

4

Al-Gosaibi: A Debt Default that Rocked the Middle East





It was a high-profile corporate collapse that occurred in Saudi Arabia. It involved the Bahrain-based The International Banking Corporation (TIBC) as the owners, AHAB (Ahmad Hamad Al Gosaibi & Brothers Company) Group clashed with the Al-Saad Group into which they had married. It garnered interest across financial world as they were amongst the biggest business names in the country.

The allegation

Hamad Al Gosaibi (Gosaibi Family) is one of Saudi Arabia's top business magnates, with interests in multiple sectors, spanning countries, and continents.

Maan Al Sanea is a Saudi billionaire with roots in Kuwait. The big boss at the Al-Saad Group, primarily an investment company, he was the second largest shareholder in the HSBC Bank.

In the early 1970s, while oil was transforming the Middle East into an economic powerhouse, Al-Sanea married into the Gosaibi family. Sanea was put in-charge of AHAB's financial services businesses, and quickly rose in stature and influence within the company.

AHAB had a Money Exchange Division, which borrowed large sums from global banks. One estimate points out that about USD 120Bn was raised as loans, during 2000-09. The number alone is hard to digest, given the nature of the Money Exchange's business. What is certain, however, is that most of these loans were routed through TIBC in Bahrain, which in turn had raised funds from intermediate markets.

In May 2009, TIBC defaulted on its instalment obligation. As a direct fallout, the Money Exchange Division of AHAB too defaulted. In the ensuing legal battle, the Gosaibis declared that they weren't the fraudster but were victims of a USD 9bn fraud, orchestrated by Al-Sanea, who, they claimed, had complete control of the finance businesses.

More about the warring groups

Al Gosaibi Group

Ahmad Hamad Al Gosaibi and Bros (aka AHAB) is a highly respected private company in Saudi Arabia. Its founder, Ahmad Hamad, was initially involved in the production of silver coins for Saudi Aramco. In the 1950s, Hamad strengthened those ties by supporting Saudi Aramco's operations in catering, warehousing, oil pipes, and equipment. Later, he began supplying tires and boats and then expanded into fuel vending and automobile spare parts.

When his children grew up, they helped develop the business, leading to the establishment of Ahmad Hamad Al Gosaibi and Bros (AHAB). Later, the group opened the 1st Pepsi bottling factory in the eastern province of Saudi Arabia. Over time, it set up a diversified portfolio that covered manufacturing, construction, consumer products, energy, tourism, and hospitality.

Al-Saad Group

Maan Al-Sanea, a Kuwaiti fighter pilot who repatriated to Saudi Arabia in the 1970s, promoted the Al-Saad group. It was an equally respected name.

Al-Sanea started construction and contracting venture that became a business conglomerate, comprising 37 firms in such diverse fields as manufacturing, construction, engineering, real estate, financial services, hospitality, and healthcare, with investments cutting across countries and continents.

TIBC: what went wrong

When Al-Sanea married into the Al-Gosaibi group, he was asked to run AHAB's Money Exchange Division in Khobar. The Exchange was an excellent idea. It gave expatriate workers a convenient way to send remittance home and offered a few essential financial services. It also functioned as Al-Gosaibi family's in-house bank. The money exchange grew under Sanea and he has considerable influence over the banks.

Over time, Al-Sanea came into contact with Glenn Stewart who would eventually work as TIBC's CEO. Stewart was an Oxford graduate, with interest in Middle East affairs. He leveraged his knowledge of Arabic and Islamic finance to forge business relationships and create Islamic finance products. In 1989, after brief stints in Bahrain, Stewart moved to Saudi Arabia to join Al-Gosaibi.

Stewart began advising Sanea on various short-term finance mechanisms, including Sharia-compliant arrangements. In 2001, with AHAB's Money Exchange facing legal restrictions, Stewart suggested opening a bank in Bahrain. It was a masterstroke for two reasons. One, international bankers were comfortable with Bahrain, as it was ranked 11th in the Economic Freedom Index. Two, they would be lending to a bank instead of a corporation.

In 2003, The International Banking Corporation (aka TIBC) came into existence, with Al-Sanea, as managing director and Glen Stewart, as the chief executive officer. AHAB owned TIBC, and this prompted bankers to believe that AHAB would make good on any business loss that TIBC might make. TIBC lent to SME businesses in Saudi Arabia and routed the transactions through the Money Exchange.

In 2004, Sanea established Awal Bank, in Bahrain. Following that he left the office of the Board of Directors in TIBC, but remained engaged in its affairs.

By 2008, TIBC had the third highest capital to risk ratio among Arab banks. From 2004 to 2009, it had loaned USD 6.3bn to over one hundred customers. Some of these loans were as big as USD 67mn, and several customers renewed the loan multiple times. There were a few bizarre loans, like the USD 7.5mn to a textile merchant, USD 12mn to a man who traded in 'decor items,' and USD 35mn to support an auto-parts dealer.

After the onset of the global financial crisis, TIBC defaulted on its borrowing. The creditors expected AHAB to repay, but the Gosaibis weren't willing. They claimed that they were victims of a multi-billion dollar fraud and that they were ignorant of the siphoning of funds that took place in the company. These claims were undermined, when documents showed that an AHAB partner was aware of some of the transactions. Taking cognizance of this, an English court rejected AHAB's claim.

A series of suing and counter-suing ensued.

Who sued who

| Party | Counter - Party | Claim (\$mn) | Jurisdiction |
|---------------------------|-----------------------|--------------|--------------|
| Mashreq Bank | Al Gosaibis | 225 | New York |
| Deutsche Bank | A subsidiary of AHAB | - | New York |
| Commerz Bank | Al Gosaibis | | London |
| Abu Dhabi Commercial Bank | Unit of Al-Saad group | 30 | - |
| Société Générale | Al-Saad Group | 50 | London |

Source: The Gulf AHAB/Al-Saad cover story

The financial crisis that began in Wall Street had unintended consequences across the globe. The fall of Lehmann Brothers led to banks demanding repayment from TIBC. Since it was impossible to pay up, Stewart made an interim arrangement through a 'split-value' foreign-exchange deal.

A 'split-value' deal takes advantage of the fact that banks exchanging currency operate in different time zones and different holiday periods. Suppose a New York bank paid TIBC a hundred dollars on a Thursday afternoon in exchange for equivalent Saudi riyals. TIBC would not make the return payment until Sunday because banks in Bahrain are closed on Friday and Saturday. But on Sunday the banks in New York are closed so such a deal would be settled only on Monday!

This arrangement delayed an immediate disaster. However, in the last week of April 2009, Stewart, in a final effort to keep TIBC afloat, requested the Dubai-based Mashreq Bank to loan USD 150mn to AHAB. Stewart promised to return it a week later. When the loan fell due on May 5th, instead of repaying, Stewart sought an additional USD 75mn, for which Mashreq Bank agreed. He assured the lenders the full support of Al-Gosaibis in repaying the loan.

The Gosaibis, in turn, echoed these assurances to Mashreq.

Then, on May 11th, 2009, TIBC defaulted. AHAB now owed Mashreq \$250Mn. There were also dues to an incredible 62 other banks, which it could not service.

In Feb 2010, the Bahraini government hired Kroll, a private investigation firm, which was paid by the Al-Gosaibis. Kroll's report had it that Al-Sanea provided most of the names and their relevant documents to Stewart. It also revealed that there were names of real businesses in TIBC loan books and that these were carried out without the company's consent.

In the aftermath of the collapse of TIBC, a travel ban was imposed on Stewart in connection with an ongoing investigation into TIBC conducted by audit major, Ernst & Young (now EY).

Saud-Al Gosaibi, the brother in law of Maan Al-Sanea, upped the ante against Al-Sanea by bringing in lawyers to investigate what had transpired in TIBC. Eric Lewis, a US-based attorney, spearheaded a lawsuit in California against Stewart, naming him a co-conspirator, along with Maan Al-Sanea in defrauding the Gosaibi family of \$9Bn.

In 2011, five banks collectively went to trial against the Gosaibis in the U.K. over the AHAB debt. The banks argued that the Gosaibis, as the owners of TIBC and the Money Exchange, were obliged to cover their obligations. The Gosaibis denied any responsibility, stating that they did not know about the extent of Al-Sanea's activities or even of the existence of TIBC. The banks won the case as documents emerged suggesting the Gosaibi family members' knowledge of the transaction.

In 2013, the Gosaibis agreed to drop the charges on Stewart to focus on reclaiming billions from Sanea. Four years (2009-13) since the crisis the ramifications of the fraud are still felt by the Gosaibis. They were forced to sell their Pepsi facility, and the Saudi government banned them from traveling abroad.

Stitching a settlement

Saudi-based or Saudi-owned banks hold one-third of the debt. Banks from abroad, including BNP Paribas and Standard Chartered, hold another one-third. Rest of the debt is with non-bank investors, who bought them in secondary markets.

In a bid to resolve these claims, AHAB met the foreign creditors in the summer of 2014 and offered to pay 20 cents on the dollar, plus at least half of any recoveries from litigation against Al-Sanea.

Meanwhile, the Al-Saad Group came out with a statement on June 2nd, 2009 saying that their business accounts were unimpaired, but creditors made a quick exit. On the same day, the Group's credit rating was cut and later suspended. Five days since, on June 7th, 2009 banks in the UAE were instructed not to lend any more to Al-Sanea. In an emergency move to raise cash for its operations, the Al-Saad Group sold its holdings all over the world, including shares in HSBC, in which it was the second-biggest shareholder; Berkeley, a British homebuilder; and 3i, the private-equity firm.

Nine years on, the creditors are yet to reach an agreement on how they should recover their money.

An S&P survey of 30 commercial banks showed that, while total exposure net of collateral to the Al-Saad and Al Gosaibi groups is significant and will put additional pressure on ratings, banks, in general, should be able to manage any fallout.

Banks from Saudi Arabia, home to the two troubled groups, and the UAE, the region's financial centre, have been the most exposed to these groups.

While an agreement that does not involve Saudi banks is unlikely to be approved by the regulators, some of the creditors feel that the government has been little more willing to nudge the local banks to accept the agreement, as that would send positive signals to global investors. Al-Gosaibi Group signed a 'Settlement support agreement' with its creditors. AHAB said that 90 percent of creditors by number and 56 percent by value had agreed to the terms, which potentially allow them to recover around 50 percent of their loans, albeit at below par rates. If the required level of support from either creditors or the government proves unattainable, the saga's future could turn out to be a lot longer than it's past.

The Al-Gosaibi Scandal had comparatively lesser ramifications as Saudi Arabia had enormous cash reserves to stave off the crisis. And two, the government's decision to freeze the assets of Al-Sanea, bolstered Saudi Arabia's position as an uncompromising country that clamps down on the wrongdoers.

At one point, people had wondered if TIBC's default may have led to questions about the sustainability of Bahrain's banking sector. This was quickly put to rest, as Fitch Ratings reaffirmed Bahrain's "A/Stable" outlook.

Post script

In June 2018, the Chief Justice of Cayman Islands dismissed rival claims made by Al-Gosaibis and Al-Sanea, finding both groups to have defrauded scores of banks over decades. The ruling follows a decade-long dispute played out in international courts between the warring families over who was instrumental in the fall of each other's empires. The court found that AHAB knew of and authorized the fraud carried out by Al-Sanea. It also dismissed a \$5.9 billion counterclaim by Saad.

Key-event timeline

On May 12, 2009, Bahrain based TIBC, wholly owned by Ahmad Hamad Al-Gosaibi and Brothers Co. (AHAB), of which Al-Sanea is the managing director, defaulted on some of its bank debt. This default fuelled rumours that the bank would start a company-wide restructuring. S&P lowered the bank's

rating to ‘Selective Default’ that alleged that the company was unwilling to honour its debts, despite having USD 400mn in its equity.

On May 22, 2009, the situation worsened for Al-Sanea, as S&P revised its outlook for Al-Saad group from stable to negative. Reasons cited by S&P included the high concentration of securities holdings in the global financial services sector, the volatility of Al-Saad Group’s portfolio, the active use of debt to expand the Group’s asset base and the company’s high level of exposure in the real estate industry. Real estate was one of the most affected sectors in the region following the crisis.

On May 28, 2009, the Saudi Arabian Monetary Agency (SAMA) ordered to freeze the accounts, including credit cards, of Al-Sanea, his wife, and four other family members. Public knowledge of the development raised alarms about the unprecedented move by the Saudi government against one of its most influential business houses.

On June 2, 2009, Moody’s downgraded the ratings of major Al-Saad group of companies by six levels: from Baa1 to B1 (Junk Bond) status. Moody’s also added that the group’s ratings could be downgraded further as it was at a heightened risk of default.

On June 24, 2009, Al-Gosaibis held a creditors’ meeting in Bahrain. In the meeting, it was revealed that the group owes \$9.2 billion to over 120 banks all over the world. The group’s representatives claimed “substantial financial irregularities” in the group’s financial-services arm.

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