IFN Islamic Finance news
The World's Leading Islamic Finance News Provider

DUBAI ISLAMIC ECONOMIC ROUNDTABLE

SERIES 2014 – 5

Wealth Creation and Wealth Management in a Shariah Compliant Manner

Panelists

Morgan Lewis
Ayman A. Khaleq
Managing Partner (Dubai), Morgan, Lewis & Bockius

AZIMUT
Giorgio Medda
CEO, AZ Global Asset Management, Azimut Group (Istanbul)

RASAMEEL
Issam Z. Al-Tawari
Chairman & Managing Director, Rasameel

NASDAQ DUBAI
Moinuddin Malim
Managing partner, AIMS

DFSA
Prasanna Seshachellam
Director & Head of Islamic Finance, Dubai Financial Services Authority

In partnership with

GOVERNMENT OF DUBAI

Dubai Economic Council

DIFC Dubai International Financial Centre

Morgan Lewis

Our Islamic finance team

advises public and private entities on a full range of Shari'a-compliant investment and financial products. Our practice has experience in conventional and Islamic debt and equity capital markets, banking and structured finance, fund formations, structured products, restructurings and workouts, and project finance. We have worked on the first private Sukuk offerings out of Germany, Luxembourg, and the United States, in addition to Oman, and continue to be active in representing foreign issuers in raising debt and equity from Islamic investors.

together

contact
Ayman A. Khaleq
+971.4.319.7936
akhaleq@morganlewis.com
www.morganlewis.com

Almaty • Beijing • Boston • Brussels • Chicago • Dallas • Dubai • Frankfurt • Harrisburg • Houston • Irvine • London • Los Angeles
Miami • Moscow • New York • Palo Alto • Paris • Philadelphia • Pittsburgh • Princeton • San Francisco • Tokyo • Washington, D.C. • Wilmington

Panelists:

Ayman A. Khaleq
Managing Partner (Dubai), Morgan, Lewis & Bockius

Giorgio Medda
CEO, AZ Global Asset Management, Azimut Group (Istanbul)

Issam Z. Al-Tawari
Chairman & Managing Director, Rasameel

Moinuddin Malim
Managing Partner, Alternative International Management Services

Prasanna Seshachellam
Director & Head of Islamic Finance, Dubai Financial Services Authority (DFSA)

Ayman Khaleq is the managing partner oft Morgan, Lewis & Bockius' Dubai office. He focuses on advising clients on corporate and structured finance and debt capital market transactions, as well as restructurings and investment funds. He has particular experience in the structuring and documentation of innovative Islamic finance transactions, having advised on the first corporate Sukuk (Islamic bonds) issuances from the US, Germany, Luxembourg and Oman.

Giorgio Medda is the CEO and fund manager of AZ Global Asset Management, the Turkish platform of Azimut Group. Previously he worked at CSFB (now Credit Suisse) in London and Mediobanca in Milan as a sell-side equity research analyst covering European and emerging markets.

Issam Al-Tawari is currently the chairman and managing director of Rasameel Structured Finance; and also chairman of Dubai-based Rasameel Investment Bank. He is the ex-chairman of Ain Takaful Insurance Company and ex-chairman of Binaá & Namaá (Sorooh) Investment. He is also co-founder of Ritaj Investment Company.

Moinuddin Malim is the founder and managing partner of Alternative International Management Services (AIMS), a boutique Islamic advisory partnership. As the former CEO of Mashreq Al-Islami and head of the Islamic Banking Division of Mashreq Bank, Moinuddin has over 25 years experience in the Islamic finance industry.

Prasanna Seshachellam is the director and head of Islamic finance for the DFSA, and is responsible for the supervision of prudential risks faced by all authorized firms operating in the Dubai International DIFC, with specific emphasis on the banking and insurance sectors and including the supervision of credit rating agencies and registered auditors in the DIFC. He leads the Islamic Finance Initiative of the DFSA, and represents the DFSA in the Technical Committee of the Islamic Financial Services Board.

[Disclaimer: The views expressed in this publication are those of the above and do not represent the views of and should not be attributed to the Dubai Financial Services Authority]

Wealth creation and Wealth Management in a Shariah Compliant Manner

A group of leading industry experts recently gathered at the Dubai International Financial Center (DIFC) under the aegis of IFN and the Dubai financial authorities to discuss the current lack of a robust and material Islamic wealth management sector that can meet the needs of its high net worth clients and attract them away from the conventional arena.

The crux of the discussion revolved around the lack of a track record in Islamic wealth management and the current inability to attract investors. An average Middle Eastern high net-worth individual is said to be around US$890 million. So where are they investing, what asset categories do they favor and what can asset managers do for them?

Islamic Finance *news* was delighted to bring together the comprehensive knowledge and experience of leading industry experts including Ayman Khaleq, Giorgio Medda, Issam Al Tawari, Moinuddin Malim and Prasanna Seshachellam. Representing a cross-section of the wealth management industry from top to bottom including advisors, lawyers, regulators and participants, the panel achieved a rewarding and challenging discussion.

IFN: What we're going to be focusing on is the lack of track record of Islamic wealth management and the problems in attracting investors - and where current middle eastern high net worth investors are putting their money and what Islamic asset managers can do to attract those funds. Let's just kick off with a very general question to start off with: is there such a thing as Islamic wealth management as an industry? Is there a specific sector for that yet? Perhaps I can hand that over to the fund manager first of all – Giorgio?

Giorgio: Well I do think that at the moment if you are looking at wealth management financial services in general, Islamic wealth management would probably be a sub- component of the whole industry, where certain needs and objectives of investors are fulfilled within the context of the Shariah. So when looking at the market overall, there is not a specialized Islamic wealth management industry in my view. Obviously there are many Shariah compliant products that can be part of an Islamic wealth management or private banking mandate, but it's very hard to see in the industry today, a clear perimeter or a clear size with a track record that can be measured.

In this respect I do think there is huge potential for such an Islamic wealth management business to develop – obviously along with the development of products that are compliant.

IFN: would you agree with that?

Issam: I think that there were attempts to create Islamic wealth management back in the early 1990s. Moinuddin and I both used to work for a firm called The International Investor, which was set up in Kuwait and which made one of the first attempts to create and develop Islamic wealth management. I think the first year they launched six funds and were able to attract investors and funds under management after five years of about US$3 billion. So there was an attempt. However, this is a very sensitive industry in the sense that it is prone to a reputational risk. It is also a business of scale.

However, if you look carefully at the industry, it is about 80% retail focused, and only 20% institutional. In the West, it is 70% institutional, 30% retail. So in order to get the scale and size in a global we need to see institutional investors - the likes of pension funds, insurance companies... they are not investing in funds, which would basically develop the wealth management offering. That's the challenge that we see at the moment.

Moinuddin: Let me just add to that. The International Investor was a pioneer – before that, there were a few other banking groups that started as well. But Sedco today is probably the only specialized, unique Islamic firm to be an asset management platform and a range of products. To be a successful wealth management entity you need to have the right asset managers – I think that's where we see a slight disconnect. And the disconnect is not because of industry players not being able to size the industry – it is basically lack of trust, and what it takes to create that specialization.

Asset management as an industry is substantially large; one could not put a figure to it. What is value of global asset


Ayman A. Khaleq

management - I don't know, US$100 trillion dollars? Probably more, possibly less. But if you look at the Islamic arena – Sukuk has become a speciality product: Sukuk funds have emerged and are doing very well. But where are the other specializations? We don't have specialists sitting in Islamic banks. If you look at Al-Rajhi, which is the biggest Islamic bank, to Dubai Islamic Bank, to even the Malaysian banks: you don't have sectoral specialists within those banks who can guide them into different sectors, like what multinational banks who have experts industry analyst and specialists for example, telecoms, oil and gas, transportation and so on. From their sectoral expertise you develop the asset management capabilities and take advantage of emerging market trends, expected growth forecasts and they create investment opportunities as well diverting part of their own liquidity into it and market it to their private banking channels as well selling across the board to others. That is lacking in our industry. We are very much focused on retail and a few investment products, corporate banking products – and that's about it.

Ayman: Just to add something, I service the industry – I'm not in the industry - so I've been looking at all these developments. And one big disappointment from my point of view, when I first started as a junior associate, I was given on my first day on the job an assignment that involved structuring the first Shari'a-compliant capital-protected fund for one of the large Saudi Arabian banks. I knew nothing about funds let alone Islamic funds, and let alone call options and structured notes - so I had to learn it on the job the hard way. That was 1998-99. But the point is that many of these issues are still there, and we are in 2014. Basically we have seen innovation but has there been enough of it? Everyone is passing around this number, this dollar size – the US$2 trillion industry – but where are we really? Seriously, I am curious. And I am not talking as a practitioner but as somebody who picks up the

newspaper and reads. US$2 trillion is supposed to make a big impact on the economy, on investments, on the kind of products we have, but I doubt that we see such impact. So that's the first point – real scale, versus the advertised figures. Secondly, the human resource deficit. We have also been talking about this for years and years. This is why when we did the first Sukuk in the US, which was oil and gas-related, the boutique outfit that had actually secured and pretty much structured the deal didn't have energy-specific and US transactional expertise. So they brought in Merrill Lynch which, obviously, had the energy and US transactional expertise. We still see they human resource deficit play out a lot – among bankers, lawyers and, more importantly, Shariah scholars So what's the solution? It comes up at every conference, at every roundtable. I frankly cannot think of any solution that does not entail a big investment and over a long period of time.

> ***"It's very difficult because there isn't even a size of the Islamic wealth management –we say around US$90 billion, but nobody knows for sure"***

Moinuddin: There have been attempts made, for example, by HSBC Amanah – they established some 12 plus Islamic products, which were very decent offerings and focused on various segments of the economy. But what they couldn't do is get their Islamic private banking model up and running. Why is that? First because I think there is a commingling of the investor base. If you look at people who are ultra high net worth investors in the region, there is ambiguity as to how you segregate people or separate out from who is pure Shariah compliant, and who is neutral – people who want to have better products but who would not sacrifice that for a lower return and take higher risk if it's an Islamic product. Those questions are not being answered.

Ayman: But someone did a study once and they came out with the conclusion that 60% of Islamic investors prefer Islamic products provided it is not more expensive than conventional products.

Moinuddin: All the surveys are there. A recent one for example about sizing was from Thomson Reuters, which said that the total estimate for Islamic asset management right now is only US$56 billion - which is really small .

Ayman: Yes, this sounds a lot more realistic.

Moinuddin: Yes of course. I mean US$2 trillion is the size of the entire Islamic finance market – but even that, you think - where is that number coming from?

Giorgio: I also think that in terms of structure there are two very important issues. One is related to the lifecycle of the asset management industry: because very often people talk about asset management and wealth management like they are the same thing. Asset management for me is something very much related to individual product management: it's a system or a method of investment where we look at asset classes and try to find the best way to manage it to make money. Wealth management is more the offering of multiple products in the context of a specific investment objective or financial goal.

For me when we talk about Islamic wealth management we should really talk about financial advisory. Financial advisory is a business model in the extreme of the lifecycle – it is very developed in the US and more developed now in Europe. People talk to the financial advisor to understand how to manage their money in the context of their entire lifespan. They need to understand how to manage their money because at some point they are going to retire, they are going to pay for tuition fees of the kids. Real life objectives.

When we are looking where Islamic finance should develop – in the Middle East, in Southeast Asia – it's far too early for this business model to be stretched to that level. We are talking about a huge pot of wealth – US$2-3 trillion, there are all sorts of numbers on the table. But I think we are at too early a stages to be thinking about wealth management in context of conventional standards. And to that extent, thinking about Islamic wealth management as comparable to conventional wealth management? This is a topic we will be discussing for the next five to 10 years – it's far too early. Also, markets do not allow you to create products which are that sophisticated. Another aspect is the role of banks, I think particularly in the Middle East, banks still have a dominant position; and there is no interest whatsoever for a conventional bank to develop wealth management or financial advisory because for them it's much easier to raise funding to get the money or the customers through deposits, and to use those deposits to do business elsewhere.

Obviously to doing wealth management is something else. And also, here in the Middle East people are more likely to look at the deployment of their cash abroad, away from this region: and again, the availability of Islamic products and strategies away from the Middle East and Asia is very limited. So there are a couple of structural issues that inhibit Islamic finance, Islamic wealth management, from developing naturally. But the underlying markets are now developing, so now it is just a question of getting the right products in to create that infrastructure.

Moinuddin: Let me take your train of thought - we see wealth and asset management go hand in hand. You can't create effective wealth management division unless you have the asset management capabilities, i.e., be an efficient and effective aggregator of Islamic investment products. If you look at the likes of Coutts or Merrill Lynch or Credit Suisse, they are not creating their own products. Whereas one of the key issues that we face – if you look at any Islamic bank they want to create their own product and make sure that they also manage it themselves. They don't want to trust that money

with third party fund managers. So what we don't have today are the Islamic asset aggregators. For example, Credit Suisse came into investment banking and they left it two years ago, saying this is not our piece of pie. And their focus again went to private banking. They had huge losses when they came into investment banking. So again, with Islamic – other than Sedco and perhaps few others, I don't think there is any single fund manager who could be classified as a effective and efficient Islamic product aggregator - and that is what you really need to be an effective Islamic wealth or private banking entity.

Ayman: But then again, their impact on the financial crisis...?

Moinuddin: Yes, but you see they are creating their own product. If you go to Merrill Lynch or Coutts or Credit Suisse - they will show you everything they have in the universe you need to give the client the right portfolio, based on the risk profile or the return criteria the investor desires. Whereas in Islamic wealth management you don't have the same thing. Islamic banks, first of all, don't want to create the product because it is too expensive to put together and time consuming as well . Any time you talk to an global fund manager to structure an Islamic proposition – you'd need at least US$100 million of commitment to create that Islamic product. Where is that investment? It is not there most of the times.

IFN: Giorgio, I am interested in your point about banks and about deposits. Speaking as a former private banker, I used to work in high net worth and the majority of our clients' funds were probably held in cash products most of the time. Only a very small proportion of funds at any one point were being channelled into funds or structured products, on the retail side. So surely there is an opportunity for wealth management, for Islamic financial advisors, to take those deposits and do something with them? Specifically, I think the question we are trying to answer is why this advisory service itself has not yet developed in the Islamic financial world. So bearing that in mind and moving onto the next question: where are high net worth individuals placing their money right now? Where are the funds going?

Ayman: Switzerland!

Moinuddin: Although with the new transparency laws and changes in tax regimes, a lot of money is coming from abroad back into Dubai; however, most of it is diverted into real estate.

IFN: Prasanna, are you seeing that - and is that something you're trying to encourage?

Prasanna: I'll try to address the previous question in a different way: as a regulator and as somebody who has been watching the Islamic finance industry for the last seven years closely, as an outsider. I don't do business.

I think the industry has to take a fundamental approach to asking the question as to why the growth is happening, but not in a substantial manner: in a manner which will grow the


Giorgio Medda

industry in a sustainable fashion. Looking from outside as a person who spends a lot more time in the conventional business, I think that Islamic finance, the Shariah compliant way, actually lends itself naturally to providing financial services to clients, to consumers of all kinds, in the best way possible. Particularly when you talk about what we call in regulation as conduct of business regulation (there is prudential regulation which talks about risks, and then there is conduct of business regulation). Conduct of business is relatively new to Asia and definitely new to this part of the world. But Islamic finance lends itself naturally to dealing with this conduct of business, to providing financial services in the right conduct. Basically treating customers fairly and related aspects. The problem is that the industry – be it in funds, be it in wealth management, be it in banking, in Takaful, anywhere – the industry is so much focused on growth, on top line assets under management, on performance metrics- . Added to that is a resource constraint in terms of the number of people who can really understand and make the difference.

So it's all about running and trying to get the immediate target finished and then you are done and you move onto something else. And what you're left with is a whole lot of products and services which are mimicking something else - and from a conduct perspective its actually delivering, as a regulator, an undesirable result, opposite of what is expected.

I would normally expect it to deliver a result which is so good that as a regulator I can take comfort that this is a Shariah compliant fund so I don't have to look at conduct of business. But actually what's happening now is that I have more worries. For example the key things are fiduciary responsibilities -duty of care and diligence; ethical products. Giving the customer what you are actually telling them, or telling what you are actually giving - disclosure in the right sense. Not serving or providing a product in such a way that the customer is going to be disappointed after he takes it – which is what I call classic post-purchase cognitive dissonance.

The way in which the industry is working right across the board – regionally, type of customers, type of business – there is so much focus on just getting the deal done, and what is invariably happening is that people are attracted to the products, growth is happening in a whole lot of areas and due to a whole lot of reasons, but substantially every consumer at every level is going off thinking well OK but this is just a façade, this is a show. Because the industry is not coming up with products which substantially comply with Shariah criteria and actually giving the target market, the people who want Shariah compliant services and products, something they can taking home thinking yes, I came looking for this. Now that disappointment gap is still there. And this has been around for 15-20 years.

> ***"The segment which nobody can capture is the ultra high net worth set, where the family offices and the bigger distribution houses come in. These guys, if they want to do Islamic, they will go and directly invest their own money into projects and assets categories they desire"***

Issam: I don't necessarily agree with that statement. I take what you are saying but I think what you described is more of a general sort of phenomenon that's not special to Islamic financial institutions. You would find that even with conventional institutions that are operating this market, because they are operating in a very competitive market. The issue is highlighted more with Islamic financial institutions because they are supposed to be basically a form of ethical finance, and hence one would expect them to be even more diligent. And so that's the issue. So the observation is not specific to Islamic financial institutions.

Going back to the point of Islamic and non- Islamic: all Islamic financial institutions that are offering these products have a Shariah committee which goes thoroughly through the products, and they give them a hard time before they approve anything. So that is a Shariah compliant product. The issue here is that if you take that product to another institution, if their Shariah committee is from a different school of thought, they will raise issues and concerns. This has been addressed actually, in more developed market like Malaysia, where they have established a Shariah committee at the level of the central bank which basically gives their Fatwas so that you do not have inconsistency in that market because there is one reference point. Hopefully this will filter through into other markets.

Having said that, it is true that there are situations which were exposed during the financial crisis, where people who do not necessarily belong to the industry have taken advantage of the industry. Hence that's why I said that there's a reputational risk associated with this kind of business. Because once you have a problem people will lose their trust and they will never come and invest in your product. And your capability to develop new products and sell more into the market diminishes considerably. And I've seen it because I've lived through it, I have had personal experience, where we've seen that whatever you do you – you can bring your best product, the best innovative product, and it will not sell because people don't trust you anymore.

Prasanna: I do agree with the point you've made. You've actually answered the second part of what I was going to say. I was not trying to find fault with the industry, I was just trying to find out how the industry can grow sustainably - in the sense that if you look at fundamental critical success factors with this industry, one of the things that they can leverage is the fact that they are being Shariah compliant. This lends the industry naturally towards being ethical, to providing financial services to end consumers in a way that builds confidence and trust. That's natural to it. In conventional business it's not natural, conventional financial business is just financing business made for profit and they have to do it this way because of regulation. That's the first point I was trying to make.

When I initially looked at this I thought wow, this looks great – if they actually go about doing it this way then that's exactly that what as a regulator I would want them to do. And that's exactly what would bring, as you say, confidence and trust with the customer. But the problem is – and OK, maybe I am broad-brushing it – but the majority of the industry is trying to deliver Shariah compliant financial services and products, in the same way as the conventional industry, and that doesn't help.

As you rightly said, Shariah compliant finance sets the bar high. That is the beauty of it - by setting the bar higher and performing to it, you are actually going to take the industry to a next level and achieve that. In the short-term that is always going to be difficult. You're competing with others. But after all the pain and the structural development, by judging yourself by higher standards you are going to hold a higher ground and that will actually not only develop the industry in a sustainable way, it will also make your product stronger.

Issam: Actually I've been in this industry for twenty years and I can tell you the short answer to this. The challenge was basically at the infancy stage you had people who believed in the industry and had their faith and trust in the industry. As the industry grew rapidly and had to find professionals, you had to bring in some professionals who were technically sound but did not necessarily believe in the product itself. So therefore basically interest and profit was the same to them. So they ended up shortcutting the whole thing and that's when we started having issues. It's just this rapid growth - at one point we had just 10-20 institutions and now we have 250.

Moinuddin: There's a dichotomy here, and the dichotomy is that Islamic banks are pushed by regulators to act like conventional banks. Even if you look at Malaysia they have parallel banking system, but they have not really encouraged Malaysian banks to develop what we likes to see as a pure Islamic banking model. Well, first of all I don't believe in the term 'Islamic banking'. There's no such thing as 'Islamic banking' – there is Islamic investment, Islamic financing, Islamic asset management, Islamic insurance... but 'banking' is a misnomer. Islamic intermediation of any form pertaining to finance or investments as such is all part of the Islamic economy. So you need to have the right models where you should encourage "true" partnership, encourage the fiduciary role andencourage risk participation. Do such model exits in any shape or form today in a regulated environment? They are nowhere to be found. Unfortunately it's not just the practitioners that have come into Islamic banking who don't differentiate between "profit" and "interest" (some even going at length to argue that they are one and the same)- but it is also to do with regulators. Regulators even in this region or any region – they are pushing Islamic banks and Islamic finance companies to act like and work like and are regulated like any other conventional bank. Once you act like one, you are one!

Prasanna: I can explain that. The point you make is correct. You don't have to actually provide Islamic banking - all you should do and tell the potential customer is that: OK, I will manage your money, I will invest your money and share the risk. But what happens is that when Islamic banks starts working like conventional banks then there are other risks, like for example, financial instability risk, that we do have to take into consideration. So any central bank, even the Central Bank of the UAE – we actually don't have that problem because we don't have central bank authority in the DIFC. But if you are responsible for a country, and responsibly for monetary policy, financial stability, macroprudential issues – that is when I have to deal, as a regulator, with Islamic banks as with conventional banks – because they are behaving like regular banks.

And that is a problem. If they behave like a bank and appear to the customer like a bank, then if something happens to them then the customer is not going to differentiate between them as a 'bank' and an 'Islamic bank' and they will lose trust in the industry.

Moinuddin: If I can explain my argument. Until January I was CEO of Mashreq al Islami for the last four years – it is an Islamic window, one of the better windows. The chairman of the UAE Banker Federation founded 10 committees and one of them was Islamic, and I was elected chairman. So we looked at all the things that the committee could do, and we looked at all the regulators who are also regulating Islamic institutions and we addressed to the central bank of the UAE with a draft proposal, that it was time for them to have a Shariah Governance and Compliance unit at the central bank. It has been a year and a half and they are still looking at the paper. The point being that there has to be a proactive approach by the regulator to accept Islamic finance as an integral part of the finance industry, and to regulate it differently. Prudential regulations don't change, but you need


Issam Z. Al-Tawari

to put an extra layer of Shariah governance and compliance over the top to make sure they are acceptable.

And secondly, the biggest dichotomy that we face, from my experience when I was at Dubai Islamic Bank is with customers themselves. We had substantially large family group, very respectable and known for their desire to be adapt Shariah compliant banking and finance. They were building a mega mall in the UAE and had secured a prime land for it. They approached the bank and said that they wanted a pure form of Shariah compliant finance. And they also informed the bank that they were working with other banks who are offering conventional financing but since they prefer Shariah complaint financing they wanted the bank to consider entering into a Musharakah arrangement with them. The bank decided that since the group have acquired the land, was willing to commit additional equity towards construction and showed a detailed feasibility where the IRR was projected to be upwards of 30%, the bank may participate in such a risky financing model. As this was one of the good relationship, the bank offered to partner with them under a Musharakah arrangement as requested by the customer where the bank was willing to share the risk, invest its capital and take a share in the profitability. The capital contribution worked out to be 60:40 with 60% funding from bank and balance from the customer. This tantamount to risk / reward sharing at similar ratios. The customer was bemused, turnaround with a frown and stated that they has an offer from the conventional bank at LIBOR +3% pa and if the bank was willing to entre into this Musharakah at this rate, only then they will consider. This is where I witnessed Islamic banking goes up in a puff of air. The basic concept of Islamic finance of risk participation and sharing of reward will only work when it is acceptable from all perspectives, essentially a tripartite arrangement between the regulator, the financial institutions and the end-user / investor.

IFN: So if I can just step in here: we are trying to concentrate on Islamic wealth management so if we can just pull it back – you have all made valid points so if we can start relating these back to Shariah compliant wealth management and return to looking at where high net worth clients are investing right now, where are they putting their money? Giorgio – I know you are based in Europe, what are you seeing?

Giorgio: Well obviously there is an abundance of market research regarding the amount of financial wealth in the Middle East region. Last week I saw something that said financial wealth in the Middle East is an excess of US$5 trillion. When we are looking at asset management or wealth management we will probably be looking at about half of this – US$2-2.5 trillion. And it's a very well-known fact that probably the Middle East region is one of the top in world rankings when it comes the amount of wealth held offshore – and again here there is plenty of market data. We are probably talking about US$1-1.5 trillion of Middle Eastern wealth being held offshore - mostly in Switzerland, although I'm sure there is also money in the UK or the Channel Islands.

Ayman: But that's not Islamic.

Giorgio: No, no in general… as matter of fact i think its zero Islamic, in financial terms.

> *"Rich people in this part of the world are very much richer than the very rich people elsewhere"*

IFN: Well that is a question - are there Islamic offerings offshore? Are we seeing Shariah compliant offerings develop in offshore centers as well, is there any demand for that?

Issam: If you are talking about Shariah compliance there are three centers: Luxembourg, the GCC and Malaysia. That's where the hub for this is.

Giorgio: But let me give you an example – even if you look at every country over here. One of the biggest Islamic wealth management wealth platforms at the moment is Qatar. But most of the products are either Luxembourg or Ireland-based - these are platforms that allow all the pieces to be run through managed accounts. It's a very effective way of running a private banking or wealth management platform. This is essentially offshore money run through indigenous financial institutions in the region. So it's very hard to say how much of it is offshore or onshore because essentially you go to your bank in Doha and you leave the money there but the money then is offshore. You give your money to Luxembourg or Ireland but it's not necessarily offshore like it would be if it was held in Switzerland or the UK - particularly Switzerland. These are viable and legitimate offshore platforms where you have many benefits beyond the simple fiscal or secrecy aspects.

So it's very difficult because there isn't even a size of the Islamic wealth management –we say around US$90 billion, but nobody knows for sure. When I'm looking at the funds size probably you're talking about US$30-40 billion - and for the mutual funds business, that is very very small compared to total wealth. It's no mystery that when you look at mutual funds industry in the Middle East this represents 3-4% of the GDP - compared to 150% in the UK. I'm coming from Turkey and the number would be very similar but if I'm looking at Italy, again funds there are 40-50% of GDP. So this is a sign that when it comes to wealth, as opposed to the total size of the economy, most of this money is actually held in cash or real estate, and comes away from official rankings and away from the possibility of seeing where the real money is held.

Moinuddin: But you have to take that into consideration and look at how Middle East is actually organized. Number one –the saving behavior pattern is very low in the Middle East compared to rest of the world. If you see statistics you will see that the saving pattern is only 7-10% depending on the country. Number two: the way the wealth proposition is looked at by local banks, they have wealth proposition which is for the affluent segment, then have a private banking segment for high net worth; both segements are under served due to lack of products and poor customer profiling. But then the segment which nobody can capture is the ultra high net worth set, where the family offices and the bigger distribution houses come in. These guys, if they want to do Islamic, they will go and directly invest their own money into projects and assets categories they desire - they don't go to any fund managers. In the midst of crisis, when the subprime real estate issues hit the global markets , a lot of GCC players went in and started acquiring properties and acquiring businesses. Kuwait is a prime example. When you look at Kuwait, at one time it had 100 investment companies listed on the stock exchange – and most of this 100 were owned by wealthy families and – and their own wealth just became a private investment arm of these companies: going in buying Aston Martins, Governors House, banks, you name it. And that's the pattern, that's why you don't see them investing in funds - because at the product level, they don't have that product sophistication and there is no aggregator out there who can show them the type or variety of product that maybe they need.

Giorgio: But it's different because there's always this misconception about high net worth individuals in the region. Rich people in this part of the world are very much richer than the very rich people elsewhere. I mean the average wealth for an HNWI client in the region is 7 or 8 higher than a HNWI elsewhere. Obviously when we're looking at this for private banks, this is an ideal market. If you are cherry picking, you get five customers and you will probably make the same business size as you would with 2,000 elsewhere. The fact is though, that these are not the typical customers that should be targeted, when it comes to Islamic wealth management. Affluent, high net worth individuals - those should be the people that banks and firms are looking at.

Moinuddin: Yes, but the range of products are not there.

Giorgio: Because there is no underlying market! Let me make an example, if we say that 50% of the wealth in the region is invested in cash and real estate, then by definition there's no space within this part, this considerable part of the wealth, for Islamic finance to take any role. First because when it comes to cash - forget about Sukuk for the moment, about addressing the issue of low risk, low returns – when it comes to safe investment there are no products. There is nothing available. Even liquidity management under Shariah compliant mechanisms is very ineffective and inefficient compared to what you can find in conventional.

Ayman: 30-40% of the funds actually are money market funds.

Giorgio: That is very typical in this part of the world.

Ayman: No, we are talking Islamic…

Giorgio: Yes, but I am talking generally. When you are looking at asset management, in many parts of the world everything is in cash. In Turkey, 95% of the mutual funds are money market funds. The fact is when you are looking at these parts, these typical asset classes, there is nothing available. There is no market. In fact, the development of a healthy Sukuk market makes people look at a different asset class, that might satisfy those investors who need to invest in low risk, relatively high return, relatively safe investments. But when you look at what is there in the market right now, there is nothing viable. So this is the problem with Islamic wealth management, asset management, this is my point. In Islamic asset management, most of what is out there is equity funds, commodity funds, with an Islamic wrapper. You go out there and you get your Fatwa, and you say you are not investing in Haram industries, and you can call it a Shariah compliant equity fund. But how many people are investing in equities here? Not many. People who invest in equities are either super rich, or...

Ayman: No, no – I think we need to have a clearer understanding of how the market is behaving; the way I see it, a good chunk of these investments are more focused on long-only equity interests as well as real estate. This is reflective of an investment appetite that preceded the growth in Islamic banking so many Islamic investors are following this tried and tested path and focusing on the type of products that their conventional peers from the region have focused on in the past.

Prasanna: I think the point here, in a more fundamental way, is that if you look at wealth management it's not just about products. Wealth management is not just about funds, products, structures - that's only a small part of it. When I think about myself, I think about relationship, trust, confidence, service. And then these other things - secrecy, where I want my money to be, succession planning – all these things matter as well. All these things need to be delivered by a potential wealth manager who can come to the whole issue and see the whole picture.

The point is that to come to that you need scaleability, and then you have to think about other aspects – training,


Moinuddin Malim

human capital. And at that point you have to think about how Shariah compliant you are – or the fact that you are a Shariah compliant wealth manager, how can you leverage that to take it to a higher level. That is the point I made earlier as well – I do not think that has been leveraged so well yet. And in the absence of that, you are only as good as any other wealth manager – as a conventional wealth manager, who is not Shariah compliant.

Moinuddin: While there is not short of human capital, in my opinion, Islamic banks and Islamic asset managers are not even close to their conventional counterparts – they are not even at near their level of sophistication, specialization or assets under management.

Prasanna: Yes, so then comes other factors: in terms of how big you are, how scalable you are, what is your tradition, what is your track record, what is the technology you have - and the other people beat you, becausethe Coutts, the other wealth mangers of the world, they have been doing this for years and they are way ahead of you. All I am trying to say is that Islamic wealth management has to close the gap. They need to look at what can differentiate them, because in this they are definitely behind all of the others. Simply because of the scale, size, track record, years of history and client base. The conventional managers, they already have 10,000 clients, compared to an Islamic wealth manager from Malaysia or UAE, who are still in a growing phase , and probably just have a thousand or so.

Giorgio: It's not even conventional wealth management here. You can have a foreign private bank, , who comes over, who tries to channel out the money - into markets that are not local. When I say people are not investing in equities, this is the result. When you're looking at the equity market capitalization of the GCC it is incredibly small as opposed to the size of the economy. People may still invest in the S&P 500 or in Euro stocks, but they are not investing in local equities. So people do look at equities as risky component of

the portfolios - but it's a small part as opposed to what you could have elsewhere. This is all I'm saying - that more than half of the demand for financial products that are Shariah compliant today are not addressed by suitable products. When you want to have more money invested in cash you just go to your Islamic bank you open your Mudarabah account. Maybe you want to invest in real estate, you might get your Islamic contract. But when it comes to Islamic equities - yes maybe you can put an Islamic wrapper around any equity structure in the world, but this is not wealth management. This is asset management. It is investing in equities, yes, but how is that equity portion going to fit in the context of your more complex investment portfolio? If you don't have a financial advisor how will you judge? We are not anywhere close to the level of sophistication of services that are provided as opposed to the conventional offerings in the area.

> *"Wealth is a by-product of capital markets"*

Moinuddin: This is one of the reasons that if you look at Islamic finance, most of commercial banks are trying to operate a wealth model. If you look at actual private banking they are nowhere, they are just commercial banks. When I set up the asset management and capital markets division at Dubai Islamic Bank from scratch, I was very successful - in three years' time I put out fifteen products but they were not generic off-the-shelf products, they were actual asset management products investing in real economy, in actual industry segments into assets such aviation, shipping, timber, water resources, development projects - where you have a genuine theme and true risk participation. And this sold very well. But then again, it was a commercial bank doing it. Coming back to your point, there has to be a starting point. You can set up a wealth model but unless you have products to support it, what are you going to sell? You can have best technology, the best people, you're ethical, you have trust arrangement but you don't have products - what are you going to sell? So it goes hand in hand.

IFN: So where are those products coming from then? This might be a good point to move on to Sukuk funds, which Issam, I know you want to discuss. Is that an area of growth we are seeing? Giorgio, I believe you just raised US$75 million for your new Sukuk fund...?

Issam: Well the way markets as we see them going, investors are particular about having yield, basically, so they are therefore focusing more on emerging markets – that's the first thing. And we are seeing a growing tendency towards an allocation to fixed income, and that's where we see the Sukuk funds coming to market. And over the past three years the number of Sukuk funds have actually doubled. But it's always a yield game, you know – especially for investors in this part of the world. They are not interested in the 3%, the 4% return. That's why outside the wealth management model, you find them going and investing directly, by themselves. That's why you see markets like Saudi have been growing tremendously over the past few years, especially the equity market – in terms of trading volumes -simply because interest rates went down, and they clamped down on real estate Musharakahs, so the next thing everyone started doing was the equity market. So they go in and out with huge liquidity: and this just proves to you that some investors, they like to be directly involved.

But investors in Southeast Asia are completely different. They have a much higher propensity to save, for example. Last year, 16 funds were launched in Indonesia, because it is a new market, new investors, and a huge target in terms of population. And people there tend to save more, compared to over here. In this part of the world, people spend more. So it is different markets, different characteristics, in terms of the way the behave.

IFN: Given that in these roundtables we are looking specifically at Dubai, let's perhaps focus on the way that Middle East and GCC high net worth individuals manage their wealth?

Moinuddin: Let me give you another example. We're talking about wealth, we're talking about asset management, but if you look at a different matter: in the Middle East investors basically invest in the equity market and the real estate market. Where are the domestic debt capital markets? We see equity but not debt. You need a balanced capital market where there are both equity markets and debt markets – that is what Malaysia has, and Malaysia now controls more than 60% of the Sukuk market – and 99% of those are ringgit-based. You have the sovereigns, you have the GREs, you have the corporates – all issuing ringgit Sukuk. Here in the GCC, where are the domestic, local currency denominated Sukuk? Where are the risk-free papers that you should see – short-term, medium-term, long-term. The thing is, that wealth is a by-product of capital markets.

IFN: So Giorgio, where is your fund investing?

Giorgio: For us I think around 75% of the fund is focused on the MENA region, and the GCC makes up around two thirds of the fund's exposure. You know I think what is happening now to the Sukuk world is pretty important – it's almost the perfect storm for bossting the industry. We are very close to an optimal environment for Sukuk as an asset class to make it through – to actually push Islamic asset management, the Islamic financial markets, to develop. There has been this big hunt for yield in the conventional part of the world, and Islamic is following that. As you know, interest rates are close to zero, and when it comes to Europe, investors have been seeking better yields in different asset classes. So Sukuk can come in very handy as they are fixed income instruments, but it happens that the measure of credit for a Sukuk issuer tends to be much better than for a conventional issuer, just because most of the Middle Eastern issuers are 'A' or 'AA'. And that is encouraging people to come to this part of the world – for the first time ever, they can invest in the Middle East. Also, they can do it without going through equities – a very thin market, with constraints for foreign ownership. Through Sukuk they can invest in Dubai, in Qatar, in Kuwait, in a way that they could not before.

So in this perfect storm, more and more Sukuk issues are coming to the market. The success of Malaysia or of Indonesia compared to the Middle East is for me related to the nature of those economies as opposed to the Middle East. A typical Sukuk issuer in the GCC is a bank. It issues Sukuk because it is a funding tool to develop and expand its balance sheet, as opposed to the development of the business. In Malaysia, real companies and real sectors, real industries, issue Sukuk to fund their growth and development plans. So for investors, through Malaysian Sukuk you can get exposure to these real economies, through an instrument that is fixed income, but still gives you the possibility of capitalizing on these growth opportunities that are embedded. Here in the GCC, most Sukuk are from financial institutions. For me, as the time passes, I think there will be more industrial issuers in this part of the world, and there will be more demand from foreign entities.

One aspect that is very important – when I look at the KL stock exchange, when a Malaysian entity issues Sukuk it is actually listed in Kuala Lumpur. Whereas here that is not the case. For example Al Hilal, a prime local financial institution - their Sukuk was listed in Dublin. That has all been the case for all the Qatari issues. So no one is really using the local financial marketplace to list their paper and to get investors over here to trade. Most of the Sukuk is listed in Luxembourg, in Dublin...

Moinuddin: I disagree with that. Today NASDAQ Dubai is ranked number three for international Sukuk and is expected to take over London by the end of the year.

Giorgio: It should be number one.

Moinuddin: NASDAQ Dubai is for international dollar Sukuk listing platform. Malaysia today, if you take the ringgit issuances out, is behind Dubai in terms of international dollar Sukuk listings. So my first point was that you need a domestic capital market - for which you have Abu Dhabi Exchange ("ADX") and Dubai Financial Market (DFM). My second point is that if you look at international dollarized Sukuk – Malaysia, London, NASDAQ Dubai, Ireland, etc. - NASDAQ Dubai is expected to overtake London, because of the number of international SUKUK listing it is attracting. It is attracting more a lot more Sukuk than others. Then in terms of your point regarding financial institutions, Islamic financial institutions actually started two years ago when they wanted to secure Tier 2 capital without raising additional equity capital. You will see in the Middle East the ratio of Sukuk issuance is roughly 70:30. Whereas 70% is government-related entities issuing Sukuk and 30% are financial institutions. Yes there are corporate Sukuk in between but the ratios is rather small yet increasing every year. What is the reason why many corporates are not issuing Sukuk? First of all if you look at the stock listing of the entities in financial markets you see they are mostly government-related or established entities and tightly controlled entities including banks. Where are the family groups, why are they not listing? Because the local regulators have made the environment so tough that they don't want to list. And if they do want to, they will go to AIMS in London. Because the regulators are doing overkill – they are making the regulations so tight in order


Prasanna Seshachellam

to protect investors, that they have killed the market before it can start in terms of corporates listing. Now if you look at Sukuk, let me share with you an antidote when I was part of a thinktank some 12 years ago when the central bank and Securities Commission wanted to look at establishing Bond and Sukuk issuance laws. And they instructed a law frim to draft world's best protective laws to safe guard the investors. Thankfully this regulator never saw the light of day, if it had, by virtue of this everyone looking to issue Sukuk must attain rating. How has Malaysia tackled this issue? They localized the rating agencies, adapted a rating grid which rated the Malaysian corporate a higher local rating that in comparison would otherwise attain two or three notches below as per the international rating agencies criteria, and that facilitated their issuance platform. Why, because, no legal entity would like to get below investment grade rating. This gave a tremendous boost and encouragement to local corporates and the results are in front of us.

Issam: Two weeks later they even allowed unrated issuance.

Moinuddin: Exactly - probably the facilitation and the Financial Services Authority (FSA) is better there, because the FSA is looking more at how to compete internationally, compared to local regulators…

Giorgio: I am sorry to interrupt you but I think it is in your favor, what I want to say. I disagree that you should look for an easing of the regulatory framework...

Moinuddin: I'm not saying easing, I am just saying don't kill the market...let it develop naturally and attain an equilibrium rather than coercing a behaviour pattern else these issues are not encouraged to come to market.

Giorgio: We are actually a Luxembourg-regulated entity, and actually when you look at the level protection provided to customers and investors it is the highest that you can get in the world. And that is good because you can go to any person in the world and he knows we are regulated by Luxembourg and that gives him confidence.

Moinuddin: Regulation doesn't mean that you don't have to relax that framework. Just don't overkill.

Prasanna: No, Moinuddin I think you are totally off the mark – I think what Giorgio says is right. Your points might be valid, but it just won't happen so let's not waste our time. Don't even talk about relaxing lender regulations, at least for the next few years – it just won't happen.

> ***"Let the market breathe, let it develop. If you babysit it to this extent, it will never grow up"***

Moinuddin: But I'm giving you practical approach: because I'm a practitioner, I know the market and know what is required to get it positively engaged in Sukuk issuance.

Prasanna: Well I will tell you the opposite side of it. We have the records, you can go to DFSA website on the enforcement page and see what has happened. If you have a proper, open and adequate approach to sharing risk, when you go out to issue capital, you have to accept the fact that people who invest in your company are part-shareholders, part-owners of the company. I don't think investors their family group members in general in this part of the world have matured to accept that reality. What they want is give me money. In fact I should expand that to most of Asia. The reality is that they cannot accept the truth - they think this is my company, I let come you in to give me money but only to certain extent because I must always control the company and you are a minority investor.

Moinuddin: So why do they go and list overseas then? Why don't they list there issuance with local exchanges here but they do list in foreign markets? Because there is an overkill of policy here!

Prasanna: AIMS' risk tolerance is different. For example, AIMS has no public policy to protect its investors. We also don't have that – that is why our policies are liberal. We have no public policy objective, we don't have to protect anybody. But SAMA, OCMA - they all have public policy objectives to protect their citizens, so they can't just open the door and let people come in and then not protect them.

Issam: But the point here, is that as a regulator you have different categories of investors. You have sophisticated investors and you have retail investors and these are totally different. Sophisticated investors have access to information, technical know-how and so on and so forth. And therefore, to say for example that all issues have to be regulated in this case is overkill because the sophisticated investor has the ability to basically make his own assessment and to decide whether that risk is acceptable or not. If I am going to target that product for retail then this regulation should be there, OK. But when you implement it into public policy, that's general, that applies to all categories of investor, and you just can't do that.

Prasanna: I accept your point but if you look at DFSA's framework we are actually rolling out a new super-exempt fund category, which is exactly like what you are talking about. No requirements, because you are targeting a professional investor. You just have to file a request, and you get approved, and you can start selling straight away. The point I am trying to make in a general sense, though, is that this is not the time at which you would expect a national financial regulator to relax its rules. I'll just say that different countries are evolving at different level. In Europe you have had these regulations for years, they have gone through many cycles, and different things have evolved. The UAE will reach that stage, but in the process, the first thing will always be to protect the market. Then after that, they will loosen up. So you are not going to get the best level of perfectly fine-tuned regulations right in the initial stages. It is an evolutionary process, and you have to give it time.

Moinuddin: Yes, but you could start by letting the market develop and encourage more issuers to tap the local markets.

Ayman: I agree with that. Liberalizing the market and "letting it be" is part of the growth process. Qualified investors have expectations and they will force managers to adjust accordingly. So long as a broad regulatory network exists.

Moinuddin: My discussion with the regulators always has been we don't want to let the market develop because investors will go bankrupt. Yes there will be cases, but then accept that, and respect that! Put in a regulatory framework which encourages regulators to come, and then define an Islamic layer on top of that. And yes, sophisticated investors should be treated differently from retail investors and if they lose money in the process that is not your responsibility. This is the only way investors will attain sophistication and will not be dependent on the regulator alone to protect them.
IFN: Let's just pull this back to the topic at hand. How many Shariah compliant wealth management clients would be sophisticated investors compared to retail investors?

Issam: There are lots, actually. When we talk about family offices, and high net worth individuals...

IFN: So is that a gap is Islamic wealth management? Is the regulation a big issue?

Giorgio: There are regulators from my experience, who are basically facilitators for business and they implement the framework and make sure everybody is working within that framework. And there are regulators - sorry to say this but they have no understanding of two way communication. It is like – this is it, and this is what I want done. And that really kills the business.

Prasanna: I agree but I ought to give a fair perspective - we can do that we can afford to do that, because we are looking at a wholesale market and our objectives don't include anything like - we don't have public policy imperatives at all. More of our focus is about developing DIFC so we have a largely free hand. Whereas if you go to other countries – I worked in Canada as a regulator and they all have these policy objectives which is the reason for their existence, the reason they get paid, everything. It's only to protect the investor and protect the market, everything else comes second to that. So I'm just saying let's accept the reality. I accept your point and let's say with Islamic wealth management, if you were to go to the next level, what kind of thing could you actually do? If the regulator takes a more fine-tuned approach, as you said, which is more risk sensitive it will develop and help the growth of the industry -no doubt about it, absolutely. But I'm just saying that at this particular point in time the regulator needs to focus on other issues. I'm just saying that this is not the right place and time to look for help from that sector. I am a member of the DFSA and we participate internationally in various fora and I can tell yo that international regulators are not thinking along these lines.

> *"If you look at Europe or Asia, people save for a rainy day. Here, we don't save"*

Moinuddin: That is because they are different as markets, they are all suffering, they are haemorrhaging because they had not regulated few financial instruments or had very lax regulatory framework mainly due to power of lobbying by large investment banks. But here the market has not yet started, so what do you start with?

Prasanna: But it is about what international standards dictate. Whether the subprime crisis took place in the UAE or not doesn't matter - there are international standards and every country is increasingly being forced to stick to that. India, Indonesia – they may never have had a CDS, but they still have to sign up to derivatives regulations, for example.

Moinuddin: Which is fine! But my point is that – say when Turkey issued its Sukuk regulations, for example. It passed a law encouraging any corporate that issues a Sukuk to give them a 5% tax rebate. That encouraged the market to start. But here, we said no! We said everyone has to be rated, and if not you cannot issue. That's the comparison. Local regulators have come a long way, but they are still restricting local issuers. Local issuers might not be fair, transparent, disciplined, whatever. But let the market breathe, let it develop. If you babysit it to this extent, it will never grow up.

IFN: Can I now pull this back to the supply side, as time is running away with us. Let's look at the actual wealth management platform that we have here, perhaps we could move on to talk about where the current gaps are in terms of Islamic wealth management, especially in the middle east. I'd like to hear a little bit from Ayman about that...?

Ayman: One player that we have not covered yet are the private banks themselves, the conventional private banks. What they're doing is, because they do have some Islamic investors, they react by "Islamizing" a product on an ad hoc basis. But they're not being proactive - they are reactive to the market. So we can't actually look at the industry by just focusing on the regional banks - the international banks, the private equity banks are actually looking at it, and some of them are saying: let's be careful because we're not Islamic banks. They are waiting for the investor to specifically request them to come up with derivative products, a capital-protected model..etc - and sometimes they can and sometimes they can't. This also takes us to another key point: how are these products being marketed? The one common denominator among local and international asset managers is that you're going to have to take that product to someone somewhere, and how you go about marketing it triggers all types of regulatory (namely securities law driven) issues.

IFN: Does that not suggest that there's a gap in the market where there could be an Islamic wealth management platform that offers that service - and if so why aren't people providing that service?

Moinuddin: There was, but the problem is that Islamic wealth renders itself very well to private equity. A few cases in point – in Bahrain you have a number of houses. Gulf Finance House, Arcapita, Bank Al Khair, Al Salam Bank, etc...in Kuwait there are a number of these as well. And they did very well when the market was up, their model was a valid model. But it was a private equity model, and they put in direct equity and then there was a mismatching of funds. They took in short-term funds and invested in long term assets, essentially instead of equity capital or pure private equity. And since private equity is not regulated, when the market tanked they all went bankrupt, as the banks started to pull their funding lines, banks also got effected. It wasn't that the right model wasn't there. Their funding strategy was not questioned by their shareholders, investors and funny enough even by the commercial banks who lent to them.

Having said that, in the UAE as well, we have a few private equity houses – but they are conventional. And we don't have an Islamic wholesale investment bank in the UAE either – whether onshore or offshore. There is a branch of a Turkish bank in the DIFC but that's it. The proposition just is not there.

IFN: Yes, but what about wealth management platforms?

Giorgio: The real gap today I think I think the real original gap is all about transferability. There is really nothing today to replace the power of a typical Islamic banking account. We mentioned low risk low returns, today most probably people are looking for more risk. They might look at all the solutions but when it comes to the open-ended product structure there is nothing available. That is the product gap. It may be because regulations are too tough, it may be because there

isn't much of a supply of this product but the product gap is the most important thing. I do think that over the next five years, that is probably the most important issue for a viable market of Islamic financial instruments to develop.

Moinuddin: But I don't understand why these products have to come from GCC or UAE. The UAE is an open country, there are a lot of investors, both local investors and expats, that have traditionally been investing either in their home countries or internationally. And now they can also invest locally. It makes no senses why should all these products should originate from the GCC or UAE? If you have a wealth management platform you can bring any products in from around the world with best asset managers with large assets under management and excellent performance track record. Local investors or anyone with right level of understanding and sophistication should be able to invest anywhere – there are no legal restrictions. So why should there be equity coming from this country to create new product offering?

> ***"We desperately need the right regulations to allow Muslim expats to do their own estate planning under local law"***

Giorgio: There are many important reasons, today say there are 1,000 Islamic or Shariah compliant funds. Most of them, let's say 90% are equity or commodities funds. What is the willingness of the typical investor here to put all his money into a risky asset allocation? People today want low risk - maybe low return but they want low risk solutions. The point here is to find instruments that respond to the need, and these instruments can only come from this part of the world. When it comes to Sukuk – it is a fixed income instrument but it is not even an option for western entities or a non-Islamic entities. So the point is that it is essential to create that market here, because the issuers are here.

Prasanna: There's capital here, investors are bringing the capital to the wealth management platform, and then the products can come from anywhere as long as the issuers demand it and the people are looking for capital. These are open economies where there are no capital controls and these investors have recently been investing overseas, so I don't think that the product has to come from this geography, it can come from anywhere as long as you have the platform and the product providers who can create it and bring it to them.

Moinuddin: Just to support this argument, there are attempts being made by entities within the DIFC to start looking at derivatives, ETFs - I think that's what he meant. That's outside of the money and equity markets we need to have more products of that nature in this market to facilitate the growth.

Prasanna: NASDAQ Dubai has done a great job in bringing international Sukuk into Dubai, even though the issuers are not here - the mandates actually bring Sukuk from issuers internationally, and they are getting here. There is no reason we cannot do that with other products.

Moinuddin: The point again is to do with savings - how a typical average wealth customer looks at his portfolio and saves. He's comfortable with local risk, and then he puts something in equities, and he buys real estate, then he puts in an insurance cover for his health, and then if there's money left he likes to creates an international portfolio. That's the typical pattern - and for that, the savings rate is too low. This is a consumerism society where people every year or every other year want to buy a new car, they will change their furniture – whereas if you look at Europe or Asia, people save for a rainy day. Here, we don't save.

Giorgio: That's very normal but when you think about wealth management industry not thinking about now but thinking about over the next five to 10 years… societies evolve into a savings-based attitude.

Moinuddin: We are all evolving … and since we're at the tail-end, the regulators and wealth managers are all working towards that - but unfortunately we don't have a model wealth program which is home-grown. It's all foreign-based. Yes, we are servicing the market by showing them the products, but when you look at the wealth model or private banking model that's when people become neutral in terms of - if Islamic is not there I want a product, so give me conventional.

IFN: So is there an opportunity in this market for there to be a home-grown offering, is there an opportunity for an Islamic bank to step in and fill that gap?

Prasanna: There are some areas. For example succession planning or trust and custodial services - where Shariah advice at a more specialized end of wealth management platform was attempted. We set up a few things which we thought were great ideas because that end of the spectrum of the wealth management business in the conventional sense has done very well globally and that's where you make maximum money in terms of margins and fees. I don't know they didn't really take off.

Issam: I'll tell you why. Sometimes certain ideas and concepts look very good on paper, but they have their own reality. You don't have the right set of people and they don't have the trust or the access to be able to convince people to bank with them or to invest through them. So it does not take off. Again, as we said earlier, this is a business of scale. If you don't have scale, you don't have mass, then you have no business case. The other thing is that if you have a general policy in terms of creating or developing a wealth management business, and you put regulations where you should put incentives, then for people to invest through wealth management, there is no reason for them to do so.

The first Islamic investment company was set up in Kuwait, and the reason was because the pension fund of Kuwait was basically backing that company. And that company has

grown from a US$50 million company to having over US$3.5 billion assets under management. Why? Because you had institutional investors backing up the wealth management concept. But if you try to start from scratch without having institutional investors it will not work - and the minute the institutional investor pulls their support, the whole thing collapses. And that's what we don't have here. Going back to the point when you say wealth management is mostly focusing on retail. Institutional investors are not there - and when we talk about institutional investors: how many pension funds do we have in this area? We only have sovereign pension funds. We don't have local basic pension funds, we don't have pension funds for the military or pension funds for the navy or pension funds for teachers. Actually there were some attempts at the very beginning but they all disappeared once the state pension fund came in.

Ayman: One important player are governments – they need to take ownership of this and come up with pension products – particularly for expats. Many expats are here and saving - basically without any provision.

IFN: But surely the problem with that, with the absence of pension fund participation in the Islamic market is the lack of rated paper in which they can invest?

Issam: And the problem also is the size – very small.

Ayman: Sure – but putting the size aside, the product is not there. I know a company that is looking into this, and we are helping them – it is a Western company developing a product for distribution in the capital market. Much of this know-how is actually coming from Western players – especially those who boutique one. Not the big investment banks – their composition changes all the time, their exposure to the Middle East changes, whether they even like Islamic banking or not is subject to change! So you need those boutique players, who can come in and cover that human resource deficit that we have. And definitely the insurance industry is one area where this is needed. These are the kind of products you need – and we need that kind of thinking and that kind of structure.

Issam: Yes, and the insurance and the Takaful companies also invest according to policy regulations! So you need to change the policies in order to promote this side of the business.

IFN: As someone who has been fundraising recently, Giorgio, what kind of investors have you been attracting?

Giorgio: Well we manage a global Sukuk fund – and as we run a cross-border strategy, we invest with no geographic restrictions. I think that is a key differentiating factor, as opposed to the common Sukuk funds which are very much focused on one jurisdiction. We have been marketing our fund mostly into Europe, and mostly towards conventional money – conventional investors. In nine monthsmonths we raised US$75 million, which is very surprising, given that we are not ourselves an Islamic asset management platform. We started up this business out of Istanbul because the Turkish government has been very involved in promoting the wealth and asset management business there, and I have to say that when we are talking to investors generally I do see their interest in investing in a diversified pool of assets where they are not only taking exposure to a specific issuer or type of Sukuk or geography, but in the possibility of gaining the advantage of diversification that means local relations and reduced risk. When we talk to certain investors it becomes very obvious, the question of OK: what can I do now more, in terms or risk – or less, in terms of risk. And looking at the products that are available – whether in-house or outside, there are very few out there. So for me, it is just a matter of this market widening and deepening to provide this. A single investment in a global Sukuk fund doesn't mean anything. It can be the best investment for that specific asset class, but it doesn't respond to a need. As a matter of fact the people who invest in Sukuk – they are banks, buy-to-hold strategies, they buy Sukuk to keep them on their balance sheet and God knows whether you as a professional investor will ever be able to invest in them again on the secondary market. Although in the last 18 months I must say that I have seen the market becoming a little bit more liquid, so perhaps that will play to our advantage.

> ***"We really need a better understanding of the private banks particularly in temrs of their views of the Islamic market and the opportunity it represents. This trigger a discussion on whether such banks would be willing"***

Moinuddin: One of the key industries that hitherto has not been developed due to the absence of proper regulation, is estate planning for Muslim expats. If you look at the GCC, the DFSA have establish the trust law and estate planning is now allowed – but if my assets are held locally and I were to pass on, these would go to the Shariah court and even though the Shariah allows Muslims to write a will, the local court insists on the strict Shariah allocation. What that means is that if my children are in school here, my family is living here- the court doesn't even allow for the running expenses of the household while the matter is in court – and that can take up to a year, 18 months. Why? Because the Shariah courts require all of my relatives, from everywhere, to come and testify that they don't have any claim on my assets, before my family can touch the wealth left behind – not even take funds to sustain their existing life style, which I used to provide. The suffering of family in this manner, is this Shariah compliant? Obviously not. But then why don't we amend these laws through "ijtihad" i.e., ruling of Shariah bodies based on current circumstance.

This is one of those cases where we desperately need the

right regulations to allow Muslim expats to do their own estate planning under local law. This is where we need wealth managers and financial advisors as well, who can assist people to do effective estate planning. Develop an effective trust law, and new products will emerge, new providers will emerge. And this could give birth to a whole new wealth industry here. As foreign expats in the UAE, we own property here, we own assets here. We have accumulated wealth over 10-20 years, and we tend to spend it here. There is a big market potential which is being overlooked.

Ayman: That's important for Dubai. In fact, the Gulf in general. This is a big issue - and without fixing this, we are missing a key factor.

Moinuddin: It is a structural issue, and if we can fix this everything will fall into place. Fix them and it will give you the scale and then you can invest in other areas and it all builds from there.

IFN: Keeping an eye on the time, we are coming to the end of the sessions and we have covered a lot of ground - so perhaps let's just go round the table and conclude with each of your opinions on what is needed to take Islamic wealth management to the next level.

Issam: I would go back to regulations. Regulations that would first, help facilitate the development of the industry; second, provide more transparency; and third, that would provide the instruments and the tools that will give flexibility for the investors to invest in terms of different asset classes, different geographies and so on. I don't think this industry is regulated per se, its part of investment banking rather than having its own niche – it needs some special attention.

Moinuddin: I would focus more on the basic building blocks, and regulations are part of that. I think if you were to assess the market you would find that as we have discussed, one of the single biggest things that needs to happen is estate planning for Muslim expats. Non-Muslim expats are allowed to exercise their own wills but Muslim expats cannot. If you allow them to have this estate planning and have their wills recognized within the local law then resources will come, companies will come, products will come, everything will follow - because there is a huge market that is currently unserved.

Ayman: I think there are two areas. First, we need to look at how we can develop the corporate Sukuk market, the way Malaysia has done – whether local currency or dollar-denominated. There have been a few small Sukuk but we have not seen enough of these. It can't just be the banks and GREs.

And secondly, we really need a better understanding of the private banks particularly in temrs of their views of the Islamic market and the opportunity it represents. This trigger a discussion on whether such banks would be willing to share that know-how. Because I feel that this is a very important piece of information, that currently is not available to us. The knowledge they have, the calls they get – is there really genuine interest? There are a couple of banks that are looking at it now – more so than I have seen in the past 10 years. If they start setting up Islamic units or even teams (or even informal groups of interested bankers), and bringing in this knowledge and expertise then that will be a key driver. And finally we also need product development, because you don't just want to Islamize a conventional product, it needs Shariah foundations.

Giorgio: I think that we need to take steps to create a more liquid market. I think that regulation could be introduced to offer incentives for businesses to be set up in the region to provide wealth management services. And I do think that as there is so much money currently being funnelled away from the region, most of the efforts should be focused on setting up Islamic wealth management platforms within the region with the idea of facilitating capital repatriation, with the commercial tool of having new products that are currently not available. I don't think just opening up an office here is going to make much of a difference, as the money is elsewhere. But to facilitate that money to come back, that is a big thing. And in Switzerland right now for example– there is so much stress and effort to comply with international standards and regulations that a lot of money is moving away from these countries – and not necessarily to other offshore platforms. Why could it not come here?

IFN: Excellent, well there is another opportunity to look at. Gentlemen, thank you very much.