

Weekly Economic Commentary – Dec 17, 2017

Markets

Last week US stock indices scored another set of all time records in the wake of positive economic data, dovish Fed remarks after the FOMC meeting and lingering optimism on the tax reform. Wall Street pulled up emerging markets, however European and Asian indices lost ground dragged down by the bank sector. Regional markets were mostly mixed, but the Qatari bourse stood out raising almost 5% on the announcement of an expansionary state budget (see the Regional Development Section). Conversely, a similar fiscal impulse in Saudi Arabia failed to lift investors' mood and share prices. In currency markets, the dollar was mildly propped up by the Fed's rate hike, while the yen was under pressure due to the risk-off attitude prevailing in global markets. Oil prices hovered around the high levels prevailing since the Opec agreement on production cuts were announced, supported also by another large drawdown of US inventories. Gold prices, in the absence of geopolitical tensions, were almost unchanged near the lower bound of the trading range in place since Sep, despite a jump after the Fed press conference.

Global Developments

US/Americas:

- **In the US the Senate and House negotiators** have framed a tentative agreement on the final text of the tax bill, as Republican leaders are determined to get it signed by President Trump before year's end.
- As expected, the **US Fed hiked the fed funds rate target range** for the third time in 2017 by 25 bp to 1.25%-1.5%. The falling unemployment rate and an upbeat assessment

of the economic outlook support the case for additional raise despite moderate inflation (core PCE inflation forecasts for 2017 and 2018 were stable at 1.5% and 1.9%, respectively). In fact, the median “dot plot” still suggests 3 hikes in 2018 and the long-run equilibrium fed funds rate remains unchanged at 2.75%.

- **The US inflation** rate in Nov was 0.4% mom (2.2% yoy) vs 0.1% mom (2.0% yoy) in Oct, lifted mainly by energy prices. Core inflation rose just 0.1% mom (1.7% yoy) vs 0.2% mom (1.8% yoy) in Oct.
- **The IHS Markit US Composite PMI declined** to 53 in Dec from 54.5 in Nov. The service sector output performance eased to a 15-month low of 52.4 from 54.5 in Nov, while manufacturing production expanded at the fastest pace since Jan to 55 from 53.9 in Nov.
- **US retail sales jumped** by 0.8% mom (5.9% yoy) in Nov vs 0.5% (4.9% yoy) in Oct, with gasoline sales surging 2.8% mom. Growth was strong across the board, with only vehicle sales recording a monthly decline.
- **US industrial production rose** by 0.2% mom in Nov vs 0.9% in Oct thanks to good performances in manufacturing and mining, whereas utilities production faltered.
- **US business inventories fell** by -0.1% mom in Oct after no change in Sep. Manufacturers stockpiles were 0.2% mom higher, retailers held flat, and wholesalers shed -0.5%. Business sales advanced 0.6%.
- **US initial claims for unemployment benefits fell** 11,000 to 225,000. The 4-week moving average declined from 242,000 to 235,000. Continuing claims fell from 1.91 mn to 1.89 mn, near historical lows.
- The **Bank of Mexico raised** its overnight rate by 25 bps to 7.25%, the highest in 8 years, to counter the peso depreciation and climbing inflation, now at 6.63% yoy.

Europe:

- **The euro zone's inflation** was 1.4% yoy in Nov, down from

1.5% in Oct. Core inflation in Nov was 0.9% yoy, unchanged from Oct.

- **The ECB did not change its policy tools:** asset purchases will be cut in half to EUR 30bn in Jan and until Sep 2018, when this amount will be revised depending on the inflation rate. GDP growth estimates by the ECB staff upgraded growth in 2018 to 2.3% from 1.8% projected in Sep.
- **The eurozone composite flash PMI** hit a fresh 6.5-year record of 58.0 in Dec, up by 0.5 points from Nov. The improvement was driven by gains in the services and manufacturing, with the latter scoring an all-time high of 60.6. New orders showed the biggest uplift for a decade and job creation stayed at a 17 years top.
- **The eurozone's trade surplus** shrunk in Oct to EUR 18.9bn, from EUR 26.4bn in Sep, as exports grew more slowly than imports which were boosted by the pick up in economic activity.
- **The eurozone's industrial production** rose by 0.2% mom (3.7% yoy) in Oct, after falling -0.5% (3.4% yoy) mom in Sep. Output grew in France, Spain, and Italy, offsetting a -1.4% mom drop in Germany and an even deeper -1.8% mom tumble in Holland.
- EU leaders gave a nod to **advance Brexit talks** into the second phase focusing on a transition deal and future trading relationship. Meanwhile Brexit legislation proposed by May's government was rejected by the Commons, so in practice, any final Brexit deal must be ratified by the UK parliament.
- **Germany's inflation** accelerated to 1.8% yoy sa in Nov from 1.5% in Oct.
- **The German ZEW index of investor confidence** declined mildly in Dec to 17.4 from 18.7 in Nov due to lingering political uncertainties over the formation of a new government. However, the current conditions assessment touched a fresh 6-year high of 89.3, the third highest since the survey began in 1991.

- **The ZEW expectations measure for the eurozone** retreated to 29 in Dec from 30.9 in Nov.
- **The Bank of England, by unanimous consent, left rates unchanged** at 0.5%, but the Governor must send a letter to the government explaining why inflation exceeds the target range.
- **UK inflation** reached 3.1% yoy (0.3% mom) in Nov, from 3% yoy (0.1% mom) in Oct, the top in almost six years. Recreation goods led the jump but also food and fuel prices shot up. Core inflation was more subdued at 2.7%, unchanged from Oct..
- **UK retail sales** grew 1.6% yoy (1.1% mom) in Nov vs a flat reading in Oct (0.5% mom). Activity was likely boosted by one-off Black Friday discounts.
- **The Russian Central Bank lowered its key interest rate** 50 bp to 7.75% as inflationary pressure subside.

Asia Pacific:

- **China's M2 money supply** growth rebounded to 9.1% yoy in Nov from 8.8% in Oct thanks to sustained bank lending in the wake of mortgage demand, while corporate bond issuance was subdued.
- **China's industrial production** rose 6.1% yoy in Nov vs 6.2% in Oct. Manufacturing output remained healthy, sustained by tech demand and domestic auto demand.
- **China's fixed asset investments growth** slowed marginally to 7.2% yoy in Nov from 7.3% in Oct. Public investment is compensating for weak private investment with investment in manufacturing rather stable but below the levels in H2 2017. Electronics continues to be the leading sector while investments in bulk commodities stagnate.
- **Retail sales in China** rose 10.2% yoy in Nov up from a 10-month low of 10% in Oct. Communications equipment led the gains, with a 33.9% yoy surge. Online goods surged 28.5% yoy and online services sales skyrocketed +64.1%

yoy.

- **Japan's Tankan index of large manufacturers** rose for the fourth consecutive quarter to 25 in Q4 (a 13-year high), up from 22 in Q3, thanks to perky external demand especially for tech products.
- **Inflation in India increased** to 4.9% yoy in Nov, from 3.6% yoy in Oct smashing market expectations. It is the highest rate since Aug 2016, mainly due to a spike in vegetables and fuel prices.

Bottom line: Inflation rates are gradually picking up globally: the Moody's Analytics Global Consumer Price Index rose 0.4% mom (3.8% yoy) in Nov vs Oct's 0.3% led by developing economies' 0.5% rise, while in developed economies inflation was 0.2% mom. This means that monetary policy worldwide must be more aggressive than currently envisaged and asset prices will feel the pinch sooner or later. Furthermore, global growth is maintaining its momentum: the OECD composite leading indicator in Oct was stable at 100.1 for the fourth month in a row. The geographical breakdown underscores that activity in the eurozone is booming, especially in Germany and Italy, while the US is holding up at cruising speed. In emerging markets Brazil, Chile, Turkey and New Zealand are expected to be the best performers.

Regional Developments

- **Bahrain's** central bank has issued regulations recognising both offshore and locally-domiciled **exchange-traded funds**; furthermore, it will expand the categories of locally-domiciled mutual funds to include ETFs as another type of collective investment undertakings that may establish in Bahrain.
- The Central Bank of **Bahrain's FinTech** and Innovation Unit announced a partnership with the Bahrain FinTech Bay to support the development of the FinTech ecosystem in the country.
- **Egypt's** annual urban **consumer price inflation** eased to

26% in Nov (Oct: 30.8%). Core inflation fell to 25.53% from 30.53%. The finance minister expects inflation to ease to 20% in Jan and to 13-14% by Aug.

- The **current account deficit** in **Egypt** narrowed to USD 1.6bn in Q1 of the 2017-18 financial year from a deficit of USD 4.8bn in the same period a year earlier. Overall balance of payments meanwhile posted a USD 5.1bn surplus compared to USD 1.9bn a year ago.
- **Foreign investment** in **Egyptian securities** touched USD 19bn as of Dec 6 since the devaluation of the pound.
- The **Egyptian Electricity** Holding Company (EEHC) is in the process of setting up three electricity companies – with a total capacity of 14,400 MW, and worth EUR 6bn. The EEHC's share in each company is about 51%. The investments of the three electricity companies to be offered on the EGX amounted to EGP 120bn.
- **Egypt's internet subscribers** increased by 4% yoy to 41.9mn in Nov: .
- **Jordan** and the **World Bank** signed a **financing agreement** with a value of USD 200mn to fund a reform programme related to the education sector. The repayment period of the loan extends over thirty-five years, and the first installment of the programme (USD 77mn) will be transferred to the Treasury before the end of this month.
- The European Bank for Reconstruction and Development (EBRD) is extending a USD 22mn **loan towards new solar power plant** in
- **Kuwait's** central bank left the **discount rate unchanged** at 2.75% in spite of the Fed's hike, partly based on the ability of local banks to absorb any effort to raise interest rates on their dinar deposits.
- **Inflation** in **Kuwait** increased to a multi-month high of 1.4% in Oct, while core inflation rose to 3.3% yoy (Sep: 2.5%).
- **Current account surplus** in **Kuwait** improved to KWD 0.62mn in Q2 (Q1: KWD 0.44mn) on lower remittances, a decline

in imports, and gain in investment income.

- The **IIF** estimates **Lebanon's growth** to reach 3.1% next year, "driven by some recovery in investment and exports", from a projected 2.2% this year.
- **Lebanon** approves **offshore oil and gas exploration** bids, with exploratory drilling expected to start at the beginning of 2019.
- The number of **tourists** coming to **Lebanon** is expected to reach 1.9 million at end-2017, compared to 1.68mn last year, according to the Hotel Owners Association.
- **Fitch** downgraded **Oman** to BBB- from BBB, with a negative outlook, due to dissatisfaction with the current fiscal outlook.
- **Oman's** government has announced plans to introduce in Jan a **new fuel subsidy scheme** for low-income citizens who will receive 200 litres per month of M91 petrol at a capped price of 180 baisa per litre.
- The Central Bank of **Oman** reported an increase of 3.22% yoy in **individuals' bank deposits** at the end of Sep to OMR 12.41bn.
- According to the Ministry of Commerce and Industry **Oman's trade balance** in 2016 recorded a surplus of OMR 2bn.
- **Qatar's 2018 state budget** sees a 2.4% increase in spending to QAR 203.2bn (USD 56bn), and with revenue rising by 2.9% to QAR 175.1bn. This would bring the deficit down by 1.1% to QAR 28.1bn. The budget (based on oil at USD 45 per barrel) deficit will be financed through debt sales.
- **Saudi Arabia** approved SAR 72bn (USD 19.2bn) worth of **stimulus measures to boost private sector growth**: proposals include residential housing loans worth SAR 21.3bn, a SAR 10bn fund to support economic projects, SAR 1.5bn to support distressed companies, and a SAR 2.8bn government fund to invest in smaller companies. This forms part of a broader private sector reform plan, projected to cost SAR 200bn, spanning four years: of

this, SAR 72bn will be spent over the next four years, including SAR 24bn in 2018.

- **Saudi Aramco** is seeking **proposals** from bankers before year-end for roles of **bookrunners** and global coordinators for its planned 2018 IPO. Separately, the company announced plans to raise its spending to USD 414bn over the next 10 years – including USD 134bn to spend on drilling and well services and USD 78bn to maintain oil output potential.
- **Saudi Arabia** plans to establish an **export bank** with capital of SAR 30bn (USD 8bn) to support exports from its industrial and mining projects; about SAR 5bn have been allocated as a first installment this year, according to the country's energy, industry and mineral resources minister.
- **Saudi Arabia** will revise upwards the prices of gasoline, diesel, as well as electricity tariffs, effective from Q1 next year. New electricity tariffs for households and commercial establishments would be applied from Jan. 1, with tariffs for all but the largest residential users to more than triple, albeit from a very low base. A cash handout system is planned for low- and middle-income citizens to offset the impact of the changes.
- **Saudi Arabia** will announce the **state budget for 2018** after markets close on Dec 19, revealed the Information Ministry.
- **Saudi Arabia's** central bank has directed banks to not misuse the funds deposited in the **Citizen's Accounts Program**. About 3.7mn households have signed up to the programme, representing some 13mn total beneficiaries.
- **Saudi Arabia and China** have launched a "Digital Silk Road" initiative. As part of the MoU intended to promote and develop the "Digital Silk Road", it will also review the Chinese experience in building smart cities.
- **Saudi Arabia** will maintain its **crude oil shipments** in Jan at 6.9 million barrels per day (bpd), though oil shipments to Asia will be reduced by more than 100k bpd.

- **Saudi Arabia lifted a 35-year-old ban on cinemas**, thereby opening up the cultural and entertainment sector for greater private sector participation and employment opportunities.
- Energy ministers from both **UAE and Kuwait** have stated that the OPEC could consider a strategy to end **output cuts** by Jun, if the market is re-balanced by then.
- According to the report “Global Sovereign Outlook 2018: Brighter With Risk of Turbulence”, published by S&P, Oman ranked ninth, Qatar 20th, Bahrain 28th, Kuwait 51st and Saudi Arabia ranked 77th out of 80 sovereigns. UAE was not part of the S&P list.

UAE Focus

- The **IMF** stated that **non-oil sector growth in the UAE** is projected to rise from 1.9% this year to 2.8% next year and 3.3-3.5% in 2020. Consolidated fiscal deficit is to shrink to 1.3% of GDP next year and gradually disappear in subsequent years, from 2.2% this year.
- The **UAE** is working with Saudi Arabia’s central bank to issue a digital currency based on blockchain that would be accepted in cross-border transactions between the new nations – to be used among banks, not by individual consumers – according to the former’s central bank governor.
- **UAE** officials clarified that **VAT will be implemented for the banking and insurance sector** beginning next year: for the banking sector, services with margins or interests will be exempt, while other services will be subject to VAT.
- **UAE non-oil sector** is likely to grow at 3% this year versus the 2.7% a year ago, according to the central bank. However the bank estimates overall GDP growth to decline to 1.6% from 3.0% last year.
- **Gross credit in the UAE** grew by 2.3% to AED 1.58trn in Q3; lending to the private sector was up 2.4% to AED

1.07trn. Bank deposits increased by 5.8% to AED 1.595trn by Q3.

- The **Dubai Economy Tracker** eased to 55.3 in Nov from 55.6 in Oct, with the retail sector the strongest category; job creation gained for the ninth consecutive month.
- **Dubai's 2018 budget**, which disclosed a 19.5% increase in state spending to AED 56.6bn, focuses heavily on the infrastructure development related to Expo 2020. State salaries and wages are projected to increase 10% next year, accounting for 30% of total spending. A budget deficit of AED 6.2bn (1.56% of GDP) is estimated next year in 2018, versus a deficit of AED 2.5bn this year.
- **Real GDP growth in Dubai** is expected to reach 3.2% this year, 3.5% in 2018 and 3.7% in 2019, according to the Dubai DED. Dubai's total trade (direct and free zones) grew by 3.5% to AED 985bn during the first nine months this year.
- **Dubai Roads and Transport Authority** plans to complete **key infrastructure projects** worth AED 3.2bn (USD 871mn) next year including the upgrade of the roads network around Dubai Expo site and Route 2020 Project.
- **Digital transformation** in the **UAE** will generate AED 33.8bn (USD 9.2bn) over the next three years, according to the DG of the Smart Dubai office. Open data is estimated to add AED 10.4bn to Dubai's GDP by 2021, while blockchain technology in public services will add AED 5.5bn by 2020, stated the DG.
- **Bilateral trade between China and UAE** surpassed USD 35bn in Jan-Sep 2017, and is expected to cross 2016's USD 46.3bn mark this year.
- **Remittances from the UAE** grew by 2.1% to AED 121.1bn during Jan-Sep 2017, according to the central bank. In Q3 alone, AED 43.3bn was transferred from the UAE (up 14.1% yoy), with Indians transferring around 35.7% of the total Q3 remittances.
- The **UAE pharmaceutical sector** is estimated to grow to AED 14.11bn in 2020, supported by increased healthcare

expenditure, mandatory health insurance, and growing medical tourism.

Media Review

The Role of sovereign wealth in the Gulf

<https://www.bloomberg.com/news/videos/2017-12-11/the-role-of-sovereign-wealth-in-the-gulf-video>

Financial Investors wish list for 2018

<https://www.project-syndicate.org/commentary/global-financial-performance-2018-by-mohamed-a-el-erian-2017-12>

Inclusive entrepreneurship policies

http://www.oecd-ilibrary.org/employment/the-missing-entrepreneurs-2017/executive-summary_9789264283602-4-en

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