The Week Ahead: US and UK inflation data in focus; Turkey's constitutional referendum

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G4: US and UK inflation, Yellen scheduled to speak today

The key US release this week will be March inflation data (14 April), with consensus forecasting headline inflation to have slowed to 2.6% y-o-y (February: 2.7%). This softening is expected on the back of a decline in seasonally adjusted energy prices and weak food inflation. However, core inflation is estimated to have risen to 2.3% y-o-y (February: 2.2%), after a monthly rise of 0.2%. April consumer confidence data will also be closely watched (13 April), with retail spending expected to rebound in 2Q2017, after a weak 1Q. Indeed, March retail sales (14 April) are forecast to contract by 0.1% m-o-m led by car and gasoline sales. Meanwhile, Fed Chair Janet Yellen is scheduled to speak this week (10 April) at the University of Michigan. Markets will particularly look for insight on the Fed's plans for reducing its balance sheet, following the release of the March FOMC minutes (page 4). Meanwhile, UK's March headline inflation (11 April) is expected to remain steady at 2.3% y-o-y, with lower energy prices compensating for the higher imported inflation. This will be comfortably below the BoE's year-end forecast of 2.7%, reducing the urgency for the BoE to raise rates in the near term.

Saudi Arabia: Meeting bond investors for international sukuk

Saudi Arabia will start an investor roadshow for its first international sukuk this week. This follows Riyadh's debut international bond (conventional) in October when it raised USD17.5 billion. The sukuk is expected to have a dual-tranche structure with 5- and 10-year maturities. As we have previously highlighted, further international borrowing will be critical for the government to cover its budget deficit without tightening domestic banking sector liquidity. The sharp drawdowns in SAMA's NFAs in 2M2017 reflect the government's focus on tapping FX reserves to cover its budget deficit with reduced reliance on domestic channels, aimed at supporting liquidity in the banking system. We expect to see the falls in NFAs moderate following the issuance. The government is looking to raise c.USD15 billion in 2017. Its current low level of debt (13.2% of GDP at end-2016) provides ample space to do so.

Turkey: Referendum vote remains close call

Politics will also take centre stage this week, with the focus on developments in Syria and Turkey's referendum. Turkish citizens will vote on a constitutional referendum (16 April), on whether to switch to a presidential system, from a parliamentary one. The referendum, if passed by a majority, will give sweeping powers to the president, including the authority to appoint his own cabinet and judges, with limited parliamentary checks. The opinion polls indicate a tight race between "Yes" and "No". If the electorate votes "No", President Recep Tayyip Erdogan's government is likely to announce fresh general elections, which might increase short-term asset market volatility. Victory by the "Yes" camp could stem near-term turmoil in Turkish financial markets, but only at the cost of a delay in urgently needed economic reforms.

I. Recent Events and Data Releases

A. MENA Economies

Qatar: Removing gas production moratorium for North Field

Qatar looking to maintain global market share, especially as demand grows

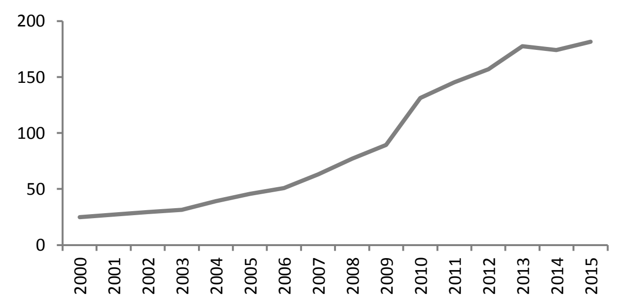
Qatar announced last week that it will remove the moratorium on gas development from the giant North Field, which it shares with Iran. The freeze has been in place since 2005, aimed at studying the North Field's long-term potential. The removal of the moratorium has been anticipated for some time as it was initially expected in 2013 or 2014. Qatar Petroleum announced that studies have confirmed the potential for developing a new gas project targeted towards the export market. The proposed project would develop the southern section of the field, with a capacity of 2 billion cubic feet per day. This would increase current production from the North Field by around 400K barrels of oil equivalent per day, and production is expected to start in five to seven years.

Qatar looks to maintain dominant share as gas demand increases in medium-term

We see the removal of the moratorium as a move by Qatar to maintain its global market share, especially as a number of other countries (Australia, Russia and US) are set to increase their gas production. Iran has also been looking to step up its production from the shared field (known as South Pars in Iran) aimed at the medium-term LNG market. Global LNG demand is also expected to rise from around 2024. Qatar continues to produce gas at a cheaper price than most other key suppliers and is looking to take advantage of any medium-term demand growth. The economic impact of the move will be limited in the short to medium term though it provides some visibility of support for investment after the 2022 World Cup. Qatar's gas production is expected to increase in 2017 and 2018 due to the Barzan project (also from the North Field). The project was sanctioned before the 2005 moratorium and the gas produced will be used domestically.

Fig. 1. Qatar: Gas production stabilising after major gas projects completed in 2012

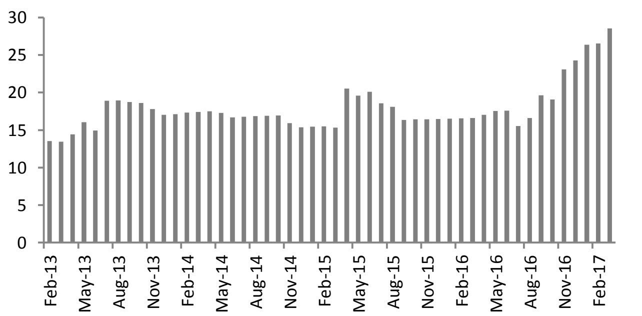
Billion cubic metres



Source: BP

Fig. 2. Egypt: FX reserves reach six-year high in March; further increases expected due to IMF programme

USD billion



Source: Central Bank of Egypt

Egypt: FX reserves rise by USD2 billion in March to USD28.5 billion

We estimate import cover reached c.5.5 months in March

Egypt's FX reserves rose by USD2 billion to USD28.5 billion at end-March. FX reserves are now at their highest level since March 2011, and we estimate that import cover has risen to around 5.5 months. We see various drivers behind this, including a USD1 billion loan from the World Bank disbursed in March. Ongoing portfolio inflows and Saudi Arabia resuming oil product shipments to Egypt from mid-March also likely contributed. Reflecting the strong portfolio inflows in March, the Head of Public Debt at the Ministry of Finance, Samy Khallaf, noted that foreigners have bought USD1 billion in Egyptian debt since mid-March and 4 April. Meanwhile, there is a five-year grace period before the Egyptian government needs to start paying for the oil product shipments from Saudi Arabia. We expect further increases in Egypt's FX reserves going forward with additional disbursements from the IMF and World Bank.

B. G4 Economies

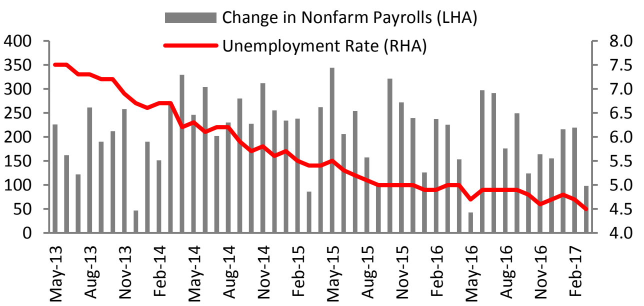
US: March jobs growth misses expectations, though underlying trend solid

Unemployment rate falls to 4.5% in March, down from 4.7% in previous month

The US economy added just 98K jobs in March, substantially below consensus expectations of 180K jobs. Moreover, the two-month payroll net revisions were -38K, resulting in fewer jobs being created in 2M2017. Despite this, the jobs report was solid, with encouraging details within the report continuing to point to reduced slack in the labour market. The unemployment rate fell to 4.5% from 4.7% in February. Moreover, the underemployment rate fell to 8.9% (February: 9.2%), its lowest level since December 2007. The participation rate remained steady at 63%, as did monthly wage growth at 0.2% m-o-m. However, the y-o-y rise in wages slowed moderately to 2.7% in March, down from 2.8% in the previous month.

Fig. 3. US: Pace of 3- and 6-months jobs growth still solid despite weak March print

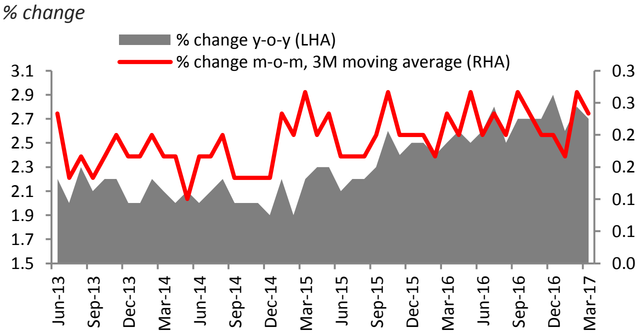
'000 (LHA); % (RHA)



Source: Bureau of Labor Statistics

Fig. 4. US: Annual wage growth trending upwards on tightening in labour market

% change



Source: Bureau of Labor statistics

Average jobs growth remains solid, further signs of labour market tightening

The soft jobs growth in March is seen as being payback for the strong gains in 2M2017, which was supported by the warmer seasonal weather. The 3-month (177K) and 6-month (162K) averages remain healthy despite the latest disappointing NFP report. Both the goods and service sectors saw weak job creation in March reflecting this payback. However, the retail sector continued to lose jobs, shedding 29.7K in March, after a loss of 30,000 in February, on the back of the structural shift towards online sales. Reflecting the still strong underlying labour trends, the markets still see a c. 63% probability of a 25 bps rate hike in June, with no impact from the March labour data.

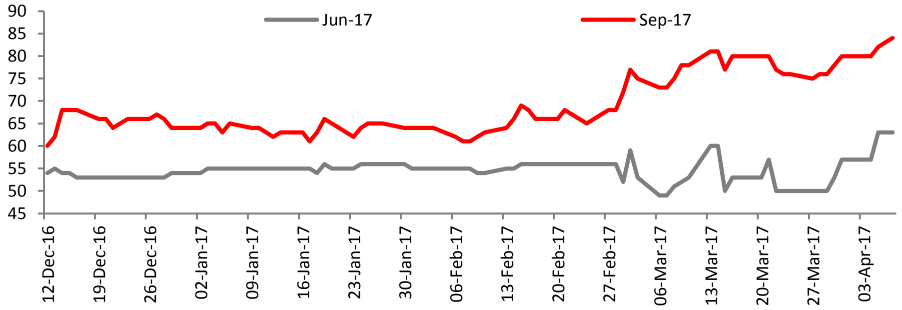
US: No surprises on Fed economic outlook; reinvestment policy being discussed

Many FOMC members have not factored in fiscal support for 2017

The Fed provided limited new details on its economic assessment in the minutes of its 14-15 March meeting where benchmark rates were raised by 25 bps. The market reaction to the minutes was therefore muted. The report highlighted that the FOMC members' outlook on the economy had not changed markedly from the last meeting. Fed committee members continue to expect a pick-up in business and consumer spending in 2017, and also have strong inflation expectations with many members indicating that it was important to gradually reduce the central bank's "accommodative stance". Members' views on fiscal policy were mixed with almost half not factoring any fiscal support into their assumptions. The Fed also saw global risks moderating, especially surrounding the economies of China and the Eurozone.

Fig. 5. US: Market expectation of 25 bps FFTR hike at June meeting did not change following March NFP report

Market probability of 25 bps increase in FFTR by Fed meeting



Source: Bloomberg

"Most" thought a change in reinvestment policy was appropriate later in 2017

The most interesting component of the minutes was the discussion concerning reducing the Fed's balance sheet. The Fed has c.USD2.5 trillion in Treasury securities and USD1.8 trillion in mortgage-backed securities (MBS), which it continues to reinvest at the time of maturity. The minutes highlighted that "most" meeting participants thought that a change in the reinvestment policy would be appropriate later in 2017. The discussion also showed a preference for phasing out or ceasing reinvestment of both maturing Treasury securities and MBS holdings at the same time. Discussion of the reinvestment policy will continue in the upcoming meetings, with the Fed informing the markets well in advance of it implementing any changes. Notably, some key FOMC members, such as New York Fed President William Dudley, have indicated that interest rate hikes could take a temporary pause as the balance reduction starts. This could have implications for the timing of the next Fed rate hikes. We expect a further two 25 bps rate hikes in September and December. However, if the Fed is looking to start unwinding its balance sheet at end 2017, this could result in rate hikes being brought forward to June and September. We believe that the strength of the US economy will be critical for such a scenario. More specific details are likely to be revealed around midyear to start preparing markets.

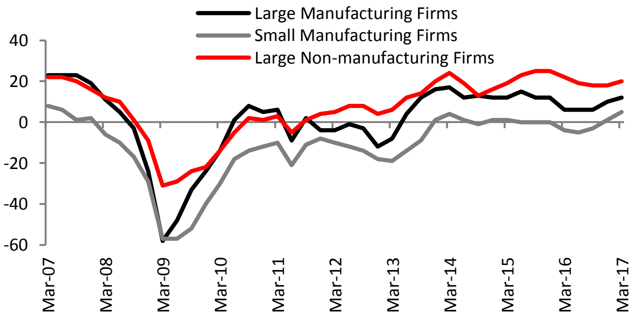
Japan: Broad improvement in corporate sentiment but inflation expectations still muted

Significant improvement in Japanese firms' capex intentions

The Tankan business conditions index for large manufacturing industries released by the BoJ last week came in at 12 in 1Q2017 (consensus: 14; 4Q2016: 10), slightly below the consensus number but at the highest level since 2Q2015. The improvement was broad-based with increases also registered in business sentiment for small firms (5 after 1 in 4Q2016) and non-manufacturing firms (20 after 18 in 4Q2016). The responses indicated that much of the improvement in sentiment was due to a relative pick-up in overseas demand, though domestic demand conditions also showed a mild recovery. Furthermore, firms' USD:JPY exchange rate expectations for FY2017-18 (July 2017-June 2018) remained relatively strong at 108.43 compared to the current levels of 110-111. Thus export conditions could remain more favourable than implied in the survey, even if there is some mild appreciation in the USD:JPY from current spot levels. A sharp tightening in the pair from the current levels is not our base case. Another encouraging aspect of the data release was stronger-than-expected investment intentions by firms at 0.6% y-o-y (consensus: -0.3%, 1Q2016: -0.9%) with large manufacturing firms planning to boost their capex by 5.3% y-o-y (1Q2016: 3.1%). The most bullish investment intentions were from firms in the heavy machinery and metals sectors (export-driven) and retail and hospitality (likely 2020 Olympics-led).

Fig. 6. Japan: Corporate sentiment improves across firms, driven largely by overseas demand

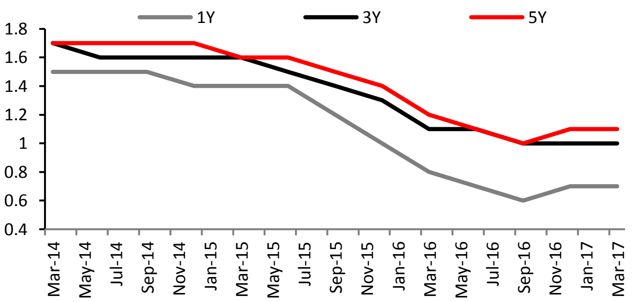
Tankan Business Sentiment Index



Source: Bank of Japan

Fig. 7. Japan: Inflation expectations remain well-below BoJ's 2% target; firms looking to cut prices in medium term

Corporate inflation expectations in % (1,3 and 5 years ahead)



Source: Bank of Japan

However, corporates still intend to cut prices in medium term

The Tankan surveys provided further evidence for our view that while external demand has supported corporate investment sentiment in Japan recently, firms' inflation outlooks remain far below the BoJ's target. Indeed, the Price Outlook Survey accompanying the releases revealed that firms expect inflation to remain at 1.1% y-o-y for the next five years (unchanged from 4Q2016). Uncertainty among corporates about the sustainability of the current economic recovery explains part of this stickiness. Firms still expect to cut the prices of their goods over the medium term (3-5 years), citing tight external competition (notably due to the exchange rate). This development, combined with the modest wage hikes announced by major firms so far this year, suggests that the BoJ is likely to keep its current accommodative monetary stance in place to alleviate disinflationary pressures.

Eurozone: ECB re-affirms commitment to accommodative policy stance

ECB says it will closely watch wage growth developments

The minutes of the ECB's March monetary policy meeting dispelled market perceptions that the central bank was looking to further taper its QE purchases or hike its benchmark rates any time this year. The Governing Council noted that "any removal" of an easing bias in its forward guidance would be "premature", though it acknowledged that economic activity had firmed up, with less downside risks to growth. We believe that soft underlying inflation dynamics are the reason behind the ECB's reluctance to unwind its monetary stimulus too soon. Wage growth in the Eurozone, including in stronger economies like Germany and the Netherlands, has been subdued, even as data released last week showed that the unemployment rate fell to an eight-year low of 9.5% in February. Indeed, President Mario Draghi's comments in the minutes noted that wage growth remains the "lynchpin" for the ECB to revise its views on inflation. So far this year, we have seen only limited improvement in the indicators we track to measure the underlying strength in inflation (credit growth and capacity utilisation), which suggests that the recent jump in headline CPI is likely to be short-lived. We expect the ECB to begin tapering its asset purchases only in 1Q2018, but keep its policy rates at a near-zero level throughout this year and next.

C. Emerging Market Economies

India: RBI more cautious on inflation outlook; takes steps to improve monetary transmission

RBI raises reverse repo rate and increases its inflation forecasts for FY18 by 50 bps

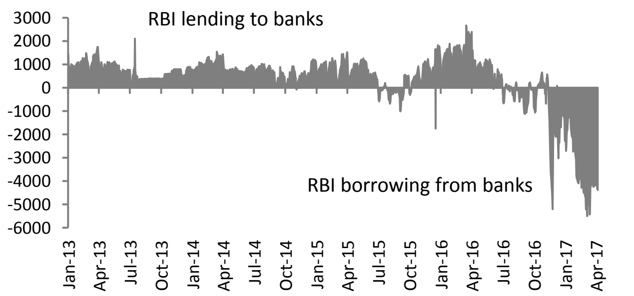
The RBI kept its benchmark repo rate on hold at 6.25% last week, in line with our and market expectations. However, in a move to improve monetary transmission, the RBI narrowed its Liquidity Adjustment Facility (LAF) corridor to 50 bps (100 bps previously). This was achieved by raising the reverse repo rate (RBI's borrowing rate) by 25 bps to 6% and lowering the marginal standing facility rate (ceiling rate) by 25 bps to 6.5%. In our view, this action is intended to bring the interbank money market rate closer to the benchmark repo rate. Since demonetisation, the massive influx of deposits in the banking system and weak credit demand from the over-leveraged corporate sector has created an unprecedented daily liquidity surplus of c.INR4 trillion, which lowered interbank and short-tenor government bill rates 30-40 bps below the benchmark repo rate. By raising the reverse repo rate, the RBI sets a floor on interbank rates, by offering to borrow surplus cash from money market participants at 6% (25 bps below repo rate).

Central bank to remain on hold until 2Q2018

Looking ahead, we expect more measures by the RBI to absorb surplus liquidity in the banking system over the coming quarters, including a Special Deposit Facility, which allows banks to park cash with the central bank (without collateral) at a rate close to the current benchmark repo rate. However, we expect the RBI to keep the benchmark repo rate on an extended pause until 2Q2018, despite an acceleration in headline inflation over the coming quarters, for two reasons. First, we expect much of the pick-up in inflation this year to reflect the transitory impact of the Goods and Services Tax (GST). Second, we see GDP growth in FY18 (April 2017-March 2018) at 7% y-o-y, which is softer than the RBI's forecast of 7.4% y-o-y, mainly due to muted private capex growth, and a lower than expected boost from urban consumption. That said, the recent increase in state government current expenditure in rural areas poses some risks to our forecasts, implying an earlier than expected tightening cycle by the RBI. Indeed, the RBI highlighted greater upside risks to inflation in FY18 in its post-policy comments, compared to its last meeting, revising up its inflation forecast for the year to 4.75% (4.25-4.3% in February forecasts). Specifically, the central bank highlighted the upward pressures to inflation from rising state government deficits and a less plentiful monsoon than last year.

Fig. 8. India: RBI hikes reverse repo rates to absorb liquidity from interbank markets more effectively

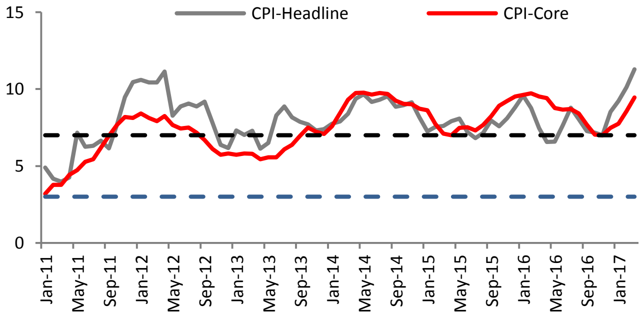
Daily net operations in repo market, INR billion



Source: Reserve Bank of India

Fig. 9. Turkey: Inflation continues to climb in March as weaker TRY feeds into core prices

% change y-o-y



Source: Central Bank of the Republic of Turkey

Turkey: March inflation at nine-year high, further rate hikes expected

CBRT may tighten liquidity further at next policy meeting

Inflation continued to accelerate in Turkey in March, rising by 11.3% y-o-y (consensus: 10.7%; February: 10.1%). Both food (12.5% after 8.7% in February) and core inflation (9.5% after 8.6% in February) picked up in the month, suggesting broad-based price pressures in the economy. Notably, prices of core goods (automobiles, furniture and clothing) saw a sharp increase due to the pass-through of the weaker TRY, despite significant indirect tax cuts for these goods announced in February. Furthermore, core inflation momentum continues to accelerate, hinting at further upside pressure on prices. In our view, price momentum across segments is more widespread than was expected by the CBRT at its last monetary policy meeting in March. In its upcoming policy meeting (26 April), we expect the central bank to further extend its liquidity-tightening measures either through the reduction of repo limits or by raising the Late Liquidity Lending Rate (marginal lending rate) by another 50 bps to 12.25%. However, we continue to believe that liquidity tightening through a conventional benchmark repo rate hike of 50 bps to 8.50% would be a more prudent course of action in the current inflationary environment. This would reduce uncertainty about the future path of monetary policy in Turkey and also address the lack of monetary transmission of recent liquidity measures into retail lending and deposit rates.

II. Economic Calendar

Fig. 10. The week ahead

Time*	Country	Event	Period	Prior	Consensus
Expected this week					
	Saudi Arabia	GDP Constant Prices, q-o-q	4Q	0%	--
	Qatar	CPI, y-o-y	Mar	0.7%	--
	Kuwait	M2 Money Supply, y-o-y	Feb	2.9%	--
	Oman	CPI, y-o-y	Mar	2.4%	--
	China	M2 Money Supply, y-o-y	Mar	11.1%	11.1%
	Bahrain	M2 Money Supply, y-o-y	Feb	--	--
	China	New Yuan Loans CNY	Mar	1170B	1200B
	China	Aggregate Financing CNY	Mar	1147.9B	1500B
	India	Exports, y-o-y	Mar	17.5%	--
Monday, 10 Apr					
	Egypt	Urban CPI, y-o-y	Mar	30.2%	--
	Egypt	CPI Core, y-o-y	Mar	33.1%	--
3:50	Japan	BoP Current Account Adjusted	Feb	¥1259.8B	¥1788.8B
11:00	Turkey	Industrial Production, y-o-y	Feb	2.6%	2.5%
Tuesday, 11 Apr					
00:00	US	Fed's Yellen Speaks at University of Michigan			
12:30	UK	CPIH, y-o-y	Mar	2.3%	2.3%
12:30	UK	CPI, y-o-y	Mar	2.3%	2.3%
12:30	UK	CPI Core, y-o-y	Mar	2%	1.9%
12:30	UK	PPI Input NSA, y-o-y	Mar	19.1%	17%
12:30	UK	PPI Output NSA, y-o-y	Mar	3.7%	3.4%
13:00	Eurozone	Industrial Production, y-o-y	Feb	0.6%	1.9%
13:00	Eurozone	ZEW Survey Expectations	Apr	25.6	--
18:00	US	JOLTS Job Openings	Feb	5626	--
21:45	US	Fed's Kashkari Participates in Q&A in Minneapolis			
Wednesday, 12 Apr					
3:50	Japan	Machine Orders, y-o-y	Feb	-8.2%	2.5%
5:30	China	CPI, y-o-y	Mar	0.8%	1%
12:30	UK	Average Weekly Earnings, 3M/y-o-y	Feb	2.2%	2.2%
12:30	UK	ILO Unemployment Rate 3Mths	Feb	4.7%	4.7%
12:30	UK	Employment Change 3M/3M	Feb	92K	70K
15:00	US	MBA Mortgage Applications	7-Apr	-1.6%	--
16:00	India	CPI, y-o-y	Mar	3.7%	3.9%
16:00	India	Industrial Production, y-o-y	Feb	2.7%	1.4%
Thursday, 13 Apr					
	China	Imports, y-o-y	Mar	38.1%	15.5%
	China	Exports, y-o-y	Mar	-1.3%	3.4%
	China	Trade Balance	Mar	-$9.15B	$12.5B
16:30	US	Initial Jobless Claims	8-Apr	234K	--
18:00	US	U. of Mich. Sentiment	Apr P	96.9	96.5
Friday, 14 Apr					
16:30	US	CPI, m-o-m	Mar	0.1%	0%
16:30	US	CPI, ex-Food and Energy, m-o-m	Mar	0.2%	0.2%
16:30	US	CPI, y-o-y	Mar	2.7%	2.6%
16:30	US	CPI, ex-Food and Energy, y-o-y	Mar	2.2%	2.3%
16:30	US	Retail Sales Advance, m-o-m	Mar	0.1%	-0.1%
16:30	US	Retail Sales ex-Auto and Gas, y-o-y	Mar	0.2%	0.3%
16:30	US	Retail Sales Control Group, y-o-y	Mar	0.1%	0.3%
Sunday, 16 Apr					
	Turkey	Constitutional referendum on presidential system			

* UAE time
Source: Bloomberg

Fig. 11. Last week's data

Time*	Country	Event	Period	Prior	Consensus	Actual
EM Data						
	Qatar	GDP Constant Prices, y-o-y	4Q	3.9%	--	1.7%
	Qatar	M2 Money Supply, y-o-y	Feb	-0.8%	--	2.5%
	Bahrain	GDP Constant Prices, y-o-y	4Q	3.9%	--	1.1%
	Egypt	Net Reserves	Mar	26.5B	--	28.5B
	Egypt	Gross Official Reserves	Mar	26.6B	--	28.5B
	China	Foreign Reserves	Mar	$3005.1B	$3011B	$3009.1B
Monday, 3 Apr						
3:50	Japan	Tankan Large Manufacturing Index	1Q	10	14	12
3:50	Japan	Tankan Large Non-Manufacturing Index	1Q	18	19	20
3:50	Japan	Tankan Large All Industry Capex	1Q	5.5%	-0.3%	0.6%
4:30	Japan	Nikkei Japan PMI Manufacturing	Mar F	52.6	--	52.4
9:00	India	Nikkei India PMI Manufacturing	Mar	50.7	--	52.5
11:00	Turkey	CPI, y-o-y	Mar	10.1%	10.7%	11.3%
12:30	UK	Markit UK PMI Manufacturing SA	Mar	54.5	55	54.2
13:00	Eurozone	Unemployment Rate	Feb	9.6%	9.5%	9.5%
17:45	US	Markit US Manufacturing PMI	Mar F	53.4	53.5	53.3
18:00	US	ISM Manufacturing	Mar	57.7	57.2	57.2
Tuesday, 4 Apr						
8:15	UAE	UAE PMI	Mar	56	--	56.2
8:15	Saudi Arabia	Saudi Arabia PMI	Mar	57	--	56.4
18:00	US	Factory Orders, m-o-m	Feb	1.5%	1%	1%
18:00	US	Durable Goods Orders, m-o-m	Feb F	1.7%	1.7%	1.8%
Wednesday, 5 Apr						
15:00	US	MBA Mortgage Applications	31-Mar	-0.8%	--	-1.6%
16:15	US	ADP Employment Change	Mar	245K	185K	263K
18:00	US	ISM Non-Manf. Composite	Mar	57.6	57	55.2
22:00	US	FOMC Meeting Minutes	15-Mar	--	--	
Thursday, 6 Apr						
13:00	India	RBI Repurchase Rate	6-Apr	6.25%	6.25%	6.25%
15:30	Eurozone	ECB account of the monetary policy meeting				
16:30	US	Initial Jobless Claims	1-Apr	259K	250K	234K
Friday, 7 Apr						
4:00	Japan	Labor Cash Earnings, y-o-y	Feb	0.3%	0.5%	0.4%
12:30	UK	Industrial Production, m-o-m	Feb	-0.3%	0.2%	-0.7%
12:30	UK	Industrial Production, y-o-y	Feb	3.3%	3.7%	2.8%
16:30	US	Change in Nonfarm Payrolls	Mar	219K	180K	98K
16:30	US	Unemployment Rate	Mar	4.7%	4.7%	4.5%
16:30	US	Average Hourly Earnings, m-o-m	Mar	0.3%	0.2%	0.2%
16:30	US	Average Hourly Earnings, y-o-y	Mar	2.8%	2.7%	2.7%

* UAE time
Source: Bloomberg

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