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The Evolution and Role of Sukuk Market in the Islamic and Global Economy

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Abstract

This study investigates the development and significance of the Sukuk market in both Islamic and global economies, amid modern technological and economic changes. It examines the Sukuk's structure, distribution, and key markets, noting their shift from corporate to sovereign financial instruments. The research highlights Sukuk's role in sustainable development and their attraction for ethically-minded investors. It analyzes various studies to emphasize Sukuk's impact on economic welfare and growth, particularly in countries like Malaysia and Bahrain. Additionally, the study explores Sukuk's influence on financial markets and Islamic banking services.

✓ Sukuk Market. Islamic Economy. Technological Evolution. Islamic Finance, Global Financial Markets. Sustainable Development. Ethical Investment.

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1. INTRODUCTION:

In the modern world of finance and business, where there is an increasing demand for ethical and inclusive financial markets, the Sukuk market emerges as a prominent component in the Islamic financial system, offering an innovative and ethically compliant alternative to traditional financial markets. Sukuk, considered as Islamic bonds, provide an asset-based financing mechanism, reflecting the principle of profit and loss sharing and avoidance of interest (Riba) and prohibited transactions according to Islamic law.

Since the first issuance of Sukuk in the early 1990s, the market has seen significant development, evolving from a rare financing tool to a major financial instrument in global markets. This evolution reflects changes in financial markets and shows adaptation to the changing needs of both Muslim and non-Muslim communities. Moreover, the role of Sukuk in financing projects that contribute to sustainable development and achieving social goals enhances their attractiveness to investors seeking ethical investment options.

However, the rapid growth of this market also poses numerous challenges, including the need to standardize Shariah standards and adapt regulatory and legal frameworks to facilitate the integration of Sukuk into global financial markets. The challenge also lies in how this market adapts to technological advancement and digital transformation, which can play a significant role in enhancing the efficiency and transparency of Sukuk issuance and trading processes.

The main objective of this research is to explore the development of the Sukuk market and examine its impact on the global economy. The research also aims to analyze the opportunities and challenges facing this market, focusing on its evolution and adaptation to global and technological changes.

Despite the growing development of the Sukuk market, there remains a lack of research addressing how this growth impacts the global economy in general and financial markets in particular. There is a pressing need to understand the dynamics of this market and the factors contributing to its success and challenges.

Thus, the following research question is posed:

How does the Sukuk market face global and technological challenges, and what is its impact on both Islamic and global economies?

The importance of this research lies in its ability to highlight one of the most important Islamic financial markets and its role in enhancing the global economy. It also contributes to understanding how Islamic principles can be integrated into modern financial transactions, opening new avenues for research and development in this field.

The research will be divided into several main sections. It begins with an overview of Sukuk, followed by a detailed analysis of its role in the Islamic and global economy. The research will also discuss the challenges and opportunities in this market, focusing on the impact of technology and global developments. In conclusion, recommendations will be presented based on the findings of the research.

2. Relevant Literature Review and Theoretical Relationships:

In her study, Zagirovna (2023) explored the history and evolution of the global Sukuk market, highlighting its transition from a corporate financing tool to a sovereign financing instrument. The study covers the structure, regional distribution, and key markets of Sukuk, as well as the challenges and prospects of Sukuk issuance in countries that were part of the Soviet Union. It also sheds light on the role of Islamic banking institutions in developing this market and the preference of issuers and

investors for Ijara contracts in Islamic bonds, especially in Indonesia, due to the fixed rental payments.

Öner (2022) analyzed the factors influencing the development of Sukuk markets in Turkey, using panel data analysis. The study concluded that several factors positively and negatively impact Sukuk markets in Turkey. Positive factors include GDP, interest rates, exports, profit rates and assets of participating banks, stock market, public expenditure, and the size of the banking sector. Inflation and foreign direct investments negatively influence these markets.

Elmorabit et al. (2023) highlighted the significance of Sukuk in the Islamic financial industry, pointing out their key role in mobilizing financing for investment projects. The study shows the positive impact of Sukuk on economic growth in Malaysia and Bahrain and how they help attract non-traditional investors. It emphasizes the negative relationship between the financial development index and economic growth, affirming the effective role of Sukuk issuance in supporting economic development.

Boukhatem (2021) addressed the role of socially responsible investment funds in the Islamic financial market, uncovering a lack of Sukuk in investment portfolios and the influence of corporate performance on the rental rates of Islamic bonds. The study highlights the importance of Sukuk in improving economic well-being and investor welfare, affirming that the development of the Sukuk market enhances investor welfare through risk hedging.

Ibrahim et al. (2022) focused on the development of the Sukuk market and Islamic banking performance, particularly emphasizing the dominance of Ijara contracts in Islamic bonds in Indonesia. The study indicates that issuers and investors prefer Ijara contracts due to the stability of fixed rental payments. It also stresses the necessity of

expanding the Sukuk market and Islamic banking services for economic growth. However, the study suggests that the development of one market may negatively impact the expansion of other markets, meaning that the development of the Sukuk market could come at the expense of Islamic banking services, or vice versa.

3. Islamic Sukuk

3.1.The Nature of Islamic Sukuk:

- **Linguistic and Historical Origin**: Sukuk, the plural form of the Arabic word "Sakk", originally meant a stamp or seal. Historically, it referred to legal documents or checks. In traditional Islamic literature, it denoted certificates issued to government employees as a substitute for their salaries. Over time, the meaning of Sukuk evolved to include financial certificates in a modern context.

- **Technical and Economic Definition**: Within Islamic finance, Sukuk are defined as bonds or investment certificates compliant with Sharia, Islamic law. Issued in equal values, these certificates represent undivided shares in the ownership of underlying assets, their benefits, or services, reflecting the right to partake in these assets rather than being based on debt. Sukuk are used as a tool for financing specific projects or investment activities.

- **Evolution and Economic Function**: Initially issued as financial certificates for government employees, Sukuk have now become a significant instrument in the Islamic economy. They serve as an alternative to traditional bonds in Islamic finance, focusing on asset investment while avoiding usurious interest.

- **Compliance with Islamic Sharia**: Sukuk rely on the principles of Islamic Sharia, which prohibits interest. Instead, profits are derived from the performance of the

underlying assets, requiring tangible, real assets as their basis, either through ownership or lease agreements.

Thus, Islamic Sukuk are innovative financial instruments used in Islamic finance, merging Sharia principles with practical economic needs. Sukuk enable investors to participate in assets and returns in a Sharia-compliant manner, representing a significant development in Islamic financing tools. (Alvi, et al., 2010) (Lahsasna, Ahmad, & Hassan, 2018)

3.2.Characteristics of Islamic Sukuk :

The Sukuk have unique characteristics that include :(Lahsasna, Ahmad, & Hassan, 2018)

- **Common Ownership Representation**: Sukuk represent a share in the ownership of tangible assets, benefits, or services. They are issued in equal values to establish the rights and obligations of the holder.
- **Profit Sharing and Loss Bearing**: Sukuk participate in profit entitlement at a predetermined ratio and bear losses according to the principle of "profit comes with the risk of loss," without a predefined rate of return on the nominal value.
- **Bearing Investment Operation Results**: Sukuk holders are obligated to bear the full results of the investment. A financial guarantee by an independent third party is permissible under Sharia.
- **Issuance Based on a Sharia-Compliant Contract**: Sukuk are issued based on contracts compliant with Islamic Sharia and adhere to Sharia guidelines in trading.
- **Bearing Ownership Burdens**: The Sukuk holder bears all burdens related to asset ownership and expenses of the investment activity.

- **Formation of an Independent Moral Entity**: Sukuk holders have the right to form an independent body to represent them with investment entities.
- **Tradability**: Sukuk are tradable through various means, as long as they comply with the Sharia guidelines for the assets, benefits, and services they represent.
- **Indivisibility**: A Sukuk cannot be divided in dealings with the company, and in case of inheritance, a single representative must be appointed to represent the heirs before the company.
- **Compliance with Sharia Guidelines**: Sukuk are regulated by Sharia guidelines in their issuance, trading, and the nature of activities and investments they engage in.

3.3.Key Advantages of Sukuk:

- **Development of Sharia-Compliant Financial Instruments**: Providing an alternative to traditional securities, based on assets and free of interest.
- **Direct Connection to the Economic Sector**: Sukuk are linked to underlying assets and commercial activities in the market, offering participation in the resulting profit.
- **Diversity in Financing and Investment Mechanisms**: Offering opportunities for diversifying investment portfolios and providing new financial instruments.
- **Benefits for Investors and Markets**: Providing returns and profits for investors and contributing to the growth of Islamic financial markets.
- **Tradability and Easy Settlement**: Sukuk offer fixed or variable return rates and facilitate the settlement process and capital valuation.
- **Ratings by International Agencies**: Sukuk ratings by rating agencies provide guidelines for risk and return assessment.

- **High Demand and Multiple Subscription Potential**: Due to their numerous advantages, Sukuk enjoy high demand and can be subscribed to multiple times their value.

These characteristics make Sukuk a unique instrument in the Islamic financial system, combining Sharia principles with economic efficiency, and represent an attractive alternative to traditional financial tools .(al-Amine, 2012)

The emergence of digital and cryptocurrency has necessitated the development of digital financial instruments using modern technologies. Here, encrypted smart Sukuk utilizing blockchain technology offer a significant opportunity for financing small and medium-sized enterprises and projects. These Sukuk are characterized by flexibility, transparency, and security, providing an innovative alternative to traditional Sukuk. They include smart Sukuk based on debt obligations such as Murabaha, Ijarah, Istisna, and Salam, as well as those based on risk-sharing through investment in activities or projects based on returns generated from the invested capital of the Sukuk, according to Sharia-compliant investment formulas like Mudaraba, Musharaka, and Investment Wakala, in addition to composite Sukuk. (Khan, et al., 2020)

3.4.Smart Sukuk:

Smart Sukuk are innovative investment documents relying on blockchain technology and smart contracts to achieve high efficiency and reduced costs while adhering to Islamic Sharia principles. They symbolize shares in ownership of specific assets, benefits, services, or in the assets of a particular project or special investment activity. These encrypted documents improve transparency, eliminate fraud, and reduce costs associated with issuing traditional Sukuk. Smart Sukuk expand the investor base, allowing companies of any size to independently issue their Sukuk. They provide secure and transparent access to issuance information and allow for the

automatic distribution of returns to holders of encrypted Sukuk according to predetermined rules in the smart contract, eliminating the need for traditional financial intermediaries. Smart Sukuk represent a significant advancement in the Sukuk market, offering effective solutions for standardization challenges, issuance, and maintenance costs, and facilitate trading and distribution through platforms based on smart contracts, contributing to the renewed development and growth of the Sukuk market. (محمد و زعير، 2022)

The process of issuing Islamic smart Sukuk involves several advanced stages using blockchain technology:(محمد و زعير، 2022)

1. **Announcement of Issuance**: Companies announce the issuance of smart Sukuk for sale via a blockchain platform.
2. **Downloading the Application**: Investors can purchase smart Sukuk through mobile applications or online banking services.
3. **Value of Smart Sukuk**: The value of the Sukuk is determined in the currency of the issuing country, with currency exchanges facilitated through a smart contract automatically approved by a central registry institution.
4. **Approval and Registration Process**: The smart contract is automatically approved through the central registry.
5. **Transfer of Encrypted Sukuk to Client Wallets**: After approval, the encrypted Sukuk are transferred to the clients' wallets.
6. **Trading Process of Smart Sukuk**: Conducted through several steps including the transfer of buy and sell orders on the blockchain system, and transactions are automatically settled through a security clearing and settlement institution.

7. **Blockchain Transaction Settlement**: On the settlement date, the currency code is sent to the bank through the smart contract, and the encrypted Sukuk are automatically settled with transaction registration in the clearing and settlement institution.

3.5.Current Examples of Smart Sukuk:

- **Blossom Smart Sukuk: A Transformation in Islamic Finance**

"Blossom Finance," established in the United States in 2014 and relocated to Indonesia in 2015, is a pioneer in offering smart Sukuk through Ethereum blockchain technology. This enables raising funds from investors in exchange for digital tokens representing shares in underlying assets. These Sukuk rely on the performance of the asset, not on the cryptocurrency market price, ensuring stability and Sharia compliance. They are characterized by efficient distribution of returns, transparency, and the ability to support Sukuk issuance in local currency, opening opportunities for small companies and investors to participate in the global market. "Blossom Finance" aims not only for microfinance but also to achieve positive social impact by directing finance towards entrepreneurial projects contributing to sustainable development. (Liaqat, 2019)

- **"Wethaq" Platform in UAE: A Pioneer in Blockchain Sukuk**

"Wethaq," established in collaboration between "R3" and "Wethaq Financial Technology," is a leader in using smart contracts and blockchain technology in Islamic capital markets for Sukuk issuance, launching the first experimental Sukuk in 2019. The platform is multifunctional, serving as a registrar, payment agent, and trustee, using the "Corda" platform to update records and settle disputes. It enhances efficiency and transparency in the Sukuk market and is Sharia-compliant, facilitating financing and distribution processes in Islamic markets. (محمد و زعير، 2022)

➢ **Other Experiences in Smart Sukuk:**

- **Al Hilal Bank - UAE**: On November 26, 2018, Al Hilal Bank in Abu Dhabi executed a smart Sukuk transaction worth USD 500 million due in September 2023 using blockchain technology. This represented the first global use of blockchain in Sukuk transactions.

- **Inablr - Bahrain**: In September 2021, Bahrain's Inablr announced plans to launch a blockchain-based investment platform in 2022 for clients interested in owning bonds and Sukuk with amounts not exceeding USD 1,000. The company intends to use Tezos blockchain technology to develop the platform's infrastructure, supported by the Central Bank of Bahrain's innovation lab.

- **Bursa Malaysia Berhad**: In September 2021, the exchange began testing blockchain and DLT technologies for issuing non-physical digital security certificates, completing the tests in November 2021 in collaboration with financial industry partners.

- **Bursa Malaysia - Digital Bonds**: In August 2020, it announced the successful issuance of digital bonds in partnership with Hashstacs in Singapore. The initiative included "Project Harbour" to explore DLT management of bonds, asset tokenization, efficiency improvement, cost reduction, and the use of smart contracts.

- **HLC - Dubai**: The company is developing a platform for issuing smart Sukuk using blockchain technology but has not yet issued any Sukuk.

These examples demonstrate the integration of blockchain technology in Islamic financial services, particularly in Sukuk issuance, to enhance efficiency, transparency, and ease of access in financial transactions. (محمد و زعير، 2022)

3.6.Challenges Facing Traditional and Smart Sukuk

- **Regulatory Challenges** :

- **Yield Rates**: Risks associated with fixed-return Ijarah Sukuk, susceptible to interest rate fluctuations, especially when linked to LIBOR.
- **Currency**: Risks arise when the underlying asset of the Sukuk is denominated in a different currency from the fundraising currency, exposing it to exchange rate fluctuations.
- **Assets**: Risks due to changes in the value of the underlying assets, such as asset damage or depreciation, particularly significant in future Ijarah Sukuk.
- **Regulatory Complexity**: Fintech solutions are subject to complex regulatory rules, different from those for traditional financial solutions.
- **Development of Decentralized Applications**: The need to develop decentralized applications and payment gateways for converting fiat currencies to cryptocurrencies like ETH increases costs and regulatory complexity.
- **Know Your Customer (KYC) Procedures**: Challenges in implementing KYC to verify customer identities, adding to costs and complexity.
- **Performance and Scalability Challenges**: Blockchain technology is still in early development stages with performance and scalability hurdles.
- **Key Management**: Managing public and private key pairs associated with an Ethereum address requires basic technical awareness from users.

- **Legal Challenges** :

  - **Establishing Legal Ground**: Challenges related to finding a legal ground that allows and protects transactions in smart Sukuk, especially Islamic ones.

  - **Legal Recognition**: Smart contracts are not legally recognized in most jurisdictions, necessitating legal contracts for investors.

  - **Absence of Electronic Notary**: Focusing on issuing Sukuk to investors only, with Murabaha buy and sell transactions conducted off the blockchain.

  - **Data Privacy**: Challenges related to data privacy when using blockchain, with solutions like using privacy-preserving blockchain platforms.

- **Legislative Challenges** :

  - **Sharia Compliance**: Ensuring that the issued Sukuk comply with Islamic Sharia, requiring the examination of blockchain algorithms and programming for Sharia contract compliance.

  - **Role of Sharia Advisors**: The need for mutual understanding between Sharia scholars, Sukuk issuing institutions, and the tech team to ensure smart contracts adhere to Sharia standards.

  - **Complexities and Challenges of Using Cryptocurrency**: Ongoing debates among Sharia scholars about its acceptance.

- **Cybersecurity Challenges** :

  - **Internet Risks**: As blockchain Sukuk are online applications, they are exposed to risks of hacking and cyber-attacks.

- **Security Vulnerabilities in Smart Contracts**: Potential vulnerabilities that can exploit coding errors and undetected flaws.
- **Post-Deployment Cybersecurity Challenges**: Once smart contracts are deployed on Ethereum, they cannot be updated to remove any programming errors, making exploitable vulnerabilities a perpetual concern.

In summary, regulatory challenges revolve around the procedures and rules required for operation and development within the fintech framework. Legal challenges concern the legal basis and judicial recognition of the Sukuk. Legislative challenges focus primarily on ensuring the Sharia compliance of smart Sukuk and managing the complexities of merging technology and Sharia. Meanwhile, cybersecurity challenges focus on ensuring the security of the technological infrastructure and protecting smart Sukuk from cyber-attacks and security vulnerabilities. (Khan, et al., 2020)

4. Islamic Capital Market (ICM):

4.1. The Nature of Islamic Capital Market (ICM):

The Islamic Capital Market (ICM) is an integral part of the global financial system, offering a financial infrastructure that aligns with Islamic Sharia principles which prohibit riba (interest), maisir (gambling), and gharar (extreme uncertainty in contracts). ICM encompasses a variety of Islamic financial instruments, including exchange-traded funds, real estate investment trusts (REITs), Sukuk (Islamic bonds), and other Sharia-compliant derivatives.

The main difference between ICM and traditional markets lies in the handling of interest. In ICM, transactions are based on risk-sharing without guarantees for the principal amount or profit. Conversely, transactions in the traditional market are

interest-based, with guarantees for the principal amount and profit. Sukuk, as an alternative to conventional bonds, are the cornerstone of ICM. They are issued and traded in primary and secondary markets, directly contributing to economic growth and playing a vital role in financing projects and investments compliant with Islamic rulings, especially in predominantly Muslim countries. ICM is attracting increasing attention from investors due to growing wealth in the Islamic world, as investors seek financing opportunities that align with their religious and ethical values.

Supported by various international Islamic organizations like the Islamic Financial Services Board (IFSB), International Islamic Financial Market (IIFM), and the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI), ICM is continually advancing in expanding its scope and enhancing its integration with global financial markets. ICM is open to all, creating a vast global Islamic financial market encompassing over 250 Islamic financial institutions across approximately 75 countries. (Lahsasna, Ahmad, & Hassan, 2018)

4.2.Types of Islamic Capital Market:

Like the traditional market, the Islamic Capital Market (ICM) consists of two main markets:

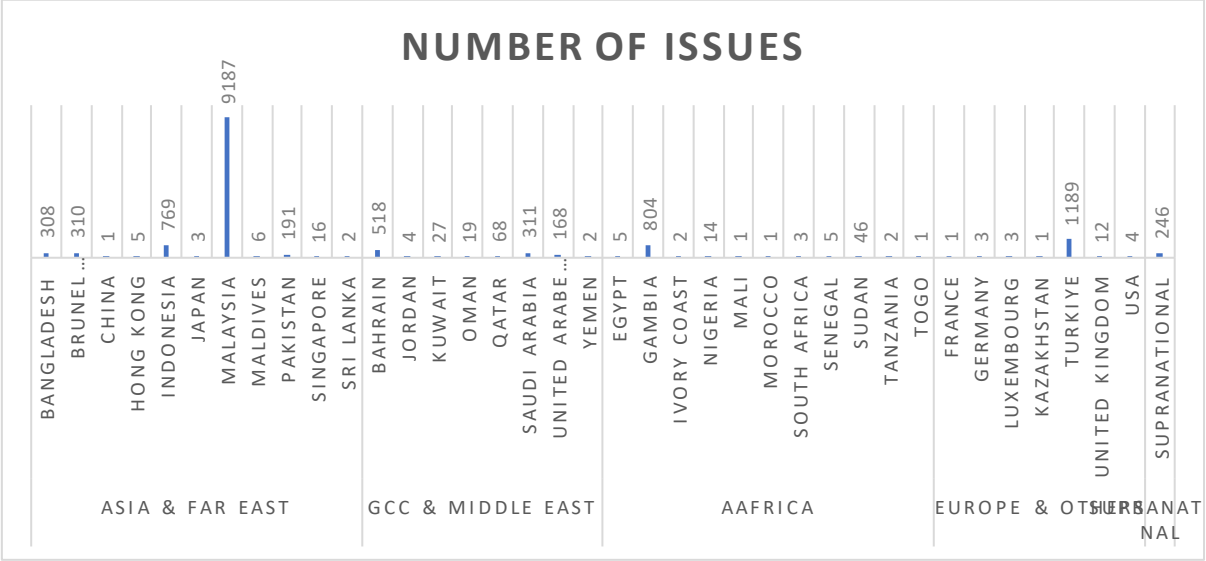
- **Primary Market**: This is where companies and governments initially issue their financial securities to raise capital for their projects and initiatives. The primary market plays a vital role in economic activities, providing a central platform that allows investors to place their investments in viable projects and enhancing market liquidity. It is also a major source of funding for both government entities and private companies, transforming saved funds into effective investments, creating new investment opportunities, and innovating financial products and instruments, particularly in the Islamic financial market.

- **Secondary Market**: This is where previously issued securities in the primary market are traded. The secondary market is crucial for providing liquidity, allowing investors to buy and sell securities among themselves. In this market, transactions occur between investors themselves, and the issuer of the asset does not directly receive money from buyers. Instead, there is a change in ownership of financial assets, and funds flow from the buyer to the seller. This market enhances active trading and facilitates access to investments for investors. (Lahsasna, Ahmad, & Hassan, 2018)

4.3.Geographic Distribution of the Global Sukuk Market:

Asia has continued to dominate the global Sukuk market since its inception in January 2001 until December 2022, where Asian issuances constitute 61.38% of the global Sukuk issuances as shown in the attached table. The Gulf Cooperation Council (GCC) countries and the Middle East rank second with a market share of 24.53%, and this region is one of the main areas driving the Sukuk market forward. International entities, particularly the Islamic Development Bank, which holds a 7.10% share, play a significant role in developing the Sukuk market. In the past few years, the contribution of the European sector has increased, especially thanks to Turkey, from 2.3% in 2016 to 5% in 2020.

Fig 1. Regional Distribution of Global Sukuk Issuances (2001 –2022)



Source: Based on (Alvi, et al., 2023)

The distribution of global Sukuk issuances by country shows that Malaysia ranks first (56%), followed by Saudi Arabia (12%), Indonesia (9%), United Arab Emirates (7%), Turkey (5%), Bahrain (3%), Qatar (2.5%), and Pakistan (2%). In Africa, Sudan is the most active in issuing Sukuk (1%). In recent years, Malaysia's share has decreased due to the activity of other players such as Saudi Arabia, Indonesia, and Turkey. Overall, the number of jurisdictions entering the Sukuk market for the first time increases each year, contributing to the activity of the entire market.

Here we will showcase the main role of some countries in the global Sukuk market:

- **Malaysia**: Since its inception, Malaysia has dominated the primary Sukuk markets, starting with the first deal by a Shell subsidiary in Malaysia in 1990. Malaysia has maintained its leadership in the market, with occasional concessions to other players in certain sectors. Malaysia accounts for 56% of total issuances, totaling $800 billion. It has also witnessed the largest number of deals, with more than 7800

transactions, representing more than 70% of the total quantitative volume. The Malaysian financial market has seen many innovations, such as the world's first mortgage-backed Sukuk in 2005 and the first convertible Sukuk in 2006. Malaysia's domestic Sukuk market is the largest in the world, comprising nearly two-thirds of the global volume, with more than $700 billion. The domestic markets in Saudi Arabia and Indonesia are seven times smaller than the Malaysian market.

- **Saudi Arabia**: The second-largest global player and a regional leader. Saudi Arabia began issuing Sukuk in 2003 when the Islamic Development Bank issued a five-year $500 million Sukuk. Since then, 260 issuances have been made in the Saudi market, totaling $175 billion. Saudi Arabia has the largest domestic Sukuk market in the Middle East and North Africa, valued at nearly $110 billion. The strong interest of local investors in sovereign risks is a key driver of the Saudi market. Saudi Arabia has seen many large sovereign issuances, such as a $9 billion sovereign bond in 2017, a major event in the global Sukuk market. The Saudi Electricity Company successfully issued a $2 billion international Sukuk, split into two tranches for 10 and 30 years. Fitch Ratings affirmed the company's AA rating, reflecting its monopolistic strength and government ownership. The deal attracted significant investor interest, with orders of $13 billion. The company plans to increase its electricity generation capacity and seeks to cover a potential funding gap through government financing and capital market operations.

- **Indonesia**: The third-largest issuer of Sukuk, with 552 Sukuk totaling $125 billion, nearly 9% of the global market. The Indonesian market's dynamics accelerated from 2002, with the number of deals increasing from 7 annually to 45 between 2017 and 2020. In 2008, the Indonesian government entered the sovereign Sukuk market with issuances of over $500 million. The Indonesian market is characterized by its diversity, including different types of Sukuk such as Hajj Fund Sukuk, Retail

Sukuk, and Global Sukuk. In 2020, a series of innovative social Sukuk (Indonesia Waqf Sukuk) were issued. Retail Sukuk, a government-guaranteed investment instrument, aims to stimulate national savings and meet the needs of Muslim communities for Sharia-compliant investment instruments. The minimum investment in these Sukuk is around 1 million rupiah (about $60). The main investors in Sukuk are traditional banks (27%) and Islamic banks (7%), along with pension funds (11%) and insurance companies (10%).

- **United Arab Emirates**: In 2002, the UAE began issuing Sukuk with Islamic Treasury Sukuk, and in 2023, Sukuk worth 1.1 billion dirhams were issued. In March 2013, Emirates Airlines issued a $1 billion Sukuk, to be repaid in 2023, to support the Islamic economy and Dubai's initiative. Also in March, Dubai Islamic Bank issued a $1 billion hybrid Sukuk to support core capital, attracting orders of over $14 billion. Until November 2023, the issuance of Sukuk and green bonds in the UAE reached about 15.45 billion dirhams, in line with sustainability goals and promoting sustainable growth.

- **Turkey**: Turkey began issuing Sukuk in 2012 after updating laws to facilitate Sukuk issuance and offering tax incentives for issuances exceeding five years. In the same year, the Turkish Treasury issued a $1.5 billion sovereign Sukuk, with demand exceeding supply by five times. Turkey has issued over 700 Sukuk totaling $67 billion, ranking second after Malaysia in terms of the number of deals. Turkish issuances account for about 5% of the global Sukuk volume, but they have not yet become the predominant instrument in the Turkish corporate debt market, constituting just over 6% of total debt securities. In the past five years, issuances have been primarily directed towards qualified local investors, but Turkish Sukuk are beginning to gain popularity among individual investors.

6. **Bahrain**: Despite the small size of its domestic Sukuk market, Bahrain has been a leader in international Sukuk issuances, representing 27% of the global volume, significantly surpassing Saudi Arabia. Bahrain is also a leader in the number of issuances in the Middle East with 467 issuances, totaling about $40 billion, approximately 3% of the global market.

7. **Qatar**: Qatar has used Sukuk as a key tool in financing infrastructure investments for hosting the 2022 FIFA World Cup, accounting for about 2.5% of the market.

8. **Pakistan**: Pakistan entered the global Sukuk market in 2005 and began developing its domestic market in 2008. It has four international issuances totaling $3.6 billion and more than 140 domestic issuances, over 80 of which are corporate. The primary buyers of Sukuk are commercial banks, mutual funds, and social insurance funds. Pakistan is undertaking massive infrastructure projects, and Sukuk is expected to play a significant role in their financing. Pakistan's Sukuk market is believed to have the potential to grow fivefold, possibly reaching issuance levels similar to Indonesia.

9. **Sudan**: The process of Islamizing the economy began in the 1980s, necessitating the introduction of Islamic liquidity management tools. At that time, the first generation of Sukuk was introduced to the market, including profit-sharing certificates from the Central Mudaraba Certificates (CMC) and Government Mudaraba Certificates (GMC). By 2014, the number of Sukuk deals exceeded 22,000, representing 97% of the total number of transactions on the Khartoum Stock Exchange (KSE). Over the years, Sudan has issued Sukuk worth over $20.5 billion, making it the leader in Africa (accounting for more than 80% of the dollar value of all African Sukuk). Sudan's contribution to global Sukuk issuances is comparable to Pakistan's, representing about 1.5% of the global total.

10. **China**: Islamic finance began to grow in China since 2009, enhanced by the Belt and Road Initiative aiming to strengthen economic relations with countries in Asia, the Middle East, and Africa. China is witnessing developments in the Sukuk market, driven by major projects and collaboration with Islamic banks. Despite being an emerging market, it is recording accelerated growth. Hong Kong, on its part, preceded China in using Sukuk by issuing a $1 billion Sukuk in 2014, a significant step in developing the Islamic market. There is now a pressing need to develop a strong legal framework to support this growth and attract more investments in the future.

Although Uzbekistan was expected to become a new issuer in the Sukuk market, with the government announcing plans to issue sovereign Sukuk in 2021, this has not yet occurred due to the early stages of local exchange development and the Islamic bank not yet fully legitimized in the country.

In Russia, a pilot Sukuk issuance worth 1 million rubles was conducted in 2017 by a company in Tatarstan, but the project did not develop due to a lack of strategic investors and legislative support.

Kazakhstan, on the other hand, has seen notable success in Sukuk issuance. In 2012, the Kazakhstan Development Bank issued a five-year Sukuk worth 240 million Malaysian ringgit, and the demand was strong from Malaysian and Kazakhstani investors, with 62% purchased by Malaysian investors and 38% by Kazakhstani investors. Despite legal amendments in 2015 to facilitate Islamic finance and new issuances, no further issuances have been conducted by Kazakhstani entities, except for the Qatar International Islamic Bank issuing Sukuk worth $500 million in the London and Astana stock exchanges in 2020.

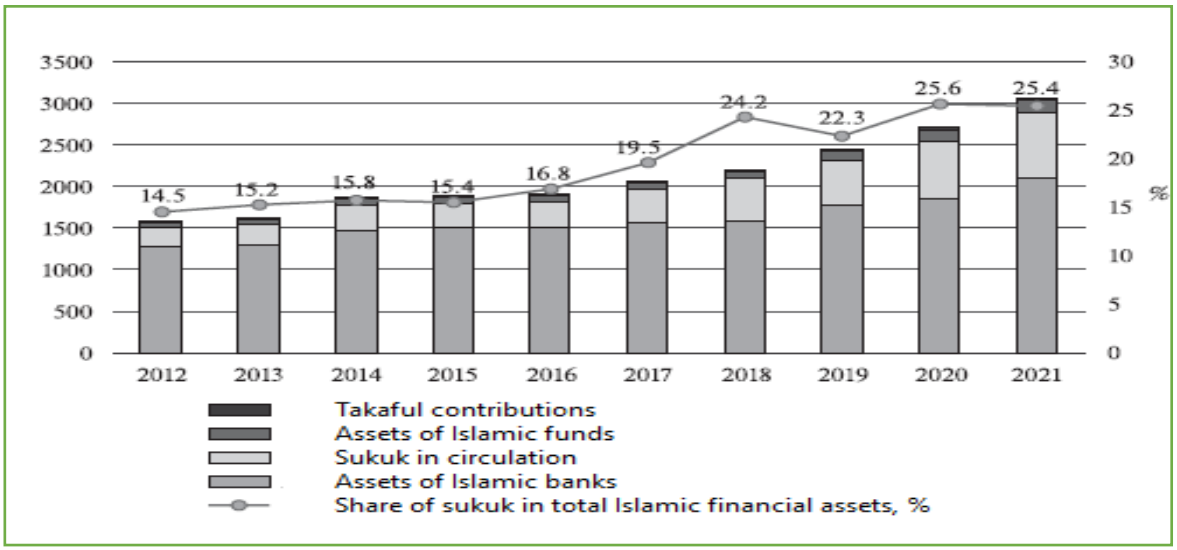
For other Muslim-majority Commonwealth countries, serious discussions about Sukuk issuance have not taken place in Tajikistan, discussions were still in their initial stages in Azerbaijan, and no Sukuk were issued in Kyrgyzstan despite legal amendments in 2016. (Zagirovna, 2023)

4.4.Key Landmarks in the Sukuk Market

Over the past decade, Islamic financial assets, encompassing Islamic banks, Takaful (Islamic insurance), Sukuk bonds, and funds, have nearly doubled in value, from $1.6 trillion in 2012 to $3 trillion in 2021 (Figure (2)). Islamic banks remain the largest sector in Islamic finance, though their share has decreased from 80% to 70% during this period. Concurrently, Islamic Capital Markets (ICM), which include Sukuk and Islamic funds, have become the fastest-growing sector in Islamic finance.

By the end of 2021, the size of ICM reached $930.3 billion, representing 30.4% of the total global Islamic financial assets. Specifically, the Sukuk market is the largest and most dynamic segment within ICM. According to analyses from the "Islamic Financial Services Industry Stability Report" for 2013-2022, the contribution of Sukuk to the Islamic financial sector has nearly doubled over ten years: from 14.5% in 2012 to 25.4% in 2021. The total market value has more than tripled: from $229.4 billion in 2012 to $775.7 billion in 2021. Consequently, the Compound Annual Growth Rate (CAGR) for the Sukuk market during this period was 13%, higher than the growth rates of any other sector in Islamic finance.

Fig 2. Dynamics of various segments of the Islamic financial sector and sukuk shares, 2012–2021



Source: (Zagirovna, 2023)

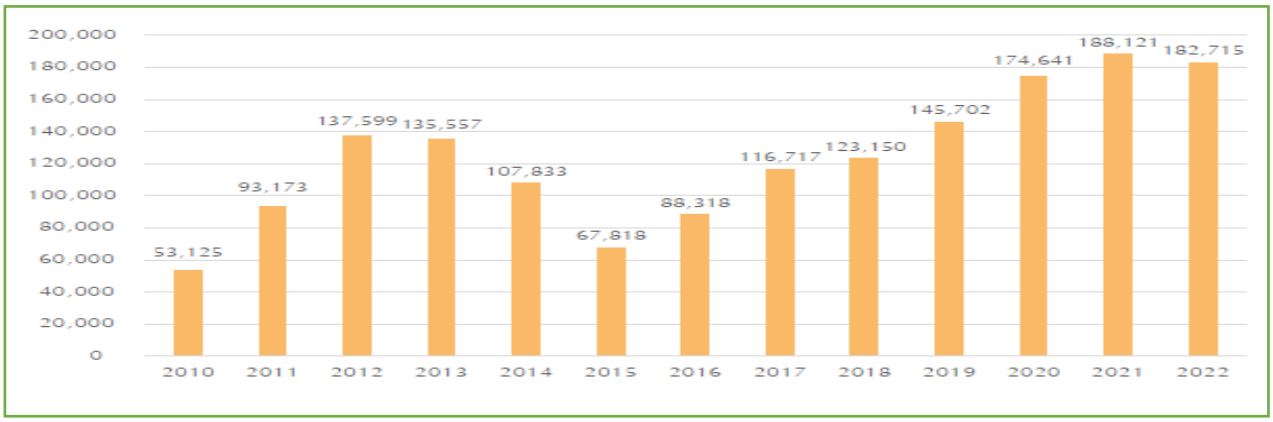
When analyzing the Sukuk market not in terms of trading volume but in terms of new issuances, the presented curve shows the global Sukuk issuances in US dollars from 2010 to 2022. This trend exhibits a general upward trajectory over the period, with noticeable growth in global Sukuk issuances. However, some annual fluctuations in issuance volumes are observed, with varying highs and lows. For instance, a decline occurred in 2013 after consistent increases from 2010 to 2012. These fluctuations reflect different economic conditions and the impact of major economic events, such as financial crises. Nevertheless, the market was able to recover and continued to grow subsequently. (Alvi, et al., 2023)

In 2019, there was an approximate 18% increase compared to the previous year, indicating the market's strength and growing interest. The slight decrease of 2.96% in 2022 might be attributed to global economic challenges, inflation, and interest rate changes, demonstrating the impact of macroeconomic conditions on the

market. Despite this decline, there has been stability or moderate growth in the first half of 2023, indicating the market's resilience and continuity.

With an estimated value of $3.25 trillion in 2022, Sukuk represent about 24.43% of the total net value of the industry, reflecting their significant importance as a financing tool. As for the future of the Sukuk market, information points to continued investor interest and diversification of their base, suggesting that the Sukuk market will remain important in the Islamic financial industry and is likely to continue evolving and growing.

Fig 3. Total Global Sukuk Issuances in USD Millions



Source: (Alvi, et al., 2023)

During the past decade, the Islamic financial assets, including Islamic banking, Takaful insurance, Sukuk bonds, and funds, have almost doubled in value, from $1.6 trillion in 2012 to $3 trillion in 2021. Islamic banks remain the largest sector, although their share has decreased from 80% to 70% in this period. Meanwhile, Islamic Capital Markets (ICM), encompassing Sukuk and Islamic funds, have become the fastest-growing sector in Islamic finance.

By the end of 2021, the size of ICM was $930.3 billion, accounting for 30.4% of total global Islamic financial assets. Specifically, the Sukuk market is the largest

and most dynamic segment in ICM. According to "Islamic Financial Services Industry Stability Report" analysis for 2013-2022, the contribution of Sukuk to the Islamic financial sector has almost doubled over ten years: from 14.5% in 2012 to 25.4% in 2021. The total market value has more than tripled: from $229.4 billion in 2012 to $775.7 billion in 2021. The Compound Annual Growth Rate (CAGR) for the Sukuk market during this period was 13%, higher than any other sector in Islamic finance.

Despite initial deals in the 1990s, rapid growth in the global Sukuk market was marked in the first decade of the new millennium. The number of issuances rose from 50 in 2000 to 1200 in 2020, with the total issuance volume exceeding $1.4 trillion. In the first decade of the new millennium, Sukuk became a key instrument in Islamic financial markets, used by governments, development institutions, financial and business entities for liquidity management, project financing, infrastructure development, budget deficit coverage, and meeting the needs of individual and institutional investors. In recent years, Sukuk continued to attract new issuers and expand the investor base, including those focused on sustainable development and Environmental, Social, and Governance (ESG) principles.

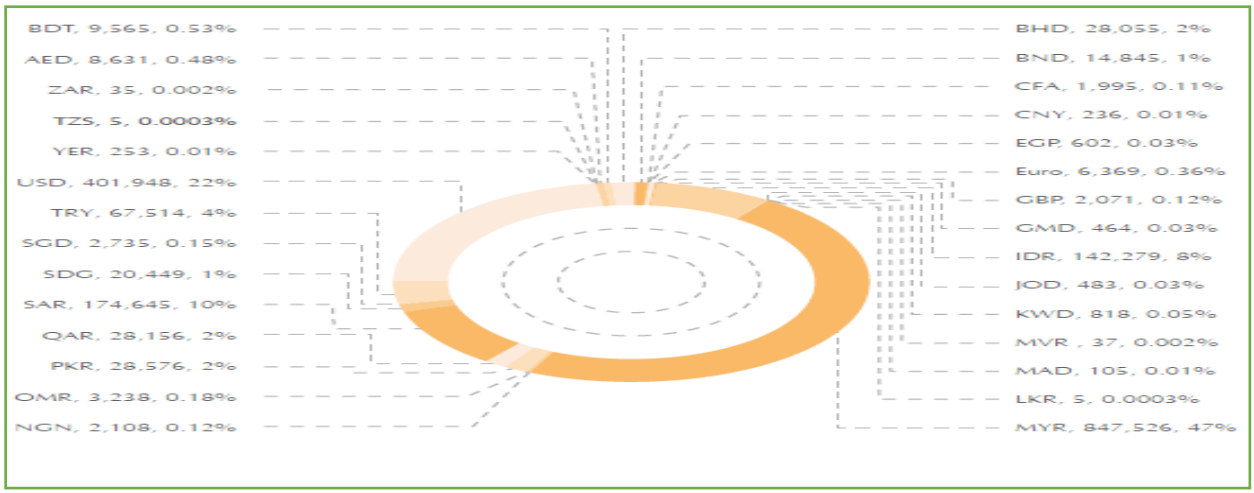
Sukuk can be issued for short-term or long-term purposes. Short-term Sukuk are essential to meet the liquidity requirements of Islamic financial institutions, especially Islamic banks. According to IIFM, the total issuance of short-term Sukuk amounted to $502 billion (or 35% of total issuances). However, the Sukuk market is primarily made up of long-term issuances, often used for infrastructure projects or project financing, constituting about two-thirds of the global market.

Regarding the ratio between international and domestic issuances, international Sukuk accounted for 24% of total global issuances since the market's inception. The

US dollar, as a hard currency, is particularly favored for attracting foreign investors. However, domestic Sukuk dominate the market, comprising 3/4 of all issuances. The year 2020 saw the highest volume of domestic issuances at $132 billion. Domestic short-term and long-term issuances are often issued in local currencies. From 2001 to 2020, Malaysia led with 65.5% in total domestic issuances, followed by Saudi Arabia (10%), Indonesia (9.5%), and Turkey (4.6%).

Regarding the currency used in Sukuk issuances, the Malaysian ringgit was the primary currency, accounting for about 51% of all issuances, due to Malaysia's leading role in the majority of domestic issuances. US dollar-denominated Sukuk came in second, at 23%. Sukuk were also issued in 27 other currencies from various countries. (Zagirovna, 2023)

Fig4. Global Sukuk Issuances Currency Break-Up (2001- 2022, USD Millions)



Source : (Alvi, et al., 2023)

The composition of Sukuk issuances over time shows a significant shift in the type of issuers. Sovereign Sukuk have played the most substantial role historically, accounting for 57% of the issuances. This is followed by corporate Sukuk at 19%, quasi-sovereign Sukuk at 15%, and financial institutions' issuances at approximately 9-10%.

Prior to the Global Financial Crisis of 2008-2009, corporate entities were the dominant issuers of Sukuk, while the role of sovereign entities was more limited. However, since 2009, there has been a marked increase in the proportion of sovereign Sukuk issuances. (Zagirovna, 2023)

Therefore, Sukuk have evolved from being a corporate financing tool to a governmental financing tool, used by many governments to cover budget deficits. Corporate Sukuk are issued by companies, sovereign Sukuk by national governments, and quasi-sovereign Sukuk by government-owned companies, which may have explicit or implicit government guarantees.

The market trend changed between 2008 and 2009, with sovereign Sukuk becoming the main component of global Sukuk issuances, significantly surpassing corporate issuances. Some analysts believe that during the global financial crisis, the investment community's appetite for corporate risk decreased in favor of safer assets such as sovereign securities. Others see this as an indication that Sukuk are more suitable for large issuers who can bear the additional costs associated with their issuance. According to another view, this reflects a greater reliance of the corporate sector on bank financing rather than capital markets.

For corporate issuances, their peak volume reached $34.6 billion in 2013. This issue also exists in traditional financial markets where the corporate sector is the first to reduce expenses and development projects during and after economic crises. Generally, corporate issuances are characterized by following economic cycles, increasing during times of economic growth and decreasing during economic contractions. Among other reasons cited are weak government support and the absence of tax incentives for potential Sukuk issuers. Indeed, the corporate Sukuk market is more developed in those jurisdictions where local governments have

created economic incentives and a favorable environment. A clear example of this is Malaysia, where Sukuk account for more than 70% of total corporate debt.

One of the strong aspects of the Sukuk market is its low default and restructuring rates, attracting institutional investors worldwide. According to statistics from 1990 to 2017, only one in every 100 Sukuk issuances experiences default. Since the market's inception, the total volume of defaulted Sukuk issuances amounted to $2.88 billion, representing over 0.2% of the total market volume by the end of 2017. This low default rate can be attributed to several reasons, including that over 50% of all issuances are sovereign, which are generally considered safer than corporate instruments, and the strong influence of Islamic finance principles that include securing financial transactions with assets.

The peak of Sukuk defaults occurred in 2008-2009, with the last known case in 2016 when a Singaporean oil and gas company failed to meet its obligations due to challenges in the global market. This highlights the stability of the Sukuk market as one of its key characteristics. (Zagirovna, 2023)

4.5.Sukuk Market Challenges:

The Sukuk market faces several challenges that limit its expansion. These include:

- **Process Slowness**: The documentation process for Sukuk issuance lacks speed and efficiency compared to the traditional bond market, leading to increased costs.
- **Shariah Scholars' Decision**: The decision of Shariah scholars plays a crucial role in structuring Sukuk, and incorporating Shariah rulings increases the cost.

- **Lack of Standardization**: The absence of unified standards, as seen in the traditional bond market, slows down the structuring process, increases costs, and restricts market spread.

- **Accepted Global Shariah Standards**: There is a need for unified Shariah standards for different Sukuk structures to harmonize various Shariah opinions.

- **Diverse Challenges**: There are other challenges such as different tax treatments compared to traditional bonds in various jurisdictions, the need for a good credit rating, and issues related to assets during the transaction period.

To overcome these challenges, emerging technologies like blockchain can be utilized. Methods to overcome include:

- **Tokenization**: Using blockchain to tokenize Sukuk generates more secure and stable data, reduces intermediaries, facilitates the issuance of Sukuk in smaller denominations, extending the benefits of structuring to small and medium-sized enterprises.

- **Smart Contract Template**: Providing a smart contract template for different Sukuk structuring methods in consultation with Shariah scholars, which eases the programming and verification process of smart contracts.

- **Mechanism**: In the Sukuk issuance process, including periodic payments and distribution of returns, blockchain technology enhances the efficiency of clearing and settlement operations. This ensures an automated delivery and payment mechanism in the absence of a central authority, significantly reducing settlement risks, making the process more efficient and transparent.

- **Credit Rating and Market Expansion**: Using artificial intelligence on blockchain data to develop alternative credit rating methodologies and expanding the market for organizations looking to raise capital through Sukuk issuance.

5. CONCLUSION

In conclusion, this study affirms that the Sukuk market, as an integral part of the Islamic Capital Market (ICM), has witnessed significant growth and garnered widespread attention in the global financial arena. This interest reflects the increasing demand from Islamic institutions and individual investors seeking Sharia-compliant financial products. Notably, Sukuk are characterized by their strong link to the real economy and assets, implying that both the financier and the beneficiary share the risks and rewards of the underlying asset's positive performance. Furthermore, Sukuk are considered safer compared to traditional bonds, as they are based on actual assets rather than merely being an obligation.

The various studies indicate that a well-developed Sukuk market contributes effectively to enhancing economic welfare and offers innovative financial solutions aligned with the evolving needs of both Islamic and non-Islamic communities. However, the market faces challenges such as the need for unified Sharia standards and legislative development to facilitate the integration of Sukuk into both local and global financial markets.

Research Recommendations:

1. **Enhancing Sharia Compliance:** It is essential for Islamic financial institutions to fully adhere to Sharia principles to ensure transparency and trust in the market.
2. **Developing Services and Technologies:** Banks should be encouraged to develop their services and adopt modern technologies to enhance the efficiency of Sukuk.

3. **Spreading Islamic Awareness and Culture:** Expanding awareness about Islamic finance concepts and terminology is crucial.

4. **Adapting Legislation to Support Sukuk:** National legislations should be adapted to support the development of Sukuk and their effective integration into local financial markets.

5. **Promoting International Cooperation:** Encourage cooperation between countries to develop the Sukuk market, exchange experiences, and best practices.

6. **Expanding the Market Scope:** Expand the Sukuk market to include funding for infrastructure projects and addressing government budget deficits.

Through these recommendations and analyses, it is clear that the Sukuk market represents a vital part of the Islamic financial system and holds tremendous potential for growth and development. This growth is expected to enhance economic welfare and strengthen economic relations globally.

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