Islamic Finance
Market Developments & Opportunities
May 16, 2007
Paris Dauphine
Where is this increasing wealth going?

- King Abdullah Economic City, Saudi Arabia
- The Palms Dubai, UAE
- Mall of the Emirates (Ski Dubai), UAE
- Burj Dubai, UAE

Eighth Wonder of the World

US$ 26.6 billion New City being built from Scratch

ERNST & YOUNG

Quality In Everything We Do
and raising consumption of luxuries

Business Times 14 December 2005

Gulf to find place in world’s top superyacht markets in a decade
BY A STAFF REPORTER

DUBAI — The Arabian Gulf region will be among the world’s top four superyacht markets within 5-10 years, according to a global transport finance expert.

“The Gulf has a strong maritime tradition that dates back over 200 years and it’s natural that it develops its relationship with the sea. This region currently has over 130 yachts in service which is almost 5 per cent of the world total.”

Khaleej Times 19 December 2005

Sales of Rolls Royce rise 36 pc in the Middle East
BY FACT FAREN

“The Middle East is one of the most important markets for Rolls-Royce, accounting for around 15 per cent of our world-wide sales.”

Last year, Rolls Royce sold 792 units world wide, up 36 per cent from the previous year.

Khaleej Times 12 December 2005

A waiting list for the latest Bugatti
BY LUCIA DORE (SENIOR CORRESPONDENT)

Already there is a one-year waiting list in the GCC for this handcrafted car, of which about five a month are manufactured. The car is priced at 1 million euros (4.3 million Dhs) excluding tax and transport costs.

Khaleej Times 15 December 2005

Middle East watch sales surge

Luxury watch brands are facing a global slump, but the Middle East market is booming.

East market is booming.

Khaleej Times 14 December 2005

Middle East leisure boat market reaches all-time high

Driven by strong growth in tourism in the region and demand for boats and leisure cruisers has reached an all-time high.

United Arab Emirates; Wednesday, October 05 - 10:31

Khaleej Times 12 December 2005

ME offers rich pickings for DaimlerChrysler

DUBAI — "The Mercedes Car Group is achieving record sales," said DaimlerChrysler’s Middle East President, "and we have a great range of new models of Mercedes-

Khaleej Times 15 December 2005

Dh2b land sold out in 48 hours
BY A STAFF REPORTER

DUBAI — Dubai Waterfront — the world's largest waterfront development — this week once again proved its status as a premier property investment location.

Khaleej Times 19 December 2005

... and raising consumption of luxuries
An area becoming richer and richer

- Asset Management offers a huge potential fueled by the flooding liquidity, exceptional stock market performance and lack of service.
- Onshore market size approximates US$400 Bn by the end of 2005, of which only 19% is under management.
- Offshore market which approximates US$ 500 Bn is also an attractive option.

→ A massive market opportunity given the large market gap, the limited number of players as well as the attractive fee structure.

(1.5% management fees on HNWI)
Preamble ...

What is Islamic Finance?
- The basis & key instruments

Industry Overview
- Islamic banking growth phases
- Asset size & distribution
- Key challenges

Potential in specific areas
- Overall development of the Islamic financial services industry
- Potential for the Islamic banking segments / service lines

Regulatory & competitive environment
- Regulatory environment in the GCC and its position towards Islamic finance
Islamic banking solutions should adhere to the basic fundamentals of Islamic finance...

- Transactions must be backed by asset
- Prohibition of payment/receipt of interest
- Tangible assets to back instruments should not belong to prohibited industries (e.g., alcohol)
- Excessive speculative trading in financial instruments is prohibited
- Every financial transaction must involve a level of risk to justify profits

Shari’a Compliant Transaction
Islamic banking solutions should adhere to the basic fundamentals of Islamic finance...

Investment avenues in conventional finance focus on risk adjusted optimal returns but in Islamic finance financial transactions have to meet the following additional criteria:

Implications:

All products need to be approved by the Shari’a scholars and this has several implications:

→ There are limitations on services that can be provided
→ Impediments to innovation exist
→ Product development is time consuming and more complex

Shari’a Compliant Transaction
Growth phases reflect favorable trends...

**Past**
- **Medium**
  - Attracting a ‘captive’ market segment mainly in the Middle East

**Present**
- **High**
  - Geographic expansion beyond ME
  - Recent Political Landscape
  - Oil prices

**Future**
- **Accelerated**
  - Phenomenal economic growth and increasing opportunities
  - Increased regional liquidity waiting to be tapped
  - Increasing market coverage
  - Regulatory initiatives
Growth phases reflect favorable trends...

<table>
<thead>
<tr>
<th>Growth phases</th>
<th>Medium</th>
<th>High</th>
<th>Future</th>
</tr>
</thead>
<tbody>
<tr>
<td>Past</td>
<td></td>
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<td>Accelerated</td>
</tr>
<tr>
<td>Present</td>
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<td>Recent Political Landscape</td>
<td>Increased regional liquidity waiting to be tapped</td>
</tr>
<tr>
<td>Future</td>
<td>Oil prices</td>
<td>GCC market capitalization touching US$ 1 trillion</td>
<td>Islamic mega banks will appear with capital ranging from US$ 1 bil. to US$ 10 bil.</td>
</tr>
</tbody>
</table>

Dominant Drivers:
- Attracting a ‘captive’ market segment mainly in the Middle East
Growth phases reflect favorable trends...

**Growth phases**

- **Past**
  - Medium
  - Attracting a 'captive' market segment mainly in the Middle East

- **Present**
  - High
  - Geographic expansion beyond ME
  - Recent Political Landscape

- **Future**
  - Accelerated
  - Increasing market coverage
  - Tapping the untapped markets
  - Increasing focus on sub segments
  - Increase in awareness and establishing acceptance

**Dominant Drivers**

- Islamic Bank of Britain setup
- First Islamic commercial bank in Canada being setup
- Saxony-Anhalt Sukuk issued in Germany
- Singapore interested in positioning itself as an Islamic Wealth Management center
Growth phases reflect favorable trends...

Growth phases

Drivers

Past

Present

Future

Geographic expansion

Recent political landscape

Oil prices

Attracting a captive market mainly in the Middle East

Growth phases reflect favorable trends

Increasing transparency

Establishing track record

Regulatory initiatives

Increasing market coverage

Increasing regional liquidity waiting to be tapped

Phenomenal economic growth and increasing opportunities

Dominant Drivers

Accelerated
The Future? Tapping the untapped markets...

Share of Islamic Banking Assets 2004

- Middle East: 92.7%
- Rest of the World: 7.3%
- Iran: 57.0%
- Saudi Arabia: 13.1%
- Kuwait: 8.2%
- UAE: 6.2%
- Bahrain: 2.3%
- Qatar: 1.8%
- Other: 9.9%
But key challenges need to be addressed...

How the Islamic banking industry compares with its conventional counterpart?

- Human capital
- Procedures and documentation
- Pricing
- Consumer awareness
- Liquidity management

**KEY:**
- Conventional
- Islamic
- Trend and pace of growth

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Quality In Everything We Do
There is potential in Islamic investment banking and wealth management...

- **Nascent**
  - Islamic Asset and Wealth Management
  - Islamic Equity and Debt Capital Markets
  - Islamic Direct Investments and Project Finance

- **Early Maturity**
  - Islamic Commercial Banking
  - Conventional Retail and Wholesale Banking

- **Advanced Maturity**

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**Mainstream**

**Emerging**

**Industry Life Cycle**

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**ERNST & YOUNG**

Quality In Everything We Do
There is potential for investment banking as illustrated by buoyant equity markets...

<table>
<thead>
<tr>
<th></th>
<th>No. of companies listed</th>
<th>Capital Market Depth (2005) (Market Cap/GDP) %</th>
</tr>
</thead>
<tbody>
<tr>
<td>Qatar</td>
<td>238</td>
<td>32</td>
</tr>
<tr>
<td>Kuwait</td>
<td>180</td>
<td>165</td>
</tr>
<tr>
<td>KSA</td>
<td>179</td>
<td>77</td>
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<td>Bahrain</td>
<td>136</td>
<td>49</td>
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<td>UAE</td>
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<td>108</td>
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<tr>
<td>Oman</td>
<td>55</td>
<td>140</td>
</tr>
<tr>
<td>GCC</td>
<td>163</td>
<td>571</td>
</tr>
<tr>
<td>US</td>
<td>140</td>
<td>5,438</td>
</tr>
<tr>
<td>UK</td>
<td>140</td>
<td>3,028</td>
</tr>
<tr>
<td>India</td>
<td>210 - 3,500</td>
<td></td>
</tr>
</tbody>
</table>

Relatively lower number of listed companies indicates great potential for growth.

IPO Capital Raised in GCC (US $ mil.): 5,500

CAGR (2000-2005): 306 %

**Quality In Everything We Do**

[Ernst & Young logo]
Excess liquidity and increasing interest is also driving the region’s Sukuk markets...

 GCC Sukuk Issuance (US$ mil.)

CAGR (2001-2005) 120 %

2001 2005 2005

100 2,341

KSA 21%

BAH 30%

UAE 41%

Corporate vs. Sovereign Sukuk Issuances (US$ mil.)

2001 2002 2003 2004 2005

100 200 1,655 2,037 2,341

100% 100% 71% 67% 5%

29% 33% 95%

Sovereign Corporate
The bulk of the market remains untapped...

Islamic orientation

Low

High

Segments

Only Conventional

Indecisive

Pure Islamic

Why are indecisive not attracted?

Limited product coverage

Lack of Value-added services

Lack of market segmentation

Other priorities for IBs

BULK OF THE MARKET
**Economic Growth & Liquidity**
- Strengthened oil prices
- Solid economic growth in the GCC has led to rise in liquidity
- Increased wealth is being retained in the region as investment opportunities are improving
- Increased government spending and investment in infrastructure/development projects

**Investors' Appetite for Shari'a Compliant Instruments**
- Shari'a compliant instruments are becoming increasingly popular with investors.
- The rapid emergence of Sukuk is testament to this.
- Family businesses want to tap liquidity with desire to go public is increasing

**Privatization & FDI**
- Increased GCC privatization initiatives will accelerate project finance and structured finance activity in the markets.
- FDI Potential in the GCC is strong and improving with better sovereign ratings and human development

**Regulatory Infrastructure**
- Improving regulatory infrastructures.
- Liberalisation of individual markets and increased investor friendliness.
- Increased foreign participation.

**Diversification**
- Diversification into non-oil sectors by GCC countries
- Investor funds have also been diversifying regionally throughout the GCC and wider Middle East region.

**Global Acceptance of Islamic Finance**
- Islamic financial instruments are becoming increasingly accepted globally due to globalization.
- Foreign regulators are accepting the industry as well (e.g. US, UK, EU, Canada, Singapore)
- Entry of global players in Islamic finance
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