Investment Strategy & Research

GCC Fixed Income Market Update

December-2020

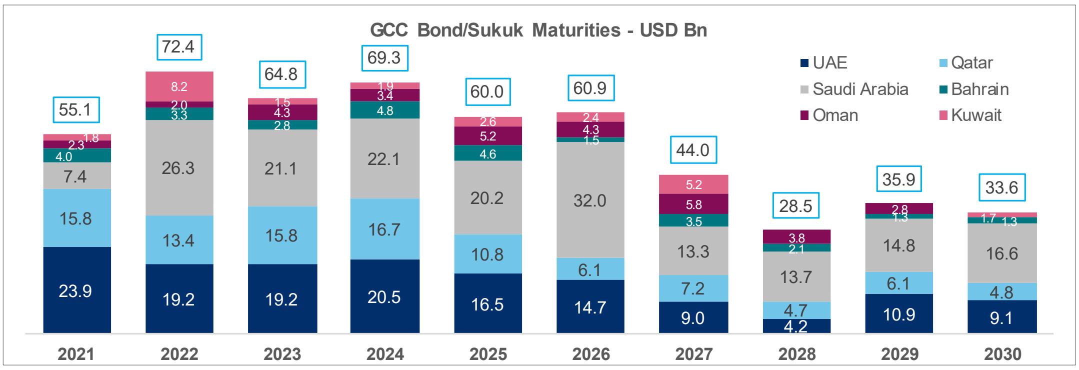
46% of total GCC FI issuances set to mature in 5 years…

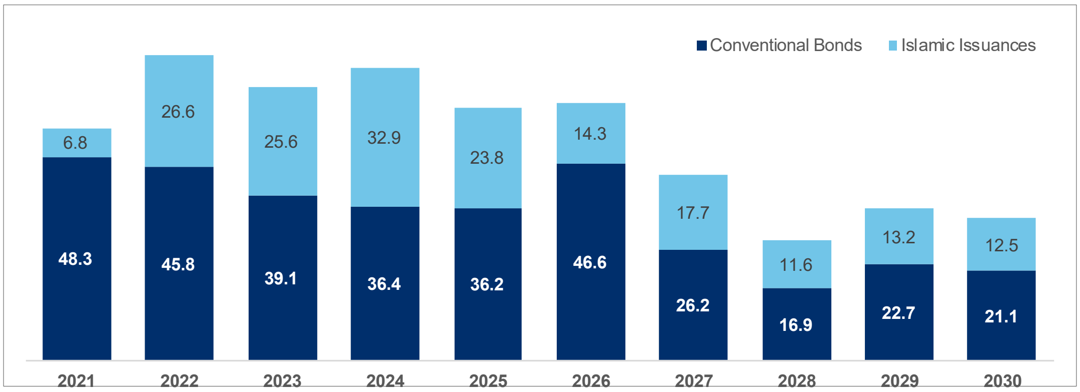
Uncertainty related to Covid-19 and its impact on economic growth across the globe continues to sustain as the number of cases have once again started increasing, especially in Europe. Several countries in Europe have announced a hard lockdown and have clearly stated that easing the restrictions would be unlikely in the near term. There are also news of new strains of the virus, further complicating plan of vaccine deployment. ***Nevertheless, despite the aforementioned, there is an underlying sense of positivity related to near term economic recovery, that is reflected in equity and bond markets as well as commodity prices.***

The fiscal pressure from the decline in economic activity and lower oil revenues has resulted in an increase in debt issuances in the GCC in 2020. This is in-line with issuances across the globe, which despite minimal dependence on oil, has seen ballooning debt levels that has reached record highs at the end of 2020. ***According to WSJ that cited data from Dealogic, emerging market governments and companies issued record amount of bonds in 2020 at around USD 510 Bn. Of this, governments issued around USD 250 Bn and the remaining USD 260 Bn were bonds issued by corporates. These issuances were mainly in hard currencies while local issuances by governments came in at around USD 30 Bn. Demand for EM bonds have remained high due to relatively higher yields as well as many countries have better fiscal management despite the pandemic.***

The bond issuances were aimed at both business expansion via new issuances as well refinancing needs. Data from Bloomberg showed that GCC government and corporate fixed income instrument maturities stood at USD 38.7 Bn since May-2020 that were largely refinanced. Total issuances this year until November-2020 stood at around USD 142 Bn, almost in line with last years levels and full year issuances in 2020 is expected to marginally exceed last year levels.

GCC governments have issued USD 47.5 Bn in bonds in YTD-Nov-2020 with USD 35.4 Bn during 1H-2020. Sukuks issued by the governments stood at USD 28.7 Bn and was almost equally split during the first half the second half of the year. *Last year, bond issuances by governments in the region aggregated to USD 48.8 Bn while sukuks issued were at USD 34.3 Bn. On the other hand, corporate issuances have also been active with USD 46.2 Bn in bond issuances this year until November-2020, whereas sukuk issuances stood at USD 19.9 Bn. This compares to last year's USD 45.3 Bn bonds and 14.8 Bn in sukuks.*





Sources : Bloomberg, Kamco Invest Research

Junaid Ansari
Vice President
+(965) 2233 6912
jansari@kamcoinvest.com

Rating actions

The pandemic has resulted in almost 48 sovereign downgrades and 13 upgrades by the three rating agencies this year and numerous corporate downgrades globally. However, with interest rates at one of the lowest levels, the cost of funding has not been significantly affected.

In terms of ratings action in the GCC, Bahrain, Kuwait, Oman and Saudi Arabia witnessed downgrades by either one or more of the three rating agencies, especially around the peak of the pandemic. Apart from the impact from the Covid-19, these downgrades mainly highlighted fiscal pressure due to the fall in oil prices as the GCC countries heavily depend on oil revenues to meet their budgeted spending. During the year, Fitch ratings initiated credit rating on the UAE and assigned 'AA-' rating with a Stable outlook. In a recent update, S&P said that the GCC region is expected to see modest recovery in the near term and growth is expected to average at 2.5% over 2021-2023. For the corporates, Fitch ratings said that 2021 outlook for GCC corporates is stable reflecting the stability in oil prices and better GDP growth in 2021 vs. 2020.

GCC - Key Central Bank Rates vs. US Fed Fund Rate

Dates	Kuwait CB Disc Rate	UAE Repo Rate	KSA Repo Rate	Bahrain ON Repo Rate	Qatar Repo Rate	Oman CBO Repo Rate	US Fed Fund Rate
Dec-17	2.75	1.75	2.00	3.50	2.50	2.06	1.25 - 1.5
Dec-18	3.00	2.75	3.00	4.50	2.50	3.01	2.25 - 2.5
Dec-19	2.75	2.00	2.25	4.00	2.00	2.28	1.5 - 1.75
27-Dec-20	1.50	0.60	1.00	2.25	1.00	0.50	0 - 0.25
1-Yr Change (%)	-1.25	-1.40	-1.25	-1.75	-1.00	-1.78	-1.5
2-Yr Change (%)	-1.50	-2.15	-2.00	-2.25	-1.50	-2.51	-2.25

GCC - Sovereign Credit Ratings Profile

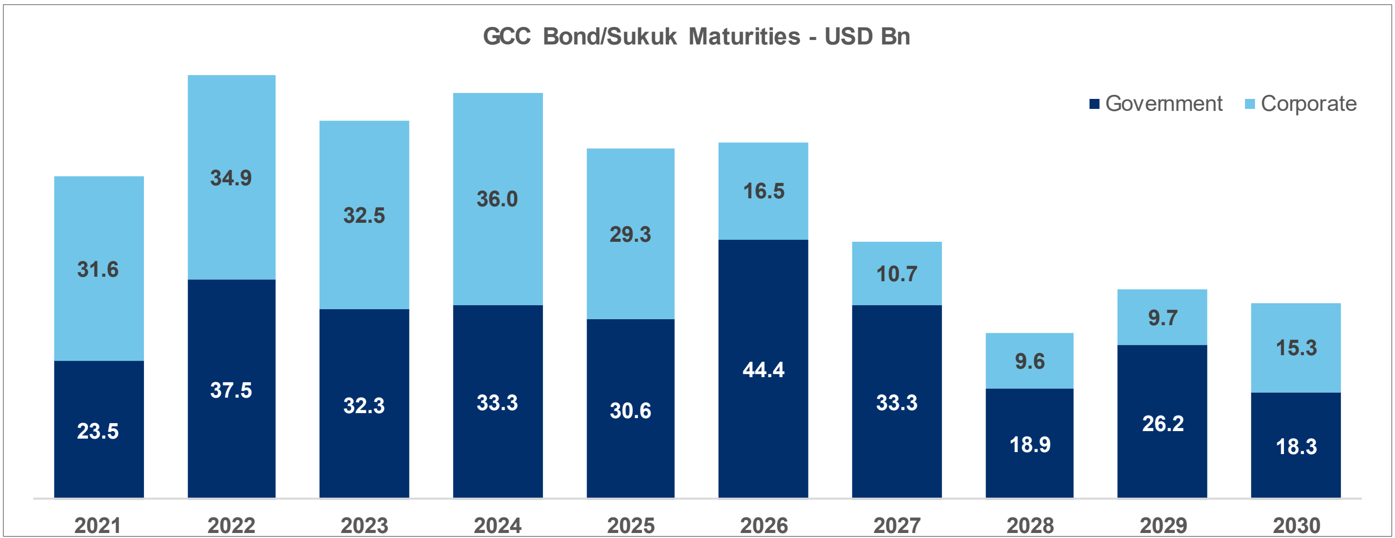
	S&P		Moody's		Fitch	
	Rating	Outlook	Rating	Outlook	Rating	Outlook
Bahrain	B+	STABLE	B2	STABLE	B+	STABLE
Kuwait	AA-	NEG	A1	STABLE	AA	STABLE
Oman	B+	STABLE	Ba3	NEG	BB-	NEG
Qatar	AA-	STABLE	Aa3	STABLE	AA-	STABLE
Saudi Arabia	A-	STABLE	A1	NEG	A	NEG
UAE	NR	NR	Aa2	STABLE	AA-	STABLE
Abu Dhabi	AA	STABLE	Aa2	STABLE	AA	STABLE

Sources : Bloomberg, Kamco Invest Research

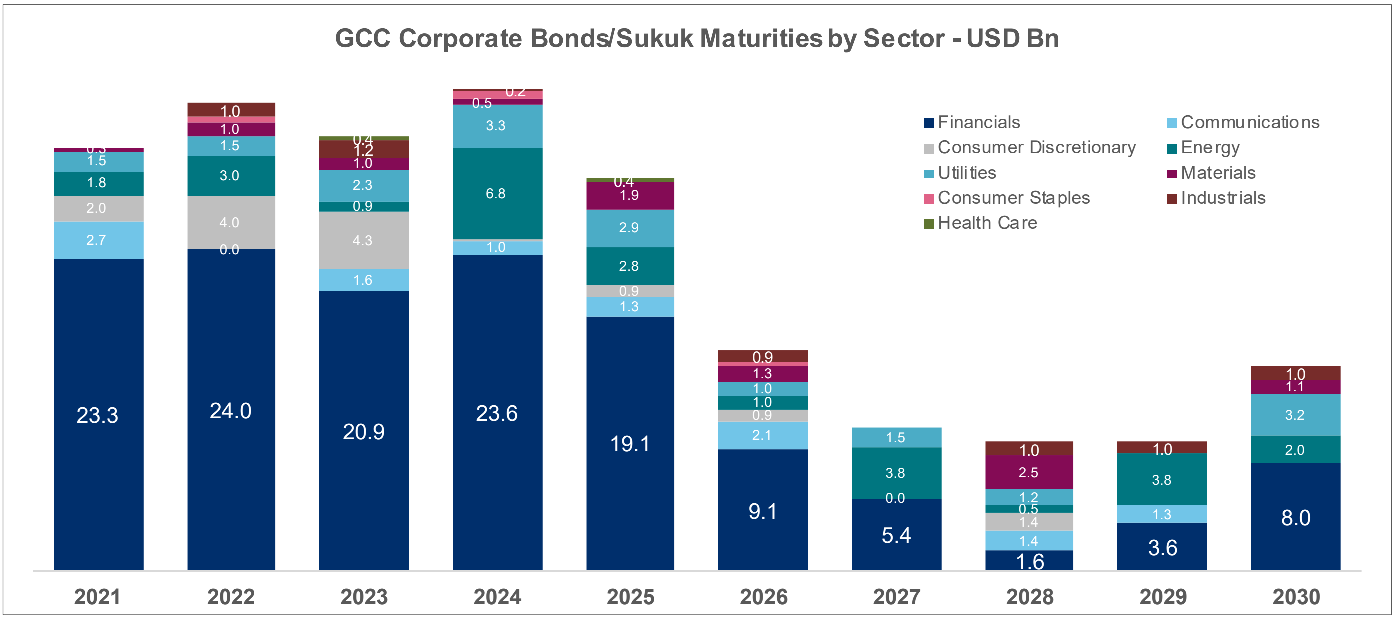
In terms of interest rates, key policy rates in the GCC have remained stable over the last six months after witnessing cuts across the board ranging from 125 bps to 175 bps during 1H-2020. These cuts mainly followed US Fed rate cuts that were implemented to support economic growth post the negative impact of the pandemic. Meanwhile, GCC currency pegs remains largely stable following expectation of stable oil prices in 2021 as well as prudent reforms implemented by the governments across the region.

Bond/Sukuk Maturities

GCC governments are expected to see USD 157.1 Bn in fixed income maturities over the next five years (2021-2025) whereas corporate maturities stand at USD 164.3 Bn. A majority of these maturities are denominated in USD at 61.3% followed by local currency issuances in SAR and QAR at 17.8% and 7.6%, respectively. In addition, due to the credit rating profile of the GCC governments, a majority of these maturities are in the high investment grade or A rated instruments. In terms of type of instruments, conventional bonds dominate with USD 205.7 Bn in maturities over the next five year whereas sukuk maturities are expected to be at USD 115.7 Bn. While bond maturities shows a declining trend over the next five years, sukuk maturities are expected to increase starting from 2022.



Sources : Bloomberg, Kamco Invest Research



Sources : Bloomberg, Kamco Invest Research

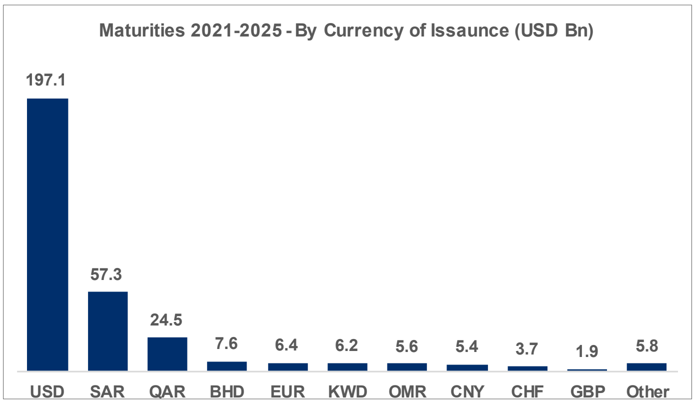
In terms of country split, UAE has the biggest share of upcoming maturities until 2025 at USD 99.2 Bn closely followed by Saudi Arabia and Qatari issuers at USD 97.1 Bn and USD 72.4 Bn, respectively. Loan maturities in the GCC region is also almost at the same level over the next five years as bonds and sukuk at USD 299.3 Bn. UAE corporates account for the bulk of the scheduled repayments over the next five years at USD 131.0 Bn followed by Saudi Arabian and Qatari corporates with scheduled repayments of USD 100.4 Bn and USD 28.6 Bn, respectively.

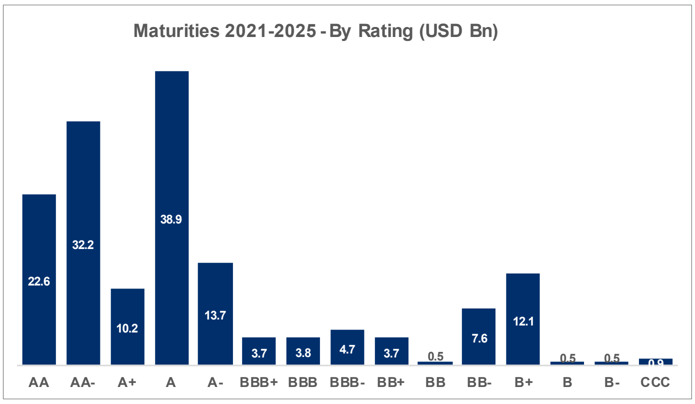
In terms of sector maturities, Banks and other Financial Services sector have USD 98.0 Bn in maturities in the next five years, accounting for around 60% of the total corporate maturities and 30.5% of the total maturities in the GCC until 2025. The Energy sector was next with maturities of USD 15.3 Bn or 9.3% of GCC corporate maturities until 2025 followed by Utilities and Airlines at USD 11.4 Bn and USD 11.2 Bn, respectively. Banks in UAE have the biggest maturities over the next five years at USD 45.4 Bn followed by Qatar at USD 26.4 Bn. Banks in the two countries accounted for 22.3% of total bond/sukuk maturities over the next five years in the GCC. Real Estate maturities are concentrated mainly in the UAE and Saudi Arabia at USD 6.9 Bn and USD 2.2 Bn, respectively, until 2025.

The structure of maturities are also changing gradually as an increasing number of issuances are perpetual instruments. According to data from Bloomberg, perpetual issuances have seen growth for the fourth consecutive year in 2020. Issuances reached record levels during the year at USD 6.2 Bn as compared to USD 5.5 Bn in 2019. Adding maturities beyond 30 years or from 2050 onwards, the issuances totaled USD 39.6 Bn in 2020 vs. USD 9.9 Bn in 2019, also a record during the year.

Outlook

GCC bond and sukuk issuances witnessed y-o-y gains for the second consecutive year in 2020 and trends for the coming year shows flat to slight decline in issuances in 2021. We believe that the year 2020 was an exceptional year with extreme events like the steep fall in economic growth rates across the globe and in the GCC as well as the historic decline in oil prices that particularly affected the oil exporting economies in the GCC. Budget spending needs by the government is expected to drive sovereign issuances next year. However, with a significantly smaller expected deficits of around USD 84.3 Bn in 2021 as





Sources : Bloomberg, Kamco Invest Research against USD 127 Bn in 2020, according to data from IMF, we expect government issuances to decline y-o-y in 2021. A number of GCC governments have announced a cut in spending next year and to focus on priority projects. Meanwhile, issuances from Kuwait could be a game changer for the region in 2021 if the government passes the debt law. Kuwait completely stayed away from the bond market in 2020 as the parliament failed to renew the debt law.

On the other hand, corporate issuances are expected to fully or partly offset the decline in issuances by governments as better economic environment is expected to result in higher spending by the private sector. Moreover, borrowers are also keen on raising funds due to the low cost of borrowing globally. In addition, with yield on sovereign bonds reaching an all time low, governments may be motivated to issue new debt and lock in the low cost of debt.

Meanwhile, with four out of the six GCC countries having comfortable investment grade ratings and the assumed support from the group to Oman and Bahrain, we believe this should support and enable raising funds in the region as well as internationally. Moreover, the sizable sovereign wealth funds for a majority of the sovereigns in the region support the overall credit ratings profile.

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Kamco Investment Company - K.S.C. (Public)
Al-Shaheed Tower, Khalid Bin Al-Waleed Street- Sharq
P.O. BOX : 28873, Safat 13149, State of Kuwait
Tel: (+965) 2233 6600 Fax: (+965) 2249 2395
Email : research@kamcoinvest.com
Website : www.kamcoinvest.com