Special Report on MENA Bonds and Sukuk Market

NBK Capital: MENA sovereign bonds and sukuk constitute 20% of EM index

GCC debt market on track for its best yearly performance in a decade

KUWAIT: The GCC international bond market is on its way to post its best performance since 2010. As of end-August 2019, the Bloomberg Barclays GCC Index, which tracks bonds and Sukuk issued by GCC entities rated as investment grade, was up 15.2 percent on a year-to-date basis. A large part of this extraordinary performance resulted from the sharp drop in yields globally. It is also the direct result of changes in the US monetary policy, whereby cuts in the Fed benchmark rates are transmitted to all US dollar denominated assets. In essence, the drop in yields on US treasuries, whether from interest rate cuts or changes in economic outlook, lifts the price of USD bonds due to the inverse relationship between interest rates and bond prices.

Furthermore, the GCC region's performance stands out from similarly rated global peers. For example, the US investment grade corporate bonds index1 rose 13.9 percent and the Emerging Markets (EM) investment grade index2 rose 13.3 percent over the same period, a whole 1-2 percentage points lower than the GCC market. It is worth noting that this outstanding relative performance happened in spite of heightened geopolitical tensions in the region and stagnant oil prices, and came largely on the back of J.P. Morgan's decision to include five GCC countries into its flagship EM Index, the Emerging Markets Bond Index Global (EMBIG)

A strategic asset class

Following last year's decision by J P Morgan to include five GCC countries into its flagship EM Index, the EMBIG, the total weight of the GCC increased to 15 percent, bringing the total weight of the MENA region in the index to around 20 percent. The inclusion translated into large inflows into the region's debt capital market, with estimates ranging from $25 to 30 billion. This additional demand helped compress GCC spreads, and pushed performance of the regional market to exceed that of it global peers. The J P Morgan EMBIG Index suite was created nearly 20 years ago as growing investor demand for EM debt motivated the need for a broad benchmark. It is considered the most widely tracked index by EM debt investors. The GCC inclusion came as a recognition of the growing size and hence relevance of the market. This makes it hard to overlook the region by any well-diversified multi-asset global portfolio going forward. The inclusion has additional positive consequences. With greater participation from foreign investors, the investor base of the regional debt market becomes broader. This enhances the market's ability to absorb a significant increase in bond issuance with relatively limited price distortion.

A market poised to grow

There is a wide market consensus that, over the foreseeable future, bonds and Sukuk issuances in the region will remain elevated given the mismatch between budgetary revenues and expenditures. Fiscal deficits have widened as many GCC economies embarked on ambitious capital expenditure programs to boost economic growth, and engaged in bold steps to diversify their economies away from oil. These steps led to an increase in borrowing-encouraged by low-interest environment-and in the total stock of debt.

Sukuk issuances are also on the rise, as economies seek to diversify their funding mix and develop the Islamic debt

market. Sukuk issuances in the international dollar market amounted to around 20 percent of the total GCC issuances in the last two years, up from 15 percent in 2016. Around USD 45 billion worth of Sukuk were issued since 2017. Looking ahead, one of the main challenges for regional economies will be to balance the need for public spending with debt sustainability. The average debt level of GCC economies measured against their GDP increased over the past three years, but still remains lower than developed countries.

NBK ECONOMIC REPORT

Oil prices drop below $60 as global growth concerns rise

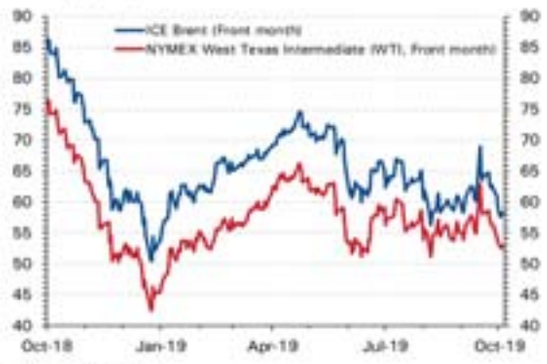
KUWAIT: September closed with oil prices trading at or below where they were on the eve of the missile strike on Saudi Arabia's oil infrastructure. International crude benchmarks Brent and West Texas Intermediate (WTI) ended the month at $60.78 (+0.68 percent mtd; +13 percent ytd) and $54.1/bbl (-1.9 percent mtd; +19.1 percent ytd), respectively. Having given up all their gains accrued in the aftermath of the attack on Saudi's Abqaiq/Khurais oil processing center, both oil markers have since fallen further, with Brent breaching the $60 barrier to close at $58.4.bbl by the end of the first week of October. This was the marker's lowest level since August.

Once again, concerns about the health of the global economy-and by implication oil demand-have come to the fore, fueling the bearish sentiment. The latest setback for oil was triggered by weaker-than-expected US manufacturing and employment data. This, allied to the news that the US had opened another front in its trade war, by slapping tariffs on European exports, to go along with those measures already imposed on China, has only reinforced the narrative of a weakening global economy.

Geopolitics strikes back, briefly

The 14 September drone attacks on Saudi Arabia's Abqaiq oil and gas processing facility and Khurais oil field knocked out 5.7 mb/d of Saudi crude production, close to half of the kingdom's production capacity, and 5 percent of global oil supplies. The international community has blamed Iran for the attacks, even though the Houthis claimed responsibility. When the oil markets reopened, Brent spiked by more than 20 percent, from $60.22 to $71.95 in intraday trading before paring back gains to $69 by Monday's close. Geopolitical risk, of minimal concern in the era of burgeoning US shale supplies, was seemingly back with a vengeance, as markets woke up to realization that the infrastructure of one of the world's most important oil suppliers was vulnerable

Chart 1: Benchmark crude oil prices
($/bbl)



Source: Refinitiv

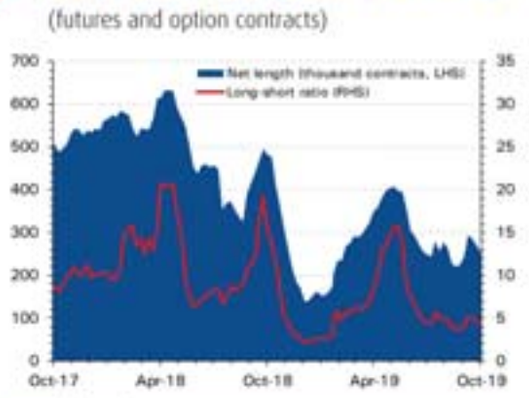
to disruption from foreign forces. And two-thirds of the world's entire crude production buffer-oil that could be pumped at short notice to offset supply losses elsewhere-was tied up in Saudi Arabia's 2.3 million barrels of spare crude production capacity.

However, supply outage concerns proved relatively fleeting; Brent fell 6.5 percent to $64.6/bbl by the close of the second trading session and fell in eight of the next thirteen sessions. Reasons for the sell-off are various: concerns over the length of the disruption were allayed by Saudi reassurances that production would be up to speed relatively quickly-within two days Abqaiq had recovered 43 percent (2 mb/d) of its production and within three weeks' Saudi output was back up to 9.9 mb/d, according to the Energy Minister; the Saudis moved quickly to reassure export customers that it possessed sufficient crude stocks (188 mb, equivalent to 28 days of export cover) with which to honor contract deliveries; various energy agencies and houses weighed in by confirming that global crude supplies in storage provided ample short term cover; and lastly a de-escalation in the rhetoric surrounding the incident by the international community even while the US proceeded to tighten sanctions on Iran.

Demand growth to decelerate

The IEA has left unchanged its oil demand growth forecast for 2019 and 2020 at 1.1 mb/d and 1.3 mb/d, respectively. The first six months of 2019 saw one of the

Chart 3: Brent money manager net length
(futures and option contracts)



Source: Bloomberg

weakest first halves of demand growth (0.5 mb/d) since 2008, amid deteriorating global trade relations. Global commercial crude stocks (OECD stocks) continue to trend higher, increasing for the fourth consecutive month to reach 2,931 mb in July. Stock levels are at their highest in almost two years and 19.7 mb above the 5-year avg, which is one of OPEC's targets.

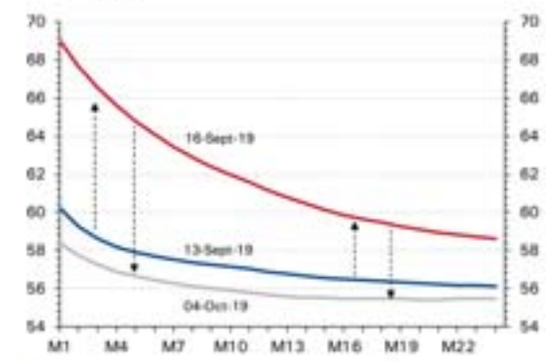
OPEC+ compliance down

OPEC+ compliance fell to 116.5 percent in August from 142.5 percent in July, with Russia, Saudi Nigeria and Iraq among those producers increasing output. Nevertheless, August was the second month in a row that both OPEC and its non-OPEC partners recorded above 100 percent compliance. The combined output cut was 1.4 mb/d, 200 kb/d more than mandated by the Vienna agreement. For Saudi-led OPEC-11, production increased in August by 225 kb/d to 25.78 mb/d, bringing compliance down to 120.3 percent from 148 percent in July. OPEC compliance in September-when that data is released later this month-should increase due to the impact of the drone attacks on Saudi Arabian production.

Demand side worries

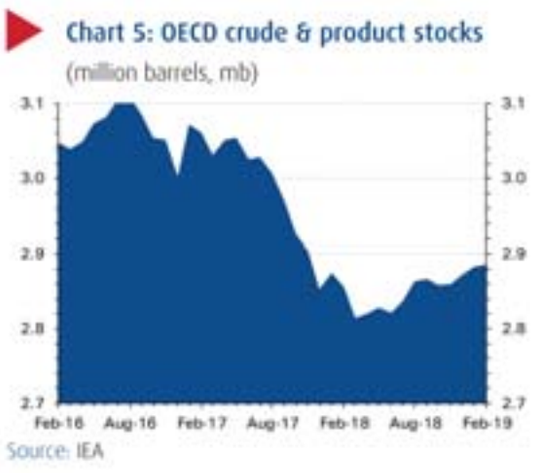
In the markets' risk assessment, geopolitics has been deemphasized in favor of global economic growth concerns. In their reasoning, in a world plainly still awash in oil, the threat posed by weakening global economic and oil demand fundamentals should assume greater importance than the threat to global oil supplies posed by supply outages. The downward movement in oil prices has, therefore, reflected that. While the assessment seems reasonable in view of rising global trade frictions and faltering economic data coming out of Europe and the OECD, geopolitical risks are present. It appears unlikely that geopolitical risk-related oil volatility will subside without some kind of movement on or resolution to the vexed issue of the Iran nuclear agreement.

Chart 2: Brent forward curve to 24 months
($/bbl)



Source: Bloomberg; note: x-axis denotes forward months

Chart 5: OECD crude & product stocks
(million barrels, mb)



Source: IEA

EXCHANGE RATES

AL-MUZAINI EXCHANGE CO.

EUROPEAN & AMERICAN COUNTRIES

US Dollar Transfer	304.750
Euro	336.600
Sterling Pound	376.060
Canadian dollar	230.170
Turkish lira	54.420
Swiss Franc	309.080
US Dollar Buying	297.350

ASIAN COUNTRIES

Japanese Yen	2.841
Indian Rupees	4.286
Pakistani Rupees	1.962
Srilankan Rupees	1.682
Nepali Rupees	2.682
Singapore Dollar	221.800
Hongkong Dollar	38.861
Bangladesh Taka	3.595
Philippine Peso	5.880
Thai Baht	10.070
Malaysian ringgit	77.941

GCC COUNTRIES

Saudi Riyal	81.321
Qatari Riyal	83.757
Omani Riyal	792.073
Bahraini Dinar	809.750
UAE Dirham	83.027

ARAB COUNTRIES

Egyptian Pound - Cash	21.100
Egyptian Pound - Transfer	18.725
Yemen Riyal/for 1000	1.224
Tunisian Dinar	112.870
Jordanian Dinar	430.290
Lebanese Lira/for 1000	0.203
Syrian Lira	0.000
Morocco Dirham	31.944

DOLLARCO EXCHANGE CO. LTD

Rate for Transfr	Selling Rate
US Dollar	304.740
Canadian Dollar	230.725
Sterling Pound	375.885
Euro	333.495
Swiss Frank	307.075
Bahrain Dinar	810.415
UAE Dirhams	83.370
Qatari Riyals	84.610
Saudi Riyals	82.160
Jordanian Dinar	431.105
Egyptian Pound	18.729
Sri Lankan Rupees	1.672
Indian Rupees	4.308
Pakistani Rupees	1.949
Bangladesh Taka	3.609
Philippines Pesso	5.872
Cyprus pound	18.130
Japanese Yen	3.815
Syrian Pound	1.595
Nepalese Rupees	2.697
Malaysian Ringgit	73.635
Chinese Yuan Renminbi	43.065
Thai Bhat	10.935
Turkish Lira	54.365
Singapore dollars	220.536

BAHRAIN EXCHANGE COMPANY WLL

CURRENCY	BUY	SELL
EUROPE		
British Pound	0.364745	0.378645
Czech Korune	0.004927	0.014227
Danish Krone	0.040618	0.045618
Euro	0.326269	0.339969
Georgian Lari	0.102133	0.102133
Hungarian	0.000908	0.001098
Norwegian Krone	0.029195	0.034395
Romanian Leu	0.053306	0.070156
Russian ruble	0.004662	0.004662
Slovakia	0.009116	0.019116
Swedish Krona	0.026575	0.031575
Swiss Franc	0.299962	0.310962
Australasia		
Australian Dollar	0.196838	0.206838
New Zealand Dollar	0.185825	0.195325
America		
Canadian Dollar	0.223343	0.232343
US Dollars	0.300650	0.305950
US Dollars Mint	0.301150	0.305950
Asia		
Bangladesh Taka	0.002920	0.003721
Chinese Yuan	0.041264	0.044764
Hong Kong Dollar	0.036761	0.039511
Indian Rupee	0.003665	0.004437
Indonesian Rupiah	0.000017	0.000023
Japanese Yen	0.002757	0.002937
Korean Won	0.000244	0.000259
Malaysian Ringgit	0.069045	0.075045
Nepalese Rupee	0.002628	0.002966
Pakistan Rupee	0.001342	0.002112
Philippine Peso	0.005683	0.005983
Singapore Dollar	0.214991	0.224991
Sri Lankan Rupee	0.001321	0.001901
Taiwan	0.009672	0.010222
Thai Baht	0.009612	0.010222
Vietnamese Dong	0.000013	0.000013
Arab		
Bahraini Dinar	0.802203	0.810263
Egyptian Pound	0.018659	0.022019
Iranian Riyal	0.000084	0.000086
Iraqi Dinar	0.000215	0.000275
Jordanian Dinar	0.424927	0.433927
Kuwaiti Dinar	1.000000	1.000000
Lebanese Pound	0.000151	0.000251
Moroccan Dirhams	0.021230	0.045230
Omani Riyal	0.785427	0.794325
Qatar Riyal	0.083051	0.083885
Saudi Riyal	0.080180	0.081480
Syrian Pound	0.001292	0.001512
Tunisian Dinar	0.102628	0.110628
Turkish Lira	0.045604	0.055449
UAE Dirhams	0.082338	0.083166
Yemeni Riyal	0.000991	0.001071