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Presented by	YBhg Dato' Zarinah Anwar, Chairman, Securities Commission Malaysia
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Distinguished guests, Ladies and gentlemen,

Assalamualaikum warahmatullahi wabarakatuh, and good morning.

First, a word of thanks to Terrapin for inviting me to deliver this keynote address at the 2nd Annual Islamic Funds Asia Conference. This gathering of experts and industry players in Kuala Lumpur to discuss the development of a robust Islamic funds market in Asia is timely and appropriate. Most certainly, the unlocking of Islamic savings through efficient intermediation is an important challenge for all Islamic markets and it is a priority item on the Malaysian capital market development agenda as well.

Perspective on the Asian fund management industry

Asia has a varied investment management landscape - with the industry well established in Japan, Hong Kong and Singapore managing not only domestic savings but also functioning as the Asian outposts for the global fund management industry.

However, the fund management industry is still relatively in its infancy in many of the emerging markets in the rest of Asia. But, "emerging Asia" is accumulating wealth at a rapid pace – powered by a combination of oil revenues, trade surpluses, high savings

and youthful demographics. These strong industry fundamentals operate in an environment of economic reforms and market liberalization and will feed into strong Asian demand for investment products and fund management services in the coming decade.

The rapid pace of economic growth and accumulation of wealth in the Gulf States, the giant economies of China and India and the economies of the Far East are prompting investment institutions in the US and Europe to increase their portfolio exposure to Asian assets. These global institutions are also positioning their investment teams across Asia, not only to be nearer to the markets they invest in but also to take advantage of asset-gathering opportunities.

Similarly, Asian firms are being unfettered from the boundaries of their domestic markets through increasing capital account liberalization to venture into other markets. Typically, they prefer the newer Asian pastures which offer more untapped opportunities rather than the more mature and highly saturated markets in US and Europe.

With the fund management industry in Asia set to undergo a sustained period of rapid growth, the Asian markets are themselves competing to attract more international fund management companies to their shores while providing incentives for home-grown fund managers to grow and to expand regionally. As part of this process, many Asian countries are implementing extensive policy reforms on their tax and regulatory frameworks to strengthen their competitive positioning as a wealth management centre.

Challenges to building an Asian Islamic fund management industry

Ladies and gentlemen,

The Islamic fund management industry has gained increasing prominence especially since the rise in oil prices. McKinsey estimates that the revenue of Gulf states from oil and gas will be between USD2 trillion to USD3 trillion this decade. Already, as at 2006, the GDP per capita of the Gulf states is estimated at close to US\$20,000.

Despite the high levels of affluence, the Asian Islamic fund management industry is still relatively small - with the exception of some prominent Sovereign Wealth Funds and private equity investors. There is therefore an anomaly that needs to be addressed; that is the gap between the large surpluses and the nascent state of the Islamic fund management industry.

Quite clearly, there are missing gaps that are hindering the development of the industry that should rightfully occupy centre-stage in the Asian landscape and be the mechanism that ensures that Islamic savings are efficiently intermediated.

One major constraint to the evolution of a broad Asian Islamic fund management industry is the relatively scarce global supply of Shariah-compliant assets. The latent demand for Shariah-compliant assets is quite evident given the high over-subscription rates for most Shariah issues – whether they are equities or sukuk.

There is therefore a need for Islamic countries to collaborate to press ahead with the task of building Islamic capital markets at a much faster pace to meet the requirements of Islamic investors. The continued deepening and broadening of Islamic markets will be both a catalyst and an enabler for the rapid growth of the Islamic fund management industry. The rising need for efficient intermediation of Islamic affluence will therefore offer tremendous opportunities for markets offering Shariah-compliant products and services.

Apart from increasing the supply of Shariah-compliant assets, there is also a need to ensure that these markets are liquid and accessible to a broad range of investors – both domestic and global. In this regard, the Islamic intermediation value chain in many markets has yet to be fully developed and the numbers of specialized Islamic intermediaries – whether full-fledged or operating as a window of a conventional operation – is still insignificant. This then impedes the origination, distribution and trading of Islamic assets on a global basis.

In this regard, it is important that the Islamic fund management industry is not perceived as a “deposit-taking” institution that acts as a passive guardian of Islamic savings. It is critical that the Islamic fund management industry generate value-add for their clients through pursuing innovative strategies in managing assets. At the moment, most of the innovation for Islamic fund management is taking place in the traditional financial centres where advanced portfolio strategies such as absolute return and hedge funds are being replicated and extended to the Islamic arena.

The Asian Islamic fund management must therefore seek to expand the frontiers of possibilities in terms of active asset management strategies that are compliant with Shariah-requirements. This would certainly include building the expertise to invest in a broader range of asset classes particularly those with high alpha portfolios and to enhance the ability to deploy risk management strategies to insulate capital.

Most critically, it is important that Islamic fund managers also consider adopting activist strategies in engaging with companies to improve the value of their investments. The tangible benefits of good governance and activist fund managers that adopt an “owner operator” mindset have become increasingly evident and will contribute to the ability to generate superior rates of return.

Related to this, cooperation among the Islamic countries is also required to build capacity and to rapidly expand the number of Islamic finance professionals. There is a substantial shortage of professionals who are well-versed both with shariah and with finance. If the talent pool is not quickly expanded, these shortages will constrain the development of the Islamic fund management industry as well as the Islamic capital market.

Regulatory challenges

Ladies and Gentlemen,

Let me now turn to several issues that are important from a regulatory perspective. From a wider context, it is imperative that Asia's savings are carefully nurtured so that the Asian populations may meet their long-term requirements in terms of retirement savings, financing their children's education as well as paying for healthcare requirements. Against this background, investors and fund managers are increasingly seeking diversification and reduced portfolio volatility by placing funds in new asset classes and new markets. And, we can observe this trend from not only the evolution of the fund management industry but also the financial planning industry itself.

In this regard, the availability of a wide range of sophisticated products will provide fund managers and financial planners the ability to construct a portfolio for clients that comprise a diversified asset class and, even within each asset class, a broad range of products that provide the appropriate risk-return profile.

There is no doubt that the countries within the Asian region vary widely in terms of the level of depth, liquidity, and sophistication of their capital markets. But what is impressive is that capital markets in this region are also developing at a very rapid pace; reaping the benefits of institutional capacity building and other structural reforms as well as international portfolio diversification.

Thus, as with any story of economic growth and diversification, the challenge lies in addressing information asymmetry, inherent product complexity and general consumer mistrust and apathy. I therefore view as particularly important, the efforts that regulators in this region have made in improving their investment climate. There is considerable evidence to demonstrate that international capital flows are stronger and more stable for countries that clarify and strengthen investors' rights, corporate governance and accounting standards. And there are concomitant benefits that come from improving the financial infrastructure, such as the clearing and settlement process, as well as the supervisory and prudential framework.

At the same time, regulators and the industry must do more to ensure that investors themselves can look after their own interests by better understanding the nature of

managed funds generally, and also the risks and benefits involved in specific products. The issue of investor education therefore is especially pertinent in the region, where managed funds are relatively new and a proper understanding of personal investments is at an early stage.

These all place heavy responsibilities on the regulator to ensure that its fund management industry is well regulated, that they will treat their clients fairly and will manage funds in accordance with the clients' mandate. In that vein, it is also important to note that Islamic funds are invested according to the religious beliefs of their clients.

It is towards the objective of developing a comprehensive and integrated regulatory and Shariah compliant framework to provide investor protection, that Malaysia has adopted a regulatory approach to ensure that all participants in our capital market are provided the same degree of clarity, certainty and protection. In addition, we have recently established a specialized unit to strengthen our supervision of the fund management industry. We have moved towards a principles based approach to regulation where the focus is very much on outcomes - are customers being treated fairly; are conflicts of interest being managed appropriately; are financial instruments being valued fairly and in accordance with firm policies; and are the business risks being appropriately and vigilantly managed.

Our national Shariah Advisory Council has also developed an extensive set of guidelines on the various intermediation practices or products to provide clarity and consistency to market participants. Investors can now draw comfort from the availability of end-to-end shariah-compliance and its consistent practice in Malaysia's Islamic capital market. We issued the Guidelines on Islamic Fund Management in 2007 to promote greater clarity and consistency in Shariah-compliance for an Islamic fund management business carried out through a standalone operation or under an Islamic window. Overall, it is our objective to ensure that an investor in Malaysia's Islamic Capital Market can be assured of an investor protection regime that is among the best internationally.

The Malaysian Islamic investment management industry

Ladies and Gentlemen,

In Malaysia at the moment, the most prominent component of the investment management industry is the unit trust industry. In 1993, there were only two Islamic unit trust funds; today, the number of Islamic unit trusts in Malaysia has increased significantly to 128 funds with a net asset value of RM16.9 billion.

Apart from the unit trust industry, intensifying research and development work have resulted in the tremendous growth in the body of knowledge and financial sophistication. This has created a facilitative environment for the introduction of other Shariah-based collective investment schemes in Malaysia.

Malaysia also became the first market to release the Guidelines for Islamic Real Estate Trusts (REITs) in 2005 and this was followed by the launch of two Islamic REITs - with hospitals and plantations as their main assets. In January 2008, Asia's first Islamic ETF was launched. The MyETF Exchange Traded Fund is designed to track the Dow Jones Islamic Market Malaysia Titan 25. Within the wealth management industry, various structured investment product based on Shariah principles targeted at institutions and high net worth individuals have also been launched.

Ladies and gentlemen,

It is a priority for Malaysia to create an attractive and fully liberalized environment for the Islamic investment management industry. Therefore, under the Malaysia as an International Islamic Financial Centre or MIFC initiative, international participation in the Islamic fund management industry has been fully liberalized with the removal of restrictions on ownership and investment abroad. In addition, income tax exemption on fees received in respect of Islamic fund management activities was provided. In tandem with this, the SC will act as a one-stop centre to expedite the approval process for the establishment of Islamic fund management businesses in Malaysia.

In addition, Malaysia also recognizes the need to promote increased cross-border investments across Islamic markets. Towards this end, the SC signed a mutual recognition agreement with the Dubai Financial Services Authority (DFSA) for the cross-border marketing and distribution of Islamic funds between the two countries.

We also seek to attract Islamic fund managers to locate in Malaysia as well as to encourage Malaysian fund managers to expand their operations to other markets. At the same time, we continue to explore opportunities for further mutual recognition arrangements to promote cross-border distribution of Islamic products as well as origination and intermediation activities.

Conclusion

Ladies and Gentlemen,

If we are to aspire to take the Islamic fund management industry to new heights, greater efforts must be channelled into developing collaboration amongst countries to establish a thriving and vibrant global network of Islamic capital markets. This will create the opportunities to stimulate cross-border investment flows that so often act as a catalyst for development.

Malaysia is therefore committed to working closely with other centres to create an Islamic capital market network that can provide the linkages necessary for the optimisation of opportunities to unlock Islamic savings in Asia through effective intermediation processes.

On that note, I would like to wish all the participants an insightful and productive conference ahead.