



# GCC Banking Sector Outlook 2025: Profitability And Asset Quality Boost Resilience

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**S&P Global**  
Ratings

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*This report does not constitute a rating action*

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# Key Takeaways

- Banks in the Gulf Cooperation Council (GCC) region are doing well. They are profitable, benefit from strong asset quality indicators and strong capitalization, and have sufficient liquidity on their balance sheets. We expect this performance will continue in 2025, even though it will likely be modestly affected by lower interest rates.
- However, an unanticipated, severe increase in geopolitical risk or a major decline in oil prices could weigh on banks' creditworthiness. Depending on how the scenario unfolds, we expect banks will be relatively resilient.
- This explains our currently high ratings on GCC banks and the positive outlook bias.

# Emerging Markets Overview | Geopolitics And Interest Rates

High geopolitical risk and interest rate cuts dominate the narratives for emerging markets (EMs)



## Geopolitical tensions can erode credit fundamentals

While we do not expect a full-scale regional war in the Middle East, a significant escalation could derail the macroeconomic environment in the region. The key transmission channels that we are keeping an eye on are energy prices, supply chain disruptions, financial market volatility, external and local capital outflows, and the resumption of inflationary pressures.



## Expected interest rate cuts by the Fed support EMs' financing conditions

While lower interest rates could benefit systems that depend on external funding, banks' bottom lines could be impaired by lower revenues if the cost of funding or the cost of risk do not decline.

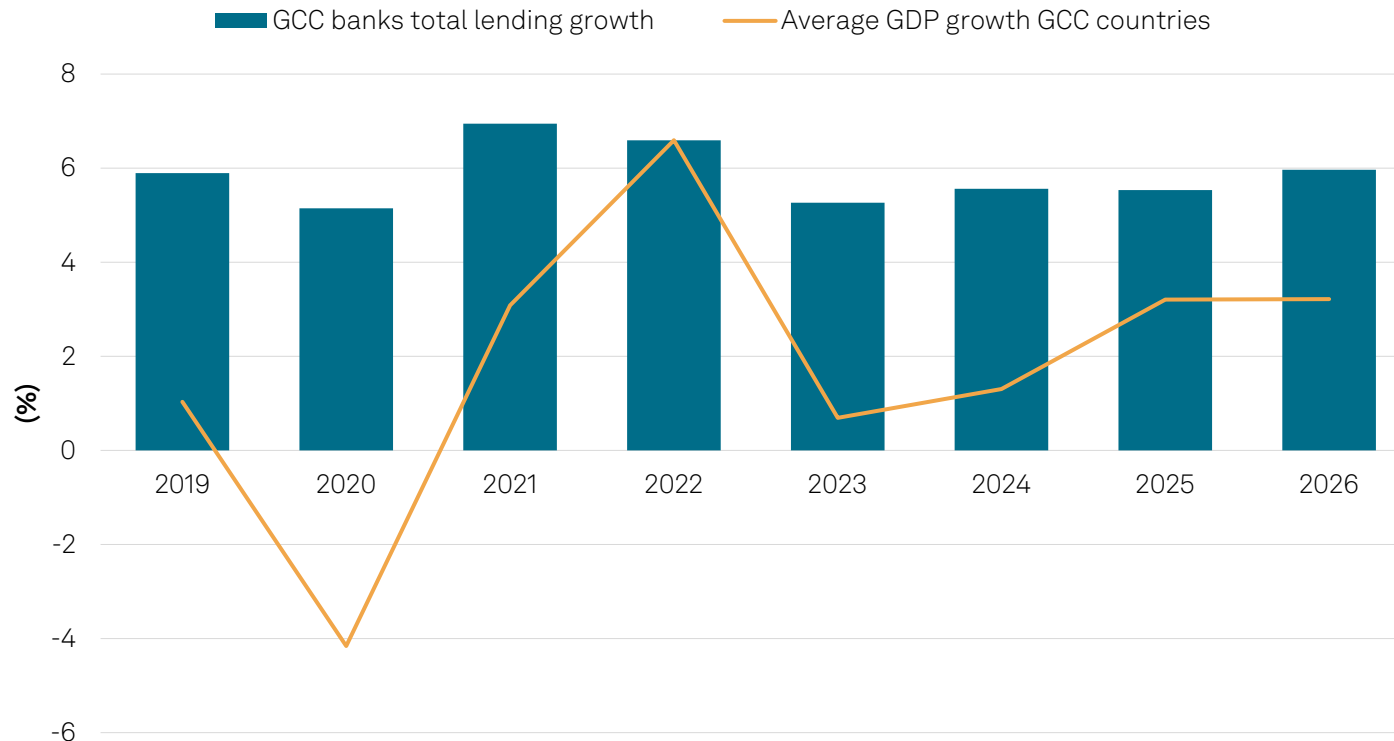


## There are a few bright spots

A few EMs are relatively better placed, particularly India and GCC countries, where profitability and asset quality indicators remain healthy. That said, an unexpected increase in geopolitical risk could weaken GCC banks.

# GCC Economies | Hydrocarbons And Transformation Plans

## Steady economic performance and continued lending growth

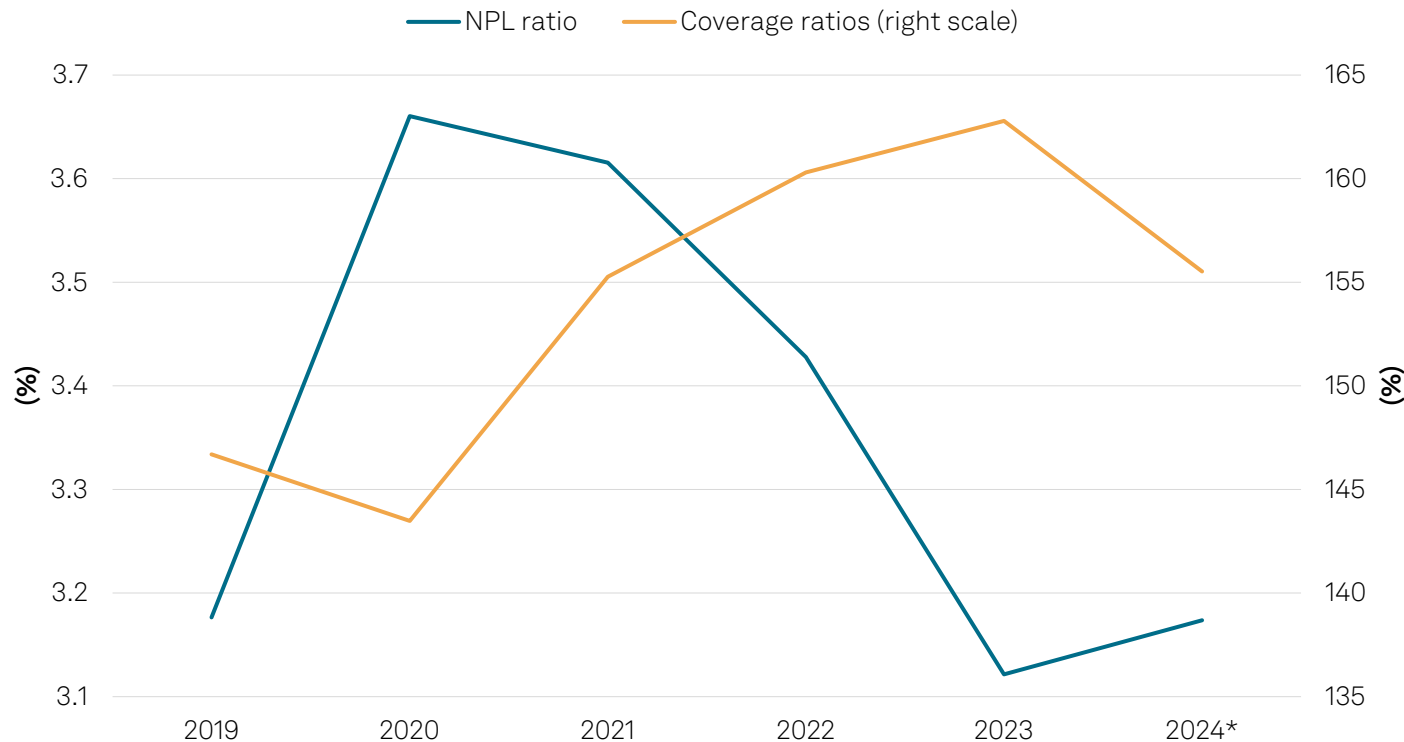


Source: S&P Global Ratings.

- We expect the Brent oil price will average \$75 per barrel in fourth-quarter 2024 and over 2025-2027, which will be helpful for most GCC countries.
- In our view, GCC countries will also benefit from the implementation of economic transformation projects (Saudi Arabia), the expansion of gas production (Qatar), reform implementations (Bahrain and Oman), and the non-oil economy's good performance (Bahrain and the UAE).
- Within this context, we think GCC banks will continue to grow their lending books without generating major macroeconomic imbalances. Lending will range from a high 8%-9% in Saudi Arabia and the UAE to a modest 3%-6% in other GCC countries.

# Asset Quality | Low NPLs And Good Coverage

Top 45 banks' asset quality indicators



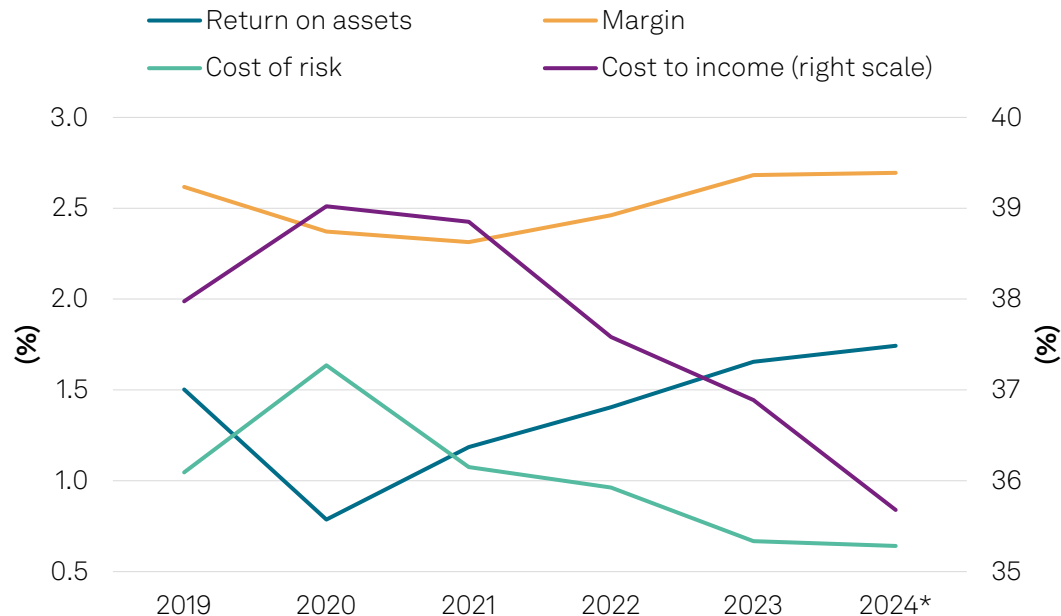
\*June 30. Source: S&P Global Ratings.

- Despite the previous shock from the COVID-19 pandemic, the nonperforming loan (NPL) ratio remained at 3%-4% since it benefited from regulatory forbearance measures and the subsequent economic improvement. The write-offs of legacy NPLs also helped.
- At the same time, banks used the strong post-pandemic profitability to continue to set aside additional provisions, which created a cushion for any potential future shocks.
- We expect asset quality indicators will remain broadly stable over the next 12-24 months. Pressures remain in markets such as Qatar, where the real estate sector continues to suffer from oversupply after the World Cup in 2022.

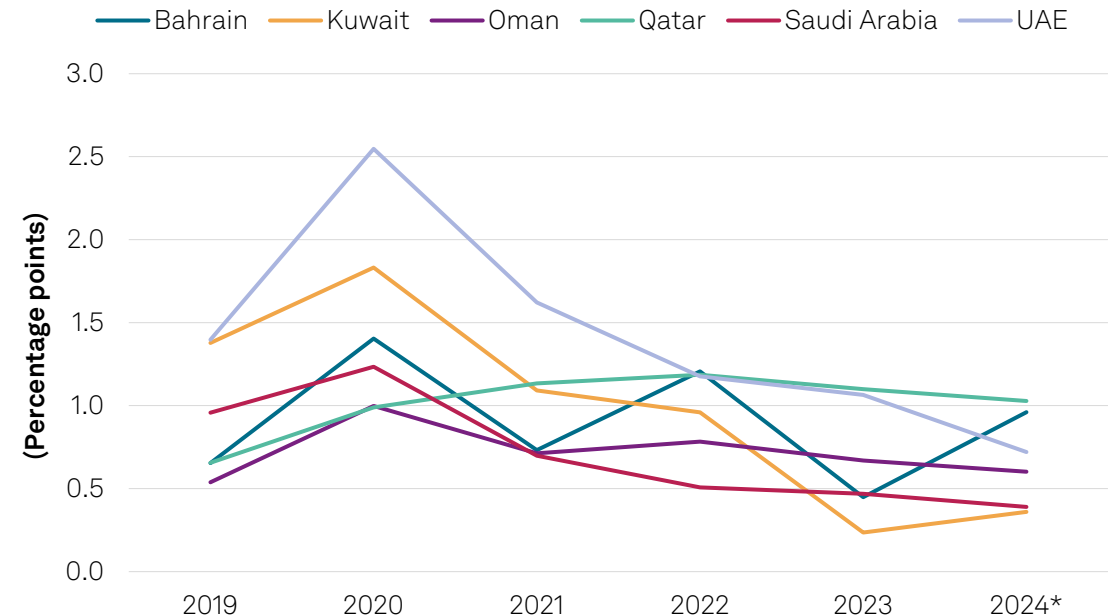
# Profitability | Good For Now, Some Moderation Due To Rate Cuts

- Margins have improved, thanks to higher rates, while cost of risk is inching up in some countries as banks use excess profitability to prepare for potential shocks or to cover for risks related to exposures in nondomestic countries.
- Banks continue to display strong efficiency, which benefits from low labor costs and increasing digitalization.

## Strong profitability for now



## Cost of risk is increasing in some countries

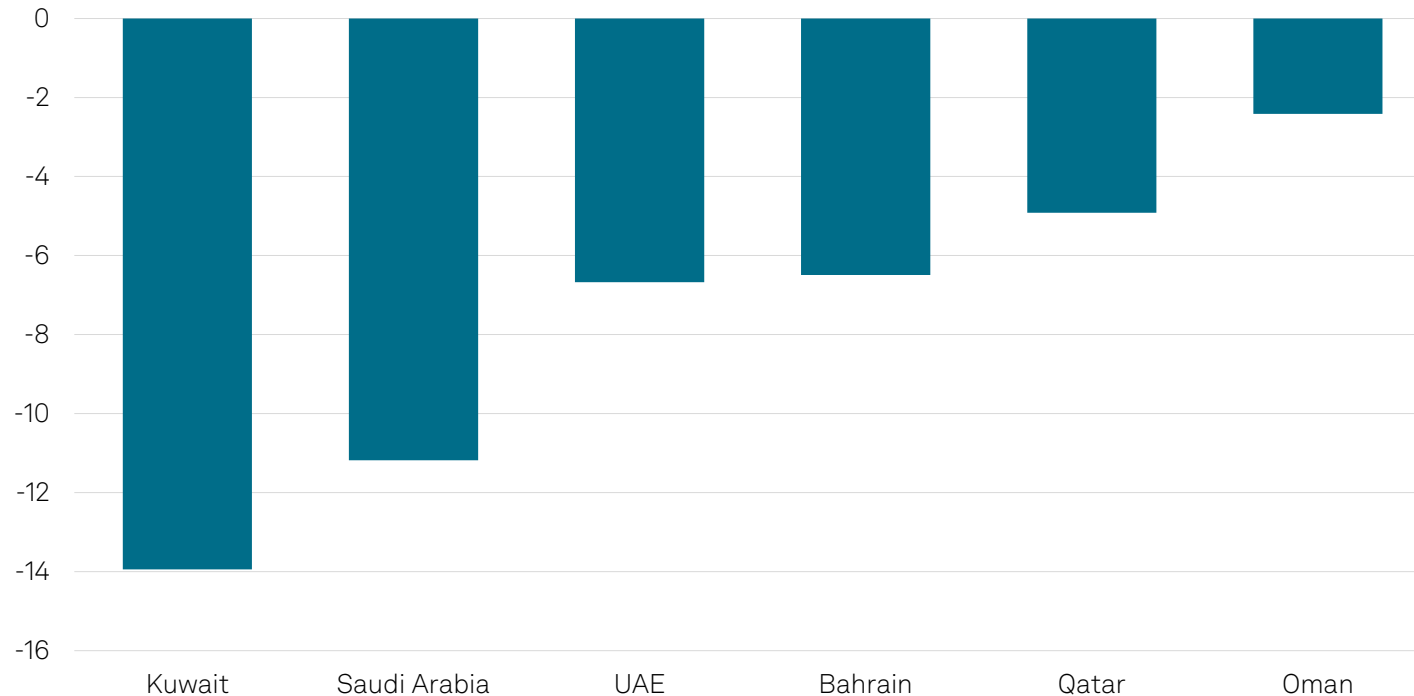


\*Annualized. Source: S&P Global Ratings.

# Interest Rate Cuts | Banks' Profitability Will Decrease Modestly

Effect of a 100-basis-point decline in interest rates, based on December 2023 disclosures

% of net income



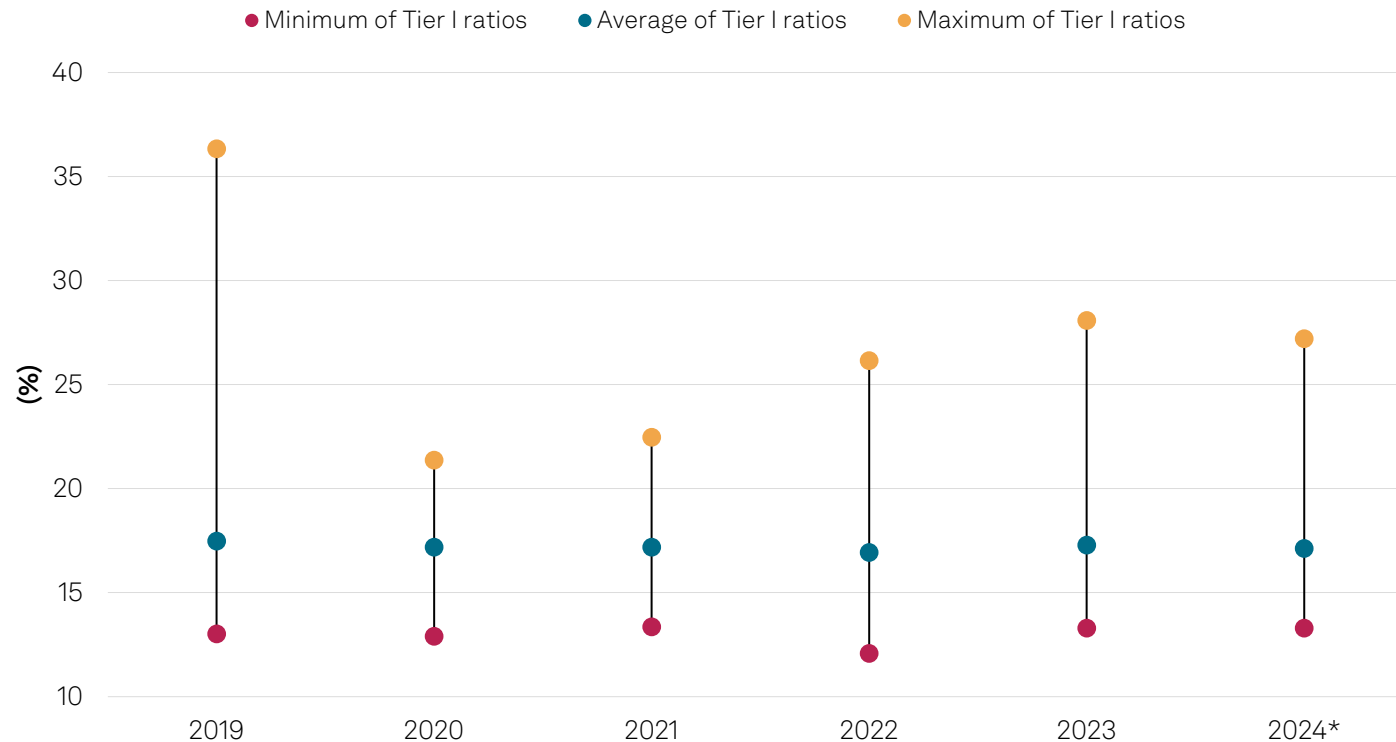
This chart is based on rated banks only and excludes any management action to deal with the rate decline. Source: S&P Global Ratings.

- We expect the Fed will cut rates by 225 basis points (bps) by the end of 2025 (inclusive of the 75-bps cut already delivered).
- GCC central banks are likely to mirror these cuts in varying degrees.
- The overall effect of the rate decline on profitability is negative. Yet it could reduce unrealized losses in securities portfolios and the cost of funding for banks that rely heavily on external funding.
- Based on our assumption that interest rates will decline by 225 bps by year-end 2025, we expect an average impact of about 25-50 bps on GCC banks' margins, with the following variations: 20-30 bps for Bahrain, 30-50 bps for Kuwait, 10-20 bps for Oman, +/-10 bps for Qatar, 20-30 bps for Saudi Arabia, and 40-60 bps for the UAE.



# Capital | A Supportive Rating Factor

## Tier 1 capital ratios show strong regional capitalization



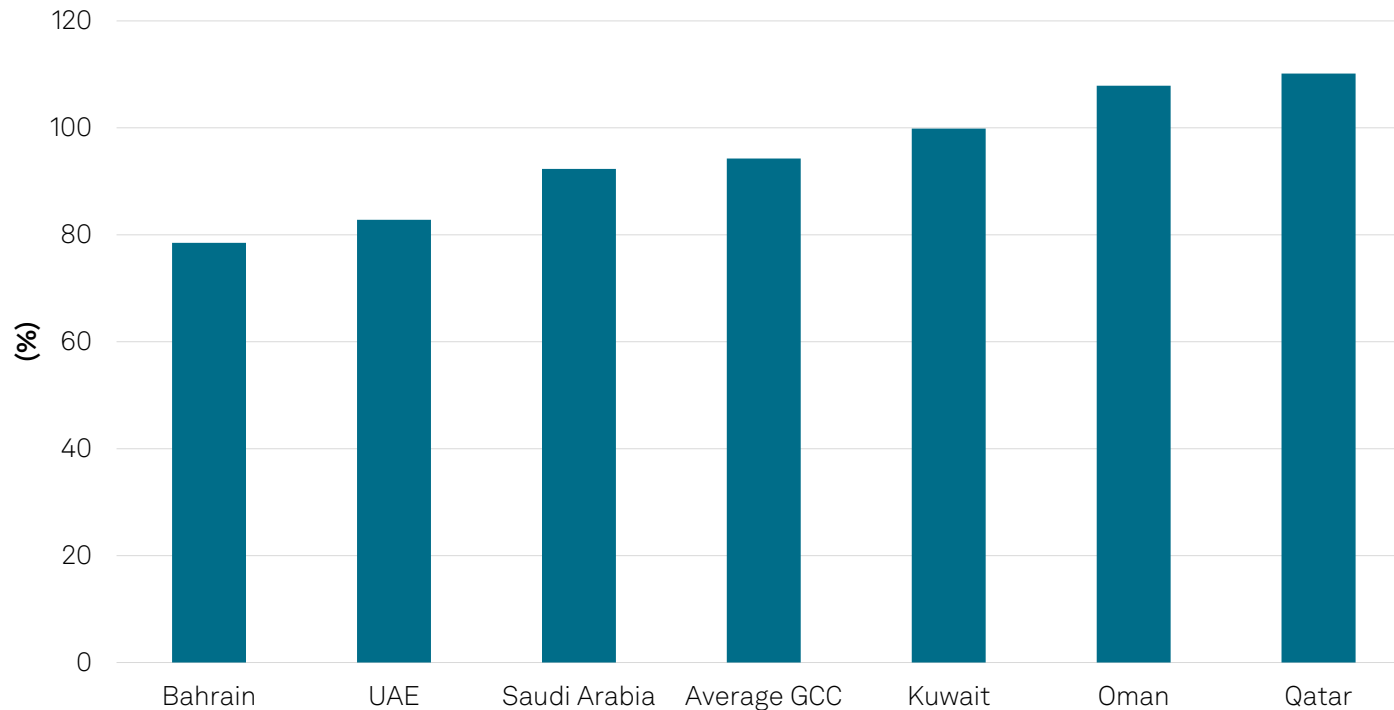
\*June 30. Source: S&P Global Ratings.

- GCC banks continue to benefit from a strong capitalization, supporting their overall creditworthiness.
- Supportive shareholders--dividend payouts tend to be below 50%--and strong profitability contributed to stable capitalization levels.
- The quality of capital is also strong, with a relatively limited contribution of hybrid instruments. We expect banks will likely increase hybrid issuance over 2025-2026 to benefit from lower rates and because several previously issued instruments will reach their first call dates.

# Funding Profile | Core Deposits Dominate

## Core deposits dominate GCC banks' funding profiles

Average loans/deposits (2019-2024\*)



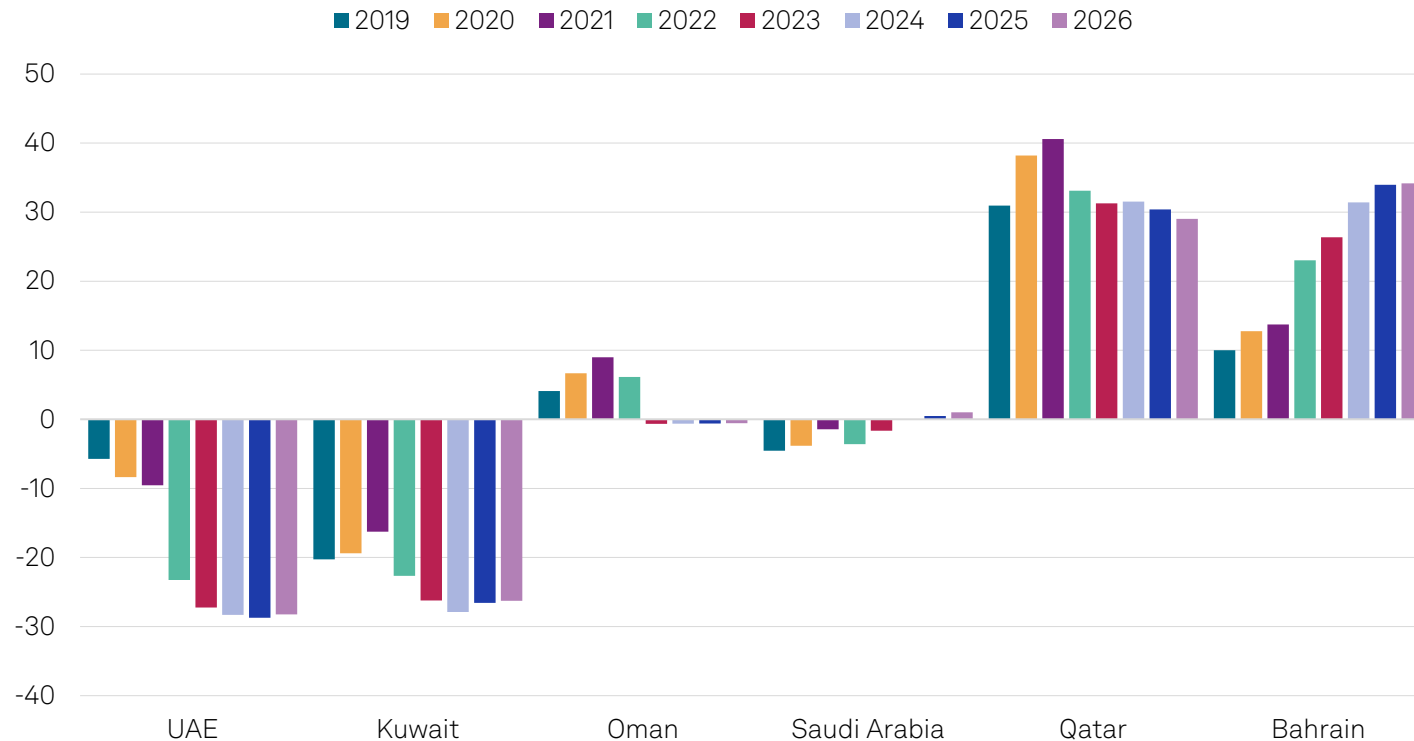
\*June 30. Source: S&P Global Ratings.

- GCC banks are mainly funded by domestic deposits, which have proved stable through periods of mild stress, such as the COVID-19 pandemic and previous instances of geopolitical risk.
- Public sector deposits typically account for 20%-30% of the deposit base (except in Bahrain, where this percentage is lower.)

# Funding Profile | External Funding Is Increasing In Some Countries

## External funding is high in Qatar and increasing in Bahrain

Net external debt/total loans (%)

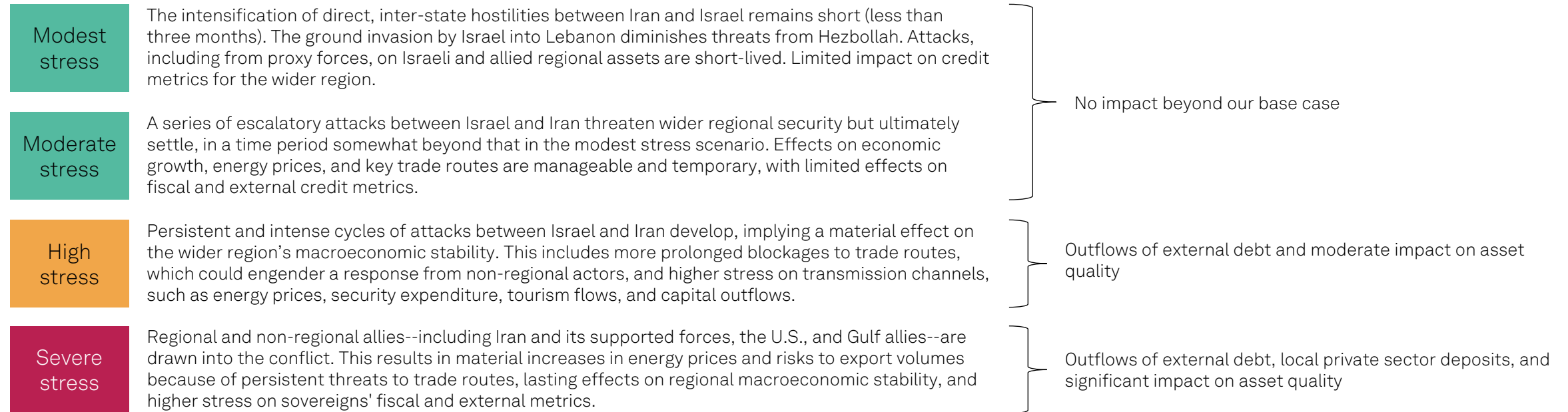


Source: S&P Global Ratings.

- UAE banks' local and external liquidity volumes are high. The system has benefited from the previous materialization of geopolitical risk. The external situation is similar in Kuwait, where banks have a strong net external asset position.
- In Saudi Arabia, deposits are not sufficient to meet the lending momentum. We therefore expect banks will resort to external funding. In Oman, banks moved to a net external asset position after external deleveraging.
- Even though external debt is significant in Qatar, the Qatari government has a strong track record of providing support to the banking system if necessary.
- The external debt increases in Bahrain is mitigated by the fact that other GCC countries account for a large portion of Bahraini banks' external debt.

# Stress Test | How Our Four Scenarios Can Affect Banks

We have identified four potential pathways via which the Israel-Hamas-Hezbollah conflict could have a more material credit impact on sovereigns and banks in the rest of the region. We have stress-tested banks' resilience to these scenarios.



For details on the numerical assumptions used for these scenarios see "What Would An Escalation Of The War In The Middle East Mean For GCC Banks?," published Oct. 21, 2024.

# Stress Test | Our Main Assumptions

## High stress

### External funding

### Outflows assumptions

- Non-resident interbank deposits: 50% outflows
- Due to banks' head offices and branches, for which we used an outflow rate of 20%.
- Non-resident deposits: 30% outflows
- Capital market liabilities: 10% outflows

### Liquid assets assumptions

- Interbank deposits: 10% haircut
- Due to head offices and branches: 20% haircut
- Investment portfolios: 20% haircut
- Loans to non-residents and other assets: 100% haircut

### Asset quality

30% increase in the stock of NPLs or an NPL ratio of 5% of total loans, whichever is higher. This scenario assumes that banks cover 100% of NPLs upfront by using existing surpluses.

## Severe stress

### External funding (same as high stress)

### Local private sector funding

- Private sector local deposits: 20% outflows, which is based on historical data from the 1990-1991 Gulf War. We do not assume outflows of government or other public sector deposits.

### Liquid assets assumptions

- Cash and deposits with central banks: 0% haircut
- Domestic investments: 20% haircut as most banks' local investments are in government bonds or highly-rated instruments

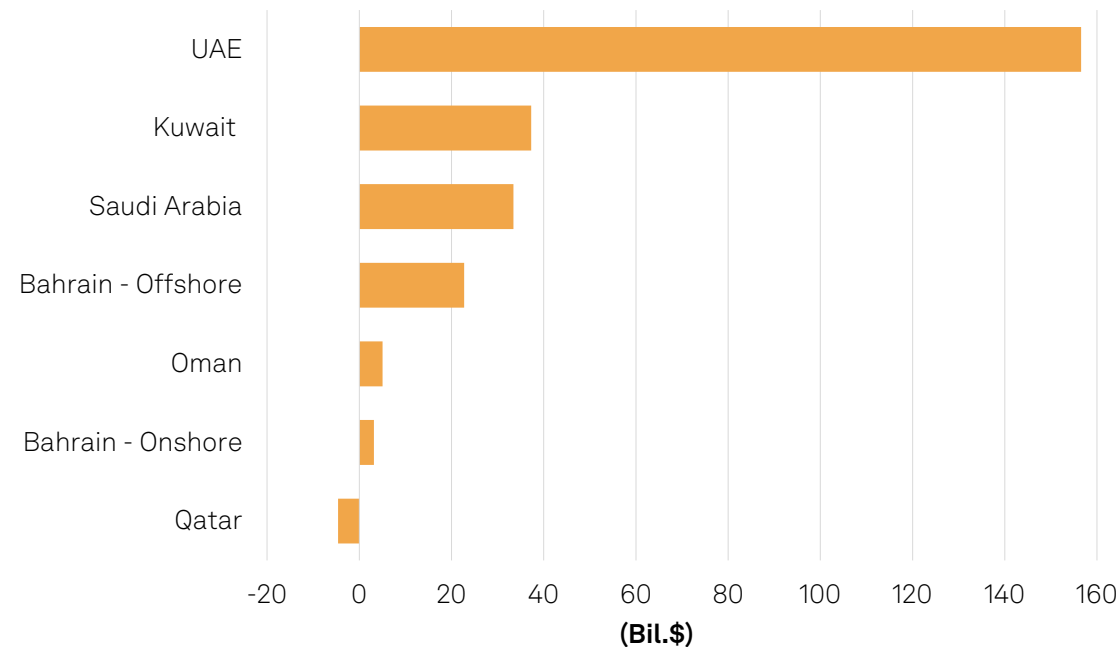
### Asset quality

50% increase in the stock of NPLs or an NPL ratio of 7% of total loans, whichever is higher. This scenario assumes that banks cover 100% of NPLs upfront by using existing surpluses.

# Stress Test | Banks Can Withstand Outflows

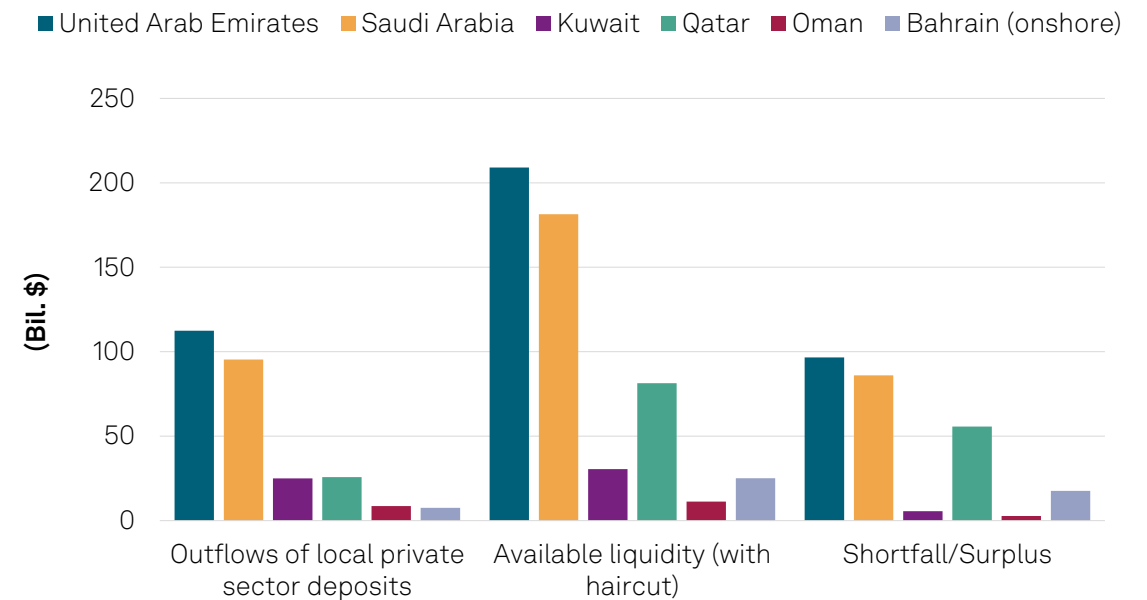
Banks appear resilient to external and domestic private sector deposit outflows. Only Qatar recorded a small deficit for external funding because of its weaker starting point. All banking systems have sufficient liquidity to withstand local deposit outflows. They even have an extra \$264 billion in liquid assets that they can deploy. All the data are as of June 30, 2024.

## All countries are in excess except Qatar



\*External liquid assets with haircuts - assumed capital outflows. Source: S&P Global Ratings' calculations.

## Banks can cope with local private sector deposit outflows

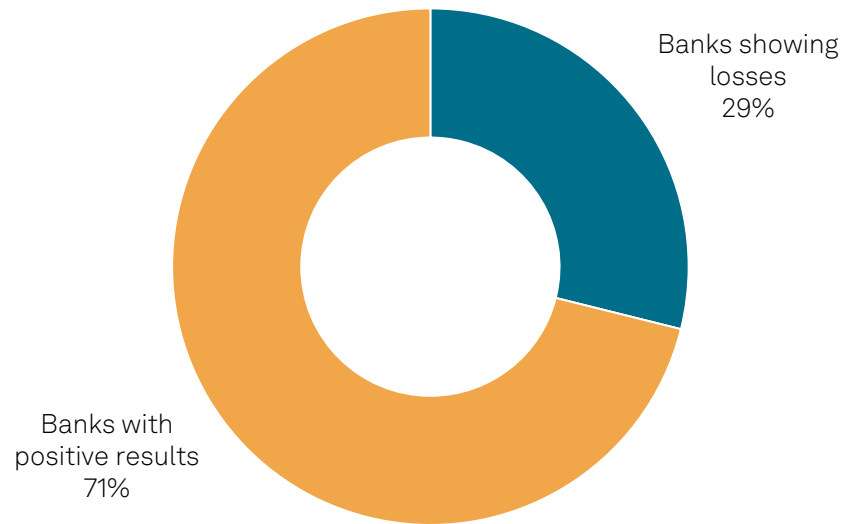


Source: S&P Global Ratings' calculations.

# Stress Test | Asset Quality Deterioration Could Cause Losses

Weak asset quality will likely generate a total cumulative loss of \$3.3 billion for 13 of the top 45 banks under the high stress scenario, and a total cumulative loss of \$24.6 billion for 25 of the top 45 banks under the severe stress scenario.

## Banks' results under the high stress scenario



Source: S&P Global Ratings' calculations.

## Banks' results under the severe stress scenario

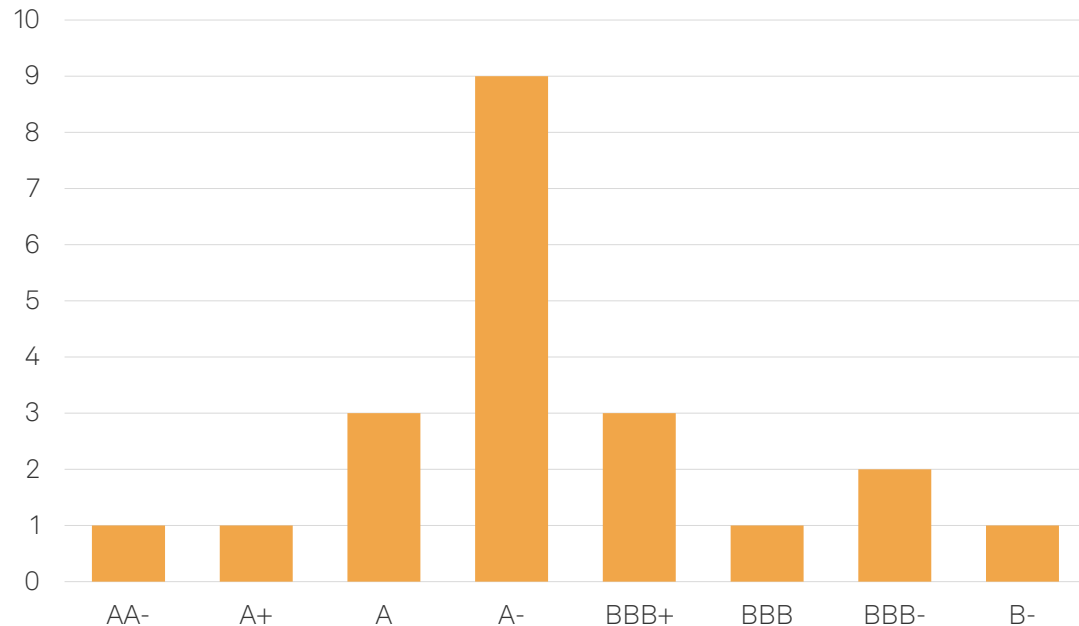


Source: S&P Global Ratings' calculations.

# Ratings | Positive Bias Mainly In Saudi Arabia

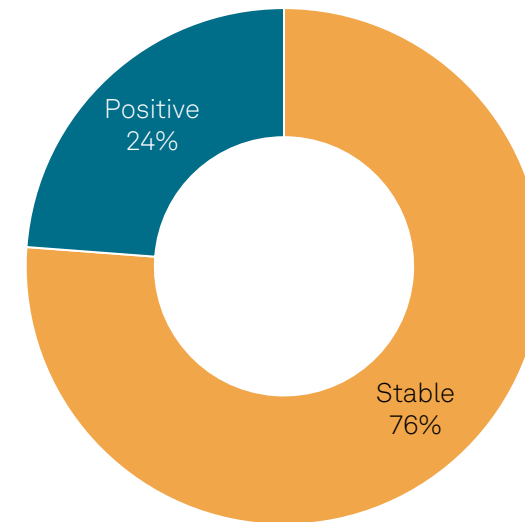
	Bahrain	Kuwait	Oman	Qatar	Saudi Arabia	United Arab Emirates
<b>Government support assessment</b>	Uncertain	Highly supportive	Uncertain	Highly supportive	Highly supportive	Highly supportive
<b>Anchor</b>	bb	bbb	bb+	bbb-	bbb	bbb-
<b>BICRA</b>	7	4	6	5	4	5
<b>Economic risk / trend</b>	7 / Stable	5 / Stable	6 / Stable	5 / Stable	5 / Stable	6 / Stable
<b>Industry risk / trend</b>	6 / Stable	4 / Stable	6 / Stable	6 / Stable	4 / Stable	5 / Stable

Bank ratings distribution as of Nov. 1, 2024



Source: S&P Global Ratings' calculations.

Outlook distribution shows a positive bias



Source: S&P Global Ratings' calculations.



## Related Research

- [What Would An Escalation Of The War In The Middle East Mean For GCC Banks?](#) Oct. 21, 2024
- [Your Three Minutes In Banking: GCC Banks Are Well Positioned To Continue Their Strong Run](#), Sept. 4, 2024
- [Your Three Minutes In Banking: When Rates Drop, GCC Banks' Profitability Will Follow](#), May 14, 2024
- [Your Three Minutes In Banking: Saudi Banks May Turn To Alternative Funding Options](#), April 30, 2024

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