

## Innovative China joins the fray

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Who would have thought that two Chinese corporates with serious mainland connections would be spearheading capital market innovation in Malaysia's ringgit market, notching up a number of notable firsts in the process? Their entry into the sukuk market with debut issuances, coincidentally last Thursday, marks a new milestone in the five decades of the contemporary Islamic finance industry.

First, it was Tadau Energy Sdn Bhd, the Malaysian subsidiary of Edra Solar Sdn Bhd and Kagayaki Energy Sdn Bhd, part of the giant Chinese clean energy group, China General Nuclear Power Corporation, who closed "the world's and Malaysia's first green sukuk" — the RM250 million Green Sukuk Tadau. The proceeds of the sukuk will be used to finance the construction of a 50 MWac solar project in Kudat, Sabah under purchase agreements signed with Sabah Electricity Sdn Bhd. The sukuk has been certified as a Green issuance by the Centre for International Climate and Environmental Research in Oslo, Norway.

Next, it was the turn of BEWG Malaysia Sdn Bhd, a subsidiary of Hong Kong-based Beijing Enterprises Water Group Limited (BEWGL), the leading Chinese wastewater and sanitation company, with a RM400 million Sukuk Wakalah, the first ringgit sukuk issued by a Chinese conglomerate for a water infrastructure project and the first sukuk issued by a Chinese company. The proceeds of the sukuk will be used to part finance the RM687 million upgrading of the Bukit Sah water treatment plant in Kemaman, Terengganu.

The last quarter may yet turn out to be game-changing for the global sukuk market, which has US\$350 billion (RM1.49 trillion) of sukuk outstanding. We have seen Saudi Arabia and its oil giant, Saudi Aramco, issuing iconic maiden sukuk both in the international and domestic market, followed by another sovereign issuance last week. Sovereign Indonesia, Oman, Turkey, Qatar, Bahrain; quasi-sovereigns such as Khazanah Nasional, the Islamic Development Bank and a spate of corporates followed suit with a variety of issuances.

Apart from the Saudi activity, for obvious reasons, being the single largest Islamic finance market in terms of assets, it is the two Chinese offerings that have caught the imagination.

Hitherto sukuk activity has been in the other direction — Malaysian entities issuing sukuk to invest in assets in China. Khazanah and Axiata Group have both issued Sukuk in the renminbi and HK dollar markets. Last year Khazanah issued a US\$398.8 million Exchangeable Sukuk, where investors could exchange payments into Khazanah's holding of ordinary shares in BEWGL. Khazanah has pioneered exchangeable sukuk with the first offering involving exchangeable shares into the mainland China outlets of Parkson Retail Group.

The Chinese entry into the Malaysian Islamic finance market is a vindication of Prime Minister Datuk Seri Najib Razak's China policy, which inter alia promotes close cooperation in trade, investment and financial services, including opening the Islamic finance sector to both Chinese investors and fundraisers. It is also the fruit of years of engagement by Bank Negara Malaysia, Securities Commission Malaysia (SC) and Malaysia International Islamic Financial Centre (MIFC) with counterparts in China and Hong Kong.

China's huge infrastructure needs and its combined sovereign wealth holdings of about US\$1.75 trillion, the single largest by any country, are mesmerising opportunities for the Islamic finance

industry to capture. Issuing sukuk in renminbi could also help the Chinese currency's journey to a wider international reach.

The Tadau Sukuk is also a major achievement of Malaysia's efforts in establishing a Sustainable and Responsible Investment (SRI) and Green Bond/Sukuk market. Indeed the Tadau Green Sukuk is the first such issuance under the SC's SRI Sukuk Framework, the first of its kind in the world and developed in cooperation with the World Bank, and established in 2014 as a channel to address global funding gaps in syariah-compliant green financing.

Khazanah has been the trendsetter in SRI Sukuk with the world's first "Pay-for-Success" RM100 million SRI Sukuk Wakalah bil Istithmar in 2015, with a second similar RM100 million tranche last month, the proceeds of which will fund Khazanah's Yayasan AMIR Trust School Programme primarily in rural Malaysia.

Climate and social-aligned finance is a fast-growing market. Backed by the appropriate regulation and public policy commitment, it is ripe for innovation as Tadau and Khazanah have shown in the Islamic space. Their issuance is a mere tip of the iceberg.

In 2016, the climate-aligned bond market grew by 16 per cent to US\$694 billion, US\$118 billion worth of which are labelled green. Global SRI assets totalled US\$22.9 trillion in 2016.

According to the Global Sustainable Investment Review 2016 Malaysia with 30 per cent share in Asia (ex Japan) is the largest SRI market in the region, as it recognises syariah-compliant funds as part of the SRI universe.

The total global primary sukuk market amounted to about US\$89 billion in 2016 and I expect it to top US\$100 billion mark this year.

The Climate Bonds Initiative established a green sukuk working group in 2012 to develop best practices in the space but progress has been slow. Here is another opportunity for SC and Malaysia to lead the way in green sukuk just as it has been doing in promoting Islamic Capital Market under the aegis of the International Organisation of Securities Commissions (IOSCO). IOSCO recently established its first regional office outside its headquarters, in Kuala Lumpur.

The SC, it seems, is up for the task ahead. Tan Sri Ranjit Ajit Singh, SC chairman, at the launch of Tadau Green Sukuk, reminded that the issuance "strengthens Malaysia's position as a leading Islamic finance marketplace as well as its value proposition as a centre for sustainable finance. We believe that there is a significant opportunity arising from strong global interest in green financing where innovative fundraising instruments like green and SRI Sukuk is a viable solution to address global needs for green and other forms of sustainable and responsible financing".

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