

Address by
HRH Crown Prince of Perak, Malaysia
Raja Nazrin Shah
Financial Ambassador for the Malaysia International Islamic
Financial Centre (MIFC)
at
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Assalamualaikum Warahmatullahi Wabarakatuh

Bismillahi Rahmani Rahim

I have indeed been blessed by the Almighty S.W.T. to be given this opportunity to be a guest of the Kuala Lumpur Business Club and to address you all this afternoon. It is a privilege to share some thoughts about our countries and how we might cooperate in ways that are closer, productive and more mutually beneficial.

2. My remarks will begin on the global stage and then proceed to drill down to some specifics. Since the early 1990's, with the end of the Soviet empire and the entry of Eastern European countries into the world market economy, with the opening up of the fast-growing economies of China and India, and with rapid globalization and deregulation elsewhere, especially in East Asia, many investment opportunities have become available.

3. All these opportunities carry with them a measure of risk. It is evident from the vast amounts of foreign investment that is made each year, however, that there has been a significant decline in the “home bias” in investment, that is, a decline in the tendency to invest savings in one’s home country as opposed to abroad. Investors today are more comfortable doing business in unfamiliar investment environments than ever before. The risk-adjusted rate of return, a key factor that determines which countries become foreign investment destinations, has accordingly become less demanding relative to investing at home.

4. While this is true, it should be noted that a large part of global foreign investment flows have been to the developed world, especially the US. The US received 60 per cent of all cross-border savings of the 67 countries that ran current account surpluses last year. Reputable economists have argued that this is because over the past decade, the higher rates of productivity growth in the US have raised risk-adjusted rates of return and led to a global demand for US-based assets. Of course, other factors are also responsible, including a greater sense of comfort with market and political risk, greater transparency, liquidity and good governance practices.

5. Let me now focus on Malaysia. In the 50 years that Malaysia has been an independent nation, it has had an open economy. It has been an active participant in cross-border trade and investment, the latter both physical and, more recently, financial. From being an economy with a narrow commodity base at the time of independence, it has become a middle-income and industrialized economy of some importance. The economy is diversified and while the manufacturing sector still dominates, the services sector is growing rapidly.

6. Since the Asian Financial Crisis a decade ago, economic growth has been achieved with relative price stability, low unemployment and strong external balance. The economy has been able to sustain the growth momentum and diversified the economic structure. Real GDP registered a growth rate of 5.9 percent in 2006 and is expected to expand by 6 per cent in 2007. The level of savings remains high, while the

level of external reserves remains strong at USD98.5 billion as at end-July 2007. This has given Malaysia a strong ability to withstand possible financial volatility originating from the external environment. In 2006, the total value of external trade exceeded RM1 trillion for the first time, while foreign direct investment has been sustained at comfortable levels. Private sector activities continue to drive the growth momentum while the public sector plays a supportive role.

7. Prospects for growth for the whole of 2007 remain positive as the economy is expected to benefit from resilient domestic demand and favourable growth performance in Europe, Japan and Asia. The services and construction sectors are expected to perform better due to stronger consumption and public expenditure. In addition, private investment activity will be reinforced by the implementation of the Ninth Malaysia Plan projects by the public sector.

8. The Government continues to promote greater flexibility for the economy to achieve a more diversified economy. Malaysians have enjoyed stability on multiple fronts – political, financial, economic, monetary and social for most of the last five decades. This has contributed to high levels of foreign direct investment. The Government continues to engage the business sector to ensure that the investment climate is further improved and is set to reduce corporate income tax to 26 per cent in 2008 and 25 per cent in 2009 from the current 27 per cent.

9. Economic and financial linkages between Asia and the Middle East are growing. While world trade has, on average, expanded by 10 per cent per annum over the 2001-2005 period, Asia's trade with the Middle East has increased by an average of 24 per cent. More than half of the exports from the Gulf States go to Asia and more than one-fifth of its imports are from Asia. The Gulf is the major supplier of fuel to Asia, while Asia in turn supplies manufactured goods and food to the Gulf.

10. Equally significant are investment activities. Since 2005, investment projects amounting to more than USD160 billion to be financed by the Gulf States in Asia have been announced. In 2006, mega-deals involving corporate acquisitions and real estate

purchases by the Gulf States in Asia are estimated to total more than USD18 billion, including multi-billion dollar IPO purchases in financial institutions in China, large oil refineries and telecom companies. The value of these investments is expected to increase to between USD20-30 billion in 2007.

11. Historically, trade and investment in Asia and the Middle East have been linked to the developed economies. However, it is now increasingly recognised that there are significant complementarities between our two dynamic regions. These complementarities provide a platform for two-way flows that enhances income and wealth creation. The different demands of each respective region reinforce the significance of the complementarities. Such investment opportunities continue to support the growth momentum in the region. At the same time, Middle East domestic infrastructure requirements are estimated to total USD500 billion for the next five years, and Asian companies have demonstrated the capacity to provide the technology, expertise and human capital to meet these infrastructure demands.

12. The Malaysian capital market offers a wide range of possibilities for investment, direct participation as well as intermediation. Currently, 86 per cent of our listed companies are *syariah*-compliant and 65 per cent of the market capitalisation of our stock exchange is accounted for by *syariah*-compliant companies. This offers investors a range of *syariah*-compliant investment opportunities in the equity market.

13. Malaysia is committed to, and extensively engaged in, strengthening linkages through Islamic finance. The country offers to serve as an investment gateway to the region, specialising in Islamic fund and wealth management, as a platform for the issuance of *sukuk* and as a centre for *takaful* and *retakaful*. This is an important gateway that provides linkages to other international Islamic financial markets and thereby provides the potential for expanding investment and trade relations between the Middle East and North Africa regions, and East Asia.

14. In positioning Malaysia as a reputable International Islamic Financial Centre or MIFC, the Government has introduced various measures directed at enhancing

institutional capacity, forging strategic alliances, embarking on promotional initiatives and enhancing *syariah* initiatives for convergence and harmonisation. Malaysia's approach toward *syariah* interpretation is that while we support serious efforts towards *syariah* harmonisation, we respect diversity of interpretations amongst various jurisdictions and hence adopt a "mutual recognition" approach.

15. We have allowed the entry of reputable foreign Islamic financial institutions from the Middle East, which has contributed to the acceleration of the liberalisation of our Islamic financial system to become an Islamic financial hub. We have further liberalized the domestic Islamic financial industry to allow for foreign ownership of up to 49 per cent of the total equity in existing Islamic banks and *takaful* operators.

16. To further entice foreign investment, the Government has relaxed the Foreign Investment Committee rules to allow for 100 per cent foreign equity ownership in International Islamic Banks (IIB) and International Takaful Operators (ITO). These firms will enjoy a range of tax incentives including tax exemption on income earned and all funds managed can be invested in foreign currency-denominated instruments. In order to develop Islamic fund management, wholly foreign-owned Islamic fund management companies are now allowed to have a presence in Malaysia. The Government is also offering stockbroking licenses to qualified firms that can play a role in broadening the Middle East investor base into Malaysia and the region.

17. Malaysia maintains a highly liberal foreign exchange regime that provides an attractive gateway for movement of funds relating to foreign direct investment and portfolio capital investments. Foreign investors are free to hedge their positions and various Islamic financial hedging instruments have been devised to facilitate this.

18. All these are aimed at creating a conducive and dynamic environment for Malaysia to become the preferred investment and fund raising destination for the global financial community, particularly from the Middle East.

19. Allow me at this juncture to make an important point. Some see Malaysia's Islamic Centre as a threat to Dubai's aspiration of itself becoming one. Why, it has been asked, should Dubai assist a competitor?

20. While this sounds reasonable in theory, it is not in practice. The market for Islamic products is only in its infancy. If we have only a limited number of financial institutions and products - whether in Kuala Lumpur or Dubai – we risk affecting the development of the infant.

21. By allowing the market to grow and by allowing issuers and investors choice of quality, services and products, both countries will in fact be working in complementary ways towards a common goal.

22. This brings me to a related point. It is worth noting that Malaysia is at the center of ASEAN, the Association of Southeast Asian Nations. The population of ASEAN is coming on to 600 million, with a broad demand profile ranging from the more basic in its relatively less developed parts, to the sophisticated at the top end. The integration of the market is already taking place, and the early bird will obviously have first-mover advantages.

23. Malaysia has the advantage of being close to both potential issuers of syariah-compliant products and investors. Our institutions are closer to the ground and can work with those seeking capital, as well as potential investors. This opens up more natural opportunities for the two financial centers to lead, manage and place financial products.

24. All this means that it is in Dubai's interest to see the MIFC grow and vice versa. This is not a zero sum proposition. It is a win-win outcome.

25. For its own part, Malaysia is positioning itself to take advantage of globalization, greater competition and newly-emerging patterns of economic integration. Even as we pride ourselves on our achievements, we are seeking further improvement. Greater transparency and better governance will only lead to higher economic benefit. Government delivery systems are being enhanced, so as to reduce time to market. Policies and procedures are being streamlined further to achieve an ideal business climate.

26. There is a massive process now taking place in Malaysia to bring development to all regions in the country. This will enhance political stability while bringing economic benefit to both people and business. In the process the economy is also being brought up the value chain. The Iskandar Development Region is one such ambitious project, which has already attracted investment commitments, for example, from Dubai World. Other economic development regions have been, and are being, launched throughout the country, offering opportunities in tourism, modern and technologically-driven agriculture, oil and gas, and many other fields. The property and real estate opportunities on offer are outstanding.

27. All of this is occurring in an investment environment that is politically safe, sound and predictable. Factors of production, namely capital and labour, have been put to work to achieve this record. In order to attain greater productivity in a globally competitive environment, there is much greater emphasis in Malaysia on capable, efficient and innovative human capital and in the use of technology. We are on the march up the value chain, without vacating areas in manufacturing and the services sector where we have comparative advantage. We are bringing the application of technology and innovation to grind a better margin and are pushing into biotechnology, environmental and human sciences.

28. Earlier, I spoke about the growth and development of the Islamic financial industry in Malaysia. The Malaysian capital market today has developed as one of the more comprehensive in the Asia-Pacific region and among developing economies. In the Islamic capital market area, we have several pioneering and attractive structures in Islamic financial products. We issued a sovereign 5-year global *sukuk* of USD600 million in 2002, Islamic residential mortgage backed securities in 2005 and the Islamic Real Estate Investment Trust in 2006. In addition, the pioneering work of the *syariah* Advisory Council (SAC) has attracted considerable interest and Malaysian-designed *syariah* structures are increasingly being adopted in the global marketplace and Malaysian *sukuk* issuances are usually over-subscribed.

29. The potential for further development and expansion of Islamic financial products is tremendous. We see the Islamic capital market as a high growth market segment. There are several Islamic product segments that offer significant potential. These include exchange traded funds, structured products and the entire spectrum of the Islamic asset management industry encompassing fund and wealth management, unit trusts, financial planning, venture capital and private equity.

30. Malaysia, with its strong linkages with the Middle East and other Asian markets, is well placed to provide *syariah*-compliant financial services to support trade flows between Asia and the Gulf States. One good example is the signing of the mutual recognition agreement by the Securities Commission (SC) with the Dubai Financial Services Authority (DFSA). This is the first such agreement between two Islamic markets, and allows for cross-border distribution and marketing of Islamic funds in the DIFC and Malaysia with minimal regulatory intervention.

31. The areas for cooperation and potential for investment in our two countries and regions are great. One possible area is to tap the Islamic capital markets to finance infrastructure development in the less developed countries. The multilateral banks have taken a lead role in this. For example, the World Bank and the International Finance Corporation have all issued *sukuk* in Malaysia for financing infrastructure development. Malaysia would certainly welcome the opportunity to collaborate with you to use both our

Islamic capital markets to recycle global wealth into capital formation and economic development.

32. Malaysia's regulatory framework already offers end-to-end *syariah*-compliance within a complete market. For example, a *syariah* investor can bank in Islamic banks, invest through Islamic windows to purchase *syariah*-compliant stocks directly or purchase a broad range of Islamic products such as unit trusts, bonds or real estate investment trusts and also get *takaful* coverage along the way.

33. However, it is important for Islamic financial products to gain the full trust and confidence of investors and issuers. Thus, a key feature of Malaysia's regulatory approach is to ensure a comprehensive Islamic financial system that co-exists with the conventional financial system and one that provides all participants the same degree of clarity, certainty and protection.

34. Malaysia adopts an open architecture for its Islamic capital market. What this means is that domestic and international conventional players actively participate in the Islamic capital market. For example, USD-denominated *sukuk* sold out of Malaysia are always over-subscribed by both conventional and Muslim investors and conventional issuers also tap the Islamic capital market for funding. Malaysia's Islamic capital market therefore offers the right balance between *syariah*-compliance, competitiveness, pricing and product integrity.

35. There are other opportunities which I cannot do justice to in a general address of this kind. They will only become apparent when one looks at them first-hand and does the hard number crunching. We should allow for the fact, however, that the process of discovery may also not take place all at once but be on a progressive basis. If we are able to forge strong bonds of relationships, this will facilitate information to flow freely between us and for the benefits of investments to be understood.

36. We have, on this KLBC mission, the Chairman of the Malaysian Securities Commission, the Deputy Governor of Bank Negara Malaysia and the Executive Director

of Khazanah Nasional Berhad, who will be expanding on these developments and, who I am sure, will be happy to take your questions. I will therefore end my address by thanking you all for your attention and wishing you all a very successful meeting.

Thank you.