

The Week Ahead: Global inflation data and FOMC minutes in focus

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► **US: Inflation expected to turn negative on weaker fuel prices**

US retail sales showed that consumer spending regained momentum in January, despite the market turbulence. Data has not been as weak as markets are implying. However, a key risk remains of the market turmoil affecting the economy through deteriorating sentiment. The data so far indicates that consumers are confident and spending as the labour market continues to improve. The focus turns to inflation this week (due 19 February), with consensus expecting a -0.1 ppt fall m-o-m led by lower gasoline prices. However, core inflation is expected to pick up moderately to 0.2% m-o-m (from 0.1% in December) on higher shelter costs. Meanwhile, the minutes of the FOMC's January meeting (released on 17 February) should provide more insight into the Fed's assessment of the market turbulence and its implications for the US economic outlook. The minutes may show a more cautious stance over rate increases, albeit stopping short of explicitly postponing a March hike.

► **Europe: Draghi to speak to EU Parliamentary Committee**

ECB President Mario Draghi will testify before the European parliament's economic and monetary affairs committee (15 February). Over the coming weeks markets will be looking for further clues of easing measures likely to be introduced at the March meeting. Recent comments from ECB members indicate firm support for a deposit rate cut within the Governing Council, though appetite for wider action still seems limited. We expect a 10bp cut at the meeting. Rising concern over the adverse effects of the negative interest rate policy, especially on banking sector profitability, will likely preclude a deeper cut. Thus, the ECB may have to frame the cut as part of a broader package, including changes to the asset-purchase programme.

► **UK: Negotiations over EU membership continue**

Negotiations over revisions to the terms of the UK's EU membership will be in focus at the EU summit (18-19 February). Progress is expected to be made towards an agreement, leading to a "Brexit" referendum possibly in June. Meanwhile, a number of important UK data releases are due including on the labour market, CPI and retail sales. The December labour market report (due 17 February) is expected to show a continued gradual deceleration in wage growth. However, the unemployment rate is expected to decline to 5% (from 5.1%), reflecting solid underlying labour market conditions which should eventually lead to a pickup in the pace of wage growth.

► **Asia: China and Japan to dominate data releases**

China will release trade, money and inflation data for January, though the data will be impacted by seasonal factors. Meanwhile, Japan's January trade data will be closely watched for the impact of the stronger JPY.

I. Recent Events and Data

A. MENA Economies

UAE: Progress on the federal debt law

Comments by Younis Al Khouri, undersecretary at the Ministry of Finance, indicate that progress is being made on a federal debt law. The new law could be ratified in six to nine months, according to Al Khouri, opening the way for an initial AED80-100 billion issue. We see the law as positive in broadening funding sources, especially given the weak outlook for oil. The issuance of federal domestic debt is further supported by the UAE's low debt. The IMF estimates total UAE gross government debt at around 18.9% of GDP in 2015. Moreover, the law will be positive for the development of a domestic yield curve, as corporates are also increasingly turning to debt capital markets for funding, especially on a longer term basis.

Progress on the federal debt law positive for broadening the UAE's funding sources

So far, there are no indications on how the proceeds of a bond sale will be allocated beyond the requirement to fund the federal budget. The federal budget for 2016 is planned at AED48.5 billion (USD13.2 billion) with a zero deficit, given the current funding methodology. The federal government has to run a balanced budget, with spending equalling transfers by the individual emirates, given its limited funding options. The Abu Dhabi government is the largest contributor to the federal budget, followed by Dubai. Thus, the issuance of federal debt could lower transfers from each emirate to the federal budget. Total federal spending accounts for less than 15% of total UAE government spending; the majority of the expenditure occurs at an emirate level.

No indications on how bond sale proceeds will be utilised – after covering federal spending

B. G4 Economies

US: Yellen sends cautious yet balanced message

There were no surprises from Fed Chair Janet Yellen's testimony to Congress last week. She again provided a fairly balanced outlook, which was very much in line with the FOMC's January post-meeting statement. While stressing the positives, she also acknowledged the increasing market risks, which provided a cautionary overall tone. Yellen emphasised that there was no "preset course" for policy, but rather a data dependent approach. She very much expects further gradual hiking this year, supported by continued US economic growth, despite the rising risks from global market volatility and China-related concerns. Moreover, she highlighted that the Fed is unlikely to reverse course on rates, despite the risks. We continue to forecast only two 25 bps rate hikes this year, with the first coming around midyear.

March rate hike not explicitly ruled out, but unlikely given market volatility

Regarding the positives, Yellen highlighted the further payroll gains shown in the January labour market report, albeit with some slack remaining in the market. She also indicated that the Fed still expects continued improvements in the labour market to support US consumer spending. The housing market was also highlighted as an area of strength. The FOMC's January assessment that economic activity will expand at a moderate pace was repeated in the testimony. However, Yellen expressed concern about the recent tightening financial conditions in the US. She said that this is likely to dampen growth, though she concluded that the Fed was not currently seeing signs of an outright credit contraction. She noted that credit availability is one of several factors that feeds into the outlook, and that the Fed would continue to watch the data heading into the March FOMC meeting.

US economy healthy, though risks highlighted

The discussion of risks to the outlook was largely international in flavour. Yellen highlighted that more persistent equity market declines and further USD strength could weigh on the economic outlook. Moreover, global growth risks have increased, with concerns mounting over Chinese growth and the country’s FX policies. Yellen concluded that “the jury is still out” on whether recent financial volatility has materially changed the US’s economic outlook. She repeated January’s policy statement that the Fed will closely monitor global economic and financial developments. She also highlighted that global developments have lowered inflation expectations. The oil price decline and USD appreciation are central to the FOMC’s expectation that inflation will remain low in the near term. However, Yellen said that she still views lower oil prices as good news for US consumers.

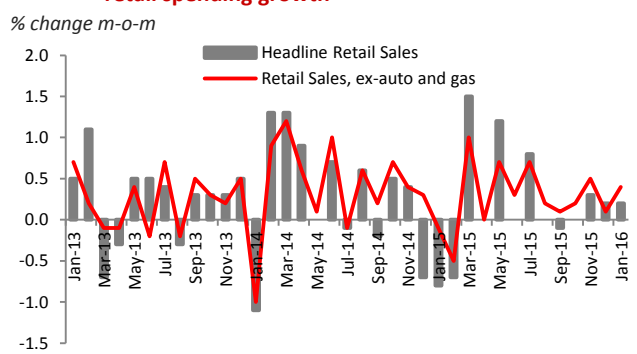
“Jury still out” on impact of market volatility on US economy

US: Retail sales solid, beating consensus expectations

Retail sales data for January showed private consumption regaining momentum after moderating in 4Q2015. The Fed will likely see this as evidence that the US economy is weathering the market turmoil and that its focus should be on underlying trends. Retail sales grew by 0.2% m-o-m in January, unchanged from the December level (revised up from -0.1% m-o-m). The headline January growth was slightly above the consensus expectation of 0.1% m-o-m. Expenditure on gasoline continues to be a drag on overall spending; expenditure at service stations fell by -3.1% m-o-m. However, core retail sales, which corresponds most closely to the consumer spending component of GDP, showed strong underlying and broad demand in the economy. Core retail sales, also known as the control group (ex automobiles, gasoline, building materials and food services) increased 0.6% m-o-m in January, from a contraction of -0.3% in December.

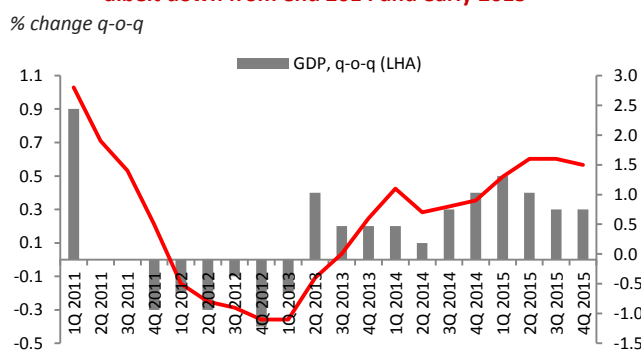
Strong growth in core retail sales of 0.6% m-o-m in January

Fig. 1. US: Lower gasoline price continues to drag on headline retail spending growth



Source: Bloomberg

Fig. 2. Eurozone: 4Q GDP growth remained respectable, albeit down from end 2014 and early 2015



Eurozone: GDP growth steady at 0.3% q-o-q in 4Q

Eurozone GDP expanded 0.3% q-o-q in 4Q2015, in line with market expectations and 3Q2015 growth. In yearly terms, the economy grew by 1.5% y-o-y in 4Q. However, there continues to be marked divergence amongst the countries within the bloc. The German economy grew by 0.3% q-o-q in 4Q, driven by consumption (private and public) and residential investment. Spain continued to register the strongest growth of 0.8% q-o-q. Growth in Italy disappointed, decelerating to just 0.1% q-o-q, its weakest in a year. Meanwhile, Greece slipped back into recession, contracting by -0.6% q-o-q in 4Q. The breakdown of GDP by type of expenditure is not yet available, but it is likely to have been driven by government and private consumption. Lower oil prices and

Private and government spending likely the main drivers of GDP growth in 4Q2015

continued employment growth likely supported personal spending. Meanwhile, government spending was likely bolstered by expenditure on refugees in 4Q. Whilst Eurozone growth was respectable in 4Q2015, the build up in domestic demand would not provide a sufficient buffer in the event of external demand weakening and/or the EUR appreciating, in our view.

C. Emerging Market Economies

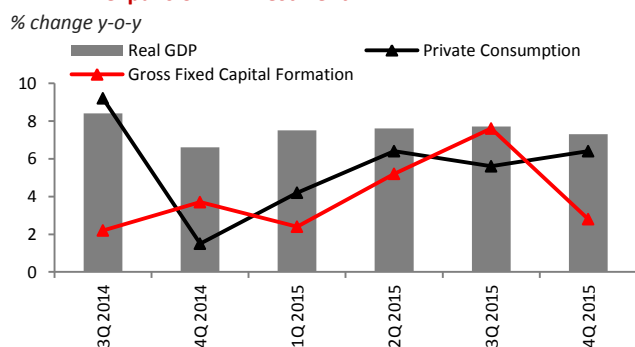
India: Economy expands 7.3% y-o-y in December, supported by consumption

India's economy grew 7.3% y-o-y in 4Q15, beating the market's expectation of 7.1%. There were also significant upward revisions to the previous quarters, with growth lifted to 7.6% for 2Q (from 7.5%) and 7.7% for 3Q (from 7.4%). The revisions were due largely to investment and the inventory buildup being stronger than initially gauged.

Stronger private and government consumption in 4Q

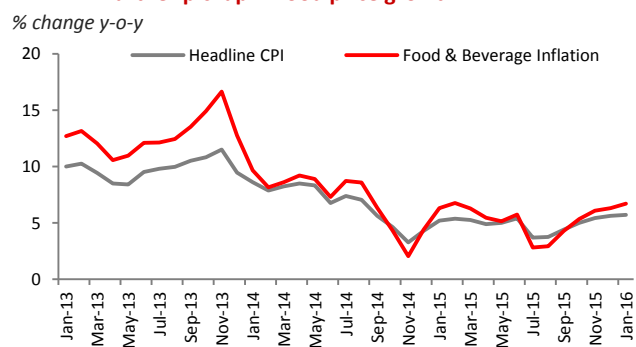
The key positive contributor to real headline growth in 4Q was private consumption, which accelerated to 6.4% y-o-y in 4Q, from 5.6% in 3Q. We attribute this pickup to lower inflation and oil prices supporting disposable income. Moreover, the interest rate cuts were likely also supportive, though the RBI's cuts have not filtered fully into commercial bank rates. Government consumption strengthened more moderately, to 4.7% in 4Q from 4.3% in 3Q.

Fig. 3. India: GDP growth slows in 4Q2015 with weaker expansion in investment



Source: Bloomberg

Fig. 4. India: Consumer inflation rises in January with a further pickup in food price growth



Source: Bloomberg

Nonetheless, the underlying data raises some concerns regarding the outlook, especially the deceleration in investment growth in 4Q. Moreover, the support from net exports was due largely to lower imports, indicating weaker overall domestic demand despite the pickup in consumption. Net exports contributed positively (0.5 ppt) to growth, as imports contracted -10.8% y-o-y. Meanwhile, exports saw a larger contraction in 4Q of -9.4% y-o-y compared to -3.4% in 3Q, reflecting the weaker global demand. We see the softening investment backdrop as the main factor behind the fall in real import growth. The expansion in investment moderated to just 2.8% y-o-y in 4Q, from an average of 6.4% in the previous two quarters. The data indicated that new projects are not picking up pace despite the government's efforts to progress with stalled projects.

Investment activity continues to decelerate

The official estimate for FY2015-16 (April-March) GDP growth stands at 7.6%, versus 7.2% in the previous fiscal year. However, this would require real GDP growth of around 7.8% in 1Q2016. With government expenditure growth likely to be softer in 1Q2016 in order to meet the fiscal deficit target, this target looks difficult to achieve, in our view. Also, concerns remain about official data overstating the economy's strength, with interim data pointing to weaker growth.

Concerns remain over data accuracy

India inflation: January CPI inflation surprised on the upside accelerating to 5.7% y-o-y (from 5.6% in December) on stronger food price increases. Consensus expected inflation to decelerate to 5.4% y-o-y in January. The pickup in food inflation (6.9% y-o-y in January versus 6.4% in December) was likely due to weak post-monsoon and winter rains, driving up prices of items such as pulses, egg, fish and meat. Pulses remained the strongest contributor to headline CPI, adding 1 ppt to the CPI print. Core inflation decelerated to 4.7% in January (from 4.9% in December), though remained steady on a monthly basis. We believe the RBI will need to see signs that the overall inflationary trend is moderating before cutting benchmark rates again. Thus, February inflation data (due to be released in mid-March) will be critical for the RBI's decision in early April, in our view. A further upward surprise in the February data would endanger our forecast of a 25 bps rate cut in April. The FY2016-17 fiscal budget will also be critical in the RBI's next rate decision.

Inflation accelerates on stronger food price growth

II. Economic Calendar

Fig. 5. Upcoming events and data releases

Time*	Country	Data point	Period	Prior	Consensus
Expected this week					
	China	New Yuan Loans, CNY	Jan	597.8B	1900B
	China	Aggregate Financing, CNY	Jan	1820B	2200B
	China	Foreign Direct Investment CNY, y-o-y	Jan	-5.8%	-5.9%
Monday 15 Feb					
3:50	Japan	GDP SA, q-o-q	4Q P	0.3%	-0.2%
8:30	Japan	Industrial Production, m-o-m	Dec F	-1.4%	--
8:30	Japan	Capacity Utilisation, m-o-m	Dec	-0.1%	--
18:00	Eurozone	ECB's Draghi Speaks to EU Parliamentary Committee in Brussels			
	China	Trade Balance	Jan	\$60.1B	\$60.6B
	China	Exports, y-o-y	Jan	-1.4%	-1.8%
	China	Imports, y-o-y	Jan	-7.6%	-3.6%
Tuesday 16 Feb					
13:30	UK	CPI, m-o-m	Jan	0.1%	-0.7
13:30	UK	CPI, y-o-y	Jan	0.2%	0.3%
13:30	UK	CPI Core, y-o-y	Jan	1.4%	1.3%
14:00	Germany	ZEW Survey Current Situation	Feb	59.7	55
14:00	Eurozone	ZEW Survey Expectations	Feb	22.7	--
17:30	US	Fed's Harker Speaks on Economy at University of Delaware			
17:30	US	Empire Manufacturing	Feb	-19.4	-10.5
19:30	US	Fed's Kashkari Delivers First Public Speech at Brookings			
Wednesday 17 Feb					
3:50	Japan	Machine Orders, m-o-m	Dec	-14.4%	4.7%
4:00	US	Fed's Rosengren Speaks at Colby College			
13:30	UK	Average Weekly Earnings, 3m/y-o-y	Dec	2%	1.9%
13:30	UK	Weekly Earnings ex Bonus, 3m/y-o-y	Dec	1.9%	1.8%
16:00	US	MBA Mortgage Applications	12-Feb	9.3%	--
17:30	US	Housing Starts	Jan	1149K	1175K
17:30	US	Housing Starts, m-o-m	Jan	-2.5%	2.3%
17:30	US	Building Permits	Jan	1204K	1200K
18:15	US	Industrial Production, m-o-m	Jan	-0.4%	0.4%
18:15	US	Capacity Utilization	Jan	76.5%	76.7%
23:00	US	US Fed Releases Minutes from Jan. 26-27 FOMC Meeting			
Thursday 18 Feb					
3:50	Japan	Trade Balance Adjusted	Jan	¥36.6B	¥62.1B
3:50	Japan	Exports, y-o-y	Jan	-8	-11
3:50	Japan	Imports, y-o-y	Jan	-18	-15.9
5:00	US	Fed's Bullard Speaks to CFA Society St. Louis			
5:30	China	CPI, y-o-y	Jan	1.6%	1.9%
5:30	Japan	BOJ Ishida speaks in Fukuoka			
16:30	Eurozone	ECB account of the monetary policy meeting			
17:30	US	Initial Jobless Claims	13-Feb	269K	275K
20:00	Eurozone	EU Leaders Start Summit in Brussels			
Friday 19 Feb					
0:30	US	Fed's Williams Gives Outlook Speech in LA			
13:30	UK	Retail Sales, ex-Auto Fuel, m-o-m	Jan	-0.9%	0.7%
13:30	UK	Retail Sales, ex-Auto Fuel, y-o-y	Jan	2.1%	3.4%
17:00	US	Fed's Mester to Speak at Global Interdependence Center			
17:30	US	CPI, m-o-m	Jan	-0.1%	-0.1%
17:30	US	CPI, ex-Food and Energy, m-o-m	Jan	0.1%	0.2%
19:00	Eurozone	Consumer Confidence	Feb A	-6.3	-6.6

* UAE time

Source: Bloomberg

Fig. 6. Last week's data

Time*	Country	Data point	Period	Prior	Consensus	Actual
Monday 8 Feb						
16:00	India	GDP, y-o-y	4Q	7.7%	7.1%	7.3%
16:00	India	GDP Annual Estimate, y-o-y	1Q A	7.2%	7.4%	7.6%
Tuesday 9 Feb						
9:15	UAE	Dubai Economy Tracker SA	Jan	51.8	--	50.7
10:00	Japan	Machine Tool Orders, y-o-y	Jan P	-25.7%	--	-17.2%
19:00	US	JOLTS Job Openings	Dec	5346	5413	5607
19:00	US	Wholesale Inventories, m-o-m	Dec	-0.4%	-0.2%	-0.1%
Wednesday 10 Feb						
3:50	Japan	Housing Loans, y-o-y	4Q	2.4%	--	2.2%
3:50	Japan	PPI, y-o-y	Jan	-3.5%	-2.8%	-3.1%
13:30	UK	Industrial Production, m-o-m	Dec	-0.8%	-0.1%	-1.1%
13:30	UK	Industrial Production, y-o-y	Dec	0.7%	1%	-0.4%
13:30	UK	Manufacturing Production, m-o-m	Dec	-0.3%	0.1%	-0.2%
16:00	US	MBA Mortgage Applications	5-Feb	-2.6%	--	9.3%
	Egypt	Urban CPI, y-o-y	Jan	11.1%	--	10.1%
	Egypt	Urban CPI, m-o-m	Jan	-0.1%	--	0.1%
	Egypt	CPI Core, y-o-y	Jan	7.2%	--	7.7%
Thursday 11 Feb						
4:01	UK	RICS House Price Balance	Jan	49%	52%	49%
17:30	US	Initial Jobless Claims	6-Feb	285K	280K	269K
17:30	US	Continuing Claims	30-Jan	2260K	2245K	2239K
Friday 12 Feb						
14:00	Eurozone	Industrial Production SA, m-o-m	Dec	-0.5%	0.3%	-0.1%
14:00	Eurozone	Industrial Production WDA, y-o-y	Dec	1.4%	0.7%	-1.3%
14:00	Eurozone	GDP SA, q-o-q	4Q A	0.3%	0.3%	0.3%
14:00	Eurozone	GDP SA, y-o-y	4Q A	1.6%	1.5%	1.5%
16:00	India	Industrial Production, y-o-y	Dec	-3.4%	-0.2%	-1.3%
17:00	India	CPI, y-o-y	Jan	5.6%	5.4%	5.7%
17:30	US	Retail Sales Advance, m-o-m	Jan	0.2%	0.1%	0.2%
17:30	US	Retail Sales ex-Auto, m-o-m	Jan	0.1%	0%	0.1%
17:30	US	Retail Sales ex-Auto and Gas	Jan	0.1%	0.3%	0.4%
17:30	US	Retail Sales Control Group, m-o-m	Jan	-0.3%	0.3%	0.6%
19:00	US	U. of Mich. Sentiment	Feb P	92	92.3	90.3

* UAE time

Source: Bloomberg

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