

A DECADE IN RETROSPECT: ANALYSIS OF SOVEREIGN *SUKUK* IN NIGERIA

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ABSTRACT

This paper explores the emergence and implications of sovereign *Sukuk* issuance in the Nigerian financial landscape. *Sukuk*, as Islamic financial instruments, have gained global recognition for their compliance with *Shari'ah* principles and their potential to mobilize capital for infrastructure development. This paper provides an in-depth analysis of the historical context and regulatory framework surrounding the introduction of sovereign *Sukuk* in Nigeria. The study delves into the motivations driving the Nigerian government's adoption of *Sukuk* as an alternative financing mechanism, considering factors such as economic diversification, infrastructure deficit, and the desire to attract Islamic investments. Through a comprehensive literature review via doctrinal research, the paper evaluates the performance and impact of sovereign *Sukuk* on Nigeria's economic indicators, fiscal policies, and the broader financial market. Furthermore, the research assesses the challenges and opportunities associated with the implementation of sovereign *Sukuk*, considering both domestic and international perspectives. It investigates the investor perceptions, market dynamics, and regulatory adaptations required to facilitate the successful integration of *Sukuk* within Nigeria's financial architecture. The findings of this study contribute to the existing body of knowledge on Islamic finance, offering insights into the specific context of sovereign *Sukuk* within the Nigerian economic landscape. The paper concludes with policy recommendations and prospects, aiming to guide policymakers, financial institutions, and investors in

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navigating the evolving landscape of Islamic finance in Nigeria.

KEYWORDS: Sovereign *Sukuk*; Infrastructural Development; Islamic Finance; Economic Development; NNigeria.

1. INTRODUCTION

Nigeria's first entrance into the Non-Interest Capital market (NICM) was sometime in 2008. This is evident with the launching of the first *Shari'ah-compliant* investment fund, the 'Halal Investment Fund' by Lotus Capital Ltd, the first known Islamic Fund Manager in Nigeria. After this, the Securities and Exchange Commission 2010 produced the Islamic Fund Management rules. However, it was only in 2013 that the SEC, deriving its powers to make rules from Section 313(6) of the Investment and Securities ACT (ISA, 2007), produced the rules on *Sukuk*, leading to the issuance of the first-ever *Sukuk* to be issued in Nigeria. Osun *Sukuk* is a sub-sovereign *Sukuk* because a state government issued it in Nigeria. Nigeria also has an Islamic equity index known as the Lotus Islamic Index.

The *Sukuk* market in Nigeria is expected to develop the country's economy in general. Most specifically, growth in businesses, construction, and rehabilitation of infrastructural projects led to the industrialization of the country.¹ However, the potential of the NICM segment as a driving force for the Nigerian economy in its fund-raising capacity has significantly been under-utilized until recently when the Federal Government of Nigeria (FGN) showed interest in the *Sukuk* market. This is because even the *Sukuk* issuance was delayed until four years after a sub-sovereign (Osun State) issued its *Sukuk*. This is quite an anomaly because, in other climes, it is the issuance by the sovereign that opens the market and usually serves as the benchmark for the issuance of other types of *Sukuk*.²

NICM's primary services include non-interest product structuring, project financing, and management services.³ Nigeria is actively

¹ NICMP "The Roadmap to Guided growth to the Nigerian NICM -2014-2024" Progress Report of the NICMP Master Plan Committee (26th March 2014)

² 'Sovereign *Sukuk*: Small Size, big ambitions' Islamic Finance News Cover Story (April 2014)

³ NICM, *Nigeria's 10-Year Non-Interest Capital Market Master Plan, 2015-2025* (Nigeria: NICM, 2015)

involved in developing a vibrant Islamic capital market because the growth of an overall Islamic financial system lies in the growth of its capital market and other interest-free financial products and services.

It is noteworthy that with the emergence of *Sukuk* into the Nigerian Islamic Finance industry, the term “*Sukuk*” has appeared synonymous with Nigeria’s Islamic capital market. This is because it is the only product that has dramatically impacted the country’s overall economy and what Nigerians can easily relate to, seeing that they could quickly identify with the result of such an Islamic investment in terms of the roads constructed and rehabilitated. Therefore, more issuances are expected this new decade to add to the already four FGN sovereign *Sukuk* issued in 2017, 2018, 2020, 2021, 2022 and 2023 respectively. Again, this is because the country’s infrastructure needs are enormous and require an Islamic finance product like *Sukuk* to fill in the gap.

2. *Sukuk* as a Source of Borrowing for Nigeria

Debt or equity might be used to raise funds. However, stock market activity in Nigeria has decreased significantly from levels witnessed during the equity boom of 2004–2008. As a result, corporations and governments have been forced to join the debt market by issuing floating bonds. There have been 80 corporate bond issuances in Nigeria since 1960, as well as state and municipal bond issuances, with state bond issuances dominating the market in recent years.⁴

Sukuk is considered alternative public financing throughout the world. Its use mainly for infrastructural development must be emphasized. It has been reinstated in several works of literature that the need for infrastructure funding globally will drive further *Sukuk* issuance. As the year continues and additional projects get launched, infrastructure investment is projected to spur *Sukuk* issuance in the GCC.⁵ In addition,

⁴ SEC ‘Corporate Bonds Issued’ <http://www.sec.gov.ng/corporate-bonds-issued-%281960-to-2013%29.html> accessed on 05 April 2018; SEC “States and Local Government Bonds Issued” <http://www.sec.gov.ng/states-and-local-government-bonds-issued-%281978-to-date%29.html> accessed on 06 April 2018

⁵ “Building on Industry: Islamic Project and Infrastructure Financing” Islamic Finance News Sector Analysis Infrastructure & Project Finance. (April 2014).

the global infrastructure funding needed between the years 2014 and 2030 is estimated at a whooping sum of US\$57 Trillion

A recent report by The Economist noted an estimate by McKinsey of a funding gap of US\$57 trillion needed for global infrastructure construction and maintenance between now and 2030.⁶

The tremendous success recorded in the *Sukuk* market in Malaysia is tied to its infrastructural needs. Standard & Poor's Rating Services says: "Funding needs and large infrastructure investments in Malaysia and the GCC, combined with better global investor sentiment, are behind today's momentum in the *Sukuk* market." Nigeria cannot, therefore, be an exception to this proven theory.

The use of sovereign *Sukuk* as alternative public financing for Nigeria, particularly in developing its infrastructural needs, is not common only to Nigeria. Research has it that other prominent countries in the world have utilized this financing mode and still utilizing it. Malaysia has dominated the market, spending vast amounts on infrastructure projects, followed by other countries in the Gulf. The western Muslim minority countries have been utilizing *Sukuk* to fund a number of their projects. The US government is one such example utilizing *Sukuk* for its oil and gas sector. *Sukuk*, therefore, serves as an essential contribution to the growth of the US energy industry, says Ayman and Richardson.⁷ It is believed that as of the year 2007, billions of dollars have been raised for the needed capital for infrastructure projects through *Sukuk* offerings.⁸

Furthermore, it has been said that:

Existing gaps in financing are increasingly being filled through a balanced approach that combines support from development agencies and export credit agencies, private equity investment, intra-continental investment, and the

⁶ *Ibid.*

⁷ Ayman H. A. and Richardson C.F., 'New Horizons for Islamic Securities: Emerging Trends in *Sukuk* Offerings.', (2007) 7(2) Chicago Journal of International Law, p. 410.

⁸ *Ibid* p. 409.

use of asset-backed debt facilities such as sharia-compliant *Sukuk* and reserve-based loans.⁹

Sukuk, therefore, provides the perfect solution for diversification of funding for the government, companies seeking to invest, Cooperative societies seeking to widen their investment portfolio and private individuals. This, in turn, translates to financial inclusion for individuals because they can invest for as low as ₦10,000 (Ten Thousand Naira).

The Securities and Exchange Commission, the main regulatory body for all capital markets, has since recognized the great potential in developing the Islamic Capital Market in Nigeria. This is evident in setting up the technical committee and approving the NICM master plan submitted. Following worldwide trends, Nigeria's Stock Exchange (NSE) created an Islamic index – Lotus Islamic Index (LII) – to track the performance of *Shari'ah-compliant* assets.¹⁰ The need for NICMPs in Nigeria was highlighted in the technical committee's report submitted to the commission. Because of its asset-based feature, it promotes transparency, accountability, and, consequently, good corporate governance. NICMPs further promote financial stability by linking the financial sector with the economy's real sector, making it attractive for infrastructure financing. Conventional and alternative models can and do co-exist to enhance product depth and financial inclusion. Following the slow growth in developed markets, it is critical to diversify our sources of investment capital, and NIMCPs provide that opportunity.

A key prospect for this diversification is the concentrated wealth in the rising Asian Tigers and the GCC zone¹¹, which tracks *Shari'ah-compliant* investment instruments. The Nigerian sovereign and corporate organizations can access a new investor base by issuing alternative capital market products. This will widen the liquidity available for investment in infrastructure and other priority projects. The market provides an investment platform to attract petrodollar investment potentials in the Gulf Arab region which is expanding its

⁹ Newendorp, T. and Thomas, S. *Mobilising Finance for Energy Development in Africa Expert Insight* (Washington: Energy Investment Banking, December 2013).

¹⁰ Shehu U.R. A, 'Islamic Banking and Finance in Nigeria: Issues, Challenges, and Opportunities.' MPRA Paper No. 42573 (November 2012).

¹¹ Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, UAE.

investment focus to Africa to tap into the high returns in the African markets. The Local investors seeking ethically compliant assets and opportunities will be attracted to the market, ensuring financial inclusion.¹²

The growth of NICM in Nigeria will be fast-tracked because non-interest finance is fast-growing worldwide. With the slowed growth in the developed world, it has become critical to diversify our sources of investment capital. Some of the wealthiest countries and individuals are seeking Sharia-compliant investments. Global economic growth has, over the years, relied mainly on domestic financial sources of funds or foreign aid. The need for governments to finance their operations forever remains a significant challenge, and the mere thought of Islamic capital markets products and instruments may be the solution.

Public Financing in Nigeria takes several forms, the major and most popular one being the debt program, where monies are borrowed from the World Bank and International Monetary Fund (IMF) with a repayment agreement of paying the principal plus interest at the agreed time. However, given Nigeria's massive infrastructure deficit and the difficulty the Federal Government of Nigeria is facing due to a drop in oil revenue, among other issues, it has become critical for State Governments and corporations to seek alternative finance to satisfy their capital development demands.

The Central Bank of Nigeria, being a shareholder in the Malaysian-based International Islamic Liquidity Management Corporation, is worthy of note. It aims to issue *Sukuk* to assist Islamic banks in managing their excess liquidity. Since Nigeria is moving gradually to adopting an Islamic economy, this invariably means more reliance on equities and asset-based financing. This is because Islam prohibits interest-inclined investment. *Sukuk* provides efficient resource mobilization and allocation.¹³

¹² NICMP 'The Roadmap to Guided growth to the Nigerian NICM -2014-2024' Progress Report of the NICMP Master Plan Committee (26th March 2014)

¹³ Ali, S.S.' Islamic Capital Market Products: Developments and Challenges' Islamic Development Bank Group & Islamic Research and Training Institute. Occasional Paper No. 9 (1425H/2005).

The *Sukuk* market is, therefore, a replacement for traditional interest-bearing securities. Malaysia's experience with the *Sukuk* issuance program included government-guaranteed and non-government-guaranteed issuances of varied tenors and maturities. It estimated returns and yields to maturity could be drawn upon. In the instance of Nigeria, a special purpose vehicle might be established to purchase a building to be used (e.g., an airport) - a sovereign *Sukuk* could then be issued to raise 15–30-year money, and the asset's service charges would be used to service the *Sukuk*.¹⁴

For *Sukuk*, therefore, in exchange for bearing partial ownership responsibility, the lender is entitled to a portion of the income or dividends generated by the supporting asset, similar to a reduced equity risk. The resultant effect is that the global market for *Sukuk* keeps growing.¹⁵ *Sukuk* is thus tied to an underlying asset, not just debt. The *Sukuk* certificate signifies ownership of an asset and not just an indication of IOU (I owe you).

3. Case Studies of Nigeria's Sovereign Sukuk

Nigeria has taken a decisive step toward establishing itself as Africa's Islamic finance center, following Tunisia, Morocco, Kenya, and South Africa in advancing Islamic finance and Takaful laws and becoming one of the few African countries to issue a domestic *Sukuk*. However, it is essential to note here that a vast financing requirement of the Government is needed to fulfil the dream of unprecedented economic growth.

The offer for a subscription to all the *Sukuk* issued so far in Nigeria is made to the public. For the first sovereign *Sukuk* issued in 2017, the Pension funds Managers could not invest the pension funds in the *Sukuk*. However, a circular was subsequently issued allowing them to invest pension funds in products such as *Sukuk*. Hence in the subsequent sovereign *Sukuk* issued, it was seen that they also took advantage of the investment opportunity provided by the

¹⁴ Sanusi L. S., 'The Role of Development Finance Institutions in Infrastructure Development: What Nigeria can learn from BNDES and the Indian Infrastructure Finance Company.'

¹⁵ Newendorp, T. and Thomas, S., *Mobilising Finance for Energy Development in Africa: Expert Insight* (Washington: Energy Investment Banking, 2013), p.53.

sovereign *Sukuk* to invest their funds in it. Interestingly, several Islamic Cooperatives invested in the issued FGN *Sukuk*.

i. Osun State Sub-Sovereign Sukuk

The Osun state sub-sovereign *Sukuk* is an epoch of transformation from Nigeria's public debt issue. This is a shift from the relationship financing of Government to that of open-market funding. *Sukuk* are the crest of a new wave of innovation in Islamic finance in Nigeria. One of the notable sovereign *Sukuk* issuances in the third quarter of 2013 was Nigeria's Osun state sovereign *Sukuk*, which paved the way for the Government of Sub-Saharan Africa's largest Muslim population (Muslims constitute substantial no of Nigerian population) to sell the first *Shari'ah-compliant* sovereign bonds (3Q13). The aforementioned high-profile deal in 2013, which received the African Deal of the Year award in 2014, welcomed the Islamic capital market into Nigeria. The strength of the Osun state *Sukuk*, as well as the opening of the sovereign *Sukuk* market, was the criteria for the award.¹⁶ The Augusto & Co., a local rating agency, gave the deal an 'A' rating, and it was launched on the Nigerian Stock Exchange (NSE) in September 2013.¹⁷

Lotus Capital¹⁸ pulled together the first sub-sovereign *Sukuk* issuance, the Osun State sovereign *Sukuk*, a domestic *Sukuk*. The SEC licensed Lotus Capital Plc as the first Islamic capital market operator. The established Lotus Islamic Index has boosted the value of Nigerian stocks leading gains across the bourse's sectorial indices. It is noteworthy that the Lotus Islamic Index is the most actively traded stock on the Nigerian Stock Exchange. The index, which tracks the performance of 15 *Shari'ah-compliant* shares on the stock exchange, rose 0.69 per cent to 1,352.49 points, while the All-Share Index rose 0.25 per cent to 23,199.03 points.¹⁹

¹⁶ "Nigerian Stock Exchange Listed Bond Wins African Deal Of the Year Award" <http://m.mondovisione.com/news/nigerian-stock-exchange-listed-bond-wins-african-deal-of-the-year-award/> accessed on 2 December 2014.

¹⁷ Islamic Financial News, *Meeting Africa's infrastructure needs*, (2013).

¹⁸ Lotus Capital is the Nigerian asset manager offering *Sharī'ah* compliant investment product.

¹⁹ 'Sovereign Sukuk: Leading the way' Islamic Finance News the World's Global Islamic Finance News Provider, Redmoney Publication. (August 2012).

The Osun state sovereign *Sukuk* is the first sub-Saharan African sovereign deal from a notable economy.²⁰ *Sukuk al-Ijarah* (Lease) is the structure of the deal, and the total amount of the issuance is \$ 62 million (10 billion Naira) with a 14.75 per cent fixed return yield.²¹ The deal was oversubscribed by 20% notwithstanding its novelty.²² The prospectus of the seven years *Sukuk* that was due in 2020 shows that two (2) elementary schools, two (2) middle schools and twenty-three (23) high schools across Osun State were constructed. The *Sukuk* has since matured and duly redeemed by the Osun State Government. There was no reported default in the payment of rent, and the Osun State Government has since taken over the underlying assets (the schools).

The Government of Osun State guaranteed the *Sukuk* and won far-reaching support from the finance industry where relatively all banks (investment, conventional and Islamic), some acting as co-underwriters, bought the *Sukuk*. This is because Nigeria has been claimed to be the most important country in Africa regarding *Sukuk*. Its sizeable Muslim population is a valuable resource to be used in fixing the country's infrastructure challenges, similar to the role played by *Sukuk* in tackling infrastructure problems in other countries. This indicates *Sukuk*'s potential as a long-term financing option for the Nigerian Government to fund infrastructure projects at both the state and national levels.²³

This inclined infrastructure security in the name of *Sukuk*, therefore, signaled the start of a trend in Nigeria. Accordingly, several analysts projected that Nigeria would witness more *Sukuk* issues in a few years from both the Federal Government of Nigeria and the states in the Federation.

²⁰ 'Nigeria Sukuk' <http://www.reuters.com/article/2013/10/02/nigeria-sukuk-idUSL6N0HS2UE20131002> accessed on 14 September 2014 and <http://newspapersinnigeria.com/newspapers-in-nigeria> accessed on 11 September 2014.

²¹ <http://newspapersinnigeria.com/newspapers-in-nigeria> accessed on 25 October 2014.

²² 'Osun Sukuk Oversubscribed' <http://www.thisdaylive.com/articles/osun-sukuk-oversubscribed-by-20-/161123/> accessed on 23 November 2014.

²³ Islamic Financial News, *Meeting Africa's infrastructure needs*, (2013).

Osun State government, sometime in 2012, made known its intention to issue a debt certificate in the form of *Sukuk* under its ₦60 Billion debt issuance programs, making it the first ever *Sukuk* to be filed with the Securities and Exchange Commission. It is also the first sub-sovereign *Sukuk* to be issued in Nigeria. Hence its unprecedented over-subscription was recorded. It was initially meant to be something other than ₦10 Billion. However, due to the high demand for the certificate from investors, it ended up being a ₦10 Billion fixed return Tranche II with a seven-year life span making its maturity date 2020. The plan was to raise the ₦10 billion by using one of the less controversial *Sukuk* available in the Islamic Financial product and services market. *Sukuk al-Ijarah*, which can be literally translated to mean lease, for the construction of twenty-seven (27) Millennium Model Schools across the various Local Governments in the Osun State was thus used.

The Osun state sub-sovereign *Sukuk*, spearheaded by the lead issuing House and fifteen (15) others, adopted an *Ijarah Sukuk* structure. In its literal form, it is known as a lease arrangement whereby rentals will be paid to the Lessor (*Sukuk* holders) regularly based on the enjoyment and availability of the usufructs on the underlying asset by the Lessee (the State Government).

However, *Sukuk al-Ijarah* is more complex than the above, because each *Sukuk* comes with its unique peculiarity, as in the Osun State Sub-Sovereign *Sukuk* case. Hence, there is a need to give a detailed description of the structure adopted for this particular *Sukuk* in question.

First, for the issuance, a Special Purpose Vehicle (SPV) was incorporated under the name Osun *Sukuk* Company Plc as a Public Limited Liability Company on 11 June 2012, which is owned by the Osun State Government and served as the issuer of the sub-sovereign *Sukuk*. The State Government, the originator of the issue, and the landowner first transferred title to the land required for the construction to the SPV through the issuance of a C.of O. (Certificate of Occupancy) in the SPV's favour. This is to legalise all the other transactions that will occur in the future because the SPV will be acting

on behalf of the *Sukuk* holders (investors), and they need to be the legal owners of the land on which the schools were built²⁴

Next, the SPV declares a Trust over the underlying asset or, in this case, the trust assets created for the benefit of the *Sukuk* holders. The SPV then issued an *Ijarah* sub-sovereign *Sukuk* to investors to raise funds for the construction. The *Sukuk* investors then pay the total amount of ₦10 Billion for the issued *Ijarah Sukuk* to the issuer before the closure date at a stipulated price of ₦1000 per unit of the *Sukuk*. Amongst the agreements entered into by the SPV, aside from the trust agreement already entered into,²⁵ was the Agency Agreement between the SPV and the Management Agency for the construction, Management, and Implementation of the Projects. The two parties, i.e., The Management Company and the SPV, agreed on what should be done with the cost of construction of the projects, and the SPV will then transfer the amount of construction to the Management Company.

There is, once more, another agreement that is added to the earlier ones mentioned. This is the *Istisna* contract that was entered into between the Management Agency's Operational Partner and the Contractors for the construction of the agreed projects.²⁶ The financial manager oversees and monitors the project's progress as well as disburses the necessary payments as at when needed. Since the structure reads *Sukuk al-Ijarah Muntahiyah bi Tamlik* (Lease-to-own Agreement), the *Sukuk* assets are leased immediately at the onset of the transaction to the State Government against periodic rental payments. Furthermore, in its capacity as the Lessee, the State Government immediately starts making rental payments. The rent is calculated on the actual presence of usufruct distributed to cover the gestation period subject to adjustment.²⁷ The lease rental payment is paid to the SPV through the appointed Agent, which is then distributed among the *Sukuk* holders. Based on the purchase undertaking given by the

²⁴ Their legality could be better if we go into the intricacies of the law that forbids the transfer of government land to individuals in whatever form and the inalienability of government lands, plus the controversies surrounding the concept of legal and beneficial ownership in law.

²⁵ i.e., the trusted delegate is given to Sterling Asset Management & Trustees Limited.

²⁶ i.e., the Elementary, Middle, and High Schools.

²⁷ This is based on the *Shar'iah* principle that there must be an enjoyment of usufruct before rental payments can be made because "you cannot reap where you have not sowed" or "you cannot sell what you do not have."

State Government, the lease rentals are paid to the *Sukuk* holders as rental payments. At the same time, the principal investment is being redeemed via a gradual sale to the Osun State Government of the School units. Hence, the Osun State Government redeems the *Sukuk* certificates on a piecemeal basis by purchasing the Leased Assets on the Scheduled maturity dates. It is imperative to note that lease rentals only accrue for the period during which usufruct exists while rental payments spread for the whole period of finance. At the end of the maturity period, that is, by the specified date (the year 2020), the appointed Agent delivers the projects, Middle and Secondary Schools to the SPV, who in turn gives them to the State Government thereby taking ownership of the said projects.

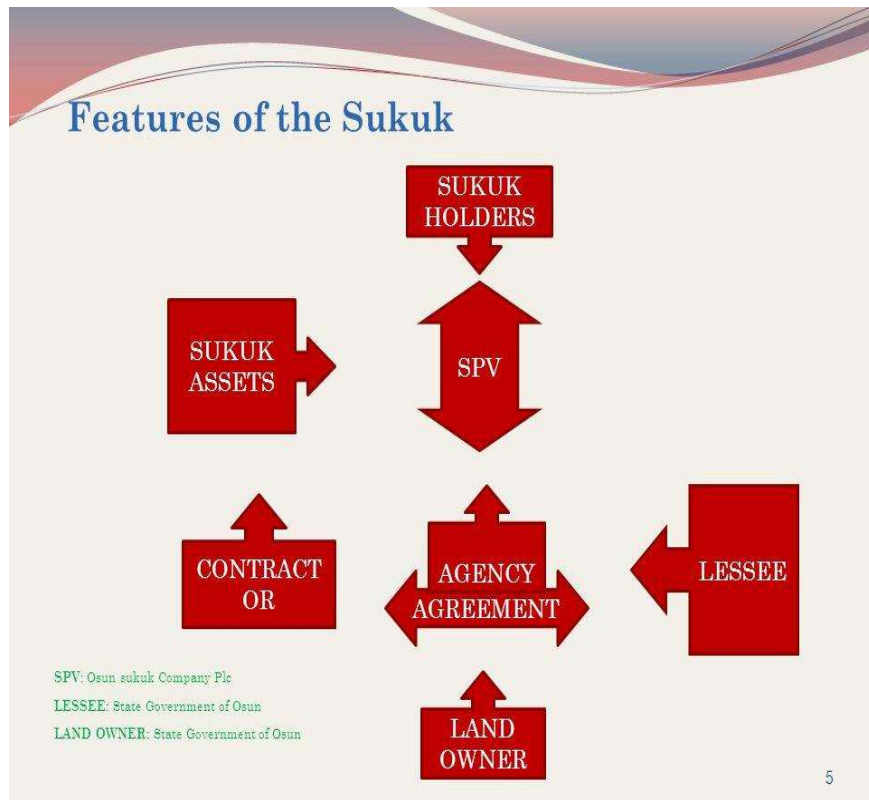


Figure 1. shows the cash flow for Osun State *Sukuk*.
Source: Capital Assets Limited

Some essential things are worthy of note in the Osun State Sub-Sovereign *Sukuk*:

1. An important aspect to mention is that the holders of *Sukuk* remain the sole owners of the underlying assets. The Osun State *Sukuk* Company Plc being the SPV holds the assets that are the projects to be constructed, i.e., the elementary, middle, and high schools, in trust for and on behalf of the *Sukuk* holders.
2. The Trustee will hold security for the payments and other issuer's responsibilities with the *Sukuk* in the form of the ISPO issued by the Federation's Office of the Accountant General.
3. There is the Omoluabi Conservation Fund, a State-owned Investment Fund.

The law establishing the fund provides that 30% of the fund, i.e., the stabilisation fund, could be deployed in the event of an imminent default of long-term obligations of the State. Therefore, the Omoluabi Conservation Fund acts as an enhancement for the *Sukuk* when needed.

The above guarantee/security provided for the *Sukuk* helps to overcome an imminent challenge known to most *Sukuk*, which is the default. Also worthy of note is that although most of the investors were institutional investors, there were few private individual investors. However, the Pension Funds Administrators could not invest in the *Sukuk* because of a circular that was issued that made it forbidden for PFA to invest in such *Sukuk* investments.²⁸ The *Sukuk* has since been issued and redeemed, and the Nigerian Stock Exchange (NSE) has listed the issue.

ii. Nigerian Federal Government Sovereign *Sukuk*

The Nigerian Federal Government boldly entered the Islamic Capital Market with its first sovereign *Sukuk* issuance to the tune of 100 billion issuance, which was highly oversubscribed. However, something central to all the FGN Sovereign *Sukuk* has been issued so far in Nigeria. They all have employed the structure of *Ijarah*, which is believed to be less controversial and widely accepted globally. Aside

²⁸ There has since been an amendment, and it is now allowed for PFAs to invest in *Sukuk* investment or its related investment types. It is therefore hoped that the next *Sukuk* coming up, PFAs would be able to invest in it.

from this, most of the contracts and agreements entered into by the parties are similar across the five issuances with negligible differences. However, this research must highlight the key features of each issuance, i.e., the 2017 FGN Sovereign *Sukuk*, the 2018 FGN Sovereign *Sukuk*, the 2020 FGN Sovereign *Sukuk*, the 2021 FGN Sovereign *Sukuk*, the 2022 FGN Sovereign *Sukuk* and the 2023 FGN Sovereign *Sukuk*.

A. 2017 FGN Sovereign Sukuk I

There is a remarkable similarity between this *Sukuk* and with sub-sovereign *Sukuk* issued by the Osun State Government because it is also structured in line with the *Ijarah Sukuk*. It is a Hundred Billion Naira (N100, 000, 000, 000. 00) with a 7-year tenure at 16.47% return per annum *Ijarah Sukuk* due in 2024. The FGN Roads Sukuk Company 1 PLC is a wholly-owned subsidiary of the Federal Government of Nigeria, administered by the Ministry of Finance and the Debt Management Office. This *Sukuk* was notable for being the first sovereign *Sukuk* issued by the Federal Government of Nigeria and oversubscribed at 105%.

It is imperative to state that two categories of documents are necessary for processing the issuance of Sukuk in Nigeria. The first category is the Capital Market Documents, mainly standard documents that need little to no changes to adapt to use in a specific Sukuk structure arrangement. Examples of such documents include a prospectus, Agency Agreements, Master Trust deeds, Subscription Agreements, and Mandate Letters. At the same time, the second category is the Transaction documents more related to the specific Sukuk being issued, such as the Sales and Purchase undertaking agreement, the *Istisna* Agreement, and the *Ijarah* (Forward Lease Agreement).

The Trust Assets consist of the Issuer/Trustee's current and future interest, rights, title, benefits, and entitlements in, to, and under the Roads, as well as any proceeds from the Roads; the Issuer/Trustee's current and future interest, rights, benefits, and entitlements in, to, and under the Transaction Documents; all amounts of money standing to the credit of the Issue Proceeds Account from time to time; and all proceeds of the foregoing. The Trust Undertaking document is part of the transaction documents needed to be submitted in the Capital market, mainly because the *Sukuk* will be listed in the NSE.

As a result, the *Sukuk* is an irrevocable obligation of the Federal Government of Nigeria that will rank *pari passu* with the government's current debt obligations in all respects and will carry the government's credit rating. The revenues of the Certificates, totaling N100,000,000,000.00, are being utilized to build portions of 25 important road projects across the country's six geopolitical zones. The specific roads to be built with the revenues of the *Sukuk* are located among the country's six geopolitical zones.

It is worth noting that the Purchase Undertaking is one of the primary transaction documents deemed beneficial/essential for the *Sukuk* issuance. The Purchase Undertaking is a document in which the Federal Ministry of Power, Works and Housing (FMPWH), as Lessee of the Leased Assets, unconditionally and irrevocably agrees to purchase all of the Issuer's beneficial title and ownership rights in the Leased Assets at the Purchase Price and on the terms outlined in the Purchase Agreement.

A Purchase Undertaking, a unilateral declaration by the FGN pledging to purchase the Lease Assets from the Issuer/Trustee at the maturity of the *Sukuk*, is dated on or around the date of the prospectus. Accordingly, any outstanding principal investment will be reflected in the purchasing price. At the same time, the Sale "Undertaking" dated on or around the date of the prospectus is a unilateral statement Undertaking by the Issuer/Trustee that the Issuer/Trustee will sell the Lease Assets to the FGN if specific criteria as outlined in the Undertaking are met.

The above two documents read together imply that the FGN is unwilling to release the roads to the investors. The intent is to get the roads constructed and then return them to being the sovereign assets it is. This takes us to the initial question of this study: whether there is a true-sale arrangement in the case of sovereign *Sukuk*. AAOIFI, in its statement, categorically forbids the purchase undertaking.

The Federal High Way Allocator is the Federal Government of Nigeria, represented by the Minister of Power, Works, and Housing (MPWH). He assigns the SPV the property on which the roads will be built. (DMO and Federal Ministry of Finance have 40% and 60% in the FGN Sovereign *Sukuk* Company plc.). The Ministry of Power, Works, and Housing is the Road Construction Agent, while the Road Lessor is

the *Sukuk* Company, also known as the SPV. The Road Lessee is the Federal Government of Nigeria, while the Road Seller is the SPV, the *Sukuk* Company. The Purchaser of the roads is the Lessee at the end of the tenure of the *Sukuk*. Moreover, the transaction Originator is the DMO on behalf of the Nigerian Federal Government.

The *Sukuk* is admitted for trading on the Nigeria Stock Exchange (NSE) floor and FMDQ Over The Counter Securities Exchange. Trading the *Sukuk* in the market represents secondary trading, which amounts to purchasing the underlying assets and the roads constructed. It is imperative to note further that under the rights of *Sukuk* holders, it is stated that: “A *Sukuk* holder shall have the right to pledge, charge, mortgage, or otherwise offer his Certificate as security for a debt, a loan or an obligation and in any such case the *Sukuk* holder shall notify the Delegate Trustees, the Registrar and the CSCS/Custodian, in writing, of the pledge, charge, mortgage or obligation.” A look at this right suggests that the trust asset, in this case, the /roads under construction, which is a sovereign asset, can be pledged by a *Sukuk* holder to obtain a loan facility from a financial institution. However, this may be challenged in a court of law because sovereign assets cannot be owned by individuals or a group of individuals.

The *Sukuk*, like any other financial product, has several risks. According to the *Sukuk* prospectus issued, the risk related to the FGN *Sukuk* includes Country Risk (Political risk); Risk related to the Macroeconomy (economic risk and inflation risk); and Risk Related to the *Sukuk* (Credit risk, Regulatory risk, and *Shari'ah* Non-compliance risk, rate of return risk, construction risk, liquidity risk, and taxation). However, it is said that although there is a credit risk on the part of the Lessee (FGN), this risk is unlikely to happen because *Sukuk* is considered a direct sovereign obligation of the Federal Government of Nigeria.

Summary of Transaction Documents and their implications

1. Letter of Allocation- This is a letter from the Federal Government of Nigeria granting the SPV the right to build roads on specific federal routes without charge or encumbrance. The letter includes an undertaking by the FGN not to disturb the SPV's right of use until the fulfilment of all obligations under the *Sukuk*. The implication is that the Federal

Government transfers the land ownership title to the *Sukuk* holders through the SPV.

2. Trust Deed- A trust agreement between the FGN Roads Sukuk Company 1plc (SPV), the FGN represented by the Minister of Power, Works, and Housing (MPWH), The Messrs STL Trustees Limited, and FBN Trustees Limited (the Delegate Trustees), under which:
The SPV declares a trust over the Sukuk Assets; the Delegated Trustee declare themselves a trustee for the Sukuk holders to ensure, among other things, the construction of the Sukuk Assets on their behalf; the MPWH agrees to lease the constructed roads; and the DMO agrees to pay for the lease on the FGN's behalf.
3. Forward Lease Agreement- An agreement between the SPV as Lessor, the FGN represented by MPWH as Lessee, and the DMO, in which the FGN agrees to lease the Sukuk Assets from the SPV and the DMO agrees to pay the lease on behalf of the FGN.
4. Construction Agency Agreement- Agreement under which the SPV appoints the FMPWH as its Agent to appoint contractors to construct the *Sukuk* assets.
5. Servicing Agreement- Agreement between the SPV and the MPWH wherein the SPV appoints MPWH as the Agent for substantial repairs to the Sukuk Assets (if any).
6. Purchase Undertaking- A unilateral declaration by the FGN Undertaking to buy the SPV's Sukuk Assets at the end of the Sukuk period. Any outstanding primary investment amount will be reflected in the purchasing price.
7. Sale Undertaking- A unilateral declaration by the SPV that the Sukuk Assets will be sold to the FGN if certain conditions are met as outlined in the Undertaking.

As noted above, the structure used for the FGN *Sukuk* is the *Sukuk al Ijarah Mawsoofa bi Thimma* (Forward Ijarah). This was adopted after careful consideration of relevant sections of the AAOIFI *Shari'ah* Standards for Islamic Financial Institutions, i.e., standard 17 and the Financial Accounting Standard No. 8 (Amended)

of the AAOIFI Accounting, Auditing and Governance Standards for Islamic Financial Institutions.²⁹

The Federal Government of Nigeria established the FGN Roads Sukuk Company 1 plc to issue *Sukuk* on its behalf. Below is the sequential flow of transactions of the *Sukuk*:

1. The FGN sends the SPV a letter allocating specific sections of Federal Highways for construction and rehabilitation.
2. The FGN enters into a forward Ijarah Agreement with the Issuer to lease developed roadways through the Minister of Power, Works, and Housing (MPWH).
3. The FGN enters into a unilateral Purchase Undertaking with the SPV to purchase developed roads when they reach maturity.
4. The Issuer declares a trust over the Roads to be built in favour of the *Sukuk* holders in a Trust Deed declaration and appoints Delegate Trustees to carry out its trustee functions under the trust.
5. The offer is subscribed to by investors, and the Issuer issues electronic investment certificates.
6. The Issuer engages in a Construction Agency Agreement with MPWH to hire contractors to construct/supervise the road.
7. The Issuer enters into a service Agency Agreement with the MPWH to execute significant road repairs.
8. The Issuer pays the contractors for construction with Sukuk proceeds after the contractors have been certified by the MPWH and the Trustees.
9. The completed roads are delivered to the SPV by the contractors via the MPWH.

²⁹ According to the standards, it is permissible to issue *Sukuk* that represents ownership of described asset/usufruct to be made available in the future.

10. In accordance with the forward *Ijarah* Agreement, the SPV (as Lessor) leases the Roads to FGN (as Lessee).

11. The FGN pays periodic rentals for the use of the roads and purchase amounts at maturity to the FGN Sukuk Repayment Account with the CBN.

12. The CBN, as Paying Agent, transfers the rental and purchase amount to *Sukuk* holders in accordance with the agreed-upon schedule.

13. The FGN buys the roads when they reach maturity.³⁰

Source: Barometer NG

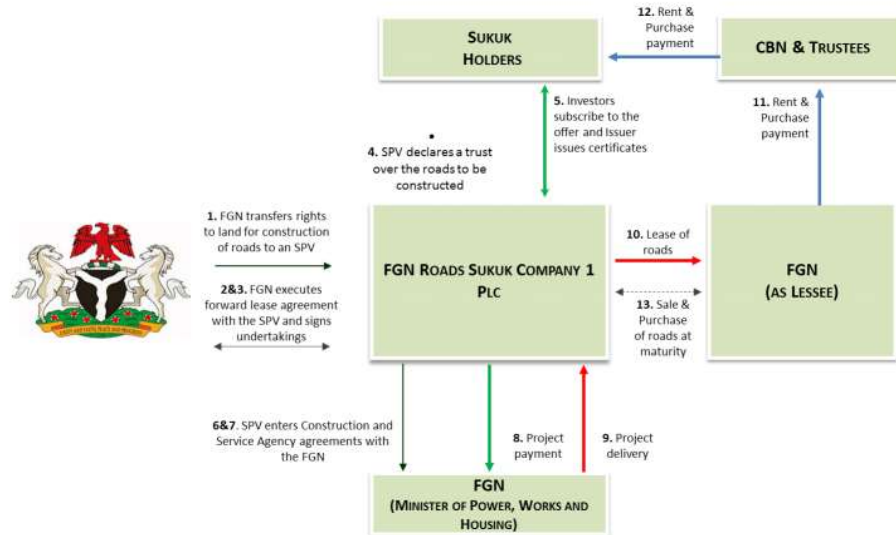


Figure 2 shows the cash flow of the FGN Sovereign Ijarah *Sukuk* I

Source: *Sukuk* Prospectus

B. 2018 FGN Sovereign Sukuk II

The Federal Government of Nigeria returned to the Islamic Capital Market in 2018 with its second Sovereign *Sukuk* issuance. This was also a N100,000,000,000.00 billion Naira *Sukuk*, with an *Ijarah*

³⁰ FGN Sukuk Prospectus

Sukuk of a 7-year tenure. Therefore, everything said about the 2017 *Sukuk* is also true for the 2018 *Sukuk*, save for the percentage of return, which is at 15.74%, as against that of 2017, which was 16.47%. This *Sukuk* maturity period is 2025 for Investors who wish to hold the same till maturity. This *Sukuk* was oversubscribed by 132%. The *Sukuk* was also issued to construct and reconstruct key road projects across the Federal Republic of Nigeria’s six geopolitical zones. 28 Roads were to be constructed/rehabilitated, i.e., an addition of 3 new roads against the 2017 FGN Sovereign *Sukuk*.

Table 1 shows statistics of the Investors’ allotment of *Sukuk*

Investor Category	Allotment
Pension Fund Administrators	40.69%
Deposit Money Banks	17.50%
Retail	17.33%
Other Fund Managers/Non-Financial Institutions	11.65%
Ethical Fund Managers/Non-Interest banks	10.94%
Other Institutional Investors	1.50%
Government Agencies	0.38%
Total	100.00%

Source: *Sukuk* Prospectus

C. FGN Sovereign *Sukuk* III

Unlike the two previously issued FGN *Sukuk*, which were a ₦100,000,000.00 sovereign *Sukuk*, this was a ₦50,000,000,000.00 sovereign *Sukuk* for the rehabilitation and construction of 44 roads across the six geo-political zones of Nigeria. Moreover, this issuance was oversubscribed at 465%, which is highly commendable. The oversubscription rate shows the increased appetite for *Sukuk* issuances in Nigeria, particularly Sovereign *Sukuk*.

D. 2021 FGN Sovereign Sukuk IV

In December 2021, Nigeria witnessed another sovereign *Sukuk* issue worth #250,000,000,000.00. This amount is the highest sum of all the issuances so far in Nigeria and has a 10-year tenor, which will be due in 2031 and has its profit rate set at 12.8%. Similar to the earlier issued one, the *Ijarah* structure was used, which was equally hugely oversubscribed. The *Sukuk* is also for constructing and rehabilitating significant roads across the country to meet the vast infrastructure deficit presently being experienced in the country.

E. 2022 FGN Sovereign Sukuk V

In December 2022, Nigeria witnessed another sovereign *Sukuk* issue worth #100,000,000,000.00. This issuance has a 10-year tenor, which will be due in 2032, with a profit rate of 15.64% per annum. Similar to the earlier issued one, the *Ijarah* structure was used, which was equally hugely oversubscribed. The *Sukuk* is also for constructing and rehabilitating major roads across the country to meet the vast infrastructure deficit presently being experienced in the country.

It is of particular interest to examine the coupon rate of the *Sukuk* issued so far in Nigeria, as depicted in the chart below.

F. 2023 FGN Sovereign Sukuk VI

Yet again in October 2023, another *Ijarah Sukuk* of N150,000,000,000.00 was issued by the Federal Government of Nigeria. With a rental rate of 15.75% per Annum, this *Sukuk* issue is to be due in 2033 and has similar features to the earlier issued *Sukuk* that utilises the Forward *Ijarah* instrument structure. Similarly, the proceeds from this structure are expected to be used for the construction and rehabilitation of key road projects and bridges across the six geopolitical zones of the country. Interestingly, it is also certified by the Financial Regulation Advisory Council of Experts (FRACE) of the Central Bank of Nigeria. It is equally pertinent to note that the *Sukuk* is backed by the full faith and credit of the Federal Government of Nigeria. The oversubscription rate of this issue is yet to be determined because, as of the time of conducting this research, the issue is still open and not yet closed.

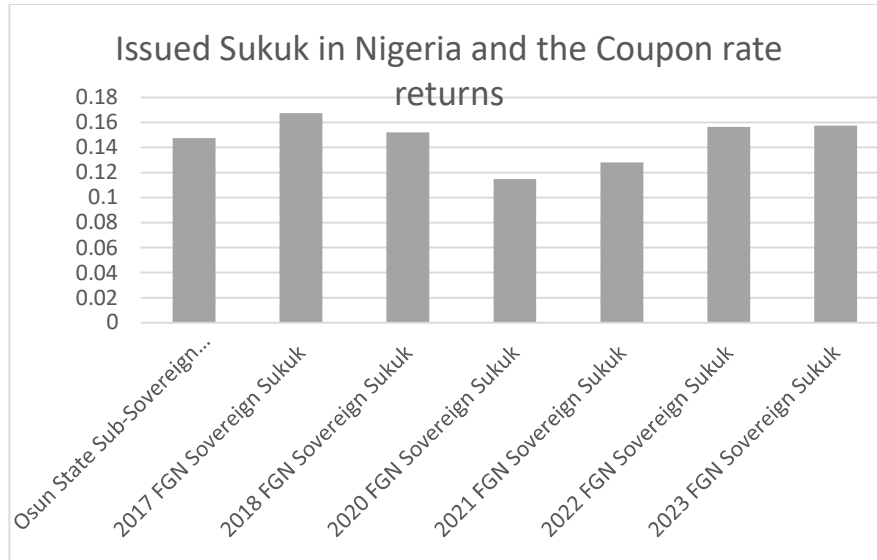


Figure 3 shows the coupon rate returns on the *Sukuk* issued.³¹

The above figure shows that the 2017 FGN *Sukuk* had a high return rate on the investment made by the public. However, there was a slight but significant decrease in the rate offered by the 2018 FGN *Sukuk*, the second sovereign *Sukuk* issued by the Nigerian Federal Government. The year 2020 saw a decline in oil prices in addition to the COVID-19 Pandemic. This also affected the return on the sovereign *Sukuk*, which is very low compared to the first two FGN *Sukuk* issued. Notwithstanding this decline in returns, the 2020 FGN *Sukuk* had the highest oversubscription, which was said to be over 446%.

³¹ Draft by the author based on the authors experience, empirical evidence and examination

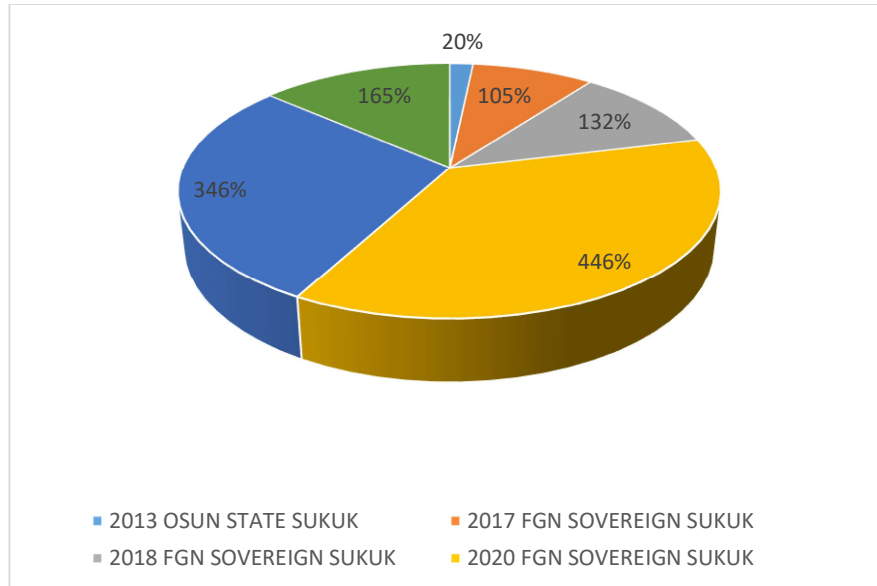


Figure 4 shows the oversubscription rate on *Sukuk*.³²

The result of the analysis further shows that there is an increase in demand for *Sukuk* issuance in Nigeria. The oversubscription rate of the five FGN *Sukuk* shows that the higher the wait from the investors for new issuance, the more the oversubscription rate. For example, the 2020 FGN Sovereign *Sukuk* oversubscription rate was a whopping 446%. In contrast, the 2018 *Sukuk* issuance was about 132% when the *Sukuk* was just issued after a year of the last issuance, i.e., the 2017 *Sukuk*, which was oversubscribed at 105%. This shows to a greater extent that the demand is higher than the supply. Even though the oversubscription rate of the issuance in 2021 was 346% which is slightly lower than that of 2020. The frequency of its issuance also has an overwhelming effect on the investors' appetite, as shown in the oversubscription rate. This appetite implies a broad acceptance of this class of Islamic finance products in the industry, and there is a considerable demand for such products that the supply cannot meet.

³² draft by the author based on the authors experience, empirical evidence and examination

4. Conclusion

A decade after its inception, Nigeria's sovereign *Sukuk* market has unequivocally proven its value, transitioning from a novel experiment to a critical instrument for national infrastructure development and financial inclusion. Sovereign *Sukuk* has the potential to accelerate Nigeria's infrastructure development. This analysis has demonstrated that *Sukuk* issuances have successfully bridged significant funding gaps, particularly in the transportation sector, while simultaneously fostering the deepening of the non-interest financial market and attracting a diverse investor base.

The prospects for sovereign *Sukuk* in Nigeria are profoundly promising. The unwavering oversubscription of every issuance signals a potent and growing demand. Looking ahead, the market is poised to evolve in three key directions: a). Market Maturation: Nigeria can aspire to become a regional hub for Islamic finance in West Africa. The next logical step involves sub-national *Sukuk* issuances by state governments and corporate *Sukuk* by major infrastructure companies, following the sovereign's credible blueprint. b). Investor Base Expansion: With greater awareness and retail products, *Sukuk* can tap into the vast informal savings pool and pension funds (e.g., PENCOR), channeling domestic capital into national development more effectively than ever before. c). Global Integration: As the market deepens and standards align globally, Nigerian *Sukuk* has the potential to attract greater foreign investment from Islamic finance hubs in the Middle East and Southeast Asia, improving foreign capital inflows.

However, the journey has also revealed challenges related to market diversity, regulatory harmonization, and public awareness that must be addressed to unlock its full potential. To consolidate these gains and ensure sustainable growth, the following policy actions are recommended:

1. For the Government and Debt Management Office (DMO):

Move towards a predictable, annual issuance calendar to build market confidence. Explore new *Sukuk* structures (e.g., Equity-Based) and finance a wider range of projects, including power, healthcare, and education, to appeal to a broader investor demographic and demonstrate tangible social impact (Maqasid al-Shariah). Partner with financial institutions to actively develop a vibrant secondary market for

Sukuk, enhancing their attractiveness by addressing the liquidity concerns of investors.

2. For Regulatory Bodies (SEC, CBN):

Strengthen the legal and regulatory framework by ensuring full clarity on standardizing Sharī'ah governance practices across all institutions. This will reduce compliance costs and uncertainty. Mandate and support educational initiatives for investors, issuers, and regulators to deepen understanding of *Sukuk* mechanics and their benefits.

3. For Financial Institutions:

Develop and promote retail *Sukuk* products and *Sukuk*-based investment funds to democratize access for the vast Muslim population and ethical investors currently excluded from large-denomination offerings. Play a more proactive role as market makers in the secondary market and as advisors to potential sub-national sovereigns (states) looking to issue *Sukuk*.

In retrospect, the past decade has laid a formidable foundation. By implementing these recommendations, policymakers, financial institutions, and investors can collectively navigate the evolving landscape. Sovereign *Sukuk* is not merely a financial instrument; it is a catalyst for inclusive economic growth, solidifying Nigeria's position as a leader in African Islamic finance and paving the way for a more resilient and diverse financial future.