**Islamic Bonds**

Islamic bonds, or sukuk, have become a crucial funding source for large companies in emerging markets like Malaysia, Indonesia, and the UAE. In 2021, Islamic corporate bonds in Malaysia accounted for 75% of total corporate bond issuances, while globally, sukuk issuances totalled $25.66 billion in the same year. By the end of 2023, the global sukuk market reached $823.4 billion. However, there is little evidence on the impact of credit ratings on Islamic bonds compared to conventional bonds.

Shee-Yee Khoo, Assistant Professor in Finance at Bangor Business School, alongside Paul-Olivier Klein, Associate Professor in Finance at iaelyon School of Management, aimed to determine whether credit ratings affect Islamic bonds in the same way as conventional bonds, focusing on how risk is priced. Islamic bonds, rooted in religious principles, may influence investor behaviour differently due to religious motivations. Using a dataset of Islamic bonds and conventional bonds from Indonesia, Malaysia, Saudi Arabia, and the UAE, they found that higher-rated Islamic bonds result in lower yields, implying under-pricing of credit risk compared to conventional bonds.

This study explores several factors, including religious signals, rating quality, and bond structuring, to explain the differences. They found that periods of Islamic bond undersupply contribute to the lower pricing of risk, which is influenced indirectly by religious preferences. Overall, it highlights secular mechanisms like market structure and supply-demand dynamics as key determinants in the pricing differences between Islamic and conventional bonds.