

New issuance rally in June enables 1H14 to outperform; Corporate sukuk sector records bumper contribution

10 July 2014

Highlights

- 1H14's issuances of sukuk posts an increase of 8.2% y-o-y to record USD66.2bln
- June is the second most performing month in 2014 year-to-date worth USD11.6bln
- It is expected for 2014's sukuk to surpass 2012's record USD131.2bln annual issuance volume

The global primary sukuk market has outperformed in the first six months of 2014 as an issuance rally in the month of June has enabled 1H2014's volume to amount to USD66.2bln, an 8.2% higher value as compared to the USD61.2bln volume in the same period last year. The month of June witnessed an increased momentum in the global primary sukuk market as issuers from as many as 9 different domiciles tapped the sector (May-14: 6) ahead of the Islamic month of Ramadan which officially began on June 29th in the Gulf Cooperation Council (GCC) and Malaysia. The month notably saw a heavy contribution from the corporate sukuk sector which contributed more than 45% of the issuance volume (May-14: 21.9%) and was led by some key issuances in the GCC region. June's overall issuances amounted to USD11.6bln which represents a 32.5% surge in volume as compared to the USD8.7bln volume in May. The tremendous issuance activity has now placed June as the second most performing month in 2014 year-to-date (YTD) and the fourth most performing month in the last 12 months (Jun-13-Jun14). Based on 1H2014's performance, some market experts anticipate bumper sukuk issuances activity this year, tipped to surpass 2012's record USD131.2bln annual issuance volume.

One of the most important limelight's during the month of June was the culmination of the race to become the world's first non-Organisation of Islamic Cooperation (OIC) country to issue sovereign sukuk. United Kingdom has officially made history by becoming the first non-OIC jurisdiction to issue a sovereign sukuk instrument, beating the likes of Luxembourg, South Africa and Hong Kong in a development which was eagerly followed by the industry stakeholders since UK's announcement in October last year on its plans to issue sovereign sukuk. The much awaited British sovereign sukuk was finally sold to investors on 25th June, raising GBP200mln (USD339.5mln) for the British Government while providing investors a profit rate of 2.036%. The programme received a very strong demand generating an order book totalling GBP2.3bln or an oversubscription of almost 12 times while attracting diverse investors including sovereign wealth funds, central banks and domestic and international financial institutions. Final geographic allocations of the programme were as follows: United Kingdom (39%); Middle East (37%); and Asia (24%).

By type of issuances, June proved to be a bumper month for the corporate sukuk sector which accounted for USD5.24bln or 45.3% of the total primary market - the highest proportionate share for corporate sukuk

Monthly Sukuk

issuances in 2014 YTD (May14: 21.9%; Apr-14: 17.6%; Mar-14: 12.95%). The sovereign and government-related entity issuers accounted for USD6.34bln or 54.8% of the monthly primary market (May-14: 78.1%; Apr-14: 82%). The remarkable surge in the corporate sukuk share was on account of two fundamental factors:

- 1) Increased volumes of corporate sukuk issued in Saudi Arabia, UAE and Turkey – these three markets issued USD4.4bln worth of corporate sukuks in June; and
- 2) An absence of multilateral / quasi-sovereign issuances by the likes of, for example, the Islamic Development Bank and the International Islamic Liquidity Management Corporation, in June.

Given the increase in the number of jurisdictions tapping the primary market in June, a total of 8 currencies were utilised to issue sukuk in June (May-14: 5 currencies) with the UAE and Turkey being the only two jurisdictions where issuers did not issue in the local currency and instead raised liquidity in US Dollars or Malaysian Ringgit in the case of Turkiye Finans – the Turkish participation bank.

The Malaysian Ringgit accounted for bulk of the issuances, representing 54.9% of the total market (May-14: 77.9%; Apr14: 58%). All Malaysian-domiciled sukuks issued in June were denominated in MYR including the Turkish sukuk by Turkiye Finans. In contrast, issuers in the UAE and Turkey utilised the US Dollars to raise funds and its market share remained consistent at 18.1% in June (May-14: 18.2%). The other jurisdictions including Saudi Arabia issued sukuk in respective local currencies and market shares for each in June were as follows: Saudi-Arabian Riyals (17.71%); Pakistani Rupees (4.3%); Great British Pounds (2.9%); Bahraini Dinar (1.3%); Indonesian Rupiah (0.65%) and the Gambian Dilasi (0.02%).

Analysing by the number of issuances, a total of 65 sukuks were issued in June, a relatively consistent number compared to the previous months (May-14: 62; Apr-14: 68; Mar14: 64). Among these 32 sukuks were issued by the corporate sector totalling USD5.24bln vs 30 corporate sukuk issued in May worth a much lesser USD1.9bln. June's value of corporate sukuk had been substantially uplifted by huge tranches issued in Saudi Arabia, UAE and Turkey. Meanwhile, 29 sukuks (including short-term central bank sukuks) were issued by sovereign issuers totalling USD5.44bln vs 31 sukuk and USD6.13bln volume in May. In addition four government-related entity sukuks in Malaysia worth USD902mln were issued in June as compared to one issuance in UAE in May worth USD700mln.

By structures of issuances, Murabahah and Ijarah remain the popular choice of sukuk issuers accounting for 50.6% and 13.8% of the total issuances in Jun-14, which is a slightly reduced share as compared to the 63.7% and 17.5% shares in the previous month. Instead, nearly 18% of the sukuks were hybrid structures

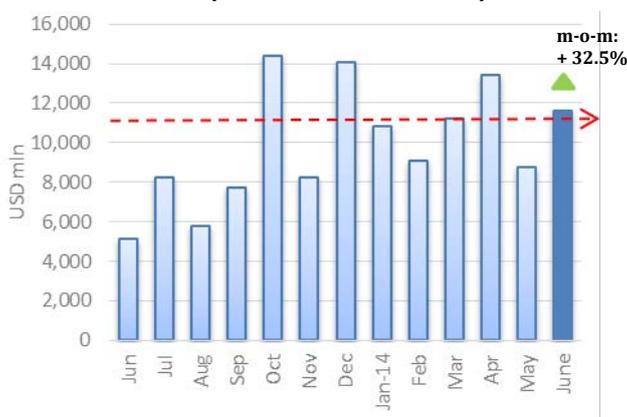
Monthly Sukuk

incorporating more than one underlying Shari'a compliant contract. Such structures are popular in the GCC where a combination of mudarabah and murabahah are widely used to structure sukuk.

By sector, the government issuances accounted for 47% or USD5.44bln of total issuances in June (May-14: 72.5% or USD6.34bln), followed by the financial services sector with a 31.2% or USD3.62bln share (May-14: 14.6% or USD1.27bln). The real estate sector accounted for 9.1% or USD1.06bln of the issuances volume while the other sectors accounted for the remaining 12.7% or USD1.47bln of the volume issued in June.

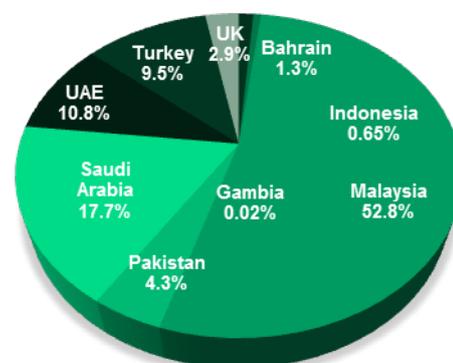
Moving forward, based on 1H2014's performance, the outlook for the global sukuk market remains promising and it is expected that 2014 may surpass 2013's annual issuances volume of USD119.7bln. The horizons of the sukuk market continue expanding as more and more jurisdictions tap the market with an increased number of business sectors issuing sukuk. To date, at least 29 jurisdictions have tapped the sukuk market (excluding offshore domiciles) and more are expected to follow suit following UK's highly successful sovereign sukuk programme. A number of efforts are being directed towards enabling sukuk to serve as viable tools for meeting global liquidity needs - for example, to support Africa's infrastructural development needs. The number of sectors utilising sukuk has also grown – for example, Etiqa Takaful became the world's first takaful operator to issue sukuk in May this year. Regulatory efforts have also been instrumental in streamlining the procedures to issue sukuk instruments. Several challenges which hampered growth of the sukuk industry, including lack of benchmark standards, guiding principles, regulatory structures, and cross-border liquidity problems, among others, are now being resolved by the efforts of various multilateral organisations such as the Islamic Financial Services Board, Islamic Development Bank, World Bank, and the Asian Development Bank, among others. In conclusion, in spite of various macroeconomic challenges and uncertain financial conditions at the start of this year, global primary sukuk market in 1H2014 has outperformed the previous year.

Global Primary Sukuk Market Issuances Trend (June 2013-June 14)



Source: Bloomberg, Zawya, IFIS, KFHR

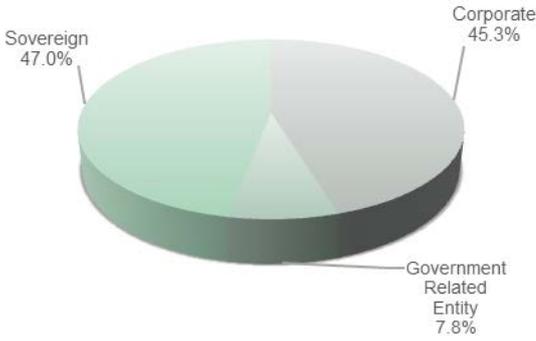
Global Primary Sukuk Market Issuances by Domicile (June-14)



Source: Bloomberg, Zawya, IFIS, KFHR

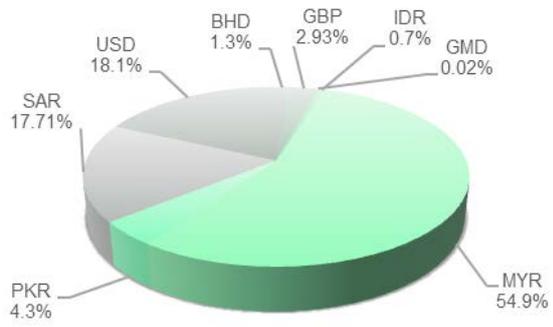
Monthly Sukuk

Sukuk Issuance by Type (June-14)



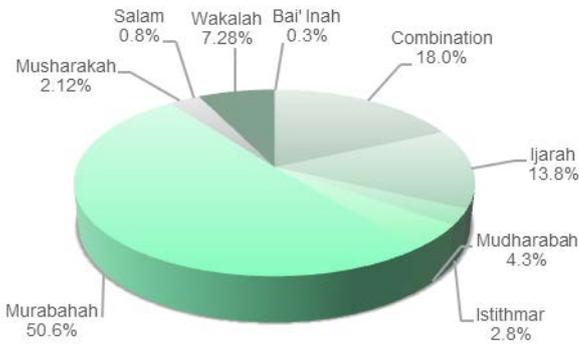
Source: Bloomberg, Zawya, IFIS, KFHR

Sukuk Issuance by Currency (June-14)



Source: Bloomberg, Zawya, IFIS, KFHR

Sukuk Issuance by Structure (June-14)



Source: Bloomberg, Zawya, IFIS, KFHR

Sukuk Issuance by Structure (June-14)



Source: Bloomberg, Zawya, IFIS, KFHR

KFH Research Ltd

By accepting this publication you agree to be bound by the foregoing terms and conditions.

KFH Research Ltd has prepared this publication for general information purposes only and this does not constitute a prospectus, offering document or circular or offer, recommendation or invitation or solicitation to purchase, subscribe for or sell any security, financial product or other investment instrument ("Investments"), or to engage in, lead into, conclude or refrain from engaging in any transaction.