Gulf Bank Insight Report

Economic Research Unit

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GULF BANK

CONSUMER CREDIT GROWTH IN KUWAIT

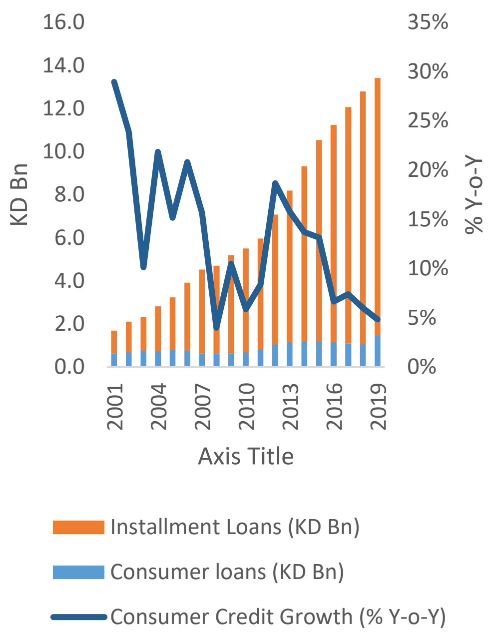
KEY HIGHLIGHTS

- Consumer credit is a key element to boost consumer spending, a key part of the economic engine. Positioned as an avenue for risk diversification and liquidity management, they form an important part of bank's loan book.
- In Kuwait's banking sector, consumer credit comprises of a considerable portion of total loans, at 34%.
- Analysis of data on different factors highlights that population growth, unemployment rate, vehicle sales and policy measures - increase in credit ceiling and distribution of grants - have a statistically significant impact on consumer credit growth. Economic Growth is significant with a lag of one year.
- Interest rates have a significant impact on consumer loans but not on instalment loans.
- Factors such as residential real estate sales, household consumption, income level and inflation do not significantly influence consumer credit.

Consumer credit comprises of consumer loans and instalment loans. Consumer Loans are availed for financing personal requirements such as consumer durables, or for covering expenses on education, health etc. Instalment Loans are utilized particularly for restoring or purchasing private residence. These loans help individuals enjoy the benefits of goods and services in the near term and pay for it over a period of time. This enables consumer spending, a key part of the economic engine. It benefits banks by providing an avenue for risk diversification and liquidity management.

In Kuwait's banking sector, consumer credit constitutes a considerable portion of the total loans at 34%.[1] Since 2001 and up to end of 2019, consumer credit has grown at a CAGR of 12.2%. This has been driven mainly by instalment loans, which have grown at CAGR of 14.4%. Consumer loans have increased by a slower rate at 4.7%. Customer base for consumer credit is largely public sector employees.[2] 60% of consumer loans and 72% of housing loans were lent to Kuwaitis. [3]

Figure: Consumer Credit Trends (2001-2019)



Source: Central Bank of Kuwait

[1] CBK, As of Dec 2020
[2] IMF
[3] Al Qabas/Gulf News

Consumer credit brings in diversification to a banks' loan book. Risk associated with consumer credit is minimised through credit of salary directly to the customer's account in a bank where loan has been taken, blocked deposits etc. Capping of loan amount in terms of salary of the borrower also aid in minimising risk. In terms of risk weighting of assets for the calculation of capital adequacy ratio which is the amount of capital that banks have to set aside to hold the loan, consumer loans carry 100% risk weighting. In comparison, risk weights assigned for a corporate range from 20% to as high as 150%, depending on their credit quality grade. [4] Additionally, the different loan tenures for consumer credit (ranging from 1 to 15 years) aid in liquidity management.

Banks adopt different strategies to boost consumer credit. A popular strategy is providing cash back, reward points or other offers on usage of their credit cards. They also offer loan top up option for customers who have re-paid 30% of their initial loan.

COVID-19 IMPACT

COVID-19 and accompanying lockdowns have impacted consumer spending and in turn consumer credit. As of June 2020, year to date consumer credit growth had been flat at 0.03%.

Banking sector in Kuwait had taken many measures to improve credit availability to consumers such as:

- Allowing delayed repayment of loans
- Reduction of interest rates
- Facility to open accounts and apply for loan/credit card online

Supported by these measures and relaxation of lockdowns in H2 2020, consumer credit growth for 2020, was higher at 6.8% y-o-y compared to a 4.8% y-o-y growth in 2019. As of February 2021, consumer credit had grown by 7.4% y-o-y, compared to 4.6% y-o-y growth in February 2020.

Key drivers of consumer credit

Several factors may influence consumer credit. Of this, a set of 10 factors and a few policy measures have been considered for analysis. Statistical analysis has been conducted on consumer credit and each of these 10 factors such as economic growth, unemployment rate, etc, to gain insights into their impact on consumer credit. Broadly, the time period covered in the analysis is 2001 to 2019.

The following factors have a significant impact on consumer credit growth:

1. Vehicle sales

Financing for vehicles has been a thrust area for both conventional and Islamic banks alike with initiatives such as zero-interest auto loans and special offers in tie-up with brands. This was reflected in the data with vehicles sales having a significant impact on consumer credit growth

2. Unemployment rate

The rate of unemployment has a statistically significant impact on consumer credit growth. They share a negative relationship whereby, with increase in unemployment, less people would be eligible for consumer credit.

[4] CBK

3. Population Growth

The increase in population over the years has had a significant impact in expansion of consumer credit. There is also high correlation between increase in population of nationals and the growth in consumer credit.

4. Economic Growth

Economic growth has a significant impact on consumer credit growth with a lag of one year. For example, consumer credit had grown 18.7% in 2012, following a real GDP growth of 9.6% in 2011. But it had slowed to 6.6% in 2016, following a 0.6% real GDP growth in 2015.

5. Policy Measures

Central Bank of Kuwait had increased ceiling on consumer loans from KD 15,000 to KD 25,000 in November 2018. This had resulted in significant uptake in credit. There have been instances of the state's grants in the past such as distribution of grants (2011) and waiver of public debt for some citizens (2013). While distribution of grants has had a significant impact on consumer credit, waiver of public debt did not significantly impact consumer credit.

A reduction in interest rates is generally seen as enabler of credit growth. In the context of consumer credit growth in Kuwait, interest rates have a significant impact on consumer loans but do not significantly impact instalment loans. This difference could be due to the duration of loans and conditions for re-financing. Though interest rate on existing consumer loans is fixed at the beginning of the loan period and is not re-priced in tandem with changes of interest rates, being short-terms loans, they are more susceptible to interest rate changes as loans are settled and refinanced as interest rates decline. For instalment loans, though re-pricing could be done once in 5 years, the change is to be not more than 2 percentage points. The option to re-finance is accompanied by the caveats such as 30% of the existing loan should have been repaid, payment of earlier instalments on due dates etc. Therefore, it could be likely that the propensity to re-finance is higher in the case of consumer loans given their lower value and ease of refinancing relatively.

6. Other Factors

Factors such as household consumption, income level and inflation do not display a statistically significant relationship with consumer credit growth.

Residential real estate sales do not share a notable link with consumer credit in general or instalment loans in particular. This could be due to the considerable difference in residential real estate prices and the maximum permissible amount on instalment loans at KD 70,000. Consumer credit growth is not significantly impacted by volatility in oil prices. This could be due to the fairly stable income levels in Kuwait.

Conclusion

In the short term, demand revival on the back of reopening of the economy and vaccines would likely support growth in consumer credit. Downside risks to consumer credit growth include lingering threat of COVID-19, decline in consumption due to repatriation of expats, a cautious approach to lending by banks in case of weakness in loan recovery, and possible government austerity measures in the event of lower oil price levels.