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Opalesque Round Table Series '12

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Editor's Note

Dear reader,

The total assets under management of all **Sovereign Wealth Funds** globally is today estimated at around USD $4.6 trillion. While most of them are active in the fixed income and equity space which they manage internally and externally through specialized portfolio managers, going forward we will see **increasing interest for alternative investments** from these players.

Their need for diversification, increased yield in the current low interest rate environment, increasing sophistication, together with the fact that they are uniquely placed to deploy long term capital, makes them well placed to continue and increase their investment programs in infrastructure, private equity, hedge funds and real estate.

When international investors come to the region, their initial focus often seems to be the UAE and Qatar. These are good entry points into the regional markets, but according to the participants of the inaugural Opalesque Gulf Roundtable, people should not overlook the larger market, Saudi Arabia.

In addition, a number of **family offices** are operating from the Gulf, often from the financial free zones like the DIFC. Of course, these family offices and sovereign wealth funds such as Mubadala, ADIA, ADIC, QIA, Qatari Diar, PIF are continually looking at investment opportunities globally, but also the **nascent domestic asset management industry** is growing stronger each day.

Hear from:

1. **Zeeshan Ahmedani,** Partner, White & Case
2. **Bhisham Manraj,** Head of Middle East and North Africa, Sovereign Wealth Funds - FICC Solutions, Bank of America Merrill Lynch
3. **Adam Sender,** Assistant General Manager, Investment Banking & Corporate Finance GCC, Samba Financial Group
4. **Renaud Huck,** Senior VP, Eurex
5. **Uwe Eberle,** Managing Director, Van Eck Global

... background and facts about:

- **Given that the SWFs' capital is not subject to regulations like Basel and Solvency II, what are some of the unique opportunities these investors target?**
- **What is behind the Qatari Royal Family's $ 10 billion investment in gold producers?**
- **Can "unconventional oil" threaten the Gulf states in the long run?**
- **How do the global regulatory changes affect the Middle East?**
- **Are the financial free zones like the DIFC in Dubai or the QFC in Qatar a success?**
- **What is the reputation of UCITS funds in the Gulf?**
- **How important is the Sharia compliant finance sector?**

The Opalesque Gulf Roundtable was sponsored by Van Eck Global and Eurex and took place in April 2012 in Abu Dhabi.

Matthias Knab
Director, Opalesque Ltd.
Knab@Opalesque.com

Cover Photo: Abu Dhabi Performing Arts Centre

Participant Profiles



(LEFT TO RIGHT)

Zeeshan Ahmedani, Uwe Eberle, Renaud Huck, Bhisham Manraj, Adrian Sender, Matthias Knab

Introduction

Adrian Sender
Samba Financial Group

My name is Adrian Sender. I work for Samba Financial Group, based out of Dubai managing the Investment Banking business which covers the following products: corporate finance, project finance, investment banking, asset management, and brokerage. My work is focused on our business outside of Saudi Arabia, predominantly in the GCC.

Samba Financial Group was formed in 1980 to take over the existing branches of Citibank in Jeddah and Riyadh, which were opened in 1955 and 1966 respectively and in 2003 Samba moved to full local management (with Citibank selling it's remaining stake in 2004). Today Samba is one of the largest and most sophisticated banks in the region, and one of the most highly externally rated banks (A+/Aa3).

Samba is a leading regional institution for investment banking and in our Asset Management business (for locally domiciled open-ended funds) is the region's second largest in terms of assets under management. We run a number of funds (long-equity, money market and alternatives), some of them have a track record going back to the 1980s. Our particular focus is on the markets which we know best, so the Saudi market and the wider GCC.

Uwe Eberle
Van Eck Global

My name is Uwe Eberle, I am a Managing Director of Van Eck Global heading their office in Switzerland, where we are developing the actively managed business in Europe and the Middle East.

Van Eck Global was one of the first international investors; John van Eck started the business in 1955. We are headquartered in New York and have approximately 150 employees. John van Eck, a student and admirer of Ludwig von Mises, concluded that worldwide inflation would lead to gold mines offering better growth prospects than industrial and financial investments, and moved the bulk of the portfolio into gold-mining shares in 1968 in time to participate in the great gold bull market of the 1970s. The company has kept a strong foothold in the commodity sector since then, of the $34.8 billion in assets we manage today, roughly $27.2 billion are in commodities, $12.4 billion in gold mining stocks.

Since our inception, the firm has been investing globally. Now that we are also starting to distribute our products globally, the Middle Eastern region is getting more and more important for us.

What makes Van Eck special? As I mentioned, we have been, since 1968, in the commodity space. A second really important factor is that many of the senior investment people in our hard assets investment team joined the firm in the mid-90s. The investment team has had almost no turnover. In 1968 we began hiring geologists to make sure we have a better understanding of our assets. This concept has been ingrained in the company since then and today we have several investment professionals that are geologists or have deep technical/operational experience in the oil service industry. That means we have a deep knowledge not only in investment management but also with respect to the operational side of the business, understanding the complexities and opportunities of the ore bodies of mines or the oil and gas exploration and exploitation. We believe that this in-depth understanding has helped to avoid some of the pitfalls you can have in commodity equity investments and to deliver significant alpha to investors over the past.

Zeeshan Ahmedani
White & Case LLP

My name is Zeeshan Ahmedani. I am a Partner at the law firm of White & Case LLP in the Abu Dhabi office, as part of our global investment funds practice. I look after the regional investment funds and asset management practice, predominantly in this region on the investor side. As we are a global practice, I am also heavily involved on the sponsor side.

Bhisham Manraj
Bank of America Merrill Lynch

My name is Bhisham Manraj. I represent Bank of America Merrill Lynch. We are one of the world's biggest financial institutions serving individual consumers, small and middle-market businesses and large corporations with a full range of banking, investing, asset management and other financial and risk management products and services. As of March 31, 2012, we had $2.2 trillion in assets, more than $1 trillion in deposits and more than $900 billion in loans. We have a global footprint, with offices in more than 40 countries and serving clients in more than 100 countries. We have a long and enduring history in the region and this year we celebrate our 50th year of operation in the Middle East.

At Bank of America Merrill Lynch, I head the coverage of MENA Sovereign Wealth Funds, in relation to their investment needs across Fixed Income, Currencies, Commodities and Alternative Assets.

Renaud Huck
Eurex Group

My name is Renaud Huck. Based in London, I am a Senior Vice President at Eurex Group which is part of Deutsche Börse Group, where I am responsible for U.K. institutional investor relations.

We are the world's leading Exchange group with over 36 offices in 21 cities around the world. We have over 3,500 staff drawn from 66 countries. Our global reach mirrors the global nature of our clients. Asia is of key importance to us hence the reason for our presence in cities such as Beijing, Dubai, Hong Kong, Singapore and Tokyo. In fact we've been present in Asia for over 20 years now.

Eurex Group includes six businesses and by working together, each of these businesses play a key role in the financial industry. The value we bring to the market is our unique business model that covers the entire process chain in securities trading. There is no other exchange group that covers trading and clearing, risk and collateral management, market data and IT under one roof. We are the experts in what we do.

At Eurex Group my role is to reach out to the buy side, be they asset managers, hedge funds, high frequency/algo firms and also sovereign wealth funds. Why? To expand the franchise across Europe and in the Middle East thereby providing greater opportunities to the buy-side in these regions.



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Eurex Group includes Eurex Exchange, the International Securities Exchange (ISE), European Energy Exchange (EEX), Eurex Clearing, Eurex Bonds and Eurex Repo.

Eurex Group is part of Deutsche Börse Group.

Matthias Knab **Can you give us an overview on the changes in the financial and asset management industry here in the Gulf, including developments on the investor side?**

Zeeshan Ahmedani

In general, the asset management industry is still a nascent one in this region. I'm speaking of the alternative asset industry in particular. In the years leading up to the financial crisis there was a lot of overheating and quite a large number of managers started out had success in raising capital. We had quite a number of success stories with large regional players who were able to establish a good name for themselves.

However the local asset management industry was still in the process of developing some depth when the crisis hit and it of course went in to a prolonged downward trajectory. Unlike some of the other markets that have started to recover, either because there is a level of sophistication – for example in pockets in the West – or because there is a great underlying economic story – like some of the emerging markets in Asia or Latin America - this region has not had across the board high performance, and therefore, lags behind in recovery. It also has some core structural issues, compounded by geopolitical events, that exacerbate the situation. To be sure, there are exceptions – Saudi Arabia is the most prominent one. You also have markets like Qatar that bounced back to a certain extent. However, those are not traditional markets in the sense of a fully diversified alternative asset management industry.

The view seems to be that investors are still somewhat scarred from the impact the crisis had on the regional alternative investment industry, and more time may be required until a certain healing within the investor base has been completed and people are willing to look at the industry again wholesale. In some respects the industry has to go back again in developing a reputation that it had immediately prior to the financial crisis.

Of course, when we talk about the region here we can't fail to mention the geopolitical events in the region. We know that many deals have been put on hold and transactions have slowed down as a result.

Not surprisingly, capital raising within alternative assets has been down. For example, there is a lot of dry powder on the private equity side. Interest in the region from both local and international investors is still somewhat depressed, and the fact that it is a very illiquid market is compounding the issue. There are a lot of liquid investors in the region, but those investors are becoming more and more sophisticated and are looking more to direct investment than indirect investment through funds that are raised for the region.



These regulatory filings enable manager selectors to have very good transparency on the hedge fund manager's positions. As a result, it is much easier to monitor risk factors such as concentration, both at the portfolio level as well as a percentage of company ownership, and to anticipate potential liquidity problems. This is much harder to do for strategies that use mainly OTC markets (such as Fixed Income Arbitrage) or that operate in unregulated environments (for example Credit or Forex).

Zeeshan Ahmedani

Adrian Sender: In my opinion, it is very important to differentiate between the different countries within the GCC. There are a number of common factors such as demographics (with the GCC having a young and growing population), but also each country (and in the case of UAE sometimes each Emirate) have different regulations and cultures, which can have an effect on the underlying business and investment environment. I see a number of new asset management

businesses coming to the region but people have to be aware that they are dealing with quite different markets and therefore have to tailor their business well, no matter be they on the buy or sell side.

When you look at the domestic asset management industries, the two countries that stand out are Kuwait and Saudi Arabia, which both have fairly active asset management industries with AUM (in open ended funds) to GDP ratios of around 4% and thus can be considered institutionalized. It is important to note that in Kuwait and Saudi Arabia the retail investor bases are quite active investing in the funds industry. This compares to an AUM to GDP ratio of less than 0.5% in the other GCC countries.



When international investors come to the region, their initial focus often seems to be the UAE and Qatar. I think these are good entry points into the regional markets, but they should not overlook the larger market, Saudi Arabia. I believe one of the big advantages (and key focus for many international asset management firms based here) is the larger investors who are becoming (and in some cases are already) the most sophisticated investors globally. Sovereign wealth funds such as Mubadala, ADIA, ADIC, QIA, Qatari Diar, PIF are continually looking at investment opportunities globally, but in a number cases also have a core remit from their governments to actively invest in their domestic markets.

Adrian Sender

Renaud Huck

At Eurex the region here has been growing in significance. A considerable number of state-related entities, sovereign wealth funds, family offices, but also domestic and international investment banks and brokerage firms are active from here or have started to become more active on our markets. It is important for us to accurately understand their needs and offer the best service to them. Due to the scope of what we cover we are able to open the global capital markets.

As my colleagues on this roundtable have already mentioned, the region, in terms of capital markets, is quite young. However we're confident that the region will play a much more significant role in the medium term. From a trading perspective, we have already seen signs of this in the last few years.

Bhisham Manraj

I will address this question in 2 parts namely evolution of domestic asset managers who focus on local markets and secondly the requirements of local investors from asset managers who offer exposure to markets outside of MENA.

The domestic asset management industry can today be described as consisting of niche players in the fixed income and public/private equity space and a small number of larger regional players, mostly in the private equity space. Following the 2008 crisis, some of the smaller players have reduced or ceased operations, while some of the larger ones have through their track record maintained their AUM and consolidated their position as providers of investment solutions with a MENA focus. Going forward, we think that with increasing savings rate among retail investors which can be deployed in local markets as well as increased appetite from international investors for certain markets such as Saudi Arabia where we have seen equity volumes double and we have witnessed an increase in volumes this year. Should cash trading via QFI in the public equity market of the Kingdom of Saudi Arabia start, we think this should spur further interest from global fund managers. In addition, should some countries in the GCC be included in the MSCI Emerging Market Index, this should also lead to significant interest in the public equity markets of those countries.



Secondly, in relation to the investor demand side for exposure outside of the MENA region, the confluence of high savings rate, budget surpluses, the need for

Bhisham Manraj

diversification and increased sophistication of the investor base, means that this region will continue to be an important source of capital for international asset managers, companies and projects outside of the MENA region. Coupled with this need for diversification, investors in the region have also, rightly so, become more focused on risks, liquidity and transparency.

I think there are certain interesting opportunities available for MENA based investors. The fact that they can deploy significant amounts, can commit long term capital and in the specific case of sovereign wealth funds and family offices, the fact that their capital is not subject to regulations like Basel and Solvency II puts them in a unique and favorable situation in the current global investment landscape.

To give just three examples of such opportunities, there is e.g. the possibility of acquisition or risk sharing in sound businesses/activities which are being reduced or terminated by European/US banks as a result of their need to deleverage or because of the high regulatory capital charges associated, secondly the need for sound middle market European companies for financing and the fact that a number of European banks are reducing their lending to this market segment is creating interesting opportunities for investors to get involved in direct lending vehicles and thirdly we continue to see certain long term demand supply imbalances in the market which investors can benefit from e.g. in the food sector. In addition, the increasing sophistication of the investor base means that the region will continue to be an important one for asset managers offering smart beta and alpha solutions.

Uwe Eberle

Recent discussions here in the Gulf region have confirmed that the region is looking for more diversification. They aim to take advantage of secular trends; we see inflows in the agricultural space and in the gold mining industry for example.

In the past there was a demand for higher risk, more beta focused strategies. In the last two to three years we have been seeing much more sophisticated approaches to investments. Investors here are getting more and more interested in alpha. If you can deliver alpha or absolute return with strong risk management, investors now express significantly higher interest than in the past when investors tended to be more aggressive. Today, investors are looking more to add let's call it mid-level risk, and they examine much more carefully how the products are set-up and structured. Therefore, I do believe the alternative investment industry has a significant upside in the region.

Matthias Knab

Can you give us more information about the open-ended funds industry and other investor types here in the region?

Adrian Sender

There is some information available in the public domain about GCC open-ended funds, and firms such as Markaz publish information on their website.

Samba economics department also does regular Macro analysis on the GCC countries which can be seen on the Samba website (under Economic Monitor).

In relation to our Samba Capital funds that are domiciled in Saudi Arabia we see a large base of retail investors invest in our money market and equity funds. Fairly uniquely to the Saudi, market a number of the funds don't have subscription fees or redemption fees (which are more tailored to the retail investor) providing flexibility to park their money and shift between the asset classes.

Samba Capital also have a number of pension funds, corporate accounts, family offices and UHNW who invest via our Discretionary Portfolio Managed accounts which offers a more bespoke solution to investing for the client.

In Saudi, last year there was around $18bn AUM in locally domiciled open-ended funds, out of a total $28bn in the GCC. These figures do not include funds which are held in discretionary accounts as this information is not available in the public domain.

Zeeshan Ahmedani

The cash generated from national wealth also allows sovereign wealth funds to take the next step of investing in themselves and their level of sophistication. Some of the SWFs have already been very developed for some time now. But others are catching up, and along with that we see a trend towards direct investments. This is true not only in this region but globally.

Bhisham Manraj: The total assets under management of all SWFs globally is today estimated at around USD $4.6 trillion. This is of course an estimate as most sovereign wealth funds do not disclose their AUMs, liabilities or investment strategies. While most of them are active in the fixed income and equity space which they manage internally and externally through specialized portfolio managers, I believe that going forward we will see increasing interest from these players for alternative investments. Their need for diversification, increased yield in the current low interest rate environment, increasing sophistication and the fact that they are uniquely placed to deploy long term capital makes them well placed to continue and increase their investment programs in infrastructure, private equity, hedge funds and real estate.

In the MENA region, we do not have official numbers on the AUM of the SWFs. What I consider as important and relevant is that we expect sovereign wealth funds will continue to be an important source of capital deployment going forward across asset classes and our teams continue to work with them to design solutions which address their needs in the liquid and illiquid space across public and private markets. The increasing sophistication of these entities also means more and more direct transactions being executed.

On the liquid strategies side, just to give some examples, we continue to develop our award winning UCITS funds platform. While the platform was initially developed for the regulatory requirements of European investors, UCITS is now considered the recognized standard, providing a clear framework of risk management and investor protection, whilst allowing access to hedge fund return profiles.



Bhisham Manraj

We do believe that regulation and transparency are necessary but not sufficient and so we continue to work with talented asset managers on our UCITS platform to innovate, create alpha and deliver absolute returns to investors globally. As of today we have about 15 funds on our platform covering a range of strategies including long short, relative value, FX, etc. We also continue developing our range of investable rules based proprietary indices with offer liquidity, for example we have developed more than 450 investable commodity strategies which leverage on the strength of our research, trading and structuring capabilities. These are just two examples of how we can assist investors with investment solutions which offer liquidity.

On the illiquid side, we look at secular themes or dislocations which can present interesting investment opportunities globally. Knowing that there are opportunities out there and being able to invest in them in a timely and efficient manner as many of us know here are two different things. In this sense, we aim to make sure that that our clients can capture such opportunities through the right structures and partners.

Matthias Knab **Is there any intermediation in those cases between the parties?**

Bhisham Manraj

Intermediation takes a number of forms. Examples are sourcing of the assets which are of interest to our investors by leveraging on our global presence, structuring investments and offering them in the right format, finding the relevant portfolio managers for the relevant asset classes, identifying co-investors, providing where required financing and associated hedging. As a general rule, we seek to offer customized solutions tailored to the risk return profile of each investor.

Uwe Eberle: Many investors around the globe do follow the sovereign wealth funds and observe where they are putting their money. I found the news from the Qatari Royal Family very interesting, which announced in October last year that they plan to spend up to $ 10 billion buying stakes in gold producers through their sovereign wealth funds. That was very surprising to us at the beginning. But when you think about it, it makes a lot of sense.



Gold mining stocks were lackluster for quite a while and currently are very cheap when compared to historical valuations. In my opinion, mainly due to the increase of the production costs, investors are ignoring the strongly increasing cash margins and the significant cash flow generation of the industry. The two major production costs are energy and labor costs. If world economic growth is slowing, I believe demand for commodities and energy should go down, and so should prices. Gold Mining stocks, on the other hand, should profit from a stable to higher gold price (fear trade would be on), but even more from the lower production costs.

Uwe Eberle

On the one hand directly from the lower energy/commodity input prices, but on the other hand as well from lower/no increases in labour costs (due to less competition due to mine closures in other commodity sectors (ex Gold).

From the Qatari's point of view a very smart investment and it could be a perfect hedge, if energy prices remain high or go further up, they might have less return on the gold mining stocks because they might still suffer from production cost increases but their income is great from the large energy revenues they have. If energy is going down, gold mining stock could strongly outperform and deliver great returns, at a time when they need it.

Uwe Eberle



The Qatari's were not able to close the deal with European Gold Fields, but I think they will find ways to execute on their goals.

Adrian Sender

The sovereign wealth funds in the Middle East are quite (and in some cases very) sophisticated and have strong working relationships with their core (relationship) investment banks.

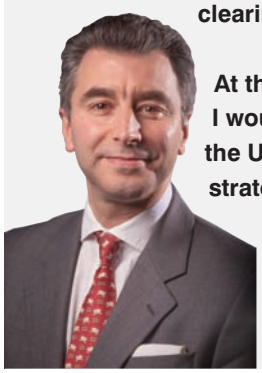
I am not familiar with the specifics of the transaction Uwe referenced, but I believe it is likely to be more than an opportunistic one. In the GCC there are a number of investments made where the focus goes beyond pure economic returns to include diversification and transformation of their respective economies. As an example in the UAE we had the AMD Mubadala (via ATIC) transaction in 2007 and are seeing the investment effects in the development of Globalfoundries with the intention in the future to have a Wafer Fab in the UAE. Another example is the partnership between Dubai (Dubal) and Abu Dhabi (Mubadala) in the initial setup and now expansion of the Emirates Aluminum facility and how this is being utilized to develop a further downstream industry around an aluminum cluster in Kizad.

Zeeshan Ahmedani

Adrian referred to the reduction in infrastructure spend. It is very interesting and worth observing that a lot of money was invested in Abu Dhabi for infrastructure and other initiatives, including some projects that others may describe as initiatives intended to put Abu Dhabi "on the map".

What we see happening in the region now though is that some of those projects are being scaled back and more money is being deployed into other sectors of the economy aimed at diversifying and providing a more tangible, direct return for the community.

Renaud Huck: From our perspective as an exchange, we know that sovereign wealth funds are sophisticated and broadly use exchange traded instruments. They have a strong futures culture and also keep an eye on the OTC clearing initiatives launched by central counterparties such as Eurex Clearing.



At the moment, a number of regulatory initiatives are really reshaping the global financial markets, and I would think that sooner or later regulators here will have a look at what's happening. In Europe and the United States, we see these regulatory changes progressively reflected in the asset allocation strategies with a very different configuration there than in the Middle East. We can expect the change of the regulatory landscape will at some point also reach this region. I would be surprised if this wasn't already on the radar of regulators here and elsewhere in the region.

Renaud Huck

As a global exchange with a strong regional footprint, we are interested in exploring the creation and launch of local futures products. We do this either by ourselves or in alliance with partners. Our tie-ups with, for example, KRX in Korea, SGX in Singapore and BSE in Mumbai illustrate this.

We're also extending our EurexOTC Clear services in June this year by launching CCP clearing services for interest rate swaps. Our clearing initiatives are geared to the buy-side segment to address their needs for asset protection, segregation and portability of positions in case of default of a clearing member. These initiatives address the upcoming regulatory changes due to come into effect in Europe and the United States soon.

Matthias Knab **Can you confirm that regulations here in the Middle East will change sooner or later?**

Zeeshan Ahmedani: To date, the most recent regulatory changes have really been less about the local products (with the exception of changes to the rules in the DIFC and the asset management initiatives of the QFC in Qatar), although I guess there is a tertiary impact on those too, but instead on inbound marketing activities. For example, Kuwait has updated their regulations in a very similar way to what the CMA does in Saudi Arabia. The intent is not to restrict the entry of products, but to make the regulatory oversight a bit more rigorous.



As Adrian mentioned, Kuwait and Saudi Arabia have a larger, active retail market, and so it is not surprising that they have the most robust regulatory framework in that respect. UAE has proposed rules on the book, which if adopted would also gear more towards the Saudi approach of regulating fund activity or marketing of fund products and financial services, so some of the regulatory changes Renaud talks about are already happening.

Zeeshan Ahmedani

My personal view is that the local regulatory framework should focus on inviting the fund management industry rather than making it tough for them to set up and do business here. The DIFC has actually been relaxing its rules making it easier for external managers to come in and sponsor funds in the DIFC. The QFC is trying to attract managers as well. These types of initiatives are to be applauded and encouraged.

Adrian Sender: Let me add some more background on my knowledge of the differences between the financial free zone and the onshore regulations.

A lot of international firms have actually set up in the Dubai based DIFC, which is regulated by DFSA. I think the DIFC and QFC (based in Doha) are probably the most progressive regulations in the region as they allow for full foreign ownership in a tax free environment together with a strong risk based regulatory framework. Investment banks, family offices and many other firms have set up in these free zones feeling very comfortable about the legal framework and practicalities about how it operates.

Of course, the DIFC is a fairly small physical zone, and any firm who starts to direct some of their activities outside of it has to be very conscious of the onshore regulations (including, where relevant, both the UAE Central Bank and the Emirates Securities and Commodities Authority (ESCA)).

Funds registered within a free zone are seen as foreign entities, so if they are looking into invest onshore they are still subject to potential foreign ownership restrictions. In most cases you need to have 51% local ownership.



Therefore, depending on what type of product you are trying to produce or distribute, being within a free zone can also be somewhat restrictive and you may need local partners. Samba has been working very closely with a number of institutions within UAE to help sell products from a distribution angle and also work together on structures within Saudi Arabia.

I expect the regulations in the GCC to further evolve, as there is active interest from member states to attract further FDI. As an example the UAE and Qatar have been making changes such as implementation of new settlement systems (DvP) and increases in foreign ownership limits to obtain MSCI Emerging Market status.

Adrian Sender

Bhisham Manraj As the participants today have already addressed local regulation, I thought I would highlight how regulation outside of the MENA region can impact investors in the MENA region from firstly an investor protection point of view and secondly from an investment opportunity point of view

Firstly, best practices and regulatory requirements that are in place in other jurisdictions and required by investors in those jurisdictions can informally influence the behaviour and requirements of investors in other regions and thus have an indirect impact. An example can be the European UCITS framework which as I mentioned was initially built for onshore regulated investors and is today viewed even by investors outside of the EU as a route for providing easy and secure access to alternative investments. Features like transparency, stringent rules on asset protection through limited counterparty exposure, ring fencing of assets and independent oversight of assets are all features which are required under UCITS Regulation but which MENA investors can also benefit from through these platforms. This is the case even if local regulations do not always require compliance with the same rules.

Secondly, imposition of new regulations outside of this region has an impact here. Imposition of new capital and liquidity ratios on banks or solvency ratios on insurance companies in Europe for example means that they will retrench from certain activities that are too capital intensive. The deleveraging exercise undergone by banks in terms of disposal of non-core assets is also another feature we have all witnessed in the past couple of years. Since the last crisis there has of course been a whole range of new regulations being introduced by regulators worldwide. What we should not lose sight of is that these regulations, being imposed in say the U.S. or Europe, can also in turn create investment opportunities for investors based in the MENA region who are not subject to the same regulations. Our teams spend a lot of time identifying these opportunities for the benefit of our clients.



Bhisham Manraj

Matthias Knab **In your view, are the financial free zones and jurisdictions like the DIFC a success?**

Adrian Sender The financial free zones like the DIFC have to be seen as a success, having attracted nearly every major investment bank in the world. The turbulence in the region emanating from the Arab Spring appears to have cemented Dubai's role further as the main regional hub.

Matthias Knab **Adrian, from the investment side, the Gulf is mostly known for its sovereign wealth funds. You mentioned that there are also numerous family offices operating from here, mostly from the free zones or jurisdictions like the DIFC. Can you tell us more about the family offices that operate from the gulf?**



Adrian Sender: There a number of family offices operating here, these include some of the old Middle East trading families who may be known through publications such as the Forbes Middle East list as well as individuals from the wider MENA region and from countries such as India and Pakistan. They come here for a number of reasons such as lifestyle, tax and geography and more recently political stability.

Adrian Sender

Matthias Knab **How else do you think will the Gulf impact the global world?**

Uwe Eberle: If you don't mind, I would turn your question around and reflect how the rest of the world could affect the Gulf to a significant extent?

At Van Eck, we have been spending a lot of time over the last three years to research and invest in unconventional oil and gas. More than 50 % of our energy exposure is currently in that field. We have made several trips around the world. For example, we visited the Shale Gas fields in Poland three times recently.

In the U.S. we have been seeing a tremendous change in the gas market due in our opinion to the advanced extraction techniques in horizontal drilling and hydraulic fracturing. These changes in technology led to record production levels, significant supply, full storages and record low prices.

Now, while we are still in an earlier stage of development in unconventional oil, we see the potential for significant production increases in the years to come.

If the early success of the Bakken and Eagle Ford fields can be replicated in the Permian basin and other areas, and the US is able to further strengthen the infrastructure to support that growth, we think that this could be a game changer for the oil industry.

An increase of several million barrels a day of oil production in the US could certainly affect the price development of world oil prices, not necessarily if the world would resume on a growth path, but probably if the world economic growth remains lack lustering.



Uwe Eberle

In fact, the US Energy Department announced in February this year, that for the first time since 1949, the United States exported more gasoline, heating oil and diesel fuel in 2011 than it imported.

The usage of the advanced extraction techniques were implemented in the US first, but there are significant unconventional oil and/or gas resources in places like Canada, Mexico, Argentina, Poland or in China, to name a few. They need more time to fine tune their drilling techniques and build up infrastructure, but we are confident that we will receive more positive news from the rest of the world sooner rather than later.

If we see the same successful path in the usage of new technology in unconventional oil, when compared to unconventional gas, and more countries are able to replicate the US unconventional gas success story, my question – as we just talked about $ 90 oil – is: What will be happening to this region if oil is coming under pressure due to additional supply and limited demand and would fall significantly below $90?

Adrian Sender

I expect the Gulf will continue to impact the world in relation to exports of oil and gas.

Increasing fiscal expenditures by the member states is having an effect on their budget break-even price. Samba's last predicted budget break-even oil price for the UAE was $90 per barrel (I understand in the press Emirates NBD are advising that based on their calculations this may have risen to $107 per barrel) and the Saudi authorities have indicated that they will defend prices of around $100 per barrel and they have some scope to manage their spare capacity to control prices.

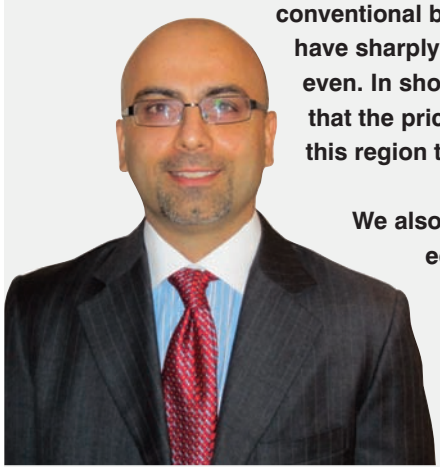
The effects of demographics in the region, with consumption becoming an important driver of growth is stimulating demand for new businesses and products and hence trade and investment.

The GCC countries have large growing populations (Saudi as an example by the most recent census has a growth rate of 3.4% compared to a global rate of 1.2%). It is important to note that this growth rate in Saudi (but also in some cases to an even greater extent in other GCC countries) is driven by expatriate communities.

Zeeshan Ahmedani

I believe that apart from the potential challenge around future revenues, some of the Gulf countries may also be challenged on the labor front and their demographics. As Adrian pointed out, some countries here have very small citizenry but rather large expat communities, including in skilled and professional sectors. A lot of that is financed through the hydrocarbons – the lifestyle and compensation in the GCC is extremely attractive to the expat. If there comes a time where hydocarbons are unable to sustain this any longer, those countries will have to rely on other sectors of their economies and an educated local population. They are all working towards that.

The impact on the global world is I think tied to how oil/gas prices behave over the next couple of years. Since 2000, the world economy has endured a five fold increase in oil prices, as constraints on conventional crude oil production ultimately had to force an increase in investment in unconventional and alternative fuel sources. Much of these non-conventional barrels have an investment hurdle of about $80/bbl. Similarly, many OPEC countries have sharply increased their budgetary requirements and now need $80 to $90/bbl to break even. In short, both OPEC and non-OPEC barrels have a strong floor at $80/bbl. So in the event that the price of oil dips below $80/bbl, I would expect to see reduced outflow of capital from this region to the rest of the world.



We also have to be cautious about price spikes even for this region as we believe the world economy can hardly afford to spend more than 9% of its GDP on energy. In the last 50 years, there have been only 2 times when we got very near or exceeded the 9% figure, which were in 1980 when we had a double dip recession and in 2008 when we had a great recession.

Zeeshan Ahmedani

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In addition, we believe we will continue to witness an increased focus on deployment of government capital within the region for job creation, social security and social infrastructure spending. For 2012, we forecast GCC GDP growth at 3.4% in 2012 due to post Arab Spring stimulus, solid non-oil growth but flattish oil production. Qatar should grow the fastest followed by Saudi Arabia.

Matthias Knab **You mentioned the sovereign wealth funds' aim to continue generating good returns. Are there any data or estimations available regarding the returns of the Gulf-based sovereign wealth funds?**

Bhisham Manraj Not really. One or two entities have started to publish some reports which gives an insight on their portfolio return and asset allocation but on the whole this information is private and confidential.

Renaud Huck We have to also realize that sovereign wealth funds are not listed companies. They do not necessarily make public what they do, and very often they explore a dual avenue, which is direct investment and at the same time allocations to external managers. They have very large allocation programs, for example the most active sovereign wealth funds are very active in the alternative investment industry, either actively allocating to single managers or to investment platforms. At the same time, they run investment programs in different asset classes. If the sovereign wealth funds' returns were to be made public, it would be difficult to know how to account the different avenues in terms of returns.

Zeeshan Ahmedani: Estimating the returns of a sovereign wealth funds gets more complicated than that as well, because it also depends on what you are calling a sovereign wealth fund.

If you are inclusive and qualify Mubadala, for example, as a sovereign wealth fund, even then the return numbers are hard to quantify. You may have the numbers, but how do you really assess what the return is? Fact is that some of these sovereign wealth funds are conduits for their governments to execute a lot of the initiatives that we have been talking about. Some of those initiatives, they recognize from day one, may not generate returns for a long time, and some of those investments may be set up not to achieve economic return but instead social and other benefits.

We are dealing here with entities that are engaged on many fronts. They are not just passive investors or private-equity style investors who exit within a certain period of time. You really cannot gauge what their returns are. Maybe you can look at specific silos and look at how those units are generating return if information is available, but I think it is really hard to assess each sovereign wealth fund's returns on a macro level.



Zeeshan Ahmedani

Matthias Knab **There is also a certain trend or an initial movement towards more transparency and towards more accountability within the global community of sovereign wealth funds. There is of course the Government Pension Fund of Norway which is probably at the forefront of that movement, but also the local ADIA fund has started to publish annual reports in 2009. What is the trend here, can we expect more going forward?**

Zeeshan Ahmedani: A number of sovereign wealth funds, although not all of them, have signed up to the Santiago Principles, including some here in GCC. However, the level of aspirational transparency that the Santiago Principles sought to obtain is a purely voluntary undertaking.



On the other hand, just as the investee jurisdictions talk about national security and national interests when there is an acquisition in a particular industry, I think so too these sovereign wealth funds have to consider it from the their side of things. If they have positions in certain investments and certain asset classes, can another jurisdiction potentially use that as pressure in a broader geopolitical sense? Therefore, while there may be some disclosure, I would not think that the type of the disclosure that maybe some want - akin almost to a public company type disclosure - will happen.

Zeeshan Ahmedani

Matthias Knab **What else is important about this region from a financial / asset management perspective?**

Adrian Sender The GCC markets offer great opportunities and a number of the local fund managers (including Samba Capital) are very sophisticated with strong track record, good performance and an increasingly diversified product range.

Saudi Arabia has a very active stock market (the Tadawul) and a strong pipeline of future IPOs. The local Saudi market is still not presently fully open to direct foreign investments but equity exposure can be obtained via funds or equity swap products.

Zeeshan Ahmedani: You can find a number of strong names in the alternative asset space here in the region. Abraaj Capital is a very good example. In fact, I think Abraaj can go toe-to-toe with a lot of players and has grown from a regional to a more international player. They are now physically in East Asia, and have been doing deals globally for some time. But the number of recognized, established managers is still small when compared to many other emerging markets.

What I hear from the sophisticated investors in the region is that they mostly prefer to do their deals locally through joint ventures and direct investing rather than through a fund sponsored by a fund manager.

Now, there is definitely a class of institutional investor that will look to a fund product, but the large sophisticated investors, in my view, would prefer to go direct and not through a fund sponsored by a manager. This means that the local asset management industry will take some time to really develop and grow. That will happen over the long-term though, but it will require some time.

Zeeshan Ahmedani



The MENA region, for example, has been ranked in the bottom half of target emerging markets for international institutional investors over the past few years. Of course this too will change, but you hear international investors say that the depth is not quite here yet. Perhaps groups like Samba and Abraaj can contribute to develop that manager base and investment environment, but I think it is going to take some time. There will also need to be some structural and economic changes in the underlying economies for a true alternative asset management industry to truly take hold, and that will take some time too.

Bhisham Manraj: I believe the outlook for the region should be of interest to your readers outside the region as this will definitely have an impact on both inward and outward investments.

Looking ahead for 2012, our latest GCC regional growth forecast is 4.3%. Higher global liquidity, supportive fiscal policies, and elevated oil prices may continue to support growth this year in the absence of deterioration of political risk. While there are still some downside risks to global growth, we believe that the MENA region is now better positioned to cope with such a slowdown given the increased oil windfall. Higher oil prices are supportive of GCC macro through higher liquidity, stronger fiscal and current account balances, assuming a regional budget breakeven oil price of USD80/bbl, and higher GDP growth, though the impact on the latter is non-linear at elevated oil prices.

There are of course risks to our base case projections. These include a sharp deterioration in global growth in 2H12, return of the Euro zone debt crisis, hard landing in China, materialization of regional geopolitical risks, or on the flipside progress in resolution of Iranian nuclear standoff which could weaken oil prices.



In relation to inflows to this region, we believe that MENA was off the radar screen for many investors in 2011. First it was the Arab Spring and its destabilizing spill-over across the region, then came along the EuroZone debt crisis and lower oil prices and finally the increased geopolitical risks around Iran. International investors have largely shied away from the region until lately. We are more constructive for 2012.

In relation to outflows from the MENA region, in the absence of some of the risks I have highlighted materializing, I believe that this region will remain important for the financial services industry as investors will continue to remain active in their search for yield and diversification. In addition with the increased sophistication of the investor base, I believe we will see an increase in the allocation to alternative investments.

Bhisham Manraj

At Bank of America Merrill Lynch, we have positioned ourselves for this trend and built the teams, expertise and infrastructure to be responsive to the needs of our clients in this region on their investment needs across all asset classes. We are very focussed on making sure that we can provide our clients in this region with the products and services they need when, how and where they want them.

Uwe Eberle

I agree, the region has to diversify further and needs to find investments with low or negative correlations. I am pretty sure that investors here will continue to diversify into other commodities outside of energy or in the energy space in unconventional oil and gas. Other sovereign wealth funds will likely follow the road of the Qatari's move into gold and gold stocks.

It might even make sense for the Middle Eastern region to invest in unconventional oil and gas service companies, which could deliver good returns if the story continues successfully. These investments could have negative correlation to the oil price.

It is our view that the move into absolute return products will continue. Absolute return products offered in UCITS format will continue to grow in acceptance, gather more assets, and similar to Latin America and Asia, UCITS will be seen as the Gold Standard. As long as a UCITS fund has similar costs and return characteristics, it should be preferred to other fund formats.

Adrian Sender: One area within the financial industry here in the Gulf that has become increasingly important, maybe less on the sovereign side, but certainly for many family offices, retail, and in some cases also some of the larger banks, is the Sharia compliant finance sector. In fact, it makes up a very large part of both the local and foreign investor base in our funds. In Saudi Arabia, open-ended Islamic Funds constitutes over 80% of the total AUM.

Adrian Sender



Matthias Knab **The Shariah banking industry is a relatively new one. We also cover it with a dedicated publication here at Opalesque, and we certainly have seen a sustained growth in this sector.**

Adrian Sender Absolutely, Sharia compliant finance products keep growing both in assets and relevance. There are certainly differences across the region, for example each investment group would have its own Sharia Board. So, each party will have different view as to what investments they believe is acceptable according to their criteria. It is important and possible to tailor structures for the underlying investor.

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