

Weekly Economic Commentary – Aug 27, 2017

Markets

At the beginning of last week US markets recovered some ground lost in mid-August, but then worries over a US government shutdown sapped the optimism and US markets closed marginally up on the week. European and Japanese indices were mostly flat or negative. On the contrary China's bourse led a substantial gain in emerging markets and the Shanghai SSE 50 has surged 16% this year to its top in over than 2 years. Regional markets were mixed as the summer lull kept liquidity low and oil price remain confined in a range just above 50\$/b. The euro-dollar exchange rate jumped above 1.19 the highest level since Jan 2015 following Draghi's speech at Jackson Hole and reached also an 8-year record high against the GBP. Oil prices were marginally down despite US inventories falling by 3.3 million barrels and gasoline inventories by 1.2 million more than double compared to analyst expectations. The oil prices were also lifted at the end of the week as a hurricane approached the Texas shore, threatening to disrupt production. The price of gold continues to benefit somewhat from the political uncertainty in the US, rising within striking distance form \$1300/ounce.

Global Developments

US/Americas:

- **The IHS Markit US Composite PMI Output Index rose to 56 in Aug from 54.6 in Jul, the top level since May 2015, as the services sector increased the most in over 2 years (56.9 from 54.7 in Jul) while manufacturing growth slowed (52.5 from 53.3 in Jul).**
- **New orders for US durable manufactured goods**

collapsed in Jul by -6.8% mom, the sharpest drop in almost 3 years. The culprit were the highly volatile civilian aircraft orders, but also those for autos and machinery fell. However, the core capital goods segment rose +0.4% mom.

- **US new-home sales plunged** in Jul by -9.4% yoy even worse than the -8.9% in Jun. Nevertheless, the Jul median new-home price rose substantially. **Existing-home sales** fell -1.3% mom in Jul (2.1% yoy) due to a sharp drop in condo sales.
- **Initial claims for unemployment benefits in the US increased** 2,000 to 234,000, but the 4-week moving average fell 2,750. Continuing claims were steady at 1.954 mn, which confirms that the labour market is not losing steam.

Europe:

- **The IHS Markit Eurozone PMI Composite Output Index was almost stable** at 55.8 in Aug vs Jul's 55.7. The index is hovering around the maximum of the past 6 years, thanks to strong manufacturing (57.4 from 56.6 in Jul), while services growth declined somewhat to a seven-month low of 54.9 from 55.4 in Jul. Among the main countries Germany and France displayed strong performances.
- **The ZEW index of investor confidence in Germany surprisingly fell** for a third month to 10 in Aug from 17.5 in Jul. **The ZEW expectations measure for the Eurozone** fell to 29.3 in Aug from 35.6 in Jul.
- **Spain's GDP expanded** 9% qoq (3.1% yoy) in Q2 almost on par with the 0.8% qoq (3.0% yoy) in Q1. Exports growth decelerated to just 0.7% qoq after a stellar 3% jump in Q1 while private consumption gained a mighty 0.7% qoq from 0.4% in Q1.

Asia Pacific:

- **Japan's inflation** was again flat mom in Jul as in Jun (0.4% yoy as in the previous 4 months). However, **core inflation** increased to 0.5% mom in Jul from 0.4% in Jun, providing some hope to the Bank of Japan's that the reflation process might be strengthening.
- **The Nikkei Japan flash Manufacturing PMI** rose to 52.8 in Aug vs 52.1 in Jul, in the wake of brisk expansion in output and new orders, both domestic and foreign.
- **The Leading Economic Index in Japan** increased to 105.90 in Jun from 104.70 in May.
- **Bank Indonesia** cut its policy rate by 25bps to 4.5% to boost growth, which is falling way below the government's 7% target.
- **Industrial output in Taiwan** rose 4% yoy in Jul after a 3.1% in Jun, thanks to strong tech exports.
- **Hong Kong's trade deficit** shrunk to HKD 29.6bn in Jul, from HKD 48.3bn in Jun with both exports and imports recording strong performances. Most of the activity, however, was for re-export, which confirms the ongoing rebound in global trade.
- **Singapore's industrial production** surged to 21% yoy in Jul adding to the 12.7% growth in Jun. The rebound was driven chiefly by electronics, but other sectors were also performing well.

Bottom line: In a week with no major data releases, attention was grabbed by the annual Jackson Hole gathering of central bankers. A self-congratulatory mood prevailed among participants as they expressed optimism on the global recovery. Fed Chair Yellen's avoided any reference to monetary policy or inflation and focused on regulatory reforms, passionately praising those enacted to stem the financial crisis, but without giving any discernible hint on what she deems appropriate for the future. All in all, Yellen's speech was largely irrelevant for markets although some analysts have interpreted it as dovish and reduced the likelihood of a rate hike this year. Analogously, Draghi's intervention avoided

references to current policy issues, and in addition to financial regulations it stressed that free trade was key to boosting growth and stemming the fallout from adverse demographics. Nevertheless the currency markets reacted by pushing the euro further up in the belief that the lack of verbal intervention signaled that the ECB was not over concerned about the appreciation. Meanwhile senior White House sources announced that Trump is planning a major push on tax reform starting with a speech in Missouri, in an attempt to score his first notable policy result. Together with the threat of a government shutdown over the financing of the wall along the border with Mexico, the (still unspecified) tax cuts are intended to unite the Republican Party and regain the support lost since Nov.

Regional Developments

- **Egypt** expects **growth** to touch 5% this fiscal year, according to the planning minister: this is a tad higher than the finance ministry's previous forecast of 4.6-4.8%. With the new investment law passed, investments are expected at EGP 646bn this fiscal compared to EGP 530bn received last year.
- **Moody's** kept **Egypt's rating unchanged** at B3 with a stable outlook, six levels below investment grade, stating that "very weak government finances" continue to constrain the rating.
- The **US** decided to **withhold from Egypt** USD 95.7mn in **aid** and to delay a further USD 195mn, citing the latter's new NGO law, and its failure to make progress on advancing human rights and democracy.
- Thanks to a 50% drop in the cost of offering IT services, **Egypt's information technology and communications industry exports** rose to USD 1.78bn at the end of the fiscal year 2016-2017.
- The **Basel AML Index 2017** ranks **Jordan** at 111 out of 146, with a score of 4.9 out of 10; Finland has the lowest

risk with a score of 3.04, while Iran is the riskiest (8.6). Jordan's is the lowest risk among other listed Arab countries: UAE scored 6.06 and ranked 72, Saudi Arabia scored 5.43 and ranked 93, while Kuwait recorded 5.53 and ranked 90, and Lebanon scored 7.07 and ranked 27. (More details on the index: <https://index.baselgovernance.org/>)

- **Kuwait's current account surplus narrowed** for the first time in three quarters in Q1, registering a KWD 0.3bn surplus. The goods surplus fell to KWD 1.9bn in Q1 (Q4 2016: KWD 2bn), retreating for the first time in a year, mainly due to a strong rebound in import growth.
- **Real estate market liquidity in Kuwait increased** by 7% mom and 26.8% yoy to KWD 190.2mn in Jul, disclosed the Ministry of Justice – Real Estate Registration and Authentications Department. According to the National Bank of Kuwait, total sales up by 12% yoy to KWD 161.5mn, as residential sales were up 43% from a year ago.
- The **demand for jobs in Kuwait's public sector** by unemployed citizens **hit an all-time record** of 7,316 as of Sunday last week, with female applicant accounting for 65.8% of the total, according to the *Al Jarida*
- **Moody's downgraded Lebanon's long-term issuer ratings** to B3 from B2 although it changed the outlook to stable from negative, citing "ongoing erosion of Lebanon's very weak government finances".
- **Lebanon's President signed the public sector pay rise and tax hike laws** last week. The latter hikes VAT by 1ppt to 11% and raises corporation tax to 17% from 15%. As for the public sector pay hike, it is estimated to cost USD 800mn-1.2bn (including certain pensions).
- **Lebanon's cabinet approved the electricity plan**, referring a proposal to the Tender Department to lease additional power barges to deal with the country's chronic power rationing.
- **Oman's nominal GDP jumped 9%** in Q1, on the back of

robust growth in oil prices and services sectors' activities. It is the first growth in nominal GDP in 2 years. Oil sector GDP soared more than 30%.

- **Foreign investors** gave an OMR 7bn **boost** in 2016 to the Oman economy, notwithstanding the low oil prices.
- **Qatar deposited** USD 6.9bn in the **local banking system** during Jul to offset outflows, following a USD 10.9bn injection the month before, as the crisis continues. As a result, total deposits grew to QAR 772.5bn from QAR 770.7bn a month before. Foreign deposits shrank to QAR 157.2 bn (Jun: QAR 170.6bn). Total domestic credit facilities extended by the banks rose to QAR 795.8bn last month (Jun: QAR 779.7bn).
- **Imports to Qatar recovered** by 6.3% mom to QAR 6.24bn in Jul (down 35% yoy) while natural gas exports seem unaffected: exports of petroleum gases and other gaseous hydrocarbons rose 7.8% yoy in Jul. Qatar's trade surplus expanded 78.1% yoy to QAR 11.9bn, although it edged down 4.8% mom.
- **Qatar** has introduced a **law to protect foreign domestic workers**, addressing some human rights groups concerns. The new rules limit the working age to between 18-60, mandate a maximum of 10 hours per working day with breaks for prayer, rest and eating, along with three weeks of severance pay at the end of their contracts, among others.
- **Saudi Arabia's foreign reserves fell** by USD 6.3bn to USD 487bn in Jul (-12.8% yoy), the lowest level since early 2011. SAMA's holdings of foreign securities shrank by USD 4.3bn to USD 333bn, while deposits with banks abroad grew by almost USD 1bn to USD 95bn.
- Outstanding **bank loans to the private sector** in **Saudi Arabia shrank** for the fifth straight month in Jul: falling by 1.3% after a reported 1.4% drop in Jun.
- **Saudi Arabia and China plan to establish** a USD 20bn **investment fund**, sharing both costs and profits on a 50:50 basis, disclosed the Saudi energy minister.

Separately, the Vice Minister of Economy and Planning revealed that Saudi may seek funding partly in Chinese yuan in a bid to “diversify the funding basis”.

- **Saudi Arabia granted investment licenses to four Chinese companies**, with a combined capital of more than SAR 190mn.
- **Saudi Arabia auctioned SAR 13bn (USD 3.5bn) of local currency Sukuk** last week, with the offer 295% subscribed. The amount of the issue was slightly lower than the first monthly offer in Jul, when it sold SAR 17bn.
- **Saudi Arabia** revealed that the 5% **VAT** will be applied on **private educational institutions**; tax will be applied to tuition fees as well as students’ transport costs. Separately, the General Authority of Zakat and Tax has launched a VAT Website (<https://vat.gov.sa/en/>) and helpline number.
- **Saudi Arabia** announced that **health and education sectors** will be open to **full foreign ownership**, without disclosing when this would come into effect. In the health sector, the ministry will “just be a regulator and not a service provider”, opening up USD 180bn of investment opportunities.
- **Saudi Arabia** plans to **transfer ownership of airports** to its main sovereign wealth fund, the **Public Investment Fund**, as part of the privatization drive. However, when or how the PIF would sell stakes in the airport companies was not revealed.
- A **national plan for SMEs** – including measures to support and finance SMEs projects – in **Saudi Arabia** will be finalised by end of this year, disclosed the governor of the Small and Medium Enterprises General Authority (Monshaat). He also added that women owned 38% of the SMEs established last year.
- All contractors working on **public sector projects** in **Saudi Arabia** that began before the **expatriate workers’ tax decision** was issued in Dec

2016 will be **exempt from expatriate workers' tax**, according to the Council of Ministers, as reported by *Al-Watan* Arabic daily.

- **Pension schemes** in most **MENA** countries are **in need of urgent reform**, according to a recent World Bank report. Pension promises being large and unaffordable, financially unsustainable schemes, fragmented schemes with costly administration and modest coverage rates are some of the problems identified with pension systems in the region (*The document can be downloaded at: <http://bit.ly/2w7tSBS>*)

UAE Focus

- The **UAE's Tax Authority** has launched a **new website** for businesses to understand excise taxes and VAT (<https://www.tax.gov.ae/index.aspx>). Legislation relating to VAT is expected to be published by end-Sep while business owners will be able to pre-register their companies for excise tax and VAT on the website from mid-Sep.
- In **UAE, VAT on schools and kindergartens** will be imposed at a zero percent rate i.e. this allows schools to reclaim VAT paid for business services and costs.
- **UAE's new excise law** states that excise tax rates shall be imposed on the "excise goods" provided that the tax rates do not exceed 200% of the Excise Price. The excise tax law consists of 30 articles, detailing the tax's general rules and procedures. The tax will be imposed on activities such as the production or importation of Excise Goods in to the UAE, as well as the stockpiling of Excise Goods in the UAE, where these activities occur in the course of doing business. The excise tax will not be imposed on the products that get exported, re-exported or those sold at airports for travelers to take outside the country. According to the law, the levy of excise tax will be on ad valorem basis. The selling

price will be the value set by the importer or producer of the relevant excise good (e.g. retail selling price), or set in accordance with standard prices which are agreed to by the tax authorities. (More: <https://www.mof.gov.ae/En/Media/News/Pages/2182017.aspx>)

- **Total bank credit** disbursed to the **realty sector in the UAE grew** by AED 16.5bn or 6.2% from end-2016 to AED 281.2bn as of end-Jun. This amounted to 19.3% of total credit channeled to all business platforms in the country. By quarter, AED 2.3bn was disbursed in Q1, and sharply increased to AED 14.2bn in Q2.
- According to the **UAE** central bank, a total of 17.815mn cheques worth AED 886.7bn were handled by the **Cheque Clearing** System during Jan-Jul 2017.
- **Non-oil bilateral trade** between the **UAE and the US increased** touching AED 111.1bn or USD 30.3bn as of end-2016 compared to USD 27.8bn in 2015, according to the Minister of Economy. He also noted that a total of 305 US companies were operational in the country until 2015 (excluding free-zone firms), in addition to 676 trade agencies and 38,290 brands.
- **Abu Dhabi's trade with 4 GCC nations** (Bahrain, Kuwait, Oman and Saudi Arabia) touched AED 11.33bn in Jan-May this year, accounting for 15.5% of the emirate's total trade. Trade with Saudi Arabia comprised 62% of trade with GCC, followed by Kuwait.
- **Emirati women investors** in the Abu Dhabi Securities Exchange (**ADX**) touched 219k in H1 this year, with the market value of their shares at AED 18.8bn.
- **Passenger traffic** at the **Dubai International Airport grew** by 5.9% yoy to 8.07mn in Jul – the busiest month on record, slightly higher than the previous record of 8.04mn passengers this Jan. Meanwhile, the number of flight movements – landings and take-offs – declined 4.7% to 34,181.
- **Abu Dhabi** invited companies to construct a **residential**

project for low-income families and bachelors: bidding companies will have to submit a tender bid of AED 500,000.

- **Dubai Duty Free** reported USD 930.3mn in sales in H1 this year, up 2.4% yoy. **Excise taxes** would have only a limited impact on sales, as it would impact goods that account for around 10% of revenues, according to the COO. Cigarettes alone account for 8-9% of sales.
- **UAE's aid to Yemen** reached AED 8.63bn (USD 2.35bn) during Apr 2015-Jul 2017, with AED 1.39bn provided this year.

Media Review

Another government shutdown saga looms

<https://www.ft.com/content/22735222-87c1-11e7-bf50-e1c239b45787>

Non-bank lending in the Middle East is taking off thanks to banks' woes

<https://www.reuters.com/article/us-mideast-debt-idUSKCN1B10FA>

Iraq shakes up Asian oil trading

<https://www.reuters.com/article/us-column-russell-crude-iraq-idUSKCN1B40FJ>

Qatar banks seek Asian, European funding as diplomatic crisis bites

<http://www.reuters.com/article/us-gulf-qatar-banks-idUSKCN1B40QZ>

Saudi government to invest in privatized sectors

https://www.zawya.com/mena/en/story/Saudi_government_to_invest_in_privatized_sectors-ZAWYA20170823053252/

UAE Minister of Economy's interview with The National

<https://www.thenational.ae/business/uae-working-on-laws-to-boost-non-oil-sector-contribution-to-80-by-2021-1.622658>

China conundrum

<https://www.wsj.com/articles/chinas-markets-cant-agree-on-how-good-its-economy-is-1503812558>

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