

# Weekly Economic Commentary – June 10, 2012

## Markets

Inventories of cardio tonic drugs on trading floors must have been depleted, in one of the most feverish weeks in quite a while. The equity market roller-coaster was driven primarily by contradictory news on rescue plans for Spanish banks and expectations of more monetary stimuli in both the US and Eurozone. This was followed by the G7 teleconference, the Chinese rate cut, statements by Draghi and Bernanke, pressure from the US on Germany and the umpteenth downgrade for Spain. The S&P scored on Wed its biggest one-day percentage gain of 2012 and the following day China's surprise cut sparked another rally in global stock markets, with investors confident that Beijing will ride to the rescue of a global economy. Then Bernanke poured cold water on QE3. The oil price reflected these wild gyrations, ending near the lowest since Oct 2011 year and almost 25% below the high in Feb. Gold lost its shine slightly after Bernanke's testimony. The Euro overall fell and the Yen rebounded once again.

## Global Developments

### **Americas:**

- **US** manufactured goods **orders** fell -0.6% mom in Apr vs. no change in Mar, more or less as expected, but hardly a sign of robust performance.
- The service sector stabilized in May, with the **ISM non-manufacturing** index virtually unchanged at 53.7 from 53.5. Business activity and new orders gained, while inventory fell and employment stayed just above the threshold for expansion. More robust growth is not imminent.

- **Initial jobless claims** fell by 12k to 377k but the four-week moving average still rose to 377,750 – the highest in a month.
- **US Trade deficit** narrowed to USD 50.1bn in Apr (Mar: USD 52.6bn) as imports were down by 1.7% mom and exports fell for the first time in five months by 0.8% to USD 182.9bn, led by capital goods and industrial supplies. Trade deficit with China widened to USD 24.6bn (Mar: USD 21.7bn).
- **Brazilian inflation** slowed to 0.36% mom in May after 0.64% in Apr (5% yoy from 5.1% in Apr), as the economy remains well below capacity.

## Europe:

- The **ECB** left rates unchanged but hinted that it is ready to open the liquidity gate if the banking sector were to come under strain.
- After dragging its feet the **Spanish** government is bowing to the pressure to accept assistance for bank recapitalization. Spain requested a EUR 100 billion loan from the European Financial Stability Facility (EFSF) and the European Stability Mechanism (ESM). Fitch estimates Spanish lenders need EUR 50 to 60 billion in fresh capital.
- **Spanish IP** collapsed -8.3% yoy in Apr (after a -7.5% decline in Mar) led down by durables and capital goods. If you think this was bad news, it was still better than the performance in **Italy**, where **IP** dropped -9.2% yoy and -1.9% mom.
  - The sa annual growth of the **euro zone's M3** money supply slowed in Apr for the first time in four months: 2.5% yoy, down from 3.1% in Mar.
  - The euro zone business and consumer **confidence index** hit a two-year low of 90.6 in May from 92.8 in Apr. due to the deterioration in confidence of manufacturers and service providers. The fall in

the index underscores that the recession in the euro zone will continue.

- The euro area **GDP** remained constant qoq in Q1 against a -0.3% drop in Q4 2011. Compared to Q1 2011 GDP is 0.1% lower.
- Eurozone **PMI** reached a three-year low in May, with a dip in new orders: composite PMI fell to 46.0 (Apr: 46.7). Even in Germany services PMI fell (May: 51.8; Apr: 52.2) followed by France (May: 45.1; Apr: 45.2). In Italy, services PMI was slightly up (May: 42.8; Apr: 42.3).
- **German manufacturing orders** fell -1.9% mom in Apr (Mar: +2.2%). Foreign orders collapsed -3.6% mom hit by orders from euro zone. Domestic orders increased 0.4% mom. Orders are unlikely to pick up soon given the recession in the euro zone.
- **German IP** plunged -2.2% mom in April, offsetting the 2.2% gain in Mar. The index is well below levels reported in the summer of 2011. The German PMI has been below 50 for 3 months which means that over the summer a rebound is unlikely.

### **Asia and Pacific:**

- In an unexpected move to sustain growth, **China** cut interest **rates** by 25bps for the first time since 2008. The benchmark one-year lending rate will be 6.31% and the one-year deposit rate 3.25%. The stimulus from such a measure will be modest, but it signals that the authorities are on alert.
- **Inflation** in **China** fell to a two-year low of 3.0% yoy in May (Apr: 3.4%), the only positive amongst a host of weak data. Both **IP**, which increased by 9.6% yoy (Apr: 9.3%), and **retail sales**, up 13.8% yoy (Apr: 14.1%), came below expectations. Official non-manufacturing **PMI** eased to 55.2 (Apr: 56.1) while HSBC's services PMI was jumped up to a 19-month high of 54.7 in May (Apr: 54.1).

**China's foreign trade** rebounded in May with imports up 12.7% yoy (Apr: 0.3%) and a 15.3% growth in exports (4.9%). The surplus increased USD 300 ml to 18.7bn.

- **Japan's** current account balance dipped in Apr to JPY 334bn (Mar: JPY 1589bn) dragged down by higher energy costs and falling exports.
- **Taiwan** exports fell by 6.3% yoy, declining for the third consecutive month, to USD 26.1bn in Apr but grew faster compared to imports causing trade surplus to widen to USD 2.26bn (+83.9% yoy; Mar: USD 0.69bn).

**Bottom line:** 6 Eurozone countries (Greece, Ireland, Portugal, Spain, Italy and Cyprus) have wide fiscal gaps (the difference between the current government primary balance and one that would stabilize the public debt-to-GDP ratio) and large resource gaps (the difference between the current trade deficit and one that would stabilize the foreign debt-to-GDP ratio). As a consequence, government and external debts are unsustainable, especially if growth stalls and interest rates remain high. This is the good news. The bad news is that the US might be mired in the same situation, but the international role of the dollar is hiding this reality and postponing the day of reckoning, thanks to a flight to safety that keeps interest rates low. Meanwhile even the rare bright spots, Germany and China, are now struggling. The next few days will be again tense with the Greek and French parliamentary elections looming and Spanish banks negotiating a bailout from the Eurozone.

### Regional Developments

- Retrenching European **banks** have withdrawn almost USD 18.4bn from the GCC region in Q4 2011, according to **BIS** data, mostly from the UAE and Saudi Arabia. Also, loans by international financial institutions to borrowers in the Gulf, excluding interbank lending, fell USD 7.3bn in Q4. Deposits in the region, however, increased by 1.2% to USD 392.9bn, thanks to Qatar.

- Unemployment in **Bahrain** declined to 3.8% in Q1 2012 compared to 4% a year ago, according to the country's Ministry of Labour.
- At the auctions held by the Central Bank of **Bahrain** last week interest rates on 6-month and 1-year Government treasury bills declined, while remaining unchanged for 3-month securities. Total issuance amounted BHD 165mn, of which BHD 100mn for 1-year bills, which were oversubscribed by 193%. Average weighted interest rate on 3-month and 6-month bills was lower than that of 1-year securities (1.69%) by 50 and 40 basis points, respectively.
- Public capital expenditure on construction projects in **Kuwait** amounted to KWD 526.7mn, or 94% of the approved budget, in the fiscal year ending March 31, 2012, according to the Ministry of Public Works.
- According to the Central Bank of **Morocco**, monetary aggregate M3 increased 5.2% yoy in Apr, banking deposits by 3.1%, and lending to the economy by 7.2%. Net foreign assets of the Central bank and local banks declined 14.6% yoy, while net claims on Central Government increased 38.5%.
- Total value of projects implemented in **Qatar** may increase to USD 108bn in the next few years from the current USD 63bn, according to the country's financial centre.
- Real GDP growth in **Saudi Arabia** in Q1 2012 was 5.94%, slightly lower than 6.64% observed in Q4 2011. Nominal GDP was up 16% yoy to SAR 612.3bn. The oil sector, which expanded by 7.17%, while the private sector grew 6.33% and government sector grew 4.24%. Inflation rate rose to 5.1% yoy in May 2012.
- **Saudi Arabia** could rein in oil sales after it achieved its target of USD 100 by cutting the price of its crude and pumping at the highest rate in at least three decades. According to Vienna-based researcher JBC Energy GmbH citing tanker data oil shipments from KSA are lower

this month. Furthermore KSA raised the July official selling price to Asia of its Arab Light, for the first time in three months. Oil production was cut to 9.8mn (bpd) in May reducing output by 300k bpd from the previous month.

- **Saudi Arabia** agreed to extend another USD 430mn loan to **Egypt** in addition to USD 1.5bn provided earlier. The new loan is expected to support infrastructural projects and SMEs.
- Monetary aggregate M4 in **Tunisia** increased by 11.6% in Jan-Apr 2012 to reach TD44.7bn, while net foreign assets declined by 47.2% during the same period, or by TD 4.3bn in absolute terms.
- Year-end inflation in **Turkey** is expected to reach 7.47% according to the survey of decision makers conducted by the Central Bank twice a month. This month's first assessment is lower than previous one by 0.19 percentage points. This is in line with the current trends in actual inflation, which declined from 11.14% yoy in Apr 2012 to 8.28% yoy in May 2012, and country's Minister of Economy expectations of further inflation slowdown.
- **Turkey** aims at expanding its annual trade turnover with Arab League Countries to USD 100bn in the next five years from USD 35bn in 2011, according to the country's Minister of Science, Industry and Technology.

## **UAE Focus**

- **DIFC Investments** (DIFCI) secured a USD 1.03bn syndicated facility to help finance the repayment of its USD 1.25bn Sukuk which matures on the 13th of June this year. The 5-year Islamic facility contains a commodity Murabaha and Ijarah tranches, was priced at 380 bps over EIBOR/Libor, and secured on DIFCI's Grade A property portfolio. S&P affirmed its B+/B rating for DIFC Investments, with a stable outlook.
- UAE is expected to **grow** by 3.0% in 2012, according to

the Minister of Economy, citing the ongoing euro-zone sovereign debt crisis and weaker global growth as the main factors for the decline from 4.2% growth recorded in 2011.

- **Inflation** in **Abu Dhabi** increased 1.2% for the period Jan-May 2012, driven by higher prices of food and non-alcoholic beverages. In the month of May, CPI was up 1.7%.
- **Etisalat** could be going public, allowing foreign investors to own its shares, once a new draft law is approved (Source: *Emarat Al Youm*). If Etisalat becomes a public shareholding company, it might also result in the reduction of royalties the company makes to the government.
- The **Telecommunications** Regulatory Authority (TRA) announced that the number of **subscribers** in the UAE increased by 13% yoy to 12.4mn. Pre-paid subscribers, at 10.9mn, outnumbered the post-paid subscribers – 1.5mn, at the end of Mar 2012. With population at 8mn, **penetration** rate is now estimated at 154% as opposed to 200% previously with population closer to 5.5mn.
- UAE has been ranked 7th globally in **public sector financial management efficiency**, as per the World Competitiveness Report 2012. The report underscores the zero-based budgeting policy followed by the UAE in 2011-13 in “enhancing the efficiency of government spending and the preservation of public money”.
- The Securities and Commodities Authority (SCA) revealed that the **GCC’s IPO draft rules** have been approved (including unified disclosure of securities and unified corporate governance principles) and it has been submitted to the Supreme Council for endorsement and implementation.
- On the heels of the delisting of Damas on **Nasdaq Dubai** came the news that RegisCard is planning to list within the next 75 days. The company has “developed software to introduce prepaid debit cards and discount cards to the

international community”.

- **Etihad** acquired a 3.96% stake in Virgin Australia – its fourth acquisition in the past 6 months. With this collaboration, the two would operate 24 flights a week between Abu Dhabi and Australia, reaching over 150 destinations.