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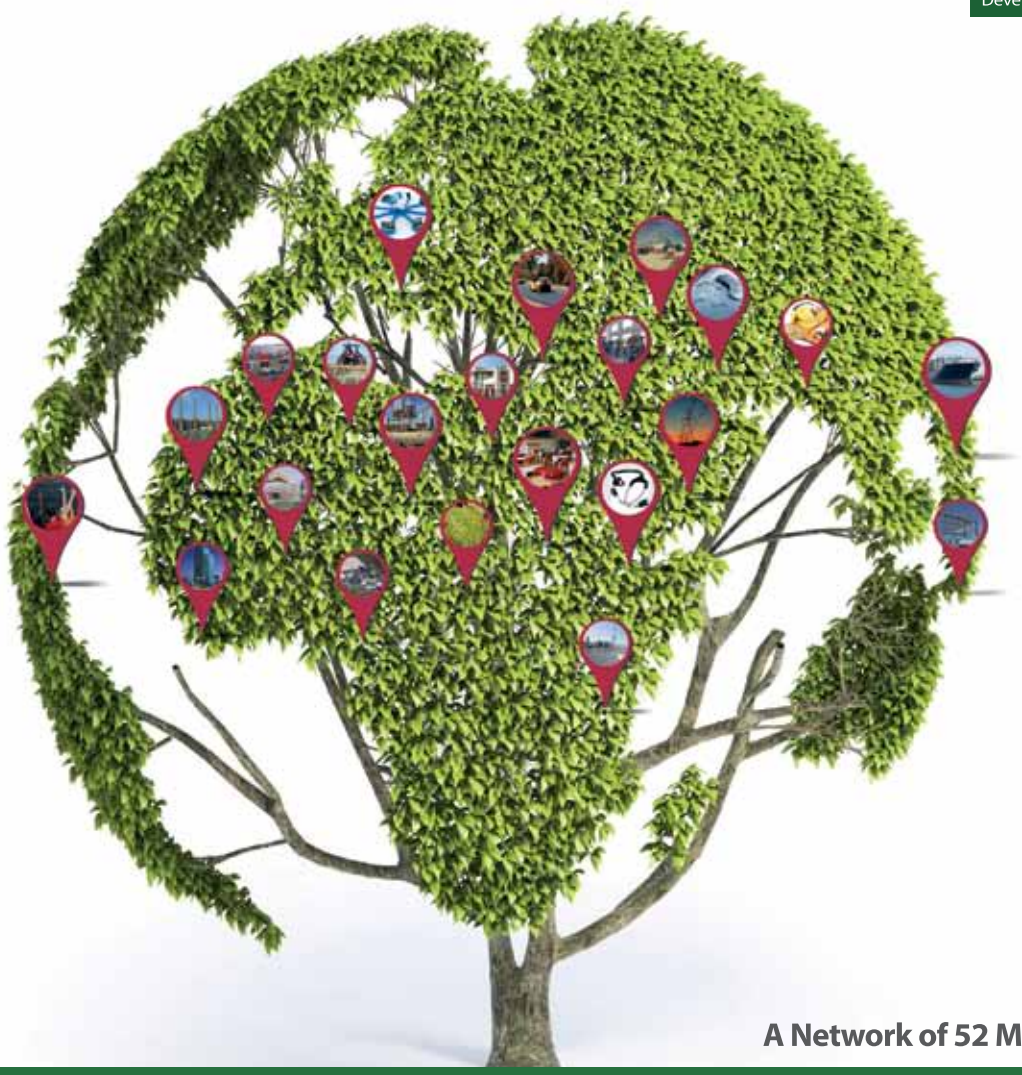

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Printed by:
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No 2 , Jalan SR 4/19, Ground Floor , Taman Serdang Raya
43300 Seri Kembangan, Selangor

www.IslamicFinanceNews.com

Editor's Note

It's been quite a year for the Islamic capital markets, and with a line of landmark deals marching their way through the months of 2014 there can no longer be any doubt of the position the sector holds as the golden child of the Islamic finance industry.

The Shariah compliant capital markets this year have not only grown in terms of size and sophistication but have made strides in global reach, mainstream acceptance and investor demand.

Increasingly innovative structures to meet the complex treasury demands of both financial and corporate institutions have developed in the private sector, while on the sovereign side the debut offerings from nations as diverse as the UK, Luxembourg, Pakistan, South Africa and Sharjah.

In our quarterly Capital Markets Guide we bring you a round up of the markets from all angles and aspects, and covering areas across the globe. From Africa to Asia, Europe to the Middle East and not forgetting the growing potential of the United States, the guide provides a comprehensive round-up of market activity throughout the year.

In addition, the results of our annual Islamic Investor Awards demonstrate just how competitive and sophisticated the industry has become – with a strong showing from all regions making the honors one of the most closely contested and prestigious battles of the year.

We wish all our readers a fruitful festive season and a productive start to 2015.

Lauren Mcaughtry,
Managing Editor

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2014: Year of the sovereigns

New entrants, groundbreaking deals, and spiking interest – the Islamic capital markets in 2014 have certainly been nothing short of exciting. But even with so many new players in the arena, has the stage seen any real innovation compared to the year before? Follow VINEETA TAN as she identifies the major Sukuk trends of the year and compares them with those of 2013 to track the latest capital market progress.

Fresh faces

One of the most prominent features of this year has undeniably been the entry of new players. From the UK to Hong Kong, 2014 has welcomed more non-traditional Sukuk issuers (sovereigns and non-sovereigns) in one year than in the last several put together, bearing testament to the growing acceptability of Shariah compliant instruments from financial communities around the world.

"A lot of excitement this year has been the new entrants. This new stream of issuers definitely created depth in the market," confirmed Rizwan Kanji, a partner with King & Spalding, to IFN. It is widely agreed that the Sukuk buzz was ignited when the UK announced its Sukuk plans in October 2013, which set in motion a great Sukuk race between itself, Luxembourg, Hong Kong and South Africa. It was indeed a wrestle between these economic powerhouses till the finish line, but they each made it to the podium and were significant in their own right. Given that for established global financial centers like Hong Kong, the UK and Luxembourg a Sukuk issuance is more of a calculated symbolic move rather than out of financial necessity, and that there are questions surrounding the commitment to a Sukuk program following their inaugural offerings, tapping the Islamic market as a strategic move to position themselves in the Shariah compliant financial universe showcases the strength of the Islamic finance industry, or at the very least, the power of Muslim wealth.

"It is interesting to see Hong Kong and the UK issuing in general, because although it is symbolic in the larger scheme of things but

Table 1: Selected Sukuk issuers of 2014

Issuer	Size/Value	Structure	Orderbook received (approximate)	Profit rate (%)	Tenor (years)	Date Issued
The UK	GBP200 million	Ijarah	GBP3 billion (unconfirmed)	2.03	5	2nd July
Senegal	XOF100 billion	Ijarah	NA	6.25	4	18th July
Goldman Sachs	US$500 million	Wakalah (51%)				
Murabahah (49%)	US$1.5 billion	2.84	5	16th September		
Sharjah	US$750 million	Ijarah	US$7.85 billion	3.76	10	17th September
Hong Kong	US$1 billion	Ijarah	US$4.7 million	2	5	18th September
South Africa	US$500 million	Ijarah	US$2 billion	3.9	5.75	24th September
Bank of Tokyo Mitsubishi (Malaysia)	US$500 million (multicurrency JPY and US$)	Wakalah	NA	NA	1	25th September
Luxembourg	EUR200 million	Ijarah	EUR500 million	0.44	5	30th September
Turkey	US$1 billion	Ijarah	US$3.4 billion (minimum)	4.48	10	18th November
Pakistan	US$1 billion	Ijarah	US$2.3 billion	6.75	5	27th November

Source: Dealogic

Table 2: Global Islamic finance debt capital market volume - Ranking by Top 10 issuer parents

01 Jan - 15 Oct 2014					01 Jan - 15 Oct 2013				
Rank	**Issuer parents**	**Deal Value US$ million**	**No.**	**%share**	**Rank**	**Issuer parents**	**Deal value US$ million**	**No.**	**%share**
1	Saudi Electricity Co	3,700	2	10.9	1	General Authority for Civil Aviation - GACA	4,056	1	13.9
2	Islamic Development Bank	3,000	2	8.8	2	Saudi Electricity Co	2,000	1	6.9
3	Public Investment Fund - PIF	2,081	3	6.1	3	Sadara Chemical Co	2,000	1	6.9
4	DanaInfra Nasional Bhd	1,617	5	4.8	4	Republic of Indonesia	1,500	1	5.2
5	Republic of Indonesia	1,500	1	4.4	5	Republic of Turkey	1,250	1	4.3
6	Khazanah Nasional Bhd	1,260	6	3.7	6	Tenaga Nasional Bhd	1,124	2	3.9
7	Tenaga Nasional Bhd	1,109	1	3.3	7	Islamic Development Bank	1,094	2	3.8
8	National Higher Education Fund Corp - PTPTN	1,074	2	3.2	8	Dubai Islamic Bank PJSC	1,000	1	3.4
9	Hong Kong Special Administrative Region - HKSAR	1,000	1	2.9	8	Dubai Electricity & Water Authority - DEWA	1,000	1	3.4
10	Bank Pembangunan Malaysia Bhd	948	1	2.8	10	Emirates Group	993	1	3.4
	Total	34,016	94	100.0		Total	29,104	89	100.0

Source: Dealogic

it indicates an interest which could materialize in more than one issuance and encourage corporates to follow through," explained Bashar Al Natoor, a director at Fitch Ratings and an Islamic finance specialist, to IFN.

Non-conventional currencies

Equally compelling is the fact that the UK and Luxembourg issued Sukuk in less traditional currencies: pounds sterling and euros, respectively, as opposed to the popular US dollar and Malaysian ringgit denominations – another noteworthy trend. Apart from sterling and euros, Bank of Tokyo-Mitsubishi (Malaysia) followed with another unconventional currency, Japanese yen, for its US$500 million Sukuk – the first in the world. These papers were all heavily oversubscribed, demonstrating the phenomenal demand for non-dollar (or ringgit)-denominated Sukuk and mirroring the deepening maturity of the Islamic capital markets and their expanding investor base.

"I would not be surprised if we were to see a samurai Sukuk or dimsum Sukuk simply because we have seen the sterling, and the euro, and I think that as Islamic financial institutions become global in their business outlook, the most natural hedging strategy is to have the same incoming and outgoing currency so I think we may see an expansion in market of currencies being issued in. Whether or not it will happen next year or in the medium to long-term, I can't say although I do believe that it is a bit further away. But again this is something that will probably happen - just not next year," said Rizwan.

It is undeniable that the Sukuk market has picked up the pace this year, most notably in new markets - but as Jawad Ali, managing partner of King & Spalding, asks: "Is this going to be effective enough to actually attract corporate, whether they are Shariah compliant or not, to actually follow through and issue Sukuk?" The key now is to harness the great momentum gathered from these high profile deals and channel it towards furthering the Islamic finance industry with repeat Sukuk programs, tax incentives and the likes. "If this stops at these new entrants, and if this list does not expand, then I think that's a lost opportunity for the growth of Islamic finance," cautioned Rizwan.

Table 3: Global Islamic Finance DCM Volume since 2013

Deal pricing date by quarter	Deal Value US$ million	No.
1Q 2013	10,556	31
2Q 2013	8,411	34
3Q 2013	7,733	20
4Q 2013	11,715	34
1Q 2014	10,856	27
2Q 2014	12,528	37
3Q 2014	10,406	29
4Q 2014 (end of October)	225	1

Source: Dealogic

So with the expansion of the Sukuk universe, is it safe for us to characterize 2014 as an exceptional year? Excellent year – most definitely, but groundbreaking? Perhaps not.
"We saw a comeback in volume of Sukuk issuance in general, which was expected, but we did not really see a breakthrough in volume as the level of issuance is still within similar regions," said Bashar.

Bashar's sentiments resonated with the UK's BLME, which noted in its latest Sukuk commentary: "Despite 2014 not being a record year it has been a landmark year for the Sukuk markets and the Islamic finance industry as a whole due mainly to the new entrants to the market, particularly the issues from outside of the GCC region and Malaysia."

Table 4: Global Islamic finance DCM volume - Ranking by deal region									
01 Jan - 15 Oct 2014					01 Jan - 15 Oct 2013				
Rank	Deal Regions	Deal Value $ (m)	No.	%share	Rank	Deal Regions	Deal Value $ (m)	No.	%share
1	Southeast Asia	16,465	71	48.4	1	Middle East	16,410	17	56.4
2	Middle East	13,362	14	39.3	2	SE Asia	10,394	67	35.7
3	Europe	2,188	6	6.4	3	Europe	2,200	4	7.6
4	North Asia	1,000	1	2.9	4	North Asia	100	1	0.3
5	Africa	500	1	1.5					
5	North America	500	1	1.5					
	Total	**34,016**	**94**	**100.0**		**Total**	**29,104**	**89**	**100.0**

Source: Dealogic

Speaking to IFN Ayman Khaleq, a partner of Morgan, Lewis and Brockius, offered his analysis: "We have not yet seen a comeback for private sector corporate Sukuk. Although there have been some Sukuk issuances and the trajectory is very positive but I think the industry has yet to establish itself in this part of the world as a viable funding alternative to family offices and the pure private sector."

According to Kuwait Finance House (KFH), the corporate Sukuk sector was ostensibly dominated by Southeast Asian obligors: with Malaysian entities leading the pack with 22 tranches worth a collective US$781.2 million (as at the end of October 2014). Overall, corporate issuance accounted for 12.6% or US$1.05 billion of the monthly Sukuk issuance volume in October. The month concluded with a notable absence of corporate issuers from the GCC and Turkey, presumably on account of various geopolitical challenges in the region. KFH also noted that the primary Sukuk market, for the third consecutive year, had exceeded the US$100 billion milestone in the first 10 months of the year.

Year-end rush

The year began on a shaky note as the US' quantitative easing plans sparked concerns among investors however, the Islamic debt capital markets rode out the waves of volatility relatively well, leveraging from a shortfall of Sukuk supply and large demand for US dollar-denominated papers buoyed by fairly strong fundamentals of the Gulf region.

"Statistically, if you cut off the period at 30th June, we are slightly above last year but we are no where the exciting levels of 2012,

Table 5: Global Islamic finance DCM volume - Ranking by sector									
01 Jan - 15 Oct 2014					01 Jan - 15 Oct 2013				
Rank	Sector	Deal Value $ (m)	No.	%share	Rank	Sector	Deal Value $ (m)	No.	%share
1	Finance	15,020	34	44.2	1	Government	8,072	6	27.7
2	Utility & Energy	6,025	8	17.7	2	Finance	6,017	23	20.7
3	Government	5,130	9	15.1	3	Utility & Energy	5,588	11	19.2
4	Real Estate/Property	3,354	14	9.9	4	Transportation	2,419	8	8.3
5	Construction/ Building	1,583	9	4.7	5	Chemicals	2,000	1	6.9
6	Transportation	1,255	4	3.7	6	Agribusiness	1,452	3	5.0
7	Telecommunications	810	4	2.4	7	Real Estate/ Property	861	11	3.0
8	Agribusiness	311	2	0.9	8	Food & Beverage	807	6	2.8
9	Holding Companies	200	3	0.6	9	Construction/ Building	520	6	1.8
10	Food & Beverage	131	2	0.4	10	Holding Companies	467	3	1.6
11	Insurance	93	1	0.3	11	Telecommunications	211	2	0.7
12	Retail	87	1	0.3	12	Metal & Steel	202	3	0.7
13	Professional Services	7	1	0.0	13	Oil & Gas	171	2	0.6
14	Oil & Gas	6	1	0.0	14	Retail	159	2	0.6
15	Consumer Products	3	1	0.0	15	Machinery	145	1	0.5
					16	Professional Services	12	1	0.0
	Total	34,016	94	100.0		Total	29,104	89	100.0

Source: Dealogic

Table 6: Global Islamic Finance DCM Volume - Ranking by Top 10 Bookrunners									
01 Jan - 15 Oct 2014					01 Jan - 15 Oct 2013				
Rank	Bookrunner Parents	Deal Value $ (m)	No.	%share	Rank	Bookrunner Parents	Deal Value $ (m)	No.	%share
1	CIMB Group	5,374	38	15.8	1	HSBC	6,267	23	21.5
2	HSBC	4,953	27	14.6	2	Standard Chartered Bank	2,645	19	9.1
3	Maybank	3,858	31	11.3	3	Saudi National Commercial Bank	2,153	2	7.4
4	Standard Chartered Bank	2,534	17	7.5	4	Deutsche Bank	2,075	4	7.1
5	RHB Capital Bhd	2,107	28	6.2	5	AmInvestment Bank Bhd	1,797	19	6.2
6	AmInvestment Bank Bhd	1,972	21	5.8	6	CIMB Group	1,655	26	5.7
7	Emirates NBD PJSC	1,430	12	4.2	7	RHB Capital Bhd	1,569	25	5.4
8	JPMorgan	1,344	3	4.0	8	Maybank	1,476	22	5.1
9	National Bank of Abu Dhabi PJSC	1,299	10	3.8	9	Citi	1,395	8	4.8
10	Deutsche Bank	1,142	4	3.4	10	Emirates NBD PJSC	859	7	3.0
	Total	34,016	94	100.0		Total	29,104	89	100.0

Source: Dealogic

although to me 2012 should not be the benchmark as it was an anomaly," said Rizwan. "But I nonetheless do think it is very pleasing to see that the level of issuances for the first half has been encouraging. It's been a better year as compared to 2013." September emerged to be the most active month driven mainly by sovereigns including the UK, Hong Kong, Luxembourg, Indonesia, South Africa and Sharjah. This surge in activity however began to decline moving into October as figures show that the month recorded a 36% month-on-month drop in Sukuk volume to US$8.7 billion as compared to September's US$12.94 billion. Yet the final quarter of the year is likely to finish off strong as a flurry of issuance made its way into the second half of November, compensating for the lull of October and early November.

Welcoming Sukuk from UAE low cost airlines flydubai and Saudi's Advanced Petrochemical Co among others, the arguably most significant program of November could however be Republic of Turkey's maiden 10-year US$1 billion sovereign Sukuk. Attracting over thrice in demand, the paper is only the third sovereign Sukuk (after Malaysia and Indonesia) to possess a longer 10-year maturity as opposed to five years. This conscious decision for a longer tenor by the Turkish government represents yet another step in the right direction of a maturing Sukuk market. Mohamad Safri Shahul Hamid, senior managing director and deputy CEO of CIMB Islamic (one of the joint lead manager for this deal), described to IFN that: "This transaction is extremely significant to the government as it helps create a new benchmark curve for Turkey and at the same time reinforces the government's continued commitment towards Islamic finance."

The program is unique not only because of its tenor but because of the nature of the issuer. As a rated sovereign who is active in both conventional and Islamic capital market space, this latest offering from Turkey provides the rare opportunity to market players to study and compare Islamic facilities with their conventional counterparts. The issuance has indeed opened the market and expanded the investment horizon of investors beyond the previously favored five-year sweet spot. "In short, the success of this transaction and the recent government of Indonesia trade had also helped alleviate whatever concerns the market (had) in terms of Sukuk longevity and are expected to pave the way for the other issuers, sovereigns and corporates to consider a longer tenure for their own global Sukuk issuances," explained Safri.

The pipeline in the last two months of 2014 remained robust, with issuances from the the International Finance Facility for Immunization (for which the World Bank acts as treasury manager), a new sovereign from Pakistan and additional International Islamic Liquidity Management Corporation paper, among others.

Bright horizon

So what's in store for the Islamic capital markets moving forward next year? Speaking to industry players, IFN observed two main consensuses: continued strong performance, and the rise of emerging markets - particularly in the African region.

"I think next year is going to be another strong year for the Sukuk industry. I do believe there will be a stabilization of the Sukuk markets in the sense that we will continue to see strong performance of the Sukuk market leaning towards a trend of issuing new Sukuk in the Middle East and in Malaysia. I also expect to see more are corporate Sukuk including mezzanine-type Sukuk and Sukuk issuances in the non-Islamic jurisdictions by the private sector be it in the US or in Europe." projected Ayman.

Rizwan agrees: "I think we will continue to see the same trends, we will see a lot of old issuers coming back because a lot of them have maturities that are approaching for existing papers. We will see a lot more from the emerging markets, particularly the East African zone – the legal infrastructure is already in place for the purpose of Sukuk issuances and Islamic finance generally. There is definitely opportunity there and we hope to see it materialize." And while Ayman thinks that emerging markets such as those in Africa will be more opportunistic but he remains cautiously optimistic: "Would those initiatives be led by countries that have an existing or upcoming energy industry? Or are the African countries ready for infrastructure Sukuk? Are lenders ready to do that? My guess is that in Africa you will either find sovereigns or energy-based Sukuk."

Venturing into a new realm: Sukuk issuances by corporates in non-Islamic jurisdictions

Follow AYMAN A KHALEQ and AMANJIT K FAGURA as they discuss the rising popularity of Sukuk among non-Islamic issuers and issues surrounding asset-backed and asset-based Sukuk.

The past several years have seen a steady, though slow, rise in the number of Sukuk being issued by and to non-Islamic entities from non-Islamic jurisdictions. Such Sukuk issuances often encounter a number of legal, accounting, tax, and obviously Shariah structuring issues which tend to vary depending on the type of assets backing such Sukuk issuances, as well as the domicile of such assets. Whilst there has been much debate on the topic of 'asset-backed' versus 'asset-based' Sukuk issuances, the general preference for Sukukholders and Shariah scholars alike is for the former asset-backed structures which are viewed by some as more in line with the principles of Shariah in light of the 2008 financial crisis. Nevertheless, asset-based structures are still widely used in the markets to date although with the expanding desire for Sukuk in the conventional market this could be set to change.

Why Sukuk?

With the limited liquidity offered in conventional markets in comparison to the growing Islamic markets, Sukuk issuances are ever increasingly being utilized by conventional entities to raise finance. This allows such entities to diversify their sources of funding and 'tap' into a less utilized market (in comparison to conventional sources of funding).

Whilst the Shariah requirements of such transactions can be a deterrent for conventional investors such investors are also becoming more aware of the opportunities and profits that can be achieved through Shariah compliant issuances; which ultimately outweighs the cons. Additionally, as western securitization markets are more accustomed to and comfortable with 'true sale' type transactions, this provides an opportunity for the Islamic finance market to also benefit from an increase in truly 'asset-backed' structures. This is especially true in securitization and non-recourse financing transactions in the conventional sphere.

Although asset-backed Sukuk issuances are preferred, asset-based issuances are still the most widely used form and are accepted in the markets by the majority of Shariah scholars. As mentioned previously, in practice, few Sukuk issuances are truly asset-backed. This is due to a combination of factors such as market appetite (i.e. originators not wanting to transfer legal ownership of their assets and investors not being driven by Shariah considerations), regulatory limitations in the jurisdiction in which the assets are located, the nature and lack of suitability

of the underlying assets (i.e. are they Shariah compliant), the costs involved in a true sale and transfer of ownership (i.e. the costs of transferring legal title to land and property) and the practicalities of transferring ownership in the underlying asset which may impact the value of the same (i.e. properties which are leased or insurance policies held by individuals).

Is there a future for purely asset-backed Sukuk?

In light of the limitations in issuing purely asset-backed Sukuk which are well publicized in the market, some may argue that asset-based issuances will not be superseded by asset-backed issuances any time soon. In fact, many Sukuk transactions in the market try to emulate an asset-backed structure as far as they are able to do so in order to provide Sukukholders and Shariah scholars with as much comfort as possible. For example, an asset-based transaction may; (i) still derive its payments to Sukukholders from the underlying assets; and (ii) provide additional security over the assets or rights to such assets on a default to Sukukholders – these are typically not the features of an asset-based Sukuk issuance.

Notwithstanding the above, if non-Islamic entities continue to invest in or issue Sukuk a shift to asset-backed deals is possible.

Examples of successful Sukuk issuances to corporates in non-Islamic jurisdictions

Below is a brief overview of a few deals that support the notion of the emergence of asset-backed Sukuk in conventional markets.

East Cameron Sukuk
The US$165 million East Cameron Sukuk issuance in 2006 by East Cameron Partners, utilized a Musharakah structure, and allocated the proceeds of the Sukuk issuance towards capital and operating costs relating to Gulf of Mexico oil and gas assets. At the time, the transaction was the first Sukuk issuance by a US corporate, and the first Sukuk issuance globally to be backed by oil and gas rights, in this case over-riding royalty interests (ORRI). The transaction was truly asset-backed as the agreed ORRI were transferred to the Sukukholders and an appropriate true sale opinion was procured.

Ultimately, East Cameron Partners filed for Chapter 11 bankruptcy in Louisiana, and the court ruled that the transfer of title over the ORRI in favor of the Sukukholders should be upheld, despite claims by East Cameron Partners that the transaction should be re-characterized as a secured loan.

FWU AG Salam Sukuk
In October 2013, Atlanticlux Lebensversicherung, a 'BBB'-rated multinational insurance provider based in Luxembourg and a subsidiary of German-based FWU, issued US$20 million Sukuk as part of the first series of a US$100 million Sukuk Wakalah program. The second series for US$40 million was issued in March 2014. The Sukuk was issued in Guernsey through an incorporated cell company which was regulated as a reinsurer by the Guernsey Financial Securities Commission. Both series of the transaction are tradeable and were listed on the Channel Islands Securities Exchange with settlement through Euroclear/ Clearstream.

The transactions were a first of their kind and involved participation by the Sukukholders in the risks associated with and hence the revenues generated from certain tariffs relating to a pre-determined Shariah compliant block of life insurance contracts originating in Italy, France and/or Germany. The participation by the Sukukholders in such risks and revenues gave rise to a quasi-ownership over the receivables to such assets pursuant to the declaration of trust.

The revenues generated from the underlying insurance blocks were accumulated on a monthly basis and paid out as distribution amounts to Sukukholders each quarter alongside payment to service providers of other fees and expenses due under the transaction. Hence whilst not an asset-backed transaction per se the deal had certain nuances akin to such structure.

Both series of the program were also rated in Europe by Fitch and attracted institutional treasury investors in both the Middle East and Europe.

New deal
Currently a US entity is in the process of issuing a Sukuk on an Ijarah basis over a portfolio of rail cars owned by a third party US entity and located in the US. The transaction is expected to involve a true sale of the rail cars hence giving it the asset-backed nature the Islamic market prefers.

> "Whilst there is a lack of regulatory framework in place to truly spearhead a transition from asset-based to asset-backed Sukuk it is also evident that the conventional legal community may be able to assist in promulgating the transition without a definitive framework"

Conclusion

Whilst there is a lack of regulatory framework in place to truly spearhead a transition from asset-based to asset-backed Sukuk it is also evident that the conventional legal community may be able to assist in promulgating the transition without a definitive framework. However, this is ultimately dependent on how developed the markets are in the jurisdictions in which Sukuk are being issued, as well as the appetite of Islamic investors to venture into new markets – and the conventional markets themselves, to venture into the realms of Islamic finance.

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IFN Islamic Investor Awards 2014: Bringing you the best

IFN is delighted to announce the distinguished winners of the inaugural Islamic Investor Awards, honoring the key players driving forward the fast-growing Shariah compliant funds industry. LAUREN MCAUGHTRY rounds up the leading lights of the landscape as elected through its most prestigious accolades.

Previously the IFN Asset Management Poll, this year IFN took the radical step of readjusting. In an industry becoming indundated with polls and prizes that no longer focused on the primary issues of performance, progression, innovation and originality, we saw the online polls become a platform for the biggest and best-recognized firms to reiterate their positions while smaller managers struggled for recognition. While recognizing the achievements of the major players, we realized it was time to shake things up.

Following IFN's policy of promoting independent and unbiased analysis across the industry, based on the success of the similarly-structured IFN Deals of the Year and leveraging our unrivalled network, we therefore assembled a confidential global advisory board of non-competing experts to review the industry and select the foremost players in their fields based on real performance and progress. Asset management firms with Shariah funds were invited to submit in a series of categories, following which the board undertook a rigorous process of assessment and exclusion to identify award-winners based on a wide range of factors including but not limited to range, reach, returns and relevance.

Collated and reported by IFN, the results represent a comprehensive overview of industry activity over the past year: with industry stalwarts and old favorites standing alongside neophytes and new entrants. The breadth of entries and range of global markets and sectors illustrate the exciting advances made by Islamic asset management; and we extend our most sincere congratulations to all our award-winners.

Category	Winner
Best Overall Islamic Asset Management Company	Franklin Templeton
Best Islamic Asset Management Company in Asia	Franklin Templeton
Best Islamic Asset Management Company in the Middle East	Al Rayan
Best Islamic Asset Management Company in Africa	Oasis Crecent Capital
Best Islamic Asset Management Company in Europe	BLME
Best Islamic Asset Management Company in the Americas	Saturna Capital
Best Investor Relations	Public Mutual
Best Investment Strategist	AmInvest
Most Innovative Islamic Asset Management Company	Arabesque Asset Management
Best Institutional Solutions Provider	EPF
Best Fund Distributor	CIMB-Principal Islamic
Best Regional Fund Performance	Al Meezan
Best Thematic Fund Performance	Asiya Investments
Best Sector Fund Performance	AZ Global
Best Funds Domicile	Luxembourg

Industry leaders

A global leader in asset management with offices in over 150 countries worldwide and a track record spanning over 65 years, Franklin Templeton Investments is one of the biggest names in the game. Winner of both **Best Overall Islamic Asset Management Company** and **Best Islamic Asset Management Company in Asia**, the firm stands out for its global multi-manager capabilities, broad geographical presence and focus on size and strength of performance.


Sandeep

The group has made a concerted commitment to the Islamic industry with major offices in Malaysia and the Middle East; nine lead portfolio managers under its Global Equity, Emerging Markets and Local Asset Management teams; and a range of 12 funds including three Shariah compliant, Luxembourg-domiciled SICAV funds (FTS) and nine Shariah mandates. With Shariah compliant global assets under management of US$2.01 billion out of a total US$922.2 billion the group may not be the biggest player on the market, but with annual AUM growth of 28.49% over the past year it has demonstrated exceptional and consistent performance along with an admirable commitment to growing its global mandate and maintaining quality rather than pushing quantity.

In an industry where fund sizes are small and critical mass is difficult to achieve, all three FTS funds surpassed the US$50 million mark within two years of inception and are all currently ranked in the top five largest Shariah cross-border funds in their


Yeoh


Percy

category: with total gross year-to-date sales exceeding US$100 million.

Its global strategic Shariah hub was launched in Malaysia in 2010 and the group has grown to account for around 14% of the total institutional market share in the country, making it a force to be reckoned with. The firm has a longstanding focus on Asia with a global center for emerging markets based in Singapore and numerous offices throughout the region: and based on its track record of Shariah commitment we feel sure that with the ongoing opening up of the industry (including new ASEAN and Asia Pacific passporting agreements) we will continue to see exciting developments. Sandeep Singh, country head and CEO of Franklin Templeton GSC Asset Management and head of Islamic business, commented that: "We are absolutely delighted and honored to be recognized for our Islamic asset management capabilities. On behalf of Franklin Templeton Investments, I would like to thank our investors for reposing faith in us and for their continued support. We look forward to growing our presence in this segment and delivering value to our investors."

Honorable mention for Best Overall Islamic Asset Management Company also goes to CIMB-Principal Islamic Asset Management for its international reach and strong growth (with 12.1% growth over the past year) and commendable commitment to encouraging emerging market development (including the recent MoU signed with Rhea Asset Management of Turkey).

Honorable mention for **Best Islamic Asset Management Company in Asia** goes to AmInvest for its size and coverage (with 53 Shariah compliant funds including 10 new launches) and exceptional AUM improvement (30% for Islamic AUM compared to 7% for conventional).

Regional winners

In an interesting turn of events, Qatar-based Al Rayan Investments took the award for Best Islamic Asset Management Company in the Middle East. The first Shariah compliant institution to be authorized by the Qatar Financial Center Regulatory Authority, the subsidiary of Masraf Al Rayan is a pioneer of the Qatari market and has achieved impressive growth since inception, securing over US$3 billion-worth of advisory and asset management mandates since 2008. Although the fund family is currently small compared to some of its contemporaries, the fully Shariah compliant firm has demonstrated commitment and consistency across its markets and mandates: with AUM of US$884 million as of September 2014 and year-on-year AUM growth of 100%. Building a notable niche among institutional investors and an innovative pioneer currently developing new products including the first Shariah compliant Qatari ETF, its existing products are also impressive: with the Al Rayan GCC Fund seeing returns of 34.7% in the past 12 months.


Selwood

Best Islamic Asset Management Company in Africa this year went once again to South Africa's Oasis Crescent Management Company, for its undeniable dominance in a market that has struggled to see regional players develop. With Shariah compliant AUM of US$1.6 billion out of a total US$3.6 billion and annual AUM growth of 12%, the group manages 20 Shariah compliant funds and has seen several new launches this year including the Oasis Crescent Hajj Policy and Umrah Policy, the first products of their kind in Africa, demonstrating a sensitive response to the needs and demands of its specific client market in the region. Adam Ebrahim, CEO and CIO of Oasis Crescent, commented that: "We are extremely honored that Oasis has retained its position as the best Islamic asset management company in Africa. The past 17 years have borne testimony to our focus on protecting and growing the real wealth of our clients over the long-term. Our unwavering commitment towards customer satisfaction and performance excellence continues to be the cornerstone of our business." Honorable mention also goes to Nigeria's Lotus Capital for its landmark steps to develop the asset management industry in sub-Saharan African: including the launch of the first Shariah compliant mutual fund, sub-sovereign Sukuk fund and ETF in Nigeria.


Adam

Europe has been one of the spotlights for growth in the industry over the past year, with new developments including the recent sovereign issuances from the UK and Luxembourg bringing renewed investor focus to the region. While there are limited numbers of domestic banks and asset managers playing a material role in the sector so far, one player stands out as a pioneer in the European Islamic asset management industry. IFN's advisory board this year unanimously awarded **Best Islamic Asset Management Company in Europe** to the UK's BLME for its efforts in developing the UK market: not least through offering European investors access to an extensive range of Islamic funds — including traditional options such as the BLME Global Sukuk Fund and US$ Income Fund, but newer and more innovative options leveraging UK market strengths, such as its Light Industrial Building Fund. Humphrey Percy, CEO of BLME, noted that: "BLME is delighted to have been the inaugural winner of this prestigious IFN award. The award recognizes BLME's asset management capabilities, in particular in fixed income and real estate management, and it is a tribute to the dedication and expertise of our investment teams. As the business expands, we are looking forward to delivering some new and exciting investment products during 2015."

Across the pond, and one of the most familiar faces in the industry once again wins **Best Islamic Asset Management Company in the Americas**. Although the US in particular has seen a number of interesting and exciting new participants enter the sector in the past year, Saturna Capital stands out for the continued performance of its respected Amana fund family. Providing a stable refuge for investors during the past periods of high volatility, the Amana Income Fund in particular has demonstrated its commitment to investor protection, providing returns of 16.83% over the past year. "At Saturna, we follow a principled and disciplined investment management process," said Jane Carten, the president of Saturna Capital, to IFN. "We are honored to have been chosen to receive this esteemed award, recognizing our commitment to putting shareowner interests first. We continue to launch new products to meet investors' demands." With total Shariah compliant AUM of US$3.8 billion, the firm continues to be one of the stalwarts of the US scene and can


Maznah

be relied upon to promote the values and advantages of Shariah compliant investing to an increasingly receptive audience. "Saturna benefits from deep expertise in analyzing investments, and the long-term results achieved by remaining steadfast in our strategies," added Carten. "We believe the criteria outlined by our faith-based products increase our ability to thrive because they inherently make us better risk managers."

Customer service champions

The second-biggest Islamic fund manager in the world, Public Mutual (a wholly-owned subsidiary of Public Bank) is Malaysia's largest private unit trust company and its biggest Islamic unit trust fund firm with a market share of 52.1% and total NAV of US$8.5 billion as of September 2014. Selected by the advisory board as the firm offering **Best Investor Relations**, the group is distinguished by its exceptional array of 35 Shariah-based funds along with three Shariah-based PRS funds, offering a wide range of equity, balanced, mixed asset, bond and money market funds to its investors. Surveys show that the firm is a "top-of-the-mind" brand among unit trust investors, and its strong retail focus has made it a major player in driving awareness and acceptance of Islamic investment within the wider market.

In terms of strategy however, Malaysia's AmInvest (a subsidiary of AmBank Group) took the top award for **Best Investment Strategist** this year. One of the biggest regional managers with RM6.45 billion (US$1.92 billion) in Islamic AUM, the fund has launched 10 new funds in the past 12 months including a range of cash, equity, dynamic Sukuk, balanced and fixed income mandates. With Shariah compliant AUM growing at 30% over the past 12 months compared to 7% for its conventional funds, the group has seen an exceptional performance of 45% CAGR for Islamic AUM over the past five years. Founder of Malaysia's first Shariah compliant fund in 1993, AmInvest has maintained its pioneering approach with a range of new strategies coming up: including a planned expansion into the UAE and wider Middle East, along with setting up a Dublin-based UCITS platform for European distribution, working towards white labeling funds for GCC distribution and focusing on a new focused strategy. Maznah Mahbob, CEO of AmInvest, told IFN that: "We are honored and very delighted to be recognized as the Best Investment Strategist. This award truly validates the effort our company is taking to the international level which is to bring UCITS compliant funds with high value and low volatility investment strategies to the Middle East and beyond."

Innovation and originality

Moving from the pioneering founders of the industry to the brash new players making waves at the forefront, the award for **Most Innovative Islamic Asset Management Company** goes this year to exciting new entrant Arabesque Asset Management, for its outstanding work in uniting the twin themes of Shariah compliant and socially responsible investing using a firm quantitative basis and demonstrating that ethical investing does not have to cost clients returns. One of the newest funds on the market, the Arabesque Prime is a passive equity fund launched in August 2014 that tracks the performance of the Arabesque Prime League, a globally diversified index of around 1,100 blue chip equities selected from over 70,000 stocks through a rigorous and systematic proprietary selection procedure. Dr Dominic Selwood, partner and general counsel for Arabesque Asset Management, commented that: "It is an enormous privilege to win the 2014 award. We are delighted the judges share our belief that sustainability is a core strategy shaping the future of asset management, and we are honored to be recognized for applying quantitative technology to make it global." With assets of US$1 billion expected by December 2015 the fund is one of the fastest-growing on the market, as investors are drawn by its combination of responsible practice and reward focus, and we look forward to seeing its performance over the next 12 months.

Institutional influence

The award for Best Institutional Solutions Provider was a close call this year, but the Malaysian giant Employees Provident Fund Board (EPF) edged out due not only to its size and scope, but its efforts towards making Shariah compliant investment available to a wider audience. EPF is an ethical fund with total AUM of RM569.69 billion (US$169.57 billion) as of June 2014, an increase of 5.77% in the six months since December 2013. Of this, 38.97% (RM222.01 billion or US$66.07 billion) is Shariah compliant (92% internally managed and 8% externally managed). In comparison, the total Shariah AUM of fund management companies in Malaysia is less than half this at RM105.2 billion (US$31.3 billion). EPF has long been a supporter of the Islamic finance industry as a whole: and has issued three Shariah mandates to external fund managers with total AUM of RM17.74 billion (US$5.27 billion) as of June 2014: including a global Sukuk, domestic Sukuk and global Shariah equity mandate. In August 2014 EPF successfully converted RM20 billion (US$5.95 billion) of its conventional loans to Shariah compliant financing, in line with its agenda to increase its Shariah compliant assets, and is currently looking into the potential offering of fully Shariah compliant fund options to its members.

Special mention for institutional solutions however must also go to index provider IdealRatings, which has been very busy over the past 12 months with new Sukukscreening methodologies, a new suite of Sukuk indices, a new REITs screening solution and a partnership with Russell Indexes for a ne co-branded global Islamic index family.

On the distribution side, CIMB-Principal Islamic takes home the prize for **Best Fund Distributor** based on its extensive reach and activities with multi-national advisors from Malaysia, Saudi Arabia, Bahrain, Canada and Indonesia (among others) along with European access through its Dublin-based platform. The firm is also to be praised for its work in encouraging the development of the industry in emerging markets: such as through its recent MoU with Rhea Asset Management to develop the Turkish market. "At CIMB-Principal, we firmly believe that client servicing is the foundation of a long-term relationship," said CEO Ramli Kamsari. "To reinforce the importance of cross-border offerings, CIMB-Principal Islamic products are available internationally and distributed away from where the company is located." UCITS funds remain an important long-term strategy for CIMB-Principal Islamic to expand beyond its familiar markets, and its three UCITS funds are currently registered in Ireland, the UK, Switzerland and Singapore; while cross-border mandates and products are managed out of offices in Kuala Lumpur, Singapore and the US.

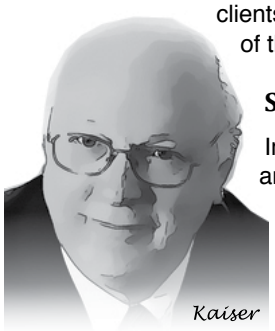
Getting down to business

From international reach focusing down to individual performance, this year the IFN Islamic Investor Awards for the first time also looked at regional, sector and thematic performance to identify the firms forging forwards in their individual specialties.

Best Regional Fund Performance was awarded to Pakistan's Al Meezan Investment Management, which currently has total Islamic AUM of US$520 million and annual growth of 14.09%. The firm has been a pioneer in the Pakistani space with 11 funds including two new launched this year: the Meezan Capital Preservation Fund II and III. The performance of the firm and its funds in a market strained by political pressure and other challenges is admirable and demonstrates the resilience and dedication of investors in the sector. Honorable mentions in this category also go to Malaysia's PMB Investments for the 114% AUM growth (to US$142 million) seen across its eight Malaysia-focused Islamic funds; and to RHB Islamic for the pioneering launch of Hong Kong's first Shariah compliant, actively managed Islamic balanced fund, the RHB-OSK Islamic Regional Balanced Fund, in April 2014 — with its mandate allowing the purchase of Hong Kong's maiden sovereign Sukuk significantly raising awareness of the issuance among investors.

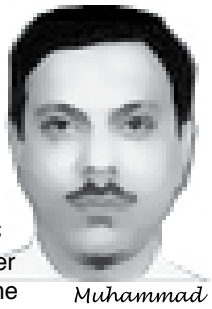
Best Thematic Fund Performance goes to new entrant Asiya Investments, an Emerging Asia specialist based in the GCC and providing a gateway for capital flows to and from growing markets in Asia. With Shariah compliant AUM of US$35 million only a small proportion of its US$1.07 billion total, the firm has nevertheless seen growth of 138% in the past year. Its Asia Islamic Trade Finance Fund, concluded the IFN board, is commendable in demonstrating the opportunities available for those brave enough to leverage new trends.

The fund provides investors with access to uncorrelated income returns from financing short-term, self-liquidating and fully Shariah compliant trade deals, as well as providing its SME businesses with a dedicated funding source to support their activities. The fund has grown in size by 50% over the last 12-months with net annualized returns of 3.67% and no negative months; with its 3.42 Sharpe ratio placing it as the highest-ranked US dollar-denominated fund on Eurekahedge's trailing 12 month ranking. The highly differentiated nature of the fund, despite its small size, along with its support of the Shariah compliant fundamentals of real economy investment and SME support, make it one of the most exciting innovations in the industry. Brian Luck, director of investment advisory, commented that: "We are delighted to have received this prestigious award. As a firm we challenge ourselves to look for innovative Islamic solutions to deliver value to our clients and we appreciate IFN's recognition of these efforts."



Sector focus

In the final fund award of the series, another new player becomes champion as Azimut Global (formerly AZ Global), the Turkish asset management platform of independent global asset management firm Azimut Group, wins **Best Sector Fund Performance** for its AZ Multi-Asset Global Sukuk Fund. Since its launch in November 2013 the fund has raised more than US$100 million (primarily from European and Turkish investors), making it the world's largest UCITS-compliant cross-border Sukuk fund and playing a vital role in raising awareness of the asset class outside of the traditional OIC economies. CEO and Turkey country manager Giorgio Medda commented to IFN that: "The success of Azimut clearly proves that Sukuk have now become a universal asset class with the benefits of enhanced liquidity and diversification potential now adding to its underlying attractive profit opportunities. As we approach the first anniversary of the fund, we are planning to expand its distribution to MENA and ASEAN regions with the aim of becoming a product of choice for Islamic asset management's portfolio solutions upon its absolute profit driven strategy invested in almost 50 listed Sukuk, with a focus on investment grade issuers and medium-term maturities that also leverages the strengths of our Luxembourg funds infrastructure." With offices in 12 countries and total AUM of over US$37 billion, Azimut is testament to the growing number of conventional players in further afield markets that are not only tapping the Islamic asset management sector, but developing it beyond its current boundaries.



To conclude the IFN Islamic Investor Award series for 2014, IFN is finally delighted to announce that Luxembourg has been selected as Best Funds Domicile for 2014, reflecting its exceptional commitment to the Islamic finance space and its growing influence in the sector. The leading investment fund center in Europe and second-biggest in the world after the US, the country has a highly tuned legal and regulatory framework that combines rigorous investor protection with an unequalled degree of flexibility in fund design, a flexibility that allows products to be tailored to the needs of Islamic clients, while its 79 international tax agreements make it a compelling location and have pushed it into the top five Islamic fund domiciles worldwide. As its finance minister this month continues his tour of the Middle East to discuss possible passporting opportunities and further investment fund relationship developments, with further sovereign Sukuk issuances expected next year and with the first continental European Islamic bank set to launch in Luxembourg in the next few months, we expect that the country will continue to play a leading role in the European Islamic investment industry.

Congratulations to all our winners

We hope you will agree that the comprehensive and wide-ranging list of winners represents all angles and aspects of an asset management industry that is developing at one of the fastest rates in the world. We are proud and pleased to be able to recognize and reward the innovation, dedication and enthusiasm of its participants, and we extend our admiration and appreciation not only to our winners and nominees, but to all the firms across the industry who are persevering so tirelessly to push the Islamic asset management industry forward.

Congratulations to all, for an exceptional year that demonstrates the social, financial and economic strength of Shariah compliant investment.

Home of the brave: Where next for Islamic finance in the US?

With the surprise return of Goldman Sachs to the Islamic debt capital market last week, a groundswell of new funds entering the asset management arena and increasing activity in the US property market, it looks as if Islamic finance could be back on the map for the world's biggest economy. But will the US remain a featherweight or finally step up to fight in its own division? LAUREN MCAUGHTRY looks at the latest activity.

Late to the table

While several major US banks have operations in the Middle East and have taken part in some Shariah compliant deals, they have on the whole been seen as less active than their European counterparts such as HSBC and Standard Chartered while even smaller European players such as Societe Generale and BNP Paribas have made moves in the Islamic space. In addition, the game of musical chairs with Islamic finance hires at the big banks has given the sector an air of uncertainty that has pervaded through the financial crisis; while ongoing pressure in the financial markets at home and the geopolitical tensions in the Middle East have restrained the return of growth and investment flows.

Bank activity

However, several of the Wall Street banks have been quietly building a presence in the industry for some years; particularly within the Middle East, and have developed significant Shariah compliant capabilities. Some of the biggest US lenders are active in the Shariah compliant corporate finance space, and their influence is growing. Morgan Stanley has built an impressive record of deal-arranging across the Gulf and Asia: in June 2012 the bank was the issuer for Barwa Bank's three-year Turkey Indonesia Equity Capital Protected Notes, while in October it became the sole lead manager and bookrunner for Singapore-based Sabana REIT's SG$80 million (US$64.6 million) convertible Sukuk, which won the 2012 IFN Equity Deal of the Year. In November the bank also arranged the groundbreaking Abu Dhabi Islamic Bank (ADIB) hybrid Sukuk, which won the 2012 IFN UAE Deal of the Year. The bank has also entered the fund space, guaranteeing ventures such as the Takaful Emarat Capital Protected Fund.

Bank of America Merrill Lynch is another US player with a history in the sector: acting as advisor for milestone deals including the US$98.66 million Noble Group Sukuk, issued in Malaysia in October 2012. In 2012 the bank embarked on a program to expand lending in the Middle East as oil-rich Gulf investors showed increasing appetite for acquisitions, and has made several senior hires in the region.

Citigroup is an equally long-term participant: and has been active as an arranger in the Sukuk sector since 2006, participating in deals such as the 2009 US$500 million GE Capital Sukuk, the biggest Islamic bond ever from a US company; the 2010 Malaysia

Airport Holdings RM1.5 billion (US$487 million) Sukuk; and the 2013 US$1.5 billion Sime Darby global Sukuk program, which won the 2012 Corporate Finance IFN Deal of the Year. It also acted as arranger for the inaugural Senegal sovereign Sukuk this month; as well as bookrunner (along with Deutsche Bank, Dubai Islamic Bank and Standard Chartered) for the upcoming Pakistan sovereign Sukuk.

JPMorgan, one of the biggest lenders in the US, has in recent years made a clear move to boost its share of the Islamic finance industry with the appointment of Hussein Hassan as its global head of Islamic finance, based in Dubai. Hussein was previously the global head of Islamic structuring at Deutsche Bank. In 2012 JPMorgan helped to arrange US$119 million of global Sukuk sales, or around 0.3% of the total. The bank won the 2013 Cross-Border Deal of the Year for the US$120.5 million Bank of Azerbaijan issuance last July; and the Real Estate Deal of the Year for the CityCentreDC US$390 million transaction in May.

US banks are also muscling in on the IPO space. Last year Deutsche Bank and Goldman Sachs were the two arrangers for the Al Noor Hospitals Group IPO in June, which won the 2013 IFN IPO Deal of the Year; while Morgan Stanley, JPMorgan Chase and Bank of America Merrill Lynch are the three joint global coordinators of the upcoming landmark Emaar Malls IPO, which according to IFN sources could reach up to US$1.5 billion.

Renewed interest

With Goldman Sachs rejoining the market with its debut issuance, which priced at a tight 2.87% (21bps over the conventional counterpart) what does this mean for the future of international banks in the Islamic finance industry? In actual fact, believe market players, not much may change. The move does not signal a renewed interest from investors in US banks, nor a growing appetite for Islamic debt from US investors. Instead, the transaction looks to be a posturing exercise in order to establish Goldman Sachs' position in the market, and improve its position in the arranger league tables. Currently US banks stand way down the rankings: with JPMorgan the highest ranking at #10 with US$1.34 billion in three deals over the last 12 months, according to the latest data from Dealogic — compared to US$7.54 billion in 30 deals from league leader HSBC. Citigroup comes in at #13 with US$816 million in eight deals; while the only other US bank in the top 30, Goldman Sachs, trails behind at #24 with just US$259 million in three deals.

However, despite the strong appetite for the initial Goldman Sachs issuance, the market is unlikely to see other US banks following its example until the sector has proven its staying power. "It's highly likely that Goldman will be the sole player in the Islamic finance market in any meaningful way for the near term," said George Thomas Conboy, the chairman of US-based Brighton Securities Corporation, a financial services company, in a recent Bloomberg interview. "There aren't as many players willing to take risks in that area until Goldman blazes a trail and it's clear that Islamic finance can be properly structured and profitable."

"Despite the strong appetite for the initial Goldman Sachs issuance, the market is unlikely to see other US banks following its example until the sector has proven its staying power"

A new frontier

Yet as the industry grows new opportunities are emerging and some institutions are already casting their nets to catch them. The recent explosion of demand for Sukuk due to its favorable yields and perceived security has led to an imbalance between supply and demand. Although US banks may not yet be taking advantage of this, Islamic investors are beginning to look further afield for their investments. "There is a growing pool of Islamic capital chasing an attractive risk reward set of US assets," said one New York-based banker to IFN. "Islamic investors will seek out such assets as a safe haven and to diversify from Middle Eastern markets. This also means that US corporates could tap into these markets by issuing US asset-backed Sukuk."

Property push

For now, however, it is as always the property market that is deriving the most benefit: with increasing fund volumes flowing out of the Middle East towards the US. Although private equity activity remains muted, direct investment volumes are expanding rapidly, with some funds and firms also getting in on the act.

"Most of the activity we see coming out of the Gulf into the US is direct real estate investment," confirmed Isam Salah, a partner with King & Spalding in New York, to IFN. "We are doing 95% real estate; and we have seen a significant increase in investment." In addition, investors are becoming more aggressive as returns decrease; looking outside of the primary markets on the East and West coasts and towards secondary markets in other parts of the country. They are looking for value-add opportunities, as a means of increasing their return," explained Isam, "and we expect to see a renewed interest in development deals in the near term". "We are seeing a lot of interest in the residential, industrial, multi-use and senior living sectors. We also see a strong interest in limited service hotels because they don't present the issues associated with full services hotels that have bars and restaurants."

Bahrain-based alternative investment firm Investcorp, for example, recently acquired a portfolio of office and industrial property assets in the US, for around US$250 million. The purchases, which cover nearly 2.2 million square feet and have an average occupancy rate of 87%, were made in separate transactions by the company's US-based real estate arm, for property in Durham in North Carolina, Seattle in Washington, and Jacksonville in Florida. Gulf investment groups that were active investors in US real estate prior to the financial crisis have returned," commented Isam, "and we have seen a number of new investment firms and family offices coming to the US to seek out direct real estate investment opportunities. Executing a direct real estate investment in the US takes a certain amount of sophistication, and as Gulf-based Islamic institutions have grown in capacity and experience, we are finding them more willing to undertake investment activities in the US market."

A quiet revolution

While direct investment rules and pre-crisis private equity activity has yet to return, a new generation of asset management firms has for the past few years also been quietly developing their own cottage industry of Shariah compliant investment funds and private placements – and not just in New York, but across the country from Chicago to Los Angeles, Seattle to Silicon Valley; representing a new breed of investor keen to tap OIC liquidity and building on the growing interest in ethical investment. As investors in the Middle East become increasingly active, demand is rising for diversified investments and asset classes. "There are some sectors that are specifically likely to attract Islamic finance funding in the US: including energy (renewables included), infrastructure, technology and telecoms," said a Dubai-based lawyer. "We will see Islamic investors specifically flowing into the US in these sectors."

While we have seen a multitude of new funds and asset managers arrive on the market to join established players such as Azzad Asset Management and Saturna Capital, it must also be noted that not all of the current activity is on the radar. Ultra high net worth investors have been using these banks for years to structure private deals for them. "Quite frankly, a number of these deals have not been announced," said the lawyer. But there is a considerable volume of private placements that you just don't hear about."

While the evolution might be slow and silent, there is no doubt that interest in Islamic finance is slowly growing on US soil, as the economic appeal of the Islamic markets becomes impossible to ignore. It will be interesting to see how US players — both financial and corporate — approach this going forward.

Africa: A destination for long-term growth investments

The African region has benefited from increased investment flows on the conventional side which as a result have simultaneously boosted demand and created a surge in appetite for Shariah compliant investment products across the continent. With several dedicated Shariah compliant investment houses, Africa is expected to bear strong growth prospects over the long-term. NABILAH ANNUAR takes a look at the continent's investment landscape and potential opportunities.

Gradually being recognized by global investors as an exciting destination, Africa has been suggested to show positive developments similar to the rise of the Asian tiger economies in the 1970s and 1980s. Nadir Thokan, an investment analyst at 27four, a South African (SA) investment firm, revealed that excluding SA, Africa is increasingly being recognized by global investors as an exciting, long-term growth investment destination. "Over the last decade, most key African countries have enjoyed economic growth in excess of 6% per annum – more than twice the average growth rate of South Africa – and over the next five years, nine out of the top 20 fastest growing economies in the world are expected to be in Africa," he said.

Shariah compliant assets available in the African investment space include: (1) Equities which are subjected to the regular Shariah compliant financial screens as set out by AAOIFI; (2) Sukuk — following issuances from Senegal and South Africa, Nigeria and Kenya are also expected to launch their Sukuk in the near future; (3) Commodity exchange traded funds (ETFs), in particular precious metal commodity ETFs listed on the Johannesburg Stock Exchange; (4) Murabahah contracts; (5) Selected private equity. According to Nadir, the most easily accessible asset class remains Shariah compliant equities as these have the largest universe eligible for selection and are also the most liquid asset class.

However, unfortunately Africa's capital markets are predominantly underdeveloped and small compared to South Africa. "Stock market penetration ratios (as a percentage of GDP) range from 15% to 60%, whereas in South Africa, this ratio is in excess of 150%. This, together with low listed equity market liquidity ratios, limits the ability to employ large amounts of capital quickly and effectively within Africa's listed equity markets. As a result, large investments are mostly private equity in nature, focusing on infrastructure and green/brownfield projects," explained Nadir. Africa's stock exchanges nevertheless remain an attractive proposition for smaller institutional investors.

Conveying a critical outlook, Nadir suggested two global factors that could challenge Africa's economic and investment landscape over the next year. The slowdown China is experiencing will likely spill over into slower growth in Africa. This is due to significant trade ties between sub-Sahara Africa's (SSA) and China. Exports to China are now equivalent to almost 7% of SSA's GDP, a much

larger ratio than in any other emerging region including Emerging Asia. This leaves SSA more vulnerable to China's economy with commodity exporters, such as South Africa, Angola and Zambia projected to be hit hardest. The second factor would be the appreciation of the US dollar and the potential for an increase of interest rates in the US, which is expected to affect all emerging markets and frontier markets such as Africa. "Country capital accounts will experience pressure, which will ultimately manifest in higher interest rates due to a pick-up in supply side inflation. This will, in all likelihood negatively impact financial asset prices," said Nadir.

The major driving factor of the African economy is the demographics of young and growing urbanised workforce that is more literate and healthier than previous generations as well as a broad economic reform which is the result of improving institutional and political governance. The demand for Islamic investment products will naturally follow given the large Muslim population, particularly in North and West Africa. However, educating potential investors on the merits of including an Africa allocation within their investment strategy, as well as depth in the Shariah compliant investment options both in terms of scope and liquidity, is imperative to develop traction for Islamic investments in the continent.

Asia: A continent of substantial development and vast opportunities

The Asian Islamic capital market has witnessed substantial growth over the past year; gaining considerable interest from the financial markets and becoming an increasingly integral component of the Islamic finance industry. NABILAH ANNUAR runs through the most significant recent developments in the Asian Islamic capital markets.

When it comes to Islamic finance, Malaysia has undeniably positioned itself at the center of this burgeoning industry as an Islamic finance hub, on both a regional and a global scale. Welcoming 2014, five Malaysian Islamic banks tapped the Sukuk market in the first half of the year to adjust to the new Basel III requirements. Maybank Islamic, AmIslamic Bank, RHB Islamic Bank, Public Islamic Bank and Hong Leong Islamic Bank launched medium-term note Sukuk programs this year, and issued subordinated Sukuk instruments with loss-absorption features that qualify as Tier 2 capital.

For the first half of 2014, Malaysia issued RM3.25 billion (US$ billion) in Sukuk, setting a record for the largest number of Sukuk issued in any year so far. According to a report by Moody's, four factors were driving the Malaysian Sukuk market this year. They are: (1) fund-raising for the execution of the government's economic transformation program; (2) Islamic banks' capital and refinancing needs; (3) ASEAN palm oil producers' funding needs; (4) issuers looking to refinance maturing Sukuk. The ratings agency expects overall Sukuk issuance to grow by 10% annually in 2014 and 2015. The Malaysian government has set a target for Islamic banking assets to reach 40% of the total industry by 2020.

Apart from Malaysia, one of the main highlights of the Asian Islamic capital market was the debut of Hong Kong's sovereign Sukuk. Aspiring to become a regional hub for Islamic finance, the government issued a US$1 billion five-year facility which was priced at 23bps over five-year US Treasuries at 2.01% attracting orders exceeding US$4.7 billion from a wide range of conventional and Shariah-seeking investors. The program gained a diverse geographic distribution with nearly half (47%) of the 120 international investors coming from Asia, along with 36% from the Middle East, 11% from the US and 6% from Europe. Banks formed the largest purchasers of the debt (56%), followed by sovereign wealth funds, central banks and supranationals (30%), fund managers (11%) and insurance companies (3%). Hong Kong's financial regulator seeks to work closely with Malaysian authorities to develop its Islamic financial market and promote Shariah compliant products to both local and international investors

Another avid participant in the Asian Sukuk market, the Indonesian government raised US$1.5 billion in Sukuk last September, a deal which was claimed to be the largest order book ever achieved for a sovereign Sukuk from Southeast Asia according to the Indonesian finance ministry. The transaction witnessed a demand reaching almost seven times its offer with

bids amounting to US$10.2 billion and is the largest single-tranche Sukuk issuance in 2014. Due to mature on the 10th September 2024, it carries a return of 4.35% and is part of the government's Trust Certificate Issuance Program set up on the 5th November 2012.

Commenting on the development of the Islamic capital market in Asia, Ary Zulfikar, managing partner at AZP Legal Consultants, said: "In terms of Islamic finance transactions, Malaysia is still leading on many fronts of Islamic finance. Other key markets are Pakistan, Indonesia, Bangladesh and Brunei. Based on data issued by the IFSB, there is a rapid development in Islamic wealth management and Sukuk markets. Malaysia is the most developed market for Sukuk at both the primary and secondary market levels."

Pushing the industry in Pakistan, the central bank recently launched a marketing campaign for the Pakistani Islamic

banking sector, providing a roadmap for the future development of the industry, with an emphasis on improving the perception and awareness of the sector, the products available and standardization and harmonization across the industry. The current shortage of sovereign Sahriah compliant debt instruments has been highlighted as one of the industry's most pressing problems by industry participants, along with a lack of public awareness regarding the sector and the quality of regulatory support — all issues that the Pakistan regulators are taking steps to address, providing a positive outlook for the country's Islamic banking sector.

> **"The Islamic capital market is still young and developing; thereby the industry's growth is expected to be sustained"**

With a substantially prominent presence in the Islamic finance landscape, the government of Turkey has yet to make final plans for Sukuk issuances; however a treasury official has reportedly stated that the government intends to release Sukuk on an annual basis. The number of entities issuing Sukuk to finance infrastructure projects is currently on the rise. Dogus Group, one of the biggest Turkish corporations operating in the banking and construction sectors intends to finance its recent projects in a Shariah compliant manner having received approval from the Capital Markets Board of Turkey for their issuance of US$370 million-worth of Sukuk in what would be the first dollar-denominated corporate transaction of its kind in the country. Agaoglu Group is another corporation planning to issue Islamic debt for their construction projects. The group's multibillion dollar construction portfolio includes the Istanbul International Financial Center which requires approximately US$1 billion.

Possibly reaching its maturity, Islamic financial markets now offer nearly all the products and services conventional markets offer such as money market and capital market instruments. Sukuk structures broadly incorporate contracts including: Murabahah (sale and buy back), Ijarah (sale and lease back, lease and lease and back, forward lease, etc), Salam (advanced payment), Istisna (sale of specified manufactured goods for delivery upon completion), Musharakah (partnership where profits are shared according to agreed ratios and losses are shared according to contributed capital), Mudharabah (profit sharing where a Rab Al-Mal or investor contributes capital and a Mudharib or manager contributes his time and efforts) and Wakalah (agency). Thus far, majority Sukuk issued in global market utilize the principle of Ijarah.

The challenges faced by issuers and investors in the Asian Islamic capital market can be segregated into three: (1) proper governance and Shariah decisions; (2) pricing issues; and (3) harmonization of standards and practices. Commenting on the first element, Zulfikar said: "Shariah experts are key to ensuring proper governance and the process of obtaining Shariah approval should be transparent and disclosed. This will lead investors or any related party understands the reasoning of the issuance of such approval which in turn would have a wider acceptance of Shariah decisions, particularly if they have implications on cross-border transactions." He further suggested relevant authorities to issue a standard guide in regards to Shariah decisions to serve as a reference material to facilitate the development of the market.

For Sukuk to be efficiently priced and credible, it has been suggested that further initiatives need to be undertaken to develop its own indicator. For instance, if a Sukuk Ijarah is issued and uses a certain property as its underlying asset, the actual rate of rental may be explored to determine the rate of return on that instrument. This would then fluctuate depending on the demand and supply for that property, which will in turn give a true reflection of the price of the underlying asset. In terms of harmonization of standards and practices, appropriate standards and guidelines to strengthen the framework in the Islamic money market, liquidity management should be in place. Additionally, the identification of key measures in the development of benchmark Islamic securities could assist to determine a particular benchmark rate for the Islamic financial system.

Speaking to IFN, Anthony Chan, CEO of Hong Kong-based New Line Capital Investment, highlighted: "Most countries, in particular non-Muslim ones, face challenges in developing a local market for Islamic finance. Due to the nature of Islamic financial products, its development requires legislative and regulatory changes that go to fit modern capitalist economies." Generally, Islamic financial products require multiple transactions to achieve equivalent function with conventional products and are therefore subject to additional tax burdens under most existing legal and taxation systems. In order to introduce these products into domestic market, changes of legal and taxation systems are pre-required. Additionally, political opposition to the adoption of Islamic elements into the economy could be another deterrent in non-Muslim countries. For example in Korea, heated political debates have occurred about the introducing Shariah into the financial markets. Even though the government expects economic and financial gains from such development, they failed to pass Islamic finance related legislation because of such resistance. Moreover, the uncertainty over the potential future economic benefits of developing Islamic financial markets poses another hurdle for non-Muslim countries for the introduction of Islamic financial products.

Conveying his outlook on the Asia's Islamic capital market in the coming years, Zulfikar said: "The Islamic capital market is still young and developing; thereby the industry's growth is expected to be sustained. Investor interest can be coming from outside Asia, such as Europe and Americas (US and Canada). Interestingly, non-Muslim countries such as the UK, Japan, and China have recognized this shift and are preparing Sharia compliant debt issues to target the liquidity-rich Middle East."

Sharing similar sentiments of a positive outlook on the Asian market, Chan also expects the Islamic finance industry in Asia to continually grow driven by both demand and supply factors as well as healthy support by government agencies and financial regulators. "A combination of strong political support, large investor base and generous tax regulations that make Islamic finance comparatively attractive for investors have propelled the Southeast Asian nation into the world's most developed market for Shariah-friendly investments, commanding more than 60% of global Sukuk issuance." Highlighting the tripartite bank merger in Malaysia, Chan noted that the combined entity at an estimated asset base of US$188 billion would be the fourth largest bank in the Association of South East Asian Nations which could pave the way for the internationalization of Malaysia's Islamic banking model..

ELIAN RAISES THE BAR IN INTERNATIONAL FINANCE SERVICES

Following a management buyout from the Ogier Group in June, Ogier Fiduciary Services became Elian. Director Peter Gatehouse, explains how its global International Finance service line is delivering administration services to trusts, partnerships, special purpose vehicles and other corporate entities established for capital markets transactions.

Always striving to achieve the highest standards, Elian has a clear, uncompromising vision: to continually deliver more value by raising the bar and setting the standard in terms of client service in the company, fund and trust administration industry.

Our client service standards are consistently at the top end of our industry but we are determined to do even better and firmly believe that we will with the additional investment now available to us. We want to set the standard that others follow. The launch of Elian, which was formally known as Ogier Fiduciary Services, builds on our solid past foundations and harnesses the excitement and enthusiasm everyone shares in our relentless drive to provide the highest levels of client service in our industry.

We have vast experience of the administration of capital markets transactions, which are originated from diverse financial centres and time zones. We work with our clients' appointed tax and legal advisors to ensure that complex structures are administered in accordance with documentary requirements. Our recent experience includes the administration across our jurisdictions of structures such as CLOs, ABCP conduits, aircraft finance, MTN programmes and hybrid corporate structures. Our role routinely includes the provision of directorship and accounting services and we have a very impressive book of clients and transactions, many of which are industry recognised and referenced.

With a keen focus on the Islamic finance market, our International Finance service line provides administration services to structured finance transactions using Sharia'h compliant instruments. We have undertaken transactions that include the issuance of Sukuk trust certificates backed by Murabaha, Wakala, Istisna'a and Ijarah agreements and assets. We have also developed useful experience in helping clients structure deals in the GCC region, from our office in Bahrain, including liaison with regulatory and professional advisors.

Elian's international scope allows us to provide our services in our clients' jurisdiction of choice, whether onshore or offshore. We routinely consider the requirements of each transaction and offer flexible solutions to ease the administrative burden of our clients. Even if a transaction spans many jurisdictions we endeavour to offer our clients one point of contact in a convenient time zone. We can call on a network of agents to assist if services are required in a jurisdiction where we are not present and we will manage this relationship for our clients to ease the administrative burden.

Elian's International Finance team boasts an outstanding reputation established over a number of years of working with the highest quality clients. I have worked in the industry for more than 30 years and most of my 34 team members are professionally qualified. The team consists of chartered accountants, lawyers, chartered secretaries, ICSA and STEP qualified administrators and fully qualified bookkeepers. Each member of the team is knowledgeable about the industry and we stay abreast of changing legislation, ensuring clients receive proactive service.

Elian has a strong heritage in terms of excellent client service: based on our client service feedback programme, 97% of clients stated they are satisfied with the service levels they currently receive from Elian and 97% also stated they would recommend Elian to a colleague.

We have a comprehensive strategy in place for growing our business organically, consolidating our position in core markets. We also have a well-funded acquisition strategy that will further accelerate our growth and we are currently considering a number of significant opportunities. Our acquisition strategy will give us critical mass in important new markets where our clients may require our services.

Led by our chief executive officer Paul Willing and the existing management team, Elian employs 500 people across 10 offices; the group has delivered 15 years of back-to-back growth since its launch as Ogier Fiduciary Services in 1999.

Europe: A bright prospect for 2015

Gaining traction in the Islamic finance community, countries across Europe have demonstrated their commitment to developing their Shariah sector locally. With the leverage of a more developed economy Islamic finance stands to gain significant potential in these mature markets. NABILAH ANNUAR explores.

The year 2014 has been said to be a turning point for the global Islamic capital market. Sovereign Sukuk issuances by non-Muslim sovereigns dominated the debt capital markets, motivated by UK Treasury's inaugural deal in July. Europe saw two countries tapping the Sukuk space – UK and Luxembourg. Apart from these two states, France, Germany, Italy, Malta and Cyprus are also attempting to gain a foothold in Europe's Islamic finance market.

The most prominent deal in the Europe would be the landmark issuance of UK's Sukuk Ijarah. Having announced it during the annual WIEF event held in London late last year the UK government successfully auctioned its paper on the 2nd July 2014. With HSBC as structuring advisor for the debut Sukuk together with Barwa Bank, CIMB, National Bank of Abu Dhabi and Standard Chartered as the joint bookrunners, a series of roadshows were conducted in the in Kuala Lumpur, Doha, Abu Dhabi, Dubai and London to market the Sukuk issuance. The 'Aa1/AAA/AA+' rated sovereign successfully auctioned a GBP200 million (US$322.16 million) paper which was 12 times oversubscribed with an orderbook rumored to be over US$3 billion. Carries a tenor of five years at a profit rate of 2.03%, the Sukuk was issued by an SPV with its obligor being The Secretary of State for Communities and Local Government, and co-obligor being Her Majesty's Treasury.

UK's emergence in the Islamic primary debt capital market almost instantaneously spurred other sovereigns to follow suit such as Hong Kong, the emirate of Sharjah, South Africa, including Luxembourg. As the second sovereign to tap the global Sukuk market, the Grand Duchy first announced its intentions several years ago. Following the passing of the country's Sukuk bill earlier in July, the country successfully issued its first Islamic bond on the 30th September 2014. Arranged by Banque Internationale à Luxembourg, BNP Paribas, HSBC and QInvest UK, roadshows for the Sukuk were conducted in the UAE, Malaysia, Saudi Arabia and Qatar. Luxembourg launched its inaugural Sukuk at the tight end of initial price guidance of 0-2bps below midswaps and finally

priced 0.436%. The 'AAA'-rated (by Moody's and S&P) Reg S facility saw positive demand as the book-building process for the landmark EUR200 million (US$253.87 million) program reportedly amassed over EUR500 million (US$634.68 million) in orders and was twice oversubscribed. Carrying a tenor of five years, the Islamic debt was distributed across 29 accounts, with up to half of the program taken up by central banks (40%) and other official institutions, confirmed the finance ministry. The Sukuk is believed to cement Luxembourg's position as one of the premier Islamic finance centers in Europe. The euro-denominated issuance also proved popular among Middle Eastern investors as they formed the bulk of the purchasers at 61% while European investors took up 20% and Asian players 19%.

Other entities in the region have also voiced out similar intentions to tap the Islamic capital markets. Majority of the deals that are currently in the European pipeline originate from Turkey: (1) The Turkish Treasury who is looking to issue lira-denominated Sukuk; (2) The Turkish government which aims to release Sukuk on an annual basis; (3) Turkiye Finans Katilim Bankasi who looks to issue US$50 million before 2015; (4) Agaoglu Group which plans to raise up to US$300 million in Sukuk; and (5) Aktif Bank which intends to raise TRY200 million (US$89.53 million). Another anticipated Sukuk by the market is from French bank, Societe Generale, which announced in August that it seeks to raise US$140 million in Sukuk. Attempting to participate in the Shariah compliant space, industry players in the Republic of Cyprus including the president of Cyprus Investment Funds Association, Angelos Gregoriades, and Nondas Metaxas, CEO of the Cyprus Stock Exchange urged the nation to follow in the footsteps of the UK and Luxembourg in issuing Sukuk to attract investment from the Middle East. Supporting the European Sukuk market, the European Commission recently released a draft on liquidity coverage ratio under Basel III which dictates the treatment of non-sovereign Sukuk. Due to be published in the near future, the proposed legislation allows Islamic banks in Europe to use Sukuk exposures as lower tier liquidity buffers at par with other corporate bonds, but under a more flexible regime in terms of minimum issue size and maximum maturity time.

Speaking to IFN, Said Qaceme, senior manager of advisory and consulting at Deloitte Tax & Consulting conveyed a positive view on the major developments of the Islamic capital market in Europe, particularly in terms of investments. "2014 is really a turning point for the Islamic capital market in Europe and should pave the way for an even brighter year in 2015. Apart from the sovereign Sukuk by UK and Luxembourg, other European countries have similar plans in the pipeline and this shows the commitment and support of governments towards the Islamic capital markets. We also expect innovation in the field of investment funds and an increasing focus on the SRI side of Islamic Finance. Europe is increasingly developing the field of Impact Investment. The development of a Shariah compliant microfinance investment vehicle and social housing developments financed by Sukuk issuance would definitely reflect both innovation and the ethical nature of Islamic finance."

Among the challenges that have been highlighted in the development of Europe's Islamic capital market are the current and increasing regulatory requirements across the continent which has been indicated to impede the application of Shariah compliant instruments. Nonetheless the growing interest, the developing pool of talents and service providers in the field allow for complex solutions to this barrier. Attributed to the recent and largely advertised sovereign Sukuk issuances as well as the creation of Eurisbank, the perception of Islamic banking and finance among the European population is seen to be improving. However as in any industry, it will be the responsibility of the project promoters to demonstrate professionalism and reliability to increase the level of acceptance. Another area of focus should be the continuous education of the public and industry players in the European market. The rise in university degrees and professional qualifications in Islamic finance is a significant step in right direction towards a globalized industry.

Industry observers expect the Islamic finance industry to pick up pace particularly in non-traditional markets, this includes the European region. Commenting on this, Qaceme pointed out: "In Europe, Muslims are looking for Shariah compliant banking services to which they do not currently have access to. Ethical investors may be looking to use a bank offering 'alternative' and SRI investments. Investors that have had a bad experience with and who mistrust Western banks (e.g. CHF loan crisis) may be attracted by smaller banking entities that enjoy better reputation." Additionally, the rising trade volumes both within the European Union (EU) as well as between the EU and emerging markets (Middle East, South East Asia) give rise to significant corporate banking opportunities. This is an area in which Shariah complaint banks may extend their support and services to the Shariah compliant businesses and corporates which already have activities in Europe. The same can be provided to other investors and corporates from the Middle East. "I have the feeling that when the first fully Shariah compliant bank gets its license, other such players may follow rapidly and try to tap into this greenfield market. The investment funds sector will also benefit from this development. Wealth management may also be a growing area to cater the needs of GCC individuals," highlighted Qaceme.

"2014 is really a turning point for the Islamic capital market in Europe and should pave the way for an even brighter year in 2015"

Slated to begin operations in the first quarter of 2015, Eurisbank, will be the first fully-fledged Islamic bank in continental Europe. The capital for the new bank in fact comes from a private Saudi Arabian institution, The Investor for Securities, with an initial paid-up capital of EUR60 million (US$76.16 million). Having obtained its license from the Commission de Surveillance du Secteur Financier back in July, Eurisbank will focus on private and corporate banking for the first three years as preparatory steps before entering the retail market.

The Islamic finance market is projected to show increasingly positive trends in Muslim majority countries and economies. There has always been healthy competition between individual jurisdictions to lead within those established regions and this progress is starting to emerge in Europe, where individual countries each aspire to lead and bring to Islamic finance the capabilities and services that they have previously brought to its conventional counterpart. Coupled with the improving economic and financial situation in Europe, market participants currently anticipate that recent developments will enhance cross border connection for Europe with other Islamic financial marketplaces, further building momentum for Islamic finance activities across the region.

Rock bottom borrowing costs drive GCC boom

In a turn that looks worryingly familiar, the GCC economy is once again surging forward based on exceptionally low borrowing costs and a booming real estate market that is blithely refinancing to take advantage of the rock bottom prices. But does all this activity rest on firm foundations – or are the emirates once again building castles in the sky?

In recent months, some of the biggest names in the Gulf have taken advantage of the current economic climate to renegotiate their loan facilities and take advantage of the low borrowing costs and improved sentiment among financial institutions in the region.

Foreign banks are keen to move in to take advantage of the booming macroeconomic situation, while the local banking system is flush with cash and keen to lend, making the climate ideal for firms with strong credit profiles to refinance while the going is good.

Race to refinance

In 2013 major names including Dubai Duty Free, the UAE Roads and Transport Authority and Emaar Properties all renegotiated existing loan facilities – reportedly in some cases to below 50% of the original cost.

On the 30th June, DP World signed a five-year US$3 billion financing facility (including a US$610 million Shariah compliant loan) in order to replace an existing US$1 billion debt due to mature in 2018.

The new facility pays just 150bps over LIBOR, compared to a previous 225bps. Triple the size of the previous loan however, some may wonder whether the lower borrowing costs are enough to justify the size of the extension, especially as the previous facility had already been renegotiated once before to extend its lifespan.

Repaying the debt

Some of the most notorious names from the 2008 property crash, which brought Dubai to the brink of bankruptcy, are also now taking advantage of the favorable conditions to make early

repayments and move back into growth territory. In January of this year, Dubai Group agreed a US$6 billion deal with lenders in one of the first big names of the Dubai crash to restructure.

On the 25th June it was announced that notorious property developer Nakheel would repay all of its bank loans four years early, amounting to around US$1.5 billion, and focus on building hospitality projects. The total loan sum will be repaid in August 2014 instead of March 2018, according to chairman Ali Rashed Lootah; using Nakheel's own income rather than any government support funding.

However, the firm is now stepping up the pace again as it looks towards new opportunities. According to CEO Sanjay Manchanda, it plans to develop over 2,900 hotel rooms and 7.9 million sqf of retail and leasing space over the next three years. This ambitious expansion plan needs financing, and the company is therefore hoping to pay off its debts.

The early repayment should save the firm around AED400 million (US$108.89 million) in interest payments. However, Nakheel does not currently plan to pay off the 10% Islamic bond due in August 2016, which was also part of its original restructuring deal; and there is no word as to whether it plans to issue any further Sukuk to fund new projects – although it is reportedly considering an IPO in the next few months.

On the 1st July, the troubled Dubai-based Amlak Finance, which is 45%-owned by Emaar Properties, also announced plans to restructure a further US$2.7 billion in debt, starting with an initial 20% down-payment to depositors with the remaining debt to be turned into a convertible instrument and paid over a period of 12 years. "Following the meeting, depositors have been given two months to assess and accept Amlak's restructuring package after which Amlak will be able to start repaying its debt and take the next steps to lift the suspension of the trading of its shares, which has been in place since 2008," said a spokesperson for the firm. The creditor committee is being advised by Emirates NBD, Standard Chartered, Dubai Islamic Bank, Abu Dhabi Islamic Bank, Dubai's Department of Finance and the National Bonds Corporation. The last published financial results for Amlak, in Q3 2011, reported a loss of around US$10.9 million, according to the Dubai Financial Market (DFM). The proposed restructuring has seen Emaar shares surge by over 8%. The deal is one of the last of the big names of the Dubai crash to restructure.

Government participation

And it is not just the private sector that is taking advantage of the attractive opportunities. At the end of June this year Borse Dubai (the holding company for the UAE stock exchanges) refinanced a US$500 million Shariah compliant loan at one of the lowest rates yet, taking on a new three-year facility with Dubai Islamic Bank at just 90 bps over Libor to replace a previous three-year loan with Emirates NBD costing a reported 210-220 bps.

Strong markets

The Borse Dubai loan not only demonstrates the optimism in the region's banking system, but the strong recent performance of its recovering equity markets. Although the GCC stock markets, especially in the UAE, have seen some volatility in recent months, overall performance has surged over the past year. Although the Dubai equity market plummeted over 20% in June, and Abu Dhabi fell 13%, the UAE has seen a strong recovery over the past month, with Dubai reaching a nine-month high last week as firms retaining strong credit profiles continue to scramble to refinance while bond and loan market conditions remain healthy.

According to Bloomberg, DFM's net profit rose eightfold to US$58.6 million in Q1 of this year, led by a surge in blue chip banks and property stocks. Last week the DFM jumped by almost 5%: with top gainers including Union Properties (up 10.5%) and DFM itself (up 12.6%). Although the DFM fell by 6% on the 20th July (the biggest fall in the last month) it rose 2.5% again on the 21st July to beat investor expectations – despite the continued decline in shares of the troubled Arabtec (which accounts for 5% of the total trading value of the DFM), which fell a total of 11.5% between Friday and Monday.

> **"Property firms and banks are the main drivers of the new economic boom, as the cycle rotates with banks keen to lend to the booming real estate industry as demand improves"**

Real estate and banks lead the way

Property firms and banks are the main drivers of the new economic boom, as the cycle rotates with banks keen to lend to the booming real estate industry as demand improves. The price for mid-range apartments in the UAE is estimated to have risen by over 40% last year, and almost 5% in the first half of 2014, according to data from Cluttons. And as firms are able to achieve loans at a lower cost, they are increasingly keen to refinance and extend their liabilities in order to leverage this favorable credit climate.

So far, it all seems to be going well. Emaar Properties, the largest listed developer in the UAE, saw a rise of 2% while Aldar Properties also rose 5%. Banks also performed well: with Dubai Islamic Bank and First Gulf Bank surging by 3.1% and National Bank of Abu Dhabi rising 1.7%.

Emirates NBD, the UAE's largest bank with around a 17% share of total banking assets, recently reported a reduction in its ratio of non-performing loans (NPLs) to below 14% in the next 12 months, as it benefits from the positive economic climate. The bank, which recently saw Moody's raise its rating to 'Baa1' and to stable from negative, expects a strong credit profile to continue: with a cost to income ratio standing at 35.7% last year, down from 36.7% in 2012.

Continued strength

The UAE is expected to see a continued surge in economic performance over the coming years, with Moody's predicting GDP to grow by up to 4.4% in 2014-15 compared to 3.3% in 2010-12 – supported by enthusiastic public sector spending and strong growth and increased diversification in the private sector.

This recovery should improve cash flows for the major government entities that have been using the current climate to restructure their financing, and concurrently support improvement in bank profitability through the lower cost of funding. Emirates NBD have

already seen its profits surge, by 27% between 2012-13 to almost US$1 billion, and the trend is expected to continue into next year.

Strengthening the state

The strength of the market and the improvement in the region's debt profile has also driven down Sukuk yields to record lows this month: falling 45 bps since January to just 4.19% as of the beginning of July, according to JPMorgan Chase – an even bigger drop than conventional bonds, which have seen a 33 bps decline in yield to 4.08% during the same period. The yield on Dubai's Islamic notes due in May 2022 reached a record low of 3.39% on the 9th June.

> **"The Dubai government announced the launch of a mega new project to build a new entertainment and hotel district, including the world's largest shopping mall, the 'Mall of the World', which gave yet more investors the sign to plunge deeper into real estate stocks"**

This has spurred a spate of government refinancing, including US$20 billion in government debt to Dubai. In March this year the Abu Dhabi Department of Finance signed an agreement with the Central Bank of the UAE and the governments of Dubai and Abu Dhabi to extend two tranches of US$10 billion (including one loan and one bond) for a further five years at a rate of just 1%.

No bubble

And although it could be feared that a new bubble is forming, with the surge in property development and the new enthusiasm by cash-rich banks for renewed financing deals, the authorities insist that this is not the case. "[The] signing of these agreements is consistent with the UAE's prudent financial policy which aims at supporting and promoting economic growth," said Khalifa Mohamed Al Kindi, chairman of the board of directors at the Central Bank. "We at the Central Bank are constantly seeking to maintain a strong economy and a sound banking sector."

However, not everyone may be so sure. Last week, the Dubai government announced the launch of a mega new project to build a new entertainment and hotel district, including the world's largest shopping mall, the 'Mall of the World', which gave yet more investors the sign to plunge deeper into real estate stocks. Although debt yields have dropped and credit profiles strengthened as growth picks up ahead of the Expo 2020, some observers are concerned about the growing over-confidence, which could lead to artificial inflation in the industry. And while many developers have benefited from the recent boom, some have not been so lucky. Limitless LLC, a Dubai World company, recently requested a two-year delay in debt payments, as well as a reduction in the margin on its US$1.2 billion Islamic facility, suggesting that risk still remains in the market for those firms not shored up by strong cash reserves and credit profiles.

Caution prevails

With soaring property prices and banks once again pouring cash into the construction industry, the signs of unsustainable demand are starting to look all too familiar. And although the authorities insist that they have taken the necessary steps to regulate the market this time round, the rapidly accelerating cycle should be raising concerns.

According to Knight Frank, Dubai property prices rose by 27.7% between January and March this year, the fastest of all the major global markets, while rents rose around 30% in the same period. And while banks may currently have the cash to support this growth, such a surge is simply not sustainable in the long-run.

The current boom in the Gulf economy is supported by strong economic factors and upcoming projects such as the Expo 2020 will continue to drive growth forward. But as firms race to refinance and borrowing costs continue to fall, investors should start to take a long, hard look at where all this frantic speed is heading – and whether they want to remain in the driver's seat, or get out while the going is still good.

Liquidity and secondary markets

One of the most commonly used secondary market options for liquidity purposes are treasury bills, which central banks globally use for draining liquidity while financial institutions participating in the global markets also use them as part of their liquidity management strategy. The securities are highest rated available and provide Basel III ratio benefits, as well as being very liquid in the secondary markets in most countries. ABDULBASIT AHMED AL-SHAIBEI explores their usage in the Islamic sector.

For central banks without effective monetary instruments, draining surplus liquidity can be a daunting task, as under normal circumstances, open market operations in various forms are the main mechanism through which central banks can provide or withdraw liquidity to and from the money market, steer short-term interest rates and signal the stance of monetary policy. Most central banks have at their disposal various types of open market operations and these include: outright transactions, repos, issuance of debt certificates, foreign exchange swaps and fixed-term deposits.

Without sufficient securities, the central bank's success in draining surplus reserves will be limited, as will any impact on interest rates. Government securities and central bank bills are the main debt instruments used and to different degrees, their primary issuances have been used to drain surplus liquidity for monetary policy and liquidity management purposes, with the focus typically on government securities (treasury bills) and central bank bills with maturities of less than a year. Both securities have low credit risk (virtually zero credit risk) and are located at the bottom end of the risk/return spectrum.

Financial institutions worldwide have further secondary market options using certificates of deposit (CDs) to ensure they utilize liquidity tools to the fullest, and they may have other short-term securities at their disposal that may have maturities with the desired profile for the same purpose. These are usually securities that are highly liquid and rated. Further to ensure the liquidity management, foreign exchange swaps may be utilized ensuring the management of local currencies versus the foreign currency liquidity are equalized, i.e. the local currency surplus or short fall may be accessed via US dollars or other currencies via this mechanism.

Islamic banks have in general for fewer available instruments accessing these global markets. Locally there may be treasury bill issuances, but these are mainly in the primary market and a secondary market is much more limited. Their liquidity mopping is purely done through these primary issuances, when the central banks request bids for accessing these instruments. There may be usage of conventional instruments that have been Islamically structured to create similar mechanisms, but the primary liquidity tools for the secondary markets lie in the Islamic bonds space, using maturities according to the required time horizons for doing so. However, the liquidity is quite low; hence there is a strong need for further developing this market.

The recently launched International Islamic Liquidity Management (IILM) instrument has created a solution to assist Islamic banks in managing liquidity, especially now the maturities are expanding. There is a secondary market that can be tapped and the amounts available have also been on the rise. In relation to foreign exchange swaps, Islamic banks have access via the foreign exchange Waad, which is an Islamic foreign exchange contract with future settlement date, and this tool is very useful to drain or obtain funds in other currencies. This has assisted banks to move local currencies to other currencies, similar to what the conventional banks are doing through conventional means.

> "The financial authority of Qatar is working to develop the debt market to help Qatari companies to diversify their sources of funding and reduce the cost of borrowing and their reliance on foreign funding"

In Qatar, the central bank issues T-bills, which are government debt instruments with maturity for not less one year. These T-bills are sold at a discount lower than their nominal value. The main objectives for the T-bills are to provide the government with a source of funding in local currency, and create a benchmark yield curve of risk free rate of pricing of financial instruments.

The financial authority of Qatar is working to develop the debt market to help Qatari companies to diversify their sources of funding and reduce the cost of borrowing and their reliance on foreign funding. Concurrently, the development of a commercial paper market and money market mutual funds will also be encouraged in order to help companies mobilize short-term resources.

Islamic banks in Qatar are constrained by a shortage of Shariah compliant secondary market liquidity instruments, because the central bank T-bills for Islamic banks are based on the Murabahah contract, which does not allow the instrument to be traded.

Morgan Lewis

Our Islamic finance team

advises public and private entities on a full range of Shari'a-compliant investment and financial products. Our practice has experience in conventional and Islamic debt and equity capital markets, banking and structured finance, fund formations, structured products, restructurings and workouts, and project finance. We have worked on the first private Sukuk offerings out of Germany, Luxembourg, and the United States, in addition to Oman, and continue to be active in representing foreign issuers in raising debt and equity from Islamic investors.

together

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