Fiscal reforms are the need of the hour in GCC

Easing measures needed to stimulate economy, create investment

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VIEWPOINT

THE US Federal Reserve raised its benchmark interest rate last month for just the second time since the financial crisis of 2008.

The Fed has also indicated three rate hikes in 2017. The UAE central bank has recently raised interest rates applied to its certificates of deposits by 25 basis points after the US Federal Reserve hiked Fed funds rate last month. Qatar's central bank said it was raising policy rates by 25 basis points. Kuwait's central bank raised its discount rate, used to determine maximum interest rates on dinar borrowing at local banks, by a quarter of a percentage point to 2.50 per cent.

Bahrain raised a range of policy rates by a quarter of a percentage point. The new rate rises mean that they will have to apply higher interest rates on consumer loans. Consumers tapping personal loans and mortgages are likely to pay more for their money as well.

Tourism-facing sectors such as hospitality and retail will also be hit as customers from countries with weaker currencies against the strong dollar become more cost-conscious. Exporters can also feel the effect of a stronger dollar.

Low oil prices have created a tighter liquidity scenario in the GCC and more easing measures are needed to stimulate the economy, create investment and reduce deflationary pressures. The SME sector, which had experienced increase in loan defaults on account of low oil prices, will further feel the strain on account of higher borrowing costs.

GCC bond market robust

In 2016, GCC bond issues were worth more than $71 billion. The GCC sukuk market was close to $13 billion and GCC conventional bonds accounted for more than $58 billion.

The major sukuk issues in 2016 were from Etihad Airways — $1.5 billion, DP World — $1.2 billion, the Investment Corporation of Dubai — $750 million, the emirate of Dubai — $569 million, and the emirate of Sharjah — $500 million.

The major GCC conventional bond issues in 2016 were from the emirate of Abu Dhabi — $5 billion, Qatar National Bank — $2.58 billion, and the Kingdom of Bahrain — $600 million.

$71b+
worth of bonds were issued in the GCC in 2016

The GCC government bond issues were from Saudi Arabia — $17.5 billion, Qatar — $9 billion, Abu Dhabi — $5 billion, Oman — $4.5 billion, Dubai — $569 million, Sharjah — $500 million, and Bahrain — $2.6 billion in 2016.

In recent times, borrowings by GCC sovereigns from the international market and slightly higher oil prices have eased the funding squeeze and, therefore, money market rates have not reacted much to the US Fed rate hike.

Debt turns costly

However, GCC governments are further preparing to raise billions of dollars in debt to plug deficits that have increased owing to falling oil prices. It means that both GCC governments and corporates will pay more to raise debt from bond markets.

Qatar has recently announced its budget of 2017 in which it has a forecasted deficit of QR28.3 billion. The shortfall is expected to be covered by issuing debt instruments in the local and international financial markets, while maintaining its reserves and investments.

The rising interest rates find the GCC in a different economic cycle than the US on account of low oil prices and their widening fiscal deficits. The region's economies will be more affected by the pace of fiscal and structural reforms than just the cost of capital. The economic slowdown facing the region increases the need for additional fiscal and structural reforms to support growth, boost productivity, stimulate private investment and create high-paying private sector jobs.

We need to see how the GCC works on these reforms. Fiscal and monetary policy need to be aligned when a scenario of low oil prices and Fed monetary tightening prevails.

The writer is Group CEO, Doha Bank. Views expressed are his own and do not reflect the newspaper's policies.