Eurozone GDP grows 3.2% in Q3, oil prices retreat some, US House takes a step forward on tax reform

Key market indicators

Stock markets	Index	Change (%) weekly	YTD
Regional			
Abu Dhabi SM	4,328	-1.11	-4.81
Bahrain ASI	1,270	0.18	4.05
Dubai FM	3,460	0.30	-2.00
Egypt EGX 30	13,847	-3.50	12.17
S&P GCC 40	990	-0.48	-14.27
Kuwait SE	6,309	0.81	9.76
KSA Tadawul	6,913	-0.59	-4.12
Muscat SM 30	5,106	1.00	-11.71
Qatar Exchange	7,826	-0.76	-25.02
International			
CSI 300	4,121	0.22	24.50
DAX	12,994	-1.02	13.18
DJIA	23,358	-0.27	18.19
Eurostoxx 50	3,547	-1.29	7.81
FTSE 100	7,381	-0.70	3.33
Nikkei 225	22,397	-1.25	17.17
S&P 500	2,579	-0.13	15.19

Commodities	$/unit	Change (%) weekly	YTD
Brent crude	62.7	-1.26	10.38
KEC	58.4	-3.52	12.60
WTI	56.6	-0.33	5.27
Gold	1295.8	1.84	12.68

Exchange rates	Rate	Change (%) weekly	YTD
KWD per USD	0.302	-0.18	-1.21
KWD per EUR	0.351	0.00	10.28
USD per EUR	1.179	1.11	12.18
JPY per USD	112.070	-1.29	-4.11
GBP per USD	1.321	0.17	7.09
EGP per USD	17.590	-0.28	-2.28

Interbank rates	%	Change (bps) weekly	YTD
Bhibor - 3 month	2.57	1.5	46.5
Kibor - 3 month	1.75	-6.3	31.3
Qibor - 3 month	2.44	-1.3	65.6
Eibor - 3 month	1.61	1.4	13.8
Saibor - 3 month	1.81	1.3	-22.1
Libor - 3 month	1.44	2.3	43.8

Bond yields	%	Change (bps) weekly	YTD
Regional			
Abu Dhabi 2022	2.81	13.9	n/a
Dubai 2022	3.03	-0.5	-26.4
Qatar 2022	3.18	-10.1	24.4
Kuwait 2022	2.75	1.9	n/a
Saudi Arabia 2023	3.13	-10.3	n/a
International			
UST 10 Year	2.35	-4.6	-7.8
Bunds 10 Year	0.36	-4.8	15.7
Gilts 10 Year	1.30	-4.5	5.6
JGB 10 Year	0.04	-0.4	-1.3

Source: Thomson Reuters Datastream; as of Friday's close 19/11/2017

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Overview

Continued uncertainty over US tax reform, disappointing earnings results, concern over valuations and the shadow cast by the Russia probe on the Trump administration saw US stocks edge lower following the previous week's all-time highs. By contrast, strong German Q3 GDP figures (3.2% q/q annualized) added to recent buoyant news from the eurozone. This combination helped push the trade-weighted US dollar index to its lowest this month, and now down 7% year-on-year.

Following a 5-week bull-run, oil prices lost momentum last week, with Brent edging back down to $62.7/bbl from a peak of $64 a week earlier. One catalyst was the IEA's bearish new long-term projections, which forecast an "unprecedented" surge in US production to 2025, alongside slower demand growth. With an extension to OPEC's current production cuts beyond 1Q18 now factored in, the group could yet look to seize back the initiative by announcing still deeper production cuts when it meets at the end of November.

It was a relatively quiet week in the Gulf region, with investors still absorbing the implications of the Saudi corruption clampdown. One notable economic release was the decline in GDP in Abu Dhabi reported for Q2 of 0.9% y/y – the first outright fall in output of the current cycle, albeit driven mostly by a 1.9% drop in oil output. The emirate accounts for more than half of the UAE economy and – despite its vast oil wealth – figures point to cuts in public sector spending for several quarters in real terms. Non-oil GDP was virtually stagnant in 1H17.

International macroeconomics

US: The inflation data was slightly more robust in October, though this did little to dispel concerns of soft inflation momentum. Core inflation accelerated slightly in October to 1.8% y/y, with the month seeing a moderate pick-up in price growth. (Chart 1.) The moderate gain comes amid months of milder pressure on the index and on key components. Producer prices were robust in October; core PPI inflation rose to 2.4% y/y.

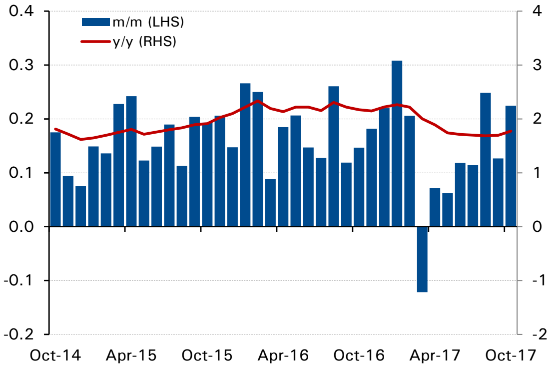
Other economic data were robust, indicating continued strength in economic activity. Retail sales rose by 0.2% in October, on the heels of a strong post-Hurricane month in September. Less volatile sales excluding autos and gasoline were also healthy. The Philadelphia Fed index eased in October but remained strong at 22.7. The industrial production index saw a healthy jump in October, with the key manufacturing component seeing a solid 1.3% monthly gain. Housing starts were also strong.

Tax reform, which promises a healthy fiscal stimulus, made some progress with the House passing its more ambitious version of the bill last week. Still, the Republicans could be short of the 50 votes needed in the Senate down the road, after some members came out against the legislation.

Eurozone: The eurozone's 3Q17 flash growth was confirmed at 2.5% y/y, re-affirming the bloc's resurgence on the wings of sturdy core economies. German GDP was revised higher to an annualized 3.2% q/q (2.4% previously); Spain grew by 3.2% and Italy and France both by 2.0%.

Chart 1: US core inflation

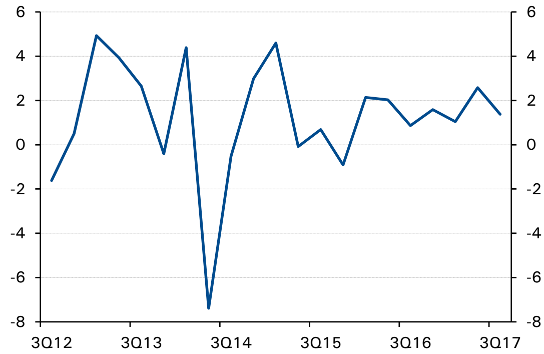
(%)



Source: U.S. Bureau of Labor Statistics

Chart 2: Japan real GDP

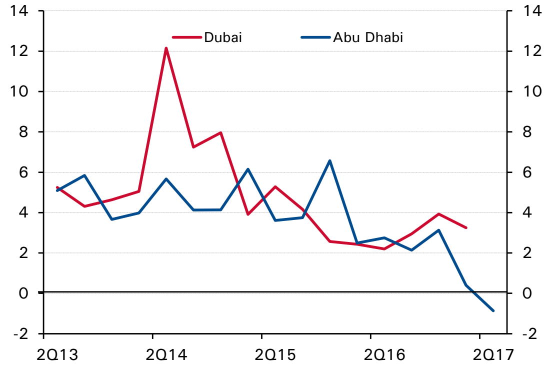
(% y/y, annualized)



Source: Japan Cabinet Office

Chart 3: Dubai and Abu Dhabi real GDP

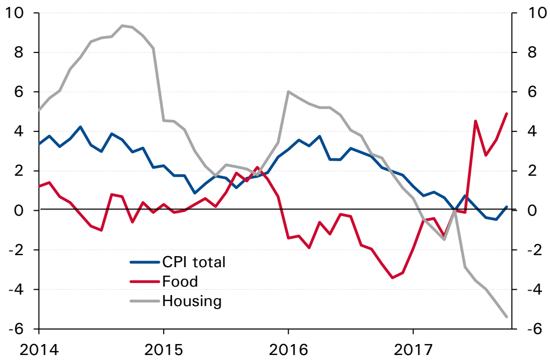
(% y/y)



Source: Dubai Statistics Center, Statistics Centre – Abu Dhabi

Chart 4: Qatar consumer price inflation

(% y/y)



Source: MDPS

In Germany, economic optimism remained firm with the ZEW current conditions index coming in above consensus at 88.8 and business expectations rising to 18.7, its third consecutive increase.

UK: PM Theresa May acquiesced to pro-European MPs' demands to have a final say on the Brexit deal with the EU. Parliament will be allowed to vote on both the exit deal and on the bill that would enshrine the deal into law. As the government faces possible defeat on the key withdrawal bill currently being scrutinized, the concession was symbolic. The government insists, however, that a potential rejection of the final agreement by MPs would not prevent Britain from leaving the block; rather, the country would just exit the EU without any deal.

Inflation held at 3.0% y/y in October for the second month in a row. However, while the headline rate was steady, food prices increased by 4% y/y in October, their fastest pace in four years and pressured by currency weakness.

China: October data signal cooling Chinese activity. Industrial production registered a slightly lower-than-expected growth of 6.2% y/y, and fixed asset investment also witnessed slower growth of 7.3% y/y in the first ten months of this year. The property market followed the trend, with property investment growth ytd easing to 7.8% y/y. Finally, retail sales cooled to 10% y/y in October.

Japan: Japan's annualized real GDP growth eased from a two-year high of 2.6% in 2Q17 to a still decent 1.4% in 3Q17, as the continued strength in export growth offset some of the weakness in consumer spending. (Chart 2.) Exports have been buoyed by the ongoing weakness in the yen and an improving global environment, and are expected to support the economy.

GCC & regional macroeconomics

Kuwait: The IMF revised down its outlook for Kuwait's non-oil growth in a statement concluding its Article IV visit to the country. Non-oil growth is now seen at 2.5% in 2017, down from 3.5%. This revision appears largely driven by the weaker official GDP figures for 2015 and 2016 released back in July. Though the IMF continues to see non-oil growth improving, it projects a more gradual acceleration toward 4% by 2021, driven by capital spending and "improved confidence".

Earnings of Kuwaiti listed corporates rose by 16% y/y during the first nine months of the year. 157 listed companies out of 167 have reported profits of KD 1.5 billion, with over two-third of the companies being profitable. The banking sector was the highest contributor to growth, with sector profits reaching KD 595 million and growing by 17% y/y.

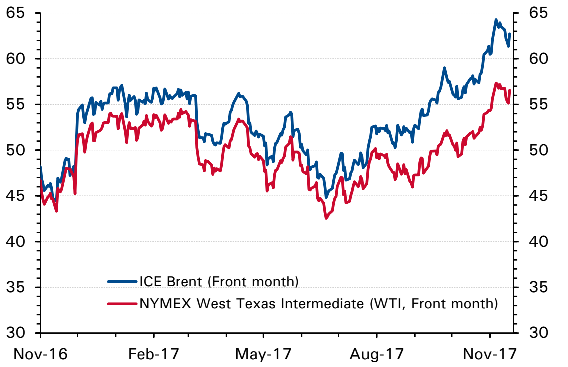
Saudi Arabia: The Capital Markets Authority (CMA) suspended trading activity for the accounts of individuals under investigation in the government's anti-corruption drive. While this did not affect the stock market as much as expected, there is increasing concern, however, that capital outflows could accelerate should the crackdown drag on.

Japan's SoftBank Group plans to invest almost $25 billion in the kingdom over the next three to four years, of which $15 billion will be directed towards the mega-city project NEOM (through the SoftBank Vision Fund) and as much as $10 billion will be invested in the Saudi Electricity Company. Along with SoftBank, other investors in the Vision Fund include Abu Dhabi's sovereign wealth fund, Apple, and Foxconn.

UAE: Real GDP in Abu Dhabi fell by 0.9% y/y in 2Q17, mainly on the back

Chart 5: Benchmark crude oil prices

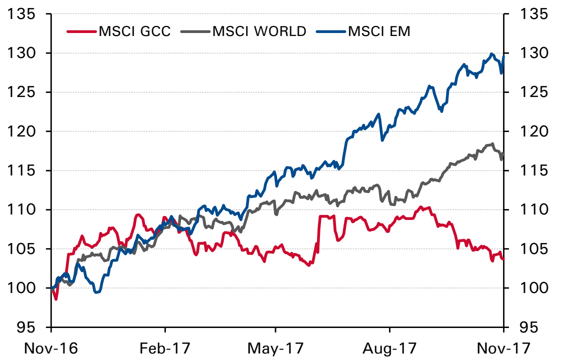
($/bbl)



Source: Thomson Reuters Datastream

Chart 6: Total return indices

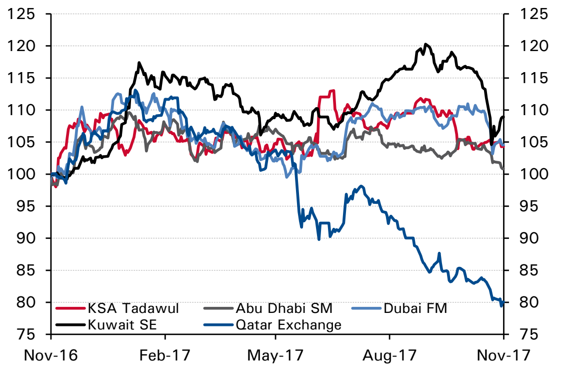
(rebased, 17 November 2016=100)



Source: Thomson Reuters Datastream

Chart 7: GCC markets

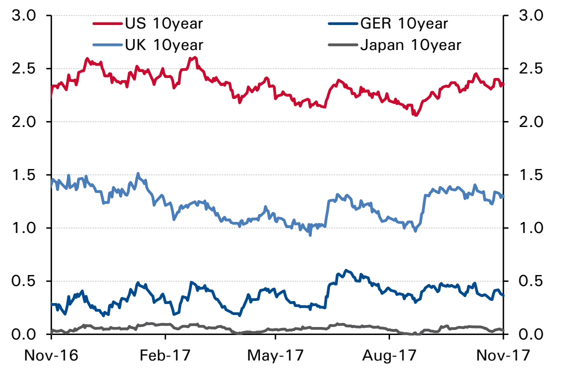
(rebased, 17 November 2016=100)



Source: Thomson Reuters Datastream

Chart 8: Global benchmark yields

(%)



Source: Thomson Reuters Datastream

of a 1.9% y/y drop in oil activity. (Chart 3.) Growth in non-oil activity was flat during the same period, weighed down by fiscal consolidation efforts. However, with fiscal consolidation set to ease and infrastructure activity projected to gather steam in 2H17, non-oil GDP growth is expected to gradually improve into 2018. Real GDP growth in Dubai has so far fared better. Latest figures showed growth in Dubai at 3.2% y/y in 1Q17. This should help offset some of the weakness in Abu Dhabi.

Qatar: CPI data for October generally revealed a return to upwards, albeit limited, price pressures. Inflation crept up to 0.2% y/y after two successive months in negative territory. (Chart 4.) However, the rise was boosted by a base effect; prices had fallen significantly a year earlier.

In the detail, the most eye-catching figure was a further fall in the housing component, to -5.4% y/y from -4.7% in September. This segment has recorded monthly falls in 9 of the past 10 months, reaffirming that the property market is going through an extended downward adjustment, which may have intensified since the diplomatic dispute began in June. Elsewhere, our measure of 'core' inflation, which excludes housing and food, picked up noticeably to 0.8% y/y from 0.1%, but the figures still suggest that inflation will average 0.5% for 2017, rising to 2.5% next year.

Oman: Omantel purchased 12.1% of Zain Group for $1.35 billion ($2.58/share). The Omani telecom company now owns 21.9% of Zain, the second largest share following Kuwait's sovereign wealth fund. No change in executive management is expected, but Omantel will hold five of the eight board seats.

Egypt: The CBE decided to keep policy rates unchanged at its monetary policy meeting. The CBE feels that current rates are appropriate to bring inflation down to the 13% target in 2018 and below 10% beyond that.

The CBE closed a $3.1 billion one-year loan agreement with foreign banks, rolling over a maturing $2 billion facility and borrowing a net $1.1 billion. The repurchase agreement will help meet around $14 billion in foreign debt repayments due in 2018.

Markets – oil

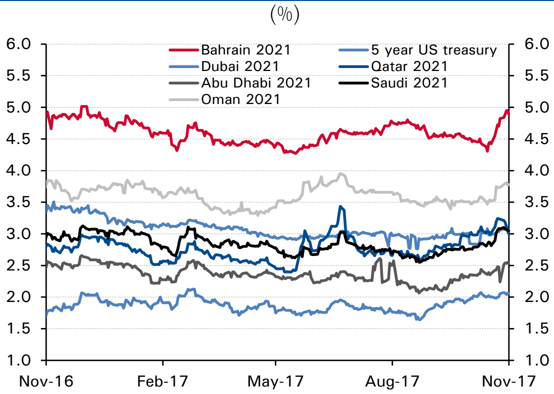
Oil prices posted their first w/w decline in almost five weeks on Friday, with Brent closing down 1.3% to $62.7/bbl and WTI down 0.3% to $56.5/bbl. (Chart 5.) Prices were under pressure for most of the week on reports that Russia was hesitant to commit just yet to an extension of its output cut agreement with OPEC and preferred to wait until March 2018 before making a decision. In response, Saudi Arabia's minister of energy moved to reassure the markets that an OPEC extension was likely, managing to lift prices a little on Friday.

Markets also responded negatively to the latest US petroleum data, which showed crude production hitting another shale-era high last week. At 9.65 mb/d, output is just 4% off the US all-time high of 10.04 mb/d of 1970.

Indeed, in its just-released World Investment Report 2040, the IEA predicts that US shale output will surge by a further 34% to 9 mb/d by 2025, with total US output crude and refined products output likely to reach 16.9 mb/d by 2025. These figures will make the US the "undisputed global oil and gas leader for decades to come", surpassing Saudi Arabia and Russia, the IEA's Executive Director, Fatih Birol, remarked last week.

US shale output will, however, begin to decline after the middle of the next decade, which will see OPEC increasing its market share of the total crude

Chart 9: GCC yields



Source: Thomson Reuters Datastream

and petroleum liquids market to 46% by 2040 from the current 43%.

Markets – equities

All markets were mostly down, as the focus returned to macroeconomic developments rather than earnings. The MSCI World All Country index closed down 0.4%. (Chart 6.) US equities trended lower most of the week over doubts surrounding tax reform and on the lower commodity prices. The S&P 500 and DJIA ended the week slightly down at 0.1% and 0.3%, respectively. European equities tracked US equities' losses, pushing the Euro Stoxx 50 down 1.3% on the week. FTSE 100 index was down 0.7% as UK employment data showed real wages down. Emerging market (EM) equities were up with the MSCI EM improving 0.3% following the global market rebound on Friday. Chinese stocks lagged behind as disappointing Chinese data (industrial output, home sales) raised slowdown concerns.

GCC markets posted mixed results this week, in line with international markets. The MSCI GCC index closed the week slightly down 0.5%. (Chart 7.) Boursa Kuwait was up 1.3% on the week, erasing the losses incurred since the beginning of the month. Qatar's market continues to feel the heat from the sanctions, with the index down 0.8%. Saudi's Tadawul was down 0.6%, with the decline limited by buying from state-linked funds.

Markets – fixed income

Investors went to risk-off mode, following uncertainty over US tax reform, Brexit, and weaker commodity prices. This supported bonds. Some hawkish comments by the ECB, passage of US tax legislation in the US House, and strong US data were not really a factor. 10-year US Treasury and German Bund yields were both down 5 bps on-the-week, to settle at 2.35% and 0.36%, respectively. (Chart 8.)

Meanwhile, an imminent rate hike is causing the US yield curve to flatten, as current conditions continue to improve but inflation expectations remain stubbornly low. Markets are now expecting with near certainty (97%) a rate hike in December. This caused the 2-10 year spread in yields to tighten to 62 bps, the closest since 2007.

Yields for Saudi and Qatar were down on the week, while Abu Dhabi re-priced. Debt maturing in 5 years for the former two dropped in yields by 10 bps each. Lower prices, following last week's developments, may have enticed some buyers in. In Abu Dhabi, yields on 2022 bonds were up 14 bps, to settle at 2.81%. An oil price over $60/bbl helped keep yields on Kuwaiti, Bahraini and Dubai 5-year debt steady, while Omani 5-year debt shaved 7 bps. (Chart 9.)

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