Weekly Economic and Markets Review
NBK Economic Research Department I 27 May 2018
International & MENA

Political instability weighs on the euro; oil prices dip on prospect of output increase by OPEC and Russia

Key market indicators

Stock markets	Index	Change (%) weekly	YTD
Regional			
Abu Dhabi (ADI)	4,601	3.82	4.61
Bahrain (ASI)	1,263	-0.76	-5.15
Dubai (DFMGI)	2,954	1.44	-12.33
Egypt (EGX 30)	16,634	-1.44	10.75
GCC (S&P GCC 40)	1,011	3.82	2.68
Kuwait (All Share Index)	4,731	-1.45	n/a
KSA (TASI)	8,038	0.26	11.23
Oman (MSM 30)	4,564	-1.92	-10.49
Qatar (QE Index)	9,049	1.78	6.17
International			
CSI 300	3,816	-2.22	-5.32
DAX	12,938	-1.07	0.16
DJIA	24,753	0.15	0.14
Euro Stoxx 50	3,515	-1.63	0.33
FTSE 100	7,730	-0.62	0.55
Nikkei 225	22,451	-2.09	-1.38
S&P 500	2,721	0.31	1.78

Bond yields	%	Change (bps) weekly	YTD
Regional			
Abu Dhabi 2022	3.56	-7.8	61.5
Dubai 2022	4.00	4.1	85.7
Qatar 2022	3.90	0.2	82.5
Kuwait 2022	3.49	-9.8	68.5
Saudi Arabia 2023	3.86	-19.8	64.5
International			
UST 10 Year	2.94	-13.2	52.4
Bunds 10 Year	0.41	-16.8	-1.6
Gilts 10 Year	1.32	-17.6	13.6
JGB 10 Year	0.04	-1.7	-0.8

3m interbank rates	%	Change (bps) weekly	YTD
Bhibor	3.20	2.5	47.5
Kibor	1.94	-6.3	6.3
Qibor	2.63	-1.6	-10.9
Eibor	2.47	-3.0	67.3
Saibor	2.43	1.5	53.6
Libor	2.32	-1.2	62.5

Exchange rates	Rate	Change (%) weekly	YTD
KWD per USD	0.302	0.08	0.25
KWD per EUR	0.353	-0.75	-0.59
USD per EUR	1.165	-1.06	-2.88
JPY per USD	109.4	-1.23	-2.92
GBP per USD	1.331	-1.22	-1.52
EGP per USD	17.87	0.62	0.79

Commodities	$/unit	Change (%) weekly	YTD
Brent crude	76.4	-2.64	14.31
KEC	73.9	-2.67	16.36
WTI	67.9	-4.77	12.35
Gold	1303.3	1.02	-0.23

Source: Thomson Reuters Datastream; as of Friday's close 25/5/2018

Overview

Politics remained in focus with markets buffeted towards the end of the week by the calling-off of the US-North Korea summit, the economic proposals of Italy's likely new populist government and by the calling of a no-confidence vote in the government in Spain. The news saw stocks reverse gains made early in the week, pushed up the spreads on Italian and Spanish government bond yields and weighed on the euro, which dropped to a six-month low of nearly $1.16 versus the dollar. The strengthening of the dollar came despite a relatively dovish set of minutes of the Federal Reserve's last policy meeting, which increased the chances of two rather than three further rate hikes this year.

Brent crude prices saw their first weekly drop since early April, declining nearly 3% w/w to end just above $76/bbl. The dip came on expectations that OPEC and key non-OPEC producers – whose supply discipline has been central to the recent rally – will announce an increase in production by up to 1 million b/d when they meet next month to offset the drop in output in Venezuela and in Iran once sanctions take effect. Prices are still 14% higher than at the start of the year and nearly 50% up on a year ago.

The sharp dip in oil prices came too late in the week to affect markets across the Gulf region. But there were encouraging signs on the region's longer-term prospects from the latest World Competitiveness Report by Swiss business school IMD, which showed both the UAE (7) and Qatar (14) making it into the top 15 out of the 63 countries ranked in 2018. Both countries advanced their scores from the previous year, and scored highly for economic performance. The UAE topped the international league in the areas of international trade and attitudes and values, and finished second in a host of other areas.

International macroeconomics

USA: The minutes of the Federal Reserve's May policy meeting where rates were left on hold noted policy-setters' concern about the possible negative impact on business sentiment of recent trade tensions, and hinted at some tolerance for inflation climbing above the 2% target for a time. The minutes were interpreted as dovish, and although the next rate hike is still expected in June with almost certainty, the probability of three rather than two further rates hikes this year has fallen.

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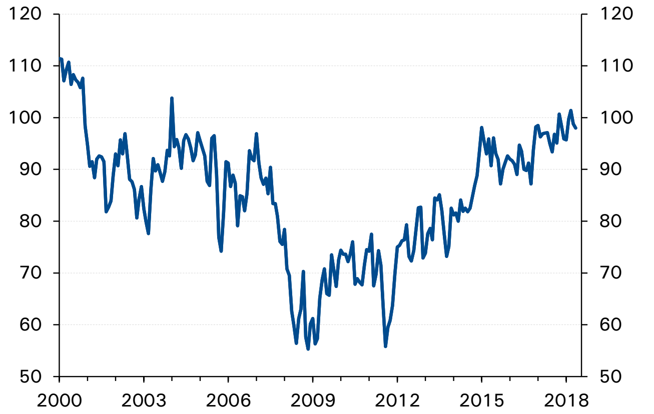
Elsewhere, data point to continued upbeat conditions in industry. The flash PMI figure for May came in at a strong 55.7 from 54.8 in April, above expectations and including a rise to 56.6 for the services component. Underlying durable goods orders also rose a robust 0.9% m/m. Consumer-related data, however, were a touch disappointing. Home sales – both new and existing – came in softer than anticipated, perhaps affected by rising prices: the FHFA house price index for March showed prices rising a sturdy 6.7% y/y, despite a modest 0.1% rise on the month. And the final reading of the University of Michigan's consumer confidence survey showed sentiment slipping to 98 – still historically strong but below the mid-month flash estimate. (Chart 1.)

Chart 1: Univ. of Mich. consumer sentiment

(index)



Source: Thomson Reuters Datastream

Eurozone: Soft May Eurozone indicators hint at a longer-lasting period of lower growth. The Eurozone composite PMI came in well below expectations at 54.1 – impacted by slower new order growth and weaker export demand – while German consumer sentiment eased for a second consecutive month. Despite the apparent softening of economic momentum recently, the pace of the current expansion remains healthy.

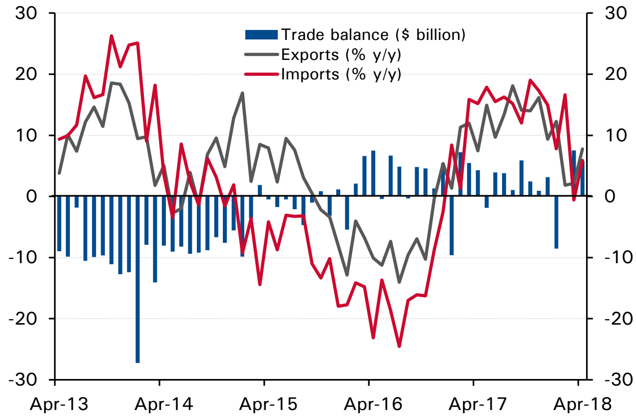
Political factors were also at the fore across Europe. In Italy, Guiessepe Conte, a newcomer to the political scene, was appointed prime minister, while Moody's has placed the sovereign's credit rating on review. Also, prospects of an early election in Spain were brought forth following a campaign finance scandal associated with PM Rajoy's Popular Party.

These developments may warrant more caution from the ECB. The bank is currently expected to end its QE program by end-2018, with rates hiked by mid-2019. However, further softness in the data and increased political uncertainty may see the latter pushed back. Eurozone inflation and economic sentiment, both market-moving indicators, are due this week, and are seen at 1.6% y/y (higher) and 112 (unchanged), respectively.

Japan: Export and import growth both accelerated in April. Export growth climbed from 2.1% y/y in March to 7.8% y/y in April, mainly on the back of higher car and manufacturing equipment shipments. Import growth recovered from the 0.6% y/y contraction in March to expand 5.9% y/y. (Chart 2.) The rise in export growth should offer some support to the overall economy, after it contracted in 1Q18.

Chart 2: Japan trade

(% y/y)

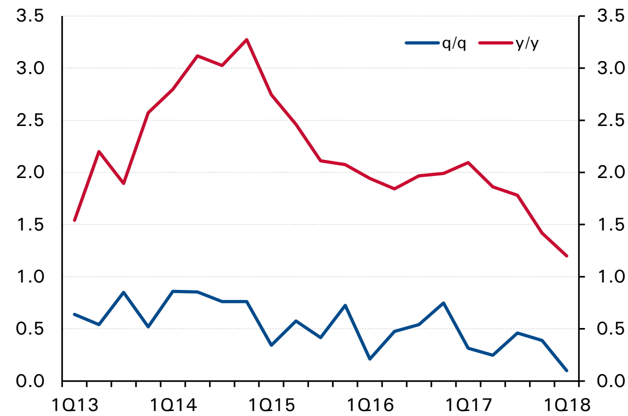


Source: Thomson Reuters Datastream

UK: Second estimates of GDP growth in 1Q18 show that the economy expanded by only 0.1% q/q and by 1.2% y/y. (Chart 3.) The quarterly growth rate is the slowest since 2012, with consumer spending (+0.2% q/q) and business investment (-0.2% q/q) especially weak. Services fared slightly better (+0.3% q/q), but like other sectors in the economy, was pulled down by the poor weather of Jan-March. Amid Brexit-related uncertainty, the slowdown in the growth of consumer-facing industries is a particular source of concern for policymakers.

Chart 3: UK real GDP

(% change)



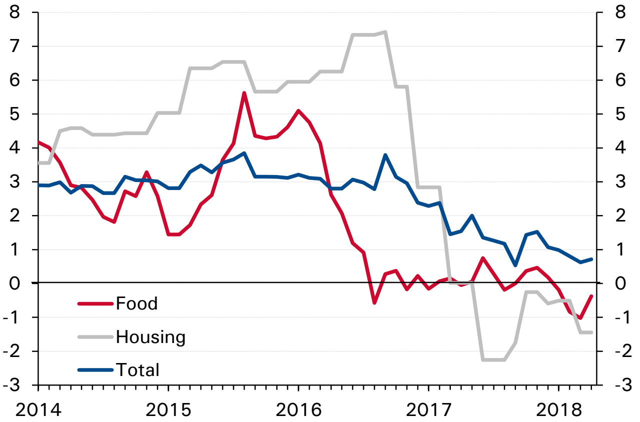
Source: Office for National Statistics (ONS)

GCC & regional macroeconomics

Kuwait: Inflation picked up slightly to 0.7% y/y in April versus March's 0.6% figure, with food deflation declining to 0.4% y/y from 1.0% a month earlier. (Chart 4.) Prices for furnished goods rose at a slightly faster pace of 2.4% y/y versus 2.0% in March. Inflation in clothing and footwear along with other miscellaneous goods eased, at 0.4% y/y and 5.6%, respectively. Core inflation, which excludes food and beverages as well as housing, was steady at 2.6% y/y.

Chart 4: Kuwait consumer price inflation

(% y/y)



Source: Central Statistical Bureau

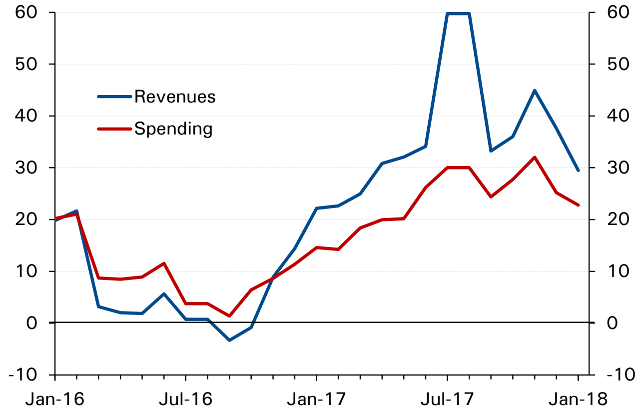
UAE: Following cabinet approval last week, foreigners will be able to own a 100% share of businesses in the UAE by end-2018. Currently, they are not permitted to own more than 49% of UAE firms outside of designated "free zone" areas. The move is part of a wider plan that includes residency visas of up to 10 years to highly skilled expats, including investors and specialists in the scientific, technical, medical and research fields. The new ownership and residency rules are expected to stimulate FDI inflows as well as the domestic real estate market.

Bahrain: Credit default swap (CDS) rates – one bellwether of sovereign risk – spiked to near multi-year highs last week amid a global sell-off of emerging-market debt and growing concerns about Bahrain's fiscal deficit and mounting debt burden. As of the 23rd of May, the CDS on five-year government debt was at 383 bps, up 93 bps year-to-date. Yields on five-year government debt also jumped, to a record high of 7.36% around the same time.

Egypt: Public finance figures for the first seven months of FY2017/18 (starting July) suggest that the modest pace of fiscal adjustment remains broadly on track against a backdrop of robust economic growth and rising tax revenues. Growth in spending eased to a still-high 23% y/y in July-January from a peak of 32% in November. (Chart 5.) Revenue growth remains strong, but also eased to 30% y/y. At EGP218 billion (US$12 billion), the deficit was up 11% on a year earlier, but is still likely to shrink to around 10% of GDP this year from 10.9% in FY2016/17. The IMF just concluded its third review of the Extended Facility Program, indicating that Egypt is heading toward realizing a primary fiscal surplus and thus reducing public debt for the first time in a decade. A disbursement of $2 billion will be made at the conclusion of the review, bolstering further international reserves.

Chart 5: Egypt public finances

(fiscal year-to-date, % y/y)



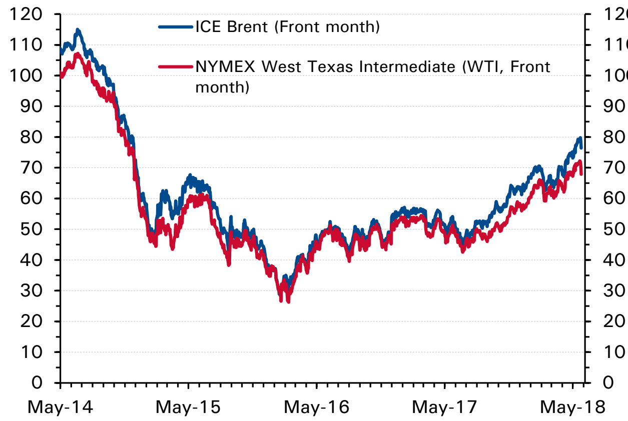
Source: Thomson Reuters Datastream

Markets – oil

Oil prices were pulled down on Friday, settling at $76.4 for Brent and $67.9/bbl for WTI after Saudi oil minister Khaled Al-Falih commented that OPEC+ is "likely" to increase production in the second half of the year to keep prices from rising too high. (Chart 6.) Al-Falih's remarks, which followed a meeting on Friday with his Russian counterpart, Alexander Novak, appear to be the first move in a coordinated play to take the steam out of the oil rally for fear that higher prices would ultimately undermine longer-term oil demand.

Chart 6: Crude oil prices

($/bbl)



Source: Thomson Reuters Datastream

Al-Falih indicated that up to 1 mb/d of additional supply could be released in 2H18 (amid robust oil demand and to compensate for actual Venezuelan and potential Iranian lost barrels) after OPEC concludes its biannual ministerial meeting in June. The announcement triggered a market sell-off that saw Brent decline by almost 3% on Friday and 3% week-on-week, breaking a run of six consecutive weekly gains.

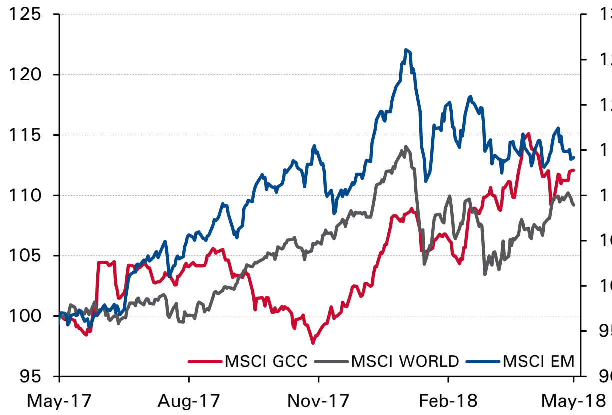
Prices were also under pressure earlier in the week after the EIA revealed a surprise increase in US crude inventories (+5.8 mb to 438 mb) as imports rebounded and refinery runs fell in the w/e 18 May; US crude production also increased (+2 kb/d w/w, +943 kb/d ytd) amid a further rise in the oil rig count.

Markets – equities

Global equities finished the week mixed, but were down overall on renewed political uncertainty in Europe and faltering negotiations with North Korea. The MSCI AC index retreated 0.3% w/w. US markets, however, outperformed, with the S&P and DJI up 0.3% and 0.2% w/w, respectively, benefitting from softening trade rhetoric. Meanwhile, concerns over Italy's new government and the possibility of early elections in Spain dragged the Euro Stoxx 50 1.6% lower, while US-North Korea tensions and the possibility of US tariffs on auto imports pulled the MSCI EM index down 0.4%. (Chart 7.)

Chart 7: Total equity return indices

(rebased, 25 May 2017=100)

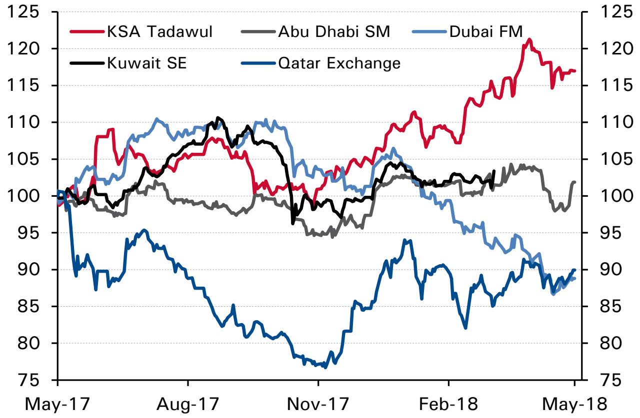


Source: Thomson Reuters Datastream

Regional markets outperformed on solid gains by Abu Dhabi and FDI reform in both Dubai and Qatar. The MSCI GCC index was up 0.7% w/w. Abu Dhabi led the pack (+3.8%), followed by Qatar (+1.8%) and Dubai (1.4%). Foreign investors can now own 100% of a company in Dubai, in addition to obtaining long-term visas. In Qatar, the government passed a similar draft law but went a step further by allowing full ownership in all economic sectors. Saudi coasted, up 0.3% w/w, on lower Ramadan trading and anticipation of the MSCI upgrade. Kuwait's all-share index was down 1.5% w/w. (Chart 8.)

Chart 8: GCC equity markets

(rebased, 25 May 2017=100)



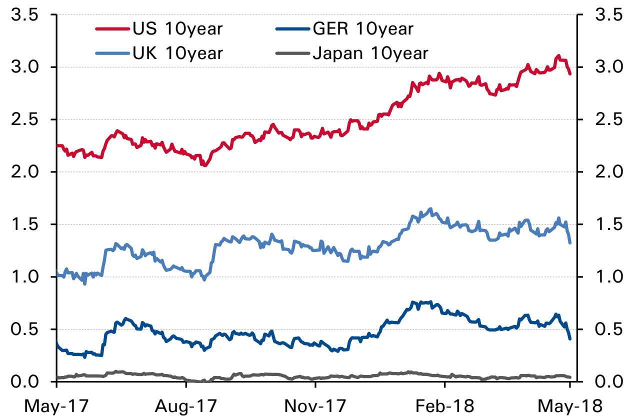
Source: Thomson Reuters Datastream

Markets – fixed income

Geopolitical jitters, political uncertainty, and softening growth pressured international benchmark yields lower. US 10-year yields and 10-year Bund yields were down 13 and 17 bps, respectively. (Chart 9.) In the GCC, most sovereign benchmark yields followed US yields lower, shedding up to 20 bps in the case of Saudi Arabia's 2023.

Chart 9: Global bond yields

(%)



Source: Thomson Reuters Datastream

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