations.

The **Bahrain Monetary Agency** listed US$230 million of six-year Islamic bonds, which were sold by the Central Bank. The bank paid a coupon of 5.6%, on the Bahrain Stock Exchange (BSE).

Kuwaiti Islamic firm **Manafa'e Investment Company** was slated to attract US$342.3 million in financial portfolios in its first year of operation.

Arab Banking Corporation announced a group net profit for 2005, totaling US$129 million, an 18% increase on the net profit from continuing operations of US$109 million in 2004. Total income amounted to US$352 million.

The **Public Bank Group** posted a record pre-tax profit of RM2.05 billion (US$546.23 million) for the year ending on the 31st December 2005, up 11% from RM1.85 billion (US$492.99 million) in 2004. The group's net interest income and net Islamic banking financing income grew by 7% to RM2.89 billion (US$770.13 million) in 2005, underpinned by strong loan growth and improvement in asset quality.

The **Dow Jones Islamic Market Sustainability** Index was launched by the Dow Jones Indexes and **SAM Group**. The index was the first to merge Islamic investing principles and sustainability criteria.

Bahrain Islamic Bank was chosen to be the exclusive mortgage financer for new property development **Riffa Views**.

Kuwait Financial Centre's flagship local investment funds, including a Shariah compliant fund, performed well, surpassing market benchmarks. Markaz's Islamic Fund returned an 80% yearly average since its inception in October 2003, as of year end 2005.

Dubai Islamic Bank announced that it is currently in the final stages of negotiation to buy MNG Bank of Turkey for US$160 million.

Amlak Finance raised its mortgage rates for existing clients to 7.5%, citing the international 2.25% increase in financing rates over the past 12 months as the reason behind the 0.25% rise.

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The **Dubai International Financial Centre Authority** and the **Dubai Financial Services Authority** released for consultation the Limited Partnership Law, DIFC Law No. 1 of 2006, and the accompanying Limited Partnership Regulations.

The **Financial Services Authority** granted the **European Islamic Investment Bank (EIIB)** authorization to open for business, making it the first Shariah compliant independent investment bank to be regulated by the FSA.

The National Investor became the first UAE-based investment bank to be authorized by the Dubai Financial Services Authority to operate from the **Dubai International Financial Centre**.

Shares in **CIMB** were suspended ahead of its complete delisting from Bursa Malaysia, as part of the bank's restructuring of **CIMB Bumiputra-Commerce Bank**.

Bank Negara Malaysia launched the first Bank Negara Malaysia Sukuk Ijarah with an issue size of RM400 million (US$107.54 million).

First Gulf Bank commissioned a team of experts to investigate potential overseas markets for the bank. The bank also opened an Islamic finance window under its Islamic banking division, in line with growing interest in the Islamic markets.

India's **Bank of Baroda** announced its plans to expand overseas, especially into the Gulf countries of Kuwait, Saudi Arabia, Bahrain and Qatar. The bank also expressed a possible induction of Islamic banking systems.

The **Securities Commission of Malaysia** approved **Prinsiptek**'s plan to issue Murabahah Commercial Papers and Medium-Term Notes with a nominal value of US$21.5 million to repay or refinance bank borrowings and as working capital.

SABB Bank signed the first Shariah compliant deal hedging lending rates with Fawaz Al Hokair & Co. to protect Al Hokair against the possible rise of lending rates.

Dubai Islamic Bank launched its first Islamic credit card with the support of Card Tech, a UK-based bank card systems provider and proces sor.

The **Dubai Financial Services Authority** granted a license to South Africa-based **Standard Bank** to operate within the Dubai International Finance Centre (DIFC).

Saudi Arabia's former **Al Rajhi Banking and Investment Corp** changed its name to **Al Rajhi**.

Kuwait Finance House Malaysia announced its plans to concentrate on its investment banking and fund management business.

Emirates Islamic Bank announced an increased return of 6.3% on a two-year term deposit in the final quarter of 2005, from 3.88% in the corresponding quarter previously.

Arcapita Bank's net income leapt 48% to US$104.3 million for the year ending on the 31st December 2005. The Bahrain-based bank said that performance in corporate investment, real estate investment and asset-based investment all remained strong, generating a total operating income of US$237 million, an increase of 38% on 2004.

Qatar National Bank and **Qatar Real Estate Investment Company** arranged a Sukuk issue and syndicated Islamic facility. QNB's subsidiary **QNB Al Islamic** acted as lead arranger.

The **Dubai International Financial Centre** granted a license to Zurich-based **EFG International**, the global private banking group.

Shamil Bank was named lead issue manager and financial advisor and **KPMG** is co-financial advisor for the initial public offer of the Bahrain-based **Ithmaar Bank**. The bank has also appointed **Global Investment House**, **Amwal**, **Abraaj Capital**, **BBK** and **Bahrain Pension Fund** as underwriters.

Boubyan Bank and **Ryada Capital** launched the **Ryada Islamic Private Equity Fund** to exploit investment opportunities in private companies in the GCC and MENA region.

Saudi Arabia's **National Commercial Bank** launched the Al Ahli Secured Saudi Trading Equity Fund "A." The minimum subscription was set at US$66,663 million.

The umbrella **FTSE-SGX Shariah Index Series** was launched in Singapore along with the inaugural FTSE-SGX Asia Shariah 100 Index. This followed the rival group's launch in Turkey in January of the **Dow Jones DJIM Turkey Exchange Traded Fund** in Istanbul, based on the Dow Jones Islamic Market Turkey Index.

Islamic loans worth US$400 million were secured from eight Saudi and foreign banks to finance the US$1 billion Jamrat Bridge expansion project in Mina, undertaken by the **Saudi Binladin Group**. **Bank Albilad**, **Al Khaleej Bank**, **Samba Financial Group**, **National Commercial Bank**, **Emirates Bank**, **Riyad Bank**, **Banque Saudi Fransi** and **Saudi Hollandi Bank** were involved.

** US$ rates were correct at the time the story was first published.*

MARCH news briefs

Singapore's Islamic finance industry was set in gear as the city state targeted large funds and foreign high net worth individuals.

Malaysia's largest corporate offering of Shariah compliant securities was sold by **Khazanah Nasional**. The state-run investment firm offered up RM10 billion (US$2.69 billion) of Islamic commercial papers and long-term bonds.

Standard Chartered Bank expressed hopes for 30% of the bank's new corporate deposits and 10% of new corporate financing to come from its Islamic alternative deposit and financing product – Commodity Murabahah Program-i.

NBK Capital, the investment and merchant banking subsidiary of **National Bank of Kuwait**, was bestowed a license by the **Dubai Financial Services Authority** as an authorized firm in the **Dubai International Financial Centre**.

The **Dubai International Financial Centre** inducted **Deutsche Bank**'s Dubai branch, after the bank officially launched its new office in the emirate.

Investment bank **EFG-Hermes UAE** became the first regional institution to join the **Dubai International Financial Exchange** as a broker.

RHB Capital's profit for the financial year, ended on the 31st December 2005, was boosted by income from its Islamic banking business, now led by **RHB Islamic Bank**. Income from Islamic banking amounted to RM147.7 million (US$39.85 million).

Jordan's **Investment House for Financial Services** finalized the first stage in establishing a JD50 million (US$70.02 million) Islamic financing company in the country.

Kuwait Finance House's net income for the year ending on the 31st December 2005 rose considerably by 46% to US$40.2 million (from US$28 million in 2004), representing a 27% return on average equity for 2005. Total assets increased by 47% to US$687 million.

Boustead Holdings posted a net profit rise of 60% to RM191 million (US$51.54 million) for the year ended on the 31st December 2005. Contributing to this result was the completion of Malaysia's largest Islamic plantation asset backed securitization transaction.

Kuwait's parliament approved the establishment of a new Islamic bank and fund in the name of late **Amir of Kuwait**, His Highness Sheikh Jaber Al-Ahmad Al-Jaber al Sabah.

Al Masref Bank was awarded a license by the Bahrain Monetary Agency. The bank's paid-up capital amounted to US$10 billion, with its authorized capital at US$20 billion.

Global index provider the **FTSE Group** signed an agreement to develop a range of Shariah compliant and conventional equity indices with the **Dubai International Financial Exchange.**

The **Dubai International Financial Centre** revealed intentions to become the accredited hub for managing the region's huge wealth – estimated at US$1.5 trillion – in the near future.

Qatar Islamic Bank was ranked among the top ten Islamic banks in the world. **Qatar Islamic Bank** was eighth among world Islamic banks in terms of deposits in 2003, ninth in terms of assets and tenth as regards shareholder number.

Sharjah Islamic Bank and **Kuwait Finance House** commenced talks to launch joint banking services, expand investment cooperation and build strategic relationships in Islamic banking sectors.

Al Salam Bank's initial public offering was 63 times over-subscribed. The largest in Bahrain's history, the Al Salam bank initial public offering offered 35% of its paid-up capital in the form of 42 million ordinary shares to investors. Public subscription collected over BD2.7 billion (US$7.16 million) from UAE and Bahrain citizens within a fortnight.

Emaar Properties appointed a Fatwa and Shariah Board to monitor the company's compliance with Islamic jurisprudence.

Jordan Islamic Bank launched an SMS banking service using the Fastlink network.

The Certified Islamic Professional Accountant qualification was launched in Bahrain by the **Accounting and Auditing Organization for Islamic Financial Institutions**; providing candidates with theoretical concepts and practical applications on a range of areas in Islamic finance.

Dana Gas announced that it will become a fully Shariah compliant company.

The **Shura Financial Committee** re-amended the Financial Trustees Bill, which was passed by the Chamber of Deputies, without the words "Islamic regulations" in the management of trusts' funds.

Gulf Finance House approved the Board's recommendations to increase the bank's capital through a rights issue and to pay a US$90 million record dividend to shareholders, following 2005's excellent results.

Abu Dhabi Investment House posted a net profit of Dh40 million (US$10.89 million) in its first quarter of operations, translating into a net profit of 20% of ADIH's Dh200 million (US$54.45 million) paid-up capital.

Kuwait Finance House became the first fully licensed foreign Islamic bank to operate in Malaysia.

Islamic commercial and investment bank **Shamil Bank** introduced a Shariah compliant financing facility for Bahraini individuals interested in subscribing to the 150 million shares of **Ithmar Bank**'s initial public offering.

The **Islamic Development Bank** expressed interest in providing finance for air operators in Nigeria to acquire new aircraft.

The **Islamic Development Bank** and Sierra Leone signed a loan accord worth US$10 million to finance a project to increase and diversify animal and botanical production, as well as to fight poverty

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MARCH news briefs *(continued...)*

in the rural regions of the country.

Islami Bank Bangladesh commenced its online banking at 37 selected branches nationwide.

Bank Islam Malaysia posted a net loss of RM35.54 million (US$9.6 million) in the first half of its 2006 financial year, compared to a net profit of RM19.21 million (US$5.2 million) in the corresponding period in 2005.

Sharjah Islamic Bank, as part of its effort to provide a premier service, opted to become **Datawatch** Middle East banking solution's pioneer customer.

Gulf Finance House and **Qatar Islamic Bank** signed an agreement to establish Qatar's first Islamic investment bank, with authorized and paid-up capital of US$1 billion and US$500 million respectively.

Investment Dar successfully closed a KD125 million (US$428 million) private placement for 50% of the capital of its new holding company **Istihwaz**.

Kuwait Finance House signed a Murabahah deal amounting to US$850 million with an international consortium, allowing customers to make purchases without having to take out a loan or pay interest.

The UK **Chancellor of the Exchequer**, Gordon Brown, gave Muslim leaders private assurances that he will provide a "level playing field" in the economy, to increase Shariah compliant financial products for British Muslims.

Gulf Finance House, **Commercial Bank** and **Abu Dhabi Investment** launched a €144 million (US$173 million) offering to be invested in residential properties in Berlin, Leipzig, Dusseldorf and Halle, amongst other locations across Germany.

The **European Islamic Investment Bank** became the first independent, Shariah compliant investment bank to be authorized and regulated by British authorities, under Part IV of the UK Financial Services and Markets Act 2000.

Public Mutual launched the **PB Islamic Bond Fund**, a fund aimed at providing annual income to investors through investments in Islamic debt securities.

National Bank of Kuwait launched the first Islamic investment fund specifically targeted to its Al-Thahabi customers.

Emirates Islamic Bank officially opened its new full-service Jebel Ali Free Zone branch to serve the industrial area and local residents.

Saudi investment firm **Al Tawfeek** launched a US$100 million Islamic private equity fund for investment in Middle Eastern and North African countries.

The Malaysian Islamic banking sector posted a pre-tax profit before zakat of RM1.55 billion (US$419.94 million) in 2005, up 57.4% from RM988 million (US$267.68 million) in the previous year.

Bin Shahib & Associates became the first UAE-based law firm to be registered by the **Dubai Financial Services Authority** to operate in the **Dubai International Financial Centre** as an ancillary service provider.

Iran-based **Esfahan Steel Company's** syndicated Murabahah financing facility was successfully closed with a total of US$70 million from leading regional Islamic and conventional institutions, including **Emirates Islamic Bank**, **ABC Islamic Bank** and the **Commercial Bank of Qatar**.

Sabre Abraaj Capital and Dubai-based **Abraaj Capital**, a US$250 million joint venture private equity fund was formed to create Indian investment opportunities.

The **European Islamic Investment Bank** announced plans to set up its Bahrain operation in the second quarter of 2006, in anticipation of obtaining authorization from the Bahrain Monetary Authority.

The **Dow Jones Citigroup Sukuk** index, to measure the performance of global bonds complying with Islamic investment guidelines was launched.

Al Baraka Banking Group reported an increase of 115.4% in its net profits to US$79.37 million for 2005. The group agreed to distribute cash dividends worth US$17 million to shareholders and to issue new shares amounting to US$122 million.

Washington-based private equity firm, **Emerging Markets Partnership**, announced its plans to start an Islamic infrastructure fund worth US$500 million to invest in Indonesia.

The **Central Bank of Kuwait** and lawmakers were urged to expedite the issue of Islamic Sukuk law to increase investment tools in the Islamic financial market.

Malaysia's Central Bank initiated a RM500 million (US$135.3 million) endowment fund to support the operations of the **International Centre for Education in Islamic Finance.**

Dubai Islamic Bank started up operations in Pakistan with the opening of its first branch in Karachi,

Gulf Finance House's US$188 million rights issue attracted a huge response from shareholders. The rights offer of 136,155,079 shares provided the bank with funding to launch its next expansion phase into the global markets.

The **North London Enterprise Credit Union** and **Business Finance North West,** set up two funds with an initial capital of £250,000 (US$436,000) to provide UK businesses with capital within the limits of Islamic law.

An extraordinary general meeting of **Abu Dhabi Islamic Bank** approved a tripling of the bank's capital to US$814 million, and the sale of 30% of the shares in an initial public offering.

Al Hajri International Group secured Dh100 million (US$27 million) in funding from the **Islamic Corporation for the Development of the Private Sector** for its proposed new factory.

Doha-based **Commercialbank** became the first conventional bank to apply for a license and to introduce an Islamic banking service unit, **Al Safa**.

** US$ rates were correct at the time the story was first published.*

APRIL news briefs

BIMB Unit Trust Management, a wholly-owned subsidiary of **Bank Islam Malaysia**, targeted 20% growth in sales for its newly re-branded Islamic trust funds. The rebranding of the four unit trust funds was part of its strategy to penetrate new markets and increase acceptance by the investing public.

The **European Islamic Investment Bank** began operations making it the first independent Shariah compliant Islamic investment bank to be authorized and regulated by the Financial Services Authority.

Injazat Capital was granted a license by the **Dubai Financial Services Authority** to operate as an authorized firm in the **Dubai International Financial Centre**.

Emaar Properties and **Dubai International Properties** announced projects worth US$18.9 billion in Morocco as part of a commitment exceeding US$20 billion by UAE investors in the coming 10 years.

Unicorn Investment Bank agreed to acquire 16.8 million of Al Tajamouat for Touristic Projects plc (Al Tajamout)'s common shares through a private placement in Al Tajamout's capital raising program.

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DBS Bank, the largest bank in Singapore, received approval from the **Dubai Financial Services Authority** to open its first branch at the **Dubai International Financial Centre**.

Bahrain Islamic Bank posted net profits of BD3.8 million (US$10.1 million) for the first quarter of 2006, an increase of 90% on 2005's corresponding period.

The Malaysian **Employees Provident Fund** held 20% with **Kuwait Finance House Malaysia** holding 20% and **Sunway City** with the remaining 60% in the proposed Sunway South Quay mixed-use property development.

University Bancorp Inc reported a record profit of US$1.99 billion in 2005 against a net loss of US$584,820 in the corresponding period in 2004. 66.3% of this was earned from its Islamic subsidiary.

Dubai Islamic Bank and **Dubai World** launched a first of its kind US$5 billion family of private equity funds to participate in strategic transactions on a global basis.

Investment Dar arranged US$1.5 billion worth of floating rate Islamic bonds to fund regional real estate projects.

Sharjah Islamic Bank opened subscriptions to its Al Hisn Property Fund, a GCC real estate fund, to UAE nationals, GCC citizens and UAE residents, with a unit price of US$5,000.

The **Central Bank of Syria** collaborated with the **Islamic Institute for Training and Researches** in Jeddah, Saudi Arabia, to train people in Islamic banking operations to meet the needs of Syrian Islamic banks.

Qatar International Islamic Bank announced that it will start operations in Syria under its subsidiary the **Syrian Islamic Bank**.

The **European Islamic Investment Bank** announced its plans to have its ordinary shares traded on the Alternative Investment Market in London post its initial public offering of £200 million (US$348.7 million).

Dubai Holding incorporated **Dubai International Properties** to consolidate its real estate activities.

Bank Muscat International participated in a total of US$250 million in syndication deals, of which US$25 million was for **Bank of Beirut's** Mudarabah financing, US$75 million for the syndicated term loan facility for **International Finance Company**, and the remaining US$150 million for a real estate development with **Al Fardan Real Estate Company** in Qatar.

Abu Dhabi Commercial Bank began a study to establish an Islamic banking subsidiary with scope in the UAE as well as the wider Gulf region.

The **Qatar Financial Centre Regulatory Authority** was admitted as an associate member to the **Islamic Financial Services Board.**

The **European Investment Bank** offered a €70 million (US$85.02 million) loan to Sri Lanka to finance its small and medium-sized industries, tourism and other sectors affected by the tsunami disaster.

Unicorn Investment Bank's proposed US$150 million Shariah compliant fund was approved by the **Bahrain Monetary Agency**.

Qatar National Bank posted a net profit of QR611.6 million (US$167.99 million), up by 56.1%, for the first quarter of 2006.

A member of the UAE-based **Al Rostamani Enterprise**, **KM Properties,** established a US$2.3 billion, Shariah compliant, real-estate development fund to develop and own an international chain of hotels that abide by the Islamic principles of Shariah.

Lloyds TSB of Scotland announced the launching of a series of products compliant with Islamic law.

The **Islamic Development Bank** allotted US$356 million to delve into development and technical assistance projects as well as loans to members and non-members.

United International Bank received an overwhelming positive response from investors from across the region, including financial institutions, banks, big business families and individual businessmen.

First Investment Company appointed **Advantage Consulting**, to help the former with its organizational reengineering, streamlining its internal policies and procedures, internal communication protocols, review of the corporate governance initiatives and its investment strategies.

Emirates Islamic Bank's Asset Management Unit launched the Emirates MENA Opportunities Fund to achieve long-term capital growth through investments in a range of growth orientated assets, including equities and real estate.

continued...

APRIL news briefs *(continued...)*

Three Islamic banks were granted license to start operations in Syria.

National Bonds Corporation announced sales of more than AED130 million (US$35.39 million) worth of National Bonds in its first month of sales.

Path Solutions was ranked the world's number one dedicated Islamic banking system Vendor for 2005 in the influential International Banking Systems annual sales league table.

Al Salam Bank signed an agreement with the Bahrain Stock Exchange to pave the way for the trading of shares on the bourse.

CIMB-Principal Asset Management announced its merger with **SBB Mutual** and **SBB Asset Management**, making it Malaysia's largest asset management company.

The **Islamic Development Bank** granted the Moroccan refinery LASAMIR a Fund Line of Credit of US$100 million intended to cover the importation of crude oil by the company.

The **Islamic Development Bank** approved US$460 million for project financing and trade operations.

Al Rajhi's US$500 million Murabahah financing facility was successfully closed. The joint book-runners **Calyon** and **Gulf International Bank** confirmed the facility's oversubscription, increasing its size from US$300 million to US$500 million.

The **Islamic Development Bank** financed four major water industry projects in Iran, worth US$150 million.

Qatar National Bank and **QNB Al Islami** agreed to provide banking facilities and funds for Dar Investment and Development's two prestigious projects in Doha – the Lagoon Plaza and Palm Towers.

Qatar International Islamic Bank posted a net profit of QR101.5 million (US$27.88 million) in the first quarter of 2006, up 114% from the previous corresponding period.

The **International Investment Bank** launched a commercial real estate investment offering investors attractive returns over a relatively short investment holding period.

Kuwait Finance House called for the providing of administrative and legal incentives to encourage investment in the real estate sector.

Abu Dhabi Islamic Bank posted a net profit of Dh156.3 million (US$42.6 million) for the first quarter of 2006, up by 277.5% over Dh41.4 million (US$11.27 million) earned in the same period in 2004.

Bank Rakyat Indonesia announced its intentions to spin off its Shariah unit to become an independent Islamic bank.

Dubai International Financial Centre Authority's investment arm acquired more than a 1% stake in **Euronext** to complement its centers in Europe, USA and the Asia Pacific region.

Amlak Finance reported a net profit of AED37.1 million (US$10.1 million) (after depositor's share) for the first quarter ended 31st March 2006; an 86% increase over the same period in 2005.

The **Dubai International Financial Centre Authority** launched a subsidiary called **DIFC Investments**.

HSBC Bank Malaysia introduced the country's first Shariah compliant structured investment product to further complement the success of its Islamic banking business.

The **Islamic Development Bank** intensified its operations in Bosnia including staff training on principles of Islamic banking.

Sharjah Islamic Bank acquired Sharjah National Hotel Corporation for Dh520 million (US$141.6 million) from the Sharjah government.

The total assets of Malaysia's Islamic banking industry stood at RM47.1 billion (US$12.94 billion) in 2005, accounting for 11.3% of country's total banking assets.

The Malaysian **Securities Commission** introduced a set of enhanced guidelines aimed at promoting greater protection for shareholders and investors, as part of its continued efforts to further develop a facilitative regulatory framework for fundraising.

Merrill Lynch was accepted as a General Clearing and Trading Member firm to trade securities by the **Dubai International Financial Exchange (DIFX)**.

The **National Commercial Bank** signed a SR725 million (US$193 million) Islamic finance contract (Commercial Taysser) supported by assets with the Abdul Latif Jameel Company.

Moody's Investors Service announced its plans to establish an office in Dubai.

Bahrain-based **Shamil Bank** reported a 10% increase in profits in the first quarter of 2006.

Gulf Finance House obtained approval from the Emirates Securities and Commodities Authority to list its shares on the **Dubai Financial Market**.

Kuwaiti investors took up 32% of the total capital of the proposed **Al-Sham Bank** in Syria.

Abu Dhabi Commercial Bank was appointed to provide sub-custodian services on the **Dubai International Financial Exchange**.

Real Estate Finance Company was launched to offer its services to homebuyers and property investors in Bahrain's rapidly growing real estate sector.

The **Bahrain Monetary Agency** announced the oversubscription of the monthly issue of its short-term Islamic Leasing Sukuk securities.

Bank Pembangunan Malaysia issued RM1 billion (US$274 million) in notes pursuant to its Islamic and conventional 30-year medium-term notes (MTNs) programs of an aggregate amount of up to RM7 billion (US$1.92 billion) established in early 2006.

** US$ rates were correct at the time the story was first published.*

MAY news briefs

International Investment Bank created a real estate development company for investment in the Saudi Arabian real estate market with an authorized capital of SR400million (US$107 million). The entity will invest SR2 billion (US$533 million) in the Saudi Arabian property sector over the next three years.

Brunei initiated its Islamic capital market with the issuance of short-term BND150 million (US$95.3 million) Sukuk al-Ijarah making it the first Ijarah-based Islamic money market program in the world.

United International Bank was launched by the **Bahrain Monetary Institution**, making it the biggest Islamic bank in the Middle East.

Bahrain-based offshore investment bank **United Gulf Bank** projected a 5% growth to US$85 million in net profit for 2006.

Gulf Finance House recorded a net profit of US$57 million for the first quarter of 2006 charting a 75% increase from 2005. Total assets increased by 133% to US$1.28 billion, while shareholders' equity grew by 110% to US$524 million.

RUSD Investment Bank announced plans to launch a US$200 million Islamic fund to be invested in Malaysian properties.

Singapore-based **CapitaLand** Commercial and Integrated Development signed a memorandum of understanding to acquire land and develop a US$600 million residential and retail zone within the Bahrain Bay development project.

IXIS Corporate & Investment Bank received a **Dubai Financial Services Authority** license to operate out of the **Dubai International Financial Centre**.

Allen & Overy and **Shook Lin & Bok** were appointed to advise **HSBC** on the development and implementation of Brunei's Ijarah based Islamic debt program, as well as the first issue of a US$95.3 million debut Islamic Sukuk issue.

The **Islamic Development Bank** signed six financing agreements amounting to more than US$170 million with the Palestinian authority and Morocco.

The **Emirates Bank Group** announced a 123% increase in net profits to Dh603 million (US$164 million) for the first quarter of 2006, compared to Dh270 million (US$73.51 million) in the same period of 2005.

The **Saudi Health Investment Company** signed a landmark agreement with **Injazat Capital's** Shefa Healthcare Fund for the former to invest US$37.5 million in private equity capital into the fund and gain three seats on the fund's board of directors.

Qatar Islamic Bank's new structure, which requires the managing director, executive committee, Shariah Control Board and the executive president to report directly to the bank's board of directors, was approved.

The **Dubai Department of Civil Aviation** completed a US$1 billion 3-year Ijarah facility, with **Dubai Islamic Bank** appointed as mandated lead arranger to spearhead the funding of the development and expansion of **Dubai International Airport**.

Bosnia-based **Bosna Bank International** partnered with Dubai's **Misys Equation Islamic** and **Misys Trade Innovation** to help expand the reach and capabilities of its retail banking operation and trade finance services for corporate customers.

It was reported that Islamic investment funds in Bahrain increased by 20% from 2001 to 2006, almost hitting the US$1 billion mark.

RHB Unit Trust Management launched the first fund in Malaysia tracking the Dow Jones–RHB Islamic Index, priced at RM1 (US$0.277) during the initial period (up to 31st May), with its minimum initial investment set at RM1,000 (US$277) or US$1,000.

Kuwaiti company **Markaz** obtained a license to open a branch office at the **Qatar Financial Centre**.

Amlak Finance announced the establishment of **Amlak Investments** with an authorized capital of Dh500 million (US$136 million).

Hong Leong Islamic Bank saw its financing business grow by 14% for the nine month period ending on the 31st March 2006.

Abu Dhabi Investment House opened a US$41.5 million private placement to finance the 600,000 square feet Lagoon project in Bahrain.

The initial public offering of **Bank Asya** was 50 times oversubscribed and raised US$160 million from the selling of 60 million shares.

International Investment Bank posted a five-fold increase in net profit to US$3.54 million for the first quarter of 2006.

Bondweb Malaysia was appointed Malaysia's first bond pricing agency by the Malaysian **Securities Commission**, making it the official source for fair valuation of ringgit bonds.

Emirates Bank and **Standard Chartered Bank** were mandated by Dubai Holding to finance a 35% equity stake in **Tunisie Telecom**.

Shamil Bank chalked up a 10% increase in net profit to US$11.3 million for the first quarter of 2006 from the previous US$10.2 million in the previous corresponding period.

Sokouk Holding Company partnered with **Munshaat Real Estate Projects Company** to form one of the largest Islamic investment banks specializing in Sukuk exchange activities in Bahrain.

Arcapita Bank's US$800 million capital-doubling proposal was approved, with US$200 million shares to be issued to existing shareholders and the remaining US$200 million offered to new investors.

The shares of **Gulf Finance House** commenced trading on the **Dubai Financial Market**, making it one of the few GCC companies to be cross-listed on the Kuwait Stock Exchange, Bahrain Stock Exchange and the Dubai Financial Market.

continued...

MAY news briefs *(continued...)*

The **Islamic Development Bank** confirmed a partnership with **JK Bank** in the Mission Kashmir project, in which the former will tap into the network of JK Bank to sell its products in the economy.

The **National Bank of Ras Al Khaimah**'s proposal to establish an Islamic finance company in the UAE was approved by the Central Bank with a start-up capital of US$54 million.

Malaysian Prime Minister Abdullah Ahmad Badawi urged all D-8 countries to collaborate in enhancing their respective capacities in Islamic finance and jointly spearhead further growth of the sector at the Fifth D-8 Summit in Bali.

Gulf Finance House closed a US$90 million syndicated Murabahah facility with nine banks across Europe, Asia and the Middle East.

The **Gulf International Bank** signed a US$40 million 13-year term loan facility with the **Bahrain District Cooling Company** to finance the construction of cooling plants for the latter's major contract, which includes the Bahrain World Trade Centre.

Total assets of the **Islamic Bank of Brunei** and the **Islamic Development Bank** increased by almost six-fold from B$769 million (US$486.9 million) in 1993 to approximately B$5 billion (US$3.17 billion) in January 2006.

Dubai Financial successfully acquired a 31.5% stake in **Marfin Financial Group**.

The Malaysian **Securities Commission** approved the listing of the Al-'Aqar REIT by **KPJ Healthcare** with an initial fund size of 205 million units.

The **Dubai International Financial Exchange** became the first stock exchange in the Middle East to list financial derivatives, index products and financial instruments compliant with Islamic law.

Dubai Islamic Bank closed a US$500 million Ijarah facility to finance an upgrade of the Jebel Ali refinery of **ENOC Processing Company**, a wholly owned subsidiary of **Emirates National Oil Company**.

Abu Dhabi Investment House signed a memorandum of understanding with **Al Areen** to develop four residential and commercial properties for US$335 million.

The **European Islamic Investment Bank** raised £75 million (US$142 million) through its initial public offering, of which £60 million (US$113 million) was raised through an offer to existing shareholders.

Bukhatir Investments signed a US$50 million agreement on the establishment of its first investment agency Sukuk in Sharjah.

Dubai Islamic Insurance and Reinsurance Company launched its initial public offering to increase its capital to Dh200 million (US$54 million).

Maybank raised RM1.5 billion (US$417 million) from the second sale of its Islamic bonds within a six-month period.

National Bonds Corporation included **Wall Street Exchange** and **Redha Al-Ansari Exchange** as their distribution partners to help meet the rising demand for its Shariah compliant savings scheme.

Abraaj Capital collaborated with **Deutsche Bank** and **Ithmaar Bank** to raise a US$2 billion Shariah compliant alternative assets fund.

Sumitomo Mitsui Banking Corporation was licensed by the **Dubai Financial Services Authority** to operate at the **Dubai International Financial Centre**.

Dow Jones Indexes and **Citigroup Corporate and Investment Banking** launched the first global Islamic bond index – the Dow Jones Citigroup Sukuk – in the US.

Unicorn Investment Bank collaborated with **Abu Dhabi Holding Company** to launch its second real estate fund – Gulf Springs, a US$150 million Shariah compliant fund.

Dubai Islamic Bank announced the launch of its newest investment fund – Al Islami Capital Protected Note.

Commercial Bank of Kuwait increased its stake in the **Bank of Bahrain and Kuwait** to 20.15% from last year's 6.75%.

Al-Baraka Turk Participation Bank's net profits for the first quarter of 2006 rose to US$9.16 million, an increase of 29.9% compared to US$7.05 million in the previous year.

People's Leasing Co., Sri Lanka's biggest company began offering Islamic financial products to the 7.5% Muslim population.

Arab Bank received a banking license from the **Financial Services Authority, UK** to establish the **Europe Arab Bank**, with a capital of €500 million (US$642 million).

First Dawood Islamic Bank received an Islamic banking license from the **State Bank of Pakistan**.

The **Dubai International Financial Centre** increased its stake in Europe's second-biggest stock exchange – Euronext – to 3.48% from 1.67% earlier in 2006.

Dubai Financial Market appointed **OMX** to be the system provider for the license, customization, implementation and support of the market's new high performance trading system platform.

Central Bank of Kenya approved the setting up of the first Islamic bank in Kenya.

Deyaar raised its paid-up capital to Dh1 billion (US$272 million), a 100% increase from Dh500 million (US$136 million) after obtaining approval from its board of directors and parent company, **Dubai Islamic Bank**.

Kuwait Finance House revealed its US$150 million plan of building over 300 luxury villas in Ishbiliya Village, Al Qadam, on a 176,000m2 site close to Manama.

Ithmaar Bank embarked on an agreement with the **Bahrain Stock Exchange** to have its shares listed on the exchange.

** US$ rates were correct at the time the story was first published.*

JUNE news briefs

Dow Jones Indexes launched the **Dow Jones Islamic Market China Offshore Index**, representing companies in China that have undergone Shariah screening.

Deutsche Bank became the first broker from outside the Gulf to be listed as a full member of **Tadawul Stock Exchange** when it launched its brokerage business on the GCC's largest exchange.

The **Bahrain Monetary Agency** and **Qatar Financial Centre Regulatory Authority** signed a memorandum of understanding aiming to improve co-operation between both countries on financial matters.

Kuwait was announced to have the most Islamic financial institutions in the world and ranked third in terms of the assets of these bodies, at US$22.7 billion.

The **Islamic Development Bank** announced its plans to develop the first Islamic currency swap through raising US$263 million in Malaysian ringgit bonds and swapping the earnings into a different currency.

Bukhatir Investments officially launched its first investment agency Sukuk, a US$50 million Sukuk Al Wakala Bel-Istithmar, to fund the company's ongoing investment activities. **Emirates Islamic Bank** and **Liquidity Management Center** served as the mandated lead arrangers.

Albaraka Banking Group posted a US$102.09 million net profit at the end of 2006's first quarter, as compared to US$67.35 million in the previous year.

Islamic Development Bank executives approved a total of US$393.5 million to finance projects, including seven new development projects in six member states and non-refundable grants to finance education projects in four Islamic societies.

The **Islamic Corporation for the Development of the Private Sector**, founded by the **Islamic Development Bank**, shifted its strategy towards involvement in the private sector, rather than relying solely on government ventures.

UAE vice-president and prime minister Shaikh Mohammad Bin Rashid Al Maktoum issued a decree to set up a committee to transform the **Dubai Financial Market** into a public shareholding company.

The **Islamic Development Bank** announced the establishment of a new arm aimed at increasing trade activities among the 56 **Islamic Development Bank** member states to 20% from the current 13%.

Hawkamah, the Institute for Corporate Governance, and subsidiary of the **Dubai International Financial Centre Authority** signed a memorandum of understanding with the **Egyptian Banking Institute** to promote corporate sector and corporate governance reforms.

First Gulf Bank announced the launch of two major developments in Abu Dhabi – Ocean Terrace and Seashore Villas– amounting to Dh645 million (US$175.6 million).

Dubai Islamic Bank partnered with the **National Human Resources Development and Employment Authority** to meet UAE nationals seeking employment at the bank.

The **Dubai Financial Services Authority** granted **Citigroup Global Markets** a license to operate at the **Dubai International Financial Center**.

Bank Islam Malaysia declared an increase in revenue by 22% to RM724.3 million (US$200 million) for the third quarter, while securing RM545 million (US$150.5 million) in non-performing loans.

Saudi Basic Industries Corporation announced the launch of an Islamic finance arm managing its domestic Islamic bond issuances.

The **Commercial Bank of Kuwait** launched the Tijari Islamic Fund with a capital of KD100 million (US$345.8 million).

A consortium of Middle Eastern investors, comprising **Sokouk Holding**, **Kuwait Investment**, **Commercial Real Estate** and **Qatar Islamic Bank**, revealed plans to invest US$200 million in the development of a Sukuk Exchange Center in Bahrain.

Aabar Petroleum Investment Company launched a US$350 million exchangeable Sukuk al Mudarabah for book-building through its subsidiary **Aabar Sukuk**.

UM Financial surpassed US$50 million assets in real estate investments within a Musharakah product, involving 200 residential units, during its first operational year.

Kuwait Finance House Malaysia started offering the KFH Promissory FX Contract-I, which has a hedging mechanism to protect customers against fluctuations in foreign exchange rates.

Shamil Bank developed a series of investment opportunities in the high-growth China real estate market following the successful launch of the first Islamic real estate fund for investment in China earlier in 2006.

Affin Bank officially launched **Affin Islamic Bank**, serving as its Islamic banking subsidiary.

The **Bahrain Monetary Agency** issued licenses for two international groups – **Dexia Group** and **American Express Bank** – to expand their operations in the country.

Malaysia's largest private healthcare group – **KPJ Healthcare** – proposed to increase the fund size of its Al Aqar KPJ REIT to 340 million units, a 66% increase from its initial 205 million units.

Abraaj Capital, in collaboration with **BMA Capital**, launched the largest private equity fund at US$300 million targeting investments in Pakistan, called the Abraaj BMA Pakistan Buyout Fund LP.

Sama Dubai, the international real estate investment and development arm of **Dubai Holding** entered a joint venture with **Emirates Bank Group** to create a Dh22 billion (US$5.9 billion) real estate fund.

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JUNE news briefs *(continued...)*

Qatar International Islamic Bank received approval from the Ministry of Economy and Commerce to develop a rights issue, to raise the bank's capital by 15% to QR467 million (US$128 million).

Ahli Capital Company, a new closed shareholding company, was established in Kuwait with a capital of KD15 million (US$51.8 million) and 150 million real shares valued at 100 fils per share.

FTSE Group and the **Dubai International Financial Exchange** joined create the first GCC country tradable indices– FTSE DIFX UAE 15 Index, FTSE DIFX Kuwait 15 Index and FTSE DIFX Qatar 10 Index.

The **National Bank of Dubai** obtained pre-approval from the UAE Central Bank to establish an Islamic finance company.

BIMB Holdings plans to become the first true-blue Islamic investment bank in Malaysia through the rationalization of its operations.

Unicorn Investment Bank and **WestLB** embarked on a roadshow promoting their five-year US$150 million Musharakah Trust Sukuk for the Kuwaiti company Investment Dar.

The **Monetary Authority of Singapore** announced the allowance for banks to offer investment products through Murabahah.

The **Islamic International Rating Agency** became a member of the **Association of Credit Rating Agencies** in Asia.

Ithmaar Bank invested its US$2 billion Islamic private equity fund in infrastructure in the MENA region and South Asia, in projects estimated to be worth over US$20 billion.

Poh Kong Holdings increased its Islamic debt to RM200 million (US$54.5 million), to be used to refinance existing debt, repay shareholders' and directors' loans, as well as for working capital, capital expenditure and future investments.

The **Islamic Development Bank Group**'s board of governors approved the proposed doubling of the bank's capital to US$40 billion.

The Bahrain Monetary Agency partnered with eight leading Bahraini Islamic banks to establish a special fund to support research, education and training in Islamic finance.

KASB chose Misys Equation, the core banking system of **Misys Banking Systems**, to help grow its retail banking business.

The International Investor successfully acquired **RFM Loyalty Private**, a Karachi-based credit card and loyalty management services business.

Amanah Capital collaborated with **Deutsche Bank** in the launch of the Al Hosin Fund, the region's only Shariah compliant investment product with an 80% profit lock-in and weekly entry/exit options.

Unicorn Investment Bank acquired a 20% equity stake in the **First Dawood Islamic Bank**, enabling **Unicorn Investment Bank** to penetrate the Pakistani market.

JS Finance announced the launch of the first of a series of real estate Mudarabah businesses – Modaraba Al Makatib – with a capital of RS200 million (US$3.3 million).

Bemo Securitization successfully closed the first ever Shariah compliant oil and gas securitization, valued at US$165.67 million.

A.T. Kearney announced its intention to establish a regional base at the **Dubai International Financial Centre** to serve its growing client list and to support the continued expansion and diversification of the UAE economy.

Trade and Islamic finance specialist **CCH International** increased its financing facilities by US$50 million, raising its committed funding lines to over US$240 million.

SBB Mutual posted an income distribution of RM0.05 (US$0.0136) per unit for SBB Dana Al-Ihsan, equivalent to 7% of its current net asset value.

The Ministry of Finance, Brunei **Shell Marketing** and **Bank Islam Brunei Darussalam** jointly launched an Islamic system for fleet card management – Kad Inden – to ensure the government's efficiency in buying fuel.

The **Bahrain Stock Exchange** signed an agreement with **Investment Dar Sukuk Company** to list the company's US$100 million Musharakah Sukuk on the stock exchange with par value of US$10,000 each.

CIMB Group partnered **Yusuf Bin Ahmed Kanoo Holdings** in the establishment of a joint venture entity in Bahrain. Both CIMB and Kanoo Group will have a 50% equity interest in the **CIMB-KANOO Islamic Investment Company** respectively.

The **Dubai International Financial Centre** announced its target to host 20% of the world's investment funds.

Bahrain Monetary Agency granted an initial license to set up the first Islamic investment bank for women in Bahrain, with a capital of US$1 billion and a paid-up capital of US$500 million.

The **Bahrain Monetary Agency** announced regulatory reforms to modernize and strengthen the licensing framework for banks.

Amana Investments collaborated with **PATH Solutions** to acquire the latter's Islamic banking software – iMal.

Ithmaar Bank announced plans to acquire a 60% stake in its sister company, **Shamil Bank**, from the **Dar Al- Maal Al-Islami Trust**.

Gulf Finance House appointed **PricewaterhouseCoopers** to advice on the development of **Qatar Finance House**.

Dubai Bank launched Muhafez, a Shariah compliant investment certificate.

London-based **Yasaar** became the first Shariah compliant financial advisory firm to be based at the **Dubai International Finance Center**.

Abu Dhabi Islamic Bank launched e-ADIB, an online banking service to provide customers with the flexibility of performing banking transactions at their convenience.

** US$ rates were correct at the time the story was first published.*

JULY news briefs

Deutsche Bank became the first custodian bank in Indonesia to offer Shariah fund administration services certified by the Republic's National Shariah Board.

FS International Partners launched an investment scheme to establish the first Shariah compliant bank in France: **Tayseer Bank**.

The **Institute of Corporate Governance**, Hawkamah, announced the development of the first corporate governance code for listed companies in the UAE, having signed a memorandum of understanding with the **Emirates Securities and Commodities Authority**.

The **Dubai Financial Services Authority** granted **ABN Amro** a license to operate fully in the **Dubai International Financial Center**.
Islamic Funds
Abraaj Capital jointly with **Ithmaar Bank**, launched the **Serai Group** to develop and manage an international chain of Middle Eastern-themed Shariah compliant hotels, with a capital of US$500 million.

Dubai Islamic Bank launched the Al Islami Shipping Fund, a Shariah compliant investment fund investing in selected shipping assets through Musharakah joint ventures.

A US$200 million Syndicated Mudarabah restricted with Commodity Murabahah Financing Facility for **Bank TuranAlem** was successfully closed by the mandated lead arrangers, **Abu Dhabi Islamic Bank** and **Calyon**.

The **Saudi Basic Industries Corporation**'s proposed issue of up to SR3 billion (US$799.94 million) of Sukuk was approved by the Saudi Capital Market Authority, making it the first to be launched in Saudi Arabia under the new Capital Market Law.

Bank Negara Malaysia's total liquidity surplus was cut to RM6.64 billion (US$1.82 billion), of which RM3.9 billion (US$1.07 billion) was from conventional operations and the balance of RM2.74 billion (US$750 million) was in Islamic funds.

Aabar Sukuk listed its US$460 million Sukuk al Mudarabah on the **Dubai International Financial Exchange** to raise the capital of its sponsor – **Aabar Petroleum Company** – for ongoing business development.

Forsyth Partners relocated its global headquarters from London to Dubai, by establishing its group holding company in the **Dubai International Financial Centre**.

Dubai Investment Group via its subsidiary, **Dubai Financial**, signed an agreement to acquire a 40% stake in **Bank Islam Malaysia**.

Qatar Islamic Bank slashed the price of its rights issue to QR70 (US$19.23) per share, in view of the prevailing weak market scenario.

The **National Bonds Corporation** announced that more than Dh300 million (US$81.67 million) worth of National Bonds were sold since the launch of sales in March 2006.

The **Islamic Development Bank**'s executive directors met at the bank's 293rd session to discuss the IDB's contribution to an increase in the capital of the Islamic International Agency for Specifications and Standards.

South Africa began looking to Islamic banking as a financial alternative to conventional banking, having been impressed by the success of the industry in Malaysia.

Indonesia's state electricity company, **Perusahaan Listrik Negara** announced plans to offer up US$2.5 billion in Islamic bonds.

Islamic banks were urged to compete with traditional banks to create a competitive environment in Pakistan's banking sector.

The **Islamic Development Bank** approved US$125 million as leasing finance in favor of **Saudi Basic Industries Corporation**'s subsidiary **YANSAB National Petrochemicals Company**.

First Finance, the Islamic financial services company in Doha, listed at the Doha Securities Market.

Calls were made to fulfill the growing need for Shariah auditors in the Islamic financial system as Malaysia continued its move towards becoming a world-renowned Islamic financial hub.

RHB Unit Trust Management's RHB Global Islamic Portfolio Series saw a take-up rate of 30%.

The shares of **Tamweel** commenced trading on the **Dubai International Financial Exchange**.

The **Dubai International Financial Centre** began talks to create a financial district in India, hoping to open as early as 2007.

The **Dubai International Financial Centre** signed a memorandum of understanding with **Standard Chartered** to train and develop UAE nationals for careers in the financial services industry.

EFS International received approval from the **Dubai Financial Services Authority** for a license enabling it to offer a comprehensive range of investment banking products and services from a base in the **Dubai International Financial Exchange**.

Bahrain-based **Noriba Bank** fully integrated into its owner, the **UBS Group**.

Dubai Islamic Bank reported a 56% rise in its first half net profit to reach Dh707 million (US$192 million), compared to Dh454 million (US$123 million) in 2005.

Bahrain-based **Unicorn Investment Bank** and Johannesburg-based **Standard Bank** closed the first true-sale securitization in the GCC on behalf of **Kingdom Installment Company** in Saudi Arabia, backed by US$23 million.

Dlala Islamic Brokerage announced a 150% increase in its customer base, mainly due to more stock investors from the GCC states joining its clientele portfolio, and the growing number of companies investing in Islamic stocks and banks listed on the Doha Securities Market.

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JULY news briefs *(continued...)*

Bahrain-based **BankMuscat International** posted a net profit of BD1.9 million (US$4.9 million) – an increase of 34% – for the first half ending on the 30th June 2006.

The **Dubai Financial Services Authority** approved **Gulf Capital Group** to operate from the **Dubai International Financial Center**.

Sharjah Islamic Bank posted net profits for the first half of 2006 of Dh91.3 million (US$24.85 million), as against Dh98.4 million (US$26.8 million) for the same period in 2005.

UAE banks reported lower profits in the second quarter due to the lack of earnings from initial public offerings, in addition to poor returns from a falling stock market.

The **Islamic Development Bank** announced its plans to sell up to RM1 billion (US$271 million) worth of Islamic bonds in what will be its first debt offering in the Malaysian currency.

Qatar International Islamic Bank recorded a net profit of QR191.8 million (US$52.7 million) for the first half of 2006, up 114% on the QR89.5 million (US$24.58 million) it earned in 2005.

Switzerland's **Liechtensteinische Landes Bank** launched two investment funds focused on the Gulf and MENA markets, with total subscriptions of US$2 billion.

Abu Dhabi Commercial Bank reported a record net profit for the first half of 2006 of Dh1.19 billion (US$324 million), as against Dh844 million (US$229.77 million) for the same period in 2005.

Emaar Properties reported a 21% growth in first half net profit to Dh3.053 billion (US$831 million), compared to Dh2.53 billion (US$689 million) for the same period in 2005.

Two Abu Dhabi-based UAE banks applied for licenses to operate in Pakistan.

Public Mutual received the **Securities Commission's** approval to increase the fund sizes of its Public Islamic Dividend Fund, Public Islamic Balanced Fund, Public Regional Sector Fund and Public Islamic Opportunities Fund.

HSBC Amanah completed its first Islamic private equity investment of US$31 million in the management buy-out of **Amtech Power Software**.

Minetech Resources announced plans to issue up to RM100 million (US$27.12 million) Islamic debt papers to tap the competitive private debt securities market and reduce its borrowing costs for expansion.

Mashreq Capital, a wholly-owned subsidiary of Mashreqbank was granted a license from the **Dubai Financial Services Authority** to operate at the **Dubai International Financial Center**.

Union National Bank's first half net profit increased by 20%, reaching AED627.34 million (US$170.8 million).

Zecon Toll Concessionaire proposed to issue a RM60 million (US$16.27 million) Bithaman Ajil Islamic Debt Securities facility to refinance its short-term loan and for working capital.

The **Dow Jones Islamic Market** BRIC Equal Weighted Index was launched to measure the performance of companies in the Brazil, Russia, India and offshore China markets that pass screens of Shariah compliance.

CIMB lead managed the **National Central Cooling Company**, **Tabreed**'s US$200 million Sukuk.

Emirates Islamic Bank revealed expectations for its business to double by 2009 with increasing demand for Islamic banking.

Saudi Basic Industries Corporation signed the underwriting agreement for its debut SR3 billion (US$800 million) Sukuk with the lead manager **HSBC Saudi Arabia** and a group of co-managers including **Banque Saudi Fransi**, **National Commercial Bank**, **Samba Finance Group**, **Saudi Hollandi Bank**, **SABB** and **Gulf International Bank**.

Jasper Capital launched its new subsidiary, **Jasper Consult Financial Services**.

Thailand's bourse began studying the feasibility of introducing an Islamic Index to draw Muslim investments into the local bourse.

The world's first Islamic real estate investment trust, Al-'Aqar KPJ REIT IPO was launched with **AmMerchant Bank** appointed as the adviser, managing underwriter and sole placement agent.

Emirates Bank Group chalked a net profit of AED971 million (US$264.3 million) for six months ended 30th June 2006, reflecting a 36% increase over AED712 million (US$193.48 million) earned in the same period in 2005.

Standard Chartered Bank Malaysia, along with **Bank Muamalat Malaysia** executed the first Islamic cross-currency swap in the world.

The Malaysian **International Centre for Education in Islamic Finance** inked a memorandum of understanding with **Lembaga Pengembangan Perbankan Indonesia** for human capital development in the Islamic finance industry.

Dubai International Financial Center announced the establishment of an Islamic liquidity management center with a start-up capital of US$1 billion.

Kuwait Finance House Bahrain teamed up with **Bahrain Development Bank** to form a US$10 million venture capital company to finance and invest in the Small and Medium Enterprises in Bahrain.

BIMB Unit Trust Management declared an income distribution of 1.5 sen (US$0.004) per unit for its **Amanah Saham Bank Islam** Dana Al-Muin, equivalent to a 6.42% return from the fund's net asset value as at 1st July 2006.

** US$ rates were correct at the time the story was first published.*

AUGUST news briefs

It was confirmed that **AmBank Group** was working closely with the **Zambia Malcolm Group** to establish an Islamic bank in the Christian-dominated Zambia.

Kuwait Finance House Malaysia launched a Shariah compliant foreign exchange hedging solution, which allows customers to protect themselves against unexpected movements in foreign currency.

Dubai Bank's Shariah Board approved the bank's plan to convert into an Islamic bank.

PLUS Expressways announced plans to sell RM6 billion (US$1.63 billion) in bonds.

Sharjah Islamic Bank revealed it would offer its first US$200 million Sukuk issue.

Lloyds TSB launched Islamic student accounts through its 2,000 UK branches.

Khaleeji Commercial Bank reported a 228% rise in net profit to BD5 million (US$13.26 million) for the first half of 2006.

The **Hwang-DBS** Islamic Cash Fund, a Shariah compliant institutional cash management product targeted at corporate and institutional investors, was launched.

Public Mutual launched its first overseas Islamic fund, the Public Asia Ittikal Fund.

Pakistan's Central Bank revealed that Islamic banking licenses may be granted to two new applicants.

Calyon announced it would offer Shariah compliant deposit services in Singapore, before expanding into Brunei, Indonesia and Malaysia.

The inaugural **Malaysian Islamic Finance - Issuers & Investors Forum 2006** (MIF) was hailed as a success by the deputy governor of Malaysia's Central Bank, among other key industry figures.

Dubai Bank revealed its plan for conversion from a conventional to a Shariah compliant institution. The conversion was targeted for completion within an 18-month period.

Cooling company **Tabreed** successfully closed its innovatively structured US$200 million Sukuk after an overwhelming response from international investors.

Bank Negara Malaysia revealed measures designed to attract foreign investors to Islamic banking in Malaysia.

The **Malaysian Securities Commission** and the **Dubai Financial Services Authority** signed a memorandum of understanding to improve co-operation between the Malaysian and the Dubai regulators.

Bursa Malaysia announced it would introduce Islamic indices to encourage foreign investors to invest in Shariah complaint products in Malaysia.

Bank Negara Malaysia revealed its Murabahah instrument will use crude palm oil as the underlying transaction tool.

Kuwait Finance House was in discussions with various undisclosed government-linked companies over how to structure Islamic Real Estate Investment Trusts to attract foreign direct investments.

CIMB revealed it would set up an Islamic finance banking business in Thailand.

An Islamic financial hedging tool was been introduced by **Standard Chartered Malaysia**.

A US$230 million Islamic loan, arranged by **Kuwait Finance House**, was secured by Southeast Asia's largest budget carrier, **AirAsia**, in order to purchase more planes.

Unicorn Investment Bank posted record half year results for the first six months of 2006. Net profit increased from US$5.3 million to US$23.8 million (a 353% rise) year-on-year.

The **Islamic Development Bank** was considering granting a US$1.5 billion loan to Iran.

The first ever corporate issue of Shariah compliant financial instruments based on the Sukuk Al Ijarah concept - a collaboration between **Brunei LNG**, **Bank Islam Brunei Darussalam** and the **Ministry of Finance** - were launched.

Malaysian property developer **Glomac** proposed to issue RM175 million (US$48 million) of Islamic Murabahah underwritten notes and Murabahah medium-term notes facilities.

Ithmaar Bank purchased 136.97 million shares in its sister company **Shamil Bank** in a US$410 million transaction, bringing its share in Shamil Bank up to 60%.

Qatar Islamic Bank, the largest Islamic lender in Qatar, received orders for over double the stock it offered in a share sale.

Kuwait Finance House Malaysia said it was finalizing an Islamic bond issue for a Chinese state-owned company.

The **Malaysian Securities Commission** approved **AmMerchant Bank** to establish and list Malaysia's first equity exchange traded fund on the **Bursa Malaysia** main board.

Debt-plagued Malaysian steel miller **Perwaja** announced it would sell RM400 million (US$109.23 million) worth of Islamic bonds to refinance its debts.

Standard Chartered agreed to buy an 80.9% stake in Pakistan's **Union Bank** for US$413 million, making the biggest purchase by a foreign bank in Pakistan.

Dubai Islamic Bank subsidiary **Al Islami Financial Services** opened its first branch exclusively for women in UAE.

Mashreqbank revealed its plans to launch an independent Islamic finance subsidiary - to be called **Badr Al Islami** - and had appointed its Shariah board.

continued...

AUGUST news briefs *(continued...)*

FTSE Group and the **Dubai International Financial Exchange** jointly created two Shariah compliant, Gulf Co-operation Council country equity indices for domestic, GCC and international investors.

Dubai Islamic Bank launched a Shariah compliant investment fund - Al Islamic Shipping Fund - that invests in selected shipping assets through Musharakah joint ventures.

Bank Sohar was planning to float a RO20 million (US$52 million) initial public offering at the beginning of November.

Shuaa Capital's proposed buy-back of up to 10% of its shares within the next 12 months obtained approval from the **Emirates Securities and Commodities Authority**.

Kuwait donated US$300 million to a poverty fund set up by the **Islamic Development Bank** to help the least-developed Muslim nations.

Amanah Raya expected to launch a RM1 billion (US$272.89 million) unit trust in September, half of which would be Shariah compliant.

Gulf Finance House signed an agreement with the **Egyptian government** and an alliance of GCC establishments on the development of infrastructure in Egypt.

Shamil Bank posted a net income increase of 80.3% from the US$21.21 million earned in the first half of 2005 to US$38.23 million earned in the first six months of 2006.

The **Dubai Financial Services Authority** granted a license to **Goldman Sachs International** to operate as an authorized firm in the **Dubai International Finance Centre**.

The Bahrain-based **Islamic International Rating Agency** was looking to extend its influence into the Islamic financial industry of the Far East.

Emirates Islamic Bank charted a net profit of AED 43 million (US$11.70 million) registering a net profit increase of 177% over the net profit results in the corresponding period in 2005.

The public issue of Islamic healthcare real estate investment trust, **Al-'Aqar KPJ REIT**, of 15 million shares was oversubscribed by 4.13 times

The **Islamic Development Bank** pledged to help mobilize funds in the oil-rich Middle East for investing in major infrastructure projects in Indonesia.

The **SABIC** affiliate, **National Industrial Gases Company** signed a SR1.2 billion (US$320 million) Islamic loan agreement with **Banque Saudi Fransi**.

Bahrain Stock Exchange signed a co-operation memorandum of understanding with the **Dubai International Financial Exchange** to develop and strengthen capital markets activity in the region.

First Dawood Islamic Bank chose **System Access**' flagship product SYMBOLS to deliver a world class Islamic banking solution fully compliant with Shariah principles.

Nepline SPV obtained approval from the **Malaysian Securities Commission** on the proposed issuance of RM170 million (US$46.3 million) Sukuk Al-Ijarah.

Al Salam Bank Bahrain posted a net profit of BD4.2 million (US$11.1 million) during the short period since its start of operations.

GFI Group opened a new Islamic banking and finance broking desk in London.

Kuala Lumpur was identified by **Citigroup** as their base for its Islamic banking unit in Asia and will use the Malaysian capital to further strengthen its Islamic banking franchise in the Asia Pacific region.

The **Islamic Development Bank** agreed to grant a US$20-million loan to **Iran Tractor Manufacturing Co**. and **Mehrcam Pars**, a supplier of automotive parts, each.

The **Bahrain Monetary Agency** authorized an Islamic equity fund, sponsored by leading Kuwait based asset management firm, **Global Investment House**.

Oasis Group Holdings, fund manager for Malaysia's first global Islamic equity fund announced it would use its link with **AmInvestment Group** as a base to widen its presence in Asia.

An alliance of Gulf investment institutions, comprising **Venture Capital Bank**, which is an Islamic investment Bank in the Kingdom of Bahrain, and the **Commercial Real Estate Company**, State of Kuwait, was established with the **Caisse De Depot et De Gestion** in the Kingdom of Morocco on the basis of co-operation and partnership.

The board of directors of **EFG-Hermes** accepted the bid made by Dubai based **Abraaj Capital** for the acquisition of 25% of EFG-Hermes

Kenya Commercial Bank launched its Shariah compliant product, dubbed the KCB Amana Account, to address the sensitivities of customers who adhere to the Islamic faith.

Affin Islamic Bank of Malaysia set a target to have nationwide presence in three to four years with new branches opened at a cost of RM500,000 (US$136,000) in addition to its first dedicated outlet in SS2, Petaling Jaya.

Perbadanan Tabung Amanah Islam Brunei introduced a fixed deposit scheme called TAIB Deposit Certificate, in its effort to inculcate saving habits and create awareness of financial planning.

Dubai Islamic Bank launched a unique leadership development program Qiyadi to all the UAE nationals that is meant to identify, develop and hone leadership skills to head the bank's branches in the future.

Dubai Islamic Bank donated Dh5 million (US$1.3 million) in aid to the Lebanese people.

Hong Leong Islamic Bank signed a strategic partnership agreement with **Amanah Raya** to market the latter's Will Writing Service-I. HLIB

** US$ rates were correct at the time the story was first published.*

MIF MALAYSIAN ISLAMIC FINANCE

Malaysia - The International Islamic Financial Centre

Malaysian Islamic Finance - Issuers and Investors Forum 2006

MIF 2006 - HOSTS

Monday 14th and Tuesday 15th, August 2006 at the Mandarin Oriental, Kuala Lumpur witnessed the inaugural Malaysian Islamic Finance – Issuers & Investors Forum 2006. The event was hailed as a success by the deputy governor of Malaysia's Central Bank, among other key industry figures.

MIF 2006, which attracted over 1,000 senior participants, was the Islamic finance industry's largest ever event. Twenty four countries were represented at the forum and 65 of the industry's leading practitioners appeared as panelists. Keynote addresses were made by the governor of Bank Negara Malaysia Dr Zeti Akhtar Aziz, chairman of the Securities Commission Zarinah Anwar, the second deputy minister of finance Dr Awang Adek B. Hussin, secretary-general of IFSB Professor Rifaat Ahmed Abdel Karim, and the deputy governor of Bank Negara Malaysia Mohd Razif Abd Kadir.

In August this year, Islamic Finance events, will host MIF 2007 Issuers & Investors Forum. Following the phenomenal success of the inaugural Malaysian Islamic Finance conference in the corresponding month last year, delegates attending the second event can expect a similar experience – only better. MIF 2007 will focus on Malaysia's role as the dominant and prominent force in Islamic finance. Currently boasting the world's largest Islamic bond market, Malaysia is ideally placed as a launching pad not only to the rest of South East Asia but the Middle East and further a field too.

We will again draw on the experience and expertise of the industry's elite to provide insightful, explorative and thoughtful discussion on the topical areas of Islamic finance today. Delegates will hear from the world's leading practitioners as well as senior government officials from the industry's key participants. Key regulators and associations will again be in full attendance as they were in 2006. Not only those from Malaysia, but from around the globe.

The inaugural forum held during August 2006 was quite categorically the industry's largest ever event. With 65 Panelists, 1,141 Delegates from 24 Countries ascending on Kuala Lumpur. In 2007, with a larger event planned, it is very likely this figure will be surpassed ensuring again that this event will be the largest of its kind during the year.

MIF 2006 - SPONSORS

TAKAFUL SPONSOR

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MIF 2006 - What was said

"This was one of the ***best conferences*** I have attended. Very diverse and a good mix of people attended the event. It was heartening to see a full attendance on both days and till the end of the conference. A great effort by the organizers."
Mohsin Nathani, *Managing Director, Citi Islamic*

"The conference was very ***well attended*** both days and very focused on Islamic investors and issuers primary concerns.
Jean-Marc Riegel, *Assistant General Manager, Chief Corporate Investments & Development, Qatar Islamic Bank*

"MIF now will be a ***must attend*** for those interested in Islamic finance especially for South East Asia."
Dr Omar Marwan Kamal, *Head of Strategic Transactions/Acquisitions, Al Salam Bank*

"I too enjoyed the two day event and I have no doubt the ***overwhelming response*** from participants is good testimony to the success of the conference."
Vaseehar Hassan, *Chairman, RHB Islamic Bank*

"A high quality Islamic finance event that addressed a ***broad array of interesting topics*** and stimulated an interesting exchange of views and perspectives with experienced market practitioners. Prominent industry leaders were represented and provided a unique opportunity to network and cement relationships."
Sohail Jaffer, *Partner, FWU Group*

"I was impressed by the excellent mix of attendees – practitioners, regulators and academics from around the world. The use of ***interactive panels*** to discuss topics of interest was a brilliant change to the standard conference fare of prepared speeches and powerpoint slides."
Arul Kandasamy, *Former Head of Islamic Banking, Calyon*

"The event was ***well organized.*** The panelists and moderators provided valuable insights into Islamic finance from their respective perspective. The forum also provided an opportunity for cross fertilization of ideas."
Jamal Abbas Zaidi, *Chief Executive Officer, Islamic International Rating Agency*

"The event is a unique annual event in the field of Islamic finance which provides a unique opportunity to not only ***meet with the leading figures*** but also share knowledge and expertise in addressing the issues confronted by the industry. Besides the highly interactive mode of communication, which is a departure from traditional forums having dry and lengthy presentations, it ensures a meaningful dialogue between industry experts."
Naseeruddin Ahmad Khan, *Managing Director, Rusd Investment Bank Inc.*

"I walked away anxious to attend more such similar events by this conference organizer. Certainly one of the ***best Islamic banking events*** I have attended. Very beneficial in every aspect."
John A. Sandwick, *Managing Director, Encore Management S.A.*

SEPTEMBER news briefs

The **Islamic Bank of Britain** launched the UK's first Shariah compliant savings account.

Kuwait Finance House sold its KD21.49 million (US$74.31 million) stake in the **Bahraini Islamic Bank**.

The **Dubai International Financial Center** authorized **JPMorgan Chase** to operate out of the center.

OCBC Bank launched the OCBC Treasury Mudharabah Account, a profit-sharing product designed to address the gap in the Islamic treasury products market.

Al Waha Petrochemical Company signed what was thought to be the biggest Islamic financing of a petrochemical project in Saudi Arabia.

Teshkeel Media Group and **Unicorn Investment Bank** completed an agreement whereby Unicorn would underwrite and assist Teshkeel to raise US$25 million via a private placement.

The **Central Bank of Bahrain** granted a license to the **Royal Bank of Scotland** to establish a representative office in the country.

BIMB Holdings announced that the increase in provisions in its banking unit-**Bank Islam Malaysia** - would not exceed RM1.52 billion (US$412.8 million) for the reporting period from December 2005 to September 2006.

Construction firm **Kuala Lumpur Sentral** announced it would sell RM700 million (US$190.22 million) worth of Islamic bonds, with maturities of up to 7 years.

KNM Group said it would increase its annual capacity by 30% by using half of its RM300 million (US$81.54 million) Islamic commercial papers/Islamic medium-term notes to fund its expansion into Brazil and China.

Amanah Raya Unit Trust Management said its first two unit trust funds, one of which is Islamic, would be fully subscribed by the end of the year.

Qatar National Bank was planning on boosting its Sukuk business after the country's first corporate Sukuk, the Qatar Real Estate Investment Company Sukuk, closed four times oversubscribed.

The **Islamic Bank of Britain** was planning its first Scottish branch in Glasgow for 2007.

The Australian **Macquarie Goodman Group** revealed it would purchase UK properties for A$432 million (US$326 million) from **Kuwait Finance House**.

Saudi Investment Bank launched its new Islamic banking program - Alasalah – and opened 10 new Shariah compliant branches in the Kingdom.

Al Baraka Banking Group announced plans to set up branches in India, Indonesia and Malaysia.

PLUS Expressways sold RM675 million (US$183.6 million) of two-part 14-year Shariah compliant zero coupon bonds and RM700 million (US$190.6 million) in 15-year Islamic paper.

Kuwait Finance House Malaysia announced it begin selling Islamic bonds for a Chinese firm in November. The Sukuk was estimated to be between US$200 million and US$250 million, and the first for a company from China.

Dubai Financial Market and **Pakistan's Central Depository Company** signed a memorandum of understanding to enable the two authorities to work together and provide mutual support.

Aseambankers Malaysia revealed it would expand its services to Brunei, Singapore and Indonesia, amongst other regional markets.

The **Islamic Development Bank** and the **African Development Bank** signed a memorandum of understanding on enhancing co-operation between the two institutions.

The US$150 million Musharakah Trust Sukuk for Kuwait's **Investment Dar** was successfully closed by **Unicorn Investment Bank** and **WestLB** London Branch.

First Finance Company said it list its Shariah compliant shares on the **Amman Stock Exchange** with a capital of JD50 million (US$70.6 million).

ABN AMRO Bank's RM350 million (US$95.4 million) Islamic fixed rate bond issue for **RHB Capital** was completed 1.7 times oversubscribed.

Abu Dhabi Investment House and **Qatar Islamic Bank** signed a memorandum of understanding to offer a placement of 66 million shares for US$100 million in Masrafy, the Islamic investment bank for women in Qatar.

State Bank of Pakistan issued a license to **National Bank of Pakistan** for its first Islamic banking branch.

The Kausar Balanced Growth Shariah Fund - Indonesia's first Shariah compliant balanced unit trust fund with partial offshore exposure - was launched by **CIMB Group**.

Malaysia's **Suria Capital Holdings**' unit **Sabah Ports** proposed the issue of RM150 million (US$40.76 million) Islamic securities.

A five-year Sukuk was issued by the **National Industries Company for Building Material** in Kuala Lumpur.

Tamweel made a request to the UAE Central Bank for an Islamic banking license

Bahrain-based **Arcapita Bank** launched a new Islamic venture capital fund - the US$200 million Arcapita Ventures I - the first fund to offer Gulf-based investors access to Islamically approved venture capital investments from the US.

Islamic Development Bank subsidiary **Islamic Corporation for Investment and Export Credit** has issued a US$10 million policy to **Zamil Industrial Investment Company**.

continued...

SEPTEMBER news briefs *(continued...)*

Standard Chartered announced it would expand its Islamic financial services in Pakistan and may open an Islamic unit in the country.

Qatar National Bank and **QNB Al Islami** successfully closed the **Qatar Real Estate Investment Company** Sukuk Al Musharakah.

Arab National Bank implemented a SR500 million (US$133.32 million) Islamic financing agreement to fund the construction of the **Northern Region Cement Factory**.

Brunei was positioning itself as a regional Islamic fund management center.

Ithmaar Bank's profits grew by 104% for the first six months of 2006.

Sarawak Power Generation and **Mukah Power Generation**, both **Sarawak Enterprise Corporation** units, received approval from the Malaysian Securities Commission to issue a RM215 million (US$58.87 million) Sukuk Musharakah program and a RM950 million (US$260.14 million) Sukuk Mudharabah program respectively.

The wealth management division of **Dubai Islamic Bank** launched Shariah compliant 3-year Commodity Linked Individually Capped Performance Notes.

The **International Swaps and Derivatives Association** and the **International Islamic Financial Market** signed a memorandum of understanding in a step towards developing an agreement for documenting privately negotiated Shariah compliant derivatives transactions.

UBS was granted permission to open an office in the **Dubai International Financial Center**.

The **Islamic Development Bank** announced plans to sell a Shariah compliant Malaysian ringgit denominated bond.

Barclays Bank was granted a banking license by the **Qatar Financial Center**.

United International Bank received final approval, to start operations at its headquarters in Bahrain, from the Central Bank.

Qatar Islamic Bank suggested it may issue Lebanon's first Sukuk, with the aim of raising between US$250 million and US$300 million.

Boustead Holdings and **Boustead Properties** jointly planned to establish a RM500 million (US$136 million) Islamic plantation real estate investment trust named **Al-Hadharah Boustead REIT**.

Bank Islam Brunei Darussalam launched the BIBD Investment Certificate.

SHUAA Asset Management launched its first Islamic product - the Arab Islamic Gateway Fund.

Sharjah Islamic Bank announced it would float a long-term Sukuk in the final quarter of 2006 in order to fund its expansion plans.
Commercial Bank International revealed plans to set up an Islamic banking subsidiary by early 2007.

Permodalan Nasional of Malaysia announced it would launch a RM1 billion (US$272.09 million) Islamic real estate investment trust.

The authorities of Mauritania gave authorization to **BNP Paribas** to open a full service bank in Islamic Republic of Mauritania, north-west Africa.

Prime Bank lead arranged the first ever Shariah compliant syndication deal in Bangladesh.

New York-based **Anchor Finance Group** formed a Shariah advisory board to guide the group in its North American and overseas Shariah compliant financing activities.

National Commercial Bank said it would launch an emerging market Islamic fund which will focus on the markets of Brazil, Russia, India, and China.

QNB Al Islami and **BARWA Real Estate Company** signed a QR1 billion (US$274.7 million) Islamic financing agreement to utilize in financing BARWA's real estate investment projects.

Oasis Group Holdings and **AmInvestment Group** were collaborating to promote Islamic capital markets in Asia and Australia.

The **Bahrain Monetary Agency** authorized an Islamic equity fund sponsored by Kuwait-based Islamic investment firm, **First Investment Company**.

Dow Jones Indexes launched Pakistan's first Islamic equity index.

Malaysia's 2007 Budget focused strongly on Islamic banking, with tax incentives to encourage Malaysia to become the leading global Islamic financial hub.

Trade finance group **CCH International**'s wholly owned unit **CCH Europe**, together with Russia's **Globex bank**, approved a US$20 million Shariah compliant Murabahah.

The **Bank of Bahrain and Kuwait** was approved for listing on the **Kuwait Stock Exchange**.

It was announced that two Islamic banks would be operational in Syria by the end of 2007. Namely: **Sham Bank** and **Al-Baraka Bank**

Dubai Islamic Bank successfully closed the Al Islami Shipping Fund.

Maybank posted a 15.3% rise in its pre-tax profit from RM3.49 billion (US$1 billion) for the first half of 2005, to RM4.03 billion (US$1.1 billion) for the same period in 2006.

Oasis International Leasing, **National Central Cooling Company** (Tabreed), and **Gulf International Bank** signed a Dh55 million (US$15 million) Islamic Ijarah facility. tioning.

AREF Investment Group appointed **ABC Islamic Bank** and **Standard Chartered** to arrange and underwrite a US$100 million, 3-year revolving Murabahah financing facility.

Qatar National Bank received approval to set up a representative office in the Libya.

** US$ rates were correct at the time the story was first published.*

OCTOBER news briefs

The **Export Development Canada** and the **Islamic Corporation for the Insurance of Investment and Export Credit** signed a Memorandum of Understanding to help the former build a closer relationship with Islamic financial institutions.

National Australia Bank revealed its plan to introduce Islamic financing into its product range.

Maybank Singapore announces it would introduce Islamic banking initiatives before the end of 2006 as part of its diversification strategy.

The **Central Bank of Bahrain** granted a license to Zurich-based global private banking group **EFG International** to launch a representative office in Bahrain.

Lembaga Tabung Haji said it would begin investing in overseas equities, with an allocation of up to RM500 million (US$136.24 million) for 2007, in order to provide higher returns to its depositors.

Palm District Cooling secured a three-year US$50 million Islamic finance facility from the **Dubai Islamic Bank** in order to fund its ambitious expansion plans.

Al Salam was granted a license to launch an Islamic bank in Algeria with a paid-up capital of US$100 million.

Shape Finance Corporation was appointed as Shariah advisor for the world's first GCC-oriented, open-ended Sukuk fund – the **Sanad Sukuk Fund**.

Sharjah Islamic Bank revealed net profits of Dh143.5 million (US$39.07 million) for the first nine months of 2006, up from Dh143.6 million (US$39.1 million) the previous year.

Qatar International Islamic Bank announced profits of QR285.5 million (US$78.43 million) for the first nine months of 2006.

The **Government of Dubai** confirmed it would purchase a 50% stake in the **National Bonds Corporation** through its investment arm, **Investment Corporation of Dubai**.

Kazakhstan's **TuranAlem bank** claimed it would consider Islamic funding once it had accumulated the sufficient understanding and experience.

Sharjah Islamic Bank successfully closed its global Sukuk – the first rated Sukuk issued by a GCC institution – at US$225 million.

Albaraka Banking Group and **Emirates Islamic Bank** signed an agreement to strengthen their existing relationship of co-operation and enable both banks to provide more integrated Islamic financial services.

The **Dubai Financial Services Authority** licensed its 100th regulated firm in the **Dubai International Finance Center**.

Pearl Real Estate Development Company agreed upon a collaboration with Bahrain-based **Reef Real Estate Company** to provide Shariah compliant mortgage financing to buyers in the BD95 million (US$250 million) Abraj Al Lulu development.

Abu Dhabi Commercial Bank launched a new fund, the Meethaq Mudarabah Investment Program, to invest customer's funds in a broad range of Shariah compliant assets.

A US$150 million Sukuk created by **The Investment Dar Company** was listed on the **Dubai International Financial Exchange**.

Lembaga Tabung Haji and **Dubai Investment Group** both finalized their purchases of 49% and 9% stakes respectively in **Bank Islam Malaysia**.

Abu Dhabi Islamic Bank revealed that for the first nine months of 2006 the bank made a net profit after distribution to depositors of Dh405 million (US$110.26 million).

International Islamic revealed plans to launch another Asian-based entity with a capital base of US$100 million by the first quarter of 2007, forming part of its strategy to have a pan-global presence.

The third quarter of 2006 brought net profits of QR728.3 million (US$200.06 million) to **Qatar Islamic Bank**.

Africa's **Standard Bank** announced plans to launch a fund to invest in Iranian stocks, having received significant investor interest in such shares.

RHB Sakura Merchant Bankers was renamed **RHB Investment Bank**.

Kuwait Finance House Bahrain appointed software and processing solutions company **SunGard** to introduce a new risk management technology platform for the bank.

Qatar Real Estate Investment Company signed a US$105 million Murabahah facility with **HSBC** and **Masraf Al Rayan**.

Mobile Telecommunication Company – Kuwait's leading mobile operator – authorized a group of banks to provide a US$750 million syndicated Murabahah.

Malaysia's **Securities Commission** approved the proposed RM100 million (US$27.13 million) Islamic debt issue by **Boon Koon**.

The **Reserve Bank of India** said that India is still not ready for Islamic banking.

Dubai Islamic Bank successfully closed its three-year Commodity Linked Individually Capped Performance Notes. The notes received an overwhelming response, collecting a record US$38 million in four weeks.

UBS announced plans to launch the first Islamic fund linked to commodity prices. The product is to be related to copper, nickel and oil prices.

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OCTOBER news briefs *(continued...)*

Boeing Capital Corporation's regional director, Nadim Fattaleh, suggested that using aircraft, as opposed to real estate, to back Sukuk is highly likely.

Al Manal Development and **Emirates Islamic Bank** signed a memorandum of understanding to provide mortgage finance to customers wanting to purchase property in Al Manal Development's Dh300 million (US$81.69 million) flagship venture.

Bahrain Islamic Bank posted a net profit of BD9.7 million (US$25.73 million) in the third quarter of 2006, an 88% increase on 2005.

Dubai-based investment house **Istithmar** purchased the landmark W Hotel Union Square, a luxury hotel in Manhattan, New York valued at US$285 million.

Aldar Properties proposed to borrow up to US$4 billion to fund projects in the UAE and abroad.

Khazanah Nasional's US$750 million Islamic exchangeable Sukuk issuance was listed on the Labuan Financial Exchange.

Bahrain Islamic Bank and the **Jordan Permanent Exhibition** signed a memorandum of understanding as part of the Tas'heel Personal Finance Scheme, which is to provide Shariah compliant credit facilities to everyone planning a travel to Jordan for medical treatment or to join an educational program.

Jeffries International won a license from the **Dubai Financial Services Authority** to operate as an authorized firm from the **Dubai International Financial Center**.

The **Central Bank of Indonesia** set up new regulations to boost Islamic banking following an increased demand for such products in Indonesia.

Scomi Group's 92.5%-owned **KMCOB Capital** received approval from the Securities Commission of Malaysia to issue RM630 million (US$170.59 million) of Islamic debt notes.

Bahrain Islamic Bank revealed it would double its capital base to almost US$400 million.

Fitch Ratings announced its plans to purchase an equity stake in **Malaysian Rating Corporation**.

The **Qatar Islamic Insurance Company** and **Qatar International Islamic Bank** launched the new **Tasheelat Company**.

Pakistan's **Bank Alfalah** revealed its plans to launch a fully fledged Islamic bank.

RHB Islamic Bank said it was considering setting up an international Islamic banking unit to tap the potential for Middle Eastern investors in search of quality assets.

Bank of Tokyo Mitsubishi UFJ and Malaysia's **CIMB Group** announced they would work together to launch Islamic financing operations and provide investment banking services for Japanese companies operating in Malaysia.

Dubai Islamic Bank's investment banking subsidiary, **Millennium Finance Corporate** advised **Anzon Energy** regarding the issue of US$75 million worth of shares, bonds, and convertible bonds to **Ras Al Khaimah Petroleum**.

Yemen's **SabaFon Telecommunications** signed an Islamic Murabahah financing agreement for US$50 million with **HSBC**.

Indian information technology company **Infosys** won its first contract from a Saudi bank, **Arab National Bank**, for its Islamic banking solution.

Bank Negara Malaysia granted approval to **Kuwait Finance House Malaysia** for a financial management product – KFH Ijarah Rental Swap-I – a risk management tool suitable for customers with Ijarah financing arrangements that are either subject to fluctuations of the reference rates such as cost of funds, or fixed over the Ijarah or lease facility period.

Faisal Private Bank of Switzerland was awarded a full banking license by the Swiss Federal Banking Commission, making it the first Islamic private bank in Switzerland.

Emaar Properties announced it would raise US$1 billion through a five-year Musharakah Islamic syndication.

Calyx Financial formed a Shariah supervisory board for its Calyx Islamic Strategist program. The board is: Sheikh Yusuf Talal Delorenzo, Dr Mohd Daud Bakar and Sheikh Nizam M. S. Yaquby.

The **Syrian International Islamic Bank** said it would place up to 51% of its capital shares for underwriting by Syrian citizens.

Qatar International Islamic Bank was approached by the US Federal Reserve to operate in the USA, and was said to be investigating the possibilities.

A memorandum of understanding was signed by Indonesia and Qatar on the establishment of the Qatar Trust Fund, which hopes to collect up to US$1 billion in funds.

Global Investment House launched a GCC Islamic Index, as part of a series of indices.

Al Rayan Bank opened its office in the Al Sadd area of Doha.

Tadhamon International Islamic Bank's first half profits for 2006 revealed a 90% year-on-year increase to YR7.2 billion (US$36.7 million).

The board of executive directors of the **Islamic Development Bank** approved US$705.9 million in project financing and trade operations.

The **Islamic Development Bank** approved a sum of US$347,000 for their share of the increase of the capital of the **International Islamic Rating Agency** in Bahrain.

Tamweel opened its first branch in Abu Dhabi, offering the company's entire range of Shariah compliant home finance products and services through professionally trained mortgage advisors.

** US$ rates were correct at the time the story was first published.*

NOVEMBER news briefs

OCBC successfully placed its first Mudarabah bonds to raise RM200 million (US$55.16 million).

The **National Bank of Abu Dhabi** launched two indices – the NBAD UAE-listed Islamic Index and the NBAD UAE Islamic Index, allowing investors to gauge the performance of their investments against the collective movement of Shariah compliant stock prices.

Ceylinco, along with **Malaysia's Central Bank** and Malaysia's **International Center for Education in Islamic Finance**, set up a faculty for Islamic financial studies in Sri Lanka.

Citigroup Asia's head of Islamic banking, Rafe Haneef, urged the development of Islamic hedging products for Islamic institutions and Muslim individuals in order to minimize investment risks.

Boustead real estate investment trust was given the green light to set up the Al Hadarah Boustead REIT by the Malaysian **Securities Commission**.

Sharjah announced plans to raise, through **Sharjah Islamic Bank**, a US$350 million Sukuk via a Sukuk Al Ijarah facility.

Emirates Islamic Bank began operations in Khorfakkan, in line with expanding its geographical reach.

The **Central Bank of Bahrain** announced the oversubscription of the monthly issue of Sukuk Al Ijar by 110%.

Governor of the **Dubai International Financial Centre**, Dr Omar Bin Sulaiman, met with Takuma Hatano, the ambassador of Japan to the UAE, and Hiroyasu Kobayashi, consul general of Japan, reaffirming Japanese ties with Dubai.

Maybank's third quarter pre-tax profit of RM881 million (US$242.8 million) was 7% lower than the corresponding period the previous year.

RHB Capital increased its net profit 29.33% to RM102.34 million (US$28.2 million), up from 2005's RM79.13 million (US$21.8 million).

Standard Chartered revealed plans to expand its geographical reach by introducing more innovative products and focusing on SME's and Islamic banking.

House Building Finance Corporation, Pakistan's oldest housing finance institute, applied for an Islamic commercial banking license.

Qatar National Bank and **Gulf International Bank** extended a QR335 million (US$92 million) loan to Qatar Navigation. The loan is to enable **Qatar Navigation** to finance the construction of a 52-storey tower in the West Bay Area of Doha.

Bank Islam and **Bank Muamalat** signed an agreement to execute a derivative master agreement to document Islamic derivative transactions.

Citigroup was appointed lead manager and sole arranger for the launch of **Emaar**'s US$1 billion Musharakah Islamic syndication.

US-based **Shariah Capital** successfully procured a private placement capital raise.

A €200 million (US$256.46 million) Sukuk, the first Islamic bond transferable into capital covered by European income-generating properties, was issued by **Qatar Islamic Bank**.

Dubai Islamic Bank was ready to issue US$10 billion in Sukuk to European and US companies from the oil and gas, infrastructure and telecommunication sectors.

Dubai Islamic Bank was in talks with Australia's **Anzon Energy** and **Aabar Petroleum** to advocate investment in Middle East and African oilfields.

Abu Dhabi Islamic Bank was to embark on a European road show for a five-year dollar-denominated Sukuk under the bank's US$5 billion medium-term notes program.

Abu Dhabi Commercial Bank and **Gulf International Bank** led a US$104 million term loan facility signing with Star Cement, part of the **ETA/Star Group**.

Dubai Islamic Bank launched a Shariah compliant investment product – the DIB investment note. The note has a 3-year protected capital, with a minimum investment of US$10,000.

Saudi Investment Bank declared its profits had surged to more than SR1.705 billion (US$454.6 million), which is 119.6% more than the previous year's.

Malakoff's single largest shareholder, **MMC**, announced plans to raise RM7.9 billion (US$2.17 billion) in Islamic debt papers to buy out its parent company.

Basell and **Sahara Petrochemical Company**'s joint venture – **Al-Waha Petrochemical Company** –signed up for Shariah compliant financing.

The **National Bank of Kuwait** launched an Islamic European Real Estate Fund compliant with Shariah regulations.

Millennium Finance, a unit of the **Dubai Islamic Bank** announced the launch of two US$1 billion private equity funds.

Amlak Finance and **Dallah Al Baraka** set up the **Amlak International Company** with an investment of US$266.6 million.

The **Islamic Development Bank** announced plans to set up an Islamic investment company in Azerbaijan.

The **Islamic Finance Qualification**, the world's first global benchmark qualification for Islamic finance, was launched in London.

The US$2.5 billion **Nakheel Group** Sukuk was launched. **Dubai Islamic Bank** and **Barclays Capital** were the joint lead underwriters and book runners.

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NOVEMBER news briefs *(continued...)*

Unicorn Investment Bank announced strong profits of US$34.9 million.

Pakistan's second largest gas company **Sui Southern Gas Co**. issued PKR1 billion (US$16.6 million) five-year Islamic bonds.

A 3-year US$100 million Standby Commodity Murabahah financing facility was launched by **Gulf Finance House**.

Standard Chartered recently executed a US$150 million 3-year profit rate swap deal with Kuwait-based **Aref Investment Group** allowing both parties to exchange a series of profit payments in a single currency for another series of payments in the same currency.

Bahrain Islamic Bank revealed it was keen to acquire an interest in Cairo-based **Arab Investment Bank**.

Aldar Properties was seeking approval from the UAE Ministry of Economics to issue an Islamic bond and/or debentures early in 2007.

The world's first GCC open-ended Sukuk, **Sanad Sukuk**, fund launched in Zurich.

Dubai Islamic Bank announced a Shariah compliant 3-year capital protected Dubai Financial Market note.

Qatar Islamic Bank launched the **Islamic Investment Bank of Qatar.**

Saudi Aramco and Co**nocoPhillip**s were planning a US$1 billion Sukuk to finance construction of a refinery in Jubail. **Riyad Bank** was appointed advisor.

Microlink Solutions Malaysia became a **Capability Maturity Model Integration Framework** Level 3 company becoming part of an influential group of organizations worldwide that have proven and sustainable process management for their products and services.

Qatar Islamic Bank announced plans to expand its Asian operations by opening offices in Indonesia, Singapore and Brunei.

A new investment fund launched by **Qatar National Bank** called Al Watani 4 was fully subscribed to the amount of QR2.2 billion (US$604.2 million).

The **Qatari Awqaf Authority** was launched in order to take over the activities of the Awqaf department at the Qatari Ministry of Awqaf and Islamic.

State Bank of Pakistan governor, Dr Shamshad Akhtar, disclosed that the Central Bank had submitted a scheme to launch a Shariah compliant Baitul-Mal Sukuk to the Ministry of Finance.

New rules were established in Bahrain to eliminate the double payment of stamp duty on Shariah compliant Islamic mortgages.

Malaysia's first absolute benchmark Islamic fund was launched by **Pheim Unit Trusts** – the Pheim Asia ex-Japan Islamic fund.

Prudential was granted a license from the **Dubai Financial Services Authority** to operate as an authorized firm from the **Dubai International Financial Center**.
Bahrain and Luxembourg signed an agreement to promote foreign investment between the two countries.

The establishment of the largest asset management company in Malaysia was agreed upon between **CIMB Group** and the **Principal Financial Group**.

CIMB Islamic announced it desire to be the financial advisor for the Indonesian government when it issues national and international Shariah bonds in 2007.

The list of Shariah compliant securities held by **Malaysia's Securities Commission** increased to 886 with the addition of 33 newly compliant securities.

Britain was poised to become the first western country to introduce a regulatory regime to support the domestic issuance of Sukuk.

A QR365 million (US$100.26 million) contract was signed by **Qatar Islamic Bank** for the financing of the "Silhouette" Tower project in the West Bay.

It was announced that the soon-to-be opened **Eamar International Bank** would be launched with a capital of US$1 billion.

BIMB Holdings began an internal reshuffle to turn the company around. Its financial year ended on the 30th June 2006 revealed a loss of RM1.230 billion (US$336.8 million).

The **Bahrain Institute of Banking and Finance** was appointed as the "executive manager" of the Waqf Fund board of trustees.

Injazat Capital, the first investment firm to offer an Islamic venture capital fund worldwide, was officially launched.

Emirates Bank International revealed plans to open a representative office in Singapore in December making it the first UAE bank to establish a presence in the city state.

Gulf Finance House saw a 90% rise in its cumulative net profit for the first nine months of 2006, posting a profit of US$176 million, as against US$92 million the previous year.

Tamweel announced a US$217.3 million profit for first nine months of 2006. Its Islamic financing and investing activities rose to US$24.2 million during the nine months period, registering a 215% increase, as compared to the US$7.6 million in 2005.

Khaleej Finance and Investment launched Optimum, a US$50 million Shariah compliant capital protected fund comprised of Dow Jones Islamic equity index, crude oil and copper.

Almari, the largest Gulf Arab dairy firm, was contemplating an Islamic bond issue to help finance a SR4 billion (US$1.06 billion) expansion, funding investments and the development of new products.

Aseambankers Malaysia announced its plans to go international with its Islamic capital markets services with the Middle East, Indonesia and Europe all in sight.

** US$ rates were correct at the time the story was first published.*

DECEMBER news briefs

Bank Indonesia launched a program to accelerate the development of Indonesia's Islamic banking sector. The program, based on four main strategies, includes promoting supply and demand, strengthening the Shariah banking system in terms of capitalization and management, optimizing the functions of government and inducting all the stakeholders in the Shariah banking sector into the program.

Global Investment House's Shariah compliant Global Asia Real Estate Fund, together with a Kuwaiti partner won the bid to acquire a distressed asset in China. The asset, located in north-east China's Dalian Economic and Technological Development Area, possesses a value of US$32 million.

UAE developer **Aldar Properties** announced plans to sell US$3.5 billion in Sukuk in the first quarter of 2007.

Dexia Asset Management opened an office in Bahrain which will service Lebanon, Jordan, Egypt and the GCC region.

It was announced that a US$200 million **Sukuk Exchange Center** will be set up in Bahrain by early 2007 in order to create new Islamic investment and financial tools to support and contribute liquidity in the Islamic capital and investment markets.

The **State Bank of Pakistan** granted permission for Islamic banks to invest in the share market under regulated conditions.

Singapore's **CapitaLand** announced it will set up a US$630 million Shariah compliant real estate fund, investing in Bahrain's prime waterfront development – Bahrain Bay.

Gulf Finance House completed a US$300 million, three year tenor, Shariah compliant international credit facility in London supported by 30 banks.

HSBC Amanah was awarded the sole lead manager and book runner role for the Abu Dhabi Islamic Bank's US$800 million, five-year Sukuk debut.

Al Rajhi Bank announced plans to establish up to 50 branches in Malaysia.

The European Islamic Investment Bank launched its Shariah compliant real estate fund, mandating **Knight Frank Investment Management** as property fund advisor.

ABC Islamic Bank, **Arab Bank**, **Calyon**, **Gulf International Bank**, **Kuwait Finance House**, and the **National Bank of Abu Dhabi** acted as mandated lead arrangers for the US$1.2 billion Murabahah facility for **Mobile Telecommunications Company**.

Qatar National Bank was granted a full banking license by the **Central Bank of Kuwait**.

The **McKinsey Competitiveness Report 2006** suggested Islamic finance players should focus on large-scale and lucrative activities to strengthen their position in wholesale banking. The development and re-enforcement of risk management and front-end excellence is also vital in determining the continued growth of the Islamic industry

Pakistan's Central Bank permitted the establishment of fully fledged Islamic micro-finance facilities across the country.

Dubai Islamic Bank launched the Shariah compliant Al Islami Land Trading Finance for UAE nationals purchasing land.

The **Dubai Financial Exchange** and the **Dubai Financial Market** were in talks to align their activities, which may entail allowing dual listing.

Injazat Capital's US$50m Islamic Technology Fund bought a 19% stake in international IT services provider **Atos Origin Middle East**.

Bank Abilad was appointed by **Jabal Omar Development Company** to manage the company's SR2.014 billion (US$537.05 million) initial public offering.

TAIB Bank launched its Shariah compliant company **Acacia Real Estate BVI**, worth US$500 million.

The **Arab Banking Corporation** successfully closed **United Stainless Steel Company**'s US$153 million syndicated debt financing facility.

Deutsche Bank announced its first Shariah compliant mutual fund capability via its global subsidiary **DWS Investments**.

Gulf Finance House revealed plans to invest at least US$1 billion in China and increase its US$2 billion investment in India by two to threefold.

Malaysia's Central Bank and **Bursa Malaysia** announced it will be implementing commodity Murabahah banking products with crude palm oil as the base transaction tool. This first-of-a-kind product is expected to be available in early 2007.

Calyx Financial announced it will market its new Shariah compliant investment vehicle, the Calyx Islamic Strategist Fund, to South-East Asian clients.

The **State Bank of Pakistan** stated it will soon issue a set of guidelines for Islamic banks called the Shariah Compliant Framework.

Citigroup estimated Singapore has a Sukuk market worth US$300 to US$350 billion with a growth rate of 15%.

Dubai Islamic Bank suggested it was considering Malaysia for its Asian regional hub.

SABIC Europe BV, the European subsidiary of **Saudi Basic Industries Corporation**, appointed **HSBC** as acting joint lead manager and bookrunner to raise €2 billion (US$2.65 billion) in debt.

Liquidity Management Center launched a Musharakah Sukuk worth US$125 million for **Lagoon City**. The Sukuk will have a five-year tenor.

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DECEMBER news briefs *(continued...)*

The **Islamic Financial Services Board** admitted 16 new members, including the **Securities Commission of Malaysia** and the **Capital Market Authority of Saudi Arabia**. Eleven others were inducted as observer members, including the **Insurance Commission of Jordan**, **Hong Kong Monetary Authority** and **Central Bank of Morocco**. The **Asian Development Bank**'s status was upgraded from observer member to associate member.

Eurohypo, the German mortgage lender, announced plans to expand its property financing deals with Gulf investors via Shariah compliance.

Bank of Bahrain and Kuwait, together with **Shamil Bank**, launched their 50–50 Shariah compliant mortgage financing company joint venture, **Sakana Holistic Housing Solutions**.

The **Central Bank of Bahrain** announced the oversubscription of its monthly Sukuk Al Salam Islamic bonds by 178 times. Subscriptions worth US$71 million, with a maturity of 91 days, were received for the US$40 million issue.

The **Dubai Financial Market General Index**, which was launched on the 3rd December 2006, lost 3.31% on its first day. All 16 traded shares reported losses.

Arab Banking Corporation and the National Oil Corporation of Libya signed an MoU appointing the bank as financial advisor to specific NOC projects.

The Washington DC-based **Carlyle Group** announced it will conduct private equity investments in the Middle East and North Africa, having formed a new team for the purpose.

Emirates Islamic Bank revealed its plans to expand its Shariah compliant Islamic investment products in the future, including the Emirates Real Estate Fund.

Abu Dhabi Islamic Bank raised US$800 million from its Sukuk debut, with almost 40% of the investors coming from Europe.

Dubai World's investment subsidiary **Istithmar** acquired a stake in Canada's **GPS Industries**.

Al Amanah Islamic Investment Bank of the Philippines was informed it needed to comply with its charter's regulations and establish partnerships with international Islamic institutions to gain privatization.

Halal Industry Development teamed up with the **Islamic Chamber of Commerce** and Industry with the hope to dominate the world's halal market.

Dubai Bank, 30% owned by **Emaar** and 70% by **Dubai Holdings**, said it expects to double its capital to a proposed Dh1 billion (US$272.3 million) to facilitate expansion.

China Resources, along with **Al Rajhi Investments**, announced it would introduce Shariah compliant investments to the Chinese market through the Shariah Investment Fund.

Saudi Arabia was set to become **Citigroup**'s largest asset provider with 20% of the bank's Middle Eastern clients being based in the Kingdom.

Aldar Properties revealed plans to develop a master-planned community in Al Yas Island with US$40 billion worth of investment.

Alam Maritim, a Malaysian oil and gas services firm, were in talks to raise RM600 million (US$165.94 million) worth of Islamic bonds.

The **National Bank of Abu Dhabi** was awaiting approval to launch its first Islamic finance company.

Citigroup launched the Murabahah Deposit-i in Malaysia. **Kuwait Finance House** Malaysia was Citibank's first currency Commodity Murabahah interbank counterparty.

BumiGas Energi of Indonesia announced plans to raise US$308 million through the sale of Shariah compliant bonds to finance the building of two geothermal power plants.

Deputy chief executive officer of **Kuwait Finance House Malaysia**, Jamelah Jamaluddin, urged Malaysian Islamic finance players to branch out to promote and market initiatives of Islamic financial products, especially to the Middle East.

Affin Holdings recorded a pre-tax profit of RM54.37 million (US$15.03 million) in its third quarter – RM53.47 million (US$15.03 million) lower than the previous year.

The group's revenue, however, rose to RM543.52 million (US$150.34 million) from RM447.85 million (US$123.88 million) in the same quarter in 2005.

Injazat Technology Fund signed an investment deal with telecom solutions manufacturer **Broadlink Research**. Shariah compliant Injazat Capital's private equity fund aims to mobilize financial and strategic business support, maximize investor returns, reduce risk and propel Broadlink and similar companies' participation in the regional ICT market.

Dubai Financial Market's Dh1.6 billion (US$435 million) initial public offering was oversubscribed by 300 times. It closed on the 23rd November 2006 with a return of US$52.6 billion. 45% of the shares were open to Dubai government-related companies and employees, with the remaining 55% available to UAE, GCC nationals, foreigners and institutions.

Malaysian Rating Corporation said it expected to see an increasing demand for Sukuk and Islamic securitization in both the Malaysian and the global Islamic bond market. Vice-president of MARC, Hafizan Haron, is confident that Malaysia has the talent, resources and market infrastructure to be a key Sukuk player.

** US$ rates were correct at the time the story was first published.*

Global Takaful Review for 2006

By Sohail Jaffer

Takaful industry growth

The renaissance in socially responsible investing (SRI) and the demand for Shariah compliant solutions has spurred the double-digit growth of the global demand for Islamic insurance, or Takaful. Moody's Special Comment – entitled Takaful: *A Market with Great Potential* – in August 2006 indicated that "Takaful or Islamic insurance has shown very impressive premium growth rates of about 20% in recent years. The first Takaful company was established in 1979 and now there are over 250 globally. Total Takaful premiums exceeded US$2 billion in 2005, and are expected to reach US$7.4 billion by 2015". The nascent Takaful industry needs to gain critical mass, provide an array of innovative products and superior quality customer services, build worldwide brand recognition and exceed the performance standards set by the conventional insurance industry.

Takaful product innovation and distribution

The Takaful product family spans across the general, life, health and pensions business lines. According to a report from the Salama Islamic Arab Insurance Company, "Approximately 52% of the projected total annual Takaful premiums would be non-life with an impressive gain with life/family Takaful segment increasing to US$4.9 billion."

Due to the ethical guidelines underpinning Islamic financial services, the increasing transparency of customer terms and conditions, the pricing structure, regular compliance monitoring by the relevant Shariah boards and supervisory regulators and adequate disclosure of information and transparency to policyholders, such offerings have tended to attract both Muslim and non-Muslim customers. Acceptance of Islamic savings, education, marriage and retirement plans is gradually increasing among the affluent customer base, but significant investment in customer education and training of financial planners and investment advisors is required. A successful distribution model needs to develop a thorough understanding of customers' needs; offer product and process innovation; eliminate flaws in product terms and cost structures; and enhance customer service delivery.

Creative product design and packaging, customer convenience and transparency of product terms, conditions and pricing are key to gaining a competitive advantage across general, life, health and pensions business and multiple distribution channels. The Takaful industry has been successful in distributing products through its agency sales force, direct channel, e-commerce and to a limited extent via certain retail banks. Business skills and successful distribution models need to be crafted and redeployed intelligently in the development of new markets. Use of web-based point of sale and online administration systems and the enlightened deployment of e-commerce can optimize customer interface, relationship management and effective after-sales customer service. Major Takaful operators need to enhance their capacity to innovate, carefully review and understand evolving customer and market-specific needs, carefully reengineer their product design and customer benefits package, strengthen customer education and interaction and expand customer reach across multiple distribution channels.

"Approximately 52% of the projected total annual Takaful premiums would be non-life with an impressive gain with life/family Takaful segment increasing to US$4.9 billion"

Advent of Bancassurance

In light of the exponential growth of Islamic retail banking, several enterprising banks have sought to diversify their business by including bancassurance in their product offerings (for example, Prudential and Bank Simpanan Nasional launched a joint venture – Prudential BSN Takaful – in August 2006 in Malaysia to offer a range of Takaful savings, protection and investment products through the bank's network of branches). Hence, Islamic savings, education, marriage and retirement plans that combine investments with protection benefits are starting to become attractive. The average maturity of such capital accumulation plans is between 15 and 20 years and the customer retention period in good performing programs is much longer than direct investments in mutual funds.

Product customization for the different bank channels (retail, mass affluent, private banking), customer referrals and gaining brand loyalty are important critical success factors. Banks are keen to work with strategic product partners who offer a bespoke family Takaful investment-linked program, the opportunity to "white label" such a program and open investment architecture. Clearly the ability to tailor suitably

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Global Takaful Review for 2006 *(continued...)*

diversified risk–reward investment portfolios, select top quartile performing funds from major international brands and control defined portfolio risk levels are powerful drivers for the retail value proposition. Furthermore, product certification by an independent Shariah board of experts and ongoing compliance monitoring with high ethical standards has favorably impacted transparency, disclosure of different terms and conditions, charges and frequency of reporting.

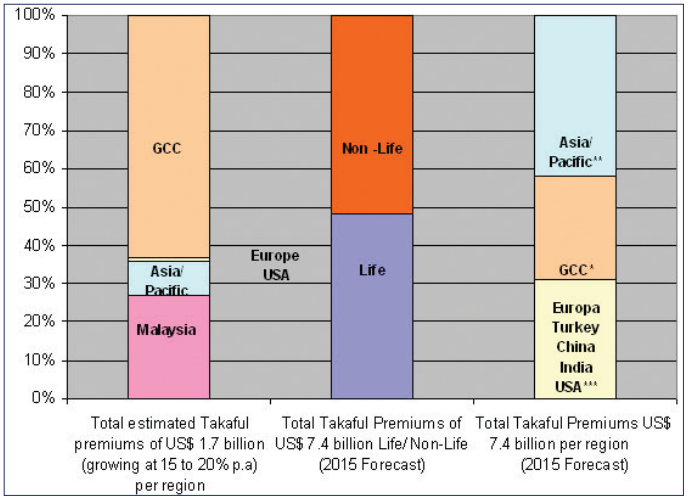
Bank distribution partners generally prefer a "white label" family Takaful-linked investment plan for the following reasons:

- Customers are more comfortable with a bank's "own brand" equity.
- Banks can blend their own Islamic mutual funds with quality third party Shariah compliant funds.
- All customer assets of the family Takaful-linked investment business are in the bank's custody and it also gains the corporate bank account of the life insurance company supplying the product.
- Banks have access to the web-based point-of-sale and online administration system without having to integrate new systems or build new interfaces.
- Due to the life cycle nature of the product, banks enhance customer relationships and retention rate.

The distribution of Takaful life and savings products through bank channels is relatively new, but the sales process through the branch banking network has been facilitated by the advent of web-based point-of-sale and online administration systems. Abu Dhabi Commercial Bank (ADCB) has introduced a Shariah compliant Takaful and savings scheme in joint arrangement with Dubai Islamic Insurance and Reinsurance Company and FWU Group. ADCB's Meethaq Takaful and Savings Program offers investment-oriented life Takaful products to UAE residents. In addition to the benefits of customer convenience, the "white label" advantage of using own brand equity, transparency of product terms and conditions, open investment architecture and efficient online processing have all proved attractive to major bank distribution partners.

2006 Takaful industry highlights

Salama Islamic Arab Insurance Company's report looking ahead to 2006 stated that: "nearly US$2 billion in annual premiums would be written in GCC markets, US$3.1 billion written in the Asia-Pacific region, and an additional US$2.6 billion in Europe, Turkey, China, India and the US." Major markets include Malaysia and Indonesia, Saudi Arabia and



*GCC US$2 billion (Saudi Arabia US$900 million, UAE US$480 million and Egypt US$467 million).
**Asia-Pacific US$3.1 billion (Malaysia/Indonesia US$1.4 billion).
***Europe, Turkey, China, India and the US US$2.3 billion.
Source: Shuaa Capital

other GCC countries, Pakistan and Iran. Both Europe and the US also offer considerable untapped potential for the Takaful industry.

Growth in the Middle East

Currently, insurance penetration and per capita density in the GCC states are both low. However, the GCC will see a dramatic increase in insurance in general and especially in Takaful over the coming years. According to the report by Salama Islamic Arab Insurance Company: "The Saudi market within the GCC has attracted several new market entrants and liberalization of foreign ownership in the UAE and other markets in the insurance sector will further accelerate growth. Among the GCC states, Saudi Arabia is expected to generate close to US$900 million in premiums, followed by the UAE (US$480 million) and Egypt (US$467 million)." This growth is spurred by the introduction of "compulsory health insurance for expatriates from the 1st January 2006 and motor third party liability in Saudi Arabia" and "compulsory health insurance for foreigners" in the UAE.

The Kingdom of Saudi Arabia in particular will see the rise: the Jeddah Chamber of Commerce believes the insurance market will triple from SR8 billion (US$2.13 billion) to SR24 billion (US$6.4 billion) within the next decade. Insurance currently contributes 0.7% of the GDP; this is expected to reach 3.7% in five years. In October 2006, the Council of Ministers in the Kingdom of Saudi Arabia licensed 13 new insurance companies: Gulf Union Co-operative Insurance, Arabian Shield Insurance, Sanad for Co-operative Insurance, Saudi United Co-operative Insurance, Assurance Saudi

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Global Takaful Review for 2006 *(continued...)*

Fransi, Al-Ahlia Insurance, Mediterranean and Gulf Insurance and Reinsurance, Malath Insurance, Saudi Indian Insurance, Saudi IAIC, Allied Co-operative Insurance Group, SABB Takaful and Saudi Arabian Insurance. Most of the new licensed insurance companies are joint ventures with foreign insurance companies (for example SABB Takaful, which was recently licensed to undertake insurance business in Saudi Arabia, is a joint venture insurance company with 32.5% owned by SABB, 32.5% owned by subsidiaries of the HSBC Group, and the balance owned by the public by way of an initial public offering). Applications from a further 18 companies are at different stages of evaluation. These include Al-Alamiya Insurance, AXA Co-operative Insurance, BUPA Arabia, Tokio Marine and Nichido and United Co-operative Assurance (UCA).

In the UAE, Takaful is an area that has seen tremendous growth, particularly in the real estate and home finance market. High service standards, product innovation and the delivery of competitive propositions have contributed to this growth. For example, Tamweel's recent Yusr product is a Shariah compliant adjustable repayment mortgage finance that allows customers to make lower monthly repayments in the initial years and amortize the difference over the remaining years of the repayment period. The expansion of the Shariah compliant home finance market has also contributed to the growth of Takaful mortgage protection products, with Aman Insurance taking the lead in this particular product line within the UAE.

In Bahrain, American Insurance Group (AIG) recently launched a regional Takaful company, AIG Takaful, with a capital of US$15 million, which provides a range of Takaful products including accident and health, motor, personal contents property and casualty insurance. AIG Takaful will offer its products in the Middle East initially, expanding into South-East Asia in 2007 and later to the UK and North America.

In Syria, the Insurance Supervisory Committee granted approval in principle to the Syrian Qatari Insurance Company, the Nour Insurance Company and Al Aqila Insurance Company to provide Islamic insurance in an emerging market estimated at US$500 million.

Pakistan

The Securities Exchange Commission of Pakistan (SECP) introduced a comprehensive Takaful regulatory framework in 2005. As a result, in the same year Takaful Nasional of Malaysia entered into a joint venture agreement with Pak Kuwait Investment Company (Private) (PKIC) to establish the first Takaful company in Pakistan – to be known as Pak-Kuwait Takaful Company. The shareholders of Pak-Kuwait Takaful Company are PKIC (30%), Takaful Nasional (25%), Meezan Bank (10%) and other shareholders 35%. PKIC provides the infrastructure and human capital, Takaful Nasional provides the technical expertise and Meezan Bank, as Pakistan's first fully fledged commercial bank dedicated to Islamic banking, provides the distribution channel.

"The nascent Takaful industry needs to gain critical mass, provide an array of innovative products and superior quality customer services, build worldwide brand recognition and exceed the performance standards set by the conventional insurance industry"

Qatar Islamic Insurance Company (QIIC) and Qatar International Islamic Bank (QIIB) together with Pakistani nationals (residents and non-residents) and strategic investors plan to establish the Pak-Qatar General Takaful Company and the Pak-Qatar Family Takaful Company in Pakistan by the end of 2006. The Pak-Qatar General Takaful Company has an initial paid-up capital of Rs250 million (US$4.11 million), while the Pak-Qatar Family Takaful Company will have a capital base of Rs400 million (US$6.58 million). The Pak-Qatar Family Takaful Company will offer investment and protection products, saving products, retirement and education policies, while the Pak-Qatar General Takaful Company will offer specialized products covering accident, fire, marine, engineering, money and banking, property insurance and liability.

Asia-Pacific

In Malaysia the current market penetration is low, but Takaful is expected to constitute 20% of the total insurance market by 2010 (up from its current 6.5%). At that time, Takaful's share of the Malaysian insurance industry is estimated to be worth RM7 billion (US$1.85 billion). Bank Negara Malaysia (BNM) issued four new Takaful licenses in January 2006 to four joint Takaful ventures involving foreign partners from the Middle East, Asia-Pacific and Europe. The companies obtaining the licenses were:

- HSBC Insurance (Asia-Pacific) Holdings, Jerneh Asia and Wang Simpanan Pekerja.
- Hong Leong Bank, Millea Asia, Japan, and Hong Leong Assurance.

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Global Takaful Review for 2006 *(continued...)*

- Bank Simpanan Nasional and Prudential Holdings.
- MAA Holdings and Solidarity.

In Indonesia, Allianz recently launched life and non-life Takaful products and Allianz Indonesia expects to see growth of over 30% in this market segment over the next two years.

Europe

A new Islamic insurance firm, British Islamic Insurance Holdings, is currently being established in the UK to offer Shariah based insurance solutions to the country's Muslim population. British Islamic Insurance Holdings is currently working on strategy, recruiting management and obtaining a regulatory license from the UK's Financial Services Authority.

"The Takaful industry is an important component in the overall Islamic financial system, given its role in providing risk protection"

Takaful industry developments

Re-Takaful capacity

Vital to the growth of the Takaful industry is the corresponding development of Shariah compliant reinsurance. Few re-Takaful operators have been established in comparison to the number of direct Takaful operators. However, it is noteworthy that international reinsurers such as Tokio Marine re-Takaful (TM ReTakaful), Swiss Re and Converium have entered the re-Takaful business in various jurisdictions including Bahrain, the Dubai International Financial Center (DIFC) and Malaysia. Recently, the Central Bank of Bahrain issued a license to Hannover Re in Germany to establish a wholly owned Islamic reinsurance company in Bahrain. Hannover Re Takaful will have a paid-up capital of BD20 million (US$53 million) and will focus on general and life classes. Hannover Re Takaful will be the principal underwriter of Hannover Re's worldwide re-Takaful business. BNM granted a re-Takaful license to Munich Re, amongst others, to conduct general and family re-Takaful business in Malaysia.

In the UK, Lloyd's insurer Creechurch Underwriter has created, in partnership with Salama Islamic Arab Insurance Company, the first Takaful syndicate, with an initial underwriting capacity of £41 million (US$81.48 million). The Takaful syndicate will benefit from the same security rating provided to all Lloyds syndicates, as provided by Standard & Poor's, AM Best and Fitch.

Global Takaful Standard

Currently, the regulation of Takaful is at various stages of development throughout the world. Jurisdictions such as Malaysia, Bahrain and Pakistan have introduced specific Takaful laws or regulations. However, the growth of the global Takaful industry would be encouraged by the introduction of uniform regulations of the Takaful business to promote cross-border activity and the global marketing of Takaful. To this end, the International Financial Services Board (IFSB) and the International Association of Insurance Supervisors (IAIS) have established a joint working group which released an issues paper on the applicability of the existing IAIS core principles to the regulatory and supervisory standards for Takaful to be developed by the IFSB.

The issues paper (dated August 2006) released by the joint working group identified four critical areas to the regulatory and supervisory framework of the Takaful industry which need to be addressed in an integrated way:

- Corporate governance (including the appointment, composition and report of the Shariah board).
- Financial and prudential regulation.
- Transparency, reporting and market conduct.
- Supervisory review process.

According to BNM's deputy governor in a keynote address at the 2nd Seminar on Regulation of Takaful on the 23rd February 2006, the issues paper may lead to the "issuance of a specific guidance paper or standards that correspond to the IAIS core principles."

Financial Strength Rating

A financial strength rating from an international rating agency would provide the members of a Takaful company with financial security. The Moody's August 2006 report – "Takaful: A Market with Great Potential" – sets out its approach in attributing a financial strength rating to a Takaful company:

> "The credit strengths and weaknesses of a typical Takaful company will typically be influenced by a number of considerations that do not apply to a western mutual insurer. Some are detailed below:

- **Corporate Governance.** The key performance indicators used by the Shariah board to assess the management of the operating company may have a greater focus on compliance with Islamic law rather than technical issues, such as underwriting performance and risk management. The nomination process to the board, as well

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Global Takaful Review for 2006 *(continued...)*

as the background of members appointed to it, will also be critical in ascertaining the quality of corporate governance and its ramifications on the financial strength of the Takaful fund.

- **Strategic Asset Allocation Policy**. A diversified and circumspect investment management strategy is a major credit factor for an insurer. Assets of a Takaful company may have different liquidity and volatility characteristics, as well as different risk–return profiles than those of a typical western insurer. For example, some Takaful insurers may exhibit a propensity to overweight Shariah compliant equities and real estate assets. Shariah compliant bonds may have concentration in certain geographical areas (e.g. Gulf states, Malaysia) which, in absence of credit enhancement by an international institution, may increase the risk profile of the Takaful fund. The effect of the alternative investment strategy on overall profitability will also need to be ascertained.

- **Structural Features of Family Takaful Products**. The profit sharing mechanism of long-term Takaful products may have certain distinctive features. For example, the determination, crediting and payment of profit participation on life policies, as well as the structure of any explicit or implicit guarantees, will need to be carefully examined.

- **Long-Term Capitalization Strategy and Regulatory Environment**. While the capital structure of a Takaful company is not in itself conducive to large distributions (the fund is in many cases de facto not distributable), ongoing profit sharing may be subject to competitive pressures and as such vary in time and by market. The position of the supervisory authority with regards to capitalization and its ability as well as willingness to enforce the regulation in place will also tend to have an influence on the Takaful company's financial strength."

Conclusion

The Takaful industry is an important component in the overall Islamic financial system, given its role in providing risk protection. Future challenges and opportunities include the development and harmonization of the regulatory framework and prudential standards for the Takaful industry, the promotion of corporate governance, transparency and market discipline, the creation of suitable Shariah compliant investment securities and the development of viable Islamic capital markets, the introduction of an internationally recognized rating system, the education of consumers, building brand loyalty, optimizing the use of technology for customer after-care and the creation of strongly capitalized global re-Takaful and multi-line Takaful providers.

The Takaful industry needs to cater to the growing needs of both Muslim and non-Muslim customers around the world. Primary markets within Europe that have a sizeable Muslim population include the UK, France and Germany. In Asia, China, India and Indonesia also offer opportunities. Islamic centers of product excellence include Malaysia, Bahrain and the UAE, but Indonesia, the Kingdom of Saudi Arabia and Pakistan are fast evolving and building their product expertise. There is significant untapped latent potential for Islamic financial services in the US, Europe and Asia.

Global insurance players such as Swiss Re, Hannover Re, Prudential, Allianz, AXA and Munich Re have recognized the opportunities in the Takaful and re-Takaful industry and as a result have recently entered the market. The major GCC and international cross-border banks such as Dubai Islamic Bank, National Commercial Bank, Kuwait Finance House, HSBC, Citigroup, Maybank and Bank Mandiri are also well positioned to package premier products and services for their middle income and affluent customers and to expand their cross-border distribution reach across multiple distribution channels including, but not limited to, international bank distribution chapters and corporate group plan sponsors.

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Potential Growth of Takaful in Europe

By Bassel Essam Hanbali

Financial saving is considered to be a virtuous trait for any member of society. Our way of life, and its current status, has turned us into consumer-driven nations, wanting to get rid of our money, as if we are plagued by the fact that money exists in our wallets. This has caused us to fall into financial problems, which hinder our flexibility, and thus we end up taking difficult financial decisions, due to our lack of saving or lack of funds, which hinders our future plans and goals. However, cultural and religious obligations play a major role in holding back the development of our individual financial situation due to the lack of products and plans that satisfy the principles of Islamic Shariah.

Today, with the current development of Takaful, individuals, families and businesses have the opportunity to help plan for their financial situation by utilizing methods that comply with the guiding principles of Islamic Shariah.

The global Takaful market

The global Takaful market is still in its relative infancy. However, regional economic growth and understanding of the concept of Takaful are major factors to the expansion of this Islamic financial system. In fact, there is now a greater awareness, from every social and business class, of the need for financial services, and a cultural and religious resistance towards conventional services, thus making Takaful the preferred option.

The reform of regulatory and legal bodies has also played a role in the rise of the Islamic system of insurance and assurance, Takaful. As the regulator of a leading financial hub, the Central Bank of Bahrain (CBB) (previously the Bahrain Monetary Agency (BMA)) has been at the vanguard of change, being the first country to standardize and regulate the practice of Takaful through a framework that takes into account the special nature of the Takaful model and the unique relationship between participants and shareholders. The Saudi Arabian Monetary Agency (SAMA) seems to have taken note of the efforts of the CBB and the subsequent strength of the Takaful industry in the Kingdom of Bahrain, and has introduced its own reforms to establish a dedicated insurance and Takaful authority in the Kingdom of Saudi Arabia.

The market in Europe

Several factors stand as proof of how far Islamic financial services have come in a short span of time in Europe. Strategic alliances between internationally recognized financial institutions to manufacture and distribute Takaful products in Europe are a sign of the potential growth of this unique Islamic system of financial services. Solidarity, the Bahrain-based Takaful company, newly signed an agreement with Chubb Federal Insurance, a top 10 US insurance provider, which allows Solidarity to meet the growing demand for specialty lines Takaful products.

Conferences taking place worldwide, and primarily in Europe, reiterate the growing importance of Islamic financial services and hence Takaful in the western world. Switzerland, the heart of Europe's private banking sector, now hosts the International Islamic Financial Forum to discuss the future of this industry and to help in creating a bridge between the east and the west. In a milestone event for the Islamic banking world, the Swiss Federal Banking Commission recently awarded Faisal Finance Switzerland a full banking license, making it the first private Islamic bank in Switzerland.

"There is now a greater awareness, of the need for financial services, and a cultural and religious resistance towards conventional services, thus making Takaful the preferred option"

Crucially, strategic alliances, honoring licenses and Islamic financial conferences are evidence that Europe has recognized Islamic financial services as a legitimate, effective form of services on a par with conventional finance. It also signals that Europe has grasped the fact that Islamic banking and insurance have become increasingly important to Europe's growing Muslim and non-Muslim population, especially those seeking principled financial services.

Total assets worldwide in the Islamic financial sector is continually growing at an estimated annual rate of 15%. In terms of the insurance and re-insurance sector, HSBC has predicted that the Takaful market will be worth an estimated US$15 billion in the year 2015 – a five-fold increase on its

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Potential Growth of Takaful in Europe *(continued...)*

current size. Industry professionals predict that a significant portion of this increase in the Takaful market will be generated in the western world, mainly the European market. The effects of globalization mean the world is becoming smaller and, as industry experts, we are all in effect citizens of a "global village." This has in turn affected the mindsets, opinions and attitudes of people all over the world and in particular the west; Europeans no longer perceive Takaful to be the exclusive domain of Muslims and have opened themselves up to new ways of thinking about insuring themselves and their families.

According to recent research by the European Islamic Investment Bank, between 70% and 80% of Sukuk are believed to be held by non-Islamic investors, a statistic which may reflect the fact that European investors now understand the opportunities and returns that can be gained from investing in the Islamic banking and Takaful sector.

In order for us to capitalize on the latent potential that exists for the Takaful market in Europe we need to adopt a two-pronged approach that places equal emphasis on regulating our practices and on investing in human capital.

Independent bodies like the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) are doing us an outstanding service by displaying to the western world our adherence to best practices and our efforts to regulate our systems and procedures.

"We need to adopt a two-pronged approach that places equal emphasis on regulating practices and on investing in human capital"

In Robin Wigglesworth's report on "Takaful Rising", he talked about Europe as an equally profitable market for Takaful, especially with the significant population of wealthy and increasingly aware Muslims scattered across the European Union (EU). Furthermore, Sameer Al Wazzan, Solidarity's chief executive officer, has shared his interest in the 2.8 million Muslims residing in the UK market; his company is developing customized Takaful products that meet the UK's regulatory requirements and market needs. Besides, Salama, in January 2006, established the first Shariah syndicate at Lloyds with an initial underwriting capacity of US$72 million and has further plans to enter other western markets, such as the US, Canada and western Europe, in the near future.

Investing in human capital is crucial to ensuring that the Takaful market in Europe grows to optimum levels; we need to encourage and motivate students to pursue the study of business practices from an Islamic point of view and to identity its role in finance and humanity. An increase in our resources in terms of Islamic scholars and field experts will assist us in reaching a wider customer base and tapping new markets within Europe.

Conclusion

This is an exciting time for the Takaful market in Europe. To take advantage of this positive climate, financial services providers and Takaful companies need to approach the market in the most professional manner and create consumer confidence through the genuineness of their products and services. Educating the public about the concept, the products, and the benefits of this unique Islamic financial system will allow it to rise to the challenge of global competition, by unleashing the creativity and entrepreneurial flair of financial services manufacturers who share and believe in the Islamic financial system in general, and Takaful in particular.

In short, providers of family and general Takaful products need to apply best business practices in their operations, aiming to assist in the growth of the personal living standards of Muslim and non-Muslim communities through wealth creation and protection. As financial professionals, we are witnessing the birth of a new era of Islamic financial services taking place across the EU and beyond. The future for Takaful is bright and we look forward to seeing it grow in leaps and bounds year on year.

سوليدرتي
SOLIDARITY

The author is head of corporate communications and marketing at Solidarity, one of the largest Takaful companies worldwide with US$275 million in paid-up capital. He leads the company's international marketing team with the key objective of strengthening the organizational brand image and maintaining awareness, recognition and attractiveness of the products among targeted groups.

TAKAFUL NEWS BRIEFS

JANUARY

Takaful Re gained a license from the **Dubai Financial Services Authority** to operate from the **Dubai International Financial Center**. The move was in tandem with the company's re-Takaful expansion plan in the MENA region and South East Asia.

SALAMA Islamic Arab Insurance Company signed an agreement with **MedNet Group** to provide Islamic health insurance in the UAE. SALAMA recorded a provisional net profit of Dh110 million (US$30.14 million) in 2005, an increase from the previous year's Dh3.599 million (US$1 million) profit.

The **Qatar Islamic Insurance Company** saw an increase in net profit of 318% for 2005, recording a QR173.2 million (US$47.58 million) profit. The board of directors also recommended a 15% cash surplus distribution on insurance premiums paid by policyholders. The shareholders also proposed a 15% cash dividend and 100% stock dividend to represent one bonus share for every share held.

The net profit for 2005 of the **National Company for Cooperative insurance** increased to SR313 million (US$83.5 million) in 2005, a boost of 66% from 2004.

Malaysia National Insurance and **Takaful Nasional** were inducted into the **Maybank** Group via **Mayban Fortis Holding**'s finalization of 74.2% of **Malaysia National Insurance**.

FEBRUARY

Dubai Islamic Insurance and Reinsurance Company (AMAN) announced a net profit increase of 865% for 2005, reaching Dh82.04 million (US$22.34 million) from Dh8.5 million (US$2.31 million) in 2004. The company's assets grew by 134% to Dh246 million (US$66.98 million) from Dh105 million (US$28.59 million) in 2004.

The UAE's **Arab Islamic Insurance Company (Salama)** received approval from the **Saudi Arabian Monetary Agency** to establish an Islamic insurance company with a capital of SR100 million (US$26.66 million).

German insurance firm **Allianz** announced plans to launch life and non-life Shariah insurance products in Indonesia. **Asuransi Allianz Life** offering unit linked life insurance and **Asuransi Allianz Utama** offering fire and motor vehicle insurance.

SALAMA Islamic Arab Insurance Company established the first Shariah syndicate at **Lloyd's of London**. The Takaful syndicate commenced trading with an initial underwriting capacity of US$72 million. It was awarded a security rating of A, as afforded to all Lloyd's syndicates by **Standard and Poor's**, **AM Best** and **Fitch**.

Abu Dhabi Commercial Bank launched the "Meethaq" Shariah compliant Savings and Takaful program, combining both savings and Takaful benefits. It became the first Shariah compliant regular savings program in the UAE to do so. The bank also signed an agreement with **Dubai Islamic Insurance and Reinsurance Company** – **AMAN** – allowing the establishment of a financial portfolio investing in 16 Islamic Shariah compliant investment funds, working along three set strategies with a minimum investment time period of seven years.

The **Association of Indonesian Shariah Insurance** called for the Takaful industry to hold a 2% market share of the Indonesian insurance industry in 2006, an increase from the 1.5% market share held in 2005.

Doha Insurance company and Bahrain-based **Solidarity** signed a memorandum of understanding in order to form **Doha Solidarity**, offering Solidarity's range of Takaful products in Qatar.

HSBC Insurance (Asia Pacific) Holdings, along with **Jerneh Asia** and the **Employees Provident Fund** of Malaysia, obtained approval from **Bank Negara Malaysia** to form a joint venture Takaful company in the country.

Malaysia Assurance Alliance affirmed confidence that its Takaful joint venture with **Solidarity** of Bahrain would raise between US$26.89 million and US$34.96 million in premiums within a year of starting up.

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TAKAFUL NEWS BRIEFS *(continued...)*

MARCH

Repeated calls were made for a regulatory framework for the Takaful industry at the 2nd Seminar on the Regulation of Takaful in Langkawi, Malaysia. Dr Bassel Hindawi, vice chairman and director general of the **Insurance Commission of Jordan**, stated that a Supreme Shariah Judicial Authority, a legislative framework, good governance, capital adequacy and the nurturing of re-Takaful were vital for industry growth.

Qatar Islamic Insurance Company announced plans to launch three major joint ventures in 2006.

Arab Insurance Group posted a record profit of US$48.2 million for 2005, up 82% from US$26.5 million in 2004. The group's paid up capital also increased to US$220 million.

SALAMA Islamic Arab Insurance Company became the first insurance company from the UAE to receive regulatory approval to offer its shares to all GCC nationals. Over one million SALAMA shares were bought by non-UAE nationals in the first week of trading.

Syarikat Takaful Malaysia announced its 20% growth target in premiums for 2006.

Dubai Islamic Insurance and Reinsurance Company (AMAN) received approval from the Ministry of Economy to increase its capital to Dh200 million (US$54.45 million) without any subscription fee.

Dhipaya Insurance stepped up marketing of its Takaful policies for its Muslim customers. The marketing strategy targeted THB50 million (US$1.28 million) in Takaful premiums for 2006, THB80 million (US$2.06 million) for 2007 and THB120 million (US$3.08 million) in 2008.

Al Khaleej Insurance raised its capital by 150% through a bonus issue for its shareholders. The bonus issue translated into a capital base of QR127 million (US$34.9 million), from its previous QR50.8 million (US$13.9 million).

The **Bahrain Monetary Agency** finalized its plans to establish an **International Takaful Association**.

The Arab insurance sector was urged to exploit the increasing economic growth in the region, in light of the Bahraini government's implementation of reforms gearing towards free trade and an investment boom.

Takaful International distributed BD500,000 (US$1.3 million) in cash dividends to shareholders, equivalent to 10% of its paid-up capital.

Hong Leong Bank announced commencement of Takaful operations in October, initially offering at least two products.

Syarikat Takaful Malaysia expressed its target to capture 10% of the total brokerage market by 2010.

Dubai Islamic Insurance and Reinsurance Company (AMAN) declared a distribution of 15% cash dividend and 15% bonus shares to its shareholders, on top of the distribution of 2% of its profits to policyholders.

Takaful International's chairman Isa Abdulla Al Mannai announced the company's success in completing its 17th year in business and noted the drawing of a four-year strategic business plan to achieve a qualitative development in all the company's local and regional business activities.

APRIL

It was announced that total worldwide Takaful premiums covering both non-life and life insurance are expected to reach US$7.4 billion by 2015.

Malayan Banking (Maybank)'s latest Takaful fund – Takaful Capital Protection Plan II – announced its plans to invest at least 70% into fixed income and the balance into equities from the **Dow Jones Islamic Market World Index**.

Dubai Islamic Insurance and Reinsurance Company (AMAN)'s proposed increase in paid-up capital to Dh200 million (US$54.45million) obtained the approval of its shareholders. Foreign ownership of its shares amounted to 15%.

Dubai Financial Services Authority chairman Dr Habib Al Mulla called for regulators to put its Shariah systems in place without dictating which Shariah regulations companies should follow.

Dr. Saleh Malaika, vice chairman and CEO of **Salama Islamic Arab Insurance Company** announced the need for a Takaful regulatory body to be formed with representatives from the Takaful and re-Takaful industry. He explained the three components required to develop the Takaful industry "They are, first, to establish an authority to regulate the industry; second, to assign ratings similar to those applied to banks; and third, greater cooperation between the Arabic and Asian members of the industry." he explained.

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TAKAFUL NEWS BRIEFS *(continued...)*

ISM Insurance Services Malaysia, teamed up with **SAS Malaysia** to launch its knowledge management services for the insurance and Takaful industry.

The chairman of the **Dubai Financial Services Authority (DFSA)** called upon Takaful companies to adopt an innovative approach to their products.

It was announced that he Middle East's Takaful industry is poised for annual double digit growth over the next decade, according to Dr Saleh Malaikah, vice chairman and CEO, **SALAMA Islamic Arab Insurance Company**.

Doha Insurance Company launched its Takaful branch, **Doha Solidarity**, having partnered with the Bahrain-based **Solidarity**.

Market penetration in the local Takaful industry rose to 5.6% in 2005 from 5.1% previously, underpinned by a strong domestic economic growth. **Bank Negara Malaysia** said other factors which contributed to the industry's strong performance included a combined family and general Takaful net contributions, which grew by 18.8% to RM1.3 billion (US$355million) from RM1.1 billion (US$300 million) in 2004.

Perbadanan Tabung Amanah Islam Brunei launched its Takaful arm, Insurans Islam TAIB, at the opening of its Kuala Belait branch's new office building.

SALAMA Islamic Arab Insurance Company announced its plans to launch family Takaful to compliment its previously launched health Takaful, in order to meet the increasing demand for Shariah compliant personal insurance solutions.

MAY

AMPRO Holdings Singapore, in partnership with **United Overseas Insurance**, a member of **United Overseas Bank**, launched three Takaful schemes focusing on motor, domestic help and travel cover.

Chairman of **SALAMA** Sheikh Khaled bin Zayed bin Saqr Al Nahyan projected global demand for Takaful and re-Takaful products and services to grow significantly over the next five years, with market value increasing from Dh6.23 billion (US$1.7 billion) to between Dh27.5 billion (US$7.5billion) and Dh36.7 billion (US$10 billion).

Bahrain Islamic Bank signed a memorandum of cooperation with **Takaful International** to provide social and Takaful security for its employees and their families. The insurance covers death for any reason and total disability resulting from illness or accident.

Group One Takaful Holding was registered as an Ancillary Service Provider at the **Dubai International Financial Centre**.

Focusing on the retail market, **Takaful Ikhlas** announced its aims to achieve contributions of RM220 million (US$61.4 million) for its 2007 fiscal year.

SALAMA Islamic Insurance Company reported net profits of Dh70 million (US$19 million) for the first quarter of 2006, an increase of 8% on its provisional Dh65 million net profit (US$17.8 million).

JUNE

The inaugural preparatory meeting for a planned **International Takaful Association**, was held at the **Bahrain Monetary Agency**. The summit attracted a participation of ten Takaful companies worldwide. A five-member committee was formed to develop new articles of association, membership structure, membership fees and budget.

Allianz AG expressed its plans to offer more Islamic products in Indonesia and expand into Malaysia to tap the potential offered by the 500 million Muslims in South-East Asia.

SALAMA Islamic Arab Insurance Company raised its shareholding in **BEST-Re**, the world's first and largest re-Takaful company, to 100% from 60% as part of its expansion into the Takaful and re-Takaful markets.

A collaborative Mudarabah founded in 1997 earned **Takaful Malaysia** a RM2.9 million (US$797,801) contribution from unit trust companies.

MNRB Holdings laid out plans to offer re-Takaful products to its clients in early 2007.

New insurance obligations of the **Islamic Corporation for Insurance of Investments and Export Credits**, a member of **Islamic Development Bank**, increased to US$808 million in 2005. Actual insured transactions reached US$618 million, an increase of 83% from US$337 million in 2004.

The **Qatar Islamic Insurance Company** received approval from the Pakistan authorities to establish two Takaful companies in

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TAKAFUL NEWS BRIEFS *(continued...)*

the country by the end of 2006 with an initial paid-up capital of Rs650 million (US$10.8 million).

A closed shareholding Takaful company was established in Kuwait. The **Boubyan Takaful Insurance Company**, started up with a capital of KD10 million (US$34.5 million) and 100 million real shares, operating in the areas of Takaful, co-operative insurance and Shariah compliant re-insurance.

BMS Asia Intermediaries received approval from the **Labuan Offshore Financial Services Authority** to establish a re-Takaful division – **BMS Asia Re-Takaful** – within its Kuala Lumpur office.

Shamil Bank appointed **Solidarity** as the healthcare Takaful provider to the bank's employees and their families.

Allianz General Insurance announced plans to tap into the Takaful industry due to its high growth potential, citing Malaysia as a particularly interesting market.

Having acquired licenses to set up Takaful companies in Saudi Arabia and Malaysia, **HSBC Amanah** expressed its intention to shift the current focus of the Islamic finance industry to a mode of financing where people take on the role of investors and start protecting their future and that of their children.

MAA Holdings received approval from **Bank Negara Malaysia** for its proposed joint venture Takaful business with **Solidarity**.

The Qatar government rolled out its final stages of issuing a comprehensive set of new insurance laws. **Qatar Islamic Insurance Company's** general manager Izzat M. al-Rashid commented that the revised laws would boost insurance activity in Qatar over the coming few years.

Swiss Re launched a fully Shariah compliant Family re-Takaful solution to meet strong market demand, using the Wakalah model, instead of the cost-effective Mudarabah model, due to its universal Shariah compliance.

JULY

Global Investment House set up an Islamic reinsurance company in Kuwait, called the **Al Fajer re-Takaful Insurance Company**, with a paid-up capital of KWD50 million (US$174 million). Al Fajer was the first re-Takaful company in Kuwait and the second in the Gulf region.

Takaful Ikhlas expressed its aims to be the top information technology provider in Malaysia for its customers and associates. Takaful Ikhlas has invested RM15 million (US$4.1 million) since 2003 to provide online services, with the main objective of conducting as many online transactions as possible to maximize transactions.

The **Saudi Capital Market Authority** confirmed that Saudi Arabia was drafting a legislation to facilitate the issuance of Islamic financial products, including Takaful to be ready by the end of 2006.

Qatar Financial Center offered life insurance companies, including Takaful operators to set up operations through free repatriation of capital and profit and a zero-tax regime until the end of 2008. It also promised the absence of ownership restrictions.

Salama Islamic Arab Insurance Company predicted the global demand for Takaful and re-Takaful products and services to grow notably in the near future, with market value expected to increase from US$1.7 billion to US$7.5 – US$10 billion. The global Takaful personal insurance sector is also predicted to reach Dh17.8 billion (US$4.84 billion) by 2015.

Takaful Ikhlas received approval from **Bank Negara Malaysia** to open regional offices in Sabah, Sarawak and Putrajaya.

Takaful Ikhlas teamed up with Islamic gold dinar distributor **EQirad** to provide comprehensive group Takaful scheme Islamic dinar investors. The alliance will provide those who purchase the gold dinar ringgit-for-ringgit Takaful cover.

The **General Authority for Health Services for the Emirate of Abu Dhabi** announced a new list of authorized insurance companies for its new health insurance law, bringing the number of authorized insurers to 14.

Jerneh Asia assessed the feasibility of investing in the life insurance business in India, Vietnam and Myanmar due to the companies' close proximity and enormous growth potential.

MNRB Holdings planned its Dubai entrance before the end of 2006. Its chairman Mohammad Abdullah confirmed that the reinsurance firm was in the process of finalizing the plan to open a representative office including obtaining clearance from relevant authorities.

Takaful Ikhlas announced its aims to gain a higher revenue of RM220 million (US$59.9 million) in 2006 from RM147 million (US$40.02 million) in 2005.

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TAKAFUL NEWS BRIEFS *(continued...)*

AUGUST

Acting director of financial institutions for **Brunei's Ministry of Finance**, Hj Mohd Roselan Mohd Daud expressed that Takaful was in dire need of experts with dual expertise in Shariah and actuarial sciences.

Syarikat Takaful Malaysia introduced the provision of a twenty-four hour tele-assistance service for its clients. The service was launched under the Motorized Vehicles Takaful Scheme.

The **Associated Chambers of Commerce and Industry of India** announced its expectations for rural and semi-urban India to contribute US$35 billion by way of insurance premium by 2010. Of this, US$20 billion is expected from life insurance and the remainder through the insurance of vehicles, property, livestock, crop and farm equipment.

The **Kuwaiti Ministry of Health** called for expatriates to make their medical insurance or Takaful payments to banks rather than to insurance companies, due to heavy losses resulting from the failure to collect more that KD100 million (US$345.7 million) from insurers.

Prudential and **Bank Simpanan Nasional** launched a joint venture Takaful company– **Prudential BSN Takaful**. BSN and Prudential hold 51% and 49% respectively.

Al Baraka Banking Group bought two Takaful covers – Public Offering of Securities and Directors and Officers Liability from Bahrain-based insurance company **Solidarity**.

The **Dubai Islamic Insurance and Reinsurance Company (AMAN)** attained a 22% Emiratization of jobs, reportedly the highest level among insurance companies in the UAE for 2006.

Dr Zeti Akhtar Aziz, governor of **Bank Negara Malaysia**, at the Malaysian Islamic Finance – Issuers & Investors Forum 2006 in Kuala Lumpur, revealed that licensed Takaful operators offering Islamic financial services in international currencies would be allowed to set up International Currency Business Units within existing institutions.

Syarikat Takaful Malaysia targeted overseas expansions, particularly in Asia and the Middle East slated in the begining of 2007.

HSBC Amanah Takaful (Malaysia) was fully registered by **Bank Negara Malaysia** to be opened for business in September 2006.

Damascus approved the establishment of three joint-venture Takaful companies offering agriculture, health and life, among other Takaful covers. The three licensees were **Al-Aqeelah** with a capital of US$20 million, **Al-Nour** with a capital of S£1.5 billion (US$28.9 million) and **Syrian-Qatari Company** with a capital of S£850 million (US$16.37 million).

The Doha bourse's five listed insurance companies reported a fall of over 12% in net profit to QR250.3 million (US$68.76 million) for the first half of 2006. This was attributed to an increase in claims and an erosion in the value of investments.

A six-member steering committee was formed by members of the proposed **International Takaful Association** to speed up the organization's formation. The Association aimed to be the first Takaful industry trade body in the Gulf.

Kuwait Finance House Malaysia made an agreement with **Syarikat Takaful Malaysia**, **Takaful Nasional** and **Takaful Ikhlas** – in order to provide Islamic insurance products.

Saudi Arabia announced the issuance of 13 operating licenses to insurance companies from Bahrain, the UK, France, Germany, Holland, India, Japan, Jordan, Lebanon, Switzerland and the US.

Bank Negara Malaysia governor Dr Zeti Akhtar Aziz announced the limit for foreign ownership in local insurance companies be raised from 30% to 49%, in a bid to improve development of domestic capabilities in areas of technical expertise, innovation and operating processes.

A check for US$100,070.39 was handed over from **Takaful IBB** to **Joffren Omar Co** and **Syarikat Kejuruteraan Sistematik** for their Mudarabah entitlement relating to the company's participation in Takaful packages for 2005.

Takaful International signed a deal with **Almoayyed Computers** to provide the production and test environment infrastructure for insurance business solutions' Integrated Insurance Management System, from **Tata Consultancy Services**.

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TAKAFUL NEWS BRIEFS *(continued...)*

SEPTEMBER

Bank Negara Malaysia again stressed the need to move towards a more risk-focused approach in the insurance and Takaful industry. Calls were made for the regulatory framework to move towards providing a more flexible regime for stronger and well-managed institutions, while providing supervisory intervention to weaker institutions.

Gambia was slated to be next in line in the Takaful race, after the first Bill of Islamic Insurance in Gambia was listed before the National Assembly of Members for possible ratification. The Bill, which was listed by Dr Aja Isatou Njie-Saidy, vice president and Secretary of **State for Women's Affairs**, sought to amend the Insurance Act 2003 to allow for the operation of Takaful.

The council of the **Islamic Financial Services Board** announced six new members, bringing the total number of members to 94. The added members included the **Malaysia Deposit Insurance Corporation** as an associate member, and the **Ahli United Bank**, Bahrain; **Perbadanan Tabung Amanah Islam Brunei**, Brunei; the **Islamic Insurance Co**, Jordan; **Osoul Leasing and Finance Company**, Kuwait; and **Al Baraka Bank**, Lebanon as observer members.

Malaysia Deposit Insurance Corporation led the establishment of an international committee for Islamic deposits insurance during the **International Association of Deposits Insurers** meeting in Kuala Lumpur.

Countries in the Gulf region displayed low rates of insurance penetration relative to global averages, **Standard & Poor's** noted in a report entitled "Gulf Region Sees Rapid Insurance Growth as Market Demands and Business Benefits Increase."

Gulf Takaful Insurance Company engaged **Advantage Consulting Company** for organization restructuring of their Kuwaiti operations.

Qatar International Islamic Bank and **Qatar Islamic Insurance Company** announced the setting up of an Islamic insurance firm in Pakistan: **Pak-Qatar Takaful**. The company involved two Takaful entities – Pak Qatar Family Takaful and **Pak Qatar General Takaful** with a subscribed capital for **Family Takaful** at Rs400 million (US$6.6 million) and Rs250 million (US$4.13 million) for **General Takaful**.

Solidarity launched an environmental awareness campaign to educate its staff to collect papers and deliver them to a recycling factory.

Takaful Ikhlas announced its RM1 million (US$272.3 million) target in premium for their internet-based Takaful service – e-IKHLAS – in 2006.

The **Central Bank of Bahrain** awarded a license to global reinsurance company **Hannover Re** to establish a re-Takaful company in Bahrain.

The **Central Insurance of Iran**, or **Bimeh Markazi Iran,** announced its bid to promote e-Takaful and micro-Takaful to increase insurance penetration in the country.

Qatar Islamic Insurance Company finalized its entrance into the Syrian market by establishing a US$20 million subsidiary.

The **Syrian Insurance Supervision Committee** gave the green light to three new insurance firms, introducing Takaful in the country for the first time. The companies included the **Syrian Qatari Insurance Company**, the main shareholders of **Nour Insurance Company** – **Pak Kuwait Takaful Company, Nour Financial Investment Company** and individual Syrian, Kuwaiti and Arab investors; as well as the **Al Aqila Insurance Company**.

American Insurance Group announced its proposed foray into the Takaful market. Charles Bouloux, president of **AIG MEMSA** commented: "We are looking at this [Takaful] and will announce in the very near future what we will do. It is more than likely we will have a positive statement to make," he said

Bank Negara Malaysia approved two applications for re-Takaful licenses for **Munich Re** and **MNRB Holdings**.

British Islamic Insurance Holdings – was being developed to offer Shariah-based insurance solutions in the UK, and list on the **Alternative Investments Market**.

continued...

TAKAFUL NEWS BRIEFS *(continued...)*

OCTOBER

Global insurer **AIG** launched a regional company **AIG Takaful** in Bahrain, licensed by the Central Bank.

The **Syrian International Islamic Bank**, a joint venture between **Qatar International Islamic Bank** and other Qatari partners, requested a license to set up an Islamic insurance company in Syria with a capital of S£850 million (US$16.4 million).

Foreigners were given the green light to own up to 25% of the **Islamic Arab Insurance Company** or **Salama**'s shares. The company became the first insurer in the UAE to admit foreign shareholders.

The Takaful market recorded a premium growth of 20% up to 2005, with total premiums of over US$2 billion. Moody's Investors announced that the industry was expected to grow to US$7 billion-plus by 2015.

The government of Saudi Arabia granted licenses to 13 cooperative insurance companies. R. R. Nair of the newly launched **Indo-Saudi Insurance Company** commented that the move would help to launch new products in the market at competitive rates, benefiting the consumer.

Swiss Converium Holdings received approval from the **Labuan Offshore Financial Services Authority** in Malaysia to provide international re-Takaful services, in line with the company's plans to write international re-Takaful business in South and South-East Asia.

LS Associates signed a memorandum of understanding with **Takaful Ikhlas** to provide IKHLAS Motor Takaful cover for clients of its mega auto mart – KARS.

Takaful International and the **Batelco Trade Union** signed an agreement for the provision of insurance services to trade union members. Under the agreement, Takaful International is to provide a range of services, including building and motor insurance for members and their families; travel insurance for members and their domestic helpers; family Takaful insurance and other services.

SABB Takaful Company was granted a license to operate in Saudi Arabia, offering both Family and General Takaful products for personal and corporate customers.

The third series of **Maybank**'s Takaful Capital Protection plan – TCPIII – was launched. The RM120 million (US$32.67million) five-year, closed-end Shariah compliant investment plan aims to provide family Takaful coverage and is underwritten by **Mayban Takaful**.

Takaful Ikhlas announced its target to achieve a 50% rise in premium collection for the 2006/2007 financial year, equating to about RM220 million (US$59.81 million).

NOVEMBER

Syrian authorities granted two more licenses to new insurance companies. The two new joint venture companies were the **Syrian–Kuwaiti Insurance Company** and **Arab Insurance Company** Syria. Both have a 49% overseas interest.

Sri Lanka's biggest financial conglomerate, **Ceylinco Consolidated**, announced plans to launch more insurance products in the Gulf through its flagship company **Ceylinco Insurance**.

As part of a key move by the **National Company for Cooperative Insurance** to establish itself more strongly in the Saudi insurance market, the board of directors reorganized the company into five strategic units – medical, motor, property & casualty, marketing & sales and key accounts.

Islamic insurance company **Amana Takaful** revealed that it will list 12.5 million shares on the secondary board of the Colombo Stock Exchange by way of an introduction. The shares will be priced at Rp10 (US$0.22) each

Syarikat Takaful Malaysia reported an income of RM176.492 million (US$50.4 million) and a profit of RM34.360 million (US$9.81 million).

The **Association of the Insurance & Reinsurance Companies of Turkey**'s chairman, Huluri Taskiran, expects the Turkish insurance market to grow by 50% by 2010. He projected the total volume in the Turkish market to be between US$6 billion and US$6.5 billion for the first time in 2006, or as a minimum three times the size it was in 1999.

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TAKAFUL NEWS BRIEFS *(continued...)*

Al Safat Takaful Company selected **PREMIA**, an integrated insurance management solution from **3i Infotech** to automate its General and non-Life insurance business.

The **Oman Insurance Association** was launched to strengthen co-operation amongst the ever-increasing number of market players.

SALAMA Islamic Arab Insurance Co. achieved record profits for the third quarter of 2006, triple of 2005's Dh110 million (US$29.95 million) for the same period.

Salama Takaful Group's subsidiary, **Saudi IAIC**, revealed plans to open eight branches in Saudi Arabia, adding to its current six branches. It is amongst the first of the 13 insurers who were granted licenses in October by the regulator, the **Saudi Arabian Monetary Agency**, under the Kingdom's new insurance laws.

Takafulink, a Shariah compliant investment-linked plan, was launched by **Prudential BSN Takaful**. allowing customers to adjust their protection and savings according to their needs. It will also return 100% surplus back to its participants.

An agreement was signed between Bahrain-based **Solidarity** and **Federal Insurance Company** of Labuan to jointly offer specialty lines of Takaful insurance. Solidarity said the alliance will focus on writing directors and officers' liability, professional liability, fidelity bond and financial institution bond policies.

A Takaful expert suggested a standardized set of guidelines for the Islamic insurance sector to foster growth in an emerging market. ABM Nurul Haq, a member of the Takaful and Re-Takaful Committee set up by the Jeddah-based **Islamic Development Bank**, says that Takaful companies currently rely on their own Shariah boards.

The **Central Bank of Malaysia** jointly hosted the 2nd International Convention on Takaful and re-Takaful with the **Islamic Banking and Finance Institute** and **Malaysian Takaful Association**. The convention focused on "Reshaping Takaful Landscape: Forging Global Excellence".

Mayban Fortis Holdings projected its pre-tax profit to reach RM500 million (US$35.8 million) for the financial year ending on the 30th June 2009, following its takeover of **Malaysia Nasional Insurance** and **Takaful Nasional.**

The **National Company for Cooperative Insurance**, Saudi Arabia's biggest insurer, signed an agreement with global re-insurer **Munich Re** to provide up to US$100 million worth of energy insurance cover.

The **Malaysian Takaful Association** and the **Islamic Banking and Finance Institute of Malaysia** signed a memorandum of understanding to develop and introduce a Takaful basic examination together. The examination will be a compulsory entry qualification for Takaful agents and executives in the financial services industry, promoting Takaful products and services.

The **International Center for Education in Islamic Finance** signed a memorandum of understanding with Takaful operators in Malaysia over the Certified Islamic Finance Professional program for Takaful senior executives.

The **Central Bank of Bahrain** proposed a new licensing fee system for financial institutions – currently out for a consultation exercise. The new system would impose a single annual charge set at 1% of a licensee's operating costs. The revised fee would be subject to a floor and a cap for different license categories. This system is set to be implemented in 2007.

Maybank launched Takaful Insan, a family protection plan to provide for families of those afflicted by permanent disability or death which allows flexible choice of tenures and affordable monthly fees for customers.

Reinsurance and Takaful company **MNRB Holdings** recorded a lower profit of RM31.80 million (US$8.76 million), before zakat and taxation, for the third quarter. The company experienced a RM7.83 million (US$2.16 million) decline from 2005's third quarter. Its revenue rose by 9.4% to RM418.6 million (US$115.4 million) as a result of an increase in gross premiums written by its reinsurance subsidiary **Malaysian Re**.

The **Gulf Takaful Insurance Company** announced plans to utilize **ARIMA Insurance** Software's Medical and Life Takaful Insurance Software. ARIMA is a software subsidiary of **Arab Insurance Group** specialized in developing and marketing insurance software solutions across the MENA region. The implementation of both Medical and Life Takaful Software were completed in record time by ARIMA.

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TAKAFUL NEWS BRIEFS *(continued...)*

DECEMBER

AXA Insurance (Gulf) was given the green light by the **Qatar Financial Center Regulatory Authority** to operate in the Qatar Financial Center.

Takaful Malaysia allocated RM40 million (US$11.03 million) to upgrade its Takaful integrated system in order to stay competitive.

Hong Leong Tokio Marine Takaful will undertake Takaful in international currencies, allowing the company to expand overseas. An International Currency Business Unit will be established by the company to conduct non-ringgit composite Takaful and re-Takaful business

Amana Takaful of **Amana Investments** commenced trading on the **Colombo Stock Exchange**. Amana was listed on the second board through an introduction process which does not require an initial public offering.

Takaful Malaysia appointed the **Islamic International Rating Agency,** of which it is a shareholder, to provide it with a Shariah quality rating.

The GCC's insurance market is expected to expand by US$2 billion by 2010, when it will reach US$7.1 billion, **Nexus Insurance Brokers** forecasted.

Razif Abdul Kadir, deputy governor of **Bank Negara Malaysia**, stated that concerted efforts must be taken to educate the public and forge stronger governance in Takaful.

Takaful agents were urged to cut down their current reliance on conventional reinsurance, instead moving to re-Takaful. In 2005, the amount of reinsurance needed by Takaful operators was US$200 million. There were also suggestions for re-Takaful operators to be given priority over conventional re-insurers by Takaful companies, to provide a boost to this sector of the industry.

Mannai Motors signed an agreement with **Solidarity** to establish itself as an authorized service center set to service the claims of all Solidarity Motor Takaful policyholders.

The informal **Asian Takaful Group** adopted the new moniker, **Global Takaful Group** to attract international membership.

The period between March and September 2006 saw the Iranian insurance market grow by 23%, with the country's insurance penetration rate standing at 1.3% – still relatively low by international norms.

Risk Management Services Private was given the mandate to serve as an insurance broker in Pakistan. Insurance broker and consultant, **Risk Management Services,** jointly sponsored the company with a Pakistan-based group.

Wala Insurance of Saudi Arabia announced that it will mark the commencement of its operations through a 40% initial public offering of its 20 million shares. Wala Insurance's operations are slated to begin in the second quarter of 2007.

GLOSSARY

A

Ajr = commission or fee charged for services

Amanah = reliability, trustworthiness, loyalty, honesty
An important value of Islamic society in mutual dealings. It also refers to deposits in trust, where a person may hold property in trust for another.

B

Bai al Arboon = deposit-secured sale
A sale agreement in which a security deposit is provided in advance as part payment towards the price of the commodity. The deposit is forfeited if the buyer does not meet his obligation.

Bai Al Salam = future delivery
A contract whereby the payment is made in cash at the point of contract but the delivery of asset purchased will be deferred to a predetermined date.

Bai Bithaman Ajil = deferred payment sale
Also known as *Bai Muajjal*.
The sale of goods on a deferred payment basis. Equipment or goods requested by the client are bought by the bank, which subsequently sells the goods to the client for an agreed price, including a mark-up (profit) for the bank. The client may pay by installments within a pre-agreed period, or in a lump sum.

This sale works in a similar way to a Murabahah contract, but with deferred payment.

Bai Dayn = debt financing
The provision of financial resources required for production, commerce and services through the sale and purchase of trade documents and papers. Bai Dayn is a short-term facility with a year or less maturity. Only documents evidencing debts arising from bona fide commercial transactions can be traded.

Bai Inah = sale and buy-back
The sale and buy-back of an asset for a higher price than that for which the seller originally sold it.

A seller immediately buys back the asset he has sold on a deferred payment basis at a price higher than the original price. This can be seen as a loan in the form of a sale.

Bai Istijrar = supply sale
When a supplier agrees to deliver to a client on a regular basis at an agreed price and mode of payment.

Bai Muajjal = see Bai Bithaman Ajil above

Bai Muzayadah = open bidding trading
The principle governing open auctions, where the asset is awarded to the highest bidder.

Bai Wafa = sale and buy-back
The sale and buy-back of an asset within a set time, when the original buyer agrees to the original seller's repurchase.

Baitul Mal = treasury

Batil = null and void

D

Darura = necessity
In an emergency, Muslims may disregard aspects of Shariah laws in order to save their lives, or to preserve the Islamic community.

Dhaman = guarantee
A contract of guarantee whereby a guarantor shall underwrite any claim and obligation that should be fulfilled by an owner of the asset. This concept is also applicable to a guarantee provided on a debt transaction in the event a debtor fails to fulfill his debt obligation.

Dirham = unit of currency
A unit of currency, usually a silver coin, used in the past in some Muslim countries and still used in some Muslim countries today, for example Morocco and the UAE.

F

Fard al Kifa'i = socially obligatory duties
A collective duty of Muslims. The performance of these duties (for example funeral prayers) by some Muslims absolves the rest from discharging them.

This term covers functions which the community fails to or cannot perform and hence are taken over by the state, such as the provision of utilities, or the building of roads, bridges and canals.

Fasid = unsound or unviable
A forbidden term in a contract, which consequently renders the contract invalid.

Fatwa = religious decree

Fiqh = Islamic jurisprudence
The science of the Shariah. An important source of Islamic economics.

Faqih = Shariah jurist
Plural = Fuqaha

continued...

GLOSSARY *(continued...)*

G

Gharar = uncertainty
One of three fundamental prohibitions in Islamic finance (the other two being riba and maysir). Gharar is a sophisticated concept that covers certain types of haram uncertainty in a contract. It is an exchange in which one or more parties stand to be deceived through ignorance of an essential element of the exchange. Gambling is a form of gharar because the gambler is ignorant of the result of the gamble.

The prohibition on gharar is often used as the grounds for criticism of conventional financial practices such as short selling, speculation and derivatives.

H

Hadith = the Prophet's sayings and commentary on the Quran

Hajj = pilgrimage to Mecca
There is a duty on every Muslim who is financially and physically able to carry out Hajj, the fifth pillar of Islam, at least once in his lifetime. The pilgrimage takes place in the week from the 8th until the 13th day of the 12th Islamic month of Dhul Hijjah.

Hak Tamalluk = ownership right
A tradable asset in the form of ownership rights.

Halal = lawful, permissible
The concept of halal has spiritual overtones. In Islam there are activities, professions, contracts and transactions that are explicitly prohibited (haram) by the Quran or the Quran. All other activities, professions, contracts and transactions are halal.

This concept differentiates Islamic economics from conventional economics. In western finance all activities are judged on economic utility. In Islamic economics, spiritual and moral factors are also involved – an activity may be economically sound but may not be allowed in Islamic society if it is not forbidden by the Shariah.

Hanbali = Islamic school of law
Islamic school of law founded by Imam Ahmad Ibn Hanbal. Followers of this school are known as Hanbalis.

Hanifite = Islamic school of law
One of the major Islamic school of law, founded by Imam Abu Hanifa. Followers of this school are known as Hanafis.

Haram = unlawful, forbidden
Activities, professions, contracts and transactions that are explicitly prohibited by the Quran or the Sunnah. See *halal* above.

Haq Maliy = rights on the financial assets
Haq Maliy are rights on the financial assets. Examples of such rights are haq dayn (debt rights) and haq tamalluk (ownership rights).

Hawala = bill of exchange, remittance
A contract which allows a debtor to transfer his debt obligation to a third party who owes the former a debt. The mechanism of Hawala is used for settling international accounts by book transfers, thus obviating the need for a physical transfer of cash.

Hibah = gift
A gift voluntarily donated in return for a loan provided or a benefit obtained.

Hila = forbidden structure
A transaction which appears permissible, but is in fact structured in an un-Islamic way.

I

Ibra = rebate
When a person withdraws the right to collect payment from a borrower.

Ijarah = leasing
A lease agreement whereby a bank or financier buys an item for a customer and then leases it to him over a specific period, thus earning profits for the bank by charging rental.

The duration of the lease and the fee are set in advance. During the period of the lease, the asset remains in the ownership of the lessor (the bank), but the lessee has the right to use it. After the expiry of the lease agreement, this right reverts back to the lessor.

This is a classic Islamic financial product.

Ijarah Thumma Bai = leasing to purchase
The principle governing an Ijarah contract at the end of the lease period, when the lessee buys the asset for an agreed price through a purchase contract.

Ijarah wa Iqtina = buy-back leasing
A hire and purchase mode of financing where an Islamic bank finances equipment, a building or other facility for the client against an agreed rental, together with an undertaking from the client to repurchase the facility at the end of the contract. The rental and the purchase price are fixed so that the bank gets back its principal sum along with some predetermined profit.

Ijtehad = effort, exertion, industry
A faqhi's endeavor to formulate a rule on the basis of evidence found in the Islamic sources.

continued...

GLOSSARY *(continued...)*

Inan = financial partnership

Istijrar = recurring sale
Different quantities are bought from a single seller over a period of time. Sometimes it is also referred to transactions whereby seller delivers different quantities in different installments to complete the full purchase. Some divergence among the scholars in terms of the timing of fixation and pricing.

Istisnah = advance purchase of goods or buildings
A contract of acquisition of goods by specification or order, where the price is paid in advance, or progressively in accordance with the progress of a job. For example, to purchase a yet to be constructed house, payments would be made to the builder according to the stage of work completed.

This type of financing, along with Salam, is used as a purchasing mechanism, and Murabahah and Bai Bithaman Ajil are for financing sales.

Ittifaq Dhimni = pre-agreed contract
The sale and repurchase of an underlying asset. Prices are agreed in advance, prior to the contract, to allow the bidding process to take place.

J

Jahl = ignorance (of morality or divinity)

Ji Alah = pre-agreed contract
A unilateral contract promising a reward for a specific act or accomplishment, also known to be a contract of reward;

Ju'alal = stipulated price for performing a service
Applied by some in Islamic banking. Bank charges and commission have been interpreted to be Ju'alal by the jurists and thus considered lawful.

K

Kafalah = guarantee
Shariah principle governing guarantees. It applies to a debt transaction in the event of a debtor failing to pay.

Khilabah = fraud
A form of fraud, either in word or deed by a party to the trading contracts with the intention of inducing the other party into making a contract. This is prohibited according to the Shariah.

Khiyanah = deception
Refers to deception by not disclosing the truth or breaching an agreement in a hidden way. This is prohibited according to the Shariah.

L

Loan (with service charge)
Some Islamic banks give loans with service charges. The Council of the Islamic Fiqh Academy has resolved that it is permitted to charge a fee for loan-related services offered by an Islamic bank, provided that the fee relates to service-related expenses.

The service charge can only be calculated accurately after all administrative expenditure has been incurred (at the end of the year). However it is permissible to levy an approximate charge on the client, and then reimburse/claim the difference when the actual expenses are known.

M

Maaliki = Islamic school of law
Islamic school of law founded by Imam Malik Ibn Anas. Followers of this school are known as Maalikis.

Mansil = Shariah compliant property mortgage in the UK

Maysir = gambling
One of three fundamental prohibitions in Islamic finance (the other two being riba and gharar).

The prohibition on maysir is often used as grounds for criticism of conventional financial practices such as speculation, conventional insurance and derivatives.

Muamalat = economic transaction
The lease of land or fruit trees for money, or for a share of the crop.

Mudarabah = trust financing, profit sharing
An investment partnership, whereby the investor (the rab al maal) provides capital to the entrepreneur (the mudarib) in order to undertake a business or investment activity. While profits are shared on a pre-agreed ratio, losses are born by the investor alone. The mudarib loses only his share of the expected income.

The investor has no right to interfere in the management of the business, but he can specify conditions that would ensure better management of his money. In this way Mudarabah is sometimes referred to as a sleeping partnership.

A joint Mudarabah can exist between investors and a bank on a continuing basis. The investors keep their funds in a special fund and share the profits before the liquidation of those financing operations that have not yet reached the stage of final settlement. Many Islamic investment funds operate on the basis of joint Mudarabah.

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GLOSSARY *(continued...)*

Mudarib = entrepreneur in a Mudarabah contract
The entrepreneur or investment manager in a Mudarabah who puts the investor's funds in a project or portfolio in exchange for a share of the profits. A Mudarabah is similar to a diversified pool of assets held in a discretionary asset management portfolio.

Mufawadah = equal, unlimited partnership

Murabahah = cost-plus financing
A form of credit that enables customers to make a purchase without having to take out an interest-bearing loan. The bank buys an item and sells it to the customer on a deferred basis. The price includes a profit margin agreed by both parties. Repayment, usually in installments, is specified in the contract.

The legality of this financing technique has been questioned because of its similarity to riba. However, the modern Murabahah has become the most popular financing technique among Islamic banks, used widely for consumer finance, real estate, the purchase of machinery and for financing short-term trade.

Muqasah = Debt settlement by a contra transaction.

Musaqah = agricultural contract
A contract in which the owner of agricultural land shares its produce with another person in return for his services in irrigating the garden.

Musharakah = joint venture, profit and loss sharing
An investment partnership in which all partners are entitled to a share in the profits of a project in a mutually agreed ratio. Losses are shared in proportion to the amount invested. All partners to a Musharakah contribute funds and have the right to exercise executive powers in that project, similar to a conventional partnership structure and the holding of voting stock in a limited company.

This equity financing arrangement is widely regarded as the purest form of Islamic financing.

The two main forms of Musharakah are:

Permanent Musharakah: an Islamic bank participates in the equity of a project and receives a share of the profit on a pro rata basis. The length of contract is unspecified, making it suitable for financing projects where funds are committed over a long period.

Diminishing Musharakah: this allows equity participation and sharing of profits on a pro rated basis, and provides a method through which the bank keeps on reducing its equity in the project, ultimately transferring ownership of the asset to the participants. The contract provides for payment over and above the bank's share in the profit for the equity held by the bank. Simultaneously the entrepreneur purchases some of the bank's equity, progressively reducing it until the bank has no equity and thus ceases to be a partner.

Muzara'a = agricultural contract
A contract in which one person works the land of another person in return for a share in the produce of the land.

N

Nisab = exemption limit
Exemption limit for the payment of zakat, which differs for different types of wealth.

Qabdh = discount
Qabdh means possession, which refers to a contract of exchange. Generally, qabdh depends on the perception of 'urf or the common practices of the local community in recognizing that the possession of a good has taken place.

Q

Qard = loan

Qard Hasan = benevolent loan
A loan contract between two parties for social welfare or for short-term bridging finance. Repayment is for the same amount as the amount borrowed. The borrower can pay more than the amount borrowed so long as it is not stated by contract.

Most Islamic banks provide interest-free loans to customers who are in need. The Islamic view of loans (qard) is that there is a moral duty to give them to borrowers free of charge, as a person seeks a loan only if he is in need of it. Some Islamic banks give interest-free loans only to the holders of investment accounts with them; some extend them to all bank clients; some restrict them to needy students and other economically weaker sections of society; and some provide interest-free loans to small producers, farmers and entrepreneurs who cannot get finance from other sources.

Qimer = gambling
An agreement in which possession of a property is dependant upon the occurrence of an uncertain event. By implication it applies to those agreements in which there is a definite loss for one party and a gain for the other, without specifying which party will gain and which party will lose.

Quran = the holy scriptures of Islam

continued...

GLOSSARY *(continued...)*

R

Rab al maal = the investor in a Mudarabah contract

Rahn = collateral
An arrangement whereby a valuable asset is placed as collateral for a debt. The collateral may be disposed of in the event of a default.

Riba = interest
An increase, addition, unjust return, or advantage obtained by the lender as a condition of a loan. Any risk-free or "guaranteed" rate of return on a loan or investment is riba. Riba in all its forms is prohibited in Islam.

In conventional terms, riba and "interest" are used interchangeably, although the legal notion extends beyond mere interest.

Riba al Buyu = usury of trade
Also known as riba al fadl.
A sale transaction in which a commodity is exchanged for an unequal amount of the same commodity and delivery is delayed.

To avoid riba al buyu, the exchange of commodities from both sides must be equal and instant. Riba al buyu was prohibited by the prophet Mohammad to forestall riba (interest) from creeping into the economy.

Riba al Diyun = usury of debt
Also known as usury of delay (riba al nasia).
The usury of debt was an established practice amongst Arabs during the pre-Islamic period. It can occur as an excess increment on top of the principal, which is incorporated as an obligatory condition of the giving of a loan.

Alternatively, an excess amount is imposed on top of the principal if the borrower fails to repay on the due date. More time is permitted for repayment in return for an additional amount. If the borrower fails to pay again, a further excess amount is imposed, etc.

Ruq'a = payment order
A payment order to draw money from the bank; used in the early Muslim period.

S

Sadaqah = voluntary charitable giving

Salam = advance purchase
Advance payment for goods which are to be delivered at a specified future date. Under normal circumstances, a sale cannot be effected unless the goods are in existence at the time of the bargain. However, this type of sale is an exception, provided the goods are defined and the date of delivery is fixed. The objects of sale must be tangible goods that can be defined as to quantity, quality and workmanship.

This mode of financing is often applied in the agricultural sector, where the bank advances money for various inputs to receive a share in the crop, which it then sells.

Samad = Shariah compliant property mortgage in the US

Sarf = currency sale
Refers to buying and selling of currencies.

Shafi'e = Islamic school of law
Islamic school of law founded by Abu Abdullah Ahmad bin Idris or Imam Shafie. Followers of this school are known as Shafi'es.

Shariah = Islamic jurisprudence
Islamic cannon law derived from three sources: the Quran, the Hadith and the Sunnah

A "Shariah compliant" product meets the requirements of Islamic law.

A "Shariah board" is the committee of Islamic scholars available to an Islamic financial institution for guidance and supervision in the development of Shariah compliant products.

A "Shariah advisor" is an independent Islamic trained scholar that advises Islamic institutions on the compliance of the products and services with the Islamic law

Shirkah = partnership
A contract between two or more persons who launch a business or financial enterprise to make a profit.

Suftajah = bill of exchange

A bill of exchange between three parties (the payor, the payee and the transmitter), which was used for the delegation of credit during the Muslim period, especially the Abbasides period. It was used to collect taxes, disburse government dues, transfer funds by merchants and was commonly used by traveling merchants. Suftajahs could be payable on a future fixed date or immediately.

It differs from the modern bill of exchange in that a sum of money transferred by suftajah had to keep its identity and payment had to be made in the same currency. Also it usually involved three persons (A pays a certain sum of money to B for agreeing to give an order to C to pay back to A). Finally, a suftajah could be endorsed. The Arabs had been using endorsements (hawala) since the days of the Prophet Muhammad.

continued...

GLOSSARY *(continued...)*

Sukuk = Islamic bond
An asset-backed bond which is structured in accordance with Shariah and may be traded in the market.

A Sukuk represents proportionate beneficial ownership in the underlying asset, which will be leased to the client to yield the return on the Sukuk.

Sunnah = practice and traditions of the Prophet Muhammad

T

Tabarru' = Takaful donation
A contract where a participant agrees to donate a pre-determined percentage of his contribution (to a Takaful fund) to provide assistance to fellow participants. In this way he fills his obligation of joint guarantee and mutual help should another participant suffer a loss. This concept eliminates the element of gharar from the Takaful contract.

Tadlis al' aib = intentionally hiding the defects of goods
Refers to the activity of a seller intentionally hiding the defects of goods. This activity is prohibited according to the Shariah principles.

Takaful = Islamic insurance
Based on the principle of mutual assistance, Takaful provides mutual protection of assets and property and offers joint risk-sharing in the event of a loss by one of the participants. Takaful is similar to mutual insurance in that members are the insurers as well as the insured.

Tanajusy = manipulation
Refers to a conspiracy between a seller and a buyer wherein the buyer is willing to purchase the goods at a higher price. This is done so that others would rush to buy the goods at a higher price, resulting in the seller obtaining a huge profit. This transaction is not permissible in Islam.

Tawarruq = reverse Murabahah
In personal financing, a client with a genuine need buys an item on credit from the bank on a deferred payment basis and then immediately resells it for cash to a third party. In this way, the client can obtain cash without taking out an interest-based loan.

Ta'widh = deliberate delay in payment
Penalty agreed upon by the contracting parties as compensation that can rightfully be claimed by the creditor when the debtor fails or is late in meeting his obligation to pay back the debt.

U

Ujrah = fee
The financial charge for using services, or manfaat (wages, allowance, commission, etc...)

Urbun = deposit
Earnest money which forms part payment of the price of goods or services paid in advance, but will be forfeited in the event the transaction is cancelled. The forfeited money is considered as hibah (gift).

'Uqud al-Mu'awadhart = Contracts of exchange.

'Uqud al-Tabarruat = Charitable contracts.

'Uqud al-Isytirak = Contracts of partnership.

W

Wadiah = safekeeping
The safekeeping of goods with a discount on the original stated cost. An Islamic bank acts as the keeper and trustee of depositors' funds. It guarantees to return the entire deposit, or any part of it, on the depositor's demand.

The bank may give to the depositor a hibah in appreciation.

Wakalah = agency
Absolute power of attorney: where a representative is appointed to undertake transactions on another person's behalf.

In terms of Takaful operations, Wakalah refers to an agency contract, which may involve a fee for the agent.

Waqf = charitable trust
Plural = Awkaf, Awqaf
An endowment or a charitable trust set up for Islamic purposes (usually for education, mosques, or for the poor). It involves tying up a property in perpetuity so that it cannot be sold, inherited, or donated to anyone.

Z

Zakat = religious tax
An obligatory contribution which every wealthy Muslim is required to pay to the Islamic state, or to distribute amongst the poor.

There are two types of zakat:

Zakat al Fitr, which is payable by every Muslim able to pay at the end of Ramadan. This is also called Zakat al Nafs (poll tax).

Zakat al Maal is an annual levy on the wealth of a Muslim above a certain level. The rate paid differs according to the type of property owned.

Global Islamic Bond League Table by Issuer

Full Year 2006							
	Issuer	Nationality	Instrument	Amt US$ m	Iss.	%	Manager
1	Nakheel Development	UAE	Convertible Sukuk Ijarah	3,520	2	23.4	Barclays Capital, Dubai Islamic Bank
2	Malaysia	Malaysia	Islamic Sukuk	2,595	3	17.3	Malaysian Government bond
3	Cagamas	Malaysia	Bithaman Ajil Islamic Securities	1,003	14	6.7	Cagamas, AmMerchant Bank, Aseambankers
4	Rantau Abang Capital	Malaysia	Sukuk Musharakah MTN	999	2	6.6	CIMB, AmMerchant
5	ADIB Sukuk Co	UAE	Sukuk Ijarah	800	1	5.3	HSBC
6	Rafflesia Capital	Malaysia	Periodic Payment Exchangeable Trust Certificates	750	1	5.0	CIMB Investment, HSBC Amanah, UBS
7	Projek Lebuhraya Utara Selatan	Malaysia	Sukuk Musharakah MTN	743	18	4.9	CIMB Investment
8	Aabar Sukuk	UAE	Exchangeable Sukuk Mudarabah	460	1	3.1	Deutsche Bank
9	Putrajaya Holdings	Malaysia	Murabahah MTN	456	9	3.0	Alliance Merchant, CIMB, RHB Sakura
10	Maybank	Malaysia	Bai Bithaman Ajil Subordinated Bonds	416	1	2.8	Aseambankers
11	Jimah Energy Ventures	Malaysia	Istisnah Islamic MTN	308	20	2.0	RHB Sakura, MIMB, Bank Muamalat Malaysia, AmMerchant
12	Segari Energy Ventures	Malaysia	Sukuk Ijarah	258	6	1.7	Aseambankers
13	SIB Sukuk Co	UAE	Musharakah Sukuk	225	1	1.5	HSBC
14	Tabreed 06 Financing Corp	UAE	Sukuk Istisnah	200	1	1.3	CIMB, HSBC, Dresdner Kleinwort Wasserstein
15	KMCOB Capital	Malaysia	Murabahah MTN	178	4	1.2	CIMB Investment, United Overseas Bank (Malaysia)
16	East Cameron Gas Co	US	Asset-backed Sukuk	168	1	1.1	Merrill Lynch International
17	WAPDA First Sukuk Co	Pakistan	Sukuk Ijarah	134	1	0.9	Citibank NA (Pakistan), Jahangir Siddiqui & Co, MCB Bank
18	AmIslamic Bank	Malaysia	Subordinated Sukuk Musharakah	113	1	0.7	AmMerchant
19	Special Power Vehicle	Malaysia	Bai Inah Islamic MTN	110	10	0.7	AmMerchant, Bank Muamalat Malaysia, MIMB
20	Bank Pembangunan Malaysia	Malaysia	Murabahah MTN	109	1	0.7	CIMB, HSBC
	Total of issues used in the table			**15,038**	**273**	**100.0**	

South East Asian Islamic Bond League Table by Issuer

Full Year 2006

	Issuer or Group	Nationality	Instrument	Amt US$ m	Iss.	%	Manager
1	Malaysia	Malaysia	Islamic Sukuk	2,595	3	27.6	Malaysian Government bond
2	Cagamas	Malaysia	Bithaman Ajil Islamic Securities	1,003	14	10.7	Cagamas, AmMerchant Bank, Aseambankers
3	Rantau Abang Capital	Malaysia	Sukuk Musharakah MTN	999	2	10.6	CIMB, AmMerchant
4	Rafflesia Capital	Malaysia	Periodic Payment Exchangeable Trust Certificates	750	1	8.0	CIMB Investment, HSBC Amanah, UBS
5	Projek Lebuhraya Utara Selatan	Malaysia	Sukuk Musharakah MTN	743	18	7.9	CIMB Investment
6	Putrajaya Holdings	Malaysia	Murabahah MTN	456	9	4.8	Alliance Merchant, CIMB, RHB Sakura
7	Maybank	Malaysia	Bai Bithaman Ajil Subordinated Bonds	416	1	4.4	Aseambankers
8	Jimah Energy Ventures	Malaysia	Istisnah Islamic MTN	308	20	3.3	AmMerchant, Bank Muamalat Malaysia, MIMB, RHB Sakura
9	Segari Energy Ventures	Malaysia	Sukuk Ijarah	258	6	2.7	Aseambankers
10	KMCOB Capital	Malaysia	Murabahah MTN	178	4	1.9	CIMB Investment, United Overseas Bank (Malaysia)
11	AmIslamic Bank	Malaysia	Subordinated Sukuk Musharakah	113	1	1.2	AmMerchant
12	Special Power Vehicle	Malaysia	Bai Inah Islamic MTN	110	10	1.2	AmMerchant, Bank Muamalat Malaysia, MIMB
13	Bank Pembangunan Malaysia	Malaysia	Murabahah MTN	109	1	1.2	CIMB, HSBC
14	BNM Sukuk	Malaysia	Sukuk Ijarah	107	1	1.1	Malaysian Government bond
15	Syarikat Pengelar Air Sungai Selangor	Malaysia	Murabahah MTN	103	19	1.1	United Overseas Bank (Malaysia)
16	Penang Bridge	Malaysia	Redeemable Secured Serial Sukuk Istisnah	96	6	1.0	CIMB Investment
17	Perwaja Steel	Malaysia	Murabahah MTN	84	7	0.9	RHB Sakura
18	Mukah Power Generation	Malaysia	Sukuk Mudarabah	83	10	0.9	RHB Islamic
19	Dura Palms	Malaysia	Sukuk Ijarah	77	4	0.8	Avenue Securities
20	Bank Muamalat Malaysia	Malaysia	Bai Bithaman Ajil Islamic Debt Securities	68	1	0.7	HSBC, Standard Chartered
	Total of issues used in the table			**9,396**	**262**	**100.0**	

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Global Islamic Bond League Table by Bookrunner

Full Year 2006				
	Manager or Group	Amt US$ m	Iss.	%
1	Malaysian Government bond	2,702	4	18.0
2	CIMB	1,788	46	11.9
3	Barclays Capital	1,760	2	11.7
4	Dubai Islamic Bank	1,760	2	11.7
5	HSBC	1,479	9	9.8
6	AmMerchant Bank	1,293	43	8.6
7	Aseambankers	839	21	5.6
8	Cagamas	592	8	3.9
9	Deutsche	460	1	3.1
10	RHB	392	66	2.6
11	United Overseas Bank	282	36	1.9
12	UBS	250	1	1.7
13	Alliance Investment	201	16	1.3
14	Merrill Lynch & Co	168	1	1.1
15	Standard Chartered	150	17	1.0
16	MIDF-Sisma Securities	130	32	0.9
17	Bank Muamalat Malaysia	123	31	0.8
18	EON	114	30	0.8
19	Oversea-Chinese Banking Corp	83	11	0.6
20	Avenue Securities	77	4	0.5
	Total of issues used in the table	**15,038**	**273**	**100.0**

South East Asian Islamic Bond League Table by Bookrunner

Full Year 2006				
	Manager or Group	Amt US$ m	Iss.	%
1	Malaysian Government bond	2,702	4	28.8
2	CIMB	1,722	45	18.3
3	AmMerchant	1,293	43	13.8
4	Aseambankers	839	21	8.9
5	Cagamas	592	8	6.3
6	RHB	392	66	4.2
7	HSBC	387	6	4.1
8	United Overseas	282	36	3.0
9	UBS	250	1	2.7
10	Alliance Investment	201	16	2.1
11	Standard Chartered	132	16	1.4
12	MIDF-Sisma Securities	130	32	1.4
13	Bank Muamalat Malaysia	123	31	1.3
14	EON	114	30	1.2
15	Oversea-Chinese Banking Corp	83	11	0.9
16	Avenue Securities	77	4	0.8
17	OSK Asia Securities	22	4	0.2
18	Affin Investment	18	12	0.2
19	Hwang-DBS Securities	8	2	0.1
20	PT (Persero) Danareksa	7	1	0.1
20	PT Andalan Artha Advisindo	7	1	0.1
20	PT Trimegah Securities	7	1	0.1
	Total of issues used in the table	**9,396**	**262**	**100.0**

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Top 10 Islamic Funds by Key Performance Statistics

2006 Returns (in %)				
	Fund	Fund Manager	Performance Statistic	Fund Domicile
1	Futuregrowth Albaraka Equity Fund	Momentum Collective Investments	34.64	South Africa
2	AAA Amanah Syariah Fund	PT Andalan Artha Advisindo Sekuritas	34.20	Indonesia
3	Alfanar Europe Ltd.	TT International	30.20	British Virgin Islands
4	Prudential Dana Al-Ilham (PRUdana Al-Ilham)	Prudential Unit Trusts	29.50	Malaysia
5	Crescent Global Equity Fund	Oasis Global Management Company (Ireland)	29.19	Ireland
6	OSK-UOB Dana Islam	OSK-UOB Unit Trust Management	28.75	Malaysia
7	PNM Syariah	PT PNM Investment Management	27.77	Indonesia
8	Frater Islamic Equity Fund	Frater Asset Management	26.37	South Africa
9	ING Ekuiti Islam Fund	ING Funds	26.23	Malaysia
10	Alliance Dana Adib	Alliance Unit Trust Management	26.20	Malaysia
	Eurekahedge Islamic Fund Index		***1.75***	

Annualised Returns since Inception (in %)				
	Fund	Fund Manager	Performance Statistic	Fund Domicile
1	AlAhli Emerging Markets Trading Equity Fund	The National Commercial Bank	45.56	Saudi Arabia
2	Al Darij Investment Fund	National Investments Company	33.31	Kuwait
3	Intrinsic Crescent Ethical MDA	Intrinsic Investmemt Management	31.55	Australia
4	Frater Islamic Equity Fund	Frater Asset Management	29.09	South Africa
5	Al Dar Securities Fund	ADAM	27.73	Kuwait
6	Egyptian Saudi Finance Bank Mutual Fund	Hermes Fund Management	26.73	Egypt
7	AlAhli Islamic Asia Pacific Equitybuilder Certificates	The National Commercial Bank	24.83	Germany
8	IPB Syariah	PT Kresna Graha Sekurindo	24.02	Indonesia
9	Al Safwa Investment Fund	National Investments Company	23.20	Kuwait
10	Faisal Islamic Bank of Egypt Mutual Fund	Hermes Fund Management	23.16	Egypt
	Eurekahedge Islamic Fund Index		***4.21***	

Notes:
** Ranked by the best Returns / least Standard Deviation / highest Sharpe Ratio, as the case maybe.*
*** Based on 92.6% of the December-2006 NAVs reported to us as at 30-Jan-2007*

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Top 10 Islamic Funds by Key Performance Statistics

Annualised Standard Deviation of Returns since Inception (in %)				
	Fund	Fund Manager	Performance Statistic	Fund Domicile
1	AlAhli Euro Murabahat Fund	The National Commercial Bank	0.12	Saudi Arabia
2	Emirates Dynamic Liquid Fund	Emirates Bank International	0.21	Channel Islands
3	Al Muthanna Islamic Money Market Fund	First Investment Company	0.31	Kuwait
4	TA Islamic CashPlus Fund	TA Investment Management	0.32	Malaysia
5	AlAhli Diversified Saudi Riyal Trade Fund	The National Commercial	0.33	Saudi Arabia
6	Alliance Islamic Money Market Fund	Alliance Capital Asset Management	0.33	Malaysia
7	Lifetime Dana Fayyad	CIMB-Principal Asset Management	0.35	Malaysia
8	AlAhli Diversified US Dollar Trade Fund	The National Commercial Bank	0.38	Saudi Arabia
9	Al Dar Money Market Fund	ADAM	0.42	Kuwait
10	Al Badr Saudi Riyal Fund	Banque Saudi Fransi	0.48	Saudi Arabia
	Eurekahedge Islamic Fund Index		***8.12***	

Sharpe Ratio				
	Fund	Fund Manager	Performance Statistic	Fund Domicile
1	Emirates Real Estate Fund	Belgravia Asset Management	9.14	Channel Islands
2	AlAhli Emerging Markets Trading Equity Fund	The National Commercial Bank	7.68	Saudi Arabia
3	BIG Dana Muamalah Fund	Bhakti Asset Management	5.40	Indonesia
4	Insight I-Hajj Syariah Fund	PT Insight Investments Management	4.46	Indonesia
5	Al Dar Money Market Fund	ADAM	4.30	Kuwait
6	Emirates Dynamic Liquid Fund	Emirates Bank International	3.39	Channel Islands
7	Frater Islamic Equity Fund	Frater Asset Management	3.24	South Africa
8	Al Dar Real Estate Fund	ADAM	2.82	Kuwait
9	Egyptian Saudi Finance Bank Mutual Fund	Hermes Fund Management	2.78	Egypt
10	Asia Pacific Adil Fund	CIMB-Principal Asset Management	2.66	Malaysia
	Eurekahedge Islamic Fund Index		***0.03***	

Notes:
** Ranked by the best Returns / least Standard Deviation / highest Sharpe Ratio, as the case maybe.*
*** Based on 92.6% of the December-2006 NAVs reported to us as at 30-Jan-2007*

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Top 10 Islamic Funds by Fund Geographic Mandate

Global				
	Fund	Fund Manager	Dec-06 Return (%)	Fund Domicile
1	Al Dar Fund of Funds	ADAM	1.68	Kuwait
2	BNP Paribas Islamic Fund Equity Optimiser	BNP Paribas Asset Management	1.40	Luxembourg
3	Emirates Islamic Global Balanced Fund	Emirates Bank International PJSC	1.28	Channel Islands
4	Amanah Global Equity Index Fund	The Saudi British Bank	1.28	Saudi Arabia
5	AlAhli Small Cap Trading Equity Fund	The National Commercial Bank	0.97	Saudi Arabia
6	Citi Islamic Portfolio Equity B	Citi Islamic Portfolios	0.85	Luxembourg
7	Citi Islamic Portfolio Equity A	Citi Islamic Portfolios	0.85	Luxembourg
8	AlAhli Islamic Global Equitybuilder Certificates	The National Commercial Bank	0.70	Germany
9	AlManarah Medium Growth Portfolio	The National Commercial Bank	0.54	Saudi Arabia
10	Tricon Forfaiting Fund	Tricon Trade Management Limited	0.48	Bermuda
	Eurekahedge Global Islamic Fund Index		***0.78***	

Developed Markets (North America, Europe)				
	Fund	Fund Manager	Dec-06 Return (%)	Fund Domicile
1	AlAhli Islamic Europe Equitybuilder Certificates	The National Commercial Bank	3.94	Germany
2	Alfanar Europe Ltd.	TT International	2.91	British Virgin Islands
3	Crescent Global Equity Fund	Oasis Global Management Company (Ireland)	2.54	Ireland
4	NTUC Amanah Equity Fund	State Street Global Advisors	1.86	Singapore
5	Alfanar Investment Holdings N.V.	A.I.H. Investment Management Company	1.18	Netherlands
6	AlAhli Europe Trading Equity Fund	The National Commercial Bank	1.02	Saudi Arabia
7	Alfanar U.S. Large Cap Ltd.	W.P. Stewart Asset Management	0.81	British Virgin Islands
8	Amana Growth	Saturna Capital Corp	0.58	United States
9	Dow Jones Islamic Fund	Allied Asset Advisors	0.37	United States
10	Takaful Global Fund	HSBC Insurance Singapore Pte	0.00	Singapore
	Eurekahedge Developed Markets Islamic Fund Index		***-0.29***	

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Top 10 Islamic Funds by Fund Geographic Mandate

Emerging Markets

	Fund	Fund Manager	Dec-06 Return (%)	Fund Domicile
1	Al Naqaa Asia Growth Fund	Banque Saudi Fransi	3.58	Saudi Arabia
2	AlAhli Emerging Markets Trading Equity Fund	The National Commercial Bank	2.63	Saudi Arabia
3	PNM Syariah	PT PNM Investment Management	2.49	Indonesia
4	AAA Amanah Syariah Fund	PT Andalan Artha Advisindo Sekuritas	2.17	Indonesia
5	PNM Amanah Syariah	PT PNM Investment Management	2.02	Indonesia
6	BIG Dana Muamalah Fund	Bhakti Asset Management	1.54	Indonesia
7	Kotak Indian Shariah Fund	Kotak Mahindra (UK)	-0.27	Mauritius
8	Pakistan International Element Islamic Fund (PIIF)	Arif Habib Investment Management	-0.91	Pakistan
9	Meezan Balance Fund	Al Meezan Investment Management	-1.51	Pakistan
10	Meezan Islamic Fund	Al Meezan Investment Management	-2.25	Pakistan
	Eurekahedge Emerging Markets Islamic Fund Index		***0.62***	

Asia Pacific

	Fund	Fund Manager	Dec-06 Return (%)	Fund Domicile
1	ASBI Dana Al-Falah (previously ASBI Dana Pendidikan)	BIMB UNIT Trust Management Berhad (BUTM)	6.52	Malaysia
2	Intrinsic Crescent Ethical MDA	Intrinsic Investmemt Management	5.66	Australia
3	Alliance Dana Adib	Alliance Unit Trust Management	4.62	Malaysia
4	TA Dana Optimix	TA Investment Management	4.41	Malaysia
5	IPB Syariah	PT Kresna Graha Sekurindo	4.15	Indonesia
6	TA Islamic Fund	TA Investment Management	4.01	Malaysia
7	Apex Dana Al-Faiz-i	Apex Investment Services	3.57	Malaysia
8	MAAKL Al-Fauzan Fund	Meridian Asset Management	3.49	Malaysia
9	MAAKL Al-Faid Fund	MAAKL Mutual	3.27	Malaysia
10	ASBI Dana Al-Munsif (previously ASBI Dana Persaraan)	BIMB UNIT Trust Management (BUTM)	3.11	Malaysia
	Eurekahedge Asia Pacific Islamic Fund Index		***1.25***	

Middle East / Africa

	Fund	Fund Manager	Dec-06 Return (%)	Fund Domicile
1	Egyptian Saudi Finance Bank Mutual Fund	Hermes Fund Management	6.11	Egypt
2	Zajil - Service & Telecommunications Fund	National Investments Company	4.53	Kuwait
3	Mawarid Industrial and Petroleum Services Fund	National Investments Company	4.43	Kuwait
4	Faisal Islamic Bank of Egypt Mutual Fund	Hermes Fund Management	4.43	Egypt
5	Al Darij Investment Fund	National Investments Company	4.30	Kuwait
6	Al Danah GCC Equity Trading Fund	Banque Saudi Fransi	3.91	Saudi Arabia
7	Futuregrowth Albaraka Equity Fund	Momentum Collective Investments	3.30	South Africa
8	Al Safwa Investment Fund	National Investments Company	3.16	Kuwait
9	Al-Bashaer GCC Equity Fund	Gulf Finance House	2.86	Bahrain
10	Al Aseel Islamic Equity Fund	Shamil Bank of Bahrain	2.75	Bahrain
	Eurekahedge Middle East/Africa Islamic Fund Index		***1.14***	

EVENTS DIARY 2007

DATE	EVENT	VENUE	ORGANIZER
February			
13th – 14th	Islamic Finance Asia 2007	Singapore	IQPC
13th	Seminar on Risks, Rewards & the Role of Regulation in Islamic Investment in Real Estate	Amman	IFSB
14th – 15th	Innovations in Islamic Real Estate Investments	Amman	ICG
26th – 27th	Middle East Project Finance	Doha	Middle East Economic Digest
March			
3rd – 4th	The Second GCC Capital Market Forum 2007	Dubai	Gulf Research Center
4th – 5th	World Islamic Finance & Investment Conference	Kuwait	Mega Events
4th – 6th	Islamic & Conventional Securitization	Bahrain	BIBF
6th – 7th	Singapore International Waqf Conference	Singapore	CERT
12th – 13th	2nd Islamic Banks and Financial Institutions Conference	Damascus	Al Salam
18th – 20th	The Asian Banker Summit	Jakarta	
20th – 21st	1st International Conference – Banking & Finance in Libya	Libya	IBC Gulf Conferences
26th – 27th	Takaful Conference	Singapore	Asia Insurance Review
26th	10th Meeting of the IFSB Council	Kuala Lumpur	IFSB
26th	5th General Assembly of the IFSB	Kuala Lumpur	IFSB
26th – 29th	Global Islamic Finance Forum	Kuala Lumpur	Bank Negara & IFSB
27th	4th International Seminar on Challenges Facing the Islamic Financial Services Industry	Kuala Lumpur	IFSB
27th	Interactive Session: "Recent Developments in the Islamic Financial Services Industry: Are They Adding Value To or Diluting the Industry?"	Kuala Lumpur	IFSB
28th – 29th	3rd Seminar on Legal Issues in the Islamic Financial Services Industry: "Surveys on Legal and Shariah Issues in the Islamic Financial Services Industry"	Kuala Lumpur	IFSB
29th	The London Islamic Financial Services Summit	London	City & Financial Conferences
April			
2nd – 5th	International Islamic Finance Forum	Dubai	IIR Middle East
17th – 19th	Inclusive Islamic Financial Sector Development	Brunei	IRTI
19th	Seminar on Regulation of Islamic Capital Markets	Kuala Lumpur	IFSB
24th – 26th	Enhancing Islamic Financial Services for Micro and Medium Sized Enterprises	Brunei	CSM
25th	Sukuk: Exploring the Phenomena	Dubai	Middle East Business Forum
May			
2nd – 6th	Islamic Finance Summer School	Durham	Durham University
6th – 7th	World Islamic Funds & Capital Market Conference	Bahrain	Mega Events
7th – 8th	World Halal Forum 2007	Kuala Lumpur	Kaseh Dia
15th – 16th	4th Islamic Financial Services Board Summit: "The Need For A Cross-Sectoral Approach to the Supervision of Islamic Financial Services"	Dubai	IFSB
17th – 18th	3rd International Conference on Islamic Banking, Finance and Insurance	Ottawa	Ansar Financial Group
21st – 22nd	Commodity Investment Week 2007	Dubai	Terrapinn
22nd – 24th	Islamic World Finance North America 2007	Toronto	Terrapinn
27th – 29th	3rd World Islamic Economic Forum	Kuala Lumpur	ASLI
29th – 30th	32nd Islamic Development Bank Annual Meeting	Senegal	IDB
June			
3rd – 6th	Funds Middle East	Dubai	Terrapinn
25th – 27th	Islamic Finance and Investment World Europe 2007	London	Terrapinn
July			
2nd – 6th	Islamic Markets Program	Kuala Lumpur	Securities Commission
August			
13th – 14th	MIF Forum 2007	Kuala Lumpur	Islamic Finance Events
November			
27th – 28th	3rd Seminar on the Regulation of Takaful	Cairo	IFSB
December			
8th – 10th	The World Islamic Banking Conference	Bahrain	Mega Events