

Weekly Economic Commentary – August 23, 2009

Markets

Fluctuations in risk appetite continue to generate volatility in all markets, but stock indices and exchange rates stayed within limited ranges. On Wall Street the S&P 500 passed the 1000 psychological threshold and most other markets were broadly up, despite sharp fluctuations in China equity markets (down 5% one day up 4.5% the next) affecting all emerging markets, which recorded losses for the week. All regional stock markets were down, with the real estate sector weighing heavily on the decline in the DFM index. However, Saudi closed higher yesterday, following the US market rally and the oil price surge Friday. In fact, oil rallied above \$70/b as a big decline in U.S. inventories ignited a rush to cover short positions. Gold continues to fluctuate mostly in tandem with the dollar which weakened marginally against major currencies.

Global Developments

USA: The real estate market remains weak with new house starts down 1% mom in July, and 37% yoy. The small recovery seen in June did not last. Initial jobless claims increased to 576,000, indicating that labor market conditions are still broadly depressed. The only silver lining for the US this week came from the leading economic indicators which were up 0.6% mom for a fourth consecutive month.

Europe: Surveys data were upbeat with the PMI recording the second sharpest rise on record for the services index driven by a positive surge of sentiment in Germany. The manufacturing index was also up but more moderately. The ZEW index which gauges economic expectations in Germany rose in August, taking the indicator to its highest level since April 2006. Based on

past experience the data are consistent with Euroland GDP rising by about 0.2%qoq in Q3, after a drop of 0.1% in Q2.

UK inflation was flat on the month and up 1.8% yoy, a notable difference with the euro area where prices are decreasing. Retail sales increased in July confirming the resilience of consumers even in these testing times.

Asia and Pacific: Japan's GDP increased by 0.9% in Q2 as a result primarily of the stimulus package which boosted consumption. Singapore's July non-oil domestic exports fell by 8.5% yoy but the pace of decline has significantly slowed compared to large drop in January-February. Taiwan GDP fell 7.5% in Q2 which is much less than in Q1, largely thanks to a surge in domestic demand offsetting the weakness of the export sector.

Bottom line: The flow of data was scarce last week and it has not dramatically changed the global picture. Q2 saw an overall global improvement in economic conditions, but with striking diversity. Emerging Asia recorded generally double-digit q/q, saar, GDP growth rates, while North America continued its slump, driven by deep ongoing adjustments in the U.S. (especially the labor market) and a weak auto sector (GM and Chrysler). Europe was in the middle, with economies that resemble the U.S. (U.K., Ireland, and Spain) and countries following in the wake of Asia driven by Industrial Production (Germany, France, Poland). Q3 will see the crucial test for the global economy, i.e. whether the stabilization in Q2 will be followed by a recovery. The equity markets are heavily betting on this outcome while the bond markets foresee a continuation of easy monetary policy and weak growth. They cannot be both right.

Regional Developments

- According to the Alroya al Eqtissadia newspaper Algosaibi & Brothers' (Ahab) senior staff met creditor banks' executives in Dubai apparently to show falsified documents used by The International Banking Corporation

(TIBC) to obtain loans and money transfers.

- The GCC countries are likely to invest as much as \$50 billion in power projects between 2009 and 2015, according to the Economist Intelligence Unit (EIU) due to buoyant economic growth, coupled with increases in population.
- Moody's gave a negative credit outlook for Bahraini financial institutions, with a likely increase in non-performing loans and exposure to construction and real estate sector raising concern.
- The GCC bond and Sukuk market is recovering, with volume reaching \$18.4 bn in H1 09, increasing 37% compared to the same period last year; sovereign issuances dominated the majority of the amount raised while most Sukuk issuances were from Bahrain.
- Kuwait's budget surplus for the fiscal year ended Mar09 fell by around 70% to \$9.6 bn from last year's \$32.4 surplus. Though high oil prices in H1 08 boosted oil revenues to a record high, the spending of \$63.6 bn reduced the surplus substantially.

Market Intelligence on the UAE

- Independent reports by EFG-Hermes, Colliers and Landmark Properties put the drop in Dubai real estate price in a range between 44-60% depending on location and characteristic of the property (Source: Zawya). Some positive signs are nevertheless detectable for example on Palm Jumeirah, where prices are crawling up.
- The National reported that public prosecutors are investigating or bringing to court 11 cases of corruption and fraud in Dubai with 34 executives in at least 8 major firms (6 of which owned by the Dubai Government) have been indicted. The documents specify that AED 3.58 billion had allegedly been stolen or used as bribe money. The biggest case involves Dubai Islamic Bank, which officials say has been defrauded of AED

1.82bn. Analysts expect the investigations will improve investor confidence.

- A study released by Dubai Chamber of Commerce & Industry based on the first half of the year showed total export in Q2 09 was 6.5% higher than the total exports of AED 43.7 bn in Q1, with Saudi Arabia the largest market among the GCC countries.
- To lower borrowing costs, the Central Bank has allowed banks to borrow at a rate of 1% rate for up to a month against certificates of deposit compared with a limit of a week until now.
- The Ministry of Economy reported that per capita income in 2008 rose by nearly 16% to Dh196, 100.