Tharman Shanmugaratnam: Building financial bridges between Asia and the Middle East

Luncheon address by Mr Tharman Shanmugaratnam, Minister for Education and Deputy Chairman of the Monetary Authority of Singapore, at the Inaugural Asia-Middle East Dialogue, Singapore, 21 June 2005.

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Your Excellencies

Distinguished Guests

Friends, it is a privilege to address you here today at this important gathering, as we discuss ways to strengthen ties between our two regions, Asia and the Middle East - two regions of the world that not only have immense potential in themselves but have the potential to shape each other's futures for the better. Let me use this opportunity to talk about the bridges we can build in financial services, and how financial flows can help shape this inter-dependence between the Middle East and Asia. I will also touch on what we can do in education together, because it is in education that we build trust and lasting relationships between our peoples.

Financial bridges between Asia and the Middle East - the economic underpinnings

The economic underpinnings for financial flows between our two regions are in many ways obvious. Both the Asia and the Middle East regions are on an upward trajectory of economic growth. The economies of Asia and the Middle East are growing at a trend rate of 7.5% and 5% respectively. To put this in historical perspective - no region of the world saw sustained growth exceeding 5% for any period before the middle of the last century, except for Australia and New Zealand in the 19th century.

No one expects growth to be linear or to continue unbroken, in either Asia or the Middle East. There will be bumps along the journey, sometimes flash floods, and sometimes a cave-in. But the basic trajectory is upward. The growth story that we are seeing is not an aberration, or a flash in the pan before growth in Asia or the Middle East recedes to the very modest norms that were seen for much of economic history before World War II.

Growth is being propelled by fundamentals. First, both our regions have an abundance of <u>natural resources</u>, and are benefiting from the natural interplay between industrialization and demand for natural resources. Asia's industrialization alone is driving an unprecedented global demand for raw materials, energy and other commodities. China and India alone have contributed over 35% of the increase in global oil demand over the last 15 years. Yes, there are huge inefficiencies in energy use, and concerns over the environment, that have to be addressed before long. But the basic interplay between industrialization and natural resources will continue for many years to come.

Further, both our regions are not just opening up to global markets, but developing <u>domestic demand</u> in our own economies. They are diversifying, and growth is becoming more balanced. Asia is reducing its dependence on manufactured exports as the main driver of growth, and Middle East is seeking to reduce its dependence on energy exports. Both regions are strengthening their social, transport and economic infrastructures as they diversify their economies. The examples are all around us, like India and Indonesia's major energy and transport infrastructure plans, Bahrain's Financial Harbour project, and Qatar's Education City.

Finally, the appetite for prosperity is unshakeable among our younger generations. Young people all across our regions can see what economic growth brings, for their families and themselves, and for their communities. Whether their quest is for material or spiritual fulfilment, young people know instinctively that economic growth and better jobs will help them fulfil their needs. They want to move ahead, to educate themselves, and to give whole communities pride in what they can achieve - in science, in business and in culture. These <u>aspirations of our young</u> are probably the biggest positive for our regions. They will also bring us together over the long haul.

High savings will be increasingly intermediated within Asia and the Middle East

On the financial side of things, the fundamentals are also solid in both our regions. First, the supply of savings in Asia and the Middle East is higher than in any other region of the world. Savings rates in Asia are expected to remain in the region of 35-40% of GDP for some years to come. Likewise savings in the Middle East have been rising over the past decade and are expected to average about 32% of GDP in coming years. (In 2004, the current account surpluses as percentage of GDP for Asia and the Middle East were about 6% and 14% respectively.) With Asian official foreign currency reserves exceeding US$ 2 trillion, and Middle East oil revenues topping US$ 180 billion in 2004 alone, the management of surplus savings and reserves in both regions will offer large business opportunities. It will also offer scope for sharing of experience between government investment agencies and central banks in both regions.

Besides official savings, there is also a growing number of wealthy individuals in the two regions. Asia alone now has an estimated 2.3 million high net worth individuals (HNWI; people with at least US$ 1 million in financial assets), not far behind the US with 2.7 million and Europe with 2.6 million. Asian HNWIs control an estimated US$ 7.2 trillion in financial assets. The size of this group in Asia is growing at 7% per year, second only to the Middle Eastern HNWI, now 300,000 which is growing at 9% per year. Traditionally, Asian and Middle Eastern investors have looked to the developed, Western markets to meet their investment needs. But increasingly, they are looking to diversifying their assets globally. It is a interesting new story, that is only beginning to unfold in Asian markets.

This is not just a post-9/11 story. Increasingly, wealthy investors the world over are looking to spread the risks and enhance the overall returns on their investment portfolios. We are seeing this search for diversification and improved returns on investment amongst sophisticated investors from the Middle East and Asia. It provides an opportunity for markets in Asia and the Middle East which can offer wealthy investors with higher expected returns at acceptable risk.

The demand side of the financial equation in our two regions is equally compelling. First, there are unprecedented demand for funds to finance infrastructure projects, across the region. In Southeast Asia alone, about US$ 461 billion is expected to be spent over the next 15 years to upgrade infrastructure. This is not even looking at China and India. Likewise in the Middle East - the reconstruction of Iraq and Qatar's infrastructural plans are each expected to cost US$ 100 billion.

Second, besides infrastructure finance, we are seeing huge growth potential in the consumer finance sector in our two regions. It is driven by a rapidly expanding middle-class, who want better housing, cars and other big-ticket items like middle classes anywhere else in the world. For instance, India's "consuming class" will rise from the current 30% of households to 40% by 2010. Similarly in China, the "middle class" is set to double over the next 5 years.

Facilitating greater financial flows between Asia and Middle East

Financial services are therefore growing rapidly in Asia and the Middle East. And there is scope for greater deployment of our savings within our two regions, as investors in both regions look for improved returns.

We are seeing the beginnings of a fruitful and meaningful relationship in financial sector cooperation. There is much scope for regional financial centres like Singapore and Kuala Lumpur to provide a gateway for fund flows between the Middle East and Asia. Singapore can by no means be a complete financial centre for the Middle East. That role will be played by financial centres in the Middle East. But we can and will complement and work in partnership with financial centres in the Middle East, and other Asian centres like KL. We can provide a gateway to take Middle Eastern investors into Southeast Asia and China, and to take investors from the region into the Middle East.

What can we do to facilitate and spur on these financial ties and build sturdy bridges? Allow me to make three observations. First, the wealth management industry can play a pro-active role in helping investors to diversify their portfolios by introducing them to opportunities in Asia and the Middle East. In so doing, we will also help Asian and Middle Eastern capital markets grow and become deeper and more liquid. We are already seeing asset managers based in Singapore receiving investment mandates from investment agencies in the Middle East. And Singapore's CapitaLand and the Middle Eastern-owned Arcapital Bank have recently set up a property fund aimed at investing in Japanese real estate, with a target asset size of US$ 300 million.

Second, similarly for the banking sector. I expect to see more Middle East banks and financial institutions set up in Singapore and Asia going forward, and a counter-flow into the Middle East over time. Some Middle East banks are already planning to scale up their presence in Singapore to service Middle Eastern entities interested to operate in Asia, as well as to help Asian corporates to operate in the Middle East. There are similar plans by Singapore-based financial institutions to step up their profile in the Middle East as they seek to tap into Middle Eastern financial flows. Such plans may give added impetus as Singapore concludes FTAs with more Middle Eastern countries, including those which are currently ongoing with Qatar and Kuwait.

Third, Islamic finance is an area that shows considerable promise globally. We know the size of the market - around US$ 200 to US$ 300 billion globally, and growing at about 15% per annum. Efforts are being made in Asian markets, to grow Islamic financial services. For example, Malaysia has been awarding Islamic banking licences to foreign players and encouraging the subsidiarisation of Islamic banking windows. It aims to have 20% of total banking assets to be Islamic by 2010. Singapore, as an international financial centre, is also keen to offer Islamic financial services. We must, as part of the comprehensive suite of financial services that we offer to global investors and borrowers.

Shariah-compliant financial instruments allow issuers to tap a new source of funds and liquidity. But the development of an Islamic financial services market does not just serve indigenous Muslim populations. Malaysia, for instance, has successfully launched global sukuk, or Islamic bonds, to tap liquidity from investors in both Asia and the Middle East. Other issuers of global sukuks have also stopped by Singapore on their road shows to tap Singapore's investor pool. It may not be too long before we have a Singapore corporate issuing a sukuk to raise funds from global investors.

We are also seeing already private fund managers in Asia and the Middle East working together. Recently, for instance, ARA Asset Management based in Singapore had worked in partnership with Dubai Islamic Bank to launch a US$ 450 million Islamic Far Eastern Real Estate Fund with underlying assets located in Asia.

Fourth and finally, we can do more to foster people-to-people interaction in the financial sector. For instance, Asian central banks including the Monetary Authority of Singapore have participated actively in Middle East finance and central banking seminars to share our perspectives on issues of mutual interest. Tomorrow there will be a seminar organised jointly by the Islamic Financial Services Board and Islamic Development Bank tomorrow in Kuala Lumpur on developing a 10-year master plan for the Islamic financial services industry globally. In Singapore, the MAS conducts courses in banking supervision and capital markets which we have extended invitations to both our Asian and Middle Eastern counterparts to participate in. We must think of many other platforms and vehicles which could facilitate people-to-people interactions, including those involving think-tanks, universities, training institutes, and private sector financial bodies like the Association of Banks for example.

There is also a financial stability dimension to these networks. As cross-border financial transactions increase, effective supervision will require countries to foster greater cooperation with their regulatory counterparts. The Monetary Authority of Singapore, for example, is in discussions to conclude MOUs with the UAE's Emirates Securities and Commodities Authority and Qatar's Financial Centre Regulatory Authority to provide for training and supervisory cooperation.

I have highlighted earlier that investment agencies in our two regions are now managing sizeable foreign reserves. There is much scope for our investment agencies to touch base with each other, exchange knowledge of global markets, share the latest in reserve management techniques, and help each other navigate in one another's regional hinterlands where appropriate. We could even co-invest in specific investment opportunities when they arise.

Building educational bridges

Finally, a few remarks on education, and how we can bring our young people together. We all know how much education matters, for all our societies. It is the bedrock for human development, and the means for whole societies to realise their potential.

But there is further significance in education as we address the issue of strengthening ties between Asia and the Middle East. Our long historical ties, going back to the 2nd century B.C., are an asset. Singapore's Arab lineages run through our veins. But to build bridges between our peoples in the 21st century, we have to not only look back to our historical ties and roots, or rekindle and reinvigorate our ties in trade. We have to work with our young. Our young today grow up knowing very little of each other. We have to give them opportunities to meet, to find resonance in each other, and to strike up friendships. If we do this when our people are young, we build up trust for the future. And trust is what makes economic and business relationships last.

Singapore, Kuala Lumpur and other Asian cities can play a growing role in this regard. For some years now, we have been creating what we call a "global schoolhouse" here in Singapore. Today, Singapore has some 66,000 international students pursuing different levels of education. At the university level, we have today some 16 of the best global institutions providing programmes in diverse areas. Top business schools such as INSEAD and University of Chicago have established their own campuses in Singapore.

At our Singapore universities, there is already a small Middle Eastern presence, with 10 undergraduate and 16 postgraduate students from Middle Eastern countries (including Turkey, Jordan and the UAE). For the coming academic year, 31 Iranian graduate students have been offered A*STAR International Graduate Scholarships, to pursue Master's degree studies at NUS and NTU in the areas of Biomedical Sciences, Physical Sciences and Engineering. (The scholars were selected from top Iranian Universities, including Sharif University of Technology, University of Tehran, Shiraz University and Isfahan University of Technology.)

Recently, Al-Azhar University, the Harvard equivalent of Islamic education, announced that it will be helping Singapore develop a centre of Islamic learning. Established in 988 AD, Al-Azhar is the oldest operating university in the world. It is collaborating with the Islamic Religious Council of Singapore (MUIS) to run programmes that are likely to range from introductory to post-graduate courses in Islamic studies.

We can bring students together not just for formal degree courses, but for summer schools. Middle Eastern families can come to Singapore for holidays and health services, while the young go to school. Middle Eastern youth will find Singapore a friendly, multicultural and multi-religious city. They will find an English language environment and educational programmes that combine the best of East and West. They will find friends from Singapore, Southeast Asia, China and India.

A further area of potential collaboration is in teacher training and education research. For example, the National Institute of Education has been appointed by the Abu Dhabi Educational Zone in the UAE to advise on the setting up of a teacher training institute. We will be able to exchange training materials and officials, as well as collaborate on innovative projects in education.

Each of these initiatives may be small. But they all add to the soft infrastructure and networks that we have to create between Asia and the Middle East, to build enduring economic and business ties.

Conclusion

To conclude, let me just say that the financial centres of both our regions can play an important role in catalysing cross-regional flows of savings, and creating a multiplier effect on Asia and Middle East growth and investment. We must also establish and strengthen people-to-people links, and contribute to each others' efforts to develop financial sector skills and build management capacity. And we must start with our young, bring them together, and help them dispel stereotypes of each other, not just by understanding their differences but finding what they share in common. I suspect they share far more in common than the generations before them.

AMED provides a vehicle to jumpstart this process. I hope that the potential areas of cooperation that I have highlighted will throw up more ideas, for the financial sector panel session later today as well as in the field of education. Thank you.