

Weekly Economic Commentary – December 16, 2012

Markets

Global **equity** markets rallied this week on optimism that the US Fed money will lift the real economy and as Japanese industrial data painted a less grim picture of the world's third largest economy, shrugging off downbeat news from the euro area. Regionally, markets were mostly down with the **UAE** markets hit by the announcement of royalty fees for its telecom operators. The **euro** reached a three-month high against the greenback as the dollar continued to weaken on the fiscal cliff uncertainty while the **gold** price was on the wane.

Global Developments

Americas:

- The US Fed decided to extend QE purchases for USD 45bn from Jan 1 to absorb the expiration of Operation Twist, combined with the USD 40bn worth of mortgage-backed securities (MBS) already in play. Furthermore, the Fed adopted **quantitative thresholds**, keeping rates low as long as **inflation is below 2.5%** (with stable outlook) and **unemployment above 6.5%**.
- US **wholesale inventories** rose 0.6% mom s.a. in Oct (Sep: +1.1% mom s.a) but rose 6.6% yoy while **sales** of wholesalers fell 1.2% mom (Sep: +1.9% mom), the largest drop since June. Sales of durable goods slipped 0.9% mom. Additionally, **producer prices** contracted 0.8% mom and core PPI was up 0.1% mom in Nov.
- **Retail sales** increased 0.3% mom in Nov (rebounding from Oct's -0.3%), flat excluding autos, and was up 0.7% excluding autos and gas. Sales gains were seen across the board: in autos at +1.4%, furniture +1.0%, electronics +2.5%, building materials +1.6%, healthcare +0.6% and clothing +0.9%.

- **Oct trade deficit** rose 4.7% mom to USD 42.2bn (Sep: USD 40.3bn, revised) with **exports** falling to USD 180.5bn and **imports** shrinking to USD 222.8bn. Over the Jan-Oct period, the trade deficit fell 1.5% yoy to USD 452.5bn as against USD 459.3bn a year ago.
- **Initial jobless claims fell by 29k to 343k** – a nine-week low and the second lowest level in 2012 while the less volatile four-week average fell 27k to 381,500.

Europe:

- European finance ministers reached an agreement which gives the ECB banking supervision powers over the largest banks; EBA rules were adjusted to balance voting powers of states outside the supervisory mechanism.
- **Germany's trade surplus** shrank to a 7-month low in Oct to 15.2bn euro (Sep: 16.9bn euro, revised downwards) as imports recovered faster than exports. **Imports** surged 2.5% mom s.a. (Sep: -1.4%) to the highest level since May while **exports** rose 0.3% mom s.a (Sep: -2.4%).
- **Germany's wholesale price index** eased for the 2nd month in Nov, falling 0.7% mom (Oct: -0.6% mom), bringing the annual rate to a 3-month low at 3.2% yoy (Oct: 4.6% yoy) on cheaper energy and food.
- **France manufacturing output** fell 0.9% mom in Oct (Sep: -3.4% mom), dragged by transport equipment manufacturing. Overall **industrial output** fell 0.7% mom in Oct (Sep: -2.7% mom) but remained stable qoq.
- The final estimate of **Italy GDP** confirms that the economy shrank for the 5th quarter, contracting 0.2% qoq in Q3 (Q2: -0.7%). Household spending fell 1% qoq and exports declined 0.5% qoq. On annual basis, GDP fell 2.4% yoy (as against Q3 last year).
- Sentix **Eurozone investor sentiment** indicator rose for the 4th month in Dec to -16.8 (Nov: -18.8). The current expectations sub-index was little changed while the expectations component surged to -1.5 from -5.5 in Nov.

Similarly, the ZEW **Eurozone economic sentiment** index rose to 7.6 in Dec (Nov: -2.6).

- **Eurozone industrial production (IP)** unexpectedly fell by 1.4% mom s.a. in Oct (Sep: -2.3%), as durable goods output dropped 3.8% mom (Sep: -3.5% mom). **German** IP fell for the 3rd month by 2.4% mom (Sep: -1.6% mom) while declines in **France** moderated to -0.6% mom (Sep: -2.8% mom) and production in Portugal, Ireland and Spain rebounded.
- **Consumer inflation** in **France** eased in Nov falling 0.2% for the 2nd month on cheaper transport and communication, bringing the annual rise to a 2-year low at 1.6% yoy (Oct: 1.8% yoy). Similarly, **German** CPI fell 0.2% mom in Nov (Oct: 0.1% mom) and rose 1.9% yoy (Oct: 2% yoy) while consumer prices in **Greece** fell 0.3% mom (Oct: +0.7% mom) and decelerated to 0.4% yoy (Oct: +0.9% yoy).

Asia and Pacific:

- **China has raised foreign investment limits** in its step towards greater capital account convertibility. With this move, sovereigns and central banks can apply to invest more than USD 1bn in buying Chinese assets through the Qualified Institutional Investor Programme. No upper limit was mentioned.
- **China's trade surplus** reduced sharply in Nov, falling to USD 19.6bn (Oct: USD 32bn), as **export** growth eased to 2.9% yoy (Oct: +11.6%) and **imports** were flat (Oct: +2.4%).
- **China new yuan loans** fell 7.1% yoy in Nov to CNY 522.9bn but rose 3.5% mom as against CNY 505.2bn in Oct, suggesting an economic recovery is still underway. New yuan-denominated loans year Nov were up 13.5% yoy to 7.75 trillion. A separate report showed **China M2 money supply** slowed to 13.9% yoy in Nov (Oct: 14.1% yoy).
- **India's Nov trade deficit came in at USD 19.3bn**, a tad

lower than Oct's record high USD 20.1bn, on lower imports. Value of exports fell 4.2% yoy to USD 22.3bn but imports fell by 5.8% mom to USD 41.6bn.

- **Oct industrial production (IP) recovered in India** and grew at the fastest pace in 16 months, rising 8.2% yoy (Sep: -0.7%), helped partially by seasonal base effects. Consumer durables production reached a 20-month high, while capital goods production was up 7.5%. Meanwhile, IP in **Malaysia** grew 5.8% in Oct (Sep: 5.0%), boosted by strong mining output.
- **Japan's core machinery orders**, though rising for the first time in three months and up 2.6% mom in Oct (Sep: -4.3%), fell below market expectations. The data failed to bring any cheer as even the Cabinet Office lowered its machinery orders assessment and called it a "weakening" trend.
- **Confidence in Japan seems to be waning**, even as the country goes into polls today: Tankan survey showed business sentiment worsening and at a near 3-year low of -12 in this quarter from -3 last quarter. Consumer confidence weakened to 39.4 in Nov (Oct: 39.7) staying within the "pessimism" zone of below 50.
- **Indonesia** held its policy rate steady at a record low of 5.75% to support the rupiah which hit a three-year low.

Bottom line: The explicit macroeconomic targets announced by the FED for its monetary policy represent an idea that Bernanke wished to pursue at the start of its mandate, but whose implementation was derailed by the crisis. From the theoretical point of view these two objectives are the exhumation of the Phillips curve buried in the 1970s. From the practical point of view they represent little more than a voodoo ritual. The woes of the American economy are structural: deteriorating human capital, deteriorating infrastructure, deteriorating technological edge, deteriorating financial sector, which monetary measures do not address.

Regional Developments

- The first round of **Egypt's referendum**, which witnessed a high turnout, has ended and counting is underway. The second round will be held next week and to pass, the constitution must be approved by more than 50% of voters who cast ballots.
- **Egypt's** Morsi (on Monday) reversed, in an attempt to woo voters ahead of the referendum voting, Sunday's **decision to raise taxes** on various goods and services including cigarettes, soft drinks, oil, beer, cement and fertiliser, mobile calls, water and electricity.
- **Iraq's** oil minister stated that the country was looking to **expand production** to 3.7mn bpd next year from the 3.4mn bpd current capacity, with a corresponding rise in exports to 2.9mn bpd from 2.6mn bpd now. The additional output is anticipated from the Majnoon oil field in southern Iraq.
- **Jordan's Social Security Corporation** has announced a 1.2% rise in pensions, in addition to the 3.2% hike given earlier in March 2012. With almost 90k+ persons benefitting from this hike, the cost to the government is placed at JOD 938k a year.
- With a view to increase competition and enable the provision of new services, **Jordan's government is planning to open the telecom sector** to new operators.
- **Qatar National Bank**, on a **regional expansion strategy**, now has its sights on **Turkey**. Having acquired Societe Generale's Egyptian unit for USD 2bn, it is now "looking at a majority stake in a top 10 Turkish bank as a means to add value", according to QNB's CFO.
- **Saudi Arabia** reported **GDP growth at 5.9% in Q3**, compared to Q2's 5.5% but slower than 6.8% a year ago. Growth was supported by higher government spending (Q3: +12.2%; Q3 2011: +6.1%) as both oil sector and private sector GDP growth slowed to 2.3% and 5.1% respectively (Q3 2011: 5.5% and 7.9% respectively). Nov **cost of living index**

increased at the slowest rate in more than 5 years, recording 3.4% yoy, rising only 0.2% from Oct.

- **SAMA's latest report places bank net earnings** at SAR 28.75bn for the period Jan-Oct 2012, compared to SAR 30.9bn in full year 2011 and 2010's SAR 26.1bn, boosted by banks' credit expansion alongside strong liquidity profile with rising deposits.
- According to **Apicorp**, the potential gas deposits in the Middle East are estimated at 26.6 tcm. Given that the Middle East's proven reserves account for nearly 42% of the world's total gas wealth, cross-border collaboration could help maximise the gains from these resources, especially through **a regional energy grid**.
- **Investment in Middle East projects is expected to increase in 2013**, according to a recent PwC report. About two-thirds of respondents reported spending over USD 100mn on major projects in 2012, with 72% expecting higher spending in 2013. While funding constraints were often cited, governance, accuracy and completeness of reporting were also key factors for improvement going forward. UAE and Qatar were identified by the respondents as top targets for investing in capital projects and infrastructure, followed by Egypt and KSA.
- **Retail sales in the Gulf region is expected to grow at a CAGR of 7.7% between 2011 and 2016** to USD 270.3bn, reported Alpen Capital, helped by growing population, rising purchasing power and an expanding tourism and hospitality sector. Duty free and travel retail sales are expected to outperform with a CAGR of 11.6%.

UAE Focus

- **Support for the SME sector** was further strengthened with a Federal decree, including the establishment of a SME Fund to finance around 100 national entrepreneurial projects every year in addition to allocating 10% of government procurements to projects initiated by Emirati

youth.

- **Dubai's non-oil trade crossed the AED 1.0 trillion mark**, with Jan-Oct 2012 total touching AED 1.029 trn compared to AED 911bn in the same period a year ago. Top trade partners for the period were (unsurprisingly) India and China, with total trade at AED 127bn and AED 94bn respectively, followed by Switzerland, the US and Turkey while gold continued to top the list of commodities (AED 113bn).
- **Bilateral trade between UAE and EU** was at AED 74.4bn in H1 2012, but exclusion of the UAE from a new EU list of countries with low rates of tariffs on their exports from the start of 2014 in addition to the carbon trading tax for its airlines are likely to act as obstacles to greater cooperation between the two.
- **Dana Gas** has reached a restructuring agreement with its creditors for the USD 1.0bn Sukuk as follows: it will reduce the debt to USD 850mn by paying down USD 70mn and cancelling the USD 80mn share it already owns. Further, the USD 850mn would be split equally into two tranches – one, as an ordinary sukuk, which will pay a profit of 9%, and another as a convertible sukuk at 7% that will convert to shares.
- **Khalifa Port** was officially launched by HH Sheikh Khalifa on 12th of Dec; the port is expected to handle 2.5mn TEU containers and 12mn tonnes of general cargo a year initially and will, by 2030, be able to process 15mn TEUs and 35mn tonnes of general cargo yearly.
- The new **Al Maktoum International airport**, forecast to cater to about 160mn passengers, is expected to start its passenger terminal operations before end of 2013 and ahead of next year's Dubai Air Show, according to HH Sheikh Ahmed bin Saeed Al Maktoum
- **Royalty fees to be paid by the telecom units**, Etisalat and du, were announced last week: while Etisalat will pay 35% on profit and 15% on revenue, du has been asked to pay 5% of revenue and 17.5% of profit in royalties.

By 2016, both operators would be paying 15% of revenues and 30% of profits. The move towards a rise in revenue share is in anticipation of increased competition between the two operators after the implementation of number portability and fixed line sharing.

- A **CBRE** report noted a **17% yoy rise in Dubai's residential rents**, alongside a 13% rise in residential sales of which only less than 20% were funded by mortgages. CBRE also expects 36,000 new units to enter market between 2013-2015.

MENA Economic Associates

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