Global Liquidity Management
Regulators’ Perspective
The IILM is an international organisation established on 25 October 2010 by central banks, monetary authorities and multilateral organisations to develop and issue high quality, short-term, Shari’ah-compliant financial instruments to facilitate effective cross-border liquidity management for institutions that offer Islamic financial services (IIFS).

The IILM aims to facilitate cross-border liquidity management amongst IIFS by making available a variety of high quality, short-term, tradable Shari’ah-compliant financial instruments on commercial terms to suit the varying liquidity needs of these institutions.

The current members of the IILM Governing Board are the central banks of: Indonesia, Kuwait, Luxembourg, Malaysia, Mauritius, Nigeria, Qatar, Turkey and the United Arab Emirates, and the Islamic Development Bank Group. Members of the Governing Board are represented by their respective Governors and President.

The availability of the IILM Sukūk is expected to enable the IIFS to compete on a more level playing field with their conventional counterparts. There are several important features of the IILM Sukūk that are intended to assist the establishment of a liquid, cross-border market for IIFS.

The IILM Sukūk are:
(1) Shari’ah-compliant, US Dollar-denominated highly rated short-term financial instruments issued at maturities of up to one year;
(2) backed by sovereign assets;
(3) traded globally via a multi-jurisdictional primary-dealer network; and
(4) have strong regulatory support as they represent a unique collaboration between several central banks and a multilateral development organisation with the aim of enhancing the financial stability and efficiency of Islamic financial markets.

On 26 August 2013, the IILM made history for being the first institution to issue US Dollar-denominated highly rated tradable short-term Sukūk. The inaugural IILM Sukūk of USD490 million, which were rated A-1 by Standard & Poor's Rating Services, had a tenor of 3 months and was fully subscribed. The programme, which currently has USD1.850 billion outstanding cumulative Sukūk, provides the first tradable, Shari’ah-compliant, US dollar-denominated financial instrument with a tenor of under one year. As at today the Sukūk were reissued ten times at maturity. Since the first issuance in August 2013, a total of USD7.64 billion Sukūk have been issued and reissued at auctions.
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To join the community: online.thomsonreuters.com/ifg

TO VIEW OUR IFG RESEARCH SOLUTIONS: http://www.zawya.com/ifg-publications/
The International Islamic Liquidity Management Corporation (IILM) and Thomson Reuters hosted a two-day roundtable in London, UK from August 6-7, 2014 on liquidity management instruments for Islamic financial institutions. The roundtable included presentations and active discussions between central bank regulators, banking practitioners, the IILM, supported by data from a survey of bankers conducted by Thomson Reuters.

The roundtable reviewed many of the issues inhibiting Islamic banks’ ability to manage their liquidity in detail and approached the subject via many different perspectives. Participants raised potential solutions that can help Islamic banks to better manage their surplus liquidity and deal with liquidity shortfalls, some of which are highlighted below.

Roundtable Sessions Overview
Following an introduction, the first session focused on a regulatory perspective of liquidity management that is grounded in monetary stability, financial stability and the policy incentives of increasing global liquidity. Central bankers rely upon yield information as a key input in developing monetary policy, yet in many countries, the yield curve only reflects the activities of conventional banks. This is challenging for central bankers because it limits their ability to see and react to yield anomalies between conventional and Islamic financial systems.

The regulators perspective was followed by the presentation of results from the survey conducted by Thomson Reuters on Islamic bankers regarding the current state of Islamic liquidity management. Treasurers indicate that their demand for Sukūk for investment needs is much greater than their availability of such Sukūk. As a result, bankers use Commodity Murabahah where local counterparties are preferred. The Regulators suggested that the IILM Sukūk can serve as an ideal instrument to meet the gap between supply and demand; and that while more work is needed to expand the issuance any eventual increase will still only represent a portion of the Sukūk that will be needed to fill the gap.
When the focus shifted to give bankers the floor, they discussed the growing limitations on liquidity as a result of new regulatory rules that limit the use of some products to meet their liquidity needs, economic changes where governments are trying to reduce their debt outstanding at the same time as the banks are increasing demand for sovereign debt. One of the possible solutions raised in the session was the use of qualifying securitizations (simple, transparent and non-synthetic) to back liquidity support.

The final session on the first day was focused on the IILM Sukūk and provided a detailed overview of its structure which uses structural aspects of assets-backed commercial paper conduits adapted to Islamic finance principles. In order to receive a high rating, the IILM’s programme (currently, the rating is on the instrument issued, not the IILM itself) relies on high quality underlying assets from its member states and highly rated primary dealers to provide liquidity Sukūk support. The programme is designed to meet a crucial need in Islamic banking, one that is filled in most other sectors by US Treasuries (which of course are not permissible for Islamic financial institutions). In providing for this need, the IILM is contributing to financial stability while also providing support for economic development and debt management in its member countries.

The second day of the roundtable began with an overview of the legal and Shari‘ah perspective. One of the major roles for international organizations in developing new products is that they are able to achieve operational and legal simplification of new structures to lower the cost for other issuers. As the short-term liquidity management sector develops, tax equalization will represent a key impediment in some countries while others will face challenges associated with rules on asset sales and transfers when they look to develop sovereign Sukūk.

The roundtable came to an end with a session looking into the future at how the Islamic finance industry can continue the shift away from bilateral contracts which have dominated to date and towards tradable products that can underpin proper liquidity management.

One alternative raised in the session was a return to an old idea of trade bills which were extensively used in the UK up to a few decades ago and would provide a way to meet liquidity needs as well as to tie the industry to the non-financial economy. These trade bills do however require more work on the Shari‘ah compliance side to ensure they will be widely accepted. Another important area, that would also demand more work, is the difficulty in developing a Shari‘ah-compliant alternative to repos.
Day 1

Welcome and Opening Remarks
Welcome and Opening Remarks

with the observation that “many bank failures are due to inadequacies in managing their liquidity problems” which can lead to financial system instability, Professor Datuk Rifaat, the CEO of the IILM began the two-day roundtable on Islamic liquidity management. His remarks provided an overview of the issue the IILM was designed to solve. Islamic banks have limited options for liquidity management, a problem which has hampered its development for years as larger cash buffers yielding nothing hurt competitiveness and Commodity Murabahah, on which the industry “rel[ies] heavily” lead to inefficient use of funds as a result of low returns and high costs.

His remarks provide a synopsis of the detailed issues to be discussed in the roundtable. The first session provided the backdrop from a regulators’ perspective where liquidity challenges at Islamic banks provide a systemic risk that could grow larger as the percentage of assets held with Islamic banks increase. This was followed by a presentation of a survey of Islamic banks conducted by Thomson Reuters and a discussion of the bankers’ perspective. These focused on the priorities for bankers among liquidity management products as well as how they manage the delicate tradeoff between the search for higher returns for shareholders and limiting risks to comply with national and international rules on capital adequacy and liquidity management.

Following the regulators’ and bankers’ perspectives, Professor Datuk Rifaat presented a detailed overview of the IILM Sukūk, which was followed by an in-depth discussion with lawyers and Shari’ah scholars of the challenges associated with meeting the needs of regulators and bankers within a structure that meets both conditions of secular law and Shari’ah.

Speakers

Professor Datuk Rifaat Ahmed Abdel Karim
CEO, International Islamic Liquidity Management Corporation (IILM)

Mr. Mustafa Adil
Head of Research & Product Development
– Islamic Finance, Thomson Reuters

Mr. Sameeh El-Din
Global Head of Government Market Development, Thomson Reuters
Speakers

H.E. Tan Sri Dato’ Sri Dr. Zeti Akhtar Aziz
Governor, Bank Negara Malaysia

H.E. Hamood Sangour Al-Zadjali
The Executive President, Central Bank of Oman

H.E. Dr. Mohammad Y. Al-Hashel
Governor, Central Bank of Kuwait

Summary

- Global shifts of liquidity are increasingly important in global financial markets with implications for Islamic financial institutions
- Regulators’ new concerns for financial stability and macroprudential policy have to contend with differences between Islamic and conventional financial institutions
- Product and market limitations restrict central bank policy options and can lead to a buildup of yield anomalies and opportunities for regulatory arbitrage between conventional and Islamic banking systems
- In normal times official sources of liquidity are primarily domestic while private liquidity is cross-border focused which means that during crises, global liquidity is dependent on private sector access to official liquidity

Recommendations

- Central banks should add the IILM Sukūk as eligible collateral to provide the liquidity support needed for it to be counted as a High Quality Liquid Asset (HQLA)
- Regulators and governments need to study options for creating sovereign assets and overcome the existing legal limitations that act as impediments to using sovereign assets for sovereign financial instruments
- Government and/or central bank Sukūk issuance should focus on building a sovereign yield curve as a key input into monetary policy
H.E. Dr. Zeti introduced the panel with an overview of the importance of liquidity management in the financial system today and noted the significant global shifts in liquidity during and after the global financial crisis. The initial response to the crisis, the epicenter of which was located in the developed world causing worldwide liquidity impacts, was quantitative easing (QE). Many developing countries experienced surges of capital flows which reversed when the advent of an unwinding of QE began with the Federal Reserve tapering.

The effects of the crisis were dysfunction in markets highlighting the degree to which there is a highly integrated global financial system with interconnectivity through money markets. As a result, countries have learned there are two-way effects that require the development of a strong domestic Islamic interbank money market and liquidity management instruments. This helps cope with the possibility of domestic events spilling over into the global markets as well as protect against effects of global events amplifying movements in money markets domestically. The Islamic Financial Services Board (IFSB) standards developed so far have come a long way to address the financial stability aspects, H.E. Dr. Zeti noted, but significant attention is still needed in liquidity management.

Following H.E. Dr. Zeti’s introduction, H.E. Dr. Al-Hashel highlighted the changing role of regulators’ perspective from one where they move from focusing solely on ensuring monetary stability to use macroprudential policy to meet the financial stability objective. Liquidity management plays a role on a day-to-day basis with monetary operations as well as through liquidity regulations put in place to ensure financial stability. Both have to be done in the context of the current economic and financial cycles which is more difficult in a heterogeneous banking system where Islamic banks and conventional banks each operate at different levels of development and have limited interaction.

Regulators believe they should place a focus on regulating based on common principles of financial intermediation for both Islamic and conventional banks’, rather than being an intermediary between the conventional and Islamic sectors. Multilateral institutions like the IILM and the IFSB should help Islamic and conventional banks “improve mutual interaction” to minimize the need for future central bank intervention to deal with a buildup of surplus liquidity in one sector and a shortage in another. This buildup is likely to emerge from the...
ability of conventional banks to acquire instruments developed for Islamic banks while the opposite is not necessarily true.

The limited supply of instruments that are acquired by both conventional and Islamic institutions coupled with a more limited number of industry pricing benchmarks and too few instruments for interbank deposits has led to many challenges. The scarcity of Shari’ah-compliant securities has compounded the limited liquidity that is available to allow banks to organize a market among themselves and not to rely on central bank activity.

These challenges, in addition to limited lender of last resort facilities and deposit insurance coverage for Islamic institutions, have led to more cash being held by Islamic banks in lieu of an automatic stabilization mechanism from more integration between Islamic and conventional banks. Even where there are mechanisms for trading between the two sectors, the products and their supporting documentation are not always agreed upon among the banks.

The central bank tools to manage in this type of dual system involve being able to forecast liquidity needs, which is at best an imprecise science, but one aided by a central bank’s routine contacts with market participants. Within this process, there is equal treatment for the conventional and Islamic banks but the different instruments for each sector create differences. In conventional monetary instruments the yield is predetermined, while with Islamic instruments, it may not always be quantifiable when using Musharakah or Mudarabah.

The important target for central banks in their monetary policy operations is reducing the potential for yield anomalies between the two sectors which could otherwise lead to a buildup of liquidity imbalances. The central bank addresses this target through the cycle while adjusting conventional policy tools (interest rate targets) but where these are insufficient, they have employed unconventional tools to maintain confidence in the banking system. However, not all of these tools are available in the Islamic banking sector in part because of a shortage of Islamic government securities outside of a few markets like Pakistan and Malaysia.

The shortage of Shari’ah-compliant securities is complicated by both legal impediments that would allow the use of state assets for additional security issuance and difference in how monetary transactions are conducted based on the need for Shari’ah committee approval. New regulatory and supervisory requirements like the Liquidity Coverage Ratio (LCR) and Net Stable Funding Ratio (NSFR) being implemented during the phase-in of Basel III standards raise the need for more Shari’ah-compliant assets that qualify as High Quality Liquid Assets (HQLA).
## BASEL III HQLA changes

<table>
<thead>
<tr>
<th>Final Rule</th>
<th>Previously proposed guidance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Amends and clarifies details for two levels of high-quality liquid assets specifically added and defined in detail. Level 1 assets are cash, certain government securities and other 0% risk-weighted assets under Basel II. Level 2 assets are limited to 40% of buffer after adjustments and have a minimum 15% haircut. Level 2 assets have a 20% Basel II risk weight and meet specifically defined criteria.</td>
<td>Annex introduced permissible Level 2 assets, but further clarification was needed.</td>
</tr>
<tr>
<td>Characteristics defining high-quality liquid assets for liquidity buffers are clarified to require historical data analysis to demonstrate breadth.</td>
<td></td>
</tr>
</tbody>
</table>

Source: BIS, EY

## NSFR required stable funding (RSF) factor

<table>
<thead>
<tr>
<th>Type of exposure</th>
<th>RSF factor</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash, short-term unsecured instruments, securities with less than one-year residual maturity and with no embedded option that would extend maturity to more than one year, securities with exactly offsetting reverse repurchase transactions, less than one-year unencumbered loans to financial entities</td>
<td>0%</td>
</tr>
<tr>
<td>Unencumbered longer-dated sovereign/public sector securities having 0% risk weight under the Basel II standardized approach and with active repo markets</td>
<td>5%</td>
</tr>
<tr>
<td>Unencumbered AA-rated or higher longer-dated corporate bonds meet all conditions for Level 2 assets in the LCR Unencumbered longer-dated sovereign/public sector securities with 20% risk weight under the Basel II standardized approach, which meet all the conditions for Level 2 assets in LCR</td>
<td>20%</td>
</tr>
<tr>
<td>Unencumbered gold, equities on a major exchange not issued by financial institutions, non-financial corporate or covered bonds rated A+ to A-, central bank eligible and traded in deep and active market with low concentration</td>
<td>50%</td>
</tr>
<tr>
<td>Less than one-year residual maturity unencumbered loans to non-financial corporate clients, sovereigns, central banks and PSEs</td>
<td>50%</td>
</tr>
</tbody>
</table>
or an asset to be considered HQLA, it has to be high quality and be traded in a deep and active secondary cash and repo market, something which is absent and which is constrained by a hold-to-maturity preference among Islamic banks as a result of the shortage. This dilutes the central bank’s efforts to meet its objectives for monetary and financial stability on an equal basis for conventional and Islamic banks and opens up a regulatory arbitrage opportunity between the two sectors.

H.E. Dr. Al-Hashel concluded by commending the IILM on its high-quality short-term Sukuk whilst highlighting the need for further progress in appropriate liquidity management tools in addition to the IILM Sukuk and to designing ‘suitable liquidity regulations in line with the Islamic banking model.

After H.E. Dr. Al-Hashel’s presentation, H.E. Dr. Zeti added that the current environment with “extreme behaviour by the market caused by excess liquidity in markets and irrational exuberance” has made liquidity management challenges more acute. Whereas on the other end, panic behavior emerges when there are financial crises causing tightening of liquidity.

H.E. Dr. Zeti’s remarks were followed by the presentation of H.E. Al-Zadjali which began with the background that Oman is a newcomer to the Islamic banking sector.

“The current environment with ‘extreme behaviour by the market caused by excess liquidity in markets and irrational exuberance’ has made liquidity management challenges more acute.”

H.E. Tan Sri Dato’ Sri Dr. Zeti Akhtar Aziz
Governor of Bank Negara Malaysia

The cross-border operations of banks bring private liquidity into markets complementing the official sources of liquidity from the central bank.

As a result of these interlinkages between private and official liquidity, the former is highly cyclical as a result of divergences in growth rates, monetary policies and risk appetite. The spillovers from this cyclicity can influence financial stability depending on whether financial institutions dampen or amplify stimulus from central banks as well as their impact from creating their own liquidity which are reflected in either a process of leveraging or deleveraging.

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**NSFR required stable funding (RSF) factor (cont)**

<table>
<thead>
<tr>
<th>Type of exposure</th>
<th>RSF factor</th>
</tr>
</thead>
<tbody>
<tr>
<td>Unencumbered residential mortgages and other loans qualifying for 35% or lower risk weight under Basel II standardized approach</td>
<td>65%</td>
</tr>
<tr>
<td>Less than one-year residual maturity unencumbered loans to retail clients and small business customers other than those qualifying for the 65% RSF</td>
<td>85%</td>
</tr>
<tr>
<td>All other assets</td>
<td>100%</td>
</tr>
</tbody>
</table>

Source: BIS, EY

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**Minimum LCR**

<table>
<thead>
<tr>
<th>Jan-15</th>
<th>Jan-16</th>
<th>Jan-17</th>
<th>Jan-18</th>
<th>Jan-19</th>
</tr>
</thead>
<tbody>
<tr>
<td>60%</td>
<td>70%</td>
<td>80%</td>
<td>90%</td>
<td>100%</td>
</tr>
</tbody>
</table>

Source: BIS, EY

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During normal times, rising asset prices can ease credit constraints and induce greater risk taking while during periods of financial deleveraging there will be a similar effect in terms of economic retrenchment. During periods of stress, however, the interaction between official and private liquidity become more closely linked where global liquidity is affected by the private sector’s access to official liquidity. Three lines of defense are vital to promote financial stability:

- international cooperation between regulators;
- prudent policies for a vibrant and liquid secondary market in government securities; and,
- cooperative measures to provide liquidity in times of stress.

The effectiveness of the central bank’s policy will depend on the depth of secondary markets because the yield curve provides a key input to central bank policymaking. The process of building the yield curve begins with short-term government securities as well as creating a weekly liquidity forecast with government cash balances and the actions to be undertaken by the central bank.

As liquidity develops, confidence will grow as well, reducing transaction costs and improving risk allocation by refining the signal generated by the market’s perception of government policy, which can also allow for changes in the government’s financing when needed. The secondary market liquidity also provides a reference point for collateralized and uncollateralized deposit rates while providing information for the central bank to use when it sets repo rates for liquidity management.

Following the presentation by H.E. Al-Zadjali, H.E. Dr. Zeti highlighted the aspects of his presentation about the importance of financial infrastructure to support liquidity and the role that an active and deep domestic Sukuk market can play, particularly for Islamic financial institutions. This is a field, she said, where there is a lot of talent needed with experience in managing liquidity risks.

Professor Simon Archer asked about the specific importance for central banks accepting the IILM Sukuk as eligible collateral and highlighted the potential for this to confirm its status as a HQLA, particularly since the lack of trading and liquidity could lead to questions about its qualifications as a HQLA.

Brandon Davies mirrors Professor’s Archer remarks relating the liquidity issues of Central Banks and other securities will be acceptable if they are good stores of value rather than high liquidity instruments in a traded market.

African Development Bank representative, Dr. Bakri Musa Abdul Karim, emphasised on the need to build competent capacity in Islamic finance field in order to increase the interaction between conventional and Islamic banks.

H.E. Dr. Al-Hashel responded that a technical working group has been set up in Kuwait to decide that as far as whether the IILM Sukuk would qualify as a HQLA under Basel III, it would be up to individual jurisdictions as a result of the special nature of Sukuk and the scarcity of instruments for Islamic banks.

H.E. Dr. Al-Hashel strongly supports the IILM Sukuk qualifying as a HQLA since it is short-term and supported by the governments of the IILM members. Even though it has a tenor longer than 7 days the high quality means it should be accepted in the short-term bucket. He added that while there was not a deep secondary market yet, central banks should accept it as collateral because it is high quality. In response to the question from Professor Archer, H.E. Al-Zadjali said that usually government bonds would be eligible for discounting for liquidity provision but that he was not sure whether the IILM would qualify as eligible collateral for discounting. H.E. Dr. Zeti added that most members of the IILM have accepted the IILM Sukuk as eligible collateral and the IILM was considering adding a 6-month tenor and were
able to extend out to as long as 12 months or as short as 1
month. (Note: The IILM issued its first 6-month tenor Sukūk
after this Roundtable discussion, on Aug 25, 2014.)

Professor Datuk Rifaat provided additional detail on what
the IILM has done including testing the possibilities for different
tenors. As the IILM Sukūk was introduced into the market,
the yield premium and overall yield was disappearing. It had
existed at first because the IILM was new but now that the
outstanding value of Sukūk reached $1.35 billion and trading
activity increased from 3% of issued volume to 20% of issued
volume as investors became comfortable with the idea that if
they sold their holdings, they could replace it later.

The increased secondary market liquidity reflects the role
of the IILM Sukūk for liquidity not investment, which increases
trading relative to longer-tenor Sukūk. If the holder needs to
offload, they can sell and then replace later with new issuance
which they are able to do with less price risk as a result of the
shorter duration. The IILM conducted a study of longer-term
Sukūk and found that as expected they had a higher volatility,
a key reason why many treasurers avoid long-term Sukūk.

Abdoul Aziz Ba, an Executive Director at the IILM
added that the IILM had received growing demand from
primary dealers (PDs) including the conventional banks
that acted as PDs. Leon Koay, MD and Head of Global
Markets Malaysia at Standard Chartered Bank added that
as one of the PDs they looked at participation in the IILM
as a long-term agenda with a good start. While there are
many reasons why banks buy, hold or trade paper, at this
point a key factor is that demand far exceeds supply and
the IILM is reaching the point where awareness is increasing
exponentially with a doubling in the number of purchasers
and they are seeing very strong latent demand.

Further questions were asked by David Vicary Abdullah,
President and CEO of INCEIF, about the capacity of the IILM,
which H.E. Dr. Al-Hashel responded by highlighting that
the IILM philosophy is not to meet the entire need for Islamic
liquidity but that the IILM Sukūk could provide an international
benchmark for domestic Sukūk and other liquidity management
products like tawarruq. H.E. Dr. Zeti concurred and highlighted
the important role of private market participants facilitating
transactions to manage liquidity, particularly in the local currency
markets. She noted that while the IILM currently only provided
supply in US dollars, it was considering other international
reserve currencies going forward.
Session 2: Potential Market Developments of Liquidity Management

The clock tower at the end of Tunis’ Bourguiba Avenue is covered with the national flag, January 14, 2013 © REUTERS/Zoubeir Souissi

Current IILM primary dealers include Abu Dhabi Islamic Bank, AlBaraka Turk, Barwa Bank, CIMB Islamic Bank Bhd, Kuwait Finance House, Luxembourg’s KBL Private Bankers, Maybank Islamic Bhd, National Bank of Abu Dhabi, Qatar National Bank and Standard Chartered Bank
Speakers

**Professor Victor Murinde**  
*Director, African Development Institute – African Development Bank Group*

**Dr. Sayd Farook**  
*Global head Islamic Capital Markets – Thomson Reuters*

**Ms. Nida Fatima Raza**  
*Director Financial Services Advisory – Ernst & Young*

Professor Victor Murinde, session chair, started by highlighting that the need to identify the tools for Islamic liquidity management is just as important as identifying what tools are employed and the extent of their employment by Islamic financial institutions. The Survey on Volume and Depth of Liquidity Management Tools used by Islamic financial institutions conducted by Thomson Reuters Islamic Finance Gateway and the IILM pinpoints insights and information on the direction and tools employed by Islamic financial institutions across major Islamic financial jurisdictions.
Survey on Volume and Depth of Liquidity Management
Tools used by Islamic financial institutions

Dr. Sayd Farook began his presentation on the findings by clarifying how the financial crisis that swept through the Gulf and Asia have caused banks to withdraw from lending, forcing treasuries to become the only potential source of profitability. The trend continues, despite the fact that lending has resumed in full swing, as financial institutions are awash with cheap money. With global interest rates at a record low, the pressure for profitability is even higher now, as the survey findings show.

Scope of Survey
Between May and 30 June 2014, Thomson Reuters Islamic Finance Gateway conducted a survey of more than 40 Islamic banks and Islamic banking subsidiaries of conventional banks.

Objective of Survey
To assess the preferences, needs and profiles of Islamic financial institutions around the key Islamic finance jurisdictions.

Key Outcomes

<table>
<thead>
<tr>
<th>Primary Concerns for Treasurers</th>
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<tbody>
<tr>
<td>Profitability</td>
<td>Shari'ah Compliance</td>
</tr>
<tr>
<td>Liquidity</td>
<td>Credit Quality – A &amp; above / IG</td>
</tr>
</tbody>
</table>

Global instruments such as the IILM Sukūk programme are ideal in filling this gap and need further support to increase volume of issuances.
1. Survey geographical reach represents Islamic financial assets distribution

Survey Reach

- GCC: 50%
- Malaysia: 20%
- Other: 30%

Survey vs Islamic finance assets breakdown

- GCC: 41%
- Malaysia: 20%
- Other: 30%

The survey was distributed to a wide range of banks, both full-fledged Islamic and subsidiary, most of which are Thomson Reuters clients. The respondents are fairly representative of the universe of Islamic financial assets, with 50% of respondents from GCC, 20% from Malaysia and 30% from other countries.
2. Survey was distributed to decision makers in treasuries with a wide-range of geographic focus for their financial institutions.

- The respondents’ profiles were varied, but most were in senior treasury positions.
- The majority of respondents had an international or regional investment focus and only 19% were country-specific.
- The majority of respondents represented commercial banks, and only 18.5% represented the investment banking community.

<table>
<thead>
<tr>
<th>Respondents job role</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Senior Treasury Dealer</td>
<td>25%</td>
</tr>
<tr>
<td>Director / Head of Treasury</td>
<td>18%</td>
</tr>
<tr>
<td>VP Treasury</td>
<td>14%</td>
</tr>
<tr>
<td>Treasury Manager</td>
<td>11%</td>
</tr>
<tr>
<td>Deputy Treasurer</td>
<td>11%</td>
</tr>
<tr>
<td>Treasury Dealer</td>
<td>7%</td>
</tr>
<tr>
<td>Chief Dealer</td>
<td>7%</td>
</tr>
<tr>
<td>Treasury Consultant</td>
<td>4%</td>
</tr>
<tr>
<td>Head of Trading</td>
<td>4%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Geographical focus of respondents</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>International</td>
<td>37.0%</td>
</tr>
<tr>
<td>Regional - GCC</td>
<td>22.2%</td>
</tr>
<tr>
<td>Local - Country Specific Only</td>
<td>18.5%</td>
</tr>
<tr>
<td>Regional - Europe, Middle East and Africa</td>
<td>7.4%</td>
</tr>
<tr>
<td>Regional - South East Asia</td>
<td>7.4%</td>
</tr>
<tr>
<td>Regional - MENA</td>
<td>7.4%</td>
</tr>
</tbody>
</table>
3. On average, banks have 55% liquid assets available for investing. Malaysia has slightly more than other countries.

Average percentage of liquid assets available for investing or have invested

By type of bank

By region

When asked what percentage of assets they had in the liquid category, commercial banks interestingly had an average of 34% of liquid assets, while universal banks had a much higher percentage. GCC banks on average have lower percentage of liquid assets compared to Malaysian banks.
4. Malaysian banks have a slightly higher concentration of short-term assets perhaps attributed to their deeper product suite.

Average percentage of liquid assets available for investing

By type of bank

- Multinational Bank: 60% Short Term, 30% Medium Term, 10% Long Term
- Investment Bank: 50% Short Term, 12% Medium Term, 37% Long Term
- Universal Bank: 36% Short Term, 40% Medium Term, 24% Long Term
- Commercial Bank: 38% Short Term, 26% Medium Term, 36% Long Term

By region

- GCC: 46% Short Term, 23% Medium Term, 31% Long Term
- Malaysia: 51% Short Term, 22% Medium Term, 27% Long Term
- Other: 22% Short Term, 25% Medium Term, 52% Long Term

The findings show that multinational and investment banks have a higher percentage of short term assets, while commercial and universal banks have a lower percentage marking roughly 38%.

Malaysian banks have a slightly higher concentration of short term assets, possibly attributed to its deeper product suite and instruments available in the domestic market.
5. Currency preferences are mostly aligned with banks’ local currencies, with GCC banks preferring USD as they go further out on the curve.

Banks prefer their local currencies when investing on a short-term basis, the findings reveal. However, GCC banks have a higher preference for USD when investing on a short-term basis – given their USD-pegged currencies.

Malaysian banks however still prefer Malaysian Ringgit on the medium-term, representing the domestic orientation of the banks in the country and the cost of foreign exchange arbitrage.
6. Shari’ah compliance, liquidity and counterparty credit quality are the primary concerns of treasurers, the survey findings show.

There is consensus on the importance of Shari’ah compliance which was ranked as the highest priority for banks with respect to liquidity management. This could be attributed to the impact Shari’ah non-compliance can have on treasury profits, that is, any income generated deemed Shari’ah non-compliant needs to be donated to charity.

Unsurprisingly, the second and third highest priority was liquidity of their instruments / portfolio and the credit quality of the counterparty. Profitability was a close fourth.

Most of the banks however showed no concern over deploying the excess liquidity, presumably attributed to having available avenues to invest. In addition, findings show that respondents have no high concern over flexibility, tradability or quality of the instrument.

Hence, when structuring instruments, it is critical to emphasise on strict Shari’ah compliance, ability to liquidate positions and thirdly, factor in quality of the credit. Profitability is also an overwhelming aspect on the minds of treasurers.
7. Banks surveyed prefer placing their short-term funds with local Islamic banks first, then regional financial institutions and foreign Islamic banks, while international banks are ranked the lowest in preference.

Local Islamic banks were the highest preference, followed by regional financial institutions and foreign Islamic banks. Among the Islamic banks, a common interest is evident on the preference of investing either amongst the Islamic banks themselves or with regional financial institutions. Notably however, international financial institutions were the least preferred.

Preference for placing short-term funds

- Local Islamic banks: 24%
- Regional financial institutions: 17%
- Foreign Islamic banks: 16%
- Government backed entities: 16%
- Central bank: 15%
- International financial institutions (such as Standard Chartered / HSBC / Credit Agricole): 12%
8. **Sukūk, Mudarabah and investment Wakalah are the three most preferred short- to medium-term investment vehicles for both GCC and Malaysia.**

The findings show that Murabahah and Mudarabah, two most common treasury investment instruments, are in fact the most used modes when investing short- to medium-term funds. However, most showed preference in employing Wakalah and Sukūk for short-term funds. This indicates that treasurers don’t have the appropriate allocation of Sukūk.

Commodity Murabahah with a local Islamic bank or Islamic subsidiary was the third most preferred instrument when investing short-term funds. Commodity Murabahah has become a thorny topic across the GCC countries, after some scholars and bankers opined that it had been abused and, some say, perpetuates leakage, or the flow of Shari’ah-compliant capital to non-compliant investment activities.

### Currency preference when investing excess liquidity on a short-term basis

<table>
<thead>
<tr>
<th>Investment Method</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mudarabah with a regional Islamic bank</td>
<td>15%</td>
</tr>
<tr>
<td>Mudarabah with a local Islamic bank</td>
<td>15%</td>
</tr>
<tr>
<td>Investment Wakala with a regional or foreign Islamic bank or Islamic subsidiary</td>
<td>14%</td>
</tr>
<tr>
<td>Investment Wakala with a local Islamic bank or Islamic subsidiary</td>
<td>12%</td>
</tr>
<tr>
<td>Investment Wakala with an international bank or Islamic (e.g. HSBC, Standard)</td>
<td>11%</td>
</tr>
<tr>
<td>Commodity Murabahah with a local bank</td>
<td>10%</td>
</tr>
<tr>
<td>Commodity Murabahah with an International bank</td>
<td>9%</td>
</tr>
<tr>
<td>Investing in Sukūk</td>
<td>8%</td>
</tr>
<tr>
<td>Placing with the Central Bank</td>
<td>6%</td>
</tr>
<tr>
<td>Investment Wakala with a local Islamic bank or Islamic subsidiary</td>
<td>18%</td>
</tr>
<tr>
<td>Investing in Sukūk</td>
<td>16%</td>
</tr>
<tr>
<td>Commodity Murabahah with a local bank</td>
<td>13%</td>
</tr>
<tr>
<td>Investment Wakala with a regional or foreign Islamic bank or Islamic subsidiary</td>
<td>12%</td>
</tr>
<tr>
<td>Placing with the Central Bank</td>
<td>12%</td>
</tr>
<tr>
<td>Murabaha with a local Islamic bank</td>
<td>11%</td>
</tr>
<tr>
<td>Commodity Murabahah with an International bank</td>
<td>11%</td>
</tr>
<tr>
<td>Investment Wakala with an international bank or Islamic (e.g. HSBC, Standard Chartered etc)</td>
<td>7%</td>
</tr>
</tbody>
</table>
9. Commodity Murabahah remains a controversial topic among treasurers in different jurisdictions, but is more widely accepted in Malaysia.

Treasurers opinion on Commodity Murabahah as a means to invest excess liquidity

The survey findings clearly depict diverse opinions on the acceptability of Commodity Murabahah. In the GCC, 19% would rather avoid it. 19% believe it is operationally costly, another 18% have reservations due to liquidity, but since no other options are available they use the instrument. Lastly, 31% believe it is perfectly fine. This disjointed opinion hinders the growth of Islamic finance and relevant stakeholders must pursue common ground on the use of Commodity Murabahah. However, Malaysia is more dichotomous and 50% find it perfectly acceptable.
10. GCC Shari’ah boards are divided on Commodity Murabahah while Malaysian boards have no concerns

Interestingly, the majority of Shari’ah boards, i.e. 56%, are perfectly fine with Commodity Murabahah with only about 38% having issues with it. Notable among the issues are the proceeds going to conventional Islamic financial institutions. Region-wise, Malaysia is fairly acceptable, while GCC boards have a spectrum of opinions.

Institution’s Shari’ah Board’s perspective on investing through Commodity Murabahah or equivalent structures

<table>
<thead>
<tr>
<th>Perspective</th>
<th>By region</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fairly acceptable</td>
<td>GCC</td>
</tr>
<tr>
<td>Not allowed</td>
<td>Malaysia</td>
</tr>
<tr>
<td>Has reservations about proceeds going to Conventional IFs</td>
<td>Other</td>
</tr>
<tr>
<td>Other</td>
<td></td>
</tr>
<tr>
<td>Has reservations but is acceptable</td>
<td></td>
</tr>
<tr>
<td>Requested to avoid</td>
<td></td>
</tr>
</tbody>
</table>

0% 20% 40% 60% 80% 100%

- **Requested to allow**
- **Has reservations about proceeds going to Conventional IFs**
- **Has reservations but is acceptable**
- **Fairly acceptable**
- **Not allowed**
11. Shari’ah compliance remains the highest priority for treasurers but counter-party credit risk outranked liquidity as second highest priority when investing in short- and medium-term instruments.

Key priorities when investing in a short- and medium-term instrument:

- **6 - 12 Months**
  - Shari’ah compliance: 20%
  - Counterparty credit risk: 16%
  - Liquidity: 14%
  - Tradability: 13%
  - Capital protection: 11%
  - Efficient trading infrastructure: 10%

- **0 - 6 Months**
  - Shari’ah compliance: 19%
  - Counterparty credit risk: 17%
  - Liquidity: 16%
  - Tradability: 13%
  - Capital protection: 11%
  - Efficient trading infrastructure: 10%

12. All else being equal, most treasurers are now concerned about extracting maximum returns from excess capital with a secondary focus on liquidity and diversification.

What asset and liability / liquidity management issue is most on your mind?

- Maximize return from excess capital: 42%
- Liquidating my positions in case of liquidity shortfalls: 25%
- Diversifying my risk by investing across markets: 25%
- Finding shariah compliant assets': 8%
13. High preference for investment-grade papers while Malaysian banks require mostly A and above ratings possibly due to stringent capital adequacy requirements.

What types of counter-party risks are you able to accept as a minimum?

Based on your current capital adequacy, what kind of Basel III-based risk categories are you able to absorb on your balance sheet from investing your short-term liquidity?
14. Despite the projected growth in Sukūk issuance, the demand and supply gap will continue to exceed $200 billion in the near future.

PROJECTED SUKŪK DEMAND & SUPPLY LEVELS (2013 - 2016)

On the projection of Sukūk demand in the next five years, Dr. Sayd Farook pointed out that a Sukūk study conducted by Thomson Reuters and Zawya Islamic reveals that Sukūk demand will continue to outstrip supply by $200 billion even when accounting for a possible increase in issuance in the next five years.
Summary of key findings

- Treasurers desire investing in Sukūk, but they only have access to a small pool in which to do so, as shown by disparity between preferences and actual behavior.

- Commodity Murabahah is not widely preferred for a variety of reasons and most would avoid it if other options are available.

- Surprisingly, Commodity Murabahah with local banks are also preferred by many treasurers.

- Most banks show imminent need for high quality investment grade paper at the minimum, with Malaysian entities requiring 'A' and above possibly because of more stringent capital adequacy requirements and lower capital bases by percentage.

- Global instruments such as the IILM Sukūk are ideal in filling liquid instruments gap and need further support to increase volume of issuance.

- More work is required with the IILM to expand its issuance programme and enable it to issue in more significant volume and in larger number of jurisdictions than is what is currently available.
“Whilst profitability is important, credit quality and/or counterparty credit quality is amongst the most important issue for two main reasons: 1) Given the nature of short-term liquidity instruments, and 2) Regulations in light of BASEL, treasurers prefer zero-rated or 20% risk-weighted assets only, in order not to reserve much capital against instruments that do not confine with the latter preference.”

Ms. Nida Fatima Raza
Director Financial Services Advisory – Ernst & Young

When discussing how the lender of last resort and possibly conventional banks absorb some of the excess liquidity, Islamic banks rest on, a fundamental concern had yet to be appropriately addressed. Namely, most Islamic banks, particularly in the GCC region, still have excess liquidity without adequate tools to employ them on or lending excess funds to other Islamic banks, which in most, has excess liquidity. The profitability suffers subsequent to this liquidity loop, Ms. Nida Raza highlighted.

What conduits can be developed in order to channel Islamic liquidity in a Shari’ah-compliant manner, asked Ms. Nida Raza, to entities that require liquidity such as corporate or conventional banks? Commodity Murabahah may be acceptable by some, but Islamic banks are discouraged when Shari’ah scholars oppose such type of activity, Ms. Nida Raza continued. From an ethical perspective, it is generally known that conventional banks will ultimately funnel liquidity under Commodity Murabahah into their proprietary requirements, which essentially is not Shari’ah-compliant.

Lastly, flexibility was not chosen as a key concern, but when reverting to the liquidation of instruments, contracts such as salam and murabahah can only be traded at par value. Treasurers should have the option to trade either below par or above par as, Ms. Nida Raza said, flexibility is required in the contract structure.

Wakalah instruments are known to be employed by Islamic banks to absorb excess liquidity. Not only similar types of Wakalah instruments are required when Islamic banks inter-bank, but also cross-border regionally and internationally. Professor Murinde then opened the floor for discussion and Professor Datuk Rifaat, Chief Executive Officer of the IILM commented on Ms. Nida Raza’s suggestion in moving away from Commodity Murabahah. He clarifies how the IILM Sukūk issuance falls under a rated programme and not a rated institution. Part of the rating requirements of the IILM Sukūk programme is to have a liquidity support from ‘A1’ rated primary dealers. Currently, Al Rajhi is the only ‘A1’ rated Islamic bank, presenting a small capacity for Islamic banks. Hence, some Islamic banks confront an unavoidable necessity to turn towards conventional banks, at least in an interim ground. This may possibly help Islamic banks further embolden their infrastructure, be it liquidity management or other, until a conclusive infrastructure is uniquely developed for Islamic banks.
In reference to the presentation given by Dr. Sayd Farook, Mr. Abdoul Aziz Ba, Executive Director of IILM, enquired on whether the demand for Sukuk includes short- or long-term Sukuk. The projection for Sukuk demand was based on total assets of Islamic financial institutions, with an assumption that 30% would be invested in liquidity management instruments, said Dr. Sayd Farook. However, no distinction was made to identify whether demand is for short- or long-term Sukuk.

H.E. Hamood Sangour Al Zadjali, The Executive President of Central Bank of Oman, asked whether there is a legal—based requirement for the issuances of Sukuk, should it be in the form of regulation. In response, Ms. Nida Raza pointed out the importance of establishing a legal framework for Sukuk in order to encourage financial institutions and corporates to raise capital through this channel. However, as far as standardisation is concerned, Sukuk broadly have a standardised structure which can be adaptive. Setting standardised templates for structures such as Ijarah and others is impractical when the conventional side has no standardised templates yet demonstrates a highly successful experience. In addition, harmonisation is harder to achieve when templates and structures are based on different opinions and interpretation of Shari’ah. In conclusion, regulators should provide the same guidance on Sukuk and ensure emplacing a sound legal environment for Sukuk.

H.E. Murat Çetinkaya, Deputy Governor of the Central Bank of the Republic of Turkey, asked in reference to the survey that showed how treasurers prefer Shari’ah compliance and counterparty credit. This can be attributed to the short-term nature of these products, he said, meaning most tools treasurers employ for their short liquidity management purposes are via OTC products and not an organised market setting. Secondly, treasurers face the effect of lack of standardisation, forcing them to replicate conventional liquidity instruments.

Professor Datuk Rifaat, clarified a legal perspective on Sukuk. The IILM, mandated by its governing board, only allows sovereign assets. The key question is: would sovereigns permit selling local assets, whether financial or physical assets? The IILM portfolio mandates to have 51% tangible assets and remaining 49% to be intangible. Sovereigns are often not permitted to dispose of assets, including selling to a supranational institution so the IILM adopted the “temporary separation of ownership” instead. This makes it feasible because the assets remain owned by a local SPV, ownership of which is transferred to the IILM which concurrently rents the asset back to the sovereign. The issue that arose from the sale back is determining the price at which the asset is sold back. The Shari’ah scholars have ruled that it is permissible to sell the asset back at par.

H.E. Tan Sri Dato’ Sri Dr. Zeti Akhtar Aziz, Governor of Bank Negara Malaysia commented that entities should be issuing these short-term liquidity instruments; Bank Negara Malaysia issues such Ringgit-denominated instruments in order to fulfill the requirements of the market. The ideal situation would be to have central banks of different jurisdictions to issue such instruments, helping to establish unified multi-currency instruments. The story behind what the IILM has been introducing is five years of collectively conceptualising, setting up an international corporation that would be issuing this form of short-term instruments as only the U.S. supplies similar type of short-term instruments to the rest of the world. H.E. Dr. Zeti commented on how challenging it would be to have development banks contribute to this undertaking, mainly due to pricing and distribution. Central banks can distribute appropriately through primary dealers, who are usually other central banks.

Further elaboration on the idea behind having development banks issue short-term Sukuk, Mr. Ashraf Mohammed, Assistant General Counsel and Practice Leader – Islamic Finance at the Asian Development Bank said ADB do not usually lend in short-term, but tenors vary between 15 and 32 years. In addition, they often lend to countries in need of capital under a conventional basis, issuing at a low cost which then gets transferred to the country in need of capital. However, when studying to issue Sukuk to financial institutions that usually seek higher yields forces high pricing, a price that would be transferred to the countries the ADB lends to, making them reluctant to borrow at a higher cost.
In August 2014, the IILM increased its total Sukuk outstanding to $1.65 billion.
Speakers

H.E. Murat Çetinkaya  
Deputy Governor, Central Bank of the Republic of Turkey

Mr. Brandon Davies  
Non-Executive Chairman, Premier European Capital Limited

Mr. Muzaffar Hisham  
Chief Executive Officer, Maybank Islamic Bank

Summary

- Short-term funding requirements create a significant risk to all banks and the risk has been recognized by the LCR and NSFR requirements enshrined officially within Basel III.

- The EU faces a growing challenge of too scarce HQLA as governments commit to reduce debt but regulations push banks away from corporate bonds and into government paper.

- Banks in Asia face constraint from Basel III LCR and NSFR that forces them to compete with all other banks for the same pool of sticky, low cost deposits which pressures their net interest margins and ultimately raises the cost of finance for individuals and businesses.

Recommendations

- Regulators should be flexible to encourage a diversity of HQLA qualifying assets to mitigate the limitations caused by excluding non-sovereign assets.

- Islamic banking regulators should consider developing a Shari’ah-compliant version of self-liquidating trade bills as an alternative source of HQLA.

- Bankers should consider finding alternative sources of stable funding to limit the degree to which they compete on price alone to attract stable funding.
From a bankers’ perspective, global liquidity management in the current environment is focused on the evidence, since the Federal Reserve first considered tapering its asset purchases, that even liquid markets can become illiquid very quickly, said H.E. Çetinkaya. Short-term markets for wholesale funding present a particular risk even as Basel III liquidity ratios require banks to become more cautious. As many Islamic banks operate in fiercely competitive markets with limited liquidity management products, there will be financial stability issues for Islamic banking.

Within Turkey during the past five years, participation banks have seen growth at twice the rate of conventional banks and this has led regulators to focus on risks facing the Shari’ah-compliant banks. Central banks coming together to develop the IILM Sukuk product is a good solution to a problem facing the industry, something which H.E. Çetinkaya believes the roundtable will help to advance.

From this introduction which mirrored the comments earlier in the day from H.E. Dr. Zeti the discussion turned to the use of self-liquidating trade bills both in a conventional setting and also for Shari’ah-compliant banking, a point raised by Brandon Davies. He put the challenge facing Islamic banks into a broader context of one that is facing Europe which policymakers at the European Central Bank (ECB) and the Bank of England (BoE) explored in a rare joint discussion paper (PDF).

The problem lies in the large size of the Euro Area bank assets relative to GDP—currently 350% compared to under 100% in the US. The liquid asset pool that qualifies under Basel II and Basel III is shifting much more towards government bonds, drying up liquidity in the corporate bond market. Because securitization markets are less developed in the Euro Area, the result is banks holding mostly illiquid loans on their balance sheets and now far less liquid corporate bonds.

Holding government bonds of Euro governments exposes banks to variable credit quality and a high reliance on local...
central banks and the ECB refinancing facilities. If Euro-area countries conform with their long-term obligations to reduce government borrowing to 60% of GDP the amount of liquid assets will fall significantly. Relative to the present state, the government debt will be falling while GDP rises leading to an expansion of bank balance sheets while liquid assets fall and creating a liquidity problem that many Islamic banks would recognize:

- Lack of availability of suitable liquid assets to comprise stock liquidity AND
- A lack of liquid markets for asset backed/based securities (ABS) that can be used to manage balance sheet pressures.

One solution is the development of a Euro Bills market on which Graham Bishop addressed (in Session 6 of the Roundtable) while to others is the joint ECB/BoE initiative on securitization. The proposal would provide liquidity support to banks backed by “qualifying securitisations” leading to Central Bank eligible ABSs. These securitisations could include many things including SME debt but would have to be “simple, structurally robust and transparent”. One thing in particular they could not include is “synthetic” securitizations which contributed to the much higher rate of securitization defaults in the US (14%) compared to the EU (0.5%) since 2007.

Challenges exist including the high capital requirements for investors combined with sovereign credit rating caps in securitization rules under Basel III and CRD IV, the availability of loan level data (transparency), Basel risk weighting proposed for institutions covered by Solvency II, uncertainty about capital relief for bank issuers, high credit ratings required for providers of ancillary services (e.g., swaps, bank accounts) and the need for a liquid secondary market.

Following Mr. Davies’ presentation of options that the ECB and BoE are exploring to deal with limited non-sovereign high quality assets for liquidity management, Muzaffar Hisham discussed how Islamic banks manage...
their liquidity. After presenting an overview of the financing-to-deposit ratio in Maybank Islamic’s key markets, he discussed the scarcity of HQLA (particularly sovereign Sukūk in Asia-Pacific markets outside of Malaysia) and highly rated corporate bonds, as well as the challenge of low yields on the ones that do exist.

There has been some growth in HQLA and Sukūk more broadly as double taxation restrictions are removed. However, the liquidity requirement candle is burning from both ends as banks have to compete over the same pool of sticky, low from state-owned corporations, or possibly a multi-tier OIC central bank Sukūk.

Following Muzaffar Hisham’s presentation two comments followed questioning whether changing regulatory attitudes in Basel III towards corporate debt was frustrating efforts despite many corporations being safer than some sovereigns but still not being eligible as HQLA. Davies responded that this could persist for a while since they haven’t yet defined what a qualifying securitization is. Hisham added that there was significant information provided by an efficient market and that to some degree we should “trust the market”.

Another comment raised an issue with the idea of self-liquidating receivables from a Shari’ah perspective. Because most would represent receivables, they may be only eligible for trade at par which would limit their use as a liquidity asset. Davies responded that an important aspect of the proposal would be its ability to provide an opportunity to develop a Shari’ah-compliant asset that would also be

Mr. Brandon Davies talking with delegates at the sidelines of the Islamic Liquidity Management Roundtable
Session 4: The International Islamic Liquidity Management Corporation

The IILM Sukūk is a Shari’ah-compliant, US Dollar-denominated short-term instrument rated A-1 by Standard & Poor’s Rating Services which are backed by sovereign assets.

Kuala Lumpur’s skyline is seen during sunset June 15, 2009 © REUTERS/Zainal Abd Halim
Session 4: The International Islamic Liquidity Management Corporation

Speakers

Mr. Daud Vicary Abdullah
President & Chief Executive Officer, International Centre for Education in Islamic Finance (INCEIF)

Professor Datuk Rifaat Ahmed Abdel Karim
CEO, International Islamic Liquidity Management Corporation (IILM)

Mr. Juan De Mollein
Managing Director, Lead Analytical Manager EMEA, Standard & Poor’s

Mr. Leon Koay
Managing Director & Head Global Markets Malaysia, Standard Chartered Bank

Summary

◊ The IILM Sukūk help deal with some liquidity management issues, but there remain significant challenges in Shari’ah alignment and resolving tax issues for Sukūk in many countries

◊ The IILM’s Sukūk programme (not the IILM itself) is rated A-1 and uses an asset-based commercial paper (ABCP) structure adapted for Islamic finance needs

◊ Primary dealers provide for the liquidity needs of the programme which means any primary dealers must also have a high credit rating (A-1 or higher)

◊ Designed to meet the need filled in the conventional banking industry by US Treasuries

Recommendations

◊ Provide investors and central banks with education on the working of the structure to build confidence to expand programme and increase its use to meet HQLA needs in countries with Islamic banks

◊ Use the simple structure which is backed by long-term financing for projects in the IILM member countries to provide Islamic banks with more HQLA options within local markets
In his introduction to the final session on the first day of the IILM Roundtable on Liquidity Management, Daud Vicary Abdullah put the institution’s progress in the context of the development of Islamic finance globally where the depth and breadth of the market has been expanding rapidly. However, the industry still faced issues in addition to the liquidity management instruments that the IILM Sukūk help to alleviate including Shari’ah alignment and dealing with important tax issues in many countries. However, the industry must still meet its long-term goal of efficient and effective mobilization of capital for the development of the real economy.

The introduction was followed by Professor Datuk Rifaat providing an overview of the IILM whose shareholders are nine central banks from around the world and a multilateral organization, the Islamic Development Bank (IDB) Group. He began by covering the existing instruments in the market for short-term liquidity management including central bank Sukūk, Commodity Murabahah, interbank Mudarabah and Wakalah and Islamic repo which has limitations in terms of currency, tradability, ratings and counterparty risk.

With this background, he presented the IILM which is not rated itself but which has a rated Sukūk programme that offers an alternative with more desirable characteristics for financial institutions than the other options. The programme itself is an asset-backed commercial paper (ABCP) which has been adapted to the specifications of Islamic finance. The programme can only hold sovereign assets with a rating of at least A or higher, 2% time reserved and the ABCP benefits from a commitment up to the size of the programme from its primary dealers who must be rated at least A-1.

The programme, which has $1.35 billion currently outstanding, is rated A-1 by Standard & Poor’s Rating Services and is the first tradable, Shari’ah-compliant, US dollar-denominated financial instrument under one year. Since the first issuance in August 2013, a total of $7.64 billion has been issued or reissued at auctions, as of the time of the Roundtable. The Sukūk are money market instruments backed by sovereign assets and are tradable globally through the primary dealer network and which are expected to qualify as HQLA under Basel III standards.
and will receive favorable regulatory treatment by the IILM member central banks, most of which have said the IILM Sukūk are eligible securities.

In concluding his presentation, Professor Datuk Rifaat said that the IILM Sukūk provides a complete golden triangle; in its role in providing financial stability it plays a role in both economic development and debt management for its member countries. Juan De Mollein of S&P followed with a description on the rating side of the IILM programme which focused on the ABCP vehicle for the risks associated with its long-term assets funded by short-term Sukūk.

The primary dealers allows the vehicle to go through longer periods of time without losing funding access since the primary dealers are obligated to purchase Sukūk and are required to have the same A-1 rating as the IILM programme. The underlying assets also protect it because they are from sovereign entities and must be ‘A’ rated and if they fail to be, they can be substituted for assets that do meet the requirements.

In the session’s final presentation, Leon Koay highlighted that the IILM Sukūk was designed to replace US Treasury bills which are a widely used tool for liquidity management.

Professor Datuk Rifaat speaking on the sidelines of the Islamic Liquidity Management Roundtable

“The IILM Sukūk provides a complete golden triangle; in its role in providing financial stability it plays a role in both economic development and debt management for its member countries”

Professor Datuk Rifaat Ahmed Ahmed Abdel Karim
CEO, International Islamic Liquidity Management Corporation (IILM)

Currently there is no similar Shari’ah-compliant alternative which is what the IILM set out to provide. A challenge facing the IILM is that, unlike the Federal Reserve, it does not have the ability to print more dollars if there is a supply issue which led to the ABCP approach including the liquidity support provided by the primary dealer network.

Under the primary dealer/ABCP structure, the IILM does not rely upon liquidity support from its members and stakeholders to give it a central bank-like structure without explicit support in the form of a blank check from central banks who would not be willing to provide such a
guarantee. The role of Standard Chartered as a primary dealer came from the bank’s overlapping presence with the member countries (it overlaps all except Luxembourg) across the 20 markets where Standard Chartered provides a primary dealer-type function with national central banks.

This role differs from the typical corporate relationship because the bank understands the expectations of the central banks, with which there is not always a full written agreement of every facet of the relationship. One difference in the IILM Sukūk was having the primary offer act as liquidity providers, a change from normal Sukūk structures but one consistent with the idea that ‘new solutions require new thinking’. A part of this new thinking is education for the end investors as well who took a wait-and-see approach to the paper but became much more interested after the first reissuance in November 2013.

The roundtable participants had several questions beginning with the key risks to the Sukūk and whether the credit risk analysis performed by S&P differed on the basis of the central bank involvement. De Mollein replied that the methodology was the same although it was a more complex application of the credit rating methodology because most ABCPs have a single liquidity provider while the IILM ended up with seven and has nine today. While the A-1 rating means the same as any other A-1 rating, it was a more difficult analysis process particularly in the legal side and the process took one year where a less complicated ABCP rating would take one month.

De Mollein added that the simplicity of the structure was the beauty and using the ratings of counterparties helped particularly since there were multiple counterparties which added resilience to changes in liquidity providers’ ratings. In addition, there is a credit risk assessment of the underlying assets prior to their addition which means that as the institution expands it will benefit from greater diversification of its assets. Koay added that the IILM is viewed as a quasi-sovereign institution since it is backed by multiple central banks, which is unique. However, this required more understanding about the sovereign’s willingness to pay and if they had approached the credit demonstration process like they would with a corporate, the Sukūk would not have happened.
The IILM programme can only hold sovereign assets with a rating of at least A or higher. 2% time reserved and the ABCP benefits from a commitment up to the size of the programme from its primary dealers who must be rated at least A-1.
Session 5: Legal, Shari’ah and Regulatory Aspects of Liquidity Management

Islamic Liquidity Management 2015

Speakers

H.E. Sultan Bin Nasser Al Suwaidi
Former Chairman of the IILM Governing Board and Governor, Central Bank of the United Arab Emirates.

Datuk Dr. Mohd Daud Bakar
Chairman of the Shari’ah Committee, IILM

Mr. Kenneth Aboud
Partner, Allen & Overy LLP

Professor Simon Archer
Visiting Professor, University of Reading

Summary

◊ Use of Sukūk by Islamic financial institutions is limited by the lack of use of these instruments by central banks in their open market operations, limited trading and settlement systems and in some cases, a lack of regulatory clarity on their treatment.

◊ International bodies will lead the way to develop globally accepted products and to provide operational and legal simplification for their issuance to lower cost to other issuers.

◊ Significant challenges emerge from permissible actions by sovereigns which are often constrained by procurement rules, ability to sell assets, and in many civil law jurisdictions, a lack of a law allowing a trust structure used in most Sukūk.


Recommendations

◊ Countries that have not harmonized the tax treatment of Sukūk with conventional bonds should start with this because it represents a key barrier to issuance.

◊ More international development banks representing a variety of regions and targeting different investor bases should issue Sukūk to provide globally accepted structures for use by governments and central banks.

◊ Central banks should permit multilateral development banks and government-issued Sukūk to be used in repo markets to increase liquidity and consider whether they can also be used in open market operations.
The second day opened with an introduction by H.E. Al Suwaidi who highlighted some of the areas covered in the previous day including the importance of liquidity management for the effective functioning of financial institutions. The challenge facing Islamic financial institutions is wider and H.E. Al Suwaidi grouped them into six areas. On the legal and Shari’ah side, the vast majority of tools used for liquidity management like Commodity Murabahah, repo and Commodity Murabahah alternatives are questionable for Shari’ah scholars. These products are also unnecessarily complex, costly and have legal uncertainties that expose Islamic financial institutions to risks not facing conventional banks.

With these challenges associated with the limited products currently available, there are also technical challenges in sovereign alternatives in many countries and too few high quality sovereign assets which could be used to structure a Sukūk. On the international level, there exist Shari’ah challenges associated with finding a generally acceptable structure for the underlying asset pool as well as short-term Sukūk issued from the asset pool. These challenges direct attention to the ongoing problems within Sukūk more broadly which compound the short-term shortages as a result of an unavailability of secondary trading and repo markets which leads to the buy and hold mentality for the limited supply of highly liquid assets.

Within the few countries that do have significant Islamic finance assets and Sukūk their central banks may not currently be using Islamic government instruments in liquidity operations and many countries lack effective trading and settlement systems, or may have limited regulatory guidance and incentives, or a combination of these problems. Globally there are varying product structures and suboptimal market development. International bodies are essential to help develop globally-accepted products to provide operational and legal simplification to lower costs.

With the backdrop of these issues and the rapidly changing environment for Islamic banks, talent development has become more important. While some institutions are offering Islamic finance training that will eventually lead to this pool of talent, it takes time while the continued internationalization and deployment of technology in finance has increased the skills required in the industry today and heightened the need for long-term research to promote future innovation.
Following H.E. Al-Suwaidi’s presentation Kenneth Aboud presented an overview of the legal issues that arise when structuring Sukūk, many of which are common between short- and long-term Sukūk. In the IILM case, the structure involves primary dealers and short-term Sukūk issued by an SPV trust holding interest over several long-term assets (long-term Sukūk) sold to it by the central banks. In considering this structure, issues arise about how well Sukūk will fit into laws regulating sovereign actions, tax, and securities. One of the factors that helps issuance is that in most common law jurisdictions, it is possible to separate legal and beneficial ownership. This is not possible in civil law jurisdictions so a separate law (like, for example, in Indonesia) is required to allow Sukūk issuance.

Even where the laws are able to accommodate Sukūk, there are challenges to Ijarah Sukūk if the government doesn’t have sufficient tangible assets without encumbrances. There may be political or legal rules that limit the government’s ability to sell assets, or there may be conditions set down under procurement rules, negative pledges and limitations placed on the investors’ recourse to sovereign assets. In most cases, investors are provided just a claim against the government which raises issues of sovereign immunity and the rights of investors. The ongoing legal struggle involving Argentina provides an example of the importance of the documentation behind sovereign issuance.

Other areas of importance for sovereign issuance are the issue of taxes which has been widely discussed where transfer taxes or stamp duties make Sukūk less advantageous than conventional bonds. To put conventional and Islamic issuance on an equal footing, many of these taxes would have to be waived or otherwise removed for the purposes of Sukūk offering. In addition, a new issuance also has to factor in the enforceability of the purchase undertaking and issues with insurance of the underlying asset. In general, issuance through private placement is easier in international markets. Regulation S provides a widely used exemption to some disclosure requirements under US laws but limits the participation of US investors whereas issuing under Rule 144A opens this market but has stricter disclosure and due diligence requirements.

After the comprehensive overview provided by Mr. Aboud, Shari’ah scholar Datuk Dr. Bakar shifted towards the tensions between conformance with the HQLA requirements under Basel III and the preferences for Shari’ah compliance. From the ratings perspective, credit enhancements can help make the asset be rated as higher quality through a number of ways including parent guarantee, third-party guarantee, or subordination where the Sukūk is more senior to other debt. While Commodity Murabahah offers an easier option as a debt product, it is difficult to get stakeholders around the world to accept it and its non-tradability makes it relatively inflexible for liquidity management.

The structure with a wakala backed by longer-term assets funded by short-term Sukūk is a viable structure, and Commodity Murabahah can fit in quite well in some circumstances. A Wakalah Sukūk with a combination of Ijarah and Commodity Murabahah assets as the underlying assets is easier and helps to manage the limitation in the quantity of tangible assets available. There is still disagreement on the required ratio between the commonly used 51% tangible asset threshold and the minimum requirement of 30% under AAOIFI rules.

When structuring the Sukūk, it is important to be aware of the differences including a minority opinion of scholars who require the ratio to be maintained throughout the tenor. The majority of scholars only require the ratio to be met at the point of issuance. In addition, there needs to be assurances that any of the Commodity Murabahah transactions are authentic and there are no fictitious aspects in order to satisfy Shari’ah scholar requirements for a genuine Commodity Murabahah transaction.

“There needs to be assurances that any of the Commodity Murabahah transactions are authentic and there are no fictitious aspects in order to satisfy Shari’ah scholar requirements for a genuine Commodity Murabahah transaction. Governments may also find opportunities for the government to use murabahah transactions instead of tawarruq transactions that can be securitized alongside the tangible assets in a Sukūk offering”

Datuk Dr. Mohd Daud Bakar
Chairman of the Shari’ah Committee, International Islamic Liquidity Management Corporation (IILM)
The final presenter, Professor Simon Archer, continued on some of the issues with Basel III compliance raised earlier and began by highlighting that the 3-month tenor of the IILM’s first issuance was popular because under accounting rules it meant that holdings of these Sukūk could be counted in the cash equivalent securities. This is important to Islamic banks, many of which are holding excess liquidity that is not generating income.

If there were more assets that qualified as HQLA, Islamic banks would like to shift their funds from cash, but those available today have limitations that prevent them from qualifying towards the HQLA requirement and so they remain in cash and non-income generating deposits with the central bank. Within the HQLA categories, three categories (Level 1, Level 2A and Level 2B) have different haircuts and limitations of how much can be used to count towards the total HQLA requirement based on credit quality, liquidity and price stability. The Level 2B are particularly unhelpful because they have a relatively low maximum level allowed and also because they have a steep haircut.

As the rules are written currently, Level 1 HQLA can only be sovereign or quasi-sovereign issuances. It seems to be rather arbitrary but at the moment the restriction doesn’t have practical effect because corporates don’t issue much short-term high quality paper today. If they did and a Shari’ah-compliant alternative could be created, this restriction would be “irksome” and would prohibit some otherwise very high quality corporates from issuing into the large market demand from liquid Islamic banks.

Delving further within the HQLA requirements, Professor Archer discussed the challenges on the liquidity side as well which, under the Basel rules, are challenging for the IILM Sukūk because they were not written with a newly introduced instrument in mind. Level 1 and 2A requires a proven record of liquidity as a reliable source in stressed market conditions.

The liquidity requirement’s limitation on market maker concentration is challenging for Sukūk even where they would otherwise meet price volatility rules and eligibility for central bank liquidity facilities is “highly desirable”. There is not a good benchmark currently for the pricing of short-term Sukūk, but the starting point probably could be the 90-day
T-bill and adjusting for quality (probably quite small) and liquidity (which may be larger). It appears that the Sukūk have been underpriced because they appear to be priced based off of longer-tenor Sukūk.

In response to a question from a participant, Professor Archer noted that there is accommodation in the Basel rules for Sukūk but it was not substantive and would likely only apply to Level 2B requirements. The IILM Sukūk solves some of the issues, but it can only meet part of the excess demand for HQLA.

Whereas a corporation that faces a barrier to issuance in one market has the option of finding a more facilitative market, the sovereign has to work within the laws in existence in its own jurisdiction. In response to a question about the priority of Shari‘ah and the Basel requirements, Datuk Dr. Bakar said that in a conflict between the Basel rules and Shari‘ah, Basel III would take priority but they were in conversation with the Basel committee to consider flexibility on this issue.
Session 6: Potential Market Developments of Liquidity Management

Islamic Liquidity Management 2015
Speakers

Sir William Blair
Justice of the High Court, Queen’s Bench Division and President of the Board of Appeals of European Supervisory Authorities

Mr. Lawrence Oliver
Deputy Chief Executive Officer, DDCAP Limited

Mr. Graham Bishop
Consultant on European Union Integration

Dr. Adnan Chilwan
Chief Executive Officer, Dubai Islamic Bank

Summary

- The development of liquidity management for Islamic banks has been dominated by bilateral contracts used for asset financing, not enough for proper treasury management purposes.

- Trade bills should be considered as an option for Islamic banks as they have a long history in conventional banking, and overlaps with the idea of tying Islamic banking to the non-financial economy although Shari’ah issues remain.

- Presentation showed structure for international cooperation within the Euro area using an issuance of matched bills among countries in ‘good standing’ to provide EU-wide market-based benchmark.

Recommendations

- Continued work to build a repo market and find an acceptable structure to the majority of the market is important and must be done before it is needed in a crisis.

- Consider the role which Shari’ah-compliant trade bills could fill the need for short-term instruments for liquidity management.

- Regulators should find opportunities to broaden availability of cross-border financial markets infrastructure to allow Islamic banking and finance to capture the benefits of internationalization.
The final session of the Roundtable began with a return to the interbank markets with a perspective from Lawrence Oliver, whose firm is involved in many of the interbank Commodity Murabahah transactions that provide the limited options to date for Islamic banks to manage their liquidity. He highlighted the challenge from the lack of market infrastructure which includes very limited access to a lender of last resort. Despite these weaknesses, Islamic banks have shown themselves to be resilient and reaching their current emergent stage without active Islamic money and capital markets.

The historical picture of Islamic money markets and wholesale liquidity has been one dominated by bilateral contracts that are more relevant to asset financing requirements than treasury management. The development of structures has been reasonably efficient, it has involved complexities that extend the timelines associated with the products and introduced operational, settlement and counterparty risk and added cost from the involvement of third parties.

Since 2000, there has been a parallel capital market in the form of Sukūk that have developed but there are not enough tradable Sukūk assets. There are some Islamic liquidity funds which since 2008 have increasingly tried to act as the Shari'ah-compliant equivalent to conventional AAA-rated money market funds and some are rated. Due to the limitation on eligible securities, the offerings provided by money market funds do not always match up with the liquidity management needs of banks and other Islamic financial institutions. One of the complications in the development of these funds is that there still exists limited tradable Sukūk with a low enough volatility to meet their investor requirements so these funds are overweight in murabahah contracts.

Despite these complexities, Commodity Murabahah has remained a reliable product for short-term liquidity management despite criticisms it must be ‘real’. One such
The change made to the documentation is the stipulation that physical delivery has to be available to the client, which can and is tested both as part of the diligence process but also in actuality with some clients requesting physical delivery. In addition, DDCAP’s own Shariah board is able to inspect the physical assets for transactions where DDCAP is involved.

DDCAP has evolved and focused on developing more automation of process and electronic platforms have been a demand from its clients. In the process, they have consulted with Shariah scholars to build a reliable online platform which is widely used. Among the requirements from the Shariah scholars was that only commodities purchased from DDCAP were done through DDCAP systems. The other legs of the transaction with other brokers had to be done through their own platforms.

In addition to the operational challenges of meeting their liquidity management needs, Islamic banks will operate at a disadvantage as they have to meet the same liquidity requirements as the conventional banking system because of the scarcity of sovereign Sukuk. In the UK, for example, the Islamic banks have only a very small supply of GBP-denominated HQLA from recent UK sovereign issuance.

In the absence of enough GBP-denominated HQLA, the regulators permit Islamic banks to hold IDB Sukuk which is AAA-rated but USD-denominated which introduces the forex risks should a systemic crisis affect FX markets.

Despite the steps taken to date to provide Islamic banks with Shariah-compliant alternatives to meet their requirements, more is needed to satisfy the ever-increasing appetite from the Islamic finance market. For example, there will need to be further sovereign issuance to counter the investor tendency to buy and hold to maturity since it is eligible for both conventional and Islamic investors which has created additional shortages. Outside of Malaysia, there has been limited development of infrastructure Sukuk which could be suitable for Islamic banks. In some countries further development could come from allowing for Islamic banks to park reserves in interest-free reserve accounts with the central bank to provide a safe place for banks to place their funds.

One way to expand would be through the revisiting of trade bills and while some Islamic banks have visited this issue, there are some Shariah points remaining to be addressed. Many central banks also offer standing...
financing for conventional banks through repo transactions, but despite work towards creating a Shari'ah-compliant alternative, this is an area that needs significantly more development.

Following Lawrence Oliver’s presentation on Commodity Murabahah and alternative Islamic finance products, Graham Bishop provided an overview of a proposal the ECB is considering for a Temporary Eurobill Facility (TEF) as a case study of how other situations involving limited liquidity products are adapting and finding solutions. The motivation for this plan is the distinction between the banking union in the Euro area without a capital markets union. There is currently no Euro-wide HQLA that gets a zero risk weighting under Basel III.

The solution he describes is a proposal for bills of maturity up to two years issued by a Euro-wide fund that invests in matched bills from Euro area governments in ‘good standing’ (where there is no credit questions) to provide a euro-area asset and a benchmark for short-term interest rates. On the latter outcome, it works better than benchmarks like LIBOR because it wouldn’t be susceptible for inflated or deflated rate submissions.

The TEF, if it were put in place would require modest capital callable from the member states of the TEF but the capital requirements would be reduced by its own bills being short tenor and matching the tenor of the national assets it buys. Yet it could offer significant capacity. If it bought every available bill from Eurozone member countries, it would have about €2 trillion in capacity compared to €3.1 trillion in the US Treasury markets. It would also assuage concerns about national sovereignty by remaining as a temporary institution that would not take control of national budgeting and could stop issuance at any time and would runoff naturally within two years if wound down.

While no agreement is in place to launch the TEF, it could be done relatively easily with Germany’s approval. It would only include countries that other members believe are credit-worthy. The first loss position would come from the European Stability Mechanism (ESM) which would pay off member country T-bills if a country defaulted, which is callable as needed. The largest four countries that would be members would together account for about 80% of the total capital which could easily be able to meet the needs of smaller countries.

“Beyond the national central banking focus on domestic markets, there is also an international, cross-border liquidity challenge in response to which the IILM has emerged as an important player but not one that will be able to solve all of the related issues”

Dr. Adnan Chilwan
CEO, Dubai Islamic Bank

The final presentation of the IILM Roundtable was delivered by Dr. Adnan Chilwan who provided a summary of the liquidity management issues facing the Islamic finance industry. He highlighted the challenges that come because the “liquidity we thought we had, we hadn’t”. The changing of perceptions about how the market behaves under stressed conditions such as the freezing of third party repo markets during the financial crisis of 2008 forced a rethink of the global regulations around liquidity.

He questioned, however, whether the only liquidity risk was a deficit of liquidity and asked whether a surplus of liquidity that is found with many Islamic banks should lead central banks to take an investor of last resort role. Beyond the national central banking focus on domestic markets, there is also an international, cross-border liquidity challenge in response to which the IILM has emerged as an important player but not one that will be able to solve all of the related issues.”

Dr. Adnan Chilwan at Session 6 during the Islamic Liquidity Management Roundtable
markets, there is also an international, cross-border liquidity challenge in response to which the IILM has emerged as an important player but not one that will be able to solve all of the related issues.

As markets have recovered from the crisis and loan growth accelerated, Islamic banks have remained well-capitalized which will next be put to the test from ambitious infrastructure needs to support the Expo 2020 in Dubai and the FIFA World Cup to be held in Doha, Qatar in 2022.

As a result of these and other infrastructure needs, there has been a growing issuance of sovereign Sukūk. Part of this issuance growth is recognition that by tapping Sukūk markets, it is possible to reach a wider market (as evidenced by the huge oversubscriptions for recent issuance, even of unrated issuers) whereas conventional bond issuance excludes Shari'ah-sensitive investors. Some of this issuance has pushed out to previously untapped tenors in order to minimize asset/liability mismatches.

The roll out of Basel III rules, including the NSFR and LCR requirements will challenge banks and some estimates put the capital shortfall across all GCC banks at $27bn by the end of 2017. Some banks, including Islamic banks, are moving early to meet their future capital needs through various Tier I and II structures that are in compliance with Basel III rules coming into force in the coming years.

On other issues, there is still room for improvement. Dr. Chilwan specifically highlighted limited options in credit-linked notes and repos (repurchase agreements). On the repo issue, despite work over the years to develop a consensus structure, there has only been limited use but rather than wait for a future crisis, it was incumbent upon Islamic banks and regulators to develop and make sure the repo alternative works now, while times are good.

To close his presentation and the roundtable, Dr. Chilwan highlighted the need for more cross-border cooperation to work on liquidity management issues. Financial institutions are currently more comfortable working with domestic counterparties, but in the future there will be more internationalization with, for example, Middle Eastern banks looking to Asia and Asian banks looking to Africa. He placed the task of pushing these cross-border links with regulators who can develop coordinated instruments to facilitate the deepening of cross-border liquidity markets by financial institutions.
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Roundtable Leadership and Management

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