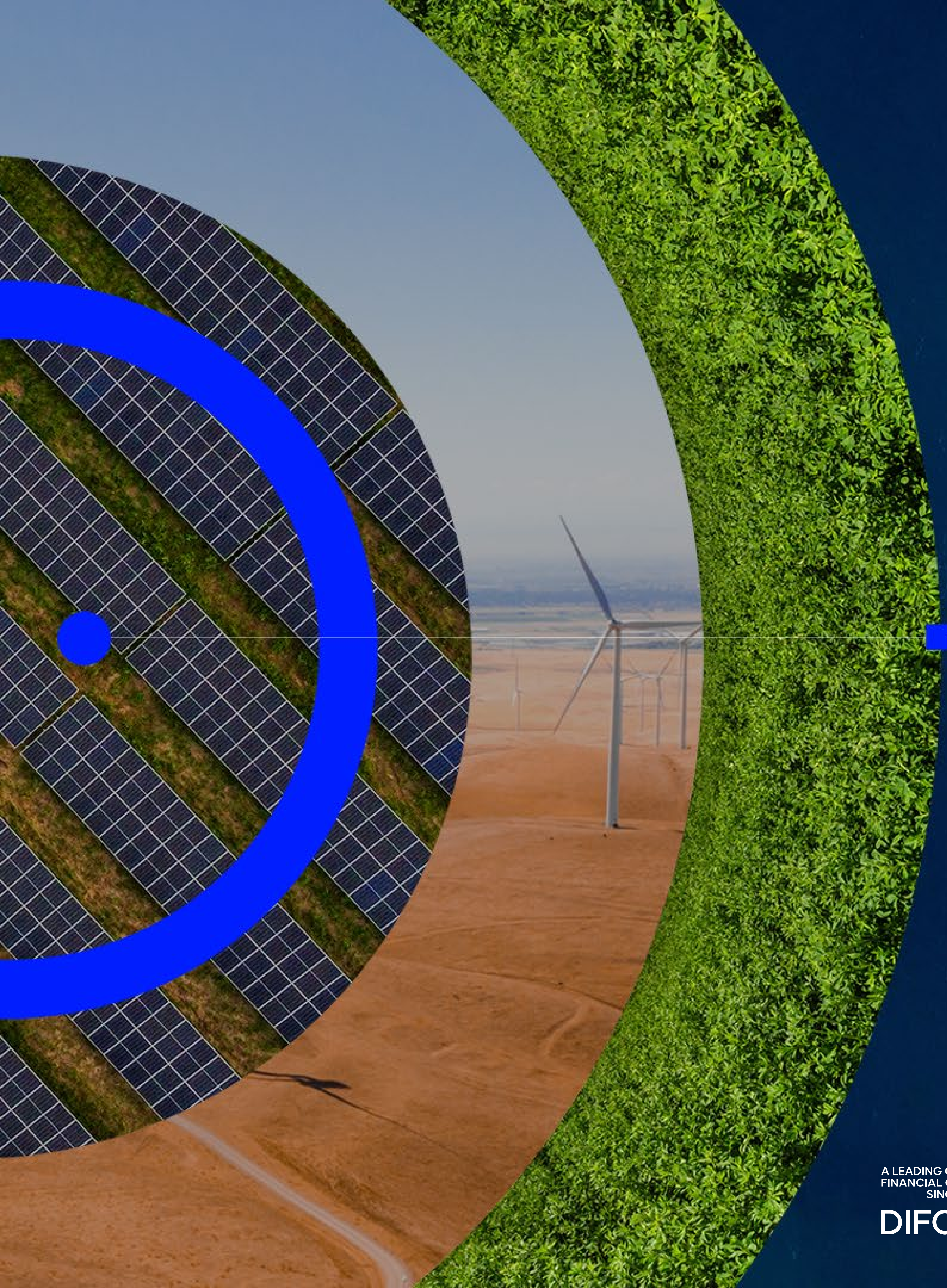

#GreenSukuk2024

GREEN AND SUSTAINABILITY
SUKUK UPDATE 2024

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ACKNOWLEDGEMENT

We acknowledge the valuable contribution of members of the High-Level Working Group on Green and Sustainability Sukuk (HLWG) towards drafting the “Green and Sustainability Sukuk Update 2024”. The HLWG’s members, led by Shrey Kohli from London Stock Exchange, supported us in providing valuable market insights and extensive advice on multiple drafts of the report.

ABOUT THE REPORT

The report is a collaboration between London Stock Exchange Group (LSEG), the Islamic Finance Council UK (UKIFC) and the Global Ethical Finance Initiative (GEFI) as one of the outcomes of the HLWG in its third and final year.

ABOUT THE GLOBAL ISLAMIC FINANCE AND UN SDGS TASKFORCE

The Global Islamic Finance and UN SDGs Taskforce was a collaboration between the public and private sectors to raise awareness of the role Islamic finance can play in achieving the United Nations Sustainable Development Goals (SDGs).

With assets estimated to be over $4.9 trillion, Islamic finance is one of the fastest growing sectors in the global financial industry. Achieving the 17 SDGs, as outlined in the UN’s 2030 Agenda for Sustainable Development, has been estimated to require over US$5 trillion per year of investment, with the financing gap standing at around $2.5 trillion per year.

To achieve a better and more sustainable future, addressing issues such as climate change and equality, and unlocking the necessary finance to do this, will require a coordinated global effort.

Despite a natural synergy between many principles of the Maqasid al Shariah and SDGs, however, analysis conducted by UKIFC has highlighted a distinct lack of engagement across the global Islamic finance sector.

The Taskforce, launched in 2020 by the UKIFC and UK Government, brought together over 200 Islamic finance institutions and industry stakeholders from across the globe to better understand and address the challenges and opportunities presented to the sector by the SDGs.

The Taskforce examined the potential contribution of the Islamic finance sector to closing the SDGs funding gap whilst enhancing its commercial success and addressing the climate-related nationally determined contributions (NDCs).

The HLWG was one of the Taskforce’s four core workstreams.

ABOUT THE HIGH-LEVEL WORKING GROUP ON GREEN AND SUSTAINABILITY SUKUK

The UN Climate Change Conference of the Parties (COP) gathers global leaders each year to to progress the aims the efforts of the Paris Agreement and the UNFCCC. COP26, held in Glasgow in 2021, marked six years since the signing of the Paris Agreement, a legally binding climate treaty aimed at keeping the global temperature rise below 2°C, preferably under 1.5°C. COP26 presented an opportunity for the Global Islamic Finance and UN SDGs Taskforce to announce a pioneering initiative on green and sustainability sukuk.

Central to the Paris Agreement are the NDCs, which detail each country’s plans to cut emissions and adapt to climate impacts. However, funding remains a major hurdle, especially for adaptation projects, which could cost developing countries $140 billion-$300 billion annually by 2030 and potentially $500 billion by 2050.

Islamic finance, particularly through instruments like green and sustainability sukuk, offers a promising funding source, especially for the Organisation of Islamic Cooperation (OIC) states, which cover 24% of the global population. By leveraging sukuk, countries like Indonesia are growing their Shariah-compliant debt markets to fund climate initiatives. The UKIFC projects that green sukuk could raise $30 billion-$50 billion towards SDGs by 2025.

Supported by the Islamic Development Bank, the UK and Indonesian governments, and key partners including LSEG, Emirates NBD, the UKIFC and GEFI, launched the HLWG at COP26 in Glasgow in December 2021.

"As a pioneer in the issuance of international green sukuk, the Ministry of Finance of Indonesia is honoured to be able to work together with Her Majesty's Treasury, the UK Islamic Finance Council, the Islamic Development Bank, the London Stock Exchange Group and the Global Ethical Finance Initiative to further develop green sukuk market. The initiative aims to promote green sukuk as an alternative financing instrument, which combines two principles that are very much aligned, to a wider audience globally, and enabling issuers not to only tap skuk investors but also Socially Responsible Investment (SRI) investors across the world. ***Sri Mulyani Indrawati, Minister of Finance, Republic of, Indonesia (2021)***

"The launch of the High-Level Working Group on Green Sukuk is a significant milestone for the development of Islamic finance and sustainable finance globally. I am delighted that LSEG is a founding member to help scale green sukuk through our markets and data, allowing companies to access finance in a manner consistent with their faith and values. Green sukuk are strongly linked to assets in the growing green economy and can help mobilise the capital needed to fund the U.N. Sustainable Development Goals. ***Julia Hoggett, Chief Executive, London Stock Exchange (2021)***

Over a three-year period, the HLWG sought to foster international collaboration in promoting green and sustainability sukuk as a key financing tool to attract capital for environmental projects that help countries achieve the NDCs and broader SDGs. Its key objectives included:

1. Promoting sukuk at COP: Ensuring green and sustainability sukuk is featured at each COP summit until 2024, boosting awareness and issuance among corporates, governments, and multilateral oganisations.

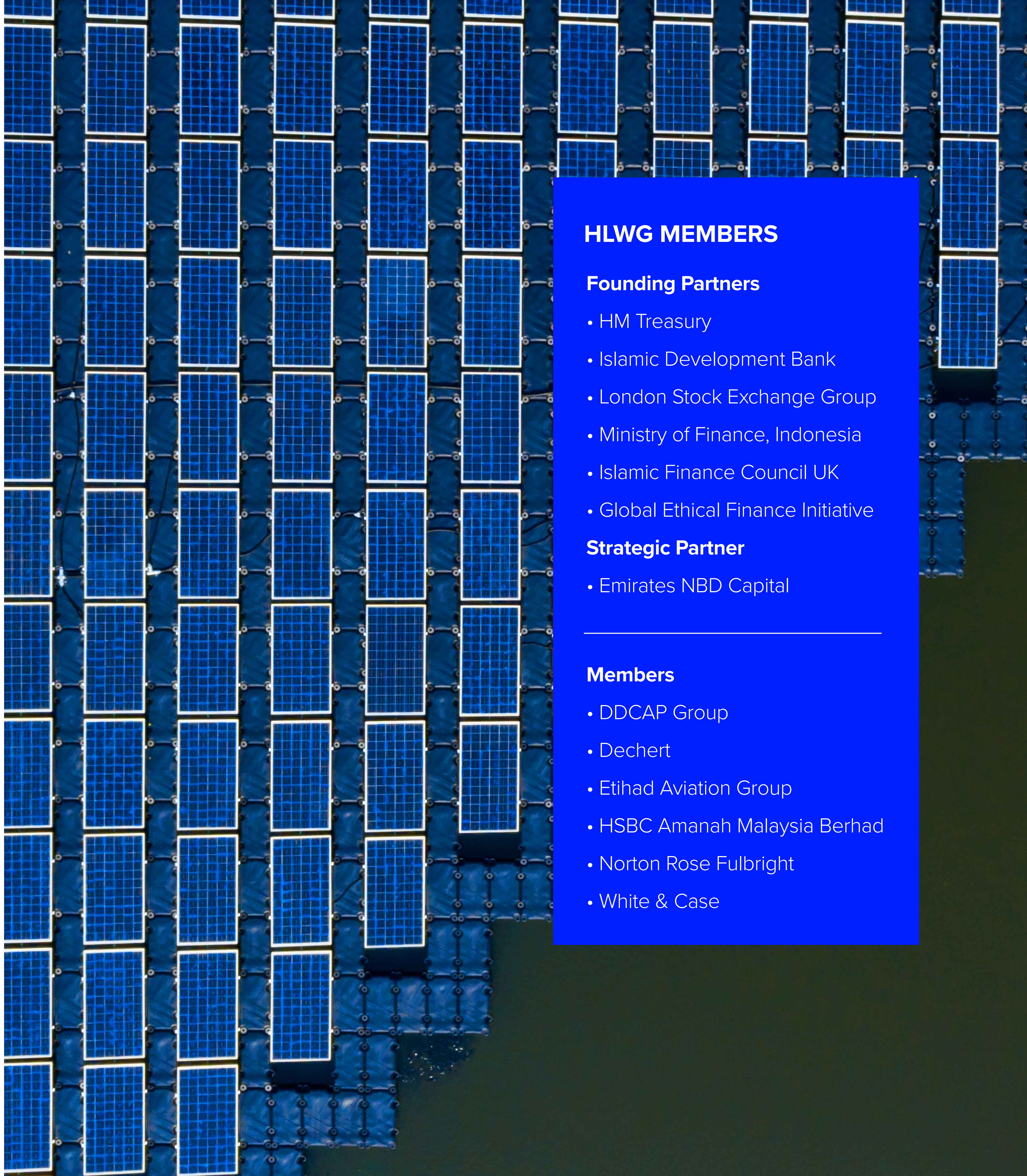
2. Aligning Islamic finance with global standards: Supporting global regulatory bodies (e.g., UN, IsDB) in integrating Islamic finance with sustainability-focused financial frameworks.

3. Addressing market challenges: Tackling specific barriers in green and sustainability sukuk supply and demand.

ABOUT FINANCING A SUSTAINABLE FUTURE REPORT

The HLWG issued its first report, titled "Financing a Sustainable Future", during COP27 in Egypt in November 2022. As well as providing insights on the green and sustainability sukuk market, highlighting transactions and regulatory developments, and providing views from key industry stakeholders, the report proposed a roadmap outlining key recommendations to facilitate the development of the green and sustainability sukuk ecosystem globally.

The recommendations, which included promoting common regional and international standards, developing capacity with issuers, and expanding the wider ecosystem, formed the basis of the HLWG workplan. The HLWG held over 30 meetings, including bilateral and focus groups, to progress these recommendations, with further details included in the final section of this report.



HLWG MEMBERS

Founding Partners

- HM Treasury
- Islamic Development Bank
- London Stock Exchange Group
- Ministry of Finance, Indonesia
- Islamic Finance Council UK
- Global Ethical Finance Initiative

Strategic Partner

- Emirates NBD Capital

Members

- DDCAP Group
- Dechert
- Etihad Aviation Group
- HSBC Amanah Malaysia Berhad
- Norton Rose Fulbright
- White & Case

Contents

Foreword

As the HLWG draws to a close, issuance of green and sustainability sukuk is set to reach yet another record high in 2024, nearing our goal to triple the size of annual issuance by the end of its three-year term. This underscores the growing importance and acceptance of these instruments in financial markets, and paves the way for more innovative and impactful investment opportunities.

This year has seen active primary debt markets, and issuance till the third quarter marked the strongest year on-record since 2020. Following that trend, ESG bond issuance has also seen an increase and is expected to reach $1 trillion by the end of 2024. This is being driven by a number of factors, including increasing adoption of sustainable taxonomies and transparency initiatives, a rise in issuance from emerging markets, and increased efforts to accelerate the energy transition. Resilient demand from investors for sustainable investments and supportive climate policies are also playing an important part. However, short-term growth is likely to remain moderate as macroeconomic uncertainty and other external factors continue to linger in the primary market.

Against the backdrop of COP28, hosted by the UAE in December 2023, sustainable finance has emerged as a key focus across several GCC markets, driven by diversification plans and substantial demand for ESG investments across developed markets. This trend is reshaping the financial landscape, and aligning regional strategies with global sustainability goals.

The HLWG completes its third and final year of operation, culminating in COP29 in Azerbaijan in November 2024. Throughout this period, we have focused on coordinating international efforts to develop and position green and sustainability sukuk as viable financial instruments. Our aim has been to direct investments into green and sustainable projects, thereby unlocking potential Islamic investments to facilitate the UN Sustainable Development Goals (SDGs).

The introduction in 2024 of International Capital Market Association (ICMA) Guidance on Green, Social, and Sustainability Sukuk was a significant milestone for the HLWG and the Islamic finance industry more broadly. Developed in collaboration with LSEG and the IsDB, this guidance provides a comprehensive overview for issuing green and sustainability sukuk, aligning them with international standards and promoting transparency and accountability. It has been well received by various stakeholders, including major financial institutions and regulatory bodies. We expect this guidance to facilitate the growth of the green and sustainability sukuk market and attract a broader range of investors interested in sustainable and ethical investments.

We hope this report, published during COP29, will continue to encourage countries to adopt green and sustainability sukuk as an innovative approach for financing their SDGs and sustainable development plans. This update includes the latest statistics and insights on green and sustainability sukuk, highlights from the roadmap we proposed in the 2022 report, and profiles of some of this year's notable issuances.

We would like to sincerely thank the members of the HLWG for the generosity with their time, experience and expertise during the course of the last three years. We have accomplished much, as shown in this – our final report – and have seen our recommendations resonate and drive collaboration within the industry. We will continue to work with our partners to enhance the awareness of sukuk as an asset class and accelerate progress towards climate and sustainability goals worldwide.

Shrey Kohli
Head of Debt Capital Markets
London Stock Exchange
Chair, High-Level Working Group on Green and Sustainability Sukuk

Mustafa Adil
Head of Islamic Finance
London Stock Exchange Group

Omar Shaikh
Advisory Board Member & Director, Islamic Finance Council UK (UKIFC)
Secretariat, High-Level Working Group on Green Sukuk

Executive summary

Green and sustainability sukuk poised for another record year, despite tempered growth

Global ESG bond issuance reached $745.8 billion in the first nine months of 2024, a 3.2% increase from the same period in 2023. The rise was relatively moderate, however, after a decline in ESG bond issuances that had begun in 2022 continued through 2023 due to volatile market conditions, including inflationary pressures, rising interest rates, and geopolitical tensions.

In contrast, while growth in the overall ESG bond market has been modest in 2024, green and sustainability sukuk are set for another record year with double-digit growth. Issuance of these sukuk reached $11.9 billion in the first nine months of 2024, up 18% from the same period in 2023. They accounted for 1.6% of total ESG bond issuance and 6.4% of total sukuk issuance.

After last year's rebound in green sukuk issuance, which made up 58% of the global value of green and sustainability sukuk, sustainability sukuk regained momentum in the first nine months of 2024. The trend suggests that the surge in green sukuk last year was significantly influenced by the hosting of COP28 in the UAE.

Accelerating momentum in GCC issuance, supported by expansion into new markets

Indonesia, Saudi Arabia, and the UAE led green and sustainability sukuk issuance in the first nine months of 2024, with Saudi Arabia and the UAE together contributing 26% of the total. The GCC region has become a significant driver of market growth, accounting for 58% of issuance in 2024 and 38% cumulatively since the market's inception.

This growth is being fuelled by the region's commitment to sustainability and by rising investor demand for ESG-compliant instruments. The market has also expanded into new countries, including Qatar and Kuwait, as more GCC corporates entered the market following COP28.

Green and sustainability sukuk have predominantly been issued in international markets, with an annual average of 70% issued in foreign currencies since 2019. In comparison, international issuances of traditional sukuk averaged 40% of annual issuance during the same period.

Financial institutions driving growth in green and sustainability sukuk issuance

Corporate issuers have become more active in the green and sustainability sukuk market, accounting for 64% of the value issued in the first nine months of 2024, up from 55% in 2023. This growth is being driven by Saudi issuers and new entries from Qatar and Kuwait.

Financial institutions are leading the market, contributing 56% of the total value, with GCC-based banks issuing some of the largest sukuk. Most proceeds are directed towards climate change adaptation and essential services.

Sovereign green and sustainability sukuk, all issued by Indonesia, made up 27% of the total. Indonesia has issued several green sukuk since 2018, raising $12.6 billion in all for climate change adaptation.

ESG mandates spurring higher demand for green and sustainability sukuk

Demand for green and sustainability sukuk is higher than for traditional sukuk, as they attract a new group of investors that prioritise ESG credentials over Shariah compliance. LSEG's 2024 ESG Sukuk Survey found that 83% of fixed-income underwriters and advisers reported a moderate increase in demand over the past two years, with 50% expecting significant growth in the next two years.

Green and sustainability sukuk were subscribed at 4.3 times their issuance values on average in the first nine months of 2024, compared to 3.1 times for traditional sukuk. The higher demand is mainly being driven by European investors. The survey revealed that the leading reasons for investing in these sukuk are Shariah compliance and to fulfil ESG mandates.

The survey found that more than 45% of respondents identified limited green and sustainability sukuk offerings as the biggest challenge to investing in this market. Additionally, more than 70% of respondents emphasised the high importance of increasing the availability of these sukuk.

The evolving ecosystem and governance of green and sustainability financing require ongoing awareness and thought leadership to help stakeholders understand these instruments' nuances.

However, a lack of awareness was another significant challenge, noted by just over a third of respondents. The survey revealed that 63% of participants had at most a basic understanding of green and sustainability sukuk. Moreover, despite one-third possessing deep knowledge and practical experience, all respondents expressed a desire to further their understanding.

GCC sovereigns setting the stage for green and sustainability issuances

Indonesia and Malaysia have so far been the only countries to issue sovereign green and sustainability sukuk. However, GCC countries are preparing for similar issuances. Some GCC governments have already issued sovereign green or sustainability bonds. For example, Sharjah issued its first sustainability bond in 2023, raising $1 billion, and Qatar issued a $2.5 billion green bond in May 2024.

Oman, Qatar, and Saudi Arabia released their sovereign sustainability or green financing frameworks in the first nine months of 2024, setting guidelines for eligible projects. These frameworks ensure transparency and accountability, providing investors with confidence that funds will be used for genuine environmental and social benefits.

Key Islamic finance markets have introduced a mix of new regulations and updates in 2024 for issuing green and sustainability sukuk. These are part of ongoing efforts to enhance regulatory frameworks for sustainable finance, aiming to ensure greater transparency, accountability, and effectiveness in directing capital towards projects with environmental and social benefits.

New issuance guidance enhancing market awareness

In April 2024, London Stock Exchange Group (LSEG), in collaboration with the International Capital Market Association (ICMA) and the Islamic Development Bank (IsDB), published new guidance[1] on issuing green, social, and sustainability sukuk. The Guidance aims to help issuers label their sukuk and align with ICMA Principles, including examples and best practices.

1. ICMA, IsDB and LSEG publish guidance on green, social and sustainability sukuk

Survey responses on issuer awareness of green and sustainability sukuk were mixed. Half of the underwriters and advisers surveyed reported that issuers were very familiar with these sukuk, while the other half noted a lack of deep understanding, highlighting the need for further education.

Many issuers have been hesitant to issue green and sustainability sukuk due to a lack of awareness and understanding of the processes, costs, and requirements. The new guidelines are expected to enhance the credibility and appeal of sustainable sukuk, encouraging more issuers to enter the market. Two-thirds of survey respondents viewed the guidelines positively, suggesting they could foster a more sustainable financial environment.

Path to 2030: Key recommendations for green and sustainability sukuk development

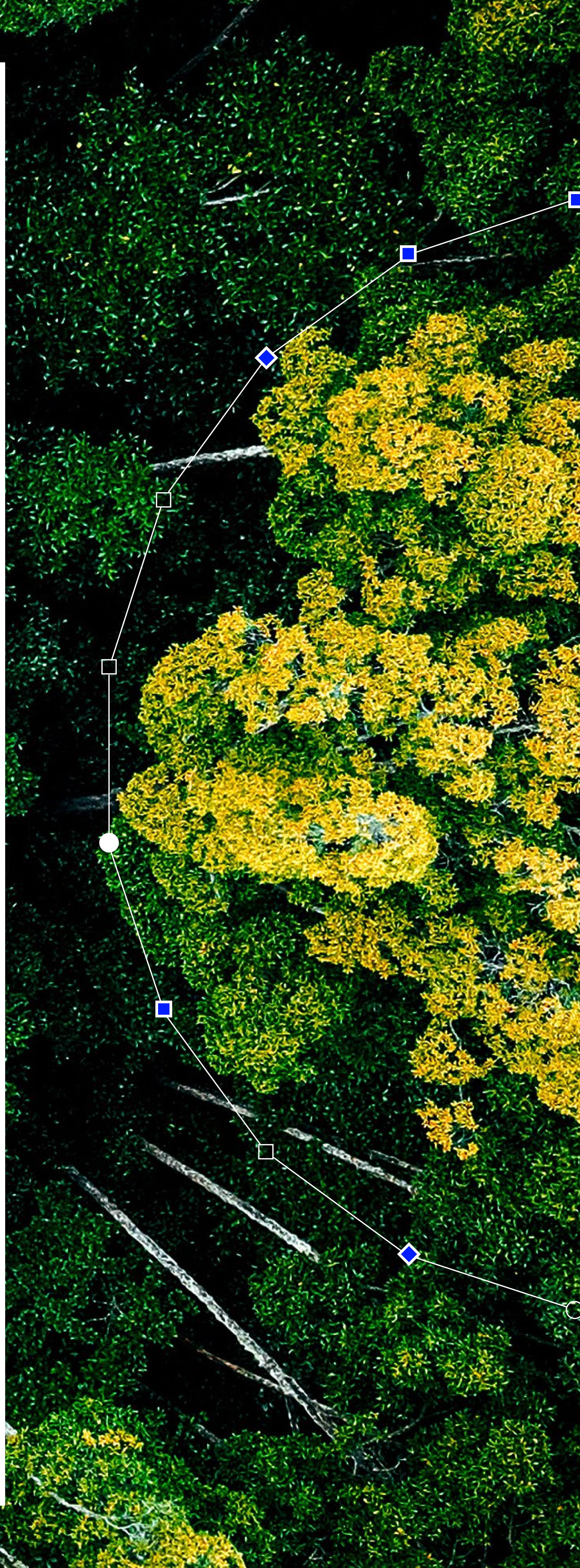
The green and sustainability sukuk market is still at a nascent stage, with considerable growth opportunities in sight.

Mobilisation of capital is critical to fulfilling global commitments towards the Sustainable Development Goals (SDGs) and climate change adaptation. Specific targets have been set by various international agreements and organisations to ensure adequate funding for these initiatives. Achieving the SDGs by 2030 requires $5.4 trillion–$6.4 trillion annually, with a $337 billion funding gap across 48 developing countries.

Around $30 billion to $50 billion of capital dedicated to the SDGs could be raised through green and sustainability sukuk by 2025, according to UKIFC. The "Green and Sustainability Sukuk Report 2022" outlined a roadmap to capitalise on rising demand to maintain the growth momentum of green and sustainability sukuk sukuk and enhance their potential based on best practices and the experiences of established sukuk markets.

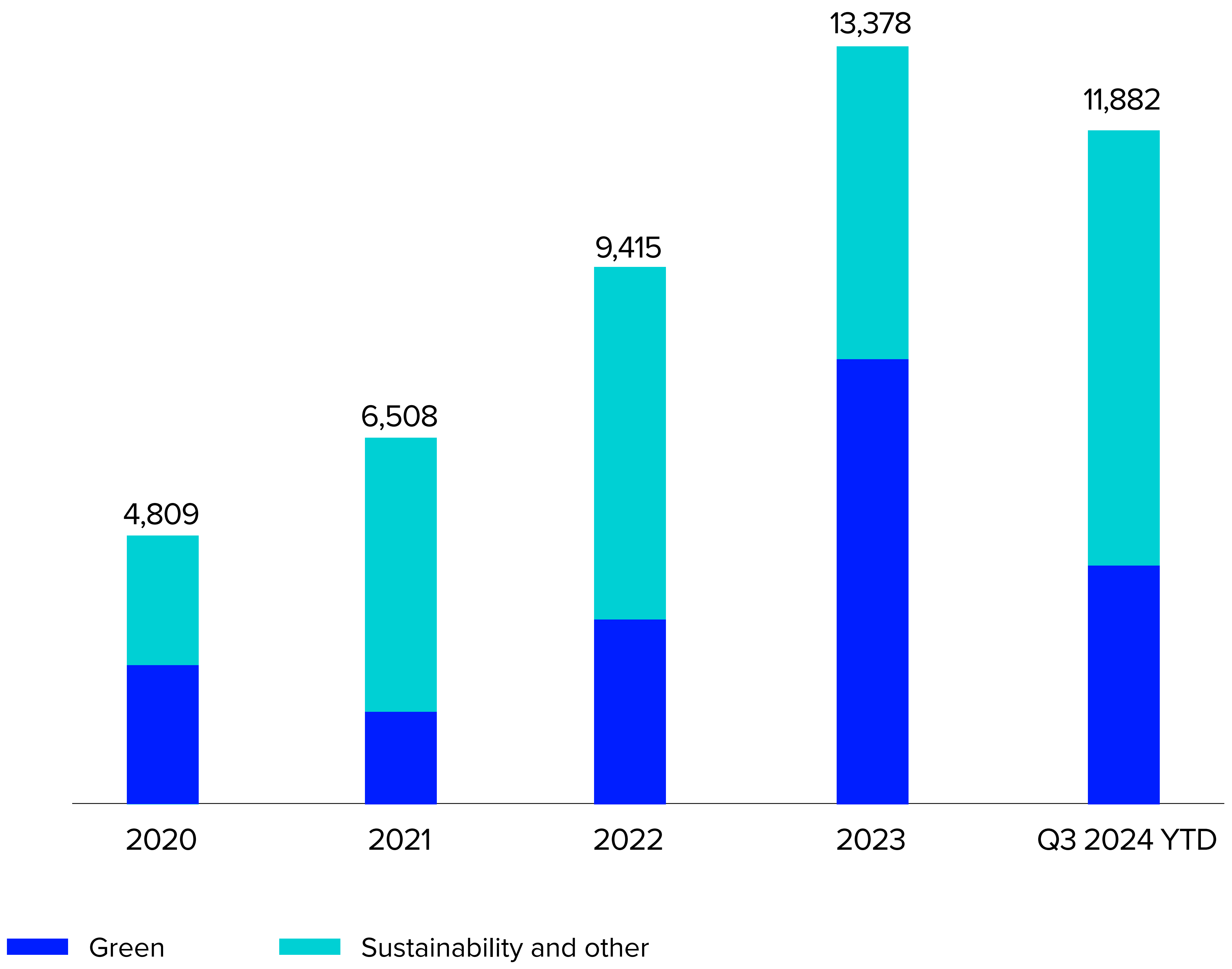
This update outlines the key areas for development and recommendations from the roadmap, highlighting the HLWG's initiatives within some of these areas:

- **Promote common regional and international standards** to build a common understanding of the market
- **Build capacity** with issuers and enhance the wider ecosystem
- **Expand the investor base** beyond traditional sukuk Investors

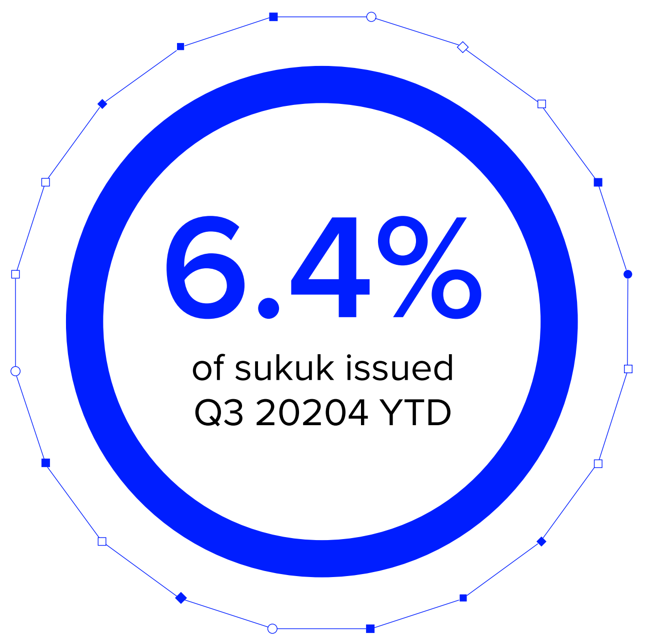


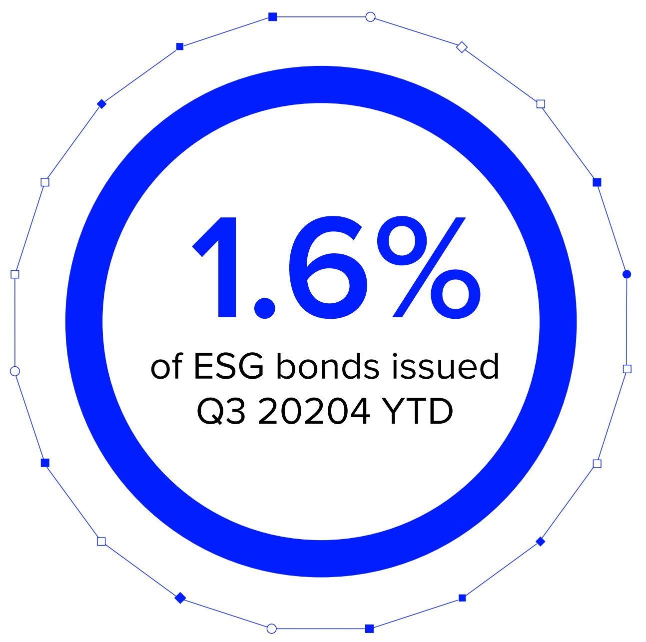
Green and sustainability sukuk issuance 2020 – Q3 2024

USD million



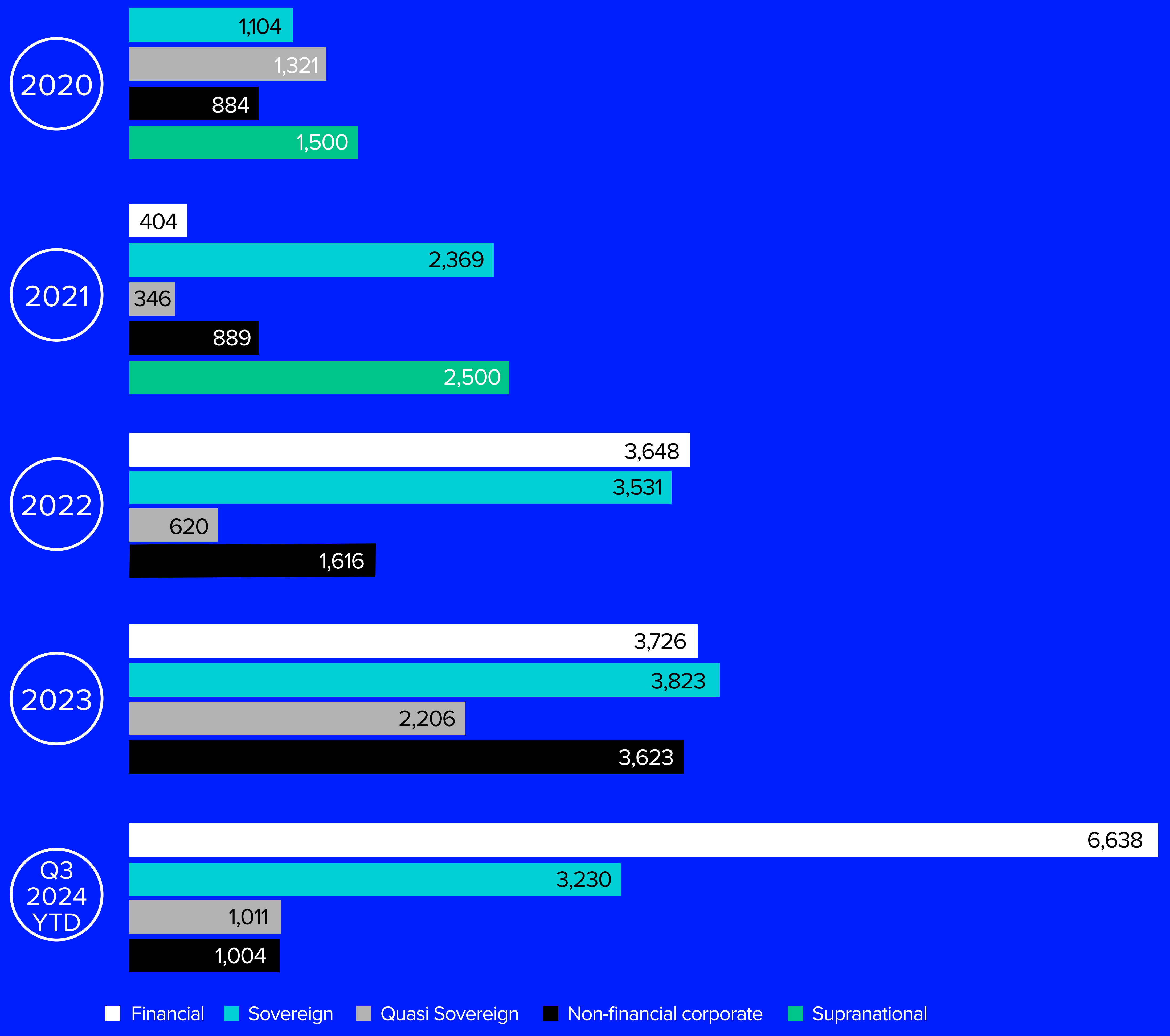
Source: LSEG Workspace





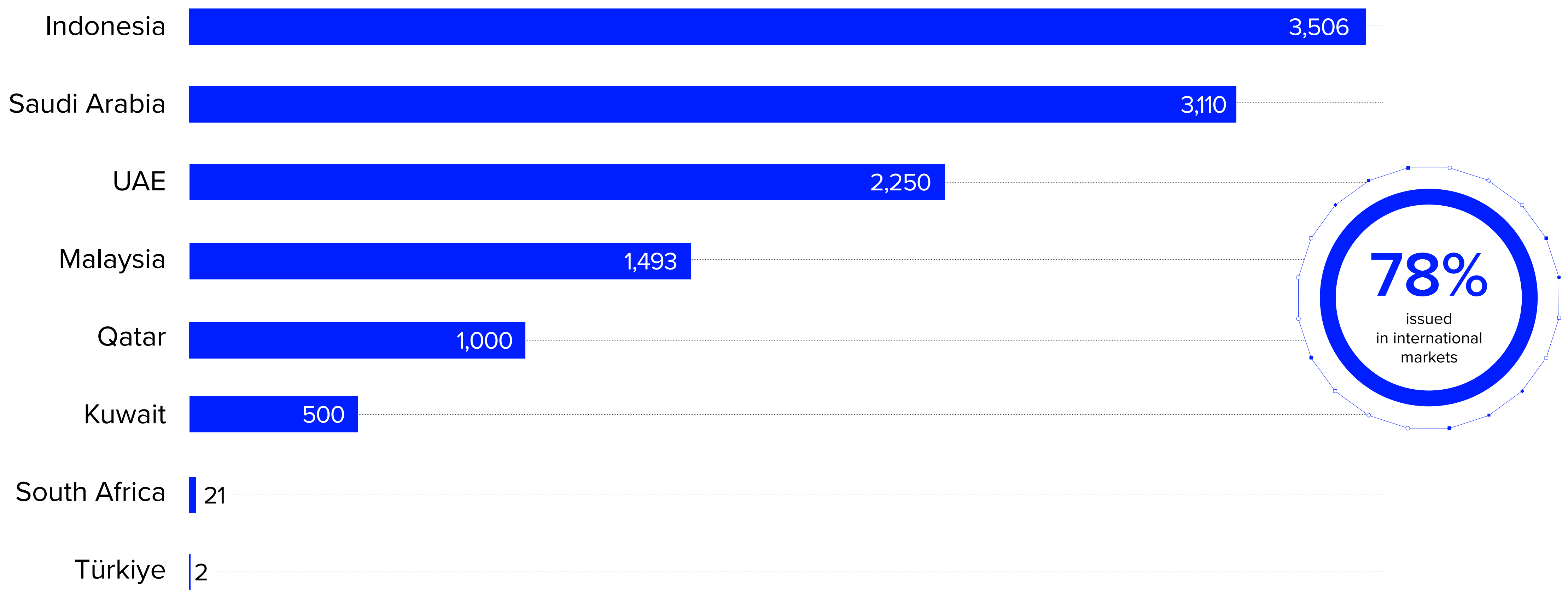
Green and sustainability sukuk issuance by issuer type 2020–Q3 2024

USD million

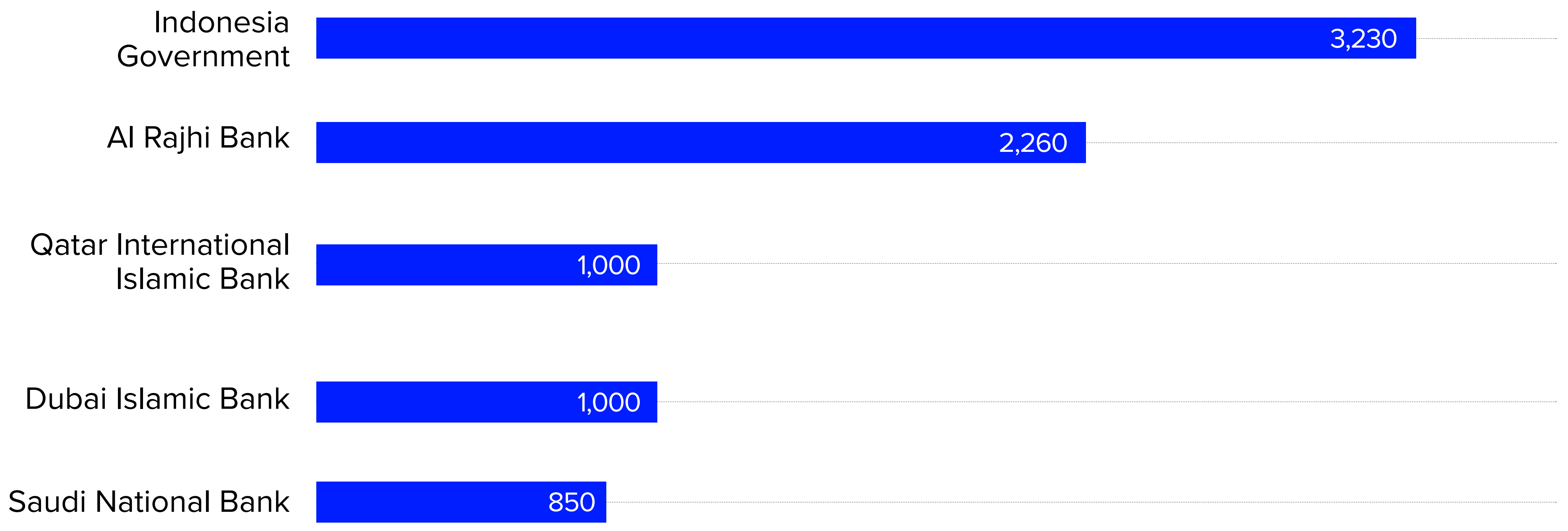


Source: LSEG Workspace

Green and sustainability sukuk issuance by country Q3 2024 YTD
USD million



Top issuers of green and sustainability sukuk Q3 2024 YTD
USD million



Survey insights on sukuk demand

50%

of underwriters and advisers surveyed expect a significant increase in demand in the next two years

Fulfilment of ESG mandates

leading reason investors choose to invest in green and sustainability sukuk

TOP SELECTION CRITERIA

for green and sustainability sukuk
- Shariah compliance
- Clear use of proceeds and ESG impact
- Pricing and valuation

55%

of investors plan to invest in green and sustainability sukuk within the next three years

More than 45%

of investors cited limited green and sustainability sukuk offerings as the most significant challenge to investing in this market

63%

of investors have at most a basic understanding of green and sustainability sukuk and their general principles

Recent developments impacting green and sustainability sukuk

GCC sovereigns laying groundwork for green and sustainability issuance

New and updated regulatory frameworks guiding issuance

Guidance on Green, Social and Sustainability Sukuk

Collaboration between London Stock Exchange Group (LSEG), the International Capital Market Association (ICMA) and the Islamic Development Bank (IsDB)

Other updates

• New criteria and guidelines for ICMA “Principles”

• Updated Green Bond Dataset Methodology

Green and sustainability sukuk roadmap

Promote common regional and international standards to build a common understanding of the market

Build capacity with issuers and enhance the wider ecosystem

Expand the investor base beyond traditional sukuk Investors

MARKET LANDSCAPE

Green and sustainability sukuk set for another record, despite moderated growth

While growth in the broader ESG bond market has been marginal so far in 2024, green and sustainability sukuk are set for another record year with double-digit growth. Green and sustainability sukuk issuance reached $11.9 billion in the first nine months of 2024, up 18% from the same period in 2023.

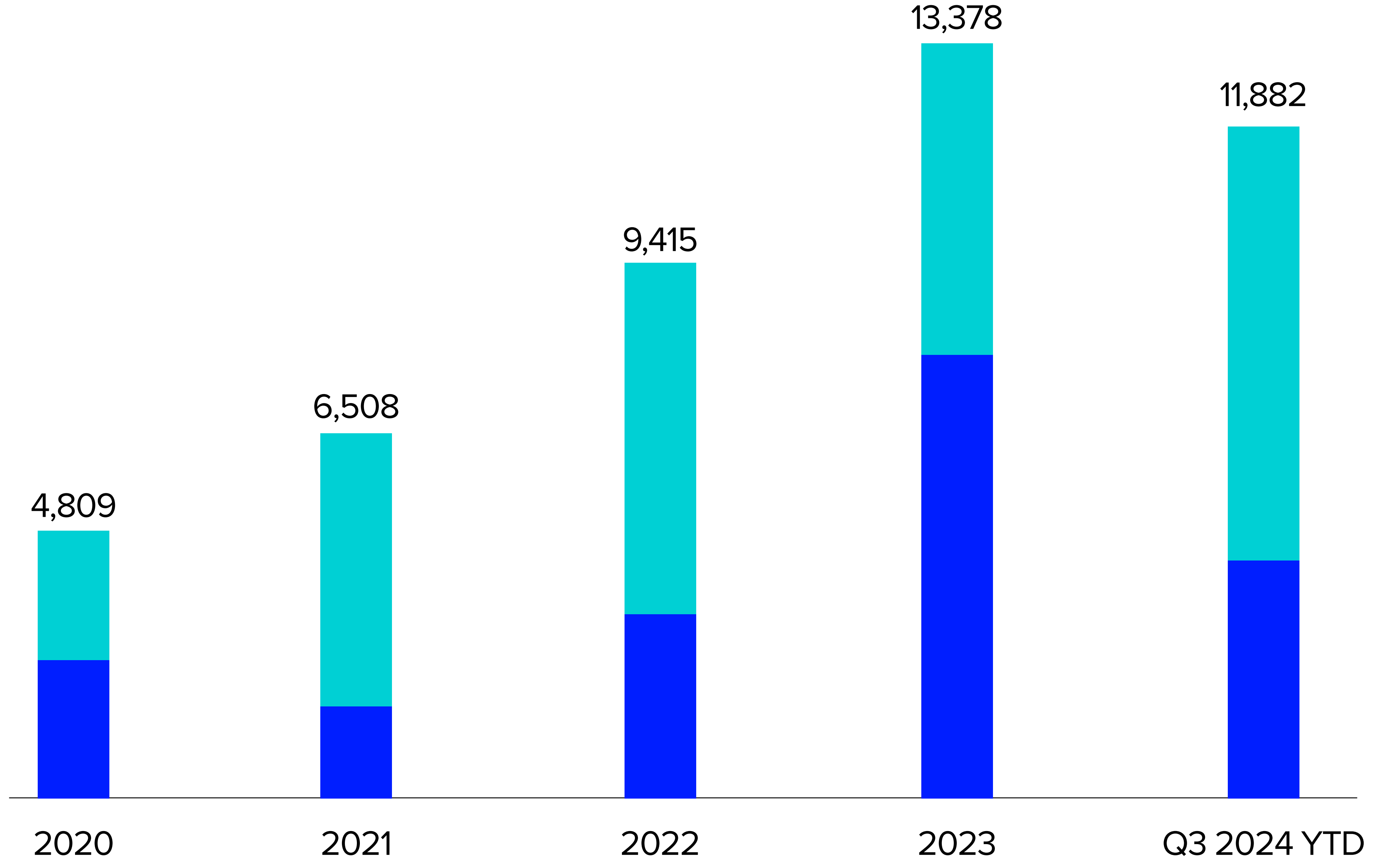
Global ESG bond issuance reached $745.8 billion in the first nine months of 2024, a modest 3.2% increase from the same period of 2023. ESG bond issuances in 2023 had continued a decline that began in 2022 as a result of volatile primary market conditions characterised by mounting inflationary pressures, rising interest rates, and geopolitical tensions.

Although demand for green and sustainability sukuk remains strong, issuance momentum has moderated in 2024 from previous years as issuers anticipate more favourable conditions in the fourth quarter and 2025. Green and sustainability sukuk accounted for 1.6% of total ESG bond issuance and 6.4% of total sukuk issuance in the first nine months of 2024.

Following last year's rebound in green sukuk issuance, which constituted 58% of the total value of green and sustainability sukuk issued, sustainability sukuk regained momentum in the first nine months of 2024. These included social, sustainability, and sustainability-linked sukuk. This trend suggests that last year's surge in green sukuk was likely significantly influenced by the hosting of COP28 in the UAE.

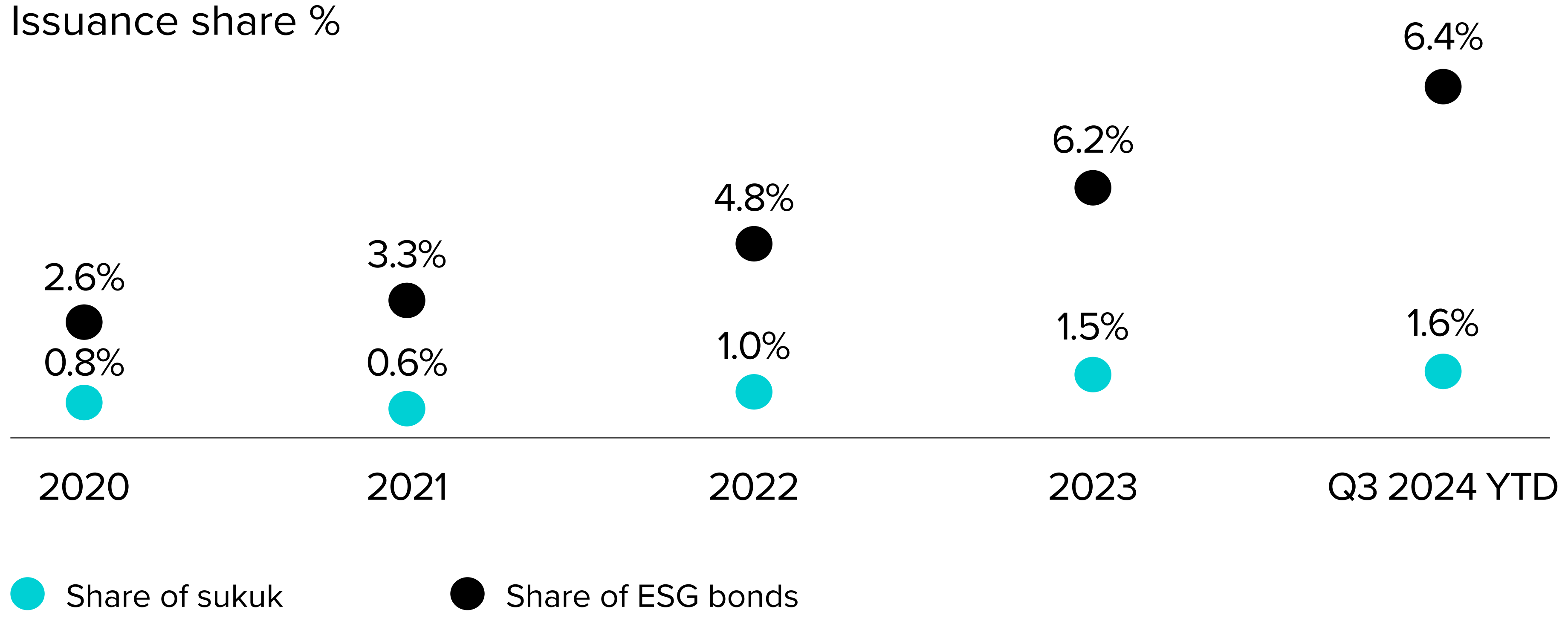
Conversely, green bonds accounted for 57% of ESG bonds issued in the first nine months of 2024, compared to 61% of the total in 2023. Green bond issuance is being driven primarily by non-financial corporates. Meanwhile, sustainability sukuk issued by financial institutions represent 50% of green and sustainability sukuk issued so far in 2024.

Green and sustainability sukuk issuance 2020 -Q3 2024
USD million



Source: LSEG Workspace

Green and sustainability sukuk share of sukuk and ESG bond markets 2020–Q3 2024
Issuance share %



Source: LSEG Workspace, LSEG Analysis

GCC issuance driving momentum, boosted by expansion into new markets

Green and sustainability sukuk issuance is being led by Malaysia, Indonesia, the UAE, and Saudi Arabia, which between them raised 84% of the cumulative issuance value by Q3 2024.

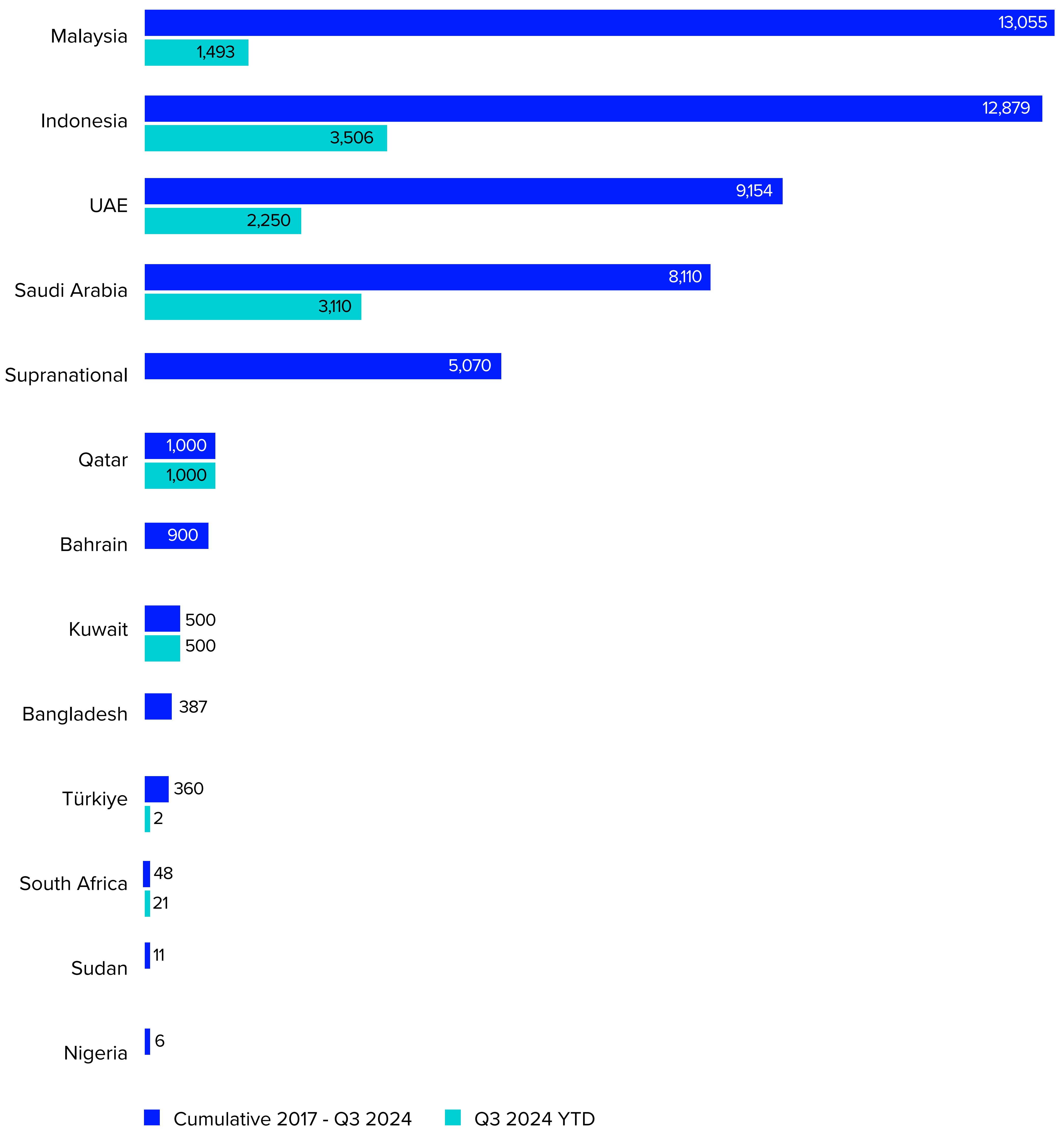
The largest issuance bases for green and sustainability sukuk in the first nine months of 2024 were Indonesia, Saudi Arabia, and the UAE, with the latter two accounting for 26% of total issuance.

Green and sustainability sukuk issuance is growing from GCC-based issuers, accounting for 58% of issuance in the first nine months of 2024 and 38% of cumulative issuance since market inception. Green and sustainability sukuk issuance from GCC issuers has been the main driver of market growth in recent years, a trend that is expected to continue. The region's commitment to sustainability and growing investor demand for ESG-compliant financial instruments have significantly boosted the market. Green and sustainability sukuk expanded into new markets in 2024, including Qatar and Kuwait, as more GCC corporates entered the market following COP28.

In January 2024, Qatar International Islamic Bank issued a $500 million sustainability sukuk, known as the "Oryx" sukuk. This was the first green or sustainability sukuk from a Qatar-based issuer. It met overwhelming demand, being oversubscribed by more than eight times. Over 120 investors from more than 19 countries participated in the issuance, demonstrating the strength of demand from international investors.

Similarly, Kuwait-based Warba Bank issued that country's first sustainability sukuk in August 2024, raising $500 million. The issuance racked up an order book worth nearly 3.6 times the issue size.

Green and sustainability sukuk issuance by country as of Q3 2024
USD million



Source: LSEG Workspace

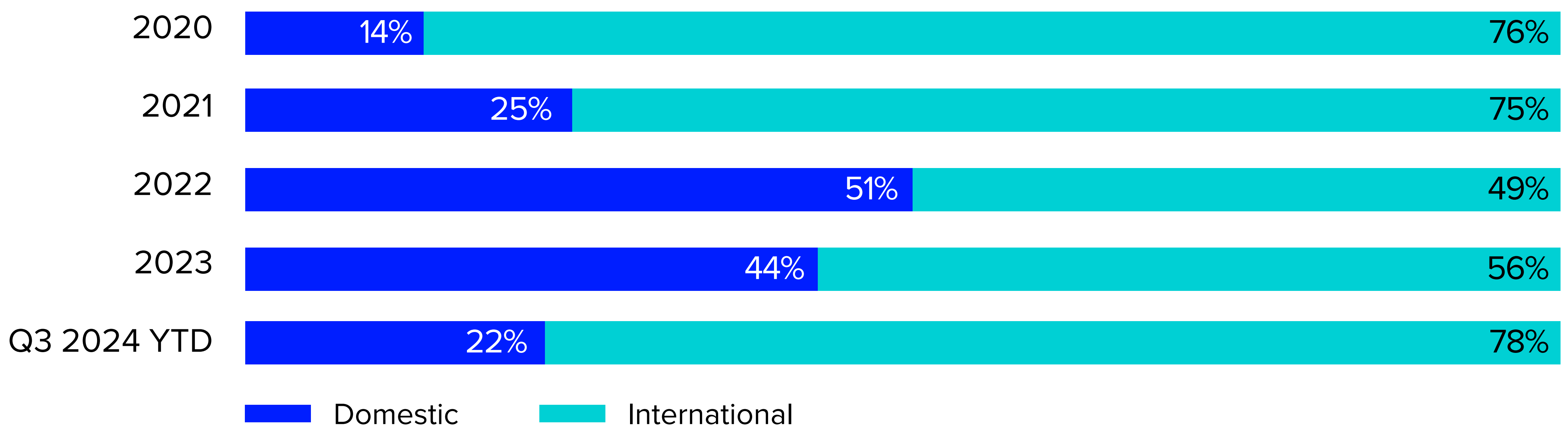
Tapping demand from international agnostic investors

Green and sustainability sukuk have predominantly been issued in international markets, with an annual average of 69% issued in foreign markets since 2020. In comparison, international issuances of traditional sukuk averaged 27% of annual issuance during the same period.

According to LSEG's ESG Sukuk Survey 2024, 100% of responding investors said they prefer to invest in international markets. To date, all green and sustainability sukuk issued by GCC-based entities have been sold on the Eurobond market and listed on the London Stock Exchange.

London Stock Exchange has emerged as one of the most popular venues for listing green and sustainability sukuk, hosting 36% of listed international sukuk in this category. Listing on this exchange offers a range of advantages: access to broader pools of international investors and capital, which helps mobilise funds for sustainable projects; a respected and balanced regulatory environment that enhances investor trust and confidence; and a dedicated segment for green and sustainability bonds, supporting issuers in meeting their sustainability goals and attracting ESG-focused investors.

Green and sustainability sukuk issuance by market of issue 2020–Q3 2024
USD million

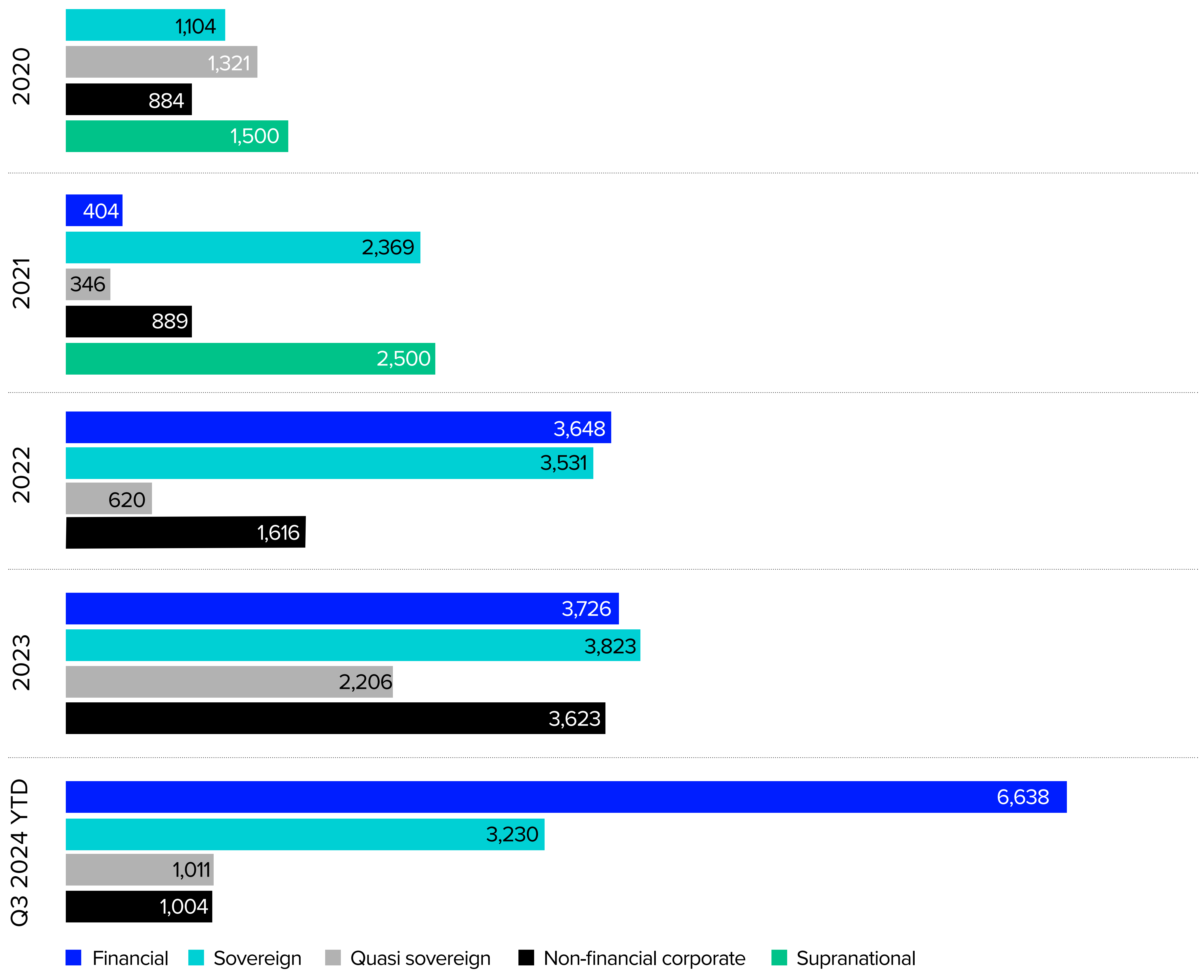


Source: LSEG Workspace

Financial institutions dominating sustainability sukuk issuance

Corporate issuers have become increasingly active in the green and sustainability sukuk market, accounting for 64% of the value issued in the first nine months of 2024. This compares with 55% in 2023. The rise has been driven by Saudi issuers and debut issuances from Qatar and Kuwait.

Green and sustainability sukuk issuance by issuer type 2020–Q3 2024
USD million



Source: LSEG Workspace

Financial institutions accounted for the largest share of green and sustainability sukuk issued in the first nine months of 2024, at 56% of the total value. More than half of this came from GCC-based banks, which issued some of the largest sukuk during this period. Most of the proceeds from these sukuk will go towards climate change adaptation and access to essential services.

The second-largest share belonged to sovereign green and sustainability sukuk, all of which were issued by the Indonesian government, making up 27% of total issuance in the first nine months of 2024. Indonesia has been the most consistent issuer in the market since it established its green sukuk programme in 2018. The sovereign has so far raised a total $12.6 billion through green sukuk to fund the country's climate change adaptation.

Top 10 issuers of green and sustainability sukuk Q3 2024 YTD

Issuer	Amount issued (USD million)
Indonesia Government	3,230
Al Rajhi Bank	2,260
Dubai Islamic Bank	1,000
Qatar International Islamic Bank	1,000
Saudi National Bank	850
Emirates Islamic Bank	750
Malaysia Rail Link	665
Warba Bank	500
Aldar Investment Properties	500
Pengurusan Air	279

Source: LSEG Workspace

There have been significantly fewer issuances from non-financial corporates in the first nine months of 2024, as Malaysian corporates held back in anticipation of more favourable conditions starting in the fourth quarter and 2025. There was significantly lower issuance from the utilities, transport and logistics, and construction and real estate sectors during the year, which had respectively accounted for 14%, 11%, and 9% of total issuance in 2023. Collectively, these sectors issued 2.1% of the total green and sustainability sukuk in the first nine months of 2024, with the utilities sector making up only 0.01% of the total.

DEMAND AND SUPPLY DYNAMICS

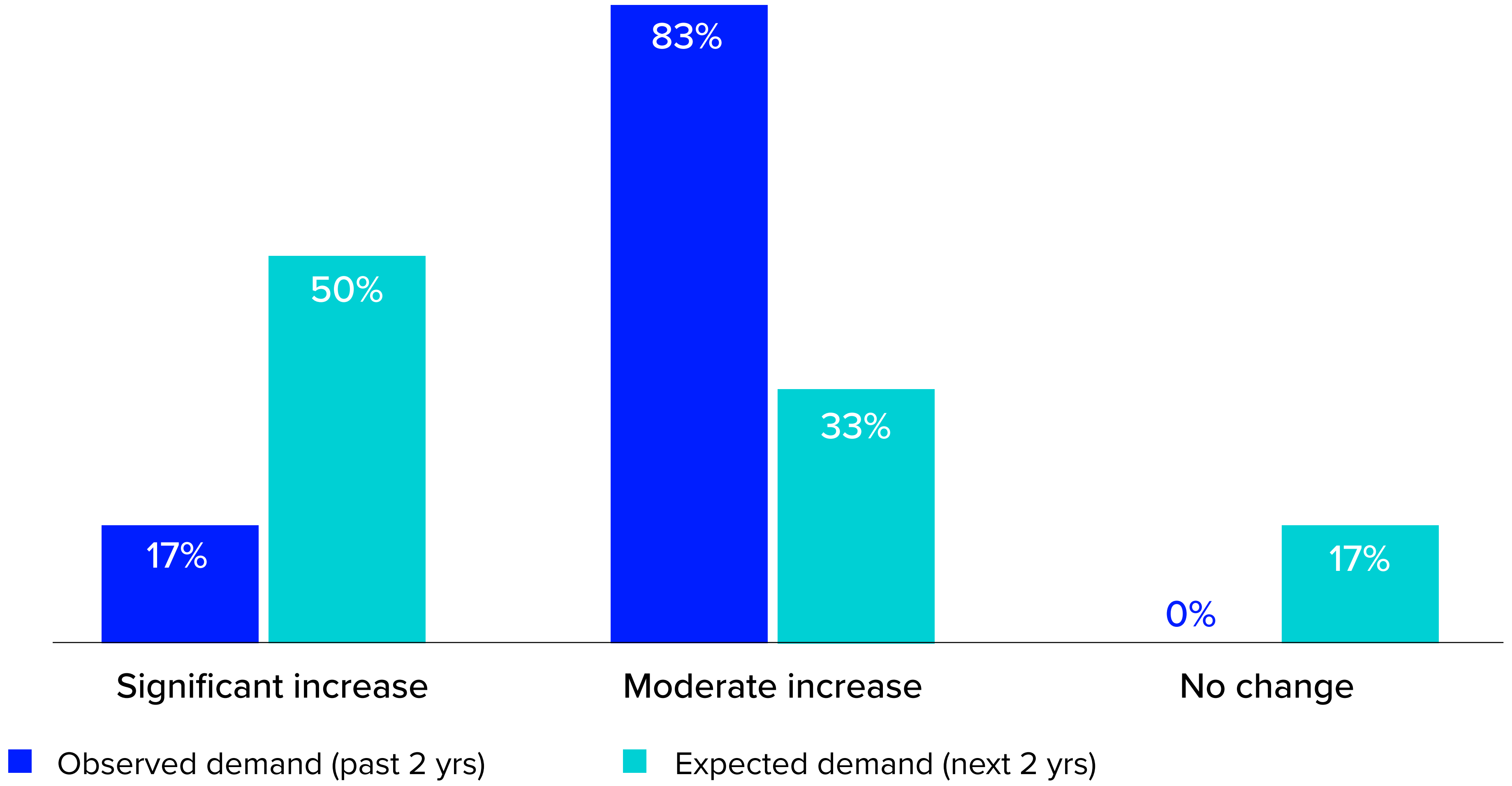
ESG mandates driving higher demand for green and sustainability than for traditional sukuk

Demand for green and sustainability sukuk remains higher than for traditional sukuk, which points to a new group of investors having entered the sukuk market. These are agnostic investors who seek to align with the ESG criteria incorporated in their investment mandates regardless of the Shariah compliance of the investment instrument.

Based on a select sample of sukuk issued in the first nine months of 2024, green and sustainability sukuk were subscribed at 4.3 times issuance values on average, compared with 3.1 times for traditional sukuk. This is a direct result of their green and sustainability labels, the majority of which came from European investors.

According to fixed income underwriters and advisers who responded to the LSEG's 2024 ESG Sukuk Survey, demand for green and sustainability sukuk increased over the past two years, with 83% saying the rise was moderate. Looking ahead, however, 50% of respondents expected a significant increase in demand in the next two years, suggesting demand is gathering pace for these financial instruments.

Observed and expected demand for green and sustainability sukuk
Responses %

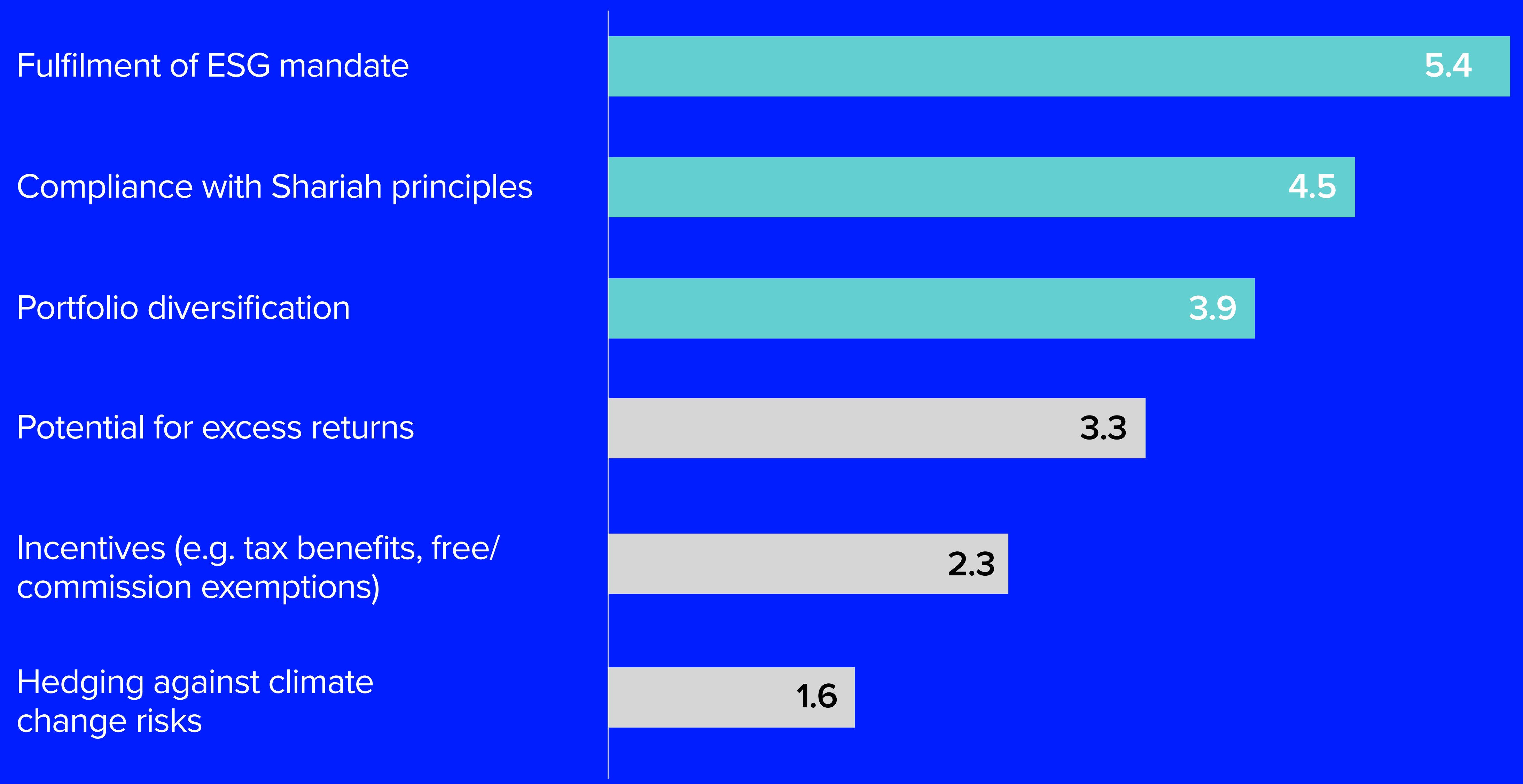


Source: LSEG ESG Sukuk Survey 2024

The growth in demand for green and sustainability sukuk is a testament to the increasing importance of sustainable and ethical investing. As more investors prioritise ESG considerations in their investment decisions, the market for green and sustainability sukuk is expected to continue its upward trajectory, offering promising opportunities for both issuers and investors.

The survey highlights the top three reasons investors choose to invest in green and sustainability sukuk. The foremost reason, with a clear lead, is the fulfilment of ESG mandates, which has an average rank of 5.4, (where a score of 6 is judged the most important factor and 1 the least important).

Reasons to invest in green and sustainability sukuk
Average rank, 6 = most important



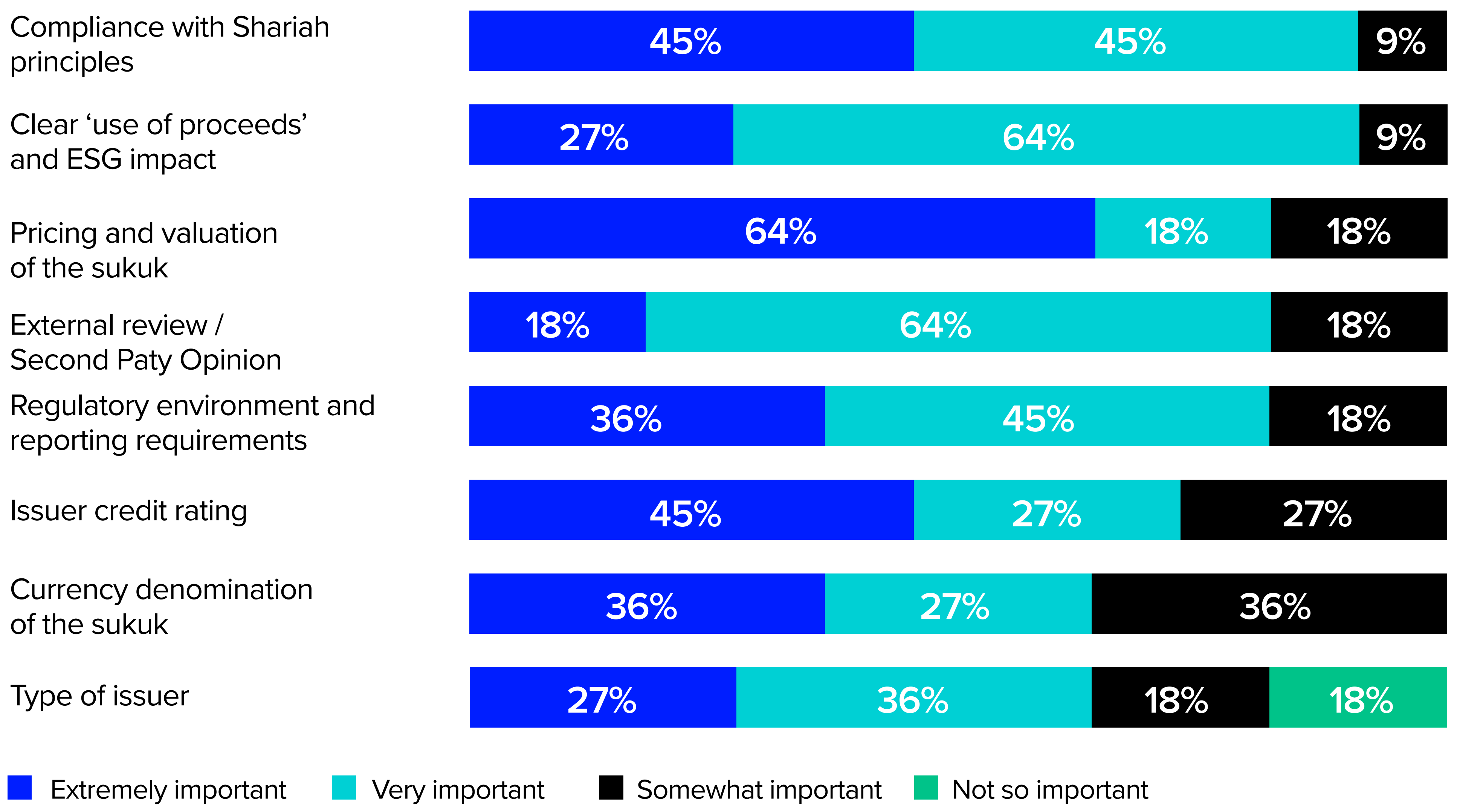
Source: LSEG ESG Sukuk Survey 2024

Interviews with a number of globally recognised fund managers outside core Islamic finance jurisdictions confirmed that their investments in sukuk are contingent upon their alignment with the fund's mandates. For instance, if a fund's mandate includes a Shariah compliance criterion, the fund manager will invest in sukuk if they also satisfy other criteria in the mandate. This includes traditional, green, or sustainability sukuk. Similarly, if the fund's mandate encompasses an ESG requirement, the manager may invest in a green sukuk, provided it meets the other investment criteria, which may not necessarily include Shariah compliance.

Compliance with Shariah principles ranks second in the criteria, with an average rank of 4.5, and portfolio diversification comes in third with an average rank of 3.9. It has been observed in core Islamic finance jurisdictions that while typical investors in sukuk invest in green or sustainability sukuk, this demand is mostly driven by the Shariah-compliance requirements of their mandates.

Looking further into investors' selection criteria for green and sustainability sukuk, 91% of those surveyed equally rated 'Shariah compliance' and 'clear use of proceeds' as being very or extremely important.

Investors' selection criteria for ESG investments
Responses %



Source: LSEG ESG Sukuk Survey 2024

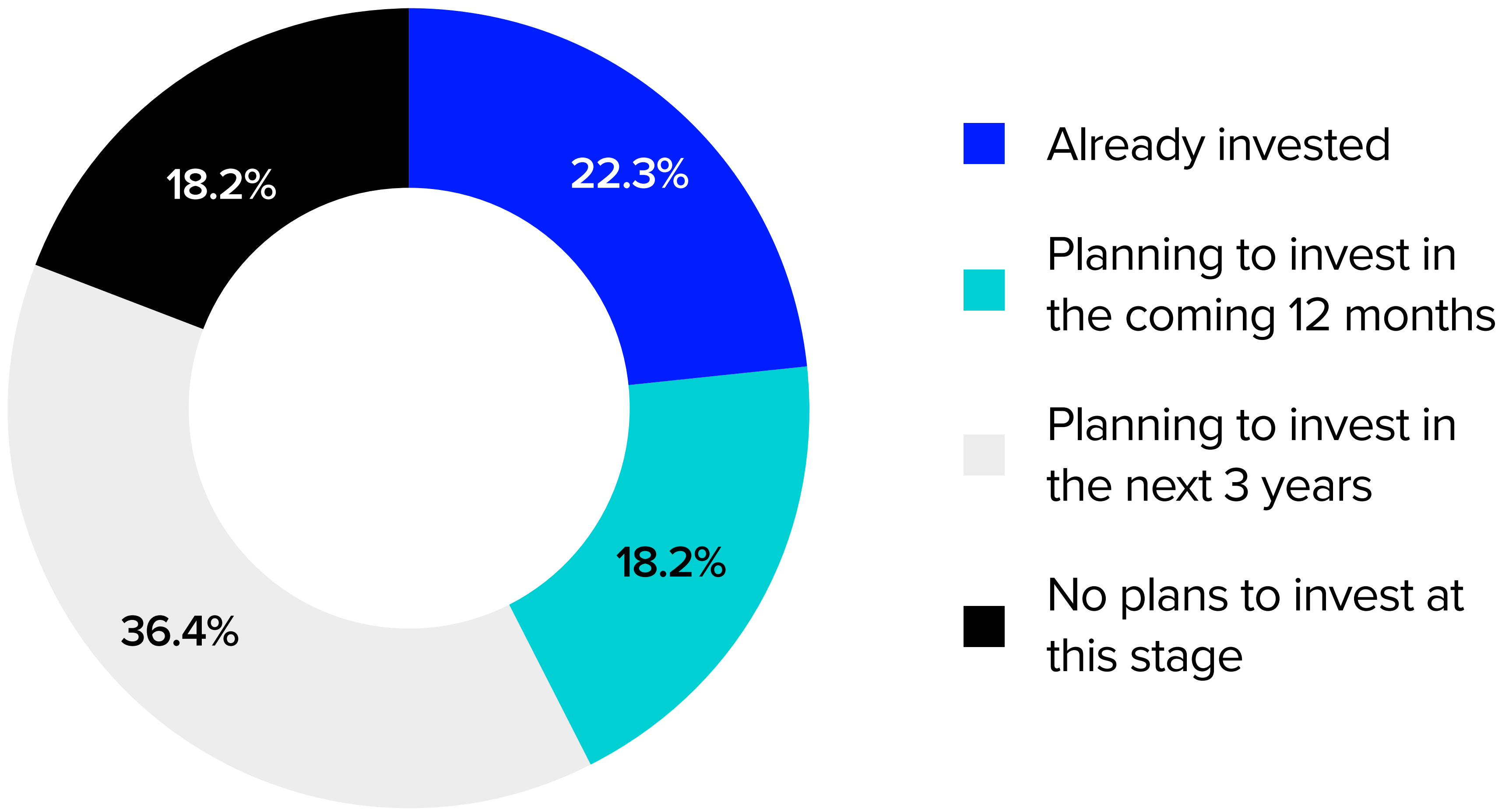
Around 46% of respondents rated Shariah compliance as extremely important due to the higher proportion of investors with fully or partial Shariah-compliance mandates. Meanwhile, use of proceeds and external reviews, or Second Party Opinions (SPOs), were rated as very important by nearly two thirds of respondents, emphasising the importance of verifying the green and sustainability labels of the sukuk. This also indicates a strong level of investor awareness around assessing and verifying these labels.

It is noted that pricing and valuation were rated by almost two thirds of investors as extremely important – the highest among all factors. This selection criterion is essential for fixed income investors, whether investing in traditional or green and sustainability bonds and sukuk, to ensure these instruments fit within the overall mandate.

Short supply limiting investments in green and sustainability sukuk

The survey also revealed that a noticeable percentage of investors are already engaged with green and sustainability sukuk. Specifically, 22% of investors have already invested, although a third of them are allocating 5% or less of their portfolios to green and sustainability sukuk.

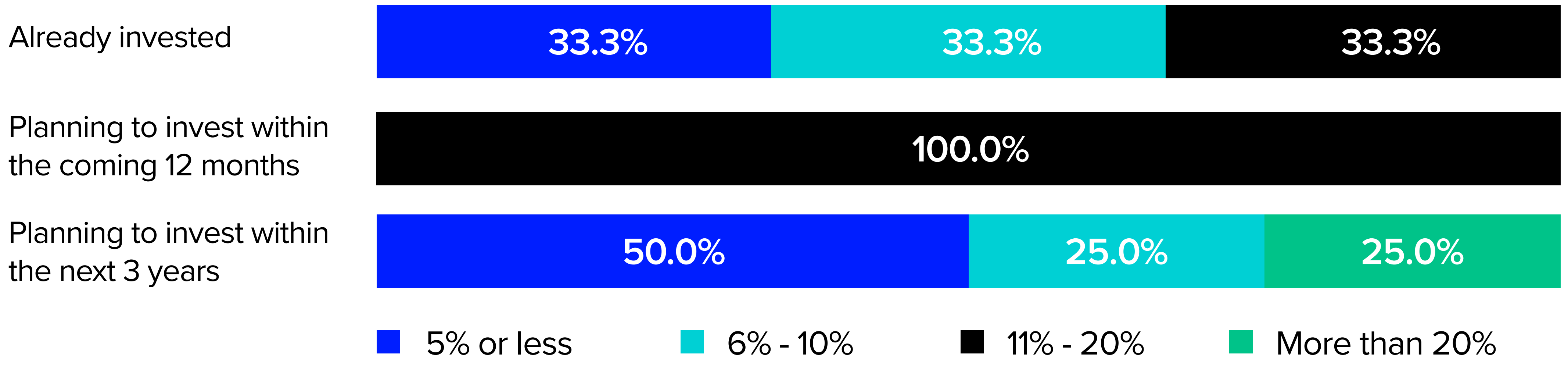
Investors' current and planned investments in green and sustainability sukuk
Responses %



Source: LSEG ESG Sukuk Survey 2024

Meanwhile, 18% of those surveyed plan to invest within the coming 12 months, who all plan to allocate between 11% and 20% of their portfolios to green and sustainability sukuk. Investors planning to invest in these sukuk within the next three years made up 36% of responses, and half these investors also planned to allocate 5% or less of their portfolios, although a significant portion plans to allocate more than 20%.

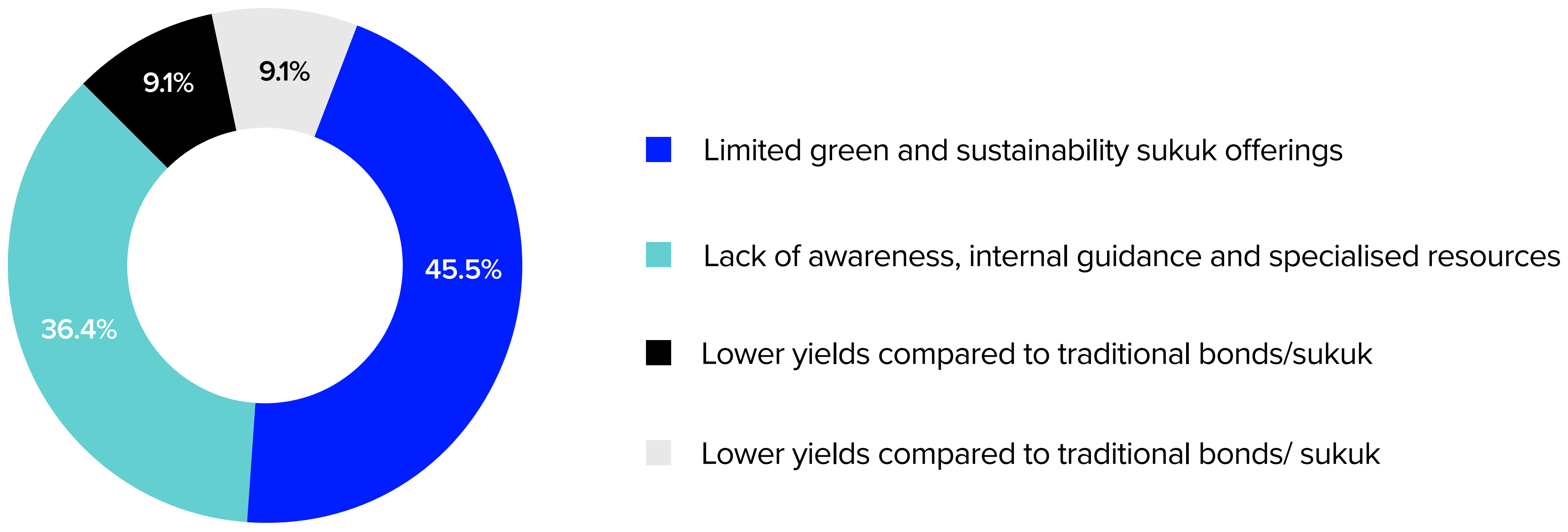
Investors’ current and planned allocations in green and sustainability sukuk
Responses %



Source: LSEG ESG Sukuk Survey 2024

More than half of respondents either already allocate or plan to allocate 10% or less of their portfolios to investments in green and sustainability sukuk, with the majority of this group choosing to invest less than 5%. This has no strong correlation with investors’ ESG or Shariah compliance mandates; rather it is most likely due to the limited supply of green and sustainability sukuk across the board.

Main challenges to investing in green and sustainability sukuk
Responses %



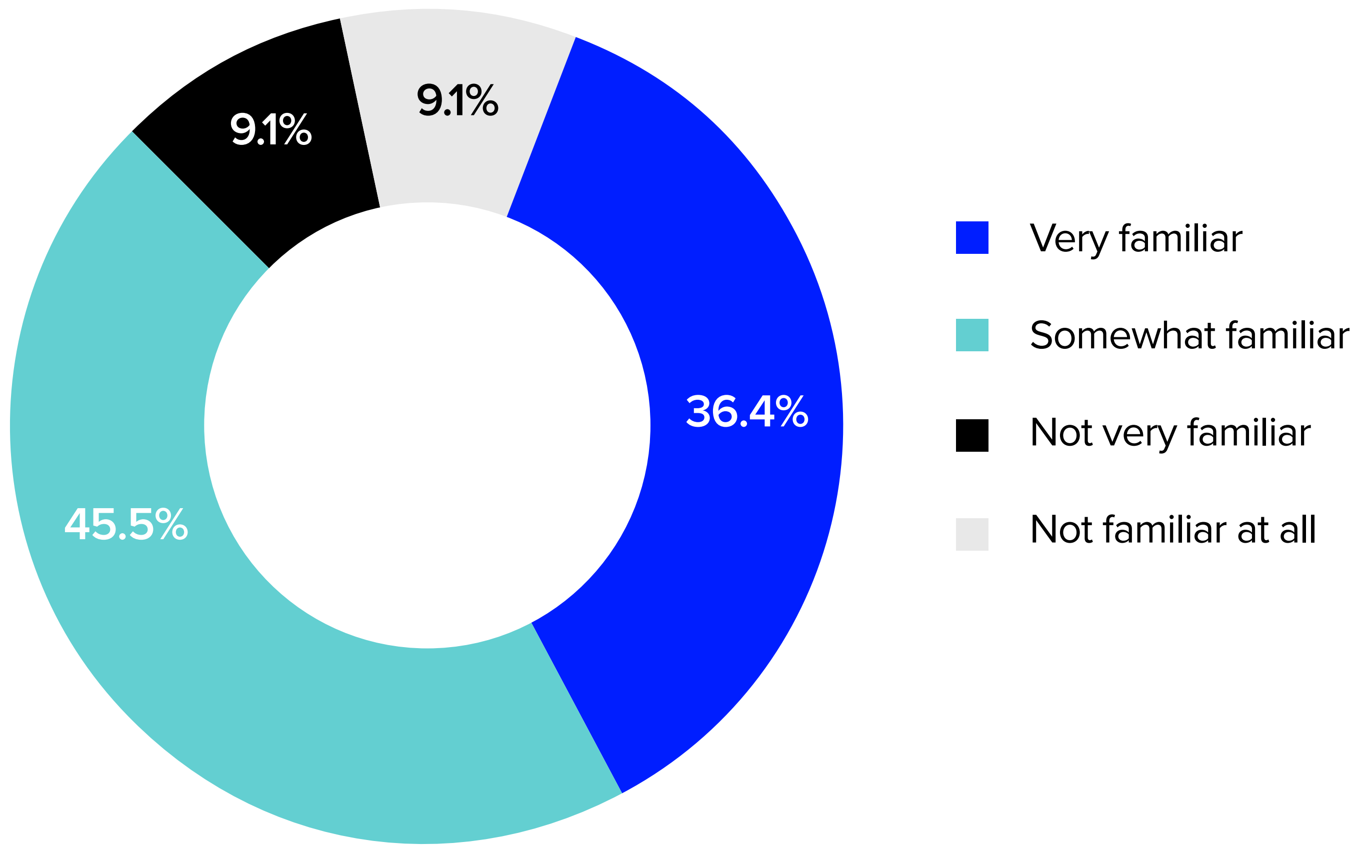
Source: LSEG ESG Sukuk Survey 2024

The survey revealed that more than 45% of respondents cited limited green and sustainability sukuk offerings as the most significant challenge to investing in this market. Confirming this, two-thirds of respondents said an increase in green and sustainability sukuk available for investment is very or extremely important.

Another significant challenge is low awareness, cited by one-third of respondents. Most were familiar to some degree with green and sustainability sukuk, although 63% said that they had at most a basic understanding of these sukuk and their general principles.

Still, even though nearly two-thirds of respondents had a deep understanding and practical experience with green and sustainability sukuk, all of them expressed interest in learning more about these instruments. The ecosystem and governance of green and sustainability financing and investments continue to rapidly evolve as new risks emerge and use cases are developed, which requires regularly updated awareness and thorough leadership efforts to enhance market stakeholders’ understanding of the nuances of these instruments.

Investors’ awareness of green and sustainability sukuk
Responses %



Source: LSEG ESG Sukuk Survey 2024

RECENT DEVELOPMENTS

GCC sovereigns laying groundwork for green and sustainability debt issuance

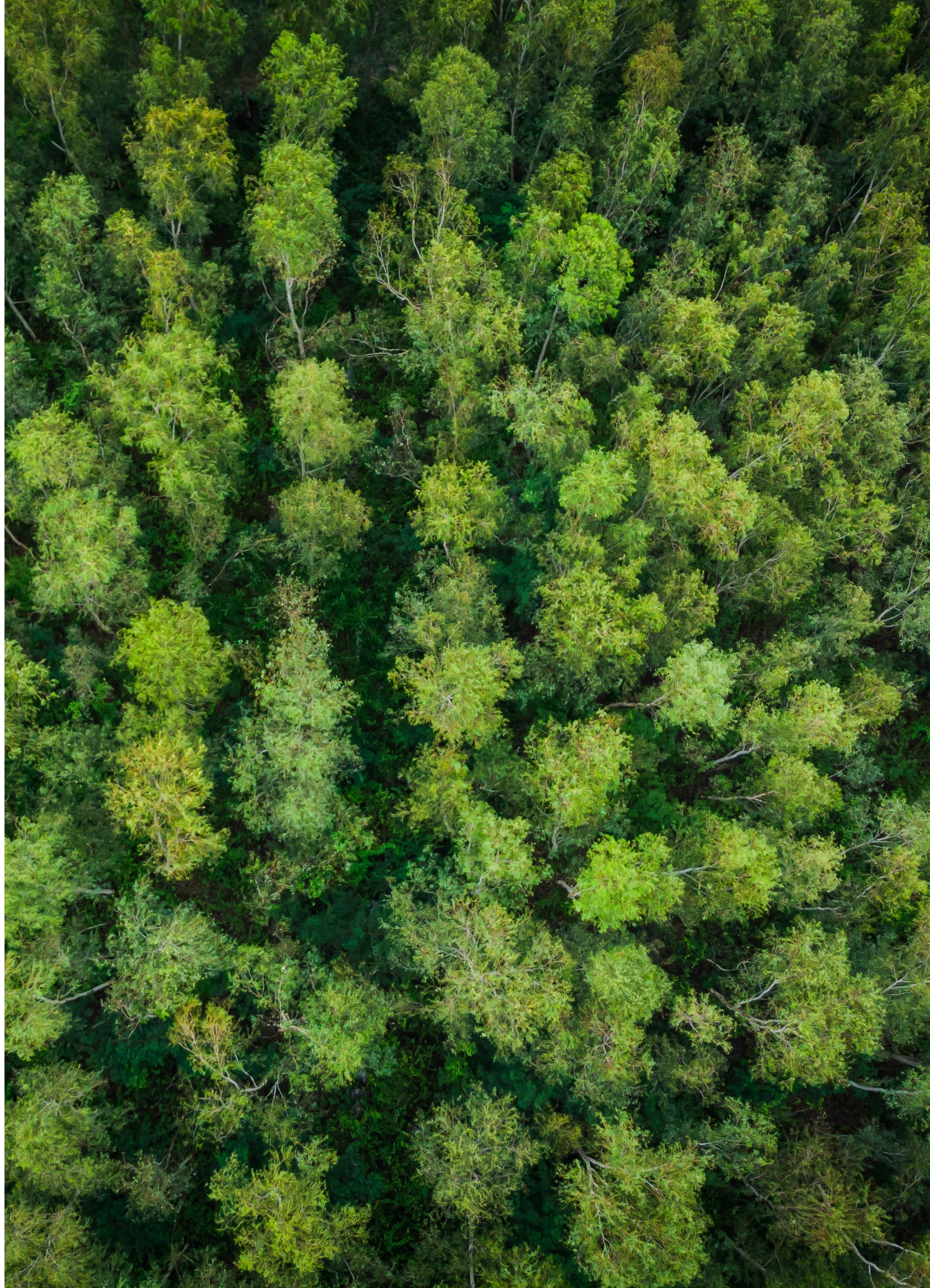
Indonesia and Malaysia have been the only countries to date to issue sovereign green and sustainability sukuk. However, this is poised to change as countries in the GCC region are laying the groundwork for similar issuances. Some GCC governments have already issued sovereign green or sustainability bonds. For instance, the Sharjah government issued its debut sustainability bond in 2023, raising $1 billion, and Qatar was the first country-level government in the GCC to issue a green bond in May 2024, raising $2.5 billion.

Oman, Qatar, and Saudi Arabia each released sovereign sustainability or green financing frameworks during the first nine months of 2024, indicating plans to issue such bonds or sukuk. These frameworks establish the guidelines and criteria for eligible projects. They also provide investors with confidence that the funds will be used for genuine environmental and social benefits, which is a prerequisite for issuing green or sustainability debt instruments.

Oman's Ministry of Finance launched its Sustainable Finance Framework in January 2024, aimed at supporting the country's green energy transition and climate-mitigation strategies. The framework includes issuance of green, social, sustainability, and blue loans, bonds, and sukuk, in addition to Waqf sukuk to fund projects aligned with Oman's commitments to the SDGs and Net Zero objectives. Given Oman's heavy reliance on oil and gas, this framework represents a significant shift towards diversifying the country's economy and investing in sustainable infrastructure and renewable energy projects.

Saudi Arabia's Ministry of Finance unveiled its Green Financing Framework in March 2024 to advance the Kingdom's sustainability goals under its Vision 2030. The framework is part of the country's Financial Sector Development Program and aims to achieve net zero emissions by 2060 through the Circular Carbon Economy approach. It includes the issuance of green bonds and other financial instruments to support projects that reduce greenhouse gas emissions, promote renewable energy, and enhance environmental sustainability. Saudi Arabia's framework underscores its commitment to transforming its economy, reducing its carbon footprint, and investing in large-scale renewable energy projects such as NEOM city and various solar and wind energy initiatives.

Qatar introduced its Sovereign Green Financing Framework in April 2024 as part of its commitment to sustainable development and the Paris Agreement. This framework supports the Qatar National Vision 2030 and the National Environment and Climate Change Strategy, focusing on a broad range of sustainable development goals. It includes the issuance of green, social, and sustainability bonds, sukuk, and loans to finance projects that will contribute to environmental and social benefits such as reducing greenhouse gas emissions, enhancing biodiversity, and promoting sustainable resource management. Qatar's framework reflects its ambition to balance economic growth with environmental stewardship, employing its financial resources to support sustainable urban development and infrastructure projects.



New and updated regulatory frameworks guiding green and sustainability debt issuance

Several regulations on the issuance of green and sustainability sukuk have come into force in Q4 2023 and in 2024 in key Islamic finance markets. The updates reflect the ongoing efforts of these countries to enhance their regulatory frameworks for sustainable finance as they look to ensure greater transparency, accountability, and effectiveness in directing capital towards environmentally and socially beneficial projects.

Indonesia: New regulations on Issuance and Requirements for Sustainable Debt Securities and Sustainable Sukuk, classifying economic activities based on their environmental impact. Indonesia's Financial Services Authority (OJK) aims to create a more transparent and accountable framework for sustainable investments.

The new framework encourages investments in green projects such as renewable energy and sustainable infrastructure. It is designed to attract more capital into sectors that contribute positively to environmental sustainability. Issuers can use the guidelines to access a broader base of environmentally conscious investors, thereby contributing to Indonesia's environmental sustainability goals and ensuring a greener and more sustainable future for the country.

Pakistan: The Securities and Exchange Commission of Pakistan (SECP) issued updated guidelines for the issuance of green bonds in June 2024. These provide detailed criteria for eligible green projects, focusing on areas such as renewable energy, water management, and pollution control. The aim is to create a more robust framework for financing environmentally sustainable projects that aligns with international standards. The initiative is part of Pakistan's broader efforts to enhance its sustainable finance landscape and attract green investments.

The original guidelines issued in 2021 laid the foundation for green bond issuance in Pakistan. The guidelines were designed to diversify sources of financing for green projects and ensure that proceeds were used for activities promoting energy efficiency, renewable energy, pollution prevention, and sustainable management of natural resources. Through this, the SECP aimed to support the country's environmental sustainability goals and create a transparent and accountable framework for green investment. The 2024 update refined the criteria and expanded the scope to support Pakistan's commitment to sustainable development.

Oman: In March 2024, Oman's newly established Financial Services Authority (FSA), which replaced the Capital Market Authority (CMA), introduced new regulations for the issuance of bonds and sukuk. The new guidelines are part of the broader financial sector development plans under Oman Vision 2040 and the National Program for Fiscal Sustainability and Financial Sector Development, known as "Estidamah," which aims to enhance the competitiveness of the financial sector by fostering the development of efficient and effective markets.

The regulations include specific provisions for green and sustainable securities, focusing on financing projects that contribute to environmental sustainability. This includes sectors such as renewable energy, sustainable infrastructure, and water conservation. The regulations also cover blue bonds, aimed at financing projects related to ocean and marine conservation, and Waqf sukuk, designed to support the development of Waqf (endowment) institutions for educational, medical, and social purposes. By aligning with Oman's national sustainability goals, the guidelines encourage investments in projects that support the country's commitment to reducing carbon emissions and promoting the efficient use of natural resources.

Green and sustainability sukuk issuance guidance enhancing market awareness

In April 2024, London Stock Exchange Group (LSEG), in collaboration with the International Capital Market Association (ICMA) and the Islamic Development Bank (IsDB), published new guidance on the issuance of green, social, and sustainability sukuk. One of the key outputs of the HLWG, this guidance aims to provide practical information for issuers and other market participants on how green and sustainability sukuk can be labelled as such and how they can align with ICMA Principles. The guidance includes examples, case studies, and best practices to help develop the sustainable sukuk market.

Many issuers have been reluctant or uninterested in issuing green and sustainability sukuk due to a lack of awareness about the nuances of this type of sukuk when compared to traditional sukuk, as well as a lack of understanding of the issuance processes, costs, and requirements. This guidance is the first step towards deepening this awareness.

The guidance assists issuers in structuring their sukuk to meet green, social, and sustainability criteria, and are expected to play a pivotal role in enhancing the credibility and appeal of related sukuk. They have been well received as a step towards encouraging potential green and sustainability sukuk issuers to enter the market, according to two-thirds of underwriters and advisers who responded to the survey. This positive outlook suggests the new guidance could play a significant role in fostering a more sustainable and socially responsible financial environment.

Updated ICMA “Principles” enhancing transparency and credibility in sustainable finance

The majority of green and sustainability sukuk so far issued have complied with one of the ICMA principles (the “Principles”) - including the Bond Principles (GBP), Sustainability-Linked Bond Principles (SBP) and Sustainability Bond Guidelines (SBG) - which have collectively become the world’s leading frameworks for the issuance of thematic bonds.

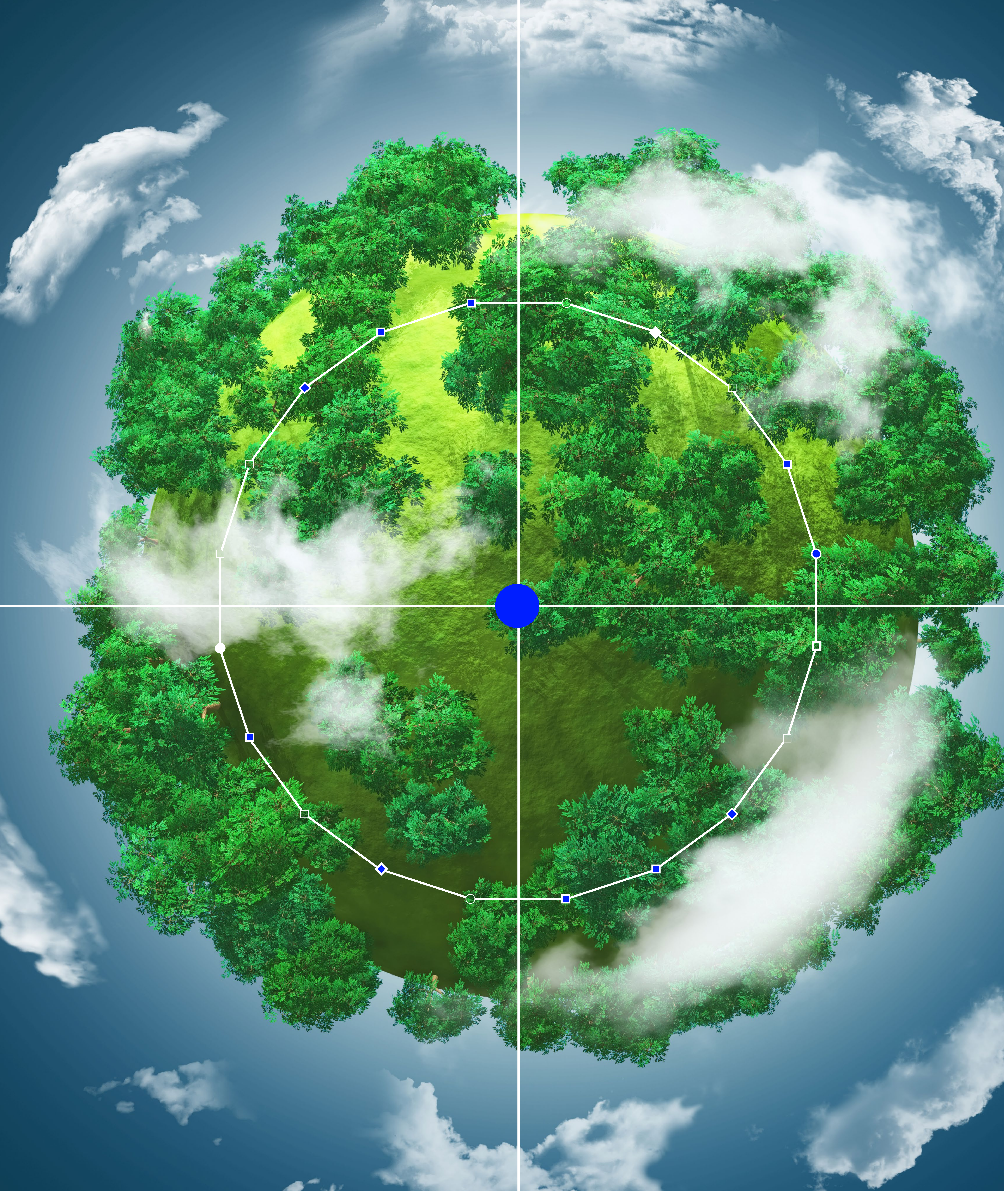
The ICMA introduced new criteria and additional guidelines in June 2024 to support the Green, Social, Sustainability, and Sustainability-Linked Bond Principles.

The new materials and guidance include:

Guidance for Green-Enabling Projects: This helps identify projects that, while not explicitly green, are crucial to the value chain of green projects. It addresses both induced and avoided emissions and the management of related environmental and social risks. By broadening the scope of what can be considered a green project, the update encourages more comprehensive environmental impact assessments and investments. This is particularly important for industries that support green projects indirectly, ensuring that their contributions are recognised and incentivised. This will enhance transparency, accountability, and investor confidence in green and sustainability sukuk.

Updated Sustainability-Linked Bond (SLB) Principles: These principles include clarifications on key performance indicator (KPI) selection, encouraging issuers to align KPIs with their overall sustainability strategies. The update introduces a new SLB disclosure data checklist and expands the SLB KPIs registry to include more environmental themes. This will ensure that sustainability-linked bonds are more transparent and aligned with broader environmental goals. For fossil fuel-dependent industries like oil and gas or aviation, the updated principles could encourage issuers to consider issuing transition sukuk, a form of SLB. These sukuk can be structured to include KPIs related to reducing carbon emissions or increasing the use of renewable energy, making it easier for these industries to demonstrate their commitment to transitioning towards more sustainable practices.

Impact Reporting Handbook: A new annexe has been added to this handbook to cover the potential environmental and social risks associated with eligible project categories for green bonds. This addition aims to provide issuers with a more comprehensive framework for reporting the impacts of their green projects. By offering detailed guidance on risk management and impact reporting, this update helps issuers ensure their projects meet high standards of environmental and social responsibility.



Updated Green Bond Dataset Methodology pushing transparency and inclusivity

In April 2024, the Climate Bonds Initiative (CBI) released significant updates to the Green Bond Dataset (GBD) Methodology. The updates were designed to enhance the framework for assessing and classifying green bonds and sukuk. Nearly all green sukuk issued to date align with the CBI's taxonomy.

The updates include:

• **Broader definition of green credentials** to include transitional activities vital to the post-2050 low-carbon transition.

• **Expanded sector coverage** to include blue economy and marine resources, with a screening approach rooted in minimum climate and environmental safeguards.

• **Flexibility in the use of proceeds,** introducing a 10% margin of flexibility to accommodate sectors lacking readily available metrics or requiring further assessment against a benchmark or proxy.

By improving data accuracy and expanding the criteria for what qualifies as a green bond or sukuk, the updated methodology allows for a broader range of projects and sectors to be included. This means that more diverse environmental initiatives can receive funding through green bonds and sukuk, promoting a wider impact on sustainability efforts.

For investors, the updates provide a more reliable and comprehensive tool for evaluating the environmental credentials of green bonds and sukuk, which helps them make informed decisions and manage risks more effectively. For issuers, the enhanced reporting standards and expanded criteria mean they can attract a larger pool of investors by demonstrating their commitment to sustainability. This not only helps in raising capital for green projects but also boosts the credibility and marketability of their bonds.

OUTLOOK

The mobilisation of capital is critical to fulfilling global commitments towards the SDGs and climate change adaptation. Specific targets have been set by various international agreements and organisations to ensure adequate funding for such initiatives.

Developed countries pledged to mobilise $100 billion per year by 2020 to support climate mitigation and adaptation efforts in developing countries, and this target was extended to 2025. According to the Intergovernmental Panel on Climate Change, global mitigation investments will need to increase by a factor of 36 by 2030 to limit warming to 2°C.

In parallel, the estimated annual cost to achieve the SDGs by 2030 ranges from $5.4 trillion to $6.4 trillion, according to a 2023 study by UNCTAD of 48 developing countries.[2] These countries face an estimated funding gap of $337 billion annually. This funding is needed to address various goals, including social protection and decent jobs, transforming education, food systems, climate change, biodiversity loss and pollution, energy transition, and inclusive digitisation.

Green and sustainability sukuk could raise between $30 billion and $50 billion of capital dedicated to the SDGs by 2025, according to projections made in 2021 by UKIFC. The value of green and sustainability sukuk issued between the announcement of these projections and the third quarter of 2024 amounted to $41.2 billion and is on track to exceed $50 billion in 2025. However, this is only a small share of the required funding needed to fulfil SDG financing requirements.

In addition, projections by GEFI estimate that the integration of the sustainability agenda will contribute $750 billion - $1 trillion to the size of the global Islamic finance market over the next decade.

Burgeoning global demand for ESG investments presents further opportunities for growing the green and sustainability sukuk market. Total assets under management in the global responsible investments fund market stood at $2.9 trillion at the end of Q3 2024, according to data from Lipper. Compared to a year before, assets increased substantially by 18.5%, or $459.5 billion. Demand will continue to increase as ESG investment growth extends into developing economies, which will prompt even higher flows into ESG-focused fixed-income funds. Naturally, this will increase demand for green and sustainability sukuk as a tool for diversification and a source of higher yields.

2. When expanded to cover all developing economies, using the median per-capita cost for the 48 economies in the study, the total annual needs fall between $6.9 trillion and $7.6 trillion.

Executive insights

Shrey Kohli
Head of Debt Capital Markets
London Stock Exchange

Chair, High-Level Working Group on Green and Sustainability Sukuk

1. What do you consider the most significant achievements of the High Level Working Group on Green and Sustainability Sukuk over the past three years?

Over the past three years, the High Level Working Group on Green and Sustainability Sukuk (HLWG) has made significant progress in promoting sustainable finance through green and sustainability sukuk.

During this period, we have seen a substantial increase in green and sustainability sukuk issuances, which reached nearly $12 billion by the third quarter of 2024. This growth reflects the rising global demand for sustainable investment options and the successful alignment of Islamic finance with ESG principles.

Our efforts have laid a robust foundation for the continued growth and integration of green sukuk into the global financial system, supporting broader climate and sustainability goals. A notable milestone was the introduction of the Guidance on Green, Social, and Sustainability Sukuk, launched by LSEG, ICMA, and IsDB in April this year. This guidance aims to standardise and clarify sustainable sukuk issuance across markets, providing essential direction for issuers by aligning sukuk with the ICMA Principles. This alignment ensures that sukuk are labelled as green, social, or sustainable by adhering to the Green Bond Principles (GBP), Social Bond Principles (SBP), and Sustainability Bond Guidelines (SBG), promoting integrity and consistency in the market.

In collaboration with LSEG Data & Analytics, we launched a series of state of the market reports, detailing a $30 billion to $50 billion market opportunity and providing a structured roadmap with recommendations to build the market. Our capacity-building efforts included working with GEFI and UKIFC who have taken the lead in developing a programme with IsDB for Debt Management Offices (DMOs), equipping them with the necessary skills and knowledge to issue green and sustainability sukuk. Additionally, we launched a knowledge portal featuring case studies to help issuers successfully engage with the market.

2. What was the main challenge you faced in raising the visibility on green and sustainability sukuk, and how did the working group address them?

One of the main challenges we faced in raising the visibility on green and sustainability sukuk was the lack of awareness and understanding among potential issuers. We observed that several active and potential issuers in the sukuk market were unfamiliar with the nuances of structuring green and sustainability financing frameworks, in line with global sustainability principles. and the additional processes such as sourcing a Second Party Opinions, compared to a traditional sukuk.

To address this, we held over 30 meetings, including bilateral and focus groups, to foster collaboration and educate stakeholders. Our participation in major events like COP27 and the G20, alongside the UK Government, Indonesia's Ministry of Finance, the IsDB, and key lead arrangers and issuers, has also contributed to raising awareness and driving market development.

The Guidance on Green, Social, and Sustainability Sukuk also offers practical information through examples, case studies, and best practices, helping issuers understand how to structure and label their sukuk appropriately. It outlines eligible project categories for green, social, and sustainability sukuk, ensuring that the proceeds are used for projects that meet specific environmental or social criteria. By providing a clear framework, the guidance helps develop the green, social, and sustainability sukuk market, attracting more investors and broadening the issuer base. This comprehensive approach helps issuers navigate the complexities of labelling sukuk, ultimately contributing to the growth of sustainable finance.

3. How do you see the landscape for green and sustainability sukuk evolving?

The green and sustainability sukuk market is on the cusp of significant growth. We expect to see further record annual issuance in the foreseeable future as issuers from new jurisdictions enter the market.

With increasing awareness and commitment to green and sustainability agendas along with the onset of policy rate cuts this year, we expect to see new issuers from existing markets. Particularly, we highly anticipate the issuance of sovereign sukuk from established players like the GCC states.

Moreover, we are excited about the increased focus from regulators, who are expected to develop robust regulatory frameworks. These frameworks will guide the issuance process, ensuring alignment with established taxonomies and international standards.

4. What steps are necessary to ensure continued growth and impact of this market?

To ensure the continued growth and impact of the green and sustainability sukuk market, several key steps are essential. First and foremost, raising awareness, particularly among issuers, is crucial. There remains a need for more detailed guidance on the issuance process, which complements the capacity-building programmes we have supported.

Additionally, establishing a robust pipeline of green and sustainability projects is vital. Issuers should be able to identify projects that can be made eligible for green and sustainability financing. Innovative financing structures, such as green or sustainability-linked sukuk, can align investor interests with sustainability goals. By quantifying the environmental, social, and economic benefits of these projects and engaging with relevant stakeholders, we can build support and demonstrate the value of investing in sustainable initiatives. This approach ensures a steady flow of projects eligible for green or sustainability sukuk financing, thereby supporting market growth.

Implementing standards to ensure that green sukuk meet rigorous environmental criteria is also essential. Providing clear and consistent benchmarks for issuers and investors alike will enhance market integrity. Furthermore, enhancing ESG disclosure requirements through regional or international collaboration will help standardise practices and improve transparency. This will not only simplify compliance for issuers but also boost investor confidence in the green sukuk market.

Path to 2030: Key recommendations for green and sustainability sukuk development

The green and sustainability sukuk market has demonstrated remarkable resilience, maintaining double-digit growth despite unfavourable market conditions over the past three years. However, a considerable development journey lies ahead for the market if it is to maintain its growth momentum and leverage increasing investor demand and growth opportunities from SDG funding needs.

This section outlines the key areas for development and recommendations for driving the growth of green and sustainability sukuk in the next five years and enhancing their potential, based on best practices and the experiences of established sukuk markets. Additionally, it highlights notable developments and the initiatives of the HLWG that mark progress in these areas.

Key recommendations for green and sustainability sukuk development

Promote common regional and international standards

- Develop green and sustainability sukuk masterplans or roadmaps
- Introduce specific green and sustainability sukuk guidelines or regulations
- Harmonise taxonomy approaches
- Adapt internationally accepted green and sustainbility standards for sukuk applications
- Standardise ESG disclosure and reporting requirements
- Build issuer awareness and a specialised ESG talent pool

Build capacity with issuers and enhance the wider ecosystem

- **Enable increasing issuance and market depth**
  - Incorporate green and sustainability sukuk within the government funding mix
  - Offer issuers cost-reduction incentives
  - Establish ESG segments within stock exchanges
- **Innovate to broaden green and sustainability sukuk offering**
  - Support issuance of transition sukuk
  - Introduce blue and nature sukuk
  - Use Sukuk-Waqf to fund social finance projects

Expand the investor base beyond traditional sukuk investors

- Offer incentives for investors
- Promote investor awareness and capacity-building
- Expand the investor base beyond traditional sukuk investors

Pillar 1: Promote common regional and international standards, to build a common understanding of the market

Develop green and sustainability sukuk masterplans or roadmaps

The development and success of green and sustainability sukuk markets depends initially on government support. Some OIC countries' national economic and financial sector development plans have set out objectives that address certain aspects of sustainable finance. However, establishing a dedicated, comprehensive masterplan or roadmap focused on developing domestic ESG capital markets, or more specifically green and sustainability sukuk, would further underline governments' commitment.

Islamic financial jurisdictions could develop similar national-level plans taking local context into account. A masterplan for green and sustainability sukuk should identify specific initiatives to encourage more primary market issuance, facilitate liquidity, establish a wider investment pool, and promote foreign investment through the development of the appropriate regulatory frameworks, market infrastructure, capacity-building, and incentivisation programmes.

Introduce specific green and sustainability sukuk guidelines or regulations

Regulatory support is integral to the development and growth of the green and sustainability sukuk market. Regulatory guidelines or frameworks specific to these sukuk should serve as an extension to existing bond or sukuk regulations, and address more specific areas of the issuance process, including the use of proceeds, eligible ESG projects, disclosure and reporting requirements, and external reviews. They would also be beneficial for distinguishing between use of proceeds and the sukuk's underlying assets, to address any ambiguities while identifying eligible ESG projects. It is proposed that regulators develop these guidelines based on international standards and best practices for green and sustainability bonds and sukuk. However, the regulations should be periodically revised so that they remain aligned with international standards and to ensure that procedural bottlenecks do not impede market development.

It is also proposed that green and sustainability sukuk regulations identify and clarify which Shariah standards should apply to the sukuk and mandate their compliance. Clarifying the stage of the issuance process at which a Shariah review should take place would benefit issuers. It is suggested that it takes place before the ESG external review/SPO.

Market development
Several capital market regulators in the GCC, including Qatar, the UAE and Oman, have introduced regulations in the past three years on the issuance of green and sustainability bonds and sukuk that are aligned with international standards. Meanwhile, previously established frameworks in Malaysia, Indonesia, and Pakistan have been updated to reflect recent market and broader regulatory trends.

HLWG outcome
The Guidance on Green, Social, and Sustainability Sukuk launched by LSEG and IsDB, in collaboration with ICMA, provides issuers with essential direction on labelling sukuk as green, social, or sustainable, as it aims to standardise and clarify sustainable sukuk issuance across markets.

Harmonise taxonomy approaches

Developing a global green and sustainability taxonomy that can serve as a 'gold standard' would reduce information and data inconsistency as well as the difficulty of comparison, which in turn would mitigate greenwashing and social-washing risks.

An international green and sustainability sukuk taxonomy could be developed in alignment with internationally accepted taxonomies such as the CBI Taxonomy for green bonds. The taxonomy should be comprehensive, recognising differences between national contexts and priorities to ensure inclusive coverage of projects or sectors that would otherwise be excluded. It is also important for the taxonomy to follow a multi-tier approach, similar to the CBI and ASEAN taxonomies, to ensure clearer labelling of green and sustainability investments.

Adapt internationally accepted green and sustainability standards for sukuk applications

As with taxonomies, multiple green and sustainability compliance standards could raise concerns over compliance risk in the long run as various regulators impose differing local, regional, and international standards.

Existing green and sustainability standards can be expanded to include sukuk-specific provisions that take into consideration the nuances of various Islamic financing structures, following the concept of the ASEAN GBS. It is also suggested that these standards should be supplemented with guidance notes on their application to green and sustainability sukuk. Ideally, this would be a joint initiative with an international green and sustainability standards-setting body such as the ICMA.

Standardise ESG disclosure and reporting requirements

The adoption of the Taskforce on Climate-Related Financial Disclosures (TCFD) framework in core sukuk markets remains at a nascent stage. The framework could be incorporated within green sukuk guidelines among the disclosure and reporting requirements. Its wide international adoption and acceptability would make compliant green sukuk more attractive to international investors.

The standardisation of disclosure and reporting requirements can also help address the challenge of fragmented and inconsistent ESG data and ratings faced by investors, which can result from the use of varying ESG definitions and performance assessment methodologies.

Build issuer awareness and a specialised ESG talent pool

Issuer awareness and capacity-building are two of the main challenges facing the development of green and sustainability bond and sukuk markets. Knowledge gaps still exist around the differences between green and sustainability and traditional sukuk, as well as their advantages and challenges.

To develop a talent pool with in-depth knowledge and expertise of ESG debt markets, regulators could set up training programmes and sponsor ESG certifications and qualifications for their staff. Industry development bodies could also conduct awareness campaigns on ESG investment career development options for market professionals and offer training programmes for various stakeholders.

HLWG outcome

The working group, led by GEFI, has engaged with IsDB on developing and delivering a capacity-building programme for debt management offices in member countries.

HLWG Co-Secretariat GEFI has committed to developing a structured training programme to run over an 12-18 month period tailored to empower Shariah scholars and market stakeholders to better understand conventional sustainable finance frameworks and how they can be applied in a Shariah-compliant context.

Aligning with the wider Global Islamic Finance and SDGs Taskforce, HLWG members have delivered capacity-building workshops on the UN Principles for Responsible Banking (PRB) in Pakistan and Dubai, leading to three new signatories to the PRB. A PRI workshop was also delivered in Dubai as part of the build-up to COP28.

GEFI has also become a member of the Global Capacity Building Coalition (GCBC), which was launched by Glasgow Financial Alliance for Net Zero at COP28. The Coalition aims to support financial institutions to strengthen their internal capabilities to help de-risk decision-making, create favourable conditions for low-carbon projects, and align financial flows with long-term climate goals, accelerating the overall journey to Net Zero. GEFI co-organised GCBC's inaugural Climate Finance Capacity Building Forum in Dubai as part of a wider effort to bring more Islamic financial institutions into the Coalition.

Pillar 2: Build capacity with issuers and enhance the wider ecosystem

Enable increasing issuance and market depth

Incorporate green and sustainability sukuk within the government funding mix. Establishing a dedicated, comprehensive masterplan or roadmap focused on establishing domestic green and sustainability sukuk markets would underline government support for the development and success of these markets. Islamic financial jurisdictions could develop similar national-level plans.

As part of incorporating sustainable finance within national development plans, it is proposed to promote the use of green and sustainability sukuk for financing environmental transition and sustainability projects led by governments or state-owned entities. The resulting green and sustainability sukuk issuances would be the main driver of market growth, increasing market activity and liquidity and encouraging similar issuances from the private sector.

An added benefit to increasing sovereign green and sustainability sukuk is the creation of a yield curve that would help guide the pricing of similar corporate issuances. This in turn would encourage more corporates to issue green and sustainability sukuk.

Market development

Several OIC governments, including most of the GCC states, have recently issued green or sustainability financing frameworks that include green and/or sustainability sukuk as an additional source of funding. GCC countries are large producers of carbon emissions due to their vast oil industries, which is prompting multi-billion-dollar investments in energy-transition projects that can be financed through green and sustainability sukuk.

Offer issuers cost-reduction incentives. Compared to conventional bonds, green and sustainability sukuk involve two additional cost layers: the cost of a Shariah-compliance review and the cost of a green or sustainability SPO. This leaves potential issuers reluctant to venture into the green or sustainability sukuk issuance process.

Cost-reduction incentives have proven to be an effective tool for encouraging corporates to issue sukuk, as evidenced by the Malaysian capital market development model. Such incentives include tax deductions, fee waivers, discounts and grants.

Other incentives that could be offered to issuers include subsidising listing fees for new issuers or waiving regulatory approval fees for returning issuers.

Market development
The UAE's Securities and Commodities Authority (SCA) has undertaken initiatives, aligned with the broader COP28 agenda, to encourage corporates to issue green and sustainability bonds and sukuk to fund environmental and sustainable projects. In June 2023, the SCA announced that corporates looking to list green or sustainability-linked bonds or sukuk in the local market would be exempt from registration fees for that year, and later extended to the end of 2024.

Establish ESG segments within stock exchanges. Stock exchanges that are popular with sukuk issuers - such as Bursa Malaysia, Nasdaq Dubai or Tadawul – should establish green, sustainability or ESG segments, either as parallel markets or within their main markets. Dedicated green or ESG segments of stock exchanges offer a win-win opportunity for issuers and investors alike.

Such platforms offer issuers access to substantial liquidity derived from institutional investor capital. They also vet potential listings based on robust ESG standards, disclosures and sustainability reporting, which enhances issuers' profiles and boosts their visibility to investors. This vetting process also offers investors greater transparency and assurance of ESG compliance at both the issuer and sukuk levels.

Innovate to broaden green and sustainability sukuk offering

Support issuance of transition sukuk. Transition sukuk can play an important role in facilitating the transition of corporates in carbon-intensive industries, including oil and gas, iron and steel, chemicals, aviation, and shipping.

There is room for growth in transition sukuk, but this will require greater transparency on the use of proceeds and dedicated standards so that they gain greater acceptance by investors for mitigating greenwashing cases, where issuances by heavily emitting corporates could be labelled `green' because `transition' is not clearly defined.

Collaborative efforts between market stakeholders to clearly define transition bonds and sukuk and introduce specific disclosure and reporting requirements at an international level would greatly boost investor confidence in these bonds.

Introduce blue and nature sukuk. An increased focus on ecosystem restoration and preservation has resulted in the development of two niche segments in the ESG bond market: blue bonds and nature bonds. Sukuk issuers, particularly sovereigns that have set national priorities for marine conservation and restoration, could emulate and leverage blue sukuk to expand their green and sustainability sukuk offerings, and perhaps reduce borrowing costs in the process.

Nature bonds and sukuk, a concept still under development, have been proposed to link issuances to biodiversity targets and carbon emissions, whereby borrowing costs can be reduced if quantified targets are met. Issuers might also be able to pay back debt using carbon credits.

OIC jurisdictions such as Pakistan, Indonesia, and Malaysia could also leverage nature sukuk to finance biodiversity initiatives if dedicated guidelines or frameworks are developed.

HLWG outcome
The HLWG has developed a long-term strategic plan to examine how sukuk could be utilised in more strategic financing areas, including blue and nature financing, with the view that the next phase of the market will guarantee financing that is based on biodiversity, nature, and the generation of carbon credits.

Use Sukuk-Waqf to fund social finance projects. Green and sustainability sukuk have the potential to fund Islamic social finance initiatives, and Waqf projects aligned with the SDGs in particular. This can be achieved using the 'Sukuk-Waqf' model, whereby sukuk proceeds are used to finance pre-screened Waqf projects complying with green, sustainability or social bond principles.

The main difference between these and other sustainability sukuk lies in investors' objectives. In theory, investors would not be driven by profit, rather by serving the public interest. On this basis, it is suggested this type of sukuk mimics the structure of a social impact bond, where investor pay-off is contingent on the performance of the underlying project against pre-defined KPIs.

Pillar 3: Expand the investor base beyond traditional sukuk investors

Offer incentives for investors

As with issuers, investors can be encouraged to invest in green and sustainability sukuk through cost-reduction incentives. While these may not be necessary in light of the surging demand for ESG investments, they may be influential in jurisdictions where ESG criteria have not yet been incorporated in investment mandates.

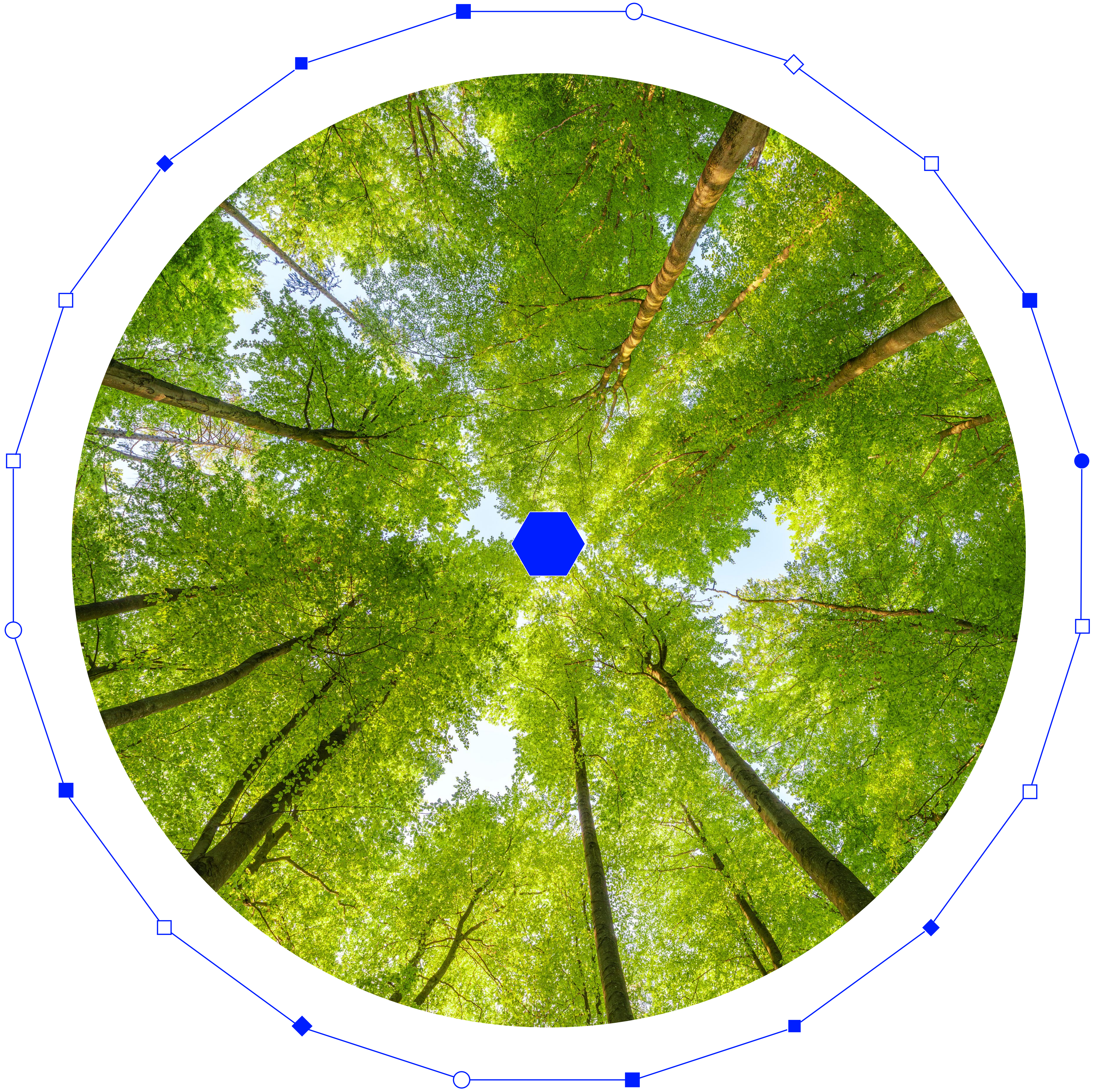
Regulators could offer investors tax or Zakat exemptions on income from profit payments, where applicable. Alternatively, exemption from, or discounts on, stamp duty, trading commissions or transaction fees could facilitate greater activity and liquidity for listed green and sustainability sukuk.

Promote investor awareness and capacity-building

The high demand for ESG investments is mainly driven by institutional investors from developed markets such as the US and Europe, where most investment mandates have incorporated ESG guidelines. However, in most sukuk markets, ESG investing is still at an early phase, partly due to a lack of awareness among traditional investors.

It is proposed that regulators and industry development bodies launch investor education and awareness programmes providing educational materials and workshops, and support market-led initiatives for green and sustainability sukuk investor engagement and training. Engaging investors earlier in the investment process by involving them in the development of green and sustainable infrastructure investment pipelines can facilitate more green and sustainability sukuk investment.

It is also proposed to encourage institutional investors to pursue ESG capacity-building within their investment teams, and to build their knowledge of ESG investments, particularly fixed-income instruments, as well as best practices for ESG investment processes. A number of ESG certifications and qualifications are now available to investment professionals worldwide, which can help them develop knowledge and insights into ESG asset classes, investment strategies, and risk management.



HLWG outcome
The HLWG published a “Green and Sustainability Sukuk Report” in 2022 and its subsequent annual updates, which have informed and guided the HLWG’s actions between 2022 and 2024. The report series provides insights on the green and sustainability sukuk market and broader ecosystem and highlights the key areas for its growth and development.

As part of Indonesia’s G20 presidency, the HLWG co-hosted an official virtual event to promote green and sustainability sukuk. HLWG members have participated in events showcasing green and sustainability sukuk in the Blue Zone at COP27, COP28 and COP29.

The HLWG organised an Islamic Finance & the SDGs Virtual Summit to coincide with the UN General Assembly in September 2021. The Summit included a discussion between the Indonesian Government and UNDP on “How can sukuk - Islamic bonds - deliver capital towards the SDGs?”?

The HLWG has also developed a beta version of a knowledge portal. The online platform will provide comprehensive information on green and sustainability sukuk, including case studies and reports, as well as contributions from issuers.

Expand investor base beyond traditional sukuk investors

Demand for ESG investments in domestic OIC markets has not gathered pace. Meanwhile, there is high demand for such investments, mainly driven by agnostic institutional investors from developed markets such as Europe and the US. Many of these investors follow mandates that include ESG considerations and they are putting pressure on issuers in emerging markets to broaden their green and sustainability investment offerings.

Tapping this demand can contribute to the growth of green and sustainability sukuk issuances, as well as attract more foreign capital flows into domestic markets that can fund environmental and sustainable projects and initiatives.

Greater emphasis can be placed on the ESG characteristics of green and sustainability sukuk when promoting them to investors in developed markets, many of whom follow mandates that include ESG criteria, and put pressure on issuers in emerging markets to offer more ESG instruments. Tapping this demand can contribute to the growth of green and sustainability sukuk issuance and attract more foreign capital flows into domestic markets that can fund environmental and sustainable projects and initiatives.

HLWG outcome
The HLWG conducted an ESG Sukuk Survey 2024 which sought to understand the dynamics of the green and sustainability sukuk market. As part of the research, the HLWG reached out to conventional investors with and without Shariah-compliant funds.

HLWG Co-Secretariat UKIFC recently launched an Islamic Sustainable Investing Platform inspired and framed by the Islamic concept of “Tayyib” (pure, wholesome, and impactful). This seeks to reflect Shariah compliance coupled with an enhanced focus on active sustainable (also referred to as ESG/Responsible) investing framed by Islamic values. The platform has been promoted as a best-practice approach to conventional investors who are considering developing new Shariah-compliant funds or seeking Shariah compliance for existing funds.

At Ethical Finance ASEAN 2024, which attracted over 1,200 registrations from practitioners across the globe, the HLWG chair and select members participated in a fireside chat discussing the role of green sukuk for climate action. This included an update on the ICMA practitioner guidelines.

In September, HLWG Chair, LSEG, hosted a round table with PRI in Dubai looking at Islamic green finance. The session bought together a panel of experts who discussed developments in 2024 and the potential in the Middle East region, while addressing future challenges to continue growth and highlighting the need for more innovative products.

APPENDIX: CASE STUDIES

Warba Bank marks Kuwait's entry into sustainable debt markets

Issuance details	
Company	Warba Sukuk
Rating (Fitch)	A
Sector	Banking
Market	ISM - London Stock Exchange

Transaction details	
Issue date	10 July, 2024
Issue size	$500 million
Coupon	5.351%
Maturity	5 years

- Warba Bank issued $500 million in sustainability sukuk, marking a major step in the bank's $2 billion sukuk issuance programme. This was Kuwait's first issuance of green or sustainability sukuk.
- Proceeds will finance or refinance projects including those focused on renewable energy, sustainable water management, and community development that meet environmental, social, and institutional governance standards.
- The transaction was finally priced at a profit rate/yield of 5.351% per annum and tightened to a final spread of 105bps basis over US Treasurys.
- Demand was robust, with the order book peaking at $1.8 billion – 3.6 times oversubscribed.
- Emirates NBD Capital, HSBC, and Standard Chartered Bank acted as joint global coordinators to the transaction. Warba Bank, the Islamic Corporation for the Development of the Private Sector, Arab Banking Corp., Al Rayan Investment, Boubyan Bank, Dubai Islamic Bank, KFH Capital Investment Company, and Mashreqbank acted as lead managers and bookrunners.

QIIB issues $500 million "Oryx" sustainability sukuk

Issuance details	
Company	QIIB Senior Oryx
Rating (Fitch)	A2, A
Sector	Banking
Market	ISM - London Stock Exchange

Transaction details	
Issue date	24 January, 2024
Issue size	$500 million
Coupon	5.247%
Maturity	5 years

- QIIB issued the $500 million sustainability 'Oryx' sukuk for a period of five years as part of the bank's $2 billion sukuk programme.
- The issue was priced at a spread of 120 basis points above the five-year US Treasury rate, with a final yield of 5.247% annually.
- The issue was oversubscribed more than eight times, receiving bids in excess of $4 billion.
- The sustainability sukuk attracted bids from more than 120 investors from the GCC, the Middle East, Europe, Asia and America. More than 55% of the investors are from outside the GCC and Middle East.
- Standard Chartered Bank acted as global coordinator for the issuance, along with Al Rayan Investment (Masraf Al Rayan Group), Dukhan Bank, Emirates NBD Capital, KFH Capital, Mashreqbank, and the Islamic Corporation for the Development of the Private Sector and QNB Capital acting as joint bookrunners and lead managers.

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CROSSING BORDERS

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UKIFC

LSEG DATA & ANALYTICS