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SUKUK VALUE AND ITS FACTOR DETERMINANTS IN MALAYSIAN ISLAMIC CAPITAL MARKET

Noriza Mohd Saad[1*]
Dila Sharina Yusri[2]

[1]Faculty Business and Management, Universiti Teknologi MARA, Kampus Machang Cawangan Kelantan, 18500 Bukit Ilmu Machang, Kelantan, Malaysia, (E-mail: noriza@uitm.edu.my)
[2]Faculty Business and Management, Universiti Teknologi MARA, Kampus Kota Bharu Cawangan Kelantan, 15050 Kota Bharu, Kelantan, Malaysia, (E-mail: 2023781843@isiswa.uitm.edu.my)
*Corresponding Author

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Abstract: *Malaysian Islamic capital market is a market leader in sukuk issuance compared to other capital market in the world. Thus, the objective of the study is to investigate the relationship between sukuk value of issuance with its factor determinants since this medium term and long term debt instrument facing a challenge in reducing default risks during turbulent economic situation. This study uses secondary data. The data are gathered from year 2000 to 2023 with full completed number of observations only be considered for 2840 observations. Multivariate regression are utilized for such relationship impact between sukuk value and its independent variables. The results postulated that positive real gross domestic product (real GDP), longer years to maturity and real interest rate spreading is significant positive relationship with sukuk value issuance in Malaysian Islamic capital market, thus can attract new investor and enhances existing investor confidence and reduces credit and default risks. Inversely negative growth may signify economic instability that could affect market sentiment among stakeholder.*

Keywords: *Sukuk Value, GDP, Inflation, Real interest Rate, Multivatiate Regression*

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Introduction

Capital Market Masterplan (CMP1) was come out with a total of 152 recommendations include establishment of Malaysia as an international Islamic capital market centre. This has reduced concentration and maturity mismatch risks as well as provides greater avenues for the financing of large scale projects (CMP2, SC, 2011). Considering to this scenario, SC was introduce Policies and Guidelines on Issue/Offer of Securities (Issues Guidelines) in July 1998 for additional capital-raising flexibilities. Besides, there are further action taken place by formation of the National Economic Recovery Plan (NERP) in 1998 highlighted the need for broad, deep and well-developed bond market that would provide a more stable source of financing which would also diversify the risks associated with cyclical economic bearish.

In addition to that, SC are not free hand to release various legislations as well as rules such as Capital Markets and Services Act 2007, Sections 212(2)(a) and 212(4), guidelines such as Guidelines on the Offering of Islamic Securities and Guidelines on the Registration of Bond Pricing Agencies in July 2004 and January 2006 respectively and practices notes such as Recognition of Credit Rating Agencies in January 2006 for the purpose of rating bond issues. Besides, Minister of Finance (MOF), Bank Negara Malaysia (BNM) and Rating Agency Malaysia (RAM) are also regulators which are monitoring the Malaysian capital market performance.

Furthermore, successful formation of CMP1 covered from 2001 to 2010 as a long term blueprint for capital market development and CMP2 (2011-2010) by regulators give a good roadmap to issuer and investor in their trading mechanisms. CMP2 focused on ensuring robust governance arrangements to manage risks to investor protection and stability is a proactive strategy in case of default for both sukuk and conventional bonds since they are in similarities of some characteristics such as ratings, yields, maturity date, size of issuance and coupon or profit rate (Mohd Saad, et.al. (2020; 2023). Next, the CMP 2021-2025 and NIP 2030 ensuring the sustainable and responsible investment (SRI) for sukuk investment for Malaysia. The high percentage recorded by Malaysia sukuk issuance gives it a dominant position in sukuk by the size of issuance denominated by Malaysian Ringgit (MYR). Besides, the stabilization of global liquidity, economic growth and high financing needs in core Islamic finance countries significantly increased sukuk issuance in 2023 with forecast of $160-$170 billion in 2024 (Damak, 2024; Mohd Saad, et. al, 2025). Thus, the relationship between sukuk value of its issuance and the factor determinants especially on economic variables is significantly to be research for long term investment in Malaysian Islamic capital market.

The reminder of this paper will be discuss the past studies related to sukuk issuance in Malaysia and at global capital market with its factor determinants, follow by data collection and research methodology applied, then proceed with findings discussions and concluding remark.

Literature Review

The connectedness between sukuk investment and its factor determinants especially on macroeconomics variables discussed in this part. There are mixed results associated by many studies between dependent and independent variables used in this study, mostly because of the types of the debt instrument itself either Islamic or conventional debt. Liu & Skully (2005) found that securitisation and mortgage yield spreads differentials among four groups of Australian mortgage providers (mortgage corporations, commercial banks, building societies

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and credit unions) through 2262 observations from 180 institutions in 2001 are positively associated with both small and large loans size. The largest loans may have higher credit risk, requiring over 20 basis points higher than its reference. In contrast, the smallest loans do not have economies of scale and are more costly, requiring around ten basis points higher than its reference. This links to credit policies of the lender in origination. These costs of credit include borrowing cost for corporate bonds which have two major components, the rebate rate paid by the lender and the market interest rate (Asquith, Au, Covert & Pathak, 2013). Asquith et al. (2013) and Chen et al. (2016) reports that bond borrowing costs are related with controlling variable, loan size.

Next, Manconi, Massa & Yasuda (2010; 2012) studied yield spreads for conventional bonds and mutual fund and insurance companies and found that trading volumes impact corporate bond yield spreads. They found that the institutional investors' (i.e., mutual funds and insurance companies combined) net trades and bond yield spreads were positive in the pre-crisis periods. However, an inverse relationship is reported when net sales are associated with yield increases in the crisis periods. The impact from these changes in yield was investigated further by looking at the spread of both yields. The result revealed that yield spreads and bond sales volume increased more for corporate bonds held immediately before the crisis by mutual funds with heavy exposure to securitised bonds, compared to same-issuer bonds that were held by unexposed mutual funds. They claimed that issuer variation in yield spread changes proves a sharp increase in credit spreads of corporate bonds. Mutual funds with high liquidity needs were left with exposure to the now illiquid securitised bonds and played a significant role in spreading the crisis from the securitised bond market to the seemingly unrelated corporate bond market. Elyasiani, Jia & Mao (2010); Mohd Saad, et. al (2020; 2025) have shown that bond yield spreads is negatively related to issue-size.

There is no difference between tenure for sukuk and conventional bonds whereby both can be issued for medium-term or long-term in the capital market as stated in Bondinfohub in Bank Negara Malaysia by using a symbol of IMTN and IBond and MTN and Bond respectively. A longer tenure of maturity leads to huge uncertainty and volatility of bond prices and yield spreads and could mean huge possible return or loss (Jones, Lamont & Lumsdaine, 1998; Rusgianto & Ahmad, 2013). Aloui, Hammoudeh & Hamid (2015a) investigate the co-movement pattern between sukuk and conventional bonds reported that the patterns do not seem to behave differently in regard to frequency and time. Aloui, Hammoudeh & Hamid (2015b) report that there is negative relationship between shariah stock and sukuk on daily for 5-years data covering the period from July 10, 2008, to July 13, 2013.

Custodio, Ferreira & Laureano (2013) and Mohd Saad, et. al (2020) explained the relationship between the tenure of debt investment with the default risk. They used debt-maturity in US industrial firms from 1976 to 2008 for a total of 97215 observations from 12938 firms. Their result postulated that shortening of debt-maturity had increased the exposure of firms to credit, and liquidity shocks since firms with higher abnormal earnings have better projects and are expected to issue short-term debt as a signal of good quality.

Then, the decision to issue and hold short-term, medium-term or long-term debt is one of the factors that needs to be considered when the firm decides to issue to avoid any default risk in future. As reported by Loffler (2004), the association between holding period strategies took

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one, three and five years to reduce default risk. This shows that the strategy yields smaller losses than each of the strategies that favour the longer period of five years. McEnally & Ferri (1982) studied the relationship between risks of corporate bonds and found it related negatively to rating besides justifying duration is superior to coupon as a dominant factor in influencing betas benignly.

With respect to the yield spreads, Elyasiani, Jia & Mao (2010) found that bond yield spreads are positively related to bond age. They claimed that YTM is the length of time (in years) before the bond matures and are positively related to the cost of debt. As argued by Helwege & Turner (1999), through the theory of liquidity premium bonds with longer maturities have a greater risk. This study is consistent with Chen et al. (2016) also revealed that controlling variable as proxy by maturity period have significant positive relationship with firms' cost of debt.

On the contrary, Bhojraj & Sengupta (2003) found a significant positive relationship between bond age with bond yields. Consistent with Fields, Fraser & Subrahmanyam (2012) also reported a significant positive relationship between bond age and yield spreads. The results pointed out about the higher cost of debt beared by the issuer and the likelihood to be default is also high.

Inflation is another critical factor that influences sukuk investment. High inflation rates can erode the purchasing power of returns on sukuk, making them less attractive to investors. However, some studies suggest that moderate inflation may not significantly impact sukuk investment, as long as it remains within controllable limits (Basyariah et al., 2021). The relationship between inflation and sukuk is complex, as it can vary depending on the overall economic context and investor expectations.

Data Collection and Research Methodology

This study uses secondary data. The data are gathered from year 2000 to 2023 with full completed number of observations only be considered for 2840 observations. Measurement of the sukuk value issuance is based on the total value of tranche issuance in Malaysian Ringgit (MYR). The figure has been logged (lnSukukValue) because the data provided in Bondinfo hub is in millions. Tenure of the sukuk issuance with proxy by years to maturity also were gathered from the same data sources. Independent data variables with regards to the real GDP, inflation and real interest rate was gathered from department of statistics, Malaysia's website. This variables has been considered based on past studies that highlight the significant impact of the independent variables in explaining the relationship with sukuk value of investment.

Next, to achieve the objectives of the study to analyze the relationship between sukuk value issuance with its factor determinants, this study run a multivariate regression using the model regression equation as follows:

$$\ln SukukValue_{it} = \beta_{it} + \beta_1(Yearstomaturity_{it}) + \beta_2(\mathrm{Re}alGDP_{it}) + \beta_3(Inflation_{it}) + \beta_4(\mathrm{Re}al\,\mathrm{int}erest) + \varepsilon_{it}$$

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Where:

β_{it} = the coefficient estimates in constant of the explanatory variables

$\ln SukukValue_{it}$ = the sukuk size of issuance of the companies for the year,

$RealGDP_i$ = the gross domestic product growth for the year,

$Inflation_i$ = the consumer price index for the year,

$IRspread_i$ = the real interest rate spreading for the year.

Results and Discussion

Table 1: Descriptive Statistic Results

Variable	Obs	Mean	Standard Deviation	Minimum	Maximum
lnSukukValue	2,840	17.894	1.778	12.341	23.249
Years to Maturity	2,819	7.534	6.323	0	50
Real GDP	2,840	4.785	1.714	-5.457	8.859
Inflation	2,840	2.298	.935	-1.139	5.441
Real InterestRate	2,840	2.630	2.589	-3.903	11.782

Table 1 report on the descriptive statistic results for the dependent and independent variables for maximum of number of observations of 2840 to all dataset except for years to maturity is for 2819 observations. The natural log of sukuk value (lnSukukValue) has a mean of 17.894 with a standard deviation of 1.778, indicating moderate variability in valuations across the issuance. The range spans from 12.341 to 23.249, reflecting the diversity of sukuk issuances, from smaller-scale instruments to high-value sukuk likely tied to large infrastructure or government-backed projects.

The years to maturity variable has a mean of 7.534 years and a standard deviation of 6.323 years, highlighting significant variation in Sukuk maturities. The minimum tenure of 0 years likely represents short-term Sukuk designed for liquidity, while the maximum of 50 years aligns with long-term investments commonly used for infrastructure or sovereign funding. This wide range indicates the flexibility of Sukuk in catering to both short-term and long-term investor preferences. The variability reflects market dynamics in regions like the GCC and Southeast Asia, where both short-term and long-term instruments play a significant role in capital markets.

Real GDP exhibits a mean of 4.785 with a standard deviation of 1.714, indicating moderate variability. The range extends from -5.457, reflecting periods of economic situation for up and down crisis, to 8.859, signaling economic growth is still under stable condition. Real GDP with positive sign is generally connected to good performance in sukuk value issue by listed companies or government, as it enhances investor confidence and reduces credit risks, whereas negative growth may signify economic instability that could affect market sentiment.

Inflation, with a mean of 2.298% and a standard deviation of 0.935%, indicates low to moderate inflationary pressures. The range spans from -1.139% (deflation) to 5.441%, capturing varied economic conditions across the sample. Moderate inflation rates, as observed in many emerging markets, often support stable financial environments conducive to Sukuk issuance.

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However, periods of deflation or high inflation could introduce challenges, influencing investor sentiment and the relative attractiveness of Sukuk as investment instruments.

The real interest rate has a mean of 2.630% and a standard deviation of 2.589%, reflecting substantial variability. The range from -3.903% (negative real rates) to 11.782% captures diverse monetary policy environments, from expansionary policies aimed at stimulating growth to contractionary measures designed to curb inflation. This wide range highlights the sensitivity of Sukuk markets to interest rate changes, although their asset-backed and profit-sharing structures provide resilience compared to conventional bonds.

In summary, the dataset demonstrates significant variability in years to maturity, GDP, inflation, and real interest rates, reflecting diverse economic and financial conditions influencing Sukuk markets. Sukuk value itself shows moderate variation, aligning with its adaptability to different market needs.

Table 2: Pairwise correlations Results

Variable	lnSukukValue	Tenure	Real GDP	Inflation	Real IntRate
lnSukukValue	1.0000				
Years to Maturity	0.1500	1.0000			
Real GDP	0.1770	0.0078	1.0000		
Inflation	0.0825	0.0539	0.4851	1.0000	
Real InterestRate	-0.0501	-0.0331	-0.5684	-0.6205	1.0000

The correlation analysis reveals a positive relationship between sukuk value (lnSukukValue) and tenure (r=0.1500), suggesting that longer maturities are associated with higher Sukuk valuations. This finding aligns with the Time Value of Money, which posits that longer maturities enhance present value by providing stable cash flows over time. Longer-tenure sukuk are often preferred by institutional investors such as pension funds and sovereign wealth funds, as they offer predictable returns and lower reinvestment risks. Supporting studies, such as Sa'ad, Muneeza, Haron and Othman (2022), highlight the appeal of long-term sukuk in diversified portfolios, while Mohd Saad et. al (2020), Mohd Saad et. al (2025) emphasize their importance in markets with robust regulatory frameworks. For issuers, designing medium- to long-term sukuk can align with investor preferences and maximize valuations, particularly in regions with significant infrastructure funding needs, such as the GCC and Malaysia.

Real GDP (r=0.1770) also shows a positive correlation with sukuk value, reflecting the critical role of macroeconomic stability in fostering investor confidence. Economic growth enhances the ability of issuers to meet financial obligations, reducing perceived risks and attracting investors. Policymakers should focus on fostering GDP growth to support sukuk markets, while issuers can strategically time sukuk issuances to coincide with periods of economic expansion. While, inflation (r=0.0825) exhibits a weak positive correlation with sukuk value, indicating a limited but positive effect. This relationship can be attributed to sukuk's asset-backed nature, which provides a hedge against inflationary pressures by tying returns to tangible assets. The Inflation Hedge Theory supports this observation, suggesting that real asset-linked instruments maintain value better than nominal instruments during inflationary periods. When, inflation's direct impact on sukuk valuation appears minimal, issuers can position sukuk as resilient

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investment options in inflationary environments to attract risk-averse investors seeking protection against rising prices.

The interrelationships among the independent variables provide additional insights into macroeconomic dynamics affecting sukuk valuation. The moderate positive correlation between real GDP and inflation (r=0.4851) reflects the interconnectedness of economic growth and price levels, underscoring the need for balanced monetary and fiscal policies. The strong negative correlation between real GDP and real interest rate (r=−0.5684) suggests that economic growth is often accompanied by lower real interest rates, benefiting sukuk valuation and issuance. Similarly, the inverse relationship between inflation and real interest rate (r=−0.6205) highlights the role of monetary policy in managing inflationary pressures while maintaining stable interest rate environments. These interdependencies suggest that policymakers should aim for macroeconomic stability to create favorable conditions for sukuk markets.

Multivariate Regression Results

Equation	Obs	Parms	RMSE	R-square	F	P
lnSukukValue	2,819	5	1.724	0.9908	60676.49	0.000

lnSukukValue	Coef.	Std. Err.	t	P>|t|	[95% Conf.	Interval]
Years to Maturity	.042	.005	8.17	0.000	.032	.052
Real GDP	.222	.023	9.46	0.000	.176	.268
Inflation	.055	.045	1.22	0.224	-.034	.144
Real InterestRate	.064	.017	3.71	0.000	.030	.098

The multivariate regression results provide insights into the relationships between sukuk value (lnSukukValue) and its independent determinants: years to maturity, real GDP, inflation and real interest rate. The model demonstrates an R-square value of 0.9908, indicating that 99.08% of the variability in sukuk value is explained by the independent variables included in the model. This exceptionally high R-square suggests a strong explanatory power of the model, underscoring the robustness of the selected determinants in capturing the variations in sukuk valuation. The model's overall significance is confirmed by an F-statistic of 60,676.49 and a p-value of 0.000, indicating that the independent variables collectively have a significant impact on sukuk value.

Tenure (β=0.042) demonstrates a positive and statistically significant relationship with sukuk value, as evidenced by a t-value of 8.17 (p=0.000). This suggests that each additional year of sukuk maturity increases the natural logarithm of sukuk value by 0.042 units, holding other factors constant. The significance of the t-value indicates that tenure is a meaningful predictor of sukuk valuation. This relationship aligns with the theory of Time Value of Money, which emphasizes the value of longer maturities in providing stable and predictable returns. Longer-tenure sukuk appeal to investors seeking portfolio stability, particularly institutional investors like pension funds. Previous studies, such as Mohd Saad et. al (2020), Sa'ad, Muneeza, Haron and Othman (2022), Mohd Saad et. al (2025) have similarly noted the positive effect of tenure on sukuk valuation in markets with high demand for long-term investments.

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Real GDP (β=0.222) exhibits a strong positive relationship with sukuk value, with a t-value of 9.46 (p=0.000). This indicates that a one-unit increase in real GDP corresponds to a 0.222-unit rise in lnSukukValue, holding other factors constant. The high t-value reflects the significance of GDP as a driver of sukuk valuation. Macroeconomic stability, as captured by GDP growth, enhances investor confidence and reduces default risks, making sukuk more attractive. The Macroeconomic Stability Hypothesis supports this finding, suggesting that robust economic growth fosters the demand for financial instruments like sukuk.

Inflation (β=0.055) has a weak positive relationship with sukuk value, but its t-value of 1.22 and p=0.224 indicate that this relationship is not statistically significant. The lack of significance suggests that inflation does not directly affect sukuk value in this dataset. This result aligns with the Inflation Hedge Theory, which posits that sukuk's asset-backed structure inherently buffers against inflationary pressures, preserving their real value. While inflation's direct effect is minimal, its indirect impact on investor sentiment and macroeconomic stability may still influence sukuk markets.
Real Interest Rate (β=0.064) exhibits a positive and statistically significant relationship with sukuk value, as evidenced by a t-value of 3.71 (p=0.000). This indicates that a one-unit increase in real interest rate results in a 0.064-unit rise in lnSukukValue, holding other factors constant. The significance of the t-value reflects the unique behavior of sukuk compared to conventional bonds, which typically lose value as interest rates rise. Sukuk's asset-backed nature and profit-sharing mechanisms mitigate sensitivity to interest rate fluctuations, providing stability in volatile monetary environments.

Conclusion and Policy Recommendations

The implications of these findings extend beyond industry allocation and into broader policy considerations for Islamic financial regulation, market development, and economic sustainability. As Malaysia continues to position itself as a global leader in sukuk issuance, policymakers must address key structural challenges to ensure that sukuk remain an inclusive and dynamic financial instrument for national and regional economic development. Another critical policy consideration involves improving secondary market liquidity for sukuk, which remains a key constraint compared to conventional bonds. The illiquidity of sukuk secondary markets can deter investors, leading to reduced market efficiency and higher issuance costs. Improving sukuk market liquidity is crucial for fostering a more vibrant secondary market. Sukuk trading infrastructure should be enhanced by establishing digital sukuk marketplaces, integrating blockchain-based trading mechanisms, and introducing market-making incentives to boost liquidity. Additionally, expanding investor education programs would increase awareness of sukuk investment opportunities, particularly among institutional investors, sovereign wealth funds, and retail investors. The successful implementation of these strategies would not only strengthen Malaysia's position as a global leader in sukuk issuance but also contribute to broader economic growth, financial stability, and sustainable development.

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