UAE Global Investment Forum

Your Excellencies, Ladies & Gentlemen,

As I think back on the tumultuous events of the last 18 months in global financial markets I am reminded of the old Chinese proverb and curse “may you live in interesting times”. I for one must indeed be fortunate because I assure you that in my lifetime I have never seen times as interesting as this. Few, if any, would have believed in January of last year that 2008 would see the global financial system brought to its knees? Who would have imagined we would see a bellwether like as Lehman Brother, a 158 year old household name in banking file for chapter 11 bankruptcy protection. Nobody would have believed we would see names like AIG, Goldman Sachs, Morgan Stanley, JP Morgan, Bank of America and Citigroup to name just a few, lining up to be rescued from bankruptcy by the US Treasury. Of perhaps more relevance in the context of this event, who in this audience would have believed that 2008 we would see an unprecedented 73% wiped off MSCI UAE index. Interesting times indeed!

So where does this position us right now? The financial turmoil that started in the US has now spread to almost all developed and emerging countries, and become the most severe global financial crisis since the Great Depression. A recent working paper by the IMF examined the factors contributing to the last 123 recessions and attributed them to equity price busts, house price busts or a credit crunch. The current crisis appears to be only the 5th instance where all 3 factors occur simultaneously. Of course, past performance is not indicative of future results as we clearly warn in our marketing literature but as Mark Twain succinctly put it, “History doesn't repeat itself, but it does rhyme”.

Globally almost all financial institutions and a wide range of non-financial institutions have experienced strain during the crisis as asset prices collapse. Delinquencies and the house price bust was one of the major catalysts of the crisis, especially in the US where the banks have a combined exposure of 58 percent of total loan book to residential and commercial mortgages compared with 29 percent in the UK, 30 percent in Europe and 31% in Asia. This will continue to plague particularly US financial institutions until such time as the declining trend in house price deflation is reversed.

Another significant concern for global markets is the slowdown in the world trade, reflected in the Baltic freight and other shipping indices. In the last couple of months, the expectation of a US recession and global downturn has been exacerbated by a

significant contraction in credit and finance for trade. According to the IMF global output and trade plummeted in the final months of 2008, and it expects world trade volumes to contract this year, falling by 2.8 percent. The export led countries like Japan, China and others are already feeling the heat of the plunge in the global trade.

It's well accepted that emerging market economies, including the UAE and MENA region are in far better shape than their developed market counterparts. Emerging markets are playing an increasingly important role in global development with their share of global growth growing from 20% to 60% over the last 46 year with the UAE making a valuable contribution to this.

There are obvious structural differences between the developed economies and emerging economies, specifically in the context of leverage. Household debt as percentage of GDP for emerging markets is much lower than in mature markets; the MENA region for example has total household debt of 22.1% of GDP compared to a mature market household debt to GDP ratio of 79.5%. This is even more pronounced in the UAE where household debt to GDP is as low as 10%. These low levels of household debt provide a cushion in times difficulty by supporting consumption expenditure.

Despite the more favourable macro position, pressure on emerging markets intensified in September 2008, following the collapse of Lehman Brothers, as counterparty risks rose and as the credit crunch's impact on economic activity became indisputable. According to a recent report by IMF emerging market banks face mounting write-downs and require fresh equity as economic conditions deteriorate rapidly. Estimates of the potential scale of write-downs on loans and securities at emerging market banks have been rising sharply in recent months. Write-downs in emerging market banking systems, including in the subsidiaries of foreign parent banks, could reach $800 billion or around 7 percent of assets.

We are, however, starting to see the first signs of a thawing of the freeze in credit markets. Over the last few weeks we have seen a substantial tightening across emerging market CDS rates of between 40 and 100 basis points. This, together with equity market gains of 15-20 percent suggests that a bottoming process is underway as investors gradually become less risk averse.

As alluded to in my introduction, the global crisis has not spared the Middle East as a confluence of several factors prompted a pause in the exponential growth of the last 5 years. Amongst others the region has been impacted significantly by:

A substantial fall in the price of oil

A deterioration of external financing conditions and reversal of capital inflows

The local property and equity markets price collapse

A deterioration of domestic liquidity conditions

And a massive widening of credit spreads

The IMF estimates real GDP growth of 2.5% in 2009 for the MENA region with positive contributions coming from Qatar, Iran and other gas reach countries.

Like most countries around the world, this region has also experience a correction in real estate prices due largely to a lack of mortgage availability and a crisis of confidence. Mortgage penetration across the region, the GCC in particular is exceptionally low when compared to developed markets. In 2006, mortgage loans as percentage of GDP averaged 5% for the UAE, 1 percent for Saudi Arabia and 3 percent for Qatar and Oman compared to 73 and 87 percent for the US and UK respectively. While perhaps a contributing factor to the current woes, this relatively underdeveloped and underpenetrated mortgage market offers one the biggest opportunities for local financial institutions over the next 5 years.

According to Central Bank Governor Sultan bin Nasser Al Suwaidi, "the ratio of mortgage loans extended by local banks was only 17.8 per cent of the GDP at the end of 2008." UAE central bank figures show that the countries 24 national banks and 28 foreign units provided around Dh172.7 billion in real estate credit to the end of 2008, an increase of around Dh57bn from the start of the year. He said the loans remained below the banks' combined reserves of Dh180bn.

The local banking system remains stable and sound. Regional banks have been prudent in creating adequate provisions to cover nonperforming loans. GCC banks on aggregate raised provisions of more than 80% of nonperforming loans in 2007, a number which increased even further into 2008. Nonperforming loans as percentage of total loans for 2007 was also well under control with most of the regional countries seeing NPL’s of around 3% compared to much higher delinquency rates in mature

markets. UAE banks are also well capitalised compared to international peer. According to the UAE central bank, the average capital adequacy for UAE national banks stands at 16.4%, a high number by global standards.

I believe that the UAE is well positioned to whether the current storm and emerge from it in a dominant position. This is largely due to:

the wise leadership and prudent directions of the president H.H Shaikh Khalifa Bin Zayed Al Nahyan, close follow up of H.H Shaikh Mohammed Bin Zayed Al Nahyan, Abu Dhabi Crown Prince, deputy supreme commander of the UEA armed forces and the timely intervention of both local and federal authorities

A strong, well capitalised banking system

supportive national policies utilizing the buffers accumulated during the boom years.

high government expenditures filling the void left by the retrenchment of private sector activity

a myriad of measures implemented by authorities to shore up confidence and prevent a systemic banking crisis. These have included introducing blanket deposit insurance providing liquidity, and injecting capital into banks.

Interesting times breed interesting opportunities; perhaps we should consider the Chinese proverb to be a blessing rather than a curse, the recent interesting times have presented the whole finance industry with an opportunity to re-evaluate priorities and streamline operations. Survivors will exit this crisis in a formidable position, ready to face head on the challenges of the next phase in the UAE's economic development.

Thank You