

Another time, another place

THE MIDDLE EAST IS KNOWN FOR ITS AMBITIOUS BUILDING PROGRAMME, BUT ITS BURGEONING FINANCIAL SERVICES SECTOR IS LIKELY TO BE ITS MOST POWERFUL DEVELOPMENT. **MICHELLE PERRY** INVESTIGATES.



Executive summary

Financial services, driven by the development of Islamic finance, are growing strongly in the Middle East. With a rapid pace of change – “Dubai time” – and an increasingly sophisticated market to attract business, the region is appealing to those hoping to avoid the worst of the global recession. And while some adjustment to local customs is advised, this is a truly international environment.

without earning interest – in accordance with Sharia law. All products must be signed off by Islamic scholars to ensure compliance with the Sharia law.

Someone who has experienced that tremendous growth is Raphael Ricaud, head of Islamic finance at Rothschild. Ricaud arrived in Riyadh at the end of 2001, when IF “was close to zero”.

“I have seen the development in the sector, particularly in this field, grow quickly,” says Ricaud, who has also worked in HSBC’s Islamic division in Dubai.

Since global banks such as HSBC, a pioneer in developing Sharia-compliant products, brought it into the mainstream, many products are just as competitive as other commercial, non-IF products.

What has also helped develop Islamic finance in the region is endorsement and encouragement by the emirates’ rulers. In Qatar, for example, the emirate created its own pure Islamic megabank two years ago, explains Ricaud.

In other states IF has developed from the grassroots in the form of small national investment banks that are Sharia-compliant. In the past, the older national banks in Saudi Arabia and Kuwait offered some IF products, but nothing to the extent we now see.

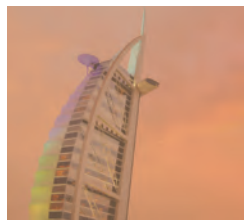
Today, most of the older national banks in the region have IF divisions or subsidiaries but there are now also myriad pure Islamic finance banks, as well as the IF divisions of the global investment banks. It is increasingly a mainstream component of the global banking system, with products having moved

The Middle East has for millennia been the gateway for traders from the east and west offering entrepreneurs of the day the perfect location geographically to sell and buy their wares.

As savvy as ever, the region’s rulers have been strategically positioning the emirates over the past five to six years in a bid to diversify away from its reliance on oil and gas – in which incidentally they are still rich – to create a financial centre important enough to rival the world’s best centres. And the jewel in the crown is, for now, Dubai, slowly edging over Bahrain as the region’s most important financial centre.

Most people are familiar with the extent of construction – a barometer frequently used by insolvency experts to gauge a region’s affluence – in the UAE, and particularly Dubai. They know the area is exceptionally wealthy, but what is less well known is the development in the financial services arena.

DRIVING FORCE One of the triggers for growth in financial services has been the development and sophistication of Islamic finance (IF) products, which allow Muslims to invest



beyond lending, insurance and investment funds to include Sukuk, hedge funds, currency swaps, and more.

The value of Islamic project finance deals being closed is projected to grow to \$3bn by 2012, representing up to 30% of all major structured deals finalised in the region, according to the Middle East's business intelligence service, Middle East Economic Digest.

International Islamic Financial Market (IIFM), an industry association, calculates that corporate Sukuk issuance leapt from \$0.4bn in 2000 to \$24.5bn in 2006.

GROWING COMPLEXITY IN TREASURY Although still lacking the West's sophistication, treasury services in the Middle East are becoming more advanced. As more expertise is brought into the region and local skills develop, the treasury function is growing in complexity.

"The products are simpler and the use of derivatives lower. The volume of the local stock markets are much less developed," explains Ricaud.

But he adds: "What I have seen is the development of Islamic treasury products that weren't there three years ago. It's possible to structure a Sharia-compliant interest rate swap and currency swap now."

Still, treasury services have a long way to go before they meet levels in the West. "If you need global treasury services then you would be working with JP Morgan or HSBC rather than local banks," says Michael Killian, executive vice president and treasurer at Dubai Aerospace Enterprise.

He adds, however: "They are coming up the curve quickly because they can skip a lot of the middle stuff and jump straight to the most sophisticated services."

The main challenge facing IF from the treasury perspective is how to develop treasury products in a more sophisticated manner, Ricaud says. "It is growing slowly, but I believe the trend will continue."

FAST PACE OF CHANGE The pace of change is what impresses many foreigners in the region. Tushar Patel, assistant group treasurer at global port operator DP World, was asked to go to Dubai two years ago to help set up a treasury function following DP's takeover of P&O. It was an opportunity he grasped with both hands and he has not looked back.

"It's very dynamic. DP is one of the most recognised companies there. It's right at the forefront in driving things in treasury.

"We did the largest acquisition facility at the time. The largest bond issue for 30 years and IPO all at the same time," Patel explains. "A lot of Middle Eastern companies look to DP and follow what we do."

Patel cites the company's governance structures and risk management processes as systems that are also adopted by national companies looking to improve transparency.

What inspires him most about the region is the national companies' energy. "Western companies are often more conservative, while Middle Eastern companies are more dynamic. P&O was always one of those to wait and see what other companies would do. DP prefers to be the first," he adds.

THE PACE WITH WHICH PEOPLE MOVE IS VERY QUICK. DUBAI-TIME, THEY CALL IT, WHEN YOU DO THINGS RIGHT AWAY

Killian, who has been based in Dubai for the past two years, agrees. "One of the things we find is that the pace with which people move is very quick. Dubai-time, they call it, when you do things right away," he says.

In terms of international corporates setting up in the Middle East the region is young in knowledge and application of governance and risk management processes. But Killian says companies learn quickly and are "coming up the curve very fast".

In fact, he says, there is much more shareholder interaction with companies and that is acting as an incentive to improve transparency and openness. Backed by the government, which holds a stake in many national companies, transparency levels are improving significantly, say treasurers working in the region.

Often, however, in a fast-paced business environment it takes a while for things to catch up. Buildings go up daily – in fact it's said that 27% of the world's cranes are currently in Dubai – but as Killian has observed, the infrastructure often lags behind, whether roads or governance procedures.

The Middle East is managing to attract highly skilled treasurers to the region with great career opportunities and that ensures standards are kept high. Importing skills is also helping in terms of developing the local skills set.

RELATIONSHIPS ARE IMPORTANT It is very different doing business in the Middle East to elsewhere in the world, say those working in the region. There is little separation between business and pleasure time. This blurring of the lines between work and play can confuse many Westerners, more used to abiding by the rules of a division in activities. But they are not all disconcerted by these mores and if you want to forge a successful career in the region it is advisable to get used to combining work and pleasure.

"What I really appreciate in this part of the world is that business is part of social life. The Arabs are very emotional people and so the concept of trust is more developed here. It's critical to build personal relationships before you can do business," says Ricaud.

It is a close knit community with around 15 players in Islamic banking. While the level of sophistication in banking relationships is not quite on a par with the West, bankers tend to stay in the region, if not in the same job, for a long time, so nurturing relations is vital.

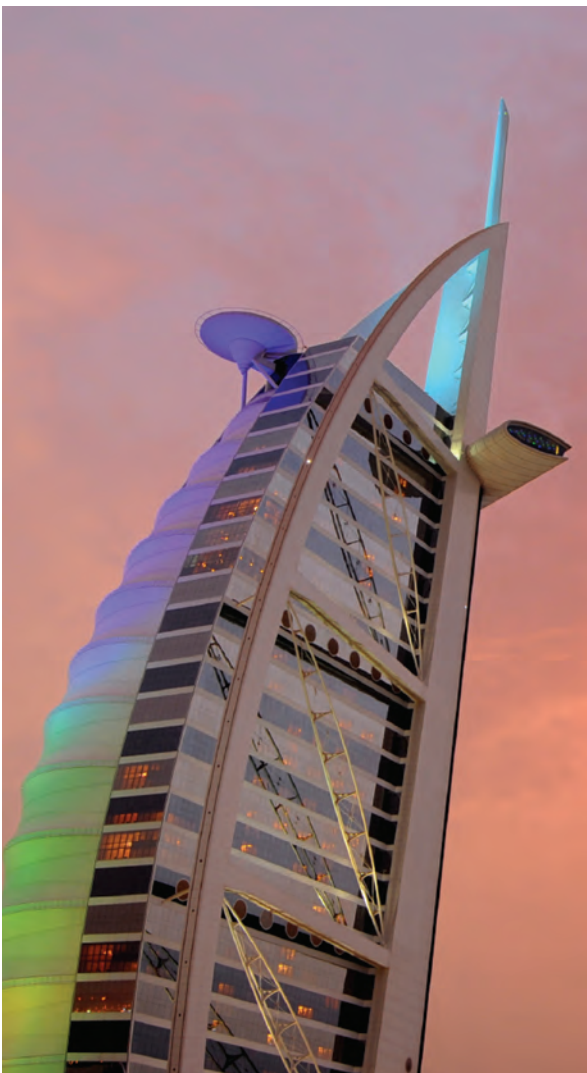
Investors work in the same way as in the West in process launching, structuring and distributing bonds. The distribution cut is the conventional platform. "In that sense there's not much different between the West and the Middle East," says Ricaud.

COSMOPOLITAN AND TRADITIONAL CONVENTIONS

There have always been strong links between Britain and the Middle East but Westerners increasingly gravitate towards the region now, not least for its tax-free benefits. You can forge a comfortable and sociable lifestyle in the region as long as you always remain aware that it is a Muslim country and there are conventions to adhere to.

The working week runs from Sunday to Thursday as Friday is an important holy day. And it's considered rude or forward for men to shake Muslim women's hands when they meet – either in business or social situations.

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Once they are au fait with the regional mores ex-patriots feel at home. Patel says since he moved out two years ago a lot of people who went to university or studied treasury management with him have been offered a job opportunity somewhere in the region.

Dubai is a particular favourite with Westerners as out of the seven emirates it appears the most Westernised. Dubai was built on a Western model, with many of the country's chief advisers having lived in London or elsewhere in Europe. It's still part of the Arab world with strict customs and that must be respected.

"Westerners sometimes forget that Dubai is part of the Muslim world. It's normal as it's very cosmopolitan here with all the skyscrapers and shops and you have a large Indian/Bangladeshi community too. If it weren't for the call to prayer you would forget you were in the Middle East," says Ricaud.

With a huge ex-patriot community the region is becoming more and more international. Killian says: "This has been a fabulous experience. It's truly international here and a cross-cultural experience is great."

CHANGING TIMES The oil-rich Middle East is cosseted thanks to its wealth and booming economy from the current global financial crisis. However it is not completely isolated from it.

"The atmosphere has changed. It's harder to raise debt in the Middle East now but 2007 was an amazing year. Everyone is waiting until next year to do anything," says Patel nostalgically.

Although the market is expected to be much tougher in 2009 than in 2007, it is unlikely the Middle East will be hit as hard as industrialised nations.

On the upside however, "The market capitalisation of each company is little but this has a positive side in the context of what is happening now. Even if prices here are affected by the crisis the region will withstand the global crisis much better than the West," Patel adds.

While some are less sanguine, we could nevertheless see the Middle East taking advantage of cheap assets. It is pretty much the only place on the planet at the moment with any wealth to spend.

"The interesting thing about the Middle East is that it's sitting on oil wells and has a large wealth of capital and with assets cheap we will see Middle Eastern companies look to snap up some bargains," predicts Patel.

Even British prime minister Gordon Brown visited the Middle East in the autumn with his begging bowl. He went to ask the Gulf states to increase trade between Britain and the oil rich states, as well as to "persuade the Gulf states, who've made an awful lot of money in the past few months... to redistribute some of that to help other states".

He also suggested the states had a duty to use some of their massive oil wealth to help ease the impact of the credit crunch on the world economy.

By the time the global recession eases it is likely more Western companies will be under the banner of the Middle East, with its burgeoning financial centre much more powerful than it is now. Watch this space.

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