

Weekly Economic Commentary – Jul 22, 2018

Markets

Global stock markets started last week on a cautious note waiting for Powell's Congressional testimony and the repercussions of the Trump-Putin summit. The Fed's Chairman's positive remarks gave a little jolt to US equity prices but then at the end of the week the announcement of further sanctions against China pulled the indices down (despite good earning reports) to close the week flat. In Europe the dynamics was almost identical while in Asia the Shanghai Composite fell during the week and recovered on Friday. Emerging markets managed to contain the losses in volatile trading. Despite the jitters spurred by the trade war, global equities markets are living a bullish summer even if fundamentals are not particularly uplifting. In regional markets KSA hit a 3-year record thanks to an upbeat banking sector (at a 52 weeks high) and the UAE continued its positive streak. Other bourses lagged behind with Egypt suffering from the volatility in emerging markets. The dollar started the week very strong against major crosses, touching a six-month high against the JPY, and breaching the 1.3 level against the GBP for the first time since Sep 2017 (due to weak retail sales). Then on Thursday Trump's criticism against the Fed and an escalation in the trade war led to a precipitous retreat of the green back. China's yuan remains on the back foot after slipping close towards a one-year low. In general Asian currency volatility is part of an emerging-market tempest: in Q2 emerging markets currencies had their worst fall against the dollar in seven years. Oil prices plunged at the beginning of the week and then recovered a little despite US crude inventories growing by 5.8 mn barrel against predictions of a 3.5 mn barrel draw. US oil production reached in mid July 11

mn barrel per day, an all time record. Gold prices have fallen below most technical support levels for no particular reason.

Global Developments

US/Americas:

- **The US Fed's Chairman Powell** in his periodic Senate testimony **reaffirmed the commitment to normalize interest rates**, with two additional hikes this year, as economic growth remains perky thanks to supportive monetary policy. The normal size of the Fed's balance sheet remains anybody's guess.
- **President Trump expressed his dissent over the Fed's rate increases**, violating a taboo of economic policy. Later he announced potential additional tariffs on imports from China worth USD 500 bn. The administration also lashed out at China for forcing US firms to transfer technologies to Chinese entities.
- **The Fed's July Beige Book indicates that economic activity expanded moderately or modestly** in 10 of the 12 districts, while the Dallas district was booming and the St. Louis district was downbeat. Firms are worried about trade policies, which are leading to higher prices and supply disruptions. Labor markets are tight. Home sales are rising slowly, but contracts seem unaffected by rising interest rates.
- **US industrial production grew 3.8% yoy (0.6% mom)** in Jun, following a 3.2% (-0.5% mom) rise in May, to mark a record pace since Jul 2014. Manufacturing went up 1.9%, utilities 5% and mining soared 12.9%.
- **US retail sales in Jun rose 0.5% mom (6.6% yoy)** adding to the 1.3% growth in May in the wake of upbeat autos sales. Ex autos, sales grew 0.4% mom led by drugstores, restaurants, online retailers and fuel stations.
- **The US Conference Board's Leading Indicators Index rose 0.5% mom** in Jun after being flat in May. Of all components, only building permits declined.

- **Housing starts in the US plummeted** -12.3% mom to an annualized rate of 1.17 mn in Jun, following a 4.8% rise in May. It is the sharpest drop since Nov 2016.
- **US business inventories rose** 0.4% mom in May, marginally up from 0.3% in Apr. All 3 categories rose: merchant wholesalers advanced 0.6%, retailers 0.4%, manufacturers 0.2%. Business sales surged 1.4%.
- **US initial unemployment claims fell** by 8k to 207k a new cyclical low. The 4-week moving average fell by 2,750 to 220,500. Continuing claims rose slightly by 8,000 to 1.751 mn.

Europe:

- **The Eurozone's inflation** reached 2% yoy in Jun vs from 1.9% in May, due to food and energy inflation. Core inflation cooled to 0.9%, from 1.1% in May.
- **The Eurozone's trade surplus shrunk** in May to EUR 16.5bn, from EUR 19.3bn a year earlier. Imports rose 0.7% yoy while exports declined -0.9%.
- **UK inflation was unchanged** at 2.4% yoy in Jun. Energy and transportation were pushed up by higher electricity and Brent prices, while textile and recreation inflation fell.
- **UK retail sales unexpectedly declined** by -0.5% mom (2.9% yoy) in Jun after growing by 1.4% (4.1% yoy) in May. Good weather and the World Cup pushed up food sales, at the expenses of nonfood sales.

Asia Pacific:

- **Chinese GDP expanded** by 6.7% yoy in Q2 vs 6.8% in Q1. It was the weakest pace of expansion since Q3 2016 as the deleveraging continues to exert its drag.
- **China's industrial production growth slowed** to 6% yoy in Jun from 6.8% in May, with weakness spread across all sectors: manufacturing (6% vs 6.6% in May); electricity, gas and water (9.2% vs 12.2%); and mining (2.7% vs 3%).

- **China's fixed-asset investment increased** by 6% yoy in H1, compared to a 6.1% in the Jan to May period. It was the weakest pace since the series began in 2004, as a result of anemic public investment (3% vs 4.1% in Jan-May), while private investment rose 8.4% (vs 8.1%).
- **China's retail sales increased** 9% yoy in Jun vs 8.5% rise in May.
- **Japan's core CPI**, which includes energy prices, **was up** 0.8% yoy in Jun, while the core-core CPI, excluding food and fuel, was up 0.2% yoy, (-0.1% mom). Essentially, energy prices are the only source of inflation in Japan.
- **Japan's trade surplus** was JPY 66.25bn in Jun, after posting a deficit of JPY 297bn in May.

Bottom line: Having started the year believing in a synchronised acceleration in global growth, the market consensus is now contemplating a widening divergence in economic performance, and therefore in monetary policy stance, with only the US benefiting from the pro-growth policy mix. On the contrary in the euro area, growth is faltering in Japan and the United Kingdom: the IMF in an update of its World Economic Outlook continued to project global growth of 3.9% for 2018 and 2019, but warned that this strong growth is *“less even, more fragile [and] under threat.”* In essence the trade war *“could derail the recovery and depress medium-term growth prospects, both through their direct impact on resource allocation and productivity and by raising uncertainty and taking a toll on investment”*. If current trade threats (which do not include the latest threat on Chinese imports worth USD 500 bn) are realized and business confidence falters, global output could be 0.5% below current projections by 2020, the IMF estimated. Equity markets have a different view: the S&P 500 has jumped more than 2% this month underscoring optimism that the trade fight will be resolved before the next midterm elections in the US.

Regional Developments

- The **IMF**, in its Jul update of the World Economic Outlook, **increased its growth estimates for the MENA region** to 3.5% this year and 3.9% for 2019. Though the outlook for oil prices improved, the need for fiscal consolidation and intensifying geopolitical risks continue to weigh on growth among the oil exporters, according to the Fund.
- **Egypt revealed the first 5 state companies that plan to float shares** later this year on the Cairo Exchange. This includes Alexandria Mineral Oils Company, Eastern Tobacco, Alexandria Container and Cargo Handling, Abou Kir Fertilizers, and Heliopolis Housing.
- **Egypt is establishing a EGP 200bn (USD 11bn) sovereign wealth fund**: the parliament passed a law approving EGP 5bn start-up capital for the fund called "Egypt Fund", with EGP 1bn to be transferred from the Treasury.
- **Remittances into Egypt are expected to rise** to USD 26bn (up 49% yoy) in the 2017-18 fiscal year, according to the central bank. The apex bank revised down the 10-month remittance inflow to USD 21.9bn (from the previously reported USD 26bn).
- An amendment passed by Parliament allows **Egypt to offer citizenship to foreigners** who deposit at least EGP 7mn (USD 392k) in the country, if they surrender the deposit to the Treasury after five years.
- **Jordan's Ministry of Labour** has issued over 106k **work permits for Syrian refugees** so far while the number of workers in the informal economy remains at an estimated 300k, according to a senior official.
- **Currency in circulation in Kuwait posted a decline** of 3.2% yoy and 1.6% mom to KWD 1.84bn (USD 6.1bn) in Jun.
- **Saudi Arabia and Kuwait have established a coordination council** to boost bilateral ties: bilateral trade has increased to USD 2.34bn in 2015 from USD 506mn in 2001. This move follows other coordination councils set up with a number of countries including the UAE and Iraq.
- **Electrical power generated from "rooftop" solar**

photovoltaic systems in Lebanon now exceeds 50 megawatts, from about 9.45 MW in 2015, according to the general-director of the Lebanese Center for Energy Conservation.

- **Oman's government deficit** plummeted to OMR 1.1bn during the Jan-May 2018 period, down from OMR 2.03bn during the corresponding period of 2017 thanks to a rebound in oil prices and expenditure consolidation. **Oman's government revenues surged** 23.2% in the first five months of 2018 to OMR 4.1bn.
- **Deposits at Omani conventional banks** were down by 0.8% yoy to OMR 18.9bn in Apr.
- **Qatar's industrial production index (IPI)** grew 4.7% yoy and 3.3% mom to 108.5 in May 2018, thanks to a pickup in the mining segment (+6.3% yoy) and supported by an increase in crude oil and natural gas production (+3.6%).
- **Passenger traffic at Qatar's international airport** fell 13% yoy to 16.5mn in H1 this year, while cargo volumes grew by 7.6% yo 1.05mn tonnes.
- The **IMF revised upwards Saudi Arabia's growth forecast for this year**, to 1.9%, up 0.2 ppts from its Apr forecast. Growth for 2019 was kept unchanged at 1.9%.
- **Around 350k new jobs will be created in Saudi Arabia** across various sectors in the near future, reported *Al Madina* newspaper quoting GaStat figures. The food, commercial and housing sectors will provide the biggest opportunity, offering roughly 38,000 vacancies for Saudi citizens and 67,000 vacancies for foreigners.
- **Expat remittances from Saudi Arabia** fell 0.2% yoy to SAR 60.46bn during Jan-May period, according to SAMA. Remittances grew by 8.8% mom and fell by 2.2% yoy to SAR 12.75bn in May 2018.
- **Saudi Arabia** reported a **trade surplus** of SAR 122mn (USD 33mn) **with Egypt** in Q1 2018. Saudi non-oil exports to Egypt were SAR 1.55bn in Q1, and imports stood at SAR 1.4bn.

- **Saudi Arabia approved the license for Commercial Bank of Iraq** to open a branch in the country. One of the first private sector banks set up in Iraq, the Commercial Bank of Iraq is also partly owned by Bahrain's Ahli United Bank (which has a 64.71% stake).
- **Saudi Arabia plans to install some 2.5mn smart electronic meters** in the coming three years in the residential, commercial and industrial sectors

UAE Focus

- **The Chinese President was on a State Visit in the UAE** last week, the first visit by a Chinese leader in 29 years. This trip witnessed the establishment of a comprehensive strategic partnership, with cooperation in areas of economy, trade and energy. The two nations signed 13 MoUs and agreements to boost non-oil bilateral trade by more than 9% to USD 58bn this year. The UAE accounts for 30% of China's total exports to Arab countries and 22% of total Chinese-Arab trade. (More: <https://www.thenational.ae/uae/uae-and-china-declare-deep-strategic-partnership-as-state-visit-ends-1.752515>)
- The Abu Dhabi Global Market (ADGM) **announced the establishment of the first Chinese state-owned financial services firm** – Industrial Capacity Cooperation Financial Group – in the free zone, to provide investment and financial support to Chinese firms in the Khalifa Industrial Zone of Abu Dhabi and as part of the Belt and Road initiative.
- **UAE's strong trade-tourism ties with China:** Dubai's trade with China grew by 6% yoy to USD 48bn in 2017, wither-exports up 60% to AED 4.99bn. Non-oil trade between Abu Dhabi and China was AED 13.2bn (USD 3.59bn) in 2017, accounting for 8.2% of the total trade in the emirate. Dubai reported a 119% increase in overnight Chinese visitors since 2014 and a 41.4% yoy increase in 2017; in the Jan-May period, there were a record 400,547

visitors from China.

- **UAE's Federal Tax Authority** urges buyers of **commercial real estate** to pay the due VAT before proceeding with the transfer of ownership.
- **Real estate brokerage commissions in Dubai** touched AED 571mn in H1 this year, disclosed the Dubai Land Department, from 5181 active brokers (including 678 female brokers). This is a 30% dip from the same period a year ago, given the substantial drop in the value of property transactions.
- In a move offering more support for UAE businesses, **Ajman Media City Free Zone** announced plans to **scrap a compulsory security deposit on visas** for new companies.
- The **Dubai Department of Economic Development** issued **1185 new business licenses in Jun**, with renewals amounting to 11,043 transactions. Among the new licences, 61.9% were commercial, 35.6% were professional, while industrial and tourism accounted for 1.4% and 1.1% respectively.
- The Dubai International Financial Centre (**DIFC**) reported an **8% increase in the number of active registered companies** to 2003 in H1 this year (+14% yoy), with 614 regulated firms.
- **Emirates NBD** disclosed an **exposure** of AED 78.24mn (USD 21.3mn) in **Abraaj's** asset management business. It also revealed AED 64.65mn (USD 17.6mn) exposure in three of Abraaj's funds. Separately, multiple bidders (including an Abu Dhabi investor) are being considered by the joint provisional liquidators (PwC and Deloitte) for buying the firm's investment management business.
- In a bid to boost tourism during the summer months, the **UAE Cabinet** announced an **exemption of visa fees for dependents** aged 18 and below. The exemption is applicable between Jul 15- Sep 15.
- **Dubai Duty Free sales** are up 10% yoy to USD 1bn in H1 2018, with retail sales in the Departures area showing an 11% increase to AED 3.2bn in the same period.
- **Dubai was included as one of the world's top five in**

the International Shipping Centre Development Index, joining Singapore, Hong Kong, London and Shanghai.

- **Sharjah Airport** reported a 4.34% yoy **growth in passenger traffic** to 5.73mn in H1 2018.
- **A new Salik (toll) gate will be operational from Oct 24th in Dubai,** and is expected to reduce traffic by 25% on Dubai's Sheikh Zayed Road. This will be Dubai's 7th tollgate, and is expected to generate more than AED 300mn in annual revenues, in addition to the estimated AED 2bn annually from the 6 other existing gates.

Media Review

IMF's World Economic Outlook, July 2018 update

<http://www.imf.org/en/Publications/WE0/Issues/2018/07/02/world-economic-outlook-update-july-2018>

Trump's attack on the Fed is futile and damaging

<https://www.wsj.com/articles/trumps-fed-outburst-all-downside-no-upside-1532089274>

The trade war is getting out of hand

<https://www.ft.com/content/40acba7a-8c08-11e8-b18d-0181731a0340>

Xi Jinping's Superpower Plans

<https://www.wsj.com/articles/mr-xis-superpower-plans-1532013258>

How to rescue the WTO

<https://www.economist.com/leaders/2018/07/19/how-to-rescue-the-wto>

Sabir stake acquisition and the Aramco IPO timing

<https://www.ft.com/content/b6ab0f4a-8cc8-11e8-b639-7680cedcc421>

<https://www.thenational.ae/business/energy/aramco-s-potential-sabic-stake-acquisition-could-impact-ipo-says-ceo-1.752547>

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