Global equities reach record highs; higher oil prices and easing austerity boost the Gulf region

Key market indicators

Stock markets	Index	Change (%) weekly	Change (%) YTD
Regional			
Abu Dhabi SM	4,548	3.41	3.41
Bahrain ASI	1,312	0.48	0.48
Dubai FM	3,464	2.77	2.77
Egypt EGX 30	14,782	-1.56	-1.56
S&P GCC 40	1,007	3.41	2.31
Kuwait SE	6,454	0.72	0.72
KSA Tadawul	7,277	0.64	0.64
Muscat SM 30	5,105	1.14	1.14
Qatar Exchange	8,631	1.23	1.23
International			
CSI 300	4,139	2.68	2.68
DAX	13,320	3.11	3.11
DJIA	25,296	2.33	2.33
Euro Stoxx 50	3,608	2.96	2.96
FTSE 100	7,724	0.47	0.47
Nikkei 225	23,715	4.17	4.17
S&P 500	2,743	2.60	2.60

Commodities	$/unit	Change (%) weekly	Change (%) YTD
Brent crude	67.6	1.12	1.12
KEC	64.76	1.98	1.98
WTI	61.4	1.69	1.69
Gold	1320.3	1.07	1.07

Exchange rates	Rate	Change (%) weekly	Change (%) YTD
KWD per USD	0.301	-0.06	-0.06
KWD per EUR	0.355	0.00	0.00
USD per EUR	1.203	0.27	0.27
JPY per USD	113.060	0.35	0.35
GBP per USD	1.357	0.41	0.41
EGP per USD	17.660	-0.39	-0.39

Interbank rates	%	Change (bps) weekly	Change (bps) YTD
Bhibor - 3 month	2.73	0.0	0.0
Kibor - 3 month	1.88	0.0	0.0
Qibor - 3 month	2.63	-11.6	-11.6
Eibor - 3 month	1.77	-3.3	-3.3
Saibor - 3 month	1.90	-0.2	-0.2
Libor - 3 month	1.70	0.9	1.0

Bond yields	%	Change (bps) weekly	Change (bps) YTD
Regional			
Abu Dhabi 2022	2.93	-2.0	-2.0
Dubai 2022	3.03	-11.4	-11.4
Qatar 2022	3.14	6.0	6.0
Kuwait 2022	2.85	4.0	4.0
Saudi Arabia 2023	3.20	-2.0	-2.0
International			
UST 10 Year	2.48	6.5	6.5
Bunds 10 Year	0.44	1.6	1.6
Gilts 10 Year	1.25	5.8	5.8
JGB 10 Year	0.06	0.9	0.9

Source: Thomson Reuters Datastream; as of Friday's close 5/1/2018

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

Overview

The mood of optimism helped propel global equities to fresh highs last week, with the Dow hitting 25,000 on the positive outlook for US economic growth and the impact of the Trump tax cuts. Based upon futures prices, the odds of a 25 bps Fed interest rate hike in March have risen to around 67%, in what would be the first of 2-4 rate increases expected by analysts for 2018.

After rallying some 18% in 2017, Brent crude oil prices started 2018 in similarly bullish fashion, edging up $1 to reach $68 for the first time in three years and closing in on levels not seen since prices crashed in 2014. On top of solid global demand growth and OPEC/non-OPEC supply cuts that are slowly tightening market fundamentals, recent unrest in Iran has raised concerns over supply stability in OPEC's third largest producer, particularly if it triggers a reinstatement of US sanctions on Iran's oil industry. Crude prices have also benefited from a slightly softer US dollar.

The climb in oil prices has benefited the mood in the Gulf region, where most equity markets enjoyed decent gains in December including a 10% rally in the Qatari market that saw it recover around one-third of its losses since the start of the diplomatic dispute. Against a backdrop of stronger oil revenues, there were also further signs of an easing in the pace of fiscal austerity across the region, with Oman's government announcing a 7% increase in budgeted spending for 2018 despite its still precarious fiscal position and recent ratings downgrades.

International macroeconomics

USA: The pace of employment growth was slower in December, with non-farm payrolls increasing by a lower-than-expected 148,000. Nonetheless, this follows two strong months, with the 3-month average remaining quite solid at 204,000, the highest figure recorded in 2017. The employment report also showed wage growth somewhat stronger, rising to 2.5% y/y on a healthy 0.3% rise during the month. (Chart 1.)

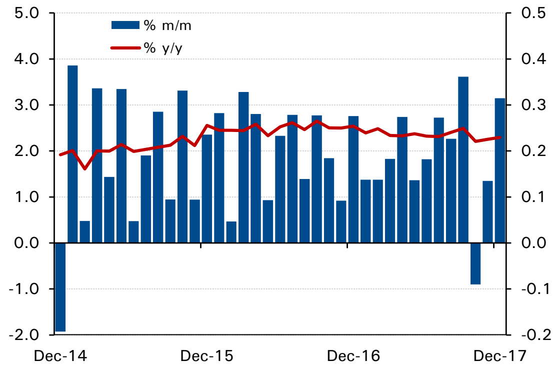
The minutes from the December FOMC meeting indicate that the Fed remains less concerned with the softer inflation data, especially with a tightening labor market. Members also indicated they believe the recent tax cuts should provide a further boost to the economy. Markets expect that a rate hike in March is likely, with the CME Group reporting a probability at 67%.

Meanwhile, economic activity continues to show strength. The ISM manufacturing index exceeded expectations in December, rising to 59.7, with new orders coming in exceptionally strong. In further signs of strength, the survey shows inventories being drawn down and delivery times increasing. The ISM non-manufacturing index slipped, but at 55.9 remains quite solid.

Eurozone: December's flash eurozone headline inflation came in as expected at 1.4% y/y, down from November's 1.5%. Core inflation remained at 0.9%. (Chart 2.) Overall, inflation seems to be steadying below the 2% target, supporting the ECB's case for a careful retreat from

Chart 1: US wage growth

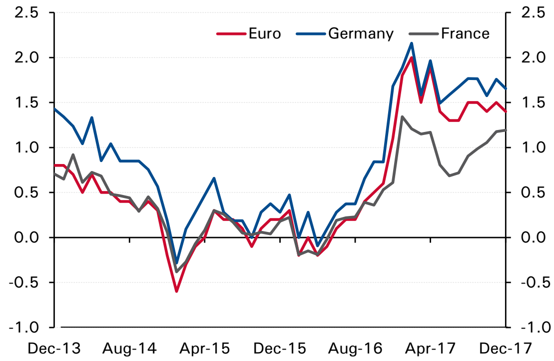
(%)



Source: U.S. Bureau of Labor Statistics

Chart 2: EZ inflation

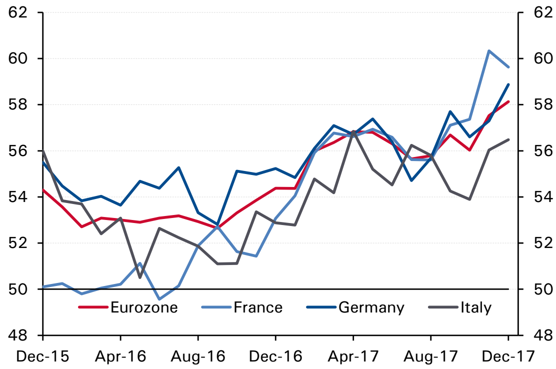
(% y/y)



Source: Thomson Reuters Datastream

Chart 3: Eurozone PMIs

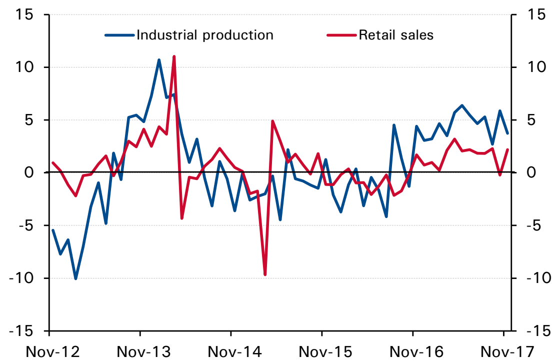
(index)



Source: IHS Markit

Chart 4: Japan industrial production & retail sales

(% y/y)



Source: Thomson Reuters Datastream

monetary easing. Meanwhile, the eurozone's December PMI was confirmed at 58.1, its strongest reading in almost 7 years, supported by a healthy pick-up in Germany. (Chart 3.) This and other strong consumer-related data helped European equities. The euro finished the week above 1.20.

Japan: Industrial activity continued to hold up reasonably well in November, growing at a better-than-expected 3.7% y/y (chart 4), mainly thanks to strength in exports, which rose by an impressive 16.2% y/y. (Chart 5.) Growth in exports has been fueled by a weaker yen as well as a steady improvement in global demand. Retail sales remained subdued, but continues to show signs of a recovery. In November, sales witnessed a rebound, growing by 2.2% y/y. (Chart 4.)

GCC & regional macroeconomics

Kuwait: Inflation rose slightly to 1.5% y/y in November, predominantly driven by price rises of some retail goods and services. (Chart 6.) Inflation has remained subdued, held back by deflationary pressures in housing rents and a slow pick-up in food and beverage prices. However, inflation excluding housing rent, food and energy prices has been stronger, rising to 3.4% y/y in November.

The value of awarded projects dropped to KD 3.6 billion in 2017, a 36% drop from 2016. (Chart 7.) 2016 had benefitted from a steady supply of transport sector awards that slowed in 2017. Last year also witnessed some delays that affected project activity. The KD 800 million Al-Zour North 2 independent power and water project (IWPP) was cancelled in in August, in a setback for public-private partnership (PPP) in general. Other PPP projects were delayed as a result, including further Al-Zour IWPP phases and Khiran IWPP; nonetheless, there was some progress, particularly the award of the KD 235 million Kabd municipal solid waste PPP project.

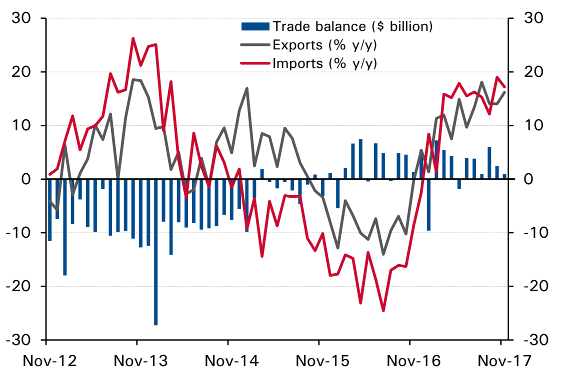
Saudi Arabia: On 1 January, the Saudi government introduced a VAT (5%) for the first time. In doing so, the authorities activated one of their more significant Vision 2030-mandated non-oil revenue earners, estimated at SR 22 billion ($5.9 billion, or 1.5% of non-oil GDP). On the same day, the authorities also rolled out a second round of energy price rises and utility tariff increases.

However, last weekend, after disgruntled citizens took to social media to complain about the double hit to their pockets, King Salman reinstated annual pay rises for Saudi civil servants, ordered a SR 5,000 bonus for Saudi military personnel involved in the Yemen conflict, and increased the government's monthly cost of living allowance for public sector workers by SR 1,000. Retirees, social benefits recipients and students were also among those benefitting from the additional allowances. The handouts could cost the state at least SR 50 billion this year (5% of the 2018 budget), a royal court official noted.

The government reportedly arrested 11 princes over the weekend for staging an anti-austerity protest at the royal palace. The princes had rejected the state's move by royal decree to stop paying royal family members' electricity and water bills.

The Saudi headline PMI continued to signal an improvement in non-oil private sector activity, registering 57.3 in December 2017. (Chart 8.) Despite a slight easing in the headline rate from the previous month, Saudi businesses continued to report sharp expansions in output, new orders and new export orders. Payroll numbers also continued to expand, although

Chart 5: Japan international trade



Source: Thomson Reuters Datastream

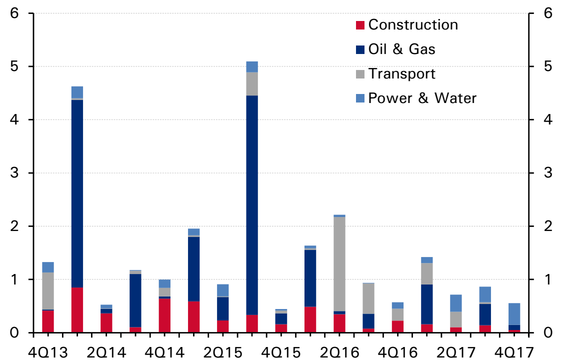
Chart 6: Kuwait CPI inflation

(% y/y)

Source: Central Statistical Bureau

Chart 7: Kuwait awarded projects

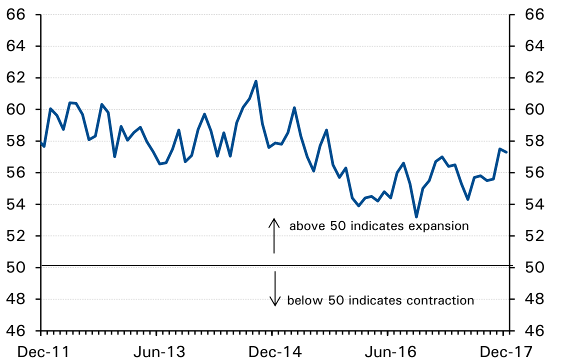
(KD billion)



Source: Central Statistical Bureau

Chart 8: Saudi PMI

(index)



Source: Markit/Emirates NBD

the pace of growth has slowed considerably, firms reported.

Saudi Aramco has changed its legal status to that of a joint-stock company ahead of its potential IPO this year. An 11-member board of directors has also been established, with over half (6) nominated by the government.

UAE: The non-oil sector continues to steadily improve. The headline PMI edged up from 57.0 in November to an almost three-year high of 57.7 in December, thanks to a rebound in export orders and as both new orders and output remained firm. (Chart 9.) Export orders came in at a multi-month high of 53.3, thanks in part to a weaker currency and an improvement in global demand. New orders jumped from 60.2 in November to 64.8 in December, while output remained robust at 60.7, as domestic conditions held firm and consumers ramped-up purchases ahead of the introduction of the VAT on 1 January 2018.

Qatar: Qatari GDP surprised to the upside in 3Q17, suggesting that the diplomatic dispute had a less severe initial impact on activity than previously feared. GDP growth rebounded to 1.9% y/y from 0.3% in Q2, despite being the first full quarter of the diplomatic dispute that began in early June. (Chart 10.) Admittedly, the improvement was largely attributed to stronger mining sector output (+0.2% y/y versus -3.1% in Q2) – possibly linked to higher gas output due to the earlier commissioning of the Ras Laffan 2 condensate refinery. Non-oil growth ticked lower to 3.6% y/y, but given the impact on travel, trade, tourism and finance revealed in other official data, held up reasonably well. Although the data suggests that non-oil growth in 2017 will come in higher than the 3.5% we had forecast, we still expect it to drift slightly lower in 2018 as the diplomatic crisis rumbles on.

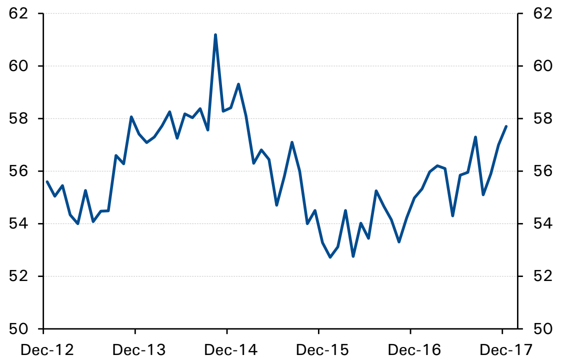
Oman: The government announced an expansionary budget for 2018, with a 7% increase in expenditures and a projected deficit of OMR 3 billion (10% of GDP). The government intends to increase project spending in 2018 and relax its subsidy bill. It has budgeted around OMR 2.8 billion for development and oil & gas investments, a 3% increase from the 2017 budget. Subsidies will also increase to OMR 765 million as the government implements hand-outs to help low-to-middle income individuals. Current expenditures are expected to grow by 6%, but this is due to a higher interest bill and defense spending and not wages. Meanwhile, revenue is expected to pick-up to OMR 9.5 million, on the back of a higher oil price and higher non-oil receipts. Oman has postponed the introduction of its VAT to 2019, though it expects to implement an excise tax in 2H18.

Ultimately, fiscal policy in 2018 may in our view be less expansionary than the budget implies, with spending likely to have overshot budget estimates last year. But we do expect a slightly larger deficit of OMR 3.5 billion (12% of GDP) than the government projects.

Egypt: The PMI fell to 48.3 in December, slipping back below the 50-mark after briefly rising above it in November. (Chart 11.) While the PMI has recovered noticeably over the last 18 months, it has yet to reflect the robust economic growth visible in other data. GDP figures show that growth picked up to a robust 5.2% y/y in 3Q17. While weakness was visible in all production components, employment was a bright spot in December, rising to its highest level in over two years. Meanwhile, inflationary pressures continued to ease.

The Central Bank of Egypt (CBE) kept policy rates unchanged at its 28 December monetary policy meeting. The CBE indicated that, though inflation had moderated, price pressures remained elevated. The robust

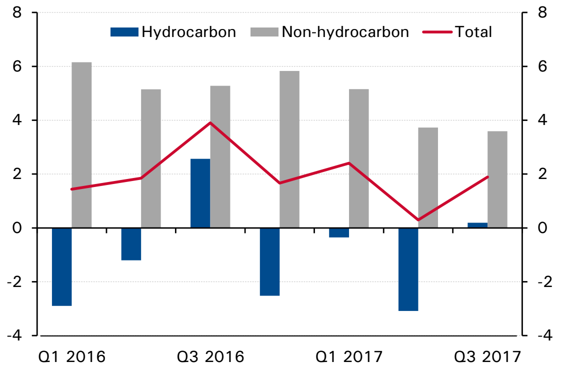
Chart 9: UAE Purchasing Managers' Index



Source: Markit

Chart 10 : Qatar GDP

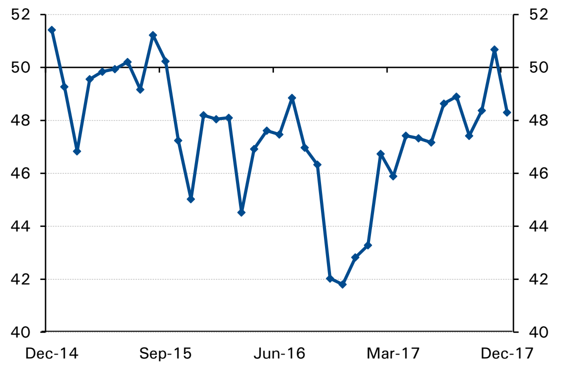
(% y/y)



Source: MDPS

Chart 11: Egypt PMI

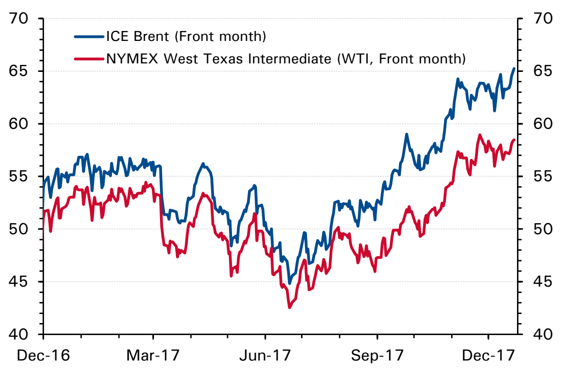
(index)



Source: IHS Markit

Chart 12: Benchmark crude oil prices

($/bbl)



Source: Thomson Reuters Datastream

recovery through 3Q17 reassured monetary authorities that high rates have not crimped growth, though the CBE made clear in its statement that rate cuts will hinge on data showing a "moderation of underlying inflationary pressures".

CBE reserves hit a historic high of $37 billion after rising $0.3 billion during December to an estimated 8.1 months of imports. Reserves have soared by $18 billion since the decision to float the currency in November 2016.

Markets – oil

Brent crude rose above $68/bbl last week for the first time since late 2014 as protests in Iran re-emphasized the geopolitical risk premium that the oil markets often command. In fact, oil prices had their best year-opening week since 2013, with Brent rising by 1.1% week-on-week (w/w) to $67.6/bbl and WTI increasing by 1.7% w/w to $61.4/bbl. (Chart 12.) Recent price increases also come on the back of supply outages associated with the closures in December of the Brent Forties pipeline in the North Sea due to a leak and a major pipeline in Libya due to sabotage.

With oil market fundamentals increasingly supportive of elevated oil prices – winter crude demand appears robust, supplies are being trimmed by OPEC and crude stockpiles are drawing down (-7.42 million barrels in the US last week) – investors appear increasingly bullish. Net long positions have reached a record.

Markets – equities

Most international markets finished the first week of 2018 higher after retreating in the final week of 2017. Investors, encouraged by the synchronized pick-up in global growth and further bolstered by the recent inflow of positive data, were bullish on equities, preparing for what they believe is another good year. As a result, MSCI's world index was up 2.5% on the week.

US equities plowed through new highs. The S&P 500 breached 2700 and was up 2.6% on the week, while the DJI broke through 25000, adding 1000 in record time and increasing by 2.3%. Meanwhile, hawkish statements about the end of the ECB's QE and strong consumer data saw investors leave European bonds in favor of equities. This pushed Euro Stoxx 50 up 3.0% on the week. Emerging markets were also up on Chinese gains, with MSCI's emerging market index up 3.0%. (Chart 13.)

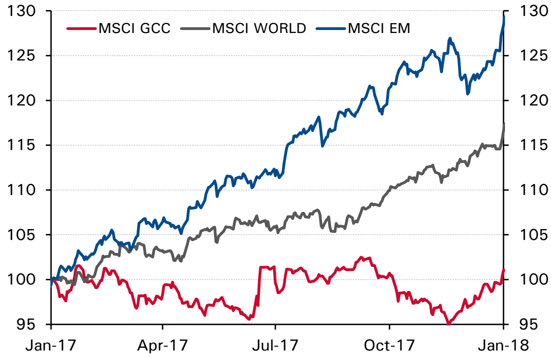
In the GCC, performance was positive across the board, supported by rising oil prices, but Saudi Arabia lagged. The MSCI GCC index was up 1.4% on the week. The Kingdom's stock market was held back by the increase in fuel prices, and was up a modest 0.6%. Abu Dhabi and Dubai, on the other hand, benefitted from bargain buying following renewed optimism over the UAE's economic prospects following strong PMI data. The ADX was up 3.4%, while the DFM climbed 2.8%. (Chart 14.)

Markets – fixed income

Benchmark yields reversed their recent decline, driven by year-end buying, on hawkish comments by ECB officials hinting at the end of the ECB's QE program, strong EZ consumer data, and healthy US data. (Chart 15.) Meanwhile, the Fed's minutes had little impact on bond markets. The release reiterated concern over the slow rise in inflation and a slow approach to raising rates. Fed policymakers also discussed the impact of recent tax changes. US 10-year Treasuries increased by 6.5 bps to 2.48%, while 10-year Bunds settled at 0.44%. GCC benchmark yields were mixed,

Chart 13: Total equity return indices

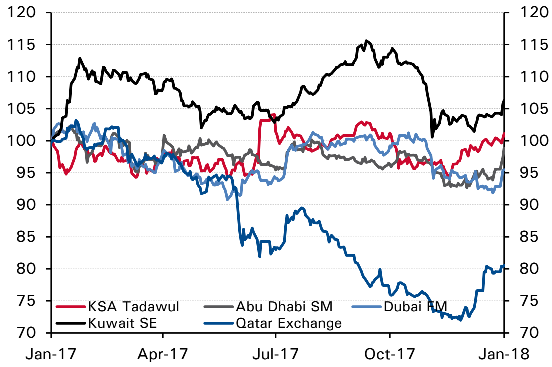
(rebased, 5 January 2017=100)



Source: Thomson Reuters Datastream

Chart 14: GCC equity markets

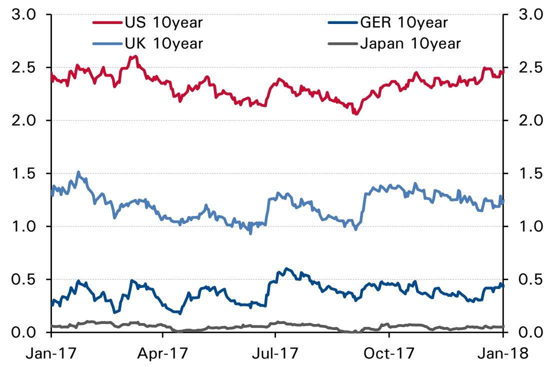
(rebased, 5 January 2017=100)



Source: Thomson Reuters Datastream

Chart 15: Global benchmark yields

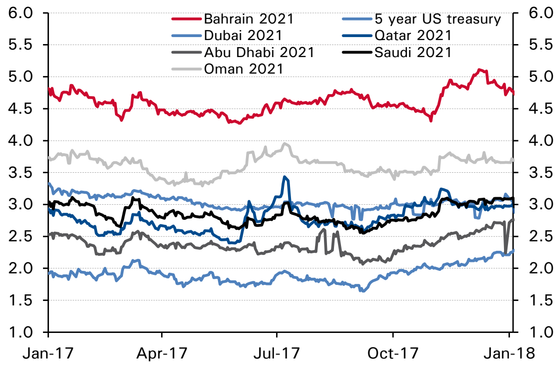
(%)



Source: Thomson Reuters Datastream

Chart 16: GCC yields

(%)



Source: Thomson Reuters Datastream

as higher oil prices offset the global sell-off in bonds. (Chart 16.)

In a bid to fund its deficit, Oman has hired banks to help issue a multi-tranche bond. Moody's assigned a provisional Baa2 rating for this new global medium-term note program.

Head Office

Kuwait
National Bank of Kuwait SAKP
Abdullah Al-Ahmed Street
P.O. Box 95, Safat 13001
Kuwait City, Kuwait
Tel: +965 2242 2011
Fax: +965 2259 5804
Telex: 22043-22451 NATBANK
www.nbk.com

International Network

Bahrain
National Bank of Kuwait SAKP
Zain Branch
Zain Tower, Building 401, Road 2806
Seef Area 428, P. O. Box 5290, Manama
Kingdom of Bahrain
Tel: +973 17 155 555
Fax: +973 17 104 860

National Bank of Kuwait SAKP
Bahrain Head Office
GB Corp Tower
Block 346, Road 4626
Building 1411
P.O. Box 5290, Manama
Kingdom of Bahrain
Tel: +973 17 155 555
Fax: +973 17 104 860

United Arab Emirates
National Bank of Kuwait SAKP
Dubai Branch
Latifa Tower, Sheikh Zayed Road
Next to Crown Plaza
P.O.Box 9293, Dubai, U.A.E
Tel: +971 4 3161600
Fax: +971 4 3888588

National Bank of Kuwait SAKP
Abu Dhabi Branch
Sheikh Rashed Bin Saeed
Al Maktoom, (Old Airport Road)
P.O.Box 113567,Abu Dhabi, U.A.E
Tel: +971 2 4199 555
Fax: +971 2 2222 477

Saudi Arabia
National Bank of Kuwait SAKP
Jeddah Branch
Al Khalidiah District,
Al Mukmal Tower, Jeddah
P.O Box: 15385 Jeddah 21444
Kingdom of Saudi Arabia
Tel: +966 2 603 6300
Fax: +966 2 603 6318

Jordan
National Bank of Kuwait SAKP
Amman Branch
Shareef Abdul Hamid Sharaf St
P.O. Box 941297, Shmeisani,
Amman 11194, Jordan
Tel: +962 6 580 0400
Fax: +962 6 580 0441

Lebanon
National Bank of Kuwait
(Lebanon) SAL
BAC Building, Justinien Street, Sanayeh
P.O. Box 11-5727, Riad El-Solh
Beirut 1107 2200, Lebanon
Tel: +961 1 759700
Fax: +961 1 747866

Iraq
Credit Bank of Iraq
Street 9, Building 187
Sadoon Street, District 102
P.O. Box 3420, Baghdad, Iraq
Tel: +964 1 7182198/7191944
+964 1 7188406/7171673
Fax: +964 1 7170156

Egypt
National Bank of Kuwait - Egypt
Plot 155, City Center, First Sector
5th Settlement, New Cairo
Egypt
Tel: +20 2 26149300
Fax: +20 2 26133978

United States of America
National Bank of Kuwait SAKP
New York Branch
299 Park Avenue
New York, NY 10171
USA
Tel: +1 212 303 9800
Fax: +1 212 319 8269

United Kingdom
National Bank of Kuwait
(International) Plc
Head Office
13 George Street
London W1U 3QJ
UK
Tel: +44 20 7224 2277
Fax: +44 20 7224 2101

National Bank of Kuwait
(International) Plc
Portman Square Branch
7 Portman Square
London W1H 6NA, UK
Tel: +44 20 7224 2277
Fax: +44 20 7486 3877

France
National Bank of Kuwait
(International) Plc
Paris Branch
90 Avenue des Champs-Elysees
75008 Paris
France
Tel: +33 1 5659 8600
Fax: +33 1 5659 8623

Singapore
National Bank of Kuwait SAKP
Singapore Branch
9 Raffles Place # 44-01
Republic Plaza
Singapore 048619
Tel: +65 6222 5348
Fax: +65 6224 5438

China
National Bank of Kuwait SAKP
Shanghai Representative Office
Suite 1003, 10th Floor, Azia Center
1233 Lujiazui Ring Road
Shanghai 200120, China
Tel: +86 21 6888 1092
Fax: +86 21 5047 1011

NBK Capital

Kuwait
NBK Capital
38th Floor, Arraya II Building, Block 6
Shuhada'a street, Sharq
PO Box 4950, Safat, 13050
Kuwait
Tel: +965 2224 6900
Fax: +965 2224 6904 / 5

United Arab Emirates
NBK Capital Limited - UAE
Precinct Building 3, Office 404
Dubai International Financial Center
Sheikh Zayed Road
P.O. Box 506506, Dubai
UAE
Tel: +971 4 365 2800
Fax: +971 4 365 2805

Associates

Turkey
Turkish Bank
Valikonagl CAD. 7
Nisantasi, P.O. Box. 34371
Istanbul, Turkey
Tel: +90 212 373 6373
Fax: +90 212 225 0353