

Helping on the road to Recovery

Zak Hydari, Chief Executive of Rasmala, examines how financial institutions beyond the banking sector can help recovery in a post-COVID-19 world.



COVID-19 is the most serious public health and economic emergency the world has faced in modern times. The impact on the global economy will be severe and long-lasting. The eventual outcome will depend upon actions taken now by the various political and economic participants and stakeholders.

In the UAE, the Government has acted quickly to protect its population from the virus and has taken steps to mitigate and contain the threat to public health. It is also ramping up its health system to ensure that the country is adequately prepared to treat patients and manage the crisis.

The Government has also announced an emergency stimulus plan to support the economy and mitigate the impact of the COVID-19 shock by supporting lenders and UAE based businesses.

Fiscal policy will be central in efforts to shore up the country's economy. The UAE has introduced measures to defer government fees, defer loan payments and increase financing for small and medium-sized enterprises (SMEs).

Many SMEs are facing a sudden and significant drop in sales, supply chain disruption and cashflow constraints. They are also facing the impact of large corporates delaying supplier payments to conserve cash. This is important because in the UAE these companies contribute around 60

percent of non-oil economic output and employ around 90 percent of the private workforce.

Over the last 10 years the UAE Government has taken significant steps to boost the SME sector and increase its contribution to the economy. This crisis will adversely impact the entire sector and will make it difficult for many companies to survive without access to finance and broader government support.

The challenge now is how best to deliver this support.

The Government expects the banks to play a leading role in transmitting its fiscal stimulus to the economy. But many banks, in the UAE and elsewhere, are unable to support SMEs due to higher perceived risks, and therefore costs, compared to other more profitable segments. The capital requirements against such exposures also negatively impact the supply-side of bank lending to this sector. Although more than 90 percent of businesses, by number, in the UAE are SMEs, they account for only some 5 percent of total bank lending.

In this situation, the non-banking financial sector – Non-Banking Financial Institutions - can play an important and supportive role in acting as transmission entities to those companies, particularly SMEs, that need access to finance quickly.

As well as providing capital quickly and efficiently, Non-Banking Financial Institutions are ideally positioned to provide non-financial support including governance, talent management, mentorship, strategic advice and M&A.

There is a well-developed community of Non-Banking Financial Institutions in the UAE, including alternative asset managers, private equity firms and other independent investment firms. They tend to have specialist investment capabilities and are well placed to work closely with the Government, to increase the rate of transmission. The priority must be to make sure that every eligible business can access financing quickly and survive through the crisis.

It is equally important to increase access to capital in the form of subordinated loans and equity like instruments. This could be achieved by establishing a national strategic investment fund with local sovereign wealth funds (SWFs) acting as anchor investors and guarantors to other equity investors and lenders to the fund. A guarantee would make it easier and quicker for banks to lend to SMEs via the fund.

Although the Government might become a bigger shareholder in the wider economy, and the SME sector more specifically, the benefits would be twofold.

In the first instance, swift support will protect the economy by maintaining the highest level of employment possible. This is particularly important in the UAE which does not operate an income tax or social security system, so there is no corresponding safety net for the majority of the

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population. We have seen in previous crises, in the event of job losses and the lack of alternative jobs, residents are forced to leave the country. This has resulted in long term losses to the economy, both in terms of economic output and knowledge.

And secondly, if capital is made widely accessible, in a timely manner, and is structured to avoid the burden of additional debt, good companies will be in the best position to bounce back, expanding their operations and driving the growth that will repair the economic damage wrought by COVID-19.

If we can deploy capital by involving the broader financial community, this will amplify the economic impact and also strengthen the UAE as a leading financial centre. In seeking to mitigate the social and economic impact of the virus, the UAE has an opportunity to maintain its world class environment - retaining the best of human capital, technology, entrepreneurship, resources and business ideas.