Sultan Bin Nasser Al-Suwaidi: The regulatory partnerships for sustained growth in the MENASA Area

Speech by H E Sultan Bin Nasser Al-Suwaidi, Governor of the Central Bank of the United Arab Emirates, at the MENASA (Middle East North Africa South Asia) Forum, Dubai, 24 May 2010.

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Good Evening,

Excellencies
Ladies & gentlemen
The distinguished panel speakers

It gives me great pleasure to be with you this evening at this important Forum.

The subject of my speech is: "The regulatory partnerships for sustained growth in the Menasa area".

Under this subject, I will talk about four issues:

First: Implementation of similar banking laws and regulations

Implementation of similar banking laws, using similar banking regulations, and adopting similar processes in banking supervision in the MENASA Area countries, in my opinion, will go a long way in providing banking sectors with a strong basis for building on successes. It will also make regulators realize the importance of regional cooperation and coordination, which hopefully will lead, at one stage in the future, to enabling cross-border branching of banks and other financial institutions.

But is it realistic to imagine that cross-border branching of banks and other financial institutions will be achieved soon?

Another complication is the type of banking institutions that we have in this Area. Most banks are retail commercial ones, and these are operating in the protected zone. I mean here; protected through the growing need to protect interests of national banks. So, the question that comes up; shall the cross-border access of banks be done through a new type of banking institutions? Which the Area is not familiar with yet.

On implementing of similar banking laws and using similar regulations, I will start here from the possible regulatory response to the Global Financial Crisis.

The banking regulatory response that countries in the Area might adopt is a mix between internationally set standards, through decisions of G20 countries and the national requirements, which might cause slight ring-fencing or insulating of national financial systems from direct competition.

The Global Financial Crisis might have already impacted the international cross-border banking business, which might lead to improved regional cooperation and therefore improve doing banking business, region wise.

Trade related transfers outward and inward will continue to move without much hindrance. Foreign exchange deals will also go through, as G20 countries are eager to do more trade to improve their economic conditions. However, there will be some restrictions on investment flows both outward and inward, because risks have been clearly identified in investment transactions. Outward flows will be scrutinized by regulators for type of investment and whether direct or passive. Also complexity of investment products will draw special attention. As for inward investment flows, regulators will put some type of filters to prevent Hot Money, or huge inflows followed by quick outflow of funds.

Banking regulations will probably be amended in the coming few months. I believe, the smaller economy countries will steer their banking system towards lowering the growth rate of loans and advances plus investments versus stable deposits. Investment banking business, on the other hand will be subjected to a great deal of more regulations than in the past.

In summary, I think that the present Global Financial Crisis will impact globalization of financial services, as many restrictions will be put in place in many countries including the G7 countries, which might open a window of opportunity for countries in our region or the wider Area.

Second: Cross-border investment flows

Cross-border investment flows should be welcomed by recipient countries and encouraged by source countries, as many countries in our Area need to set rules to enable the establishment of large projects for the purpose of creating jobs. That will also enhance peace and stability on the national level, which will certainly improve the prospects for the regions in this vast Area. Any help by the World Bank in improving and unifying investment laws in addition to watching their implementation, will go a long way in achieving this important regional objective.

Sovereign Wealth Fund source countries should also be interested in investing in mega projects in the region for three reasons, as follows:

1. The Global Financial Crisis proved that investments through Industrialized Advanced Countries' investment banks are not totally risk free.
2. There is a need within SWF source countries to safe guard flow of food imports at reasonable prices, and the possibility for incorporating companies as direct investment projects in countries in the region is a realistic possibility, when investment laws are enacted and maintained at international standards.
3. SWF source countries should be interested in the maintenance of social order, peace and stability in the regions of this Area.

Another reason that makes me think that SWFs from our region might change the flow of their direct investments, is that once we see the proposed Regulations re Sovereign Wealth Funds in the Industrialized Advanced Economies start being implemented, when economies in the West start doing well, more questions will be asked and more forms will become necessary to fill and more disclosure and transparency will be demanded. This behavior will signal that there is no strong need for foreign capital in the West, and that the political mood has changed.

Therefore, we might see gradual tightening of the scrutiny on capital flows from SWF countries, at one stage, especially funds that are destined for direct investment in certain companies.

Faced with all this nonsense, SWFs will certainly come to the conclusion that it is time to change strategy. This could make SWFs avoid direct investment in certain companies, or even avoid direct investment in all companies, and become more of passive investment vehicles in the West. As, SWFs have large sums to invest, this might make them direct part of their investments to existing or newly created companies in the region. This situation, if it happens soon, will lead to creating a new regional developmental cycle.

Third: Linking regional payment systems

Linking regional payment systems and using local currencies for settlement of transactions should be a long-term objective for countries in the MENASA Area, as this will improve speed, efficiency and will achieve transaction cost reduction, for the benefit of cross-border trade, investment flows and tourism business.

Achieving this would be a big challenge, because the good old routes, which we all are used to, will have to be abandoned. Also, trust in each other's national currency in addition to trust in the efficiency of national payment systems across regions is another challenge. However, these challenges can be overcome over a period of time, maybe depositing of the settlement amount with the counterpart payment system provider in the recipient country would create the required trust.

To build trust in national payment systems, it will also be necessary for the national regulatory authority to take a leadership role. Payment systems on the national level should be unified into one system, and operate with strict rules for action against mistakes or events of fraud through members.

To achieve some form of common payment system among MENASA Area Countries, it will be necessary to:

1. Identify countries that are ready to be linked, through national payment systems that satisfy certain pre-set standards.
2. Setting-up of a steering committee, consisting of technical staff representing the national payment systems, who would agree to work on a certain strategy aimed at achieving a common payment system, that would use local currencies for settlement, at a future stage.

Forth: Investment in infrastructural projects

Encouraging regional capital flows aimed at investment in infrastructural projects in the MENASA Area Countries should be encouraged through capital markets.

This could be achieved through allowing corporations that are in marine transportation, air transportation, rail road companies, road authorities, storage facility companies and ports/air port authorities to raise money through capital markets in countries of the Area, especially countries that are capital surplus ones.

The Area can draw on the experience of the UAE in this respect, when it allowed its banking system to raise money for Indian companies as early as the eighties of last century. Certain Indian companies were allowed to raise capital against certain commitments and undertakings. This was possible through the high requirements and standards implemented in both India and the UAE at that time.

We believe Indian companies were able to benefit from such funds for a long period of time. Many of such companies are large conglomerates now.

Providing a special window for infrastructural projects will benefit the flow of trade and investments across regions of the Area, and will help to sustain growth of economies.

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With this I come to the end of my speech, but before I close, I would like to thank the organizers of this important forum for inviting me and for the excellent arrangements.

Thank you for your attention.