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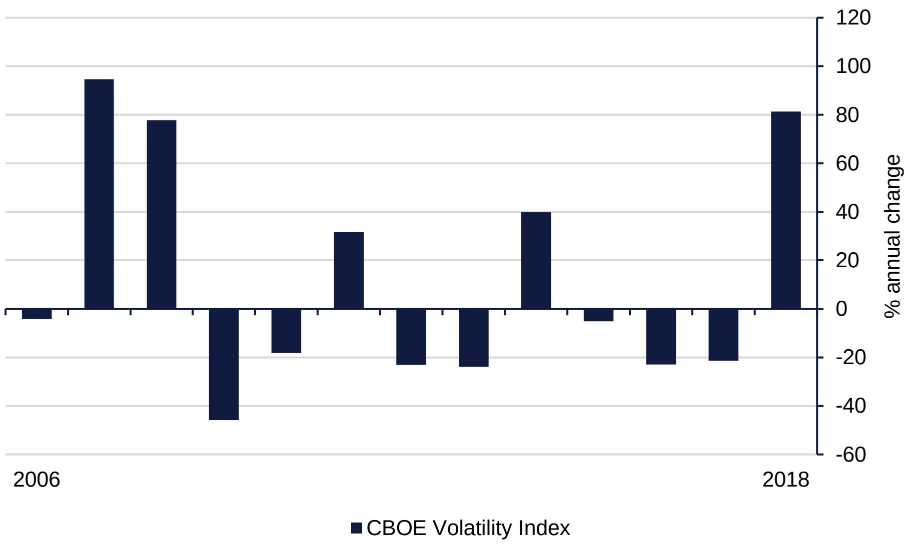
Monthly Insights

As the year end comes into view the outlook for 2019 is becoming increasingly hazy and volatility is rising. Trade tensions, monetary policy normalization and geopolitical risks are all themes that will carry over from 2018 into next year, and perhaps intensify, adding to questions about whether current growth rates can be sustained and whether financial markets can continue to hold up.

The next Monthly Insights will be released in January 2019.

- **Global macro:** We recently visited the US where we met with a number of market participants and a surprising degree of unanimity about the outlook for the US economy.
- **GCC macro:** As we head into the final stretch of the year, the downside risks to growth in the GCC appear to be increasing.
- **MENA macro:** Although the US announced just prior to the reimposition of stringent sanctions on Iran on November 5 that it would in fact grant waivers on imports of Iranian crude to eight countries, we see this more as a stay of execution for the Iranian economy rather than any significant lifeline.
- **Interest Rates:** The UST yield curve continued to move higher though sovereign yields in other developed economies softened in anticipation of slower global growth ahead.
- **Credit Markets:** Credit spreads on GCC bonds increased in response to falling oil prices and rising geopolitical risks in the region.
- **Currencies:** Approaching the midpoint of the final quarter of 2018, the dollar has continued to appreciate, reaching an 18-month high.
- **Equities:** Global equities remained weak as investors began to position themselves for greater political and monetary policy unpredictability and uneven economic growth heading into 2019.
- **Commodities:** Middle East oil exporters face a challenging year in 2019 as weaker demand projections, moderating supply risks and fuel quality regulations bite into the market.

Volatility turning sharply higher heading into 2019



Source: Bloomberg, Emirates NBD Research.

Content

Global Macro

We recently visited the US where we met with a number of market participants and a surprising degree of unanimity about the outlook for the US economy. Below we summarize our main findings about the key issues facing the US and the rest of the world in 2019.

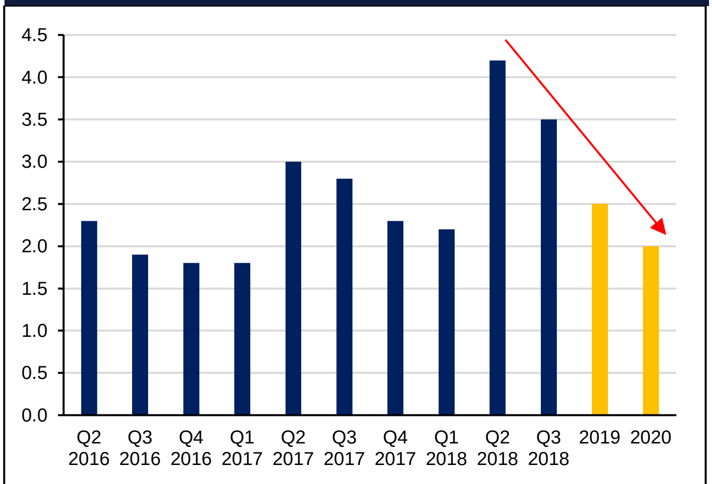
US growth to slow to trend in 2019-2020

The overall impression we took away a was a fairly positive one whereby the US economy was expected to continue growing next year and in 2020, albeit at a slower pace than in 2018, but with little to no risk of a recession over that period, and with interest rate risks skewed to the upside of the Fed's forecasts of three hikes in 2019.

This was a little surprising, as much of the conjecture regionally and internationally appears to be anticipating when a recession will occur given the longevity of this economic cycle, and there was only one opinion on our trip that warned that this could indeed happen in 2020.

However, for the most part US growth was anticipated by most participants to be closer to the trend growth rate of 1.5-2.0%, but with the employment rate at risk of falling further towards 3.0% (from 3.7% currently) the chances are rising of inflation moving up slowly and steadily forcing the Fed to continue tightening. The US fiscal stimulus has been huge, worth approximately USD1.5 trillion over 10 years, and the peak impact is likely to be felt in H1 2019.

U.S. growth to slow to trend in 2019-2020



Source: Bloomberg, Emirates NBD Research

Market may be too dovish on rates

There was broad unanimity of the view that that the Fed will accordingly tighten 3-4 times in 2019, after raising once more this year in December, and with the possibility of a further hike(s) in 2020. Our own forecast has been that interest rates will be raised only twice in 2019, as we see the impact of higher rates starting to be felt in H2 2019 and we expect the economy to be feeling the cumulative pain from evolving trade tensions. This view appears to be held by the markets too which are still not pricing in the full three rate hikes implied by the Fed's dot plot in 2019. However, there are now much clearer upside risks to this view with the lagged effects of fiscal stimulus still being felt deep into 2019, albeit being partially offset by gradual monetary tightening and the impact of trade tensions.

In terms of the impact of recent Trump criticism of the Fed, this was thought likely to be minimal overall, although there was an observation that it might actually produce the opposite result to the one intended by causing the Fed to bring forward its hikes in 2019, ahead of the election in 2020. In any case it was highlighted in a number of meetings that the Fed Chair cannot be fired by the President and that Chairman Powell would likely be oblivious to Trump criticism, as would most of the FOMC.

There were a number of interesting observations about useful gauges of recession risks to monitor. Some of these were about the how the Fed reacts to equities and the yield curve, while others were more about economic data. The view about equities was that a bear market amounting to a 20% correction would have to be sustained over at least 3 months for it to meaningfully impact Fed decision-making. As far as the yield curve is concerned it was felt that only a vocal minority at the Fed is bothered by a flattening in the yield curve, as its shape reflects so many different variables, while most members are more relaxed about its' shape. In fact more important than the yield curve itself was thought to be the New York Fed survey of market participants in terms of what it says about expectations about the economy and Fed policy, and to some extent the economic data itself, in particular the non-farm payrolls data, which over time give a more reliable lead on recession risks.

End of balance sheet normalization

It was thought likely that the Fed will signal an early end to balance sheet normalization next year, with the Fed likely to announce this at its March 2019 meeting, gradually lowering the reinvestment caps over the 6 months ending in September 2019. This fits with the picture of a Fed looking to tighten monetary fairly quickly, and reinforces the positive sentiment towards the dollar.

The impact of this on bond yields was viewed differently by various institutions. **For the most part the sense was that 10-year bond yields would be steady at around 3.0-3.30%,** which should result in the USD staying strong even as the yield curve flattens a little. However, there were some institutions that saw yields moving higher still as a result of increased supply of treasury bills and bonds, as the US government is expected to run the largest budget deficit of the major advanced economies at around 6.0% of GDP, and as foreign central bank demand for USTs diminishes.

Other than above factors, the main observation was that 2019 will have a very busy risk calendar. Trade wars, Iran sanctions, Brexit and 'Quitaly' were all mentioned as key issues, along with the end of ECB QE, North Korea's continued weapons program, the Mueller investigation, Turkey and other EM risks. The impact of the US mid-terms that were held last week will also be important on the prospective legislative agenda, as well as on the political volatility that might be expected to be experienced both within the US and internationally.

Trade wars to remain an issue in some form

On trade, it was pointed out that this is an issue that President Trump has firm beliefs about: namely that trade deficits are bad and trade surpluses are good. As such, the situation is likely to get worse before it gets better, and it could be the second half of 2019 before trade tensions come to an end. However, most analysts expected a deal to be reached earlier next year. Even then, tensions will not go away completely due to the different world views that the US and China have.

In terms of US-China there will be repeated rounds of testing each other's resolve, until continued pain forces an eventual compromise. The US tariff rate on USD200bn of Chinese goods will likely rise from 10% to 25% on the 1st of January and the back and forth will continue until weakening economies cause weak markets and a public pushback. China will retaliate and the US has promised tariffs on all remaining Chinese products. The possibility was also mentioned of Trump imposing quotas on Chinese imports if tariffs alone do not reduce the trade deficit. Only when both sides are out of ammunition will the basis for a negotiation be found.

In this context the USD will not be challenged as a reserve currency as reserve status results from a 'disorganized collective choice' and to change it would require a degree of coordination that is unlikely to be achieved in the coming years at least.

The inflationary impact of trade wars were thought likely to be limited as the strong dollar will help to offset it in the US. Also the fiscal stimulus will cushion any growth and confidence shocks. Agreements with South Korea, the EU, Japan, Mexico/ Canada are a template as to how things will develop, and will not be settled until China agrees to buy a lot of US imports.

If all tariffs are imposed the impact will be to knock 0.5% off Chinese growth, taking it below 6.0% while the US could see 0.7% off its growth. The knock-on effect will be felt on China's supply chain, and the EU will be the next tension point with the US, although Merkel's exit could however make the US/EU relationship easier. To some it was felt that the US's trade spat with everyone else could lead to more liberal trade policies in the rest of the world, including between the EU and China.

US political risk to remain elevated

The split Congress will result in gridlock until the 2020 Presidential election. Although there will be some areas where the Republicans and Democrats can find compromises (infrastructure, drug prices), overall there will be limited policy action, and Trump may see some value in forcing a government shutdown relatively quickly to demonstrate the dysfunctionality of Congress. It all suggests that the fiscal stimulus will fade and with it growth, but that the Fed will continue to tighten gradually.

The speed with which Trump changed his Attorney General suggests that he is gearing up for the findings of the Mueller probe, and there were hints that some big indictments could be around the corner. Democrats may ultimately have to choose between promoting legislation and doing deals on the one hand, and supporting investigations into Trump on the other, with the Presidential election in two years' time already in many people's minds.

Some global risks and themes

- Italy was portrayed as an accident waiting to happen, with fiscal policy becoming unsustainable and structural reforms being reversed. All in all it could end up with a sovereign debt default and with Italy crashing out of the EU in a crisis that was described as 'Quitaly'.

- When it comes to Brexit it is harder to conceive of a no-deal Brexit, than to expect a deal that does not command a Commons majority. Even after divorce deal and a 3 year transition there was a view expressed that the UK could seek to re-enter the EU in a number of years' time, a view we find a little far-fetched. More likely it seems that the UK is heading towards a deal that commands no majority in Parliament, a situation that may end up with another referendum.

- The ECB was broadly believed to be running out of bullets and will not hike until September 2019, with the risk skewed towards a delay, especially if the Italy debt problems become worse which seems likely.

- China will adopt an aggressive easing to offset the slowdown affected by trade wars. It is widely recognized that China requires growth of at least 6% in order to keep unemployment from rising, even with an aging population and declining workforce. This highlights the inefficient allocation of resources/ savings in that economy.

- Finally, Japan has the best chance in 20 years to get out of deflation. The BOJ will be steady on monetary policy all the way to 2020, while concerns about debt seem premature, with most analysts of the view that the upcoming consumption tax increase next year was inappropriate and would weigh on growth.

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GCC Macro: Downside risks abound

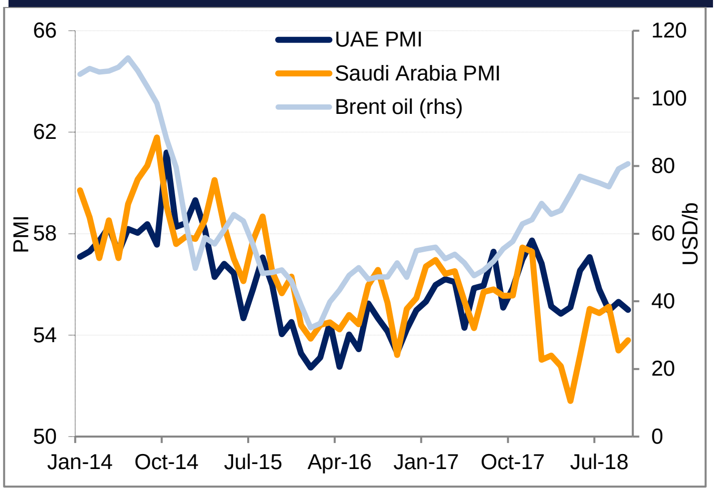
As we head into the final stretch of the year, the downside risks to growth in the GCC appear to be increasing. Recent PMI data show that non-oil sector activity slowed at the start of Q4 2019, with higher oil prices seemingly failing to translate into faster economic growth.

The return of the bear market in oil over the last few weeks, and the recent announcement by Saudi Arabia that it would cut oil exports by 500k b/d next month, now raises the possibility that the increase in oil output that we had expected to underpin GDP growth in 2019, fails to materialize.

A soft start to Q4 for the non-oil sectors

While the headline PMI for the UAE remained in the mid-50s, the October reading was the lowest since December 2016. Dubai's Economy Tracker Index fell to 52.5 in October, the lowest reading since March 2016. The Saudi PMI rose slightly to 53.8 in October, but remains low by historical standards. Although by themselves the PMI readings look fine in absolute terms – all indicate an expansion in the non-oil sectors – in the context of the rally in oil prices since over the last 18 months, they appear rather lackluster.

PMIs and oil price



Source: IHS Markit, Bloomberg, Emirates NBD Research

Indeed, the chart above shows that the doubling in oil prices since their Q1 2026 low has had very little pass-through to non-oil sector growth. To some extent this has been due to relatively tight fiscal policy in the GCC in 2016-17, as governments in the region cut spending and introduced taxes in order to reduce budget deficits. However, with the region's largest economy boosting government spending by nearly 25% in Q1-Q3 2018, and other countries also relaxing their fiscal stance somewhat, we had expected a recovery in non-oil sector growth to become evident in H2 2018. This does not appear to be the case, based on the survey data.

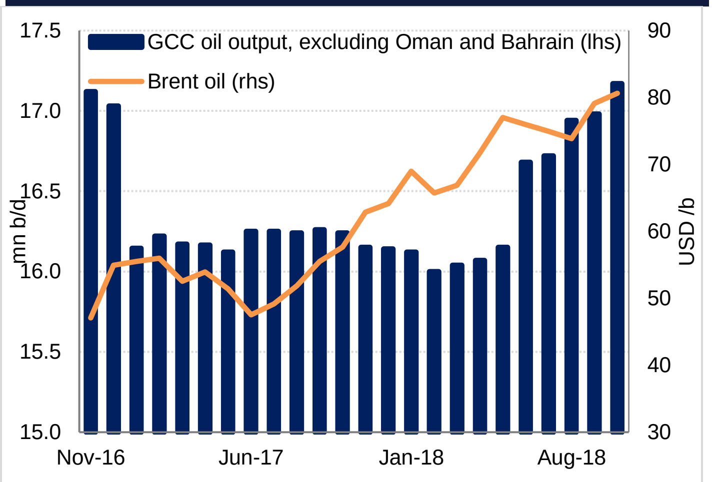
With the PMIs indicating that non-oil sector growth has not accelerated this year, it would seem reasonable to revisit our 2018 GDP growth forecasts. **In the UAE, we have retained our headline GDP growth forecast of 2.2%, but we have revised our forecasts for the drivers of growth**. We have upgraded our forecast for the oil sector to 0.7% (from no change), and revised our estimates for non-oil sector growth down to 2.8% from 3.1% previously.

In Saudi Arabia, oil production will likely be up around 2.5% this year, even after a 500k b/d cut in December, while H1 2018 GDP data shows non-oil sector growth of 1.8% y/y. Both of these are in line with our assumptions for the full year, and **we retain our 2.0% growth forecast for the Kingdom this year**.

Oil production in 2019 may disappoint

The uncertainty around our 2019 forecasts is higher however. Our current forecasts assume that 1) oil production in the GCC countries will rise further in 2019 and that 2) oil prices are likely to average USD 73/b, allowing governments to increase spending next year. Concerns about softer demand in 2019, and the recent sharp sell-off in oil prices, suggest that GCC oil producers may not be able to increase oil production by as much as we had anticipated. OPEC is due to meet formally in early December to review market conditions and its strategy going forward, and we will review our 2019 GDP growth forecasts after that meeting.

Will GCC oil output continue to rise?



Source: Bloomberg, Emirates NBD Research

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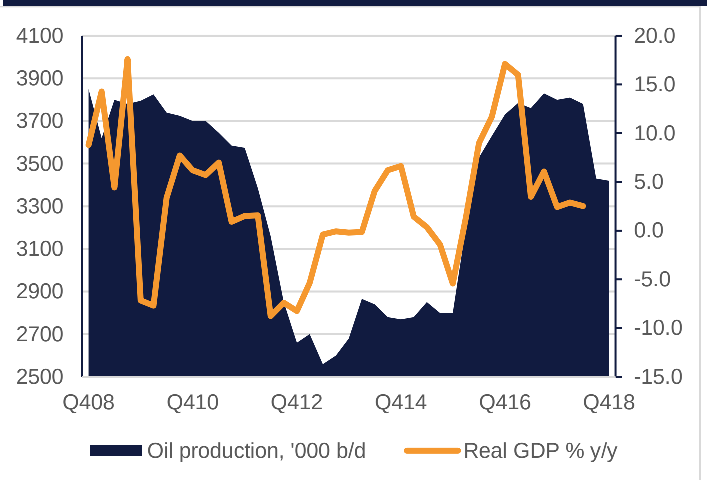
Non GCC Macro: US sanctions will negatively impact Iranian growth

Although the US announced just prior to the reimposition of stringent sanctions on Iran on November 5 that it would in fact grant waivers on imports of Iranian crude to eight countries, we see this more as a stay of execution for the Iranian economy rather than any significant lifeline. The impact of the US's decision to pull out of the JCPOA nuclear deal may be more protracted, but it will be only marginally less severe for the economy over the medium term, and other significant challenges to growth remain in play. As such, we are for the meantime leaving our real GDP growth forecasts for Iran unchanged at -1.9% in 2018 and -4.0% in 2019.

Those eight countries – China, Greece, India, Italy, Japan, Taiwan, Turkey and South Korea – which have been granted waivers have 180 days before these are up for review once more, and within this time they likely have to prove that they have made significant headway on reducing their imports of Iranian crude. As such, demand for Iranian oil exports will still fall off as countries seek to ensure compliance with the US on these measures. According to central bank data, Iran's oil GDP saw real growth of 5.2% y/y in Q2, following a -4.2% contraction in the first quarter. With production already down significantly in Q3, and likely to fall further still in Q4, this will contribute to what we project will be a decline in headline real GDP in 2018 and 2019, forecasting contractions of -1.9% and -4.0% respectively.

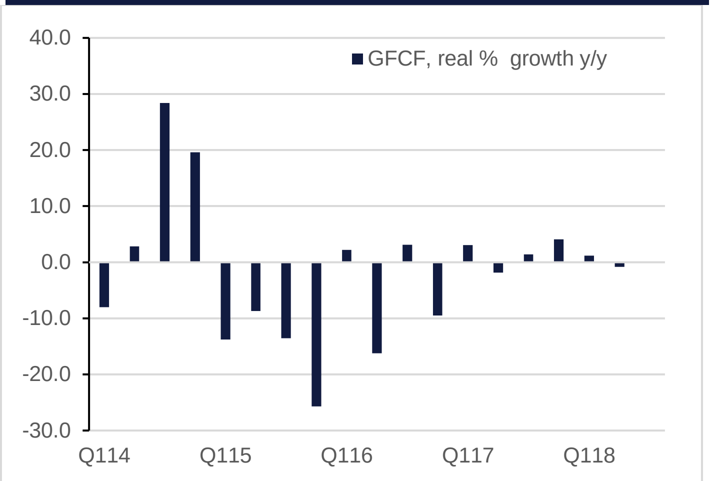
Oil sector influences GDP growth



Source: Bloomberg, Haver Analytics, Emirates NBD Research

While the granting of waivers allows a brief and limited reprieve to Iranian oil sector activity, the sanctions on oil are not the only penalties imposed on the country by the US through its withdrawal from the JCPOA. For starters, revenues secured from oil sales to those countries granted waivers will not flow directly to Iranian government coffers, but will be held in escrow accounts in local currency for the purchase of non-sanctioned goods. Additionally, financial messaging service SWIFT has cut off a number of Iranian banks, which will make it harder to process international transactions. The US has also imposed sanctions on over 700 individuals and entities, and has promised to be diligent in penalising those firms that seek to evade these. Secretary of State Mike Pompeo told a news conference on November 5: 'I promise you that doing business in Iran in defiance of our sanctions will ultimately be a much more painful business decision than pulling out of Iran.'

Investment will remain weak



Source: Havers Analytics, Emirates NBD Research

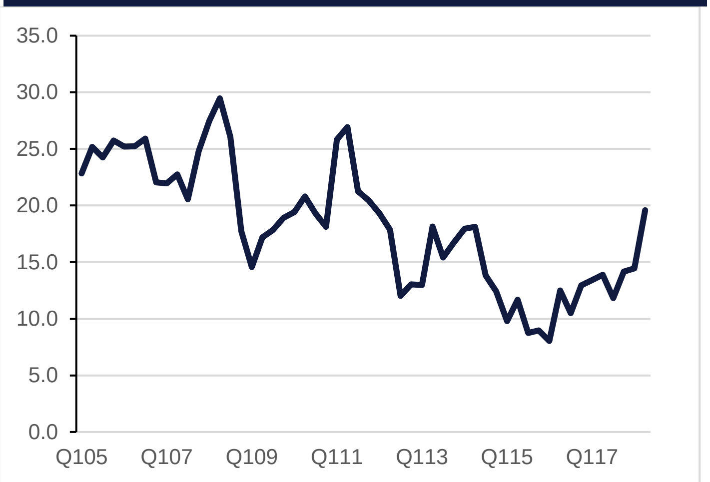
In light of this, firms that had been enticed by the promise of the Iranian market in the wake of the JCPOA's signing in 2015 have already pulled back from the country, and we see no likelihood that they will reengage as long as these US sanctions remain in force. Among the most high profile of these companies are Boeing, Maersk Line, Groupe PSA and Airbus, in addition to Total in the oil space. This withdrawal is despite a move by move by European countries sill supportive of the JCPOA to create a special purpose vehicle by which firms could continue to operate in Iran, and we expect little meaningful uptake of this in the future for those very reasons outlined above by Pompeo. This may leave some space for smaller firms less exposed to the US to move in, for instance from China or Russia, but it will unlikely be sufficient to offset the economic contraction we still expect. Real growth in gross fixed capital formation was negative -0.8% in Q2 2018, and we anticipate that it will remain in negative territory through the remainder of 2018 and 2019.

Resistance economy?

With the economic path predicated on the JCPOA chosen by President Hassan Rouhani having been derailed by geopolitics, Iran will have to turn once more to what it has termed its 'resistance economy.' As defined by Ayatollah Khamenei in a speech of 2016, this encompasses boosting domestic production and pursuing import substitution wherever possible, clamping down on corruption and economic rents, and generally making better use of its resources. According to the Supreme Leader, 'By pursuing the policies on the economy of resistance in a practical and pragmatic way, we can immunise the country. We can immunise the country so that we will no longer tremble in the face of sanctions and the possibility of sanctions.'

It is worth noting that even before the imposition of stringent nuclear-related sanctions through 2010-2012, Iran was theoretically better able to withstand sanctions on its oil sector than its oil exporting Middle Eastern peers might have been. Despite having among the largest proven oil and gas reserves in the world, the economy is comparatively well diversified, and in 2010, the oil sector accounted for only 21.2% of GDP. This fell to just 9.4% in 2015 as the JCPOA was signed, but even since then the sector has only recovered to 13.5% of GDP in 2017, and 16.2% in H2 2018. This is compared to 65% in neighbouring Iraq, for example. This is one of the factors behind our expectation that the economic impact of sanctions this time around will be less severe than in 2012, when the economy contracted by 7.8%. Nor is there an over reliance on just one other sector for the rest of the economy – agriculture, manufacturing, transportation, real estate and restaurants and hotels all have a share of around 10%-15% of GDP.

Oil GDP, % total



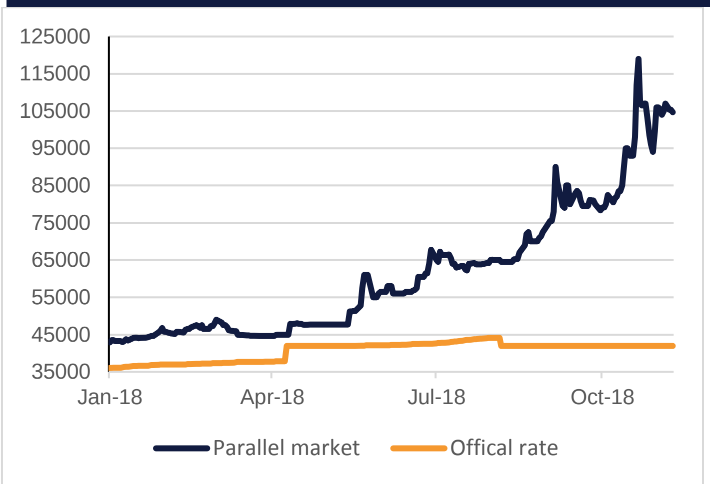
Source: Haver Analytics, Emirates NBD Research

Alongside its endowment with natural resources, Iran also has significant human capital; at 81mn it has the second-largest population in MENA after Egypt, and is larger than the six countries of the GCC combined. Among these 81mn, there is a significant youth population and educational attainment is reasonable (ranked 74th out of 137 globally, and higher than a number of other MENA markets including Oman, Kuwait, and Egypt). On the downside, female participation in the labour force is lowest in the world, but this represents significant untapped potential.

Impact will still be acute

While the Iranian economy can in theory endure better than some of its peers might be able to under similar circumstances, the negative impact of sanctions will nevertheless be severe, and especially so on households. This has already begun to play out in 2018, as the Iranian rial has sold off rapidly in the parallel market, despite government efforts earlier in the year to unify its exchange rates and criminalise black market activity. At the time of writing on November 11, the parallel exchange rate was reportedly at IRR 144,000/USD according to Bonbast, compared to the official rate of IRR 42,000/USD. This has contributed to CPI inflation ticking up to 36.9% y/y in October, levels not seen since the last sanctions-driven spike in 2012/2013. High levels of M2 growth, at 20.4% y/y in Q2 2018, will also have played a part, and we expect that inflation will accelerate still further over the coming months, forecasting a year-end rate of 40.0% with risks to the upside.

IRR/USD exchange rate



Source: Bloomberg, Bonbast, Emirates NBD Research

Some of the worst effects of this on households will be mitigated by government support in the way of subsidised foodstuffs. The improvements made in food security over the past several decades, and especially since Rouhani came to power, will also dampen the risk. In 2013, Iran's food self-sufficiency stood at 55%, according to Iranian reports, and has risen to as high as 90% in the intervening period. Combined with domestic oil production and refining capacity, this means that it is in a relatively strong position to withstand sanctions with regards essentials. However, while Iran scores quite well on the Global Hunger Index, and the risks in this regard are minimal, there will nevertheless be a squeeze on disposable incomes.

This will combine with a more general dearth of opportunity as private sector growth stalls, likely to be felt most acutely by the middle classes. Enrollment in tertiary education in Iran has risen from just 19.3% in 2000 to 68.8% in 2016, according to World Bank data. Additionally, there are many thousands of Iranians studying abroad (for whom life will become harder under renewed sanctions as banking transactions are made more difficult). However, this increase in higher education has not been matched by a commensurate increase in graduate positions. Youth unemployment stood at 28.3% in July, with many more likely employed in jobs not making full use of their education and ambition. As such, mounting dissatisfaction with the economic malaise could lead to renewed unrest in Iran.

Interest Rates

The UST yield curve continued to move higher though sovereign yields in other developed economies softened in anticipation of slower global growth ahead.

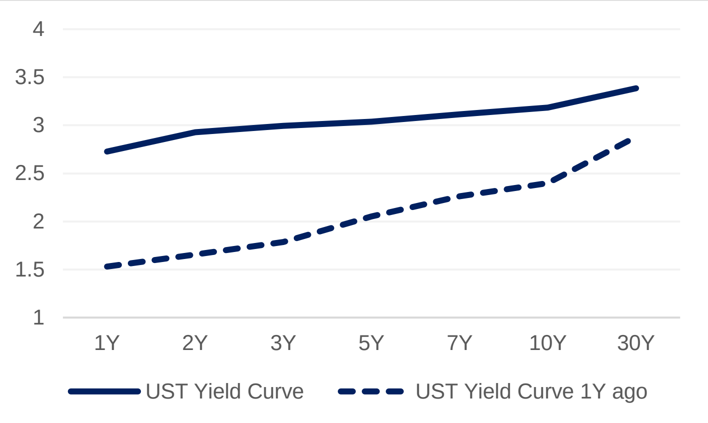
US Rates

Last month marked an inflection point as investors began to question the sustainability of the current pace of global growth. While the US continued to enjoy strong economic data, growth in Europe softened slightly thereby causing sovereign bond yields to eease there.

The US Federal reserve left interest rates unchanged at their November meeting but there was nothing in the policy statement to suggest that the Fed will deviate from its plan to raise rates again in December. The Fed's judgement to continue raising interest rates is supported by the latest data which points to economic growth running above an annualized rate of 3% and core PCE inflation running at the 2% target. Consequently the UST yield curve continued to shift upwards albeit with a bear flattening bias.

The yield curve flattened as the outcome of the US mid term election, with Republicans losing control of the House, raised prospect of more checks and balances in US politics. The Yield on 2yr, 5yr and 10yr closed the month at 2.92% (+7bps, m/m), 3.03% (+2bp, m/m) and 3.18%(+2bps, m/m) respectively.

UST Yield Curve (%)



Source: Bloomberg

These movements presumably reflected a view that while another round of fiscal stimulus would be much less likely under a Democrat- than a Republican-controlled House, the risk of a government shutdown under a split Congress has increased. With the current government funding bill due to expire on 7th December, the next trigger point for potential spike in the short term yields may only be a few weeks away.

Global Rates

In the UK, while GDP growth picked up pace in Q3 (+0.6% q/q growth), reflecting its strongest quarterly gain since late 2016, it was mainly on the back of pick up in construction activity after weather related slowdown in the first half. Otherwise, the data provides enough validation that Brexit uncertainty has caused firms to limit their spending. The clouded outlook on Brexit deal caused the yield on 10yr Gilts to soften, closing the month down by more than 14bps to 1.48%.

10Yr Government Bond Yields

	Yield %	1M chg	3M chg	12M chg
US	3.18	+2	+31	+78
UK	1.43	--20	+19	+9
Germany	0.38	-11	+7	-2
Japan	0.11	-3	+10.3	+7
Brazil	5.46	-	-20	+69
Argentina	9.16	-48	-64	+334
Turkey	7.25	-28	-107	+173

Source: Bloomberg

Uncertainty around the Italian budget continued to weigh on risk sentiment in the Eurozone area. Italy's redrafted budget reflected little changes to the first draft budget, raising the risk that the European Council penalises Italy under an Excessive Deficit Procedure. Besides Italy, there are concerns in the Eurozone area about slowing GDP growth with the negative impact of the 7% slump in car production filtering into the economies. Quarterly euro-zone growth slowed to just 0.2% in Q3. Yields on 10yr Bunds narrowed 10bps to 0.38% in response.

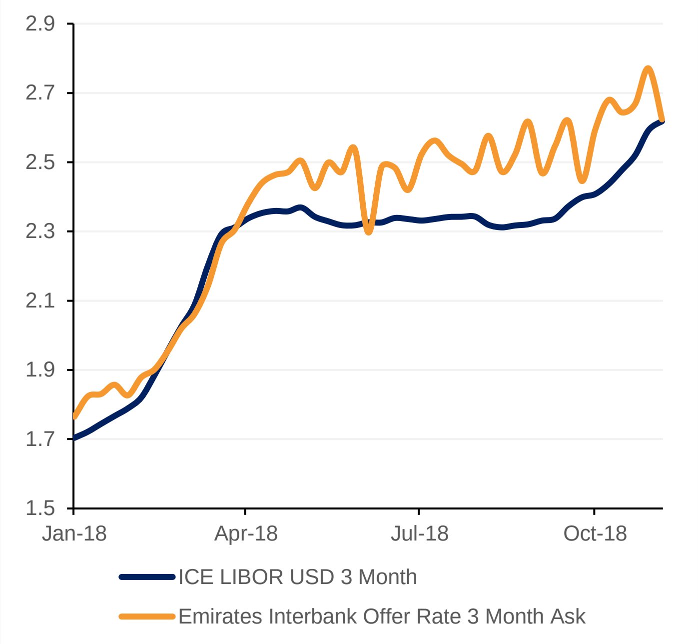
Worries about US protectionism against China have been a key factor behind the struggles of the emerging market sovereign bonds in recent months. Post the midterm election, markets now appear to have concluded that the election outcome doesn't make a huge difference to the current uncertainties surrounding the trade tariffs. Despite the Democrats' victory in the House of Representatives, there is no sense that they will bind President Trump's hand in his trade war with China. If anything, some left-wing Democrats would prefer an even tougher stance than Trump has adopted so far. It seems that the trade related concerns are unlikely to go away anytime soon and therefore sovereign yields in emerging market economies are llikely to remain volatile.

GCC Local Rates

Policy rates in the GCC are deemed to move in sync with the rising US rates. However interbank rates do not always keep pace with the USD LIBOR rates and instead reflect the level of liquidty in the local banking systems.

Last month the 3m EIBOR – LIBOR spread and also the 3m SAIBOR – LIBOR spread narrowed as higher oil prices boosted deposits in the local banking systems.

3m EIBOR – LIBOR spread narrows



Source: Bloomberg, Emirates NBD Research

In the longer tenured space, there is limited government bond supply in local currency markets. The USD denominated GCC sovereign bonds recorded minimal yield changes barring Oman which saw the yield on its 10yr bond increase by 20bps mainly as a result of the USD 1.5 bn sovereign sukuk issued last month.

	Rating	Yield %	1M chg	3M chg
Oman 01/28	Baa3	6.38	+20	-2
KSA 03/28	A1	4.48	-2	+24
Sharjah 03/28	A3	4.47	+1	+14
Qatar 04/28	Aa3	4.27	-2	+2
Bahrain 10/28	B3	7.21	+7	-91

Source: Bloomberg

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Credit Markets

Increasing credit spreads on the back of falling oil prices and rising geopolitical risks in the region left GCC bonds weaker during the month.

Global Bonds

Anticipation of slower global growth and the recent sell off in oil prices reduced risk appetite and caused credit spreads on corporate bonds to rise across the globe. In addition, the rising UST benchmark yields further dampened returns on USD denominated bonds from DM as well as EM economies.

Barring Europe, where benchmark sovereign bond yields had a narrowing bias on the back of slowing GDP growth, total return on credit bonds from most other jurisdictions were negative. US IG Corp index recorded a loss of -0.53% over the last one month and the loss on US HY bonds was -0.42% mainly attributed to widening of credit spreads on the HY index by circa 17bps to 361bps.

Global Corporate Bond OAS (bps)

	OAS	1M chg	3M chg	12M chg
US IG Corp	115	+6	+3	+15
US HY Corp	361	+17	+41	+2
EUR IG Agg	88	-	+5	+34
USD EM Agg	293	+7	-26	+42
GCC Agg	168	+2	-7	+5

Source: Bloomberg

Credit spread widening was fueled by increasing fears of the negative impact of rising US interest rates on economic growth and corporate profitability going forward. CDS levels on US IG Main and Euro Main widened by 3bps and 1bp during the month to 69bps and 71bps respectively.

In addition, emerging market bonds remained under pressure as dollar strength and rising UST yields drained dollar liquidity.

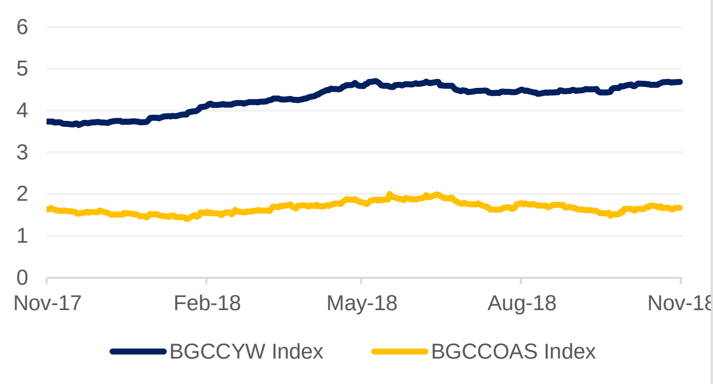
GCC Bonds – Secondary Market

GCC bond markets felt the pinch from recent decline in oil prices which dampened investor sentiment. Also ongoing geopolitical issues in the region affected the bid for Saudi bonds negatively. Despite the helping hand of the technical bid on the back of the pending inclusion of the GCC bonds in the JP Morgan EMBIG index and reducing budget deficits, overall credit spreads on Barclays GCC bond index rose over 10bps during the month to 168bps.

Monthly total return on GCC bond index was barely +0.02% as capital losses from rising yields were offset by coupon collection of annualized circa 4.5% on GCC bonds.

Despite the bearish oil market, CDS spreads on local GCC sovereigns were stable with **Saudi Arabia** and **Abu Dhabi** 5yr CDS levels closing the month mostly unchanged at 94bps and 67bps respectively.

Barclays GCC Credit Index: YTW & OAS %



Source: Bloomberg

The biggest new development was the finalization of the Federal Debt Law by the UAE government which would allow the UAE to issue sovereign bonds and sukuk at the federal government level. As announced by the Ministry of Finance, under the new law, the government will establish a Public Debt Management Office to oversee new federal-level borrowings. The government plans to seek a sovereign rating and sell bonds once the law gets enacted. Given the Dubai government's ambition to establish Dubai as a hub for Islamic Finance, we would expect part of the Federal Government debt to be in sukuk format, particularly as it will provide instruments for Islamic Banks to comply with their Basel III requirements.

GCC Bond Market Universe

	No. of Sec's	Amt USD'mn	% of Total
USD	306	320,473	62.72
SAR	102	105,793	20.7
QAR	59	27,147	5.31
BHD	40	13,585	2.66
KWD	49	12,907	2.53
OMR	24	7,506	1.47
AED	5	1,473	0.29
OTHER	57	22,082	4.31
Total	**642**	**510966**	**100**

Source: Bloomberg

Credit rating changes in the region have been mixed over the last quarter. **Dubai Aerospace's** rating was upgraded by a notch from Ba2 to Ba1 / stable by Moody's as the company made progress on diversifying its funding base and reduce reliance on secured funding. Straight after the upgrade, DAE Funding raised USD 1.0bn via 2-part senior notes. The USD 500mn each 3NCL and 5NC2 priced at 5.25% and 5.75% respectively. On the side, the yield on existing DUBAEE 24s closed the month circa 30bps wider at 5.91%.

Moody's also revised the outlook on **APICORP's** Aa3 rating to positive. The key driver of the outlook change to positive reflects progress that APICORP, the multilateral development bank (MDB) owned by the member states of the Organization of Arab Petroleum Exporting Countries (OAPEC), continues to make in reducing balance sheet maturity mismatches and its reliance on wholesale deposits in its funding mix by diversifying and lengthening its funding profile. Nevertheless, yield on APICOR 23s moved in sync with the wider GCC market, widening by circa 6bps to 4.15% over the month.

In contrast, Moody's placed the A3 rating on the **Commercial Bank of Dubai** on review for downgrade in view of the deterioration in the bank's asset quality.

Fitch affirmed **Dolphin Energy's** rating at A+ and revised the outlook back to stable from negative, citing the company's track record of continuing to operate at full capacity over the past year despite the standoff between Qatar and its neighbours. The yield on DOLNRG 19s fell 64bps during the month to 3.26%, making it one of the best performing bonds last month.

Moody's affirmed **Saudi Arabia's** rating at A1/stable citing expectations of higher GDP growth growing forward of 2.5% in 2018/19. Moody;s expects govt debt / GDP to remain below 25% in the medium term. On the side, financial information released by the Ministry of Finance in Saudi Arabia reflected its 9m budget deficit at SAR 49bn (USD 13.1bn), compared to SAR 121bn a year ago which augurs well for the 2018 full year deficit to be lower than the initial projection of SAR 195bns. Oil revenues still made up circa 68% of the total revenues. Oil revenue was up 63%, non oil revenues up 45% and spending was higher by 21%. That said, SAMA's net foreign assets declined to USD 499.78bn in September and 2Q unemployment rate among Saudi was unchanged at 12.9%. The yield on KSA bonds increased across the curve with KSA 23s closing at yield of 4.09% (+18bps, m/m)

GCC Bonds - Primary Market

Last month was another active month for GCC primary markets. Year to date total bonds and sukuk from the GCC region reached USD 76bn and appears well on the path to achieve our full year target of between USD 75 – 90bn of new supply this year.

Nogaholding (Bahrain's National Oil and Gas company) priced USD 1bn deal across two tranches with 6yr portion pricing at 7.625% and the 10yr at 8.375%. Given the cheap initial pricing, the bonds fared well in the secondary market, each rising by more than a point and half in the first week of trading.

Sultanate of Oman, rated Baa3 by Moody's and BBB- by Fitch, completed its financing for the year, raising USD 1.5bn via a 7yr sukuk Al-Ijara that priced at MS + 280bps, 20bps tighter than the original guidance of 300bps, however circa 25bps wider than what its secondary market curve would have implied.

Also AA/Aa2 rated, **Mubadala Development** priced USD 800mn 10yr bonds at MS+135bps vs IPT of 150bps.

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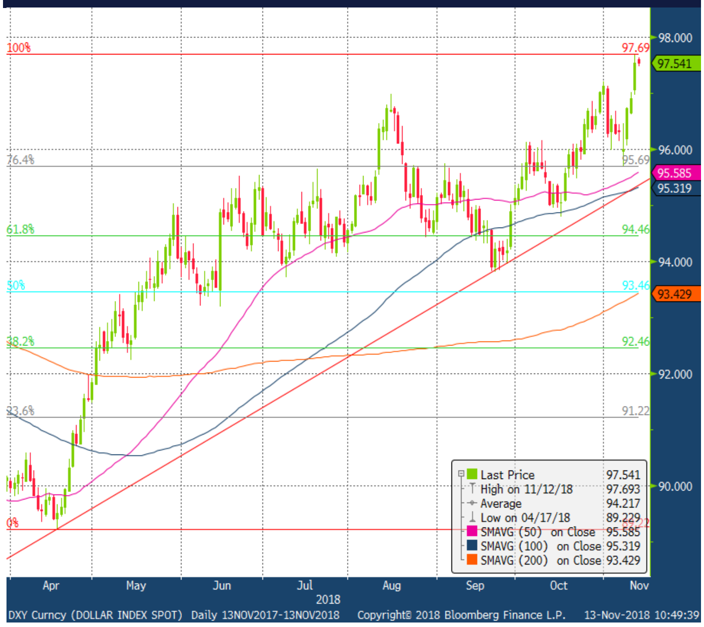
Currencies

The dollar hovers near 18-month high

Approaching the midpoint of the final quarter of 2018, the dollar has continued to appreciate, reaching an 18-month high. This is in contrast to the performance of the dollar in the first quarter, where it fell to the lowest level since December 2014. The main driver behind this reversal of fortunes has been Fed rate hikes and the expectation of more to come. Having already raised rates three times in 2018, the Federal Reserve has paved the way for a fourth hike in December at their meeting earlier this month with the market implied probability of a 25bps hike just short of 76%. Supported by continued strong growth, employment, inflation and consumer confidence data, it is likely that the current cycle of normalization of monetary policy will continue into the first half of 2019 at least. This prospect is likely to underpin dollar strength for longer and we have revised our USD forecasts to reflect this (see page 28).

DXY remains near 2018 highs



Source: Bloomberg

Technical analysis of the Dollar Index's daily candle chart shows that the price has been in an uptrend since April 2018. In addition, over the last month, the 50-day and 100-day moving averages (95.584 and 95.319 respectively) have supported the index and have halted all declines, without fail. Having gained 2.61% over the last 30 days to reach 97.511, the index is also on target to close above the 200-week moving average (95.871) for a fourth week and has even broken above the formerly resistive 50-month moving average (95.466) which has provided support in Q4 2018. These developments lead us to believe that further short-term gains lie ahead for the dollar and while the price remains above the 200-week moving average, further gains towards the 76.4% five-year Fibonacci retracement of 97.940 are probable.

EUR has lowest daily close since June 2017

The euro has found itself under significant pressure over the last month as softer than expected economic data and political risks have weighed on the single currency. While ECB President Mario Draghi kept a positive tone at October's central bank meeting and confirmed policy makers' intentions to end the Asset Purchase Program by the end of the year, economic data has been less encouraging. A report from Eurostat showed that Eurozone aggregate GDP slowed to 0.2% q/q in Q3 2018 from 0.4% in Q2, taking annual growth down from 2.2% y/y to 1.7%. In addition, retail sales showed no growth in October and consumer confidence has taken a hit amid growing concerns over trade dispute escalations. On the geopolitical side, Italy's first budget draft was rejected by the European Commission in October due to a larger budget deficit than previously committed to. With the populist government demonstrating an intent to stick to its plans, cutting taxes and increasing spending, the risk is that the EU will impose financial penalties on Italy. Further out the greater risk is of a debt default by Italy.

EURUSD has daily close below 1.13

Source: Bloomberg

Since our last monthly publication, EURUSD has realized a loss of 2.83% to reach 1.1252. The price had fallen as low as 1.1219 before profit taking helped relieve some of the downwards pressure. Of note is that there was a daily close on Monday 12th November 2018 below the 1.13 level, the first time this has happened since June 2017. While the price remains below this level, there is a significant chance of additional declines towards 1.10, an outcome whose probability will be increased if there is a daily close below the 23.6% five-year Fibonacci retracement of 1.1203.

As Brexit edges closer, the pound stays weak

Despite UK GDP accelerating to 0.6% q/q from 0.4% the previous quarter and annual GDP accelerating from 1.2% y/y to 1.5%, sentiment on GBP is still largely being dictated by Brexit. Although a tentative deal between PM Theresa May and the EU appears to be inching closer, the support of the UK cabinet is far from certain even before members of Parliament can vote on it. It is not surprising in this context that speculation is rising about the possibility of a second referendum, which is beginning to be reflected in GBP's ongoing softness.

GBPUSD breaks back below 1.30

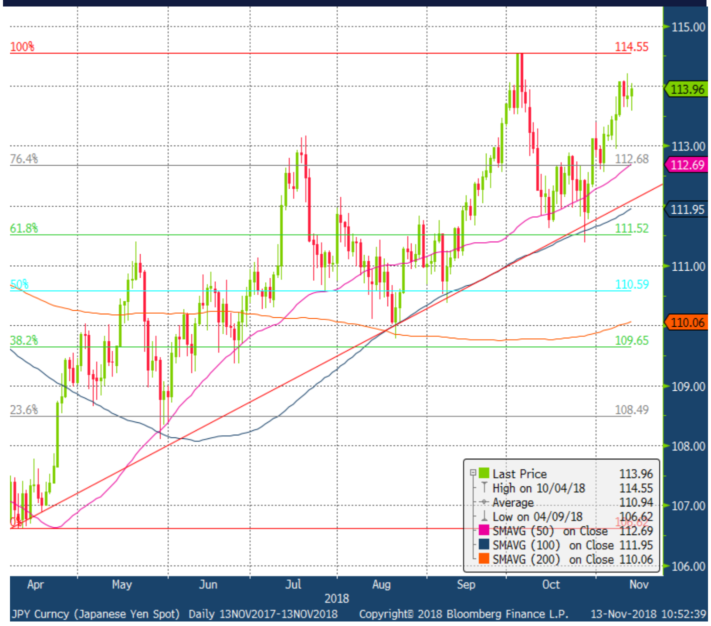
Source: Bloomberg

The pound has endured a volatile performance during the last fortnight of October and the first half of November. Falling from the monthly highs of 1.3258 on October 12th to lows of 1.2696 on October 30th, the price was then able to recover to a November high of 1.3175 on the 7th before falling to the current levels of 1.2890. In the process the price has fallen back below the 100-week moving average (1.3130) as well as the formerly supporting 50-day and 100-day moving averages (1.30312 and 1.3026). We still expect the pound to recover significantly over the course of 2019 if a deal is negotiated between the U.K and the E.U, but this looks far from certain right now. As such in the short term sterling is still vulnerable to further declines. While the price remains below the prior mentioned moving averages, there is a risk that the 2018 low of 1.2662 is revisited, with a break of this level exposing GBPUSD to 1.25.

JPY underperforms in November

Thus far, JPY has been the worst performing G-10 currency in November. With the climb in U.S. yields, the 10-year UST has stayed above the 3% mark since September 18th, USDJPY has remained supported and risen more than 1% in November to reach 114.10, not far from the 2018 highs of 114.55 seen during the first week of October. A break and daily close above this level, is likely to result in further gains towards the 61.8% five year Fibonacci retracement of 115.61, an outcome made more likely if there is a break above 114.53, the daily capping trendline that has held since January 12th 2017.

USDJPY advances past 114



Source: Bloomberg

INR outperforms other EM currencies

The INR was among the few emerging market currencies to outperform over the past month despite USD strength. The INR has gained +2.4% 1m compared to a decline of -0.89% 1m in the JP Morgan EM Currency index. The outperformance is in line with our expectations *(see India Monitor, 3 October 2018)* and can be broadly attributed to sharp correction in oil prices and sustained strength in macroeconomic data. That coupled with benign inflation trajectory, a relatively sanguine Reserve Bank of India, and strength in direct and indirect tax collections have reduced fears of an exaggerated twin deficit scenario and reinforced view of a credible pick-up in economic activity. Having said that, the immediate risk to our year-end target of 71.0 remains the elevated political risk. Any reversals by the incumbent in the current round of state elections (results scheduled for 11 December 2018) could see return of heightened risk aversion sentiment ahead of general elections in 2019.

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Equities

Global equities remained weak as investors began to position themselves for greater political and monetary policy unpredictability and uneven economic growth heading into 2019.

The factors driving performance of global equities over the past month could be rightly seen a microcosm of 2018. For market participants it was effectively a face-off between concerns over tighter financial conditions and political uncertainty on one hand and strong economic growth and corporate earnings on the other. With both side of the scale lacking a definite tilt in its favor, volatility has remained elevated and investors have turned cautious. The CBOE volatility index is on track for its biggest annual jump since 2007 with year to date gains of +81.1%.

Over the last month, the MSCI All Country index dropped -1.7% 1m to take its year to date losses to -5.2%. The weakness was broad-based with all major sub-indices closing lower with the exception of the MSCI Frontier Market index. The MSCI Emerging Markets index and the MSCI G7 index lost -1.4% 1m and -2.0% 1m respectively. The notable trend was the underperformance of technology and energy sector stocks across the board. The MSCI All Country Information Technology index dropped -5.2% 1m to move into negative territory for the year. If the losses sustain, then this would be the first annual loss for the index since 2011 after having rallied +124% since 2012. The MSCI All Country Energy index dropped -6.7% 1m to also move into negative territory for the year. The move in energy stocks was a direct reflection of a sharp sell-off in oil prices. The Brent and WTI oil have corrected -14.5% 1m and -17.7% 1m respectively. Both these sectors together account for c.25% of the broader index.

Notwithstanding the expected result from the US mid-term elections, politics is likely to remain a key catalyst in the near term. The focus will be on Europe where both the Italy budget issue and the Brexit talks are nearing the end-game. Also, investors will keep a keen eye on how the results of the midterm election weighs on default policy choices of the US President Donald Trump especially on trade. Another key element will be the last Federal Reserve meeting of 2018. While a 25bp rate hike is priced in, investors would be sifting for clues on the probable peak rate and the number of hikes in 2019. Regionally, the level of oil prices have become a factor again and will be closely watched.

Equities – the underperformer

Global equities have underperformed most asset classes so far in 2018. While it was always anticipated to be a challenging year for equities in general given that 2017 was among the best performing years in the last decade, it would be fair to say that the longevity and unpredictability of political issues have trumped a consistently strong economic backdrop and record corporate earnings. For the first time in last three years, concerns over tighter monetary policy also became a factor. It would be fair to say that 2018 marked the end of the central bank backstop to global equities which has been in place for better part of a decade. Even a fiscal stimulus in the US failed to offset the intangible factors.

Asset Class Returns

	2010	2011	2012	2013	2014	2015	2016	2017	2018 ytd
Global Equities	13.29%	-6.84%	16.82%	23.48%	4.75%	-1.80%	8.53%	24.65%	-3.05%
DM Equities	8.34%	-11.68%	17.96%	23.43%	-4.32%	-0.28%	1.59%	25.70%	-8.56%
EM Equities	19.24%	-18.16%	18.62%	-2.32%	-1.96%	-14.60%	11.74%	37.79%	-14.49%
FM Equities	22.19%	-18.43%	8.47%	25.94%	6.60%	-14.78%	2.66%	31.83%	-15.11%
MENA Equities	12.56%	-13.87%	4.50%	20.83%	-0.17%	-17.38%	4.39%	0.77%	6.84%
Dev Sov Bonds*	3.02%	4.29%	3.65%	0.31%	7.05%	1.28%	2.63%	1.07%	-0.68%
Treasuries*	-	9.77%	2.03%	-3.37%	6.19%	0.85%	1.03%	2.31%	-2.14%
Global High Yield	14.82%	3.12%	19.60%	7.33%	0.01%	-2.72%	14.27%	10.43%	-2.06%
GCC Credit		7.25%	13.62%	0.22%	5.93%	0.80%	4.56%	5.22%	-0.74%
Commodities	16.83%	-13.32%	-1.06%	-9.52%	-17.01%	-24.66%	11.77%	1.70%	-4.23%
Gold*	29.48%	10.06%	7.14%	-27.97%	-1.34%	-10.20%	8.56%	13.09%	-7.85%
Oil (Brent)*	21.58%	13.33%	3.47%	-0.28%	-48.26%	-34.97%	52.41%	17.69%	4.86%
Global REITs	31.37%	5.68%	21.08%	-2.10%	33.51%	0.70%	6.51%	7.98%	0.29%
Hedge Funds	7.34%	-5.15%	5.04%	7.37%	1.43%	0.61%	3.59%	9.73%	-8.80%

Source: Bloomberg, Emirates NBD Research. As of 12 November 2018

*Indices used - Global Equities (MXWD index), DM Equities (MXEA Index), EM Equities (MXEF Index), FM Equities (MXFM Index), MENA Equities (DJMENA Index) Dev Sov Bonds (SPFIDSLT Index), Treasuries (BUSY Index), Global High Yield (LG30TRUU Index), GCC Credit (BGCCTRUU Index), Commodities (BCOMTR Index), Gold and Oil (Spot Prices) Global REITS (ENXG Index), Hedge Funds (BBHFUNDS Index). * shows price change while others show total return*

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The MSCI All Country index returned -3.1% ytd compared to -2.1% ytd return in US treasuries and -7.9% return from Gold. Therein lies perhaps a paradox as gold is generally considered a proxy for risk aversion and a hedge against increasing inflation. Hedge funds and commodities returned -8.8% ytd and -4.2% ytd respectively.

The underperformance of global equities was driven by a sharp fall in emerging market equities. The MSCI EM index returned -14.5% ytd compared to a return of -8.6% ytd from developed market equities. Brazilian equities were notable exceptions to the broad sell-off in emerging market assets. The Bovespa index has rallied +12.3% ytd with most of its gains coming in the last three month during which the current President Bolsonaro won elections. US equities have so far managed to remain in positive territory with the S&P 500 index gaining +2.0% ytd.

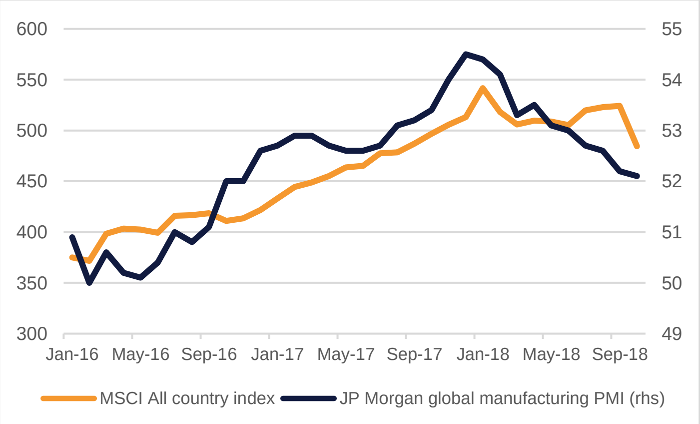
For the MENA region, the performance so far this year has been positive but uneven. The broad +6.8% ytd gain in MENA equities has been driven by strength in Saudi Arabian, Qatar and Kuwait equities. These three countries saw some follow-through impact of positive development from their participation in broad indices. For example, it was confirmed that Saudi Arabian equities will be included in the MSCI EM index from next year.

Risks in 2019 – An early peek

Fear

The biggest risk for global equities in 2019 could possibly be the embedded fear in investors' minds that an economic recession or a sustained slowdown is around the corner. While we are not arguing that such a possibility is completely unfounded, however it does appear premature. Most estimates show that the world GDP growth will slow but still remain above trend in 2019. Global trade will likely emerge as the biggest factor in moulding investor sentiment as the current moderation in global manufacturing PMI readings is being attributed to ongoing trade tantrum. It must be noted though they continue to remain in expansion territory.

PMI & Equities



Source: Bloomberg, Emirates NBD Research

The positive correlation between manufacturing PMI index and equity market movements suggests that any further deterioration could breed greater macro uncertainty and higher volatility which in turn could see investors' first preference shift towards risk-aversion.

Interest Rates

One certain risk for global equities in 2019 is tighter liquidity conditions as most central banks in developed and emerging markets reaffirm their commitment to remove accommodative policies. The Federal Reserve is ahead of the curve relative to all other central banks and hence will be keenly watched. What the neutral rate is, and whether hikes will extend into 2020, is likely to dominate the conversation.

The impact of higher rates are multifold. It impacts companies' profitability and valuations through avenues of demand, higher cost and concurrent moves in FX. Additionally, it hurts companies which are highly leveraged and hold foreign currency debt.

Also importantly, a rise in real interest rates has already begun to result in price to earnings multiple contraction. For example, the MSCI ACWI is currently trading at 13.9x forward price to earnings ratio compared to 15.0x it was trading three months ago. The trend is similar in emerging markets with the MSCI EM index currently trading at 10.3x compared to 11.4x three months back. It would be fair to say that lower multiples are likely to be a headwind notwithstanding growth in corporate earnings.

Politics – Trade & beyond

In terms of political risk, 2019 is unlikely to be much different from 2018. In fact, the lack of resolution of issues lingering on from 2018 could have a deeper impact on markets than in 2018. US President Donald Trump will remain at the center given his continued tendency to comment on all matters including oil prices, trade policy, stock market movements and central banks. However, 2019 is likely to see enhanced domestic pressure on his presidency given Democrats' control over the House of Representatives. If past experience is any guide then it will be no surprise to see a more rigid position on trade talks with China and Europe and perhaps more populism through looser fiscal policy. The impact of an extended trade skirmish is already visible in equity markets through weakness in stocks directly affected and renewed concern over demand of commodities. The S&P industrial sector index has dropped -6.1% year-to-date.

While the Brexit issue is likely to dominate headlines in early 2019, it could well result in a full-blown political crisis for the United Kingdom. Similarly, the impending departure of Angela Merkel could see intra-Eurozone issues become more frequent. Indian general elections could well set the tone for emerging markets in 2019 given the direct correlation between stable and strong government and structural reforms in such economies. Within the MENA region, 2019 could well be a year of reckoning as multiple issues remain on horizon including continued need of economic diversification away from oil.

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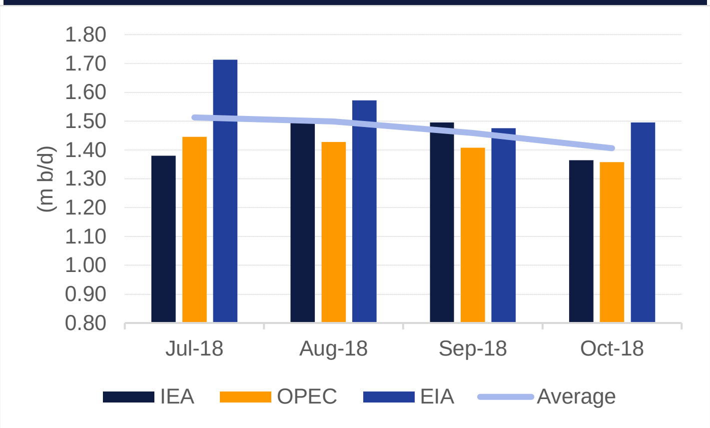
Commodities

Middle East oil exporters face a challenging year in 2019. Projections for oil demand growth are at their softest in the last few years as the global economy reels from tightening financial conditions and the impact of a US-instigated disruption to world trade. Production outside the region is set to accelerate thanks to productivity gains in the US and higher output in the former Soviet Union while inventory levels have stabilized. Meanwhile sanctions on Iran and a reluctance to worsen an emerging market surplus will dampen the region's contribution to global oil supply growth. Beyond these headline issues, oil quality and regulation issues will be a significant headwind for oil producers in the GCC, against which there are few easy fixes.

The top-down view for global oil markets in 2019 looks challenging. Demand growth projections from major forecasting agencies have been trending lower as economic conditions are set to weaken, particularly in emerging economies which are the major contributors to oil demand growth. OECD demand is also set to resume its downward trajectory after a few years of surprising performance. The IEA projects demand growth of 1.37m b/d compared with a five-year average of more than 1.5m b/d as the benefit of lower oil prices has waned.

2019 demand forecasts moving lower



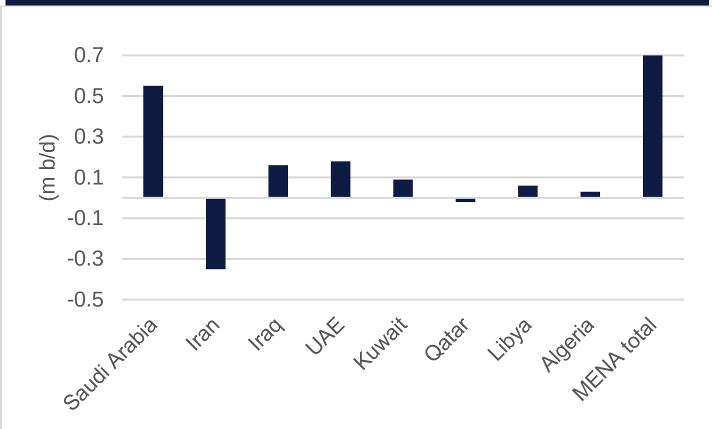
Source: IEA, OPEC, EIA, Emirates NBD Research. Note: EIA's November STEO forecasts growth of 1.41m b/d

At the same time, supply projections from the IEA for non-OPEC nations show a surge in output next year of nearly 1.8m b/d after the more than 2m b/d estimated for 2018. The US, Brazil, Russia and Canada will account for the bulk of next year's increase in non-OPEC supply and companies there are arguably less burdened by the high socio-economic revenue requirements facing national oil companies in the Middle East.

The softer demand projections and strong view on non-OPEC supply cuts the space for OPEC to continue increasing production incessantly. Indeed the IEA's latest estimate for the 'call' on OPEC crude is just 31.55m b/d, more than 1m b/d lower than what OPEC produced in Q3. The 'call' on MENA OPEC countries for 2019 is 26.03m b/d, 1.15m b/d below September production levels (the gap has likely worsened thanks to a large increase estimated for October).

OPEC agreed to raise production in June to compensate for declining output in Venezuela, offset an anticipated drop in Iranian volume and bring compliance with its production cut agreement back to 100%. Since the start of the year to September output from OPEC's MENA countries has increased 700k b/d as substantial increases from Saudi Arabia, Iraq, the UAE and Libya more than offset declines from Iran. But space to raise output more substantially seems to be narrowing. US sanctions on Iran have now been reintroduced in full but waivers for eight major importers of Iranian crude have tempered their impact, at least temporarily.

MENA oil supply growth ytd



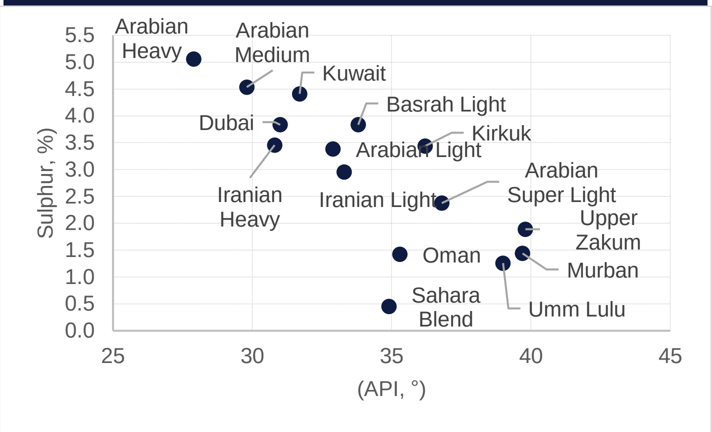
Source: IEA, Emirates NBD Research. Note: data as of September 2018.

The sanctions relief will last for 180 days and will likely encourage OPEC to keep production level at its next meeting (December 6th) rather than risk exacerbating a market surplus via significantly higher production. Market chatter is already suggesting a production cut is being mooted by OPEC and its partenrs. Our forecasts for oil production growth in 2019 among MENA producers in OPEC shows output increasingly modestly—just 90k b/d—as an increase of more than 500k b/d from GCC members are offset by a drop in Iran's output.

But once the sanctions waivers expire at the end of 180 days Middle East producers face a more structural challenge to their share of the global oil market. From 2020 new UN regulations governing the sulphur content of fuel oil come into effect (IMO 2020 in industry jargon). From 2020 onward shipping companies, the main consumers for fuel oil, will be mandated to use a maximum of 0.5% sulphur fuel in their vessels down from the currently accepted 3.5%. There are several options available to shipping companies to work under the new regulations: install devices that clean emissions—scrubbers—and continue using high sulphur fuel oil (HSFO); use LNG as an alternative fuel, requiring a refit of engines; or mix existing fuel stock with lighter sulphur products such as gasoil. Industry appears to be leaning toward greater use of gasoil in shipping fuels as it requires the least amount of retrofitting. There has been a corresponding improvement in gasoil prices and cracks over crude in anticipation of more demand for the fuel, particularly in the run up to 2020 as inventories will need to be built at critical bunker ports.

Fuel oil is a product of oil refining and is valued at much lower levels than gasoline components or gasoil/diesel. In normal market conditions fuel oil is priced at a discount to crude given its relative low economic value. Heavy crudes that produce a relatively higher volume of fuel oil compared with other products attract a discount to lighter crudes. The strict sulphur requirements will create additional distinction between crudes on offer from Middle East producers, both within the region and relative to competing international grades.

ME crudes by weight and FO sulphur



Source: EIKON, Emirates NBD Research. Note: sulphur % is approximate measure of sulphur quantitiy in fuel oil produced from regional crude grades.

Most of the crude produced by regional NOCs tends to be both heavy (i.e. higher in fuel oil content) and sour (higher in sulphur). Murban, one of the lightest and sweetest (low sulphur) crudes produced in the region, is still heavier and more sour compared with benchmarks Brent or WTI. For the benchmark grades produced by Saudi Arabia the difference is starker: Arabian Light has an API of 33 and sulphur content around 1.9% compared with Brent's 40 and 0.35% sulphur. Consequently Middle East crudes are likely to be discounted relatively to other origins in 2019-20 as refineries with the capacity to cut down the sulphur content are run at maximum and there will be limited demand for marginal barrels of heavy, sour crude. The relative relaxation of sanctions on trading Iranian oil could worsen the discount demanded on MENA grades as it will keep supplies of heavy and sour grades on the market.

Spreads between crudes are a characteristic of the market based on quality differentials. However, the impact of IMO 2020 could make a reasonably wide gap permanent as demand for higher sulphur grades drops off permanently.

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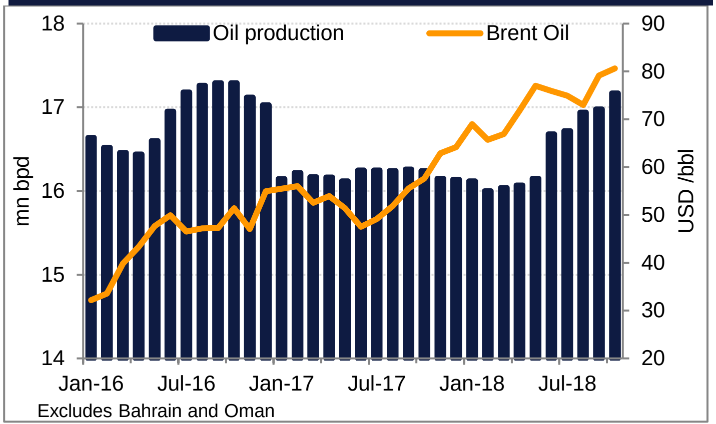
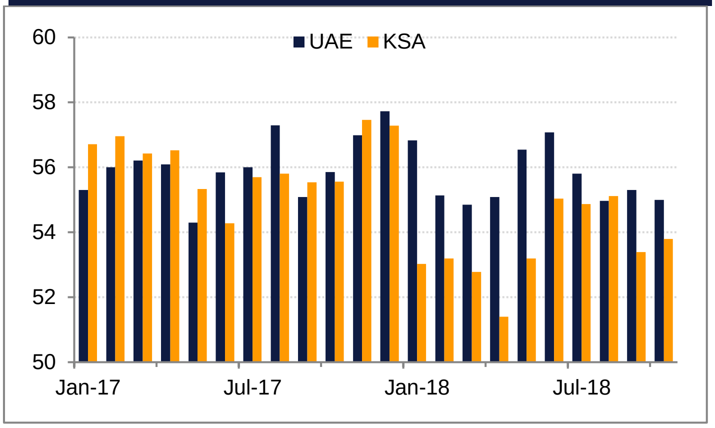
GCC in Pictures

GCC Oil Production and Oil Price



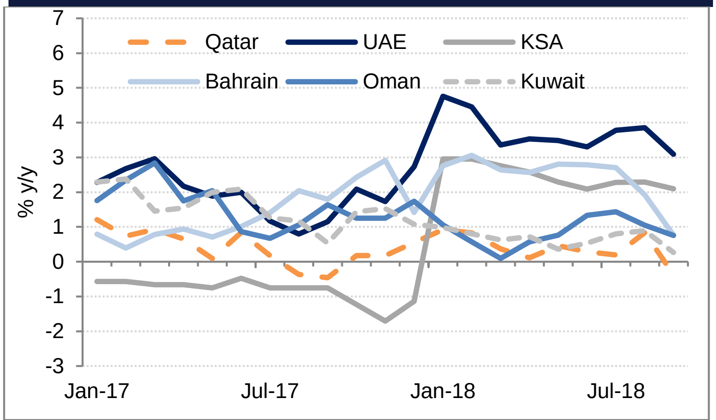
Source: Bloomberg, Emirates NBD Research

Purchasing Managers' Index



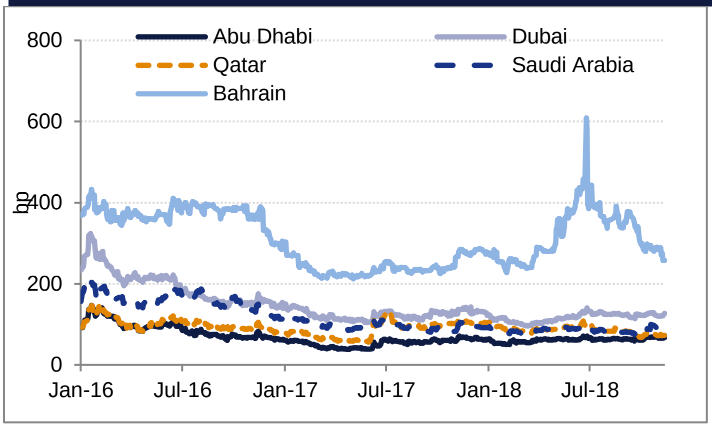
Source: IHS Markit, Emirates NBD Research

Inflation



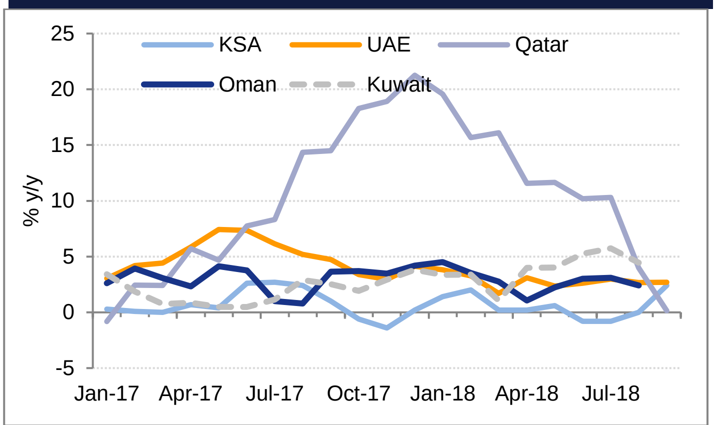
Source: Haver Analytics, Emirates NBD Research

CDS Spreads



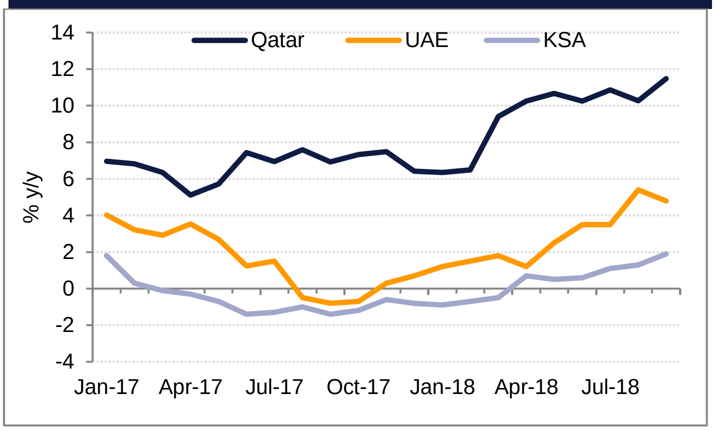
Source: Bloomberg

Money supply (ex Government. deposits)



Source: Haver Analytics, Emirates NBD Research

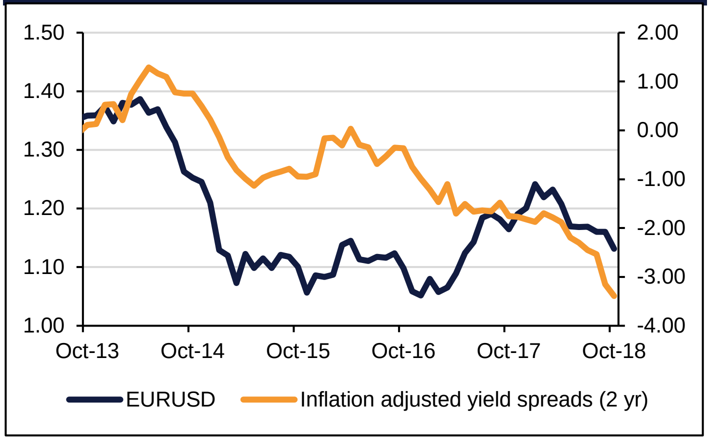
Private sector credit*



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

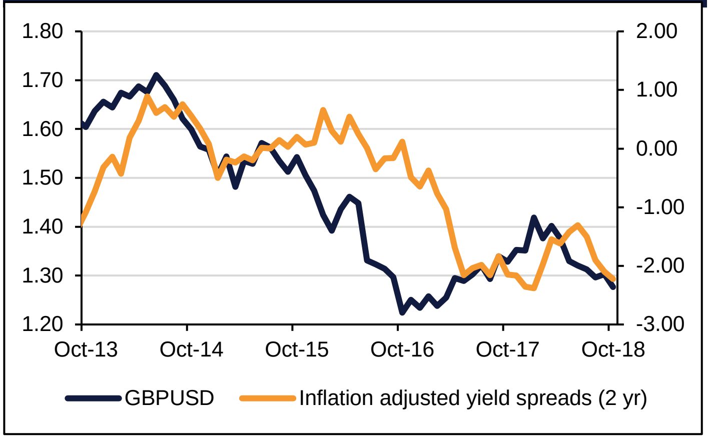
FX–Major Currency Pairs & Real Interest Rates

Interest Rate Differentials–EUR



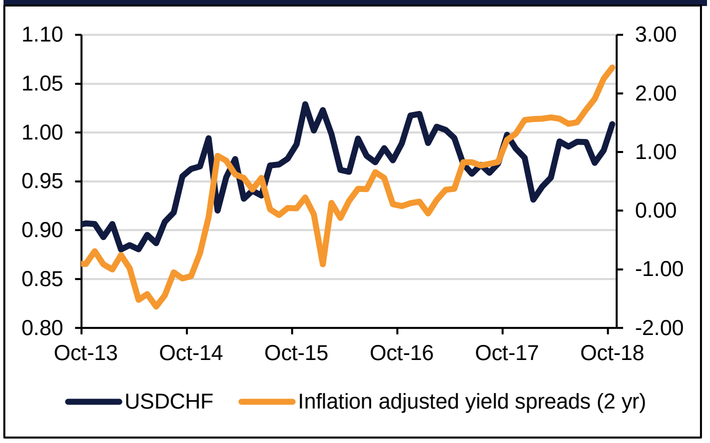
Source: Bloomberg, Emirates NBD Research

Interest Rate Differentials-GBP



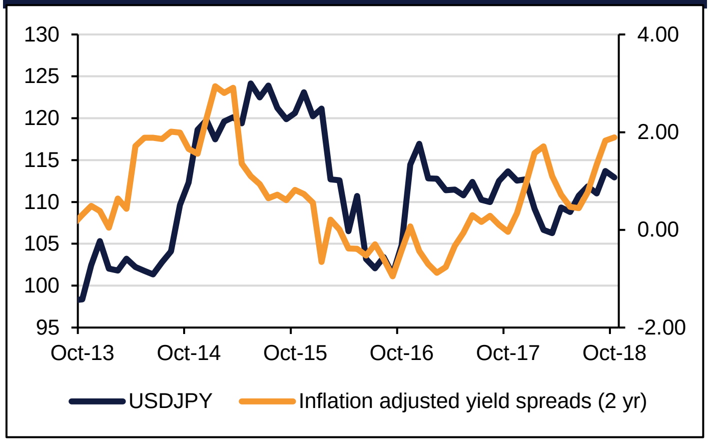
Source: Bloomberg, Emirates NBD Research

Interest Rate Differentials-CHF



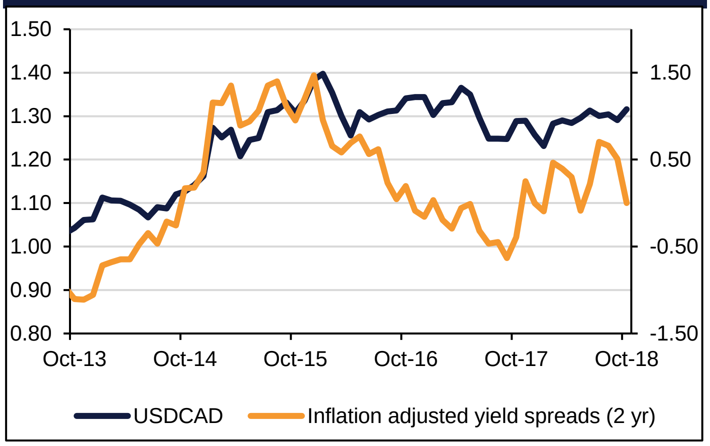
Source: Bloomberg, Emirates NBD Research

Interest Rate Differentials-JPY



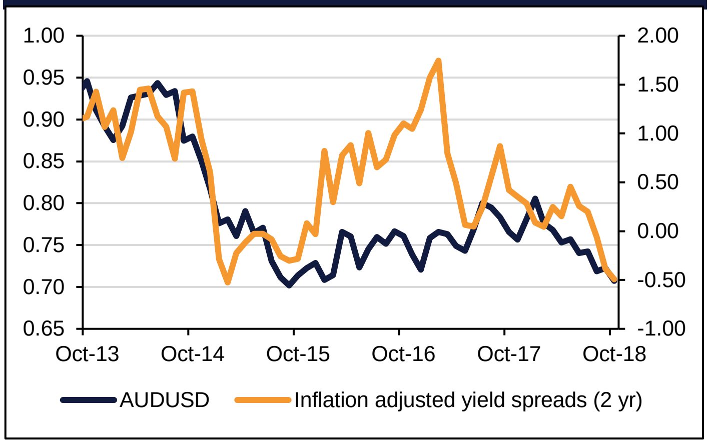
Source: Bloomberg, Emirates NBD Research

Interest Rate Differentials-CAD



Source: Bloomberg, Emirates NBD Research

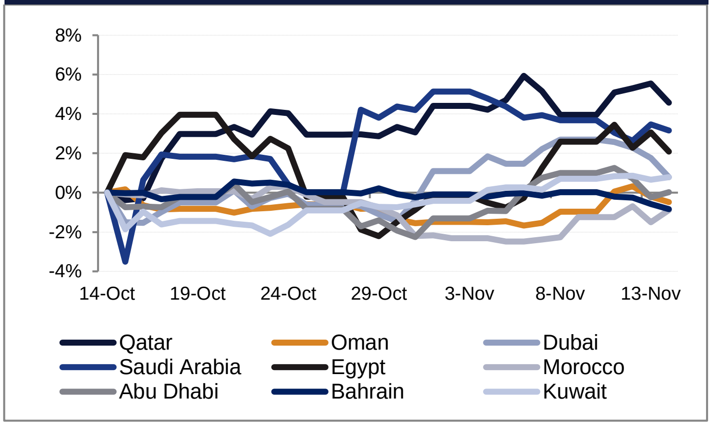
Interest Rate Differentials-AUD



Source: Bloomberg, Emirates NBD Research

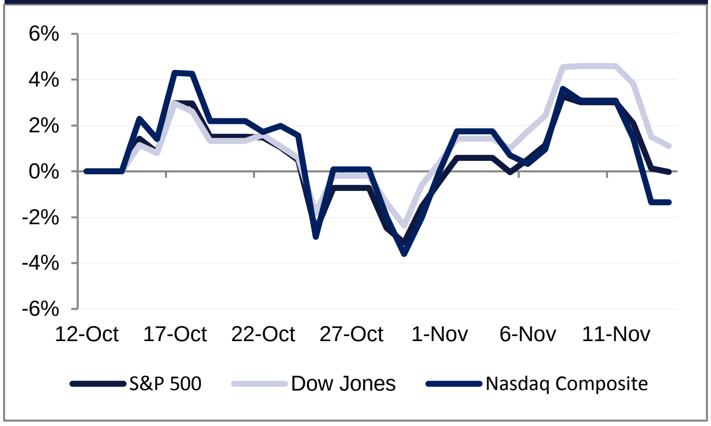
Major Equity Markets

MENA Equity Markets



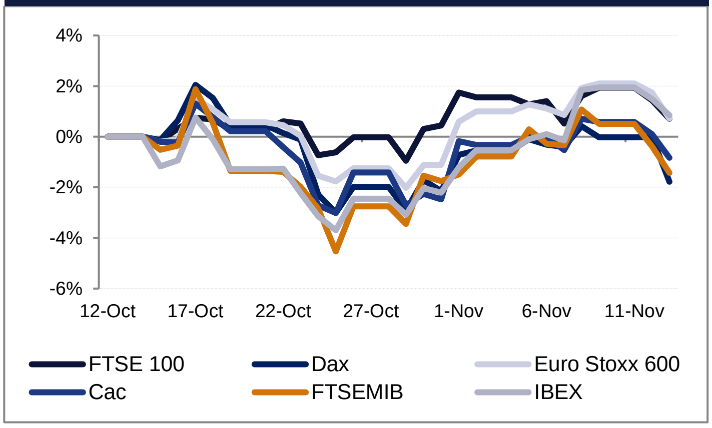
Source: Bloomberg, Emirates NBD Research

US Equity Markets



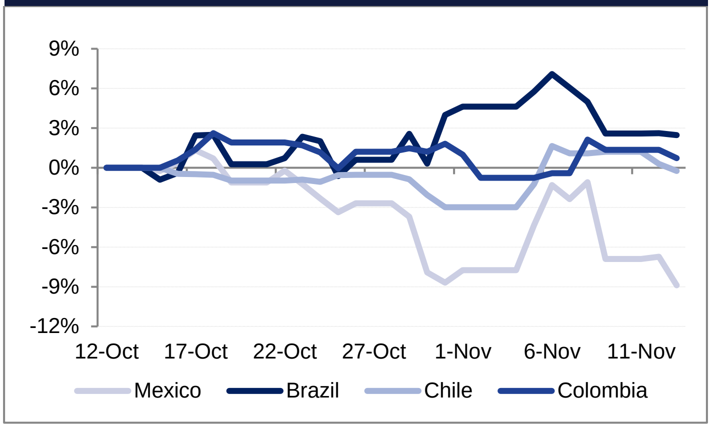
Source: Bloomberg, Emirates NBD Research

European Equity Markets



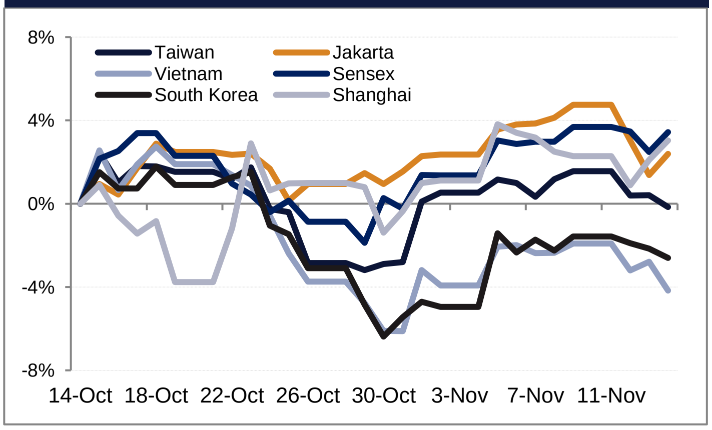
Source: Bloomberg, Emirates NBD Research

Latin American Equity Markets



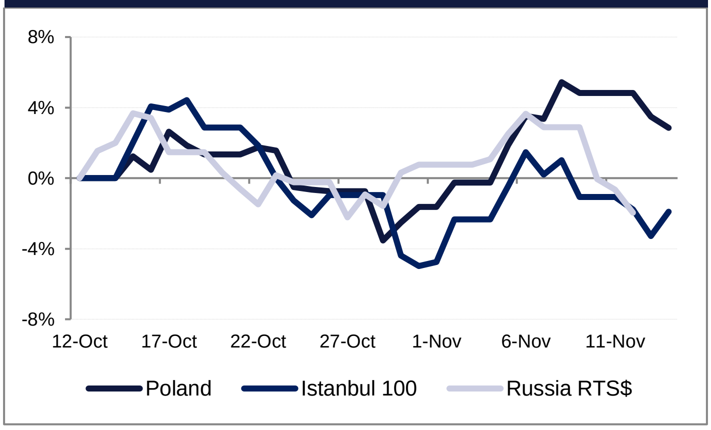
Source: Bloomberg, Emirates NBD Research

Asian Emerging Equity Markets



Source: Bloomberg, Emirates NBD Research

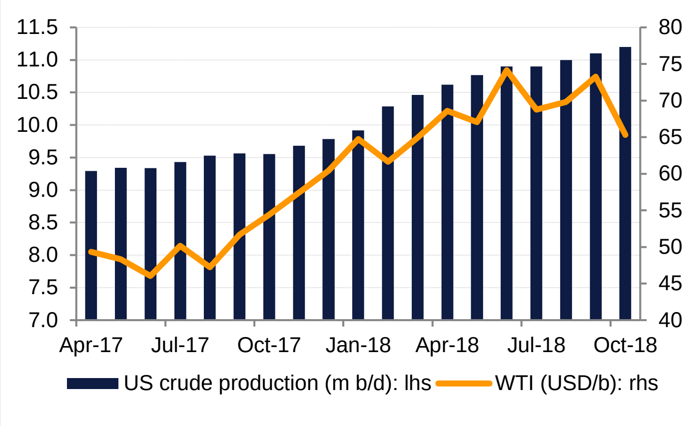
Emerging Europe Equity Markets



Source: Bloomberg, Emirates NBD Research

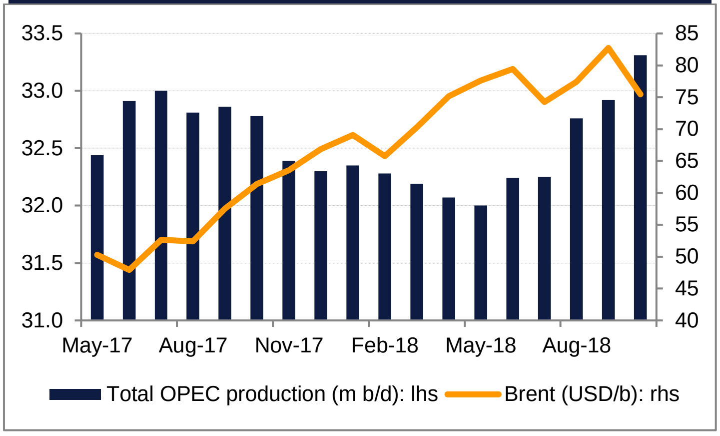
Major Commodities Markets

US oil production and price



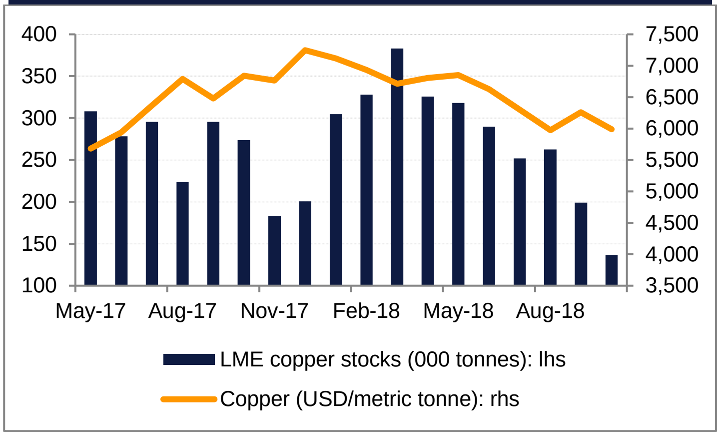
Source: EIKON, Emirates NBD Research

International oil production and price



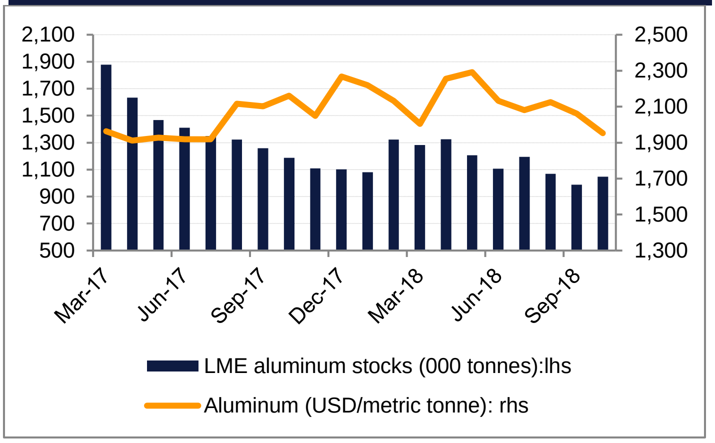
Source: EIKON, Emirates NBD Research

Copper stocks and price



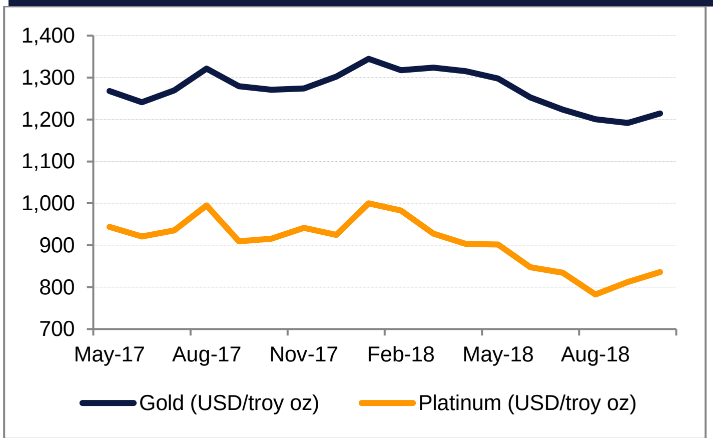
Source: EIKON, Emirates NBD Research

Aluminum stocks and price



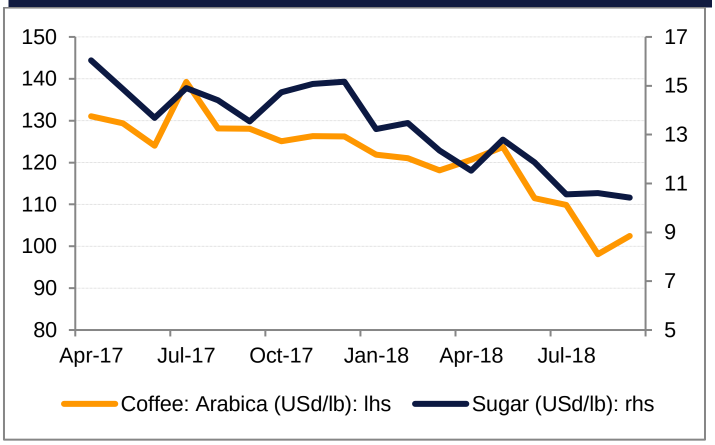
Source: EIKON, Emirates NBD Research

Precious metals prices



Source: EIKON, Emirates NBD Research

Agriculture prices



Source: EIKON, Emirates NBD Research

Key Economic Forecasts - GCC

United Arab Emirates	2015	2016	2017	2018f	2019f
Nominal GDP $bn	358.4	357.3	382.8	426.8	448.7
Real GDP %	5.1	3.0	0.8	2.2	3.6
Current A/C % GDP	4.7	2.4	3.6	7.1	6.9
Budget Balance % GDP	-3.4	-4.2	-2.6	1.3	2.2
CPI %	4.1	1.6	2.0	3.5	1.7
Saudi Arabia					
Nominal GDP $bn	654.3	644.9	683.8	769.2	803.0
Real GDP %	4.1	1.7	-0.7	2.0	2.4
Current A/C % GDP	-8.7	-3.7	2.2	9.1	9.1
Budget Balance % GDP	-15.8	-12.9	-9.3	-2.8	-3.6
CPI %	1.2	2.1	-0.8	2.5	2.0
Qatar					
Nominal GDP $bn	161.7	151.7	166.9	191.0	201.8
Real GDP %	3.4	1.8	1.1	3.1	3.6
Current A/C % GDP	8.5	-5.5	3.8	8.1	13.5
Budget Balance % GDP	-1.9	-9.0	-4.9	-0.7	0.0
CPI %	1.9	2.7	0.4	1.0	2.0
Kuwait					
Nominal GDP $bn	114.6	109.4	119.5	140.2	149.0
Real GDP %	0.6	2.9	-3.5	2.4	3.0
Current A/C% GDP	3.5	-4.6	6.3	14.3	15.3
Budget Balance % GDP	-13.4	-13.9	-9.0	0.4	2.8
CPI %	3.3	3.2	1.6	1.0	2.0
Oman					
Nominal GDP $bn	68.8	66.7	72.5	84.1	87.7
Real GDP %	4.7	5.4	1.0	2.6	3.6
Current A/C % GDP	-15.9	-18.5	-14.9	-3.6	-5.9
Budget Balance % GDP	-17.5	-20.6	-12.5	-5.5	-3.8
CPI %	0.1	1.1	1.6	1.0	3.0
Bahrain					
Nominal GDP $bn	31.1	32.2	35.3	38.9	41.0
Real GDP %	2.9	3.2	3.9	2.9	3.4
Current A/C % GDP	-2.4	-4.6	-3.9	-1.6	-0.4
Budget Balance % GDP	-13.0	-13.5	-11.4	-8.0	-5.9
CPI %	1.8	2.8	1.4	2.5	3.0
GCC (Nominal GDP weighted avg)					
Nominal GDP $bn	433	429	454	508	530
Real GDP %	4.0	2.4	-0.1	2.2	3.0
Current A/C % GDP	-2.4	-3.1	2.1	8.0	8.6
Budget Balance % GDP	-10.8	-10.6	-7.2	-1.5	-1.2
CPI %	2.2	2.1	0.4	2.4	2.0

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	223.0	236.5	276.8
Real GDP %	4.4	4.3	4.2	5.3	5.5
Current A/C % GDP	-3.7	-6.0	-6.5	-2.5	-2.4
Budget Balance % GDP	-11.43	-12.05	-10.96	-9.42	-8.82
CPI %	10.4	13.7	29.6	15.0	12.0
Jordan					
Nominal GDP $bn	37.5	38.7	40.3	41.7	43.2
Real GDP %	2.4	2.0	2.0	2.2	2.6
Current A/C % GDP	-9.1	-9.5	-10.7	-8.1	-7.4
Budget Balance % GDP	-3.4	-3.2	-2.7	-3.0	-2.7
CPI %	-0.9	-0.8	3.3	5.2	3.8
Lebanon					
Nominal GDP $bn	50.1	51.1	57.6	63.0	67.5
Real GDP %	0.8	1.0	1.2	1.4	1.8
Current A/C % GDP	-17.0	-20.5	-21.5	-19.9	-19.6
Budget Balance % GDP	-8.0	-9.8	-6.9	-9.4	-9.6
CPI %	-3.8	-0.8	4.5	7.0	5.5
Morocco					
Nominal GDP $bn	101.3	103.3	109.6	118.7	122.6
Real GDP %	4.5	1.1	4.1	3.0	2.7
Current A/C % GDP	-4.2	-3.6	-3.5	-3.3	0.0
Budget Balance % GDP	-4.5	-4.2	-3.5	-3.3	-2.8
CPI %	1.6	1.6	0.8	2.2	1.9
Tunisia					
Nominal GDP $bn	43.0	41.7	39.0	40.3	41.5
Real GDP %	1.1	1.0	1.7	2.7	2.9
Current A/C % GDP	-8.9	-8.9	-10.5	-9.7	-8.8
Budget Balance % GDP	-4.8	-6.2	-6.3	-4.6	-4.4
CPI %	4.9	3.7	5.3	7.5	6.9
Oil Importers (GDP weighted avg)					
Nominal GDP $bn	224.3	223.9	145.3	154.6	180.9
Real GDP %	3.71	3.05	3.40	3.82	4.02
Current A/C % GDP	-5.7	-7.3	-8.3	-6.0	-4.8
Budget Balance % GDP	-8.8	-9.4	-7.6	-7.0	-6.8
CPI %	6.4	8.5	15.5	9.5	7.9

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

Key Economic Forecasts – Non-GCC Oil Exporters

Algeria	2015	2016	2017e	2018f	2019f
Nominal GDP $bn	166.5	160.2	165.6	165.1	170.0
Real GDP %	3.7	3.3	1.6	2.4	2.9
Current A/C % GDP	-12.9	-12.3	-13.2	-8.5	-7.2
Budget Balance % GDP	-15.3	-13.1	-6.6	-7.0	-6.1
CPI %	4.4	5.8	6.0	4.0	5.3
Iran					
Nominal GDP $bn	419.6	441.8	433.9	424.8	465.5
Real GDP %	-1.4	12.4	3.3	-1.9	-4.0
Current A/C % GDP	0.3	3.7	3.6	0.3	-2.5
Budget Balance % GDP	-5.2397	-4.7704	-5.1316	-5.6419	-7.9395
CPI %	15.8	8.7	10.0	22.0	26.0
Iraq					
Nominal GDP $bn	164.2	165.2	184.6	214.7	242.8
Real GDP %	4.0	11.0	-0.3	3.5	4.3
Current A/C% GDP	2.5	1.7	1.7	4.4	4.8
Budget Balance % GDP	-13.0	-14.5	-6.6	-4.4	-4.0
CPI %	1.2	1.3	0.7	0.5	2.4
Libya					
Nominal GDP $bn	34.4	43.6	63.3	78.4	92.3
Real GDP %	-0.1	-6.9	34.8	8.1	9.6
Current A/C% GDP	-9.4	-10.2	-9.5	-8.6	-8.7
Budget Balance % GDP	-21.8	-18.1	-10.6	-4.2	-4.0
CPI %	9.5	9.5	25.0	11.5	10.0
Oil Exporters (GDP weighted avg)					
Nominal GDP $bn	300.0	312.4	299.5	294.2	322.5
Real GDP %	0.8	9.0	5.0	1.3	0.4
Current A/C % GDP	0.4	0.6	-1.0	-1.8	-3.1
Budget Balance % GDP	-6.2	-7.9	-7.9	-6.6	-6.4
CPI %	9.7	6.1	8.0	12.8	15.1

Key Economic Forecasts - Global

US	2014	2015	2016	2017	2018f	2019f
Real GDP %	2.6	2.9	1.5	2.2	2.7	2.5
Current A/C % GDP	-2.1	-2.4	-2.4	-2.3	-3.0	-2.5
Budget Balance % GDP	-2.7	-2.6	-3.1	-3.4	-3.5	-4.7
CPI %	1.6	0.1	1.3	2.1	2.5	2.3
Eurozone						
Real GDP %	1.3	2.1	1.8	2.4	2.3	1.8
Current A/C % GDP	2.4	3.2	3.3	3.5	2.8	3.2
Budget Balance % GDP	-2.5	-2.0	-1.5	-0.9	-1.6	-0.9
CPI %	0.4	0.0	0.2	1.5	1.5	1.7
UK						
Real GDP %	3.1	2.3	1.9	1.7	1.5	1.5
Current A/C% GDP	-5.3	-5.2	-5.8	-3.9	-3.3	-3.3
Budget Balance % GDP	-5.3	-4.1	-2.9	-1.8	-2.8	-1.8
CPI %	1.5	0.0	0.7	2.7	2.6	2.1
Japan						
Real GDP %	0.4	1.4	0.9	1.8	1.2	1.0
Current A/C % GDP	0.8	3.1	3.8	4.0	3.5	3.8
Budget Balance % GDP	-7.7	-6.7	-5.7	-3.5	-4.8	-3.8
CPI %	2.7	0.8	-0.1	0.5	1.0	1.1
China						
Real GDP %	7.3	6.9	6.7	6.9	6.5	6.3
Current A/C % GDP	2.3	2.8	1.8	1.3	1.3	0.6
Budget Balance %GDP	-1.8	-3.4	-3.8	-3.7	-3.5	-3.5
CPI%	2.0	1.4	2.0	1.6	2.2	2.3
India*						
Real GDP%	6.4	7.4	8.2	7.1	7.3	7.8
Current A/C% GDP	-1.4	-1.1	-0.6	-1.5	-2.0	-2.8
Budget Balance % GDP	-4.3	-3.5	-3.7	-3.9	-3.5	-3.3
CPI %	6.7	4.9	5.0	3.3	3.9	4.6

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

FX Forecasts

	FX Forecasts - Major					Forwards		
	2-Nov	Q4 2018	Q1 2019	Q2 2019	Q3 2019	3m	6m	12m
EUR/USD	1.1236	1.1300	1.1500	1.1800	1.2000	1.1335	1.1426	1.1626
USD/JPY	114.14	114.00	116.00	114.00	112.00	113.19	112.33	110.42
USD/CHF	1.0109	1.0000	1.0000	0.9800	0.9700	1.0011	0.9922	0.9730
GBP/USD	1.2901	1.3000	1.3500	1.4000	1.4400	1.2966	1.3024	1.3151
AUD/USD	0.7197	0.7300	0.7550	0.7700	0.8000	0.7206	0.7217	0.7247
NZD/USD	0.6741	0.6800	0.6900	0.7100	0.7400	0.6750	0.6761	0.6787
USD/CAD	1.3235	1.3000	1.2650	1.2600	1.2500	1.3211	1.3192	1.3157
EUR/GBP	0.8709	0.8692	0.8519	0.8429	0.8333	0.8742	0.8772	0.8841
EUR/JPY	128.25	128.82	133.40	134.52	134.40	128.25	128.25	128.25
EUR/CHF	1.1358	1.1300	1.1500	1.1564	1.1640	1.1347	1.1336	1.1312
	FX Forecasts - Emerging					**Forwards**		
	2-Nov	**Q4 2018**	**Q1 2019**	**Q2 2019**	**Q3 2019**	**3m**	**6m**	**12m**
USD/SAR*	3.7512	3.7500	3.7500	3.7500	3.7500	3.7512	3.7518	3.7555
USD/AED*	3.6730	3.6730	3.6730	3.6730	3.6730	3.6737	3.6743	--
USD/KWD	0.3045	0.3020	0.3020	0.3020	0.3020	0.3015	0.2995	--
USD/OMR*	0.3848	0.3850	0.3850	0.3850	0.3850	0.3855	0.3861	0.3879
USD/BHD*	0.3770	0.3770	0.3770	0.3770	0.3770	0.3761	0.3761	0.3791
USD/QAR*	3.6523	3.6400	3.6400	3.6400	3.6400	3.6523	3.6530	3.6547
USD/EGP	17.9568	18.0000	18.1250	18.2500	18.2500	18.3850	18.8800	19.8800
USD/INR	72.629	71.000	72.000	69.000	68.000	73.3500	74.1300	75.6300
USD/CNY	6.9587	6.9000	7.0000	7.1000	7.2000	6.9605	6.9605	7.0155
USD/SGD	1.3832	1.3500	1.3200	1.3000	1.2900	1.3801	1.3765	1.3686

Data as of 13 November 2018
Source: Bloomberg, Emirates NBD Research

Interest Rate Forecasts

USD Swaps Forecasts					Forwards		
	Current	3M	6M	12M	3M	6M	12M
2y	3.10	3.30	3.35	3.40			
10y	3.23	3.43	3.45	3.35			
2s10s (bp)	13	13	10	-5			
US Treasuries Forecasts					US Treasuries Forecasts		
2y	2.89	3.10	3.15	3.20			
10y	3.16	3.35	3.35	3.20			
2s10s (bp)	27	25	20	0			
3M Libor					3M Libor		
3m	2.61	2.85	3.10	3.35			
3M Eibor					3M Eibor		
3m	2.71	3.00	3.25	3.55			
Policy Rate Forecasts							
	Current %	3M	6M	12M			
FED (Upper Band)	2.25	2.50	2.75	3.00			
ECB	0.00	0.00	0.00	0.25			
BoE	0.75	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)	6.50	6.50	6.50	6.75			
SAMA (reverse repo)	2.25	2.50	2.75	3.00			
UAE (1W repo)	2.50	2.75	3.00	3.25			
CBK (o/n repo rate)	2.25	2.50	2.75	3.00			
QCB (repo rate)	2.50	2.75	3.00	3.25			
CBB (o/n depo)	2.25	2.50	2.75	3.00			
CBO (o/n repo)	2.72	2.97	3.25	3.55			
CBE (o/n depo)	16.75	16.75	15.75	14.75			

Source: Bloomberg, Emirates NBD Research

Commodity Forecasts

Global commodity prices							
	Last	2019Q1	Q2	Q3	Q4	2018	2019
Energy							
WTI	58.71	65.00	65.00	67.50	68.00	66.32	66.38
Brent	68.83	78.00	75.00	70.00	70.00	73.76	73.25
Precious metals							
Gold	1,198.30	1,300.00	1,350.00	1,350.00	1,380.00	1,281.83	1,345.00
Silver	14.03	15.00	15.25	15.50	15.00	15.80	15.19
Platinum	844.80	850.00	900.00	950.00	950.00	872.18	912.50
Palladium	1,106.68	1,000.00	1,050.00	1,150.00	1,150.00	989.84	1,087.50
Base metals							
Aluminum	1942.00	2,050.00	2,150.00	2,150.00	2,250.00	2,119.69	2,150.00
Copper	6049.00	6,500.00	7,000.00	7,250.00	7,500.00	6,553.44	7,062.50
Lead	1929.00	2,165.96	2,312.58	2,385.26	2,457.64	2,259.32	2,330.36
Nickel	11,400.00	13,000.00	12,500.00	12,250.00	11,850.00	13,552.07	12,400.00
Tin	19,265.00	21,000.00	20,750.00	20,750.00	20,500.00	20,219.32	20,750.00
Zinc	2,496.50	2,579.80	2,744.51	2,825.87	2,906.75	2,857.12	2,764.23

Prices as of 13 November 2018. Note: prices are average of time period unless indicated otherwise.
Source: EIKON, Emirates NBD Research

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