

## PAKISTAN'S GREEN SUKUK: PIONEERING CLIMATE-LINKED ISLAMIC FINANCE FOR SUSTAINABLE DEVELOPMENT

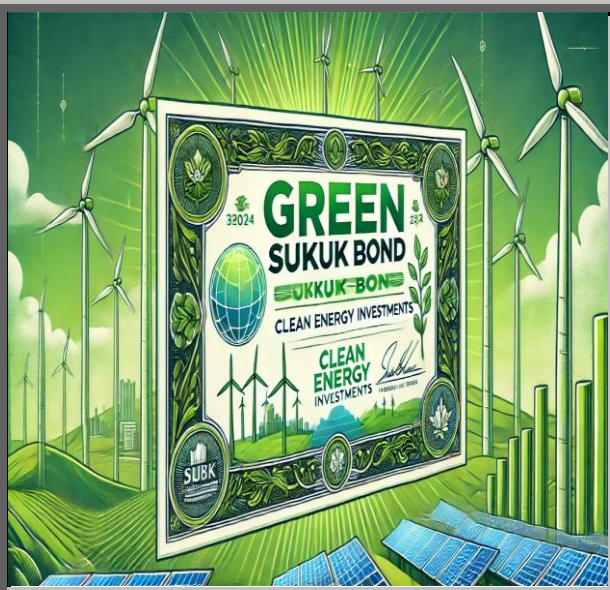
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*(Views expressed in the brief are those of the author, and do not represent those of ISSI)*



### Introduction

Pakistan took a significant step towards financial innovation and environmental responsibility with the successful launch of its first Sovereign Domestic Green Sukuk on May 16, 2025.<sup>1</sup> This marks a notable intersection between Islamic finance and green investment, aimed at aligning capital market activities with the country's broader climate resilience and sustainability objectives. As climate change increasingly poses challenges to the socio-economic fabric, the adoption of climate-linked, Shari'ah-compliant financing solutions like Green Sukuk presents a compelling opportunity for sustainable development to Pakistan.

The launch event, held on 16 May 2025, coincided with *Youm-e-Tashakur* (Thanksgiving Day) after the latest Pakistan-India conflict, symbolizing optimism and national pride. The Green Sukuk auction was open to a wide range of investors: local retail, institutional, and corporate participants; non-resident Pakistanis (NRPs); Roshan Digital Account holders; and foreign investors. Key financial institutions — including Meezan Bank, Dubai Islamic Bank, Bank Islami, and Bank Alfalah — served as

<sup>1</sup> "Pakistan launches first Green Sukuk worth Rs30 billion to fund new energy projects," Profit, May 16, 2025, <https://profit.pakistantoday.com.pk/2025/05/16/pakistan-launches-first-green-sukuk-worth-rs30-billion-to-fund-new-energy-projects/>

joint financial advisors.<sup>2</sup> This inclusive approach promotes greater participation in the capital market while building trust in Pakistan's reform-oriented economic policies underlining the importance of collaborative institutional support in scaling up green Islamic finance.

### Understanding Green Sukuk

Green Sukuk are Islamic financial instruments specifically designed to raise capital for environmentally sustainable projects. They are structured in accordance with Shari'ah law and are backed by tangible assets. Rooted in the traditional concept of *sakk*, which dates back over a thousand years, Sukuk represent a form of investment certificate granting the holder ownership in a pool of assets and the returns generated by them. Unlike conventional bonds, returns on Sukuk are not interest-based but derived from the actual performance of the underlying assets.<sup>3</sup>

The foundation for Green Sukuk was laid in 2015 with the establishment of the Green Sukuk Working Party (GSWP) by the Clean Energy Business Council (MENA), the Climate Bonds Initiative, and the Gulf Bond and Sukuk Association. This initiative aimed to develop Shari'ah-compliant financial products to fund climate solutions. The GSWP facilitated the design of a standardized Green Sukuk architecture to enable product issuers and investors to operate with confidence regarding compliance with both Islamic finance and environmental standards. Furthermore, the GSWP focused on engaging with governments and financial institutions to encourage market development, sharing best practices, and creating templates for Green Sukuk issuance.<sup>4</sup>

Additionally, in the case of Green Sukuk, the proceeds are earmarked exclusively for climate-positive investments such as renewable energy projects, clean transportation, energy efficiency, and sustainable infrastructure.<sup>5</sup> This innovation addresses the Islamic ethical concern for environmental stewardship while meeting the demand for green financial instruments in compliance with Shari'ah.

### Pakistan's Green Sukuk Initiative: A Turning Point

Pakistan launched its inaugural Green Sukuk in 2021 when the Water and Power Development Authority (WAPDA) issued Rs. 6.5 billion to finance an additional hydropower unit at the Tarbela

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<sup>2</sup> Salman Siddiqui, "Pakistan issues Rs30bn Green Sukuk to fund renewable projects," Business Recorder, May 16, 2025, <https://www.brecorder.com/news/40363049/pakistan-issues-rs30bn-green-sukuk-to-fund-renewable-projects>

<sup>3</sup> "Green Sukuk | Climate Bonds Initiative," Climate Bond Initiative, Accessed on May 28, 2025, <https://www.climatebonds.net/projects/facilitation/green-sukuk>

<sup>4</sup> *ibid*

<sup>5</sup> Ismail Dilawar, "Pakistan launches first Shariah-compliant 'Green Sukuk' to attract eco-friendly investment," Arab News, May 7, 2025, <https://www.arabnews.com/node/2599893/pakistan>

Dam.<sup>6</sup> This marked the country's entry into the global green Islamic finance arena. Building on that foundation, the government issued a three-year Ijarah-based Sovereign Domestic Green Sukuk on May 16, 2025, raising Rs. 31.99 billion against an initial target of Rs. 30 billion. The issue was oversubscribed 5.4 times, receiving bids worth Rs. 161.74 billion — a strong signal of investor confidence.<sup>7</sup>

Structured under the Sustainable Investment Sukuk Framework and aligned with Vision 2028, this issuance reflects the government's strategic shift towards interest-free, climate-conscious financing. The Sukuk carries a variable rental rate, with the cut-off rate set at 10.6364%, nearly 61 basis points lower than the applicable reference rate, making it an attractive low-cost borrowing tool.<sup>8</sup>

### **Economic and Environmental Impact**

Proceeds from the Green Sukuk are earmarked for financing three small dam-cum-hydropower projects: Garuk in Balochistan, Nai Gaj in Sindh, and Shagarthang in Gilgit-Baltistan.<sup>9</sup> These projects will not only enhance renewable energy generation but also contribute to water management, agriculture, and regional development.

Finance Minister Muhammad Aurangzeb, addressing the launch at the Pakistan Stock Exchange (PSX), emphasized the importance of this initiative in broadening the investor base and accelerating Pakistan's transition to a green and resilient economy. He also highlighted that 14% of the country's domestic debt — approximately Rs. 5 trillion out of Rs. 37 trillion — is now Sukuk-based, indicating a significant pivot towards Islamic finance.<sup>10</sup>

Dr. Shamshad Akhtar, Chairperson of PSX, pointed out that Pakistan's climate adaptation needs are estimated at \$348 billion by 2030. With traditional financing mechanisms proving inadequate, Green Sukuk offer a promising alternative to tap into the \$4 trillion Islamic finance market and the \$2.5 trillion global green bond market.<sup>11</sup>

Adviser to the Finance Minister, Khurram Schehzad, highlighted that climate change and rapid population growth are Pakistan's two most pressing challenges. He noted promising trends, such as

<sup>6</sup> Khaleeq Kiani, "Govt launches sukuk to promote green economy," Dawn, May 8, 2025, <https://www.dawn.com/news/1909335>

<sup>7</sup> "PSX Holds Gong Ceremony to Mark the Launch of Pakistan's First Sovereign Domestic Green Sukuk," PSX, May 16, 2025, <https://www.psx.com.pk/psx/files/?file=254022-1.pdf>

<sup>8</sup> ibid

<sup>9</sup> Khaleeq Kiani, "Govt launches sukuk to promote green economy," Dawn, May 8, 2025, <https://www.dawn.com/news/1909335>

<sup>10</sup> "First green Sukuk launched," Tribune, May 17, 2025, <https://tribune.com.pk/story/2546299/first-green-sukuk-launched>

<sup>11</sup> ibid

an improved tax-to-GDP ratio rising from 9.5% to 10.6% over the past 15 months, with a target of 11% by FY2026. The debt-to-GDP ratio has also improved from 74% to 65%, suggesting enhanced fiscal discipline and macroeconomic stability.<sup>12</sup>

The issuance of Green Sukuk is also a part of a broader strategy to restructure Pakistan's debt portfolio by transitioning from short-term Treasury Bills to long-term, lower-cost instruments like Pakistan Investment Bonds (PIBs) and Sukuk. In 2024, the State Bank of Pakistan reported a reduction in reliance on T-bills from 24% to 21% of the debt mix — a trend expected to continue.<sup>13</sup>

The government's policy direction includes diversifying funding sources, strengthening macroeconomic indicators, and ensuring fiscal stability. As part of this effort, Pakistan also plans to launch a Panda Bond — a renminbi-denominated instrument aimed at accessing the Chinese capital market — in the final quarter of 2025.<sup>14</sup>

### The Way Forward

The Green Sukuk marks a new chapter in Pakistan's financial history — one that combines Islamic ethical principles with a commitment to climate action. By embedding sustainability into its financial instruments, Pakistan is not only mobilizing capital for urgent development needs but also positioning itself as a regional leader in Shari'ah-compliant green finance.

Moving forward, the government is expected to continue innovating in financial products and policies to expand the green Sukuk program, deepen capital markets, and meet its Vision 2028 targets. The success of the initial issuance sets the stage for more frequent and larger-scale offerings, potentially attracting international investors and development finance institutions.

Green Sukuk, therefore, offer an ideal vehicle to channel this capital into renewable energy, low-carbon infrastructure, and climate adaptation projects. Eligible assets under the Climate Bonds Standard for Green Sukuk include solar and wind power plants, biogas facilities, electric vehicle infrastructure, mass transit systems, and energy-efficient buildings. These sectors represent not only urgent environmental needs but also strategic economic opportunities for countries like Pakistan, which faces escalating climate vulnerabilities.

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<sup>12</sup> *ibid*

<sup>13</sup> "Pakistan launches first Green Sukuk worth Rs30 billion to fund new energy projects," Profit, May 16, 2025, <https://profit.pakistantoday.com.pk/2025/05/16/pakistan-launches-first-green-sukuk-worth-rs30-billion-to-fund-new-energy-projects/>

<sup>14</sup> "Pakistan launches first Green Sukuk, eyes Panda Bond to boost sustainable growth," The Nation, May 16, 2025, <https://www.nation.com.pk/16-May-2025/pakistan-launches-first-green-sukuk-eyes-panda-bond-to-boost-sustainable-growth>

Pakistan's foray into Green Sukuk signals an evolution in how it addresses development financing, climate resilience, and investor engagement. As a climate-vulnerable country with immense renewable energy potential, integrating Islamic finance with sustainability goals offers a powerful model for other nations in the Global South. Through strategic reforms, inclusive market participation, and innovation in financial instruments, Pakistan is laying the groundwork for a more resilient and greener economic future.