

# The Development of Sovereign Sukuk in Indonesia

Nisful Laila<sup>a\*</sup>, Muslich Anshori<sup>b</sup>, <sup>a,b</sup>Graduate School of Universitas Airlangga, Indonesia <sup>a,b</sup>Faculty of Economics and Business, Universitas Airlangga, Indonesia, Email: <sup>a\*</sup>[nisful.laila@feb.unair.ac.id](mailto:nisful.laila@feb.unair.ac.id)

The purposes of this study are to assess the problems faced by the Indonesian Government in developing sovereign sukuk; to provide alternative solutions and to produce a draft strategy to be applied; and to determine what are the determinants in developing sovereign sukuk. The method used is an Analytic Network Process (ANP), which has advantages to measure and synthesise a number of factors in hierarchy or network. The initial phase of this study is to conduct a literature survey and in-depth interviews with stakeholders, including academicians, practitioners, regulators, and associations, to fully understand the problem. This is followed by creating an ANP model, filling questionnaires by expert respondents, data processing by ANP super decision software, and then performing a results analysis.

We conclude that the three most important problems to be solved are related to government commitment (15.5 per cent), adequate transaction infrastructure (10.3 per cent), and adequacy of regulation (9.6 per cent). The three most important solutions that should be the attention of policy makers are the importance of increasing government commitment (12.8 per cent), easiness of transaction (11.1 per cent), and regulatory revision (10.9 per cent). The three most important strategies that need to be implemented soon are making the roadmap of Islamic financial development, in addition to providing infrastructure by the government (11.2 per cent), the importance of supervision in regulatory implementation (11.1 per cent), and the importance of optimising the government's role in asset identification and tax incentive and competitive sukuk pricing in sovereign sukuk trade (8.6 per cent).

**Key words:** *Sovereign sukuk development, sovereign sukuk, Analytical Network Process (ANP).*

## Introduction

Sukuk is defined as a certificate presenting an indispensable proof of ownership of a tangible asset, the value of benefits, services or asset ownership of a particular project or investment activity. Unlike the financial instruments in general, sukuk comply with the principles of sharia, which means that sukuk does not have any things that are prohibited in Islamic law such as *riba* (interest), *gharar* (uncertainty), *maysir* (speculation) and *haram*. Sukuk must fulfill according to the Shariah and real assets-based transactions.

The development of sukuk globally shows that more and more countries are contributing to issuing sukuk. From 2001 to December 2016, there have been 29 countries that publish global sukuk and most of them are countries with a majority Muslim population. The highest sukuk country is Malaysia at 55 per cent, followed by Saudi Arabia and the United Arab Emirates (UAE) which has a 14 per cent and nine per cent issuance of sukuk from the existing global sukuk. New on the fourth order, Indonesia reached 8, 1 per cent, followed by Qatar, Turkey and Sudan. The issuance of sukuk in the Yuan Chinese currency, Turkish Lira and Singapore Dollar and British Pound sterling, is a new development that brings optimism about the development of sukuk in the future.

From the above description, Indonesia — with the largest Muslim population in the world — only ranks fourth in the percentage of sukuk issuance (8, 1 per cent), which is far behind Malaysia (55 per cent). This certainly raises the question, why the development of sukuk in Indonesia cannot be more rapid again as has occurred in the neighbouring country of Malaysia?

In terms of demand, Sukuk Negara is in great demand from investors. Since it was first launched, the Sukuk Negara recorded a record of potential investors who are far above the amount of sukuk to be issued by the government. This means the public sees the State Sukuk as a lucrative investment alternative, while the risks contained in the Sukuk Negara can be said to be zero. This is because the State Sukuk is issued by the Indonesian Government, and fully guaranteed by the government, the State Sukuk belongs to a *risk-free investment* instrument.

As sovereign, when the government increases emissions of sukuk, it will provide benefits for the people of Indonesia kar ena increasing alternative sources of funding in the Budget Penda ents and Expenditure (APBN), m enurunnya portion of the source of funds from the issuance of obligation or public debt, m Enhancing independence of the nation, encouraging the growth of Islamic euangan kthoroughly, even the most important are eni n m obtained gkatnya blessing Indonesian people for using those resources that are free of usury, as Allah says in Surat al-Araf: 96.

By the end of 2017, the issuance of sukuk as a source of national development funding experienced significant improvements, amounting to Rp 11 trillion in 2013 and rising to Rp 16.7 trillion in 2017. However, when compared to the size of the state budget, sukuk issuance in the country is still very small, with a maximum of only eight per cent. On the other hand, Indonesia's debt in 2017 reached Rp 3,600 trillion. If the State Sukuk upgraded its emission, then the State will be greatly helped. It can be said that the issuance of sukuk is a form of financial independence of the State, because the people of Indonesia who buy the State Sukuk, especially retail sukuk, is as a form of direct participation in society on national development. The issuance of the State Sukuk can also be said to be a form of mutual cooperation among Indonesians to participate in financing state projects. When compared to the government's efforts to get the source of funds from debt to third parties, then of course loaded with the political interests of donor countries, the development of the State Sukuk becomes an alternative source of potential and strategic funding for the sustainability of national development.

Various studies on sukuk have been done, including Hafiduddin (2007), who examines the possibility of using sukuk for financing in agriculture. Ascarya (2009) also wrote about the comparison of sukuk developments in Malaysia and Indonesia. On the other hand, Rusjdiana (2010) has also been researching the issues surrounding corporate sukuk in Indonesia, while Musari (2012) examines the State Sukuk and the welfare of a nation.

Although there has been a lot of research on sukuk, there is no deep and comprehensive research to answer why sukuk in Indonesia, especially Sukuk Negara, has a relatively small growth compared to sukuk in other Muslim majority countries. Given the magnitude of the role of sukuk in a country's economy, it is very important to conduct the research in question.

### ***Basic Concepts of Investment in Islam***

In various economic literature, the term of investment refers to the notion of delaying current consumption for use in efficient production over a given period (Jogiyanto, 1998: 5). Meanwhile, Sharpe (1995: 1) states that investment means sacrificing dollars now for more dollars in the future. From the definition of these investments, the implied three elements on investment activity are the sacrifice of resources, the uncertainty, and the results or the expected returns in the future. Investments are also interpreted as delivering funds for a specified period and providing returns to invest or as a reward for time sacrificed, after accounting for factors about the inflation rate and the risks inherent in the investment (Shamsudin Ismail 1992: 728). Adiwarman Karim (2001: 21) explains that investment in Islam is to distinguish between money and capital. In Islam, money is a flow concept whereas in conventional investment, it is a stock concept. In the economy, the more money spins, the better the rate of economic growth. In this case, Islam forbids the

accumulation of money to establish the concept of al-qard and alms that can accelerate the circulation of money. According to Me nurut Huda (2008: 18), the concept of an investment is nuanced and spiritual knowledge for using the norms of sharia, as well as the essence of a science and charity, therefore the investment is highly recommended for every Muslim.

### ***Sovereign Sukuk***

Based on the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI), sukuk is a certificate of equal value representing a share of ownership entirely to tangible assets, benefits and services or ownership of assets of a particular project or investment activity. The most obvious sukuk and obligation comparison is its compliance with sharia, both its contract and its use of funds, in addition to the necessity of underlying asset, which in the second bond does not necessarily exist because the sukuk definition is a proof of ownership of an asset while the bond is a debt. Several types of sukuk have been issued by both government and private companies.

Sukuk are divided into two types, namely as collateral assets or as business investment. As collateral assets or asset sukuk, the asset is usually designed in the scheme of a sale and purchase agreement by using murabahah (general buying), Istisna (buying and selling by order first) and greetings (buy and sell with advance order and payment paid in advance of contract), or lease agreement scheme with an Ijarah contract (lease on an asset). Whereas, if the sukuk is a business investment, it can use a mudaraba contract (a partnership in which one party deposits 100 per cent of the funds, the other provides 100 per cent of the skill) or musyarakah (each party deposits a certain amount of capital and skill in agreed percentage).

Sukuk as an Islamic financing instrument is a very important product for producers and investors, both state and private. For the country, sukuk is used as a financing tool for mobilising capital, a means to foster the participation of private parties in financing public interest projects, becoming instruments for fostering domestic and inter-national investment, and fiscal decentralisation.

Based on the issuing institution, the sukuk is divided into two; the sukuk corporates, namely sukuk issued by private companies, as well as sukuk issued by government agencies (Sovereign Sukuk). In Indonesia sovereign sukuk is called State Sukuk which is Government Shariah Securities (SBSN) issued based on sharia principles as proof of the share of state assets, both in the currency of Rupiah and foreign currency. According to Hadiningdyah (2014), there are several important meanings of the State Sukuk. First, Sukuk Negara as diversified funding sources, which means that Sukuk provides an alternative source of funds for the government. If the source of funds is far more derived from debt, then

the government can get the source of funds from the public investors but not based on debt and comply with sharia. Secondly, the State Sukuk as a tool in liquidity management. With the issuance of the State Sukuk, Islamic banks have the freedom to choose financial instruments to maintain their liquidity. Furthermore, Sukuk Negara is also very useful in providing choices for the investor community to obtain safe investment products and in accordance with sharia. Finally, the State Sukuk is useful in terms of financing infrastructure projects being undertaken by the government.

## **Research Method**

Based on the formulation of the proposed problem, this research is aimed to elaborate the problems in the development of State Sukuk, as well as to find the right solutions and implementation strategies based on the opinions of experts and stakeholders. This research uses a qualitative research approach which has the characteristics of research that prioritises non-positivistic paradigms, and inductive and constructive approaches to the meaning of the facts and not just objectively measuring the facts. A qualitative approach is chosen because it has advantages to answer the problems in this study which cannot be done with quantitative measurements, and needs to involve the related aspects. To answer the problem formulation that exists in this research, collecting and analysing data was performed using an Analytic Network Process (ANP). The data research was obtained by conducting in-depth interviews with stakeholders, including regulators, managers of associations, academics and practitioners, who have an understanding of the issues discussed. From the informant's assessment data to the problem that became the object of research, then becomes the object of research in a numerical scale. The numerical scale is a scale of one to nine to indicate whether the respondent agrees or disagrees with a statement.

The selection of informants in this study was conducted by considering the understanding of informants on the problems in the development of State Sukuk in Indonesia. The number of informants in this study consisted of twelve people, with the consideration that they have expertise related to the State Sukuk. The twelve informants are dikelompokkan in four groups, namely: 1) regulator; in this case, is the ministry of finance, especially the directorate of debt management of the country; 2) a scholar or sukuk expert who has a track record of research and a good understanding of sukuk and existing problems related to sukuk; 3) An association; informants who are actively involved in associations related to Islamic finance, especially the State Sukuk, and consisting of the Association of Islamic Economic Society (MES); and 4) praktisi; the informants who in their daily work use sukuk in its investment portfolio.

## **Results and Discussion**

Overall, the ANP results show a majority of respondents (associations, regulators, practitioners) agree that in terms of problems, issuers (31.2 per cent) are the most important issue in sukuk development, followed by legal (23.9 per cent), where most academics contribute in summarising that legal problems are the main problem faced in the development of the sukuk. Meanwhile, equally important is the market problem (23.8 per cent), which occupies the third priority, although according to the views of each category of respondents, they still disagree on the order of priority. Similar to market problems, the problem faced by investors (21.1 per cent) is also a problem that occupies the last priority in the overall development of sukuk.

### ***Cluster Solution Priority***

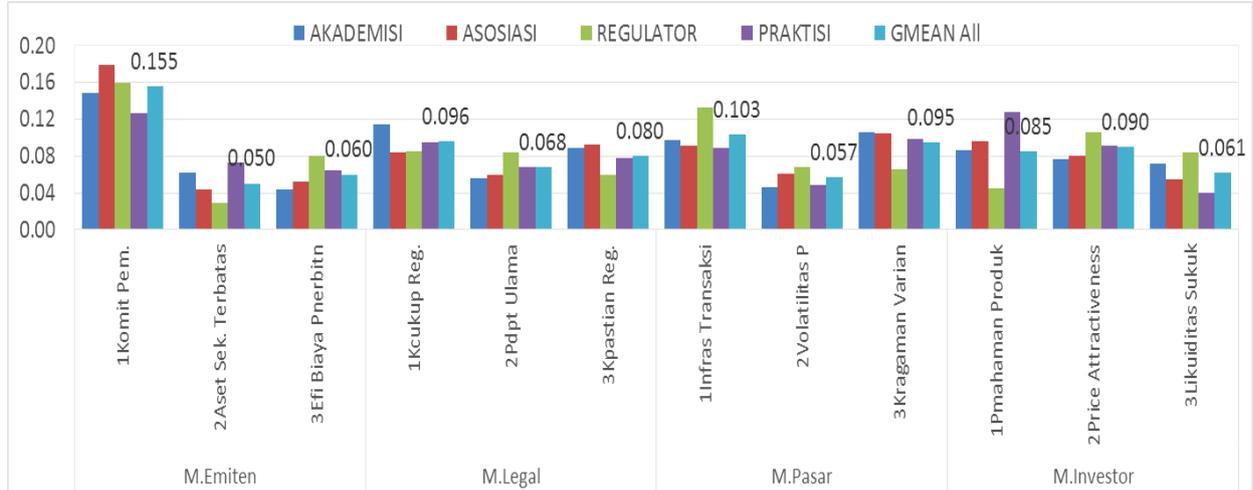
In line with the overall ANP results in assessing the problems faced in the development of sukuk, it shows that most respondents (associations, regulators, practitioners) agree that from the solution side, the issuer (32.3 per cent) is the main solution to deal with sukuk development issues, especially in tackling the problem arising from the issuer's side. This is followed by the legal solution (28.4 per cent), where the academics group contributed most in concluding that the legal solution is the main solution that must be performed to develop sukuk. Meanwhile, equally important is the market solution (23.3 per cent) that occupies the third priority, although according to the views of each category of respondents, they still disagree on the order of priority. Similar to the market solution, the solution that must be done immediately is the solution from the investor side (16 per cent).

### ***Cluster Strategy Priority***

In line with the overall ANP results in assessing the problems faced and the proposed solutions in the development of sukuk, it showed that most respondents (associations, regulators, practitioners) agree that from the aspect of strategy, issuers (37.9 per cent) are the main strategy in sukuk development, especially in tackling problems arising from the issuer's side and the strengthening of policy solutions to be implemented. In contrast to the priority outcomes of problems and solutions, a more important strategy is market strategy (23.1 per cent), according to the views of the associations, regulators, and practitioners. This was followed by legal strategy (21.9 per cent), and lastly, the strategy of the investor (17.1 per cent).

**Priority Detail Issues**

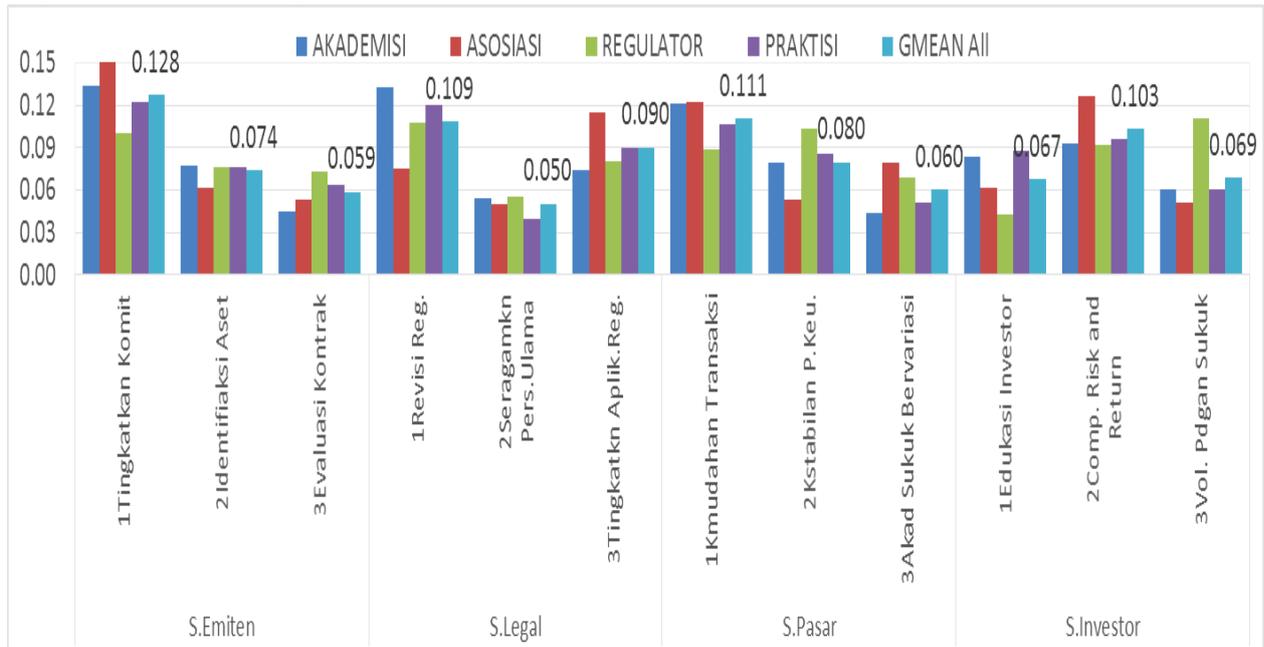
**Figure 1.** ANP Results Priority Detail Issue



In detail, the ANP results indicate that all respondents (academics, associations, regulators, practitioners) agree that the most important issue is government commitment (15.5 per cent), followed by the transaction infrastructure (10.3 per cent), and the third priority in whole said that the adequacy of regulation (9.6 per cent) is also a major problem encountered in the development of sukuk.

**Priority Detail Solutions**

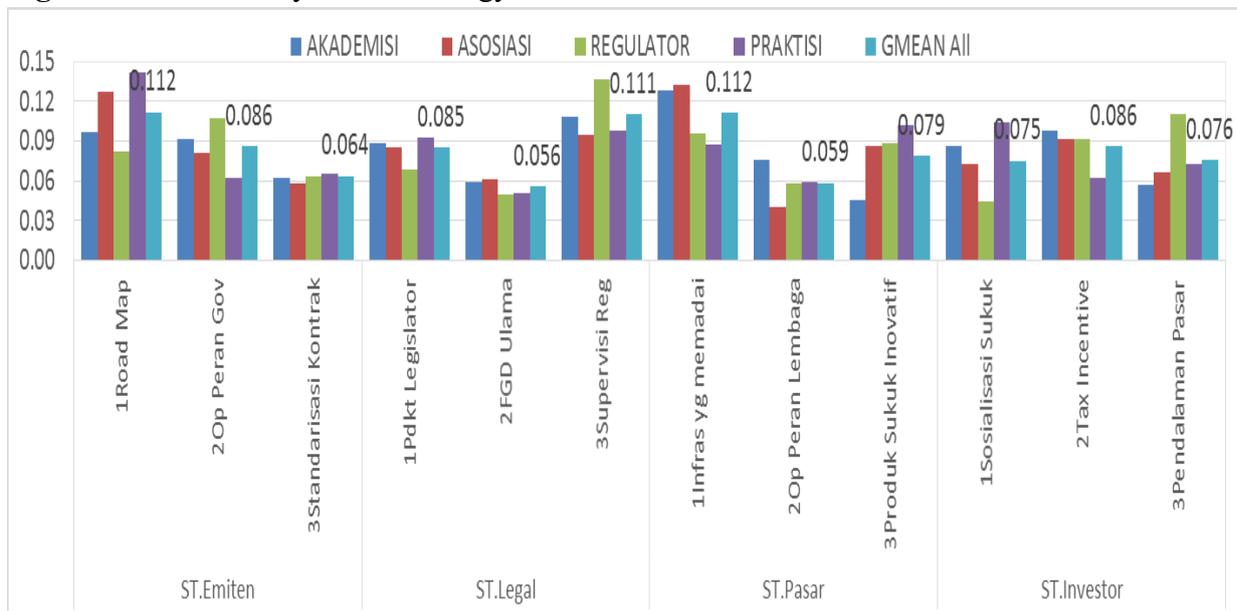
**Figure 2.** ANP Priority Detail Solution Results



In terms of the proposed solutions, the ANP results indicate that all respondents (academics, associations, regulators, practitioners) agree that the most important solution that should be immediately undertaken is to increase government commitment (12.8 per cent). This is in line with the problems encountered. This is followed by the convenience of the transaction (11.1 per cent), and the third priority in whole said that the regulatory revision (10.9 per cent) is also the main solution that should be completed by the regulator in sukuk development.

### Priority Detail Strategy

**Figure 3.** ANP Priority Detail Strategy Results



From the proposed strategy side, the ANP results indicate that all respondents (academics, associations, regulators, practitioners) agree that the most important strategy that must be undertaken is to make a road map and provide adequate infrastructure (11.2 per cent). This is in line with the problems encountered. It is followed by regulatory supervision (11.1 per cent) and the third priority in whole said that the optimisation of the government's role and a tax incentive (8.6 per cent) will also stimulate the development of the national sukuk.

### Conclusion and Recommendation

The most influential factor in developing the State Sukuk is divided into three groups: problem groups, solutions groups and strategy groups. Three of the most important issues to be resolved are the government's commitment (15.5 per cent), inadequate infrastructure transactions (10.3 per cent), and the adequacy of regulation (9.6 per cent). The three most important solutions that should be the attention of policy makers are the importance of increasing government commitment (12.8 per cent), ease of transaction (11.1



per cent), and regulatory revision (10.9 per cent). The three most important strategies that need to be implemented soon are making a road map of Islamic finance development, in addition to providing adequate infrastructure by the government (11.2 per cent). This is followed by the importance of supervision of regulatory implementation (11.1 per cent) and the importance of optimising the role of government and the existence of tax incentives in the trade of State Sukuk (8.6 per cent). The recommendations are as follows: 1) Certainty of taxation through revised regulation and tax incentive must be done immediately. A minimum amount of tax on sukuk is equal to bond, so sukuk and bond can compete equally in the capital market. 2) The role of government in supporting the development of State Sukuk can be optimised further by doing certain project-based financing or covering the budget deficit with a State Sukuk instrument.



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