

Weekly Economic Commentary – June 2, 2019

Markets

Equity markets in the US suffered the worst May since 2010, with the latest drag on markets being Trump linking tariffs on Mexican goods with immigration and reports of China's potential retaliatory moves including on rare earth mineral exports (*more in Media section*). Markets in Asia remained mixed (tmsnrt.rs/2zpUAR4) while in Europe, most markets closed lower. Government bonds extended their rally: ten-year US Treasury yields are back at levels last seen in Sep 2017 while German government bonds yield fell to the lowest level on record. Markets are now pricing in two interest rate cuts from the Fed this year. In the Middle East, most markets gained except Egypt and Saudi, with the latter remaining volatile given its inclusion in MSCI's emerging market index. The dollar weakened against its peers, yen benefitted from its safe haven status and the Mexican peso tumbled posting its steepest single-day loss since Oct. Oil prices fell (below \$65 a barrel) while gold prices touched a 7-week high.

Global Developments

US/Americas:

- **US GDP was revised lower to a 3.1% annualized rate in Q1 2019**, slightly down from the previously estimated 3.2%, after inventory estimates were trimmed. Excluding trade, inventories and government spending, US expanded at a 1.3% rate (Q4 2018: 2.6%), the slowest since Q2 2013. Separately, Atlanta Fed is forecasting GDP growth at 1.3% in Q2.
- The **personal consumption expenditures (PCE) price index** grew by 0.3% mom and 1.5% yoy in Apr (Mar: +0.2% and +1.4% yoy). Excluding the volatile food and energy components, the PCE index increased at 0.2% mom and 1.6%

yoy rate in Q1, lower than the previous month's readings of a 0.1% mom and 1.5% yoy pace.

- **US consumer spending**, which accounts for more than two-thirds of economic activity, **slowed** to 0.3% in Apr versus an upwardly revised 1.1% in Mar (biggest rise since Aug 2009) as consumers spent less on services, including household electricity and gas. Personal income was up 0.5% in Apr (Mar: 0.1%) while savings were up to USD 990.3bn (Mar: USD 963.7bn).
- **Chicago PMI rose** to 54.2 in May from Apr's reading of 52.6.
- **US trade deficit in goods widened** to USD 72.1bn in Apr: exports fell 4.2% mom and imports dropped by 2.7%.
- **S&P Case Shiller national home price gains continue to weaken**: Mar's 3.7% increase was down from Feb's 3.9%, and was the slowest pace posted in 6.5 years.
- **Initial jobless claims grew** by 3k to a seasonally adjusted 215k for the week ended May 25. The 4-week moving average of initial claims fell by 3750 to 216750 last week.

Europe:

- **The European Commission's sentiment index picked up** to 105.1 in May from 103.9 last month.
- **German preliminary CPI reading dropped** to 1.3% yoy in May, the lowest since Feb 2018 and following the previous month's 2.1%.
- **German unemployment ticked up for the first time since 2013**, with the rate edging up to 5% in May from 4.9% in Apr. The Federal Labour agency noted that roughly two-thirds of the increase in unemployed was due to a statistical reclassification.
- **Retail sales in Germany fell** by -2% mom in Apr, though turnover was up 4% yoy when adjusted for inflation.

Asia Pacific:

- **The official NBS manufacturing PMI in China fell below the 50-mark again:** the May reading at 49.4 was dragged down by new export orders (which dipped to 46.5 from 49.2) and employment index was at the lowest since Mar 2009. **Non-manufacturing PMI remained unchanged** at 54.3 in May.
- **Japan's final leading economic index eased to its lowest level in 3 years,** posting a reading of 95.9 in Mar versus a preliminary reading of 96.3. The final coincident index eased to 99.4 in Mar, compared to Feb's 100.4 and the preliminary figure of 99.6.
- **Japan's industrial production was up** by 0.6% mom in Apr (Mar: -0.6%), supported by an increase in production of cars, airplane parts, and machines used to make flat panel displays. However, inventories of semiconductors and electronic parts rising at the fastest pace in seven months is likely to weigh in on future output.
- **Retail trade in Japan grew** by 0.5% yoy in Apr (Mar: +1.0%).
- **South Korea's industrial output was up** by 0.7% mom in Apr (Mar: +1.5%), thanks to a 6.5% rise in semiconductor output, a 11.2% pick up for oil refiners, and a 1.6% expansion in mining and manufacturing industries.

Bottom line: Last week of May, as the "cold war" with China continued, came a few more trade "actions" from the US – India will be stripped of its preferential market access to the US from Jun 5th, and Trump plans to link a 5% tariff on Mexican goods to illegal immigration. With the latest weak PMI data from China, expectations of policy support remain strong: it is estimated that the People's Bank of China injected CNY 430bn (USD 62bn) last week via reverse bond repurchase agreements. The ECB's Jun 6 meeting – being held in the backdrop of global trade wars, weak PMIs, weak Germany, and "Brexit?" under a new PM – is likely disclose details for the upcoming TLTRO loans and maintain a dovish stance. Expect frayed nerves at the G20 meeting in Japan this month.

Regional Developments

- **Bahrain's parliament passed the 2019-20 budget into law:** the budget deficit this year is estimated to decline to 4.7% of GDP vs 2018's 6.2% (was projected to be 9.8%). The budget is based on projected oil price of USD 60, and state spending is still expected to account for 24% of GDP in 2019 and 23.1% in 2020.
- **Bahrain MP's budget for foreign trips have been reduced** by 30% as part of an austerity drive: they are no longer permitted to travel first-class and plans are underway to minimize unnecessary attendance by MPs and senior officials.
- **Moody's revised the outlook for the Bahraini banking system to stable** from negative on expectations of a 2.1% GDP growth this year and the USD 10bn support package from its GCC peers.
- **Bahrain exports increased** by 16% yoy to BHD 204mn in Apr, with the top 10 nations accounting for 82% of exported value. Imports declined 12% to BHD 448mn, with China, Bahrain and the UAE top import partners.
- **Remittances from Egypt rose** by 27.8% mom to USD 2.3bn in Mar, according to the central bank. **Money supply in Egypt slowed** to 11.33% yoy to EGP 3.76trn as of end Apr (Mar: 11.39%).
- The **Central bank of Egypt** will now allow banks to include their equity investments in funds focused on SMEs within the minimum requirement of their SME loan portfolios (at 20% of their total loan portfolios).
- **Egypt's property tax revenue expanded** by 60.8% yoy to EGP 3.7bn during Jul 2018-Mar 2019, with bulk of the revenue coming from tax on buildings (EGP 3.63bn) and the rest from tax on land. Egypt's total revenue reached EGP 598.68mn in this period.
- **Bilateral trade between Egypt and China** grew by 7.6% yoy to USD 4.188bn in Jan-Apr 2019, with Chinese exports to the country rising 13.2% to USD 3.73bn during the

period.

- **Egypt is planning to combine stamp duty and capital gains taxes on equity investments**, according to the chairman of the stock exchange. Under this proposed change, the government could refund some stamp duty if the amount exceeded capital gains charges payable at the end of the year.
- **Saudi Arabia's investments into Egypt surged** by 44% yoy to USD 125.5mn in Q2 2018-19, according to the Central Agency for Public Mobilization and Statistics.
- **Iraq's oil exports from the southern ports increased** to 3.454mn barrels per day (bpd) in May, according to *Reuters* This compares to previous exports of 3.354mn bpd (in Apr) and 3.254mn bpd (Mar).
- **The Jordan Renewable Energy and Energy Efficiency Fund has implemented JOD 50mn worth of renewable energy projects over the past four years.** This also includes the installation of 22k solar heating units in houses across Jordan, providing heating systems for schools and replacing traditional light bulbs with energy-saving LED ones.
- **Kuwait's sovereign wealth fund (SWF)**, with assets at USD 592bn, is **ranked 4th among global SWFs** and 2nd in the region after Abu Dhabi (USD 696.66bn).
- **Inflation in Kuwait** touched 0.8% yoy in Q1 this year, versus 0.4% recorded in Q4 last year.
- **Lebanon's 2019 budget** – that cuts public spending and reduces the deficit-to-GDP ratio to 7.59% from 11.5% last year – **has been given Cabinet approval.** This resulted in a drop in CDS spreads and dollar bond gains. Ratings agencies like Fitch and S&P Global applauded the move but questioned whether this was sufficient to restore investor confidence and keep default concerns at bay.

(More:

<https://www.reuters.com/article/us-lebanon-economy-budget-analysis/lebanon-budget-seen-a-good-first-step-but->

[numbers-questioned-idUSKCN1SY1YJ](#))

- **Oman's Shura Council approved the New Foreign Capital Investment Law:** it removes the need for Omani partners for foreign investors and also removes minimum and maximum investment levels for companies in certain sectors. Next, it needs to be approved/amended by the State Council (within 15 days) before the Law is sent for final approval to the King.
- **Oman will implement a new selective tax** on tobacco, pork meat, energy drinks and soft drinks **starting 15 Jun:** the imposed tax on soft drinks will be 50% and on the rest 100%.
- **More than 27k Omani citizens have been recruited in the private sector this year;** construction, sale, distribution and industry account for 58% of the recruitment.
- **Qatar's PM travelled to Saudi Arabia to attend the emergency Arab summit last week,** the highest level of Qatari official to visit the country during the ongoing diplomatic rift.
- **SAMA's assets increased** by more than SAR 26bn to SAR 1.919trn (USD 491.7bn) in Apr, from the month before. In yoy terms, assets declined by SAR 16.541bn.
- **Tadawul cut the par value of 29 domestic government debt instruments** issued by the Saudi government to SAR 1,000 from SAR 1mn, **effective 9 June.**
- **The volume of residential new mortgage finance for individuals jumped by three times** in Apr: residential financing contracts reached 45,860 contracts worth SAR 31,528bn as of Apr. This compares to 50,496 contracts worth SAR 29.5bn in 2018.
- **Saudi Arabia's trade surplus widened** by 80.16% yoy to SAR 589.9bn by end-2018, with exports rising by 32.69% to SAR 1.104trn. Oil exports grew 36% to SAR 868.442bn while non-oil exports expanded by 21.7% to SAR 235.458bn. **Non-oil trade balance with the GCC moved into a SAR 9.55bn deficit last year,** compared to a surplus

SAR 4.59bn the year before.

- **Saudi Arabia dominated the MENA region's IPO market in Q1** this year, according to EY, raising USD 58.3mn in capital from one listing.
- **Remittances from Saudi Arabia declined** by 8.5% yoy and 23% mom to SAR 10.723bn in Apr. In Q1, remittances were down 11.3% yoy to SAR 31.93bn.

UAE Focus

- **UAE's central bank has revised downwards economic growth forecasts for this year** to 2% from the previously estimated 3.5%. Non-oil growth is estimated at 1.8% (3.4% previous estimate) and growth in the oil sector will fall to 2.7% on lower oil production.
- **UAE approved the distribution of VAT revenues:** the approximately AED 27bn collected will be distributed as 30% to the federal government and 70% to the local governments.
- **UAE non-oil foreign trade increased** to AED 1.628trn (USD 440bn) in 2018, with direct non-oil foreign trade accounting for 63% of the value. Bilateral non-oil trade between the UAE and Arab states grew by 21% last year (2017: 19%) while their re-exports totalled AED 170.1bn.
- In the latest move to reduce costs of doing business, the **UAE decided to amend and waive fees for more than 1,500 government services** provided by the Ministry of Interior, Ministry of Economy, and the Ministry of Human Resources and Emiratisation. No further details of the fees were provided.
- **UAE fuel prices increase further in Jun:** depending on the grade of petrol, prices were increased by 2.0-3.4% mom, while diesel price was up 1.18% mom to AED 2.56 per litre.
- **Abu Dhabi's manufacturing sector expanded by 6.02% yoy last year**, creating an added value of AED 49.3bn (USD 13.4bn) to non-oil GDP.

- The Dubai DED disclosed that **over 18,975 Chinese investors own 5,977 active business licenses in the emirate of Dubai.**
- **Hotel revenues in Abu Dhabi increased** by 16.1% yoy to AED 1.7bn (USD 460mn) in Q1, with hotel rooms rising by 5.1% to 33,074 and occupancy rates touching 79%.
- **Dubai Customs** disclosed that the emirate **imported foodstuffs** worth AED 8.3bn (USD 2.26bn) to meet demand ahead of **Ramadan.**
- **Real estate transactions in Sharjah** touched AED 5.2bn (USD 1.42bn) in Q1 this year from a recorded 13,195 transactions.
- **Grants provided by the UAE** (both locally and overseas) **grew** by 14.7% yoy to AED 19.8bn (USD 5.39bn) in 2018, according to the central bank.

Media Review

How Central bank Independence Dies

<https://www.project-syndicate.org/onpoint/how-central-bank-independence-dies-by-kenneth-rogoff-2019-05>

China's rare earth plan for when the trade war deepens

<https://www.bloomberg.com/news/articles/2019-05-31/china-has-a-rare-earths-plan-ready-to-go-if-trade-war-deepens>

<https://www.theguardian.com/business/2019/may/29/us-china-trade-what-are-rare-earth-metals-and-whats-the-dispute>

UK: no-deal or a 2nd referendum?

<https://www.economist.com/britain/2019/05/30/britons-are-ever-more-polarised-between-no-deal-and-a-second-referendum>

The Takeover of China's Baoshang Bank

<https://www.reuters.com/article/us-china-banks/takeover-of-little-known-baoshang-casts-doubt-over-other-small-chinese-banks-idUSKCN1T011G>

Companies in Middle East on war footing as tension rises

<https://www.ft.com/content/0efb548a-8399-11e9-b592-5fe435b57a3b>

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