Weekly Economic Commentary – November 18, 2012

Markets

Equity markets were mostly lower, and recorded the second consecutive weekly dip, as the “fiscal cliff” and possibility of a global recession weighed in on investor sentiment. Newly announced elections however boosted **Japan**’s Topix as investors anticipate more central bank easing and stimulus spending under the new government. **Regional** markets painted a mixed picture while Saudi continued on a bearish trend, falling almost 2%. **Yen** weakness and continued sell-off was the order of the week after elections were called for Dec 16 while **euro** was down against the dollar. **Gold** prices were down again last week while **oil** prices were slightly up on tensions in the Middle East.

Global Developments

Americas:

- **Retail sales** fell for the first time in 3 months in Oct, **slipping 0.3% mom (Sep: +1.3%)**, dragged by a dip in automobile purchases. Retail sales excluding autos remained flat mom, suggesting heightened consumer caution in light of the looming fiscal cliff.
- **The Producer Price Index (PPI)** for finished goods rose to 2.3% yoy in Oct (Sep: 2.1%) but fell 0.2% mom in Oct (Sep: +1.1% mom). Core PPI, excluding food and energy, also fell 0.2% mom in Oct after holding steady in Sep, suggesting a stable inflation environment.
- **Industrial production unexpectedly fell** 0.4% mom in Oct after a revised 0.2% increase in Sep, but overall output was reportedly hampered by hurricane Sandy with an estimated impact of 1%. **Manufacturing output fell 0.9%**

mom (Sep: +0.1% mom) but remained stable after excluding the hurricane impact.

- **Small business optimism remained flat in Oct** with the NFIB index inching 0.3 points to 93.1. The percentage of business owners who are uncertain of short-term business conditions reached a record high.
- **Initial jobless claims** continued to be influenced by Hurricane Sandy as it increased by 78k to 439k last week.

Europe:

- **The euro area slipped into a technical recession in Q3** as GDP fell 0.1% qoq (Q2: -0.2%), the third consecutive quarterly decline, as contractions in periphery counties counteracted modest growth in Germany and France.
- **Euro area finance ministers and the IMF will give Greece up to 2016** to narrow its spending gap but postponed the decision to release the next tranche of its rescue package (31.5 bn euro) until their next meeting on Nov 20th.
- **Euro-area Industrial Production (IP) fell 2.5% mom in Sep** (Aug: +0.9%) and declined 2.3% yoy, led by Portugal and Ireland. Germany's IP fell 2.1% mom (Aug: -0.5% mom) underscoring the weakening regional economic situation.
- **Anti-austerity strikes** broke out in Spain and Portugal and labor unions in France, Italy and Greece planned demonstrations and strikes as part of a 'European Day of Action and Solidarity'.
- **The Bank of England downgraded its 2013 growth forecast to 1%** warning that GDP will stay below its pre-crisis level for 3 more years.
- **UK headline CPI rose to 2.7% in Sep** (Aug: 2.2%) driven by a rise in university tuition fees. The bank of England released its inflation forecasts expecting a decline beginning H2 2013 to reach the 2% target in 2014.

- **UK unemployment fell to 7.8% in Sep from 7.9% in Aug,** however the recent labor market improvement may be slowing as employment increased by 100K over the last 3 months as against +212K in the 3 months to Aug and jobless claims rose 10.1K over Oct.

Asia and Pacific:

- **Japan's economy shrank 3.5% (qoq ann.) in Q3** (Q2: revised down to 0.3% qoq ann.), the first decline in 2 quarters and the largest in magnitude since Q1 2011 when Japan's earthquake struck, spurring concerns of a recession. The decline was driven by a fall in exports (-18.7% qoq ann.) and private sector capex (-12.1 qoq ann.)
- **China Yuan credit supply** unexpectedly **slowed in Oct** as CNY 505.2bn of new loans were issued (Sep: CNY 623bn), undermining signs of a recovery. Similarly, M2 growth slowed in Oct to 14.1% yoy and fell 2.7% mom (s.a.a.r) (Sep: 27.8% mom s.a.a.r).
- **India's Industrial Production (IP)** fell 0.4% yoy and 2.2% mom in Sep (Aug: 2.3% and 1.6%, respectively) largely driven by a dip in consumer goods IP suggesting that **business investment activity remains weak**.
- **Weaker exports led to disappointing Q3 GDP data in Hong Kong and Singapore:** Hong Kong's economy grew by a less-than-estimated 1.3% yoy (Q2: 1.2%) while in Singapore, growth contracted by 5.9% qoq annualised (Q2: +0.5%) as exports slipped on weakened global demand. **Malaysia**'s Q3 GDP expanded by 5.2% (Q2: 5.6%) as growing domestic demand outweighed export slowdown.
- **Australia's consumer confidence rose sharply in Nov**, up 5.2% mom and 1% yoy, to its highest level in 18 months and third consecutive month of gains. The largest improvement was seen in the backward-looking household sub-components. The NAB **business confidence index slipped** 1 point to -1 and **business conditions index fell**

2 points to -5 this month, suggesting further deterioration in overall sentiment.

- **Australia's wage growth slowed in Q3** with the Wage Price Index gaining 0.7% qoq (s.a.) (Q2: 1% qoq) but remained steady yoy at 3.7%. Wage pressure appears to be localized in the **mining** (5.2% yoy) and **wholesale trade** (5.3% yoy) industries.

Bottom line: The GDP data from the euro area and especially the worse than expected figure from Japan confirmed the parlous state of the global economy. News from other parts of the world were hardly encouraging, putting in serious doubt the rosy view that the world economy is on course for a pick up in 2013. Truth is that stimulus measures are not working and structural reforms have hardly been put on the agenda.

<u>**Regional Developments**</u>

- **Egypt announced its long-anticipated economic programme** on Tuesday, providing economic projections for the economy in the short, medium and long term, but without addressing pending issues like Egypt's energy needs, and investors' uncertainty with regards contractual agreements with the government. It downgraded its 2012/13 growth forecast to 3.5-4% (previous forecast: 4-4.5%), which is expected to in turn generate 700,000 employment opportunities, and envisions growth of 4.5% in 2013/14.
- **EU announced the approval of a EUR 5.0bn financial aid package for Egypt** while IMF continues its discussions with the authorities regarding the loan.
- **Egypt's urban inflation** increased to 6.7% in Oct (Sep: 6.2%) on rise in prices of non-food items while core CPI was at 4.64% (Sep: 3.84%).
- **Jordanians continue to protest against rising fuel prices** after the government cut fuel subsidies in order to secure a USD 2bn IMF loan. While the Ministry of Energy studies the possibility of **hiking electricity**

rates by almost 5% and 13% in 2013 and 2014 respectively, the government revealed some measures aimed at rising revenues and cutting spending – this includes plans to merge some independent public agencies, increase royalty fees on mining firms and enhancing tax collection among others.

- **Jordan is planning to establish an industrial city south of Amman** exclusive for European factories with an investment of USD 5bn. The development is expected to generate 9K job opportunities for Jordanians.
- Under the Investment Promotion Law, **Jordan attracted about USD 2.15bn in foreign and domestic investments in Jan-Sep period** – an increase of 81% compared to the same period a year ago. Volume of foreign investments alone was up 78% yoy.
- **CPI inflation in Kuwait fell to 1.9% in Sep** – the lowest since 2009 – as food price inflation slowed and the housing component continued to decline. Core prices were 1.4% in Sep.
- **Lebanon is expected to grow at 2%** this year, according to the central bank – a sharp slowdown compared to the official 5.2% growth in 2011. The **Syrian uprising** has left a large impact: it is estimated that Lebanese banks have lost almost USD 400mn in Syria during the 20-month crisis; with the registered refugees in Lebanon now at 118,633 (greater than Turkey), the government is requesting almost USD 450mn in funds for refugees.
- **Lebanon**'s consumer confidence index hit "the lowest point on a monthly basis" in June and also recorded a decline across all 26 subcategories in Q2, due to factors including "domestic political volatility, security breaches, concerns about spillovers from the escalating Syrian crisis, and the dispute over the minimum wage".
- **Morocco's budget is severely constrained by the Compensation Fund** – it is expected to cost between MAD 45.9 and 49.3 billion in 2013, based on oil price at USD

105-110 per barrel. For the period 2013-16, it will reach more than MAD 200bn compared to MAD 123bn in the period 2009-11, as per figures from the Ministry of Economy and Finance. Hence, the government identifies that reforms to the compensation fund are top priority with work starting on it in 2013 but reforms will not be introduced until 2014.

- **Qatar recorded a budget deficit of QAR 18.5bn in Q1 of the fiscal year 2012/13**, representing 10.7% of GDP, as against a deficit of QAR 2.2bn or 1.4% of GDP in the same quarter last year.
- **Qatar Holdings**, which was the second largest shareholder of Xstrata with 11.6% stake, has agreed to back the USD 39.7bn merger between commodity giants Xstrata and Glencore. In this deal, Qatar Holdings will "secure the improved exchange ratio of 3.05 new Glencore shares for every one existing Xstrata share". While it is a tad below the 3.25:1 ratio negotiated for, but definitely better than the 2.8:1 offered earlier.
- **Foreign assets in Saudi Arabia grew to USD 613bn in Aug** (end-2011: USD 547bn) and investment in foreign securities, which account for almost two-thirds of the total, touched USD 424bn (end-2011: USD 380bn).
- The **Saudi government will enforce a fine of SAR 2.4K on private sector businesses for every additional expat employee** and the funds so raised will be used to train Saudi's youth.
- Unless domestic oil consumption is curbed, **Saudi Arabia** will need oil prices at USD 320 per barrel by 2030 in order to balance its budget; additionally, it could lead to a budget deficit by 2014, depletion of foreign assets by 2026 and a large foreign debt by 2030, as outlined at a recent energy conference.
- The newly-formed **Syria opposition bloc** was vetted by the GCC, with the Qatari PM calling it the "legitimate representative of the Syrian opposition".
- According to UAE's MoF official, three outstanding

issues need to be tackled to ensure a smooth implementation of the **GCC Customs Union** in 2015: Saudi Arabia's "protection policy" and high customs duties for some emerging national industries, movement of goods between Bahrain and Oman (which have signed an FTA with the US) and the other 4 countries and the relationship between the agencies and agents within the GCC. While these discussions are ongoing, the distribution of customs revenues has not yet been agreed upon.

- **Afghanistan** is planning to set up a financial free zone to house its 17 local banks and its first-ever stock exchange – the firm Afghanistan Financial Services has already been awarded the stock market licence and aims to be operational by 2014. The budget for the project is expected to be finalised by the end of next month and will be a major boost for the economy once it develops, given the scope for reconstruction efforts in the country and the region.

<u>UAE Focus</u>

- **Abu Dhabi's investment in its hydrocarbon sector grew 11.5%** in 2011 to reach AED 48.8bn as against AED 43.7bn in 2010 year-end and AED 18.5bn in 2008 when oil prices were at its peak.
- Sheikh Ahmed bin Saeed al-Maktoum, head of Dubai's Supreme Fiscal Committee, stated that there was **no need to recapitalise the financial support fund** as "the companies" were "doing well". The IMF had placed expenditures of the fund at AED 19.2bn in 2011, following AED 14.7bn and AED 48.9bn in 2010 and 2009 respectively.
- **Inflation in Abu Dhabi** grew 0.8% mom in Oct, due to higher food prices. In yoy terms, inflation rose 1.2% in the first ten months of the year, with food prices accounting for almost 52.5% of the increase, followed by the restaurants and hotels component.

- The UAE central bank's latest release places total **bank deposits** at AED 1.14 trillion in Sep (up AED 16bn and 1.5% mom – the fastest rate of deposit growth since March) while total bank loans and advances surged by 1.2% mom to AED 1.10 trillion.
- The **Dubai Mercantile Exchange** has opened an office in Singapore, as it looks to be closer to its Asian customers and develop its Oman crude oil futures contract as a global benchmark. While around 60% of DME's volume of trade comes from Singapore, 40% of its crude goes to China.
- Dubai DED's **Consumer Confidence Index** was up 7 points to 129 in Q3, with respondents denoting growing confidence on personal finances and with 86% maintaining a brighter outlook for the next 12 months.

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