

# Saudi Arabia raises interest rates ahead of likely move by US Federal Reserve

## Key market indicators

| Stock markets             | Index   | Change (%)   |       |
|---------------------------|---------|--------------|-------|
|                           |         | weekly       | YTD   |
| <b>Regional</b>           |         |              |       |
| Abu Dhabi (ADI)           | 4,543   | 0.35         | 3.28  |
| Bahrain (ASI)             | 1,356   | -1.08        | 1.79  |
| Dubai (DFMGI)             | 3,197   | 1.26         | -5.13 |
| Egypt (EGX 30)            | 16,999  | 3.20         | 13.18 |
| GCC (S&P GCC 40)          | 976     | 0.35         | -0.86 |
| Kuwait (Price Index)      | 6,760   | -0.26        | 5.50  |
| KSA (TASI)                | 7,745   | 2.41         | 7.17  |
| Oman (MSM 30)             | 4,897   | -0.67        | -3.97 |
| Qatar (QE Index)          | 8,848   | 6.49         | 3.81  |
| <b>International</b>      |         |              |       |
| CSI 300                   | 4,056   | -1.28        | 0.63  |
| DAX                       | 12,390  | 0.35         | -4.09 |
| DJIA                      | 24,947  | -1.54        | 0.92  |
| Euro Stoxx 50             | 3,437   | 0.49         | -1.90 |
| FTSE 100                  | 7,164   | -0.84        | -6.81 |
| Nikkei 225                | 21,677  | 0.97         | -4.78 |
| S&P 500                   | 2,752   | -1.24        | 2.93  |
| <b>Bond yields</b>        |         |              |       |
|                           | %       | Change (bps) |       |
|                           |         | weekly       | YTD   |
| <b>Regional</b>           |         |              |       |
| Abu Dhabi 2022            | 3.37    | -2.0         | 42.0  |
| Dubai 2022                | 3.40    | -2.7         | 25.9  |
| Qatar 2022                | 3.59    | -6.0         | 51.0  |
| Kuwait 2022               | 3.33    | 1.0          | 52.0  |
| Saudi Arabia 2023         | 3.72    | 1.0          | 50.0  |
| <b>International</b>      |         |              |       |
| UST 10 Year               | 2.85    | -4.6         | 43.7  |
| Bunds 10 Year             | 0.57    | -8.1         | 14.6  |
| Gilts 10 Year             | 1.43    | -6.3         | 24.3  |
| JGB 10 Year               | 0.04    | -1.3         | -1.2  |
| <b>3m interbank rates</b> |         |              |       |
|                           | %       | Change (bps) |       |
|                           |         | weekly       | YTD   |
| Bhibor                    | 3.00    | 0.0          | 27.5  |
| Kibor                     | 1.88    | 0.0          | 0.0   |
| Qibor                     | 2.62    | -8.2         | -12.4 |
| Eibor                     | 2.11    | 3.7          | 31.4  |
| Saibor                    | 2.02    | 6.0          | 11.9  |
| Libor                     | 2.18    | 10.6         | 48.3  |
| <b>Exchange rates</b>     |         |              |       |
|                           | Rate    | Change (%)   |       |
|                           |         | weekly       | YTD   |
| KWD per USD               | 0.300   | -0.17        | -0.54 |
| KWD per EUR               | 0.370   | 0.05         | 4.25  |
| USD per EUR               | 1.229   | -0.15        | 2.43  |
| JPY per USD               | 106.0   | -0.72        | -5.92 |
| GBP per USD               | 1.394   | 0.66         | 3.16  |
| EGP per USD               | 17.54   | -0.27        | -1.10 |
| <b>Commodities</b>        |         |              |       |
|                           | \$/unit | Change (%)   |       |
|                           |         | weekly       | YTD   |
| Brent crude               | 66.2    | 1.10         | -0.99 |
| KEC                       | 61.1    | 2.17         | -3.76 |
| WTI                       | 62.3    | 0.48         | 3.18  |
| Gold                      | 1311.3  | -0.84        | 0.38  |

Source: Thomson Reuters Datastream; as of Friday's close 16/3/2018

## Overview

There was mixed news on the performance of the US economy, with figures showing retail sales falling in February despite a boost from tax cuts and continued labor market strength. The data--combined with concerns over US policy direction following the ousting of Secretary of State Rex Tillerson--pushed down the yield on 10-year treasuries and weakened the dollar, but both subsequently recovered on strong industrial production and consumer confidence data. Expectations remain almost unanimous that the Federal Reserve will hike interest rates by 25bps this coming Thursday--its sixth hike since the start of the tightening cycle.

In Europe, amid improved economic performance, ECB president Mario Draghi reaffirmed a dovish approach to future policy tightening, stating that interest rates would be unchanged "well past" the ending of the bank's asset purchase program, likely later this year.

Brent crude oil prices rose 1% w/w to \$66. The International Energy Agency reported that although the oil market was likely to be in surplus in 1Q 18, rebalancing was 'clearly moving ahead' amid solid global demand and OPEC supply restraint. It also highlighted the risk to the market of further supply disruption from crisis-hit Venezuela, whose crude production has plunged over the past year.

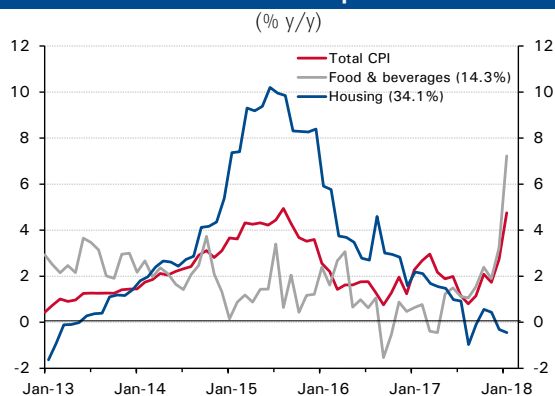
GCC equity markets were mixed last week, with the MSCI index up 2.5% but boosted by a 6.5% jump in the Qatari market following an announcement by Qatar National Bank that it would look to lift foreign ownership limits to 49% from their current 25%. Meanwhile, most central banks in the GCC are expected to raise interest rates following the Fed's likely step later this week, with Saudi Arabia already hiking its main policy rates by 25 bps last week in anticipation of the move.

## International macroeconomics

**USA:** Inflation in both consumer and producer prices was softer in February, easing concerns over stronger price pressures which had rocked markets a month ago. While the CPI gain of 0.2% during the month was at consensus, annual core inflation did not move from its pace a month before, remaining at 1.8% y/y despite a consensus at 1.9%. The softer data was already apparent in February's wage growth figure released earlier this month.

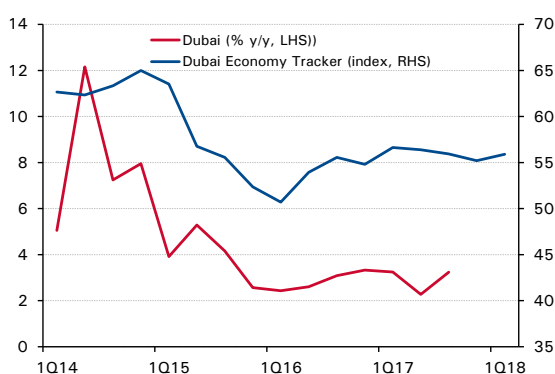
Other economic data was mixed. The Philly Fed survey remained exceptionally strong at 22.3 for March. New orders and unfilled orders were particularly healthy. February's industrial production was also solid gaining 1.1% on the month following some months of weakness. However, softness characterized other data including housing starts and retail sales. Retail sales slipped 0.1% in February compared to a consensus for a 0.4% monthly gain. Weakness in autos was only partly to blame as sales there slipped from post-Hurricane Harvey strength.

**Chart 1: UAE consumer price inflation**



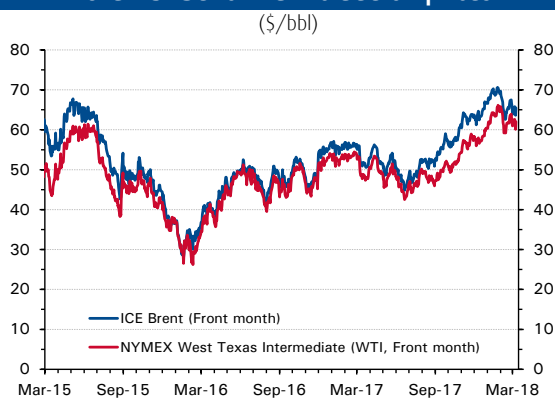
Source: FCSA

**Chart 2: Dubai real GDP and Economy Tracker**



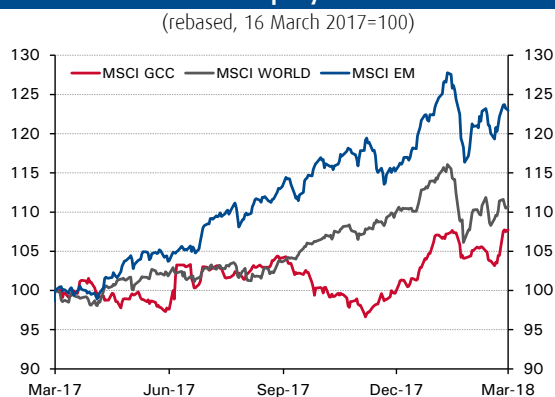
Source: Dubai Statistics Center, IHS Markit, Emirates NBD

**Chart 3: Benchmark crude oil prices**



Source: Thomson Reuters Datastream

**Chart 4: Total equity return indices**



Source: Thomson Reuters Datastream

## GCC & regional macroeconomics

**Saudi Arabia:** SAMA raised its key interest rates, the repo and reverse repo, by 25 bps to 2.25% and 1.75%, respectively, last Thursday. While a near-term increase in the reverse repo was expected, in step with the US fed's rate tightening program, the repo's change was its first since 2009. The move came as the 3-month Saudi interbank rate fell last week below the US dollar equivalent LIBOR for the first time since the financial crisis (-14.5 bps difference), which officials fear could trigger capital outflows.

Prince Mohamed Bin Salman's high profile visit to the UK last week concluded with at least \$90 billion in mutual trade commitments over the next few years including an MOU for the purchase of Typhoon fighter jets from UK aircraft manufacturer BAE systems.

Saudi officials also revealed that the much-feted Aramco IPO may be postponed to 2019. There is still no indication which of the major stock markets--London, New York or Hong Kong--the kingdom is leaning towards for Aramco's international listing.

**UAE:** Inflation in the UAE climbed from 2.7% y/y in December to 4.8% y/y in January, following the introduction of a 5% VAT and higher fuel prices. (Chart 1.) Food price inflation leapt to 7.2% y/y, but the continued decline in housing costs helped limit the rise in the overall index.

Dubai's real GDP expanded by a solid 3.2% y/y in 3Q17, higher than the 2.3% y/y pace recorded in 2Q17. (Chart 2.) The pick up was driven by the trade, finance and real estate & construction sectors. Growth is expected to have expanded further still in 4Q17 as both consumers and businesses front loaded their purchases and production ahead of the introduction of the VAT. Meanwhile, the Dubai economy tracker slipped slightly in February to 53.9, but remains at solid levels.

**Qatar:** The government released its second five-year National Development Strategy report, covering 2018-2022. The report highlights broad aims such as boosting productivity, skills and institutional capacities and promoting private sector development and R&D. The government will also curb transfers to the Qatar Investment Authority going forward.

The release came in a week that saw a major bounce in the Qatari stock market (+6.5% w/w)--partly a recovery following steep declines in previous weeks but also on positive news about an increase in Foreign Ownership Limits.

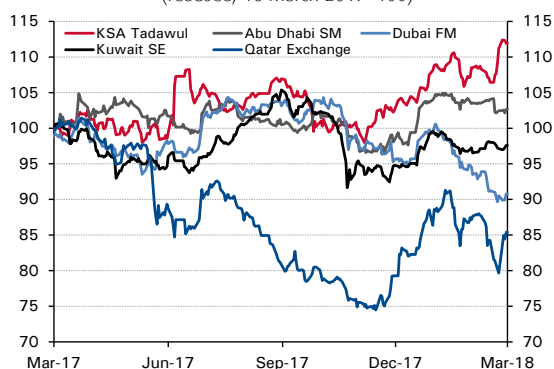
**Oman:** Moody's downgraded Oman to BAA3, with a negative outlook, over sluggish economic growth and fiscal sustainability concerns.

## Markets – oil

Oil prices were on course to close the week down before a last minute rally, seemingly without an identifiable catalyst, pulled Brent and WTI up to end the week higher for the second week in succession. Brent gained 1% w/w to reach \$66.21/bbl and WTI rose by 0.5% w/w to settle at \$62.31/bbl. (Chart 3.) Last week's improvement did find some support, however, from a diverse range sources including the replacement of secretary of state Rex Tillerson with the more hawkish Mike Pompeo, and the IEA's recently-raised global oil demand growth forecast for 2018 (+90 kbd to 1.5 mb/d).

**Chart 5: GCC equity markets**

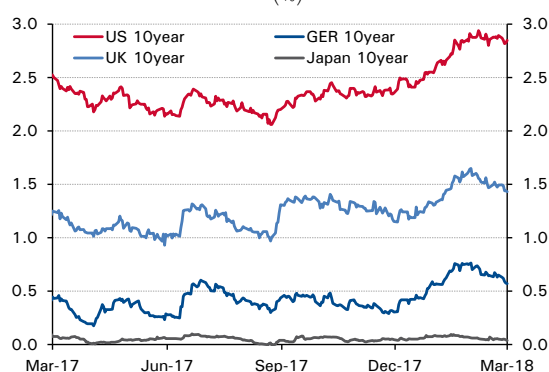
(rebased, 16 March 2017=100)



Source: Thomson Reuters Datastream

**Chart 6: Global bond yields**

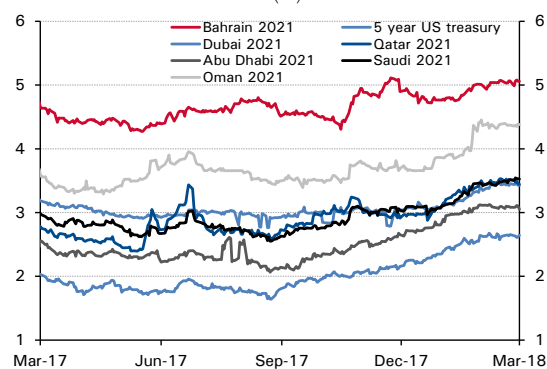
(%)



Source: Thomson Reuters Datastream

**Chart 7: GCC bond yields**

(%)



Source: Thomson Reuters Datastream

## Markets – equities

Global equity markets were volatile throughout the week, swinging on geopolitical and economic cues. White House developments also weighed on sentiment. Overall, the MSCI AC index fell 0.5% on the week. (Chart 4.)

In the US, investors digested the departure of secretary of state Rex Tillerson with caution, while unsurprising US inflation kept analysts' forecasts broadly unchanged. The DJI and the S&P 500 fell 1.5% and 1.2%, respectively. Elsewhere, trade war fears and geopolitics concerning Russia kept investors wary. The Euro Stoxx 50 was up 0.5% and the MSCI EM index increased by a tame 0.6%.

GCC markets outperformed, lifted by expectations of foreign inflows and changes to ownership limits, with the MSCI GCC index up 3% last week. Saudi was boosted by prospects of being included in both the FTSE (March) and MSCI (June), with banks and petrochemicals benefitting the most. Meanwhile, capital increases and changes to foreign ownership limits of some large market players boosted Dubai and Qatar. Kuwait was relatively little changed, with its weighted index up 0.4% w/w. (Chart 5.)

## Markets – fixed income

Global geopolitics, White House tumult and unsurprising data saw benchmark yields ease last week. US treasuries benefitted from investors seeking safe havens amidst more political upheaval, benign inflation, and weaker retail sales. (Chart 6.) Anticipation of this week's FOMC meeting (20-21 March) saw traders book profits, containing the fall in yields. US 10-year treasuries were down 5 bps w/w to 2.85%. Yields on Bunds followed their US counterparts lower and were further pressured by dovish rhetoric from ECB president Mario Draghi. As such, 10-year bunds shaved 8 bps w/w, reaching 0.57%. Meanwhile, GCC benchmark yields were mixed, with Qatar 2022 losing 6 bps on the week, while Kuwait 2022 and Saudi 2023 each gained 1 basis point. (Chart 7.)

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