

Weekly Economic Commentary – May 3, 2015

Markets

Stocks finished the week slightly lower hit by the negative news on US GDP. Investors digested a substantial news flow both on the macro front and on and corporate earnings, and the reaction was tendentially downbeat. As the week ended, signs of progress in Greece's negotiations with lenders its financial bailout eased fears of a traumatic Grexit. Major indexes were lower on the week, with the Dow Jones down 0.3%, and the S&P 500 almost flat. European shares saw their first monthly decline of 2015 in April, as optimism over ECB's QE programme began to fade. Regional markets were an exception at global level and among emerging markets, scoring substantial weekly gains. The euro recorded a major rebound as the US GDP data led to conclude that the Fed will remain dovish for longer. Oil prices came off their best monthly gain in nearly six years, but still scored a weekly gain, their seventh rise in a row notwithstanding reports that Iraq's crude exports rose to a 30-year high. The fluctuation phase of the dollar seems to continue as it marginally reverses previous week's backslide. Gold prices recorded their lowest in six weeks, logging their third straight weekly loss to settle at USD 1,174.5 per ounce.

Global Developments

US/Americas:

- **US GDP** barely grew in Q1 ticking only 0.2% qoq ann vs. 2.2% in Q4 and smashing all expectations. Trade and nonresidential investment were dismal. Only consumer spending surprised on the upside. Worryingly business fixed investment contracted by 3.4%, reflecting a 23% annualized drop in nonresidential structures investment.

- **The Fed FOMC** acknowledged that growth had slowed over the winter and that there were some soft patches across the economy. They emphasised transitory factors in their analysis and reiterated optimism on the US outlook overall. Overall, the final statement gave a solomonic view of the current economic situation and hinted the Fed remains very much in a data-dependent mode, but did not shake convictions that the first rate hike will come in September.
- **The ISM manufacturing index** was unchanged at 51.5 in Apr, keeping it below its Q1 average of 52.6. The Production rose from 53.8 to 56 while new orders also edged higher.
- **Inventories of crude oil in the US** rose by 1.9 ml barrels against expectations of 2.3m barrels. Stocks at Cushing, the delivery hub where WTI is priced, fell by 514,000 barrels – the first decline since November 28. US crude oil inventories are at record high in 80 years and have risen for 16 consecutive weeks.
- **Existing-home price** appreciation accelerated yoy in the three months ending in Feb relative to the same period in Jan. The 20-city composite index is up by 5% yoy in Feb, compared with 4.6% yoy in Jan . Pending home sales index rose 1.1% to 108.6 in Mar.
- The Conference Board **Consumer Confidence Index** tumbled 6.2 points in Apr to 95.2, a four-month low and well short of expectations for a modest increase.
- **Initial claims for unemployment** benefits fell sharply, dropping by 34,000 to 262,000. The trend remains solid as the four-week moving average fell from 285,000 to 283,750.
- **US Personal Income** stagnated in Mar after rising 0.4% mom in Jan and Feb. Spending rose 0.4%, the best increase since Nov.
- **Construction spending** decreased 0.6% mom in March, falling far short of expectations. Private construction fell 0.3%, driven lower by the residential component.

- The **Brazilian central bank** delivered another 50bp hike in the Selic rate, in line with market expectations, focusing on inflationary pressure, rather than taking into account the economic slowdown and the sharp exchange rate appreciation in the past few weeks.

Europe:

- **Euro zone officials** sought to wring policy concessions from **Greece** to unlock urgently needed aid after Athens said it would present a list of reforms to show it is serious about its promises. ECB Board member **Benoit Coeure** reiterated that the **ECB** is making no plans for a Greek exit from the euro zone.
- **Euro zone consumer prices** remained unchanged yoy in Apr, following a 0.1% drop in Mar and confirming that deflation is not entrenched.
- The **euro zone's M3 money supply** grew 4.6% yoy in Mar, following a 4% increase in Feb.
- The **Conference Board Leading Economic Index** for the **euro zone** rose to 105.1 in Mar from a revised 104.7 in Feb.
- The **eurozone's unemployment** rate in Mar was 11.3%, unchanged from Feb. Among individual countries, **French unemployment** rose 0.4% in Mar after increasing 0.4% in Apr, **Italy's unemployment** rate jumped to 13% in Mar from 12.7% in Feb, reversing all past improvements and **Germany's unemployment** rate in Apr remained at 6.4% for the second consecutive month.
- **UK GDP** rose by 0.3% qoq (2.4% yoy) in Q1, weaker than expected versus 0.6% qoq, (3.0% yoy) in Q4. Growth was dragged down by sharp falls in construction output (-1.6%qoq) and mining, oil and gas (-2.1%qoq), and weak growth in business services (0.1%qoq).
- The **U.K. Nationwide Housing Price Index** climbed 5.2% yoy in Apr, following a 5.1% increase in Mar.
- **French household consumption** decreased -0.6% mom in Mar, following a 0.1% rise in Feb driven by lower spending on

nondurables and energy.

Asia and Pacific:

- **Japan central bank** maintained its stimulus policy unchanged as prices edge higher and the jobless rate falls even further.
- **Japan's core inflation** remained at 2.2% yoy in Mar for the 4th consecutive month, which was in line with the market expectations.
- **Japan's industrial production** fell -0.3% mom in Mar (-1.2% yoy), after Feb's -3.1% mom fall (-2.0% yoy). The data, which beat expectations, over the past two months have been influenced by the New Lunar Year seasonality.
- **Japan's housing starts** surprised on the upside raising to 0.7% yoy in March from -3.1% back in Feb.
- **Japan's retail sales** fell a sharp 9.7% yoy in Mar. Overall, retail spending remains weak mainly due to the decline in oil prices and paltry wages growth.
- **Taiwan's GDP** grew 3.5% yoy in Q1, slightly higher than Q4's 3.4%. Exports and manufacturing were bright spots thanks to improved technology.
- **South Korea's inflation rate** was 0.4% yoy in Apr, as low oil prices continue to exert downward pressure on transportation and utility prices. **Bank of Korea** business confidence index increased to 80 in April from 77 in March.
- **South Korea's industrial production** fell 0.1% yoy in Mar, following Jan's revised 5.0% fall. Korean producers are losing out as a strong won hinders competitiveness.
- **The Bank of Thailand** surprised the markets by cutting interest rates by 25bp to 1.5%.
- **Thailand's industrial production** fell -1.8% yoy in Mar after rising 3%. Yet the overall momentum in 2015 is still positive as recovery from 2014 production decline continue.

Bottom line: The cold shower of the US GDP data are a painful

reminder that the global economy is again in the doldrum and that equity markets are out of touch with reality. The US economy, described the only cylinder of global growth, is now sputtering. The media pointed to temporary factors like bad weather in Boston and a brief port walkout in LA. But those clearly were not the main issue, otherwise forecasts for Q2 would be in the order of 5% qoq annualized growth, once the temporary factors wane. On the contrary the early estimates for Q2 point to another weak quarter, with some raising the possibility of negative growth. Another momentous development is taking place in the US oil industry: crude output at 9.366 ml b/d, is 56,000 b/d lower than the peak on 20 March. The rig count in the four main US shale plays has dropped for almost 6 months and stands at 501 after having lost 583 rigs in a year. The decline is expected to accelerate over the summer not only due to further dismantling but also because cash flow at current oil prices is too low to complete most wells being drilled. Essentially capital is only available to for basic operating costs and completion of the most productive wells that are profitable even at present prices. Unless oil prices rebound above USD 75/b, money to complete additional will dry up. Anyway a speedy recovery of production even if prices rebound is out of question. Well completions and drilling activity is stalling hence workers are moving out of the shale oil regions. Those jobs and skills will not quickly return. To stabilize output, the rig count in US shale plays would need a boost in the order of 200 units, which at present is not in the cards.

Regional Developments

- **Egypt's** finance minister revealed that the country plans to issue an ijara-structured **sukuk** in the beginning of the 2015-16 fiscal year. Furthermore, he disclosed that following complaints about the ambiguity of the payment method of a new tax on stock dividends and capital gains, amendments were being made.

- **Money supply** M2 in **Egypt** grew 17% yoy to EGP 1.6826 trillion in Mar.
- Revenues from **Suez Canal** reached USD 420.1mn in Mar (Feb: USD 382mn).
- **Iraq's crude oil exports** rose to a record high of 3.08 million barrels per day (bpd) in Apr from 2.98mn bpd the previous month.
- **Fuel prices** in **Jordan** are expected to increase by between 2-3.5% as of May 1, according to the Gas Stations Owners Association, based on the average price of Brent crude on the global market.
- *Kuwait Times* reported, citing government sources, that the **Kuwaiti** cabinet had agreed on a decision to freeze its existing **expatriate population**, and allow foreigners into the country only to replace those leaving.
- A recent World Bank study revealed that the **Syrian conflict** had no impact on **Lebanese** merchandise and services exports at the aggregate level; while the drop in exports was influenced more by international demand, the conflict generated opportunities for Lebanese exporters to replace the loss in Syrian production. Another report disclosed that the Syrian crisis eroded government revenue collection by some USD 1.5bn while increasing state expenditures by USD 1.1bn, with a total fiscal impact of USD 2.6bn over a three-year period from 2012 to 2014.
- The **World Bank** plans to double its **investments** in **Lebanon** by 2020, investing an annual USD 300mn in Lebanon in the next four years, according to the new MENA region vice president.
- **Oman's GDP** at current prices increased 5.2% during Jan-Sep 2014 compared to a growth of 2.6% in the same period a year ago, according to preliminary data.
- **Foreign trade surplus** in **Qatar** increased 53.7% yoy to QAR 19.1bn in Mar; total exports of goods dipped 40.7% yoy and 3.3% mom to QAR 1.7bn in the last month of Q1 while imports were up 9.9% yoy and 9% mom.

- In a surprise move, **Saudi** King announced Mohammed bin Nayef (55), his nephew, as crown prince and Mohammed bin Salman (30), his son, as deputy crown prince – thereby deciding **successions** for the decades to come. This also means the rulership will pass to a new generation for the first time since 1953.
- **SAMA's net foreign assets** dropped by 4.7% yoy to SAR 2.59trillion in Mar, the lowest level since July 2013. Net foreign assets fell by USD 16.0bn mom while in Feb the drop was a higher USD 20.2bn mom.
- **Saudi Aramco** is to be restructured and separated from the Oil Ministry, reported Al Arabiya TV.
- EY's World Islamic Banking Competitiveness report estimates **Shariah-compliant assets** in **Saudi Arabia** to touch USD 683bn by 2019. In 2013, 54% of all financing was Shariah compliant.
- Further **economic diversification** in the **GCC** – on average economic diversification levels of OECD – could help the region to gain upto USD 17.7bn, as per EY. The report identified the following sectors as aiding diversification: transport, financial services, retail and tourism, telecoms and R&D.
- Alpen Capital's **GCC Food Industry** Report 2015 revealed that food consumption is expected to grow at a compounded annual growth rate of 3.5% between 2014 and 2019, to 51.9mn metric tonnes, supported by population growth, high income and tourism.

UAE Focus

- **UAE bank lending** growth accelerated to 8.2% in Mar, following a 7.8% pickup the month before. Meanwhile, **M3** money supply growth at 7.6% was at the slowest since Mar 2013.
- **DP World** reported a 4.4% rise in gross container volumes to 15 million 20-foot equivalent units (TEU); Europe Middle East and Africa, which includes the UAE ports,

rose 9.2% to 6,405 TEUs.

- **DEWA**'s CEO revealed that the company would invest AED 60bn in utility projects till 2020, with most to be conducted as public-private partnerships. The Dubai Energy Strategy 2021 also mentioned that DEWA would reduce carbon emissions by 16% (saving five million tonnes of CO₂) by 2021.
- **Banking sector** in the **UAE** reported strong growth in assets and profits alongside improvement in asset quality, liquidity and capital adequacy as per the published Q1 financial results.

Media Review

Is oil rally doomed?

<http://www.bloomberg.com/news/articles/2015-04-28/the-oil-rally-looks-doomed-in-five-charts?>

US oil production decline has begun

<http://www.artberman.com/the-u-s-production-decline-has-begun/>

Norwegian SWF earns more than government spends

<http://www.ft.com/intl/cms/s/0/23693448-ee72-11e4-88e3-00144feab7de.html#axzz3YYPjhKnF>

Saudi Succession Reshuffle

<http://www.economist.com/news/middle-east-and-africa/21650037-king-salmans-royal-reshuffle-brings-young-faces-while-bolstering-his-line-palace>

The dollar joins the currency wars

<http://www.project-syndicate.org/commentary/dollar-joins-currency-wars-by-nouriel-roubini-2015-05>

Grexit (if it happens) unlikely to lead to contagion or spillover to other Eurozone countries

<http://www.businessinsider.com/r-absence-of-contagion-changes-whole-greek-game-2015-4>