

# Islamic finance - a specialty of Western banks!

## GCC institutions still fringe players in funding of oil and gas industry

With international lenders dominating GCC oil and gas funding, what role is there for regional banks' Islamic finance propositions? **Mazen Khoury** (right), Senior Manager at Middle East Strategy Advisors, a UAE-based strategy consultancy, argues regional bankers need to articulate an Islamic finance value proposition to lower transaction costs - made up mostly of lawyer and due diligence fees - and credibly compete in the regional long-term funding arena.

**RECENT OIL** price increases have translated into massive revenue streams but not yet in investment into new productive oil and gas capacity.

Most international oil companies have used proceeds to buy back shares while national oil companies have handed back revenue to governments to wipe off accumulated budget deficits.

Project finance and an increased call on long-term structured funding solutions have resurfaced, given the magnitude of the investments and the scale effects these transactions can benefit from. Key long-term structured funding sources are large European and Japanese financial institutions - with three main attributes:

1. Demonstrated project structuring skills and capabilities, allowing for lower average transaction costs.
2. Political clout to warrant alliances with oil and gas majors and Western equipment suppliers when negotiating new projects with GCC sponsor governments.
3. Sufficient scale supporting underwriting capabilities.

GCC banks are still fringe players in the business. Often, they are relegated to the role

of participants, effectively shut out from margins accruing to the more established players of the global project finance industry. Local banks are left scrambling for short-term finance deals and bridge loans.

There are recent signs that times are changing, however.

In July, Dolphin Energy announced that 25 banks will provide conventional and Islamic project finance totaling \$3.45 billion. Of this, \$1 billion is an Islamic Istithna'a instrument which was led by five banks including two regional institutions.

Dolphin Energy pro-actively approached Arab bankers with lead banks making a special point to invite Islamic investors from across the Middle East and Asia to join the financing.

This allowed banks to benefit from supportive funding terms while helping build a track record of key local bankers with the advent of innovative Islamic instruments.

There are considerable challenges ahead for GCC local banks which while being backed by substantial market liquidity still must actively seek capital-intensive investment or loan propositions. In order to place deals, regional bankers are



presently driven to decrease the rigour with which they will assess projects' risk / reward profiles under normal circumstances.

According to our interviews with regional oil company chief financial officers and Islamic financial institutions, the key to GCC bankers placing Islamic finance instruments and effectively funding the region's investment in oil and gas productive assets is that they need to build size, establish differentiated products, and articulate a simple well defined value proposition.

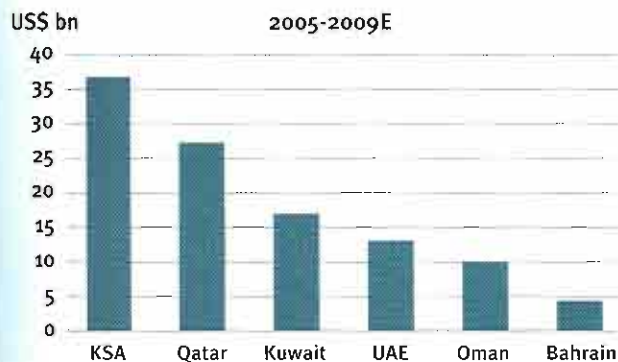
To secure a more sizeable share of the oil and gas funding market, regional banks should focus on both improving Islamic offerings as well as targeting conventional lending. In both regards key success factors include:

- Clarifying the legal and regulatory uncertainties currently prevailing in the fields of Islamic structured finance: the creation of Shariah compliance boards by key players, and the proactive involvement of

theologians in affirming compliance standards

- Devising structured products that are not currently offered by large international players: including increased use of securitisation techniques, and arranging more complex Sukuks, or Islamic bonds
- Pursuing ways to introduce Islamic finance products as self-contained tranches of larger conventional project finance, as is the case with Dolphin Energy
- Targeting sector specialities and seeking to replicate to achieve cost-effectiveness such as in the LNG market, funding refining facilities and production of oil fields in areas such as Yemen, Libya or Oman
- Seeking long-term alliances with Western project promoters and suppliers, to influence funding decisions at the beginning of the finance structuring plan
- Partnering with smaller oil and gas players seeking entry into the regional oil and gas arena by providing

## GCC Oil and Gas infrastructure investment needs



Source: Standard Chartered Bank

customised funding solutions

- Effectively lobbying Western European and US export credit guarantee agencies to cover Islamic-compliant project finance terms, rendering the entire market more attractive to participants
- Leveraging relationships with shareholders, often high net worth individuals who demand Islamic solutions and are often also key political sponsors or medium scale oil and gas projects.

Regional banks are clearly on the scene and advancing along many of these fronts; however, meaningful progress is likely to continue to come from champions willing to aggressively drive the emergence of local banking

expertise and define the value of Islamic finance for oil and gas structured finance.

*Mazen Khoury participated in structuring Qatar LNG project funding working with the Societe Generale group in Paris. He also conducted a financial performance improvement project for a large OPCO in Abu Dhabi. He previously worked with global consultancies such as Cap Gemini, Diamondcluster and Kaiser in Europe and Middle East.*

*Middle East Strategy Advisors provides services in consulting, interim management and investment advice. The company has offices in Abu Dhabi, Dubai and Muscat. For more details visit*

[www.mesadvisors.com](http://www.mesadvisors.com)

## GCC oil and gas project finance deals, May 04 – April 05

Arranger	Number of deals	Amount Sbn	Share %
Barclays (UK)	5	2.0	9.6
Mizuho (Japan)	11	1.8	8.5
Royal Bank of Scotland (UK)	9	1.5	7.2
BNP Paribas (France)	12	1.4	6.6
Westpac (Australia)	7	1.2	5.5

# UNCOMPROMISED QUALITY



Not only are we proud to be the largest manufacturer of pre-engineered buildings in Asia, Africa and Europe, but also the most quality-conscious pre-engineered building supplier in the world. Our engineering output is the most comprehensive and detailed; our design procedures follow the most international standards; our raw materials are under continuous scrutiny from source to factory to site; our buildings are manufactured within a strict quality control programme; our services start from the day you meet us and never end; our aim is your peace of mind when you buy a steel building.

So why not join our satisfied customers and let Zamil Steel be your steel building solution provider?



A pleasure to do business with

### Area Offices

Office	Code	Phone	E-mail
Dammam	(966 3)	847 2146	ZSDammam@ZamilSteel.com
Riyadh	(966 1)	472 5555	ZSRiyadh@ZamilSteel.com
Jeddah	(966 2)	860 0012	ZSJeddah@ZamilSteel.com
Kuwait	(965)	484 8510	ZSKuwait@ZamilSteel.com
Manama	(973)	178 3180	ZSManama@ZamilSteel.com
Doha	(974)	465 9000	ZSDoha@ZamilSteel.com
Dubai	(971 4)	214 0424	ZSDubai@ZamilSteel.com
Abu Dhabi	(971 2)	627 7279	ZSAbuDhabi@ZamilSteel.com
Muscat	(968)	68 3303	ZSMuscat@ZamilSteel.com
Sanaa	(967 1)	44 8399	ZSSanaa@ZamilSteel.com

### Head Office

PO Box 877 Dammam 31421 Saudi Arabia  
Phone (966 3) 847 1840 Fax (966 3) 847 1291  
E-Mail [pebmarketing@zamilsteel.com](mailto:pebmarketing@zamilsteel.com)

www.zamilsteel.com