

Weekly Economic Commentary – June 20, 2010

Markets

Stock markets extended their rebound after a dismal May performance led by Euroland. Emerging markets interrupted their slide despite doubt looming on China's soft landing. The GCC stock index was marginally higher thanks to KSA and Qatar, but other bourses displayed negative signs. Low volumes typical of the summer period are dominating most regional markets, dragging most share prices lower and some indices to new yearly lows. The euro firmed from recent four-year lows as investors' risk tolerance rose with the set-up of the European intervention fund and euro zone industrial output data surged. Gold hit fresh record highs while oil prices advanced and are now close to \$80 per barrel.

Global Developments

Americas:

- US Single-family housing starts and permits slumped in May (-10% mom), after expiry of homebuyer tax credit.
- May's producer price index declined 0.3% mom, largely from lower energy prices (-7%) while PPI ex-food and energy rose 0.2%, reflecting rise in tobacco (2.2%), lightweight vehicles, aircrafts and prescriptions prices.
- Industrial production registered an unexpectedly strong gain in May at +1.2% mom (+7.6% yoy).
- May CPI was broadly in line with expectations (-0.16% mom) – a 2.9% drop in energy prices pulled the overall index down while food prices were flat on the month.
- Jobless initial claims rose by 12k to 472k in the week ended June 12, while continual claims rose by 88k during the week ended June 5. Still no respite in sight in the weak labor market. The modest recovery is a jobless one

which is likely to affect November mid-term election results.

Europe:

- Moody's downgraded the Greek sovereign to 'junk' (from A3 to Ba1, with a stable outlook).
- Fear of contagion from Spanish banks hit the markets, but fears subsided when the authorities promised to conduct a stress test on the banks' balance sheets (and disclose the results). Other EU countries will follow this practice.
- Eurozone industrial production shows that the recovery is robust, +0.8% mom (+9.5% yoy).
- May's inflation for the Eurozone clocked +1.6% yoy, in line with preliminary estimates.
- The Eurozone ZEW Survey on economic sentiment for June showed a steep decline to 18.8 from prior month's 37.6. More specifically, the survey for Germany surprised negatively, declining to 28.7.
- German PPI grew at +0.3% mom in the month of May and 0.9% yoy beating expectations, while UK CPI rose 0.2% mom in May, (2.9% yoy), putting pressure on the Bank of England for revising up its interest rate.
- April unemployment is down to 7.9% in UK and the claimant count decreased by -31k in May, both better than expected. Surprisingly during this recession the UK unemployment has risen only slightly.
- Ahead of the UK budget this week (June 22nd), public sector net borrowing surprised on the lower side – at £16.0 billion in May, above £10 billion in April, but below expectations of £18.3 billion.

Asia and Pacific:

- China has signaled to the US government that it is ready to revalue soon the Renminbi.
- Japan's industrial production grew 1.3% mom in April

(+29.5% yoy).

- India's inflation (WPI) for May rose to a high 10.2% yoy, with core inflation (excluding food and fuel) also increasing sharply by 2.7% mom after an earlier decline in March.
- Singapore's non-oil domestic exports were up 24.4% yoy in May- sustained by electronics exports. Exports to China remained robust, while there were signs of moderation in exports to the US and Europe.

Bottom line: Manufacturing across the world continues to perform strongly across the world, but the employment situation is not improving and the banks are still under stress, especially in Europe where losses might still be concealed in balance sheets. A great deal of attention is absorbed by the soft landing engineered by the Chinese authorities through a mix of monetary tightening and administrative measures to stem real estate inflation. The proposed flexibility/revaluation of the Remimbi must be seen in this context. Meanwhile labor unrest is a sign that a boost to domestic living standards in China is becoming a political hot potato and not only a request from outsiders, eager to curtail its current account surplus.

Regional Developments

- According to a recent Moody's report, the year 2012 will pose a major challenge for GCC corporates as \$28 bn worth of debt will mature that year, with majority held by entities based in Dubai and Abu Dhabi.
- Ernst & Young reported that the value of MENA's mergers & acquisitions dropped 59% yoy to US\$6.5 bn in Q1 2010 while the number of announced deals dropped to 76 in Q1 2010 (Q1 2009: 91). Egypt, with 10 deals, Saudi Arabia with 8, and Qatar and Jordan with 4 each recorded the maximum number of deals while Qatar attracted 39% of total deal values in the region, followed by Lebanon (\$450 mn) and Saudi (\$381.4 mn).

- The GCC investor confidence, reported by Shuaa Capital, fell – for the second time in a row – 5.7 points to 107.4 in May. Oman and KSA dropped moderately to 107.3 and 123.6 points respectively, while Kuwait (97.9) and Bahrain (98.6) indices moved below the threshold 100 points implying overall negative sentiment.
- Oman's revenues during the Jan-Apr 2010 registered a rise of 42% yoy to OMR 2.9 billion, boosted by oil and gas revenues reaching OMR 1.9 bn and OMR 304.1 mn by April respectively.
- The appetite for Sukuk is still strong: investors from the GCC, led by Islamic Development Bank subscribed to the \$1.25 bn Sukuk al-Ijara issued by the Malaysian government priced at US Treasury 5-year plus 180 basis points with yields touching 3.928% to be distributed on a fixed-rate basis annually.
- Inflation in Saudi Arabia rose to 5.4% in May (Apr: 4.9%) – the highest level since May 2009 – due to an increase in food prices and rents. Rent, fuel and housing-related services rose 9.4% yoy in May (Apr: 1.1%) while the food and beverages index was up 5.4%.
- A Doha based daily reported that Qatar's Public Works Authority plans to implement infrastructure projects worth \$20 bn in the country over the next five years, with local companies awarded 30% of the projects' value.
- Saudi Arabia's Central Department of Statistics & Information revised upward data for 2009 real GDP growth: +0.6% yoy from 0.2% earlier; oil sector contracted 6.7% (6.4 %) while the private sector grew 3.5%.

UAE Focus

- Dubai consumer prices rebounded in May, rising 0.78% mom, after falling for six months, boosted by rising housing costs and food prices.
- Moody's stated that asset quality among UAE banks will

remain under pressure this year. Dubai World's recent restructuring is essential to determine the asset quality challenges to the UAE banking system.

- UAE's oil export revenues for Jan-May 2010 rose to \$28bn from \$16 bn in the corresponding period last year according to figures released by the US Energy Information Administration. The figures place UAE as the third largest earner in the 12-nation OPEC after Saudi Arabia and Iran.
- The UAE Central Bank Governor was quoted saying that the UAE is likely to grow at about 4% this year and next.
- UAE's six airports are expected to handle 41.7 million passengers by 2020 (current level: 26 mn), according to the projections by the General Civil Aviation Authority. Flight movements in the UAE are projected to grow at about 6.0% annually to touch about 997,000 by 2020.
- UAE's Minister of State for Financial Affairs announced that the government would be issuing several new laws, compiled by the MoF in co-operation with the Securities and Commodities Authority, the Central Bank and the Insurance Authority, to regulate the UAE's financial sector and reform the bankruptcy code.
- Dubai's non-oil trade was up 19.0% yoy to AED 136bn in Q1 2010 according to Dubai customs.