

Weekly Insights 14 Sep 2020: A Balance Act as UAE remains open amid Covid19 surge

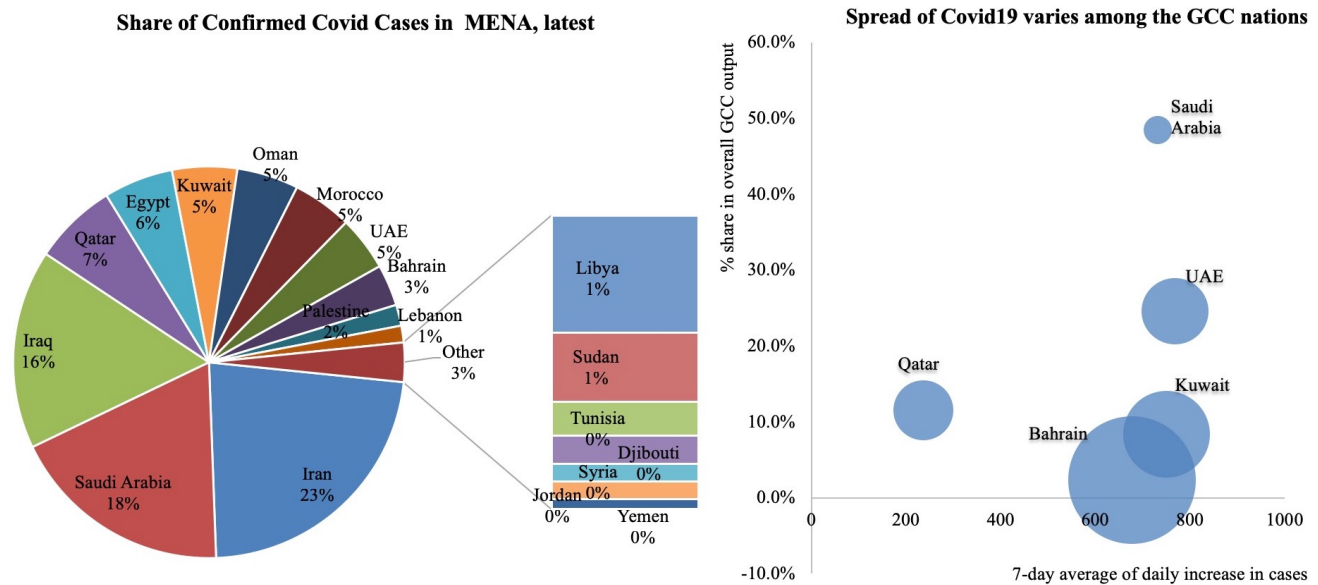
Charts of the Week: This is a crucial period for GCC, including the UAE. How can one decide on the balance between reopening the economy, supporting economic activity, while also containing the spread of Covid19? What policy measures should top the list to support businesses and consumers?

1. Spread of Covid19 in the GCC/ UAE

Confirmed Covid19 cases in the Middle East has crossed 1.75mn, with the GCC nations accounting for 43.7% of total cases. Many of these nations have seen a recent spike in cases, after stay-at-home orders and travel restrictions were lifted in addition to reopening previously constrained activities (e.g. mosques, gyms, salons). Among the GCC nations, the spread of the outbreak is still varied. The chart on the right maps the share in total daily increase in confirmed cases per million persons (x-axis) against the share of the country in overall output (y-axis), with the size of the bubble denoting the 7-day average of the daily increase in cases.

Among the GCC nations, Oman seems to be relatively better off – when it comes to both the 7-day average of daily increase in Covid19 cases as well as the daily confirmed cases per million people; not surprising considering that it is the most “stringent” among the group – the Oxford Covid-19 government response stringency index[\[1\]](#) places Oman at 86.11 vs the least stringent being UAE at 36.11 (Sep 2020). The UAE, which accounts for one-fourth of GCC’s GDP, has the highest 7-day average of daily increase in Covid19 cases (size of bubble). While officials have stressed the need for greater adherence to social distancing measures, no lockdown has been imposed as yet. Within UAE, Dubai is already welcoming tourists subject

to Covid19 negative tests.



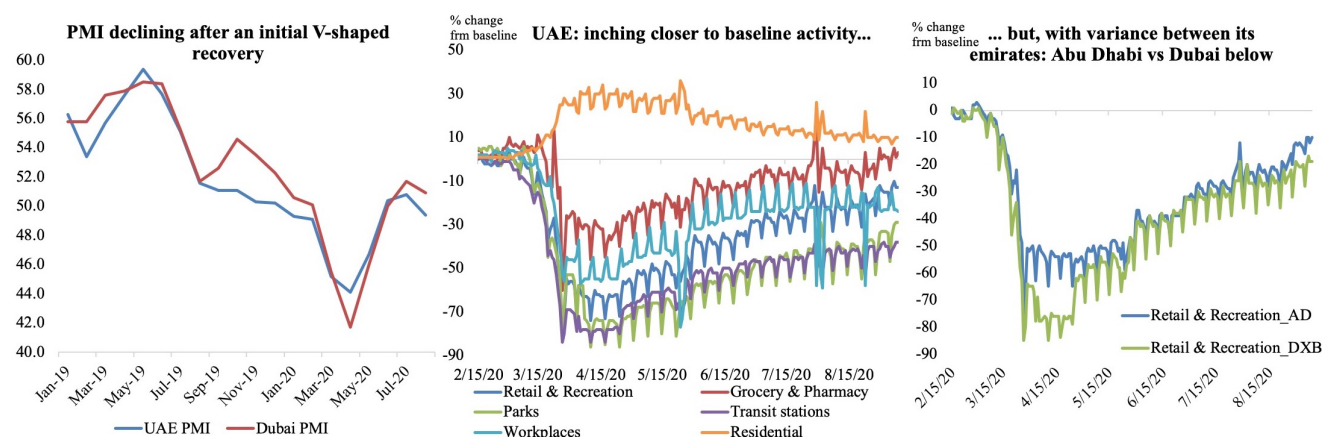
Source: Worldometers, Our World in Data, Nasser Saidi & Associates. The size of the bubbles on the RHS chart denotes the 7-day average of daily increase in cases.

This implies a sharper downturn in GDP this year due to the outbreak, while the effects of lower oil prices and the OPEC+ led cut in oil production will worsen the growth outlook. Given the large proportion of expat population in the country, a dip in growth will also spillover into the labour-importing nations: ranging from job losses (& the return of these residents to home countries), as well as lower remittances. In anticipation of lower growth this year, the government and central bank have rolled out private sector stimulus packages to support the economy, while reducing expenditures (UAE posted a record budget surplus of AED 9.75bn in Q2 this year). The Federal ministries have reduced spending (including compensation of employees), with overall cuts in capital and infrastructure spending will be detrimental to economic growth.

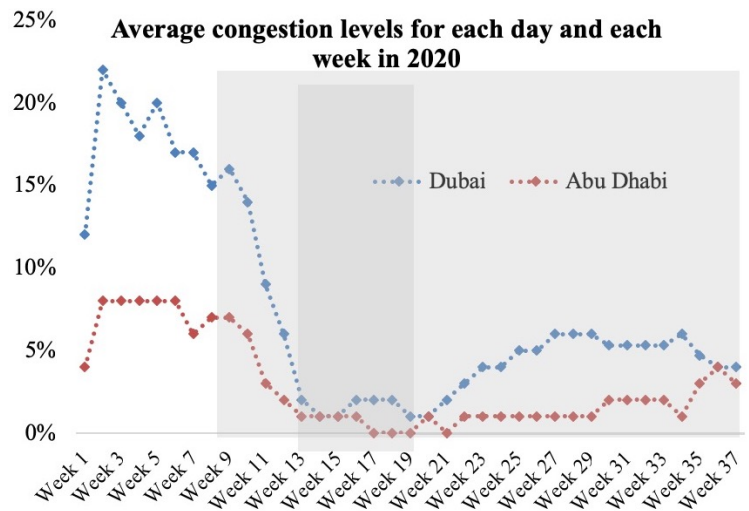
To compensate from lower oil prices and lower non-oil fiscal revenues, borrowing from international capital markets has gathered steam: so far this year, Abu Dhabi issued a USD 5bn multi-tranche bond (that included a 50-year tranche – the

longest term for a bond issued by a GCC sovereign issuer) after having raised USD 10bn previously this year, while Dubai government sold a USD 2bn dual-tranche in early-Sep (the prospectus also disclosed that the emirate had raised over USD 3.6bn in debt this year through several instruments, used to support Emirates Airlines and expenses related to the Expo). An important point to highlight is that though Dubai government debt is placed at USD 34bn, the exposure of government-related enterprises (GREs) were not disclosed – an amount estimated at more than USD 120bn by the IMF. A related point was mentioned in the [previous weekly insights](#): bank credit to the public sector and government are rising, threatening to crowd out lending to the private sector (which recorded a 0.1% yoy dip in Jun).

2. Economic Activity in the UAE: PMI, Mobility Indicators & Traffic Congestion



th UAE and Dubai (most dependent on non-oil sectors) declined the most in Apr – to 44.1 and 41.7 respectively. Following that dip, the PMI readings have been rising in both UAE and Dubai, though it came to a halt in Aug. Employment continues to be the biggest drag on the index (the sub-index was at the lowest in 11 years in the UAE while in a 6th consecutive month of contraction in Dubai) while a rise in sales and related spending was attributed to steeper price discounting (respondent firms generally pointed towards subdued customer demand, not surprising given the wider economic uncertainties).



Source: TomTom Traffic Congestion Index, Nasser Saidi & Associates. Grey areas indicate Covid19 restrictions, with the darker shaded area the severe restriction dates.

Retail and recreation readings are just under 15% lower than the baseline case in the UAE. There is however a slight difference between Dubai and Abu Dhabi with the latter having recovered faster – probably more confidence as result of specific lockdown restrictions (i.e. need to provide a negative test result to enter the emirate). Workplace is still 25% lower compared to the baseline – possibly the result of working from home policies in many firms. Congestion statistics already show a slow pickup – but below pre-Covid19 levels – more so in Dubai than Abu Dhabi.

3. Policy recommendations for the UAE

As businesses adjust, governments can provide stimulus support to facilitate transition to the new normal. **The focus in this section is businesses and consumers.** The main immediate concern for firms is operating costs and cash flow: lowering rents/ license fees or offering installment plans for payment of license fees/ rents would help ease financial burdens. Additionally, the government could offer grants to support firms' digitalization/ roll out of innovative processes. Strains on businesses could have a spillover effect on the banking sector via non-performing loans or increased flight risk of business owners unable to meet repayments. Towards this end, an extension of loan repayments deferment should be considered by the central bank (this has already been done by

other GCC nations). Banks should also be nudged to lend to the SMEs and not just already “established” firms with a better financial standing: this could take the form of working capital loans or trade loans, with a SME guarantee scheme (specifying criteria for eligible lenders and the assessment process).

As firms’ lower headcount to adjust, it would be beneficial to remove barriers to labour mobility (e.g. allowing part-time work visas/ freelancing options versus being tied to a specific company): this would allow employees (and families) to remain in the country to search for alternative jobs (and continue school, visit malls and use hospitals among others thereby contributing to overall consumer spending). Ensuring that sudden job losses will not require a move back to their native country, will increase confidence to invest in the economy (be it real estate or starting new business ventures). A longer-term policy would be to establish social security nets and/or unemployment insurance to reduce financial burdens alongside jobs support schemes.

[\[1\]](https://ourworldindata.org/grapher/covid-stringency-index?year=latest&time=2020-01-22..latest) *Check*
<https://ourworldindata.org/grapher/covid-stringency-index?year=latest&time=2020-01-22..latest>

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Weekly Insights 7 Sep 2020:

Businesses, Credit & Economic Activity in UAE & KSA

Charts of the Week: As manufacturing PMIs touch new highs in Aug, services PMI stalls. Regional activity is at odds with global peers. Are consumers/ businesses feeling the pinch of Saudi Arabia's VAT hike? Why is the credit disbursement pattern different in the UAE?

1. Manufacturing PMIs: Global vs. Regional

Manufacturing PMI numbers for August signal a tentative recovery compared to the massive dip in the Covid19 lockdown period. Global manufacturing PMI reached its highest in 21 months (51.8 from Jul's 50.6), as output and new orders rose at the fastest rates since Apr and Jun respectively, while export demand stabilised. The headline manufacturing indices in the US and Europe improved as restrictions were lifted and more production came online. However, a key point to note is that in many cases export demand has not recovered as much as domestic demand (post lockdown). Meanwhile, services sector activity has almost stalled: the initial rebound is tapering off given ongoing social restriction policies. The bottom line is that though PMIs have shown some improvement, the impact might be hampered by rising unemployment, subdued international demand alongside overall economic and public health uncertainty.

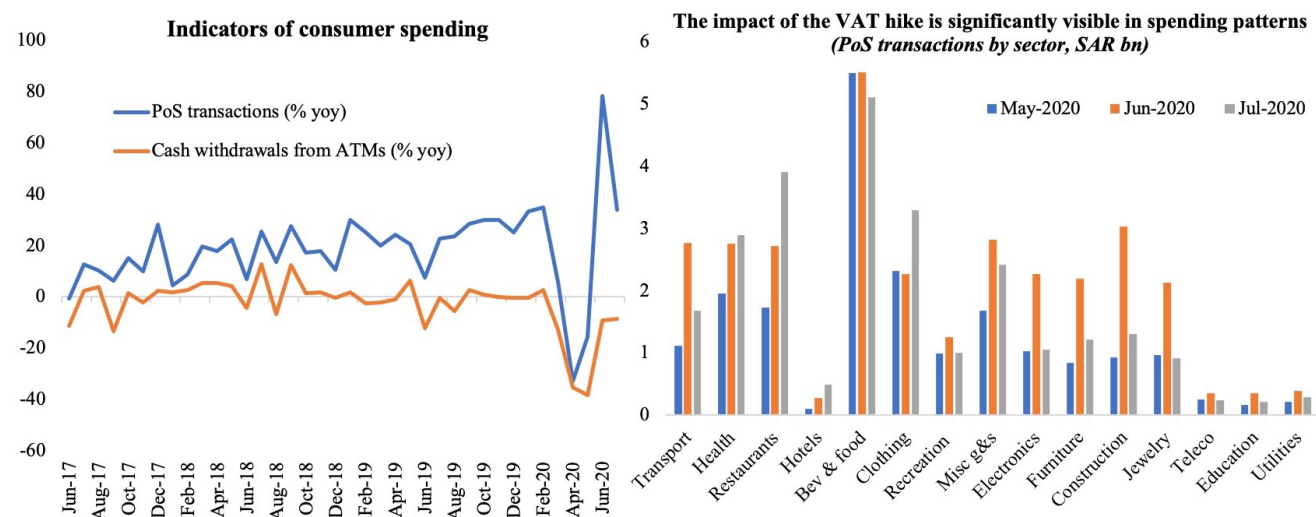
Heatmap of Manufacturing/ Non-oil sector PMIs

	US	Germany	EU	UK	Japan	China	India	UAE	Saudi Arabia	Egypt	Lebanon
Jan-19	54.9	49.7	50.6	52.8	50.3	48.3	53.9	56.3	56.2	48.5	46.5
Feb-19	53.0	47.6	49.5	52.1	48.9	49.9	54.3	53.4	56.6	48.2	46.9
Mar-19	52.4	44.1	48.3	55.1	49.2	50.8	52.6	55.7	56.8	49.9	46.3
Apr-19	52.6	44.4	48.4	53.1	50.2	50.2	51.8	57.6	56.8	50.8	46.7
May-19	50.5	44.3	47.9	49.4	49.8	50.2	52.7	59.4	57.3	48.2	46.3
Jun-19	50.6	45.0	47.6	48.0	49.3	49.4	52.1	57.7	57.4	49.2	46.3
Jul-19	50.4	43.2	46.6	48.0	49.4	49.9	52.5	55.1	56.6	50.3	47.7
Aug-19	50.3	43.5	47.1	47.4	49.3	50.4	51.4	51.6	57.0	49.4	47.8
Sep-19	51.1	41.7	46.0	48.3	48.9	51.4	51.4	51.1	57.3	49.5	46.4
Oct-19	51.3	42.1	46.2	49.6	48.4	51.7	50.6	51.1	57.8	49.2	48.3
Nov-19	52.6	44.1	47.0	48.9	48.9	51.8	51.2	50.3	58.3	47.9	37.0
Dec-19	52.4	43.7	46.4	47.5	48.4	51.5	52.7	50.2	56.9	48.2	45.1
Jan-20	51.9	45.3	48.1	50.0	48.8	51.1	55.3	49.3	54.9	46.0	44.9
Feb-20	50.7	48.0	49.1	51.7	47.8	40.3	54.5	49.1	52.5	47.1	45.4
Mar-20	48.5	45.4	44.3	47.8	44.8	50.1	51.8	45.2	42.4	44.2	35.0
Apr-20	36.1	34.5	33.4	32.6	41.9	49.4	27.4	44.1	44.4	29.7	30.9
May-20	39.8	36.6	39.5	40.7	38.4	50.7	30.8	46.7	48.1	40.0	37.2
Jun-20	49.8	45.2	47.4	50.1	40.1	51.2	47.2	50.4	47.7	44.6	43.2
Jul-20	50.9	51.0	51.7	53.3	45.2	52.8	46.0	50.8	50.0	49.6	44.9
Aug-20	53.1	52.2	51.6	55.2	47.2	53.1	52.0	49.4	48.8	49.4	NA

Source: Refinitiv Datastream, Nasser Saidi & Associates

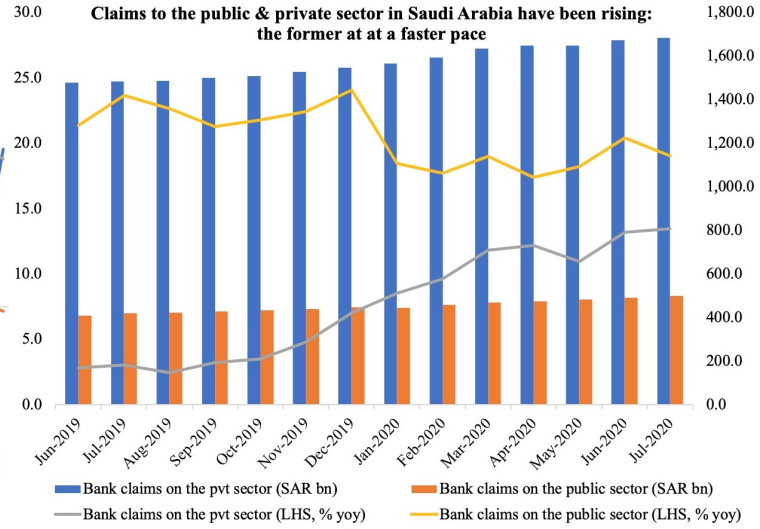
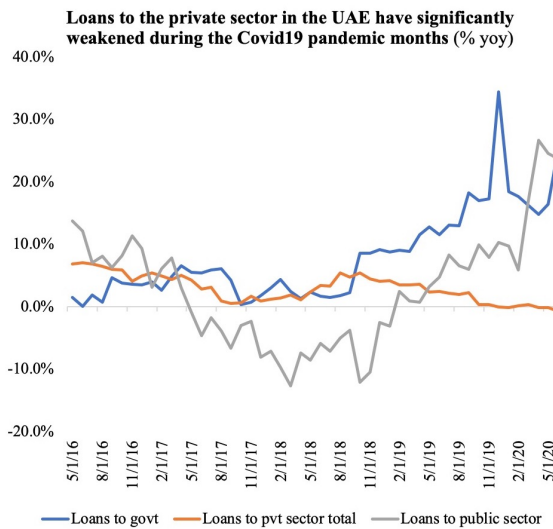
From the list above, only Japan and countries from the Middle East are sub-50 indicating a contraction. Egypt posted the 13th straight month of contraction in Aug, while both Saudi Arabia and UAE moved below 50. The relevant question for the region is why? A sharp decline in jobs is the main drag on headline indices, as firms try to lower operational costs amid a scenario of weak demand and subdued growth prospects. In the UAE, not only did the employment sub-index fall to its lowest in 11 years (with one in 5 panelists reducing number of employees) but firms also had to deal with price discounting to remain competitive. In Saudi Arabia, the hike in VAT (from Jul) drove up input costs, adding more pressure on firms. Overall, a prolonged weaker recovery could lead to firm closures, that would lead to job losses, bankruptcies as well as an impact on the banking sector via an increase in NPLs.

2. Saudi Arabia impacted by the VAT hike: how has consumer spending fared?



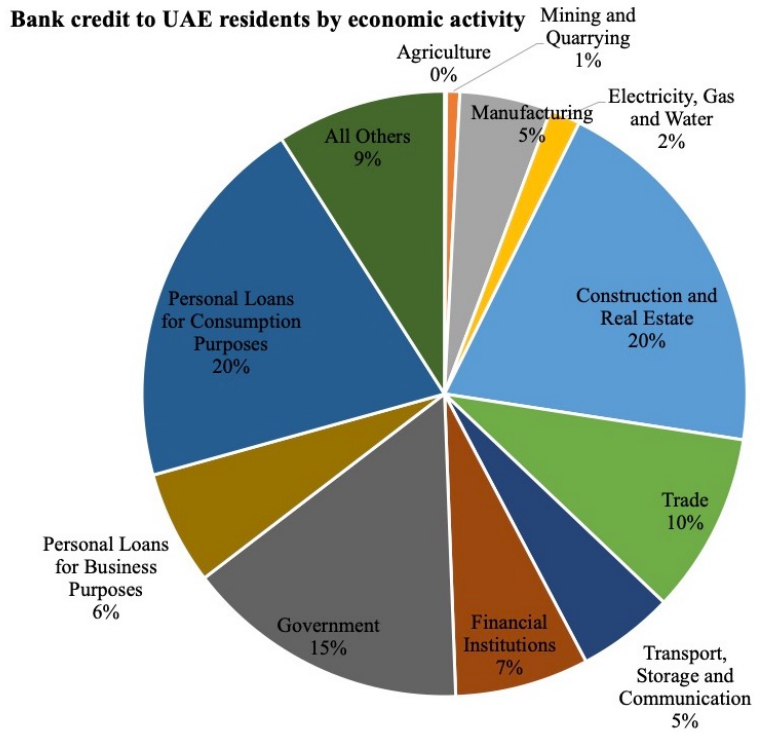
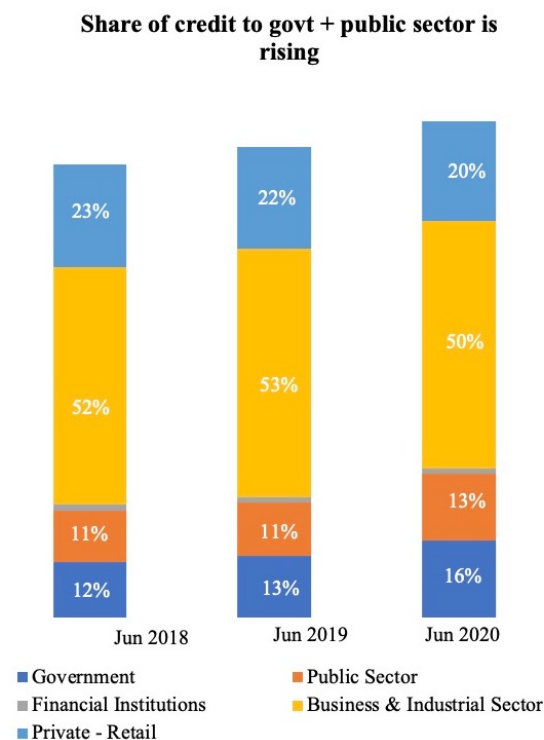
Saudi Arabia's VAT hike has negatively affected consumers as well as businesses. Consumers, who ratcheted up spending in June (similar to patterns in Dec 2017, prior to the introduction of VAT in Jan 2018), have reverted to "normal" spending habits come July. Comparing the patterns by sector, the difference in Jul is striking in purchases of big-ticket items – electronics, furniture, jewelry as well as construction and building materials. Interestingly, sectors like hotels, restaurants and clothing showed an uptick in spending in spite of the VAT hike – a probable explanation is end of lockdown and the Eid-al-Adha holidays which fell towards end of the month; new clothes are a must and restrictions on international travel resulted in people opting for more regional travel and staycations, thereby boosting payments at hotels and restaurants.

3. Is private sector activity supported by credit disbursement? A tale of two nations



di and UAE central banks have undertaken multiple measures to support their economies through this Covid19 phase: this includes increased liquidity, deferral of loan payments (which was recently extended further till Dec 2020 by SAMA) as well as support for the private sector (specifically those businesses most affected by the pandemic, and SMEs) from banks. However, while credit to the private sector has picked up in Saudi Arabia, the opposite was the case in the UAE. Why?

4. The big picture of credit activity in the UAE



Source: UAE central bank (latest available data, Jun 2020), Nasser Saidi & Associates

on, lending to the private sector in the UAE has been on the decline since Aug 2018 and worsened during the pandemic phase (Fig 3). In both year-on-year and month-on-month terms, growth in credit to the public sector and government constantly outpaced the private sector, leading to a growing share of the public sector and government. UAE banks lent most to the business sector (50% of total, as of Jun 2020 vs. 53% in Jun 2019), while the public sector & government together account for close to 30% of all loans (vs. 24% a year ago). Lending remains quite high for construction/ real estate (20%), government (15%) and personal loans (20%); this compares to 21.8%, 12.9% and 21.2% respectively a year ago.

The UAE central bank has been proactive in releasing liquidity to the financial sector during Covid: in addition to the Targeted Economic Support Scheme (Tess) rolled out in Mar, in early-Aug it temporarily relaxed the net stable funding ratio (NSFR) and the advances-to-stable resources ratio (ASRR) by 10 percentage points to enhance banks' capacity to support customers. As of July 18, banks had withdrawn AED 43.6bn, equivalent to 87.2%, of the AED 50bn Tess programme made available to them. The central bank also disclosed that, as of Jul 2020, 260k individuals and 9527 SMEs had availed the interest-free loans under Tess; credit to SMEs accounted for 9.3% of total amount disbursed to the private sector and individuals had received support worth AED 3.2bn from banks. This is but a drop in the ocean compared to the overall amount made available to the banks (i.e. AED 50bn Tess, part of the wider AED 100bn stimulus unveiled in Mar, and a further easing of buffers raising stimulus size to AED 256bn).

In this context, the questions to be answered are two-fold: 1. Are customers not seeking loans during these troubled times? Or 2. Are banks unwilling to lend during these troubled times? The answer is not crystal-clear, but more likely a combination of both (as evidenced below).

According to the latest "Credit Sentiment Survey" by the UAE

central bank, about 53% of respondents stated that the demand for both business and personal loans in Q2 had declined either substantially or moderately. In the backdrop of Covid19, and heightened economic uncertainty, it is likely that consumers do not want to take on loans they cannot service or repay in case of job loss or firm closures; the same applies for businesses in sectors that are tourism-specific or aviation/travel-related firms or others affected by the pandemic (insolvencies/ bankruptcies). On the other hand, for banks, knowingly lending to such firms/ customers could result in an increase in NPLs that would affect their profit margins and bottom line: going by the H1 earnings of the 4 largest listed banks in the UAE, combined net profits are down by 36% yoy while provisions have increased (ENBD by 243% yoy). So, banks have tightened credit standards instead, hence lowering pace of lending to the private sector. Both demand side and supply side of credit are impacting credit.

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