

Sukuk Comparison between IDB (Islamic Development Bank) Case and Qatar Case

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Abstract: This paper aim to compare between IDB case and Qater case, where both focus on investment banking matters, with IDB focusing on trust assets, and Qater concentrating on land parcels and beneficiaries.

Keywords: IDB, Qater sukuk, Sharia Board.

1. INTRODUCTION

The IDB sukuk and the Qatar sukuk work under the same principles of the Sharia Board, but follow their own operational processes with facing considerable level of challenges. In this regard, one of the foremost challenges faced by the IDB sukuk is its resource mobilization in the year 2008, which has recently been substantiated by the issue of trust certificates with a value of \$400 million in the US currency. The unique attribute of the IDB sukuk is the trust asset and its respective portfolio, which enables its bearers to have the right of retrieving payments in exchange of the certificates of the trust assets. On the other hand, the Qatar sukuk mainly focuses on land parcel and its right of beneficiary as the unique factors of exchange wherein the sellers can receive payments within a specified time (Tariq, 2004).

2. IDB CASE

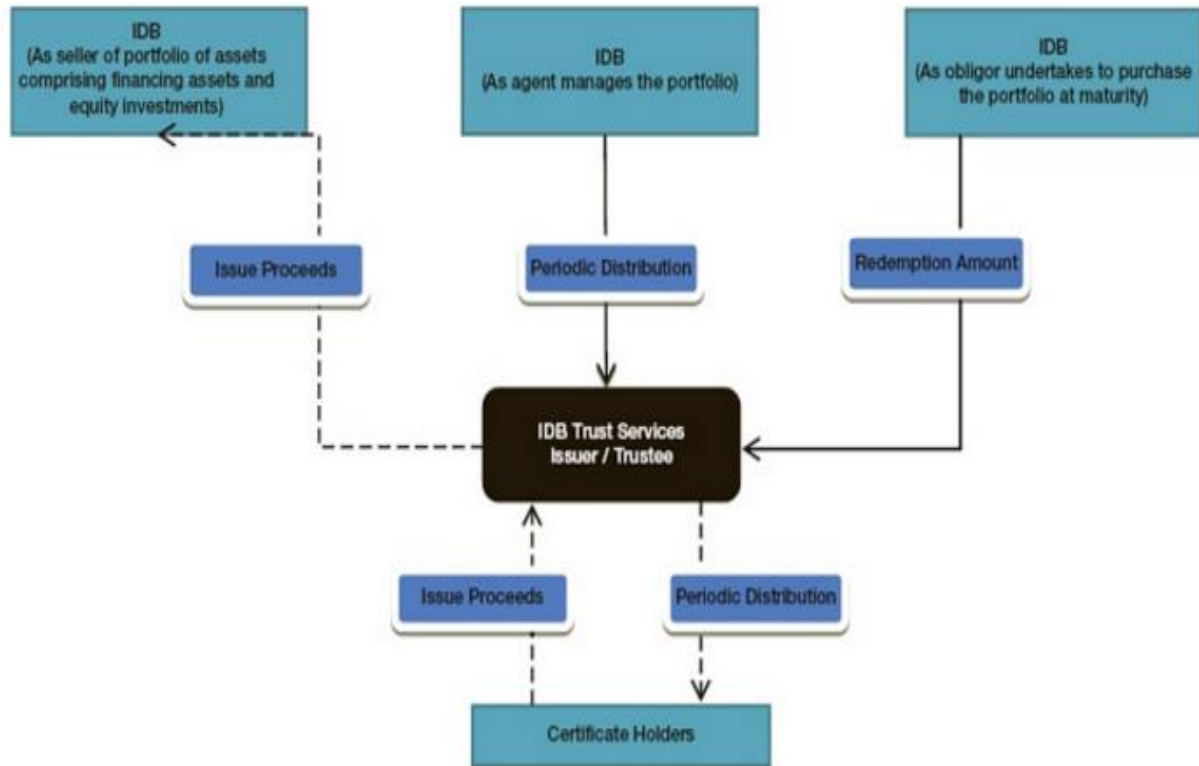
1. Role of the Islamic Development Bank (IDB)

IDB is one of the financial institutions that work for the development of its member nations in the perspective of economic growth. It acts as support for the entrepreneurs of various regions to start up their business operations, thereby leading the nations towards sustainable development and progress in the long run. In the present scenario, the world is facing numerous challenges such as poverty and initiative to reduce poverty from the member nation. In this context, IDB focuses on these issues and ensures social development of Muslim communities as well as member countries. In order to do so, it provides funds as resources to various concerns of trade and production as well as works for the creation of employment opportunities for people. This employment opportunities further contributes to the elimination of the poverty from the roots. The Strategic framework of the IDB Group largely helps in promoting the financial institutions and industries of the Islamic communities thereby leading to enhancement of its positive impacts on the economic condition of its member nations (Islamic Development Bank, 2015; UN Chronicle, 2008).

2. Nature of the IDB Sukuk

IDB was the first financial institution to use bonds for mobilising their funds, which they had termed as 'Sukuk'. The sukuk issued by IDB primarily serves as the financiers for the development of the trading and production concerns in the member countries. From the year 2005, the IDB has been evident of initiating the Medium-Term Note (MTN) program with an increment of US\$ 2.5 billion by the year 2010 (Bacha, & Mirakhor, 2013; Kettell, 2009a). The program also enables IDB to raise awareness regarding sukuk that are issued in series based on the alternate currencies/options, which are primarily used as investments in the development of various firms within the member countries. The most recent sukuk series with maturity date in year 2015 is said to be using a new structure of issuing sukuk called the 'Wakalah

Structure’, where the IDB Trust Service Ltd. acts not only as the issuer but also as the trustee for the same. IDB also employs certain restriction in the purchase of assets with sukuk. For instance, a minimum of 51% should be of the tangible assets (sukuk or shares), while the rest 49% will comprise of the intangible assets. The nature of operation of the MTN program has been illustrated below for the better understanding in the long run (Bacha, & Mirakhor, 2013; Kettell, 2009a).



Source: (Bacha & Mirakhor, 2013)

Figure 1: The Nature of IDB Sukuk as per the MTN Program

3. Islamic Modes of Finance Underpinning the IDB Sukuk

There are various modes of financing as per Islamic finance, and some of them are sole reasons behind the strengthening of the IDB sukuk. The most prominent modes of finance under the Islamic operations underpinning the sukuk of IDB in its member nations are loan contracts, Istisna'a, leasing through Ijara Muntahia Bitamleek, installment sales, and Murabaha (Moody's Investors Services, 2014).

4. Description of the Modes of Finance, Their Work and Relationship with the IDB Sukuk

The loan contract is one of the most significant modes of financing by the IDB in the member countries, which are comparatively less developed in contrast to others. This mode of financing provides the projects with services free of interests and sometimes even at nominal fees for covering the expenses. Another mode is the Istisna'a, according to which the IDB gets involved in a contract with the buyer for the sale of some or the other products or even services at a particular prices and within the pre-specified time. Additionally, leasing through Ijara Muntahia Bitamleek is also an important mode of financing for the retaining the ownership of an asset by the IDB for a particular time span in the form of a lease and is transferred to the beneficiary after the maturity of the period. Besides, the installment sale is another mode of Islamic finance, which comprises of selling particular products to the beneficiary with the payment at regular intervals and at a price higher than that of the actual amount. Murabaha also acts as a significant mode of financing as per the Islamic norms according to which, assets are sold by the IDB at a contract price that entails the profit amount along with the rate to be charged for the passage of time (Moody's Investors Services, 2014).

5. Sharia Board Requirements

The Sharia Supervisory Board is actually a religious board that manages transactions within the financial institutions of the Muslim nations. The board is responsible for proper functioning of the corporate houses, thereby leading them towards immense level of progress and development in the long run. The application of the Sharia norms consists of increasing level of complexity and sophistication of the modern financial endeavors in case of initiating innovative transactions as well as proposals. It also entails the role of investigation in the operational reviews of the transactions as a whole. The proper implementation of these norms into regular working of the financial institutions is likely to bring about a positive change in the transactional pattern (IIBI, 1990). IDB tends to abide the requirements of the Sharia Board in its proceedings related to the implementation of the modes of financing in providing support in the form of ijarah, murabahah and loans among the most important ones. These modes of financing for the development of new and existing projects at the time needs to be supervised by the Sharia Board has made the complex tasks much simpler and smoother to enable proper functioning in the long run. Furthermore, the IDB also implements and integrates the needs of the varied organizations to contribute largely in reducing poverty to the utmost level possible (Greuning & Iqbal, 2008).

6. Relevancy of Corporate Governance

The standards of corporate governance are the foremost important reason behind the great transformation that the world evidences in the Islamic nations at present. The proper connection between different stakeholders also makes the environment largely effective in maintaining the socio-economic setting. This also enables those associated with the financial institutions to stay aware of the entire situations to be ready to accept challenges and mitigate the potential risks in the long run. The financial institutions of the Islamic nations performing under the Sharia Board have been found increasing their standards in the global scenario. This has kept forward an assurance that the developing countries will also be able to escape from the grips of the corporate governance in the long run. Therefore, it is clearly understood that the effectively working corporate governance is undoubtedly important for strengthening the Islamic financial institutions like IDB (Chapra & Ahmed, 2002). As per the case study, a range of 'Islamic-compliant assets' were put on sale by IDB, which was later on purchased by the Islamic Corporation for the Development of the Private Sector (ICD), another member of the IDB. It was then allocated to the trustee that is the Solidarity Trust Services Limited for the issue of the certificates.

7. Innovation

The Sharia board in the present scenario is focussing largely on the competition of the fiduciary duties such as safeguarding the interest of the individual stakeholders, thereby assuring their voluntary and effective participation in the regular operations. The proper implementation of the expertise, competency, as well as the experience of the stakeholders into the operations of the institutions makes the issue of corporate governance one of the most innovative steps towards its sustainability (Islamic Financial Services Board, 2009). Besides, innovation in this issue found in the case study of IDB was that of the involvement of murabaha contracts as well as the istisna contracts within the transactions, which was not identical to the traditional norms of the sharia board (Kettell, 2009a).

8. Rating of the Issue

The Fitch Ratings Ltd. has rated AA for the issue of IDB, whereas the Standard and Poor's Rating Services has rated AAA for the same. The issue rated based on the attainment of subscribed payments by the certificate holders of IDB (Kettell, 2009a).

9. Risks Associated With Investing In Sukuk

Investing in sukuk involves a wide range of risks such as operational risk, systematic risk and most importantly the sharia compliance risk. The operational risk comprises of the risks of default credits and counterparty risks, which are most commonly found among the investors of Ijarah Salam and Istisna'a. The market risk for the investors of sukuk constitutes of the interest rate risks as well as the foreign exchange rate risks. Additionally, the Sharia compliance risk entails breach of contracts and responsibilities from the part of issuer and other risks that creates a gap in adhering to the norms of the sharia supervisory board (Financial Islam, 2015).

10. Result of the Issue

The issue clearly reflects the quality performance of the IDB Sukuk. It was indeed a great success, as most of the Islamic banks and financial institutions depended on attainment of the cash flows. The IDB Sukuk also held the first and the second position in the capital and the securities markets in the global scenario respectively (Kettell, 2009a).

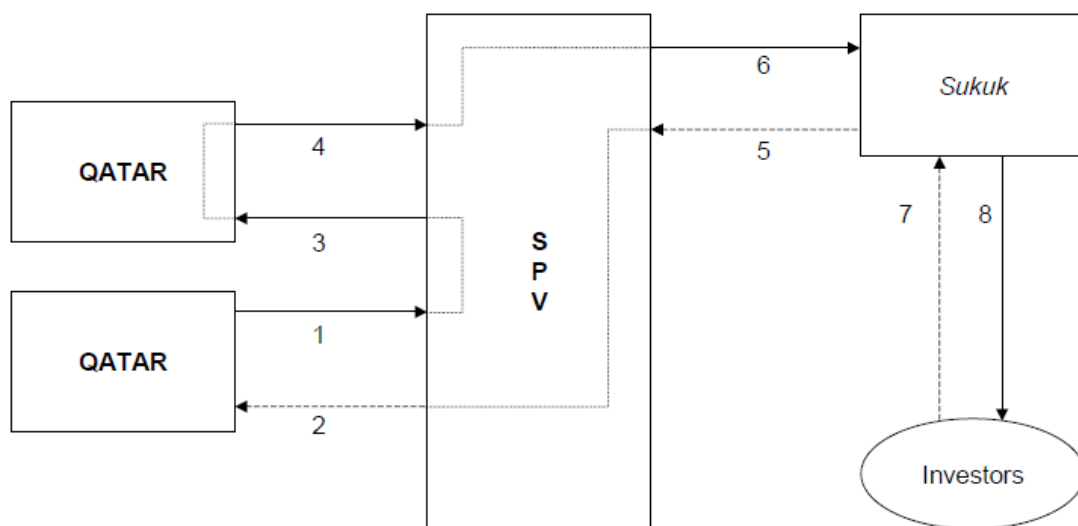
11. Lessons Learnt from the Issue of Future Sukuk

In order to cope with the problems as stated in this case of issue of IDB, certain aspects need to be clearly managed. Measures to overcome constraints, related to the development of products and services as well as encourage innovations, need to be infused into the Islamic finance sectors for its further progress into the modern world. Moreover, further innovations needs to be taken in such a manner that the norms are easily attained under the guidance of the sharia board of supervision.

3. QATAR CASE

1. Nature of the Qatar Sukuk

The Qatar central bank primarily works for stabilizing the value of money to provide assurance of financial stability of nation in the long run. It also acts as a helping hand for the development of the new concerns to some extent, thereby focussing on the global economy (Qatar Central Bank, 2014). The sukuk of the Qatar bank works with the name of Doha Securities Market (DSM) that had started its operations in year 1995. With its continuous progress in business of sukuk or bonds it aspires to reach a position of a regional player. It is completely upgraded exchange that performs electronically with the main purpose of serving its domestic customers in funding at the time of their requirements. The Sukuk of the Qatar bank termed as the Qatar Global Sukuk (QGS) is generally used for funding the public interests by the government of the state of Qatar. Additionally, QGS also helps the government in bringing a substantial rise in the Sharia Compliant Funds. Unlike IDB, which follows the ‘Wakalah Structure’, the QGS is found to be following the ‘Qatar Sovereign Ijarah Sukuk Structure’ (Figure 2) (Bacha & Mirakhor, 2013; Kettell, 2009b).



Source: (Kettell, 2009b)

Figure 2: The Qatar Sovereign Ijarah Sukuk Structure

2. Islamic Modes of Finance Underpinning the Qatar Sukuk

The most prominent mode of finance as covered by the Qatar Sukuk is the Ijarah that is transferring the ownership of property as curtailed with the possession of the respective certificate. The various categories of sukuk that comes under the Ijarah are leasing Ijarah Sukuk, liquidity Ijarah Sukuk, and financing Ijarah Sukuk (First Qatar Real Estate Development Company, 2014; Kettell, 2009b).

3. Description of the Modes of Finance, Their Work and Exact Relationship with Qatar Sukuk

As per the issue of Qatar sukuk, the Ijarah Sukuk is the most important Islamic mode of finance, which primarily aims at attainment of funds from its investors. In this case, the supplier sells the assets to the issuer, who gives it on a lease to the lessee paying a certain sum within the specified period. The ownership of the asset is finally handed over the lease once the lease is matured and the whole amount of payment is completed (First Qatar Real Estate Development Company, 2014).

4. Investment Considerations

The foremost important consideration for investment in the QGS is the absence of its secondary market and the restricted number of the certificate-holders, thereby leading to the fluctuations in the certificates' market value. Moreover, the issuer needs to be completely new in the field of investments and must not possess any such history in any part of the world. The remedial measures for certificates held by the investors are limited in nature and possess any unsecured obligations from the trust's point of view. Another significant aspect that needs to be considered is that the certificate ratings might change at any point of time in turn affecting the certificates' fair value as available in the markets (Kettell, 2009b).

5. Is Qatar A Good Place To Invest?

Qatar is indeed a good place to invest as the government of Qatar guarantees the payment of rentals to its investors on a floating rate, which is equivalent to the sum of LIBOR and margin rate. This will indeed create a situation leading to the maximization of the profit scale for the investors at regular intervals of time and will ensure them of getting the returns in time (Kettell, 2009b).

6. Sharia Board Requirements

The foremost important aspect that the QGC needs to take into consideration is the maintaining the norms of the sharia board in the process of conducting its Ijara rentals. Additionally, it also focuses on the needs associated with the religious contexts of the Islamic community to relate with the actual principles of the Ijara financing. The certificate holders, the issuer, lessee, and the seller of the trust assets needs to understand the operation of the financing mode completely with adherence of the principles and guidelines of the Islamic faith under the supervision of the Sharia supervisory board.

7. Relevancy of Corporate Governance

The corporate governance entails the basic relationship between the various stakeholders of particular concern and the advantages that they tend to earn in their entire proceedings of the operations. In accordance with the issue, the Ijara financing consists of various attributes starting from the buyer, seller, issuer, lessee, leaser and other who is involved with the operations and proper balancing of their workings in regular basis, which makes the corporate governance relevant. The responsibilities are also shared within the members that is stakeholders, who are in complete association with the Sharian principles, thereby making the complete proceeding fair enough to be acquainted with at all points of time.

8. Innovation

The 'Qatar Sovereign Ijarah Sukuk Structure', is originally a traditional mode of financing under the Sharia Supervisory Board and thus there exists the possibility of finding innovations within its proceedings. Additionally, based on the innovation about issue it can be highlighted that the implementation of innovative measures in the operation is likely to bring about a positive impact on the market (IFLR, 2008).

9. Rating of the Issue

Standard & Poor's (S&P) has rated the certificates of the QGS. It has been rated A+ based on regularity in the payments made to the certificate holders on the floating rate as determined in the past (Kettell, 2009b).

10. Result of the Issue

The result reflected that the Trust Certificates worth US\$700,000,000 had been issued with denomination of the value of minimum US\$10,000 on the trust assets of the plot that had been allocated for the Hamad Medical City at Doha region in Qatar. However, the based on the certificate summary it can be mentioned that the equivalent sum is due since 2010 and receiving it can bring better result for QGS (Kettell, 2009b).

11. Lessons Learnt From the Issue of Future Sukuk

The need for innovation is the most important aspect that can be understood from this issue of QGS. The initiation of the newer aspects is likely to lead the sukuk towards immense progress, thereby increasing its potential in attracting the interest of the future investors. The critical factors or issues faced by the Qatar Sukuk are different from case of IDB. The main difference is associated with the mobilisation of resources that is being faced by IDB. Thus, it is recommended that managing the resources would be beneficial for Qatar Sukuk managing certain risk factors.

Identification of the parties:

Issuer - Qatar Global Sukuk QSC

Ownership of the issuer – Land Parcel

Seller - The Government of Qatar

Lessee - The Government

Identify and explain the following elements of the Sukuk Certificates:

Form and Delivery of the Certificates: The issuance of the certificates will be made available in the globally registered form exclusive of coupons and the representations will be made in the Euroclear and Clearstream's depository (Kettell, 2009b).

Clearance and Settlement: The certificate holders are likely to hold the global certificate interests held in the form of a book-entry through the depository (Kettell, 2009b).

Denominations: Minimum US\$10,000 with excess in multiples of 1000 (Kettell, 2009b).

Status: The certificates will individually attain the rank of pari passu, that is the assets undivided ownership (Kettell, 2009b).

The Trust Assets: The land parcel and associated benefits created by Qatar Global Sukuk QSC under the trusts' declaration (Kettell, 2009b).

Purchase Agreement: The agreement between the seller and the issuer of the land parcel, which will give a clear idea of the norm related to the purchase (Kettell, 2009b).

Land Parcel: In case of this issue, the land parcel is the plot at Doha in Qatar that has been allocated for building the Hamad Medical City in the future (Kettell, 2009b).

The Master Ijara Agreement: An agreement displaying clearly the norms related for leasing between the issuer and the government (Kettell, 2009b).

Rentals: The payments made to the investors by the government of Qatar periodically through the transactions accounts (Kettell, 2009b).

Limited Recourse: The process of ownership of the 'Land Parcel' provides those associated with a restricted limit of alternatives to complete their obligations without their individual interests (Kettell, 2009b).

Negative Pledge: The prohibition of both the government of Qatar and the issuer in attaining any kind of security interests on their sukuk or the certificated related to the trust assets is referred to as the negative pledge under the 'Qatar Sovereign Ijarah Sukuk Structure' (Kettell, 2009b; Kamalpour, 2004).

Use of Proceeds: The amount paid to the seller at the maturity of the certificate by the issuer as per the norms of the purchase agreement (Kettell, 2009b; Kamalpour, 2004).

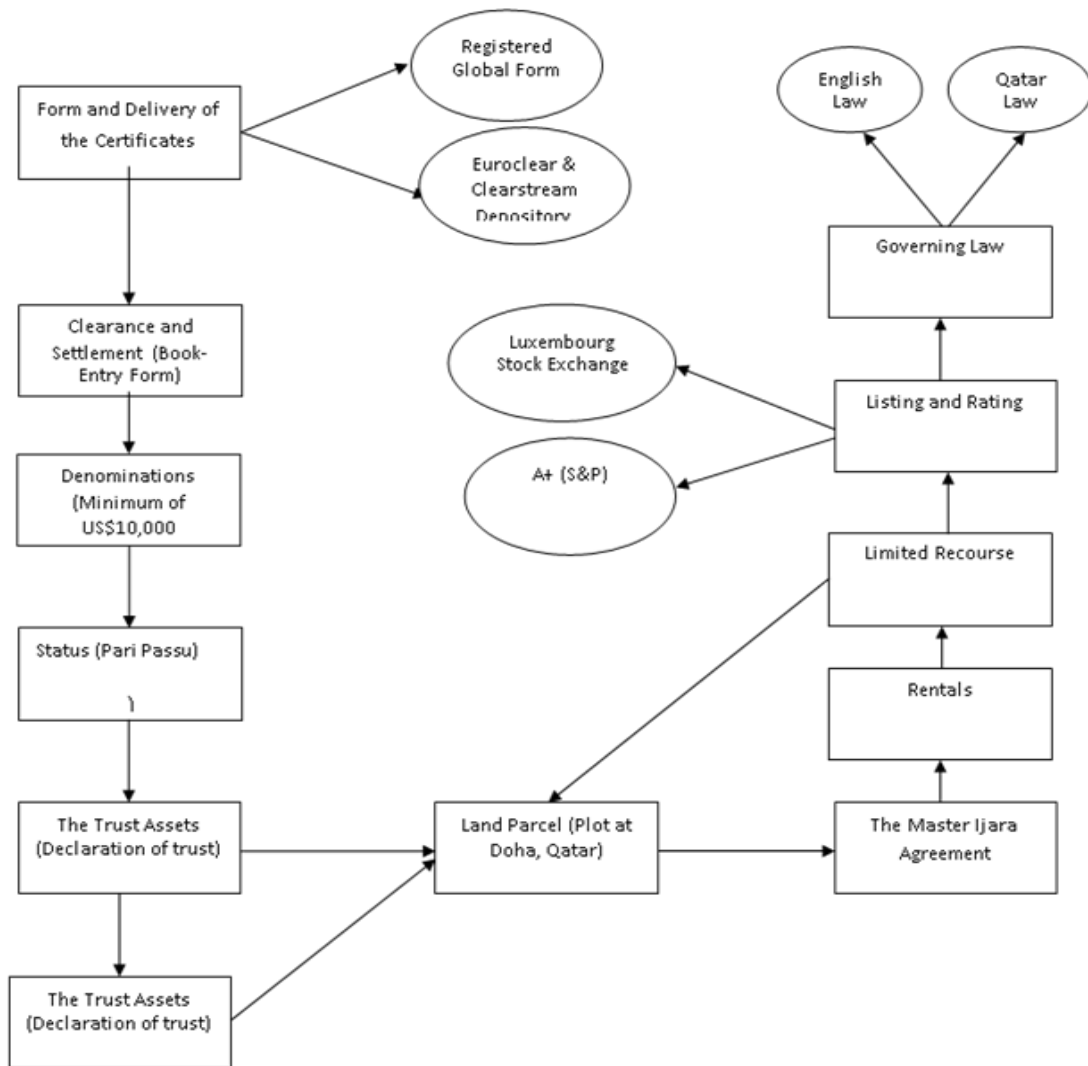
Listing: The sukuk are primarily listed under the Luxembourg Stock Exchange and even under the Labuan International Finance Exchange (Kettell, 2009b; Kamalpour, 2004).

Rating: The certificates or the Sukuk as found in this issue has been rated A+ by the exchange of S&P (Kettell, 2009b).

Governing Law: The bodies governing the entire proceeding of the Ijara for the QGS are categories primarily under the two main heads

- **English law** governing the agency agreement, declaration of trust and the Certificate Purchase Agreement
- Qatari law, the governing head of the Master Ijara Agreement, the purchase agreement, the sale undertaking, the purchase undertaking, the Share Agency Declaration, the costs undertaking and the agency declaration

Flowchart



4. CONCLUSION

From the above discussion and comparison being made, it is quite clear that the investment criteria for the IDB and the Qatar sukuk are largely different in their proceedings and therefore need to be clearly manifested. From the perspective of an investment consideration, the Qatar sukuk primarily provides its clients with the services that are related to leasing of a land on the floating rate of interest and on a quarterly basis. The rental payments on the other hand are calculated on a half yearly basis so as to avoid any kind of complexity as well as make the sum payable throughout the entire tenure. On the other hand, with respect to the facet of investment consideration, the IDB sukuk, unlike the Qatar sukuk, can be traded only based on the primary markets, which makes the instruments entirely secured for the maintenance of accuracy. This again involves the proper exchange of the funds as a part of the contracts, thereby making the investment criteria to be one of the decisive factors for making adequate level of debt arrangements.

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