

# Market Insights & Strategy

Global Markets

10<sup>th</sup> April 2019



**Chavan Bhogaita**

Managing Director & Head of Market Insights & Strategy

**Rakesh Sahu**

Director, Market Insights & Strategy

Please click [here](#) to view our recent publications on MENA and Global Markets

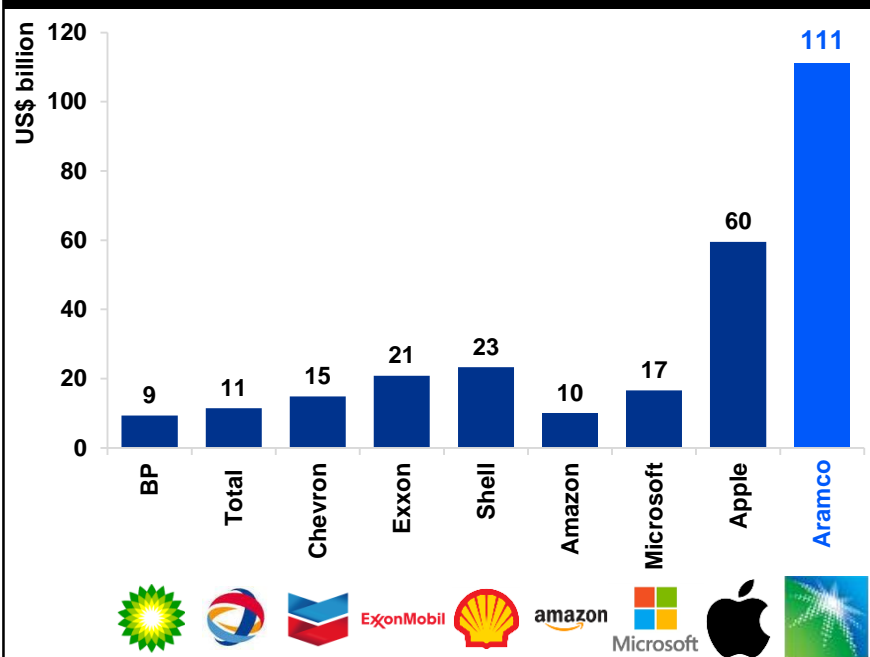
## Aramco. *'This is Big'*

In today's world, size does matter. That said, adjectives such as big, enormous, monumental and various others are often used too liberally and somewhat lose their meaning both in absolute and relative terms. Then, very occasionally, something happens that reinstates the true meaning of scale. Something that leaves people speechless, jaws wide open, struggling to digest and comprehend what they are seeing. The arrival of Saudi Aramco to the debt capital markets is one such thing.

For many years markets have "known" that Aramco, the national oil producer of Saudi Arabia, is a large entity. Profitable even. Cash rich? Surely. Blue-chip? It goes without saying. However until a few days ago when the company released its financials and other key information that had thus far remained undisclosed, most of us couldn't have really appreciated the true scale, calibre and depth of this organisation. Upon reading through the now public information about Aramco, it becomes clear that – beyond any shadow of a doubt – *this* is what **big** looks like.

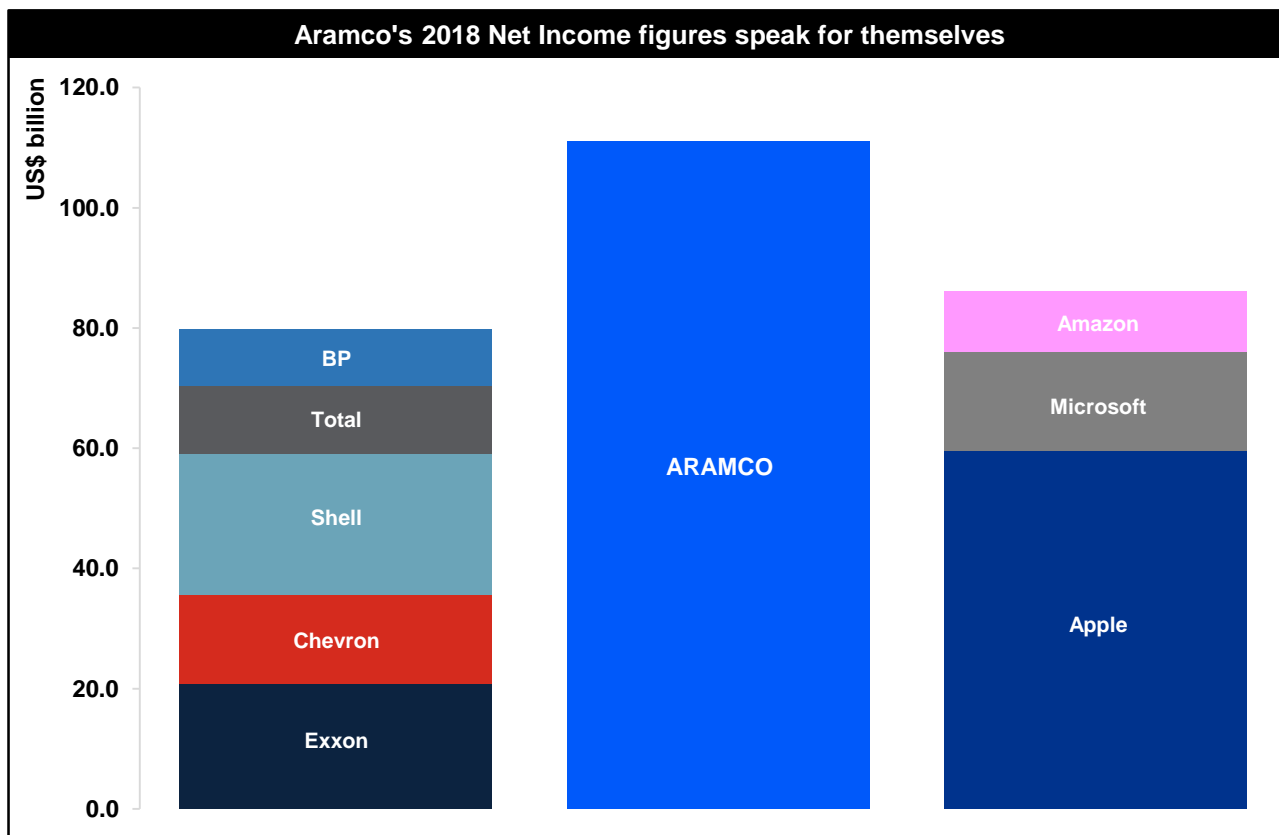
The charts below do a better job of explaining this than any superlatives could achieve. Let's take net income as an example; if you add together the 2018 net income for 5 of the largest oil companies in the world, then add another 30% (yes thirty) to the aggregate number, you would still end up with a figure that is lower than Aramco's net income for the same period. Absolutely staggering. And it isn't just oil giants that Aramco dwarfs, as the same can be said of what we all consider to be some of the largest corporates on the planet – namely Apple, Microsoft, Amazon. And remember, Aramco is this big before having ever tapped capital markets (debt or equity). To say that this makes its scale noteworthy would be an understatement.

2018 Net Income: Aramco dwarfs others

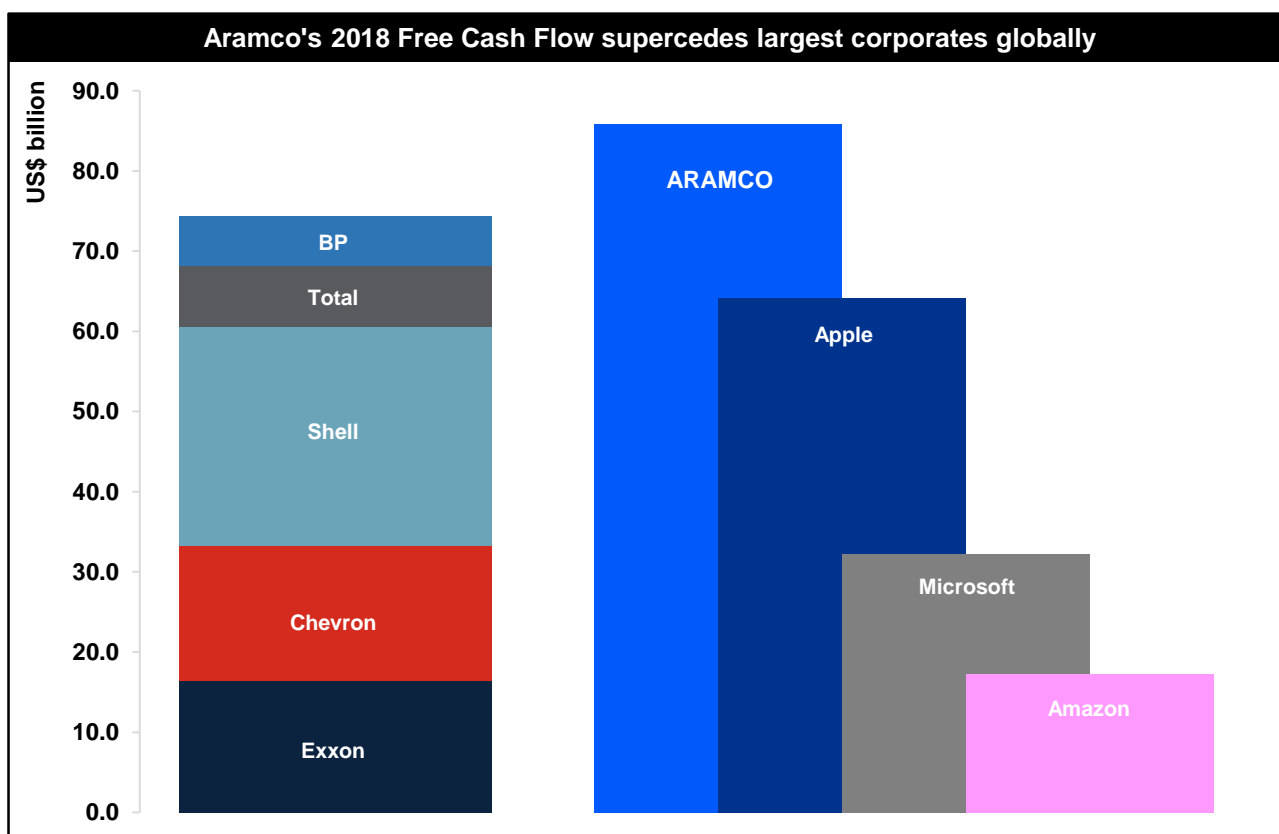


Source: Bloomberg/Aramco/FAB

The below charts provide some further evidence regarding the scale of Aramco's operations and its cash generating ability vis-à-vis the best known and - thus far regarded as the "big boys" in the oil industry - and indeed some of the largest corporates globally.

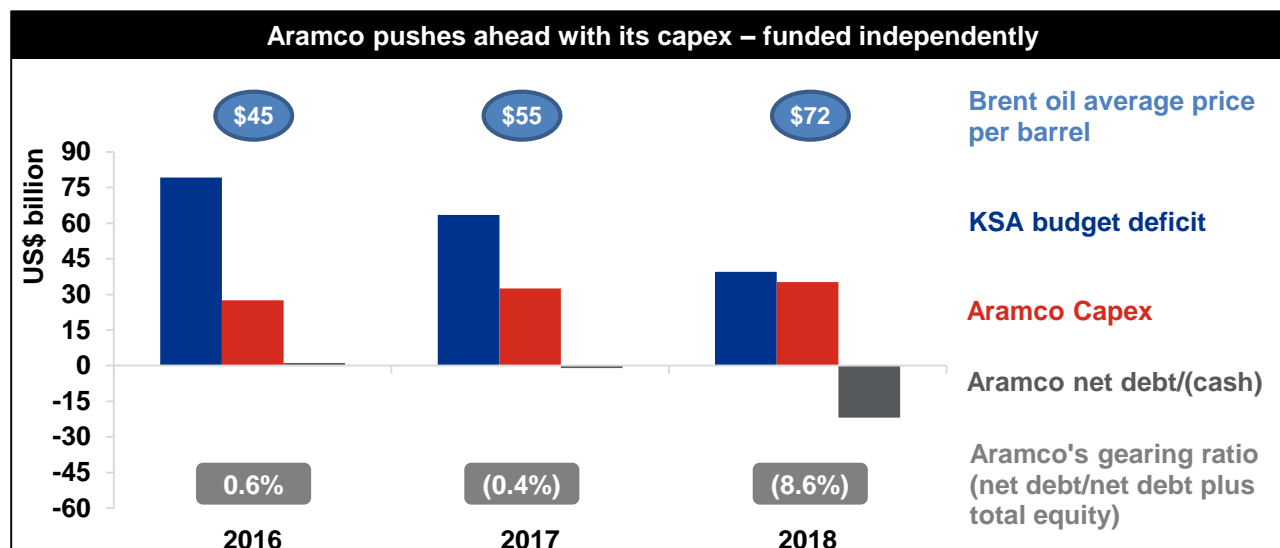


Source: Aramco/Bloomberg/FAB



Source: Aramco/Bloomberg/FAB

A closer look into Aramco's financials reveals that over the past three years, while the Saudi government was experiencing some fiscal challenges, Aramco has continued to follow its corporate strategy and has funded its capex independently from its internal cash flows while keeping its leverage under control. Meanwhile, the sovereign funded its budget deficit from external borrowings. The fact that the company has been able to maintain its substantial capex spend – and fund it internally – whilst the sovereign has been tapping debt capital markets to fund its budget deficit says a lot about Aramco's financial strength.



Source: Aramco/Bloomberg/FAB

### This transaction is significant for other reasons too.

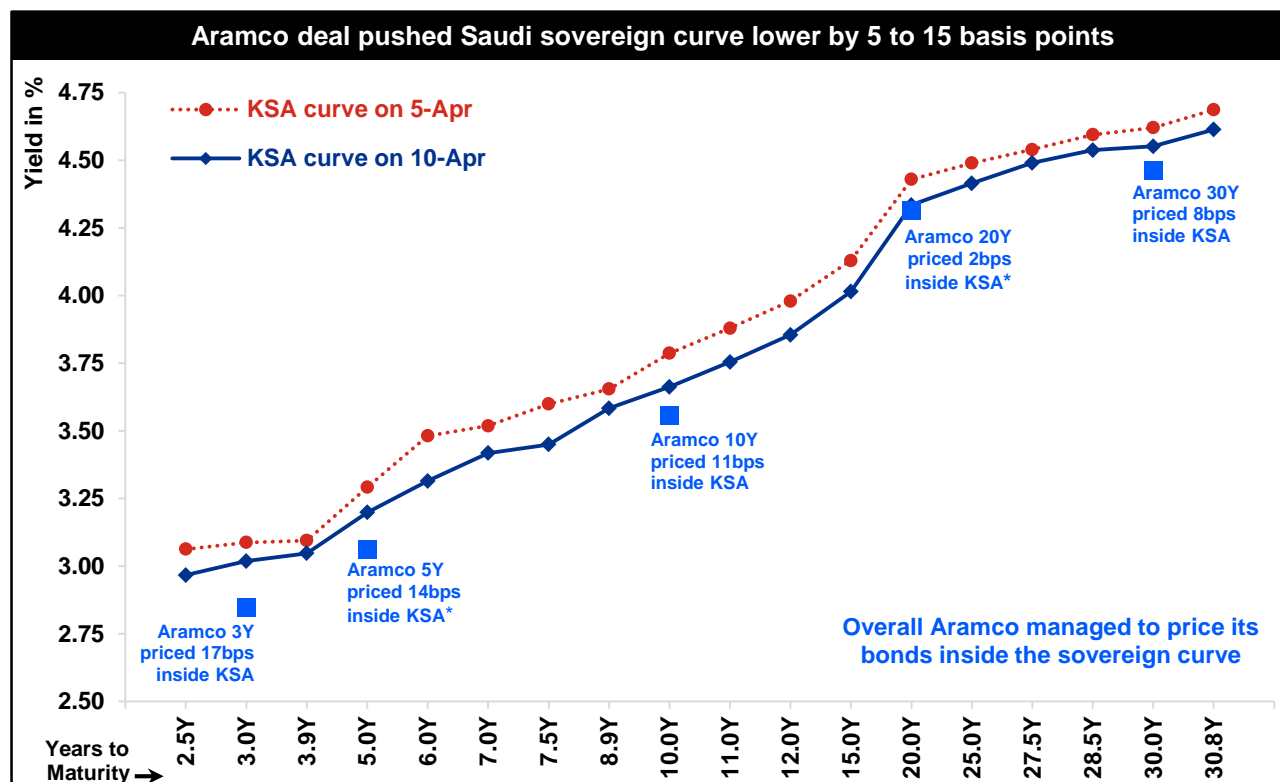
Moving on from Aramco's scale, the company's debut transaction in the global debt capital markets is hugely significant for reasons beyond the company's scale:

- First time that the company has published its credit ratings from the major agencies AND one of the very rare occasions on which a Government Related Entity is awarded a stand-alone rating that is higher than its sovereign owner. Furthermore, according to the agencies, Aramco's fundamental credit quality is so strong that its ratings are actually constrained by the sovereign ratings of Saudi Arabia. Think about it, this is quite a testament to Aramco's credit quality.
- First time the company has engaged with international investors in such a manner, with roadshows, presentations, substantial transparency about the company and its financials, etc. A major milestone.
- First time in the [relatively short] history of the GCC bond and sukuk markets that a borrower could issue paper priced tighter than its respective sovereign. This is big.
- This transaction could well set the tone for Aramco's much hyped and anticipated IPO, as and when that happens.

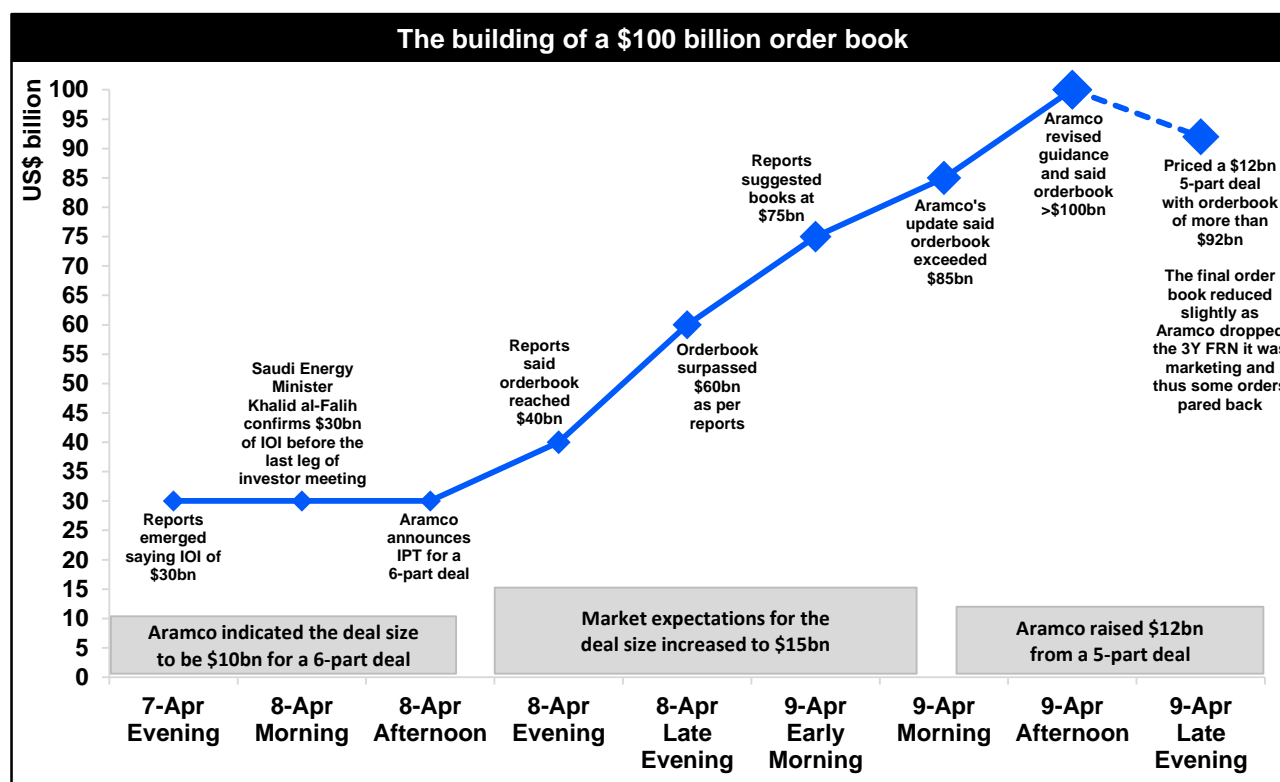
Aramco Deal Summary					
Saudi Aramco credit rating	Moody's: A1 (stable)			Fitch: A+ (stable)	
Total deal size	\$12bn				
Combined orderbook	\$92bn (7.7x oversubscribed)				
Tranche	3Y \$1bn	5Y \$2bn	10Y \$3bn	20Y \$3bn	30Y \$3bn
Maturity	16-Apr-22	16-Apr-24	16-Apr-29	16-Apr-39	16-Apr-49
IPT	T+75a	T+95a	T+125a	T+160a	T+175a
Priced	T+55	T+75	T+105	T+140	T+155
Coupon	2.750%	2.875%	3.500%	4.250%	4.375%
Indicative Yield at Pricing (estimated)	2.847%	3.062%	3.558%	4.313%	4.463%
Issue price	99.723	99.139	99.516	99.161	98.553

Source: Bloomberg/FAB

The above statistics speak for themselves. An orderbook surpassing the \$100 billion mark (largest ever for a single deal in the Emerging Markets space) with a \$12 billion deal printed. This isn't just big by GCC standards but even by global standards this transaction is noteworthy indeed. The chart below illustrates that not only did Aramco successfully print a jumbo deal at pricing tighter than the sovereign equivalent (across tenors) but the deal effectively re-priced the sovereign curve and pulled it tighter. Without a doubt, this transaction has repriced (for the better) Saudi risk in the debt capital markets. Period.

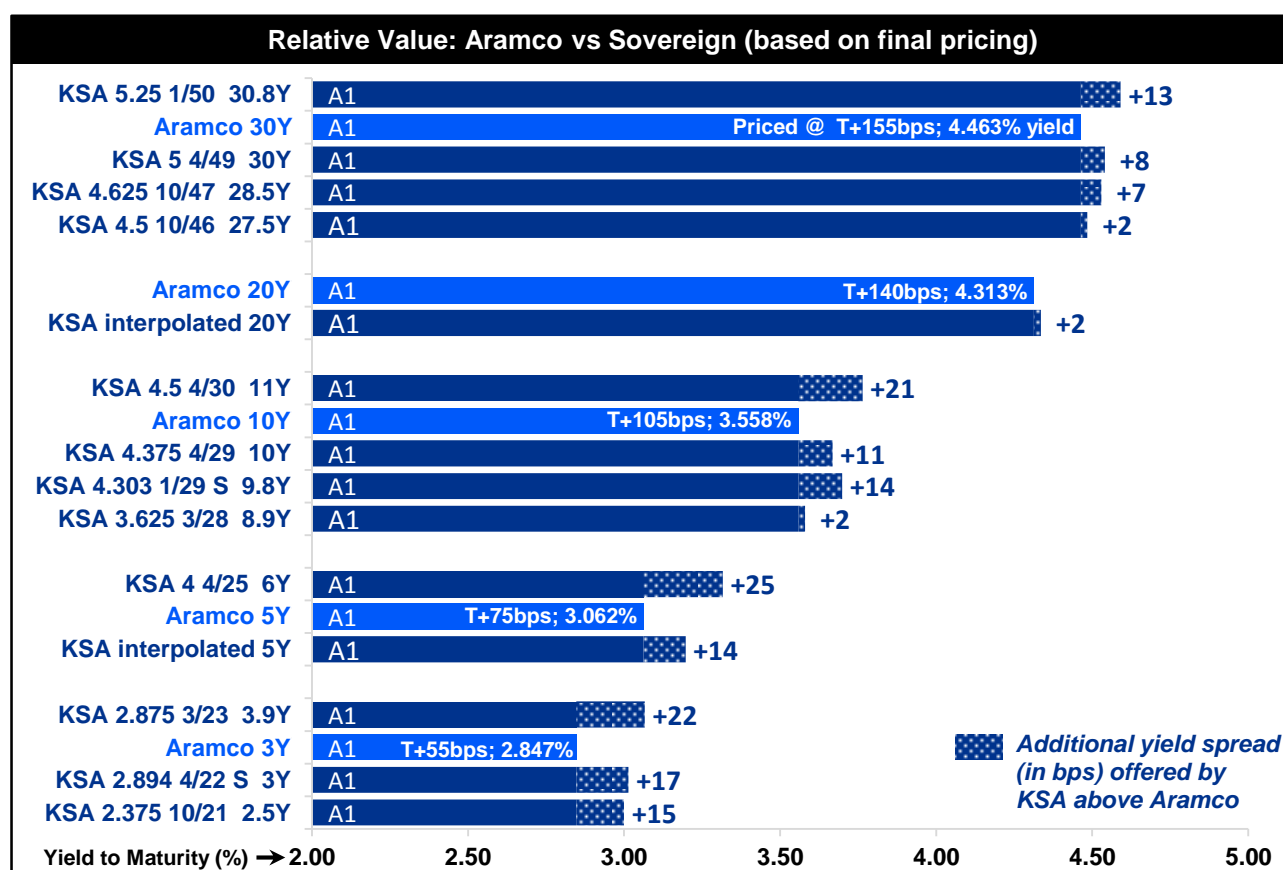


Source: Bloomberg/FAB; Credit ratings shown are ratings assigned by Fitch Ratings; \* Indicative only as it is interpolated level

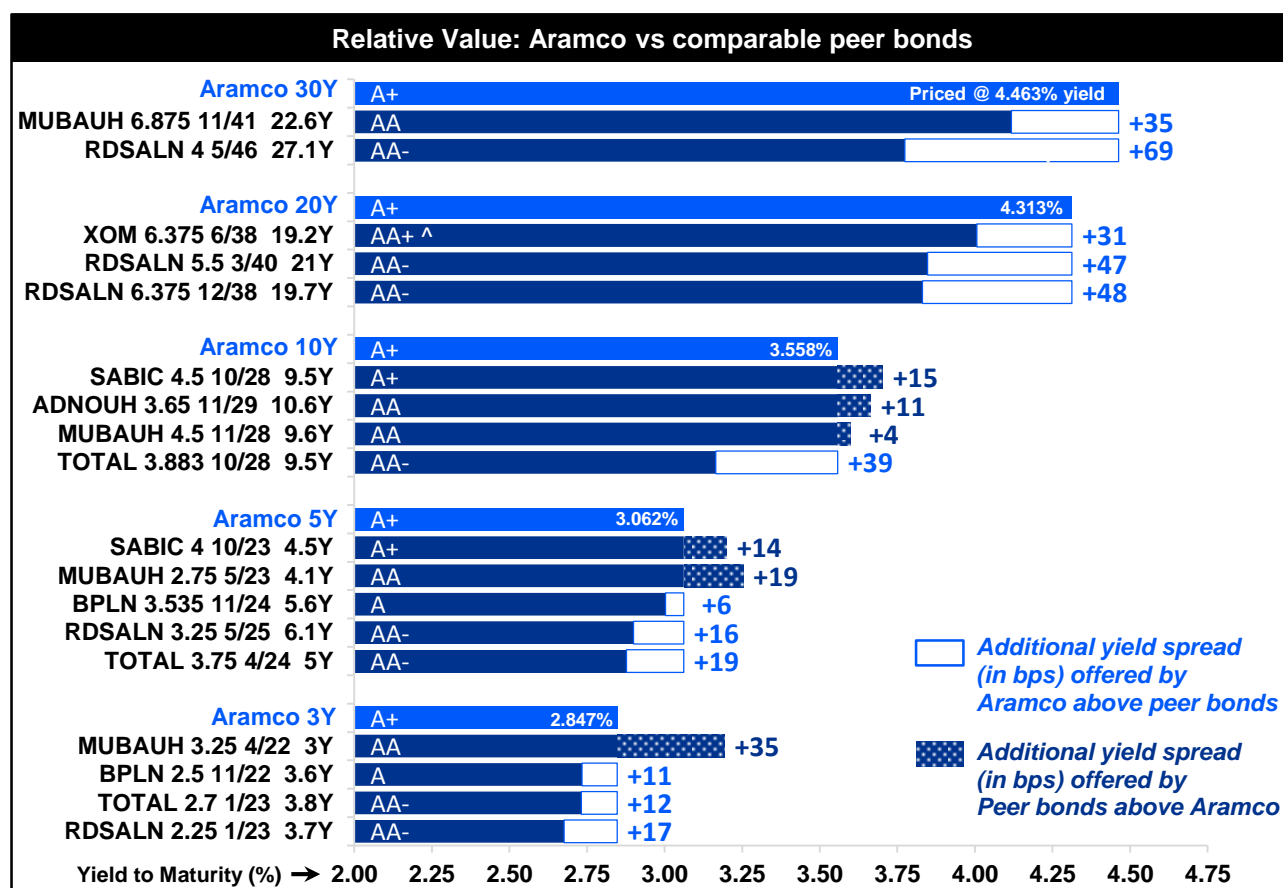


Source: Bloomberg/FAB; The timing mentioned above are as per UAE time

How do the new bonds stack up vs. the KSA sovereign bonds and also other peers in the market?



Source: Bloomberg/FAB; Credit ratings shown are ratings assigned by Fitch Ratings



Source: Bloomberg/FAB; Credit ratings shown are ratings assigned by Fitch Ratings; ^ Exxon Mobil (XOM) rating is S&P rating

### Our initial take on this transaction

While Aramco's bond issue was seen as a precursory financing arrangement for its acquisition in of a 70% stake in Sabic, worth circa \$69bn, Aramco's management have expressly stated that the deal should be considered as the company's opening up to capital markets investors and not as a financing transaction because of its "fortress-like corporate position" (referring to its cash reserves and balance sheet strength). Aramco intends to pay 50% of Sabic's acquisition price – circa \$34.5bn – at the closing of transaction, while the remainder will be paid over the next two years. According to Aramco, it will pay the remainder \$34.5bn from internal cash flows and other potential sources.

The timing of Aramco's debut bond transaction couldn't be better as it ticks many boxes both for the company and its investors:

- ✓ The global interest rate environment is more in favour of issuers than it was in past six months. In November last year 10-year US treasury yield was at 3.24% vs the current level of 2.52%
- ✓ Aramco has A+/A1 rating (caped at sovereign rating) with underlying credit quality of Aaa – this means it's a blue chip investment for investment grade investors globally
- ✓ Being a Saudi quasi sovereign, it falls under Emerging Markets and eligible for the inclusion in J.P. Morgan's Emerging Market Bond Index (EMBI) – certainly a big plus for EM investors as it is an index eligible and high quality credit
- ✓ It's a first time issuer – hence a diversification opportunity for investors that provides incremental yield without compromising on credit quality
- ✓ Rarity value – you seldom find an issuer with this kind of balance sheet strength - it's a net cash company and dwarfs the biggest of the names in the corporate world in terms of net income, ebitda, free cash flow, return on capital employed and various other metrics

Notwithstanding the size of the orderbook and the overall gravitas of the deal, we do see this transaction as ultimately being something of an exploratory exercise for Aramco's management and treasury team. Let's face it, given the company's net cash position, immense cash generating ability, and indeed the scale of its operations and balance sheet, this \$12 billion deal wasn't about fundraising. It has shown Aramco, and indeed the markets, what kind of demand there is for their paper and also what cost of funding they can realistically achieve. Furthermore, given the order book of circa \$100bn the company could have quite easily printed a much larger deal to fund the Sabic acquisition. The fact that despite the demand they printed a very restrained \$12bn deal is, in our opinion, a clear demonstration of the financial strength and flexibility that Aramco has built.

Going forward, we see a fair possibility that Aramco may come to the market more regularly in the coming years, albeit at a smaller scale than this inaugural deal, as part of a more diversified funding strategy. Watch this space for further updates.

### Market Insights & Strategy

#### FAB Global Markets

Email: [Marketinsights&strategy@bankfab.com](mailto:Marketinsights&strategy@bankfab.com)

Tel: +971 2 6110 127

Reuters dealing codes: **FABU / FABA**

Please click [here](#) to view our recent publications on MENA and Global Markets



**Disclaimer:** To the fullest extent allowed by applicable laws and regulations, First Abu Dhabi Bank (the “Bank”) and any other affiliate or subsidiary of the Bank, expressly disclaim all warranties and representations in respect of this communication. The content is confidential and is provided for your information purposes only on an “as is” and “as available” basis and no liability is accepted for or representation is made by the Bank in respect of the quality, completeness or accuracy of the information and the Bank has undertaken no independent verification in relation thereto nor is it under any duty to do so whether prepared in part or in full by the Bank or any third party. Furthermore, the Bank shall be under no obligation to provide you with any change or update in relation to said content. It is not intended for distribution to private investors or private clients and is not intended to be relied upon as advice; whether financial, legal, tax or otherwise. To the extent that you deem necessary to obtain such advice, you should consult with your independent advisors. Any content has been prepared by personnel of the Global Markets division at the Bank and does not reflect the views of the Bank as a whole or other personnel of the Bank.

The Bank processes your personal data to provide you with information or promotional and advertising communications on products, services, other events and campaigns. If you wish not to receive any emails from the Market Insights team at the Bank, please click [here](#) to send us your request to unsubscribe, and you shall no longer receive such information.

You are entitled according to the applicable laws to exercise your rights to access, to rectification, to erasure and to portability of your personal data, to restrict the use of and to object to the processing of your personal data. You may exercise your aforesaid rights by sending your request to FAB at the following address: [privacy@bankfab.com](mailto:privacy@bankfab.com).