



THE INTERNATIONAL ISLAMIC LIQUIDITY MANAGEMENT CORPORATION, HEADQUARTERED IN KUALA LUMPUR, MALAYSIA, WAS ESTABLISHED BY EIGHT CENTRAL BANKS AND ONE

MULTILATERAL INSTITUTION TO CREATE AND ISSUE SHARIAH-COMPLIANT FINANCIAL INSTRUMENTS

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Issuer's role vital for institutions seeking Shariah-compliant high-quality liquid assets

The International Islamic Liquidity Management Corporation (IILM) has raised its sukuk programme by 50% from US\$4 billion to US\$6 billion in a significant step towards increasing its asset size. This has enabled the company to add more high-quality assets as it addresses the gap between sukuk demand and supply, and helps strengthen its mandate and role in facilitating effective cross-border liquidity management among institutions offering Islamic financial services

BY CHITO SANTIAGO

IILM CEO Mohamad Safri Shahul Hamid states: "I came here with a clear mandate to grow the asset size, widen the investor base and expand the product offerings – and make the IILM relevant in the Islamic finance space." And 10 months into the job in October, that's exactly what he's doing.

Safri was appointed to lead the IILM for a three-year term effective January 1 2024, succeeding Umar Oseni, who completed his term

on December 31 2023. He joined IILM after spending 13 years at CIMB Bank where he had served in various capacities, including as a deputy CEO for CIMB Islamic Bank and as a senior managing director at the CIMB Bank's public sector group.

The IILM was established in October 2010 by the central banks of eight countries – Indonesia, Malaysia, Mauritius, Qatar, Nigeria, Turkiye, Kuwait and the United Arab Emirates – and one multilateral institution – the Islamic Corporation for the Development of the Private Sector – to create and issue Shariah-compliant financial instruments to facilitate effective cross-border Islamic liquidity management for institutions that offer Islamic financial services.

"The IILM was set up to address

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the growing pool of liquidity in the Islamic finance market driven by the continuing expansion of Islamic banks, which needed an avenue to put their excess funds to work," Safri tells *The Asset* in an interview at his office in Kuala Lumpur. "As an issuer, we come in and plug the gap between supply and demand through the issuance of short-term sukuk."

The liquidity issue in Islamic finance is evident each time the IILM undertakes an auction with its bid-to-cover ratio amounting to at least 2x. "This demonstrates that Islamic banks are flush with liquidity," Safri says. "While this is a good problem to have, it also points out that we need to address an issue – that being, demand far outstrips supply for sukuk paper."

The IILM sukuk are money market instruments backed

by sovereign, sovereign-linked and supranational assets. They are tradable Shariah-compliant short-term financial instruments with tenors of one-, three-, six- and 12-months, backed by a high tangibility ratio of the asset portfolio. They are high-quality instruments rated A1 by S&P Global Ratings and F1 by Fitch Ratings, supported by high-grade, long-term investment.

As high-quality paper, the IILM sukuk are priced competitively, Safri says. "More often than not, our sukuk are

THE IILM, YEAR-TO-DATE TO SEPTEMBER, HAS ISSUED A CUMULATIVE US\$12.32 BILLION ACROSS 39 SUKUK SERIES

US\$12.32 billion

priced inside the prevailing secondary curve in the market."

Investor base

In terms of the nature of IILM investors, as of the third quarter of 2024, 88% are Islamic investors and 12%, conventional ones. A further breakdown shows that 74% of the investors are banks, 90% of which are Islamic; 18% are supranationals, sovereign wealth funds, ministries of finance and central banks; 5%, pension funds and asset managers; and 3%, private banks and high-net-worth individuals.

The IILM sukuk are allocated and distributed through an auction via a network of primary dealers – currently comprised of Abu Dhabi Islamic Bank, Affin Islamic Bank, alBaraka, Boubyan Bank, CIMB Islamic Bank, Dukhan Bank, First Abu Dhabi Bank, Kuwait Finance House, Maybank Islamic, Qatar Islamic Bank and Standard Chartered.

"We are inviting more Islamic banks to become our primary dealers as we continue to increase the supply of our short-term sukuk," Safri notes. Affin Islamic Bank is the latest to be onboarded as a primary dealer in May this year, and he shares that another

bank may join the network later this year.

With six of the primary dealers based in Gulf Cooperation Council (GCC) countries, the IILM auctions are usually dominated by Middle East accounts. But, as Safri points out, demand from Asia and Turkiye has been increasing – with the latter now accounting for 14% of the IILM investor base.

Under Safri, the IILM has made a significant step towards increasing its asset size when it announced in August a 50% increase in its sukuk programme from US\$4 billion to US\$6 billion. “This increase will allow us to add more high-quality assets,” Safri states, “and inevitably help strengthen our mandate and role in facilitating effective cross-border liquidity management among institutions offering Islamic financial services in particular.”

This also reflects the growing and sustainable demand for high-quality sukuk issued by the IILM, which has seen oversubscription rates exceeding 220%. And, he adds: “It reinforces the IILM’s status as a unique provider of Islamic safe-haven liquidity management instruments, vital for institutions seeking Shariah-compliant high-quality liquid assets.”

Year-to-date to November 19, the IILM has issued a cumulative US\$12.32 billion across 39 sukuk series, following the completion of the issuance of three new short term sukuk worth a total of US\$500 million. The issuance was spread across tenors of one-month amounting to US\$280 million, three-month (US\$160 million) and six-month (US\$60 million). This brings the IILM total outstanding sukuk in the market to an all-time high of US\$4.5 billion.

The latest auction, announced on November 19, witnessed a competitive tender among the primary dealers and investors from markets across the GCC and Asia with a combined order book



MOHAMAD SAFRI SHAHUL HAMID, CHIEF EXECUTIVE OFFICER, IILM

“**WE ARE ASSESSING THE IMPACT OF THE LONGER TENOR SUKUK TO OUR PROGRAMME SINCE OUR MANDATE IS TO ISSUE JUST SHORT-TERM SUKUK**

in excess of US\$1.05 billion, representing an average bid-to-cover ratio of 209%.

The fresh issuance marks a significant milestone as IILM ramps up and diversifies its asset portfolio further with the inclusion of a new asset obligor.

New assets, clients

With most of the IILM primary dealers among the leading sukuk arrangers, Safri is confident in their ability to bring new deals to the table, which translates into new assets and clients. The deals are from typically prolific issuers in the public sukuk market, all rated A and above.

The primary dealers also play an important role in the IILM secondary market sukuk trading, which has been increasing and amounted to US\$3.3 billion in 2023, according to Safri. This is the result of the sukuk holders basically being buy-and-hold investors.

“Our primary dealers are incentivized to make market and provide pricing to IILM sukuk investors,” Safri explains. “The incentives are based on the ability of the primary dealers to drive the

secondary market activity, such as bringing new orders, which, in turn, will enable the dealers to make larger bids during an auction. This helps demonstrate that the IILM is a stable source of liquidity management instruments in the Islamic finance space and provide investors with the ability to participate in secondary market trading.”

Going forward, IILM is assessing the possibility of issuing sukuk in reserve currencies other than the US dollar. “We are getting enquiries from some of our primary dealers to consider issuing non-US dollar-denominated sukuk, such as in euro and sterling, and even in Singapore dollars,” Safri states. “But the feedback at the moment has been mixed. There are primary dealers that do not like the idea and prefer to continue issuing in US dollars since they do not have the requirement for other currencies. We have to be very clear in our plan when it comes to issuing in other currencies because we do not want it to be a one-off kind of a deal. We have to ensure certainty in demand and that the sukuk are taken up. While we have an option to swap the sukuk back into US dollars, it will incur the IILM an additional cost.”

Another option the IILM is looking at is that of issuing sukuk with tenors longer than 12 months. Apart from primary dealers, there are non-primary dealers that have reached out to the IILM to consider issuing sukuk with tenors of up to three years. Safri offers: “We are assessing the impact of the longer tenor sukuk to our programme since our mandate is to issue just short-term sukuk.”

The IILM, though, is not rushing to make decisions on these issues. “There is something that we need to address first before we start looking at these innovations,” Safri points out. “That is closing the gap between demand and supply of sukuk.” ■

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PANELLISTS SEE A HIGHER RISK APPETITE FOR ISLAMIC FINANCE PRODUCTS AMONG INSTITUTIONAL AND RETAIL INVESTORS

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Growth story deepens roots

Regulation tightens as more issuers and products come to the market

Islamic finance is gaining further momentum as countries pursue development projects and companies expand operations. The digitalization and sustainability trends have driven the growth of the sukuk market, which is witnessing the entry of new issuers and the emergence of new products in a shifting regulatory landscape

BY THE ASSET

Sukuk issuance has been robust over the past couple of years. In Malaysia, the market is underpinned by foreign investments flowing into government securities, as well as data centre projects riding on the artificial intelligence (AI) boom. The country, in fact, is positioning itself as a data centre hub in Southeast Asia, and there are several factors working in its favour.

“First of all, it comes to the promoters of the data centre, then it is the counterparties, and the third is the availability of the infrastructure,” Yeoh Teik Leng, head of debt markets group at AmInvestment Bank, shares in a panel discussion at the 7th Global Islamic Finance

Issuers and Investors Leadership Dialogue, organized by The Asset Events, in Kuala Lumpur.

“A lot of the promoters are grabbing land to put up a data centre first, but eventually, we have to be aware of who we are going to pop in the servers afterwards. Developers have to be a little bit more cautious on this front,” he suggests.

On the global front, sukuk has gained traction among a group of diverse issuers. Despite risks related to geopolitics and high interest rates, the international sukuk market is on track to hit US\$1 trillion in issuances in a couple of years, notes Bashar Al Natoon, managing director and global head of Islamic finance at Fitch Ratings.

“We are poised for more new entries. Although they’re not going to change the core of the market, they mean significant contributions when it comes to deepening the market depth,” he says. “For instance, the United Arab Emirates (UAE) issues dirham-denominated Islamic treasury sukuk. Other countries are as well exploring tier one sukuk, not to mention sustainable sukuk coming to the fore. Both the actual offering and issuer base are broadening.”

Short-term sukuk

While the majority of Islamic finance products are expected to see a new wave of growth, short-term sukuk risks reversal. Short-term yields are heading for a steep fall as the yield curve continues to normalize. “Our asset income is expected to be reduced next year. Inevitably, short-term issuance and profit paid to investors will be affected,” explains Hichem Bouqniss, executive director in business operations at International Islamic Liquidity Management Corporation (IILM).

Nonetheless, Bouqniss remains upbeat on the private placements of sukuk.

Asset allocation patterns of Islamic investors have also changed. Izad Sallehuddin, chief executive officer of Principal Islamic Asset Management, notices a higher risk appetite among institutional and retail clients, who constantly convert cash into higher-yielding investments.

This sweeping shift of investment choice has driven the growth of alternative investments. Currently, according to Sallehuddin, Principal Islamic Asset Management is overseeing

US\$110 billion of assets in real estate.

“For a lot of institutional clients, they are trying to match their long-term liabilities,” he shares. “The real estate investment spans across different properties, say, multi-family apartments, data centres, logistics, student accommodations, office buildings and hospitality. What we’ve seen is that growth in alternatives has outpaced that in conventional funds.”

New regulation

As the Islamic finance market moves to a new stage, regulators are putting in place more stringent guidelines. The Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) is drafting standard 62, under which unsecured sukuk must be levelled up to asset-backed securities.

This regulatory shakeup may come as a transformational shock to the market, says Al Natoon, given that this standard doesn’t provide the flexibility of different practices among Islamic jurisdictions. “It is a binary approach, you either adopt it or not. If you have someone strictly implementing it, everyone has to follow and transform the debt,” he explains.

If standard 62 is officially put into effect, Sallehuddin observes, corporates may have to undergo a more costly and cumbersome process to fit the sukuk into the new framework. He advises the market to stay careful and prudent in approaching standard 62.

Products development

While new regulation will potentially have a negative impact on the Islamic finance market, strong conditions for product development remain. For instance, retail products are listed among the new



Mashafuddin: New products should be competitive and relevant, service quality maintained



Al Natoon: The retail sector is powerful enough to change the industry and its size



Sallehuddin: Growth in alternatives has outpaced that in conventional funds



Yeoh: The capital requirements of charging stations are not as large as a solar farm’s



Bouqniss: Asset income is expected to be reduced next year, profit paid to investors will be affected



Johan: We work with ministries to assist in the framework design and strategy implementation

offerings. Although this sector varies in size in different economies, Al Natoon notes that Saudi Arabia maintains an 85% share of Islamic financing, which is largely driven by retail demand.

“The retail sector is powerful enough to change the industry and its size. But it only transpires through a top-down approach, otherwise it will never exist or only exist in a very tiny way,” he emphasizes.

Affin Islamic Bank has rolled out new retail products, including education financing, personal financing, as well as concessional electric vehicle financing. “From a retail perspective, people become more comfortable to take on Islamic finance products in banking and asset management,” says the bank’s chief executive officer Syed Mashafuddin. “In view of that, the new products should be competitive and relevant. The retail service quality also has to be maintained, and the price should be uniform.”

Apart from retail products,

sustainable sukuk is also witnessing rising demand. Saudi Arabia, Oman and Qatar are bracing for more of such issuances and formulating the corresponding regulatory frameworks.

Sustainability agenda

Available projects and potential green assets are strong components underpinning the region’s sustainable sukuk market, Al Natoon notes. Malaysia has the same goal, but suitable green assets are confined to solar energy and other renewables, given the size of other sustainable projects are too small to be financed.

“For example, mobility projects don’t possess the required critical mass in financing,” notes Yeoh. “Even for charging stations

across Malaysia, their capital requirements are not as large as a solar farm’s. Their financial values aren’t substantial enough to go into the sukuk market.”

The World Bank is helping Malaysia overcome some of the challenges it faces in the pursuit of sustainability. Shahira Johan, senior financial sector specialist at the World Bank, stresses that a full-fledged sustainability agenda is built on granular details. As such, the World Bank is giving hand-holding support to Malaysia on the foundation of predetermined roadmaps.

“We work with relevant ministries not only to assist in the framework design, but strategy implementation and the knowledge transfer from private to public,” Johan says. “We hope to illustrate a clear picture of where the fund goes, and how the pipeline is actually executed. Only by this clarification process can the sustainable sukuk be established on a solidified basis.” ■