AN OVERVIEW OF PARTICIPATORY PROJECT FINANCE & VENTURE CAPITAL FINANCE IN THE GCC - IMPLICATION FOR INDIA

DR. NIKHAT MUSHIR

Assistant Professor, FCMS, PDM University.

Abstract

There has been tremendous growth in infrastructure development in the GCC (Gulf Cooperation Council) countries in the past decades and it ought to be since Infrastructural development is an important precondition for economic growth of any country. This high rate of growth in Infrastructure development also owed to growing demands from increasing population and backed by huge oil revenue surplus. However there has been slow down in the Infrastructure sector investment over the last few years due to falling oil price. Still as the past historical records shows the potential in this sector remains high given the fact the projects have been kept rolling over to the next year instead of been cancelled. An estimate of infrastructure investments for the GCC region varies from USD 535 billion over the next decade to about USD 2 trillion by 2020. With governments commitment to provide high quality of standard of living to its nationals and at the same time overall slowdown in the world economy that has restricted the conventional sources of finance to certain limit. It raises an enquiry over the role of Islamic financial sector in providing an alternative source of finance. The Islamic finance which operates in all sectors such as retail banking to investment banking and from Islamic insurance to asset management. In this context this paper attempts to find out the role of Islamic equity finance such as venture capital finance and project finance in the GCC. It will look into the theoretical development viz a viz Islamic Venture Capital (IVC) and Islamic Project Finance (IPF). It will further frame an argument that Islamic Venture Capital and Islamic Project Finance could play a positive role in India's massive demand of funds for the sectors conducive for equity financing.

Keywords: Project Finance, Venture Capital Finance, Participatory/Islamic Project Finance, Islamic Venture Capital Finance

1. Introduction

The Infrastructural development is considered inevitable for the economic growth of any country and it helps building a better economy by adding to the efficiency of the business environment. It becomes even more important in case of developing countries because empirical evidences show that one of the reasons for the developing countries in lagging behind is lack of proper infrastructure (Raisuddin Ahmed and Cynthia Donovan, 1992). The countries without proper roadways or power or water supply would only create inefficiency at all levels.

The GCC countries (a regional cooperation block of six Arabian Gulf countries) with peculiar economic structure are often called a rentier economy state. The Arab oil states represent, it has been said, the example par excellence of rentier states. With oil exports' revenues, the Arab oil states depend on external rent. Oil revenues represent more than 90 percent of budget revenues, 95 percent or more of exports. Therefore, the Government's role being the principal rentier in the economy becomes crucial and it becomes the central player of economic activity of the country (Hazem Beblawi). Thus, providing for the excellent public utility services to their citizen was also realized by the governments and it got more prominence with the undertone of rentier mentality.

In recent decades they have made huge infrastructure investment and in 2007 the total infrastructure investment in the GCC hit the mark of USD 206.33 billion.[1] Since 2003, more than USD 1.1 trillion worth of contracts has been awarded as GCC worked towards transformation of their physical infrastructure.[2] Anecdotal incidents related by visitors coming back to major cities such as Doha, Riyadh and Dubai after 10 years could hardly believe the scale of the transformation over such a short period of time. In recent years the investment in physical infrastructure has been slowed down and with projects being shelved over to the next year. The sector reached its nadir point in 2014 when it awarded only USD 86 billion worth of infrastructure projects.[3] One of the factors behind this slump has been said to be unprecedented downfall in oil prices. For the past year there have been some dramatic developments in oil market. The oil prices began to fall and keep falling from a high of USD 115 per barrel in June last year to USD 40 per barrel in January this year, a decline of 60% [4] and finally reached a low of USD 33 per barrel as on 21st February 2016.[5]

However, the scaling back of projects is not permanent situation as predicted from reports such as – "Qatar will not scale back economic development projects, they have announced plans to spend around USD 200 billion on infrastructure projects over the next decade or so, many related to Qatar's hosting of the 2022 soccer World Cup. Construction industry sources say some projects have been delayed or suspended in the past year, partly to avoid waste and ensure quality. But Emadi said there would be no cancellations to save money. "We're not going to scale back. Most of our projects are already at the execution stage so we're going to continue with those - we've already put a public plan of what we're actually going to do for the next 10 years,"

[1] Ahmed, Habib, *Islamic Financing for Infrastructure Projects*, Dubai: DIFC, pp 2

[2] MEED Insight, MENA Projects Forecast and Review Report 2013, accessed on 20 November 2015, URL: http://www.meed.com/download?ac=40767

[3] Arabianindustry.com, accessed on 10th November 2015, URL: http://www.arabianindustry.com/construction/news/2015/jul/30/gcc-2014-infrastructure-investments-totaled-86bn-5112185/#.VkGt6LcrLIW, pp 11

[4] The Wire, *How Falling Oil Prices are Aggravating Economic and Political Uncertainties*, accessed on 15th November 2015, URL : http://thewire.in/2015/09/22/how-falling-oil-prices-are-aggravating-economic-and-political-uncertainties-11205/,

[5] Oil-price, accessed on 21st February 2016, URL: http://www.oil-price.net/

he said.[6] Saudi's Finance Minister Ibrahim Alassaf said. "There are some projects like the ones that have been approved a few years ago and haven't been carried out until now - that means such projects are not currently necessary and can be delayed," he added. "Projects in sectors such as education, health and infrastructure are not only important for the private sector but also for the long-term growth of the Saudi economy."[7]

It shows there is a huge demand side of Infrastructure development technically, financially and operationally. For instance, there is more than USD 700 billion of megaprojects or large master planned developments of more than USD 1 billion in KSA. These megaprojects are part of broader government led development plan that promises to transform Saudi Aabia's economy.[8] Conventionally it is the Governments or any public agencies catering to Infrastructure facilities. But it is seen that government run projects due to lack of efficiency often succumb to long delays and even failure. Therefore, to cope up with increasing demand and future needs and to resolve financing issues, government has been encouraging the private sector to improve their involvement. This gave rise to public-private partnerships (PPP) in project development.[9] The private source of financing for these infrastructure projects may come from various sources both *Shariah* and conventional. For instance, Saudi Aminister Alassaf said the government would continue issuing bonds and might also sell Islamic bonds, or sukuk, to finance specific projects. "There may be an issue (of sukuk) before the end of 2015 but I cannot say this will continue - it all depends on the need to finance the budget deficit."[10]

Therefore, this paper aims to look into the financial requirement of infrastructure sector in GCC. It will explore Islamic equity financing such as venture capital and project finance, its tools and techniques. The paper will try to understand the role played by Islamic finance industry in this context. Finally, the paper will argue for the viability of IVC and IPF in India.

2. Islamic Finance

Islamic economics or financial system are derived from *Shariah*. *Shariah* is basically based on the guidelines of Quran and *Hadith*. The *Shariah* which deals with economic and financial affairs lays down the principles of Islamic jurisprudence for Islamic economic/financial system. The basic principles of Islamic financial system can be summarized as follows:

a) Prohibition on usury generally taken as equivalent of interest.

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[6] Zawya, Qatar won't scale back projects, cut subsidies–minister, accessed on 7 September 2015, URL: http://www.zawya.com/story/Qatar_wont_scale_back_projects_cut_subsidies_minister-TR20150907nL5N11D21KX2/?lok=123708150907&weeklynewsletter&zawyaemailmarketing,

[7] Zawya, Saudis trimming expenses, slowing some projects-minister, accessed on 8 September 2015, URL: http://www.zawya.com/story/Saudis_trimming_expenses_slowing_some_projects_minister-TR20150906nL5N11C06SX2/?lok=100903150906&weeklynewsletter&zawyaemailmarketing

[8] Martin, Matthew (2013), "Riyadh lays groundwork for continued spending", Saudi Arabia Megaprojects, Dubai: MEED, pp 3

[9] Ahmed, Habib, *Islamic Financing for Infrastructure Projects*, Dubai: DIFC, pp 5

[10] Zawya, Saudis trimming expenses, slowing some projects-minister, accessed on 8 September 2015, URL: http://www.zawya.com/story/Saudis_trimming_expenses_slowing_some_projects_minister-TR20150906nL5N11C06SX2/?lok=100903150906&weeklynewsletter&zawyaemailmarketing

b) Profit and loss sharing.
c) Prohibition on speculative business activities.
d) Prohibition on investing in un-Islamic (*haraa`m*) business activities.[11]

2.1 Project Finance

It has been defined as ‘a nonrecourse or limited recourse of financing structure in which debt, equity, and credit enhancement are combined for the construction and operation, or the refinancing, of a particular facility in a capital-intensive industry, in which lenders base credit appraisals on the projected revenues from the operation of the facility, rather than the general assets or the credit of the sponsor of the facility and rely on the assets of the facility, including any revenue-producing contracts and other cash flow generated by the facility, as the collateral debt’.[12] Hence, project finance is a financing technique or structure and it differs from other forms of financing techniques as it principally looks to the revenue generated by that particular project and the assets attached to the project in order to secure and service the loan of the project. Moreover, in project finance the financier usually has little or no recourse to the non-project assets of the borrower or the sponsors of the project. It assumes its importance as it is one of the most widely used techniques of financing long-term, capital-intensive, infrastructural projects worldwide. Historically, project finance was first used in the oil extraction and power production sectors. These were more appropriate sectors for developing this structured financing technique because they involve low technological risks, a reasonably predictable market, and possibility of selling the product to a single buyer or a few large buyers on multiple-year contract. It has also been used in projects like mine, toll road, railway, pipeline, power station, ship, hospitals etc which is repaid from the cash-flow of that project.[13] The sectors which dominates the use of project finance are Energy and Infrastructure sectors as the energy and power sector absorbed nearly 50 percent of all loans granted from 2003 to 2006 followed by transportation and infrastructure with around 25 percent of the total and then by telecom and media with just over 6.5 percent.[14]

2.3 Islamic Project Finance

It is a set of contractual agreements that has the features of conventional project (as mentioned above in introduction) finance minus the features that contradict with *Shariah* complaint finance (as mentioned in preceding paragraph). The IPF is a microcosm of the larger body of Islamic economic and financial system. It employs project evaluation by social well-being as opposed to

[11] Ayub, Mohammed (2007), *Understanding Islamic Finance,* UK: John Wiley, pp 43-57.
[12] Hoffman, Scott L (2008), *The Law and Business of International Project Finance*, New York: Cambridge University Press, pp 4
[13] Gatti, Stefano (2013), *Project Finance in Theory and Practice: Designing, Structuring, and Financing Private and Public Projects*, MA: Academic Press, pp 4
[14] Ibid, pp 22

the conventional project finance which evaluates projects based on the rate of return achievable.[15]

Stefano Gatti (2013) in *Project Finance in Theory and Practice: Designing, Structuring, and Financing Private and Public Projects* discusses the concept of project Finance. It has lucidly explained rather complex theory of project Finance. It has helped the researcher in understanding the conventional project finance which in turn helped in comparing/ differentiating it with Islamic Project finance. Scott L. Hoffman (2008) in *The Law and Business of International Project Finance* discusses this unique financing technique and its operational structure. John Dewar (2011) in *International Project Finance: Law and Practice* has explored the legal issues surrounding the cross-border, multi country projects. It discusses about disputes and conflicts in case of international projects and what would be their legal remedy. It explains the conflict resolution and concepts like litigation and arbitration. This book helps in understanding the legal status of parties involved in infrastructure projects. Anthony Merna et el. (2010) in *Project Finance in Construction: A Structured Guide to Assessment* has discussed about the conventional as well as Islamic project finance. It has conceptualized the whole theory through case building and very well explained. It has also shed light on the growing demands in infrastructure development in Asia. Michael J.T McMillen (2009) in his article Shariah-Compliant Project Finance: A Structural Overview" has discussed about Islamic project finance within the broader spectrum of Islamic finance. The article mentioned above also reviews of the different school of thoughts (madhhab) and the role of *shariah* supervisory board. The study has helped in understanding the nuances of IPF. The work by Maha Gabbani (2009) in *Islamic Project Finance* discussed the convergence and divergence between Islamic project finance and conventional project finance. It has discussed theoretically blending the two and argued that they can be adapted with one another to achieve the same economic efficiency. This study has helped in understanding the technical similarities and differences between the two structures and how the Islamic tranches has been with conventional project finance. Don Babai (1999) in "Islamic Project Finance: Problems and Promises" has observed that in spite of the huge needs and the substantial opportunities, project finance has been relatively more lagged behind when it comes to the development of the Islamic financial industry. With exception of Malaysia, a robust Islamic market for the financing of infrastructure projects has yet to emerge. He has examined various factors both internal and external that have limited the scope of Islamic project finance until then. The factors for such lagging behind have been located as the institutional shortcomings, ranging from the lack of standardization of legal rulings and provisions for liquidity mechanisms. It also discusses some of the ways in which Islamic finance could make distinctive contributions in the area of project finance. This work however old considering a lot has been improved since then has still helped in understanding the how far or less Islamic project finance has travelled.

[15] Noor Amila et el. (2014), *Financing PF2 Projects: Opportunities for Islamic Project Finance*, Fourth International Symposium on Infrastructure Engineering in Developing Countries, vol Procedia Engineering 77 (2014) 179 – 187, pp 4

2.4 Contractual Structures of Islamic Project Finance

A. Istisna - a traditional Istisna is mainly manufacture/construct/build to sale contract as the literal meaning of Istisna suggests. In this type of contract one party undertakes to manufacture a specific asset according to certain agreed specifications, price of the asset and the date of delivery in the beginning. The liability of the purchaser to pay the price and the liability of the developer to deliver the assets are deferred to a future specified date. Although traditional Istisna contracts have been used successfully for infrastructure projects, they effectively require the financiers to enter into a construction contract directly with the contractor. This fundamentally changes the risk profile of a project financing for the financiers who, by entering into a direct contractual relationship with the contractor, would be taking an additional risk in the form of the credit and performance risk of the contractor itself. Because of above mentioned constraint, a variant of traditional Istisna has been developed and market moved towards them.

B. Ijara – Ijara is basically a lease contract done within the Islamic framework. It offers the certainty of regular payments throughout the life of the financing with the flexibility of tailoring payment instalments in a manner that allows for financiers to achieve a profit margin structure comparable to that of conventional financiers.[16]

In case of brownfield projects (existing project), the traditional Ijara is being used. It involves the lease of an existing physical asset and is typically used in the form of a sale and leaseback arrangement which is the case of. In case of greenfield projects and in order to enable the financiers to receive a return during the construction period certain scholars have permitted the use of a forward lease arrangement (known as Ijara Mawsufah Fi Al Thima or Ijara Fil Thimma), whereby advance rental payments are made prior to project completion and actual rental payments commence from project completion. The strict proviso attached by the scholars to the use of forward lease structures is that, if delivery of the asset to be leased never occurs (and therefore the lessee never has the benefit of that asset), the lessor (i.e. the financiers) must refund all advance rental payments that have been made to it by the lessee (i.e. the project company). This obviously presents an unsatisfactory scenario for the financiers and increases the importance of clear remedies under other parts of an Islamic project finance structure such as Istisna or procurement arrangements.

C. Ijara combined with Istisna – In this type of contract, the Istisna part of contract applies to the manufacturing or construction phase of a project and the Ijara part of contract applies to operations phase of the project. It can be elaborated by splitting up the two contractual forms into two phases as, during the construction phase by using Istisna contract, the borrower procures the construction of project assets and then transfers the title of assets to Islamic lenders. The Islamic lenders make the phased payments to the borrower (equivalent to loan advances). During the operation phase, the Islamic lender lease back the assets to borrower using Ijara

[16] Ibid

contract and the borrower makes the lease payments to Islamic lenders (equivalent to debt service).[17]

An Istisna or procurement contract is a contract actually to provide funding whereby payments are made by the Islamic lenders to the borrower (project company or to EPC contractors) during the construction period while an Ijara or Ijara Mawsufah Fi Al Thima enables the Islamic lenders to generate a return from the project. However, it must be noted that forward lease contract is normally made at the same time as the Istisna contract (i.e. at a time when there is no physical asset in existence and its construction is being commissioned) but actual leasing itself does not start until the asset has been delivered. Once the assets have been delivered and leasing has commenced, service arrangements become effective whereby the financiers appoint the project company as its service agent to insure the assets, to be responsible for major maintenance and manage other ownership-related tasks; and any purchase and sale undertaking arrangements (documenting termination and prepayment rights) also become effective once the assets have been delivered.[18]

D. Wakala-Ijara

Under this structure, the borrower is employed as the Islamic lenders' agent or *Wakil* in accordance with the terms of an agency agreement known as a *Wakala* agreement. The *Wakala* agreement more or less fulfills the same function as an *Istisna'a* agreement in the other structure, although being an agency agreement, the contractual relationship between the Islamic finance institutions and the borrower is different. The borrower procures the design, engineering, construction, testing, commissioning and delivery of the assets identified in the *Wakala* agreement as the agent for the Islamic lenders.[19]

2.5 Growth and Development in Islamic Project Finance in the GCC

The origins of IPF deals can be traced back to the early 1990s. It was the Hub River Power Project in Pakistan which used USD 92 million as Islamic tranche for the total USD 1.8 billion project. Since then there have been numerous projects mostly in the gulf countries involving Islamic tranches with increasing size and frequency.[20]

<u>Table 1</u>

[17] Keenan, Richard (2010), *Islamic Project Finance: Structures and Challenges*, accessed on 28 Jan 2015, URL: http://www.chadbourne.com/files/Publication/c4ae820b-24ba-4e5b-9f7d-186814289e7e/Presentation/PublicationAttachment/20d7847a-8644-4b0f-b3e7-19a496eebf22/pfn_Intl_0210.pdf

[18] Latif, Q (2011), *Introduction to Islamic Project Finance*, accessed on 28 January 2015, URL: http://www.cliffordchance.com/briefings/2011/05/introduction_to_islamicprojectfinance.html

[19] Keenan, Richard (2010), *Islamic Project Finance: Structures and Challenges*, accessed on 28 Jan 2015, URL: http://www.chadbourne.com/files/Publication/c4ae820b-24ba-4e5b-9f7d-186814289e7e/Presentation/PublicationAttachment/20d7847a-8644-4b0f-b3e7-19a496eebf22/pfn_Intl_0210.pdf

[20] Global Islamic Finance Report (GIFR) 2010, accessed on 28 Jan 2015, URL: http://gifr.net/gifr2010/contents/ch_12.pdf

List of Islamic Equity Financing (Project Finance)				
S#	**Project Name**	**Project Value (in USD)**	**Year**	**Project Details (if any)**
1	Dolphin Gas Project	7 billion	1999	Project involved production, process, and transportation of natural gas from Qatar's North Field to the UAE and Oman.
2	Equate Petrochemical Plant	2 billion (200 million)	1995	This was one of the first projects to use Islamic finance as a major source of funding on a pari passu basis with conventional financing in Kuwait.
3	Sohar Aluminium Smelter	2.4 billion	2004	Sohar Aluminium took a landmark Greenfield aluminium smelter project in the Sultanate of Oman and is jointly owned by Oman Oil Company, Abu Dhabi National Energy Company.Aluminium project was nonetheless hugely successful in attracting the necessary funding. It took only eight months to obtain full financial close and secure Islamic financing as a significant element of the project – a notable first for Oman.
4	Rabigh Refining & Petrochemical	600 million (total vaue 9.8 billion)	2005	Project involved Islamic tranche as part bigger project financed in KSA.
5	Al Waha Petrochemical	526.55 million	2006	Project involved private petrochemical project in KSA. This was the first project financing in the West Asia which was done on a purely Islamic basis.
6	Yanbu National Petrochemical	846.8 million (total value 3.5 billion)	2006	Project involved Islamic tranche to the conventional project financing deal in KSA.
7	Saudi Kayan Petrochemical Project	10 billion & 644 million as W.C	2006	Project involved financing package for the development of a petrochemical complex (the world's largest) to be built in Jubail Industrial City, KSA. This project financing included an Istisna'a / Ijara tranche which, at the time of signing, was the largest ever Ijara facility provided in a project financing.
8	Shuaibah IWPP / Shuqaiq IWPP	1.83 billion	2010	Project involved independent water and power projects for which part of the financing was raised using Islamic finance in KSA.

9	Arabian Amines	195.4 million	2010	Huntsman Corporation and the Zamil Group's poject involving an ethyleneamines facility in the KSA. This project financing was done on a purely Islamic basis.
10	Sadara Chemical Company in Saudi Arabia	20 billion	2013	This project involves Saudi Aramco's JV with Dow Chemical Company, to build and operate world-scale integrated chemicals complex in Jubail Industrial City, Saudi Arabia. Saudi Aramco in a USD2 billion sukuk issuance by Sadara Basic Services Company on behalf of Sadara, followed by a USD 10.5 billion financing package with loans provided by a combination of the Public Investment Fund of the Kingdom of Saudi Arabia, seven export credit agencies (ECAs) and a diverse range of commercial banks and Islamic financial institutions (participating in both wakala and procurement funding structures).

Source: Collected from various websites.

3. Venture Capital Finance

Venture capital finance is widely considered a significant source of financing for early-stage, innovative, and high growth start-up companies. These companies usually hold significant intangible assets and spend heavily on R&D activities. As a result, external sources of financing for these companies are costly and difficult to obtain. For many of these companies and other unproven and high-risk projects, venture capital may become the only potential source of finance. The focus of Venture capital firms provides development of entrepreneurial skills that help the new firms in startup phase in reaching out to underserved potential market, adding value to the customers, offering innovative solution and hence penetrating into the market and be able to compete. That is why firms in startup phase need venture capital and not just money. For the established firms it is good source of external finance which is otherwise costly.[21]

3.1 Islamic Venture Capital Finance (IVC)

It falls within the same ambit of venture capital finance in principality. The objective of both is to provide the required capital and participates in decision making.[22] The only way the Islamic venture capital could be summarized as it's the venture capital undertaking which is bounded by the Shariah principles viz. prohibition of Riba, Qimar, Maysir in its transactions and thus uses

[21] Elsiefy, Elsayed (2014), "Fundamental requirements for Building an Islamic Venture Capital Fund Model", *Journal of Accounting and Finance Research*, vol. 3(1): 63, accessed on 10 February 2016, URL: www.sciedu.ca/afr

[22] Ibid, pp 58

the modalities accordingly. One argument is that since Musharakah and Mudarabah mode of financing has been practiced as earliest forms of Islamic finance transactions thus the idea of partnership has its roots in pre-Islamic Arab and hence an earliest forms of Islamic finance technique.

Elsayed Elsiefy (2014) in his work *Fundamental requirements for Building an Islamic Venture Capital Fund Mode*l has emphasized on the importance for Islamic venture capital firms in Islamic countries. It criticized the conventional venture capital unwillingness or inability in fulfilling the need facing the Islamic countries such as job creation for youth. It has also criticized the Islamic banking practices that it mainly focuses on Murabaha and not in participatory forms of finance. Finally, it proposes a model for Islamic venture capital firm that should be based on strong legal environment and standardized Musharakah contract and creating an easy exit mechanism which is a real issue in case of IVC. M. H. Khatkhatay (2011) in "Islamic Real Estate Venture Capital in India" begins with the arguement that VC is very close to the ethos of Islamic finance as they both are participatory in nature. It further sheds light on challenges faced by real estate sector in mobilising the large amount of funds from banks and other financial institutions and builds the case for Islamic real estate sector to mobilise funds from Islamic venture capital firms. This paper stresses for real estate to create SPV in order to secure the Islamic funding through debt-like-structures (not like conventional debt). This debt like structures would help in tax saving and would be mutually beneficial for both the investor and investee.

3.2 Techniques and Contracts in Islamic Venture Financing

These are the most commonly used forms of contracts used in Islamic Venture Financing.

A. Mudharabah - It is basically a contract between two parties to finance a business. The parties are divided into mainly two parts; one who solely provides the capital is called *rab al maal* (in this case the venture capitalist or the venture capital firm) and other the borrower of the fund called *mudharib* (entrepreneur) who solely manages the project. If the venture is profitable, the profit will be distributed based on a pre-agreed ratio. In the event of a business loss, it should be borne solely by the capital provider, to the extent of the capital contribution. And the entrepreneur will lose his labour.
B. Musharakah - It is a partnership between two or more parties to do business jointly whereby all parties contribute capital either in the form of cash or in kind. Profits are shared at a pre-agreed ratio while in the event of a loss; the loss shall be shared on the basis of capital contribution.
C. Wakalah - It is a contract where the owner or the provider of the fund called *rab al maal* (here called the Principal) entrust his funds to other party or parties called *wakeel* (in this case Agent) with full or limited authority to act on his behalf, based on the agreed terms and conditions. Pursuant to the *Wakalah* contract, it confers the power and rights to the Agent to act on behalf of the Principal as long as the Principal is alive.

3.3 Growth and Development of Islamic Venture Capital Finance in the GCC

Table 2

Major Venture Capital Deals during the Year 2015		
Client	**Nature of Investment**	**Country**
Delta Company Limited	Acquired 45% stake in specialist contractor for electrical power, transmission and distribution	KSA
24 Buckingham gate, London SW1	Structured and advised on acquisition of prime freehold residential site underdevelopment	London
VCBank Liquidity Programme 2	Shares backed by the prime asset of Jebel Ali Labour Accommodation	UAE

Source: Extracted and prepared from the Consolidated Annual Report for year 2015 of Venture Capital Bank

The projects listed above shows that they are operating across region and cross and even international. Thus, IVC is not confined and can operate in other jurisdictions. It has diverse investment type, and interestingly unlike the conventional venture capital finance that has the tendency to invest and supports the R&D and IT sector more often than other sector. Here, we did not find that cliché. That is understandable from the regions leaning towards real estate, construction and petrochemicals.

Table 3

Investments (selected items) of Islamic Venture Capital Bank			
	30 June 2014	**30 June 2015**	
Items	**Value**	**Value**	**Remarks**
	USD '000	USD '000	
Investment	145,741	163,045	Increase
Investment in association & JV accounted under the equity method	27,847	27,816	Status quo
Investment in property receivables	31,335	27,345	Increase
Funding to Project companies	14,083	13,860	Decrease

Source: Prepared from Annual Report of 2014-15 of Venture Capital Bank

Table 4

Investments (selected items) of Islamic Venture Capital Bank in GCC region			
	30 June 2014	**30 June 2015**	
Items	**Total**	**Total**	**Remarks**
	USD '000	USD '000	
Investment	79,857	83,464	Increase
Investment in association & JV accounted under the equity method	26,514	26,704	Increase
Investment in property receivables	16,386	15,823	Status Qou
Funding to Project companies	4,665	4,707	Increase

Source: Prepared from Annual Report of 2014-15 of Venture Capital Bank

Table 3 shows the level value of Islamic Equity Investments however it is mainly consists of IVC investments but researchers make now such assumptions. Without the inadequacy of information regarding which form of Islamic financing has been used, it is still enough to make out the presence of Islamic Equity financing and at such volumes. Table 4 shows the Islamic Equity financing within GCC region exclusively as table 3 includes the investments made outside of GCC for the year ending 2014 and 2015. Hence, these empirical evidences give enough insight into the contemporary Islamic Equity Finance prevalent in GCC that it is increasing leaps and bounds and ready to enter new markets.

Islamic finance has evolved and emerged in the last few years as an alternative mode of finance and has now become a full-fledged industry making its way from retail banking to investment banking. In this section the researcher will try to consider the Islamic equity financing in the GCC with the help of some empirical evidence from the industry. With growth in the sectors like energy, power, infrastructure and other projects in the West Asia (particularly the GCC), there is a concern that international banks, which provide the majority of financing for such projects, may not fulfill the demand and be unable to provide finance due to their own specific risk-allocation ceilings. This issue can be addressed by diversifying the funding techniques used in project financings so far and look for alternatives. A key cornerstone of the Islamic finance industry has been the development and growth of the *sukuk* market - a market that has global reach and appeal to both Muslim and non-Muslim investors. However, the use of *sukuk* in project financings has been not been fully exploited, it is expected that a newer project will also look to raise capital through the capital markets by way *sukuk* issuance.[23]

[23] Latif, Q (2011), *Introduction to Islamic Project Finance*, accessed on 28th January 2015, URL: http://www.cliffordchance.com/briefings/2011/05/introduction_to_islamicprojectfinance.html

4. Implications for India

The prospect of Islamic equity finance can also be seen further in infrastructure, petrochemical, hydropower generation, real estate development and newly launched start up by the government of India. The rationale of choosing these sectors are firstly these are the most important sectors considering the shape, size and requirements of our economy, secondly these are the sectors which are compatible for gulf investors which can be tapped into via Islamic venture capital firms.[24]

In recent years the Government of India is in search of foreign investment and what India can give back to them is definitely politically stable environment which is highly friendly of foreign investments. In 2008, the committee on financial sector reforms chaired by Dr. Raghuram G. Rajan organized by RBI he opined for the closer look into the issue of financial exclusion of certain community and hence into Interest free banking. But it is only recently in September 2016 that a committee for recommendations on medium term path on financial inclusion has been organized by Reserve bank of India. The committee in its report with subject 'Policy and framework for financial inclusion' in its fifth clause and onwards has given positive recommendations towards establishment of interest free financial institutions. Moreover, the world faced and is still facing financial crisis and India has been resilient to large extent with could be translated into a stable rate of return on investments and so on and so forth. In this context this paper argues that there is a synergy between the India's demand of fund and Islamic venture capital firms especially in GCC as a source of fund.

One of study in this context has laid that there is significant value of *'Infrastructure Funding Deficit'* in India and it has been estimated to be around INR 14, 60,784 crores. It is 22.47 % of total required investment for Infrastructure development in India.[25] It can be argued that such a huge demand of fund which has no other source of funding can be met by pooling-in the Islamic tranche of funding. According to one of the study shows that the power project of INR 55.5 billion by an Indian Enterprise namely Adani Power Maharasthra was the largest deal in the region and the second largest transaction globally. This has attracted Islamic finance projects analyst as they see emerging scope of *Shariah* based project finance in India.[26]

For a country like India where there is huge scope for infrastructure development right from roads, sewage, highways, stadium to school, hospitals and heavy industries. If this technique of Islamic Project Finance is to be considered, the major challenge is to streamline some acts such Indian Banking Act. Apart from that awareness among the users regarding how it works.

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[24] Khatkhatay, M. H. (2011), "Islamic Real Estate Venture Capital in India", paper presented at IOS seminar on VCF's at Parliament Annexe, New Delhi, pp 1

[25] Majeethia, Y and T. Bosh (2014), "Islamic Financial Instruments an Opportunity for Financing Infrastructure in India", *Journal of Business Management & Social Sciences Research*, vol. 3 no 5, pp 18-25

[26] Merna, Anthony et al. (2013), *Project Finance in Construction: A Structured Guide To Assessment*, New Delhi: Wiley-Blackwell, pp 3

5. Issues and Challenges

The Islamic Project Finance faces multi-faceted issues via-a-via commercial, political, legal, technological and environmental and so on. Since the Islamic project finance is amalgamation of two different frameworks hence it faces the challenges associated with both the Islamic project finance in addition to the inherent challenges of conventional project finance. There are some key challenges such as that of development of economically viable structure and efficient mechanism that can address issues pertaining to double taxation and stamp duties, risk management of the assets owned by Islamic financier in the absence of Insurance.

The Project finance is a multi-party, multi-contract often cross-border, multi-jurisdictional contract. Thus it is vulnerable to multiple risks. These risks could be bundled into two major categories such as commercial and political risk. These risks may give rise to disputes in case a default takes place. In the instance of disputes which can be attributed to commercial risk, there is the following legal remedy available. Such a dispute could be resolved under one of the two legal frameworks: Litigation and Arbitration.

Litigation is seeking to resolve the dispute in national courts (of the host state or some other state). Arbitration is taking it to some International Arbitration Institute. In practice the parties already put in a clause which states which legal framework they want in case of dispute. If a project has a jurisdiction clause, it will permit or require parties to pursue claims in one or more national courts which parties will choose. If a project has arbitration clause, it will require parties to submit disputes to final and binding determination by a non-government decision-makers. Both the framework has its own pros-cons and each project has to be analyzed individually before choosing any of the two frameworks. However, there is lot of ambiguity as to legal matters, the steps have been taken such as the creation of International Islamic Centre for Reconciliation and Arbitration (IICRA) in UAE.

Disputes arising out of Political risk: This is not very significant in here as the political risk mainly arises out of regime change and GCC states are politically quite stable so far. However, the formation of the GCC in itself is one important measure in strengthening and bringing greater uniformity in regional economy. Now, the intra-GCC Projects will be smoother owing to various treaties signed among GCC states. The creation of such organization like EU, ECA, OHADA help minimize political risks to greater extent by standardization of corporate procedures and policies. And even then if disputes arises (which is very probable in these big projects), there is a degree of ease in addressing such disputes.[27]

6. Conclusion

It has been seen even after an unprecedented growth in Islamic finance industry whose core lies in the equity financing, still industry have started to look into it in last decade only. However, there has been tremendous growth infrastructure, construction, real estate sectors. It has not harnessed or contributed to that extent and conventional finance is still dominant. Nonetheless, our empirical evidence shows that from last Islamic equity finance has emerged and impacted in the GCC. It even emerged as an alternative source of finance at one point of time when there was liquidity crisis in the aftermath of 2008 crisis. We also found that Islamic equity is effective in

[27] Dewar, John (2011), *International Project Finance: Law and Practice*, New York: Oxford University Press

certain sector more than in others. Our analysis shows that Islamic finance which has unique agenda of socio-economic development and equity finance at its core, must stick to it. It will help Islamic equity finance to develop in more concrete way and keeping its uniqueness alive.

Pursuant to this, we propose that developing countries like India where there is an ample investment opportunities in real/tangible business activities, the Islamic venture capital ought to diversify towards these markets. Theoretically there is a synergy between the two. Also, with the expected policy reforms in India, one of the greatest challenges will be partly resolved and Islamic financial institutions would be legalized in India.

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