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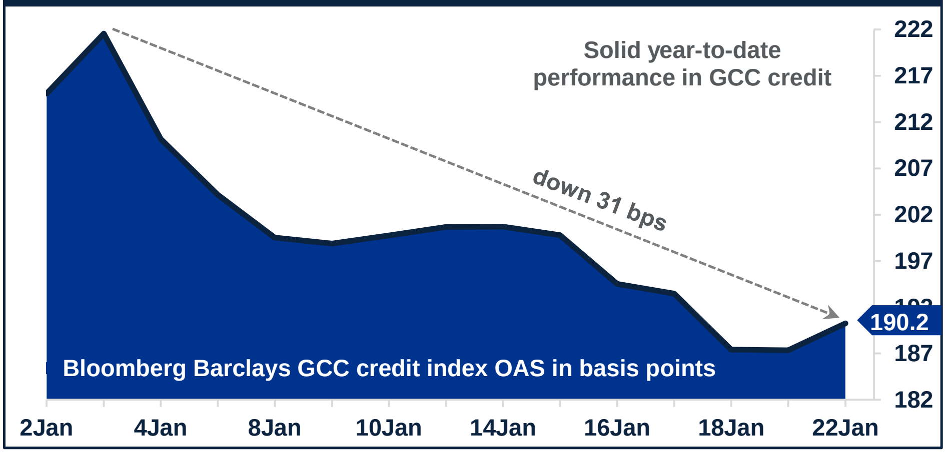
GCC Fixed Income
Establishing solid foundations for 2019

The GCC fixed income market has had a solid start to 2019, in terms of both primary and secondary market performance. Moreover, this is a trend that we expect to extend through the year as global macro uncertainties further highlight and enhance the relative value appeal of the asset class' strong underlying fundamentals.

The opening weeks of January have seen a sharp spread compression in the Bloomberg Barclays GCC credit index. While the index has eased back a little this week (to the 190bp OAS level) amid a pick-up in market volatility, the index has tightened by an impressive 22bps since the beginning of the year (and 31bps from the wide seen on January 3).

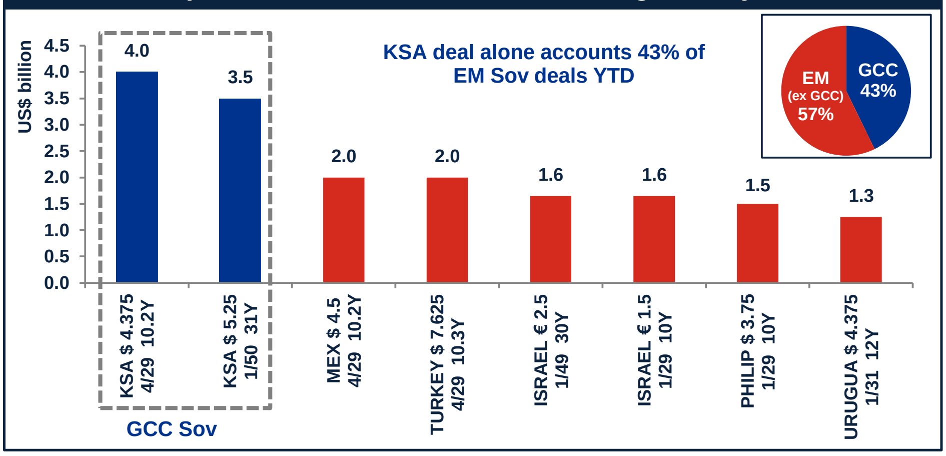
Solid start to the year



Source: Bloomberg/FAB

Strong credit fundamentals, along with the combined allure of liquidity and incremental yield meant that the Kingdom of Saudi Arabia 10Y and 31Y new issues have accounted for 43% of the January emerging market sovereign issuance volume.

Major eurobond deals from EM Sovereigns this year



Note: Issuance data as at 22-Jan-2019; Source: Bloomberg/FAB

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Simon Ballard
Macro Strategist

Rakesh Sahu
Analyst

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Further support for the asset class should be forthcoming this year. US$ bonds from five GCC states – Saudi Arabia, the UAE, Qatar, Bahrain & Kuwait – are due for the inclusion in JP Morgan's flagship Emerging Markets Bond Index starting 31st January and will be done in a phased manner until 30th September.

JP Morgan has indicated that the five GCC states together would secure around 12% weight in the EMBI index. This means more funds inflow in to the GCC bond market. To know more about this fast growing bond market, please refer of our GCC Fixed Income Chart Book: FY 2018 Review.

Aside from the liquidity/yield story in the primary market though, as highlighted above, we would suggest that there is a far more structural appeal to GCC credit risk. Not only does the asset class offer investors the reassurance of an attractive, solid single-A risk profile, but this comes with a respectable total return offering.

Bloomberg Barclays Index	Index Description	Average credit Rating	Change in OAS (in bps)	Change in Yield (in bps)	Current Yield (in %)	Total return YTD (in %)
LF98TRUU Index	US Corporate High Yield US$	B+	-93.3	-82.4	7.13	+3.69
I31732US Index	EM High Yield US$	B+	-66.8	-60.6	7.94	+3.11
LG30TRUU Index	Global High Yield Multi Currency	B+	-75.8	-68.0	6.98	+3.09
LG20TRUU Index	EM Hard CCY Aggregate	BBB-	-33.5	-28.0	5.29	+1.81
BEHGTRUU Index	EM Inv. Grade US$	A-	-19.3	-13.1	4.42	+1.33
BGCCTRUU Index	**GCC Aggregate IG & HY US$**	**A**	**-22.0**	**-14.5**	**4.51**	**+1.24**
BGCITRUU Index	**GCC Aggregate IG US$**	**A+**	**-17.3**	**-10.5**	**4.14**	**+1.05**
LUACTRUU Index	Global Corporate IG US$	A-	-15.8	-10.0	4.10	+1.03
BEUCTRUU Index	EM Asia Aggregate US$	BBB+	-19.2	-13.2	5.38	+0.97
BEUGTRUU Index	EM Asia Inv. Grade US$	A-	-11.2	-5.4	4.27	+0.72
LBEATREU Index	Euro Aggregate IG	A+	+0.6	-1.4	0.75	+0.29
LGUSTRUU Index	Global Aggregate IG US$	AA	-4.3	+1.0	3.29	+0.26

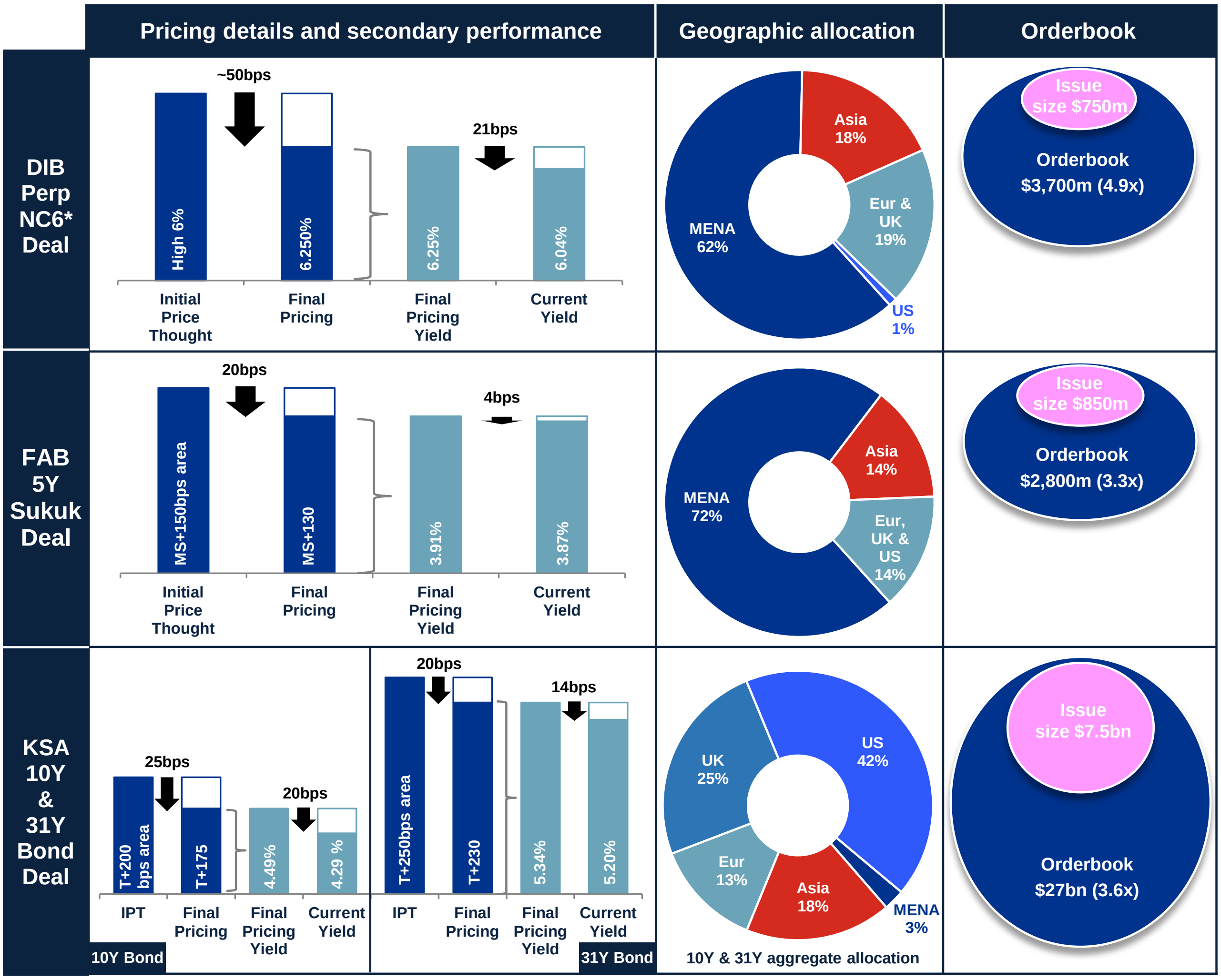
Note: Data as at 22-Jan-2019; Source: Bloomberg/FAB

As such we would conjecture that GCC credit sits at the mid-table sweet spot within the fixed income asset class as a whole. As per the above table, GCC credit indexes sit favorably alongside its IG, HY and EM peers, in terms of both rating and total returns.

This structural support and investor appetite for the asset class also carries clear benefits for GCC issuers. A look at new issue price and yield performance in January shows how issuers, bringing correctly-priced transactions to the market, have been able to benefit from a positive price discovery process as well as strong robust secondary market performance (please refer to the chart on next page). Such spread and price achievements have been founded on orderbooks that have easily exceeded issue sizes, by between 3 and 5 times on average.

Healthy geographic dispersion of new issue allocations in January also highlights the strength and depth of the sector's investor base. This in turn should help to support and facilitate issuers' return visits to the market, as and when funding needs require.

For example, if we look at the Saudi deal, the bond allocation was primarily skewed towards investors from the United States (42%), thereby implying anchor demand for such blue-chip credits from the region. Asian investors are also very active in the GCC fixed income market; they have accounted for 15-20% of recent deals, including Islamic bond (sukuk) deals.



*Note: * NC6 is non-callable for six years; Current yield indicates closing yield as at 22-Jan-2019; Source: FAB/Bloomberg*

We believe that the above charts and data underscore the strong performance that the GCC fixed income space has experienced during these opening weeks of 2019. The performance is perhaps all the more impressive when viewed in the context of the current global macro and political uncertainties – slowing global growth, U.S./Sino trade tensions, Brexit – that continue to overhang market sentiment.

All of which should make for an interesting and compelling case for continued capital investment flows in favour of this region and asset class.

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FAB Global Markets

Email: Marketinsights&strategy@bankfab.com

Tel: +971 2 6110 127

Reuters dealing codes: FABU / FABA

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