

# Weekly Economic Commentary – Jul 1, 2018

## Markets

Last week started on a negative note, due to the tussle on trade which affects sharply China (the Shanghai Composite closed in bear market territory) and most other emerging markets. Wall Street initially contained the losses thanks to a rebound in energy and tech stocks (and despite bank stocks hit a low for the year), but the rest of the week saw selling orders dominate, as the trade war fears intensified. All major bourses recorded weekly losses which marked also a rather negative month (the Dow Jones lost almost 2%). In Europe the broadly positive end of the European Council helped to contain the losses. MENA markets were also skewed to the downside with the exception of Dubai, Qatar and Bahrain (the latter supported by the Saudi-led rescue package). In bond markets the US 2-10y spread hits a fresh 11y low at 33bps. In currency markets the yen slipped in response to trade tensions while the euro regained ground; the largest movements involved emerging currencies: the yuan touched new lows for the year, while rising energy prices sent India's rupee to an all-time low against the dollar. The oil price continued its positive streak, unfazed by the additional output agreed in the Opec-Russia deal and sustained by the disruptions at a Libyan port; a draw of 9.9 mn barrel in US crude inventories further boosted the upward swing. Gold prices slipped close to the lower bound of its multi-month trading range, despite resurgent inflation.

## Global Developments

### **US/Americas:**

- **US core PCE** index (the Fed's preferred gauge of

inflation) **rose** 0.2% mom (2.0% yoy) in May the same rate as in Apr (when it was 1.8% yoy), hitting the Fed's target for the first time in 6 years.

- The final estimate showed that the **US GDP expanded** by a paltry 2% qoq ann. in Q1, down from a first estimate of 2.3% and 2.9% in Q4. The slowdown resulted mainly from disappointing consumer spending.
- **New orders for US manufactured durable goods fell** -0.6% mom in May adding to a -1% drop in Apr, due to a sharp slowdown in transportation equipment. Meanwhile, orders for non-defense capital goods ex. aircraft, a proxy for business spending plans, slipped -0.2% vs a 2.3% surge in Apr.
- **US trade goods deficit** in May **shrunk** by USD 2.5 bn to USD 64.8 bn, the smallest goods deficit in more than a year. Nominal exports rose 2.1% mom, while imports gained 0.2%. Capital goods and foods, feeds and beverages provided the largest support to exports.
- **The S&P CoreLogic Case-Shiller US national home price index** in Apr **rose** 6.4% slightly down from 6.5% in Mar.
- **US sales of new single-family houses jumped** 6.7% mom to an annual sa rate of rate of 689,000 in May recouping a -3.7% fall in Apr. It is the highest rate since Nov.
- **US pending homes sales tumbled** -2.2% yoy (-0.5% mom) in May following a -2.1% (-1.3% yoy) drop in Apr. It is the fifth consecutive month of yoy declines.
- The **US Conference Board Consumer confidence index dipped** -2.4 points in Jun to 126.4, as consumer expectations fell to their lowest level since Dec. Present situations were strong, but faltering business and income expectations weighed in. Inflation expectations remained exceptionally high at 4.9%.
- **US initial claims for unemployment benefits** reached 227,000 from 218,000, but remain historically low. The 4-week moving average rose by 1,000 to 222,000. Continuing claims fell by 21,000 to 1.705 mn.
- **Nominal personal income in the US rose** by 0.4% mom in

May vs 0.2% in Apr. Nominal disposable income grew at the same rate up from 0.3% in Apr. Real disposable income was up 0.2% mom.

## Europe:

- **Inflation rate in the eurozone** touched 2% yoy in Jun vs 1.9% in May, the highest rate since Feb 2017, lifted by higher energy and food prices.
- The **business climate indicator for the eurozone** lost only -0.05 points to 1.39 in Jun from May. Managers' appraisals of total and export orders worsened markedly, while their assessments of the past production and the stocks of finished products was flat . By contrast, managers' production expectations improved substantially.
- **The German Ifo Business Climate Index** was marginally down at 101.8 in Jun from 102.3 in May, the lowest reading in a year, caused primarily by worsening business conditions (105.1 from 106.1), while the gauge of future expectations was unchanged at 98.6. Sentiment worsened uniformly across all sectors.
- **German inflation** crawled back to 2.1% yoy in Jun from a 15-month high of 2.2% in May. Services inflation eased while energy prices kept climbing.
- **German retail sales** dived -2.1% mom (-1.6% yoy) in May wiping out the 1.6% (1% yoy) rise in Apr, the sharpest fall since May 2011.
- **The UK current account** shrunk to GBP 17.7bn in Q1 from GBP 19.5bn in Q4, thanks to a lower trade deficit (GBP 1.9bn vs GBP 3.8bn in Q4).

## Asia Pacific:

- **The official NBS Manufacturing PMI in China** fell to 51.5 in Jun from 51.9 in May. Output (53.6 from 54.1 in May) and new orders (53.2 from 53.8) rose more slowly while new export orders declined for the first time in 4

months (49.8 from 51.2). Employment (49.0 from 49.1), raw materials in stock (48.8 from 49.6) and orders in hand (45.5 from 45.9) dropped again.

- **The official NBS Non-Manufacturing PMI in China crawled up to 55.0 in Jun from 54.9 in May.**
- **The unemployment rate in Japan unexpectedly declined to 2.2% mom in May from 2.5% in Apr, the lowest rate since 1992.**
- **Industrial production in Japan surged 4.2% yoy (-0.2% mom) in May, accelerating from 2.6% (0.5% mom) in Apr. On a monthly basis the drop was due to metal industries output and electrical machinery.**
- **Retail sales in Japan plunged -1.7% mom (0.6% yoy) in May more than offsetting the 1.3% (1.5% yoy) jump in Apr. Since the start of this year only 2 months recorded positive mom growth figures.**
- **South Korea trade surplus narrowed to USD 6.3bn in Jun from USD 10.7bn in a year earlier. It was the smallest surplus since Feb.**
- **Industrial production in South Korea increased 1.1% mom (0.0% yoy) in May, after surging 3.1% (0.8% yoy) in Apr.**
- **Consumer Confidence in South Korea dropped to 106 in Jun from 108 in May.**
- **The Bank of Indonesia hiked its rates by 50 bps, vs expectations of a 25-bp increase.**

**Bottom line: Some key macro data on both sides of the Atlantic were mildly negative – from the US GDP and durable goods orders to German retail sales – while in Asia they were mildly positive, especially in Japan. But the horizon is dominated by worries over an impending paradigm shift. A secular consensus on the benefits of global trade and cooperation is under attack from a protectionist US administration. Whether the US pressure on the pillar of global growth can be contained is the question that keeps investors and top managers awake at night. In any case the uncertainty ensuing from Trump's reckless tactics has already inflicted notable damages to**

global growth: it is unlikely that firms will increase investment in such a poisonous climate. In emerging markets Argentina, Turkey, and Brazil play the role of the 'canaries in the coal mine' alerting on serious disruptions in emerging markets.

### Regional Developments

- **Saudi Arabia, UAE and Kuwait pledged to support Bahrain financially**, thereby also calming investors concerns. Prior to the announcement, the country's credit default swaps had risen to a record high 543 points, sovereign bonds had fallen to record lows and the dinar had weakened in the spot market (prompting the central bank to commit to its currency peg). **No details of the aid package were revealed**, but the market response was favourable – CDS spreads were down and appetite for government debt recovered.
- **Bahrain**, as it awaits financial aid from its regional peers, **plans to balance its finances**: the PM announced the set up of a committee, including the finance minister and central bank chief, to devise a plan to balance the budget.
- **Egypt's central bank left interest rates unchanged**: its deposit and lending rates were left at 16.75% and 17.75% respectively. The central bank also expects one-off increases in inflation, following the latest round of austerity measures (including the fuel and electricity price hikes).
- **Money supply (M2) in Egypt grew** by 19.31% yoy in May (Apr: 21.36%) to EGP 3.4trn (USD 190bn).
- **Egypt's current account deficit narrowed** to USD 1.93bn in Q3 of the 2017-18 fiscal year, from USD 3.1bn a year earlier, thanks to an increase in tourism revenues (to USD 2.27bn from USD 1.256bn a year ago) and expat remittances (to USD 6.46bn from USD 5.78bn a year ago). Overall balance of payments improved, recording a

surplus of USD 5.38bn in the Jan-Mar quarter versus USD 3.97bn a year before.

- **Remittances into Egypt increased** by 23.6% yoy to USD 19.53bn during Jul 2017-Mar 2018 period, according to the central bank.
- **Egypt's exports to Russia increased** by 41% yoy to USD 284mn during the first four months of this year, according to the minister of trade and industry, supported by the increase in exports of fruits and vegetables.
- **The Egyptian tax authority expects to collect nearly EGP 6bn in tax revenues from the ride-sharing apps** Uber and Careem. This follows the executive instructions issued earlier this month stating that the smart mass transport service would be subject to a 13% retroactive VAT as of 8 Sep 2016 and a 14% of the value as of 1 Jul 2017.
- **Egypt's President ratified a basic salary increase for state employees:** with more than 6.5mn Egyptians registered as state employees, this is expected to cost the state EGP 24bn.
- **The IMF approved payment of USD 2.02bn to Egypt,** the fourth installment of the USD 12bn loan, bringing the total received so far to USD 8bn.
- **Egypt's parliament approved the extension of a nationwide state of emergency for three months** from Jul 14.
- **A manual recount of votes in Iraq's May election will begin this week,** according to the parliament speaker. The panel of judges now in charge of the recount stated that the recount would only be conducted for "problematic" ballots. In the meanwhile, Iraq's parliament held its final session on Saturday (Jun 30), leaving the country without a national assembly for the first time since 2013.
- **Jordan's trade deficit narrowed by 5% in H1 this year,** supported by a 4% pickup in exports and a 2.5% dip in imports.

- **The World Bank plans to extend USD 500mn** in concessional and non-concessional financing to support **Jordan's ongoing reforms** like promoting inclusive growth, and job creation among others.
- **Kuwait's GDP grew by 1.6% in Q1 this year**, with the oil sector's contribution at 48.4% (compared to 44.5% in the same quarter a year ago).
- **Kuwait's energy minister disclosed that it would raise oil production by 85k barrels per day (bpd)** to 2.785mn, from this week.
- **Nearly 400 refugees started to leave Lebanon for Syria last week**, reported *Reuters*. More than 1 million have fled Syria to Lebanon, according to UNHCR though the government puts the number higher at 1.5mn (or a quarter of the total population).
- **Credit by commercial banks in Oman increased 6% yoy** in Q1 and stood at OMR 20.9bn. Personal loans accounted for OMR 8.22bn or 39.4% of the total banking credit.
- **Qatar's bank deposits declined by 1.11% mom** to QAR 785.43bn (USD 215.76bn) in May, due to a decline in non-residents' deposits. In yoy terms, deposits were up 3.04%.
- **Saudi Arabia boosted oil supply to 10.7mn barrels per day (bpd) in June**, up 700k bpd from May and close to a record high, reported *Reuters*. July output is expected to show a further jump, with production plans estimated at 11mn bpd. Separately, Trump tweeted that, in a conversation with the Saudi King, the latter had agreed to raise oil output by "maybe up to 2mn barrels".
- **Inflation in Saudi Arabia eased to 3% yoy** in May (Apr: 2.5%); housing and utilities costs declined by 0.4% while food and beverages and transport costs were up by 5.3% and 10% respectively. In mom terms, prices were down by 0.4% in May, following a 0.2% dip in Apr.
- **Saudi Arabia's finance ministry sold SAR 3.1bn (USD 827mn)** in its **monthly domestic sukuk sale**, bringing the total size of the sukuk issue, divided into five-

seven- and 10-year tranches, to SAR 12.05bn.

- **Saudi Arabia's exports grew** by 17.5% yoy and 2.2% qoq to SAR 243.71bn in Jan-Mar 2018. Oil exports grew by 15.9% to SAR 187.53bn during the 3-month period while non-oil exports were up 23.5% yoy (and 0.8% qoq) to SAR 56.18bn.
- Without indicating the reasons for non-compliance, the **Saudi Arabian Monetary Agency has warned 14 insurance firms that their licenses could be withdrawn**. If their practices are not reviewed within 20 days (from Jun 26), the regulator would proceed requesting the license withdrawal.
- **More than 120k women have applied for licenses in Saudi Arabia** and the demand is very high, according to a spokesman for the Ministry of Interior.
- A **2018 Global Business & Spending Survey by American Express** shows **UAE and Saudi Arabia to be more confident to increase spending and investment levels** in their business. Around 84% and 83% of finance executives in the UAE and Saudi Arabia respectively were upbeat. Almost three quarters (73%) of Middle East respondents expect to increase headcount by 6% or more this year, compared to 71% globally.
- According to **EY's MENA Hotel Benchmark Survey report**, in Apr 2018, **Abu Dhabi** reported the highest occupancy rate of 87.9% and **Dubai** posted the highest RevPAR of USD 235, as well as maintaining the highest average room rate of USD 288.
- **Cost of living in Abu Dhabi and Dubai** were shown to have **declined** in Mercer's 24th Annual Cost of Living survey, with the latter dropping to 26<sup>th</sup> most expensive city globally from 19<sup>th</sup> previously; Abu Dhabi slipped to 40 from 22 before. However, the main reason for the cost of living to have dropped is the depreciation of the dollar (and hence AED) versus other major currencies; dip in rentals also supported. Riyadh however moved up to 45<sup>th</sup>

spot from 52<sup>nd</sup>

## **UAE Focus**

- **Inflation in Abu Dhabi edged down** to 3.2% in May (Apr: 3.4%).
- **Money supply (M1) in the UAE declined** by 3.3% mom to AED 500.1bn at end-May, due to a dip in monetary deposits. M2 also declined, by 0.7% to AED 1.204trn. Gross bank assets were up 0.9% while gross credit grew by 0.7%.
- **Abu Dhabi implements the “Tamm” system**, which reduces the process of obtaining an economic license from 8 to only one step – without the need to visit any government entity. This move will improve business competitiveness and raise the average rate of issuing licenses.
- **Abu Dhabi Global Market launched its framework to regulate spot crypto asset activities**, including those undertaken by exchanges, custodians and other intermediaries in ADGM, following a public consultation.
- **Sharjah aims to increase FDI by at least 15% this year:** the Sharjah Investment and Development Authority (Shurooq) stated that the current FDI is around AED 7bn (USD 1.9bn) versus the AED 5.97bn worth FDI it attracted last year.
- **Dubai World Trade Centre announced a 50-70% reduction on licensing and incorporation fees**, with a 40-50% reduction on immigration related service fees depending on the scale of business operation within the free zone Authority.
- A product called **Gofreelance** has been created to support **freelancers in the education and media sectors** the freedom of the ‘gig economy’ through licenses for activities such as education advisor, executive coaching, film director, and scriptwriters, among others. This will provide access to facilities at Dubai Media City and Dubai Knowledge Park.
- **Bilateral trade between UAE and Hong Kong touched USD**

10.87bn in 2017, from USD 10.59bn a year ago. Road vehicles, telecommunications equipment, electrical machinery are few of the top imports from Hong Kong.

- **Abu Dhabi topped the list of Smart Cities in the Middle East**, in a McKinsey Global Institute study. The capital, with a score of 18.4, was ranked ahead of Dubai at 17.3. The report can be accessed at: <https://www.mckinsey.com/industries/capital-projects-and-infrastructure/our-insights/smart-cities-digital-solutions-for-a-more-livable-future>

### **Media Review**

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<https://www.topdowncharts.com/single-post/2018/06/18/Chart-Global-Trade-High-Frequency-Indicators>

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<https://www.ft.com/content/f2cdebd8-7949-11e8-8e67-1e1a0846c475>

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[https://www.zawya.com/mena/en/story/Gulf\\_countries\\_to\\_benefit\\_from\\_OPEC\\_output\\_hike\\_analysts-SNG\\_119919919/](https://www.zawya.com/mena/en/story/Gulf_countries_to_benefit_from_OPEC_output_hike_analysts-SNG_119919919/)

**Trump, trade wars and China**

<https://www.project-syndicate.org/commentary/section-301-report-wrong-on-china-trade-by-yongding-yu-2018-06>

<https://www.vox.com/world/2018/6/29/17515260/china-tariffs-trump-soy-trade-war>

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<https://af.reuters.com/article/metalsNews/idAFL8NITS1U0>

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