

Lim Hng Kiang: Towards a new era of growing connectivity between Asia and the Middle East

Opening address by Mr Lim Hng Kiang, Minister for Trade and Industry and Deputy Chairman of the Monetary Authority of Singapore, at the 2nd World Islamic Banking Conference: Asia Summit 2011, Singapore, 8 June 2011.

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Your Excellencies, distinguished guests, ladies and gentlemen,

Introduction

1. I am honoured to be invited to deliver the opening address at the 2nd World Islamic Banking Conference: Asia Summit (WIBC Asia). I would like to extend a warm welcome to our overseas guests, especially our distinguished speakers who will be sharing their insights during this conference.

Growing connectivity between Asia and the Middle East

2. Despite the recent spate of shocks, the world economy has been resilient with growth projected to moderate slightly to 4.5%¹, compared to 5.8% last year. Downside risks such as high energy and commodity prices, the European debt crises, geopolitical tensions in the Middle East and North Africa (MENA) and the Japan tragedy have not substantially derailed the economic momentum.

3. Asia is expected to remain the main locomotive driving economic growth. The International Monetary Fund (IMF) projects Asia's growth to reach almost 7% this year, led mainly by China at 9.6% and India at 8.2%. Asia has been, and will still be the key engine for global trade. In 2009, the region accounted for 35% of world exports, up sharply from 25% a decade earlier². Within Asia, the ASEAN-5 (Association of Southeast Asian Nations-5) countries³ are expected to expand by 5 to 6% this year and their external trade volume will reach around 60% that of China. ASEAN, which is a two-trillion-dollar economic grouping, is the fifth largest in the world in terms of purchasing power parity. ASEAN countries have been working steadily together towards greater economic integration and have committed to build the ASEAN Economic Community, a single market and production base, by 2015.

4. In 2010, MENA as a whole grew 3.8%, led principally by the Gulf Cooperation Council (GCC) economies. Considering the uncertainty in parts of MENA, the IMF nevertheless still expects the GCC to grow by 7.8% this year, driven by the robust expansion of oil production and strong public spending. The medium-term outlook remains good as countries in the region lay the foundation for sustainable and diversified growth.

5. Asia will become increasingly important for the GCC as the patterns of trade, investment and consumption shift from the West to the East. To reap greater benefits from these highly dynamic and fast-expanding regions, we should press on towards the goal of growing connectivity and deepening economic cooperation between our two regions. We

¹ Sources: Monetary Authority of Singapore, Consensus Economics Inc, weighted by shares in Singapore's NODX.

² IMF, Regional Economic Outlook: Asia and Pacific, April 2011.

³ ASEAN-5 comprises Indonesia, Malaysia, Thailand, Philippines and Singapore.

need to create stronger linkages in the vital areas of trade and investment, business as well as financial linkages. There are several ways to achieve this:

6. Firstly, the Asian Development Bank (ADB) has identified growing South-South economic linkages via trade and investment as a potential driver of global growth and emphasized the need for policymakers to further reduce barriers to trade and investment⁴. Trade between Asia, Middle East, Africa and Latin America has developed over the past two decades but still remains a relatively small 17% proportion of world trade. Asia's share of total trade with the GCC grew from just 10% in 1980 to 36% in 2009⁵. Having identified this as a priority area, ASEAN and GCC foreign ministers met in Singapore last year and agreed upon a Plan of Action to boost cooperation in trade and investment, among other areas. Islamic finance can potentially play a part in facilitating more trade between Asia and the Middle East with the involvement of more global and Islamic banks from both regions.

7. Secondly, the high level of savings and wealth accumulation in the GCC and Asia should also be mobilized by the financial sector and channeled towards more productive economic uses in both regions, especially to meet the demand for national infrastructure such as power plants, hospitals, roads and rail networks. The ADB Institute estimated that Asia will need US\$8.2 trillion in infrastructure investment between 2010 and 2020. Seeing the large gap between the demand and supply of infrastructure investment, the ADB and Islamic Development Bank (IDB) have jointly set up a US\$500m Islamic Infrastructure Fund in 2009. Several ASEAN countries such as Malaysia and Indonesia have also outlined plans to tap global Islamic funding for their infrastructure projects.

8. Thirdly, given the many ambitious initiatives and plans in the GCC for new industrial developments and infrastructure projects, the Middle East remains a high-potential market for Asian companies. ASEAN-based companies should therefore invest more time and resources to evaluate these opportunities and assess the risks, so as to help fill this demand. In Singapore, International Enterprise Singapore and the Singapore Business Federation (SBF) have been playing a vital role in helping our local companies to understand and differentiate Middle East markets better and to expand their regional footprint.

9. Lastly, many leading Middle East financial institutions have established a presence in Singapore to offer financial services such as wholesale banking, treasury services, trade finance, and wealth management. These institutions play an important bridging role by guiding companies in the region to expand into the Middle East and vice versa. Bank Muscat, the largest bank in Oman, is the latest player to set up in Singapore.

Sustaining the growth of Islamic finance

10. As investors and businesses in the Middle East and Asia seek a wider range and diversity of financing options from banks and capital markets, Islamic finance will have to respond to meet their rising needs. National and industry players have to work closely together to address the many challenges faced by Islamic finance as it internationalizes into new markets. This morning, let me touch on just three issues, which I am sure you will be discussing in greater depth during the course of the conference.

11. First, there is a fundamental need for further standardization and harmonization of both regulatory and Shariah standards across the Middle East and Asia. The greater use of standardized legal documentation will increase efficiency, certainty, transparency and liquidity. This would allow for easier cross-border offering of financial products that would reach a wider investor base and thereby bring about greater economies of scale and reduce transaction costs. Standardisation will also enable better risk management by ensuring that risks are clearly identified and appropriately mitigated between financial institutions and their

⁴ Asian Development Bank, Asian Development Outlook 2011 (April 2011).

⁵ Economist Intelligence Unit, "GCC trade and investment flows: The emerging-market surge", 2011.

counterparties. Shariah scholars and multilateral agencies such as the IDB, Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI) and Islamic Financial Services Board (IFSB) are already working to address these critical issues. As a member of the IFSB, the Monetary Authority of Singapore (MAS) will work with them in their efforts to allow greater access to an even larger global community, including non-Muslim countries.

12. Second, we need to ensure that the legal and regulatory regimes remain robust in ensuring the safety and soundness of markets and institutions, and yet conducive for Islamic finance to grow at a sustainable rate. Some progress has been made on this front with the IFSB issuing new regulatory standards that serve as useful reference points for supervisors. However, as the global financial reforms take shape, all financial institutions including Islamic institutions will have to rethink the assumptions underlying their business strategies and reassess their business models in light of the structural shift. They will have to retool their organizations so as to remain competitive and to serve their customers better.

13. Third, the industry's need for more manpower will be an important issue, given the lead time needed to develop new competencies. As Islamic finance becomes more widely accepted and more financial institutions begin to offer a greater variety of Islamic products, the demand for financial, accounting and legal professionals who are conversant with Islamic finance will rise. In this regard, institutes of higher learning, such as the Singapore Management University's International Islamic Law and Finance Centre, and quality training providers can play a vital role to increase the knowledge of Islamic finance, and develop new capabilities and products through industry-relevant research.

Singapore's role

14. I will now briefly touch on Singapore's role in growing connectivity in the global arena. Singapore already enjoys excellent and long-standing relations with the GCC. We have entered into investment guarantee agreements with Bahrain, Oman and Saudi Arabia and concluded the GCC-Singapore Free Trade Agreement in Doha in 2008 – the first such agreement signed by the GCC. We will do more to broaden our ties with the Middle East.

15. We have identified three areas where Singapore can offer its services as a financial centre to support the growth of Islamic finance – namely in wholesale banking services, asset management and capital markets. The MAS has facilitated the development of Islamic finance in Singapore's financial markets. Last year, we saw several sizeable cross-border transactions, including the world's first Shariah-compliant data centre fund (Securus Data Property Fund), the listing of the world's largest Islamic Real Estate Investment Trust (Sabana Shariah-Compliant REIT) on the Singapore Exchange, as well as Khazanah Nasional's landmark S\$1.5b Sukuk deal – the largest Singapore Dollar Sukuk to date.

16. However, we need to continue working together with our key stakeholders to raise the level of awareness and understanding of Islamic finance, and to enhance the conduciveness of our business environment. I am glad that the SBF and industry players such as The Islamic Bank of Asia, CIMB Islamic, OCBC Bank and Allen & Gledhill have undertaken to organize business seminars to educate our local companies.

17. To provide greater tax clarity and certainty to the industry, I am pleased to announce today that Singapore will issue new income tax regulations for Islamic finance. The Ministry of Finance will provide additional clarification and detailed explanation of the income tax treatment on more prescribed Islamic financing arrangements including financing through a partnership arrangement, project finance as well as interbank placement of funds⁶. This is in

⁶ The tax circular will cover Islamic financing arrangements based on Diminishing Musharaka (financing through a partnership arrangement) and Istisna (project financing) and interbank placement based on Wakala (agency contract) and Murabaha (sale at cost-plus) concepts.

keeping with our long-standing principle that Shariah-compliant products should not be disadvantaged in terms of regulatory and tax treatment where the economic substance and risks are similar to conventional products. We hope that this will expedite the development of more such financial products in Singapore.

Conclusion

18. To sum up, the Middle East and Asia continue to present attractive opportunities. Both regions need to work closer together to achieve greater synergy and accelerate the global growth of Islamic finance. Singapore will play its part in this international effort together with our regional and industry partners.

19. I am glad to see more players from Middle East and Asia participating in this year's Summit. I hope that you will take up the challenge to work together to spur the development of Islamic finance as a bridge between Asia and the Middle East. Thank you.