The Week Ahead: US data important as debate on Fed hike timing intensifies

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US: PCE spending and inflation data in focus

Personal spending and PCE inflation data will be key releases this week, especially in light of the increased focus on inflation following the July FOMC minutes. Personal spending is forecast to have strengthened to 0.4% m-o-m in July, from 0.2% in June, on the back of solid retail spending. However, the PCE deflator is expected to moderate to 0.1% m-o-m in July, from 0.2% in June, on the back of weaker energy prices. The more bearish July minutes, in which the Fed expressed greater concern over low inflation, makes the interest rate liftoff in September a close call, though it remains our base case. The onus was put on further improvement in the data to warrant a rate hike. This is opposed to the earlier stance whereby data would have had to weaken in order to prevent the Fed from hiking in September. There has been some traction in economic data, pointing to a buildup in domestic demand, since the July meeting. Moreover, US data (ex-inflation) released last week generally surprised on the upside. However, the deterioration in the global outlook and the increased deflationary pressures (CNY weakening and the double dip in oil prices) have increased the risk of postponement. Separately, we expect further monetary loosening (RRR and interest rate cuts) by the PBoC in the coming weeks in order to support economic growth.

US: Jackson Hole Symposium and 2Q GDP also important

The Jackson Hole Symposium (27-29 August), focusing on the topic of Inflation Dynamics and Monetary Policy, will be watched closely for any comments. However, Fed Chair Janet Yellen will reportedly not be participating. Other important US data releases this week will be durable goods orders and the second estimate of 2Q GDP. The consensus expects GDP growth to be revised up by nearly a full percentage point to 3.2% q-o-q SAAR for 2Q (from 2.3% in the first reading), driven by stronger investment, inventory accumulation, and consumer expenditure. The upward revisions to May and June retail spending point to more robust consumer spending in 2Q, whilst investments were likely boosted by both residential and non-residential construction.

UAE: To announce September fuel prices on 28 August

In the UAE, the Ministry of Energy is to announce fuel prices for September on 28 August. This will be the second month in which prices are set by the ministry since they were partially deregulated in August. While no details have been given on the pricing mechanism, we believe that price changes in the coming months could be more gradual than the initial adjustment in August. Informal comments from Dr. Matar Al Nyadi, Undersecretary for the Ministry of Energy and Chair of the Fuel Price Committee, indicate that he expects both gasoline and diesel prices to decrease in September. This could indicate greater influence of market movements in setting prices, though gasoline prices remain lower than they would be if they were fully liberalised, in our view.

I. Recent Data and Events

A. MENA Economies

UAE: Inflation accelerates to 4.4% on higher food prices

Food price inflation expected to moderate in coming months

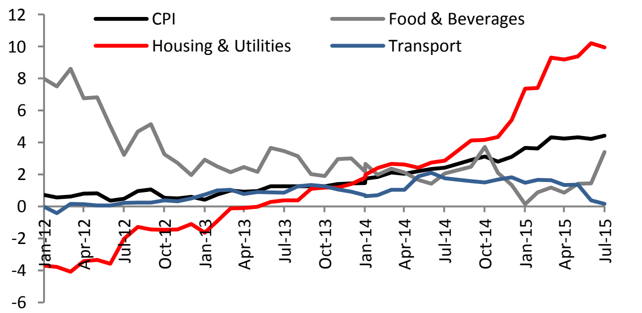
UAE inflation accelerated to 4.4% y-o-y in July, from 4.2% in June. The pickup was due largely to higher food prices, which we attribute to the Eid period. Food & beverage price growth strengthened to 3.4% y-o-y, up from 1.4% in June. The monthly data point to a weak buildup of inflation in other areas of the consumer basket, with most seeing zero or negligible price increases. Housing and utility inflation moderated to 0.1% m-o-m in July, from 0.8% in June. We believe that this could reflect the lower rental prices in Dubai. Given the strong USD and weak global food inflation, we expect food price inflation to moderate going forward.

August inflation should accelerate with increase in gasoline prices

More critical will be the impact of the partial liberalisation of fuel prices on headline inflation, which will begin to be reflected in the August inflation data. Please see our **Economic Research Weekly – Global Data Watch 3-7 August 2015**, published on 3 August 2015. We estimate that the higher gasoline prices in August could add around 1-1.3 ppt to headline inflation, though future changes to the price will be important to the inflation outlook. The Ministry of Energy is to announce the prices for September on 28 August. While no details of the mechanism for determining fuel price changes have been announced, we believe that price changes may be more gradual in the months following the initial (August) gasoline price increase. We continue to see the possibility of a rising trend for gasoline prices in the medium term, as UAE prices remain lower than they would be if they were fully liberalised, in our view.

Fig. 1. UAE: Higher food prices behind inflation acceleration in July

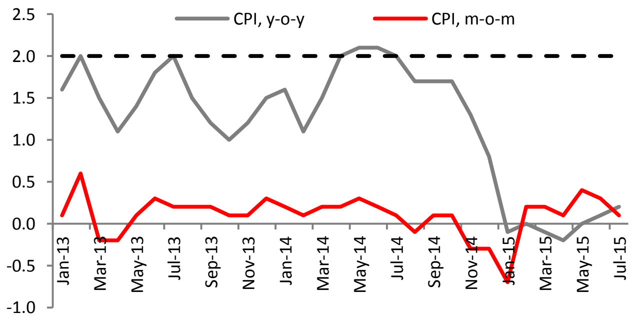
% change y-o-y



Source: National Bureau of Statistics

Fig. 2. US: Headline inflation moderates to three-month low (m-o-m), led by deceleration in energy price growth

% change



Source: Bloomberg

Further fiscal reforms expected, including VAT

With oil prices expected to remain weak into the medium-term, we foresee further fiscal reforms. The UAE has said that it is reviewing its taxation system, including studying the impact of the introduction of corporate tax and VAT. However, issues in agreeing VAT parameters with other GCC countries are delaying its implementation. The GCC countries are looking to introduce VAT simultaneously across the region. We believe that the UAE will seek to balance increasing revenues with containing the impact on the economy, as it has sought to do with the gasoline price increase. Official comments highlight that entities will have around 18 months after the introduction of VAT to implement and fulfil the requirements of their tax obligations.

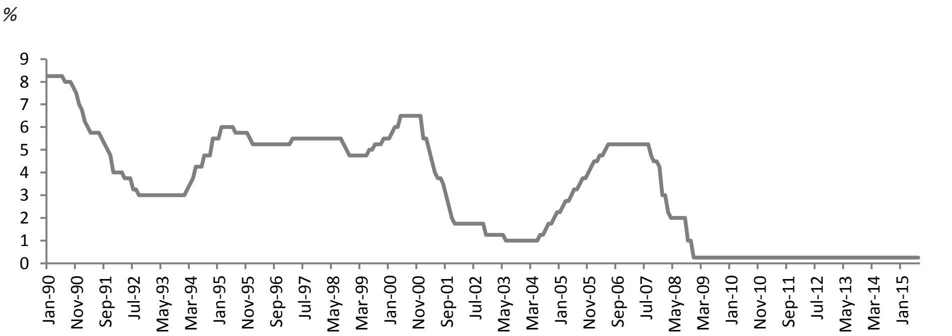
B. G4 Economies

US: Greater uncertainly over September following July FOMC minutes

Further improvement in economic data required before Fed will hike

The minutes of the FOMC's 28-29 July meeting were more bearish than markets had expected. We see two key developments in the minutes: i) greater concern over a weaker inflation outlook; and ii) that there needs to be further improvement in the data before interest rates can be increased. The minutes noted that most of the FOMC members felt that conditions were approaching a point at which to raise rates, but that this level has not yet been reached. This implies that the Fed needs to see further improvement in economic data, whilst earlier statements had implied that the data would have had to weaken in order to prevent the Fed from hiking in September. The minutes indicated that labour conditions are very nearly satisfied, with "many members" believing that full employment was close. The subsequent July employment report was consistent with the improvement required, in our view. The Fed continued to note that it only needed to see "some" more improvement in labour markets before hiking rates.

Fig. 3. US: Fed looking to raise Federal Funds Target Rate* from emergency low levels, but double dip in oil prices and global developments making it difficult



* Upper boundary of target range as of December 2008
Source: Bloomberg

Inflation remains main hurdle, deflationary pressures increasing

However, the weak inflation outlook remains the main hurdle for an interest rate liftoff, in our view. The minutes indicate downside risk to inflation from the USD and weakening oil prices. Whilst the minutes noted that "most participants" expected these factors to be temporary, deflationary pressures have actually increased in August. There was greater focus on international developments and the impact of the USD, which is expected to strengthen further and thus pose renewed downside risk to both economic activity and inflation. On the external front, the material slowdown in the Chinese economy was highlighted as a risk to the US economic outlook. In the end, "almost all" voters said that "they would need to see more evidence that economic growth was sufficiently strong and labour market conditions had firmed enough for them to feel reasonably confident" on the inflation outlook. Importantly, the FOMC did not indicate that it would be looking to the inflation data to decide if it is "reasonably confident" in the inflation outlook. This likely reflects that upside to inflation is limited in the short term, especially in light of the falling commodity prices.

Fed wants to move, but global developments making it difficult

We continue to see September as the most likely time for the US to raise interest rates (by 25 bps), though the risk of a later (December) start has increased. Data releases in the next few weeks will be important, especially on the labour front. FOMC members appear still to want to raise rates from their current low emergency levels by year end. Indeed, "some participants" emphasised that the economy had made significant progress over the past few years, and viewed the economic conditions as being in place to begin to increase the Federal Funds Target Rate. However, this is being made more difficult by the various disinflationary forces and greater global uncertainties.

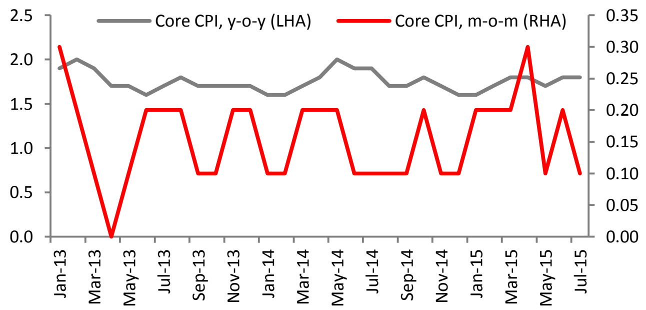
Inflation: Overall July inflation outturns were in line with the consensus, with headline CPI at 0.2% y-o-y and core CPI at 1.8% y-o-y. However, on a monthly basis, inflation decelerated to a three month low of 0.1% m-o-m, from 0.3% in June, as energy prices fell. The July data were consistent with a longer timeline for inflation to return towards the Fed's 2% target rate. Core inflation remained steady on a yearly basis, with shelter costs compensating for a sharp decline in airfares. While core inflation was not far from the overall inflation target, it was driven largely by rent, implying a limited pickup in wider inflation.

Solid housing data for July

Housing data: Housing data released thus far for July have continued to highlight that the sector remains an area of strength for the economy. Housing starts rose to a near eight-year high in July, driven by single family homes. Housing starts rose 10.6% y-o-y in July to 1.2 million (SAAR). New building permits fell m-o-m, though this followed several months of very strong gains. Meanwhile, existing home sales surprised on the upside, coming in at 5.59 million SAAR in July, versus the consensus of 5.43 million.

Fig. 4. US: July core inflation moderates on a monthly basis, with sharply lower airfares

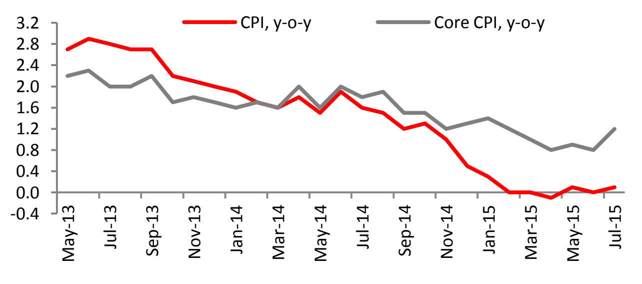
% change



Source: Bloomberg

Fig. 5. UK: Core inflation rises in July, likely on transitory factors

% change y-o-y



Source: Bloomberg

UK: July Core inflation surprises on upside

Core inflation reaches five-month high of 1.2% y-o-y

UK inflation surprised on the upside in July, especially core inflation, which jumped to its highest level in five months. The core measure increased to 1.2% y-o-y, from 0.8% in June and compared to the 0.9% consensus. The higher reading was due largely to clothing prices, with smaller discounts in the summer sales this year compared with last year. This partly reflected the stronger demand environment, in our view. Moreover, airfares also contributed to a stronger core inflation reading in July. However, both the clothing and airfare components are volatile and could moderate going forward. This is especially the case as seasonal demand moderates (airfares) and given the weak global inflation and strong trade weighted GBP (clothing).

The stronger clothing and airfare inflation helped compensate for the fall in energy prices, resulting in headline inflation of 0.1% y-o-y (up from 0% in June). Nevertheless, headline inflation remained exceptionally weak, still well below the BoE's 2% target. As such, and with signs of recent moderation in employment data, we expect interest rates to remain on hold until 1Q2016.

Headline inflation remains exceptionally weak

Greece: Heading for parliamentary elections; risk to bailout programme

Greece is likely to hold parliamentary elections (slated for 20 September) after Prime Minister Alexis Tsipras resigned last week and called new elections. The elections are to be held after opposition parties have the opportunity to form a coalition government (which they are expected to fail to do). Early elections became a possibility after Tsipras lost the support of left-wing members of his Syriza party. Consequently, he has needed opposition support to be able to pass legislation required by Eurogroup creditors in the Greek parliament. The aim of this move is to strengthen Tsipras' mandate, both by quelling the rebellion within Syriza and garnering public support for the bailout programme.

Parliamentary elections could be delayed as opposition tries to form coalition

Tsipras is planning to run again for the office of prime minister, and recent polls see the Syriza party as the most likely winner of the new elections. However, risks remain from the new anti-austerity camp, which is against the EUR85 billion bailout programme, and is likely to receive substantial support. A new anti-austerity party, Popular Unity, was formed last week, splitting from Tsipras' Syriza. If the elections have no clear winner and Tsipras cannot form a majority government, complicated negotiations will follow. Meanwhile, all reforms will be put on hold until after the parliamentary elections. Consequently, Greece is unlikely to pass the first review of the bailout programme in October.

Polls suggest Syriza likely winners of new election, but risks remain

Japan: Economy contracts in 2Q on weaker consumption and exports

Japan's GDP contracted -0.4% q-o-q in 2Q, slightly less than the consensus of -0.5% q-o-q. However, the already strong 1Q 2015 GDP data were upwardly revised, resulting in 1.1% q-o-q (versus 1% growth earlier). The drop in GDP in 2Q was driven by weaker private consumption and export activity. Consumption contracted -0.8% q-o-q in 2Q, with a number of one off factors contributing. These included bad weather, postponed bonus payments, and the moving of large retailers' summer sales to July. Nevertheless, the underlying data reflected the fact that private spending has yet to stage a sustained recovery since the national sales tax rose in April 2014, in part because wages have yet to rise as quickly as prices. The weaker JPY is also resulting in higher imported food prices. Meanwhile, net exports detracted -0.3 ppt from headline GDP growth, a deterioration from the -0.1 ppt drag in 1Q. The slowing Chinese economy remains the main bottleneck to a recovery in exports. Investments and inventories contributed positively to growth.

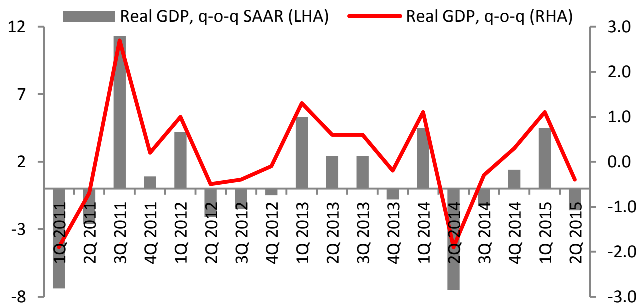
Numerous one-off factors negatively impact private consumption

The 2Q contraction was due partly to the strong growth seen in 1Q. Consequently, the growth rate in 1H2015 was still very strong at 2.2% SAAR. The weakness in 2Q is unlikely to extend into 3Q, and the economy is expected to return to expansionary mode; this would be on the back of private consumption normalising after the one-off factors. Corporate capital expenditure is also expected to strengthen on the back of improved earnings. However, the growth rate in 2H is likely to be weaker than in 1H. We believe that the BoJ will look past the 2Q data and keep interest rates on hold in 2H. However, weak Chinese demand remains a risk to the outlook. Thus, greater fiscal stimulus may be more beneficial to the economy than monetary stimulus, with the

Economy expected to return to positive growth in 3Q weaker JPY unlikely to bolster Chinese demand for Japanese exports. Nevertheless, we see further monetary easing in 1Q2016, with inflation remaining low and substantially below the BoJ's target.

Fig. 6. Japan: Real GDP contracts q-o-q in 2Q, driven by exports and consumption

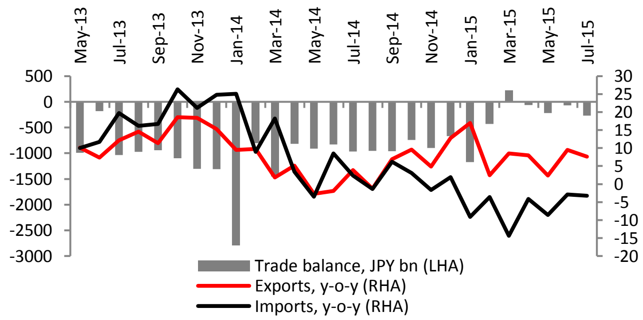
% change q-o-q



Source: Bloomberg

Fig. 7. Japan: Export growth moderates to 7.6% y-o-y in July, led by China

JPY billion (LHA); % change y-o-y (RHA)



Source: Bloomberg

Japan trade balance: The July export data continued to point to a softening external demand environment. Thus, net exports are unlikely to boost the economy in 3Q. Export growth moderated to 7.6% y-o-y in July, down from 9.5% in June, albeit still above the consensus of 5.2% growth. Export growth to China moderated to 4.2% y-o-y in July, from 5.9% in June. The US remained a bright spot, with export growth accelerating to 18.8% y-o-y from 17.6% in June, driven by cars and pharmaceuticals. Meanwhile, imports contracted -3.2% y-o-y, below the consensus of -8.2%.

Export growth continues to decelerate in July

C. Emerging Market Economies

Turkey: Keeps interest rates on hold; to tighten policy to support TRY

The CBRT kept interest rates on hold last week (policy rate at 7.5%, ON lending rate at 10.75%, ON deposit rate at 7.25%). Some market participants had expected an increase in the ON rate, aimed at supporting the TRY, which has come under downward pressure from rising political uncertainty. The recent moderation in inflation due to weaker food and fuel prices likely supported the decision to keep interest rates on hold. With rates remaining on hold, the CBRT will largely rely on utilising FX to manage TRY volatility.

Lower inflation gives CBRT time before tightening policy

However, the CBRT provided a roadmap for tightening monetary policy in the coming months as the US starts normalising interest rates. The tightening is aimed at reducing pressure on core inflation from the weaker TRY. The roadmap includes implementing a tighter liquidity policy and narrowing the interest rate corridor to make it more symmetric with Turkey's policy rate once Fed starts hiking rates. The latter implies that the CBRT will have to hike its policy rate. The CBRT also plans to sell more USD in daily auctions to reduce exchange rate volatility. However, political pressure remains against higher interest rates. This pressure could increase on the back of the elections scheduled for 1 November; these were announced after Prime Minister Ahmet Davutoglu abandoned efforts to form a coalition government.

Higher interest rates expected going forward once Fed moves

II. Economic Calendar

Fig. 8. Upcoming Events and Data Releases

Time*	Country	Data point	Period	Prior	Consensus
Expected this week					
	Kuwait	CPI, y-o-y	Jul	3.5%	--
	Bahrain	M2, y-o-y	May	6.6%	--
	Saudi	M2 Money Supply, y-o-y	Jul	12.4%	--
	Bahrain	CPI, y-o-y	Jul	1.7%	--
Tuesday, 25 Aug					
6:00	China	Conference Board China July Leading Economic Index			
10:00	Germany	GDP SA, q-o-q	2Q F	0.4%	0.4%
10:00	Germany	GDP NSA, y-o-y	2Q F	1.6%	1.6%
12:00	Germany	IFO Business Climate	Aug	108	107.6
12:00	Germany	IFO Current Assessment	Aug	113.9	113.9
12:00	Germany	IFO Expectations	Aug	102.4	102
14:40	Eurozone	ECB Vice President Constancio Speaks in Mannheim			
17:45	US	Markit US Composite PMI	Aug P	55.7	--
17:45	US	Markit US Services PMI	Aug P	55.7	55.6
18:00	US	New Home Sales, SAAR	Jul	482K	510K
18:00	US	New Home Sales, m-o-m	Jul	-6.8%	5.8%
	Japan	Cabinet Office Monthly Economic Report for August			
Wednesday, 26 Aug					
14:40	Eurozone	ECB Executive Board Member Praet Speaks in Mannheim			
16:30	US	Durable Goods Orders, m-o-m	Jul	3.4%	-0.4%
16:30	US	Durable Goods Orders, ex-Transport, m-o-m	Jul	0.6%	0.4%
16:30	US	Capital Goods New Orders, non-defense, m-o-m	Jul	0.7%	0.4%
18:00	US	Dudley Answers Questions At Press Briefing on Local Economy			
Thursday, 27 Aug					
10:00	UK	Nationwide House PX, m-o-m	Aug	0.4%	0.4%
15:00	Eurozone	ECB Executive Board Member Coeure Speaks in Paris			
16:30	US	GDP Annualized, q-o-q	2Q S	2.3%	3.2%
16:30	US	Personal Consumption	2Q S	2.9%	3.1%
16:30	US	Initial Jobless Claims	22-Aug	277K	275K
	US	Kansas City Fed Hosts Symposium in Jackson Hole, Wyoming			
Friday, 28 Aug					
3:30	Japan	Natl CPI, y-o-y	Jul	0.4%	0.2%
3:50	Japan	Retail Trade, y-o-y	Jul	1%	1.1%
12:30	UK	GDP, q-o-q	2Q P	0.7%	0.7%
12:30	UK	GDP, y-o-y	2Q P	2.6%	2.6%
13:00	Eurozone	Economic Confidence	Aug	104	103.8
13:00	Eurozone	Consumer Confidence	Aug F	-6.8	--
16:00	Germany	CPI, y-o-y	Aug P	0.2%	-0.1%
16:30	US	Personal Income	Jul	0.4%	0.4%
16:30	US	Personal Spending	Jul	0.2%	0.4%
16:30	US	PCE Deflator, y-o-y	Jul	0.3%	0.3%
16:30	US	PCE Deflator, m-o-m	Jul	0.2%	0.1%
16:30	US	PCE Core, m-o-m	Jul	0.1%	0.1%
16:30	US	PCE Core, y-o-y	Jul	1.3%	1.3%
18:00	US	U. of Mich. Sentiment	Aug F	92.9	93.1

* UAE time
Source: Bloomberg

Fig. 9. Last Week's Data

Time*	Country	Data point	Period	Prior	Consensus	Actual
GCC data						
	UAE	CPI, y-o-y	Jul	4.2%	--	4.4%
	UAE	M2, m-o-m	Aug	0.4%		-0.4%
	Qatar	CPI, y-o-y	Jul	1.4%		1.6%
	Oman	CPI, y-o-y	Jul	0.2%	--	0.5%
Monday, 17 Aug						
3:50	Japan	GDP SA, q-o-q	2Q P	1.1%	-0.5%	-0.4%
3:50	Japan	GDP Annualized SA, q-o-q	2Q P	4.5%	-1.8%	-1.6%
16:30	US	Empire Manufacturing	Aug	3.9	4.5	-14.9
Tuesday, 18 Aug						
12:30	UK	CPI, m-o-m	Jul	0%	-0.3%	-0.2%
12:30	UK	CPI, y-o-y	Jul	0%	0%	0.1%
12:30	UK	CPI Core, y-o-y	Jul	0.8%	0.9%	1.2%
12:30	UK	PPI Output NSA, m-o-m	Jul	-0.1%	0%	-0.1%
12:30	UK	PPI Output NSA, y-o-y	Jul	-1.6%	-1.5%	-1.6%
16:30	US	Housing Starts	Jul	1204K	1180K	1206K
Wednesday, 19 Aug						
3:50	Japan	Trade Balance	Jul	-¥70.5B	-¥53B	-¥268.1B
3:50	Japan	Exports, y-o-y	Jul	9.5%	5.2%	7.6%
3:50	Japan	Imports, y-o-y	Jul	-2.9%	-8.2%	-3.2%
8:30	Japan	All Industry Activity Index, m-o-m	Jun	-0.5%	0.4%	0.3%
16:30	US	CPI, m-o-m	Jul	0.3%	0.2%	0.1%
16:30	US	CPI, ex-Food and Energy, m-o-m	Jul	0.2%	0.2%	0.1%
16:30	US	CPI, y-o-y	Jul	0.1%	0.2%	0.2%
16:30	US	CPI, ex-Food and Energy, y-o-y	Jul	1.8%	1.8%	1.8%
16:30	US	Fed Releases Minutes from 28-29 July FOMC Meeting				
Thursday, 20 Aug						
12:30	UK	Retail Sales, ex-Auto and Fuel, m-o-m	Jul	-0.3%	0.4%	0.4%
12:30	UK	Retail Sales, ex-Auto and Fuel, m-o-m	Jul	4.1%	4.3%	4.3%
16:30	US	Initial Jobless Claims	15-Aug	273K	271K	277K
17:00	US	Existing Home Sales, m-o-m	Jul	3%	-1.1%	2%
18:00	US	Philadelphia Fed Business Outlook	Aug	5.7	6.5	8.3
18:00	US	Leading Index	Jul	0.6%	0.2%	-0.2%
Friday, 21 Aug						
10:00	Germany	GfK Consumer Confidence	Sep	10.1	10.1	9.9
18:00	Eurozone	Consumer Confidence	Aug A	-7.1	-6.9	-6.8

* UAE time
Source: Bloomberg

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