

# Weekly Economic Commentary – Sep 30, 2018

## Markets

Concerns over trade tensions resurfaced at the beginning of last week due to China's retaliatory tariffs, and lingered even after the Fed announced its largely expected rate hike; ultimately Wall Street ended on a weak note as investors started to express doubt on the outperformance of the US economy. On the positive side, the S&P500 ended Q3 with the best quarterly results since 2013. Elsewhere, European bourses suffered from the turmoil caused by the Italian government's fiscal recklessness, while Japanese stocks were lifted by positive macro data and the weak yen. Emerging markets remained on the back foot as market participants debate whether the worst is over. Regional stock markets surged in response to the upwards movement in oil prices', with the exception of Bahrain which still needs external support for its economy. In currency markets the euro, after being supported by Draghi's hawkish comments, retrenched vis à vis the USD in the wake of the FOMC meeting. The Brent oil price touched a 4-year high after OPEC and Russia ruled out further output increases, despite clumsy public pressures from Trump. Furthermore, uncertainty over the effects of the US sanctions against Iran induced traders to take long positions, even though US oil inventories grew by 1.9 mn barrels vs predictions of a 1.1 mn draw. The price of Oman oil spiked to almost USD 89/b. Gold prices hovered in the vicinity of USD 1200/ounce.

## Global Developments

### **US/Americas:**

- **The US Fed raised the fed funds target range by 25bps to 2.00-2.25% which brought to 200 bps the cumulative hike since Dec 2015. The Fed projected one more hike this**

year and possibly three in 2019, based on an assessment of stronger growth and tame inflation. The central bank removed from the final statement prior assurances that policy will remain “accommodative”.

- **The third and final estimate of the US GDP confirmed that growth in Q2 was 4.2% qoq ann.**, supported by the fiscal stimulus and strong job growth. The only substantial drag were inventories.
- **US goods trade deficit rose** to USD 75.83bn in Aug from USD 72.05bn in Jul. Exports dropped -1.6% mom due to the ongoing trade tensions. Imports rose 0.7%.
- **New orders for US durable manufactured goods** in Aug **jumped** by 4.5% mom, vs -1.7% in Jul driven by the volatile nondefense aircraft segment, which surged 69.1% mom. Core capital goods orders fell by -0.5% and inventories by -0.4%.
- **US wholesale inventories rose** 0.8% in Aug vs 0.6% in Jul. Retail trade inventories were up 0.7% vs 0.6% in Jul. These figures will boost GDP growth in Q3.
- **The Conference Board consumer confidence index advanced** 3.7 pts mom to 138.4. The assessment of the economic climate rose modestly, with the present situations index gaining 0.3 pts. But the main drivers were expectations (up 6 points to 115.3) and business conditions.
- **The S&P CoreLogic Case-Shiller national home price index growth fell** to 6% yoy in Jul from 6.2% in Jun.
- **The US pending home sales index dropped** -1.8% mom to 104.2 in Aug from 106.1 in Jul, almost a record low since late 2014.
- **US initial jobless claims spiked** by 12k to 214,000 due to Hurricane Florence. The 4-week moving average increased to 206,250 and continuing claims from 1.645mn to 1.661mn.

**Europe:**

- **Inflation in the eurozone rose** to 2.1% yoy in Sep from 2.0% in Aug, a 66-month high, lifted by energy prices. Core inflation declined to 0.9% yoy in Sep from 1.0% in Aug.
- **The eurozone's Business and consumer sentiment indicator fell** to 110.9 in Sep from 111.6 in Aug. The mood across Europe is turning sour as manufacturers' expectations falter. At country level, sentiment was steady in Germany, while it dropped 1.7 pts in France and 1.5 pts in Spain.
- **The Italian government decided to ignore the limits** on the deficit to GDP ratio agreed with the EU for the next three years, heading for a collision course with bond markets, the ECB and the EU authorities. The move also violates the Constitution, which imposes a balanced budget.
- **The German IFO business confidence index held steady** at 102.2 in Sep on the back of improved current business situation, although expectations weakened slightly. The survey and other indicators point to economic growth of 0.4% qoq in Q3.

### **Asia Pacific:**

- **The Caixin China Manufacturing PMI fell to a 16-month low** of 50 in Sep from 50.6 in Aug just on the threshold between recession and expansion. Output growth crawled back, new orders stalled, and new export business fell the most since early 2016. Also, employment dropped at the fastest rate in 14 months.
- **Japan's industrial production fell** -0.1% mom in Jul, after plummeting -1.8% in Jun. Tech sectors lifted the headline, particularly information and communications and electrical machinery.
- **Japan's retail sales increased** by 1.5% yoy in Jul, following the 1.7% rise in Jun, led by fuel and sustained also by auto and medical expenses.

- **The unemployment rate in Japan declined** to 2.4% in Aug, the same rate as in Jun after a blip up to 2.5% in Jul. New jobs surged by 260k, while the number of unemployed fell by 50k.
- **The Bank of Korea's Consumer sentiment index fell** 1.8 pts to 99.2 in Aug from 101 in Jul.
- **Bank Indonesia hiked the 7-day reverse repo rate by 25 bps** to 5.75% reiterating its hawkish "preemptive" stance to stem capital outflows and support the rupiah (amongst Asia's worst-performing currencies in 2018). This cumulative tightening since mid-May added to 150 bps.

**Bottom line: In the US, capacity constraints, cost pressures and labour shortages are increasingly prevalent. If new investments and immigration do not remove these bottlenecks the expansion will run into a wall. Inflation pick-up, low unemployment and wage rises are all symptoms of late cycle risks. Monetary policy cannot ignore that the economy has fully recovered from the Great Recession and should focus more aggressively on removing the unprecedented stimulus. The trade tensions for now are offset by the bullish atmosphere but companies are tending to delay investment decisions: an Atlanta Fed survey revealed that 30% of manufacturers were reassessing their capital plans because of tariff worries. In Europe the political malaise spurred by 'sovereignist' parties is sapping business and consumer confidence, while the Italian challenge to the EU austerity poses a bigger threat than the Brexit.**

### **Regional Developments**

- **Bahrain's GCC counterparts are planning a 5-year aid package** of almost USD 10bn to support the country's financing needs, reported *Bloomberg*, with the package including deposits and low-interest loans. Though the final amount has not been agreed, the funds would allow the nation to borrow from international debt markets at cheaper interest rates.

- **Bahrain plans to approve VAT and pensions reform laws** before the upcoming election on Nov 22, by holding an extraordinary session in Oct.
- **Net foreign assets at Bahrain's central bank rebounded in Aug**, rising by 47% mom to BHD 734.2mn (USD 1.95bn).
- **Bahrain EDB disclosed that FDI inflows increased by 138% during Jan-Sep this year**; attracting 76 companies so far this year, investment crossed USD 810mn breaking last year's record of 71 companies with an investment of USD 733mn. Investments are expected to create some 4.2k jobs over the next three years.
- **IMF applauded Egypt on showing "strong signs of recovery"** under the 3-year reform plan; these reforms "will help achieve more sustainable, inclusive and private-sector led growth".
- **Egypt's central bank left interest rates unchanged** at the latest meeting: overnight deposit rate was left at 16.75% and the overnight lending rate at 17.75%.
- **Egypt plans to launch tours in Asia and Europe from this week to market its international bonds**, according to the finance minister. Egypt plans to issue Eurobonds worth about USD 5bn in the coming months.
- **Bilateral trade between Egypt and the US increased by 29.2% yoy** to USD 3.8bn in Jan-Jul 2018. US investments in Egypt are at USD 2.4bn, distributed over 1,222 projects across various sectors.
- **Egypt announced that it will no longer be importing natural gas**: its final liquefied shipments arrived last week. The Ministry of Petroleum estimates that the country would save USD 3bn this fiscal year given the halt in gas imports. Production of natural gas this month reached 6.6bn cubic feet per day, compared with 6bn feet per day in July.
- **Jordan sent its latest draft tax bill to the parliament**: the new law raises personal income thresholds and reintroduces personal exemptions in a bid to soften the impact on the middle class. However, anger is mounting

over the new tax law – one of the points of contention is that the end-of-service benefits will be subject to income tax, an issue labelled by many as unconstitutional.

- The number of **Kuwaiti employees in the public sector** reached 244,162 in the fiscal year 2017-18 and compares to expatriate staff at 44,572.
- The **central bank of Kuwait issued guidelines for all service providers to register in its electronic payment system**, to allow all e-payment transactions to be regulated. Banks will be listed automatically as service providers while other institutions will have to apply for registration.
- The **total bank credit of commercial banks in Oman** at the end of Jun grew 4.1% yoy to OMR 20.94 bn.
- **Foreign Direct Investment (FDI) in Oman surged 16.8% yoy** at end-Q2 to OMR 9.7bn.
- **Qatar** – currently rated AA minus by **S&P** – **is currently at the highest risk of being downgraded** as it continues to feel the impact of the boycott from other Arab states.
- **Qatar's investments in the UK touched USD 50bn**, revealed the Lord Mayor of London.
- **Saudi Arabia's foreign assets increased** by 1.7% mom and 4.4% yoy to SAR 1.91 trn (USD 510bn) in Aug; **foreign reserves grew** by 2.5% yoy in Aug 2018.
- **Inflation in Saudi Arabia remained flat** at 2.2% yoy in Aug; transport costs surged 10.5% yoy, restaurants and hotel inflation touched a record high 8.4%, prices of food and beverage grew 6.6% while housing and utilities costs fell 1.3%.
- **Non-oil trade between Saudi Arabia and UAE** touched AED 720bn (USD 196bn) in H1 2018. UAE imports from Saudi Arabia touched AED 244.2bn during this period while exports amounted to AED 144.8bn.
- **Aramco's CEO** stated to the *FT* that the **IPO has been postponed** till the majority stake acquisition in Sabic

is complete. He also revealed that negotiations are still in “early phases” and that the deal’s value has not been agreed.

- **Saudi Arabia’s Aramco is planning an expansion of crude output capacity**, with some 550k barrels per day expected online from two fields starting Q4, reported *Reuters* citing a source aware of the matter.
- **Remittances from Saudi Arabia** declined by 16.9% yoy and 14% mom to SAR 10.4bn in Aug, bringing the total to SAR 93.7bn in the first eight months of 2018.
- **Saudi Arabia amended the anti-corruption law** to remove a 60-day statute of limitations for investigating allegations against current or former ministers.
- **Saudi Arabia will offer an electronic visa for foreign visitors to attend sporting events and concerts** from Dec. The “Sharek” visa will offer “free mobility within specific Saudi territories” during, before and after an event and will be introduced in time for the Saudia Diriyah E Prix on Dec 15.
- **Saudi Arabia** disclosed, along the sidelines of the UN General Assembly, its support to the Central Bank of **Yemen** and provision of **direct humanitarian assistance** totaling USD 13bn to the country over the past four years.
- **Five GCC members (excluding Oman) will become eligible for inclusion in JPMorgan’s emerging-market bonds indexes from end-Jan**, potentially attracting around USD 30bn in inflows (of which Saudi expects USD 11bn, given its 3.1% weighting). The inclusion will be phased in between Jan 31 and Sep 30, 2019.

## UAE Focus

- **UAE gross bank assets increased** to AED 2.8trn (USD 762bn) by end-Aug, rising 4% from end-2017, according to the central bank. Total deposits grew by 0.5% mom to AED 1.703 trn while claims to the private sector grew to AED

1.123trn in Aug (Dec 2017: AED 1.086trn).

- **UAE raised fuel prices for Oct:** prices for petrol increased by 0.8% mom while diesel costs were up 4.5% mom.
- **Abu Dhabi Industrial Producer Price Index** increased 13.4% yoy and 4.2% qoq to 80.6 in Q2 2018. Prices of the production of coke coal and refined oil products increased by 29% while chemical materials and products grew by 29.2%.
- **Abu Dhabi's trade in aluminium**, which represents around 2.6% of its total non-oil trade, increased to around AED 2.6bn in Jan-Jul this year.
- **Investors can now start business in Dubai from remote locations**, as per a new initiative undertaken by Dubai FDI and US-based Alliance Business Centres Network.
- Nasdaq Dubai's latest listing of Islamic Development Bank's USD 1.3bn Sukuk places **Dubai as the largest centre globally for Sukuk listings by value** (currently USD 60.15bn).
- **Dubai real estate transactions** topped AED 131bn (USD 35bn) in Jan-Aug 2018, via more than 39k investors.
- **Dubai plans to issue a new rent law before end-2018:** the draft law proposes standardizing the relationship between tenants and landlords in Dubai, while providing legal clarity and protecting rights of both tenants and landlords.
- **Dubai was named the 4<sup>th</sup> most visited city** by Mastercard's Global Destination Cities Index (GDCI) 2018. Having received 15.79mn overnight visitors last year, the city also leads the list in terms of the value of international overnight visitor spending, at UD 29.7bn last year.
- **Abu Dhabi disclosed a 10.5% yoy increase in the number of hotel guests** staying in the emirate in Aug to 477.6k. This brings the total to 3.31mn guests during Jan-Aug, up 5.8% yoy. China is still Abu Dhabi's number one

source market.

## **Media Review**

### **The US-China trade war intensifies**

<https://asia.nikkei.com/Economy/Trade-War/US-China-trade-war-intensifies-as-both-sides-impose-new-tariffs>

<https://www.project-syndicate.org/commentary/trump-trade-policy-goals-china-tariffs-by-martin-feldstein-2018-09>

### **Total expects oil prices to reach triple digit**

<http://businessweekme.com/total-sees-100-oil-coming/>

### **The next financial crisis will be a cyber attack**

<https://www.oliverwyman.com/our-expertise/insights/2018/sep/how-a-cyber-attack-could-cause-the-next-financial-crisis.html>

### **Saudi Crown Prince in Kuwait for Qatar talks: Reuters**

<https://www.reuters.com/article/us-saudi-kuwait-qatar/saudi-crown-prince-to-visit-kuwait-for-talks-on-qatar-news-agency-idUSKCN1M816K>

### **A floating electricity plant divides Lebanon (subscription)**

<https://www.economist.com/middle-east-and-africa/2018/09/29/a-floating-electricity-plant-divides-lebanon>

### **Saudi Arabia's Public Investment Fund is launching an uber-luxury project for international tourists**

<https://www.thenational.ae/business/economy/saudi-arabia-court-s-uber-lux-travellers-with-red-sea-project-1.774515>

### **Saudi Arabia's legal revamp offers hope for cautious investors**

<https://www.reuters.com/article/us-saudi-economy-court-analysis/saudi-arabias-legal-revamp-offers-hope-for-cautious-investors-idUSKCN1M7157>

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