

Weekly Economic Commentary, 6 Mar 2016

Markets

Global stock markets recorded the third consecutive week of gains hitting fresh two-month highs on receding fear of recession, expectations of monetary stimulus in Europe and China and better macro data. Even US Treasury yields are firmer, as risk aversion ebbs. Regional stock markets followed the global trend and benefitted from the rebound in the oil market. In the currency space the GBP regained some ground while major crosses were relatively stable. Gold is on an upward trajectory, driven by the conviction that central bank actions will sap the value of fiat money.

Global Developments

US/Americas:

- **Non-farm payroll employment** increased by 242k in Feb from 172k in Jan, confirming that the labour market remains resilient despite global financial turbulence and a cloudier outlook.
- **US unemployment claims** rose 6,000 to 278,000; however the **4-week moving average** dropped from 272,000 to 270,250 near the midpoint of the range seen since Q2 2015.
- **The ISM manufacturing index** rose from 48.2 in Jan to 49.5 in Feb, reporting the 5th consecutive monthly appreciation. However, it remains below in contractionary territory. **The ISM non-manufacturing Index** decreased a marginal 0.1 points to 53.4 in Feb.
- **The Fed's Beige Book** reported that US economic activity continued to expand in most districts from early Jan to late Feb but at different pace across regions and within sectors. Consumption increased in most districts, manufacturing activity was flat, labor market improved, wage growth "varied considerably".
- **Non-farm business output per hour** fell -2.2% qoq in Q4 2015, a minor improvement from Q3's decline while growth in the **hours worked index** cooled from 3.3% to 3.2%. **Compensation per hour** increased 1.1% in Q4, implying an increase in unit **labour costs** of 3.3%.
- **US new orders for manufactured goods** rose 1.6% mom in Jan, the first increase in 3 months. Durable goods orders gained 4.7%, the largest increase in about a year, whereas core capital goods orders rose 3.4%. Excluding defense, new orders were up 1.3%.
- **The Black Knight Home Price Index** expanded 0.1% mom and 5.5% yoy in Dec, unchanged from Nov.
- **The pending home sales index** dropped 2.5% to 106 in Jan from 106.8, its lowest level since Jan 2015.
- **Brazil's GDP** shrank -3.8% in 2015 as investment plunged and more than 1.5mn workers were laid off. It was the worst performance of any G20 nation in 2015.

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Europe:

- The **Eurozone M3 money supply** accelerated to 5% yoy sa in Jan from 4.7% yoy in Dec.
- The **Eurozone inflation** dropped to -0.2% yoy in Feb from -0.4% yoy in Jan as a result of lower commodity prices.
- The **Eurozone unemployment rate** fell to 10.3% in Jan, down from 10.4% in Dec.
- **Eurozone's PPI** fell -2.9% yoy in Jan, almost similar to the -3.0% recorded in Dec.
- The **UK Nationwide Housing Price Index** was up 0.3% mom in Feb, the same rate as in Jan.
- The **UK Halifax Housing Price Index** fell -1.4% mom in Feb, following a 1.7% mom increase in Jan.
- **German retail sales** rose 0.7% mom in Jan after gaining 0.6% mom in Dec.
- **Bank loans to German nonfinancial corporations** increased 1.5% yoy (0.7%) mom. Loans to households decreased -0.1% mom but rose 2.7% yoy.

Asia and Pacific:

- The **Chinese Central Bank cut the reserve ratio** by 0.5% to 17% to prop up the economy and injected USD 100 bn of cash.
- The new **Chinese 5-year plan** aims to achieve growth between 6.5% and 7.0%, fight unemployment and restructure inefficient industries. However it could prove illusory as the plans eschew the hard political choices that would boost growth and downplays the challenges ahead.
- **Japan's Industrial Production** expanded 3.7% mom in Jan, reversing the -1.7% decline from Dec. Electronics and machinery were major drivers, however production is still hindered by the Yen appreciation.
- **Japan's Retail Sales** fell -0.1% yoy, up from a -1.1% decline in Dec. Japanese consumers remain unwilling to spend considering declining real wages and volatile financial markets.
- **Japan's Housing Starts** increased 0.2% yoy in Jan, up from -1.3% drop in Dec. Despite the unexpected positive news, the housing sector remains lackluster.
- **Australia's GDP growth** decelerated to 0.6% qoq in Q4 2015 from 0.9% in Q3.
- Moody's changed **the outlook on China's credit rating** from stable to negative, citing a weakening of fiscal stance and a drop in FX reserves, however stressing that the sheer amount of such reserves gave enough time to enact reforms and address economic woes.
- **South Korea's inflation increased** to 1.3% yoy in Feb from Jan's 0.8%. Despite the drop in consumer sentiment, prices are stabilizing.
- **South Korean exports** declined for the fourteenth consecutive month, the longest sequence in recent history. Exports contracted 12.2% yoy in Feb following Jan's 18.8% drop.
- **South Korea's Industrial Production** fell -1.9% yoy in Jan, slightly better than -2.2% in Dec. Competition in China and Japan and weak global demand continue to thwart activity.
- **South Korea's Retail Sales** dropped -1.4% mom in Jan, much worse than the -0.1% in Dec.

Bottom line: The most important conjunctural indicator, the US non-farm payroll, has proved resilient to the weakness recorded at the turn of the year, thereby injecting a much

needed dose of optimism in an otherwise mixed picture. However, while economic forecasts are based on linear models, financial markets at critical junctures, where shifts occur, follow non-linear dynamics. This explains why a relatively minor improvement might have large repercussions on financial assets' and commodities' prices. In essence the situation on global markets will remain precarious, until the global recovery regains traction and as long as the policy responses are heavily skewed towards monetary gimmicks.

Regional Developments

- **Moody's** placed **Saudi Arabia's** Aa3 rating **on review for a possible downgrade** as well as the UAE, Kuwait and Qatar. It cut Bahrain's rating by one notch to Ba1, below investment grade and kept the rating on review for a further downgrade.
- **Egypt's** net **foreign reserves** grew slightly to USD 16.53bn in Feb (Jan: USD 16.48bn). Separately, M2 **money supply** was up 17.4% yoy to EGP 1.912 trn in end-Jan.
- **Tourism revenue** in **Egypt** declined by around USD 1.2-1.3bn after the plane crash last Oct, according to the Prime Minister.
- **Egypt** cancelled last Monday the planned **5-year Treasury bond issue**, the first cancellation of any Treasury sale since Aug 2014. The average yield on the 10-year bond jumped more than 21 basis points to 15.999% on Monday from 15.788% in the previous auction on Feb. 15, as per the finance ministry.
- **Egypt's Suez Canal revenues** fell in Jan to USD 411.8mn from USD 429mn in Dec.
- **Fitch** revised the outlook on **Iraq's** long-term foreign currency Issuer Default Rating to negative from stable. Lower oil prices and subsequent fiscal and current account deficits amidst higher government debt were the main drivers behind this revision.
- **Iraq's** oil ministry disclosed that **oil exports** from the country's **southern region** had dropped slightly to an average of 3.225mn barrels per day in Feb (Jan: 3.285mn bpd). Oil revenue stood at USD 2.2bn in Feb, with 93.54mn barrels sold at an average price of \$23 per barrel, up slightly from \$22.21 the month before.
- **Kuwait's crude oil exports to Japan** grew 4.4% yoy to 8.26 million barrels in Jan, or 266k barrels per day. Kuwait accounted for 7.8% of Japan's total crude imports.
- The IIF called for **Lebanon** to implement **fiscal reforms** to reduce debt: it estimates that an increase in the excise tax on gasoline from 20 cents to 35 cents per liter, would generate at least USD 320mn, or 0.7% of GDP, in additional revenues. However, any narrowing of the fiscal debt is based on a scenario whereby regional tensions ease and a President is elected in H1 this year, among others, like raising excise tax on gasoline.
- **Qatar's trade surplus** reduced by 58% yoy and 17.8% mom to QAR 7.25bn in Jan: exports slipped 33.6% yoy to QAR 17.94% on decline in shipments while imports expanded (especially from the US, Germany, China and Switzerland) 10.1% yoy to QAR 10.69bn.

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- **Qatar bank credit to the real estate sector** grew 27.36% yoy to QAR 125bn last year, according to the central bank. Banks' total domestic credit rose to QAR 660bn in 2015, up from QAR 586bn reported in 2014.
- **Bilateral trade** between **Qatar** and **Italy** touched USD 3bn last year, accounting for 2.8% of Qatar's foreign trade, as per the Minister of Economy and Commerce.
- **Water consumption per capita** estimates in **Qatar** provides a striking contrast: an expatriate consumed an average of 76.8 cubic metres of water in 2014, while the figure for nationals was around 7 times higher at 569.7 cubic metres.
- **Net foreign assets** at **Saudi Arabia's** central bank dropped 2.4% mom and 18.2% yoy to SAR 2.23 trillion riyals in Jan - the lowest level since 2012.
- **Growth** in **Saudi Arabia** is expected at around 2% this year, according to a central bank official; this is higher than IMF which forecast only 1.2% growth in 2016.
- **Saudi Arabia's** central bank plans to launch an “**affordable mortgage**” programme: while details of its size nor eligibility was provided, it was disclosed that Saudi home buyers would make an advance payment of 15% of the property's value, with commercial banks supplying a further 70%, as well as an additional 15% that would be guaranteed by the Ministry of Finance.
- *Reuters* reported last week that **Saudi Arabia's** government has asked banks to discuss providing it with a major **international loan** that could total around USD 10bn.
- According to **Saudi Arabia's** Ministry of Labour, as reported in *Makkah* newspaper, there are some 65,000 expats working in the public sector. The Ministry of Civil Service reported it had Saudized 5,627 positions in the past five years, while 3,367 Saudi women replaced non-Saudi women in public sector jobs.
- **Deposit growth** in **Saudi Arabia's** banks slipped to 1% last year, from 12% in 2014, as per a report from **Moody's**. The report expects banks' muted deposit growth to moderate lending growth, with overall loan growth in 2016 falling to 5%, the lowest since 2010, from 8% in 2015.
- **Saudi Arabia's** aviation regulator is in talks with government agencies to set up **free zones** at Jeddah and Riyadh airports, revealed its chairman.
- **Sovereign wealth fund withdrawals** of USD 46.4bn of assets in 2015 were concentrated in equities, and from the most liquid segments of their investments, according to research firm eVestment. Over USD 17bn was withdrawn from global equity mandates, USD 10.5bn from US equity funds and USD 3.5bn from emerging market equities. Inflows were seen in core US fixed income and US short duration fixed income, which attracted USD 2.7bn and USD 3.3bn respectively.
- According to a Reuters survey, **supply from the OPEC** declined in Feb to 32.37mn barrels per day (bpd) from a revised 32.65mn bpd in Jan; the biggest drop was from Iraq due to a stoppage in flow from a pipeline that is expected to be shut till mid-Mar.
- Qatar, Kuwait and Abu Dhabi have significantly larger **fiscal buffers relative to expected funding needs** than the other three Gulf countries, stated **S&P** last week in a research note.

- **Business tourists** in the GCC comprise of one in three of all tourists in the region, as per a Strategy & study. Dubai alone accounted for nearly 27% of the USD 1.3bn MICE (meetings, incentives, conferences, and events) GCC market.

UAE Focus

- The non-oil sector in UAE rebounded in Feb, with the **PMI** rising to 53 from 52.7 in Jan, supported by an uptick in new export orders and employment.
- **Dubai property** market recorded **deals** worth AED 68bn in the first 53 days of the year, according to the Dubai Land Department.
- A new free zone launched last week, named **Dubai Wholesale City**, is expected to boost UAE's share in global trade and will be implemented by Dubai Holding. The 550 million square feet development, at AED30bn, is anticipated to attract close to 15k wholesale traders.
- **Abu Dhabi inflation** stood at 3.2%yoy in Jan, and down 0.6% mom. The new series reflects a change in base year to 2014 from 2007 earlier and reduced the weighting of housing and utilities in the consumer basket to 31.2% from 37.9%.
- UAE reduced **petrol prices** for this month to AED 1.36 from AED 1.47. The price of diesel however went up to AED 1.4 from AED 1.37.
- **Dubai** was labelled the **fifth most important hub for wealthy individuals** with USD 30mn or more in assets, according to a Knight Frank report.

Media Review

China's 5-year plan

<http://www.firstpost.com/fwire/china-sets-economic-growth-target-at-or-above-6-5-percent-in-five-year-plan-reuters-2658102.html>

Oman credit rating downgrade

<http://www.globalfinancialconferences.com/news/article/451/omans-credit-rating-downgraded-by-moodys>

Saudi Arabia's diversification ambitions

<https://next.ft.com/content/11706390-dc80-11e5-a72f-1e7744c66818>

How long will it take to run down the massive oil inventories?

<http://www.bloomberg.com/news/articles/2016-03-02/saudi-arabia-faces-a-new-oil-titan-once-battle-with-shale-is-won-ila2vccq?>

Oil Production and marginal production cost by country

<http://knoema.com/vyronoe/cost-of-oil-production-by-country>

Kuwait's electricity tariff hike proposal

http://www.zawya.com/story/Kuwait_plans_to_hike_electricity_charges-ZAWYA20160304050612/

Saudi PPP plan needs reforms: Jeddah Economic Forum

http://www.zawya.com/story/Saudi_publicprivate_partnership_needs_reforms-ZAWYA20160303035055/

Saudi Arabia wants to avoid projects' delays

http://www.zawya.com/story/S_Arabia_Innovative_approach_vital_to_avoid_project_delays-ZAWYA20160304034931/