AFF 亞洲金融論壇 ASIAN FINANCIAL FORUM

Workshop IV

"A Bigger Investor Universe"
Making Hong Kong the Islamic Gateway to China

Can Hong Kong become the Islamic world's financial portal to mainland China? That question was explored by a workshop on 21 January at the Asian Financial Forum 2010 in Hong Kong.

"Islamic finance offers great potential and vast opportunities for market players," said workshop moderator Pius Chong, Asia-Pacific Managing Director and Head of Transaction Management for HSBC. "As an international financial centre, it would be desirable for Hong Kong to develop a platform to facilitate intermediation of savings and investments between the Islamic financial communities and this region."

Mr Chong is also Convenor of the Working Group on Development of Islamic Finance with the Treasury Markets Association, which organised the workshop and is helping the Hong Kong government promote Islamic finance.

Conduit to the Mainland

YC Cheng, Hong Kong's Deputy Secretary for Financial Services and the Treasury (Financial Services), said Islamic finance, which offers profit sharing instead of interest, was becoming an integral part of the global financial system as a new investment alternative, with strong growth prospects.

Mr Cheng outlined Hong Kong's competitive advantages – including its common-law legal system and independent judiciary, the free flow of capital and information, a rich pool of professionals, robust infrastructure and low taxes. Moreover, he said, Hong Kong is the gateway to the mainland financial market.

All these credentials "would provide us with a very solid foundation to act as the two-way springboard linking the Middle East and mainland China," he said. Hong Kong could help mainland enterprises expand their global investor base by raising money from the Middle East. "For Middle East investors, we would serve as a conduit channelling their funds for investment opportunities relating to mainland China."

Mr Cheng said the government's strategies include enhancing the market infrastructure to "level the playing field" for *sukuk* (Islamic bonds) vis-à-vis their conventional counterparts, which would involve reviewing tax legislation.

Sharia Compliance

Sam Kwok, Treasurer of the Airport Authority Hong Kong, noted that the authority had the same credit rating as the Hong Kong government, making it a good candidate to raise money by issuing sukuk.

He explained that Islamic finance rules prohibit the making of profit from interest but encourage the generation of profit from the performance of an underlying asset, excluding such activities as gambling, casinos and alcohol. The most common form of sukuk is Ijara structure, sometimes called a "sale and leaseback structure," which uses a special purpose vehicle to handle the underlying asset.

"Last but not least, to be sharia [Islamic law]-compliant, we need to have an opinion from the Islamic scholars saying that the structure of the sukuk is compliant with the principles of Islamic finance so that Islamic-compliant investors can buy into such an asset. That is a crucial difference between a conventional bond and a sukuk."

"The major advantage for us would be, through a sukuk structure, you can tap into a much bigger investor universe," Mr Kwok said. "Islamic or sharia-compliant investors who are not permitted to buy a conventional bond would be able to buy a sukuk, so that enlarges the universe of potential buyers of the bond substantially."

Huge Potential

Saad Rahman, Executive Director of Global Islamic Banking with Calyon, the Crédit Agricole Group's corporate and investment arm (recently renamed Crédit Agricole CIB), noted that there were some 1.6 billion Muslims, nearly 25 per cent of the world's population. He said Islamic finance, despite the global credit crisis, "is one of the few sectors in the financial service arena that continues to show double-digit growth."

Islamic funds currently total between US$500 billion and $1 trillion. "The Islamic potential is estimated at $4 trillion," he said. "We've got a long way to go before we reach the full potential."

Risk management, securitisation and money-market instruments are fields currently lacking in Islamic financial products, he said, and there is room for innovation despite the cautious approach of Islamic scholars.

“Islamic finance is still dependant on two markets – Malaysia and the Gulf – but its global expansion will bring it to a critical size that would avoid it having to rely on a limited number of countries for its publicity and its growth.”

Tax Issues

Roslinda Ahmad, CIMB Islamic Bank Berhad’s Associate Director and Head of Debt Market and Corporate Finance, referred to a US$550 million sukuk issue in 2008 by Khazanah Nasional Berhad, the Malaysian government’s investment arm, to highlight a tax concern facing Hong Kong.

The issue, for which her bank was joint lead manager, was exchangeable for shares in the mainland’s Hong Kong-listed Parkson Retail Group. Under the sukuk structure, the shares were sold by a Khazanah subsidiary to a special purpose vehicle, which then sold them to the issuing company, Paka Capital.

Khazanah applied for an exemption from stamp duty because the sale of the underlying shares was strictly to facilitate an Islamic transaction.

“I’m proud to say, thank you to the regulators in Hong Kong, that the exemption was given to Khazanah, and that saved them a few million ringgit,” she said. But in the case of sukuk holders opting for shares rather than cash when they redeemed the sukuk, CIMB did not ask for an exemption “because that was a real transfer.”