

The Shift in The Balance of Power: Issues and Implications

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Emerging Growth Poles: Challenges and Opportunities

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Luncheon Address

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FORUM 2012

THE BIG SHIFT

Traversing the Complexities of a New World

1 & 2 October 2012



AT THE WORLD'S CROSSROADS SHIFTING FROM NATIONAL TO GLOBAL

In many ways, the Khazanah Megatrends Forum 2012, themed "The Big Shift – Traversing the Complexities of the New World" provided a comprehensive overview of economic, political and social Big Shifts happening around the globe from a geographic perspective.

The rich and insightful discussions provided a wealth of viewpoints on how the forces that pervade the globe were increasingly borne out of the East, shifting away from the West.

In the closing address of the Khazanah Megatrends Forum, graciously delivered by the Honourable Prime Minister Dato' Sri Mohd Najib bin Tun Abdul Razak, an alternative hypothesis of what the Big Shift constitutes was proposed.

The Prime Minister postulated that perhaps another Big Shift

that was happening was not necessarily of a geographic nature, but of a scalable nature.

Dato' Sri Najib proposed that rather than a Big Shift from West to East or North to South, the Big Shift was actually from the national and divided to the global and interconnected.

As technology in all forms, particularly the rise of social media, bridged gaps between classes, countries and continents, it was only natural that whatever that was once thought of to be local was becoming increasingly global.

Yet, given Malaysia's position, not just in geographic terms, as the very crossroads of the world in many ways, the Shift from the national to the global will certainly expose the nation to strong winds. The Prime Minister gave clear examples of such strong winds, citing ripples from

global natural catastrophes, economic contagion and climate change. Against this backdrop however, the Prime Minister spoke with a tone of opportunity rather than one of pessimism.

Dato' Sri Najib stated that his administration was working as hard as it could to ensure that Malaysia would successfully navigate the strong winds that it would inevitably face.

A recent World Bank report stated that nations in Asia would need to rebalance their growth towards one that was more externally-dominated to one that was more domestic-driven, based on productivity and innovation.

Thus, he stated, the government launched a series of initiatives in the recent Budget 2013 to increase funding for research and development at both the commercial and academic level, strengthening the incentives

for the commercialisation of public research.

Cognisant of Malaysia's ever expanding presence in the global arena, the Prime Minister stated that it was key for the Budget to be both responsive to the needs of the people while remaining fiscally responsible simultaneously. A budget that failed to achieve either objective could potentially lead to a tremendous rocking of the Malaysian ship by the strong external and domestic winds.

The Prime Minister concluded his address with a note of inquiry, suggesting that all participants of KMF, singling out the youth in particular, ponder on this shift that Malaysia and perhaps all nations face in transitioning from the national to the global and whether it will prove to be the Biggest Shift of the century.

GROWTH AND INEQUALITIES

For inequality, empirically, there have been 2 key changes in recent years. Firstly, inequality between the East and West has been falling due to the rise of the middle class in the East and the decline of the middle class in the West. Second, there is greater inequality within the East itself, partly due to a rise in China's wealth that has resulted in job losses in other nations. >Page 3



LEADERSHIP AND COMPLEXITIES

A crucial element in good leadership is human governance which is an inside-out rather than outside-in approach. Human governance needs to be adaptable, resilient and positive. >Page 3



Thank you YAB Prime Minister for delivering the KMF 2012 Closing Address



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Balance of Economic Power is Shifting

- Growth in these recent years are mostly due to emerging economies. However, we still see a divided world economy and many policy dilemmas. In the west, policy is relatively poor and fragile; in Asia, it's mixed and has proven to be more resilient.
- What we see now has been seen before – a super-cycle and a period of economic growth. The key drivers to these are larger scale as countries branch out globally, growing domestic markets in Asia, new trade corridors (Asia-Africa, intra-Asian, Asia-LATAM) and greater interconnectivity both at the country and corporate level.
- There are 3 underlying structures to this shift in the balance of economic power – Positive: The shift will make the cake bigger for everyone; Negative: The inflation of debt globally; Neutral: More companies and economies are moving up the curve particularly across emerging economies.

The Balance of Non-Economic Power is also Shifting

- Financial: Financial power is a consequence of a shift in economic power. In the East, the state's role in finance is more evident through SWFs, government pension funds and government foreign reserves management.
- Military: The center of military activity is moving towards Asia with China's military spending expected to reach America's military spending by 2025.
- Policy/Political: This shift is not happening very quickly. Institutional organisations such as the G20 and the WTO have been ineffective. In the UN, the most important group – the P5 – is still mostly dominated by the West. The global policy forum has yet to adjust for the emergence of rising Asian giants.
- Soft: Asian nations do not really have that much power to attract and co-opt talent or to be trend leaders in the world just yet.

Social Shifts are also Occurring

- Environmental issues are being underestimated despite these issues putting significant stress on the world's food, water and energy resources, which have led to a rise in commodity prices.
- Demographic changes are also occurring with the most concerning trend being that the most rapidly growing group in the world are the old, prevalent in the West and picking up in the East.

The Shifting Growth Poles

- As the balance of global economic growth has shifted, the growth poles of the world that were previously predicted by international organisations are becoming weaker.
- Thus, the selection of countries as potential growth poles – based on size, openness, linkages with other economies – must also evolve.
- On the business end, trade and finance are also shifting. The flows of goods and services and of capital are shifting to emerging markets and will likely pick up momentum in years ahead. Cross-border M&A deals have also increased, thereby increasing the presence of emerging market corporates.
- There is an emergence of a multi-polar economy (sharing both economic and military power). The candidate countries to become growth poles in addition to current ones are China and Russia though Russia's economic power is relatively insignificant.

The Emergence of East Asia

- East Asia as a whole can also be an emerging growth pole as a region made up of several countries.
- There are 4 elements that support this vision which are shared experience, shared identity, shared economic models and self-interest that dictate close cooperation.
- Moreover, most Asian countries have strengths and weaknesses that are complementary of each other. Thus, there is a key incentive to collaborate and much to gain from close cooperation with one another.

Opportunities for East Asia as a Growth Pole

- The emergence of the East Asian growth pole is a realistic vision. However, towards this end, ASEAN+3 must focus on implementing 4 key initiatives.
- First, there is a need for an East Asia equity market which allows equities to be traded in the region which will increase risk-sharing among countries.
- Second, there is a need to ensure that the existing swap arrangements serving the countries of the region be improved.
- Third, there is a need to ensure a low probability of a paper economy (an economy of paper assets with very low links to the real sector of the economy)
- Fourth, there is a need to ensure that there is a level playing field between debt and equity as reliance on debt creating flows will cause vulnerabilities to remain.

Lack of Sustainability in Current Policy

- Despite the numerous pro-growth policies that are in place in many nations across the world such as fiscal stimulus packages, quantitative easing, LTROs, and generally low interest rates, the global economy has not undergone a sustained recovery from the global financial crisis.
- While the measures have managed to prevent the global economy and the various nations from slipping into a recession, they have not managed to return growth trajectories on to a sustainable path.
- Thus, nearly half a decade after the financial crisis, the global economy is still stuttering, if not suffering.

Factors in the Sluggish Recovery

- There are three key factors that have hampered the efforts of policymakers around the world from returning growth to a sustainable trajectory.
- The first factor is that of the weak underlying fundamentals in the global economy and global financial system. Currently, the economy is unwinding excess that has been built up over a long period of time and hence, a long unwinding period is required.
- The second factor is a lack of transformation in institutions, particularly policy making institutions, to evolve along with the global challenges. Existing institutions need to transform to adapt to the new environment to help their stakeholders move up the success ladder.
- The third factor is informational in the sense that there exist information asymmetries across the world which may prevent policymakers from having a thorough understanding of global economic and financial issues.

Guiding Policy Direction

- Over the course of the past 2 decades, Malaysia has embarked on some unorthodox type policies which have drawn criticism from the global arena. For example, Bank Negara employs very strong oversight for which it was criticised but it has paid off for Malaysia.
- Therefore, policies can no longer be benchmarked necessarily against global 'leaders' and thus, policymakers must have the ability to adapt and change where necessary.
- If unsure of optimal policy direction, the best thing to do remains to determine policy on a sound fundamental basis of ethics and integrity.

SPECIAL ADDRESS

The Shift in The Balance of Power: Issues and Implications

Speaker: Dr Gerard Lyons, Chief Economist and Group Head, Global Research, Standard Chartered Bank



SPECIAL ADDRESS

Emerging Growth Poles: Challenges and Opportunities

Speaker: Prof Dr Abbas Mirakhor, First Holder of INCEIF Chair of Islamic Finance



LUNCHEON ADDRESS

Speaker: YBhg Tan Sri Dato' Sri Dr Zeti Akhtar Aziz, Governor, Bank Negara Malaysia



SESSION 3

GROWTH AND INEQUALITIES

Empirical and Theoretical Views on Inequality

- For inequality, empirically, there have been 2 key changes in recent years. Firstly, inequality between the East and West has been falling due to the rise of the middle class in the East and the decline of the middle class in the West. Second, there is greater inequality within the East itself, partly due to a rise in China's wealth that has resulted in job losses in other nations.
- In the case of inequality, the notion of returns to labour is important. In Malaysia, productivity growth has outstripped wage growth. This problem is compounded by the fact that most of Malaysia's manufacturing is still low-skilled manufacturing.
- This then begs the question of whether there exists a tradeoff between inequality and growth, which is an ideological point. It is not inevitable to create vast polarisations of wealth in countries that seek to grow.
- What is needed to mitigate the tradeoff, if any, is a progressive income distribution policy, a vibrant middle class and equality of opportunity for all members of society.

Commoditisation Versus Differentiation

- A small nation that is a commodity producer in a market full of commodity producers is destined to be a price taker. Thus, if the nation is not producing something differentiated, it is destined to be poor, at least at a relative level.
- Countries need to differentiate themselves by adopting the right policies, and thus, governments must play a regulatory role without leaving the economy to be run solely by the markets. In addition, nations need to have the right education – not just in terms of higher expenditure on education, but a world class quality curriculum.

The Role of Values

- It is important to keep in mind that inclusive societies are better from an economic point of view, but not necessarily from a value perspective. Inclusiveness is therefore just one of many necessary solutions to mitigate inequality.
- Values must be taken into account in determining solutions – thus, value-corrupting activities must be addressed such as rent-seeking, non-meritocratic mobility and the creation of monopolies and oligopolies.
- There must be a shift in the economic way of thinking to incorporate values as the classical thinking of economics in the Adam Smith sense can be used to justify rent-seeking.



SESSION 4

LEADERSHIP AND COMPLEXITIES

Leadership as Taught by Islam

- Prophet Mohamed is seen as a leader for Muslims, with Jesus Christ seen as a leader for Christians. The key term of leadership for these leaders was "service" as servants of God.
- Islam teaches that leadership must also be about service to God and humankind, beyond simply serving customers with the best products and services.
- Towards this end, it is important for each aspiring leader to "know thy self" as he who knows himself, knows his Lord. This will then allow that leader to be as close to his respective prophet as possible.
- This concept of leadership is related to what it means to be human as well in that mankind is to be proper stewards of the breath of the divine in themselves. Since we are all stewards or trustees, we can only be effective trustees if we understand the meaning given by the creator.
- In addition, the Quran reminds us that people do want a more horizontal leadership.

The Values of a Leader

- A crucial element in good leadership is human governance which is an inside-out rather than outside-in approach. Human governance needs to be adaptable, resilient and positive.
- Leaders must also be moderates as global moderation is what is needed; extremism, the opposite, is what is the bane to many nations.
- Other key values highlighted include transparency, consistency, visionary, a willingness to make the unpopular but right move, and inclusive.
- Some key leaders highlighted during the session include Warren Buffet, Jack Welch, Steve Jobs, Abraham Lincoln and the Don Vito Corleone from the Godfather.

Leadership for a New Generation

- In today's technological age, leadership is becoming more democratised which has allowed leaders from any background to rise and overtake previous market leaders.
- Leadership needs to be more bottom-up as well, as leadership cannot be taught and is learned only by doing. Thus, leaders need to be more hands-on in the understanding and execution of their leadership skills.
- Leaders also need greater breadth in knowledge, especially with information so widely accessible, to mitigate the downside of "jumping to conclusions" in an ever more rapid world.





RAMSAR MANGROVES SPECIAL EVENT

The final session of KMF 2012 before the Prime Minister's dialogue was a special event honouring the Ramsar mangroves of Johor, and showcasing Khazanah's environmental and CR initiatives in this area. The event began immediately after the arrival of the Prime Minister, the MB of Johor and the Minister of International Trade and Industry. It was a unique event, in that it involved the work of creative people – each with a different art form.

KNB has actively undertaken various programmes to meet our Corporate Responsibility obligations. Many of our CR initiatives were showcased at our recent Hari Raya Open House. Khazanah's mandate as a treasury for the nation is not purely a financial one. Khazanah is tasked with protecting important national assets, including **natural** ones. Today there is an increasing focus on the importance of natural heritage and natural resources. The work we are doing in this field is for the benefit of future generations.

This event at KMF 2012 was about the environment, and in particular about our involvement in Iskandar – which is at the tipping point in 2012, after six years of very significant catalytic development. Given our investments in Iskandar, we felt it appropriate that we announce measures that fulfill the environmental responsibility which comes with economic development.

Mangroves are absolutely critical to our global ecosystem and the Ramsar convention in 1971 identified a number of such sites around the world for preservation. Three of these are in Johor.

This session evoked the Ramsar Mangrove of Iskandar Malaysia; launched a book about it; and creative guests each honoured the mangrove in their own way.

Media technologist Adrian Cheok introduced his video of young people talking about the importance of preserving the environment. The individual segments were crowd-sourced using social networking.

A short film by writer-director Dain Said was shown. This was a poem evoking the mangrove and expressing love for the Earth. Dain believes that the environment shapes us, just as much as we shape the environment, and this sacred relationship was elegantly conveyed.

Environmentalist Irshad Mobarak spoke about the ecological importance of the mangrove.

Professor Nigel Osborne introduced music he wrote to evoke the life of the mangrove – and his pieces were played live on stage.

Shareen Ghani, Director of Corporate Responsibility at Khazanah, then spoke about Khazanah's CR initiatives concerning the environment in Iskandar.

Khazanah began its work in Iskandar Ramsar in 2010. Whilst we understood its importance, we wanted to see what we could do to help protect these internationally recognised sites.

The Iskandar Ramsar sites have three distinct characters: Pulau Kukup is an island; Tanjung Piai is a cape; Sungai Pulai is a river estuary. These sites have some

species that are unique to its location. The experiences the three mangroves offer in these sites are also different.

A central part of our work was the commissioning of the environmental sector study. We looked at a number of issues that were affecting the mangroves.

The key outcomes from these studies were:

A **biodiversity valuation** study that showed the intrinsic and tangible value of the three Iskandar Ramsar sites that concluded in with findings of a total estimated net present value (NPV) of USD670 million.

The second study focused on the coastal erosion of **Tanjung Piai**. Tanjung Piai is of significant value due to its iconic status as the southernmost tip of Asia. These are pictures showing the coastal degradation that is happening today. According to a study conducted by University Kebangsaan Malaysia in 2011, significant coastal erosion has already occurred.

The third key outcome was the **Ramsar Management Plan**.

The plan was important to maintain the international Ramsar status as required under the Ramsar Convention. With this plan, a more comprehensive implementation of the Iskandar Ramsar programme can be undertaken.

Today's event also saw the launch of three key initiatives as Phase Two of our work in Iskandar Ramsar.

The **three initiatives** are:

The **Coastal Mitigation Plan for Tanjung Piai** to provide a mid-term solution of 3-4 years to protect Tanjung Piai from further erosion. In addition, a rubbish boom and an oil boom will be constructed off the shore aimed at preventing further pollution.

Repositioning and improving the visitor experience of Tanjung Piai through upgrading of the visitor center. With the planned improvements, we anticipate the visitor numbers to double to close to 100,000 per year.

The launch of 'Friends of Iskandar Ramsar' as a platform to collaborate on various conservation efforts. The Friends of Iskandar Ramsar we envision will bring together NGOs, Academia, Local Authorities, Corporates, Communities and individuals.

Khazanah also announced the founding members of the Friends of Iskandar Ramsar.

They are: the Johor National Parks Corporation, Malaysian Nature Society Johor, Iskandar Regional Development Authority, the Earth Observation Center of Universiti Kebangsaan Malaysia and corporate partner, Iskandar Investments Berhad.

Khazanah made a pledge of RM10million to implement the initiatives.

The final part of this event was the launching of the book, *'Sandpipers and Mudskippers: A Journey Through the Ramsar Mangroves of Iskandar Malaysia'* – which was done by the Prime Minister. A copy was given to every audience member.