

Weekly Economic Commentary, 25 Oct 2015

Markets

Wall Street had a positive week which took the S&P500 within striking distance from the 2100 level touched in August before the global stock market rout triggered by the Chinese bubble burst. Once again the take off was due to the prospect of further monetary flooding, this time from the ECB. Regional markets were mostly down: there was little to cheer about in the IMF's forecasts on regional growth while in Egypt, low voter turnout cast a shadow on the long-awaited parliamentary elections. In currency markets the euro was the main loser after Draghi's press conference, while the yen was largely stable against the greenback. Oil prices tumbled after US oil inventories data showed an unexpected accumulation. The announcement of the interest rate cut in China provoked only a short-lived rally. Gold prices, despite the prospect of further monetary easing, continued to slide.

Global Developments

US/Americas:

- **US housing starts** showed steady growth in residential construction, increasing by 6.5% mom (17.5% yoy) in Sep to a 1.21mn annualized rate - and the second highest level in eight years. However, this growth is expected to slow in correlation to the decline in permits that decreased by 5% mom.
- **US existing home sales** recorded a material jump in Sep, growing 4.7% mom (8.8% yoy), reversing losses from the prior month, while maintaining healthy growth on a yearly basis.
- **NAHB Housing Market Index** rose by 3 pts reaching 64 in Oct, up from a revised figure of 61 the previous month. Builder confidence recorded its highest level in the past decade.
- **US monthly purchase-only house price index** gained 0.3% mom in Aug, slower than Jul's revised growth of 0.5%. The gain translated into 5.5% yoy fell below market expectations.
- **St. Louis Fed Stress Index** decreased to -0.78, 10% lower than the previous week. The release of more soft economic data eased financial market stress, with growing investors' confidence that the Federal Reserve will hold off on raising up interest rates.
- **US Risk of Recession Probability** in the coming six months, as calculated by Moody's, increased from 15% to 17% in Sep, indicating tightening financial market conditions.
- **US initial unemployment claims** increased 4,000 in the week ended 17 Oct, reaching 259,000 from 255,000 previously.

Europe:

- The **ECB President Draghi** in the press conference asserted that the central bank stands ready to "adjust the design" of the QE and further lower the deposit rates, which is already in negative territory.

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- **Euro zone's credit conditions** persisted, with tighter credit according to the net percentage of banks reporting a drop to -4% in the three months to Sep, down from -3% in the previous quarter.
- **The euro zone's current account surplus** dropped to EUR 13.7bn in Aug, down from EUR 17.4bn a year earlier. Surplus on the goods and income account squeezed, on the other hand the current transfers' deficit rose, as a comparison with Jul's current account surplus of EUR 37.9bn this year.
- **German producer prices** declined 2.1% yoy in Sept, after a 1.7% fall in Aug. Weak demand and low oil prices have been weighing on producer inflation. While, a weaker euro should drive import prices up.
- **The UK retail sales index** rose 3.7% yoy in Aug, down by only 0.4% from a 4.1% increase in Jul. Moody's Analytics forecast a 4.2% yoy gain.

Asia and Pacific:

- **China's central bank** to provide a new stimulus to the economy cut the one year lending rate, as well as the headline deposit and lending rates by 25bp to 4.35% and the banks' reserve ratio by 0.5% for qualifying banks and 25bps for the others, while removing the ceiling on deposit rates. This year, the cumulated cuts in interest rate totaled 165bps.
- **China's GDP** grew 6.9% yoy in Q3, down from a 7% expansion in Q2, on increased downward pressure on exports. This is the slowest pace since the first quarter of 2009.
- **Chinese industrial production** grew 5.7% yoy in Sep, weaker than Aug's 6.1% gain. **Fixed-asset investment** decelerated growing by 10.3% yoy in Sep, down from a 10.9% yoy in Aug.
- **Chinese retail trade** rose 10.9% yoy in Sep from Aug's 10.8%, driven by low inflation and oil prices.
- **Korea's GDP** expanded 1.2% qoq in Q3, at the fastest pace since Q2 2010, up from the 0.3% qoq gain in Q2. Gross fixed capital formation rose 2.9% qoq, driven by a rise in construction activity, while private consumption and government spending were up 1.1% and 1.9% on quarter respectively.
- **Taiwan's industrial production** fell -5.3% yoy in Sep, up from a -5.7% yoy decline in Aug.

Bottom line: *Against the backdrop of slowing global growth, two major central banks, the People's Bank and the ECB, have once again deployed their tools to prop up their sagging economies. The PBoC has acted decisively, while the ECB has just announced a possible step up in the QE and additional easing on rates. But there is a striking difference between China and the ECB. In the former the government is also engaged in a spate of structural reforms in finance, banking and state owned enterprises, which more or less gradually will modernize the economy. In the euro area, apart from the banking union, which is proceeding at glacial pace, there is scant evidence of any political willingness to enact reforms to free markets, cut red tape and reduce wasteful public spending. Meanwhile an emerging-market debt crisis is looming. The IMF reckons that emerging market liabilities are now twice the size of their equity, a doubling compared to four years ago. If the Fed raises its interest rate, emerging*

market companies are at risk of insolvency. In the meantime, the slowdown exposes poor governance and erratic policymaking, compounded by currency depreciation and downward pressure on living standards.

Regional Developments

- The **IMF**, in its recently released **Regional Economic Outlook** for the MENAP region, projects GCC growth to slow to 3.25% this year and further to 2.75% next year from 3.25% in 2014. Non-oil growth is estimated to be just under 4% both this and next year. While lauding the UAE's move to deregulate oil prices, the IMF underscored the need for fiscal consolidation, with adjustments on both revenue and spending plans. The report also forecasts GCC unemployment rate to increase from 12% to 16% by 2020, with almost 5mn job market entrants estimated to be unemployed by 2020.
- **Egypt** is planning to **delay** the issuance of its second tranche of international **bond**, expected in Nov, citing market turbulence and China's economic slowdown. The finance minister further stated that "we will choose the right time to enter (the market)".
- About 26.3% of **Egypt's** population lies beneath **poverty line** for the year 2012/13 compared with 25.2% in 2010/11, according to official statistics. The domestic poverty line is at a monthly average of EGP 214 per person.
- **Iraq's budget deficit** is estimated at IQD 23.5 trn, or 11.9% of GDP in 2016, revealed the finance minister. More than 70% of total expenditure plugged at IQD 106.9 trn is set aside for salaries and payments to the public sector officials while oil is expected to account for more than 80% of fiscal revenues in 2016.
- It was disclosed by a member of the Parliamentary Commission on oil and energy that **Iraq** was "obliged to pay" USD 8-9bn as **dues to oil companies** for last year and this year.
- The **IMF** may provide a **new loan to Iraq** in 2016, further to building a track record on policy implementation, which is likely to recommend steps to reduce energy price subsidies and reform state-owned enterprises.
- **Jordan** reported an **unemployment rate** of 13.8% in Q3 this year, with jobless rate among men at 11.1% and 25.1% among women.
- The **consumer sector** in **Kuwait** remains robust, according to an NBK report: household debt growth remained in the double-digits posting 12.5% yoy growth in July, while personal facilities excluding credit for the purchase of securities rose to KWD 10.2bn.
- **Lebanon**, with 294.2 borrowers per 1,000 adults at commercial banks in 2014, reported the 26th highest **loan penetration rate** in the world, according to the IMF.
- **Oman's budget deficit** widened to OMR 2.68bn in the period Jan-Aug 2015, with oil revenues declining by nearly 46%, already surpassing the government's 2015 budget estimate for a shortfall of OMR 2.5bn. The first eight months of 2014 had seen a surplus of OMR 205.7mn.
- **Oman's total exports** declined by 32.61% yoy to OMR 6.81bn in H1 this year, from OMR 10.11bn recorded for the same period last year.

- Total assets of **Oman's** conventional **commercial banks** increased by 14.7% yoy to OMR 27.9bn in Aug this year. Of the total, credit disbursement accounted for 46.6%, rising by 10.6 % to OMR 18bn at end-Aug.
- **Qatar's** PM stated that the country's **non-hydrocarbon sector** is expected to grow by 10% in 2016; he also revealed that the volume of non-petroleum exports reached QAR 1.5bn as of Jul 2015.
- **Cost of living** in **Qatar** grew 1.5% yoy in Sep, on higher education costs, rents and tobacco prices.
- About 2.25 million **visitors** came into **Qatar** during the first nine months of the year, up 8% yoy, as per the Tourism Authority. The office expects total tourists to reach 3mn by end of this year.
- **Russia exports of crude oil to China** last surpassed Saudi Arabia in Sep - previous instance of this was in May this year. Chinese customs data showed the country bought 4.042 million tonnes of crude oil from Russia last month, or about 983,590 barrels per day (bpd), up 42% from a year earlier; imports from Saudi Arabia were at 961,710 bpd.
- **Saudi Arabia** needs "a sizeable, structured, multi-year fiscal adjustment", according to the IMF, and also stating that the Saudi authorities were "evaluating all areas".
- **Saudi Arabia's** CMA chairman, in an interview with Reuters, revealed that the country would be open to **relaxing its rules on foreigners investing directly** in its stock market to help it get included in global indices.
- **Saudi Arabia** is delaying **payments to government contractors**, in addition to seeking to renegotiate prices on contracts, as the oil price slump continues, Bloomberg reported last week.
- According to Reuters, **M&A deals with Middle Eastern** involvement grew 23% yoy to USD 33.7bn in Jan-Sep 2015, also the best annual start since 2010. **Investment banking fees** were down 22% yoy to USD 480.5mn during Jan-Sep 2015, the lowest first nine month total since 2012.
- **Trade** between the **GCC and Japan** declined 41.7% yoy to USD 50.36bn during H1 2015, partly due to the declining oil prices and partly to the slide in value of yen vis-a-vis the dollar.

UAE Focus

- The **IMF** predicts UAE's real GDP growth to dip to 3% in 2015, before edging up slightly to 3.1% in 2016, and from 4.6% in 2014. UAE's fiscal consolidation measures in addition to its relatively more diversified economy will help the country move from deficits into the fiscal surplus zone within two years.
- The **Abu Dhabi Global Market**, the UAE capital's financial free zone, has declared itself "open for business", following the publication of ADGM's rules and regulations, and is expected to start accepting applications from potential member firms.

- **Inflation** in the **UAE** eased to 4.3% yoy in Sep (Aug: 4.9%), on lower transportation and oil prices, though housing and utility costs grew 8.3% yoy. **Dubai inflation** was up 4.28% yoy in Jan-Sep 2015, with household items price up 8% and housing, utility costs reporting a 7.25% rise.
- **Abu Dhabi's non-oil sector** accounted for 50.2% of GDP in 2014, with real estate activity accounting for the largest share at 20.7% of gross fixed capital formation.
- The number of **millionaires** in **UAE**, currently at 59k, is expected to surge to 96k by 2020, as per forecasts in the sixth annual Global Wealth Report from The Credit Suisse Research Institute. In Saudi Arabia this number is expected to rise 72% to 86k by 2020.
- The **UAE Information Technology** market, estimated at close to AED 17bn, is likely to rise to AED 22bn by 2019, and per capita spending is expected to reach above AED 2k by 2018, according to a Dubai Chamber of Commerce study.
- **UAE** is India's second top destination for export of **electronics goods**, with the country exporting electronics goods worth USD 440mn to UAE in 2014-15.
- Cash is king in the **UAE**, accounting for more than 75% of all transactions in the country. Annually, the UAE spends about USD 230bn in consumer payments to 170 government entities and more than 350k merchants. This picture could change by 2020, with greater use of digital wallets, mobile point-of-sale to electronic payments and other such means, according to a **digital payments** service company, Triple.

Media Review

The Saudis are about to crush the US oil boom

<http://www.bloomberg.com/news/articles/2015-10-20/after-year-of-pain-opec-close-to-halting-u-s-oil-in-its-tracks?>

The write downs in the US energy sector are piling up

<http://www.bloomberg.com/news/articles/2015-10-23/-6-5-billion-in-energy-writedowns-and-we-re-just-getting-started>

China's Economy at the Fifth Plenum

<http://www.project-syndicate.org/commentary/china-fifth-plenum-economic-reform-by-andrew-sheng-and-xiao-geng-2015-10>

Gulf bond market power shift

http://www.zawya.com/story/Sukuk_issues_show_Gulf_bond_market_power_shift-TR20151020nL8N12K2MXX2/