Development of Sukuk Negara
(Success Story of Indonesia Sovereign Sukuk)

Directorate of Islamic Financing
Directorate General of Budget Financing and Risk Management
Ministry of Finance

The 10th Meeting of COMCEC Financial Cooperation Working Group
Ankara, Turki
28-29 March 2018
AGENDA

Section 1  Overview of Indonesia Sovereign Sukuk (Sukuk Negara)
Section 2  Infrastructures for Sukuk Negara Issuance
Section 3  Sukuk Negara: Prospects and Challenges
Milestone of Sukuk Negara

- Enactment of GoI Sukuk Law
- Debut GoI Sukuk issuances:
  - Islamic Fixed Rate (IFR)
  - Retail Sukuk (SR)
  - Global Sukuk (SNI)
  - Hajj Fund Sukuk (SDHI)
- Debut GoI Sukuk auction in domestic market

2008 - 2010

- Debut issuance of Islamic Treasury Bills (SPN-S)
- Debut auction for Project-Based-Sukuk (PBS)
- Green Shoe Option (GSO) auction
- Debut issuance of Project Financing Sukuk (earmarked)

2011 - 2013

- Global Sukuk issuance under Wakala structure
- Debut issuance of Savings Sukuk
- The largest GoI single-tranche global sukuk issuance (USD2 bio)
- 1st Global Green Sukuk issuance by Sovereign

2014 - 2018

- Total issuance = IDR 848.14 trillion eq. USD63.2 billion (from 2008 to March 8, 2018)
- Total outstanding = IDR 589.75 trillion eq. USD44 billion (as of March 8, 2018)
- Denomination = IDR and USD
- Issuance methods = auction, book building, and private placement

Sukuk Negara Issuance: 2008 – March 8, 2018

Composition of Outstanding by Currency

<table>
<thead>
<tr>
<th>Currency</th>
<th>Issuance</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>IDR</td>
<td>IDR376.25 Trillion</td>
<td>63.8%</td>
</tr>
<tr>
<td>USD</td>
<td>IDR213.5 Trillion</td>
<td>36.2%</td>
</tr>
</tbody>
</table>

Composition of Outstanding by Tenor

<table>
<thead>
<tr>
<th>Tenor</th>
<th>Issuance</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>0 – 5 years</td>
<td>IDR372.15 Trillion</td>
<td>63.1%</td>
</tr>
<tr>
<td>6 – 10 years</td>
<td>IDR139.11 Trillion</td>
<td>23.6%</td>
</tr>
<tr>
<td>&gt;10 years</td>
<td>IDR78.49 Trillion</td>
<td>13.3%</td>
</tr>
</tbody>
</table>

Source: Ministry of Finance, Republic of Indonesia
1USD = IDR13,400
Since 2012, establishing an Islamic Global Medium Term Notes (GMTN) for more flexible issuance in terms of timing, size amount, and product.

Pioneered continued innovation in Global Sukuk Structuring through Wakala sukuk structure.

Considered as the largest international sovereign sukuk issuer with total issuance of USD16.15 billion.

Demonstrates the ROI’s commitment to enhance its Islamic finance credentials and to continue setting liquid and on-the-run benchmarks in the global Sukuk arena.
The First Sovereign Global Green Sukuk

On February 22, 2018, the Republic of Indonesia successfully priced an international sukuk offering totaling USD3 bn, including its debut offering in green format.

Summary Terms of Offering

<table>
<thead>
<tr>
<th>Obligor</th>
<th>The Government of the Republic of Indonesia, represented by the Ministry of Finance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Issuer</td>
<td>Perusahaan Penerbit SBSN Indonesia III</td>
</tr>
<tr>
<td>Issuer Rating</td>
<td>Baa3 Moody's (Positive) / BBB-S&amp;P (Stable) / BBB Fitch (Stable)</td>
</tr>
<tr>
<td>Exp. Issue Rating</td>
<td>Baa3 Moody's / BBB-S&amp;P / BBB-Fitch</td>
</tr>
<tr>
<td>Instrument</td>
<td>USD Wakala Trust Certificates (&quot;Sukuk&quot;), issued under a USD25 bn Trust Certificate Programme</td>
</tr>
<tr>
<td>Format. Status</td>
<td>144A / RegS registered, senior unsecured</td>
</tr>
<tr>
<td>Aggregate Size</td>
<td>USD3,000 mm</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Maturity</th>
<th>5-year Green Global Sukuk</th>
<th>10-year Regular Global Sukuk</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tranche Size</td>
<td>USD1,250 mm</td>
<td>USD1,750 mm</td>
</tr>
<tr>
<td>Profit Rate</td>
<td>3.750% p.a. (30/360)</td>
<td>4.400% p.a. (30/360)</td>
</tr>
<tr>
<td>Reoffer Price / Yield</td>
<td>100.000 / 3.750%</td>
<td>100.000 / 4.400%</td>
</tr>
<tr>
<td>UST Benchmark (Price / Yield)</td>
<td>2.375%/01/31/23 (98-224%/2.655%)</td>
<td>2.750%/02/15/28 (98-16+%/2.923%)</td>
</tr>
<tr>
<td>Reoffer Spread</td>
<td>+109.5 bp</td>
<td>+147.7 bp</td>
</tr>
<tr>
<td>Use of Proceeds</td>
<td>General financing requirements in line with the Green Bond and Green Sukuk Framework</td>
<td></td>
</tr>
<tr>
<td>External Reviewer</td>
<td>CICERO second party opinion</td>
<td></td>
</tr>
<tr>
<td>Other Terms</td>
<td>USD200k/1k denominations, English and Indonesia law, Singapore and NASDAQ Dubai listing</td>
<td></td>
</tr>
<tr>
<td>Joint Lead Managers</td>
<td>Abu Dhabi Islamic Bank PISC, CIMB Investment Bank Berhad, Citigroup Global Markets Inc., Dubai Islamic Bank PISC, The Hongkong and Shanghai Banking Corporation Limited</td>
<td></td>
</tr>
</tbody>
</table>

Transaction Highlights

- First-ever green sukuk offering by any sovereign globally
- First USD sovereign green offering, in either sukuk or conventional formats
- Accessed a window of relative stability without any competing supply for aggregate size of USD3 bn, which remains to be the largest sukuk offering by a non-GCC issuer to-date
- Maximized green structure and full investment grade ratings to set all-time low spreads to U.S. Treasury for any sukuk offering by the Republic of Indonesia
- Set the flattest curve between any 5- and 10-year sukuk offering by the Republic, at only 65 bp
- Over USD7 bn of demand at pricing, featuring sponsorship from investors of the highest quality, green focused funds and sovereign-related entities inclusive

Demand and Allocation Statistics

<table>
<thead>
<tr>
<th>5-year Green Global Sukuk</th>
<th>10-year Regular Global Sukuk</th>
</tr>
</thead>
<tbody>
<tr>
<td>Indications / Book Cover</td>
<td>USD3,000 mn / 2.4x</td>
</tr>
<tr>
<td>Allocations</td>
<td>USD1,250 mn</td>
</tr>
<tr>
<td>Number of Accounts</td>
<td>145</td>
</tr>
<tr>
<td>Allocations by Geography</td>
<td></td>
</tr>
<tr>
<td>Islamic</td>
<td>10%</td>
</tr>
<tr>
<td>Asia</td>
<td>18%</td>
</tr>
<tr>
<td>EU</td>
<td>25%</td>
</tr>
<tr>
<td>US</td>
<td>22%</td>
</tr>
<tr>
<td>Indonesia</td>
<td>32%</td>
</tr>
<tr>
<td>Allocation by Type</td>
<td></td>
</tr>
<tr>
<td>Islamic</td>
<td>29%</td>
</tr>
<tr>
<td>Asset Manager / Fund Manager</td>
<td>10%</td>
</tr>
<tr>
<td>Pension Fund / Insurance</td>
<td>71%</td>
</tr>
<tr>
<td>Private Bank</td>
<td>6%</td>
</tr>
<tr>
<td>Non Green</td>
<td>1%</td>
</tr>
<tr>
<td>Bank</td>
<td>47%</td>
</tr>
<tr>
<td>SWF / Central Bank</td>
<td></td>
</tr>
<tr>
<td>Other Green</td>
<td></td>
</tr>
<tr>
<td>Green</td>
<td></td>
</tr>
</tbody>
</table>
Incoming bids of Sukuk Negara auction has increased significantly during the last 3 years.
On-the-run series are Islamic Treasury Bill (SPN-S) and Project Based Sukuk (PBS).
During 2017, total incoming bids has reached IDR374.23 trillion (eq. USD27.9 billion) with total awarded bids of IDR135.14 trillion (eq. USD10.08 billion).
Sukuk Negara secondary market performance is increasing steadily over the years. Average volume and frequency in Mar-18: Rp 1.97 trillion (eq. USD147 million), 87 times. Average volume and frequency in 2017: Rp 1.73 trillion (USD129.1 billion), 111 times.
Retail Sukuk for Promoting Financial Inclusion

- For Indonesia citizens
- Min. purchase: IDR 5 million (eq. USD370)
- Max. purchase: IDR 5 billion (eq. USD370,000)
- Fixed coupon, monthly payment
- 3 years tenor
- Tradable
- Structure: Ijarah Asset to be Leased
- Through Selling Agents

Purchased by individual investors at 34 Provinces (case study Retail Sukuk SR-010)

<table>
<thead>
<tr>
<th>Region</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Western (Excl. Jakarta)</td>
<td>56.9%</td>
</tr>
<tr>
<td>Jakarta</td>
<td>32%</td>
</tr>
<tr>
<td>Middle</td>
<td>10.5%</td>
</tr>
<tr>
<td>East</td>
<td>0.6%</td>
</tr>
</tbody>
</table>

1USD = IDR13,400

10 Retail Sukuk Series has been issued (2009-2018)

243,364 Total Retail Sukuk Investors

IDR 144.7 Trillion Total Issuance of Retail Sukuk (2009-2018)

IDR 67.5 Trillion Outstanding of Retail Sukuk (March 2018)

Investors come from various professions (case study Retail Sukuk SR-010)

- 33% Professional, Employee
- 30% Art worker, Student, Retiree
- 17% entrepreneur
- 12% housewife
- 8% Civil servants, TNI / Polri

Purchased by individual investors at 34 Provinces (case study Retail Sukuk SR-010)
Hajj Fund Sukuk

- **Series:** SDHI (Sukuk Dana Haji Indonesia)
- **Structure:** Ijarah Al-khadamat. Sukuk represent ownership of described future services
- **Underlying asset:** Hajj services flight, housing, catering.
- **Issuer:** Perusahaan Penerbit SBSN Indonesia

**IDR 62.17 Trillion** (eq. USD4.6 billion)

Total accumulated issuance (2009 - March 2018)

**IDR 36.70 Trillion** (eq. USD2.7 billion)

Outstanding as of March 8, 2018
Financing Infrastructure Project Through Sukuk Negara

2013

**IDR800 Billion**

- Double Track Railways (Cirebon – Kroya route in middle Java)

2014

**IDR1.57 Trillion**

- Double Track railways (Cirebon – Kroya); Double-Double Track railways (Manggarai – Bekasi)
- Revitalization and Development of Hajj Dormitory

2015

**IDR7.13 Trillion**

- Double Track railways (Cirebon – Kroya, Martapura – Baturaja); Double-Double Track railways (Manggarai – Bekasi); Elevated Track railways (Medan – Kualanamu)
- Roads and bridges (Sumatera, Jawa, NTB, Kalimantan, Sulawesi, Maluku & Papua).
- Building and facilities development of the State Islamic Higher Education.
Financing Infrastructure Project Through Sukuk Negara

2016

IDR13.67 Trillion

- Double Track, Double-Double Track & Elevated Track Railways (Jabodetabek, Central Java, East Java & Sumatera).
- Roads, flyover, underpass, tunnel, bridges development (Sumatera, Java, NTB, Kalimantan, Sulawesi, Maluku & Papua).

2017

IDR16.76 Trillion

- Elevated & Double Track Railways (Jabodetabek, Central Java, East Java, Sumatera & Sulawesi).
- Roads, flyover/underpass/tunnel & bridges development (Sumatera, Java, NTB, Kalimantan, Sulawesi, Maluku & Papua).
- Flood and lava control, management of urban main drainage and coastline security, management of dams, embung, and other water containers buildings, raw water supply and management.
<table>
<thead>
<tr>
<th>Section 1</th>
<th>Overview of Indonesia Sovereign Sukuk (Sukuk Negara)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Section 2</td>
<td>Infrastructures for Sukuk Negara Issuance</td>
</tr>
<tr>
<td>Section 3</td>
<td>Sukuk Negara: Prospects and Challenges</td>
</tr>
</tbody>
</table>
Factors Supporting Sukuk Negara Development

Legal infrastructure provides certainty:
- Legal basis of issuance
- Special Purpose Vehicle
- Underlying assets
- Tax neutrality

Issuance methods:
- Auction
- Bookbuilding
- Private placement

Sukuk Negara

In compliance with Sharia principles:
- 6 Fatwa & several Sharia endorsement
- 4 sukuk structure applied:
  - Ijarah Sale and Lease Back
  - Ijarah Asset to be Leased
  - Ijarah Al Khadamat
  - Wakalah

Variety of Instruments

Instruments for various investor:
- Islamic Fixed Rate (IFR)
- Project Based Sukuk (PBS)
- Hajj Fund Sukuk (SDHI)
- Indonesia Global Sukuk (SNI)
- Islamic Treasury Bills (SPN-S)
- Retail Sukuk (SR)
- Savings Sukuk (ST)
Legal Basis

Legal basis of Sukuk Negara issuance (Law No.19/2008):

- Provide mandate to the government for issuing Sukuk Negara
- Establishment of the Special Purpose Vehicle
- Utilize state-owned assets and government projects as underlying

Legal certainty for investors:

- Principal amount and coupon payment are guaranteed by the GoI as Obligor
- Comply with sharia principles

Tax treatment parri passu with Government Debt Securities (Bonds)
## Special Purpose Vehicle (SPV)

<table>
<thead>
<tr>
<th>Legal Form</th>
<th>Role in Sukuk Issuance</th>
<th>Characteristics</th>
</tr>
</thead>
</table>
| Special Purpose Vehicle (SPV) is an independent legal entity incorporated solely for the purpose of issuing bond/sukuk. SPV can be established in the form of a corporation, trust, partnership, limited liability company, subsidiary, or a separate entity. | - Issuer of sukuk.  
- Acting as Trustee.  
- Acting as Counterpart in transactions of underlying assets.  
- Appoint other parties as co-trustee to help carry out the tasks as trustee. | - Small capital, comes from sponsoring company that is 100% owned SPV.  
- Established in the country or tax heaven country, for a specific purpose;  
- Not having management or employee (ex-officio)  
- Bankruptcy remote  
- Off-balance sheet  
- Single SPV vs. one-off SPV. |

### Perusahaan Penerbit SBSN

- Perusahaan Penerbit SBSN (Sukuk Negara issuing company) is the SPV in Sukuk Negara issuance.
- The issuance of Sukuk Negara may be conducted directly by the Government or by the Sukuk Negara Issuing Company/Perusahaan Penerbit SBSN (act as SPV) [Law no 19/2008 article 6].
Underlying Assets of Sukuk Negara

1. State Owned Assets
   - Lands and buildings
   - Purchased or obtained under the state budget or other legitimate sources
   - Subject to the parliament approval

2. Financing Project/ Government Activities
   - Government activities allocated in state budget:
     - Infrastructure Projects
     - Procurement of Goods
     - Services

3. Hajj Service Procurement
   - Land and air transportation
   - Accommodation (housing)
   - Logistic (catering, health, etc)

Beneficial Right
- The utilization of SOE as underlying asset is within the framework of beneficial right/ownership
- The Beneficial Right is the right to own and to obtain the full right to the usage of an asset without requiring registration for such ownership and right. (Law no 19/2008 article 6).

Terms/Condition of State Owned Asset /SOA (as underlying asset):
- have economic value
- in good condition/feasible
- listed in the Document Administration
- not the main weaponry system
- not in dispute
- not associated with symbols of statehood
- not being used as another underlying asset
Tax Neutrality

Underlying Asset Transaction

- Tax is a hidden cost in any funding structure, potential tax liability and tax inefficiencies will affect any financing structure.
- In Islamic Finance, due to the underlying asset within each transaction, tax neutrality as well as the tax treatment of profits need to be resolved.

IJARAH SUKUK:

- Due to the additional underlying asset transactions required for Syariah financing, tax neutrality rules would mean that the underlying transactions would be ignored for tax purposes.
- This will mean that the Sukuk will be treated to be similar as any conventional bonds so that it is not treated worse off.
Fatwa & Sharia Endorsement

Obtained from National Sharia Board – Indonesian Council of Ulama

Fatwa:
- Number 69/2008 on Sovereign Sharia Securities
- Number 70/2008 on Issuing Methods of Sovereign Sharia Securities
- Number 71/2008 on Sale and Lease Back
- Number 72/2008 on Sovereign Sharia Securities Ijarah Sale and Lease Back
- Number 76/2010 on Sovereign Sharia Securities Ijarah Asset to be Leased
- Number 95/2014 on Sovereign Sharia Securities Wakalah

Provision:
Number 01 /DSN-MUI/III/2012 on Criteria of Project which Comply with Sharia Principles

Sharia Endorsement:
Sharia endorsement on every Sukuk Negara issuance
Instrument Development

1. **IFR**
   - Sukuk Negara debut, issued in Aug 2008 by bookbuilding method.
   - Underlying assets: State-Owned Assets.
   - Regular issuance through auction since 2009 until 2012.

2. **SR**
   - For retail Indonesian investors.
   - Medium term tenors (3-3.5 years).
   - Bookbuilding method
   - Predetermined coupon, tradable in secondary market
   - Min/max order: IDR5 million/ IDR5 billion for each individual.

3. **ST**
   - For retail Indonesian investors.
   - Medium term tenors (2 years).
   - Bookbuilding method
   - Predetermined coupon, non-tradable
   - Min/max order: IDR2 million/ IDR5 billion for each individual.

4. **SNI**
   - Foreign currency denominated Sukuk, issued in international capital market (Global Sukuk).
   - To diversify investor base, specially to tap Middle East and Islamic investors.

5. **SDHI**
   - Private placement transaction with Ministry of Religious Affair for Hajj fund investment.
   - Underlying assets: Hajj services.
   - First time issued in May 2009.
   - Non tradable securities.

6. **SPN-S**
   - Islamic Treasury Bills.
   - 6-month tenor.
   - Discounted basis.
   - Regular auction since August 2011.

6. **PBS**
   - Project Based Sukuk.
   - Underlying assets: State Budget projects.
   - Mid to long term tenors.
   - Issued regularly since 2012.
**Issuance Program**

### Domestic Market

#### Auction
- IFR, Islamic T-Bills, PBS.
- Conducted regularly twice a month based on annual calendar of issuance.
- Auction participants/Dealers.

#### Bookbuilding
- Conducted for Retail Sukuk & Savings Sukuk.
- By appointing selling agents (banks & securities companies).

#### Private Placement
- For SDHI series (Hajj Fund Sukuk) and other series based on market demand.
- Bilateral agreement.

### International Market

#### Bookbuilding
- For global sukuk (USD denominated / SNI series)
- 144A/Reg-S issue format
- By appointing joint lead managers (book runners)
AGENDA

Section 1  Overview of Indonesia Sovereign Sukuk (Sukuk Negara)

Section 2  Infrastructures for Sukuk Negara Issuance

Section 3  Sukuk Negara: Prospects and Challenges
## Tax Neutrality

- Globally acceptable Sukuk structures, namely Ijara and Wakala, typically involve the transfer of beneficial interest in assets such as land and buildings.
- Such transfers tend to attract taxes and/or stamp duty under national land laws/regulations.
- To provide a level-playing field for Sukuk transactions, such transfers should be viewed as part of financing and therefore exempted from taxes and/or stamp duty that would otherwise be applicable.

## Cost Neutrality

- Having a level-playing field from a tax angle, so that a Sukuk issuer does not have to bear extra costs when compared to issuing conventional bonds.
- Transaction advisers, including legal, tax and accounting advisors, do not charge a premium for advising on Sukuk transactions - this would take place when Sukuk transactions become a norm in particular jurisdictions and advisors become familiar with the workings and documentation involved.

## Legal and Regulatory Frameworks

- The existence of frameworks that recognize and facilitate the issuance of Sukuk from a local perspective.
- This should extend to remedies available for Sukuk investors in the event of default, which should be as comprehensive as that available for investors in conventional bonds.

Source: CIMB Islamic
Apart from financing government spending, governments in nascent Sukuk markets have issued Sukuk to establish a benchmark for future issuances.

The issuance of the Hong Kong, UK and Luxembourg debut sovereign Sukuk created new benchmarks and would help develop their domestic Sukuk markets. Sovereign and quasi-sovereign issuers are expected to drive growth in the global sukuk market.

As the regulatory, tax and Shariah frameworks are assimilated, the market becomes active with sovereign issuances. Corporate issuance are likely to emerge soon after.

The challenge moving forward is to extend the success of sovereign issuances to corporate issuances. Government support in providing a level-playing field and sovereign issuances will attract corporate participants into the market.

Sukuk can also provide ‘diversification’ opportunities for investors. Sukuk appeal to both sets of investors – the conventional fixed-income investors, as well as the vast Islamic financial community in search of “quality” papers.

Top-down Approach = THE Preferred Approach

Source: CIMB Islamic
### Prospects

- Faster Islamic financial institutions growth.
- Larger potential investors: Islamic and conventional.
- Limited of sukuk supply, overwhelming demands.
- Authorities strong support: Establishment of National Committee for Islamic Finance.
- Projects financing sukuk: preparation and availability is being improved.

### Challenges

- Ongoing market development, and relatively less liquid secondary market.
- Buy and hold perspective.
- Higher yield expectation and price discovery mechanism.
- Market infrastructure development.
- Diversification of underlying assets.
Wassalamu’alaikum Wr Wb

Thank You

Inquiries, Information and Suggestions:

Directorate of Islamic Financing
Directorate General of Budget Financing and Risk Management
Ministry of Finance of the Republic of Indonesia

Website : www.djp.pr.kemenkeu.go.id
Telephone : (+6221) 351-6296, Fax. (+6221) 351-0728
E-mail : webmaster@djp.pr.kemenkeu.go.id
          sukuknegara@kemenkeu.go.id