

Weekly Economic Commentary – June 9, 2013

Markets

Another week another tumble in Tokyo: the Nikkei is almost 20% down from its peak, while European **equity markets** reacted negatively to Draghi's remark on the meager prospects of eurozone recovery and the need to maintain the lid on government deficits and debt. On Wall Street the week ended on a soft tone with high yielding stocks in the utilities and telecoms sectors sharply down over the past month, as a consequence of the jump in bond yields. **Regional markets** were mixed; Saudi and Oman's indices gained while Egypt's gauge plummeted the most in two months ahead of planned protests at month-end. The **dollar** weakened against major currencies and the **yen** rallied after a positive US employment report fueled speculation that the Fed will scale back easing. A widening divergence is taking place in the **oil** market, with sweet crudes retrenching but sour grades on the rise. Spot prices for Dubai & Oman oil are significantly higher than forward contracts, a condition known as "backwardation". Brent, on the other hand, briefly flirted with the opposite condition known as "contango". **Gold** took another hit, dipping to a 10-day low.

Global Developments

Americas:

- US **non-farm payrolls** rose to 175K in May, up from 165K in Apr while the unemployment rate was up a decimal to 7.6%. Manufacturing shed 8K jobs while most gains came from retail, up 28K; business services, up 57K; education and health, +26K; and leisure +43K positions.
- US **ISM manufacturing index** dropped to 49 in May from 50.7 in Apr, below 50 for the first time since Nov. New

orders plunged from 52.3 to 48.8. The inventory index did not display its seasonal tendency to decline in May and rose from 46.5 to 49.

- US **construction spending** increased a paltry 0.4% mom (4.3% yoy).
- The **US foreign trade deficit** widened to USD 40.3bn in Apr from USD 37.1bn deficit in Mar in line with recovery leading to a rise in imports.
- US **initial claims** declined 11K to 346K, continuing claims fell 52K to 2.95mn. The four-week moving average increased from 348K to 352K, its highest since late April. However the figures have been quite volatile in recent weeks so it is hard to detect a direction.
- The **Fed's Beige Book** indicated that the US economy expanded at a 'modest to moderate' pace during Apr-May with improvements in all districts. Strong gains in construction, a rise in consumer spending and steady hiring helped to support growth.

Europe:

- The **ECB** left rates unchanged, but Draghi warned that the pace of deficit reduction efforts must be maintained. The growth forecasts for 2013 were downgraded, while an uptick is predicted at 1.1% in 2014. On inflation the forecast were 1.4% and 1.3% so well below the ECB target.
- **Eurozone retail sales** slumped more than expected in Apr, falling 0.5% mom (Mar: -0.1% mom) and -1.1% yoy.
- The contraction in **Eurozone manufacturing** eased in May for the first month in five. Markit's Eurozone PMI rose to 48.3 from 46.7 in Apr and an initial reading of 47.8 with improvement seen in all of the region's largest economies.
- **German manufacturing orders** dived unexpectedly by 2.3% mom (-0.4% yoy) in Apr. This follows a 2.3% mom (-0.3% yoy) rise in Mar.

- **German exports** recovered in Apr rising 1.9% mom, beating expectations, after falling -2.8% mom in Mar and -4.2% mom in Feb. Exports to the Eurozone rose 4.3% while exports outside of the region surged 13.6%. Imports also rose at 2.2% mom, pointing to robust domestic demand.
- **German industrial production** unexpectedly rose the most in a year in Apr gaining 1.8% mom after an increase of 1.2% mom in Mar. Construction output surged 6.7% – attributed to a catch up after an unusually long winter – and manufacturing output rose 1.5%.
- The **Bank of England** held interest rates at 0.5% and the asset-purchase programme at GBP 375bn in June. The new Governor Mark Carney will be chairing the next monetary policy meeting in July.

Asia and Pacific:

- A slew of **Chinese economic data** for May raised economic growth concerns: **exports** rose a lower than expected 1% yoy following a 14.7% yoy gain in Apr and imports fell -0.3% yoy; **consumer inflation** came in slightly below expectations at 2.1% yoy (Apr: 2.4% yoy), dipping 0.6% mom; new **local currency lending** slowed to 667.4 bn from 792.9 bn in Apr.
- **China's industrial production** rose 0.6% mom in May (Apr: 0.9% mom) and 9.2% yoy (Apr: 9.3% yoy).
- HSBC's **India manufacturing PMI** fell to the lowest level in 4 years to 50.1 in May from 51 in Apr. Domestic orders grew at a slower pace while export orders surged.

Bottom line: The macro data confirm week after week the sluggish pace of global recovery especially in mature economies where only the US and a few commodity exporters manage to crawl up. The job creation numbers in the US data pointed to an improving environment but not strong enough to trigger an instant Fed reaction on QE. By contrast on the other side of the Atlantic, where another spate of mostly negative figures were released, Draghi warned that the calm on

the markets might not last longer in the absence of structural reforms in labor, product and financial markets. Lack of traction is the dominant theme also in China and India, the first dealing with the hangover of large public investments, real estate boom and credit growth, and the second mired in a political stalemate.

Regional Developments

- **Iranian oil production** is expected to drop to 2.5-2.6mn bpd in May, a level last seen in 1989 during the Iran-Iraq war, as a result of US and European sanctions. The largest reduction in imports came from Japan, which bought virtually no Iranian crude in April. China, South Korea and Turkey kept their imports constant, but they are expected to further reduce imports in the near future to escape the consequences of US sanctions.
- **Bahrain's budget deficit** widened almost 7-times to BHD 227mn (USD 601mn) in 2012, almost 2% of GDP but lower than the initially expected deficit of BHD 1.33bn. Expenditure grew by 14% to BHD 3.26bn while the rise in oil and gas income led to a 21% increase in revenues to BHD 3.03bn. IMF estimates the deficit to widen to almost 8.6% of GDP by 2018.
- **Kuwait** will have to burn 700-900k barrels of oil per day to generate electricity and desalinate water by 2030 if no conservation efforts are initiated, according to the Undersecretary for Planning and Training, Ministry of Electricity and Water.
- **Oman** is projected to grow 4.2% in 2013 and 3.5% in 2014, according to the latest estimates from the IMF. The projection is lower than Oman's official growth estimate of 7% for 2013.
- **Oman's government spending** rose 13.1% yoy to OMR 1.563bn in Q1 2013, with the largest increase reported in gas production spending which surged 54% yoy. Total revenues for the period rose 12% yoy to OMR 3.456 bn. Revenues

from crude exports rose 13.9% to OMR 2.714bn while gas revenues reached OMR 370mn, an increase of 11.3% yoy.

- In Q1 total private deposits at **Oman's commercial banks** rose 9.2% yoy to OMR 9.2 bn. Total loans grew 8.7% yoy to OMR 14.28bn.
- **Qatar** ranks 4th globally in the list of **ultra-high net-worth households** and registered the world's highest density of millionaires, as per a BCG report, with 143 in 100k households falling under this category.
- About 80% of small businesses in **Saudi Arabia** are run by expatriates, and their Saudi "owners" receive between SAR 7-10k per month thanks to sponsorship, according to a newspaper report quoting an HR specialist.
- The world's largest desalination plant, being built with an investment of SAR 23bn (USD 6.1bn) and located in **Saudi Arabia**, is almost 75% complete and is expected to start production in Q3 this year.
- Green building projects in **Saudi Arabia** are picking up, with over 76 projects currently on the books valued at about SAR 100bn (USD 26.7bn). The country accounts for about 5% of the Middle East green building projects and 43 of these projects are based in Riyadh alone.
- A recent **EIU** report projects Dubai to emerge as the **most competitive city** in the Middle East and North Africa region by 2025. It would rank 23rd globally, closely followed by Doha at 24 and Abu Dhabi at 39. New York tops the global list followed by London and Singapore.
- Natural gas development projects worth USD 73bn are currently in the tendering or EPC phase in the GCC, supported by the rising domestic demand for gas, according to a senior ADNOC official.
- Introduction of taxes in the GCC remains one of the key elements towards greater economic diversification, according to an Apicorp report that also highlighted three long-term structural issues including the impact of energy security-climate change nexus on petroleum export markets, unsustainable fiscal spending and

inability to create employment opportunities within the oil sector.

UAE Focus

- Dubai and Abu Dhabi will merge their **aluminum** production to create a company valued at USD 15bn, the world's fifth-largest producer with annual output of 2.4m tonnes once the Abu Dhabi smelter is completed in mid-2014. A source close to the deal said Dubai's enterprise was valued USD5bn.
- Expansion in new export orders (up from a 9-month low in Apr) and employment took **UAE PMI** to a 3-month high of 55.3 in May (Apr: 54).
- The **UAE Central Bank** has set up a committee to draft a **mortgage law** that would include not only the soon-to-be implemented lending rules, but also rules guaranteeing the rights of the lenders. However, it is imperative that this be accompanied by a comprehensive property database and an early warning system to manage banks' mortgage credit.
- About 58.4% of Emirati families in **Abu Dhabi** took **loans** in Q1, with reasons ranging from purchasing a car (60% of borrowers), to buying a house (25%) to marriage expenses (12%) and travel (3%) according to a recent study by Abu Dhabi DED.
- **Household wealth in the UAE** increased by 8.2% in 2012 to a total of USD 400bn amongst 57k families across the country, as per a recent BCG report. Ranked at 15 globally with regard to high net worth individuals, 3 in 100k families fall into this category.