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A MARKAZ Subsidiary

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GCC Risk Premium – H1 2020

A Toolkit for Corporate Financiers



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Chapter 1

Executive Summary

The outbreak of the COVID-19 pandemic in early 2020 in China and its worldwide spread has had a mixed impact on the cost of capital of GCC countries. GCC countries with investment grade ratings have seen a fall in their cost of capital while Bahrain and Oman, the two GCC members with sub-investment grade rating have seen their cost of capital increase in H1 2020 compared to H1 2019. An important factor has been the flight to safety by investors, which has resulted in a fall in 10-year U.S treasury yields as well as that of GCC countries' sovereign yields except Bahrain and Oman. The successive rate cuts by the U.S. Fed in March 2020 have also helped in significant decrease in the sovereign yields for Saudi Arabia, Kuwait, Qatar and UAE. This has resulted in overall reduction in cost of capital for these countries.

In June 2020, Moody's Investors Service downgraded the long-term issuer ratings of Oman to 'Ba3' with negative outlook from 'Ba2' negative outlook. The ratings agency had earlier downgraded Oman from 'Ba1' to 'Ba2'. It cited the low oil-price environment, which is likely to persist in the medium term and erosion in the foreign currency sovereign reserves as reasons for the downgrade. As a result, Equity Risk Premium for Oman increased.

While Bahrain did not see a downgrade from Moody's in 2020, S&P Global ratings downgraded Bahrain from BB to BB- in March 2020. In May 2020, Bahrain received USD 4.57billion in financial aid from Saudi Arabia, Kuwait and UAE as a part of the rescue package agreed in 2018. However, S&P believes Bahrain would need additional support

Cost of capital under the CDS method has decreased for all GCC countries except Oman, Dubai and Bahrain primarily due to the fall in risk-free rates and due to the lower CDS spreads for the respective countries.

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