August 2019

GCC Markets lifted by the rally in UAE and Kuwait equities

Undervalued Dubai equities attract investors; US Fed cuts interest rates

Research Highlights
GCC Economic and Market Commentary for July, 2019

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GCC markets ended the month of July on a positive note continuing the momentum from last month aided by the strong growth witnessed in the Dubai and Abu Dhabi stock markets. The S&P GCC composite index gained 1.1% for the month, extending its yearly gains to 11.0%. The global markets as well as the US indices registered gains during the month, in the run-up to the first interest rates by the Fed in more than a decade. Oil prices witnessed downward pressure even though OPEC decided to extend production cuts into 2020, due to the shadow cast by the negative outlook towards global demand growth and the consistent rise in output from U.S. fields.

We see the following four issues as key developments during the month of July:

1. **Kuwait's rally around MSCI inclusion – Will history repeat itself?**
   Markets that have been upgraded by the MSCI from Frontier to Emerging in the past decade have exhibited a pattern that is similar to each other in terms of their performance. With Kuwait securing a conditional upgrade in June 2019, will it follow the trend that has been previously observed?

2. **Foreign investment trends in GCC equity markets:**
   Foreign inflows into GCC equity markets could potentially be a key growth driver for the private sector, helping GCC economies in achieving their broader economic objectives. With Kuwait and Saudi Arabia securing emerging market inclusions in the recent past year, foreign investments into the GCC equity markets is expected to surge after remaining subdued during the past two years.

3. **ETF listings - Kuwait market gaining global prominence:**
   Kuwait has been recently upgraded to EM status by leading index providers. This has set in motion the listing of Kuwait-focused ETF outside Middle East for the first time. This could be a positive trigger for the markets and potentially lead to a wide range of instruments becoming available for foreign investors.

4. **Kuwait Retail Sector Positioned for Significant Growth:**
   Kuwait retail market is set to capitalize on the rise of consumerism due to favourable demographics, a rise in population and a strong growth trajectory in tourism and per capita income. The value of non-store retailing is forecast to increase by 48% in Kuwait between 2018 and 2023. With average mall occupancy levels at 93% and several supermarkets in the pipeline for 2019, Kuwait's retail sector is poised for solid growth.

GCC Market Commentary

GCC Market Trends – August 2019

Index	M. Cap (USD Bn)	Last close	2018 %	Jul-19	YTD %	S&P correlation**	ADVT* (USD mn)	P/E TTM	P/B TTM	Div. Yield
S&P GCC	893.6	119	8.4	1.1	11.0	0.105	**N.A**	14.8	2.0	3.4
KSA	556.5	8,733	8.3	-1.0	11.6	0.035	764.9	17.9	2.0	3.6
Abu Dhabi	150.9	5,318	11.7	6.8	8.2	0.083	47.1	13.5	1.5	4.7
Qatar	140.5	10,505	20.8	0.5	2.0	0.084	44.4	13.8	1.4	4.2
Kuwait	114.4	6,117	5.2	4.9	20.4	0.021	140.0	14.4	1.4	3.4
Dubai	79.9	2,918	-24.9	9.8	15.4	0.107	53.0	7.9	1.0	4.3
Bahrain	25.4	1,548	0.4	5.2	15.7	0.045	3.2	11.2	0.9	4.5
Oman	12.3	3,761	-15.2	-3.2	-13.0	-0.013	4.3	7.7	0.7	7.7

Source: Reuters, Zawya, Note: * Average Daily Value Traded ** - 3-year daily return correlation with S&P 500 index

The S&P GCC composite index, a comprehensive benchmark that covers stocks from all GCC countries, gained 1.1% for the month, lifted by the positive performance from the UAE markets. The emirates of Dubai and Abu Dhabi led the gains, rising by 9.8% and 6.8% respectively, followed by Bahrain, Kuwait and Qatar which closed 5.2%, 4.9%, 0.5% respectively for the month. KSA and Oman ended the month of July in the red, losing -1.0 % and 3.2% respectively.

Monthly returns heat-map of S&P GCC Composite index

Year	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Total
2014	3.4%	3.7%	2.7%	2.8%	3.2%	-7.4%	8.1%	6.4%	-1.4%	-6.8%	-10.9%	-4.4%	-2.6%
2015	2.8%	4.4%	-6.9%	10.1%	-2.3%	-3.5%	0.1%	-13.2%	-1.1%	-2.7%	-2.3%	-2.4%	-17.3%
2016	-10.7%	3.7%	1.9%	5.7%	-5.1%	1.1%	-0.1%	-1.2%	-3.9%	2.2%	7.9%	4.2%	4.3%
2017	1.6%	-0.8%	-1.5%	-0.4%	-1.4%	3.2%	-0.4%	0.9%	-0.6%	-2.7%	-1.5%	3.4%	-0.4%
2018	5.3%	-2.5%	3.4%	2.9%	-0.4%	1.1%	2.2%	-2.5%	0.2%	0.1%	-2.0%	0.7%	8.5%
2019	6.8%	-1.0%	2.8%	4.4%	-5.6%	2.5%	1.1%						11.0%

Source: Reuters

Kuwait continued its positive run in 2019, registering gains for the seventh consecutive month. Kuwait's All Share index rose by 4.9% while its Premier market index rose by 5.8% in July. Kuwait continues to be the best performing market in the GCC region in 2019 with a YTD gain of 20.4%. The impact of the MSCI upgrade process on the market have been clearly visible, and could continue to positively affect Bourse Kuwait in the period leading to the implementation and potentially even beyond. Among Kuwait's Blue Chip companies, Mobile Telecommunications Company and Kuwait Finance House were the top gainers, increasing by 9.3% and 9.2% respectively. Among sectors, Telecom index was the top performer in July, increasing by 8.4%.

Dubai Stock Exchange has been consistently gaining momentum in 2019 and was the star performer for the month of July with registered gains of 9.8% resulting in a yearly gain of 15.4%. The Abu Dhabi Index ended the month of July with strong gains of 6.8%. After Dubai's benchmark stock index lost almost half its value in the past five years, it is finally beginning to attract investors on the lookout for bargains. In its latest efforts to attract foreign investment, the UAE government is preparing a draft law that would allow foreigners to own up to 100% of businesses in the maritime industry in accordance with specific criteria. As, interest towards the Saudi Tadawul index tapers after the country's inclusion in the MSCI EM index, investors are now looking towards the emirates to offers the higher potential returns in the coming months. First Abu Dhabi Bank and Abu Dhabi Commercial Bank were the top performing blue chip companies with a rise of 7.6% and 7.5% for the month of July.

Among GCC Blue Chip companies apart from Kuwait, First Abu Dhabi Bank and Abu Dhabi Commercial Bank were the top gainers, increasing by 7.6% and 7.5%respectively, whereas Saudi Basic Industries Corporation and DP world lost 6.3% and 4.9% respectively.

Global Market Trends – August 2019

Equity	Last close	MTD%	YTD%
S&P GCC	119	1.1	11.0
MSCI World	2,188	0.4	16.1
S&P 500	2,980	1.3	18.9
MSCI EM	1,037	-1.7	7.4
MSCI FM	976	1.8	7.9
Commodities			
IPE Brent	65	-2.1	21.1
Gold	1,414	0.3	10.2

Source: Reuters

Global equity markets continued their positive trend in July guided by the strong performance witnessed in major developed markets with US leading the way. The MSCI World Index closed 0.4% higher than the previous month. The U.S. S&P 500, U.K.'s FTSE index and Japan's TOPIX rose by 1.3%, 2.2% and 0.9% respectively in July. The U.S. Fed lowered its key overnight lending rate by a quarter of a percentage point to a target range of 2.00% to 2.25%, cutting its rates for the first time since the depths of the financial crisis more than a decade ago. Fed Chairman Jerome Powell cited signs of a global slowdown, US-China trade tensions and a desire to boost low inflation in explaining the central bank's decision to lower borrowing costs. With no clear reasons for this stimulus, US stocks breached the 3000 mark for the first time ever in July, but witnessed slight pullback after the official announcement by the Fed. With the election of Boris Johnson as the new British PM, the chances of a hard Brexit has greatly magnified which can cause global uncertainty in the lead-up to the October 31st Brexit deadline.

Emerging markets were negative, losing 1.7% during the month of July, with China (Shanghai A shares index) losing 1.5%. Indian markets continued their negative performance with the Sensex losing 4.9% for the month. Oil prices witnessed downward pressure even though OPEC decided to extend production cuts into 2020, due to the shadow cast by the negative outlook towards global demand growth and the consistent rise in output from America fields. IPE Brent Crude lost 2.1% ending the month at USD 65/bbl.

1. Kuwait's rally around MSCI inclusion – Will history repeat itself?

Kuwait has been the best performer among GCC equity markets in the first half of 2019. The performance of Kuwait in recent times could be largely attributed to the upgrade to emerging market status by global index providers. Morgan Stanley Capital International (MSCI) announced on June 25, 2019 that it would conditionally reclassify Kuwait as an emerging market. On finalization, Kuwait's stocks would enter MSCI's emerging market indices from May 2020 with a weightage of 0.5%.

The rally of Kuwaiti stocks indicates the positive sentiment among investors stemming from the upgrade. The move is perceived by many as a sign of approval from MSCI, recognizing the improvements undertaken by Boursa Kuwait and Kuwait Capital Market Authority. However, it remains a question whether the rally is sustainable or driven by momentum.

MSCI's global equity indices are tracked by several investors. Assets worth approximately USD 1.9 trillion track the MSCI EM index while assets worth approximately USD 324 billion track its FM counterpart. Upgrade to an index that tracks more assets would naturally bring more inflows into the reclassified market. Therefore, investors tend to react to the decision positively, contributing to a surge in prices. Kuwait follows the footsteps of several markets that have received an upgrade from MSCI. On observing the performance of markets that have been either upgraded to Emerging from Frontier markets in the past two decades by MSCI, a pattern could be identified.

Markets upgraded by MSCI to Emerging markets from Frontier markets in the past 20 years

Country	Announcement	Effective from	Old Index	New Index	Returns % (b/w announcement and effective)	Returns % (effective +1 Year)
Pakistan	Jun-16	Jun-17	Frontier	Emerging	23.2	-10.0
Qatar	Jun-13	Jun-14	Frontier	Emerging	54.3	-12.1
UAE	Jun-13	Jun-14	Frontier	Emerging	98.3	-11.3

Source: Reuters;

Considering the evidence from past upgrades of Pakistan, Qatar and the UAE, the market performance between the announcement date and the effective date is better than the performance one year after the effective date. In the case of UAE and Qatar's upgrade, where the effective date coincided with the slump in oil prices, the market performance and liquidity have eroded further in subsequent years.

Kuwait went on a positive run in 2019, registering gains for the sixth month in succession, closing the first half of the year gaining 19.1%. Since the announcement of MSCI, Kuwait registered a gain of 4.0%[1]. From a valuation perspective, Kuwait has historically traded at a P/E range of 14x-17x between 2015 and 2018, suggesting that there is still potential for further upside at a P/E ratio of 14.4x, which is after factoring in the rally observed in previous months. Saudi Arabia, which received an upgrade prior to Kuwait trades at a P/E of 17.8x. However, Kuwait's dividend yield of 3.47% is the lowest among GCC emerging market peers.

Valuation metrics of emerging markets

Country	Market Cap (USD Bn.)	P/E TTM	P/B TTM	Dividend Yield
China	4,689	12.25	1.36	2.66
South Korea	1,085	12.10	1.25	1.28
India	982	23.75	3.32	1.18
Brazil	822	17.40	2.19	3.29
Saudi Arabia	572	17.80	2.06	3.53
Abu Dhabi	149	13.34	1.46	4.74
Qatar	139	14.00	1.41	4.15
Kuwait	**115**	**14.38**	**1.43**	**3.47**
Dubai	75	7.37	0.91	4.61

Source: Reuters; Data as of July 21 2019 close

[1] Returns between 25 June 2019 close and 21 July 2019 close

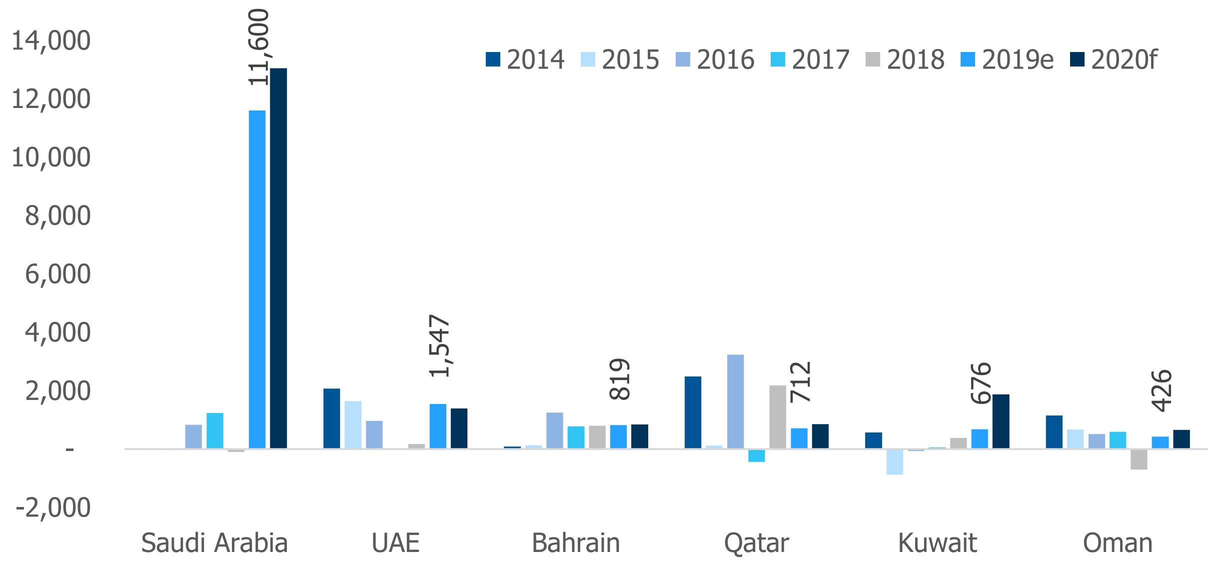
Despite past precedence where markets have initially surged due to the euphoria of earning an upgrade and slowly correcting later, it does not necessarily mean that Kuwait will exhibit the same pattern. With only one month having passed since the MSCI announcement, there is still a long way to go. As Kuwait is predominantly an oil based economy, the volatility in oil markets would be a key factor that could affect the performance of equity markets moving forward. With banking stocks having sizeable presence in Kuwait's equity markets, the effect of potential rate cuts by the Fed on the profitability of Kuwaiti banks remains to be seen. Geopolitical events are also potential factors that have historically been a drag on GCC markets, raising concerns of foreign investors. On the other hand, reforms undertaken by Boursa Kuwait, expansionary spending plans of the government to boost economic growth and the ability of Kuwait to absorb external shocks are expected to be perceived positively. Therefore, it is advisable to wait and watch whether Kuwaiti markets will continue to perform in the coming years.

2. Foreign investment trends in GCC equity markets

GCC countries are in the process of opening their economies to make them more attractive to foreign investors. The inflow of foreign funds through FDI would augur well for diversification of these economies away from oil to reduce their large oil dependence more so because it's markets are cyclical and volatile. Attracting investments in non-oil sectors through equity markets is also one of the means to achieve this goal. Foreign equity inflows into GCC capital markets is expected to rise sharply in the coming years, aided by the recent inclusions of Saudi Arabia and Kuwait in emerging market indices by global index providers such as MSCI, FTSE and S&P.

The influx of foreign capital into GCC equity markets would contribute to broader development of these markets and may allow domestic companies to raise capital at favorable rates from an enlarged base of investors. This in turn, will lead to higher growth of the private sector in these countries, a major objective of the governments in the region as part of their focus on growth of the non-oil economy.

Net Foreign Portfolio investment into Equity (USD million)



Source: IIF, Note: Non-resident flows are considered foreign flows

According to data from IIF, non-resident flows into GCC equity markets have been sluggish in the past two years, falling from USD 6.7 billion in 2016 to USD 2.2 billion and USD 2.7 billion in 2017 and 2018 respectively. Foreign portfolio investments into Saudi Arabia have been historically low, with 2018 seeing further deterioration due to geopolitical issues in the second half of the year. Saudi Arabia's markets witnessed an outflow of USD 99 million in 2018, as against an inflow of USD 1.2 billion in 2017. Saudi markets are expected to buck this trend in the next two years, owing to passive and active inflows from MSCI and FTSE upgrades, raising net foreign inflows to an estimated USD 11.6 billion and USD 13.1 billion in 2019 and 2020 respectively. Similarly, Kuwait markets are also expected to benefit from index inclusions. Net foreign portfolio inflows into Kuwait's equity markets in 2018 rose to USD 378 million in 2018 from USD 56 million in 2017, as the integration into FTSE EM index took place during the year. Furthermore, the inflows are estimated to progressively rise to USD 676 million and USD 1.9 billion in subsequent years (2019 and 2020) owing to the potential inclusions in MSCI and S&P EM indices. Qatar's markets were the best performer in terms of price returns as well as net foreign portfolio inflows in 2018. Its inflows amounted to USD 2.2 billion in 2018, up from a net outflow of USD 445 million in 2017. Qatar's ability to successfully manage the diplomatic isolation of GCC neighbors helped in changing the outlook of global investors on Qatar in 2018. The UAE's net foreign portfolio inflows have been on the decline since 2016, due to the slump in Dubai's property market. According to data from the IIF, net foreign portfolio inflows into UAE's equity market stood at USD 170 million in 2018.

Classification of major GCC equity markets by Global index providers

Country	MSCI	FTSE	S&P Dow Jones
UAE	Added to the MSCI EM Index in 2014	Weightage in Index - 1.02% No. of companies in index - 17	Weightage in Index - 0.7% No. of companies in index - 23
Saudi Arabia	Inclusion has commenced and will occur in two phases - May 2019 and Aug 2019.	Inclusion has commenced and will occur in five phases between Mar 2019 and Mar 2020. Expected weightage of 3.19% in FTSE EM All Cap by March 2020.	Inclusion has commenced and will occur in two phases - Mar 2019 and Sep 2019.
Kuwait	Conditionally reclassified to Emerging markets in June 2019 Inclusion into MSCI EM Index to take place in a single phase in May 2020 with 0.5% weightage	Weightage in Index - 0.89% No. of companies in index - 9	Will be included into Emerging Market indices by Sep 2019. Projected weight – 0.56%
Qatar	Added to the MSCI EM Index in 2014	Weightage in Index - 1.28% No. of companies in index - 21	Weightage in Index - 1% No. of companies in index - 23

Source: MSCI, FTSE and S&P; Data as of June 30

With several reforms being initiated and upgrades secured from global indices providers, GCC capital markets have attracted the attention of global investors. The flows from foreign investors into the equity markets in recent times look promising. The index inclusions are expected to drive passive and active inflows into Kuwait and Saudi Arabia in coming years, similar to what happened in the case of UAE and Qatar in 2014. The move is expected to have a knock-on effect on the other GCC equity markets as well.

Saudi Arabia, which is the GCC region's largest stock exchange in terms of market capitalization, has lagged behind its neighbours UAE and Qatar in previous years due to its reluctance to open its market to non-residents. However, Saudi markets have undergone several changes since then, and in 2015 they opened the doors to foreign investors by permitting non-resident institutional investors to invest directly. A string of reforms followed and ultimately led to inclusion of Saudi stocks by FTSE, MSCI and S&P. Further in June 2019, Saudi Arabia relaxed the 49% ownership limit for foreign strategic investors investing in Saudi equities, with a view to expand its institutional investor base and attract funds from foreign investors. Additionally, new rules have been framed to prevent major price fluctuations in stocks after their IPO. Tadawul exchange saw foreign inflows for six consecutive months in 2019, receiving net inflows of approximately USD 10.6 billion in the second quarter of 2019 alone. The first phase of MSCI EM inclusion, which coincided with this period is the primary reason for such huge inflows. Foreign ownership of Saudi equities touched record highs, closing at 7.47% at the end of June 2019, which is a record. Notably, the ownership was 1.4% at the end of Jan 2019

Kuwait, whose equity market is dominated by banking stocks, decided to lift the foreign ownership limits of local banks in a bid to increase inflows into the equity markets and lower the cost of capital through global participation. The move also bodes well for the potential inclusion of Kuwait into MSCI's EM index in May 2020, which again is expected to bring sizeable inflows into the country's equities. In the past one year, Gulf Bank has seen the biggest change, with the total foreign ownership rising from 1.5% in Aug 2018 to 11.5% in July 2019. National Bank of Kuwait, the largest bank in the country by total assets, has the highest foreign ownership among domestic banks at 13.4% as of July 2019.

Foreign Ownership of Kuwaiti Banks

Bank	Foreign Ownership (%)		Change in Ownership levels (%)	Free Float (as a % of shares outstanding)
	As of 09 Aug 2018	As of 17 July 2019		
National Bank of Kuwait	9.4	13.4	4.0	94.4
Kuwait Finance House	4.3	6.8	2.5	75.7
Boubyan Bank	1.6	3.3	1.8	38.8
Commercial Bank of Kuwait	0.2	0.5	0.2	76.6
Gulf Bank	1.5	11.5	10.0	76.7
Burgan Bank	3.2	2.5	-0.7	29.9
Ahli United Bank	0.3	0.6	0.3	16.1
Al Ahli Bank of Kuwait	0.1	0.1	0.0	42.3
Warba Bank	0.9	3.1	2.1	49.1
Kuwait International Bank	6.3	4.9	-1.5	51.8

Source: Reuters

The next one year is expected to be a busy period for GCC equity markets with the eyes of global emerging market investors focused on the region due to index inclusions. The time is right for GCC countries to push forward with further reforms and sustain the inflow of foreign capital. The role of capital markets does not end with index inclusion. They must ensure that corporate governance standards and disclosures are improved. Stricter regulations need to be enforced to improve transparency for market participants. Steps must be taken to encourage and incentivize more companies to seek listing and not remain as privately companies and family businesses. Capital market authorities must also facilitate listed companies to raise capital easily. To encourage investors, new products must be introduced so that liquidity remains strong, and investor confidence increases. Capital market authority needs to work towards making equity an attractive asset class for domestic investors. All this will ensure that GCC markets' index inclusions are not merely a flash in the pan, but a progressive step to help in achieving the broader objectives of the GCC governments to increase the inflow of foreign funds into the region for a faster and stable form of economic growth.

3. ETF listings - Kuwait market gaining global prominence

MSCI recently announced its decision to reclassify Kuwait to its Emerging Market index subject to availability of omnibus account structures and same National Investor Number (NIN) cross trades for international investors. Boursa Kuwait has committed to introduce these changes by November 2019. The move would be an upgrade from the country's current status as a Frontier Market and echoes similar changes made by S&P and FTSE Russell. Upon inclusion into MSCI Emerging Market Index, Kuwait will have a weightage of 0.5% and could attract inflows of USD 10bn[2].

Various indices provided by MSCI including Emerging Market index and Frontier Market index are widely used as a benchmark in the ETF industry. Investors gain exposure to Kuwait listed stocks by investing in ETFs that track Frontier markets or those with geographical focus as GCC or Middle East. However, these ETFs provide lower exposure to Kuwait, thereby limiting the ETFs ability to attract investors looking for higher exposure.

For instance, iShares MSCI Frontier 100 ETF, a US listed ETF has an exposure of 26.42% to Kuwait listed stocks with a total AUM of approximately USD 518mn. This means that out of the total AUM only USD 137mn is tracking the Kuwait listed stocks.

List of select ETFs with exposure to Kuwait

ETFs	AuM (USD Mn)	Expense Ratio	Kuwait Exposure
iShares MSCI Frontier 100 ETF	518	0.81%	26.42%
Invesco Frontier Markets ETF	62.2	0.70%	15.71%
WisdomTree Middle East Dividend Fund	25.1	0.88%	13.40%
MSCI GCC Select Swap UCITS ETF	32.4	0.65%	9.00%
Global X Next Emerging & Frontier ETF	19.2	0.55%	8.60%

Source: ETFDB, DWS | Note: AuM as of 19th July 2019

In April however, HANetf which is an independent provider of UCITS ETFs, launched first ever ETF in Europe that provides exposure specifically on Kuwait listed stocks. The KMEFIC FTSE Kuwait Equity UCITS ETF was created in partnership with Kuwait & Middle East Financial Investment Company (KMEFIC). The ETF tracks the FTSE Kuwait All-Cap 15% Capped Index and currently includes 15 listed companies. The ETFs AUM has grown to USD 43.17mn as of 18th July 2019. The ETF has a total expense ratio of 0.80% and is listed on multiple stock exchange in Europe including London Stock Exchange, Borsa Italiana and Xetra (Germany).

Top 10 Index Holdings and sectoral weightage - KMEFIC FTSE Kuwait Equity UCITS ETF

Company	%	Sector	Weightage
KFH	15.55%	Banks	63.15%
NBK	15.23%	Telecom	13.99%
AUB B.S.C.	14.97%	Industrial goods & services	13.83%
Zain	13.99%	Chemicals	4.30%
Agility	8.82%	Financial services	3.86%
Gulf Bank	6.64%	Food & Beverage	0.88%
Boubyan Bank	6.25%		
Boubyan Petrochemical	4.20%		
HumanSoft	3.87%		
National Industries Holding Group	2.66%		

Source: HANetf

[2] Franklin Templeton

UCITS - a regulatory framework of the European Commission that creates a harmonized regime throughout Europe for the management and sale of mutual funds.

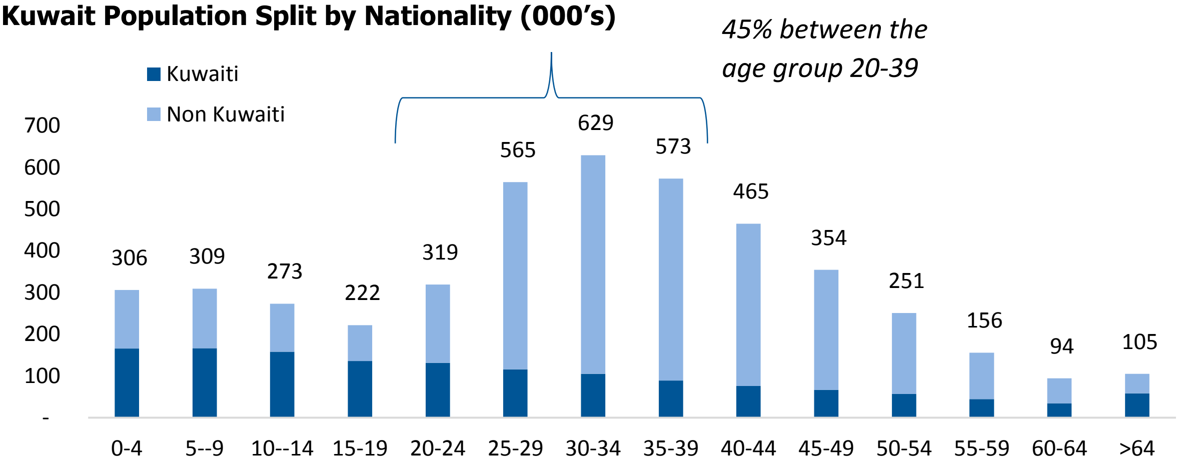
Therefore, for international investors, seeking exposure to Kuwait equity market may not be straightforward, therefore launch of ETFs focused on Kuwait equities can provide a platform to gain exposure to Kuwaiti listed stocks, that have been the leading performer not just in the region but globally so far in 2019. Kuwait All share index has gained over 25% as of 18th July 2019, though the rally in Kuwait's stocks is primarily attributed to positive sentiment surrounding MSCI's decision regarding the reclassification of Kuwait's market.

Thus, launch of Kuwait focused ETFs could just be the beginning of expansion of instruments available for foreign investors to participate in Kuwait's emerging economy. With launch of such ETFs, retail investors in the UK and other parts of the world will for the first time have direct access to the Kuwait equity market, which is one of the most stable markets in the Middle East.

4. Kuwait Retail Sector Positioned for Significant Growth

Kuwait's retail sector is small in absolute terms when compared to regional peers like the UAE or Saudi Arabia. However, Kuwait has one of the highest concentrations of international retailers in the GCC, with luxury segment proving to be a major draw. The value of Kuwait's retail market was KD 3.5bn or 9.1% of non-oil GDP, as of February 2018.[3] These figures are expected to grow even further as consumers have shown an increased preference for international brands and shopping experiences. Several factors have led to the success of the retail sector in Kuwait. As of 2018, Kuwait enjoys one of the highest per capita income in the world at USD 34,244 as compared to the global average of USD 11,297[4]. Moreover, Kuwait has approximately 45% of population in the 20 to 39 age brackets, and these young consumers have a high inclination towards retail spending in retail malls, and in the purchase of international brands.

Kuwait Population Split by Nationality (000's)



Source: Kuwait Central Statistical Bureau

Kuwait's retail demand remains split between popular community centers, with focus on food and beverage concepts, as well as larger scale regional shopping centers, which have demonstrated high occupancy rates and stable leasing rates. A new report by the global real estate advisory firm, CBRE indicates that in the second quarter of 2019 there was 702,000 square meters of shopping mall gross leasable area (GLA) in Kuwait, that was categorized as either regional or super regional in scale. Market outlook also reveals buoyant developmental activity across the retail sector with approximately 167,000 square metres of GLA is due between 2020 and 2021. Some of the major retail projects in pipeline include, Tamdeen Development in Al Khairan, Al Manshar renovation, Salhiya Retail Mall in Kuwait City, and a second mall by the Gate Mall Company.

Average mall occupancy levels across existing stock remain strong at 93%, indicating an opportunity for retailer as well as customer-led demand growth moving forward. Regional and super regional retail projects, scheduled to be launched in 2019, are designed to be consistently larger in scale than existing comparable properties with approximately half the operating supply seen to have a GLA of between 10,000 and 40,000 square meters.[5] The potential introduction of a 5% value-added tax (VAT) from January 2018 has been delayed until 2021 as higher oil prices have eased pressure on the financials of the Kuwaiti government. The delay in introduction of VAT has been a welcome relief for retailers and consumers alike.

[3] Oxford Business Group
[4] World Bank 2018 estimates
[5] Zawya

Rise of Hypermarkets

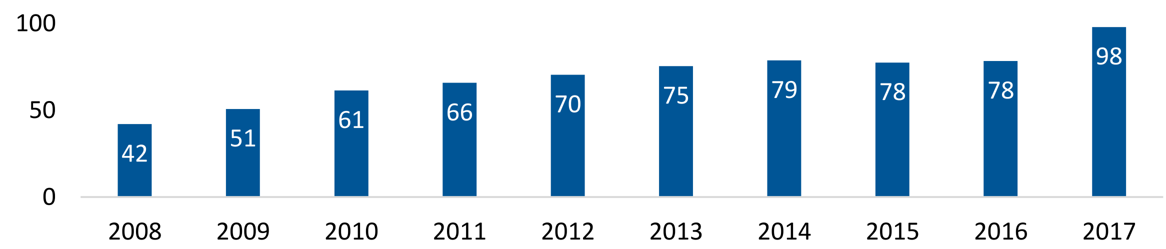
The penetration of large modern grocery stores in Kuwait have historically remained low, as local players like The Sultan Center and Kuwaiti Union of Cooperative Societies, a government union, still hold majority of the market share through their stand-alone grocery and convenience stores. Although market penetration of modern supermarkets and hypermarkets remains low in Kuwait at 45%, which is the lowest in the GCC, the situation is changing. Over the years private operators like Lulu and Carrefour are steadily expanding their presence in the country. Revenue generation from supermarkets and hypermarkets is predicted to grow at a strong rate.

With the arrival of hypermarket operators, the industry has started to turn more competitive with increased product offerings at competitive prices, thereby compelling local cooperatives to discount their goods so as to attract consumers. However, competitive pricing and increased product offerings are not the only way these modern supermarket and hypermarket chains are attracting Kuwaiti customers. They are also faster at responding to changing consumer demand. For instance, Kuwaiti supermarket chain Saveco has enjoyed substantial accomplishments, since opening its first store in 2014, targeting locals and mid to high earning expatriates. Partnering up with global retailers gave the company access to a range of exclusive and health-oriented food products, while its distinctive interior design, has helped to set it apart from local competitors. Moreover, Saveco have also succeeded in engaging effectively with customers online via social media platforms, enabling them to reach a larger customer base.

During the recent period, several large multinational retailers have announced expansion plans in Kuwait.

- In March 2018 LG Electronics opened a two-storey premium store in Kuwait City.
- 2018 also saw some US fast-food restaurant chain Wendy's, ramping up their presence in Kuwait, opening two additional stores in Kuwait International Airport and Al Kout mega-mall.
- A host of international brands including NYX Makeup, South Korea's Etude House and H&M Group's Monki, among others, also made their entry into the market in March 2018 with the opening of Phase IV of the USD900m Avenues mall.
- Galeries Lafayette, the high-end French department store chain, is set to open a 7500 square metres store in Kuwait City's Assima Mall in 2019.

Kuwait Internet users (% of population)



Source: World bank/Kuwait National ICT

The internet penetration in Kuwait is one of the highest in the world at 98% as of 2017. This has helped Kuwait's e-commerce market in expanding rapidly as Kuwaitis and expatriates are shopping online. The value of this subsector was estimated at USD 560Mn in 2014, and is expected to rise to over USD 1bn by the year 2020. There are approximately 2.4mn people actively shopping online in Kuwait, 65% of whom are adults below the age of 40[6]. Furthermore, Amazon's acquisition of Dubai-based online retailer Souq.com for USD580 million in July 2017 is expected to have a significant impact on the regional retail market. Kuwait is one of the major market's for Souq, and with Amazon reportedly looking for further regional expansion and acquisitions, Kuwait's e-commerce market is likely to become competitive.

[6] Marmore Estimates

Challenges for the Market

Kuwait retail sector remains challenging due to factors like government regulations, import delays, and limitations to the availability of commercial retail and warehousing space. There are very few good opportunities to open new stores and they tend to be very expensive, especially for hypermarkets. Zoning laws in the country are also strict, something which further squeezes the accessibility of retail space. This often impacts smaller firms the most, making it harder for them to increase market share. Moreover, Kuwait has introduced a rather stringent set of rules and policies for its expatriate population so as to address the rising concern among the local population which can have a negative impact on the retail sector. As a step towards Kuwaitization, the social affairs and labour ministry plans to lower expatriate population from 70% in 2018 to 34% by 2025[7]. Expatriates are increasingly exposed to layoffs, thousands of expatriate contracts being cancelled over the past year. Although there was an increase in total arrivals, the growth was associated with the implementation of new infrastructure and development projects, with the recruitment of blue-collar workers in support of employment figures.

Outlook

Euromonitor's research reported that Kuwait retail market is set to capitalise on the rise of consumerism due to favourable demographics, a rise in population and a strong growth trajectory in tourism and per capita income. The value of non-store retailing is forecast to increase by 48% in Kuwait between 2018 and 2023. The retail sector in Kuwait will attract considerable attention following the rise in international oil prices after several difficult years. With several supermarkets in the pipeline for 2019, there will be ample opportunity for brick-and-mortar retailers to expand business. Competition from hypermarkets is expected to increase over the years to come as consumers increase demand for foreign brands and lifestyle alternatives. As more and more consumers turn towards online shopping, retailers will need to focus more towards these platforms with increased efforts to integrate them into their customer experience models to avoid losing out on a wide customer base. It is expected that these trends will continue aided by stable macroeconomic fundamentals and government infrastructure programmes towards boosting growth and investment.

[7] Arabian Business - kuwait-considers-reducing-expats-by-15m-in-7-years

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