Markets consolidate; US optimism up into Trump administration; inflation a bit firmer across countries

Key market indicators

Stock markets	Index	Change (%) weekly	YTD
Regional			
Abu Dhabi SM	4,681	1.72	2.97
Bahrain ASI	1,212	0.44	-0.71
Dubai FM	3,721	2.56	5.37
Egypt EGX 30	13,224	3.12	7.12
KSA Tadawul	6,922	-3.85	-4.00
Kuwait SE	6,108	4.74	6.26
Muscat SM 30	5,762	-0.52	0.31
Qatar Exchange	10,709	-0.07	2.61
MSCI GCC	471	-1.73	-0.90
International			
DAX	11,629	0.26	1.29
DJIA	19,886	-0.39	0.62
FTSE 100	7,338	1.77	2.73
Nikkei	19,287	-0.86	0.90
S&P 500	2,275	-0.10	1.60

Commodities	$/bbl	Change (%) weekly	YTD
Brent crude ($/bbl)	55.5	-2.89	-2.41
KEC ($/bbl)	49.4	-4.85	-4.76
WTI ($/bbl)	52.4	-3.00	-2.51
Gold ($/t oz.)	1188.1	1.37	2.74

Exchange rates	Rate	Change (%) weekly	YTD
KWD per USD	0.305	-0.13	0.01
KWD per EUR	0.323	0.59	1.35
USD per EUR	1.064	1.08	1.22
JPY per USD	114.51	-2.05	-2.02

Interbank rates	%	Change (bps) weekly	YTD
Kibor – 3 month	1.44	0.0	0.0
Qibor – 3 month	1.84	0.5	5.8
Libor – 3 month	1.02	1.3	2.5

Fixed income	%	Change (bps) weekly	YTD
Regional			
Abu Dhabi 2021	2.54	-2.8	-0.4
Dubai 2021	3.21	2.5	-11.2
Qatar 2021	2.85	-6.8	-10.5
Saudi Arabia 2021	2.99	-5.8	-6.5
International			
UST 10 year	2.38	-3.8	-5.2
Bunds 10 year	0.34	3.2	13.1
Gilts 10 year	1.37	-1.6	12.6
JGB 10 year	0.05	-0.6	0.1

Source: Thomson Reuters Datastream

> Economic Research Department
+965 2259 5500
econ@nbk.com

Summary

World equity markets advanced in the week, albeit moderately. The Dow Jones Industrials is still attempting to break 20,000, some caution appears to have set in as we approach the Trump inauguration. GCC markets are led so far this year by Dubai and Kuwait, while Saudi takes a breather following a very strong finish to 2016.

Oil, exchange rates and yields were also about consolidation, after big moves late in 2016. Brent oil is hovering around $55 per barrel (bbl), the euro is back above 1.05, and the 10-year US note closed the week at 2.4%.

Inflation data from China, the Eurozone, the US and the UK among others point to firmer headline numbers (thanks to higher oil prices). These had all been in negative territory a while back. However, that firmness does not mean that inflation is about to become a problem, just that the pressure on central banks should abate somewhat.

Growth in the Eurozone remains on track, with Germany posting 1.9% GDP growth in 2016, the best in 5 years. The concerns for Europe are primarily political for this year, with at least 3 major elections looming: the Netherlands, France and Germany.

Locally, Kuwait awarded a solid KD 13.6 billion worth of projects in 2016, and consumer confidence showed further improvement in December.

International macroeconomics

USA: As we approach the Trump inauguration on 20 January, the policy fog is starting to lift, but much uncertainty remains. Various business and consumer sentiment measures/surveys, however, rose to new highs in the US with the firm expectation that a friendlier business environment is dawning with the incoming Trump administration (lower taxes, deregulation, added infrastructure spending). The latest such measure was the NFIB Index of Small Business Optimism, which rose in December to a 14-year high (105.8).

December retail sales were a tad disappointing; they closed the year up 0.6% m/m, but a weak 0.2% m/m if autos are excluded. Optimism and consumer confidence remain firm. (Chart 1). US producer price index (PPI) inflation, in line with other countries, is firming primarily because of rising oil prices. December's PPI, both core and headline, were up 1.6% y/y.

Eurozone: Preliminary estimates for Germany's GDP show the economy expanding by 1.9% in 2016. This beat expectations, but was in line with recent improvements in PMI and manufacturing data. Growth was driven by private consumption and state spending. This follows last week's strong jump in December consumer inflation, and the latest reading helps steer growth and inflation expectations to the upside for 2017.

Italy's constitutional court rejected a bid by the country's largest trade union to hold a referendum over a jobs act proposed by the recently resigned PM Matteo Renzi. This was a relief to a still fragile government.

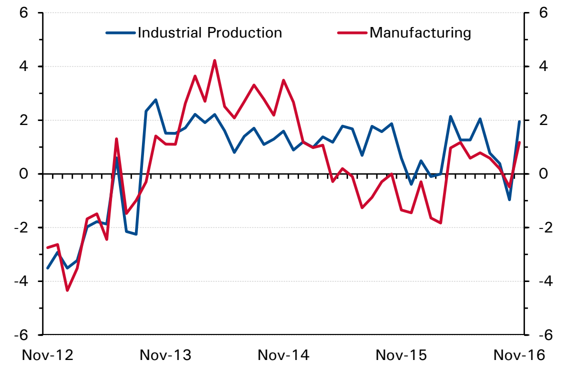
Chart 1: NFIB Index of Small Business Optimism

(monthly index)

Source: Institute Of Supply Management

Chart 2: UK industrial production

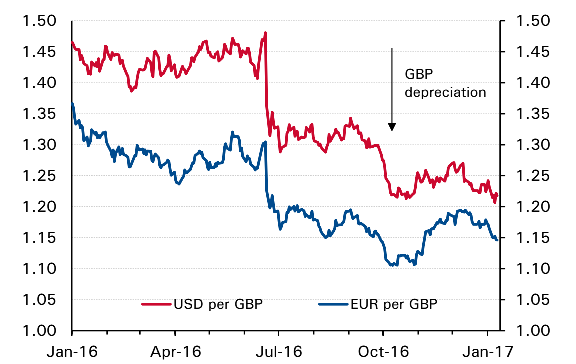
(index, % y/y)



Source: ONS, Thomson Reuters Datastream

Chart 3: UK Pound Sterling exchange rate

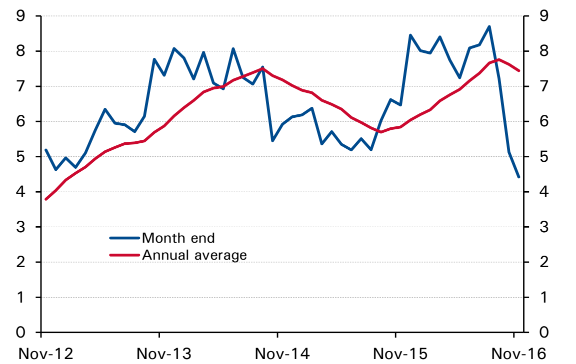
(foreign currency per pound)



Source: Thomson Reuters Datastream

Chart 4: Kuwait private credit

(% y/y)



Source: Central Bank of Kuwait

This and other political accomplishments since the December referendum, however, were not enough to maintain Italy's investment grade rating. DBRS became the latest major agency (mandated/used by the ECB) to downgrade Italy's sovereign rating, dropping it from A (low) to BBB (high) on concerns of political and financial instability. Standard & Poor's rates Italy BBB-, Moody's rates it BBB+, and Fitch rates it Baa2.

Monte dei Paschi's (MPS) bailout could make some progress in the coming weeks, with the state expected to inject EUR 6.5 billion in the ailing bank. Last month, the Italian government approved EUR 20 billion to support its financial sector. The ECB estimates MPS could require as much as EUR 8.8 billion.

China: Producer price inflation reached a five-year high, continuing 2016's reversal of a four-year deflationary trend that had weighed on global prices. The PPI increased to 5.5% y/y in December, rising from November's 3.3% y/y. Higher factory prices in China will add inflationary pressure to global prices. Headline inflation was reported at 2.1% y/y in December 2016, cooling slightly from November's 2.3% y/y.

UK: UK economic data continue to surprise to the upside. Industrial production data for November showed activity rising by 2.0% m/m from October and 1.9% y/y. (Chart 2.) Annual growth rebounded from the -1.0 y/y recorded in October, with crude oil & natural gas production and pharmaceuticals manufacturing leading the way. Analysts had been expecting growth of 1.0% m/m in November.

Last week's data continue to confound the gloomy predictions of most economists in the wake of Brexit, but it should be noted that the UK is still to trigger Article 50, so the actual departure process has not even begun. Nevertheless, the GBP has been the first casualty of Brexit: the pound fell further, to 3-month lows, against the US dollar (-1.2%) and the euro (-1.6%) last week to USD 1.2 per GBP and EUR 1.14 per GBP by Friday's close, respectively. This was after PM Theresa May remarked that the country was likely to leave the single market altogether rather than attempt to keep 'bits' of membership. (Chart 3.)

Markets are nervously awaiting the PM's speech on the government's Brexit strategy on Tuesday and the ruling of the UK Supreme Court on the government's prerogative to trigger Article 50 without parliamentary approval. Any ambiguity on the part of the PM is likely to result in Sterling being punished further.

GCC & regional macroeconomics

Kuwait: Credit growth slowed once again in November. Growth came in at 4.4% y/y as credit fell by KD 34 million during the month. (Chart 4.) Growth continued to reflect the large repayment of debt in October following the Americana deal; growth adjusted for this one-time event is estimated at a robust 6.5% y/y. We expect growth to average 7% during 2016. M2 money supply growth accelerated to 6.5% y/y on base effects.

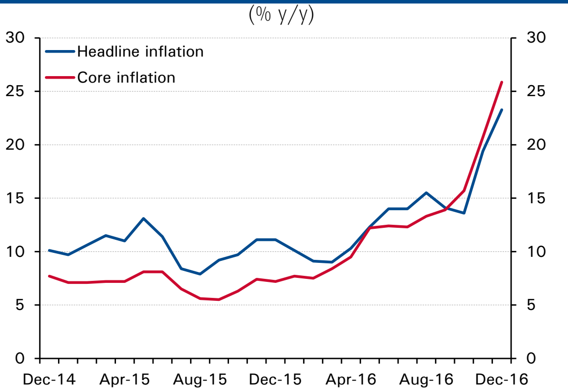
Consumer confidence improved in December, with the ARA index rising to 99. The index had dropped to 83 in September 2016, its lowest level in seven years. It has since seen a gradual improvement. Despite the rise, consumer confidence remained under pressure, with the index level still below the 103 average seen during the first seven months of 2016.

Project awards in Kuwait amounted to USD 13.6 billion during 2016. The figure was well below the USD 33 billion awarded in 2015, but the latter was boosted by oil megaprojects. The USD 13.6 billion exceeds the USD 10 billion average that had been the norm in the period before project

Chart 5: Dubai Economy Tracker
(index)

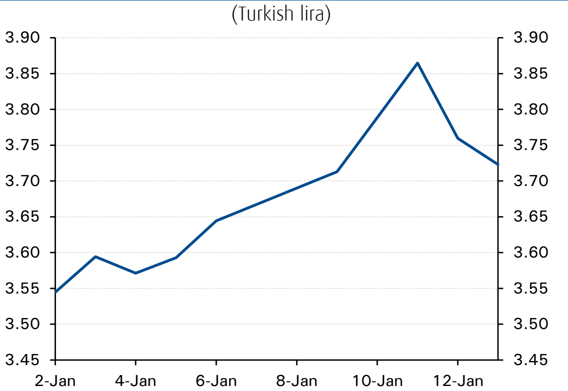
Source: Emirates NBD

Chart 6: Egypt inflation
(% y/y)



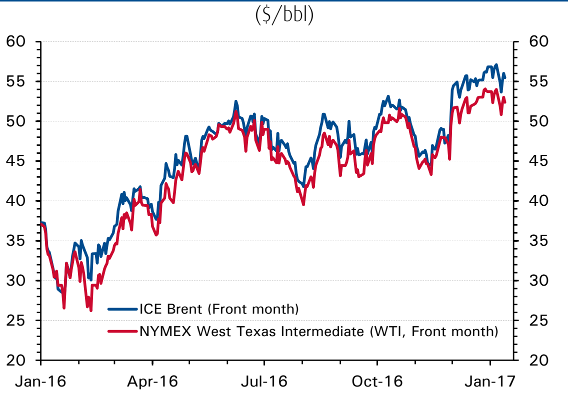
Source: Central Bank of Egypt, Thomson Reuters Datastream

Chart 7: USD TRY exchange rate
(Turkish lira)



Source: Thomson Reuters Datastream

Chart 8: Crude oil prices
($/bbl)



Source: Thomson Reuters Datastream

implementation picked up in 2014. Projects awarded during 2016 included KNPC's LNG import and regasification terminal (USD 2.9 billion), South Mutla City (USD 1.0 billion) and a new maternity hospital (USD 0.7 billion).

UAE: According to the Emirates NBD Dubai Economy Tracker (DET) index, non-oil sector activity in Dubai hit a five-month high in December 2016. (Chart 5.) The pick-up in the non-oil economy mainly came on the back of robust output and new work levels in the construction sector. Business expectations also came in at a strong 74.5 in December. The construction sector in Dubai is expected to continue to see gains in the months to come as preparations for the Expo 2020 begin to accelerate.

Qatar: The IMF, in its Article IV Mission note, praised Qatar's efforts in managing its spending. The government is expected to garner additional revenues by cutting subsidies on utilities, increasing government fees, and introducing taxes on tobacco, soft drinks, and possibly fast food in 2017. In 2018, the 5% VAT will be introduced. Despite domestic banks being adequately capitalized, the IMF advised that Qatar needs to carefully manage liquidity with low energy prices and rising US interest rates.

Oman: Oman is in talks to secure multi-billion dollar deposits from its GCC neighbors to bolster official reserves and help defend its peg to the USD. The move follows Oman's recent commitment to the Saudi-led coalition against Iranian influence in the region, adjusting its usually neutral stance. Foreign reserves currently cover around 9 months of imports, but external liabilities and expenses are expected to grow. In addition to its official reserves, Oman has a sovereign wealth fund of around USD 35-40 billion.

Egypt: Inflation rose in December as the effects of the November decision to float the pound (EGP) continued to impact domestic prices. Inflation accelerated more than expected to 23.3% y/y. (Chart 6) Still, the monthly gain in prices moderated to 3.1% from 4.8% the previous month. The EGP has been mostly steady since falling by around 50% in November, which should help reduce inflationary pressures in the coming months.

Lebanon: The newly-formed Hariri cabinet approved two decrees that could pave the way for Lebanon to begin exploration of offshore oil and gas. The country first sought to auction exploration rights more than three years ago. The recent end to a 2-year presidential vacuum rejuvenated hopes of progress on this front.

Turkey: The Turkish lira continued to hit new lows against the USD during the first 10 trading days of 2017. By 11 January it was down 9% ytd. (Chart 7.) This prompted the central bank to lower the foreign-currency reserve requirement ratio and tighten lira liquidity through the interbank market by making it more costly for commercial banks to borrow. This has, to some extent, helped the lira.

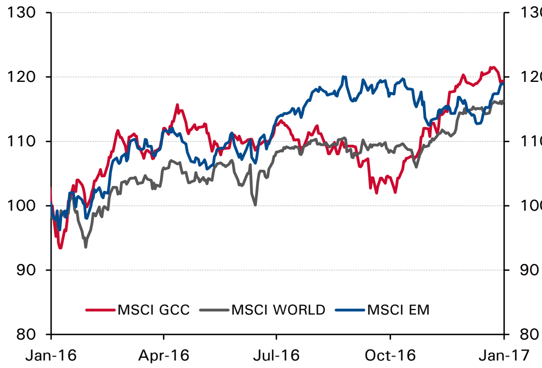
Markets – oil

Oil prices seesawed last week, initially falling on the expectation of further crude stock builds and rig count increases in the US, before rising after the same set of data showed that US crude refiners had processed 17.1 million barrels a day of crude, a record. Oil climbed further on Wednesday/Thursday, posting the highest 2-day gain in almost 2 weeks on news that Saudi Arabia had cut its oil production by even more than that required under the terms of the OPEC deal. Brent and WTI were back up to $55.5/bbl and $52.4/bbl, respectively, on Friday. (Chart 8.)

The improvement in mood also came despite further gains in US crude oil production (+176,000 b/d to 8.95 mb/d) and the EIA's upwardly revised

Chart 9: Total return indices

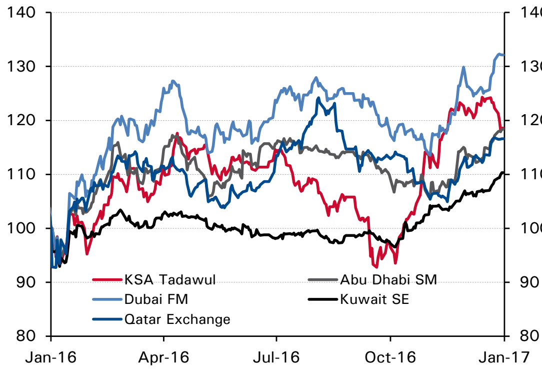
(rebased, 14 Jan 2016=100)



Source: Thomson Reuters Datastream

Chart 10: GCC markets

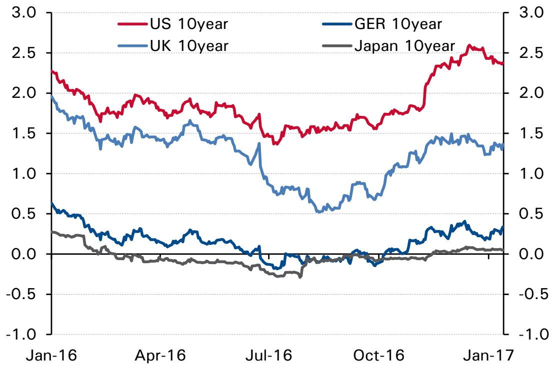
(rebased, 14 Jan 2016=100))



Source: Thomson Reuters Datastream

Chart 11: Global benchmark yields

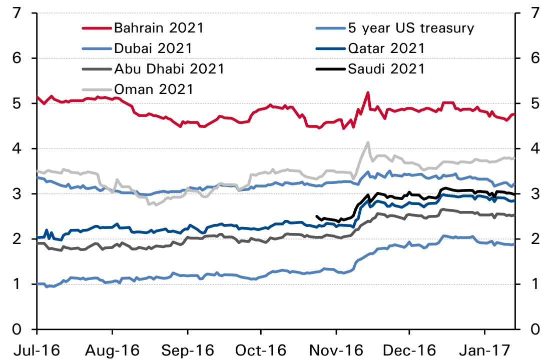
(%)



Source: Thomson Reuters Datastream

Chart 12: GCC yields

(%)



Source: Thomson Reuters Datastream

forecast for production growth in 2017 (+110,000 b/d to 9.0 mb/d) and 2018 (+300,000 b/d to 9.3 mb/d). The agency expects both conventional crude production, from the Gulf of Mexico, and shale production to rise this year, with the latter benefitting especially from improved rig efficiency and productivity.

It appears that the expectation of higher oil prices in 2017-18 is spurring oil majors to get back into the game. Capital spending by oil companies is projected to rise this year, by 3%, to USD 450 billion after two consecutive years of declines, according to a report by Wood Mackenzie. Rystad Energy, another consultancy, has estimated that 15 billion barrels of oil equivalent (boe) in new offshore production capacity will be sanctioned in 2017, compared to only 6 billion boe last year.

Markets – equities

The performance of equity markets was mixed last week. Advanced market equities were lackluster, with the MSCI World index closing the week up a mere 0.1%. (Chart 9.) The S&P 500 and DJIA retreated 0.1% and 0.4%, respectively. European equities also lacked momentum, with the Euro Stoxx 50 up 0.1% on the week. Emerging markets continued to outperform, with the MSCI index up 1.3% on the week.

GCC equity markets also saw a mixed performance, with a notable decline in the heavily-weighted Saudi market weighing on regional indices. The MSCI GCC index retreated 1.7%. (Chart 10.) Profit-taking in Saudi equities over the first two weeks of the year followed a strong rally in the last quarter of 2016. Market observers seem to be holding off in anticipation of earnings announcements. Dubai, on the other hand, had a strong start to the year, with its general index adding 2.6% last week.

Kuwait also had a good start to the year, with its general index increasing by 1.9% last week. There was a more notable pick-up in activity/volumes. Average daily turnover almost tripled in the first weeks of 2017 compared to its 2016 average.

On the legislative front, Saudi's Tadawul published draft rules for the implementation of the T+2 settlement cycle. This is another move towards aligning the market with international best practice.

Markets – fixed income

With data releases lacking this week, talk of hard Brexit, Chinese capital controls, and growing skepticism over Mr. Trump's economic policies saw investors buy into bonds early in the week. Yields on most benchmarks were later lifted by more hawkish minutes from the ECB meeting and remarks from Fed officials, in addition to Italy's downgrade. As such, movements in benchmark yields were relatively contained in a band throughout the week, with US 10-year bonds losing only 4 bps on the week, while Bunds were up 3 bps. (Chart 11.)

GCC yields were mixed over the week, with some benefitting from strength in oil prices. Saudi Arabia, Qatar, and Abu Dhabi's 5-year benchmarks were down by 3-7 bps. Meanwhile, Oman, Bahrain, and Dubai's 5-year papers were up 2-7 bps. (Chart 12.)

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