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Featured Interview

Interview with President of the Gulf Bond and Sukuk Association (GBSA)

Marmore held an exclusive interview with Mr. Michael P. Grifferty, President of the Gulf Bond and Sukuk Association (GBSA) and gained insights about conventional and Islamic bonds (Sukuk) in the Gulf region.

Please read below the complete transcript of the interview.

Could you please provide a brief introduction about your organization and its purpose?

GBSA is the member organization that speaks for the Gulf bond and Sukuk industry, advocates its positions and strengthens the region's voice in the global arena. We set practices and work with governments, regulators, central banks and corporates to grow the market. GBSA members are the market leaders.

Though our focus is the Gulf, we are increasingly involved and adding value in places like Turkey and Egypt. We also work closely with the international financial institutions like EBRD, World Bank, IMF and Arab Monetary Fund.

GBSA members participate in committees and working groups addressing all major matters of the bonds business. Through these activities, a networked business community has evolved that our members find extremely valuable to be part of.

At the end of last year, outstanding bonds and Sukuk issued by GCC entities reached USD 257billion, up 16.4% from a year ago, driven primarily by strong private sector activity. What is your outlook for 2014?

I think that we will see another increase, but I don't worry much about those figures. There are other indicators that show a maturing market, like diversity of issuers and extension of tenors. Only a few years ago, government and government related issues were the main story line.

Now they are ceding their place to a range of lower rated and more interesting private sector credits. This trend should continue, especially as the GCC is somewhat insulated from negative emerging market sentiment.

> "Saudi Arabia should continue to supply new issuance in 2014"

What are the regional markets for fixed income that would be in focus for 2014?

Saudi Arabia should continue to supply new issuance. There are a host of solid cash-generating companies that are looking beyond bank financing and whose Sukuk would be well received. We know a number of companies are seriously considering coming in for the first time. These wouldn't be of international benchmark size like government-related entities can issue but significant nonetheless.

According to media sources, GCC investors prefer medium to long-term investments. With the recovery in developed markets, do you forecast any change in this preference? What would be your outlook for the next couple of years?

Gulf investors are beginning to get comfortable with longer tenors, but we don't yet have that solid long-term investor base of insurers and pension funds that need to fund their own long-term liabilities with bonds. Updated regulation of insurance and pensions all across the region would make a big difference.

What do you think are the emerging trends in the GCC sovereign and corporate debt markets and what are the key challenges faced?

I think that domestic currency government markets will finally come to the fore. We have been working on these with the authorities over a number of years, and there are signs that this will start to pay off. Sovereigns may from time to time freshen up their dollar benchmark bonds to support financing of major projects, but I don't see a lot of straight sovereign dollar bonds in the future. On the corporate side, we will continue to see new names as privately owned businesses dip their toes into the capital market waters.

Qatar launched a USD 3billion issue of 3- and 5-year Sukuks in January of this year, along with an issue of USD 3.6billion in conventional investments. While this seems a strong start for the year, the Islamic debt market declined by around 12 per cent in 2013 to USD 120billion. What is your forecast for 2014? And what are the challenges faced by the Islamic Debt Market?

We applaud the Qatar authorities for supplying the local market with medium term conventional and Islamic instruments. They are a leader in this respect. For our part, we are working with them on market practice and infrastructure so that future, larger issuances will be well-received and form the basis for a liquid local market. I won't repeat what you hear everywhere about the need for standardization. The main challenge for the region's Sukuk market is to grow the overall debt capital market, of which Sukuk is a prominent part.

Do you see the regional debt markets improving in terms of market size, primary and secondary market trading activities?

Yes, there are factors like Basel III, infrastructure spend, and in some countries, budgetary pressures, that will drive issuance, but remember growing the primary market size is relatively easy. The secondary markets need more work in terms of infrastructure, practices and transparency.

Despite low correlation with US treasuries, are the recent cuts to quantitative easing and possible increase in interest rates expected to have an impact in the GCC debt markets?

The GCC is part of the emerging markets universe and is not immune from global interest rate trends and credit spreads. Having said that, Gulf national balance sheets are very strong and investors distinguish between these credits and those of the so-called "Fragile Five" or even longer lists of at-risk countries. The impact on the Gulf would be selective.

With a host of infrastructure spending and growth in non-oil GDP in the GCC, how the corporate bond and Sukuk markets are expected to fare in 2014? And which are the sectors that are expected to pick up this year?

Infrastructure spend will definitely support market growth and we think the best way forward is to ensure the private sector has a role in providing infrastructure. Project finance will be important and a part of that we hope will be via project bonds. As far as sectors to watch in 2014, you might see parts of the economy not yet represented in the market. Last year, private education became an issuer. I think we should keep an eye on health care.

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For a GCC based entity, what are the key regulatory requirements to investing in the debt market? In the recent years, what are the major legislative steps taken by the authorities to regulate the GCC debt markets?

The obstacles to investing the debt market come not so much from local regulation, but rather from lack of access to issues from the region. Most issuance is in USD and on the international markets, so GCC investors compete with big European and Asian accounts for access to issues from the Gulf. There is still too much buy and hold in the market, so if you don't get in at the initial distribution, especially for Sukuk, you might have to buy later, but at a significant premium. The local authorities are largely not involved in that market. The national regulators in virtually all of the GCC states have announced that bonds and Sukuk are a priority, but have advanced at different paces.

The debt markets across the region are expanding. Do you believe that the present regulatory regimes in the GCC are equipped to handle this growth? What changes would you suggest to further improve the markets?

I think even the regulators would agree that the current regulatory regimes are not yet where they need to be to handle the growth and give the local markets a role. We are working with a number of them to implement international standards at the local level so these markets can take part. Legislation could be improved to facilitate issuance. The process to have an issue approved can be long and uncertain and the disclosure required may be more appropriate to equities. In several GCC states companies cannot issue beyond the level of their paid-in-capital. This requirement is from a past time and should be removed or at least amended, as Kuwait has done. Another big step forward would be to modernize the risk and investment parameters for insurance companies who are still disproportionately exposed to real estate and equities.