

amount was USD250 million and classified based on Sukuk Al Ijarah, with a maturity of 5 years and fixed rental payment (Tariq & Dar, 2007).

Islamic finance has been a phenomenon in the world market, especially with the economic crisis of 2008. Many governmental and private institutions specializing in the financial sector have given importance to this industry that has a growth of 10 to 20 percent and created new markets around the world. This phenomenon has resulted in considerable research and studies through the institutional research of universities or finance centres, or institutions of the Islamic financial system, to develop the stability and growth of the Islamic financial industry.

Islamic finance was born in the Arabian Gulf and the Middle East in the sixties and seventies and then expanded around the world. The financial assets of Islamic finance in 2015 reached USD1451 billion with 480 complete Islamic banks and conventional banks with Islamic windows in 75 countries of the world. The CCG, ASEAN, GCC, and South Asia areas have led the Islamic finance sector in the world, with the Islamic finance assets in the CCG (Saudi Arabia, UAE, Kuwait, Qatar, Bahrain and Oman) reaching USD749.339 billion in 2015. This is why the Islamic Bank of Saudi Arabia Al Rajhi Bank is classified as the largest Islamic bank in the world and in the GCC area, with assets of 82,056 billion dollars in 2015. The other GCC members (i.e., Iran, Jordan, Egypt, and Sudan) constitute the second most active area of Islamic finance with USD425.305 billion. This is led by Iran with the largest Islamic bank, GCC Bank Mellat, with assets of USD52.269 billion, and which ranks as the largest bank in Iran and as the largest Islamic bank in the world. The ASEAN Islamic finance assets (Malaysia, Indonesia, Brunei, Thailand, the Philippines, Singapore) do not exceed 187,610 billion dollars and are led by Malaysia, with the largest market for that industry in the area, followed by the South Asian countries (Bangladesh and Pakistan), which

are the fifth largest market in the world in the Islamic finance industry with bank assets of USD41,059 billion led by Bangladesh (Staff Writer, 2018).

2.2.2 Sukuk Development in Malaysia

The fundamental intensity of Malaysia is to implement the tasks in the most practical and accountable way that would promote resolving specific relevant issues encountered by the community. The religious scholars have been unceasingly preventing the community from the forbidding of riba, and the obligation to avoid any participation in financial transactions that include any suspicious activity of riba. While riba was not effortlessly avoided, the necessity to have a fully clean fund to fulfil Hajj¹ has become a considerable challenge. The Pilgrims Fund and Management Board is known as the PFMB and is one of the most significant Islamic financial institutions in the nation. It not only has large Shari'ah-compliant assets and investments, but also arranges the Hajj pilgrims efficiently (Sukmana & Kassim, 2010).

Sukuk development in Malaysia is a pattern for a success story that has begun to be an essential tool and grants the required capital for the public and corporate sectors. In fact, Malaysia began to be the leading issuer of Sukuk in the world. Malaysia led the development of global Sukuk market with the launch of the Supreme 5-year global Sukuk with a value of USD600 million in 2002. The Sukuk market has encountered improvement with Malaysia actively forming one of the biggest issuers of Sukuk for many years. The development of the market of Sukuk in Malaysia is maintained by an extensive infrastructure development that incorporated the reporting and commercial agreements, and accounted for the dynamic primary market of Sukuk (Ahmad, 2014).

¹ Hajj is in Islamic rite that is an annual religious event and is performed by Muslims who meet the requirements of visiting the holy city Makkah and can afford to do so.

Malaysia proposes one of the best vital alternatives for involvement in this rapidly increasing asset category. Malaysia has more than thirty years of experience in Islamic finance and a comprehensive and extensive conventional domestic industry. Malaysia proposes many appealing and worthwhile proposals for domestic and global Sukuk issuers and investors. The issuance of Sukuk is adjusted by the Securities Commission Malaysia in accordance with the infrastructure provided by the Guidelines on Sukuk.

Sukuk is designed in accordance with a strict Shari'ah-compliant asset exchange agreement. This agreement can be formed by the sale and acquisition of an asset in accordance with deferred profit and the leasing of certain assets. Thus, Sukuk issuance is not a money-for-money swap with interest; it is preferable to swap Islamic-compliant assets for financial circulation that use different Shari'ah comparisons, like Bai' Bithaman Ajil (BBA), Murabaha, Ijara, Mudaraba, and Musharaka, which allow investors to make profit from transactions. Malaysia enjoys a thriving business environment to encourage the development of the Islamic capital market, especially for Sukuk issuance (Salah, 2013). Penetrating the Sukuk market by Malaysia has paved the way for other Islamic countries, such as Indonesia, Saudi Arabian, Pakistan, United Arab Emirates, Turkey, and Bangladesh, to adopt the Malaysian experience.

2.2.3 Sukuk Development in the GCC

The GCC region includes 21 countries as listed by the International Monetary Fund (IMF) (IMF, 2015), the World Bank (WB, 2018), and the office of the United States Trade Representative (USTR, 2018). These countries are “*Algeria, Bahrain, Djibouti, Egypt, Iran, Iraq, Jordan, Kuwait, Lebanon, Libya, Mauritania, Morocco, Oman, Qatar, Saudi Arabia, Somalia, Sudan, Syria, Tunisia, the United Arab Emirates, and Yemen.*” The GCC is simply considered as a group of countries that share the same

region, or to be more specific, countries sharing the same borders. The GCC countries are located in Asia (Middle East) and North Africa. Most of the GCC nations are Muslim with the exception of some countries that have a variety of religions, such as Djibouti. In the majority of GCC countries, there is a lack of political and economic stability (Belkhir, Boubakri, & Grira, 2017). Some of the GCC countries were ruled under communist regimes, such as Egypt, Jordan, Libya, and Syria, and some were ruled under capitalist regimes, such as Yemen, Algeria, Somalia, and Sudan (Naceur, Casu, & Ben-Khedhiri, 2011; Turk Ariss, 2008). However, till today, the finance sector controls all the GCC countries' financial systems. In fact, the capital markets in GCC countries are not proficient or well developed because the central banks in the GCC countries are in full control of the financial systems (Cherif & Dreger, 2016).

According to Tables 2.1 and 2.2 the Saudi Sukuk market occupies the largest domestic Sukuk issuances in the GCC in terms of the total amount issued from 2001-2019, with a percentage of 10.42% of the total domestic issuance during this period, and the third largest international Sukuk issuance with a percentage of 23.39%. The United Arab Emirates (UAE) has preferred to target international domination rather than the domestic market, and its international issuance of Sukuk formed 33.08% of the total international issuance during the period 2001-2019, while its domestic Sukuk issuances reached only 0.97% for the same period. Other countries, such as Qatar and Indonesia, issued 5.72% and 7.70% for the international market, respectively, while their domestic issuance for the period 2001-2019 only reached 2.30% for Qatar and 9.34% for Indonesia.

Table 2.1: International Sukuk Issuance (January 2001- December 2019)

Country	No. of issuances	Value (USD millions)	% of value
Indonesia	21	18,703	7.70%
Malaysia	138	73,183	30.12%
Qatar	22	13,895	5.72%
Saudi Arabia	68	56,826	23.39%
United Arab Emirates	125	80,364	33.08%
Total	374	242,971	100

Source: The International Islamic Financial Market (IIFM) (2020)

Table 2.2: Domestic Sukuk Issuance (January 2001- December 2019)

Country	No. of issuances	Value (USD millions)	% of value
Indonesia	469	80,205	9.34%
Malaysia	6,952	660,565	76.96%
Qatar	31	19,772	2.30%
Saudi Arabia	149	89,465	10.42%
United Arab Emirates	15	8,324	0.97%
Total	7,616	858,331	100

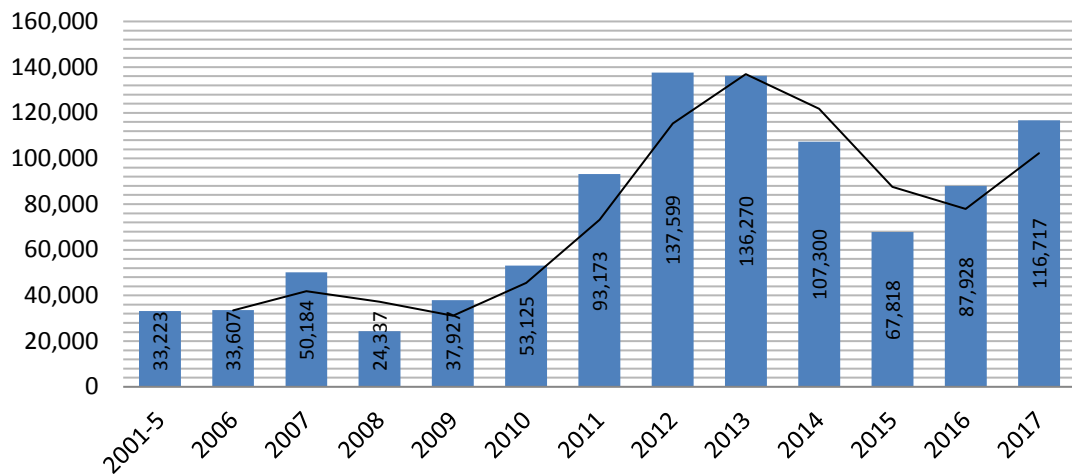
Source: The International Islamic Financial Market (IIFM) (2020)

2.2.4 Global Trends of Sukuk

Since the beginning of the economic crisis, in 2008, Islamic finance has experienced notable growth, as evidenced by the fact that from 2008 to 2012 its assets doubled; from USD720 billion in 2008 to USD1,814 billion at the end of 2014, and 2 trillion dollars at the end of 2015. The Islamic banks reached USD1346 billion in financial assets of the Islamic financial industry in 2014, followed by Islamic bonds (Sukuk) with USD295 billion, Islamic investment funds with USD56 billion, and Islamic mutual insurance services (Takaful) with 33 billion dollars (Thomson Reuters, 2016). Takaful leads the annual growth with 12% and a growth of 10%, respectively,

while the Sukuk and the Islamic funds experienced a growth of 6% and 7%, respectively. However, there was a 45% increase in the reported number of new funds; from 645 thousand in 2013 to 934 thousand in 2014. According to the same report of Thomson Reuters 2015 – 2016, the total Islamic financial assets are projected to reach USD3247 billion by 2020, while the Islamic bank hopes to get its financial assets to reach USD2610 billion in 2020, Sukuk to reach USD395 billion, takaful to USD47.38 billion, and the Islamic investment funds to USD88.58 billion. The considerable growth of the Islamic financial industry in recent years, especially in Islamic countries, has been a phenomenon in the global economy, in which major conventional banks have started offering financial services that comply with Shari'ah, such as Deutsche Bank, HSBC Bank, and Standard Chartered Bank.

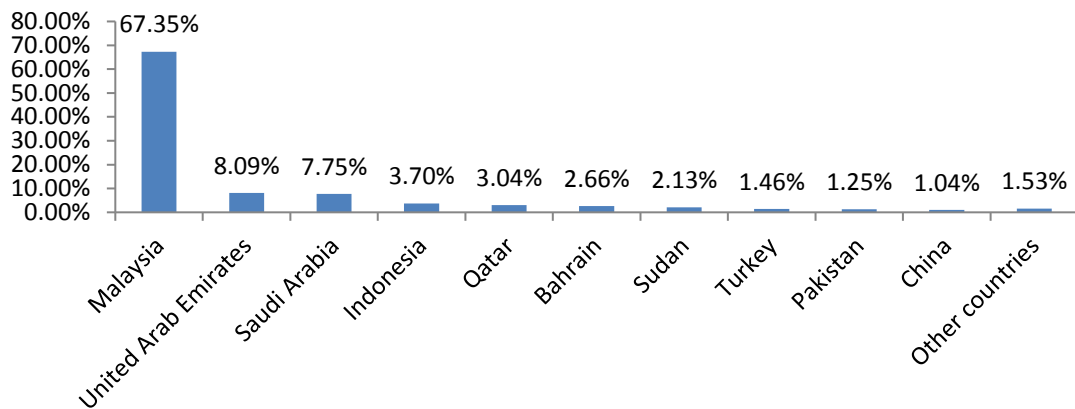
Recently, the new era of the capital market has witnessed a tremendous demand for debt instruments. Furthermore, the global bond market has reached around 50% of the total capital market globally (Tendulkar & Hancock, 2014). The rapid growth of debt market reflects the advantages of filling the business needs from debt. Despite the rapid growth of Sukuk issuances during the last decade, the global issuance of Sukuk witnessed a moderate decline from USD137.5 billion in 2012 to USD60.69 billion in 2015, or by 55.86%; as shown in Figure 2.1.



Source: IIFM Sukuk database

Figure 2.1: Total Global Sukuk Issuance (January 2001 - December 2017), All Tenors, All Currencies, in USD Millions

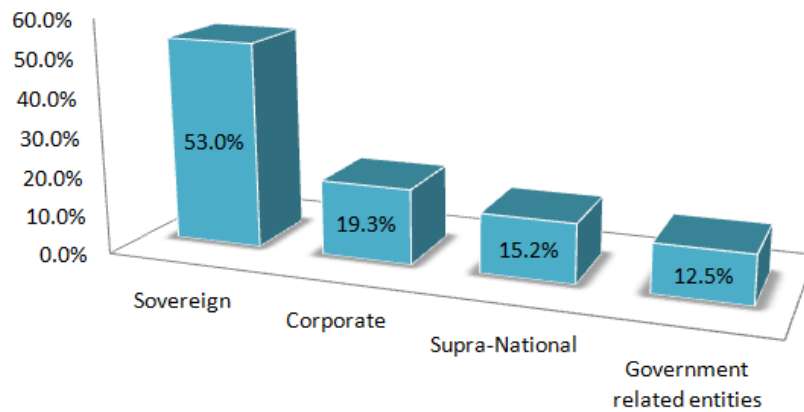
As a result of the link between the financial market and the global economy, the huge decline in oil prices has caused a recession situation, especially for the countries issuing Sukuk, in that most of these countries are closely tied to the oil prices. Despite this sharp decline in the global Sukuk market, the Malaysian financial market of Sukuk is still considered to be the largest Islamic bond hub globally (refer to Figure 2.2) (BNM, 2015b). It is noted that the corporate Sukuk issuance is dominated by 49% compared to the sovereign issuer by 35% and quasi-sovereign by 16%, as of 4Q 2015 (Figure 2.3).



Source: IIFM Sukuk database

Figure 2.2: Sukuk Issuances by Country (4Q2017)

Furthermore, as shown in figure (2.3), the global Sukuk market can be divided into four categories based on the type of issuer: the sovereign Sukuk is the primary issuer with a share of 53% from the total global issuance of Sukuk, while the corporate type comes in second place with 19.3%, and the supra-national and government related entities by 15.2% and 12.5%, respectively. Accordingly, this thesis is motivated to concentrate on the corporate issuer type, through investigating the market reaction towards the corporate Sukuk issuance, and its implications on issuer's stock prices volatility, as well as determining the significant differences due to the type of Sukuk structure.



Source: ISRA database, IFIS, Zawya, Bloomberg

Figure 2.3: Sukuk Issuances by Issuer Type (4Q2017)

2.3 Sukuk vs. Conventional Bonds

Although there are only a few fundamental differences between conventional and Islamic bonds, these differences play a major role in operating the Islamic financial institution according to the law of Shari'ah. Once the Sukuk instrument was placed in the financial market, several studies attempted to identify the main differences between the Sukuk and the conventional bonds. This section illustrates the main criteria of the two instruments in the context of ownership, profitability base, profit source, Shari'ah compliance, pricing base, and capital guarantee; as illustrated in Table 2.3:

Table 2.3: Sukuk and Conventional Bond Comparison

Criteria	Sukuk	Conventional Bond
Ownership	Sukuk is considered as an asset ownership	Bond refers to an obligation of debt
Profitability base	Profit sharing	Fixed income guaranteed by the issuer
Principal value	Sukuk gains its value from its associated asset, if asset value increases, Sukuk value increases in return	Fixed value guaranteed by the issuer
Shari'ah compliance	Compliance with the provisions of Islamic Shari'ah law	No compliance
Capital guarantee	No guarantee for getting back the principal value in case of loss	Principal value guaranteed by the issuer

2.4 Islamic Sukuk Structure

Structuring Sukuk refers to the type of Sukuk purpose, taking into consideration that the structure must comply with Islamic law. The structuring mechanism has a variety of options due to the type of income or the fiscal domains. This section relies on the AAOIFI classifications of Sukuk, which categorized Sukuk structure into seven types. Table 2.4 clarifies the most popular types of Sukuk in the financial market.

Table 2.4: Sukuk Classifications

Structure base	Sukuk types
Asset-based	- Ijarah
Debt-based	- Istisna
	- Salam
	- Murabaha
Equity-based	- Mudarabah
	- Musharakah
Agency-based	- Wakala

Source: AAOIFI

2.4.1 Ijarah Sukuk

Sukuk Ijarah represents a lease contract involving two parties – Sukuk holders and obligatory lessee. Sukuk holders in this structure are considered to be the transaction financiers, those providing the required capital to purchase a fixed asset from party A the seller obligator, which is the same party (the seller obligator) that agreed to lease the asset once the selling transaction of the asset is done. The return from this transaction to the Sukuk holders is the periodical rental from the lessee, which is predetermined the transaction. Figure 2.7 illustrates the Ijarah Sukuk transaction.

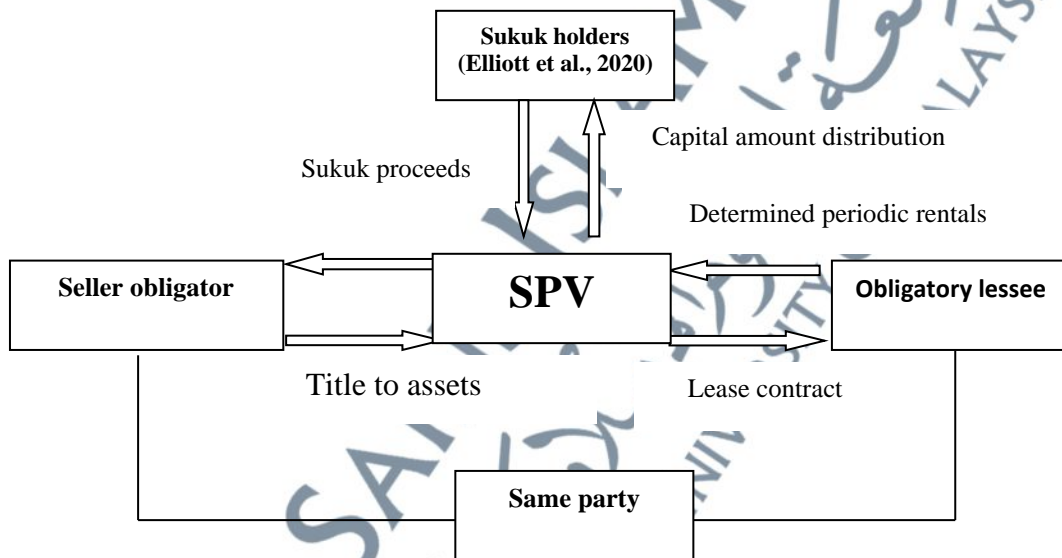


Figure 2.4: Ijarah Sukuk Transaction Structure

2.4.2 Istisna Sukuk

Istisna Sukuk is also known as Sukuk al-istisna'a and is useful for financing large infrastructure projects. Sukuk is derived from Istisna'a, which is the lease of a financial structure. A certificate carries the equal value and is issued with the aim of mobilizing funds required, like producing products that are owned by the certificate holders. A manufacturer/builder agrees to build a well described good or building at a given price

on a given date in the future. Istisna is also a contractual agreement for manufacturing goods allowing cash payment in advance or future payment and future delivery.

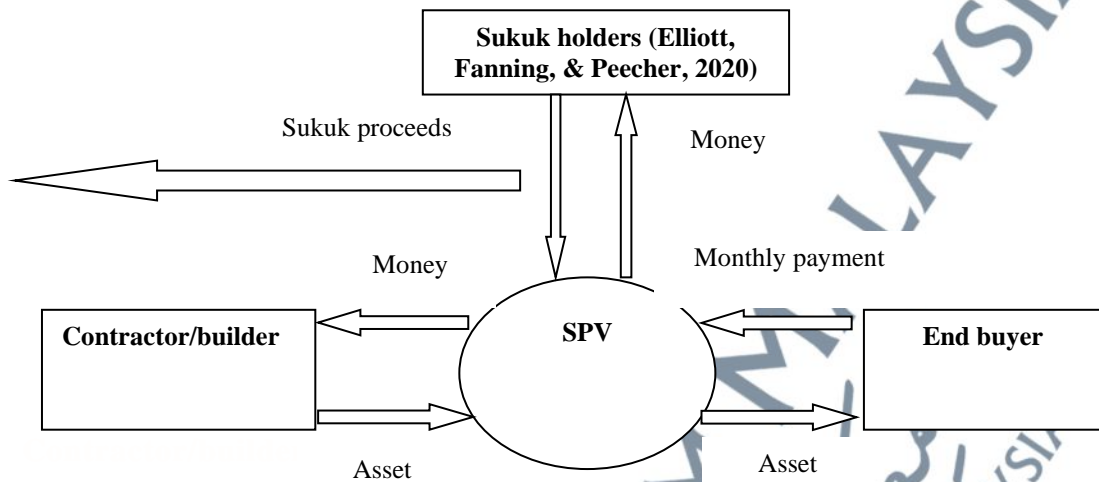


Figure 2.5: Istisna Sukuk Transaction Structure

This is how Istisna Sukuk transaction procedures are implemented as illustrated in Figure 2.5:

1. SPV is the way to issue a Sukuk certificate to raise funds for the project.
2. Sukuk proceeds are the key/used to pay the contractor or builder for them to build and deliver the future projects.
3. Assigned assets means they are transferred to the SPV.
4. The monthly payments and the assets in end buyer are the property/project that is leased or sold to the end buyer. The end buyer will pay monthly instalments to the SPV.
5. The returns are distributed among the Sukuk holders.

2.4.3 Salam Sukuk

This is considered to be a certificate of equal value that is issued for the purpose of mobilizing Salam capital; it is the goods to be delivered on the basis that Salam comes

to the ownership of the certificate holders. The issuer of certificates is a seller of the goods of Salam. The buyers of goods will be the subscribers, and the holders of Salam goods will be sold through a parallel Salam. Salam focuses on the base securities that may be created and sold by an SPV under the funds mobilized from investors and paid in advance to the company SPV in return for delivering a commodity at a future date. SPV can be appointed as an agent in the market. The promise of the quality at the time of delivery at the same time is the higher price. The Salam requirements include full payment by the buyer at the time of affecting the sale, clear enumeration of quality, the quality and standard nature of the underlying assets. The Salam Sukuk transaction structure is shown in Figure 2.6.

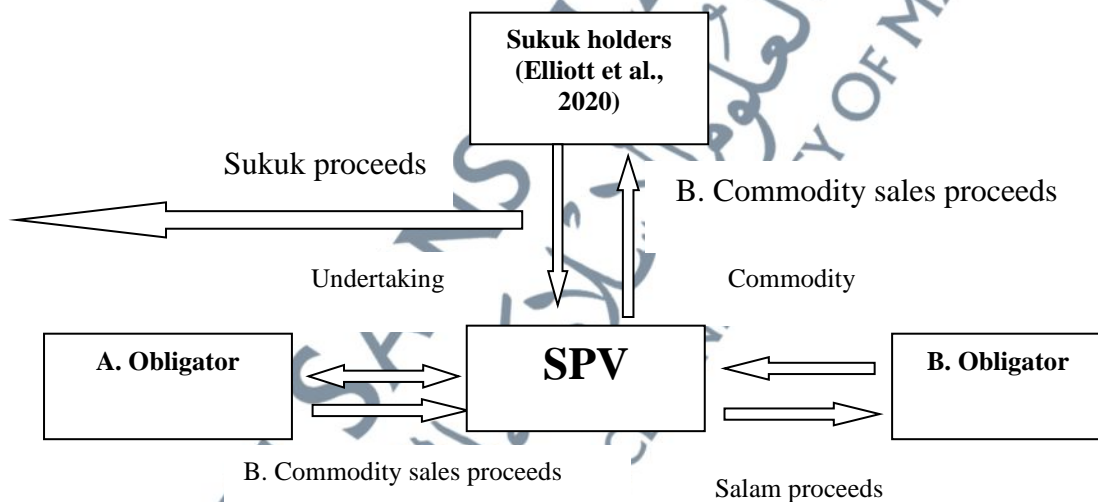


Figure 2.6: Salam Sukuk Transaction Structure

1. SPV sign an undertaking with an obligator. The obligator undertakes the future sale of the commodity for the investors. In the box of A. Obligator shows the arrow sign that means to source both commodities and buyers. The A. Obligator is the way contracts are bought on behalf of the end Sukuk

holders/investor, and now the commodity is the key to sell for the profit of the Sukuk holder or investor.

2. The Sukuk proceeds are the receiver of the Salam certificates that will be issued to the investors and SPV.
3. The Salam proceeds are passed on the B. obligator that sells the commodity on a Salam basis.
4. SPV will now receive the commodities from the B. obligator.
5. The A. commodity sale proceeds onto the A. obligator, who, on behalf of the Sukuk holders/investors, will sell the commodities profit.
6. Then Sukuk holders/investors will receive the commodity sale proceeds.

2.4.4 Murabaha Sukuk

Sukuk Al-Murabaha represents a selling contract of an asset that is financed by Sukuk holders. The financier pays to the SPV, which holds an agreement with the borrower (mostly financial institutions) to purchase the asset and re-distribute it to other potential buyers. Sukuk holders gain from this contract a determined profit plus the principal. Figure 2.7 illustrates the Al-Murabaha Sukuk transaction.

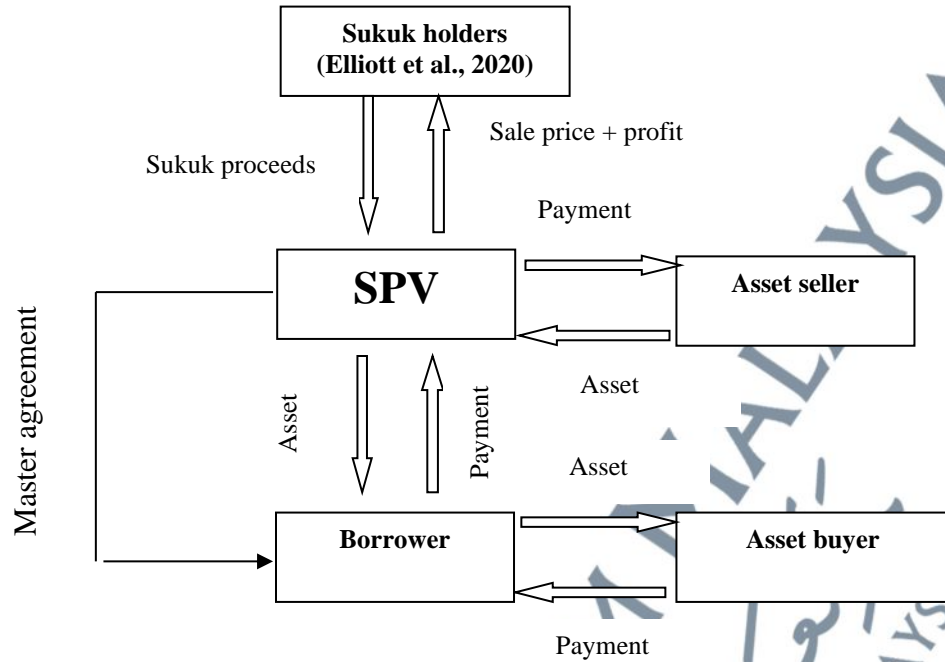


Figure 2.7: Murabaha Sukuk Transaction Structure

2.4.5 Musharaka Sukuk

Musharaka Sukuk represents a venture contract of profit and loss sharing. Sukuk holders in this contract have the right to participate in managing the Musharaka transaction. Sukuk holders gain a predetermined ratio of profit from the venture, while losses are broken down in accordance with the capital proportions. The main purpose of the Musharaka Sukuk is to finance an existing project or establish a new one. Figure 2.8 illustrates the Musharaka Sukuk transaction.

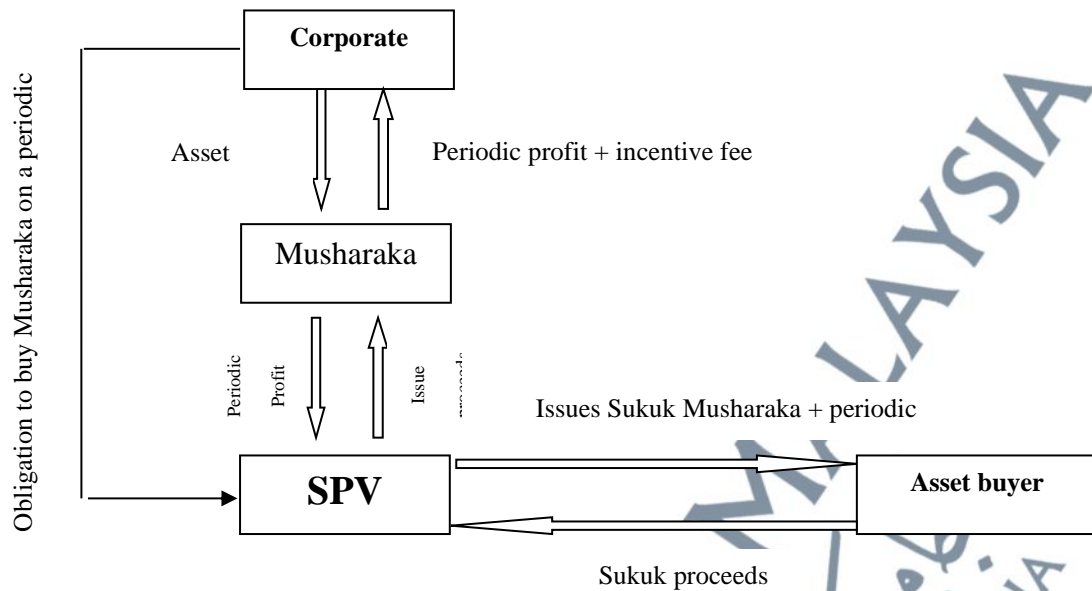


Figure 2.8: Musharaka Sukuk Transaction Structure

2.5 Sukuk Issuance

The Islamic finance is run by the common principle of prolonging the fundamentals of the religious beliefs in Shari'ah financial contracts and transactions. Shari'ah law prohibits the sale and acquisition of debt agreements, earnings taken without actual economic performance, as well as performances that are not considered to be Halal, or Shari'ah-compliant. Only interest-free patterns of finance related to investments that do not incorporate any involvement with pork, alcohol, firearms, or adult pleasure are considered permissible in Islamic finance. Islamic finance fundamentals ensure that contractual confidence and a reciprocally advantageous balance are supported between the lenders and borrowers. Inasmuch as Islamic law does not acknowledge the time element of money as occurs in standard finance, payment liabilities are fixed and cannot be varied after an agreement has been completed (Yatim, 2009). The framework of Sukuk has to be reaffirmed and accepted by a Shari'ah adviser, who is assigned by the issuer. A Shari'ah adviser may be an individual Shari'ah adviser maintained by the Shari'ah Committee linked with a financial organization that

performs Islamic finance activities and accepted by Bank Negara Malaysia (Ariff & Safari, 2012).

The contractual connections between financiers and borrowers are not controlled by capital-based investment benefits but share the business risk from the entrepreneurial investment in terms of legitimate performance. Any financial transaction under Shari'ah law indicates direct involvement in asset activity and appoints to financiers clearly distinguishable rights and responsibilities for which they are qualified to accept equivalent earnings in the shape of state-conventional remunerations. The earnings are made in line with Shari'ah instructions and are not able to be assured ex-ante but only arise from if the investment itself concedes earnings. Of all the quickly increasing Islamic capital market pledges, none have gained as much popularity as Sukuk. The Islamic finance sector, on average, has grown by approximately 15% over the last three years in response to an abundance of investment commodities, which has been filled with the growing need for investments that comply with Islamic law (Soon, 2021).

Recently, more than USD800 billion were registered in Islamic banks, insurance projects known as takaful, mutual funds, and Islamic affiliates of standards banks. The most well-known pattern of Islamic finance is Sukuk, which is a wholesale, asset-built capital market protection. Recent years have evidenced a rush in Sukuk issuance by corporative and public sector organizations due to the increasing need for disjunctive investments. Sukuk does not pay interest but makes a profit via real transactions, like profit sharing. Although Sukuk is designed in accordance with the corresponding method for standard asset-backed securities, it has a remarkable variety of basic forms and supplies. Most significantly, Sukuk, similar to other Islamic financial tools, needs to abide by Shari'ah, which bans the invoice and remuneration of interest and determines that earnings should be obtained from a primary actual business risk rather

than as assured profits from a loan. Therefore, Sukuk does not provide obvious earnings assurance. Intrinsically, investors possess the primary assets through a Special Purpose Vehicle (SPV), which finances unprotected remunerations to investors from direct investment, in fact, religiously authorized economic performance. The Sukuk issuers replace capital market investors for traditional lenders as the source of financing by transforming the anticipated profits from reciprocal risk sharing between lenders and borrowers in Shari'ah-compliant finance agreements, such as transactions, into tradable protection. Consequently, Sukuk refines the objects of three dominant patterns of Islamic fund – Murabaha, Ijara, or Musharaka (Godlewski, Turk, & Weill, 2010).

2.6 Sukuk Issuance Process

The Sukuk issuance process is quite different from conventional bonds. The Sukuk issuance process is considered more complicated compared to the process of issuing conventional bonds (Jobst, Kunzel, Mills, & Sy, 2008). The Sukuk issuance process takes a longer time than conventional bonds, which results from the multiple parties involved in the issuance process. The Shari'ah advisor is considered to be one of the most involved parties in issuing Sukuk, as they ensure full compliance of the Sukuk structure with Islamic law, which does not feature in issuing conventional bonds.

2.6.1 Involved Parties

Table 2.5 illustrates the ten main parties involved in the Sukuk issuance process as required by the Bank Negara Malaysia (BNM), the Securities Commission Malaysia (SCM) and the Central Bank of Indonesia, while the Saudi regulator represented by the Saudi Ministry of Finance does not have the Shari'ah advisor.

Table 2.5: Parties Involved in Sukuk Issuance

No	Parties	Task description
1	Originator	A firm that seeks to get financing source to develop an existing project, or to establish a new one.
2	SPV	The Sukuk issuer on behalf of the sponsor.
3	Trustee	The observer of the timeline of Sukuk issuance from the beginning to the redemption phase (on behalf of the Sukuk holders).
4	Manager/lead arranger	Party that manages and arranges the issuance process (usually a financial institution).
5	Paying Agent	Is responsible for arranging the flow of payments between the issuer and the Sukuk holders (mostly the lead arranger of issuance).
6	Shari'ah advisor ²	A party that verifies the compliance of the Sukuk structure with Shari'ah law (appointed by the issuer).
7	legal counsel	A party that takes care of drafting and arranging the required documents for the issuance (represented by a team of solicitors. appointed by the issuer)
8	Chartered accountant	A party that verifies the audited financial statements of the originator.
9	Sukuk holder	Investor who seeks to invest their capital in Sukuk.
10	Credit Rating Agency	A party that provides an independent assessment of the related credit risk of the issuer.

2.6.2 Issuance Process Flow

The issuance of Sukuk passes through several process steps. Figure 2.9 illustrates twelve of the steps concerning the issuance of Sukuk in Malaysia and Indonesia, while the sixth step is excluded in the issuance process in Saudi, the UAE, and Qatar as the regulator does not have Shari'ah advisor. These twelve steps are conducted within four phases of the process, as follows:

² Shari'ah advisor must be approved by the authority. In the case of Malaysia, the Shari'ah advisor must be approved by the National Shari'ah Advisory Council. In this regard, Datuk Dr Mohd Daud Bakar is one of the top Shari'ah advisors and has verified almost 349 Sukuk issuance over the period 2001-2014.

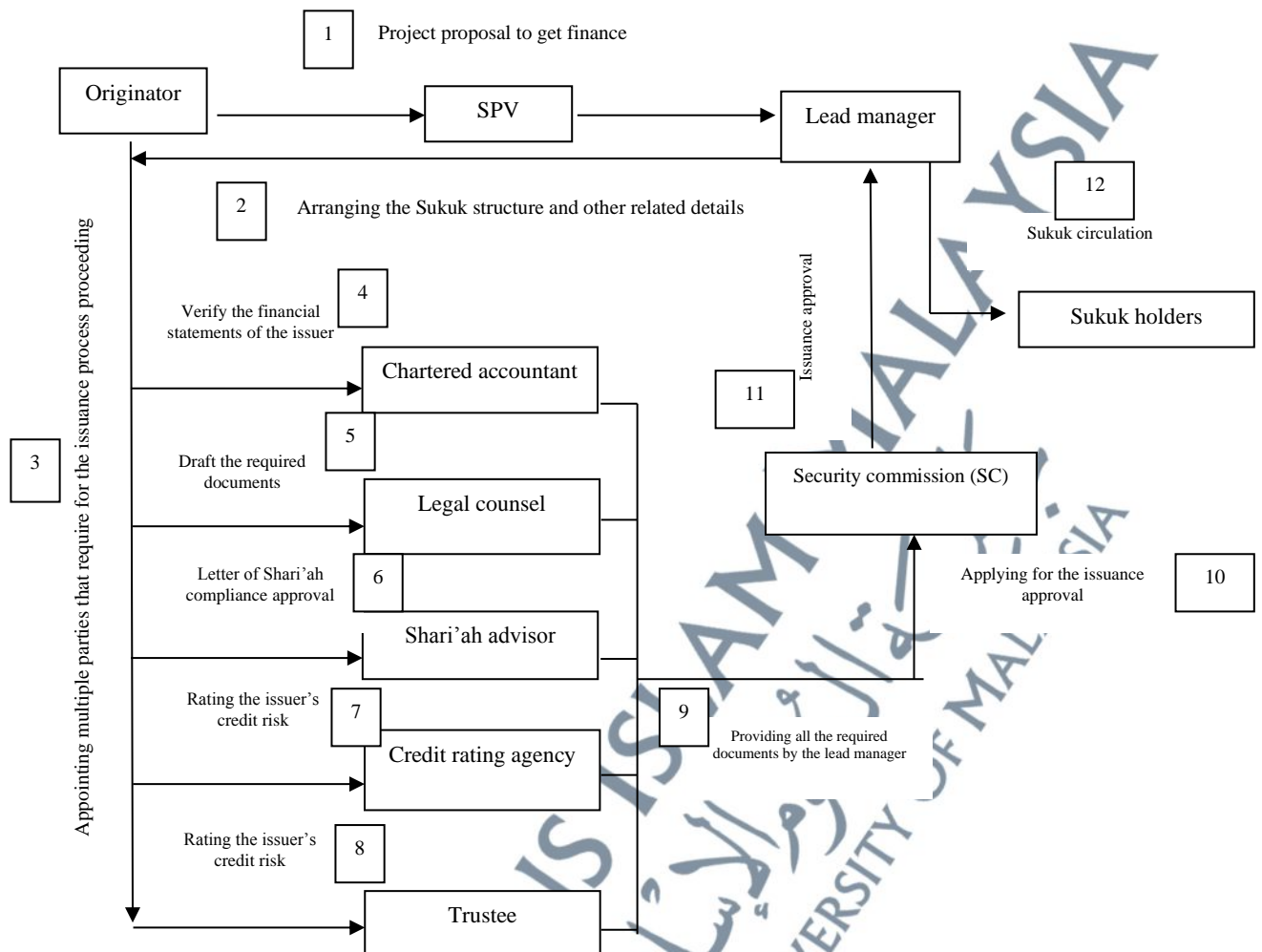


Figure 2.9: Sukuk Issuance Processing Flowchart

The first stage is the preparation of a sukuk proposal, which comprises two steps:

1. In this step, the firm seeks for a fund to finance a new project/asset or develop an existing project/asset prepares a proposal, which clarifies all the related details to the project or asset. The proposal will then be delegated to a Special Purpose Vehicle (SPV) that facilitates the issuance process transaction.
2. The originator is a point manager for the issuance process transaction. According to the Malaysian Securities Commission (SC); three types of managers can handle the Sukuk proposal and submit it to the commission – investment banks, Islamic banks, or international brokers.

The second stage is preparing the required documents. These are undertaken in steps three to eight:

3. This step involves completing all the required documents that must be prepared. The lead manager of the transaction on behalf of the originator appoints five parties, in which each party prepares a specific document that is required for the issuance process transaction.
4. A chartered accountant or audit firm will be appointed to verify the financial statement of the issuer. The financial statement clarifies any potential risk that may result from the financial position of the issuer.
5. The legal counsel or a team of lawyers work together with the lead manager in drafting the legal documentation for the issuance process.
6. A Shari'ah advisor is appointed to verify that the Sukuk structure complies with Islamic law. If the Shari'ah advisor considers that there is a lack of compliance, the Sukuk structure must be revised to follow the Shari'ah requirements.
7. The credit rating agency³ provides its opinion in regard to the credit risk of the issuance. The credit rating agency follows a specific and accepted methodology in identifying the potential risk related to the issuance and the quality grade.
8. The trustee is the party appointed by the lead manager and who takes the responsibility to protect the Sukuk holder's interests. The trustee verifies the compliance of the Sukuk issuance with the Sukuk holder's interests.

³ Most of the Sukuk issuers have to rate their issuances by an authorized agency. In Malaysia, there are two credit rating agencies: Rating Agency Malaysia (RAM) and Malaysia Rating Corporation (MARC). In the United Arab Emirates, the Dubai chamber recognizes the credit rating for the Sukuk issuances. In Indonesia, Kasnic Credit Rating Indonesia (KCR), PEFINDO Credit Rating Indonesia, and the latest entrant into the market is the ICRA Indonesia.

The third stage is applying for SC approval, which follows three steps:

9. All the required documents prepared in the previous phases must be submitted to the SC. The lead manager on behalf of the issuer takes the responsibility for applying for the SC approval and attaches all the required documents according to the SC guidelines.
10. From one to a few months will be taken by the SC to make the decision. In case of the failure of providing the required documents, the lead manager has to fulfil the requirements to meet the approval conditions.
11. The SC takes the decision to approve or reject the application.

The final stage is sukuk circulation:

12. Once the lead manager gets the SC approval, the lead manager proceeds to the Sukuk circulation. Noting that most of the Sukuk underwriters are financial institutions that pledged the circulation in earlier phases of appointing the leader manager.

2.7 Sukuk Issuance Announcement

The Islamic bonds and bond market drivers, the positive responses hypothesized as coming after the Islamic debt issuance announcements are as follows:

1. Inexpensive financing price: greater liquidity of Islamic debt protection because of broader investor base compared to standard debts disputably accounts for the transaction costs of issuing Islamic securities and the price of debt becoming lower than corresponding prices of regular obligations.
2. Appeal to investors: the Shari'ah-compliant stocks have a broader investor base encircling both ordinary and Islamic investors. The massive development of Islamic stocks in Malaysia in recent years confirms the

greater need for Shari'ah-compliant funds compared to non-Shari'ah funds. This interprets why 85% of total securities in Bursa Malaysia are Shari'ah-compliant (Jobst et al., 2008).

The funds brought up from the Islamic debt proposals are utilized to fund new projects. According to the earlier discussion, the stock market value is affected by the Sukuk announcements due to several aspects of the issuer. According to the previous debates, it is assumed that everything else being equal:

1. The scale of the issuer is negatively related to the firms that have a less asymmetrical data issue.
2. The scale of the issue is positively related to the stock market reaction when providing much information content for the issuance.
3. The higher the potential investment, the higher possibility of a positive market reaction.
4. The free cash flows of the issuer are positively related to the stock market reaction since the larger the free cash flow, the greater the decrease in the agency cost accomplished via the utilization of debt funding.
5. The leverage of the issuer is negatively related to the stock market reaction – the lower the leverage, the higher the likelihood that the organization could benefit from the reduction of interest on tax.

2.8 Sukuk Secondary Market in Malaysia

The secondary market has been defined by the BNM as the financial market for the trading of bonds that have already been issued in the primary market. The retail investors have the right to buy or sell both corporate and government bonds from/to any principal dealer or bank. The secondary market operations in Malaysia comprise two

types of Sukuk, listed and unlisted Sukuk. Listed Sukuk is traded by the Securities Commission (SC), while unlisted Sukuk is largely traded Over the Counter (OTC). The following sections provide more explanation for the secondary market emergence, supervisory, development, and trading activities process by the Electronic Trading Platform (ETP).

2.8.1 Secondary Market Emergence

The Malaysian government developed a secondary market for bonds – Islamic or conventional – to achieve two objectives; first, to widen the demand for government securities, and, secondly, to improve the market liquidity. In this regard, the Malaysian government, represented by Bank National Negara (BNM), established the Principal Dealer (Gunathilaka, Smart, Fleming, & Hasan) system in 1989, which is part of the government initiative to boost the public debt securities. The BNM has approved 12 financial institutions to guide the secondary market activities; PD undertakes to perform the secondary market activities according to the BNM and SC guidelines.

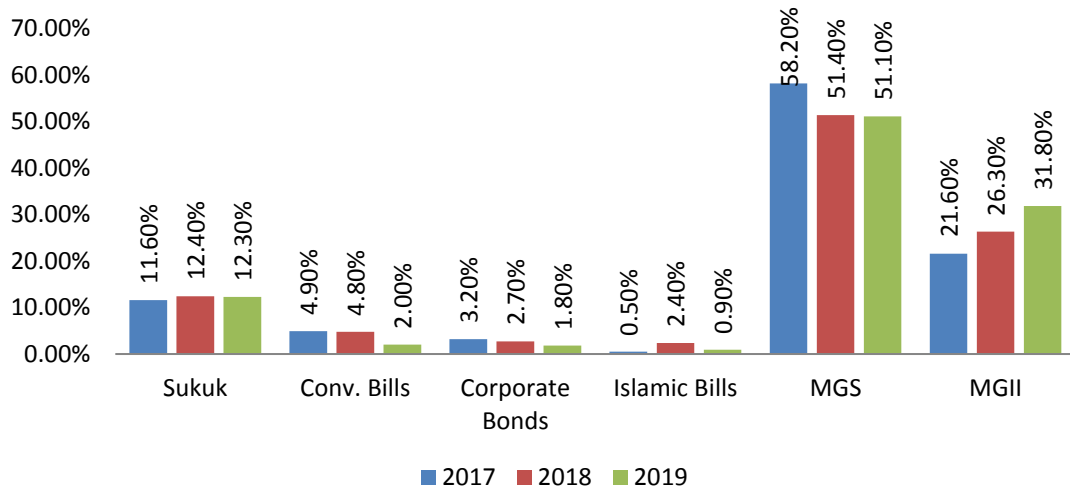
The rapid development of Islamic finance since the late 2000s in Malaysia has driven BNM to establish a parallel system for the Islamic debt securities. In 2009, BNM introduced the Islamic Principal Dealer (I-PD) system to play an integrated role with the PD. The BNM appointed six financial institutions to handle the Islamic debt securities within the secondary market. The I-PD abide by a set of criteria from the BNM, which include the ability of these dealers to trade with large volume transactions and their capability of managing market risk. Furthermore, a semi-annual assessment is performed by BNM to evaluate the I-PD and PD performance as well as their ability to handle the secondary market activities.

2.8.2 Secondary Market Supervisory

BNM has full authority to regulate the corporate debt securities until July 2000. After that, the corporate debt securities will be regulated under the SC's purview. BNM continues to support corporate debt securities by developing the debt market infrastructure. The SC issued several guidelines for regulating the secondary market, as well as regulating the trading activities within the secondary market, besides its cooperation with BNM in inspecting the principal dealers' effectiveness.

2.8.3 Secondary Market Development

The secondary market of bonds has witnessed a notable development over the last three years, 2017-2019. According to the issued bond league table by Bank Negara Malaysia (BNM), the total trading activities within the secondary market recorded RM1.95 trillion in 2017; corporate Sukuk had occupied 11.6% of the overall trading activities, recording a growth of 2% compared to 2016 and amounting to RM174.34 billion. While the secondary market's share of the corporate Sukuk in 2018 recorded a growth of 0.8% compared to 2017, which occupy 12.4% of the total trading activities within the secondary market; while the total trading in 2019 grown by 49% to reach RM2.3 trillion, Sukuk had occupied 12.3% from the overall trading activities as shown in Figure 2.10.



Keywords: MGS: Malaysia Government Securities; MGII: Malaysia Government Investment Issue

Source: Bank Negara Malaysia's (BNM) bond info hub

Figure 2.10: Secondary Bond Market – Malaysia

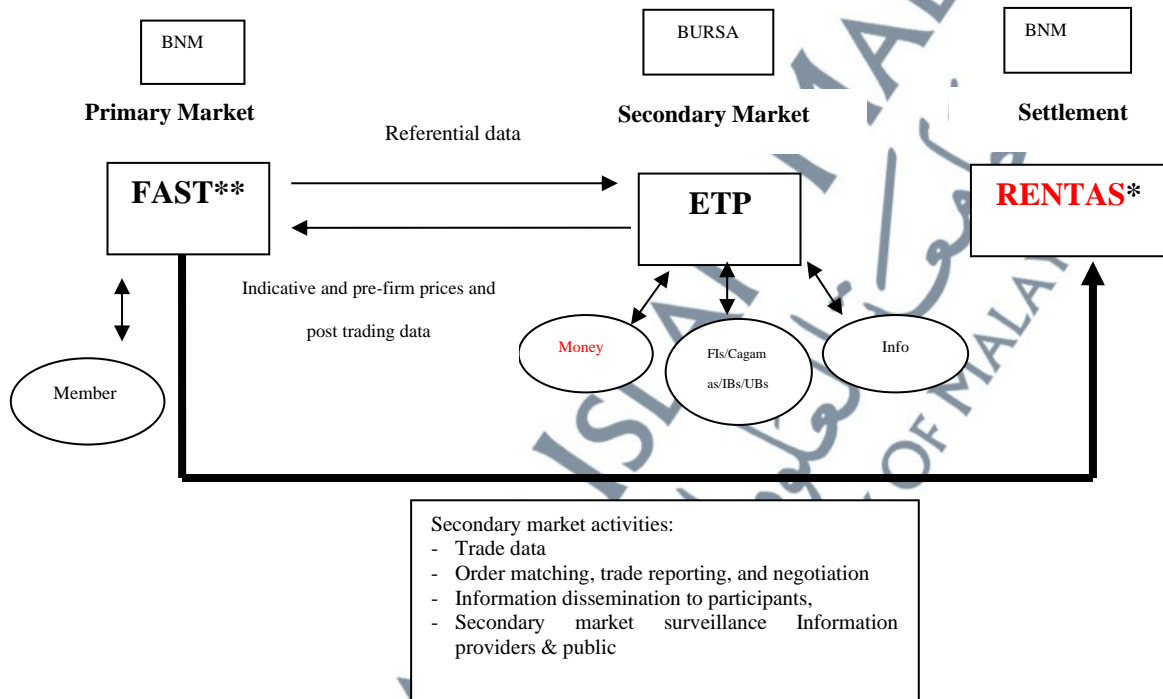
2.8.4 Electronic Trading Platform (ETP) Process

The Electronic Trading Platform (ETP) is a registered electronic facility and is considered to be one of the essential secondary market pillars, which is structured as a real time investor based order driven platform and has the following features: (1) order matching, (2) trade negotiation, (3) trade reporting, and (4) information dissemination.

An Electronic Trading Platform (ETP) for the Malaysian bond market was launched by Bursa Malaysia in March 2008, in line with the National Bond Market Committee's mandate to develop a single electronic trade reporting and trading platform for the domestic bond market. The ETP is operated by Bursa Malaysia. The ETP provides the secondary market with the following facilities:

1. Mandatory reporting of all secondary bond market transactions by taking over the function from the Bond Information Dissemination system (BIDS), which was operated by Bank Negara Malaysia.

2. An electronic order matching platform for the matching of bid and ask quotes for MGS, GII, and corporate issues.
3. An advertisement and a negotiation platform, where the dealers can advertise and negotiate for 'one-to-one' deals for all debt securities and Sukuk; as illustrated in Figure 2.11.



*RENTAS; Real Time Electronic Transfer of Funds and Securities System
 **FAST; Fully Automated System for Issuing/Trending

Figure 2.11: ETP Business Infrastructure – Malaysia

2.9 Sukuk Rating Frame

2.9.1 Credit Rating

Credit rating is an assessment opinion from the rating agency, it assesses the default risks for a particular firm or obligation in a particular time (Securities & Commission, 2003). Usually, rating agencies use three predictors for assessing the related default risks, the first predictor stands on the financial ratios (e.g. return on

assets, return on equity, earnings per share, leverage, liquidity, risk solvency), the second predictor is more related to the legislation side, which concerns the compliance with the corporate governance, while the third predictor relies on the economic indicators, such as gross domestic production, inflation rate, and interest rate (Kamarudin, Kamaluddin, Manan, & Ghani, 2014).

2.9.2 Rating Agencies

Rating agencies are one of the information providers parties; this information plays a major role in taking decisions by the market participants, such as trustee institutions, investors, securities commission, and government bodies. This information provides support for the market participants in their decisions. The rating agencies are divided into international and local agencies. At the international level there are three reputed rating agencies – Standard and Poor's, Moody's, and Fitch. For the local level, each country has one or more private rating agencies that help market participants in making their investment decisions. In respect of the Southeast region, Malaysia, as the largest hub of Sukuk issuing has two private rating agencies: Rating Agency Malaysia (RAM) and the Malaysian Rating Corporation (MARC). These two credit rating agencies play a major part in providing an assessment opinion about Sukuk issuers and Sukuk issuance. In Indonesia, PT Pemeringkat Efek Indonesia (PEFINDO) and PT Kasnic Credit Rating Indonesia (ICRA) are the two licensed credit agencies for providing opinion. In respect of the GCC credit rating agencies for Sukuk, in Saudi Arabia there is only one licensed company, Saudi Credit Bureau (Yacob, Jamaluddin, Rahman, Mustafa, & Yusop), which was approved by the securities commission in February 2017, noting that the earlier Sukuk issuances were rated by international

agencies – Standard and Poor's, Moody's, and Fitch. In the United Arab Emirates (UAE), the Dubai chamber provides its rating services for firms and debt issuances.

2.9.3 Rating Sukuk

In terms of the Sukuk context, similar to conventional bonds, Sukuk issuer and issuance must go through a rating agency upon issuance, as well as at least one time over the tenure of Sukuk. This rating is approved by a certificate of credit rating for the issuer and the underlying asset. Similar to the conventional bonds, rating the Sukuk ranges is based on the issuer's ability to meet its obligation, which can be evaluated as stated above by several predictors. Rating the Sukuk range varies among the credit rating agencies; for example, RAM has eight rating ranges: AAA, AA, A, BBB, BB, B, C, and D. The highest rating range, AAA, refers to superior safety for payback payment, while the lowest rating D refers to a default situation of the issuer for the payment obligation.

2.10 Stock Market Index

A stock market index is a statistical indicator of the movement of the price of certain shares listed on the market and is representative of a segment thereof. It serves as a reference for wealth management and serves as an underlying for certain financial instruments. The first Stock Indices were created to reflect the behaviour of a set of securities over a period of time. One of the oldest is the Dow Jones Industrial Average, known as the Dow Jones, which was created by Charles Henry Dow in conjunction with the Wall Street Journal in the late 1800s to measure US economic and financial activity (Smith, 2004). Another of the most powerful indices is S&P; this index is prepared by

Standard & Poor's and compiles the 500 largest companies in the United States, among them, Apple, Microsoft, and Coca Cola.

The indices are calculated and disseminated by specialized companies or by the market itself, their main utility being the observation of the behaviour of a certain series of listed securities to serve as a reference, and, thus, use them as underlying assets for derivative products, thus contributing more liquidity to the market (Sutcliffe, 2006). The main utility of a stock market index is that it allows the evolution of a market as a whole to be measured with a single number. If a stock index rises 2%, that means that, on average, the shares of the companies that make up the index have risen by the same percentage.

There are usually two ways to weight an index: the classic and by market capitalization. The classical weighting interprets all companies equal regardless of the value and number of shares. In contrast, the market capitalization weight takes into account, to a large extent, the value and number of shares of a listed company. This type is much more complex to calculate, but more efficient since each company is computed by its specific weight. So much so, that most of the world's stock indices are made up of capitalization. The differentiation by means of the weighting is given because, in the financial markets, there is a possibility of having to compare two securities with different capitalizations from different sectors or countries in an established period of time (Smith, 2008).

This study aims to identify the stock market response to three main activities of Sukuk. In this regard, this study tests the stock market response within three scopes of investigation: stock market reaction, stock market volatility, and stock market liquidity.

This investigation involves three categories, the first category, stock market reaction, comprises two regions Southeast Asia (including the Malaysian stock market index and

the Indonesian stock market index), and the GCC (includes Saudi stock market index, United Arab Emirates stock market index, and Qatar). The second category, for stock market volatility, focuses on the Malaysian stock market index and the Indonesian stock market index. The third category, for stock market liquidity, only involves the case of the Malaysian stock market index. Table 2.6 clarifies the five indexes covered by this study.

Table 2.6: List of Indexes Covered by This Study

No	Stock market scope	Index Symbol
1	Malaysian stock market	KLCI
2	Indonesian security market	JKSE
3	Saudi security market	TASI
4	Qatar security market	DSM
5	United Arab Emirates security market	ADSMI

The Kuala Lumpur Composite Index (KLCI) index was established in 1977. This index comprises the 30 largest companies, as measured by market capitalization, listed on the Main Board of the Bursa Malaysia. It is a free-float (minimum of 15%), capitalization-weighted stock market index. The Jakarta Stock Price Index (JKSE) is a major stock market index that tracks the performance of all companies listed on the Indonesia Stock Exchange. It is a modified capitalization-weighted index. The Jakarta Stock Price Index had a base value of 100 as of 10 August 1982. The Tadawul Saudi Index (TASI) is a major stock market index, which tracks the performance of all companies listed on the Saudi Stock Exchange. The index had a base value of 1000 as of 1985, and it was reorganized on 30 June 2008. The Doha Security Market (DSM) is a major stock market index that tracks the performance of the 20 most liquid companies traded on the Qatar stock market. It is a capitalization weighted index. The DSM index

had a base value of 1000 as of 31 December 1999. The Abu Dhabi Securities Exchange (ADX) is a benchmark stock market index that tracks the performance of stocks listed on the Abu Dhabi securities exchange. It is a capitalization weighted index. The ADX index had a base value of 1000 as of June 2001.

2.11 Stock Market Liquidity

Liquidity can be defined as the ability to trade an asset in the market with ease, that is, expeditiously, with low transaction costs and little price impact (Fang, Noe, & Tice, 2009). At first glance this seems to be well established, and liquidity is a concept widely used by investors worldwide. But what is not so obvious is whether liquidity is valued, that is, if there are predictions in stock market liquidity that are explained by the Sukuk liquidity (Hanafi, Hamid, & Yunus, 2018).

Liquidity is a factor that could be valued by the market since liquidity (or rather illiquidity) is a risk that the investor must face when trading a bond in the market (Butler, Grullon, & Weston, 2005). Illiquid assets will surely be more difficult to buy and sell, incurring higher transaction costs, and, possibly, suffering a lag between the time of placing the order and the transaction itself (Nguyen, Duong, & Singh, 2016). In conclusion, liquidity can be a source of risk, so it would affect the prices, spreads, and returns of bonds.

Stocks have liquidity as one of their characteristics, since they have the possibility of generating a return when sold on the market at the market value; this concept relates to liquidity. Stock market liquidity refers specifically to its ability to be quickly transformed into money (Singh, Gupta, & Sharma, 2015). The liquidity describes the extent to which an asset can be bought, sold quickly, and at stable prices. In simple terms, it is a measure of how many buyers and sellers are concerned, and whether

transactions can be carried out easily. Liquidity is normally calculated by taking the volume of trades or the volume of trades on the market (Amihud, Mendelson, & Pedersen, 2012).

High levels of stock market liquidity arise when there is a significant level of trading history, and there is a high supply and demand for an asset since it is easier to find a buyer or a seller. If there are only a few market participants trading infrequently, it is called an illiquid stock market. Stock market liquidity is important for many reasons, but mainly because it affects the speed with which positions can be opened and closed (Kahraman & Tookes, 2014). A liquid stock market is generally associated with less risk, as there is always someone willing to take the other side of a given position. This can attract speculators and investors to the stock market, which adds to the favourable stock market conditions. In a liquid stock market, the seller will quickly find a buyer without having to cut the price of the asset to make it attractive. Conversely, a buyer will not have to pay a larger amount to secure the asset they want (Amihud, Hameed, Kang, & Zhang, 2015).

The liquidity of an asset is also a key factor in determining the margin that a leveraged trading provider, such as Sukuk, can offer. High liquidity means that there are a large number of orders to buy and sell in the underlying stock market. This increases the probability that the highest price that any buyer is willing to pay and the lowest price that any seller is willing to accept, it will come closer. In other words, the bid-offer spread will narrow (Hamiza & Hamid, 2017). As asset prices derive from those of the underlying stock market, a lower bid-offer spread will translate into lower spreads offered on the platform. If a stock market is illiquid, it could mean that there is a much wider margin. The liquidity of the stock market is not necessarily fixed, but it works on a dynamic scale from high liquidity to low liquidity (Muharam, Anwar, &

Robiyanto, 2019). The liquidity position of a stock market depends on a variety of factors, such as the volume of economic condition, political decisions, monetary intervention decision, and the transaction timing. High stock market liquidity is often associated with large trading volumes and low spreads (or costs of sale).

2.12 Concluding Remarks

The contrast between the conventional market and the Islamic law has led to the emergence of the Sukuk market. The initial response from the Sukuk market towards filling the lack of conventional instruments compliance was limited to a few Sukuk structures. The maturation of the Sukuk market has resulted in several structures that meet the market expectation. In contrast to conventional bonds, Sukuk structures have provided more diversification. The remarkable development of the Sukuk structure has attracted investors from different religious backgrounds. The notable trends of these types of investors towards the Islamic debt market is not limited to the several diversifications of Sukuk only, but also relevant to the lower level of risk to the conventional instruments, which has been proven during the latest successive financial crises. Furthermore, Sukuk has become more favourable as a government instrument in financing new infrastructure. This chapter has reviewed the development of Sukuk in Asia and the GCC regions. The gradual development of Sukuk during the last two decades has resulted in different structures of Sukuk. These structures have been designed based on many dimensions, such as the purpose of issuing and the security level.