PREPARING FOR A NEW ERA

Address by

IBRAHIM S. DABDOUB
CEO, NBK

Olayan School of Business
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Dear Dr. Najjar, Members of Olayan School of Business Faculty, AUB students, Alumni and friends

I am honored and delighted to be here today to address such a distinguished group of academics, business people and young leaders. When Dean Najjar asked me to speak, I did not hesitate to say yes, not only because of my association and love for AUB, but also out of respect for its role in developing some of the best minds in our region. I felt it would be a privilege and an opportunity for me to carry a message to a country I consider my own, where like most Arabs I have taken Lebanon as my adopted country for the unique and special standing it has in the region.

My message in a nut shell: I have spent 45 years in the Gulf where I started my career at NBK in 1962. I have witnessed booms and busts, and many crises. I believe the boom we are living today is much bigger than we have ever seen before, providing an opportunity for all Arabs to reset our course in the right direction and deal with our challenges from a position of strength and comfort. A lot needs to be done to meet the aspirations of our youth and there is a role for all concerned to play and ensure this tide will lift all boats.

I started with the intention of talking to you about Arab management and the
challenges in revolutionizing it to rise up to the opportunities ahead. I was planning to touch upon a long list of issues from how different the traditional Arab Management style is in comparison to Western management principles, my experience in bringing about change at NBK, to what needs to be done to prepare for the transformation we are going through in the Arab world.

Then I realized that I will end up boring you, either because you have heard it before or probably because many management professionals feel that they know it all. When you get to be my age, boring your audience is the last thing you want to do. So, I will restrict myself to telling you this anecdote that probably sums up where Arab management is coming from.

Back in the 70s, NBK hired a consultant to develop a 5 years strategic plan for the bank. It was after the first oil boom when we started our activities in international banking. In a meeting with our late chairman, I tried to explain to him what we were doing in planning for the future of our bank. He looked at me as though I was so naïve and told me “my son لا يعلم بالغيب إلا الله” Out goes strategic planning! I have full respect for our culture but planning should not conflict with it. This story tells you a lot about Arab management and strategic planning, or lack thereof. It demonstrates the cultural challenges Arab management faces, and believe it or not such cultural "blocks" still exist till today. I hope those of you here who appreciate the importance of strategic planning and vision are as tenacious as I was in pursuing what I thought was right for NBK.

While I was preparing for the new topic that I decided to cover today, I came across a speech I gave in New York in 95 which made me wonder how much we have changed since then. At the time, I was reflecting on why we were missing the opportunity to benefit from the prevailing global trends. I summed it up then in the fact that:

- While we were out breeding dictatorships in the Arab world, wasting our resources on war machines in order to fight each other, the developed world was fostering democracy and respect for human rights.
- While we were out teaching our children archaic slogans "بالروح بالدم نفديك يا زعيم", other countries were teaching their children science and technology.
- While we were out inflating our public sector, the world was encouraging entrepreneurship and private initiative.

Unfortunately it is not too different now!

However, despite all that, I can now see a glimmer of hope and the beginning of a transformation in the Arab world, which convinced me to talk to you today about the coming oil windfall in the Gulf countries and its ramifications throughout the region. Thanks to China, India and the US, the Arab oil producing countries (the GCC as we
call them) are going through a major boom which may last for 10 or even 15 years. In 2006, the GCC countries, which control 40% of the world's oil reserves, reaped $360 billion in oil revenues, and supplied the world with $200 billion in capital because the oil windfall was far higher than they could spend. To put it in perspective, the GCC was the largest exporter of capital, accounting for 15% of the world's total net capital outflows, ahead of China and Japan.

Cumulative capital surpluses of the GCC over the past 5 years exceeded $700 billion. Most of this money is now held in "sovereign wealth funds", or what many refer to today as the new power brokers in the world. These funds generally invest in foreign assets whose size is estimated to have reached $2 trillion.

What is remarkable about sovereign wealth funds is not their size per se; rather it is their rapid growth that has caught the financial world by surprise. If they can maintain their growth rates of 20% per annum they can double again by 2012. Indeed, the McKinsey Global Institute estimates that "GCC oil export revenues will add up to $6 trillion over the next 14 years if oil averages $70 a barrel, but if oil stays at $100, cumulative oil revenues will rise to almost $9 trillion." This is no small change! There is now a shift of wealth from the US and Europe to the East including the G.C.C. It is really a major change that these new power brokers are now shaping global capital markets. Can you imagine the power we will have in the next decade if we know how to use it.

Can you imagine what would have happened to the financial markets if Abu Dhabi and Kuwait did not bail out Citibank and Merrill Lynch, and still more to come?!!

The question that keeps analysts worldwide busy is "what will we do with the windfall?" This question also concerns all Arab countries. That is because this new era of growth provides a unique opportunity to turn the tide and the dynamics of our Arab economies. Not many nations get such an opportunity, and rarely a second one. God has given us this "natural endowment", and a second chance to get it right. It is now up to us not to let this opportunity pass us by.

Fortunately, Gulf countries seem to have recognized this opportunity, for how else can we explain the surge in investor confidence and optimism. You can see it in the changing landscape from Dubai to Kuwait. You can see it through the growing number of national champions, companies that have tapped capital markets to undertake aggressive expansion plans across the region and beyond. You can see it in the surge of regional equity markets by more than 400% since 2000. You can see it in the initiatives undertaken by many GCC governments to liberalize their economies in the hope of attracting foreign investors and winning the race to become regional trade...
and financial centers. This transformation has brought to the fore the issue of corporate governance and many Gulf countries have moved to adopt minimum standards. It won't be long before all have such standards in place.

You may ask: "but how can non-oil producing countries like Lebanon benefit from the oil windfall?" Let us start by understanding where the new money will go.

For starters, as one would expect, GCC governments used the increase in oil revenues to accelerate development of their economies by increasing their domestic investment. Many countries are working on setting up new industrial cities, cultural, touristic, health or financial centers. But there are limits to their capacity to absorb such new investments, as well as risks of creating inflationary pressures they won't be able to contain. The remaining surplus will have to be channeled into foreign investments. Such flows are likely to exceed their domestic investments over the long-term.

The drive to diversify their financial investments is behind a new trend emerging in the GCC since 2002. Whereas most GCC money used to go to the US and Europe, new evidence shows that nearly one-third of Gulf foreign investment flows is directed to Asia and the MENA region. The latter type of investments have caught the attention of many Western "nationalists" and legislators who sounded the alarms of "national security" after a few high profile deals came to the surface, such as the Dubai Ports acquisition of a port operator in the US.

Recent capital infusions of more than $14 billion into leading western financial institutions including CitiGroup, Merrill Lynch, and UBS following the unraveling of the sub-prime credit crisis was not welcomed either by many, though the politically motivated opposition to petrodollars (whether out of general mistrust of foreign money, or post 9-11 sentiments toward Arabs, or Israeli lobbying), the opposition was muted somewhat by the recognition that the alternative might have been far worse without the liquidity injection from these funds. For that matter, increased liquidity from SWFs is estimated to have reduced interest rates globally by up to 75 basis points over the past six months.

I could feel and hear the anxiety over the growth of sovereign wealth funds last month when I participated in a panel debate about the subject at the World Economic Forum meet in Davos. The panelists, all distinguished professionals including a Nobel Prize winner, were nearly in consensus about the growing role of SWFs in capital markets. Many though were advocating protectionist measures under the guise of asking SWFs to commit to an unspecified code of conduct. I spent a lot of energy arguing that GCC funds add value to their target acquisitions and their home countries. I told them "you blamed us in the 50s and 60s for having no money, and now you blame us for having
However there is a silver lining in the "Western" opposition camp to Gulf petrodollars is that managers of SWFs will continue to focus on emerging Asia and the MENA region as destinations for their investments. As such, non-oil producing MENA countries, like Lebanon, must position themselves to compete for GCC business and investment with the rest of the world. So, if I were you, I would pray that stupid politicians and protectionists would prevail in the West, no doubt influenced by the Israeli lobby, so that such investments get diverted to the Arab world.

I should add here that government controlled funds are not the only petrodollars providing liquidity and investment flows to global markets. The oil windfall has also created a lot of private wealth, as many private businesses benefited directly or indirectly from the increase in government spending. Numerous millionaires have emerged, some merely from playing the regional stock markets. Most are looking for regional investment opportunities, whether real estate, private equity, mergers and acquisitions, or green field projects.

Unfortunately, Lebanon and the other Levant and North African countries have a long way to go to make their markets attractive to investors. I will focus on the two most important areas in need of reform: government and governance. It is critical for you to attend to these as people's futures in most Arab countries outside the GCC countries are still being hi-jacked by the same archaic slogans that held five generations of Arabs back, irrespective of how different the words or faces behind them are.

You are probably wondering why I am saying this to you, and what can you do. Well, collectively you can make a difference. You need to find an effective way to influence your environment so that you do not miss this 'once in a lifetime' opportunity: the coming oil windfall. First and foremost, you need to turn your country (or I should say countries) into a more hospitable environment for doing business by pursuing political and regulatory reforms. It means reducing political and regulatory risks for investors. It also means privatization and greater transparency which afford investors better opportunities and a greater ability to assess risks.

Longer term, continued focus on education will be crucial as human capital has become the main source of competitiveness and value creation in this age of knowledge. This has always been a competitive advantage for Lebanon, which explains why it exports so much human capital to the rest of the Arab world, and beyond. And surely, the coming windfall will favor the demand for educated and capable Lebanese. My only wish is that Lebanon can stop its brain drain and create the enabling environment for this pool of knowledge to organize into globally competitive industries. This requires securing rights of private property and personal
liberty, including the right to live and to aspire for a better future, as well as the rights of minorities or even the losers in democratic elections.

Business institutions can do their own share. They need to focus on developing competitive businesses whose growth derives from advancements in productivity and the employment of knowledge instead of protectionism, favoritism and collusion between business and political elites.

Sound corporate governance is another area for you to focus on. Irrespective of what the local norms and regulations are, it is not sufficient to meet them. Instead, you should work on building trust in your control arrangements and managing your business better than anyone else. As someone once said, regulations should not be a substitute for honesty. Educating young people about the importance of governance was behind NBK's decision to support the Corporate Governance program at AUB.

If you focus on these two areas, you will not just help your country compete for GCC investments, but leave it better placed to compete for investment from further a-field, as well as improving business conditions for domestic investors.

Lebanon has a lot to offer investors if only the Lebanese could find a way to get past this impasse and recognize that one cannot put his house in order in one fell swoop. You start with the priorities and recognition that compromise is important, as well as an understanding that any solution must be a win-win solution. This is as true in politics as in business. This is also how to develop trust. I wish you luck, but more than that I wish for reason to prevail and a clear vision to be restored!

Thank you.