From the Editor

Investment markets have returned in many cases to heights previously achieved, following the interruption and uncertainties associated with the US’s monetary tapering plans. As the situation in Ukraine appeared to be contained, while still threatening, investors in April and May turned increasingly confident again.

Stocks and bonds showed renewed strength that surprised analysts, who have expected the anticipation of a tightening policy cycle to lead to a degree of caution and rising yields. It seems the hunt for income trumped those concerns, logically in a sense, as the idea of inflation returning renders cash an even more unrewarding vehicle.

In this edition we document those trends once again, accounting for surging indices in the Gulf, especially Dubai, the revival of sentiment among certain Asian bourses, subject to political variables, and even the evidence of pick-up in copper prices, said to be a reliable indicator of the state of the world economy. We enter a note of caution too as to further market exuberance.

Besides offering our digest of news in the Islamic finance sector, and regular review of sukuk offerings reaching the market, we again carry feature and viewpoint pieces, highlighting developments in the industry in various locales. This time we spotlight the sector’s stuttering progress in Tunisia, and the merits that London claims in making its pitch for a share of what continues evidently to be a growing business.
Africa: This massive continent shows understandably considerable potential for growth by the Islamic finance sector, whether in the Northern region as a constituent of MENA or Sub-Sahara. Despite the already substantial Muslim populations of, for instance, both West and East Africa, at present the industry is described as still in its infrancy. However, that is steadily changing, and Shariah-compliant assets are now reaching 10% of total in several countries. While central banks are working with counterparts to help develop the sector further, in some cases there remain political hurdles to cross.

London: The UK’s financial fulcrum, the City of London, vies perennially with New York for global leadership as a hub for conventional finance and trading, but is taking on the mantle of advancing Islamic finance as well, heading rivals on the European continent. Besides the open-door attitude of the authorities towards adding to the range of services offered, as an international centre, there is a case to be made for the benefits of both the English language and legal principles and framework as supporting factors in this strategic development, underlined by the expertise of the practitioners concerned.

Global Stocks: Recent trading has exhibited a sweet spot in the equity markets, encouraged both by extended recovery signs in the world’s locomotive still, the US, and the insistence nevertheless of the Federal Reserve that it will maintain monetary accommodation for a period prolonged enough to ensure that the rebound in activity is not curtailed. At the same time, inflation has not reached proportions to scare investors. The knock-on effect has been clearly seen across other bourses, although there are grounds to be wary of complacency, particularly as retail players are attracted towards apparent price momentum.
Bahrain’s rules for Islamic advisory firms

This month Bahrain’s central bank announced the finalisation of rules for the supervision of Shariah-compliant advisory firms. These would help small Islamic finance institutions and fund managers outsource the process of reviewing whether their activities are compliant with Islamic principles. The central bank is also set to release a new regulatory framework for Islamic insurance, and is studying changes to rules for Shariah-compliant financing arrangements which can be offered to accredited investors.

Source: Reuters, May 19th

GOLCER finds this regulatory support as emerging from the country’s wider overhaul of standards as the Gulf state steps up its efforts in Islamic finance. Bahrain pioneered Islamic finance -- with the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) being established in the early 2000s -- and currently competes with other centres such as Dubai, London and Kuala Lumpur for the sector’s business. Traditionally, Islamic banks have set up their own internal Shariah boards to rule on whether activities and products follow religious principles. The new rules’ promotion of the outsourcing concept is expected to enhance Islamic financial institutions’ operations and reduce the costs of such services.

Africa is offering strong growth options

In several East and West African countries there is a high growth opportunity for Islamic banking products, these markets being home to large populations of Muslim residents. Nigeria has the largest such segment in Africa, with around 80m people. Across Sub-Saharan Africa, the number of Muslim residents is expected to grow by 37% to over 386m by 2030.

Still, while Islamic banking assets have grown rapidly around the world to stand at more than $1.3 trillion at the end of 2013, the industry has remained in its infancy in Africa. This position is now changing, with Islamic banking looking to account for up to 10% of total banking assets in five or six Sub-Saharan African countries by 2020, including Kenya and Nigeria.

Governments and regulators in many African countries in Africa no longer view Islamic banking as a niche industry, but actively support and encourage local Islamic banking products to aid economic growth. Also there is a growing awareness of the significant liquidity source available through issuing Islamic bonds, arising across the Middle East, for funding crucial infrastructure investment. (See Focus box.)

Central banks from several African countries, including Nigeria, Tanzania and Uganda, are already working with more mature Islamic banking markets to gain experience and knowledge for the benefit of their respective markets.

Source: Khaleej Times, May 18th

GOLCER perceives this flourishing of the industry in Africa as representing a clue for the continent’s banking sector as a whole, not just the region’s large Muslim populations. Islamic banking is moving now to more market-based instruments to provide wider choices for all consumers, but on a Shariah-compliant basis. African domestic investors are becoming more informed about the value in choosing their bank in accordance with their faith, particularly after the failure of conventional banking to mitigate the financial crisis of 2007. We expect a fast-growing future for the industry, with the service gap between
Islamic and conventional banking narrowing and as the Islamic banking range of products develops and becomes more sophisticated. That Islamic banking is currently appealing to non-Muslim clients is more evident in the Middle East, where banks are widely promoting their Islamic banking products to a growing target customer base.

Islamic finance in Saudi Arabia

Islamic finance’s growth in Saudi Arabia has been surprisingly slow. Its government was the last in the GCC region to allow Islamic banking, although the sector’s presence in the Gulf began with the establishment of the Islamic Development Bank (IDB) in Jeddah in 1975. Recently the Kingdom’s central bank – unexpectedly, according to the market -- sold its shareholding in the International Islamic Liquidity Management Corp (IILM), a body which aims to create a liquid cross-border market for Islamic financial instruments. Saudi Arabia’s Shariah-compliant market represents only 15.4% of total global value, at approximately $138bn. There are 28 Islamic Finance Institutions registered in Saudi Arabia, the largest of which is Al Rajhi Bank, with assets totalling approximately $44bn in 2008, some 32% of the local Islamic banking market. Other banks, including HSBC’s arm (SABB), offer Islamic banking as part of their wider services.

Source: Global Islamic Finance Magazine, May 21st

Qatar planning deposit insurance scheme

Qatari regulators are currently studying the establishment of a deposit insurance framework that will include a Shariah-compliant dimension. This represents one of several reforms aimed at modernising the financial sector of the world’s top exporter of liquefied natural gas (LNG). The scheme would initially be set up under central bank law, and would help bring Qatar in line with best practices in other high-income jurisdictions. By comparison, Bahrain pioneered Islamic deposit insurance, while others including Kuwait, Jordan and Malaysia have developed their own versions.

Source: Reuters, May 15th

GOLCER views this scheme as part of the country’s strategic plan to support domestic banks. However, it is a late step (not only in Qatar but also for other cash-rich Gulf countries, as deposit insurance is rare in the region), with Islamic banks now holding over a third of total banking assets in Qatar. Also, Qatar should work on strengthening regulation of Islamic finance institutions to further develop the sector.

Delay to Tunisian sukuk

A further update on the intention of Tunisia to issue Islamic bonds, its first such issuance, reveals it is now postponed to September after months of delays already. The proposed offering is meant to raise $140m to boost dwindling currency reserves and help cover the budget deficit. The ministry initially planned a $500m sukuk and gave no reason for the reduction in size.

Source: Reuters, May 15th

GOLCER finds these recurrent delays as reflecting a political crisis, along with the instability of the financial sector and the stalled adoption of an Islamic finance law by parliament. The reason for...
the reduced size of the issuance is unclear, especially after the securing of more financing by the government from international lenders and foreign partners, which is designed to support the economy post–the damage caused by political turbulence.

**IBRD plans equity stake in Pakistan bank**

The World Bank’s International Finance Corporation (IFC) is considering buying an equity stake in Pakistan’s Islamic Bank Alfalah, which was established in 1992, is owned by the Abu Dhabi Group, and operates the second-largest Islamic banking operation in the country. The bank held 31.9 billion rupees ($323m) worth of assets at last year-end, and has a presence in Afghanistan, Bangladesh, Bahrain and a representative office in the UAE.

Source: Reuters, May 21st

**Focus – Into Africa**

The potential for Islamic finance to grow on the African continent has been an increasing theme in recent times.

In April Reuters reported that the private sector arm of the Jeddah-based Islamic Development Bank plans to increase its activities there. Its Islamic Corporation for the Development of the Private Sector (ICD), established in 1999, has around 12% of its cumulative investment approvals in Africa, a figure expected to rise in coming years as projects “come on line”. Some of those will be led by Senegal-based Tamweel Africa Holding, jointly owned by the ICD and Turkey’s Bank Asya; Tamweel already holds stakes in Islamic banks in Senegal, Niger, Guinea and Mauritania.
CEO Khaled Al Aboodi spotlighted North Africa, which “represents a large and still untapped market of 190 million people. With the Arab Spring and the changing political map there are huge opportunities in these countries.” Improving access to Shariah-compliant financing for small and medium-sized enterprises (SMEs) will be a particular focus.

In March the African Press Organization reported the World Bank’s International Finance Corporation’s (IFC) announcement of an investment of $5m in Gulf African Bank to support corporate finance and lending to SMEs in East Africa, marking the IFC’s first engagement with an Islamic finance institution in Sub-Saharan Africa. The IFC declared itself “committed to helping expand access to financial services in Africa”.

A study by rating agency Standard & Poor’s in January saw Islamic finance as a “good fit” for infrastructure and project finance in North Africa, because banks lack the long-term funding that these projects require”. Regulatory changes are now creating an “enabling environment”, it said.

According to the report, several projects in renewable energy, transport infrastructure, and communication are ongoing or expected to be launched. Using sukuk to finance some of these projects “could help diversify investors’ base and tap an additional pool of resources”.

Last December the Financial Times reported that when the heads of state of African and Middle Eastern countries met in Kuwait for their third summit, both sides were more interested in talking about business than politics -- particularly that cash-rich investors should be tapped to finance large infrastructure programmes, as their ample liquidity would reduce the cost of borrowing.
How the UK appeals to Islamic Finance
by Stephen Denyer

Head of City and International, Law Society of England & Wales

The United Kingdom is a worldwide hub for Islamic finance. This type of finance has developed rapidly in the UK over recent years - some 10 to 15% per year according to government estimates.

With £12bn of reported assets held in Shari’acompliant funds, six wholly Islamic banks, sukuks listed on the London Stock Exchange and a regulatory environment that puts Islamic finance on a level playing-field with conventional finance, there is little doubt that the UK is the leading Western centre for Islamic finance. The choice for London as the location for the 9th World Islamic Economic Forum (WIEF) in October 2013 -- the first time the WIEF has been held outside an Islamic country -- reflects this fact.

English law is a significant reason why the UK has been able to position itself as one of the leaders in the Islamic finance industry. The famed adaptability of English law makes it possible to draw together traditional principles and the needs of modern commerce. By providing a flexible and predictable framework, it can accommodate traditional Islamic financing structures, and gives the parties confidence that their agreements will be enforced by the courts.

English law is a significant reason why the UK has been able to position itself as one of the leaders in the Islamic finance industry. Its famed adaptability makes it possible to draw together traditional principles and the needs of modern commerce.

British legal experts have a wealth of experience in Islamic finance, and law firms are able to combine this with the international expertise for which they have always been known.

Equally, since English is one of the most widely spoken languages in the world, proceedings conducted in English, interpreting English language statutes and cases, are easily accessible for all commercial parties.

So, in detail, why use English Courts to resolve disputes involving Islamic finance and law? A number of points apply.

First, English courts will generally give effect to agreements structured on the basis of Shari’a principles. They do this not by applying Shari’a law, or by reviewing whether the arrangements are consistent with Shari’a, but by giving effect to what the parties agreed to. This approach gives parties the certainty that their agreement will be objectively adjudicated.
Second, the judiciary in the UK are respected throughout the world for their impartiality and their experience and skill in dealing with complex cases. Judicial independence is a key principle of the UK constitution.

Third, an English judgment can be easily enforced within the European Union by virtue of the Brussels 1 Regulation and the European Enforcement Order. Outside the EU, the UK is party to a number of reciprocal arrangements allowing for mutual recognition and enforcement.

Fourth, England is an established centre for mediation and alternative dispute resolution (ADR), helping parties to settle cases outside the court process.

Similarly, why use English law for Islamic finance transactions?

First, English law, being based on the principle of freedom of contract, will recognise and give effect to the intention of the parties. It provides a framework within which parties can enter into transactions reflecting the principles of Shari’a. English law has very few mandatory provisions and allows parties to forego rights (such as to receive interest) that would otherwise impede Islamic finance instruments.

Second, English law is transparent and predictable, having been developed from a combination of statute and case law in which publicly-decided cases form what is known as the common law. Parties to Islamic finance transactions can predict, with greater certainty than in many civil law systems, whether a proposed course of action is likely to be lawful or unlawful.

Third, a favourable regulatory environment results from the UK Government being at the forefront of enacting legislation to create a level playing-field for Shari’a-compliant institutions and products. They do not suffer tax penalties, are regulated to the same standard, and are given a similar degree of consumer protection compared to other types of financing.

Fourth, English law is well recognised around the world, and the markets are familiar with English law contracts and the concepts used in them. Its practitioners can also be found in all major centres of commerce.

The Law Society of England and Wales is the representative body for almost 170,000 solicitors located in 137 countries around the world. The experience of law firms in facilitating Islamic finance transactions is increasingly becoming an important asset to clients worldwide.
Having been almost totally neglected for ideological reasons by the previous regime, the prospects for Islamic Finance (IF) in Tunisia have changed markedly following the events of 2011, although still subject to delay.

The CEO of the private sector arm of the Islamic Development Bank (IDB), Khaled Al-Aboodi, commented to Reuters earlier this year that “North Africa represents a large and still untapped market of 190m people. With the Arab Spring and the changing political map, there are huge opportunities in these countries.”

For Tunisia the development of the sector could prove beneficial for all parts of the economy, from funding the budget deficit to attracting much-needed FDI from the oil-rich Gulf states and Malaysia, also to providing micro-finance for small- to medium-sized companies, as well as banking services to the estimated 7% of the population which is currently non-banked.

At an international conference held at the end of last year on ‘Finance and Enterprise’ in Tunisia, jointly organised by a number of organisations including the World Bank and the IMF, Muhammad Zubair Mughal, CEO of
the Pakistan-based Alhuda Centre of Islamic Banking and Economics (CIBE), floated the idea of an even larger role for Tunisia, that of the global hub of Islamic Finance for French-speaking countries.

Market commentators share this optimistic outlook. In an extensive report published last year, Thomson Reuters set out two scenarios. The first one assumed ‘efficient and effective government support’ in developing the sector over the next five years. Under these conditions IF assets should achieve 40% of total financial institution assets by the fifth year (2018), equating to $28.5bn. This number was echoed by the Tunisian Central Bank Governor Chedly Ayari in a press conference last year. The report’s second scenario took a slightly more cautious view of government support, but still supposed that Islamic finance assets would achieve 25% of total. In fact, even the second scenario would bring Tunisia in line with the current average of the Gulf states.

The sector is certainly starting from a low base, with only 2.5% of total financial assets being Islamic. Having been out of favour prior to the revolution, the country’s exposure to IF has been limited to two Islamic banks: Al Baraka Bank and Zitouna Bank.

Al Baraka Bank was established in 1983 after obtaining an offshore banking licence. It was subsequently allowed to come onshore provided its deposits did not exceed 1% of the total banking system, curtailing its growth. Zitouna Bank is a commercial bank founded in 2009, and is the only bank allowed to offer Islamic financial services to the domestic retail market. Both entities are looking to expand under the new regime. Zitouna Bank is planning over 100 branches across the country within five years, as well as expansion overseas.

The existence of these two banks is highlighted as a key strength in a SWOT analysis carried out by Thomson Reuters. Other strengths are the proportion of the population inclined towards Shariah-compliance and the strong support of government initiatives. The key weakness named is the absence of specific regulations (though expected soon), the stalled adoption of which would have an adverse impact on investor confidence. Moreover, the research identifies a big gap in retail consumer understanding of Islamic finance, and a limited Shariah financing ‘ecosystem’, i.e. the mesh of scholars, institutions, media, trained professionals and events.

The absence of laws or regulations covering Islamic Finance is being addressed through committees that have been set up by the finance ministry, religious affairs ministry and central bank. The process had started pre-revolution, but the pace has been stepped up. The Council of Islamic Finance in Tunisia (COFIT) was set up in 2012 to develop a legislative framework that would define Islamic financial products.

Of course there are advantages to coming to the party late. Regulators and stakeholders have been able to review all major Islamic finance models, and it appears the Malaysian experience is favoured, although best practice from all sides is being monitored. They are also
looking to avoid mistakes. An example given by a bank representative relates to ‘tawarruq’, a product widely used in the GCC that is being rejected in the Tunisian case.

The sector’s drive for growth is coming from several interested parties.

Greater understanding of IF is being assisted by a number of universities in Tunisia offering masters programmes in the subject, several of which are supported by Bahrain-based Al Baraka Bank. Besides Zitouna Bank’s interest in cross-border growth, non-Islamic Tunisian banks could enter the market using Islamic windows.

Mohamed Sadraoui, deputy director of general supervision and banking regulation at the central bank, has said Islamic windows would be permitted to operate under central bank guidelines that ensured operations were segregated. “There are four or five well-known banks in Tunisia that are trying to facilitate the way for their Islamic finance businesses,” said Mahmoud Mansour, deputy general manager of the Tunisian arm of Al Baraka Bank. He added that three takaful (Islamic insurance) companies had applied for licences.

Tunisia is also getting assistance from external sources. In the key area of Islamic microfinance, for example, it is working with the Jeddah-based ICD (Islamic Corporation for the Development of the Private Sector, part of the IDB) to provide Islamic financing to SMEs. The plans have included a 50 million dinar ($32.3m) Shariah-compliant SME fund. “The success of the fund will serve to increase FDI and further develop Islamic banking in the country,” according to United Gulf Financial Services chairman Mohamed Fekih in a statement.

Earlier this month Reuters reported Tunisia’s finance minister as saying that the country will sell its first Islamic bond in September, after months of delays, raising $140m to boost receding currency reserves and help cover the budget deficit. The sukuk has been put back several times as political turmoil in the North African country has delayed the adoption of an Islamic finance law by parliament.

The way forward may now be clearer. “This time there will be no delay, and we will issue [it] in September,” Hakim Ben Hammouda told Reuters. The ministry had planned a $500m sukuk, and gave no reason for the reduction in size.

Thus, Islamic finance continues to face a bumpy road in the North African state, but nevertheless seems to be on its way to making notable progress.
Stock Markets

GCC

Most Gulf bourses continued their advance during April, dominated again by Dubai’s surging index, complemented by gains in Abu Dhabi and Qatar, also notably Bahrain. Saudi Arabia’s and Kuwait’s uplifts were muted by comparison, while Oman slipped back a little. The key drivers for the UAE markets were again the real estate and associated financial services sectors, indicating to some degree an increasing momentum play. The steadier pickup in the Saudi benchmark Tadawul index represented a mixed picture of improving small-caps but modest losses in the large-cap petrochemical and banking sectors, while still generally buoyed by firm oil prices benefiting the region’s coffers, relatively rapid economic growth, and an earnings season broadly in line with positive expectations.

Egypt / MENA

Egyptian stocks suffered during April and into May, for a combination of reasons. One was somewhat technical, as investors drained funds to engage in the country’s first IPO for four years. Arabian Cement’s $110m issue jumped 15% in its initial movement. Another, however, was an increasing realization that previous euphoria needed a reality check, which was embodied in leading presidential candidate Al Sisi’s remark that the private sector would have to share the costs of recovery, reducing profit margins. Reduced central bank support took positive momentum out of the currency, and the GDP growth prospect for the year remains modest in the 2-2.5% range, insufficient to make much of a dent in unemployment, with the IMF’s proposed loan and stability programme pending. Political matters still hung over sentiment too, with a leadership election due and incidents of deadly, sporadic violence.

South East Asia

Asian markets were more progressive in April, gradually shrugging off the effects of the ‘taper tantrum’ in past months. The Philippines was the standout performer, boosted by an unexpected
rating upgrade, helpful corporate earnings data and hopes for the government’s revised infrastructure spending plan. Investors felt able to cast aside concerns among the developed market blocs over the Ukraine situation, but were held in check to some extent by ongoing doubt about Chinese manufacturing, for which latest statistics showed contraction for a fourth successive month. The Thai market, though, was hurt further by political stalemate that turned to violence and tension that would escalate. Indonesian shares responded well to expectations of a presidential win for a popular candidate. The reappearance of foreign flows in significant sums also aided the Malaysian bourse, particularly upon surprisingly good growth data for Q1.

Rest of the World

At the global level the prolonged climb of equities was maintained through April and into May, but with a note of caution attached, avoiding the euphoric stage, tempered partly by Ukraine’s turmoil and the West’s attempts to put pressure on Russia. While the US boasted stronger economic data, it saw profit-taking in tech stocks. The European space reflected a moderate growth story, qualified by concern for deflation, which nevertheless itself translated into anticipation that easy money policy would prevail. Japan’s indices slipped upon yen appreciation and doubts about the impact of recently-installed consumption tax, with the central bank restraining itself from further support. Emerging markets generally showed reticence still as investors inspected more closely individual country prospects, compared to earlier times of mass flows in search of yield. Chinese and Indian stocks experienced a quiet period.

Sources: GIC, Reuters, Bloomberg, broker reports
Islamic Stock Indices

Islamic or Shariah compliant indices exclude industries whose lines of business incorporate forbidden goods or where debts/assets ratios exceed 33%. The increasing popularity of Islamic finance has led to the establishment of Shariah compliant stock indices in many stock markets across the world, even where local Muslim populations are relatively small, such as in China and Japan.

Conventional Stock Indices

Volatility is a measure of uncertainty of market returns. It is calculated as the standard deviation of the returns in the reported month. The formula for the standard deviation is: $\sigma = \sqrt{E[(X-\mu)^2]}$.
Commodities

Oil

Amid a generally uneventful month for commodities, oil ticked moderately upwards upon supply concerns as well as absorbing a risk premium associated with developments in Ukraine. A strengthening US economy and increased demand for gasoline lifted WTI, along with tightening inventory, although an uncertain Chinese outlook, affecting world trade, and profit-taking limited that impetus. The benchmark had already been underpinned by bouncing off technical chart support. While equally affected by international issues, the Brent series was constrained by additional Libyan production being anticipated. The Saudi oil minister reaffirmed the idea of the $100 level being a fair price, indicative of no likely OPEC policy adjustment.

Gold/Precious Metals

Gold’s safe-haven appeal was enhanced by the Ukraine situation, but the precious metal was not otherwise favoured in economic conditions of moderate growth and moderate inflation. Market positioning for several weeks showed confusion over whether the US Federal Reserve would be inclined to keep its very cheap money stance for longer. The Fed itself has appeared committed both to tapering its quantitative easing strategy, but also avoiding any premature hiking of interest rates, unsure still of the economic outlook. Analysts tended to expect further testing of the downside in prices, but with a distinct sense of uncertainty in play, keeping many traders on the sidelines. There was some speculation that India would relax its import restrictions, liable to rekindle an important segment of consumption.

Copper/Base Metals

Copper continued to retrace its path, with traders holding short positions ultimately scrambling to cover themselves by buying from the net longs, against perceptions of rebounding global business. In mid-April a recovering US dollar meant a negative price reaction, corroborating the weakness derived of China’s apparently soft economy. That was later offset, however, by the increasing confidence felt in the US case, and then a stockpile squeeze in the local Chinese market. Analysts were unsure whether this would be an isolated flurry of activity in what has been perceived as predominantly a sellers’ market.

Sources: OPEC, Reuters, Bloomberg
Bonds and CDS markets

GCC

Gulf bond prices sustained their steady uptrend in the period covered, assisted by local demand, returning confidence across the emerging market class, and the ongoing commitment of global policymakers to retaining an accommodative policy stance, which lifted risky assets across the board. Against a background of resurging US Treasuries, market appetite in the region was such that paper of longer duration was being sought, although much focus remained on primary issue opportunities rather than secondary action.

Egypt / MENA

Egypt’s bonds proved hardier than stocks through April and into May, a reflection that the government’s focus on restoring the country’s finances remains sufficiently keen, even while the economy struggles for vigour. Although an economic growth rate of some 2–2.5% this year makes fiscal improvement difficult, the authorities seem to have adopted the need to reduce the subsidies that strain the budget, as per IMF orthodoxy. CDS spreads dropped towards the 300 basis points level from around 600 at the start of the year.

Malaysia / South East Asia

In common with the global trend, Asian credits rose in April and especially May, engaging with the flipside of the volatility that was previously induced over the US Fed’s curtailment of QE. Conditions being so favourable for Treasuries meant that Asian bonds and currencies both rebounded in self-reinforcing tandem, in a sharp reversal of sentiment. Even so, Malaysian bonds were subject to some reserved judgement, as the central bank signalled it might raise interest rates in response to what it viewed as growing financial imbalances.
Global Benchmarks

US Treasuries set the agenda for other markets with a surge that was unexpected to most observers earlier in the year. Ten-year yields dropped below 2.5%, upon several factors, essentially feeding a collective realization that the US’s tapering of monetary stimulus, itself to be a very measured process, was likely to be replaced by similar efforts in Europe, China and Japan. Billions flew into mutual bonds funds, despite jobs data denoting America’s recovery.

The flight-to-quality in reaction to the Ukraine impasse gave support, while the hunt for yield tilted demand in Europe towards peripherals, compressing spreads massively versus German bunds. Inflation has yet to appear meaningfully as a factor in the global upturn, and liquidity is plentiful. JGBs remain captive to overwhelming central bank buying, denying movement either way from elevated levels.

Source: Invest AD, Bloomberg, broker reports

Sovereign Bond Markets

The table reports the price index on which the MTM Change is calculated (month-to-month) and the Yield of sovereign bond maturities typically be between 6 months and 25 years. Data as at 30/4/2014. MTM Change refers to the change relative to the previous month.

<table>
<thead>
<tr>
<th>Country</th>
<th>Price</th>
<th>MTM Change (%)</th>
<th>Yield (%)</th>
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<tr>
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<td>148.15</td>
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<td>Japan</td>
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<td>0.23</td>
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Evolution of Bond Markets in April 2014 relative to the previous month. The table reports the price index on which the MTM Change is calculated (month-to-month) and the Yield of sovereign bond maturities typically between 6 months and 25 years. Data as at 30/4/2014.

Credit Default Swap Markets

The index reported here represents the average basis points (bp) of a 5-year CDS for protection against sovereign bonds. Data as at 30/4/2014. MTM Change refers to the change relative to the previous month.

<table>
<thead>
<tr>
<th>Country</th>
<th>CDS Spread (bp)</th>
<th>MTM Change (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bahrain</td>
<td>175.33</td>
<td>-1.65</td>
</tr>
<tr>
<td>Qatar</td>
<td>58.79</td>
<td>-6.55</td>
</tr>
<tr>
<td>Saudi Arabia</td>
<td>49.84</td>
<td>-3.92</td>
</tr>
<tr>
<td>Dubai</td>
<td>172.14</td>
<td>-5.10</td>
</tr>
<tr>
<td>Abu Dhabi</td>
<td>98.34</td>
<td>0.51</td>
</tr>
<tr>
<td>Egypt</td>
<td>385.87</td>
<td>-16.48</td>
</tr>
<tr>
<td>Thailand</td>
<td>124.40</td>
<td>-4.59</td>
</tr>
<tr>
<td>Indonesia</td>
<td>171.50</td>
<td>-1.34</td>
</tr>
<tr>
<td>Malaysia</td>
<td>101.47</td>
<td>-0.96</td>
</tr>
<tr>
<td>India</td>
<td>252.63</td>
<td>6.74</td>
</tr>
<tr>
<td>China</td>
<td>145.03</td>
<td>-0.85</td>
</tr>
<tr>
<td>Italy</td>
<td>113.77</td>
<td>-14.79</td>
</tr>
<tr>
<td>Portugal</td>
<td>168.41</td>
<td>-8.41</td>
</tr>
<tr>
<td>Spain</td>
<td>91.62</td>
<td>-12.61</td>
</tr>
<tr>
<td>France</td>
<td>45.75</td>
<td>-6.27</td>
</tr>
<tr>
<td>Germany</td>
<td>21.02</td>
<td>-9.05</td>
</tr>
<tr>
<td>UK</td>
<td>22.55</td>
<td>-8.54</td>
</tr>
</tbody>
</table>

Evolution of CDS Spreads in April 2014 relative to the previous month. The index reported here represents the average basis points (bp) of a 5-year CDS for protection against sovereign bonds. Data as at 30/4/2014. MTM Change refers to the change relative to the previous month.
Islamic Bonds (Sukuk)

With confidence in fixed-income prospects growing surprisingly in the global context, the sukuk market picked up again in April, culminating in Dubai Department of Finance’s $750m, 15-year ijara offering with a coupon rate of 5%, twice or three times oversubscribed.

It was reported that Kuwait Finance House research revealed new issuance volume in the month rising by some 20% against the previous month to $13.4bn, boosted by the return of Gulf names especially. Sovereigns and quasi-sovereigns still predominated.

Further substantial issues were seen in May.

Most recently, Dar Al Arkan Real Estate Development Co of Saudi Arabia raised $400m with a 5-year sukuk inducing final orders in excess of $1bn, and a profit rate of 6.5%, representing a tightening on earlier pricing.

The Malaysian-based International Islamic Liquidity Management Corp (IILM) re-issued a $490m Islamic bond, a 3-month issue priced at 0.52%, as part of its strategy to meet a shortage of highly-liquid, investment-grade financial instruments for Islamic banks to utilise in short-term risk management.

Malaysia’s Hong Leong Islamic Bank Bhd established a sukuk programme to raise as much as 1bn ringgit ($310m). The subordinated Islamic bond programme is Basel-III compliant, as tier-2 regulatory capital.

Earlier this month Investment Corporation of Dubai (ICD) increased the amount to be raised from the sukuk portion of its debut bond issue, exchanging that for a reduction in the conventional portion. It will now seek to secure $700m on a 6-year maturity, from the $500m initially nominated.

Sources: KFH, GIC, Reuters
Perspective
When short-term momentum meets long-term fundamentals
by Andrew Shouler

Stock markets around the world have surged again recently, having caught their breath, reappraised conditions, and decided it’s safe to go back into the water again – encountering very warm liquidity indeed. Not least, the search for yield has not retreated as an incentive, but perhaps even intensified with any incipient threat of inflation in various parts.

Not only has the US’s benchmark S&P 500 been setting records still, but emerging markets have recovered from the severe knock to confidence from the Federal Reserve’s announcement of tapering plans last year. In the Gulf, Dubai has been most notable in advancing strongly, particularly in the banking, related financial services and real estate sectors.

Over prolonged periods of investment it has been shown that it is the prudent approach, the ‘buy-and-hold’ mentality, and returning of dividends into accumulating further holdings, that historically has worked best in the long term. Yet, there will be many investors once again tempted into riding the wave of momentum that results from not only the easy-money environment but also a gently recovering world economy, represented in improvements to corporate earnings.

It is in this heady atmosphere that warnings have arisen from seasoned market watchers that volatility is due, given that the markets appear still to be over-discounting economic trends, and the Fed is gradually switching from an outstandingly accommodative policy towards the possibility of tightening, albeit on a carefully moderated basis. Experienced asset manager Mohammed El-Erian is one leading figure from that industry delivering that message.

As a general rule, naturally it’s better to buy low and sell high than to buy high and expect to sell higher, assuming holding stock in perpetuity is not the requirement. So climbing back onto the markets’ surfboard carries greater dangers now, although potentially exhilarating and financially rewarding.

In the Gulf region, for instance, local exchanges may not be quite so developed yet or as liquid as those of international benchmarks, so that the scope for their turbulence and potential overreaction could be aggravated in the event of turbulence.

There is also the scope for tension to consider between the forces of overseas market trends spilling over to the region on the one hand, and the special circumstances of the Gulf on the other, as they are still benefitting from remarkably stable oil prices at elevated levels.

Data released by Global Investment House have endorsed the impression of solid underpinning for Gulf stocks in terms of corporate performance. Noticeably, while earnings rose 12.1 per cent year-on-year in the first quarter overall, Dubai’s soared by 45.6 per cent, relying heavily on real estate and financials -- sectors associated with the bubble of the last financial crisis, and perhaps vulnerable to pullback at some point.

It will be interesting to discover whether “it’s different this time”, as sometimes suggested during an extended upturn in fortunes, and whether the herd instincts of retail investors might again be exposed as a contrarian indicator.

In the meantime, momentum alone can be very rewarding for short-term participants, and very often has a lot of mileage.
CALL FOR PAPERS

4th Islamic Banking and Finance Conference (IBF 2014)

23rd to 24th June 2014
Venue: Lancaster University Management School

Keynote Speaker
Thorsten Beck
Professor of Banking and Finance, Cass Business School

The constraints applied by Islamic banks rendered them more resilient in the recent financial crisis compared to their conventional counterparts. This has attracted the attention of market participants and researchers to their liquidity buffers, leverage ratios, managerial efficiency and bespoke financial products. Islamic banking products are now offered in more than twenty countries and their expanding suite includes bonds, equity indices and insurance. The sector is estimated to exceed $1 trillion in value, while growing at about 15% per annum. Among many issues still subject to debate is the purity of Islamic finance in practice, given the need to compete and to operate with customers whose expectations have been formed by conventional banking practices.

EIBF centre at Aston Business School in collaboration with GOLCER Lancaster University Management School is organising a conference on Islamic Banking and Finance. The conference aims to provide a forum for an exchange of views on recent developments and to identify key issues/challenges underlying the paradigm of Islamic Banking and Finance in the 21st century.

Original contributions are invited on any of the listed topics:

- Financial risk and stability
- Transparency, governance and corporate social responsibility
- Earnings management and impression management
- Performance, efficiency and convergence
- Mutual funds
- Risk Management, Accountability and auditing
- Competition
- Microfinance and SMEs
- Behavioural finance

Conference Organisers: Dr Omneya Abdelsalam (Aston University), Dr Marwan Izzeldin (Lancaster University)

Special Issue
Journal of Economic Behaviour and Organisation (JEBO)
Ana Timberlake Best paper Research Award: £500

Co-editors for the JEBO Special Issue
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For paper submissions please email Marwa Elhassab: islamicfinance@aston.ac.uk

Important Dates

<table>
<thead>
<tr>
<th>Conference Abstract Submission</th>
<th>Conference Full Paper Submission</th>
<th>Submission for JEBO Special Issue</th>
<th>Special Issue Publication</th>
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<tr>
<td>31st March 2014</td>
<td>27th April 2014</td>
<td>1st October 2014</td>
<td>October 2015</td>
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