



SARASIN
ALPEN

Islamic Wealth Management Report

2010

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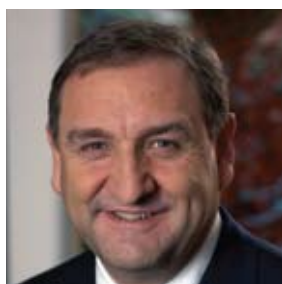
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Wealth brings with it responsibility



Joachim H. Straehle
Chief Executive Officer
Bank Sarasin & Co. Ltd
Switzerland

Bank Sarasin's oak tree is a powerful symbol. It celebrates strength and growth. Echoing Islamic beliefs it also recognizes that a holistic approach to wealth cultivation and preservation is critical to healthy, sustainable returns. Our oak tree demonstrates that "Wealth brings with it responsibility" and has been a guiding principle for Bank Sarasin since our founding in 1841. Socially responsible wealth management, with a long-term perspective, avoiding risks and seizing opportunities, is our approach of choice. We have also championed that approach in the financial markets, pioneering sustainable wealth management 20 years ago.

Our commitment echoes the concept of Islamic wealth management. With locations in Switzerland, Europe, the Middle East, and Asia, we see great opportunities in Asia and the Middle East. Islamic wealth management is one key to unlocking these opportunities for us and our clients. To support this further growth, Bank Sarasin established a Sharia Advisory Board to oversee our comprehensive Islamic finance product range, managed by a dedicated division of renowned experts. Our offerings address the needs of our clients, be it in cash management, portfolio management or estate planning, in full compliance with the holy Sharia.

I am delighted that, with this report, we are offering additional insight regarding Islamic Wealth Management to global investors.



Fidelis Goetz
Head of Private Banking
Bank Sarasin & Co. Ltd
Switzerland

We are proud to launch the first-ever Islamic Wealth Management Report 2010, just months after we introduced our comprehensive Islamic Finance offering. This pioneering report provides investors with a synopsis of the Islamic Finance market over the past 18 months. It is intended as a significant contribution to this specialized area of financial services and will further the development of Islamic wealth management in the best interests of our clients.

We hope that, as a milestone for Islamic wealth management, this report will help educate and provoke further discussions. We trust that this report will reach a wide readership, and very much look forward to being a dynamic partner in the growth of this industry.

Wealth Preservation – Our long-term focus



Rohit Walia
Executive Vice Chairman and CEO
Bank Sarasin-Alpen Group
Middle East & South Asia

Islamic wealth management is one of the fastest growing sectors in the Middle East and has sparked interest further afield. In 2009 we introduced a comprehensive new Islamic wealth management service offering the full spectrum of Sharia-compliant private banking products and services.

To support this service, Bank Sarasin has established a rigorous investment screening process ensuring that all of our products are continuously monitored by our Sharia Advisory Board. We believe that the Islamic Wealth Management Report 2010 constitutes a powerful contribution to the development of Islamic Finance, and is a thoughtful addition to the existing literature on the field. We hope that you will benefit from this report, which provides an overview of Islamic wealth management and its trends, as well as our economic outlook for 2010.

Hope you enjoy reading it!



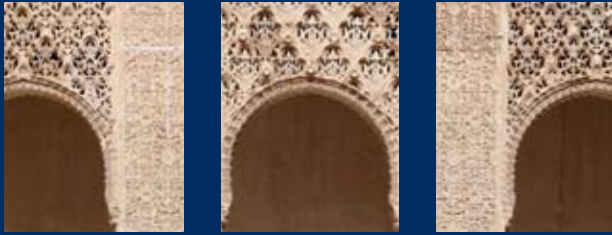
Fares Mourad
Head of Islamic Finance
Bank Sarasin & Co. Ltd
Switzerland

Bank Sarasin and Islamic Finance offer a powerful combination of tradition based on sustainability, Islamic values and almost 170 years of private banking experience. Together, they represent a bridge that spans cultures, civilizations and industries to create enlightened and responsible wealth management. Together, they offer clients a unique opportunity to benefit from our strong tradition of serving investors with a long-held philosophy of responsible investing.

In this report, we are particularly proud of the important chapter on Islamic Estate Planning and Wealth Preservation. The distinction between general estate planning and that which is required by the Qu'ran is seldom discussed, and, in our view, does not receive enough attention within the Islamic world. We are delighted to make this contribution to the practice and development of estate planning and wealth preservation.

We hope that you will enjoy reading this report, and thank you for your trust in Sarasin.

Sharia Advisory Board of Bank Sarasin, Switzerland



To accommodate the requirements of investors seeking the expertise of a dedicated Swiss private bank in conformity with the Sharia, Bank Sarasin approached us about a year ago with the request to oversee its Islamic banking and investment activities, and to help develop the bank's products and service offerings.

Despite the short period, many services and products have already been reviewed by us, and we are happy to note that Bank Sarasin is now in the position to offer a wide range of Sharia-compliant services ranging from short-term simple and complex investment schemes, asset management capabilities, investment advisory services, and various financing possibilities, to important approaches serving wealth preservation and estate planning. The platform has been built on the basis of experience accumulated by the bank in serving private banking clients since 1841.

The bank not only sheds light on the status of Islamic wealth but addressed a topic hardly ever discussed or addressed: Islamic estate and succession planning. Islamic Wealth Management 2010 presents this topic not only as food for thought but to enhance our duty to ensure that the trust placed in us by Allah is handed to our successors in a proper manner with full confidence that they are also well trained to carry the trust in a sustainable manner.

We, as the Sharia Board, are satisfied with the approach and the way the Islamic finance division of Bank Sarasin is handling and pursuing its Islamic finance offering. We would like to express our best wishes to Bank Sarasin and its dedicated Islamic finance team for sustainable success with Allah's blessing.

Wallahu waliuu alTawfiq.

Sheikh Dr. Mohamed Ali Elgari
Member

Dr. Muhammad Imran Ashraf Usmani
Member

Dr. Monzer Kahf
Member

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With the conventional financial industry hard hit, Islamic finance gains new prominence



The events of 2008 – the credit crunch, the financial crisis, and the ensuing panic – cast a long shadow into 2010, having destroyed trillions of dollars of wealth. Among the worst hit were retail investors and the segments that bore the brunt were those with the most to lose: the rich and the very rich. Tried and true investment wisdom failed to counter this historic crisis.

Against this background we review the relatively young Islamic wealth management industry. Until recently, there were no dedicated Islamic wealth management services so that rich investors either managed their own assets or simply utilized conventional financial products, knowing that these may not comply with Sharia law.

Sharia law, risk and the family's future

The global financial crisis brought Islamic finance more to the fore as pundits and analysts recognised that Sharia requirements provide an additional risk screen, and therefore effectively decreased exposure to toxic sub-prime debt, sparing some investors from the worst excesses of the crisis. Nevertheless, the average investor lost an estimated 20% of his net wealth during the crisis.

Just as Sharia law dictates a specific approach to investing, it provides specific requirements for wealth preservation and transfer. Regardless of the impact on their net wealth, Islamic investors are faced

with the issue of family and generational wealth management. The complexity of Islamic requirements is so great that wealthy investors may need to establish professional family offices to assist with asset management, business management and legal issues.

The year ahead

Like the conventional financial sector, the Islamic wealth management industry is facing perhaps its most challenging period and, at the same time, its greatest opportunity, for both investors and service providers. As ever, understanding the very complex needs of the client will be of paramount importance, as will offering solutions that meet or exceed their expectations. Investors, especially the rich, are invariably sophisticated and Islamic investors are no exception. Now, more than ever, clients will be looking for strong and impartial advice. This could be the opportunity that the Islamic wealth management industry has been waiting for. The industry had better make the most of the opportunities presented.

Islamic Estate Planning and Wealth Preservation



Wealth management cycle by Bank Sarasin

Unlike in the West, estate planning for Muslims is based on the principle that all wealth belongs to Allah and that anyone who possesses wealth is simply its caretaker. According to the Qu'ran, wealth creates specific religious responsibilities that can be interpreted as a Muslim version of socially responsible investing.

Specifically, Islamic estate planning takes into consideration the concept and meaning of wealth in Islam, the religious requirements of making a will and the rules of inheritance. In the Qu'ran, mankind is a trustee of the Creator and everything belongs to Him. The Qu'ran (Sura 24, Verse 64) says:

**“Be quite sure that
To Allah doth belong
Whatever is in the heavens
And on earth. Well doth He
Know what ye are intent upon:
And one day they will be
Brought back to Him, and He
Will tell them the truth
Of what they did.
For Allah doth know
All things.”**

Social responsibility and accountability are deeply embedded in this concept. Wealth management, therefore, has three phases: first, the proper acquisition of wealth; second, the preservation of wealth; and third, the correct expenditure and distribution of wealth. Estate planning predominantly manages its preservation and distribution. “A Muslim should prepare himself for the next world as if he is going to die tomorrow, but at the same time work hard to improve all his worldly comforts as if he is going to live forever.” (A quote from the Prophet narrated by Al-Dailami).

Earning wealth from acceptable sources is morally of utmost importance and being wealthy is seen as a positive and graceful attribute, especially when wealth expenditure and distribution is conducted

modestly and demonstrates obligatory and voluntary charitable spending.

As wealth is considered to belong to the Creator and mankind is nothing other than its guardian, private guardianship of wealth ends with the death of the guardian. Appropriate provisions to deal with death must be in place. A man asked the Prophet, “O Allah’s Apostle! What kind of charity is best?” He replied, “To give in charity when you are healthy and greedy, hoping to be wealthy and afraid of becoming poor. Don’t delay giving to charity until you are on your death bed saying, ‘Give so much to so-and-so and so much to so-and so,’ because at that time the property is not yours but already belongs to so-and-so (i.e. your inheritors).” (A quote from the Prophet narrated by Abu Huraira in Sahih Bukhari, Volume 4, Book 51, Number 11).

Hence wealth requires forward planning that incorporates and affects life-long action. Good financial deeds should be conducted during one’s lifetime as preparation for the afterlife. Charity is not effective when a person fears imminent death. Each Muslim should know this and determine charitable allocations that most closely match his values.

The limits set by Allah

During his lifetime, a Muslim may plan to give away his wealth to a charity or to others, including family members, without violating the principles of Sharia, since he is still the guardian. However, as death approaches, the distribution of assets is ordained by Allah, its Ultimate Owner, in accordance with the Qu'ranic inheritance rules. These rules are mandatory as the Qur'an says, "Those are limits set by Allah. Those who obey Allah and His Messenger will be admitted to Gardens with rivers flowing beneath, to abide therein, (forever), and that will be the supreme achievement." (The Qu'ran, Sura 4, Verse 13) Furthermore, the Prophet allows that one may assign, by virtue of a last will, up to one-third of the net estate to charitable causes. In this regard, Ibn Abbas, the Prophet's companion and cousin says: "I recommend that people reduce the proportion of what they bequeath by will to one-fourth (of the legacy), for Allah's Apostle said, "One-third, yet even one-third is very much." (Sahih Bukhari, Volume 4, Book 51, Number 6).

The portion to be transferred by means of a will should therefore not exceed one-third. The remaining assets are already "assigned" to heirs within the family. This Qur'anic assignment cannot be changed by a last will. Even though the inheritance proportions are fixed, it remains necessary for each Muslim to write a will, leaving his worldly affairs in good order. The Prophet said: "It is not permissible for any Muslim who has something to will to rest for two nights without having his last will and testament written and kept with him." (Narrated by Abdullah ibn Umar: Sahih Bukhari, Volume 4, Book 51, Number 1).

What must will be

The elements of such a will and testament, (wasiyah, regarding the transferable third), include distribution to charities and to persons who are not ordained to inherit,

such as the grandchildren of surviving children, (parents are first in line to receive, rather than grandchildren, unless the parent is deceased) and friends. Further, in countries that do not have Sharia-based inheritance laws, it becomes necessary to include distribution to heirs according to Sharia-assigned proportions because of their mandatory religious nature.

However, it is very common to add more issues of importance to a last will. These additions may include naming creditors and necessary debt settlements, guardianship of minors, healthcare instructions in case of incapacitation, instructions for funeral rites, and naming a trusted person to act as the estate administrator, (wasiy). Additionally, local legal requirements may need to be met in the country of residence.

To summarise, Islamic estate planning has two major instruments:

1. An irrevocable gift during a lifetime. This can be personal or in the form of Waqf, (endowment of a public or private cause).
2. A will, allowing for a maximum of one-third of the estate to be passed on to any designated charitable entity or person.

Estate planning may be complex if the estate is domiciled in various countries and thereby subject to different estate and tax laws, resulting in delays to transfers and possibly forced deviation from the will.

Knowledge is better than wealth

Since a family business is typically the source of wealth, estate planning must address succession issues. Family business presents a special challenge regarding how it should be managed, continued and passed on to the heirs. Wealth preservation in this regard faces numerous family dynamics that need to be considered. The central guideline for managing such dynamics is, in the words of Ali Ibn abi Talib, "Knowledge is better than wealth because knowledge will

take care of you, but you have to take care of wealth”.

Many families are satisfied with the guidance given by their lawyers with respect to wealth preservation. However, in reality, most of those families are not successfully preserving their wealth when measured against the universal cultural proverb: “From shirtsleeves back to shirtsleeves in three generations”. Legal solutions do not usually guard against this possibility, which is counter to Islam.

Recent studies have shown that:

- A family can successfully preserve its greatest wealth, capable individuals who form the family, over a long period of time.
- A family’s wealth consists first and foremost of its human capital (individual family members) and intellectual capital (individual family members’ knowledge) and second of its financial capital.
- The purpose of the family is to enhance the individual members’ achievement of happiness, (Khair, the good in the here and in the hereafter), in the overall pursuit of the long-term preservation of the family as a whole.
- Successful long-term wealth preservation requires the creation and maintenance of a system of governance or joint decision making that assures broad consensus over a period of at least 100 years.

According to the ethics of Islam, a family must be governed in accord with the writings of the Qu’ran. A family mission statement is therefore a key part of a governance system. It is an expression of the purpose, vision, values, and goals of a particular individual, couple, family, or enterprise. The creation of a Sharia-compliant family mission statement is the starting point for determining the family’s approach to preserving its wealth.

Defining a family’s goals

For a family that is already organised, the need to express its purpose, values and goals will become apparent as soon as the first problem arises and family members have no shared way of understanding how to resolve it. When a family is in the process of wealth preservation, a mission statement will help achieve long-term success. If a family cannot define its goals, how will it know how and if they have been achieved?

What are the issues a family mission statement needs to address to define the family’s purpose, vision, values, and goals?

- A family needs to understand its purpose. While it can be argued that the purpose of a family is to enhance the pursuit of happiness in the worldly life and in the hereafter for its individual members, and thereby preserve its human, intellectual and financial capital, each family must determine and define its own philosophy. The first goal of a mission statement is defining the family’s philosophy behind its purpose.
- A family must have a common vision. It must look ahead to the future and form a consensus around a shared goal. A family should ask itself how it plans to achieve its current goals, while looking ahead 25, 50 and 100 years.
- A family shares certain values. These are the values that foster that family’s uniqueness.
- A family needs to acknowledge its “secrets”. Every family has open secrets. Not addressing these “secrets” creates an atmosphere in which every member thinks the family is connected to each other, but in reality the family is falling apart because no one is willing to discuss buried issues. Such a situation will drain not only the family’s wealth but its human and intellectual capital.
- A family needs to recount its history. The preparation of a family mission statement allows an opportunity to tell family stories.

Family stories are the glue that binds individual family members together. Every family that is successfully preserving its wealth sets aside time at its family gatherings to share its unique history. Both young and old tell stories, discovering their common bonds and values. A family mission statement should express the family's unique history.

- A family must choose a form of governance. The family mission statement should indicate the form of governance selected by the family and how it will assist in long-term wealth preservation.
- Each person needs to understand his or her role in the family. A family mission statement affords each individual family member the opportunity to consider his mission as a member of the family and as an individual.

Once clarified, an ethical, goal-oriented day-to-day operation is possible. This is what classical authors of Islamic administrative ethics call "Tadbir". If the mission and roles are not defined, administration cannot act responsibly.

Measuring a family's balance sheet

The family balance sheet and family income statements are key tools for measuring the health of a family's wealth preservation strategy. A traditional balance sheet attempts to measure the state of well-being of a business at a specific time. Such balance sheets contain statements of assets, liabilities and shareholder equity as a reflection of the business's financial status.

Similarly, a family balance sheet also lists assets, liabilities and shareholder equity but it expands on what each category measures. Because successful long-term family wealth preservation is achieved by enhancing the well-being of individual family members over a long period of time, the family balance sheet must measure human and intellectual

capital as well as financial capital. A family balance sheet is an addition to, not a substitute for, a family financial statement. Those managing the family's wealth, like every other financial manager, must know its financial capacity to carry on its mission. Only based on this understanding can profound decisions be made about governance and the potential solutions for succession. Such tools might be an Initial Public Offering or a Trust, depending on the family's total balance sheet, in the sense of a balanced approach based on justice.

Transcending prudence

Reasons for creating Trusts & Waqf and their technicalities:

Extending the view of a family business to overall family wealth accumulation that includes real estate and bankable assets again raises the issue of wealth preservation. Wealth preservation transcends prudent investment strategies such as diversification and modern portfolio theory to take into account:

- Business ownership, for example keeping the business family-owned as an alternative to an IPO.
- Political risk factors, including where assets or residences are located.
- Local legal systems and inheritance laws that could, for example, mean assets may be frozen.
- International tax issues.
- Potential disputes, both personal and legal.

Some examples

The family business is passed onto five heirs, such that each owns 20%. Some heirs aim to sell, while others want to hold. Agreement cannot be reached.

A Muslim resident in one of the GCC countries holds US securities in his portfolio and owns one apartment in the US occupied by his son, who studies in the US. US inheritance laws do not tax individuals specifically but primarily the estate, hence

the US securities and properties would be subject to US inheritance tax per se. A son who studies in the US may receive a substantial gift from his father. The son would then be subject to US gift tax which could possibly be lowered or avoided in consultation with international tax lawyers.

A Muslim living in the GCC wants to spend his summers at his property in Nice, France. The property may become subject to local inheritance tax, capital gains tax and wealth tax depending on how the property was acquired and financed.

Each case illustrates some of the many difficulties that may arise if estate planning is not handled professionally. Hence, advice from private bankers, tax planners and lawyers is needed to structure solutions that avoid costly emotional and financial pitfalls.

Trusts may be part of a solution. What is a Trust? It is similar to the concept of a Waqf. Waqf (plural Awqaf) consists of assets assigned to support a specific cause. If the cause is philanthropic, it is called Waqf Khayr and if for family members, Waqf Ahli. The documents constituting donation, (Waqfiyya), are registered with the court, (Qadi), or Department of Awqaf. One of the Waqf's main principles is perpetuity, meaning only the income is for the beneficiaries but the corpus (principal or capital sum) of the assets must be preserved. This is reflected in the word Waqf, which has 'to hold' as its Arabic root. The sale of the core assets is restricted and, at best, permissible only if replaced by equivalent assets.

Providing in perpetuity

In the history of Islam, Waqf became very popular in both its applications – the charitable Waqf that provides for philanthropy, and the family Waqf that is used to protect and preserve the family

business as a consolidated unit and to support family members through its revenues. The Waqf has its own legal entity as a juristic person; its appointed representative is the Mutawli, (the trusted agent).

An Anglo-Saxon Trust, in contrast, is not a juristic person. The assets transferred are held in Trust by the Trustee. Further, a Trust may allow certain options not known in Islamic law, such as the power to dispose of the corpus by the Trustee. A Trust may be established for a temporary period while the Waqf is intended to exist in perpetuity.

Cash becomes a lasting investment

While initially only physical real estate was deemed to be a lasting investment for a Waqf, cash was allowed later. In US Trust history there was an interesting shift in the way assets have to be managed. Originally the Prudent Man Rule, (originating from 1830), directed trustees "to observe how men of prudence, discretion and intelligence manage their own affairs, not in regard to speculation, but in regard to the permanent disposition of their funds, considering probable income, as well as probable safety of the capital to be invested".

This required the Trustee to judge each investment implicitly on its own merits. Only in 1992 did modern portfolio theory lead to a new approach known as 'The Uniform Prudent Investor Act', whereby Trustees apply modern portfolio theory to guide investment decisions. Under the Prudent Investor Act, a Trustee would not be held liable for individual investment losses, as long as the investment, at the time of acquisition, was consistent with the overall portfolio objectives.

Such an approach allows for greater flexibility in applying socially responsible criteria. Trustees may be told which non-financial criteria should be applied to investments,

for example, regarding the typical screening for Sharia-compliant stocks and securities. Such socially responsible criteria should be outlined explicitly or the Trustee is obliged to focus only on financial criteria to fulfil his duties and avoid dispute.

Furthermore, since an important goal of an Islamic Trust or a Waqf is perpetuity, active exclusion of risk factors, such as high indebtedness and harmful industry sectors, and inclusion of long-term opportunities, such as alternative energy and water, and best practices in environmental management, are natural investment criteria which further foster the aim of perpetuity.

For a Muslim client, four main types of Islamic Trusts meet different needs and are customised to accommodate varying personal objectives:

1. A Trust for the purpose of benefiting Islamic charities or causes.
2. A Trust which replicates the Waqf by preserving capital but allocating income to beneficiaries.
3. A Discretionary Trust during the settler's lifetime, which will be distributed according to Islamic inheritance laws thereafter, but quickly and efficiently without probate.
4. An Irrevocable Discretionary Trust following Islamic principles, while remaining flexible for interpretation by the various schools of Fiqh, for example, to defer entitlements of children until they are older.

Using Islamic-oriented Trusts as instruments for estate planning, the settler, ('testator' in the US), can achieve tax-efficient global solutions, legally entrusting his assets to a politically stable environment, while keeping his worldly affairs in good order.

The settler may assign beneficiaries who are close to his heart, because they took additional care and showed prudence in

their lives. Irrevocable gifts (Hibah) should be made during the settler's lifetime and fall outside the Islamic inheritance laws. This is fully compliant with the form and spirit of Sharia if the intent is pure, meaning that it does not counter the proportion of assets due to heirs under the Islamic inheritance system. Furthermore, gifts to children and grandchildren should not unjustly favour some over others, as the Prophet is reported to have rejected gifts that are not equal.

Inheriting in Islam

Islamic inheritance law is based on the principles of redistribution, lineage and interfamily members' financial responsibilities. As already discussed, a maximum of one-third can be given to non-heirs, the remainder must be left to the heirs. However, before any distribution, the estate's debts and funeral expenses must be paid. Islam introduced shares for women in inheritance. Previously, under ancient laws they were not allowed to take part in inheritance. The share of a female is half that of a male in most cases, because of the much greater economic responsibility assigned to Muslim men. While men must support families and parents under Islamic law, women are not obliged to provide such financial support. However, many Muslims live in countries where women are legally obliged to support their relatives financially. A gift made during the settler's lifetime could compensate for this obligation.

Managing Islamic philanthropy

Aside from serving family issues, the Trust can be an excellent charitable instrument with Muslim philanthropy as the cornerstone. The status of a Muslim in regards to Allah depends only on his "God-consciousness" (Taqwa), but there are two areas where he may envy others, as cited by the Prophet: "There must be no envy except in two: a person to whom Allah has given wealth and who spends it in the right way and a person to whom Allah has given wisdom

(i.e. religious knowledge) and who takes his decisions accordingly and teaches such wisdom to others.” (Narrated Ibn Masud: Sahih Bukhari, Volume 2, Book 24, Number 490).

Furthermore, a Trust allows the deceased to receive rewards even after his death. In a Hadith in Sahih Muslim, Abu Huraira reported Allah’s Messenger as saying: “When a child of Adam dies, his deeds come to an end, except for three:

1. Recurring charity, or,
2. Knowledge (by which people) continue to benefit, or,
3. A pious son, who prays for him.”

As such, the high importance of giving is apparent and deserves further comment.

Islamic philanthropy, a duty practiced

Under Islam, giving is not only a theoretical religious duty but a standard practice. USAID, in its report ‘The Idea and Practice of Philanthropy in the Muslim World, 2005’, estimated the magnitude of philanthropic giving in Muslim communities at between USD 250 billion and USD 1 trillion annually.

By itself this is astonishing, but it should be noted that such giving has a long tradition. Historically three quarters of all the land in the Ottoman Empire in the 1850s was Waqf.

Awqaf is a recurring charity, since its revenues are distributed to charity year after year and, from a religious point of view, it is highly prized since it rewards the deceased even after death. Islamic Trusts can be used for such a purpose.

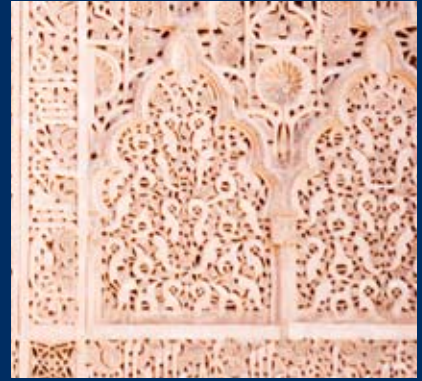
Contemporary themes that charity addresses range from: poverty alleviation, education and social services to support for culture such as arts, literature and music and scientific research and improvement. These themes are not independent, as poverty alleviation is impacted by education

which fosters sustainable self-help. Among Muslims it is often preferable to give discretely to a needy person. Equally important, such generosity should not make the donor feel proud.

Giving under these various approaches needs analysis, a clear concept and planning to achieve a significant impact and to last for generations. It is therefore an indispensable part of Islamic estate planning in order to create and preserve wealth and share it with dependents and the less fortunate, as commanded by Prophet Muhammad, (s.a.s*), who said: “The best charity is that which is practiced by a wealthy person. And start giving first to your dependents.” (Narrated Abu Huraira: Sahih Bukhari, Volume 2, Book 24, Number 507).

* ‘Salla alaihi wa salam’ means peace be upon him

Equities



Sharia-compliant indices cater to Islamic investors

Equities have long been the mainstay of many investors around the world so it is hardly surprising that they feature heavily in the realm of Islamic wealth management. One reason for their lasting appeal is that they can offer rewarding returns when compared with other assets classes. They can also offer diversification across a wide range of geographies and industries, although recent history shows that such diversification may not offer protection should markets collapse globally.

An Islamic investor wants to invest in equities that are deemed Sharia-compliant. There are a range of indices that can be used to establish whether an equity is Sharia-compliant. They are offered by Dow Jones Indexes, the FTSE Group, Morgan Stanley Capital International (MSCI) and Standard & Poors (S&P), among others. Since the launch of the global Dow Jones Indexes in 1999, these indices effectively constitute the benchmark for Sharia-compliant equity investing.

Islamic investors are not allowed to invest in companies that make most of their revenue from non-Sharia compliant business activities or in companies that are highly leveraged. Sharia indices typically review companies for Sharia compliance through two separate areas of screening: business activities and financial ratios. Business activities that are forbidden typically involve dealing with pork, pornography, alcohol, tobacco, gambling, and non-Islamic financial services.

Clearly it is much easier to tell if a company falls foul of these rules if it is the company's primary activity, but when its involvement is in a secondary capacity then the application of the screening becomes much more difficult.

A 5% rule seems to have become the accepted level of exposure to such

Haram (unlawful) activities: if a company earns less than 5% of its revenues from these then it can be considered Sharia-compliant. Because this can be difficult to ascertain, there are inevitably some differences of opinion as to which stocks are acceptable. This means that some fund managers have composite portfolios that rely on stocks across a range of indices.

Such a composite can help increase the total number of permitted investable companies, although caution must be exercised when assessing the Sharia compatibility of some of the included equities. In practice it can be hard to determine, for example, how much profit a supermarket chain makes from the sale of pork products since this is typically not the sort of information the company would monitor.

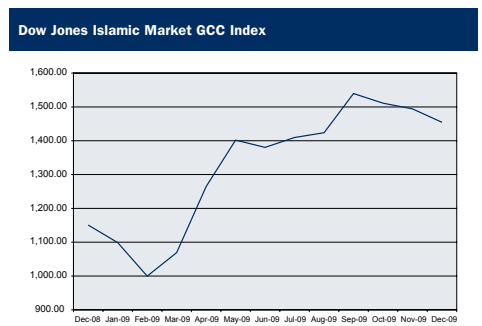
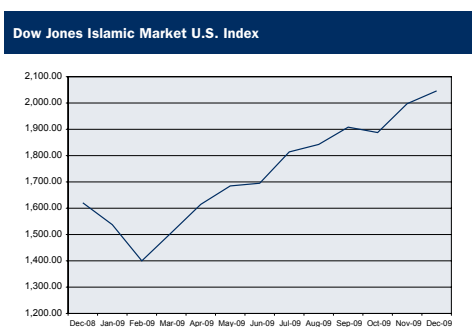
The future for equity investing

During the market turmoil equity markets around the world were volatile and unpredictable. While there were some bright spots to be found, the general trend across equity markets was downward for many months, with some markets collapsing completely. The markets of several Muslim countries, including those of the GCC, saw huge falls, and markets lost as much as 70% of their value in a relatively short time. 2009 experienced a rebound,

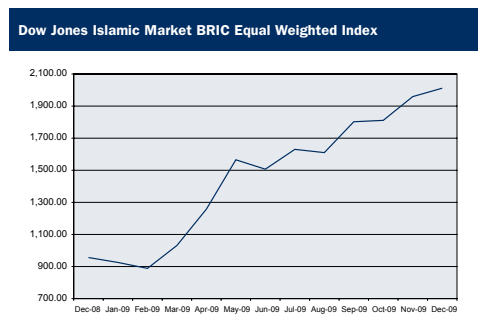
Last year was clearly the year of the emerging markets. The DJIM Indonesia Index advanced 133% in 2009 and ended at 1,196.90 points (as at close of trading on 22 December). Indonesia was followed by the DJIM BRIC Index (Brazil, Russia, India, China), which gained 103% over the year, closing at 1,943.01 points.



Three Sharia-compliant Dow Jones indexes – the DJIM Europe Titans 25, the DJIM US Titans 50 and the DJIM Japan – on the other hand, were among the worst performers of the DJIM indexes. They closed with relatively small annual returns of 23% (closing at 2,122.74 points), 19% (at 2,150.02 points) and 16% (at 1,003.45 points), respectively.

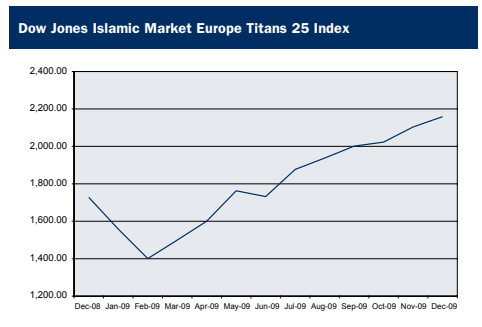


Recent experience has shown that while investing in Sharia-compliant stocks is not a hedge against equity market declines, the declines have been more modest than for the market at large. The lower leverage of the equities involved and lack of financial industry stocks are likely the main reasons. Consequently it appears that much of the time gains are not as high as those of the market as a whole due to lower leverage.



Where to from here?

In the coming years, the market for Islamic equities is expected to grow, as is the availability of Sharia-compliant equities. For example, In 2009 Dow Jones Indexes announced that Argentina, Colombia, Croatia, Lebanon, Mauritius, Nigeria, Peru, Saudi Arabia, Serbia, Tunisia, and Ukraine would be added to its Islamic Market Index universe. This increased the total number of countries in the Dow Jones Islamic Market Index universe from 57 to 68. Michael Petronella, president, Dow Jones Indexes said the expansion was “a reaction to market demand but also reflects the growing importance of



these countries for Islamic investors”.

In late 2009 surprisingly positive fundamental data replaced falling risk aversion as the driving force behind the equity markets' development. The end of the recession and the transition to a new growth phase will also feed through to corporate earnings. Bank Sarasin anticipates a continuing rise in earnings expectations in the coming months, which should support the stock market rally. Provided investor sentiment does not become overly optimistic, the risk of major setbacks is low and the markets should continue to advance, although minor setbacks due to the strong rally in 2009 may occur.

The key for Islamic investors will lie either in putting their faith in an Islamic index or indices which might offer modest returns, or in selecting a professional Portfolio Manager who closely monitors the markets to make active investments.

Real Estate



A lack of transparency hampers Islamic real estate investing

While the investor faces all the typical concerns regarding direct and indirect investing in real estate, particularly since the financial crisis, he must also consider whether the property investment is Sharia-compliant. In a direct investment, the building use and tenants' activities must all be reviewed, while for indirect investment, a variety of specialist funds are available for the Islamic investor.

Sharia-compliant real estate funds

There is no shortage of Sharia-compliant real estate funds. According to Islamic Finance Information Service (IFIS) there are 43 Islamic funds focused on real estate (please see IFIS Real Estate Funds Table, pg 28/29). Their assets account for 7% of all Islamic funds, not including some of the private equity and other funds with property exposure. The average amount invested in the 43 funds for which the IFIS has data is USD 119 million which suggests that the total invested is around USD 5 billion.

Performance figures are not available for many of the funds, which makes comparisons difficult and comparisons with other asset classes more challenging still. Such a lack of transparency means that investors cannot choose funds and fund managers based on historic performance.

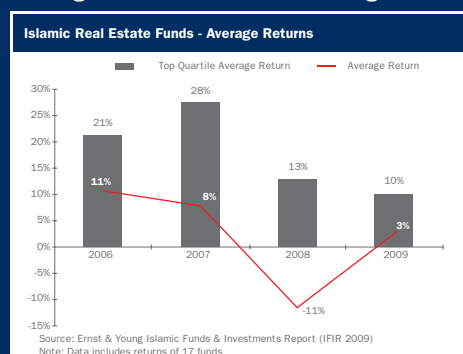
Islamic real estate funds have been researched by IFIS since August 2002. Just over five funds have been launched annually over the past seven years. While the number of new funds had been increasing, launches have dried up since the financial crisis began and some funds no longer exist. The relatively modest USD 80 million Inovent Real Estate Investment Trust is the only fund to have been launched since August 2008.

This is not surprising given market

performance. According to Ernst & Young's Investment Funds & Investment Report 2009, the average returns from Islamic real estate funds fell from 8% in 2007 to -11% in 2008 and rising to +3% in 2009.

Real Estate Investment Trusts

Islamic Real Estate Investment Trusts (REITs) are capital market vehicles for owning real estate and deriving income.



They can address some of the liquidity issues presented by real estate funds. These collective investments pool money from a variety of investors to buy, manage and sell real estate assets. A REIT can invest in income producing Sharia-compliant real estate or a Sharia-compliant Special Purpose Vehicles (SPV) that holds Sharia-compliant assets. Investors or unit holders in an Islamic REIT typically receive a proportion of the rental income generated from the assets as their return.

For the investor, these collective investments can offer exposure to larger

individuals otherwise could not access. Such investors may also find that these units are far more liquid than the underlying real estate assets. In other words, investors can invest in real estate through Sharia-compliant capital market instruments that are easily tradable.

In many respects, the Securities Commission of Malaysia is a leading light in issuing guidelines on Islamic REITs and their treatment. In 2005 the Commission issued its first set of guidelines for Islamic REITs, the first globally.

In summary, these guidelines state:

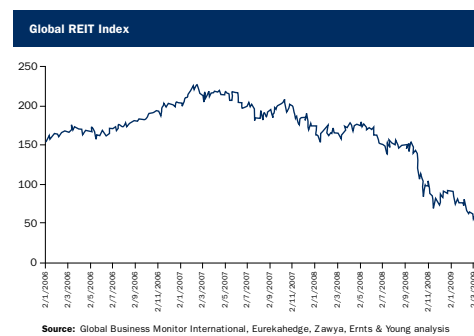
- Rental income must be derived from permissible business activities. Rental income from non-permissible activities cannot exceed 20% of the total turnover of the Islamic REIT.
- Islamic REITs cannot own properties in which tenants conduct non-permissible activities.
- Islamic REITs cannot accept new tenants whose activities are fully non-permissible.
- Only 20% of the floor area of a property can be utilised for non-permissible activities.
- All forms of investment, including deposit and financing instruments, must be Sharia-compliant.
- Property insurance must be based on Takaful except where Takaful schemes do not operate.
- Each Islamic REIT must have a Sharia Board responsible for ensuring that the Islamic REIT complies with Sharia principles.

In 2006, a research study called ‘Sharia Compliance in Real Estate Investment’ was undertaken by Muhammad Faishal bin Ibrahim and Ong Seow Eng of the Department of Real Estate of the National University of Singapore to compare the performance of Islamic and conventional REITs. The exercise was theoretical since

not enough Islamic REITs existed to undertake empirical research. To simulate this exercise, Ibrahim and Ong constructed a synthetic portfolio and analysed the returns. They stated that “Sharia compliance seems to create a return trade-off and less restrictive compliance requirements appear to provide better historical returns. However, Sharia compliance does not mean that Sharia-compliant real estate mutual funds necessarily under-perform relevant indexes when relevant risk factors are considered and allowing for differing sensitivities to benchmark returns”.

The authors concluded: “The acid test will be empirically possible only with time and as more Islamic REITs and real estate funds become established”. Experience over the past three years shows that REITs as a whole have not performed well in the cold light of the financial crisis as the following chart makes clear.

Despite the economic downturn, real estate remains a core asset class for investors, who have particular concerns. Islamic REITs



and many Islamic real estate funds mitigate liquidity issues, although for investment purposes more needs to be done to provide benchmark indices. In particular, the lack of public data on the performance of Islamic real estate funds needs to be addressed urgently if the sector is to mature.

IFIS Real Estate Funds Table

Date	Fund Name	Fund Domicile	Geofocus
09/04/2009	Inovent Real Estate Investment Trust	Bahrain	Gulf Cooperation Council (GCC)
25/08/2008	SHUAA Saudi Hospitality Fund	Saudi Arabia	Saudi Arabia
01/07/2008	Global GCC Real Estate Fund II	Bahrain	GCC
11/06/2008	Al Imtiaz Real Estate Fund	Kuwait	GCC
27/05/2008	Waed Real Estate Investment Fund	Kuwait	GCC
13/03/2008	Emirates Islamic Global Property Fund - Retail	Jersey	Global
13/03/2008	Emirates Islamic Global Property Fund - Institutional	Jersey	Global
28/02/2008	Danat India RIA Fund	India	India
18/02/2008	Islamic Turkey Real Estate Fund	Cayman Islands	Turkey
02/02/2008	Taibah KSB Real Estate Fund	Saudi Arabia	Saudi Arabia
01/10/2007	Global Real Estate Ijarah Fund	Bahrain	Middle East and North Africa
22/08/2007	OSK-UOB Asian Real Estate Fund	Malaysia	Asia Pacific
11/07/2007	Amar Real Estate Fund	Kuwait	Kuwait
30/05/2007	US Retail Realty Fund	United Arab Emirates	United States
23/05/2007	Markaz Real Estate Opportunities Fund	Kuwait	Middle East and North Africa
01/05/2007	Al Islami US Properties III Fund	United Arab Emirates	United States
27/02/2007	4-Year Capital Protected Global REIT Note	United Kingdom	Global
15/02/2007	Samba Real Estate Fund	Saudi Arabia	Global
31/12/2006	Boubyan Real Estate Sukuk Fund	Bahrain	Saudi Arabia
01/12/2006	US Development Opportunities Fund	Cayman Islands	United States
30/11/2006	Islamic European Real Estate Fund	Cayman Islands	Europe
16/09/2006	Boubyan Global Real Estate Fund	Kuwait	Global
01/08/2006	Global Asia Real Estate Fund	Cayman Islands	Asia
01/05/2006	Asian Real Estate Fund	Kuwait	Asia
01/03/2006	Prime Industrial Real Estate Fund 2	Kuwait	United States
24/01/2006	China Realty Modaraba Fund	Cayman Islands	China
24/07/2005	Global US Real Estate Fund	Cayman Islands	United States
01/07/2005	Emirates Real Estate Fund - AED	Jersey	UAE
01/07/2005	Emirates Real Estate Fund - Income	Jersey	UAE
01/07/2005	Emirates Real Estate Fund - Accumulation	Jersey	UAE
14/06/2005	GCC Real Estate Fund	Bahrain	GCC
17/04/2005	Awaed Real Estate Fund	Kuwait	GCC
01/02/2005	Amlak First Real Estate Fund	United Arab Emirates	UAE
01/11/2004	Solidarity European Real Estate Fund	Bahrain	Global
30/05/2004	Islamic Asian Real Estate Fund	Cayman Islands	Asia
01/05/2004	Al Islami French Property Fund	United Arab Emirates	France
20/04/2004	Solidarity International Real Estate Fund	Bahrain	Global
01/03/2004	Shuwaikh Real Estate Fund	Kuwait	Kuwait
01/10/2003	The US Commercial Properties Portfolio Fund	United Arab Emirates	United States
28/05/2003	Makaseb Real Estate Fund (Previously Aayan 1st Real Estate Fund)	Kuwait	GCC
01/02/2003	Markaz Real Estate Fund	Kuwait	Kuwait
29/08/2002	Al Dar Real Estate Fund	Kuwait	GCC

Source IFIS

	Asset Type	Base Currency	Fund Size (US\$m)	Fund Manager	Type
	Real Estate	BHD	79.81	Inovest	
	Real Estate	SAR	240	SHUAA Capital Saudi Arabia	Closed Ended
	Real Estate	USD	500	Global Investment House	Closed Ended
	Real Estate	KWD	N/A	Al Imtiaz Investment	Open Ended
	Real Estate	KWD	N/A	Al Dhow Investment Company	Open Ended
	Real Estate	USD	N/A	Emirates Fund Managers (Jersey) Limited	Open Ended
	Real Estate	USD	N/A	Emirates Fund Managers (Jersey) Limited	Open Ended
	Real Estate	AED	57.18	Khaleeji Commercial Bank	Closed Ended (Renewable)
	Real Estate	USD	N/A	Wafra Investment Advisory Group	Closed Ended
	Real Estate	SAR	52.01	KSB Capital Group	Closed Ended
	Real Estate	USD	75.4	Global Investment House	Closed Ended
	Real Estate	MYR	N/A	OSK-UOB Unit Trust Management Bhd	Open Ended
	Real Estate	KWD	N/A	Amar Finance and Leasing	Closed Ended (Renewable)
	Real Estate	USD	47	Investcorp Bank B.S.C	Closed Ended
	Real Estate	USD	200	Kuwait Financial Centre (Markaz)	Closed Ended (Renewable)
	Real Estate	USD	N/A	Investcorp Bank B.S.C	Closed Ended
	Real Estate	USD	N/A	Dubai Islamic Bank	Closed Ended
	Real Estate	SAR	N/A	Samba Asset Management	Open Ended
	Real Estate	USD	150	Boubyan Bank	Closed Ended
	Real Estate	USD	48.42	Shamil Bank	Closed Ended (Renewable)
	Real Estate	EUR	N/A	Wafra Investment Advisory Group	Closed Ended
	Real Estate	KWD	N/A	Boubyan Bank	Open Ended
	Real Estate	USD	100	Global Investment House	Closed Ended
	Real Estate	USD	250	Kuwait Finance House	Closed Ended
	Real Estate	USD	N/A	Kuwait Finance House	Open Ended
	Real Estate	USD	150	CIAM-Shamil Asset Management Ltd.	Closed Ended
	Real Estate	USD	100	Global Investment House	Closed Ended (Renewable)
	Real Estate	AED	N/A	Emirates Fund Managers (Jersey) Limited	Open Ended
	Real Estate	USD	N/A	Emirates Fund Managers (Jersey) Limited	Open Ended
	Real Estate	USD	262	Emirates Fund Managers (Jersey) Limited	Open Ended
	Real Estate	USD	100	Global Investment House	Closed Ended (Renewable)
	Real Estate	KWD	N/A	Aayan Leasing & Investment Co	Closed Ended (Renewable)
	Real Estate	USD	75	Amlak Finance	Closed Ended
	Real Estate	EUR	10.07	Solidarity BSC(c)	Open Ended
	Real Estate	USD	N/A	Wafra Investment Advisory Group	Closed Ended
	Real Estate	EUR	39.6	Dubai Islamic Bank	Closed Ended
	Real Estate	USD	15.65	Solidarity BSC(c)	Open Ended
	Real Estate	KWD	N/A	Al Madar Finance & Investment	Open Ended
	Real Estate	USD	30	Dubai Islamic Bank	Closed Ended
	Real Estate	KWD	N/A	Aayan Leasing & Investment Co	Closed Ended (Renewable)
	Real Estate	KWD	103.15	Kuwait Financial Centre (Markaz)	Closed Ended
	Real Estate	KWD	N/A	Al Dar Asset Management	Closed Ended

Sukuk



The place of fixed income in a balanced portfolio

Fixed income plays a part in any conventional diversified portfolio, particularly for ultra high net worth individuals. Bonds, both corporate and sovereign, can offer investors a fixed rate of return over a specified period that is often comfortably in excess of the prevailing rate of time deposit rates. As a result, such instruments can offer a significant element of stability and predictability that helps to offset the risks represented by more speculative elements of a portfolio.

Traditionally, the appeal of such instruments was underpinned by several important factors: whether the bonds were rated by a reputable rating agency and whether they were listed on an exchange and were therefore tradable. Many huge investment vehicles, such as pension funds, can only invest in 'investment grade' debt, basically rated 'A' and above.

In the past, the rating of Islamic debt instruments, or "Sukuk", has not been a pre-requisite for many investors and many unrated Sukuk have been massively oversubscribed. This may have led issuers to believe that a rating was an unnecessary extra expense.

The same might be said of listing a Sukuk on an exchange. Previously, Sukuk investors held their investments to maturity simply because there were so few Sharia-compliant assets available. This began to change as Sukuk issuance grew to the heady levels that the market witnessed in 2007 and 2008, and trading became slightly more commonplace. HSBC, for instance, became a market maker in Sukuk although the volumes traded were generally thin.

Malaysia was always a different proposition due to its very active primary and secondary Sukuk market. This is in part because of strong government and

central bank support for the Islamic debt capital market, and also because every Sukuk issued in Malaysia must have a rating. Generally Malaysian Ringgit-denominated Sukuk would be rated by one of the domestic rating agencies, Rating Agency Malaysia Berhad (RAM) or Malaysian Rating Corporation Berhad (MARC).

New realities

The financial crisis has increased the size of the world's debt markets. In 2009, bond issuance by corporates was about USD 1.7 trillion, 80% of which was investment grade, according to Bank Sarasin. Debt issuance increased as corporates found it difficult to borrow from banks, and as investors were lured by attractive corporate bond returns.

The Nakheel conundrum

Dubai government-owned developer Nakheel had a USD 3.52 billion Sukuk which matured in mid-December 2009, together with an approximately USD 500 million profit payment on the Sukuk. Nakheel has been hard hit by the financial crisis, particularly since the value of property in Dubai had halved.

In early November the government of Dubai had to repay a five-year USD 1 billion Dubai Global Sukuk issued in 2004 on behalf of the Dubai Civil Aviation

Authority. While some observers have speculated that refinancing the Sukuk would be expensive, the Dubai Department of Finance advised Zawya Dow Jones in September 2009 that defaulting on the Sukuk “isn’t an option”.

However shortly afterwards, DP World, a government-owned entity, requested a ‘standstill’. Investor concerns drove the Sukuk price of its subsidiary, Nakheel, to 40 cents on the US dollar. The Sukuk had been volatile due to the financial crisis, but shortly before the standstill request, confidence returned and by mid-September prices rose from 63.5 cents to 102.5 cents on the US dollar in February 2009. Ultimately, the Nakheel Sukuk was paid on time with support from the neighbouring Emirate of Abu Dhabi.

As a result, the implicit sovereign rating of government-owned entities will no longer be taken for granted by investors – any new issuance will require an explicit guarantee assigned with the credit standing of the sovereign, at least in the region.

Other question marks

Two other developments have caused concern about Sukuk. One is the bankruptcy filing by East Cameron Partners in the US, which was behind the issuance of the US’s first and only Sukuk. How the courts deal with this bankruptcy will be crucial in determining what happens to Sukuk under these circumstances. In legal terms, since this is largely uncharted territory, Sukuk holders will be keen to see where they appear on the list of creditors. The other is the default by Investment Dar of Kuwait on a Sukuk payment that matured in 2009. As a result, Sukuk are no longer viewed as safe havens that offer predictable returns with minimal risk.

Beyond these investor concerns, furore broke out when it was incorrectly reported that Sheikh Taqi Usmani declared that 85% of Sukuk were not Sharia-compliant. Usmani had said no such thing and his remarks were directed towards certain malpractices in structuring Sukuks based on partnerships (Musharaka). But the controversy demonstrated investor insecurity regarding the Sukuk market.

Total			2008	2009				
		Total Sukuk Issued	14.9	23.3				
		Cumulative Sukuk Issuance	76.7	100.0				

Total			2008	2009				
By country	2009 (in USD)	Bahrain	1,360.1	5.8%	2008 (in USD)	Bahrain	684.5	4.6%
		Brunei Darussalam	148.0	0.6%		Brunei	95.1	0.6%
		Gambia	7.2	0.0%		Gambia	12.1	0.1%
		Indonesia	1,744.5	7.5%		Indonesia	663.7	4.5%
		Malaysia	12,611.6	54.1%		Kuwait	190.0	1.3%
		Pakistan	364.6	1.6%		Malaysia	5,497.9	36.9%
		Saudi Arabia	3,109.2	13.3%		Pakistan	476.3	3.2%
		Singapore	35.8	0.2%		Qatar	300.9	2.0%
		UAE	3,330.6	14.3%		Saudi Arabia	1,668.9	11.2%
		US	600.0	2.6%		UAE	5,300.2	35.6%
				23,311.6		100.0%		
By currency	2009	AED	680.6	2.9%	2008	AED	5,163.6	34.7%
		BHD	610.1	2.6%		BHD	334.5	2.2%
		BND	148.0	0.6%		BND	95.1	0.6%
		GMD	7.2	0.0%		GMD	12.1	0.1%
		IDR	1,094.5	4.7%		IDR	663.7	4.5%
		MYR	11,111.6	47.7%		MYR	4,947.9	33.2%
		PKR	364.6	1.6%		PKR	476.3	3.2%
		SAR	2,259.2	9.7%		SAR	1,668.9	11.2%
		SGD	35.8	0.2%		SGD	1,527.5	10.3%
		USD	7,000.0	30.0%		USD	14,889.6	100.0%
		23,311.6	100.0%					

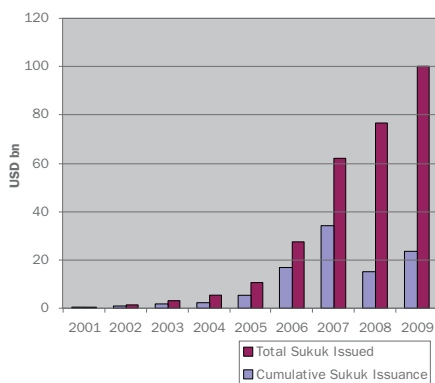
Source: Standard & Poor’s

The year 2009 for Sukuk

According to data received from Standard & Poor's, new Sukuk issuance in 2009 increased to USD 23.3 billion compared to USD 14.9 billion in 2008. The geographic spread of Sukuk issuance showed a marked resurgence in Asia in general and Malaysia in particular with 54% of the total volume. Saudi Arabia also saw an increase from USD 3.1 billion in 2009 compared to USD 1.7 billion in 2008.

Interestingly, market turbulences led to a recovery in US dollar (USD) issuance, which reached USD 7 billion in 2009 from only USD 1.5 billion in 2008, while Arab Emirates dirham (AED)-denominated issues dropped to AED 680.6 million (AED 5.2 billion in 2008). The reason behind this is two-fold: First, the price to issue a Sukuk in AED became much higher than in USD, and secondly, the credit environment was not supportive. The strong increase in Malaysia, Indonesia and Saudi Arabia shows the importance of local debt markets, which are helping to insulate domestic markets from the overall global crisis. International investors are unlikely to be attracted to domestic issues because they create foreign-exchange exposure. As an example, only wealthy Muslim investors in Indonesia are likely to invest in an Indonesian Rupiah-denominated product.

Total Sukuk Issuance (2001-2009)



While Sukuk issuance dropped significantly during the crisis, it seems to have recovered as the following chart shows:

According to S&P there are still significant issues facing the Sukuk industry in the years ahead. These include:

- Difficult market conditions, which are slowing the planned issuance of numerous Sukuk;
- The lack of standardisation, notably of Sharia interpretation; and
- The low liquidity of the Sukuk market, which constrains investors trying to exit the market in times of turbulence, and limits access to distressed sellers.

The market is unlikely to grow until default and bankruptcy situations are clarified.

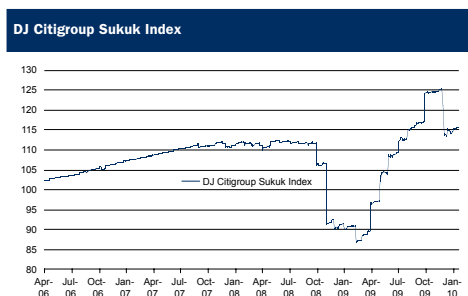
The Islamic Development Bank

The Islamic Development Bank (IDB) has often been the subject of discussions concerning Sukuk since the institution has a significant history of issuing landmark transactions over the years. 2009 was no exception and the IDB came to market with a USD 500 million issue in early September. The marketing roadshow covered Saudi Arabia, the UAE, Malaysia, Brunei, Tanzania, the UK, Singapore, and Switzerland, showing that oversubscription these days is not automatic, even for issues from the triple-A rated IDB. "According to the IDB, 'The Sukuk has a tenor of five years, and is priced at 77 basis points over US Treasuries. The order book for the Sukuk was USD 2 billion, 2.4 times oversubscribed despite being offered during Ramadan, the month of fasting. The final size of the issue was USD 850 million."

The prospects for Sukuk and the wealth management industry

There is no doubt that the Sukuk market has reappeared on the radar of many investors over the past year. Despite the challenges that the Sukuk market has witnessed over the past 18 months, there is a place for a

fixed-income product in most portfolios. A number of financial institutions have already started their own Sukuk funds.



The secondary market trading of Sukuk in 2009 showed some activity but especially high volatility in pricing, as shown by the DJ Citigroup Sukuk Index.

We are likely to see a 'flight to quality' with listed Sukuk from triple-A rated issuers snapped up while the unrated and unlisted languish. We may also see a trend toward only blue-chip managers and lead managers bringing issues to market. While this would be good for some issuers and investors, it could knock out the smaller issuers that have come to typify the Sukuk market, unless they pay a substantially higher return.

It is likely that Sukuk will be priced in a much more competitive fashion as they compete with other Sharia-compliant and non-Sharia compliant products.

In Malaysia there is a trend for a single set of documentation for Islamic Medium-Term Note programmes that can be used for multiple issues by the same issuer. These are sensible and could be a useful addition to the battery of US dollar-denominated instruments. The next six to 12 months are likely to be fascinating for the Sukuk niche, whether or not the much discussed USD 50 billion 'pent up demand' for Sukuk materialises.

The Middle Eastern business portal Zawya has encouraged debate and discussion on expanding and enhancing secondary market trading in Sukuk, establishing an online forum that has received fascinating insights from market participants. Besides the need for well-rated Sukuks, investor demand for medium and long-term fixed coupon Sukuks has not been addressed.

These discussions indicate that the industry itself is ready to take the next step towards maturity. If this leads to more rated and listed Sukuk on the primary market, and healthy trading on the secondary market, this can only be good for the UHNW investor looking for a stable and predictable asset for his portfolio.



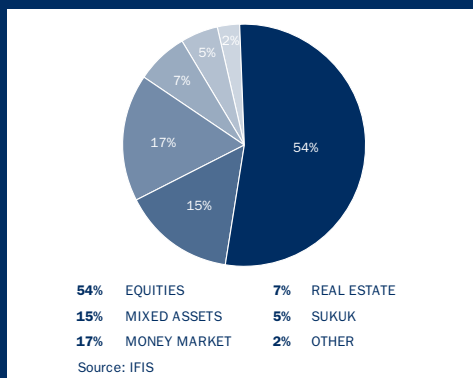
Islamic Funds



Islamic Funds

Islamic funds are the most dynamic part of the Sharia-compliant sector, with increasing demand from investors and greater wealth held by these investors. The Asian Development Bank estimates that Islamic assets, estimated at USD 1 trillion, will increase 10-15% per year.

The Islamic Finance Information Service (IFIS, the Islamic finance portal of Euromoney) has one of the most extensive databases on Islamic funds. As of mid-October 2009 it listed 556 Islamic funds with a total value of USD 22.8 billion. These funds are focused on a variety of asset classes as the following pie chart shows:



Most funds are targeting regional investments, mostly GCC/MENA (Middle East and North Africa), international, Asia/Pacific and other emerging markets. The average year-end performance is fairly close to its index benchmarks. Hence, to be successful, an investor needs to form an opinion on the management and their commitment and ability to outperform, rather than to track the index performance.

In 2009 new Islamic funds were brought to market to capitalize on the growing interest in Sharia-compliant funds, despite the crisis. Funds are being launched at an unprecedented rate, with some coming from non-Islamic finance houses such as NBK (National Bank of Kuwait), which launched its first Islamic KD Ijara Fund in June. The second Islamic KD Ijara Fund II, launched in August, was fully subscribed in one day. Responding to investor demand, a month later NBK launched the KD Ijara Fund III, offering investors the equivalent of 6% per annum throughout the life of the fund. Minimum investment in the Kuwait Dinar-denominated fund is USD 100,000.

Almost concurrent was the launch of the Shamil Solid Return Fund, a Sharia-compliant multi-asset investment fund from the Shamil Bank of Bahrain. According to the bank, the fund is designed specifically for the expert investor who is looking to diversify in the current market. Although small at USD 25 million, the fund invests in a mixture of assets including Islamic equities, Sukuk, Mudaraba investments and crude oil.

In November 2009 QInvest from Qatar established a USD 200 million five-year mezzanine fund with Fortis Bank

		31.12.2008	31.12.2009	Return 2009	Islamic Funds compared
Dow Jones Islamic World Index	DJIM	1,475.9	1,974.8	34%	27.0%
Dow Jones Islamic Asia-Pacific	DJIAP	870.9	870.9	50%	48.3%
Dow Jones Islamic Emerging Markets	DJIEMG	1,168.8	1,168.8	74%	43.2%
GulfBase GCC Index				12%	9.0%

Source: Bloomberg, Trustnet Middle East

Nederland to buy shipping assets to take advantage of falling prices in the maritime sector. The Sharia-compliant fund will invest over the next 18 months after its launch. The fund demonstrates that Sharia-compliant vehicles are being used more opportunistically to optimize market opportunities created by the financial crisis.

Abu Dhabi's The National Investor (TNI) and Kipco Asset Management Company (Kamco) set up a USD 150 million Islamic fund in September 2009, further proof that Islamic funds are attracting players who operate as conventional financial institutions. It is a sign that the market share of Islamic financial products in the GCC is still on the rise. TNI and Kamco will each contribute USD 15 million to the fund, while the remaining USD 120 million will come from third-party investors. The target return for the investments is 30%. The Sharia-compliant fund aims to make six or seven investments with an average equity of USD 25 million each in mid-size, family-owned companies that require external funding to survive the financial crisis.

The importance of Islamic funds is expected to grow. The Ernst & Young Islamic Funds and Investment Report for 2009 seems prescient when it stated, "Despite this setback, the fundamentals of the Islamic fund industry remain strong. With almost USD 50 billion in fund assets under management and a large, expanding and untapped Muslim population, there are likely to be considerable opportunities in the future. This is a time when strategic choices have to be made and market participants have to adapt to survive".

A controversial product

With investors' continued frustration over the shortage of Sharia-compliant investment opportunities, financial engineers

have tried to manufacture alternatives. One of the most controversial is the use of hedging structures in Islamic finance. Many Islamic investors believe hedge funds are not linked to the real economy and involve short selling equity, which is prohibited. Despite various Fatwas (Islamic legal opinions) this perception remains unchanged, effectively stopping the development of this sector.

That doesn't mean the fund management companies haven't tried, given the potential rewards. Despite efforts since 1997, the sector remains small. To date, there does not appear to be an Islamic hedge fund which has substantial assets under management. Due to this, and the uncertainty regarding hedge funds in general, substantial investment in this field is not expected in the short term, with investors preferring to allocate funds to their standard long-only equity funds and portfolios.

Long-only instead of long-short

Hence, most investors will look forward to the classical long-only equity strategies, which, on average, yielded around 27%.

Islamic indexes went up in 2009 with many investors missing out for fear of incurring losses. The most challenged areas are those funds which were launched before the crisis but are substantially leveraged, mostly non-equity funds, and often real estate funds. For the equity industry it was a good year, which may persist in 2010, although risks of a setback exist, requiring thoughtful stock and manager selection.

Private Equity and Venture Capital



Private equity has Sharia appeal

There is a close relationship between the Islamic tenets of investing and private equity. By definition private equity is participatory so an investor shares both risks and rewards. If a company seeking capital complies with Sharia laws, and is not heavily indebted, few forms of co-investing could be more appropriate from a Sharia-compliance perspective, given transparency.

Industry estimates suggest that the global conventional private equity market is worth about USD 2.2 trillion. Fundraising by private equity firms was badly hit by the global financial crisis, with 2009 its worst year since 2004. Only USD 246 billion was raised by 482 funds worldwide, according to the latest 2009 figures. Data from Preqin, a leading source of information for the alternative assets industry, showed that only USD 35 billion was raised in the fourth quarter of 2009, which is the lowest quarterly fundraising since the third quarter of 2003, according to Zawya. The crisis hit hard, especially as private equity firms operate with high levels of leverage and credit is no longer available.

Although official figures for the Islamic private equity industry do not exist, estimates suggest that these funds accounted for about USD 4 billion in 2009 compared to USD 20 billion of the total GCC Private Equity industry according to Zawya Private Equity Monitor. This is far less than the USD 40 billion forecast for the industry by 2011, and a fraction of the total Islamic finance industry, estimated at USD 800 billion.

There are only 17 Islamic private equity funds identified. The largest is Abraaj Capital's Infrastructure and Growth Capital Fund (IGCF), accounting for half the total. The USD 2 billion fund, sponsored by Deutsche Bank and Ithmaar Bank, closed in December 2007 and was not topped in size until 2009.

The GCC private equity industry as a whole, including conventional activities, developed very well until 2009 when the total size of funds dropped below USD 1 billion, compared to USD 9 billion the year before. The size of entry transactions fell from USD 1.44 billion to USD 156.8 million, while exits dried up completely. This means that the GCC private equity market volume was effectively hit harder than the global market.

The Islamic private equity industry is still in its infancy. As per much of the Islamic finance industry, more expertise is required for this specialized sector to mature. There is, however, an opportunity in every challenge: with private equity suffering from high leverage pre-crisis, the post-crisis industry may be more restrained and gain ground from an Islamic perspective.

Fund Analysis

	Total	2009	2008	2007	2006
Number of Funds	67	3	20	17	27
Total Size of Funds (USD mn)	19,659.5	900	9,159.8	5,607.6	3,992.1
Average Size of Funds	293.4	300	398.3	215.7	137.7
Transaction Analysis		2009	2008	2007	2006
Entry Transactions		17	52	76	65
Total size of entry transactions (USD mn)		156.8	1,446.6	3,611.8	1,747.2
No. of exits		2	17	20	16
Total Size of Exits		0	2,961.7	1,366.6	119.9

Venture Capital

Since venture capital investors are a particular breed it is unlikely that many investors will become venture capitalists. In this report, venture capital is defined as seed capital for a new venture in the process of being established, rather than capital for facilitating the growth of small business.

Rather like its cousin, private equity, venture capital seems ideal for Islamic finance through the application of various Islamic financing concepts, with the Mudaraba concept (profit sharing between investor and manager and loss bearing by the investor) being the most common.

Like its conventional counterpart, Islamic venture capital appeals most to investors who understand a sector or an industry intimately and are prepared to risk a portion of their capital on the strength of a business plan, the proposed management team, and the investor's ability to pick

a winner. Both Islamic venture capital and conventional venture capital deals are small compared to private equity transactions.

As the chart shows, there are very few Sharia-compliant venture capital funds. Funds that do exist tend to be misnamed private equity funds or even real estate funds with a venture capital gloss.

Few governments have done much to encourage the growth and development of Islamic venture capital funds. The exception is Malaysia which launched a small USD 10 million fund in 2008. In the meantime, Islamic venture capital investing is generally conducted by wealthy families. The efforts of organizations such as the Gulf Venture Capital Association will be critical to the growth of this sector and should lead to more cooperation, greater professionalism and the exchange of experience.

Sharia-compliant Private Equity & Venture Capital Funds October 2009

Status	Fund Name	Closing Date	Fund Manager	Investment Focus	Geographical Focus	Fund Size
Fund Raising	Al Fares Private Equity Fund	-	Al Mal Capital	Buyout	MENA	-
Investing	Al Mal Capital Partners Fund L.P.	Apr 08	Al Mal Capital	Buyout	MENA	USD 40 mn
Investing	Alimtiq Investment Fund	-	Al Imtiq Investment Company	Buyout	MENA	-
Fund Raising	CMH Enterprise Fund 1	-	Capital Management House	Buyout	GCC	-
Fund Raising	CORECAP Islamic Private Equity Fund I (CIPEF I)	-	CORECAP	Buyout	MENA	-
Investing	Eastgate MENA Direct Equity L.P.	Nov 07	Eastgate Capital Group	Growth Capital	MENA	USD 250 mn
Investing	GCC Real Estate Fund	2005	Global Investment House	Real Estate	GCC	USD 100 mn
Investing	Global MENA Financial Assets	2008	Global Capital Management Limited	Buyout	MENA, South Asia, Turkey	USD 500 mn
Liquidation	Gulf Springs Real Estate Fund	-	Unicorn Investment Bank	Real Estate	GCC	-
Investing	Infrastructure and Growth Capital Fund	16 Oct 07	Abraaj Capital	Buyout	MENA	USD 2,000 mn
Announced	Kunooz Islamic Opportunities Fund		The National Investor KIPCO Asset Management Company	Buyout	GCC	USD 150 mn
Investing	Markaz Real Estate Fund	Feb 03	Kuwait Financial Centre	Real Estate	Kuwait	USD 84.41 mn
Investing	Mezzanine Investment Partners II Limited	30 Oct 08	SHUAA Capital Amwal Qinvest	Mezzanine Capital	GCC	USD 199.92 mn
Fund Raising	NBD Sana Capital	Feb 08	Sana Capital	Buyout	MENA, Turkey	USD 500 mn
Investing	Rasmala MENA Private Equity Fund 2	30 Nov 08	Rasmala Investments Holding	Buyout	GCC	USD 120 mn
Investing	Shefa HealthCare Fund E.C.	Aug 07	Injazat Capital	Buyout	MENA	USD 60 mn
Investing	The Libya Fund	Q4 2007	Tuareg Capital	Venture Capital	Libya	USD 30 mn

Source: Zawya's Private Equity Monitor

Economic Outlook



Economic Outlook 2010 by Bank Sarasin: The decisive year

An unconventional monetary policy and fiscal policy stimuli have saved the global economy from a deflationary spiral and powered a powerful cyclical recovery in H2 2009, which continued into Q1 2010. Nonetheless, initial indicators suggest this upswing will peter out from Q2 and growth should slow again. The powerful headwind triggered by the moribund financial system and heightened pressure on consumers to save will remain. Rising domestic demand in the emerging market economies is the only factor that can turn the upswing into a sustained recovery in 2011.

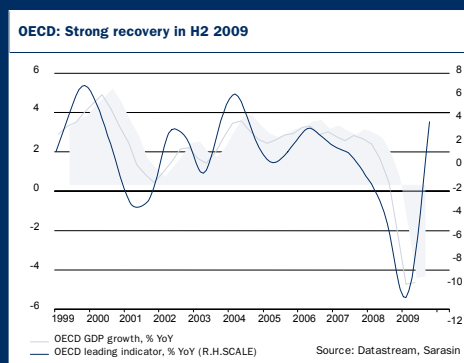
Like a phoenix rising from the ashes: An upswing from H2 2009 . . .

2009 will certainly be regarded as one of the most curious years in economic history. The global economy experienced one of its blackest moments, which will be dubbed “The Great Recession” by many economic historians. After the bankruptcy of investment bank Lehman Brothers in September 2008, global money and credit flows dried up, causing a sudden increase in risk aversion. However, the fact that a downward spiral of job losses, production declines, falling asset prices and bank collapses along the lines of the Great Depression of the 1930s did not materialise is largely due to the authorities’ valiant response to the crisis. First, just about every government issued guarantees for banks relevant to the financial system and shored them up with bailout packages. Second, for the first time central banks around the world applied unconventional measures synchronously, transcending the standard tools of interest-rate policy. This provided the economy with an unprecedented level of liquidity and almost doubled central banks’ balance sheets. Third, finance ministers in the major industrialized countries devised government stimulus packages that generally totalled 10% of their national GDPs. By the end of 2009, these measures had already started to

bear fruit and had triggered a cyclical upswing, which promised to be as powerful as the previous downturn.

...but whether this proves to be lasting will only become apparent in 2011

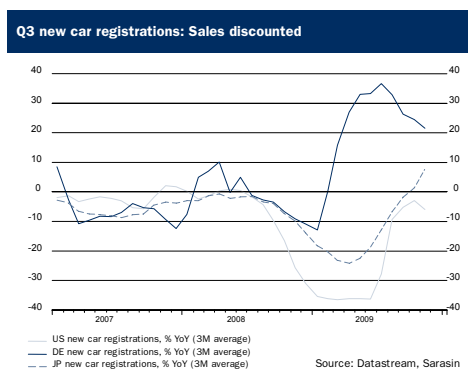
Whereas economic history will view 2009 as the year of fiscal stimuli, many observers expect 2010 to be the year in which policymakers discontinue the lax monetary and fiscal policy. Even if several emergency measures designed to bolster liquidity during the severe financial crisis do expire, the economy will still require quantitative monetary easing instruments. The upswing is too fragile for this policy to be discontinued without triggering an economic relapse. Instead, we believe 2010 will be the year that determines whether the upswing is sustainable. Despite the fact that we confidently expect this question to receive a positive answer by the beginning



of 2011, the economy still has a long way to go before it is self-sustaining. We still cannot completely rule out the possibility that the industrialized countries will take the same route Japan took in the last 20 years: deflationary development with rising debt levels and weak growth. The issue in 2010 is going to be how to turn the recovery into a sustainable upswing.

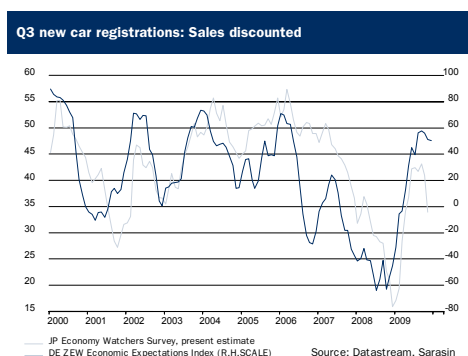
Leading indicators suggest powerful growth rates initially

The economy has to pass through a number of economic phases to reach a sustainable level of development. This pattern was apparent last year: The rise in global leading indicators sparked (as usual) the first phase of the new cycle at the beginning of 2009. After the doom-and-gloom atmosphere of March, the rising level of sunlight in spring revealed the first green shoots of recovery. Hopes that the economy would soon turn the corner were confirmed by growth figures in Q3 2009. In this second phase of the upswing, growth depended on government demand, which supported consumption in particular (cash-for-clunkers programme). The sudden stabilisation of end demand revealed the need to restock inventories, which had dropped to minimum operating levels. According to historical correlations, the start-up of production should lead to the third phase of the upswing: a rise in investments that were neglected and curtailed during the recession year. Based on the data published thus far, this is expected in Q4 2009. Investments boost efficiency levels at first, but they also create jobs to an increasing degree. Hence, we expect all the concerns about a so-called “jobless recovery” will be swept from the table in Q1 2010 with the turnaround in the US labour market. If, in future, the improvement in the labour market translates into income and consumer confidence, the recovery will enter the fifth phase: it will be sustainable.



Initial signs that the recovery is losing steam

But until we reach this point, we cannot know for if the upswing is also actually sustainable. In fact, a number of factors suggest that the growth spurt could soon subside. Most of the original growth stimulus was driven by government-induced one-off effects. Consumer incentives such as the cash-for-clunkers programme are not lasting impulses. On the contrary, there is a risk that they will not only prevent structural change but also push up demand and, thus, leave a vacuum the following year. Second, the reduction in inventories was not as significant as the drop in sales. Hence, the expected restocking could soon vanish again and the usual multiplier effect could fail. But the biggest danger is that the decline in assets could prompt a steady increase in households’ savings ratio. Above all in the US, the UK and Spain, there is a risk that due to the negative asset price effect, the savings ratio will increase precipitously



and growth in income will not be able to support consumption.

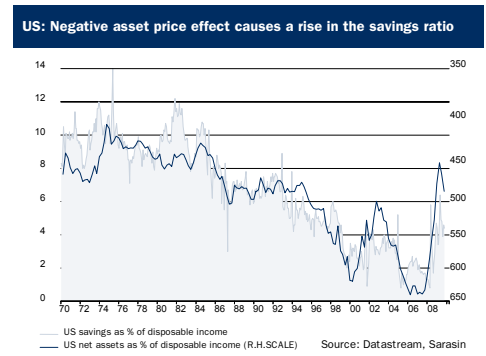
Slowdown from Q2 2010 is unavoidable

There are initial signs that the growth momentum is weakening. Several leading indicators, which showed a turnaround several months before the economy as financial markets hit a low in March 2009, appear to have already reached their peak in Q4 2009. More specifically, the German ZEW Economic Expectations Index, as well as the Consumer Sentiment and Economy Watchers Index in Japan, indicate with their usual six-month lead time the possibility of a cyclical relapse as early as Q2 2010. Also, the momentum (3-month average minus 12-month average) of the US Purchasing Managers' Index (ISM) has passed its peak. If momentum decreases, it does not necessary mean that these indicators, which lead the cycle, have definitely passed their peak. Nonetheless, our analysis shows that even in the event of such a spectacular rise in momentum, the upper turning point of the ISM occurs four to five months after the change in momentum. If we adopt the approach taken by our analysis, we would expect to see from March 2010 onward another downtrend from a level of almost 60 in Q1 2010, which should send the ISM Manufacturing Index back below the level of 56 from May onwards, and down to 52 as of September 2010. By year-end 2010, a further decline should evoke strong doubts about the sustainability

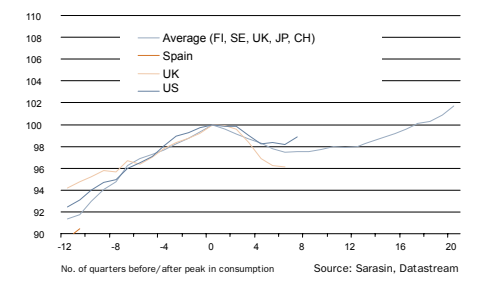
of the upswing and even revive fears of a recession. Whether or not these fears dissipate in 2011 will depend on the solutions that are found to the structural problems facing the global economy.

Deleveraging: A secular challenge

In order to grasp the scope of these structural problems, it is worth taking a step back and investigating the cause of the last boom-and-bust cycle. The real estate bubbles that occurred in recent years in a number of global regions were not isolated events. Instead, they were associated with a worldwide increase in leverage (borrowing ratio). With the drop in growth volatility and inflation since 1980, domestic credit as a percentage of gross domestic product (GDP) increasingly expanded. Part of this sustained increase in lending activities is explained by financial deepening. However, the acceleration in recent decades is ascribed to the rise in borrowing on the basis of rising asset values. After the tech bubble burst in 2000, one might have thought that the



After real estate crises, average consumption only returns to its original level after four years



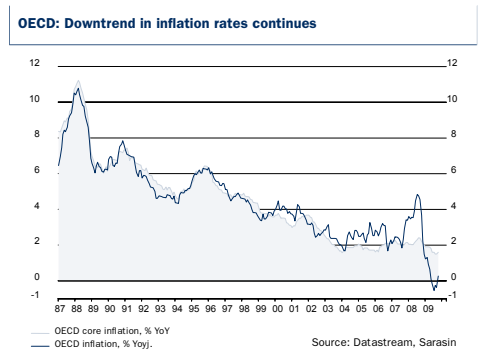
ensuing negative asset price effect would significantly dampen private consumption. But bold interest rate cuts by the central banks prevented an excessive correction. Instead, the next asset price bubble was created – this time in real estate markets in the US and on the periphery of the eurozone – increasing the leverage of these economies further. Although central banks around the world also boldly intervened

after the real estate bubble burst, the fact remains that the more authorities use fresh rate cuts and credit expansion to fight bubbles, the blunter the instrument of monetary policy becomes. The painful deleveraging process, (i.e. reducing the borrowing ratio) cannot be put off any longer. It will dampen potential growth in the new decade but, notably, it runs the risk of plunging the global economy into another recession.

Banks must downsize

Although the bubble in real estate prices only occurred in a handful of regions, credit risks were exported throughout the world due to the emergence of securitisation and the globalisation of the financial system. Banks in economies with surplus capital and visible exports, such as Japan, Germany and Switzerland, financed deficit countries like the US, the UK and Spain and their real estate bubbles. When the value of their assets declined and funding sources dried up on the liabilities side, hundreds of banks had no choice but to apply for government bailouts and guarantees. Even those that managed to continue operating under their own steam rely on the central banks' zero interest rate policy. This policy allows them to use the steepness of the yield curve and absorb write-downs on bad loans and toxic assets via retained earnings. However, there is a side effect in that they cannot expand as much in the riskier – but economically essential – credit business. Although far-reaching changes in accounting regulations have allowed banks to hide bad loans and worthless mortgage papers in their balance sheets, this has bought them time, whereby profits made over the next few years will be used to write off these positions. Market pressures, together with the regulatory authorities, are forcing banks to reduce their leverage and retain a bigger share of equity. Proposals issued by the Basel

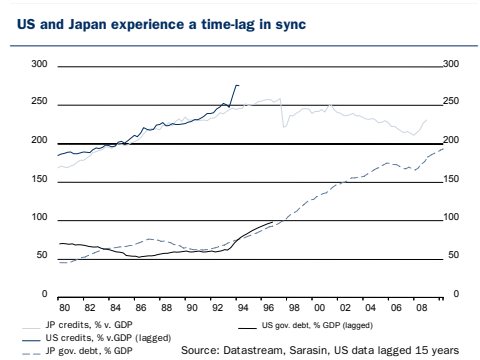
Committee on Banking Supervision include guidelines to tighten regulations. We therefore believe the so-called leverage



ratio (equity/total assets) could climb as high as 5% and the core capital ratio (core capital/risk-weighted assets) could rise above 13%. Hence, banks will expend great efforts in restoring their balance sheets, which will keep them occupied for the foreseeable future. The next cycle will have to do without any tailwinds from credit expansion.

Disinflation continues

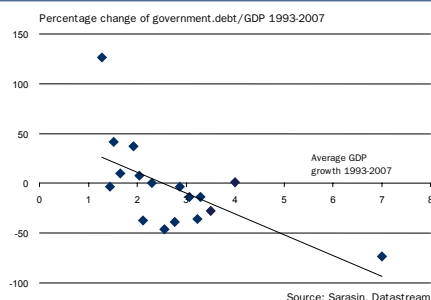
Against a background of weak lending activities and a rising savings ratio, inflation is not expected in the foreseeable future. In fact, past experience of real



estate crises in Finland, Sweden, the UK, Japan, and Switzerland shows that core inflation slowed on average from 8% to below 2% in the four succeeding years. Ireland's core inflation rate was already

negative at the turn of 2009/10, while Spain is on its way there. However, retreating core inflation rates are also evident in the export-dependent regions of the global economy which, like Japan and Germany, are not suffering a steep slide in real estate prices. Even after the cyclical recovery, capacity utilisation in the industrial sector remains extremely low throughout the world and dampens the price trend. Monetary developments may not change this because the money multiplier and the velocity of money have dropped noticeably. The trend in commodity prices should lead to a rise in headline inflation at the beginning of the year. By mid-2010, the positive base effect will probably no longer apply and deflationary concerns will move to the fore again.

Negative correlation: The greater the growth, the faster the decline in the debt-to-GDP ratio



Governments take on mountains of private debt

Leaving the adjustment of the banks' and private households' leverage ratio to the market would have put an enormous strain on GDPs and price levels. Governments stepped into the breach to ease this process. National finances across the globe helped to cushion the deflationary pressure by: 1) nationalising banks and taking over their debts; 2) subsidising companies; and 3) supporting private households via tax benefits, consumer incentives and social transfers. This is very reminiscent of Japan in the 1990s. After

the Japanese real estate bubble burst, loans to the private sector contracted from 250% of GDP in 1996 to a little over 210% of GDP in 2008. During the same period, the national debt rose from almost 100% to 160% of GDP. If we turn back the economic hands of time 15 years in the US, the figures look very similar. Government debt will rise from about 60% of GDP in 2007 to 100% of GDP by 2011.

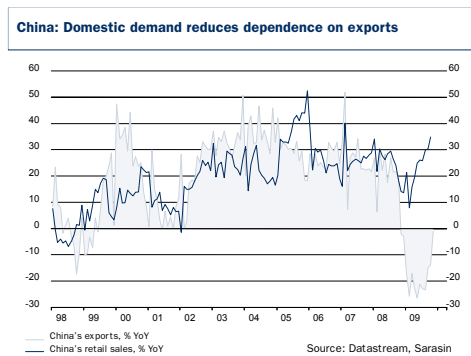
Risk of national bankruptcies: Growth is the solution

Meanwhile, Japan's debts threaten to break the sound barrier at 200% of GDP. Inevitably, this sparks fears that an OECD country will become insolvent in the coming years. Consequently, many observers are calling on finance ministers to raise taxes. However, tax hikes would poison the economy. Japan's example shows that the tentative steps taken after the real estate bubble burst ended in a deflationary spiral, from which there appears to be no escape. Although the Japanese authorities also chose the route of zero interest rates, quantitative monetary easing, an expansive fiscal policy and bank restructuring, it is clear in retrospect that they acted too late and much too slowly. Although Japan pays extremely low rates on its national debt, the mountain of debt continues to grow in real terms due to deflation. The lesson learnt from the Japanese example is that only growth can reverse deflation and lower the debt level. Growth also increases tax revenues and thus reduces the budget deficit. Selective savings with measures that have low multiplier effects are also helpful; however, tax hikes would be counterproductive because they would dampen growth afresh. Governments in the OECD countries would be well advised not to introduce austerity measures. As soon as the recovery turns into a sustained development, the theme of national insolvency will no longer be an

issue. However, governments will need to prepare themselves to meet the next crisis by making plans to consolidate their national budgets in the medium term. As a consequence, consolidation will be another structural headwind in the next decade.

Return to a global trade balance acts as a brake...

Growth drivers capable of reducing the debt-to-GDP ratios will differ from those of the past decade. Optimistic consumers in economies with laxer lending standards and rising real estate prices were largely responsible for the rise in global trade

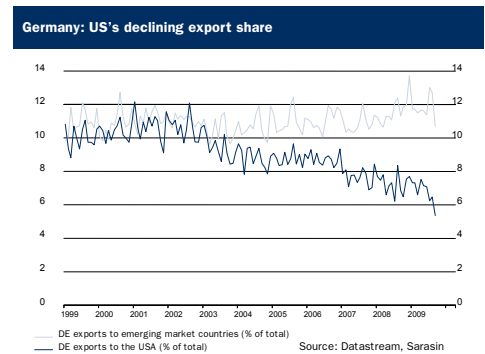


imbalances. At the peak in 2007, the US consumed 7% more goods than it produced. As savings ratios rise, consumer demand will tend to dampen global economic development. The realignment of the US economy from domestic demand toward foreign demand will be a painful process not only for the US. Given that the US is the world's biggest importer, export-dependent economies will have to find new export markets to drive their growth, or boost domestic demand.

...and offers an opportunity: Hope rests with the emerging market countries

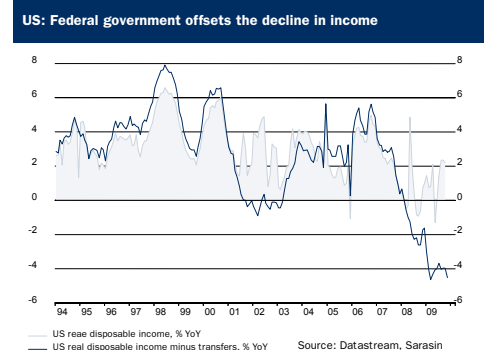
But this also spells an opportunity for the global economy. The need to stimulate domestic growth momentum in regions where consumption has hitherto suffered

from a high savings ratio may have a liberating effect. China has shown the world how a country can change from dependence on exports to domestic demand. While Chinese exports were declining by about 25% until mid-2009, retail sales rose by 20% and investments by as much as 30%. China also recorded a strong growth rate of 8% in 2009, a year dogged by catastrophes, making it one of the few economies to post positive growth rates in 2009. The measures introduced by the Chinese government in the



Macroeconomic forecasts

	(as %)	2008	2009	2010	2011
World	GDP (YoY)	3.2	-0.8	4.0	3.0
US	GDP (YoY)	0.4	-2.4	2.4	1.5
	Unemployment rate	5.8	9.2	9.9	10.2
	Inflation (CPI)	3.8	-0.4	1.1	1.1
Euroland	GDP (YoY)	0.5	-3.8	2.4	1.2
	Unemployment rate	7.6	9.4	9.8	9.7
	Inflation (CPI)	3.3	0.5	0.8	0.7
Japan	GDP (YoY)	-0.7	-5.1	2.6	0.5
	Unemployment rate	4.0	5.1	6.0	5.0
	Inflation (CPI)	1.4	-0.9	-0.5	-0.3
Switzerland	GDP (YoY)	1.8	-1.4	1.9	0.9
	Unemployment rate	2.6	3.8	4.9	5.0
	Inflation (CPI)	2.4	-0.4	0.6	1.0
China	GDP (YoY)	9.1	8.0	9.6	7.0
	Inflation (CPI)	5.9	-0.9	2.5	1.5



pension and healthcare systems should strengthen the consumption rate in the long term. Also in terms of investments, infrastructure programmes are expected to stimulate growth in 2010, which will benefit not only Chinese companies but other regions as well. Thus, the hitherto huge export surplus will melt away and sooner or later will stimulate demand in the global economy to a significant extent. The structure of German exports already shows that the US share is decreasing more and more, while the emerging market share is growing.

Fiscal policy stimulus, a reduction of excesses to 2011

But even without additional impetus from the emerging markets, we believe the slowdown in growth expected before the end of 2010 will be cushioned by fresh fiscal stimulus. G20 governments have little choice. Given the danger of a deflationary spiral and the need in the medium term to reduce the towering mountains of debt with growth, they will stimulate growth for as long as it takes a new upswing to appear. If they do not manage to achieve this in 2010, it will be too late in 2011. Governments are already expending considerable efforts to keep disposable income constant in order to lay the foundation for an upswing. The chart above shows how the massive increase in unemployment in the US has lowered disposable income without transfers. If, however, we include transfers, even income shows an increase. In Germany, unemployment (excluding measures for short-time work) is about 3.5 percentage points higher. This has given both disposable income and consumer sentiment a big boost. These measures, coupled with infrastructure programmes in the US and the emerging market countries, should help to stabilise end demand by the end of 2010. In addition to this, some of the past excesses will

also have been reduced. If banks are recapitalised by then and finished goods inventories extensively reduced, we believe there is a good chance that the upswing in 2011 can be sustained.

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