Debt markets

GCC issued record $50 billion in international sovereign debt last year

> Chaker El Mostafa
Economist
+965 2259 5356, chakermostafa@nbk.com

> Daniel Kaye
Head of Macroeconomic Research
+965 2259 5363, Danielkaye@nbk.com

GCC sovereigns issued a record $50 billion in international debt in 2017, helping push total GCC issuance – public and private – over $100 billion for a second consecutive year. Despite this, reduced austerity and stronger commodity prices helped confidence return to the region, pushing benchmark yields lower, while international benchmark rates edged higher or were little changed. Synchronized global growth, on the other hand, ushered in tighter credit and monetary conditions.

International benchmarks were range-bound and ended the year mixed, as political tensions and positive economic data wrestled for market direction. Uncertain US fiscal policy, White House drama, EZ elections, stubborn inflation, and North Korea kept a lid on international yields, but hawkish central banks and rallying international equity markets placed a floor under them. Indeed, most benchmark yields hovered within a range of 42 to 59 basis points (bps), despite the Fed raising its policy rate 3 times in 2017 and the ECB trimming its QE program.

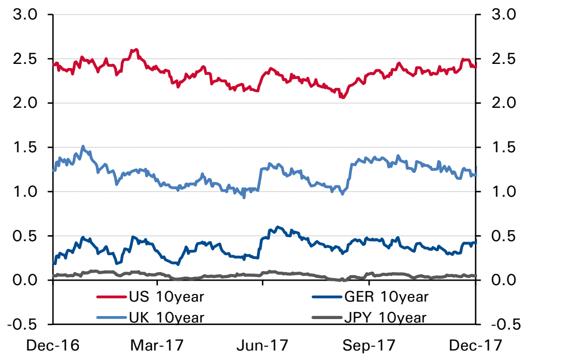
At 2.41%, US 10-year Treasuries finished 2 bps lower in 2017, though yields were relatively volatile throughout. (Chart 1.) The new administration's plan to cut taxes and Fed hawkishness initially propelled rates as high as 2.61%. Weak follow through on promised reforms, underwhelming inflation, and geopolitical strife, however, saw yields soften afterwards. Investor sentiment then remained averse for most of the year, with 10-year yields reaching a low of 2.06% in late 3Q17, before turning around, driven by stronger data, tax reform, rallying markets, and a third Fed rate hike.

Despite the political uncertainty that dominated the first half of 2017, 10-year Bund yields ended the year higher on stronger economic prospects and a tighter monetary outlook. Indeed, the threat of right-wing extremism that dominated investors' concerns early in 2017 subsided following the election of a slew of pro-EU candidates, supported by a strengthening economic backdrop. Surprisingly strong economic data throughout the year also pushed monetary policy officials to adjust their dovish tone. This culminated in 3Q17 with the ECB extending its current program by 9-months and trimming its monthly purchases by half. Economic data has since remained encouragingly positive, feeding into the ECB's increasing hawkishness. As such, yields on 10-year Bunds added 22 bps over the year. (Chart 1.)

GCC benchmark yields maturing in 8-9 years were mixed, with some little changed while others saw their risk premium shrink significantly. (Chart 2.) Movement was first dictated by the weakness in commodity prices and later by regional tensions. However, the relative success of GCC fiscal reforms, the extension of the OPEC deal, and the modest impact of the Qatari diplomatic crisis helped contain a climb in yields. The recovering oil price late in the year also helped keep yields down. Saudi's 2026, Kuwait's 2027, and Oman's 2027 bonds shed between 19 and 40 bps over the year. Meanwhile, Qatar 2026 and Bahrain 2026 only dropped between 6 and 9 bps. (Chart 3.)

Chart 1: Global benchmark yields

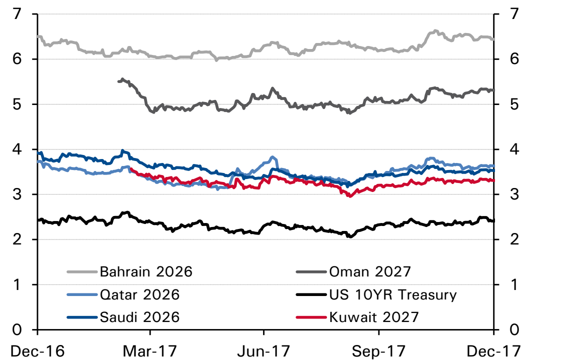
(%)



Source: Thomson Reuters Datastream

Chart 2: GCC sovereign yields

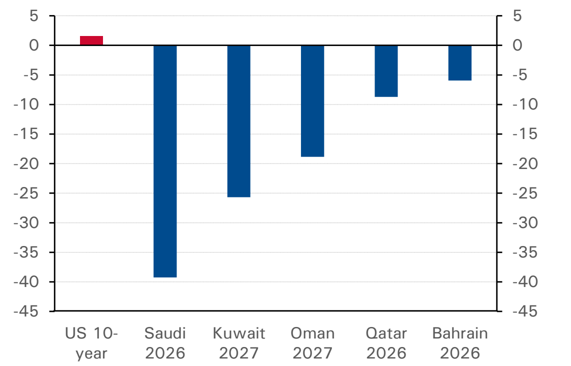
(%)



Source: Thomson Reuters Datastream

Chart 3: 12-month change in GCC sovereign yields

(as of 29 December, 2017; bps)



Source: Thomson Reuters Datastream; Kuwait and Oman change is calculated from their respective issuance dates circa March-17

With the global economy witnessing a broad-based recovery, monetary conditions tightened despite modest inflation. Indeed, the Federal Reserve, encouraged by the stream of positive data, stuck to the hike path it laid out at the beginning of the year and raised its policy rate three times, dismissing, for now, inflation's underwhelming performance. Similarly, the ECB announced the wind-down of its quantitative easing program notwithstanding the stickiness of its core inflation well below the 2% target. Moreover, the strength at which the Canadian economy picked-up required the Bank of Canada to raise its policy rate twice in 2017. In the UK, although Brexit is proving to be a drag on economic activity, the rising threat of inflation pushed the Bank of England to increase its policy rate for the first time since August 2016.

Most GCC central banks followed the Fed, raising key policy rates by 25bps three times, with Oman and Kuwait being the exceptions. The moves were in line with the need to support USD pegs. Oman's Libor-linked repo rate crept gradually higher over the year. Kuwait passed twice on hiking its lending policy rate, but did hike the repo rate, seeking to protect the currency without hurting domestic credit growth. (Chart 4.)

Gross GCC issuance (public and private) crossed $100 billion for the second year in a row, supported by robust sovereign activity. Indeed, public sector debt issuance (central government plus related firms) accounted for $84 billion of all new debt in 2017, $50 billion of which was international sovereign debt, a regional record. Meanwhile, private sector issuance eased to $16 billion, down $4 billion, but remained strong, on the back of healthy non-financial sector activity. Total outstanding debt increased by 16%, to $436 billion. (Chart 5.)

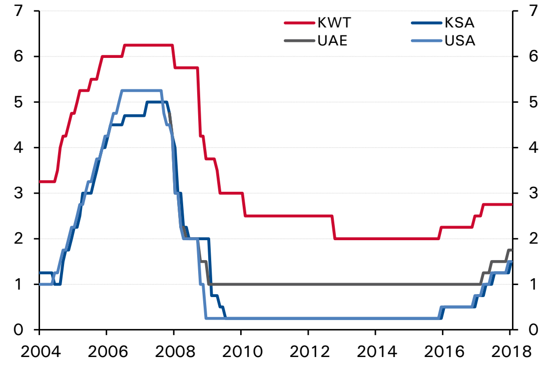
Supported by adequate global funding conditions, total international GCC sovereign borrowing covered close to 50% of government financing needs and was sought after by international investors. Issuance was led by Saudi Arabia, with a $12.5 billion bond and a $9 billion Sukuk, followed by Abu Dhabi's $10 billion offering, and then Kuwait's $8 billion bond, its first. Meanwhile, Oman and Bahrain issued $7 billion and $3 billion, respectively. These issues were all well received, each on average oversubscribed three to five times in spite of credit downgrades, reflecting the overall strong attractiveness of GCC debt.

The perceived riskiness of investing in the region also dropped in 2017 on reduced austerity and stronger commodity prices. CDS rates were down for most tracked sovereigns, declining by between 5 and 30 bps, with Dubai experiencing the strongest jump in confidence. (Chart 6.)

With the aggregate GCC fiscal deficit estimated at $74 billion in 2018, the outlook for regional debt is expected to remain healthy. Oman has already tapped international markets for $6.5 billion and other sovereigns are expected to soon follow. However, the gradual tightening of global monetary policy, notwithstanding possible delays due to subdued inflation, and the volatility of oil prices may weigh negatively on regional funding conditions. This could be worsened by regional geopolitical uncertainty.

Chart 4: Policy rates

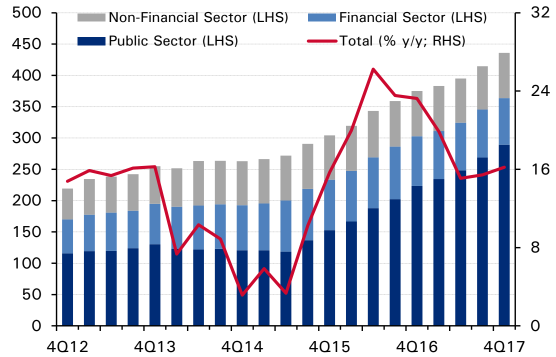
(%)



Source: Thomson Reuters Datastream

Chart 5: Outstanding GCC debt securities

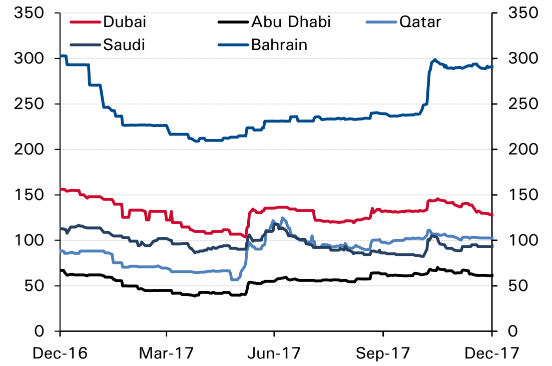
($ billion)



Source: Zawya, Thomson Reuters Eikon, press

Chart 6: GCC 5-year credit default swaps

(basis points)



Source: Thomson Reuters Datastream

Table 1: Gross GCC Issuance by sector (USD billion)

	1Q16	2Q16	3Q16	4Q16	1Q17	2Q17	3Q17	4Q17
Public	15.8	27.0	18.5	23.5	20.0	18.2	22.7	23.4
Financial	2.1	5.6	3.3	1.4	4.7	1.7	0.9	1.0
Non-financial	1.0	3.5	0.3	2.3	1.5	1.1	0.4	4.5
Total	18.9	36.2	22.1	27.2	26.1	21.0	24.0	28.9

Table 2: Gross GCC issuance by country (USD billion)

	1Q16	2Q16	3Q16	4Q16	1Q17	2Q17	3Q17	4Q17
Bahrain	0.0	1.2	0.8	2.8	1.1	0.0	4.2	1.5
Kuwait	2.1	4.6	2.5	4.4	11.6	3.2	4.6	0.3
Oman	0.4	3.3	2.0	0.3	5.0	2.9	0.8	0.9
Qatar	1.7	12.6	4.3	1.0	5.1	3.5	0.6	0.0
KSA	12.8	6.4	11.5	17.5	0.0	9.5	11.1	12.6
UAE	2.0	8.1	1.1	1.3	3.4	1.9	2.7	13.6
GCC	18.9	36.2	22.1	27.2	26.1	21.0	24.0	28.9

Source: Zawya, Thomson Reuters Eikon, Central Bank of Kuwait, press

Head Office

Kuwait
National Bank of Kuwait SAKP
Abdullah Al-Ahmed Street
P.O. Box 95, Safat 13001
Kuwait City, Kuwait
Tel: +965 2242 2011
Fax: +965 2259 5804
Telex: 22043-22451 NATBANK
www.nbk.com

International Network

Bahrain
National Bank of Kuwait SAKP
Zain Branch
Zain Tower, Building 401, Road 2806
Seef Area 428, P. O. Box 5290, Manama
Kingdom of Bahrain
Tel: +973 17 155 555
Fax: +973 17 104 860

National Bank of Kuwait SAKP
Bahrain Head Office
GB Corp Tower
Block 346, Road 4626
Building 1411
P.O. Box 5290, Manama
Kingdom of Bahrain
Tel: +973 17 155 555
Fax: +973 17 104 860

United Arab Emirates
National Bank of Kuwait SAKP
Dubai Branch
Latifa Tower, Sheikh Zayed Road
Next to Crown Plaza
P.O.Box 9293, Dubai, U.A.E
Tel: +971 4 3161600
Fax: +971 4 3888588

National Bank of Kuwait SAKP
Abu Dhabi Branch
Sheikh Rashed Bin Saeed
Al Maktoom, (Old Airport Road)
P.O.Box 113567,Abu Dhabi, U.A.E
Tel: +971 2 4199 555
Fax: +971 2 2222 477

Saudi Arabia
National Bank of Kuwait SAKP
Jeddah Branch
Al Khalidiah District,
Al Mukmal Tower, Jeddah
P.O Box: 15385 Jeddah 21444
Kingdom of Saudi Arabia
Tel: +966 2 603 6300
Fax: +966 2 603 6318

Jordan
National Bank of Kuwait SAKP
Amman Branch
Shareef Abdul Hamid Sharaf St
P.O. Box 941297, Shmeisani,
Amman 11194, Jordan
Tel: +962 6 580 0400
Fax: +962 6 580 0441

Lebanon
National Bank of Kuwait
(Lebanon) SAL
BAC Building, Justinien Street, Sanayeh
P.O. Box 11-5727, Riad El-Solh
Beirut 1107 2200, Lebanon
Tel: +961 1 759700
Fax: +961 1 747866

Iraq
Credit Bank of Iraq
Street 9, Building 187
Sadoon Street, District 102
P.O. Box 3420, Baghdad, Iraq
Tel: +964 1 7182198/7191944
+964 1 7188406/7171673
Fax: +964 1 7170156

Egypt
National Bank of Kuwait - Egypt
Plot 155, City Center, First Sector
5th Settlement, New Cairo
Egypt
Tel: +20 2 26149300
Fax: +20 2 26133978

United States of America
National Bank of Kuwait SAKP
New York Branch
299 Park Avenue
New York, NY 10171
USA
Tel: +1 212 303 9800
Fax: +1 212 319 8269

United Kingdom
National Bank of Kuwait
(International) Plc
Head Office
13 George Street
London W1U 3QJ
UK
Tel: +44 20 7224 2277
Fax: +44 20 7224 2101

National Bank of Kuwait
(International) Plc
Portman Square Branch
7 Portman Square
London W1H 6NA, UK
Tel: +44 20 7224 2277
Fax: +44 20 7486 3877

France
National Bank of Kuwait
(International) Plc
Paris Branch
90 Avenue des Champs-Elysees
75008 Paris
France
Tel: +33 1 5659 8600
Fax: +33 1 5659 8623

Singapore
National Bank of Kuwait SAKP
Singapore Branch
9 Raffles Place # 44-01
Republic Plaza
Singapore 048619
Tel: +65 6222 5348
Fax: +65 6224 5438

China
National Bank of Kuwait SAKP
Shanghai Representative Office
Suite 1003, 10th Floor, Azia Center
1233 Lujiazui Ring Road
Shanghai 200120, China
Tel: +86 21 6888 1092
Fax: +86 21 5047 1011

NBK Capital

Kuwait
NBK Capital
38th Floor, Arraya II Building, Block 6
Shuhada'a street, Sharq
PO Box 4950, Safat, 13050
Kuwait
Tel: +965 2224 6900
Fax: +965 2224 6904 / 5

United Arab Emirates
NBK Capital Limited - UAE
Precinct Building 3, Office 404
Dubai International Financial Center
Sheikh Zayed Road
P.O. Box 506506, Dubai
UAE
Tel: +971 4 365 2800
Fax: +971 4 365 2805

Associates

Turkey
Turkish Bank
Valikonagl CAD. 7
Nisantasi, P.O. Box. 34371
Istanbul, Turkey
Tel: +90 212 373 6373
Fax: +90 212 225 0353