Chapter 37

Economic and Social Impacts of Sovereign Sukuk

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ABSTRACT

This chapter explores the economic and social impacts of sovereign Sukuk in Sudan and its unique challenges. The first of its kind, this research collected primary data from different groups of investors of Sudanese governmental Sukuk. Adopting a qualitative approach (interview questions and open and closed-ended surveys), four sets of questions were distributed to four groups (individual investors, institutional investors, government officials, and academics). The survey found that despite Sukuk’s influence in activating the economy and financial markets, and encouraging savings awareness, the market in Sudan is facing many challenges. Accordingly, it is recommended that Sukuk issuances should appeal to a wider audience including retail investors. The ensuing system, which could likewise be adopted by other countries, would generate more liquidity for development projects and may prove helpful for developed Sukuk markets. Additionally, evolving capital markets would enhance the economic and social impact of governmental Sukuk.

INTRODUCTION

Since 1960s some Islamic financial institutions had emerged to fulfil the needs of Muslim investors and savers. The main challenge faced by those institutions is how to modify or generate liquidity with various zero-interest financial products in order to mobilize saving. In this context, Sukuk has emerged in Sudan as one of the innovation products of finance with zero interest while combining the features

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of equity and debt securities. This *Sukuk* enables Islamic banks to provide finance for large investment projects instead of the other Islamic financial tools. (Salih, 2012) The issuance of *Sukuk* activate Islamic banks operation through securitization of income generation to provide liquidity for banks. Moreover, the issuance of *Sukuk* plays an initiative role in mobilizing financial resources from the surplus holders allowing besides, it can be traded in the secondary market.

*Sukuk* has been an important financing instrument for many economic entities including governments. Many sovereign *Sukuk* has been issued in the last decade to help financing public enterprises or just as monetary policy and interbank liquidity instruments. Sudan is not an exception from this especially that the entire financial system is deemed to be based on Islamic law. Moreover, the economic problems in Sudan like poverty, public deficit, unemployment, economic sanctions and other issues have created serious need for liquidity where *Sukuk* can help in fulfilling such need.

*Sukuk* can be classified in a variety of ways. AAOIFI classifies *Sukuk* based on their underlying *Shari’ah* contracts. AAOIFI FAS 17 (AAOIFI, 2010) approves 14 types of *Sukuk* although only a handful of these approved types are commonly used. The most common types are *Murabahah*, *Ijarah*, *Mudarabah*, *Musharakah* and *Wakalah* (Mohammed, 2016). A brief presentation for the four main *Sukuk* structures would be important.

1- **Sukuk Al-Ijarah**

*Sukuk Al-Ijarah* is based on the *Ijarah* (lease) contract that involves the transfer of the usufruct of a designated asset or assets for an agreed rental payment over a specified period (until maturity of the *Sukuk*) (Ayub, 2005). The lease structure is similar to conventional leasing except that this contract must comply with *Shari’ah* requirements (Rafay, Sadiq & Ajmal, 2017).

2- **Sukuk Al-Mudarabah**

The *Mudarabah Sukuk* follows the underlying *Mudarabah* contract which is like a silent partnership in conventional terminology. The *Mudarabah* contract is therefore an equity-based contract as one party contributes capital and the other provides the expertise for the purpose of derivation of a profit (Chapra, 1998; Usmani, 1999 as cited in Mohammed, 2016). The profit is shared according to a pre-agreed profit-sharing ratio. In the event of a loss, it is the provider of capital that suffers the loss of capital.

3- **Sukuk Al-Musharakah**

In *Musharakah Sukuk*, parties come together to provide capital to a specific project or business venture by pre-agreeing a profit-sharing ratio. *Musharakah* is an equity-based form of financing as profits are variable and distributed based on actual earnings. *Musharakah* contracts fulfil the profit and loss concept of investment that is a fundamental principle in Islamic finance (Chapra, 1998 as cited in Mohammed, 2016). In pure *Musharakah Sukuk* (equity-based *Sukuk*) that is a partnership in profit, the underlying structure can also be made perpetual in nature as *Sukuk*-holders receive profits from the cash-flows generated through the SPV that holds specified *Musharakah* assets (Mohammed, 2016).
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