

Weekly Economic Commentary – Apr 1, 2018

Markets

After experiencing the worst week in two years, in the last week of the quarter, US equity markets enjoyed a respite. The S&P500 was almost unchanged, while the Dow Jones had a strong performance. News about M&A activity (Renault in talks to merge with Nissan) led to some upward movements in Europe's equity markets. However, Q1 saw stocks in the US posting the first quarterly loss since 2015 while STOXX 600 posted its worst quarter in the past 2 years. In the region, Qatar stocks took another hit, while the FTSE's decision to include Kuwait and Saudi Arabia among the emerging markets, had ephemeral effect due to profit-taking towards the end of the week. The dollar index fell to a 16-month low earlier in the week after trade war talks unsettled markets, and ended the quarter down 5.7%. Despite the unexpected increase in US oil inventories by 1.643 mn barrels (marking the 3rd increase in the past 10 weeks), Brent prices ended close to USD 70 on rising geopolitical uncertainty. Gold prices lost some ground after days of directionless trade, but continue to hover above USD 1300 per ounce.

Global Developments

US/Americas:

- **The final reading showed that US real GDP growth in Q4 was 2.9% qoq ann, slightly below the 3.2% in Q3 but above the 2.6% initially reported. Consumer spending was the main driver of growth while investment and government spending also improved. Inventory and foreign trade dragged growth down.**
- **US headline and core PCE deflators in Feb both increased**

0.2% mom. The core PCE, which is the main gauge of inflation monitored by the Fed rose 1.6% yoy. Goods prices actually declined slightly the services deflator rose 0.3% mom.

- **US real disposable income growth was disappointing** at 1.1% yoy in Q4 after rising 0.7% in Q3. The saving rate fell to 2.6%, the lowest since 2005. Corporate profits fell 0.1% qoq (not ann.) after rising 4.3% in Q3.
- **US nominal personal income growth was flat** at 0.4% mom in Feb, despite the tax cuts with wages and salaries advancing 0.5% mom vs 0.6% in Jan.
- **US real spending was unchanged mom** in Feb after a -0.2% decline in Jan. The breakdown shows that nondurable goods spending fell, durable goods gained somewhat and service spending was almost flat.
- **US consumer confidence declined** 2.3 points in Mar to 127.7, reversing some of the increase in Feb. Both the present situation index and the expectations index fell, though workers are still quite optimistic over the labor market. Purchasing plans plunged, with autos falling to a 6-month low and home purchasing plans falling to a record low in more than a year.
- **Wholesaler inventories in the US surged** 1.1% mom in Feb surpassing the 1% increase in Jan. Retail inventories gained 0.4% rise vs 0.7% gain in Jan thanks primarily to auto and parts dealers.
- **The US Case-Shiller national house price index retreated** marginally to 6.2% in Jan from 6.3% in Dec.
- **The US goods trade deficit** in Feb was USD 75.4bn adding to the large deficit of USD 89bn in Jan. Barring a sharp decline in Mar, the Q1 deficit could be the largest since 2008, putting a heavy brake on GDP growth. Nominal goods exports rose 2.2% mom and imports gained 1.4%.
- **The US pending home sales index increased** 3.1% mom sa (-4.1% yoy) to 107.5 in Feb, reversing in part Jan's dip.
- **The US initial claims for unemployment benefits fell**

12,000 to 215,000 the record low since Jan 1973. The 4-week moving average slid 500 to 224,500, however continuing claims rose 35,000 to 1.871 mn, still a very low historical level.

Europe:

- **The Eurozone's economic confidence indicator fell** to 112.6 in Mar from 114.2 in Feb, still quite high, although it is the third consecutive drop interrupting the upward trend initiated in early 2016. Industry, services and retail confidence declined, while consumer confidence was buoyant. Construction was the only sector to advance.
- **German inflation picked up** to 1.6% yoy in Mar from a 15-month low of 1.4% in Feb.
- **The UK current account deficit shrunk** to GBP 18.4bn in Q4 2017 from GBP 19.2bn in Q3 It is the smallest deficit since Q3 2012.
- **UK consumer confidence rebounded** to -7 in Mar from -10 in Feb. All five subcomponents increased mom especially households' prospects about their personal finances.

Asia Pacific:

- **China's official PMI increased** to 51.5 in Mar compared to Feb's reading of 50.3, supported by improved seasonal demand: output (53.1 vs. Feb's 50.3), total new orders (53.3 versus 51.0) and export orders (51.3 from 49.0) all climbed up. Meanwhile, composite PMI increased to 54.0 in Mar, from Feb's 52.9.
- **The official non-manufacturing PMI in China recovered** to 54.6 in Mar from a 4-month low of 54.4 in Feb. In particular, new export orders returned to growth (50.4 from 45.9 in Feb) and new orders continued to expand but just marginally (50.1 from 50.5 in Feb). Confidence remained almost stable and quite strong at 61.1 from 61.2 in Feb. Contraction in employment deepened to 49.2

- from 49.6 in Feb.
- Official export data revealed that **China virtually halted exports** of fuel, coal and key commodities to **North Korea** in the past few months before summoning Kim Jong Un to Beijing.
 - **Japan's industrial production rebounded** partially in Feb by 4.1% mom (1.4% yoy) mom from a -6.8% mom (2.5% yoy) plunge in Jan. Output rose in most sectors, especially business machinery and electronics.
 - **Japan's retail sales rose** 0.4% mom (1.6% yoy) in Feb. There was a slowdown in some big-ticket items, while fuel costs increased, due to higher energy commodities prices.
 - **Business confidence in South Korea** in Mar **declined** just one point to 74 compared to Feb, but in the past 6 months the index has gradually lost almost 10 points.

Bottom line: The outlook for equities and other assets' valuation in the medium term will hinge on a combination of macroeconomic factors, not on a single element or event. The dynamics are rapidly changing, especially in the US and are bound to spark repercussions around the globe: the fed funds rate is up by 150bp from its low and the 10-year T-bill rate is up 140bp; equities since late January are wobbling and volatility measured by the VIX surged from 9 to 25 in a few months. A particularly disturbing risk scenario is emerging from the macro data in Q1: slower global growth, higher interest rates and higher inflation will abruptly disrupt the goldilocks and the narrative that justifies historically high valuations. The Fed has been behind the curve for more than a year and its latest economic projections are not coherent: above-trend growth, falling unemployment (to levels not seen in nearly 60 years), inflation miraculously stabilized around the 2% target, despite a massive public spending plan and lower taxes implying massive budget deficits. Such disconnect with historical experience should induce offloading risky assets before the stampede starts.

Regional Developments

- **Bahrain** sold USD 1bn of 7-1/2-year **Sukuk** last week, but scrapped plans for an issue of conventional bonds after investors' demanded a premium to buy it given concerns about rising public debt levels. Orders for the Sukuk peaked at about USD 2.1bn from over 100 investors, and 59% of the Sukuk was distributed in the MENA region itself.
- **Bahrain's** Shura Council approved a **pension benefits law for private sector employees**: this will allow private sector employees to purchase assumed years of service so that they can enjoy relevant pension benefits in line with public and military sectors.
- A **public tender** has been **issued in Bahrain** for a 100MW **solar power plant**, planned to be functional by Dec 2019.
- **Egypt's President Sisi won the elections** with more than 90% of the vote with state media reporting a 40% turnout. Official results will be released April 2 by the elections authority.
- **Egypt's current account deficit narrowed** to USD 1.8bn in Oct-Dec 2017, compared to the USD 4.67bn deficit recorded during the same period a year ago. Tourism revenues surged to USD 2.28bn during the quarter (USD 826mn), while trade deficit widened to USD 9.81bn (USD 9.6bn), remittances rose to USD 7bn (USD 5.7bn), but net FDI declined to USD 2.184bn (USD 2.4bn).
- **Egypt's central bank cut key interest rates by 100bps**: overnight deposit rates were reduced to 16.75% from 17.75% and its overnight lending rate to 17.75% from 18.75%.
- **Egypt's M2 money supply growth accelerated** by 25.4% yoy in Feb (Jan: 20.4%) to EGP 3.295trn.
- **Iraq's oil reserves may be double the current estimated level**, stated the oil minister – most likely associated with potential increases in the future. Iraq had last year upgraded its reserve estimates to 153bn barrels

from their previous level of 143bn.

- **Kuwait** is inching closer to finalize an **agreement to purchase Iraqi gas** in the next two months, revealed Kuwait's minister of oil, electricity and water.
- **Jordan may issue USD 1bn Eurobonds** during Q4 2018, if deemed necessary, disclosed the finance minister.
- **Kuwait's nominal GDP** grew by 8.7% yoy to KWD 36.4bn (USD 120.2bn) in 2017 while real GDP reported a 2.9% yoy decline to KWD39.76bn. Transformative industries' contribution to GDP touched 7.2% at current prices and 5.7% at constant prices.
- **Budget deficit in Kuwait** narrowed by 7.7% mom to KWD 2.52bn (after deducting KWD 1.44bn for the Future Generations Fund), thanks to the 13.4% mom increase in revenues.
- **FTSE plans to upgrade Kuwait in two stages:** Kuwaiti stocks entering the index will be given 50% of their weightings in Sep and the remaining 50% in Dec, by then resulting in a 0.4% weighting in the index. The confirmed list of stocks will be published on Aug 24 this year.
- **Kuwait's ministries let go expatriate employees:** the Health ministry fired 253 expat employees from administrative jobs, effective Jul 1st; 85% of expat employees have been laid off at the Ministry of Electricity and Water, leaving only 1,351 as of Jan 2018.
- **Lebanon Ministry of Finance plans a USD 5bn debt swap with the central bank** to cut servicing costs and ease the burden of managing state debt (estimated at over 150% of GDP in 2017).
- **Lebanon's** central bank governor, in an interview, stated that **a managed devaluation of the currency was not being considered** as "it will be detrimental to confidence, detrimental to the economy and interest rates will go up much more".
- **Lebanon's Parliament approved the 2018 state budget,**

which estimates deficit at USD 4.8bn, marginally lower from 2017.

- **Unemployment rate in Lebanon has soared** to 46%, given selectiveness of Lebanese in choosing a job alongside willingness of Syrian refugees to work at much lower rates, according to the President. Official figures estimate unemployed at 25% among the general population and 35% among youth aged 18-25.
- **Oman nominal GDP grew** by 10.1% in the first nine months of 2017 thanks to the hydrocarbons sector gaining by 23.9% yoy and the non-hydrocarbons 4.9% yoy.
- **The total value of real estate deals in Oman** during Jan-Feb of 2018 **surged** by 24.6% yoy to OMR 565.3mn vs. OMR 453.5mn in the same period of last year.
- **Total credit from the financial sector in Oman increased** 7.3% yoy to OMR 23.7bn by end of Jan 2018, including a 5.8% yoy increase in total credit to the private sector to OMR 21.1 bn.
- **Qatar's international reserves and foreign currency liquidity edged down** to USD 37.6bn in Feb, from Jan's USD 37.7bn.
- **Foreign share ownership was raised to 49%** in the Qatar stock exchange listed shares of three subsidiaries of **Qatar Petroleum**.
- **Saudi Aramco will be ready for an IPO** in the second half of this year, stated its CEO on Bloomberg, while also acknowledging that the venue and the timing will depend on the government.
- The **Saudi CMA** chairman revealed that a **price stabilization mechanism would be introduced by end-Jun**: this allows underwriters of an IPO to use some of the company's stock to bolster its price, should it fall in the days after it starts trading, or the volume of shares changing hands is weak.
- **FTSE** announced that **Saudi Arabia would be classified as a "Secondary Emerging" market, starting Mar 2019**. This move is likely to add about USD 5.5bn of inflows from

passive funds linked to the Saudi market, according to the index provider's CEO. Saudi will account for about 2.7% of the emerging market index, rising to around 4.6% in the event of a 5% listing of Saudi Aramco.

- **Saudi Arabia** disclosed being **in discussions with Russia** to forge an unprecedented **10-20 year cooperation agreement**, essentially extending the short-term alliance on oil curbs that began in Jan 2017.
- **Saudi Arabia's** finance ministry **plans to reimburse contractors** working on **government projects** (agreed before Dec 2016) for increased expat fees.
- **Saudi Arabia and the US signed 46 deals** – including 13 in the oil and gas sector and 6 each in the defense and technology sectors – worth USD 400bn, set to create 750k jobs, during the US visit of the Saudi Crown Prince.
- **Passenger traffic** at **Saudi Arabia's** airports grew by 7.7% yoy to about 92mn in 2017 (from 741k flights). The country's 5 major airports accounted for 78mn passengers from a total of 594k flights during the year.
- **Saudi Arabia unveiled plans to build the world's largest solar power project**: the USD 200bn plan, in partnership with Softbank, will reach a capacity of 200 gigawatts. The first of the two solar parks will begin construction this year, and will start rolling out electricity by 2019. The plan will transform its solar power production, could see Saudi become a major solar power exporter, and create up to 100k jobs in solar power schemes alone.

UAE Focus

- **Inflation** in the **UAE declined** to 4.5% yoy in Feb, down from Jan's 4.8%. In mom terms, prices fell 0.2% in Feb (Jan: +2.7%). Prices of food and non-alcoholic beverages increased 6.5% yoy (Jan: +7.2%) alongside moderations in the costs of clothing and transportation; housing and utility prices fell 0.6% yoy, after a 0.5% decline the

month before.

- **UAE central bank assets grew** by 9.3% yoy to AED 398.6bn in Feb 2018, thanks to an increase in banks' deposits (up by AED 25.68bn from a year ago to AED 102.64bn in Feb).
- **Exports from UAE's free zones increased** by 6.6% yoy to AED 225.5bn (USD 61.4bn) in 2017, accounting for 19.5% of UAE's total exports.
- **Dubai's non-oil trade with South Korea was up** 8% yoy to AED 27.43bn (USD 7.5bn) in 2017; this included AED 22.1bn in imports, AED 4.47bn in exports and AED 866mn in re-exports.
- **Artificial Intelligence (AI) technologies** will help UAE to increase its GDP by 35% by 2031, according to a Ministry of Economy report. UAE's AI strategy will generate an annual economic return, in many sectors, of around AED 22bn (USD 5.98bn), through raising individual productivity by 13%, and also saving 396mn hours annually from commuting, reducing transportation costs by 44% (equivalent to AED 900mn) among others.
- The **value of contracts awarded to Emirati-owned SMEs in Dubai** touched AED 1.5bn in 2017 – taking the total value to AED 5bn since the launch of the Government Procurement Programme in 2002.
- The **volume of spending during the Dubai Shopping Festival increased** by 6.75% yoy in 2018, according to Network International (a payment solutions provider in the Middle East; processes more than 50% of all transactions across UAE). Spending using credit, debit, prepaid and other types of cards surged by 10.21% in 2015, followed by increases of 5.39% in 2016 and 10.76% in 2017.
- **Hotel guests in Abu Dhabi increased** by 15.2% yoy in Feb to a total of 405,849 visitors. Visitors from China surged by 83.6% yoy to more than 48,900 guests – there was a 50-fold increase in traffic to the Chinese language version of the Visit Abu Dhabi website over the

last three months.

- **Passenger traffic at the Dubai International Airport declined** by 0.3% yoy to 6.93mn passengers in Feb, with the airport handling 3.2% fewer flights during the month.
- A **survey commissioned by Visa** (of 500 consumers in the UAE) revealed very high awareness of **biometric technology** (51% stating “very familiar” with the technology) and 98% keen to use biometrics for payment; while better security compared to passwords and PINs was cited as the top benefit (45%), consumers also raised concerns about security and loss of sensitive information (48%).
- **UAE has pledged** AED 1.84bn (USD 500mn) to **support** the United Nations 2018 **Yemen Humanitarian Response Plan**; UAE has provided close to AED 10.4bn since Apr 2015.

Media Review

The US trade war will be an Afghanistan

<http://www.businessinsider.com/trump-china-trade-war-from-tariffs-hurt-economy-2018-3>

Omanisation needs to focus on quality

<http://timesofoman.com/article/130762>

The expansion is reaching a cusp

<https://www.marketwatch.com/story/this-is-the-beginning-of-the-end-for-this-economic-expansion-2018-03-26>

The US public debt is out of control

https://www.washingtonpost.com/opinions/the-debt-crisis-is-on-our-doorstep/2018/03/27/fd28318c-27d3-11e8-bc72-077aa4dab9ef_story.html

China Oil Futures

<https://www.bloomberg.com/news/articles/2018-03-26/china-s-first-ever-yuan-oil-futures-begin-trading-in-shanghai>

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