

ISLAMIC FINANCE
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Sukuk: Islamic bonds reshaping global finance

Sukuk are Islamic financial certificates similar to conventional bonds, but structured to comply with Sharia (Islamic law).

Since Islamic finance prohibits earning or paying interest, Sukuk provides an alternative way for governments and companies to raise capital without relying on interest-based lending.

Instead of lending money, investors purchase certificates representing partial ownership in a real asset or project.

The funds are used to acquire or develop tangible assets such as roads, buildings, power plants, or other infrastructure, ensuring the investment is tied to real economic activity rather than a purely financial transaction.

Returns to investors come from income generated by these assets, such as lease payments, service fees, or operating revenues, rather than interest.

At maturity, the issuer, typically a government or company, repurchases the certificates at face value, allowing investors to recover their principal.

Dickson Ssembuya, the director of market research and development at the Capital Markets Authority Uganda, notes that about \$4.5 billion exists across Islamic banking, capital markets, and insurance globally, reflecting strong demand for Sharia-compliant products.

He adds that roughly 13 percent of Uganda's population adheres to Islamic principles, meaning conventional financial products may not suit them.

"Existing capital markets exclude this segment, highlighting the need for Sharia-compliant instruments like Sukuk to broaden financial inclusion," he notes.

The growth and mechanics

Since 2000, when the first Sukuk were issued in Malaysia, these Sharia-compliant financial instruments have grown rapidly in popularity.

Malaysia's early success showed that large-scale financing could comply with Islamic law while attracting global investors.

Soon after, Bahrain issued its first Sukuk in 2001, helping expand the mar-



ket beyond Southeast Asia into the Middle East.

Over time, more governments, financial institutions, and corporations adopted Sukuk to raise capital.

Today, both Islamic corporations and state-run institutions issue Sukuk, which account for a growing share of the global fixed-income market, reach-

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Asset performance
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ing about \$1 trillion by the end of 2025 out of a total market valued at over \$145 trillion.

The rise of Sukuk is closely tied to a key principle of Islamic finance: the prohibition of *riba*, or interest.

Under Islamic law, earning money simply by lending funds and charging interest is not permitted.

Because of this, traditional debt instruments such as conventional bonds cannot be used in their usual form by institutions seeking to comply with Sharia principles.

Sukuk were, therefore, developed as an alternative structure that links financing to real economic activity.

Instead of paying interest, the returns and cash flows are tied to a specific asset or project funded by the investment.

The money raised from investors is used to acquire or develop a tangible asset, and investors share in the economic benefits it generates.

For this reason, Sukuk represent undivided ownership shares in a tangible asset connected to a particular project or investment activity. Each certificate gives investors a proportional claim on both the asset and income it produces.

Sukuk and traditional bonds

Sukuk and traditional bonds share similarities but differ in key ways.

Both provide investors with periodic payments and are issued by governments and corporations to raise capital. They are generally considered safer than equities due to more predictable returns and lower volatility.

The main difference is how returns are generated. Sukuk investors earn a share of profits from an underlying asset, while bondholders receive fixed interest payments. Structurally, sukuk represent partial ownership of an asset, whereas bonds are debt owed by the issuer. This means sukuk returns are linked to income from underlying assets, while bonds provide fixed interest payments, though the market value of both instruments can change.

Key takeaways

- Sukuk were, therefore, developed as an alternative structure that links financing to real economic activity.
- Instead of paying interest, the returns and cash flows are tied to a specific asset or project funded by the investment.
- Sukuk investors earn a share of profits from an underlying asset, while bondholders receive fixed interest payments.

Sukuk must also be backed by halal, Sharia-compliant assets, whereas bonds typically involve interest and may fund non-compliant activities.

Valuation differs as well: sukuk depend on asset performance, while bonds are driven by creditworthiness and interest rates.

"They [Sukuk] have principles. They don't believe in interest, they don't believe in speculation," says Ssembuya, because Sharia finance follows core rules.

Interest (*riba*) is prohibited, as returns should come from real economic activity. Speculation (*maysir*) and excessive uncertainty (*gharar*) are avoided to ensure clarity. Investments must be asset-backed, risk-sharing, and ethical.

"That is why," he adds, "conventional products; based on interest and often detached from real assets, do not align with these principles."

Sukuk structures

The most common form of sukuk is issued as a trust certificate. Although these certificates are often governed by Western legal frameworks, the structure behind them is more complex.

To raise funds, the issuing organisation first establishes an offshore Special Purpose Vehicle (SPV).

The SPV then issues trust certificates to investors and uses the proceeds to finance the originating entity through a funding arrangement.

In return, investors receive a share of the profits generated by the underlying asset.

This structure, however, depends on the ability to create an offshore SPV in a jurisdiction that permits trust arrangements, which is not always possible.

When such structures cannot be established, sukuk can instead be arranged under a civil-law framework.