

# ISLAMIC BONDS (SUKUK) CASE STUDY (5)

## Qatar Global Sukuk

US\$700 million Sukuk Trust Certificate by Qatar Global Sukuk

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This case describes the basic structure of the Qatar Global Sukuk. It is intended to be used as the basis for class discussion. Answers are not provided. It is expected that the course leader will guide participants accordingly.

### Case Abstract

An Islamic bond (*sukuk*) has economic characteristics similar to those of a conventional bond, but is structured so as to be compliant with Shari'a law and can be sold to Islamic investors who are prohibited by Shari'a law from investing in conventional debt securities. This case describes Qatar Global Sukuk (QGS) issuing rated trust certificates (Sukuk), the proceeds of which will ultimately be used for general funding purposes by the Government of the State of Qatar. The rationale for this transaction is to allow the Government of the State of Qatar to raise shariah compliant funds.

QGS purchased a certain land parcel from the Government of the State of Qatar. The land parcel was leased by QGS to the Government of the State of Qatar for a 7-year period corresponding to the duration of the trust certificates. QGS declared that it would hold these assets in trust for the holders of the trust certificates. The lease rental payment from the Government of the State of Qatar to QGS will exactly match the periodic distribution payments payable on the trust certificates. The lease rental payment is calculated based on 6-month US dollar LIBOR plus a margin.

‘Those who take riba (usury or interest) will not stand but as stands the one whom the demon has driven crazy by his touch.’

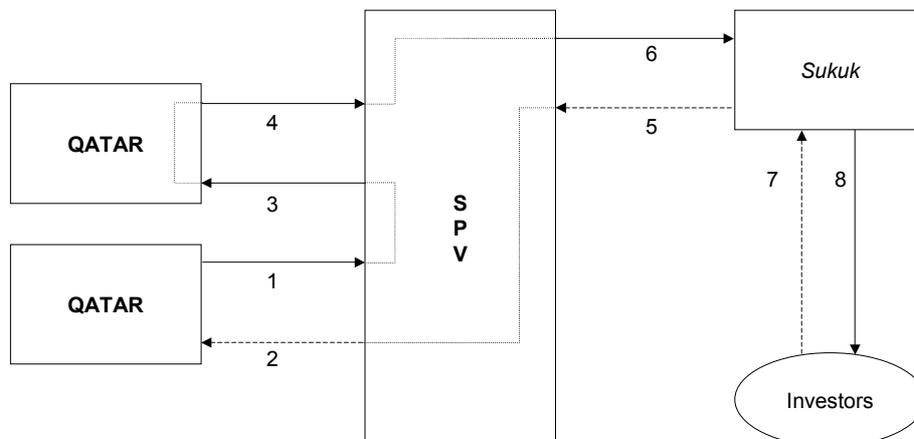
Qur’an Sura 2:275-280

## Qatar Global Sukuk

Qatar Global Sukuk QSC was incorporated as a joint stock company in Doha during October 2003, and established a joint-venture special purpose vehicle (SPV) by the government of Qatar, Qatar International Islamic Bank (QIIB) and HSBC. On 8<sup>th</sup> October, 2003 the government of Qatar issued US \$700 million worth of Trust Certificates (*sukuk*) due 2010. The proceeds from this issuance were utilised to finance the construction and development of the Hamad Medical City located in Doha, Qatar.

Each certificate holder has an undivided *beneficiary right* to a *land parcel* (which is the medical complex) between October 2003 and 2010. Under the arrangement, the SPV buys the parcels from the government of Qatar and re-sells them to the buyers of the issues. It does so by buying the beneficiary rights and keeping them as a trust and issuing trust certificates (*sukuk*) to the investors. The distribution dates are the ninth day of every April and October. The SPV, on behalf of the investor, leases the land parcel back to the Government of Qatar in conformity with the Master *Ijarah* Agreement. Under the terms of the agreement between the issuer (lessor) and government (lessee) the rental payments are to be calculated semi-annually (in April and October) with reference to LIBOR plus the margin, and will equal the periodic distribution amounts payable on the respective dates. These rental payments are equivalent to the semi-annual distribution funds. The returns are guaranteed by the government of Qatar, and thus replicate floating rate Qatari sovereign debt instruments. The certificates were rated A+ by Standard & Poor’s (S&P) and applications were made to list the issuances on both the Luxembourg Stock Exchange and the Labuan International Financial exchange (Malaysia). See Figure 1 for details of the structure.

**Figure 1: The Qatar Sovereign *Ijarah* Sukuk Structure**



- The government of Qatar sells land parcels valued at US \$700 million
- The purchase price is US \$ 700 million
- The SPV leases out the land parcels back to the Government of Qatar

- The Government of Qatar pays semi-annual lease rentals
- The SPV disburses semi-annual distribution payments equal to the government's rental payments
- Investors (both Islamic and conventional) secure the *sukuk* issuances
- The investors are reimbursed periodically by the distributions from the SPV funded by the government rental payments on the land parcels

The periodic distributions are floating rate which are calculated for the first four distribution dates using the equation:

$$(\text{LIBOR for the return accumulation period plus margin of 0.4\%}) \times (\$700 \text{ M}) \times (\text{number of days in return accumulation period}/360)$$

After the first four distribution dates, the periodic distribution is calculated as:

$$\text{Amortization Payment} + (\text{LIBOR for such return accumulation period plus margin of 0.4\%}) \times (\$700 \text{ M}) \times (\text{number of days in return accumulation period}/360)$$

The Prospectus for the Qatar Global Sukuk can be found on

<http://lfxsys.lfx.com.my/others/qatar/Offering%20Circular%208%20oct%202003.pdf>

## Summary of the Offering

### Parties

Issuer	Qatar Global Sukuk QSC, a joint stock company incorporated in Qatar under Article 68 of the Commercial Companies Law, Law No. 5 of the year 2002 (the " <b>Issuer</b> "). The Issuer has been incorporated solely for the purpose of participating in the transactions contemplated by the Transaction Documents (as defined below).
Ownership of the Issuer	The authorised and issued share capital of the Issuer is 30 Riyals divided into three ordinary shares of par value 10 Riyals each. The Issuer's ordinary shares are owned by the Government and HSBC Bank Middle East Limited (in the latter case, solely as agent for the Certificate holders). Pursuant to a Share Agency Declaration dated the Closing Date (the " <b>Share Agency Declaration</b> ") made by HSBC Bank Middle East Limited (in such capacity, the " <b>Share Agent</b> "), the Share Agent holds its share in the Issuer (the " <b>Golden Share</b> ") as agent for and on behalf of Certificateholders.
Seller	The Government (in such capacity, the " <b>Seller</b> ") will convey to the Issuer (as trustee and agent for and on behalf of

Certificateholders) title to a certain Land Parcel (as defined below) pursuant to the Purchase Agreement (as defined below).

Lessee

The Government will lease from the Issuer the Land Parcel on the terms set out in the Master Ijara Agreement (as defined below) for a period of seven years commencing on the Closing Date and terminating on the Periodic Distribution Date falling in October 2010.

### Summary of the Certificates

Certificates	US\$700,000,000 Trust Certificates due 2010 (the “ <b>Certificates</b> ” or the “ <b>Sukuk</b> ”) .
Closing Date	9 October 2003.
Issue Price	100 per cent of the aggregate principal amount of the Certificates.
Form and Delivery of the Certificates	<p>The Certificates will be issued in registered global form only, without coupons attached.</p> <p>The Certificates will be represented by interests in the Global Certificate deposited with a common depository for Euroclear and Clearstream, Luxembourg.</p> <p>Definitive certificates evidence holdings of Certificates will only be issued in exchange for interests in the Global Certificate in certain limited circumstances.</p>
Clearance and Settlement	<p>Holders of the Certificates may elect to hold their interest in the Global Certificate in book-entry form through each of Euroclear or Clearstream, Luxembourg. Transfers within Clearstream, Luxembourg or Euroclear will be in accordance with the usual rules and operating procedures of the relevant clearance system.</p>
Denominations	The Certificates will be issued in minimum denominations of US\$10,000 and integral multiples of US\$1,000 in excess thereof.
Status	Each Certificate represents an undivided beneficial ownership in the Trust Assets and will rank <i>pari passu</i> , without any preference, with the other Certificates.
The Trust Assets	<p>The “<b>Trust</b>” is the trust created by the Issuer under the Declaration of Trust.</p> <p>The “<b>Trust Assets</b>” are the Land Parcel, all of the Issuer’s rights, title, interest and benefit, present and future, in, to and under the Transaction Documents to which it is a party, all monies standing to the credit of the Transaction Account, and all proceeds of the foregoing.</p>
The Purchase Agreement	Pursuant to the Purchase Agreement, the Seller will sell to the Issuer the Land Parcel (free from all claims and encumbrances and with all attached or accrued rights as of the date of the Purchase Agreement). The gross proceeds received by the

	<p>Issuer from the issuance and sale of the Certificates will be used to pay the aggregate purchase price payable by the Issuer to the Seller for the Land Parcel.</p>
Land Parcel	<p>The “<b>Land Parcel</b>” is the plot of land designated for the proposed development of Hamad Medical City in Doha, Qatar.</p>
The Master Ijara Agreement	<p>Under the terms of a Master Ijara Agreement dated the Closing Date between the Issuer as lessor and the Government as lessee (the “<b>Master Ijara Agreement</b>”), the Issuer will agree to lease to the Government, and the Government will agree to lease from the Issuer, the Land Parcel during the term commencing on the Closing Date and extending to the Scheduled Dissolution Date.</p>
Rentals	<p>The Rentals will be paid by the Government on each Periodic Distribution Date directly to the Transaction Account. Upon receipt of each Rental on the relevant Periodic Distribution Date, the Payment Administrator will withdraw such monies from the Transaction Account and use such amounts to make payments on, among other things, the Certificates in the order of priority set out below.</p>
Limited Recourse	<p>Each Certificate represents solely an undivided beneficial ownership interest in the Trust Assets. Holders of the Certificates will have no recourse to any assets of the Issuer other than the Trust Assets. Any creditor of the Issuer (other than Certificateholders) will have no recourse to the Trust Assets. Proceeds of the Trust Assets are the sole source of payments on the Certificates. The Certificates do not represent an interest in or obligation of any of the Issuer, the Government (to the extent it fulfils all of its obligations under the relevant Transaction Documents), the Joint Lead Managers, the Agents or the Payment Administrator or any affiliate of any of the foregoing entities. Accordingly, Certificateholders will have no recourse to any assets of the Issuer (other than the Trust Assets), the Government (to the extent it fulfils all of its obligations under the Transaction Documents to which it is a party), the Joint Lead Managers, the Agents or the Payment Administrator or any affiliate of any of the foregoing entities in respect of any shortfall in the expected amounts from the Trust Assets. However, the Government is obliged to make the payments under the Transaction Documents to which it is a party directly to the Issuer, and the Issuer, as trustee for the benefit of the Certificateholders and any other Trustee, will have direct recourse against the Government to recover payments due to the Issuer from the Government pursuant to the Transaction Documents to which the Government is a party.</p>
Negative Pledge	<p>So long as any of the Certificates remains outstanding, the Issuer and the Government (to the extent provided in the Master Ijara Agreement) have undertaken that neither will secure any of its present or future indebtedness for borrowed money by any lien, pledge, charge or other security interest upon any of its present or future assets, properties or revenues (other than those arising by operation of law).</p>
Use of Proceeds	<p>The gross proceeds of the issue of the Certificates will be used by</p>

	the Issuer to purchase the Land Parcel from the Seller pursuant to the Purchase Agreement.
Listing	Application will be made to list the Certificates on the Luxembourg Stock Exchange and the Labuan International Finance Exchange.
Rating	The Certificates have been rated "A+" by S&P.
Governing Law	The Declaration of Trust, the Agency Agreement, the Certificate Purchase Agreement and the Certificates will be governed by English law.  The Purchase Agreement, the Master Ijara Agreement, the Purchase Undertaking, the Sale Undertaking, the Agency Declaration, the Share Agency Declaration and the Costs Undertaking will be governed by Qatari law.

## Investment Considerations

***There is currently no secondary market for the Certificates and there may be limited liquidity for Certificateholders.*** There can be no assurances that a secondary market for the Certificates will develop, or if a secondary market does develop, that it will provide the Certificateholders with liquidity of investment or that it will continue for the life of the Certificates. The market value of Certificates may fluctuate. Consequently, any sale of Certificates by Certificateholders in any secondary market which may develop may be at a discount from the original purchase price of such Certificates. Consequently, an investor in the Certificates must be prepared to hold the Certificates for an indefinite period of time or until their maturity.

***The Issuer has no operating history.*** The Issuer is a newly formed entity and has no significant operating history. The Issuer will have no material assets other than the Land Parcel, which will be leased to Qatar pursuant to the Master Ijara Agreement. The Issuer will not engage in any business activity than the issuance of the Certificates and the acquisition and lease of the Land Parcel as described herein and other activities incidental or related to the foregoing. Payments by Qatar under the Master Ijara Agreement, the Purchase Undertaking and the Sale Undertaking, which payments are direct obligations of Qatar to the Issuer, will be the Issuer's principal source of funds.

***The Certificates are limited recourse, unsecured obligations of the Trust.*** Recourse to the Issuer is limited to the Trust Assets and proceeds of the Trust Assets are the sole source of payments on the Certificates. Upon occurrence of a Dissolution Event, the only remedy available to Certificateholders will be to exercise the option under the Purchase Undertaking to require Qatar to purchase the Land Parcel at the Exercise Price. Certificateholders will otherwise have no recourse to any assets of Qatar (to the extent it fulfils all of its obligations under the Transaction Documents to which it is a party), the Joint Lead Managers, the Agents or the Payment Administrator or any affiliate of any of the foregoing entities in respect of any shortfall in the expected amounts from the Trust Assets. Qatar is obliged to make its payments under the Transaction Documents to which it is a party directly to the Issuer, and the Issuer, as trustee for the benefit of the Certificateholders, will have direct recourse against Qatar to recover payments due to the Issuer from Qatar pursuant to the Transaction Documents to which Qatar is a party. There can be no assurance that the net proceeds of the realisation of, or the enforcement with respect to, the Trust Assets will be sufficient to make all payments due in respect of the Certificates.

***The ratings on the Certificates may be changed at any time and may adversely affect the fair market value of the Certificates.*** It is a condition to the issuance of the Certificates that

the Certificates be rated “A+” by S&P upon issuance. The rating addresses the likelihood of full and timely payment to the Certificateholders of all payments of Periodic Distribution Amounts on the Certificates on each Periodic Distribution Date. The ratings of the Certificates will be based primarily on the credit rating of Qatar. If S&P lower their ratings of Qatar, the rating of the Certificates may be lowered by S&P. A rating is not a recommendation to purchase, hold or sell the Certificates. There is no assurance that a rating will remain in effect for any given period of time or that a rating will not be lowered or withdrawn entirely by an assigning rating agency. If the ratings initially assigned to the Certificates are subsequently lowered or withdrawn for any reason, no person or entity will be obligated to provide any additional credit enhancement with respect to the Certificates. Any reduction or withdrawal of a rating may have an adverse effect on the liquidity and market price of the Certificates. Any reduction or withdrawal of a rating will not constitute an event of default with respect to the Certificates or an event requiring the Issuer to redeem any Certificates.

### **Qatar Global Sukuk: Case Study questions**

Following the recent string of successful Sukuk issues, and the fact that they are a relatively new concept in corporate finance, your employer, an Investment Bank, has selected your group to make presentations to the Board regarding the key issues involved.

Your group must consider the following questions and you must present your findings to the whole class. Please be ready to explain any technical concepts to the class. You will be expected to defend your answers.

Remember that “time is money” and that your responses must be succinct and not overly descriptive. In other words – get to the point!!

1. Describe the exact nature of the Qatar Sukuk
2. What Islamic modes of finance underpin the Qatar Sukuk?
3. Describe how these modes of finance work and the exact relationship they have with the Qatar Sukuk
4. What investment considerations would you need to take account of when considering investing in these Sukuk.
5. Is Qatar a good place to invest?
6. What Sharia Board requirements were put in place?
7. Are issues of corporate governance relevant to this issue?
8. What was innovative about this issue?
9. How was the issue rated and by whom?
10. Was the issue a success?
11. What lessons can be learnt for the issue of future sukuk? How do the critical factors for Qatar Sukuk compare with those for the other Sukuk issued.?

Identify the following parties in the Qatar Sukuk:

Issuer

Ownership of the Issuer  
Seller  
Lessee

Identify and explain the following elements of the Sukuk Certificates:

Form and Delivery of the Certificates  
Clearance and Settlement  
Denominations  
Status  
The Trust Assets  
Purchase Agreement  
Land Parcel  
The Master Ijara Agreement  
Rentals  
Limited Recourse  
Negative Pledge  
Use of Proceeds  
Listing  
Rating  
Governing Law

Demonstrate with a flow chart the nature of the underlying transactions.