

Sukūk: AN ALTERNATIVE TO BANGLADESH'S EXISTING BOND MARKET

By

A.K.M Tanzimul Haq

A project submitted in the fulfillment of the requirements for the degree of Bachelor of
Business Administration in Finance.

BRAC University

BRAC Business School

Dhaka, Bangladesh

May 24, 2016

May24, 2016

Syeda Saherabanu Shahbazi

Lecturer,

BRAC Business School

BRAC University.

Subject: Letter of Transmittal

Dear Madam,

With due respects, I, Tanzimul Haq, an undergraduate student of BBA Spring-2016 Batch have reported on '*Sukūk*: An Alternative to Bangladesh's Existing Bond Market' under the course of BUS 400 (Internship).

Although the report consists of the basic facts of the conventional bond and the alternative of the aforesaid financial instrument, this report has enabled me to obtain practical knowledge about my research on bonds and its alternative. Thank you for your supportive cooperation for permitting me to research and present my ideas. Without your vindication, this report would be an incomplete one.

Lastly, I would be thankful once again if you please give your judicious advice on effort.

Yours Sincerely,

A.K.M Tanzimul Haq

I.D: 10104006

ACKNOWLEDGEMENTS

For this opportunity, I would like to thank the following people:

- **M.M Mostafizur Rahman: AVP and Branch Manager, First Security Islamic Bank (Ring Road Branch)** –for giving me the opportunity to complete my internship in his branch.
- **ShamsiaJahan:SPO, First Security Islamic Bank (Ring Road Branch)** – for supervising my day to day work and guidance.
- **Masud Rahman: Senior Officer First Security Islamic Bank (Ring Road Branch)**
- **Md. Monirul Islam: Officer, First Security Islamic Bank (Ring Road Branch)**
- **Syeda Saherabanu Shahbazi: Lecturer, BRAC Business School** – for her generous guidance and assistance to help me complete this course, and for the preparation of this report.

Table of Contents

<u>TOPIC</u>	<u>PAGE NO.</u>
• Executive Summary	1
• Organizational Profile	2-7
• Job Description	8
• Project Orientation	9
• Project Details	10
• Chapter 1: Literature Review	11-15
• Chapter 2: Bond Market in Bangladesh	16-19
• Chapter 3: <i>Sukūk</i> -An Alternate of Bond	20-40
• Project Analysis	41-42
• Recommendation	43
• Reference	44-46
• Appendix	

Executive Summary

The following report has been prepared in response to the fulfillment of the successful completion of Bachelor's degree in Business Administration with the major concentration in Finance.

The report has been divided into three major portions as instructed by the department and the format provided.

The first part contains detailed information about the organization, its historical background, vision, mission and strategic goals. In addition, a brief description of the organization's current product and services has also been added to the report along with its future plans.

The second part contains brief description about the job I was involved with, its specifications, scopes, key learning points, and different aspects. Critical observations and recommendations have also been provided in this part.

The Final part contains the project which has been designed to test theoretical and practical knowledge of the knowledge acquired from the in-house sessions I have received.

First part of the project contains detailed information about the existing bond market in Bangladesh, and the obstacles the market has been facing that hinders its improvement. This part tests the theoretical knowledge gathered from textbooks and similar reading materials.

The second part is more experimental and exposed to the practical knowledge. In this part a specific financial instrument has been experimented with to see whether it will be a better substitute to boost the dynamics of Bangladesh's current bond market.

Due to the shortage of time, there has been a lack of in-depth researches which could have been provided to make the report more enriched.

ORGANIZATIONAL PROFILE

- **INTRODUCTION**

Currently I am completing my bachelor's degree majoring in Finance at BRAC University. As a mandatory part of the BBA program, I have completed a 3-month internship in First Security Islamic Bank Ltd.

The prime reason for doing my internship was to obtain a practical knowledge about the day-to-day activities of an organization, especially a bank, along with a new path of learning, improving, and developing a whole new set of skills.

The reason I chose First Security Islamic Bank Ltd., because of its good reputation as a new generation bank, working style, friendly environment, ample resources etc.

- **HISTORY**

First Security Islamic Bank Ltd was formed on August 29, 1999. Enlisted as a banking company on the same date, First Security Islamic Bank Ltd started its operation with registered office located in Dilkusha. On September 20, 1999, the bank received license from Bangladesh Bank for issuing IPO.

Currently the bank is in its 16th year of operation, and has been providing an excellent service to all its customers through their wide network of 148 branches across Bangladesh. The bank's head office is currently located in Gulshan-1.

First Security Islamic Bank Ltd. was established focusing on the new generation banking system which would include internet and mobile banking, ATM facilities, online remittance receiving facilities etc.

In addition, First Security Islamic Bank is encouraging school banking systems by encouraging students' manage their savings by the means of opening savings account and depositing their pocket moneys.

- **Mission Objectives:**

1. To contribute to the socio-economic development of the country.
2. To attain the highest level of satisfaction through the extension of services by dedicated and motivated professionals.
3. To maintain continuous growth of market share by ensuring quality.
4. To ensure ethics and transparency in all levels.
5. To ensure sustainable growth and establish full value of the honorable shareholders and above all, to contribute effectively to the national economy.

- **Vision:**

To be the premier financial institution in the country by providing high quality products and services backed by latest technology and a team of highly motivated personnel to deliver excellence in banking.

- **Strategies:**

1. To achieve our customer's best satisfaction & win their confidence.
2. To manage & operate the bank in the most effective manner.
3. To identify customer's need & monitor their perception towards meeting those requirements.
4. To review & update policies, procedures & practices to enhance the ability to extend better customer services.
5. To train & develop all employees & provide them adequate resources so that a customer's need can reasonably addressed.
6. To promote organizational efficiency by disclosing company plans, policies, and procedures openly to the employees in a timely fashion.
7. To ensure a congenial working environment.
8. To diversify portfolio in both retail & wholesale market.

- **PRODUCT OFFERINGS**

First Security Islamic Bank offers a wide range of product to their clients. A client can easily choose from a wide range of deposit schemes, or s/he can choose to remain with the conventional products. In addition, the bank provides several types of deposit scheme and savings account for students of school, college, and university.

There are basically four types of product the bank currently offers to its clients:

1. ***Al-Wadiah* Current deposit**
2. ***Mudārabah* Savings Deposit**
3. ***Mudārabah* Term Deposit**
4. ***Mudārabah* Deposit Schemes**

These basic products are categorized differently according to the client's needs. All of the categorized products have been described below:

- **Current Deposit Accounts:**

1. *Al-Wadiah* Current Deposit (111)
2. ***Morjada*** (*Al-Wadiah* Current Plus) (117)
3. ***Somman*** (*Al-Wadiah* Current Premium) (118)

- **Savings Deposit Accounts:**

1. *Mudārabah* Staff Salary Account (121)
2. *Mudārabah* General Savings Account (122)
3. ***Mehenoti*** (*Mudārabah* Workers Savings Account) (124)
4. ***Onkur*** (*Mudārabah* Students Savings Account) (125)
5. ***Prapti*** (*Mudārabah* Salary Savings Account) (126)
6. ***Probeen*** (*Mudārabah* Senior Citizen Savings Account) (127)
7. ***Projonmo*** (*Mudārabah* New Generation Savings Account) (128)
8. Mobile Banking Service Account (129)
9. *Mudārabah* Special Notice Savings Account (131)

- **Term Deposit Accounts:**

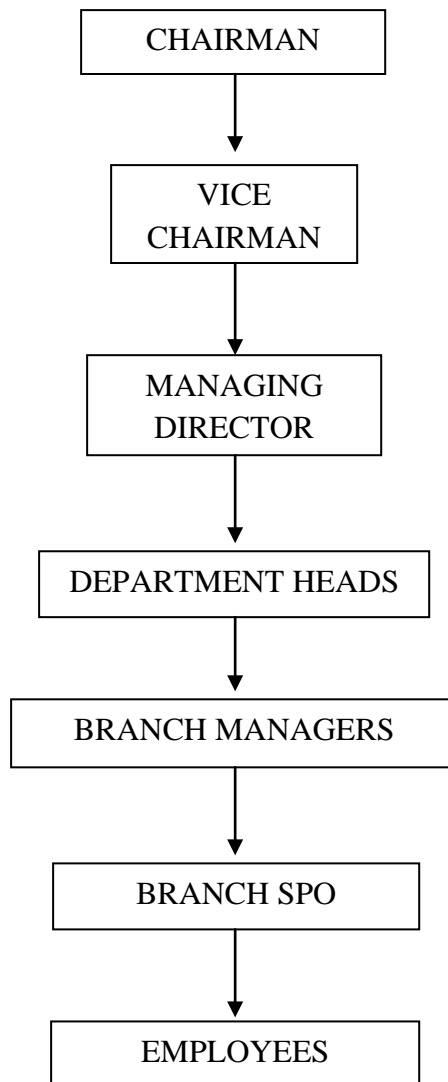
1. *Mudārabah* Term Deposit (1-month maturity period) Account (241)
2. *Mudārabah* Term Deposit (3-month maturity period) Account (243)
3. *Mudārabah* Term Deposit (6-month maturity period) Account (246)
4. *Mudārabah* Term Deposit (1 year maturity period) Account (244)

- **Deposit Scheme Accounts:**

1. *Mudārabah* New Generation Deposit Scheme (**Uddipon**)
2. *Mudārabah* Education Deposit Scheme (*Alo*)
3. *Mudārabah* Double Deposit Scheme
4. *Mudārabah* Triple Benefit Scheme
5. *Mudārabah* Four Times Benefit Scheme (*Araba*)
6. *Mudārabah* Monthly Profit Scheme
7. *Mudārabah* Marriage Deposit Scheme (*Bondhon*)
8. *Mudārabah* Health care Deposit Scheme (*Niramoy*)
9. *Mudārabah* Pension Deposit Scheme (*Obosor*)
10. *Mudārabah* Non-residential Bangladeshi Deposit Scheme (*Sodesh*)
11. *Mudārabah* Housewife Deposit Scheme (*Ghoroni*)
12. *Mudārabah* Millionaire Deposit Scheme (*Agrosor*)
13. *Mudārabah* Crorepati Deposit Scheme (*Unnoti*)

Other services include locker systems, receiving foreign remittance (western union, money gram), and inter-bank transfer systems.

Operational Network Organogram



- **FUTURE VISIONS**

First Security Islamic Bank is currently now in its 16th year of operation, and as they consider themselves to be very new in banking sector with a very little experience gathered from these years of service to the public, the bank believes that it has a long way to go down the road.

For their long term plans they have recently acquired the ownership of United Commercial Bank and National Credit and Commerce Bank in order to utilize their resources for their business expansion.

In addition, they have plans for opening more branches both in Dhaka and outside of the capital so that they can conduct their banking services throughout the country. Providing customers with better services is also one of their main key objectives.

JOB DESCRIPTION

During my internship program, I was assigned to the bank's cheque clearing department in order to obtain specific knowledge about the clearing process of cheques, its importance within the three modes of transaction held by the bank, and the necessary formalities and official process of documenting all the details needed to run the department's operational works smoothly.

The key responsibilities that were given to me were as follows:

1. Keep and register all outward going cheques of the bank.
2. Learn about the common mistakes of writing a cheque.
3. Learn the manual process of clearing an outward going cheque.

Besides the main responsibilities, I performed some other out-of-department duties in order to enhance my experience level and knowledge of a bank. They were as follows:

1. Front desk jobs, i.e., serving clients, processing account forms, understanding different forms of vouchers, bank statements, etc.
2. Learning how to create a pay order.
3. Gaining a general knowledge about opening an LC.
4. Gaining basic knowledge of client supplementary statements.
5. Learning about the bank's organizational culture.

My practical work exposed me to the challenges that an aspirant candidate would have to face in order to procure a strong career in banking sector. The most important factor that I have learned from my internship program was to adopt with an organization's atmosphere, its people and handle operational tasks.

In addition, I also obtained practical knowledge about the different work procedures of a bank which would serve me as a basic ground during my corporate career.

PROJECT ORIENTATION

- **General Summary**

For my internship project, I chose a rather specific topic where I can justify my theoretical knowledge with the practical knowledge.

The project undertaken by me contains a two-part research and analysis. The first part explains the current situation of bond market in Bangladesh, its size, investors, and the problems it contain. Being finance major, I designed this part as to implement my theoretical knowledge.

The second part contains more analytical section as I have tried to show whether an alternative of bond can be introduced to the market that would put more dynamics to the economic circulation of our country.

For my alternate source, *Sukūk*, a specific financial instrument was chosen and primary works has been done in the project to show how it can be more reliable than a corporate bond. Since Bangladesh is a Muslim country, it was only imperative that choosing an instrument belonging to Islamic finance would be more helpful in making the project.

Due to a limited amount of time, the in-depth researches were not added to the project which is a major disadvantage in making this report.

PROJECT DETAILS

- **Objective:**

The prime objective of the project was to understand the current situation of bond market in Bangladesh, and to unearth the reasons for its ongoing problems. The specific objectives of this project are as follows:

1. To get an overview of the history and evolution of bond market in Bangladesh.
2. To identify the specific characteristics of bond market in Bangladesh.
3. To identify the problems of debt market in Bangladesh.
4. To get introduced with *Sukūk* (Islamic Bond), its characteristics, differences with conventional bond and share, and its benefits.
5. To improvise the *Sukūk* in different aspects of financial activities.

- **Methodology:**

Most of the primary data are collected from Bangladesh bank, Securities and Exchange Commission (SEC), Dhaka Stock Exchange (DSE), Islamic Financial Service Board (IFSB), and Central Depository Bangladesh Limited (CDBL).

The secondary data were collected from the following resources:

1. Banking Regulation and Policy Department, Bangladesh bank.
2. Newspaper articles.
3. Website materials.
4. Govt. Publications.
5. Journals.

- **Limitations:**

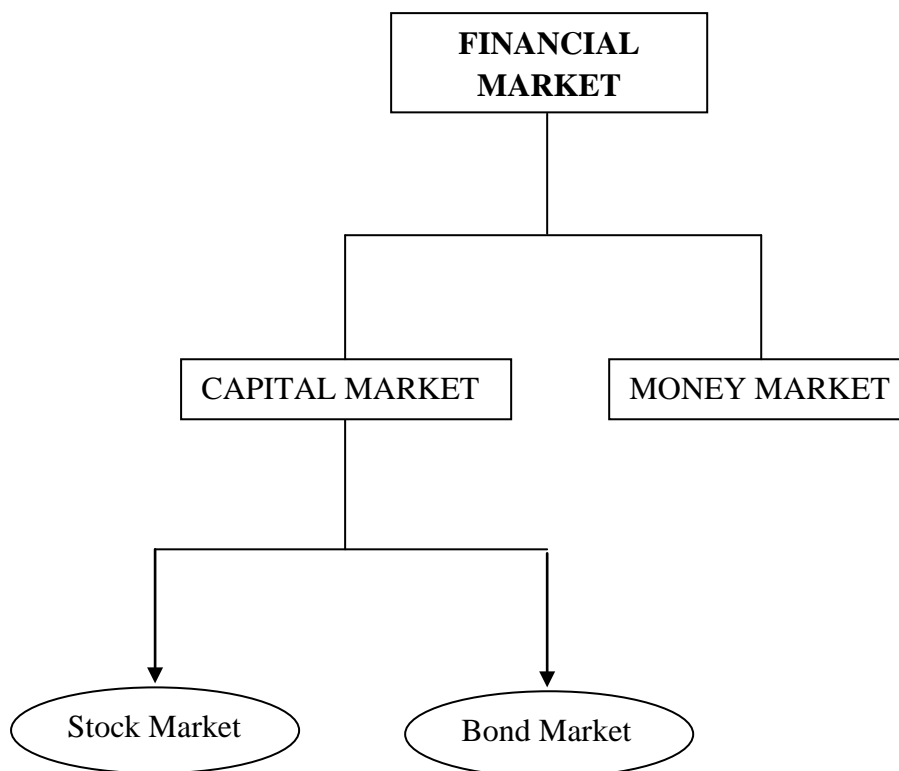
Certain data set pertaining to government borrowing especially for state own enterprises are unavailable. Not all data are verified or validated due to data characteristics.

CHAPTER 1

1.1 Literature Review:

Economists consider financial markets as a primary pillar supporting and stimulating economic growth and also in setting the velocity of growth. The markets help in allocating savings and deciding on the optimal use in the economic circuit. The markets in addition provide an avenue for raising capital mainly for the private sector, the government and also public sector units. Every capital market has distinctive characteristics, resulting from history, culture, and legal structure though gradually today they tend to operate on common ground with identical basic features.

Bond market is a connected part of the financial market. Since the focus of this research is on bond markets, the discussion is restricted to bond markets. Further discussion will provide some theoretical understanding about bond markets, its features, and general obstacles faced by bond markets in Asian countries in developing the strategies.



1.2 Definition of a Bond

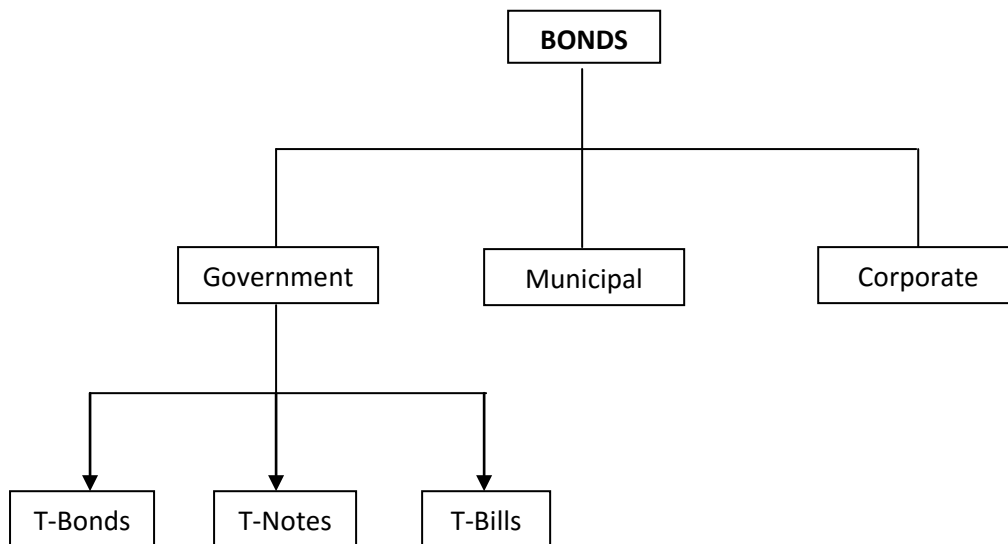
A bond is debt instrument issued for a specific period for the purpose of raising capital by borrowing. A bond is a long-term obligation. Generally, a bond is fixed interest financial instrument issued by Government, Corporate, and other large entities. In other words, a bond is an agreement to repay the principal along with the interest or coupon. There are some bonds which carry a zero coupon or interest but have fixed term. These bonds are called as zero coupon bond or deep discount bond bonds. These bonds are sold at a price which will be far below the face value of the bond depending on the risk characteristics and prevailing interest rates in the market.

Bonds are tradable and basically the price of a bond depends on the existing interest rates in the market for an equally risky instrument and the coupon on the bond. A bond market has the role to facilitate the flow of long-term funds from surplus units to deficit units.

Thus bond acts as a loan where the buyer or holder of the bond is the lender or creditor, the issuer is the borrower or debtor and the coupon is the interest.

1.3 Types of Bond

A simple way to classify bonds is based on the different kind of issuers. There are 3 main issuers of a conventional bond which has been described below:



- **Government Bonds**

According to the length of duration, government bonds can be classified into three main categories. They are as follows.

Bills: debt securities whose maturity period is less than one year.

Notes: debt securities whose maturity period is 1 to 10 years.

Bonds: debt securities whose maturity period is more than 10 years.

- **Municipal Bonds**

These are called governmental agency bonds. These bonds are not issued directly by the government but with the backing of the government. In most countries, the returns from municipal bond are free from government tax. Because of this tax advantage, the interest on a municipal bond is normally lower than that of a taxable bond. Thus, a municipal bond can be a great investment opportunity on an after-tax basis.

- **Corporate Bonds**

A company can issue bonds like stocks. Corporate have many options to increase its capital from the market, the perimeter is whatever the market will bear. Corporate may issue short-term (less than 5 years), medium-term (5 to 10 years) and long-term (more than 10 years) bonds. Corporate bond may be convertible i.e. the holder can convert it into stock. It can be callable also, which allows the company to redeem an issue prior to maturity.

There are some other types of bonds such as lottery bond, war bond, serial bond, revenue bond, climate bond etc.

1.4 Features of a Conventional Bond

The key features of a conventional bond are described below:

- **Face Value:** It is the amount on which interest is paid and normally which has to be repaid by the issuer at maturity. It is also called principal, nominal or par value.
- **Issue Price:** It is the amount which a buyer pays when the bonds are first issued. Generally, this value will be almost equal to the face value. Thus the net amount which the issuer receives is the issue price minus the issuance fees.

- **Maturity:** It is the date on which the issuers have to repay the principal amount. The issuers have no more obligations to the bond holders when they repay the principal amount at the maturity date. Usually bonds can be divided into three categories on the basis of maturity:
 1. Short-Term Bonds: Bonds having a maturity between 1-5 years.
 2. Mid-Term Bonds: Bonds having a maturity between 5-10 years.
 3. Long-Term Bonds: Bonds having a maturity longer than 10 years.
- **Coupon:** It is the interest rate which the issuer has to pay to the bond holders. In case of a conventional bond, the coupon rates are always fixed.
- **Convertibility:** When the bondholders are allowed to exchange the bonds into the issuer's common stock, they are called convertible bonds.

1.5 Risks Associated with the Issuance of a Conventional Bond

There are certain risks associated with the issuance of a conventional bond which are to be carefully assessed by both the issuer and the investor. These risks are described as follows:

- **Interest Rate Risk:**

The prices of bonds are negatively related to interest rates. If the interest rates increase, the prices of bonds will decrease. The coupon (interest) of a bond is set at the time of issuance. The buyers will not be willing to purchase the bonds in the secondary market at earlier rate if the interest rates increase. For example, if the coupon is 7% and the interest rate of an equally risky instrument in the market is at 8%, the interest rate on bond is less what makes investors motivated to invest the high interest bearing instruments. Thus it can be risky to buy long-term bonds at the time of low interest rates.

- **Credit Risk:**

A few organizations who issue bonds rarely default on their obligations just as individuals occasionally default on their loans. The value of the investment is completely lost in this case. Bonds issued by government, are usually protected from default. Municipal bonds are defaulted very infrequently. The best part s of municipal and corporate bonds is that the holders of the bonds are compensated with a higher interest rate for assuming a higher risk. The interest rate on corporate bonds is higher than that of municipal bonds, which is higher than that of government bonds. Furthermore, there is a rating system that helps the investors to know the amount of risk for each class of bonds.

- **Call Risk:**

The Company may call back some bonds which are issued earlier. When a company wants to issue new bonds at lower price, it redeems it existing bonds. This creates forces to the investors to reinvest the principal earlier than expected, usually at a lower interest rate.

- **Inflation Risk:**

Usually the yield on the bond is set at time of issuance, as is the principal which will be returned at maturity date. The real value of the investment will suffer if there is a significant inflation over the period the investor holds the bond.

CHAPTER 2

Bond Market of Bangladesh

2.1 History

Currently Bangladesh bond market plays a small role in the economy. The bond market is very thin compared to the neighboring countries. At the end of 2014, the outstanding bond amount was only 12 % of GDP, compared to Sri Lanka (55%), India (35%), and Pakistan (31%). The share of the Bangladesh bond market among South Asian countries was only 0.2% the smallest among the five countries.

The market is dominated by the fixed income government debt instruments. The maximum savings of small investors are mobilized by only one instrument name National Saving Certificate. The interest on this saving certificate is higher than that of other bonds in the market. Besides the national saving certificate, the other government debt instruments are treasury bills and treasury bonds.

In December 2003, government issued 5 and 10 years' maturity treasury bonds and 15 and 20 years' bond were issued in July 2007. The capital raising pattern has been changed from a focus in treasury bills to a noteworthy increase in treasury bonds. Consequently, the ratio of treasury bills from about 20: 80 in 2005 to 80:20 in 2011. Banks and financial institutions are the main buyers of treasury bonds. Commercial banks have obligation to purchase government securities as it is accepted security to meet their statutory liquidity requirement (SLR) under the Banking Companies Act. This is still a small market. Banks and financial instruments which have SLR obligations are the only participants in this market. The government bonds are rarely traded on the exchange.

In September 2006, the Ministry of Finance started publishing the yearly treasury bills and bonds auction calendar. The calendar shows the information of dates, types of instruments and amount of each auction. Bangladesh bank also started publishing the auction results on its website.

Bangladesh corporate debt market is very small in size. The outstanding amount is only 0.2% of GDP. Thus corporate bond market in Bangladesh is at a budding stage. During 1988-2011, only 3 corporate bonds and 14 debentures were issued by public offerings.

Many of these bonds and debentures were partially convertible to common stocks. The biggest issue of corporate bond was made first in 2007. It was a perpetual bond named 'IBBL

Mudārabah Perpetual Bond’ with a size of Taka 3,000 million (approximately US\$ 40 million). It is an Islamic bond on profit sharing basis since interest is prohibited by *Sharī’ah* principles. At the end of 2011, three corporate bonds and eight debentures were outstanding. The corporate bond market of Bangladesh faces manifold impediments although it has a good prospectus because of an expected growth in financial market. It is believed that the availability of long-term instruments is a prerequisite for developing an efficient market structure.

2.2 Constraints on Development of Bond Market in Bangladesh

The sluggish growth of the bond market in Bangladesh has been recognized due to a number of factors which are described below:

- **Limited Number of Investors:** The numbers of investors willing to invest in the bond are very few in numbers compared to the investors in stock market.
- **Capital Gain:** The chances of capital gain in bonds are limited whereas most of the investors in Bangladesh look for the first option while investing their savings.
- **High Rate of Return in Govt. Bonds:** Rates of return in risk-free government bonds are too high, and as a result corporate bond issuers have to set the rates even higher to compensate the risk an investor would take while investing in their bonds.
- **Alternate Sources of Funding:** Loans from commercial banks are a good source of alternate funding for a company rather than issuing bonds, because borrowing from banks in Bangladesh is quick and flexible along with low interest rates compared to issuing debt instruments which carries high risk rate.
- **Weak market Infrastructure:** Bond market in Bangladesh has no structured rules and regulations, nor do they have any strong market infrastructure. Market failure is considered as a common scenario. As a result, investors either go for risk-free government bonds, or they invest in the stock market instead.
- **Underdeveloped tax System:** The overall taxation system in Bangladesh is still underdeveloped. Taxes can be easily avoided by using unfair means. As a result, tax incentives given against bonds are not very high and effective.
- **Illiquid Secondary Market:** Illiquidity in the secondary market of government debt securities makes constraints makes it difficult to determine the proper pricing of the treasury bonds in the market.

- **High Interest rate:** The interest rate on national savings is comparatively high in Bangladesh along with its risk-free policy. For this reason investors are more attracted to these kinds of savings and ignore the debt securities issued by companies.
- **High Transaction Cost:** One of the major problem in issuing bonds is the high cost of issuance. A company, before issuing debt instruments has to pay the registration fees, stamp duties, ancillary charges, and annual trustee fees on the outstanding amount in the market. These costs can sometimes de-motivate companies from issuing new bonds.
- **Cheap Syndicate Loans:** It is common in Bangladesh where several banks form a syndicate and provide customized loans to fund large projects. Since these loans are customized to suit the needs of a borrower (company), they become uninterested in issuing bonds.
- **Default on Interest Payment:** Since the bond market is underdeveloped in Bangladesh, and where market failure is a common scenario, it is expected that the bond issuing companies might default on paying interest. In addition, government bonds are risk-free and have a high rate of return which is a fact investors feel discouraged to invest in corporate bonds.
- **Inexperienced Investors:** Investors in Bangladesh are extremely inexperienced. Instead of going for a steady cash flow income, they opt for capital gain by investing more in stock market. In addition, investors in Bangladesh are highly speculative. They invest money based on rumors rather than market analysis.

2.3 Existing Corporate Bonds in Bangladesh

Currently, only two types of bond exist in the bond market in Bangladesh which is:

- IBBL *Mudārabah* Perpetual Bond, issued by Islamic Bank Bangladesh Ltd.
- BRAC-EPL sub 25% Convertible Bond, issued by BRAC Bank.

Islamic Bank Bangladesh Ltd issued the *Mudārabah* perpetual bond in 2007 in order to collect the necessary funds for their Tier-1 capital. The bond has been issued under the strict rules of *Sharī'ah*, and do not follow the usual rules of a conventional bond. Total paid-up capital for this bond is BDT 3000 million, and each bond has a face value of BDT 1000.

This bond can be purchased by any individual or companies as 100% of this bond is publicly funded. Since it is a perpetual bond, the bondholder will continue to gain profits from it for infinite periods of time.

The second existing corporate bond in Bangladesh was issued by BRAC-EPL in 2010 with the same requirements as the first one. The bond issued has a 25% conversion option-meaning investors can convert 25% of the current value of their bond into common shares. The total paid-up capital of this bond is BDT 2967 million, and each bond has a face value of BDT 1000. 90% of the bond is publicly funded while 10% of the ownership was given to government.

CHAPTER 3

***Sukūk*: An Alternative of Conventional Bond**

3.1 Primary Overview

Previously it has been discussed that a conventional bond issuance has some common problems for the both the issuer and the investor. Besides the problems, conventional bondholders receive a certain amount of interest which is considered as *riba* (interest) according to the principles of *Sharī'ah*, because it is a kind of social evil, and contrary to the welfare of the people.

It has been mentioned in the Holy Quran that:

“Those who devour usury will not stand except as stands one whom the Satan by his touch has driven to madness. This is because they say: “Trade is like usury.” But Allah hath permitted trade and forbidden usury. Those who after receiving admonition from their Lord, desist, shall be pardoned for the past. Their case is for Allah (to judge), but those who repeat (the offence) are companions of the fire. They will abide therein (forever).” (2:275)

Islamic finance has always promoted trade and discouraged usury, and the banking and financial sectors are allowed to conduct their activities by following this same rule. A business institution, be it trade, commerce, industry, transportation, power or agriculture has to work for profit.

For example, if a banking institution is contributing to productivity, they have to share the productivity in the form of profit; and profit cannot be pre-determined before the costs are booked against business revenue and the profit and loss account is prepared (Sharif, 1996).

Bangladesh is a place where 88% of the population is from Islam background. So it is only imperative that they follow the rules of Islamic financing system in their business activities, and for that, a specific instrument of Islamic finance system-a substitute to the conventional bond has been introduced in details in this paper.

3.2 Introduction

Sukūk (plural of *Sakk*) are certificates where each *Sakk* represents the proportional and undivided right over all kinds of tangible and intangible (i.e. goodwill) assets, monetary assets usufruct, services or debts, or pools of such assets or a business venture (i.e. *Mudārabah* or *Mushārah*). The mentioned asset must be clearly identifiable, and may be in a specific project or investment activity in accordance with *Sharī'ah*.

Issuance of *Sukūk* including the utilization of funds which has been raised through such issuance should not involve any elements of *riba* (interest), *gharar* (uncertainty), and any such activities prohibited in *Sharī'ah*. The ownership right on *Sukūk* assets may be either a right of legal ownership, or a right of beneficial ownership through trust which holds the assets for the benefit of the *Sukūk* holders, commonly known as 'asset-backed *Sukūk*'.

In most of the cases, *Sukūk* has been known to everyone as 'Islamic bond'. However, *Sukūk*, is in fact not a bond, and neither it is similar to corporate share. *Sukūk* is in a sense, a different kind of financial instrument even though it resembles some features of bonds and shares.

A table below illustrates the characteristics of *Sukūk*, and indicates how this financial instrument is different from bonds and shares:

Determinants	<i>Sukūk</i>	Bonds	Shares
Nature	Not a debt of issuer, but common ownership share in specific asset/business venture.	Debt of issuer.	Ownership share in a company.
Assets	A minimum of certain percentage of tangible assets that meets the <i>Sharī'ah</i> compliance.	Generally no assets are required.	Not required.

Claims	Ownership claims on the specific asset or business venture	Creditors claim on the borrowing entity, and in some cases, liens on assets.	Ownership claims on the company.
Security	Secured by ownership rights in the underlying assets/venture in addition to any additional collateral structure.	Generally unsecured except in cases such as mortgage-backed securities.	Totally unsecured.
Principal & Return	Not guaranteed by the issuer.	Guaranteed by the issuer.	Not guaranteed by the company.
Purpose	Must be issued only for <i>Sharī'ah</i> compliant purposes.	Can be issued for any purpose.	Can be offered for any kind of purpose.
Trading of security	Sale of ownership interest in a specific asset /venture.	Sale of debt instrument.	Sale of shares in a company.
Holder's responsibilities	Responsibility for defined duties relating to the underlying asset/venture limited to the extent of participation of the issue.	Bond holders do not have any responsibilities for the circumstances of the issuer.	Responsibility for the affairs of the company limited to the extent of holding in the company.

Asset related expenses	Asset related expenses may be attached to <i>Sukūk</i> .	Bond holders are not required to pay any asset related expenses, if any.	Not required to pay.
Prices	Prices of the <i>Sukūk</i> depend on the market value of underlying assets.	Prices are based on the creditworthiness of the issuer.	Prices are based on the future expectations of <i>inter alia</i> earnings and dividends of the firm.
Issuer's insolvency	<i>Sukūk</i> holder's recovery depends on the quality of underlying assets.	Complete/partial loss of lent money and/or interests for the bond holders.	Shareholders are second in line to the bond holders in the event of insolvency.

Considering the facts and the differentiations, it can be clearly understood that *Sukūk* is completely a different kind of financial instrument having its own unique features, rules and regulations.

To be more specific, a mathematical example has been shown below:

- **Example:**

Suppose, a piece of industrial machinery costs Tk. 1 million, and in order to acquire the machine, the company either has issued:

1. Corporate bonds, with a face value of Tk. 1,000, coupon rate of 10%, and a maturity period of 5 years. Or,
2. *Sukūk*, with a face value of Tk. 1,000, with the same maturity as the bond's, and a proportionate profit.

Market rate of return for both of the cases is 12%, and is supposed to be constant for ease of calculations.

1,000 certificates of bonds/*Sukūk* were issued, and an individual has purchased a single certificate of either one of them. Therefore, the present value of the bond would be:

$$\begin{aligned}
 V &= I (PVIFA_{12\%, 5}) + MV (PVIF_{12\%, 5}) \\
 &= \text{Tk. } 100(3.9655) + \text{Tk. } 1,000(0.567) \\
 &= \text{Tk. } 396.55 + \text{Tk. } 567 \\
 &= \text{Tk. } 963.55
 \end{aligned}$$

In case if the issuer has issued *Sukūk*, then the present value of the certificate would be:

Value of the Asset (Tk.)*	Value of each <i>Sakk</i> (Tk.)	Provisional Rate of Profit	Net Profit on Asset (Tk.)	Proportional Profit on each <i>Sakk</i> (Tk.)
900,000	900	8%	72,000	72
800,000	800	9%	72,000	72
700,000	700	11%	77,000	77
600,000	600	10%	60,000	60
500,000	500	7%	35,000	35

*A depreciation of Tk. 100,000 has been deducted for each year.

$$\begin{aligned}
 V &= \frac{P}{(1+k_d)^1} + \frac{P}{(1+k_d)^2} + \frac{P}{(1+k_d)^3} + \frac{P}{(1+k_d)^4} + \frac{P}{(1+k_d)^5} + \frac{MV}{(1+k_d)^5} \\
 &= \frac{72}{(1.12)^1} + \frac{72}{(1.12)^2} + \frac{77}{(1.12)^3} + \frac{60}{(1.12)^4} + \frac{35}{(1.12)^5} + \frac{500}{(1.12)^5} \\
 &= \text{Tk. } 64.29 + \text{Tk. } 57.40 + \text{Tk. } 54.81 + \text{Tk. } 38.13 + \text{Tk. } 19.86 + 283.71 \\
 &= \text{Tk. } 234.49 + \text{Tk. } 283.71 \\
 &= \text{Tk. } 518.2
 \end{aligned}$$

From the example, we can see that *Sukūk* and bond is not the same.

3.3 Classification of Sukūk

Sukūk can be issued against all major products offered by Islamic financial system. However, not all *Sukūk* can be traded in the secondary market, as some of them are issued without any backing of tangible assets. This kind of *Sukūk*, however can be bought or sold, but no additional benefit could be derived from them except the par value. Any additional benefit derived from non-asset backed *Sukūk* will fall under *riba* (interest).

General classifications where *Sukūk* can be issued against products of Islamic financial system are described below:

- **Salam Sukūk:**

Salam Sukūk represents proportionate ownership of the capital ownership of *Salam* transaction, where the *Salam* capital is constituted by an advance payment to counterparty as supplier of commodity (the subject matter) to be delivered at a future date. This type of *Sukūk* is generally considered to be non-tradable, since the subject matter is considered to be a financial asset, i.e. a receivable.

The gross return to the *Sukūk* holders consists of the margin/spread between the purchase price of the subject matter and its selling price following delivery. In certain, *Sukūk* issues, a third party gives an undertaking that the subject matter will be sold at a price exceeding the purchase price by a specified margin. This may be achieved by means of a parallel *Salam* transaction in which a third party purchases the subject matter for delivery on the same delivery date as in the original *Salam* contract.

- **Istisnā Sukūk:**

Istisnā Sukūk represents proportionate shares in the financing of a project to construct an asset at a price to be paid in future installments, the total of which equals the total face value of the *Sukūk*, in addition to mark-up. The *Sukūk* can be in the form of serial notes or certificates with different maturity dates that match the progress schedule of installments as agreed between the *Sukūk* issuer (as manager on behalf of the *Sukūk* investors), and the construction firm.

It is allowed to trade (generally no-tradable) *Istianā Sukūk* in cases where the funds have been utilized to build or construct the asset for the *Sukūk* holders during the *Istisnā* period. In the case of parallel *Istisnā*, if the value of *Istisnā* is being paid in cash or the assets have already been delivered to the buyers, and then the tradability of such *Sukūk* will be subject to the rules of dealing with debt. The subject matter in *IstisnāSukūk* is considered to be a non-financial asset (work in process inventory).

- ***Ijārah Sukūk:***

Ijārah Sukūk represents the holder's proportionate ownership in a leased asset where the *Sukūk* holders will collectively assume the rights and obligations of the lessor. The *Sukūk* holders are entitled to a share of the lease rentals in proportion to their ownership shares in the leased asset or assets. *Ijārah Sukūk* are tradable from the issuance of date, as the subject matter is a non-financial asset owned by the *Sukūk* holders.

As a proportionate owner, an *IjārahSukūk* holder assumes a proportionate share of any loss if the leased asset is destroyed, or the cost of meeting the obligation to provide an alternative asset, failing which the lessee can terminate the lease without paying future rentals.

- ***Mushārahah Sukūk:***

This kind of *Sukūk* represents the direct proportionate ownership shares of the holders in the assets of a private commercial enterprise or project, where the subscription money is normally employed in purchasing non-liquid assets or assets such as real estate or moveable assets.

A *Mushārahah Sukūk* is a profit and loss sharing instrument where the exposure is of the nature of an equity position in the banking book, except in the case of investments (normally short-term) in assets for trading purpose.

- **Mudārabah Sukūk:**

Sukūk holders subscribe to the certificates issued by a *Mudārib* and share the profit/bear any losses arising from the *Mudārabah* operations. The returns to the holders are dependent on the revenue by the underlying investment. *Sukūk* issued against *Mudārabah* contract has no secondary market options.

- **Wakālah Sukūk:**

The *Wakālah Sukūk* holders provide the capital for *Sharī'ah* compliant investment activity, and the investment agent (*Wakīl*) undertakes the investment of the funds. These *Sukūk* entitle the holders to a return in proportion to their investment in the underlying assets and a right under a purchase undertaking to buy all or a proportion of the underlying assets if certain conditions are fulfilled.

- **Murābahah Sukūk:**

For the case of a *Murābahah Sukūk*, the originator (and also, in some cases, the issuer) of the *Sukūk* is the buyer (on credit) of the *Murābahah* asset, the *Sukūk* investors are the sellers (on credit) of that asset, and the credit provided by the *Sukūk* investors and received by the issuer consists of the *Murābahah* selling price of the asset, which the originator sells to obtain the necessary funds it seeks.

The *Sukūk* holders own the *Murābahah* and are entitled to receive payment of that receivable (the selling price of the asset), either in installment or in a lump sum at the end of the contract. Such *Sukūk*, being securitized receivables, are not generally considered tradable in most cases.

3.4 Usage of *Sukūk* around the World

After the issue of using *Sukūk* instead of bonds was raised in 1998, several countries came forward to look into the matter, and set up with the formalities of the usage of *Sukūk* in their respective countries.

According to the 2014 Global Islamic Finance Report, around \$1.813 trillion worth of assets are being managed with the help of *Sukūk* around the world.

Sukūk was first introduced in Malaysia by SHELL MDS which was worth RM 125 million. Since then, many other countries have been adopting this idea and improving their economic pictures. At first the usage of *Sukūk* was only limited to Muslim countries, but from 2009, that line was broken when Singapore showed interest in issuing this instrument.

Current market of outstanding *Sukūk* has been estimated to be around \$882 billion in the world.

(Source: HSBC)

List of Countries that use *Sukūk*

1. Bahrain
2. Brunei
3. Egypt
4. Gambia
5. Indonesia
6. Iran
7. Malaysia
8. Kazakhstan
9. Kuwait
10. Pakistan
11. Qatar
12. Singapore
13. Saudi Arab
14. Somalia
15. U.K (June 25, 2014)
16. Turkey

- 17. U.A.E
- 18. Hong Kong (Mid-2015)
- 19. Bangladesh (Limited Case)

More countries are showing interest in issuing *Sukūk* rather than issuing conventional bonds. The economic meltdown of 2008 has speed up the process of adapting *Sukūk* in many Non-Muslims countries.

Issuance of *Sukūk* around the world

2007	\$ 13.8 billion
2008	\$ 2.14 billion
2009	\$ 7.47 billion
2010	\$ 5.35 billion

(Source: 2012 International Islamic Financial Report, p-12)

3.5 Usage of Sukūk in Bangladesh

Before 2004, no Islamic banks or financial institutions in Bangladesh issued Islamic instruments in the primary or secondary market for the mobilization of financial resources, and they were fully dependent on the deposited funds.

However, due to the need of the mobilization of financial resources, Bangladesh Bank issued *Mudārabah* bond named as ‘Bangladesh Government Islamic Investment Bond (BGIIB)’, in October 2004, on behalf of the government to support Islamic banks and financial institutions especially to encourage their investment which is to be considered as liquid assets for meeting requirements of SLR.

The bond is an approved security for the purpose of modifiable SLR as well as providing an outlet for investment or procurement of funds by the banks. In addition, the bond is also open for investment by any private individual, companies or large corporations.

The prime features of BGIIB are as follows:

1. The BGIIB will be governed by the Islamic *Shari’ah*, i.e. the principals of issuing *Mudārabah Sukūk* discussed earlier in the paper.
2. The BGIIB means the document of definite value issued in the name of their owners against funds they pay to the issuer or Bangladesh Bank.
3. Profit Sharing Ratios (PSR) relating to the bond may be determined separately for each deal. Bangladesh bank will act as a *Mudārib* in this case.
4. Under the rules, any individual, private or public companies Islamic banks and financial institutions may purchase the bond. Any non-resident Bangladeshi may also invest in the bond from his/her NFCD account maintained with any bank in Bangladesh.
5. The minimum amount of investment may be Tk. 100,000 and multiples thereof, and the rates of return to be given to the investors are as follows:
 - a) For the period of investment of 6 months: PSR is 80:20 in which 80% profit will be given to the bond holders, and 20% will be retained by Bangladesh Bank.
 - b) For the period of investment of 1 year: PSR is 90:10 in which 90% profit will be given to the bond holders, and 10% will be retained by Bangladesh Bank.

- c) For the period of investment of 2 years: PSR is 95:5 in which 95% profit will be given to the bond holders while 5% profit will be retained by Bangladesh Bank.
6. BGIIB may be used as collateral for availing loan or investment form any financial institutions. In this case, bond must be recorded in the Subsidiary General Ledger (SGL).
 7. BGIIB is qualified securities for the purpose of complying with the liquid asset requirements to be maintained by the banks and financial institutions. With regard to this, Bangladesh Bank may provide the discount window facility for banks and financial institutions to buy or sell the bonds with Bangladesh Bank.
 8. There is a provision in the rules that the bond holders will get interim profit on the maturity date of the bond. This interim profit will be adjusted after finalization of the investment accounts. The interim provision of profit is based on the received monthly profit realized on the invested funds in the Islamic banks or financial institutions (as per Clause No.7-b of the rules). The interim profit rates will be given as follows:
 - a) For 6 months BGIIB: 2% less from the realized average rate of profit generated through financing of the Islamic investment bond proceeds.
 - b) For 1 year BGIIB: 1.5% less from the realized average rate of profit generated through financing of the Islamic investment bond proceeds.
 - c) For 2 years BGIIB: 1% less from the realized average rate of profit generated through financing of the Islamic investment bond proceeds.
 9. The trading of the BGIIB will be based on the interim profit rate derived from the investments of those with the Islamic banks. The interim profit rate will be reviewed on monthly basis.
 10. The formula for calculating the profit element to be paid to the bond holders is as follows:

$$B = \frac{prt(k)}{Y}$$

Where **B** = Profit payable on the bond investor, **p** = Principal investment to the BGIIB, **r**= Rate of monthly profit received (in % per annum), **t** = bond period (number of days invested), **k** = Profit sharing ratio to be applied to the bond holders, and **Y** = 365 days.

11. BGIIB may not be a transferable instrument for more or less than its face value. If it is returned to the Bangladesh Bank before maturity, then the bond holder may be eligible to get only the principal amount invested. No profit will be allowed for the period before or after maturity of the bond, if not encashed on maturity.

Government Islamic Investment Bonds are playing an important role in developing the Islamic banking system of Bangladesh, whereby Islamic banks and financial institutions are actively participating to park their cash surpluses.

Bangladesh Government sells Islamic bonds based upon 3 different types of maturity dates – 6 months, 1 year, and 2 years. Generally these bonds are sold to different banks and insurance companies, who on the other hand, invest these bonds on a short term basis, ranging from 30 days to 6 months.

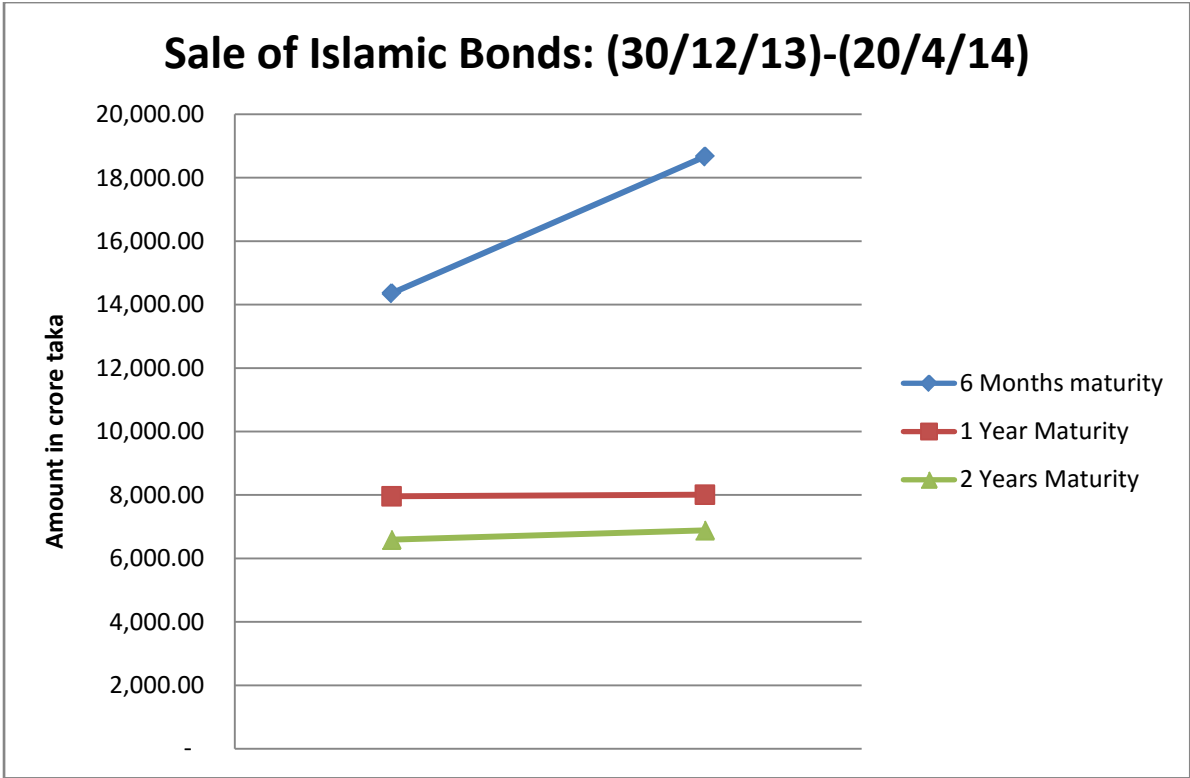
Analyses about the recent activities of selling and investing activities of Islamic bonds given in two different points along with the names of some banks with the detailed amount of the bonds they purchased from the government and how much they have invested it.

From the provided tables, we can see that the banks were more interested in purchasing bonds with a lower maturity period. Around half of all the bonds sold to the banks stated in the table were of 6 months maturity period.

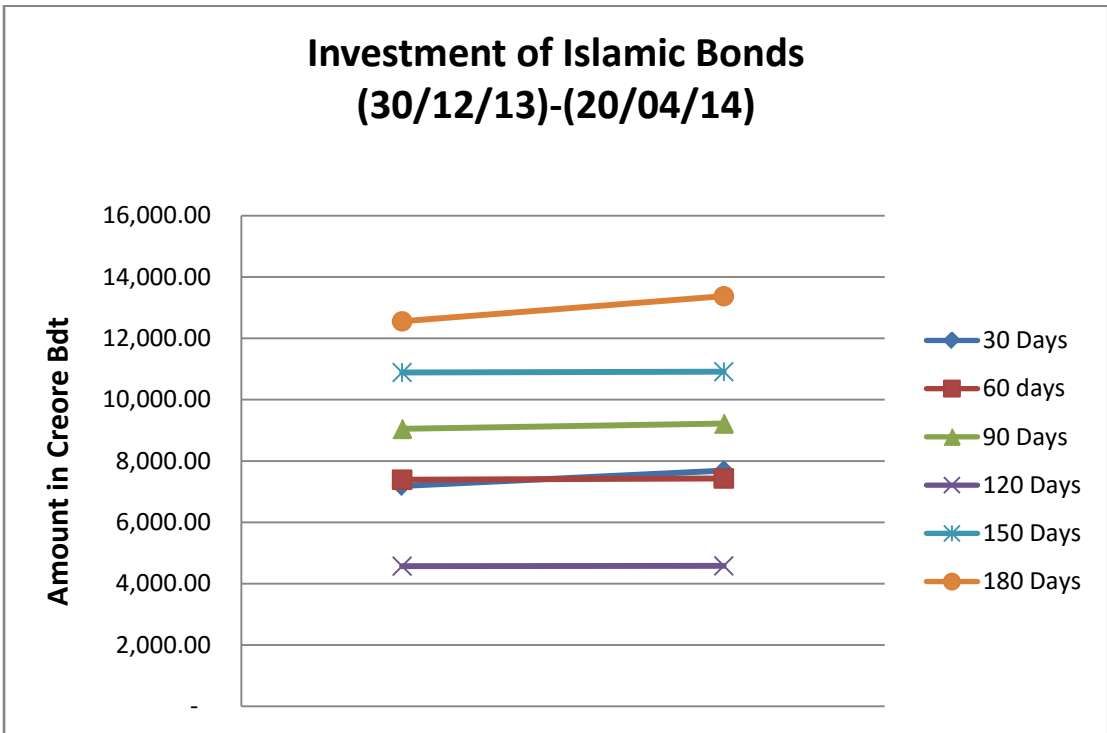
Banks were more interested in buying low maturity period bonds, because the bonds having a low maturity period carries a lower amount of risk compared to the bonds with a higher maturity period.

In addition, around two-third of all the bonds sold to the banks stated in the table were returned to Bangladesh Bank on the date of maturity.

The graphical chart provided below also supports the statement of banks choosing bonds with a lower maturity period over the higher ones:



Bonds purchased by these banks were invested in different sectors of economy to gain return from them. Generally the bonds are invested for a period of time not lasting more than 180 days. Details about these investment patterns of bonds are given below:



From the graph, it is clear that more investment has been made by the banks on a 180-day maturity basis. Other than that, all other investment options remained the same through this two time point.

The major factor that has been found out between the sale and investment pattern of Islamic bonds is that both sale and investment time periods revolve around a specific time frame, in this case 6 months. It means that banks prefer to purchase and invest Islamic bonds that have a maturity period not more than 6 months.

- **Mudārabah Perpetual Bond**

This is another form of *Sukūk* which was introduced shortly after the Islamic bonds were issued. This bond is a perpetual bond, and will not be redeemed by the issuer. Unlike any, it will be registered and traded in the stock market.

Investors would get a profit by deploying *Mudārabah* fund at the weight of 1.25 plus equivalent to 10% of the declared dividend. The bonds are, however, subordinated to the depositors, but remain high compared to the shareholders in respect of repayment of dividend and profit. *Mudārabah* perpetual bonds are treated as a component of *Mudārabah* deposit, and regarded as supplementary capital up to the maximum 30% of Tier-1 capital.

This bond is fully governed by the rule and principal of utilization and distribution of profit of *Mudārabah* fund. The bond is fully paid-up, and the bond holder is not entitled to any kind of investment facilities against the bonds. Tax on profit on the bonds is determined in accordance with the principals of NBR.

The MPB is a *Sharī'ah* based product. The fund being collected on *Mudārabah* principles through the MPB is deployed in business activities under *Sharī'ah* principles. *Mudārabah* arises when a provider of capital called the *rabb al mal* (or a group of such capital providers) enters into a contract with a manager (called the *mudarib*) to engage in any specific trade activity with the objective of sharing the potential profit. At the core of any *Mudārabah* contract there are four basic conditions between the *mudarib* and the capital provider(s) which are as follows:

1. Profit, when realized, has to be shared between the two parties in accordance with a profit sharing ratio pre-stipulated at the time of the contract. If loss occurs, it has to be borne entirely by the *rabb al mal* as the *mudarib* only losses his/her effort.
2. The *rabb al mal* cannot disrupt the day to day management of the *Mudārabah*, apart from his/her right to restrict possible fields of economic activity for the *Mudārabah*. The provision, however, has to be made clear within the contract.
3. The *mudarib* has a ‘hand of trust’ (*yad amna*) in the management of *Mudārabah* capital, which means he/she would work to his/her best effort, and therefore, cannot guarantee profit or capital to *rabb al mal*.
4. Loss of capital can be guaranteed by the *mudarib* only when such loss proves to be the result of mismanagement or delinquency of the *mudarib*; or where such loss results from a breach of the contract, like violating restricted fields of economic activity.

The MPB will not carry any fixed profit percentage; rather the profit percentage will vary from time to time, depending on the overall profitability of the asset pool of the bank. That means the investors of MPB are exposed to certain amount of business risk which is an essential requirement of income of the MPB holders being *Sharī’ah* compliant.

Unlike the interest based traditional bond, MPB is a subordinate instrument. As a *Mudārabah* instrument, it gets priority over the shareholders in respect of getting profit and also refund of principal in case of liquidation of the bank. The bond holders will however, stand subordinated to the depositors in respect of the payment of both profit and refund of principal.

The MPB has been listed with both of the bourse of the country and it remains freely transferable depending on the market demand. The bond holders are not entitled to enjoy any rights or privileges as enjoyed by the shareholders except statutory requirements.

ANALYSIS ON THE PROJECT

Since *Sukūk* has been adopted by both Islamic and Non-Islamic countries, it can be said from the primary perspective that *Sukūk* has gained popularity very fast across the world since its introduction.

Even though the instrument has lots of added benefits, there are some drawbacks that might seem inappropriate to some investors. For instance, *Sukūk* can only be used for purposes

which fall under the *Sharī'ah* compliance, meaning that any financial activities that is out of the compliance cannot be financed by *Sukūk*, and even it does, that would not be considered as *Sukūk* financing, but a project financed by conventional bond/share.

Secondly, *Sukūk* holders have to face loss (if it occurs) just like a shareholder of a common stock would do whereas *Sukūk* has been mentioned to be an intermediary between bond and share. If the investors treat *Sukūk* as a bond, and if loss occurs, they would lose money like common stock which would hamper their purpose of investment.

For instance, if an investor would like to have a steady cash flow but invested in *Sukūk*, then there is a slim chance of losing money. Therefore, *Sukūk* would not serve the purpose of that investor.

Thirdly, some of the forms of *Sukūk* have no secondary market. They cannot be bought or sold with a price higher or lower than the face value. For this, investors might be demotivated in investing in *Sukūk*.

Sukūk holders have to bear the cost associated with the underlying assets which the bond/shareholders do not have to consider. Investors might not feel interested to bear the cost and invest at the same time.

Last but not the least; *Sukūk* can be issued against tangible assets only. It does not allow us to invest in intangible assets in a business.

Although *Sukūk* have these mentioned disadvantages/limitations, there are some benefits which only a *Sukūk* holder or the issuer can enjoy.

Firstly, *Sukūk* can be issued against any tangible assets, both as an individual asset or a group of similar or different assets that falls under *Sharī'ah* compliance. So if any individual or company wishes to issue *Sukūk* on a single asset they can easily do that.

Like share, *Sukūk* certificates can sometimes return high profits on the underlying asset(s), but a bondholder will only get a certain amount of income from the bond, and nothing more.

Sukūk can be issued by government for financing large construction projects. For example, Bangladesh government can issue *Istisnā Sukūk* to finance their large construction projects like bridge construction, or sea port development, industrial area setups etc.

Issuer of the *Sukūk* can gain some advantage compared to issuing bonds. Since the issuer has to pay a certain amount of fixed interest to the investor even the business fails, this might pose a threat to them. On the other hand, if the issuer hands over the *Sukūk*, they will only have to give the profit or divide the loss.

RECOMMENDATIONS

Sukūk is an individual financial instrument which serves specific purposes of an investor. Therefore, no certain recommendations can be imposed, because the purpose of *Sukūk* varies from one investor to another.

The prime focus of issuing and investing in *Sukūk* is based on religious background. Since it is strictly forbidden in Islam to receive any kind of interest in business, *Sukūk* in this case may serve better purpose than a conventional bond. In Bangladesh where 88% of the total population belongs to the Islamic ethnicity, *Sukūk* may be a better option than a conventional bond for conducting business.

Since the economic meltdown in 2008 has slowed down the worldwide business, and where it is the main feature of a bond to return its holder a fixed amount of interest income at the end of every period, issuing a bond may not be the best option to raise fund when there is an uncertainty of distributing such fixed incomes.

Since *Sukūk* holders receive income on the underlying asset they have invested upon, they are aware of the fluctuation of the profit received from their *Sukūk* certificate, even loss. Therefore, it can be recommended that with situations like this, *Sukūk* may be proven more useful than a conventional bond.

Sukūk holders may share profit or face loss in their certificates; this option will only attract the experienced investor who knows in which business to invest funds and are aware of managing a diversified portfolio. As more experienced investors would invest in *Sukūk*, the overall financial market would become more dynamic.

Sukūk can be issued against a single asset or a group of asset. Businesses that have a small capital would be able to issue *Sukūk* on their limited assets and raise funds. As a result, more companies would be interested to conduct business and diversify their investments and fund-raising options.

REFERENCE

- Mujeri, M. K. and Rahman, M. H. (2008). “Financing Long Term Investment in Bangladesh: Capital Market Development Issues” Policy Paper: Bangladesh Bank: 0905.
- Rose, P. S. (2003). “Money and Capital Markets”, Financial Institution and Instruments in a Global Market Place, Eighth Edition, McGraw Hill, Higher Education. PP. 4-7.
- Usha Thorat and T. Rabi Sankar, (April, 2005- April, 2011), “Developing a Yield Curve and Promoting Secondary Market for Government Debt in Bangladesh”, Phase I-XI, Bangladesh Bank.
- Islam, Md. Ezazul and Bisnu Pada (2006), “Public Debt Management and debt Sustainability in Bangladesh”, Working Paper No. WP0705, PAU, Bangladesh Bank, Dhaka.
- Ahmed. Faruquddin. (1999). “The Money Market in Bangladesh” Bank Parikrama, Vol. XIX, Nos. 3 & 4 September and December 1994, pp. 19-34.
- Azad. Abul Kalam (December 2002). "Behavior of Treasury Bills Market in Bangladesh", Journal of Business Studies. Dhaka University. Vol XXII, No. 2. pp. 285-302.
- Rangarajan, C., Aupam Basu and Narendra Jadhav (1989), „ Dynamics of Interaction between Government Deficit and Domestic Debt in India“, RBI Occasional Papers, Vol. 10.3,september.
- Bilquees, Faiz (2003), “An Analysis of Budget Deficit, Debt Accumulation, and Debt Instability,” The Pakistan Development Review, Volume 42 No. 3 pp. 177-195.

- Ahmed, Shamim and Md. Ezazul Islam (2006b), "Interest Rate Spread in Bangladesh: An Analytical Review", Bangladesh Bank Quarterly, April-June, 2006, PP. 22-28.
- Mujtuba Kabir, (June 2010), "Sustainability of Public Debt in Bangladesh and Role of Bangladesh Bank", Intern report, IBA, DU.
- Amihud, Y., and H. Mendelson, (1991). "Liquidity, Maturity and the Yield on U.S. Treasury Securities", Journal of Finance, 46, 1411-1425.
- Brandt. W Michael and Kavajecz A. Kenneth, (2003) "Price Discovery in The U.S. Treasury Market:The Impact of Order flow And Liquidity on the Yield Curve", NBER Working Paper 9529.
- Cammack, E.B., (1991), Evidence on bidding strategies and the information in Treasury bill auctions, Journal of Political Economy 99, 100-30.
- Cook, Timothy Q., (1981) "Determinants of the Spread Between Treasury Bill and Private Sector Money Market Rates, " Journal of Economics and Business, vol. 33 (Spring 1981), pp. 177-87
- Cook, Timothy Q., and Thomas Hahn (1990). "Interest Rate Expectation and the Slope of the Money Market Yield Curve" Federal Reserve Bank of Richmond Economic Review, vol. 76. pp.3-26.
- Hardy, Laniel C. (2000). Building Behavior in Treasury Bills Auctions, Evidence Pakistan, IMF Working Paper-WP/00/111, June.
- Kim, Yun-Hwan (2001), Developing Treasury Securities Market in Asia, Asian Development Bank, Manila, June."
- McCullouch, J. Huston., "The Monotonicity of the Term Premium: A Closer Look," Journal of Financial Economics, vol. 18 (March 1987), pp.185-92

- Nyborg, K.G. and S. Sundaresan, (1996), Discriminatory versus uniform Treasury auctions: Evidence from when- issued transactions, *Journal of Financial Economics* 42, 63-104.
- Simon, D.P., (1994a), Markups, quantity risk and bidding strategies at Treasury coupon auctions, *Journal of Financial Economics* 35, 43-62.
- Simon, D.P., 1994b, The Treasury's experiment with single-price auctions in the mid-1970s: Winner's or taxpayer's curse? *Review of Economics and Statics* 76, 754-60.
- Spindt, P.A. and R.W. Stolz, (1992), Are U.S. Treasury bills under priced in the primary market? *Journal of Banking and Finance* 16, 891-908.
- Buitert, W. H. (1985), “A guide to Public Sector Debt and Deficits”, *Economic Policy*, pp. 14-79.
- IMF (2007): *The Debt Sustainability Framework for Low-Income Countries*, at Updated, October 30, IMF.
- IMF Mission (2008), “Bangladesh: Joint Fund-World bank Debt Sustainability Analysis”, IMF staff study.
- GOB: *Flow of External Resources in to Bangladesh, (Various Issues)*, Economic Relation Division, Ministry of Finance, and Dhaka.
- GOB: *Economic Review, (Various Issues)*, Ministry of Finance, Dhaka.
- www.dse.com
- www.stockbangladesh.com
- www.fsiblb.com

**CONSOLIDATED FINANCIAL STATEMENTS
(UN-AUDITED)
OF
FIRST SECURITY ISLAMI BANK LTD.
FOR THE QUARTER ENDED 30 SEPTEMBER 2015**

FIRST SECURITY ISLAMI BANK LIMITED
CONSOLIDATED BALANCE SHEET (Un-audited)
AS AT 30 SEPTEMBER 2015

	September, 2015 Taka	December, 2014 Taka
<u>PROPERTY AND ASSETS</u>		
Cash	21,803,630,155	16,290,256,291
In hand (Including foreign currencies)	1,538,535,437	1,269,388,801
Balance with Bangladesh Bank and its agent bank(s) (Including foreign currencies)	20,265,094,718	15,020,867,490
Balance with other Banks and Financial Institutions	1,135,458,290	597,224,010
In Bangladesh	196,067,292	124,300,885
Outside Bangladesh	939,390,998	472,923,125
Placement with Banks & other Financial Institutions	14,695,000,000	14,094,000,000
Investments in Shares & Securities	12,754,574,076	10,583,235,873
Government	11,620,005,000	9,830,006,400
Others	1,134,569,076	753,229,473
Investments	177,433,101,444	152,370,707,597
General Investment etc.	177,099,951,802	152,069,308,714
Bills Purchased and Negotiated	333,149,642	301,398,883
Fixed Assets Including Premises, Furniture & Intangible Assets	3,162,053,208	3,132,826,430
Other Assets	9,803,895,817	7,808,204,866
Non Banking Assets	-	-
Total Assets	240,787,712,987	204,876,455,067
<u>LIABILITIES AND CAPITAL</u>		
Liabilities		
Placement from Banks & other Financial Institutions	844,626,419	417,565,547
Deposits and Other Accounts	213,905,760,800	182,503,183,390
Al-Wadia Current Deposits and Other Deposit Accounts	10,290,298,409	9,589,544,900
Bills Payable	1,009,911,654	954,717,747
Mudaraba Savings Deposits	12,378,384,860	9,525,501,444
Mudaraba Term Deposits	148,415,366,652	122,347,027,420
Other Mudaraba Deposits	41,811,799,224	40,086,391,879
Mudaraba Subordinated Bond	2,000,000,000	2,382,000,000
Other Liabilities	14,497,755,848	10,926,961,738
Total Liabilities	231,248,143,066	196,229,710,675
Capital/Shareholders' equity		
Paid-up Capital	6,788,738,880	4,114,387,200
Right Share Money Deposit	-	1,564,966,255
Statutory Reserve	1,746,878,452	1,609,267,996
Other Reserve	35,495,817	35,495,817
Asset Revaluation Reserve	382,320,802	382,320,802
Retained Earnings	293,884,546	669,349,319
Total Shareholders' Equity	9,247,318,496	8,375,787,389
Non-controlling Interest	292,251,424	270,957,003
Total Liabilities and Shareholders' Equity	240,787,712,987	204,876,455,067

FIRST SECURITY ISLAMI BANK LIMITED
CONSOLIDATED BALANCE SHEET (Un-audited)
AS AT 30 SEPTEMBER 2015


	September, 2015 <u>Taka</u>	December, 2014 <u>Taka</u>
OFF- BALANCE SHEET ITEMS		
Contingent Liabilities		
Acceptances and Endorsements	15,926,486,590	11,433,615,498
Letters of Guarantee	5,927,161,810	6,381,276,624
Irrevocable Letters of Credit	3,837,116,538	4,910,289,756
Bills for Collection	830,065,077	939,777,561
Other Contingent Liabilities	-	-
Total	26,520,830,015	23,664,959,439
Other Commitments		
Documentary credits and short term trade related transactions	-	-
Forward assets purchased and forward deposits placed	-	-
Undrawn note issuance and revolving underwriting facilities	-	-
Undrawn formal standby facilities, credit lines and other commitments	-	-
Total	-	-
Total Off -Balance Sheet Items Including Contingent Liabilities	26,520,830,015	23,664,959,439


 Chief Financial Officer


 Company Secretary


 Managing Director


 Director


 Chairman

Dhaka, 27 October 2015

FIRST SECURITY ISLAMI BANK LIMITED
CONSOLIDATED PROFIT AND LOSS ACCOUNT (Un-audited)
FOR THE PERIOD 01 JANUARY 2015 TO 30 SEPTEMBER 2015

	Jan-Sept '15 Taka	Jan-Sept '14 Taka	July-Sept '15 Taka	July-Sept '14 Taka
Investments Income	17,221,978,574	15,933,281,839	5,989,169,859	5,446,143,620
Profit Paid on Deposits	(14,021,839,170)	(13,056,386,398)	(4,749,399,334)	(4,526,067,142)
Net Investment Income	3,200,139,404	2,876,895,441	1,239,770,525	920,076,478
Income from Investment in shares & Securities	132,616,216	244,860,620	23,520,831	89,826,943
Commission, Exchange and Brokerage	344,971,780	248,676,603	116,872,901	91,272,220
Other Operating Income	157,133,766	160,730,504	40,076,126	39,287,896
	634,721,762	654,267,727	180,469,858	220,387,059
Total Operating Income	3,834,861,166	3,531,163,168	1,420,240,383	1,140,463,537
Less: Operating Expenses				
Salary and Allowances	1,400,079,380	1,081,168,108	568,758,425	390,089,792
Rent, Taxes, Insurances, Electricity etc.	353,835,135	275,671,921	111,962,528	92,838,816
Legal Expenses	2,665,674	2,670,864	1,493,887	426,391
Postage, Stamps, Telecommunication etc.	16,421,827	14,683,831	5,287,686	5,978,779
Stationery, Printings, Advertisements etc.	140,907,228	108,561,244	27,344,120	28,591,646
Managing Director's Salary and Fees	6,883,675	13,200,000	2,600,000	5,000,000
Auditors' Fees	572,689	579,500	207,563	158,750
Directors' Fees	1,801,050	1,617,150	444,250	298,250
Shariah Committee's Fees	86,750	63,250	-	23,000
Depreciation and Repair of Bank's Assets	270,273,607	213,711,112	90,391,843	73,981,309
Zakat Expenses	31,436,817	18,564,075	10,478,939	188,025
Other Expenses	603,625,909	475,241,832	220,738,067	180,164,958
Total Operating Expenses	2,828,589,741	2,205,732,887	1,039,707,307	777,739,715
Profit before Provision and tax	1,006,271,425	1,325,430,281	380,533,076	362,723,822
Provisions for Investments including off-B/S items	208,583,700	457,400,000	133,000,000	242,400,000
Provisions for diminution in value of investment in shares	52,827,157	47,166,797	15,722,334	(35,746,339)
Total Provisions	261,410,857	504,566,797	148,722,334	206,653,661
Total Profit before Taxes	744,860,568	820,863,484	231,810,742	156,070,161
Provision for Taxation	(344,262,384)	(455,869,282)	(130,165,076)	(94,946,936)
Deferred Tax Income	-	-	-	-
	(344,262,384)	(455,869,282)	(130,165,076)	(94,946,936)
Net Profit after tax for the period	400,598,184	364,994,202	101,645,666	61,123,225
Retained Earnings Brought Forward	669,349,319	506,439,968	243,735,704	474,824,327
	1,069,947,503	871,434,170	345,381,370	535,947,552
Appropriations:				
Statutory Reserve	137,610,456	155,799,928	40,201,022	27,282,083
Non-Controlling Interest	21,294,421	15,893,722	11,295,801	9,389,148
Issue of Bonus Share	617,158,080	-	-	-
Cash Dividend	-	200,464,200	-	-
	776,062,957	372,157,850	51,496,823	36,671,231
Retained Earnings Carried Forward	293,884,546	499,279,805	293,884,546	499,279,805
Earnings Per Share (EPS)	0.59	0.54	0.15	0.09

Chief Financial Officer

Company Secretary

Managing Director

Director

Chairman

Dhaka, 27 October 2015

1

FIRST SECURITY ISLAMI BANK LIMITED
CONSOLIDATED CASH FLOW STATEMENT (Un-audited)
FOR THE PERIOD 01 JANUARY 2015 TO 30 SEPTEMBER 2015

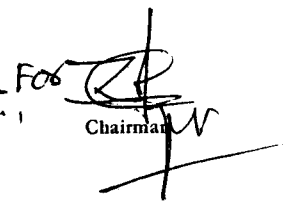
	Sept, 2015 Taka	Sept, 2014 Taka
A. Cash Flow from Operating Activities		
Profit received	16,261,950,937	15,033,961,921
Profit paid	(11,063,259,428)	(11,945,475,269)
Commission, exchange & brokerage received	344,971,780	248,676,603
Payment to employees	(1,406,963,055)	(1,094,368,108)
Payment to suppliers	(173,521,662)	(136,945,635)
Income tax paid	(638,839,567)	(561,808,771)
Received from other operating activities	157,133,666	152,622,761
Paid for other operating activities	(955,157,436)	(315,588,435)
Operating Profit before changes in Operating Assets & Liabilities	2,526,315,235	1,381,075,067
Increase / Decrease in Operating Assets & Liabilities		
Investments to Customers	(24,427,371,157)	(16,485,739,464)
Other Assets	(1,337,553,946)	(871,832,597)
Deposits from Customers	28,443,997,668	32,841,078,300
Other Liabilities	2,966,156,282	2,288,468,191
	5,645,228,847	17,771,974,430
Net Cash Inflow from Operating Activities	8,171,544,082	19,153,049,497
B. Cash Flow from Investing Activities		
Investment in Shares and Securities	(2,171,339,603)	(3,811,384,064)
Purchase of Property, Plant and Equipment	(266,885,952)	(824,845,219)
Sale of Property, Plant and Equipment	-	-
Net Cash Inflow from Investing Activities	(2,438,225,555)	(4,636,229,283)
C. Cash Flow from Financing Activities		
Increase/ (Decrease) in Share Capital	-	-
Receipt from Issue of Right Share	492,227,345	-
Increase/ (Decrease) in Placement from Banks & FI	427,060,872	(4,004,186,208)
Net Cash Inflow/(Outflow) from Financing Activities	919,288,217	(4,004,186,208)
D. Net Increase/Decrease of Cash & Cash Equivalent (A+B+C)	6,652,606,744	10,512,634,006
Effect of Exchange Rate on Cash & Cash Equivalent	-	-
E. Opening Cash & Cash Equivalent	30,981,486,701	25,928,834,862
F. Closing Cash & Cash Equivalent (D+E)	37,634,093,445	36,441,468,868
Cash in hand (Including Foreign Currencies)	1,538,535,437	1,172,506,870
Balance with Bangladesh Bank, other banks & financial institutions	36,095,553,008	35,268,955,598
Prize Bond	5,000	6,400
	37,634,093,445	36,441,468,868


Chief Financial Officer


Company Secretary


Managing Director


Director



Chairman

Dhaka, 27 October 2015

FIRST SECURITY ISLAMI BANK LIMITED
CONSOLIDATED STATEMENT OF CHANGES IN EQUITY (Un-audited)
FOR THE PERIOD 01 JANUARY 2015 TO 30 SEPTEMBER 2015

Particulars	Paid-up Capital	Right Share Deposit	Statutory Reserve	Other Reserve	Assets Reval. Reserve	Retained Earnings	Non-Controlling Interest	Total
	Taka	Taka	Taka	Taka	Taka	Taka	Taka	Taka
Balance as on 01 January 2015	4,114,387,200	1,564,966,255	1,609,267,996	35,495,817	382,320,802	669,349,319	270,957,003	8,646,744,392
Changes in Accounting Policy	-	-	-	-	-	-	-	-
Restated Balance	4,114,387,200	1,564,966,255	1,609,267,996	35,495,817	382,320,802	669,349,319	270,957,003	8,646,744,392
Surplus/Deficit on account of Revaluation of Properties	-	-	-	-	-	-	-	-
Surplus/Deficit on account of Revaluation of Investments	-	-	-	-	-	-	-	-
Net Gains and Losses not Recognized in the Income Statement	-	-	-	-	-	-	-	-
Net Profit for the period	-	-	-	-	-	400,598,184	-	400,598,184
Cash Dividends	-	-	-	-	-	-	-	-
Transfer to Statutory Reserve	-	-	137,610,456	-	-	(137,610,456)	-	-
Transfer to Other Reserve	-	-	-	-	-	-	-	-
Revaluation reserve to Other Reserve	-	-	-	-	-	-	-	-
Issue of Bonus Share	617,158,080	-	-	-	-	(617,158,080)	-	-
Receive Money for Right Share	-	492,227,345	-	-	-	-	-	492,227,345
Capitalized the Right Share Deposit Money	2,057,193,600	(2,057,193,600)	-	-	-	-	-	-
Noncontrolling Interest in Subsidiary Profit	-	-	-	-	-	(21,294,421)	21,294,421	-
Balance as on 30 September 2015	6,788,738,880	-	1,746,878,452	35,495,817	382,320,802	293,884,546	292,251,424	9,539,569,921
Balance as on 30 September 2014	4,114,387,200	-	1,466,198,798	114,061,074	392,381,876	499,279,805	264,806,909	6,851,115,662


Chief Financial Officer


Company Secretary


Managing Director


Director


Chairman

Dhaka, 27 October 2015

**Selective Notes to the Financial Statements
For the 3rd Quarter ended 30 September 2015**

01. Basis of Accounting

The financial statements for the 3rd quarter ended 30 September 2015 have been prepared in accordance with Bangladesh Accounting Standard (BAS)-34 "Interim Financial Reporting", Bangladesh Financial Reporting Standard, Income Tax Ordinance 1984, Bangladesh Bank Circulars, the Securities and Exchange Rules 1987 and other laws and rules applicable in Bangladesh.

02. Accounting Policies

In case of preparing these financial statements, the Accounting Policies which have been followed are same as applied in the financial statements of the Bank for preceding period.

03. Cash and Cash Equivalent

As per BRPD circular no. 15 dated November 09, 2009 and BAS-7, cash and cash equivalents include notes and coins in hand, balances lying with ATM, unrestricted balance held with Bangladesh Bank and its agent Bank, balance with other Banks and Financial Institutions, Placement with Banks and other Financial Institutions.

04. Basis of Consolidation

The consolidated financial statements have been prepared in accordance with Bangladesh Accounting Standards 27-"Consolidated & Separate Financial Statements". The Consolidated Financial Statements are prepared for the 3rd quarter ended 30 September 2015.

All intra-group transactions, balances, income and expenses are eliminated at the time of consolidation.

05. Provisions

a) General Investments and Investment in Shares & Securities

Provision for general investment has been made as per directives of Bangladesh Bank issued from time to time. As on 30 September 2015, there is no need to require the provision against investment in shares because as on the date the market value of shares is greater than the cost price.

b) Taxation

Provision for income tax has been made on taxable income after necessary add back in accordance with the provisions of Finance Act 2015, The Income Tax Ordinance 1984 and other relevant legislation as applicable.

06. Depreciation on Property, Plant and Equipment

As required in paragraph 43 of IAS 16-Property Plant and Equipment, depreciation has been charged at the reducing balance method, except on motor vehicles and building on which straight-line method is applied. Depreciation on addition to fixed assets is charged when the asset is available for use and the charge of depreciation is ceased after the asset is sold out/disposed off/fully depreciated.

07. Retirement Benefits of Employees

Required in BAS-19: Employee Benefit, provident fund and gratuity benefits are given to eligible staff of the bank in accordance with the locally registered rules and the entity shall disclose the amount recognized as an expense for defined contribution plan.

08. Others

Figures relating to previous year/period included in this period have been rearranged wherever considered necessary.