

Islamic Business & Finance

THE AUTHORITATIVE VOICE OF ISLAMIC FINANCE

C P I
FINANCIAL

www.cpifinancial.net

NOVEMBER 2009 | ISSUE 47



A WINNING TEAM

Ahmed Bin Sulayem, Executive Chairman, Dubai Multi Commodities Centre Authority
Eric Meyer, Chairman and Chief Executive Officer, Shariah Capital, Inc.

PLUS:

DUBAI'S DEBT | THE UK'S SUKUK | RETAIL BANKING | ISLAMIC INDICES



A winning team

Dubai Shariah Asset Management was formed to create Shari'ah-compliant alternative investments. Robin Amlôt spoke to founding partners Ahmed Bin Sulayem, Executive Chairman of Dubai Multi Commodities Centre Authority, and Eric Meyer, Chairman and Chief Executive Officer of Shariah Capital

When the Dubai Multi Commodities Centre Authority (DMCCA) announced its partnership with Shariah Capital last year to build commodity-focused, Shari'ah-compliant alternative investments, there was no shortage of challenges. As their partnership, Dubai Shariah Asset Management (DSAM), overcame one obstacle after another - in the course of the worst global economic meltdown since the 1930s - few expected the extraordinary results of the DSAM Kauthar funds this year.

In fact, two of the DSAM Kauthar funds, the Gold Fund, up over 60 per cent year-to-date (YTD), and the Global Resources & Mining Fund, up over 50 per cent YTD, are the top performers this year in the Bloomberg Active Index for Islamic Funds, as well as in other worldwide rankings. The DSAM Kauthar Commodity Fund is claiming top billing over all commodity fund-of-funds with a return of over 30 per cent so far this year.

Did you have any idea your funds would do so well so quickly?

Bin Sulayem: Our objective was to identify the world's very best commodity managers and then convince them to manage a Shari'ah-compliant fund for

us. We knew that if we successfully enlisted experienced managers with sound investment strategies, they would deliver competitive performance over time. We did not expect that they would lead all Islamic funds this year with record gains.

Meyer: We constantly heard that Shari'ah guidelines would impede performance. We continually were told we would not be able to attract the very best team to manage a Shari'ah account. We believed otherwise. I think the performance of our DSAM Kauthar funds this year demonstrates convincingly that, in fact, Shari'ah does not negatively impact performance. Some of our investment managers actually feel that it helps performance. Shari'ah may be one of the reasons why our funds have done so well.

Don't forget that our managers have strong macroeconomic modelling along with a disciplined fundamental analysis process in each of their respective commodity industries. They make long-term price forecasts on underlying commodities and have strong relationships with company managements that enable them to develop earnings models. All of this contributes to their superior performance.

How do Shari'ah guidelines help performance?

Meyer: Let's dissect the portfolio structures of our funds. They have Shari'ah-compliant long and short positions in shares of companies, and cash. Nothing else. No options, no futures, no derivatives. Assets are ring-fenced where our Shari'ah scholars can look at every investment at any time. The success of the portfolio depends strictly upon the manager's ability to pick stocks. Shari'ah compels managers to focus on the basics of picking stocks. It eliminates the distractions of derivative instruments and brings managers back to the fundamentals. That focus only helps performance.

Bin Sulayem: The key to portfolio performance is disciplined research and stock selection. Shari'ah reinforces that mandate. All of our managers have a proven methodology for selecting stocks, an important criteria we looked for during our due diligence process. Our funds are successful because we've chosen managers who have a rigorous stock selection process.

You mention short positions. Most Islamic investors believe that shorting is forbidden.

Bin Sulayem: Yes, conventional short sales are forbidden. Our managers don't use conventional short sales, however. Working with Shari'ah scholars over a number of years, Eric and his team



developed an Arboon-based short sale alternative incorporated within customised prime broker documents. The Arboon has been approved by the OIC Fiqh Council and now is widely accepted by Islamic institutions throughout the world.

Meyer: We worked hand-in-hand with the Shari'ah scholars to perfect this solution. Their guidance on the Arboon was critical. The greater challenge for us was rewriting prime brokerage documents and establishing a framework of internal procedures at the prime broker for coordinating the Shari'ah process.

Absolute return funds, or hedge funds, have been in the news recently, not always in the most favourable light. What has been the market reaction to your Shari'ah-compliant hedge funds?

Meyer: After the global meltdown last year, investors understandably are anxious about allocating money to any new investments, including hedge funds. When they see our results, however, they look seriously at how our strategies can play a role in their overall portfolios.

Remember, our Shari'ah screening process requires a separately managed account at Barclays Capital, the prime broker. Investor funds are not co-mingled with other manager funds and never leave Barclays. To ensure Shari'ah compliance, Shaykh Yusuf Talal DeLorenzo, Shariah Capital's Chief Shariah Officer, reviews every trade. This level of transparency - required by our Shari'ah guidelines - enables us to identify prohibited trades before they even settle. It's an embedded layer of transparency you don't find in conventional accounts.

The Al Safi Trust platform was designed to enforce transparency, separate fund responsibilities, and avert conflicts of interest. We've engaged independent service providers like Walkers (trustee), Citco (administrator), PricewaterhouseCoopers (auditors) and Barclays Capital (prime broker and custodian) specifically for this purpose. No other alternative asset platform we know of offers comparable

levels of transparency and professional oversight to offset concerns investors may have about hedge funds.

Bin Sulayem: Although we are still building our track record, the market reception to our funds has been very positive. We currently are in active discussions with a number of institutions in the Gulf where our DSAM Kauthar funds would fit perfectly within their Islamic portfolio management strategies. When re-allocations begin later this year and early next year, we expect our funds to become part of these revised investment models.

How do conventional portfolio managers react to the idea of managing Shari'ah-compliant funds?

Meyer: Once they understand how we've streamlined the Shari'ah process with our screened universe and built an operational framework with Barclays

returns, and market a global client base truly diversified from their domestic institutional clients.

Tell me about DSAM and the winning team your firms have built together?

Bin Sulayem: DMCCA's directive is to undertake initiatives that establish Dubai as a global hub for commodities. An asset management effort, focused on commodity-centric investment strategies, is an integral part of that directive. DMCCA had always planned for an asset management capability and we are committed long term to growing this business.

Dubai is an acknowledged leader in Islamic finance, so the Shari'ah-compliant aspect of asset management was something we wanted to pursue actively. The opportunity to participate in the first Shari'ah-compliant hedge funds and fund-of-hedge funds was an innovation I wanted to support right

“ DUBAI HAS ALWAYS DEFIED ITS SKEPTICS. WE'VE ALWAYS BEEN ABLE TO MAKE ADJUSTMENTS, FIND WAYS TO INNOVATE, AND CONTINUE GROWING. I AM HIGHLY CONFIDENT THAT WE WILL MAKE IT THROUGH THIS PERIOD THE SAME WAY. ”

Capital, they are very enthusiastic. Hedge funds traditionally have relied upon money from endowments and pensions. That client base suffered serious losses in the real estate and equity markets last year. As a result, these clients are revising their allocations to all asset classes.

Bin Sulayem: As investors change, hedge funds must change as well. Hedge funds now understand the need to diversify their client bases. They need to develop new clients in new markets in order to continue growing their businesses. Our DSAM Kauthar funds are perfect examples of how qualified hedge funds can offer Islamic investors Shari'ah-compliant equivalents to their existing strategies, without sacrificing

from the start. As it turns out, the DSAM Kauthar funds are one of DMCCA's great success stories.

Meyer: Ahmed's asset management vision has been inspirational for DSAM. But it was his courage and leadership late last year, when DMCCA funded our managers in the midst of the global meltdown, that underscores our synergy and mutual respect. Having come through the challenges of that period together, our partnership is stronger and more committed than ever.

Your funds are the first on the Al Safi Trust platform. Why did you choose to lead this platform?

Meyer: The Al Safi Trust, the result of a strategic initiative between Barclays



Capital and Shariah Capital, was created with the goal of being the world's first institutional-quality Shari'ah-compliant alternative asset platform. It is a competitively-priced vehicle with top service providers that allows a manager the ability to offer a Shari'ah alternative to his conventional fund.

One of our DSAM managers spoke recently at a major investor conference in Bahrain. When asked how his DSAM fund fared against his conventional fund, he responded by saying that his DSAM fund performance was better. I am very proud that our platform has helped facilitate this manager's strong return.

Bin Sulayem: After analysing Al Safi, we quickly realised the platform offered DMCCA a solid framework on which to innovate and create new, world-class Shari'ah commodity offerings. We willingly seeded the first four managers on Al Safi and created Dubai Shariah Asset Management to distribute their funds. Our managers are happy with the platform's mechanics - and we are very happy with their returns! Our first-mover advantage with Al Safi, coupled with our managers' strong performance, should pay off significantly as we begin to raise assets.

Some have suggested that DSAM's performance is simply the result of investing when markets were low, that DSAM invested in commodity-linked companies when they were selling at deep discounts.

Bin Sulayem: One can only make that judgment once our performance record encompasses a complete investment cycle of 3-5 years. Regardless of market levels, successful portfolio management depends on managers picking the right stocks at the right time.

Meyer: Two of our managers recently completed road shows in the region. In every meeting, both argued convincingly that commodity-linked equities are only in the early stages of a prolonged bull market. Those who think the DSAM Kauthar funds' early returns are the result of market timing regret

that they did not invest earlier. Our response to them? Invest now; there are still much greater returns ahead.

Based on recent news, it appears as if Dubai World and its subsidiaries are now right-sized for the new economic environment. Will this restructuring allow you to shift into a growth mode? If so, what are your plans for 2010?

Bin Sulayem: Dubai has always defied its sceptics. We've always been able to make adjustments, find ways to innovate, and continue growing. I am highly confident that we will make it through this period the same way.

With the global recognition of our DSAM managers' performance, I believe DSAM is today a true jewel for DMCCA and Dubai World. DSAM embodies the product excellence that has come to define Dubai. Now established as a leader in Islamic hedge funds and Shari'ah-compliant alternative assets, DSAM intends to capitalise on its success by expanding its size and scope in 2010.

Meyer: 2009 was our year to prove that Shari'ah-compliant hedge funds can successfully compete at the highest levels with other Islamic funds - or conventional funds - anywhere in the world. 2010 will find us working closely with both Islamic and conventional institutions that want access to proven Shari'ah-compliant, commodity-focused investment products.

Mr. Bin Sulayem, you said before that you saw investor appetite returning. Where do you see your product addressing this appetite?

Bin Sulayem: Some exposure to commodities is practically a necessity these days, given the volatility of global markets. With a decline in currencies, especially the dollar, commodities are a perfect hedge.

Meyer: I see the historical overweighting of real estate as a thing of the past and a disciplined allocation across all asset classes, including commodities, as the wave of the future.

Are you marketing your funds directly to investors or are you willing to distribute your funds with the help of other institutions?

Meyer: We believe that a product like DSAM needs high-quality partners in every region of the globe. Strategic distributors are key. These partnerships might take the form of direct access to the DSAM Kauthar funds, private-labeling our funds, or other creative arrangements.

Bin Sulayem: We welcome collaboration with Islamic and conventional institutions with product initiatives directed to Islamic investors.

What growth prospects do you see for Islamic alternative investments?

Meyer: Oliver Wyman, the international management consulting firm, reported earlier this year that Islamic finance has grown over 30 per cent annually since 2000. By 2012, Wyman projects total Islamic assets will reach \$1.6 trillion (with revenues of \$120 billion), a near 150 per cent increase since 2007. Its report cites surveys that suggest one-half of the 1.4 billion Muslims worldwide would opt for Islamic products if given competitive alternatives. Doing the math: if alternative investments represent just 10 per cent of that Islamic market (well below the 15 per cent usually seen within institutional portfolios in the West), that's a \$160 billion market for Islamic alternative investments in just three years!

Bin Sulayem: Clearly, the market is growing exponentially. That's the reason DSAM is working with such urgency to bring superior-quality alternative commodity investment products to market. We believe demand for absolute return investments among Islamic investors is strong and growing. For its part, DSAM will continue to support best-of-breed Western managers who follow Shari'ah guidelines. Our team has a formula for success that works. We are committed to build on that momentum.