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# ARAB Banker

The Global Magazine of the Arab Bankers Association (ABA)

Arab Bankers Association
جمعية المصرفيين العرب

**BANK ABC** BUILDING AN INTERNATIONAL BANKING POWERHOUSE IN THE MIDDLE EAST

**SAUDI ARABIA'S** VISION 2030

**EXECUTIVE SEARCH** IN THE MIDDLE EAST

**ALGERIAN BANKS** SEARCH FOR A NEW BUSINESS MODEL

SME BANKING IN EGYPT

US LAW ENFORCEMENT AND ARAB BANKS

CRUDE OIL AND THE GLOBAL ENERGY MIX

Volume XXVII, Autumn 2016

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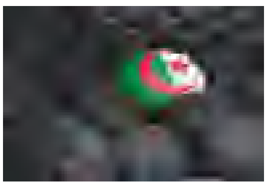

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ARAB Banker

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# Arab banks face new challenges, but also see new opportunities

Arab banks survived unscathed the greatest financial crisis the world has seen in many generations, and they have been successfully navigating the worst political turbulence that the Middle East has witnessed for many decades, but Arab banks are now facing a set of new challenges that will test the skills of their managers in the years to come.

First, there are the negative consequences of the exceptional drop in the price of oil in the economies in which Arab banks operate. There will be challenges as to their liquidity. There will also be a heightened level of risk in their credit portfolios.

However, this challenge also brings opportunities. Arab banks will have to meet the task of funding governments that have hitherto operated budget surpluses. This will create new business opportunities which will help to enhance professional skills, and will drive local financial markets to greater levels of sophistication.

Second, there are dangerous complications arising from sanctions' compliance. For Arab banks this issue is made all the more sensitive by the complex and highly charged political environment in which they operate. The dangers of even the slightest mishap are evident. Managers have to be exceptionally risk averse in this area and then cope with the difficulties that such an approach entails.

Third, there are increasing and ever more complicated regulatory pressures. Arab banks are leaders when it comes to meeting, if not exceeding, regulatory requirements and combating financial crime. However, regulation can be excessive. Witness for example the situation in the City of London where Arab banks have their biggest external presence, and where they have had, for the most part, an exemplary record. Here, Arab banks are simply looking for proportionality to be the regulators' guiding principle. This is understandable given Arab banks' size, the nature of the business they undertake, and the evident fact that they present no systemic risk.

Samba Financial Group, one of the biggest banks in Saudi Arabia and the Middle East, took a decision on 8th June 2016 to close its London branch. Its board cited concerns over long term profitability as the reason for its closure. The regulatory pressures, and their impact on the cost of doing business, and their distraction to management away from business development activities cannot be ignored as factors in that decision. UK banking authorities should consider what needs to be done to ensure that London remains an attractive and profitable city in which Arab banks can do business.

Fourth, de-risking presents a threat to many banks around the world, but it is particularly harmful to Arab banks. The origins of this threat are political, regulatory and economic in nature. Some Arab banks are responding effectively to this danger by employing a multidisciplinary approach. The response is a combined effort by compliance and risk management, and the active and businesslike management of correspondent banking relationships. This approach has proven to be successful.

It is no wonder that with this unfavourable environment Arab banks have reverted to housekeeping as a strategic focus. They are now concentrating on building up their risk management and compliance functions, in addition to skills in other areas. Expansion plans have generally been put 'on hold'. Attention is being paid to the increasing costs that are arising from the issues mentioned above.

'Brexit' is a political development that carries no risk to the Arab banking community in London. Banks that have established branches in London have already established branches in other European cities if they saw the need to do so. As for those banks that operate in continental Europe through London-based subsidiaries, there may be a period of uncertainty as questions of 'passporting' are resolved, but it is inconceivable that European regulators will try to push away branches of foreign banks – quite the reverse, they are more likely to try to attract them.

I have no doubt that, either inside or outside the EU, London will remain the most important centre of Arab business, banking, culture and entertainment outside the Arab world.

We at the Arab Bankers Association believe strongly that Arab banks are well managed, their regulators are highly proficient, and their governments very supportive. We believe, therefore, that they will cope, and cope well, with the challenges being thrown at them. Many of them will remain the safest in the world.

The Arab Bankers Association continues to do its best to support the Arab banking community. Our seminars and other events are dedicated principally to discussing the changing nature of the banking landscape and offering analysis and understanding of threatening trends. We also hope that, at least in some cases, we are providing answers.

**George Kanaan**
**Chief Executive Officer**
**Arab Bankers Association**

# Broad coverage of Arab banking, with detailed insight from industry experts

I am delighted to be able to present the fourth edition of the new *Arab Banker* magazine, which again has been published on schedule at the end of September and without placing any financial burden on its parent, the Arab Bankers Association.

This edition of *Arab Banker* has the strongest editorial content of any of the four editions that we have published since re-launching the magazine in September 2013.

Our main feature is on Bank ABC, a flagship of Arab banking for more than 35 years. On pages 12–15, Khaled Kawan, the Group CEO and Saddek Omar El Kaber, its Chairman, describe the repositioning and rebranding of the bank, and the recent upgrades to its operating units. On pages 18–20, Michel Accad, the CEO of Al Ahli Bank of Kuwait explains the rationale for his bank's recent acquisition in Egypt, and also the rationale behind Ahli's 'Simpler Banking' strategy. On pages 25–26, Fahad Al Khalifa, the Group CEO of one of Qatar's youngest banks, al khaliji, explains how aligning his bank's business strategy with Qatar's long-term economic vision makes good business sense for both shareholders and customers.

In April, Saudi Arabia launched its Vision 2030, an ambitious plan to transform the Kingdom both economically and socially. On pages 22–24, Hasan AlJabri, the CEO of Sedco Capital, one of Saudi Arabia's leading asset managers, tells us what Vision 2030, and other recent policy initiatives, is going to mean for local and foreign investors in Saudi Arabia.

As *Arab Banker* was going to press, details were being finalised for the merger between National Bank of Abu Dhabi and First Gulf Bank. The merged bank, which will retain the National Bank of Abu Dhabi name and branding, will be the biggest in the Middle East. On pages 28–29, Samer Hijazi, a partner with Grant Thornton who heads his firm's operations in Abu Dhabi, gives his views on the merger and looks ahead to other possible corporate restructurings in Abu Dhabi that might follow.

Looking beyond the GCC, we have coverage of Libya, Algeria, Egypt and Lebanon.

Saddek El Kaber combines his role as Chairman of Bank ABC with the Governorship of the Central Bank of Libya. On pages 16–17, he describes his work at the Central Bank, and his hopes for the future of the Libyan banking system. On pages 34–36, Rachid Sekak, the former CEO of HSBC's branch in Algeria, considers the challenges that Algerian banks are facing as a result of low oil prices, and on pages 38–39 Rashwan Hammady describes the SME finance market in Egypt, with particular reference to the steps that his bank, Commercial International Bank, is taking to expand its market share.

Dr. Amine Awad enjoyed a distinguished career at Lebanon's Banking Control Commission before taking up his current position as an advisor to BLOM Bank on governance, risk management and compliance. On pages 42–43, he explains the steps that BLOM is taking to further strengthen its internal controls, and draws on his experience to give some advice to banks that are following in the same path.

The interview with Dr. Awad is followed, on pages 44–45, by an article from Pillsbury Law about recent actions by the US Department of Justice against Swiss banks and the likely next steps that the DOJ could take against Middle Eastern banks. On pages 46–47, we consider the factors that are driving large international banks to reduce their correspondent banking relationships with emerging market banks and we review recent guidance from international standard setters on due diligence practices that banks should follow if they hope to satisfy the increasingly stringent requirements of regulators.

Our coverage of Middle East finance also includes an interview with Bert de Ruiter, of Stormbridge International, about the recruitment market for bankers in the Middle East (pages 30–31), a review of recent changes to credit ratings on Middle East governments (pages 40–41 – there have been some significant downgrades in the last year), and a listing of the largest GCC banks, ranked by equity (pages 32–33).

We have our regular features on the global energy market and on the political scene. This year, Dr. Carole Nakhlé of Crystol Energy describes how global energy markets are changing and how this will affect the role of oil and gas over the long term. Anthony Harris, a former British ambassador and long-standing resident of Dubai, gives us a historical perspective on current political issues in the Middle East and finds some reasons to be optimistic about the future.

Looking beyond the Middle East, we have features on the men who are leading Chinese banks, on the London real estate market, and on platinum as an investment asset class. We also have our regular cultural features at the back of the magazine.

I would again like to thank George Kanaan, the Chief Executive of the Arab Bankers Association, for his support in getting this magazine published. Thanks also go to Martin Cox of JPS Print Consultants for his excellent design and layout of the magazine, and to Jason Smith of JPS, who printed it.

**Andrew Cunningham**
**Editor in Chief**

## Ahli United Bank celebrates 50 years of banking in the United Kingdom

Ahli United Bank (UK) celebrated 50 years of continuous presence in the United Kingdom with a star-studded reception in London's Millenium Hotel, Grosvenor Square on 3 June.

Speaking at the celebration, Ahli United's Chairman, Mr. Hamad Al-Humaidhi said, "AUB UK, our London subsidiary, has the distinction of being the oldest established bank from the Gulf and MENA region to continuously operate in the UK market." He added that, "AUB UK has gained a second distinction of always trading profitably, except for one year, 1998, whose losses were immediately recovered the following year. This is a track record which most larger UK and international institutions would greatly envy over the same period."

L–R: Mr. Hamad Al-Humaidhi, the Chairman of Ahli United Bank and HE Khaled Al-Duwaisan, the Kuwaiti Ambassador to the United Kingdom

Ahli United Bank is a pan-regional banking group with operations in seven Middle Eastern countries – Bahrain, Kuwait, Oman, the UAE, Egypt, Iraq and Libya – as well as in the UK. The bank is one of the biggest in the GCC, with assets at the end of 2015 of $34 billion. Its Group Chief Executive Officer and Managing Director is Adel El-Labban. The Chief Executive Officer of AUB UK is James Forster.

United Bank of Kuwait (UKB) was founded by Kuwaiti shareholders as a London-based consortium bank in 1966 and in 2000 merged with Bahrain's Ahli United Bank to form Ahli United Bank Group. UBK was renamed as AUB UK.

## Saudi Arabia appoints HSBC's Tuwaijri as Deputy Minister for Economy and Planning

HSBC's Chief Executive Officer for the Middle East and North Africa, **Mohammed al-Tuwaijri**, was appointed Saudi Arabia's Deputy Minister for Economy and Planning in May. The Minister for Economy and Planning is Mr. Adel Fakeih.

Tuwaijri's appointment was part of a series of changes to government economic portfolios in May. Other changes included the appointment of Ahmed al-Kholifey to replace Fahad al-Mubarak as Governor of the Saudi Arabian Monetary Agency, and the appointment of Mr. Khalid al-Falih to lead a newly-expanded Ministry of Energy, Industry and Mineral Wealth, replacing Mr. Ali Naimi, the long-standing Minister of Oil.

Mr. Tuwaijri had been CEO of HSBC's MENA operations since 2013 after re-joining HSBC in 2010. He had previously led JP Morgan Chase's operations in Saudi Arabia. Mr. Tuwaijri began his career as a pilot in the Saudi air force.

HSBC announced that **Robin Jones** would take over as interim CEO for the Middle East. He had previously been Mr. Tuwaijri's deputy.

## New Chief Executive for BLME

BLME, the London-based Islamic bank, appointed **Jabra Ghandour** as its Chief Executive with effect from 25 March. He replaced Michael Williams, who had been appointed interim CEO in May 2015, following the departure of Humphrey Percy. Mr. Williams has returned to his role as a non-executive director of the bank, a position that he held prior to his appointment as interim CEO.

Mr. Ghandour joined BLME from International Bank of Qatar where he was Managing Director. Prior to that, he had held a variety of senior positions with National Bank of Kuwait, including General Manager, Jordan, and Head of Private Banking.

BLME was licensed in 2007 and is the largest Shari'ah-compliant bank in Europe. Its biggest shareholder is Kuwait's Boubyan Bank with 19.94%. National Bank of Kuwait is the majority shareholder in Boubyan Bank.

Omar Bouhadiba replaced Jabra Ghandour as Managing Director of International Bank of Qatar in November 2015.

## QIB (UK) to appoint new CEO

As *Arab Banker* was going to press, QIB (UK), the London subsidiary of Qatar Islamic Bank, was seeking regulatory approval to appoint the person it had chosen to succeed Bert de Ruiter, who had led the bank for two years from March 2014 until early 2016.

Guy Priestly, the Deputy CEO, has been holding the position of acting CEO in between the departure of de Ruiter and the arrival of the new CEO.

De Ruiter is credited with resolving regulatory issues that had accumulated at QIB UK in recent years and with reaching a satisfactory settlement with the UK regulators.

## Commercial Bank of Qatar appoints new CEO from ANZ Bank

Commercial Bank of Qatar (CBQ) appointed **Joseph Abraham** as its new CEO in July, replacing Suleiman Al-Raisi who will become an advisor to the Board of Directors.

Before joining CBQ, Mr. Abraham worked for Australia and New Zealand Banking Group, based in Jakarta. He had previously held positions in Indonesia, Singapore, Hong Kong, Ghana, the United Kingdom and India.

CBQ is the second largest bank in Qatar, ranked by equity. In addition to its domestic operations, it has a 40% stake in Sharjah's United Arab Bank and a 35% stake in National Bank of Oman. It also has a 71% stake in Abank, a Turkish bank previously known as Alternatifbank.

## Samba Financial Group to close in London

Samba Financial Group announced on 8 June that it would close its branch in London. The Board cited concerns over long-term profitability as the reason for its closure.

Samba first received a branch licence in 1987. Since then, the branch has focused on private banking, serving corporate clients in the UK and in Saudi Arabia, and deploying through its treasury excess liquidity accumulated at head office.

Arab banks in London have become increasingly concerned about the high costs of regulation and compliance in London and some have complained that the amount of time and expense that they have to devote to these issues is disproportionate to their role within the UK banking system and the UK economy.

Commenting on Samba's decision, George Kanaan, the CEO of the Arab Bankers Association, said, "Regulation of Arab banks in London has been relentless and disproportional and it needs to be examined and reviewed before more Arab banks reconsider their positions in London."

## Michel Sawaya is new CEO of Citibank Lebanon

**Michel Sawaya** was appointed Chief Executive Officer of Citibank Lebanon in April, replacing **Elissar Farah**, who had moved to head Citibank's operations in the UAE. Mr. Sawaya had been Head of Corporate Banking for Citibank Lebanon since 2013 and had previously been Head of Treasury and Trade Solutions.

Citibank Lebanon was established in the 1950s and is the bank's oldest franchise in the Middle East. For many years it acted as the bank's regional hub. In 1996, it was re-established as a fully licensed Lebanese branch.

## Round-up of other recent banking appointments

**Deutsche Bank** appointed Jamal al-Kishi as Chief Executive for the Middle East and Africa and Salah Jaidah as its Chairman in the region. Mr. al-Kishi is the CEO of Deutsche Securities Saudi Arabia and will continue to hold this position. Mr. Jaidah will continue as the bank's general manager in Doha and country officer for Qatar.

Jamil El-Jaroudi resigned in July as Chief Executive of **Bank Nizwa**. He had been in the role for four years. He was temporarily replaced by Khalid Al-Kayed, the bank's General Manager for Finance.

**Bank Sohar's** acting General Manager and CEO, Mr. Rashad Al-Musafir, resigned in June and was replaced by Mr. Sasi Kumar. Mr. Musafir had been in his position since October 2014, when he replaced Mohammed Kalmoor.

Bank Sohar has been in discussions with **Bank Dhofar** about a possible merger for almost three years. In July the two banks announced that they had signed a non-binding agreement to merge and that they would be continuing with their due diligence.

In April, Hisham Ramez was appointed Chairman of **Arab International Bank**, the Cairo-based bank that is majority-owned by the Central Bank of Egypt and Libya Foreign Bank. Ramez served as Governor of the Central Bank of Egypt from March 2013 until late 2015, when he was succeeded by Tarek Amer.

**Morgan Stanley** appointed Motaz Alangari as Head of Investment Banking for Saudi Arabia. He joined from Samba Capital.

**ING Bank** has appointed Serge Rahman as its new Head of Wholesale Banking, Dubai, with effect from 1 June 2016, and it has appointed Howard Lambert as Head of Corporate Clients, Dubai, with effect from 1 August.

## ABANA rebrands to reflect wider membership and global reach

The Arab Bankers Association of North America (ABANA) rebranded itself in June and is now known simply by its acronym – ABANA. The full name will no longer be used.

Announcing the change, ABANA's Chairperson, Mona Aboelnaga Kanaan (no relation to the ABA's George Kanaan), noted that ABANA's membership has expanded well beyond a traditional definition of 'Arab banker' and now brings together Arab and non-Arab professionals with activities in North America and the MENA region. In addition to banks and financial institutions, membership includes private equity funds, institutional investors and family offices, as well as law firms, real estate companies and technology professionals.

Alongside the rebranding, ABANA has updated its mission statement. It is now, "To connect, support and inform finance professionals and institutions with interest in the Middle East and North Africa."

ABANA has also revamped its membership options with the aim of providing more targeted benefits to those who live in the New York area and those who do not, including those who are based overseas.

ABANA was founded in 1983 by a group of financial professionals including Hutham Olayan, Issa Baconi, Monir Barakat and Fakhruddin Khalil. At the time, many Arab banks had significant operations in New York.

ABANA's new website is www.abana.co

## Central Bank of Egypt limits tenure of bank CEOs to nine years

The Central Bank of Egypt issued a circular on 23 March 2016 limiting the term of office of bank chief executives/managing directors to nine years. The nine-year limit applies to consecutive years of service and, cumulatively, to terms of service that are not consecutive.

The new rule applies to state-owned banks (whose chief executives are appointed by the Prime Minister), private banks and branches of foreign banks.

Where chief executives/managing directors have already been in office for more than nine years, they may continue until the next General Assembly meeting, subject to agreement from the Central Bank.

Several chief executives/managing directors of Egyptian banks had been in office for more than nine years at the time when the Central Bank circular was issued.

The Central Bank circular noted that staff turnover is one of the most effective ways of developing a banking system, that it incentivises the next generation of managers, and that it ensures that new blood flows through organisations.

# Building an international banking powerhouse in the Middle East

Bank ABC is on a mission: to be the Middle East's leading international bank, strong in wholesale and retail throughout the region and with subsidiaries and branches across its broader network to enable clients to conduct their business efficiently and profitably wherever in the world they may be.

*Arab Banker* spoke to Mr. Saddek Omar El Kaber, the bank's Chairman and to Dr. Khaled Kawan, its Group Chief Executive Officer, about the bank's plans for the future, and the progress that it has already made since it re-branded itself and re-launched its strategy in 2015.

Saddek El Kaber and Khaled Kawan

Bank ABC has been a feature of the Middle Eastern banking scene for more than 35 years. Originally founded as Arab Banking Corporation, it was a flagship of the Bahrain offshore banking market and led the internationalisation of Middle Eastern banking in the 1980s, building businesses in Europe, Asia and the Americas that have stood the test of time.

But no bank can stand still and hope to prosper. Starting in 2014, Bank ABC's board and management initiated a fundamental review of the bank's businesses and market position. The results, coinciding with the 35th anniversary of the bank's foundation, began to be implemented in 2015 with significant strengthening of wholesale operations, a re-branding, and upgrades to internal operations.

"The business environment in the Gulf States, and elsewhere in the Middle East, is changing and the needs of our customers are changing too. We have to make sure that we are able to meet their expectations in terms of product selection, efficiency of execution, and geography," says Dr. Kawan.

He adds, "We also realise that the way in which international banking is being conducted has fundamentally changed since the global financial crisis of 2008. There is much more focus on compliance, risk management, reliability of IT systems, quality of capital funding, and developing products able to create dependable fee income. Regulators expect higher standards and so do our customers."

As he describes the changes that are taking place, Dr. Kawan points first to developments in the wholesale bank, the largest part of its operations.

To be of more value to its clients, the bank has launched a full-service global capital markets platform, including a central treasury sales platform. The results are being seen in the bank's strengthening position in MENA syndication markets and in recent successes in debt capital markets.

For example, the bank was ranked first in the syndication league table for Middle East bookrunners in 2015, with 17 deals including several in the GCC and some further afield in Egypt and Turkey. In the asset-backed/Shari'ah-compliant market, the bank has arranged murabaha financing for Sharjah Islamic Bank and Turkey's Ziraat Bankasi, as well as a sukuk issuance for Dubai Islamic Bank.

"We are now able to expand our treasury capabilities outside Bahrain, cross-selling capital-efficient products such as commodity hedges, repos and Islamic derivatives," says Dr. Kawan. "And we have hired a range of senior bankers with regional and international experience to accelerate execution of this initiative."

"Our long-standing international operations give us access to a much wider range of investors than those available to many other GCC banks. That's one of the reasons why we've been able to win mandates from Middle Eastern banks and companies who are looking to diversify their investor base beyond their home markets and regions," says Dr. Kawan.

Likewise, in order to increase the connectivity of the markets it serves, the bank is upgrading its representative office in Singapore into a full branch and is applying for a licence to operate in the Dubai International Financial

**Bank ABC: shareholders, 31 December 2015**

| | |
|---|---|
| Central Bank of Libya | 59.37% |
| Kuwait Investment Authority | 29.69% |
| Others, with shareholdings less than 5% | 10.94 |

**Notes:**

- Bank ABC listed on the Bahrain stock exchange in 1990.
- In 2010, the Central Bank of Libya bought the 17.72% stake held by the Abu Dhabi Investment Authority.

Centre. Both of these platforms will enable the bank to further strengthen origination and distribution globally, not just in Asia, and connect its MENA customers with broader geographies.

## European operations strengthened

In London, ABC International Bank has been strengthened with a new leadership team including the recruitment of a high-calibre group to develop trade business with financial institutions. Elsewhere in Europe, new business-focused general managers have been appointed in the three European branches in Paris, Frankfurt and Milan. A new head of Scandinavian marketing was recruited for the Stockholm marketing office. A new Global Trade Distribution Unit has already been launched and further strengthening of the European trade finance network is expected in 2017.

Dr. Kawan makes clear that the bank is committed to expanding its retail business to create a more even balance between the retail and wholesale franchises. The existing domestic banking businesses in the MENA region and Brazil are earning strong returns, are largely self-funding and have sustainable growth paths (the Tunisian branch network is being expanded), but the bank is now actively reviewing acquisition opportunities as a way of expanding the retail business.

Internally, the bank has been responding to the tougher regulatory environment faced by all banks since the global financial crisis.

Dr. Kawan points to the upgrade in the bank's compliance department, which began in 2014 with the appointment of a new and highly experienced Group Compliance Officer and the subsequent designation of a dedicated Group Money Laundering Reporting Officer. Structurally, Group Compliance was transformed into an independent function reporting to the Audit Committee and with direct access to the Board, as well as to senior management.

As part of the re-consideration of group risk and compliance, the Board of Directors re-shaped the bank's Risk Appetite Statement in 2015 to align it with international best practices. The bank is now implementing a group-wide Governance, Risk and Compliance package that will align all three functions throughout the bank.

Alongside the strengthening of the business, Bank ABC has moved to strengthen and unify its branding.

In June 2015, the bank changed its name from Arab Banking Corporation (ABC) to Bank ABC. Although the legal entities have retained their original names, the brand name 'Bank ABC' is now being applied across the whole spectrum of its operations, with the sole exception of Banco ABC Brasil. So, for example, ABC International Bank remains the legal name of Bank ABC's London subsidiary but it is now known as, and trades as, Bank ABC.

"Our objective was to have a consistent, single, universal brand across all of our operations, making absolutely clear that all parts of the group are following the same strategy and are working together for the common good of our clients," says Dr. Kawan.

An artist's impression of what Bank ABC's head office building will look like after it has been upgraded, and with the addition of a newly-purchased tower (on the right)

## A distinguished history

Arab Banking Corporation was created in 1980 by three Middle Eastern governments: Abu Dhabi, Kuwait and Libya. It quickly carved out a central role in the recycling of Arab oil revenues – massively enhanced by the high prices that followed the Iranian revolution of 1979 – into the global economy. It was the leading financial institution in the Bahraini offshore banking market, and within a few years it had bought banks in Spain, Hong Kong and Brazil and was developing European business through branches in London and Milan, a subsidiary in Germany, and a branch in Paris. (The London branch was upgraded to a subsidiary in 1991.)

In 1990, the ownership structure was opened through an IPO on the Bahrain and Paris stock exchanges, although the three governments retained control.

During the 1990s, Middle East financial markets were maturing and liberalising, and ABC began to identify opportunities to use the expertise that it had gained in global markets in countries that were closer to home.

The bank's strategy was re-focused on the Middle East. Retail banking operations were launched in Jordan, Egypt, Tunisia and Algeria during this decade.

As part of that pivot to the Middle East, the bank sold Banco Atlantico in 2003 and International Bank of Asia in 2004. Both these banks had occupied a significant amount of balance sheet space, so their disposal freed up huge amounts of capital to develop business in the Middle East.

Further changes were to come in 2008 when the bank's paid-up capital was increased to $2 billion and in 2010 when it was increased again to $3.1 billion, catapulting the bank back into the ranks of the Middle East's biggest financial institutions.

The capital increase in 2010 enabled the Central Bank of Libya to take majority ownership of the bank since it not only subscribed its share of rights in full but also bought the 17.7% share held by the Abu Dhabi Investment Authority.

Saddek El Kaber, Bank ABC's Chairman and the Governor of the Central Bank of Libya, has this to say about Libya's role in the bank: "Libya has always been an active supporter of Bank ABC because it has been playing an important role in the economic development of the region, not least by facilitating finance for mega projects in the oil and gas sector, industry and infrastructure."

Mr. El Kaber also provides a broader perspective on Libya's role in Middle East financial markets: "Libyan financial institutions have always lived up to their obligations as shareholders. In the 1990s, some banks in the GCC faced difficulties as they adjusted to lower oil prices and slower economic growth in the region. Libya always supported those banks; we never walked away from our financial obligations."

Mr. El Kaber was elected Chairman in late 2011, shortly after he became Governor of the Central Bank of Libya, replacing Mohammed Layas, a senior Libyan official who had served as ABC's Chairman for ten years. Prior to his appointment to the Libyan Central Bank, Mr. El Kaber had been serving as Deputy Chief Executive Officer of ABC International Bank in London.

Libya provides four of Bank ABC's nine directors, including its chairman, and Kuwait provides four, including the deputy chairman. The ninth member is Dr. Farouk El Okdah, who was the Governor of the Central Bank of Egypt from 2003 until 2013. Dr. El Okdah was appointed to Bank ABC's Board in 2015.

In 2013, the bank promoted Dr. Khaled Kawan to be its new Group Chief Executive Officer. Dr. Kawan had been with the bank for 25 years, most recently as Deputy Chief Executive and, immediately prior to his appointment, as acting Chief Executive.

Together, Mr. El Kaber and Dr. Kawan initiated the business review that led to the re-branding and a refined business strategy that is driving the bank forward today.

## Taking a long-term view

"Bank ABC is destined to continue to play a leading role in the banking industry in the region for the long term," says Mr. El Kaber. "Long-term financial strength, including the ability to consistently serve our clients, is more important than short-term profits."

### Geographical breakdown of loans and liabilities, end-2014)

| % of total | Loans | Liabilities and equity |
|---|---|---|
| Arab world | 52 | 77 |
| Western Europe | 9 | 4 |
| Asia | 4 | – |
| North America | 3 | 4 |
| Latin America | 22 | 16 |
| Others | 10 | – |
| **Total** | **100** | **100** |

*Source: Bank ABC*

### Geographical structure of income, 31 December 2015

| | MENA subsidiaries* | International wholesale banking | Group treasury | ABC Brasil | Other | Total |
|---|---|---|---|---|---|---|
| **Operating income** | 186 | 204 | 52 | 255 | 32 | 729 |
| **Profit before tax and unallocated operating expenses** | 91 | 144 | 32 | 147 | 8 | 422 |
| **Tax on foreign operations** | -26 | -6 | -1 | 32 | – | -1 |
| **Unallocated operating expenses** | | | | | | -114 |
| **Profit for the year** | | | | | | 237 |
| **Operating assets** | 3,588 | 9,622 | 8,879 | 6,039 | 67 | 28,195 |
| **Operating liabilities** | 3,049 | | 15,864 | 5,169 | 5 | 24,087 |

** Algeria, Jordan, Egypt and Tunisia. Source: Bank ABC*

**Group Financial Structure, 31 December 2015**

| | Assets | Loans | Deposits | Equity | Branches | ABC shareholding |
|---|---|---|---|---|---|---|
| **ABC Algeria** | 585 | 377 | 399 | 151 | 24 | 87.7% |
| **ABC Jordan** | 1,451 | 767 | 1,178 | 215 | 27 | 87.0% |
| **ABC Egypt** | 1,291 | 326 | 1,083 | 171 | 28 | 96.6% |
| **ABC Tunisia** | 218 | 89 | 179 | 35 | 12 | 100.0% |
| **ABC Internat. Bank (London)** | 4,202 | 2,723 | 3,052 | 656 | 4 | 100.0% |
| **Banco ABC Brasil** | 6,025 | 3,037 | 4,370 | 675 | 6 | 61.2% |
| **ABC Islamic Bank (Bahrain)** | 1,337 | 872 | 1,046 | 278 | – | 100.0% |
| **Arab Financial Services (Bahrain)** | 68 | – | 1 | 58 | – | 54.6% |
| **ABC Parent (ABC BSC)** | 16,905 | 5,767 | 8,934 | 3,773 | n/a | n/a |
| **ABC Group** | 28,195 | 13,958 | 18,454 | 3,773 | n/a | n/a |

** According to Basel 2.*
*Source for data: Bank ABC*

The bank's financial strength is easy to discern. Bank ABC showed a risk-weighted capital ratio, under Basel III, of 19.4% at the end of 2015. Non-performing loans accounted for only 3–4% of the portfolio. Provisions were equivalent to 121% of non-performing loans.

As for funding, customers' deposits account for about 60% of the balance sheet and are sufficient to fund the bank's lending activity. Long-term funding provides a fifth of non-equity liabilities.

Earnings in 2015 were compromised by weakening currencies in key markets. (The bank reports in US dollars.) This was particularly evident in Brazil, which witnessed a devaluation of more than 30% in the local currency during 2015. Similarly, a 20% devaluation in the Algerian dinar during 2015 pushed dollar-denominated profits lower.

Despite these challenges, the bank generated $180 million in net profits for its shareholders in 2015.

So what does the future hold for Bank ABC?

Khaled Kawan says, "We're happy with the structure of the Group. We have three key franchises: the four MENA subsidiaries in Algeria, Egypt, Jordan and Tunisia that conduct both retail and wholesale business; international wholesale banking, directed from Bahrain and with significant presence in London; and of course Banco ABC Brasil. All three are generating sustainable profits. We're interested in further acquisitions, but we will take a cautious approach based on the long-term interests of our shareholders and our customers."

Saddek El Kaber reinforces his Chief Executive's statement: "We're very conscious of our heritage, both as a flagship institution for Bahrain and as a flagship for the Middle East within the global financial system. With our new strategy and new brand, we are perfectly positioned to serve our customers wherever their business may take them." ■

**Bank ABC: summary of financial condition, 2011–2015**

| Financial Statements ($mn) | End-2015 | End-2014 | End-2013 | End-2012 | End-2011 |
|---|---|---|---|---|---|
| Loans | 13,958 | 14,819 | 13,653 | 12,860 | 11,985 |
| Non-trading securities | 5,535 | 4,627 | 5,116 | 4,005 | 6,050 |
| Assets/liabilities | 28,195 | 29,356 | 26,545 | 24,527 | 25,015 |
| Customers' deposits | 13,384 | 13,945 | 13,030 | 12,029 | 11,526 |
| Shareholders' funds | 3,773 | 4,006 | 3,940 | 3,778 | 3,598 |
| Total operating income | 729 | 888 | 857 | 816 | 818 |
| Net profits | 180 | 256 | 239 | 205 | 204 |
| **Ratios (%)** | | | | | |
| ROAA | 0.63 | 0.90 | 0.93 | 0.83 | 0.76 |
| ROAE | 4.80 | 6.50 | 6.20 | 5.50 | 5.70 |
| Cost/income | 58 | 49 | 51 | 49 | 51 |
| Basel capital ratio* | 19.4 | 21.1 | 22.3 | 23.6 | 24.3 |

** Total capital ratio for 2015 under Basel III, previous years under Basel II*
*Source: Bank ABC*

# Saddek El Kaber: steering the Central Bank of Libya through times of crisis

In some ways, Saddek El Kaber is a very fortunate man. As Chairman of Bank ABC he is spearheading one of the Middle East's most prestigious banks.

But, in other ways, he is a man few would envy. As Governor of the Central Bank of Libya he has been facing the nearly impossible task of managing monetary policy and a banking system in a war-torn country where rival governments and armies vie for power and territory. And, of course, as a Libyan, he feels the sadness of someone who has seen his country misruled and abused for decades.

*Arab Banker*'s Editor, Andrew Cunningham, spoke to Saddek El Kaber about his work at the Central Bank of Libya, his professional background, and his hopes for the future.

**_ARAB BANKER_: What are your key priorities as Governor of the Central Bank of Libya (CBL)?**

SADDEK EL KABER: The CBL must continue to operate as a critical component of the Libyan government that fulfils its mandate whilst ensuring that the country continues to function on a day-to-day basis. On occasions, the government is unable to operate effectively, and we attempt to bridge the administrative gaps that sometimes open up, for example between the Ministry of Finance and the Ministry of Economics. One of the key responsibilities upon which I place a lot of focus is managing Libya's financial reserves, which must be handled in a fully transparent manner and in accordance with our laws.

At a more day-to-day basis, my focus is on ensuring that payments can be made and that cash is available to allow the economy to operate. For example, when we receive new shipments of physical banknotes, we make sure that they are distributed throughout as much of the country as possible. We are also trying to enhance the electronic payment system in order to keep reliance on physical cash to a minimum.

One of our successes has been the modernising and updating of the Civil Registry. This was a project initiated and financed by the CBL and it enabled us to pay salaries using people's National Identification Number. It led to us saving billions of dinars from the government's salary bill.

**What is a typical working day like, as Governor of the CBL?**

In these exceptional times there is no 'typical working day' since every day is so different, but what I would say is that our working days in the Central Bank are more 'normal' than you might expect. My day starts at 7.30am, and I have to respond to any situations that have arisen overnight. My schedule has to be very flexible in order to accommodate the changing political and security environment in Tripoli and the rest of the country.

My colleagues and I hold meetings with commercial banks to discuss issues of concern and issues of policy, just like other central banks all around the world are doing every day. For example, in recent months, I have called in representatives of the banks to discuss the efficiency of documentary credits for importers, I have called in compliance officers to discuss banks' adherence to regulations and laws, and, as indicated above, I have been speaking to the banks about the electronic payment system.

Our head office building in Tripoli has survived the civil war in tact. Even during the revolution itself, none of the militias tried to destroy the Central Bank building – everyone recognised that the CBL is an institution for the whole of Libya.

I would add that I am fortunate to have many supportive colleagues at the central bank but if I were asked to highlight two of them I would identify Dr. Tarik Yousef and Mr. Hamuda Al-Aswad.

**What are the biggest challenges you are facing at the CBL?**

The biggest challenges relate to the instability of the government and also to the lack of security. Then there is the problem of revenues. Oil exports have fallen from around 1.6mn barrels/day (b/d) before the revolution to around 200,000 b/d. As a result, the amount of money at the disposal of the government – and the Central Bank – is much less than we need to effectively run the country.

Turning specifically to the Central Bank, I would highlight a problem of demotivated employees that had previously not been given comprehensive training for the roles they performed. That was not their fault – it was the fault of the previous political regime. As conditions in Libya improve, staff training and development is one of my priorities in the Central Bank.

### Aggregate balance sheet of commercial banks in Libya, December 2015

| | Million Libyan dinars | Million US dollars |
|---|---|---|
| Deposits with Central Bank of Libya | 45,123 | 32,396 |
| Deposits with banks abroad | 6,700 | 4,810 |
| Credit to the economy | 20,213 | 14,512 |
| Other assets | 18,198 | 13,065 |
| Assets/liabilities | 90,233 | 64,783 |
| Deposits | 71,257 | 51,159 |
| Other liabilities | 13,889 | 9,971 |
| Capital and reserves | 5,088 | 3,653 |

*Source for statistics: Central Bank of Libya website*

### What other long-term priorities do you have?

Upgrading the national digital payment system is a top priority. Even after peace is restored, Libya will be a heavily cash-based society. We need to have more transactions, both retail and business, conducted on electronic platforms.

More broadly, my top priority will be to restructure the banking system and to force the commercial banks to put greater focus on governance, compliance, transparency and accountability. This is because the banking system will be critical to the stability of the country and to restoring the confidence of international markets in our economy. As part of this upgrading of the banking system we will certainly want to work with international partners. I already spend part of my time meeting with international organisations, keeping them updated on current events and thanking them for the support that they are giving us.

Before the civil war erupted, I had spoken to Standard and Poors (S&P) about re-issuing a sovereign credit rating on Libya. We had investment grade ratings from both Fitch and S&P before the revolution but both agencies withdrew their ratings during the civil war. I still think that getting an international credit rating will be a priority for Libya as we re-engage with the global financial system.

Finally, I would mention Islamic banking. Although the banking law was updated in 2005 to permit Islamic banking, in practice Libyan banks were not offering Islamic banking services before the revolution. However, two of our banks, Goumhouriya and Wahda, announced in 2013 that they would be offering Shari'ah-compliant services, and I am confident that as the Libyan banking system develops in the years ahead we will offer attractive opportunities to Shari'ah-compliant institutions and investors outside of Libya, as well as meeting the needs of our own citizens who want to bank in a Shari'ah-compliant manner. ■

### Cleaning the books of Umma Bank

*Saddek El Kaber tells the story of his days at Umma Bank*

I returned to Libya in 1988 having previously worked for CIGNA Corporation, managing real estate investment in North America. Shortly after my return, I was chosen to take over Umma Bank as Chairman and General Manager. This was in September 1988 and the bank was known to be in trouble. It had not closed its books for eight years and its internal controls/compliance were in complete disarray. Only one or two of its branches had stand-alone computers. Head office and other branch records were kept on paper. We began working our way through the books and upgrading the management information systems. Arbift, the Abu Dhabi-based bank that is a subsidiary of Libya Foreign Bank gave us a lot of help at this time, particularly with the customisation of our software. [Arbift is now known as Al Masraf.] After four years, we managed to close the books and then we drew a line. We said from now on everything in the bank has to go by the book. Everything has to be done in line with our new internal controls system. It was a good time for Umma Bank and staff called it a 'golden era'. We managed to attract fresh blood to the management team – Libyans coming from the US, Canada and the UK. We had a new IT system and we were seen as a 'pilot' for change in the Libyan banking sector. Unfortunately for me, a few years later I was named by the Governor of CBL (after no consultation with me) to create a new network of community banks throughout Libya. This was a political project of Colonel Ghaddafi and I didn't think it was bankable, feasible, practical or good for the country. Having refused to proceed with it, I had no alternative but to leave Umma Bank in October 1998.

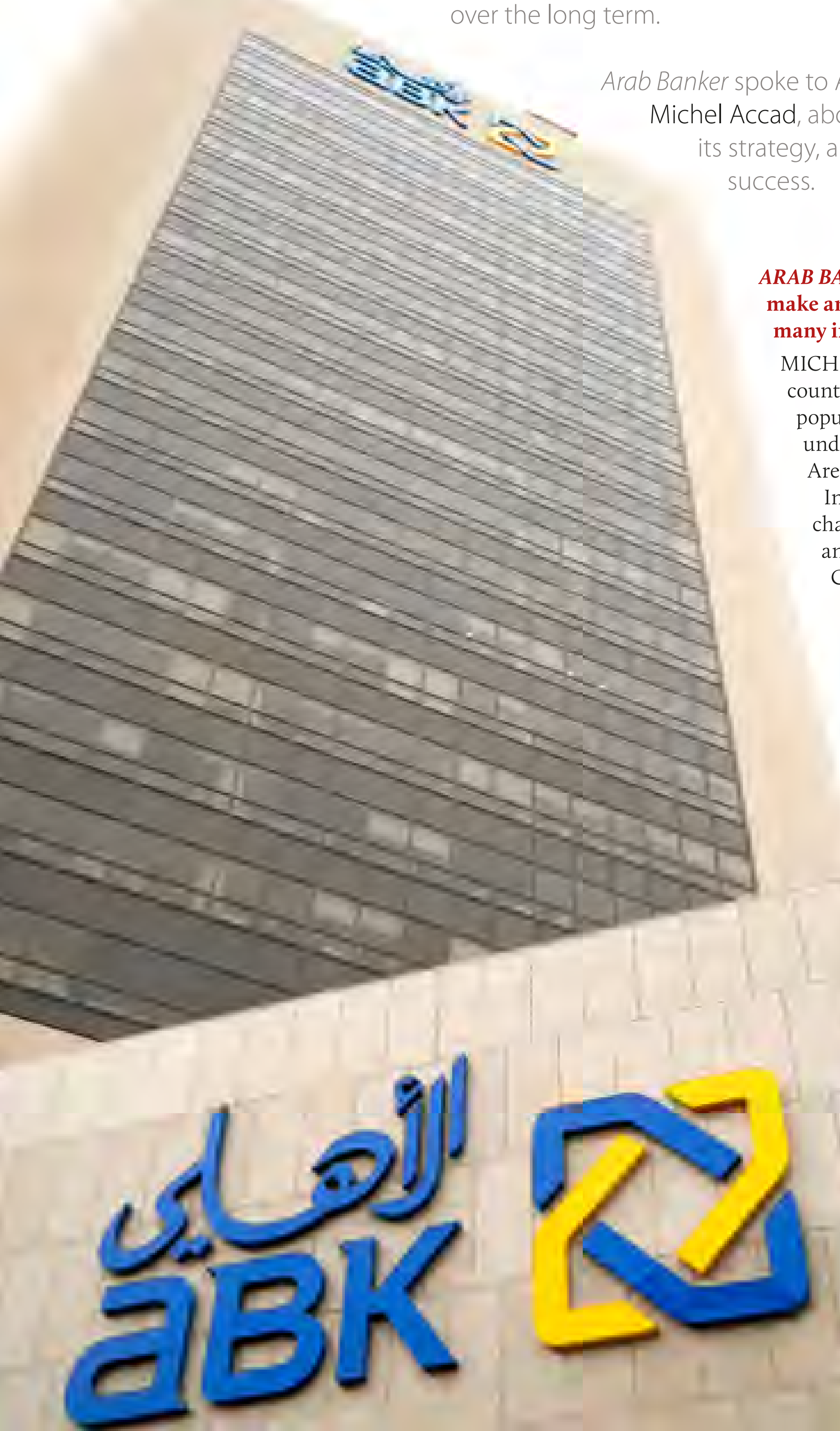
**Saddek El Kaber**

Saddek El Kaber was appointed Governor of the Central Bank of Libya in October 2011. He had previously spent ten years as Chairman and General Manager of Umma Bank, one of the country's largest commercial banks. From 2003–2008, Mr. El Kaber joined Arab Banking Corporation Tunis as General Manager and Resident Country Manager before moving to Libya to act as the Country Manager and Chief Representative in ABC's Tripoli Representative office. From 2010–2011, Mr. El Kaber was Deputy CEO of ABC International Bank in London and was appointed Chairman of ABC Group in December 2011.

# **To Egypt and beyond:** Al Ahli Bank of Kuwait is on the move

Al Ahli Bank of Kuwait is developing its operations abroad, through its acquisition of Piraeus Bank Egypt, while at home it is pioneering a more customer-friendly approach to banking that it believes will bring more business – and bigger profits – over the long term.

*Arab Banker* spoke to Al Ahli Bank's Chief Executive Officer, Michel Accad, about the bank's expansion into Egypt, its strategy, and how the bank measures its own success.




***ARAB BANKER:* Why did Al Ahli Bank Kuwait (ABK) make an acquisition in Egypt in 2015, a time when many investors were staying away from Egypt?**

MICHEL ACCAD: Egypt is the most populous country in the Arab world; it has a young population and a growing middle class; and it is under-banked. So what's not to like about Egypt? Are there risks? Of course there are!

In the short term, Egypt is facing quite a few challenges, with the drop in tourism revenue and the softening in world trade and Suez Canal movements, but in the medium term, this is a very resilient country, and I am personally optimistic about its future and growth prospects, especially after 2018, when revenues from the new gas discoveries will start to be felt. Frankly, for a Kuwaiti bank with presence in the UAE, and an aspiration to play a bigger, more regional, role in the Arab world, where else should we have gone?

Finally, within Egypt, Piraeus Bank Egypt (PBE) presented the best opportunity possible for us: it had the right size, with about 1,000 people and 39 branches (broadly ABK's size), but with a significantly smaller, yet very clean, balance sheet. The purchase price was also extremely attractive for us – I don't think anyone today would be able to buy an established bank in Egypt at anywhere close to our multiple!

**How did you fund the acquisition of Piraeus Bank Egypt and what effect has the acquisition had on your end-2015 balance sheet?**

The acquisition cost of $150 million was funded entirely internally. ABK had excess capital in 2015, and this purchase allowed us to deploy it much more effectively. Today our capital adequacy ratio is in the 16–17% range, which is more 'normal' than the 20%+ we were maintaining before 2015.

**What changes have you made to Piraeus Bank Egypt since you took control? Are you planning more changes?**

The acquisition was only completed in November 2015, less than a year ago, so it's too early to talk about the changes and their impact on the business, but in summary I can say this: On the people front, we are not making wholesale changes – the executive team in place is very solid and has done a good job at cleaning up the balance sheet (at a time its Greek parent was unable to invest in growing the franchise); but some of the senior expatriates have been asked by the Greek parent to return to Piraeus Head Office, so they will eventually need to be replaced.

On the strategy side, there will be some changes as we hope to grow the bank and be more active in soliciting new business, both locally as well as Kuwait-linked. We will also market new products to our Egyptian retail clients and provide regional corporate finance solutions for the medium to large size local and regional corporates.

At the same time, we expect the success transfer to work both ways: for instance, Piraeus Bank Egypt has initiated a very successful SME business, which we would like to replicate in Kuwait and eventually the UAE.

**Are you planning further international acquisitions or expansion?**

Well, we need to learn to walk before we can run! Our priority therefore is to integrate the Egypt business within the ABK family, not to go for another acquisition at this point. Besides, we are already present in the three most attractive countries of the Arab world: Kuwait, the UAE and Egypt. Of course, this doesn't mean that we should ignore a great opportunity if it comes knocking at our door, but if we do something else inorganic over the next two/three years, it's more likely to be in the form of asset or liability purchases to beef up our footprint in one of our three countries rather than an outright bank acquisition in a new market – but of course, one should never say 'never'.

**How is the Kuwaiti economy being affected by the prolonged drop in the price of oil?**

All oil exporting countries are negatively impacted by the drop in oil prices, and Kuwait is no exception – but it is the least impacted among the big GCC exporters because it has the lowest break-even oil price needed to balance its internal budget. In fact, I suspect that Kuwait can probably withstand the current low oil prices practically indefinitely while maintaining ordinary government expenditures at present levels. Kuwait has been very wise in its spending and in accumulating foreign exchange reserves in good times, and this is now paying dividends. Of course, we also expect Kuwait to introduce new measures to boost government revenue, for instance by imposing some form of company tax and VAT, but such initiatives are best managed and coordinated regionally rather than locally to minimise the temptation for 'tax arbitrage'.

> "We wish to be viewed as primarily a Kuwaiti bank, but with a sufficient contribution from our regional operations to benefit from potentially higher growth opportunities in foreign markets."

**Over the long term, what percentage of your business do you expect to be generated by Kuwaiti customers, and what percentage by overseas customers?**

Currently, Kuwait accounts for around 85% of our income, with the remainder split between the UAE and Egypt. We do not aspire to be a full regional player, with a substantial portion of our income derived internationally, nor do we want to be a pure-play local bank with 95% or 100% of our income coming from Kuwait. We wish to be viewed as primarily a Kuwaiti bank, but with a sufficient contribution from our regional operations to benefit from potentially higher growth opportunities in foreign markets. At the same time, we would not wish to be over-dependent on our foreign operations, nor would we want to be in a position where a bad year overseas could cripple the bank's overall results. So it's a delicate balancing act. Today I feel that a 80-20 split would be ideal, but over time, as we gain more experience managing foreign businesses, we would allow that ideal split to move closer to 75-25, or even possibly 70-30, but this is quite a stretch for us and requires more time and more sophisticated matrix and control reporting structures.

**Al Ahli Bank's loans-to-customers' deposits ratio rose to 122% at the end of 2015, from 98% at the end of 2011. Could you comment on the bank's long-term funding strategy?**

Historically, we have always remained reliant on customer deposits for funding our growth. However, more recently, we began sourcing deposits from inter-bank and financial institutions to fund our rapidly growing balance sheet, diversify our deposit base and reduce concentration risk. Our strategy is to continue to maintain a reasonable degree of diversity in our deposit portfolio with an emphasis on stable, longer tenor funding. To this end we plan to issue a 10-year senior bond in the international markets later this year and also to develop attractive longer-term deposit products for our customers across the geographies in which we operate. We believe that our acquisition in Egypt, where loan to deposit ratios are historically low, provides us with an ideal opportunity to accelerate our deposit growth.

**Al Ahli Bank has introduced a 'simpler banking' strategy. Why have you done this and what day-to-day benefits will it bring to your customers?**

The 'Simpler Banking' strategy is very dear to everyone's heart in ABK, starting with our Board members. Banks need to differentiate themselves against the competition, and there are several worthwhile approaches: one is to differentiate on price and be the lowest cost provider; another is to be the first in the market and offer the most innovative products; a third is to provide tailor-made solutions to individual clients; and another is to be the safest bank in town; and I could go on. Our approach goes back to the basics: what do our clients want?

I believe our clients want smooth, fast, easy, simple banking. No one likes to spend hours in a bank to sign documents, or spend hours waiting for a trade to be processed, or to fill the same forms several times, or to sign in 20 different places. Ideally, most banking transactions should be done in minutes, and the client should leave the premises (if he has to come in at all) with everything in hand – his account number and debit card if he came to open an account, or his credit approval if he came in for a loan.

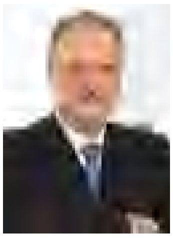
"More importantly, we need to live by our core values of Transparency, Integrity, Simplicity, and Excellence, and we need to follow our overall Vision of Reimagining a Simpler Bank."

Of course, this is much easier said than done, as it obviously requires a full re-design/re-engineering of our processes, and it can't be achieved overnight. It's also much easier to make things unnecessarily complex than to make them as simple as possible. We have already been able to implement several tactical steps, both in our online banking and in branches (such as faster loan approvals, smoother account opening process, better call centre interface, easier log-in and password management…), but to go to the next level of the customer experience, we need to upgrade our IT systems, an exercise we expect to complete in the next couple of years. The bottom line? We believe simplicity is a unique differentiator for ABK.

**What are the key indicators that you use to measure Al Ahli Bank's progress and success?**

In the recent past, we were primarily driven by our bottom line, and while this works well in the short term, it may not be the best lead indicator for our progress in the medium term – mostly because of the weight and unpredictability of the precautionary provisions. Also, when you lose a fraction of a percentage point in market share every year because of the single-minded focus on net profit, you don't quite notice it, but after five or six years, a couple of percentage points drop in market share makes a big difference! That is why we now prefer to focus more on the top line and on our share of market and share of mind. From that, we believe, the rest (including the bottom line) will follow.

More importantly, we need to live by our core values of Transparency, Integrity, Simplicity, and Excellence, and we need to follow our overall Vision of Reimagining a Simpler Bank. Clearly, this is more motivating, more rewarding, and more inspiring than simply 'making more profit', and it's also easier to translate our core values and Vision into a business strategy and a set of actionable initiatives. In the end, 'making more profit' is a lagging indicator – it is the result of a strategy, but it is not the strategy. ■



**Michel Accad**

Michel Accad became Chief Executive Officer of Al Ahli Bank of Kuwait (ABK) in May 2014, after successfully leading the turnaround of Gulf Bank, another Kuwaiti bank, and its return to profitability following the 2008 crisis. At ABK, Michel has led the successful acquisition of Piraeus Bank Egypt and launched ABK's new 'Simpler Banking' strategy.

From 2006 to 2009, Michel was the Assistant Chief Executive of Arab Bank PLC, based in Amman, with direct responsibility over all banking businesses globally, including Corporate and Investment Banking, Consumer Banking, Private Banking and Wealth Management, Treasury, and Credit.

Before moving to Arab Bank, Michel spent 27 years with Citigroup, which he joined in 1979. His last post with Citi was Managing Director and CEO for the Middle East and North Africa Division (MENA), a unit that spanned 10 presence countries and contributed over $1 billion to Citi's bottom line.

**Al Ahli Bank of Kuwait: selected financial information**

| | 2015 ($mn) | 2015 KDmn | 2014 KDmn | 2013 KDmn | 2012 KDmn | 2011 KDmn |
|---|---|---|---|---|---|---|
| **Assets** | 14,338 | 4,359 | 3,499 | 3,193 | 2,973 | 3,080 |
| **Loans** | 10,022 | 3,047 | 2,422 | 2,189 | 1,987 | 2,066 |
| **Customers' deposits** | 8,210 | 2,496 | 1,938 | 1,947 | 1,837 | 2,102 |
| **Equity** | 1,829 | 556 | 558 | 541 | 517 | 491 |
| **Net profit** | 100.0 | 30.4 | 37.6 | 35.4 | 30.0 | 50.3 |
| **Risk-adjusted capital ratio** | 17.2 | 17.2 | 23.7 | 26.9 | 27.7 | 25.1 |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# **Saudi Arabia's Vision 2030:** opening new investment opportunities for a re-energised economy

These are exciting times for Saudi Arabia. The Kingdom is responding to the present era of low oil prices with a bold range of policy initiatives that aim to stimulate the private sector, create jobs for local people and, ultimately, reduce the country's dependence on oil.

At the centre of the Kingdom's plans is Vision 2030, the ambitious and detailed blueprint announced by Deputy Crown Prince Mohammed bin Salman in April 2016.

*Arab Banker* spoke to Hasan AlJabri, the CEO of Sedco Capital, one of the Kingdom's leading asset managers, about Vision 2030 and the investment opportunities that will follow for both foreign and Saudi investors.

**_ARAB BANKER_: How will Vision 2030 stimulate economic growth in Saudi Arabia?**

HASAN ALJABRI: One of the key elements of Vision 2030 is the government's desire to accommodate 30 million pilgrims per year on the Umrah, compared to the present number of 8 million. [The Umrah is the shorter-duration pilgrimage that Muslims can complete at any time of the year, in contrast to the full pilgrimage, that happens once a year.] In order to cope with such large numbers, infrastructure around the two holy mosques and the cities of Mecca and Medina is being significantly developed and made more efficient. So, for example, a new international airport has been launched in Medina and Jeddah's airport is being expanded. In addition, significant rail services (the Haramain Railway) are under construction, connecting Mecca, Medina and Jeddah.

The government is opening opportunities for the private sector to invest heavily in hotels in the major pilgrimage cities. It is important to recognise that private sector opportunities around the expansion of Umrah traffic will not be confined to big companies – the Umrah drives a lot of employment in restaurants, shops and small hotels. There will be many opportunities here for small and medium sized enterprises (SMEs), which are a priority sector for the Saudi government because SMEs create a lot of jobs.

Other important elements of Vision 2030 are the government's plan to improve the efficiency of the domestic petrochemical industry and to make it less dependent on state subsidies, and plans to expand the health sector and the education sector.

Another interesting area is internal tourism – Saudis visiting parts of their own country rather than travelling abroad for holidays. We have to admit that Saudi Arabia is not very well equipped for tourists at the moment, even though we have some magnificent areas of natural beauty, such as the Red Sea coast and the mountainous region of Abha in the south-west, and of course the Islands of Tiran and Sanafir that were previously leased to Egypt and have now been returned to Saudi Arabia.

The Saudi Commission for Tourism and Natural Heritage, led by HRH Prince Sultan bin Salman, the brother of the Deputy Crown Prince, has been very active in trying to develop the internal tourist market, which may become attractive to non-Saudis as well.

Let me be clear. Vision 2030 is real, it is tangible and it has the full support of the Saudi government and Saudi community.

**What is the Saudi government doing to encourage foreign investment into Saudi Arabia?**

First of all, the Saudi Arabian General Investment Authority (SAGIA) is becoming more active. For example, earlier this year, SAGIA not only reduced the number of documents that foreign investors need to provide in order to get a licence to operate in Saudi Arabia, but it made licences more flexible (so investors can now get a three-year licence to enable them to explore the market, while more established investors will be able to apply for 15-year extensions to their licences). SAGIA is also making it easier to get visas for managers and staff of innovative projects.

Secondly, there has been a further opening of the stock exchange to foreigners. When the market was first opened in the middle of 2015, qualified foreign investors had to have a minimum of \$5bn under management. That requirement is being reduced to \$1bn. Settlement time is also being changed from T+0 to T+2, which is the international standard and one which is accessible to a much wider range of investors than T+0. Also, the percentage of Saudi firms that foreign investors may own is being increased to 10% from 5%.

The Saudi stock exchange (known in Arabic as the 'Tadawul') is expected to qualify to join the MSCI Emerging Market Index within the coming 18 months. When that happens, a large amount of passive as well as active investments will come onto the exchange. We are predicting that the Tadawul will account for between 2% and 4% of the MSCI Emerging Market Index.

Finally, I think it is important that people are aware of Deputy Crown Prince Mohammed bin Salman's very successful visit to the United States in mid-June. The Prince did not just meet senior US officials, including President Obama, but he also met US business leaders, explained Vision 2030, and encouraged them to consider starting operations in the Kingdom. We have already seen good success with Dow Chemicals and Babson College. I am certain that more will follow.

**Do you think the Saudi government is serious about privatising state-owned companies?**

Yes, I do. There is a lot of attention being given to privatisation within the government. The focus is on airports, ports, and utilities such as the water company and many others.

I have personally witnessed the success of such privatisation when I sat on the board of Saudi Airlines Catering Company. Saudia airlines initially invited local and international investors who had expertise and interest in the catering industry to come into the company through a private placement. Once the company moved into successful commercialisation it was floated and then publicly listed, and now the government's stake is less than 50%. I think that is a good model that can be followed with many more government-owned entities.

The privatisation of ARAMCO will be very different, due to its huge size. The main benefit of privatising ARAMCO, apart from the cash windfall to the government, will be the increase in transparency, reporting, and efficiency that will have to follow. This in turn will lead to a stronger and more profitable company, although it has to be said that ARAMCO is very well run already.

**What are the big opportunities for domestic Saudi investors in the years ahead?**

Residential housing will be a big area. In the past, this was not attractive because developers were only interested in prime residential housing. There was no mortgage law to stimulate demand from less affluent Saudis, and developers found it hard to get financing.

This is now changing. Engineer Maged al-Hogail, who has vast experience in real estate development and housing, was appointed Minister of Housing in July 2015. Before his appointment, Eng. al-Hogail was running a very successful real estate development firm. The Ministry is becoming much more active and is working closely with developers, for example by helping to identify good areas for new developments and ensuring that there will be adequate house-buyers with financing (from the Housing Bank) ready when the development is complete. And of course we now have a mortgage law, which makes banks much more willing to extend loans for residential property.

The tax on unused land, which the Saudi government approved in June, will encourage many landowners to sell, lease or build on their unused plots, and this should contribute to a reduction in the cost of building residential housing units.

Hospitality is another big area for Saudi investors, particularly in relation to the expansion of the Umrah, mentioned above. We can only just cope with 8 million pilgrims per year now. We will have to greatly increase the number of hotels, restaurants and shops in the two holy cities as well as Jeddah.

**Your company, Sedco, is a Shari'ah-compliant investor. How do you ensure that you are always investing your clients' money in a Shari'ah-compliant manner?**

First, we have a 'negative screen' that entails ensuring that we are not investing in companies that trade in industries such as alcohol, pornography, gambling, etc. Secondly, we ensure that potential investee companies comply with some financial criteria. For example, companies' financing should be structured in line with Shari'ah guidelines and we will not invest in a company if conventional financing accounts for more than one third of its market value.

International banks are now very familiar with the Islamic finance and investment products so structuring Shari'ah-compliant real estate funds and listed equity funds is now easier to do. It is a bit more difficult when we come to private equity. For private equity, we look at the fund's track record and whether they have been making a lot of investments that do not comply with our guidelines. If they have, then we do not pursue a relationship. But if the number of investments that are outside our guidelines has been small, then we ask the general partner of the fund for an 'opt out' so we do not take our investors into areas that are not Shari'ah-compliant.

Having said that, venture capital, which is one part of private equity, is often involved with firms that have no debt or very little debt – because of where the companies are in their life cycle. (See page 24 for more on SEDCO's ethical investment strategy.) ■

**Hasan AlJabri**

Hasan AlJabri is CEO of Sedco Capital and Chairman of Sedco Capital Luxembourg. He is also the Chairman of the micro finance bank, Ibdaa Bank. From 1984 until 1998, Mr. AlJabri worked for Samba Financial Group, and then spent three years at the DMI Islamic finance group, during which time he merged several of the group's banks in Bahrain. From 2001 until 2007 he was a Board member of NCB Capital, and Managing Director and Head of Investment Banking.

## Engaging with the UN's Principles for Responsible Investment

In 2005, the then UN Secretary General Kofi Annan, invited some of the world's largest institutional investors to work with him to develop the Principles for Responsible Investment (UNPRI). The Principles were launched in 2006 and in April 2016 had been signed by 1,500 firms who together had $62 trillion (yes, trillion!) under management.

In 2014, Sedco went to some fund managers who were overseeing funds that were based on the UNPRI and asked them to review two of Sedco's own listed equity strategies. The first fund had an investible universe of 275 stocks. Of these, only four were not compliant with the UNPRI. The second strategy had 100 stocks, of which only one did not comply with the UNPRI.

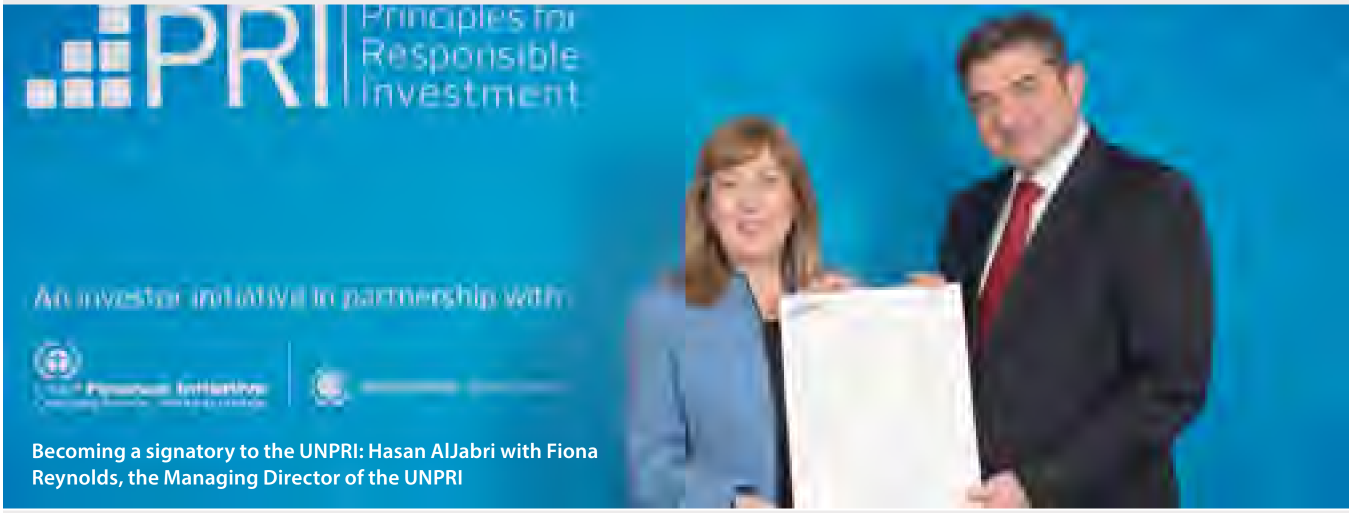
When Sedco looked at the equities that would have to be removed in order to comply with the UNPRI, it concluded that there were good reasons not to include them, even if they were Shari'ah-compliant. Soon afterwards, Sedco became a signatory to the UNPRI.

A few years later, Sedco was approached by a major fund that was investing in forests and timber. Sedco told the fund that it would be interested in investing, but only if the fund could ensure that it was compliant with the UNPRI in addition to being Shari'ah- compliant. For example, Sedco did not want to invest in a fund that would turn forests in to arid land, and it did not want to invest in a fund that would need to drive local people from their homes in order to cut timber. The fund managers were surprised by Sedco's request, but agreed to review the UNPRI and consider whether Sedco's concerns could be accommodated. Soon afterwards, not only did the fund manager agree to Sedco's conditions, but the fund itself decided to become a signatory to the UNPRI!

The three key themes of the UNPRI are governance, social responsibility and the environment. Hasan AlJabri says, "As investors, we want to ensure that companies are balancing the needs of clients, shareholders and staff, and that they are transparent. We want to invest in companies that are not only complying with laws but which also take a socially responsible approach to business. And we also care about the environmental effect that our investments will have. For example, when we invest in real estate, we want our buildings to use energy and resources efficiently. There is a building that we've invested in in India that is fully 'green' and recycles all its water for at least one additional use."

For SEDCO Capital, Prudent Ethical Investing (PEI) goes beyond compliance with leverage ratios (as required by its Shari'ah methodology) – it is an investment style that aims to avoid high and undue financial and qualitative risks and focus on the long-term sustainability of returns. AlJabri continues, "We apply an integrative approach in which the ESG criteria and prudence become a central part of our investment process. From our experience, a common mistake in the industry is to have a separate process for responsible aspects or apply them as restrictions. Thus, our investment professionals take full ownership for ESG criteria because these are important non-financial and longer-term criteria and define an investment opportunity's risk/return profile."

Prudent ethical approaches can result in better risk-adjusted returns than traditional (unconstrained) ones. As an example, take the Dow Jones Islamic Market US Total Return Index (as a proxy for PEI) and compare it to the Dow Jones US Total Stock Market Total Return Index (as a proxy for traditional/unconstrained) through the current US business cycle starting with the beginning of the recession in December 2007. While both strategies delivered similar returns through the cycle, PEI had lower volatility, resulting in a better risk-adjusted outcome. Furthermore, PEI outperformed in the bad times of the global financial crisis – when outperformance was particularly appreciated.




**Becoming a signatory to the UNPRI: Hasan AlJabri with Fiona Reynolds, the Managing Director of the UNPRI**

## About SEDCO Capital

SEDCO Capital is a Jeddah-based asset manager offering investment solutions in a wide range of countries and in a diverse range of asset classes. Having established a strong track record of advisory services and investment management, SEDCO Capital currently manages assets in a diversified spectrum of asset classes including real estate, equities and other businesses, and has approximately $5.1bn under management. SEDCO Capital employs highly efficient investment professionals throughout the world. The company follows the highest standards of corporate governance rules and practices including the use of advanced information technology systems. SEDCO Capital is also the first Saudi asset manager and the first fully Shari'ah-compliant asset manager to be a signatory of the United Nations Principles of Responsible Investing (UNPRI). Through its successful track record, SEDCO is committed to offering innovative Shari'ah-compliant investment products and today has the largest Shari'ah-compliant investment fund platform in Luxembourg through its SEDCO Capital Global Funds platform. **www.sedcocapital.com**

# **Banking for the future:** an interview with Fahad Al-Khalifa, the Group CEO of Qatar's al khaliji bank

Launched in 2008, Al Khalij Commercial Bank (al khaliji) is one of Qatar's youngest banks, and one of the youngest in the GCC, but it has quickly developed a strong profile both at home and abroad. As a new bank, al khaliji is determined to do things differently, linking its progress to the development of Qatari society and focusing heavily on environmental and social issues.

*Arab Banker* spoke to Fahad Al Khalifa, al khaliji's Group Chief Executive Officer about the bank's ambitions.

**_ARAB BANKER_: How does al khaliji differentiate itself from other banks in Qatar?**

FAHAD AL KHALIFA: We have aligned the core values and business strategy of our bank with the Qatar National Vision (QNV) 2030. We believe that pursuing a business strategy that follows the QNV makes good business sense for our shareholders, enables us to provide the best services for our customers, provides our employees with an inspiring work environment, while also contributing to the good of Qatari society as a whole.

The QNV was launched in 2008, the same year that we began operating, with the aim of transforming Qatar into an advanced society capable of achieving sustainable development by 2030.

So far we have been successful. Even though our first years of operation coincided with the global financial crisis and more recently we, like other banks, have faced the challenge of low oil prices, we have shown consistent growth and strong profitability. Our success has been recognised in numerous awards that we have received. We also enjoy A-grade ratings from both Fitch and Moody's.

When it comes to our offerings, our role is to exceed our customers' expectations with an unrivalled level of service, making us the bank of choice for our premium and corporate clients.

Providing differentiated corporate and individual products and services tailored to client needs, coupled with multiple privileges led al khaliji to be named the Best Corporate Bank and the Best Premium Bank in Qatar, which is a testament to our winning strategies as well as the hard work and dedication of our team.

We consider ourselves a 'next generation bank' in the sense that we are looking to the future of Qatar, and trying to provide excellent financial services to all sectors of our society and to customers of all ages.

**What are your key business lines?**

Our three key business lines are wholesale banking, treasury services and personal banking. During the first half of 2016, 42% of our revenue came from wholesale banking, while treasury and personal banking contributed 18% each. Our subsidiaries contributed the remaining 22%, mostly from wholesale banking.

We consider ourselves the number one Qatari bank in the Premium/High Net Worth market and a bank of choice for local corporates. We have a regional footprint, through our presence in the UAE, and international capability through our subsidiary in Paris.

**Where will growth opportunities come from in the years ahead?**

Most banks and financial institutions in Qatar are working to grow their loan books and diversify their deposits, while also developing new products and services in order to enrich existing client relationships and attract new customers. In Qatar there are some very large projects planned and as a result banks are offering large credit facilities to contractors. But banks are also supporting new export activity by Qatari clients, and in particular trade and high-value industries that are being started by small and medium sized enterprises.

In a nutshell, diversification will be the key to growth both for us and for other Qatari banks in the coming years.

**The Qatari economy is dominated by government spending and the oil and gas industries. Do you think that the Qatari economy will diversify in the years ahead and, if so, how?**

Increasingly, Qatari banks have been getting involved in large-scale infrastructure projects outside of Qatar as a way of hedging their heavy dependence on the local market and economy.

However, many Qatari banks are also beginning to realise the potential for growth and profits in other areas such as exports, cross-border business, wealth management, and SMEs and start-ups. Providing services to this wide range of customers is not only good business for banks, but it also contributes to diversifying the Qatari economy, which is one of the key objectives of the QNV.

I would also mention that there is a shift in GCC policy-making towards sustainable development, including sustainable cities and industries, and towards projects that cross country borders in the GCC. Infrastructure or rail projects are some of the massive projects that will need to be funded and these will not only provide good business opportunities for banks, but they will also enable banks to diversify their risks.

**How did al khaliji enter the French market? What sort of business do you do in France and how will your French business develop in the years ahead?**

In 2008, we acquired BLC Bank (France) S.A. after receiving the necessary regulatory approvals. We converted BLC into a subsidiary of al khaliji.

Establishing a subsidiary in France is part of our vision to be not only a Qatari and regional bank, but also a cross-border financial institution that meets the needs of our premium customer base wherever they may be.

The Paris subsidiary is making a solid contribution to Group income and gives us access to the French corporate sector. We enjoy excellent relations with other banks in the Cercle des Banques Etrangères (the French equivalent of the Association of Foreign Banks in London).

**Why do you put your UAE branches under France, rather than under Qatar? What type of business do you do in the UAE and how do you want to develop it in the years ahead?**

Our acquisition of BLC Bank (France) S.A. included the bank's branches in the UAE – in Abu Dhabi, Dubai, Ras Al Khaimah and Sharjah. This enabled us to launch our entire range of products and services to the UAE market through the BLC's established branch network in the Emirates.

In developing our operations in Paris, we wanted to replicate the areas where we were making a market at home, such as premium banking and treasury while also capturing business from cross-border trade. We are doing the same with the new branches in the UAE where, in addition to offering our premium services, we are also working to increase our share in the mid-cap sector and in other domestic Emirati segments.

**What are the key financial metrics that you use to judge the bank's performance and what other measures (non-financial) do you use to access the bank's performance?**

We use financial metrics and non financial metrics to monitor and evaluate our performance as a whole, and the performance of individual business lines and functional units.

We are looking at four aspects of our activity: financial performance, internal processes performance, customer retention performance and our own staff performance.

For example, we use the cost-to-income ratio to measure the efficiency of our operations and the non-performing loan ratio to measure the quality of our loan portfolio. We also measure the net interest margin as an indicator of the efficiency of our asset portfolio.

We also monitor the rate at which our deposits are growing since this gives us information on how much additional lending we will be capable of, and we monitor a range of capital ratios, including the Basel capital adequacy ratio.

The Central Bank of Qatar requires the banks that it supervises to calculate their risk-adjusted capital ratios in line with Basel III, and since 2014 it has set a minimum capital ratio of 12.5% (including the 2.5% capital conservation buffer). Our ratio at the end of 2015 was 13.8%, which comprised entirely Tier 1 capital.

As for non-financial indicators, we constantly measure levels of customer satisfaction and investor confidence in order to ensure that we are staying on track for success in future. We measure the length of our operational cycles and the quality of our internal processing and we benchmark them against accepted industry standards. We also look at the penetration of our products and our brand in local markets and across various segments of each individual market, and we measure various indicators related to learning and growth of our own staff. ■

**al khaliji bank's view of the wealth market in Qatar**

A Boston Consulting Group (BCG) study estimates that Qatar has the third-highest density of millionaires in the world – out of every 1,000 Qatari householders, 116 have private wealth in excess of $1mn. BCG estimates that the proportion of millionaire householders in Qatar will increase by 10% in the next five years, with those people holding 47% of their portfolio in equities, 44% in cash and 9% in bonds.

However, from our position in Doha, we can see many sub-segments within the wealthy communities in Qatar, each with distinct profiles, needs and expectations.

For example, there is an 'affluent' sub-segment, which we define as households with investable and stable assets of more than $200,000. These people tend to be high-level executives, households with dual incomes and small business owners. They are tech-savvy professionals and include Qataris, non-Qatari Gulf citizens and expatriates. These people want a tailored advisory service that uses technology to provide a multi-channel offering – they are no longer satisfied with a 'plain vanilla' product-centric approach.

In contrast, there is a class of self-driven investors who are mainly business owners and entrepreneurs. These people prefer to make their own investment decisions and want a more digital, real-time and responsive service that includes technical support.

Another very important sub-segment is high net worth (HNW) individuals and households, which we define as those with at least $1mn of investable assets. These people's main objective is to expand and efficiently operate their international business interests. HNW clients want international banking services with wide geographic reach.

On the higher end of the spectrum, there are ultra-HNW households with $50 million or more of investable assets. There are 500–550 of these people in Qatar with a combined wealth in the region of $68–$72Bn, according to the consulting firm Strategy&. Most ultra-HNWs have already developed a solid relationship with one or more banking providers but they will consider new offerings that help them streamline, consolidate and simplify the management of their wealth.

**Fahad Al Khalifa**

Fahad Al Khalifa has been Group Chief Executive Officer of al khaliji since October 2014. Prior to his appointment, he had spent eight years at Qatar National Bank, where he was Group Treasurer and then General Manager for Group Corporate Banking and Financial Institutions. Earlier in his career, he worked at the Qatar Central Bank and was also President of Qatar Forex. Mr. Al Khalifa is a graduate of Seattle University, where he obtained a Bachelor of Science in Finance in 1994.

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# NBAD–FGB merger opens the way for further financial sector consolidation in the UAE

In June, the two biggest banks in Abu Dhabi announced plans to merge. The new bank will be the biggest in the Middle East and it will strengthen the UAE's position as the leading financial services market in the region.

In the following article, Samer Hijazi, the partner in charge of Grant Thornton's office in Abu Dhabi, assesses the prospects for UAE banks in the years ahead and finds reasons to be optimistic.

The announcement in June by National Bank of Abu Dhabi (NBAD) and First Gulf Bank (FGB) that they would merge did not come as a surprise to those who have been following the banking market in the United Arab Emirates (UAE).

The new bank, which will retain the legal name and branding of NBAD, will be the largest bank in the Middle East in terms of its balance sheet indicators. With total equity of over $20bn, it is likely to rank about 60th in the world but will have a market value greater than Credit Suisse, Standard Chartered Bank and Deutsche Bank. This is the most significant event in the UAE banking sector since the merger that created Emirates NBD in 2007.

The merger remains subject to approval by the Central Bank of the UAE, but is being driven by the authorities in Abu Dhabi, the richest of the seven emirates that comprise the UAE.

The structure of the UAE banking system reflects the structure of the UAE as a whole, which consists of seven emirates, each with their own government, grouped together in a federation. Abu Dhabi and Dubai are by far the largest emirates in terms of economic activity and population and Abu Dhabi alone accounts for about two thirds of the UAE economy. The other five emirates, Ajman, Fujairah, Ras Al Khaimah, Sharjah and Umm Al-Quwain, are smaller.

The UAE banking system is, by many measures, the largest in the Middle East, even though the UAE economy is significantly smaller than that of Saudi Arabia.

Both Dubai and Abu Dhabi have their own 'offshore' banking centres, which are separately regulated and have their own legal systems. The Dubai International Financial Centre (DIFC) was created in 2004 to house financial services firms that operate in the Centre and do business with institutions outside the UAE. The Dubai Financial Services Authority (DFSA) is responsible for issuing licences, setting regulations and supervising licensed firms. The DIFC also has its own legal and regulatory framework that applies to transactions and entities within the DIFC.

Abu Dhabi's financial free zone, the Abu Dhabi Global Market (ADGM) is a more recent creation, with the first phase of licensing beginning in late 2015. Like the DIFC, ADGM has its own regulatory body, the Financial Services Regulatory Authority and its own legal system.

Despite the success of the DIFC in attracting foreign firms (and the potential for the ADGM to do so in future) it is the local banks that dominate financial services in the UAE. It is these banks that will shape the future of banking in the UAE.

In this framework, let us consider the prospects for the UAE banking system in the years ahead.

Firstly, it is important to recognise that UAE banks have performed well in the years since the global financial crisis. UAE banks have been among the best performing in the GCC. They consistently show high levels of capitalisation and profitability. Net losses in the UAE banking system are very rare. As a result, the UAE banking system is entering the present more difficult environment from a position of strength.

Secondly, the UAE government has made it clear that it intends to maintain expenditure despite lower oil revenues. It is able to do this because it holds huge financial reserves, accumulated during previous years of more buoyant prices. The Federal budget for 2016 is only slightly lower than that for 2015, and more than half of the expenditure is devoted to education, health, social projects and infrastructure.

Thirdly, the Central Bank of the UAE has made it clear that its supervisory focus in the years ahead will be on prudential risk management, i.e. while it continues to expect banks to lend to the market, it also expects this to take place through a rigorous credit risk management process.

In this wider context, the NBAD–FGB merger does make strategic sense with NBAD being particularly strong in wholesale banking (and having a large international network), while FGB's strengths lie in its larger and more profitable domestic consumer and retail business. Both banks are effectively controlled by the Government of Abu Dhabi, or entities and individuals close to the Government.

NBAD is larger when it comes to total assets but FGB has been delivering a higher return on equity in recent years. If the merger completes successfully, the new entity might find itself in the envious position of having the benefits of NBAD's deeper liquidity and access to global wholesale markets together with FGB's ability to deliver higher earnings per share.

Other reasons believed to be behind the merger include a desire to achieve cost savings. There are many operational areas where the two banks complement each other and other areas where they overlap. Indeed, you can drive down some streets in Abu Dhabi and find branches of NBAD and FGB side by side.

Finding such efficiencies is particularly important at a time when economic growth in the Gulf region has slowed as a result of low oil prices, but mergers such as these also reflect the opportunity offered by new technology to maintain and enhance levels of service while using fewer resources.

The new and enlarged bank will also be in a better position to make its mark in global financial markets. For some time now, NBAD has been pursuing its international strategy of 'West–East Corridor', i.e. the growth region of the world stretching from West Africa to East Asia, while FGB has also been making inroads into these markets. The new bank will be able to combine people and resources and, with its enlarged balance sheet behind it, will emerge as a forceful competitor to many local and international banks in these markets.

No one can deny the merger comes with its own challenges. Mergers of this size can invariably be very complex and, often, quite costly in their own right. The challenge will be to manage the costs of the merger while also delivering operational savings in the future which outweigh these costs. Another challenge will be getting the 7,500+ employees of NBAD to work effectively with the 1,400+ employees of FGB, all of whom will have to adapt to new processes, management teams and a new culture. The cultural challenge should not be underestimated. Having worked with the Lloyds Banking Group (which comprises Lloyds and Halifax Bank of Scotland) earlier in my career, I can still remember some people proudly telling me that they were 'Bank of Scotland' employees even though the Halifax-Bank of Scotland merger had taken place many years before!

While many industry observers have been calling for more consolidation in financial services across the GCC, the authorities in both Abu Dhabi and Dubai have shown a refreshing willingness to merge troubled institutions or, in the case of NBAD and FGB, to initiate mergers between institutions that are strong but where the opportunities for synergies and efficiencies of scale exist.

A few weeks after the NBAD–FGB merger was announced, the Abu Dhabi authorities announced plans to merge two of their investment funds, International Petroleum Investment Corporation (IPIC) and Mubadala Development Company. IPIC was created in 1984 and holds Abu Dhabi's investments in oil and gas companies while Mubadala was created in 2002 specifically to diversify Abu Dhabi's exposure to oil and gas by investing in other sectors.

In Dubai, the authorities have used their holdings in local banks to restructure institutions that faced difficulties during the global financial crisis and as a result of the fall in local real estate prices, ensuring that the emirate has remained free of troubled banks.

All of this indicates that a fundamental and strategic re-assessment of the positioning of the UAE economy and financial services in particular is taking place to respond to what is described as the 'New Normal' in global markets.

Speaking to many bankers in the market, I find that the mood is mixed. While the majority of people welcome the merger as a positive for the UAE banking sector, opinions differ as to what will happen next. Some believe this will be a one-off transaction, while others feel it is only the beginning of a much-needed consolidation in the banking as well as the wider financial services sector. Speculation is rife in the market as to what the next merger might be. Could Abu Dhabi Commercial Bank now acquire Union National Bank? Or Abu Dhabi Islamic Bank merge with its Islamic competitor – Al Hilal Bank? What about the insurance sector? A look at the website of the Emirates Insurance Authority (the regulator of all onshore insurance providers in the UAE) shows a list of nearly 100 insurance providers – will we see some consolidation in that sector as well before the end of 2016?

Scope for further banking consolidation clearly exists in the UAE and the industry will benefit from consolidation in the long term. There are currently approximately 50 banks all competing in a market which is already highly penetrated with very tight margins. Achieving satisfactory growth in such conditions is a challenge and it has obvious implications for the financial conduct of bank salespeople desperately trying to achieve their targets. Consolidation is one way of addressing this issue.

There are obstacles to further consolidation. For example, one obstacle lies in the differing business models of Islamic banks and conventional banks. Although mergers and acquisitions between Islamic banks and conventional banks have occurred in the region (in Bahrain, Salam Bank, an Islamic bank, acquired BMI Bank, a conventional bank), the need to convert the conventional bank into an Islamic bank can complicate the transaction. However, past experience shows this is not impossible.

Our own view is that if oil prices stay at current levels, further consolidation can be expected. Indeed, if NBAD and FGB complete their merger successfully and really do emerge as a regional powerhouse, other financial institutions will be forced to consider merger options to be able to continue to compete effectively with the new bank. Either way, we also expect the UAE economy to continue offering banks good business opportunities, both at the corporate and at the retail levels, but we also expect that banks will be scrutinising credit decisions more closely than before. ■

**Grant Thornton United Arab Emirates**

Grant Thornton UAE is a member firm within Grant Thornton International Ltd. Grant Thornton UAE has been providing assurance and advisory services to growth-oriented entrepreneurial companies which are based in all markets and industries since 1966.

Extensive local and regional knowledge gained through the years has supported the development of the firm's reputation for providing a distinctive client service to its local, national and international client base.

**Samer Hijazi**

Samer Hijazi is a partner in Grant Thornton UAE and is based in Abu Dhabi. He joined Grant Thornton UAE in November 2015 having worked for 15 years in London with KPMG's financial services audit and advisory practice where his clients included FTSE 100 listed banks, global investment banks and sovereign wealth funds. Samer is also a member of the Board of Directors of the Arab Bankers Association.

# Executive search in the Middle East: bankers still in demand in a changing market

The Middle East has long offered good employment opportunities for bankers. Salaries have been high, taxes low and the fringe benefits attractive. But as Middle Eastern financial markets mature, and the reservoir of local talent grows, how is the employment market in the region changing for financial service professionals? And how is it being affected by lower oil prices and more straitened economic circumstances?

*Arab Banker* spoke to Bert de Ruiter, a partner with London executive search firm Stormbridge International, about the trends that he is seeing in the employment market for bankers in the Middle East.

**_ARAB BANKER_: Are banks in the Middle East still hiring, despite the slowdown in economic activity caused by low oil prices?**

BERT DE RUITER: The simple answer is, "Yes, they are still hiring." But the picture is diverse and is not yet supported by statistical analysis given that the market really started to change in the course of 2015.

In the GCC, we're seeing a slowdown as a result of slower economic growth and we expect that the number of new vacancies will reduce as growth plans and new initiatives are scaled back. On the other hand, difficult economic conditions can increase the rate of staff turnover in banks, particularly at the senior level, and of course that opens up vacancies for new appointments required in support of revised strategies and transformation.

Historically, the UAE has been the biggest and most attractive employment market for expatriate bankers because of the number of banks active there and the relatively open market. I expect that the UAE will continue to hold this position, although the supply–demand balance may change as a result of banks trying to cut costs. The recently announced merger between NBAD and FGB is in my opinion a good example of a revised focus on cost efficiency.

We are still seeing employment opportunities in Qatar, even though the banking market is smaller. The other GCC countries are more protected in the sense that there is great pressure or obligation to hire local nationals, but the need for senior expatriate bankers will always exist, if only to provide advisory services.

With Middle Eastern banks in London – and Europe more generally – we are experiencing an increase in the recruitment of middle and senior managers in response to constant tightening of regulatory requirements. Internal Audit, Compliance and Risk are particular areas of growth. Banks are both hiring more people and also 'up-skilling' through the recruitment of more senior and experienced people.

Britain's recent decision to leave the European Union (often referred to as 'Brexit') has created some uncertainty for Middle Eastern organisations that are present and expanding into Europe. In the short term, until there is more clarity on the actual impact of Brexit, this could slow down new hiring. At the same time, we expect that the recent developments around Brexit will have some positive impact on the European recruitment activities of Middle East banks. After Brexit, it is likely that banks will no longer be subject to regulation by the European Banking Authority, and the British regulators will have a freer hand. Also, UK-based Middle Eastern banks with branches or subsidiaries in the EU will have to review their operating model. These events will definitely lead to increased hiring requirements.

Going back to the GCC, tightening regulation in those countries is also having an effect on recruitment, leading to more opportunities for Audit, Risk and Compliance professionals.

**What about Wealth Management in Switzerland?**

We are seeing high levels of recruiting in the Wealth Management area in Switzerland, although, after the recent loosening of laws related to banking secrecy, Switzerland is facing competition from the Far East. An operating model based on activities in the UK, Switzerland and/or France is not uncommon.

**What about the non-GCC Middle East employment market?**

There is always a certain demand for new hires in the non-GCC Middle East, but a lot of countries are facing political challenges and we are seeing slow growth in their financial systems. Lebanon has always had a vibrant banking system but there are so many Lebanese bankers that the banks are able to recruit from within their own community.

We would mention West Africa and especially Nigeria as an area where the number of banking jobs is expanding. We know that West Africa is not the Middle East, but it is a region worth keeping an eye on from a recruitment perspective.

### What is happening to salary levels for bankers in the GCC?

The picture is complex. For positions within Compliance and Risk, where there is big demand for high-calibre people, salaries have been increasing. For senior managers, there has been downward pressure, simply due to supply–demand factors: the big global banks have been shedding staff, so there are more people willing to consider a position with a Middle Eastern bank – either in the GCC or in London – than before.

In the UAE we have seen salary packages becoming more 'westernised' in the sense that employees are more likely to be paid a salary and told to cover their own expenses – as opposed to having all costs such as accommodation, car, school fees, etc., covered, and then given a salary on top. Outside the UAE, we still see packages being structured the old way, but we think that is likely to change gradually in the years ahead.

At the very senior level, the so called 'C-suite' – CEO, deputy CEO, etc. – the Middle East banking sector, like everywhere else, is a very unique market. If you're a strong candidate, then you have a lot of room to negotiate a package that suits your own needs.

### How easy is it for a conventional banker to get a job with an Islamic bank?

It is getting easier because Islamic banks are now competing more directly with conventional banks. Consequently, there has been a trend to hire conventional bankers for roles with Islamic banks.

Generally speaking, if you are an experienced conventional banker, it is not necessary to have Islamic banking qualifications if you want to work for an Islamic bank. Bankers from a conventional background will often be used to provide general management input or, in the case of front-line employees, to structure a deal. Simultaneously, Shari'ah experts will be brought in to review the structure's compliance with Shari'ah rules.

Speaking as one of those conventional bankers who went on to work for an Islamic bank, I can say that you can learn the basics of Islamic banking – the elements you need to do your job day to day – quite quickly.

### If someone leaves a big global bank to go and work for a Middle Eastern bank, either in the GCC or London, will they be able to get back in to a big global bank later in their career?

That is in the hands of the individuals themselves. Usually when someone moves from a mainstream bank to a Middle Eastern bank they are cashing in their personal 'brand value' and applying the skills and experience they have learned in the past to a smaller bank where they will often have greater responsibility and authority than they have had before.

For bankers who have been working for considerable time with Middle Eastern banks, there may be no easy way back into the mainstream, but it is entirely possible for bankers to move back into big global banks provided that they make sure that they continue to develop their skills.

Remember that the global economy is changing and emerging markets, including in Asia and parts of the Middle East, are gaining in importance. That means that the mainstream banks are more likely to be interested in hiring someone with knowledge of those regions.

### What about family life? Doesn't that suffer if you're working in the GCC as opposed to, say, London?

I don't think so, and I speak from personal experience. My daughter was five weeks old when the family moved to Qatar and I found Qatar a good place to live, especially for young families.

Every country will have its own specific features. For example, in Dubai everything is right in front of you, 'in your face!', whereas in other countries you might have to look a bit harder to find the lifestyle you want. Clearly, there is less entertainment in Saudi Arabia, but there is a strong feeling of community in the expatriate compounds, and I have many friends who have had very happy years working and living in the Kingdom with their families, and who have lifetime friends from those times.

Living abroad is a fantastic life experience, but you have to find your way in the new environment. However, becoming a banker with a global view and mobility is something I can fully recommend. The banking sector is changing fast, globalisation and digitalisation have a large impact on the job market. As a result, future bankers cannot afford to be too rigid in their employability appetite. ■



**Bert de Ruiter**

Bert de Ruiter has over 25 years' experience in the financial sector in Continental Europe, the UK and the Middle East. Before joining Stormbridge, Bert worked for Qatar Islamic Bank (QIB), initially as General Manager of the bank's Wholesale Banking Division, based in Doha, and in the last years as CEO of QIB (UK). During his employment with QIB, Bert held several non-executive director roles. Before working for QIB, Bert held a wide range of senior banking positions at Lloyds Banking Group, including Managing Director of the bank's operations in Dubai and Country Manager in the Netherlands. Bert began his banking career at ABN AMRO Bank, where he held several Relationship Management roles.

Bert's focus is on leading confidential searches for both Europe and MENA-based clients. He also helps in developing the Stormbridge's Executive Management function, a service that works alongside executives to assist them in managing their career aspirations and to explore opportunities at the Board and non-executive director levels.

# GCC banks adjust to harder economic climate

A year ago, GCC banks were responding to the fall in oil prices that had begun in the second half of 2014, but their financial statements were still not reflecting the changes in the GCC economies. But, by the end of 2015, signs of strain could be seen in the banks' end of year results.

*Arab Banker*'s Editor, Andrew Cunningham, presents our listing of the biggest GCC commercial banks, and finds reasons for optimism amid the uncertain outlook.

Despite the prolonged fall in oil prices which began in mid-2014, GCC banks remain profitable and well capitalised.

Their financial statements for 2015 include a full year of low oil prices, whereas their 2014 statements reflected only the beginning of a period of lower economic growth and tighter liquidity. Despite that, none of the largest 50 GCC banks declared a net loss for 2015. None had reported a net loss for 2014. But there are signs of strain. Sixteen of the biggest 50 banks reported a fall in net profits compared to only seven in 2014. Eleven banks showed a fall in customers' deposits during 2015, compared to eight in 2014.

On the other hand, capital levels remain strong. The median risk-adjusted capital ratio of the 50 banks was 16.77% at the end of 2015 (the average was 17.71%). This is slightly lower than a year before, when the median was 17.225% and the average 18.18%, but the difference can be explained by the shift by some GCC regulators from Basel II to the stricter Basel III risk-adjusted capital criteria. More importantly, risk-adjusted capital ratios of around 17% are high, far in excess of international standards, and they give GCC banks a large cushion against any future problems arising from the economic slowdown in their region.

Looking beyond the biggest 50 commercial banks, performance remains generally strong. Only five commercial banks declared a net loss in 2015, compared to three in 2014, and all five rank among the smallest 15 in the region. Two of those five are the recently created Islamic banks in Oman, Nizwa Bank and Alizz, now in their third year of operation and still making the transition from start-ups to mature banks.

*Arab Banker*'s ranking of GCC commercial banks is based on equity size at the end of 2015. It does not include investment banks or private equity firms, although in practice none of the GCC-incorporated investment banks or private equity firms such as Investcorp or United Gulf Bank is large enough to feature. The ranking only includes commercial banks that are active.

The largest commercial bank in the region continues to be Qatar National Bank (QNB), which showed equity of $17.9 bn at the end of 2015. National Commercial Bank (NCB) of Saudi Arabia was the second largest bank, following a $1.5 bn Tier 1 sukuk issue. Emirates NBD was the third largest.

Seven banks had more than $10 bn in equity at the end of 2015, and 51 had more than $1bn. (Kuwait's Boubyan Bank, the 51st biggest in the region, had equity of $1.1 bn at the end of 2015.)

These capital levels make GCC banks the giants in the Middle East but at best medium sized banks on the global stage. The highest ranked Middle Eastern bank in *The Banker* magazine's 2015 list of the biggest 1,000 global banks was NCB at 106, one place ahead of QNB. (*The Banker*'s rankings are based on Tier 1 capital not total capital and this is why NCB ranked ahead of QNB.)

However, GCC banks are much bigger than those in other Arab countries. Jordan's Arab Bank showed equity of $8 bn in early 2016, but National Bank of Egypt had equity of about $2.5 bn (depending on the exchange rate used). The biggest Lebanese banks have about $3 bn.

As *Arab Banker* was going to press, there were reports that National Bank of Abu Dhabi and First Gulf Bank would merge, potentially creating a bank far larger than QNB. Both banks are controlled by the ruling family of Abu Dhabi.

What has yet to be seen in the GCC is big cross-border mergers. There are banks in the GCC and beyond that have regional footprints – Ahli United Bank, and Bank ABC in Bahrain, and National Bank of Kuwait and QNB are the most evident – but all these banks have expanded through buying or investing in smaller banks in other countries. There have been no cross-border 'mergers of equals'. Candidates for such mergers do exist – if only in the pitch books of international investment banks – but national sensitivities are likely to preclude large-scale combinations in the foreseeable future. No Gulf state will want to lose control of one of its own large banks.

A more open question is whether new banking licences will be issued. Several new banks were created in the years before the global economic crisis, when liquidity was plentiful and economies expanding but none have been granted since then, apart from the Islamic banking licences issued in Oman following the passage of new regulations permitting Islamic banking.

With so much new economic thinking in Saudi Arabia, and a new central bank governor, it is possible that new licences will come back onto the agenda in the Kingdom, and there are even indications that the authorities may take a more open view of Islamic banking.

But, over the short term, the priority for Gulf banks will be to preserve their balance sheets, maintain earnings and keep capital ratios high in an era of low oil prices. So far they have coped well, but they will remain under pressure in the year ahead. ■

**Largest 50 GCC commercial banks, ranked by equity size (end 2015)**

| *Figures in $ mn except for the capital ratio which is %* | | | Equity | Assets | Net loans | Customers' deposits | Net profit | Capital ratio (Basel)* |
|---|---|---|---|---|---|---|---|---|
| 1 | Qatar National Bank | Qatar | 17,882.6 | 148,053.6 | 106,734.6 | 108,630.8 | 3,114.1 | 16.3 |
| 2 | National Commercial Bank | Saudi Arabia | 14,811.3 | 119,817.1 | 67,071.0 | 86,203.6 | 2,439.4 | 17.20 |
| 3 | Emirates NBD | UAE | 13,820.8 | 110,722.3 | 73,689.8 | 78,224.5 | 1,940.1 | 20.74 |
| 4 | Al-Rajhi Bank | Saudi Arabia | 12,436.4 | 84,160.3 | 56,054.8 | 68,323.4 | 1,901.2 | 20.83 |
| 5 | National Bank of Abu Dhabi | UAE | 11,770.2 | 110,723.3 | 56,078.3 | 63,676.9 | 1,424.8 | 16.74 |
| 6 | Samba Financial Group | Saudi Arabia | 10,762.0 | 62,727.7 | 34,616.3 | 45,702.8 | 1,390.4 | 20.10 |
| 7 | National Bank of Kuwait | Kuwait | 10,529.9 | 77,867.0 | 44,715.4 | 39,792.8 | 978.4 | 16.80 |
| 8 | First Gulf Bank | UAE | 9,887.0 | 61,956.2 | 40,787.2 | 38,798.2 | 1,639.3 | 17.50 |
| 9 | Riyad Bank | Saudi Arabia | 9,744.8 | 59,547.4 | 38,577.4 | 44,554.7 | 1,079.8 | 18.4 |
| 10 | Abu Dhabi Commercial Bank | UAE | 7,825.1 | 62,166.1 | 41,852.4 | 39,087.9 | 1,341.8 | 19.76 |
| 11 | Saudi British Bank | Saudi Arabia | 7,512.8 | 50,063.8 | 33,444.5 | 39,634.6 | 1,154.7 | 17.61 |
| 12 | Banque Saudi Fransi | Saudi Arabia | 7,328.6 | 48,990.3 | 32,910.8 | 37,798.0 | 1,076.3 | 17.18 |
| 13 | Kuwait Finance House | Kuwait | 6,782.7 | 54,534.6 | 37,358.2 | 35,765.7 | 626.3 | 16.7 |
| 14 | Duabi Islamic Bank | UAE | 6,207.6 | 40,823.0 | 26,476.7 | 29,952.3 | 1,045.6 | 14.8 |
| 15 | Arab National Bank | Saudi Arabia | 6,034.8 | 45,443.0 | 30,703.3 | 36,180.9 | 788.4 | 15.46 |
| 16 | Mashreq Bank | UAE | 5,034.4 | 31,361.8 | 16,385.5 | 20,053.8 | 663.0 | 16.90 |
| 17 | Alinma Bank | Saudi Arabia | 4,893.9 | 23,658.5 | 15,084.5 | 17,476.8 | 392.0 | 23.00 |
| 18 | Commercial Bank of Qatar | Qatar | 4,758.8 | 33,934.0 | 21,064.1 | 19,183.4 | 400.6 | 13.51 |
| 19 | Qatar Islamic Bank | Qatar | 4,721.0 | 34,918.4 | 23,975.8 | 25,157.4 | 558.1 | 14.10 |
| 20 | Union National Bank | UAE | 4,608.7 | 25,450.7 | 17,445.6 | 18,364.1 | 550.2 | 19.40 |
| 21 | Ahli United Bank | Bahrain | 4,360.2 | 33,965.3 | 19,353.2 | 23,495.2 | 566.6 | 16.70 |
| 22 | Bank ABC | Bahrain | 4,108.0 | 28,195.0 | 13,958.0 | 13,384.0 | 237.0 | 19.40 |
| 23 | Abu Dhabi Islamic Bank | UAE | 4,105.6 | 32,238.9 | 21,352.3 | 25,852.4 | 526.7 | 14.59 |
| 24 | Doha Bank | Qatar | 3,630.5 | 22,900.2 | 15,287.6 | 14,504.6 | 377.6 | 15.73 |
| 25 | Bank Muscat | Oman | 3,640.9 | 32,693.5 | 19,104.0 | 17,561.4 | 457.4 | 16.31 |
| 26 | Masraf al-Rayan | Qatar | 3,397.1 | 22,822.4 | 17,114.6 | 15,289.9 | 556.9 | 18.54 |
| 27 | Saudi Investment Bank | Saudi Arabia | 3,209.5 | 24,967.5 | 16,005.7 | 18,753.2 | 354.3 | 16.94 |
| 28 | Saudi Hollandi Bank | Saudi Arabia | 3,207.1 | 28,817.1 | 20,303.8 | 23,687.2 | 539.3 | 15.58 |
| 29 | Burgan Bank | Kuwait | 2,759.6 | 22,520.0 | 13,237.4 | 12,784.4 | 290.1 | 15.60 |
| 30 | Gulf International Bank | Bahrain | 2,431.0 | 24,192.4 | 9,161.4 | 14,683.4 | 90.4 | 17.80 |
| 31 | Commercial Bank of Dubai | UAE | 2,241.0 | 15,758.6 | 10,626.9 | 11,022.9 | 290.4 | 16.59 |
| 32 | National Bank of Ras Al-Khaimah | UAE | 2,101.8 | 11,044.2 | 7,570.5 | 7,576.5 | 382.7 | 27.49 |
| 33 | Bank Al Jazira | Saudi Arabia | 1,976.8 | 16,869.4 | 11,162.9 | 13,245.5 | 343.2 | 15.83 |
| 34 | Commercial Bank of Kuwait | Kuwait | 1,903.0 | 13,322.6 | 7,581.3 | 8,401.9 | 152.5 | 18.39 |
| 35 | Barwa Bank | Qatar | 1,876.0 | 12,425.1 | 7,833.5 | 6,999.8 | 200.1 | 16.6 |
| 36 | Al Ahli Bank of Kuwait | Kuwait | 1,836.0 | 14,384.1 | 10,054.8 | 8,237.3 | 100.3 | 17.23 |
| 37 | Gulf Bank | Kuwait | 1,776.3 | 17,943.2 | 11,990.1 | 12,662.6 | 128.7 | 15.56 |
| 38 | Bank Albilad | Saudi Arabia | 1,717.8 | 13,658.0 | 9,134.0 | 11,247.2 | 210.2 | 15.88 |
| 39 | Al Khalij Commercial Bank | Qatar | 1,645.8 | 15,567.7 | 9,193.9 | 8,503.4 | 171.9 | 13.80 |
| 40 | Qatar International Islamic Bank | Qatar | 1,519.9 | 11,143.7 | 6,866.0 | 7,329.4 | 215.6 | 16.71 |
| 41 | Al Hilal Bank | UAE | 1,486.4 | 11,735.5 | 8,271.3 | 8,756.1 | 117.1 | 16.0 |
| 42 | National Bank of Oman | Oman | 1,341.4 | 8,505.1 | 6,604.4 | 5,863.4 | 156.6 | 18.0 |
| 43 | Sharjah Islamic Bank | UAE | 1,281.2 | 8,138.2 | 4,452.5 | 4,617.0 | 111.6 | 21.99 |
| 44 | Bank of Sharjah | UAE | 1,258.9 | 7,513.0 | 4,095.1 | 5,308.4 | 68.2 | 21.13 |
| 45 | Ahli Bank of Qatar | Qatar | 1,248.1 | 8,878.4 | 6,609.4 | 5,603.2 | 178.0 | 15.00 |
| 46 | Bank Dhofar | Oman | 1,241.9 | 9,364.3 | 7,113.1 | 6,756.3 | 122.0 | 14.70 |
| 47 | International Bank of Qatar | Qatar | 1,208.4 | 8,771.5 | 5,681.2 | 5,545.9 | 110.0 | 16.14 |
| 48 | Ahli United Bank Kuwait | Kuwait | 1,190.6 | 12,883.4 | 8,844.4 | 8,779.4 | 141.2 | 15.5 |
| 49 | National Bank of Fujairah | UAE | 1,165.5 | 8,179.2 | 5,361.9 | 5,885.9 | 152.2 | 18.36 |
| 50 | National Bank of Umm al-Qaiwain | UAE | 1,088.0 | 3,644.8 | 2,400.3 | 2,387.4 | 147.8 | 34.68 |

* *Some regulators require their banks to use Basel II standards and some require Basel III, so different banks' ratios may not be exactly comparable.*
*Source for data: Darien Analytics Ltd, based on publicly available financial statements.*

# Algerian banking: in search of a new business model

Information on Algerian banks is hard to find, but anyone who has been working with Algerian banks and companies knows that until recently both local and foreign Algerian banks were highly profitable.

But now the days of easy profits are over. The Algerian government has taken steps to reduce the fees that banks can earn on trade finance, while low oil prices are reducing liquidity and compromising asset quality across the banking sector. Yet the picture is not all gloomy: the Algerian Central Bank is pushing banks to upgrade their internal controls, and is doing what it can to inject liquidity into the system.

*Arab Banker* spoke to Rachid Sekak – who led the renegotiation of Algeria's foreign debt in the 1990s, and more recently established and led HSBC's branch in Algiers – about the challenges that Algerian banks are facing and their options for the future.

**_ARAB BANKER_: Could you describe the current structure of the Algerian banking system?**

RACHID SEKAK: There are six state-owned banks and 14 private banks that are wholly or partly owned by non-Algerian interests. Among the state-owned banks, Banque Nationale d'Algérie (BNA), Banque Extérieure d'Algérie (BEA), and Banque de l'Agriculture et du Développement Rural (BADR) are the biggest, while among the private banks, Société Générale, BNP Paribas, Natixis and Algeria Gulf Bank (a subsidiary of Kuwait's Burgan Bank) have the largest networks.

BNA and BEA have assets of about $30 billion, which is much bigger than the other banks. The total assets of the banking system are about $115 billion.

Figures from the Banque d'Algérie (the Central Bank) show that the public sector banks accounted for 88% of deposits in the banking system at the end of 2014 and also 88% of credit. Of 1,428 bank branches in Algeria, 1,113 – 80% – belonged to the state-owned banks. As for banking staff, of 36,287 at the end of 2014, 82% worked for the state-owned banks.

However, the picture changes if you look at the market share of import trade finance. Here, private banks account for more than 50% of all business.

**How do Algerian banks make money?**

The state-owned banks finance state-owned companies and are also significant lenders to the private sector. In contrast, the private banks are focused solely on the private sector, and about 70% of their business entails providing working capital.

For about ten years, state-owned enterprises were prohibited from doing business with private sector banks – either on the deposit side or the borrowing side. These restrictions arose following the failure of some small private banks in the early 2000s: Khalifa Bank is the best known. Even though the restrictions have now been lifted, in practice state-owned enterprises are reluctant to work with the private sector banks. This is because managers can go to gaol if they make bad decisions.

**How have recent policy changes affected the profitability of Algerian banks?**

In 2009, the Algerian government tried to reduce imports by requiring importers to use documentary credits – this enabled the government to keep greater control of what was being brought into the country because the Central Bank was the source for all of the foreign exchange needed to process the documentary credits. At the same time, the authorities put a ban on certain forms of consumer credit, such as car loans. This was another attempt to reduce imports.

At this time, the commissions on trade finance were huge – maybe two or three times what you could earn elsewhere in North Africa. The banks chose not to try to undercut each other so rates stayed high.

But since 2013, the Central Bank has taken two measures to limit the profits that the banks can make. First, it put a cap on trade finance fees and, secondly, it restricted the amount of foreign business that banks could do in relation to their equity. Initially, documentary credits were limited to four times capital, and then in 2014 the ratio was reduced to two times capital, and then in 2015 to one times capital.

**The fall in oil prices, which began in mid-2014, has had a severe impact on the Algerian government's budget and current account position. How has it affected the banks?**

For the moment the banks are in a reasonably strong position. The capital ratio of the system as a whole was 17% at the end of 2015 (compared to 16% at the end of 2014), of which 14% comprised Tier 1 capital. The figures for private banks are significantly higher than the average. The system's return on equity was 24.6% during 2015 and its return on assets was 2.2%.

On the other hand, with the slump in oil prices, the days of cheap deposits and low funding costs are over. Liquidity is tightening. Deposits in the system decreased in 2015, and the loans to deposits ratio increased from 69.5% at the end of 2013 to 74.7 at the end of 2014 and 86.7% at the end of 2015.

The banks are also going into the current time of difficulties with fairly high levels of non-performing loans (NPLs): 9.5% for state-owned banks and 8.7% for the private banks, according to IMF estimates, although it is worth noting that, until recently, NPLs at the state-owned banks were trending down.

Liquidity is tightening, although the Central Bank has taken steps to alleviate liquidity shortages: in April 2016 they reduced the reserve requirement to 8% from 12%, liberating $4 billion in liquidity; and in March 2016 they re-opened the discount window, allowing banks to swap eligible bonds for cash.

### Looking beyond the immediate liquidity squeeze, what are the fundamental challenges that Algerian banks face?

For the state-owned banks, the main issues are governance and management information systems.

The Presidents-Directeurs-Généraux (PDGs) of the state-owned banks are appointed by the Treasury and they tend to move from one state-owned bank to another during their banking careers. We need the staff inside these banks to be more commercially-minded and more aggressive in seeking new opportunities and driving profits. Some of the public banks have started to move in the right direction but it will be a long journey.

The management information systems at the state-owned banks are outdated and need to be replaced. Even good commercially-orientated managers will not be able to make state-owned banks more efficient and profitable if they don't have good management information systems to tell them how their portfolios are performing.

Furthermore, strengthening ALM capabilities will be a crucial issue in raising awareness of financial risks.

As for the private banks, their challenge is to develop broad-based franchises rather than relying on niche markets. I think those private banks that have big branch networks will be best placed to thrive in future, in part because they will be able to collect sticky deposits more easily, but also because they will have a broader range of customers.

**Large Algerian banks, summary financials (end-2014)**

| End 2014 (DZD Mn) | Banque Nationale d'Algérie | Banque Extérieure d'Algérie | Banque de l'Agriculture et du Développement Rural |
|---|---|---|---|
| Loans to clients | 1,831,665 | 877,653 | 659,397 |
| Loans to financial institutions | 55,145 | 753,789 | 295,545 |
| **Assets/liabilities** | **2,620,619** | **2,581,393** | **1,376,079** |
| Customers' accounts | 1,742,546 | 2,095,988 | 1,376,079 |
| Capital and reserves | 147,845 | 162,064 | 1,222,024 |
| **Net profit** | **298,784** | **29,808** | **6,125** |
| Memo item Assets/liabilities in $mn* | 29,967 | 29,519 | 15,736 |

** Exchange rate used: $1 = DZD 87.45 (the rate at the end of 2014)*
*Source: Bank Reports*

### Is the Banque d'Algérie implementing the Basel standards?

The Banque d'Algérie has been taking important steps to improve the regulatory and supervisory framework. It has begun applying Basel II and some aspects of Basel III. It has some basic liquidity standards which it expects banks to meet, but it is not yet introducing the liquidity coverage ratio or the net stable funding ratio.

It is also worth mentioning that the Central Bank has recently introduced stronger accounting standards and higher standards for risk management.

Prudential and regulatory frameworks have been upgraded over the last few years but still need to be enhanced.

### How will the structure of Algerian financial markets change in the years ahead?

It's possible that one or two of the state-owned banks will be partially privatised in the next few years. Privatisation

**Algerian commercial banks: aggregate assets and liabilities**

| | Sep-15 US $ bn* | Sep-15 DZD bn | Dec-14 DZD bn | Dec-13 DZD bn | Dec-12 DZD bn | Dec-11 DZD bn |
|---|---|---|---|---|---|---|
| Credit to the private sector | 33.2 | 3,505.10 | 3,119.70 | 2,719.90 | 2,244.70 | 1,981.50 |
| Credit to public sector enterprises | 35.1 | 3,707.60 | 32,24.6 | 2,434 | 2,040.2 | 1,741.7 |
| Credit to the state | 14.2 | 1,496 | 1,472 | 1,334.3 | 1,403.9 | 1,406.1 |
| Banks abroad | 0.1 | 12.7 | 6.1 | 7.5 | 50 | 53.8 |
| **Assets/liabilities** | **115.4** | **12,176.8** | **11,976.4** | **10,320** | **9,654.4** | **9,002.4** |
| Private sector deposits | 43.1 | 4,544 | 4,376.3 | 4,001.2 | 3,644.6 | 3,192 |
| Public sector deposits | 29.0 | 3,060.2 | 3,197.9 | 2,610.2 | 2,530 | 2,631 |
| Deposits from the state | 5.1 | 541.8 | 557.8 | 502.5 | 473 | 346.4 |
| Foreign liabilities | 1.7 | 175.3 | 138.3 | 93.9 | 75.9 | 39.5 |
| Capital and reserves | 7.9 | 835.5 | 744.4 | 724.2 | 667 | 609.9 |

** Figures in Algerian dinars converted to dollars at the rate of $1 = dinar 105.5, the rate applicable at the end of September 2015.*
*Source: Banque d'Algérie, Bulletin Statistique Trimestrial, Décembre 2015.*

would serve several objectives: raising money, bringing new expertise and products into the banks, and, potentially, increasing the range of shares traded on the stock exchange.

It is difficult to say whether new banking licences will be issued. The stumbling bock is the 51/49 rule introduced in 2009, under which foreigners may own no more than 49% of Algerian companies. The rule was not retroactive, so those foreign banks that are already majority owned by foreign interests are not affected, but 51/49 is a disincentive to new investors. And I do think that Algeria would benefit from new banks and more competition.

A large proportion of the population is unbanked. We need to develop new products such as leasing and factoring. The government has recently lifted restrictions on car financing and consumer credit. Mobile and internet banking is not well developed in Algeria, although a vast country such as ours is exactly the sort of place where mobile and internet banking could bring real benefits very quickly. There are plenty of opportunities to build profitable banking businesses in Algeria.

### Who will be taking the decisions on these matters?

The supervision of the banks is under the authority of the Banque d'Algérie and its governor, Mohamed Loukal. The Ministry of Finance will have to take the lead on modernising the state-owned banks, since it is the Ministry that owns them.

I would add that Governor Loukal, who was appointed in June 2016, has considerable experience both of domestic banking and of international banking. He was previously the head of Banque Extérieure d'Algérie and in that capacity has been a director of London-based British Arab Commercial Bank, and two Paris-based banks, UBAF and Banque International Arabe.

### Will Algeria get a credit rating from one of the big international credit rating agencies?

I don't think government officials see the need for a credit rating right now. Personally, I think they should get a credit rating since that would be most useful for future external borrowing, would facilitate the flow of foreign direct investment and would also greatly improve the perception of the local business environment. It would also facilitate the creation of a bond market. We do need to develop an Algerian government bond market with a yield curve that private sector firms can use to benchmark their own credit raising efforts.

### What do you think the Algerian government's top three priorities should be for the banking and financial system in the coming year or two?

Going forward, key priorities include:

- A careful calibration of monetary policy to address simultaneously tightening liquidity issues and the necessity to control inflationary pressures. Not an easy task and a real challenge!
- The promotion of better access to credit for small and medium-sized enterprises and the private sector as a whole.
- The development of domestic capital markets to facilitate the financing of forthcoming fiscal deficits and to encourage economic growth.
- To complete the above, I would add the IMF's recommendation of "enhancing creditors' rights, modernising the bankruptcy framework and improving debt enforcement procedures" as an important priority. ■

### Algerian banks: financial ratios

(Ratios taken from the IMF's Article IV Consultation, May 2016)

| | 2015 (Preliminary) | 2014 | 2013 | 2012 | 2011 |
|---|---|---|---|---|---|
| **Capital adequacy** | | | | | |
| Public banks | 16.2 | 14.9 | 19.9 | 21.6 | 21.9 |
| Private banks | 20.6 | 20.9 | 28.5 | 31.9 | 31.2 |
| **NPLs/total loans** | | | | | |
| Public banks | 9.5 | 9.7 | 11.4 | 12.4 | 16.1 |
| Private banks | 8.7 | 5.1 | 4.8 | 5.2 | 4.0 |
| **Provisions/classified loans** | | | | | |
| Public banks | 63.4 | 64.8 | 67.4 | 69.4 | 69.9 |
| Private banks | 44.9 | 71.9 | 80.3 | 71.7 | 75.9 |
| **Return on equity** | | | | | |
| Public banks | 27.7 | 25.1 | 17.9 | 22.7 | 26.1 |
| Private banks | 15.7 | 19.6 | 21.6 | 24.8 | 21.4 |
| **Return on assets** | | | | | |
| Public banks | 2.1 | 1.8 | 1.3 | 1.6 | 1.8 |
| Private banks | 3.1 | 3.3 | 3.8 | 4.6 | 4.5 |
| **Liquid assets/total assets** | | | | | |
| Public banks | 25.9 | 37.0 | 39.4 | 45.1 | 51.1 |
| Private banks | 35.9 | 44.0 | 46.5 | 50.9 | 43.2 |
| **Liquid assets/short-term debt** | | | | | |
| Public banks | 62.8 | 83.4 | 95.7 | 110.7 | 106.6 |
| Private banks | 69.8 | 75.4 | 84.1 | 93.5 | 84.6 |

*Source: Algeria, 2016 Article IV Consultation, May 2016.*

**Rachid Sekak** MBE

Rachid Sekak MBE leads BRS Consultants & Associés, a consultancy based in Paris that provides strategic and financial consulting services to multinational companies, banks, financial institutions and governments throughout Africa, MENA and Mediterranean regions.

Rachid opened and led the operations of HSBC Algeria from 2007 to 2013 as its Chief Executive Officer, having joined the HSBC Group in 2006. He had previously worked for the Union de Banques Arabes et Françaises first as General Manager for branches and Asia, and then as General Manager of one of the commercial divisions. In 1990, he had been appointed to the post of Special Advisor to the Governor of Algeria's Central Bank and was later promoted to Secretaire General du Conseil de la Monnaie et du Credit, the Bank's Board of Directors. He subsequently was appointed Director of External Debt and as Chief Debt Negotiator, shaping the Algerian debt renegotiations with the London Club and Paris Club.

Rachid started his career as a teaching assistant at the University of California and at the University of Algiers.
In 2014, Rachid was honoured by Her Majesty the Queen as a Member of the Order of the British Empire (MBE).

# Building a successful SME lending business in Egypt: Commercial International Bank explains its strategy and its results

SME banking is one of the hottest topics of discussion in Middle Eastern banking as governments recognise the significance of SMEs within their economies and the potential that SMEs have to create jobs and drive growth. Nowhere is this more evident than in Egypt, where the Central Bank of Egypt (CBE) has recently taken steps to encourage local banks to increase the amount of credit that they extend to the SME sector.

Commercial International Bank-Egypt (CIB) was one of the first Egyptian banks to launch a dedicated department to serve SMEs, launching its SME 'Business Banking' Department in 2011. *Arab Banker* spoke to Rashwan Hammady, CIB's Head of Business Banking about the bank's SME banking portfolio, and the recent moves by Egypt's Central Bank.

**_ARAB BANKER_: How much SME banking does CIB do?**

RASHWAN HAMMADY: We have a database of more than 40,000 Egyptian companies, out of which 6,500 companies are offered specially tailored products and services to meet their needs, in addition to a dedicated Relationship Manager. Within our Business Banking division, we have a professional distribution team comprising more than 100 highly trained relationship managers who have passed through our internal 'SME Business Banking' training course. The relationship managers are distributed across our network of branches all over the country, to ensure customers' convenience.

Our SME deposits and assets have been growing steadily. At the end of March 2016, we had EGP 44 billion in SME deposits and EGP 4 billion in SME assets.

**SME banking is often discussed in terms of 'Credit for SMEs'. Do you think that is the right way to think about it? How much of your SME banking involves providing credit and how much of your SME banking is based on other, non-credit, products?**

Credit is not our sole focus. Credit facilities mainly support enterprises that have financial shortfalls, and not all do, but they face many other challenges during their development and business cycles. We focus on helping SMEs manage their cash cycle, easily access their accounts, and build strong business plans. We also develop bundles of financial and non-financial solutions to cover all customers' needs. These bundles include cash management packages and digital solutions, plus training sessions that we offer in partnership with institutions, including IFC, EBRD and the Egyptian Banking Institute (EBI). The ultimate objective is to support our customers' business development and take them to the next level.

**Is SME banking in Egypt more or less profitable than retail banking and corporate banking?**

Egypt has more than three million SME enterprises, and fewer than 240,000 of these deal with banks. As a result, there are huge opportunities for business development. We believe that the SME market is potentially more profitable than corporate and retail segments, which are saturated and, in the case of the retail segment, constrained by the CBE's regulations capping an individual's debt burden ratio to 35% of their income. In the SME segment, banks have flexibility to price products based on their risk appetite and target market. And of course remember that the profits on SME business are not necessarily being generated from credit facilities. They are coming from areas such as payments acceptance, trade finance and cash management.

**The Central Bank of Egypt has recently published a regulation requiring banks to increase their SME credit portfolios to at least 20% of their total credit portfolios by the end of 2019. What is CIB doing to make sure that it will be able to meet this deadline?**

CIB Business Banking has been serving SMEs since 2011 and we believe that we are one step ahead of the market, with strong SME banking infrastructure, trained staff and a large SME portfolio. Fortunately, the definition of SMEs used by the CBE is very similar to our own. We only had to make slight changes to our four-year strategy in order to line up with the CBE's requirement for SME lending to reach 20% of our total loan portfolio by 2019.

We have focused on our target market segmentation to ensure that each segment is offered the best array of products. Additionally, we have been upgrading our human capacity and creating development plans for each staff member, including internal training and external overseas training in order to provide our customers with the best banking experience in the SME Egyptian market, while using the global market to benchmark our business model development.

We are also spending a lot of time developing our IT infrastructure. We want the entire SME banking transaction to be automated, end to end. This will accelerate turnaround times and offer our clients the most convenient solutions. We think our IT infrastructure gives us a competitive edge in the Egyptian SME market.

**The Central Bank has set a maximum interest rate of 5% on loans to small and very small companies. Will banks be able to make a profit on this business?**

Banks are not obliged to offer a maximum of 5% interest rate to SMEs. Banks can set their own pricing, but if they keep interest to 5% or lower, then they do not have to keep deposit reserves with the CBE in respect of those loans. This then unlocks funds that would otherwise be earning no interest while placed with the Central Bank. Furthermore, the CBE has announced that it will launch a guarantee scheme for SMEs before the end of 2016 and this will mitigate the risk of charging only 5% on SME loans. We also believe that the strong IT and automation that we bring to SME banking brings efficiencies that reduce the costs associated with SME banking – and as a result the 5% figure is not as daunting for us as it might be for others.

**How does the Central Bank of Egypt define 'medium', 'small' and 'very small' businesses?**

CBE classifications are based on the company's annual sales turnover and number of employees, except for start-ups, where the classification is based on paid-in capital. Micro SMEs are defined as those with less than EGP 1 million annual sales turnover, while very small enterprises are those with sales turnover ranging from EGP 1 million to EGP 10 million. Enterprises with annual sales turnover ranging from EGP 10 million to EGP 20 million are classified as small-sized enterprises, and medium enterprises are those with sales turnover ranging from EGP 20 million to EGP 100 million.

This is the first time we have had a unified definition for SMEs in Egypt and it is an important development. It will improve the comparability of data, both within Egypt and between Egypt and other countries. International benchmarking will help us identify areas where we can improve banking services and financial market infrastructure for SMEs in Egypt.

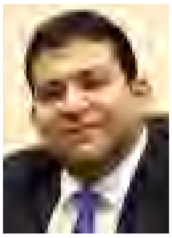
**What are the biggest challenges to SME banking, including SME lending, in Egypt?**

One of the main challenges is that SMEs do not have the formal documentation that we need in order to grant them facilities. Government regulations and laws are burdensome and very time-consuming, and as a result most small businesses do not formalise their status legally. That makes it more difficult for banks to engage with them.

It is also worth noting that SME banking is relatively new in Egypt – it has really developed only in the last ten years and fewer than half Egyptian banks were involved in SME banking before the recent CBE initiative.

**What do you think needs to be done – at a national level – to make it easier for banks to provide services, profitably, to SMEs?**

If we are to unlock the full potential of the SME sector, we need more co-ordination between the banks, the government and other institutions such as EBI and the IFC. Each of these three groups needs to work on automating their SME-related processes, and this applies in particular to business registration and taxation. It is very important to provide incentives for SMEs to move from the informal sector to the formal sector. ■



**Rashwan Hammady**

Rashwan Hammady was appointed to lead CIB's Business Banking Segment at the beginning of 2013. Prior to this, he spent six years in CIB's Strategic Planning Group, engaging with senior management and Board members on issues such as mergers and acquisitions, re-structurings, and the launching of new businesses.

Rashwan joined CIB in 2004 after graduating from the Faculty of Commerce, Sohag University. He worked initially in the finance team and successfully completed CIB's credit analysis certification, before moving to the Strategic Planning Group.

Commercial International Bank is a leading private sector bank in Egypt. At the end of 2015 it had assets of EGP 179.5 bn ($23.2 bn) and equity (before net profit) of EGP 11.8 bn ($1.5 bn).

# Rating agencies react to prolonged fall in oil prices

Over the last year, the big three international rating agencies have made some significant adjustments to their ratings on Middle East governments, with Saudi Arabia and Bahrain suffering particularly severe downgrades. But ratings on many countries, both oil exporters and oil importers, are unchanged.

*Arab Banker*'s Editor, Andrew Cunningham, analyses the changes to sovereign credit ratings over the last year.

Downgrades of Saudi Arabia, Bahrain and Oman hit the headlines earlier this year as the three big international rating agencies – Moody's, Standard and Poors (S&P), and Fitch – adjusted their ratings to reflect the prolonged period of low oil prices and the pressure that reduced oil revenues is putting on government finances.

Not all Middle East governments have been affected. Long-standing AA ratings on Kuwait and Qatar are unchanged, and so are the ratings on individual emirates within the United Arab Emirates (UAE). Abu Dhabi continues to hold a AA rating. The ratings on Sharjah, first assigned in January 2014, have not moved (A from S&P and one notch lower from Moody's). The same is true of the ratings on Ras Al Khaimah (A from both S&P and Fitch).

Outside the GCC, ratings on Morocco, Tunisia and Jordan have not changed over the last two years. Lebanon's ratings have been stable since Moody's announced a one-notch downgrade to B2 in December 2014. Egypt's ratings have also been stable since Moody's upgraded by one notch to B3 in April 2015.

The most dramatic rating change over the last year has been S&P's opinion on Saudi Arabia. The agency downgraded the Kingdom by one notch to A+ in October 2015 and then by another two notches to A– in February 2016. At this level, Saudi Arabia's rating is the same as Malaysia and Mexico, just four notches above the investment grade/sub-investment grade divide.

When announcing the February 2016 downgrade, S&P commented that oil prices had fallen since its October 2015 review and that is had revised its 2016–2019 oil price assumptions down by $20/B.

The price of oil had been around $100/B for several years

**Ratings on Middle East governments ('sovereign ratings')**

| | Moody's* | | S&P | | Fitch | |
|---|---|---|---|---|---|---|
| | 10 July 2014 | 5 July 2016 | 10 July 2014 | 5 July 2016 | 10 July 2014 | 5 July 2016 |
| AAA | | | | | | |
| AA+ | | | | | | |
| AA | Abu Dhabi, Kuwait, Qatar, UAE | Abu Dhabi, Kuwait, Qatar, UAE | Abu Dhabi, Kuwait, Qatar | Abu Dhabi, Kuwait, Qatar | Abu Dhabi, Kuwait, Qatar, Saudi Arabia | Abu Dhabi, Kuwait, Qatar, |
| AA- | Saudi Arabia | | Saudi Arabia | | | Saudi Arabia |
| A+ | Oman | Saudi Arabia | | | | |
| A | | | Oman, Ras Al Khaimah, Sharjah | Ras Al Khaimah, Sharjah | Ras Al Khaimah | Ras Al Khaimah |
| A- | Sharjah | Sharjah | | Saudi Arabia | | |
| BBB+ | | Oman | | | | |
| BBB | Bahrain | | Bahrain | | Bahrain | |
| BBB- | | | Morocco | Morocco, Oman | Morocco | Morocco |
| BB+ | Morocco | Morocco | | | | Bahrain |
| BB | | Bahrain | | Bahrain | | |
| BB- | Tunisia | Tunisia | Jordan | Jordan | Tunisia | Tunisia, |
| B+ | Jordan, Lebanon | Jordan | | | | |
| B | | Lebanon | | | Egypt, Lebanon | Egypt, Lebanon |
| B- | | Egypt | Egypt, Lebanon | Egypt, Lebanon | | |
| CCC or lower | Egypt | | | | | |

** Moody's ratings are cited using S&P/Fitch notation* before falling to around $45/ between mid-2014 and early 2015. It then remained within a range of $45–60/B until late 2015 when it fell to around $30/B. It then rose to around $50/B in June and July.

The downgrades of Bahrain have also been severe, especially because they have resulted in Bahrain losing its investment grade rating. Moody's downgraded Bahrain by one notch to Ba1 in March 2016 and by another to Ba2 in May. S&P downgraded by two notches to BB in a single action in February and Fitch downgraded by one notch to BB+ in June 2016.

Oman retains its investment grade ratings despite a three-notch downgrade to Baa1 by Moody's (two notches in February 2016 and another one notch in May) and a two-notch downgrade by S&P in February.

Downgrades of GCC oil exporters have gone hand in hand with downgrades of oil exporters outside the region. Moody's downgraded Azerbaijan at the same time as it downgraded Bahrain and Oman, and put ratings of Angola, Gabon, Kazakhstan, Nigeria and Russia on review for downgrade. Angola, Gabon, Kazakhstan and Nigeria were then downgraded in April. S&P also took action on a range of oil exporters in early 2016.

Credit ratings are more significant for the GCC states than at any time in the recent past since GCC governments are embarking on large borrowing programmes to finance their budget deficits. Bahrain cancelled a planned $750mn bond issue in February after the S&P two-notch downgrade. In May, Qatar successfully launched a $9bn bond issue, which at the time was the biggest ever issue in the region.

Saudi Arabia raised $10bn from international banks in April and in June mandated three banks to raise up to $15bn in bonds. In July, Kuwait announced plans to raise up to $10bn from international banks, in addition to around $6bn from domestic banks.

Ratings on governments have a big influence on ratings assigned to local banks and companies. This influence can be indirect – if economic conditions and a government's budgetary position deteriorates, rating agencies may conclude that banks and companies are likely to face tighter liquidity and delayed payments. It can also be direct – if a bank or company is rated at the same level as the government, then if the government is downgraded it is highly probable that the bank or company will be downgraded at the same time.

In March, S&P downgraded four big Saudi banks, citing deteriorating economic conditions (indirect influence). In July, Fitch downgraded the Bahraini government companies Mumtalakat and Batelco as a direct result of its earlier downgrading of the Bahraini government (direct influence).

None of the three rating agencies has ratings on the Government of Dubai, but Moody's and S&P do rate the Dubai Water and Electricity Authority (DEWA), a government-owned utility. In the past, the rating of DEWA could be used as a proxy to gauge how the Dubai government might be rated.

In May, S&P updated DEWA by one notch to BBB+ and, in June, Moody's upgraded it by one notch to Baa1. Moody's press release noted that the company's financial profile had improved due to two tariff increases in 2008 and 2011 and the introduction of a fuel surcharge in 2011. Population growth had also led to higher water and electricity consumption.

The lesson of the DEWA upgrade is that Middle East utilities and other government-owned companies, as well as private sector entities, have scope to strengthen their ratings by improving their internal financial condition, regardless of what is happening in the wider economy. ■

### Ratings on selected non-Middle East governments (Moody's ratings only)*

| | |
|---|---|
| AAA | USA, Australia, Canada |
| Aa1 | UK |
| Aa2 | France, Korea |
| Aa3 | China |
| A1 | Japan |
| A2 | |
| A3 | Malaysia, Mexico |
| Baa1 | |
| Baa2 | South Africa, Italy |
| Baa3 | Turkey, Indonesia, India |
| Ba1 | Russia |
| Ba2 | Brazil |
| Ba3 | |
| Ba3 | |
| B1 | Angola |
| B2 | |
| B3 | Ecuador |

*Ratings on 5 July 2016. See 'Comparison of rating notation' table to compare Moody's notation with that of S&P and Fitch.*

### Comparison of rating notation

Fitch and S&P use the same notation for ratings above CCC. Moody's uses a different notation, but it can be directly mapped to the Fitch–S&P scale above the CCC range.

Ratings BBB-/Baa3 or higher are considered 'investment grade', while those below this level are considered 'sub-investment grade'.

Below the CCC, there are differences between the Fitch and S&P scales and neither can be directly mapped to the Moody's scale. The CCC range begins after the B-/B3 ratings and implies a very low level of creditworthiness, and, at its lower levels, actual default.

| Fitch and S&P | Moody's |
|---|---|
| AAA | Aaa |
| AA+ | Aa1 |
| AA | Aa2 |
| AA- | Aa3 |
| A+ | A1 |
| A | A2 |
| A- | A3 |
| BBB+ | Baa1 |
| BBB | Baa2 |
| BBB- | Baa3 |
| BB+ | Ba1 |
| BB | Ba2 |
| BB- | Ba3 |
| B+ | B1 |
| B | B2 |
| B- | B3 |

# Developing risk management, compliance and internal controls for a new era in banking: the example of BLOM Bank in Lebanon

Throughout the world, banks are upgrading their risk and compliance functions, and their internal controls, in response to regulatory pressures and in recognition of the new and changing risks that confront them. In Lebanon – a country that faces particular risks that go beyond those seen in most global banking environments – BLOM Bank has been taking a lead. *Arab Banker* spoke to Dr. Amine Awad, a former Executive Board Member of Lebanon's Banking Control Commission, who now advises BLOM Bank on Governance, Risk Management and Compliance.

**_ARAB BANKER_: How are the risk management and compliance functions structured at BLOM?**

DR. AMINE AWAD: Compliance is a major area of risk management – the cost of failing to identify the risk of non-compliance of a customer could be material and in some cases could become fatal to the bank. As a result, compliance issues have to be managed as effectively as any other risk in the bank's balance sheet.

However, due to the burden put on the 'compliance function', on one hand, and on other risk areas such as credit, market, liquidity, operational, legal, reputational, etc., BLOM Bank has decided to have two separate departments, one in charge of risk management and the other in charge of compliance.

Each one of these two departments has to identify the risks BLOM Bank is exposed to at the level of the Group as a whole and at the level of each entity of the Group, to measure these risks, to suggest the necessary procedures to avoid their occurrence, and to suggest the measures to be taken to mitigate their impact.

The Banking Control Commission of Lebanon (BCCL – the Lebanese banking supervisor) requires banks and financial institutions to have an independent risk management department reporting to the Board (Circular Nº 242, dated 30 June 2004). The Banque du Liban (BDL – the regulator) requires banks and financial institutions to have an independent legal compliance unit with at least two different units covering legal compliance and AML/CFT (Circular Nº 128, dated 12 January 2013).

Our risk management department is headed by Mr. Roy Rubeiz, Acting Group Chief Risk Officer, while the compliance department is headed by Mr. Malek Costa.

Each of these two departments reports to the Board through a specialised committee, the Board Risk Management Committee and the Board Compliance Committee. Both committees are chaired by a different independent non-executive board member with considerable expertise in the field.

Since my appointment at BLOM Bank in June 2015, as a Group Advisor, I have spent much of my time focusing on harmonising the procedures between the different entities of the BLOM Bank Group, especially in the GRC (Governance, Risk Management and Compliance) areas.

**How have the risk management and compliance functions changed in recent years?**

Risk management as well as compliance functions, like all other functions in the banking industry, are moving fast and are constantly evolving due to the ever-changing environment.

After having recourse to modellers to help the risk experts analysing credit and market risks, banks discovered that other risks can be more dangerous and require different approaches.

Following the recent international financial crisis, international regulators and standard setters highlighted the importance of new types of risks and of new ways to measure and manage these types of risks.

To give an example, the International Accounting Standards Board (IASB), after many years of conflicts with banking standard setters, mainly the Basel Committee for Banking Supervision (BCBS), accepted that banks should take preventive measures to manage their credit risk by adopting the concept of Expected Credit Loss (ECL) rather than only Incurred Loss, through the new IFRS 9, which is due to be fully implemented on 1 January 2018.

This new concept led many banks, including BLOM Bank, to hire new experts in actuarial science to help in calculating the lifetime ECL of impaired portfolios.

New staff members have also been hired to help understand the new AML/CFT concepts that are evolving so fast.

On the other hand, priorities within different risk segments are constantly changing.  Liquidity risk is now as important for banks as market risk. In compliance, fighting tax evasion is becoming as important as fighting illicit actions. In operational risk, IT security is also becoming a cornerstone in protecting bank transactions, etc....

**What are the biggest risk management challenges that Lebanese banks face, and how is BLOM in particular responding to those challenges?**

From my previous experience as a bank regulator, I would say that the biggest risk management challenge that Lebanese banks face is the forward-looking approach to risk management, especially the computation of the Expected Credit Loss on their portfolios. This is due to the fast–changing macro-economic environment, high exposure to sovereign credit risk, the high interconnectedness of the banking system, and political instability in the MENA region and its direct impact on Lebanon.

We at BLOM have decided to face this highly volatile environment by adopting a very conservative approach in our activities and this is done through several internal policies and limits that go far beyond the regulatory requirements.

To illustrate what I am saying, here are some examples:

- Internal limits (a floor) for the ratio of placements with foreign prime correspondents/total liquidity placements.
- Limits for sectorial concentration of loans (this ratio is constantly observed, in relation to macro-economic studies).
- Internal limit (a ceiling) for the loan/deposit (LTD) ratio, below the regulatory one.

**What are the biggest compliance challenges that Lebanese banks face, and how is BLOM in particular responding to those challenges?**

What I have seen in the last couple of years, not only in Lebanon but also worldwide, is that banks are suffering from large penalties imposed on them by tax authorities, due to some practices considered as facilitating tax evasion. (The 'Panama Papers' is the last episode that is expected to lead to large fines.) Other large banking conglomerates have been forced to pay huge amounts to some public authorities, because their financing transactions are thought to have helped sanctioned parties.

Lebanese banks are facing the same types of risks, with an increased exposure to some risks as a result of the direct presence that some of them have in countries where the government or some parties are under international sanctions, such as Syria, Iraq and Sudan.

BLOM Bank has an affiliate in Syria and branches in Baghdad and Erbil in Iraq. This presence puts a heavy burden not only on the management of the local entities, but also on the Group compliance department at the Head Office, to draft policies that strictly respect sanctions while trying not to kill the 'clean' business in these countries.

BLOM Bank, as all other Lebanese banks, has to abide by the law that was recently adopted in the US and known as 'Hizballah International Financing Prevention Act', while knowing that Hizballah is a party with a presence in Lebanon and part of the democratically elected parliament and government, and has social humanitarian activities.

The uncertainties arising from this US law have been resolved by BDL Circular Nº 137, dated 3 May 2016, and the Memo Nº 20, dated 26 May 2016, issued by the Special Investigation Commission (SIC – which is the Lebanese financial investigation unit). These documents were issued to clarify the contents of BDL Circular Nº 126, dated 5 April 2004, asking banks and FIs operating in Lebanon to adopt a risk-based approach and vet the identity of all their customers and economic beneficial owners, and to stay fully and permanently informed of the laws and regulations governing their correspondents worldwide and to deal with the latter, in conformity with the laws, regulations, procedures, sanctions and restrictions adopted by international organisations or the sovereign authorities in the correspondents' home countries.

**What is the role of BLOM's internal audit department in ensuring that the bank's risk management and compliance functions are operating effectively?**

BLOM Bank's management is increasingly relying on the internal audit department in its effort to manage fraud risk. The internal audit department works closely with the operational risk unit in the risk management department.

The ever-increasing regulations, the continuous geographical (local and international) expansion of BLOM Bank, in addition to the new products and services launched at a very speedy rhythm, exposed the bank to greater financial, compliance and reputational risks.

The internal audit department has, as a main objective, a systematic appraisal of operations and controls within the bank, to determine whether the reported information is reliable and accurate and whether the risks BLOM Bank is exposed to are clearly identified and well managed and whether regulations and internal procedures and policies are followed, and, finally, whether the bank's resources are used in an efficient and economic way. Internal audit missions always lead to drafting reports that relate the observed facts and suggest corrective actions.

This new approach was adopted recently by the Board of Directors of BLOM Bank to complement the traditional role of the internal audit department in ensuring an efficient application of the bank's policies and procedures.

In consequence, the scope of work of the international audit department is widening more and more, and includes concepts newly introduced by the regulators in Lebanon such as 'consumer protection' practices, and 'market conduct'.

**What advice would you give to Arab banks that want to strengthen their own risk, compliance and internal audit functions?**

Based on the events that have happened in recent years and the unstable geopolitical environment in the Arab world, my advice to the banks in our region can be summarised as follows:

- Give as much attention to the control functions as you do to the operation functions; each area complements the other.
- Build buffers to face unpredictable situations by keeping a good balance between building up reserves and distributing dividends.
- Be proactive in taking corrective actions every time a warning is issued by the bank's controls.
- Be preventive by installing early warning systems that help detect anomalies at an early stage.
- Finally, co-operate closely with your regulators and supervisors to ensure smooth implementation of international standards and regulations. ■

# US law enforcement and Arab banks: moving beyond Iran sanctions

With nearly a year passed since the landmark deal to end nuclear-related sanctions on Iran, Arab banks are now weighing their options for engaging in business with Iran or in processing Iran-related transactions. Of course, many challenges remain in doing this, but over time business with Iran should normalise to a significant degree for non-US banks.

But this does not mean that Arab banks no longer face risks from US law enforcement agencies. In fact, US enforcement agencies have been emboldened by the way in which economic sanctions and anti-corruption laws have succeeded in changing the behaviour of non-US banks and companies.

In the following article, James Campbell and Stephen Huttler, both partners in Pillsbury Winthrop Shaw Pittman, the international law firm, describe US plans to pursue those they suspect of facilitating tax evasion or money laundering overseas.

It is well known that many citizens seek to avoid paying taxes. To mask the amount and source of funds, many citizens use non-US banks, and especially those based in jurisdictions with a reputation for banking secrecy and client confidentiality.

One of the jurisdictions that used to be favoured by those seeking to avoid tax was Switzerland. However, as a result of recent action by the US Department of Justice (DOJ), many Swiss banks have made settlements with the US authorities and provided information about their US customers.

Following on from their success in Switzerland, we expect the DOJ to turn its sights to other locations, many of them in the Arab world. As a result, it is important for Arab banks to understand what the DOJ did in Switzerland.

On 29 August 2013, the DOJ and the Swiss Federal Department of Finance announced the 'Program for Non-Prosecution Agreements or Non-Target Letters for Swiss Banks' (the 'Program'). Under the Program, the DOJ held out an offer of non-prosecution agreements (NPA) concerning potential tax-related offences under US law to Swiss banks that made broad disclosures about their US banking practices and their related account holders.

Among the disclosures the DOJ required under the Program was information concerning

a) accounts in which US taxpayers held an interest,
b) potential misconduct by bank employees and executives, including cross-border activities,
c) names of banks outside of Switzerland to which money was transferred when US-related accounts were closed.

The DOJ required each bank participating in the Program to pay a penalty based upon a percentage of the amount of assets under management for US taxpayer accounts, though such penalties could be reduced if the bank provided mitigating evidence. 'Mitigating evidence' could include, for example, evidence that an account had been declared to US authorities via timely reporting by the taxpayer or through the taxpayer's participation in a voluntary disclosure programme encouraged by the bank.

On 27 January 2016, the DOJ announced that it had signed an NPA with the final participating Swiss bank. In total, 80 Swiss banks participated in the Program, paying an aggregate penalty of $1.36 billion (with individual penalties as high as

$211 million and $188 million). Through the Program, the DOJ acquired a wealth of information about offshore accounts and their use by US taxpayers as vehicles for tax evasion. This information – particularly when aggregated across the 80 participating Swiss banks – gives the DOJ clear indications about which banks to pursue for potential tax-related offences outside Switzerland.

Although the DOJ has remained silent about the next jurisdiction to which it will offer a programme similar to the Swiss Bank programme, Acting Assistant Attorney General Caroline Ciraolo indicated in early 2016 that the DOJ will continue pursuing investigations beyond Switzerland and warned institutions that have facilitated account concealment and tax evasion to anticipate DOJ investigations. She encouraged such institutions to voluntarily disclose criminal activity before the DOJ begins its investigations.

Banks in the Middle East are increasingly viewed as potential targets for DOJ investigations concerning tax evasion and account concealment by US taxpayers. Similar to Switzerland, many Middle Eastern countries – including the UAE, Qatar, Oman, Kuwait, Bahrain and Saudi Arabia – levy income and other taxes at a low to non-existent rate on foreigners. These tax-convenient locations attract US taxpayers who wish to avoid paying US taxes on their worldwide income. In addition, banks in two Middle Eastern countries – Lebanon and Bahrain – offer services with a high level of secrecy, with the result that foreign governments are thwarted from scrutinising transactions and identifying account holders.

Moreover, many Swiss banks that participated in the Program are linked to affiliate banks in the Middle East. Their disclosures gave the DOJ immediate access to relevant information about those affiliates and may have exposed practices that will require a formal investigation by the DOJ. The recent disclosures of the 'Panama Papers' have similarly delivered to the DOJ a treasure trove of information about possible tax evaders and their affiliates. This includes information identifying shell companies or other entities used to obscure the nature, source and ownership of funds.

Banks in the Middle East should therefore anticipate increased scrutiny by US authorities relating to account concealment and tax evasion by US taxpayers.

## Increased focus on money laundering

Similarly, Arab banks should also expect an increase in anti-money laundering (AML) activity by the US authorities, including the exercise of the DOJ's international capabilities.

In recent years, many foreign banks with branches in the US have come under investigation by the DOJ for allegedly evading sanctions requirements, or even for facilitating the laundering of illicit proceeds. Some of these investigations have resulted in astronomical fines and serious reputational damage.

Foreign banks that do not have a branch in the US may still be exposed to US jurisdiction through their correspondent banking relationships. As a result, in the present environment, US financial institutions are likely to require assurances from foreign banks that they have sufficient AML controls to detect potential illicit activity. To the extent that foreign banks cannot give such assurances, many US banks will simply choose to 'de-risk' and not transact business in certain jurisdictions.

Importantly, money laundering statutes in the United States expressly provide for extra-territorial applicability over conduct covered by the statute if the conduct is by a US citizen or, in the case of a non-US citizen, if the conduct occurs in part in the US and the value of the funds involved exceeds $10,000.

In practice, any evidence that the money originated in, ultimately returned to, or passed through the US is sufficient for jurisdiction in the US. Money laundering necessarily involves financial transactions using funds generated by a 'specified unlawful activity', to (i) promote additional specified unlawful activity, (ii) conceal the nature, source or ownership of the funds, (iii) evade state or federal reporting requirements, or (iv) evade taxes on the income produced by the specified unlawful activity. The term 'specified unlawful activity' includes a very long list of state, federal and foreign crimes, including bribery violations of the Foreign Corrupt Practices Act (FCPA).

It is also worth noting that the FCPA, which, among other things, criminalises the bribery of non-US government officials, remains a priority of the DOJ. As investigations of potential corruption increase, there will be more focus on 'following the money', thus implicating financial institutions with deficient AML controls.

We therefore counsel banks to ensure that their AML controls meet the highest global standards if they clear dollar transactions, even if they have no presence in the US. We also encourage them to engage with US regulators and policymakers to understand the growing implications of the extra-territorial impact of the DOJ on their business. ■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**Pillsbury** is a full-service law firm with an industry focus on energy and natural resources, financial services including financial institutions, real estate and construction, and technology. Based in the world's major financial, technology and energy centres, Pillsbury counsels clients on global business, regulatory and litigation matters. The needs of Pillsbury's clients are often international in scope and, to meet those needs, Pillsbury operates a fully integrated network of 19 offices worldwide that advises clients doing business around the globe. www.pillsburylaw.com

# No end in sight for the decline in correspondent banking relationships

De-risking has become one of the hottest issues in international banking. Big international banks are cutting back on the services that they offer to smaller banks overseas, and in emerging markets those smaller banks are complaining that reduced access to international finance is compromising economic growth and pushing some of their customers to use informal and unregulated financial services.

International bodies such as the World Bank and the Financial Stability Board have recognised that there is a problem and have responded by publishing reports and statistics. Standard setters and regulators have issued guidance that they hope will slow the decline in cross-border banking activity.

*Arab Banker*'s Editor, Andrew Cunningham, considers what 'de-risking' means in practice, and asks what emerging market banks can do to maintain access to international financial services.

In 2015, the World Bank asked big international banks, emerging market banks and bank regulators to describe the changes they were seeing in the correspondent banking market. Their responses confirmed what emerging market banks had been saying, and large international banks shyly admitting, for some time: there had been a huge decline in the availability of international correspondent banking relationships (CBRs) during the previous three years.

Sixty per cent of the 170 local or regional banks that responded to the World Bank's questionnaire said that they had witnessed a decline in CBRs. Seventy-five per cent of large international banks that responded said that they had reduced the number of correspondents to whom they offered banking services.

The World Bank also surveyed banking authorities. One hundred and ten responded, and half of these confirmed that they were seeing a decline in CBRs in their jurisdictions.

The World Bank report identifies international wire transfers as the service most significantly affected as large banks reduce their CBRs. Wire transfers denominated in US dollars are particularly heavily affected. Next in line were clearing and settlement services and cheque clearing services, followed by trade finance and cash management.

US banks were most frequently cited as those that are reducing CBRs, followed by British banks.

The dangers presented by this trend go beyond the inability of some regional banks to fulfil the needs of their clients. As the World Bank points out, as international banks end their relationships with higher risk customers (or those perceived to be higher risk) the system as a whole pushes that risk into less transparent channels with the result that risk within the system actually increases.

This is particularly true in the field of remittances. As regional and local banks lose access to international financial networks, their customers may start to rely on informal payment channels. Having worked hard to bring money exchange firms, including the 'hawala' networks in the Middle East, into the formal, regulated banking system, international standard setters may find that they are unwittingly incentivising millions of expatriate workers to find remittance arrangements outside the regulatory framework.

When challenged on their reasons for reducing CBRs, the large international banks generally cite supervisors' heightened expectations for due diligence and compliance, and in particular the large fines handed out by supervisors for failure to comply with sanctions and anti-money laundering regulations.

The large enforcement actions are well known, such as the $8.9bn fine levied on BNP Paribas by the US authorities in 2014 in respect of violations of economic sanctions, and the $1.9bn payment levied from HSBC in 2012 as part of a settlement related to alleged money laundering through the bank's branches in Mexico.

But enforcement actions have not been confined to large western banks. In 2015, the British regulator fined the Indonesian company Bumi for weak internal controls, and it fined Bank of Beirut for failures in its compliance and internal audit functions. Also in 2015, the US authorities took action against China Construction Banking Corporation for deficiencies in its anti-money laundering programme.

It is important to recognise that the decline in correspondent banking is rooted in a wide variety of factors that extend beyond rules on money laundering and the financing of terrorism (ML/FT) and it precedes the current era of large regulatory fines.

In 2014, the *Economist* reported that the number of CBRs in the eurozone had fallen by nearly 30% between 2003 and 2010 and that the principal driver of this trend was consolidation in the banking industry.

But the decline in CBRs accelerated rapidly after 2010, falling by about another 20% in the next two years, the *Economist* said.

This accelerated decline has been driven by two factors. The first is indeed the fear of regulatory sanctions, but the second relates to broader economic and financial factors that include bank consolidation, but also arise from new regulations on bank capital and liquidity.

The Basel III capital standards, first announced in 2010 and still in the process of implementation, require banks to hold more capital than in the past, particularly against riskier assets. These higher capital requirements are squeezing risk-adjusted profitability, forcing banks to think more carefully about the value of the services that they provide.

In the case of the Middle East, there is an additional factor. The fall in oil prices since 2014 has reduced liquidity in the Gulf States and in other oil exporting countries. Banks in these countries were often happy to pay a small fee to international banks to keep correspondent banking lines open, even if they never expected to use them. But as liquidity contracted, some of these banks began to draw on their lines, forcing international banks to consider the importance of their relationships with smaller banks in smaller economies and the value of the fees that they had been receiving.

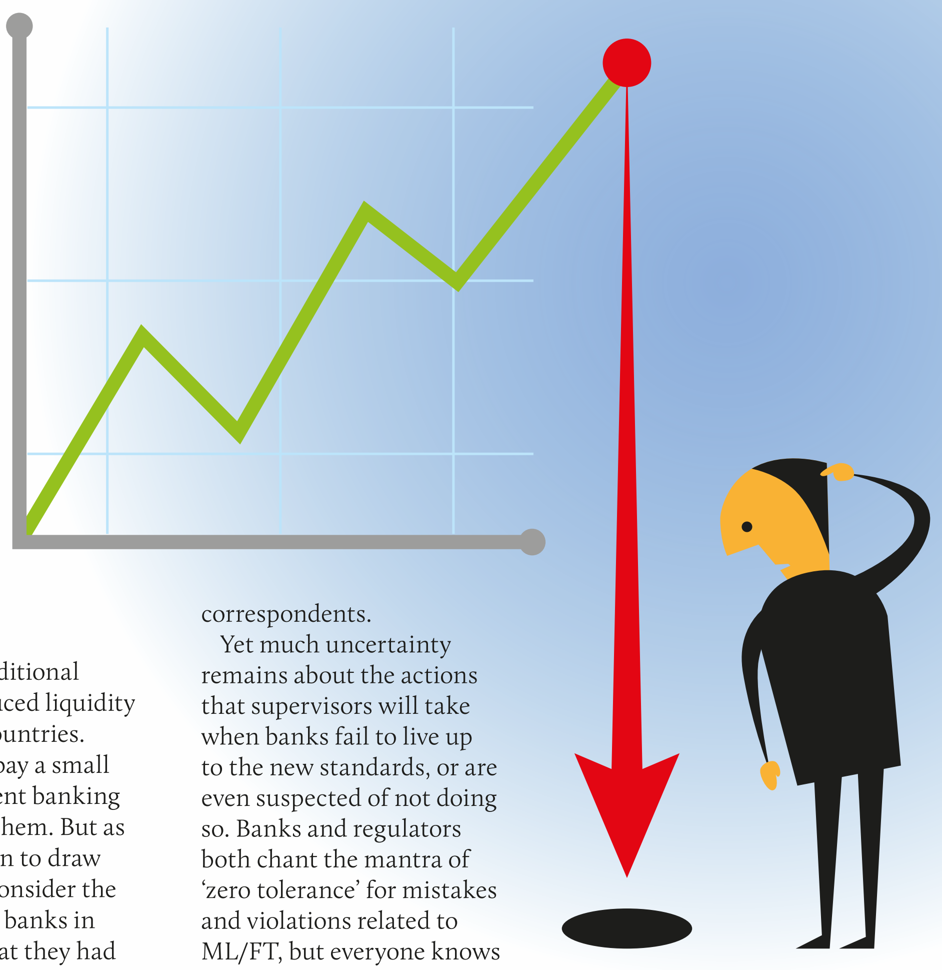
If current regulatory expectations on due diligence lead to the bank having to send staff half-way round the world, on business class flights, to conduct annual reviews of correspondent banks, profits on CBRs can disappear very quickly.

This problem is compounded by the introduction of the Net Stable Funding Ratio, the new Basel liquidity standard that limits banks' ability to fund long-term assets with short-term liabilities, and also takes account of foreign currency mismatches within the asset/liability structure. In simple terms, if a eurozone bank is going to extend lines in dollars (for example to a bank in the GCC), then there is greater pressure than before to fund that line with dollars rather than with euros.

Nonetheless, discussions about CBRs and de-risking inevitably return to issues of compliance and to fears that banks may unwittingly offer services to others who engage in criminal activity, or whose customers engage in criminal activity.

New standards on capital and liquidity may be pressurising banks' profits, but the challenge is not new and, more importantly, capital and liquidity ratios can be controlled and managed by the banks themselves. In contrast, compliance risk has been transformed in recent years as a result of new standards and huge changes in regulators' expectations.

There is no shortage of guidance for banks on how to manage CBRs and specific risks related to ML/FT. For example, guidelines published by the Basel Committee on Banking Supervision in February 2016 include specific recommendations related to account opening and the information that should be gathered by a bank on its correspondents.



Yet much uncertainty remains about the actions that supervisors will take when banks fail to live up to the new standards, or are even suspected of not doing so. Banks and regulators both chant the mantra of 'zero tolerance' for mistakes and violations related to ML/FT, but everyone knows that you cannot run a commercial business if every possibility of making a mistake has to be excluded.

Until the supervisory responses to mistakes and violations become more predictable, we are unlikely to see a revival of international correspondent banking. ■

**Key documents on de-risking and the decline in correspondent banking***

*Withdrawal from Correspondent Banking: Where, Why and What to Do About it*. World Bank, November 2015.

*Report to the G20 on Actions Taken to Assess and Address the Decline in Correspondent Banking*. Financial Stability Board, November 2015.

*Effective Supervision and Enforcement by AML/CFT Supervisors of the Financial Sector and Law Enforcement*. Financial Action Task Force (FATF), October 2015.

*Sound Management of Risks Related to Money Laundering and Financing of Terrorism*. Basel Committee on Banking Supervision, February 2016.

*Consultative Paper on Correspondent Banking*. Committee on Payments and Market Infrastructures, October 2015.

* These documents contain references to numerous other recent reports and studies relevant to correspondent banking, AML/CFT and, more broadly, compliance and internal controls in banks.

# The long-term role of crude oil in the global energy mix: an interview with Dr. Carole Nakhlé

In the Middle East, discussions about energy tend to focus on the price of oil and the future of OPEC. That is hardly surprising given the dependence of so many of the region's biggest economies on revenues from oil exports, and the vulnerability that some of the region's importers have to high oil prices.

But the global energy market is much larger and more complex than the market for crude oil. In fact, crude oil accounts for only 30% of total energy consumption worldwide.

To understand how the global energy market is changing, and how these changes might affect the Middle East, *Arab Banker* spoke to Dr. Carole Nakhlé, the Founder of Crystol Energy and an advisor to governments and private sector companies on global energy trends.

***ARAB BANKER*: What long-term trends do you see in global energy usage, both looking back to the past, and forecasting what may happen in future?**

DR. CAROLE NAKHLÉ: For most of the last 100 years, there was always one dominant fuel used as a source of energy: coal replaced biomass (mainly firewood), and then was itself replaced by oil. But since the first oil crisis in the early 1970s when oil became an expensive source of energy, several other sources have developed, such as gas, nuclear power and renewables, such as hydropower, biofuels, and solar and wind power.

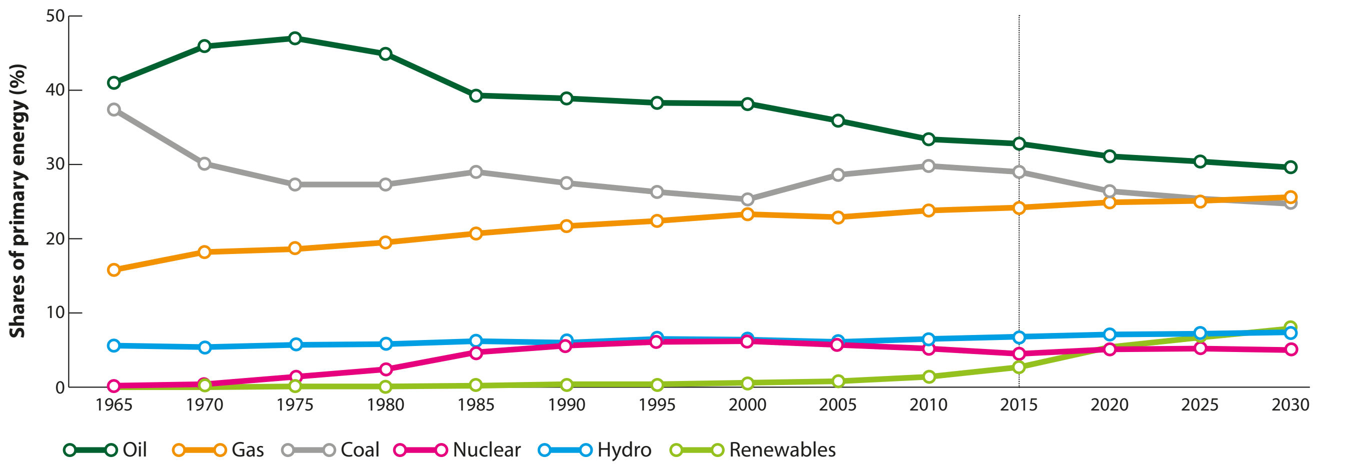
We are currently living with a much more diverse energy mix than at any time in the past. Oil will continue to dominate the transport sector, and coal will remain important in China and India. Gas is becoming more plentiful, easier to use, and easier to trade. Oil, coal and gas will likely have roughly equal shares of the global energy mix in the years ahead.

Nuclear energy's contribution is unlikely to play a major role as its expansion will be constrained by various economic, political, and environmental issues among others. Renewables, mainly solar and wind, will maintain their rapid growth but we should take into consideration that they are starting from a low base.

**Why won't renewable energy have a bigger share, given all the attention that it is receiving these days?**

There is a limit to how far you can expand hydroelectric power. Simply put, you can't block up every river in the world to build a dam. As for biofuels, there is a balance to be struck between using land and crops to create energy or using them to grow food. There is a choice, and in many countries, the

**Shares of primary energy**




*Source: BP Statistical Review 2015, BP Energy Outlook 2016*

Petrofac hosted a roundtable dinner for Women in Energy entitled 'Iran: Winners and Losers'. The dinner was held at London's Caledonian Club.

## Providing access for Women in Energy

Women in Energy is a not-for-profit organisation founded by Carole Nakhlé in 2007 to encourage and help women to reach senior positions in the energy industry.

The group provides advice and networking opportunities for women working in the energy business. Its membership is diverse: it includes accomplished women and experienced professionals who hold senior positions in private sector firms or in the public sector and graduates keen to develop knowledge of global energy markets and extend the range of their personal contacts. The group publishes a regular newsletter and organises events for its members.

Women in Energy works closely with the Windsor Energy Group, a not-for-profit organisation chaired by Lord Howell of Guildford, that arranges high-level roundtables on current energy issues for both public and private sector executives.

The London firm MEC International acts as a Secretariat for Women in Energy and may be contacted at projects@meconsult.co.uk. More information on Women in Energy can be seen on the Crystol Energy website: www.crystolenergy.com

sensible choice will continue to be to grow crops for food not fuel.

As for other 'green' sources of energy, what we see is that every time the nuclear industry seems ready to take off, there is an accident: those at Chernobyl in 1986 and Fukushima in 2011 are the best known but there have been several other smaller nuclear accidents. Following these accidents, the commissioning of new nuclear power plants is delayed. Remember too that nuclear power plants have a limited life, so while some new plants are being commissioned, others are being de-commissioned, or are about to be de-commissioned – the net new availability of nuclear energy is therefore not substantial. So, I don't expect nuclear power to play a big role in the global energy mix at least in the two decades to come.

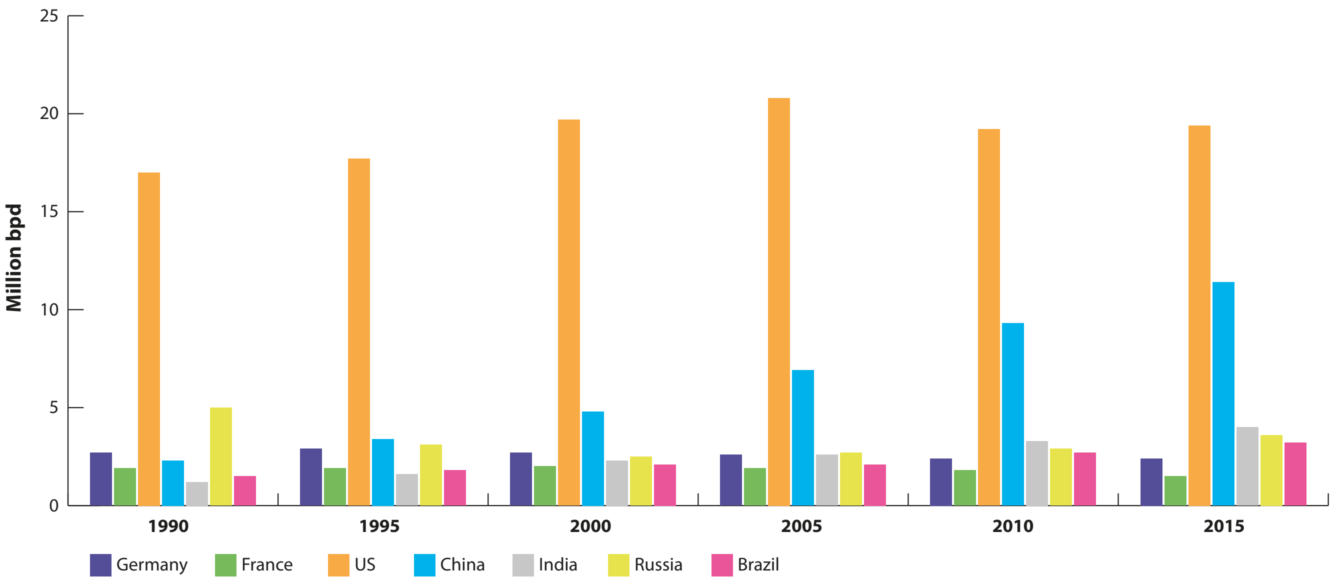
### How will political pressures and the climate change agenda affect the types of energy we use over the long term?

Historically, we have focused on the price and availability of energy, whereas now we also need to consider the climate change agenda. Its impact will be gradual, but it will be important.

In June 2015, the G7 group of leading industrial nations agreed to end using fossil fuels by the end of this century. That is going to put downward pressure on the use of coal, oil and gas, regardless of their cost and availability.

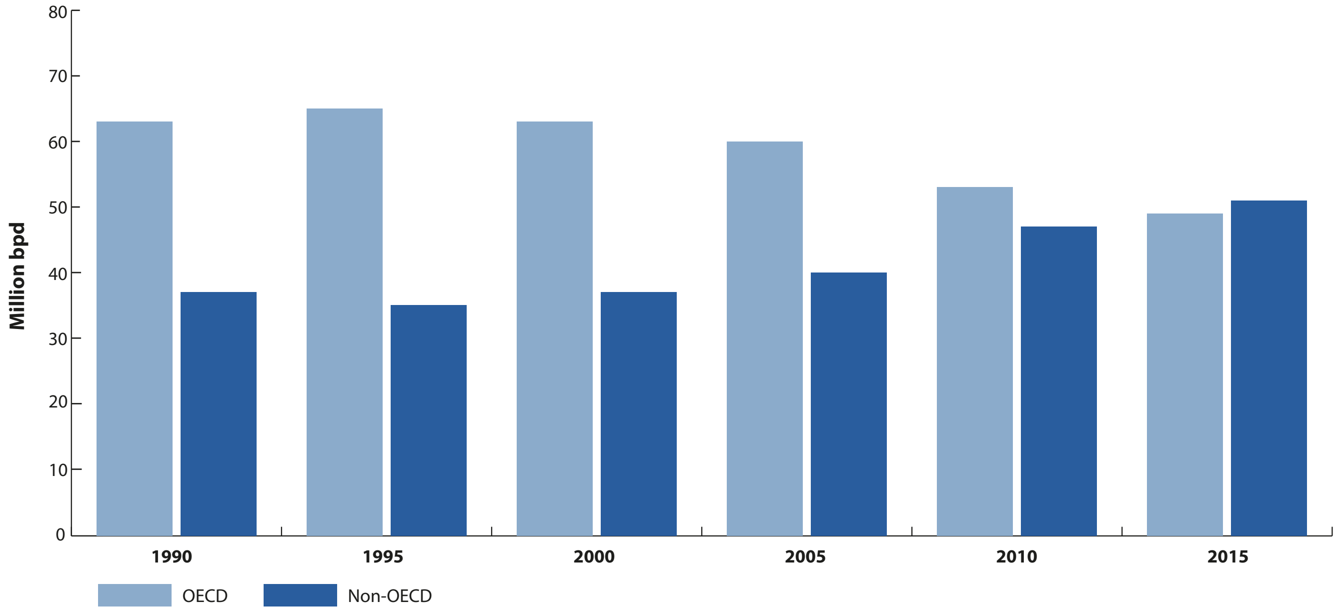
But we do need to keep a sense of proportion. For example, everyone is very excited about electric cars, and they certainly will become a significant feature on our roads. But the growth of electric cars is starting from a very low baseline, and of course ships and airplanes are going to continue using oil-based fuels for the foreseeable future.

## Crude oil demand in major economies




*Source: BP Statistical Review 2015, IEA May 2016 Monthly Report*

**Shares of primary energy demand**




*Source: BP Statistical Review 2015, IEA May 2016 Monthly Report*

## How is the gas market changing?

The percentage of gas that is traded remains low – around 30% of total supply. That percentage is increasing, with larger amounts of liquefied natural gas (LNG) linking various markets.

The way in which gas is bought and sold is very different from the way in which oil is traded. But currently the price of a significant proportion of traded gas remains linked to the price of oil. This system of indexation was developed in the early days of the development of the gas industry in the 1970s/80s when gas exporters needed a pricing mechanism that would make gas competitive with other existing fuels, mainly oil. But indexation no longer reflects the economic realities of either the gas market or the oil market. As a result, half of the gas market is always unhappy – they are either paying too much or receiving too little!

That is why LNG and gas is increasingly being traded 'spot' rather than through long-term contracts based on oil indexation.

Gas remains a fossil fuel. It may be a cleaner fossil fuel than coal or oil but it is still targeted by the G7 ambition to end fossil fuel usage by the end of the century.

Putting all that together, I see gas as a 'bridge fuel' that will be important as we transition from overwhelming dependence on coal and oil to greater reliance on renewable greener energy.

## Which countries are going to be the main suppliers of global oil in the years ahead?

The big three oil suppliers are currently Russia, the US and Saudi Arabia. They are likely to remain so for the years ahead. But we should not discount other countries like Canada that continues to expand its oil output, and China.

Other countries and regions still surprise. Oil production from the North Sea, for instance, showed a reversal in decline for the first time in two decades. New fields continue to be discovered and developed. The Johan Sverdrup Field, discovered in 2010, is one of the five biggest oilfields on the Norwegian continental shelf. Its production is expected to start in 2019 and extend well beyond 2050.

Venezuela has proven that the availability of resources in the ground does not dictate production levels or trends. Venezuela not Saudi Arabia has the largest proven oil reserves in the world. That is because the very heavy crude oil in the country's Orinoco Oil Belt was not previously considered commercial, but with the development in oilfield technology, such a heavy oil is now classed as 'conventional' oil. Yet, because of erratic government policies, Venezuela's oil production does not reflect its potential.

## Isn't shale oil revolutionising the global energy supply market?

If you mean bringing in new suppliers – not really because shale production, which started first with gas then extended to oil, did not create any new oil producers; it simply expanded the capacity of existing producers and, in particular, arrested the decline in US oil production.

In terms of changing the existing oil order, yes – think of the stability in the oil price between 2010 and 2013 then the decline in summer 2014 and the implications on OPEC's strategy.

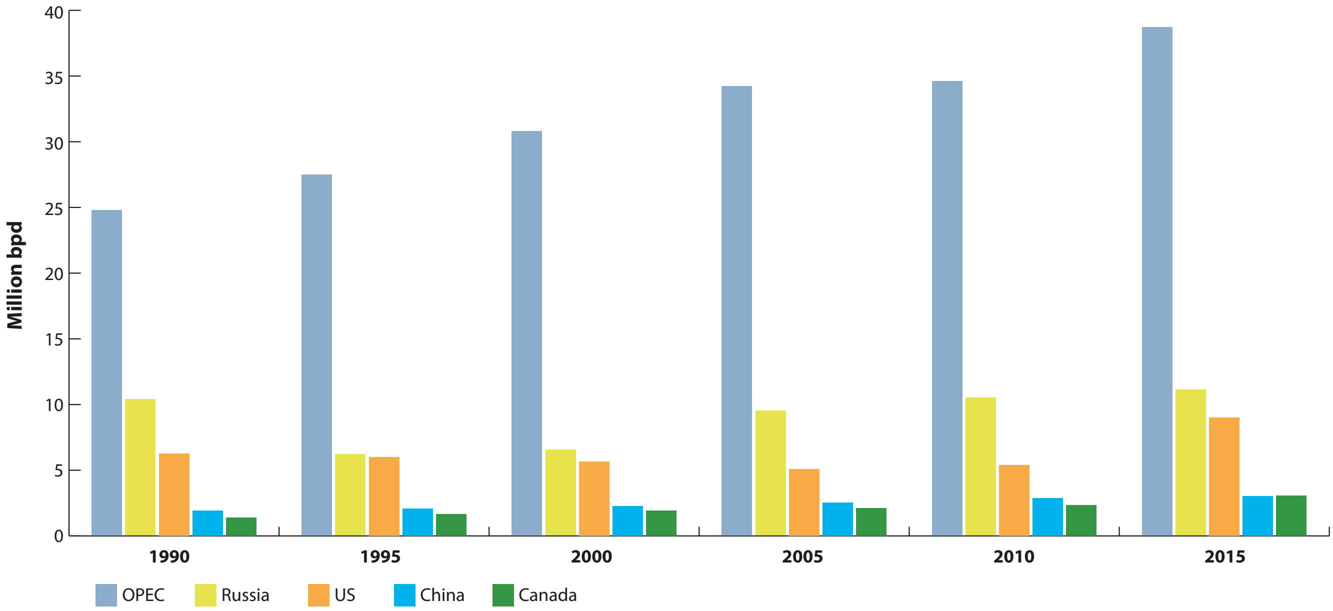
In the longer term, of course new shale producers are expected to emerge but perhaps not on the same scale or at least not at the same speed as in the US which has a unique combination of favourable above ground factors whether in terms of regulations, level of competition, availability of infrastructure or others.

## What about the 'demand' side of global energy? How is that going to change in the decades ahead?

Developed countries remain major energy consumers – they consume nearly 50% of global crude oil support – although their demand for energy is barely growing.

The rapid growth in energy demand is being driven by developing countries, and it will continue to be driven by them.

**Largest crude oil producers, 1990–2015**




*Source: IEA Monthly Reports*

China, of course, continues to use more and more energy even though its rate of economic growth is slowing: the economy is still growing, but at a slower rate than before, not surprisingly given the economic rebalancing. And China's energy mix is changing accordingly, with gas becoming increasingly popular.

India is the 'wild card' in global energy demand. India is expected to have a bigger population than China within the next few years and its demand for energy is going to be substantial, other things being equal. Some of the big questions are around India's energy efficiency. Industrial processes are now more efficient, so we shouldn't expect India's energy consumption to exactly replicate the Chinese energy consumption experience. Nonetheless, increasing energy demand from India will be one of the key factors driving global energy demand in the years ahead.

### The US is much less dependent on the Middle East for its energy supplies than in the past. How do you think this is going to affect the way in which the US engages with the Middle East?

I don't subscribe to the view that because the US is less dependent on Middle East oil it is going to care less about what happens in the region. The oil market is global with prices based on global supply and demand so if, for example, there are significant supply disruptions in the Middle East these can translate into higher oil prices which in turn will affect the US economy, irrespective of how much oil the US is importing from Saudi Arabia or its neighbours.

Furthermore, look at the other, non-energy-related interests that the US has in the Middle East: its support for Israel, its fight against terrorism, and its recent diplomatic agreement with Iran, in addition to the investment of American companies in the region (in both oil and non-oil sectors). These issues will ensure that the Middle East remains important to US foreign policy interests.

### Is OPEC still relevant to the oil market?

We can stop thinking about OPEC when oil ceases to be an important part of the global energy supply mix. Until then, what OPEC does will continue to matter, albeit of varying degrees.

Current low oil prices have caused problems for many OPEC members, but they have succeeded in shutting down a lot of shale oil production and some of the more expensive conventional oil exploration projects – and that is very much in line with OPEC's interests: to limit future non-OPEC supply growth.

Historically, OPEC has not typically acted in a coherent manner, but it has been able to act cohesively at times. For example, in 2008 it agreed and implemented two cuts in its members' oil production and succeeded not only in ending a sharp fall in prices but also in pushing them back up to around $100/B. We certainly should not rule out the possibility that OPEC will act in a cohesive manner again in future. ■

**Dr. Carole Nakhlé**

Dr. Carole Nakhlé is the founder of Crystol Energy and an international expert in energy economics. She has worked for major oil and gas companies, such as ENI and Statoil, and for policy makers and international organisations.

She lectures in energy economics at the University of Surrey in the United Kingdom and has written for the Carnegie Middle East Centre and the Lebanese Centre for Policy Studies.

More information about Dr. Nakhlé and Crystol Energy is available at www.crystolenergy.com

# Learning from the past to build a more prosperous future: a discussion with Anthony Harris about political developments in the Middle East

For many in the Middle East, recent years have seen turmoil and bloodshed, while for others stability has been compromised by uncertainty and the need to adapt to changed economic and political conditions.

To understand the reasons behind what has been happening and the prospects for a more stable region in the years ahead, *Arab Banker* spoke to Anthony Harris, a former British diplomat and ambassador to the UAE who now lives in Dubai as the Senior Executive Officer in the Gulf for Robert Fleming Insurance Brokers.

***ARAB BANKER:* For the last five years, significant areas of the Middle East have been in turmoil and many others face uncertain futures. Are these problems likely to continue for the next five years?**

ANTHONY HARRIS: Today, the Middle East region is remarkable for its volatility and instability, yet when I first came to the region 50 years ago, it was possible to drive freely around the whole Middle East. I was fortunate to travel widely in the days when one simply collected the customs documentation for the Land Rover and headed off from London to Beirut, London to Khartoum, Istanbul to Beirut, or from Khartoum to Iran, to name just some of the journeys that I made in those early days. The fact that such journeys are now virtually impossible, even if one had an armoured vehicle, says a good deal about the region.

There are six states in the Arab world where the fabric of society has largely collapsed: Iraq, Syria, Yemen, Libya and the two Sudans. We must include non-Arab Somalia and Afghanistan as being similarly afflicted with instability. On top of these, we must mention Tunisia and Egypt, which are facing internal instability, and Lebanon and Jordan, which are suffering huge pressures from their immediate neighbours. To complete the picture, we must also mention Palestine, lest we forget the longest running problem in the region, which is still festering and which cannot be disassociated from many of the causes of instability.

How can this chaotic situation, which has developed so quickly, be explained? The trigger for much of the disruption was the US invasions of Afghanistan and Iraq, which were backed by several Western countries. More recently, Europe took the lead, but needed US support when, with no regard for recent history in the Arab region, France and Britain decided that regime change was required in Libya.

One could argue that problems would not have arisen if there had not been underlying discontent among the tribes and peoples, and bad governments promoting inequality, oppression and corruption. What the regimes of these collapsing countries failed to create, even where they ran stable governments, was solid institutions that were trusted, reliable and staffed with well-trained administrators, and that would therefore be able to outlast uprisings, regime changes and tribal conflicts. In most cases, the states concerned simply disintegrated into civil war, yielding power to men with guns and militias with pick-up trucks.

There is no easy formula for a solution. The West, which used to pontificate about democracy as a cure for all ills, has rightly grown more reticent in the past few years. Building new institutions takes years or even decades when most of the educated citizens are dead or have fled. Often the army is the only steady, solid part of the power structure, as in Egypt, but in Syria, Yemen and Iraq the original military forces have largely disintegrated.

Religious leaders can hold large groups together, but more often they are only interested in denigrating other sects or tribes, and in effect making matters worse: few of them have a broader vision of inclusive rule where other sects and minorities can find security and play their full part in society.

**Iraq has been experiencing some form of domestic conflict for more than 13 years now. Is there any realistic prospect for peace in Iraq in the medium term?**

Iraq is a particularly bad example of what happens when societies break down. It had been for millennia a country where a rich pattern of tribes and sects learned to live together. Baghdad has played a remarkable role in Arab history. The British thought that they knew how to manage the region, but their experiment was short-lived. They were eventually replaced by a regime that was vicious and tyrannical, but at least understood the complexities of the country, even if it cared little for its own people.

What we have now is a massive mess where, to take a recent example, the inhabitants of Fallujah, who have suffered several bloody battles over the past 25 years since the first Gulf War, have fled in their hundreds of thousands. After the Americans took over the city, following two vicious battles in the streets in 2004, there was a partial vacuum, which was filled in 2014 by ISIS. In the battles last summer, the Government retook parts of the city, but perhaps 80% of the population has fled in recent years, and the remainder seemed very reluctant to be liberated by the Iraqi Army or various Shia militias.

There is little prospect of peace in Iraq in the short or medium term. The political leaders in Baghdad have failed to inspire any loyalty among the Sunni population, many of whom seem to have decided to take their chance with ISIS rather than be a part of a state run from Baghdad. ISIS is now under pressure from many sides, and may be imploding in its turn, but the removal of ISIS from the north, if that happens, will not solve Iraq's problems.

The Americans have hitherto encouraged the Baghdad government to keep trying to unify the country and have spent billions of dollars propping up Haider Al-Abadi, the Prime Minister, hoping that successive elections would eventually include and protect minorities, and assist in pacifying the provinces. But Iraqi governments have in fact pursued a winner-takes-all policy, with the resulting alienation of the Sunnis, Kurds and other minority peoples.

**The Gulf States have successfully managed political succession in recent years, often with ageing rulers handing over power to sons and nephews who are younger and more technocratic; but is this leading to any change in the way politics is conducted in the region?**

The six GCC States have demonstrated that the old tried and tested ways of government in the region work well, and they have retained the support of their peoples. Younger leaders have been brought into the governments of all the GCC States in one way or another. For the Gulf ruling families, it is supremely important that, when necessary, power should pass to another member of the ruling family with minimal disruption and with broad support from the other key families. The stability of the Gulf States proves that they have got this largely right.

My impression is that Gulf Arabs have seen what instability has done to neighbouring states and they are shocked by what they see. So while Gulf Arabs accept that the world is changing fast, they want evolution not revolution and are grateful for the way that their leaders, and the prosperity created by the oil era, have brought them a better and stable life. Rapid change has taken place within a traditional framework, which suits the vast majority of Gulf Arabs.

The Gulf rulers have survived by staying in contact with their peoples and listening to their views. The majlis has traditionally been the key to Shaikhly rule, where the ruler sits regularly with his chief advisors, close family members and representatives of leading tribal groups and families. There has been a tendency in recent years for the mobile phone to replace the majlis, and for larger, more formal, bodies like parliaments and councils of ministers to manage the main business of the state. This is normal as states grow in size and complexity, but there still needs to be a flow of information and direct personal contact between the ruler and people.

There have been a few popular outbursts of anger, for example because of lack of employment in Oman, or social inequalities in Bahrain, but the ruling families have generally shown that they are aware of what their peoples are thinking and are making efforts to manage change.

**Do you think the Gulf Cooperation Council, as an institution, will become more or less relevant in the years ahead?**

Given the chaos on their borders, in Iraq, Syria and Yemen, the GCC leaders are well aware that they need to stick together and face common threats to their stability. We have recently seen how Riyadh and Abu Dhabi have cooperated over the situation in Yemen, and whatever the rights and wrongs of waging war on the Houthis, the leaders of the two states have seen Yemen as a common threat and are now engaged in the UN-backed peace conference with the Yemenis in Kuwait. The GCC States have also tried to find a common policy on the other main regional issues, like Syria and Iraq, and the perceived threat from Iran. Not all GCC States see eye to eye on all issues, but there has recently been a major effort to coordinate policy in many areas, especially in security and defence.

While the various ruling families retain some suspicions of each other – the smaller states tend to be reluctant to let the Saudis dominate in every area – and resent any interference in their affairs from whatever source, there is a growing awareness that with so many storms washing up on their shores, they need to coordinate for their own stability and security. The GCC will therefore be compelled to collaborate more closely in the future. Over time the GCC will evolve better institutions and find ways to work together more closely.

**In April, the Saudi Deputy Crown Prince launched Vision 2030 – an ambitious plan to reduce Saudi dependence on oil and develop civil society. How realistic is the Vision?**

There has been a great deal of international scepticism about Vision 2030 and the ambitions of the Deputy Crown Prince, Muhammad bin Salman bin Abdul Aziz (MBS) to modernise the Saudi economy. However, it is clear that Saudi Arabia must change as the world around it changes, and in particular the Kingdom must adapt to lower oil prices, which seem to be anchored around $50 per barrel. Even if the oil price rises, there is a huge volume of production in other parts of the world that can be brought on-stream, and there are many forms of renewable energy under development, and this would create downward pressure on prices again. The Saudi Government cannot therefore simply rely on prices rising to where they were before 2014: that may never happen.

So the question is not whether Saudi Arabia can change: the Kingdom has no choice. MBS has a big advantage: he is in his early thirties and therefore nearer the age of the majority of the country. Sixty percent or more of Saudis are younger than MBS, and he can therefore talk to his countrymen with added authority. Such criticisms as are sometimes reported in the Western press about the new Deputy Crown Prince probably originate from older, more conservative, princes who see their chance of power and influence slipping away.

It is hard to see how Saudi Arabia can quickly move away from its present habits: Saudi society is built on doing everything slowly and only introducing change after extensive consultation and balancing of interests among the ruling groups, religious and secular. Yet governing any country is a question of managing change. The speed of change in the Kingdom is accelerating. Young Saudis must be given skills that are relevant in the modern world, and must be taught the importance of a work ethic which will enable them to compete.

Millions of young educated Saudi women also want to be included in the workforce, which is necessary for the Kingdom's economic development, but this puts added pressure on the government when millions of young men cannot find jobs either.

**What are Iran's objectives in Syria, Iraq and Yemen, and more broadly in the Middle East?**

Iran believes that it has suffered a bad deal in recent years. It is a proud country with a long history, and one, it must be admitted, that does not have a particularly high regard for Arabs. The struggle to find common ground with the Arab states of the region and the rest of the world and to end the UN sanctions regime has been a long one. Even now, US trade restrictions on Iran, known as 'primary sanctions', remain in force.

Given that the Iranian regime, in common with any other regime, wants to stay in power, the current government has only crept slowly towards an accommodation with the West. It has, however, done what the IAEA has required of it, and trade with Iran is slowly resuming. Despite the impossibility of transacting in dollars, thanks to primary sanctions, the Boeing Aircraft Company is concluding negotiations with the Iranians to sell them 100 aircraft and the US Secretary of State has called on the international banks to find a way of trading with Iran, so trade with Iran might be starting to open up.

This drive to find a way to deal normally with Iran, which was once the West's largest trading partner in the region, has coincided with an outburst of Saudi suspicion of Iran and the West. The Kingdom is going through a period of hostility to Shia Islam and fears that its own economy will suffer if Iran is again allowed to trade freely with the rest of the world, and in particular, export its oil. In Saudi eyes, the increase in Iranian oil exports is contributing to the depressed oil price.

In short, Iran wants to be left alone to act as it sees fit and not be pushed around by the West or anyone else. This has coincided with the Saudis feeling particularly misunderstood and hoping to convince the Americans and others that they and the other GCC States face real threats. The rest of the world is not convinced of the Saudi case and is urging them to come to terms with their neighbours across the Gulf.

Several of the Gulf States have long had close trading links with Iran. Dubai and the smaller emirates in particular have traditionally been close to Iran. In recent years, mainly because of sanctions, ties with Iran have grown weaker, and the amount of trade flowing from Dubai to Iran has fallen to a fraction, but large numbers of Iranians still have businesses and investments in the northern emirates. Dubai was until seven years ago, when the last round of sanctions largely closed the doors, the largest Gulf port through which Iranian imports and non-oil exports passed.

The current period of poor relations have been caused by the sanctions regime, and in particular by Dubai being forced to stop trading across the Gulf, and by Saudi nervousness, which Abu Dhabi shares, that Iran is provoking a rise in Shia influence in the region. Other Gulf States like Oman and Qatar have been less vocal, and though they have been prevented from trading with Iran, they have managed to keep up a dialogue. Oman in particular has acted as a private channel for negotiations over the past year with Tehran.

Relations with Iran should, barring accidents, quietly improve as trade ties resume and banks begin normal business again. As power passes to a younger generation of rulers in Saudi Arabia we should see growing confidence on the Arab side of the Gulf and a greater willingness to settle regional differences through direct contact with Tehran.

**Are you generally optimistic or generally pessimistic about the prospects for peace and prosperity in the Middle East in the years ahead?**

I am pessimistic about prospects for a quick return to peace and prosperity in the region. Some states like Syria, Iraq, Yemen and Libya have descended into chaos. Some international borders have been dismantled, huge populations dispersed and many towns destroyed. Vicious militia gangs roam the landscape. Ancient communities have been wiped out or driven into exile. In these countries, it will take a decade of peace for communities to be resettled, refugees to begin returning, and the infrastructure of the countries rebuilt.

The problem is that no clear way can be seen for this to happen. It was a Western illusion before the invasion of Iraq in 2003 that democracy would enable Arab states to be run in a more just and efficient manner and protect minorities. Most Western countries no longer think that they have the answers, at least in the next few decades, nor believe that they have a formula which will help Arab societies to begin the process of reconstruction.

The key problem is that few Arab states, except the GCC countries, have developed institutions which are solidly based and trusted by their peoples, and which can withstand civil unrest. When times are hard, Arabs retreat into their families and tribes, and their religious sects. These do not provide solid forms of government: institutions dissolve when Sunni turns against Shia, as happened in Iraq, or when tribes turn against each other, as in Syria, Libya and Yemen. The Arabs must find their own solution if the flood of refugees pouring into neighbouring countries, and into Europe, is to be reversed. It will be hard to resist interfering when there are cries of help from the region, and more mass migrations, but the history of the past few years shows that foreign interference can have even more catastrophic effects. Finding ways of helping without interfering will be the task of the next generation of Western politicians and diplomats. ■

**Anthony Harris**

Anthony Harris spent 34 years as a British diplomat, mainly in the Arab world. In 1994 he was appointed Ambassador to the UAE. Other postings included Lebanon, Sudan, Saudi Arabia and Egypt. He has lived in Dubai since 2000, and is currently Senior Executive Officer of Robert Fleming Insurance Brokers (RFIB) and was General Manager of RFIB Saudi Arabia from 2011 to 2014. He also acts as a senior consultant to Al Shafie Miles, the Cairo-based political risk consultancy.

# Managing Chinese banks in the 21st century

Chinese banks are among the biggest in the world, they are well managed and they are expanding overseas. But what do we know about the people who are managing these banks? Not much.

Stephen Timewell has been visiting Chinese banks and calling on their most senior executives for 25 years. In the following article, he identifies some of the leading figures in Chinese banking, and describes some of the challenges that they are facing.

Senior Chinese bankers operate today in a very different political and financial environment than they did in the past. Their banks are bigger, disclosure about their activities is greater, and China's position in the global economy has been transformed.

For example, in 2000, only nine Chinese banks featured in *The Banker* magazine's 'Top 1000 World Banks' compared to 117 in the 2015 listing. In fact, 10% of the world's biggest banks are Chinese, including four of the biggest ten.

The type of people now running the big Chinese banks reflects these changes, and the growing global importance of the Chinese banking system.

In my experience of watching China's banks over 25 years, it seems to me that China is the most money-focused country in the world and as a result its bankers have a profoundly difficult task in satisfying the needs of their huge numbers of staff and customers. Industrial & Commercial Bank of China (ICBC) has around 400,000 employees and 440 million individual customers. It is the largest bank in the world in terms of total assets and Tier 1 capital. The three other 'big four' Chinese banks have similar scale.

> "The people managing the big state-owned banks are highly competent bankers who are able to balance their political linkages and their commercial obligations with considerable skill."

How do you manage a bank that size, and what sort of person do you need to do the job?

ICBC's Chairman, Jiang Jianqing, is a formidable banking personality, as is China Construction Bank's Chairman, Wang Hongzhang, and Bank of China's Chairman, Tian Guoli. All three are running state-owned banks but it would be a big mistake to see them as 'clones' or government flunkies. They are highly competent bankers who are able to balance their political linkages and their commercial obligations with considerable skill.

Chairman Jiang is widely credited with building ICBC into China's most profitable state-owned bank, but he, like the others, still faces tough scrutiny in the Beijing political system, which remains largely opaque to Western observers. These senior bankers have to run the gauntlet of the country's fragile financial system along with playing the political games endemic in all senior posts, a problem not really faced by Western bankers who lead much simpler lives by comparison.

Understanding how the careers of bankers evolve remains a mystery to outsiders. The Chairman of the People's Bank of China (PBoC; the Central Bank), Zhou Xiaochuan, was first appointed in 2002 and then again in 2013. He is a very capable and discerning economist, but every year for the past five years there have been rumours that he is about to be replaced. But he has survived. The politics of these decisions are not understood outside China but Mr. Zhou appears to have done a remarkably competent job in difficult times.

Another banker whom I have known well has been Guo Shuqing, who was Chairman of China Construction Bank from 2005 to 2011 prior to Chairman Wang taking over. A hugely competent, well-educated financier, Mr. Guo went on to become Chairman of the China Securities Regulatory Commission (CSRC), China's securities regulator. Then in 2013, he was appointed Governor of Shandong province in eastern China. People see this as part of the political grooming process for Mr. Guo to become a possible future premier or possible successor to the PBoC's Mr. Zhou. But we don't really know.

How these senior appointments are made or not made is a quandary for China's financial observers. What we can say is that there is no shortage of very well-qualified candidates for these key posts and that China has a highly competitive education and training system that produces candidates that are suitable to take responsibilities at all levels in the system. It is a great mistake to underestimate the capabilities of Chinese bankers, even if traditional cultural practices and customs may seem distracting at times.

For example, why did Bank of China Chairman Guoli need to have eight senior executives with him when I interviewed him in 2014? This seemed odd to me especially when Chairman Guoli was the only bank official to speak, being very forthright with his comments. (One of his comments during that interview was, "There is nothing more

"Chinese banking culture is diverse and is now being influenced by highly educated Chinese bankers who are returning home after spending time overseas."

important than the internationalisation of the renminbi.") This traditional style of running meetings and managing banks occurs at many other banks, including Beijing Rural Commercial Bank, but is changing. A few years ago, I was able to have a one-on-one interview with China Guangfa Bank President, Morris Li, who has worked in Asia for Citigroup. While traditional elements remain, most major banks today reflect trends across global banking and global banking regulation.

Similarly, a more open style was shown by PBoC Deputy Governor Yi Gang in a wide-ranging interview discussing China's foreign reserves. With the expected checks and balances, Mr. Yi was quite forthcoming on issues which often in the past were not discussed at all. The level of bank disclosure today is a quantum leap forward from that of 15 years ago and Chinese bankers, given the necessary safeguards are in place as well as the requisite trust, are able to deal with all the financial figures and issues that they now face.

The radical changes that have taken place in terms of disclosure of information and the abilities of senior bankers are clearly reflected in attitudes and policies of private sector banks. The tenth largest bank in China, China Minsheng Bank, is privately owned and has been an important pioneer in financing domestic infrastructure and small and medium enterprises (SMEs) as well as community banking. Chairman Dong Wenbiao was keen to push new strategies in new areas and as a result Minsheng has been able to create innovative ways of doing business.

Unlike the state-owned banks, Minsheng also approached its clients and others in new and different ways. Attending a dinner with the Chairman in the bank's golf course in outlying Beijing, there was a much more relaxed atmosphere and convivial style where my eating and drinking capacity were tested to the full. Getting a grip of the banking culture is vital and we must remember that the culture is diverse and is now being influenced by highly educated Chinese bankers who are returning home after spending time overseas.

Amongst all this change, how are President Xi JinPing's policies affecting banks and how they do business? Political sensitivities are possibly even more heightened now given President Xi's urge to control all aspects of the way China runs and his very clear anti-corruption strategy. The largesse Chinese banks showed in the past has now been tempered and while the success of organisations such as Tencent and Alibaba have significantly altered the business culture in China, banking continues to remain conservative and very well aware of the problematic political sensitivities surrounding the sector.

As the market upheavals of 2015 demonstrated, China's financial system is fragile and President Xi is looking for stability to override the uncertainty that besets most of the world's major economic players. It is no surprise that in these difficult times there have been few key changes at the top of the banking and regulatory sectors. President Xi is keen to avoid any social upheavals and a stable financial sector is more important in China than in many other countries. Senior Chinese bankers have a tough task ahead to avoid any unwanted turbulence. ■

**Stephen Timewell**

Stephen Timewell is Editor Emeritus of *The Banker*, the global monthly banking magazine of the Financial Times Group. He was the magazine's Editor from 1992 to 2003 and Editor-in-Chief from 2003 to 2009 when he retired. In his 23 years at *The Banker* he wrote about banks in all areas of the world, and in particular on China and on the Middle East.

Before joining *The Banker*, Stephen had been Editor of *The Arab Banker* from 1988 to 1990. In the 1980s he worked for First Chicago and for Middle East Economic Digest (MEED). He has a Bachelor of Economics from Monash University in Melbourne, Australia, and a Masters in Islamic History and Arabic from University of Chicago.

# Fundamental factors underpin the London commercial property market

The UK's decision to leave the European Union (EU) took many by surprise and, when coupled with the uncertainties surrounding the formation of the new British government, it led to short-term uncertainty and volatility in financial markets.

As the dust settles from the 23 June referendum result (universally known as 'Brexit'), Raed Hanna, Managing Director of the London-based property finance boutique Mutual Finance, considers whether London will be able to retain its place as the most attractive real estate market in Europe as the UK prepares to leave the EU.

London has always been one of the most diverse and culturally exciting cities in the world and a hugely popular destination for commercial real estate investment from the Middle East, and indeed the rest of the world. The immediate shock waves from the Brexit vote did of course have an impact on some property deals that were being structured or marketed at the end of June, but the property market is used to coping with political changes and world events and we saw that the market quickly digested the unexpected referendum result and, to a large extent, regained its poise over the summer.

Following the referendum result, there are some concerns that the property market could cool, but the situation is very different from 2008.

During the financial crisis of 2008, we saw a sharp drop in the value of office and commercial property funds and this led to big capital losses for investors.

Today, bank lending leverage is much lower than the 80%+ levels that we have witnessed in recent years – leverage of 60% or less is now much more common. As a result, if there is a sustained slowdown in economic activity, borrowers will not have huge bank loans to repay as they did in 2008 and the years that followed.

We should also remember that the London market was already starting to cool during the first half of 2016 and that activity levels always fall during the summer months. Looking beyond the two or three weeks that followed the referendum vote on 23 June, it is difficult to tell just how much of a fundamental difference Brexit is making.

Although the Brexit vote may depress the way in which investors feel about UK commercial and residential property prices, particularly in London, we at Mutual Finance are not

expecting rental incomes to fall. The main reason for this is that there is no supply 'overhang' except perhaps in certain areas of prime residential property.

Looking beyond the UK, London still retains many advantages for investors, and we expect that there are many reasons why London will retain its favoured position in the commercial property market, even as the UK negotiates its withdrawal from the European Union.

For example, London is an accessible market with very few barriers to entry and investment. In contrast, Switzerland, which is often seen as a safe haven for investors, strictly regulates the acquisition of real estate by non-residents. The Lex Koller requires 'persons abroad' to obtain a permit from the appropriate cantonal and federal authorities before buying real estate in Switzerland.

The Swiss authorities also limit the number of properties that are open to investment from non-residents. The number varies from year to year but, whatever that number may be at any given time, it is acting to inhibit non-residents investing in Swiss real estate.

Leasing regulations is another area where London has an advantage over many other international cities. The Fully Repairing and Insuring (FRI) lease, which is standard in the London commercial property market, places the obligation for managing and maintaining a building firmly on the tenant, with all the tenant's responsibilities clearly stated. The leases normally run for periods from five to 25 years, with the timing of rent reviews agreed at the outset. Leases often have provisions for fixed raises in rents and there is always the option to review the rents against open market values. Even when reviewed against the market, rents are subject to upward-only revisions.

The UK's Landlord and Tenant Act governs the terms and implementation of these leases, but landlords have an option to opt out, effectively rendering the leases 'outside the act' and giving landlords even greater flexibility.

Compare this against the commercial real estate market in Paris.

Commercial real estate leases in Paris are highly regulated and to a large extent follow a standard format prescribed in French law. Usually, commercial leases have a nine-year term which is fixed – much shorter than many of the leases in London. Furthermore, these leases have 'break clauses' at the end of every three years (after three years, six years and at the end of the full nine years).

**Mutual Finance**

Founded by Raed Hanna, Mutual Finance is a progressive and innovative financial intermediary specialised in structuring and raising leveraged debt for real estate development. Based in London's Mayfair district, the firm is one of the UK's largest financial intermediaries financing more than £750 million of asset-backed and real estate transactions during 2015.


**Raed Hanna, Managing Director, Mutual Finance**

> "The structural factors underpinning the London market – laws, typical leasing structures, acceptability of different types of property assets – will continue to give it an advantage, over the long term, against other European cities."

Sitting tenants have a statutory right to renew, with the result that it can be hard to get vacant possession of a building, and this in turn hampers opportunities for redevelopment and innovative asset management.

Finally, the termination of the lease is subject to very unfavourable (for the landlord) procedural requirements, and if the landlord does not comply with these, he can be subjected to harsh penalties.

The German real estate market also has hurdles for investors and landlords. Leasing contracts typically do not impose undue burdens on landlords, but there are no guaranteed rent reviews and with short- to medium-term lease commitments landlords are working in an environment of considerable uncertainty.

Constraints on commercial finance in Germany also arise from the banking system. Much of German commercial property is financed through the Pfandbrief (covered bond) market, which is highly developed and mature, but which also has its own ideas on what constitutes appropriate leverage. As a result, loan to value ratios greater than 55–60% are unusual, and therefore more difficult to finance. Lower leverage levels such as these often restrict the return that can be earned on capital.

Some asset classes do not qualify for Pfandbrief financing with the result that alternative lenders have to step in to provide finance. In contrast, the London market takes a far more open and flexible approach to asset finance.

Looking further south across Europe to the Mediterranean region, we see continuing economic uncertainty. For example, in Spain – historically one of Europe's better performing economies – commercial property prices continue to be 30% below their peak in 2008. Such large discounts may offer buying opportunities, but they also highlight the huge volatility in prices that characterises many southern European markets.

The structural factors underpinning the London market – laws, typical leasing structures, acceptability of different types of property assets – will continue to give it an advantage, over the long term, against other European cities.

Furthermore, the City of London has always been able to provide the expertise and the financing needed to structure and execute large property transactions. Most European and US banks have lending platforms in London through local subsidiaries or branches. Developers and investors are used to sophisticated debt tranching through the capital stack, making the structuring of leveraged transactions much easier.

In the short term, uncertainty about the effects of Brexit are being balanced by developments in the monetary environment that are enhancing the attractiveness of London to investors.

The Bank of England's decision in early August to cut interest rates to 0.25% drew five-year swap rates down to 0.45% (plus credit spread and lending margin) making borrowing cheaper than it has been for many years. Furthermore, currency exchange rate changes since the Brexit vote have made London even more inviting for foreign investors.

"Leasing regulations is an area where London has an advantage over many other international cities."

We have seen several commercial property transactions agreed since the end of June. For example, investors from the Middle East have exchanged contracts to purchase 5 King William Street in the City of London. This is the UK headquarters of the Japanese investment bank Daiwa. It was purchased for about £90mn to generate a yield of about 3.6%. An investor from Singapore has made an offer for 160 Aldersgate Street, again in the City of London, for £175mn, to yield a little below 5%. These are the new offices of law firm DLA Piper.

So the overall picture that we are seeing is one of resilience to the Brexit decision. A few deals have been delayed, but deals are still being done, and there is no shortage of investors looking to take advantage of the underlying structural strengths of the UK property market – strengths that will be undiminished by Britain's departure from the European Union. ■

**ABOVE: 5 King William Street, in the City of London, which was recently bought by Middle Eastern investors for about £90mn. LEFT: 160 Aldersgate Street, in the City of London, which was recently bought by an investor from Singapore, for £175mn.**

We are what we repeatedly do;
excellence, then, is not an act but a habit.

*-Aristotle*

# Out of the shadows and into the mainstream: the rise of platinum as a global asset class

Investors in commodities are used to giving their opinions on the prospects for gold and silver prices, on the outlook for crude oil, and the supply–demand trends for industrial metals such as copper and zinc.

But what about platinum? Do you have a view on the platinum market? Do you even know what the price of platinum is? If you don't, you should.

Platinum is becoming an asset class for professional and retail investors as its usage in industry and for jewellery increases, and as bullion and ETF markets mature.

In the following article, *Arab Banker* describes the changes occurring in the platinum market, and considers the forces driving its availability, uses and pricing.

Platinum has a long history going back to the ancient Egyptians and to the Incas of South America, but it is also a very modern metal. Because its melting point is far higher than that of gold or silver, platinum jewellery was rare until the development of high-temperature jewellers' torches about one hundred years ago.

Platinum's industrial uses are also strongly tied to the modern era. About 40% of global demand is for catalytic converters – devices that convert noxious exhaust emissions from cars and other vehicles into less harmful gases. The introduction of automotive emissions standards in the 1970s gave a big boost to platinum demand. Today, continuing tightening of emissions standards around the world, combined with ever-increasing numbers of vehicles on the roads, is underpinning a steady increase in platinum usage by the automotive industry.

A January 2016 report by Glaux Metals estimated that use of platinum by the automotive industry had a compound average annual growth rate of 8.1% between 2009 and 2015.

Platinum is 30 times more rare than gold and global deposits are heavily concentrated in South Africa.

Mining of platinum produces 78% of its global supply, which in 2015 amounted to 7.9 million ounces. The remainder comes from the recycling of products containing platinum – dominated by used autocatalysts removed from end-of-life cars.

South Africa accounts for about 70% of all mined platinum each year (and most of South Africa's production comes from a single area, the Bushveld Complex, north of Johannesburg). Russia accounts for about 12% and Zimbabwe 7%.

In recent years the South African platinum mining companies have been cutting back on capital expenditure as a result of reducing margins, which in turn are the result of sustained cost increases and weak metal prices. It is unlikely that South African mines will show significant increases in production in the years ahead and there is a real possibility that current levels of capital investment will lead to a further decrease in output. Production of nearly 4.5 million ounces in 2015 was already 7% down on levels seen in 2011.

The complex political situation in Zimbabwe has discouraged investment in the country's mines and so precludes increased production in the medium term.

Capital investment in platinum supply is also being depressed by the dramatic fall in the prices of by-product metals that are also found in platinum bearing ores such as palladium, rhodium and nickel.

Some increased supply is likely to come from recycling in the coming years. As the amount of platinum used in vehicles increases to meet ever more stringent emissions limits (particularly for diesel cars in Europe, which have a higher portion of platinum in their catalysts), the metal content of scrap autocatalysts also increases over time. As these cars reach the end of their life – roughly 50% are scrapped between 7 and 15 years – the higher metal content increases annual supply from this source.

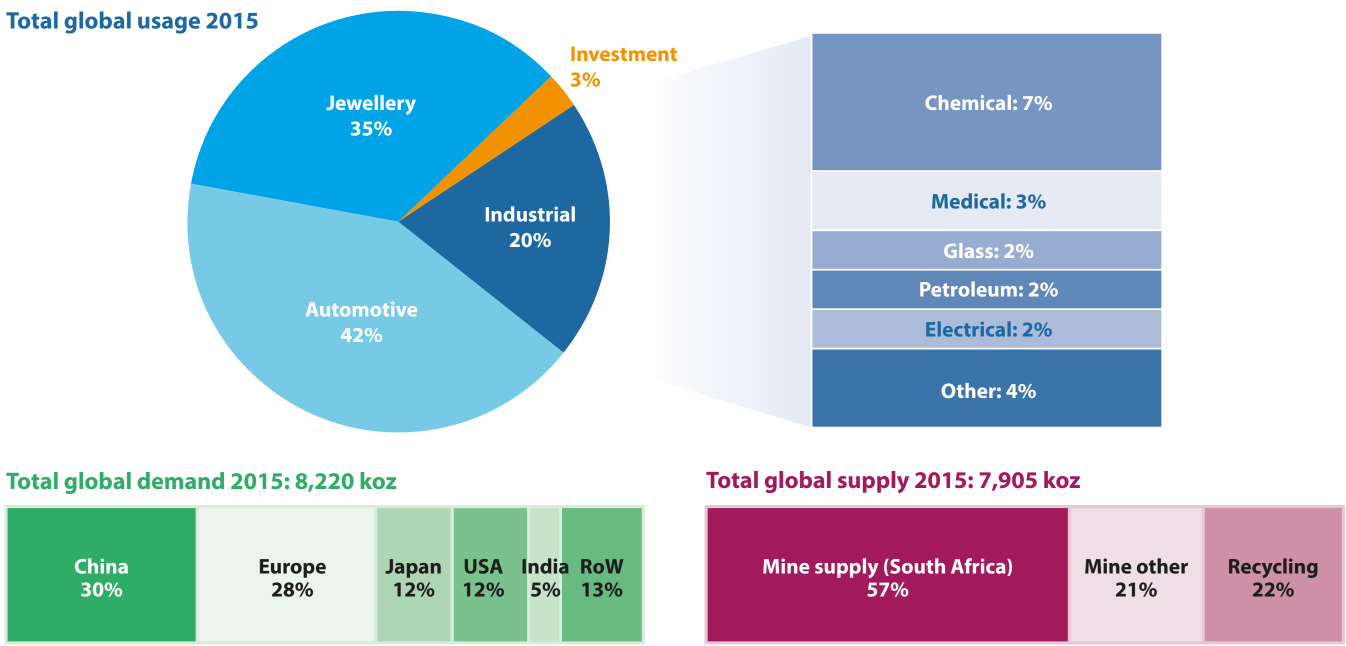
But the overall picture is of flat or even falling supply over the medium term.

## Platinum has a crucial role in reducing $CO_2$ emissions

In contrast, demand is likely to increase. The main driver for this will be increasing sales of diesel-fuelled vehicles and ever-stricter regulations on exhaust emissions.

Petrol cars use very little platinum in their catalytic converters – they can use palladium and rhodium, both of

**Platinum global usage and demand, 2015**




which are currently cheaper. But autocatalysts on diesel vehicles are dominated by platinum. Much therefore depends on global growth and the pace of industrialisation in the major emerging economies – greater industrialisation leads to greater usage of diesel-powered trucks, off-road diesel engines and, of course, cars.

The portion of diesel cars on the road is likely to remain similar to the current level because diesel cars emit 20% less $CO_2$ than gasoline cars and assist automakers in achieving the required $CO_2$ target levels for their fleets.

Over the long term, the significant reduction in $CO_2$ emissions required is likely to drive growth of fuel cell electric vehicles (FCEVs), which emit no $CO_2$ and offer competition to internal combustion engine vehicles in terms of range and refuelling time. (In contrast, battery electric vehicles are unlikely to overcome, in the short term, their inherent limitations of multi-hour recharge times and limited range.) Increased usage of FCEVs will also lead to increased platinum demand since FCEVs require more than double the platinum used in diesel cars. Most of the world's leading car manufacturers have or are about to launch FCEVs.

The global agenda for reducing carbon emissions is particularly relevant to the platinum market and, in simple terms, emissions targets will only be met if global usage of diesel and FCEVs increases in relation to petrol vehicles.

After the automotive industry, the jewellery market is the second biggest user of platinum, accounting for about one third of global demand.

The growth in disposable income in China, the largest global platinum jewellery market, is driving increased purchases of jewellery. The platinum industry believes that it has barely scratched the surface of the urban female population in China (whereas awareness of gold is well established), and the industry is developing new products in India to try to capture a larger share of the jewellery market, which is estimated at $40bn. A recent industry survey in India asked the question, "Which metal means love?" 'Platinum' was by far the most common answer.

### Platinum: a noble history

Platinum is one of the 'noble' metals, so called because they resist oxidisation and corrosion in moist air. Other noble metals include gold, silver, palladium, iridium and rhodium. 'Base' metals, such as copper, lead, nickel and zinc, do oxidise or corrode and are much cheaper than noble metals.

Platinum is dense, malleable and ductile. It is also heavy – a six inch cube of platinum weighs as much as the average human being. 'Malleability' refers to the metal's ability to be hammered or pressed into a shape without cracking or breaking. Being 'ductile' (as opposed to brittle) means that a metal can be stretched without losing its toughness – one gram of platinum can be stretched into a wire over one mile long.

Platinum is also extremely rare – 30 times more rare than gold. As the World Platinum Investment Council describes it, "All the platinum ever produced would only cover your ankles in an Olympic-sized swimming pool, but all the gold ever produced would fill three Olympic-sized pools."

Platinum is found with the other platinum group metals and with metals such as copper and nickel. European appreciation of platinum arose through contact with Central America in the mid-sixteenth century although it was not properly understood until the mid-eighteenth century. The word 'platinum' means 'little silver' and platinum was often confused with silver until it was clearly identified as a distinct metal.

Platinum melts at 1,768 degrees centigrade (compared to 1,064 for gold and 962 for silver) and this extremely high melting point makes it difficult to work with, so in the eighteenth century scientists often used it as an alloy with gold, making it more malleable. It was only at the end of the eighteenth century that platinum was successfully isolated.

Louis XV, who ruled France in the mid-eighteenth century, described platinum as the only metal "fit for a king". In 1937, Queen Mary wore a platinum crown during the coronation of her husband as George VI, the first British crown to be made of platinum.

A variety of industrial processes require platinum and together they account for about 20% of the metal's global demand. Growth in industrial usage over the next few years, while dependent on platinum applications in specific industries, will remain largely driven by global economic growth. For example, platinum is used in the manufacture of nitric acid for fertiliser, so as the global demand for food increases then the need for platinum increases. Similarly, as improved healthcare reaches developing economies more platinum is needed for medical devices.

The final source of demand for platinum is the investment community. Currently, investment accounts for about 3% of global demand, although this figure has been far higher in some recent years. Until 2007, large institutional investors held platinum in vaults in large bars, but in 2007 Exchange Traded Funds (ETFs), backing issued shares with physical vaulted metal, were launched in Europe, leading to a big leap in investment demand. Similarly, investment demand grew when new ETFs were launched around the world with the most impressive example being in South Africa in 2013. The World Platinum Investment Council (WPIC) is working with global providers of investment products to increase the availability of investment vehicles that are based on physical metal. This will provide more investors with the ability to consider the merits of including platinum in their investment portfolios.

### The supply–demand deficit will continue at least until 2021

When we put the sources of supply and the sources of demand together, a clear picture emerges. In every year since 2012, demand has outstripped supply, and it is expected to continue doing so over the next five years.

The years 2013 and 2014 were exceptional, with supply deficits in each of over 700,000 ounces, against total supply in those years of over 7 million ounces. The Glaux Metal report forecasts supply deficits averaging 260,000 ounces per year until 2021.

Against the backdrop of such clearly supportive fundamentals it is reasonable to question why the price of platinum has been so poor in recent times.

Platinum's price decline and continued weakness since 2011 has been inconsistent with the strong fundamentals of the global platinum market. The WPIC believes the weakness in the platinum price that began in 2011 was largely driven by sales from investors' unpublished vaulted holdings. Continuing low prices into 2016 were the result of momentum and short-term traders, and a tightened correlation between the gold and platinum prices, the WPIC says.

Platinum has historically traded at a healthy premium to gold. Indeed, there have only been four occasions during the last 40 years where platinum has been priced at a discount to gold for a sustained period. In all previous cases, the price has markedly recovered in the following years.

In recent years, platinum has generated investment returns between those of gold and equities (see table below). Those returns have generally not shown high correlation with other asset classes, with the result that adding platinum to most investment portfolios will enhance their risk-adjusted return. (In mathematical terms, the Sharpe ratio of many portfolios increases when platinum is added to them.)

The WPIC was established by the industry in 2014 to provide robust research and information on the platinum market, and to facilitate the development of new investment vehicles. An example of its work can be seen in its recent partnership with Valcambi, the Swiss precious metals refiner, which aims to increase the availability of platinum bars and coins for the investment market. The Council also publishes detailed supply–demand data and analyses, including a detailed quarterly report on its website.

These are interesting times for the platinum market. Demand is increasing due to factors as diverse as the global climate change agenda and increased disposable income in China, but supply will be constrained over the medium term.

Platinum is coming out of the shadows. This is a metal we all need to understand. ■

**Long-term investment performance, platinum vs. other asset classes**

| 1990–1995 | 1995–2000 | 2000–2005 | 2005–2010 | 2010–2015 |
|---|---|---|---|---|
| Macro Hedge Fund (29%) | Private Equity (23%) | Oil (20%) | Gold (22%) | Private Equity (13%) |
| Equity HF (24%) | Equity Hedge Fund (22%) | Emerging Market Equities (19%) | Emerging Market Equities (13%) | Developed Market Equities (8%) |
| Emerging Market Equities (22%) | Developed Market Equities (13%) | Global REITs (17%) | **Platinum (13%)** | Global REITs (8%) |
| Developed Market Equities (12%) | Macro Hedge Fund (11%) | Gold (14%) | Oil (10%) | US Fixed Income (3%) |
| Global REITs (11%) | **Platinum (9%)** | Commodities (11%) | Macro Hedge Fund (7%) | Equity Hedge Fund (3%) |
| US Fixed Income (9%) | Commodities (7%) | **Platinum (10%)** | US Fixed Income (6%) | Macro Hedge Fund (0%) |
| Commodities (8%) | Global REITs (7%) | Macro Hedge Fund (9%) | Equity Hedge Fund (4%) | Emerging Market Equities (–4%) |
| Gold (0%) | US Fixed Income (6%) | Equity Hedge Fund (7%) | DM Equities (3%) | Gold (–6%) |
| **Platinum (–1%)** | Oil (5%) | US Fixed Income (6%) | Global REITs (3%) | **Platinum (–13%)** |
| Oil (–8%) | Emerging Market Equities (–4%) | Developed Market Equities (3%) | Commodities (1%) | Commodities (–13%) |
| | Gold (–7%) | Private Equity (2%) | Private Equity (–6%) | Oil (–17%) |

*Source: Bloomberg (Annualised Returns)*

# New members and new activities: another good year for the Association

The Arab Bankers Association has broadened its range of activities over the last year and attracted new corporate members. We also have new Board members.

The Association has held 12 member events since the last edition of *Arab Banker*, a year ago. Six of these were technical seminars on issues ranging from the foreign exchange market, real estate investing, and the tools banks can use to fight financial crime. These evening seminars typically drew 80–100 members and their colleagues. We pride ourselves on bringing speakers with hands-on knowledge of their subject matter and the presentations are always followed by a buffet dinner to enable participants to mix informally with the speakers and each other.

We held two executive lunches during the year. These were invitation-only events for our corporate members. The first, held in January, considered bankers' personal liability under the UK regulators' new Senior Management Regime (which came into effect in March) and the second considered new rules on disclosure of tax and wealth, and the implications for bankers of the 'Panama Papers' revelations. On each occasion, three subject matter experts led the discussion, and representatives from about 12 corporate members attended.

In February, we arranged a meeting between our members and representatives of the UK's Prudential Regulatory Authority (PRA). Twenty-eight senior bankers from 21 Arab bank branches or subsidiaries attended the meeting, which lasted for two hours. The discussion addressed specific concerns related to recruitment for 'controlled functions' under the Senior Management Regime, supervision of branch and subsidiary liquidity in relation to parent bank liquidity, and new capital requirements under the Basel III Capital Conservation Buffer. Both the bankers and the PRA officials deemed the meeting a success and agreed to hold another before the end of the year.

We held three social events, including our gala dinner. Shaukat Aziz, the former Prime Minister of Pakistan (and former Citibanker and CEO of Samba) was our guest of honour and he was introduced by Lord Lamont, the former British Chancellor of the Exchequer. Adel El-Labban, the Managing Director and Group Chief Executive Officer of Ahli United Bank, received our award for Distinguished Service to Arab Banking.

Other social events were our Christmas party, and our Eid Dinner held in July.

The Association now has 33 corporate members, including 21 Arab banks whose parents are based in nine different Arab countries and in the United Kingdom. Our corporate members also include non-Arab banks, law firms, accounting and auditing firms, and industry bodies.

During 2016, we have welcomed new Board members, including Stephen Blyth, Acting General Manager of Arab National Bank's London branch, Paul Jennings, Managing Director and Chief Executive Officer of Bank ABC London, Ralph El Raheb, Managing Director of Morgan Stanley in London, and Hani Salem, a Senior Manager with PwC in London.

Late last year, one of our Board members, Tarek Amer, was appointed Governor of the Central Bank of Egypt.

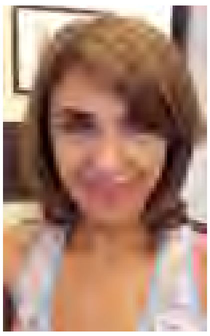
The Association's financial situation is strong, and is becoming stronger.

We have introduced new features to our website, www.arab-bankers.co.uk, including a Gallery tab, where we post photographs of our events, and a Magazine tab, which contains current and previous editions of this magazine. Where possible, we also post the presentations from our seminars on the website in the Events section.

Membership of the Arab Bankers Association LinkedIn Group continues to grow, which in turn drives more traffic onto our website.

The Arab Bankers Association is led by George Kanaan, the Chief Executive Officer. George is assisted in the London office by Joumana Karam, Membership Secretary, Esin Erdil, Accounts and Administration, and Dania Archid, Business Development. Carol Hovsepian, Business Development, works from Beirut. Andrew Cunningham is the Association's Editor in Chief, overseeing content for the website and producing publications, including *Arab Banker* magazine. ■

**L–R: Dania Archid, Business Development; Joumana Karam, Membership Secretary; George Kanaan; Esin Erdil, Accounts and Administration**



**Carol Hovsepian, Business Development**

## The ABA's Board of Directors is elected at the Annual General Meeting, which is usually held in September. A list of serving Board members, as of August 2016, is given below.

**Abdulaziz Al-Khereiji (ABA Chairman. Board member since 2012)**
Abdulaziz has been working within London's financial services sector for over 25 years. He joined Riyad Bank's London branch in 1996 and is now its Chief Manager. He is also Riyad Bank's Senior Vice President for Overseas Units, and in this capacity he manages the bank's international corporate relationships in the United States, Europe and Asia, focusing on clients' business activities in the Kingdom of Saudi Arabia and the GCC as a whole.

**Fawzi Dajani (ABA Vice Chairman. Board member since 2008)**
Fawzi is the Managing Director of National Bank of Kuwait (International) plc, the London-based subsidiary and European arm of National Bank of Kuwait (NBK). Fawzi joined NBK in 1985 and held positions in Singapore, Kuwait and London before leaving to take up senior posts at Merrill Lynch International Bank and then HSBC Private Bank. He has been Managing Director of National Bank of Kuwait (International) since 2007.

**Neel Patel (ABA Treasurer. Board member since 2016)**
Neel is Head of Finance, Bank ABC London. He was previously a Senior Manager in KPMG's banking audit and assurance practice. During his 11 years with KPMG, Neel accumulated experience in the investment, retail and banking sectors. Neel joined KPMG from UBS Investment Bank, where he was a CDS analyst. He studied economics at University College London and is a Qualified Chartered Accountant and a member of the ICAEW.

**Vivien Davies (ABA Company Secretary. Board member since 2012)**
Vivien is a partner in the London law firm Fieldfisher. During her career she has specialised in company, banking and commercial disputes, including complex cross-border disputes and international arbitration. In addition to general commercial clients, she regularly acts for foreign banks and enterprises from the hospitality, construction and healthcare sectors, together with media organisations. She is an active member of the UK's Middle East Association and is fluent in Arabic.

**George Kanaan (ABA CEO. Board member since 2009)**
George was appointed Chief Executive Officer of the Arab Bankers Association in August 2009. He began his banking career with Citibank in New York in 1975 and spent three years with First Chicago in London from 1984. He returned to Citibank in 1987 to establish and become General Manager of the London branch of Saudi American Bank (which was managed and partly owned by Citibank) and its associated investment company. After leaving Saudi American Bank, he established and managed a family office and acted as a consultant to Arab companies and high net worth individuals.

**Ziyad Akrouk (ABA board member since 2012)**
Ziyad has been Chief Executive Officer of Europe Arab Bank plc, which is part of the Arab Bank Group, since May 2011. He is based in London. He was previously CEO of Citibank's operations in Kuwait and also held senior roles within Citibank in Bahrain, Poland, Egypt and Jordan. Before becoming a banker, Ziyad spent his early career working as a civil engineer.

**Farid Barakat (ABA board member since 2010)**
Farid is the Country CEO and Managing Director Global Wealth UK of the National Bank of Abu Dhabi (NBAD) and head of its London branch. He is based in London. Farid joined NBAD in 1977. The bank's London branch specialises in private banking services and high profile property financing and has a growing corporate and trade finance department.

**Stephen Blyth (Board member since 2016)**
Stephen is a seasoned banker with more than 37 years experience. He is currently Acting General Manager of the London branch of Arab National Bank (ANB). He has been with ANB in various senior roles since 1991 and between 1994 and 2004 was based in the bank's head office in Riyadh. Stephen has held a variety of roles during his banking career and for the last 10 years, in addition to jointly running ANB's London branch, much of his time has been focused on regulatory change. He holds both CF10 and CF11 functions.

**Samer Hijazi (Board member since 2012)**
Samer is a partner with Grant Thornton, heading its Abu Dhabi office and leading its Islamic Finance practice. Prior to joining Grant Thornton in November 2015, Samer was a Director in KPMG's Financial Services Audit practice. Before joining KPMG's London office in 2000, he worked for another Big Four firm in the United Arab Emirates, where his clients included leading local and international financial institutions.

**Paul Jennings (Board member since 2016)**
Paul is Managing Director and CEO of Bank ABC London. Previously, he was Deputy CEO of the bank and Group Head, Global Trade Finance, Bank ABC Bahrain. Paul joined Bank ABC London in September 1999 and has over 30 years' experience in the international wholesale banking sector. He also represents Bank ABC as Deputy Chairman of Bank ABC Islamic and is a Director of Banco ABC Brasil S.A.

**Hani Kablawi (Board member since 2010)**
Hani is an Executive Vice President at BNY Mellon and the head of the bank's EMEA asset servicing division. He is based in London. Hani previously managed country and client relationships across EMEA for BNY Mellon and was co-Chair of the bank's Sovereign Advisory Board, which oversees relationships with sovereign wealth funds and central banks globally. He previously worked for BNY Mellon in New York, Abu Dhabi and Dubai.

**Charbel Khazen (ABA Board member since 2014)**
Charbel is a Senior Vice President at Bahrain-based Gulf International Bank (GIB) and the manager of its London branch. He is based in London and has lived in the UK since 1985. Charbel joined GIB in 1995 and has held his current position since 2006. Before joining GIB, Charbel worked for Qatar National Bank and Europe Arab Bank (then known as Arab Bank) in London. Most of his banking career has focused on corporate and institutional banking, with an emphasis on relationship management and business development.

**Ralph Al Raheb (ABA Board member since 2016)**
Ralph is a Managing Director at Morgan Stanley and is Head of Fixed Income for Middle East and North Africa. He is based in London and is a member of Morgan Stanley's MENA Management Committee. Ralph transferred from Paris to London in 2005 to cover the MENA region. In 2007 he was named Vice President and in 2009 became an Executive Director. In 2010 he was appointed Head of Fixed Income Sales for MENA and then became Head of Fixed Income for the region. In January 2015 he was made a Managing Director. Ralph has a Master's in Economics and a Master's in Finance and Asset Management from Paris IX.

**Bert de Ruiter (ABA Board member since 2014)**
Bert is a partner with Stormbridge International, the London-based executive search firm. Prior to joining Stormbridge in early 2016, he had been Chief Executive Officer of Qatar Islamic Bank (QIB) (UK) with effect from March 2014. He previously worked for QIB as General Manager of the bank's wholesale banking group, based in Doha. Before working for Qatar Islamic Bank, Bert held a wide range of senior banking positions at Lloyds Bank, including CEO of the bank's operations in Dubai and Country Manager in the Netherlands. A Dutch national, Bert began his banking career at ABM AMRO Bank.

**Hani Salem (Board member since 2016)**
Hani is a Senior Manager in PwC's Banking and Capital Markets assurance practice. He has more than 10 years experience auditing and advising international banks, sovereign wealth funds and other financial services firms in the UK and the Middle East. He is currently providing audit and other assurance services to one of the largest European banking and financial services organisations. Hani is a Certified Public Accountant from the New Hampshire Board of Accountancy.

**Amr Turk (ABA board member since 2010)**
Amr is the General Manager of the London branch of BLOM Bank France. He is based in London. A graduate of the University of Oxford, Amr joined the Planning and Administration Division of Saudi Oger in Riyadh in 1983. In 1984, he joined BLOM Bank France and was among the first staff to be involved in setting up the London branch that was, and continues to be, focused on providing private banking services, property finance and documentary credits. With over 30 years in the UK, Amr has developed an in-depth knowledge of the financial system and he has established links with many corporations and individuals seeking banking services in the UK.

# ABA annual gala dinner: Adel El-Labban receives award for Distinguished Service; Shaukat Aziz delivers keynote address

The Arab Bankers Association's 2015 gala dinner was a star-studded affair that included a former Prime Minister, a former Finance Minister and the head of one of the Middle East's biggest banks.

More than 270 guests attended the dinner, which was held at the Jumeirah Carlton Tower in London's Knightsbridge on 5 November 2015.

During the dinner, George Kanaan, the Association's CEO, and Abdulaziz al-Khereiji, the Chairman, presented the Association's Award for Distinguished Service to Arab Banking to Adel El-Labban, the CEO and Managing Director of Bahrain's Ahli United Bank. In his acceptance speech, Mr. El-Labban highlighted, *inter alia*, the increasing burden of banking regulation, particularly in London.

Before the award to Adel El-Labban, Lord Lamont, the former British Chancellor of the Exchequer, introduced HE Shaukat Aziz, the former Finance Minister and Prime Minister of Pakistan. In his speech, Mr. Aziz described a recent meeting he had attended with very high-level Chinese officials, in which they expressed their concern that China's increasing economic and political weight could, unnecessarily, lead to regional and international tension. He also explained the reasoning behind the recent creation of the Asian Infrastructure Investment Bank.

Towards the end of the evening, guests were entertained by Farrah El-Dibany, an opera singer, and pianist Leonardo Reyna. Farrah is Egyptian (although she has been based for some time in Germany) and her performance included Egyptian songs as well as those from the classical repertoire.

Five banks took premium tables at the dinner: National Bank of Kuwait (International), Europe Arab Bank, Riyad Bank, National Bank of Abu Dhabi and British Arab Commercial Bank. Eleven institutions took standard tables: Jordan International Bank, Arab National Bank, Ahli United Bank, Gulf International Bank, KPMG, Abu Dhabi Islamic Bank, Qatar Islamic Bank (UK), Byblos Bank, Bank ABC, Mishcon de Reya and Curtis Mallet-Prevost, Colt & Mosle. Numerous other guests attended individually or with friends and family. ■


Mr. Adel El-Labban receives the 2015 Award for Distinguished Service to Arab Banking from George Kanaan and Abdulaziz al-Khereiji

Farrah El-Dibany and pianist Leonardo Reyna


L–R: Mr. Adel El-Labban, Mr. George Kanaan, HE Shaukat Aziz, Rt. Hon. Norman Lamont


Stephen Blyth, Arab National Bank, and guests


HE Shaukat Aziz


# Responding to financial crime and increasing cyber security

Lawyers, bankers, regulatory experts and IT consultants combined to brief ABA members and their colleagues on financial crime and cyber security on 21 April 2016.

Two partners in PwC's Risk and Regulation Practice, Andrew Clark and David Choi, opened the seminar by describing how banks can use technological solutions to respond to pressure from regulators for increased diligence on high-risk clients. Antonis Patrikios, a partner at Fieldfisher, then summarised legal requirements on cyber and data security that apply to banks. He was followed by Dan Crisp, the Global Chief Information Risk Officer and Head of Technology Compliance at BNY Mellon, who described his bank's response to cyber challenges.

Jonathan Partouche, CEO of Origone, then gave a fascinating explanation of the 'dark web' and the new cyber threats that his firm is observing, including the methods that cyber criminals employ to acquire confidential information that they can then use to defraud bank customers. ■


Andrew Clark, PwC


David Choi, PwC


David Sambar, Grace Agedengbe, Bank ABC London, Abdulaziz al-Khereiji, Riyad Bank


Jonathan Partouche, Origone


Dan Crisp, BNY Mellon


David Dao


Antonis Patrikios, Fieldfisher

# Practical responses to sensitive situations involving financial crime

On 11 May 2016, a leading London law firm and a top US security specialist, led a seminar on how banks should deal with specific incidents related to fraud.


Mohamed Khamisa QC, Mishcon de Reya

Partners from Mishcon de Reya and Alvarez & Marsal explained how banks can respond to issues such as fraud and data theft committed either by internal employees or external criminals. They also described new techniques for tracing fraudsters using forensic technology and practical steps that banks should take after they have identified a fraud.

As with all our evening seminars, the presentations and question and answer session was followed by a buffet dinner. ■


Phillip Beckett, Alvarez & Marsal

Julian Jones, Alvarez & Marsal, and Stephen Tsirtsonis, Endace

Fadi Elkhoury, Samba Financial Group

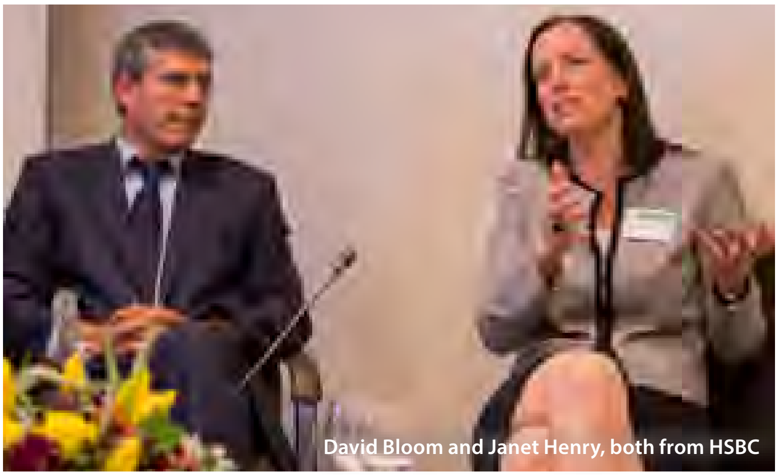
The weather smiled and guests were able to enjoy the buffet on the terrace

L–R: Peter Meyer, Chairman and CEO of the Middle East Association, George Kanaan, David Sambar

Marwan Dagher, HSBC

Marcus Grubb, World Platinum Investment Council

Ross Norman, Sharps Pixley



David Bloom and Janet Henry, both from HSBC

Dania Archid from the ABA and Wael El-Miqdadi

# Annual FX and commodities seminar draws a big crowd

Our annual seminar on the foreign exchange and commodities markets was held on 31 May 2016

HSBC's Global Chief Economist, Janet Henry, opened the seminar with an overview of global growth trends and the role that EU governments and the Chinese economy are playing in stimulating economic activity. She was followed by HSBC's Global Head of FX Strategy, David Bloom, who gave an entertaining explanation of the reasons for the dollar's weakness and a prescient analysis of what might happen to the pound if Britain voted to leave the EU.

Marcus Grubb, Director of Market Development at the World Platinum Investment Council, explained the economics of platinum production and pricing, and Ross Norman, the Chief Executive of Sharps Pixley, described the current state of the gold market.

Marwan Dagher, HSBC's Head of Institutional Sales in Europe, the Middle East and Africa, moderated the question and answer session. The seminar was followed by a buffet dinner.

The speakers' presentations were posted on the Association's website. ■

# Members and friends celebrate Eid el-Fitr at Maroush Gardens

Our annual Eid party was held at Maroush Gardens on 7 July.

This year the Association held its first ever Eid party. In previous years, we usually held an Iftar – the meal, beginning at sunset, when Muslims break their day-long fast. With Ramadan now falling in the middle of the summer – and therefore Iftars not beginning until nearly 10pm – we decided to hold an Eid party to coincide with Eid el-Fitr, the celebration that marks the end of the fasting month of Ramadan.

One hundred and twenty guests attended the party, which was held at Maroush Gardens in London's Mayfair. The event was sponsored by Bank ABC, National Bank of Kuwait (International) and QIB (UK). ■

Rajiv Adrian and Faisal Alshowaikh, Bank ABC

Emilie Dandan and Mrs. Dajani

Joumana El-Assad

Tatiana Al Raheb and Ralph Al Raheb, Morgan Stanley

Saeed Amin

# **Understanding the UK property market:** Brexit, underlying trends, and the effect of tax changes

Our annual real estate seminar is often one of the most popular of the technical seminars that we hold. This year's, held on 13 July, was no exception.

Our real estate seminar took place three weeks after Britain voted to leave the European Union, so many of the panellists considered how 'Brexit' is affecting the UK property market, both in terms of prices and in terms of the availability of finance. But the speakers also stood back from the immediate concerns related to the UK's position in Europe to reflect on longer term trends in the London prime residential property and in the UK commercial property market. The speakers also explained how recent changes to UK taxation are affecting the viability of certain types of property transactions. The evening included a briefing on current major developments being undertaken in London by Qatari Diar.

There was a lot of demand for the slide packs that supported the presentations, and these were posted on the Association's website a few days after the seminar.

The seminar was sponsored by Al Rayan Bank, National Bank of Kuwait (International) and Qatari Diar.

Reem al-Jumaily and Shaima Jillood, Boodle Hatfield

Suhail Ismail and Rima Kalai, Byblos Bank Europe

Tony Williams and Nigel Talbot-Ponsonby

The panellists L–R: Andrew Sneddon, Trowers and Hamlins; James Roberts, Knight Frank; Liam Bailey, Knight Frank; George Kanaan; Michael Bowles, National Bank of Kuwait (International); Maisam Fazal, Al Rayan Bank; Miles Wood, Qatari Diar.

# Corporate members' lunches give opportunities to discuss current issues and concerns directly with the experts

We held two special lunches for our corporate members in the first half of 2016.

Our corporate lunch programme aims to give our corporate members direct access to subject matter experts in an informal setting. The lunches are open to all corporate members, although for practical reasons numbers are limited to about 15 on a first come, first served basis. Members sometimes send their most senior London manager, but sometimes they send the member of staff whose work is most closely related to the subject being discussed

The first lunch of the year was held on 29 January and addressed the issue of bankers' personal liability, particularly in the context of the UK's Senior Managers Regime (SMR), which came into force in March. The three subject matter experts were Francis Kean, Executive Director of Willis Towers Watson, a leading global insurance broker; Peter Bibby, a partner at law firm Brown Rudnick; and Adam Epstein, a partner at law firm Mishcon de Reya.

All the speakers stressed that the introduction of the SMR will result in regulators giving greater focus to the behaviour of individual bank executives and that it will facilitate the targeting of individuals within banks when breaches of regulations have occurred.

The second lunch, on 21 April, was led by KPMG and addressed issues related to the disclosure by banks of information about their clients' wealth and tax affairs. Mike Walker, a partner in the firm's private client advisory practice, Derek Scott, Associate Partner and head of the firm's tax investigations unit, and Mariam Moi, one of KPMG's senior managers, outlined the issues and led the discussion.

The KPMG team explained the numerous ways in which banks are now being required to disclose more information about their clients' activities (for example, the financial statements of trust structures that could previously be kept confidential), and, more broadly, how the concept of 'privacy' is changing in the financial world. ■

ABOVE LEFT: **On the left, Peter Bibby from Brown Rudnick, explains a point to the attendees. Francis Kean, from Willis Towers Watson, is sitting fourth from the left.**
ABOVE RIGHT: **George Kanaan, with, L-R, Derek Scott, Mariam Moi and Mike Walker from KPMG.**

Our corporate lunch programme aims to give our corporate members direct access to subject matter experts in an informal setting.

# Celebrating Shakespeare!

## *Arab Banker's* guide to enjoying England's greatest playwright

2016 marks the 400th anniversary of the death of William Shakespeare so it is no surprise that this year the British cultural scene has been full of events celebrating the life and works of Britain's greatest playwright.

But how far does Shakespeare's appeal stretch? Aren't his plays too serious? Aren't they about obscure English kings that no one outside a university history department has ever heard of? And isn't it all written in sixteenth-century English that even English people find hard to follow?

"Not at all," cries Lady Penelope Cobham, a Trustee of the Shakespeare Birthplace Trust and Chairman of Visit England. "Shakespeare wrote his plays to be understood and enjoyed by everybody, from the highly educated Lord to the illiterate peasant, and his storylines address universal themes such as love, jealousy, family feuds and the use of political power."

And the Middle East? Is there anything that will strike a chord with those who have worked and lived in the region? "A huge amount," says Lady Cobham. "There are numerous references to the Middle East in Shakespeare's work, and the plays are regularly performed by Middle Eastern actors who adapt his plays to reflect local conditions."

More importantly, there are numerous ways to engage with Shakespeare in addition to watching or reading his plays. A visit to Stratford-on-Avon, his birthplace, provides a window onto Shakespeare's life and onto a crucial period in English history.

The *Arab Banker's* Editor, Andrew Cunningham, spoke to Penelope Cobham about Shakespeare's connections to the Middle East, and how those from the region can both engage with Shakespeare's plays and learn about this life and times.

You might be surprised to hear this, but the Middle East looms large in Shakespeare's plays. *Othello*, one of Shakespeare's greatest characters was a Muslim from North Africa, and so were Pericles, Prince of Tyre (in modern Lebanon), and the comic character of the Moroccan Prince in *The Merchant of Venice*. The opening scenes of *The Tempest* portray the Duke of Milan returning from Tunis, where his daughter has been married to the King of Tunis.

There's even a reference to the Prophet Mohammed in the first of Shakespeare's trilogy of plays about the English King Henry VI.

Reflecting the attitudes of the times, not all Muslim characters are portrayed sympathetically. Aaron the Moor, in the play *Titus Andronicus*, is a murderous villain. Othello, as a Muslim, is condemned for his love of Desdemona, a Christian.

On the other hand, in his comedy *Twelfth Night*, a character comments favourably on the fabulous wealth of the ruler of Persia, known as the 'Sophy', while another character is tricked into believing he has to conduct a sword fight with an unassailable enemy, who had been 'fencer to the Sophy'.

These references are not accidental. There was considerable engagement between England and the Muslim world during the reigns of Queen Elizabeth I (1558–1603) and King James I (1603–1625). This engagement is expertly explored in Jerry Brotton's recent book, *This Orient Isle*, essential reading for those who want to learn more about early contacts between Britain and the Muslim world.

The Levant Company had been founded in 1581 to develop the silk trade with the Ottoman Empire. In 1600, the ruler of Morocco, Mulay Ahmed al-Mansur, sent an ambassador to London to negotiate an alliance with Queen Elizabeth, and in 1619 Shah Abbas I of Persia granted the East India Company (which had been established in 1600) trading rights at all Persian ports.

Shakespeare was not alone in making references to Muslims and to what we now call the Middle East. Writers such as Christopher Marlowe and the now largely forgotten William Percy and George Peel all wrote plays that were centred on Middle Eastern characters and events.

But, the question remains, if your interest in Shakespeare has been aroused, how do you engage with him?

"Arab writers have been engaging with Shakespeare since the late nineteenth century," says Penelope Cobham. "At first, Arabic versions of plays such as *Hamlet, Othello* and *Macbeth* were produced, sometimes with scenes and plots changed, and endings re-written. Over time, this led to more exact translations of the texts. We know that *Othello* was performed in Arabic in Egypt in 1884."

The Arab League, founded in 1945, established a programme under its Cultural Committee to produce professional


**The title page of Mohammed Hamdi's translation of *Julius Caesar*, published in Cairo in 1912**

translations of Shakespeare's plays.

Productions of Shakespeare's plays continue to be very popular in Arab countries today, both in English and in translation.

In 2007, Suleiman al-Bassami's *Richard III, An Arab Tragedy* – which substitutes a despotic ruler of a Gulf sheikhdom for Shakespeare's villainous English king – was produced in Stratford, New York and Damascus. Performed in Arabic by an Arab cast, it was made accessible to non-Arabic speakers through subtitles projected around the stage.

In 2012, the Globe-to-Globe Festival – launched by London's Globe Theatre – sponsored versions of Shakespeare in 37 different languages, including Arabic. The Palestinian theatre group Ashtar performed a version of *Richard II* while an Iraqi company performed *Romeo and Juliet in Baghdad*, a version of the play that had Romeo as Shi'a and Juliet as Sunni in post-Saddam Iraq, and their families feuding not only as a result of religious differences but also due to an old business dispute involving ships and pearl diving.

But you don't need to wait for the next Arabic Shakespeare production to get to know with Shakespeare and his world.

For those in London, there is the Globe Theatre, on London's South Bank, about 20 minutes walk from Waterloo Station and about 10 from London Bridge Station. The Globe is a replica of Shakespeare's own theatre, with the cheapest tickets being sold to those who stand in front of the stage rather that sitting in the balconies around it. The theatre is also open to the sky and performances sometimes have to be suspended due to rain! The Globe has a permanent exhibition that explores Shakespeare's life and the areas of London where he lived.

The South Bank was the 'bad' area of London during Shakespeare's day, full of drinking houses, brothels ... and theatres. In contrast, the areas north of the river (where the City of London is today) were more sophisticated.

Shakespeare was living during a fascinating time in English history. There was long-running religious conflict between Catholics and Protestants, with the Spanish king actively supporting the Catholic cause and trying to overthrow Queen Elizabeth (most famously with the Spanish Armada, a huge invasion force sent in 1588). In 1604, the same year that Shakespeare wrote his plays *Othello* and *Measure for Measure*, anti-government protesters were arrested just hours before they could implement a plot to blow up the Houses of Parliament, with King James I inside.

To fully experience Shakespeare, a visit to Stratford-on-Avon is essential.

Shakespeare was born in Stratford in 1564, went to school there and married a local woman, Ann Hathaway. After many years performing and writing in London, he returned to Stratford for the last 19 years of his life and wrote some of his most famous plays.

Stratford-on-Avon (not to be confused with the areas of east London called Stratford) is about a two-and-a-half hour drive from London, or about two hours by public transport. It has plenty of good hotels and restaurants.

There are several sites with connection to Shakespeare in or near the town. These include his birthplace in the town centre, Holy Trinity Church where he is buried, and the home of his daughter, Suzanna. A short walk from the town is the house of his wife. The house of his mother, Mary Arden, is a 10-minute drive down the road. Mary Arden's house is now kept as a working sixteenth-century farm, and is fun to visit for both adults and children.

Penelope Cobham singles out Shakespeare's 'New Place' as something every visitor to Stratford must see. This is Shakespeare's family house, which he had built after he returned to Stratford from London and where he wrote plays such as *The Tempest*, *The Merchant of Venice* and *Pericles*.

The 'New Place' has been re-built as Shakespeare knew it with beautiful a garden filled with the plants and herbs that were common in Shakespeare's day. There is also an exhibition about Shakespeare's life and works.

Although Shakespeare dominates Stratford (don't forget the two theatres, home to the Royal Shakespeare Company) there is plenty more to see, such as a twelfth-century church and the old-style Falcon Hotel. You can also hire small boats and take a trip down the River Avon (mind out for the swans!).

One last thing...

What about Colonel Ghaddafi's claim that Shakespeare was actually "Sheikh Zubeir", an Arab merchant living in London? (And it is true that Arab traders did live in London at the time...) Penelope Cobham laughs. "That was just another of the Colonel's flights of fancy," she says. "Shakespeare was as English as anyone can be, but his plays are for all of us, wherever in the world we may come from." ■

**ABOVE: Shakespeare's chair, on display at the 'New Place' in Stratford-on-Avon.**
**BELOW: The garden of Shakespeare's family house in Stratford-on-Avon (the 'New Place') with the Swan Theatre in the background.**

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# Book reviews

## Britain in the Middle East, 1619–1971
### Robert Harrison
**Bloomsbury, 2016. £19.99. 283 pages**

## What the British Did: Two Centuries in the Middle East
### Peter Mangold
**I.B. Tauris, 2016. £25.00. 372 pages**

## The Poisoned Well: Empire and its Legacy in the Middle East
### Roger Hardy
**Hurst, 2016. £20.00. 243 pages**


Foreign intervention in the Middle East has a particularly bad name these days. The invasion of Iraq 2003 is almost universally believed to have been a disaster, and the intervention in Libya has been followed by five years of civil war. Western intervention in Syria has been erratic and has been ineffective in producing its desired results.

Western engagement in the Middle East is of course not new, as each of these three books shows. Robert Harrison begins his description of Britain's involvement in 1619, the year in which Sir Robert Roe signed Britain's first trade agreement with Safavid Persia.

British firms, such as the Moscovy Company, the Levant Company, and of course the East India Company, had been trading in the East for some years prior to 1619, but Roe's agreement was the first to be concluded with a Middle Eastern power.

British involvement intensified during the late seventeenth and the eighteenth centuries, primarily in Persia and the Arabian Gulf. Aden was occupied in 1839 by an officer of the East India Company in response to the expansionary policies of Mohammed Ali of Egypt.

The French invasion of Egypt in 1798 opened an important new chapter in the story of western intervention in the Middle East. Both Harrison and Mangold devote significant space to the Anglo-French rivalry and to the eventual British hegemony. Initially crucial in guarding the route to India (the Suez Canal opened in 1869), Egypt was later central to Britain's Middle East operations during the two world wars.

All of these three books provide frank but fair appraisals of British and wider Western intervention in the Middle East.

Harrison's book offers the widest historical view, beginning in 1619 and taking the story to Britain's withdrawal from the Gulf in 1971.

Chronologically, the bulk of his book focuses on three time periods: the seventeenth and eighteenth centuries, when the East India Company developed trading posts in Persia, the Gulf and Egypt; the mid-nineteenth century, which includes the high point of the Eastern Question and Britain's successful efforts to preserve the Ottoman Empire while also taking effective control of Egypt; and the decline of empire in the twentieth century.

A lot of space is devoted to Egypt, and in particular to events preceding and following the British assumption of control in 1882. The 1840 'London Treaty' that ended Mohammed Ali's threat to the Ottoman Empire is well explained.

The author occasionally lapses into irritating colloquialisms: one battle is described as a 'five week slugfest' and Reza Shah is said to have 'trashed' a British-sponsored security treaty.

Nonetheless, the book contains plenty of good detail (for example, that the Yemeni port of Mocha was one of the East India Company's most important outposts in the Middle East in the early nineteenth century) but Harrison is also good at standing back from the detail and quickly providing a sense of perspective. (From 1838 to 1856, Britain had to use force on four occasions to crush adversaries: Aden, Afghanistan, Egypt and the Crimea.) The chapter on the Second World War is particularly good.

However, the period from 1945 to 1971 receives only 20 pages, including less than two on the withdrawal from Aden – Britain's only colony in the Middle East – and a single paragraph on the withdrawal from the Gulf.

Peter Mangold begins his narrative in 1798 but he also scrutinises early eighteenth century involvement in Persia, the Gulf and Aden as he takes the story rapidly forward to the First World War and its aftermath. Mangold not only devotes significant space to the post Second World War dissolution of British influence, but he also continues the story to the present day. For those new to the Middle East, the final chapter, covering the first Gulf war that followed Saddam Hussein's invasion of Kuwait in 1990, the invasion of Iraq in 2003, and the rise of the 'Islamic State' group is worth reading on its own. Mangold identifies the timing of the end of the first Gulf war (ending it before Saddam had been overthrown) and the failure to plan for the aftermath of the 2003 invasion as the most serious misjudgements in the region of modern times.

The final two chapters give a fair assessment of British actions in the region. He does not gloss over failures and mistakes, but he is also careful to recognise the context in which British officials made their decisions, and the political and cultural norms during the time they were taken.

Hardy's book is shorter and less detailed, though he does not confine his focus to British intervention. Each chapter addresses a separate geographical area, such as Arabia, Egypt, Iraq and Persia. Hardy alone of the three books devotes space to Algeria and its fight for independence. He is good on British disengagement from Aden – one of the most significant elements of British colonial history, and one of the least distinguished.

Harvey is also good on the Sykes–Picot agreement – one hundred years old this year and the subject of much loose analysis. "It has become fashionable to say that the Sykes–Picot agreement … has been torn up, leaving a scarred landscape of failed and failing states." This is to miss the point, Hardy says. "It is not the 'lines in the sand' – the borders inherited from the colonial era – that are the heart of the problems of the Middle East, but what goes on within them. Islamism, the Arab Spring, and global jihadism are the products, not of artificial borders, but of long-simmering crises of state."

What emerges from all of these books are the complex and varied consequences of foreign intervention in the Middle East. The Second World War – whose origins lay in disputes between the world's major powers – brought destruction to many areas of the region, but Allied victory saved the Middle East from rule by a victorious Hitler. Exposure to the West facilitated the partial modernisation of economies such as Egypt's and opened Middle East religion and culture to different ideas, yet high-handed disregard of local leaders – the overthrow of Reza Shah and of Mossadeq in Iran, and the bullying of King Farouk in Egypt come immediately to mind – left the region with poor foundations on which to build modern states. The army was often the only national institution in which colonial administrators consistently took an interest and, when it suited them, developed.

So which of these books would this reviewer recommend? Hardy's is the shortest and easiest to read – it could be comfortably digested during the course of a flight from London to Dubai. Those seeking a more detailed and robust approach, including an appreciation of what was driving British policy and the structures through which policy was exerted, should turn to Mangold. Harrison is also good, and only he chronicles the early years of intervention. ■

*Andrew Cunningham*

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## From Banking to the Thorny World of Politics

### Shaukat Aziz (with Anna Mikhailova)

**Quartet, 2016. £20.00. 325 pages**

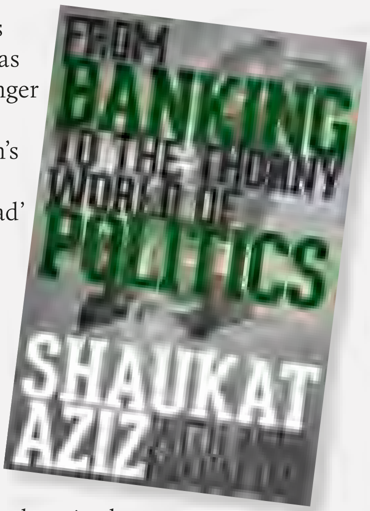
Shaukat Aziz must stand as one of the most successful bankers of the modern era. His career with Citibank took him from Pakistan to the Middle East and then to the highest ranks of the bank. He was an Executive Vice President in New York in 1999 when he was called by Pervez Musharraf, newly installed as President of Pakistan, and asked to return to his homeland as Finance Minister. From 2004 until 2007, he served as Prime Minister, and was the first Prime Minister of Pakistan to serve out a full term.

This book of memoirs covers his early life, his time with Citibank and his government service in Pakistan, as well as giving Aziz an opportunity to air his views on a range of global issues.

The book is divided into easily digestible chapters. It does not dwell on the early years, and it gets straight into the subjects that readers are going to find most interesting.

The main value of the book is in providing a high-level Pakistani perspective on global events. The chapters on India are particularly interesting. Regardless of whose side you take in the long-running feud between India and Pakistan, Aziz's book will leave you better informed and more understanding of Pakistan's position (for example, if you're not a specialist in the region, you probably won't have heard of India's 'Cold Start' military doctrine, introduced in 2004, and the way in which Pakistan responded).

The chapters on China describe Pakistan's role in facilitating the thaw in relations between the US and China (it was from Pakistan that Henry Kissinger made his first secret visit to China in July 1971), and Pakistan's relationships with China today, including the 'One Belt One Road' policy that includes Chinese financing for roads from China through Pakistan to the port of Gwador, giving China access to the Gulf and the Indian Ocean.




The book also provides insight into recent Pakistani politics, including the political career of Benazir Bhutto (again, if you are not a specialist, there is plenty here that will be new), and the Pakistani economy, including Aziz's successful efforts to get Pakistan out of the IMF's tutelage. He describes the devastating effects of the 2005 earthquake in Kashmir, and he bravely takes on the question of whether the Pakistani authorities knew that Osama bin Laden was living in Abbotabad. (They didn't.)

Aziz also gives an account of his time with Citibank. Those with long memories will recall that Aziz successfully restructured Saudi American Bank, Citi's joint venture in Saudi Arabia, after the oil price collapse of the early 1980s – Aziz describes this as the turning point in his career with Citi. But there is plenty in this book about his later years, and the lessons that high-level international banking provides for those who are responsible for governing countries.

The book is well written, with a fast pace. It will be of interest both to bankers and to anyone who wants a better understanding of the Middle East and of Asia. ■ *A.C.*

## Aleppo: The Rise and Fall of Syria's Great Merchant City

### Philip Mansel

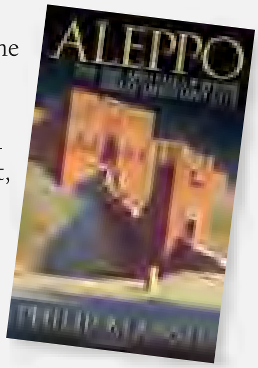
**I.B. Tauris, 2016. £17.99. 250 pages**

Philip Mansel's description of Aleppo illuminates the city's regional significance within the Levant and across transcontinental trade routes while also presenting a picture of different religious communities living side by side in a way that is inconceivable in the Middle East today.

The book is divided into two parts. The first 60 pages chart the history of Aleppo from the sixteenth century to the present day. Most of those pages cover the period of Ottoman control. Only a handful address the reign of the Assads, so those seeking a modern history of Aleppo, or an account of its travails during the current civil war, should look elsewhere. (Charles Glass's article in the December 2012 *New York Review of Books*, updated in his short book *Syria Burning*, would be a good place to start.)

The second part of the book comprises extracts from the writings of Western travellers in the East. Inevitably, some of these are more interesting than others, but many provide fascinating details about daily life in Aleppo during previous centuries.

Mansel has written widely on the Levant and the Mediterranean and his breadth of knowledge enhances this book. Although not a port city – Aleppo's nearest port, Alexandretta (present-day Iskanderun) was 100 miles away – Aleppo stands alongside Thessalonika (Salonica), Izmir (Smyrna), Alexandria and Istanbul (Constantinople) as one of the great cities of the Eastern Mediterranean and the Levant. These were cities that, in former times, thrived on a rich and diverse ethnic and religious mix: Muslims, Christians, Jews, Armenians and others. Reading this book, one again laments the loss of such diversity and tolerance in the Middle East, and the suffering and loss that has been the result.




The book's early chapters show the extent of trade and diplomatic interaction between European powers and the Levant, including Aleppo, during the seventeenth and eighteenth centuries – interaction that was between equals rather than between dominant Western powers and fading Orientals.

In the mid-eighteenth century, Aleppo was also significant as a major city on the land route from Europe to the East. From Aleppo, traders would travel to Basra and then by sea through the Persian Gulf to India and beyond. This land route to India took six months compared to nine months going round the Cape of Good Hope. Faster ships began to compromise this advantage, and the opening of the Suez Canal in 1869 destroyed it.

But the decline of Aleppo had begun before the cutting of the Suez Canal. A major earthquake in 1822 destroyed much of the city. Writing in 1831, the British traveller Francis Newman described "internal signs of decay", noting that when buildings collapsed, the rubble was left uncleared, while camels died in harness, their carcasses left to rot in the streets.

When the French mandate was established after the First World War, the country's capital and principal institutions were placed in Damascus. "Like other pre-1914 international cities such as Trieste, Salonica and Constantinople ... (Aleppo's) horizon's had narrowed," says Mansel.

In his final chapter, entitled, 'The Death of a City' Mansel notes that of all the mixed Ottoman cities, inhabited by different races and religions, Aleppo survived longer than most. Salonica was Hellenised; Constantinople and Smyrna Turkified; Alexandria Egyptianised; Nicosia, Sarajevo and Baghdad sectarianised; and Beirut gutted by civil war. But since 2012, Aleppo too has been destroyed. ■ *A.C.*

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## Intermediate Islamic Finance

### Nabil Maghrebi, Abbas Mirakhor, Zamir Iqbal

**Wiley, 2016. £60.00. 391 pages**


This book provides a detailed account of financial market theories and some consideration of the applicability of such theories to an Islamic financial market. It is not, and is not intended to be, an account of Islamic finance in practice. (No Islamic bank appears in the book's extensive index.)

The authors are noted experts on Islamic finance, and Mirakhor and Iqbal are the authors of Wiley's *An Introduction to Islamic Finance*.

The book opens with a chapter entitled, 'The Epistemology of Finance' and proceeds to a consideration of financial ethics, after which it examines key pillars of financial market theory such as theories of interest, market efficiency and the valuation of financial instruments. At all times, the analysis is supported by copious references to recent academic papers and books.

The authors ensure that conventional financial market theories have been fully examined before turning their attention to the specific aspects of Islamic finance. The chapter on Financial Engineering and Derivatives runs for 45 pages before turning its focus to the valuation of ijarah contracts and the permissibility of risk hedging, though the chapter on Securitization and Structured Finance devotes proportionally more space to Islamic finance, and includes useful analysis on how a double wa'd structure can be employed to replicate the economic effects of total-return swaps and short-selling. The chapter on financial stability comprises a masterful review of the post-crisis literature on financial market failures, and adds a consideration of how an Islamic financial system based on risk sharing rather than debt might be immune to such crises.

This book will be welcomed by readers familiar with financial market theory who are looking to extend their knowledge of conventional finance into the realm of Islamic finance. ■ *A.C.*


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