

Weekly Economic Commentary – Jun 1, 2014

Markets

The **rosy market consensus is under skeptical scrutiny since early 2014, when global growth was expected to pick up and interest rates to rise gradually. The downbeat US GDP data reinforces this view; however stock markets seem largely unaffected.** The US indices scored another record high and the FTSE Eurofirst 300 closed the week at a six-year peak. Emerging markets have seen a turnaround for several weeks benefiting from cheap borrowing in dollars, which spurred carry trades and higher leverage. Also many hope that elections will deliver economic reforms in places like India and later in Brazil. Last week however EM stocks lost ground except in our region where all indices rose (bar Egypt). The euro remained stable and no major moves were recorded in other pairs. Gold drifted down to a fresh three-month low losing almost USD 50 dollar lower in a week. Oil prices were slightly down after a week of directionless trade.

Global Developments

US/Americas:

- **US GDP** second estimate for Q1 was **revised sharply down** from +0.1% qoq ann. to a contraction -1%. The weakness was due almost entirely to falling inventories. Consumption growth remained almost unchanged at 3.2%. Business fixed investment was revised up from a fall of -2.8% to -2.3%; housing investment was revised from an annualised fall of -5.7% to -5%.
- **US consumer spending slipped** -0.1% mom in Apr after a revised 1.0% in Mar, the largest gain since August 2009. Last month's decline was the first since Apr 2013.

- **US CPI inflation is running** 0.2% mom (1.6% yoy the largest gain since Nov 2012) in Apr, the same as in Mar (1.1% yoy). Ex food and energy, CPI also increased 0.2% mom or 1.4% yoy a top since Mar 2012.
- **US durable goods orders increased above expectations** in Apr by 0.8% mom after gaining an upwardly revised 3.6% mom in Mar. Orders for non-defence capital goods – a proxy for business spending plans – dipped -1.2% after rising 4.7% in Mar.
- The **S&P Case-Shiller home price index increased more than expected** by an annualized 12.4% in Mar after rising 12.9% in Feb. The purchase-only house price index rose 0.7% mom in Mar (6.5% yoy), recording similar gains for Q1, the 11th quarterly increase
- The Thomson Reuters/University of Michigan **consumer sentiment index fell unexpectedly** 2.2 points to 81.9 in May from Apr.
- **US initial jobless claims fell** by 27,000 to 300,000, with continued claims dropping by 17,000, the lowest since Nov 2007.

Europe:

- **German retail sales unexpectedly fell** in Apr by -0.9% mom after rising 0.1% mom in Mar.
- **Germany's unemployment rate** was **steady** at 6.7% sa in May for the fourth consecutive month. The number of unemployed rose by 24,000, following a 25,000 drop in Apr.
- **Eurozone M3 money supply growth eased** to 0.8% yoy in Apr following a downwardly revised 1% yoy rise in Mar.
- **Eurozone's economic sentiment** index reached in May a **two-year peak** at 102.7 from 102 in Apr, and was above its long-term average for the sixth consecutive month. Consumer confidence rose to -7.1 in May from -8.6 in Apr reinforcing an upward trend.
- **French household consumption** in Apr **dropped** -0.3% mom

following an increase of 0.6% in Mar.

Asia and Pacific:

- **Japan's core consumer price index surged** 3.2% yoy in Apr following a 1.3% yoy gain in Mar as a result of higher sales taxes.
- **Japan industrial production fell** by a more-than-expected -2.5% mom in Apr after rising a 0.7% mom in Mar.
- **Japan retail sales slumped** -13.7% mom in Apr – the largest drop in 14 years in reaction to the higher VAT rate.
- **South Korean trade surplus** scored a 10-year **record** at USD 10.7bn in Apr.
- The **Philippines'** economy **grew a disappointing** 5.7% yoy in Q1 down from 6.3% in Q4 as a result of typhoon Haiyan.
- **Singapore's** industrial production in Apr **grew** 4.6% yoy down from 12.1% in Mar dragged down by electronics.

Bottom line: While global equity markets hovering at all-time highs, bond markets conversely point to a significant downgrade in global growth. US 10-year Treasury yields have fallen by half a percentage point to about 2.5% since early 2014. German Bunds and UK followed suit. This suggests **entrenched doubts on a sustained growth acceleration that would justify current equity valuations – and confirms that years of easy money have failed to spur a robust recovery.** Furthermore the view is gaining consensus that markets have been so heavily distorted by undue government intervention since Lehman bankruptcy that investors are unwilling to deploy their capital in new ventures or in expansions. Another sign of global weakness came from the Netherlands Bureau for Economic Policy Analysis, a government think-tank that collates data on international trade around the world: its **measure of world trade indicates a -0.8% qoq drop in Q1.**

Regional Developments

- **Egypt's** former army chief Abdel Fattah al-Sisi won the Presidential **elections**, though the turnout was only about 46% of Egypt's 54mn voters (lower than for the previous elections). Stock markets were down, also because the finance minister approved a 10% tax on stock market profits while Fitch confirmed its low rating, reflecting **substantial risks to Egypt's weak public finances**.
- The Central Bank of **Egypt** left the overnight deposit and lending **rates unchanged** at 8.25% and 9.25%, respectively while also maintaining the discount rate at 8.75%.
- With spending for 2014/15 estimated at EGP 807bn, up EGP 65bn from current year, **Egypt's** government **forecasts a budget deficit of 12% of GDP** in its final draft budget – submitted to the interim President – which also forecasts 3.2% economic growth.
- **Bahrain** has become the second GCC nation, after Saudi Arabia, to clarify its stand on the treatment of **capital-boosting instruments** under **Basel III** rules, stating that such instruments need to include loss absorption features. The central bank has also drafted separate rule books for conventional and Islamic banks, proposing they both come into effect in Jan 2015.
- Reuters shipping data reveal that **exports** from **Iraq's** southern terminals have averaged 2.60mn barrels per day in the first 27 days of May. If sustained for the rest of the month, it is estimated that southern exports would top April's level of 2.51mn bpd, the **highest since 2003**.
- **Oman exports** totaled OMR 1.8bn in Jan, recording a **drop** of 8.1% yoy; the only increase recorded was in non-oil exports, which grew by 6.1% to OMR 346.6mn, thanks to a 79.5% rise in mineral product exports.
- **Qatar exports were down** 7% yoy to QAR 40.1bn in Apr while imports grew 10% to QAR 8.8bn. Top trade partners for Qatar's exports were Japan (QAR 10.8bn or 27% of total exports), South Korea (QAR 6.2bn, 15%) and India

(QAR 5.4bn, 13%).

- All companies listed on **Qatar**'s stock exchange will **raise their foreign ownership limit to 49%**, according to an order announced in a bourse filing last week. The move, ahead of the MSCI reclassification, will encourage liquidity, but the changes will not be immediate because they are subject to companies amending their articles of association, requiring shareholder approval.
- **Tourist arrivals into Qatar grew** 9% yoy to 387,022 in Q1; GCC tourists were up by 5% during this period, of which Saudi Arabia was the largest single source of visitors with 188,621 travelers and Kuwait the fastest growing with 42%. Average hotel occupancy rate rose to 75% during this period from 68%.
- **Non-oil activity in Saudi Arabia grew** in Apr, with the increase in new orders the quickest since Jan '14 and new export business also rising, but the rate of growth was down from Mar's joint-series high, the HSBC Emerging Markets Index, a monthly indicator derived from the PMI surveys. EMI was 50.4 in Apr (Mar: 50.3) and well below its eight-and-a-half year long-run trend level of 53.9.
- **Saudi Aramco** stated that it would **invest** more than USD 100bn in **downstream projects** over the next decade as global demand for oil is expected to rise by a quarter in the next 25 years.

UAE Focus

- **UAE has pledged additional support to Egypt;** the UAE has already provided more than AED 22bn, in cash and interest-free loans to guarantee fuel supplies and fund projects in health care, education, food, housing and transport.
- **Remittances from UAE** expats exceeded USD 20bn in 2012, according to a report from the Ministry of Foreign Affairs. The report also revealed that UAE has ratified nine major International Labor Organization conventions

related to the rights of workers.

- **Passenger traffic** in Dubai was **up** 13.7% yoy to 6.1mn in Apr, registering a 11.9% increase year-to-date to 24.5mn and compares to London Heathrow's 22.2mn passengers till Apr this year.
- **Moody's** revealed that **Sharjah's A3 credit rating** is supported by its very strong fiscal and government debt position, "characterised by small fiscal deficits, low levels of government debt and manageable wider public-sector debt".
- **Hotel occupancy in UAE dipped** during Q1, as per EY estimates, with Dubai and Abu Dhabi witnessing occupancy drop 1% to 88% and 82% respectively.

Media Review

Winning the election in Egypt is just the starting point for Al Sisi

<http://www.bloombergtview.com/articles/2014-05-29/egypt-vote-is-more-a-warning-than-a-victory>

Iraqi Kurdistan sells oil despite Baghdad opposition

<http://www.bbc.com/news/world-middle-east-27545439>

El Erian warns on the M&A conundrum

<http://www.bloombergtview.com/articles/2014-05-22/m-a-boom-has-yet-to-help-the-economy>

Low volatility in markets prices might be pathological

<http://www.ft.com/intl/cms/s/0/05a4b31a-e5ae-11e3-aeef-00144feabdc0.html>

The shale oil and gas bonanza might be grossly exaggerated

<http://www.marketwatch.com/story/dream-of-us-energy-independence-was-just-revised-away-2014-05-22>

European Agency Reports Surge in Illegal Migration

<http://www.nytimes.com/2014/05/31/world/europe/european-border-agency-reports-surge-in-illegal-migration.html>

Saudi Arabia's hidden uprising

<http://www.bbc.com/news/world-middle-east-27619309>

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