

# Weekly Economic Commentary – Feb 4, 2018

## Markets

Global equities fell sharply last week with the S&P 500 and Dow Jones suffering their worst week since Jan 2016 amid a sharp selloff in developed market government bonds; 10-year US Treasury yields rose to 2.8% for the first time in 4 years. The sell-off, preceded by weeks of turmoil in the fixed income markets, as inflation fear mounted, was triggered by the FOMC minutes which seemed to signal a rate hike in Mar. On Friday the rout intensified recording the biggest daily loss of the Trump presidency after the payroll report confirmed a robust rise in wages. Major bourses in developed and emerging markets felt the contagion, although the Topix contained the losses and several regional markets, including Oman had positive performances. After the presentation of the budget the Indian Sensex lost 840 points on Friday as investors worried that the ambitious social goals will turn out to be mostly pre-elections handouts. In currency markets the dollar slipped again on major crosses, although the dollar index recovered from a 3-year trough. After weeks of steady gains oil prices lost ground, especially after data on US oil inventories showed an unexpected increase by 6.8 m/b and the EIA estimated that US output was just under 10.04mn barrels per day in Nov, a whisker below the all-time record set in Nov 1970. Counterintuitively, given the higher inflation expectations, even the price of gold fell amid the global market turmoil.

## Global Developments

### **US/Americas:**

- **US non-farm payrolls rose** by 200k in Jan vs 160k in Dec marking the 88th consecutive month of job creation, the

longest streak on record. The unemployment rate remained for the fourth month in a row, at 4.1%, its lowest level since Dec 2000, although the under-employment rate increased to 8.2%. Labor force participation was 62.7% and wages rose 0.3% mom (2.9% yoy), provoking an inflation scare.

- **Initial claims for unemployment insurance benefits in the US** fell 1,000 to 230k. The 4-week moving average fell 5,000 to 234,500. Continuing claims rose 13,000 to 1.953 mn.
- The **minutes of the US Fed FOMC Dec meeting** were hardly exciting. The target range for the fed funds rate remains at 1.25% – 1.5%. The changes to the wording of the statement were not substantial. A hawkish tinge posited that inflation will increase this year and stabilise around the 2% yoy medium term target. Markets interpreted this a sign that in Mar the rates will be hiked again.
- The **ISM manufacturing index** in Jan **retrenched** slightly to 59.1 from 59.3 in Dec. The big surprise was the rise of the inventory index by 3.8 points to 52.3, which should boost GDP growth.
- **US core PCE** in Dec **rose** by 0.2% mom and 1.5% yoy, slightly above the bottom of 1.3% yoy in August.
- **US nominal personal income growth accelerated** to 0.4% mom in Dec from 0.3% in Nov. Real disposable income rose 0.2% mom. Wages and salaries rose 0.5% from 0.4% in Nov.
- The **Case Shiller US national house price index** **increased** by 6.2% yoy in Nov vs 6.1% in Oct.
- The **US pending home sales index** **rose** by 0.5% mom sa (0.5% yoy) to 110.1 in Dec, the third consecutive monthly uptick, propelling the index to its highest level since Mar.
- The **Conference Board consumer confidence index** **advanced** 3 pts to 125.4, in Dec driven entirely by consumer expectations about the labor market (at record high since 2001). However, the present situation index

declined 1.2 pts.

- The **US Employment Cost Index** in Q4 showed that private wage growth accelerated to 2.8% yoy from 2.6% in Q3, the fastest pace since the end of the recession.
- **US non-farm productivity fell** by 0.1% qoq ann in Q4 after a 2.7% gain in Q3. For the whole 2017 productivity rose 1.2%, better than in 2016, but hardly enough to lift potential growth.
- **US factory orders rose** by 1.7% mom in Dec vs 1.3% in Nov, the fifth monthly gain, thanks to a large nondefense aircraft and defense orders, while core capital goods orders shed 0.6% mom.

## Europe:

- The **Eurozone GDP in Q4 expanded** by 0.6% qoq (2.7% yoy), almost on par with 0.7% (2.8% yoy) in Q3. The average yearly growth in 2017 was 2.5%, the highest since 2007, vs 1.8% in 2016.
- **Eurozone inflation decelerated** to 1.3% yoy in Jan from 1.4% in Dec. Core inflation was constant at 1% yoy in Jan, only 0.1% higher than 12 months earlier.
- The **Eurozone's economic confidence indicator** lost 0.6 point in Jan retreating from a 17-year high in Dec.
- **German retail sales plunged** by -1.9% mom (0.7% yoy) in Dec, reversing the same gain in Nov.

## Asia Pacific:

- The **Indian 2018-19 profligate government budget** comprises the re-introduction of standard deductions, wider medical expenses exemptions for the elderly, a revamp of the healthcare system to benefit the poor, higher minimum crop prices for farmers, a long-term capital gains tax and more spending on infrastructure projects. Fiscal discipline is de facto dead.
- **China's Caixin-Markit PMI** in Jan was **unchanged** from Dec at 51.5. The output growth sub-index was at the top

since Dec 2016, but the employment component declined again. Total new orders notched a nineteenth consecutive month of growth but at a slower pace.

- **China's official PMI** (which is skewed towards large state owned companies) came in at 51.3 in Jan marginally below the 51.6 in Dec due in part to dwindling new orders.
- **Industrial production in Japan soared** 2.7% mom in Dec vs 0.5% in Nov, pulled by transport equipment and general purpose machinery.
- The **Nikkei-Markit Japan PMI rose** to 54.8 in Jan from 54.0 in Dec. New order growth advanced for a third month in a row to a 4-year top, with new business from overseas reporting the fastest rate of growth since May 2010.
- **Japanese household consumption rose** 0.8% yoy in Dec, down from 2.4% in Nov.
- **Japan's retail sales** in Dec expanded 3.6% yoy from 2.1% in Nov thanks to a broad-based pickup, especially in motor vehicles and fuel.
- **Japan's consumer confidence was unchanged** in Jan at 44.7 with sluggish performances in all major categories, except employment.
- **Taiwan's GDP** in Q4 grew 3.3% yoy, up from 3.1% in Q3.
- **South Korean Industrial production** in Dec fell -6% yoy accelerating the -1.7% drop in Nov.
- **South Korean inflation** crawled up only 1% yoy in Jan, down from 1.5% in Dec, well below the Bank of Korea's 2% target.
- **South Korean exports surged** 22.2% yoy to USD 49.2bn in Jan compared to 8.9% in Dec. Imports rose 20.9% yoy in Jan to USD 45.49bn. The trade balance shrunk to USD 3.5bn against USD 5.54bn in Dec.

**Bottom line:** Despite all the hype on Trumponomics the Eurozone annual growth for 2017 at 2.5% was higher than the 2.3% growth in the US and 1.8% in the UK. Last week the plunge in global

stock prices came as a reminder that the combination of massive debt levels with the “duration” risk due to ultra-low yields and a shift toward longer maturities is a dangerous mix. Equity valuations have been pushed up to historically high levels by massive injections of liquidity which cannot last forever. And in fact the data on US wage inflation made clear that the Fed will soon be forced to act more aggressively than previously forecast. Moreover, as inflation rises the bond prices will inevitably drop causing heavy losses. According to data from the Institute of International Finance, global debt levels have hit a record 327% of GDP, up 51% since the 2008 collapse of Lehman Brothers. A 1% rise in rates would cause losses for USD 1.2 tn in the Barclays US Aggregate Bond Index and even larger losses in “junk” bonds, fixed-rate mortgages, and interest rate and bond derivatives.

### Regional Developments

- **Money supply in Egypt** grew by 20.919% yoy to EGP 3.2trn, according to the central bank.
- **Egypt** is targeting **economic growth** of 5.8% this financial year 2018-19, revealed the planning minister, a tad lower than the 6% projection mentioned last month.
- **Budget deficit in Egypt** is expected to touch 9.4% of GDP in the 2017-18 fiscal year, according to the deputy finance minister, and up from earlier projections of 9%, largely due to an increase in global oil prices and high local interest rates.
- **Egypt's foreign reserves increased** to USD 37.02bn in Dec, from USD 36.723bn at end-Nov.
- **Egypt** passed the country's first **bankruptcy law** aimed at encouraging investments: the law abolishes imprisonment in cases of bankruptcy, and also simplifies post-bankruptcy procedures. Moody's reported that this move would be “credit positive for banks”.
- **Foreign investment in Egypt's domestic debt** reached USD 19.8bn in the week ending Jan 26, reported *Al Shorouk*

newspaper, quoting the deputy finance minister.

- **Egypt's** Ministry of Finance disclosed the **repayment** of USD 1.36bn worth of **international bonds** that were due at end-Dec 2017.
- **Egypt** agreed to a USD 3bn **financial deal with the International Islamic Trade Finance Corporation** to purchase essential items such as food and petroleum, revealed the investment ministry.
- **Crude oil exports** by **Iraq's** state-oil marketer SOMO recorded an average rate of 3.5mn barrels per day in Jan; the average could top Dec's 3.535mn bpd record.
- **Kuwait** released its **budget** for the financial year **2018-19**: spending is expected to rise to KWD 20bn (USD 66.7bn) while deficit is projected at KWD 5bn before transfers to the Future Generations Fund (and KWD 6.5bn after transfer of 10% of total revenue to the FGF). The budget is based on an average oil price of USD 50 per barrel. The budget had no mention of either VAT or excise taxes.
- **Inflation** in **Kuwait** is set to touch a multi-year low of 1.75%, thanks to a decline in housing rents and food prices, and despite higher energy and water prices, revealed the IMF.
- **Standard & Poor's** affirmed its AA/A-1+ **ratings** for **Kuwait**, with a "stable" outlook, citing strong public and external balance sheets backed by a significant stock of financial assets.
- **Kuwait Petroleum Corp** plans to carry out a number of major projects to boost **oil production** to 4.75mn barrels per day by 2040. To achieve this objective, the company plans to spend USD 114bn in capital expenditure over the next five years and an additional USD 394bn beyond that to 2040.
- **Lebanon** is expected to set **new ceilings on bank housing loans**, reported *The Daily Star* citing sources. The expectation is that interest rates on bank housing loans may be hiked by 50bps.

- **Morocco** will not seek to renew its USD 3.47bn **liquidity line** with the **IMF** when it expires in Jul, stated the country's finance minister. The country had previously renewed the facility twice without drawing on it.
- A **six-month ban has been imposed on hiring of expatriate professionals** in 10 sectors in **Oman**, including information technology, finance, human resources and administration, marketing, insurance, media, medical field, aviation sector, engineering and technical fields.
- **Qatar's** central bank resumed its **auctions** and sold QAR 1.15bn (USD 316mn) of Treasury bills; no sale was announced in early Jan.
- **Saudi Arabia's** Aramco and Google's parent company Alphabet Inc. are in early talks to create a **new technology hub** in the country. As part of the plan, data centres would be built around Saudi Arabia – though whose data the centers would house or who would control them is not clear.
- **Saudi Arabia** seized over SAR 400bn (USD 106bn) in **financial settlements** from the **corruption purge**, according to the attorney general. Around 56 people are still in custody, down from 95 the week before.
- **Foreign reserves** in **Saudi Arabia** **rose** for the third consecutive month (for the first time since mid-2014) in Dec, growing by USD 2bn to USD 488.9bn in Dec.
- **Saudi banks** have provided SAR 1.4trn (USD 381bn) in **funding to the private sector**, according to the secretary general of the media and banking awareness committee. He was speaking about the challenges and solutions that startup businesses face in the banking sector.
- **Expat remittances** dropped by 6.74% yoy to SAR 141.6bn last year, according to the **Saudi Arabian** Monetary Authority; the highest remittances in 2017 were recorded in Dec when it was SAR14.04bn. Total remittances by expatriates reached more than SAR 752bn in five years,

reported *Al Hayat* newspaper, citing SAMA statistics.

- **Saudi Arabia's** Ministry of Labour and Social Development added 12 new job categories and activities – sales jobs in electronics retail stores, car dealerships, furniture stores and clothing stores among others – that would be off-limits to expatriates beginning later this year.
- **Saudi Arabia** plans to attract USD 11bn into large-scale **water projects**, primarily in water desalination. The largest desalinated water investment – an Independent Water and Power Project – will have a water production capacity of 1,170,000 cubic meters per day and power capacity of 3k Megawatts.
- The **IMF's** managing director, at a regional conference, **called on the Arab nations to "take urgent action"**, create more jobs and empower SMEs while trying to solve the issues of limited access to finance and weak legal frameworks. (The complete speech is available at: <http://www.imf.org/en/News/Articles/2018/01/29/sp013018-md-morocco-opening-remarks>)
- **Productivity** has been declining for many years across the **Middle East**, according to PwC's latest economic bulletin. UAE exceeded the global average of 10% growth in real productivity between 2010 and 2017, while Oman and Lebanon continued to decline.
- Sweden is the most straightforward country in which to **recover debt** (scoring 30 out of a 0-100 scale), compared to a global average of 50, while the **Middle East** region ranks as the **most complicated**, according to Euler Hermes 2018 Collection Complexity Score and Rating report. The UAE and Saudi Arabia, the only two Middle Eastern economies included in the study, scored 81 and 94 respectively.
- Around USD 560mn of **investments** were made in 260 **MENA startups** last year, as revealed by Magnitt's annual State of MENA Funding. UAE was the dominant market, accounting for 70% of all investment amounts and 37% of transaction (excluding Careem's investment of USD



150mn).

- The total value of **GCC healthcare projects** exceeded AED 223.5bn (USD 61bn) in Jan from around 707 projects; of these, 445 projects worth USD 51.9bn are hospital projects

## **UAE Focus**

- **UAE non-oil trade grew** by 1% yoy to AED 1.7trn (USD 318bn) in Jan-Sep 2017. Direct non-oil foreign trade accounted for 68% of total trade volume, while free zones share was AED 317.5bn (32%). Exports stood at AED 139.1bn during this period while re-exports touched AED 325bn.
- About AED 93bn of **loans** were given to **SMEs** in the **UAE** (almost 41k loans), revealed the central bank governor at the Federal National Council. This amounted to 6% of total credit disbursed in the country.
- **UAE passed a draft law regulating lease financing:** companies who practice lease financing without a license from the Central bank will face a fine of between AED 200,000-10mn, and/or a jail sentence.
- **UAE's crude oil production** fell to 2.85mn barrels per day (bpd) in Jan, from 2.862 bpd pumped in Dec. Under the OPEC deal, UAE output target is 2.874mn bpd.
- **UAE fuel prices reached an all-time high** in Feb, since the deregulation of prices since Aug 2015. Petrol prices – which are now inclusive of VAT- increased by 5-6% in Feb, while diesel prices were up 6.9%.
- **Ras Al Khaimah's** Chamber of Commerce disclosed a 6% yoy increase in registration of new **firms** to a total 33,652 last year. Around 19,680 licenses were renewed while around 1821 new firms were registered (247 in the free trade zone).
- **Permits** to drivers of **passenger transportation vehicles** increased by 45% to 12,390 in 2017, according to the Roads and Transport Authority. Such permits include

school transport and female attendant permits, taxi and limo permits, and heavy bus permits.

### **Media Review**

**The euro break fears are at record low**

<https://www.bloomberg.com/news/articles/2018-01-31/euro-breakup-fears-slide-to-record-low>

**Exxon forecasts oil demand in 2040**

<http://businessweekme.com/2018/02/03/exxon-sees-oil-demand-20-2040-maybe-itll/>

**Post-Davos Depression**

<https://www.project-syndicate.org/commentary/davos-ceos-tax-cuts-trump-by-joseph-e-stiglitz-2018-02>

**Democracy continues its disturbing retreat**

<https://www.economist.com/blogs/graphicdetail/2018/01/daily-chart-21>

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