

GCC equity investment outlook Q2, 09

The recent spurt in the equity markets has brought some hope for investors. **M.R.Raghu** and **Amrith Mukkamala** analyses the GCC equity investment outlook for the year.

After a bloodbath in Q4-08, it is time to get a sense of what can be expected for the ensuing quarter. The consensus opinion is that the, "worst is behind us". However, this does not imply moving from a negative scale all the way to a positive scale. The transition will likely be gradual with many potholes in between. For equities, the view is neutral for Q2-09. This is because the earnings weakness is expected to continue further into 1Q09 along with weak liquidity. However, the good thing to note is that volatility has cooled off significantly, while there are signs of macroeconomic

stability, especially where inflation is concerned.

Earnings

GCC earnings growth came to a halt in Q4-08. The overall earnings for the GCC for Q4-08 were a loss of US\$13 billion compared to profits of US\$14 billion on a YoY basis. For the full year 2008, the numbers indicate a negative growth of 39 per cent. Among the six GCC countries, the worst affected in 2008 was Kuwait with a decline in earnings of 96 per cent (Table: 1) and there are still around 10 investment companies that are yet to declare

their results. This is most likely expected to result in the earnings declining further. Saudi Arabia, which forms 35 per cent of the GCC earnings, has seen its 2008 profits slump by 45 per cent. The only positive growth was in Qatar with the full year earnings growth rate coming in at 31 per cent. The factors that are affecting the overall earnings growth are a steep decline in earnings in the financial services segment due to massive write downs and mark to market losses. Real estate is also suffering due to price and demand decline, while commodities are down as price and volume fall.

Going forward, Qatar is expected to post some revival in earnings on a QoQ basis as majority of the earnings are from commodity driven companies and there has been a modest turnaround in commodity prices as compared to the December 08 quarter. Saudi Arabia is rated negative on earnings. The commodity related story in Saudi Arabia is continuing to witness significant weakness. Sabc's Q1-09 numbers were worse than expectations. The Q1-09 loss was at US\$0.26 billion with the operating profit declining by 96 per cent on a YoY basis. The decline in core earnings apart from the goodwill write-off shows continuing weakness in Sabc's business. The banking, real estate and the rest of the financial sector will continue to be pressurised. On an overall basis, GCC earnings growth will continue to be negative in Q1-09.

Investment outlook summary						
	Earnings	Liquidity	Valuation	Risk	Macro economic	Overall
Saudi Arabia	Negative	Negative	Neutral	Positive	Positive	Neutral
Kuwait	Negative	Neutral	Negative	Neutral	Neutral	Neutral
UAE	Negative	Negative	Positive	Positive	Neutral	Neutral
Qatar	Positive	Neutral	Positive	Neutral	Neutral	Neutral
Bahrain	Negative	Negative	Negative	Positive	Positive	Negative
Oman	Negative	Negative	Positive	Positive	Neutral	Neutral
GCC	Negative	Negative	Positive	Positive	Neutral	Neutral

Table: 1 – Earnings Trend – GCC						
US\$ Mn	Q4-07	Q4-08	YoY	2007	2008	YoY
Saudi Arabia	5022	-6316	NA	22,533	12,449	-45
Kuwait	2544	-7826	NA	13,320	560	-96
UAE	4293	193	-95	13,551	13,483	0
Qatar	1663	1169	-30	5767	7544	31
Bahrain	537	-271	NA	2444	872	-64
Oman	506	15	-97	1551	1307	-16
GCC	14,566	-13,036	NA	59,165	36,215	-39

Source: Company filings, Zawya Investor, Markaz Research

Table: 2 – Value Traded trend

Value Traded (US\$ Bn)	Q109	QoQ %	YoY %
Saudi Arabia	81	-6	-57
Kuwait	12	-48	-73
UAE	10	-33	-81
Qatar	5	-53	-53
Bahrain	0.07	-87	-92
Oman	0.87	2	-64
GCC	109	-20	-63

Source: Respective stock markets, Zawya Investor, Markaz Research

Table: 3 – Valuation snapshot – GCC markets

Country	Market Cap (US\$ Bn)	PE (x)	PB (x)	Dividend Yield %	% Change YTD
Saudi Arabia	237	12.61	1.92	4.84	-2
Kuwait	89	10.19	2.08	7.91	-12
UAE	93	8.60	1.72	4.70	NA
Qatar	40	7.25	1.65	8.73	-29
Bahrain	17	18.07	1.28	5.92	-10.75
Oman	10	9.02	2.27	7.00	-12

Source: Reuters 3000xtra, Markaz research

Liquidity

The liquidity levels, which indicate investor sentiment, have witnessed significant declines across the GCC region. The aggregate value traded level has seen a 20 per cent decline on a QoQ basis in Q1-09 and a YoY decline of 63 per cent (Table – 2). Liquidity levels are rated negative across the region for Q2-09, as clients continue to face difficulty in obtaining leverage to trade.

Valuation

Valuation levels across GCC have witnessed significant declines. At the current prices, most of the banks in the region are trading either at their book values or at a discount. The price to earnings, taking the trailing twelve month earnings into consideration, looks comparable with emerging market peers for most of the GCC markets.

Due to the decline in price levels, the dividend yield of the markets is

also looking attractive at an average 6.52 per cent for the GCC markets. Except for Kuwait and Bahrain, the rest of the GCC markets are rates positive on the valuation levels. Saudi Arabia is rated neutral (Table: 3).

Risk

Risk levels as characterised Markaz Volatility Index (MVX - proprietary index built by Markaz for gauging risk) shows significant reductions as compared to its historic highs witnessed in October. At a GCC level, the MVX has witnessed a decline of 60 per cent from its peak in Oct 08. On a QoQ basis too, all the GCC markets ex-Qatar have witnessed a reduction in risk levels with Oman and Bahrain leading the pack.

We are positive on all GCC markets ex-Qatar and Kuwait in terms of risk. Kuwait and Qatar have been rated neutral mainly due to the smaller deviation these markets

have seen as compared to their trend lines (Table: 4).

Macro economic

Macro economic situation is gauged by taking several factors such as – GDP growth, inflation rates, money supply and bail out packages announced into consideration. Most of the markets are expected to witness significantly lower GDP growth rates as compared to 2008. However, there has been a significant decline in inflation rates too. Also, all the central banks in the region ex-Qatar have slashed their interest rates to provide a boost to their respective economies. A slow down in GDP growth has already been priced into the valuations. The recent efforts of the regional central bankers and sovereign wealth funds like Kuwait, Qatar, UAE and Saudi Arabia by cutting interest rates, announcing fiscal stimulus packages, buying stakes of banks in the secondary markets provide a cushion to the fall in the economic growth. All the GCC economies Ex-Saudi Arabia and Bahrain are rated as neutral. Saudi Arabia is rated positive and Bahrain is rated negative for macro economic scenario.

Table: 4 – Markaz Volatility Index Trend

	Current MVX level	% Change QoQ	% Deviation from Last 12M High	Last 12M High date
Saudi Arabia	3842	-37.73	-66.25	14-Oct-08
Kuwait	1954	-49.49	-55.19	26-Oct-08
Abu Dhabi	3666	-29.06	-60.16	14-Oct-08
Dubai	4515	-34.20	-68.54	16-Oct-08
Qatar	8039	91.29	-37.64	14-Oct-08
Bahrain	954	-58.23	-70.53	30-Oct-08
Oman	2621	-66.84	-77.66	14-Oct-08
GCC	2663	0.82	-60.85	14-Oct-08

Source: Markaz Research

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