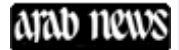


Structured Trade Finance Fund ought to be a major asset class

The logo for Arab News, consisting of the words "arab news" in a white, lowercase, sans-serif font inside a black rectangular box.

04 January 2010

The imminent launch in early 2010 of the Shariah-compliant Structured Trade Finance Fund by Gatehouse Bank PLC, the latest wholesale Islamic bank authorized by the UK's Financial Services Authority (FSA), and DDCAP Limited, the London-based wholesale Islamic market intermediary company, will see a welcome return to a classical bread-and-butter asset class and financing activity, which the Islamic finance industry seems to have neglected over the last few years.

The industry, according to seasoned Islamic bankers, has become pre-occupied with the more lucrative sukuk (Islamic bond) market and the "bricks-and-mortar" real estate market over the last few years, especially in the Gulf Cooperation Council (GCC) countries. They stress that trade finance ought to be a major asset class in the global Islamic finance industry for several reasons.

Trade finance, they point out, supports real trading activity through financing imports and exports, and therefore the real economy. The financing is backed by real assets such as receivables whether commodities, equipment and machinery. These can be used as part of an asset pool which can be securitized in the case of a sukuk issuance. The Islamic Development Bank (IDB), for instance, in its latest \$850 million sukuk under its \$1.5 billion MTN Program, used a pool of underlying assets which comprised Ijara (leasing) assets, Murabaha receivables, Istisna receivables and the IDB's own portfolio of equity and sukuk investments.

Trade finance could also be an ideal way of stimulating the elusive goal of increasing intra-Islamic trade, which currently stands at about 14 percent of the total trade of the 56 member countries of the IDB. The IDB has disbursed \$34.8 billion in trade finance for the period 1996 to 2008 financing the imports and exports of member countries, primarily through installment sales, Murabaha (cost-plus financing) and lines of financing.

In some markets such as Turkey, trade finance forms a major part of the financing portfolios of the Islamic banking industry. Indeed, letters of credit (LCs) and guarantees are in fact confirmed through counterparties in Bahrain for the above transactions which run into millions of dollars a year. There have been a number of trade funds established over the years, especially by National Commercial Bank of Saudi Arabia, whose Al-Ahli Global Trading Fund has been perhaps the largest and also by institutions such as Al-Rajhi Bank. But they have been consumed by the glamor of mutual, private equity and real estate funds, and more recently by the odd sukuk fund.

Several Islamic bankers rue the fact that many Islamic financial institutions are neglecting trade finance in order to pursue other types of transactions -- private equity, asset management, real estate etc. This despite the fact that these banks often lack the expertise in these areas and usually source in whole teams to run

these departments only to find out down the line that the exercise was a waste of time and resources because the team are not necessarily familiar with Islamic financing structures or the deal flows are limited.

Gatehouse Bank and DDCAP, not surprisingly, stress that the Structured Trade Finance Fund will invest capital in structured trade finance transactions in order to inject new flows of capital into the global marketplace. Currently, as a result of the credit crisis, many Western banks operating in this sector are restricted in their trade finance activities and the creation of an Islamic fund to service this sector would have worldwide benefits, providing liquidity to a market that has been seriously constrained. According to the promoters, the Structured Trade Finance Fund is deliberately designed as a clear-cut and accessible approach to financing, facilitating the natural flow of business and kick-starting credit flow in the real economy. Global in outlook, the fund will be weighted toward the Organization of Islamic Conference (OIC) economies.

"Given the liquidity challenges that many banks are experiencing," explained Richard Thomas, CEO of Gatehouse Bank, "the Shariah-compliant Structured Trade Finance Fund has been launched at a time that will help alleviate the lack of capital available for transactions. This back-to-basics approach will have benefits for international trade and will continue to do so as the economic situation improves. The Islamic finance model promotes accessible, low risk investments whilst achieving good returns, benefiting every stakeholder. We are firmly of the belief that it is both good business and totally in accordance with the principles of Shariah to encourage the real economy through international trade."

The Structured Trade Finance Fund, according to the promoters, also provides an attractive alternative to traditional asset classes, having no direct correlation to equity markets or macro-economic cycles. Instead, it is very much focused on commodities. The fund is open-ended and domiciled in Cayman Islands and will support the activities of the traditional trade finance banks and other trade finance funds, as well as originating its own business.

By bringing an Islamic solution and operating with Islamic financing structures, the transactional risks will be further reduced and an exemplary template for providing funds to support trade and commerce in the future will be created. The fund structure is such that it is an ideal way for the Islamic Investors to enter into this market. "The Shariah-compliant Structured Trade Finance Fund," explained Stella Cox, managing director, DDCAP Limited, "provides an uncomplicated, ideal way to become a major player in the Trade and commodity finance sector, with a wide range of available transaction types. Combined with Gatehouse Bank, we have the right expertise and experience to manage this fund and, using the principles of Islamic finance, it will experience low levels of volatility and drive attractive, stable returns for participants."

The launch of the fund comes as Gatehouse Bank continues to prove Islamic finance as a more accessible and widely used method of finance internationally. Gatehouse Bank recently transacted the first cross border trade with CIMB Islamic Bank of Malaysia on the Bursa Suq Al-Sila' commodity trading platform, an end-to-end Shariah-compliant commodity trading platform facilitating commodity-based Islamic financing under Shariah principles launched by Bursa Malaysia, the national stock exchange.

By Mushtak Parker

© Arab News 2010

Article originally published by [Arab News](#) 04-Jan-10