

Weekly Economic Commentary – April 29, 2012

Markets

Markets were volatile, though strong corporate earnings results overshadowed the soft data releases, especially the muted GDP growth in **US**, and the S&P downgrade of **Spain's** sovereign debt last Thursday. **Regional** markets were mixed, with Q1 profits announcements key; many UAE listed companies, including real-estate firms, announced better-than-expected earnings. The **US\$** weakened on soft US data though the **euro** held surprisingly strong in spite of the downgrade; the **pound**, meanwhile, hit a 22-month high against the euro. **Gold** prices were up and **EIA's** announcement that increased Saudi output helped global oil supply exceed demand by 500k bpd in Feb-Mar also led to some minor fluctuation in **oil** prices.

Global Developments

Americas:

- The **US** posted lacklustre **GDP** growth for Q1 at 2.2% yoy (Q4: 3.0%) on the back of a slowdown in inventory investment. Real personal consumption expenditure rising 2.1% qoq in the same period (1.3%).
- **Bernanke** said US monetary policy was “more or less in the right place” but the Fed is ready to launch another QE round if the economy falters.
- The **S&P/Case-Shiller** 10-City Composite Home Price Index slid for the sixth consecutive month, dropping 3.6% yoy in Feb 2012 (Jan: -4.1%). **New home sales** experienced a sharp decline of 7.1% mom (Feb: +7.3%), amounting to 328k units, saar, in March.
- **Durable goods** orders slumped in March 4.2% mom (Feb: +1.9%), a record since Jan 2009, due to a drop in demand for civilian aircrafts and parts.
- **Initial jobless claims** dropped by 1k to a seasonally

adjusted 388k. The 4-week moving average rose 6,250 to 381,750, the highest since Jan 7.

Europe:

- **UK GDP** in Q1 contracted 0.2% qoq after a 0.3% drop in Q4 2011, implying recession. Construction was the biggest drag with a 3% qoq drop.
- Flash **Composite PMI** for **Euroland** in Apr was 47.4 versus 49.1 in Mar, signalling that the recession in Europe is worsening. Flash **German** Manufacturing PMI came in at 46.3 in Apr (Mar: 48.4), contracting at the fastest pace since July 2009. The **French** index rose to 47.3 (46.7).
- **German inflation** eased mildly to 2.0% yoy in April (Mar: 2.1%) as energy prices rose at a slower pace.
- According to the ECB's Ewald Nowotny, the EU will never issue general obligation euro-zone bonds because Germany is opposed to this.
- **BIS** reported that in Q4 2011 **banks** cut lending to Italy by USD 68.5bn, to Spain by USD 54bn, to Portugal by USD 12bn and to Greece by USD 18.6bn.
- **S&P cut Spain's credit rating** to BBB+ on account of a dismal economic outlook and the current state of its budget deficit, down two notches from A. Spanish **unemployment** hit 24.4% in Q1 2012 (Q4: 22.9%), reinforcing the S&P downgrade. Inflation accelerated to 2% in Apr (Mar: 1.8%).

Asia and Pacific:

- **S&P** changed the outlook for **India** to negative and threatened to downgrade its sovereign debt unless the widening fiscal deficit, currently at 6% of GDP, is brought under control. Fiscal discipline however is sapped by a political gridlock which makes it impossible to reduce subsidies and modernize tax collection.
- **China's** Flash HSBC Manufacturing **PMI** rose to 49.1 in Apr (Mar: 48.3), indicating a contraction in the sector, but

at a slower rate.

- The National Consumer **Price Index** in **Japan** saw a mild 0.5% yoy increase in March (Feb: 0.3%), while its **unemployment** rate came in flat at 4.5%. Japanese **construction orders** were down 0.3% yoy in March (-1.8%), rising 7.1% for the whole of FY2011. **Housing starts** were up 5% yoy for the month (7.5%). Bank of Japan left interest rates unchanged at 0.1%.
- **Japanese IP** rose 1% mom (Feb: -1.6%), surging 13.9% on a yoy basis, while **Thai IP** fell 3.2% yoy and **Singapore's** dropped 3.4% yoy (Feb: +11.8%), but rose 2.7% mom.
- **South Korean GDP** rose 0.9% qoq and 2.8% yoy during Q1 2012 (Q4: 0.3% qoq & 3.3% yoy) as manufacturing and exports (+3.4% qoq) expanded, but was weighed down by the 0.7% qoq drop in construction investment.
- **Taiwanese Industrial Production (IP)** fell 3.42% yoy in Mar led by a 3.77% drop in manufacturing.
- **Singapore's** March CPI **inflation** accelerated to 5.2% yoy from 4.6% year in Feb, led by higher costs of housing (+9.1%) and transport (+8.6%).
- **Thailand's trade deficit** in Mar ballooned to USD 4.6bn as imports surged 25.6% yoy and exports decreased by 6.5% yoy. Thai Capacity Utilization for the month increased to 68.1, from Feb's 62.5.

Bottom line: The week was a mildly worrisome on the macro front: soft GDP data from **US** and **UK** in recession, S&P action on **Spain and India**, but equities held strong on company profit announcements. **Politics** could play havoc as **Greece and France** prepare to go to polls next week; meanwhile, Romney is de facto anointed as the Republican nominee; Sarkozy is trailing the Socialist challenger Francois Hollande; in Egypt, the Presidential candidates have been announced, with 13 names including that of former Prime Minister Ahmed Shafiq.

Regional Developments

- The **IMF Regional Economic Outlook** forecasts growth at

4.2% for MENA, higher than previously expected (see addendum below) but with divergent trends between oil exporters and oil importers.

- **Funds** managed by the Gulf's roughly 100 asset management companies totalled USD 26.5bn, in about 328 funds at end 2011, according to a report by Markaz.
- Ernst and Young reported a 40% yoy decline in value of **mergers and acquisitions** to USD 8.5bn in the MENA region in Q1 2012 while the number of transactions was up 7% to 105. Top 10 deals accounted for 85.5% of the regional total while UAE, Qatar and Saudi Arabia accounted for 78% of total announced domestic deals in the region.
- Citigroup reports that Saudi Arabia tops the market for **construction** in MENA with USD 750bn of new projects in the pipeline, making up 31% of the regional market.
- UNCTAD reported that of the total USD 284bn in **FDI** received by the Arab nations between 2001 and 2010, close to 60% was received by the GCC nations. Of these Saudi Arabia topped the list with USD 154bn, followed by UAE and Egypt at USD 75bn and USD 53bn respectively. The bulk of FDI went to energy and telecommunications.
- An agreement in principle to increase of **customs tariffs on cigarettes and tobacco imported by the GCC** states from 100% to 200% may be approved during the meeting of finance and health ministers of the Council, scheduled for May 2012, according to a senior Saudi official.
- At the **monthly auction** of **Bahraini** Government's 91-day Sukuk Al Salam Islamic Securities, held by the Central Bank of Bahrain, the total issuance of BHD 18mn was oversubscribed by 232%; expected return amounted to 1.18%.
- **Kuwait's** Central Bank released its monthly bulletin for March: **monetary** aggregate M3 increased 7.8% yoy to reach KWD 29.0bn; growth rate of private sector deposits at the local banks, which amounted KWD 27.97bn, was 7.4% yoy; local banks' claims on private sector grew at a slower pace of 3.5% yoy; average interest rate on 12-

month customer time deposits at the local banks was 1.63% for KWD, and 0.77% for USD.

- Growth of food prices was the main driver of **inflation** in **Kuwait**, where CPI increased to 4.1% yoy in March from 3.8% yoy in February.
- **Oman** is in the process of setting up a new Small and Medium Enterprises (**SMEs**) Development Fund with an initial capital of OMR 100mn provided by private sector pension funds, financial institutions and a few large business groups.
- The **Omani Ministry of Transport** signed 11 agreements worth OMR 158.4mn for road construction projects.
- According to a senior official of the **Qatari SWF**, its assets under management exceed USD 100bn, and it may invest around USD 30bn in 2012.
- **Turkey's** economy minister said his country could achieve 5% real **GDP** growth in 2012, while the IMF projections imply 2.3% growth for the current year. As for data releases, **Capacity Utilization** in Turkey increased in April to 74.7 from 73.1 in March.
- **Confidence indices** recently released by the statistics authority of **Turkey** improved markedly and demonstrate moderate optimism in Services, Retail trade, and Construction sectors: the indices for these sectors increased in April 2012 by 7.0%, 4.7%, and 3.7% to reach 110.1, 111.5, and 99.5 respectively (index value between 100 and 200 indicates optimistic outlook).

UAE Focus

- **Dubai's** USD 1.25bn **Sukuk**, to be issued in two tranches was oversubscribed by 3.5 times, with as many as 260 investors showing interest. The issue, expected "to manage budget deficits and refinancing plans proactively", is the first one after the previous successful tap into the market in June 2011.
- The prospectus issued alongside the Sukuk highlighted

that **Dubai** government's **budget deficit** fell sharply in 2011 to AED 3.7bn (2010: deficit of AED 6.0bn), in spite of an increase in actual government spending to AED 35.98bn as opposed to AED 33.68bn planned.

- **Arab Monetary Fund** estimates that oil prices boosted the **UAE's trade surplus** to a record level, USD 86.2bn in 2011, while the current account surplus surged above 10% of GDP.
- The **UAE Central Bank** announced an increase in **banks' assets** by AED 38bn in Jan-Feb 2012 to touch AED 1.7 trillion as of end-Feb. Loan to deposit ratio fell to 96.6 in Feb, from just above 100 in Dec 2011.
- **Abu Dhabi's real estate transactions** totalled AED 43bn in 2011, up 5% yoy, according to Abu Dhabi Municipality. Meanwhile, CB Richard Ellis reported that rents were down 3.5% qoq and 18% yoy.
- The **IMF** stated that there were several **loans** in the pipeline to the Arab countries, without specifying the nations. In UAE, National Bank of Abu Dhabi announced a AED 1.0bn fund to revitalise the property market, with the plan to go public within two years.
- UAE **air traffic** in Q1 reaffirmed the role of transportation in contributing to the economy. In **Abu Dhabi**, passenger traffic increased by 21.2% yoy to 3.4mn passengers in Q1 and was up 22% yoy to 1.2mn in March alone. At **Dubai's** airports, March witnessed a 15.4% growth in passengers to 4.85mn.

Addendum: IMF MENA Regional Economic Outlook

The **IMF** issued its Spring 2012 Regional Economic Outlook for the MENA region. Growth in the MENA region is expected at 4.2% in 2012, to be followed by a lower rate of 3.7% in 2013. However, within the region, the **trends are quite diverse between the oil exporters and importers**, with the former expected to grow at faster rates (2012: 4.8%, 2013: 3.7%) than the latter (2.7%, 3.6%). Higher oil production and prices alongside expansionary fiscal policies have favoured the oil

exporters including the GCC. While internal political and social challenges continue to bog down growth in oil-importing nations, the negative impact on remittances, tourism and capital flows adds to their woes. Geopolitical risks, sanctions on Iran and spill overs from Europe (especially for the North African countries) are also high on the list of external challenges. Inflation, forecast at 10.0% in 2012 for the MENA region, is expected to decline to 8.9% in 2013. In the GCC, inflation is expected to stabilise around 3.8% this year, and as low as 1.5% in the UAE.

MENA countries are expected to post a **current account surplus** (+14.5% of GDP) in 2012 – though (again!) with a wide disparity between oil importers and the rest. The GCC's twin balances (fiscal and current) are forecast to be higher in 2012 compared to a year ago as the increase in oil exports and corresponding rise in fiscal revenues will offset expansionary government spending and imports. Very much like the two sides of a coin, where oil exporters gained, MENA's oil importers paid the price of higher oil prices; their combined current account deficit is estimated to be about 7.5% of GDP in 2012, coming off 2011's deficit of 7.3% of GDP. The further challenge for these nations, coming off a transition year, will be to consolidate fiscal spending.

The **short-term outlook is subject to unusually high uncertainties** as the "Arab Spring" political transformations unfold, with growing doubts surrounding external demand given the current political and security situation. Job creation in the public sector has meant an increase in government spending, and could exacerbate high unemployment rates as the private sector is crowded out. With limited fiscal space in transition countries, it is likely that there might be more requests for financial assistance. Closer home, strong trade ties with Iran are likely to cause concerns, if the nation's standoff with US continues.