

Weekly Economic Commentary – Sep 13, 2015

Markets

Another week of heightened volatility in stock markets ahead of the momentous Fed decision on rates. In mid week, in the wake of a strong two-day rebound in the Shanghai Composite, the MSCI Asia Pacific Index jumped the most since 2009 (with the Nikkei up 7.7% in a day). Wall Street was also on fire after the Labor Day weekend, with the three major indices – S&P 500, Dow Jones and Nasdaq Composite – scoring their second biggest two-day gains of 2015. Regional markets were also part of the frenzy, with the exception of Egypt. The euro registered a notable gain versus major crosses, as USD bears bet on the Fed dovishness. Oil prices fell sharply on Friday, erasing the rally a day earlier, on the wake of a stronger USD and KSA's dismissive remarks over a producers' summit. Gold prices retrenched despite global uncertainty.

Global Developments

US/Americas:

- **US wholesale inventories** decreased by -0.1% mom in Jul compared to +0.2% in Jun. Meanwhile, sales dropped -0.3% mom in Jul, vs 0.2% in Jun. The inventory-to-sales ratio held steady at 1.3.
- The preliminary University of Michigan **consumer confidence index** in Sep fell 6.2 points to 85.7, the lowest for 2015, well below the consensus and the third consecutive monthly decline. Current economic conditions and consumer expectations were weak due to the stock market vagaries.
- **US PPI inflation** in Aug was flat mom, down from 0.2% in June.

- **Initial unemployment claims** fell 6,000 to 275,000. The four-week moving average rose 500 to 275,750.
- **S&P cut Brazil's investment grade credit rating** from BBB-minus to BB-plus, i.e. junk status with negative outlook, further pushing the country towards a debt crisis spiral.

Europe:

- The **euro zone's real GDP** growth slowed marginally to 0.4% qoq in Q2 from a revised 0.5% in Q1, and 1.5% yoy.
- **Germany's CPI** rose 0.1% yoy in Aug, following a 0.3% increase in Jul. **Spain's CPI** fell -0.4% yoy in Aug, down from a 0.1% gain in both Jun and Jul as a result of lower transport and utility prices.
- **German industrial production** rose 0.7% mom in Jul, offsetting a revised -0.9% mom decrease in Jun. **UK industrial production index** fell -0.4% mom (0.8% yoy) in Jul after retreating -0.4% (1.5% yoy) in Jun; **Italy's industrial production** rebounded in July, with output rising 1.1% mom after a revised -1% mom drop in Jun; **France industrial production** fell -0.8% mom in Jul, following a no-change in Jun; **Spain's industrial production** strengthened to 5.6% in Jul from Jun's 4.8%.
- **The UK goods trade deficit** rose to GBP -11.1bn in Jul from GBP -8.5bn in Jun.
- **Germany's trade surplus** widened to EUR 22.8bn in Jul from EUR 22.1bn in Jun, expanded from EUR 21.4bn in Jul 2014.
- **The UK house price index** was up 2.7% mom (9% yoy) in Aug, following a contraction mom (7.8% yoy) in Jul.

Asia and Pacific:

- **China's CPI** rose 2% yoy in Aug, following a 1.6% increase in Jul, driven by higher food prices.
- **Chinese exports** fell -5.5% yoy in Aug better than expected, while imports fell a more than expected 13.8%

yoy.

- **China's PPI** continued its free fall by -5.9% yoy in Aug. after a -5.4% decline in Jul.
- **Japan's Q2 GDP** recorded a -0.3% qoq contraction, an uptick from the initial estimate of -0.4% and following a strong 1.1% gain in Q1.
- **Japan's consumer confidence index** rose to 41.7 in Aug. from 40.3 in Jul. Yet the index has a long way to rebound toward the neutral 50 level, which is unlikely without stronger wages growth.
- **Japan's machinery orders** shrank -5.6% mom in Jul, beyond all market expectation. The upset continued after falling by -7.9% in Jun.
- **India's industrial production** expanded 4.2% yoy in Jul. down from a revised 4.4% gain in Jun. Manufacturing softened while the mining and electricity sectors accelerated.
- **New Zealand's central bank** cut its rate for the third time in a row by 25bps to 2.75% and asserted that a further slowdown in China would warrant more cuts.
- **South Korea's unemployment rate** fell to 3.6% in Aug from 3.7% in Jul, but weak external conditions are expected to discourage hiring in coming months.
- **Taiwan's inflation rate** decreased -0.5% yoy in Aug, just a notch from Jun's revised -0.6% decline. Transportation and utility costs sunk due to oil prices.

Bottom line: The data flow was rather scant, so the macro picture has not changed much. China continues to slow, hitting severely emerging economies while Europe and the US seem to have been so far resilient, but hardly picking up. The Fed decision on interest rates adds another dose of uncertainty, because the fragility of the financial architecture is an imponderable risk and even a small shock, despite having been announced for months, could prove highly detrimental for those areas of the markets (e.g. EM fixed income and US junk bonds) that are highly leveraged and irresponsibly overstretched.

Regional Developments

- **Bahrain's banking sector** is expected to remain resilient despite the impact of lower oil prices, according to Moody's. Loan growth is expected to remain stable at around 4% this year, similar to past two years, while funding growth would be supported by infrastructure investment in the GCC. Though NPLs are relatively high compared to its GCC peers, the average NPL is expected to be in the range of 6-6.5% of total loans by mid-2016.
- Urban consumer **inflation** in **Egypt** dropped to 7.9% in Aug (Jul: 8.4%), the slowest in 2 ½ years, and core inflation was down to 5.61%, down from a high of 8% in May.
- **Egypt's current account deficit** widened to USD 12.2bn in the 2014-15 fiscal year from USD 2.7bn the previous year, as per the central bank. Separately, **foreign currency reserves** fell to USD 18.096bn at the end of August from USD 18.534bn the month before.
- **Egypt's exports to Russia** were up 22% yoy in 2014, according to a Cairo Center for Economic and Strategic Studies report; bilateral trade grew 86% to USD 5.4bn compared to USD 1.8bn in 2012.
- **Tourists** into **Egypt** were up 2.9% in Jul this year, as reported the Ministry of Tourism and the Egyptian Tourism Authority. Arab tourists were up 39.5% in Jul while tourists from UAE and Saudi Arabia increased by 65.6% and 53.1% respectively in Jan-Jul this year.
- **Egypt's cabinet** has resigned and will stay on as caretaker till a new government is formed. Egypt is planning to hold its long-delayed parliamentary elections next month.
- As **Iraq** began its roadshow for a **sovereign international bond issue**, its prospectus revealed that **GDP** shrank by 6.7% yoy in Q1 this year. The prospectus also lists that total public debt rose to USD 39.5bn at end-Jun from USD 33.3bn at the end of last year. Iraq's sovereign credit

ratings, from both Standard & Poor's and Fitch, are at B-minus, six notches below investment grade.

- **Jordan** will launch a package of **economic reforms**, including new investment and tax legislations, as the government seeks to attract investments of close to USD 20bn to spur growth as envisioned in the Jordan 2025 Blueprint released earlier this May, according to the Minister of Planning and International Cooperation.
- **Jordan** and **China** have inked a multiple memoranda of understanding (**MoU**), worth around USD 7bn, to bolster economic, trade and investment cooperation. Deals signed include a USD 1.7bn financing agreement with Attarat Power Company and a USD 2.8bn agreement to fund the Jordanian national railway network scheme.
- Seismic surveys conducted by the **Kuwait** Oil Company has revealed large quantities of **crude oil** in several strategic areas that could potentially increase the country's production levels to 3.3mn barrels in two years, *Al Khaleej* reported. Kuwait's current production rate is around 2.9mn barrels per day.
- **Kuwait banking sector** reported double-digit asset growth in 2014, its highest rate in the last seven years, rising 12.2% yoy to KWD 66.4bn. Loan growth was driven mainly by strong demand for infrastructure project financing and retail banking, according to Fitch.
- **Lebanon's balance of payments** posted a deficit of USD 1.32bn in Jan-Jul this year compared to a surplus USD 131mn in the same period a year ago, according to the central bank.
- **Non-tax revenues in Oman** in 2014 stood at OMR 1.983bn compared to OMR 1.931bn in 2013.
- **Oman's telecom sector** grew 7% yoy in 2014, generating a total revenue of OMR 803.544mn as compared to OMR 749.252m in 2013.
- **Net domestic credit** in **Qatar** grew by 32.1% yoy to QAR 567bn in Jul, as per latest central bank statistics. Money supply, as denoted by M2, continued to grow,

rising 8.7% yoy to QAR 519bn.

- **Qatar**'s finance minister stated that the country, given its strong government finance buffers, would not scale back economic development projects or cut state fuel and food subsidies in response to low oil and natural gas prices.
- **Qatar**'s ratio of **nationals to expats in private sector jobs** is markedly lower than other GCC nations, as per an IMF paper focused on private sector employment for nationals and expatriates in the GCC. Qatar has a little more than 12k nationals in private sector, while Saudi's top the GCC (excluding UAE) list with a total of 16,56,000 persons.
- **Qatar**'s central bank will grant **licences to GCC banks** to open branches in the state, it was announced last week.
- The **IMF** released the **Article IV** for **Saudi Arabia**, in which it calls for the country to reduce domestic energy subsidies and its public sector wage bill. It is estimated that 2015 GDP growth will be 2.8% while the government's fiscal deficit will be around 20% of GDP this year.
- The **cost of living** index in **Saudi Arabia** was up 0.4% mom and 2.1% yoy in Aug.
- **Saudi Arabia** plans to **ease restrictions** on foreign investors to let them own 100% of **retail and wholesale businesses** versus upto 75% permitted currently; this was revealed by the Saudi Arabian General Investment Authority (SAGIA) to US businessmen during a visit by King Salman to Washington.
- **Saudi** officials were "seriously" thinking about reducing **fuel subsidies** gradually, reported Reuters, citing a source in the Gulf oil industry.
- **Saudi Arabia**'s finance minister revealed during a TV interview that the government is "**cutting unnecessary expenses**" and **delaying some projects** to compensate for low oil prices, though projects significant for the economy would go ahead.

- **GREs** in the **GCC** are turning to **banks to finance its infrastructure projects**, rather than opt for state-funding, revealed Societe Generale's chief regional officer for the Middle East. He said that the bank hence had "a very good pipeline of projects" for this year and next in the Gulf.
- The **Middle East** currently **imports** about USD 35bn worth of **food** annually, and this looks set to double to USD 70bn in two decades, thanks to population increases and climate change, revealed an official from the International Center for Agricultural Research in the Dry Areas.

UAE Focus

- **Private sector growth** in **Dubai** accelerated in Aug, as the Emirates NBD Dubai Business Activity Index rose to 57.6 in Aug, up from July's 40-month low of 53.1, thanks to strong output increases and new orders. However, confidence towards the 12-month business outlook moderated for the second month in a row in Aug.
- The World Bank expects **UAE** to record **budget surpluses** of 0.2% and 1.5% in 2016 and 2017 respectively, after an estimated deficit of 2.9% this year. Separately, it was revealed that the Ministry of Finance, with the help of the World Bank, will develop a **Fiscal Coordination Unit** in order to better coordinate between different government sectors.
- **UAE population** was 9.3 million at the end of 2014, according to the Ministry of Health; last week a senior Health Ministry official disclosed that the population is "closer to 10 million", without elaborating further.
- **DIFC** reported that the number of active registered **companies** in the centre was up 8.3% to 1327 while the total number of employees grew 4.8% to 18,521.

Media Review

Low interest rates are not the cure – they are part of the

problem

<http://www.ft.com/intl/cms/s/0/619b139c-3ce4-11e5-8613-07d16aad2152.html#axzz3lDiS1TEW>

US Fed: To hike or not to hike

<http://seekingalpha.com/article/3506786-weighting-the-week-ahead-to-hike-or-not-to-hike>

IMF Article IV report on Saudi Arabia

<http://www.imf.org/external/pubs/ft/scr/2015/cr15251.pdf>

China's Forex Follies: Barry Eichengreen

<http://www.project-syndicate.org/commentary/china-forex-follies-by-barry-eichengreen-2015-09>

10 most important economic charts last week

<http://qz.com/500467/greenbacks-redbacks-and-the-back-half-the-10-most-important-economic-charts-of-the-week/>

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