

Islamic Finance Bulletin

January 2012

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The Petronas Towers were the tallest buildings in the world from 1998 to 2004 and remain the tallest twin buildings in the world. The Petronas Company, the national oil-company of Malaysia, occupies all of Tower One, while Tower Two lists offices of Bloomberg, IBM, Boeing, Reuters, and Microsoft.

Year of construction: 1998

Max Height: 378m

Coordinates: [3.15785°N 101.71165°E](#)



Global Indices

Global Islamic* indices embarked the New Year with positive returns as the economic data of US and China have signaled a sense of optimism in the global economy. The MENA indices have the highest volatility, followed by the far eastern and GCC indices. The Asian indices, mainly India and China have risen significantly. Egypt showed a tremendous recovery by jumping about 13 percent. Jordan, Qatar, and Kuwait indices reported losses in January.

	Country	Index	MTM Return	Volatility	Value at Risk
GCC	Bahrain	S&P Bahrain Shariah	▼ -2.48%	0.64%	-1.29%
	Kuwait	S&P Kuwait Shariah	▼ -3.23%	0.49%	-1.08%
	Oman	S&P Oman Shariah	▼ -1.76%	0.30%	-0.73%
	Qatar	FTSE Nasdaq Dubai Qatar 10 Shariah	▼ -5.46%	0.62%	-1.33%
	Saudi Arabia	S&P Saudi Arabia Shariah	▲ 1.43%	0.48%	-0.77%
	UAE	FTSE Nasdaq Dubai UAE 20	▲ 5.49%	1.26%	-2.41%
MENA	Egypt	MSCI Egypt Islamic	▲ 12.78%	1.34%	-1.27%
	Tunisia	S&P Tunisia Shariah	▲ 0.35%	0.93%	-1.34%
	Morocco	S&P Morocco Shariah	▲ 9.53%	1.06%	-2.72%
	Jordan	S&P Jordan Shariah	▼ -5.44%	0.83%	-1.82%
	Lebanon	S&P Lebanon Shariah	▼ -2.15%	1.31%	-1.12%
Far East	Thailand	SPGI BMI Thailand Shariah	▲ 1.73%	1.17%	-1.94%
	Taiwan	SPGI BMI Taiwan Shariah	▼ -0.62%	0.67%	-1.17%
	Singapore	SPGI BMI Singapore	▲ 6.25%	0.77%	-0.53%
	Philippines	SPGI BMI Philippines Shariah	▲ 6.00%	1.78%	-3.25%
	Indonesia	Jakarta SE Islamic	▲ 6.09%	0.94%	-1.25%
	Malaysia (H)	FTSE Bursa Malaysia Hijrah Shariah	▲ 0.87%	0.44%	-0.92%
	Malaysia (E)	FTSE Bursa Malaysia Emas Shariah	▲ 2.06%	0.40%	-0.76%
Rest of the World	South Korea	SPGI BMI Republic of Korea Shariah	▲ 4.34%	1.34%	-1.87%
	Japan	S&P Japan 500 Shariah	▲ 2.89%	0.93%	-1.19%
	South Africa	FTSE South Africa Shariah	▲ 6.74%	1.06%	-1.29%
	Hong Kong	SPGI Hong Kong Shariah	▲ 2.66%	0.83%	-1.04%
	India	FTSE Shariah India	▲ 19.84%	1.31%	-0.22%
	China	FTSE Shariah China	▲ 10.86%	1.40%	-1.53%
	DJ Islamic	DJ Islamic	▲ 6.14%	0.64%	-0.40%
	FTSE World	FTSE Shariah World	▲ 6.22%	0.70%	-0.67%

Table 1: Evolution of Islamic Stock Markets since the beginning of January 2012 for GCC, Far East, Middle East North Africa (MENA) and Rest of the World markets. Percentage Month-to-Month(MTM) Returns, Percentage Volatility, Percentage Value-at-Risk(VaR). Volatility is a measure of uncertainty of market returns. Value at Risk (VaR) estimates the worst possible return that can happen tomorrow with a given confidence (here 95%). Source: Datastream

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.

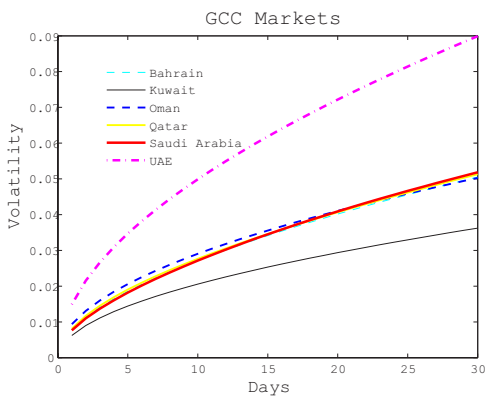
GCC

Qatar was the worst performing index in the region, falling by 5.46 percent owing to a fall in the country’s banking sector. Investors are disappointed as Qatar National Bank (QNB) proposed to pay a 40 percent cash dividend and issue bonuses that would amount to 10 percent of the share capital. QNB is the biggest bank by assets in the country.

UAE, the best performer in the GCC, increased by 5.49 percent as oil traded above \$100 per barrel. However, the tension in Iran an ongoing impact on the nation UAE, was also the riskiest index as its Value at Risk* was at -2.41 percent.

The average volatility for the region was 0.63 percent. Volatility forecasts for February describe that UAE would continue to be the riskiest market.

* Value at Risk (VaR) estimates the worst possible return that can happen tomorrow with a given confidence (here 95%).



MENA

Egypt and Morocco kicked off 2012 on a positive note climbing by 13 percent and 10 percent in January. In Egypt, the peaceful protests marking the first anniversary of the anti- Hosni Mubarak movement have definitely signaled a bullish market. The country has also urged to the IMF to lower the interest rate for the loan it has requested.

The Benkirane government’s new economic reforms have led to a jump in the country’s index as it is said to pave way for restructuring in the economy and thus a fair distribution of wealth. Notable gains were also seen in the banking sector in Morocco.

The average volatility in the MENA region was 1.1 percent. Morocco had the highest Value at Risk this month. The forecasts for February predict Tunisia to be the riskiest index and Jordan the safest.

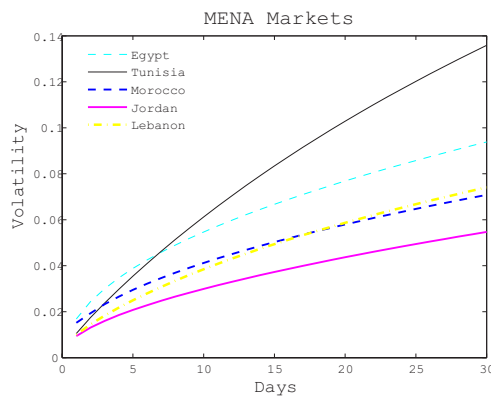


Figure 2: 30-Day ahead volatility forecast for the GCC, MENA markets. The 30 day period starts on the 1st day of the bulletin’s month. The plot represents the standard deviation of returns expected if you hold the indices for the next 30 days. The value on the 30th day is the volatility forecast of the expected return if you purchased the indices on the first day and held it for 30 days.

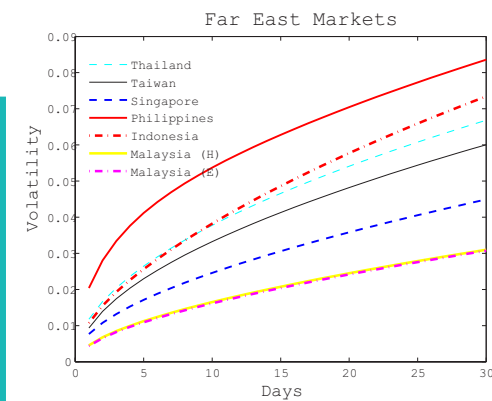
Far East

Most indices in the far eastern region have shown positive returns which could be in line with the optimistic outlook in the global economic conditions. Singapore showed the highest returns this month as the economic scenario has turned bullish in the US thereby increasing the demand for export related industries such as shipping and electronics.

Taiwan index had fallen owing to a slump in overseas demand of its exports. This has greatly affected its manufacturing industry and job markets.

Indonesia climbed 6 percent owing to obtaining a better sovereign rating by the Moody's coupled with overall fiscal prudence in the economy. Analysts say that the economy is expected to keep its rising trajectory.

The average volatility for the region was about 0.9 percent. Forecasts for volatility in February show that Philippines would be the riskiest index and Malaysia the safest. Philippines were also the riskiest index this month with a Value at Risk at -3.25 percent.



Rest of the World

“It’s a crisis of confidence, not of capitalism”, said George Osborne. Rising technology stocks coupled with higher corporate earnings has driven up the Asian indices as the New Year commenced. Falling European borrowing costs has also attracted investors to emerging market assets.

Increasing demand for emerging market assets, opening up of the stock market to individual foreign investors and thus the strengthening of the Indian Rupee has led to a tremendous gain in the Indian index, rising by 20 percent.

In Hong Kong, there has been a rise in the property market as China eases its monetary policy. China climbed by about 11 percent after the government decides to boost its slumping economy.

Japanese stocks showed a strong performance after gains from increase in orders for machinery. This has also had positive spillover on other Asian indices.

Our volatility forecasts predict China to be the riskiest and Hong Kong to be the safest indices in February.

Source: FT, Bloomberg, Reuters

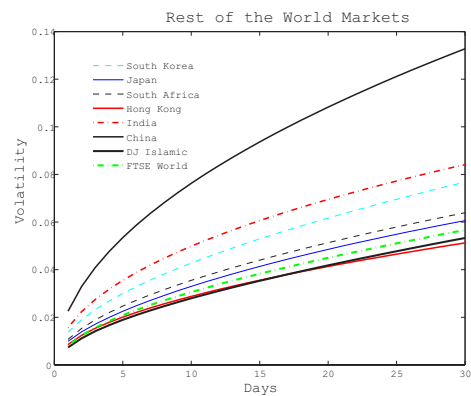


Figure 3: 30-Day ahead volatility forecast for the Far East and Rest of the World markets. The 30 day period starts on the 1st day of the bulletin’s month. The plot represents the standard deviation of returns expected if you hold the indices for the next 30 days. The value on the 30th day is the volatility forecast of the expected return if you purchased the indices on the first day and held it for 30 days.

Commodities

2012 has kicked off on a positive note for commodities. Monetary easing in the US and a positive outlook in the Chinese economy has boosted the price of commodities. Even though the euro crisis has led to bearish swings in the commodity markets, analysts predict prices to rise by medium term. Last year, we saw investors to be very quick in buying and selling commodities thus making it a very volatile market.

Source: FT, Bloomberg

Commodity	Units	MTM Return	Volatility	Value at Risk
Brent Oil	US \$/bbl	▲ 1.96%	1.37%	-1.29%
Dubai Oil	US \$/bbl	▲ 4.09%	0.91%	-1.08%
WTI Oil	US \$/bbl	▲ 0.65%	1.43%	-0.73%
Natural Gas	US \$/MMBTU	▼ -10.41%	4.08%	-1.33%
Gold	US \$/Troy Ounce	▲ 9.50%	1.14%	-0.77%
Copper	US \$/MT	▲ 11.46%	1.65%	-2.41%
Sugar	US c/LB	▲ 4.56%	1.88%	-1.94%
Palm Oil	US \$/MT	▲ 1.19%	0.52%	-1.17%

Table 2: Evolution of highly traded commodities in January 2012. MTM Percentage Returns, Percentage Volatilities and Percentage VaRs. US \$ and US c indicate United States Dollar and United States cent respectively. bbl=billion barrels, MMBTU=Million British Thermal Units, MT=Metric Tonne and LB=Pound. Source: Datastream

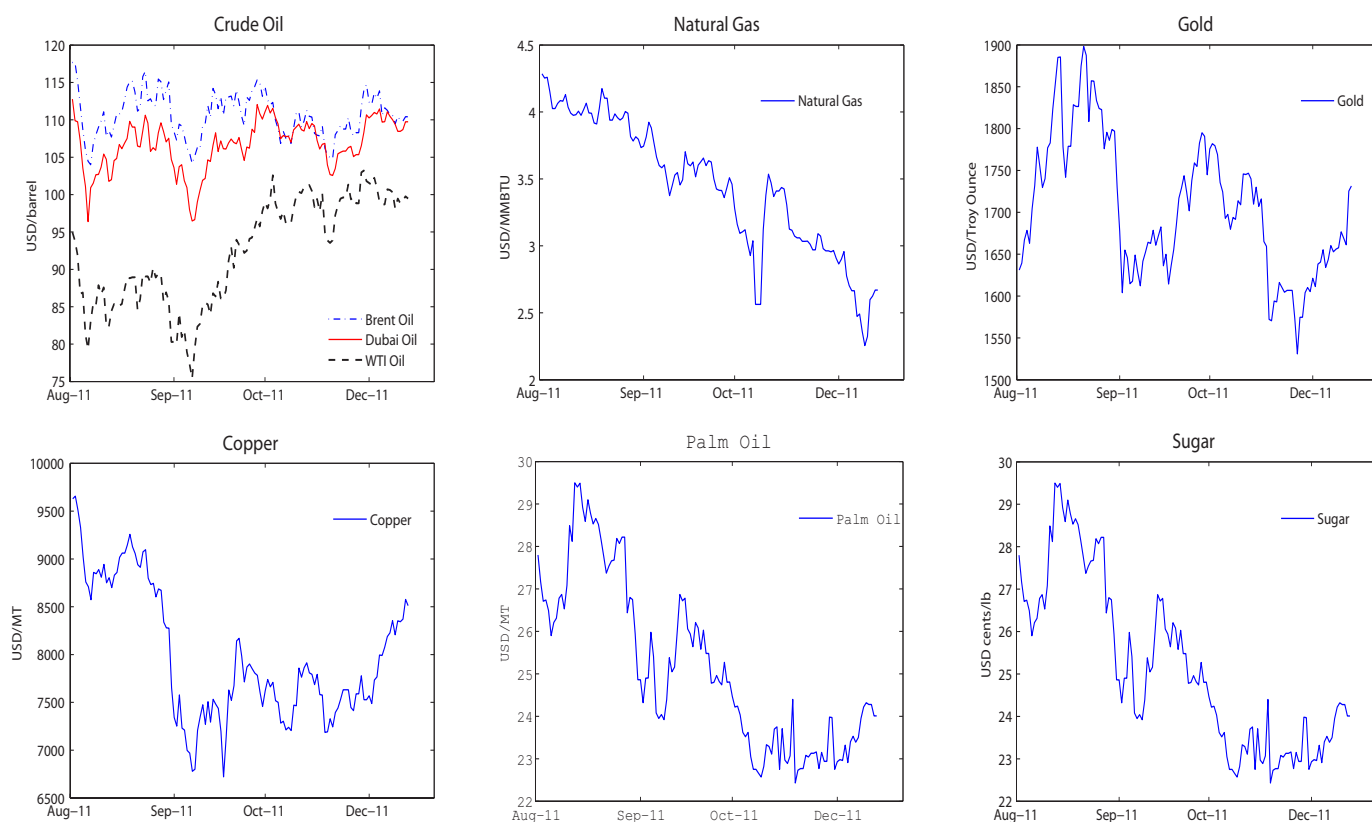


Figure 4: Evolution of highly traded commodities (prices) in August 2011 - January 2012. Source: Datastream

Crude Oil

In January, as the EU plans an embargo on Iranian oil imports, the price of oil has risen. A representative from the OPEC says that the embargo would result in an economic suicide for the west as it would push up the price of oil greatly. There has also been a warning from the OPEC saying that the oil industry is up for a period of intense price volatility.

Natural Gas

Natural gas prices continue its fall this year as well dropping by about 11 percent. An increasing stock pile and very low demand owing to mild winters has led to this fall in prices. Individual energy producers are now facing high risks due to this ongoing loss. It was highly volatile in January and had a Value at Risk at -1.33 percent.

Gold

Gold has jumped significantly by 10 percent as the dollar weakens. As the US Federal Reserve announced that the low interest rates would continue till 2014, the bullion took a positive turn.

Copper

Copper prices rise by 12 percent as China decides to boost its manufacturing sector so as to improve its economic growth. However, prices are said to fall in the coming months as the metal has been stocked up in China since the end of 2011.

Palm Oil

In January, the palm oil prices rose as Malaysia, the second largest producer of the crop dropped production. There is a concern over a decline in inventories as well as bad weather which may affect the crop yields.

Sugar

Sugar prices have risen by about 5 percent this month as there is concern about the supply of the crop from Brazil. There are also risks suggesting decrease in production in Mexico and India.

Source: FT, Bloomberg, Reuters.

Issues on the Accountancy Rules and Regulations for Islamic Banks and Islamic Finance Industry

Issues on the Accountancy Rules and Regulations for Islamic Banks and Islamic Finance: Towards the Adoption of Basel III by IBs:

At the recent Financial Services Board (IFSB) seminar in Brunei, the IFSB's secretary general 'Jaseem Ahmed' stated that there is an existing working group to revise the existing 2005 capital adequacy standard (CAS) to be consistent with Basel III requirements. The final draft is expected to be issued in 2013. He further highlighted that among specific issues facing the working group is the treatment of subordinated debt, capital convertible contingent capital and other types of Shariah compliant instruments and Sukuk.

In our opinion, the attempts to smooth out the effects of Shariah requirement to preserve harmonization with the conventional application of Basel III are likely to result in unpleasant outcomes represented by high implementation costs. These costs are expected to be forced on customers in IBs. One of the fundamental motives toward the adoption of Basel III is to mitigate procyclicality in regulatory capital. It seems to us that this is likely to tighten the credit supply for conventional banks and to reduce the magnitude of Mudharaba contracts in IBs

Source: The IslamicGlobal.com

The Absence of Shariah Authoritative Body in UAE:

The absence of a central Shariah banking supervisory body in the UAE has been brought to the fore again with Obaid Tayyer, the emirates' minister of finance, questioned at the Federal

National Council (FNC) level on the failure to set up such an authority. Unlike other thriving markets for Islamic finance such as Bahrain and Malaysia, whose central banks have established a national Shariah board and a Shariah advisory council, the Central Bank of the UAE has not set up a body of its own to govern the emirates' Islamic banking sector.

Scholars have long demanded the creation of a central Shariah board; in an effort to create neutrality, transparency and standardization. It seems to us that it's now the time to find serious steps to address the absence of such board in the UAE, given the eminent growth of the Islamic banking services in UAE.

Source: Islamic Finance News

Pakistan's Regulators Opens up Takaful Sector:

The development of Islamic Finance in Pakistan continues apace due to the approval of draft Takaful rules by the Security Exchange Commission of Pakistan (SECP). A statement was published at the mid of January 2012 stating the completion of the first stage of its regulatory review of the country's insurance laws to accommodate Takaful. The statement suggested that the new rules will call for the establishment of a central Shariah board to oversee Takaful nationally. Interestingly, the legislation will allow conventional insurers to open Islamic Windows to develop and distribute Takaful products.

Source: The IslamicGlobal.com

Recent Developments in the Islamic Finance Industry

Massive Sukuk Issuance at the Start of the Year.

The Islamic finance industry has gotten off to an explosive start for this year; with two Sukuk issuances in the second week of January alone. Global sales of sukuk, which pay asset returns to comply with Islam's ban on interest, rose to \$10.7 billion in Jan 2012 from \$125 million in the same period in 2011, according to data compiled by Bloomberg. These comprise Projek Lebuhraya Usahasama's US\$9.67 billion Sukuk, the world's largest offering by a single issuer to date and the launch of a Sukuk from Saudi Arabia's General Authority for Civil Aviation, marking the first ever sovereign Islamic bond from the kingdom. Also, based on HSBC Holding PLC's expectations the sales of Islamic bonds may rise to \$44 billion this year as demand outstrips supply and as Asian and Middle East investors tap the market complying with Islamic banking rulings. Predictions for this year reflect a significant increase in sukuk issuance as it performed well against the financial crisis and liquidity crunch in 2011 in addition the sukuk market is already off to a strong start in 2012.

Given this optimism we believe that uncertainty still landscape the Islamic financial markets for this year, due to the economic and political instability surrounding many Islamic countries like Egypt and Syria along with the with the tighten budgeting strategy in many gulf countries to recover from the global financial crisis.

Source: Islamic Finance News and Bloomberg.com

Badische Anilin- und Soda-Fabrik (BASF) is added to the Dow Jones Islamic Market Index.

With its significant commitment to growth in the Middle East, the largest chemical company in the world (BASF) is now listed on the Dow Jones Islamic Market Index (DJIM). The DJIM represents listing for investable equities that are screened for Shariah compliance consistent with Dow Jones indexes methodology. There currently exist more than 125 licensees of more than \$5bn in assets benchmarked to DJIM Indexes. BASF has showed greater expansion with substantial long term investments in manufacturing in the Middle East over the last three decade. Harald Kroll (Managing Director of BASF) views the listing in DJIM not only strengthens the brand in the region, in line with the interest of Shariah compliant investors, but also initiates from the company abide to the highest ethical standards and mores of the customers in the operating-countries.

Source: AMEinfo.com

UAE are Well Positioned to Refinance in year 2012.

Banks in the UAE may plan to refinance more than US\$3 billion-worth of bonds due in 2012 should pricing remain at current levels, as they seek to extend the average maturity of their debt. Samer Mardini, the vice-president of fixed income and Islamic finance products at SJS Markets in Dubai, noted that the current price for bond sales in the UAE market is between 3-4%. This suggests that banks will not pay more than that to come to market

this year. Raj Madha, an analyst at Rasmala Investment Bank, also states that the amount due is “a lot”, especially to mature at the same time. However, recent Sukuk sales show that deals can be done at the right price even in the prevailing difficult international environment.

Source: Islamic Finance News

Middle East Remains the Easiest Region to pay Taxes, according to PwC’s Annual Report.

Based on the annual report ‘Paying Taxes 2012’ issued by PwC, the World Banks and the IFC, the Middle East has the simplest tax laws in the world. The report compares the taxing system across 183 countries and presents that all the six GCC States fall within the top 15 countries. The report also shows that the time to complete the tax obligations is significantly lower than countries worldwide given the limited number of taxes that are currently being levied. The UAE, for the second time, is ranked among the top 10 for ease tax payments, ranked as the 6th in 2012 compared to the 5th in 2011. Qatar received the 2nd position, KSA the 7th, Oman the 8th, Kuwait the 12th, and Bahrain the 13th.

Source: AMEinfo.com

Missing Analysts’ Estimates and Earnings Decline for QIB.

Qatar Islamic Bank (QIBK) resulted in declines in the nation’s banking stocks after profit missed analysts’ estimates and the Shariah-compliant lender reduced its dividend. The shares of the Persian Gulf country’s biggest Islamic bank dropped to 3.1%. Doha

Bank QSC (DHBK) lost 2.9 % after reporting earnings that matched estimates. Qatar National Bank SAQ (QNBK), the country’s biggest lender, retreated as much as 0.5%. QIB and Doha Bank had the biggest percentage declines on the country’s benchmark stock measure, the QE Index, (DSM) which fell 1.1%. The bank’s full-year net income was 1.37 billion riyals (\$376 million) after 1.26 billion riyals a year earlier while the mean estimate of eight analysts was for a profit of 1.46 billion riyals. The lender plans to pay a 4.5 riyal-cash dividend compared with 5 riyals a year earlier.

Source: BloomBerg.com

The Launch of the Islamic Banking Sector in Oman with the IDB Pledging Interest:

The Islamic Development Bank (IDB) from the start has been supporting the establishment of Islamic banks and financial institutions through equity participation. The IDB at the end of January has pledged to invest equity into IBs in Oman. The country’s newly set-up Islamic banks, Bank Nizwa and Al Izz International Bank (Bank Al Izz), are slated to begin operations this year, while Ahlibank, Bank Muscat, Bank Sohar and the National Bank of Oman comprise conventional lenders which have expressed interest in establishing Islamic windows. The participation from the IDB is expected to encourage the Oman’s government to move further in the development of the country’s Islamic finance sector; providing capital support in an area where the government has already said it will not.

Source: Islamic Finance News

The Egyptian Plans for the Issuance of Islamic Bonds.

Egypt is currently preparing for a debut sovereign Islamic bond, after the government has been forced to rely on local banks for funds in the wake of last year's popular revolt. The government is studying a new legal structure that will allow them to issue a sovereign sukuk. Analysts expect that Egypt will need international support in order to avert a financial crisis, but among noticeable local attempts are the advocate shift to the Islamic finance system and the issuance of Islamic Sukuk.

Source: AMEinfo.com

First Islamic Bank in Ethiopia.

Ethiopia is expected to have its first Islamic bank 'ZamZam Bank' opening at the first 6 months of 2012. The bank is currently in the formation stage. It has been established in 2008 but did not operate due to the central bank's amendments to the country's banking regulations to allow interest-free banking. The move-

ments toward the adoption of Islamic banking model in Ethiopia are indicative of the growing appetite for Islamic banking in the sub-Saharan Africa.

Source: The IslamicGlobal.com

First Gulf Bank Received \$1.4 Billion in Bids for Islamic Bond.

The First Gulf Bank PJSC (FGB) is a lender controlled by Abu Dhabi's ruling family has received \$1.4 billion in bids for its \$500 million Islamic bond sold on the 17th of January of 2012. 69% of the investors in the sukuk were from the Middle East, 15 % from Europe, and 16 % from Asian markets. Commercial and investment banks bought about 72% of the bonds, fund managers 18%, private banks 7% and insurance and pension companies 3%. The CEO of the bank stated that the proceeds will be used for general corporate purposes and to enhance the bank's services.

Source: Bloomberg.com

The Gulf One Lancaster Centre for Economic Research (GOLCER) was established in May 2008 by Lancaster University Management School and Gulf One Investment Bank. The centre is funded by a donation from Gulf One Bank.

The main purpose of the Centre is to conduct empirical research focused on key economic and financial developments in the Middle East and North Africa (MENA) region, with special emphasis on the Gulf region. This region includes Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and United Arab Emirates, countries that form the Gulf Cooperation Council.

GOLCER's research agenda will include, as primary topics, energy economics, Islamic banking and finance, telecommunication and infrastructure economics. Recent developments in these fields will be assessed in the light of their impact on the economy of the Gulf region.

In addition to its research activities, GOLCER will provide tailored training courses in specialised areas, including quantitative methods and applications of state-of-the-art econometric and statistical software packages to economic and financial phenomena. GOLCER will also provide consultancy services.

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