Strong US labor market and easing tensions in Italy lift markets, but trade war concerns intensify

Key market indicators

Stock markets	Index	Change (%) weekly	YTD
Regional			
Abu Dhabi (ADI)	4,605	0.09	4.70
Bahrain (ASI)	1,266	0.21	-4.95
Dubai (DFMGI)	2,964	0.33	-12.05
Egypt (EGX 30)	16,415	-1.32	9.29
GCC (S&P GCC 40)	1,004	0.09	1.99
Kuwait (All Share Index)	4,736	0.09	n/a
KSA (TASI)	8,161	1.53	12.94
Oman (MSM 30)	4,607	0.93	-9.66
Qatar (QE Index)	8,881	-1.86	4.19
International			
CSI 300	3,771	-1.20	-6.46
DAX	12,724	-1.65	-1.50
DJIA	24,635	-0.48	-0.34
Euro Stoxx 50	3,454	-1.76	-1.44
FTSE 100	7,702	-0.37	0.18
Nikkei 225	22,171	-1.24	-2.61
S&P 500	2,735	0.49	2.28

Bond yields	%	Change (bps) weekly	YTD
Regional			
Abu Dhabi 2022	3.58	1.8	63.3
Dubai 2022	4.01	1.1	86.8
Qatar 2022	3.89	-1.2	81.3
Kuwait 2022	3.52	2.8	71.3
Saudi Arabia 2023	3.83	-3.2	61.3
International			
UST 10 Year	2.90	-4.0	48.4
Bunds 10 Year	0.38	-3.1	-4.7
Gilts 10 Year	1.28	-4.2	9.4
JGB 10 Year	0.04	0.2	-0.6

3m interbank rates	%	Change (bps) weekly	YTD
Bhibor	3.20	0.0	47.5
Kibor	1.94	0.0	6.3
Qibor	2.63	0.0	-10.9
Eibor	2.56	8.6	75.9
Saibor	2.44	0.5	54.1
Libor	2.32	0.2	62.7

Exchange rates	Rate	Change (%) weekly	YTD
KWD per USD	0.302	0.02	0.27
KWD per EUR	0.353	0.03	-0.56
USD per EUR	1.166	0.09	-2.80
JPY per USD	109.5	0.14	-2.79
GBP per USD	1.335	0.30	-1.22
EGP per USD	17.85	-0.11	0.68

Commodities	$/unit	Change (%) weekly	YTD
Brent crude	76.8	0.46	14.83
KEC	71.9	-4.86	13.15
WTI	65.8	-3.05	8.92
Gold	1294.8	-0.65	-0.88

Source: Thomson Reuters Datastream; as of Friday's close 1/6/2018

Overview

The news that US jobs growth picked up in May and unemployment fell to an 18-year low gave markets an end-week boost, with the S&P 500 rising 1.1% on Friday, benchmark US and European bond yields edging up and the US dollar slightly firmer. Markets also cheered an easing in political tensions in both Italy and Spain, with the former agreeing a new coalition government that, although anti-establishment in nature, reduces the risk of fresh elections. Looking forward, these positive developments may be offset by trade disputes, with EU officials vowing to respond to the ending of a waver that will see the US apply tariffs on imports of steel and aluminum from Europe and North America, ratcheting up trade war fears. Other G7 countries condemned the US's move.

The price of Brent crude edged up 0.5% following the previous week's sharp decline, finishing at just below $77/bbl. The market continues to digest the potential for an easing in OPEC-led supply cuts through 2018, though mid-week reports suggesting that existing production might be raised only gradually this year saw crude recover its earlier losses. Meanwhile however, the price of the US benchmark WTI fell 3% w/w to $66, its largest discount to Brent in over three years as surging US shale production continued to meet pipeline capacity constraints, leaving an excess of US crude on inland markets.

Regionally, the run-up in oil prices this year has improved the fiscal and external current accounts positions and led to a surge in international reserves. For Bahrain though, a small oil producer, the IMF has called for the government to urgently implement a 'credibly large fiscal adjustment' in order to address a still-large fiscal deficit, rising debt and low financial reserves.

International macroeconomics

USA: As expected, GDP growth in 1Q18 was revised down a touch to an annualized pace of 2.2% from 2.3% before on the back of slightly softer consumer spending and weaker inventories. Current expectations are for growth rebound closer to the 3% mark in Q2. But Friday's news from the labor market was more upbeat, with employment surging 223,000 in May – well above expectations – and unemployment falling to an 18-year low of 3.8%. (Chart 1.) Earnings growth edged up to 2.7%

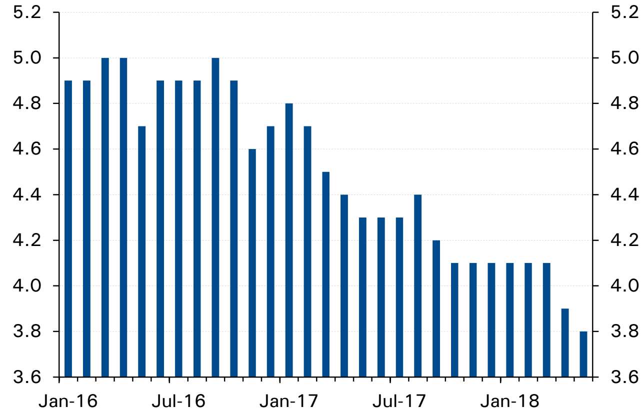
y/y from 2.6% in April and the report was seen as cementing the case for a Fed rate hike later this month.

Data from earlier in the week also revealed a consumer sector in decent shape. Consumer spending rose a solid 0.6% m/m in April, though the closely-watched core PCE inflation measure was unchanged at 1.8% y/y. Meanwhile, the Conference Board's gauge of consumer confidence edged up to 128 in May from 126 in April – close to recent 17-year highs – and the Case-Schiller house price index rose a solid 0.5% m/m in March, leaving the annual rate unchanged at 6.8% y/y.

Key surveys of manufacturing activity for May were also very strong, with the PMI broadly unchanged at 56.4 while the ISM gauge rose to 58.7 from 57.3 in April. Both surveys signaled strong order books, rising backlogs, delivery delays, and also hinted at rising selling prices reflecting capacity constraints in the sector.

Chart 1: US unemployment rate

(%)



Source: Thomson Reuters Datastream

Eurozone: Politics remained at the forefront in the Eurozone. A turbulent week for Italy ended with a sigh of relief, with Italy's president accepting the populist coalition's government following staunch opposition earlier in the week. Meanwhile, Spain's prime minister was defeated in a no-confidence vote sparked by a campaign scandal, and was forced to step down.

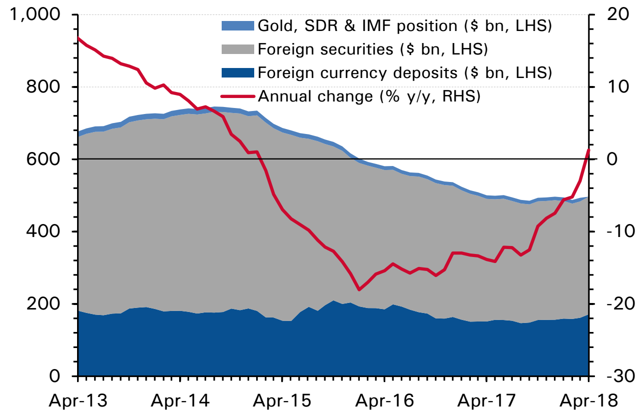
Eurozone data was mixed. Economic sentiment was little changed, edging down 0.2 m/m to 112.5. Weakness in industry and services was offset by increases in retail and construction. Headline inflation, on the other hand, increased to 1.9% in May from 1.6% in April on higher oil prices, and the core rate climbed to 1.1%. The manufacturing PMI fell for a fifth consecutive month, on weaker external demand.

GCC & regional macroeconomics

Kuwait: The trade surplus picked up in 1Q18 by 19% q/q and 43% y/y, reaching KD 2.3 billion from KD1.9 billion in 4Q17. The strong improvement occurred due to a recovery in both oil and non-oil exports. Oil exports reached KD 4.4 billion in the first quarter, up 18.7% y/y, helped by a 23% rise in the price of Kuwait Export Crude. Non-oil exports jumped 26% y/y to KD 372 million. Import growth was moderate at 3.4% y/y.

Saudi Arabia: Saudi foreign reserves in April topped $500 billion for the first time since June 2017. Thanks to higher oil prices which have led to the return of current account surpluses, official reserves have grown for two consecutive months (+$13.2bn in April) to reach $506.6 billion; annual growth, at 1.3% y/y, also turned positive for the first time in more than three years. (Chart 2.)

Chart 2: Saudi foreign reserve assets

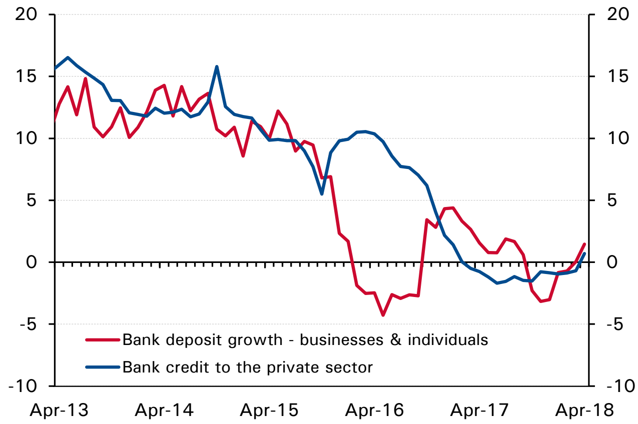


Source: SAMA

However, both private sector credit and deposit growth remain lackluster at 0.7% y/y and 1.5% y/y in April, respectively. (Chart 3.)

Chart 3: Saudi private sector credit & deposits

(% y/y)



Source: SAMA

These figures are still quite a way below rates of growth in the pre-2014 oil downturn period. In the case of bank credit, borrowing by manufacturing, commercial and construction firms remains especially weak.

Bahrain: S&P affirmed Bahrain's long and short-term foreign and local currency sovereign ratings at B+/B and maintained its stable outlook for Bahrain on the basis of the kingdom's continued access to foreign capital. Financial assistance from regional allies and access to international funding, through sovereign debt issuances, for example, have been instrumental in helping Bahrain to replenish its reserves (which fell to the equivalent of a mere 1.4 months of imports earlier this year).

Nonetheless, following the conclusion of its mission in Bahrain, the IMF reiterated the need for fiscal reform to reduce its stubbornly-large fiscal deficit and to support the currency. The government has reportedly said that it would reduce its fiscal deficit to 11% of GDP in 2018 from around 14% in 2017. The IMF expects the economy to grow 3.2% in 2018, led by a recovery in oil production, GCC-funded infrastructure projects and an expansion in refinery and aluminum capacity.

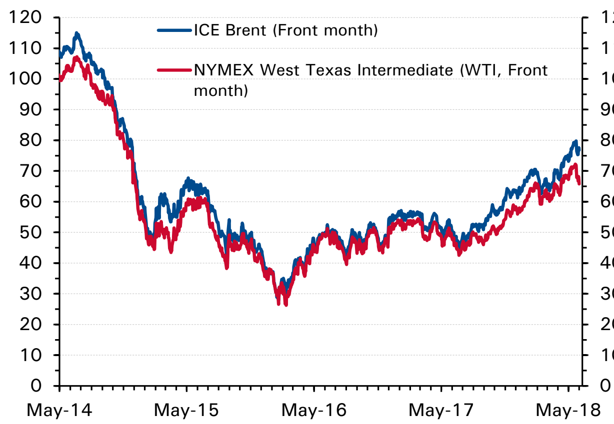
Turkey: In a bid to stem the steep decline in the Turkish lira, Turkey's central bank held an emergency meeting last week during which it raised its interest rates by 300 bps and announced that it would return to using the one-week repo rate as its benchmark interest rate, to help simplify and improve the predictability of its policy. The lira gained some 2% following the meeting but pared its gains by the end of the week, as concerns about Turkey's double-digit inflation rate (data due on Monday) weighed on sentiment.

Markets – oil

Oil prices closed last week with the two major crude benchmarks pursuing different trajectories. While Brent closed up 0.5% w/w at $76.8/bbl, WTI, the US marker, fell 3% to $65.8/bbl – the second consecutive weekly fall and the marker's lowest level in a month. (Chart 4.)

Chart 4: Crude oil prices

($/bbl)



Source: Thomson Reuters Datastream

Oil prices have generally been on the back foot since Saudi Arabia and Russia indicated in late May that they could open the taps as soon as the end of this month (after the OPEC meeting on June 22) the divergence in the two crude benchmarks is a reflection of local US oil market dynamics. Last Friday, the spread between the two markers reached $11/bbl – the highest since 2015 – as surging US crude output (+44 kb/d to 10.77 mb/d in w/e 25 May) is swamping local transport and storage infrastructure, overloading pipeline capacities.

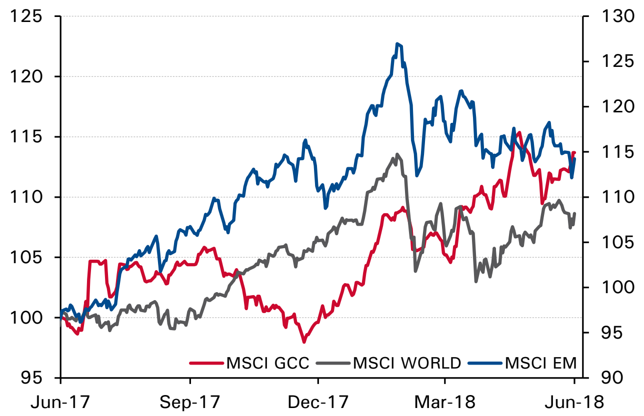
Markets – equities

Global equity markets were driven by the political uncertainty that surrounded Italy, while trade disputes also weighed. The MSCI AC index declined 0.1% w/w.

US equities sold-off on Tuesday before almost recovering completely on Wednesday following some easing in political tensions in Italy, but protectionist trade rhetoric from Washington dampened the recovery. The S&P 500 was up 0.5%, while the DJI declined by 0.5%. Europe's Stoxx 50 pared back some losses following the Italian resolution, but was held back by the ousting of Spain's PM. The index was down 1.8% w/w. Meanwhile, trade war concerns kept emerging markets on edge, with the MSCI EM retreating 0.5%. (Chart 5.)

Chart 5: Total equity return indices

(rebased, 6 June 2017=100)



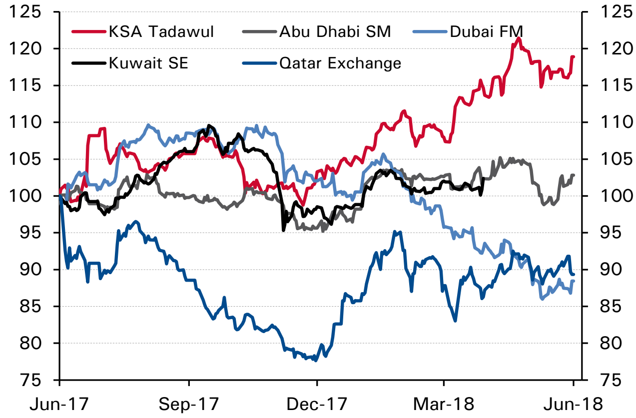
Source: Thomson Reuters Datastream

Retreating oil prices, weaker global sentiment and concerns over the newly announced visa programs initially weighed on regional markets, but turned around helped by the recovery in oil prices. The MSCI GCC index finished the week 1.2% higher.

Property and banking shares in Abu Dhabi (+0.1%) and Dubai (+0.3%) led the sell-off earlier in the week but rebounded later on firmer oil prices. Saudi (+1.5%) also benefited from higher oil prices, as well as the anticipation surrounding its ascension to MSCI's emerging market index – expected June 20. Qatar (-1.9%), however, experienced some profit taking, while Kuwait was little changed. (Chart 6.)

Chart 6: GCC equity markets

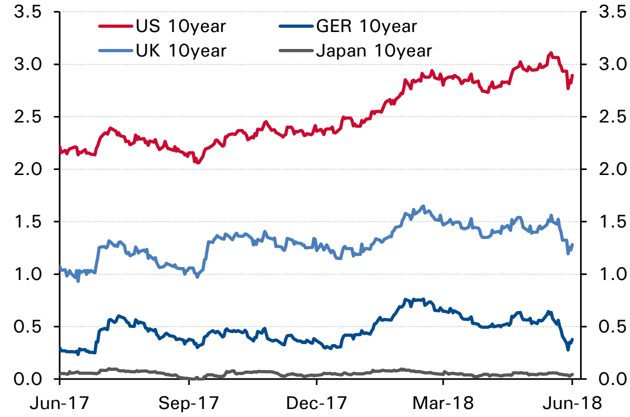
(rebased, 1 June 2017=100)



Source: Thomson Reuters Datastream

Chart 7: Global bond yields

(%)



Source: Thomson Reuters Datastream

Markets – fixed income

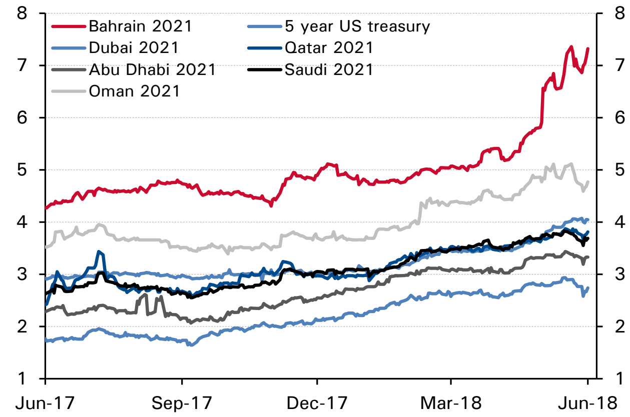
The turmoil in Europe and President Trump's confrontational trade position has favored safe havens, with bond prices up on the week despite an end-week decline on stronger US data and as Italian political tensions eased. US 10-year yields dropped 4 basis points to 2.90%, while 10-year Bunds shed 3 bps, to settle at 0.38%, close to their lowest levels since December. (Chart 7.)

Concerns over Italy and Spain have put into question Eurozone growth, and by extension global growth. This in addition to more protectionist trade rhetoric shifted expectations of four rate hikes by the US Fed in 2018 lower to 30% from 47% more than a month ago.

GCC yields were mixed, as uncertainty over OPEC oil production had somewhat offset the down pull of US treasuries. (Chart 8.)

Chart 8: GCC bond yields

(%)



Source: Thomson Reuters Datastream

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 Maktoom, (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