Monthly Insights

18 March 2020

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Preface

Global macro: Ever more stringent measures imposed by governments across the world in a bid to impede the spread of the Covid-19 coronavirus will weigh heavily on economic growth this year. Developed economies are set to see flat-to-negative growth in 2020.

GCC macro: Against the deteriorating global macro backdrop, the non-oil sectors of the GCC are unlikely to expand this year. Add to this the impact of sharply lower oil revenues and the ability of governments in the region to increase spending to support growth is much more limited. We have revised our GDP growth and fiscal forecasts in the region accordingly.

Sub-Saharan Africa macro: Sub-Saharan Africa was slow to report cases of the coronavirus, but now it has reached the region the impact will likely be severe. SSA will not only be affected by the direct impact of the disease, but also through the commodities channel (lower prices and diminished exports) and capital flight as risk-off sentiment rises.

MENA macro: Egypt has closed all international airports through the second half of March at least, the latest development which will serve to hobble the tourism sector in 2020. Rapid monetary easing by the CBE will be only a modest salve, and the economy is set to suffer as a result.

Currencies: With the world now entering a twilight zone of lockdowns and social distancing, it may be some time before accurate economic data is seen on which to base rational investment decisions. FX markets are likely to reflect this vacuum, with reduced liquidity likely to be the main factor moving currencies rather than fundamentals.

Financial Markets: Over the last month, financial markets entered unchartered territory as a classic 'Black Swan' event emerged. Relative to a standstill in global economic activities, gyrations in financial markets have been intense.

Commodities: Oil markets have fallen into a vortex as the twin shocks of extensive demand destruction caused by the Covid-19 pandemic and a market-share strategy adopted by OPEC and its rivals weighs on markets.

Timothy Fox
Chief Economist & Head of Research

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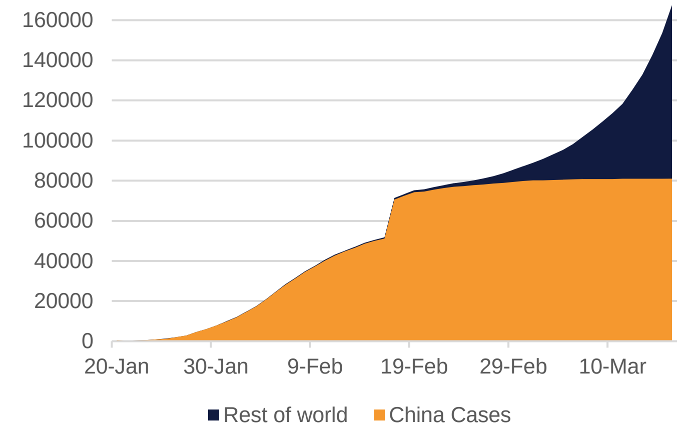
Global Macro

The coronavirus outbreak which began in China but has since spread to encompass over 140 countries worldwide continues to wreak havoc in the global economy, and looks set to continue to do so for some time to come. There remains a great deal of uncertainty regarding just when the disease will be contained, but government scenarios are increasingly tending towards the bleaker end of projections, envisaging a protracted impact and potentially millions infected at its peak. As such, we will not look to try and adjust our global growth forecasts with enormous precision for the time being, in common with the US Fed who have said they will not publish their new projections until June. Rather we are now simply assuming a global recession on account of supply disruptions and a sudden stop to demand, with flat-to-negative growth rates in most developed countries reflecting this.

More cases now outside China than in



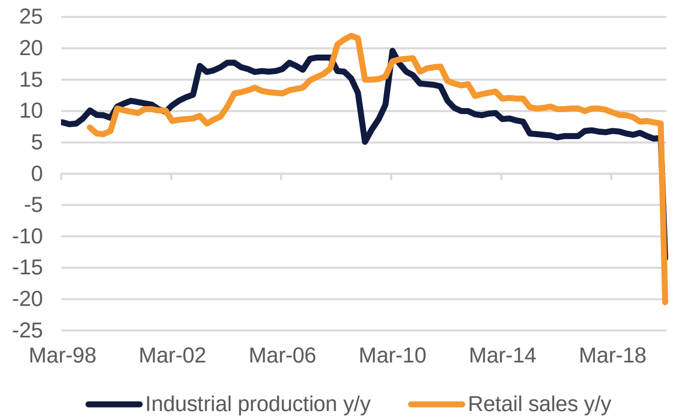
Source: WHO situation reports, Emirates NBD Research (China figures include Hong Kong & Macau but exclude Taiwan),

Nevertheless, what looks increasingly certain is that many countries are recession-bound in 2020, and that the negative impact will take many sectors to breaking point. The coordinated monetary policy response we have seen is no longer sufficient to calm market turbulence, with stocks plummeting on March 16 despite a surprise Fed cut the day before. As such, it is increasingly on the fiscal front that the difference will be made. First, though, the priority will be containing the disease, and we are seeing progressively more governments and local authorities implement measures that will paralyse their economies in the near term, but hopefully return the desired effect in stemming the spread.

Economic data starting to indicate the gravity

We are starting to see the economic data confirm what the markets have been saying for some time, especially those now coming out of China. The outbreak began in the Chinese province of Hubei in late 2019 before taking hold around the country, and the government was fairly swift to implement draconian restrictions on activities. In January/February, industrial output declined -13.5% y/y, retail sales declined -20.5%, and fixed asset investment dropped nearly a quarter. To put this into context, this is the first time any of these data points have fallen y/y since the series began in 1998. Reassuringly, the number of new cases reported in China has slowed dramatically in recent weeks, but the recovery in economic activity will take time, especially given the foothold the disease has now taken in key trading partners.

China slump the worst on record



Source: Bloomberg, Emirates NBD Research

Regardless of the fact that the Chinese economy comprises nearly a fifth of global GDP, and affects other economies through its massive commodities imports and the growing importance of its consumer base, all major global economies now look set to be afflicted by their own localised outbreaks, and a global recession looks increasingly likely. Italy, Iran and Korea have the highest number of reported cases after China, but there have been rapid spreads in the US, Spain, France, Germany, and many other key markets also. The growth outlook for these countries was already fairly lacklustre, and it seems fair to say that this crisis has come about when the global economy was not in a position of particular strength from which to endure it. The US Empire State Manufacturing survey released on March 16 dropped by a record 34.4 points to -21.5, the lowest level since the global financial crisis.

US Empire state manufacturing survey

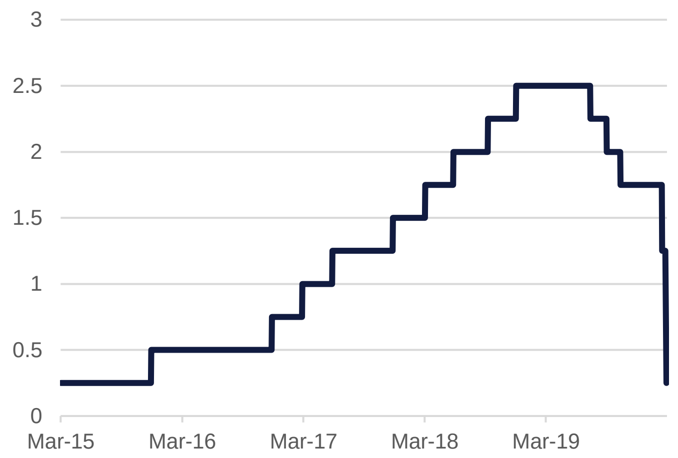
Source: Bloomberg, Emirates NBD Research

Many countries have now implemented their own severe restrictions, with Italy and Spain in particular leading the way through effectively quarantining millions of people. Around the world, travel restrictions have been put in place, with the global air travel and tourism sectors set to fall off a cliff – American Airlines has announced that it will cut long-haul international services by 75%, while IAG is cutting capacity by at least 75% for the next two months. Ryanair has cut capacity 80%. The closure and cancellation of bars, clubs, cinemas, events and shops worldwide will hit the tourism and retail sectors. All of these developments will hit jobs. The wealth effect, as savers see the value of their holdings fall as equity indices plummet, will likely further impact activity, as consumers increasingly hunker down and look to effectively sit the next several months out. As things stand, it seems hard to overstate the risk to global output.

Central banks have shot their bullets

In such an extraordinary environment, it is little surprise that there has been an extraordinary response from central banks, most notably from the US Fed. On March 15, the central bank made its second irregular 50bps cut to the target rate in as many weeks, taking the upper bound to just 0.25%, equal to the lows seen as the global financial crisis took hold (subsequently kept through to 2015). Other central banks to have implemented cuts since the crisis took hold include the Bank of England (50bps on March 11), Bank of Canada (100bps over the past two weeks), Reserve Bank of New Zealand (75bps on March 16) and Reserve Bank of Australia (25bps on March 2). China cut its one-year prime rate to 4.05% on February 29.

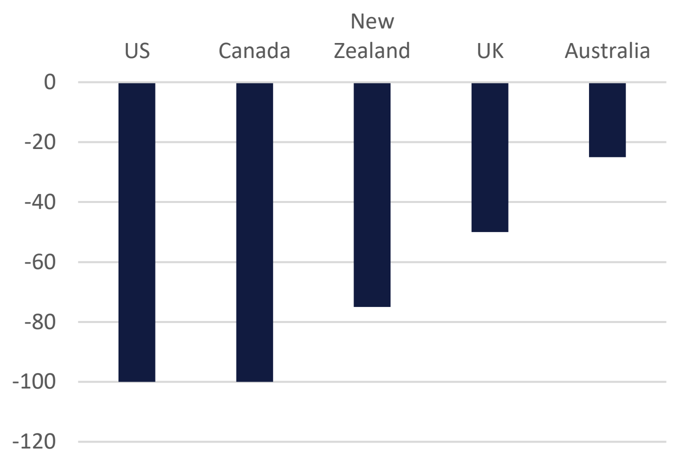
Extraordinary cuts to Fed funds rate



Source: Bloomberg, Emirates NBD Research

The notable outliers are the ECB and the BOJ, which have both maintained their benchmark rates at -0.5% and -0.1% respectively. However, that is not to say that they have not been active. The BOJ is buying more assets, is set to double the pace of its ETF purchases, and has also introduced a new zero-rate loan facility. The ECB, meanwhile has widened the TLTRO through allowing banks to borrow for three years at -0.25% and has implemented a 'temporary envelope of additional net asset purchases of EUR 120bn' until the end of the year. These measures are in common with the other central banks, with QE boosted to varying degrees. In its surprise March 15 move, the Fed promised to boost bond holdings by at least USD 700bn.

DM central banks cutting deep in March



Source: National sources, Emirates NBD Research

The fact that the two major developed market central banks to not cut rates in recent weeks are both already in negative territory is perhaps illustrative of concerns that such moves are reaching the limits of their efficacy, especially in the face of what is a health, rather than a financial, crisis (at least for now). BOJ governor Haruhiko Kuroda has said that they will 'cut the rate deeper' if needed, but the diminished firepower available to central banks to combat this as compared to previous crises is starkly apparent. There will likely be more tinkering around the edges in terms of QE and financial engineering, and the move from global central banks to lower the pricing on USD liquidity swap arrangements is an encouraging instance of a coordinated response, but there is a sense that central banks have fired their bullets already. Even prior to the coronavirus outbreak there were mounting calls for greater fiscal stimulus to boost growth this year, but now there is a stark necessity for government action in order to stave off collapse.

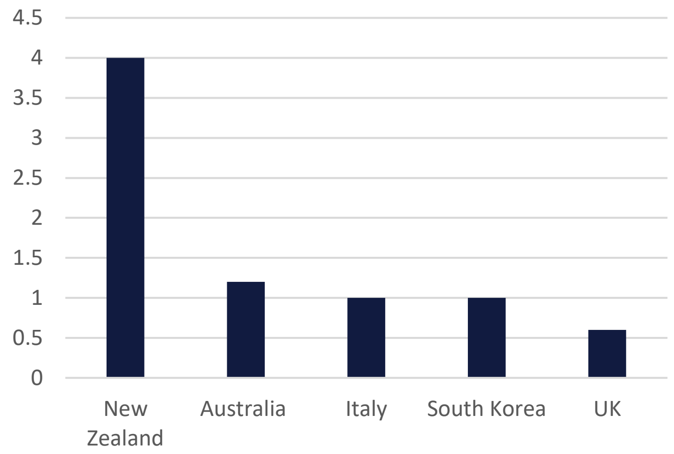
Bloomberg US financial conditions index

Source: Bloomberg, Emirates NBD Research

Fiscal response will now be key to recovery

Fiscal responses to the crisis have been somewhat slower coming than the monetary policy responses, reflecting the greater political implications of such moves, and the greater accountability of governments as compared to central banks. Nevertheless, the scale of the negative impact of the coronavirus outbreak means that automatic stabilisers will be far from sufficient to counter this crisis, and concerted government action will become increasingly crucial. As the number of cases have risen in various countries the respective governments have for the most part indicated their awareness of this, and announced a series of general and targeted support measures. Among the most headline-grabbing fiscal stimulus packages so far announced are New Zealand's USD 7.3bn (4% GDP), Australia's USD 11.4bn (1.2% GDP), Italy's USD 28bn (1% GDP), and South Korea's USD 9.8bn (1% GDP). In the UK, newly appointed chancellor, Rishi Sunak, introduced an expansionary budget of some USD 37bn (0.6% of GDP, though not all in response to the current crisis).

Notable stimulus to date, % GDP



Source: Bloomberg, Emirates NBD Research

Even Germany has prepared to abandon its long-standing reluctance to spend, promising on March 13 to make EUR 550bn in lending available to companies through state bank KfW to survive the crisis and protect their employees. Finance minister Olaf Scholz said that 'this is the bazooka', adding that 'we'll check later to see if we need additional weapons' – meaning the possibility of Germany taking on debt and enacting full-blown stimulus if necessary.

In the US, the response has been slow, but the first stimulus bill was passed overwhelmingly by the House of Representatives on March 13 on a rare bipartisan sweep, at 363-40. It is expected to pass the Senate, and President Donald Trump has pledged to sign it off as soon as he receives it. The White House has subsequently proposed stimulus measures, including cash payments to individuals, worth USD 1.2tn in a bid to keep the unemployment rate from rocketing.

Many of these various plans contain similar measures, such as business tax rebates for small companies, subsidies to firms to enable them to continue paying staff, benefits for the self-employed who have been forced to self-isolate and low-cost loans to businesses. These will help those affected weather the storm, but beyond the near term there will be further calls for spending to kick-start the economic recovery once the crisis has passed – how able governments will be to do this remains to be seen.

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Key Economic Forecasts – Global

US	2015	2016	2017	2018	2019e	2020f	2021f
Real GDP %	2.9	1.6	2.4	2.9	2.3	0.0	2.5
Current A/C % GDP	-2.2	-2.3	-2.3	-2.4	-2.6	-2.4	-2.4
Budget Balance % GDP	-2.6	-3.1	-3.4	-4.2	-4.7	-4.8	-4.7
CPI %	0.1	1.3	2.1	2.5	1.8	2.1	2.1
Eurozone							
Real GDP %	2.1	1.9	2.5	1.9	1.2	-1.0	0.8
Current A/C % GDP	2.8	3.3	3.2	3.1	3.0	2.7	2.6
Budget Balance % GDP	-2.0	-1.4	-0.9	-0.5	-0.8	-1.1	-1.1
CPI %	0.2	0.2	1.5	1.8	1.2	1.3	1.4
UK							
Real GDP %	2.4	1.9	1.9	1.3	1.4	0.1	1.5
Current A/C% GDP	-4.9	-5.2	-3.5	-3.9	-4.3	-3.9	-3.8
Budget Balance % GDP	-4.5	-3.3	-2.5	-2.2	-1.9	-2.4	-2.4
CPI %	0.0	0.7	2.7	2.5	1.8	1.7	1.9
Japan							
Real GDP %	1.3	0.5	2.2	0.3	0.7	-0.5	0.6
Current A/C % GDP	3.1	4.0	4.1	3.5	3.3	3.3	3.3
Budget Balance % GDP	-3.6	-3.5	-3.0	-2.4	-2.6	-2.9	-2.7
CPI %	0.8	-0.1	0.5	1.0	0.5	0.7	0.6
China							
Real GDP %	7.0	6.8	6.9	6.7	6.1	3.5	6.2
Current A/C % GDP	2.8	1.8	1.6	0.4	1.2	0.8	0.5
Budget Balance %GDP	-3.4	-3.8	-3.7	-4.1	-4.9	-4.8	-4.6
CPI%	1.4	2.0	1.6	2.1	2.9	3.1	2.2
India*							
Real GDP%	7.4	8.0	8.3	7.0	6.1	5.0	6.0
Current A/C% GDP	-1.1	-0.6	-1.5	-2.4	-0.9	-1.3	-1.6
Budget Balance % GDP	-3.5	-3.6	-3.9	-3.6	-3.5	-3.7	-3.5
CPI %	4.9	5.0	3.3	4.0	3.7	4.4	4.3

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

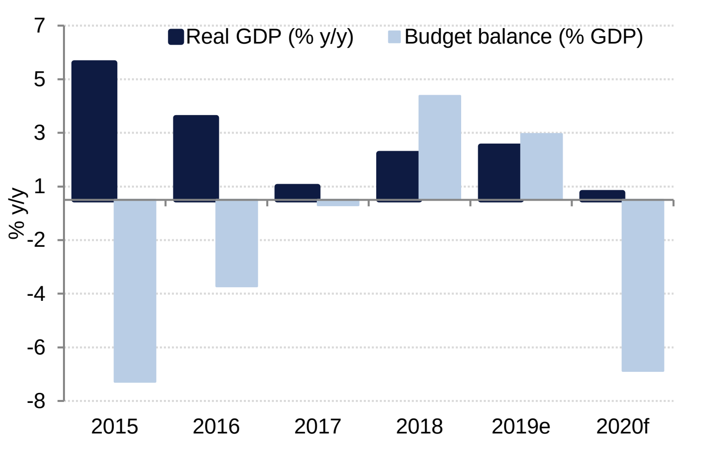
GCC Macro

The speed with which events have evolved globally and in the region over the last month, and the still-high level of uncertainty combined with a lack of actual economic data points in the GCC have made it even more difficult than usual to forecast key economic indicators. Besides Saudi Arabia, no GCC country has published GDP statistics for 2019 yet. The decision by OPEC+ to abandon production curbs has led to a significant drop in oil prices with negative consequences for GCC budgets.

The near daily changes in how governments around the world are responding to the spread of the coronavirus with new travel curbs, closure of entertainment and leisure services and in some countries complete lockdown; and the uncertainty about how long all this will last suggests that there will continue to be downside risks to even our revised forecasts. Nevertheless, we have made some adjustments to our outlook for the region to take into account the developments so far. The European Commission has indicated a contraction of -1% is possible this year, and President Trump indicated that the US economy may go into recession. Recent economic data from China points to a GDP contraction in Q1 2020 on an annual basis.

Against this background, the non-oil sectors of the GCC are unlikely to expand this year. Add to this the impact of sharply lower oil revenues and the ability of governments in the region to increase spending to offset the weaker global backdrop is much more limited.

UAE GDP growth and budget deficit



Source: Haver Analytics, UAE Ministry of Finance, Emirates NBD Research

In the UAE, the PMI survey data for January and February indicate a modest contraction in the non-oil private. However, the most severe restrictions came into effect only in March, so we think a contraction in non-oil activity H1 is now likely. Assuming economic activity starts to recover in Q3 and strengthens sharply in Q4, we estimate UAE non-oil sector growth of -0.7% in 2020. However, the UAE's oil sector is likely to grow 2.5% on average in 2020 as crude output curbs are lifted and investment in new oil and gas capacity increases. Overall then, we expect headline GDP growth of 0.3% in 2020, down from an estimated 2.0% in 2019, and lower than our previous forecast of 1.6%. We expect growth to rebound in 2021 to 2.0-2.5%.

The double-whammy of the coronavirus and lower oil prices is also reflected in our new budget estimates for this year. Oil revenue is likely to decline by around -30% from 2019, but non-oil revenue will also be affected as a result of lower fee and tax revenue. In addition to the waiving of fees and taxes, increased subsidies and other measures announced over the last few days by the governments of Dubai and Abu Dhabi in order to support private sector businesses, weaker consumption generally and the shuttering of many leisure and services businesses will have a negative impact on VAT income as well. As a result, we now see the UAE budget moving into deficit of around 6.4% of GDP this year.

For Saudi Arabia, we have revised down our non-oil sector growth forecast to -0.2%, as the government is reportedly looking to reduce spending by more than had been budgeted in the face of sharply lower oil prices, and strict restrictions on travel and social interactions have been introduced. While the PMI survey data have indicated some improvement in business conditions in January-February, the readings were lower than the same period last year. As with the UAE, the impact of travel curbs and restrictions on hospitality, retail and other sectors' activities will likely only be reflected from March onwards. However with oil production set to rise sharply from April, we have upgraded our 2020 oil sector growth forecast to 3.3%. Headline GDP growth in the kingdom is now forecast to reach 1.2% in 2020, only fractionally lower than our previous forecast of 1.3%.

We have also revised our deficit projection for KSA to -10.2% of GDP this year, from -7.2% previously, and much wider than the -4.5% deficit recorded in 2019. This assumes a -4.5% decline in total government spending this year, compared to the budgeted -2.7% decline.

For other GCC countries we have assumed zero non-oil growth in 2020 and adjusted oil sector growth figures higher to reflect increased oil production. For the GCC as a whole then, we now estimate real GDP growth of 0.9% in 2020 down from 1.5% previously. The weighted average budget deficit for the region is forecast to widen to -10% of GDP, from an estimated -3.6% of GDP in 2019.

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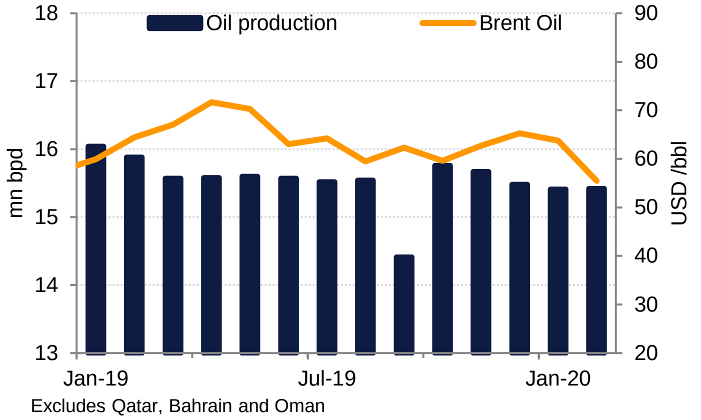
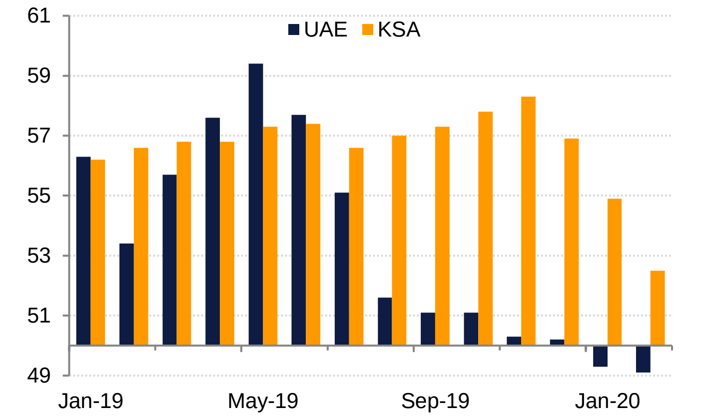
GCC in Pictures

GCC Oil Production and Oil Price



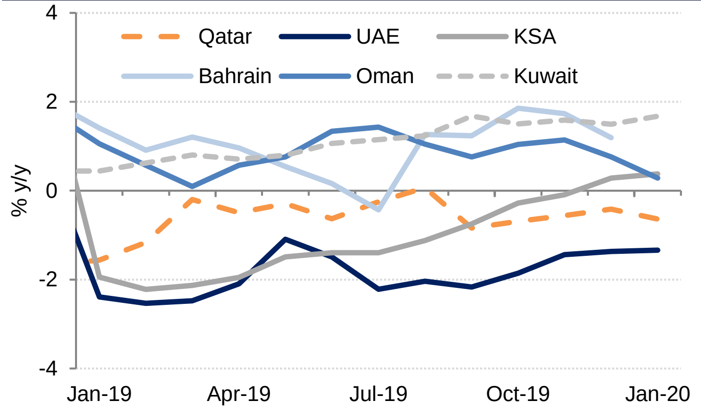
Source: Bloomberg, Emirates NBD Research

Purchasing Managers' Index



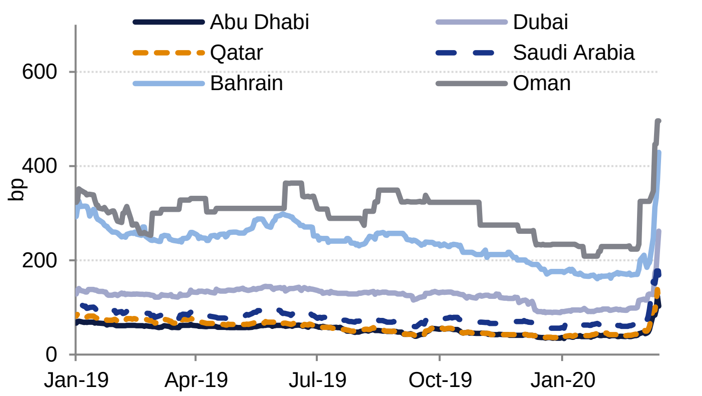
Source: IHS Markit, Emirates NBD Research

Inflation



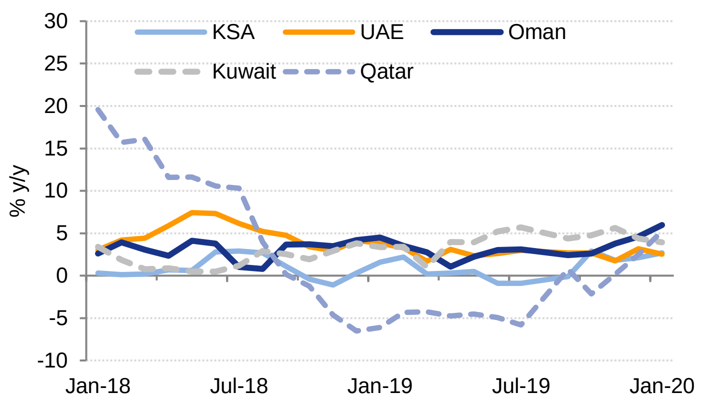
Source: Haver Analytics, Emirates NBD Research

CDS Spreads



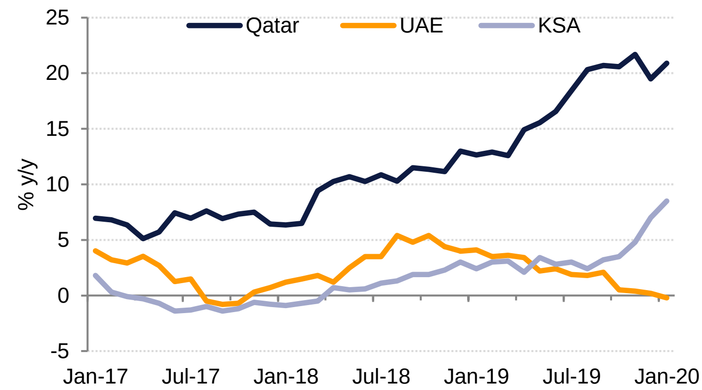
Source: Bloomberg

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

Key Economic Forecasts - GCC

United Arab Emirates	2017	2018	2019e	2020f	2021f
Nominal GDP $bn	378.0	414.5	411.5	385.9	412.2
Real GDP %	0.5	1.7	2.0	0.3	2.4
Current A/C % GDP	7.3	9.1	7.5	3.1	0.0
Budget Balance % GDP	-0.2	3.9	2.4	-6.4	-3.4
CPI %	2.0	3.1	-1.9	0.0	2.0
Saudi Arabia					
Nominal GDP $bn	688.6	786.5	793.0	746.8	796.9
Real GDP %	-0.7	2.4	0.3	1.2	2.0
Current A/C % GDP	1.5	9.0	4.2	-3.1	0.0
Budget Balance % GDP	-9.2	-5.9	-4.5	-10.2	-7.3
CPI %	-0.8	2.5	-1.2	1.0	2.0
Qatar					
Nominal GDP $bn	166.9	191.4	182.5	171.2	202.3
Real GDP %	1.1	1.4	-1.3	0.4	3.2
Current A/C % GDP	3.8	8.7	3.8	-8.4	-3.7
Budget Balance % GDP	-6.6	2.2	-1.6	-7.9	-4.8
CPI %	0.4	0.3	-0.7	1.0	1.5
Kuwait					
Nominal GDP $bn	119.5	141.5	138.9	138.0	147.5
Real GDP %	-3.5	1.2	0.5	1.2	2.2
Current A/C% GDP	8.0	14.4	9.4	4.7	6.7
Budget Balance % GDP	-9.0	-3.0	-13.4	-15.9	-12.6
CPI %	1.6	0.6	1.0	1.5	1.5
Oman					
Nominal GDP $bn	70.5	79.2	77.8	70.6	74.6
Real GDP %	0.3	1.8	1.1	0.8	1.7
Current A/C % GDP	-15.6	-5.5	-6.8	-14.1	-10.6
Budget Balance % GDP	-13.9	-8.7	-10.4	-14.2	-11.0
CPI %	1.6	0.9	0.1	1.0	1.0
Bahrain					
Nominal GDP $bn	35.4	37.7	38.4	37.1	39.2
Real GDP %	3.8	1.7	1.4	0.2	2.0
Current A/C % GDP	-4.5	-5.9	-6.4	-8.3	-7.7
Budget Balance % GDP	-10.0	-6.3	-4.9	-8.3	-6.5
CPI %	1.4	2.1	1.0	1.0	1.5
GCC (Nominal GDP weighted avg)					
Nominal GDP $bn	456	518	523	494	525
Real GDP %	-0.3	2.0	0.6	0.9	2.2
Current A/C % GDP	8.1	15.6	10.5	-0.5	-0.9
Budget Balance % GDP	-6.8	-2.4	-3.6	-10.0	-6.8
CPI %	0.1	2.4	-0.5	1.5	2.6

Source: Haver Analytics, National sources, Emirates NBD Research

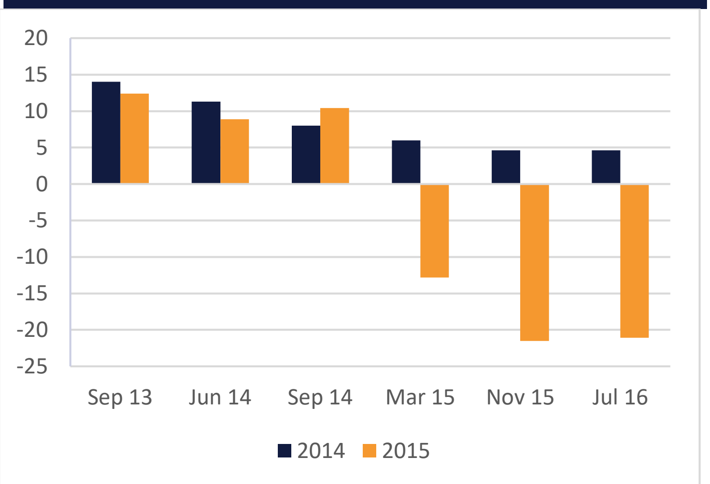
Sub-Saharan Africa Macro : Potential three-way hit from crisis

Sub-Saharan Africa (SSA) was slow to confirm cases of Covid-19 but the disease has now started to take hold in the region, with potentially hazardous consequences for ill-equipped health services. Even should SSA economies be successful in containing the disease and limiting its local impact, they will suffer through the sharp decline in demand for commodities, and their prices, seen since the start of the year, and through the general risk-off sentiment which will likely prompt capital flight.

Direct impact

The ill-preparedness of many SSA countries for a medical emergency was starkly illustrated during the West African Ebola outbreak which began in 2014, affecting Guinea, Liberia and Sierra Leone most dramatically. Despite significant aid from France, the US and UK in particular the countries' health services were found to be insufficient to deal with the outbreak. People not only died from the disease itself, but hospitals were unable to provide their usual care for more common diseases such as malaria, exacerbating the impact. Should the coronavirus outbreak take a greater hold in SSA, this is likely to play out in a similar manner. The DRC has already been battling a deadly measles outbreak which has claimed over 6,000 deaths, and the country has now reported its first two coronavirus cases. The difference between this coronavirus outbreak and the 2014-2015 Ebola crisis is that with the disease having taken root around the world, the ability of the international community to provide aid will be significantly reduced.

Sierra Leone IMF real GDP growth revisions



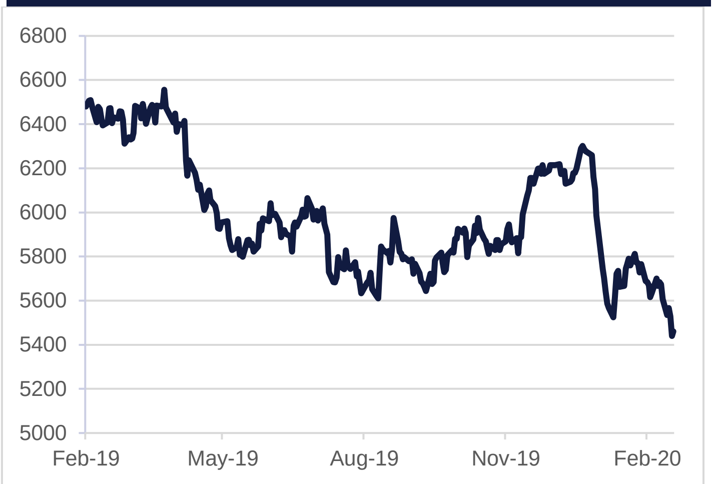
Source: IMF, Emirates NBD Research.

Aside from the terrible human cost, the Ebola outbreak devastated these three West African countries economically also. For instance, the IMF forecast 2015 real GDP growth of over 10% in Sierra Leone prior to the crisis. In the event, the economy contracted by over 21%, while the growth outlooks for Guinea and Liberia were also slashed. A collapse in nascent tourism sectors, quarantines and restrictions on travel, a reduction in investment and mothballing of projects by mining firms and other international companies all combined to devastate the economies. As countries implement restrictions in a bid to contain the virus, and tourism is hit, growth in SSA economies is likely to be severely impeded this year also.

Commodities channel

It is true that the complete disintegration of the growth outlooks for those three West African economies devastated by Ebola in 2014-2015 was not solely owing to the disease; the collapse in iron ore prices that year also played a part. Major projects such as the Simandou mine in Guinea were delayed or cancelled as the lower global prices, combined with the local disruption, served to make them untenable. However, SSA economies, whether directly impacted or not by the coronavirus outbreak, look set to be hit through the commodities channel this year also.

Copper hit by stalling demand



Source: B, Emirates NBD Research

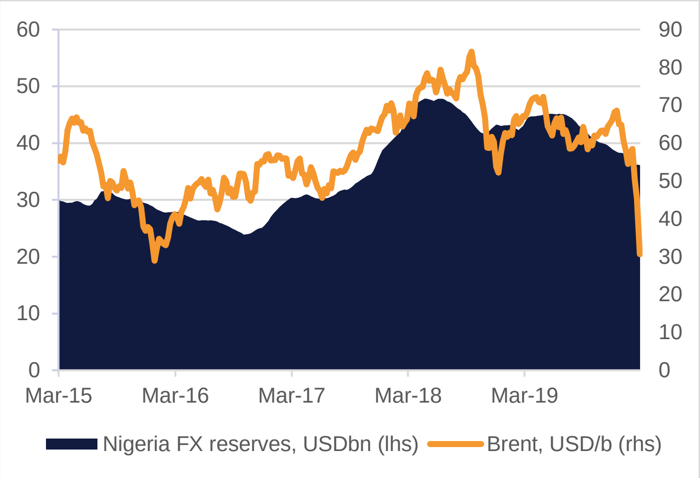
February data for China, the epicentre of the coronavirus outbreak, shows just how severe the impact of the outbreak has been on the economy, as industrial production declined -13.5% y/y. As the biggest importer of a host of commodities, with many of these provided by SSA countries, this will have a massive impact on African exports, especially as the disruption has spread to other major import economies. This has been reflected in commodity prices, with copper prices down 13.4% from its recent January peak. Oil, meanwhile, which has seen its price crunch exacerbated by a market share war between Russia and Saudi Arabia, has lost over half from where it was in January.

As such, SSA economies will be hit through lower exports, and governments will also have diminished fiscal space to implement stimulus, just as the need to do so becomes more pressing. Since the debt forgiveness at the turn of the century, many countries have seen their debt levels steadily rise once again, fueled by cheap money and the global hunt for yield. While global interest rates look set to remain low for some time, investors' risk appetite for many of these economies will be far less than it was.

Capital outflows

Finally, those countries which attract portfolio inflows will struggle as their outlook becomes less positive and global risk aversion rises. Nigeria's outlook is increasingly clouded given the economy's reliance on the oil sector. Although oil makes up only around 10% of GDP, it accounts for over 90% of exports, and the government needs prices around USD 57/b to balance its budget. With oil unlikely to recover any time soon, reserves – already at a more-than-two year low – will continue to decline, raising questions over the naira peg's sustainability. Capital importation in Nigeria was already declining in Q4, when it fell 32.4% y/y, and this is likely to fall further in the current environment.

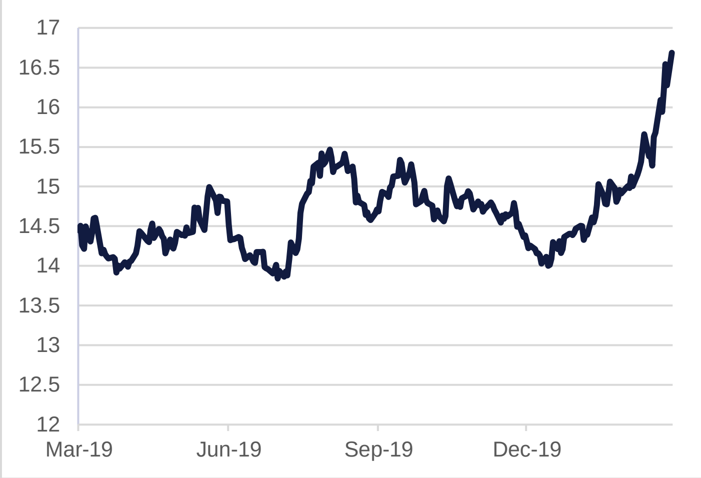
Naira peg will come under pressure



Source: Bloomberg, Emirates NBD Research

South Africa meanwhile, which has declared a national disaster with attendant restrictions on travel and gatherings, is also under pressure. There were already significant questions around fiscal sustainability given ongoing issues with parastatal energy firm Eskom, and the risk around a Moody's downgrade which would see the country lose its last non-junk rating, prompting automatic bond outflows. The latest developments have exacerbated these pressures, illustrated in a sell-off across FX, bond and equity markets.

ZAR/USD exchange rate



Source: Bloomberg, Emirates NBD Research

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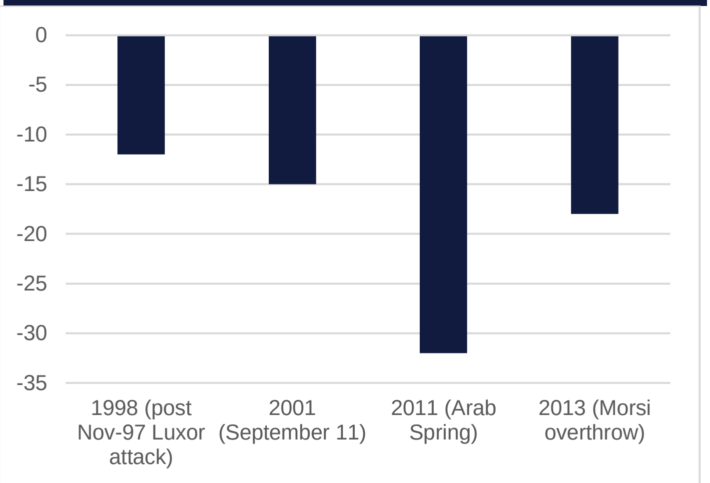
MENA Macro: Egypt tourism sector set for renewed pain

As the coronavirus has hit North Africa, the Egyptian authorities have taken dramatic steps to both limit the outbreak's spread, and to try and protect the economy from the negative side effects of these measures. Nevertheless, as with both developed and emerging markets around the world, the outlook for the Egyptian economy is now far bleaker than it was prior to the outbreak. We are revising our forecasts to reflect this, but until the severity and longevity of both the local and global outbreaks are clearer, these are heavily caveated. The risks are weighted to the downside at present.

Egypt had 126 confirmed cases as of March 16, according to the WHO's latest situation report. With local transmission entrenched and 33 new cases reported that day, it seems likely that the number will head higher, putting considerable strain on the country's healthcare services. With the initial cases having been brought into the country by tourists on Nile cruises, the government on March 16 took the extraordinary measure of halting all international flights from March 19 through to the close of the month. This will have a multi-faceted impact on the real and nominal economies.

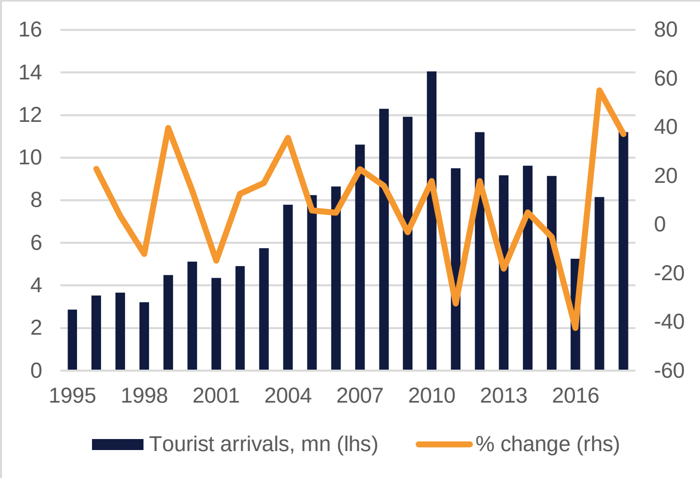
% declines in visitor numbers



Source: World Bank, Emirates NBD Research

From a growth perspective, it will lead to weaker tourism activity than would have otherwise have been anticipated. Egyptian tourism has been a growth sector in recent years, with visitor numbers posting growth of 55% and 37% respectively in 2017 and 2018. Growth last year was likely also strong given that the year started with y/y growth of 21% over January-February, and balance of payments data indicate a robust expansion in travel receipts. However, the expansion has now been derailed in 2020. This will weigh on real GDP growth given that the sector accounted for 11.9% of GDP in 2018 (direct and indirect), according to the World Travel & Tourism Council. Crucially, it also provided 2.5mn jobs, nearly 10% of the total, and the impact here will be particularly severe, especially combined with other restrictions on movement imposed by the Egyptian government.

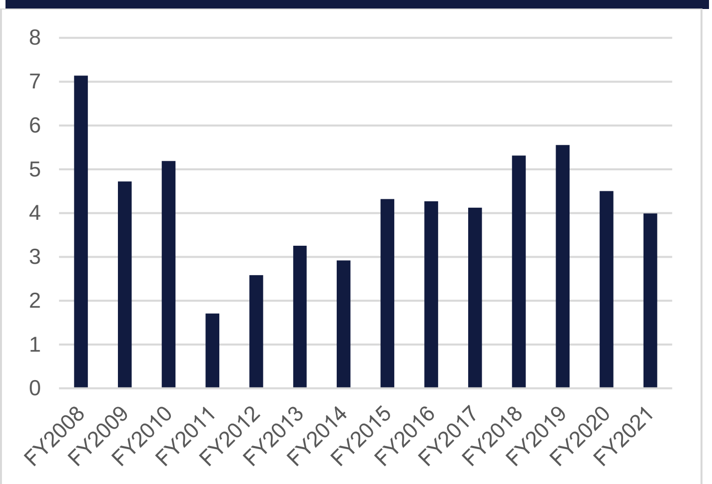
Tourist arrivals still off 2010 peak



Source: World Bank, Emirates NBD Research

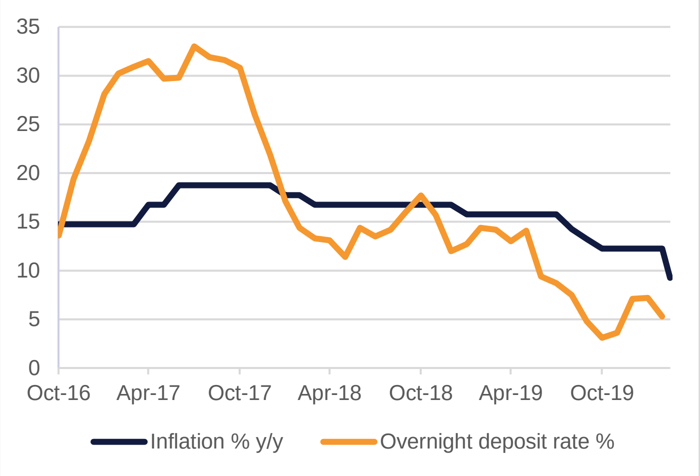
While the Egyptian closure of air travel may be lifted at the end of March, it is unlikely that there will be a rapid recovery in visitor numbers given there will be continued local travel bans in source countries and tourists will probably remain reluctant to travel for some time to come; new bookings are reportedly down 80%. That is not to say that the Egyptian tourism sector will not recover, but it could take some time; visitor numbers in 2018 were still off the pre-Arab Spring 2010 peak, and this poses a further setback to the recovery process. We have made initial downward revisions to our 2019/20 (ending June 30) and 2020/21 forecasts, from 5.5% and 5.9% to 4.5% and 4.0% respectively, but the risks are to the downside. Aside from the tourism sector, Egypt will also be bit by lower trade flows through the Suez Canal and slower FDI into the gas sector, while lower remittances from Gulf states will compound the negativity.

% declines in visitor numbers



Source: Haver Analytics, Emirates NBD Research

Real rates still positive



Source: Haver Analytics, Emirates NBD Research

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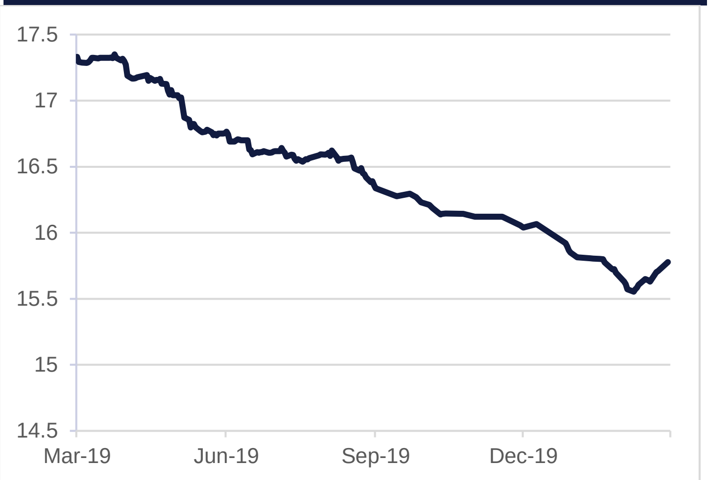
The Egyptian authorities have not only been active in trying to prevent the disease's spread: they have also introduced measures aimed at shoring up the domestic economy. Most notably, the Central Bank of Egypt (CBE) made an irregular 300bps cut to the benchmark overnight deposit rate on March 16, taking it to 9.25%. The cut indicates a change in tack by the CBE, indicating a commitment to supporting local demand in the face of the coronavirus crisis even at a risk to portfolio inflows and potential currency weakness. With inflation having dipped to 5.3% y/y in February, real interest rates are still in positive territory following the surprise CBE move, but the attractiveness of the Egyptian local debt market will have diminished.

EGP/USD exchange rate



Source: Haver Analytics, Emirates NBD Research.

That being said, a generalised global risk-off sentiment is entrenching in the face of the virus-related uncertainty in any case, and it would have been hard indeed for the CBE to maintain hot money inflows in such an environment. Added to this, the balance of payments will be under pressure from the anticipated lower tourism revenues, canal revenues, remittances, FDI and gas exports, not sufficiently mitigated by lower petroleum imports. As a result, a continuation of the sell-off of the EGP seen over recent weeks is likely.

Key Economic Forecasts – Non-GCC Oil Importers

Egypt*	2017	2018	2019e	2020f	2021f
Nominal GDP $bn	225.8	241.5	291.7	345.1	371.0
Real GDP %	4.1	5.3	5.6	4.5	4.0
Current A/C % GDP	-6.4	-2.5	-3.7	-3.1	-3.9
Budget Balance % GDP	-10.8	-9.8	-8.6	-7.4	-6.7
CPI %	29.6	14.4	9.4	7.5	8.0
Jordan	332.4	225.8	241.6	299.2	368.4
Nominal GDP $bn	40.7	41.5	42.5	43.5	44.5
Real GDP %	2.1	2.0	2.1	0.0	2.1
Current A/C % GDP	-10.8	-7.1	-5.4	-6.6	-7.9
Budget Balance % GDP	-2.7	-2.6	-2.2	-4.3	-4.8
CPI %	3.3	4.5	0.3	1.8	2.5
Lebanon					
Nominal GDP $bn	52.1	62.3	65.9	66.0	70.4
Real GDP %	0.6	0.2	-0.3	-6.2	1.1
Current A/C % GDP	-23.3	-21.4	-21.5	-23.1	-23.6
Budget Balance % GDP	-7.0	-10.8	-9.3	-11.8	-10.8
CPI %	4.5	6.1	2.5	10.0	5.0
Morocco					
Nominal GDP $bn	109.6	117.9	118.2	122.0	128.1
Real GDP %	4.2	3.0	2.5	1.1	3.3
Current A/C % GDP	-3.4	-5.5	-4.1	-4.9	-5.3
Budget Balance % GDP	-3.4	-3.4	-4.2	-4.3	-4.0
CPI %	0.8	1.8	0.2	0.6	0.8
Tunisia	103.3	109.6	117.9	119.1	123.7
Nominal GDP $bn	40.1	35.6	33.6	34.6	35.6
Real GDP %	2.0	2.4	1.6	-0.1	3.1
Current A/C % GDP	-10.2	-12.5	-12.2	-11.5	-10.3
Budget Balance % GDP	-6.7	-5.6	-5.1	-4.7	-4.4
CPI %	5.3	7.4	6.7	6.0	5.8
Oil Importers (GDP weighted avg)					
Nominal GDP $bn	147.3	158.6	192.6	233.6	257.5
Real GDP %	3.4	3.6	3.7	3.9	4.5
Current A/C % GDP	-8.3	-6.6	-6.4	-5.6	-5.8
Budget Balance % GDP	-7.6	-7.5	-7.0	-6.4	-5.9
CPI %	15.7	9.1	5.7	5.2	5.5

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

Key Economic Forecasts – Non-GCC Oil Exporters

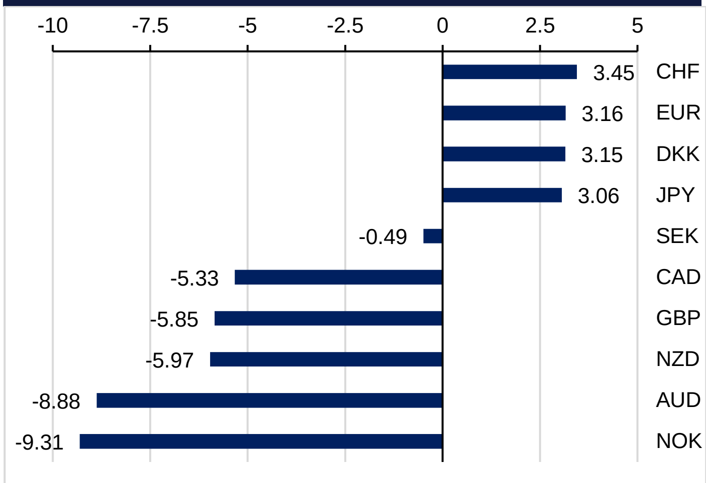
Algeria	2016	2017	2018e	2019f	2020f
Nominal GDP $bn	167.6	165.5	163.4	160.3	164.7
Real GDP %	0.4	1.6	1.0	-0.9	2.0
Current A/C % GDP	-13.3	-10.4	-8.7	-10.6	-10.4
Budget Balance % GDP	-6.5	-9.2	-9.5	-14.9	-14.1
CPI %	6.0	3.5	2.4	2.3	3.2
Iran					
Nominal GDP $bn	446.9	422.4	528.6	632.3	742.1
Real GDP %	3.3	-4.2	-8.7	-5.2	1.7
Current A/C % GDP	3.5	3.7	-0.2	-2.2	-2.2
Budget Balance % GDP	-5.1	-4.2	-4.3	-5.5	-5.1
CPI %	10.0	21.0	38.7	27.5	20.0
Iraq	441.8	446.9	433.4	494.1	586.2
Nominal GDP $bn	166.2	215.5	243.3	243.4	260.5
Real GDP %	1.0	0.3	4.2	0.6	2.7
Current A/C% GDP	9.0	15.9	11.1	5.6	4.6
Budget Balance % GDP	-1.8	8.3	-4.6	-6.0	-4.0
CPI %	0.7	0.4	-0.2	0.8	1.0
Libya					
Nominal GDP $bn	35.4	34.1	35.3	40.9	44.4
Real GDP %	30.3	0.9	2.7	-1.7	-14.9
Current A/C% GDP	-9.5	-2.1	-2.6	-2.7	-2.6
Budget Balance % GDP	-10.6	-7.1	-6.2	-5.5	-5.1
CPI %	25.0	11.5	10.0	8.5	7.0
Oil Exporters (GDP weighted avg)					
Nominal GDP $bn	314.5	302.5	377.4	451.0	534.8
Real GDP %	4.1	-1.4	-3.5	-2.7	1.2
Current A/C % GDP	0.7	3.6	0.3	-1.7	-1.6
Budget Balance % GDP	-6.7	-2.8	-4.8	-6.2	-5.5
CPI %	7.6	12.4	22.3	17.1	13.1

Currencies

Liquidity over fundamentals

Given all the extraordinary events and policy measures over the last month direction in FX markets is understandably becoming more about liquidity than fundamentals. That being said there are some thematic trends that have been apparent. While over the last week the USD has been the main winner from global stimulus steps, as interest rates were lowered around the world, the Fed's move to the zero bound at the start of this week has begun to blunt these gains. Over the month as whole the picture is more mixed, with safe havens like the CHF and the JPY outperforming. Meanwhile commodity reliant currencies have underperformed, and GBP has been another notable casualty.

30 day performance vs USD (%)



Source: Bloomberg. Data as of March 17,2020

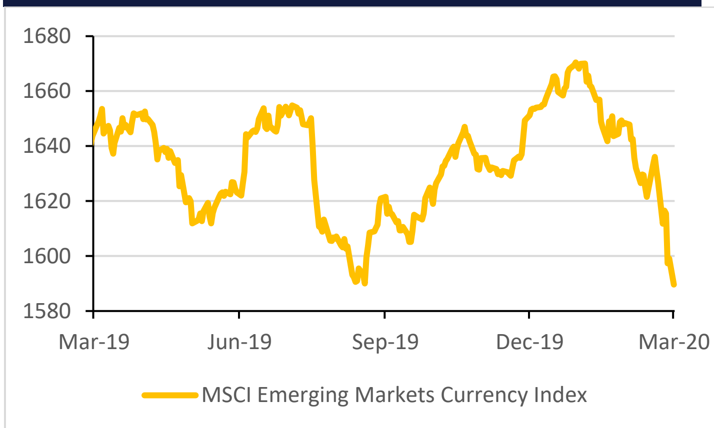
Policy tools close to exhaustion

With central banks in the G7 world having almost exhausted their policy tools over the last few weeks, the scope for fundamentals to drive FX markets is becoming more limited, especially as the reliability of economic data is also in doubt. Indeed with the world now entering a twilight zone of lockdowns and social distancing, it may be some time before accurate economic data is seen on which to base rational investment decisions. FX markets are likely to reflect this vacuum, with reduced liquidity likely to be the main factor in moving currencies than fundamentals in coming weeks. To the extent that residual fundamentals arguments might matter the risk-off theme is likely to remain with us, helping to keep the JPY and the CHF underpinned. The USD appears to alternate in its role as a safe-haven, benefiting to some extent at the start of the coronavirus crisis when it was largely perceived as an overseas issue, but losing ground since it started to affect the United States. Now that its interest rates are close to zero the chances are that it may also lose some of its appeal based on rate differentials, although funding pressures are currently providing offsetting support. The U.S. is also broadly seen as being behind the curve in its tackling of the coronavirus issue, which may also limit the USD's upside scope especially while the news flow is so limited. Certainly until there is greater visibility about the timeline for this crisis the markets will be operating in a state of suspended animation with little overall confidence over which currency or asset to place faith in. In some ways it may be the currencies of countries that appear to be tackling the healthcare issue most aggressively that will be most rewarded, rather than those simply adopting conventional monetary policy and fiscal policy responses.

Global recession looms

However, what does seem likely is that with the world now looking at a global recession and subpar demand for an extended period (at least for the rest of H1), those currencies that are highly correlated to the global demand cycle like the AUD and GBP will remain on the defensive, at least until hopes of a recovery start to be seen. The same probably applies to EM FX as well, although distinctions may be seen based on relative interest rates and on how EM countries fare in terms of coronavirus contagion. GBP is also suffering on account of the more complex outlook for the UK's post-Brexit arrangements. To some UK-EU trades talks look likely to be more difficult and protracted given the greater focus and priority on healthcare issues. However, this may be a mistaken view as it may well turn out to be in both the UK and EU's interests to get a deal done quickly in view of the recession risks that they are both facing. Beyond these relatively broad thematic brush strokes, however, we have highlighted below the technical levels that investors should watch.

EM currencies remain under pressure



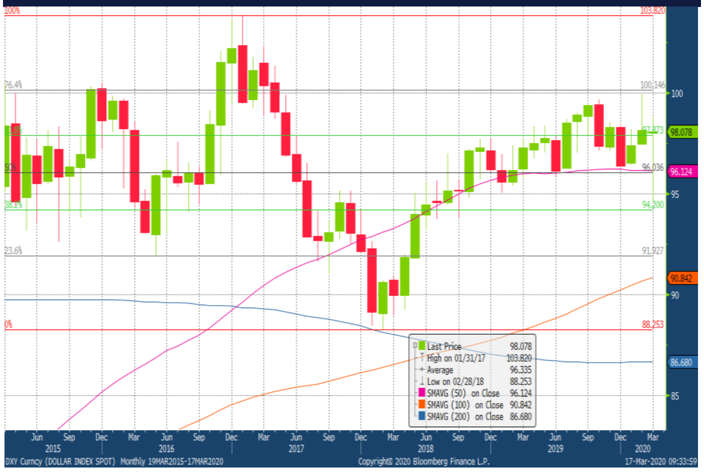
Source: Bloomberg. Data as of March 17,2020

Dollar Index between two key levels

Presently the Dollar Index (DXY) is trading at 98.062, above the significant 50-day, 100-day and 200-day moving averages (97.969, 97.792 and 97.826 respectively). In addition to this, the price remains above the 50-week moving average (97.753) and while the price closes the week above this level, upside risks will persist for the index. Over the last month, we saw the index fall to a fresh 2020 low of 94.650 on March 9, before recovering the climb back above the 23.6% one-year Fibonacci retracement as well as the 38.2% one-year Fibonacci retracement (96.659) and the 50% one-year Fibonacci retracement (97.280). In addition to overcoming these hurldles, the price is currently above the 61.8% one-year Fibonacci retracement. Analysis of the daily candle chart, shows that further advances have been restsisted at the 76.4% Fibonacci retracement (98.669). Should the price break above this level, we are likely to see further upside towards the psychologically significant 100.

Technically significant is the consistent monthly closes above the 50-month moving average (96.124) and the 5-year 50% Fibonacci retracement (96.036) both of which have provided support since February 2019. Should there be a monthly close below this level, it is likely to result in a retest of 94.200 a level that has provided support since June 2018 and 38.2% five-year Fibonacci retracement.

DXY remains supported above 96.05



Source: Bloomberg

JPY endures volatile month

Heightened risk aversion helped JPY strengthen against the dollar this last month, with USDJPY falling from highs of 112.23 to as low as 101.19 before recovering the the current levels of 106.65. The current reistance level appears to be the 200-day moving average (108.24) which will need to be broken in order for USDJPY to sustain additional gains. On the downside, a break and daily close below the 38.2% one-year Fibonacci retracement of 105.47 is likey to result in further losses and a retest of 104.

EURUSD remains above the 200-day MA

The 200-day moving average (1.1098) has continued to provide daily support to EURUSD. While the price remains above this level, a retest of 1.1221 (the 61.8% one-year Fibonacci retracement) seems the most likely short term outcome. On the other hand, a daily close below this key level is likely to result a decline towards 1.0950.

GBP vulnerable below 1.28

A 6% decline over the last 30 days has taken GBPUSD to 1.2253 in a move that saw the price break below the supportive 23.6% five year Fibonacci retracement of 1.2806. This level is now providing monthly resistance and while the price remains below this level as per monthly closes, there are significant downside rtisks to price breaking below 1.20. On the other hand, should the price break above this level, further resistance can be expected at the 50-month moving average (1.3095). Should this level be overcome, the price may see a larger climb towards the 1.34 level.

GBPUSD finds support at 100-day MA

Source: Bloomberg

AUD and NZD to remain soft

AUD and NZD have been among the biggest losers over the last month as their respective economies have been hit by declining tourism and commodity prices. Despite NZD receiving a temporary reprieve due to the government announcing a 4.0% GDP stimulus measure on March 17, the relief is likely to remain temporary and risks remain to the downside.

As we go to print NZDUSD is trading at 0.60410, levels not seen since June 2009, with the risk for further declines below the 0.60 level looking like the path of least resistance. Should the price realize a daily close below this level, it could trigger a larger decline towards 0.5820, not far from the 23.6% 15-year Fibonacci retracement of 0.5827.

Next door, the AUD is faring even worse and has softened even more than the NZD over the last month. Currently AUDNZD is trading at 1.0102, the lowest level seen since April 2015 with the risk of parity between the two currencies for the first time ever being a possibility in the short term.

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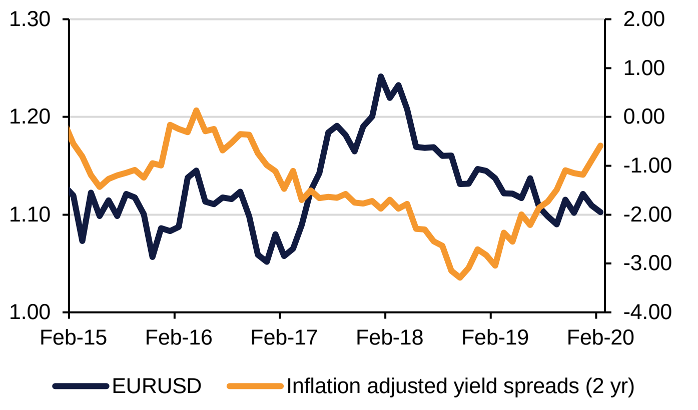
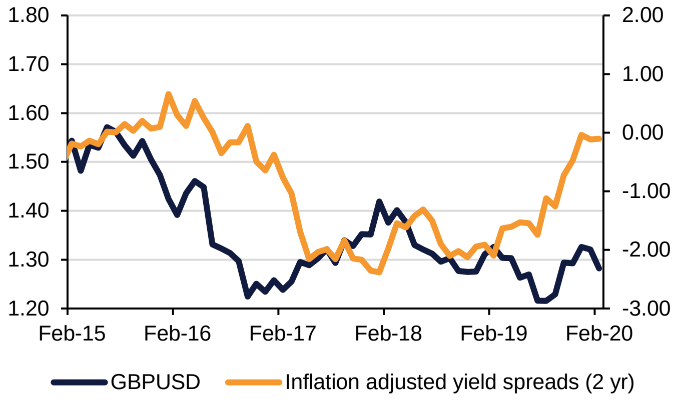
FX–Major Currency Pairs & Real Interest Rates

Interest Rate Differentials–EUR



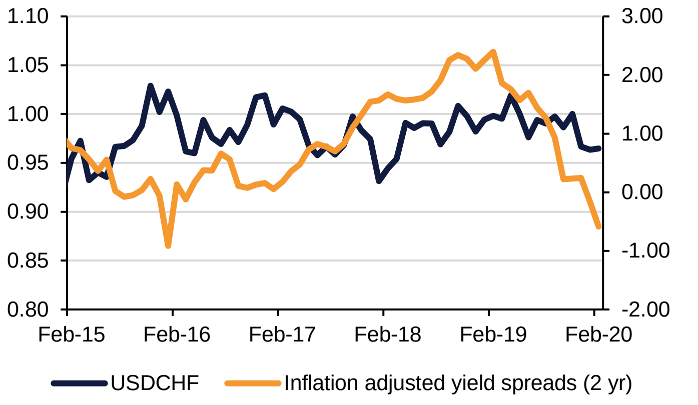
Source: Bloomberg, Emirates NBD Research

Interest Rate Differentials-GBP



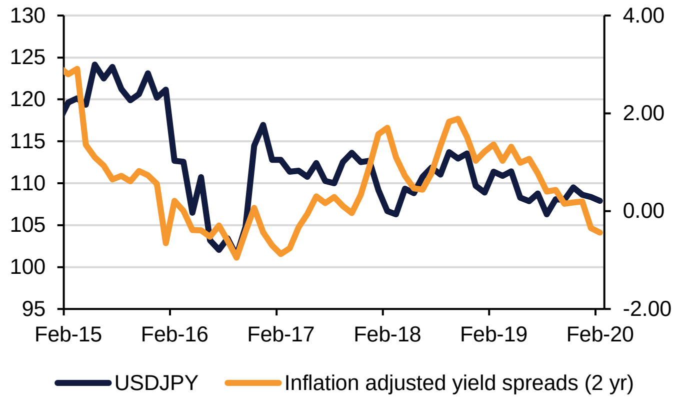
Source: Bloomberg, Emirates NBD Research

Interest Rate Differentials-CHF



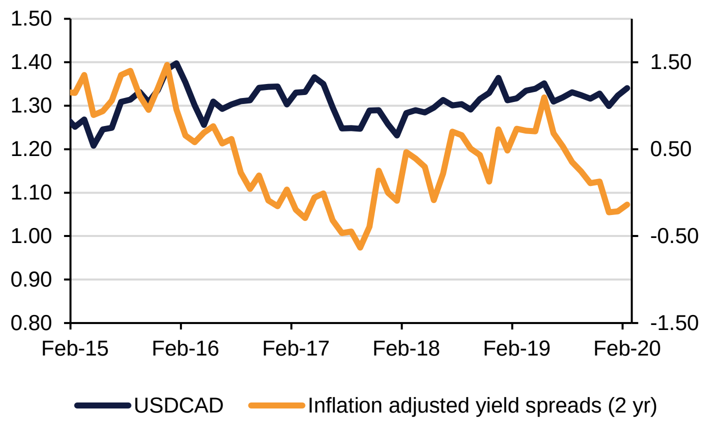
Source: Bloomberg, Emirates NBD Research

Interest Rate Differentials-JPY



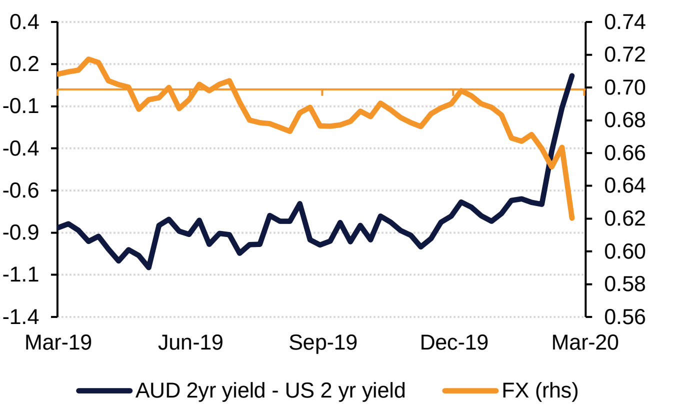
Source: Bloomberg, Emirates NBD Research

Interest Rate Differentials-CAD



Source: Bloomberg, Emirates NBD Research

Interest Rate Differentials-AUD



Source: Bloomberg, Emirates NBD Research

FX Forecasts

FX Forecasts - Major						Forwards		
	17-Mar	Q1 2020	Q2 2020	Q3 2020	Q4 2020	3m	6m	12m
EUR/USD	1.1170	1.1200	1.1400	1.1500	1.1700	1.1221	1.1252	1.1311
USD/JPY	106.37	108.00	108.00	107.00	107.00	105.90	105.60	105.07
USD/CHF	0.9486	0.9500	0.9400	0.9300	0.9300	0.9422	0.9388	0.9319
GBP/USD	1.2240	1.2600	1.3000	1.3400	1.3800	1.2272	1.2274	1.2276
AUD/USD	0.6092	0.6200	0.6250	0.6400	0.6900	0.6090	0.6086	0.6077
NZD/USD	0.6033	0.6000	0.6000	0.6500	0.6700	0.6026	0.6018	0.6003
USD/CAD	1.3990	1.3900	1.4000	1.3600	1.3500	1.3980	1.3975	1.3963
EUR/GBP	0.9125	0.8889	0.8769	0.8582	0.8478	0.9144	0.9168	0.9214
EUR/JPY	118.81	120.96	123.12	123.05	125.19	118.81	118.81	118.81
EUR/CHF	1.0596	1.0640	1.0716	1.0695	1.0881	1.0572	1.0562	1.0541
FX Forecasts - Emerging						**Forwards**		
	17-Mar	Q1 2020	Q2 2020	Q3 2020	Q4 2020	3m	6m	12m
USD/SAR*	3.7567	3.7500	3.7500	3.7500	3.7500	3.7533	3.7550	3.7663
USD/AED*	3.6730	3.6730	3.6730	3.6730	3.6730	3.6749	3.6772	3.6832
USD/KWD	0.3086	0.3020	0.3020	0.3020	0.3020	0.3101	0.3112	--
USD/OMR*	0.3849	0.3850	0.3850	0.3850	0.3850	0.3911	0.3959	0.4039
USD/BHD*	0.3776	0.3770	0.3770	0.3770	0.3770	0.3781	0.3785	0.3793
USD/QAR*	3.6650	3.6400	3.6400	3.6400	3.6400	3.6678	3.6690	3.6750
USD/EGP	15.7494	15.7500	15.7500	15.5000	15.5000	16.8750	17.5750	18.5750
USD/INR	74.015	75.000	75.000	72.000	70.000	75.4800	76.2400	77.7400
USD/CNY	6.9967	7.1000	7.2000	7.2000	7.2000	7.0255	7.0485	7.0993
USD/SGD	1.4219	1.4000	1.3600	1.3250	1.3000	1.4210	1.4201	1.4203

FX Forecasts - MENA					
	17-Mar	Q1 2020	Q2 2020	Q3 2020	Q4 2020
USD/MAD	9.6830	9.6500	9.5000	9.4000	9.4000
USD/TND	2.8337	2.8000	2.8000	2.7000	2.7000
USD/TRY	6.0167	6.0000	6.2000	6.2000	6.3000

Data as of 17 March 2020
Source: Bloomberg, Emirates NBD Research

Equities/Fixed Income

Over the last month, financial markets entered unchartered territory as a classic 'Black Swan' event emerged. Relative to a standstill in global economic activities, gyrations in financial markets have been intense. The primary driver has been the 'fear of unknown' as no market participant is in a position to model the breadth and severity of the viral outbreak which effectively makes any exercise of assessing its impact on economic growth and corporate profits rather redundant.

Since the start of this month, global equity markets have lost c. USD 11tn in market capitalization, the Bloomberg Barclays Global Aggregate index has returned -1.2% and the Bloomberg Commodity index has dropped -11.2%. Unsurprisingly, volatility has jumped across assets with the VIX index (equities) and MOVE index (bonds) jumping +504% 1m and 100% 1m respectively.

State of play

With tangible evidence of the probable impact of Covid-19 on economic growth just beginning to emerge, we will try to assess the current state of play and its implications.

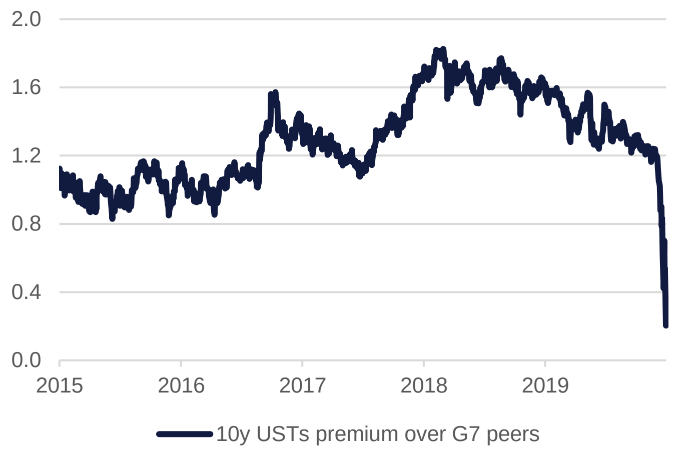
Are policy responses appropriate?

Monetary

The immediate response of most central banks across the world has been to rely on the traditional interest rate mechanism to provide support to the economy and more importantly to ensure system stability. The Federal Reserve has cut interest rates by 150 bps to bring the lower bound of rate to 0%. Additionally, the central bank also announced a quantitative easing program of USD 700bn. The Bank of England and the Bank of Canada followed the Federal Reserve in cutting their benchmark rates by 50 bps and 100 bps respectively. The European Central Bank and the Bank of Japan resorted to more targeted and unconventional measures instead of cutting rates. Or perhaps their hands were rather tied considering that benchmark rates were already deep into negative territory. Emerging market central banks have also followed their developed market counterparts but on balance have been more restrained. The plausible reason for that could be the desire to hold onto as much foreign inflows as possible and also importantly to minimize pressure on their currencies.

While central bank actions were coordinated at one end of the spectrum, the substance widely varied. It is no surprise then to see the premium of 10y treasury yields over its G7 peers drop from as high as 183 bps in 2018 to 25 bps currently. Unsurprisingly, the premium between 10y treasuries and emerging market USD bonds has widened to its highest in over 5 years.

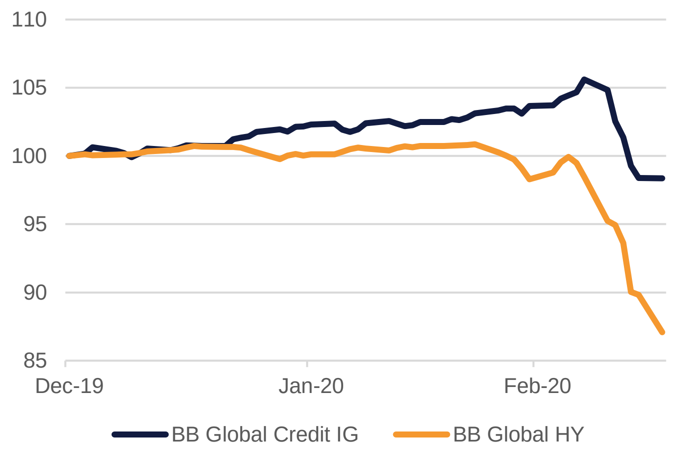
Premium of USTs over G7 peers drop sharply (10y)



Source: Bloomberg

The impact of central bank moves on broader credit markets has been mixed as the flight to safety and hunt for yield impulse took center stage simultaneously. However, unprecedented volatility and dislocation in financial markets ultimately forced investors to liquidate whatever they could to raise liquidity.

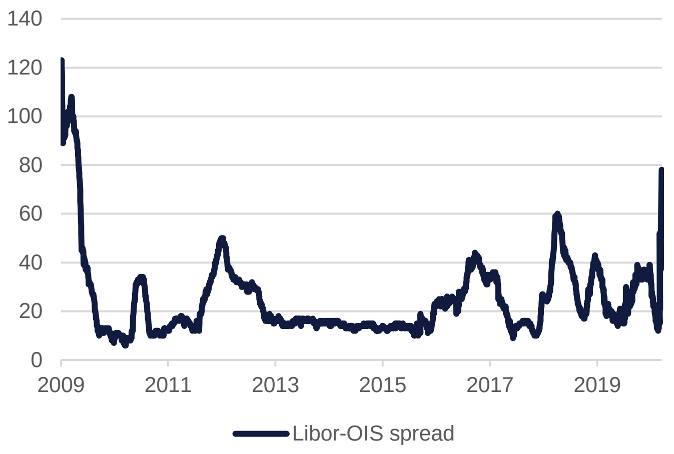
Both investment grade and high yield credit has suffered losses



Source: Bloomberg

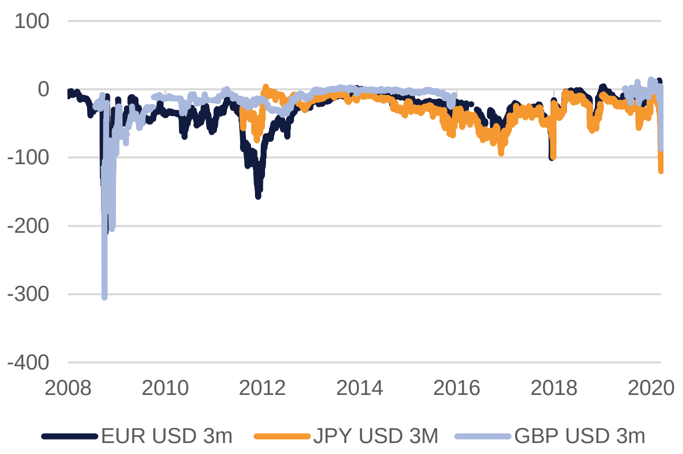
Despite central banks across economies pumping liquidity in the system and providing swap lines, signs of stress remain in some segments of the broader market. The widening bid-ask spread even in treasuries, Libor-OIS spread and cross currency swaps all suggest an immediate contagion of credit stress and funding squeeze.

LIBOR-OIS spread widens



Source: Bloomberg

Cross currency swaps blow out



Source: Bloomberg

Beyond the immediate term, investors need to be slightly wary of lack of obvious firepower in the global central bank's arsenal following their moves in the last fortnight. For example, during the 2008 financial crisis, the Federal Reserve had to cut rates by as much as 525 bps before reaching 0% compared to merely 150 bps in the current instance. The same also supports our long-held argument of the limited efficacy of monetary policy in the current economic environment and a dire need for a comprehensive fiscal stimulus across economies.

Fiscal

Governments across economies have allowed their central banks to do the heavy lifting. While there have been statements promising to do whatever it takes, the actual spending plans have fallen well short of what is required Most of the fiscal measures are aimed at easing cash flow problems for companies, generous medical leaves or enhanced insurance support. Some economies like Hong Kong also promised cash handouts.

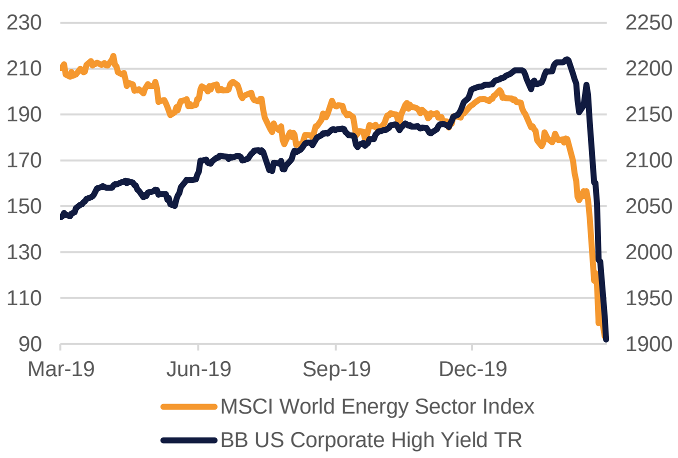
However, it can be safely said that measures announced so far, with exceptions, indicate more a bridge effort to tide over current issues and are not aimed at creating sustained demand over the medium term. It must be recalled that even before the current crisis, there were calls for a large fiscal stimulus program. China so far has been an exception with some provincial governments pledging to spend as much as USD 500bn this year on infrastructure projects and perhaps that in part explains the outperformance of Chinese equities relative to broader markets. The Shanghai Composite index has dropped -8.9% ytd compared to a loss of -25.3% ytd in the MSCI EM index and -27.5% in the MSCI World index.

Where are equities?

The recent move in equity markets has caught the attention of investors because of the unrelenting speed and depth of the decline. In our view, it is simply a case of equities finally catching up with other financial assets which have been showing signs of stress since before the outbreak of coronavirus. The earlier dislocation between equities and other asset classes could be put down to complacency and inherent confidence of investors in the central bank 'put'. While the central bank put did arrive, it came under the shadow of uncertainty with no expiry date.

Nearly three-fourth of year to date decline in the MSCI World has come in the last two weeks. This stands out when compared to treasuries which have seen 45% of its year to date move in the last two weeks. Risk-on currencies and the copper/gold ratio also exhibit moves similar to USTs.

Energy sector under pressure



Source: Bloomberg

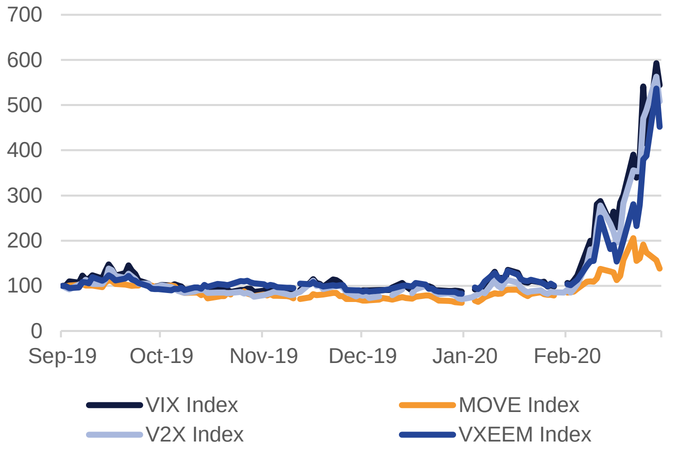
Another plausible reason for the sharp acceleration in equity decline could be the unravelling of the OPEC+ deal on production cuts. The development caused sharp a decline in oil prices which in turn weighed heavily on energy stocks especially at a time when oil demand has dropped substantially due to several restrictions imposed by governments across the world to stem the spread of the virus. Both energy stocks and bonds (located mainly in US high yield space) have collapsed in absolute and relative terms.

What do other indicators show?

Volatility

Volatility in both equities and fixed income is at extreme levels. In fact in equities (VIX index), volatility surpassed the levels seen in 2008 on the same day as the Federal Reserve cut interest rates by 100 bps. There is a general tendency to consider peak volatility as a turning point or a sign of a trough in global equities. However, it is worth highlighting here that the quickest the S&P 500 index has rebounded from a 30% drop has been 2 years in 1987.

Volatility at record levels



Source: Bloomberg

Positioning

Unsurprisingly, funds have flown out of equities and fixed income market. It is likely that value-at-risk shock is precipitating those outflows as forced selling kicks in. However, in our view, the outflow has not yet reached peak levels. For example, outflow from institutional emerging market debt funds so far this year stands at USD 3.5bn which is still lower than inflows of USD 5.2bn inflows in 2019.

For equities, while the outflow has been sharper and quicker, it still has seen pockets of inflows. According to data from EPFR, the second week of March, which saw capitulation in equity markets, saw outflows of USD 4.5bn. However, even during that week flows into US and Japan equity funds wer at five and eight week highs respectively.

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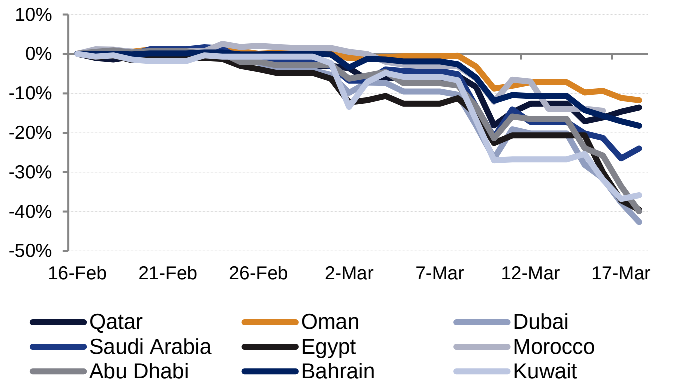
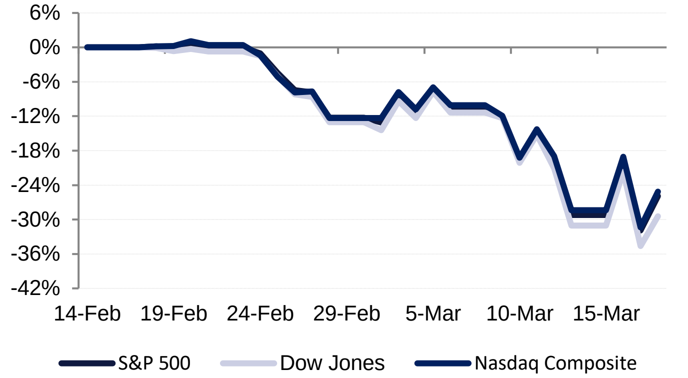
Major Equity Markets

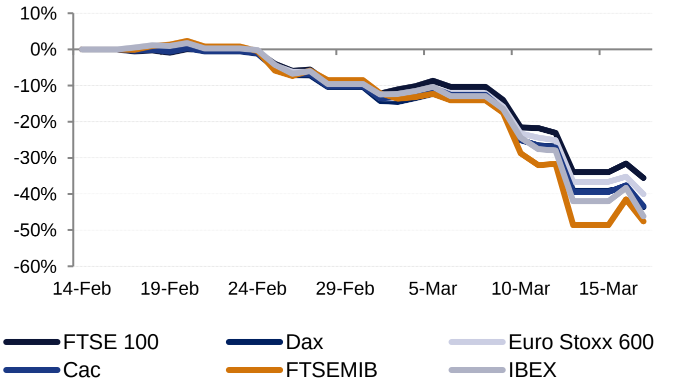
MENA Equity Markets



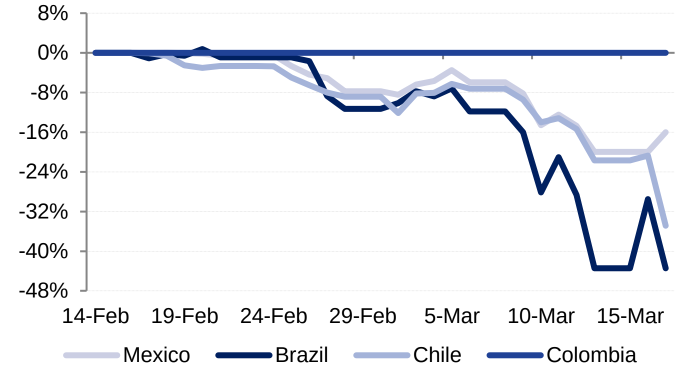
US Equity Markets



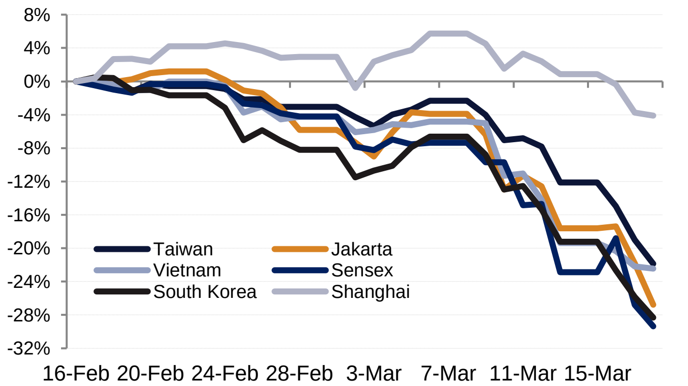
European Equity Markets



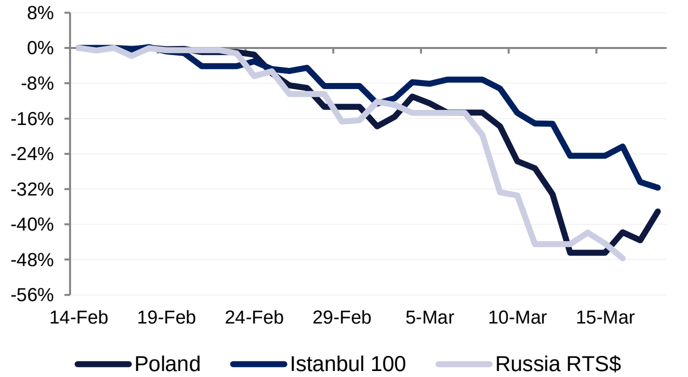
Latin American Equity Markets



Asian Emerging Equity Markets



Emerging Europe Equity Markets



Source: Bloomberg, Emirates NBD Research

Interest Rate Forecasts

US Treasuries Forecasts				
	Current	Q2 2020	Q3 2020	Q4 2020
2y	0.49	0.45 – 0.60	0.55 – 0.70	0.80 – 0.95
10y	1.07	0.90 – 1.05	1.00 – 1.15	1.05 – 1.20
3M Libor				
3m	1.05	0.80	0.85	0.90
3M Eibor				
3m	1.11	1.00	1.05	1.10
Policy Rate Forecasts				
	Current %	Q2 2020	Q3 2020	Q4 2020
FED (Upper Band)	0.25	0.25	0.25	0.25
ECB (deposit rate)	-0.50	-0.50	-0.50	-0.50
BoE	0.25	0.25	0.25	0.25
BoJ	-0.10	-0.10	-0.10	-0.10
SNB	-0.75	-0.75	-0.75	-0.75
RBA	0.50	0.25	0.25	0.25
RBI (repo)	5.15	4.90	4.90	4.90
SAMA (reverse repo)	0.50	0.50	0.50	0.50
UAE (Repo rate)	0.75	0.75	0.75	0.75
CBK (o/n repo rate)	1.00	1.00	1.00	1.00
CBB (o/n depo)	0.75	0.75	0.75	0.75
CBO (o/n repo)	1.225	1.225	1.225	1.225
CBE (o/n depo)	9.25	9.25	9.25	9.25

Source: Bloomberg, Emirates NBD Research
As of 17 March 2020

Commodities

As economic activity globally shudders to a halt as a result of the Covid-19 pandemic oil prices have collapsed. Demand has evaporated in major economies and will record a large annual decline for 2020 as a whole, the first full year decline in oil demand since the Global Financial Crisis but likely at a scale that market participants will struggle to digest. At the same time, OPEC has unleashed a price war on its rivals, with Russia and the US squarely in its targets. Faced with the twin shocks of demand destruction and overwhelming supply, prices have capitulated and may be at risk of much more downside volatility.

GCC output will flood onto markets in Q2

Following a failure to agree on extending production cuts at its scheduled March meeting, OPEC and Russia have now positioned for a costly price war with the aim of capturing as much market share as possible. Saudi Arabia slashed its official selling prices and will increase production to 12.3m b/d from April, the UAE will supply markets with 4m b/d and other OPEC producers will follow with production increases of their own. Russia's oil companies will be looking collectively to raise output by around 500k b/d from April and sustain production at elevated levels. Beyond raising current production levels, both Aramco and ADNOC have announced plans to fast-track investment into capacity increases: Saudi Arabia will aim for 13m b/d and ADNOC will expedite already in place investments to hit 5m b/d. The messaging from regional NOCs—with Aramco's senior managers saying they were happy with oil prices around USD 30/b—suggests the market share strategy isn't going away any time soon.

To accommodate this surge in OPEC and Russian output, producers in the US and Canada have announced major cuts to capital expenditure, as much as 60% lower. IOCs have also announced plans to slash capex this year amid the volatility in oil prices while a de-anchoring of long-run price expectations—the entire Brent curve is sub-USD 50/b out until the mid-2025—threatens long-term supply stability outside of OPEC producers.

Long run prices threaten investment plans

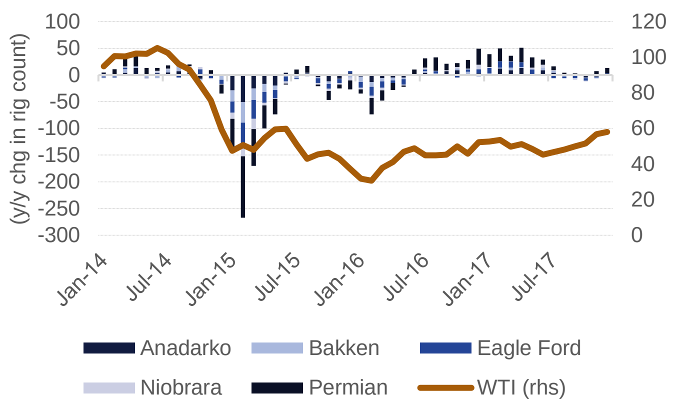
Source: Bloomberg, Emirates NBD Research.

How to measure the success of a price war

As far as reordering market share, the price war strategy can achieve short-term success. OPEC last used a market-share/price war strategy from late 2014 until the end of 2016 and production from shale basins in the US fell by almost 300k b/d from Nov 2015 to a trough in Feb 2017. During that period OPEC increased their share of the market from 38.8% in Q4 2014 to 41.6% in Q4 2016. Cuts to capex that we've seen announced in the US suggests another decline will be on the cards for US producers and we could see output from shale basins peak over the next few months before declining sharply into 2021.

The cost of the market-share strategy is, however, painful relative to the modest increase in how much more of the market OPEC will occupy. In 2015-16 oil prices collapsed, falling to USD 51/b for Brent on average in Q4 2016 from USD 77/b in Q4 2014. The enormous decline in prices in the last few weeks—prices are 40% lower than they were a month ago—may just be a sign of things to come over the coming months and quarters. Fiscal and external positions in the GCC will deteriorate along with non-oil sectors of the economy dependent on government financing.

It worked last time…

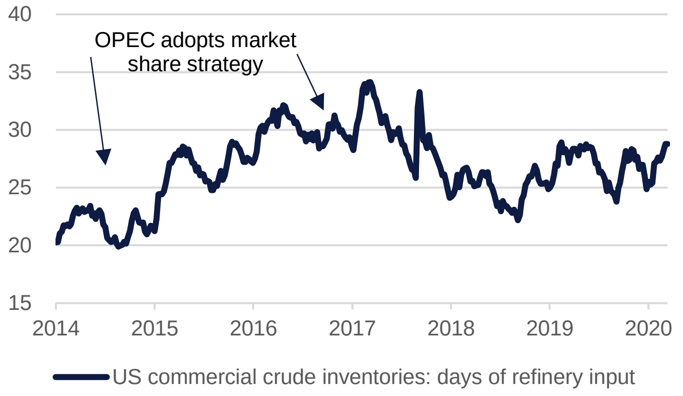


Source: Bloomberg, Emirates NBD Research.

This flood of crude from OPEC comes amid the worst demand conditions in recent market history. Travel restrictions and economic lockdowns have obliterated demand growth and we haven't even seen the full impact of the Covid-19 pandemic on the US economy. The IEA's baseline is for oil demand to decline by 90k b/d this year with a downside risk scenario of a decline of closer to 700k b/d. But even that risk scenario looks far too sanguine in current market conditions.

Faced with the twin shocks of demand collapsing and supply surging, inventories will blow out. Our baseline expectation, using the IEA's recent demand projections, sees OECD stocks ending 2020 530m bbl higher than end 2019. However, that is likely to be far too conservative and an increase in inventories of as much as 750m-1bn bbl is in the realm of possibility. In 2015-16 demand recorded a noticeable bump in response to low prices caused by OPEC production increases but it still took a considerable time for oil inventories to normalize. In the US, commercial stocks of crude oil measured against days of refinery input didn't return to pre-OPEC market share strategy levels until Q3 2018. Demand currently is in the process of extensive destruction and when it recovers it won't be 'making up' for the lost ground of H1 2020. Burdensome inventories will persist well into 2021 even if there is a sizeable negative supply response from producers in North America.

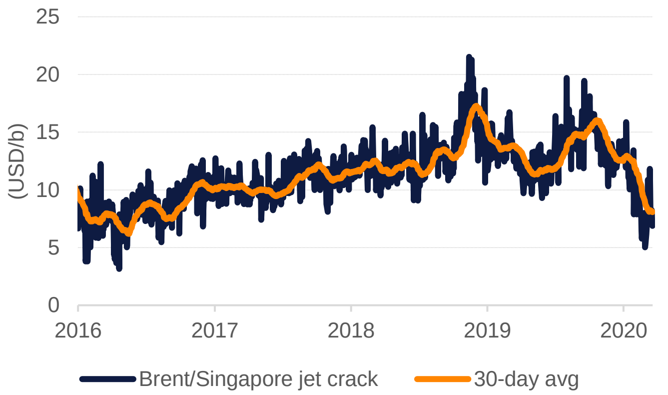
…but maybe a little too well



Source: EIA, Bloomberg, Emirates NBD Research.

Moreover, with demand already so negatively impacted by Covid-19 the flood of crude will overwhelm refineries already facing weak margins for products. Product stocks in Singapore were already on the rise ahead of the OPEC strategy shift, depressing cracks for middle distillates like jet fuel in particular. Importers reliant on crude from OPEC members already had to endure a highly volatile 2019 as geopolitical risks added upside volatility to prices. The market-share strategy—while theoretically positive for refiners as crude prices sink—will reinforce a sense among importers that OPEC oil production strategies are too heavily influenced by non-economic factors that are essentially impossible to hedge appropriately.

An unwelcome gift to refiners



Source: Bloomberg, Emirates NBD Research. Note: USD/troy oz.

Prices may test levels otherwise unthinkable

Following the breakdown of OPEC we lowered our price expectations for the year to averages of USD 45/b for Brent and USD 41/b in WTI. However, with few barriers in the way of prices testing lower at the moment we expect to see significant downside volatility. Prices may push to levels that are difficult to fathom given the price war strategy originated in producers with fiscal/socio-economic break-evens almost 200% higher than current Brent levels..

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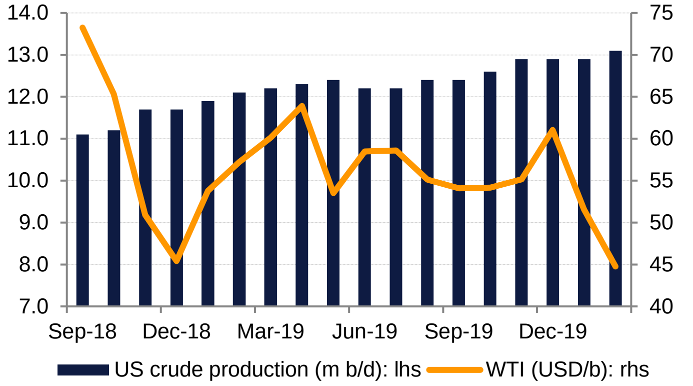
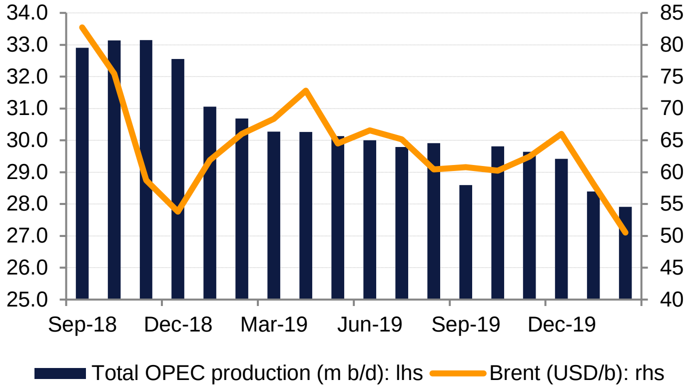
Major Commodities Markets

US oil production and price



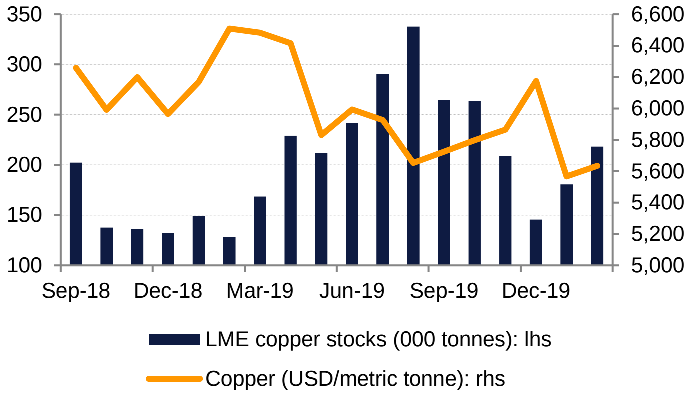
Source: Bloomberg, Emirates NBD Research

International oil production and price



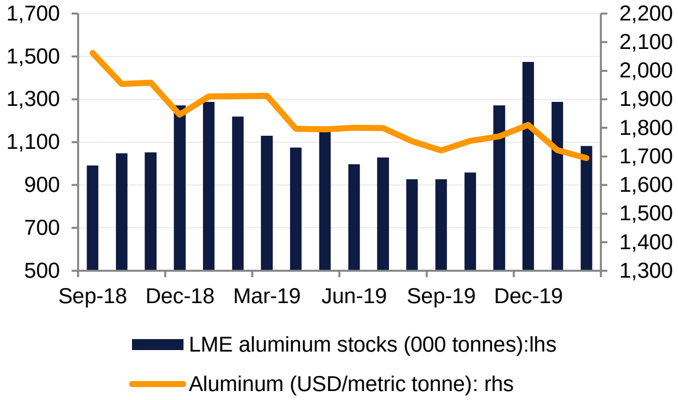
Source: Bloomberg, Emirates NBD Research

Copper stocks and price



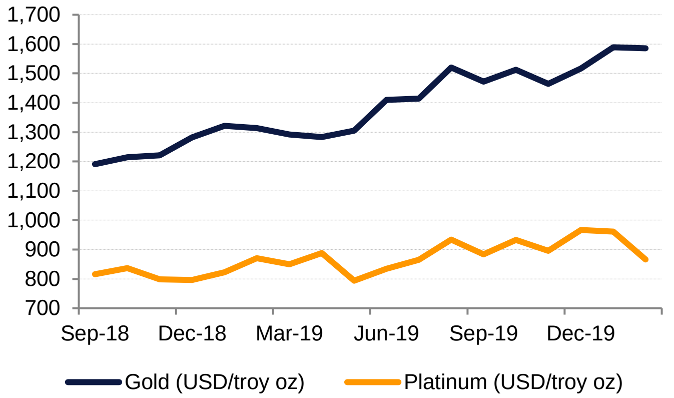
Source: Bloomberg, Emirates NBD Research

Aluminum stocks and price



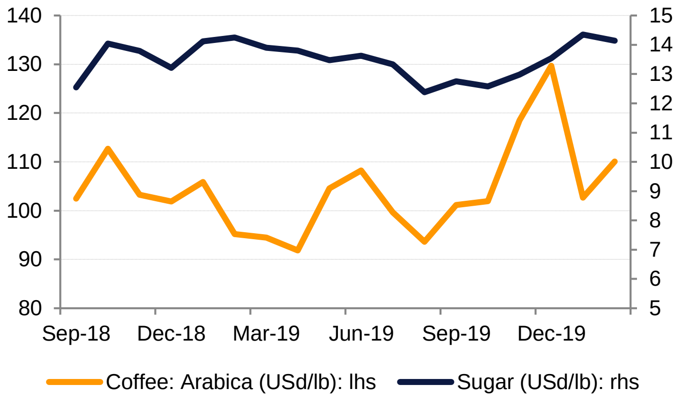
Source: Bloomberg, Emirates NBD Research

Precious metals prices



Source: Bloomberg, Emirates NBD Research

Agriculture prices



Source: Bloomberg, Emirates NBD Research

Commodity Forecasts

Global commodity prices							
	Last	2020Q1	Q2	Q3	Q4	2019	2020
Energy							
WTI	27.13	55.00	32.50	35.00	40.00	57.03	40.63
Brent	29.16	58.00	35.00	38.00	48.00	64.19	44.75
Precious metals							
Gold	1,530.22	1,550.00	1,500.00	1,450.00	1,450.00	1,392.40	1,487.50
Silver	12.85	17.00	13.50	14.00	15.00	16.20	14.88
Platinum	679.39	1,000.00	700.00	800.00	900.00	864.97	850.00
Palladium	1,665.40	2,250.00	1,700.00	1,850.00	1,900.00	1,539.86	1,925.00
Base metals							
Aluminum	1,651.50	1,800.00	1,750.00	1,800.00	1,820.00	1,813.14	1,792.50
Copper	5,144.00	6,000.00	5,800.00	5,750.00	5,750.00	6,023.08	5,825.00
Lead	1,619.00	2,072.31	2,011.52	1,996.26	1,996.26	2,004.91	2,019.09
Nickel	11,780.00	13,500.00	14,000.00	15,000.00	15,000.00	13,938.00	14,375.00
Tin	14,250.00	16,000.00	16,500.00	17,750.00	17,900.00	18,612.26	17,037.50
Zinc	1,871.00	2,389.58	2,323.46	2,306.84	2,306.84	2,509.85	2,331.68
Iron ore	90.05	90.00	85.00	75.00	70.00	93.32	80.00

Prices as of 18 Mar 2020. Note: prices are average of time period unless indicated otherwise.
Source: EIKON, Emirates NBD Research

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