

# Weekly Economic Commentary – March 25, 2012

## Markets

A tumultuous week for global **markets**: markets were on a roller-coaster last week, having touched close to 8-month highs, but were spooked by the decline in Chinese manufacturing data only to rebound on Friday. Among regional markets, **Saudi** and **Oman** were the biggest gainers as in the latter, talks of a potential merger between HSBC Holdings' local unit and Oman International Bank lifted shares. The **euro** closed at a three-week high against the dollar while **gold** recorded a fourth consecutive weekly loss, in spite of recording the biggest one-day gain in a month. Concerns about Iran continue to affect oil prices, with **Brent** closing at USD 125.13 on Friday.

## Global Developments

### Americas:

- **Housing starts** slipped 1.1% mom in Feb to 698k (Jan: 706k), while building permits rose 5.1% to 717k (682k), indicative of increased housing activity in the coming months.
- Existing **home sales** slipped slightly by 0.9% mom in Feb to 4.59mn (Jan: +5.7%, 4.63mn), but outperformed sales from a year earlier, up 8.8% yoy, the strongest in five years. Feb new home sales unexpectedly fell 1.6% mom to 313k, adding to concerns on global growth, though rising 11.4% yoy.
- **Initial jobless claims** dropped 5k to 348k for the week ended Mar 17, the lowest since March 2008. The 4-week moving average also recorded a 4 year low, slipping to

355k.

## Europe:

- Flash **manufacturing PMI** for France and Germany fell to 4-month lows of 47.6 (50.0) and 48.1 (50.2), respectively, in March. Eurozone Manufacturing PMI was at 47.7 (Feb: 49.0) – a 3-month low as composite PMI declined to 48.7 (49.3).
- **UK retail sales** slipped further than expected by 0.8% mom in Feb (Jan 0.3%), but were up 1% yoy. The largest declines were seen in clothing and footwear (0.4%) and food sales (0.1%).
- **UK inflation** continued its steady fall since Sep 2011, coming in at 3.4% yoy (Jan: 3.6%), its lowest since Nov 2010. The retail price index also eased for the month at 3.7% yoy (Jan: 3.9%).
- The **UK Budget** announcement included an income tax rate cut from 50% to 45% from April 2013 and an immediate corporation tax cut of 1% to 24% from April. UK's budget deficit is expected to reach 5.8% of GDP in the next fiscal year.
- The Eurozone faces strong opposition from Germany in an attempt to raise the combined lending power of the **EFSF** and **ESM** to EUR 700bn from EUR 500bn, intended as a measure to pacify markets and G20 leaders before the upcoming April meeting.
- Retail sales in **Italy** rose 0.7% mom, sa in Jan (Dec: -0.8%) on a 1.2% jump in food purchases, but slipped 0.8% yoy (Dec: -3.7%). Meanwhile, **industrial orders** saw a sharp decline in Jan at 7.4% mom (-5.2%).

## Asia and Pacific:

- Flash China **manufacturing PMI** came in at 48.1 for March – from Feb's four-month high of 49.6 – indicating a further contraction. Output and employment in the sector

declined, after expanding in the previous month and new orders shrank at a faster rate.

- China, the world's largest oil consumer, hiked **fuel prices** for the second time in 2012, raising the benchmark retail price for petrol by USD 0.7 per litre, the biggest rise in three years.
- The **Reuters Tankan** manufacturing sentiment index for Japan rose to +2 in March (Feb: -11), the first positive reading in four months.
- **Japan** posted its first **trade surplus** in five months at JPY 32.9bn in Feb (Jan: JPY 1.5trn deficit), as external demand strengthened – especially the auto industry, with its exports to US rising by 26.9% yoy.
- **Malaysian** CPI saw a 2.4% yoy increase in Feb (Jan: 2.7%), led by an increase in food & beverages of 2.9%, and remained unchanged from Jan 2012. **Singapore's** inflation numbers for the month of Feb came in higher at 4.6% yoy (Jan: 4.8%), owing to increases in housing (9.5%), food (2.6%) and transport (4.4).
- **Taiwanese export orders** rose 17.6% yoy in Feb (Jan: -8.63%), attributed to stronger demand from the US and China and a low base effect as the Lunar New Year fell in February last year. Industrial production recovered partially in Feb, rising 8.4% yoy (Jan: -16.75%).
- The **central banks of Taiwan and Thailand** left key rates unchanged, citing inflation as a key concern for both the East Asian economies on account of higher oil prices.

## **Bottom line:**

The decline in Chinese and European **PMI** hogged the limelight last week, bringing back global recovery concerns, even overshadowing the positive news on the US job front. **Oil** continues to be a talking point, with the IMF's Chief stating that prices could surge 20-30% if there is a supply disruption via Iran's exports while Saudi's Oil Minister remained

confident of meeting any shortfall in the market; he mentioned the possibility of raising output to full capacity of 12.5bn barrels per day as opposed to 9.9mn bpd currently. Meanwhile, as the US Republican primaries continue without a clear frontrunner, **bond auctions** in Italy and Spain along with the meeting of European Finance ministers are crucial for EU sentiment this week.

## Regional Developments

- While verbal interventions by **Saudi** officials added to oil prices stabilization last week, **IMF** Managing Director revealed Fund experts' estimates of oil prices potential surge by 20 to 30% in case of global oil supply shortage due to rising tensions around Iran.
- The **GCC** is studying the possibility of introducing a multi-currency real-time payment system, in line with the vision for the Gulf Monetary Union.
- **Egypt's** central bank cut reserve requirements on local deposits to 12% from 14%, but left its benchmark lending rate unchanged at 10.25% on account of mild inflation. Meanwhile, the **IMF's** visit to Egyptian authorities did not result in any agreement regarding the USD 3.2bn loan – as the government has not yet provided a concrete plan regarding the dissemination of these funds.
- **Kuwait's** 2012-13 Budget amounting to KWD 22bn estimates a spending increase of 13% over the current year's budget. Although revenues are estimated at KWD 14bn, implying a budget deficit, the projection is made using an oil price of USD 65/barrel. Kuwait is likely to post a budget surplus if oil prices continue to remain high.
- Despite the administrative measures undertaken by the **Kuwaiti** official agencies, prices of some of the food items on the local markets increased more than twice as a result of the strike held by the Customs employees. The strikes by country's public sector workers was discussed by the Parliament of Kuwait, which decided to

form a joint committee of the officials from legislative and governmental bodies to study draft laws on salary increments.

- **Arcapita**, whose biggest creditor is the Central Bank of **Bahrain**, filed for bankruptcy in the US over its USD 1.1bn debt, as its restructuring talks failed – causing a 12bps rise in Bahrain 5-yr CDS to 370 on Monday.
- According to Global Investment House, increased budgetary expenditure associated with the measures aimed at infrastructural development and coping with the consequences of the global financial crisis led to **Bahrain's public debt** to GDP ratio growth from 8.5% in 2008 to 27.6% in the end of the first half of 2011, which however remained below the 60% ceiling set by the Gulf Monetary Union.
- Capital Market Authority of **Oman** promoted the idea of a minimum capital increase for the new insurance companies. The measure is intended to strengthen local insurance sector's competitiveness and ability to retain more companies within the country, while mergers are seen as a reasonable approach for local companies to benefit from economies of scale.
- Unemployment in **Saudi Arabia** is close to 10.5%, equivalent to 500k persons looking for work, according to the Labour Minister. He also stated that there were 9 foreign employed workers per unemployed local person in the country.
- Moody's reported that **GCC banks** were likely to face short-term funding difficulties if there was a "sustainable retrenchment" by European banks in the region, given that European bank lending to the GCC region amounted to around USD 237bn as of Sep 2011.

## **UAE Focus**

- The UAE Minister of Economy reiterated that a **merger** of the Abu Dhabi Securities Exchange and the Dubai

Financial Market is still on the cards, expecting a decision to be reached by the end of the year.

- Dubai's **JAFZA** is proposing a three-pronged strategy to **refinance** its USD 2bn Sukuk maturing in November of this year, comprising a reduction in debt level of USD 191mn, a new bank loan of USD 1.09bn and the issue of a new Islamic bond worth around USD 653mn.
- **Mubadala** has unveiled plans to build a gas terminal in Fujairah that would allow oil & gas tankers to bypass the Strait of Hormuz, hence reducing risk of potential closure threat.
- UAE's **central bank** has directed lenders in the country to alleviate the debt burden of UAE nationals, instructing further study to find solutions. However, according to analysts cited by the Gulf News, extensive write-off of the loans of Emiratis bogged down in debts may deteriorate financial position of UAE based banks, and create bad precedents.
- UAE is arguing a strong case to be exempt from US **sanctions against Iran**, on account of its historic commercial ties with the country. Bilateral trade between Iran and the UAE amounts to USD 13.61 bn annually. This comes on the heels of a partial lift of sanctions for Japan and few European countries.
- **UAE** attracted about USD 1.8bn in **FDI** in 2011, compared to USD 8.64bn in GCC, according to Abu Dhabi DED's undersecretary.
- Dubai DED is planning to introduce instant business licenses, a '**120 days hassle free license**', which would substantially reduce the time taken to start a business as well as simplify the investment and business registration process.
- **Inflation** in the **UAE** fell by 0.44% mom and was up by 0.56% yoy in Feb – food and non-alcoholic beverages recorded an uptick, while among the Emirates monthly inflation in Abu Dhabi and Dubai declined amidst a rise in other emirates.