Middle East

Point *of* View

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Winter 2013

Changing times, changing places

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87 Eighty seven years in the Middle East

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The world may not have ended in December 2012, as had been predicted by certain civilizations, but it has certainly changed. These changes, which encompass all aspects of life as we have grown accustomed to it, be they political, economic, financial, business or environmental to name but a few, have been so strong and so wide-reaching that they have questioned many ideas we had accepted to be truths. Even a traditionally conservative Middle East has had to react.

The Internet of course has been a catalyst to such transformations, at the center of these changes. Offering an unparalleled wealth of information in one location, hitherto unprecedented, one can reach for a favorite book, learn the best businesses practices, even find one's grandmother's favorite recipe and learn all the components of a plane's engine, even learn to play a favorite piece of music, in the comfort of one's own armchair.

But like all that is good and beneficial, there are risks and measures to be taken to mitigate these. Anything you say or do on the world-wide web (the name is suggestive enough) can, and will be, held against you. Proceed with caution.

Emmanuel Durou, in his article on the growth of e-commerce in the region *Click.buy.com*, suggests that "e-laws," despite having "undeniably progressed over the past few years with a number of markets implementing the necessary digital policies including e-commerce and data privacy laws," remain a weak link in the development of e-commerce in the Middle East. "The challenges," he says, "lie in the diverse legal structures from country to country and the relatively recent adoption of these laws resulting in lack of awareness and enforcement mechanisms."

Julie Kassab, author of *May the best branch win*, highlights how Internet banking is affecting the industry by "dramatically changing the role of the traditional bank branch. "The reduced number of in-bank transactions is forcing banks to rethink their communication and growth strategies as well as their budgets." Banks in the GCC," she says, "will need to prepare for the next phase and become high performers, through interacting with customers and telecommunication service providers to deliver through the channels quicker."

Speaking of growth strategies, Rajeev Mehta and Richard Clarke discuss the benefits and downsides of pursuing a mergers and acquisitions-led strategy for growth in their article *M&A: it pays to get it right*. Many companies, they argue, will be "looking for good investment opportunities" rather than keeping "large cash reserves on their balance sheets and earning low interest returns from the bank." That is one of the factors that they outline. But, they argue, "if you don't have an M&A strategy, how will you know when it's right for you?"

A growth of a different kind is discussed in the article by Suketu Gandhi, Giovanni Rodriguez and Greg Banks *From mad man to superwoman:* the rise of the Chief Marketing Officer, a rise they describe as "inevitable in the age of the empowered customer."

Also empowered are the Small and Medium Enterprises in the Middle East says Rushdi Kikhia as governments wake up to their importance in driving the economy and "are setting up programs to create them, support them and enable them to succeed." For more about the subject read his article *Is small more beautiful?*

Also in this issue read Ali Kazimi's and Paul McConville's thoughts on the final FATCA regulations. "Whether or not there is finality with respect to all aspects of this new information reporting regime," they say "impacted organizations should begin – or in some cases continue – a path toward compliance."

Dr. Louis Hobeika shares with us his thoughts on the future of the International Monetary System and its impact on the Middle East North Africa region.

Revolving back to our theme of change and caution, Ross Pennington outlines how although "there was little surprise" at the announcement that foreign investors would eventually be permitted to invest directly in Saudi Arabia's Tadawul index "the application of a cautious and measured approach to the change appears to be their ongoing strategy."

Just as our ongoing strategy here at the *Middle East Point of View* is to keep you updated and informed. And in contributing to the technological changes that are transforming our world, we are happy to inform you that you can now read all ME PoV on your tablet, on the move or in the comfort of your armchair.

ME PoV editorial team

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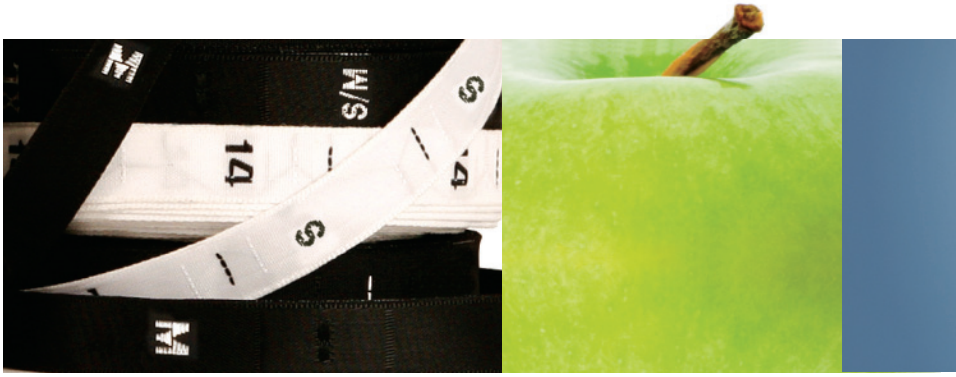

In this issue

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The Middle East region has witnessed strong growth of e-commerce despite weak links in the value chain

On many counts, the past two years have been extraordinary for e-commerce in the Middle East. The total value of online transactions in the region grew three- or even four-fold in some countries. A number of regional start-ups bucked the e-commerce trend with many overpassing the symbolic USD 1m mark in revenues after less than two years of operations. Some of these success stories include JadoPado, EmiratesAvenue and Alshop. Simultaneously, group-buying companies such as Cobone also drove the growth of e-transactions in 2011 though the trend has receded in 2012 with the exit of Livingsocial from the market. One of the first homegrown movers in this space, Souq.com, has consolidated its leadership in the market through acquisitions (including Sukar.com, the online private shopping club) and grew its business from an "à-la-eBay" auction platform to a full-fledged fixed price online marketplace. E-commerce companies have also attracted a significant amount of foreign investment with Souq.com, Namshi and MarkaVIP securing USD 75m overall last year from foreign investors including the likes of JP Morgan and Naspers.

However, the spectacular growth of e-commerce hides some important gaps in the market and some missing links in the e-commerce system that need to be addressed in the next few years to allow for the sustainable growth of online business in the region.

Consumers' adoption of e-commerce still immature

On the demand side, and despite the growth experienced over the past two years, e-commerce adoption remains relatively low compared to international benchmarks and varies greatly by country. In a recent survey conducted by Deloitte and Ipsos on

media and online behaviors in the Arab world, it averred that 16 percent of the population in the United Arab Emirates (UAE) shops online. In other markets such as Morocco, Egypt and Saudi Arabia, e-commerce penetration appeared to be significantly lower at 2-3 percent of the population. A second indicator reveals that e-commerce in the region remains in its early adoption phase as online shoppers in the Middle-East tend to buy limited physical goods such as electronics or fashion items and buy primarily tickets, usually perceived as less risky to be purchased online. Indeed, in the same survey, ticketing (including entertainment and flights) still makes up for more than 60 percent of online purchases.

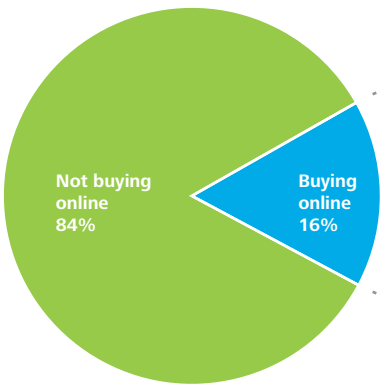
Three core enablers are essential to ensure a vibrant e-commerce market: good logistics, fit-for-purpose regulation and effective payment gateways

Small and medium businesses in the region have yet to embrace the e-commerce trend

On the supply side, with a few regional exceptions, the market remains dominated by international heavyweights – Carrefour's online retailer for instance is believed to account for around 20 percent of total e-commerce transactions in the UAE. More importantly, while the region – and specifically Jordan and the UAE – has seen the advent of a number of e-commerce start-ups, the vast majority are online marketplaces such as MarkaVIP or Souq.com and there is limited adoption of e-commerce as an alternative retail channel amongst the Small and Medium Business (SMB) segment. The growth of e-commerce worldwide has been fueled by a number of high-profile success stories of small businesses online – from selling cupcakes to oversized shoes. In the Middle-East, the SMB segment has yet to embrace e-commerce. In a recent survey done by Deloitte and TNS in Qatar, it averred that only six percent of SMBs interviewed sell goods and services online across industry sectors, with the key barriers to adoption being security concerns, lack of funds and lack of IT skills.

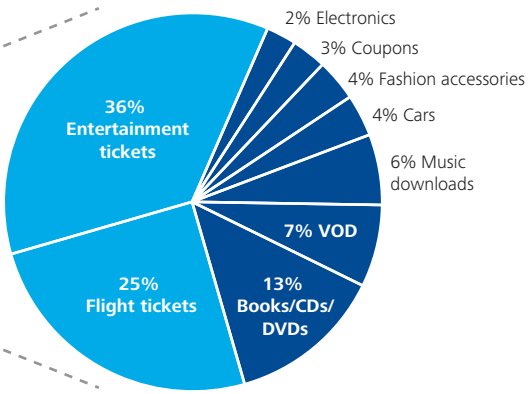
Figure 1 - e-commerce behavior in the UAE

Online buyers in the UAE (%)



Note: UAE - % of total (sample = 430)

Type of items purchased online in the UAE (%)



Note: UAE - % of online transactions - multiple responses were allowed (sample = 71)

Source: Arab Media Outlook 2011-15. Published in April 2012.

Weak links in the regional e-commerce value chain

A deeper dive into these adoption gaps from a demand and supply side uncover some critical missing links in the regional e-commerce economic system. Three core enablers are essential to ensure a vibrant e-commerce market: good logistics, fit-for-purpose regulation and effective payment gateways.

While there are strong differences from country to country in the region, it is fair to say that the Middle East has yet to develop a more robust position on all these three enablers. Logistics and delivery services often hinder the growth of e-commerce due to the difficulty to coordinate home delivery with the existing postal system and, in many markets, the uncompetitive nature of domestic delivery. It is not surprising that the countries with the highest penetration of e-commerce also enjoy the availability of alternative delivery providers such as Aramex. Regarding regulation, "e-laws" in the region have undeniably progressed over the past few years with a number of markets implementing the necessary digital policies including e-commerce and data privacy laws. Again, for regional e-commerce players, the challenges lie in the diverse legal structures from country to country and the relatively recent adoption of these laws (e.g. Qatar passed the e-commerce law in 2010) resulting in lack of awareness and enforcement mechanisms. The last enabler, payment gateways, is proving to be an issue primarily from an affordability standpoint. Merchant Service Commissions and cost per transaction in the region tend to be on the high side when compared to international standards and the set-up and annual fees for the service are usually prohibitive for small and medium businesses.

The good news for e-commerce in the region is that the local market has been creative in finding solutions to the shortcomings of the traditional e-commerce value chain. Aramex has worked very closely with e-commerce providers such as Souq.com and, more recently, Namshi to optimize the inventory and delivery logistics. On the payment front, Cash-on-delivery has proven to be a good (if not sustainable) interim solution to the lack of credit card adoption and trust in online transactions. Still, today close to 70 percent of all orders in the Middle East are done on a Cash-on-delivery basis. In the same vein, pre-paid card payments of online orders have been a potent alternative to credit cards to the extent that a regional, homegrown company, CashU, developed a successful business model out of it.

The better news for the region is that a new generation of entrepreneurs is leading the transformation of the regional economy into the digital age

The better news for the region is that a new generation of entrepreneurs is leading the transformation of the regional economy into the digital age. The survey conducted in Qatar by Deloitte and TNS, showed that local SMBs in their growth phase (2 to 10 years of existence) are twice more prone than average to the adoption of e-commerce activity. These young companies share some common traits – a strong belief in the benefits of technology adoption, a willingness to develop beyond borders and just enough cash to start investing in future growth. Should the region overcome the current limitations of its e-commerce environment, there is no reason to doubt that the Middle East will continue to experience high double digit growth in e-commerce in the coming years.

by **Emmanuel Durou**, Telecommunications, Media and Technology (TMT) director, Deloitte Middle East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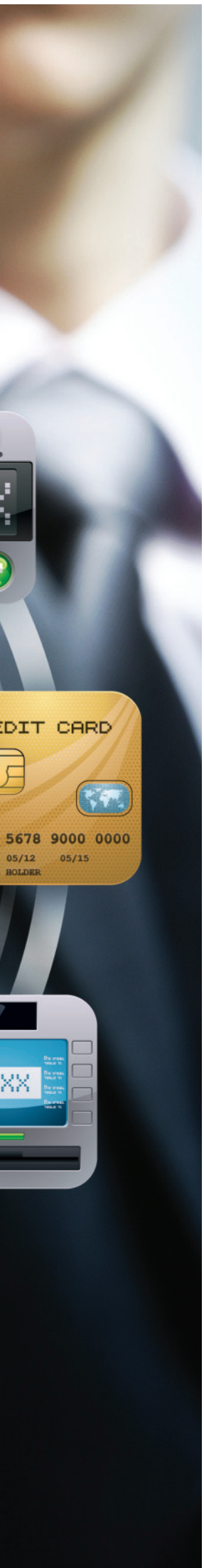


May the best branch win

The traditional bank branch vies with its virtual counterpart

As the Internet and related social media continue to prove themselves a powerful, if unavoidable, tool to help businesses in keeping their employees and customers connected, banks are facing fundamental issues with the rise of electronic banking transaction channels, namely about the role of the traditional bank branch and its future.

Many banks consider the branch to be their primary customer relationship channel – they focus and rely on branches to promote their products and new services. But do their customers still want to make the trek to the bank? Bank customers have needs that can be mainly summarized in three points: they want to have control over their finances (more than the bank does), they want options for their finances instead of focusing on one bank and they want a better experience – they want to have the ability to access banking services at any time, from any location; they want transparency in fees and access to quality.

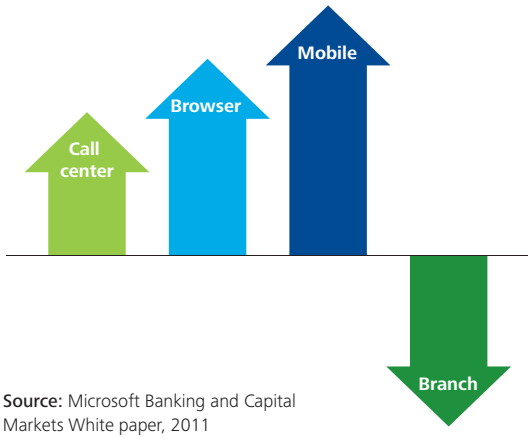
These needs can be summarized in one main service: Internet banking. Internet banking allows customers to monitor their finances and check their balances and fees at any time.

Accordingly, the role of the bank branch is changing dramatically. Today, the majority of daily banking transactions are done electronically and very few customers still visit the branch to perform their banking operations. In addition, new technologies, such as social networking, are forcing banks to develop new ways to create the right customer experience and ceding them more control.

By 2006, Internet banking had overtaken day-to-day branch operations and by 2010, 75 to 90 percent of retail banking transactions were being processed through the call centers, the Internet and mobile devices. Multi-channel banking had become a reality.

Banks are using several channels to deliver their services, such as call centers, Internet and mobile banking. The majority of these bank channels were independent (as shown in figure1). In the 1980s a customer would visit a bank 20 to 25 times a week to withdraw cash and enquire about their balances. Then the call centers were developed and the need for a bank visit lessened. By 2006, Internet banking had overtaken day-to day branch operations and by 2010, 75 to 90 percent of retail banking transactions were being processed through the call centers, the Internet and mobile devices. Multi-channel banking had become a reality. Customers have a 360° view of their activity on every channel and at any point of time.

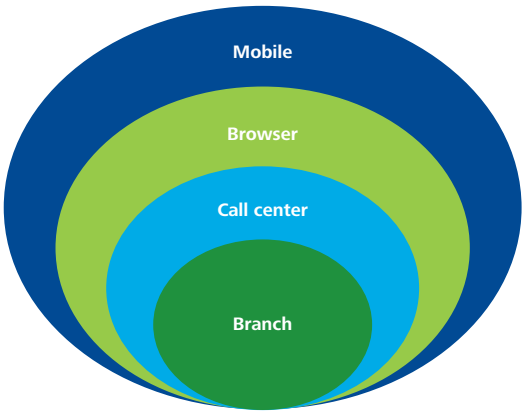
Figure 1 - Independent channels with fragmented impact



Source: Microsoft Banking and Capital Markets White paper, 2011

Statistics in early 2011 reported that the average number of in-branch transactions in the United States dropped from 11,400 per month in 2006 to 8,440 in 2010, leading to expectations of a 56 percent reduction in teller staff by 2015. Customers sometime like to research online and get advice from a customer service at the same time. These channels should complete each other and should be integrated all together. They need to be reinforcing (as shown in figure 2).

Figure 2 - Integrated channels and growing influence



Source: Microsoft Banking and Capital Markets White paper, 2011

Banks stand to gain substantial benefits by investing in integrated multi-channels. First it helps in optimizing operating cost and resources. Branch staff could be deployed in other functions and investment in branches would be smaller as the number of customers visiting would be fewer. Second, banks with advanced banking services can attract customers from other banks, especially with mobile banking, which is considered the most advanced service requested by customers. Thirdly, by decreasing costs and improving sales, investment in multi-channels can affect the ranking and positioning of individual banks.

A study performed by Accenture entitled *Banking in the Gulf Cooperation Council in 2015* and performed on the banking industry in the Gulf countries reveals that higher customer expectations will mold the industry by 2015. This expectation can be mainly addressed through strengthening and enhancing the distribution channels. For example, mobile banking will be particularly useful in improving customer engagement and could encompass innovative services delivered over mobile devices.

The challenge of the banks is to decide when and where to start. Each bank should seek to define its own vision and set strategies to replicate the competition. Understanding what customers want is key to success.

However, banks in the GCC will need to prepare for the next phase and become high performers, through interacting with customers and telecommunication service providers to deliver through the channels quicker.

Because today mobile banking is taking off as the fastest growing channel for retail banking services, GCC banks recognize the importance of IT in their business operations and are increasing their IT spending over the last years.

To conclude, the challenge of the banks is to decide when and where to start. Each bank should seek to define its own vision and set strategies to replicate the competition. Understanding what customers want is key to success. Bank branches exist nowadays in a world of constant change, as do the customers. Strengthening the relationship between them is the primary role of the bank in the future.

by **Julie Kassab**, principal, Audit, Deloitte Middle East

M&A

It pays to get it right

In the aftermath of the global financial crisis corporate priorities are shifting away from strategies centered on the short-term goal of self-preservation – such as cash accumulation, debt paydown and cost reduction – and more towards "growth." What do we mean by growth, why is it so important and how do we achieve it?

Companies, be they private or public, all need to evidence growth as a key stakeholder objective. Growth (both financial and non-financial) drives confidence that in turn influences multiple facets, both tangible and intangible, within an organization. For example, a growing company is seen as a successful company, both from within the organization and by the outside market. The company benefits as its people are happier (employees generally want to work for successful organizations), its trading partners are happier (as their businesses grow as a result) and the shareholders are happy as returns increase. But most importantly, growth drives value and this is most clearly evidenced in the public markets where companies that outgrow their competitors see their share price rise.

Acquisition-driven growth can deliver accelerated growth and can supercharge your business if it is done properly. But there is a downside: if it is done poorly, it can severely damage your business.

So if a growth agenda is so important why aren't more companies following growth strategies? The simple answer is that most are. Growth can take a number of forms, which are most commonly grouped as "organic" or "acquisition-driven" growth. Organic growth is generally considered more conservative and while it does have many benefits, an organic growth strategy most probably won't set you apart from your peers, as all good companies are continually looking to innovate and grow organically. Acquisition-driven growth can deliver accelerated growth and can supercharge your business if it is done properly. But there is a downside: if it is done poorly, it can severely damage your business.

Is now the time to follow a mergers and acquisitions-(M&A) driven growth strategy? For every reader the answer will be different. However, M&A activity is picking up and will probably continue to gather pace in 2013. What is going to drive this M&A activity? Firstly, many global organizations have large cash reserves on their balance sheets and rather than earning low interest returns from the bank, they will be looking for good investment opportunities. If these can't be found, shareholders will want to see these excess funds returned. Secondly, the pricing gap between vendors and acquirers has narrowed considerably during 2012. Thirdly, with many domestic economies showing little or no growth, there is limited opportunity for organic growth. Fourthly, M&A activity, both locally and globally from financial investors such as private equity houses is increasing (as evidenced by our recent Private Equity confidence survey). Most investors remain optimistic about the short- to medium-term outlook with some going as far as to say that 2013 will be the year of renewed vigor.

So what does this all mean? That if now is not the right time to drive growth through acquisition, it soon will be. If you don't have an M&A strategy, how will you know when it's right for you? Develop your M&A strategy and ascertain what you want to achieve through an acquisition. Goals may include, but are not limited to:

- Growth in market share through elimination of a direct competitor;
- Acquisition of suppliers or intermediary customers (collapsing the value chain);
- Product or technology acquisition;
- Geographical expansion or acquisition of key customers;
- Diversification away from your core business; or
- Human capital acquisition.

Most businesses are not resourced to easily deal with M&A internally, so there comes a time when you may need to ask for some help. There are many M&A advisors in the market, these advisors cannot, and should not, make decisions for you, but they can help you navigate the often complex world of M&A. More importantly, they can help you identify suitable targets, understand what you are buying (identifying and qualifying risks), assist with business modeling and valuations and if you do choose to proceed with an acquisition, can assist in managing the integration. Make sure the advice you get is of the highest quality as an acquisition is often one of the most significant events in a company's history – it pays to get it right!

There are many M&A advisors in the market, these advisors cannot, and should not, make decisions for you, but they can help you navigate the often complex world of M&A

You can always learn from the best, and Warren Buffett is arguably the most successful investor of his generation. Here is a collection of useful insights into Buffett's views on some of the more 'sticky' issues:

On investment timing:

"…We simply attempt to be fearful when others are greedy and to be greedy only when others are fearful."

On what to buy – flight to quality:

"It's far better to buy a wonderful company at a fair price than a fair company at a wonderful price."

"The best thing that happens to us is when a great company gets into temporary trouble. We want to buy them when they're on the operating table."

"I try to buy stock in businesses that are so wonderful that an idiot can run them. Because sooner or later, one will."

On price or valuation:

"Price is what you pay; value is what you get. Whether we're talking about socks or stocks, I like buying quality merchandise when it is marked down. The price of an investment can mask its true value because of factors such as emotion, market booms or busts, and even tax considerations. Sadly, all most people see is the price, they are often unable to perceive value."

On risk appetite:

"I don't look to jump over 7-foot bars: I look around for 1-foot bars that I can step over."

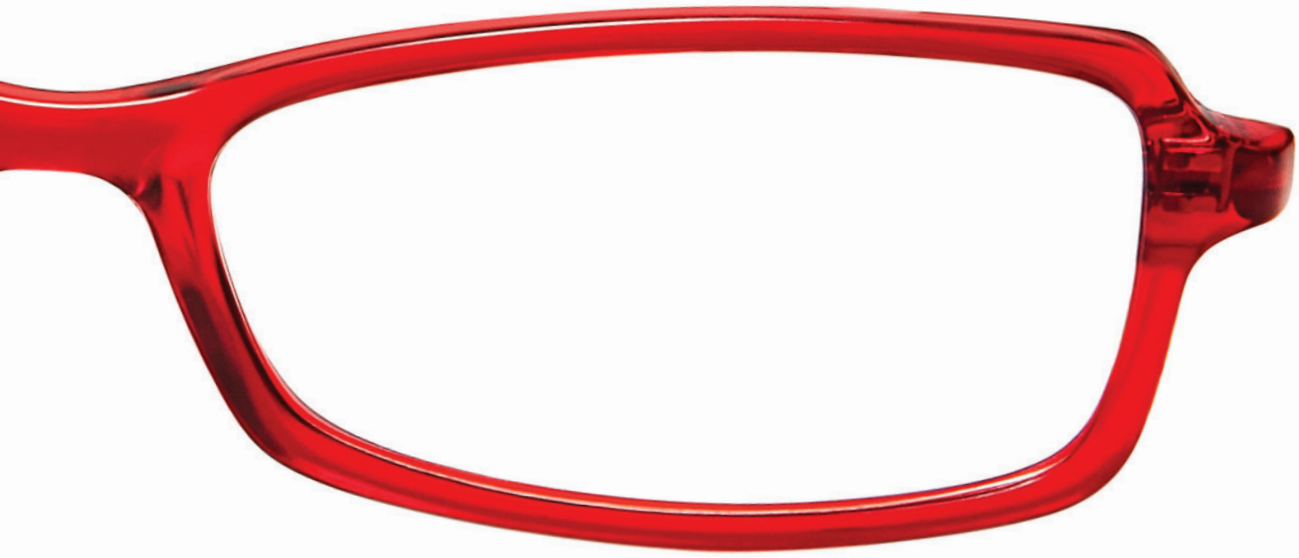
"Risk comes from not knowing what you're doing."

"In the business world, the rearview mirror is always clearer than the windshield."

by **Richard Clarke**, managing director, Transaction and Restructuring Services, Deloitte Middle East and **Rajeev Mehta**, director, Transaction & Restructuring Services, Deloitte Middle East

From mad man

Today's Chief Marketing Officer (CMO) is smarter, wiser and – contrary to popular belief – enjoys a higher average tenure. But it hasn't always been this way. What happened? Let's take a short trip back in time and experience the evolution of this executive. Her ascendance was always in the cards, but she had to wait for the rise of another player.



to superwoman

Prologue: The carousel

In what is perhaps the most memorable moment in Mad Men – the popular TV show about the heyday of mass marketing – fictitious 1960s adman Don Draper brings a roomful of men to tears with a pitch for a product that would soon be iconic. But for anyone watching the show – a half-century into the future – the power of the scene comes not from what the pitch means for the future but instead how it addresses our need to connect with the past. Indeed, the concept for the scene, the episode and the entire show is nostalgia, which Draper defines as a "twinge in your heart, far more powerful than memory alone." Draper renames the product – a slide projector – "The Carousel," because it "lets us travel the way a child travels – around and around, and back home again, to a place where we know we are loved."

The scene provokes nostalgia not just for the characters but for each viewer, and particularly those with ties to the marketing world. For everyone and everything in this scene – the people, their purview and the product (a romantic product from a simpler, bygone age) would someday be disrupted. Next time you watch this scene, ask yourself: who works inside the enterprise, and who works outside? Who is at the head of the table, and who is off to the side? But it's just as important to ask who is not in this scene. In a bit of creative brilliance – and misdirection – the hero of "The Carousel" is not anyone from Kodak nor from Draper's fictional agency. The hero is the customer, dramatically projected on the wall of the conference room. The reason the people in the scene – and we as viewers – are bowled over is that they see themselves on the screen. They were experiencing not only a brilliant business pitch but the beginning of an unstoppable trend: the rise of the customer, she who

would ultimately flip the conference room table and rearrange the many relationships in the marketing ecosystem. As we show later in this article, even the table itself – a real and symbolic theater of operations for marketing people – is swapped for another. Despite all that, some things remain the same.

In the pages that follow, we'll take a close look at what has changed and what has not. And we'll take a look at the rules and tools that marketing executives now have at their disposal to do the work of connecting with the customer. We'll also consider how the myth of the all-powerful creative genius outside the enterprise would be supplanted by the impossible ideal of the all-powerful CMO inside the enterprise. It's a myth that's worth exploring – and deconstructing. For the history of the CMO, in part, is about the positioning and marketing of the CMO. And if there's anything we know about CMOs, it is that they are very good marketers.

Act I: The evolution of a profession

To understand what life is like for the CMO today, it pays to look at this story. And while the 1960s are a good place to start the narrative, there are other intervening periods, each with its own disruptions, and each with a specific set of challenges.

For the history of the CMO, in part, is about the positioning and marketing of the CMO. And if there's anything we know about CMOs, it is that they are very good marketers.

Creatives

Let's begin with the actual "Mad Men," a class of creative professionals whose moniker refers to the mecca for marketing minds of the day (Madison Avenue in New York) and alludes as well to the legendary temperament of its most talented practitioners. The reputation of the creatives was in part undeserved, but telling. The rap: they are not like us; they are special (in a good way and in a bad way). And if you were a client back then (e.g. a CMO predecessor), you would understood that you would have to look outside the enterprise and make that visit to Madison Avenue. You needed them.

But what else can we say about them? First, they had a profound and lasting effect on the still young marketing industry. Some, like Bill Bernbach, co-founder of agency giant DDB, and George Lois, one of the alleged inspirations for Mad Men's Don Draper, continue to inspire practitioners today. Second, while their reputation for flash tends to dominate, what the best from this era stood for was something quite different: a more quiet and deliberate attempt to focus on the customer. In his recent book, Lois talks about the marriage of art and text that produced famous campaigns like "You Don't Have to Be Jewish to Love Levy's."[1] At a time when the creative mystique was running at its highest, Bernbach and Lois were at work laying down the law, which prescribed connecting with the customer. They looked into the hearts and minds of the customer. And, perhaps for the first time, a few of these masters found a home inside marketing where they could design memorable campaigns. It was a turning point. Marketing would never be the same.

Targeters

The Levy's campaign is a good segue to the next period: the era of targeted marketing. Marketers gradually found ways to cleverly expand their companies' appeal

by segmenting their messages to multiple demographic, psychographic and other types of customers. Over the next couple of decades marketing would witness the acceleration of databases, CRM and – toward the end of this period – a new tool for direct marketing: email. The magazine industry exploded, going from a handful of publications that advertisers could reliably depend upon to hundreds of new titles that targeted and chased the increasing heterogeneity in America.

And TV? Marketers had to navigate a bewildering expansion from three broadcast networks to the huge and expanding catalog of channels on cable TV. And the targeting had an impact on the marketing ecosystem as well. The supplier network fragmented as agencies specialized to remain competitive. And, of course, with these new skills and competencies came a new wave of leaders. These were the days of Robert V. Goldstein, a vice-president of advertising at Procter & Gamble – an example of a modern CMO – who was a leader on the impact of mergers in advertising, and also recognized and responded to the impact of cable television.[2] And, perhaps fitting at a time when brands were increasingly seeing the benefits of customer diversity, these were also the days of executive diversity. For example, there was Charlotte Beers, the first female vice-president at J. Walter Thompson and later CEO of Ogilvy & Mather. And there was Tom Burrell, the founder of the legendary Burrell agency, focused on the needs of African-Americans. This was also the era when Hispanic marketing came into the mainstream.

Indeed, the leaders in this era were more diverse – by gender, race and religion. Some were inside; some were outside. Some were on the creative side of the business; others were more on the side of the new sciences that were entering the world of marketing. And along with this diversity came complexity. The simple time of Mad Men – those days were over, though they still played on the imagination of both the industry and the public.

Marketers gradually found ways to cleverly expand their companies' appeal by segmenting their messages to multiple demographic, psychographic and other types of customers. Over the next couple of decades marketing would witness the acceleration of databases, CRM and – toward the end of this period – a new tool for direct marketing: email.

With their appetite for facts and figures now whetted, marketers took a keen interest in the scientific side of the profession and began importing and developing new competencies. From the 1980s to the end of the century several branches of technology and science-enabled marketing emerged. This is when many of the top companies first began to work with sophisticated systems, which allowed, for example, for targeting segments all the way to "one." The analyses at first came with esoteric names like "hidden Markov models" and "auto-regressive moving averages." But there were simple names too. The Burke Recall Test, as an example, swept through this era as a way to measure viewers' recall of TV commercials. ("Hey, we pulled a 35 on Burke; let's knock off early!") In the laboratories, marketers were also looking at "controlled geographies" across the United States, attempting to isolate the variables of media spending and creative change.

While it's true that many businesses assigned the CMO title in the digital era, an alternative explanation is, once again, the steepening rise of the customer

If the three-piece suit was the signature garb of Madison Avenue, the power suit of the new era was the white lab coat. The marketing whiz held the consumer under the microscope, entered her home and studied her with pen and pad – and increasingly, computer – in hand. But there were organizational changes as well. What drove the adoption of the new scientific tools was the ongoing rise of consumerism, and the new consumer sciences held the promise that marketing could be measured like any other business function. Marketing was accountable after all. It could, in fact, create a new place in the C-suite, where the ability to discuss numbers is the price of admission.

Digerati

According to some who have studied the topic, the rise of the CMO title came around the time that the Web rose to prominence and ushered in the digital era. As one industry insider later opined – in a blog entitled "Are You a CMO or a VP of Marketing?" – this was the age of hype, and Internet marketers were of course "good at marketing the job of marketing and themselves."[3] In an article for Forbes, two others noted, "like so many things during that period, [the CMO title] was driven by a preoccupation with appearances more than by practical need."[4]

While it's true that many businesses assigned the CMO title in the digital era, an alternative explanation is, once again, the steepening rise of the customer. This rise was apparent in the creative era. And it was palpable in the subsequent targeted and scientific eras. In the digital era, however, there was a leap in customer centricity. Marketing would never be the same. The tools that emerged in this period – the graphical user interface (GUI), click-through advertising, display ads, e-commerce and search – all derived their strength from providing a new experience for the customer. Well before the dawn of Web 2.0, we heard the mantra that the customer was in charge.

In practice the customer had always been in charge, but now the tools of the trade for engaging them were more direct, more transparent and increasingly more interactive. The digital era, defined by the disruptive force of the Web, gave way to a new pantheon of

technology players to accompany the buyers (the brands), the sellers (the agencies) and the publishers (the media companies). And square in the center of this disruption was Google's big bet on a new category – search – which placed the customer's immediate desires smack in the middle of the universe. Perhaps the best way to frame the value of search came from John Battelle in his book The Search: Google is a "database of intentions."[5]

A database of customer intentions, to be precise. In the digital era, the customer truly began to call the shots. But this era doesn't belong to Google alone. It was the beginning of an era marked by many innovations in online interaction and mobility. And, yes, the beginning of a large new category that would figure even bigger in the next era: social media.

Act II: The Impossible Job

But what was the impact on the job of the top marketer, the newly minted CMO? With each successive phase we saw the steadily accelerating rise of customer power. And with each successive phase we also saw the emergence and consolidation of organizational power with the top-ranking marketer. With the rise of the customer came the rise of the CMO. Finally, each era also came into being with one or more major disruptions by way of media, technology or social change. So as she rose, the job of the top marketer kept getting harder. The history of the CMO we have plotted thus far follows a precipitous path – more a storyline for a fallen hero like Icarus – destined for a short lifespan (tenure) because of his or her ambitions.

Well before the dawn of Web 2.0, we heard the mantra that the customer was in charge

New responsibilities/New risks

It pays to take a closer look at some of the details of the job inherited by the CMO in recent years. On one level, as noted, there were things that made the new job harder. On another level, there were relationships with a new group of peers and professionals that would have been foreign to the 1960s adman. The combination of the two made life very challenging.

First, the skills became expansive. In addition to assuming the roles of the creatives, targeters, scientists and digerati, what exactly are the expectations for today's CMO? It helps to begin by looking at how the job of marketing has been framed. The marketer is responsible for the customer. To paraphrase Philip Kotler, one of the influential leaders in marketing education, marketing is about "meeting customer needs profitably."[6] And as Wikipedia has defined it, "marketing is used to identify the customer, satisfy the customer, and keep the customer."

Expanding on this view in the context of the top marketing job, one commentator observed that "a CMO should be the interface between the company and the customer – responsible not only for marketing communications but also product development and sales."[7] This expansion of scope has been a common theme in articles about the CMO job in media and marketing publications. "Some CMOs," according to an article in MediaPost, "are taking responsibility for functions including operations, finance and public policy."[8] And this expansion has ultimately forced top marketing execs to acquire not just any type of skill but those more typically associated with a better known member of the executive suite: the CEO.

In an article entitled "The Rise of the Chief," Lesley Young noted that "being a CMO in most cases results in new responsibilities and a heavy-duty reliance on basic business skills. For better or worse, CMOs accept that their title means they are now under the corporate spotlight and glaringly accountable."[9]

But what was the impact on the job of the top marketer, the newly minted CMO? With each successive phase we saw the steadily accelerating rise of customer power. And with each successive phase we also saw the emergence and consolidation of organizational power with the top-ranking marketer. With the rise of the customer came the rise of the CMO.

And are there any particular executive suite skills that he or she should master? Strategy, metrics and analytics. CMOs gain credibility, according to one writer, "not by touting taglines but by crunching numbers."[10] CMOs, wrote another, "distinguish themselves with the "strategic long-term view, exceptional measurement and analytical capabilities and financial management." The title of a recent article in Ad Age proclaimed, "When CMOs learn to love data, they'll be VIPs in the C-suite" – but not until then.[11]

And if all of this is not enough, the modern CMO has to do this work in the public eye, more than perhaps any other person on the executive team. In an article entitled "Why Do Chief Marketing Officers Have Such a Short Shelf Life?," Mike Linton, the former CMO of eBay, noted, "just like major league managers, a CMO's game plan and tactical brilliance are on display every day."[12]

And what about the relationships with the marketing chief's new peers? If the need to get real about numbers wasn't enough of a clue, let us be clear: the CMO now needs to be cozy with the CFO. The CMO today needs to be fluent in the lingua franca – financial returns – of all corporate boardrooms, and the CFO is the person closest to these types of numbers.

And another relationship has arisen as well, precipitated by forces we will examine momentarily: the CMO's relationship with the CIO. While it's now commonplace to talk about how these two people must work together, not long ago the idea was unimaginable. The importance of technology in the execution of today's marketing has created a sense of urgency for this alliance. Perhaps the most dramatic illustration of this point came recently in a Gartner report that stated that by 2017, "an organization's CMO may have a bigger 'IT' budget than the CIO."[13]

With this type of future, clearly the CMO and CIO will need to become cozy. But this sounds easier than it is in practice. The language, culture and values of the two have been, for decades, worlds apart. No wonder a recent Ad Age article proclaimed that large

consultancies increasingly are asked to provide the services historically associated with traditional marketing services agencies.[14]

And finally, whose job is it to bridge all these worlds – the customer, the organization, the C-suite? Because the aggregation of skills and relationships is being driven by the urgency to keep up with new ways of identifying, satisfying and retaining the customer, we suspect that this job of bridging, like so many others, will go to the CMO.

Act III: The postdigital tipping point

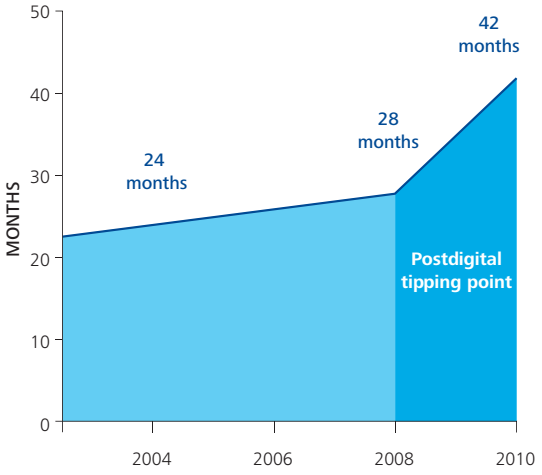
If you ask industry observers to comment on the expectations versus the performance of CMOs today, there is a big delta. First, there is the notion of the "super CMO," which Ad Age has described as someone whose mission "isn't just marketing, but strategy and overall growth" of the company,"[15] or the CMO as a "super species," defined by Media Post as someone who has "responsibility for functions including operations, finance and public policy." Slightly less aggressive, but still elevated, is the idea – from one of the top talent recruiting firms – of the CMO as "marketing's CEO."

The CMO is, of course, as high as you can go in marketing. But the expectation should give one pause. The role of the CMO has been fluid and rapidly changing, and some of the new responsibilities have come so recently as to make it nearly impossible for many to get their arms around them. The average tenure of CMOs, perhaps, tells that story. As a Spencer Stuart survey reported in 2008, the average tenure for CMOs was just 28 months, up a mere four months from 2004 (see figure 1).[16]

That CMOs would fare so poorly in the face of such great expectations should come as no surprise. But like so many other things in the history of marketing, there's more here than meets the eye. In their 2010 CMO survey, Spencer Stuart reported that the average lifespan of the CMO rose by an astounding 14 months – to a new record of 42 months – in only two short years.[17]

And what about the relationships with the marketing chief's new peers? If the need to get real about numbers wasn't enough of a clue, let us be clear: the CMO now needs to be cozy with the CFO.

Figure 1 - Average tenure of the chief marketing officer



Source: Spencer Stuart Press Release, Average Chief Marketing Officer Tenure Hits New High: 42 Months, May 24, 2011

This raises a question: if the previous eras in the history of marketing – creative, targeting, scientific and digital – were each brought about by a technological or social disruption, what was the disruption in the last two years that solidified the role of the CMO? Our answer: the network-driven empowerment of individuals. This includes networked customers, of course, and also everyone else in the marketing ecosystem.[18] Network-driven empowerment may in fact be the disruption driving our current CMO era, which we call the postdigital era. If the CMO owns the disruption, great things can happen. If not, woe to the CMO.

The new tools

But what are the new tools of the trade that might in fact enable the CMO to "own the disruption?" Let's start with the technology, because in many ways it is responsible for this postdigital era. Shortly after social media burst on the scene, savvy marketing thought leaders made it clear that the business premise of all this is the connected individual. Networked customers can now be motivated to work on behalf of companies by co-creating the brand and sharing it within their own networks. The rise of social networks such as Facebook, Twitter and others has enabled more than a billion customers to interact in this manner. It's not just connected customers buoying the CMO; it's also the networked employee, the connected supplier, and of course the networked citizen. Myriad industries are expanding their market footprint by empowering people in their ecosystems, and social technology in all of its forms, is helping to drive this growth.

But there's more to this story than just social technology. The disruption that has helped usher in the postdigital era is also about analytics, which enables organizations and their participants to know virtually everything about one another; it's about mobility, which enables all actors in the ecosystem to connect, wherever they happen to be; it's about the cloud, which provides participants with a more flexible, scalable and affordable infrastructure for networking; and it's about cyber security, which enables organizations to manage the attendant risks of new technologies. And while each of these tools is powerful on its own, they are even more potent in the composite. A good example of this is innovation in the automotive industry, where expectations driven by the connected customer are forcing manufacturers to rethink their in-car experience. What infrastructure (cloud) would enable a car company to deliver an Apple App Store-like experience inside its vehicles? What platforms (mobile) would the apps live on? What's the interaction (social) between customers and others in the ecosystem (the manufacturer, the dealer, the customer service rep and other customers)?

Network-driven empowerment may in fact be the disruption driving our current CMO era, which we call the postdigital era. If the CMO owns the disruption, great things can happen. If not, woe to the CMO.

Finally, there's more to this postdigital era than just technology. There's enablement. Today's CMO can connect to customers in ways a 1960s adman could not imagine. Today's marketer can literally create a meaningful and intimate connection with billions of customers all at once. The new requirement for customer intimacy at scale may in fact be the simplest explanation for the CMO's lengthening lifespan.
In the Mad Men era, marketing was revered in part for its utter simplicity: the creative process – the marriage of art and copy. But marketers were constrained by the limitations of mass media. In the targeting, scientific and digital eras, new tools emerged to enable marketers to communicate with an increasingly diverse and empowered customer base. Throughout all this time, however, it was still marketers talking to customers.

Finally, there's more to this postdigital era than just technology. There's enablement. Today's CMO can connect to customers in ways a 1960s adman could not imagine. Today's marketer can literally create a meaningful and intimate connection with billions of customers all at once.

In the new postdigital era, marketers help their companies become part of a larger system where the opinions of all stakeholders are in play simultaneously. Now companies must really, every day and hour, listen and respond to their customers. In contrast to yesterday's one-to-many channels, CMOs must manage on a many-to-many basis.

Epilogue: around and around… and back home again

To meet the new challenges in this new era, CMOs will of course need to adopt new operational frameworks for harnessing the art, science and individuals involved. The job of the CMO is not easy, prompting industry wags to say that it requires superhuman skills. But already we're beginning to see innovation in this area in a wide range of sectors.

One framework that has recently emerged across a range of sectors is the three-dimensional engagement matrix, or "the engagement cube," as articulated by our colleagues Chris Heuer, Dan Elbert and Dan Nieves (see figure 2). The effectiveness of an organization's

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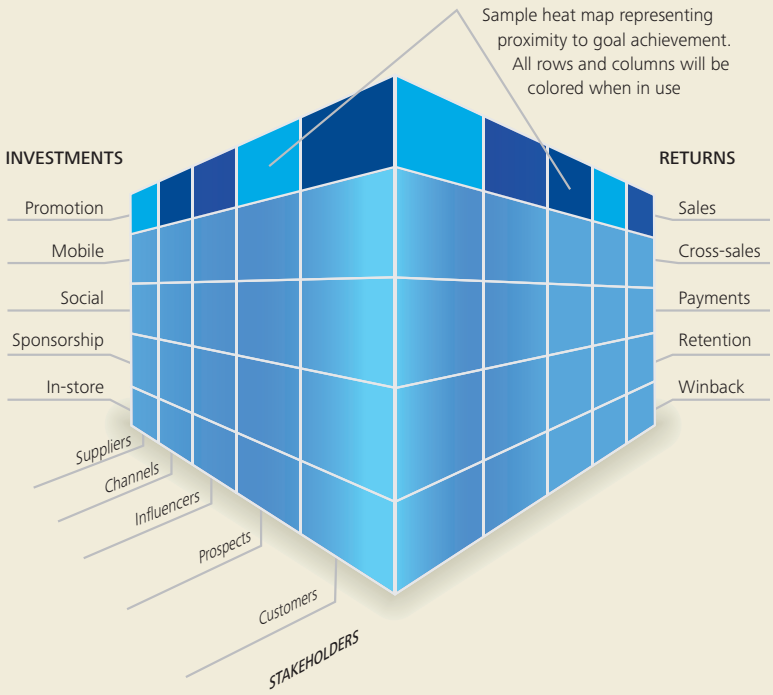
Figure 2 - "The Cube" engagement matrix (illustrative)



By arranging the organization's relationships across several dimensions – the company's stakeholders, the topics that most matter to them, and the goals that the organization has for each of these stakeholders – a CMO can use the Cube as a framework to more readily spot where there is a problem or opportunity.

marketing hinges on its ability to empower all constituencies at once – internal and external – through a vast and complex ecosystem. The cube enables organizations to quickly visualize all these net- works, diagnose their strengths and weaknesses, and, most importantly, gain competitive advantage. It also helps organizations better understand who they are – and what they can be – in the new world that postdigital technology and practices have wrought.

This approach to reimagining and empowering new ecosystems is beginning to take hold in a number of industries and often through – you guessed it – the marketing departments. The cube is part of a larger framework designed to enable the CMO to understand the actual costs of managing and activating a multi-constituent ecosystem. And that is perhaps the framework's most disruptive feature – it enables the chief marketer not only to see what's working and what is not, but to find ways to "disintermediate" the middleman where disintermediation makes sense. For in the postdigital world, where the rules of tools of engagement have come in house, the CMO increasingly has the opportunity to "own" the relationship with the customer. But the simplicity of the cube – a deliberate rethinking of the unwieldy relationship matrices that marketers struggle with today – is just as noteworthy. For in the end, what will really distinguish the postdigital CMO is his or her ability to follow this profession on its accelerating purpose: to connect with the customer.

By arranging the organization's relationships across several dimensions – the company's stakeholders, the topics that most matter to them, and the goals that the organization has for each of these stakeholders – a CMO can use the Cube as a framework to more readily spot where there is a problem or opportunity. And by ranking the relative worth of any of these relationships – e.g. by mapping their influence on the overall ecosystem – the CMO can know where to invest and where to make changes (staff, training, support). Finally,

it provides the CMO with a measurement tool ("how well are we doing?") that can be shared and understood by the stakeholders inside the postdigital enterprise.

This tool – which you can imagine today's CMO spinning and turning in the palm of her hand – is an elegant reminder of the power of her calling. And as with the carousel in that scene in Mad Men, we've come around and around and are back home again. The top marketer is at the top of the table, albeit a different table (in the executive suite) and with a different set of tools. And she still commands our attention.

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Is small more beautiful?

To some they are the catalysts of economic growth, the backbone of the private sector; to others they empower people, drive creativity and encourage specialization. They are the small and medium enterprises (SMEs).

Many governments are waking up to the importance of SMEs to the economies of their countries – in terms of GDP, growth and talent – and are setting up programs to create them, support them and enable them to succeed. Even the independent accounting standard setting body – the International Accounting Standard Board (IASB) – has acknowledged the importance of SMEs and has issued International Financial Reporting Standard (IFRS) for SMEs.

Importance of SMEs to the economy – GCC specific

SMEs are a dynamic and vibrant sector of the economy. They contribute significantly to GDP and provide jobs for the majority of private sector employees, an important asset in the GCC where most countries have employee nationalization programs. GCC governments seeking ways to diversify their economy from oil and gas have opted to boost this important sector. In Bahrain, it is estimated that SMEs contribute 25 percent of total nominal GDP and employs around 75 percent of private sector employees. SMEs also constitute around 90 percent of the private sector entities. In the United Arab Emirates, it is estimated that SMEs contributed 60 percent of GDP in 2011.

Banks in the GCC, through their cautious lending approach adopted in the wake of the financial crisis, are increasingly focusing on lending to SMEs as opposed to personal or large corporate lending because SMEs form a booming market and provide an opportunity to diversify from concentrated lending. In addition, governments in the Gulf countries encourage banks to lend to SMEs and, in some instances, partly or fully guarantee their loans.

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Challenges to SMEs

SMEs have challenges that are general with other entities within the economy and particular to their size and nature, especially in the wake of the global financial crisis whose effects are still felt to this day. SMEs, which are mostly involved in trading, services, manufacturing and construction operate in highly competitive markets, with tight regulatory environments and thin profit margins. More specific challenges to SMEs are the financial and technical restrictions in addition to technology and human resource limitations.

Role of Government

Governments recognize the importance of SMEs as key to economic growth and have established specialized bodies and developed regulations and programs to support and nourish them. This support comes from the initial creation of SMEs and expands to providing technical assistance, financial lines, development of human capital and access to local and global markets. Governments also tend to distinguish between SMEs that are established by 'first generation entrepreneurs' as compared to 2nd or 3rd generation family businesses, favoring those who create employment and provide opportunities.

To take Bahrain as an example, the Bahraini government established Tamkeen in 2006 to support the private sector and position it as the key driver of economic growth. Through the private sector support programs, Tamkeen assists SMEs in hiring well-trained local talent, obtaining sophisticated financial management systems, technological developments and with access to finance. Tamkeen works with banks, financial consultants and training institutions to fulfill its mandate.

In 2002, the Mohammed Bin Rashid Establishment for SME Development (Dubai SME) was incorporated into the Department of Economic Development (DED) as an agency with a vision to nurture business leadership through entrepreneurial spirit. This commitment to the SME sector provides the resources and expertise necessary for providing constant and consistent support. Dubai SME has also launched Dubai SME 100, a premier ranking of Dubai's 100 top performing SMEs. The Dubai SME 100 seeks to identify Dubai's top SMEs that can act as role models. More than just a ranking, the objective of Dubai SME 100 is to inspire willing and able SMEs that have the potential to be world-class enterprises, to invest in innovation and people and to sustain growth. The ranking will also serve as a tool for helping SMEs identify capability gaps for improvement and attract the attention of investors, which is its real value added.

In Qatar, the Qatar Authority for the Development of SMEs was established by an Emiri Decision in 2011, with a responsibility of encouraging the development of the SME sector in Qatar and putting a strategy in place to encourage growth for these enterprises by providing them with technical assistance and coordinating with banks and governmental institutions for the purpose of financing and marketing projects.

In June 2012, The Shoura Council in the Kingdom of Saudi Arabia unanimously approved a set of draft regulations for a separate authority for SMEs. During the discussion, the house felt that such an authority would not only improve the Saudi economy but also provide a substantial number of job opportunities for the unemployed youths in the Kingdom.

Most recently, The Public Establishment for Industrial Estates (PEIE) of Oman announced that it will set a National Business Center in the first quarter of 2013, aimed at encouraging the growth of SMEs. The center will act as a premier platform for developing and supporting Omani entrepreneurs.

Accounting Standards for SMEs

The IASB has carefully considered simplifying the IFRS to reduce compliance costs and, at the same time, increase the benefits of the information it provides to users. Consequently, it issued the IFRS for SMEs in July 2009, a self-contained standard of 230 pages, designed to meet the needs and capabilities of SMEs, which are estimated to account for over 95 percent of all companies around the world. Compared with full IFRSs, it is less complex in a number of ways:

- Topics not relevant to SMEs are omitted
- Where full IFRSs allow accounting policy choices, the IFRS for SMEs allows only the easier option
- Many of the principles for recognizing and measuring assets, liabilities, income and expenses in full IFRSs are simplified
- Significantly fewer disclosures are required
- The standard has been written in clear, easily translatable language

The IFRS for SMEs are available for any jurisdiction to adopt, whether or not it has adopted the full IFRS. It is up to each jurisdiction to determine which entities should use the standard. It is effective immediately on issue.

Conclusion

In the final analysis small is beautiful. After all, the Mini Cooper, the SMART and the VW Beetle are very successful cars. Size produces visible benefits but also hidden costs and risks. Large entities can be vulnerable to many external and internal risks whereas SMEs face lower risks because of their agility. Governments will continue to have a leading role in encouraging the creation of SMEs and pushing them forward. The SMEs' role in empowering the private sector will increase with greater vital contribution to GDP and to the development of their economies. Let us hope that SMEs could, one day, stand for "Solution to the Middle East."

by **Rushdi Kikhia**, partner, Audit, Deloitte Middle East

Governments recognize the importance of SMEs as key to economic growth and have established specialized bodies and developed regulations and programs to support and nourish them

Definition

SMEs are distinguished by the number of full-time employees and initial capital invested or annual turnover. The thresholds differ from one country to another. In Bahrain for instance, a micro and small entity is one that employs up to 50 employees and has a capital of up to BD 500,000 (c. USD 1.3 million) whereas a medium entity is one that employs between 50 to 150 employees, with a capital investment between BD 500,000 – BD 2 million (c. USD 5.3 million). Entities above these ranges are considered large.

As for the IASB, companies are considered small or medium if they:

- Do not have public accountability, and
- Publish general purpose financial statements for external users.

Listed companies, regardless of size, may not use IFRS for SMEs.

The road ahead

Thoughts on the final FATCA regulations

On January 17, 2013, the U.S. Treasury Department and Inland Revenue Service (IRS) released the long-awaited final regulations for the Foreign Account Tax Compliance Act (FATCA) and in so doing are attempting to provide a balanced and integrated method for implementing this law and a risk-based approach that effectively addresses policy, eliminates burdens and builds on existing practices and procedures.

FATCA, codified as Chapter 4 of the Internal Revenue Code, represents the United States Government's efforts to prevent U.S. taxpayers who hold financial assets in non-U.S. financial institutions (foreign financial institutions or FFIs) and other offshore vehicles from avoiding their U.S. tax obligations.

As of January 2014, virtually all non-U.S. financial intermediaries and withholding agents that own or hold U.S. investments will be subject to its information reporting and disclosure requirements. This U.S. legislation will greatly impact organizations' tax functions, technology systems, operations and business strategy.

So what are the modifications to the earlier guidance rules? Below is a summary highlighting several of the specific takeaways from the 544 pages making up the final regulations and preamble.

The Treasury emphasized the adoption of a risk-based approach to address policy considerations and eliminate unnecessary burdens

Treasury's risk-based approach limits institutions, obligations and accounts subject to FATCA

The Treasury emphasized the adoption of a risk-based approach to address policy considerations and eliminate unnecessary burdens. To that end, the regulations:

- Introduce new categories of deemed-compliant FFIs (certain qualified credit card issuers, sponsored FFIs and limited-life debt investment entities),
- Move certain existing categories (retirement funds to definition of exempt beneficial owner and certain non- profit organizations) to a category of excepted non- financial foreign entities (NFFEs),
- Provide greater clarity on conditions to qualify as deemed-compliant FFIs, treat certain passive entities not professionally managed as NFFEs rather than FFIs and,
- Provide an exemption for financial institutions and passive NFFEs that are part of a non-financial group of companies.

While the Treasury's efforts to adopt this risk-based approach succeed, in some part, at limiting the institutions, obligations and accounts subject to FATCA, a consistent and robust approach is still required to successfully manage, remediate and document accounts under the FATCA regime.

Collaboration with foreign governments is a leap towards a global information reporting framework

The guidance also addresses the coordination of the Intergovernmental Agreements (IGAs) and the regulations by making it clear that foreign financial institutions (FFIs) in Model 1 jurisdictions (i.e. countries entering into so-called "Model 1" IGAs will be governed by the laws implemented by their own countries while those in Model 2 jurisdictions (i.e. countries entering into "Model 2" IGAs) will need to follow the regulations in order to achieve compliance.

Perhaps first initiated to remove compliance impediments posed by privacy laws, the Intergovernmental Agreement (IGA) model has essentially moved towards a global information reporting framework. This is clearly evident in the final regulations, which introduce the Global Intermediary Identification Number (GIIN)[1] and mention the possibility of adopting a single format for reporting FATCA information, whether that information is reported directly to the IRS or to the tax administration in a Model 1 IGA jurisdiction. The Treasury also places great emphasis on the relationship with the two forms of IGAs (Model 1 and Model 2). In particular, the final regulations make clear that FFIs in Model 1 IGA jurisdictions will be governed by the laws in force in their own countries, while those in Model 2 IGA jurisdictions will follow the final regulations. However, the final regulations leave open the opportunity for foreign governments to negotiate with Treasury for inclusion of IGA terms that would benefit or protect entities within their jurisdictions from the requirements of the final regulations. Accordingly, the final regulations' emphasis on IGAs may signify Treasury's realization that IGAs – and not the final regulations – may be the path forward to achieve FATCA's goal and establish a global information reporting framework.

Registration and technical implementation questions addressed

The final regulations also provide much anticipated guidance on the administrative responsibilities of FFIs, including details on the responsibilities that will be contained in the FFI agreements, timelines for paperless registration through the FATCA Registration Portal and issuance of the aforementioned GIIN.

Provisions on account documentation and due diligence requirements relieve some burden

Perhaps the greatest efforts to streamline the FATCA compliance burden are found in the sections pertaining to the requirements for account documentation and due diligence. Under certain circumstances, provisions partially reinvigorate the "eyeball test" and allow for the use of substitute and non-IRS Forms, including forms prepared in different languages, reliance on Pre-FATCA Forms W-8,[2] written statements in lieu of withholding certificates, permanent validity of documentation as well as the opportunity to cure inconsequential errors in withholding certificates. Additionally, under specified conditions, the final regulations also allow withholding agents to rely on the same documentation for multiple accounts held by the same account holder and permit new accounts of an existing customer to be treated as pre-existing obligations (allowing additional time to collect requisite documentation) where the obligations are treated as one obligation.

Perhaps first initiated to remove compliance impediments posed by privacy laws, the Intergovernmental Agreement (IGA) model has essentially moved towards a global information reporting framework

Treasury's characterization of this list as "comprehensive" begs the question as to whether this list is indeed exhaustive and does not address how certain payments not contemplated in this list will be treated

These modifications, in addition to several changes to the applicable standards of knowledge, should have a positive impact on the duty to comply with FATCA's documentation and due diligence requirements.

Rules on withholding provide clarity on certain issues but leave others ambiguous

The final provisions on withholding answer certain questions but leave others unresolved. The rules provide additional guidance on the election to be withheld upon and permit this election to be made on an account-by-account basis. With respect to grandfathered obligations, the regulations modify the scope of grandfathered obligations to include any obligations outstanding on January 1, 2014 (previously January 1, 2013) and simplify the withholding agent's ability to determine whether an obligation is grandfathered. With respect to payments that may be withheld and the definition thereof, the Treasury Department has not addressed several of the issues with respect to Gross Proceeds, in addition to remaining nearly silent on foreign passthru payments. As anticipated, Treasury did adopt a revised timeline for Gross Proceeds withholding to January 1, 2017. However, the regulations provided limited additional guidance on gross proceeds (the rules do, however, reserve the ability to elect to be withheld upon for gross proceeds), including on the much commented issue of withholding in "delivery versus payment" or "cash on delivery" transactions and the proposed imposition of withholding responsibilities on qualified clearing organizations (although Treasury did include a reserved section to provide guidance on this issue). Treasury's decision to reserve on these issues may mean that additional guidance should be expected though may not be forthcoming before 2017.

As anticipated, the Treasury Department did address the exception for ordinary course of business payments by replacing this exception with a list of excluded non-financial payments. However, Treasury's characterization of this list as "comprehensive" begs the question as to whether this list is indeed exhaustive and does not address how certain payments not contemplated in this list will be treated. Accordingly, while the provisions on withholding do provide significant guidance on certain withholding responsibilities and types of payments for which withholding will be required, the regulations do not provide clarity on a number of issues.

Reporting provisions unchanged

The final regulations provide scant additional guidance with respect to reporting requirements, with the exception of adopting a modified date for participating FFIs to report on U.S. accounts. However, Treasury did express an intention to release several new and modified forms, including Form 8966 to be used for FFI reporting and revised Forms 1042 and 1042-S.

These rules are now final

One takeaway from these revised regulations – and perhaps the most definitive – is that these rules and the obligations they implement are now final. Therefore, whether or not there is finality with respect to all aspects of this new information reporting regime, impacted organizations should begin – or in some cases continue – a path towards compliance.

Given the length and complexity of the final regulations, it will take some time to thoroughly assess their impacts and changes, but it is clear that FATCA will be a hot topic for many affected institutions and professionals as the analysis of the final regulations continues and additional guidance is issued.

by **Ali Kazimi**, partner, International Tax Services, Deloitte Middle East and **Brandon George**, director, International Tax Services, Deloitte Middle East

Endnotes

1 The GIIN replaces the FFI-EIN and FATCA ID introduced in the proposed regulations and other guidance.

2 Pre-FATCA Form W-8 means a version of a Form W-8, including a valid substitute form, that was issued prior to 2013 and that does not contain chapter 4 statuses.

One takeaway from these revised regulations – and perhaps the most definitive – is that these rules and the obligations they implement are now final

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Currency uncertainties and the future of the IMS

The world has been living without an International Monetary System (IMS) since August 15, 1971 when U.S. President Richard Nixon terminated the convertibility of the U.S. Dollar into gold, thereby ending the Bretton Woods agreement.* Since that action – often referred to as the Nixon shock – was taken, the IMS lives under the reign of the Dollar as the U.S. economy remains the largest and the most dynamic. The last decade has been harsh on the U.S. economy however, as it dipped, in 2008, into its deepest recession since 1929. "The Great Recession" weakened the U.S. economy and its currency and opened the door to a multipolar monetary system based not only on the Dollar, but also on the Euro and the Yuan, as the combined Gross Domestic Product (GDP) of the European Monetary Union (EMU), the USA and China makes up 60 percent of global GDP.

Conditions for an international currency

The essential characteristics of domestic and international currencies are a medium of exchange, unit of account and store of value. To perform an international function, a currency must be available beyond its borders and should be fully convertible. For an international currency to be considered reserve, it should have a creditor status, issued by a large economy with a developed financial system and should be heavily used. Clearly, the U.S. Dollar fulfills these criteria, the Euro to a lesser extent and the Chinese currency not. The fact that Central Banks and private investors consider U.S. T-Bills as safe assets allows the U.S. to finance its current account deficit easily. Some call it "exorbitant privilege" or the ability to print money and receive goods and services in exchange. The current situation requires countries to have faith in the Dollar even as the Fed prints, which actually weakens it. This is known as the Triffin Paradox.

* The **Bretton Woods** agreement established the rules for commercial and financial relations among the world's major industrial states, intended to govern a post-second World War economy. The chief features of the Bretton Woods system, signed in July 1944 by 44 allied states, were an obligation for each country to adopt a monetary policy that maintained the exchange rate by tying its currency to the U.S. Dollar.

Economic foundations for the multipolar system

A currency cannot have the reserve quality if it is not based on a strong economy with a solid potential. The tables below show selected and relevant economic and financial data given and computed by international organizations such as the World Bank and the International Monetary Fund for 2011 (actual), 2012 and 2013 (estimated):

	2011	2012	2013
USA			
Real GDP Growth	1.7%	2.0%	2.3%
Current Account Balance (% of GDP)	-3.1	-3.1	-2.9
Budget Balance (% of GDP)	-9.0	-7.5	-6.0
Gross Public Debt (%of GDP)	102.8	106.7	110.7
EMU			
Real GDP Growth	1.6%	-0.6%	-0.4%
Current Account Balance (% of GDP)	0.1	0.9	1.4
Budget Balance (% of GDP)	-4.0	-3.3	-2.6
Gross Public Debt (% of GDP)	89	91.2	93.2
China			
Real GDP Growth	9.2%	8%	8.5%
Current Account Balance (% of GDP)	2.8	2.3	2.5
Budget Balance (% of GDP)	-1.2	-1.3	-1.0
Gross Public Debt (% of GDP)	25.8	22	19.4

Source: IMF, World Bank

Data from these tables demonstrate clearly that the Chinese economy is strongest and soon will become the largest, although indicators remain weak on per capita basis due to the size of the population. Chinese growth rates are now weakening as the society shifts towards consumerism (and less savings) and the West is urging consumption of its own products to combat recession. The USA and the EMU have different strengths and weaknesses but strong similarities in institutions, legal foundations and culture. As such, future economic competition will be broadly between them on the one hand and China on the other.

Future of the Dollar

The easy monetary policy of the Federal Reserve Board adopted since January 2001 contributed to the housing bubble, to the crisis and to a loss of confidence in the Dollar. The policy was possible due to savings inflow from the Gulf Cooperation Council (GCC) countries and Asia, especially China. The Dollar can probably keep its status as the prime reserve currency if the U.S. can stabilize its current account deficit to around 3% of GDP along with a low budget deficit and a higher savings rate. The U.S. financial policy should change towards a strong and stable Dollar that attracts investment and promotes growth.

Future of the Euro

The crisis in the Euro-zone is severe but Europeans are succeeding in getting their act together. If austerity measures continue however, voters are likely to revolt and political extremists could take over. Financial discipline and the implementation of the Maastricht criteria are needed but not at the expense of social and political stability. The Euro-zone is heterogeneous but can improve outcomes by increasing the common central budget so transfers happen easily in times of crisis. The Euro-zone should shift slowly into an Optimum Currency Area* as defined by Nobel Prize-winning economist Robert Mundell. The Euro could therefore improve its chances of becoming a real competitor to the Dollar as a reserve currency.

* A geographical region in which it would maximize economic efficiency to have the entire region share a single currency.

Future of the Yuan

China has witnessed an impressive growth in output and exports. The country is intervening in markets to prevent an appreciation of the Renminbi against the Dollar. It seems that Chinese leaders are not eager to transform the currency from a local or regional currency to an international reserve. China's lack of open, deep and broad financial markets means that its currency cannot as of yet play a reserve role. When leadership aims for that role, it should float the currency along with full convertibility which will raise its exchange value and lower exports. Is China ready for that transformation? There is no indication of that yet.

Future of the IMS

Quantitative easing is leading to currency competition among those adopting it. Left unchecked, it could lead to a crisis of instability. The IMF should play a crucial role of coordination among central banks and surveillance of the markets to avoid potential conflicts. The Dollar will remain the most important reserve currency with a secondary but growing role for the Euro. The Yuan is not a competitor yet. Fred Bergsten and Joseph Gagnon of the Peterson Institute for International Economics estimate that if currency intervention ceases, the U.S. trade deficit would decline by USD150 bn or 1 - 2 percent of GDP. Between 1 and 2 million jobs will be created. The Euro zone will gain significantly, but less.

Impact on MENA

The world economy undergoes a shift in the balance of power as Justin Yifu Lin and Mansoor Dailami of the World Bank expect that by 2025 six emerging economies – Brazil, China, India, Indonesia, South Korea and Russia – will collectively account for half of global growth. The Middle East North Africa region still relies heavily on oil, which is denominated in the Dollar. The region favors and benefits from a strong Dollar policy that will improve the standard of living for all. It is also safer for MENA to have, over time, an IMS based on three reserve currencies to diversify choice and lower risk. MENA should deepen its relationship with Europe and China to be prepared for the multipolar system whenever it happens.

by **Dr. Louis Hobeika**, economist

It is also safer for MENA to have, over time, an IMS based on three reserve currencies to diversify choice and lower risk. MENA should deepen its relationship with Europe and China to be prepared for the multipolar system whenever it happens.

Endnotes

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Saudi Capital Markets - Open? Ouverts? Offen?

Much has been made of the decision to allow overseas investors access to direct investment in the Tadawul – the flagship exchange of the Kingdom of Saudi Arabia. But as companies across the Kingdom continue to add their names to an ever-increasing IPO pipeline, advisors, and the Capital Markets Authority (CMA) alike, are advocating a cautious approach to the listing process.

There was little surprise at the announcement in December 2011 that foreign investors would eventually be permitted to invest directly in the Tadawul All Share Index (TASI), Saudi Arabia's top index of 155[1] listed companies and widely considered to be the Gulf's most attractive capital market due to its size and maturity. Though investment through swaps and exchange-traded funds had become popular indirect routes for non-Saudi nationals to track the continued growth in the petro-chemical dominated KSA economy, allowing direct foreign ownership has long been seen as a key milestone for Gulf Cooperation Council (GCC) capital markets.

A cautious and measured approach to regulatory change

Allowing foreign investment is obviously and understandably a decision that the Capital Markets Authority (CMA) in Riyadh will not have taken lightly, even with the hint of inclusion as a 'Frontier' or 'Emerging Market' under MSCI[2] classification. Subsequently, the application of a cautious and measured approach to the change appears to be their ongoing strategy, borne out by comments from CMA chairman Abdulrahman Al Tuwaijri that any opening "should be done in an orderly and gradual manner to make sure it does not impact the market's stability,"[3] as well as the fact that, as of late 2012, a formal date and confirmed details for any changes in ownership regulations had yet to be announced by the Saudi CMA. It is expected that foreign ownership will be tested on a trial basis at some point during 2013 – although it is not yet clear what format such a trial would take – and that the foreign ownership in any single Saudi company will be capped at a limit expected to be around 20 percent. It is fair to expect that a stepped process will provide comfort to investors and current Saudi-listed companies that the authorities are considering the full implications of such a large capital inflow, as well as avoiding the creation of a dangerous market bubble. This confidence in the CMA's handling of the process may have contributed in part to the seven percent Last Twelve Months (LTM) growth of the TASI,[4] although obviously the contribution from pre-emptive moves to buy securities ahead of foreign investment cannot be underestimated.

Allowing foreign investment is obviously and understandably a decision that the Capital Markets Authority (CMA) in Riyadh will not have taken lightly

Changes in ownership rules in recent years are not the only sign that the Kingdom is serious about becoming a global capital market. As well as continuing to use share suspensions to crack down on companies not complying with ongoing listing or reporting requirements, in January 2012 the Saudi CMA announced updated listing regulations following a public consultation period in its latest step to improve governance and the listing process. Of particular significance was the express provision that independent financial and legal advisors would be required for any Initial Public Offering (IPO) process, the former being required to confirm the issuer's eligibility for listing through a due diligence process. Such moves, when contrasted with the smaller GCC capital markets, appear to indicate that the Kingdom wishes to improve the reputation of its flagship bourse, as well as the quality of its participating listed companies.

How will capital inflow from foreign investment improve the quality of KSA issuers?

As the CMA drives for improved governance and financial reporting and opens the market to limited foreign ownership, proponents of the Tadawul would hope that market confidence will lead to the long-awaited unblocking of a pipeline that has been bulging with potential IPO candidates since the early years of the financial crisis. However, as the CMA's moves to date show, potential issuers can be expected to be vetted extensively for suitability to a listing and should be aware that any shortfalls in financial reporting, availability and preparation of historical financial information and adequacy of corporate governance could adversely impact their listing aspirations (both in time and shareholder value).

Ultimately, as Saudi companies join an ever-growing queue to go public and enjoy the benefits from additional liquidity generated from direct foreign investment, they should bear in mind that the CMA now has both the luxury and the motive to be selective over the issuers it admits. Potential issuers should be ready and aware of the updated listing requirements, the ongoing reporting requirements, as well as the wider necessity of a strong equity story to attract investors. Regardless of the fine print of the regulatory changes to the Tadawul, it is clear that 2013 will be an intriguing period of transformation for the Kingdom's public market.

by **Ross Pennington,** manager, Transaction & Restructuring Services, Middle East
Deloitte Corporate Finance Limited

Regardless of the fine print of the regulatory changes to the Tadawul, it is clear that 2013 will be an intriguing period of transformation for the Kingdom's public market

Endnotes

1 As at 28 November 2012, http://www.tadawul.com.sa/
2 Morgan Stanley Capital International emerging markets index
3 Reuters, 3 April 2012, http://uk.reuters.com/article/2012/04/03/saudi-bourse-opening-idUKL6E8F31TB20120403
4 Bloomberg, 28 November 2012, http://www.tadawul.com.sa/

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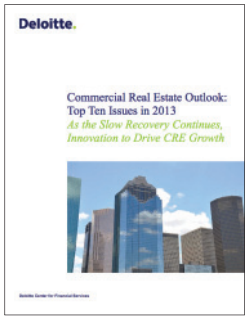

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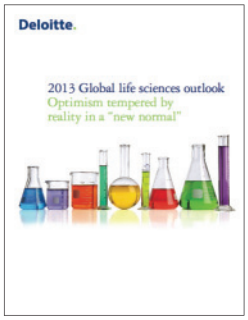

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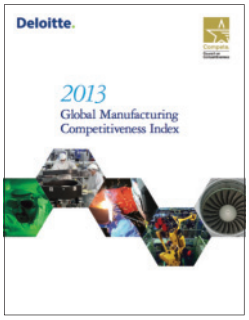

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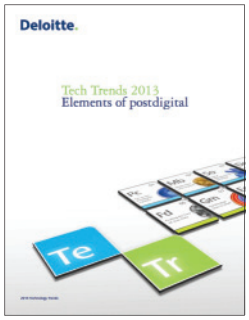

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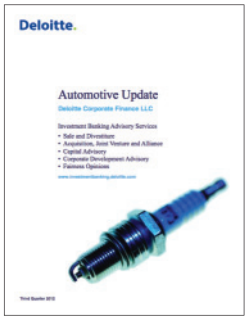

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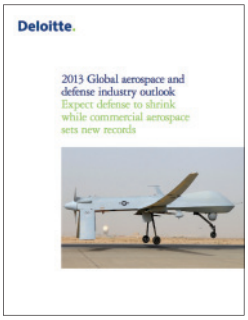

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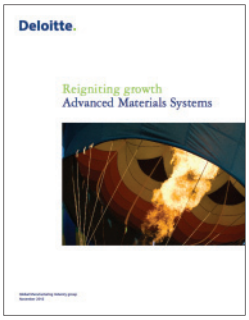

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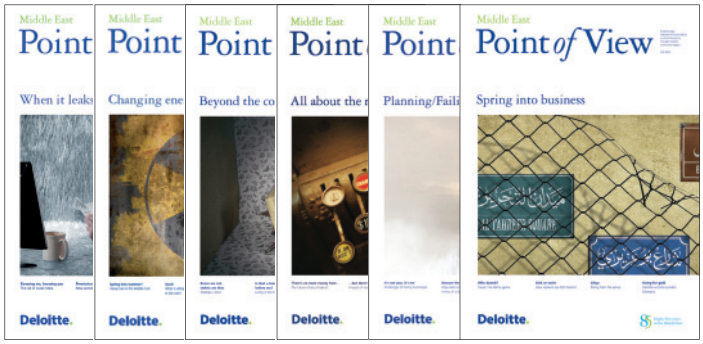

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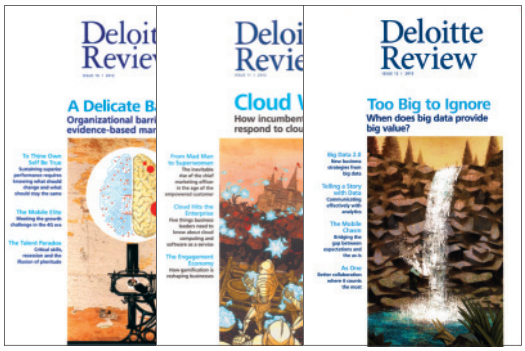

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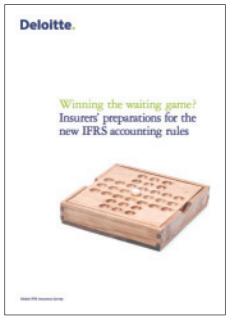

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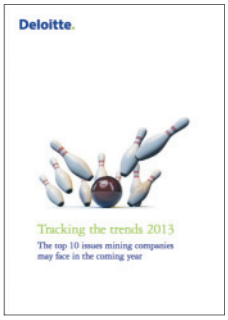

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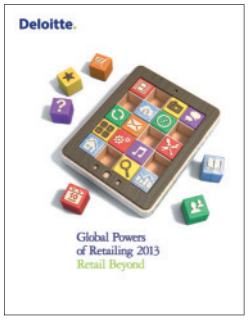

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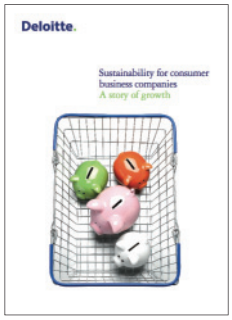

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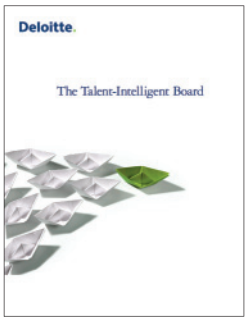

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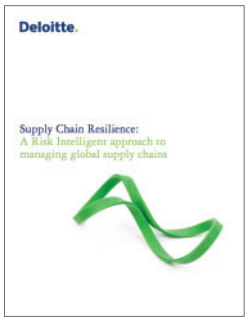

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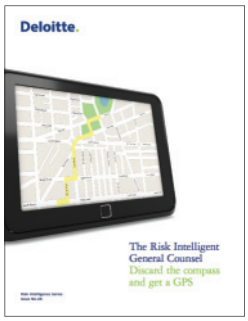

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