International scene

Steady world outlook, Macron election soothes EU concerns

> Elias Bikhazi
Group Chief Economist
+965 2259 5364, eliasb@nbk.com

Markets appear in steady mode these days. Most markets are taking a breather after run-ups late last year, especially following the Trump election in November. The leading markets seem to be in trading ranges now or just stalled near highs, awaiting some catalyst event or a change in economic conditions. We are still up 6-7% ytd on US equities, and close to 10-11% on European and emerging market stocks; GCC markets are lagging, pressured in part by struggling oil prices. Interest rates are still up on the year (US 10-year at 2.3%) but off their recent highs seen after the December 2016 Fed hike. The dollar, too, had a run-up in 2016, but is now actually down on the year against the major currencies (EUR, JPY), even more now after the French election of pro-EU president Macron.

What gives? Not much. Realism set in regarding the ability to pass (quickly) massive legislation in the US and fears of populists coming to power in the EU receded. On the Trump agenda, good and (equity) positive things are still expected: the awaited significant deregulation is occurring (energy, finance), the feared trade wars are not happening; but the wild balloon of massive and immediate tax reform, which pushed the Dow Jones Industrials Index over 21,000 earlier, lost some of its buoyancy for a time.

In Europe, the populists are still popular, along with the Euroskeptics. The Dutch and French populists (Wilder and Le Pen and others) did well in their elections, but not well enough to reach power and thus scare the markets. We therefore saw the euro gaining ground and EU interest rates rise a bit as risk-off trades were unwound. Meanwhile, concerns about Syria and North Korea, which had popped up on the radar screen, remain thankfully contained for the time being.

On economic performance, the major economies have spewed soothing data primarily, more or less in line with moderate growth, as per say the IMF's recent update for world growth of 3.5%. Noticeably, the IMF's April report included an upward revision (a slight 0.1%) to that number. Upward revisions are significant after years of consistent downward revisions at every turn. The change in direction basically means that surprises are finally coming in on the upside, usually a bullish indicator. This view is widely shared, though the assessments of the risks vary somewhat, especially regarding politics and central bank policies (potential end of QE in the EU next year, Fed reducing its balance sheet...).

The focus is now again on the US, where Trump and the Republicans are trying to pass radical tax reform in a very contentious political environment. There are also difficult issues related to "paying" for those tax cuts, in other words the deficit/debt implications. The broad lines of tax reform are: a reduction in the corporate tax rate from 35% to 15%, a tax simplification and tax cut for individuals whereby most deductions would disappear, the standard deduction would double, and tax brackets would go from seven (with the top one taxed at 40%) to only three brackets taxed: 15, 25, and 35%.

How much of the US tax plan is realized, and its actual timing will have significant bearing on the US outlook. The current 2.0% or 2.0%-plus view for 2017-2018 would start moving up if President Trump gets most of his tax plan, moving closer to 3.0% but not much higher in the near term. One concern, which we share, is that the financial markets are a bit overly optimistic as to content and timing of the proposed tax plan.

In Europe, markets are breathing easier, and now sigh in relief after the French election of centrist Macron for president. Though heavily favored before the election, the markets wanted to see the actual results of the election, having been burnt by Brexit and Trump before. The euro and European equities ran up a bit following the results.

Macron is of course pro-EU and for free trade but is more nuanced as he is seeking some protections for Europe's trade with outside partners. His positions are not very clear at this point, and his newly formed party has zero MPs in parliament. So, he will have to rely on the upcoming June election to broaden his mandate and/or work with the mainstream parties to be able to govern. Macron's election, though not market-disruptive, will still yield policy and implementation questions ahead, though not of the Frexit kind.

In the meantime, Brexit negotiations are starting between the UK and the EU, and PM Theresa May has called a June election, which is likely to increase her working majority in parliament from 17 seats to perhaps 100. A stronger government and PM were viewed positively for the GBP because they would strengthen the PM's hand and potentially move things in surer fashion; but, they could also perhaps result in a middle-of-the-road Brexit as the PM could more easily placate her hard-liners.

The Fed just ended its May meeting with no change to policy, US rates are expected to rise in June and December of this year, as data remains in line with the Fed's moderate outlook view. Recent Q1 GDP data was weaker than expected at 0.7% (q/q ann.) while the April nonfarm payroll report showed a strong 211K new jobs. These numbers do not derail things, however, as GDP was distorted by one-time factors. GDP growth is still running at 1.9% y/y, the underlying pace in our view. Furthermore, other data, such as PMIs, home sales, and sentiment indicators are all pointing to a steady moderate outlook.

Upcoming US rate hikes will of course have repercussions for GCC interest rates, where currencies are tied to the USD and where oil prices are also keenly watched. The latter have been steady in a range under $55 pb (Brent) before slipping under $50 recently. Talk of extending the OPEC-non-OPEC production cut agreement to the second half of this year is supporting prices, while reports of rising US production and of high inventory levels are pressuring prices lower. Therefore, the GCC countries are plowing along with reforms and consolidation, while their finances are looking somewhat better with the higher oil prices this year. That is easing some of the pressure on fiscality and liquidity. At the same time, most countries are carrying on with their debt issuance programs (domestic and international), the latest being Kuwait's successful issuance of an $8 billion international bond (5 and 10-year maturities).

Head Office

Kuwait
National Bank of Kuwait SAKP
Abdullah Al-Ahmed Street
P.O. Box 95, Safat 13001
Kuwait City, Kuwait
Tel: +965 2242 2011
Fax: +965 2259 5804
Telex: 22043-22451 NATBANK
www.nbk.com

International Network

Bahrain
National Bank of Kuwait SAKP
Zain Branch
Zain Tower, Building 401, Road 2806
Seef Area 428, P. O. Box 5290, Manama
Kingdom of Bahrain
Tel: +973 17 155 555
Fax: +973 17 104 860

National Bank of Kuwait SAKP
Bahrain Head Office
GB Corp Tower
Block 346, Road 4626
Building 1411
P.O. Box 5290, Manama
Kingdom of Bahrain
Tel: +973 17 155 555
Fax: +973 17 104 860

United Arab Emirates
National Bank of Kuwait SAKP
Dubai Branch
Latifa Tower, Sheikh Zayed Road
Next to Crown Plaza
P.O.Box 9293, Dubai, U.A.E
Tel: +971 4 3161600
Fax: +971 4 3888588

National Bank of Kuwait SAKP
Abu Dhabi Branch
Sheikh Rashed Bin Saeed
Al Maktoum, (Old Airport Road)
P.O.Box 113567,Abu Dhabi, U.A.E
Tel: +971 2 4199 555
Fax: +971 2 2222 477

Saudi Arabia
National Bank of Kuwait SAKP
Jeddah Branch
Al Khalidiah District,
Al Mukmal Tower, Jeddah
P.O Box: 15385 Jeddah 21444
Kingdom of Saudi Arabia
Tel: +966 2 603 6300
Fax: +966 2 603 6318

Jordan
National Bank of Kuwait SAKP
Amman Branch
Shareef Abdul Hamid Sharaf St
P.O. Box 941297, Shmeisani,
Amman 11194, Jordan
Tel: +962 6 580 0400
Fax: +962 6 580 0441

Lebanon
National Bank of Kuwait
(Lebanon) SAL
BAC Building, Justinien Street, Sanayeh
P.O. Box 11-5727, Riad El-Solh
Beirut 1107 2200, Lebanon
Tel: +961 1 759700
Fax: +961 1 747866

Iraq
Credit Bank of Iraq
Street 9, Building 187
Sadoon Street, District 102
P.O. Box 3420, Baghdad, Iraq
Tel: +964 1 7182198/7191944
+964 1 7188406/7171673
Fax: +964 1 7170156

Egypt
National Bank of Kuwait - Egypt
Plot 155, City Center, First Sector
5th Settlement, New Cairo
Egypt
Tel: +20 2 26149300
Fax: +20 2 26133978

United States of America
National Bank of Kuwait SAKP
New York Branch
299 Park Avenue
New York, NY 10171
USA
Tel: +1 212 303 9800
Fax: +1 212 319 8269

United Kingdom
National Bank of Kuwait
(International) Plc
Head Office
13 George Street
London W1U 3QJ
UK
Tel: +44 20 7224 2277
Fax: +44 20 7224 2101

National Bank of Kuwait
(International) Plc
Portman Square Branch
7 Portman Square
London W1H 6NA, UK
Tel: +44 20 7224 2277
Fax: +44 20 7486 3877

France
National Bank of Kuwait
(International) Plc
Paris Branch
90 Avenue des Champs-Elysees
75008 Paris
France
Tel: +33 1 5659 8600
Fax: +33 1 5659 8623

Singapore
National Bank of Kuwait SAKP
Singapore Branch
9 Raffles Place # 44-01
Republic Plaza
Singapore 048619
Tel: +65 6222 5348
Fax: +65 6224 5438

China
National Bank of Kuwait SAKP
Shanghai Representative Office
Suite 1003, 10th Floor, Azia Center
1233 Lujiazui Ring Road
Shanghai 200120, China
Tel: +86 21 6888 1092
Fax: +86 21 5047 1011

NBK Capital

Kuwait
NBK Capital
38th Floor, Arraya II Building, Block 6
Shuhada'a street, Sharq
PO Box 4950, Safat, 13050
Kuwait
Tel: +965 2224 6900
Fax: +965 2224 6904 / 5

United Arab Emirates
NBK Capital Limited - UAE
Precinct Building 3, Office 404
Dubai International Financial Center
Sheikh Zayed Road
P.O. Box 506506, Dubai
UAE
Tel: +971 4 365 2800
Fax: +971 4 365 2805

Associates

Turkey
Turkish Bank
Valikonagl CAD. 7
Nisantasi, P.O. Box. 34371
Istanbul, Turkey
Tel: +90 212 373 6373
Fax: +90 212 225 0353