

Chair Yellen and US data more dovish; GCC equities up on earnings; Qatar signs MoU with US

Key market indicators

Stock markets	Index	Change (%)	
		weekly	YTD
Regional			
Abu Dhabi SM	4,518	2.77	-0.62
Bahrain ASI	1,317	0.50	7.94
Dubai FM	3,537	4.01	0.19
Egypt EGX 30	13,823	3.39	11.97
S&P GCC 40	1,073	3.75	-7.09
Kuwait SE	6,788	1.62	18.10
KSA Tadawul	7,313	1.52	1.43
Muscat SM 30	5,121	0.04	-11.44
Qatar Exchange	9,470	6.13	-9.26
International			
CSI 300	3,703	1.29	11.88
DAX	12,632	1.96	10.02
DJIA	21,638	1.04	9.49
Eurostoxx 50	3,526	1.79	7.15
FTSE 100	7,378	0.37	3.30
Nikkei 225	20,119	0.95	5.26
S&P 500	2,459	1.41	9.85
Commodities			
	\$/unit	Change (%)	
		weekly	YTD
Brent crude	48.9	4.71	-13.92
KEC	45.4	2.74	-13.20
WTI	46.5	5.22	-13.37
Gold	1226.6	1.49	6.66
Exchange rates			
	Rate	Change (%)	
		weekly	YTD
KWD per USD	0.303	-0.01	-0.89
KWD per EUR	0.345	0.44	8.52
USD per EUR	1.147	0.59	9.07
JPY per USD	112.500	-1.21	-3.74
GBP per USD	1.310	1.60	6.15
EGP per USD	17.930	0.45	-0.39
Interbank rates			
	%	Change (bps)	
		weekly	YTD
Bhbor - 3 month	2.38	-2.5	27.5
Kibor - 3 month	1.75	0.0	31.3
Qibor - 3 month	2.48	2.8	69.7
Eibor - 3 month	1.55	0.1	7.2
Saibor - 3 month	1.80	1.4	-23.8
Libor - 3 month	1.30	-0.1	30.6
Bond yields			
	%	Change (bps)	
		weekly	YTD
Regional			
Abu Dhabi 2021	2.36	-3.9	-17.3
Dubai 2021	2.96	-6.3	-34.2
Qatar 2021	2.95	-45.9	1.7
Kuwait 2022	2.64	-7.9	n/a
Saudi Arabia 2022	2.96	-6.9	n/a
International			
UST 10 Year	2.32	-7.4	-11.3
Bunds 10 Year	0.60	2.6	38.8
Gilts 10 Year	1.31	0.0	6.9
JGB 10 Year	0.08	-1.3	3.0

Source: Thomson Reuters Datastream; as of Friday close 14/7/2017

Summary

Fed Chair Janet Yellen testified before Congress. The takeaways were a slightly more dovish stance on interest rates and some soothing words on tapering the Fed's large balance sheet. US rates shed a few basis points in response (10-year at 2.32%), the USD fell further and US equities rose to new highs. Late in the week, weak retail sales and CPI reports fed into the relatively more dovish Fed stance (see US below).

Qatar and the US signed a memorandum of understanding (MoU) to fight terrorism. US Secretary of State visited the region to mediate in the GCC diplomatic flap. The deal was not deemed satisfactory by the coalition demanding concessions, but was likely seen by the markets as a step in the right direction. Qatar led the GCC markets last week, with earnings announcements helping those markets as well.

International Macroeconomics

US: While the Fed had been repeating that the sub-2% inflation rate was due to transitory factors, and thus that another rate hike was in the cards this year, Chair Yellen sounded more open minded on inflation, implying the Fed may decide to postpone the next hike, should inflation fail to pick up. We are closer to the no-hike camp, and the market is still pricing a 46% probability of a December hike.

Responding to concerns related to the expected tapering of the Fed's balance sheet later this year, Yellen implied that the impact on (long) interest rates would be minimal and spread out over time. Recall that the Fed owns fixed-income assets of \$4.3 trillion, and that it would start letting go \$10 billion per month, ramping up that number slowly to \$50 billion per month. In the suggested Fed schedule, it would take three years to shed \$1.5 trillion in assets, which would still leave a very large balance sheet. By some rough estimates, this could raise 10-year rates by 50 bps gradually over three years (other things being equal). The beginning of a taper later this year may be another reason to hold off temporarily on another federal funds rate hike (to gauge market reaction to the taper).

The latest Fed Beige Book described the US economy as growing slightly-to-moderately in all 12 Fed regional districts.

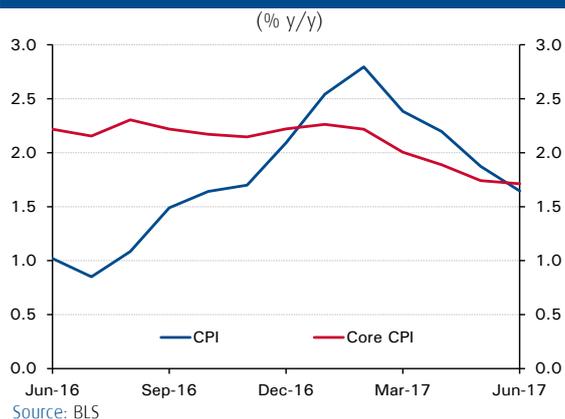
June CPI was unchanged while the core rose 0.1%, leaving y/y rates at 1.6% and 1.7%, respectively, still shy of the 2% target. (Chart 1.) Retail sales for June disappointed as well, falling 0.2% after -0.1% in May. The sales report led to downward revisions to Q2 GDP estimates by analysts, now close to 2% (q/q ann.) from over 3% a few weeks back.

Eurozone: Eurozone economic indicators were positive over the week with May's industrial production beating expectations (4.0% y/y vs. 3.6% expected) and the July's Sentix business sentiment holding up at strong levels (28.3 vs. 28.4 in June).

China: China's data came out positive for growth, beating expectations, especially June's trade figures. June exports rose 11.3% y/y, up from 8.7% growth in May. Domestic demand rose as well, as June imports grew 17.2% y/y. Healthy investment flows and trade numbers signal a pickup in growth, which should counter the effect of larger capital outflows.

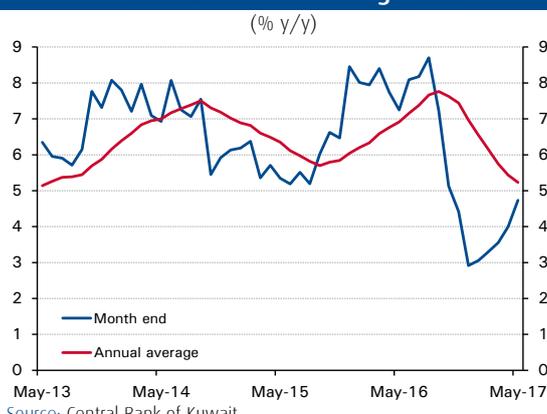
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Chart 1: US CPI



Source: BLS

Chart 2: Kuwait credit growth



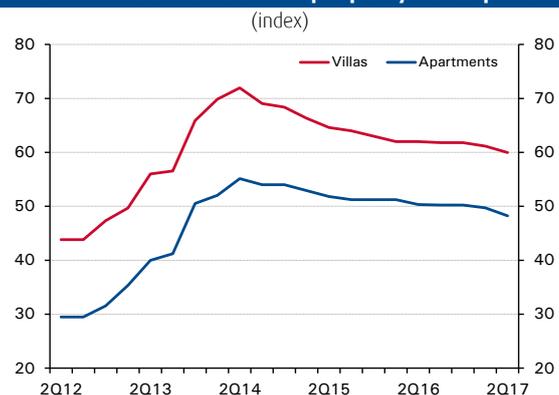
Source: Central Bank of Kuwait

Chart 3: Dubai Economy Tracker



Source: Emirates NBD

Chart 4: Dubai residential property sales prices



Source: Asteco

GCC & Regional Macroeconomics

Kuwait: Credit saw a healthy gain in May, with growth improving to 4.7% y/y. The month saw a net gain of KD 279 million in lending. Both business and household credit accounted for the healthy gain. Private deposits saw a moderate increase, but were flat y/y. (Chart 2.)

The Ministry of Finance finalized its draft law imposing excise taxes on select products, in line with a GCC-wide agreement. The law, which imposes a tax of 100% on tobacco and energy drinks and a 50% tax on carbonated drinks, will need to be approved by the cabinet before it is sent to the National Assembly for a vote.

Oman: The BP Khazzan gas project is expected to begin production in September 2017. A first train with a capacity of 500 million cubic feet per day will be deployed initially, followed by a second of similar capacity in early 2018, for a total new capacity of 1 billion cubic feet. The project is expected to lend a strong boost to GDP growth in 2018, offsetting cuts in crude oil production and a softening consumer sector.

Qatar: The US signed an agreement with Qatar to combat financing of terrorist activities, addressing one of the thirteen demands made by the group of four Arab nations boycotting Qatar. The group of four, however, released a joint statement expressing that more needs to be done to meet their demands on this issue.

Saudi Arabia: The draft value-added tax (VAT) law was approved by the Shura Council on 12 July. The VAT is in line with the GCC-wide agreement to implement this tax starting January 2018. The tax will be set at 5%, which is about a third of the European average. Still, a survey conducted by Deloitte Middle East shows 43% of respondents felt that the VAT will harm business competitiveness in the GCC.

UAE: Emirates NBD's Dubai Economy Tracker rose from 55.0 in May to 56.5 in June, on stronger output and orders data. The increase came on the back of a pick-up in all sectors, including construction, travel and tourism, and particularly wholesale and retail trade. (Chart 3.)

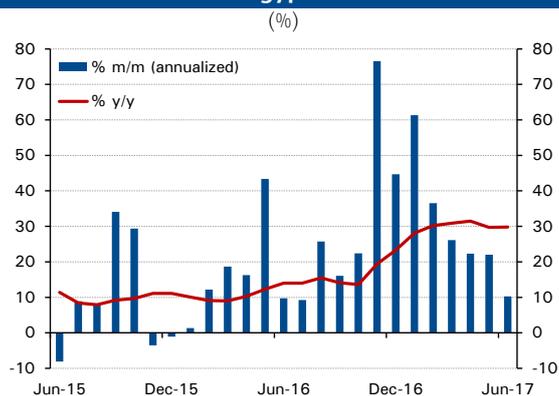
After a period of stabilization in 2016 and in early 2017, downward pressures on Dubai's residential property prices appear to have re-emerged in 2Q17. According to Asteco's quarterly indices, prices of apartments and villas in 2Q17 were down by 4.2% y/y and 3.3% y/y, respectively. (Chart 4.) The comparatively larger declines were attributed to increased housing supply and to a shift in demand towards the more affordable housing sector. (Chart 4.)

Egypt: Inflation was steady at 29.8% y/y in June, but saw a decline in monthly inflation. The monthly gain in consumer prices in June fell to an annualized 10.3%, half the prior month's pace. The central bank has sought to clamp down on a burst of inflation following the floating of the currency. It raised policy rates by 700 bps in three moves since. (Chart 5.)

Electricity prices were increased effective July in an effort to reduce the government's subsidy bill. Prices were hiked by 16-42% for the various brackets. The hikes, which followed cuts in domestic fuel and flour subsidies in recent weeks, will only partly offset the doubling in the cost of crude oil following the floating of the pound in November 2016. The schedule for phasing out electricity subsidies was pushed back to 2022.

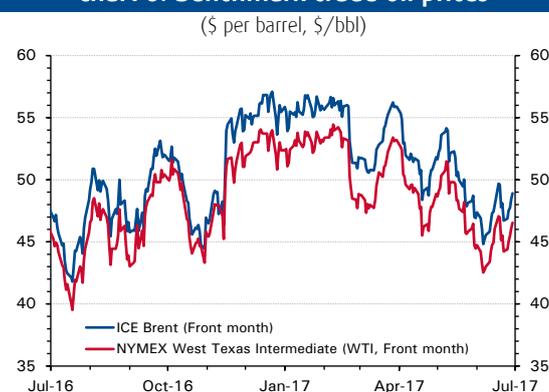
The IMF approved the payment of a second tranche (\$1.25 billion) of the \$12 billion loan agreement. The approval came as the IMF completed the

Chart 5: Egypt inflation



Source: Central Bank of Egypt

Chart 6: Benchmark crude oil prices



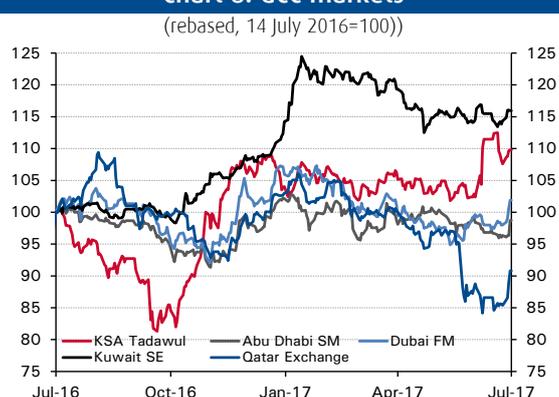
Source: Thomson Reuters Datastream

Chart 7: Total return indices



Source: Thomson Reuters Datastream

Chart 8: GCC markets



Source: Thomson Reuters Datastream

first review of progress made in implementing the reform program. The IMF sees that authorities have made good progress on fiscal as well as structural reform in recent months.

Markets – oil

Oil prices mitigated their losses, as both Brent and WTI figures rose over the past week on cuts in US and Saudi production and declines in European and US crude stockpiles. In the week ending 14 July, Brent and WTI prices increased 4.7% w/w to \$48.9/bbl and 3.3% w/w to \$46.5/bbl, respectively. In year-to-date terms, crude prices are down 13.9% for Brent and 13.4% for WTI. Trading on Friday was volatile as US rig counts increased, but demand growth from China and declining inventory kept prices elevated. (Chart 6.)

Gasoline inventories fell unexpectedly and US crude stocks dropped by 8.1 million barrels in the week ending 7 July, the biggest decline since September 2016. US rig count, however, increased by two rigs to a total of 765. Saudi Arabia announced it would reduce crude oil shipments by more than 0.6 mb/d in August in order to meet domestic demand during the summer season, but will still be in line with its OPEC production commitment. The kingdom's August crude export figure will be 6.6 mb/d, the lowest in 2017. According to Euroilstock data, stocks of oil products in Europe, mainly diesel, declined despite refineries increasing their crude oil intake in June.

Markets – equities

Equity markets made further advances this week supported by a flow of positive data and friendly central bank rhetoric, which signaled confidence in economic prospects but also keenness on a gradual phasing out of "easy" monetary policies. The MSCI World advanced market index was up 1.4% on the week. US equities continued trending upward unfazed by the latest Trump Russia troubles. The S&P 500 and DJIA were up 1.4% and 1%, respectively, and near 10% ytd. European equities also gained with the Eurostoxx 50 up 1.8%. Emerging markets outperformed with the MSCI EM up 3.3%. (Chart 7.)

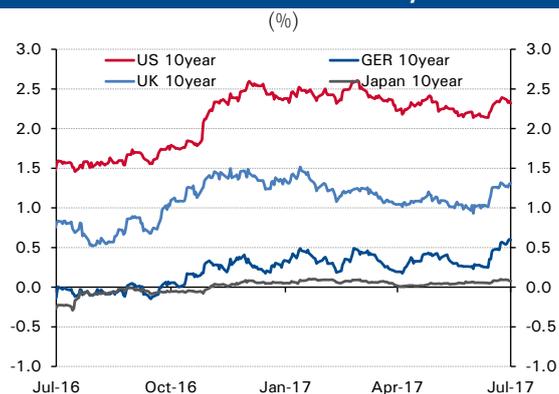
GCC markets also had a good week, buoyed by expectations of a positive earnings season. The MSCI GCC was up 2.7%, with all markets closing the week in positive territory. Within the region, Qatar was the outperformer with its general index up a strong 6.1%. Efforts by regional and western diplomats to resolve a month-long dispute between Qatar and its neighbors raised hopes. Also, Qatar's largest bank, QNB, announced results that surprised on the upside. (Chart 8.)

Markets – fixed income

US benchmark bonds took a breather following a 2-week selloff, while German bonds saw price gains reversed on news of ECB tapering guidance.

Believing that the selloff was overdone, investors bought into US and German government bonds early in the week. The buy-in was further supported by Fed Chair Yellen's relatively dovish testimony to Congress. However, soft US CPI and retail data and a WSJ article hinting at the possible announcement of a hawkish shift in ECB policy at the Fed's Jackson Hole conference in August saw US and German 10-year yields diverge. US 10-year yields finished the week down 7 bps, to settle at 2.32%, while 10-year Bunds were up to 0.60%, a level not seen in almost 19 months. (Chart 9.)

Chart 9: Global benchmark yields

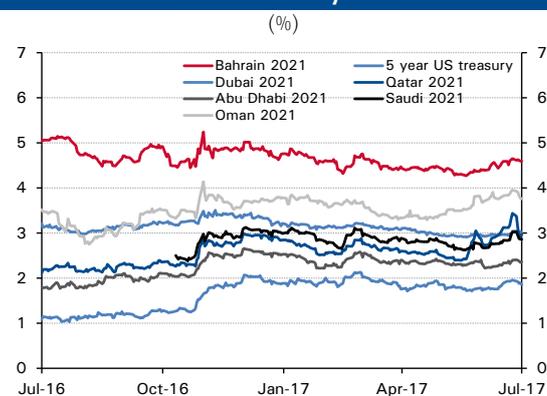


Source: Thomson Reuters Datastream

With no regional geopolitical news and oil prices firming over the week, GCC sovereign yields tracked US yields lower. Bonds maturing in 2021 for Abu Dhabi and Dubai, and 2022 for Kuwait and Saudi were down between 4-8 bps. Qatar’s 2021 yield was down 46 bps following the signing of the US-Qatar MoU on fighting terrorism.

Meanwhile, Saudi Arabia is expected to issue a local currency sukuk, or Islamic bond, this month; its first issuance after a moratorium begun in 2H16, when domestic system liquidity was under pressure. (Chart 10.)

Chart 10: GCC yields



Source: Thomson Reuters Datastream

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