بنك الإمارات دبي الوطني
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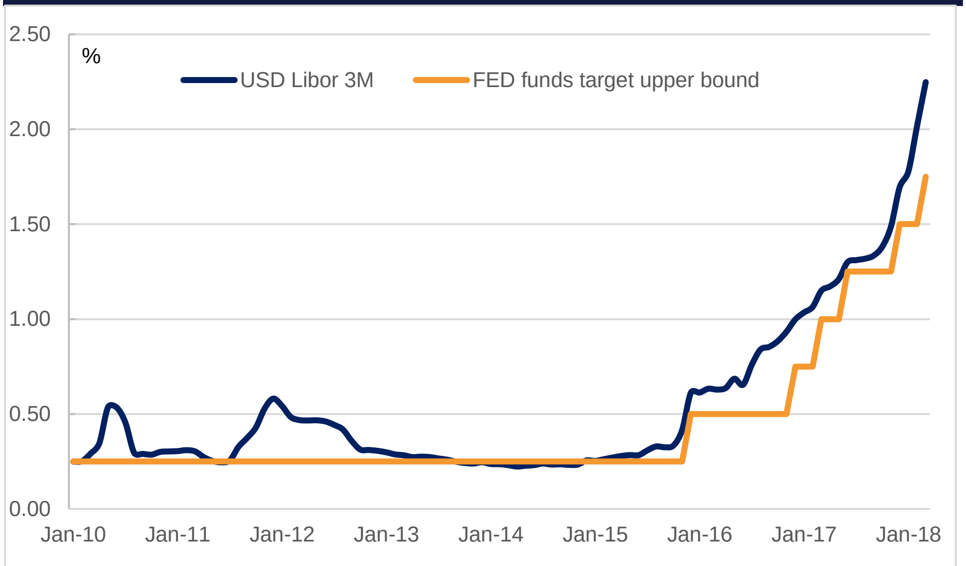
Monthly Insights

Central banks are continuing the process of monetary policy normalization, with rising interest rates in some cases and preparation for tightening in others. This is consistent with the improving condition of the global economy, although trade tensions are beginning to cast a cloud over the longer term outlook.

- **Global macro:** The last month has been dominated by talk of protectionism and fears that the world may descend into a trade war having negative consequences for global growth.
- **GCC macro:** The growth in bank deposits and slowdown in lending in the region's two largest economies have led to improved liquidity in their domestic banking sectors, contributing to the spread compression over short term USD rates.
- **MENA macro:** Monetary policy in Egypt, Tunisa and Turkey will diverge from the US-led trend of moderate hiking over 2018. Egypt has begun cutting rates from recent highs, Tunisia is being forced to hike aggressively to contain inflation, and Turkey is likely to hold rates despite above-target inflation.
- **Sector focus:** An update on Dubai's real estate sector.
- **Interest rates:** Government yield curves flattened during the month as short term rates rose in response to strong economic data.
- **Credit:** Rising fears of trade wars and the risk of capital outflow from EM markets on the back of rising US rates caused credit spreads to widen during the month.
- **Currencies:** Despite the Fed hiking rates again this month, the dollar continues to be under pressure and looks vulnerable as trade concerns grow.
- **Equities:** The first quarter of 2018 has marked the transition of global equity markets from 'low volatility & high total return' phase to 'increasing volatility and declining total return' phase. While most factors supporting equity markets still remain in place, investors' have been surprised at the speed with which some anticipated risks have manifested.
- **Commodities:** The US has imposed tariffs on imports of aluminium and steel but we hold that China's policies related to curbing over-production and pollution will have more bearing on aluminium markets this year.

Fed funds target rate & USD Libor



Source: Bloomberg, Emirates NBD Research.

Content

Global Macro

Trade war fears grow

The last month has been dominated by talk of protectionism and fears that the world may descend into a trade war having negative consequences for global growth. With the U.S. announcing tariffs on imports of steel and aluminum, markets have become fearful at the prospect of other countries retaliating. All of this is occurring, however, at a time when the global economic backdrop is a positive one, with both the IMF and the OECD forecasting global GDP growth of close to 4% and with world trade volumes improving.

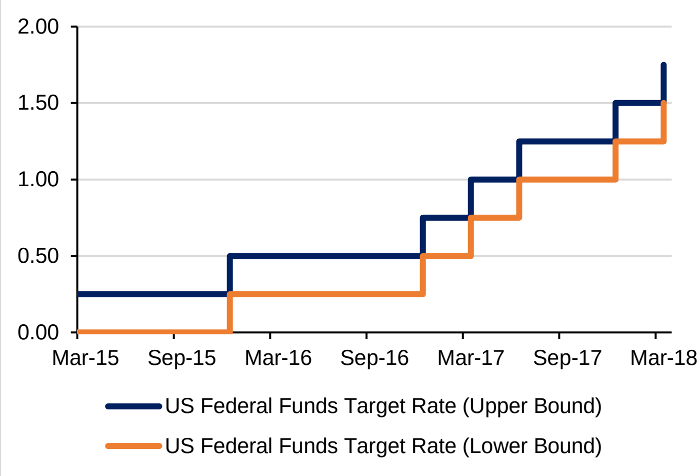
It might be tempting to dismiss the imposition of steel and aluminum tariffs as a one-off that will not be repeated across other sectors, but the signs are becoming ominous that this will not be the case. The balance of personnel at the White House has tilted significantly towards protectionism in recent weeks, most notably with the departure of Gary Cohn as Trump's Chief Economic Adviser, and with trade hawks such as Commerce Secretary Wilbur Ross and Peter Navarro now in the ascendency. The U.S. political calendar, with mid-term elections due in November, also makes trade an issue that is likely to be exploited for maximum political advantage in coming months, with protectionist rhetoric having played a significant part in Donald Trump's 2016 election win.

US steel and aluminum tariffs an opening shot

U.S. steel tariffs are likely to be an opening shot in a bigger trade war with China, with USD60bn of further tariffs rumoured as likely to be announced in the coming days targeting technology, telecommunications and intellectual property. The U. S. Treasury is also preparing its annual report on foreign exchange manipulation which could also be used to target China.

The reactions of other countries could also make an outright trade war a more protracted risk, and with it hasten the possibility of a resumption of slower growth and maybe even a return to recession. NAFTA negotiations, which are already progressing slowly, could easily break down. The EU has already prepared counter measures on EUR2.8bn of imports from the U.S., even as it is also making its case for special exemptions. Asian countries were already targeted with tariffs on washing machines and solar panels in January and are also likely to seek exemptions, but eleven have also signed a new Trans Pacific Partnership, after the U.S. withdrew from the original one last year, a move that underlines a sense of growing alarm. China of course holds the ultimate financial retaliation card, which would be the unloading of its USD1.18 trillion holdings of U.S. Treasuries, or at least slowing or halting its purchases of new Treasuries, something that Chinese officials have warned about. This could complicate plans by the U.S. to increase borrowing to finance wider budget deficits, by forcing U.S. bond yields higher and undermining U.S economic growth. More likely in the first instance China's countermeasures will revolve around imposing tariffs on US agricultural products. The GCC has specific exposure to the tariff's first round effects through UAE aluminum exports, but increasing dependence on global trade maintains a vulnerability to wider second round effects as well. Far from being 'easy to win' as Donald Trump has said, a trade war is likely to prove very difficult to reverse in the context of an already challenging and complex global environment.

Fed hikes rates 25bps

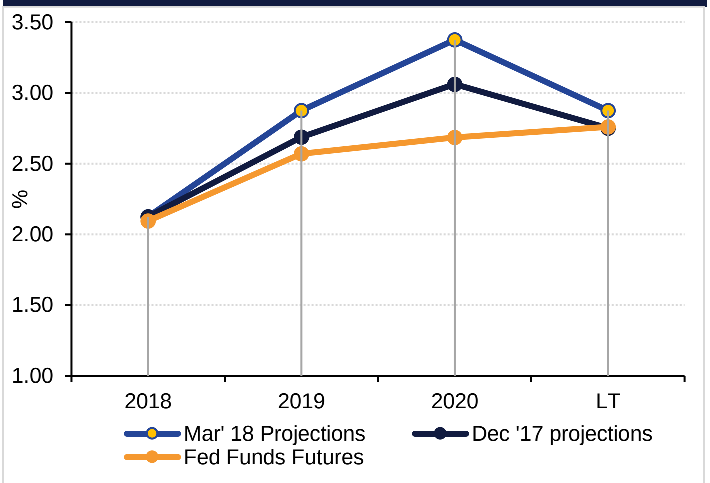


Source: Bloomberg, Emirates NBD Research

Central banks remain positive for now

For the time being, however, central banks and policy makers are responding to the other positives currently underway in the world economy, by raising interest rates in the Fed's case, and by preparing the markets for monetary policy normalization steps in others. The Fed hiked its rate band 25 basis points to 1.50%-1.75% at its March meeting as anticipated, in a unanimous decision, and retained the dot plot at 3 hikes for this year. However, the number of officials anticipating four rate hikes doubled to six, and the dot plot for 2019 was raised to 3 from 2, and for 2020 to 2 from 1.

…and raises projections



Source: Bloomberg, Emirates NBD Research

Fed upgrades its forecasts

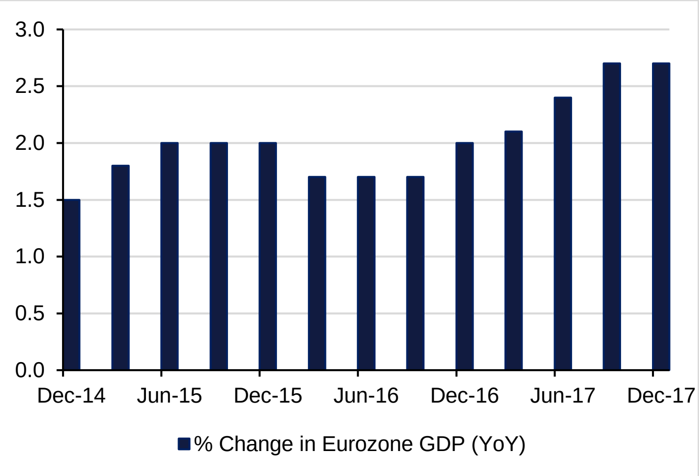
The Fed's statement introduced the view that 'the economic outlook has strengthened in recent months,' and highlighted that job gains have been strong. The change in the statement accompanied hikes in the GDP estimates and downward revisions in the unemployment rate forecasts. The median expectation for growth was raised to 2.7% this year (from 2.5%) and 2.4% in 2019 (from 2.1%), while the unemployment rate is now expected to drop to 3.6% next year. Despite these, the median forecast for core PCE inflation was raised only a little to 2.1% for 2019 and 2020 (2.0% previously), although this still implies that Fed officials now anticipate a slight overshoot in inflation over the next few years.

Powell was asked about the prospects for a trade war and the impact this might have on the Fed's forecasts, and although he acknowledged the risks he did not see it yet affecting the economic outlook.

ECB removes easing bias

The ECB removed the 'easing' bias from its monetary policy statement this month while maintaining asset purchase at EUR30bn per month until September, and possibly beyond that, depending on inflation data. It revised the Eurozone GDP forecast for 2018 up slightly to 2.4% (from 2.3% previously), though, highlighted the downside risk to growth from increased protectionism. The ECB also revised the inflation projection slightly downwards to 1.4% for 2018 and 2019. Still, with ECB officials increasingly convinced that underlying inflation has turned a corner and that the output gap is closing, the weaker numbers are unlikely to prevent the central bank from phasing out QE later this year and starting to eye rate hikes next year.

Eurozone recovery continues

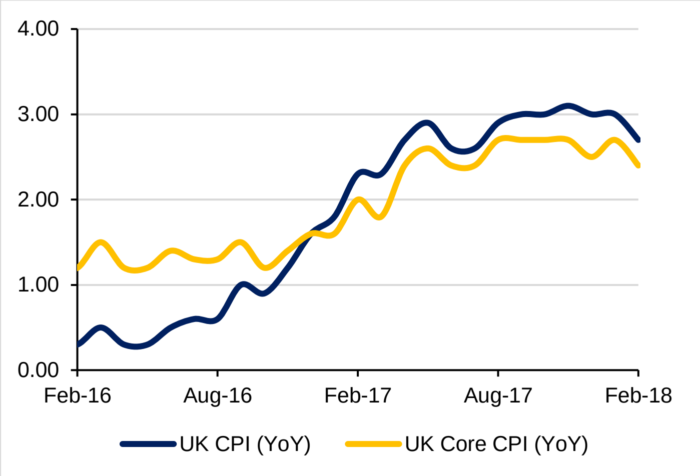


Source: Bloomberg, Emirates NBD Research

BOE expected to be next central bank to hike

Market implied probability for a Bank of England rate hike in May currently stands at 65.3%, even as inflation was softer than expected in February dampening tightening conjecture a little. The headline CPI rate fell to 2.7% y/y from January's 3.0% and core CPI dropped to 2.4% y/y from 2.7% y/y previously. Lower fuel prices and the fading impact of sterling's past appreciation contributed to the decline, with the biggest downward contributions coming from falls in transport and food prices. PPI input and output prices also came in below forecasts, at 3.4% y/y and 2.6% y/y respectively. It is probably a little too early to judge whether the softer price data will deter the Bank of England from raising interest rates in May, which has been expected, with another two months of data yet to be seen.

UK inflation retreats



Source: Bloomberg, Emirates NBD Research

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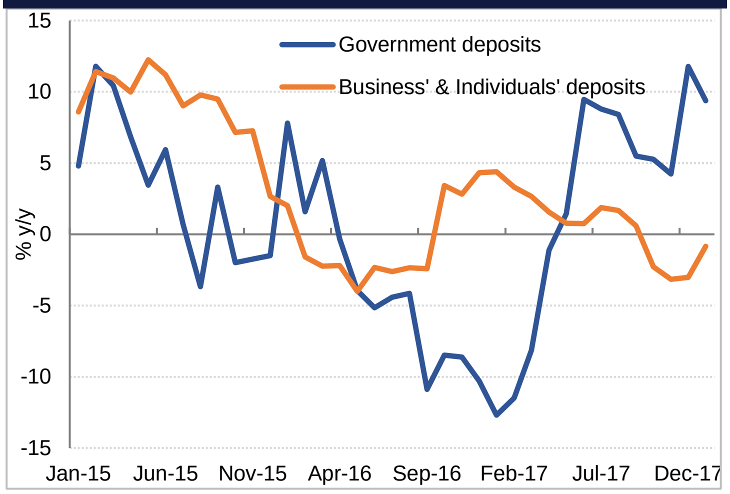
GCC Macro: Banking system liquidity improves

Recent focus has been on the negative spread between SAR and AED 3m interbank rates and 3m USD LIBOR, which has not been seen since the financial crisis and which likely prompted a surprise 25bp rate hike by SAMA last week. While higher 3m USD LIBOR has contributed to this phenomenon, the growth in deposits and slowdown in lending in the region's two largest economies has also been a factor.

Saudi Arabia: Higher oil prices, less domestic debt issuance and declining private sector credit growth

Following the sharp decline in oil prices in 2015-16, governments in the region drew down their deposits in domestic banks to meet their expenses. In Saudi Arabia, government deposits in commercial banks declined by nearly 1% on average every month in 2016, and were down more than 10% over the year. The trend was exacerbated by declining business & indivuduals' deposits as well. At the same time, Saudi Arabia started issuing domestic bonds to help finance the budget deficit, which contributed to an overall tightening in liquidity conditions in the Kingdom, as private sector credit growth also remained relatively robust through Q3 2016.

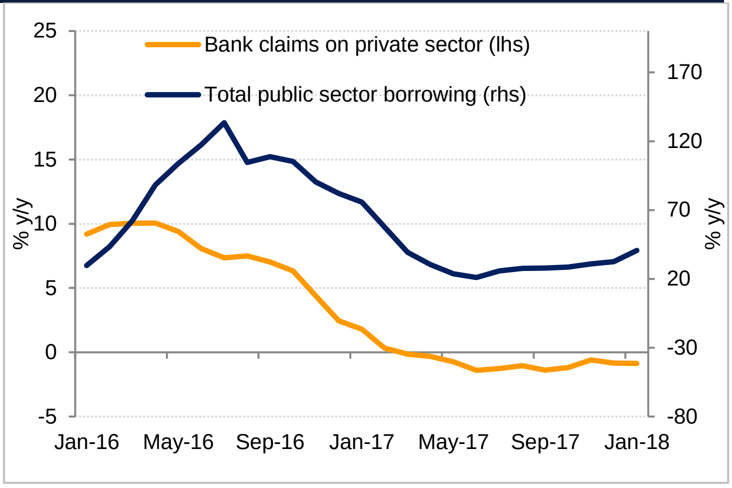
Saudi commercial bank deposits by source



Source: Haver Analytics, Emirates NBD Research

As oil prices recovered during the course of last year, government deposits at commercial banks recovered, as did private sector deposits. The government issued less domestic debt and supplemented this with external debt issuance. Importantly, private sector credit growth slowed sharply in 2017, reaching -0.8% y/y in December 2017, compared with 2.4% in December 2016. In short, the liquidity conditions in the domestic banking system improved dramatically in recent months.

Saudi credit growth

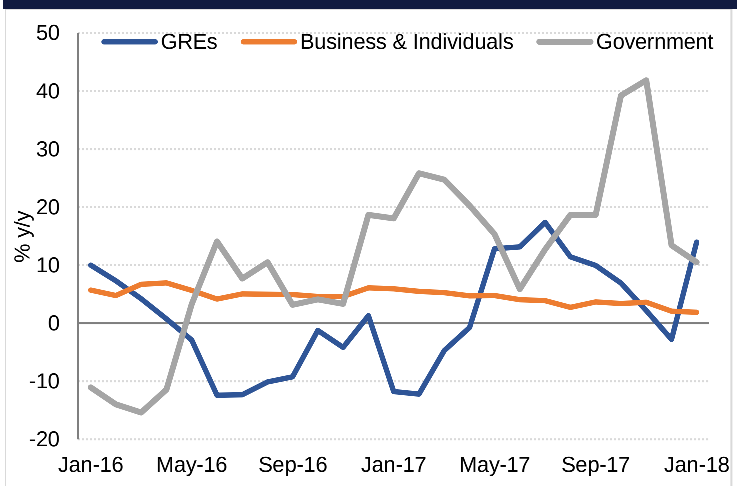


Source: Haver Analytics, Emirates NBD Research

UAE: Public sector bank deposits recover and private sector credit growth slows

The story is similar in the UAE, with government deposits rebounding in 2017 while private sector credit growth slowed sharply. After declining sharply in Q1 2016, government deposits in the domestic banking system started to recover from May 2016 and growth in government deposits accelerated in 2017, peaking at 41.9% y/y last November. In addition, GRE deposits also rebounded in H2 2017 after declining for most of 2016. Corporate and individual deposit growth slowed however, and non-residents' deposits declined outright by end-2017.

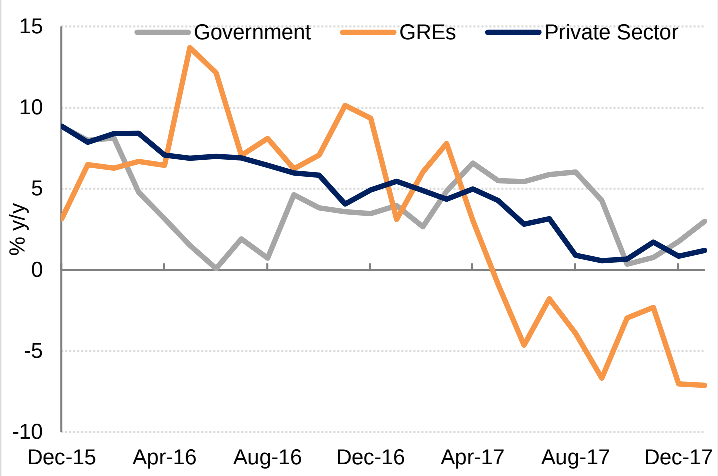
UAE commercial bank deposits by source



Source: Haver Analytics, Emirates NBD Research

Overall, bank deposits in the UAE grew 4.2% y/y in December 2017, slower than in December 2016. Deposit growth slowed further in January 2018 to 3.8% y/y. So deposit growth by itself is not sufficient to explain the 'excess liquidity' in the interbank market. Weaker private sector credit growth has also contributed. Bank loan growth eased to under 1% y/y in September and October 2017, and increased only modestly to 2.0% y/y in January. This is a slower rate of growth than in bank deposits, and the gross loan to deposit ratio stood to 97.9% (January 2018), compared to 104.7% in August 2016.

UAE bank loan growth by borrower



Source: Haver Analytics, Emirates NBD Research

The credit sentiment surveys conducted by the UAE central bank suggest that weak demand was the main driver of lower credit growth during the course of last year, rather than a tightening in lending standards. Regardless of the reason, the consequence of solid deposit growth and weaker lending growth has been an increase in liquidity in the domestic banking system, which has contributed to the tighter dirham spread over USD LIBOR. Going forward, we expect private sector credit growth to recover as non-oil economic growth accelerates in 2018. At the margin, this suggests that further spread compression due to dirham liqudiity is limited in our view.

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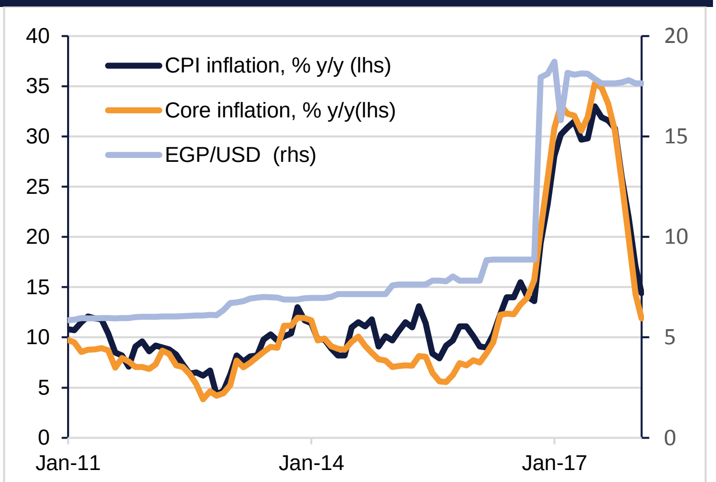
MENA Macro: Diverging monetary policy

Egypt, which began its monetary policy easing cycle in February, is something of an outlier in the broader Middle East region, cutting rates while most neighbouring countries are set to tighten policy in line with the global trend - we expect most of the dollar-pegged oil-exporting countries to hike in line with the US Federal Reserve this year. It is not only Egypt that is bucking the trend of raising rates in tandem with the US. In Tunisia, the central bank has already implemented a significant rate rise earlier in March, and we expect further hikes to its own timetable as it contends with very high inflation. In Turkey, meanwhile, the likelihood is that rates will be maintained over the next several months, despite inflation that is running at double the official target rate, as the focus remains on supporting strong real GDP growth.

Steady normalisation of policy ahead in Egypt

In February, Egypt made its first benchmark rate cut since it embarked upon its IMF-sponsored reform programme in November 2016, and we anticipate three further 100 bps cuts over the remainder of 2018. The Central Bank of Egypt (CBE) implemented a cumulative 700 bps of hikes in the wake of its IMF deal, anticipating the very high inflation which followed the removal of the Egyptian pound's peg to the dollar. As the currency lost around half of its value against the greenback, price growth rose to over 30.0% through much of 2017.

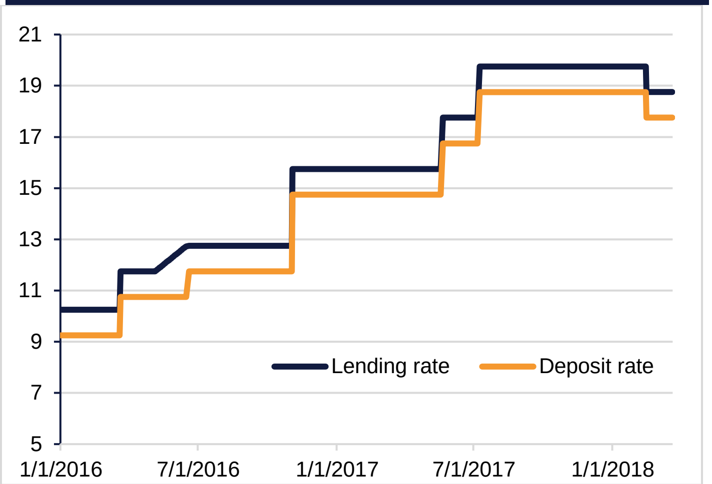
Egypt inflation & EGP



Source: Haver Analytics, Bloomberg, Emirates NBD Research

Given that inflation has fallen sharply in recent months, there is scope for the CBE to cut rates more rapidly than we anticipate. The fall in core inflation to just 11.9% in February – the lowest level since April 2016, months before the currency devaluation – could prompt the bank to enact a greater-than 100 bps cut in March as a sop to consumers. Our view that the bank will be more cautious is predicated on three factors. First, the IMF maintains strong support for high interest rates in Egypt, urging in its most recent review that Egypt 'consider a gradual easing of policy interest rates only once the authorities are confident that demand pressures and inflation expectations remain contained.' Second, and related, inflationary pressures are set to rise once more in July, when further subsidy cuts are implemented at the start of the new fiscal year. Third, the bank will be wary of cutting too sharply and seeing the strong portfolio investment enjoyed of late drop off, as other high-yielding markets such as Argentina and Nigeria gain in relative attractiveness.

Egypt key interest rates, %



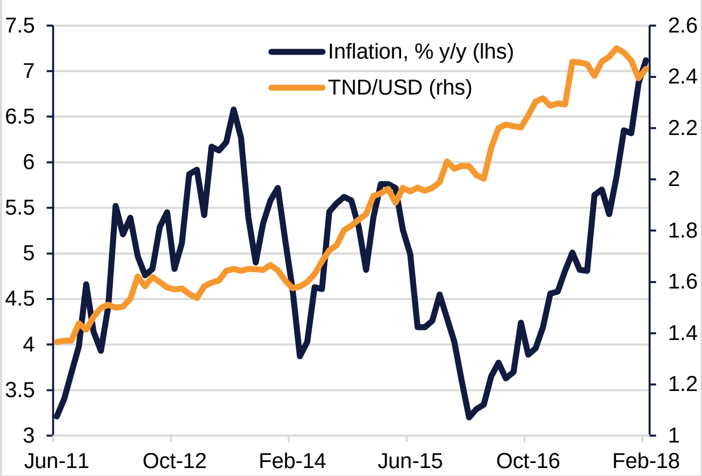
Source: Haver Analytics, Emirates NBD Research

Whether the CBE meets or exceeds our expectations in terms of its rate-cutting this year, easing monetary policy will be one of the factors behind strengthening real GDP growth in Egypt. The bank noted in its last communiqué that the improvement to date had been driven by an adjustment in the external position and greater public investment. With easing monetary policy, private consumption will come to bolster this also. The monetary easing that has now begun is testament to the textbook success of the reforms pushed through by President Sisi's government over the past 18 months. While there has been significant hardship, there is a sense that the country has now come through the worst.

Deteriorating conditions force tightening in Tunisia

In contrast to Egypt, Tunisia is at the opposite end of its cycle, and tightening monetary policy will be a further impediment to already weak anticipated real GDP growth this year. In March, the central bank was forced to hike its benchmark interest rate by 75 bps to 5.75% in a bid to 'to face up to the real risks of ongoing inflation in 2018'. The bank is already contending with spiraling price growth which at 7.1% in February is at levels not seen in 20 years. This has been prompted by austerity measures and a weakening currency, and is set to climb higher still over the coming months. Higher global oil prices will feed into higher prices at the pump, and further dinar weakness is anticipated, adding to inflationary pressures. Newly appointed Banque Centrale de Tunisie (BCT) Governor Marouane El Abassi, said in March that the bank could not defend the dinar 'even if it wanted to' given that reserves have dwindled to less-than-three-months' import cover.

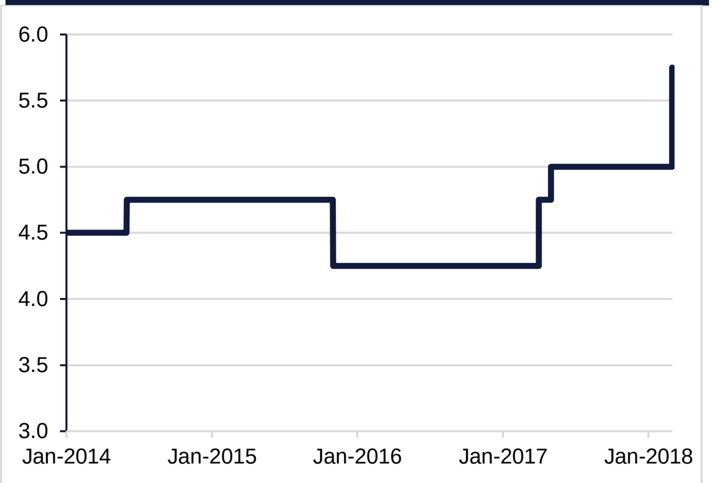
Tunisia inflation & TND



Source: Haver Analytics, Emirates NBD Research

The BCT has itself raised the likelihood of more rate hikes this year, and we envisage a further 75 bps in 2018. While essential for macroeconomic stability, this will be a blow to an economy which continues to struggle with the aftereffects of its 2011 revolution and terrorist attacks in 2015. Moody's downgraded Tunisia to B2 in March, citing its growing debt burden and ongoing fiscal difficulties. A series of governments since 2011 have struggled to fully implement much-needed reforms in the face of popular opposition, dragging out the recovery process.

Tunisia key interest rate, %



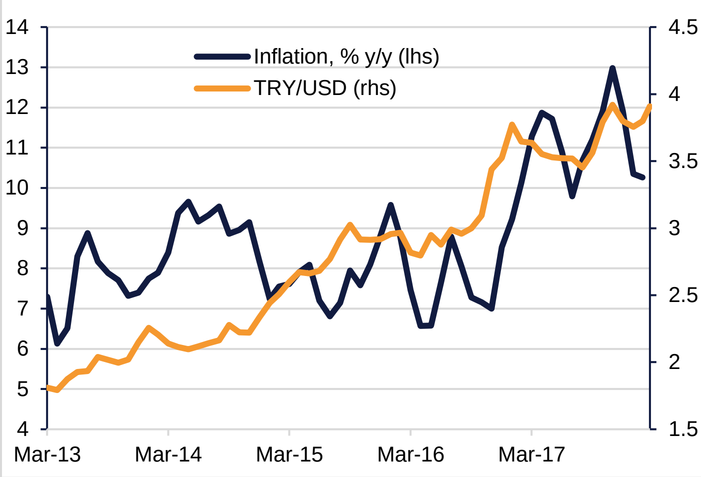
Source: Haver Analytics, Emirates NBD Research

Turkish monetary policy trajectory uncertain

Like Tunisia, Turkey was also downgraded by Moody's in March on the back of a host of challenging conditions, including high inflation which has consistently posted above 10.0% y/y over the past 12 months. This is the first time double digits have been broached since 2012, and is double the 5.0% target rate. However, while high inflation, a weak currency, and hikes in the US might usually presage further rate hikes, the likely trajectory of monetary policy in Turkey is complicated by government guidance against high rates of interest, and a hike is unlikely over the coming quarters.

While inflation has fallen modestly over the past several months, from 13.0% in November to 10.3% in February, a renewed sell-off in the Turkish lira and higher oil prices will keep inflationary pressures to the fore. The Central Bank of Turkey raised its late liquidity rate – the highest of the four rates used by the bank to direct monetary policy – by 50 bps in December as inflation remained high. However, this fell short of market expectations, and rates were maintained at the bank's last MPC meeting on March 7.

Turkey inflation & TRY



Source: Haver Analytics, Emirates NBD Research

While supportive of growth, relatively easy monetary policy, combined with ongoing loose fiscal policy, raises the risk of the Turkish economy overheating. With the US Fed having hiked by 25 bps points on March 21, and projecting a further two such hikes this year, a failure to maintain the interest rate differential in Turkey, especially as political risk is to the fore, could see the lira exceed the TRY4.0000/USD level for the first time in the pair's history as investors become more wary. Hot money inflows are essential to the country's economic stability given its persistent current account deficit and failure to attract sufficient levels of fixed investment to cover it. That said, bids for Turkey's 10-year debt auction on March 20 exceeded that offered by five times, indicating that for now there remains significant appetite for Turkish debt despite mounting challenges.

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Sector Focus: Dubai Real Estate

Real estate services sector grew 7.9% y/y in Q3 2017

The real estate services sector accounted for 6.6% of Dubai's GDP in Q3 2017. Growth in the sector accelerated to 7.6% y/y in Jan-Sep 2017 from 7.1% in Jan-Sep 2016 and just 3.5% in the same period of 2015, according to the latest data from Dubai Statistics Centre (DSC). Higher interest rates, declining rents and increasing housing supply are likely to remain headwinds for the sector in 2018. However, given the more upbeat outlook for the GCC economies, oil prices, VAT exception for residential transactions as well as better global growth prospects, we expect the downside for residential real estate to be limited this year. Overall, Dubai's economy expanded 2.9% y/y in the first nine months of 2017. Although this is below our full year GDP estimate of 3.5%, we believe that growth accelerated sharply in Q4 2017 as consumers and businesses brought forward purchases and boosted output ahead of the introduction of VAT in January this year. We estimate Dubai's growth to accelerate to 4.0% in 2018.

Dubai's real estate services sector growth

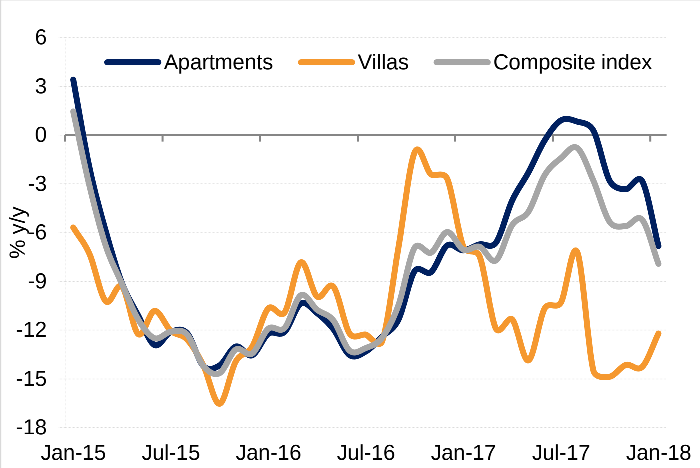
Source: Dubai Statistics Centre (DSC), Emirates NBD Research

Pressure on residential real estate prices eases in 2017

The latest data on Dubai's residential real estate prices[1] (Phidar Advisory's 9/5 House Price Index) show than on average prices fell another -4.6% in 2017. The total decline since the 2014 peak is -23.4%. Phidar Advisory's Dubai 9/5 House Price Index, which is based on Dubai Land Department data (DLD) from nine apartment communities and five villa communities in investor zones in Dubai, indicated that apartments fared better than villas. Apartment prices declined just -2.8% in 2017 compared with a -11.4% fall in freehold villa prices. Low-range properties held their values better than the premium and the mid- costs segments. Phidar Advisory expects residential real estate prices to recover modestly in 2019 and rise further in 2020-2021.

The softness in residential real estate prices continued at the start of 2018 with apartment prices again faring better than villas in January. Apartment prices were down -6.8% y/y, recording the highest annual decline since January last year while villa prices fell -12.2% y/y the same month as the graph below shows.

Dubai residential property prices



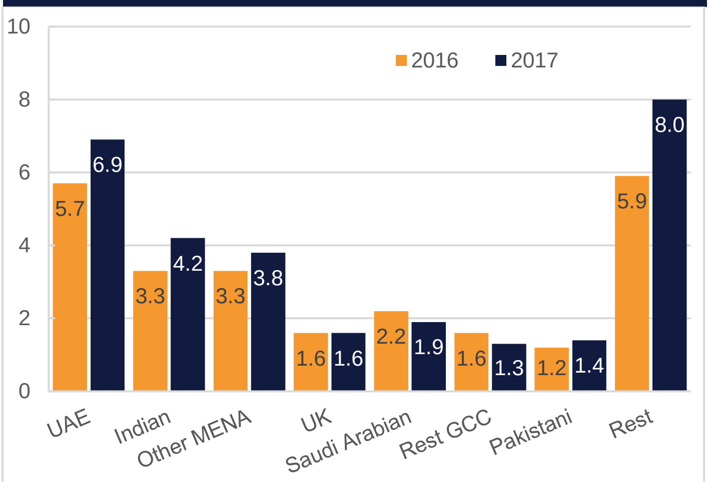
[1] We have used a composite price index based on Phidar Advisory's 9/5 House Price Indices. Apartments have an 80% weight in the composite index, and villas 20%.

Source: Phidar Advisory, Emirates NBD Research

Strong investor confidence supporting the real estate market

The value of real estate investments reached USD 29.1bn in 2017, up by 17.3% compared with the -32.6% decline in 2016, according to Dubai Land Department (DLD). Dubai's property market attracted investors from all continents with UAE nationals topping the list at USD 6.9bn or 23.6% of the total. India ranked second (USD 4.2bn), followed by Saudi Arabia (USD 1.9bn), UK (USD 1.6bn), and Pakistan (USD 1.4bn). Other top investors in Dubai's real estate include citizens from China, Jordan, Egypt, and Canada.

Investment in Dubai real estate in USD bn



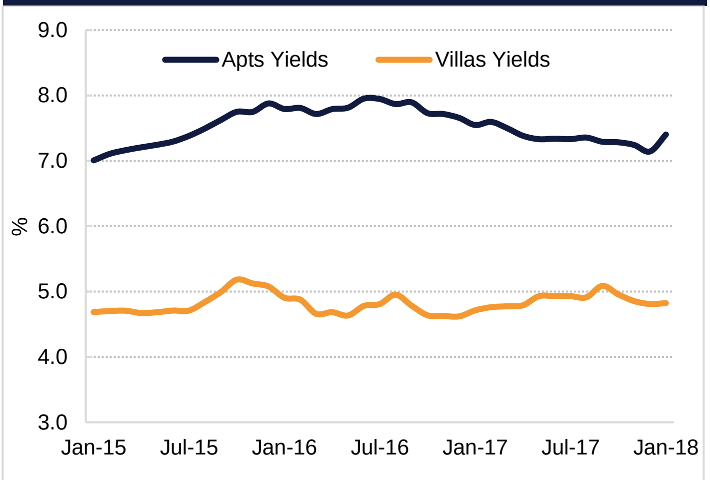
Source: Dubai Land Department (DLD), Emirates NBD Research

Volumes growth turns positive in 2017

The slower contraction in residential real estate prices over 2017 has been accompanied by higher transaction volumes in all areas of Dubai. This has been particularly evident in the apartments sector. Overall transaction volumes increased 0.7% y/y in 2017 compared with -20.4% decline recorded in 2016. However, in January 2018, total sales were down by -20.0% y/y due to lower apartment transactions (-23.6% y/y). The number of villas sales recorded in January was up by 14.0% y/y. Looking at the freehold areas included in Phidar Advisory's 9/5 Index, overall transaction volumes have fallen -17.5% y/y in 2017, mainly driven by the significantly lower transaction volumes on villas.

Separately, rents in the Dubai 9/5 Index areas have declined on an annual basis in 2017, more or less aligned with the annual fall in sales prices. Average apartment and villa rents were down in 2017 by -8.4% and -9.2% y/y, respectively. Overall however, yields on villas remained unchanged in January 2018 at 4.8%, slightly below the 2017 average of 4.9%. Gross rental yields on apartments have moderated since Q2 2016, but remain attractive by global standards at 7.1% in January and 7.4% for the whole 2017.

Dubai rental yields



Source: Phidar Advisory, Emirates NBD Research

Grade A office prices declined at slower pace in 2017

The Dubai office market declined at a slower pace in 2017 with Phidar Advisory's commercial price index showing than on average overall office prices fell -8.9% y/y in 2017, with the high quality segment (Grade A) recording the lowest decline last year, down -5.4% y/y. On a m/m basis, the average monthly price decline for offices in 2017 was -0.9% per month compared with -1.5% per month in 2016.

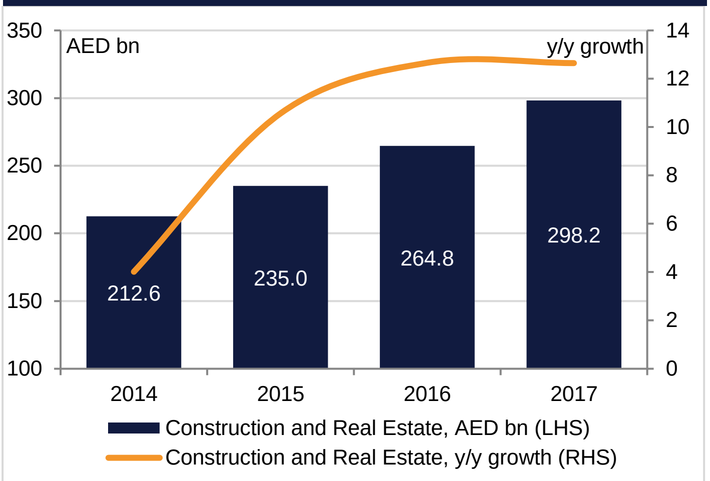
The fall in commercial real estate prices continued in January 2018 with Grade A prices again faring better than the rest, down -10.8% y/y, recording the highest annual decline since February last year. Grade B and Grade C prices also fell -11.9% and -13.5% y/y the same month, respectively.

Rents for Grade A buildings were down -6.3% y/y in 2017. Rents in the remaining areas however declined at a slower rate for the same period, more or less aligned with the annual fall in sales prices. Overall, office rents were down in 2017 by -6.7% compared with -7.9% the previous year. Average yields on offices were slightly higher in 2017 at 7.8% compared with 7.6% in 2016 with the lower segment (Grade C) recording the highest reading last year at 8.2% compared with 8.3% in 2016.

Bank credit to construction & real estate sector robust

Lending to the construction and real estate sector expanded 12.6% y/y in 2017 to roughly AED 300bn, with loans to this sector accounting for 20.5% of total bank loans. Demand growth for business loans increased in Q4 2017 compared with the previous quarter and is expected to improve further in Q1 2018 according to the latest credit sentiment survey by the UAE Central Bank. Overall, demand for business credit has increased marginally in Q4 2017 mainly attributed to the strengthening in demand in Dubai. We expect credit to construction and real estate to increase in 2018 backed by the recovery of the construction sector activity last year and the number of projects underway gearing up to the 2020 Expo.

Bank credit to construction & real estate



Source: UAE Central Bank, Emirates NBD Research

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Interest Rates

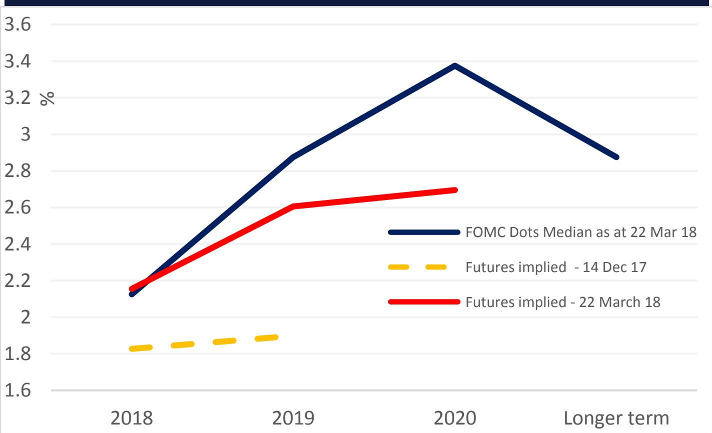
The rates market had a mixed month with shorter dated yields in the developed world rising in contrast to stable to declining yields in the longer end and a capital-outflow-fears related widening in EM bond yields.

US Rates

After raising rates by 25bps this week, Federal Reserve stuck to its projection of only two more rate hikes this year even though GDP growth and inflation projections were revised upwards. Given the strong economic data out of the US, the market implied probability of the number of rate hikes this year has crossed the level implied by the Federal Reserve's dot plot and currently indicates slightly more than two more rate hikes this year. However a lack of significant wage growth pressures, steady core inflation and a subdued dollar kept the view on long term yields dim. UST curve flattened with yields on 2yr, 5yr, 10yr and 30yr closing yesterday at 2.30% (+5bps m/m), 2.66% (+1bp), 2 .87% (-6bps) and 3.10 (-11bps m/m) respectively.

Headline inflation expectations, as implied by 5yr TIPS yields has increased from circa 1.57% in mid 2017 to 2.17% now, however remains below the 2.32% in March 2014. The 10yr TIPS yield implied inflation is at circa 2.12%. Given that TIPS' trading volume is much lower than that of Treasuries, the yield differential can often change due to technical factors not having to do with real inflation expectations.

FOMC Dot Plot vs Market Expectations



Source: Bloomberg

We continue to call for two more rate hikes in 2018, consistent with the Fed's dots, although the positive impact on inflation from tax cuts and increased spending clearly represent upside risks. Interestingly, the number of Fed officials anticipating four rate hikes this year doubled to six at the March FOMC meeting, and the dot plot for 2019 was alo raised to 3 hikes from 2, and for 2020 to 2 from 1, indicative of a more hawkish slant.

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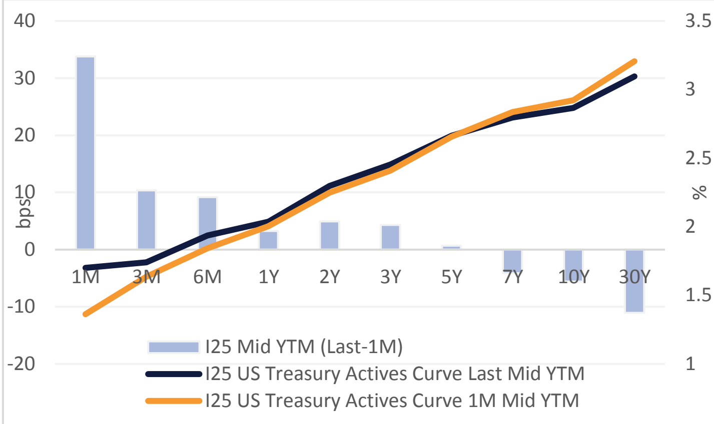
UST yield curve flattened



Source: Bloomberg

Global Rates

Data out of the Eurozone has consistently been stronger than expectations, but with the conspicuous exception being inflation, which is still subdued (headline at 1.2% and core at 1.0% in February). Despite the ECB removing its easing bias in its March meeting communication, the downward revision of inflation expectations caused short term yields to fall with 2yr Bund yields closing the month down by 7bps to -0.60%, followed by 9bps decline in 5yr yields to -0.02% and 11bps decline in 10yr yields to 0.59%. The yield differential between 10yr UST and Bunds increased to 229bps from 217bps mid last month and may put downward pressure on 10yr UST yields.

10Yr Government Bond Yields

	Yield %	1M chg	3M chg	12M chg
US	2.87	-6	+38	+46
UK	1.53	-2	+29	+35
Germany	0.59	+11	-1	-2
Japan	0.03	-2	-1	-2
Brazil	4.95	+2	+40	+37
Russia	4.54	+21	+68	+6

Source: Bloomberg

The rates market in the UK reflected the biggest moves during the month. Yields on 2yr Gilts were up 24bps to 0.91% in response to expectations of a rate hike in May this year. However the uncertain impact of Brexit kept yields on the longer end capped, thereby flattening the 2yr-10yr spread to 62bps from 95bps in mid February.

The JGB market was largely range bound during the month. Governor Kuroda's cautious attitude toward raising the long-term yield target suggests that he desires a considerably higher inflation hurdle for enacting any policy change. He clearly stated that the BoJ

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did not plan to conduct another comprehensive assessment of current monetary policy. We believe monetary policy in Japan will stay unchanged in 2019 and any revision of 10-year JGB yield target will only happen in 1H 2020.

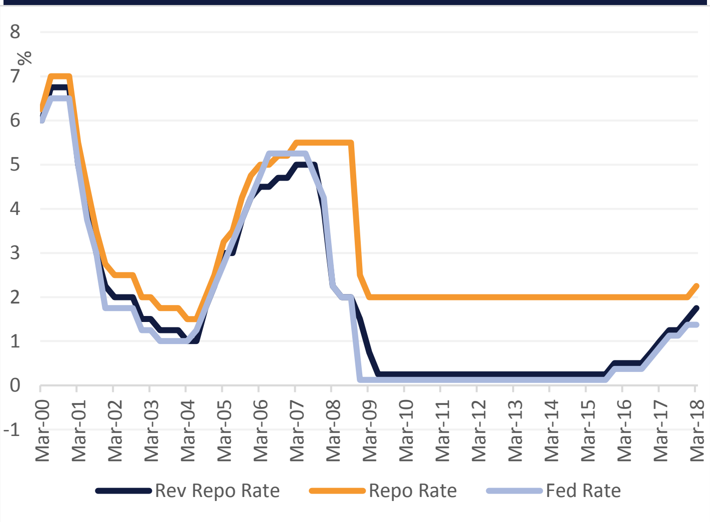
Contrasting the trend in the developed world, yields on emerging market sovereign bonds generally had a widening bias, partly because of the expectations of rate hikes in various economies and partly as a result of capital outflows. The PBOC in China has already raised interest rates following the Fed. Trade-tariff concerns likely took their toll on portfolio inflows. EM portfolio flows have turned negative in the recent past and though bulk of this outflow has been from the equity markets, bonds flows have also turned negative. Yields on 10yr Russia and Brazil increased 21bps and 2bps to 4.54% and 4.95% respectively.

Local Rates

Policy rates in the GCC generally move in tandem with those in the U.S. as the region's currencies are pegged to the dollar. Three GCC central banks, in the UAE, Kuwait and Bahrain have already followed suit with the Fed, by raising interest rates immediately following. Interestingly Saudi Arabian Monetary Authority (SAMA) has not raised rates today following its 'pre-emptive' 25bp rate hike last week, despite some speculation that it may do so following the Fed's actual decision.

Last week, SAMA raised its policy rates by 25bps, bringing the repo rate to 2.25% and the reverse repo rate to 1.75%. It had earlier decided to suspend its term repo facility for maturities of 7, 28 and 90 days. The recent negative spread differential between SAIBOR and LIBOR rates was likely the main reason for SAMA hiking before the Fed this time, rather than afterwards as it usually does.

KSA policy rates vs the Fed Target Rate



Source: Bloomberg

Going forward, we expect SAMA to raise both the repo and reverse repo rates in tandem with the Fed rate moves. However, last week's action has introduced some uncertainty regarding the timing of its future hikes.

Credit Markets

The combination of strong US growth and reduced signs of rising wage pressure were supportive of risk assets. However, rising fears of trade wars and risk of capital outflow from EM markets on the back of rising US rates caused credit spreads to widen during the month.

Global Bonds

Corporate bonds in the developed world had a month of positive returns as the UST yield curve flattened in response to no material increase in core inflation. Yields on 2yr, 5yr, 10yr and 30yr closed at 2.30% (+5bps m/m), 2.66% (+1bp), 2 .87% (-6bps) and 3.10 (-11bps m/m) respectively.The volatility index for US treasuries, MOVE Index, declined from a high of 72 in mid February to 56 now, noticeably below its 5 year average of 69 basis points. However, risk appetite for the EM exposure was dampened by negative trade related headlines, leading to widening of credit spreads which in turn caused negative total returns for EM portfolios.

European bonds outperformed with Euro aggregate index recording total return of 0.80% in the month ending 21 March compared with gain of only 0.05% for the US aggregate index as benchmark yields in Europe reduced more in response to ECB revising the Eurozone inflation expectation for 2018 and 2019 downwards. CDS levels on US IG and Euro Main had a widening bias as discomfort with possibility of trade wars increased, each closing the month four bps wider to 62bps and 58bps respectively.

Global Corporate Bond OAS (bps)

	OAS	1M chg	3M chg	12M chg
US IG Corp	106	+13	+13	-12
US HY Corp	338	-3	-4	-68
EUR IG Agg	50	+1	-2	-28
USD EM Agg	232	+10	+7	-38

Source: Bloomberg data as at 14 Feb 2018

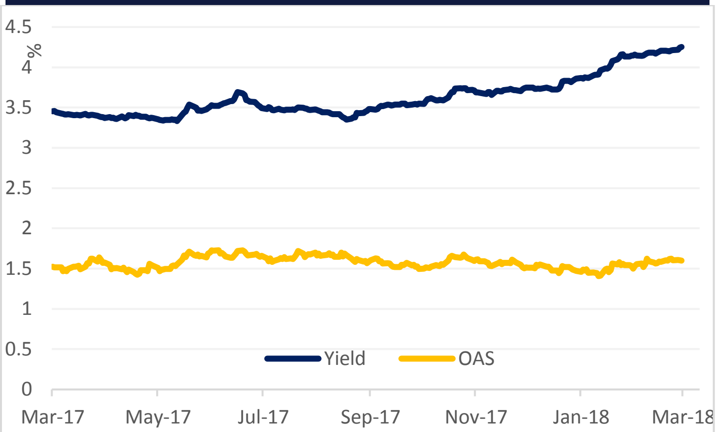
Despite solid economic growth, the fears of rising US rates causing capital outflow from the emerging markets, lead the USD denominated EM bonds generally down in price. Option adjusted credit spreads on EM USD index rose 10 bps to 232bps during the month and total return for the month was recorded to be a loss of -0.10%.

GCC Bonds – Secondary market

GCC credit markets had little idiosyncratic developments to trade on. Although oil prices rose 6% during the month, the impact of large new supply was evident on widening credit spreads. The yield on Barclays GCC bond index increased 10 bps to 4.25% and option adjusted spreads widened to 160bps (+10bps m/m). That said, longer dated bonds were well supported as the UST yield curve flattened.

We were expecting a positive first half of the year, and we certainly had a good start in January, but the winds have changed since then. February was a dampener and March so far has been a stop-start month with mixed newsflow. Credit spreads therefore are finding it hard to gain much traction. However, looking ahead, we still expect to see some credit spread tightening though pressure from technical cant be ignored.

Barclays GCC Credit Index: YTW and OAS



Source: Bloomberg data as at 14 Feb 2018

In contrast with the global trend where positive outlooks and upgrades are outnumbering the negatives, the credit rating trend in the GCC was negative. During the month, Bahrain was downgraded two notches to BB-/stable by Fitch which also lead to downgrade of the Bahrain government related GREs – Batelco and Oil & gas Holding co to (BB-/stable and Bahrain Mumtalakat Holdings to BB-/CWN. Despite the well anticipated nature of these downgrades, bonds from Bahrain underperformed the market. Even with benchmark yield tightening, Bahrain 47s fell more than two points to $92.10 and to Z-spread widening 28bps to 525bps.

Qatar's Ezdan Holdings was downgraded three notches from Ba1 to B1/stable by Moody's and one notch from BB to BB- by S&P. However the price impact on Ezdan bonds was muted given their relative value. ERESQD 21s closed the month close to its opening levels at $86.84 and yield of 9.28% (+8bps m/m). This compares with similar rated DARALA 22s trading at yield of 6.92% and DAMAC 22s trading at yield of 6.01%

On the positive front, Moody's revised the outlook on Dar-al-Arkan's B1 rating to positive citing improved revenue and profitability. DARALA bonds were amongst the best perfomring bonds during the month with DARAAL 22s gaining a point and closing at yield of 6.92% (-38bps) and Z-spread of 413bps (-48bps m/m).

Fitch's affirmation of TAQA's rating at A/stable was largely an non-event.

Emirates NBD called its $750 million subdebt EBIUH 4.875% 02/28/23 with first call date on 28 March 2018. The bonds were originally issued at 5yr MS+409.1bps. In current market conditions, the bank is likely to be able to refinance at better margins, particularly given the rating upgrade and improvement in financial strength in the last five years. Beside this sub-debt, perpetual securities issued by the bank, EBIUH 6.375% and EBIUH 5.75%, also faired well in the secondary market with yield-to-call tightening to 4.64% (-44bps) and 4.12% (-40bps) respectively last month.

Bond holders' dispute with Dana Gas remains unresolved with the local UAE court adjourning implementation of the UK court orders until it completes the hearing on 22 March. Other distressed bonds EAPART 20s and EAPART 21s fell further to $74 and $71 respectively. The issuer has announced commencement of remarking event for EAPART 21s after the liquidity pool fell below 75% of the required level as a consequence of default by Air Berlin and Alitalia

In a much anticipated move, Moody's cut Oman's rating by one notch from Baa2 to Baa3 and kept the outlook at negative. Moody's sees Oman's fiscal and external metrics continuing to weaken, with the current account deficit remaining wide at around 9% of GDP in the next few years. It also sees the country's real GDP growth remaining relatively subdued in the medium term and close to a full percentage point behind the population growth excluding expatriates. Despite wide spread expectations of the rating cut, the Z-spread on Oman government bonds widened with OMAN 28s closing at yield of 5.80% (+3bps) and Z-spread of 292bps (+6bps). We would expect ratings on Omani GREs to be cut soon in line with the sovereign rating change.

During the month Moody's released a report on the Saudi Banking System reflecting stable outlook as strong margins and increased government spending are expected to bolster profitability. As per Moody's, Saudi banks' profitability will remain the highest in the GCC (net income-to-tangible assets stood at 2.0% in 2017 versus 1.9% in 2016) even though NPLs will increase to around 2.5% in the next 12 to 18 months from 1.8% as of December 2017. Given low issuance from Saudi banks in the USD denominated bond space, the report had minimal impact on the market.

GCC Bonds - Primary Market

Year-to-date issuance from GCC based issuers is running at over $21 billion, auguring well to meet our full year forecast of between $75 billion to $90 billion. This compares with circa $27 billion done in the first quarter of 2017. Looking at the bulging pipeline of new issuers, as below, we expect new issuance to pick up pace in April ahead of upcoming Ramadan period in May this year.

- Oman Tel looking to raise $1.5 billion via USD bond.
- Doha Bank plans to raise $500k in 3Q.
- Al Ahli Bank of Kuwait hired banks for USD bond
- Kingdom of Saudi Arabia is expected to raise between 410 billion to $15 billion in the first half of this year.
- Bahrain sovereign has mandated banks for an international bond.
- Oman Oil Refineries is in talks for a USD bond sale.
- ADCB is currently roadshowing to raise funds via benchmark sized deal.

Secondary market performance of the bonds issued to date has been mixed. Bonds issued by the lower rated issuers have held up better compared with the high rated ones, which in turn is reflective of the macro back drop of rising interest rates.

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Currencies

USD ignores strong data

Recent economic data out of the US has been solid and would usually be constructive for for the dollar. The latest non-farm payroll report showed that 313,000 jobs were created in February, much higher than the anticipated 205,000 jobs and an improvement on the 239,000 jobs added in January. Furthermore, inflation continued to show upwards pressure with headline consumer price inflation at 2.2% y/y in February, from 2.1% the previous month and above the 2.0% Fed target. Survey evidence might also have given investors reasons to back the dollar with reports from the University of Michigan showing that consumer sentiment ticked up to 102.0 in March from 99.7 in February, better than the consensus expectation of 99.3.

Dollar Index remains under pressure

Source: Bloomberg

With rallies capped by fears over a pending trade war

However, sustained dollar rallies were made difficult by the announcement of protectionist policies from the Trump White House. These included tariffs on steel and aluminum (see Global Macro) which raised investor concerns about retaliatory measures elsewhere and resulting in safe haven bids. When combined with ongoing domestic political noise this caused a tendency by investors to be quick to take profit on dollar rallies.

…and a post FOMC sell-off

After the Fed dots stuck to three rate hikes this year (see macro), the dollar declined to a one month low, with the Dollar Index falling 0.65% to close at 89.783 yesterday. So far in the Asia session today, the DXY Index has fallen an additional 0.25% taking it to 89.55. The move of these last two days has taken the index back below the 50 day moving average (89.852) and bodes bearish for the dollar in the short term, a risk compounded by the 14 day RSI (Relative Strength Indicator) showing a bearish bias at 45.04. The next level of significant support will be the 38.2% five year Fibonacci retracement (88.423), an area which has halted declines on multiple occasions thus far in 2018. Should this level be breached, a larger decline towards the psychologically significant 85 level is a possibility.

Euro strength slows as inflation ebbs

Eurozone aggregate headline CPI fell to 1.2% y/y in February, from 1.3% the previous month. This result means that inflation has ticked back to the lowest level since December 2016 and remains far from the European Central Bank's target of 2.0%. This in combination with muted wage pressures means that the ECB is likely to proceed slowly in exiting from the current accommodative monetary policy framework. In addition, comments from the ECB Chief Economist Peter Praet indicated that he opposed any early tweaking of the institution's language on the ECB's stimulus. According to the OIS, the markets are currently pricing in a 14.1% of a 10bps rate hike by December 2018, compared with 32.4% change one month ago.

Euro recovers above 50 day MA

Source: Bloomberg

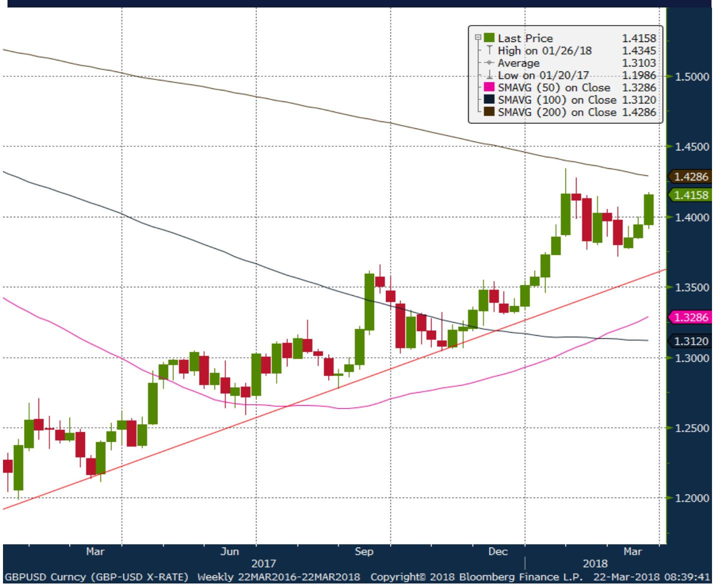
As a consequence of the USD sell off in the aftermath of the FOMC meeting, EURUSD pared some of its losses and climbed 1.31% this month reaching 1.2355 and breaking back above the 50 day moving average (1.2331). Despite this development, analysis of daily candle chart shows sideways movements overall and we expect this trend to remain intact absent a breakout below 1.22 or above 1.25.

GBP performs well despite inflation pullback

Softer than expected UK inflation readings initially weighed on sterling. Reports from the UK Office for National Statistics showed that consumer price inflation slowed by more than expected in February, with headline CPI easing from 3.0% y/y to 2.7% y/y. This was greater than the anticipated contraction of a slowdown to 2.8% y/y. In addition core CPI declined from 2.7% y/y in January to 2.4% y/y in February. These readings ease the pressure on the Bank of

England to tighten monetary policy sooner than anticipated and at present market expectations remain that the MPC will follow through with a 25bps increase in interest rates at their meeting on 10 May 2018. As we go to print, there is a 62.4% change of this eventuality according to the OIS.

GBPUSD performs



Source: Bloomberg

Firmer wages and Brexit transition.

Despite the softening inflationary pressures, January's labour report was more encouraging with wages accelerating to 2.8% y/y from 2.7% and the unemployment rate falling to 4.3% from 4.4%. GBP was also supported by the announcement that the UK and EU have worked out a transitional period that will last till the end of 2020 when the UK leaves the EU in March 2019 .

GBPUSD has gained 2.91% in March to reach 1.4160 in a move which has seen the price break above the formerly resistive 50 day moving average (1.3960) which is now acting as a support. This is bullish for GBP in the short term and while it remains above these levels, a retest of the 2018 highs of 1.4345 remains a distinct possibility. Should this level be reached and surpassed, it could pave the way for additional gains towards the 50% five year Fibonacci retracement (1.4517).

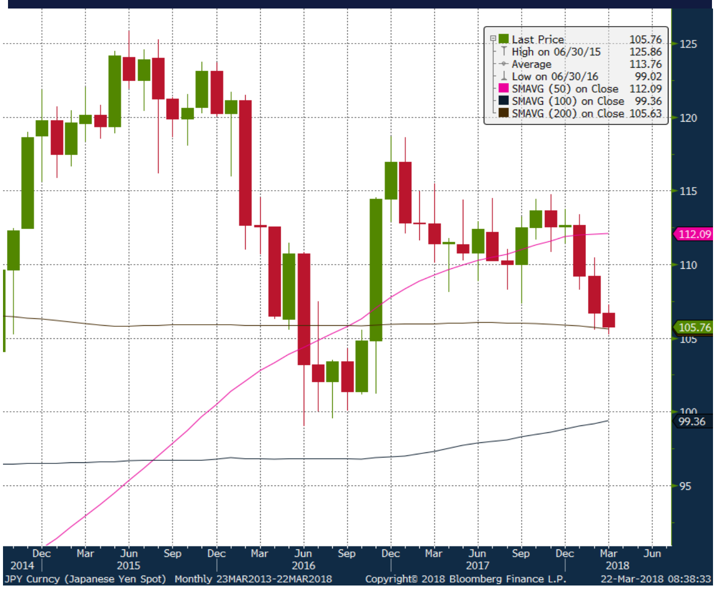
JPY supported by firm data and safe haven buying

Over the last month, the JPY has been influenced by a number of favorable factors which has resulted in investor appetite for the currency. Economic data has been one of these with data showing that in Q4 2017, GDP increased 1.6% annualized q/q, up from 0.5% in Q3 and beating expectations for expansion of 1.0%. In addition to this, the jobless rate fell to 2.4% in January from 2.7% in December showing continued improvement in the labour market while inflation in Tokyo also picked up by more than expected in February, with core inflation accelerating from 0.7% to 0.9% y/y. These reports have led to support for JPY as both readings bring the BOJ closer to its targets and the normalization of monetary policy.

However, the main driver behind JPY appreciation has been demand for safe haven assets amid the Trump administration's announcements on tariffs and concerns over global protectionism. This influence been been significant enough to break down the co-relation between US yields and USDJPY even further.

USDJPY has retreated 0.89% since the start of the month, falling to 105.74. This is the third month of consecutive falls and leaves the price close to the 200 month moving average (105.63). This level has acted as a support during the month of February and thus far in March. However, a break of this level leaves the cross exposed to a far more substantial decline towards the psychological level of 100, an event that happened that last time we saw a monthly close below the 200 month MA.

USDJPY decouples from 10 year yields



Source: Emirates NBD Research, Bloomberg

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Equities

The first quarter of 2018 has marked the transition of global equity markets from 'low volatility & high total return' phase to 'increasing volatility and declining total return' phase. While most factors supporting equity markets still remain in place, investors have been surprised at the speed with which some of the anticipated risks have manifested during the last couple of months. These include a markedly hawkish bias in the tone of major central banks, concerns over protectionism, and the enormity of churn in US domestic politics.

Nnone of these concerns have managed to have a sustained impact on equity markets, however, as they are still evolving. The random nature and lack of coherence in some of these risks i.e. trade policies initiated by the US could also be the diluting the impact of the same as could the fact that global economic growth continues to remain on a solid footing. The latest fund flow data shows that equities continue to remain the preferred asset class with inflows of USD 43bn in the last week compared to 4-week average of USD 9.1bn.

The MSCI World index has declined -0.4% 1m on the back of -0.2% 1m decline in the MSCI G7 index. Within developed markets, US equities are trading flat on m/m basis but European and Japanese equities are trading lower. The Euro Stoxx 600 index and the Nikkei index have dropped -1.4% 1m and -2.3% 1m respectively.

One interesting thing to observe is that steel-related stocks continue to underperform despite imposition of stiff tariffs on imports into the US. The NYSE Arca Steel index has dropped -4.9% 1m.

Emerging market equities continue to outperform broader equity markets with the MSCI EM index adding +0.7% 1m. However, major EM markets with the exception of the Kospi index (+3.4% 1m) closed lower. The MSCI Arabian Markets index added +2.1% 1m on the back of strength in the Tadawul (+3.1% 1m) which is seeing considerable interest from foreign investors ahead of its potential inclusion in the FTSE and MSCI EM indices.

With momentum fading away, investors will look to reassess the strength in fundamentals including corporate earnings and global economic growth, more so at a time when a lot of factors are at play.

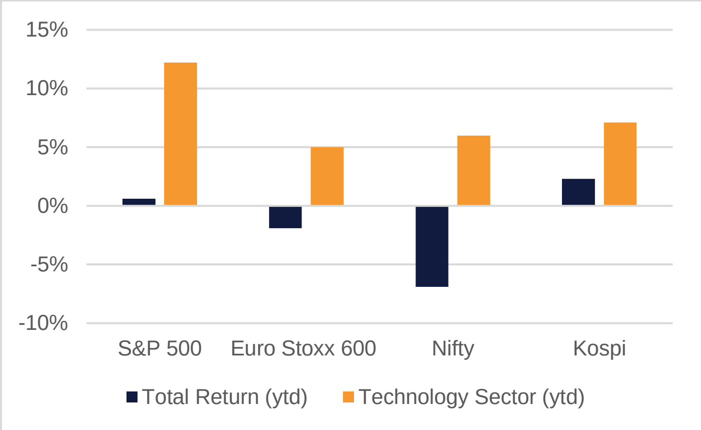
With Q1 2018 earnings reporting season couple of weeks away, the immediate direction could well hinge on how this pans out. Looking beyond the immediate term, equity market performance in Q2 2018 could well be dictated by how the 'trade tantrum' plays itself out given that most nations have so far refrained from initiating action in response to imposition of tariffs by the US. However, there seems to be no end-game in sight which increases the possibility of this turning into a major factor. Regionally, the discourse in Q2 2018 is likely to be dominated by anticipated decisions by index providers on the inclusion of Saudi Arabia in the emerging market index.

Looking beyond the headline

Sectoral breakdown

The headline move in most equity indices for the year reflects a minor pullback rather than a correction. It becomes imperative then to look beyond the headline move and see which sectors are performing. One trend which can be observed is that the performance of the broad index so far this year has been skewed by outperformance of the technology sector. For example, the total return for S&P 500 index this year has been 0.6%. However, when one looks at the sector breakdown then one finds that from 10 sectors only 3 are in positive territory. Even among those three, the technology sector has returned 12.2% ytd. This is in sharp contrast to contribution of various sectors over the past 1 year return from S&P 500 index (15.9%). During that time only two sectors out of ten gave negative returns. While technology stocks were still among the best performing stocks, they were closely followed by Healthcare and Industrials. We find a similar trend in European indices. The Euro Stoxx 600 index has a negative total return of -1.9% ytd but the technology sector has delivered a 5.0% return ytd. All other sectors are in negative territory.

Technology stocks driving broad index moves



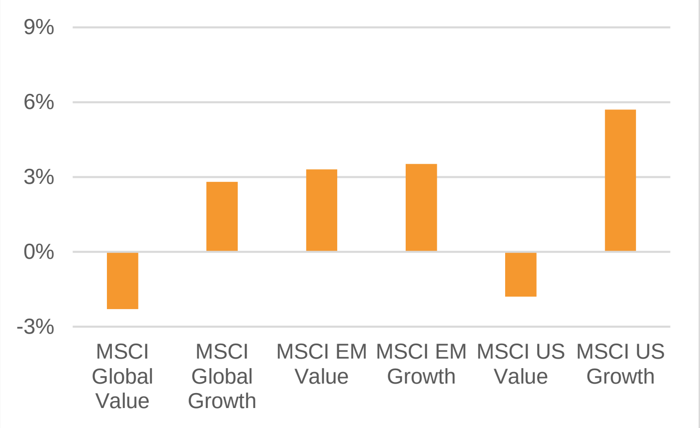
Source: Bloomberg, Emirates NBD Research

Within emerging markets, the picture is more mixed. In the case of India's Nifty index the trend is similar to that in the US and Europe. The technology sector with returns of 6.0% ytd is the only sector to deliver positive returns when the broad index is down -6.9% (total return). In China, the decline is broad based with no one sector dominating. Within the MENA region, it is hard to gauge as generally indices are dominated by two sectors. However, if one takes the example of EGX30 index then we find a more diversified performance with financials (11.0% ytd) and consumer goods (11.7% ytd) driving the gains.

Value & Growth stocks

The recent pullback in equities and rise in yields has brought the focus back on the difference between growth and value stocks. With economic growth continuing to remain strong, it is not surprising to see that the trend of growth stocks outperforming value stocks continuing.

Growth stocks continuing to outperform value stocks (ytd)



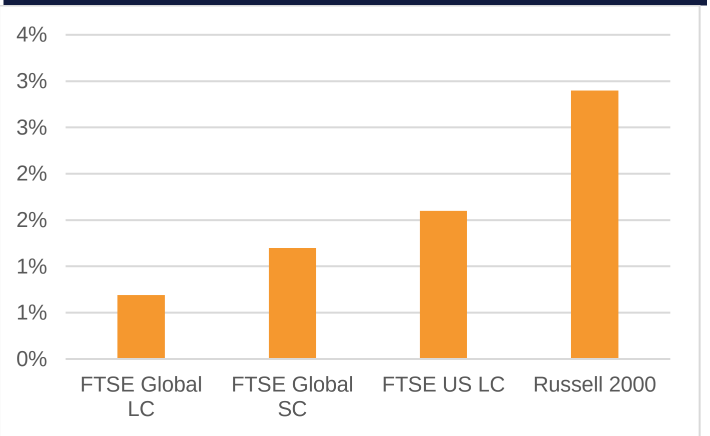
Source: Bloomberg, Emirates NBD Research

The MSCI Global value index has dropped -2.3% ytd compared to a gain of +2.8% in the MSCI Global growth index. The trend if similar when one looks at the US stocks only. The MSCI US Value index has dropped -1.8% ytd compared to a gain of +5.7% ytd in the MSCI US Growth index. The underperformance of the value stocks in the US can be attributed the declining spreads with the S&P earnings yield and the 10y US treasury yields. The spread at 172bps is the lowest quartile since 2011. The picture is more neutral when we look the EM value and growth stocks. The MSCI EM value index has returned +3.29% ytd compared to +3.5% ytd return from the MSCI EM growth index.

Large Cap & Small Cap stocks

There is a general belief that rising interest rates tends to hurt small cap companies more than the large cap companies. However, this time with the US overhauling its tax code, it was estimated that the rise in interest costs for small cap companies would be offset by the tax benefits. It is also seen that in a high growth environment, small cap companies tend to do better than large cap companies as they have more potential to grow.

Small caps outperforming large cap stocks (ytd)



Source: Bloomberg, Emirates NBD Research

The data bears that out with small cap companies outperforming large cap companies so far in 2018. The FTSE Global large cap index has gained +0.7% ytd compared to a gain of 1.2% in the FTSE Small cap index. In the US as well, the trend holds. The FTSE US large cap index has rallied +1.6% ytd while small caps represented by Russell 2000 index has returned +2.9% ytd. It is worth noting here that in the US this is a trend reversal from last year. In 2017, the FTSE US large cap index added +20.2% while the Russell 2000 index returned +13.2%.

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Commodities

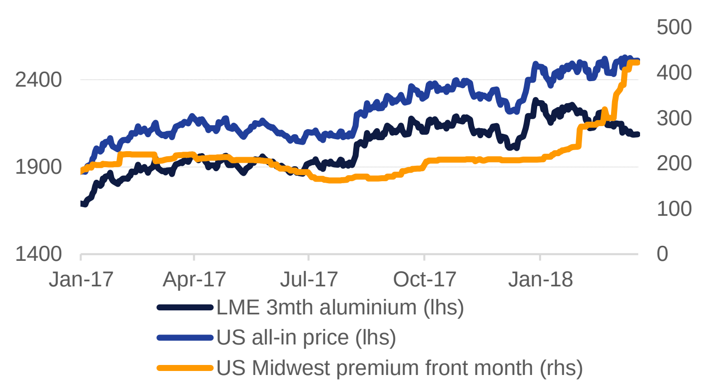
US president Donald Trump has put in place tariffs on imported steel and aluminium, rocking metals markets this month. While the tariff plans send worrying messages about how committed the US is to free trade, the impact on commodity markets is still playing out. Ultimately we expect the tariffs will have a marginal impact on global aluminium balances as US action is outweighed by contrasting policies in China.

Aluminium market to split in two?

Aluminium will be buffeted by two contrasting policy trends this year, one meant to support production and the other meant to discourage it. In the US, president Donald Trump's imposition of a 10% tariff on imports of aluminium is meant to support the domestic smelting industry by keeping the market free from what the administration claims are cheap imports of the metal.

LME aluminium prices have declined on the back of the tariff newsflow as there is a serious risk the introduction of the trade barrier will create a bifurcated aluminium market, with the US effectively an isolated and more expensive region. Premiums for near-term delivery to the US Midwest have soared, up nearly USD 200/tonne since the end of January, and has meant that US all-in prices have been moving higher while LME prices have been grinding lower.

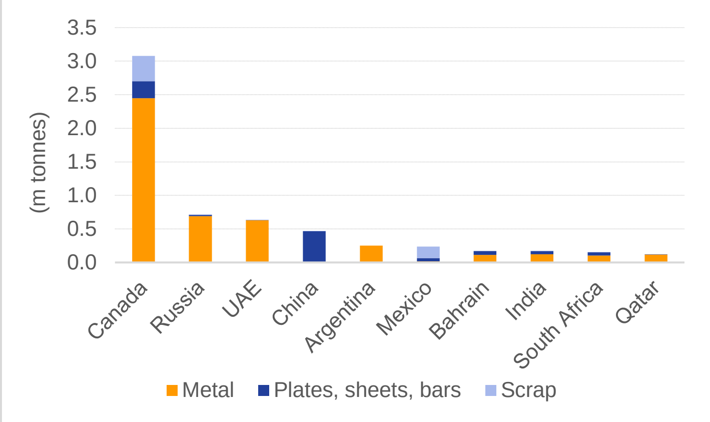
US faces higher aluminium prices



Source: USGS, Emirates NBD Research.

Imports accounted for nearly 60% of the aluminium available for consumption in the US in 2017, up from 55% a year earlier. Most of that metal comes from Canada, largely in commodity form, while China, which is the ostensible target of these tariffs accounts for less than 7% of total imports but more than a third of processed metal (plates, sheets and bars). The UAE is also a sizeable exporter of aluminium metal to the US, accounting for more than 9% of total imports last year.

US aluminium imports by country



Source: USGS, Emirates NBD Research.

Several US based smelter operators have already announced plans to restart potlines in response to the tariffs but we are skeptical how much of an impact this production could have on global markets. According to the USGS, aluminium smelters in the US operated at around 37% capacity in 2017 and an increase to the 80% capacity utilization promoted by the US Department of Commerce would mean an increase of 860k tonnes/year (in a global market of roughly 60m tonnes/year).

The decline in US aluminium output was a result of high electricity tariffs making production uneconomical more than it was competition from import markets. If access to affordable and reliable electricity is not assured, then production in the US remains at risk. While some global flows of metal will be disrupted as a result of the tariffs we do not expect it will have a dramatic impact on global aluminium markets given the relatively small size of the US smelting industry.

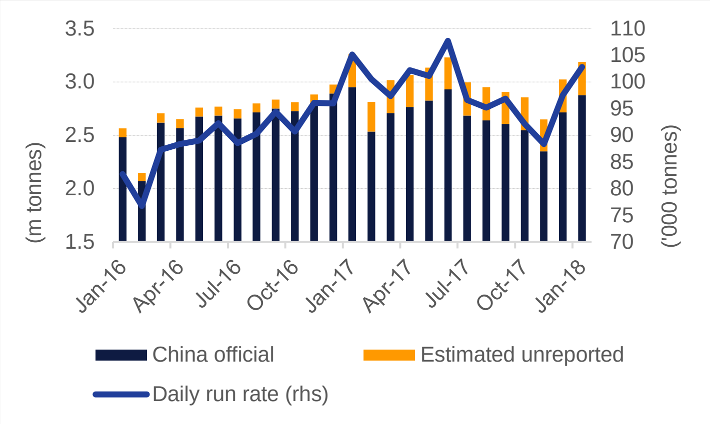
Chinese policy far more consequential

Of far more consequence to global aluminium balances is whether China makes its pollution-related curbs on heavy industry a permanent feature for metal markets. China accounts for roughly 50% of both global aluminium production and consumption so policy decisions there have an outsized bearing on international markets.

Early last year, China's government mandated the curtailment of aluminium production in provinces around Beijing during the winter heating months along with the closure of illegal capacity. The announcement of the policy helped push aluminium prices higher over much of the year but had a limited impact on China's overall balances. Indeed in December Chinese aluminium production jumped 15% month on month (m/m) and ended the year at 32.2m tonnes, up nearly 2% y/y.

However, when estimates of unreported (illegal) production are included in China's total, production there rose 10% y/y in 2017. Production has accelerated further this year with data for January showing an m/m increase of 6% and an acceleration in the official daily run rate to 92.8k tonnes compared with 78k tonnes as recently as November.

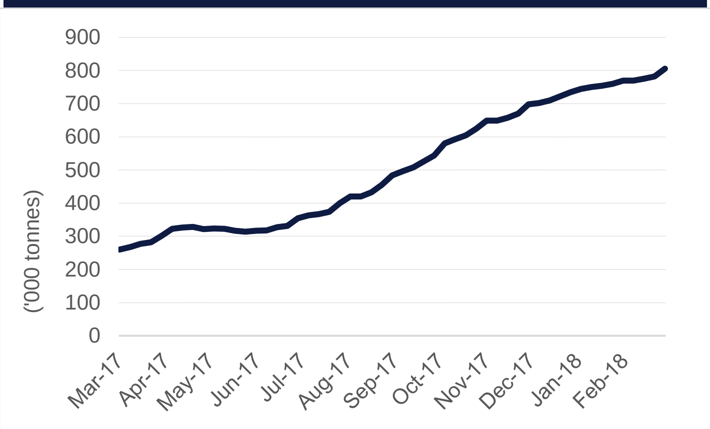
Little impact from Chinese shutdowns



Source: IAI, Emirates NBD Research.

Considering the Chinese government's efforts to clean up the country's energy mix and limits on highly polluting industries we would expect to see another round of output curtailments over the winter months at the end of 2018 and carrying forward. But the increase in production reported in 2017 shows that attempts to cut back on illegal capacity, or that swapping out older smelters for new, hasn't yet had the intended impact on lowering production. We expect that aluminium production in China will likely shift to being more concentrated in the west of the country where the enivonrmental pressures of heavy manufacturing in densely populated cities may be less actue. Moreover the high efficiency of new Chinese smelters—among the lowest power usage in the world—will likely keep overall output levels high as older capacity is closed.

SHFE aluminium inventories



Source: EIKON, Emirates NBD Research.

China's elevated production volumes of aluminium have a limited impact on global markets in commodity form as the government imposes export duties on primary exports. However, semi-finished products (wire and foil for example) have grown in scale and been passing to consumers via indirect routes in some cases. These exports of semi-finished products already faced US and Indian tariffs introduced last year and have started to drop-off. We would expect some of these 'lost' semi exports have just been delivered into the domestic market in commodity metal form and have abetted the large increase in SHFE aluminium inventories.

We forecast LME aluminium prices at an average of around USD 2,000/tonne in 2018 with a peak in Q1 of USD 2,100/tonne and declining over the course of the year. The impact of pollution related shutdowns in China appears to be limited and the Trump tariffs will likely result in 'abandoned' metal needing to find a home in other markets, at more affordable rates. Moreover, there are external factors that support our view for lower prices going forward. A weaker USD over much of 2017 helped support commodity prices generally and we think this narrative has come to an end with little further downside for the greenback.

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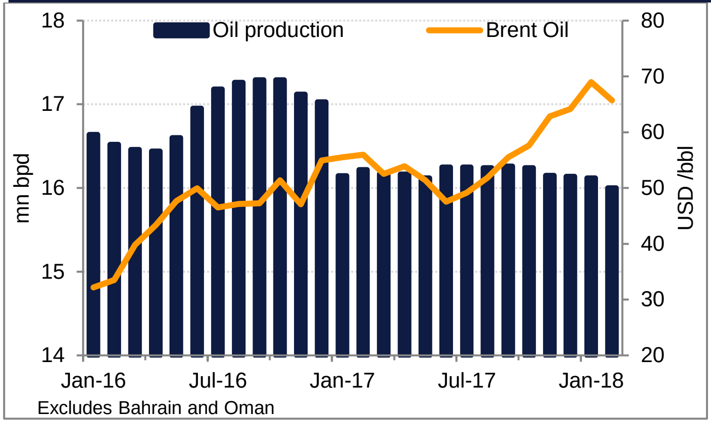
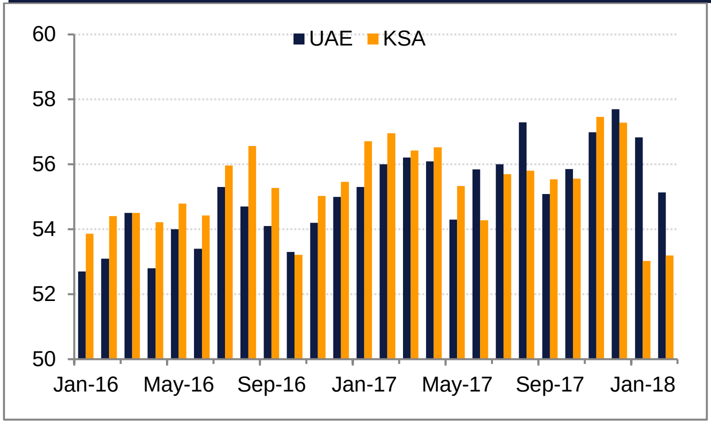
GCC in Pictures

GCC Oil Production and Oil Price



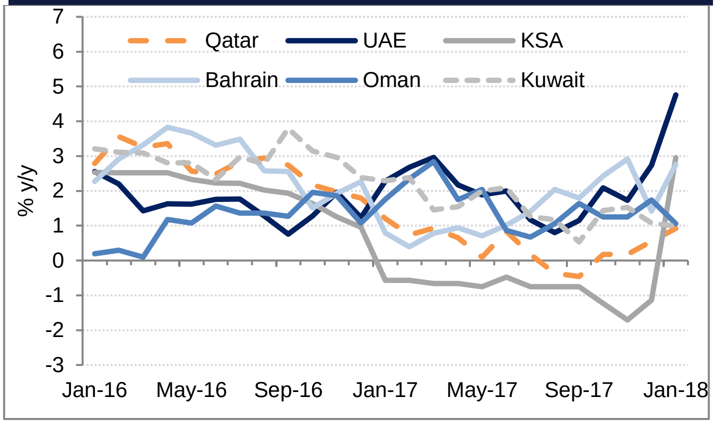
Source: Bloomberg, Emirates NBD Research

Purchasing Managers' Index



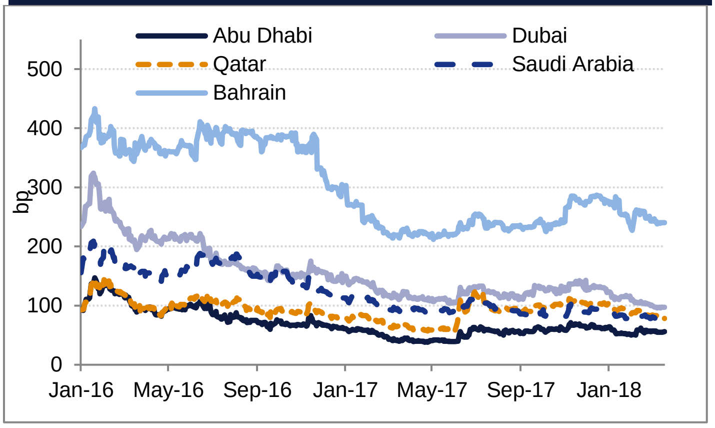
Source: IHS Markit, Emirates NBD Research

Inflation



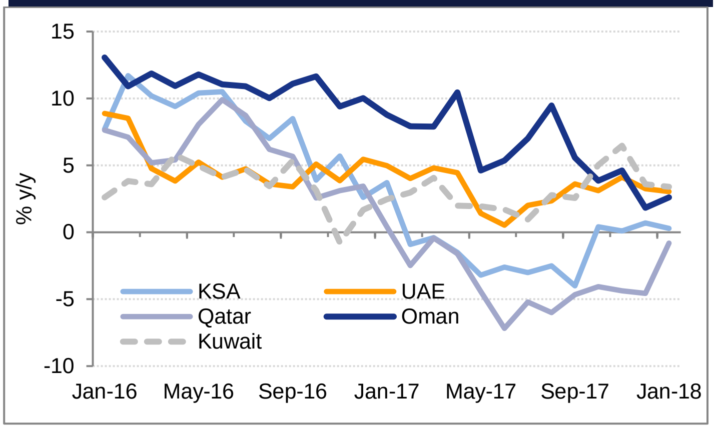
Source: Haver Analytics, Emirates NBD Research

CDS Spreads



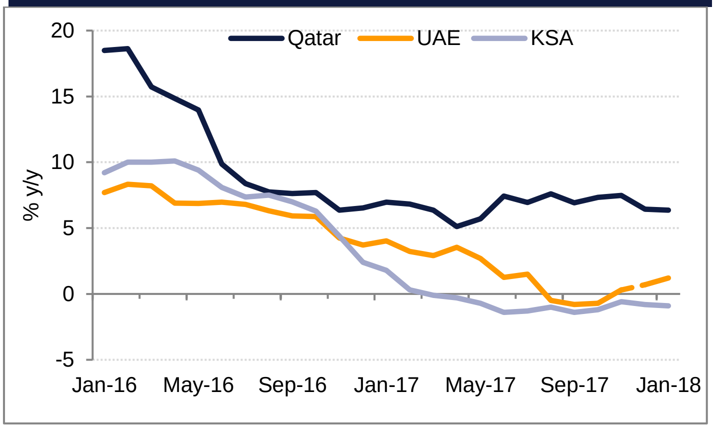
Source: Bloomberg

Money supply (ex Government. deposits)



Source: Haver Analytics, Emirates NBD Research

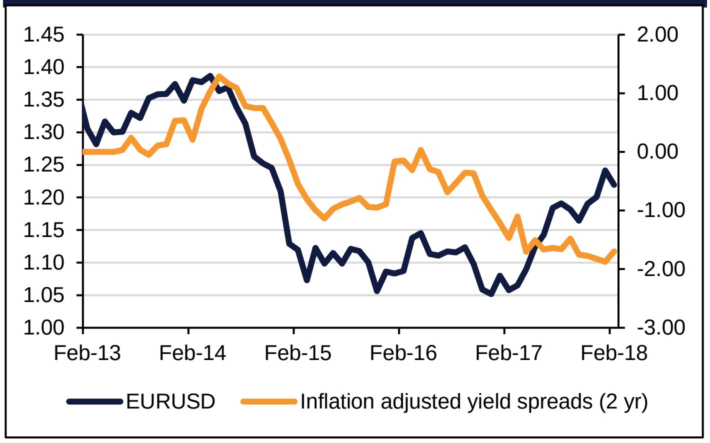
Private sector credit*



**Qatar data is bank loan growth to private sector, not total private sector credit. Source: Haver Analytics, Emirates NBD Research*

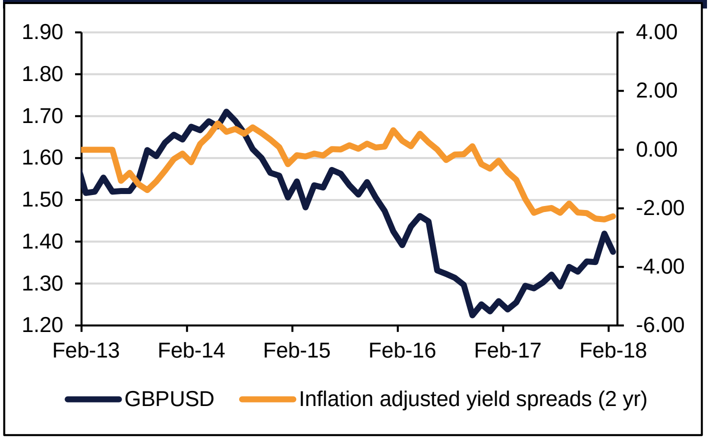
FX–Major Currency Pairs & Real Interest Rates

Interest Rate Differentials–EUR



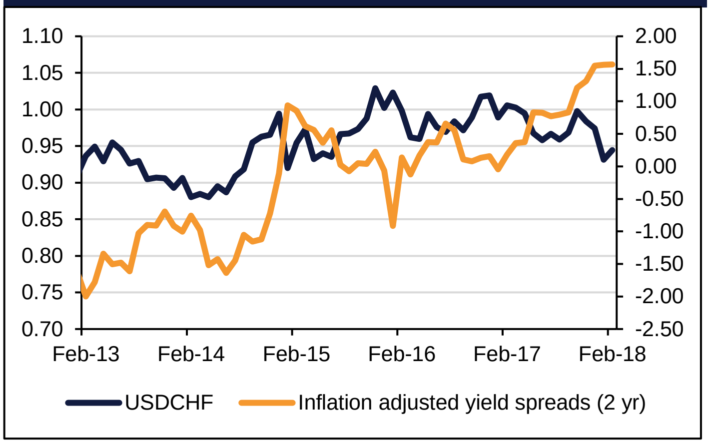
Source: Bloomberg, Emirates NBD Research

Interest Rate Differentials-GBP



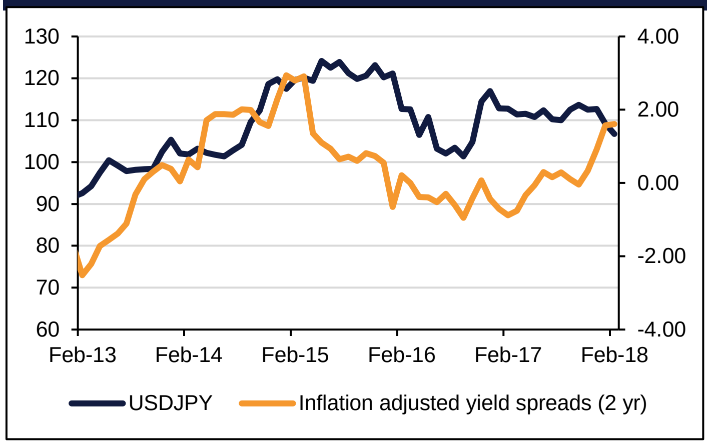
Source: Bloomberg, Emirates NBD Research

Interest Rate Differentials-CHF



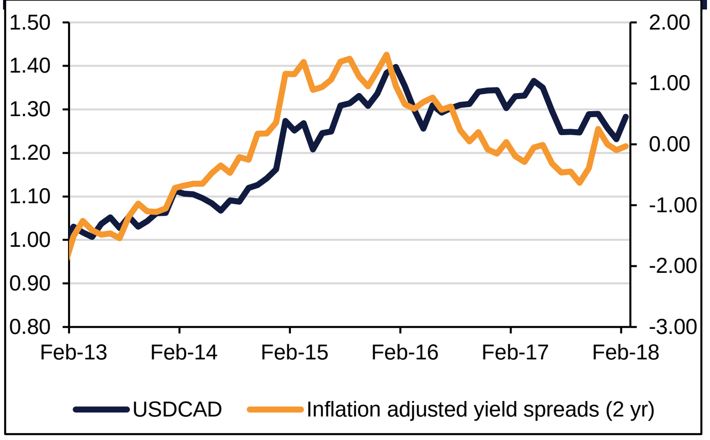
Source: Bloomberg, Emirates NBD Research

Interest Rate Differentials-JPY



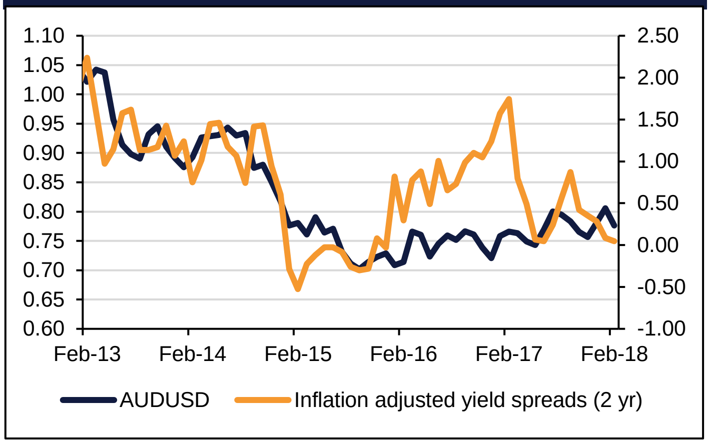
Source: Bloomberg, Emirates NBD Research

Interest Rate Differentials-CAD



Source: Bloomberg, Emirates NBD Research

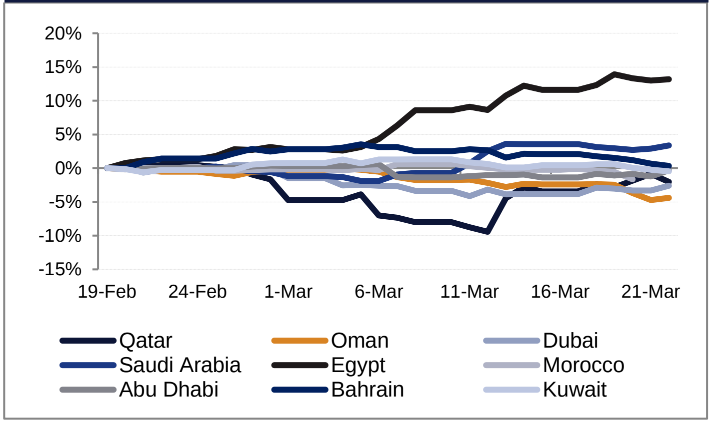
Interest Rate Differentials-AUD



Source: Bloomberg, Emirates NBD Research

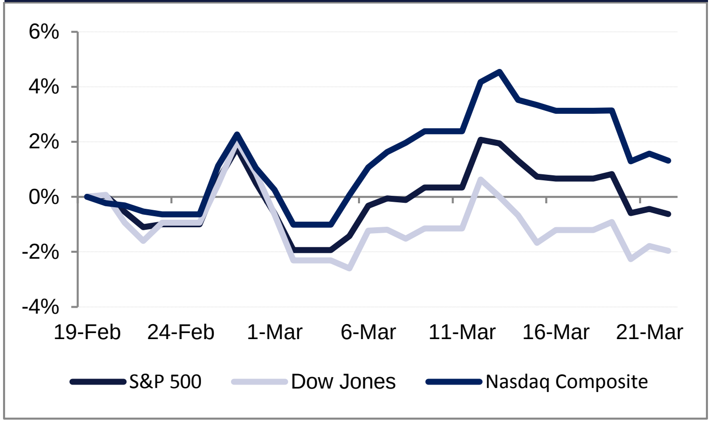
Major Equity Markets

MENA Equity Markets



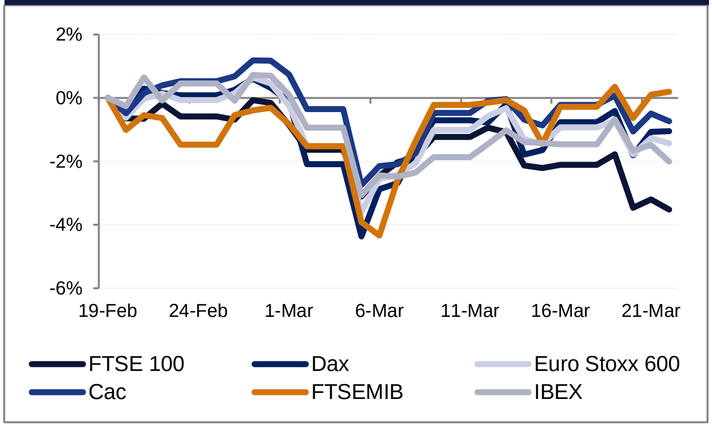
Source: Bloomberg, Emirates NBD Research

US Equity Markets



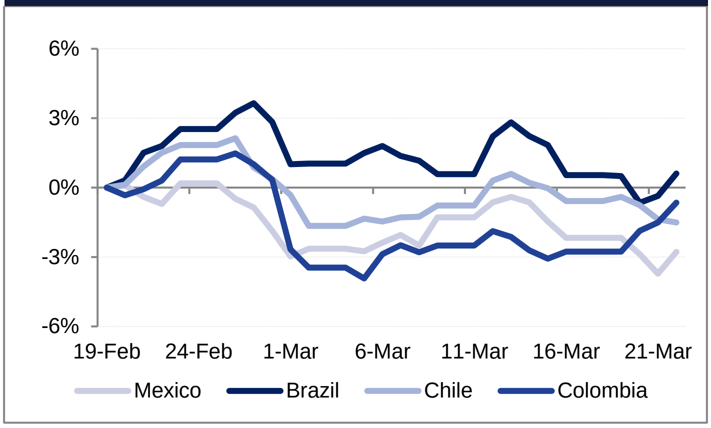
Source: Bloomberg, Emirates NBD Research

European Equity Markets



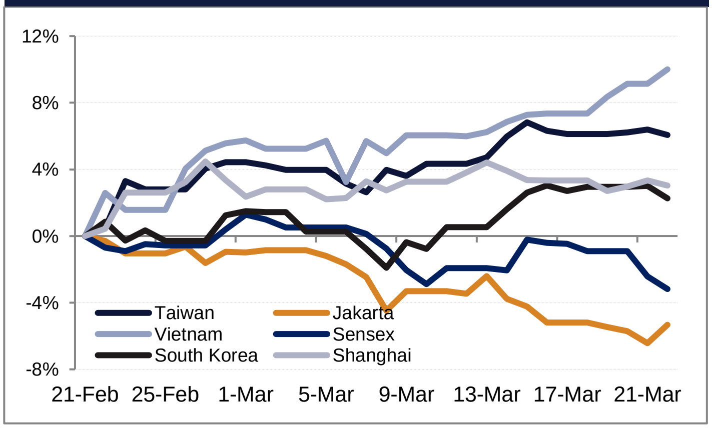
Source: Bloomberg, Emirates NBD Research

Latin American Equity Markets



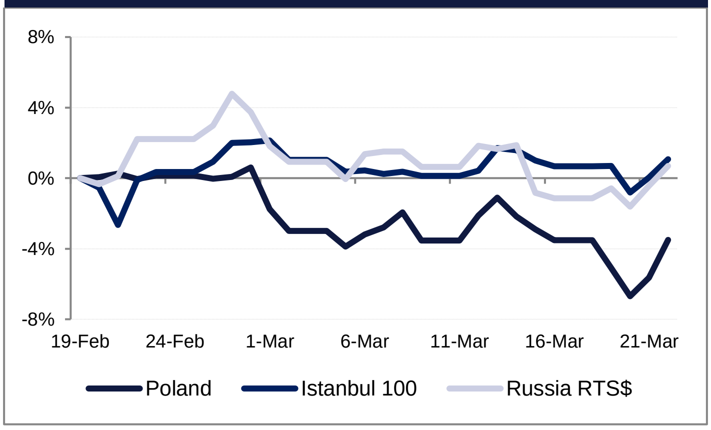
Source: Bloomberg, Emirates NBD Research

Asian Emerging Equity Markets



Source: Bloomberg, Emirates NBD Research

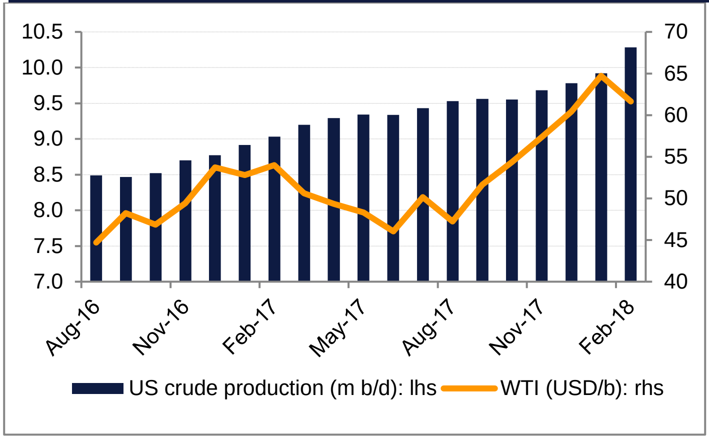
Emerging Europe Equity Markets



Source: Bloomberg, Emirates NBD Research

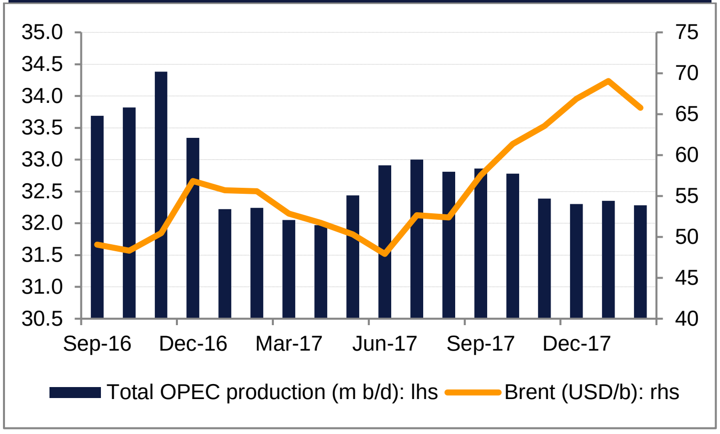
Major Commodities Markets

US oil production and price



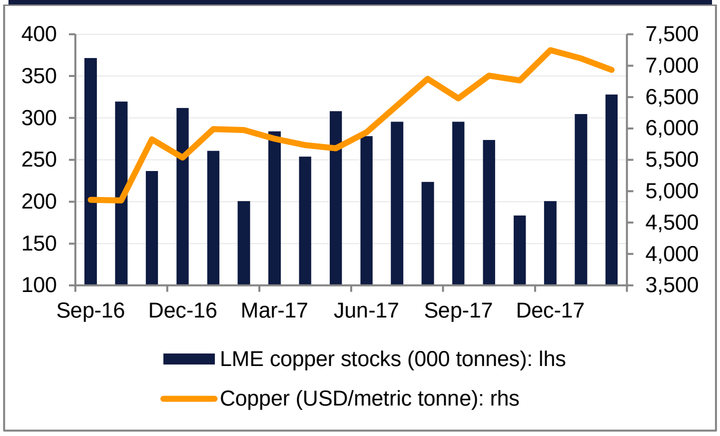
Source: EIKON, Emirates NBD Research

International oil production and price



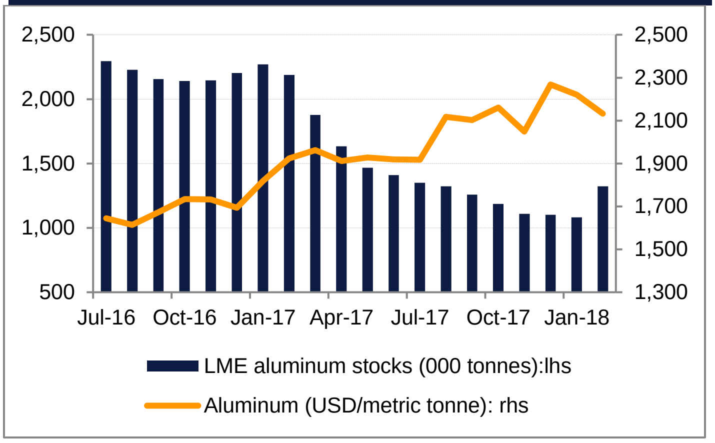
Source: EIKON, Emirates NBD Research

Copper stocks and price



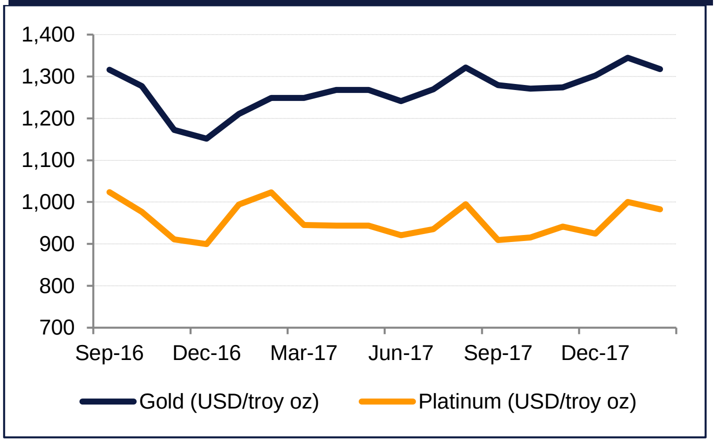
Source: EIKON, Emirates NBD Research

Aluminum stocks and price



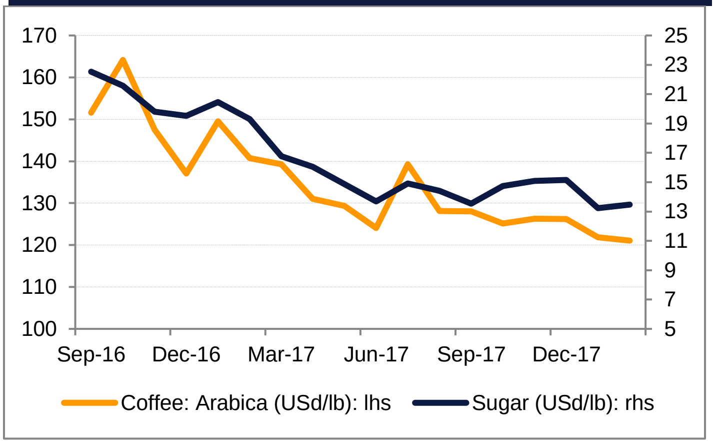
Source: EIKON, Emirates NBD Research

Precious metals prices



Source: EIKON, Emirates NBD Research

Agriculture prices



Source: EIKON, Emirates NBD Research

Key Economic Forecasts - GCC

United Arab Emirates	2015	2016	2017e	2018f	2019f
Nominal GDP $bn	358.2	349.0	373.2	401.8	424.8
Real GDP %	3.8	3.0	2.0	3.4	3.8
Current A/C % GDP	4.7	2.4	3.7	4.4	4.4
Budget Balance % GDP	-3.4	-4.3	-2.7	-0.7	1.3
CPI %	4.1	1.6	2.0	3.0	3.0
Saudi Arabia					
Nominal GDP $bn	654.3	644.9	684.2	731.8	771.9
Real GDP %	4.1	1.7	-0.7	2.5	3.0
Current A/C % GDP	-9.1	-4.0	1.0	4.0	3.7
Budget Balance % GDP	-15.0	-13.6	-9.0	-7.5	-6.3
CPI %	2.2	3.5	-0.2	3.5	3.0
Qatar					
Nominal GDP $bn	164.6	152.5	164.7	177.6	193.7
Real GDP %	3.3	2.0	2.2	3.0	3.6
Current A/C % GDP	12.7	1.2	1.1	1.6	0.8
Budget Balance % GDP	1.2	-8.4	-4.7	-0.3	0.0
CPI %	1.9	2.7	0.3	2.5	3.0
Kuwait					
Nominal GDP $bn	117.3	113.3	102.5	108.7	120.3
Real GDP %	0.6	3.5	-1.2	2.1	3.2
Current A/C% GDP	5.1	-1.5	4.1	3.1	2.6
Budget Balance % GDP	-13.1	-13.5	-8.7	-8.1	-5.0
CPI %	3.3	3.2	1.6	2.0	3.5
Oman					
Nominal GDP $bn	68.8	66.7	73.8	79.3	84.0
Real GDP %	4.7	5.4	1.0	2.8	3.2
Current A/C % GDP	-15.9	-18.5	-8.4	-4.3	-4.4
Budget Balance % GDP	-17.5	-20.6	-12.3	-10.5	-6.5
CPI %	0.1	1.1	1.6	2.0	3.0
Bahrain					
Nominal GDP $bn	31.1	32.2	34.8	36.7	38.6
Real GDP %	2.9	3.2	3.0	3.0	3.2
Current A/C % GDP	-2.4	-4.6	-4.8	-1.6	7.7
Budget Balance % GDP	-13.0	-13.6	-11.7	-11.2	-10.2
CPI %	1.8	2.8	1.7	2.0	3.0
GCC (Nominal GDP weighted avg)					
Nominal GDP $bn	432	426	455	487	512
Real GDP %	3.6	2.4	0.5	2.8	3.3
Current A/C % GDP	-2.0	-2.3	1.3	3.2	3.2
Budget Balance % GDP	-10.0	-11.0	-7.1	-5.2	-3.6
CPI %	2.6	2.8	0.7	3.0	3.0

Source: Haver Analytics, National sources, Emirates NBD Research

Key Economic Forecasts – Non-GCC Oil Importers

Egypt*	2015	2016	2017e	2018f	2019f
Nominal GDP $bn	332.6	332.4	189.9	242.6	289.3
Real GDP %	4.4	4.3	4.2	5.0	5.3
Current A/C % GDP	-3.7	-6.0	-6.9	-3.9	-3.1
Budget Balance % GDP	-11.43	-12.05	-10.96	-9.50	-7.91
CPI %	10.4	13.7	29.6	15.0	12.0
Jordan					
Nominal GDP $bn	37.5	38.9	40.3	41.7	43.2
Real GDP %	2.4	2.0	2.4	3.0	3.2
Current A/C % GDP	*-9.1*	*-9.5*	*-8.7*	*-8.0*	*-7.4*
Budget Balance % GDP	*-3.4*	*-3.2*	*-2.7*	*-2.3*	*-1.9*
CPI %	-0.9	-0.8	3.3	3.0	2.5
Lebanon					
Nominal GDP $bn	50.1	54.4	60.4	66.0	71.0
Real GDP %	1.5	1.1	1.8	1.9	2.4
Current A/C % GDP	*-16.2*	*-18.1*	*-19.2*	*-19.5*	*-19.4*
Budget Balance % GDP	*-7.9*	*-9.3*	*-9.2*	*-8.3*	*-7.7*
CPI %	-3.8	-0.8	4.6	4.3	4.0
Tunisia					
Nominal GDP $bn	41.1	41.3	39.7	40.9	42.2
Real GDP %	0.8	1.1	2.1	2.6	2.9
Current A/C% GDP	-9.4	-8.9	-10.8	-10.0	-9.6
Budget Balance % GDP	-5.0	-6.2	-5.8	-5.4	-5.2
CPI %	5.5	4.9	3.7	5.0	5.0
Morocco					
Nominal GDP $bn	109.9	101.3	103.6	117.9	125.8
Real GDP %	2.7	4.5	1.2	4.3	3.7
Current A/C % GDP	-6.3	-1.9	-3.9	-3.6	-3.0
Budget Balance % GDP	-5.2	-4.5	-4.1	-3.5	-2.9
CPI %	4.9	3.7	5.3	6.9	6.8
Oil Importers (GDP weighted avg)					
Nominal GDP $bn	224.8	223.2	126.2	158.7	189.7
Real GDP %	3.76	3.08	3.54	3.70	4.21
Current A/C % GDP	-5.4	-5.5	-6.6	-6.2	-4.3
Budget Balance % GDP	-7.7	-6.9	-4.7	-3.4	-3.4
CPI %	9.1	7.4	6.7	6.6	1.9

Source: Haver Analytics, National sources, Emirates NBD Research
**Egypt data refers to fiscal year (July-June)*

Key Economic Forecasts – Non-GCC Oil Exporters

Algeria	2014	2015	2016	2017f	2018f
Nominal GDP $bn	166.4	159.1	177.6	185.3	193.1
Real GDP %	3.8	3.4	2.3	3.0	2.7
Current A/C % GDP	-12.9	-12.3	-13.6	-12.6	-10.7
Budget Balance % GDP	-15.4	-13.0	-9.5	-8.7	-7.3
CPI %	4.4	5.8	6.6	6.4	5.3
Libya					
Nominal GDP $bn	34.4	40.4	54.3	63.5	74.5
Real GDP %	-10.2	-0.9	30.4	11.6	9.5
Current A/C % GDP	-9.4	-11.0	-11.1	-12.0	-12.2
Budget Balance % GDP	-23.6	-19.6	-12.3	-5.4	-5.3
CPI %	9.5	9.5	25.0	11.5	10.0
Iran					
Nominal GDP $bn	423.7	437.4	441.5	468.7	507.3
Real GDP %	3.7	13.4	3.9	4.5	4.7
Current A/C % GDP	2.1	3.7	5.4	5.9	6.2
Budget Balance % GDP	-5.3	-4.8	-3.9	-3.1	-2.5
CPI %	15.8	8.5	11.1	12.0	10.0
Iraq					
Nominal GDP $bn	164.2	233.6	244.2	280.2	318.2
Real GDP %	-2.4	11.1	-0.3	2.7	6.0
Current A/C% GDP	2.5	1.4	0.9	0.8	0.7
Budget Balance % GDP	-13.3	-10.0	-5.7	-5.1	-1.0
CPI %	1.2	1.3	0.9	2.0	3.0
Oil Exporters (GDP weighted avg)					
Nominal GDP $bn	302.7	317.0	314.6	337.2	367.2
Real GDP %	1.7	10.0	4.3	4.3	5.0
Current A/C % GDP	1.3	0.6	-0.1	0.3	0.2
Budget Balance % GDP	-6.4	-7.3	-7.0	-5.5	-3.4
CPI %	9.7	5.7	7.9	8.1	7.4

Key Economic Forecasts - Global

US	2013	2014	2015	2016f	2017f	2018f
Real GDP %	2.2	2.4	2.4	1.8	2.5	2.7
Current A/C % GDP	-2.3	-2.3	-2.6	-2.7	-2.7	-3.0
Budget Balance % GDP	-3.3	-2.8	-2.5	-2.5	-3.0	-3.5
CPI %	1.5	1.6	0.1	1.7	2.3	2.5
Eurozone						
Real GDP %	-0.3	0.9	1.5	1.5	1.7	1.5
Current A/C % GDP	1.8	2.4	3.0	2.7	2.6	2.8
Budget Balance % GDP	-2.9	-2.6	-2.0	-2.0	-1.6	-1.6
CPI %	1.3	0.4	0.0	0.9	1.5	1.5
UK						
Real GDP %	1.7	2.9	2.4	2.0	1.7	2.0
Current A/C% GDP	-4.5	-5.1	-4.5	-4.0	-4.0	-3.3
Budget Balance % GDP	-5.9	-5.4	-4.3	-3.2	-2.0	-2.8
CPI %	2.6	1.5	0.5	1.9	2.0	2.6
Japan						
Real GDP %	1.6	0.0	0.5	0.9	1.0	0.5
Current A/C % GDP	0.8	0.5	3.0	3.2	3.0	3.5
Budget Balance % GDP	-7.8	-7.1	-6.0	-6.0	-5.0	-4.8
CPI %	0.3	2.7	0.8	0.8	1.5	1.0
China						
Real GDP %	7.7	7.3	6.9	6.5	6.3	6.1
Current A/C % GDP	1.5	2.1	2.7	2.8	2.5	1.9
Budget Balance %GDP	-1.8	-1.8	-2.5	-3.0	-3.0	-3.5
CPI%	2.6	2.0	1.4	1.7	2.0	2.2
India*						
Real GDP%	4.7	6.9	7.4	8.0	6.6	7.3
Current A/C% GDP	-2.6	-1.4	-1.5	-1.5	-1.0	-2.0
Budget Balance % GDP	-5.9	-4.8	-4.1	-3.9	-3.9	-3.3
CPI %	10.9	6.4	7.0	5.0	4.5	5.5

Source: Bloomberg, Emirates NBD Research
**For India the data refers to fiscal year (April – March)*

FX Forecasts

	FX Forecasts - Major					Forwards		
	21-Mar	Q1 2018	Q2 2018	Q3 2018	Q4 2018	3m	6m	12m
EUR/USD	1.2271	1.2200	1.2500	1.2200	1.2000	1.2359	1.2450	1.2651
USD/JPY	106.37	107.50	111.00	114.00	118.00	105.69	104.97	103.40
USD/CHF	0.9549	0.9600	0.9900	1.0100	1.0200	0.9472	0.9393	0.9226
GBP/USD	1.4022	1.3800	1.4000	1.4200	1.4500	1.4080	1.4136	1.4257
AUD/USD	0.7704	0.7650	0.7400	0.7200	0.7200	0.7707	0.7712	0.7729
NZD/USD	0.7186	0.7100	0.7100	0.7100	0.7100	0.7184	0.7184	0.7191
USD/CAD	1.3019	1.2900	1.2600	1.2600	1.2600	1.2995	1.2972	1.2928
EUR/GBP	0.8751	0.8841	0.8929	0.8592	0.8276	0.8778	0.8807	0.8873
EUR/JPY	130.52	131.15	138.75	139.08	141.60	130.52	130.52	130.52
EUR/CHF	1.1717	1.1712	1.2375	1.2322	1.2240	1.1706	1.1694	1.1670
	FX Forecasts - Emerging					**Forwards**		
	21-Mar	**Q1 2018**	**Q2 2018**	**Q3 2018**	**Q4 2018**	**3m**	**6m**	**12m**
USD/SAR*	3.7498	3.7500	3.7500	3.7500	3.7500	3.7503	3.7513	3.7560
USD/AED*	3.6730	3.6730	3.6730	3.6730	3.6730	3.6737	3.6746	--
USD/KWD	0.2999	0.3020	0.3020	0.3020	0.3020	0.2983	0.2981	--
USD/OMR*	0.3850	0.3850	0.3850	0.3850	0.3850	0.3855	0.3864	0.3893
USD/BHD*	0.3770	0.3770	0.3770	0.3770	0.3770	0.3762	0.3762	0.3792
USD/QAR*	3.6588	3.6400	3.6400	3.6400	3.6400	3.6735	3.6770	3.6850
USD/EGP	17.5952	17.5000	17.2500	17.2500	17.0000	17.9800	18.3500	19.0400
USD/INR	65.198	65.000	66.000	66.000	65.000	66.0500	66.7300	67.9600
USD/CNY	6.3341	6.5500	6.7000	6.9000	7.1000	6.3708	6.4013	6.4558
USD/SGD	1.3125	1.3050	1.3000	1.2900	1.2900	1.3102	1.3072	1.3016

Data as of 21 March 2018
Source: Bloomberg, Emirates NBD Research

Interest Rate Forecasts

USD Swaps Forecasts					Forwards		
	Current	**3M**	**6M**	**12M**	**3M**	**6M**	**12M**
2y	2.62	2.65	2.75	2.70			
10y	2.89	3.06	3.06	2.98			
2s10s (bp)	27	41	31	28			
US Treasurys Forecasts					**US Treasurys Forecasts**		
2y	2.30	2.43	2.60	2.65			
10y	2.87	3.00	3.00	2.95			
2s10s (bp)	57	57	40	30			
3M Libor					**3M Libor**		
3m	2.27	2.50	2.60	2.75			
3M Eibor					**3M Eibor**		
3m	2.26	2.48	2.60	2.75			
Policy Rate Forecasts							
	Current %	**3M**	**6M**	**12M**			
FED (Upper Band)	1.75	2.00	2.25	2.50			
ECB	0.00	0.00	0.00	0.00			
BoE	0.50	0.75	0.75	1.00			
BoJ	-0.10	-0.10	-0.10	-0.10			
SNB	-0.75	-0.75	-0.75	-0.75			
RBA	1.50	1.50	1.50	1.75			
RBI (repo)	6.00	6.00	6.00	6.25			
SAMA (reverse repo)	1.75	2.25	2.50	2.75			
UAE (1W repo)	2.00	2.25	2.50	2.75			
CBK (o/n repo rate)	1.75	2.00	2.25	2.50			
QCB (repo rate)	2.50	3.00	3.25	3.25			
CBB (o/n depo)	1.75	2.00	2.25	2.50			
CBO (o/n repo)	2.34	2.60	2.85	3.10			
CBE (o/n depo)	17.75	16.75	15.75	14.75			

Data as of 22 March 2018
Source: Bloomberg, Emirates NBD Research

Commodity Forecasts

Global commodity prices									
	Last	2017Q3	Q4	2018Q1	Q2	Q3	Q4	2017	2018
Energy									
WTI	65.04	48.17	55.43	62.50	58.50	55.00	52.50	50.94	57.13
Brent	69.20	52.18	60.52	66.00	59.00	58.00	55.00	54.56	59.50
Precious metals									
Gold	1332.41	1,278.79	1,276.5	1,300.00	1,250.00	1,275.00	1,325.00	1,277.65	1,287.50
Silver	16.60	16.84	16.70	17.25	17.00	18.00	18.50	16.77	17.69
Platinum	959.43	951.74	920.34	950.00	900.00	925.00	975.00	936.04	937.50
Palladium	993.45	900.21	992.39	1,100.00	1,100.00	1,175.00	1,200.00	946.30	1,143.75
Base									
Aluminum	2081.00	2,026.55	2,120.6	2,100.00	2,000.00	1,950.00	1,975.00	2,073.62	2,006.25
Copper	6793.00	6,381.59	6,856.2	6,850.00	6,500.00	6,250.00	6,250.00	6,618.94	6,462.50
Lead	2400.00	2,352.52	2,495.5	2,493.57	2,381.45	2,300.85	2,300.85	2,424.05	2,369.18
Nickel	13460.00	10,588.8	11,660.	12,500.00	11,750.00	11,500.00	11,500.00	11,124.45	11,812.50
Tin	21000.00	20,369.1	19,714.	19,900.00	20,000.00	21,250.00	21,250.00	20,041.91	20,600.00
Zinc	3249.00	2,960.39	3,197.4	3,195.00	3,059.50	2,961.84	2,961.84	3,078.91	3,044.54

Prices as of 22 March 2018. Note: prices are average of time period unless indicated otherwise.
Source: Bloomberg, Emirates NBD Research

Global Equities Market Watch

Index	Last Close	ADV Traded 30d USD mn	Mtd % chg	Ytd % chg	%membera bove 200d MA	BEst PE	BEst PB	BEst Dvd Yld
Dow Jones Industrial Average Index	24,682	10,140	-1.4	-0.1	67	-	-	-
S&P 500 Index	2,712	50,238	-0.1	1.4	64	-	-	-
Nasdaq Composite Index	7,345	34,260	1.0	6.4	60	-	-	-
FTSE100 Index	7,039	6,404	-2.7	-8.4	48	13.4	1.7	4.6
DAX Index	12,309	5,458	-1.0	-4.7	45	12.8	1.6	3.2
CAC 40 Index	5,240	4,766	-1.5	-1.4	48	14.4	1.5	3.4
Swiss Market Index	8,784	3,083	-1.4	-6.4	55	15.4	2.3	3.6
Nikkei Index	21,381	15,110	-2.7	-5.7	43	16.0	1.7	1.9
S&P/ASX 200 Index	5,950	3,766	-1.4	-2.2	66	16.0	2.0	4.4
Stoxx Europe 600 Index	375	34,955	-1.2	-3.7	53	14.5	1.8	3.7
Dubai Financial Market General Index	3,207	57	-1.2	-4.8	25	8.4	1.1	5.2
Abu Dhabi Sec Market General Index	4,567	35	-0.7	3.8	42	11.2	1.5	5.2
Tadawul All Share Index	7,762	944	4.6	7.4	58	14.3	1.6	3.5
Istanbul SE National 100 Index	117,651	1,550	-1.1	2.0	66	8.5	1.3	3.8
Egyptian Exchange Index	17,147	69	10.8	14.2	87	13.1	2.4	3.3
Kuwait Stock Exchange Index	6,687	36	-1.3	4.4	28	-	-	-
Bahrain Bourse All Share Index	1,336	4	-2.4	0.4	67	-	-	-
Muscat Securities Index	4,796	6	-4.1	-5.9	43	9.6	0.9	5.7
Qatar Exchange Index	8,873	58	2.5	4.1	80	12.4	1.4	4.3
MADEX Free Float Index	10,564	13	-1.4	4.6	64	18.7	2.8	3.5
Hong Kong Hang Seng Index	31,415	6,608	1.0	4.2	80	12.3	1.3	3.3
Shanghai Composite Index	3,281	31,528	-0.2	-1.7	20	12.8	1.5	2.2
Korea Stock Exchange Index	2,485	6,166	2.9	1.2	46	9.6	1.1	2.0
BSE Sensex	33,136	117	-3.1	-2.7	48	21.8	2.9	1.4
Nifty	10,155	1,877	-3.2	-3.6	44	20.5	2.9	1.5
Karachi Stock Exchange Index	44,646	44	3.3	10.3	42	9.8	1.6	5.5
Taiwan SE Weighted Index	11,011	4,106	1.9	3.6	60	14.2	1.8	4.0
Bovespa Brasil Sao Paulo SE Index	84,977	2,846	-0.4	11.2	73	-	-	-
Micex Index	2,309	761	0.5	9.5	73	6.5	0.8	5.7
FTSE/JSE Africa All Share Index	58,289	2,155	-0.1	-2.0	57	16.1	2.0	3.2
Vietnam Ho Chi Minh Stock Index	1,169	263	4.9	19.5	46	20.2	3.5	1.4
Jakarta SE Composite Index	6,313	497	-4.0	-0.3	51	16.1	2.5	2.0
FTSE Bursa Malaysia KLCI Index	1,866	278	0.8	4.1	76	16.6	1.7	3.3
Mexican Stock Exchange	47,522	359	0.2	-3.7	35	-	-	-

Prices as of 21 March 2018
Source: Bloomberg, Emirates NBD Research

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