# Cost of funding for GCC countries rose due to COVID-19: Markaz

## Bond prices dropped in March 2020

**KUWAIT:** Kuwait Financial Centre "Markaz", in its GCC Fixed Income research report for the first quarter of 2020, has highlighted the implications of the outbreak of COVID-19 on fixed income markets in the region. The report notes that the outbreak of the disease has significantly impacted global financial markets across all asset classes, pushing central banks and policymakers to intervene and provide wide-ranging economic stimulus measures in the face of worsening economic conditions. Within the global fixed income markets, the global pandemic event has resulted in elevated volatility and widened spreads. Aside from the pandemic, global markets witnessed a sharp drop in oil prices during March as well, placing further strain on oil-dependent economies, translating into further pressure on regional fixed income markets.

### Implications of coronavirus

The implications of the pandemic on regional fixed income markets were manifold. Regional fixed income indices were down for the first quarter of the year, whereas key sectors in the GCC experienced large sell-offs of Bonds and Sukuk and elevated spreads. Primary issuances of Bonds and Sukuk in the GCC witnessed weak activity in March as a result of the uncertainty surrounding the pandemic, leading to a meager quarter of primary debt issuances in 2020 in comparison with previous quarters. Moreover, Credit Default Swap (CDS) spreads, a measure largely regarded as an indicator of default for sovereign countries, spiked across all GCC countries during March. Finally, the pandemic event and the sharp decline in oil prices pushed credit rating agencies to downgrade both Kuwait and Oman on 31 March, citing deteriorating global economic outlook and falling oil prices.

**Performance of fixed income indices**

Initially, major leading global fixed income indices were up by the end of February, before witnessing sharp declines in March and wiping any gains for the year subsequent to the declaration of COVID-19 a pandemic by the World Health Organization (WHO). By the end of February 2020, the Bloomberg Barclays Global Aggregate was up 2 percent. Similarly, the Bloomberg Barclays GCC Aggregate, an index representative of fixed income securities of the 6 countries that form the Gulf Cooperation Council, was up 1 percent. Moreover, the Bloomberg Barclays Emerging Markets Aggregate was up 1 percent, whereas the Bloomberg Barclays US Aggregate and Pan-European Aggregate indices were up 4 percent and 2 percent, respectively. However, during March, the Bloomberg Barclays Global Aggregate fell by 2 percent, therefore ending the first quarter of the year at 0 percent return. In comparison, the Bloomberg Barclays GCC Aggregate was down by 9 percent ending the first three months of the year at a loss of 7 percent, while the worst-performing index was the Bloomberg Barclays Emerging Markets Aggregate index which lost 11 percent in March, to end the first quarter of the year with a total loss of 9 percent. The Bloomberg Barclays US Aggregate index is the only index up for the year, posting a return of +3 percent for the quarter, whereas the Bloomberg Barclays Pan-European Aggregate lost 4 percent in March, recording a loss of 1 percent for the first quarter of the year.

**Sector performance of GCC fixed income securities**

With few exceptions, all GCC bonds and Sukuk across sectors were negatively impacted as a result of the disruption caused by the coronavirus outbreak and the sharp drop in oil prices, a major source of revenue for the GCC countries. Among these, high yielding bonds and longer maturities witnessed the biggest decline in each sector; however, Consumer (Non-Cyclical), Oil and Gas, Real Estate and low rated Government bonds experienced the brunt of the impact. NMC Healthcare, based in the UAE, experienced the steepest decline in its 2025 bond and saw prices fall by 90.14 percent in the first quarter of the year as reports of fraudulent financial reporting emerged indicating inflated asset purchases and capital expenditures as well as understated debt. Borr Drilling witnessed the sharpest decline in the Oil and Gas industry as its 2023 bond witnessed a 74.4 percent decline in value during Q1 2020. The Emirates REIT witnessed the sharpest decline year-to-date in the Real Estate Industry as the value of its 2022 bond declined by 33.9 percent. Among GCC Sovereign bonds, Oman experienced the greatest decline in prices across different maturities as low oil prices are expected to strain the country's fiscal budget. As of Q1 2020, Oman's 2027 bond declined by 30.36 percent, 2029 bond declined by 31.07 percent and 2048 bond declined by 34.51 percent.

**Primary issuances of GCC bonds and sukuk**

During March 2020, the total primary issuances of Bonds and Sukuk in the GCC amounted to $5.4 billion, representing a decline of 75 percent from the total primary issuances of $21.5 billion achieved in March 2019. The decline in primary issuances represents a 4-year low and is largely as a result of the uncertainty surrounding the global pandemic event. During Q1-2020, primary issuances of Bonds and Sukuk in the GCC amounted to $26.2 billion, compared to $42.5 billion during the same period in 2019. This represents a decrease of 38 percent year-on-year.

Moreover, primary issuances by Sovereign GCC entities decreased by 65 percent year-on-year to reach $10.94 billion during Q1-2020, compared to $30.83 billion in Q1-2019. On the other hand, primary issuances by Corporate entities in the GCC increased by 31 percent year-on-year to reach $15.30 billion during Q1-2020, compared to $11.70 billion during the first quarter of 2019. However, the majority of Corporate issuances in the GCC during 2020 came in January and February, prior to declaring COVID-19 as a pandemic.

**GCC CDS spreads**

In March 2020, the 5-year CDS spreads have increased for all GCC countries reflecting a perception of higher credit for these countries. The halting of the global economy and the projected fall in future oil revenues are seen as adding further strain on the budgets of GCC governments, thus increasing the perceived risk of default. During March, Qatar saw its 5-year CDS spreads change from 49.010 bps to 128.745 bps, Abu Dhabi from 44.690 bps to 116.275 bps, and Dubai from 116.070 bps to 296.290 bps. Kuwait's 5-year CDS spread was priced at 41.735 bps at the beginning of March, which increased to reach 102.025 bps. Saudi Arabia's 5-year CDS spread was priced at 76.535 bps and increased to reach 175.400 bps at the end of the month. Moreover, Bahrain saw its 5-year CDS spreads increase from 201.195 bps to 475.295 bps during March, whereas Oman's 5-year CDS increased by from 324.585 bps to 662.595 bps during the same period.

**GCC yield curve**

Bond prices have an inverse relationship with yields; as bond prices increase, yields decrease and vice versa. During Q1 2020, GCC sovereign curves shifted upwards in line with the added risk of the economic shutdowns posed by COVID-19 and fiscal budgetary pressures of low oil prices, indicating higher cost of funding for these countries Saudi Arabia saw the yield on its 2025 bond widen by 75 bps to 3.19 percent during Q1 2020, and the 2050 bond widen by 64 bps to 4.54 percent. Similarly, Qatar saw the yield on its 2026 bond widen by 63 bps to 3.01 percent and the yield on the 2049 bond widen by 30 bps to 3.81 percent. Furthermore, the 2026 Abu Dhabi bond widened by 39 bps to 2.83 percent and the 2049 bond widened by 24 bps to 3.52 percent. Dubai saw its 2025 Dubai Sukuk widen by 85 bps to 3.23 percent and the 2043 Dubai bond widen by 154 bps to 5.83 percent. Bahrain and Oman experienced heightened volatility in terms of yield spreads as the yield on the 2026 Bahrain bond widened by 452 bps to 8.26 percent and the yield on 2047 Bahrain bond widened by 311 bps to 9.02 percent. As for Oman, the yield on its 2025 bond widened by 691 bps to 11.06 percent while the yield on the 2048 bond widened by 398 bps to 10.70 percent indicating markets are perceiving higher risks of defaults amid increasing economic turbulence. Kuwait's only outstanding bonds maturing in 2022 and 2027 widened by 3 bps and 26 bps as of Q1 2020, respectively. A comprehensive yield curve cannot be established for Kuwait due to the lack of government issuances.

**GCC sovereign credit ratings**

One of the more important implications of the outbreak of COVID-19 and decline in oil prices is the S&P's downgrade of Kuwait from AA to AA- with a stable outlook and Oman from BB to BB- with a negative outlook. Moreover, Moody's changed its outlook for both countries from Stable Outlook to Negative Outlook and has placed both countries on review for a potential downgrade. Fitch, however, affirmed Kuwait's credit rating at AA and maintained a stable outlook for the GCC country.

# KIPCO's liquidity remains strong: Vice Chairman

**KUWAIT:** KIPCO - the Kuwait Projects Company (Holding) - has confirmed that it is on track to retire the $500 million bond maturing in July 2020 out of existing resources, demonstrating its strong liquidity position. There will be no other KIPCO bond maturing for almost three years.

Noting the recent decision from S&P Global Ratings to downgrade KIPCO's senior unsecured bonds, the company said its credit profile continues to be solid. The S&P rating was last affirmed in early March 2020. However, following the global equity market sell-off driven by COVID-19, quoted market prices of KIPCO's key listed assets have declined, leading to an increase in the Loan to Value (LTV) ratio above the rating agency threshold. In particular, Burgan Bank's share price has declined by around 29% year to date (YTD), in line with other Kuwaiti banks (26 percent YTD). S&P also reduced its views on the valuation of two unlisted or thinly traded assets.

Faisal Al-Ayyar said

This global sell-off is an unprecedented event with markets driven by fear and uncertainty around COVID-19 and its short to medium term impact. KIPCO believes that current prices do not represent the intrinsic value of its portfolio companies. KIPCO owns fundamentally strong market leaders in their respective sectors and, in particular, Burgan Bank, Gulf Insurance Group and KAMCO Invest have reported very good results for 2019. Furthermore, OSN's streaming platform was relaunched earlier this month, with thousands of customers joining the platform each week. Customers are enjoying the new content in the safety of their homes with fresh movies, series, family and kids content from Disney+, HBO, Nickelodeon and other major Hollywood studios. This comes as a result of OSN resetting its content rights with the studios along with securing the exclusive distribution rights for the entire MENA region across linear and digital platforms.

KIPCO's Vice Chairman (Executive), Faisal Al-Ayyar said: "One of KIPCO's strengths is its proactive management of liabilities, along with its strong liquidity position. In October 2019, the company refinanced its upcoming 2020 bond maturity in advance, thereby extending the average debt maturity. Once the July 2020 bond is repaid, there will be no debt maturing until March 2023. This structure is very supportive of the long-term nature of our investment strategy and provides us with runway to overcome any short to medium-term challenges such as COVID-19."

NEW YORK: An unprecedented crash in oil prices is adding pressure to already stressed US producers, threatening key shale regions and putting vulnerable companies at risk of going under.— Reuters

# Oil crash means more misery for US shale producers

**NEW YORK:** An unprecedented crash in oil prices is adding pressure to already stressed US producers, threatening key shale regions and putting vulnerable companies at risk of going under. A day after US oil futures closed in negative territory for the first time ever, US President Donald Trump on Tuesday ordered his administration to come up with a plan to aid embattled producers, saying on Twitter, "We will never let the great US Oil & Gas Industry down."

But it was unclear exactly what further steps were available to Trump-who has already announced plans to buy oil off the glutted market to fill the US Strategic Petroleum Reserve-or whether any kind of additional aid would come in time for the industry. A proposal in Texas to mandate output cuts from producers remained in limbo after the Texas Railroad Commission Tuesday deferred a vote on the controversial measure until May, pending a review by the state's attorney general.

The commission's chairman, Wayne Christian, struck a defiant note at the outset of the meeting.

"While this is a dark time for our energy producers and our economy, I have no doubt that once this COVID 19 is rescinded and America is back to work, a rebound will occur," Christian said. "This is not going to be easy and it will not happen overnight. But Texans will rebuild this industry which has quite literally changed worldwide the power dynamics that surround energy policy."

In the meantime, "activity is in free fall in North America," Halliburton Chief Executive Jeffrey Allen Miller said Monday as he warned of layoffs in the face of an expected 50 percent decline in capital spending on exploration and production in North America in 2020. Larger industry players such as Exxon Mobil and Chevron have slashed their capital budgets, along with midsized players, which have also taken an axe to their corporate dividends. The most vulnerable companies, though, are smaller players that have less access to capital. Interest rates on "B" rated five-year bonds, which are investment grade, are more than 25 percent, according to a note from CFRA Research.

"I think we are going to see more Chapter 11 filings," predicted CFRA analyst Stewart Glickman. "Who survives will be the firms with strong balance sheets. The ones that have too much debt are really going to have a problem."

**Downgraded to deep junk**

US oil's first-ever drop into negative territory on Monday was precipitated by the imminent expiration of the May contract, which punished traders who made bad bets at a time when there is almost no available free storage in the glutted market. US oil futures for May delivery were back in positive territory Tuesday, ending at $10.01 a barrel. But in an ominous sign, futures for June delivery sank nearly 43 percent to $11.57 a barrel. The petroleum industry has emerged as one of the most vulnerable cornerstones of the global economy as shutdowns to limit the spread of coronavirus have a devastating impact on demand for oil.

The commodity has been further weakened by a battle for market share that raged much of the spring between Saudi Arabia and Russia. Some analysts think a historic agreement last week by those two producers and other leading exporters could improve the supply-demand balance in the latter half of 2020. In the meantime, smaller companies are under pressure. These include shale producer Lonestar Resources, which is based in Forth Worth. S&P downgraded the company further into "junk" territory.

S&P's move followed the company's disclosure that it was out of compliance with its lending facilities. The company cautioned there is a risk it will be unable to reach agreement with lenders under a future default scenario, an outcome that would "create substantial doubt regarding our ability to continue as a going concern," Lonestar said in a filing last week. — AFP

# Ships, trains, caves: Oil traders chase storage space

**LONDON/NEW YORK:** Oil traders are struggling to find enough ships, railcars, caverns and pipelines to store fuel as more conventional storage facilities fill up amid abundant supply and plummeting demand due to the coronavirus crisis. Dozens of oil tanker vessels have been booked in recent days to store at least 30 million barrels of jet fuel, gasoline and diesel at sea, acting as floating storage, as on-land tanks are full or already booked, according to traders and shipping data.

That adds to about 130 million barrels of crude already in floating storage, traders and shipping sources said. Demand for oil and its products has tumbled as much as 30 percent as governments around the world have told citizens to stay home to prevent the virus spreading - grounding planes and leaving cars parked up. But the world remains awash with oil supplies.

OPEC, Russia and other major producers have forged a deal to curb production, but it will only reduce supply by about 10 percent and it does not kick in until May. It is hard to gauge the world's total oil storage capacity, but signs that the limit is being reached are increasingly obvious. Rising sea storage is one indicator, as it is more expensive than storing onshore and can be technically complex.

Oil producers, refiners and traders are also turning to more unusual tactics, such as storing crude and fuel in railcars in northeastern United States or in unused pipelines. Europe's northwestern refining and storage hub still has space to fill but industry experts say most of the remaining capacity has already been booked. Salt caverns in Sweden and other Scandinavian countries were either full or fully booked. "We are now working on the most oddball storage locations, really tough locations where there are operational constraints," said Krien van Beek, a broker at ODIN - RVB Tank Storage Solutions in Rotterdam. The United States has some refined products storage space left in the area from the Midatlantic to the Southeast and along the Gulf Coast, said Ernie Barsamian, chief executive of The Tank Tiger, a US terminal storage clearinghouse.

But he said more preferable product storage sites, such as deepwater ports in New York Harbor and Houston, which are close to the demand centers, were no longer available. "The big tanks where you pull a ship in and empty the whole thing, that's all gone. What you have is pots and pans," he said.

In the United States, onshore storage tanks are mostly reserved for local refineries which are using railcars to store crude, as well as gasoline and diesel.

"Even the railcars are going to get stacked with product," said a US-based broker who asked to remain anonymous. In hubs with a little space left, such as Chicago, tank operators can charge a premium and longer leases. They have been demanding leases of 24-36 months rather than the more usual 12 months, according to two refined products brokers.

With the market oversupplied, oil prices have plunged to their lowest levels in two decades. This week, US Western Texas Intermediate made an unprecedented dive into negative territory, so sellers had to pay people to take it. Despite the plummeting crude price, some refineries which are able to find space can still make money producing fuel.— Reuters