Political and economic trends are transforming the Middle East into a mainstream destination for international investors. In the Gulf, the stock markets of the United Arab Emirates and Qatar attracted billions of dollars of fresh foreign money this year as they were upgraded to emerging market status by equity index compilers, while Saudi Arabia announced it would open its $550 billion bourse to direct foreign investment early next year.

Returning political and financial stability in Egypt, after the turmoil of the Arab Spring, and economic reforms in Morocco may clear the way for strong growth in the next few years. As soon as this year, a diplomatic agreement on Iran’s disputed nuclear program could allow the country of 80 million people to begin rejoining the global trading system.

These issues and others were discussed at the annual Reuters Middle East Investment Summit, where Reuters journalists interviewed some of the region’s top policy-makers and executives in cities including Abu Dhabi, Cairo, Doha, Dubai, Rabat and Riyadh, producing exclusive stories and investable insights.
As oil price slides, Gulf’s private business may benefit

BY ANDREW TORCHIA
DUBAI, OCTOBER 26, 2014

Kuwait’s privately owned Jazeera Airways is preparing to bid for a big stake in state-run flag carrier Kuwait Airways, Jazeera’s chairman told Reuters. If the deal goes through, it will be a sign that the business scene is changing in the Gulf.

For several decades, Gulf Arab economies have been dominated by the heavy hand of the state. Governments’ huge oil revenues have eclipsed private sector activity. Benefiting from these revenues, state-owned firms have prospered while many private companies have struggled to raise financing and become ensnared in official red tape.

But pressures are growing for a new model. North Africa’s Arab Spring uprisings of 2011, fuelled by high unemployment, underlined to Gulf governments the need to create jobs for their citizens - and to enlist the private sector in that effort.

Meanwhile this year’s plunge of global oil prices, to below levels which some governments need to balance their budgets, has exposed the risks of relying entirely on oil for growth and revenues in the long term.

The result is a string of economic reforms and steps to open up financial markets that may create more opportunities for private firms - foreign as well as domestic - in coming years, company executives from around the Gulf told the Reuters Middle East Investment Summit.

The oil price slide is not causing panic in the Gulf but it is “getting people to think in the right direction”, said Tarek Sultan, chief executive of Kuwait-listed logistics giant Agility, which is majority privately owned.

Sultan noted that the region had a history of entrepreneurship - before the discovery of oil, economies were supported by small, flexible trading and transport businesses, many using the wooden sailing ships known as dhows.

“People have to think, how can we do without” the oil revenues that have sustained the region for the last few decades, he said.

REFORMS

Jazeera Airways may be a step towards that change. Set up in April 2004, it is one of a handful of privately owned airlines in the Gulf and now operates a fleet of 15 Airbus A320s.

Chairman Marwan Boodai told the Summit that his company was preparing to enter a bidding process for a 35 percent strategic stake in loss-making Kuwait Airways. Parliament originally approved the airline’s privatisation in 2008 but the project was delayed; it now appears to be moving ahead again.

“We believe in privatisation and think governments should focus on political administration, and not on managing airline companies or transportation or other firms,” Boodai said.

Executives at the Summit also cited a range of other efforts to stimulate private business across the Gulf, including partial deregulation of areas such as telecommunications and aviation in Saudi Arabia, and a drive by the United Arab Emirates to make
it easier for smaller companies to borrow money from banks.

These steps will not by themselves reduce governments’ economic dominance in the region, but there are signs that they are boosting private sector activity enough to at least partially offset a slowdown in the region’s oil industries.

For example, Saudi Arabia’s economic growth in the second quarter of 2014 fell to an annual 3.8 percent, the lowest rate in a year, because of a slowing oil sector. But growth in the non-oil private sector accelerated to 4.7 percent.

One of the biggest shifts in the Saudi economy for years is due to labour reforms, which are using quotas and fees to push hundreds of thousands of foreign workers out of the country and replace them with Saudi citizens.

The reforms have been criticised for raising companies’ costs, disrupting industries such as construction, and putting unqualified, unproductive employees into some posts. Some firms have been hiring Saudis for the sole purpose of meeting quotas.

But the reforms are clearly having some success in pulling Saudis into the private sector. The number of local citizens working at private firms jumped to 1.5 million by the end of 2013 from 681,481 in 2009, according to labour ministry data.

Muhammad al-Agil, chairman of Saudi retailer Jarir Marketing, said this trend was lifting Saudis’ disposable incomes and spending. Partly as a result, Jarir plans to invest 1.1 billion riyals ($293 million) over five years to roughly double the number of its stores in Saudi Arabia and the Gulf.

“We are not employing Saudis only because of the rules but because we think it is good for business,” Agil told the Summit.

Oman is taking a different tack in trying to diversify its economy beyond oil. It wants to develop its Sohar Port and Freezone, on its coast about 200 kilometres (125 miles) to the southeast of Dubai, into a gateway for imports to the Gulf.

The company launched an industrial zone at the port in 2010, offering tax and other incentives to attract private companies’ logistics and manufacturing operations.

Current operations include auto parts storage and distribution, and a chrome smelter; British-based Tri-Star Resources plans to build a $60 million plant supplying about 12 percent of current global production of antimony, Edwin Lammers, Sohar’s executive commercial manager, told the Summit.

MARKETS

In the long run, the most far-reaching boost to private sectors in the Gulf may come from the expansion of stock markets and efforts to draw more foreign investors into them.

Governments want foreign participation in local markets not because they need the money, but because they think activist foreign funds will help to impose market discipline on listed companies and promote international management practices.

In May, the UAE and Qatari stock markets won upgrades to emerging market status in the classification of international index compiler MSCI. In July, Saudi Arabia announced it would open its bourse to direct foreign investment in early 2015.

“The upgrade to emerging market status has been an important marker,” said Hai-them Katerji, chief investment officer at Al Rayan Investment, a subsidiary of Masraf Al Rayan, Qatar’s largest Islamic bank by market value.

“The expected opening of Saudi Arabia will be even more significant given the size of the Saudi economy and stock market. In the coming years the region is likely to become a more mainstream investment destination for global investors.”

After several years of inactivity in the wake of the global financial crisis, most of the governments of the six-nation Gulf Cooperation Council are now promoting public offers of shares in state-linked companies, billing the sales as a way to share the country’s corporate wealth with their citizens.

Kuwait’s sovereign wealth fund announced last week that it would resume selling stakes in local companies to the public, planning to offer its majority stake in Kuwait Investment Co in the first half of 2015.

Saudi Arabia’s state-owned National Commercial Bank IPO-NACO.SE is in the process of conducting a $6 billion IPO, the largest ever launched in the Arab world.

“The reopening of the IPO market in the region will attract more interest to our markets and encourage other companies to go public,” said Katerji. “This will help private equity and M&A activity in our markets as IPOs.”

Yasir al-Rumayyan, chief executive of the investment banking arm of Banque Saudi Fransi, Saudi Arabia’s fourth-largest listed lender, said Saudi companies were becoming more interested in listing with the encouragement of regulators.

“We have an excellent deals pipeline... We think we will see one IPO every quarter from Saudi Fransi Capital for the coming five quarters,” he told the Summit.

Additional reporting by Ahmed Hagagy in Kuwait, Azza Al Arabi in Dubai, Amena Bakr in Doha and Marwa Rashad in Riyadh; Editing by Olzhas Auyezov
From mega-projects to tax reforms, Egyptian ministers presented detailed initiatives last week to revive an economy battered by three years of upheaval and decades of neglect. Quizzed about Egypt’s political challenges, however, they had less to say.

With cameras rolling, eight Egyptian ministers opened their doors to journalists for the Reuters Middle East Investment Summit last week; that accessibility was itself a change from past decades when contact was limited and officials were aloof.

Previous administrations made big promises on the economy but rarely delivered, critics say. Discontent with their apparent detachment helped trigger a revolt in 2011 that toppled officer-turned-president Hosni Mubarak after 30 years in power.

Marking themselves out from predecessors, the ministers spoke with candour about the enormity of the challenges facing Egypt and in detail about solutions. They have already implemented subsidy cuts and tax reforms that previous governments shied away from for fear of fuelling discontent.

Those moves helped persuade Moody’s to change Egypt’s outlook from negative to stable this month, but beyond vows to hold long-awaited parliamentary polls and restore stability, talk of political reforms was general at best.

Asked how Egypt could hope to lure back investors without implementing political reforms, Telecoms Minister Atef Helmy said: “Trust us as Egyptians; we really look for peace. We look for stability. We look for the welfare of our citizens... but we need people to know their boundaries... There is a big difference between freedom and terrorism.”

The stakes are high in Egypt, where militants have stepped up attacks on police and soldiers in the Sinai Peninsula since former army chief Abdel Fattah al-Sisi ousted elected president Mohamed Mursi of the Muslim Brotherhood more than a year ago.

A day after Finance Minister Hany Kadry Dimian told Reuters about his plans for tax reforms and debt reduction, at least 33 security personnel were killed in some of the worst anti-state violence since Mursi’s removal.

Egypt moved swiftly to declare a temporary state of emergency in northern Sinai and extended military trials to civilians who attack state facilities or block roads, raising fears of a return to authoritarianism.

Sisi, who won a presidential election in May, has already cracked down on the Brotherhood. Thousands of its members have been detained, many sentenced to death in mass trials that have drawn criticism from Western governments and rights groups.

Despite the recent turbulence, multinationals have largely remained in Egypt, which continues to offer relative calm in a region consumed by conflict in Libya, Iraq, Syria and elsewhere.

Many Egyptians have tolerated what critics describe as widespread human rights abuses, hoping that Sisi would stabilise Egypt after the turmoil that followed Mubarak’s fall. But how long their patience will last is an open question.

“While investor confidence has improved thanks to the relative stability
brought about by the Sisi presidency, ongoing political polarisation, insecurity and structural economic challenges complicate investor decision-making,” political risk analysts Maplecorfit said in a recent report on Egypt.

Asked about a new draft law regulating non-governmental organisations (NGOs) that human rights groups fear will restrict their activities and funding, Social Solidarity Minister Ghada Wali gave no details on its contents.

She promised the draft would be circulated before going to parliament but in the meantime has insisted groups register under an unpopular Mubarak-era law, raising fears that those working on advocacy or human rights would face persecution.

Parliamentary elections are the final step in the roadmap set out by Sisi after Mursi’s ouster, but without a date set they could miss the plan’s self-imposed deadline. They were due to take place within six months of the presidential vote in May.

During a visit to Cairo on Monday, U.S. Treasury Secretary Jacob Lew welcomed what he described as Egypt’s “strong initial steps” toward economic reform but urged more political openness.

“We discussed the rule of law and how creating an open political environment in which individual rights are fully respected would further bolster Egypt’s ability to attract international investment,” Lew told reporters in Cairo.

MILITARY’S ROLE

On the economy, Egyptians are closely watching Prime Minister Ibrahim Mehleb’s performance on employment and housing, issues that helped foment the anger behind the 2011 uprising.

Mehleb was realistic about how quickly problems that had built up over decades could be resolved, urging patience.

“In economics, we began to open all the files that were not opened. We don’t hide anything from the people,” he told Reuters.

“This is not a cosmetic operation or making something just look beautiful. We are fixing from the roots.”

But even among major infrastructure projects, some of which are set to be showcased to investors at an economic summit in February, the changes are not as deep-rooted as they appear.

Egypt’s military, which has long played a key role in the economy, is taking a leading role in a multi-billion dollar project to expand the Suez Canal.

A new company being created to upgrade Egypt’s telecoms and internet infrastructure will also involve military-owned firms, though Helmy said they would not dominate or control it.

Housing Minister Mustafa Madbouly, whose ministry is working to meet ballooning demand and find a solution to the country’s informal settlements, said the army could also run parallel development programmes.

When Arabtec Holding, Dubai’s largest listed construction firm, agreed to build one million houses in Egypt in a $40 billion project, it partnered directly with the army rather than the government.

“The military has its own economic and financial arms which also have the right to do this,” said Helmy.

The military, whose budget is shielded from public scrutiny, has a business empire ranging from automobiles to computers. Estimates of the size of its profit-making operations range from a few percent up to nearly half of the economy.

Some see the army as more efficient than the government, and ministers point out that it sub-contracts much of its work to private firms, but critics say it crowds out the private sector and hampers growth.

Asked what had really changed in Egypt, with the Brotherhood back underground after a brief taste of power and a former general back in the presidency, Investment Minister Ashraf Salman had a simple answer: “Egyptians”.

“The big change that’s coming this time is coming from Egyptians,” he said. “They will not accept anymore somebody to be like Mubarak to stay in power for 30 years. They will not accept anymore a minister like myself to stay on this seat for 20 years. They will never accept that.”

Additional reporting by Michael Georgy, Stephen Kalin, Maggie Fick and Shadi Bushra in Cairo; Editing by Emelia Sithole-Matarise
Egypt’s Beltone Financial aims to invest around 300 million Egyptian pounds (26.12 million pounds) to expand its domestic operations next year because it believes the worst of the country’s economic instability has passed, its chairman told Reuters.

“The entire world is open to us. I see that the transition period in Egypt has ended. The investment opportunities that exist domestically are the best that can be found in the region,” Aladdin Saba said.

“We will propose our expansion plan for 2015 to the board of directors. I envision us investing in the non-bank financial sector by setting up new firms, or by buying existing businesses if they would enable us to achieve our goal and save us time.”

The optimism of Saba, who founded Beltone in 2002, is echoed by many Egyptian financiers, who think the government is getting a grip on Egypt’s economic problems after a three-year slump following the revolution of 2011.

With over 200 staff, Beltone has brokerage, asset management, investment banking and private equity operations. Foreign operations include offices in Dubai and London.

Earnings have slumped since last year, when they were inflated by one-off gains such as a property sale. Consolidated net income tumbled 84 percent from a year earlier to 11.0 million Egyptian pounds in the first half of 2014; revenues sank 26 percent to 31.6 million pounds because of lower fee income.

But the company has been one of the most aggressive Egyptian financial firms in seeking to get ahead of the expected rise in asset values in the event of an economic recovery over the next several years.

It originally announced that it would distribute a dividend of 7 pounds per share for the 2013 financial year, but then suspended that decision as it sought with billionaire Naguib Sawiris to buy a 20 percent stake in Egyptian investment bank EFG Hermes for about $257 million.

The purchase did not go through as the bid consortium attracted offers of just under half of the EFG Hermes shares which it sought. However, that setback does not appear to have dimmed Beltone’s ambitions.

The company’s board decided this month not to distribute cash dividends and to use the company’s liquidity instead to fund its future expansion plans.

“The decision to distribute dividends for 2013 was made under certain circumstances that have changed entirely, and our policy too has changed,” Saba said in an interview at the Reuters Middle East Investment Summit.

“The first sign of change was the company heading towards acquiring a stake in Hermes. Therefore we decided, whereas our policy was to be conservative and distribute cash dividends, to look into expansion and investment opportunities.”

He added, “We have liquidity of 120 million pounds and this covers a portion of the expansion that we are working on. There may be a new stage of external funding for the remainder of our investments, either through a capital increase or through obtaining bank loans.”

IPOS

Authorities are working to revive listing activity on Egypt’s stock market, which should benefit firms such as Beltone.

Arabian Cement Co listed in Cairo in May after raising $110 million in its initial public offer, the first major one on the bourse for about three years; Egyptian Exchange chairman Mohamed Omran told Reuters this month that the exchange expected to approve 10 listings this year.

“We are working on four new primary offerings, but all of them will occur in 2015,” Saba said without naming the companies.

“We have an offering with a value above 1 billion pounds, and another with a value of around 750 million pounds. We can say that the aggregate value of the four offers will exceed 2 billion pounds.”

In April, the exchange granted Beltone the country’s first licence for exchange traded funds (ETFs), a step towards deepening trade in the stock market. Omran said he had expected ETF certificates to be offered earlier this year, and now believed they would be introduced by the end of 2014.

Asked when Beltone might proceed with ETFs, Saba said: “At the earliest. Beltone is not waiting for anything. There are still a few minor changes being made to the offering circular.”

Writing by Azza Al Arabi; Editing by Andrew Torchia
Major Saudi Arabian construction firm Abdullah Abdul Mohsin al-Khodari and Sons says it may double its capital spending in coming years to cope with the work it hopes to do on the country’s big infrastructure projects.

Saudi Arabia’s 855 billion riyal ($228 billion) state budget plan for 2014 slowed total spending growth to the lowest rate in a decade as the government became more fiscally cautious. But it still included funds to build 465 schools and 11 hospitals, and a 25 percent jump in spending on infrastructure such as roads, railways, ports and airports.

Although global oil prices have tumbled to four-year lows in the last few months, below levels which analysts believe the Saudi government needs to balance its budget, industry executives do not expect major cutbacks in spending.

The government has huge fiscal reserves which it can use if necessary to maintain spending, while it views many of the projects as vital to improve public welfare – thus ensuring social peace - and to diversify the economy beyond oil.

“Most of these projects will go into the tens of billions of riyals,” the construction firm’s chief executive Fawwaz al-Khodari said in an interview for the Reuters Middle East Investment Summit.

“The scope relevant to al-Khodari in each of these projects could easily reach 7 or 8 billion. I am not necessarily saying that is what al-Khodari would capture, but that’s the potential of any one project...”

“So when al-Khodari gets its share, it will have a substantial and material impact on financials, and ultimately a positive impact on the bottom line.”

Such projects will require raising annual capital expenditure above the levels of 150 to 250 million riyals seen in past years, Khodari said.

“From one project alone al-Khodari could double its capex – so the trend upwards in capex is a fair assumption.”

The company reported a 23 percent year-on-year rise in third-quarter net profit to 15 million riyals, as its contract backlog fell to 3.36 billion riyals as of Sept. 30 from 3.99 billion riyals a year earlier.

Khodari said Saudi government spending on projects was only likely to drop if oil prices slumped for at least two years.

“For the immediate future, I see no slowdown in the projects stream. However, should the oil price decline continue and not rebound for a couple of years, then I would expect a more conservative spending policy to be employed.”

The stock market appears to endorse Khodari’s expectations; the company’s shares are up 82 percent so far this year, outpacing an 18 percent rise by the main Saudi market index.

LABOUR REFORMS

As the employer of about 20,000 workers, al-Khodari has been acutely vulnerable to Saudi Arabia’s sweeping labour market reforms, which aim to limit the use of foreign workers and encourage the hiring of Saudi citizens by the private sector.

In 2011 the government imposed penalties on companies which failed to meet quotas for hiring Saudis, who tend to cost more to employ; a year later, it introduced...
a levy of 2,400 riyals per year for every foreigner which a company employed above the number of its Saudi workers.

In April this year Khodari told Reuters that his firm’s profit margins had been eroded by more than 50 percent under the reforms, with an average annual cost impact of 50 million riyals.

In his latest interview, however, Khodari said the impact had started to fade and that by the end of 2015 there would be very little effect on his company’s financials, as contracts negotiated before the reforms exited the revenue stream.

“The worst is behind us as far as the impact of the labour reforms goes. I am not saying they have stopped, as reforms continue to change and we get initiatives from time to time, but I think that the biggest shockwave...is fading.

“Quarter by quarter the impact is less and less. Once we get beyond the second half of 2015, we will have very little that is still dragging along with our remaining contract backlog.”

Khodari warned, however, that future labour market reforms or changes could still hit Saudi Arabia’s construction sector.

He was referring to demands for governments of some labour-exporting countries to set minimum wages for their workers in Saudi Arabia. Local media have reported the Indian government plans to introduce such a policy; by some estimates, about 2 million Indians work in Saudi Arabia.

“In cases where salaries have been 800 to 900 riyals, we are now hearing talk of 1,500 riyals as a minimum salary which is a huge increase...Clearly this would become a major issue in the contracting industry.”

In addition, the Saudi labour ministry has been proposing to reduce maximum weekly working hours for private sector firms to 40 from 48, and to expand the weekend to two days from one. Companies could end up hiring more people to meet deadlines or paying extra overtime, Khodari said.

“The impact is mostly going to be a financial cost - it could be 10 percent or it could be 25 to 30 percent on the manpower cost.”

Khodari said there were simply not enough Saudi citizens available in the labour market for construction firms to meet quotas, as many people did not have the necessary qualifications, skills and work ethic. Many Saudis were not willing to work in non-administrative jobs or at remote sites, he explained.

“I agree that when you are a 100-man company, you can hire five Saudis. But when you are a 20,000-man company like al-Khodari and you have 1,600 Saudis that you must hire, don’t I need to put at least 1,400 in the field? I cannot accommodate so many in the office.”

The end result is that some companies are hiring people just for the sake of meeting quotas, Khodari said, urging all parties concerned to work with construction companies on finding a solution.

“Otherwise, in my opinion, 10 years down the line we could potentially have 3 million people who appear to be employed but not really. Should there be a construction slowdown, they will be unemployed, have no skills and be dependent, and that will be the biggest social time bomb.”

Editing by Andrew Torchia
Investment bank Saudi Fransi Capital has three big initial public offers of shares in the pipeline as the Saudi Arabian equity market booms and firms become keener to list, the company’s chief executive said.

The kingdom’s $550 billion stock market, by far the largest in the Arab world, saw just five IPOs in 2013 worth a total of around $506 million, down in both volume and value from the previous year.

But volume and value are both set to rise this year as the securities regulator encourages listings of companies which it believes contribute to economic growth.

Although the main equity index has pulled back in the last two weeks because of sliding oil prices and concern about global economic growth, it is still up 16 percent year-to-date and up 45 percent since the end of 2012.

In a reform designed to increase the long-term efficiency of the Saudi economy and stimulate private sector growth, the Capital Market Authority announced in July that it would open the stock market to direct foreign investment in the first half of next year.

“We have an excellent deals pipeline... We think we will see one IPO every quarter from Saudi Fransi Capital for the coming five quarters,” Yasir al-Rumayyan said in an interview at the Reuters Middle East Investment Summit.

Each of the three big IPOs currently in Saudi Fransi’s pipeline is larger than 1 bil-
lion riyals ($267 million), Rumayyan said: Sulaiman Al-Habib Medical Group, one of the largest private providers of healthcare in the region; water and power project developer ACWA Power; and Petromin, a lubricants producer.

“I have a bigger list than this one... We have another IPO in the steel sector, and one in building materials,” said Rumayyan, whose company is an arm of Saudi Arabia’s fourth-largest listed lender, Banque Saudi Fransi.

Saudi Arabia’s National Commercial Bank is currently conducting a $6 billion IPO, the largest ever launched in the Arab world.

**ASSET MANAGEMENT**

The deepening of the Saudi stock market through IPOs and its opening to foreign investors are expected to support growth for asset managers in the kingdom.

“Our assets under management (AUM) is about 10 billion riyals, but this number is growing tremendously, as it was less than 5 billion in 2010,” Rumayyan said.

“We want to grow like 15 to 25 percent on an annual basis, and we think it is doable because we have been doing it in the past three or four years.”

Rumayyan said his company would open an office in Dubai to cater to international investors in the brokerage and asset management sectors. In the past, Saudi banks have rarely opened overseas offices, preferring to focus on their domestic market.

The opening of the Saudi stock market to foreign institutional investors will eventually bring between $30 billion and $60 billion of funds into the bourse, especially if the market is ultimately admitted to the MSCI emerging markets index, Rumayyan estimated. The fund inflows would spur trading volume and revenues at Saudi brokerages.

“If you look at the Saudi market currently, we are ranked number 15 worldwide in terms of the daily volume - definitely if we have the international investors coming in to the market, I think we will see a minimum 15 to 20 percent increase in daily volumes.”

Like other Saudi executives, he said the plunge of global oil prices to four-year lows in the past several weeks was unlikely to hurt the economy or markets in the long term, adding that the stock market had not been closely correlated with oil for the past eight or 10 years.

“If you want to look at the real economy, you have between three and five years of backlogs of projects today with government spending, so the money is there. So even if this drop continues, you have a good three to five years of continuous government projects.”

**DEBT MARKET**

Rumayyan also predicted strong growth for Saudi Arabia’s sukuk and conventional bond markets, arguing that central bank guidance to commercial banks on limiting their exposure to single clients would push borrowers to look beyond loans.

“That means those big corporations would have to tap the capital market, whether sukuk or bonds - this really is excellent news for financial advisors like us who are involved in the capital market,” he said, adding that Saudi Fransi was working on two debt issues. He did not give details.

Asked about the obstacles to developing Saudi Arabia’s debt market, Rumayyan said the problem was not on the regulators’ side but among the issuers, who tended to prefer bank financing as long as they could get better rates.

“The challenge now is to get good issuers to issue... Investors’ appetite here in Saudi is really big, and there are a lot of money market fund managers who are waiting for and anticipating debt issuance.”

He added, however, that international investors entering Saudi Arabia might not find local debt issues attractive at present, given their very low yields which are in some cases below even U.S. Treasuries.
Tunisia will raise the normal retirement age by two years in 2015 to reduce the deficit in its social security funds, as part of economic reforms designed to stabilize state finances, minister for economic affairs Nidhal Ouerfelli said.

The North African country is reorganizing its economy as it nears the completion of a difficult transition to democracy over three years after the 2011 revolution that ousted autocrat Zine El-Abidine Ben Ali. Parliamentary elections are to be held on Oct. 26 and a presidential ballot in November.

“Today, social funds suffer a large deficit and we are studying how to fix it effectively...We are going to raise the retirement age two years from 2015,” Ouerfelli said in an interview for the Reuters Middle East Investment Summit.

He said the retirement age would rise to 62, and that the reform was justified since Tunisia was one of the few countries in the region where the age was currently still 60. The reform is not certain to go ahead, since the new post-election government will reshuffle the cabinet and may have different priorities. Ouerfelli said the initial months of 2015 would be very hard for the new government as it tackled painful reforms to increase tax revenues and cut energy subsidies.

But he said the current government had prepared a clear reform strategy for coming years, which would help the next government. Politicians in key parties contesting the election, including the secular interests led by the Nida Tounes party and the Islamist Ennahda, have expressed support for economic reforms in principle.

Tunisia hopes to reduce its state budget deficit to 5.0 percent of gross domestic product in 2015 from 5.8 percent projected for 2014.
Lebanon is planning a $1 billion economic stimulus package for 2015 to maintain growth and support an economy which has been hit by a three-year conflict in neighboring Syria, the central bank governor said.

Riad Salameh said he hoped the fresh round of stimulus, which follows $800 million in aid this year, will result in economic growth of at least 2 percent next year. The IMF in May forecast Lebanon's economy to grow by 2 percent this year.

Speaking at the Reuters Middle East Investment Summit, he described Lebanon's financial situation as "solid", pointing to foreign reserves he said have reached a historic high of over $38 billion while gold reserves were at $13 billion.

"We cannot continue in this way if we want to revive the economy and create growth by financing development projects and infrastructure."

To fill next year's budget gap, Tunisia is again assembling a complex series of external financing plans.

"We will issue, probably in the first half of 2015, bonds worth $600 million," Ouerfelli said without giving details.

In addition, Tunisia aims to borrow about $450 million from the IMF next year, $800 million from the World Bank, $380 million from the European Union and $200 million from the African Development Bank.

 editing by Andrew Torchia
from Syria’s civil war, in addition to political instability, which has scared off wealthy Gulf Arab tourists and some investors.

“Today the central bank has foreign liquidity that exceeds $38 billion which historically (is) the highest, excluding the gold reserves,” he said.

“We are launching these incentive programs while keeping an eye that the liquidity we are injecting is not creating inflation or creating a drain on our foreign currency reserves.”

Salameh said the overall aim of the bank was to maintain the stability of interest rates and the Lebanese pound LBP=, which is pegged near 1,507.5 to the dollar.

REFUGEES CONCERN

Lebanon, which hosts around 1.5 million Syrian refugees, has also seen violence spill over from Syria with bombnings in Beirut, fighting in the northern city of Tripoli, and rocket attacks on Bekaa Valley towns close to the frontier.

Apart from adding to the strain on electricity and water supplies, the Lebanese resent Syrians for taking jobs, driving down wages and overloading schools and hospitals.

Lebanese officials have repeatedly voiced concern that the growing number of refugees, estimated at a third of the Lebanese population of 4 million, threatens Lebanon’s economy and political stability and said the country needed more resources to address their needs.

Finance minister Ali Hassan Khalil told Reuters on Wednesday that the country was getting little international help ease the impact of the refugees.

Salameh, who has headed the central bank for more than 20 years echoed those sentiments. He said the international community was not doing enough to help, adding that a trust fund created by the World Bank this year to help Lebanon has received only $30 million so far.

“Truly, it’s unfair that a small country like Lebanon has to pay the related costs which the World Bank has estimated, just on the direct cost to the government, (to be) around a billion dollars a year,” he said.

“We hope that the IMF will look again into the numbers and will work with the World Bank to activate donations to Lebanon.”

Editing by Emelia Sithole-Matarise
Iran nuclear deal would open last big frontier stock market

BY ANDREW TORCHIA
DUBAI, OCTOBER 15, 2014

Years of economic sanctions and isolation have ravaged Iran’s economy but created one of the last unexploited opportunities for international portfolio investors, who could start moving their money in this year if geopolitics permit.

The Tehran Stock Exchange is “the last, large untapped emerging market in the world”, said Ramin Rabii, managing director of Turquoise Partners, a Tehran-based investment firm with around $200 million of assets under management.

Talks between Iran and world powers in Vienna this week aim to reach a deal on Tehran’s disputed nuclear program. Iranian President Hassan Rouhani said on Monday agreement was “certain”, though not necessarily before a self-imposed Nov. 24 deadline.

A deal would pave the way for the West to lift sanctions that have largely frozen Iran out of the global banking system, deterring the vast majority of foreign investors.

Those investors are expected to pour billions of dollars into Iran’s economy in the event of a nuclear deal, but negotiating contracts and obtaining licenses for business ventures and factories could take many months.

So the fastest way to gain exposure to the Iranian economy may be the stock market - a prospect for which many foreign funds have started to prepare.

“From 2011 to 2013, we used to get one email of interest from potential investors every two to three months,” Rabii, whose firm is one of the main channels for foreign portfolio investment in Iran, said in a telephone interview at the Reuters Middle East Investment Summit.

“Now we are getting a few dozen emails every month and more important than that, serious investors have come and visited us. Turquoise has hosted more than 65 investors since January this year in Tehran.”

RISKS
Investing in Iran will remain a risky business for years to come. Even if a nuclear deal is reached, Rouhani will have to grapple with hardline political rivals as he tries to push through sensitive social and economic reforms.

After shrinking in the past two years, the economy has resumed growing slowly, and inflation has come down near 20 percent from over 40 percent last year. But the scars of sanctions include high unemployment and poor infrastructure.

The government’s presence is felt in almost every area of the economy, from regulation of prices to restrictions on exports - partly the result of the “resistance economy” which Iran established to withstand the sanctions.

“Foreign investors may see government interference in the economy as the biggest risk in the market,” Rabii said.

But the flip side of those issues is that the market, which has a capitalization of about $120 billion at the official rial exchange rate, roughly the same as Dubai’s, is by some measures one of the most attractively valued in the world.

The market’s main index soared 136 percent in local currency terms last year, partly because the election of Rouhani fanned hopes for a nuclear deal. It is down 18 percent year-to-date as authorities tighten monetary policy to curb inflation.

Rabii estimated the market was now trading at about 5-1/2 times this year’s...
projected earnings - well below about 11 times for MSCI's frontier market index - and carried a dividend yield of around 15 percent, roughly three times most markets.

Potential headaches for foreign investors in the market include red tape, the lack of international custodian banks, and low liquidity, which can make it hard to get into and out of stocks, Rabii said; collecting dividends can be difficult.

But he noted that the market had become more sophisticated over the past 10 years, despite sanctions. Fifteen years ago, for example, corporate earnings were announced on pieces of paper pinned to a wall of the exchange; now they're distributed via a centralized online system.

While most of the big listed companies are still controlled by state-linked institutions such as pension and social security funds and various foundations, private investors have started to make their voices heard, Rabii said - managers can face tough questioning by shareholders at annual general meetings.

In fact, the transfer of more of Iran's corporate wealth into private hands may be one of the most lucrative trends for the stock market in the next few years.

Iran revived its privatization program in 2006 and over 15 of the 30 biggest firms on the exchange have listed since then. But the financial power of state-linked bodies meant they were able to buy up most of the shares on offer, leaving the free floats of top firms very small at around 5 to 10 percent.

Financial pressures on government-related bodies have now increased and the Rouhani administration has said it wants the private sector to play a bigger role in the economy.

As foreign investors enter Iran in coming years, there may be a “second wave of privatization” as state-linked funds facing liquidity pressure sell large stakes in major companies to private investors, Rabii said.

“If there’s a buyer for such stakes, I am certain to find a seller.”

**CHANNELS**

The experience of other markets suggests fresh flows of foreign money into Iran's bourse could eventually total tens of billions of dollars. Foreigners own 20 or 30 percent of some emerging markets; Rabii estimated they now held less than 0.5 percent of Iranian stocks.

It is likely to take years to close this gap, however. Even if a nuclear deal is reached next month, banking ties with the outside world will take months to be re-established, and many banks and investors will be very cautious at first.

“Even if sanctions are lifted tomorrow, I don’t think we can look for a flood of money into Iran tomorrow,” Rabii said, suggesting a few hundred million dollars of foreign money might enter in the first 12 months.

Large inflows of funds might take two years to appear, as big international banks rebuild ties with Iran.

Turquoise, founded in 2005, says it has about $70 million of foreign money and $130 million of local funds under management. It started as asset management company and has expanded into the brokerage business and private equity, increasing its group-wide staff to over 70 people.

Soon after Turquoise was established, Mahmoud Ahmadinejad was elected as president of Iran and inflows of foreign money began to dry up, so the company was forced to focus on domestic investors. A plunge of the rial against the U.S. dollar in 2012 - it lost two-thirds of its value over 18 months - put severe pressure on Turquoise.

Rabii, 35, was born and grew up in Iran; his family moved to Canada when he was a teenager. He studied at a boarding school in Switzerland and at SOAS, University of London.

After working briefly as a consultant in London, he moved to Tehran and chose a career there partly, he says, out of patriotism, partly out of a sense of Iran’s potential, and partly because of the chance to create something new.

“We have continued to hope for an upturn - and when the market opens up, it will be the largest opening up of a market in recent times. This has kept us going.”

Reporting by Andrew Torchia; Editing by Olzhas Auyezov
Sohar port challenges Gulf rivals as Oman pushes beyond oil

BY ANDREW TORCHIA
DUBAI, OCTOBER 16, 2014

A n advertisement by the highway outside Dubai’s massive Jebel Ali Port tells firms they don’t need to ship goods through the Strait of Hormuz, the traditional gateway to the Gulf. Instead they can have goods delivered to a port in Oman, outside the Gulf, and bring them into the region by road.

“Why go through the Strait when you can go straight to the Gulf,” the billboard reads, in a challenge to Jebel Ali, which has become one of the biggest ports in the world by handling many of the region’s imports via Hormuz.

The cheeky advertisement has been posted by Sohar Port and Freezone, an ambitious facility on Oman’s northern coast about 200 kilometres (125 miles) to the southeast of Dubai.

Sohar is starting to compete for traffic with Jebel Ali and other top ports inside the Gulf, as part of a far-reaching plan by Oman to diversify its economy beyond oil. Its plan says a lot about how business in the region may develop in coming years.

Edwin Lammers, Sohar’s executive commercial manager, said the port’s intention to handle cargo for the Gulf region, not just Oman, was a key part of the country’s drive to industrialise.

“It brings down supply chain costs for Oman,” he said in a telephone interview at the Reuters Middle East Investment Summit. “Once you have the additional capacity, new shipping lines come in, feeder lines operate and costs fall due to economies of scale.”

OIL RESERVES

Oman faces, in a more immediate and acute form, the dilemma which all the wealthy Gulf oil exporters will face in coming decades: what to do when the oil runs out?

While Saudi Arabia, the United Arab Emirates and Qatar have ample reserves to continue production of oil and gas for decades, Oman’s reserves are much smaller, so crunch time for it is likely to come sooner. Estimates by multinational energy company BP have suggested Oman’s oil reserves could run out around 2030 at current production rates.

So the government of ruler Sultan Qaboos, 73, is pouring billions of dollars into efforts to make the arid country of about 4 million people into a logistics and industrial hub.

Among big industrial and infrastructure projects planned or underway are a $3.6 billion plastics production complex to be built in the city of Sohar, a $400 million steel plant in the southern port city of Salalah, a string of new or expanded airports, and a $15 billion plan to build a 2,244 kilometre rail network, the country’s first.

Sohar port will handle many of the imports Oman needs for its industrialisation and exports which it hopes to produce. The Omani government and the Port of Rotterdam set up a 50:50 joint venture to run the port in 2002.

This year Sohar completed a $130 million relocation and expansion of its container terminal, which is operated by Hong Kong’s Hutchison Whampoa. The project raised annual capacity to 1.5 million twenty-foot equivalent units from 800,000 TEUs, and allowed the port to handle large container ships of 10,000 TEUs for the first time.

Sohar plans to increase its container capacity further to 4 million TEUs in 2017 at a cost of between 60 and 70 million rials ($155-180 million), which is likely to be raised through bank financing.

“One that’s in place, you really start to compete with other ports in the region,” said Lammers, a Dutch veteran of the container port and stevedoring industries who joined the company in 2009.

The company launched a free zone in 2010 with tax and other incentives to attract companies’ logistics and manufacturing operations. Current operations include auto parts storage and distribution, and a chrome smelter; British-based Tri-Star Resources has said it plans to build a $60 million plant supplying about 12 percent of current global production of antimony, a metallic substance used in many alloys.

After a cyclone in 2007 disrupted Oman’s food supplies, the government wants to stockpile food reserves at Sohar; grain silos will be established there next year. Oman’s first sugar refinery will also be built at the port, with an eventual annual capacity of 1 million tonnes of sugar.

The entire Gulf depends heavily on food imports so Sohar hopes it can ultimately serve as a food reserve storage centre for the region, not just Oman, Lammers said.

RISKS

Oman’s strategy carries risks. One is re-
Regional overcapacity. Deep-pocketed Dubai, Abu Dhabi, Qatar and Kuwait all plan to expand their port capacity to seek regional business; a project underway at Jebel Ali will add 4 million TEUs, bringing total capacity to 19 million TEUs in 2015.

Container traffic at Sohar has not been growing rapidly in recent months - it totalled 103,023 TEUs in the first half of this year, down from 110,453 a year earlier. Sohar’s plans are based on the assumption that rapid economic and population growth will continue around the region in coming years.

About 300,000 TEUs of annual container business was transferred to Sohar in the second half of this year when all of Muscat’s commercial traffic was relocated to Sohar.

“When you have plans for 20 million TEU capacity in both Dubai and Abu Dhabi, one can start to talk of the possibility of overkill,” said Lammers.

But he added: “They all fulfill their own role in the regional supply chain. With the economy in the region growing at 6 percent, it’s something they need to do.”

And Sohar has some cards up its sleeve. As long as geopolitical tensions persist in the Gulf, the port’s location outside the Strait of Hormuz has a potential security advantage. Iran has threatened in past years to close the narrow Strait, but would find it harder to project its naval power across the Gulf of Oman.

The future Omani rail system, which is to be connected to a planned railway network across the six Gulf Cooperation Council countries, may give a big boost to Sohar, helping it to handle larger amounts of heavy imports for the GCC such as automobiles and steel products.

The design contract for the Omani railway is expected to be awarded by the end of this year and Sohar should be connected to the system three years after that, Lammers said.

The GCC rail network “will have a game-changing effect on logistics in the region”, he said.

Just as the Port of Rotterdam became a gateway to Europe, serving the European hinterland, “we expect something similar to happen in Sohar.”

Reporting by Andrew Torchia; Editing by Olzhas Auyezov
Investcorp wants 30 percent rise in assets under management

BY DAVID FRENCH
DUBAI, OCTOBER 23, 2014

Investcorp is targeting a more than 30 percent hike in its assets under management (AUMs) in the next five years as Middle Eastern investors increasingly see private equity as a way to diversify out of traditional investment routes.

Those in the region with money to invest have historically placed it in real estate and the stock market, meaning that the region represents a tiny fraction of global private equity assets despite its affluence.

However, the increasing sophistication of Middle Eastern investors means they are beginning to allocate more of their cash to private equity, which is a boon for firms in the region, according to Mohammed al-Shroogi, president of Gulf business at alternative investment firm Investcorp.

“The two pipes of real estate and equity are almost full so you need to create a third pipe, which is private equity,” Shroogi told the Reuters Middle East Investment Summit.

“The third pipe isn’t going to be filled but there is a huge room for the liquidity to transfer and diversify away from these other two investment opportunities in the Gulf.”

Founded in 1982, making it one of the oldest Middle Eastern private equity houses, Investcorp is best known in the global space for listing luxury goods brands such as Gucci and Tiffany & Co. (TIF.N).

With $11.4 billion of AUMs as of June 30 this year, it is aiming to raise this to $15 billion in the next five years, although Shroogi admits the figure is conservative.

But the era of being known only as a luxury brands investor has passed for Investcorp, despite being heavily linked with two such names in the past 12 months.

“(Roberto) Cavalli approached us but we didn’t look at the deal, but Versace we did,” Shroogi said, adding it walked away from the Versace deal as Investcorp thought it was too expensive.

“Once in a while you’ll find a brand name that you’ll look at and if that brand name is an opportunity then we will bring that opportunity.”

DEAL FLOW

Investcorp targets deals in the mid-market space of around $200 million to $300 million in the United States, Europe and the Middle East. After fully acquiring an asset, it sells between 85 and 90 percent to its clients.

It is currently looking to complete three private equity buys, one each in Europe, the United States and Turkey, Shroogi said, while the firm is also close to signing a real estate deal in the U.S.. He declined to elaborate on details.

So far this year, the firm has closed deals including Dutch printing products firm SPGPrints Group, which it was currently marketing to clients and which should close soon, and U.S. accessories brand Totes Isotoner Corp, which it bought with Freeman Spogli & Co.

Each investment the firm makes, it targets a return of three times its original outlay, Shroogi said, a figure it exceeded in its last exit when it sold Berlin Packaging to Oak Hill Capital for $1.43 billion, 3.5-times more than it bought it for.

Shroogi said it was considering exits from a number of its current investments.

One potential exit which had been cited in the media was for Gulf Cryo. Shroogi said while it was always holding talks with banks and other parties about possible deals, there were no imminent plans to sell the industrial and medical gases firm.

SUCCESSION

Shroogi will take up the role of co-chief executive officer in June 2015, along with current chief financial officer Rishi Kapoor, when current head Nemir Kirdar retires.

Kirdar helped found the firm 32 years ago so his departure is a landmark in the company’s history. It also highlights a key trend in business across the region - how do you successfully pass control from a patriarchal figurehead who has built up the firm to a new generation of leaders.

“The founder has built up a name for himself not only regionally but also globally, and he put the Investcorp name on the map,” Shroogi said of Kirdar.

“But this is a normal change and a healthy change. All his hard work and planning is being transferred to the new team, and Investcorp will succeed because it has the foundations.”

While the succession may not impact the firm, Investcorp and the private equity sector in general have changed significantly in the past five years as they deal with the fallout from the global financial crisis.

For Investcorp, it has substantially reduced the role of debt in its business, with its leverage ratio down from 3.7 times five years ago to around 1.2 times today, Shroogi said.

It also now keeps $1 billion of cash on its balance sheet so that it can pay off its outstanding debt if needed, which at the same time gives it the money to do deals if they materialize.

“When we see something, we can powerfully acquire that company because we have the liquidity in our hands.”

Editing by Keith Weir
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