Strong US data pushes USD and stocks up; Europe beset by Spanish and UK uncertainty; oil takes a break

Key market indicators

Stock markets	Index	Change (%) weekly	Change (%) YTD
Regional			
Abu Dhabi SM	4,414	0.38	-2.91
Bahrain ASI	1,274	-0.73	4.40
Dubai FM	3,591	0.76	1.71
Egypt EGX 30	13,882	-0.05	12.45
S&P GCC 40	1,049	1.63	-9.23
Kuwait SE	6,662	-0.26	15.90
KSA Tadawul	7,259	-0.33	0.68
Muscat SM 30	5,213	1.48	-9.84
Qatar Exchange	8,132	-2.17	-22.08
International			
CSI 300	3,837	0.00	15.91
DAX	12,956	0.99	12.85
DJIA	22,774	1.65	15.24
Eurostoxx 50	3,603	0.24	9.51
FTSE 100	7,523	2.04	5.32
Nikkei 225	20,691	1.64	8.25
S&P 500	2,549	1.19	13.87

Commodities	$/unit	Change (%) weekly	Change (%) YTD
Brent crude	55.6	-3.34	-2.11
KEC	53.6	-0.50	3.24
WTI	49.3	-4.61	-8.25
Gold	1271.6	-0.77	10.57

Exchange rates	Rate	Change (%) weekly	Change (%) YTD
KWD per USD	0.302	0.07	-1.16
KWD per EUR	0.355	-1.55	11.63
USD per EUR	1.173	-0.67	11.60
JPY per USD	112.630	0.14	-3.63
USD per GBP	1.306	-2.49	5.89
EGP per USD	17.640	0.06	-2.00

Interbank rates	%	Change (bps) weekly	Change (bps) YTD
Bhibor - 3 month	2.43	-2.5	32.5
Kibor - 3 month	1.75	0.0	31.3
Qibor - 3 month	2.45	5.2	67.0
Eibor - 3 month	1.56	0.0	8.2
Saibor - 3 month	1.79	0.1	-24.3
Libor - 3 month	1.35	1.4	35.1

Bond yields	%	Change (bps) weekly	Change (bps) YTD
Regional			
Abu Dhabi 2021	2.27	14.0	-26.2
Dubai 2021	2.97	-1.4	-33.2
Qatar 2021	2.81	0.0	-12.2
Kuwait 2022	2.53	-1.0	n/a
Saudi Arabia 2022	2.80	-5.0	n/a
International			
UST 10 Year	2.37	4.2	-6.4
Bunds 10 Year	0.46	0.0	25.4
Gilts 10 Year	1.36	-0.2	12.4
JGB 10 Year	0.05	-1.0	0.5

Source: Thomson Reuters Datastream; as of Friday's close 6/10/2017

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Overview

US stocks saw six successive closing highs for the first time in 20 years, boosted by generally positive economic data – including Friday's jobs report – and progress on President Trump's tax plan. But volatility may lie ahead. The president's cryptic "calm before the storm" comment on Thursday left observers unsure if it was a reference to a possible escalation in tensions with North Korea or Iran; the administration may decide to abandon or weaken the nuclear deal with Iran this week, which could impact oil markets.

Markets in Europe, meanwhile – although up on the week – also continue to operate against a backdrop of political uncertainty. The Spanish constitutional court has blocked a session of the Catalonian regional parliament scheduled for Monday that could have resulted in a declaration of independence. And UK PM Theresa May's hapless speech at the Conservative party conference has fueled speculation over a possible leadership challenge, which could inject fresh volatility into the Brexit negotiations and raise the chance of a 'no deal' outcome.

The recent run up in oil prices came to a halt, with Brent dropping to $55.6 versus the previous week's peak of $59, helped by a stronger US dollar and the closing in of Hurricane Nate. The fall was despite Saudi-Russia talks that suggested the current oil output supply cuts could be extended from next March until end-2018. It was also a notable week for US crude exports – banned just over two years ago – which reached nearly 2 million bpd and are now starting to enter markets in Asia and Europe traditionally OPEC's turf. US crude is currently priced at a significant discount to most Middle Eastern blends.

In the Gulf region, the Saudi equity market was broadly unchanged despite last week's disappointing news that the country missed out – for now – on an upgrade to Emerging Market status in the FTSE Russell index. S&P provided cautious support for the government's reform plans by leaving its credit rating unchanged at an investment grade A- (outlook stable), helped by expectations of further successful fiscal adjustment. The Qatari stock market, by contrast, saw further bleeding, with a 2.2% loss leaving it down 18% since the diplomatic crisis broke in June.

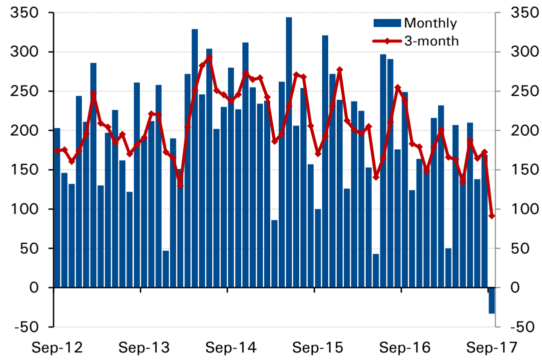
International macroeconomics

USA: Payrolls shrank in September on the back of severe hurricane weather in Texas and Florida. Nonfarm payrolls fell by 33,000 during the month, the first monthly decline in seven years. (Chart 1.) Nonetheless, there were noticeable indications of labor market tightness, with the unemployment rate declining to 4.2% and wage growth jumping 0.5%. This lends further support to chances of a Fed hike in December, with markets now pricing in a 90% probability of that happening.

The ISM manufacturing index continued to reflect strength in activity in September, rising to 60.8, its highest level in 13 years. (Chart 2.) The data appeared little affected by the severe hurricane weather, with strength visible across most of the index components. The non-manufacturing index

Chart 1: US new jobs (nonfarm)

(000s)



Source: U.S. Bureau of Labor Stastics

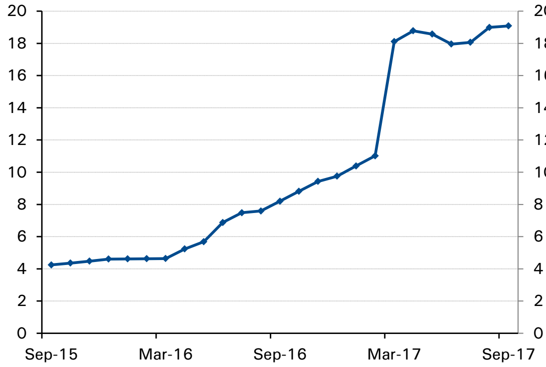
Chart 2: US ISM manufacturing

(index)

Source: Insitute for Supply Management

Chart 3: Kuwait government debt

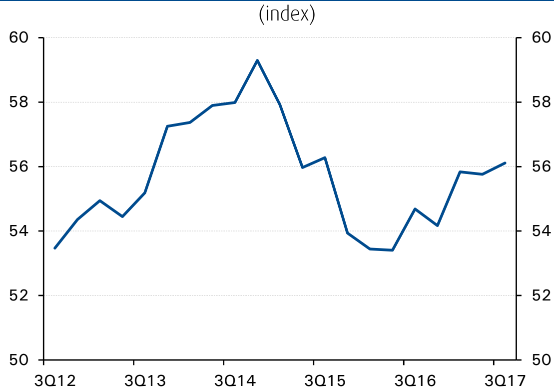
(% of GDP)



Source: Central Statistical Bureau, NBK estimates

Chart 4: UAE Purchasing Managers' Index

(index)



Source: Markit

was also robust coming in at 59.8, its best level in twelve years.

Eurozone: A tense referendum held last Sunday saw Catalans vote on secession from Spain. Preliminary results were overwhelmingly in favor, though not accounting for those who boycotted. Official results are to be released on Monday, and later the Catalan government is expected to declare independence, despite the vote's unconstitutionality. A speech by King Felipe VI reprimanded the Catalan government for "irresponsible" behavior that undermined Spanish unity. Markets were set back by the return of political uncertainty in Eurozone, with the euro weakening slightly to 1.17 following the vote. So far the IBEX 35 has dropped by 1.9%, while yields on 10-year Spanish government debt are up 17 bps.

UK: The latest round of PMIs presented mixed news on the UK economy and pointed to a divergence of performances. The construction PMI fell below 50 in September signaling a contraction in activity – the first fall in over a year. The index stood at 48.1 versus 51.1 in August. The same survey of the manufacturing sector also disappointed, dropping on the month. But at 55.9, the figure remains close to its recent highs and still signals strong expansion. One positive factor for survey respondents has been the weakness of the pound, which, despite recovering somewhat of late, is still some 8% weaker against the US dollar than before the Brexit vote of 2016, and 12% lower versus the euro. Finally, the services PMI improved a touch to 53.6, pointing to steady though unspectacular growth.

GCC & regional macroeconomics

Kuwait: The CBK issued a net of KD 400 million in domestic bonds on behalf of the Ministry of Finance in September, increasing outstanding domestic debt to KD 4.9 billion. Though net issuance was ramped up in August and September, the pace thus far in FY17/18 remained steady at around KD 175 million per month. Domestic issuance will likely finance 40-50% of this fiscal year's deficit, which we estimate at KD 4.8 billion. Total debt, including international bonds, is estimated at 19% of GDP (Chart 3).

Project awards improved slightly in 3Q17 to KD 0.8 billion from the second quarter's KD 0.7 billion, though it remained below the 3-year quarterly average of KD 1.5 billion. The quarter's awards included the much-awaited Al-Zour refinery feed pipeline, worth KD 236 million, and the Kabd solid waste project worth KD 257 million (PPP).

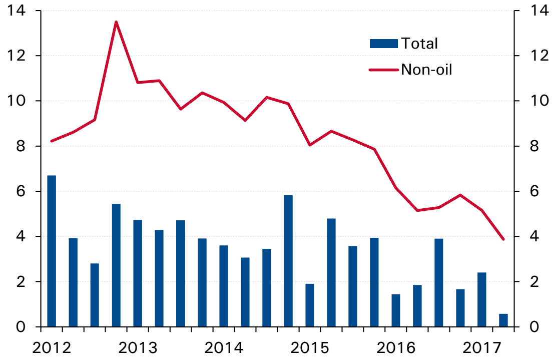
Saudi Arabia: The central bank presented a positive outlook on the kingdom's economy, despite the recent Q2 GDP figures revealing the second consecutive year-on-year fall. The bank stated that private sector growth is expected to strengthen, and that deflation – present throughout 2017 so far – would not be a worry. Meanwhile, joint investment agreements totaling over $3 billion are expected to be signed between Saudi Arabia and Russia. The deals include a $1.1 billion petrochemical plant in the kingdom to be built by Russian firm Sibur.

UAE: The headline PMI eased from 57.3 in August to a still healthy 55.1 in September, as robust new orders and output data helped offset some of the weakness in new export orders. On a quarterly basis, the headline PMI climbed to an almost two-year high of 56.1 (chart 4), reflecting the gradual recovery in the domestic market. In this setting, we expect real non-oil growth to rise from an estimated 2.7% in 2016 to 3.3% in 2017.

Abu Dhabi issued a $10 billion three-tranche bond last week, its first bond issuance since 2016. (See the fixed income section below.) Final bond yields fell after demand for the issue topped an impressive $30 billion.

Chart 5: Qatar real GDP

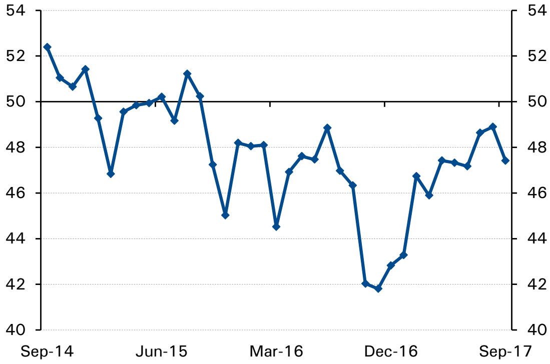
(% y/y)



Source: Thomson Reuters Eikon

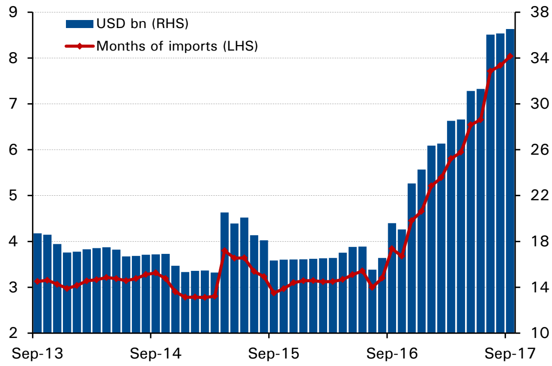
Chart 6: Egypt PMI

(% y/y)



Source: Markit

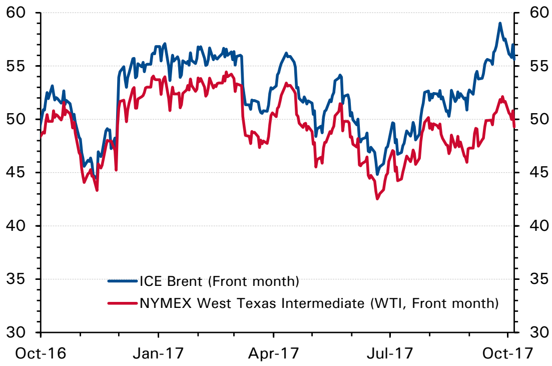
Chart 7: Egypt official reserves



Source: Central Bank of Egypt, NBK estimates

Chart 8: Benchmark crude oil prices

($/bbl)



Source: Thomson Reuters Datastream

With the UAE's fiscal balance forecast to remain in a manageable deficit of 3.1% and 2.0% of GDP in 2017 and 2018, further bond issues are unlikely within the next year. Nonetheless, the UAE is in the process of finalizing a federal debt law, which would allow the federal government to issue bonds as well.

Qatar: Economic growth in Q2 slowed more than we had expected, rising by just 0.6% y/y. This was the softest pace on record (as of 2011) and compares to the 2.4% pace recorded in Q1. Output in the oil & gas sector fell 2.7% y/y, not helped by the cuts in oil output linked to OPEC policy. But more striking was the non-hydrocarbon sector, where growth slowed to just 3.9% y/y versus 5.2% in Q1. (Chart 5.)

This data includes about one month's worth of impact from the ongoing diplomatic dispute, and there were notable slowdowns/declines in output in the transport, communications and finance sectors. Growth was also hit by a decline in import duties, clearly linked to the impact of the embargo. The data suggests a slight downside risk to our non-oil growth forecast of 4% this year.

The population data for September was slightly more reassuring – showing a bounce back of some 8% from August, to 2.63 million. Most of this rise was seasonal (i.e. post-summer holidays), but the year-on-year rate also climbed to 3.2% from 1.9% a month earlier. Although population growth has still slowed considerably from the 7.4% rate recorded in 2016, the latest numbers will at least reduce worries of a sharp drop in expatriate numbers due to the crisis.

Egypt: The PMI slipped in September as export orders, which have been a source of strength, took a hit. The general index declined to 47.4, its lowest reading in three months, continuing to suggest weaker growth than GDP figures indicate. (Chart 6.) Meanwhile, inflationary pressures eased further during the month.

The foreign reserves of the CBE rose slightly in September to close the month at $36.5 billion or 8 months of imports. The last 14 months saw reserves rise by nearly $21 billion and the import cover more than double after authorities began comprehensive reforms, which have been endorsed by the IMF. (Chart 7.)

CBE announced it will raise the required reserve ratio to 14% from 10% at a time when subduing inflation has been a key priority. Though inflationary momentum has been easing, it remains elevated at 32% y/y in August. The move is unlikely to put much pressure on loan growth as banks already maintain a high reserve ratio.

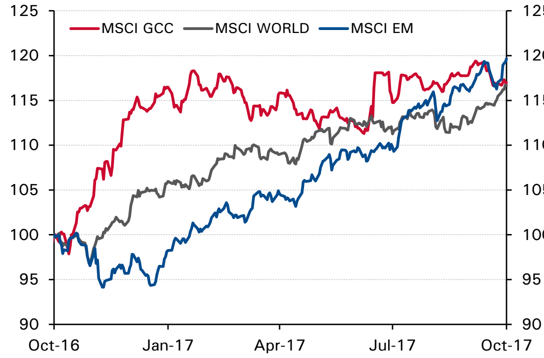
Turkey: Inflation rose to a near multi-year high of 11.2% y/y in September, on pressures from higher oil prices and a weak lira. There may have also been some seasonal impact from the long Eid holiday. With inflation remaining well above the central bank's 5% target, the monetary stance is projected to remain tight despite continued pressure from President Erdogan to lower interest rates.

Markets – oil

The oil rally cooled this week as traders foresaw supply disruptions to refineries from Hurricane Nate that hit the US Gulf of Mexico this past weekend. The dip reversed the trend that was supported by geopolitical tensions, supply cuts, and an improved demand outlook. Brent and WTI closed the week at $55.6/bbl and $49.3/bbl, respectively, with WTI down the most by 4.6% week-on-week (w/w) and Brent down 3.3% w/w.

Chart 9: Total return indices

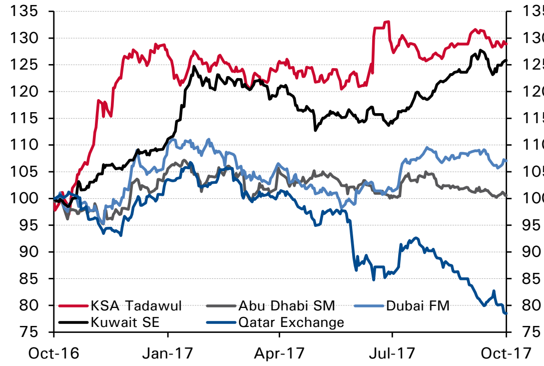
(rebased, 6 October 2016=100)



Source: Thomson Reuters Datastream

Chart 10: GCC markets

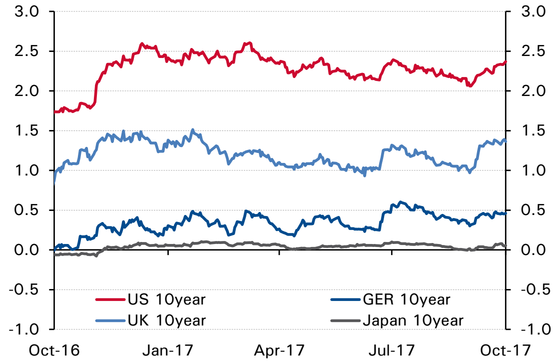
(rebased, 6 October 2016=100)



Source: Thomson Reuters Datastream

Chart 11: Global benchmark yields

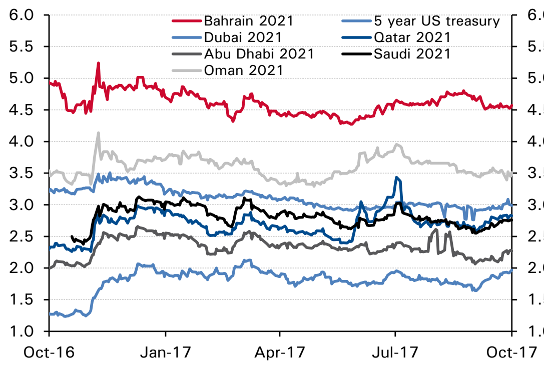
(%)



Source: Thomson Reuters Datastream

Chart 12: GCC yields

(%)



Source: Thomson Reuters Datastream

Profit-taking spurred by concerns over increased US shale production put downward pressure on prices in the week, along with a firmer US dollar. Fundamentals remain positive. The US Energy Information Administration's crude inventory report showed a fall of 6 million barrels in the week ending September 29, a second consecutive week of decline. Gasoline stocks, however, rose by 1.6 million barrels. Meanwhile, US crude exports jumped to 1.98 million barrels per day in the same week, driven in part by the widening difference between Brent and WTI prices. (Chart 8.)

Markets – equities

Most equity markets advanced last week, buoyed by strong economic releases. The MSCI World All Country index closed up 1.2%. US equities were back to making new highs as the likelihood of a December Fed rate hike increased again. The S&P 500 and DJIA closed up 1.2% and 1.6%, respectively. In Europe, developments surrounding Catalonia's bid for independence saw Spanish equities plunge, with the IBEX 35 down 1.9% on the week. Other European stock markets appeared unaffected by events in Spain, with the Euro Stoxx 50 edging 0.2% up on the week. Emerging market (EM) equities rebounded after the previous week's sell-off with the MSCI EM advanced 2.2%. (Chart 9.)

Regional markets were mixed with the MSCI GCC closing up 0.1%. The main event last week was Kuwait's upgrade to EM status by FTSE Russell which saw the market's weighted index gain 1.8% on the week. Kuwait could see passive inflows of $600-$800 million as a result of the upgrade. FTSE was also expected to upgrade Tadawul, but decided to hold off and reconsider in March 2018. Tadawul's general index was down 0.3% on the week. Meanwhile, Qatar saw another week of heavy selling with its index closing the week down 2.2%. (Chart 10.)

Markets – fixed income

Yields oscillated within a tight range last week as global risk events were pitted against stronger data. A tense Catalonian secession brought back political risk to the Eurozone. Uncertainty over US non-farm payrolls following hurricane season also added to the mix. This saw last week's tax-led "Trump trade" fade. Strong US data (see USA section), however, bolstered sentiment and helped keep interest rate expectations on track. Markets now expect a December rate hike with about 90% certainty. 10-year US Treasuries ended the week 4bps higher at 2.37% and Bunds held steady at 0.46%. (Chart 11.)

GCC sovereign yields ended the week mixed. While yields for Qatar 2021 held steady, yields for Dubai 2021 and Kuwait 2022 were down between 1-2 bps. Saudi 2022 yields were also down, falling by a further 5 bps and ending the week at 2.80%. Meanwhile, Abu Dhabi 2022 yields jumped by 14 bps following its $10 billion bond issuance. (Chart 12.)

Abu Dhabi issued a $10 billion triple-tranche bond that included for the first time a 30-year maturity. Strong demand helped the sovereign sell its offering at relatively tight spreads. It sold $3 billion in 5-year debt at 65 bps over Treasuries, $4 billion in 10-year bonds at 85 bps over Treasuries, and $3 billion in 30-year debt at 130 bps over Treasuries. The issuance was 3-times oversubscribed. This follows its previous well-received $5 billion issuance from May 2016.

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