

Weekly Economic Commentary – Apr 20, 2014

Markets

The Easter week saw reduced activity on Western stock markets, but the US stock markets enjoyed their best weekly performance in nine months despite a mixed start of the earnings season (Google and IBM disappointed, banks performed well) thanks to a rebound in the tech sector. Data from China continue to underscore tensions and challenges in the adjustment to a more market driven economy. Regional markets (except Kuwait) joined the upbeat mood. The euro lost some ground to the dollar, while in the commodities space gold retrenched again and oil gained somewhat in directionless trade.

Global Developments

US/Americas:

- **US industrial production** growth slowed to 0.7% mom from 1.2% in Feb, thanks to perky gains in durable goods and mining. Capacity utilization rose to 79.2% from 78.8% in Feb, the highest since June 2008.
- **US inflation** was 0.2% mom and 1.5% yoy in Mar, up from 1.1% in Feb. The acceleration was due to volatile food prices (+0.4% mom).
- In the **Beige Book**, eight out of twelve regional Feds evaluated growth as “modest” to “moderate” in the period. The book also stressed that the weather was a major factor in the slowdown of economic activity.
- **US retail sales jumped** 1.1% mom in Mar from a revised 0.7% in Feb pushed by a 3.1% jump in car sales.
- **US housing starts increased** 2.8% mom in Mar (against expectations of 7%) equal to an annual rate of 946K units, after a revised up 1.9% rise in Feb i.e. an

annual rate of 920k units. In yoy terms starts dropped 5.9% the biggest decline since April 2011.

- **US initial jobless claims rose modestly** 2,000 to 304K. The four-week moving average declined to 312K from 316.7K. Continuing claims fell 11K to 2.74 million.

Europe:

- **The EU Parliament approved a package of reform measures to deal with restructuring and winding down troubled banks.** Furthermore banks, not taxpayers, will guarantee deposits under EUR 100k. These measures complement the single bank supervision system, already in place, and implement some key planks of a banking union.
- **Eurozone industrial production grew** 0.2% mom in Feb (1.7% yoy), following no change in Jan (1.6% yoy), confirming a weak but ongoing recovery.
- The **French** socialist government reaffirmed its **commitment to a 3% deficit to GDP target**, set by the EU for 2015, despite having ventilated the possibility of breaching once again the Stability Pact limit. The **Italian government** on the contrary asked to delay its balanced budget by one year to 2016, while unveiling a modest tax cut and some cosmetic austerity measures, including sale of luxury government cars.
- **UK inflation slowed** to 1.6% yoy in Mar, the lowest since Oct 2009, from 1.7% in Feb.
- **UK headline ILO-harmonised unemployment rate fell** to 6.9% in the three months to Feb, while the national claimant count, which is a month ahead of the ILO data, fell to 3.4% in Mar.
- The **euro zone's current account surplus** in Feb was EUR 13.9bn, following a EUR 7bn surplus in Jan and EUR 9bn in Feb 2013.

Asia and Pacific:

- **China's GDP in Q1 expanded** 1.4% qoq (5.7% qoq ann) sa

which translates into 7.4% yoy versus 7.7% in Q4 (6.98% qoq ann). Both domestic and foreign demand were weak with investment still up 17.6% yoy but on a downtrend due to credit tightening.

- In **China** the **value of property sales fell** 5.2% yoy in Q1 and the floor space of new property construction tumbled 25.2%. Property-development investment rose 16.8% yoy, the weakest for the first quarter since 2009. Investment in urban real-estate development was equivalent to about 14% of GDP in 2012.
- **China's** broadest measure of **new credit fell** 19% yoy in Mar and money supply grew at the slowest pace on record.
- **China** has issued **stricter rules for trust companies** to stem systemic risks posed by the shadow-banking sector. Essentially to avoid Ponzi schemes regulators mandated that asset managers match each individual account with specific underlying assets, rather than pooling cash and assets into common pools. Furthermore new subscriptions cannot be used to pay dividends on old investments.
- **Japanese consumer sentiment fell** in Apr to 37.5 from 38.5 in Mar, marking the sixth monthly drop and the lowest since Aug 2011. The relentless decline from a top of 45.7 May 2013 casts additional doubts on the Abenomics' success.
- **India's CPI inflation increased** marginally to 8.3% in Mar from 8.0% in Feb. The wholesale price inflation, picked up in Mar to 5.7% yoy from 4.7% in Feb after three months of moderation due to a jump in food prices.

Bottom line: Data from China month after month continue to underscore tensions and challenges in the adjustment to a more market driven economy. The slowdown from China is hitting corporate America; for example IBM struggled to meet expectation on expansion in Asia. In developed markets on the contrary a gradual pick up is gaining steam. Emerging markets and transition economies accounted for 60.5% of the FDI flows and 54.0% of cross-border mergers and acquisitions in 2013,

according to the latest FDI Intelligence report.

Regional Developments

- The **GCC reached an initial agreement to put at rest a diplomatic spat over Qatar's support for the Muslim Brotherhood**. The foreign ministers pledged "to adopt the mechanisms that would ensure moving forward in a collective framework, and that the policies of any of the GCC member states would not affect the interests, stability and security of its members and without impacting on the sovereignty of any of its members". No reference was made to whether the Saudi, UAE and Bahrain ambassadors would return to Doha or if Doha would withdraw its support for the Muslim Brotherhood.
- The **Credit Default Swap** (CDS) on 5Y debt **Egypt fell** to 4.05% – the lowest level since Jan 2011 (4.39% at the time) from a peak of 9.25% in July 2013.
- **Egypt's** Council of Ministers approved the draft by-law governing the **decentralisation of the governorate councils and the municipalities draft law**. With an aim to achieve sustainable and comprehensive local development, the decentralisation plan is also expected to improve the performance and upgrade the quality of the services provided by municipalities and governorate councils.
- **Tourism revenues** in **Egypt dropped** 43% yoy to USD 1.3bn in Q1 this year, following an equally sharp 41% drop in revenue last year to USD 5.9bn. With about 15 countries issuing travel warnings against Egypt, the 30% yoy drop in tourists to 2mn people in Q1 was no surprise either.
- **UAE and Egypt** signed an executive **agreement** to initiate training more than 100k youth with the aim to qualify the youth to enter the job market and find jobs; the pact is worth EGP 250mn and is part of UAE's aid packages to Egypt for developmental purposes.
- **Egypt** is expected to introduce a **smart card system for**

subsidised bread nationwide by July, according to the Supplies Minister, to wipe out corruption and smuggling; the pilot scheme was initiated last Sunday. Meanwhile, the **Libyan** government announced that it is planning to propose a **smart card system for fuel subsidies**, with the initial phase expected within next 2-3 months.

- **Jordan's** economy is expected to **grow at** 3.5% this year and a further 4% in 2015, as per **World Bank estimates**, supported by aid packages from the Gulf and the latter's financial stability.
- **Inflation** in **Jordan fell** to 3.2% qoq in Q1 and compares to 5.6% in the previous quarter. This is in line with the government's inflation target of 3% this year, based on forecasts of a lower energy import bill and continued bread subsidies.
- **Jordan's tourism revenues increased** by 11.1% yoy to USD 1.026bn during the first four months of this year, thanks to rise in the number of visitors from the Arab Gulf states, US, Libya and Yemen.
- **Unemployment rate** in **Jordan fell** to 11.8% in Q1 (Q1 2013: 12.8%) but increased by 0.8% qoq; gender disparity still remained wide with unemployment rate 9.7% among males and 21.8% for females.
- **S&P raised its outlook** for **Lebanon's** Bank Audi, BankMed and BLOM Bank to stable from negative, following the upgrade of Lebanon and also affirmed the 'B-' long-term counterparty credit ratings on all three banks.
- The **World Bank** projected 4.9% **growth in Oman** this year, and cautioned that an adverse scenario where oil prices dipped to USD 90 a barrel could increase fiscal pressures especially in Oman where the fiscal breakeven is USD 100. Oman is also expected to post a fiscal deficit of 2.7% of GDP in 2014, with the deficit rising further to 6.3% in 2015.
- **Foreign investment** in **Oman increased** 9.3% yoy to OMR 13.887bn in 2012; UK accounted for the largest share of foreign investment, followed by UAE while oil and gas

(46.6%), manufacturing (18.3%) and financial brokerage (16.1%) were the most attractive sectors.

- **Real estate transactions in Qatar** touched QAR 4.2bn in Mar, with Doha municipality accounting for about 37% of overall transaction value.
- **Qatar inflation was up** 2.6% yoy and 0.3% mom in Mar, with rents and energy costs, which account for more than 32% of consumer expenses, rising 5.7% yoy and 0.6% mom.
- The powerful **Head of Saudi Intelligence**, Prince Bandar, who suffers from a serious back ailment, was **replaced** by his junior General Yousef Al Idrissi, who has no line to the throne.
- EY's **MENA IPO update** revealed that 5 IPOs launched in Q1 raised USD 1.3bn – a -21% yoy dip in value; two IPOs were in Tunisia and one each from Qatar, Saudi Arabia and the UAE with Qatar's Mesaieed Petrochemical Holding Company the largest issue, USD 905mn.
- According to the Secretary General of the Union of Arab Banks, the **consolidated assets of Arab banks** has touched USD 3 tr at the end of 2013 (assets were USD 2.7 trn at the end of Sep 2013), of which Islamic banking accounted for USD 1.3 trn, or 40%, of total assets.

UAE Focus

- **Real estate investments in Dubai increased** by a whopping 57% to AED 35bn in Q1. Attracting 13279 investors from 133 nationalities, Emiratis ranked as highest among all investors in terms of the value of investments (1228 transactions worth AED 7bn), with Indians the largest number of foreign investors (2414, spending AED 5.895bn) and Lebanese nationals represented the highest percentage of Arab investors (247 Lebanese citizens spending AED 652mn).
- **UAE inflation edged up** to 1.9% in Mar (Feb: 1.8%), the highest level since Oct 2010, thanks to rapid increase in housing costs (+2.4%) and food prices (+2%).

- **Dubai DED** issued 1834 **licenses** in Mar, recording a 13% yoy growth, with the commercial sector registering a 75% rise in the number of licenses issued.
- The recently approved **UAE** Federal Law No 2 of 2014, the **SME Law**, will boost activity of this sector, given that the legislation requires federal authorities and ministries to contract at least 10% of their procurement budget for purchasing, with SMEs. This is expected to raise the contribution of SMEs to GDP to 70% by 2021, according to the Ministry of Economy.
- **Dubai** Statistics Centre has commenced a **household expenditure and income survey** 2014-15 to provide demographic, housing, expenditure, and income data about the society. The survey will run till end-Sep and the analysis of data will happen over the next 6 months. According to the last survey, conducted in 2009, European expatriates topped the annual income list (avg annual income: AED 172k) followed by Emiratis (AED 133k) and Arab (AED 102k) households.

Media Review

The Importance of relationships for start-ups in the Middle East

http://www.zawya.com/story/Relationship_pivotal_for_startup_investments-ZAWYA20140408111847/

SWFs are slowing their M&A in 2014

<http://www.arabianbusiness.com/swfs-much-slower-pursue-m-a-deals-in-2014-542922.html>

Governance of SWFs

http://www.revenuewatch.org/sites/default/files/NRF_RWI_Complete_Report_EN.pdf

El Erian comments on the IMF Annual Meetings

<http://www.bloombergvew.com/articles/2014-04-14/the-dangers-of-policy-drift>

An overview on the next crisis: the shadow banking system in China

<http://www.ft.com/intl/cms/s/0/0053a036-c3aa-11e3-a8e0-00144fe>

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