

Weekly Economic Commentary – Apr 2, 2017

Markets

Last week started with Wall Street still badly digesting the Obamacare repeal fiasco, but strong consumer confidence data lifted stocks on Tuesday and the main US indices ended the week more or less unchanged. European shares shrugged off the formal triggering of the Art. 50 procedure for Brexit., but elsewhere, in Japan and in emerging markets (including regional markets), stocks were generally weaker, as the prospects of a more hawkish Fed sapped optimism. Taking a broader perspective, global stock markets had a bumper first quarter: the Nasdaq Composite in particular recorded its best quarter since end-2013 climbing 10%, thanks to technology stocks. In currency markets, the yen reinforced its upward trend, while the dollar was down on major crosses. The GBP avoided a further slide, despite the formal opening of the Brexit procedure. Oil price recorded their largest weekly gain on the year, as data on US oil inventories came slightly below expectations (but still 6.0% higher than last year) and fuel inventories dropped substantially. Gold prices remained resilient, as some investors continue to be concerned by the geopolitical tensions and the entrenched political uncertainty in the US and Europe.

Global Developments

US/Americas:

- **The final revision of Q4 US GDP** set the growth rate at 2.1% qoq ann vs the 1.9% preliminary figure. Consumer spending, which gained 3.5% was the main growth factor.
- **Markit flash US manufacturing PMI** fell to 53.4 in Mar from 54.2 in Feb.

- **The US PCE Deflator** rose 0.1% mom (2.1% yoy) in Feb vs 0.4% in Jan due to falling energy prices. The core PCE deflator rose 0.2% (1.8% yoy) in Feb.
- **US nominal personal income** rose by a solid 0.4% mom in Feb vs 0.5% in Jan. Wages and salary grew by 0.5% mom.
- **S&P CoreLogic Case-Shiller US home price index**, showed that in Jan existing home prices rose 5.9% yoy vs 5.7% in Dec, touching a 31-month high. Growth in the 10-city composite index increased by 5.1% yoy from 4.8% in Dec.
- **The pending US home sales index** rose 5.5% mom in Feb after slumping -2.8% in Jan. However in yoy terms the index fell -2.4%.
- **The Conference Board's Consumer confidence index** jumped from 116.1 in Feb to 125.6 in Mar. The present situation index climbed from 134.4 to 143.1 and expectations from 103.9 to 113.8. The labor market conditions index rose from 7 to 12.2, a new cyclical high.
- In Feb **US wholesale inventories** grew by 0.4% mom, following a -0.2% drop in Jan. Retailers continued to expand stockpiles with a 0.4% increase after a 0.9% surge in Jan.
- **US initial unemployment insurance claims** declined from 261,000 to 258,000. The 4-week moving average rose from 246,500 to 254,250, while continuing claims increased 65,000 to 2.052 mn.

Europe:

- **Eurozone's M3 money supply growth** slowed to 4.7% yoy in Feb from 4.8% in Jan due to weak M1 growth.
- **Eurozone's inflation** retrenched to 1.5% yoy in Mar from a 4-year high of 2% in Feb. Core inflation slowed to 0.7% yoy from 0.9% in Feb.
- **The Conference Board Leading economic index for the eurozone** increased 0.5% mom to 109.2 in Feb. **The Coincident index** advanced 0.1% mom to 103.4.
- The **eurozone's economic sentiment indicator** was almost

flat at 107.9 in Mar vs 108 in Feb, which represents a six-year high.

- **Italy's new Industrial orders** plunged -2.9% mom (-8.6% yoy) in Jan, erasing the 3% rise in Dec.
- **Inflation in Germany** fell to 1.6% yoy in Feb from 2.2% per cent in March as the energy prices slowed down.
- **German retail sales** in Feb grew 1.8% mom more than offsetting the -1% drop in Jan.
- **The German Ifo business climate index** gained again ground in Mar to 112.3 from 111.1 in Feb. Entrepreneurs are increasingly confident about the current situation and the near term outlook.
- **UK consumer confidence** was flat at -6 in Mar, as consumers express pessimism over the economic outlook and their personal finances.
- **The UK Nationwide Housing Price Index** rose only 3.5% yoy in Mar from a 4.5% in Feb. In mom terms the indicator lost -0.3% the first decrease in 21 months, underscoring that housing market will feel the strain of Brexit in 2017.

Asia and Pacific:

- **China's central bank hiked rates** for overnight standing lending facility loans, which are used mainly by small- and medium-sized financial institutions by 20 bp to 3.3%. In addition, the PBOC raised the rate for 7-day loans to 3.45% and the 1-month rate to 3.8%.
- **China's official manufacturing PMI** rose to 51.8 in Mar, from 51.6 in Feb. The advance involved all key components like new orders, output and hiring.
- **Japan's core inflation** rose 0.2% yoy in Feb, from a 0.1% in Jan due to higher imported goods prices resulting from the weak yen.
- **Japan's industrial production shot up** 2% mom in Feb, after a -0.4% slide in Jan, boosted by the yen devaluation which lifts the export-oriented sectors.

- **Japan's retail sales** rose 0.1% yoy in Feb, after the 1% jump in Jan. Sales of general merchandise and food items weighed on the headline figure.
- **South Korean economy** expanded 0.5% in Q4 slightly above preliminary estimates of a 0.4%.
- **South Korean industrial production** rose 6.6% yoy, in Feb vs 1.4% yoy in Jan, in the wake of higher electronics and automotive output.
- **South Korean retail trade** rebounded by 3.2% mom in Feb after a 2% mom drop in Jan. Durable goods were upbeat, with car sales rising 4.9% mom.

Bottom line: As the saying goes, bull markets are born on pessimism, grow on skepticism, mature on optimism, and die on euphoria. Exuberant consumer confidence, together with irrational investor sentiment, valuation, and price extension, push stock indices to peaks, that prove to be unsustainable unless real growth ensues. Data from surveys are convincing investors that the global growth has accelerated late in 2016 and in early 2017. However, hard data indicate that the expansion pace is solid, but not outstanding as highlighted by the US GDP data. Actually data point to a little softening in Q1, while the reflation is entirely due to oil prices, not to global demand rebound. Uncertainty in key areas are not being dispelled. In Europe political clouds will persist until the German elections in September, while in China the riskiest corporate borrowers are raising a humongous amount of debt overseas, with global investors piling up credit risks despite defaults quadrupled in 2016.

Regional Developments

- **Egypt's proposed 2017-18 budget** (approved by the cabinet, yet to be passed by Parliament) forecasts 9.1% budget deficit, compared to an expected 10.5-10.7% this financial year; the budget proposes a 20% hike in expenditure to EGP 1.188trn while revenues are expected at EGP 818bn (of which tax revenues are estimated at EGP

604bn or 74% of total revenues). Spending on food subsidies is seen rising to EGP 62.6bn next year, vis-a-vis EGP 49.5bn expected in 2016-17. Sources also disclosed that food subsidies may be raised by 29% to EGP 27 per person to ease the impact of rising prices.

- According to **Egypt's** finance minister, the country is planning a **return to international markets for financing** by the end of 2017 or early 2018. **Egypt lowered the customs exchange rate** to EGP 16.5 per dollar i.e. around 10% less than the price of the dollar in banks (starting Apr) in a bid to reduce inflation. Separately, the finance minister stated that inflation is expected to ease by Nov or Dec this year.
- The **central bank of Egypt** kept **policy rates unchanged** for the fourth consecutive meeting: overnight deposit rate are at 14.75% and overnight lending rate at 15.75%.
- **Egypt** expects to halve **arrears** (currently around USD 3.5bn) with **oil companies** in the coming weeks, according to the oil minister.
- **Egypt's** trade and industry ministry plans to **raise exports to USD 34bn by 2020**, from USD 19bn, by "implementing specific export plans and policies and targeting new export markets".
- With **Egypt's** VAT rate rising to 14% in the coming fiscal year starting Jul, **revenues from VAT** are expected to rise by EGP 7-8bn during 2017-18, according to the deputy finance minister.
- **Deposits from the Gulf to Egypt's** central bank have fallen to USD 2bn during 2016, from USD 31bn in 2011, revealed the central bank governor.
- **Egypt** witnessed an inflow of USD 3.1bn of **foreign investment in domestic debt instruments** since the EGP floatation till mid-Mar.
- **Iraq** has reduced its **oil output** by more than 300k barrels per day (bpd) to 4.464mn bpd average in Mar, with crude exports average till last week of Mar is around 3.756mn bpd.

- **Bilateral trade** between **Jordan and Saudi Arabia** stood at USD 5bn in 2016. Saudi Arabia is Jordan's third major trade partner after US and Iraq. Saudi investments, at USD 3bn, accounts for 54% of investments from the GCC in Jordan.
- **Kuwait** delays enforcement of **selective tax policy** until mid-year, without stating any reasons. The *Al Seyassah* daily reported that the finance ministry was ready to go ahead with implementation.
- **Kuwait** will **import fuel oil** to meet electricity generation needs for about a year, to offset part of the production decline due to the closure of the Shuaiba refinery from Apr and until the al-Zour refinery starts running in 2019. Kuwait needs 120k barrels per day (bpd) of fuel oil in the summer and 70k bpd in winter to generate power.
- **Lebanon's budget** – which forecasts spending of LBP 23.67trn (USD 15.7bn) and revenues of LBP 16.38trn – was approved by the Cabinet; this is the first Lebanese state budget in 12 years and it aims to reduce the deficit to 8.7% of GDP in 2017 from 9.3% last year. The budget will not become law until it is also approved by the country's parliament.
- **Lebanon's PM**, who stated that the country is near "breaking point" over the **Syrian refugee crisis**, urged the international community to commit to spending the equivalent of USD 10-12,000 per refugee over a period of five to seven years, compared to the current level of foreign support equivalent to USD 1-1,200 per year.
- **The weighted average interest rate of OMR deposits** increased to 1.582% in Jan from 0.948% in Jan 2016. The weighted average OMR lending rate increased to 5.104% from 4.76%.
- **Oman's central bank** has signed an MoU with the Iranian central bank to strengthen financial and economic cooperation between the two countries.
- **Qatar will invest GBP 5bn in Britain** over the next three

to five years, revealed the country's minister of finance. Separately, the CEO of the Qatar **Investment Authority** stated at an investment conference that opportunities exist in a post-Brexit Britain, and that infrastructure, healthcare and technology were a few key sectors.

- Shareholders in UK's Heathrow airport – Qatar holds 20% – will invest GBP 650mn over the course of 2019, according to the CEO of the airport.
- **Qatar's population** grew by 5% yoy to over 2.6 million at end-Feb, according to a monthly report issued by the Ministry of Development Planning and Statistics.
- **Saudi Arabia** reduced the **tax rate for Aramco** to 50% from 85% as part of preparations for the upcoming IPO; this will be implemented retrospectively effective Jan 1, 2017. Rystad Energy reported that this move increases the valuation of the company from USD 0.4 trn to USD 1.4trn, assuming long term oil prices averaging USD 75 per barrel.
- **Saudi Arabia's net foreign assets** fell by USD 9.8bn from the previous month to USD 506.9bn in Feb, recording the lowest level since Aug 2011.
- **Bank lending** to the private sector in **Saudi Arabia** slowed to 0.3% yoy in Feb (Jan: 1.8%); cash withdrawals from ATMs, a proxy for consumer spending, dropped to the lowest level for more than a year in Feb.
- **Saudi Arabia** announced a **Jordanian venture** of the **Public Investment Fund**: creation of an investment firm (initially with USD 10mn of capital, which may rise to as much as USD 3bn in the long term) that would pursue real estate, energy, tourism and infrastructure projects in Jordan. The PIF will own 90% of the new investment firm Saudi-Jordanian Investment Fund Co., with the remainder being held by 15 Jordanian banks.
- **Saudi Arabia's** Riyadh is likely to earn SAR 4.7bn in revenue from the already implemented **white land tax**, according to the Arabic daily *Al-Eqtisadiah*. The Housing

Ministry is scheduled to implement the tax from early this month in Jeddah and by end-Apr in Eastern Province.

- The number of **women working in the private sector** in **Saudi Arabia** increased to 496k in 2016 (an average of 8,500 jobs per month), from 215k in 2012, reported the Arabic daily *Al-Eqtisadiah*. Women now account for 30% of the total Saudi workforce in the private sector, up from 12% in 2011.

UAE Focus

- Speaking at the world's first Global Manufacturing and Industrialisation Summit (GMIS), the **UAE** economy minister revealed that the country is aiming to attract USD 75bn into its new **industrial manufacturing sector** by 2025. He also stated that Emirati investments in the industrial sector amounted to AED 112bn in 2016, accounting for 86% of the total investments in this sector.
- **UAE bank credit to the industrial sector** grew by 190% to AED 70bn over the past decade, accounting for 4.8% of the total loans channelled to business sectors by end-2016.
- **Fuel prices** in the **UAE** have been reduced for the month of Apr – the first decrease this year. Prices are down by 3.9-4.3% mom depending on the grade of petrol while diesel prices were down 3.4%.
- **UAE** has reduced **oil production** by more than 200k barrels per day (bpd) in Mar, according to the energy minister; he also stated that the plans were to cut production by more than 139k bpd this month and next. Separately, the UAE's average bpd oil production reached 3.089mn in 2016, according to the ministry of energy statistics, hitting an all-time high of 3.22mn in Dec.
- **Nasdaq Dubai** plans to introduce **two equity futures** this month – Dubai Investment Company and Dubai Financial Market contracts – taking the total number of shares to

11 from the current nine.

- **Passenger traffic at Dubai international airport** grew by 8.8% yoy to 6.95mn persons in Feb, bring total year-to-date to 14.99mn persons (+9.3% yoy). The UAE Cabinet decision to grant **Indian passport holders** with either a valid US visa or a green card, a visa on arrival is likely to boost numbers further.
- **China's tourist arrivals to Sharjah** grew by 63% yoy in 2016, with the country now the sixth largest source of tourists to the emirate.
- UAE's National Bank of Abu Dhabi (**NBAD**) has issued the **Gulf region's first green bond**, raising USD 587mn for projects in renewable energy, energy-efficiency, green transport and waste water treatment.
- The **UAE healthcare sector** is expected grow by 60% in the next five years to over AED 103bn in 2021, according to a report by MENA Research Partners.

Media Review

China's influence on global finance as the US retreats

<https://www.ft.com/content/16edc70e-10b9-11e7-b030-768954394623>

The devastating trade war between US and China

<https://www.ft.com/content/3b49cd2a-10ad-11e7-b030-768954394623>

A correction on Wall Street would be justified

<https://www.wsj.com/articles/a-correction-now-might-not-be-so-bad-some-investors-say-1490570768>

The puzzle of gasoline consumption in the US

<https://www.bloomberg.com/gadfly/articles/2017-03-31/u-s-gasoline-demand-data-a-puzzle-for-oil-bulls>

Brexit coverage on Project Syndicate

<https://www.project-syndicate.org/focal-points/the-brexit-bulldozer>

OPEC compliance with oil curbs rises in March as UAE joins cut – Reuters survey

<http://www.reuters.com/article/us-opec-oil-idUSKBN17025Z>

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