# Strong US data triggers market sell-off; Brent falls as US oil production hits 47-year high

## Key market indicators

| Stock markets | Index | Change (%) weekly | Change (%) YTD |
|---|---|---|---|
| **Regional** | | | |
| Abu Dhabi (ADI) | 4,612 | -0.67 | 4.86 |
| Bahrain (ASI) | 1,358 | 1.19 | 3.95 |
| Dubai (DFMGI) | 3,412 | -1.63 | 1.25 |
| Egypt (EGX 30) | 15,089 | -0.54 | 0.48 |
| GCC (S&P GCC 40) | 1,000 | -0.67 | 1.59 |
| Kuwait (Price Index) | 6,685 | 0.50 | 4.33 |
| KSA (TASI) | 7,656 | 1.79 | 5.88 |
| Oman (MSM 30) | 5,035 | 0.55 | -0.24 |
| Qatar (QE Index) | 9,207 | -2.67 | 7.99 |
| **International** | | | |
| CSI 300 | 4,271 | -2.51 | 5.96 |
| DAX | 12,785 | -4.16 | -1.03 |
| DJIA | 25,521 | -4.12 | 3.24 |
| Euro Stoxx 50 | 3,523 | -3.40 | 0.55 |
| FTSE 100 | 7,443 | -2.90 | -3.18 |
| Nikkei 225 | 23,275 | -1.51 | 2.24 |
| S&P 500 | 2,762 | -3.85 | 3.31 |

| Commodities | $/unit | Change (%) weekly | Change (%) YTD |
|---|---|---|---|
| Brent crude | 68.6 | -2.75 | 2.56 |
| KEC | 66.1 | -1.03 | 4.09 |
| WTI | 65.5 | -1.04 | 8.33 |
| Gold | 1333.7 | -1.32 | 2.10 |

| Exchange rates | Rate | Change (%) weekly | Change (%) YTD |
|---|---|---|---|
| KWD per USD | 0.299 | 0.03 | -0.59 |
| KWD per EUR | 0.363 | 0.00 | 2.37 |
| USD per EUR | 1.246 | 0.33 | 3.87 |
| JPY per USD | 110.1 | 1.28 | -2.29 |
| GBP per USD | 1.412 | -0.34 | 4.50 |
| EGP per USD | 17.63 | -0.06 | -0.56 |

| 3m interbank rates | % | Change (bps) weekly | Change (bps) YTD |
|---|---|---|---|
| Bhibor | 2.75 | 0.0 | 2.5 |
| Kibor | 1.94 | 0.0 | 6.3 |
| Qibor | 2.67 | 8.3 | -7.3 |
| Eibor | 1.88 | 2.6 | 7.7 |
| Saibor | 1.89 | -0.2 | -1.0 |
| Libor | 1.79 | 2.7 | 9.3 |

| Bond yields | % | Change (bps) weekly | Change (bps) YTD |
|---|---|---|---|
| **Regional** | | | |
| Abu Dhabi 2022 | 3.19 | 10.9 | 24.3 |
| Dubai 2022 | 3.18 | 4.9 | 4.4 |
| Qatar 2022 | 3.47 | 1.9 | 39.3 |
| Kuwait 2022 | 3.17 | 11.6 | 36.0 |
| Saudi Arabia 2023 | 3.44 | 12.9 | 22.3 |
| **International** | | | |
| UST 10 Year | 2.85 | 19.0 | 44.1 |
| Bunds 10 Year | 0.76 | 13.5 | 33.5 |
| Gilts 10 Year | 1.58 | 13.4 | 39.1 |
| JGB 10 Year | 0.09 | 0.9 | 3.5 |

Source: Thomson Reuters Datastream; as of Friday's close 02/2/2018

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## Overview

Strong US jobs and wages data triggered a sharp sell-off in bonds at the end of last week, as investors reappraised the potential for a more rapid-than-expected tightening in monetary policy in both the US and elsewhere. In Janet Yellen's final meeting as Chair, the Fed left its target interest rate on hold at 1.25-1.5%, but upgraded its inflation outlook and adopted a more hawkish tone. Some analysts saw this as cementing the case for a March rate hike. The S&P 500 fell 2%, 10-year treasury yields rose 8 bps to a 4-year high and the dollar climbed modestly from recent lows, but still lost about 3% of its value in January.

The turbulent end to the week also hit commodities including oil, with the price of Brent crude down 3% w/w to $69, though still finishing January up 3% m/m. Earlier on, the US Energy Information Administration revealed that US oil production breached the 10 million b/d mark last November, only fractionally short of the record set in 1970. Despite the increase in US oil production and robust non-OPEC supply more generally, a combination of the buoyant global economy and OPEC supply discipline may provide some scope for further price strength.

In the Gulf, the budget approved by Kuwait's cabinet for FY2018/19 appears to buck the recent trend in the region towards looser fiscal policy, with budget-on-budget spending growth almost flat at 0.5% y/y. However, given a likely underspend in FY2017/18, we still think actual spending could rise by 4% next year. This would leave the government's consolidation effort broadly on track, with the deficit (excluding investment income) forecast at 13% of GDP helped also by higher oil revenues. The budget still requires approval by parliament.

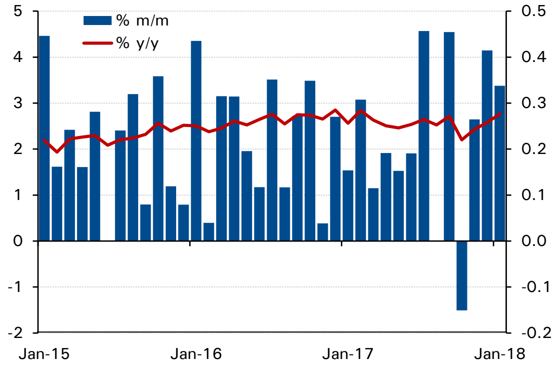
## International macroeconomics

**USA:** Last week's data continued to point to a robust economy. Employment growth saw a solid gain in January, with non-farm payrolls adding 200K during the month. More importantly, wage growth was healthy in January and pointed to a possible pick-up in inflation. Wages were up 0.3% m/m, but revisions to earlier months also boosted the annual pace to 2.9% y/y, which was above expectations (chart 1). Last week's FOMC statement, which kept rates on hold, also appeared to suggest that inflation was gaining momentum, with expectations that the 2% target will be reached sooner. The ISM manufacturing index, at 59.1 in January, also pointed to continued strength in the US economy.

**Eurozone:** The Eurozone continued to recover steadfastly, growing at its fastest pace in 11 years, 2.5% in 2017 (chart 2), and outperforming both the US (2.3%) and the UK (1.8%). Data from last week also suggests that momentum has carried through into 2018. Core inflation picked up to 1.0% in January from 0.9% the previous month, despite some easing in the headline number. Consumer sentiment also remained close to record highs, easing slightly to 114.7 in January, while unemployment held steady at its nine-year low of 8.7%.

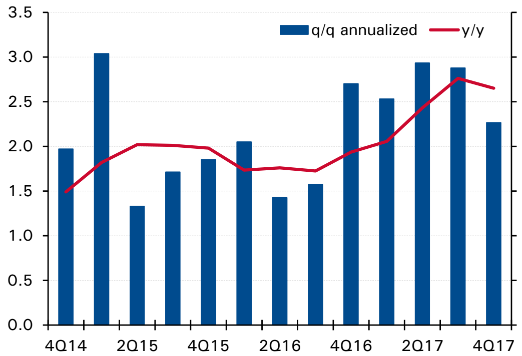
## Chart 1: US wage growth

(%)




Source: U.S. Bureau of Labor Statistics

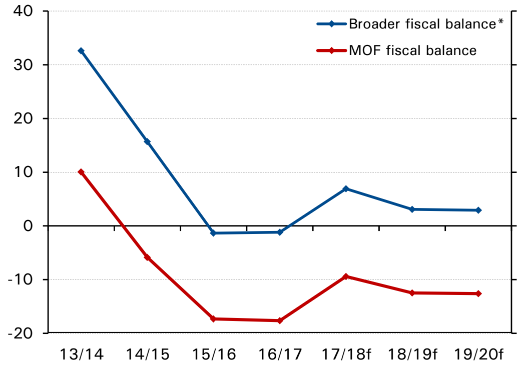
## Chart 2: Eurozone real GDP




Source: Thomson Reuters Datastream

## Chart 3: Kuwait fiscal balance

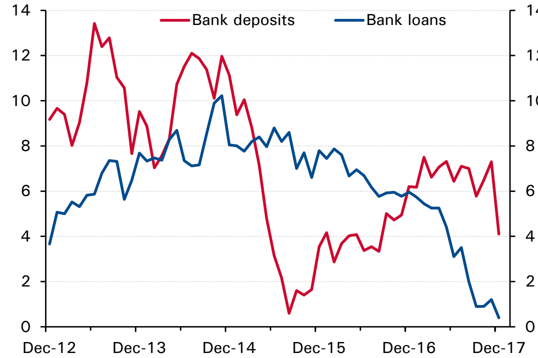
(% of GDP)




Source: MOF, NBK est.; *Before FGF transfer and incl. inv. income.

## Chart 4: UAE bank loan and deposit growth

(% y/y)




Source: Central Bank of the UAE

**China:** The official NBS manufacturing index softened to 51.3 in January from the prior month's 51.6 as a result of a slowdown in output and new orders. This index tracks larger (often state-owned) manufacturing firms. The Caixin-Markit PMI, which follows smaller private firms, showed a steady reading of 51.5 in January.

## GCC & regional macroeconomics

**Kuwait:** The cabinet approved the official FY18/19 budget with expenditure growth of just 0.5%. However, with likely underspending of 8% in FY17/18, this still leaves plenty of room for growth in actual spending. Indeed, we still see spending up 4% in FY18/19. The budget projects non-oil revenues growing by 8.5% on improvements in revenue collection. The introduction of the value-added tax will not be introduced in FY18/19 pending legislation. A deficit of 16% of GDP (after the transfer to the FGF) is projected based on a $50 price for Kuwaiti crude; we expect a smaller deficit of 13% of GDP. (Chart 3.) Meanwhile, S&P affirmed Kuwait's long-term sovereign rating at AA with a stable outlook.

Project awards reached KD 448 million in January 2018, surpassing 2017's monthly average of KD 330 million. Awards were mostly in the transport, oil, and construction sectors. The largest was for the Northern Regional Road (KD 175 million).

**Saudi Arabia:** The Saudi authorities last week released several detainees caught up in the graft scandal. The authorities reportedly recovered $106 billion in settlement fees in exchange for the dropping of all charges against the individuals.

**UAE:** Loan growth maintained its downward trend in December, falling to a multi-year low of 0.4% y/y, weighed down by moderate levels of economic activity, higher interest rates and tighter lending rules. (Chart 4.) Deposit growth slowed to 4.1% y/y from 7.3% y/y in November on the back of a drawdown in government deposits. Given the recent trends in credit and deposit growth, the loan-to-deposit ratio stood close to a multi-month low of 98% in December.

**Qatar:** The central bank reported that residential real estate prices fell 5% q/q on average in 4Q 2017, reflecting a property market downturn that began in 2015 but appeared to worsen after the start of the GCC diplomatic dispute last summer. There was a glimmer of encouragement in that prices rose 1.8% m/m in December – the first rise since June. But prices were still down 10% y/y. (Chart 5.)

## Markets – oil

Oil prices closed down last week at $68.6/bbl for Brent and $65.5/bbl for WTI. (Chart 6.) Brent's week-on-week fall of 2.8% was its largest since early December, and seemed to come in response to a stronger US dollar (after the US jobs data surprised on the upside) and amid further rises in US crude production. US crude output broke through the symbolic 10 mb/d last November, the EIA reported: at 10.04 mb/d, November's output was just 6,000 b/d short of the all-time record from November 1970. Weaker-than-expected quarterly earnings from US oil majors compounded the drop in oil prices.

Prices are still hovering at three-year highs, however, with money managers continuing to hold record net bullish positions in crude futures and options, estimated at around 550 million barrels in the case of WTI. A number of investment banks have revised up their oil price forecasts,

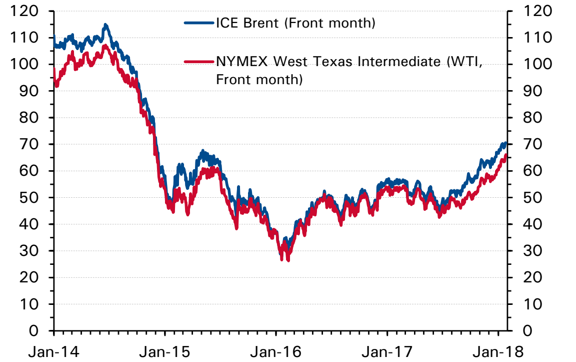
## Chart 5: Qatar real estate price index

(% y/y)


Source: Qatar Central Bank

## Chart 6: Benchmark crude oil prices

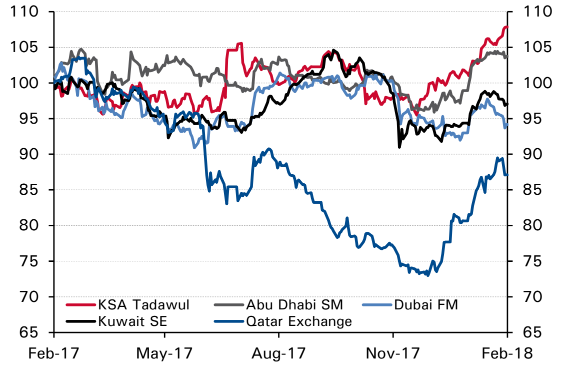
($/bbl)




Source: Thomson Reuters Datastream

## Chart 7: GCC equity markets

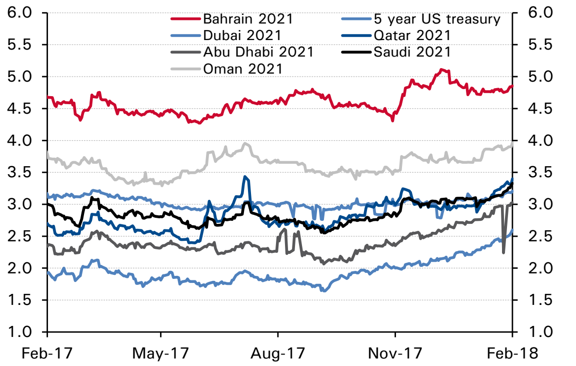
(rebased, 2 February 2017=100)




Source: Thomson Reuters Datastream

## Chart 8: GCC bond yields

(%)




Source: Thomson Reuters Datastream

with Goldman Sachs recently arguing that the oil market has reached balance and that prices will rise further on strong emerging market demand.

## Markets – equities

International equity markets retreated as investors assessed the pace of monetary tightening following strong economic data. The MSCI world index was down 3.2% on the week, the largest drop since June 2016. Indeed, the VIX volatility measure, at 17 points on Friday, was at its highest since November 2016.

US equities posted their largest weekly falls since February 2016. The S&P ended the week down 3.9%, while the DJI closed 4.1% lower, with both on Friday suffering their biggest daily losses since Mr. Trump's election. The sell-off spilled over to other global markets, with European equities down 3.4% and emerging markets retreating by 2.7%.

The MSCI GCC index was up 0.1% during the week, helped by a rebound in Saudi linked to domestic politics. The wind-down of the anti-corruption drive supported the Tadawul index. Real estate market weakness continued to weigh on Dubai, while Qatar suffered from profit taking. (Chart 7.)

## Markets – fixed income

Benchmark yields reached multi-year highs on stronger global growth and reshaped inflation expectations. The Fed kept interest rates unchanged at its latest monetary policy meeting, although markets expect a rate hike in March with close to 100% certainty, fueled by the latest jobs and wages data. US 10-year treasury yields increased by 19 basis points, the most since November 2016, to settle at 2.85%. Meanwhile, Bunds also rose following the US led sell-off, adding 14 bps on the week to reach 0.76%. GCC benchmark yields also increased, with most up 11-13 bps. (Chart 8.)

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