GCC and global markets trounced as pandemic fears weaken sentiment

Oil prices touch new lows on OPEC+ production cut disagreement

April 2020

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Kuwait and other GCC markets continued their downward spiral amidst coronavirus spread and oil price crash, as countries impose strict measures to curb the spread of COVID-19. GCC governments and Central Banks initiate reforms to soften its impact on the economy.

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

1. **Steps taken by GCC countries so far to fend off the economic impact of COVID-19–** GCC economies have proposed number of measures to address the economic impact of the COVID-19, such as fiscal stimulus packages, interest rate cuts etc. to ease the financial conditions and provide liquidity to the markets. With targeted and timely policy response, the region can stem the economic fallout from the outbreak.

2. **Did Saudi Arabia and Russia pick the worst time to wage a price war? -** With the global economy already reeling under the pressure of COVID-19, the timing of the oil price war couldn't have been much worse. For those involved, there is much more to lose than gain especially at such testing times.

3. **Parallels between COVID-19 and global financial crisis -** In the wake of coronavirus outbreak. Similar to the Global Financial Crisis (GFC) in 2008, state authorities have announced a slew of policy measures including aggressive fiscal measures to minimize the economic impact. We explore how the current crisis is evolving in a very similar manner to the GFC.

4. **Sectors under COVID-19's grip –** Fears of COVID-19 and measures to combat the virus' spread, such as lockdowns have affected businesses across sectors. While the actual impact on sectors and economies would depend on the virus' duration and intensity, we look at sectors that are likely to be most impacted.

5. **Kuwait market's biggest drawdowns and how long they took to recover –** As equity markets around the world decline sharply, we explore prior drawdowns in the Kuwait Stock market and analyse the subsequent recovery from each of them.

6. **Circuit breakers/trading curbs in GCC Stock Exchanges -** Investors have incurred huge losses because of massive volatility in stock markets caused by coronavirus worries. To contain volatility, stock exchanges in Kuwait, Dubai and Abu Dhabi have modified the circuit breaker regulations. We look at the history of circuit breakers and their effectiveness in curbing volatility.

GCC Market Commentary

GCC Market Trends – March 2020

Index	M. Cap (USD Bn)	Last Close	2019 %	Mar'20	YTD %	S&P correlation**	ADVT* (USD mn)	P/E TTM	P/B TTM	Div. Yield
S&P GCC	327.7	87	8.3	-18.2	-24.9	0.340	N.A	14.8	2.0	3.4
Saudi Arabia	2,004.4	6,505	7.2	-14.7	-22.5	0.315	1,126.1	15.1	1.6	-
Qatar	114.8	8,207	1.2	-13.5	-21.3	0.133	75.6	12.0	1.1	5.1
Abu Dhabi	111.6	3,735	3.3	-23.8	-26.4	0.271	56.5	9.4	1.0	6.5
Kuwait (All Share PR)	88.0	4,823	23.7	-20.6	-23.2	0.201	409.6	11.3	1.0	4.4
Dubai	53.1	1,771	9.3	-31.6	-35.9	0.287	66.0	4.3	0.5	0.0
Bahrain	22.2	1,351	20.4	-18.7	-16.1	0.204	17.4	10.2	0.8	5.0
Oman	11.0	3,448	-7.9	-16.5	-13.4	0.169	13.1	7.1	0.6	8.0

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

S&P GCC composite index declined by 18.2% for the month, with all markets posting losses. With businesses across sectors affected by coronavirus spread, oil price crash has fueled further declines in share prices. Dubai registered the highest loss, declining by 31.6%. Saudi Arabia ended the month losing 14.7%. Qatar has fallen the least, stemming its losses at 13.5%. S&P has affirmed its current sovereign credit ratings for Saudi Arabia and Qatar at A- and AA- respectively, citing strong fiscal buffers. UAE, Saudi Arabia and Qatar had announced fiscal and monetary stimulus over the month. The fiscal stimulus aided markets in limiting the losses. Following the U.S Fed, the central banks in GCC economies had also cut interest rates.

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

S&P GCC	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%	8.4%
2019	6.8%	-1.0%	2.8%	4.4%	-5.6%	2.5%	1.1%	-5.8%	-0.7%	-2.6%	1.3%	5.9%	8.3%
2020	-0.9%	-7.4%	-18.2%										-24.9%

Source: Refinitiv

Kuwait All Share Index registered a loss, decreasing by 20.6% in March. Among Kuwait's Blue Chip companies, Agility Public Warehousing was the biggest loser, falling by 28.4% as lockdowns cause supply chain disruptions. S&P has downgraded Kuwait's credit ratings from AA to AA- with stable outlook, citing lower oil prices and slow pace of reforms. Following the U.S Fed's lead, Central Bank of Kuwait has cut its policy rate twice this month, by a cumulative 125 bps. Fitch Rating has opined that Kuwait's banks are better placed than its GCC peers to handle the current crisis. However, with rate cuts and measures such as delayed loan repayments expected to affect the sector's profitability, banking sector index has decreased by 23.0% for the month. While Consumer goods sector was the top gainer at 2.2%, Consumer services sector was the top loser, falling by 28.0%.

Among the GCC Blue Chip companies, Saudi Telecom had gained by 5.9%. Emirates NBD has declined by 42.4%. The bank has taken measures such as deferment of loan repayments to help borrowers.

Global Market Trends – March 2020

Equity	Last close	March change (%)	2020 change (%)
S&P GCC	87	-18.2	-24.9
MSCI World	1,853	-13.5	-21.4
S&P 500	2,585	-12.5	-20.0
MSCI EM	849	-15.6	-23.9
MSCI FM	722	-22.8	-27.1
Commodities			
IPE Brent($)	23	-55.0	-65.5
Gold($)	1,571	-0.9	3.6

Source: Refinitiv

The performance of Global equity markets was negative with the MSCI World Index losing 13.5% for the month. U.S. equities (S&P 500) fell by 12.5% in February. U.S. Fed has cut its policy rate twice this month, to near zero. It also announced quantitative easing (QE) and other measures to ensure liquidity and credit flows to household. The Fed's strong action was construed as signalling a negative outlook, pushing the markets down. U.S. has passed a USD 2 trillion stimulus package to support its economy. The UK market (FTSE 100 index) closed 13.8% lower during February. UK has also cut rates, initiated QE and has pledged a fiscal stimulus. Emerging markets ended the month in negative, with the MSCI EM posting monthly loss of 15.6%. China's Shanghai A - share index has declined by only 4.5%, aided by slowdown in spread of the virus, resumption of factory activities and monetary policy stimulus.

Oil prices closed at USD 22.7 per barrel at the end of March 2020, which is 55.0% lower than February 2020. Earlier this month, talks between OPEC+ allies broke off with Russia refusing to agree to further production cut. Saudi Arabia retaliated by decreasing price of its oil to some of its customers and announced plans to increase its oil output by 2 million barrels per day. Notwithstanding the weakening demand due to coronavirus, these developments have pushed the oil price to record lows. As lower oil price would also affect shale producers, U.S. is taking efforts to end the oil price war. Gold has marginally decreased by 0.9% over the month. It has been a volatile month for the yellow metal. While spread of the virus moved investors to the safe haven asset, fiscal stimulus and investors selling the metal to cover their positions pushed prices down.

1. Steps taken by GCC countries so far to fend off the economic impact of COVID-19

The Coronavirus has spread across the GCC countries, besides its immediate impact on the public health and the well-being of the residents and citizens, the outbreak will likely have significant economic consequences across the region. As the key economic activities in the region's critical non-oil sectors like tourism, transportation are curtailed, we can expect greater macroeconomic implications. In response to the crisis, the gulf region has introduced number of new economic measures to mitigate the impact of the coronavirus and help stabilize the region's economy. At present, the policy responses primarily aim to support the individuals, businesses and sectors that will have profound impact from the downturn caused by the pandemic.

GCC interventions to support the economy

1) Fiscal Stimulus to offset the economic fallout

The gulf countries have announced financial stimulus packages of billions of dollars to revitalize the impact caused by the COVID 19 on the economy. The stimulus will enhance liquidity and help cushion the blow on the GCC economy and businesses. The hefty stimulus programmes will provide direct benefits to individuals, corporations, businesses and industries amid the ongoing coronavirus crisis. UAE announced an economic stimulus package of 126 billion dirhams (USD 34.3 billion), Abu Dhabi, the largest emirate, unveiled a AED 9 billion (USD 2.4 billion) stimulus package. The emirate's accelerator programme, Ghadan 21 is expanded to include 16-point plan that includes fee exemptions, fine waivers, SME support, and AED 1 billion allocated to establish market makers fund. Similarly, Dubai rolled out a AED 1.5 billion economic stimulus package which includes a 15 point plan.

Saudi Arabia, on the other hand announced a SAR 120-billion (USD 32 billion) worth of measures. Exemptions and postponement of government levies and fees are some of the initiatives carried out across the region to provide liquidity and bring in stability. Qatar declared a QAR 75 billion (USD 20.6 billion) package and the government of Bahrain has announced a USD 11.38 billion (29.6% of its annual GDP) economic stimulus package. In case of Kuwait, the cabinet approved a bill to increase the budget of ministries and governmental departments by KD 500 million (USD1.6 billion) for the 2020/21 fiscal year. The country has also established a fund that will allow contributions from companies, individuals and institutions; the Central Bank of Kuwait initiated a KD 10 million fund to support the economy.

2) Budget cuts

As the present economic conditions can increase the fiscal stress in the region, some of the gulf countries have declared cut back on their spending. Oman reduced its budget for civil, military and security agencies by 5% for the year 2020. Saudi Arabia's budgeted spend will be cut by SAR 50 billion (USD 13.32 billion), that corresponds to 5% of the budget, in areas with least social and economic impact. As the pandemic will likely impose strain on the countries' budget, spending cut will be a key policy action to help ease pressure and balance the budget.

3) Reducing risks in the financial system

Central banks across the GCC have rolled out support schemes to reduce the risks in the banking system. Initiatives are undertaken to maintain the market confidence and stability in the financial system. The central bank measures aims to ease the financial conditions, provide liquidity to the markets and support vulnerable sectors like SMEs. The Saudi Arabian Monetary Authority (SAMA) has announced a package of SAR 50 billion (USD 13.32 billion), to support the banking sector, financial institutions and SMEs. The Central Bank of UAE (CBUAE) has issued a support package of USD 34 billion. The stimulus will allow banks to provide relief for its retail and corporate customers from interest and principal repayments. To boost lending, the central bank allow banks to free up their regulatory capital buffers. It has also revised the real estate Loan to Value ratios and reduced the capital that banks must hold against loans to SMEs.

The Central Bank of Kuwait (CBK) will provide liquidity to commercial banks; the Kuwaiti banks have suspended the charges and commissions levied on POS, ATM and online banking transactions and extended collection of due payments. Oman's central bank provides OMR 8 billion (USD 20.8 billion) as extra liquidity to banks. The Omani banks have also cut banking fees, adjusted capital and credit ratios, and allows repayment postponements for up to six months. On a similar move, the Qatar central bank suspended the charges and fees levied for POS and ATM transaction and delayed loan installments.

4) Rate cuts

The GCC banks have lowered the interest rates to support the market functioning during the pandemic crisis. The UAE central bank reduced its interest rate on one-week certificates of deposit by 75 basis points. Saudi Arabia’s SAMA cut repo and reverse repo rates by 75 bps, while Kuwait’s central bank cut its deposit rate by 100 bps (1 per cent) to 1.5 per cent, its lowest ever. The Central Bank of Qatar reduced its deposits, lending, and repo rates. Bahrain’s central bank has slashed its lending rate and cut overnight, weekly and monthly deposit rates.

The coronavirus pandemic has created high uncertainty across the world and in the region, the GCC banks and the government have taken unprecedented measures to ease the pressure on economies and to maintain economic and financial stability. The gulf economies are creating sufficient buffers to boost the resilience of the financial system in the region. Coordinated policy action by the GCC economies can help mitigate the multiple shocks caused by the pandemic. As the crisis unfolds, more economic and financial stimulus package could be flagged, targeted and timely policy response across the region can help address the adverse economic consequences due to the COVID-19 outbreak.Kuwait was the best performing market in 2019 among GCC countries, riding on the positivity of expected upgrade to MSCI Index. While Kuwait's Premier Market index gained 32.4 per cent last year, Main Market index only increased 3.6 per cent. The average value traded in the Premier Market consisting of 18 stocks was about 84 million whereas that in the Main Market consisting of 156 stocks was about 20 million. Given the number of stocks, the volume seems low. This highlights the need and scope for improving participation in the main market, as greater participation enhances market efficiency.

2. Did Saudi Arabia and Russia pick the worst time to wage a price war?

At a time when economies worldwide have been put under stress and are contemplating the negative impact of COVID-19, the last thing they would have wanted was a price war between two of the world's largest oil producers. Coming into the year 2020, the overarching theme was a dip in global oil demand that would need strict supply restrictions to balance the Oil markets. However, with Russia's non-cooperative stance and Saudi Arabia's subsequent retaliation, oil prices have tumbled down to record lows. Saudi Arabia's reversal in stance to raise output by 2 million barrels per day and offer discounts on its oil came as a surprise as it has been a strong advocate of the supply cuts to keep prices high in recent years.

Why are they doing it?

Russia, despite also being heavily dependent on revenues from oil, decided to walk away from OPEC's proposal and let prices fall. It is widely perceived as an attempt to hit the U.S. that has been using export sanctions as a tool against other economies. Keeping oil prices low would hurt high-cost shale producers in the U.S., driving them out of business and would undermine the U.S. influence on the energy market. With a significant amount of financial cushion, Russia has the capability to withstand a period of low oil prices without straining its budget too much in the short term. Saudi Arabia on the other hand refused to budge, stating its intent to ramp up production and increase its global market share. Considering Saudi Arabia's ambitious diversification plans and the ineffectiveness of its previous oil price war, the move could be a ploy to bring Russia back to the negotiation table. Both sides refuse to budge so far, with the Russian Oil minister stating that they enough resources to cover budget shortfalls for the next 10 years if prices remain between USD 25-30 per barrel. Saudi Arabia, likewise, has ramped up production, regaining its position from the U.S. as the world's largest oil producer.

Why is the timing wrong?

The U.S.-China trade war had been threatening the global economy earlier, with several people anticipating a global recession due to protectionist measures taken by two of the world's largest economies. The global manufacturing scene looked bleak, facing slowdowns in major economies across the globe. Global oil demand had already been trending downwards, with oil prices falling from interim highs reached during 2018. With a preliminary trade deal in place, demand was expected to gradually pickup. The spread of COVID-19 quickly played spoilsport, adding further pressure from a demand side. The supply side was already under great pressure, needing oil producers to effect further cuts. In such a situation, the decision to ramp up production will only make things worse, flooding the market with cheap oil. The imbalances caused by simultaneous demand and supply shocks could end up disastrous especially when countries around are already reeling under pressure to reinvigorate economic activity. The pandemic has already forced several countries to go into lockdown, with many others set to follow. It is estimated that there might be a 25% demand contraction as a result of this pandemic. Several oil exporting countries are highly dependent on oil revenues to support their spending and balance their budgets. Low oil prices and a slowdown in activity would be a recipe for disaster for some of those nations whose financial reserves are low.

Who are the losers in this war?

The two primary parties involved, namely Saudi Arabia and Russia are not completely immune, having a set of problems of their own. Russia seems to be in a slightly better situation, with only roughly 40% of its revenues depending on oil and the breakeven oil price being lower than that of Saudi Arabia. Russia will have to drawdown from its reserves as the current price levels would mean that they would have to absorb losses in production. Production costs might be in favour of Saudi Arabia, but what seems to not be in their favour is their high dependence on Oil. Saudi Arabia's break-even oil price is expected to be USD 91 per barrel, which is comfortably above three times the current price. Its ambitious diversification plans - Saudi Vision 2030, has already hit several interim roadblocks. With current expenditure required to keep the citizens happy, their ability to do capital expenditure to incubate budding non-oil industries would be severely constrained. Despite having large financial buffers, the amount of drawdown will be unsustainable for Saudi Arabia. To put things in context, Russia would need to draw approximately USD 20 billion a year from the fund to balance the budget, whereas Saudi Arabia had already projected a deficit of roughly USD 50 billion before prices went tumbling. Lower prices would bring their deficit to three figures. The Saudi government has already proposed a cut in expenditure for the fiscal year 2020/21 citing unfavourable economic conditions and has asked several departments to formulate a plan to cut down their expenses by 20-30%. The U.S. Shale industry has been under profitability pressure and high debt levels. Lower oil prices would likely push them out of business. However, they have been able to navigate the previous low oil price levels witnessed in 2014-15. Therefore, things are not clear whether the price war would have a material impact on U.S. shale in the long term. Typically, low oil prices are a positive sign for oil importers. But in the current scenario where global manufacturing activity is close to a halt, the windfall from low prices could be considered only as a minor respite rather than a major advantage considering their stressed fiscal positions. Less wealthier nations of OPEC are also severely affected as their production capacity is not high enough to reap benefits from increased production while their economies are fragile enough to collapse if low prices become a norm. Overall, there are no clear winners in the price war, especially with a pandemic still spreading across the world.

Saudi Arabia and Russia have picked a very inauspicious time to engage in an Oil price war. Cases like Nigeria, Angola, Mexico and Venezuela are examples of nations that have wasted the benefits of oil wealth due to mismanagement. For several years, GCC nations have used revenues from oil to constructively transform their economies and build sizeable wealth for drastic situations. With the world gradually moving away from oil, they need to focus on sustainably developing their non-oil sector. A price war would not be of help, putting several oil dependent economies under pressure. Maintaining an equilibrium in the oil markets is the best way forward for everyone involved, especially in such testing times.

3. Parallels between COVID-19 and global financial crisis

Markets worldwide have experienced unprecedented volatility in the wake of the coronavirus outbreak. Though the mortality rates of those affected is much lower than that of Severe Acute Respiratory Syndrome (SARS) or the Middle East Respiratory Syndrome (MERS), Coronavirus disease – 2019 (COVID-19) being highly contagious has spread to over 190 countries and resulted in over thirty thousand deaths, majorly in Italy, Spain and China . Considering the severity of the outbreak, the World Health Organization (WHO) has declared it a 'pandemic'.

Similar to the Global Financial Crisis (GFC) in 2008, state authorities have announced a slew of policy measures including aggressive fiscal measures and have launched necessary actions like lockdowns and curfews to slow down the contagion, put an end to the outbreak and to minimize the economic impact.

The way the current crisis is evolving is very similar to the GFC in many ways:

Failure to separate the good from the bad

The carriers of the virus may not exhibit any symptoms (asymptomatic) yet could infect or transmit the virus to other. The inability to detect the virus carriers at an early stage makes it impossible to contain the outbreak unless large swathes of the population quarantine themselves for a long period. Similarly, subprime mortgages (not-so-healthy credit) were packed along with better quality mortgages (healthy credit) through securitization process and were sold to investors. Backed by rating agencies who underwrote the credit quality, they spread across investors including large financial institutions. Inability to detect them early and failure to quarantine them eventually led to freezing up of banking and credit channels leading to global financial crisis in 2008.

It is okay, until it is NOT

In 2008, it was widely believed that the real estate prices would never fall. Analysts relied on historical real estate price behaviour to extrapolate further rise on an incremental basis. This view was reinforced by the actions of rating agencies that continued to underestimate the risk attached to Collateralized Mortgage Obligations (CMOs) and Collateralized Debt Obligations (CDOs). On similar lines, when the initial news of the virus broke analysts tried to model the outcome based on SARS, MERS and other infectious diseases and underestimated its potential impact. The very fact that COVID-19 had a low mortality rate than the others has led to a much faster spread of the disease as asymptomatic people unwittingly spread it to others before they were diagnosed. Meanwhile, the world itself is much more globalised and integrated now in 2020. As a result, the world is experiencing an unprecedented crisis as the virus has spread to most countries and the number of infections continues to rise unabated.

Rejection, Realisation, Reaction

During both the instances, the actors involved underplayed and largely ignored the early warnings. In 2008, policy makers played down the gravity of the situation and only acted when the financial system was on the brink of collapse. Now, China had silenced the whistle blower and denied the contagiousness of the virus till the end of January. Other countries in the west like US, UK and others also did not take drastic measures like lockdowns until it was too late. As a result, many governments worldwide are only now imposing strict testing and containment measures and advocating social distancing as a way to tackle the coronavirus crisis.

Local to Global

In 2008, the global financial crisis was perceived to be a problem pertaining to the mortgage segment in the U.S real estate. However, in a span of weeks the crisis spread and engulfed the global banking and financial sector and eventually the wider economy was also affected causing immense economic pain and damage. Likewise, initially COVID-19 was thought to be a problem within a Chinese province or at best an Asian problem. Many thought it would be regionally contained like the SARS/MERS. As it has now spread globally, the ramifications are being felt globally. The major western countries have basically halted their economy to stop the spread of the virus, causing great economic pain just like in 2008.

Will the COVID recovery be the same as the GFC?

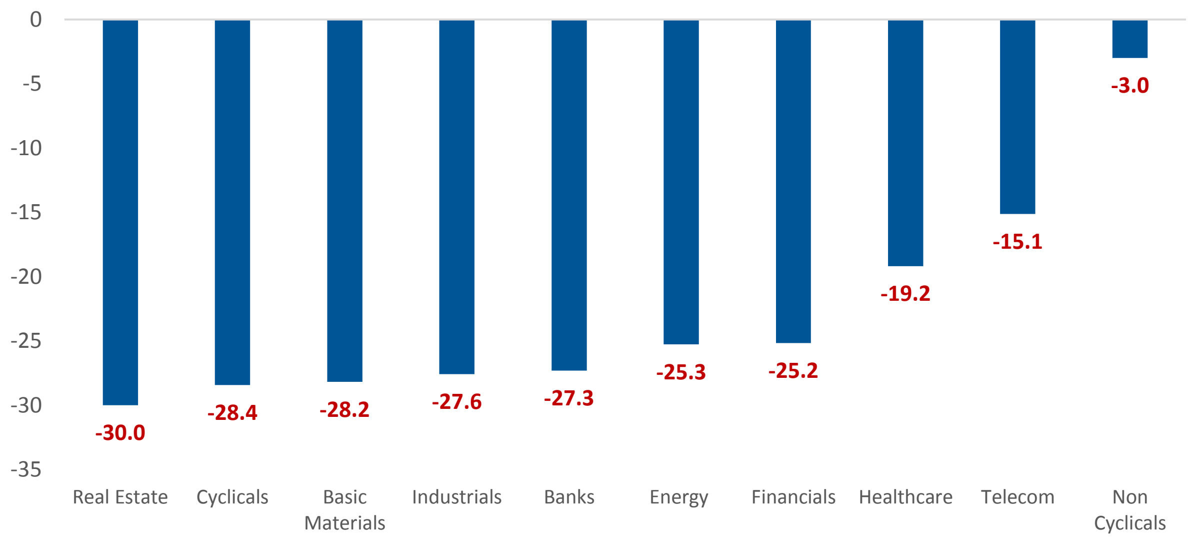
The global economy recovered from the GFC by Q3 of 2009 as the US and other major western economies came out of the recession. However, it took nearly 10 years for many western countries to reach the unemployment levels to pre-crisis levels. This time too, a long road to recovery lies ahead, only it looks much worse. The 2008 GFC was primarily a financial crisis which was addressed by bailouts by governments and central bank actions like lowering interest rates and Quantitative easing. The real economy was mostly intact as factories, offices and restaurants were still open and once the banks started lending again, consumer demand started picking up and the economy made its slow road to recovery.

This time however, we have a massive public health crisis which has led to a voluntary shut down of the entire economy. No amount of central action will restart demand unless the disease is contained in a significant way. Even the trillions of dollars in stimulus packages announced by governments can allow people and businesses to just survive for the moment. Many of the shuttered small businesses might never open again. Already we can observe the effects. On March 21, 2020 unemployment claims in the US shot up to 3.3 million. Two weeks earlier that number stood at 211,000. Such a dramatic plunge in economic activity is simply unprecedented and makes the current situation more akin to the great depression of 1929 than even the GFC. Reopening the economy prematurely can worsen the health crisis. Until a cure is found, governments have to make tough decisions on how long the social distancing measures are going to continue. To conclude, while there are similarities in the way both the crisis have evolved, a lasting cure for the economic crisis caused by Covid-19 is going to come from scientists and researchers who can find a cure or a vaccine. Until then, policymakers can only hope to contain and mitigate the economic impact to as little as possible.

4. Sectors under COVID-19's grip

As the COVID-19 pandemic continues to cast its shadow far and wide, businesses across sectors are likely to be negatively impacted. This has also reflected in equities, as stocks across sectors have taken a hit.

GCC Indices and their YTD (in %)



Source: Refinitiv; Note: Data as of 25th Mar 2020. Cyclicals includes Hospitality, Tourism; Basic Materials includes Construction; Industrials includes Aviation, Logistics.

While initial concerns were of a spill over effect from China, the virus' spread across regions, including GCC, has caused both demand and supply side shocks. As the contagion continues to spread, the actual impact on sectors and economies would depend on its duration and intensity.

Based on the developments so far, the following sectors are likely to be most affected in GCC.

Real Estate and Construction

Decreased demand in real estate would affect the sector in the near term. In countries like UAE, where oversupply had been a concern before the virus outbreak, the impact might be compounded. However once the virus threat abates, the residential sector might recover sooner aided by government measures such as Abu Dhabi's waiver of real estate registration fees and low interest rate environment. The downside for residential real estate is the unemployment trends that may prop up if the virus persists.

Social Distancing and lockdowns have caused closure of malls, offices and other commercial spaces. Many landlords are giving tenants the option of delaying rent payments. There is a call for rent freeze from commercial tenants. These measures might weigh on landlords' revenues and erode credit quality. Trends sparked by COVID-19 like work from home at scale and increased online shopping might impact demand for office and retail spaces in the long run.

From availability of construction materials to labour shortages and work stoppage to contain coronavirus spread, construction sector is being struck from multiple angles.

Energy

Hit by the double whammy of lower demand due to virus outbreak and oil price war, the energy industry is one of the most affected sectors. Energy was also one of the earliest sectors to be impacted. Even when the outbreak was limited to China, with it being the largest importer of oil, demand was expected to fall and oil prices started declining. The demand is expected to fall by about 15-20 million barrels per day in the next few weeks.[1] The uncertainty in outlook because of virus' spread and historically low prices have led to oil majors across the world slashing their expenditure budget.

Travel and Tourism

One of the first measures taken by countries to contain the spread was to impose travel restrictions. This has hurt aviation and hospitality industry at its core. In airlines and hospitality, time is an important component in service delivery. While in goods, higher demand at a later might compensate for current decrease, it is not the case in service based sectors. Demand once lost is an opportunity gone by.

In the week from 9th -16th March 2020, airlines in Saudi Arabia and UAE had reduced capacity by 15.3%.[2] International Air Transport Association has projected that airlines in the middle east are facing a 2020 revenue loss of USD 19 billion, with the revenue loss around the word estimated at USD 252 billion. CAPA Centre for Aviation has estimated that most airlines globally will be bankrupt by the end of May without coordinated government and industry action. Airlines are reportedly taking measures such as salary cuts and cancelling or postponing 2019 dividends.

Cancellation and postponement of events have cemented the decrease in demand in hospitality. Travel restrictions have led to free fall in occupancy rates and in turn revenues. Hotels are reportedly closing bookings to tide over these tough times. The magnitude of impact is still a question with expectations of it being on the higher side.

Banking

As businesses across sectors face the heat, given their credit exposure to other sectors, banks would not remain unscathed. A host of factors from weakening credit profile of borrowers, probable increase in NPAs, lower interest rates in the near term to measures such as deferring loan repayments might affect bank's profitability. Lower oil prices and potential slowdown in economic growth may slow down banks' credit growth.

Healthcare

Healthcare is the sector most intertwined with COVID-19. As the number of cases increase across countries, healthcare is swamped with COVID-19 patients in most countries. Outpatient departments are closed and planned surgeries have been postponed, leading to revenue loss for healthcare providers. Inadequacy of healthcare infrastructure - from basic protective gears to sophisticated equipment - is under spotlight as even developed countries with advanced health care systems struggle to cope with the crisis.

Education

With schools and universities asked to shut down, online learning has gained traction. From advanced apps to basic video platforms, education ecosystem is trying to make online learning work as seamlessly as possible. This might change the way the sector works in the long run. Education technology providers would stand to gain from this change. COVID-19 scare may be a deterrent for students to study abroad as it might affect perceptions of personal safety, reducing foreign student numbers at the institutions. However, as countries would take efforts to improve their health systems, this might not be a long term trend.

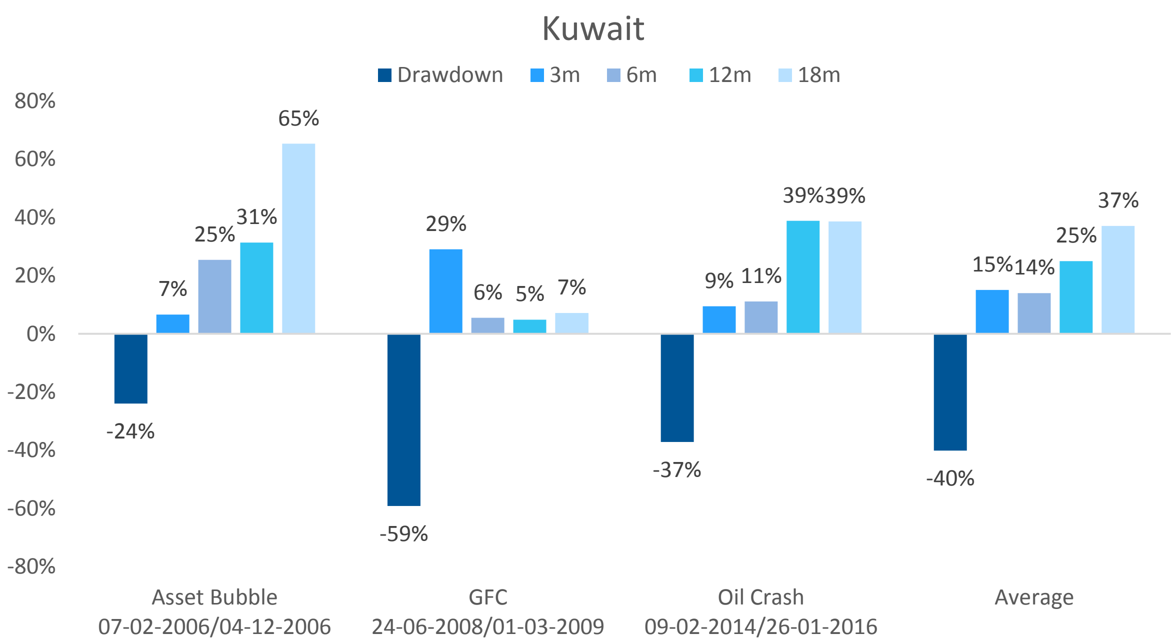
The suddenness and speed of the virus spread has added to the magnitude of the blow to businesses. While some are optimistic over pace of business revival once the COVID-19 scare passes, there is a downside risk that prolonged virus spread might push the world into recession. With the coronavirus curve flattening out in some countries, there is hope that this health crisis shall soon pass. Once it does, fiscal measures and favourable interest rates would provide adequate support structure as demand revives and sectors rebound.

[1] Estimates by Goldman Sachs, Vitol and IEA
[2] Visual Capitalist

5. Kuwait market's biggest drawdowns and how long they took to recover

Stock Markets the world over are quick to factor in and respond to global events. Research has shown that negative news affects the markets far more than positive news. Markets fall sharply after a negative event and the subsequent recovery is much more gradual. This peak to trough decline during a specific period is referred to as a drawdown. For example, due to the combination of coronavirus outbreak and oil price crash, the Kuwait Premier Market index fell 35% from the peak on Jan 19, 2020 to a low of 4,661 on March 16, 2020. Such a massive fall in a short period of time is a great cause of worry for investors. Another point to be noted is individual investors always underperform the benchmark index over time by allowing 'behaviors' to interfere with their investment discipline. It would be helpful to look at prior drawdowns of the benchmark index of Kuwait and analyze the subsequent recovery from those lows

Past drawdowns in Kuwait Stock Index and subsequent market performance



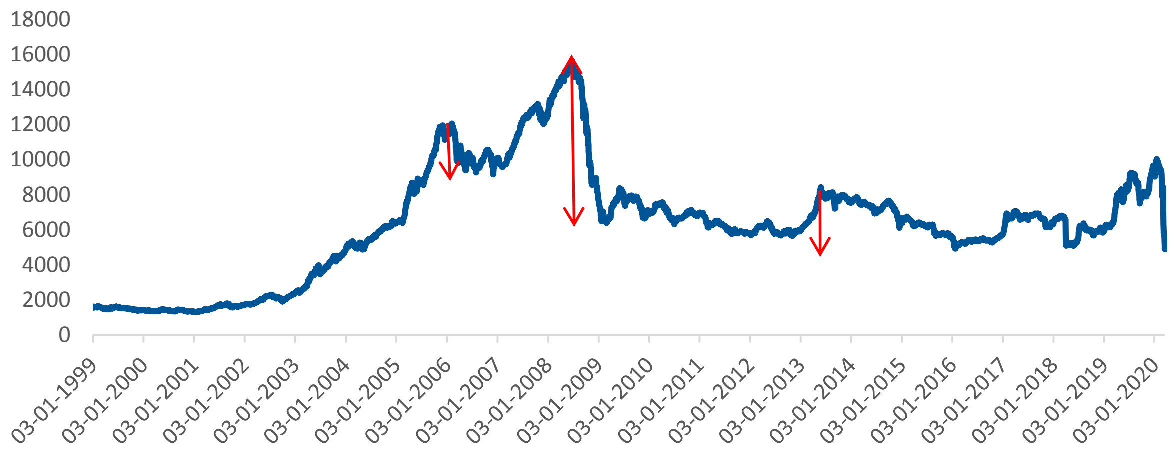
Source: Refinitiv; Note: 3month, 6month, 12 and 18months market performance after crisis period has been displayed

Variety of triggers

In recent times, a variety of triggers like speculative asset bubbles, global financial crisis, oil price crashes have caused drawdowns in the Kuwait stock markets. The subsequent recovery after each drawdown is dependent on a number of factors. The magnitude of the event's impact, fundamental strength of the country's economy and initiatives taken to respond to the event determine the magnitude, pace and persistence of recovery from the drawdowns.

In this context, we analyze the major drawdowns and the subsequent recovery of Kuwaiti markets in the recent past.

Closing Value of Kuwait Stock Exchange Index (KWSEIDX) from Jan 1999 – Mar 2020



Note: The Red arrows showcases the previous drawdowns in the Kuwaiti Stock markets

2006-07 Asset Bubble Burst

The crisis originated in Saudi Arabia and spread to other markets in the GCC including Kuwait. From 2002-2005, oil prices doubled. The stock markets were also in a bull run. Stock prices rose far away from fundamentals finally leading to a crash in 2006-07. The KWSE index fell 24% from the peak of 12,054 on February 7, 2006 to the low of 9,164 on December 4, 2006. The markets staged a recovery after that and by June 2007, the original peak of 12,054 was surpassed. The markets were able to recover because the drawdown itself was not as severe in Kuwait as in other GCC countries like Saudi Arabia which fell 67% from the peak of the asset bubble. Also, valuations had not gone up significantly during the bubble period and made the drawdown far less and enabled a recovery.

2008-09 Global Financial Crisis

Kuwaiti markets would not only recover, but go on to reach new highs in 2007 and 2008. This was due to oil prices rising steadily in the second half of 2007 and first half of 2008 before peaking at $147 per barrel in July 2008. KWSE also rose in tandem and reached a peak of 15,654 on June 24, 2008. This time valuations were higher and there was speculative capital inflows as well. However, the global markets collapsed after September 2008 leading to oil price crash and a deep fall in the Kuwaiti Stock markets, which touched a low of 6,391 in March 2009. The global nature of the event and high peak valuations made the drawdown much higher this time at 59%. The Global economy and Oil prices begin their slow recovery in the second half of 2009 and subsequently the KWSE also recovered some of the losses. But it would never again reach the June 2008 peak. The nature of drawdowns are such that in this case, markets needed to rise by 145% from the March 2009 lows to scale the peak of June 2008. The most the index would ever reach was 8,430 in May 2013.

2014-16 Oil price crash

Oil prices crashed again in the second half of 2014. KWSE again experienced a fall marking a drawdown of about 37%. The KWSE bottomed in Jan 2016 and after that could recover only 39% from these lows. This is primarily because oil prices never reached triple digits since the crash in spite of production cuts by OPEC+ group in 2018. Oil Prices being closely linked to the Kuwaiti economy has meant that stock market gains have been capped.

Re-organization of the Kuwaiti Stock market in 2018

Low oil prices have however increased the pace of reforms in the capital markets and the banking industry. The Kuwaiti Stock exchanges were re-organized in March 2018 and three indices were created viz. the Premier Market Index, which has the 18 most liquid stocks, the Main Market index and the All-Share index which is an index of around 140 stocks.

Banking stocks are the most widely traded stocks by value and have the highest market capitalization in all the indices. Kuwaiti banks reported good profits in 2018 and 2019 and saw their stock prices rise. The Banking Index (BKB), an index of 14 Kuwaiti banks reached a high of 1,528 in January 2020, a rise of 54% since the index was created in April 2018. However, the worldwide stock market panic as a result of the COVID-19 pandemic has seen a drawdown of 35% in the Premier Market Index and 37% in the Banking index as on March 17, 2020. The fall is expected to continue until the global panic subsides.

Conclusion

Trailing Price/Earnings (P/E) Ratios of GCC Stock market indices

GCC Country/Region	Index	Trailing P/E Ratio
GCC	S&P GCC Composite	15
Saudi Arabia	Tadawul FF Index	14
Qatar	Qatar Exchange General Index	12
Kuwait	Kuwait All-Share Index	11
Bahrain	Bahrain All Share Index	10
Abu Dhabi	ADI	9
Oman	Muscat SE General Index	7
Dubai	DFM General Index	4

Source: Refinitiv

Kuwait Stock markets are very vulnerable to local and global events and have seen severe drawdowns. And in most cases, the markets were unable to reach the previous highs. However, certain sectors with better fundamentals have done better than the index in terms of recovery from the drawdowns like the banking sector. Also, as shown in the table above, Kuwaiti stocks are better placed in terms of valuations than some of their GCC counterparts. The ability and willingness of the Kuwaiti Government and central bank to respond is also better than past crisis.

6. Circuit breakers/trading curbs in GCC Stock Exchanges

Stock markets around the world and the GCC have responded to the COVID-19 pandemic with massive volatility, as traders have been panic selling out of fear driving the indices down. The Boursa Kuwait All Share Index (BKAT) saw huge falls on March 8 and March 9 when the BKAT fell 9.1% and 9.4% respectively due to the oil price crash and coronavirus fears. Due to this, Boursa Kuwait has announced that from March 15, the security circuit breaker would be modified by reducing the lower limit from 10 percent to 5 percent while maintaining the upper limit at 10 percent. If the Kuwaiti indices fall by 5% (previously 10%), trading would be halted for 15 minutes after which trading would resume. Boursa Kuwait had introduced the original circuit breaker limits in 2018 as a part of wider reforms to the Kuwaiti capital markets. Elsewhere in the GCC, the Abu Dhabi and Dubai Stock exchanges also reduced the circuit breaker lower limit to 5%. The table below lists the circuit breaker limits currently in place in the GCC stock exchanges

Circuit Breaker limits in GCC Stock Exchanges

GCC Country	Index	Upper Limit	Lower limit
Saudi Arabia	Tadawul FF Index	10%	10%
Qatar	Qatar Exchange General Index	10%	10%
Kuwait	Kuwait All-Share Index	10%	5%
Bahrain	Bahrain All Share Index	10%	10%
Abu Dhabi	ADI	10%	5%
Oman	Muscat SE General Index	10%	10%
Dubai	DFM General Index	10%	5%

Source: Marmore Research

Black Monday of 1987 leads to the birth of circuit breakers

Now, 'Circuit breakers' or 'Trading Curbs' have been used by stock exchanges around the world since 'Black Monday' on October 1987 when the Dow Jones Industrial Average crashed by 23% in a single trading session causing huge losses to investors. In this case, the selling was accelerated due to technical reasons related to the markets like lack of uniform margin trading rules. The circuit breaker tries to prevent this situation. By halting trading for a designated time after a huge fall, traders would get more time to wait for new information, both technical and fundamental, and reconsider their trades when trading resumes. This would prevent the kind of massive falls like that of Black Monday and have since been adopted by almost every stock exchange in the world.

While the circuit breaker equally applies when the market rises too fast, it is clear that it primarily exists to prevent huge falls. And there has been criticism from some market participants that circuit breakers were created for political reasons rather than practical. They say that market sell offs leading to losses are covered widely in the media while stock market rises driven by speculation are rarely seen as a concern. This creates an environment of loss aversion and the desire is to prevent losses as much as possible. These market players argue that halting trading through circuit breakers is mainly to stop short sellers, who seek to profit when the market goes down. Short selling is generally looked down upon by investors and politicians alike because they are seen as trying to profit from a bad situation. Also, in some cases like in Saudi Arabia stock market crash of 2006, circuit breaker limits failed to reduce the volatility as the reduced limits of 5% forced traders to enter large sell orders as the limit was approaching. Once the trading resumed, the selling continued unabated as the market continued to crash. Despite this instance, the view from most is that circuit breakers are necessary to curb volatility and protect investors. Also, most GCC stock exchanges have introduced reforms to the stock markets and they are much more regulated and efficient than the Saudi Stock market in 2006.

Calls for shutting down markets entirely are misguided

Increasingly, there have been calls by some in the financial and political world that stock markets should be closed for weeks, perhaps months till the coronavirus situation stabilizes. While a short pause in trading triggered by circuit breakers are useful, a total shutdown of the markets in the GCC can cause real harm. Closing financial markets increase the risk of a total meltdown once they reopen and the coronavirus concerns persist even during the closure. By staying open and continuing trading, financial markets can send signals to the governments about the efficacy of fiscal and monetary stimulus policies. For example, global markets fell when a stimulus bill was not passed initially in the US Senate. When a package was finally passed, markets the world over rallied and the signal from the markets would likely have hastened the deal. Similarly the GCC governments and central banks have announced fiscal and monetary stimulus measures since March 9 when the GCC markets fell massively. These announcements have arrested the fall and small gains have been made in GCC stock markets too as the month draws to a close. To conclude, while modification to circuit breakers are a good step, the continued functioning of the stock exchanges is necessary for the long term benefit of GCC investors, governments and other stake holders.

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