Credit squeezed

GRAHAM BUCK LOOKS AT THE PLANS OF THE UAE CENTRAL BANK TO IMPOSE LENDING CAPS ON LOCAL GOVERNMENT ENTITIES.

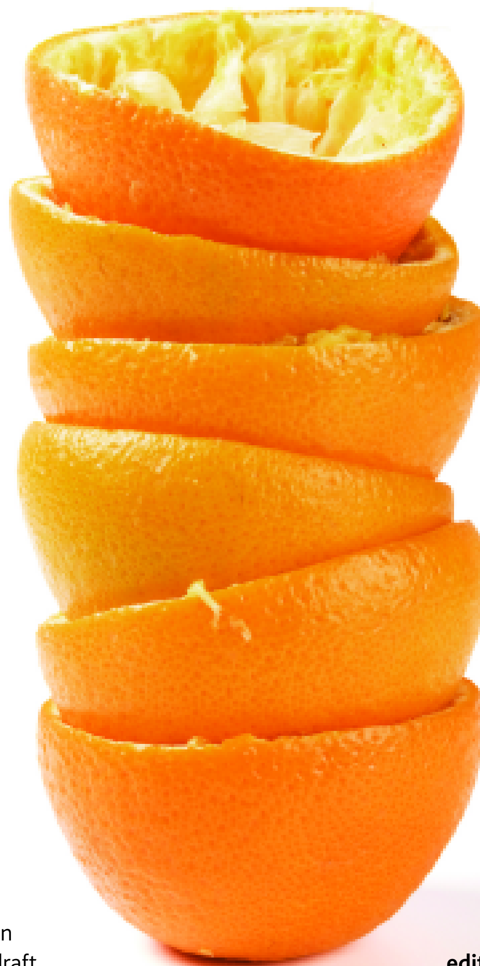
In April the UAE Central Bank announced that, following consultations with the IMF, it would no longer permit banks to lend more than 100% of their capital to governments across the seven-member UAE federation and their related entities. "Where there is an excess," a circular declared, "banks should make arrangements to regularise their position no later than 30 September 2012." The Central Bank also said that loans to individual non-commercial government borrowers would be capped at 25% of regulatory capital and at 15% for individual commercial government entities.

The restrictions have sparked concerns that credit will dry up, as banks review their loan books and reduce their exposure to local government entities before the deadline takes effect.

The Central Bank said that the IMF had urged it to protect banks from overcommitting to funding for government companies unable to access the international financial markets. Since Dubai's property market crash in 2009 and the debt restructuring requested by Dubai World, state-owned entities have increasingly relied on local lenders in the absence of funding from European banks.

In 2011, net exposure to government and public institutions of UAE banks rose by AED44bn (US$12bn), while provisions for bad loans increased 25% to AED55.3bn.

The restrictions are part of wide-ranging changes to local banking law. The Central Bank revealed that it was discussing "major amendments" with the Ministry of Finance that had reached draft stage. They include changes to the 1980 law under which the bank was established, laws governing the monetary system and the organisation of banking. Discussions also extend to a draft law on the organisation of the financial services sector. New regulations on retail banking in the UAE are expected to be issued this summer as part of a review of consumer finance.



A note published by Deutsche Bank shortly after the Central Bank's announcement identified National Bank of Abu Dhabi (NBAD) and Emirates NBD, Dubai's largest lender, as the two most at risk from the restrictions. It calculated that NBAD had a collective exposure worth 199% of its regulatory capital, ahead of ENBD at 192%.

Deutsche Bank warned that "although the interpretation of some aspects of the Central Bank's circular is open to doubt, the new limits will likely prompt some balance sheet deleveraging for the most affected UAE banks".

NBAD chief executive Michael Tomalin says the bank is in "active conversations" with the Central Bank and is confident that will produce a solution that enables NBAD to manage its balance sheet. "We don't want to sell off high-quality assets in the Middle East and be forced to buy lower-quality ones," he adds. "This would be an unintended consequence, which I don't think the Central Bank wants to see."

Reports suggest that another likely result of the new regulations will be greater activity in the international debt market. Yaser Abushaban, director of asset management at Emirates Investment Bank, says: "If you're limiting banks' ability to lend to the government and its entities, then they will have to find alternatives, which means tapping foreign banks or tapping international markets directly through bonds."

The UAE's economy and investor confidence in its prospects are steadily improving, as evidenced in Dubai's announcement in late April that it plans to raise US$1.25bn from a two-tranche Islamic bond sale. The deal is the first since the emirate last tapped the debt markets in June 2011, with a US$500m 10-year issue.

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