

MEGATRENDS

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Special Address

Ethics in Finance: Getting Back on Track - How do we Return to Higher Ethical Values in Finance?

Harnessing Creative Disruption: Unlocking the Power of Inclusive Innovation



With his focus on people, Tan Sri Nor Mohamed Yakcop's Khazanah Megatrends Forum (KMF) 2015 Opening Address anchored on 'Inclusive Innovation,' the second key component of the 2015 KMF theme, "Harnessing Creative Disruption: Unlocking the Power of Inclusive Innovation." Indeed, the core of his message can be summarized by his quote, "...we must be aware of *whose* income innovation *really* grows, as innovation does not necessarily lead to income and wealth creation for all classes in the economy.

Diving more deeply into the issue, Tan Sri Nor argued that innovation was not necessarily a game that was rigged in favour of the rich, since innovative ideas do not come only to the wealthy but from any level of the socio-economic ladder. However, when it came to the commercialisation process, innovation often favoured risk takers and so, it favoured those that have larger security blankets. In addition, he pointed out that the owners of innovation may use and abuse their product or services to further increase their wealth, to the detriment of the rest of the population.

Having described the potential pitfalls of innovation, Tan Sri Nor then turned to the question of how Creative Disruption can be harnessed for social inclusivity. He stated that innovative products,

particularly in food, health and basic livelihood, can contribute substantially to improving the welfare of the lower-income groups. This, he notes, is Inclusive Innovation, defined, by the World Bank, as "any innovation that leads to affordable access to quality goods and services for the poor on a sustainable basis and with extensive outreach."

Elaborating on the power of Inclusive Innovation, Tan Sri Nor argued that one of the core components of Inclusive Innovation is affordable access. Thus, he raised the idea of Frugal Innovation, described as "the process of reducing the complexity and cost of a good or a service and its production, so that more people may be able to enjoy the innovation, including and especially the lower-income groups."

With the need for Inclusive Innovation in mind, Tan Sri Nor delved into the question of the role of government. The Government, Tan Sri Nor suggests, needs to intervene to ensure a fair distribution of wealth and to remove social injustice arising from any disruption. However, he cautions as well that regulators need to allow for the 'creative' in Creative Disruption and, consequently, the Government must not kill the goose that lays the golden eggs and must motivate 'animal spirits' in entrepreneurs.

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The conclusion of Tan Sri Nor's Opening Address for KMF 2015 was a philosophical one. He laid the groundwork by discussing how, in the not so distant future, smart machines may replace many types of work performed by humans and, as such, even skilled workers may find themselves becoming redundant. Yet, that may not be as apocalyptic as it sounds. According to Tan Sri Nor, it is possible that the productivity gains and wealth created by robots and smart machines may enable humans – unemployed though they may be – to live a leisurely life with good income, with equitable wealth distribution by the Government.

This therefore raises the question – would this be a happy fairy tale ending for the human species on Earth? Tan Sri Nor invokes the Greek myth of Sisyphus who was punished by the Greek Gods to an eternity of pushing a boulder up a hill, only for it to roll down again at the end of every day. He adds that while people may believe that Sisyphus feels extreme punishment for having to undertake an exercise in futility for eternity, Tan Sri Nor cites French philosopher Albert Camus who argued that Sisyphus was freed by his lucid knowledge and acceptance of his task. In other words, Sisyphus was fulfilled because he had a purpose.

Relating it to innovation, Tan Sri Nor makes two points. Firstly, even if innovation eliminates the need for humans to work to lead comfortable lives, might it also eliminate human purpose? Thus, may there be a limit to technological innovation vis-à-vis purpose? Tan Sri Nor's second point reminds us that, despite the 'heroes of innovation' which tend to be more high-skilled, we must also applaud the millions of workers who work hard to put food on the table and pay their mortgages, even if they may lack the glamour of those involved in rapid innovation.

To sum, Tan Sri Nor's Opening Address was a fitting way to kick off the 2015 Khazanah Megatrends Forum. By reminding us that no matter what or when or where or how we innovate and operate, the who and why of the operation and innovation are still the most important considerations. The human species is wholly dependent on its social and relationships capacities and, consequently, Creative Disruption must be harnessed to unlock the power of Inclusive Innovation, with the primacy of Creative Disruption focused squarely on people.

Special Address

By Charles Leadbeater, Author and independent strategic advisor



An Age of Innovation and Stagnation

- We are currently living in an age of oxymorons. For instance, we are in an age of quickening innovation and yet we worry about secular stagnation and aging societies. We have an abundance of technology and information, yet the biggest problem in the world is the scarcity of clean water.
- As wealth continues to accumulate in the hands of a few while income growth of the median worker starts flattening out, the old theory of capitalism seems to be weakening.

How To Be Human In An Age Awash With Technology

- Our daily lives are threatened to be stuck in an age where “we are running faster to stand still.” There is a sense of acceleration in our daily lives without moving forward.
- The rising tide of aspirations for a better way of life met with tight constraints today is a recipe for contradiction and frustration. However, this is also a recipe for innovation as innovation relies on experimentation and imagination given resource constraints.
- Thus, the challenge is “how to be more human in an age awash with technology”. The unique element of being human i.e. our ability to create, communicate and build relationships needs to be adapted into technology.

4 Characteristics of An Innovative Organisation: Lean, Simple, Social and Clean

- **Lean:** In the midst of tight constraints a company's approach to production should be lean. From lean production to lean platforms, an organisation does not have to own everything but is able to add value by connecting the producer and consumer, such as Uber.
- **Simple:** The need to be quickly used and simple. Simple systems with clear purpose, designed to be used without too much thought.
- **Social:** The more you build society the more you spread costs and speed up learning. Social technologies create more efficiency.
- **Clean:** Innovation by reusing – Husk Power Systems can serve an entire village by reusing rice husks. The idea of mini utilities can create a big future. Another example is a Sundrop farm in Australia that created a self-reinforcing cycle to grow food.

Luncheon Address

By Dato' Sri Nazir Tun Abdul Razak



Institutions, not capital, is the issue

- Banks, the key agents of financing in the Malaysian economy, are behind the curve in funding entrepreneurs due to conservative lending.

- As a result, the government has to step in and fill the funding gap. Today, through various government entities, from Cradle to Equinas, there is a growing pool of capital allocated to finance promising start-up ideas.

- There is no lack of capital. Instead, the main issue is the lack of institutional capacity to nurture a self-sustaining ecosystem conducive for innovation in Malaysia.

Key concerns of Malaysian entrepreneurs

- Malaysia is at risk of facing greater relocation of businesses to neighbouring countries such as Indonesia and Singapore.

- Relocation of businesses is largely due to the heavy Government presence in the economy, perception that businesses are not on equal standing before the Government and the culture of top-down decision-making.

Radical social-political re-engineering

- Post 13 May 1969, the National Consultative Council (NCC) formulated the New Economic Policy (NEP) and *Rukun Negara* to mitigate inter-racial economic disparity based on a universal set of ethical principles. For the most part, this experiment has been a success.

- However, Malaysia's socio-political structures have evolved in a way that make us uncompetitive in an innovation-driven world.

- Malaysia should set up an NCC II, pooling together the best minds across every strata of society with the goal of re-engineering the socio-political landscape of this country.

Special Address

Democratising Higher Education



Education is a Basic Human Right and Needs to be Democratised

- If you give a man a fish, it lasts one night; if you show a man how to fish, it will last a lifetime.

- Current job landscape makes it vital for continued lifelong learning since average tenure at jobs are only 4.5 years.

- Thus, education needs to be made as accessible as air or water, this can double the world's GDP.

Talent Exists Everywhere but Most are Unrealised Due to Lack of Access

- Udacity increases accessibility to educational attainment for communities that would otherwise be left out of the current system.

- Sebastian's first class had 160,000 sign ups. Out of those 23,000 students finished the course. These students came from 195 countries, using 44 languages. Cost per student turned out to be extremely cheap at 60 cents per student.

- In his first class, he compared his regular Stanford students to online students, and the online students were among the top of the class.

Online Learning Is Disrupting Higher Education

- Elements of disruption via online learning: self-paced projects and classes, global mentors and coaching, certification and job placement.

- Further, the Uber-fication of student services will get more people engaged.

- Silicon Valley will help to reinvent the university: Firms determine course materials and set the educational goals.

KMF2015 Special Event

Shuttlecocks, Cinema & Artistic Disruptions





Wisma Central – a decades-old shopping and business building just a few minutes' walk from the Mandarin Oriental – has hidden within a cavernous space containing a badminton court and exhibition area, with galleries overlooking, and this was the venue for this year's unique and extraordinary Special Event: 'Shuttlecocks, Cinema and Artistic Disruptions'.

Imran Ahmad explained how this event came about. Tan Sri Azman Mokhtar said a few words, followed by the introduction of the curator of the event, Datin Saidah Rastam, and architect and Wisma Central advocate, Ridzwa Fathan. Computer controlled projectors were used to turn one wall into a stunning giant screen on which all the performances could be viewed.

Diffan Norman spoke about the digital revolution, breathtakingly illustrated on the projection wall. Amir Muhammad presented a hilarious spoof on a fictional aspect of Malaysia's film industry. Dain Said reflected on old and new values in the cinema industry. Jonathan Cavendish demonstrated the work of his Imaginarium studio, in which reality and fantasy are seamlessly blurred. Unforgettable was Chris Chong's multi-dimensional installation around the badminton court, featuring young people practising badminton.

Finally, the anachronous presence of a baby grand piano was explained by Gita Wirjawan playing some moody late night jazz.

An electrifying atmosphere prevailed throughout, and the lucky guests felt that they had been at an event that was indeed unique and special.

Session 1: Macro and Markets

From Mountain High to River Deep - Will Emerging Markets Become 'Submerging' Markets?'



The 'Bears' Anti - EM

- **Diminishing demographic dividends is a structural issue** : Demographics dividends that EM once enjoyed in the first half of the decade is diminishing. Against this backdrop, EM economies would need to improve productivity by more than 20-30% to attain the same level of growth.
- **Nature of growth in developed world no longer supportive of EM story.** The developed world's economic model is now service oriented, less trade based. This makes the case for EM recovery through exports rebound a harder story to sell.
- **EM has exhausted policy options, no easy solution but institutional change.** Policy makers have exhausted monetary policy, while fiscal policy is not a popular view among politicians.

The 'Bulls' Pro - EM

- **No hard landing in China, with China is set to become a great consumption story.** While China is at the core of EM collapse, there will be no hard landing in China. China is set to become a great consumption story in the next decade, following its transition away from its credit-led growth model.
- **Markets overshoot and psychological factors are at play.** Psychological factors are driving the markets, with markets prone to overshooting. EMs are still a good story as markets need to see past the broad volatility as value is relative.
- **Other EMs are providing opportunity for growth.** While some EMs are facing challenges, other EMs are providing opportunity for growth, i.e. Africa. India is globally the largest recipient of FDI in 1H-2015 with wonderful demographics, while Vietnam and Bangladesh exports grew in the past two years. ASEAN is still a good story, supported by intra-ASEAN trade, complementarity and good demographics.



Reflections on Day 1 by Tan Sri Dato' Azman Hj Mokhtar, Managing Director of Khazanah Nasional Berhad

The theme of this year's KMF clearly resonates and has hit a nerve among our participants, which is something we strive for. There was, I thought, a good variety of manifestations of our theme. Tan Sri Nor Mohamed Yakcop set the stage by taking a broader macro view of innovation, particularly on people and Inclusive Innovation. I really appreciated his discussion on philosophy and how innovation would fit into what it means to be human. This actually led naturally into Charles Leadbeater's session where he discussed what it meant to be human in an age of technology. This fit nicely between the macro view and the micro view by Sebastian Thrun, whose message on Inclusive Innovation resonated at the product level. It felt almost like passing a baton in a relay race!

Session 2: Firms and Transformation

Learning to Fish: How do Firms Harness Creative Disruption?



Boards & Management Structure Required for Innovation

- It is important to note the information asymmetries between the board and management; management has a much greater insight into the business vis-a-vis the board. Thus, different situations require different levels of board participation.
- Tolerance for small failures must be acceptable by management and board to bring about an innovative environment.
- We should emulate how successful companies create a conducive environment for management to invest in innovation (i.e. Apple has a weekly meeting with all divisions to keep pace with changing environments).

Culture for Innovation

- Arrogance is dangerous. Every career, company, country goes through a cycle of collapse and disruption. We should not be too fixated on labels and existing legacy identities.
- Shareholders often have their short term requirements while innovation requires a longer gestation period to provide returns. We should value short term returns but continue to invest in the future.
- The Innovation culture thrives in Silicon Valley as failure is often celebrated. Failure often seen as a valuable trait as it provides the best learning experience on how not to do things.

Trends in Disruptive Innovation

- Companies should consider investing in activities that may disrupt their own business model – “eat your own children”. This is necessary if their business models could potentially be disrupted by changes in the industry.
- When things are changing faster on the outside than it is within the company, “the end is near”. Investing into R&D and new disruptive industries must be done in anticipation on changes within the industry.
- Even consulting firms are subject to disruption as adding value to clients is becoming increasingly difficult. Freelance models, and innovation to free, digital transformation and experiential consulting trends have disrupted the consulting industry.

This was further seen in Dato’ Sri Nazir’s luncheon address which, typical of Dato’ Sri Nazir, was succinct, to the point and action-oriented. His poignant address is one which I suspect will be referred to in years and years to come.

Our two cornerstone sessions, Macro & Markets and Firms & Transformation were also terrific. The debate format (with banter attached!) for Macro & Markets was an innovation for KMF 2015, with the bears ultimately making a more convincing case. What I thought was most interesting was how closely divided the bulls and bears were, reflecting the uncertainty in markets. For Firms & Transformation, there was a good mix of speakers: disruptors, disrptees, financiers and a futurist. It made for a captivating session which highlighted the dilemmas and opportunities for firms very well.

The discussion from Firms and Transformation was then seamlessly captured by Datuk Marjorie Yang. We saw how an old industry – textiles – can be imbued with ethics and innovation to maintain its success. We

then ended the first day quite poignantly with Ethics and Finance, with some really deep thinkers on the subject. For them to sustain the crowd even after a long day showed how engaging the session was.

Day 1 of KMF 2015 saw a record turnout. Even our spillover room spillover-ed! While we are delighted that KMF sees such traction, we do apologise for any shortcomings in managing the spillovers. However, one really good consequence of such spillovers was that, in the spirit of inclusivity, CEOs, speakers, younger Khazanah staff and other distinguished guests were all seated at the same table, engaging with one another. That I think is the true spirit of KMF.

This sets us up well for the artistic KMF Special Event and Day 2 of KMF. Having covered the more macro and business topics, we now move closer towards the social and society aspects which are integral to KMF. Here’s to an amazing Day 2 of KMF 2015.

Special Session

ETHICS IN FINANCE: Getting Back on Track - How do we Return to Higher Ethical Values in Finance?



Key Disciplines in Shaping Public Honesty

- There are four types of discipline that shape honesty – self, regulatory, market and social discipline.
- While self-discipline is key, it is in itself insufficient in ensuring ethics in finance given that economic agents are susceptible to self-interest.
- Competition law is essential in ensuring market discipline. However, it is important to note that an environment of excessive competition gives rise to the possibility of bad business models.
- In the practice of prudent regulatory discipline, there needs to be an independent second party that regulates the regulators. However, it is important to ensure regulation is not excessive to facilitate greater innovation.
- Ultimately, social discipline is the responsibility of all agents in the economy.

Equity and Risk-Sharing instead of Debt and Risk-Shifting

- The future of finance will be in risk-sharing, based on trust, since risk transfer has a limit: it can't be transferred again and again. Risk-sharing could prevent debt-based bubbles: "House of Debt" – housing crisis could have been prevented if there was risk-sharing in housing loans.
- Options are a form of equity to pool risk and invest cheaply, in which an investor can lose all the capital (small downside) in exchange for a huge upside.
- We should try to see if we can screen people based on their potential, their personalities or their innate entrepreneurial talent, not their past, thereby shifting the focus to collateralising individual human capital.

Future of Banks or Lending

- The future lender would look very virtual – centralised/decentralised structure.
- Big data algorithm would be running a mass of millions of loans officers. These loan officers would screen people based on entrepreneurial potential and in the next few minutes that person would get her funds – or not.
- The dialectic between the loan officer and borrower should change. It should not be about not paying interest payments on time, but about the business going well. If it is not going well, the bank should take an interest as to why. If the business does well, the bank will do well too.



Special Address

By Datuk Marjorie Yang

Apparel industry is subject to disruption

- In the past, apparel makers only cared about production quota and labour costs. A high production quota enables economies-of-scale, while cheap labour costs maximize profit margins.
- However, as trade barriers come down (via regional frameworks e.g. TPPA, ASEAN Economic Community) and mechanisation replaces humans, apparel makers need to innovate constantly to keep up with competitors.

Mindset change is the biggest challenge

- The traditional Asian growth model is capital and labour-intensive, which suffers from diminishing returns. Without adoption of technology, productivity growth will continue to taper.
- Players in the apparel industry are generally complacent when it comes to innovation and sustainability. For example, when asked why fishes in a lake nearby are dying, factory owners say that that is the necessary environmental costs of production. But, it is possible to innovate processes to minimize energy consumption.
- Penang, the "crown jewel" of Esquire's operations, is in danger of lagging behind the innovation curve due to the resistance to change. It is easier to "start from scratch" by setting up new factories in Vietnam or China.