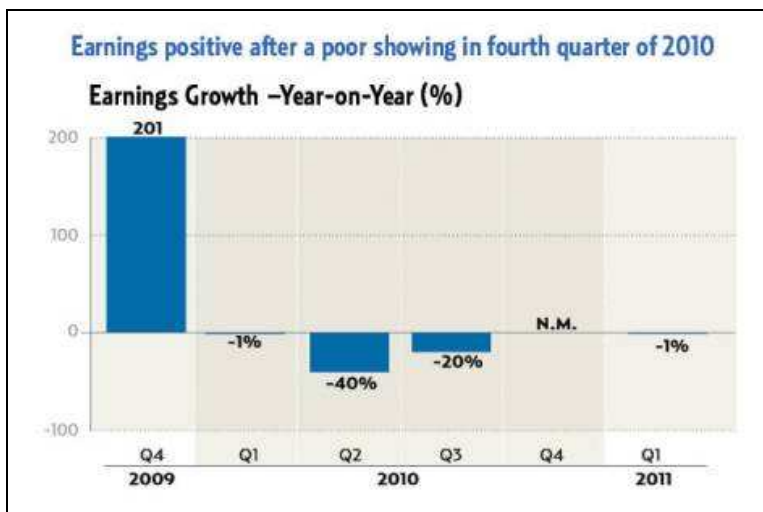


# GCC balance sheets return to growth

As the age of austerity dawns, there are still reasons for shareholders to remain uncertain

Dubai: As the dust settles on the year's first flurry of corporate earnings, company executives and investors are breathing a little easier with balance sheets across the GCC largely showing a return to growth, according to a report from the Kuwait Financial Centre, also known as "Markaz"



- Real estate recovered from 2010 losses to register profits of \$223 million for the quarter. Real estate earnings grew 44% year-on-year, led by recovery in Aldar Properties' earnings.

UAE corporate profits were almost flat year-on-year but increased to \$2.8 billion, against a loss of \$1.7 billion in fourth quarter of 2010.

The first three months of 2011 posed Gulf-based companies numerous difficulties as business dealings took place amid a backdrop of sweeping political unrest across the Arab world and a battered economy still recovering from the effects of one of the worst economic crises in living memory.

There was no shortage of local and international news catalysts to swing global equity markets as rising commodity prices, including gold, silver and crude oil, an earthquake in Japan and the killing of Al Qaida leader Osama Bin Laden in Pakistan all played a key role in shaping a particularly volatile business climate.

However, despite the numerous micro and macro economic issues, GCC corporations came through the first three months relatively unscathed with most members of the six-nation bloc posting strong earnings growth, according to the Markaz report.

Total earnings for GCC corporations came in at \$13.8 billion (Dh50.6 billion); a growth rate of 19 per cent and more than double the profits posted during the previous quarter, the report said, citing the region's continued dominance as a petrochemical hub along with a spike in commodity prices as auguring well for companies across the region.

It was a mixed picture in the UAE where corporate profits were almost flat year-on-year but increased to \$2.8 billion against a loss of \$1.7 billion quarter-on-quarter.

### **Quiet summer**

A flat year-on-year growth rate, however, is a little disconcerting for UAE companies with the traditionally quiet summer period on the horizon.

The second quarter, incorporating April, June and July, has proved to be a particularly challenging period in the past; none more so than last year when almost every sector in the UAE reported year-on-year second quarter declines amid concerns over exposure to Dubai World.

The troubled state-owned conglomerate signed a final deal with creditors in March to restructure \$24.9 billion of debt and analysts are hopeful of better second quarter numbers with the economy continuing to show signs of improvement.

"We expect second quarter earnings growth to be in-line with first quarter numbers. The banking sector will continue to maintain the growth momentum whereas real estate and construction companies may see a marginal increase in profits. The telecoms sector, with no near term catalyst, will dampen earnings," said Mandagolathur Raghu, senior vice-president for research at Markaz.

"Banks and real estate developers led the recovery in the UAE. The banking sector is expected to do [particularly] well because of the availability of low cost funds and renewed demand from government spending."

"The real estate sector recovered from losses in the past few quarters to report \$223 million in quarterly profits. However, telecoms dragged the earnings, declining six per cent year-on-year and 27 per cent quarter on quarter," Raghu added.

The UAE's banking sector may have led the short-term recovery but earnings flatlined year-on-year with most lenders missing analysts' estimates on key performance indicators such as profits, provisions and loan growth.

Emirates NBD, the UAE's biggest bank by assets, reported a 27 per cent increase in its year-on-year first quarter profits, helped by gains from the sale of a 49 per cent stake in Network International, its credit card processing unit. National Bank of Abu Dhabi (NBAD), the UAE's second-biggest bank by assets, reported a net profit of Dh927 million in first quarter, down 10 per cent from the corresponding quarter in 2010.

### **Muted volume growth**

"I would expect profitability ratios to remain in line with these figures. Sector net assets were up by 10.6 per cent year-on-year, while net loans were up just 2.6 per cent year-on-year at the end of March. Volume growth is thus rather muted," Gokkent said.

"Deposit rates have come down as liquidity has improved in the banking system but loan rates are also declining as the macro environment improves. This combination suggests that profitability will largely be affected by an expected gradual easing in the additional provisions taken on by banks," he added.

The Markaz report also said the real estate sector helped the UAE to post quarter-on-quarter growth with Aldar Real Estate leading the way.

The company, which also said it would sell a Dh2.8 billion bond to the government-owned Mubadala Development Company, made a first quarter net profit of Dh189.1 million, against a loss of Dh314.2 million in first quarter of 2010.

Emaar Properties, the builder of the Burj Khalifa, the world's tallest building, reported a 45 per cent drop in year-on-year net profit, including an 81 per cent drop in revenue from apartment sales.

### **Stronger conditions**

"General economic conditions in the UAE were stronger in the first quarter of the year than in the corresponding period in 2010, which is obviously positive news for the real estate market," said Craig Plumb, Head of Research at Jones Lang LaSalle, Middle East and North Africa.

"The property sector, however, tends to lag behind other areas of the economy and real estate companies will see the benefits of improved economic conditions later than other sectors. "The issue of supply is also a key factor. Dubai has passed the peak of its construction cycle and going forward over the next few years we will see less supply than in 2010. On the other hand, supply in Abu Dhabi is still going up as that market is yet to soften," Plumb added.

Emaar is striving to diversify its assets and the company's business subsidiaries helped it achieve a gross profit of more than Dh1 billion in the first quarter.

"The hotel and retail market performed stronger in the first quarter than the residential and office market. For example, Emaar reported a strong performance from its leisure and hospitality subsidiaries, which is reflective of the overall market trend," Plumb said.

The telecoms sector was a drag on earnings, according to Markaz, declining six per cent on a year-on-year basis and 27 per cent quarter-on-quarter. However, a closer look at the figures show a massive contrast in the fortunes of the UAE's two telcos.

It was a particularly strong quarter for du, which more than doubled its first quarter year-on-year net profit to Dh412 million before royalty fees. The company also said it added 272,000 mobile subscribers in the first three months of the year. On the other hand, etisalat, the UAE's largest telco, lost 334,000 subscribers and reported an 8.5 per cent drop in net profits.

### **Window of opportunity**

"Etisalat continues to focus more on expanding its international operations, which has given du a window of opportunity to strengthen its presence in the UAE," said Bhanu Chaddha, a senior telecommunications research analyst at IDC Middle East, Africa and Turkey.

"Du has been impressive with its performance, gaining approximately 40 per cent mobile market share in about four years' time. Going forward, etisalat will focus more on safeguarding its domestic market position as the UAE accounts for the majority of etisalat's group revenues," he added.

Both telcos are spending millions to upgrade their existing 3G networks with a view to also adopting 4G broadband services by the end of the year. Etisalat and du are also in talks with the industry regulator, the Telecommunications Regulatory Authority, with a view to introducing a number portability service, which would allow subscribers to switch between the operators providing they retain their existing number.

Moving into second quarter, each sector faces its own distinct challenges but the second quarter backdrop also features several developing issues that could affect companies across the board. Continuing demonstrations in Syria and Yemen, Europe's deepening

sovereign debt crisis and micro-economic issues within the GCC will all play a pivotal role in shaping the next batch of corporate earnings.

As the age of austerity dawns over Europe and the US, there are still many reasons for shareholders in the Gulf to remain uncertain about what could happen in the months ahead.

### **Corporate EARNINGS**

- **KUWAIT:** The highest first-quarter growth was recorded in Kuwait, which saw a sharp rebound in earnings following a sluggish performance in the previous quarter. Kuwaiti firms posted earnings worth \$2.1 billion (Dh7.7 billion), a near doubling on the same period in 2010.
- **SAUDI ARABIA** - Earnings of Saudi Arabian companies totalled \$5.8 billion, an increase of 23 per cent year-on-year and nine per cent quarter-on-quarter. Saudi Basic Industries Corporation, which reported \$2 billion in first-quarter profits, led the growth.
- **QATAR** - Qatar maintained its earnings volume with \$2.4 billion in corporate profits, a growth of 13 per cent year-on-year. The growth was led by commodities and banks with Industries Qatar reporting a net income of \$575 million and Qatar National Bank's earnings rising 35 per cent year-on-year.
- **OMAN** - Oman's first-quarter corporate earnings declined 26 per cent year-on-year and 34 per cent quarter-on-quarter as political turmoil rattled the Sultanate. The banking sector's earnings were stable at \$147 million but Oman Telecom was a drag with profits down 20 per cent year-on-year.
- **UAE** - The UAE posted strong quarter-on-quarter growth, posting earnings of \$2.8 billion against a loss of \$1.7 billion in fourth-quarter 2010. However, earnings were flat year-on-year. Abu Dhabi Commercial Bank and Emirates NBD led the growth while the real estate sector was boosted by Aldar's return to profit.
- **BAHRAIN** - Bahrain's corporates came back from the red to register \$315 million of profits despite major political upheaval in the kingdom. On a like-for-like basis, bank earnings more than tripled over the previous quarter with Ahli United Bank jumping 18 per cent to \$77 million.

*Source - Kuwait Financial Centre Markaz*