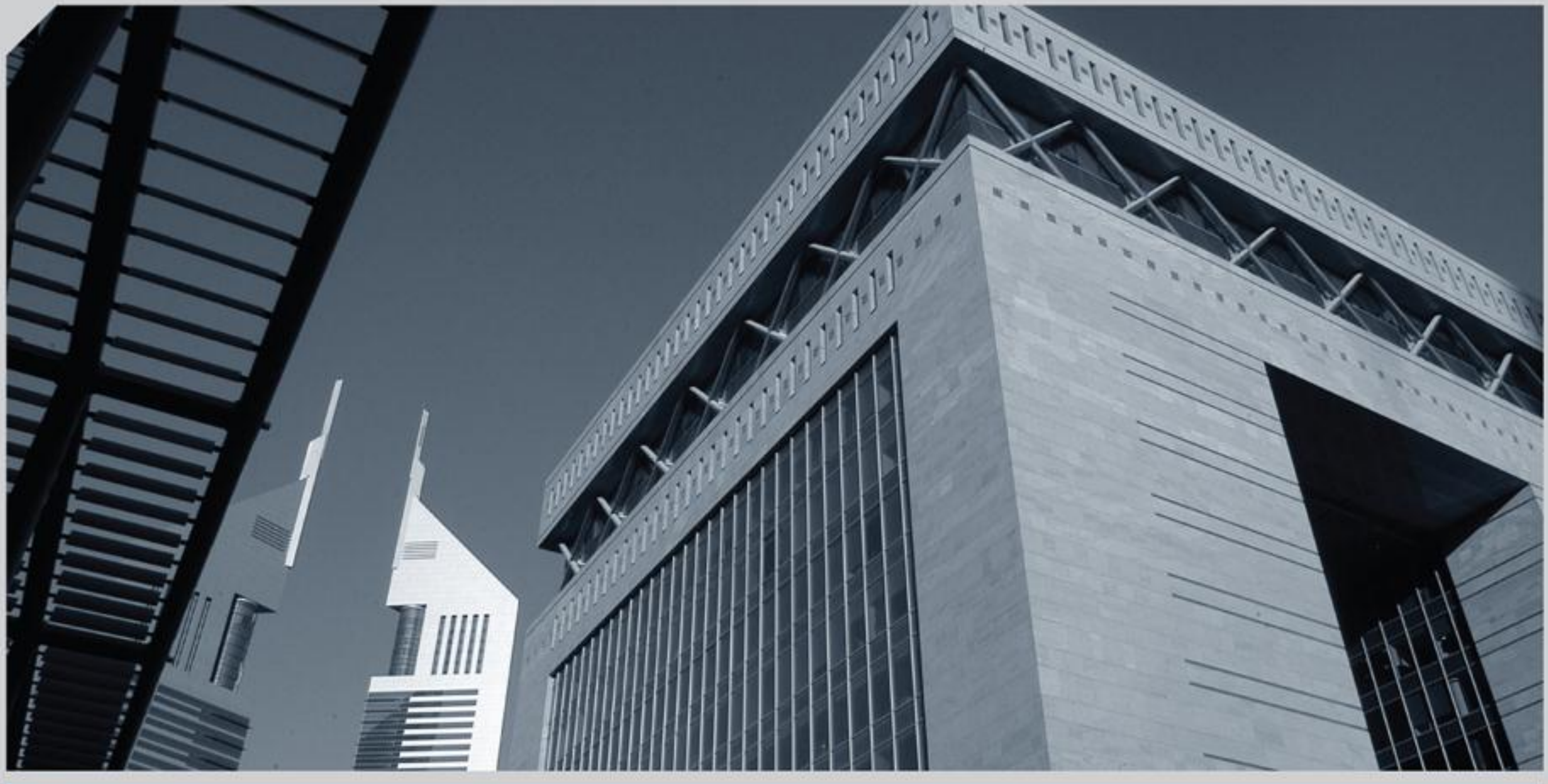

MENASA Capital Markets: Going Forward

MENASA Forum Plenary Debate

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DIFC Dubai International Financial Centre

Agenda

Towards Emerging Markets: Changing Economic & Financial Geography

New Financial Architecture & End of the Hub-Spoke Model

The Future of Regional Capital Markets

Need for Developing Local Currency Markets

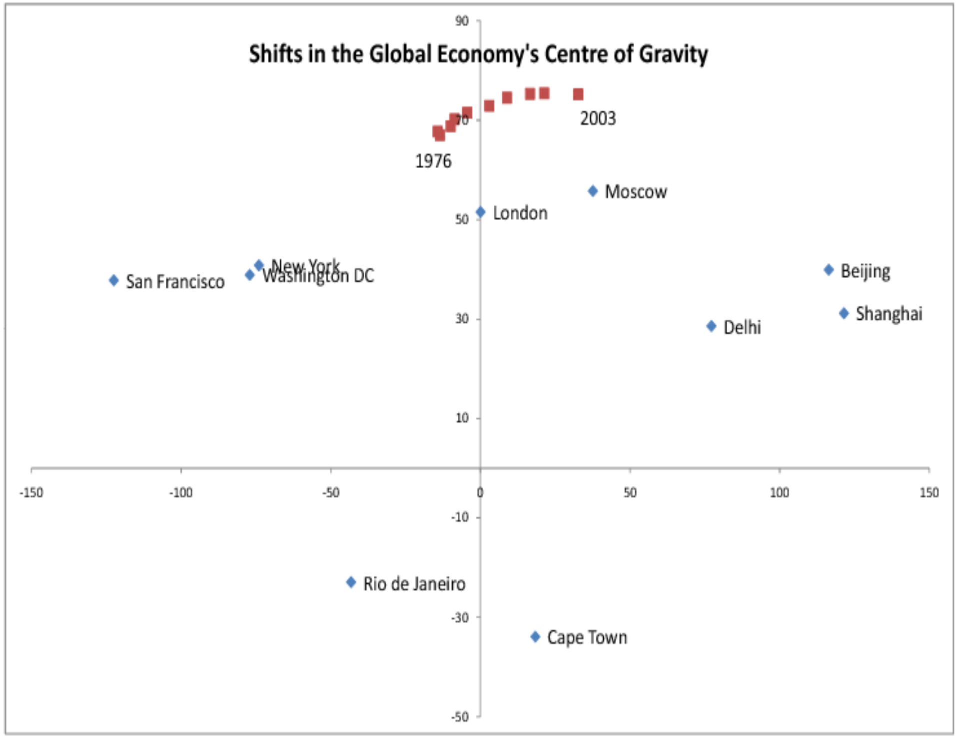
DIFC’s Transformational Role

Emerging Markets: Changing Economic Geography

Emerging markets have contributed 2/3 of global growth since 2002.

- The world's economic centre of gravity in 1976 was a point West of London, somewhere towards the middle of the Atlantic Ocean.
- But in the 30 years since then, that centre of gravity has drilled 1800 km - one third of the planet's radius - away from the US & towards the East. Epicentre between Dubai & Shanghai !

- Interestingly, evidence shows **geographical shift accelerated in 1991 & 2001 - each time the US was in recession!**
- In less-turbulent times, between 2002 and 2007:
  - China's average contribution to world economic growth approached 66% that of the US;
  - China and India's together, almost 85%;
  - East and Southeast Asia's, more than 130%.



Source: Quah, D (2009): "The Shifting Distribution of Economic Activity", London School of Economics, Oct 2009.

Emerging Markets: Changing Financial Geography

- The new economic geography is reflected in the evolution of capital markets
- The crisis will contribute to eradicate the hub-spoke model centred on London and New York giving impetus to a transition to a polycentric, spider web model

	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009(E)
World Market Cap	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%
United States	46%	47%	50%	47%	45%	43%	39%	36%	31%	33%	28%
Rest of Developed	46%	45%	41%	42%	44%	44%	44%	44%	41%	41%	41%
Emerging Markets	8%	8%	9%	11%	12%	13%	16%	20%	28%	26%	32%
BRIC	2%	3%	3%	3%	4%	4%	6%	9%	17%	15%	19%
Rest of Emerging	6%	5%	6%	7%	7%	9%	11%	10%	11%	11%	13%
of which GCC	0.3%	0.3%	0.4%	0.9%	0.9%	1.3%	2.5%	1.3%	1.7%	1.6%	1.2%

Source: Standard & Poors.

New Financial Architecture & End of Hub-Spoke Model

Nearly two-thirds of the increased financial stress in MENA countries following the Lehman shock is attributable to direct or indirect spillovers from financial stress in advanced economies. (IMF, WP/10/8, K. Moriyama, Jan 2010)

We need to design and move to an architecture of networked financial markets - a more stable and sustainable **“spider - web”** model.

- Where there is not a small number of financial centres intermediating and reallocating the entire world’s savings.
- Rather, there are numerous international financial centres across the globe that have the capital market depth & regulatory sophistication to absorb excess capital from their own regions, as well as from elsewhere.
- Such a model will prevent the enormous accumulation of savings in just one or two financial centres, creating an unstable sloshing of large waves of capital.

The move from New York/ London to the “-ai” markets – Dubai, Mumbai, Shanghai!

Financial Regulatory Revamp

General lessons for Financial Regulatory Revamp:

- Markets are not self regulating and rules are rarely self enforcing
- Leverage must be capped
- Liquidity must be preserved
- Regulation must be enforced with effective action not tick box approach

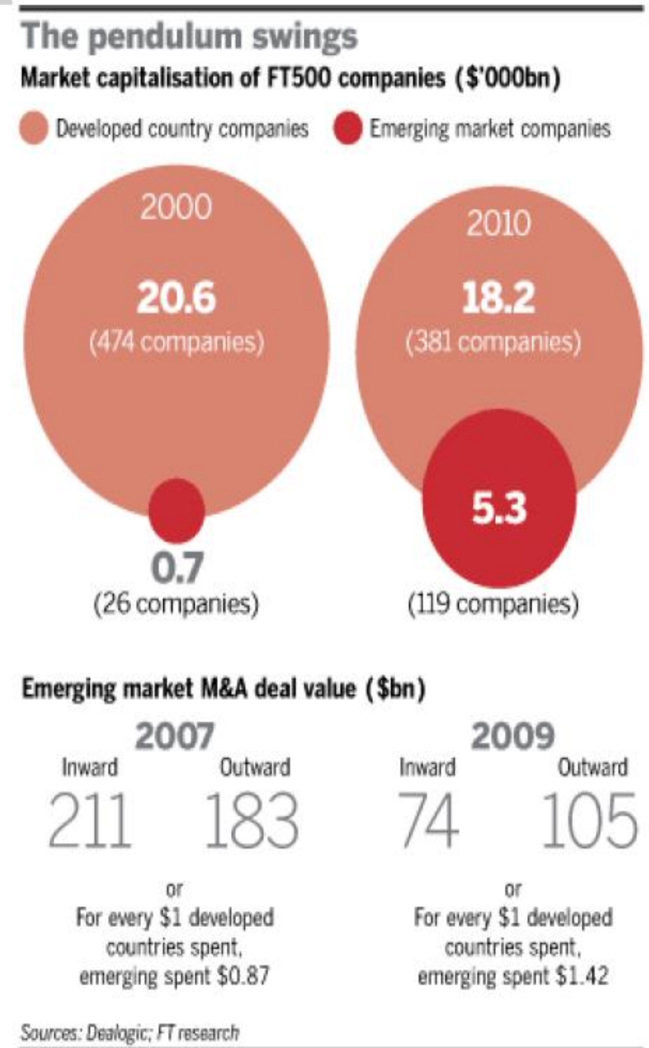
IIF's comments to the latest Basel Committee on Banking Supervision proposals covers:

- Cumulative Impact Assessment and Timing: design & calibration of the proposals needs to be based on assessment of their cumulative impact, with full consideration of the interdependencies among the proposed measures.
- Capital Composition: improving the composition of banks' capital is necessary. However, the proposed rigid definition of capital will have a significant impact on firms' lending.
- Leverage: The proposed gross leverage ratio (disregarding all risk mitigation) would result in an overstated and misleading view of firms' economic risks, leading to disproportionate constraints on lending.
- Counter-cyclical Measures: a combination of risk management, forward-looking provisioning and capital tools is needed to address pro-cyclicality.
- New Liquidity Framework: The current proposal fails to consider market effects, for example, in defining eligible assets.

Growing South-South relations

- Emerging markets have contributed 2/3 of global growth since 2002.
- US& UK had expanded as capital exporters; now it's the turn of the EMEs.
- Wealth in the EMEs suffered a setback in 2009
- HNWI financial wealth is expected to recover to $48.5 trn by 2013; Asia-Pacific will overtake North America as the largest region for HNWI financial wealth
- Shift from West to East is obvious; domestic demand is the key differentiating factor
- Most visible recently : Corporate Acquisitions
- For the first time (2009) takeovers by emerging world companies of developed world groups: $105bn > takeovers going the other way at $74.2bn, according to Dealogic.

=> ***Terms of trade b/n developed & emerging market groups are changing, with power shifting to the emerging world.***



Source: "Business: A Change in Gear", May 11, 2010, FT

What Lies Ahead? Looking to the Future

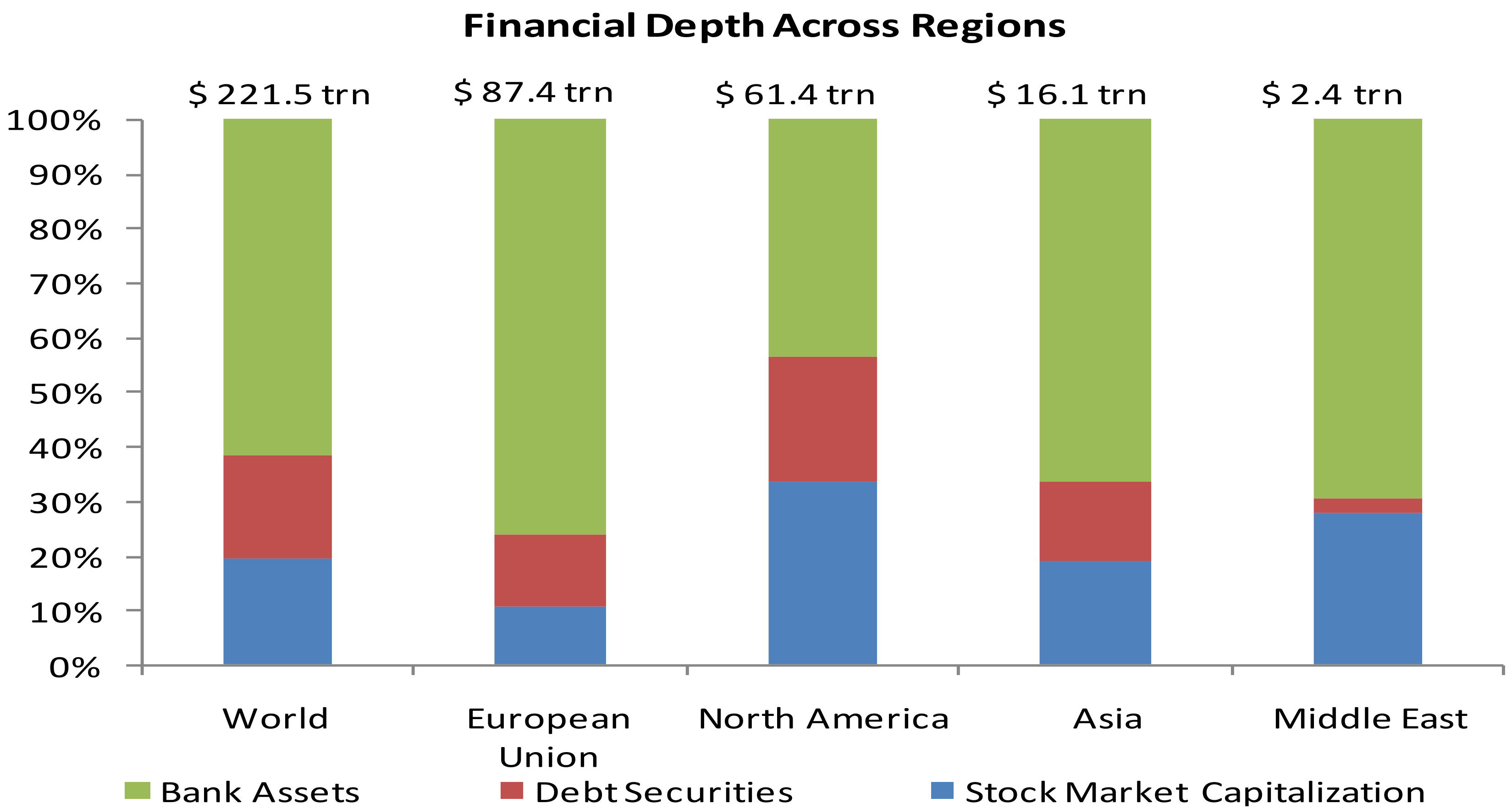
- About 2/3-rds of the world's proven oil reserves are located in this region.
- Oil reserves are estimated at over 37 trillion USD (see DIFC Economic Note # 4 on www.difc.ae)
- Gone is the era of recycling petro-dollars: these resources are now, for the first time, not amassed into foreign bank accounts but used domestically
- The diversification drive implies extracting energy resources and transforming them into the platform for the development of a XXI century knowledge based economy.

What Lies Ahead? Looking to the Future

- What additional measures are needed for capital markets?
  - ***Integration of capital markets: starting with the equity markets of UAE***
  - ***Need to develop local currency debt markets***
  - ***Creation of a second-tier market for family-owned, small and medium enterprises, the most dynamic of which are located in the free zones***
  - ***Strengthen market resilience***
  - ***Engage in design of new International Financial Architecture, policy & regulation***
  - ***Institutionalize and build economic policy capacity***
  - ***Increased transparency & disclosure***

Financial Depth Across Regions: Undeveloped Markets

- In the MENASA region, capital markets are dominated by bank assets and equities
- Debt securities make up only 2.7% of the Middle Eastern capital markets!



Source: IMF Global Financial Stability Report, Apr 2010

Local Debt Markets: Cornerstone of Development Policy

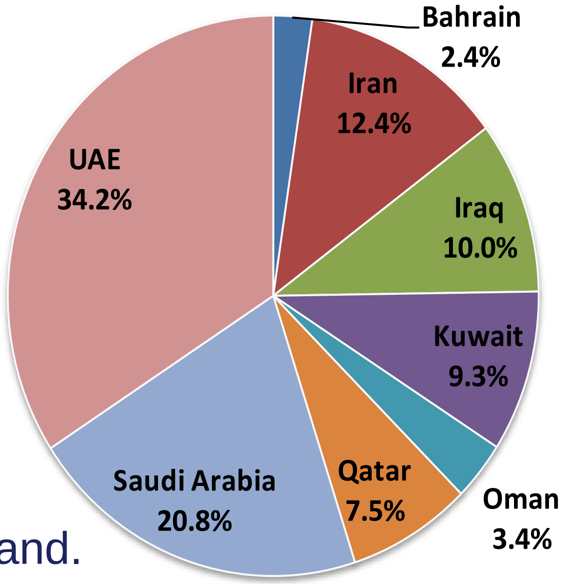
Potential drivers of MENASA Debt Market

- **Finance infrastructure** and development projects in the region
- **Corporate Debt:** Well functioning debt markets will help reduce dependence on bank finance at a time when the banking sector is in a process of deleveraging
- **Government Debt:** Diminish macroeconomic and financial vulnerability from energy price fluctuations by providing governments with an alternative source of funding to smooth out volatile revenues
- **Enable monetary policy** by providing central banks with a market to conduct open market operations & control liquidity
- **Mortgage Markets:** cornerstone of housing finance
- Provide **institutional investors** instruments that offer safe and stable long term yields in local currency

Local currency bond markets are a cornerstone of development strategy

Infrastructure Investments

- There are essentially **two epicentres in MENASA** : GCC & India
- Massive infrastructure investment by GCC countries has been a major factor & contributor to recent (2003-2008) economic growth, productivity gains, increased private sector investment and diversification.
- As of Apr 26, 2010, MEED Projects estimates value of projects planned and underway in the Gulf region at $2.26trn.
- India is the second hub, with close to 500 bn in planned Infrastructure Development till 2012.
- **Complementarity on both production & financing side**: GCC are resource-based, K exporters with abundant liquidity; India & others might require this to meet their infrastructure demand.



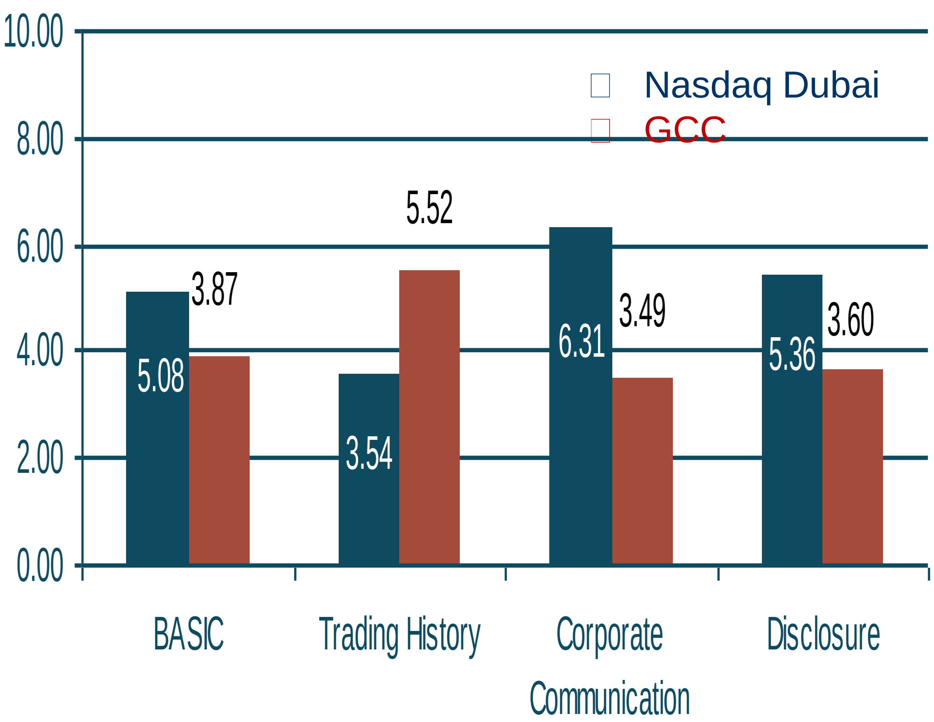
- Infrastructure spending continued despite the financial crisis: helped stabilize economies, avoid contagion effects from credit crunch & sustain growth.
- It is imperative to accelerate the pace on infrastructure & network projects that foster ***regional integration***

Source: MEED Projects

Transparency & Disclosure

One of the important lessons that came out of the global financial crisis was the need for increased transparency and disclosure – both at company and product level.

- The continuing reporting requirements of DIFC-listed companies results in high levels of transparency and disclosure.
- The BASIC report was developed by The National Investor and Hawkamah, (www.tnihawkamahresearch.org/), providing systematic insight into a number of essential parameters (including transparency & disclosure) which constitute the backbone of Corporate Governance
- NASDAQ-Dubai companies, which were included for the first time, came in as BASIC leaders compared to regionally listed companies.
- Nasdaq Dubai companies scored some 31% higher on than the GCC average.



Source:

Risks to Recovery

1. The fiscal crisis in major economies, USA, euro area, Japan

i. Inflationary pressure build up

ii. Crowding out of private investment => drop in productivity

iii. A weak recovery is not sufficient to generate enough resource to repay the fiscal debt => the Japanese syndrome spreads

iv. Pension systems' liabilities (and the health care reform cost in the US) become unsustainable

2. The persistence of current account imbalances

i. Developed countries try to continue living beyond their means

ii. China and Germany persist in their mercantilist approach

3. A property bubble in China

4. Indecision over a new financial regulation framework

i. Different country approach lead to intensification of regulatory arbitrage

ii. Re-emergence of the shadow bank

iii. Too big to fail or too interconnected to fail issues remain unaddressed

Structural Reforms

1. **Bankruptcy Law Reforms**
2. **Corporate Governance**
3. **Property Law**
4. **Company Law/FDI Law reform: majority ownership**
5. **Market Information Infrastructure: central credit reporting; companies' house**
6. **Regulatory compliance**

Transformational Role of the DIFC

DIFC has achieved **critical financial mass**: it has in place a sophisticated framework of laws, regulations & governance, modeled on international best practices

- Provides market infrastructure for GCC bloc to emerge as economic and financial hub for MENASA region
- Provides comprehensive platform for listing, IPOs, privatization, project finance, securitization
  - Opportunity for companies to tap into regional liquidity
  - Conglomerates may use regional capital markets to raise funds via primary & secondary listings
  - Establish vehicles (eg. PE funds): give regional investors exposure to MENASA markets
- Lower access barriers to financial services
- Lead integration of financial markets: starting with DFM + Nasdaq-Dubai
- Develop Regional Debt Market
- Build payment system infrastructure for $ and Euro payments

Change in Global Economic Geography requires accompanying change in Global Financial Geography