

Weekly Economic Commentary – July 12, 2009

Markets

After the euphoria of the second quarter investors are focusing on labor indicators and discount good news on those sectors (e.g., industry) which are improving. There is a general sense that stocks valuations are overstretched. The onset of the US corporate earnings season heightened the growing sense of unease about the global economic outlook. Equity markets in the region were sharply down for the second week in a row; the financial sector in the Dubai Financial Market suffered heavy losses after the S&P downgraded major banks while real estate sector continued to slide down. Oil suffered a sharp correction, falling below \$60 a barrel for the first time since mid-May, as bearish US supplies data took its toll on investor sentiment. Rising risk aversion also led to a volatile currency market with erratic daily movements.

Global Developments

IMF sees the global economy emerging from the recession “but stabilization is uneven and the recovery is expected to be sluggish.” Economic growth next year may be 0.5% higher than projected in April 2009 which means 2.5% growth, but in 2009 contraction will reach 1.4%, worse than previously estimated. Emerging markets will slow sharply, growing by only 1.5% in 2009 before rebounding to 4.7% in 2010. China will see growth of 7.5% in 2009 (8.5% in 2010) and India 5.4% (6.5%).

The most concrete outcome from the G8 summit was a \$20 billion aid package over 3 years for a “food security initiative”. A diverse set of topics ranging from financial regulation to a new economic stimulus were discussed, but views remained divergent on actions.

USA: ISM index of non-manufacturing activity grew by 3 points, with most major components rising in tandem. At 47, the index still implies contraction, but at a slowing pace. U.S. first-time jobless claims dropped 52k in the week ending July 4th, while continuing claims rose 159k – partly as a result of the auto-shutdowns in May-June. The labor market remains fragile.

Europe: Germany's Industrial Production rose 3.7%*mom* in May, a lot stronger than expected and, confirming the rebound, manufacturing orders data posted a strong 4.4%*m/m* rise in May. The momentum in the industrial sector has swung decisively through the first half of this year and May data from France, Sweden and Emerging Europe echoed this recovery: Hungary's Industrial Production was up 2.6%*m/m*, *sa*, Turkey's IP was up by an estimated 2% *mom sa*, Romania's industrial sales rose 4.9%*m/m*. French exports were up 4.5%*m/m* the strongest monthly gain since the onset of turmoil in 2007. On the negative side, UK Industrial Production was contracted by 0.6% *mom* in May, Italy's was flat, Holland's was down by 1.8% *qoq*.

Asia and Pacific: The strongest rebounds are evident in Asia: Taiwan exports were up 4.8%*m/m* in June, and were up 96%, *sar*, from Q1. In Q1, they had been down 60%, *ar*, from Q4. China reported for June a \$8.25bn trade surplus, with imports jumping \$12bn on the month, and exports \$7bn. Imports growth is a reflection of the stronger-than-expected acceleration in domestic demand growth. India's budget for FY2009-2010 had a significant negative impact: the Sensex fell 5.8%, led by financials. The rupee was down 1.3%. Investors worry about the high borrowing levels in the new budget with deficit forecast at 6.8% of GDP for FY09/10, up from 6% in FY08/09 (and an initial estimate of 2.5% of GDP). Risks of downgrade loom if fiscal discipline proves to slip further away.

Bottom line: Economists are revising up growth estimates for 2010. However, they remain divided about whether the recovery will begin in the latter half of 2009 or be delayed until 2010. Consensus suggests that the U.S. economy might bottom in H2 2009 and that Chinese acceleration in H2 2009 could be more

pronounced. The outlook remains weak for Europe (especially the East) and Japan.

Regional Developments

- MEED's annual survey of the top 20 banks in the GCC by asset size reveals that despite the difficulties caused by the global financial turmoil, their combined assets grew by 15% last year to \$752.6bn. With three exceptions – Arab Banking Corporation, Gulf International Bank and Gulf Bank – all banks on the list increased their assets in 2008.
- The Middle East economies will expand by 2%, compared to 5.2% in 2008, according to the IMF. The growth forecast for 2010 was raised 0.2% to 3.7%.
- OPEC's World Oil Outlook 2009 forecasts that consumption of crude would not return to 31 million barrels per day (the level it averaged in 2008) until 2013, because of economic weakness and slowdown in demand.
- IPO activity in MENA declined by 87% during the first half of 2009 (1H09) compared to 2008 according to data from Zawya. IPOs raised \$1.21 billion in 1H09, down from \$9.3bn during the same period last year.
- According to report released by HSBC (and picked up by Reuter and Bloomberg) Saudi banks may have between USD 4-7 bn in lending exposure to troubled conglomerates Saad Group and Alghosaibi. Zawya reported an unconfirmed total exposure of \$40bn by the banking sector to the troubled groups.

Market Intelligence on the UAE:

- S&P revised the credit ratings on Emirates Bank International, National Bank of Dubai and Mashreq bank down by one notch to A-minus from A. It also revised down the rating on Dubai Islamic Bank by one notch to BBB-plus. Banks' asset quality is still expected to

deteriorate significantly, however, the rating agency said.

- Dubai's second-largest property developer Deyaar expects to close a 500 million dirham distressed debt fund by year-end, the firm's chief executive said on Tuesday.