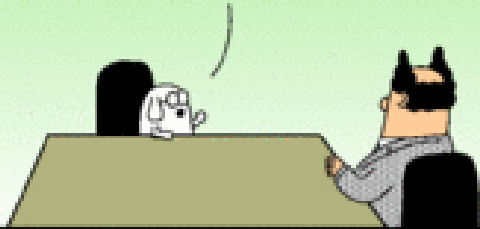


# The Role of Exchanges in Enhancing Islamic Liquidity

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## Contemporary Issues

- Managing liquidity is arguably the most critical element in the risk management framework of the financial industry
- Managing liquidity is even more challenging for IFIs due to limited availability of Shari'ah compliant instruments
- Managing short term Islamic liquidity is especially challenging for IFIs due to the absence of an international Islamic money market
- IFIs worldwide rely heavily on commodity murabaha for short term investment and liquidity management
- In some markets, IFIs also rely on government and central bank's short term Shari'ah compliant issues e.g. Bahrain, Malaysia and Sudan
- Sukuk has also emerged as a tool for managing liquidity though the market is relatively small at around USD130bn when compared to total IFI assets of approx USD830bn
- Other liquidity management solutions remain underdeveloped

## Challenges

- Absence of a uniform regulatory framework to facilitate the development of an international Islamic markets
- Limited diversity in investment tools
- Lack of price transparency resulting in pricing difficulties
- Absence of global benchmark issues
- Maturity mismatch due to limited maturity profiles of instruments
- Limited access to counterparties to trade with
- Secondary markets lack depth and breadth
- Limited connectivity between IFIs as markets tend to be very insular
- No lender of last resort facilities
- Lack of standard documentation
- Different Shari'ah interpretations and acceptance



## Initiatives to date

- The recent establishment of the International Islamic Liquidity Management Corporation (IILM) by IFSB with the objective *to issue Sharī'ah-compliant financial instruments to facilitate more efficient and effective liquidity management solutions for IFIs & facilitate investment flows of Sharī'ah-compliant instruments across borders.*
- The establishment international standard-setting bodies e.g. AAOIFI for the development of accounting and auditing standards for IFIs, IFSB for the issuance of global prudential standards and guiding principles for the Islamic Finance industry and IIFM which focuses on the standardization of Islamic products, documentation and related processes
- Issuance of benchmark sukuk by IDB and GCC & Asian sovereign sukuk
- Issuance of short term instruments by governments and central banks e.g. CBB Sukuk Al-Salam & Al-Ijara, Sudan Musharaka Certificates and Malaysian Islamic Treasury Bills, GIIs and BNM Islamic Notes

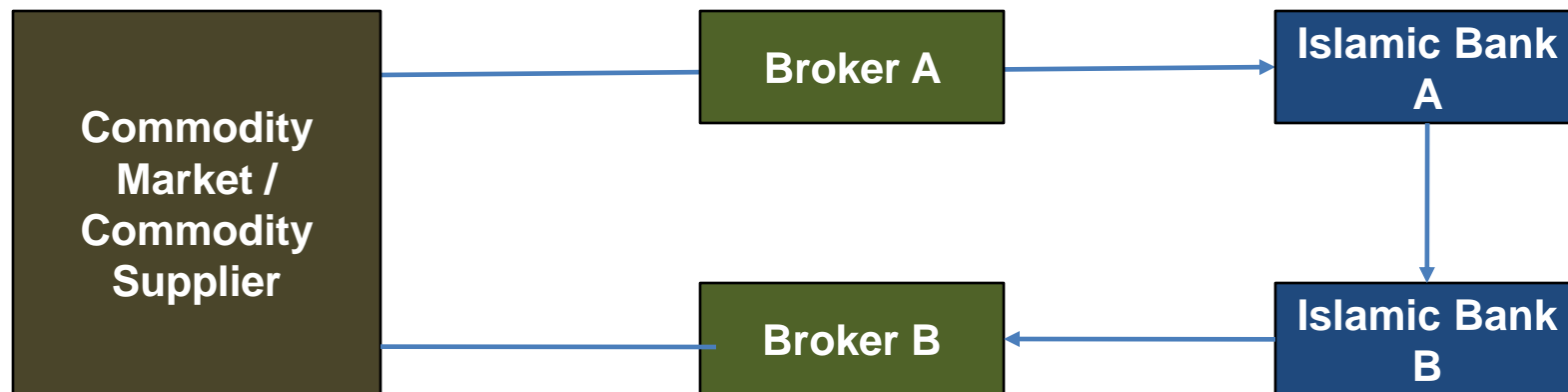
## **An Exchange can facilitate ....**

- The establishment of regulatory frameworks for trading and product offering
- The promotion of organized trades and documentation
- Investor access to a wider array of Shari'ah compliant investment products e.g. sukuk, equities and commodities
- The promotion of the introduction and distribution of new products e.g. i-ETFs, i-REITs & Commodity ETFs
- Cross border trades by enhancing global connectivity
- Price transparency
- Secondary market liquidity
- Mitigating counterparty risks thus expanding trading network
- Entrepreneurs and businesses to raise Shari'ah compliant funds
- The promotion of Shari'ah governance and integrity



## Bursa Suq Al-Sila' – A Case Study

- Malaysia initiated the development of a Shari'ah compliant exchange based commodity trading framework to facilitate commodity murabaha transactions; Bursa Suq Al-Sila' was introduced in August 2009
- Till then trades were conducted through bilateral arrangements between IFIs and commodity brokers



- Islamic Bank A purchases commodity from Commodity Broker A on spot basis
- Islamic Bank A sells the commodity to the Islamic Bank B on deferred payment basis at a profit
- Islamic Bank B sells the commodity to Commodity Broker B for cash

## Bursa Suq Al-Sila' – A Case Study (cont'd)

### Transactional flow



**Example :** Islamic Bank A is financing Islamic Bank B

1. Islamic bank A buys commodity from commodity market on spot.
2. Islamic bank A sells commodity to Islamic Bank B on deferred basis
3. Islamic Bank B then onward sells the commodity to Bursa Malaysia Islamic Services which will then sell it to the market



# THANK YOU

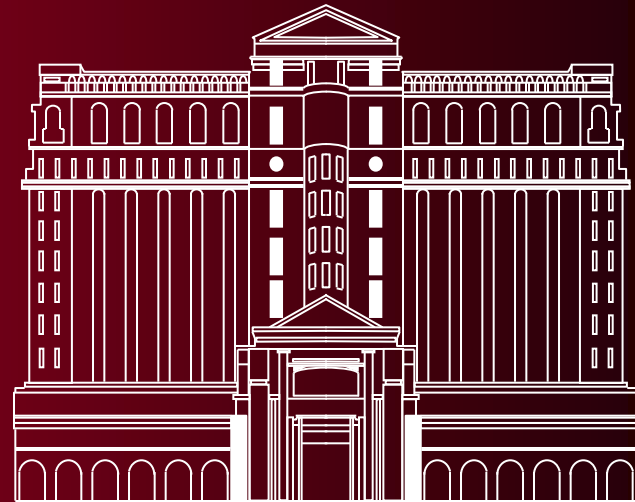
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