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MARKET STATEMENT

Established in 1994 and operating in the Structured Finance arena, **BSEC - Bemo Securitisation SAL** was the first MENA financial institution to introduce locally structured securitisation, credit derivatives and cross-border structured finance.

NewsWire is a monthly private newsletter of **BSEC** focusing on securitisation news and analysis in Lebanon and the MENA/GCC countries; It puts into perspective the different issues pertaining to securitisation in the legal, financial, tax and accounting fields.



A-SECURITISATION NEWS

CARAVAN-I SUKUK (SR103 Million)

BSEC SET TO LAUNCH THE FIRST AUTO-BACKED SECURITISATION

Lebanon-based BSEC - Bemo Securitisation SAL, the leader in MENA securitisation, is set to launch a SR103 Million Shariah compliant securitisation. CARAVAN-I Limited is the region's first Auto-Backed Sukuk deal. The 3-year maturity transaction offers the Islamic investors 6% return paid on a monthly basis. The transaction is backed by a pool of vehicles and lease agreements sold by HANCO Rent A Car, one of Saudi Arabia's leading car leasing and rental companies. BSEC worked with key advisors on the structuring of the two-tiered transaction. Baker & McKenzie acted as KSA counsel and Volaw/Voisin as Jersey counsel. Shariah compliance was provided by Yasaar Limited UK. BSEC is currently in underwriting discussions with several regional Islamic Financial institutions. Ibrahim A. Mardam-Bey, Executive VP

at BSEC, explained the elements behind the transaction: "The Islamic Banking sector is experiencing rapid growth and fuelling a demand for new product structures. At the same time many of the region's companies are looking for alternative financing resources. The CARAVAN-I Sukuk is an innovative structure that meets the requirements of both, our client and regional investors". Iad Georges Boustany, Managing Director of BSEC, said: "Family business groups are focusing on shareholder value, transparency and management structures, as they prepare their companies for the institutionalization era. Our specialization in securitisation allows us to offer unique financial tools to address these issues. Securitisation, by converting illiquid assets into marketable

securities, adds value to both, the corporations and the capital markets". The CARAVAN-I Sukuk has several structuring and credit enhancement features: A two-tier two-jurisdiction structure with 16.96% overcollateralisation, 4.75% equity tranche and 8.73% cash reserves. The structure also benefits from embedded early warning triggers mitigating its performance risk. By targeting SMEs in the MENA region, BSEC is demonstrating its ability to arrange and structure transaction often overlooked by international banks due to their size. "We believe we can serve an underserved market, provide best in class financial structuring know-how and achieve cost efficiencies for our clients and investors", Boustany added. ■

B-SECURITISATION ANALYSIS

FINANCIAL: EMERGING MARKETS FUTURE FLOW SECURITISATION



The commonly known Future Flow Securitizations are structured finance transactions that rely on the fact that the asset transferred by the originator is a future claim against future obligors. In other words, it's the future generation of assets or services that provides the cashflow for the repayment of debt. Examples for that kind of transactions would be public finance, export receivables, hotel revenues, etc. Most future flow

securitizations are issued in emerging markets where the international rating of the originator is capped at the rating of the country. Since 1991, 249 transactions have been completed totaling \$48.7 billion in origination. 1996 was the peak period witnessing 21 deals totaling \$9.0 billion. From 1999 many factors contributed in changing the market, notably reducing issuance with the drop-off in big oil deals from two large issuers (the Mexican PEMEX and the

Venezuelan PDVSA); the involvement of monoline insurers who have wrapped 43% of the total issuance since 2000 versus 14% in 1996-1999; the emergence of the financial remittance segment consisting of deals originated by banks located in emerging countries with hard currency cash flows; and finally the introduction of the political insurance as a means to mitigate sovereign risk. (Source: *Wachovia Securities Research*)■

TAX AND ACCOUNTING: TAX ISSUES IN SAUDI ARABIA



A new tax resolution is issued by the Saudi Ministry of Finance on the 7th of October 2003, according to which interest paid to non-resident banks and lending entities will be taxable, which was not the case previously. This resolution confirms that the income earned from lending transactions will be imposed to tax if: (i) the loan is secured by moveable or immoveable property in

Saudi Arabia, (ii) the borrower is resident in Saudi Arabia, and if (iii) the loan is associated with an activity carried out in the mentioned country. However, the commonly known annual income tax (Zakat) is applied on registered entities in Saudi Arabia whether Saudi owned or foreign owned or part Saudi and part foreign. If companies or partnerships are owned by Saudi or GCC

nationals and by other foreigners, Zakat is applied on the Saudi or GCC nationals' share of the Zakat base, and taxes are imposed on the foreign share of income. Zakat is charged at a rate of 2.5% on capital and long-term liabilities that is not invested in fixed assets or long-term investments and on pre-incorporation expenses■

LEGAL: FIDUCIARY AND TRUSTS: THE WAY FORWARD

Continued from NewsWire Issue N.8, November 2003):



With regard to the trust recognition, we mentioned in a previous issue of this News Wire (Issue 4) that the Lebanese legal system does not contain a text on this subject, but that some published judicial decisions have recognized the trust established abroad and have given full effect to its provisions. Such recognition is of major importance not only for purely trust matter (normally related to estate

planning) but also for structured finance: The trust is regularly used in securitization transactions, and any doubt on the validity of one of the links would have endangered the viability of the whole chain. The ratification by Lebanon of the Hague Convention of July 1st, 1985 will definitely clarify this issue and give solid ground to the Lebanese courts in future cases, which will in turn consolidate the securitisation structures involving foreign trusts. As for the fiduciary contracts, Article 4 of the new

Luxembourg law provides expressly that the law applies to fiduciary contracts where the "*fiduciaire*" (trustee) is, *inter alia*, the management company of a securitisation fund. This means that, according to Article 5, the securitisation fund receives assets from the "*fudiciant*" (settler) and becomes the owner thereof, subject to some conditions and obligation agreed by the two parties■

C-SECURITISATION COMMENTARY

SPECIAL FOCUS ISLAMIC SECURITISATION: MUDARABA STRUCTURE



The term Mudaraba is based on the union of those who have capital with those who have expertise; a Mudarib becomes the user of the capital of an investor and as an entrepreneur, he contributes management input which is viewed as a form of capital. In this sense Mudaraba structure combines financial experience with business experience since one party provides capital and the other provides labour with the purpose of earning *Halal* profit applied to the banking sector. Banks will then provide capital and

clients provide the expertise, and the profit will be shared according to the agreed ratio. Advanced funds must not be recognized as debt or liability to the Mudarib, being sometimes referred to as the Trustee and it would be interesting to investigate similarities between such a scheme and "Société en Commandite". Applied to structured finance and securitisation, in a Mudaraba scheme, the SPV would be the capital owner and contribute the capital whereas the Originator/Service provider would be the Mudarib and would provide its experience and services. The majority of the

Islamic Scholars require that in a Mudaraba the capital owner contribute the capital in cash. Certain Scholars, including certain Scholars within the Hanbali School of Islamic Jurisprudence, do allow for the capital owner to contribute capital in kind (i.e. merchandise) provided that value is mutually agreed at the time of the contract. The agreed value becomes the capital of the Mudaraba. Most of the Scholars who allow in kind contributions, however, require the business of the Mudaraba be the sale and purchase of the relevant merchandise. ■

READINGS OF THE MONTH

"ABS SUCKED INTO INVESTOR CAMPAIGN", INTERNATIONAL SECURITISATION REPORT, Issue 82, November 2003, p.6



A group of European investment institutions published a campaign document expressing investors' complaints; these complaints insisted mainly on improving the sterling and the euro fixed income credit markets, addressing issues like refining documentation, increasing disclosure and requiring covenants to protect necessarily against asset sell-offs. The lack of covenant protection against event risks increases market volatility and hampers liquidity. The document concerns essentially the corporate bond market; investors stated that "the

position of senior unsecured debt instruments should be protected by a restriction on the ability of the issuer to pledge assets, securitise cash flows or enter into any other contracts that subordinate unsecured bondholders". They also stated that in order for bonds to rate as senior unsecured they must have no more than 20% of total liabilities ranking ahead of them. However, negative pledges should not be structured in a way to inhibit securitisation, a fact that also impacts the originators' ability to securitise, due to the effect it has on their unsecured debt. Given that, a

corporate issuer may consider funding in secured or securitisation market in order to achieve better pricing while "being subject to the same extent of covenant restrictions" ■

D-CONTACTS AND DISCLAIMER

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