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THE EXPANSION OF ISLAMIC BONDS ''SUKUK''

IN THE INTERNATIONAL FINANCIAL SYSTEM.

GRADUATION PROJECT PRIOR OBTAINING THE UNDERGRADUATE DEGREE IN INTERNATIONAL STUDIES WITH EMPHASIS IN FOREIGN COMMERCE

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DEDICATED TO:

My grandpa *Lolo;* my example, guide, pride and friend.

José

My parents and my sister, who have always been on my behalf.

Mateo

WE WANT TO THANK OUR POFFESOR LUIS TONON ORDOÑEZ FOR HIS VALUABLE SUPPORT, TRUST AND DEDICATION AS A DIRECTOR OF THIS INVESTIGATION.

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RESUMEN

Desde la perspectiva global de las finanzas internacionales, este estudio analiza y describe el Sukuk; un mecanismo diferente de financiamiento basado en principios islámicos que se ha desarrollado de tal forma que, en la última década, ha dejado de ser un instrumento exclusivo de las economías de países islámicos y se ha internacionalizado. A 2016, varios países no islámicos, además de organismos multilaterales como el Banco Mundial y grandes corporaciones ajenas al islam emiten títulos Sukuk en mercados internacionales para financiar sus necesidades, lo que hace que el análisis del desarrollo y la expansión del Sukuk un fenómeno de interés global.

ABSTRACT

From a global perspective of international finance, this study analyzes and describes Sukuk; an alternative financing mechanism based on Islamic principles. This instrument has developed in such a way during the last decade that it has ceased to be an exclusive security of the Islamic economies and has become international. By 2016, a number of non-Islamic countries, multilateral organizations such as the World Bank and large non-Islamic corporations, issue Sukuk bonds in the international financial markets in order to finance their needs. This makes Sukuk´s development and expansion analysis a phenomenon of global interest.

INTRODUCTION

Our interest in international finance has raised the curiosity to understand the development of a type of security called "Sukuk", a specific Islamic financial instrument that has left the borders of the Islamic economies and has reached the most important financial centers of the world.

This study seeks to be a contribution to the field of International Finance and academia in general, addressing the issue of the expansion of an Islamic financial product to the international financial market from a global perspective.

Islamic economic practices are governed by Islamic principles reflected in the Sharia'a, known as Islamic law. This law rejects a variety of practices in the daily life of Islamic societies. These principles also regulate financial and economic routines. For example, the law opposes the charging of interest on capital and prohibits making investments in businesses that have banned activities such as betting, alcohol and more.

To meet the needs of Islamic economies, for example; provide funding, safeguard money, investing, insurance coverage; both the private and public sector have created a variety of financial instruments that comply with the commands of the Islamic law and therefore avoid paying or charging interest on capital.

Sukuk, or Islamic bond, is a financial instrument and one of the major components of the contemporary Islamic financial industry. In the last decade, these financial instruments have transcended Islamic economies and their commercialization is being developed in the largest financial centers around the globe. Non-Islamic countries and corporations are using these tools with more frequency in the international capital market.

This research aims to describe the operation of Sukuk and its development in the Islamic financial market and the international financial market. For this, three chapters have been designed.

The first chapter seeks to describe the origin and structure of these financial instruments in the context of the Islamic financial system. For instance, we analyze the cultural and religious aspects of Islam that are the fundamental basis of these titles.

Then, it describes the Islamic economies, and the actors involved in this system. Finally, we talk about Sukuk, its structure, characteristics and ways of functioning.

The second chapter quantifies the development of Sukuk both in the Islamic economies and in the international financial market in the 2001-2016 period. This section discusses the main features of the Sukuk market and its evolution. Subsequently, it is determined in which countries and in which markets this instrument is being used, the issuers and other actors related to this instrument are identified.

Finally, the third chapter explains the growing use of these instruments by institutions, multilateral agencies and governments which are considered as non-Islamic. For this, the Sukuk issued by non-Islamic institutions are quantified and the characteristics of these emissions are explored. At last, examples of specific cases of non-Islamic emissions are analyzed.

CHAPTER I:
ISLAMIC FINANCE AND SUKUK GENERALITIES

1.1. Islamic Finance: Introduction.

The study of Islamic finance has not only captured the interest of finance professionals and banks but also of the academic field. M. Fahim Khan, head of the research and training division of the Islamic Development Bank, says Islamic finance has become a subject that must necessarily be included in school curriculums in higher education institutes. The study of Islamic finance has developed over the last decade and is an issue of interest both in universities in Islamic countries and in Western countries (Ayud, 2007). There are several factors that have favored this development. Among the main ones are; the globalization of financial markets, technological changes, increasing innovation in financial products and instruments, the birth of several Islamic states and the growing presence of Islam in Western countries (Bellalah, 2013).

But, what exactly is Islamic finance? What distinguishes Islamic finance from conventional finance is that the first is based on Islamic ethical principles which differ from the principles used in conventional finance (Kettell, 2011). These Islamic principles are the basis for all economic or financial negotiations. This Islamic system complies with the commands established in the Sharia'a, also known as Islamic law. It is important to highlight two fundamental aspects of the Sharia'a to understand the differences that have been mentioned earlier. First, Islamic law prohibits the collection of riba - this Arabic term can be understood as the interest in finance and conventional banking. Secondly, the Sharia'a prohibits the allocation of economic resources to practices which promote the haram - the Arabic term which is translated as something forbidden or sin - such as the sale of alcohol, pork, betting business or elements directly contrary to Islamic principles.

It is important to approach the subject of Islam from a holistic perspective, since Islamic practice not only refers to the fulfillment of religious norms, but also covers the whole of a social and cultural system in which most of society develops according to a spiritual and divine guidance (Bellalah, 2013). In other words, almost the entire social system obeys this structure and therefore economic practice is part of it.

Consequently, Islamic financial products and instruments are used in such a way as to follow the principles and norms of this social structure. Every Islamic financial instrument is designed to return to investors the gains from businesses or deals that have been able to generate wealth on the basis of tangible assets and which necessarily share the risk and profits between the parties involved.

The notion of Islamic finance began from a conceptual idea, maintaining the vision of an evolutionary and practical reality. A number of Sharia'a-compliant contracts have been designed, these allow the creation of a variety of financial and banking instruments, finance projects, market development, insurance and reinsurance mechanisms, and risk management products.

1.1.1. Islamic finance: Origins and cultural-religious support

In order to understand the current structure of Islamic finance it is necessary to explain its religious and cultural bases, which have governed Muslim societies for centuries. Islam is the name of the religion transmitted to the world by the Prophet Mohammed, after Allah revealed it to him. Allah is the focal point of the Islamic faith. For Islam followers, Allah represents the supreme, creator of all that exists and the one who will determine the end of times. The Islamic cult considers that in obeying the commandments of Allah, the human being recognizes the existence of such in order to live in harmony with the universe (Kettell, 2011).

Within Islam there are several books and sources that set the guidelines of the daily life of its believers. First it is crucial to name the Sharia'a, recognized as the body of Islamic law. It is said that is based on divine guidance as it is directly derived from sources such as the Qur'an and Sunnah, these texts will be explained in the following paragraph. The literal translation of Sharia'a into English is: the path that must be followed. Sharia'a is of such importance to Muslims because it covers all aspects of the Islamic faith, including the beliefs and daily practices that must be carried out by Islam´s followers. Within the Sharia'a it is explicitly mentioned that Allah is the sole provider of laws and that the Ummah - the nation of Islam - is simply its confidant and follower. It is by this principle that the Ummah (the people) maintain a derivative power to create laws, but not an absolute power to create prerogative laws. Consequently, Muslims believe that only by following the guidance of this sacred text is it how they will be freed from bondage and find the way to Allah. This is why the faithful of this religion are forced to follow no other path than that established in their sacred text (Iqbal & Mirakhor, An Introduction to Islamic Finance, 2011) (Kettell, 2011).

The Qur'an is another crucial book for Islamic societies. The Qur'an is normally defined as the physical proof of the revelation that Allah made to Prophet Mohammed. This is considered as the main guide of Muslims and as the first source of the Sharia'a. The second source is the Sunnah, which refers to the practices and explanations of the Prophet Mohammed from the rules prescribed by Allaah in the Qur'an. The third source is the Ijma, which is the consensus of opinions of the Ulema - the Arabic word that names the group of scholars of Islam. Finally, the fourth source is the Qiyas, which in Islamic law is considered as analogous understandings applied to the deductions of the legal principles of the Qur'an and Sunnah. Which means, Qiyas serves as deductions from the Islamic scholars about Islamic law in order to adapt it to the daily life of the community. (Iqbal & Mirakhor, an Introduction to Islamic Finance, 2011).

It is important to mention again what was explained in section 1.1 on the two fundamental aspects that stand out in the Sharia'a and which transform Islamic economic practices by differentiating them substantially from conventional economic practices. The first aspect is the prohibition of collecting Riba. This Arabic term literally refers to excess, addition or surplus; while as an associated verb it implies an increase, a multiplication, an excess, practicing usury or demand more than due. (Iqbal & Mirakhor, An Introduction to Islamic Finance, 2011).

It can be found in the Qur'an several passages that refer to the prohibition of Riba. For example, in the part of the Qur'an - Al Baqarah S. 275 mentions the following:

> *"S. 275: Those who feed on riba will not be present (on the Day of Resurrection) except as people beaten by Shaitan (Satan) guiding them towards evil. This is because they say: "Trade is only as riba", however, Allah has allowed trade and prohibited riba. So he who receives a warning from the Lord and stops his supply of riba will not be punished for his past; every case is left for Allah to judge; but anyone who returns (to riba), such as the settlers of Hell - will remain there"*

According to the Sharia'a, Riba technically refers to the "Premium" or additional value that has to be paid by the borrower to the lender in conjunction with the principal amount as a condition of the loan or by an extension to prolong the term of one loan. There are four characteristics that defines it: it is positive and agreed before its use, according to a term and amount of a loan, its payment is fully guaranteed without giving importance to the purpose for which it was borrowed and, as last, the state apparatus sanctions and enforces its collection (Askari, Iqbal, & Mirakhor, 2015).

In other words, Riba refers to what in the conventional economic practices of the West is known as interest.

The second fundamental aspect that stands out in the Sharia'a is the prohibition of allocating economic resources to activities that are considered as haram - Arabic term that is translated as something forbidden, or sin. These activities are the sale of alcohol, pork, pornography or elements directly contrary to Islamic principles; such as gharar - term referring to uncertainty - and, Maysir - arabic word meaning bets (Bellalah, 2013).

Given the existence of a set of beliefs, principles, prohibitions and guides for followers of Islam, it is not surprising that the practical Islamic economy is consistent with what Islam requires. In economics, commerce and finance, all the commandments and guidelines must be fulfilled. In this way Islamic society has had to consolidate institutions, instruments, rules, regulators, types of contracts and a variety of characteristics and components that allow to satisfy the needs of the economy without attacking the principles established in its sacred texts. In an Islamic economy, the State is obliged to take measures against casualties which can distort the functioning of the market (Qur'an - Al-Baqarah 2: 281). Experts in Islamic economics and Sharia’a applicability control agree that the state should emphasize four fields of action to ensure the proper functioning of an Islamic economy (Ayud, 2007). These are:

1. Ensure adherence to the Islamic code of conduct (principles, guidelines and beliefs) by individuals through education, and when necessary through compulsion.

2. The maintenance of good conditions in the market to ensure its proper functioning.

3. Control in the allocation of resources and distribution of income affected by the market mechanism, guiding and regulating it, as well as, if necessary, direct intervention and participation.

4. Take positive measures in the field of production and capital formation to accelerate growth.

1.1.2. Types of contracts accepted in Islamic economies

Islamic contracts are the way in which the whole cultural and religious components are materialized in the economy. There are certain ways of doing business that are compatible with the principles mentioned in the previous section. Thus, certain standards have been developed in Islam that allow society to carry out its commercial and financial activities. Among the most used, it can be identified seven types of contracts. These basically guide all types of transactions. Brian Kettel in his book "Introduction to Islamic Banking and Finance" describes the following types of Islamic contracts and their operation:

- ***Murabaha*****:** The Murabaha contract refers to the sale of goods with a defined profit margin previously agreed upon by the parties. In its original sense, it does not have to do with finance, if the seller agrees with the buyer to provide him with an asset that has a marked gain on the cost, that transaction is already called Murabaha. This term refers simply to a sale. The only characteristic that distinguishes it from other types of sales is that the seller of the property expressly tells the buyer what cost was incurred and how much profit is marked on that price.

  However, the use of this contract within the Islamic financial system is very frequent, especially within Islamic banking. Within this sector two classes of Murabaha contracts are used. The first, when an Islamic bank buys goods and makes them available for sale without any promise of prior purchase by a consumer. The second is when an Islamic bank purchases goods that were previously required by a consumer. Once under the possession of the bank, the bank sells the assets to the consumer who requested them, who previously knew the original cost and the profit obtained by the bank.

This type of transaction does not violate Islamic law since the bank would be financing the purchase of an asset by buying the asset on behalf of its client and adding a profit value over the cost before selling the asset to its customer. The customer knows the cost and the difference on the final transaction price or benefit, thus avoiding the collection of riba, since a physical asset is financed and transferred, not lent or receiving money itself.

- ***Mudarabah*:** This contract refers to a type of business in which one party provides the capital, while the other party provides personal effort and time in that same business. The profits are divided into previously agreed proportions. In case of not having generated any profit both parties face a loss, the party that provides the capital is affected because it would have lost all or part of the amount contributed, whereas the loss of the other part, in this case, would be that did not obtain any profit or gain for its effort and time invested in the development of the business. The one who finances is called Rab ul Mall and the other part Mudarib.

  Within Islamic banking this type of contract can also be used in two ways. The first form occurs when the Islamic bank acts as financier and the other part as an administrative partner. In this case the profits would be shared depending on the agreed percentage. If no profits are generated, the one that would assume the loss of capital would be the bank. The second, when the Islamic bank acts as Mudarib as it accepts to handle the funds of its depositors, who this time would be the Rab ul Mall. Likewise, the profits would be shared according to a previous margin. And, in case of loss, it is assumed by the depositors unless in the process there has been misconduct, negligence or violation of the conditions agreed by the Islamic bank.

  It is firmly held that this type of contract complies with Islamic law since in the biography of Prophet Mohammed it is proven that before his revelations, he traveled to Syria as a Mudarib making use of the capital of Khadija, who later became his wife. This argument would be grounded as Sunnah (practices and explanations of the Prophet Mohammed).

- ***Musharaka*:** The Musharaka class contract involves a type of partnership in a business, and can be defined as an association in which two or more people combine either their capital or labor (can be in equal or equivalent amounts) jointly, perceiving similar rights and obligations. In this type of contract the profits are shared. On the other hand, when there is a loss, unlike the Mudaraba type contract, it is distributed in proportion to the contributed capital. It is not permitted by Islamic law to stipulate something contrary in terms of losses. Here, each partner is both agent and guarantor of the other.

As far as Islamic banking is concerned, the Musharaka is a form of association between the Islamic bank and its clients where each side contributes capital, in equal or different amounts, to establish a new project or to become involved and share an existing one. In this case each party becomes the owner of capital on a permanent basis, that is to say forever or in a decreasing way, where its position is eventually reduced. In addition, profits are distributed according to the proportion established, just as the losses, as mentioned before are shared in proportion to the contributed capital.

To confirm that this type of contract complies with Islamic law, it is necessary to use the Ahdith - a term referring to traditional Arabic quotes. The legality of this type of association is evident in the following Arabic sayings or proverbs: "The third which is left to you must be shared" (An-Nisaa 12) this saying goes along with inheritance; it does not matter how small, it must be shared. Another says the following "there are really many partners (in business) who hurt each other; this is not the case for those who believe and base their work on acts of justice "(Saad 24), the latter emphasizes the importance of justice, loyalty and good in business.

- ***Ijara*****:** This is a term of the Islamic Fiqh – which refers to Islamic jurisprudence. It literally means giving something in exchange for an income. This type of contract can be used in two situations. The first and most common is related to the use or usufruct of assets and properties. In this case Ijara means transferring the usufruct of a particular property to another person in return for an income required by it. This type of Ijara can be compared with what in Western practices is known as leasing. The second situation of ijara is when the services of a person are used in exchange for a salary or wage. In other words, it refers to the services offered by people.

  This type of contract complies with Islamic law since Sharia'a allows a fixed charge on tangible assets upon financial assets because, by converting financial capital into tangible assets, the financier has already assumed risks for which the compensation is permissible. This is the key element that makes this type of transaction acceptable from the Islamic point of view.

- ***Istisna´a*:** This term refers to a type of sale contract in which the buyer asks the seller for the manufacture of a specific product. In most cases, the seller's raw material is used and a price is agreed beforehand. However, it may be previously agreed that the seller will supply with the raw material or only the labor.

  The word Istisna'a is a derivative of the Arabic term Sina'a, which means manufacture of a specific material. This type of contract is frequently used within the Islamic Financial System. It is used when a customer requires a good, an equipment, a construction or a project that needs to be manufactured or assembled. The customer can approach a bank to apply for an Istisna'a contract for financing. The bank offers the construction, manufacture or assembly of the object and then, after adding a profit margin, sells it to the customer.

  There is no direct support in the Sharia'a sources for this type of contract. Even most of Islamic doctrinal schools consider that this form of hiring may be inconsistent with Islamic law. Only a doctrinaire school accepts the legality of this contract, the Hanafi School, and this because somehow there is a need within society and in conventional practice (urf) to have an acceptable Islamic form of project financing.

- ***Salam*:** This type of contract is a transaction in which the seller is responsible for providing the raw material to a buyer on a predetermined date in exchange for a price fully paid at the time of the conclusion of the agreement. In this type of sale the price is paid in full but the delivery of the goods is deferred.

  This type of contract is also used by the banks of the Islamic Financial System. The bank can implement this type of agreement using two Salam contracts. For example, the bank could buy the raw material and make the payment in advance to the supplier once the delivery date has been agreed upon with the customer who wishes to buy the raw material. It can be seen that the bank uses a double Salam contract, one with the supplier and another with the client and thus the transfer of the good between them.

- ***Takaful*****:** This Arabic term refers to Islamic insurance. It is the way in which the equivalent to the insurance contracts in the conventional practices of the West is handled in the Islamic economies.

  Islamic insurance has been proof of the ability of Islamic finance to evolve and innovate. For years it has been an act of faith to believe that conventional insurance is not compatible with Islam since it contains elements of gharar (uncertainty), maisir (bets) and riba (interest). For example, prohibited practices have been strongly rejected as; the inequity in premiums collected or not collected by the insurance companies for late payments resulting in interest and surcharges. However, during the last twenty years Islamic doctrine has been able to adapt and develop alternative forms of insurance.

  Insurance as a concept does not contradict Sharia'a practices and requirements because, in essence, this system employs the Islamic principle of mutual aid. Takaful is an Arabic term meaning mutual or joint guarantee. The main feature that allows the takaful to be free of gharar (uncertainty) and maisir (bets) is the concept of tabarru, which means donation, gift or contribution. In other words, what makes takaful comply with Islamic law is that every participant who needs protection must be motivated with a sincere intention to donate or contribute to another participant who may face difficulties.

  Islamic insurance is a system where each participant contributes to a fund which is used to support other participants. Each participant contributes sufficient amounts to cover expected losses. Its purpose is to pay a defined loss of a defined fund, thus the Takaful contract emphasizes unity and cooperation among its participants.

  The existence of the takaful is based on the hadith, or the traditional speeches of the Prophet Mohammed narrated by his companions. One of them relates the following: one day the Prophet saw a Bedouin leaving a camel in the middle of the desert; then he asked the Bedouin: "Why do not you tie your camel?" The Bedouin replied: "I place my faith in Allah." Then the prophet went on and said, "First secure your camel, then put your trust in Allah." The doctrine holds that what the prophet did in this situation was to motivate the Bedouin to reduce the risk of losing his camel. It is documented that in several stories about the prophet, he insisted on taking actions that allow to reduce the risks.

This section has developed the concept of Islamic finance and its religious support. Likewise, the most common types of contracts in Islamic economic practice have been explained which support all transactions. The Islamic financial system, its structure, characteristics, the size and relevance of the system and its main individual and regional actors are discussed below.

1.1.3. Sharia´a Supervisory Board

To ensure that all financial activities carried out within Islamic society are in conformity with the Sharia'a, it is necessary to create religious directories of supervision within each bank and Islamic financial institution. These are usually called the Sharia'a Board of Directors or Supervisory Committee. It is primarily concerned with examining whether contracts, negotiations and transactions are being fulfilled in order to accomplish and implement Islamic beliefs and principles (Kettell, 2011). Each institution belonging to the Islamic Financial System has an obligation to maintain its own supervision directory. It is stated that these directories have to cover three specific objectives:

- ensure that the services and banking facilities offered are in harmony with Islam;
- ensure that the institution's investments and involvement in projects comply with Islamic law;
- ensure that the management of the financial institution goes hand in hand with Islamic values.

1.2. The Islamic Financial System (IFS)

1.2.1. Concept and development of the Islamic financial system

The Islamic financial system (IFS) is part of the global financial system, and is the group of institutions, regulations, instruments and people that, according to the principles of Islamic economic practice, seek to channel the flow of money into the economy between lenders and borrowers to transform savings into investments.

In the IFS, all financial agreements are materialized through the types of contracts mentioned in the previous section with the intention of sharing both the risk and the possible gains; or in case of losses, these will be distributed too. Derivatives of such contracts are also used with certain adaptations to allow settlements and transactions of large amounts of money while maintaining the basic essence of an Islamic contract. That is why, in this system, all financial instruments are a right to return on a contingent asset and there are no debt instruments with a predetermined or fixed rate of return.

Different ways of delimiting and quantifying the IFS have been identified, for example: the totality of Islamic financial assets, the number of financial institutions related to Islamic finance, the number of countries where Islamic financial assets are used, the number of Islamic banks and its assets, among others.

Table 1: Islamic Financial System – 2016 general overview

	Islamic financial assets – USD Millions	Islamic financial institutions	Islamic banking windows	Islamic banking assets – USD Millions	Countries where Islamic financial institutions are present	Other Islamic financial institutions
IFS	2103542	1329	480	1657087	124	527

Source: IDC – Thomson Reuters

Elaboration: Marmolejo, Mateo y Suárez José

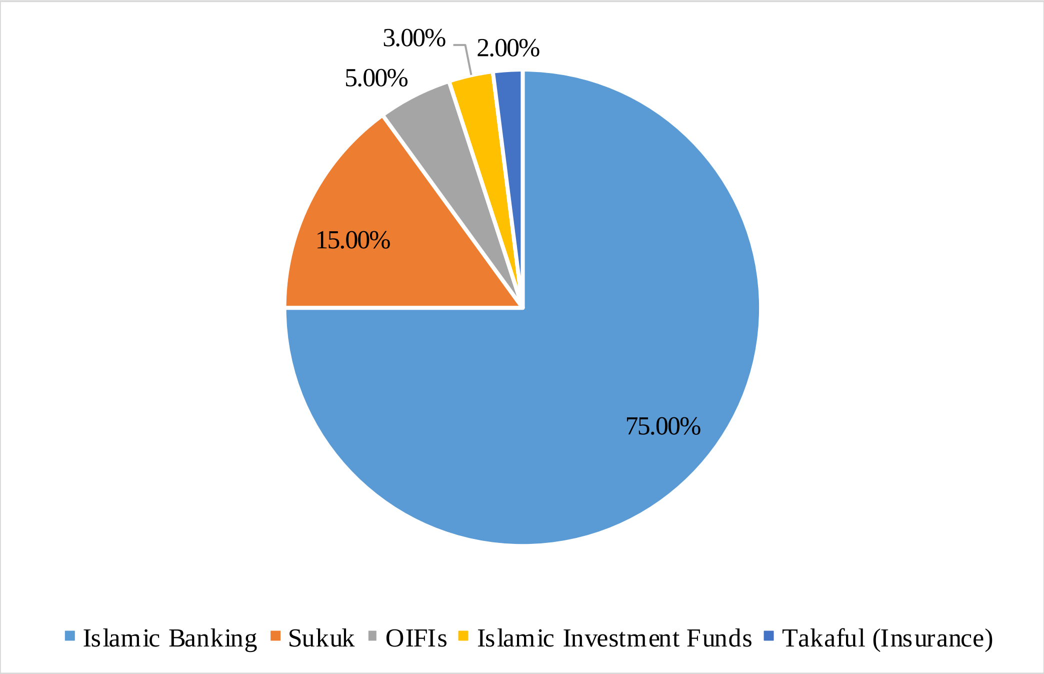
At the moment, more than 1,400 financial institutions in 124 countries participate in the IFS. The Islamic financial services industry has grown substantially over the last twenty years to a total assets of USD 21 trillion and represents 1% of the global financial system (IDC - Thomson Reuters, 2016).

According to the International Monetary Fund (IMF), the development of the modern ISF is due to two fundamental facts, the first is the surplus in the balance of payments of the Arab countries generated from the boom of oil exploitation in the region since 1975. The second factor is due to the socio-political and economic changes that the region experienced because of the birth of a stronger Islamic identity since the creation of the Arab League in 1945, which promoted the development of an economic system based on Islamic moral principles. In addition, external factors such as the integration of financial markets and the liberalization of capital movements permitted the expansion of the Islamic financial system (Iqbal, Islamic Financial Systems, 1997).

1.2.2. Structure and components of the Islamic financial system

The Islamic financial system consists of the following: 1) the Islamic banking system, 2) the Sukuk market (short and long term), 3) the Islamic insurance market, 4) Islamic investment funds, and 5) other Islamic financial institutions or OIFIs (Central Bank of Malaysia, 2013).

Graphic 1: Approximate structure of the Islamic Financial System - Total assets 2016



Source: IDC – Thomson Reuters

Elaboration: Marmolejo Mateo y Suárez José

Islamic banking is the largest component of the IFS and accounts for approximately 75% of the entire system´s assets. The second largest component is the Sukuk market assets, which represents 15% of total IFS assets. Following these are the OIFIs, which cover 5% of assets, Islamic investment funds 3% and lastly Islamic insurance occupy 2% of the entire system according to the total amount of assets. The following is a detailed description of the characteristics and a brief history of the development of each system´s component.

1.2.2.1. The Islamic banking system

Islamic banking institutions are those that base their functioning, practices and operations on Quran´s principles. Therefore, the services provided by these institutions differ substantially from traditional banking, which has no link to religious laws. Islamic banking offers services that are compatible with the religious beliefs of Islam. In particular, its services do not charge or offer interest over capital, on the contrary, there is a form of association between the bank and its depositors as well as between the bank and other people involved in the investments made. In this way, the bank's profits do not come from the difference of the active and passive rate as in traditional banking, but the profits that the bank achieves come from the yield that generates the usage of the available capital. Later, depositors receive part of this benefit in proportion to their deposits (Kettell, 2011).

Islamic banking began to develop in Egypt and Malaysia in the 1960s. The first official Islamic bank was founded in Egypt in 1963. However, the real take-off of Islamic banking occurred in early 2000 and continues to grow today. The expansion of Islamic banking services at the beginning of the present century was driven by the constant emergence of new banks of this type throughout the Middle East and North Africa region. (Bellalah, 2013)

Today, the Islamic banking system is the largest component of the Islamic financial system. Islamic banks handle between 75% and 79.5% of the assets of the IFS, approximately USD 1,6 trillion by the end of 2016 (Islamic Finance Services Board, 2016).

1.2.2.1.1. Islamic banking principles

According to Brian Kettell, the principles governing the operations of Islamic banking are as follows:

a) *Prohibition of pre-established payments: promising or requiring any type of rate, yield or fixed amount on the initial capital of a debt / loan is prohibited.*
b) *Shared benefits or losses: Financiers (investors) and the ones who use the financiers' capital (entrepreneurs) share the risk in pre-established proportions according to the type of contract being used. The lender must share the profits or losses caused by the company, project or beneficiary who made use of the funds received as loan. In bank terms, the depositor, the bank and the borrower*

share the risk of financing a certain business. Meanwhile, in traditional banking the risk is not shared, the borrower must repay the borrowed capital plus the interest, regardless of the outcome of the activity for which the funds were requested and, likewise, the investor should receive his capital plus interest agreed without the need to know what the destination of their funds.

c) *Emphasis on productivity rather than credit quality or solvency: The principle of shared risks in Islamic banking makes the creditor receive benefits only if the use of the funds by the borrower has generated a profit. For this reason, Islamic banks are not interested in the solvency or credit quality of the beneficiary that guarantees the timely payment of capital plus interest, on the contrary, the Islamic bank is interested in the productivity of the beneficiary and that the activity of the funds generates profits.*
d) *Money is only a tool of exchange: You can not create money out of nothing. Islamic principles indicate that money serves to represent the value of things and facilitate their exchange, therefore, money can not generate more money alone. In order to generate a profit, a risk must be assumed and this must be shared at the same time.*
e) *Prohibition of uncertainty: Speculation is flatly rejected. You can not set a benefit. Therefore, options and futures are considered risky and uncertain, that is why these are incompatible with many Shari'a doctrinaires.*
f) *Exclusivity of contracts compatible with the Sharia`a: Islamic banks can not engage in operations contrary to the Islamic principles that govern them. Therefore, only the contracts compatible with this practice are valid (Kettell, 2011, p.35).*

1.2.2.2. The Sukuk market

In traditional finance, there is the money market and the capital market. Money market is a term used to refer to markets where short-term and highly liquid instruments are traded. Usually, these instruments are issued by banks, corporations and governments to obtain funds to meet their needs in the short term. For example, zero-coupon instruments maturing in less than a year, such as US Treasury bills or certificates of deposit, are traded in traditional money markets. The second component is the capital markets, traditionally divided into the debt market (bonds maturing over a period of more than one year) and the stock market.

However, given the prohibition of interest, the IFS is free of a market that resembles purely the debt market as conceived in traditional financial systems.

Therefore, in order to describe the IFS more adequately, most authors agree that it is necessary to consider the Sukuk market in the short and long term as a single component of the IFS, since the Sukuk market encompasses all of the money market and 98% of the system´s capital market. In contrast, the Islamic stock market represents 1.32% of system-wide assets and is not included in what would be the traditional capital market (IDC - Thomson Reuters, 2014). On the contrary, a very significant proportion of Islamic stock market assets belong to Islamic investment funds, which is why stocks are classified under this category (Islamic investment funds). Thus, it has been omitted the classification of money market and capital market, and refers only to the long and short-term Sukuk market.

1.2.2.2.1. Short term Sukuk market

These markets were developed in the IFS thanks to the initiative of governments that began issuing short-term negotiated discount certificates that comply with the principles of Islam and thus meet the liquidity needs of the growing Islamic banking system. The first instruments of this type were issued in 1983 by the government of Malaysia under the name of Government Investment Certificates. More and more central banks in the region were gradually added to this practice. Subsequently, work began on the legal structure that would then allow the generation of long-term instruments, as well as the development of equities compatible with the principles of Shari'ah (Sam R, 2005).

In 2016, Sukuk's total short-term traded assets, similar to traditional money markets, reached $ 1 billion and represented 1.23% of total IFS assets (Islamic Finance Services Board, 2016).

1.2.2.2.2. Long term Sukuk market

Long term Sukuk are considereded those with a maturity of more than one year. This is the second largest element of IFS and accounts for approximately 15% of system-wide assets and amounts to USD 325 billion in 2016 (Islamic Finance Services Board, 2016).

The Sukuk market has experienced a major expansion since 2000, driven mainly by the increasing global commercialization of these instruments. In fact, the analysis of these instruments and their development in international markets is the main objective of this study so their characteristics and operation are detailed in the following section.

1.2.2.3. Islamic Insurance – Takaful

The emergence of the insurance industry in the IFS took place thanks to the development of Islamic banking and the need to cover the risks that were generated in the system. Before the birth of this type of insurance; individuals, consumers and businesses, considered that the classic insurance system violated the principles of Islam due to interest charges.

As detailed above the term Takaful constitutes one of the types of Islamic contract and means mutual aid or mutual guarantee. Unlike the common insurance system, where the risk is transferred from the insured to the insurer in exchange for payment of a premium, Islamic insurance are basically funds where risk is shared. In the Islamic insurance system, each participant who needs protection against some risk, must be willing to donate a part of their money that will be used to help whoever requires it. Thus, it contributes to funds called Takaful which are administered by the participants themselves. The objective of these funds is not to profit but to cover the risks that the participants themselves may incur (Kettell, 2011).

By 2016, total assets of Takaful funds amount to USD 40 billion, representing 2% of total IFS assets (IDC - Thomson Reuters, 2016). Although this type of insurance has limited application and the number of institutions offering these services is small, it is an important component for the development of the entire IFS.

1.2.2.4. OIFIs: Other Islamic financial intitutions

OIFIs or Non-Banking Islamic Financial Institutions are those organizations that are responsible for either mediating, providing information or regulating the flow of funds in the economy. They are usually specialized institutions, for example, brokerage firms, venture capital companies, domestic and international market regulators, rating agencies or real estate institutions responsible for promoting the development of Islamic finance, etc. (Ayud, 2007).

OIFIs can be public or private. By 2016 they managed 5% of IFS assets. Among the most important of the system are the following: The most important stock exchanges in the system; Bursa Malaysia, Abu Dhabi Stock Exchange, NASDAQ Dubai, Bahrain Bourse and Egyptian Exchange. Domestic and international regulators such as; the IFSB or Islamic Finance Supervisory Board or the IIFM International Islamic Financial Market, among others. In addition, the role of multilateral organizations linked to the Islamic Development Bank, which play roles in generating information, fostering the development of Islamic finance and in some cases regulating it (El-Hawary, Grais, & Iqbal, 2004).

1.2.2.5. Islamic investment funds

Islamic investment funds operate in much the same way as common mutual funds, with the exception that their investments are directed only to Sharia'a Compliant Assets. The funds are managed by a specialized entity that is in charge of investing the money of its clients in a portfolio of Islamic assets with short term as well as long term objectives (Ayud, 2007).

Islamic investment funds cover 3% of the total assets of the Islamic financial system. 44% of the assets that are managed by Islamic investment funds correspond to Islamic shares, 39% to money markets (short-term Sukuk), 7% to long term Sukuk, 4% in real estate and 6% in other assets (IDC - Thomson Reuters, 2014).

1.2.3. Main actors in the IFS

The previous section described the characteristics, functioning and structure of the Islamic financial system as a whole. The IFS has been referred to as a global pool of Islamic assets. However, there are sub-Islamic financial systems that make up the global IFS. This is because some countries have developed an internal financial system that is solely Islamic, while other countries like Malaysia have a dual internal financial system; conventional and Islamic. And in other cases where the main system is conventional and there is a slight development of Islamic financial assets. The most important Islamic financial subsystems and the development they have achieved in each jurisdiction are discussed below.

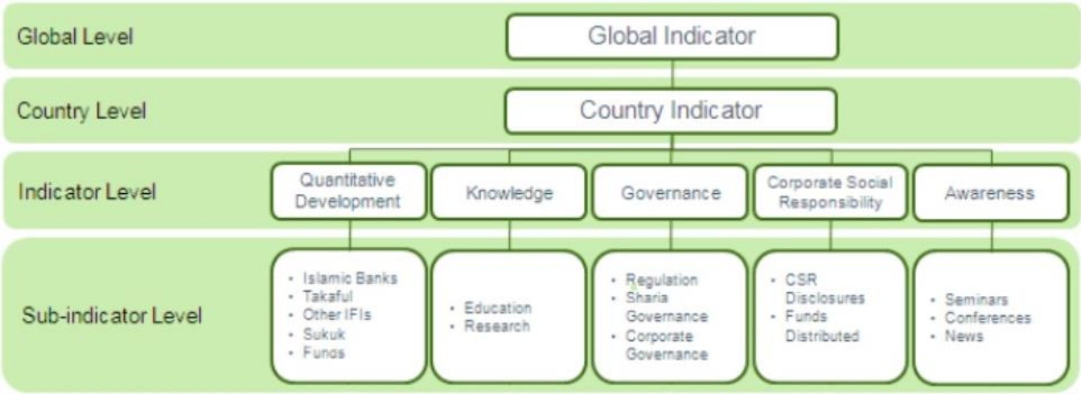
The Islamic Finance Development Indicator (IFDI) will be used to measure the evolution and define the main actors of the IFS. The Islamic Development Corporation (IDC) and Thompson Reuters have jointly developed the IFDI. The IDC is part of the Islamic Development Bank group and Thomson Reuters is one of the leading databases and providers of Islamic financial information.

The IFDI encompasses five key dimensions to measure the development of the global IFS and each of the countries that comprise it: quantitative development, knowledge, governance, corporate social responsibility, and awareness.

The graph below shows the structure of the indicator and its components. There is a total value and sub-levels, these last being the country level, indicator level and level of metric values. The index is constructed from the bottom up, first the metric values are calculated. It is necessary to mention that the metric values assigned are weighted based on a rationalization coefficient. This coefficient adjusts the scale of the values based on three parameters; the GDP, the population and the total of banking assets of each country.

For example, the average of the sub indicators obtained from banks, mutual funds, Sukuk and more constitutes the indicator value "Quantitative Development". Subsequently, the arithmetic average of the five dimensions or indicators constitute the country level indicator. Finally, the arithmetic average of all country-level indicators form the overall indicator (IFG IFDI Team, 2015).

Graphic 2: IFDI methodology



Source: IDC-Thomson Reuters IFDI Rulebook

For this research, it has been considered that the IFDI is the best way to measure the development of the global IFS and at the same time determine who are the main actors of the system. It has been decided to use this indicator because it measures different categories and not only focuses on the quantity or value of the Islamic financial assets of one or the other country. On the contrary, the holistic approach of the IFDI allows to have a better perception of the actors of the IFS.

In 2016, the IFDI assigned a value to 124 countries, however, 80% of the total value of the indicator corresponds to only 25 countries. It can be inferred, therefore, that approximately 80% of the IFS is managed by 25 countries, as can be seen in the following table.

Table 2: Islamic finance participants registered in the IFDI

Ranking	Country	Country Indicator 2016	Global Significance	Quantitative	Knowledge	Corp. Social Responsibility	Governance	Awarenes	Region
1	Malaysia	123.38	11.27%	78	200	43	88	208	Southeast Asia
2	Bahrein	86.92	7.94%	26	54	56	103	195	Golf Cooperation Council
3	United Arab Emirates	66.35	6.06%	21	39	47	63	162	Golf Cooperation Council
4	Oman	52.72	4.82%	8	25	54	61	116	Golf Cooperation Council
5	Saudi Arabia	46.67	4.26%	36	26	102	34	36	Golf Cooperation Council
6	Pakistán	46.16	4.22%	19	41	22	67	82	Asia South
7	Kuwait	44.70	4.08%	34	18	41	65	65	Golf Cooperation Council
8	Jordan	42.43	3.88%	13	69	49	36	45	Others Middle East and North Africa
9	Qatar	38.90	3.55%	21	15	47	47	64	Golf Cooperation Council
10	Indonesia	28.39	2.59%	14	29	23	62	13	Southeast Asia
11	Sudan	25.96	2.37%	17	11	16	65	20	Others Middle East and North Africa
12	Maldives	24.59	2.25%	10	12	24	53	25	Asia South
13	Sri Lanka	23.92	2.18%	7	19	36	24	34	Asia South
14	Brunei Darussalam	22.76	2.08%	6	22	31	44	10	Southeast Asia
15	Palestine	22.62	2.07%	16	11	52	16	17	Others Middle East and North Africa
16	Bangladesh	21.19	1.94%	14	15	27	44	5	Asia South
17	Tunisia	19.88	1.82%	6	61	0	8	25	Others Middle East and North Africa
18	South Africa	19.67	1.80%	6	3	65	19	6	Subsaharian Africa
19	Iran	19.01	1.74%	44	15	0	28	8	Others Middle East and North Africa
20	Singapur	18.47	1.69%	3	3	35	39	12	Southeast Asia
21	Syria	18.39	1.68%	18	7	12	45	10	Others Middle East and North Africa
22	United Kingdom	14.54	1.33%	3	12	18	33	7	Europe
23	Egypt	14.18	1.30%	9	9	10	26	16	Others Middle East and North Africa
24	Yemen	13.53	1.24%	3	8	27	19	11	Others Middle East and North Africa
25	Turkey	13.17	1.20%	5	7	18	15	20	Europe
26	Ohters	226.20	20.7%	95	211	26	302	497	

Source: IDC-Thomson Reuters IFDI Rulebook

Elaboration: Marmolejo, Mateo y Suárez, José.

As can be seen, Malaysia is undoubtedly the most important domestic Islamic financial system of the global IFS. In the last decade this country has become not only a key player in Islamic finance but a renowned international financial center. The second country in the index is Bahrain, not so much by its quantitative indicators but by important levels of governability in the Islamic finance, the directories of supervision of Sharia'a and the systems of control in this country. The latter is considered as one of the most developed, strict and efficient. The third country is United Arab Emirates, a major global financial center characterized by the awareness and inclination towards Islamic finance. The list continues with Oman, Saudi Arabia, Pakistan, Kuwait, Jordan, Qatar, Indonesia, Sudan, Maldives, Sri Lanka, Brunei DarusSalam, Palestine, Bangladesh, Tunisia, South Africa, Iran, Singapore, Syria, United Kingdom, Egypt, Yemen and Turkey.

It is seen that of the 25 most important actors of the system, the majority are located in the zone of the Persian Gulf and Middle East, as in other regions where Islam predominates such as Southeast Asia and North Africa. The exception to this list is the United Kingdom and South Africa, although somewhat distant from Islamic economic practices have been characterized by their importance for the evolution of Islamic finance and the IFS.

In order to analyze the relevance of each region in the IFS, data have been obtained from each IFDI country from 2013 to 2016. Subsequently, each country has been classified into regional divisions. To obtain the value of each region, the values of each member country of the region are summed and then the result is divided for the number of countries that comprise it. Finally, the average of the 4 analyzed years is taken to assign an average regional value, with which it is tried to explain the importance of each region in the IFS.

The first category is made up of the member countries of the Cooperation Council for the Arab States of the Gulf; Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the United Arab Emirates, which as a bloc represent more than 46% of the Islamic financial system based on IFDI values. The second most important region is Southeast Asia, driven mainly by Malaysia. Southeast Asia concentrates on average 18.48% of the system. It is followed by South Asia with 14.89% and then the Middle East and North Africa region (excluding GCC member countries) with 12.24% average IFDI participation. Clearly, the Islamic financial system is concentrated in the four regions mentioned above. Other regions such as Sub-Saharan Africa, other countries in Asia, Europe, North America and Latin America are less important players in the IFS. The following table illustrates the importance of each region as a component of the IFDI.

Table 3: IFDI participants, geographic distribution

Region	IFDI average share 2013-2016	IFDI average value 2013-2016	Countries	IFDI value 2013	IFDI value 2014	IFDI value 2015	IFDI value 2016	Sparkline 2013-2016
Golf Cooperation Council	46.05%	49.65	6	33.90	50.98	57.69	56.04	
Southeast Asia	18.48%	19.93	9	16.93	18.27	22.02	22.49	
Asia South	14.89%	16.06	7	12.58	13.73	19.13	18.78	
Others Middle East and North Africa	12.24%	13.20	14	11.70	13.29	12.46	15.33	
Subsaharian Africa	3.08%	3.32	32	3.47	2.71	3.31	3.80	
Otros Países de Asia	2.52%	2.71	13	3.58	2.46	2.10	2.71	
Europe	1.57%	1.69	32	1.55	1.79	1.85	1.57	
North America	0.70%	0.75	3	0.55	0.86	0.87	0.72	
Latin Amercia & Caribean	0.47%	0.51	8	1.37	0.46	0.10	0.10	
TOTAL			124					

Source: IDC-Thomson Reuters IFDI 2013, 2014, 2015 y 2016
Elaboration: Marmolejo, Mateo y Suárez, José.

1.3. Sukuk: Generalities and functioning

Sukuk are Islamic debt certificates issued by a borrower and owned by a lender. The word Sukuk is the plural of sakk, Arabic word meaning certificate. It is a certificate of ownership of an asset that the borrower grants to the lender as proof of possession of the asset. Sukuk are financing agreements or debt contracts valid for a certain time. These agreements give the lender a right to hold a fraction of a pool of assets that have the ability to generate income. Although, the lender does not have any administrative control over the funded project or transferred assets (Ariff, Safari, & Mohamad, 2014).

These instruments issued by a borrower are asset-backed securities. Subsequently, the certificates (Sukuk) are transferred to a Special Purpose-Company (SPC), which may be owned by the lenders, the borrowers or jointly. Finally, the repayment of the borrowed capital comes from the return of the assets transferred to the SPC.

Therefore, Sukuk are financial debt instruments that require the transfer of assets to a separate entity, the investors own these assets proportionally and enjoy the benefits that these assets are able to generate in the time while the contract is valid.

1.3.1. Historical reference

Several historical documents confirm the use of sakk during the early Islamic caliphates. Muslim society during the pre-modern period used Sukuk as documents representing financial obligations arising from various commercial activities (Adam & Thomas, 2005). During the initial stages of the theoretical and legal development that gave support to the IFS, the written instruments of credit were already a common practice. These instruments can be found in genizah documents; this term refers to a storage place within the mosques and synagogues that is used to place documents that can not be thrown away because it has the name of Allah written inside them. Documents stored in the Cairo Genizah contain fragments indicating the existence of sakk during the twelfth century C.E. – C.E. is a year-numbering system for the Julian and Gregorian calendars that refers to the years since the start of this era, that is, the years beginning with AD 1 - and that certificate was very similar to the form of a modern check. It emphasized the amount to be paid, the name of the beneficiary, the date and the name of the person issuing it (Udovitch, 1979).

1.3.2. Origin of Sukuk structure

Authors Mohamed Ariffm, Meysam Safari and Shamsher Mohamad in their book "Sukuk Financial Instruments: New Forms of Debt Contracts" provide a clear description of the origin of these securities. The most important elements are listed below.

Several investigations carried out in the Mediterranean region, an area marked by its cultural influx, reveals the existence of documents that certify loans made with the purpose of financing a productive project. Interestingly, these loans explicitly indicated a benefit-sharing clause and mutual risk exposure between the parties. The general rule then was that the loan was granted only if the borrower was an asset holder or was to acquire any assets as a result of the financing.

The birth of Sukuk as such is an element introduced by doctrinaires of the Islamic law of the Turkish Empire in order to raise public funding when the emperor asked to get large sums of money to meet the costs of the reconstruction of the empire after having been devastated by the five great crusades that culminated in the year 1258 C.E. This was the beginning of a form of fund-raising that complied with Islamic ethics. This form of financing differed considerably from other Christian practices of the time, based on Babylonian and Greek-Roman law.

1.3.3. Structure and function of Sukuk types

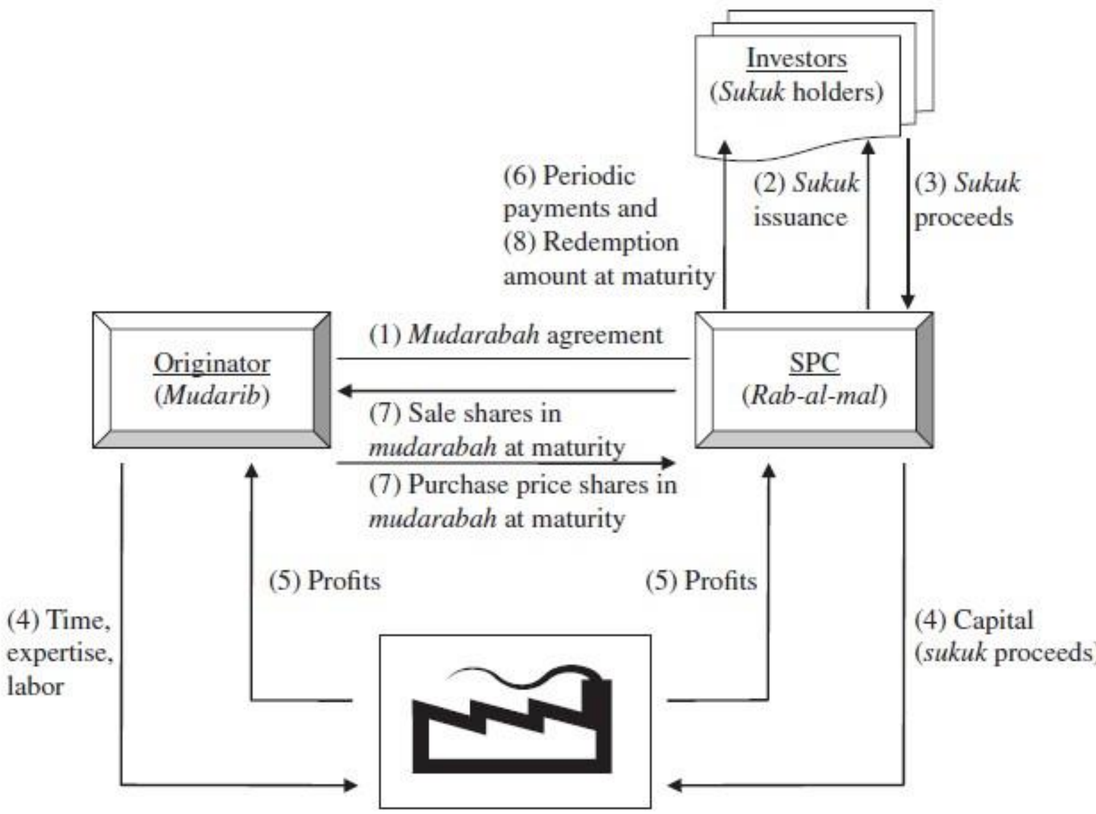
There are mainly six types of Sukuk securities. They are differentiated by the various types of agreement that were explained above which comply with Islamic principles and beliefs. These are; Mudarabah, Musharakah, Murabah, Ijarah, Salam and Istista. All these forms of Sukuk are directly related to the explanations made previously of these contracts that are used in the Islamic society, with the only difference that, in this case, its form of contracting is applied to Sukuk.

1.3.3.1. Sukuk Mudarabah

This form of Sukuk is structured on the basis of the Mudarabah contract, which, as explained in a previous section, is a form of partnership in which one party provides the capital (Rab ul Mall) and the other personal effort and time (Mudarib). Within this structure, everything begins with the financing requirement on the part of the originator or Mudarib as it will then provide its effort and time. The originator creates a Special Purpose-Company (SPC) and establishes a Mudarabah contract with this SPC. In this case, the originator and the SPC are the partners within the contract where the originator acts as the managing partner. As a managing partner, the Mudarib provides its personal effort and time while the SPC acts as the silent partner that provides the financial investment; in other words, it would be the Rab ul Mall of the contract.

Subsequently, the SPC issues certificates (Sukuk) to investors or holders of Sukuk and the sum obtained by this issuance is used as the capital contribution that is invested in assets that provide certain performance. The originator provides his / her time, expertise and work in those assets. Thus, the yield that these assets will provide will be distributed proportionally between the originator and the SPC. The SPC is responsible for directing such income, on a proportional basis, to the holders of Sukuk according to a previously agreed margin. In this way, the SPC makes periodical payments to the holders of Sukuk until the certificate reaches maturity and the corresponding refund must be made. It is worth mentioning that before making such repayment, the SPC sells its share of the assets to the originator upon reaching the maturity of the contract.

Graphic 3: Sukuk Mudarabah functioning



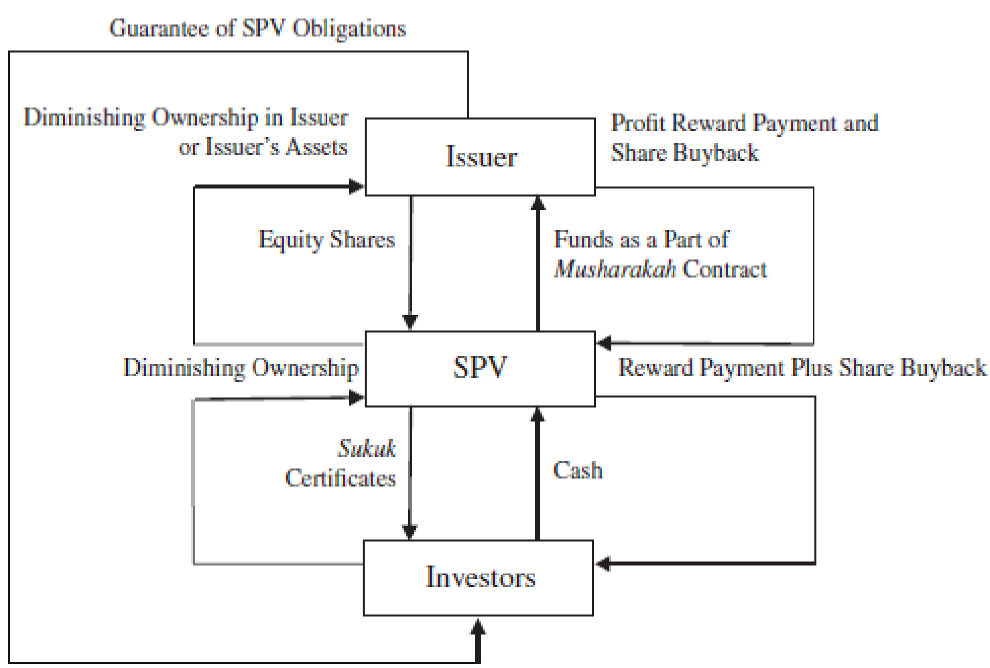
Source: Ariff, Safari, & Mohamad, 2014

1.3.3.2. Sukuk Musharakah

What essentially differentiates this type of contract is that two or more parties are free to contribute either their capital or labor. This type of capital financing agreement requires that the percentages of profit and the duration of that partnership are to be agreed in advance. Similarly, if there are losses, they will be shared according to the proportion of the capital contributed, unless negligence is proven by one of the parties.

There are a variety of forms of Sukuk emission based on this kind of contract, however, the so-called diminishing Musharakah is the one that has been most used for the last few years. In this case there is a part called the issuer (who in the previous case would be the originator) and another part that would be the investors. Both parties establish an SPC that can administer Sukuk. To make this a Sukuk diminishing Musharakah, the issuer must transfer ownership of an asset to the SPC in order to initiate the partnership agreement between the parties. On the other hand, investors enter into the agreement by means of a cash supply. In this way, this partnership is formed, making both parties owners of the SPC. However, the percentage of ownership of investors is decreasing periodically as the issuer pays fees from time to time to investors in order to repurchase the respective shares of the asset. These quotas plus the income generated by the asset constitute the cash flow of the holders of Sukuk (investors).

Graphic 4: Sukuk Musharakah functioning



Source: Ariff, Safari, & Mohamad, 2014
Elaboration: Marmolejo, Mateo y Suárez, José.

1.3.3.3. Sukuk Murabaha

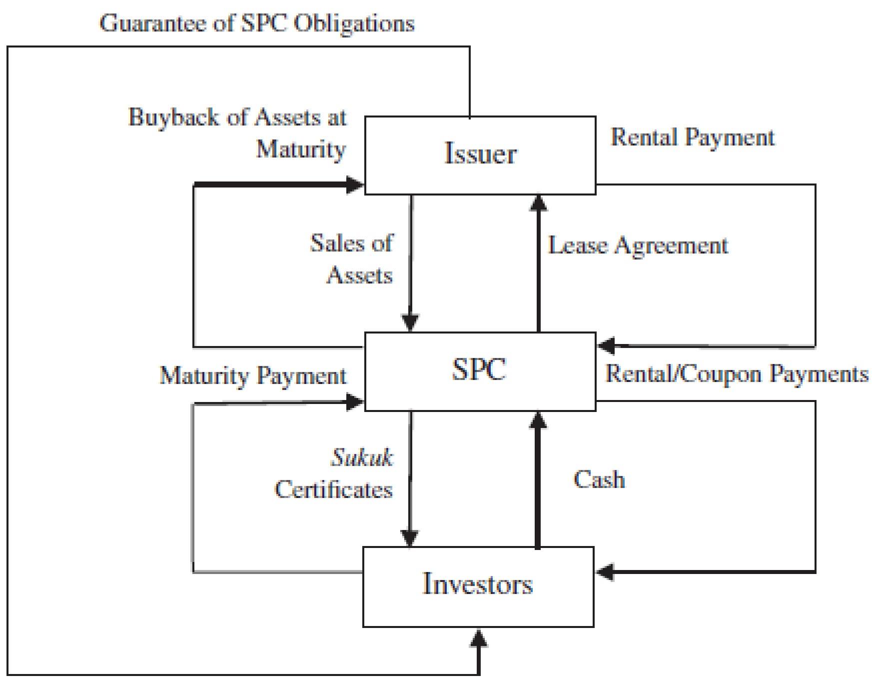
Murabaha contracts cover the process of buying, acquiring or importing a good by one of the parties (mainly an Islamic bank) and then reselling those goods elsewhere. The additional amount at the original cost constitutes the profit margin for the first part (Islamic bank). These types of contracts are mainly used in international trade and working capital financing in circumstances where the bank purchases raw materials, goods or equipment to sell to its client. An important point is that under this contract the asset is held by the bank until the payments have been completed.

In the case of Sukuk Murabaha, an SPC is established between the parties. The SPC may use the capital raised from the investors, who become holders of the issued Sukuk, to buy an asset and then sell it to the other party who is obligated to buy it at a price that includes the original cost plus a previously agreed profit. The buyer makes deferred payments to investors. This transaction is done through the SPC.

1.3.3.4. Sukuk Ijarah

Ijarah is the reward or income that comes from a lease between two parties in which the lessor (owner of an asset) leases the asset to a lessee (user of the asset). In order to issue Sukuk Ijarah, the originator (who first owns the assets) sells the assets to an SPC, which is typically constituted in an offshore tax haven. The SPC leases the assets back to the issuer at a previously agreed rental price, and then the SPC securitizes the ownership of those assets through issuance of Sukuk certificates for investors to acquire. These Sukuk certificates represent a portion of the ownership over the assets, which allows the holders of the certificates to receive a portion of the income payments for the underlying assets. Because these certificates represent ownership over real assets, they can be traded on the secondary market. The role of the SPC in driving Ijarah Sukuk is practically cash flow management, particularly by receiving periodic rents and fees from the originator and then being distributed to Sukuk holders. The SPC finishes its roll the moment in which the certificates reach their maturity.

Graphic 5: Sukuk Ijarah functioning



Source: Ariff, Safari, & Mohamad, 2014

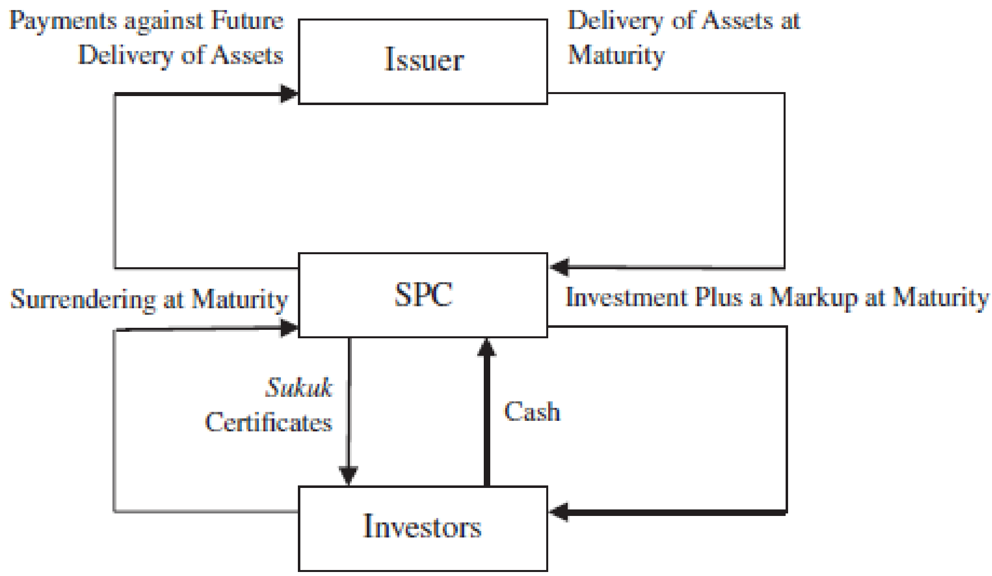
Elaboration: Marmolejo, Mateo y Suárez, José.

1.3.3.5. Sukuk Salam

Salam refers to a transaction in which the seller promises to grant a specific asset or raw material to the buyer at a future date in exchange for a prepayment of the price of the same asset. The payment must be for the total amount.

In order to issue Sukuk Salam, a non-profit SPC must be constituted as a separate legal entity for the duration of Sukuk so that it can manage the flow of payments between the issuer and the investors, as well, to maintain the title of the underlying assets. To begin, the issuer transfers the ownership title of the assets to the SPC, which consequently issues participation certificates for these to be acquired by investors. The Sukuk Salam represents an indivisible right over a part of the asset. In order to acquire a certificate, the investor must make a pre-payment, which gives the right to a future refund of the investment plus a previously agreed fixed margin.

Graphic 6: Sukuk Salam functioning



Source: Ariff, Safari, & Mohamad, 2014

1.3.3.6. Sukuk Istisna

Istisna being a contract that commissions the manufacture of the product, is the appropriate method to finance working capital in the manufacturing and construction sector (Ariff, Safari, & Mohamad, 2014). This allows a party to obtain industrial goods either with advanced cash payment and deferred delivery or deferred payment and delivery.

Sukuk Istisna has also become the contractual form to finance construction projects. In order to issue this type of Sukuk, a parallel Istisna contract must be created between the financier and the person who subcontracts the project. The project commissioner provides technical, financial and administrative specifications to the financier, who must then find the best subcontractor for project execution. The information required in the offer includes a proposal to sell the completed parts of the project over time and the amount of the expected payments. This revenue stream, which is based on the proceeds of the scheduled installments for a given period, can be used to issue the certificates.

This term refers to a type of sale contract in which the buyer asks the seller for the manufacture of a specific product. In most cases, the seller's raw material is used and a price is agreed beforehand. However, it may be previously agreed that the seller will also supply the raw material or only the labor. However, as these certificates are not based on an existing tangible asset at the time it is celebrated and are only representing a debt obligation, they cannot be traded on the secondary market at a discount. Sukuk Istisna may only be exchanged for its nominal value or used to buy goods or services whose price is equal to the nominal value of the certificate.

As mentioned above, the owner of the capital pays in advance for a project that will be completed in the future. The owner of the capital (Sukuk holders) benefits from the difference between the amount paid in advance and the market price at which the project counts as it expires. The promised payment at maturity is not previously agreed during the issuance period.

1.3.3.7. Sukuk Wakalah

The Wakalah Sukuk is based on the Islamic Wakalah contract. This is an agency agreement and consists of one party giving power to another party to act on its behalf. The investor appoints a (wakeed) agent to invest a certain amount of money on his behalf in a set of assets evidently compatible with Sharia'a. This type of Sukuk has been used with more frequency over the past few years among large financial institutions.

The contract between the investor and his agent is a Sukuk Wakalah. The investor pays a fixed amount to his agent for the administration of his funds and the agent is in charge of investing in projects and a series of Islamic assets that possibly generate a return. The agent cannot offer or guarantee a definite return to the investor. If there are profits, these are delivered directly to the investor since the agent already received a fixed payment for their services, knowledge and time.

1.4. Conclusions

After analyzing this first section, it can be conclude that the Sukuk financial instruments have their origin in the Islamic custom and in the appearance of the money in the economy. Sukuk certificates originate along with the birth of money as a means of exchange. The emergence of money impacts trade relations and creates a new need in Islamic economies.

Specifically, a method is required that facilitates the flow of money between those who demand financing and those who have savings. In this way, Sukuk certificates are born, which in turn embrace the common values and principles of Islam, such as the absence of a money price or interest payment and the application of the Islamic principle of shared risk. It is observed that the charging of interest on capital, simply by transferring it, is totally prohibited and constitutes the fundamental basis of all Islamic economic practice.

Then, it has been seen that the money can be exchanged for the same amount of money, and its face value cannot be modified. Therefore, it is stressed that money has no value over time in Islamic economies. The true value of money in these cases lies in the ability to generate value thanks to the time, effort or knowledge used at the moment of putting that capital to work. In this way, it is possible to generate benefits for the lenders or investors as well as for the borrowers, as long as the Islamic processes are fulfilled. It has been shown that in order to transfer funds, it is necessary to conclude a contract establishing the obligations and rights of each party, in which one party usually provides capital and the other time, knowledge or effort. In any Islamic contract, both parties contribute something and both sides assume the risks involved in the cooperation. Both profits and losses are distributed proportionally between the parties.

Sukuk financial instruments are the most common form of association in contracts involving large amounts of money and are considered a unique instrument of Islam. However, it has been seen that the development of Sukuk would not be possible without a legal infrastructure and a financial system to facilitate its use.

As regards to the legal framework, this chapter has identified that in Islamic economies there is a strict regulation that controls and encourages financial transactions. Primarily, the commercial laws deriving from Sharia'a and other sources of Islamic law such as the Qur'an, Sunnah, Ijma and Qiyas.

It has been shown that there are definite ways of doing business that are compatible with the principles of Islam and that there are institutions called Sharia'a supervision directories that verify the legality of contracts. Among the most commonly used standard contracts, it has was identified the contract Murabaha, Mudarabah, Musharaka, Ijara, Istisna'a, Salam, Takaful and Wakalah.

It is striking to see that there is a type of contract compatible with Islamic law for almost any type of commercial transaction carried out in non-Islamic economies, this includes the Islamic version of buying and selling goods, forms of trade association, insurance, mutual funds, usufruct, leasing, deferred payments, asset management, and futures, among others. In turn, Sukuk certificates adopt the principles of accepted contracts. It is noted that even for Sukuk instruments, different structures of Islamic contracts apply. For example, a Sukuk of the Murabaha type and a Sukuk of the Wakalah type have substantial differences. While in the first, one part provides the capital and the other a part of what the assets produce. In the second, funds are given in exchange for the administration of them. In conclusion, each Sukuk has its own structure and clearly establishes the obligations of each party and the risks they share.

With regard to the Islamic financial system, it can be concluded that it has developed mainly in Malaysia, Bahrain, the United Arab Emirates, Oman, Saudi Arabia, Pakistan, Kuwait, Jordan, Qatar and Indonesia. The IFS has been strengthened with the emergence of more Islamic financial institutions, directories of Sharia`a supervision, with more information available and greater regulation. Thus, the formalization of the IFS in these areas has been fundamental for the development of a Sukuk market. Lastly, the importance of the short-term and long-term Sukuk market for the Islamic financial system is highlighted, as it represents approximately 15% of the assets of the entire system. The growth of the Sukuk market and the formalization of the financial system along with financial globalization, have driven the commercialization of these instruments significantly in the Islamic financial market and the international financial markets since 2001.

The following chapter describes in more detail the development of Sukuk, its classification and the main actors of this market.

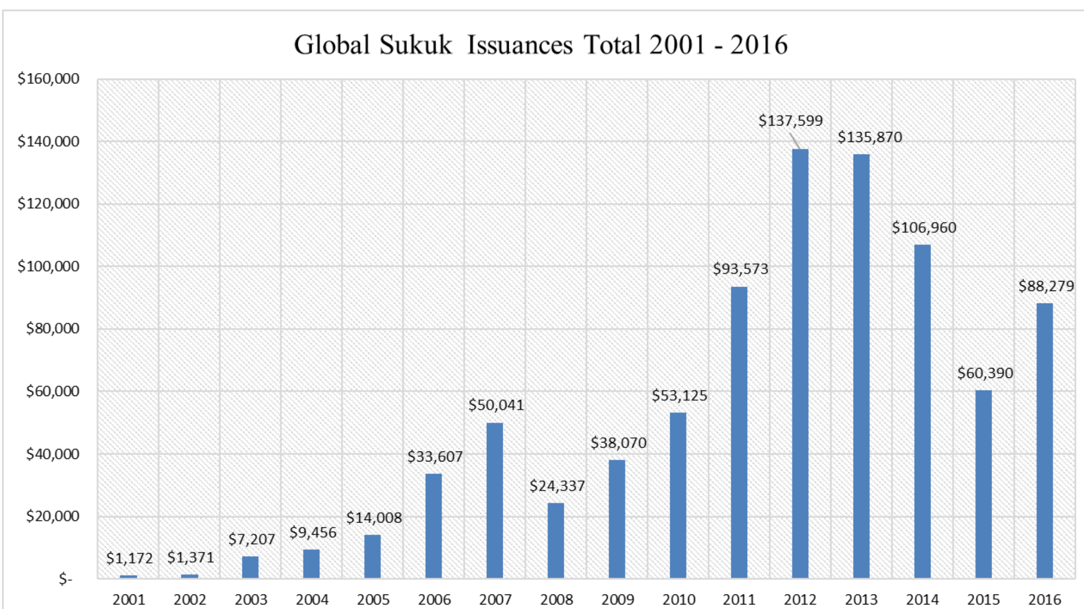
CHAPTER II:

SUKUK MARKET DEVELOPMENT AND ITS CHARACTERISTICS

2.1. Global Sukuk development: Introduction

In 2001 the Sukuk market began to be formalized, since then the issuance of these instruments has increased significantly. Sukuk emissions reached their historic maximum in 2012 and 2013 (IIFM, 2016). In 2014 the Sukuk market entered into a stage that specialists like to call the consolidation phase, in which external conditions such as falling oil prices, uncertainty in the international financial market and political decisions taken by main Sukuk issuers have, in a certain way, slowed down the growth of issuance volume of this kind of securities. However, these events are considered normal and there is confidence that Sukuk's global market is promising due to the increasing number of new issuers and the interest in this market continues to grow.

Graphic 7: Global Sukuk issuances total 2001-2016, USD millions



Source: IIFM Sukuk Report 2016 5th edition.
Elaboration: Marmolejo, Mateo y Suárez, José.

The previous graph demonstrates that in 2001 the total of Sukuk emissions reached USD 1.17 billion. The volume of emissions (USD) increased until reaching a historical maximum in 2012 with a value of USD 137.59 billion. In 2014 there was a 21.27% drop in the issued securities compared to 2013, and subsequently, 2015 emissions fell an additional 43.54%, which makes 2015 the worst year since 2011. However, if 2015 is compared with the years before 2010, 2015 demonstrates a higher emission volume. In 2016, the total issuance increased 46.18%, exceeding the previous year and reaching USD 88.27 billion. The annual geometric growth rate of Sukuk emissions is 33.4% from 2001 to 2016. In the 2010-2016 period, the average annual geometric growth is 12.77%. In conclusion, this demonstrates that the amounts issued from these financial instruments have increased since the first registrations made in 2001.

2.2. Emissions classification

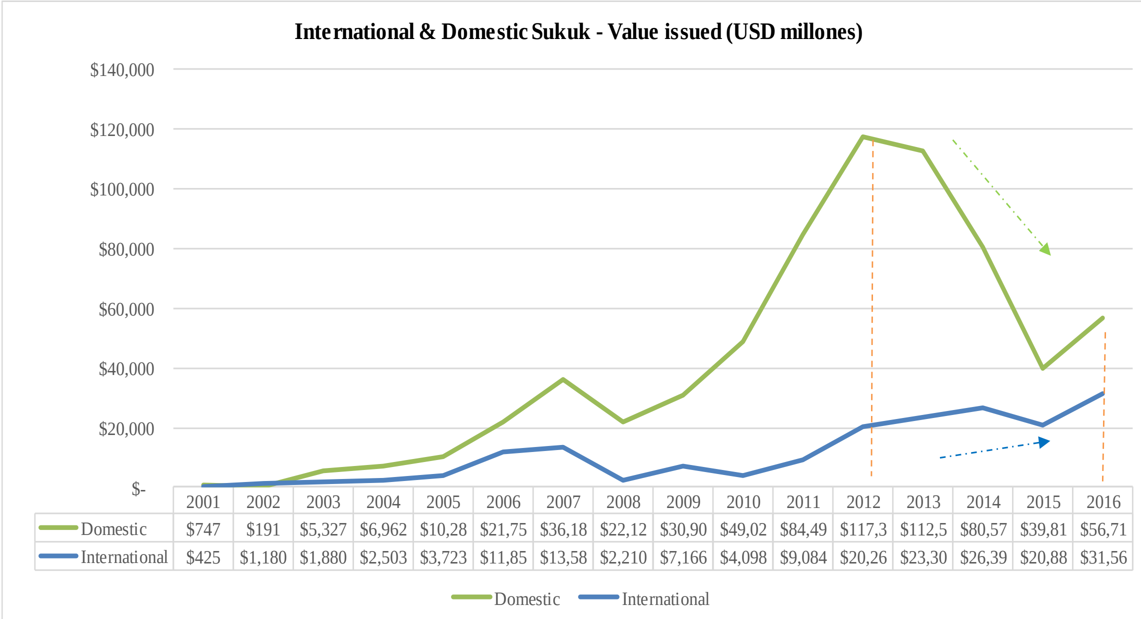
This section analyzes how Sukuk emissions are classified, this classification is based on three categories: by place of issuance, whether domestic or international; by issuance denomination, in other words the currency in which they were structured; and finally, by the issuers' nature, which can be corporate, sovereign, or quasi-sovereign.

2.2.1. Volume of domestic vs international issuances

The international category refers to Sukuk emissions made in a jurisdiction other than the legal domicile of the issuing entity. For example, a Qatar company incorporated in that country registers a Sukuk issuance in any country other than Qatar. On the other hand, a domestic issuance occurs when the instruments are issued in the same country of the entity that registers it. For example, the government of the Arab Emirates registers an issuance on the Dubai stock exchange.

The following graphic shows the annual volume of Sukuk, domestic and international, in millions of dollars. It can be seen that domestic emissions are predominant. However, it is interesting to note that international emissions reached their minimum in 2008, and then remained close to USD 20 billion since 2012 regardless of the decrease in domestic emissions during those years.

Graphic 8: International and Domestic Sukuk – USD millions



Source: IIFM Sukuk Report 2016 5th edition.
Elaboration: Marmolejo, Mateo y Suárez, José.

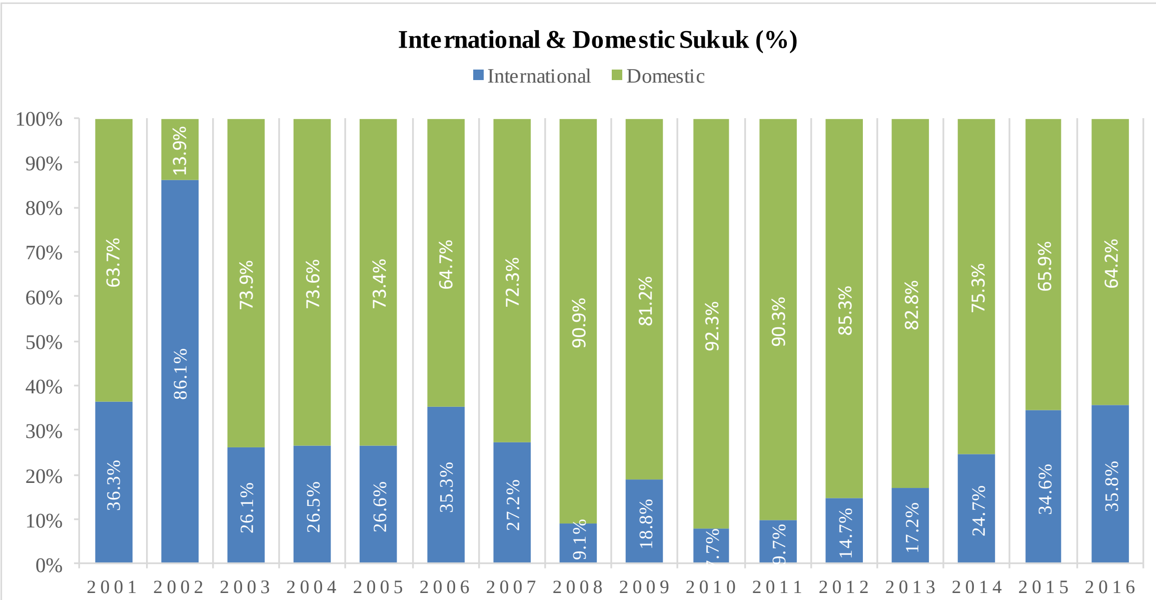
The IIFM (International Islamic Financial Market), is an agency in charge of establishing international standards for the Islamic financial industry. According to the IIFM, the decrease in domestic emissions in 2012 is due to the political decision of the Central Bank of Malaysia to cease its Sukuk emissions with a maturity of less than one year. Given the importance of Malaysia in this financial system, it can be seen that a decision of that country has a significant impact on the Sukuk domestic market. However, analysts argue that if Malaysia is excluded from total domestic emissions, these actually show an increase (IIFM, 2016). Meanwhile, international emissions represent a smaller portion than domestic emissions, however, international emissions are less volatile. The change experienced in 2012 in the domestic part did not affect the international component. On the contrary, the latter has increased since 2012 in an average of 36% per year.

The following graphic shows the percentage of international (Euromarket[1]) and domestic emissions since 2001. On average, international emissions constitute 27% of the total,

[1] Euromarket is a term used to refer to a fixed-income market in which securities are issued or loans are granted in currencies other than those of the issuing country. (Saunier & Iriye, 2017).

while domestic emissions complete the remaining 73%. It is interesting to note that in relative terms in 2008 and 2011, international emissions reached their minimum levels. According to Thompson Reuters, this is explained by the instability and uncertainty of the international financial markets in the mentioned years.

Graphic 9: International and Domestic Sukuk – by percentage



Source: IIFM Sukuk Report 2016 5th edition.
Elaboration: Marmolejo, Mateo y Suárez, José.

In any case, both relative amounts and the total volume of international issuances experienced an increase. The amount issued in different jurisdictions from those of the issuer reaches its historical maximum in 2016, which indicates that there is greater confidence in international markets compared to previous years.

2.2.2. Emissions by currency

The Malaysian Ringgit, the US Dollar, the Saudi Riyal and the Indonesian Rupee are the four most important currencies in the Sukuk market. From 2001 to 2016, 62% of the issuances have been structured in the Malaysian currency (MYR) while the dollar (USD) covers 20%. These two currencies are the most dominant. There are 20 additional currencies of smaller volumes. These have been grouped into categories based on a geographical criteria to facilitate its comparison (see the following table).

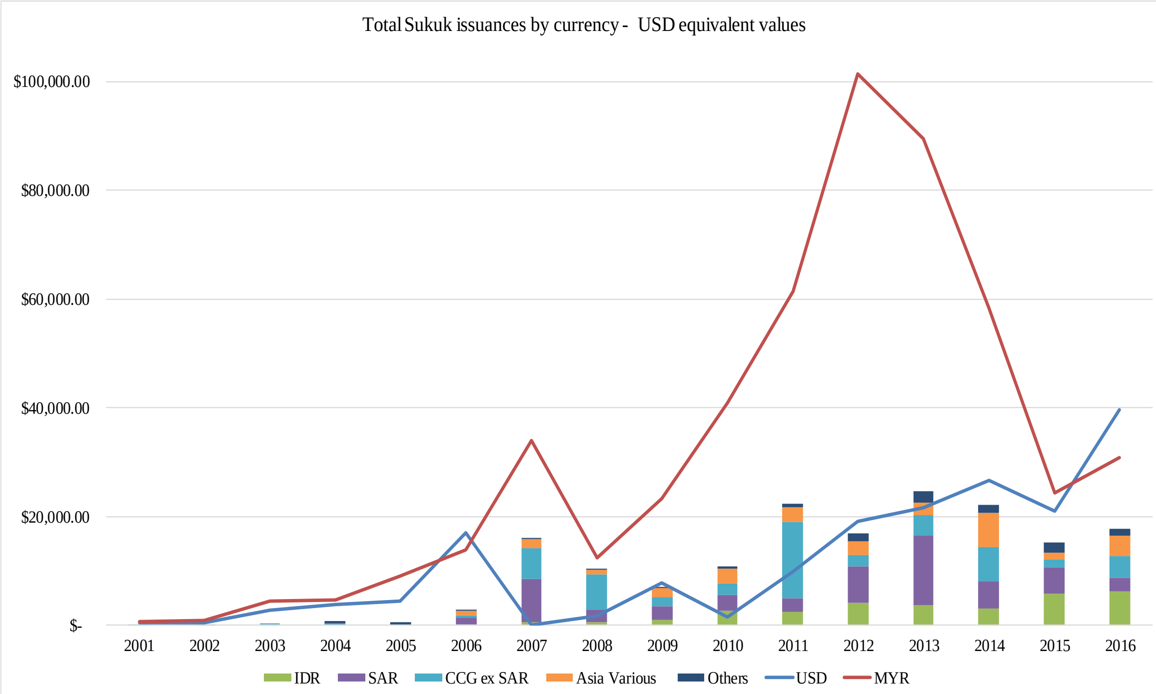
Table 4: Sukuk emissions by currency and groups of currencies 2001-2016

FX Quote	Currency	Country	Volume USD Millions 2001-2016		%
Independientes			**$**	**767,389.84**	**89.75%**
MYR	Ringgit	Malaysia	$	527,305.62	61.67%
USD	US Dollar	United States	$	175,356.95	20.51%
SAR	Saudi Rial	Saudi Arabia	$	38,926.33	4.55%
IDR	Indonesian Rupiah	Indonesia	$	25,800.95	3.02%
C.C. Golfo (Excluye SAR)			**$**	**39,642.13**	**4.64%**
QAR	Qatari Riyal	Qatar	$	15,170.97	1.77%
BHD	Bahrain Dinar	Bahrein	$	14,079.64	1.65%
AED	Dirham	United Arab Emirats	$	9,160.31	1.07%
OMR	Oman Riyal	Oman	$	862.63	0.10%
KWD	Kuwaiti Dinar	Kuwait	$	368.59	0.04%
Varios Asia (Excluye MYR e IDR)			**$**	**22,349.39**	**2.61%**
PKR	Pakistani Rupee	Pakistan	$	9,474.39	1.11%
BND	Brunei Dollar	Brunei	$	9,462.51	1.11%
SGD	Singapore Dollar	Singapore	$	3,128.42	0.37%
CNY	Chinesse Yuan	China	$	280.51	0.03%
MVR	Maldivian Rufiyaa	Maldives	$	3.57	0.0004%
Las demás			**$**	**25,683.63**	**3.00%**
SDG	Sudanese Pound	Sudan	$	17,162.73	2.01%
			$	-	
TRY	Turkish Lira	Turkey	$	5,785.26	0.68%
EUR	Euro	European Union	$	837.98	0.10%
GBP	British Pound	United Kingdom	$	737.21	0.09%
CFA Francs	African Franco	African Community	$	441.27	0.05%
YER	Yemeni Riyal	Yemen	$	268.37	0.03%
GMD	Gambian Dalasi	Gambia	$	144.26	0.02%
NGN	Nigerian Naira	Nigeria	$	141.08	0.02%
JOD	Jordanian Dinar	Jordan	$	126.23	0.01%
BDT	Bengali Taka	Bangladesh	$	39.25	0.005%
TOTAL			**$**	**855,065.00**	

Source: IIFM Sukuk Report 2016 5th edition, 2014 4th edition, 2013 3rd edition, 2011 2nd edition y Thompson Reuters: Sukuk Perceptions 2016.
Elaboration: Marmolejo, Mateo y Suárez, José.

After observing the total amounts of each currency, the following graphic shows the volume issued year by year by each country in its US dollar equivalent.

Graphic 10: Sukuk emissions by currency – USD equivalent values (millions)



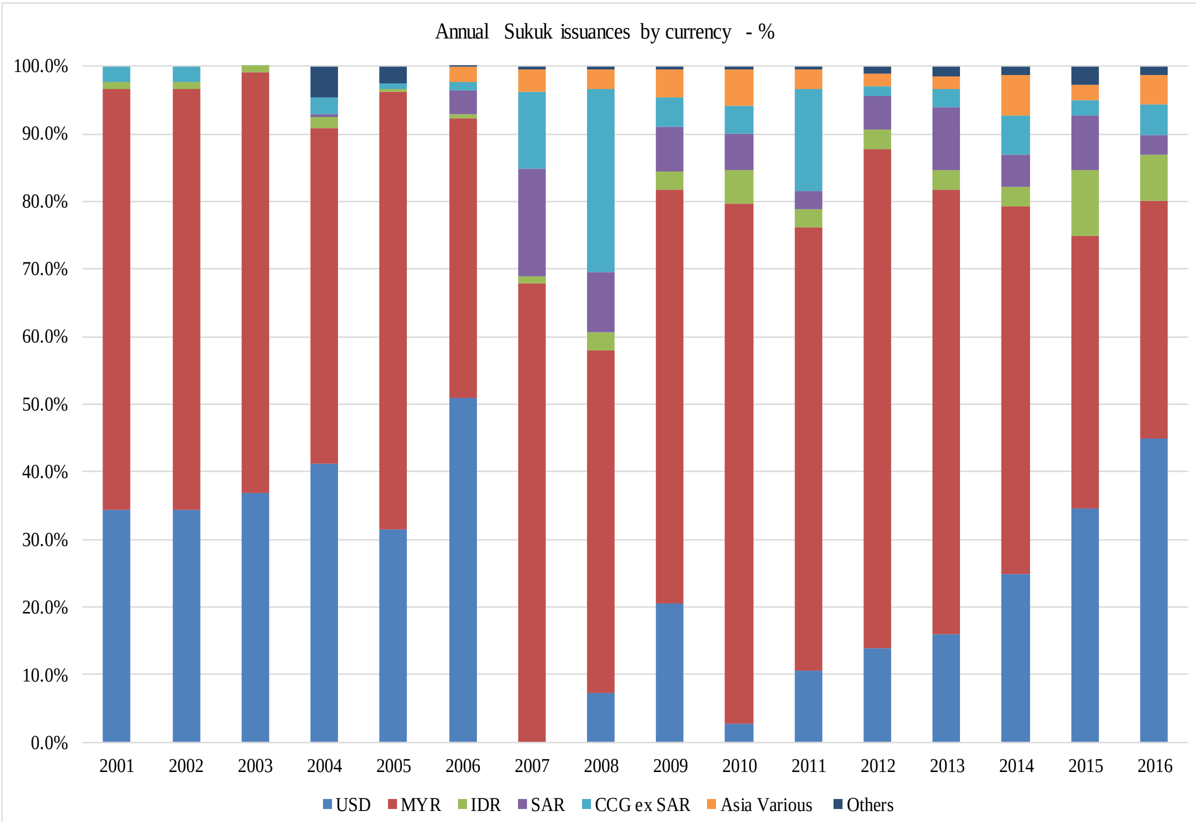
Source: IIFM Sukuk Report 2016 5th edition, 2014 4th edition, 2013 3rd edition, 2011 2nd edition y Thompson Reuters: Sukuk Perceptions 2016.
Elaboration: Marmolejo, Mateo y Suárez, José.

In figure 10 the two dominant currencies MYR and USD are represented by lines, while less representative currencies are stacked in columns. Issuances in MYR reached their maximum in 2012. Consequently in 2013, as a result of the decision of the Central Bank of Malaysia to stop issuing Sukuk in the short term, emissions in MYR are considerably reduced. The volume of securities issued in USD increases since 2010, while the rest of issuances in other currencies are more volatile. For example, in 2008, the volume of issuances in currencies from Arab Gulf countries represent 28% of the total, and is the largest part in the block of less representative currencies. However, in 2015 its participation is reduced to 2.5%

The following two graphics show the increase in USD emissions, comparing it to the rest of currencies analyzed in annual relative terms. From 2008, the Sukuk structured in USD have been gaining ground while the structuring in MYR have decreased.

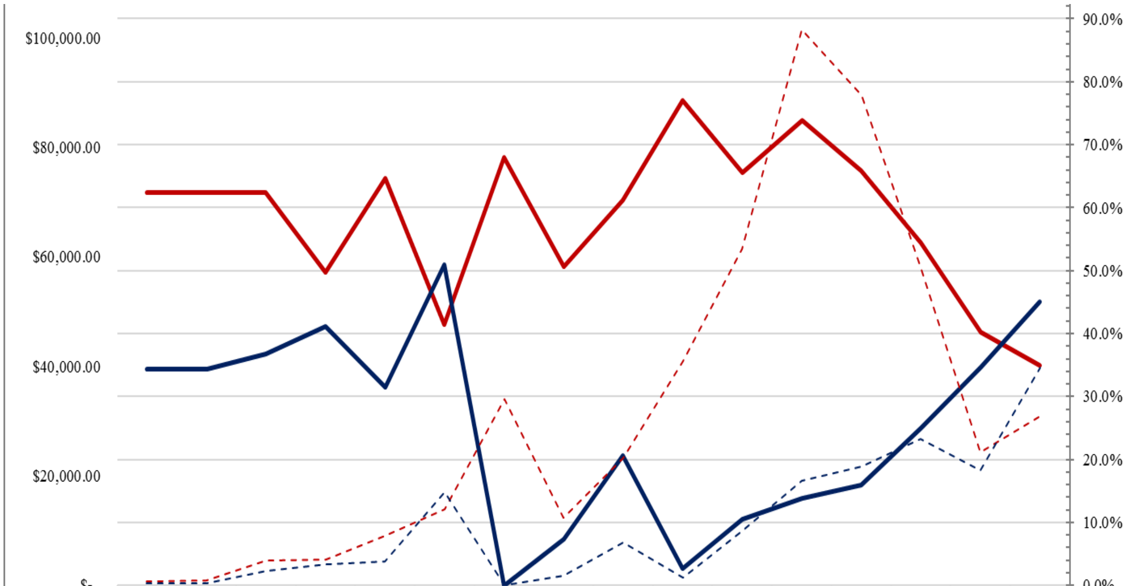
While in 2012 the MYR represented more than 73% of the emissions and the USD 13.8%, for 2016 only 35% of the emissions were denominated in MYR and 45% of the issued securities were denominated in USD.

Graphic 11: Total annual Sukuk emissions by currency – percentages (%)



Source: IIFM Sukuk Reports 2016, 2014, 2013, 2011 y Thompson Reuters: Sukuk Perceptions 2016.
Elaboration: Marmolejo, Mateo y Suárez, José.

Graphic 12: Comparison of issuances structured in USD and MYR 2001 - 2016



	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
MYR	62.4%	62.4%	62.4%	49.7%	64.7%	41.5%	68.0%	50.6%	61.2%	77.1%	65.6%	73.8%	65.9%	54.4%	40.3%	35.0%
USD	34.4%	34.4%	36.8%	41.2%	31.4%	50.9%	0.0%	7.3%	20.6%	2.7%	10.6%	13.8%	15.9%	25.0%	34.7%	45.0%
MYR	$731.1	$855.3	$4,496	$4,700	$9,066	$13,93	$34,01	$12,32	$23,30	$40,94	$61,41	$101,5	$89,52	$58,20	$24,31	$30,89
USD	$402.7	$471.0	$2,650	$3,895	$4,404	$17,09	$-	$1,786	$7,842	$1,417	$9,911	$19,05	$21,64	$26,70	$20,95	$39,72

Source: IIFM Sukuk Reports 2016, 2014, 2013, 2011 y Thompson Reuters: Sukuk Perceptions 2016.
Elaboration: Marmolejo, Mateo y Suárez, José.

Once again it can be verified the increase of the USD emissions and the decrease of the MYR. In 2016, for the first time in 10 years issuances in USD have exceeded issuances in MYR.

2.2.3. Nature of the issuer: Corporate/Sovereign/Quasi Sovereign issuance

Usually the fixed income markets are classified by the type of issuer, where three basic sectors can be identified. The government sector (sovereign issuances), the sector related to the government (quasi-sovereign issuances) and the private sector (corporate issuances).

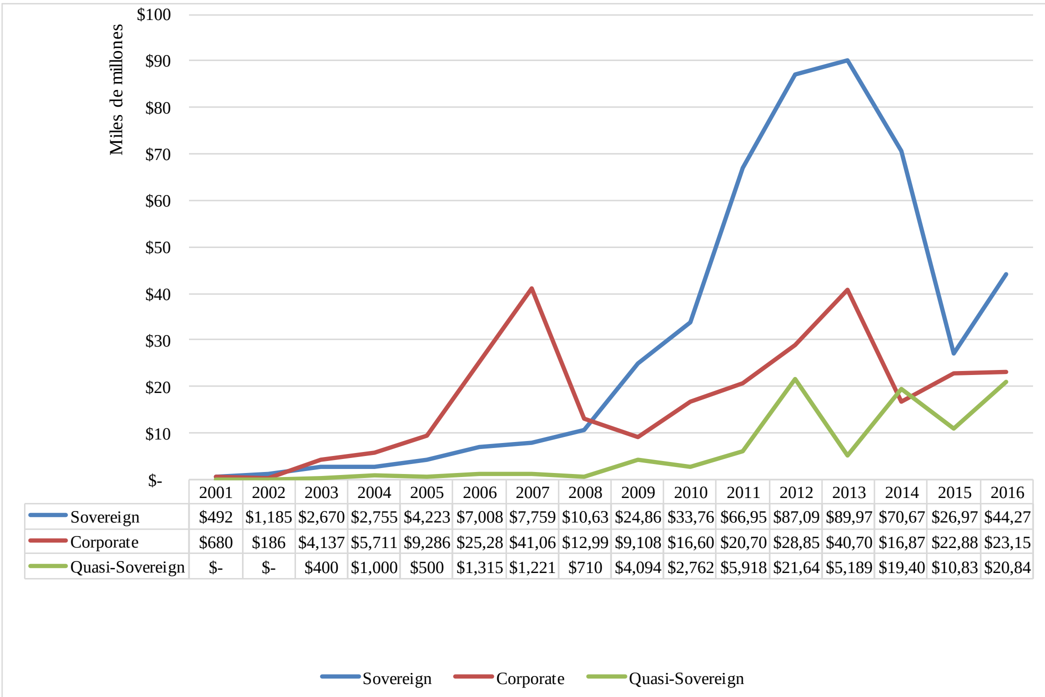
Sovereign Sukuk: These are Sukuk titles issued by a national government, usually in their local currency. They constitute an agreement or direct link with that government.

Quasi-Sovereign Sukuk: The Sukuk correspondent to this group are the ones from sectors related to one or more national governments that do not constitute an agreement or direct link with a particular government. For example, the Sukuk issued by a supranational or international body such as the World Bank or the Islamic Development Bank. Both Sukuk issuers have a certain relation to national governments without constituting direct obligation to a government.

Corporate Sukuk: These are Sukuk securities issued by entities that are not part of a government and belong to the private sector (CFA Institute, 2017).

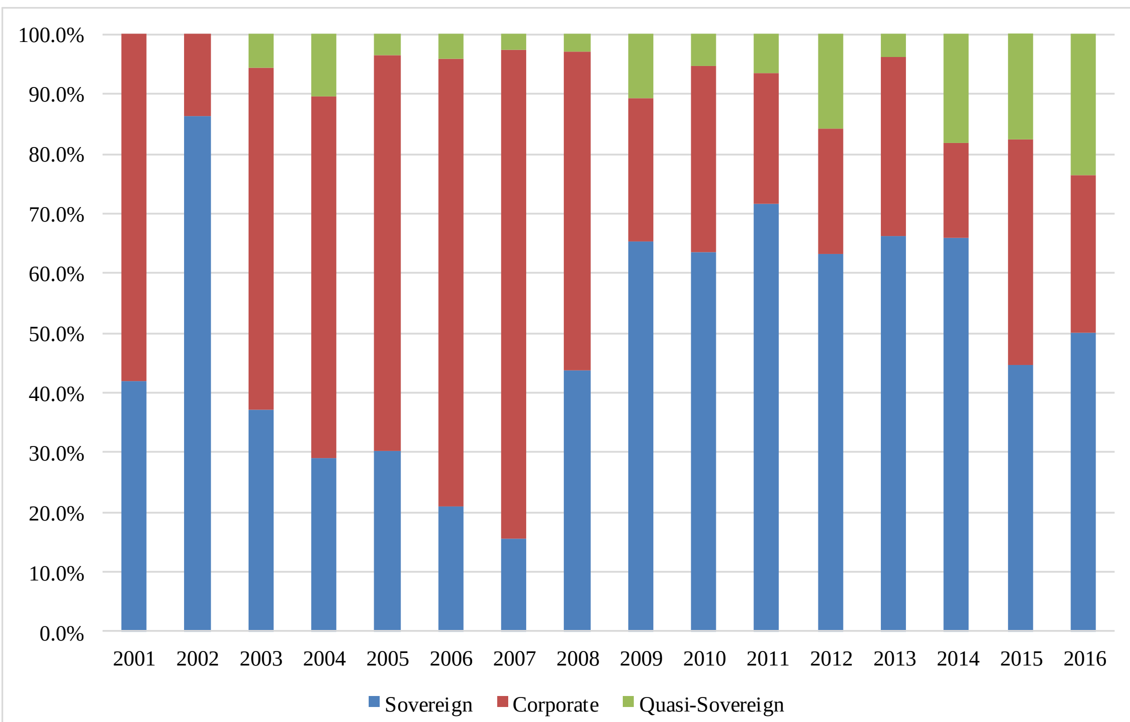
Graphic 13 demonstrates that until 2008 the corporate issuances exceeded the other two categories. Since 2009, sovereign emissions have been higher, driven by the issuance programs of Malaysia, the Arab Emirates, Saudi Arabia and Indonesia (IIFM, 2016). Sovereign issuances peaked at USD 90 billion in 2013 and subsequently declined due to the discontinuation of sovereign issuance programs from Malaysia and a group of Arab Gulf countries. On the other hand, corporate issues are now the second largest component and reached their maximum of USD 40 billion in 2007 and 2013. Finally, quasi-sovereign issues began to develop with greater force since 2008, and in 2014 exceeded corporate emissions. This is mainly due to the World Bank issuing a series of Sukuk in the international market to obtain financing.

Graphic 13: Sukuk volume by type of issuer 2001 - 2016



	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
Sovereign	$492	$1,185	$2,670	$2,755	$4,223	$7,008	$7,759	$10,63	$24,86	$33,76	$66,95	$87,09	$89,97	$70,67	$26,97	$44,27
Corporate	$680	$186	$4,137	$5,711	$9,286	$25,28	$41,06	$12,99	$9,108	$16,60	$20,70	$28,85	$40,70	$16,87	$22,88	$23,15
Quasi-Sovereign	$-	$-	$400	$1,000	$500	$1,315	$1,221	$710	$4,094	$2,762	$5,918	$21,64	$5,189	$19,40	$10,83	$20,84

Graphic 14: Sukuk annual share by type of issuer 2001 - 2016



Source: IIFM Sukuk Report 1st – 5th edition y Thompson Reuters: Sukuk Perceptions.
Elaboration: Marmolejo, Mateo y Suárez, José,

The previous illustration shows the relative amounts of emissions from each type of issuers year by year. It is observed that since 2008 sovereign issuances have exceeded more than 40% on everything issued in their respective year. On average, corporate issuances represent 30% of the total amount. Emissions that come from the quasi sovereign sector have increased since 2008. The quasi sovereign issuances represented only 4% of the total issued in 2008 and have reached its maximum of 24% in 2016.

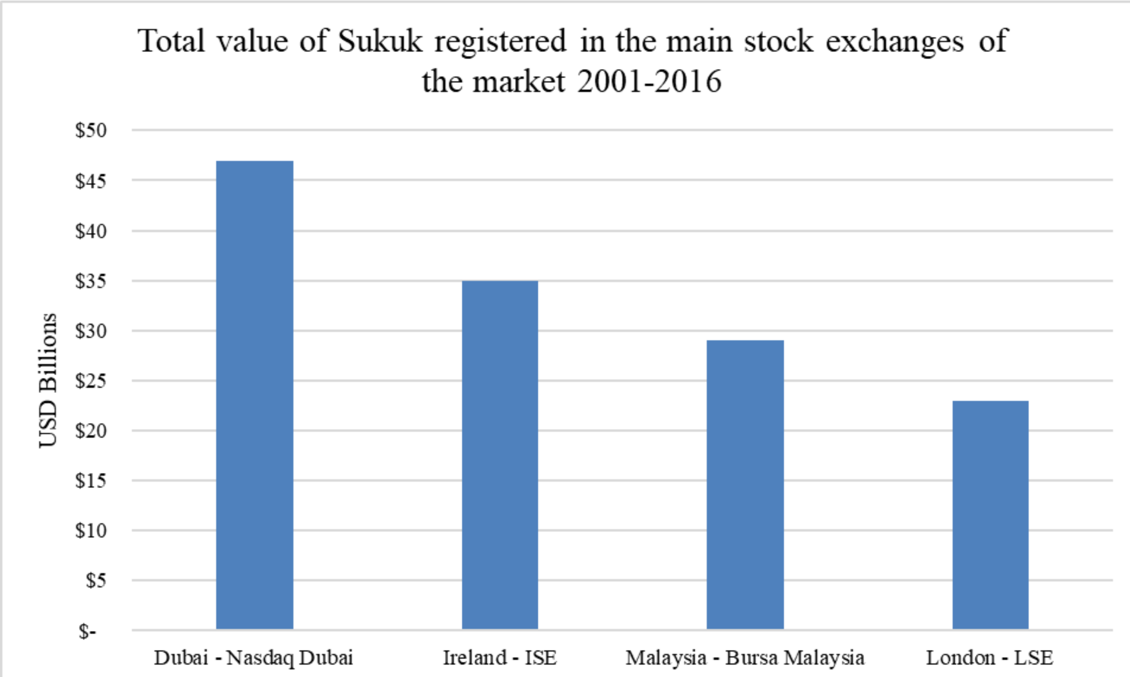
2.3. Main hubs for Sukuk commercialization

Only 30% of Sukuk securities are listed on a stock exchange to be commercialized. In many cases, the nominal value of these instruments are not large enough to cover the costs that convey registering an issuance in a stock market. Another factor to consider is the maturity, if the term is short the incentive to list it in the stock market is also smaller. A final reason for not doing so is that, until recently, the market in which these securities have been directed has been primarily domestic and has been commercialized among institutional investors outside the stock market (IIFM, 2016).

However, as the Sukuk market grows and the number of global participants increases, the willingness of these actors to issue packages of higher nominal value, in the longer term and through stock market listings, can be noted.

There are four main exchange centers that represent a global importance for the Sukuk market. These are the following stock exchanges: Dubai's Nasdaq Dubai, the Irish Stock Exchange in Dublin, the London Stock Exchange in London and Bursa Malaysia in Kuala Lumpur. Since the first Sukuk listing in a stock exchange in 2001, the total value registered in each stock exchange until 2016 can be seen in the following chart.

Graphic 15: Total value of Sukuk registered in the main stock exchanges of the market 2001 - 2016



Source: IIFM Sukuk Report 2017 6th edition.
Elaboration: Marmolejo, Mateo y Suárez, José.

The Malaysian market is the largest Sukuk exchange center, despite the decrease mentioned above due to the decisions taken by the Malaysian government. The institution, World's Islamic Finance Marketplace published an article on January 3 2017, mentioning a solid growth in Sukuk commercialization during 2016 and marks an important recovery of the Malaysian market, being this the leader and principal hub of Islamic bonds commercialization. Malaysia accounts for 46.6% of the total primary market (where newly-issued Sukuk are commercialized), followed by Indonesia with 9.9% and the United Arab Emirates with 9%. In the secondary market (market in which Sukuk that have already been traded more than once are commercialized) Malaysia has 52.6% market share, followed by Saudi Arabia with 16.3% and United Arab Emirates with 8.9%. The aforementioned data refer to the year 2016 (Central Bank of Malaysia, 2017).

In the same way it is worth mentioning that in non-Islamic economies the commercialization and emissions of Sukuk are receiving more acceptance. The United Kingdom, South Africa and Luxembourg can be named as those markets that are beginning to have relevance in the commercialization of Islamic financial instruments (di Mauro, et al., 2013).

2.4. Principal indices (domestic and international)

A financial index must meet certain requirements to be named as an Islamic index. Among these, the companies that make up the index must comply with the principles established by the Sharia'a and the Islamic community, either offering products that are acceptable within this methodology, their business activities, debt levels, how they earn their income and the type of expenses. In order to accomplish a supervision over the compliance of these requirements, the institutions that own the indices establish or submit themselves to an independent Sharia'a Supervisory Committee. The indices that will be described within this section are the most representative for the Sukuk market taking into account emission, commercialization and return levels. These are:

Nasdaq Dubai Sukuk Index is one of the most important indices that measure the overall behavior of Sukuk. This index is developed by Nasdaq Dubai, an international financial exchange center that serves the region between Western Europe and East Asia. It is one of the largest exchange centers in the world for Sukuk listings. Their listings also include stocks, derivatives, conventional bonds, and other financial products. This index has a greater appeal within the domestic market.

On the other hand, Nasdaq Dubai and Ideal Ratings[2] jointly developed an index which some consider the most representative in terms of the global Sukuk commercialization and performance called Nasdaq Dubai Ideal Ratings Global Sukuk Index. This index measures the entire global performance of Sukuk issued in multiple currencies. The index provides price benchmarks which permits regional and international investors to evaluate the performance of their portfolio (Nasdaq Dubai - Ideal Ratings, 2015).

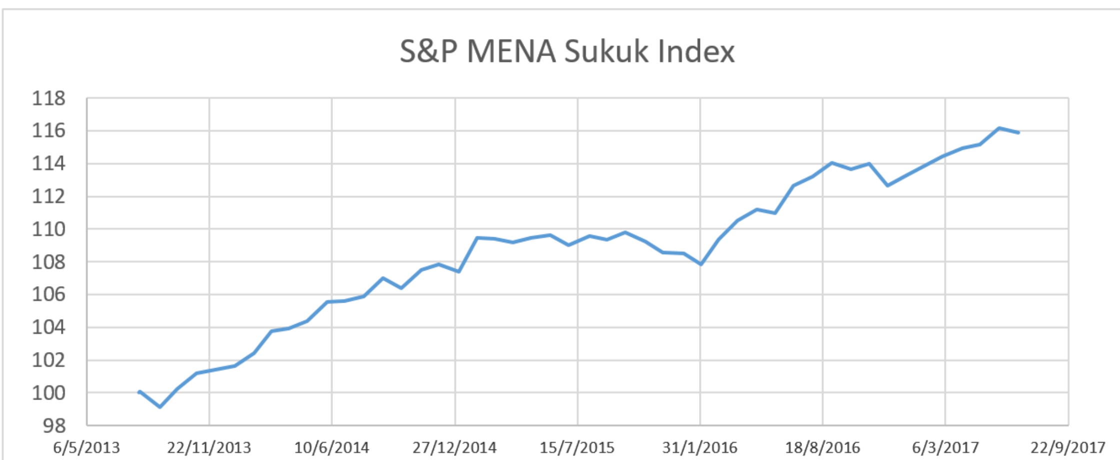
In the same way, there is the S&P Dow Jones Indices organization which is dedicated to develop and offer solutions to the world´s community of investors. It is known as the

[2] Ideal Ratings is a global provider of solutions for databases and investment information. The company calculates indices and provides customized solutions for companies in the capital markets (Ideal Ratings, 2017).

largest source of innovation, information and research in terms of indexes. Its Dow Jones Islamic Market division includes a large list of broad-market indexes, blue-chips, fixed-income (Sukuk), and other strategy and thematic indexes that have passed filters based on rules which validate them as Sharia´a compliant. The Dow Jones Islamic Market Index was launched in 1999 and was the first international Islamic financial index (S&P Global, 2017). Within the same organization there are subdivisions that have a direct focus on the evaluation and recording of Sukuk´s behavior and performance. These sub-indices are: S&P MENA Sukuk index, S&P MENA bond and Sukuk index, Dow Jones Sukuk total return investment grade index, Dow Jones Sukuk higher quality investment grade total return index and Dow Jones Sukuk BBB rated total return index (S&P Dow Jones Indices, 2017).

The following graphics represent the performance shown by some of the sub-indices mentioned in the previous paragraph:

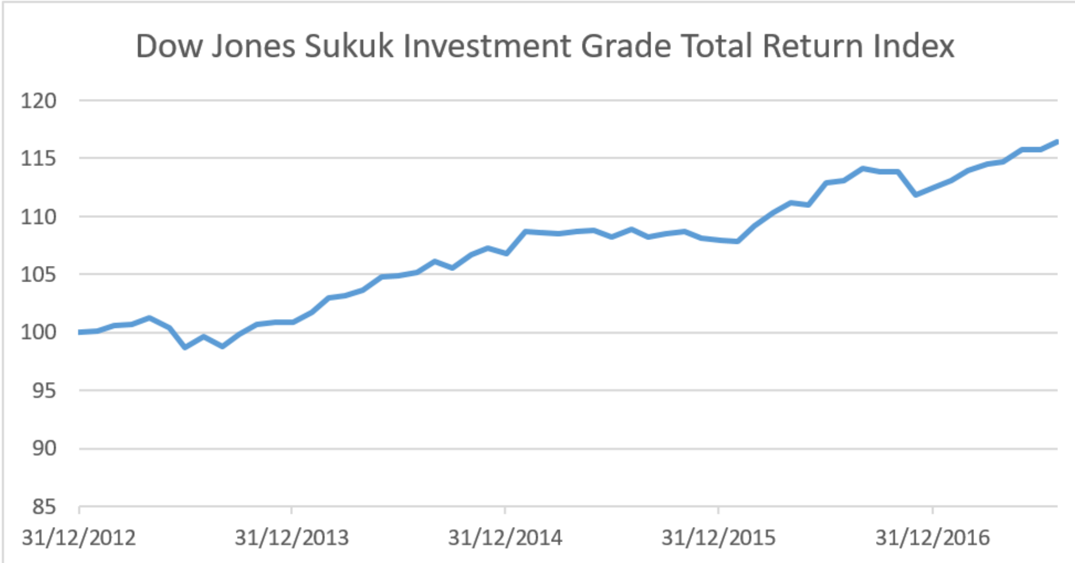
Graphic 16: S&P MENA Sukuk Index



Source: S&P Dow Jones Indices.
Elaboration: Marmolejo, Mateo y Suárez, José.

The S&P MENA Sukuk index provides a Sukuk global exposure. This includes the investment degree that this instrument has had in the African and Middle Eastern markets issued in US dollars.

Graphic 17: Dow Jones Sukuk Investment Grade Total Return Index – DJIGTR



Source: S&P Dow Jones Indices.
Elaboration: Marmolejo, Mateo y Suárez, José.

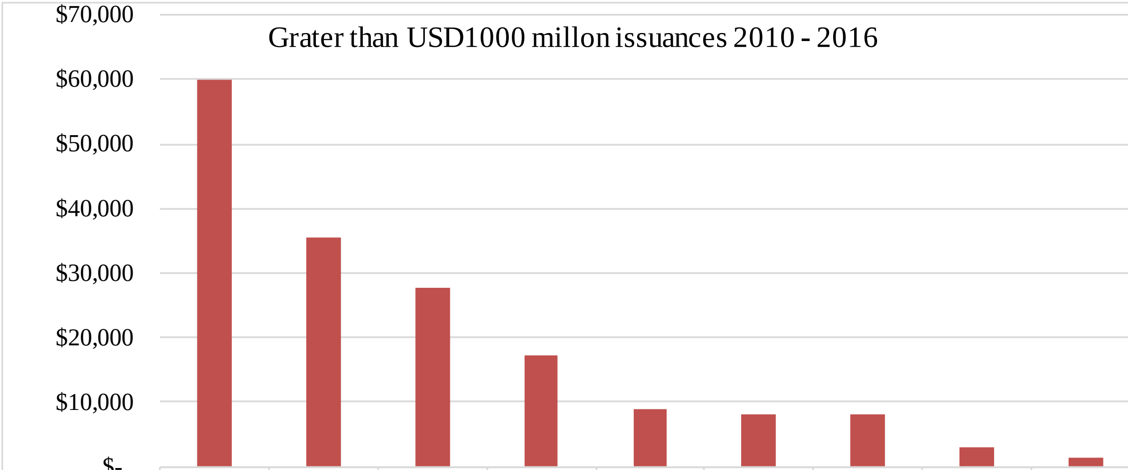
This index called the Dow Jones Sukuk Investment Grade Total Return Index is designed to track the performance of Sukuk global returns. Like the previous index, this includes Sukuk denominated in US dollars that correctly comply with the principles of the Sharia'a.

The three graphics indicated above demonstrate that the trend of the three indices is upward. Meaning that the overall performance of Islamic bonds has been positive with continued growth. Although the Sukuk market has experienced downturns due to external economic situations such as the drop in the oil price; the returns of this market are positive.

2.5. Main actors in the Sukuk market

To determine the main participants in the Sukuk market, all the emissions exceeding USD 1 billion between 2010 and 2016 were selected, where 73 emissions were obtained. By classifying these emissions by their jurisdiction of origin, it is found that the main players in this market come from Malaysia, Saudi Arabia, Indonesia, Qatar, United Arab Emirates, Turkey, Pakistan and Bahrain.

Graphic 18: Accumulation of emissions greater than USD 1 billon 2010 – 2016 by country of origin



	Malaysia	Saudi Arabia	Indonesia	Qatar	United Arab Emirates	Turkey	Pakistan	Sudan	Bahrein
Monto	$60,026	$35,520	$27,769	$17,335	$8,984	$8,181	$8,075	$3,068	$1,450

Source: IIFM Sukuk Report 2016 5th edition, 2014 4th edition, 2013 3rd edition, 2011 2nd edition y Thompson Reuters: Sukuk Perceptions 2016.
Elaboration: Marmolejo, Mateo y Suárez, José.

Table 5: List of emissions greater than USD 1 billon between 2010 - 2016[3]

YEAR	ISSUER	ISSUANCES	COUNTRY	CURRENCY	TYPE	STRUCTURE	FACE VALUE USD MILLIONS	TIME TO MATURITY	ISSUER NATURE
2016	Government of Indonesia	4	Indonesia	IDR	Doméstico	Sukuk Al Ijarah	$ 11,385.00	6	Sovereign
2012	PLUS Berhad	23	Malaysia	MYR	Doméstico	Sukuk Al Musharakah	$ 9,728.00	16	Quasi -Sovereign
2016	Government of Malaysia	14	Malaysia	MYR	Doméstico	Sukuk Al Murabahah	$ 9,551.00	11	Sovereign
2013	Government of Malaysia	10	Malaysia	MYR	Doméstico	*Sukuk* Al Murabahah	$ 9,335.00	8.65	Sovereign
2011	Government of Qatar	1	Qatar	QAR	Doméstico	Sukuk Al Ijarah	$ 9,067.00	3	Sovereign
2013	General Authority of Civil Aviation	1	Saudi Arabia	SAR	Doméstico	*Sukuk* Al Murabahah	$ 4,056.00	10	Sovereign
2012	Government of Qatar	2	Qatar	QAR	Internacional	Sukuk Al Ijarah	$ 4,000.00	16	Sovereign
2012	General Authority Of Civil Aviation	1	Saudi Arabia	USD	Internacional	*Sukuk* Al Murabahah	$ 4,000.00	1	Quasi -Sovereign
2012	Gobierno de Indonesia	13	Indonesia	IDR	Doméstico	Sukuk Al Ijarah	$ 3,620.00	9	Sovereign
2013	Government of Malaysia	3	Malaysia	MYR	Doméstico	*Bai' Bithaman Ajil*	$ 3,587.00	7.16	Sovereign
2012	Government of Pakistan	6	Pakistan	PKR	Doméstico	Sukuk Al Ijarah	$ 3,135.00	3	Sovereign
2016	Government of Sudan	1	Sudan	SDG	Doméstico	*Sukuk Al Musharakah*	$ 3,068.00	1	Sovereign
2014	Qatar Central Bank	2	Qatar	QAR	Doméstico	*Sukuk* Al Murabahah	$ 3,018.00	4	Sovereign
2014	Islamic Development Bank	2	Saudi Arabia	USD	Internacional	Sukuk Al Wakalah	$ 3,000.00	5	Quasi -Sovereign
2016	Islamic Development Bank	2	Saudi Arabia	USD	Internacional	Sukuk Al Wakalah	$ 2,700.00	5	Quasi -Sovereign
2013	Islamic Development Bank	3	Saudi Arabia	USD	Internacional	Sukuk Al Wakalah	$ 2,700.00	5	Quasi -Sovereign
2011	Pengurusan Aset Air Berhad	9	Malaysia	MYR	Doméstico	*Sukuk* Al Murabahah	$ 2,576.00	7	Quasi -Sovereign
2012	Government of Malaysia	7	Malaysia	MYR	Doméstico	*Sukuk* Al Murabahah	$ 2,527.00	12	Sovereign
2016	Gobierno de Indonesia	2	Indonesia	USD	Internacional	Sukuk Al Wakalah	$ 2,500.00	7	Sovereign
2014	Saudi Electricity Company	2	Saudi Arabia	USD	Internacional	Sukuk Al Ijarah	$ 2,500.00	20	Quasi -Sovereign
2016	Government of Turkey	4	Turkey	TRY	Doméstico	Sukuk Al Ijarah	$ 2,059.00	3	Sovereign
2014	Government of Malaysia	2	Malaysia	MYR	Doméstico	*Sukuk* Al Murabahah	$ 2,038.00	5.25	Sovereign
2011	Gobierno de Indonesia	5	Indonesia	IDR	Doméstico	Sukuk Al Ijarah	$ 2,033.00	10	Sovereign
2015	Jimah Energy Ventures	1	Malaysia	MYR	Doméstico	*Sukuk* Al Murabahah	$ 2,006.00	5	Corporate
2015	Government of Indonesia	1	Indonesia	IDR	Doméstico	*Sukuk* Al Murabahah	$ 2,000.00	10	Sovereign
2013	Saudi Electricity Company	2	Saudi Arabia	USD	Internacional	*Sukuk Al Ijarah*	$ 2,000.00	20	Sovereign
2013	Sadara Chemical Company	1	Saudi Arabia	SAR	Doméstico	*Sukuk Al Musharakah*	$ 2,000.00	5	Corporate
2011	Government of Malaysia	2	Malaysia	USD	Internacional	Sukuk Al Wakalah	$ 2,000.00	8	Sovereign
2016	Government of Pakistan	2	Pakistan	PKR	Doméstico	Sukuk Al Ijarah	$ 1,876.00	3	Sovereign
2010	Saudi Electricity Company	2	Saudi Arabia	SAR	Doméstico	Sukuk Al Istithmar	$ 1,867.00	7	Corporate
2012	Saudi Electricity Company	2	Saudi Arabia	SAR	Doméstico	Sukuk Al Ijarah	$ 1,750.00	8	Quasi -Sovereign
2013	BGSM Management Sdn. Bhd.	6	Malaysia	MYR	Doméstico	*Sukuk Al Musharakah*	$ 1,743.00	4.1	Corporate
2014	Government of Indonesia	1	Indonesia	IDR	Doméstico	*Sukuk Al Ijarah*	$ 1,664.00	3	Sovereign
2013	Malakoff Power Sdn. Bhd.	7	Malaysia	MYR	Doméstico	Hybrid *Sukuk*	$ 1,623.00	5	Corporate
2013	Government of Indonesia	1	Indonesia	IDR	Doméstico	*Sukuk Al Ijarah*	$ 1,567.00	3	Sovereign
2016	Government of Malaysia	2	Malaysia	USD	Internacional	Sukuk Al Wakalah	$ 1,500.00	20	Sovereign
2016	Khazanah Nasional	2	Malaysia	USD	Internacional	Sukuk Al Wakalah	$ 1,500.00	5	Quasi -Sovereign
2012	Government of Turkey	1	Turkey	USD	Internacional	Sukuk Al Ijarah	$ 1,500.00	6	Sovereign
2016	Etihad Airways	1	United Arab Emira	USD	Internacional	Sukuk Al Wakalah	$ 1,500.00	5	Corporate
2015	Government of Malaysia	2	Malaysia	USD	Internacional	Hybrid *Sukuk*	$ 1,500.00	20	Sovereign
2014	Government of Indonesia	1	Indonesia	USD	Internacional	*Sukuk* Al Wakalah	$ 1,500.00	10	Sovereign
2013	Government of Indonesia	1	Indonesia	USD	Internacional	*Sukuk Al Ijarah*	$ 1,500.00	5.5	Sovereign
2012	Khazanah Nasional Bhd	4	Malaysia	MYR	Doméstico	Sukuk Al Musharakah	$ 1,450.00	15	Quasi -Sovereign
2016	Government of Bahrain	2	Bahrain	USD	Internacional	Sukuk Al Ijarah	$ 1,450.00	5	Sovereign
2012	Celcom Transmission	5	Malaysia	MYR	Doméstico	*Sukuk* Al Murabahah	$ 1,442.00	8	Corporate
2014	Government of Turkey	1	Turkey	TRY	Doméstico	*Sukuk Al Ijarah*	$ 1,333.00	2	Sovereign
2014	National Commerial Bank	1	Saudi Arabia	SAR	Doméstico	Hybrid *Sukuk*	$ 1,300.00	5	Corporate
2012	Islamic Development Bank	2	Saudi Arabia	USD	Internacional	Sukuk Al Wakalah	$ 1,300.00	5	Quasi -Sovereign
2013	Government of Turkey	1	Turkey	USD	Internacional	*Sukuk Al Ijarah*	$ 1,250.00	5	Sovereign
2015	Petroliam Nasional	1	Malaysia	USD	Internacional	*Sukuk* Al *Wakalah*	$ 1,250.00	5	Corporate
2013	Ooredoo Qatar (telecom)	1	Qatar	USD	Internacional	*Sukuk* Al Murabahah	$ 1,250.00	5	Corporate
2012	Government of Dubai	2	United Arab Emira	USD	Internacional	Sukuk Al Ijarah	$ 1,250.00	8	Sovereign
2011	Manjung Island Energy Berhad	7	Malaysia	MYR	Doméstico	Sukuk Al Ijarah	$ 1,242.00	9	Corporate
2014	Bank Negara Malaysia	1	Malaysia	MYR	Doméstico	*Sukuk* Al Murabahah	$ 1,209.00	10	Sovereign
2016	DP World	1	United Arab Emira	USD	Internacional	Sukuk Al Mudharabah	$ 1,200.00	7	Quasi -Sovereign
2014	Saudi Electricity Company	1	Saudi Arabia	SAR	Doméstico	*Sukuk Al Ijarah*	$ 1,200.00	10	Sovereign
2012	National Higher Education Fund	2	Malaysia	MYR	Doméstico	*Sukuk* Al Murabahah	$ 1,118.00	10	Quasi -Sovereign
2012	Tanjung Bin Power	9	Malaysia	MYR	Doméstico	Sukuk Al Ijarah	$ 1,101.00	12	Corporate
2015	Riyad Bank	1	Saudi Arabia	SAR	Doméstico	*Sukuk* Al Murabahah	$ 1,070.00	Perpetual	Corporate
2013	Riyad Bank	1	Saudi Arabia	USD	Doméstico	Hybrid *Sukuk*	$ 1,070.00	5	Corporate
2016	Neelum Jhelum	1	Pakistan	PKR	Doméstico	Sukuk Al Mudharabah	$ 1,064.00	5	Corporate
2013	Government of Turkey	1	Turkey	TRY	Doméstico	*Sukuk Al Ijarah*	$ 1,039.00	2	Sovereign
2011	Nakheel Group	1	United Arab Emira	USD	Doméstico	Sukuk Al Ijarah	$ 1,034.00	5	Corporate
2015	National Commerial Bank	2	Saudi Arabia	SAR	Doméstico	*Sukuk* Al Murabahah	$ 1,007.00	Perpetual	Corporate
2016	Government of Pakistan	1	Pakistan	USD	Internacional	Sukuk Al Ijarah	$ 1,000.00	5	Sovereign
2016	Government of Turkey	1	Turkey	USD	Internacional	Sukuk Al Ijarah	$ 1,000.00	5	Sovereign
2015	Gobierno de Ras Al Khaimah	1	United Arab Emira	USD	Internacional	*Sukuk* Al Ijarah	$ 1,000.00	10	Sovereign
2015	Dubai Islamic bank	1	United Arab Emira	USD	Internacional	*Sukuk* Al Murabahah	$ 1,000.00	Perpetual	Corporate
2015	Islamic Development Bank	1	Saudi Arabia	USD	Internacional	*Sukuk* Al *Wakalah*	$ 1,000.00	5	Quasi -Sovereign
2014	Government of Pakistan	1	Pakistan	USD	Internacional	*Sukuk* Al Ijarah	$ 1,000.00	5	Sovereign
2014	Islamic Development Bank	1	Saudi Arabia	USD	Internacional	*Sukuk* Al *Wakalah*	$ 1,000.00	5	Quasi -Sovereign
2013	Dubai Electricity and Water Authority	1	United Arab Emira	USD	Internacional	*Sukuk Al Ijarah*	$ 1,000.00	5	Sovereign
2013	Dubai Islamic Bank	1	United Arab Emira	USD	Internacional	*Sukuk Al Mudharabah*	$ 1,000.00	4.1	Corporate

[3] The data in this table was obtained from the annual reports of the IIFM in its 1, 2, 3, 4, 5 and 6 edition.

The table above shows in detail all the emissions that exceed USD 1 billion in the 2010-2016 period. It is seen that the largest volume of emissions comes from the government sector in which the main actors are Malaysia, Indonesia, Pakistan and Qatar. The quasi-sovereign issuances come mostly from the Islamic Development Bank. Finally, among the most important corporations participating in this market are Jimah Energy Ventures, of Malaysia, Sadara Chemical Company and Saudi Electricity Company of Saudi Arabia, BGSM Management Sdn. Bhd. of Malaysia, Etihad Airways of the Arab Emirates, among others. Many of the corporate actors are related to the energy sector such as refineries and hydroelectric plants, as well as financial groups and airlines.

2.6. Conclusions

In conclusion, this chapter has shown that the Sukuk Islamic bond market has expanded considerably in the last fifteen years. In 2016, a total value of USD 88.27 billion was issued. This is 75 times more than what was issued in 2001. The importance of Malaysia for the Sukuk market in general should be highlighted, since it has been noted as one of the main actors, as well as the largest issuer of these titles and also the area of greatest commercialization of these certificates.

The characteristics of this market were analyzed and the following conclusions were obtained:

First, the Sukuk market is mainly domestic. Countries and corporations prefer to issue in their local currency and within the borders of their State. However, as of 2010, international emissions have experienced growth that is worth noting. In 2016, international emissions increased by 670% compared to 2010. Therefore, each time the number of players who are issuing outside their borders and in different currencies than their own is considerably increasing.

In addition, it was found that the preferred currencies for Sukuk emissions are those countries who demonstrate a highly developed Islamic financial system, with the exception of the US dollar. Smaller players, such as Nigeria, Jordan, Bangladesh or Brunei, often prefer to issue debt in the currencies of Malaysia, Saudi Arabia, Indonesia, Qatar and the United Arab Emirates. These countries, as seen in the first chapter, have the most developed financial systems in the Islamic world. Another aspect that can be highlighted is that along with the increase of international emissions there has been an expansion in US dollar issuances.

Second, this is a market in which countries are the main actors. The sovereign issuances have exceeded 40% of the emissions issued each year since 2008. While on average, corporate emissions represent 30%. Quasi - sovereign emissions represented only 4% of the titles issued in 2008 and have reached their maximum of 33% in 2016. Among the most important sovereign issuers are: Malaysia, Saudi Arabia, Indonesia, Qatar, United Arab Emirates, Turkey, Pakistan and Bahrain. In the quasi-sovereign part, multilateral organizations dominate, such as the Islamic Development Bank and the Saudi Electricity Company. Finally, in the private sector, companies from the energy sector, financial conglomerates and airlines stand out.

Third, it was found that each time more information is available for the stakeholders of the international financial system. For example, the development of several indices that measure Sukuk aspects such as performance, behavior, emission levels and more. This shows the formalization of the Sukuk market. The improvements in terms of information transparency, regulation, control, increase in the volume of emissions and maturity of the market in general, have led to the development of a certain inclination towards commercialization in the stock market in recent years. Although only 30% of these titles are traded on the stock market, this figure increases every year. Finally, it is noted that the main exchanges are Nasdaq Dubai, Irish Stock Exchange, Bursa Malaysia and London Stock Exchange.

CHAPTER III:
DEVELOPMENT AND CHARACTERISTICS OF NON-ISLAMIC SUKUK ISSUERS

3.1. Sukuk in the non-Islamic world: Introduction

It is often pointed out that Islamic finance is not strictly directed towards the Muslim population. This has two meanings: first, Islamic financial institutions will not reject non-Muslim clients and; second, non-Islamic people or institutions can provide Islamic financial services (Nienhaus, 2013). In daily practice you can find examples of the two instances mentioned above.

For the first case, the growing number of non-Muslim participants in Takaful contracts is usually cited in a variety of countries where Islamic practice is not common; and for the second, the large number of institutions that offer asset management operating according to the Sharia'a. Nevertheless, the message offered by the Islamic finance openness is more ambitious, since it allows to deduce that the potential market for this type of finance is much larger than only the population of Muslim countries and Muslim minorities in non-Islamic countries (Alam, 2015).

If the field of Islamic finance is for everyone, the potential market for this would be the whole world, and its growth could be virtually unlimited. This implies that Islamic finance should offer the world something superior or at least something that is not inferior to what currently exists.

For some non-Muslim people compliance with the principles of Sharia'a as a constituent element of Islamic finance is itself irrelevant. Instead, there could be macro-systematic aspects, micro-commercial characteristics, or even ethical implications of the observance of Islamic law that would make it attractive to a non-Muslim population. Macro-systematic characteristics refers to aspects of the policies that Islamic finance has at the macro level, and may be more beneficial than existing policies in conventional finance. Micro-commercial characteristics refers to aspects in the micro sphere of finance and banking as the performance that different investments can have and other positive aspects involved in financing by Islamic institutions compared to institutions immersed in conventional finance (Alam, 2015) (Nienhaus, 2013).

3.2. Historical overview of Sukuk internationalization towards non-Islamic economies

The first instrument of this type issued by a non-Islamic economy was structured in Germany in 2004. This emission in the West was made by the federal State of Saxony-Anhalt for USD 100 million. Among the factors that motivated this issuance, the following can be mentioned. First, Saxony-Anhalt is one of the States with greater specialization and knowledge in capital markets since it obtains most of its financing through this method. In addition, the vision of the Saxony-Anhalt financial authority had set itself the objective of expanding its portfolio of investors to the Middle East and Asia. Finally, and one of the most critical points, the State of Saxony-Anhalt was heavily indebted through its program of issuing notes and bonds in conventional markets. The State's per capita indebtedness was higher than any other federal State in Germany, which obliged it to finance itself at higher rates than desired. Subsequently, the State found that the cost of financing in the Islamic markets was much lower, so it decided to list a Sukuk title on the Luxembourg Stock Exchange. This being the first in the Western world and showing to the entire globe that there can be confidence in this type of instruments (IE - Business School, 2011).

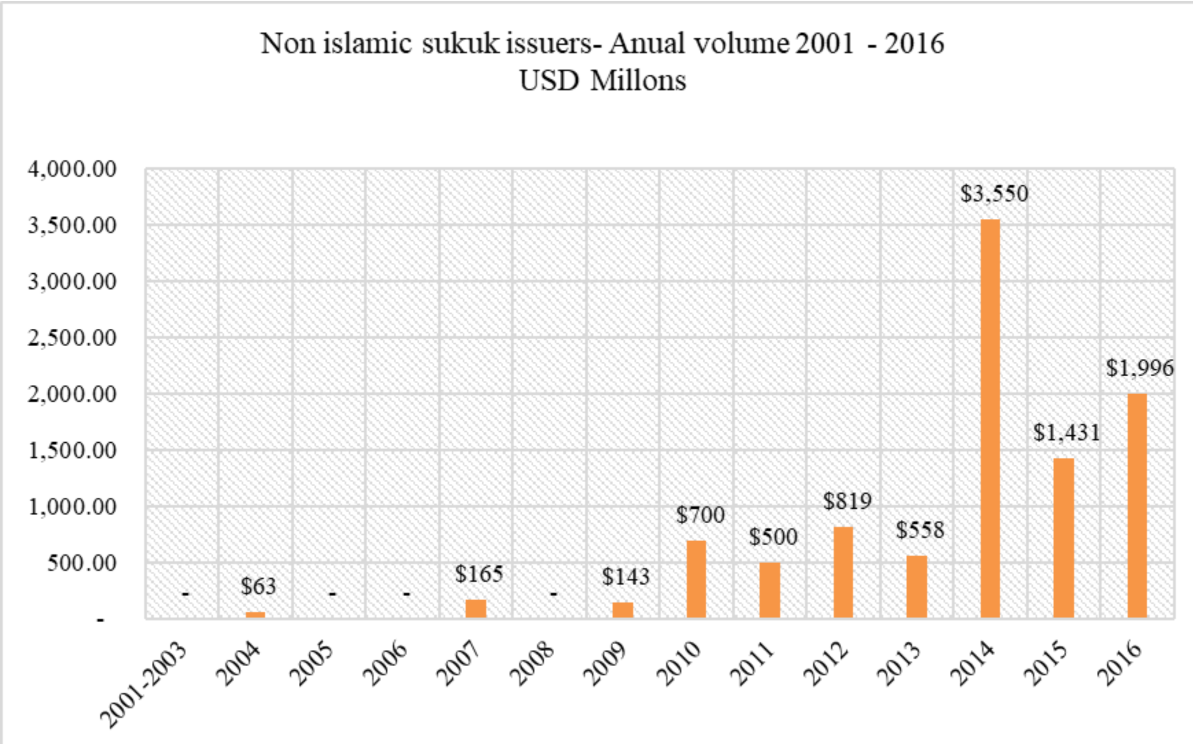
In 2007, the first corporate Sukuk was issued by a non-Islamic entity and at the same time the first in the United States. The issuing company was East Cameron Energy with an amount of USD 165 million. Two SPCs were established, one in the United States and the other in the Cayman Islands to structure a Musharaka title. The income generated by the issuance was used to pay debts previously acquired by the company. The liquidity problems of this firm and the low income generated by the extraction of natural gas caused the payment of obligations to be interrupted. The company declared bankruptcy and the first default of a non-Islamic Sukuk (Zeineldin, 2014). On the other hand, the non-Islamic world learned more about the implications of this type of instruments and in 2009 the first corporate Sukuk of USD 143 million was issued in the United Kingdom by the Sanctuary Building Company.

Subsequently, 2010 was an important year for the internationalization of these titles towards non-Islamic economies. First, the World Bank Group through the International Finance Corporation issued USD 100 million in the form of Sukuk in the international market and spoke favorably about the benefits of this type of instruments and publicly supported the development of Islamic financial markets. Confidence in these securities is felt most strongly after the issuance of USD 500 million by the American company General Electric in the same year. Toyota Financial Services, a subsidiary of Toyota based in Malaysia and The International Innovative Technologies Ltd of the United Kingdom joined the group both issuing USD 50 million. Undoubtedly, the intervention of names such as General Electric, Toyota and the World Bank generate greater confidence in this market and in this type of instruments (Verma, 2011).

Between 2011 and 2013 banks of global importance joined the market, as is the case of the British banks; HSBC through its subsidiary HSBC Bank Middle East limited, along with Gatehouse Bank. In addition, the French bank Société Générale is included. The participation of such financial institutions drives the development of this market in non-Islamic economies.

Undoubtedly, 2014 is the most important year for the non-Islamic Sukuk market. Highly valued emissions from different non-Islamic governments are added. The Government of Hong Kong issues USD 1 billion, the Government of South Africa USD 500 million, the United Kingdom Government USD 740 million, and Luxembourg's Government USD 220 million. The intervention of non-Islamic governments with issuances exceeding USD 500 million fuels interest in this market and makes the non-Islamic Sukuk expand to levels never seen before. The same year, the International Finance Facility for Immunization, a quasi-sovereign entity, issues an additional USD 500 million. Finally, 2014 concludes with an important issuance by one of the largest investment banks in the world, Goldman Sachs with USD 500 million. 2014 can be as the golden year for the non-Islamic Sukuk market.

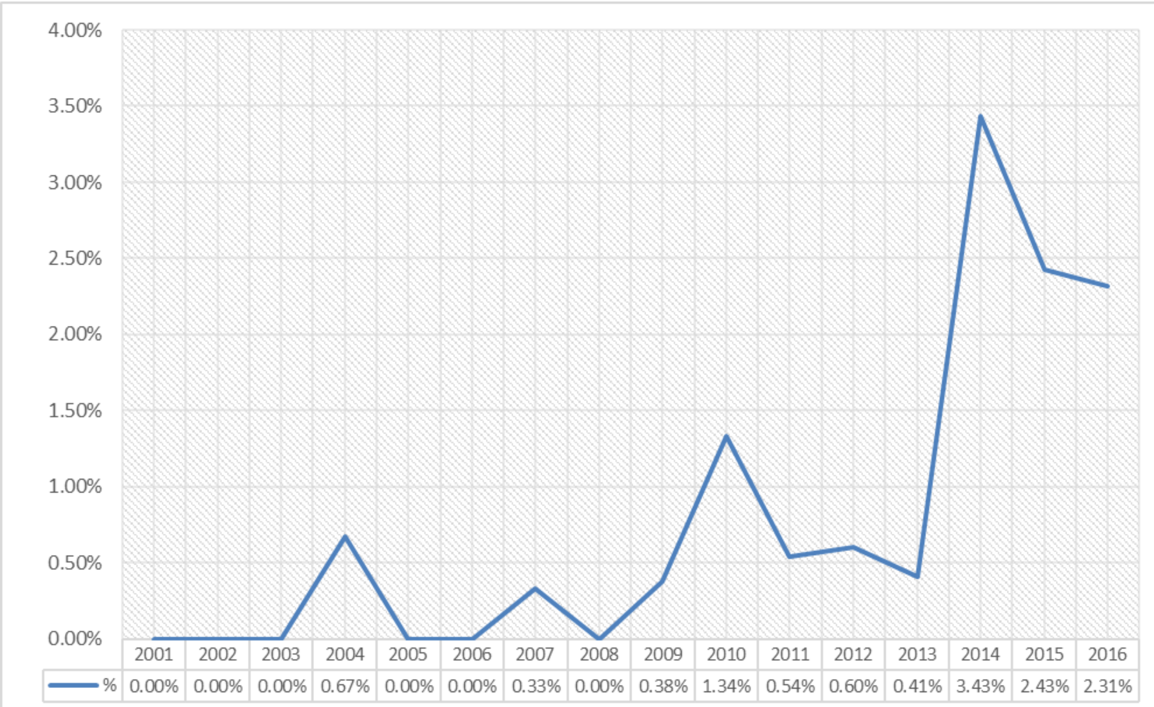
Graphic 19: Annual volume of emissions by non-Islamic issuers



Source: IIFM Sukuk Report 2016 - 2010 from 1st to 6th edition.
Elaboration: Marmolejo, Mateo y Suárez, José.

Finally, the years 2015 and 2016 register a volume of USD 1.43 and 1.99 billion respectively. These years have been driven by the intervention of governments, mainly emissions from Hong Kong and Singapore and corporations such as the Saudi British Bank HSBC.

Graphic 20: Non-Islamic participation on total Sukuk issuances 2001 - 2016



Source: IIFM Sukuk Report 2016 - 2010 from 1st to 6th edition.
Elaboration: Marmolejo, Mateo y Suárez, José.

Figure 20 demonstrates that emissions of non-Islamic participants have been increasing since 2001. This indicates that the Sukuk market is each time more attractive to non-Islamic issuers.

3.3. Current international interest

The development and formalization of the Sukuk market has increased the participation of issuers seeking international investors. Due to higher nominal values of the emissions, the amount of listings in international stock exchanges continues to increase year by year.

The transparency and regulation generated by an issuance listed on a stock exchange reduces investor´s uncertainty. Investors from regions such as the United States or Europe are sensitive to the level of emissions and markets transparency. International investors become even more demanding when it comes to unusual assets such as Sukuk. Both the increase in emissions on the stock market and the greater availability of information regarding this industry, fueled the international appeal of this market.

The international interest in these titles has undoubtedly increased. For example, in 2015 30% of a major corporate issuance of Emirates Airlines listed on Nasdaq Dubai was acquired by US investors. In other sovereign issuance by the Government of the United Arab Emirates in 2016, 45% was acquired by European and Asian investors. (Nasdaq Dubai - Ideal Ratings, 2015).

Sovereign emissions are one of the main factors that contributed most to promote interest in this market. It is recorded that every time there are more non-Islamic governments that not only support the issuance of this type of securities, but also have been high-value Sukuk issuers. It is argued that a solid sovereign sector that encourages this type of emissions makes the private sector be more confident in this market.

3.4. Analysis of emissions by non-Islamic entities

In this section, Sukuk emissions made by public and private non-Islamic entities in recent years are analyzed in greater depth. In the previous section, the development of non-Islamic emissions was reviewed chronologically, now aspects such as the place of origin, the nature of the issuer, the volumes issued and currencies preference for non-Islamic emissions will be analyzed. Finally, some of the most relevant cases of non-Islamic emissions will be mentioned in greater detail.

The following table shows all the non-Islamic emissions of Sukuk from 2001 to 2016, ordered from the highest to the lowest; plus the country of origin, the structure of the Sukuk issued, its nominal value, term and nature of the issuer. This table summarizes the analysis of each category that is done below.

Table 6: Non-Islamic issuances 2007-2016

YEAR	ISSUER	ISSUANCES	COUNTRY	CURRENCY	TYPE	STRUCTURE	FACE VALUE USD MILLIONS	TIME TO MATURITY	ISSUER NATURE
2014	Government of Hong Kong	1	Hong Kong	USD	International	Sukuk Al Ijarah	$ 1,000.00	5	Sovereign
2016	Government of Hong Kong	1	Hong Kong	USD	International	Hybrid Sukuk	$ 1,000.00	5	Sovereign
2015	Saudi British Bank HSBC	1	United Kingdom	SAR	International	Sukuk Al Wakalah	$ 750.00	5	Corporate
2016	Saudi British Bank HSBC	1	United Kingdom	USD	International	Sukuk Al Wakalah	$ 750.00	5	Corporate
2010	General Electric USA	5	United States	USD	international	Sukuk Al Ijarah	$ 500.00	60	Corporate
2011	HSBC Bank Middle East Limited	1	United Kingdom	USD	International	Hybrid Sukuk	$ 500.00	5	Corporate
2012	Gatehouse Bank	1	United Kingdom	USD	International	Sukuk Al Wakalah	$ 500.00	5	Corporate
2014	Government of South Africa	1	South Africa	USD	International	Sukuk Al Ijarah	$ 500.00	5.75	Sovereign
2014	The International Finance Facility for Immunization	1	United Kingdom	USD	International	Sukuk Al Murabahah	$ 500.00	3	Quasi - Sovereign
2014	Goldman Sachs	1	United States	USD	International	Sukuk Al Wakalah	$ 500.00	5	Corporate
2014	Government of the United Kingdom	1	United Kingdom	GBP	International	*Sukuk Al Ijarah*	$ 400.00	5	Sovereign
2014	Government of the United Kingdom	1	United Kingdom	USD	International	Sukuk Al Ijarah	$ 340.00	5.08	Sovereign
2012	First Resources Ltd	2	Singapore	MYR	International	Sukuk Al Musharaka	$ 319.00	5	Corporate
2013	Societé Générale Bank Trust	1	France	MYR	International	Sukuk Al Murabahah	$ 300.00	5	Corporate
2013	First Resources Ltd	1	Singapore	MYR	International	Sukuk Al Musharaka	$ 238.00	10	Corporate
2014	Government of Luxemburg	1	Luxemburg	EUR	International	Sukuk Al Ijarah	$ 220.00	5	Sovereign
2015	Global Vaccine Aliance GAVI	1	United States	USD	International	Sukuk Al Murabahah	$ 200.00	5	Quasi - Sovereign
2007	East Cameron Energy	1	United States	USD	International	Sukuk Al Murabahah	$ 165.00	5	Corporate
2015	The Solar Guys International	1	Australia	MYR	International	Sukuk Al Murabahah	$ 150.00	5	Corporate
2009	Sanctuary Building Sukuk	1	United Kingdom	USD	International	Sukuk Al Musharaka	$ 143.00	10	Corporate
2010	Corporación Financiera Internacional IFC	1	World Bank	USD	International	Sukuk Al Ijarah	$ 100.00	6	Quasi - Sovereign
2015	Monetary Authority of Singapore	1	Singapore	SDG	International	Sukuk Al Musharaka	$ 100.00	8	Sovereign
2016	Developer Country Garden	1	Hong Kong	MYR	International	Sukuk Al Murabahah	$ 98.00	5	Corporate
2016	Hong Kong Sukuk Limited	1	Hong Kong	USD	International	Sukuk Al Wakalah	$ 98.00	10	Sovereign
2015	BEGW Sdn Bhd	1	China	MYR	International	Sukuk Al Wakalah	$ 97.00	5	Corporate
2014	The Bank of Tokio - Mitsubishi UFJ Malasia	1	Japan	MYR	International	Sukuk Al Ijarah	$ 90.00	5	Corporate
2004	Saxony - Anhalt	1	Germany	BHD	International	Sukuk Al Ijarah	$ 63.00	10	Sovereign
2015	City Developments Limited	1	Singapore	USD	International	Sukuk Al Ijarah	$ 54.00	5	Corporate
2010	Toyota Financial Services Malaysia Subsidiary	1	Japan	MYR	International	Sukuk Al Ijarah	$ 50.00	5	Corporate
2010	The International Innovative Technologies Ltd	1	United Kingdom	GBP	International	Sukuk Al Wakalah	$ 50.00	5	Corporate
2016	Japan International Coperation Agency	1	Japan	USD	International	Sukuk Al Ijarah	$ 50.00	5	Quasi - Sovereign
2015	Franklin Global Sukuk Fund	1	Luxemburg	USD	International	Sukuk Al Wakalah	$ 40.00	5	Corporate
2015	Franklin Global Sukuk Fund	1	Luxemburg	USD	International	Sukuk Al Wakalah	$ 40.00	5	Corporate
2013	FWU Group	1	Germany	USD	International	Sukuk Al Wakalah	$ 20.00	5	Corporate

Source: IIFM Sukuk Report 2016 - 2010 from 1st to 6th edition, UK treasury department.
Elaboration: Marmolejo, Mateo y Suárez, José.

Table 7: Volume analysis of issuances by non-Islamic jurisdictions

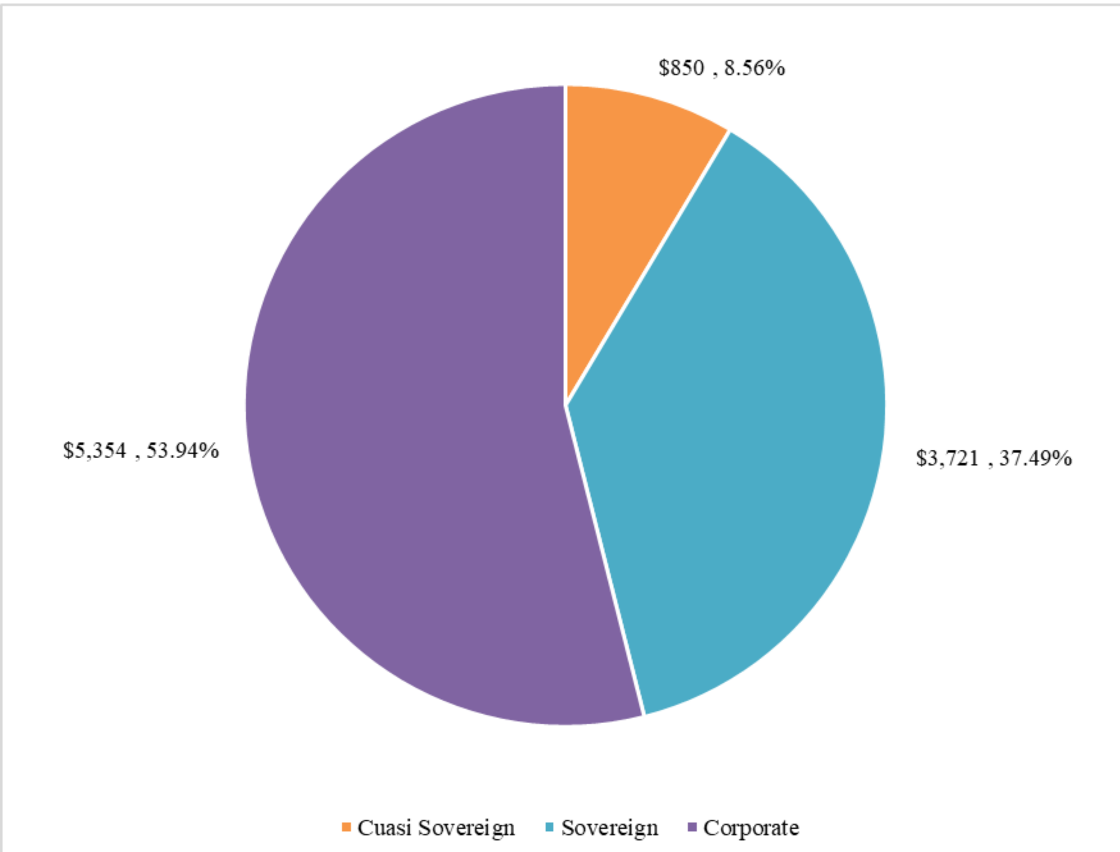
Non-Islamic Issuer	Number of Issuances	Total Face Vlue USD Millions
United Kingdom	9	$ 3,933
Hong Kong	4	$ 2,196
United States	5	$ 1,365
Singapore	4	$ 711
South Africa	1	$ 500
France	1	$ 300
Luxembourg	3	$ 300
Japan	3	$ 190
Australia	1	$ 150
The World Bank	1	$ 100
China	1	$ 97
Germany	2	$ 83

Source: IIFM Sukuk Report 2016 - 2010 from 1st to 6th edition, UK treasury department.
Elaboration: Marmolejo, Mateo y Suárez, José.

Between 2001 and 2016, Sukuk emissions registered by 11 non-Islamic nationalities and one by a multilateral institution, the World Bank. The most important players in the non-Islamic emissions market come from the United Kingdom, Hong Kong and the United States. In the same period, the non-Islamic Sukuk registered a value of USD 3.93 billion in the United Kingdom, USD 2.19 billion in Hong Kong and USD 1.36 billion in the United States.

3.4.1. Nature of the issuer: Private/Sovereign/Quasi Sovereign issuance

Graphic 21: Non-Islamic emission by type of issuer 2001 - 2016 USD million

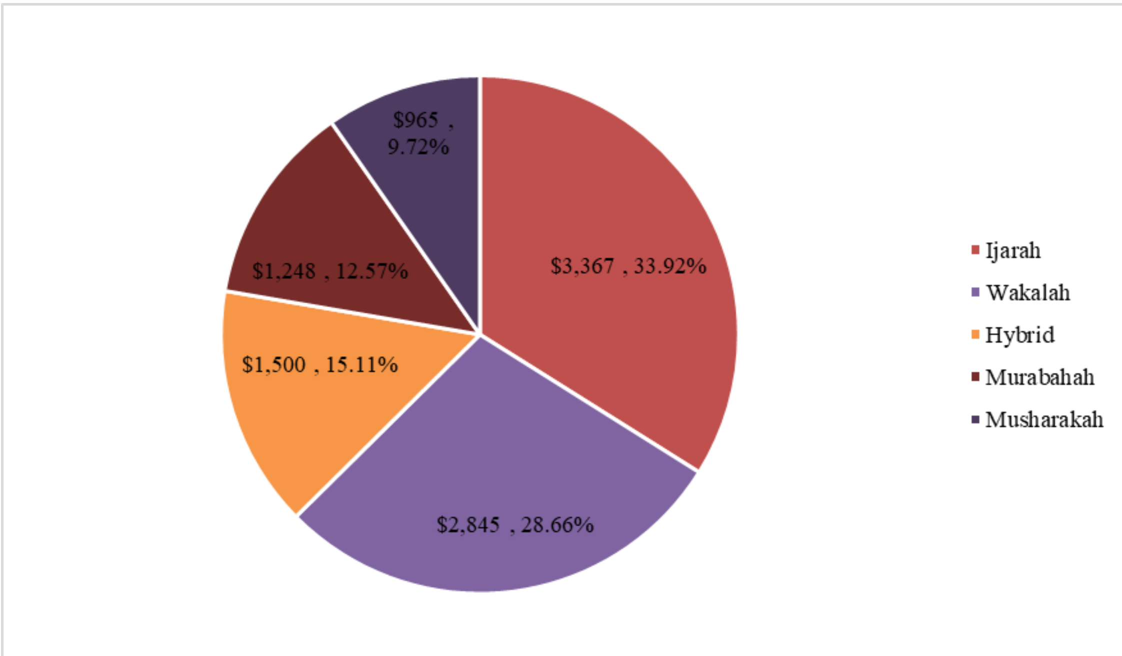


Source: IIFM Sukuk Report 2016 - 2010 from 1st to 6th edition, UK treasury department.
Elaboration: Marmolejo, Mateo y Suárez, José.

Based on the nominal values issued up to 2016, the group of non-Islamic issuers is mostly corporate. The corporate sector represents 53.94% of the issuances, followed by the sovereign sector, which accounts for 37.49% of the issuances and the quasi-sovereign entities represent the remaining 8.56%. Unlike the global market of Sukuk, which is mainly represented by sovereign entities, the non-Islamic issuers are mainly corporations belonging to the private sector.

3.4.2. Sukuk structure of non-Islamic emissions

Graphic 22: Non-Islamic emission by Sukuk type, 2001 – 2016 USD millions



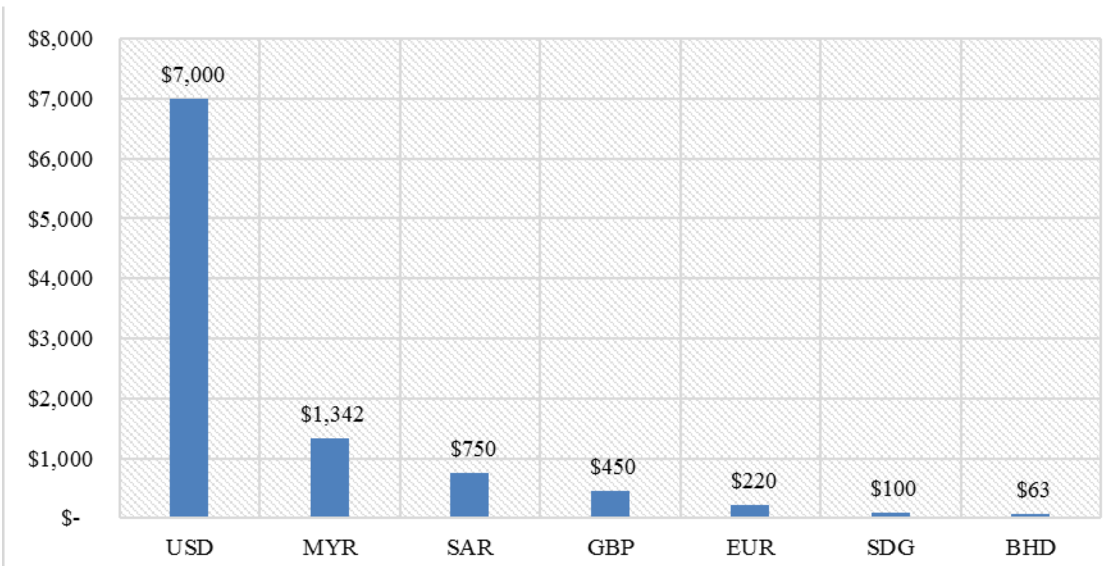
Source: IIFM Sukuk Report 2016 - 2010 from 1st to 6th edition, UK treasury department.
Elaboration: Marmolejo, Mateo y Suárez, José

The Sukuk structure of non-Islamic issuers depends mainly on the type of issuer. Although the preferred form is the Ijarah Sukuk structure, this constitutes only sovereign emissions. Meanwhile, the private sector prefers to issue Wakalah Sukuk - 29%, which constitutes one of the lowest cost structures. In addition, 15% of this type of emissions are hybrid, titles that combine more than one type of structure. While the classic Murabaha and Musharaka structures represent 12% and 10% respectively. The type of structure chosen by the issuer depends on their needs, the costs they are willing to face, and the type of assets on which the contract is based.

3.4.3. Currencies in which non-Islamic issuances are structured

The following graphic shows that the preferred currency by non-Islamic issuers is the USD by a wide margin. Emissions in USD are driven mainly by non-Islamic governments and by financial institutions based in the United States and Europe. Issuers from Asia prefer to emit in MYR - Malaysian Ringgit, SAR - Saudi Rial, SDG - Singapore Dollar and BHD - Bahrain Dinar. On the other hand, issuances in local currencies occur on the part of the United Kingdom Government in GBP- British Pounds and the Luxembourg Government in EUR -Euros.

Graphic 23: Non-Islamic issuances by currency 2001 – 2016 USD millions



Source: IIFM Sukuk Report 2016 - 2010 desde from 1st to 6th edition, UK treasury department.
Elaboration: Marmolejo, Mateo y Suárez, José.

3.5. Most relevant cases

This section describes four cases of emissions made by non-Islamic entities, taking the example of a corporate case, Goldman Sachs, two sovereign issuances, the United Kingdom and South Africa, and finally a multinational entity, the International Financial Corporation part of the World Bank Group. The latter is classified as a quasi-sovereign issuance.

3.5.1. Goldman Sachs Group – USD 500 million

The Goldman Sachs Group (GS) is one of the leading global institutions in investment banking, securities and asset management. It offers a wide range of financial services to a diversified group of customers that includes corporations, financial institutions, governments and people with high net worth. It was founded in 1869, its headquarters are located in New York City and it maintains offices in all the major financial centers of the world (Goldman Sachs Group, 2017).

J. Aron & Company (JANY), is an entity that has been an integral part of the Goldman Sachs Group for more than thirty years, dedicated especially to the operations of commodities. JANY is an indirect subsidiary of the GS Group, wholly owned by the same (IIFM, 2015). The following table presents a summary of the details of this issuance.

Table 8: Goldman Sachs issuance (summary) - 2014

Issuer	JANY Sukuk Company Limited
Obligor	J. Aron & Company
Country of Transaction	United States of America
Issue type	Sukuk Al Wakalah
Issue rating	A- (S&P) / A (Fitch)
Pricing date	September 16, 2014
Issue date	September 23, 2014
Tenor	5 years
Maturity	September 23, 2019
Profit Rate	2.844%
Listing	Luxembourg stock exchange
Governing Law	British law
Joint Lead Managers	Goldman Sachs International, Abu Dhabi Islamic Bank, Emirates NBD Capital, National Bank of Abu Dhabi, NCB Capital Company, QInvest

Source: IIFM Sukuk Report (5th edition) 2016
Elaboration: Marmolejo, Mateo y Suárez, José

The issuer ("JANY Sukuk Company Limited" an SPV or SPC incorporated in the Cayman Islands) issued the certificates and applied the issuance process aligned to the principles of the Wakalah contract. J. Aron & Company (JANY), as mentioned, is the subsidiary of the GS Group in charge of commodities operations.

JANY, with the guarantee of GS, used the capital collected through the issuance of the Wakalah contract to invest, first, in a commodities portfolio that comply with Sharia'a principles (Wakalah commodities) and second, a portfolio of commodities assigned to a second Muradahah type contract.

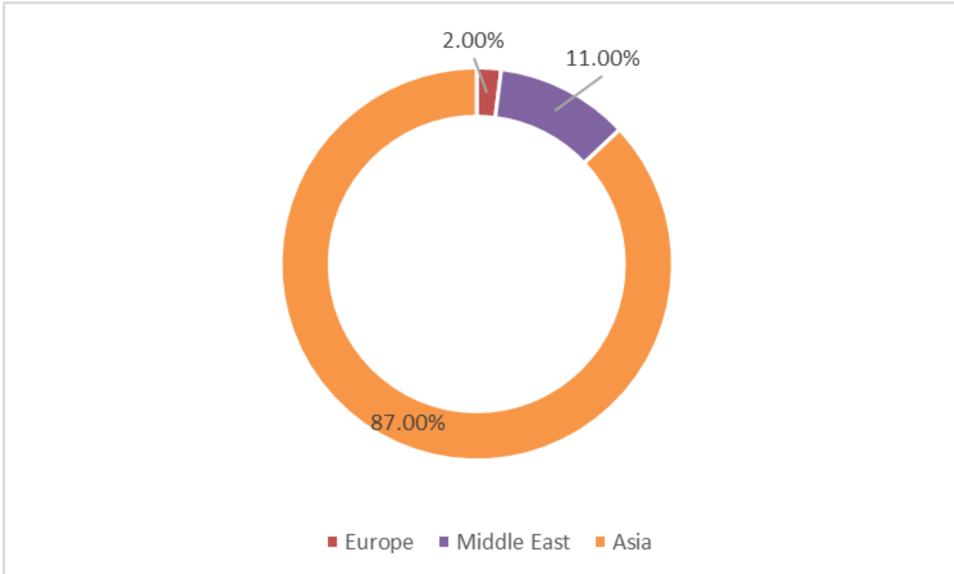
The Wakalah contract constitutes 51% of the issuance outcomes. In this emission, JANY agrees; first, to tranfer to the issuer the benefits generated through a portfolio of commodities that comply with the Sharia'a, and second, to try to generate a return based on transactions, sales and acquisitions of commodities that are based on Sharia'a principles.

The remaining 49% from the issuance of certificates corresponds to the Murabahah agreement. The assets acquired (commodities) under the second contract will be sold in the future and deferred payments will be delivered to the holders of these securities. It was established in the Murabahah agreement that the GS Group is responsible for guaranteeing such payments.

The initial price of this Sukuk issuance package with a nominal value of USD 500 million, were published at 6 a.m. London time on September 16, 2014. The list of orders grew rapidly over USD 1.4 billion between the first four hours after the opening. Offers and orders grew until the listing closed in USD 1.5 billion. This allowed the certificates to reach the market for the first time in a higher price than its initial nominal value and therefore the intermediaries of this placement acquired a profit percentage of 2.844%.

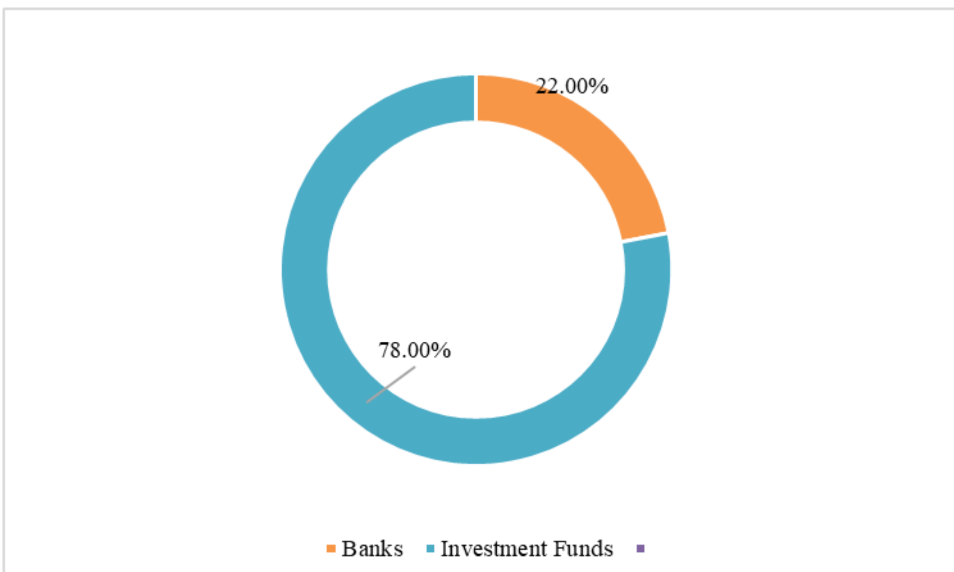
The following graphics detail the geographical distribution and the type of investors that acquired this issuance.

Graphic 24: Geographical distributions of first Goldman Sachs issuance purchases



Source: IIFM Sukuk Report (5th edition) 2016.
Elaboration: Marmolejo, Mateo y Suárez, José.

Graphic 25: Entities that acquired Goldman Sachs Sukuk on the primary market



Source: IIFM Sukuk Report (5th edition) 2016.
Elaboration: Marmolejo, Mateo y Suárez, José.

The two preceding graphics highlight that most of the investors involved in the first purchase of this issuance came from the Middle East and ordered 87% of the emission. The rest was obtained by European and Asian investors. Banks (Islamic and conventional) constituted the largest type of investor, 78%. The asset managers obtained the remaining 22%.

3.5.2. United Kingdom Government 2014 - USD 400 million

As mentioned above, the United Kingdom Government Sukuk was the first made by a non-Islamic government, and at the same time, the first issuance by a Western government. This is an Al Ijarah sovereign issuance made in 2014. It has a term of 5 years and its nominal value was GBP 340 million. Its placement in the primary market generated a return of 1.75% for its intermediaries since it was sold on par. Making a payment on par means paying more for a financial asset than its value registered on the accounting books. This transaction attracted a list of orders worth GBP 2.3 billion. Once again, the majority of buyers in the first instance were located in the Middle East and Asia, the first represented 37% and the second 24% of the total buyers. However, about 25% of the titles were acquired by investors within the same United Kingdom (IIFM, 2015). Among the buyers are various asset management institutions, central and private banks, and international financial institutions.

The Minister of Finance of the United Kingdom George Osborne commented about the main purpose of this issuance:

> "The first sovereign Sukuk issuance made by Great Britain fulfills the government's commitment to become the main western hub for Islamic finance and is part of our long-term economic plan to make Britain the undisputed center of the global financial system."

He also assured that there has been a strong demand, resulting in a price that offers an interesting quality-price ratio for investors. Osborne manifested that he hopes the success of this governmental emission will encourage other Sukuk emissions coming from the private sector in the United Kingdom (UK Government, 2014).

Finally, it should be noted that unlike the rest of the cases in this section, this issuance was listed on the London stock exchange, fulfilling the objective set by the Government Finance Minister.

3.5.3. South Africa Government 2014 - USD 500 million

The emission made by South Africa was the second made by a country that has no direct relationship with Islam after the issuance of the Government of the United Kingdom. The South African government issued a Sukuk Al Ijarah worth USD 500 million in September 2014, with a maturity period of 5.75 years. This Sukuk received orders that exceeded its nominal value (USD 500 million) for more than four, reaching an order list of USD 2.2 billion. Again, as in the previous case, the majority of buyers of this issuance came from the Middle East; combined with Asian investors made up 59% of total buyers (IIFM, 2015).

This issuance is recognized as the dollar-denominated bonds that have been sold at the lowest cost of indebtedness since 1994. The South African government manifests that this issuance was designed to expand its investor’s base to the Arab and Asian markets; especially those belonging to the Gulf States (Adrienne Klasa, 2014).

According to Megan McDonald, head of capital markets in the Standard Bank of South Africa "A key objective of the National Treasury of South Africa was to achieve a new investor’s base, in order to diversify conventional investors composed mainly by European buyers." The Standard Bank in conjunction with BNP Paribas South Africa and KFH Investment were responsible for preparing the sale.

This government demonstrated its interest in issuing Islamic financial instruments in 2011. Since then, implementing all the appropriate structure and regulation for this type of issuance as well as deciding what the appropriate assets would be for the emission type took a period of three years. That is how they carried out the structuration in 2014 (Adrienne Klasa, 2014). Since this issuance is classified as an Al Ijarah, the Sukuk holders must be guaranteed partial ownership of an asset.

The listing was done on the Luxembourg stock exchange, in the same way as in the case of Goldman Sachs. It can be seen that Luxembourg is one of the main destinations for listings from non-Islamic issuers. This was the first European stock exchange to list Sukuk, starting in 2002.

3.5.4. International Finance Corporation – USD 100 million

The issuance by the International Finance Corporation (IFC), a member institution of the World Bank Group, is another relevant case. In 2009, it announced its interest in issuing Sukuk certificates for USD 100 million. An Al Ijarah structuration was chosen, constituting the first quasi-sovereign issuance made by a multilateral organization that is not specifically Islamic.

The IFC made its Sukuk issuance in 2010 and expressed the objective of accelerating the growth of emerging economies (IFC, 2015). These certificates have a period of five years and were intended to support the different financial activities of the IFC in the Middle East and North Africa, as well as other parts of the world. This was initially listed on Nasdaq Dubai, the largest exchange center in the Middle East. Part of the emission was also listed on the London stock exchange.

The institutions that were in charge of this transaction were the Dubai Islamic Bank, HSBC, National Bank of Abu Dhabi and Standard Chartered Bank. The investors were: 75% banks, 20% official institutions and 5% fund managers (IIFM, 2015). As previously mentioned, this issuance by an entity from the World Bank Group was the one that sealed the confidence for governmental and private entities to take the step to develop this type of emissions.

3.6. Conclusions

This chapter has shown that Islamic finance is not directed only towards actors who are related to Islam, but maintain an openness to any institution or person, as long as Islamic law is respected. It has been proven that institutions foreign to Islam make use of Islamic bonds more frequently, both on the supply side (issuers) and the demand side (investors). On the one hand, non-Islamic issuances have increased annually at an average rate of 117.49% in the 2001 – 2016 period. Each time more US and European institutional investors acquire these securities through the stock market. In this regard, the United Kingdom, Hong Kong and the United States are the most relevant actors in the non-Islamic sector.

The analysis of the characteristics of non-Islamic emissions allowed the following conclusions:

First, non-Islamic Sukuk issuances are mainly international. In other words, this issuances were made in currencies and territories different than the nationality of the issuer, excluding the USD. Western issuers prefer to structure in EUR, GBP or USD and on the London or Luxembourg stock exchange, while Asian issuers choose to structure their emissions in MYR, Saudi Riyals, Singapore Dollars and Bahraini Dinars.

Second, this is a sector in which private companies are the main actors. Unlike the Islamic market which is mainly driven by sovereign issuers (40%), non-Islamic emission are mostly corporate (54%).

After analyzing specific cases, it was found that non-Islamic issuers have decided to enter this market for the following reasons:

First, improvements in market conditions. Several consider that it is a market that has been formalized thanks to different situations such as the increased volume of issuances through stock exchanges, transparency in information and regulation.

Second, political motivations and incentives in the internal market. In most corporate cases, they seek to expand and diversify the investors' base. On the other hand, sovereign issuers seek to attract investors to the domestic market, promote their local financial market with new products and boost the private sector related to this type of finance.

Third, it has been noted that financial situations also motivate to enter the Sukuk market. The cost-benefit ratio or the impossibility of obtaining financing in the common capital market forces issuers to look for alternatives in other markets.

In addition, in the four cases analyzed it is relevant that the first offer of the emissions reached the primary market at a value greater than par (accounting books value). This demonstrates investors' confidence in the issuers and, also, confidence in these instruments, since the buyers were willing to pay more than the nominal value of the securities to acquire them for the first time. In addition, it is interesting to note that investment banks can benefit in two instances by issuing these securities if the appropriate market conditions are presented. On the one hand, its subsidiaries obtain financing through SPCs and, on the other hand, the bank or parent company acts as the placement agent of these securities in the primary market. If there is an underwriting relationship and sell the securities on par, the profits are for the underwriter. Underwriting refers to an investment banker's process of packaging and selling a security on behalf of a client, the underwriter would be the bank. This was the case of the Goldman Sachs issuance in which Goldman Sachs International participated as an underwriter, therefore it obtained part of the profits generated by the difference between the nominal value and the issuance price.

CONCLUSIONS AND FINAL RECOMENDATIONS

Conclusions:

After analyzing these three chapters that describe the functioning of Sukuk and its development in Islamic and international markets we have reached the following conclusions:

1. Islamic finance is not simply an adaptation of conventional finance, but a practice that has an entire legal, moral, cultural, social and technical structure open to all types of investors.

2. Sukuk bonds were originated in Islamic economies, and are financial instruments in which capital or money is not bought or sold, therefore, it does not have an interest rate.

3. Benefits can be obtained both for those who issue these securities and for those who acquire them, because it is a form of association in which the risk is shared between the parties involved.

4. Public and private entities make use of this instrument after establishing a special purpose company or SPC which facilitates transactions. This process ensures that the principles of Islamic law are respected.

5. The Sukuk market covers approximately one seventh of the total assets of the Islamic financial system as of 2016 and is the system´s component that has grown the most in the last 15 years, surpassing the expansion of Islamic banking and insurance.

6. Much of the Sukuk market is centralized in Malaysia and is directly exposed to political and economic changes in this country.

7. These securities market has undergone a process of expansion since 2001, which is verified with the following parameters:
    a. the global increase in the nominal value of issued Sukuk securities,
    b. the increase in the average size of issuance packages, mainly sovereign,
    c. the beginning of its commercialization in financial centers of global importance,
    d. the inclusion of new non-Islamic participants in this market that includes important players in the international capital market such as governments, multinationals, corporations and multilateral organizations;
    e. and, the evolution in aspects such as information diffusion, transparency, controlling entities, regulation and standardization.

8. The main actors involved in the Sukuk market are the governments of Malaysia, Saudi Arabia, Indonesia, Qatar, United Arab Emirates, Turkey, Pakistan and Bahrain, while the main non-Islamic participants are the United Kingdom, Hong Kong and United States corporations.

9. The increasing use of Sukuk by non-Islamic entities is mainly due to:
    a. the intention to diversify the investors base,
    b. obtain better financing conditions,
    c. promotion of Islamic finance within the political sphere, as well as providing support for further expansion of local stock exchanges to this market,
    d. obtain profits.

Recommendations:

1. The viability of other forms of financing, such as Sukuk, by corporations and governments should be evaluated as an alternative to the issuance of conventional debt in capital markets.

2. Ecuador should analyze the possibility of financing through Islamic bonds and evaluate if this mechanism represents lower financing costs than the conventional methods used.

3. We believe that the dissemination of studies on the Sukuk market and Islamic finance in general should be encouraged, given that there are few academic documents available in Spanish on these issues.

4. In academic institutions that offer courses and professions related to international finance and business, the subject of Islamic finance should be included; not only because of its growing global importance, but because of alternative options and benefits granted.

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