

# Weekly Economic Commentary – Jul 3, 2016

## Markets

*The post-Brexit hysteria is ebbing in stock markets where investors, after a cooler assessment of the repercussions, drove major indices sharply high. Regional markets followed the global trend led by the UAE bourses. The heightened tension however continues to drive the fixed income markets, where the global rally in government bonds hit new highs on Friday. The US 30-year bond yield plunged as much as 10bps to a new low 2.1873%, while benchmark 10-year Treasury yields slid to a low of 1.3784%. The rally triggered as a flight to safety post-Brexit vote has induced an unprecedented buying spree. In FX markets major crosses were essentially stable, but the GBP continued to sink. Oil prices recovered some of the ground lost in previous weeks while gold remains well bid by investors in search of a safe heaven.*

## Global Developments

### US/Americas:

- **US ISM PMI** came in at 53.2 in Jun, up from 51.3 in May, beating expectations of 51.4. It is the highest reading since Feb 2015, as new orders growth accelerated and employment expanded for the first time since Nov.
- **US final Markit Manufacturing PMI** came in at 51.3 in June , slightly below a preliminary reading of 51.4 but substantially above May's 50.7.
- **US sales of previously-owned single family homes** in May fell -3.7% mom and -0.2% yoy sa, the first yoy drop since Aug 2014.
- **US jobless claims** rose to 268K, compared to 258k in the previous week. The figure came in slightly above market expectations of 267,000.
- **US GDP expanded** an annualized 1.1 % qoq ann in Q1,

according to the final estimate, higher than a second estimate of 0.8 %, and 1.4% in Q4. Consumption continued to support growth although it expanded less than expected, while exports and software investment rebounded.

- **US personal spending** rose 0.4 % mom in May, after 1.1 % in Apr., thanks to demand for both goods and services. Income rose 0.2% mom, slightly below expectations.

## Europe:

- The seasonally adjusted **annual growth of the eurozone's M3** money supply was 4.9% yoy in May, up from 4.6% in Apr.
- **Standard and Poor's cut the EU rating** following the UK's Brexit vote from AA+ to AA expressing concerns on "cohesion within the EU".
- **The euro zone's economic sentiment indicator** dipped to 104.4 in June from 104.6 in May.
- **The euro zone's unemployment rate** was 10.1% in May, down 0.1% from Apr and from 11% a year earlier.
- **UK consumer confidence** remained steady at -1 in Jun, in negative territory for the third month in a row.
- **The UK Nationwide Housing Price Index** increased 0.2% mom (5.1% yoy) in Jun, following the same increase in May (4.7% yoy).
- **The Bank of England injected** GBP 3.1bn into the domestic banking system after the vote to leave the EU.
- **Italy's consumer confidence** index decreased to 110.2 in Jun from 112.7 in May, the third monthly decline. However **business sentiment of manufacturers** increased to 102.8 in Jun from 102.1 in May as the order books improved.

## Asia and Pacific:

- **Consumer prices in China** rose 2.0% yoy May, slowing from a 2.3 % rise in the previous three months and below

market consensus. Food prices increased by 5.9% while non-food items rose at a slower 1.1% pace. Cost of consumer goods gained 2.0 % and those of services advanced 2.1%

- **Retail sales in Japan** plunged 1.9% yoy in May, from worse than -0.9% in Apr, the worst result since a -9.7% tumble in Mar 2015.
- **Taiwan's central bank** cut its benchmark rate to 1.375% from 1.5%, citing economic volatility in the wake of Brexit.
- **Exports from Hong Kong** fell for the 13th consecutive month by -1% yoy in May, up from the Apr's reading of -2.3%. Imports contracted -4.3% yoy, almost similar to Apr's -4.5%. The trade deficit was HKD 26.2 bn.
- **Malaysia reported** a MYR 3.3bn trade surplus in May, down from MYR 5.51bn surplus a year earlier and way below market consensus of MYR 8.7bn.
- **South Korea inflation** rose 0.8% yoy in Jun, the same as in May. While prices of food and transport declined, housing and utilities prices were stable.

**Bottom line: The data flow last week did not change significantly the global outlook. Brexit, for good or for bad, continues to dominate the financial markets price action and tops the list of worries on trading floors. Brexit per se does not carry the threat of an unmanageable disruption; nevertheless, given the fragile economic conditions, clumsy policy making in large economies and the still high leverage in financial markets (the IMF and the Fed pointed fingers at Deutsche Bank for its irresponsible exposure on derivatives) any shock can set in motion a snowball effect.**

### **Regional Developments**

- **Fitch downgraded Bahrain** to BB+ (one notch from BBB-), while maintaining outlook as "stable". Lower oil prices, resulting in wider budget deficits and rising government debt leading to a weaker financial position were cited

as factors for the downgrade.

- **Egypt** plans to issue a USD 3bn **Eurobond** between Sep and Oct this year, according to the finance minister, and also implement the long-delayed value-added tax (**VAT**) by Sep.
- **Egypt's non-petroleum exports** grew 3% yoy to USD 8.4bn in Jan-May this year. Exports to EU grew by 7% to USD 2.2bn while exports to Arab states grew 6.6% to USD 3.8bn.
- **Egypt's** parliament approved the government's 2016-17 **draft budget**, which estimates total expenditure of EGP 936bn and revenues of EGP 631bn. The draft budget shows total subsidy at EGP 130.1bn (down around 14%), of which EGP 46.3bn are allocated for food and farmers' subsidy.
- Reports of **Egypt** seeking an **IMF loan** worth USD 5bn has been squashed by the central bank governor, who stated that "we have not filed an official request for a programme" and said that the governor of the CBE is the only individual who can act as a representative for Egypt in discussions with the IMF.
- **Egypt repaid** the last USD 1bn installment received previously from **Qatar**; Egypt is also expected to repay USD 800mn of debt to the Paris Club of creditor countries next July, according to a central bank official.
- An **Egyptian** court **suspended** the implementation of a **central bank decree** to limit the terms of bank chief executives to nine years. If the decree were to be enforced, eight of the country's banking heads would have been removed from their jobs.
- **Electricity consumption** in **Kuwait** hit a **new record** for daily use last week by reaching 12,900 megawatts versus previous high of 12810 MW reached last summer. The ministry had raised the daily production capacity to 13,000 megawatts before the beginning of summer, while an additional 2,000 megawatts can be added through emergency generators.

- **Kuwait** agreed to postpone **Iraq's debt repayment** by one year, revealed the Kuwaiti ambassador to Iraq.
- **Lebanese banks** deposited USD 7bn at the central bank in 2015, to boost foreign currency reserves, stated the head of the Association of Banks in Lebanon. He also stated that bank loans to the private sector increased by 6.5% to USD 3.3bn last year.
- The Producer Price Index (**PPI**) of **Qatar's** Industrial Sector for April 2016 grew 1.6% mom to 43.8 points, largely due to the improvements in "mining" (+1.1% mom) and "manufacturing" (+2.4% mom) sectors.
- **Saudi Arabia's net foreign assets** grew by a modest 0.1% mom to SAR 2.148 trillion in May, recording the first mom increase since Jan 2015. This might have been due to the USD 10bn syndicated loan it obtained from banks in end-Apr. Deposits with banks abroad grew 9.3% mom to USD 141.2bn; investments in foreign securities dipped 3.4% to USD 373.1bn.
- **Saudi Arabia's non-oil GDP** is expected to slow to 2.8% yoy this year (2015: 3.4%), according to the central bank governor. He disclosed that the point-of-sale aggregate, an indicator of consumption, had increased by 15% yoy in May.
- **Saudi Arabia's** Capital Market Authority **raised** the **commission on trades on Tadawul** from 12 basis points to 15.5 basis points per transaction; it also eliminated the fixed commission on equity transactions equal to or less than 10,000 riyals.
- **Saudi Electricity Co** obtained USD 1.5bn in financing from Industrial and Commercial Bank of China (**ICBC**). This unsecured, 5-year "direct commercial funding agreement" is one of the largest loans extended by a Chinese bank in the GCC.
- **Saudi Arabia** has chosen Citigroup, HSBC and JP Morgan to manage its **debut sovereign bond issue**, reported Reuters, citing sources knowledgeable of the matter. The size of the issue is expected to be about the same as the

largest-ever emerging market debt sale – Argentina’s USD 16.5bn issue in April – and larger than Qatar’s USD 9bn deal in May (currently the largest bond from the GCC).

- **Private wealth** in the **Middle East and Africa** region is set to reach USD 11.8trn by 2020, according to BCG. UAE, Saudi Arabia, and Kuwait together account for 22.7% of that sum.
- Dubai (48) retained its position as the most transparent real estate market in **MENA region** in the 2016**Global Real Estate Transparency Index**, with Abu Dhabi (59) following closely. Saudi Arabia, at 63rd, finished in the ‘Semi-Transparent’ category for the first time.

## **UAE Focus**

- **Abu Dhabi** plans to **merge** state investment funds **Mubadala** Development Company and International Petroleum Investment Company (**IPIC**). The new fund is estimated to have combined assets worth USD 135bn.
- **Abu Dhabi** state investment fund International Petroleum Investment Co (**IPIC**) reported a net loss of USD 2.6bn last year and compares to a profit of USD 1.5bn the year before. The loss was due to weaker lower oil prices, which reduced revenue by 30% to USD 35.8bn.
- Investment Corporation of Dubai (**ICD**) posted a 3.6% dip in **profits** last year; oil revenues were down 30% to AED 49.6bn. During the year, distributions totalling AED 6.86bn were made to the government, up from AED 2.77bn in 2014, though no reasons were given for the increased payment.
- **Dubai**’s Roads and Transport Authority (RTA) awarded a AED 10.6bn contract to **expand the metro** system to reach the Expo 2020 site. Work will start later this year and a trial run is expected in end-2019, with operations set to begin five months prior to the Expo. The government will self-fund the project for the initial 6 months – to the tune of AED 1.5bn – while studying other funding

options for later.

- **Mortgage lenders** in **Dubai** disbursed AED 3.8bn in May versus Apr's AED 2.5bn. Bulk of the mortgage-supported deals involved ready properties or those nearing completion.
- **Dubai's RTA** is expected to tender for projects worth AED 4bn within eight months, as part of plans to **upgrade transport links** in the city. The Chairman of the RTA also revealed that they were studying whether to increase road tolls within three years to pay for the transportation upgrades.
- The **Dubai International airport** welcomed 6.7mn **passengers** in May, up 7.2% yoy, and bringing the year-to-date figure to 34.65mn (+7.0%). The airport is expecting "near record numbers" in the coming weeks, on seasonal peak travel, according to Dubai Airports.
- **Private wealth** in the **UAE** is projected to reach almost USD 1 trillion in 2020, at a compound annual growth rate (CAGR) of 14.1%, according to Boston Consulting Group. The wealth breakdown is expected to be 19.2% in equities, 12.1% in cash and deposits, and 4.8% in bonds.
- The **Dubai** government has saved AED 4.3bn through **shared smart services** between 2003-2015, announced Smart Dubai Government (SDG), citing 'Shared services impact report' – a six-month study compiled by IBM. The study found that the Dubai Government saved AED 5.6 for every AED 1 spent by SDG since its inception. Last year saw the highest cost-to-savings ratio of all time: SDG saved the Government an average AED 35.5mn every month.
- **UAE hotel revenues** declined in May, mainly due to the decline in average room rates, according to EY: in Dubai, revenue per available room declined by 7% yoy to AED 682 in May while in Abu Dhabi it was down 8.9% to AED 341.
- A consortium led by Abu Dhabi's Masdar is aiming to raise an USD 800mn loan to finance the building of the 800-megawatt third phase of **Dubai's solar park**. The

consortium, which also includes Spanish companies Fotowatio Renewable Ventures and Gransolar Group, submitted the lowest generation price to build the plant at 2.99 cents per kilowatt-hour.

- Dubai World Trade Centre (**DWTC**) **events** contributed AED 12bn in retained value towards Dubai's economy – equivalent to 3.1% of Dubai's GDP – last year, according to the Economic Impact Assessment report. The DWTC attracted 2.6mn attendees last year at its 104 large-scale events, of which 1.19mn were from overseas. International visitors to business events at the DWTC stayed on average six days and spent nearly AED 8,268 during their visit – nine times the average spending of UAE-based attendees.

## **Media Review**

### **Brexit: an uncertain future for the financial capital of Europe**

<http://www.economist.com/news/finance-and-economics/21701509-britains-vote-quit-means-uncertain-future-financial-capital>

### **Collateral damage: Brexit & Asian economies**

<http://qz.com/717494/brexit-is-almost-certain-to-push-hong-kong-into-recession-in-2016/>

### **Global Wealth 2016: Navigating the New Client Landscape (BCG report)**

<https://www.bcgperspectives.com/content/articles/financial-institutions-consumer-insight-global-wealth-2016/>

### **Statistics fog raises risk as cheap oil hits Gulf**

<http://www.reuters.com/article/gulf-economy-statistics-idUSL8N19E0RK>

### **Reform wave primes the pump on Saudi Arabia property investment**

<http://www.thenational.ae/business/property/reform-wave-primes-the-pump-on-saudi-arabia-property-investment>

### **Growing headwinds for UAE banks, but merger talks give hope**

<http://www.thenational.ae/business/banking/growing-headwinds-for-uae-banks-but-merger-talks-give-hope>

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