The Importance and Role of Sukuk Marketing as an Islamic Bond in the Economy

Ilhan Keskin, Hasan Bulent Kantarci

Abstract—In this study, one of the tools of Islamic financing known as “Sukuk” a non-interest bearing investment which has started to be implemented in Turkey and the world as a whole is discussed. In order to increase the vitality and efficiency of the economy, by taking lessons from the recent economic crisis new developments in the banking and investment sector are being expanded. The purpose of all investors is to obtain more revenue through the use of capital. The inability of traditional investment tools to meet the expectations of investors and the interest based financial system where one investor benefits at the expense of another there has been the need for a different, reliable and non-interest bearing financial market that is consistent with the Islamic rule. As a result an alternative and more reliable interest free financing tool “Sukuk” rental certificates covering people who are sensitive to Islamic rules, appeal to all segments, hidden remaining capital that contributes to the economy, reduce disparities in income distribution, common risk sharing system of profit and loss sharing has emerged. Today, for the structural countries by examining the state of the world market economy the applicability, enactment and future issues associated with this attractive kind of Islamic finance namely the “Sukuk” market has been explained.

Keywords—Islamic finance, Islamic markets, non-interest bearing, rental certificates.

I. INTRODUCTION

A resultant effect of the remarkably fast-growing Islamic financial services is “Sukuk” notably in terms of participatory banking for financial institutions, businesses and a country’s treasury and financial market has been a vehicle carrying the opportunity to provide resources compatible with Islamic Law [1].

Looking the reference for Sukuk, the main source of Islamic Finance begins with the Quran followed by the rules for Prophet Sunneh and Islamic tradition. Based on the results of these principles is Islamic Economics which gives prominence to profit-loss sharing rather than the interests gained from capital accumulation and investments. Thus an investment in this respect will be interest free and hence help remove the problem of inflation. Moreover, economic and social disparities in the distribution of income will fall to the lowest level and also help spread the right to participate in the ownership of properties. Negative considerations will not be given to capital owned by individuals, investments and obtained businesses. With the same logic, economic based fights between various countries can also be alleviated. However, the exchange concept underlying an economy is also included in the basic concept of Sukuk. That is an exchange based on profit-loss sharing. This includes the use of money as a mutual means of exchange for services and assets. All this will ensure that money rather than being an object will be used as a medium of exchange.

In this way, by changing traditional financial instruments based on Islamic principles, practices and beliefs Islamic bonds and tools are created and also participatory banks are established. Sukuk market is not only used by participatory banks and bonds within a country but has also expanded to the international level. The most important development in non-interest bearing financial institutions is Islamic bonds also referred to as Sukuk [2]. Until the end of 2012, worldwide trading volume reached approximately 460 billion dollars. More especially, it greatly influenced the trade of bonds in developing countries. Most of which were non-Muslim countries including England and America, even countries like France would like to have a say in Sukuk markets which shows there is a lot of income expectations from the Sukuk Market [3]. Islamic financial institutions have started to increase in both developed and developing countries, in these countries the profitability of commercial life need to include sustainable earnings, and in order to provide a dynamic process in the management of a country’s debt and assets as well as providing the next generation of a country with the most valuable economic and social capital, there is the need to spread awareness for a long and prosperous economy [4]. Given the general information on the concept and structure of Sukuk according to the scope of study, because it is an Islamic bond Islamic religious structures were also emphasized. In addition, by examining the global development of Sukuk a developing Muslim country like Turkey place in Sukuk market has also been studied.

II. THE DIFFERENCE BETWEEN SUKUK BONDS AND OTHER CLASSICAL BONDS

In many countries all over the world a common and widely used investment instrument Sukuk concept by examining its root traces the root of the word from the Arabic word “sak”. “Sak” as a word means financial certificates or documents. When using the word stock for bonds and bills in Arabic, these securities referred to in the form assets for Islamic bonds however the word “Sukuk” is used [5]. Sukuk is the plural word for the word “Sak” which means financial certificate in Arabic [6]. The Latin equivalent of “Sukuk” which is “Çek” as referred to by Muslim traders from the Middle Ages-shopping...
and other commercial activities has been used as a paper depicting financial obligations [7]. Sukuk is an asset based investment instrument [8]. In this way Sukuk, offers the right to benefit and the possibility to benefit from social wealth. Sukuk is not a debt, but a particular project which represents the undivided share in assets and the right to investors or service [9]. Additional information is provided about the widest definition of the concept of Sukuk considering the The Accounting and Auditing Organization for Islamic Financial Institutions. According to this definition, Sukuk represents the equivalent value after exportation; making advance plans on how to invest the amount realized from export and depending on the type of investment made fixed assets and the share of other assets is also represented. It means the certificate for projects or the right to form partnerships under private investment activities [10], [11], [8].

Sukuk is a tool which endeavors to comply with the Islamic ban on the use of interests and based on the transfer of the share of money realized from the use of an entity to produce a tangible asset that is it is asset-based or asset-backed. This investment instrument, relative to conventional bonds and other securities possess a relatively low risk.

Under the concept of Sukuk, these rights and assertions expressed in words is not limited only to the cash flow but also offers individuals property rights [12]. Securitization is a process by which the ownership of assets is transferred to the large number of investors through certificates that are generated in proportion to the asset’s value [13]. In this way the structure of Sukuk is different from traditional stocks and bonds. That is while conventional bonds are focused on the use of interest bearing securities, Sukuk is based on a basket of securities which consists of property assets. With the system of Sukuk unlike the system of traditional bonds in which there is a debtor entails a profit and loss partnership. Because Sukuk entails a partnership agreement investors are not guaranteed of a specified level of income or gain. In this case under the concept of Sukuk since investors are given a share of the income or gains derived from assets that are financed by them makes Sukuk different from traditional bonds [14], [11], [12].

The most basic feature of Sukuk is assets used under Sukuk can also be used for special projects and private investment. While these assets can be used in the secondary market, they also provide fixed or variable returns to investors [14]. Sukuk can be traded in secondary markets such as stock exchange and Over The Counter (OTC) markets. In this way it is opened to the access of individual investors. In this way investors who issue Sukuk can provide access to a broad investment pool [3], [15]. Sukuk financing with individual participation ensures that individuals are active in a country’s economy. The instrument of Sukuk generally is composed of Islamic investors but this profile changes over time. Sukuk market which started in Islamic countries with time began to be implemented in non-Islamic countries like Germany, England and America [16].

As it has been pointed out already, the difference between Sukuk and conventional bonds is that conventional bonds are interest bearing and in spite of the fact that under Sukuk incomes cannot be realized from interests, incomes can be generated from renting and profits accrued from undertaken activities under Sukuk. In this way, Sukuk offers a very attractive form of investment tool for investors especially Muslim investors who are not interested in conventional bonds because of it is interest bearing feature. Another distinction of Sukuk from conventional bonds is that investors have direct ownership rights over the fundamental basis of an asset or basket of assets. With respect to traditional bonds however, this is only represented by the financial liabilities of the issuer [17]. Thus, Sukuk as compared to conventional bonds is less risky because in return for an investment an investor has the right to own an asset that is even if the repayment of interest free bonds is not made Sukuk investors have the right to a share of the assets used in an investment [17]. However under classic bonds, the repayment capacity of the issuer of the bond is important and the global crisis in the past year has shown that even large firms can face the situation of not being able to repay their bills. Even the world’s most reliable investment tool generally accepted worldwide the US Treasury Bills experienced a risk to pay back bills, at the last moment the US government adopted the law that authorized the government to make additional borrowing in order to free the US Treasury Bills from such risk. Another difference between Sukuk and conventional bonds is that, organizations that issue Sukuk can only carry out commercial activities that are in compliance with Islamic Laws. In addition issued Sukuk is subject to consulting expenses and additional legal fees which are determined in compliance with Islamic laws. However, there is no limitation on commercial activities that can be carried out by issuers of conventional bonds. Moreover there are no additional administrative expenses incurred under the issuance of conventional bonds [3], [17].

III. THE FUNCTIONING AND TYPES OF SUKUK

Sukuk as an instrument on the basis of all certificates issued has to be real commercial relations. These trade relations require tangible objects such as certificates or contracts. In order for assets to be entered into the system of Sukuk they have to be already within a particular system. As a financial tool in structuring Sukuk which began in Malaysia, contract of exchange, contract of agency and the contract of participation were used as the three basic contracts [15].

The operational framework of the system of Sukuk passes through the processes outlined below [6]:

a) Incumbent (Source Organization) which is the mainstay of Sukuk representing the ownership of assets from a pre-agree price at maturity with the condition of a buy back contract sells assets to leasing companies.

b) Asset leasing companies at the purchased price in an equal manner provides term financing by issuing Sukuk certificates and pays the duty of the purchase price of the asset.

c) Lease agreement (icara lease agreement), the obligation for a specified period, for the purpose of re-leasing the
Sukuk as a much better alternative to the globally recognized financial system has to be in accordance with Islamic values and do their best to increase profitability even at the expense of the well-being of customers. This lack of ethics harms the financial system and let to the global financial crisis. Simply put, without given proper regard to the existence of enough opportunities to make repayment, giving out high amounts of credits led to most financial institutions being unable to make repayments. And like a domino effect led to the global financial crisis. In such an environment the primary objective for commercial activities or invested assets in not only to make earnings, there is the need to be fair and lawful to investors; on a macroeconomic perspective it contributes to the growth of the economy, creates employment thereby leading to a reduction in unemployment level and due the payment of taxes and social security contributions leads to an increase in the tax revenue of a country. Owing to the above Sukuk has become an indispensable financial and investment instrument [6]. Participatory banking has contributed to the economy through different ways. This is done through the provision of funds into the financial system, providing gains to savers, and the distribution of income and transferring funds to the real sector. These notwithstanding there is the formalization of unregistered economic activities, corporate taxes, value added taxes, resource utilization support fund and informalization of unregistered economic activities, corporate taxes, value added taxes, resource utilization support fund and corporate taxes, value added taxes, resource utilization support fund and formalization of unregistered economic activities, corporate taxes, value added taxes, resource utilization support fund and corporate taxes, value added taxes, resource utilization support fund and formalization of unregistered economic activities, corporate taxes, value added taxes, resource utilization support fund and formalization of unregistered economic activities, corporate taxes, value added taxes, resource utilization support fund and formalization of unregistered economic activities, corporate taxes, value added taxes, resource utilization support fund and corporate taxes, value added taxes, resource utilization support fund and bank and insurance contributions to public finance by paying taxes, direct funding of the real sector contributing to the continuity and increase of employment as well as contributions to socio-cultural activities [19].

It is more preferable in terms of increasing the rate of profit investment instruments traded on the secondary market. Firstly, the main aim of classic capitalist financing is only the maximization of profit. A result of this underlying aim of capitalists financial institutions can move away from human values and do their best to increase profitability even at the expense of the well-being of customers. This lack of ethics harms the financial system and let to the global financial crisis. Simply put, without given proper regard to the existence of enough opportunities to make repayment, giving out high amounts of credits led to most financial institutions being unable to make repayments. And like a domino effect led to the global financial crisis. In such an environment the primary objective for commercial activities or invested assets in not only to make earnings, there is the need to be fair and lawful earnings, even if the profit margins expected to be realized from an investment are not considered appropriate the financial system has to be in accordance with Islamic principles. For investors who require funding can consider Sukuk as a much better alternative to the globally recognized capitalist financial system [3].

In the international arena regardless of the interest that is
According to the communique issued by the government on is to get an effective way to gain long term resources to the of an increase in the volume second hand market products arrangements and other similar matters, there is the possibility the obstacles to overcome in the legal infrastructure development of Islamic financial products and pricing, after many activities of western financial institutions in both Today, in Islamic finance there brokerage activities as well as tools such as partnership income securities can be found. asset-backed securities, profit and loss sharing certificates than shares started to be applies in 1980-90 but now unused operate under the name "private institutions" [12]. since 1984 began with participation banks and started to operated under the name "private institutions" [12]. In Turkey non-interest bearing financial instruments other than shares started to be applies in 1980-90 but now unused asset-backed securities, profit and loss sharing certificates tools such as partnership income securities can be found. Today, in Islamic finance there brokerage activities as well as many activities of western financial institutions in both domestic and foreign banking. They are in the market with the development of Islamic financial products and pricing, after the obstacles to overcome in the legal infrastructure arrangements and other similar matters, there is the possibility of an increase in the volume second hand market products [12].

In the development of our country, an important contributor is to get an effective way to gain long term resources to the economy which can be done through the use of Sukuk. According to the communique issued by the government on April 1st 2010 and the official magazine numbered 27539 sukuk market has created a fertile ground for the capital markets of the Gulf countries to be entered into Turkey. This arrangement is important both for Turkey to attract foreign capital and to create new instruments for the capital market [20].

In August 2010 Kuveyt Turk participation Bank Inc. operating in Turkey made about 100 million dollars using Sukuk [18]. This issuance of Sukuk was the first to be issued both in Turkey and Europe. In November 2011 the same participation bank carried out its second issuance of Sukuk [20]. By the year 2015, Turkey’s Islamic banking assets are expected to reach about 87 billion dollars [1].

The Sukuk issued by asset leasing companies in Turkey has been done in the form of th application of Icara Sukuk [2]. Sukuk assets seek resources by services or projects to be implemented and the kinds of Sukuk may vary accordingly. In terms of infrastructure and in this respect is very much on the agenda, in many projects in as long as the funding sources are provided by Sukuk, there can be exceptions such as Sukuk models for infrastructure.

According to Ozeroglu, “although Turkey is one of the centres for the rapidly developing non interest based Islamic banking, it may not benefit from this opportunity due to the lack of product diversity. However, in participation banking Turkish Sukuk market is seen as one of the five largest markets with Turkish Sukuk markets in construction, infrastructure, roads, energy areas and other financial products attracting attention of investors from Asia and the Gulf countries” [21].

V. THE DEVELOPMENT OF SUKUK MARKET IN TURKEY

Sukuk in Turkey is known as a bond based on the method of revenue sharing, bridges, dams, highways, railways, telecommunication systems with sea and air ports and the like which belong to public institutions that removed some provision for regular income generating assets and these incomes are accepted as true and legal issued certificates [12].

The applications of non-interest based banking in Turkey since 1984 began with participation banks and started to operate under the name “private institutions” [12].

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VI. THE GLOBAL DEVELOPMENT OF SUKUK MARKET

First Islamic practices in the Middle Ages showed interest free loans being given by Muslim traders to enhance the development of trade. The foundations for today’s Islamic financial system were laid in the 1960’s [22].

World Sukuk market firstly started in countries with “participation banking” infrastructure [21]. Sukuk is one of the most active tools in Islamic banking. In 1979 Islamic Bank was established in Bahrain with a large portion of the income coming from oil. This bank was the first non interest based bank to be established. This feature has served as a bridge to contribute to promoting Bahrain’s participation banking [23].

After Bahrain Malaysia participated in this bridge and became the second largest doorway. The fundamentals of Islamic banking activity in Malaysia were laid in 1959 [21].

On July 1, 1983 with 500 million Malaysia dollar non interest based bank the Malaysia Islamic Bank was established by Dr. Mahathir Mohamad. The target was to make Malaysia Islamic Bank the “Global Leader in Islamic Banking” and thus emerged afterwards [24]. However, these bonds were not allowed to be traded in the secondary [6]. In spite of this the first issuance of a Sukuk in the secondary market took place in Bahrain in the year 2000 [13]. As a result of these developments by Malaysia Islamic banking sector the first Sukuk was issued in the world and in 1995 a Saudi businessman named Abdullah Salih Kemal was issued with a
Sukuk bond worth $350 million in Malaysia. Again in Malaysia in the year 2002 $600 million worth of treasury was first issued [10], [16]. However the first application Sukuk happened in the year 2002 when the Malaysian government issued Sukuk [20]. Also Malaysia has proven its place in Islamic banking as one of the largest Sukuk exporting countries. By looking at the issuance of Sukuk all over the world, it could be seen that it is concentrated in three regions namely; the South East Asian countries with Malaysia being the leader, Saudi Arabia and the Gulf States and European countries [6]. By providing resources which were channelled into investment through the issuance of Sukuk played a very important role in aiding the entry of Malaysia into emerging economies category in the world [6].

The application of Sukuk was first carried out by the Malaysian government in the year 2001. For a start of the $500 million worth of Sukuk issued %51 was issued to the Gulf countries, %30 to Asia, %15 to Europe and %4 to the United States [13].

In financial markets the main feature of participation bank is banks operating together, which is based on a previous history and intellectual and actual infrastructure which began to be created since 1960 spreading quickly all over the world [12].

Due to the inadequacy of International Fund the Persian Gulf Cooperation Council was established. This council consists of Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the United Arab Emirates. In the countries which were members to this council in order to finance infrastructure and to gain access to a pool of local liquidity the central governments issued Sukuk [25]. Sukuk according to Söyler (2014), in 2013 25% of the world’s global Sukuk issuance that is one quarter was carried out by Saudi Arabia and countries within the Gulf region such as United Arab Emirates, Qatar, Bahrain and Kuwait.

In recent years the issuance of Sukuk is not only limited to the Gulf countries and Southeast Asia but there have been many arrangements in European countries aimed at getting benefits from the issuance of Sukuk. It has served as an alternative capital market instrument not only in Islamic countries but also non Islamic countries such America, Germany, France, Russia, Britain, Japan, China and India.

For the development of Islamic finance in Ireland as well as in other countries, more than 50 funds providing services has been established and the Irish Financial Regulatory Authority has established a special team to provide investment funds which is in compliance with Sharia. Beside this, after the United States in Luxembourg which is one of the world’s second largest investment fund centre and Europe’s most important financial market there is about 1 billion dollars’ worth of Islamic fund and is the first European country to issue Sukuk and from the year 2002 to March 2014 20 pieces of Sukuk were issued [4].

England became the first western country to issue Sukuk worth 2,036 million pounds on 25.06.2014. Apart from this for Sukuk, on the London Stock Exchange an Islamic based index was formed [6]. The banking sector in Iran is managed according to Sharia law and is built entirely on Islamic financing. In Hong Kong Islamic financial transactions has accelerated since 2008. Sukuk securities issued by Malaysia-based companies in this period began to be traded on stock market of the country [26].

According to the Sukuk report published by the International Islamic Financial Market (IIFM), between January 2001 to January 2013 the issuance of Sukuk increased rapidly worldwide and there were approximately 473 billion in total resources at the beginning of 2013, dollar expenses was reached [27], [28]. Sukuk market especially in Asia, the Middle East and other developed countries as well as developing countries has become an important source of financing all over the world.

VII. CONCLUSION

In the capitalist system trade and interest are free. In the socialist system both trade and interest are prohibited. However in the Islamic system interest is prohibited but trade and profits are free. To avoid the use of interest in trade came Sukuk financing which is not only interest free but also complies with Islamic rules has attracted the attention of many investors and has provided investments through the use of Sukuk instruments. Today not only in Muslim countries but also in non-Muslim developing and developed countries the system of Sukuk is being used as financial instruments.

With the system of Sukuk, the unfair advantage obtained from interests and its uneven distribution is prevented. It has also expanded the distribution of resources between countries by establishing more robust trade bridges. By increasing the diameter of the resulting funds projects funded with these funds enlarged. One of the most important features of Sukuk is the rules for the removal uncertainty by using the profit and loss sharing ratio to reduce risk to investors in advance.

The solidarity and assistance of a competition and an interest-based economic system is very important. With the global development of Islamic finance more and more Sukuk market has started to be used on the international market, especially in Asia and the Middle East including development and developing countries has become an important source of financing all over the world. With Sukuk market being in full compliance with Islamic rules is expected to be further increased in the world economy.

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