

Weekly Economic Commentary – Oct 15, 2017

Markets

Last week US stocks hit six consecutive closing high for the first time in more than 20 years. This week it was Japan's Nikkei to touch a two-decade closing high, boosted by stronger earnings and improved macro data. Emerging markets recorded another rally while regional markets were mixed with Qatar and the UAE rebounding while KSA and Egypt were on the back foot. The dollar was hit by the Fed's FOMC minutes reporting governor's fears that low inflation might not be "transitory", while sterling dropped in response to a reported deadlock in the Brexit negotiations. Oil prices were lifted by another drawdown in US crude inventories and stronger global growth prospects. Gold made some gains largely on dollar weakness.

Global Developments

US/Americas:

- **US inflation** in Sep **rose** 5% mom (2.2% yoy, the highest since Apr), vs 0.4% mom (1.9% yoy) in Aug, with gasoline prices surging 13.1% mom. Food prices rose 0.1% like in Aug and core CPI rose a mere 0.1% mom (1.7% yoy), vs 0.2% (1.7% yoy) in Aug.
- **US retail sales** in Sep recorded their **largest jump** since Mar 2015, 1.6% mom (4.4% yoy) vs -0.1% (3.2% yoy) in Aug, propelled by a 5.8% mom blow up in gasoline sales. Vehicle sales expanded 3.6% due to postponed sales and substitution after Hurricane Harvey.
- **Minutes of the US FED FOMC Sep meeting** revealed a **split** over the inflation outlook, specifically whether the recent soft patch is temporary or permanent. Hence while most members would likely vote for a rate hike again

this year, others cautioned the decision must depend on whether inflation picks up.

- **University of Michigan's US consumer sentiment soared** to 101.1 in Oct from 95.1 in Sep smashing market expectations of 95, probably as a result of Trump's tax reform. The current condition sub-index surged from 111.7 to 116.4 while long-term inflation expectation remained almost stable at 2.4%.
- **US initial jobless claims decreased** by 15,000 to 243,000 returning to levels seen before hurricanes Harvey and Irma. Continuing claims dropped by 32,000 to 1.89 mn, the lowest since late December 1973.

Europe:

- **ECB President Draghi** pointed out that negative interest-rate policies have not sapped bank profitability as ventilated by critics and he reiterated that the **QE would continue** until inflation is comfortably in line with the ECB mandate.
- **Eurozone's inflation** remained **subdued** at 1.5% yoy in Sep.
- **The Eurozone's industrial production climbed** 4% mom (3.8% yoy) in Aug after 0.3% in Jul, with strong performances across all sector but capital goods took off with a 3.1% mom growth.
- **German industrial production surged** 6% mom (5.4% yoy) in Aug vs a -0.1% drop in Jul. All sectors except construction recorded strong performances.
- **German inflation** was **unchanged** at 1.8% in Sep from Aug.
- **UK industrial production rose** by 0.2% mom (1.6% yoy) in Aug after a 0.3% (1.1% yoy) rise in Jul, driven by pharmaceuticals and basic metals.

Asia Pacific:

- **The Caixin China Composite PMI dropped** to 51.4 in Sep from 52.4 in Aug as manufacturing expanded at the

slowest pace in 3 months (PMI at 51.0 from 51.6 in Aug) and services were barely above the growth threshold (PMI at 50.6 from 52.7).

- **China's M2 money supply increased** 2% yoy in Aug from 8.9% in Jul, as a result of buoyant loan growth.
- **China's trade surplus shrunk** to USD 29.3bn in Sep from USD 42bn in Aug. Despite a jump in exports, the surplus was hit by an even stronger imports surge.
- **Japan's current account surplus increased** to JPY 2.38tn in Aug from JPY 1.97tn in Aug 2016. It was the largest current account surplus on record for the month of Aug.
- **Japan's core machinery orders jumped** 4% mom in Aug adding to the 8% boom in Jul. The spectacular broad-based rises in the summer indicates that the economy is gathering speed.
- **Japan's tertiary activity index fell** -0.2% mom (0.6% yoy) in Aug after 0.1% in Jul, confirming the weaker momentum of recent months.
- **India's inflation** rose 3.3% yoy in Sep, **unchanged** from Aug. Rising commodity and energy prices oil prices are driving inflation and food prices are also on the rise.
- **India's industrial production rose** 3% yoy in Aug vs 0.9% in Jul, the best performance since Nov, as manufacturing production rebounded sharply by 3.1% yoy after a -0.3% contraction in Jul.
- **Singapore's preliminary Q3 data** show that **GDP** rose 4.6% yoy, vs 2.9% in Q2 pulled by a 15.5% yoy growth in manufacturing almost double the 8.2% growth in Q2.
- **Malaysian industrial production expanded** 8% yoy in Aug vs 6.1% in Jul. The acceleration was due to mining, but manufacturing remained strong at 7.6% yoy slightly below 8% in Jul thanks to exports of electronics.

Bottom line: The new IMF forecasts published in the World Economic Outlook highlighted that the world economy is enjoying its most broad-based and fastest growth since the short-lived recovery in 2010. Most countries saw upward

revisions to their growth forecasts with low inflation rates. However, the research papers in the WEO warned that leverage in the financial system is at worrisome pre-2008 levels and that government debts are at historical highs. The combinations of these two elements underscore the vulnerability to an unforeseen shock.

Regional Developments

- The **IMF**, in its latest **World Economic Outlook** report, forecasts **growth** of 2.2% this year for the **MENA** region compared to 5.1% last year. While regional insecurity and geopolitical risks remain, next year's growth (3.2%) is likely to be driven by stronger domestic demand among oil-importers, and oil production rebound in the oil exporting nations. *(The report can be accessed at: <https://www.imf.org/en/Publications/WEO/Issues/2017/09/19/world-economic-outlook-october-2017>)*
- Work on **expanding and modernising Bahrain's airport** – a USD 1.1bn project – is “on track”, according to the chief executive of Bahrain Airport Company. Once completed, the terminal's capacity would have increased four times, with the ability to handle 14mn passengers annually.
- **Egypt's inflation** rate **eased** – for the second consecutive month – to 31.6% in Sep (Aug: 31.9%). Food prices rose by 41.2%, compared with 41.6% in Aug. Core inflation meanwhile fell to 33.26% (Aug: 34.86%).
- The **IMF** forecasts **Egypt's growth** at 4.5% this fiscal year, below the government's 5-5.25% growth estimates.
- **Remittances** from **Egyptians** abroad **increased** by 40% yoy in Aug, revealed the central bank. Remittances touched USD 16.3bn in Aug, rising 17.3% since Nov when the currency was devalued.
- **Egypt** announced an extension of the **state of emergency** for another three months (starting last Fri), as per the official gazette.

- **Kuwait** announced plans to complete **three major airport projects** over the next three years, at a total investment of KWD 1.45bn (USD 4.79bn).
- The annual **cost of bribery** in **Kuwait** is close to 2% of total GDP (~USD 2bn) annually, according to the IMF. The report also finds that the cost of corruption adds upto 25% to annual government contracts (~ USD 3.8bn).
- **Lebanon's** cabinet approved USD 46.5mn to cover the **expenses of next year's parliamentary elections**. This amount is to be used to pay the salaries of about 9,000 heads of polling stations in addition to the cost of logistical equipment.
- **Lebanon's** parliament has once again **approved the tax hikes** to fund the hike in public sector salaries, after the constitutional council annulled the tax law in Sep.
- **Oman's inflation** in Sep touched 1.6% yoy due to prices of transport, furnishings, household equipment and household maintenance.
- **Qatar** has been in discussions regarding an **international bond issuance** this year, revealed a finance ministry official. However, discussions with investors revealed that issuers would likely have to pay premiums to attract sufficient demand.
- **Qatar** government is offering **incentives for the private sector**: rents in Qatar's logistics zones have been reduced by 50% during 2018 and 2019; all ministries and government departments are to increase their procurement of local products to 100% from 30%; Qatar Development Bank will postpone receiving loan instalments for up to six months to facilitate industrial sector projects.
- **Saudi Aramco** is considering a **private placement of shares** and is in talks with the Chinese, as the proposed IPO is likely to be pushed beyond the 2018 target. (More in the Media review section).
- **Saudi Arabia's** Public Investment Fund announced the creation of a SAR 4bn (USD 1.07bn) **"fund of funds"** to support the **growth of SMEs**. The investments are expected

to create 2,600 jobs and contribute SAR 400mn to GDP by the end of 2020.

- **Saudi Arabia** plans to **supply electricity to Ethiopia** through its grid in Egypt sometime in the next three years, revealed the former country's minister of energy, industry and mineral resources. He also stated that Saudi Arabia plans to invest in **electrical power projects** worth SAR 250bn over the next 5 years, bringing on board a peak load of 80k megawatts by 2022.
- The **average monthly wages** for **Saudi employees increased** to SAR 9,911 in Q2 this year, from SAR 9,884 in the previous quarter, according to data from the General Authority for Statistics. Wages for Saudi citizens are almost 60% higher than the expats, with a gap of SAR 3716 in Q2. Unemployment rate meanwhile edged up to 12.8% in Q2 (Q1: 12.7%).
- The Saudi Ministry of Commerce and Investment disclosed that it had issued 87,575 **commercial registrations** for **women** at the end of Hijra year 1438 (ended 20 Sep 2017), with the highest numbers in Riyadh (20,086) and Jeddah (13,826).
- **Saudi Arabia** has **reduced crude oil allocations** for Nov by 560k barrels per day, disclosed an oil ministry spokesman. It was also revealed that oil exports in Sep was below 6.7mn bpd "despite high customer demand and the partial reduction of domestic summer crude burning requirements".
- The **GCC Summit** is most **likely to be postponed** this year, given the ongoing Qatar rift, according to the Arabic online newspaper The paper also stated that if the summit is to be held in Dec, it is likely to happen in Riyadh, and not Kuwait – as was earlier agreed upon.

UAE Focus

- The **IIF's** latest regional economic outlook report commends **UAE as the best-managed economy in the region**.

Noting that UAE was the first mover to reform energy subsidies, the IIF also highlights the country's "large financial buffers (estimated at around USD 670bn), safe-haven status, perfect infrastructure, sound banks, and diversified and business-friendly economy" as key positives driving growth.

- **Abu Dhabi's** successfully priced USD 10bn multi-tranche international **bond offering** was subscribed by a mix of international and regional investors: the 5-year bonds were **allocated across** 78% foreign investors (8% to Asian investors, 29% to European and UK investors, 41% to US investors) and 21% to investors from the Middle East.
- **Online registration for VAT** is now open in the **UAE**: businesses must register for VAT if their taxable supplies and imports exceed AED 375,000 per year. The Federal Tax Authority has urged businesses with an annual turnover of over AED 150mn and over AED 10mn to register before Oct 31 and Nov 30 respectively.
- The Dubai Multi Commodities Centre (**DMCC**) was named "**Global and Middle East Free Zone of the Year 2017**" by the Financial Times fDi Magazine, for the third consecutive year. There are over 13,700 companies registered in the free zone, with an annual average growth rate of 33% in the last ten years.
- More **real estate policy regulation** is in the offing, according to the **Dubai** Land Department: this includes building quality ratings and inspections, in addition to an update of the Dubai's official rental index (based on additional factors including building quality) and more affordable housing initiatives.
- **Sales of off-plan properties** at the Cityscape Global event this year totaled more than AED 870mn, according to the **Dubai** Land Department.
- At the **UAE- Saudi Business Forum**, Abu Dhabi introduced new incentives to attract Saudi investors: this includes exempting Saudi investors from certain Abu Dhabi Chamber fees, discounts of up to 15% of the value of rents of

warehouses, industrial zones, and offices at Khalifa Industrial Zone and so on.

- **Spending by UAE residents is expected to rise** by 1% yoy to AED 712.1bn this year, according to Euromonitor International. The biggest expenditure items are housing (AED 300.3bn), food and beverages (AED 103.1bn) and transport (AED 93.8bn).

Media Review

Saudi Aramco considers shelving international IPO

<https://www.ft.com/content/42b521c0-b028-11e7-beba-5521c713abf4>

The outcome of demonetization in India

<https://fee.org/articles/indias-demonetization-effort-has-demonstrably-failed>

<https://www.bloomberg.com/news/articles/2017-10-08/from-farms-to-factories-india-s-facing-a-risky-drop-in-demand>

PIMCO's view of the global economy

<http://www.businessinsider.com/pimco-markets-economy-cyclical-outlook-2018-forecasts-2017-10/#-1>

What happens now that Trump has decertified Iran?

<https://www.ft.com/content/73451b82-ac37-11e7-aab9-abaa44b1e130>

Oil prices on the rise

<http://www.artberman.com/higher-oil-prices-likely-early-2018/>

Central bankers face a crisis of confidence as models fail

<https://www.ft.com/content/333b3406-acd5-11e7-beba-5521c713abf4>

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