GCC Fixed Income Weekly

July 26 2020

ADCB ASSET MANAGEMENT LIMITED

GCC Fixed Income Weekly Review

Global bond markets posted another week of positive returns, taking the year-to-date returns of Barclays Global Aggregate Index to 5%. The week was fairly mixed in terms of risk appetite with optimism on vaccine progress, passage of EU recovery fund being offset by the lack of agreement on further US fiscal stimulus, rise in US-China tensions and pick-up in initial jobless claims. US IG and HY sectors gained, benefitting from lack of supply activity. The long-dated UST yields fell, on expectation that Fed could boost purchases of 20yr and 30yr bonds. In Europe, periphery bond yields declined, in particular Italy, with the EU passing historical EUR750bn stimulus plan.

Risk taking was evident in fixed income with positive gains recorded in EM bonds. The total return analysis signals increased appetite for high-yielding low rated bonds. Within GCC, Oman was the best performer with other GCC countries also posting positive weekly returns.

CDS spreads across GCC tightened with the oil prices gaining traction in the beginning of last week. In the USD sovereign bond market, bond yields edged lower across all GCC with Oman and Bahrain recording the largest drop in yields. This reflects the hunt for yield amidst fixed income investors in spite of mixed risk sentiment. Kuwait and Dubai registered the lowest decline in bond yields. The former saw a rating outlook downgrade by S&P ratings agency recently, yet the reaction of the bond markets was muted compared to the sell-off in the country's stock markets. The Kuwaiti bond market's resilience may have to do more with lack of availability of liquid bonds and less with the country's fundamentals. The country's finance ministry has been pushing to pass debt law, which would allow the government to borrow USD65bn. On the other hand, Saudi's Finance Minister (FM) revealed its plans to widen scope of privatisation to include sectors which were not previously targeted for privatisation. The FM also sounded relatively more optimistic on growth, anticipating a lower growth contraction than the 6.8% contraction estimated by the IMF.

Country	Saudi Arabia	Abu Dhabi	Dubai*	Kuwait	Bahrain	Oman	Qatar	Egypt
Moody's	A1	Aau2	Baa1	Aa2	Ba2	Ba3	Aa3	B3
S&P	A-	AA	-	AA-	B+	BB-	AA-	B
Fitch	A	AA	-	AA	BB-	BB	AA-	B+

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GCC Fixed Income Weekly Snapshot

Bond Index Snapshot (Emerging market and GCC)

BBG Barclays*	Latest	-1w %	YTD %
EM USD Agg TR	1,233.6	1.1	2.0
EM LatAm TR	1,021.9	1.3	-1.8
EM EMEA TR	382.6	1.0	2.6
EM Asia TR	661.2	1.0	4.3
Bahrain TR	166.9	1.2	-0.9
Oman TR	114.5	2.1	-4.2
Kuwait TR	144.7	0.3	3.9
Qatar TR	147.3	1.0	8.5
Saudi Arabia TR	148.8	1.1	8.5
UAE TR	142.0	1.1	5.0
5Y Sov. CDS	**Latest (bp)**	**-1w (bp)**	**YTD (bp)**
Saudi Arabia	91.0	-14.5	33.9
Abu Dhabi	56.3	-6.5	19.5
Dubai	196.9	-8.6	100.1
Kuwait	65.0	-0.2	25.5
Bahrain	349.66	-13.0	163.5
Oman	486.3	-12.5	238.2
Qatar	54.4	-6.2	17.1
Egypt	455.1	-15.7	163.6
Turkey	500.6	-35.5	216.7
US	23.4	-0.5	8.0
Germany	13.6	-2.0	-

Interest rates (Sunday to Thursday)

3M interbank	Latest	-1w (bp)	YTD (bp)
Saudi	0.94	-1.72	-129.43
UAE	0.55	-2.75	-156.36
Kuwait	1.56	0.00	-118.75
Bahrain	2.30	0.00	-36.67
Oman	2.69	0.75	-14.70
Qatar	1.00	-4.82	-126.60
US	0.24	-2.73	-162.78
12M interbank	**Latest**	**-1w (bp)**	**YTD (bp)**
Saudi	1.04	-1.57	-127.72
UAE	1.10	-13.17	-122.00
Kuwait	2.13	0.00	-106.25
Bahrain	2.68	0.00	-15.00
Oman	3.35	0.50	-3.75
Qatar	1.31	0.08	-131.98
10Y yield	**Latest**	**-1w (bp)**	**YTD (bp)**
Saudi Arabia	2.10	-8.10	-106.80
Abu Dhabi	1.58	-13.30	-98.00
Dubai	2.94	-3.10	-30.90
Kuwait	1.37	-3.10	-102.60
Bahrain	5.22	-38.70	61.40
Oman	6.82	-48.00	126.50
Qatar	1.68	-15.20	-91.90

*Note: *Dewa rating used as proxy*

Saudi's FM expects lower growth contraction than IMF and points recent data signaling economic recovery
Saudi Arabia's Finance Minister expects shrink in growth to be less than the 6.8% predicted by the IMF. The FM stated that the recent economic data looks promising, though uncertainties remain. Saudi Arabia issued more local debt this year and spending in the budget will likely not changed, but some of the sectors will be reallocated. The FM said that whatever support the country needed will be provided to ensure the economic recovery. On introducing income taxes, the FM said that such a measure calls for more planning and stressed there was no imminent plan for introducing it.

Saudi's FM announces plans of privatization
Saudi Arabia is planning to sell assets in sectors that are currently not privatized, in order to ease the impact of continuously low oil prices. The FM mentioned that the sectors such as healthcare and education, which have not been previously targeted for privatization, are being considered. He also stated that revenue from privatization could generate more than SAR50bn during the next 4 – 5 yrs.

Saudi's central bank governor anticipates deeper contraction in 2Q economy deteriorated by 1%
Saudi's central bank governor said that the economy may have contracted further in the second quarter than the first quarter, in spite of the pickup seen in June. Saudi Arabia's GDP had contracted by 1% in the first quarter, driven by the impact of the Covid-19 pandemic and the decline in oil prices.

S&P ratings expects GCC corporates to delay investments
S&P ratings agency stressed that GCC corporates could delay investments in a bid to manage costs and liquidity and further indicated that recovery could take at least few more quarters. The rating agency has taken sixteen rating actions this year so far on the GCC corporates. GCC corporates will be reviewing their operating costs and amidst revenue challenges could resort to further pay and job cuts. The contraction will be broad based across sectors but certain sectors could face more pressure with deceleration in economic activity. Aviation and tourism sector have been the worst-impacted, specifically in Dubai. Dubai real estate sector is likely to remain under extreme pressure, explaining the recent downgrade to junk status on two largest property firms in Dubai.

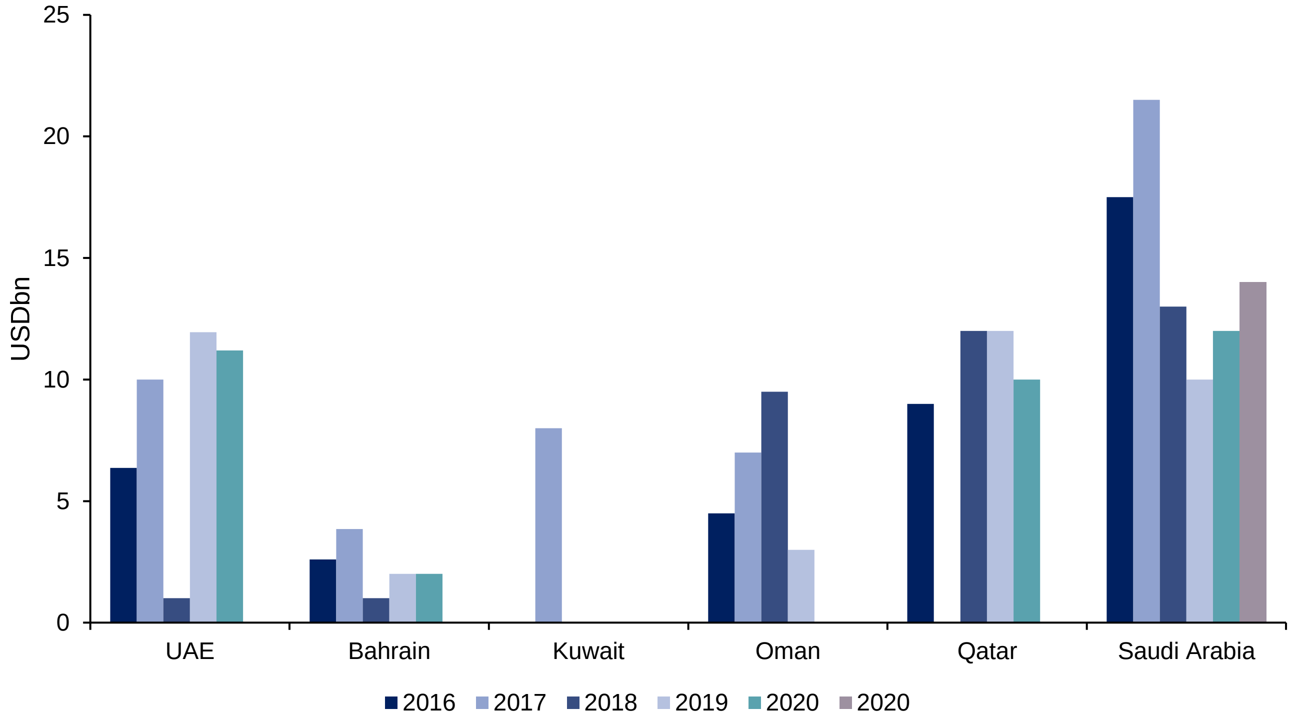
S&P rating states GCC corporates effectively manage liquidity, however oil prices and Covid-19 risks are looming
S&P ratings stated that GCC corporates have successfully managed their liquidity during the Covid-19 outbreak in spite of a very weak operating environment. However the rating agency further cautioned that the severe impact of global credit downturn has lowered the recovery rate of many sectors in the economy, thus causing negative employment trends and consumer spending. The rating agency forecasts a mid to high single digit real GDP contraction for the GCC countries this year and weak operating conditions for the following quarters.

S&P ratings expects GCC governments to increase their borrowings by a record-high of USD100bn this year
According to S&P ratings, the Covid-19 pandemic coupled with low oil prices, will result in governments in the GCC region to boost their borrowings by a record-high of approximately USD100bn this year. The rating agency expects GCC balance sheets to remain under pressure till 2023, with deficits likely to reach about USD490bn cumulatively between 2020 and 2023.

IMF says that this is not the right time for GCC to increase taxes
The IMF indicated that the current situation in GCC is not conducive for raising taxes on consumption and introducing taxes on sectors that are crucial for growth recovery. The Fund's economist chief said that instead of increasing taxes, the region should focus on improving the efficiency of the tax system. The tax system in the region can be improved by being more progressive, especially given the rising income disparity in the region.

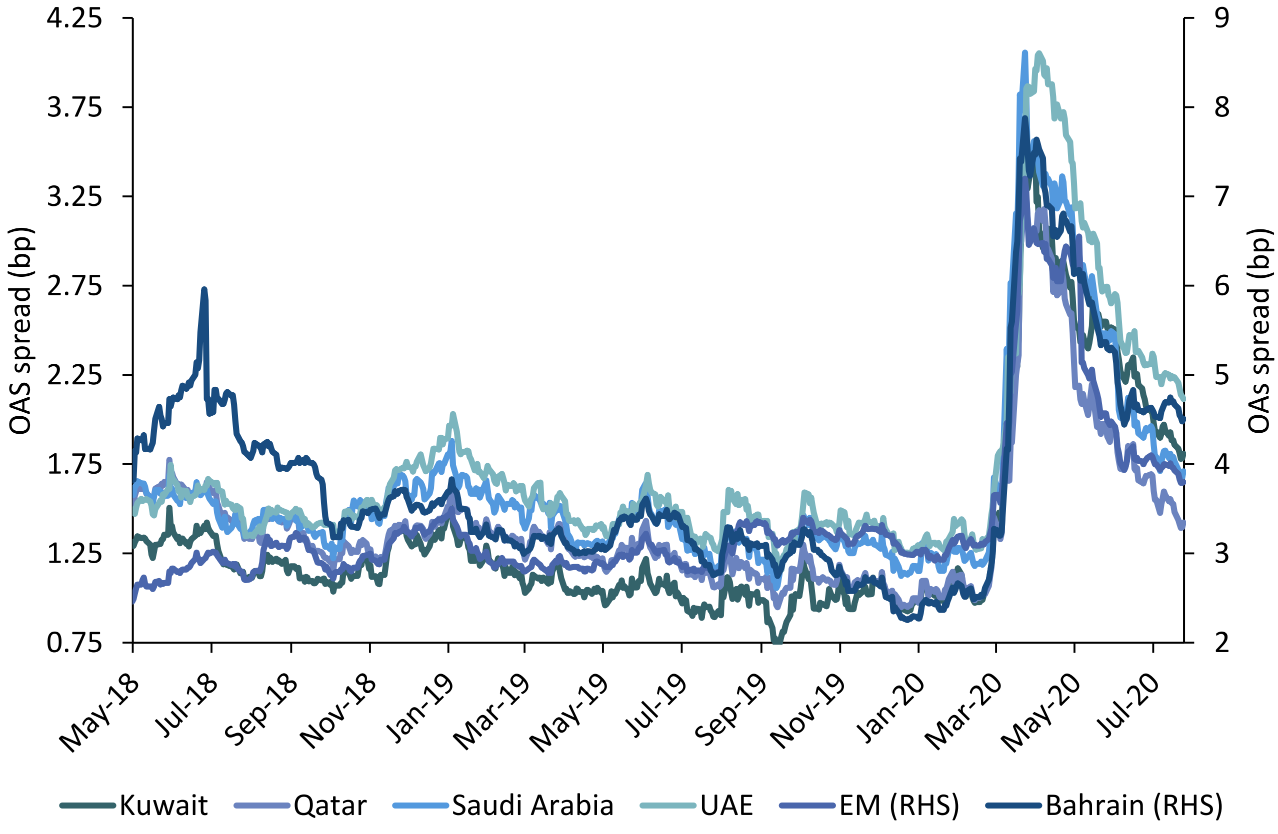
Appendix

Saudi Arabia to borrow USD14bn more in 2020



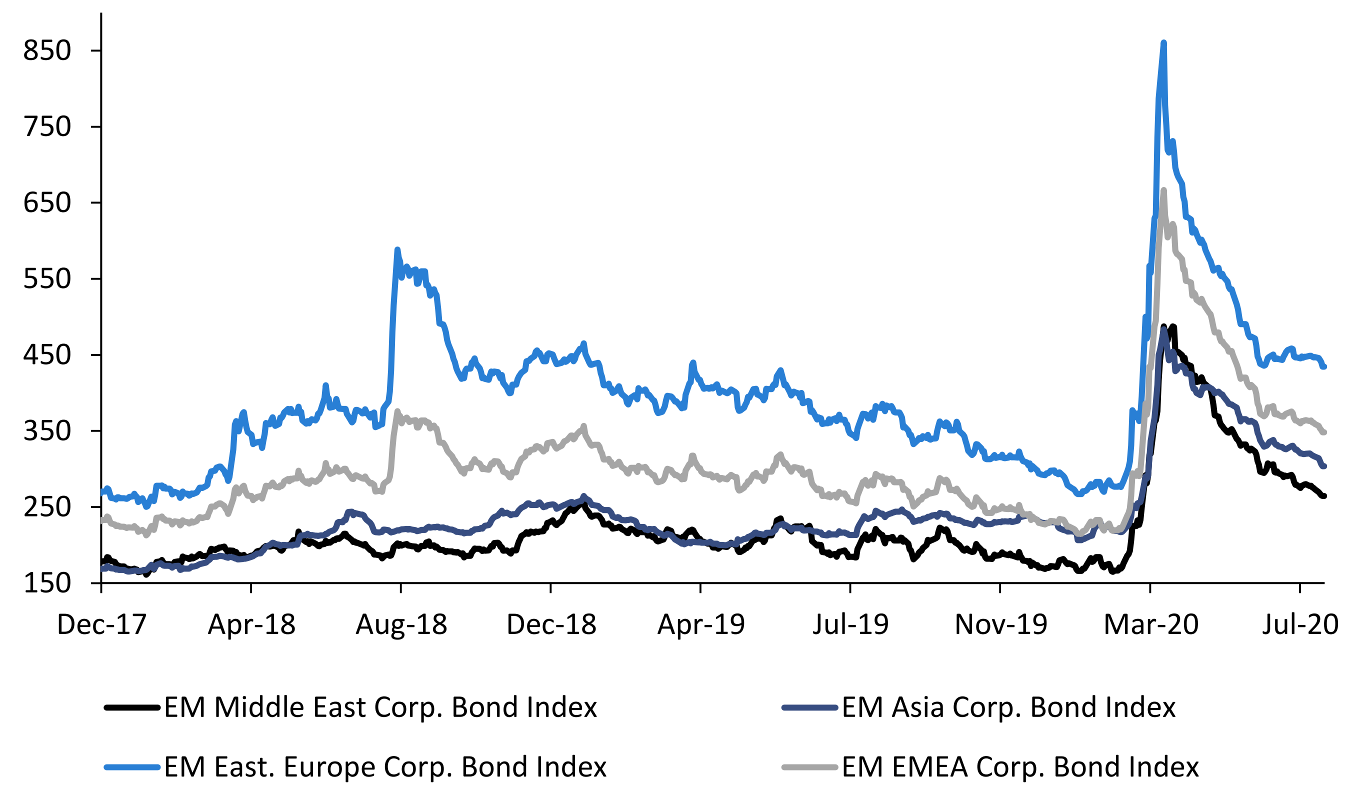
Source: Bloomberg, ADCB

Bloomberg Barclays Bond Indices OAS spread (EM vs GCC)



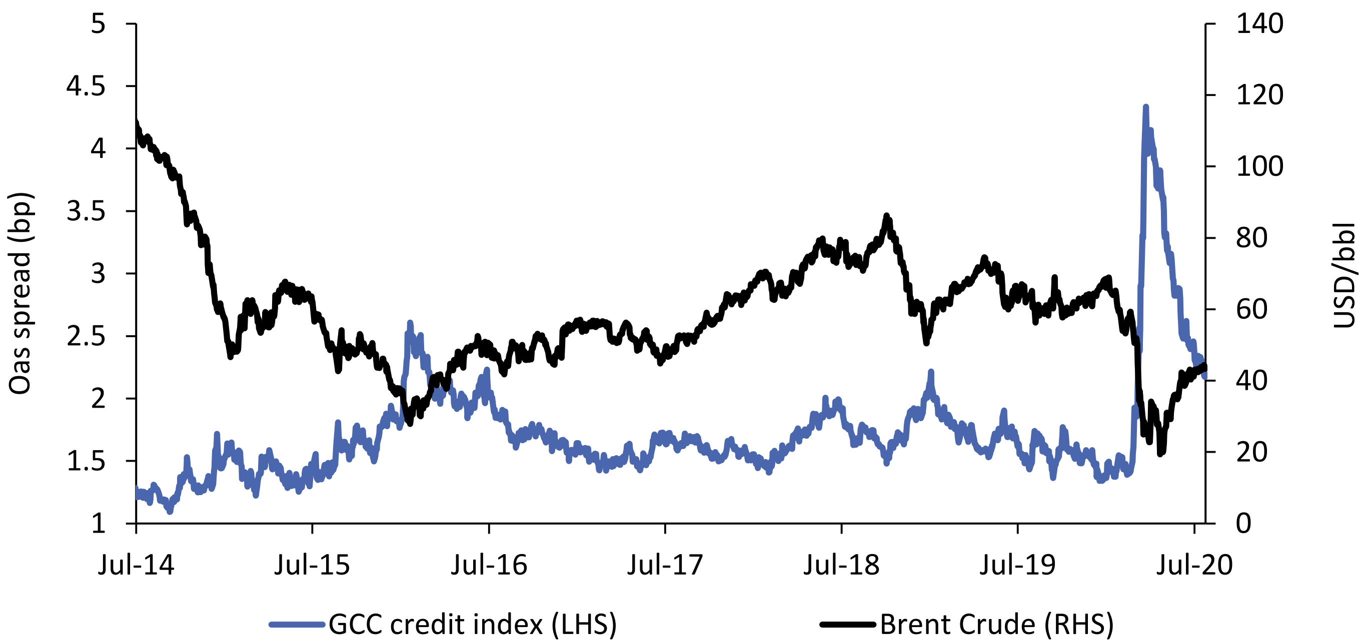
Source: Bloomberg Barclays Sovereign Bond Indices, ADCB

Emerging markets versus Middle East spread



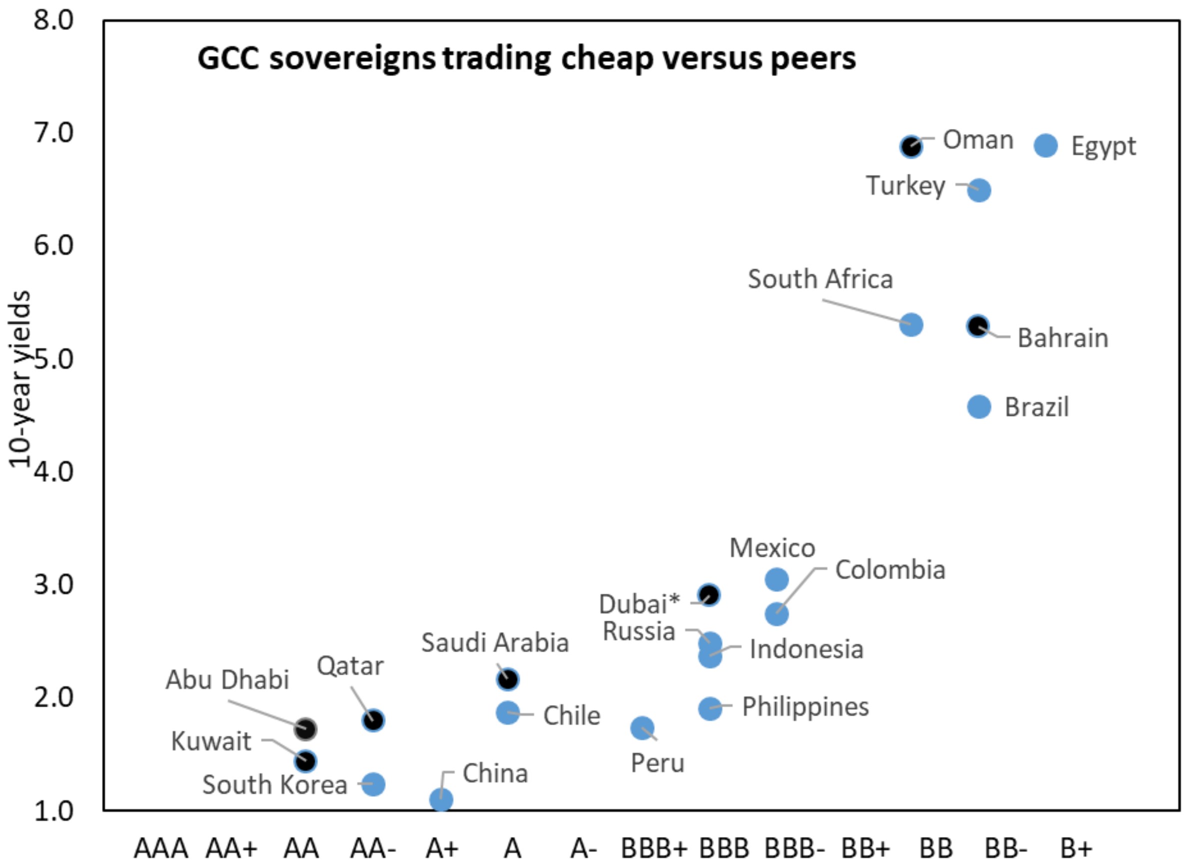
Source: Credit Suisse Corporate Bond Indices, ADCB

GCC corporate OAS spread versus Brent Crude



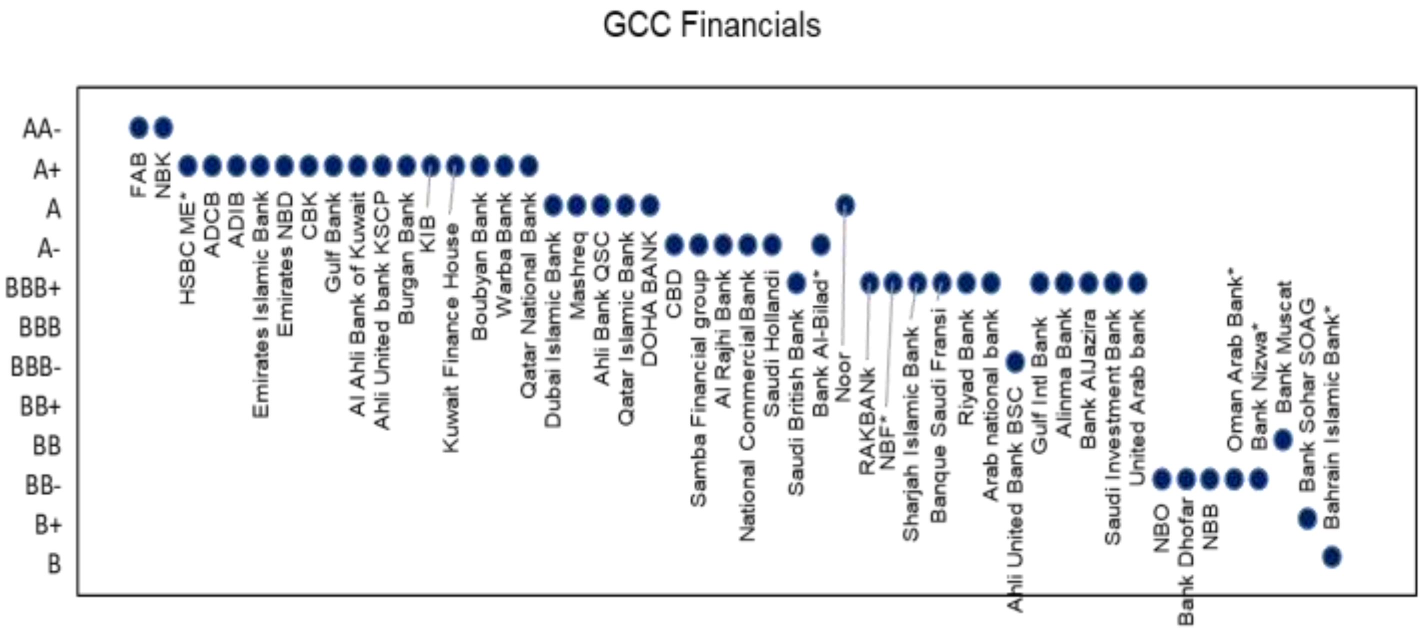
Source: Bloomberg, ADCB

10yr yield versus Credit ratings (EM vs GCC)



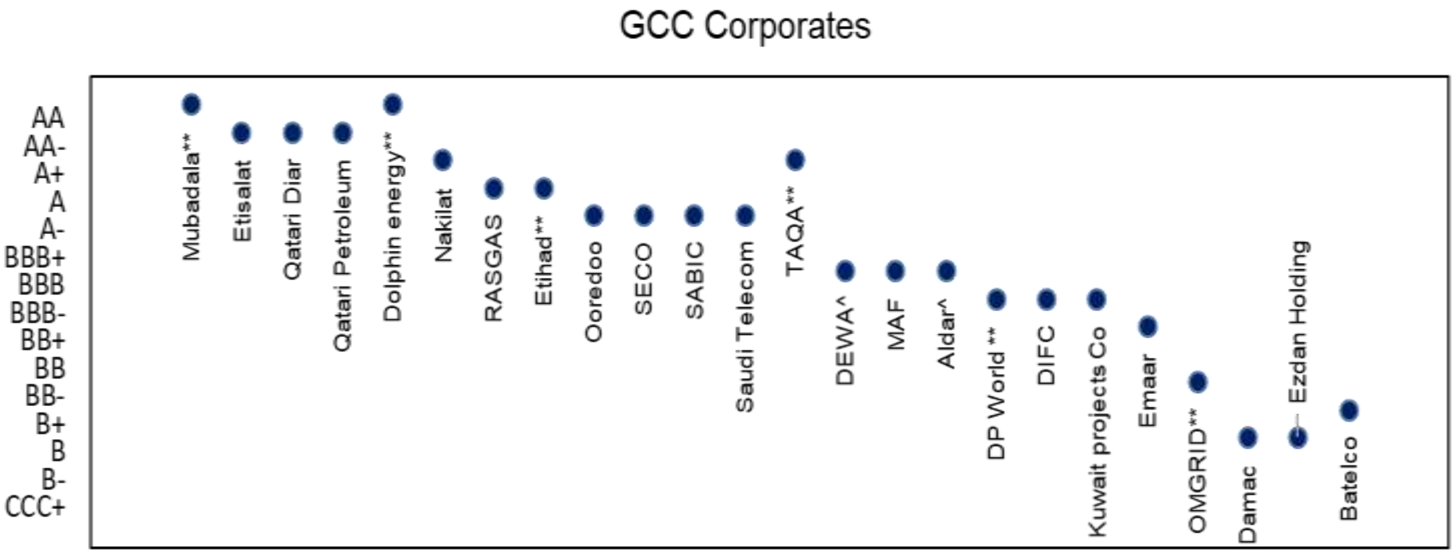
Source: Bloomberg, ADCB, *Dewa rating used as a substitute for Dubai, Fitch ratings are used for all countries

GCC Financials Credit Rating



Note: The ratings refer to Fitch ratings, *S&P rating used as substitute where the corporate/bank not rated by Fitch rating
Source: Bloomberg, ADCB

GCC Corporate Credit rating



Note: The ratings refer to S&P ratings, ** Fitch ratings used as substitute where the corporate/bank not rated by S&P ratings, ^ refers to Moody’s ratings Source: Bloomberg, ADCB

Sources

All information in this report has been obtained from the following sources except where indicated otherwise:

1. Bloomberg
2. Wall Street Journal
3. RTT News
4. Reuters
5. Gulfbase
6. Zawya

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