Weekly Economic Commentary – March 04, 2012

Markets

The upward trend is gaining ground so even those who are skeptical of its sustainability are forced to join in because their performance is judged against a market benchmark. The wave of optimism swept also the regional markets: Dubai touched a 1-year high while the Saudi market closed yesterday at the highest since Sep 2008. The euro continued to fall against the dollar due to ECB's injection while the dollar strengthened to a nine-month high against the yen. Gold prices were spooked by the lack of enthusiasm displayed by Bernanke for QE3, and closed on a low from a week ago while oil prices rose to the highest since mid-2008 as rumours of a pipeline blast led to a rush in buying.

Global Developments

Americas:

- US **Q4 2011 GDP** was revised up to 3% qoq ann from an initial estimate of 2.8% (Dec: 1.8%), the quickest pace since Q2 2010. Adding to the stream of upbeat data, the **Chicago PMI** recorded a 10-month high at 64.0% in Feb (Jan: 60.2%) and consumer confidence surged to a 12-month high in Feb at 70.8 (Jan: 61.5), indicative of a possible increase in spending for the upcoming months. However, the need for cautious optimism is signalled by the **Personal Consumption Expenditure**(PCE) which saw a mild increase of 0.2% mom in Jan (Dec: +0.1%).
- In his testimony to Congress, Bernanke, despite noticing the labour market uptrend, stressed that the fundamentals supporting consumer spending "continue to

be weak". Still the Fed Chairman did not hint to an imminent QE3.

- The **Pending Home Sales** Index, based on contracts signed in January, increased 2% to 97.0 – the highest since April 2010. The **S&P/Case-Shiller Home Prices** Index ended 2011 at its lowest since mid-2006, falling 4% yoy in Q4 (Q3: -3.7%) and 3.8% qoq, a sign that no recovery is in sight.
- US **durable orders** declined sharply in Jan by 4% mom (Dec: +3.2%) following the expiration of a tax break allowing full depreciation on equipment purchases. The drop was led by a contraction in demand for capital goods of 4.5% mom.
- **ISM manufacturing** index fell to 52.4 in Jan (Dec: 54.1) as the new orders declined to 54.9 (57.6), while export orders climbed.
- Initial **jobless claims** decreased by 2k to 351k, sa, from the previous week's revised 353k. The 4-week moving average dropped to its lowest levels since March 2008, falling 5.5k to 354k.

Europe:

- The second long term refinancing operation arranged by the ECB for Euroland's bank amounted to EUR 530 billion and is expected to boost credit to companies. The first operation was barely sufficient to compensate for the assets losses and the deposits drop. Buba's Wiedeman balked at this newly printed money flood asking for a revision in TARGET which allows central banks to settle their positions and extend credit to each other.
- Greece's debt was downgraded again – by S&P and Moody's to selective default. Markets showed no reaction.
- **Eurozone Inflation** was 2.7% yoy in Feb, up from 2.6% in Jan. Even **German CPI** rose in Feb to 2.3% yoy (Jan: 2.1%) due to energy prices.
- **Spain's budget deficit** exceeded all pessimistic

estimates at 8.5% of GDP for 2011shattering the possibility of meeting the 2012 target of 4.4%.

- The **euro-zone PMI** index crawled to 49.0 in Feb (Jan: 48.8), indicating a slower contraction in the manufacturing sector. French PMI rose to a seven-month high to the 50 mark, while Spanish and Greek PMIs were in the contraction territory at 45.0 and 37.7, respectively.
- **German retail sales** dropped in Jan by 1.6% mom, sa (Revised Dec: +0.1%), as the mild winter discouraged purchases of winter clothes.
- **Eurozone unemployment** hit a record high of 10.7% in Jan while the Dec figure was revised upwards to 10.6% from the previously reported 10.4%.

Asia and Pacific:

- **Chinese PMI** increased to 51.0 in Feb (Jan: 50.5) as both new orders and export orders accelerated to 51.0 and 51.1, respectively.
- Internationalisation of the Yuan is moving ahead: the PBoC announced that all firms in the country would be henceforth allowed to invoice or pay for cross-border transactions in the Chinese currency.
- **Indian Q4 2011GDP** grew at its slowest pace in almost three years at 6.1% yoy (Q3: 6.9%), a result of high interest rates, a hike in oil prices and a slowdown in global demand.
- **S. Korea Jan current account deficit** was USD 772.2 mn (Dec: USD 2.81 surplus), first deficit since Feb 2010, due to a slowdown in exports to the Eurozone and the Lunar New Year holiday. **Industrial production** was up 3.3% mom, sa (Dec: -0.7%) but fell 2.0% yoy (Dec: 2.8%).
- **Japanese industrial production** in Jan surged 2% mom (Dec: 3.8%), the largest contributions coming from transport equipment (3.3%), telecommunications (12%), and iron & steel production (5.9%). Construction orders

jumped by 24.5% yoy (Dec: 1.5%).

- **Retail sales in Japan** rose by 1.9% yoy in Jan (Dec: 2.5%) on the back of a surge in motor vehicle sales of 24.3% yoy following a 14.9% yoy increase in Dec. Housing starts fell by 1.1% yoy (Dec: -7.3%), declining for the fifth consecutive month.
- **Thailand's inflation** slowed to 3.3% yoy in Feb (Jan: 3.4%) in spite of higher food prices while Indonesia's was 3.6% yoy (Jan: 3.6%).
- **Philippines Central Bank** cut the policy rate by 25bps to 4.00% – for the second time this year citing the "benign inflation outlook".
- **North Korea** agreed to suspend nuclear tests, long-range missile launches and activities at a nuclear facility in an unexpected move that represents a surprise diplomatic breakthrough and a major ease of tensions along the 38th parallel.

Bottom line:

A constant theme throughout the past 15 years has been the link between asset prices and liquidity injections from the central banks. The latest rally is no exception. With the second LTRO by the ECB, markets are celebrating another dose to satisfy their addiction. But on the macroeconomic front there are still very few hints of a solid recovery if one excludes the US labor market.

Regional Developments

- Ernst and Young estimates that about 15 million young people would enter the labour force in the next 10 years (average annual growth of 2%), from the economies of Egypt, Qatar, Saudi Arabia and UAE.
- **Mergers and acquisitions in the Middle East** continue to dip in 2012: total value in Feb was only USD463mn from Jan's USD 2.64bn, an 82% decline and compares to USD

1.18bn a year ago. Transaction volumes were also lower: down 60% mom and 73% yoy.

- **Saudi Arabia's** exports increased by 37% and reached SR 1.29 trillion in 2011, while SAMA's (Saudi Arabian Monetary Agency) reserve assets exceeded SR 2 trillion. Growth rates of credit to private sector doubled, and monetary aggregates also surged in 2011, indicating risk of growing inflationary pressure in the future, while current inflation remains relatively flat at the level of 5.3% (in January 2012).
- **Qatar's** nominal GDP in 2011 grew by 48.6% to reach QR628bn (USD 172bn) majorly due to the growth of hydrocarbon prices.
- **Oman's nominal GDP** increased 23.3% yoy to OMR 20.07bn by Sep 2011, thanks to a 34.9% jump in oil activities (as the average oil price stood at $102.96 against $76.58 a year ago) and a slightly lower 13.1% hike in non-oil sectors. Industry recorded an 18% growth and services 11.5%.
- Oil prices led to higher revenues, enabling **Oman** to report a large **fiscal surplus** of OMR 1.16bn in Jan-Nov 2011, compared to a fiscal deficit of OMR 287.4mn a year ago. Public expenditure rose 19.5% to OMR 7.6bn though current spending grew faster at 18.9% than capital at 10.3%.
- Forbes, in its list of richest countries, placed Qatar on the top spot – with a **per capita income** of USD 88k (adjusted for purchasing power parity)- while UAE was at 6th ($47.5k) and Kuwait at 15th.
- **Saudi Arabia**'s Foreign Minister has reaffirmed that it would honour its pledge to provide **Egypt** with USD 3.75bn in **aid**, of which USD 500mn already disbursed to the Central Bank in May last year.
- According to Alkhabeer Capital of **Saudi Arabia**, country's GDP growth in 2012 is expected at the level of 4.6% – the second highest in the GCC area after Qatar, where GDP growth rate may reach 7%. Experts anticipate

2012 inflation in Saudi Arabia below 4%.
- **Oman** to set up Association of Banks – an independent body to represent the interests of Omani banks at local and international levels. The association will support transformation towards more transparency through the promotion of internal and international banking rules.
- Gulf News reported measures undertaken by Muscat Sultan to strengthen judiciary independence in **Oman**, where governmental influence on Supreme Judicial Council's decisions was limited after the changes in the membership of the council.
- Central Bank of **Oman** released the results of its regular certificates of deposit tender: the total amount allotted was RO322 million, maturity – 28 days, average interest rate – 0.08%. It is considered that banks' excess liquidity absorption by the central bank allows maintaining stability of interest rates and money market in Oman.
- **Turkey's trade deficit** narrowed to USD 7 bn in Jan (Dec: USD 8.1 bn), falling for the third consecutive month. Exports rose by 8.6% yoy, while imports saw a smaller gain of 2.8% yoy, despite a 26% increase in energy imports annually.

UAE Focus

- The hike in **public sector wages** in the UAE last year, which ranged between 35-100%, is likely to add around AED 3.4bn to the Federal budget every year, according to the director general of the Ministry of Finance.
- Some good news on **Dubai debt**: DEWA has announced that it will repay debt of AED 1.2bn this year, before the date of maturity while Drydocks World's new terms for its USD 2.2bn debt will be discussed bankers this week with the aim to complete in July "all aspects of its restructuring".
- The UAE is set to allow ownership by foreign companies

in selected areas of the economy, according to the CEO of the Stocks and Commodities Authority. This was in response to a question whether foreign ownership limitations had led to MSCI’s decision not to reclassify UAE, to which he had answered in the negative.

- Venture Middle East reported that the value of c**urrent construction projects in the UAE** was close to USD 1.25 trillion and that about USD 15.068bn worth of contracts would be awarded this year – a growth of 26.57%.
- Hotels in Dubai outperformed other MENA markets in the month of January, according to a survey by TRI Hospitality Consulting. Occupancy rates for four and five star hotels reached 87.7% as a result of an influx of tourists during the city’s 17th Dubai Shopping Festival (DSF). In line with this data, Dubai International Airport reported a 14% increase in passenger traffic for Jan, bringing the total to 4.85 mn passengers.