المركز
MARKAZ

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GCC Stock Market Outlook 2019

Investment Focus Topics:

1. Kuwait MSCI index inclusion
2. Dubai market meltdown
3. REITs: A rapidly evolving asset class

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Chapter 1

Executive Summary

Expectations for 2019

Title	KSA	Kuwait	UAE	Qatar	Oman	Bahrain
Economic Factors	Neutral	Positive	Positive	Neutral	Positive	Negative
Valuation Attraction	Neutral	Positive	Positive	Neutral	Positive	Positive
Earnings Growth Potential	Negative	Positive	Positive	Positive	Positive	Negative
Market Liquidity	Neutral	Negative	Negative	Negative	Negative	Negative
			Abu Dhabi / Dubai			
Overall Market View	Neutral	Positive	Positive / Positive	Neutral	Positive	Negative

Source: Markaz Research

Amidst muted growth expectations in global markets, economic outlook for the GCC region as a whole remains positive, as the surge in oil revenues and fiscal reforms of yesteryears will provide the necessary cushion for GCC countries to support economic growth through capital expenditure. Although the recovery in Oil prices did not last the entirety of the year, GCC economies witnessed a sizeable increase in oil revenues. Their fiscal and external balances started to recover after three lacklustre years with only Bahrain and Oman running twin deficits in 2018. With the exception of Bahrain, where there is weakness in government finances, economic factors remain largely favourable.

Growth in corporate earnings is expected to witness an uptick in the GCC during 2019 with the exception of Bahrain and Saudi Arabia. Banks will be the primary growth drivers, as the sector is expected to see a rise in profitability and credit growth due to tailwinds such as rising interest rates and new infrastructure projects. Commodity related companies are likely to see their earnings drop due to the fall in oil prices while the construction sector is expected to mildly rebound after years of underperformance.

From a valuation perspective, GCC markets except Saudi Arabia and Qatar remain at attractive levels. As earnings are expected to remain flat for Saudi stocks, it becomes difficult to justify their premium valuations. Similarly, Qatar is expected to undergo consolidation in 2019 after witnessing a rally during the second half of 2018. Market liquidity remains to be a pain point for GCC equity markets as institutional and foreign investor participation continues to remain low, weighed down by geopolitical concerns.

At the start of 2018, we were neutral on the Saudi Arabia, UAE and Kuwait, while remaining negative on Qatar. Saudi Arabia and Kuwait were in line with our expectations, gaining 8.3% and 7.8% respectively during the year. The UAE was a mixed bag, with Abu Dhabi and Dubai moving in opposite directions. Rise in Oil prices and government support supplemented the growth of Abu Dhabi while the slowdown of economic growth and the weakness in real estate market weighed in on Dubai. Qatar markets performed contrary to our expectations as the country successfully overcame the effects of the diplomatic standoff, which was initially expected to have a bearing on the country's economy. Quick establishment of alternate trade routes and the support lent to the banking system through the injection of government deposits helped the economy to stage a turnaround.

Chapter 2

Looking Back at 2018

GCC markets stood tall in a year that was characterized by a rout on the global equities. A bear hold that was predominantly isolated to emerging markets for most parts of the year, percolated to the developed markets as well. Strong economic growth coupled with a rising interest rate environment in the U.S. triggered a selloff in emerging market equities. Additional headwinds in the form of a U.S.-China trade war and rise in crude prices exacerbated things further, as investor sentiment deteriorated. However, the tides changed course towards the end of the year with the U.S. Fed aggressively hiking interest rates in spite of the muted outlook on global economic growth. U.S equity markets and the U.S. Dollar fell steeply in December, erasing the gains that were accumulated during the year.

At the start of 2018 (GCC Stock Market Outlook 2018), we were neutral on the Saudi Arabia, UAE and Kuwait, while remaining negative on Qatar. Qatar markets performed contrary to our expectations, bouncing back by 20.8% in 2018 after successfully mitigating the effects of the diplomatic crisis, which began in 2017 with its neighbours Saudi Arabia, UAE and Bahrain. Qatar was quick to establish alternate trade routes and ably supported its banking system though the injection of government deposits. This enabled Qatar's economy to remain on track and grow at a steady rate.

Saudi Arabia's market performed exceedingly well during the first half of 2018, aided by the emerging market upgrade bestowed upon it by renowned index providers MSCI and FTSE. As oil prices were also on a strong footing during the period, Saudi Arabia's Tadawul index witnessed an upshot of 15.1%. However, the effects weaned off in the second half of the year, as the yearly gains dropped to 8.3%, in line with our neutral expectations. Similarly, Kuwait continued its good run, gaining 7.8%, slightly lower than the 10.3% gain witnessed in 2017. Solid earnings growth of banks and the progress of capital market reforms helped Kuwait's market to end the year on a positive note for the second time in succession.

Predictions at 2018-Start & Actual Performance

Country	Expectations in 2018	Actual Performance
Saudi Arabia	Neutral	8.3%
United Arab Emirates	Neutral	-24.9% (Dubai) 11.7% (Abu Dhabi)
Kuwait	Neutral	7.8%
Qatar	Negative	20.8%
Oman	Neutral	-15.2%
Bahrain	Negative	0.4%

Source: Reuters

The UAE markets were a mixed bag, with Abu Dhabi and Dubai moving in opposite directions. As expected, Abu Dhabi markets rebounded in 2018 with gains of 11.7%, second only to Qatar in the GCC. The uptick in oil prices and the economic stimulus provided by the government supplemented growth across sectors. In stark contrast, Dubai markets have been languishing with a negative yearly return of 24.9%, its lowest since 2018. The overall slowdown of Dubai's economy in addition to the weakness of the real estate market has contributed to the underperformance of the emirate. Similarly, Oman markets also ended the year on a negative note, losing 15.2% while Bahrain managed to post a mild gain of 0.4% in 2018.

Chapter 3

Country-wise Performance Analysis

Saudi Arabia

Snapshot

Index Name	TASI Index
Last Close (Dec 31, 2018)	7,827
2018 Change (%)	8.31%
P/E TTM	17.6
Dividend Yield	3.40%
Listed Companies	185
No of Large Cap Companies	14
No of Mid Cap Companies	27
No of Small Cap Companies	134
Market Capitalization (Dec-2018) (USD Bn)	492
Large Cap - Mcap (Dec-2018) (USD Bn)	345
Mid Cap - Mcap (Dec-2018) (USD Bn)	98
Small Cap - Mcap (Dec-2018) (USD Bn)	48
Turnover Ratio (Dec-2018)	47%

Source: Reuters;
Note: Turnover is a measure of stock liquidity calculated by dividing the value of shares traded over a period by the average market cap for the period.

2018 has been a volatile year for the Saudi stock market. The Tadawul index started on a strong note as the largest market in the GCC region was upgraded to 'Emerging Market' status by both index providers, FTSE Russell and MSCI. But the market soon lost ground as a sharp fall seen in oil prices coupled with political uncertainties significantly slowed down the pace of the rise in the stock market which then had to settle with a yearly gain of 8.31%.

Growth in corporate earnings remained flat for the first nine months of 2018 when compared to the same period in the previous year. Media and entertainment sector led the way in earnings growth, with a rise of 38.3% (YoY) in Q3 2018 after the Saudi government lifted the ban on movie theatres. The banking and telecommunications sector followed suit, registering gains of 28.9% and 26.6%, respectively. Banking sector's profitability was supported by a rise in their net interest income in the increasing interest rate environment. With the sharp fall in oil prices, many of the sectors such as retail, construction, hotels & tourism and transport sectors reported lower earnings in 2018. The weakest performing sectors were Real Estate and Utilities with falls of 30.1% and 24.9% respectively.

Al-Rajhi bank and Saudi telecom were the top performers amongst the Saudi heavyweights with the stocks rising 35% and 34% respectively during the year. Saudi Electricity Company was the biggest loser among the blue chips with a fall of 28% during 2018.

OPEC members along with Russia have decided on cutting down on oil production so as to support oil prices. However, record levels of production seen in the United States along with a slowdown in global growth forecasts by the IMF, will continue to add uncertainty to the market as we step into 2019.

United Arab Emirates

Snapshot

Index Name	Dubai Index	Abu Dhabi Index
Last Close (Dec 31, 2018)	2,530	4,915
2018 Change (%)	-24.93%	11.75%
P/E TTM	7.1	12.2
Dividend Yield	6.2	5.2
Listed Companies	123	
No of Large Cap Companies	10	
No of Mid Cap Companies	18	
No of Small Cap Companies	95	
Market Capitalization (Dec-2018) (USD Bn)	240	
Large Cap - Mcap (Dec-2018) (USD Bn)	167	
Mid Cap - Mcap (Dec-2018) (USD Bn)	48	
Small Cap - Mcap (Dec-2018) (USD Bn)	24	
Turnover Ratio (Dec-2018)	11%	

Source: Reuters;

The Dubai financial market was the worst performing GCC market for the year 2018, with an YTD loss of 24.93%. All the sectors registered a negative performance with Consumer Staples and Investment and Financial Services being the worst of the lot with a loss of 62% and 44% respectively. Real Estate and Construction sector, which commands the highest weightage in the DFM General Index has seen a drop of 39% in 2018. The primary reason for the continued drop in the market can be attributed to the real estate sector as the growing supply remains to outpace the demand in the market. According to preliminary October data from STR, Dubai hotel occupancy fell 4.3% to 75.2%, Average Daily Rate (ADR) dropped 6.1% to AED 685.41 (USD 186.63) and Revenue per Available Room (RevPAR) declined 10.2% to AED 515.64 (USD 140.41).

However, signs of recovery can be seen as November's Dubai Economy Tracker Index registered a value of 55.3, up from October's 31-month low of 52.5 and the highest since June. Construction was the strongest-performing sector in November (57.5), followed by wholesale & retail (55.4) and travel & tourism (52.8). Dubai Expo 2020 projects were cited as a key reason for optimism in the construction sector. Dubai's GDP is likely to grow 4.2% in 2019 due to government infrastructure spending ahead of Expo 2020 compared to 3.4% this year. It is estimated that the mega event will generate 275,000 direct jobs to host the six-month-long exhibition. Since the Expo 2020 site will be transformed into a legacy for tourist attraction, the site will continue to generate substantial economic activity for the Emirate, driving sectors like hospitality, travel and tourism, aviation, construction, retail and real estate, among others.[1]

Among Dubai's blue chips, banking stocks were the only ones that returned a positive yearly gain for 2018. Emirates Islamic Bank, Emirates NBD and Mashreq bank gained 1.9%, 8.4% and 11.4% for the year respectively. Emaar properties, the Dubai based property giant, witnessed its stock price fall by 35.3% in 2018, as its quarterly earnings growth slowed down in 2018. DP World was another blue chip stock that corrected sharply, falling by 31.6% during the year, as the port operator witnessed deceleration in the growth of container volumes when compared to 2017.

[1] International Monetary Fund's mission chief for the UAE

The Abu Dhabi Securities Exchange on the other hand was the second best performer in the GCC market with a yearly gain of 11.75%, buoyed by healthy quarterly results of listed companies and stronger investor sentiment boosted by government-led stimulus measures. The superior performance of banking stocks was driven by improved loan yields from rising interest rates and improving asset quality and provision levels after the IFRS 9 implementation remaining within guidance. The Banking index, which accounts for 60% of the overall index composition, saw a rise of 27% for the year 2018. Abu Dhabi holds 90% of the country's oil reserves and the impact of fall in oil prices can be seen on the energy sector. The Energy sector saw strong gains up until the third quarter of 2018, however, due to the sharp decline in the oil prices thereafter, the sector was hit hard, wiping away most of the earnings and finally ending the year with a gain of 16%.

For the nine months of 2018, UAE corporate earnings were up by 13.3% compared to the same period last year. Among the Blue chips of UAE, First Abu Dhabi Bank (FAB) outperformed analysts' expectations as it reported a 16% jump in its net profits for the third quarter of 2018. Abu Dhabi Commercial bank saw a rise of 9% in its net interest income which helped push the net profit higher by 9% for Q3 of 2018. First Abu Dhabi bank and Abu Dhabi Commercial bank saw a rise of 38% and 20% in their stock prices, respectively.

Given large fiscal buffers, ample spare capacity, and rising investment needs for Expo 2020, the government has appropriately switched to providing stimulus to the economy. The introduction of VAT in 2018 has been a historic milestone and is expected to substantially strengthen and diversify government revenues in the coming years. The investment law, which seeks to allow more than 49% ownership to foreign investors in some specific business sectors, is in effect. UAE remained the major destination of FDI inflows at about USD 11 billion in 2017, accounting for 22% of total FDI to the Middle East and North Africa region and Dubai's foreign direct investment flows soared 26% in the first half of this year to USD 4.84 billion.[2]

[2] Institute of International Finance

Qatar

Snapshot

Index Name	Qatar Index
Last Close (Dec 31, 2018)	10,299
2018 Change (%)	20.83%
P/E TTM	14.4
Dividend Yield	3.28%
Listed Companies	45
No of Large Cap Companies	7
No of Mid Cap Companies	10
No of Small Cap Companies	28
Market Capitalization (Dec-2018) (USD Bn)	160
Large Cap - Mcap (Dec-2018) (USD Bn)	112
Mid Cap - Mcap (Dec-2018) (USD Bn)	33
Small Cap - Mcap (Dec-2018) (USD Bn)	15
Turnover Ratio (Dec-2018)	11%

Source: Reuters;

Registering the best performance among its GCC peers, Qatar Stock Index saw a growth of 20.83% in 2018. Most of the sectors had a positive year with Banks and Financial Services and Consumer Goods and Services registering the highest growth of 43% and 36% respectively. Qatar's banking sector remains healthy overall, reflecting high asset quality and strong capitalization.

Analysts at the ratings agency say the blockade forced Qatar to diversify its revenue sources, ultimately making it more self-sufficient, which caused the market to rally in 2018. Trade has been re-routed through other countries in the region, culminating in significant recovery in imports.

In December 2018, Qatar announced its planned departure from OPEC, the 15-member cartel of oil-exporting countries whose largest producer is Saudi Arabia. The withdrawal from OPEC was justified by Qatar's long-term strategy of shifting focus towards gas and away from oil. The country believes this move will enable it to work towards cementing its position as the world's top LNG exporter. The market has taken this news positively since the index has gained an additional 1.76% since the announcement.

Corporate profits rose 8.2% on a year-on-year basis. Qatar's banking system remains healthy with ample liquidity, high asset quality and strong capitalisation. Deposit growth of 6% and loan growth of 5% is expected this year, which should result in a further decline in the loan-to-deposit ratio.[3] The blue chips saw a strong growth this year led by the strength from the banking sector. Qatar National Bank and Qatar Islamic bank were the top blue chip performers with the share price rising 55% and 57%, respectively for the year. Industries Qatar which registered a drop of 31% in its net profits in Q3 of 2017, saw a 58% rise in its net profits on the back of higher products prices. Consequently, its share price has registered a growth of 38% in 2018.

Qatar's biggest trading partners Japan, South Korea, China, and India, which buy more than 70% of natural gas from it are all outside the politically volatile Middle East. The real estate sector which was under considerable pressure last year has seen a healthy rebound in 2018 with the sector gaining 14.2% this year. Qatar's real estate sector is expected to see more growth, especially in the beginning of next year, due to various factors, including the government support and legislative changes on the ownership of properties by foreign investors, which is likely to encourage investments in this sector.

[3] Qatar Economic insight 2018

Kuwait

Snapshot

Index Name	Kuwait Price Index
Last Close (Dec 31, 2018)	5,652
2018 Change (%)	7.78%
P/E TTM	14.7
Dividend Yield	3.46%
Listed Companies	175
No of Large Cap Companies	15
No of Mid Cap Companies	32
No of Small Cap Companies	128
Market Capitalization (Dec-2018) (USD Bn)	96
Large Cap - Mcap (Dec-2018) (USD Bn)	68
Mid Cap - Mcap (Dec-2018) (USD Bn)	20
Small Cap - Mcap (Dec-2018) (USD Bn)	9
Turnover Ratio (Dec-2018)	14%

Source: Reuters;

Kuwait continued to be a positive performer on the back of strong economic reforms and banking fundamentals. Earlier in 2018, Boursa Kuwait, which was established in 2014 as the first step towards privatizing the Kuwait Stock Exchange (KSE), announced that it has officially assumed responsibility for the management of KSE's activities. The market has been subsequently divided into three segments (Premier, Main, and Auction Markets), with the Premier Market composed of the largest and most liquid companies. The market segmentation is designed to incentivize companies to improve liquidity and transparency. Boursa Kuwait introduced new indexes designed primarily to measure the performance of the new market segments and the market as a whole. Unlike the old price index, all indexes will be market capitalization-weighted to better reflect market performance.

Due to the positive reforms undertaken by Boursa Kuwait, Kuwait was upgraded to emerging market status by FTSE Russell's index. Moreover, global index provider MSCI will consider reclassifying Kuwait from Frontier Market to Emerging Market status at its annual market review in 2019. The index inclusion is expected to create a fund inflow of close to USD 3-6 billion into the economy. This has created a positive sentiment for the country among its investors who have helped push the yearly gains of Kuwait to 7.8% for 2018.

Corporate earnings have seen a growth of 8.5% in Q3 of 2018 when compared to the same period last year. Boubyan bank continues to be the leading performer among blue chips, registering a price return of 35% in 2018. Its performance is seen as a continued realization of the Bank's 2020 strategy to build on robust domestic foundations, as they scale up their core business by focusing on affluent and high net worth clients and to be the primary banker for large and mid-market corporates. National Bank of Kuwait saw a positive share price growth of 20%. The rise in personal loan limits by the Central Bank of Kuwait, coupled with increasing the level of supervision on high values loans and putting a leash on speculative lending, would help boost the dwindling credit growth in the country and strengthen financial health of both parties.

With the largest fiscal buffers among its GCC peers as well as a very low fiscal breakeven oil price, Kuwait has insulated itself from future uncertainties in the form of losses due to fall in oil as well as geo political uncertainties. However, falling oil prices paired with the low levels of liquidity seen in the markets will continue to add pressure to the market. Considering Kuwait's aim to transform itself into a regional financial and cultural hub by 2035, attracting foreign investments remains paramount in its plans to achieve economic diversification.

What to Expect in 2019?

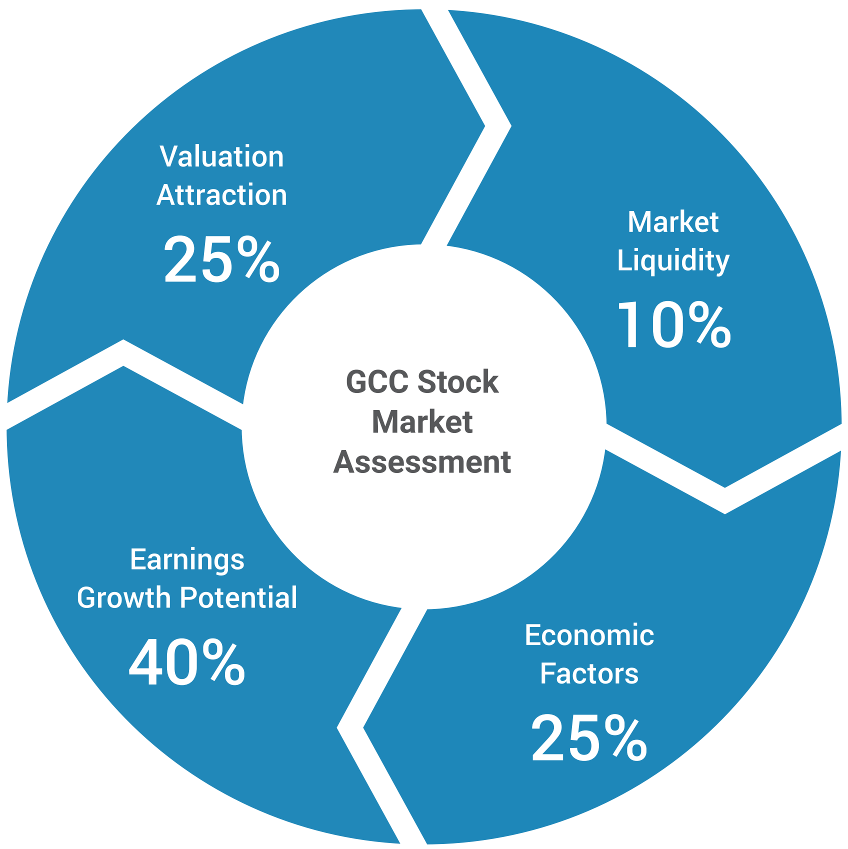
Economic conditions in the Gulf region are set to improve in 2019, after the rebound of oil prices witnessed in the first three quarters of 2018. Despite the correction seen in the closing months of 2018, oil prices are expected to stabilize at levels close to USD 65 per barrel, giving leeway for GCC government to adopt an expansionary stance to support economic growth through capital expenditure.

We remain positive on the UAE, Kuwait and Oman markets based on macroeconomic parameters, earnings growth potential and the attractiveness of valuations. Saudi Arabia on the other hand has been affirmed with a neutral outlook for 2019 despite the government hinting at extensive public spending. Clouds over earnings growth potential and premium valuations compared to GCC counterparts have been contributors to the neutral outlook on the economy.

Contrary to our expectations, Qatar emerged to become the best performing market in the GCC region during 2018 with a return of 20.8%. Taking the rally into consideration, we tone down our expectations for Qatar in 2019, with a bit of consolidation expected to come in the next few months. Bahrain is the only GCC country that has warranted a negative outlook moving into 2019 with significant weaknesses remaining in the government's finances. Market liquidity remains the major pain point for all GCC countries and is expected to grapple the regional stock markets in the forthcoming year as well.

We base our analysis on a set of four factors which we believe will influence and impact market performance. We have assigned weights to each of these factors based on our assumption about the degree of influence it would have on the stock market performance as a whole in 2019.

Four – Forces Framework



Source: Markaz

Economic Parameters

1. **Economic Growth**

Real GDP Growth (in %)

Real GDP Growth	KSA	Kuwait	UAE	Qatar	Oman	Bahrain
(2009-2014 Avg.)	4.1	4.8	4.9	11.2	3.7	5.1
(2015)	4.1	-1.0	5.1	3.7	4.7	2.9
(2016)	1.7	2.2	3.0	2.1	5.0	3.5
(2017)	-0.9	-3.3	0.8	1.6	-0.9	3.8
(2018 e)	2.2	2.3	2.9	2.7	1.9	3.2
(2019 f)	**2.4**	**4.1**	**3.7**	**2.8**	**5.0**	**2.6**

Real Oil GDP Growth Rates (in %)

	KSA	Kuwait	UAE	Qatar	Oman	Bahrain
(2009-2014 Avg.)	2.1	4.0	2.6	10.4	1.4	0.4
(2015)	5.3	-1.7	5.2	-0.6	4.5	-0.1
(2016)	3.6	2.3	2.6	-0.9	3.6	-0.1
(2017)	-3.1	-7.8	-3.0	-0.7	-2.5	-0.7
(2018 e)	2.2	1.4	2.9	1.0	1.7	0.3
(2019 f)	**2.8**	**4.5**	**3.1**	**1.2**	**7.5**	**0.2**

Real Non-Oil GDP Growth Rates (in %)

Real Non-Oil GDP Growth	KSA	Kuwait	UAE	Qatar	Oman	Bahrain
(2009-2014 Avg.)	6.5	6.6	6.3	12.6	7.0	7.4
(2015)	3.2	0.0	5.0	8.5	4.8	3.6
(2016)	0.2	2.0	3.2	5.3	6.2	4.3
(2017)	1.1	3.2	2.5	3.8	0.5	4.8
(2018 e)	2.3	3.5	2.9	4.3	2.0	3.9
(2019 f)	**2.1**	**3.5**	**3.9**	**4.3**	**3.0**	**3.1**

Source: IMF

In 2018, all GCC economies barring Bahrain grew at a pace brisker than what was seen in 2017, primarily due to the uptick in Oil prices during the year. Oil prices went on a rally in the first three quarters of 2018, fuelled by OPEC-related oil production cuts, U.S. sanctions on Iran, and supply shortages from Venezuela and Libya. Price of Brent crude closed at USD 86.29 per barrel on October 3 2018, the highest level since the beginning of 2015. However, prices corrected sharply at the end of the year, shedding more than 20% in November alone, due to concerns over a slowdown in global economic growth for 2019.

Weighing in factors such as the slowdown of global demand, OPEC's resumption of production cuts, U.S. Shale production and the trade war, oil prices are expected to stabilize at around at USD 65 per barrel. Tailwinds in the form of oil prices, in addition to the implementation of public investment projects, preparations for Expo 2020 and FIFA World Cup 2022 bode well for GCC countries, who are expected to sustain their growth through to 2019. Real GDP for GCC economies is forecasted to grow by 3% in 2019, followed by a growth of 2.4% in 2018 and a 0.4% contraction in 2017.

Kuwait's Real GDP is forecasted to grow by 4.1% in 2019, driven by the rebound in Oil GDP from 1.4% in 2018 and -7.8% in 2017 to 4.5% in 2019. The implementation of projects that are in line with Kuwait's five year development plan is expected to be one of the positive drivers for economic growth in the country. Despite the embargo laid on Qatar in 2017, the country has managed to show resilience, contrary to populist views. With preparations for the FIFA World Cup 2022 gaining momentum, its economy is expected to grow steadily at 2.8% in 2019. Bahrain is the only GCC economy whose real GDP growth is expected to slow down when compared to 2018. The weakness in its fiscal position is expected to remain, constraining the government from effectively supporting its economy.

2. Inflation

Inflation, annual change (%)	KSA	Kuwait	UAE	Qatar	Oman	Bahrain
(2009-2014 Avg.)	2.2	3.2	4.1	4.3	2.5	1.7
(2015)	1.3	3.7	4.1	1.8	0.1	1.8
(2016)	2.0	3.5	1.6	2.7	1.1	2.8
(2017)	-0.9	1.5	2.0	0.4	1.6	1.4
(2018 e)	2.6	0.8	3.5	3.7	1.5	3.0
(2019 f)	**2.0**	**3.0**	**1.9**	**3.5**	**3.2**	**4.8**

Source: IMF

Barring Kuwait and Oman, inflation has risen amongst the GCC countries during 2018. Introduction of VAT, rise in fuel prices and other consolidation measures have had an inflationary effect on consumer prices in Saudi Arabia and the UAE during 2018. Moving forward, inflation is expected to ease in 2019 for both Saudi Arabia and the UAE, down to 2.0% and 1.9% from a higher level of 2.6% and 3.5% respectively seen in 2018. The weakening position of Bahrain and Oman will nudge both countries to pursue further fiscal consolidation measures, triggering a rise in consumer prices, consequently affecting their inflation. The introduction of VAT in Bahrain from 2019 is expected to have similar inflationary effects as witnessed in the case of UAE and Saudi Arabia during 2018. Bahrain's inflation is expected to rise to 4.8% in 2019, higher than 3.0% witnessed in 2018. The trade blockade of Qatar by some of the GCC peers caused inflation to edge up in 2018 to 3.7% compared to 0.4% in 2017. Importing goods from newer destinations and the surge in investments to support self-sufficiency helped Qatar satisfy its consumption/commodity needs. However, the resultant higher transportation cost and increased outlays at home could fuel inflation. The trend is expected to extend into 2019, resulting in an inflation of 3.5% in 2019.

3. Fiscal Balance

The fiscal position of GCC countries in 2018 turned out to be far better than what was predicted a year ago. The rise in oil prices triggered an upsurge of oil and non-oil activity in the region, resulting in considerable improvement of external and fiscal balances. The increase in oil revenues eased the pressure on GCC governments and provided fiscal space for them to pursue public spending. However, with the U.S. Fed expected to make a few more rate hikes in 2019, GCC economies need to exhibit fiscal prudence and pursue reforms that would help them diversify from oil, as high oil prices could very well be a temporary phenomenon considering the headwinds that are around the corner.

Fiscal Balance

Fiscal Balance, as % of GDP	KSA	Kuwait	UAE	Qatar	Oman	Bahrain
(2009-2014 Avg.)	7.3	28.4	7.3	10.6	8.0	-0.9
(2015)	-15.8	5.6	-3.4	5.4	-15.9	-18.4
(2016)	-17.2	0.6	-2.0	-4.7	-21.2	-17.6
(2017)	-9.3	6.6	-1.6	-1.6	-12.9	-14.3
(2018 e)	-4.6	11.6	0.6	3.6	-2.0	-8.9
(2019 f)	**-1.7**	**12.0**	**1.3**	**10.5**	**0.8**	**-8.2**

Source: IMF

Saudi Arabia's fiscal deficit has been narrowing down since 2016, where its deficit was at 17.2% of GDP. The rebound in oil prices and the introduction of fiscal consolidation measures have helped the country reduce its deficit over the years. The trend is expected to continue with its deficit lowering to 1.7% in 2019. Similarly, the UAE and Oman have improved their fiscal positions over the years and are projected to run fiscal surpluses for 2019. Considering the fiscal space available to Saudi Arabia and the UAE, they have the headroom to adopt a slightly more expansionary fiscal policy to revive economic growth in the respetive countries and boost the non-oil industry.

Kuwait and Qatar are in the strongest positions among GCC economies, with fiscal surpluses of 12.0% and 10.5% of their respective GDPs for 2019. Their fiscal position is well balanced and expected to improve in the coming years. On the contrary, Bahrain remains the weakest among GCC economies, posting a deficit of 8.9% of the GDP in 2018 in spite of the rise in oil prices. The financial aid of USD 10 billion promised by its neighbours is expected to improve its fiscal position and help support its economy. Nevertheless, it's fiscal deficit is expected to be much higher than other GCC economies at 8.2% of the country's GDP in 2019.

Fiscal reforms often invloves trade-offs and can be painful to absorb in the short term. However, the long-term outcomes are expected to be beneficial in the quest of GCC countries to quell the over-dependence on oil. Due to this dependence, fiscal balances of GCC countries are still highly vulnerable to the fluctuations in oil prices. The cushion currently provided by higher oil prices should be used as an opportunity to strengthen their fiscal frameworks so that they have the required fiscal space to provide policy interventions when the macroeconomic climate turns unfavourable. Increasing revenues from non-oil sources also remain paramount in strengthening the fiscal reslience of GCC countries. Reforms such as reducing current expenditures in the form of subsidies and wages, introducing VAT followed by the implementation of a unified corporate taxation structure need to be mobilized in order to reduce the fiscal dependence on oil.

4. Current Account Balance

Current Account Balance (% of GDP)	KSA	Kuwait	UAE	Qatar	Oman	Bahrain
(2009-2014 Avg.)	16.3	33.3	10.6	21.0	8.9	6.3
(2015)	-8.7	3.5	4.9	8.5	-15.9	-2.4
(2016)	-3.7	-4.6	3.7	-5.5	-18.7	-4.6
(2017)	2.2	5.9	6.9	3.8	-15.2	-4.5
(2018 e)	8.4	11.3	7.2	4.8	-3.3	-2.5
(2019 f)	**8.8**	**11.0**	**7.5**	**6.6**	**-0.5**	**-2.3**

Source: IMF

Production cuts undertaken by OPEC in addition to the supply constraints in countries like Iran, Venezuela and Libya have had a bearing on oil prices in 2018. GCC countries, whose export revenue is heavily dependent on Oil and Gas exports witnessed a considerable improvement in their current account balances during 2018 when compared to the previous year. The cumulative current account balance of oil importing countries shifted from a deficit of USD 68 billion in 2016 to a surplus of USD 120 billion in 2018.

Saudi Arabia's current account surplus increased from 2.2% of its GDP in 2017 to 8.4% in 2018, primarily due to the rise in oil prices. The surplus is expected to remain steady at 8.8% of its GDP in 2019, with a fall in expat remittances and imports. UAE's current account surplus is expected to marginally improve in 2019, at 7.5% of GDP, as oil revenues rise with increased oil production, complemented by non-oil exports and tourism. Qatar is expected to post a surplus of 6.6% of GDP in 2019, lower than its GCC counterparts due to the effects of the diplomatic crisis. Despite the rise in export revenues, Qatar has had to revisit its imports and change its trade partners, resulting in higher import costs. Qatar has also exited the OPEC and stated its intention to concentrate on Natural Gas over Oil. Kuwait's current account balance is expected to be the highest among all GCC nations in 2019. Historically, Kuwait's imports have remained low compared to its exports. It enjoyed high trade surpluses with oil trading at its all-time high, with an average current account balance between 2009 and 2014 at 33% of its GDP.

5. Gross Debt

Gross Debt (% of GDP)	KSA	Kuwait	UAE	Qatar	Oman	Bahrain
(2009-2014 Avg.)	36.5	13.4	11.0	30.9	11.6	28.3
(2015)	5.8	4.7	18.7	35.5	15.5	66.0
(2016)	13.1	9.9	20.2	46.7	32.5	81.4
(2017)	17.2	20.6	19.7	53.8	46.9	88.5
(2018 e)	19.4	18.8	17.8	53.4	48.7	88.4
(2019 f)	**20.4**	**25.4**	**17.6**	**48.7**	**45.1**	**91.7**

Source: IMF

GCC countries resorted to a combination of external borrowing and draw-down from reserves to plug the fiscal and current account deficits ever since the prices of Oil fell. They have accessed both international and domestic markets to finance their budget shortfalls in the past few years. The current year has been a difficult one for global bond markets with the rise in interest rates, dampening expectations of global growth and volatility in oil prices playing spoilsport as investor demand continues to fall. Having the global scenario at the backdrop, GCC bonds and sukuk markets have fared out slightly better than its emerging market counterparts in 2018. The oil price rally witnessed in the first three quarters of the year boded well for the GCC, as activity in the primary and secondary market picked up due to the positive outlook for the gulf nations.

The outlook for GCC bond market in 2019 remains clouded as fed rates are expected to be hiked further in the coming year. The fallout of U.S.-China trade war and the underperformance of Europe might have a telling impact on global growth moving forward, also affecting oil demand and prices. Considering the correlation between oil price and factors such as activity in the GCC market and Credit ratings in the past, the GCC bond markets need to contend with a few more headwinds in the year to come.

The UAE has the lowest debt to GDP among GCC countries at 17.8% in 2018 and is expected to carry forward this trend in 2019 as well, with a forecasted debt to GDP ratio of 17.6%. The UAE has been lagging behind its GCC neighbors in the local currency denominated bond markets unlike the USD-denominated bond market. In order to bridge the gap, UAE finalized and announced its federal debt law in 2018. It will allow the country to establish a federal debt management office and seek a credit rating for the country. Until now, the sovereign issuances have been at the level of individual emirates. The move will allow the country to issue bonds and sukuk at a federal level and establish a dirham-based sovereign yield curve that would help spur more corporate issuances.

Qatar has seen a betterment of fortunes in 2018 as S&P revised its outlook from 'negative to 'stable' during the year. Earlier in 2017, a negative outlook was affirmed to the country on account of the ongoing diplomatic standoff. However, a stable outlook has been reinstated after the country displayed macroeconomic resilience to overcome the effects of the embargo. Qatar's sovereign credit ratings were affirmed at 'AA-/A-1+' by S&P Global Rating. The agency also expects economic growth to accelerate and external accounts to remain in surplus from 2018-2021, except in the event of larger declines in oil prices. Qatar's gross debt to GDP is expected to tone down to 48.7% of the country's GDP in 2019.

Bahrain and Oman are two other GCC economies apart from Qatar to have a higher debt to GDP ratio compared to the rest. Bahrain's debt to GDP ratio is the highest among GCC countries at 88.4% in 2018. The ratio is expected to be higher in 2019 at 91.7% due to the country's need for finances to revive its economy. Bahrain's sovereign rating remains at junk territory with S&P affirming it at B+/B with a stable outlook, supported by the agency's opinion that financial aid from its neighbors would be forthcoming, if needed. The ratings were downgraded in December 2017 by S&P, citing the country's weak liquidity and increasing risks that would limit its access to international markets for financing. Saudi Arabia, UAE and Kuwait provided respite for the archipelagic state on October 2018 by announcing that they would provide USD 10 billion as funding support for Bahrain's fiscal program, which aims to eliminate the country's budget deficit by 2022.

Oman became the second GCC state after Bahrain to see it's long and short-term foreign and local currency sovereign ratings to plunge to junk territory. During the year, S&P and Fitch downgraded Oman's rating into junk category citing the country's fiscal challenges amidst a volatile oil price environment. This leaves Moody's as the only one among the large rating agencies to retain Oman at investment grade. Oman's gross debt to GDP is expected to reduce to 45.1% in 2019.

Economic Parameters Summary 2019

Title	KSA	Kuwait	UAE	Qatar	Oman	Bahrain
Economic Growth	Neutral	Positive	Positive	Neutral	Positive	Neutral
Inflation	Positive	Neutral	Neutral	Neutral	Neutral	Negative
Fiscal Balance	Neutral	Positive	Positive	Positive	Positive	Negative
Current Account Balance	Positive	Positive	Positive	Positive	Neutral	Negative
Gross Debt	Positive	Positive	Positive	Neutral	Neutral	Negative
Qualitative Assessment	Neutral	Positive	Positive	Neutral	Positive	Negative

Source: Marmore Analysis

Earnings Potential

In the year 2018, economic heavyweights of the region – Saudi Arabia, UAE, Kuwait and Qatar are projected to witness their corporate earnings increase by 14.2%, 14.3%, 15.6% and 10.7% respectively. Qatar's earnings growth rebounded after a weak showing in 2017 as the economy showed resilience to overcome the diplomatic isolation initiated by some of its neighbours. Oman and Bahrain also showed signs of improvement in 2018 after achieving negative growth in the previous year.

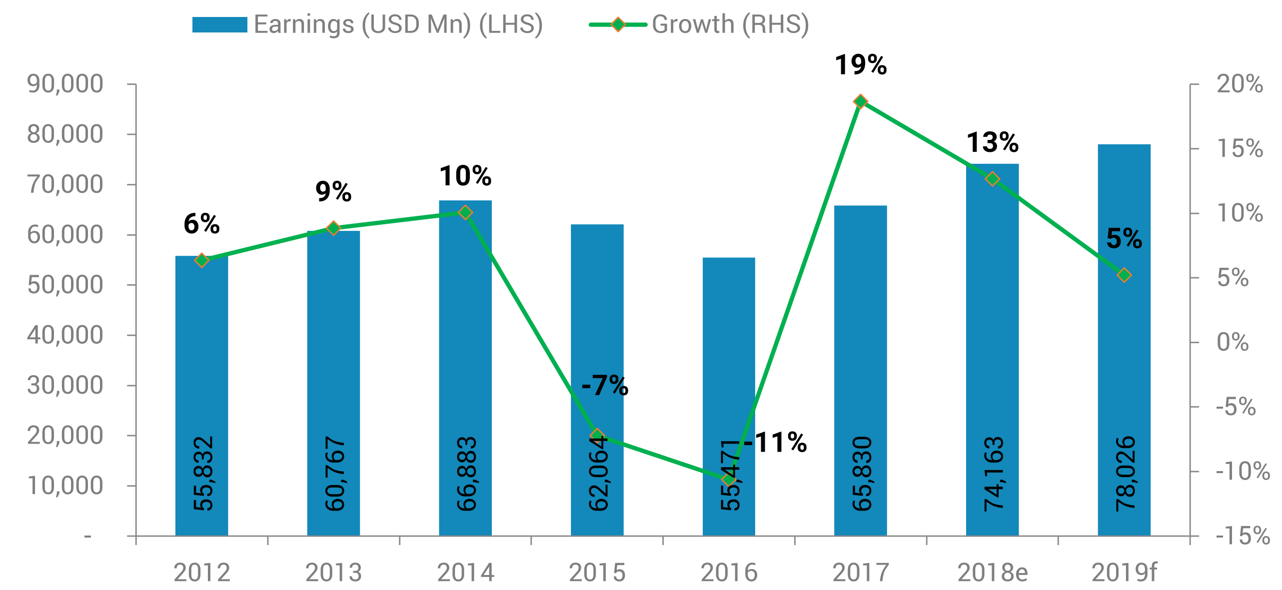
Growth in the overall corporate earnings for GCC countries is expected to be moderate at 5.2% for 2019. Earnings during the first nine months of 2018 grew at 6% when compared to the same period in 2017. We estimate the growth to improve to 14% for the full year 2018, factoring in the weak earnings witnessed during Q4 of 2017. This would mark the second year of positive earnings growth, following the 18.7% growth witnessed in 2017. Despite the expectations of an expansionary policy from major GCC economies, the consolidation of oil prices at the levels of USD 60-65 per barrel in 2019 is expected to a pain point as their oil revenues would take a hit compared to the previous year. Growth in corporate earnings for Saudi Arabia, the region's largest economy is expected to remain flat in 2019 due to the weakness expected in commodity and construction related companies. Qatar is expected to be the leader among GCC countries with earnings growth of 15% in 2019, driven by the banking sector, which contributed to more than 60% of total earnings in 9M 2018.

The outlook for GCC banks remains positive for 2019 due to the presence of multiple tailwinds. Banks, which contribute to roughly half of the total corporate earnings in the GCC by sector, have displayed steady growth in earnings since the global financial crisis, growing at a CAGR of 11.8% between 2009 and 2017. Regional infrastructure projects, such as UAE Expo 2020, World Cup Qatar 2022 and the Saudi National Transformation Program will support capital spending by the Governments and therefore facilitate credit growth in 2019. Moreover, the elevated liquidity buffers and the continuation of fed rate hikes would aid the banks in improving their profitability.

Construction related sectors have been underperforming for the past couple of years due to the underlying weakness in the GCC real estate markets. Supply demand imbalances in the property market, economic slowdown and the stagnation of projects due to fall in oil prices have impacted the profitability of companies operating in this sector. Looking forward to 2019, the sector is expected to mildly rebound due to the expansionary stance taken by the governments, resulting in new projects being initiated across the region. Affordable housing programs, reduction in government fees, relaxation of foreign ownership regulations, public-private partnerships in real estate sector are some measures that are expected to support the real estate sector and ease the profitability pressure on construction related companies. Considering the low base of earnings of these companies in 2018, an earnings growth of 26% is forecasted for 2019.

The recovery of the oil prices in the first three quarters of 2018 contributed to the surge in earnings for the commodities sector across the GCC countries. As Oil prices are expected to consolidate at levels close to USD 60-65 per barrel in 2019, the outlook for the sector remains muted, with earning likely to decline by 18% in 2019.

Earnings and Growth in GCC region, 2012- 2019 (USD Mn)



Source: Marmore Research

Earnings Growth Summary

Earnings Growth	KSA	Kuwait	UAE	Qatar	Oman	Bahrain	Overall GCC
2015	-12.3%	-5.9%	0.5%	-5.1%	-1.3%	-10.9%	-7.2%
2016	-4.0%	9.1%	-31.8%	-11.3%	-6.4%	18.0%	-10.6%
2017	9.4%	11.6%	76.6%	-4.2%	-13.7%	-2.8%	18.7%
2018e	14.2%	15.6%	14.3%	10.7%	13.5%	18.1%	14.0%
2019f	**-0.5%**	**8.0%**	**7.6%**	**15.2%**	**10.6%**	**0.9%**	**5.1%**
Qualitative Assessment	Negative	Positive	Positive	Positive	Positive	Negative	

Valuation Attractiveness

We have used P/E, P/B and dividend yield to rank the attractiveness of the individual GCC stock market.

Valuation Parameters Summary

P/E (TTM)	KSA	Kuwait	UAE	Qatar	Oman	Bahrain
2015	15.0	17.3	12.4	15.0	10.4	11.7
2016	15.4	15.2	12.8	11.5	10.1	8.8
2017	17.3	15.2	13.1	13.9	10.6	10.8
2018	17.6	14.7	11.1	14.4	10.3	9.3
P/B						
2015	2.0	1.3	1.5	2.1	1.5	1.0
2016	1.7	1.2	1.3	1.6	1.2	0.9
2017	1.7	1.1	1.3	1.5	1.2	0.8
2018	1.8	1.3	1.3	1.6	0.9	0.9
Dividend Yld. (TTM)						
2015	3.3	3.2	3.1	5.4	3.9	2.3
2016	3.2	5.5	3.9	3.5	3.9	0.7
2017	2.4	7.0	2.9	3.0	4.7	1.2
2018	3.4	3.5	5.0	3.3	6.7	5.8
Qualitative Assessment	Neutral	Positive	Positive	Neutral	Positive	Positive

Source: Marmore Research

Barring Saudi Arabia and Qatar, rest of the GCC economies have positive rating from a valuation perspective. Saudi Arabia has been trading at a premium in 2018 when compared to other GCC economies with a P/E ratio of 17.6x in 2018. Considering the flat outlook for earnings growth in 2019, it becomes difficult to justify the premium despite the government's commitment to increase spending to boost the local economy, prompting a neutral rating for the country. Qatar's P/E increased from 13.9x in 2017 to 14.4x in 2018 as the markets rallied by more than 20% during 2018. We expected consolidation of the markets moving into 2019 for Qatar's case that has resulted in a neutral rating for the market.

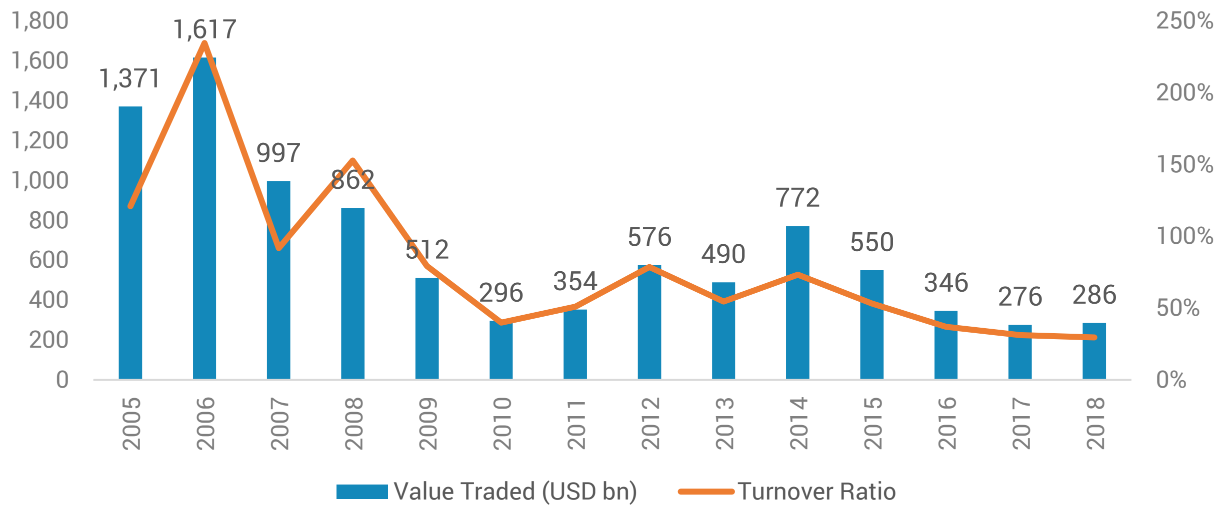
In terms of P/B ratio, Kuwait's (1.3x) and the UAE's (1.3x) P/B ratio is lower compared to Saudi Arabia (1.8x) and Qatar (1.6x), making them more attractive. Oman and Bahrain with lower P/B ratios also appear attractive despite factoring in the weakness of their economies. UAE, Bahrain and Oman look enticing when compared to other markets from a dividend yield perspective, with their yields at 5.0%, 5.8% and 6.7% respectively in 2018. UAE and Oman have seen a rise in dividend yields as Dubai and Oman's equity indices fell in 2018. Kuwait, which had the highest dividend yield among GCC markets in 2017, was the only market that witnessed a fall in yield during 2018 when compared to the previous year.

Market Liquidity

Liquidity levels in the GCC stock markets have remained low in 2018, clocking in a turnover ratio at 30% despite the MSCI and FTSE upgrade of Saudi Arabia into an emerging market, and the FTSE upgrade of Kuwait into an emerging market. Liquidity levels have shrunk for all GCC markets except Saudi Arabia in 2018, weaker than the low levels witnessed in 2017. From a liquidity angle, the outlook remains Negative for all GCC stock markets barring Saudi Arabia, which has been assigned a Neutral rating.

Despite the continual efforts of the regulatory authorities to improve liquidity in the domestic stock markets, the dearth of foreign and institutional participation has continued to remain a pain point for the regional markets. Geopolitical uncertainties remain a pressing concern for foreign investors, especially when stocks in other emerging markets appear to be available at attractive prices after the beat down witnessed in 2018. A series of upgrades in the past few years by renowned index providers like the MSCI and FTSE are a beacon of hope for the GCC stock markets, indicating that they are on the right direction. Removal of regulatory impediments, improving disclosures and the introduction of innovative products need to be undertaken to make the markets more attractive for foreign investors, thereby improving liquidity.

Value traded (in USD bn) and Turnover Ratio (in %), 2005-2018



Source: Reuters

Stock Market Turnover Ratio (value traded/market cap)

Earnings Growth	Saudi Arabia	Kuwait	UAE	Qatar	Oman	Bahrain
2014	103%	22%	75%	29%	25%	3%
2015	89%	12%	25%	13%	10%	1%
2016	60%	11%	23%	9%	10%	2%
2017	46%	20%	17%	14%	12%	4%
2018	47%	14%	11%	11%	10%	4%
Assessment	Neutral	Negative	Negative	Negative	Negative	Negative

Source: Reuters, Marmore Research

Overall Ratings

Overall Market View for GCC region

Title	KSA	Kuwait	UAE		Qatar	Oman	Bahrain
Economic Factors	Neutral	Positive	Positive		Neutral	Positive	Negative
Valuation Attraction	Neutral	Positive	Positive		Neutral	Positive	Positive
Earnings Growth Potential	Negative	Positive	Positive		Positive	Positive	Negative
Market Liquidity	Neutral	Negative	Negative		Negative	Negative	Negative
			Abu Dhabi	Dubai			
Overall Market View	Neutral	Positive	Positive	Positive	Neutral	Positive	Negative

Source: Markaz Research

Kuwait MSCI index inclusion

Kuwait's equity market added another feather to its cap as capital market reforms have put the country in contention for an emerging market upgrade in the MSCI EM Index. MSCI said that it is considering upgrading Kuwait from Frontier Market to its Emerging Market index and will review its decision to do so in its Global Market Accessibility Review June 2019. Index provider FTSE Russell has already incorporated 12 Kuwaiti stocks into its emerging market index with its two-phase implementation completing on December 2018. This will result in a weighting of just over 0.5 percent in its FTSE Emerging All Cap index.

The Morgan Stanley Capital International Emerging Markets (MSCI EM) Index is one of the most popular indices to measure the equity market performance of global emerging markets. It is a float-adjusted market capitalization index, which consists of 23 emerging economies. The UAE was promoted to FTSE's emerging index in 2010, but continued to remain as a frontier market with MSCI till 2013, due to settlement issues and restrictions on foreign ownership. The case was opposite for Qatar as it was included in MSCI EM index during 2013 while being promoted to secondary emerging market in the FTSE index as late as 2016 indicating that the inclusion in one index does not guarantee the inclusion in other. However, Kuwait remains optimistic in bagging a dual upgrade within two years of each other.

Boursa Kuwait, which took control of the Kuwait stock exchange in early 2016, introduced a number of reforms such as relaxing listing rules, delisting companies seen unfit for public investment and segmenting the market with different disclosure requirements. Since we do not have a confirmation from MSCI yet, we can estimate the weightage that Kuwait might be assigned by comparing the market capitalization of its GCC peers, like UAE and Qatar, and the weightage they have been assigned by MSCI. Qatar and UAE have a weightage of 1.34% and 1.04% respectively in the FTSE EM index and a weightage of 0.47% and 0.58% in the MSCI EM index. Taking into consideration that FTSE EM index recently included Kuwait with a weightage of 0.5%, we estimate that Kuwait can end up with a weightage of approximately 0.30% in the MSCI EM index. This can lead to an estimated fund flow of USD 2-5 billion from passive investors into the country.

Expected Fund Flow into Kuwait after MSCI inclusion

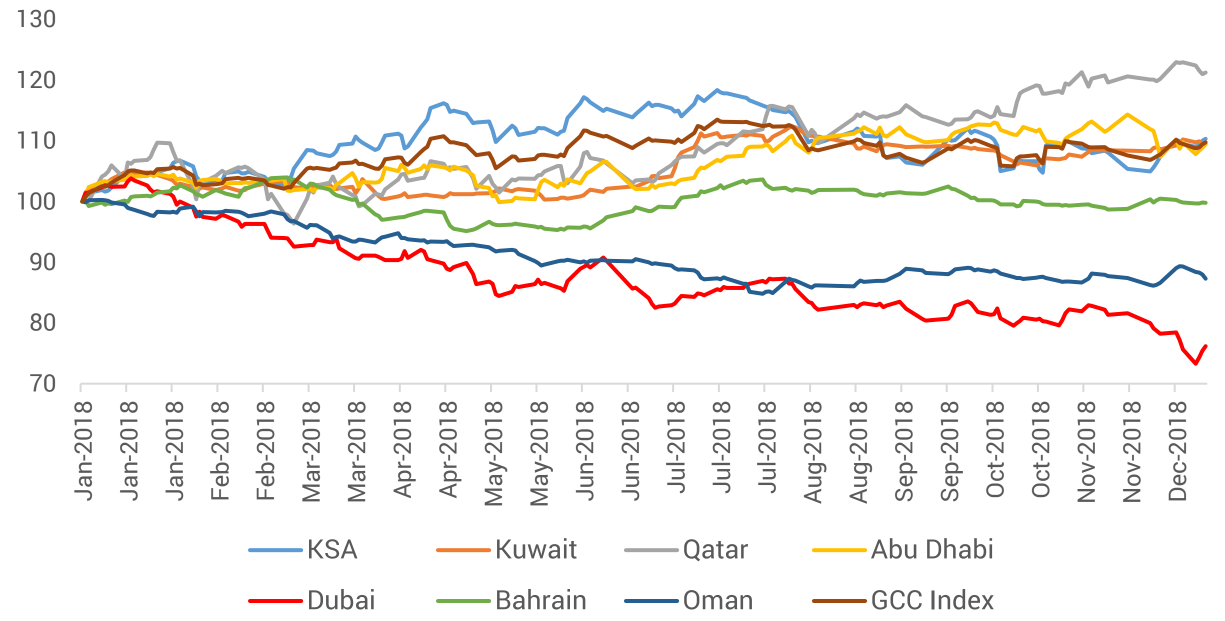
A. Funds benchmarked to MSCI EM Index	USD 1.9 Trillion		
	Best Case	Normal Case	Worst Case
B. Expected Weightage of Kuwait in the index	0.40%	0.30%	0.20%
C. Expected Fund Flow in (USD billion), (A*B)	7.6	5.7	3.8
Passive inflows at 60% (C* 60%), USD bn	4.5	3.4	2.3
Passive inflows at 40% (C*40%), USD bn	3.0	2.3	1.5

Source: MSCI, Marmore Analysis

Dubai market meltdown

Dubai financial market ended 2018 as the worst performing market in the GCC, with its main index plummeting by 24.9%. Slowdown in activity in the region, oversupply in Dubai's residential real estate market and the rising cost of living and doing business are some of the key factors which dented performance. Traditional growth engines like real estate, trade, transport & hospitality have remained weak.

Steep correction in Dubai Financial Markets



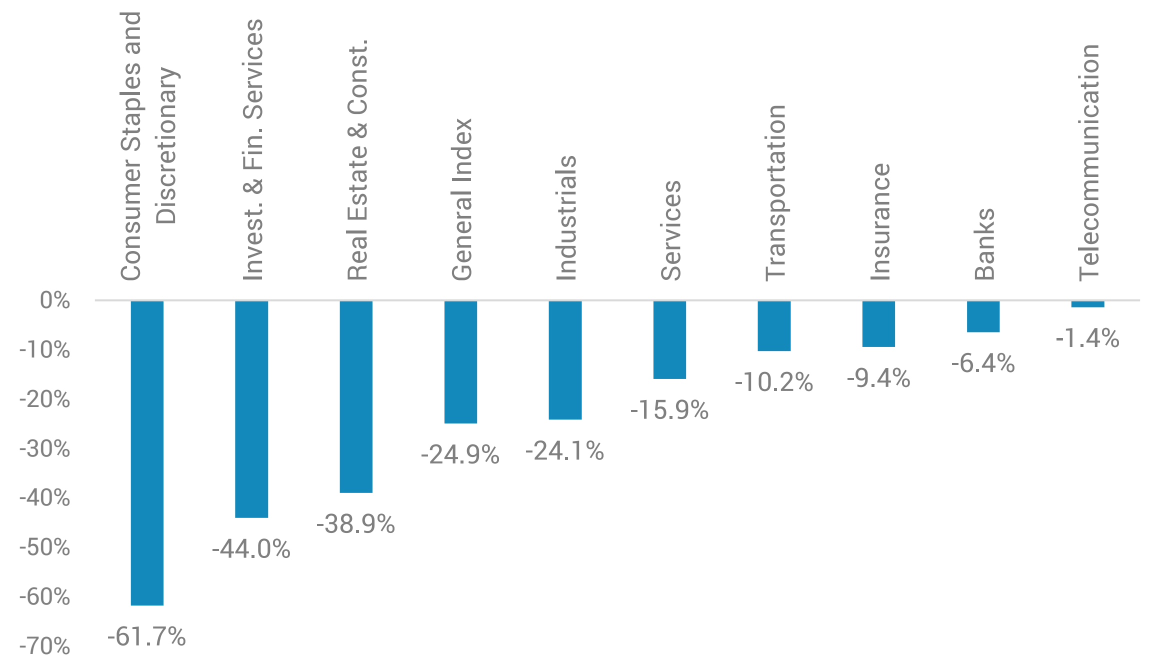
Source: Reuters Eikon, Marmore

The aggregate corporate earnings for Dubai slowed in 3Q18 to USD 2.1bn, implying a growth of 0.2% over the previous year. On a nine month basis corporate earnings growth was at 14.8% as compared to same period previous year. Real estate and constructions, retail operators, theme parks and financial-services companies are among the pillars of Dubai's economy, these are also the major losers in the stock market in 2018.

Consumer staples & discretionary segment performed the worst, as shares of DXB Entertainments declined 63% YTD. DXB continued to post losses for the 20th consecutive quarter and reported lower than projected visitor number. The company was also significantly impacted due to exclusion from MSCI Emerging Market Index. DXB is currently constructing a Six Flags attraction in Dubai. In investment and financials segment, Dubai Financial Market (DFM) shares were under pressure due to subdued market conditions as total value of trading on DFM decreased 44.8% to Dh47.7bn in 9M2018. DFM posted lower revenues and net profit in 3Q18, down 5.9% and 24.5%, respectively, compared to same period last year.

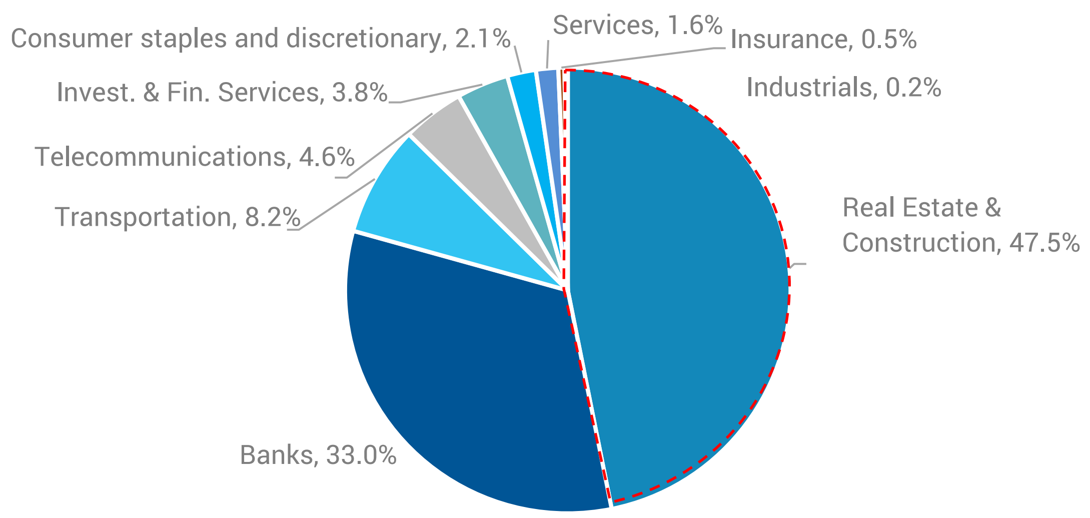
Although other sectors also underperformed in 2018, Real estate and construction which has the maximum weightage of above 45% in the DFMG Index (Fig.3) was the main catalyst for the markets underperformance. The real estate and construction sector declined 38.9% year to date.

Diminishing sectoral returns in 2018



Source: Reuters Eikon, DFM

Dubai Financial Markets General Index Constituents



Source: Dubai Financial Market

Dubai real estate sector under pricing pressure

Ever since oil prices collapsed about 4 years ago, real estate has witnessed slump owing to oversupply and lack of affordable housing. Buyers are now lured for more favorable payment terms and tenants are renegotiating terms and rents. This slowdown has led to steep correction in stock prices for most of the real estate players, which traded at 52 week lows in December 2018.

Dubai real estate sector performance

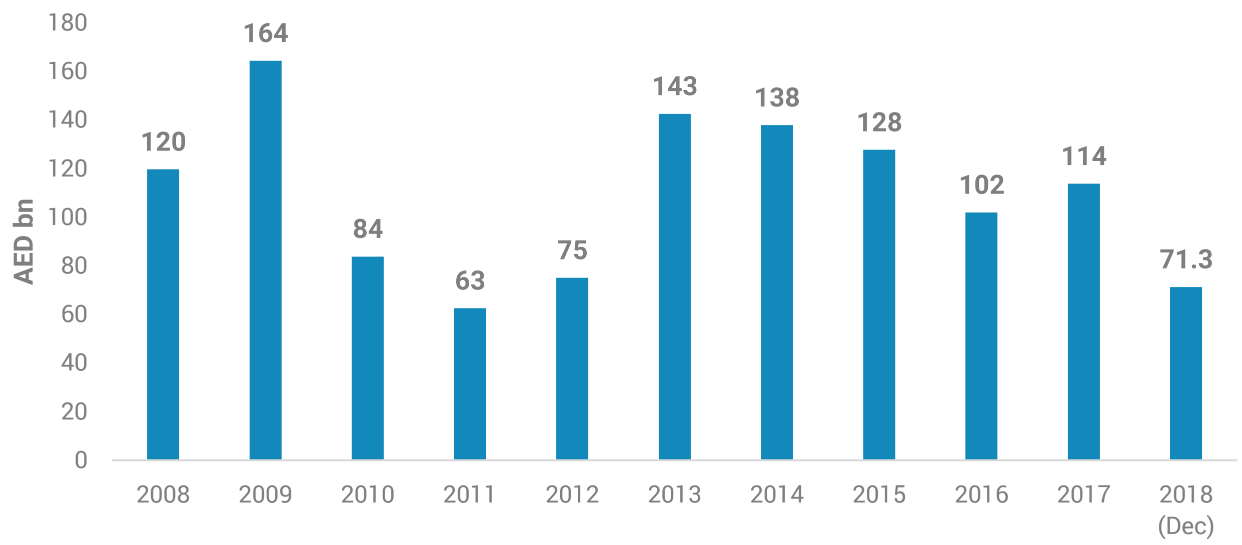
Company	2018 Stock Returns
Union Properties	-58.8%
Damac Properties	-54.2%
Dubai Investments	-44.0%
Dubai Real Estate & Construction Index	-38.9%
Emaar Properties	-35.3%
Deyaar Development	-30.4%
Arabtec Holding	-20.2%
Emaar Mall	-16.0%

Source: Reuters Eikon

Emaar, Dubai's biggest listed developer, has been detracting ever since it gave lower than expected dividend from its proceeds of partial stake sale in Emaar Development. Emaar properties has witnessed steep correction of 35.3% in its share prices in 2018. The company posted lowest quarterly profit in almost three years, a decline of 29% in net profit in September 2018 compared to the same quarter last year. In a bid to transform itself to asset light hospitality company, Emaar Hospitality (subsidiary of Emaar Properties) is selling five of its hotels, including the flagship Dubai Mall and Boulevard to Abu Dhabi National Hotels. This transaction is expected to enable Emaar Properties to fund future growth and focus on hotel management rather than ownership. In a trend common across real estate players, Damac Properties reported a decline of 68% in net profits in third quarter of 2018 as compared to the same period previous year. The company has stopped buying land and would be interested in joint venture agreements with other developers and land owners.

With the current market grappling with oversupply, the focus in 2019 would be to sell existing inventories. Dubai property sales are on pace for the worst year since 2012, down more than a third upto December 2018 to AED71.3 billion. Lack of new launches at Cityscape also indicates subdued investor sentiments. Further, in January 2018 a VAT of 5% was implemented in Dubai, which represents one of the biggest challenges to Dubai's real estate industry in 2018. As the introduction of VAT in Dubai will drive changes like the revision of accounting systems, this may create cash flow and working capital pressures for some developers. According to JLL prices are expected to further decline in the next 12 months.

Dubai land and property sales value inching to lower levels in 2018



Source: Dubai Land Department

Dubai Real Estate: Buyers/tenants market

With an average price of AED 12,804/m² the Dubai residential property prices decreased by 7.4% on annual basis and declined by 2.5% compared to the same quarter last year. The rental yield decreased slightly to 6.81%. Excess supply and slower demand are the primary reasons for the decline in rents. The rent prices declined by an annual rate of 9.6% in the third quarter of 2018. Concerning investment in Dubai's real estate market, the rental yield has been on a downward trend since last quarter of 2015 and it further declined to 6.8% in third quarter of 2018. However, the current rental yield still remains attractive for investors. In 2019 residential property prices are expected to further decline.

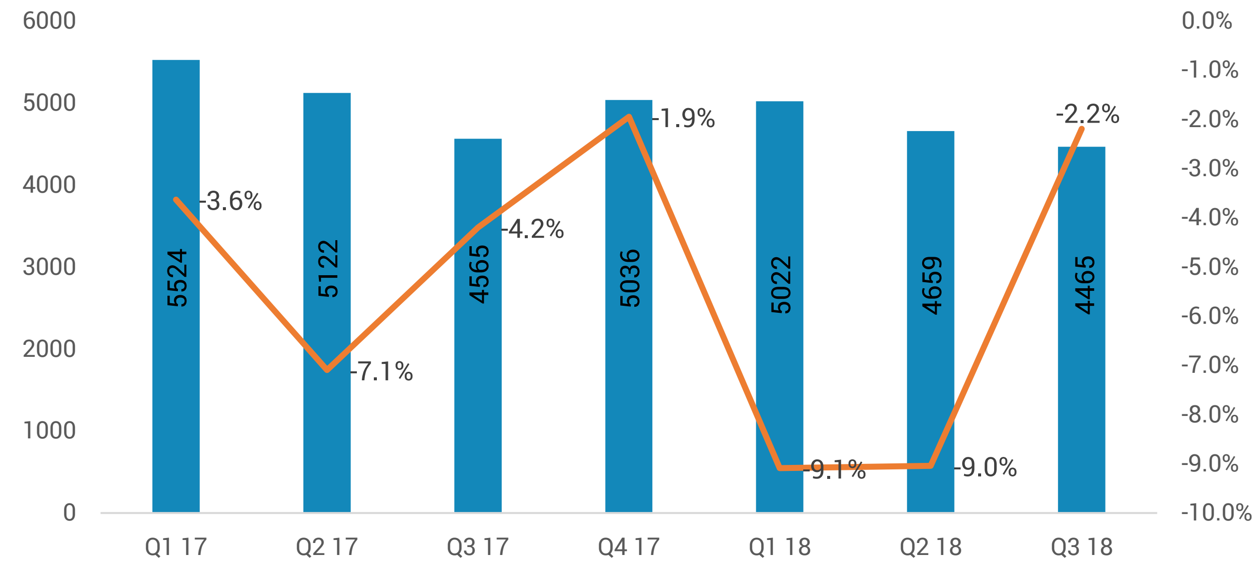
Office spaces were also under pressure as there was increase in relocations and consolidations activity. Rising supply levels are compelling landlords to offer attractive terms that include rent-free periods, fit-out contributions and other concessions. According to property consultant Core, the Dubai market added over 1.3 million sq ft of space year-to-date, with another 0.44 million sq ft expected over the remainder of the year.

Retail is the most challenged sector, as malls are now offering leasing incentives and "turnover only" leases to retain existing tenants. According to JLL this sector is further expected to decline as very high supply levels are expected in the next two years.

DFM: growth engines sputtering?

In general we see weakness across the growth engines of Dubai. Slowdown in activity in the region, oversupply in Dubai's real estate market and the rising cost of living and doing business are some of the factors which are denting recovery prospects in the near term. Employment growth has slowed to an average rate of 1.6% in the first nine months of 2018 against 2.6% in the same period of previous year. Employment in sectors that contribute the most to creation of white-collar jobs which in turn support the demand in real estate market, fell in the third quarter. Business sentiment continues to be weak as evident by declining issue of new business licenses in 2018.

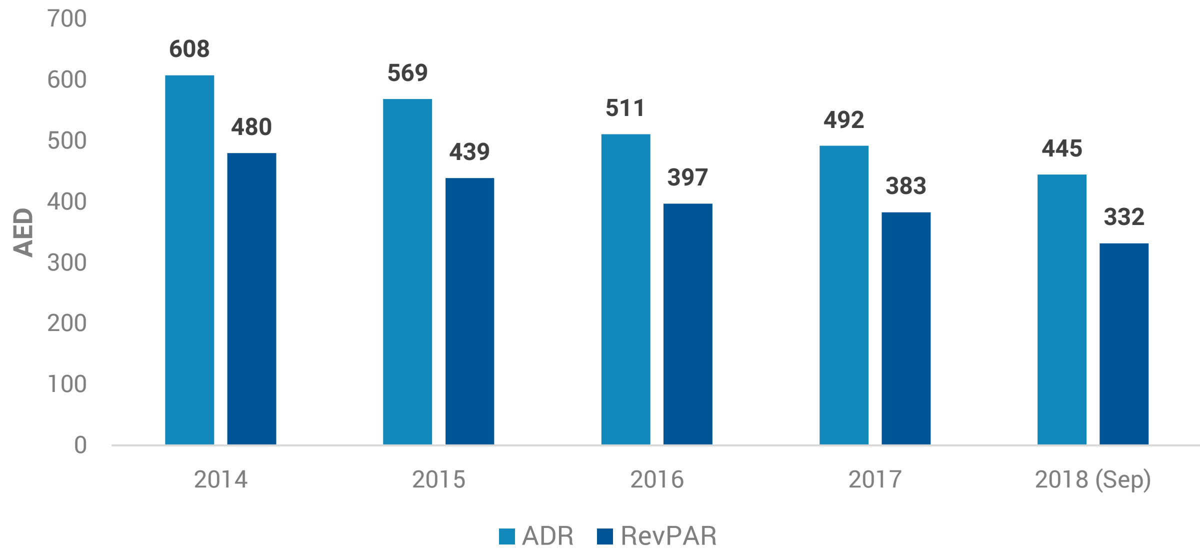
Dubai new business licenses issue



Source: Dubai Statistics Center

Number of tourists to Dubai was flat at 11.58mn in the nine months of 2018 as compared to the same period in 2017, when arrivals peaked to 7.5%. However, the new policy exempting transit passengers from Visa fees for 48 hours and other incentives is expected to aid visitor growth. According to STR Global supply (up 7.7%) in Dubai hotels exceeded demand (up 3.1%) resulted in drop in occupancy levels to 75.2% (down 4.3%) in October 2018. According to Dubai Department of Tourism, average daily rate (ADR) in Dubai dropped by 5.7% to AED445, as hotels looked to drive market share through more attractive rates, this led to decline in RevPAR by 7.7% to AED332 in September 2018.

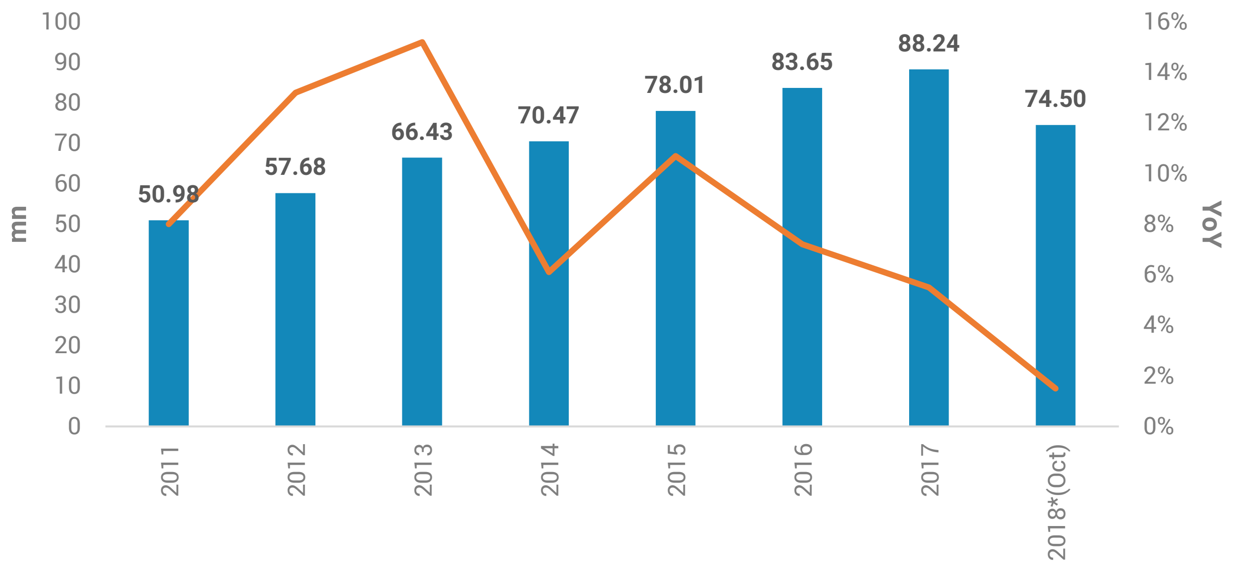
Dubai average daily revenue



Source: Dubai Department of Tourism and Commerce Marketing

Air passenger traffic growth slowed at Dubai airport after 15 years of robust increases as 74.5mn passengers used the airport in the first 10 months of 2018, up only 1.5% as compared to 17.7% growth for the same period in 2017. Dubai may lose its dominance as a travel hub due to surge in long-range aircrafts connecting Asia and Europe.

Dubai air passenger traffic



Source: Dubai airports

Government initiatives and outlook for 2019

IMF is hopeful of fiscal and structural reform based growth in non-oil private sector and forecasts Dubai's GDP at 3.3% in 2018 and 4.2% in 2019 compared to a 2.8% growth recorded in 2017. Based on Emirates NBD's Dubai Economy Tracker Index strong improvement in Dubai's non-oil private sector was witnessed in November 2018, reflecting faster expansions in business activity, new work and a stable trend in new employment.

To restore and stimulate growth the Government has taken several initiatives at the core of the cost reduction is reducing the cost of doing business, reducing the market fee from 5% to 2.5%, cancelation of 19 fees related to the aviation industry and aircraft landing permits, waiving 4% overdue property registration fees, immediate freeze on tuition fees of all private schools in Dubai for one year and cutting down hotel sales fees from 10% to 7%. The government also announced that it would issue 10-year visas for professionals and investors, and will also allow 100% foreign ownership outside free zones. This is expected to attract talent and foreign direct investment into the country.

Further, to boost retail sector in Dubai, the Department of Economic Development (DED) and Dubai Festivals and Retail Establishment (DFRE) has jointly announced the 2019 Retail Calendar with 18 events over 247 days. This aims to increase consumer spending on shopping throughout 2019.

Infrastructure spending being the predominant focus of Dubai government, has witnessed 46.5% y-o-y increase in 2018, due to allocation of more funds towards Expo 2020 projects. These infrastructure investments in-turn are expected to aid Dubai's economic growth. Infrastructure related spending accounted for 21% of the total expenditure during 2018, in Dubai's largest public budget in 2018. Further additional spending of AED10.6bn relates to Expo 2020, which in turn will act as stimulus to the Dubai economy.

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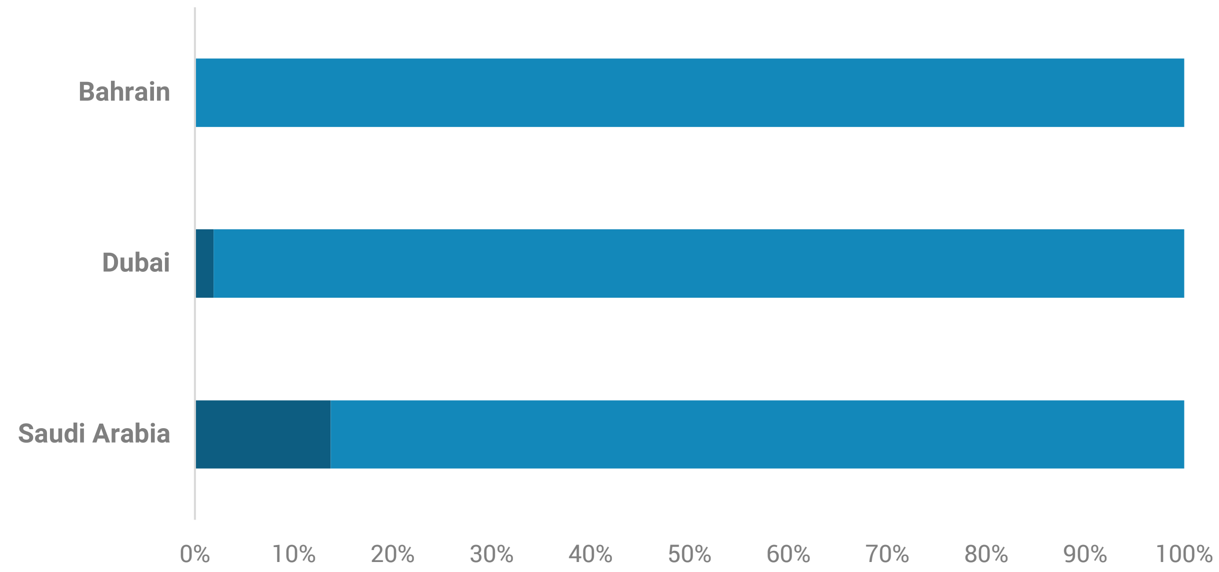
Chapter 7

REITs: A rapidly evolving asset class

REITs as an alternate investment class, which can provide consistent dividends and capital appreciation to an investor, had a very slow start in GCC. The first formation of private vehicle dates back to year 2006, when an USD200mn Arabian Real Estate Investment Trust was formed by HSBC and Daman. Subsequently, Kuwait had its first private REIT, Al-Mehrab Tower REIT (which remained closed and non-listed) launched in 2007. Later, in 2009 Inovest REIT in Bahrain and in 2010 Emirates REIT in Dubai was launched. Post that, REIT launches in the region continued to be subdued, as it lacked awareness and popularity amongst investors as an asset class.

UAE was the first GCC country to introduce a legal framework pertaining to REITs in 2006 by Dubai Financial Services Authority. Post that, further REIT laws were enacted only in 2015 in Abu Dhabi, Saudi Arabia in 2016 and Bahrain towards the end of 2016. GCC's first REITs listing occurred in 2014, when Emirates REITs was listed on Nasdaq Dubai. Post finalization of the regulations on REITs in 2016, Saudi Arabia has seen a surge in REITs listings and currently has about 16 listed REITs on Tadawul. However, all other GCC countries lag behind Saudi Arabia and are yet to catch up in terms of REIT listing. Dubai has only two listed REITs, Bahrain has just one, and Kuwait and Qatar are yet to initiate REIT listings. However, Kuwait and Bahrain now have private REITs with total sizes of USD 100mn and USD 80mn, respectively. REITs still being in nascent stage in GCC, has very low market capitalization as percent of market capitalization of real estate developer in the GCC. We expect this trend to improve as more REITs get listed.

REITs market cap as % of total Real estate developer market cap



Source: Reuters, Marmore

As listed in the table below, REITs are subject to rigorous regulatory requirements including, minimum dividend payout requirements, and strict limits on bank debt that they can borrow and on the proportion of development assets they can own. These regulations ensure that the financial risk is limited, unless the valuation of properties significantly decline due to external factors.

REITs in GCC

Country	Type	Payout from annual net income	Dividend Yield (%)	REITs Market Cap ($ mn)	Gearing limit*	Total Listed REITs	# of Islamic REITS
UAE	Closed ended investment or trust	min 80%	8.2	448	Capped at 70% in Dubai and 65% in Abu Dhabi	2	2
KSA	Closed-ended investment	min 90%	5.7	2898	50%	15	10
Bahrain	Investment trust	min 90%	6.3	50	60%	1	0
Oman	Investment fund	min 90%	NA	NA	NA	NA	NA
Qatar	Collective investment trust / company	min 80%	NA	NA	NA	NA	NA

Source: Marmore
**as % of NAV*

In line with demand for Sharia-compliant REITs, majority of REITs listed in GCC region are Islamic funds i.e. 12 out 18 listed REIT funds in GCC are Sharia-compliant. As the interest for Islamic finance rises across the world, having more sharia-compliant REITs should be favourable for GCC markets.

As tax efficiency is less relevant in the GCC, liquidity and flexibility appears to be the key to the rise of REIT in the region. It provides transparency and enables investors to diversify investment and risk. Development of REITs, also provides real estate companies with access to capital (private placements & IPO) to fund their acquisition and investment activity. This lessens the burden on traditional sources of raising funds, namely, regional banks.

As REITs become more popular and mature in GCC region, disclosures and transparency is also expected to increase. According to JLL's Global Real Estate Transparency Index (GRETI) Dubai is the top improver in the rankings in 2018, and it along with Saudi Arabia and Abu Dhabi feature in the semi-transparency list as per the rankings. While other GCC countries like Bahrain, Kuwait and Qatar feature in low-transparency list suggesting ample scope for improvement.

Global Real Estate Transparency Index

Country	Ranks
Dubai	40
Saudi Arabia	54
Abu Dhabi	55
Bahrain	62
Kuwait	70
Qatar	71

Source: JLL

Similar to a trend in mature markets, GCC region is also emerging with launch of specialised REITs which focusses on specific asset class like residential, logistics, education, malls, hotels, hospitals, and warehousing. The trend has already begun to pick up with the launches of residential REIT by Equitativa, Hospitality REIT by Five holdings, Gulf Islamic Investments REIT with monthly dividend payout in Abu Dhabi Global Market (unlisted). Further, the introduction of regulatory framework for REITs listing in Oman should support new listings in the near term. GCC REITs is expected to gain momentum as its acceptance as an asset class increases in the region, enhanced investor appetite for yield focused products and Sharia compliance nature of the REITs.

UAE: REITs performance and outlook

There are just two listed REITs in UAE, both listed on NASDAQ Dubai. Both the funds are Sharia-compliant and have about 11 assets each. Emirates REIT is the largest sharia-compliant REIT in the world by total assets and market capitalisation. Both the REITs on an average offer 8.2% dividend yield.

Global Real Estate Transparency Index

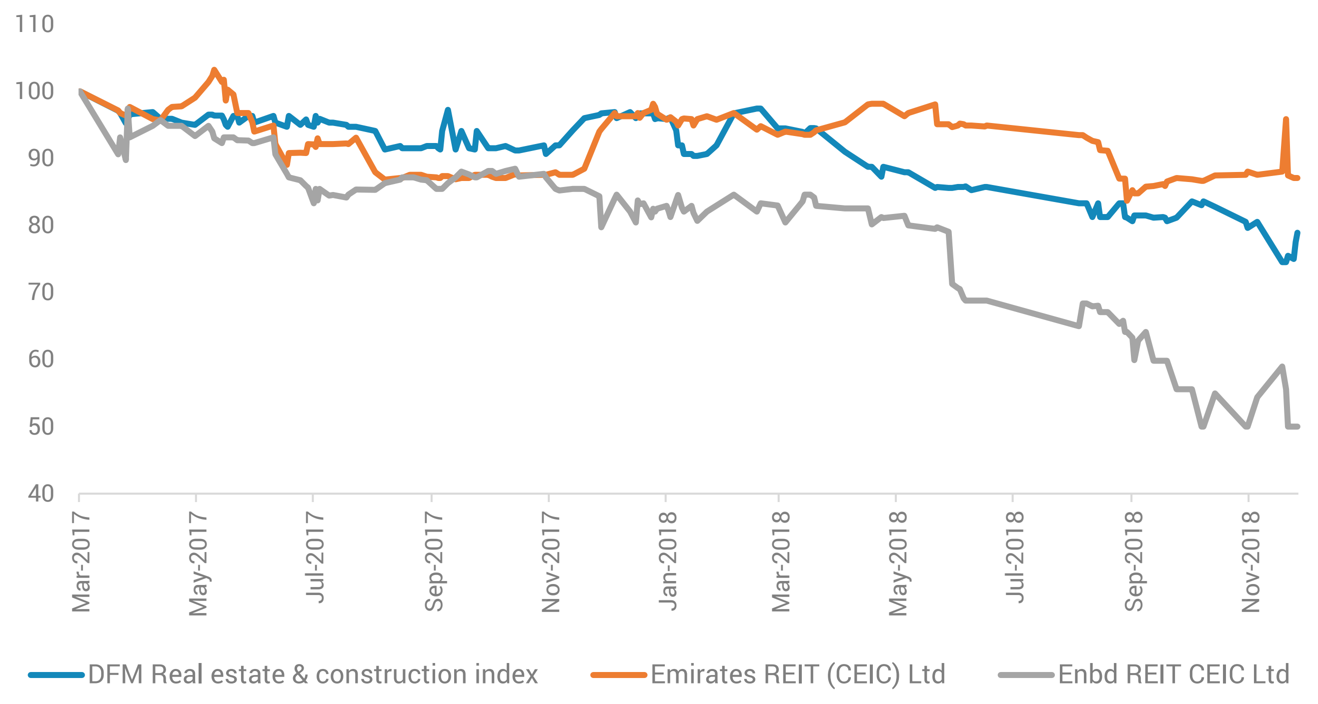
	ENBD REIT	Emirates REIT CEIC
Manager	Emirates NBD asset Management	Equitativa
Portfolio value ($mn)	459	915
# of properties	11	11
Types of property	Office, residential and alternative	Commercial , educational and retail
Occupancy	90%	74%
Loan to value	38%	41%
Gross Yield	8.3%	8.0%
NAV (USD/share)	1.12	1.76
Share price (USD/share)	0.585	0.945
Discount to NAV	-48%	-46%

Source: ENBD REIT, Emirates REIT, Reuters, Marmore

Concerning oversupply, real estate, particularly in Dubai has taken a big hit since the start of the year, as most of the real estate developers stock has retracted during the period. This has also reflected in the performance of REITs in UAE. Mainly, as UAE being relatively a more mature real estate market, sourcing difficulties for good quality high-yield assets and lower occupancy rate for REITs, could potentially lower recurring distributable income to support dividends.

With both the UAE REITs trading at steep discount to their Net asset value (NAV), Emirates REIT has managed to do better than DFM Real estate and construction index in 2018, but ENBD REIT's performance was concerning. Negative market sentiment and lack of liquidity are the key factors highlighted by the management of ENBD REIT for the fund's steep discount to NAV. ENBD REIT is in the process to launch a share buyback programme to reduce capital and to create distributable reserve.

Dubai listed REITs performance vs DFM Real Estate & construction index



Source: Reuters, Marmore

In UAE, given that the real estate market is subdued, rents are falling (particularly, in Dubai residential market), the yield expectations from such investment is lower, hence having a negative impact on the viability for alternate investment asset. However in the run-up to 2020 expo, the market is expected to stabilize and grow thereafter.

There are many REITs in pipeline in UAE like property division of Abu Dhabi's state investment fund Mubadala investment company, Mubadala Real Estate is preparing to launch a REIT for its assets based in Al Maryah Island. The company expects the UAE property market to uptick from 2019 onwards. Etihad REIT expected to list by next year and residential REIT, are expected to follow the suit.

Saudi Arabia: REITs performance and outlook

Saudi Arabia has about 16 listed REITs with more than USD2bn market capitalization. Under National Transformation Program (NTP), Saudi Arabia's aim to double its real estate sector contribution to 10% of the GDP by 2020, this is expected to provide boost to REITs growth in the country.

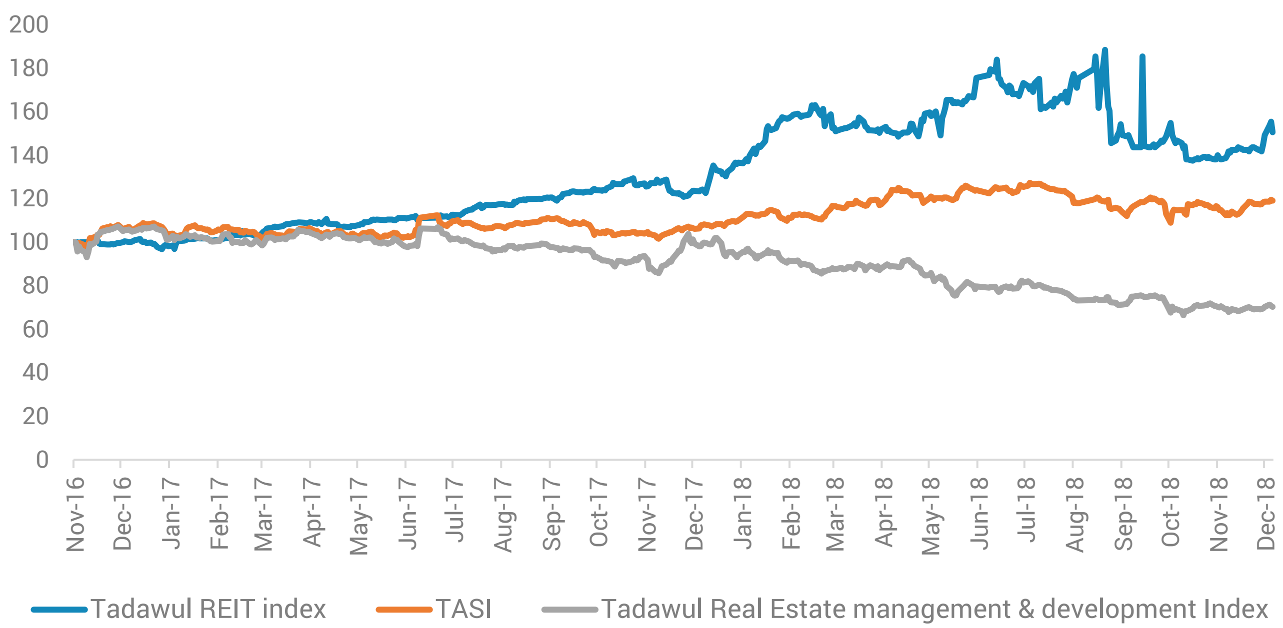
Saudi Arabia listed REITs details

REITs Name	Properties	Last Traded Price (SAR)	NAV/unit (SAR)	LTP/NAV	Trading at Discount / Premuim to NAV	Dividend Yield (%) 12M rolling
RIYAD REIT	Office, Stores, Hotels	7.86	n.a	n.a	n.a	9.26
ALJAZIRA REIT	Warehouses	14.84	n.a	n.a	n.a	4.95
JADWA REIT ALHARAMAIN	Stores, Hotels	7.42	10.63	-30%	Discount	8.56
TALEEM REIT	Educational	10.32	10.35	-0.3%	Discount	5.96
AL MAATHER REIT	Residential, Offices, stores, warehouses	7.48	9.82	-24%	Discount	3.47
MUSHARAKA REIT	Residential, Warehouses, Hotels	8.18	10	-18%	Discount	8.75
MULKIA REIT	Residential, Offices, Stores, Industrial	8.09	10	-19%	Discount	7.55
MASHAAR REIT	Stores, Hotels	7.08	10	-29%	Discount	3.67
ALAHLI REIT 1	Stores, Hotels	7.7	10	-23%	Discount	4.17
DERAYAH REIT	Residential, Offices, Stores, Warehouses	8.2	10	-18%	Discount	7.94
Al RAJHI REIT	Residential, Commercial, Educational, Warehouses	8.04	13.27	-39%	Discount	2.16
JADWA REIT SAUDI	Residential, Commercial, Educational, Warehouses	8.88	10	-11%	Discount	5.17
SEDCO CAPITAL REIT	Office, Retail, Hospitality, Education and Residential	8.06	9.83	-18%	Discount	3.78
SWICORP WABEL REIT	Mall	8.52	0	NA	NA	0
MEFIC REIT	Residential, Commercial, Office	8.38	0	NA	NA	0
BONYAN REIT	Residential, malls, Hotels	8.3	10	-17%	Discount	2.94

Source: Tadawul, Marmore

REITs used to list in 2017 at a premium to NAV, but subsequently moderated in the later half. From an investment point of view it should be noted that not all the REITs are created equal, as they differ on underlying assets and would also depend on the Funds track record in sourcing and enhancing assets returns. Market depth is expected to increase and preference would be given to high-quality assets. REITs with exposure to low-quality assets would trade at a discount to peers. REITs in Saudi Arabia had performed considerably well compared to real estate developers and the broad index as such.

REITs performance vs Tadawul Index



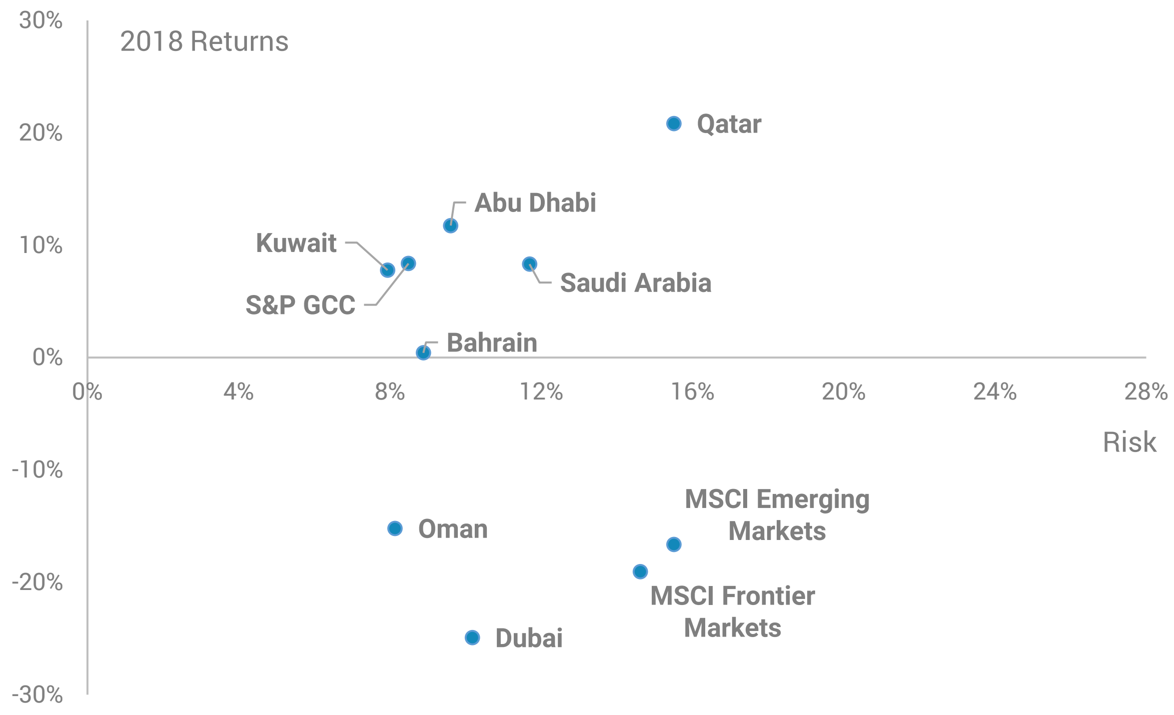
Source: Reuters, Marmore

Recently CMA increased the minimum fund requirements to SAR500mn, up from SAR100mn and also imposed restriction on investors with above 5% stake in REIT fund, prohibiting from disposing it in the first year of listing. This augurs well, as criteria for minimum required assets would only encourage participation from quality REIT managers and the decision to prohibit disposal would encourage long term participation by the investor, hence increasing transparency and investor protection.

Affordable housing programs, public-private partnership in real estate and mega projects may provide the required thrust to the sector, however quality and support of suitable assets, sustainable pipeline of future assets and softening of the current economic climate could challenge the growth of the REITs in Saudi Arabia.

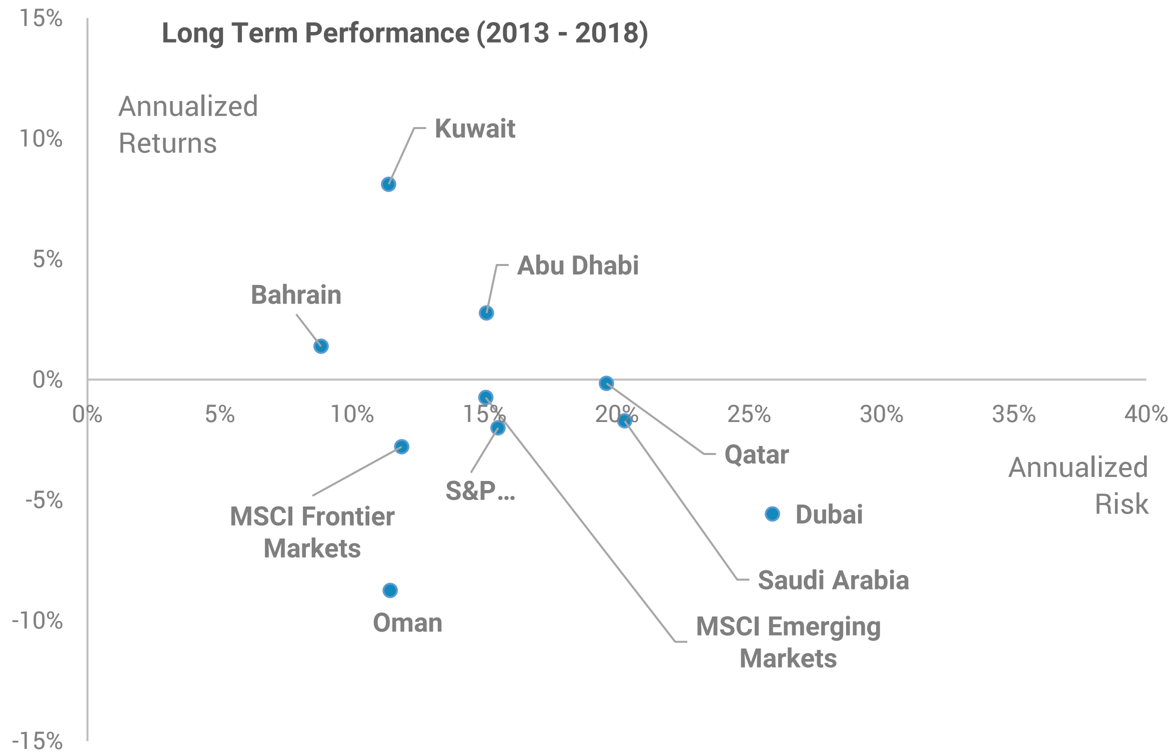
Appendix

Asset Classes: Risk-Return Profile 2018



Source: Reuters Eikon, Markaz Research

Risk-Return Profile (2013 - 2018)



Source: Reuters Eikon, Markaz Research; Note: Kuwait data is for the time period 2016-2018

Blue Chips Performance

Companies	Country	Sector	M. Cap (USD Mn)	Last Close	2018 (%)	P/E	P/B	Beta	Div. Yield (%)
SABIC	KSA	Materials	92,938	116	14%	15.84	2.06	1.08	3.61
Saudi Telecom	KSA	Telecom	48,788	92	34%	17.80	2.84	0.77	4.37
NCB	KSA	Financials	38,351	48	30%	13.56	2.29	1.13	2.36
Al-Rajhi Bank	KSA	Financials	37,518	88	35%	14.10	2.71	0.96	4.62
Saudi Electricity	KSA	Utilities	16,840	15	-28%	N.M.	0.82	0.76	4.62
First Abu Dhabi Bank	UAE	Financials	41,836	14	38%	13.45	1.53	1.15	4.96
Etisalat	UAE	Telecom	40,207	17	-3%	17.11	3.38	0.55	4.71
Emirates Islamic Bank	UAE	Financials	14,771	10	2%	63.05	7.74	-	-
DP World	UAE	Industrials	14,193	17	-32%	11.13	1.31	0.64	2.40
Emirates NBD Bank	UAE	Financials	13,453	9	8%	5.34	0.79	0.63	4.50
National Bank of Kuwait	Kuwait	Financials	17,096	834	20%	14.95	1.54	0.67	3.26
Kuwait Finance House	Kuwait	Financials	12,785	611	17%	18.10	2.11	0.83	2.53
Zain Group	Kuwait	Telecom	6,410	449	3%	11.14	1.52	0.99	7.80
Ahli United Bank	Kuwait	Financials	5,460	204	4%	8.38	1.24	0.50	6.26
Boubyan Bank	Kuwait	Financials	4,413	560	35%	27.08	2.83	0.57	1.19
Qatar National Bank	Qatar	Financials	49,470	195	55%	13.15	2.36	0.90	3.08
Industries Qatar	Qatar	Industrials	22,202	134	38%	16.90	2.31	0.95	3.74
Qatar Islamic Bank	Qatar	Financials	9,865	152	57%	14.78	1.88	1.16	3.29
Ezdan Holding Group	Qatar	Real Estate	9,457	13	7%	45.93	1.10	1.58	0.00
Masraf Al Rayan	Qatar	Financials	8,586	42	10%	14.90	2.44	1.38	4.80

Source: Reuters; Classification of companies are in accordance to MSCI methodology

Mid Cap Performance

Companies	Country	Sector	M. Cap (USD Mn)	Last Close	2018 (%)	P/E	P/B	Beta	Div. Yield (%)
Arab National Bank	KSA	Financials	8,518	32	29%	9.80	1.29	1.13	3.76
Jabal Omar Development Co	KSA	Real Estate	8,449	34	-42%	-	3.24	1.12	-
Kingdom Holding Co	KSA	Financials	7,608	8	-13%	40.48	0.93	0.71	6.49
Du (Emirates Integrated Tel.)	UAE	Telecom	6,208	5	-1%	12.45	2.80	0.29	6.96
Saudi Kayan	KSA	Materials	5,295	13	24%	12.47	1.26	1.62	-
Mesaieed Holding Co	Qatar	Materials	5,186	15	19%	14.41	1.28	0.67	4.66
Jarir Marketing Co	KSA	Consumer Discretionary	4,831	152	38%	19.66	10.73	0.72	4.32
Emaar Development	UAE	Real Estate	4,803	4	-9%	5.63	2.33	-	-
Alawwal Bank	KSA	Financials	4,571	15	28%	14.95	1.25	0.99	1.67
Qatar Fuel Co	Qatar	Energy	4,533	166	63%	14.40	2.31	0.62	4.82

Small Cap Performance

Companies	Country	Sector	M. Cap (USD Mn)	Last Close	2018 (%)	P/E	P/B	Beta	Div. Yield (%)
Saudi Research and Marketing Group	KSA	Telecom	1,755	83	40%	52.65	6.25	1.03	NULL
Abdullah Al Othaim Markets	KSA	Consumer Staples	1,680	70	14%	17.59	4.05	0.64	3.57
Ahli Bank	Qatar	Financials	1,618	28	-25%	8.93	1.09	0.01	3.40
Saudi Ground Services	KSA	Industrials	1,544	31	-21%	15.40	2.06	1.16	8.44
Aamal Co QPSC	Qatar	Industrials	1,530	9	2%	12.29	0.70	1.05	6.79
United Development	Qatar	Real Estate	1,435	15	3%	10.72	0.48	1.09	8.47
Southern Province Cement	KSA	Materials	1,387	37	-24%	20.26	1.67	0.69	4.04
Air Arabia	UAE	Industrials	1,296	1	-18%	9.04	0.71	0.46	9.80
National Central Cooling	UAE	Industrials	1,279	2	-5%	10.94	1.02	0.80	4.62
Zain Saudi Arabia	KSA	Telecom	1,270	8	13%	NULL	1.31	1.23	NULL

Source: Reuters; Classification of companies are in accordance to MSCI methodology

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