

Equity markets

Qatar: Spending cuts and tight liquidity weigh on equities in 2016

> Sara Ghazzawi
Senior Analyst
+965 2259 5355, sarag@nbk.com

> Nembr Kanafani
Senior Economist
+965 2259 5365, nemrkanafani@nbk.com

The performance of Qatari equities was lackluster in 2016, though they have done somewhat better thus far in 2017. The Qatar Stock Exchange (QSE) was flat on the year, underperforming its GCC peers. Though Qatar remains the fastest growing regional economy with non-oil GDP growth expected to average 5.5% in the coming two years, compared to a GCC average of 2.9%, government spending cuts and tightening liquidity took their toll on sentiment and corporate results. The market ended the year in better form supported by December's OPEC deal to cut oil output and support energy prices.

Despite rallying in 3Q16, QSE was unable to lock in any gains in 2016. The general index was up a mere 0.1% on the year notably underperforming the regional MSCI GCC price index which advanced 5.1%. The Qatari market, along with other GCC markets, started the year on the wrong foot when oil prices dipped to the low 20's. All GCC markets bounced back as oil prices recovered, but the QSE was unable to maintain momentum, falling behind most of its peers.

An upgrade of the market to emerging market (EM) status by FTSE had a strong though short-lived impact. Qatari equities had a good run in the weeks leading up to the upgrade; but the rally was not sustained and QSE continued with a lackluster performance for the remainder of 2016. The upgrade, which came into effect in September, was set to lure more than \$500 million through passive funds alone; indeed, foreign inflows to QSE saw a notable pick up in the second half of 2016. According to EFG Hermes, net foreign inflows to QSE averaged \$212 million a month compared to \$81 million in 1H16.

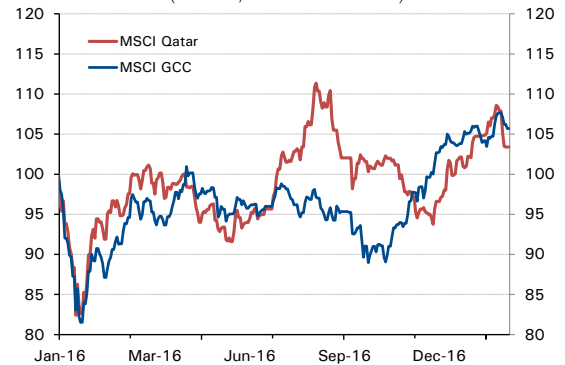
The QSE rebounded late in the year on the back of the deal by oil producers to cut oil output, and continues to do better thus far in 2017. The selling of EM assets, partly triggered by the election of Donald Trump in the US, didn't seem to have a significant effect on Qatari equities. Data showed foreign inflows mostly holding up since the election. Market capitalization stood at \$153 billion at the end of December, having added a \$1.6 billion during the year.

Sentiment in Qatar suffered due to a lack of clarity regarding cuts in government spending and declining liquidity. Despite being the fastest growing economy and having one of the strongest fiscal positions in the region, low oil prices of the past two years have taken a heavy toll on confidence and business in the country. Government spending, the lynchpin of the economy, is expected to have contracted for the second year in a row in 2016. Meanwhile, the financial sector was being pressured by declining liquidity with deposits at banks contracting 5% y/y in October 2016.

Financial companies, QSE's largest sector, felt the heat of tightening liquidity. The rising cost of funds squeezed sector margins, with some banks grappling with capital requirement issues. There are 14 banks and financial institutions listed on the Qatari exchange, out of a total of 44 companies. The sector makes up 41% of the total market capitalization.

Chart 1: Price indices

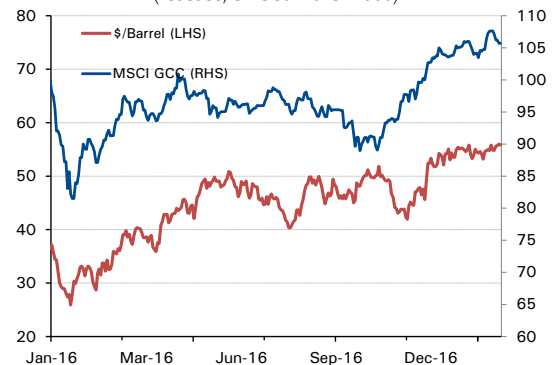
(rebased, 31 Dec 2015=100)



Source: Thomson Reuters Datastream

Chart 2: Oil prices and GCC markets

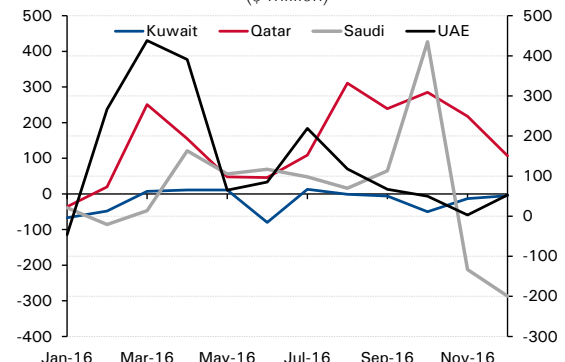
(rebased, 31 Dec 2015=1000)



Source: Thomson Reuters Datastream

Chart 3: Net foreign inflows to equities

(\$ million)



Source: EFG Hermes

Transport is the second largest sector making up 26% with the remainder distributed among five other sectors.

The low oil and gas price environment seemed to hurt Qatari corporates most. Corporate earnings for the first nine months of 2016 (9M16) continued to reflect weakness in the private sector with a sample of listed companies' profits down 11% compared to a year ago, the biggest decline among the four major GCC economies. Moreover, most 9M16 corporate announcements missed analysts' estimates, which contributed to QSE's weak performance in 4Q16. A sample of 18 companies announced profits that were on average 7% lower than forecast.

Despite their underperformance, Qatari equities remain among the most overvalued in the region. With an average P/E ratio of 14.2, QSE is the third most expensive market in the GCC. This helped the QSE become the second largest GCC stock market, having surpassed Kuwait's stock market in size in 2010. With a market capitalization to non-oil GDP ratio of 83%, the Qatari market seems overpriced compared to GCC peers.

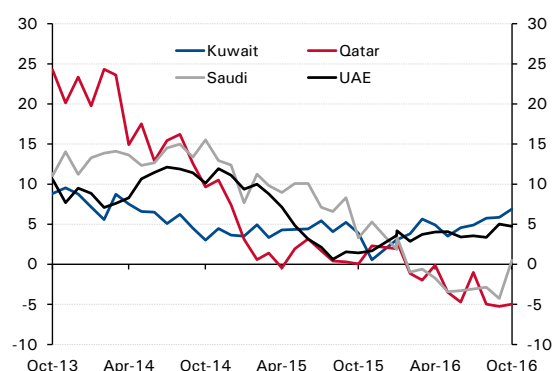
Market liquidity fell sharply as funds were directed away from equities toward bonds. The average daily turnover was \$77 million in 2016, down 27% from 2015. With banks turning to fixed-income markets to issue Basel III-compliant perpetual and other bonds, and GCC governments tapping debt markets to finance deficits, some liquidity was directed away from regional equities. However, as governments look to raise more debt internationally rather than depend on domestic borrowing, activity in equity markets has seen a pickup.

Despite a weak performance in 2016, QSE continued to lead in capital market development. According to the World Economic Forum's 2015/16 Global Competitiveness Report, Qatar ranks first in the Arab world in terms of efficiency of financial market development, availability of financial services, ease of financing through equity markets, and regulation of securities exchanges. Efforts to develop Qatar's financial and capital markets, which are part of Qatar's National vision 2030, paid off with FTSE recent upgrade and similar upgrades by MSCI and S&P in 2014.

Focus in 1Q17 will be on annual earnings announcements which have so far missed analyst estimates. Nevertheless, the market is up 1.5% year- to-date (ytd, February 3). In the medium term, investors will continue to monitor government's fiscal and reform plans for the coming years, as well as oil price developments. Internationally, with a new US administration, investor focus will be on the US, as they seek to ascertain the shift in key economic policies and their implications for capital markets globally.

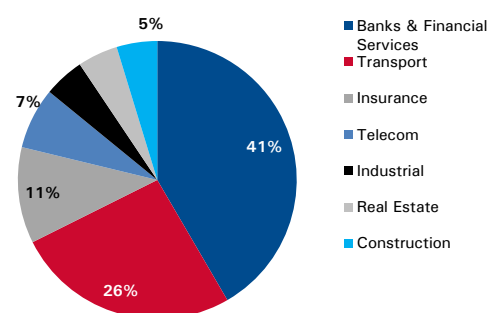
Chart 4: Deposits at banks

(% y/y)



Source: Central Banks

Chart 5: Market capitalization by sector



Source: Thomson Reuters DataStream

Table 1: GCC markets indicators

	General Index (% y/y)	Market cap (\$ bn)	Price/earnings per share	Average daily turnover (\$ mn)		Growth in profits (% y/y)
				2016	9M16	
		31-Dec-2016		2016	9M16	
Bahrain (Bourse)	0.4	19	11.2	2	-5	
Kuwait (Boursa)	2.4	84	15.8	46	-6	
Oman (MSM)	6.3	22	11.5	9	5	
Qatar (QSE)	0.1	153	14.2	77	-11	
Saudi (Tadawul)	4.7	447	17.6	1,194	-5	
Abu Dhabi (ADX)	5.6	223	12.4	237	-1	
Dubai (DFM)	12.1					
GCC		951	-	1,553	-	

Source: Thomson Reuters Datastream, Thomson Reuters Eikon

Head Office

Kuwait
National Bank of Kuwait SAKP
Abdullah Al-Ahmed Street
P.O. Box 95, Safat 13001
Kuwait City, Kuwait
Tel: +965 2242 2011
Fax: +965 2259 5804
Telex: 22043-22451 NATBANK
www.nbk.com

International Network

Bahrain
National Bank of Kuwait SAKP
Zain Branch
Zain Tower, Building 401, Road 2806
Seef Area 428, P. O. Box 5290, Manama
Kingdom of Bahrain
Tel: +973 17 155 555
Fax: +973 17 104 860

National Bank of Kuwait SAKP
Bahrain Head Office
GB Corp Tower
Block 346, Road 4626
Building 1411
P.O. Box 5290, Manama
Kingdom of Bahrain
Tel: +973 17 155 555
Fax: +973 17 104 860

United Arab Emirates
National Bank of Kuwait SAKP
Dubai Branch
Latifa Tower, Sheikh Zayed Road
Next to Crown Plaza
P.O.Box 9293, Dubai, U.A.E
Tel: +971 4 3161600
Fax: +971 4 3888588

National Bank of Kuwait SAKP
Abu Dhabi Branch
Sheikh Rashed Bin Saeed
Al Maktoom, (Old Airport Road)
P.O.Box 113567, Abu Dhabi, U.A.E
Tel: +971 2 4199 555
Fax: +971 2 2222 477

Saudi Arabia
National Bank of Kuwait SAKP
Jeddah Branch
Al Khalidiah District,
Al Mukmal Tower, Jeddah
P.O Box: 15385 Jeddah 21444
Kingdom of Saudi Arabia
Tel: +966 2 603 6300
Fax: +966 2 603 6318

Jordan
National Bank of Kuwait SAKP
Amman Branch
Shareef Abdul Hamid Sharaf St
P.O. Box 941297, Shmeisani,
Amman 11194, Jordan
Tel: +962 6 580 0400
Fax: +962 6 580 0441

Lebanon
National Bank of Kuwait
(Lebanon) SAL
BAC Building, Justinien Street, Sanayeh
P.O. Box 11-5727, Riad El-Solh
Beirut 1107 2200, Lebanon
Tel: +961 1 759700
Fax: +961 1 747866

Iraq
Credit Bank of Iraq
Street 9, Building 187
Sadoon Street, District 102
P.O. Box 3420, Baghdad, Iraq
Tel: +964 1 7182198/7191944
+964 1 7188406/7171673
Fax: +964 1 7170156

Egypt
National Bank of Kuwait - Egypt
Plot 155, City Center, First Sector
5th Settlement, New Cairo
Egypt
Tel: +20 2 26149300
Fax: +20 2 26133978

United States of America
National Bank of Kuwait SAKP
New York Branch
299 Park Avenue
New York, NY 10171
USA
Tel: +1 212 303 9800
Fax: +1 212 319 8269

United Kingdom
National Bank of Kuwait
(International) Plc
Head Office
13 George Street
London W1U 3QJ
UK
Tel: +44 20 7224 2277
Fax: +44 20 7224 2101

National Bank of Kuwait
(International) Plc
Portman Square Branch
7 Portman Square
London W1H 6NA, UK
Tel: +44 20 7224 2277
Fax: +44 20 7486 3877

France
National Bank of Kuwait
(International) Plc
Paris Branch
90 Avenue des Champs-Elysees
75008 Paris
France
Tel: +33 1 5659 8600
Fax: +33 1 5659 8623

Singapore
National Bank of Kuwait SAKP
Singapore Branch
9 Raffles Place # 44-01
Republic Plaza
Singapore 048619
Tel: +65 6222 5348
Fax: +65 6224 5438

China
National Bank of Kuwait SAKP
Shanghai Representative Office
Suite 1003, 10th Floor, Azia Center
1233 Lujiazui Ring Road
Shanghai 200120, China
Tel: +86 21 6888 1092
Fax: +86 21 5047 1011

NBK Capital

Kuwait
NBK Capital
38th Floor, Arraya II Building, Block 6
Shuhada'a street, Sharq
PO Box 4950, Safat, 13050
Kuwait
Tel: +965 2224 6900
Fax: +965 2224 6904 / 5

United Arab Emirates
NBK Capital Limited - UAE
Precinct Building 3, Office 404
Dubai International Financial Center
Sheikh Zayed Road
P.O. Box 506506, Dubai
UAE
Tel: +971 4 365 2800
Fax: +971 4 365 2805

Associates

Turkey
Turkish Bank
Valikonagl CAD. 7
Nisantasi, P.O. Box. 34371
Istanbul, Turkey
Tel: +90 212 373 6373
Fax: +90 212 225 0353