Weekly Economic and Markets Review
NBK Economic Research Department I 15 July 2018
International & MENA

US may expand tariffs on Chinese goods; GCC economic activity still soft; oil down on bearish supply

Key market indicators

Stock markets	Index	Change (%) weekly	YTD
Regional			
Abu Dhabi (ADI)	4,687	1.82	6.56
Bahrain (ASI)	1,343	0.88	0.81
Dubai (DFMGI)	2,884	0.13	-14.42
Egypt (EGX 30)	15,880	-1.52	5.73
GCC (S&P GCC 40)	1,058	1.82	7.46
Kuwait (All Share Index)	5,213	2.47	7.92
KSA (TASI)	8,362	2.26	15.72
Oman (MSM 30)	4,441	-1.83	-12.91
Qatar (QE Index)	9,319	0.63	9.33
International			
CSI 300	3,493	3.79	-13.35
DAX	12,541	0.36	-2.92
DJIA	25,019	2.30	1.21
Euro Stoxx 50	3,455	0.18	-1.41
FTSE 100	7,662	0.58	-0.34
Nikkei 225	22,597	3.71	-0.74
S&P 500	2,801	1.50	4.78

Bond yields	%	Change (bps) weekly	YTD
Regional			
Abu Dhabi 2022	3.43	-1.8	48.2
Dubai 2022	3.91	-1.1	77.4
Qatar 2022	3.70	-3.0	62.2
Kuwait 2022	3.26	-2.5	45.2
Saudi Arabia 2023	3.68	1.6	46.2
International			
UST 10 Year	2.83	0.0	42.0
Bunds 10 Year	0.28	-0.6	-14.1
Gilts 10 Year	1.27	0.6	8.5
JGB 10 Year	0.05	1.4	-0.5

3m interbank rates	%	Change (bps) weekly	YTD
Bhibor	3.50	0.0	77.5
Kibor	2.00	0.0	12.5
Qibor	2.65	0.3	-9.6
Eibor	2.64	6.6	83.9
Saibor	2.61	-0.1	71.0
Libor	2.34	0.1	64.5

Exchange rates	Rate	Change (%) weekly	YTD
KWD per USD	0.303	0.13	0.53
KWD per EUR	0.353	0.17	-0.59
USD per EUR	1.169	-0.51	-2.59
JPY per USD	112.4	1.73	-0.28
USD per GBP	1.323	-0.38	-2.07
EGP per USD	17.84	0.00	0.62

Commodities	$/unit	Change (%) weekly	YTD
Brent crude	75.3	-2.31	12.65
KEC	72.6	-2.17	14.33
WTI	71.0	-3.78	17.53
Gold	1239.6	-1.17	-5.11

Source: Thomson Reuters Datastream; as of Friday's close 13/7/2018

Overview

President Trump announced a possible expansion of his tariffs to cover an additional $200bn worth of Chinese goods (almost half of all imports from China) that could be imposed by the end of the summer. He also declared victory in his efforts to extract additional defense spending (equivalent to 2% of GDP) from NATO allies before stating—and later retracting—that British PM Theresa May's softer Brexit plans would "kill" any potential trade deal with the US. US and international financial markets took the developments in their stride, however, ending the week higher by 1.5% (S&P 500) and 1.3% (MSCI AC), respectively.

In the eurozone, industrial production in May expanded by the fastest rate (1.3% y/y) since November 2017, bringing some relief to policymakers concerned about slow growth amid worsening US trade relations. The ECB appears to be on track to terminate its QE program by the end of the year.

Regionally, economic data continued to point to lingering weakness in the GCC, with Dubai's economy tracker easing a little in June on the back of softer travel and tourism figures, and Bahrain's real GDP in 1Q18 contracting by 1.2% y/y on lower crude oil production and an easing in financial services activity. Private credit growth in Kuwait also continued its seven-month decelerating run, slowing to 0.8% y/y in May, while in Saudi Arabia, labor force figures for 1Q18 were disappointing, as the unemployment rate rose to 12.9% despite expatriates leaving the country in record numbers. In Turkey, meanwhile, ratings agency Fitch further downgraded the country's long-term sovereign rating to junk status (BB) on the country's widening current account deficit and elevated politico-economic risks.

Oil prices finished the week lower, with Brent down 2.3% w/w at $75.3/bbl, on the bearish news that Libya was due to resume oil shipments and the US could tap its strategic petroleum reserve in order to bring down domestic gasoline prices.

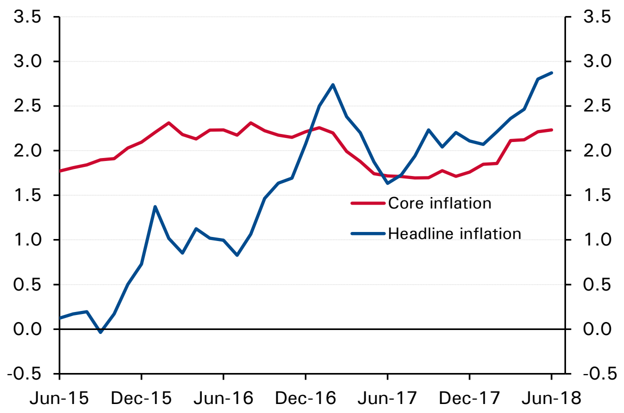
International macroeconomics

USA: Mr. Trump upped the ante in his trade war with China, considering tariffs on $200bn of Chinese imports, with implementation possibly as early as September. Unlike the tariffs imposed earlier in the month, these new measures largely target capital and consumer goods. Retaliation from the Chinese is expected, but their ability to respond in kind may be limited. US imports into China were valued at $120bn—well below the $500bn of Chinese goods imported by the US in 2017—which could possibly force the Chinese to target US services companies operating in China (though unlikely) or further devalue the renminbi to compensate for the higher tariffs. However, these tariffs may not go through, as the blowback from financial markets has been notable and the impact of these measures on republican manufacturing states ahead of mid-term elections may be negative.

Both June headline and core US consumer price inflation came in as expected, expanding by 2.9% y/y, up from 2.8% y/y in May, and 2.3% y/y, respectively. (Chart 1.) The steady rise in prices further supports the Fed's plan to raise rates twice more this year. Meanwhile, consumer sentiment dropped more than expected in July, to 97.1 from 98.2 in June, on growing concerns about US trade policies.

Chart 1: US CPI

(% y/y)



Source: Thomson Reuters Eikon

Eurozone: The ECB meeting minutes revealed that the governing council was unanimous in its plan to end the quantitative easing program by the end of 2018. The ECB appears convinced that the European economy is strong enough to withstand the withdrawal even amid softer data and global trade concerns. The bank will also continue to reinvest the proceeds from its program and will not raise rates until the autumn of next year at the earliest.

Moreover, helping to further shake off concerns of slower growth in the eurozone was May's industrial production data, which was the highest since November 2017 at 1.3% y/y. This was driven by higher output of durable and non-durable goods.

China: Producer price inflation hit a six-month high in June, climbing to 4.7% y/y from 4.1% y/y in May amid higher commodity prices (especially oil) and, to some extent, a weaker currency, which has driven up the cost of imports. In contrast, consumer price inflation was more subdued, coming in marginally higher at 1.9% y/y versus 1.8% y/y the previous month. This should provide the government with some leeway to adopt a more expansive monetary policy stance in support of the economy.

Meanwhile, as part of its 'Belt and Road' initiative, China will reportedly provide $20bn worth of loans to enhance the MENA region's economic development and bolster its economic ties with the region. It will be targeting Arab states that require reconstruction assistance in particular.

GCC & regional macroeconomics

Kuwait: Private credit growth continued to decelerate in May, slowing for the seventh consecutive month to 0.8% y/y—the weakest growth in seven years. (Chart 2.) Softer household borrowing and a drop in lending for real estate and securities purchases weighed on activity. However, borrowing by businesses was at its strongest in almost a year, led by credit for trade and construction. The rebound may finally be reflective of growing retail sector and project financing demand. Private credit should finish 2018 up by 4% y/y.

Chart 2: Kuwait private credit

(% y/y)

Source: Central Bank of Kuwait

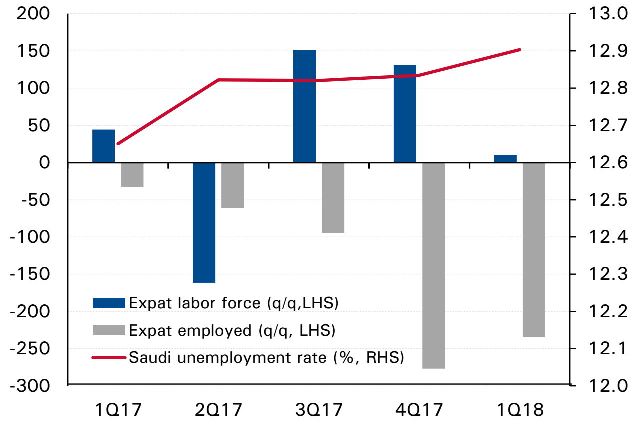
Ara's June consumer confidence improved to 114, with a pick-up across the board. The index's 12-month moving average grew by 13%, its strongest pace in 6 years, with individuals increasingly optimistic about the economic outlook including better employment prospects.

Kuwait deepened its ties with China, establishing a strategic partnership to help establish new bilateral prospects. The two countries will synergize the 'Belt and Road' Initiative with Kuwait Vision 2035 and work to promote the establishment of a China-GCC free trade area. Moreover, several bilateral agreements covering e-commerce, FDI, oil, and smart cities were signed in the process.

Saudi Arabia: The official Saudi statistics agency reported that more than 234,000 expatriates left their jobs during the first quarter of the year, bringing the cumulative total departure of expatriates since 4Q16 to more than 700,000. (Chart 3.) But the departure of expatriates has not led to a commensurate increase in Saudi employment; in fact the Saudi unemployment rate has increased from 12.3% to 12.9% over the same period, as the Saudi labor force has expanded at a faster rate than the employment rate.

Chart 3: Saudi unemployment & expat labor changes

(% Saudi unemployment; '000 expats)



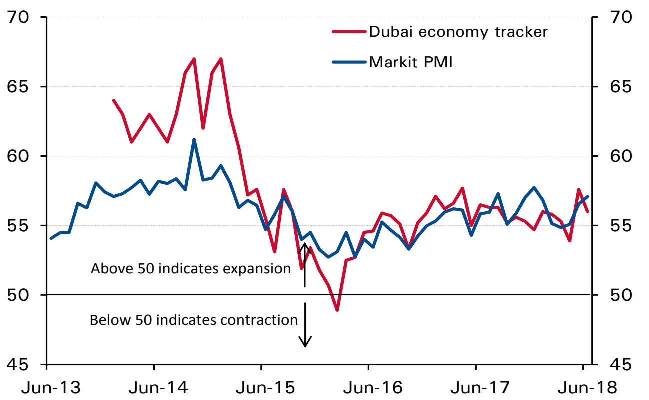
Source: General Authority for Statistics (GASTAT)

The government published its draft public-private partnerships (PPP) law, which aims to encourage the private sector to take on a greater role in the kingdom's economic development. This, the authorities hope, could be facilitated by offering the private sector exemptions from labor laws, real estate ownership restrictions and other regulations.

UAE: The Emirates NBD Dubai Economy Tracker Index fell slightly from 57.6 in May to 56.0 in June. (Chart 4.) This was mainly attributed to an easing in activity in the travel and tourism sectors due partly to the impact of Ramadan.

Chart 4: UAE PMI & Dubai Economy Tracker

(index)



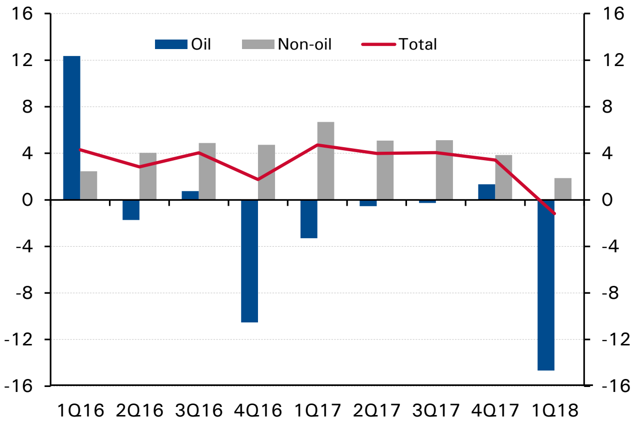
Source: IHS Markit, Emirates NBD

Moreover, UAE tourism is expected to get a further boost later this year after the authorities approved exempting UAE transit passengers from all entry fees (for the first 48hrs of their stay) and VAT refunds for tourists (starting from 4Q18).

Bahrain: Bahrain's real GDP contracted in 1Q18, by 1.0% q/q and 1.2% y/y, amid a decline in oil GDP (-14.7% y/y) related to lingering oil field maintenance issues and Bahrain's OPEC+ quota obligations, and an easing in non-oil sector economic activity (+1.9% y/y) linked to a decline in financial services output. (Chart 5.) The fall in headline growth has come after a decent run of sequential near-4% growth on average over the last four quarters

Chart 5: Bahrain's quarterly real GDP

(% y/y)



Source: Information & eGovernment Authority

Turkey: President Erdogan named his son-in-law, Beral AlBayrak, as the new treasury and finance minister. The announcement caused considerable unease among investors, sending the lira down almost 4% against the US dollar (the biggest fall since the failed coup attempt last year). The Turkish currency is down about 30% so far this year. Markets were rattled further after the President gave himself the power to appoint the governor of the central bank, thus changing the system under which the central bank governor was chosen for a five-year term by the PM and other cabinet. This, along with the prospect that the governor would have little or no say in the appointment of his/her own deputies, has left many concerned about the waning independence of Turkey's central bank.

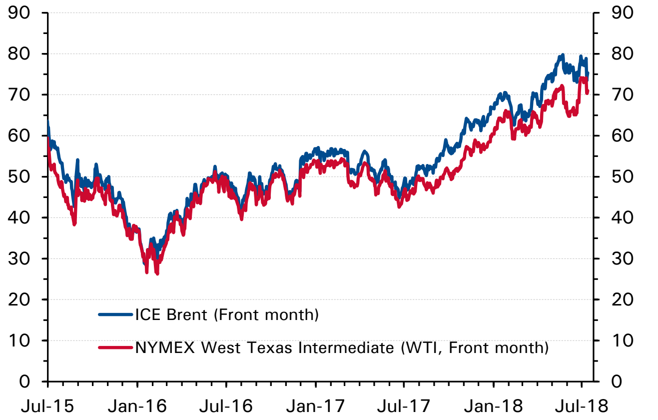
In response, rating agency Fitch cut Turkey's long-term sovereign debt rating deeper into non-investment grade territory, from BB+ to BB, citing a widening current-account deficit, rising inflation and increased economic uncertainty.

Markets – oil

Oil prices ranged lower last week, pressured by predominantly bearish supply news. (Chart 6.) Brent closed on Friday down 2.3% w/w at $75.3/bbl and WTI down by 3.8% w/w to finish at $71.01/bbl after Libya announced that it would lift force majeure on several major export terminals to resume crude exports and after it was reported that the US might tap its 660 million-barrel Strategic Petroleum Reserves (SPR) to counter rising gasoline prices. The prospect of 700,000 b/d of Libyan crude back coming back on line (as well as the broader market sell-off relating to Mr. Trump's tariff escalation) caused Brent to drop almost 7% on Wednesday—its largest daily fall in two years; oil prices were on track to fall further before the end of the week had the EIA not reported a drawdown in US crude stocks and Iran not come out on Friday to dispute Russia's claim that OPEC was lifting production.

Chart 6: Crude oil prices

($/bbl)



Source: Thomson Reuters Datastream

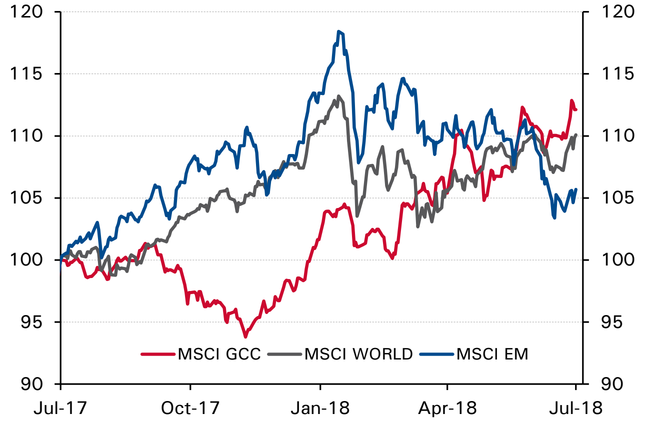
Also helping to minimize oil price losses was the bullish news that US Treasury secretary Steve Mnuchin had ruled out sanctions waivers for importers of Iranian crude, seemingly contradicting the earlier announcement by the Secretary of State Mike Pompeo that such exemptions could be possible. These sanctions, the IEA warned, would, along with further supply disruptions, cause spare oil production capacity to be "stretched to the limit". Most analysts had already raised their oil price forecasts to reflect these potentialities.

Markets – equities

International markets ended the week higher despite the increase in trade sanctions by the US on China, with the MSCI AC world index up 1.3% w/w. US markets were lifted by expectations of a strong upcoming earnings season. As a result, the S&P 500 increased by 1.5% w/w, while the DJI improved by 2.3% w/w. (Chart 7.) In Europe, the Euro Stoxx 50 was flat on the week. Meanwhile, emerging markets shook off the sell-off that followed Mr. Trump's announcement last week, supported by a renewed appetite for risk. The MSCI EM index was up 1.3% w/w.

Chart 7: Total equity return indices

(rebased, 13 July 2017=100)

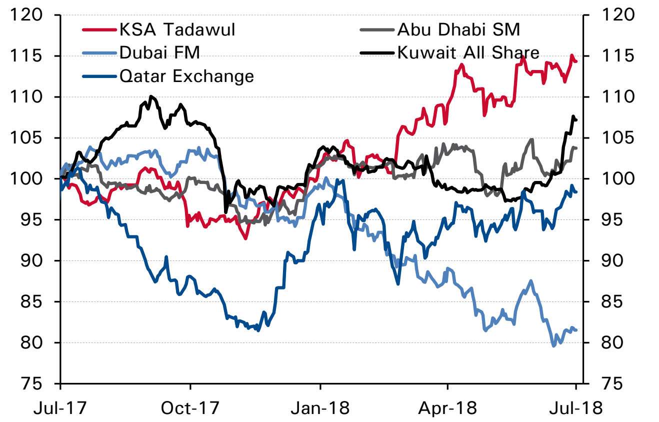


Source: Thomson Reuters Datastream

Regionally, the MSCI GCC index was up 2.1% w/w, led by renewed confidence, interest, and strong initial corporate earnings in Kuwait, helping it outperform its GCC peers to increase by 2.5% w/w. Saudi (+2.3% w/w) and Abu Dhabi (+1.8% w/w) followed, supported by still firm oil prices and strong expected earnings. (Chart 8.)

Chart 8: GCC equity markets

(rebased, 13 July 2017=100)

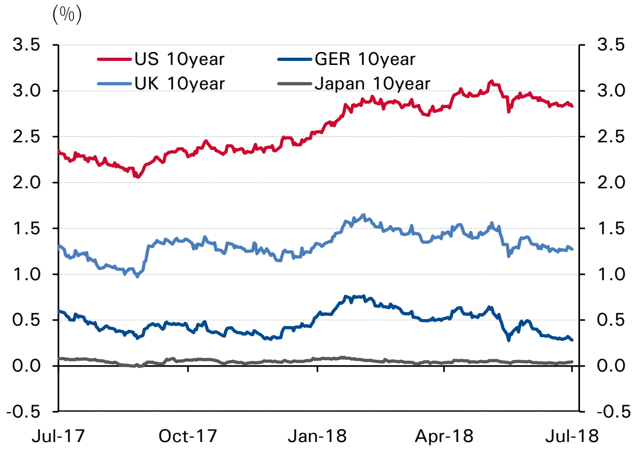


Source: Thomson Reuters Datastream

Markets – fixed income

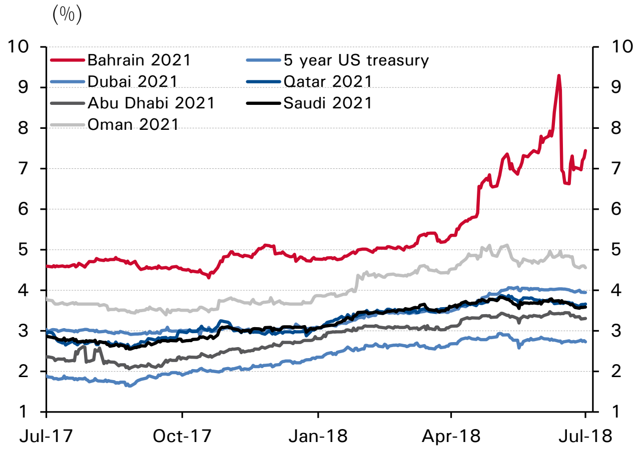
Benchmark yields were little changed last week, as Mr. Trump's trade sanctions were offset by rising inflation in the US and relatively hawkish ECB. Rates on US 10-year Treasuries held at 2.83%, while 10-year Bunds edged slightly lower to 0.28%. (Chart 9.) As such, and with no domestic catalysts, GCC yields were steady last week, shifting lower by up to 3 basis points for some. (Chart 10.)

Chart 9: Global bond yields



Source: Thomson Reuters Datastream

Chart 10: GCC bond yields



Source: Thomson Reuters Datastream

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