

# Weekly Economic Commentary – July 03, 2011

## Markets

Equity markets got some respite due to strong US data and cheerful news from Greece especially the “voluntary rollover” accepted by French banks and the austerity program passage in Athens. The mini end of month rebound & reappearance of risk appetite does not alter the outlook much, which remains dominated by a downward trend. The euro surged on positive news from Greece while the pound dropped to a 16-month low against the euro. The Brazilian real is at a 12-year high against the dollar as foreign investors flock to the region, given its high interest rates. Oil rebounded after the IEA stock release effect waned, while gold seems to have topped for now.

## Global Developments

### Americas:

- The IMF revised down the forecast for 2011 US GDP to 2.5% with increasing downwards risks.
- May consumer spending remained flat and Apr was revised down, confirming downside risk to Q2 GDP.
- S&P Case Shiller Home Price Index gained 0.7% mom in April, recording the first such increase since Jul'10. May pending home sales rose 8.2% mom (Apr: -11.3%), the strongest monthly increase since Nov.
- US initial jobless claims fell slightly by 1k in the week ended Jun 18 to 428k.
- ISM manufacturing survey rose in June to 55.3 (May: 53.5) with the increase across the board: new orders to 51.6 (51.0) and employment improving to 59.9 (58.2).

## Europe:

- Germany's provisional inflation figure for June was +0.1% mom (2.3% yoy) as the effects of higher energy prices abates.
- The Greek Parliament approved by a narrow majority the new austerity package, a pre-condition for the disbursement of IMF and EU funds.
- Eurozone PMI manufacturing dropped to an 18-month low to 52.0 in June (May: 54.6), as both exports and domestic demand slowed. Italy's manufacturing sector shrank for the first time in 20 months, while Spain's contracted for the second month in a row alongside slowing growth in both the German and French sectors.
- Eurozone unemployment rate held steady at 9.9% in May, with the highest rate recorded in Spain: 20.9%.

## Asia and Pacific:

- China announced, for the first time, an estimate of local government debt at the end of 2010, totalling some CNY 10.72 trillion (26.9% of 2010 GDP), with 46.4% of the debt held by intermediary vehicles called local government financing platforms.
- Japanese industrial production rose 5.7% mom in May (Apr: 1.6%), the most in almost 60 years pushed up by a rise in output in automobiles (69.8%) and communications devices. Growth was across the board with output from the quake-affected areas rising 18.8% compared to 4.5% increase in non-quake-affected areas, as manufacturers restore supply chains damaged by the earthquake and tsunami in March.
- South Korean IP rose for the 23rd straight month, to 8.3% yoy in May.
- Taiwan central bank raised rates by 12.5bps, to rein in inflation, taking the rediscount rate to 1.875%.
- Inflation in Thailand and Indonesia eased in June to

4.06% and 5.54%, compared to 4.19% and 5.98% respectively in May; in month-on-month terms, food prices steadily increased. Inflation in South Korea meanwhile hit a 3-month high of 4.4%, with core inflation surging to the highest level since May'09.

- Japan's Tankan index fell to -9 in the three months to June (Mar: +6), recording the first negative reading in five quarters, reflecting a worsened sentiment in the aftermath of the earthquake and tsunami.
- China PMI fell to 50.9 in June (May: 52.0), still slightly above the 50 mark, largely due to inventory adjustments. The manufacturing sector expanded at its slowest pace in 28 months, with the cost of materials declining by 3.6%-pts mom, while the new orders index, which reflects domestic demand, fell 1.3%-pts.

## **Bottom line:**

Looking back at the first half of 2011 one cannot avoid a sense of déjà vu: banks trying to raise capital to pare losses, widespread macroeconomic weakness, dismal labour markets, a retrenchment of commodities prices after a spike, stock markets pausing after two years of euphoria and hawkish statements from the ECB fighting a rear guard battle. In 2008 the crisis propagated from financial institutions, in 2011 it stemmed from sovereign debt. The difference is only apparent. A sovereign default will wipe out the capital of several banks, and weaken the balance sheet of many other including in the US through higher counterparty risk and interconnectedness effects, while European pension funds will be severely hit.

## **Regional Developments**

- In the region, DFM fell to a 3-month low last week while Saudi and Qatar gained.
- Kuwait's Supreme Petroleum Council has approved two

long-stalled oil mega projects worth more than KWD 8bn dinars (USD 29 billion).

- Kuwait's parliament passed the budget for 2011-12, with an estimated KWD 6bn deficit, given the 11% rise in spending projected at KWD 19.44bn mostly to meet pay hikes and grants for Kuwaitis, which will grow consumption and leak into increased imports.
- OPEC's Secretary General called for the IEA to halt the oil reserve release.
- Bahrain has initiated a national dialogue, in the aftermath of the protests and social tensions in the past months, in an attempt to focus on political, economic, social and rights issues.
- According to a recent report by the World Travel and Tourism Council, Oman's tourism sector is estimated to contribute USD 1.93bn in 2011, close to about 3% of GDP.
- The Central Bank of Oman's Annual Report showed that personal loans, including mortgages, comprised 40% of banks' total credit portfolio and grew 6.8% to OMR 4.29bn in 2010.
- Qatar's May inflation edged up to 1.7% yoy (Apr: 1.5%), largely on a 0.4% rise in transport and communications, which comprises 20.5% of the overall CPI.

## **UAE Focus**

- An official document reported that the UAE plans no Federal sovereign bonds before 2012.
- The UAE will provide three-year multiple entry visas to all foreign investors who own property, in a bid to revive the real estate market.
- UAE's 2011 budget has been increased by AED 540mn, with the additional amounts AED 105mn and AED 150mn set aside for health and universities respectively.
- The capital of Emirates Petroleum Corporation was increased by 50% to AED 9bn, allowing the retailer to obtain more bank loans and offset the losses arising

from petrol subsidies.

- Dubai Government departments have demonstrated support to SME businesses by providing procurement contracts worth over AED 40mn in H1 2011 according to DED.
- MIGA announced that is mobilising USD 1bn for insurance cover in MENA countries to spur investments in the region.
- The BIS has invited the UAE central bank to become a member, according to Bloomberg.
- Etihad Rail has awarded a major railway project contract worth AED 40bn, that will eventually link the major cities and towns of the UAE.