The Week Ahead: China and global inflation data in focus

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China: 4Q GDP data, December IP and retail sales

Markets will focus on data from China this week, including 4Q GDP growth. The consensus is that real GDP growth will have remained steady at 6.9% y-o-y in 4Q, supported in part by stronger government infrastructure spending. Meanwhile, the consensus is for some monthly improvement in the interim data for December, with a pickup in auto sales likely to have supported retail sales and industrial production. Much of the recent global market volatility has stemmed from concerns about China's growth outlook.

US and Europe: Inflation data and ECB meeting in focus

Elsewhere, the focus will be on US, Eurozone, and UK inflation, and the ECB's 21 January meeting. The consensus is that both the US and UK will have seen zero inflation (i.e. 0% m-o-m) in December on the back of the fall in fuel prices. We expect the latest leg down in oil prices to be highlighted by the BoE and ECB this week. BoE Governor Mark Carney will make his first speech of the year on 19 January, with markets watching closely for any guidance on the interest rate outlook. We expect the ECB to acknowledge downside risks to its inflation outlook stemming from the oil market developments, whilst reiterating its commitment to doing more if necessary. However, we do not expect any changes to monetary policy at this point. The minutes of the 3 December meeting highlighted the split within the ECB, and we believe that the bank will look for further growth and inflation trends before introducing additional loosening (expected in mid-2016).

Iran: Sanctions lifted, pace of return to oil market critical

International economic sanctions on Iran were lifted on 16 January, with the country's oil sector set to be the main beneficiary. Expectations of increased oil exports from Iran have been central to the January plunge in oil prices, with global market volatility and growth concerns also adding pressure. Markets will be watching closely for indications of the pace of Iranian oil export growth. Iranian Minister of Petroleum Bijan Zanganeh has indicated that Tehran will be able to increase oil production by 500K bpd within a week of the sanctions removal, followed by an additional 500K bpd within six months. However, he said last week that Iran would not seek to distort the market, and would re-enter gradually.

GCC: Bahrain, Oman, and Qatar introduce fuel price reforms

Bahrain, Oman, and Qatar announced higher fuel prices last week on the back of the continued fall in the oil price and pressure on their fiscal positions. Bahrain increased petrol prices by more than 50%, while Oman raised the price of super petrol by 33.3% and Qatar did so by 30%. Oman is also looking to increase its corporate taxation rate to 15%. We see GCC real non-oil GDP growth decelerating further in 2016 with the retrenchment in government spending and subsidy reforms. The reforms should also lead to high inflation in 2016.

I. Recent Data and Events

A. MENA Economies

GCC: Bahrain, Qatar, and Oman latest GCC countries to announce fuel subsidy reforms

Bahrain increases petrol prices by more than 50% on 12 January

Bahrain, Qatar, and Oman announced fuel subsidy reform last week on the back of the continued fall in the oil price and pressure on their fiscal positions. They were the latest GCC countries to announce subsidy reforms, following the UAE in mid-2015. Saudi Arabia announced widespread energy price reforms in December 2015 concurrently with its 2016 budget. Bahrain increased petrol prices by 60% for super and 56.3% for regular. Bahrain has not yet announced a fiscal budget for 2016, though we expect a further retrenchment in government spending. The country has indicated that it is looking to lower electricity and water subsidies. Meanwhile, Qatar followed suit with an announcement on 14 January that gasoline prices would rise at midnight. The price of super petrol was raised by 30%, whilst regular petrol increased by 35%.

Oman's 2016 budget looks to reduce government spending by -11%

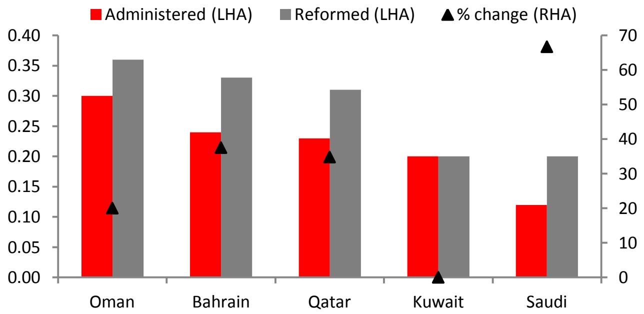
Oman this month announced concrete measures to lower its fiscal deficit, including reducing government spending by -11% in the 2016 budget. The reduction in fuel subsidies are part of the budget objective to cut subsidy spending to OMR400 million in 2016, from OMR900 million in 2015. The price of super petrol was increased by 33.3%, whilst regular petrol rose by 22.8% and diesel by 9.6%. The new prices became effective on 15 January, and are to be reviewed monthly. This initial adjustment follows Oman having indicated that fuel prices would not be liberalised completely, but rather adjusted periodically. The country is also looking to raise the corporate tax rate to 15% for all companies from the current 12% (though only for businesses earning over OMR30,000 per year). The new tax rate was approved by Oman's State Council last week, and will now be forwarded to the Council of Ministers.

Fiscal reforms to drag on non-oil GDP growth in 2016

With the renewed downward pressure on oil in January 2016, we believe that the GCC countries will feel the need to implement further fiscal reforms this year and beyond. We see the recent reforms across the GCC as part of a multi-year fiscal adjustment programme. We foresee GCC real non-oil GDP growth decelerating further in 2016 with the retrenchment in government spending and subsidy reforms. The reforms should also lead to high inflation in 2016.

Fig. 1. GCC: Recent increases in gasoline prices (regular)

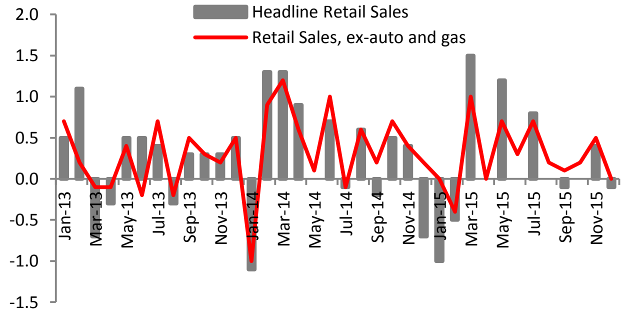
USD per litre (LHA); % change (RHA)



Source: MEES, ADCB estimates

Fig. 2. US: headline retail sales fall 0.1% m-o-m in December

% change m-o-m



Source: Bloomberg

B. G4 Economies

US: Retail sales disappoint, indicate softening economic momentum

Unseasonably warm weather contributes to poor retail sales

The latest US data indicated a moderation in economic growth momentum in 4Q. This included disappointing retail sales for December, which came in below market expectations. Headline retail sales fell by -0.1% m-o-m, underperforming the market consensus of 0.1% growth and having increased 0.4% in November. Control retail sales, which most closely resemble the consumption component in GDP data, fell by -0.3% m-o-m. This measure excludes autos, gasoline, building materials, and food services. The fall in retail sales was due partly to unseasonably warm weather in December, which reduced purchases of winter apparel. Moreover, the lower gasoline prices weighed on service station receipts. There were some limited areas of improvement, such as building material sales rising by 0.7% m-o-m, likely helped by the mild weather. For all of 2015, retail sales rose just 2.1% (the weakest annual reading since 2009), having advanced 3.9% in 2014.

Eurozone: ECB split over introduction of further easing at December meeting

Some ECB members push for more moderate loosening in December, providing space for further action if required

The minutes from the ECB's 3 December meeting provided interesting insights into the discussions within the Governing Council. The bank's loosening at the meeting, including reducing the marginal deposit rate by -10 bps to -0.3%, fell short of market expectations. Notably, highlighting a rare public rift, the bank said that not all Council members agreed with its decision, with some proposing more action and others less. Not all members saw the need for further monetary easing in December, arguing that the economic recovery was continuing, inflation expectations had stabilised, and existing measures needed more time to be fully effective. Those advising against additional action unless clearer risks (such as a meaningful deflationary trend) materialised were particularly opposed to additional QE. A key point made by those arguing for a -10 bps deposit rate cut was that it left some room for further action. Meanwhile, those pushing for more action did not ask for a cut of more than -20 bps.

Further options discussed, but no policy change expected at 21 January meeting

Regarding the asset purchase programme, some members had wanted to go beyond the six month extension that was agreed upon at the meeting. Others expressed a preference for increasing the volume of monthly purchases or front-loading purchases within the intended total programme size. Thus, both a time extension and a step-up of the monthly purchases remain on the table, as does a further rate cut. However, we believe that further monetary loosening would require a deterioration in the economic and inflation outlooks. In our view, this week's meeting (21 January) will be too soon for the ECB to take further action. However, the downside risks to inflation from the oil price's latest sharp fall will likely be highlighted. Nevertheless, with the inflation outlook weak, we foresee a further -10 bps cut in the deposit rate in mid-2016. A key event will be the ECB releasing its initial 2018 growth outlook on 10 March.

UK: BoE in holding mode; we now foresee later (4Q2016) liftoff

Tone marginally more bearish, though focus on data to see how trends develop

The BoE kept monetary policy steady at its 14 January meeting, in line with expectations. This included keeping the interest rate at 0.5% and the asset purchase target at GBP375 billion. Moreover, there was no change in the voting pattern, at 8-1. Some analysts had been expecting a unanimous vote to keep interest rates on hold with the recent slide in global oil prices. However, the minutes indicated that the BoE is in wait-and-see mode, and is in no rush to raise rates. The overall tone of the minutes was slightly more bearish, though they provided a balanced outlook and indicated that the bank is awaiting further data. The MPC members highlighted that wage growth had slowed more than expected, though they noted that the labour market was continuing to tighten, with unemployment falling. Recent comments from MPC members have suggested that they would like to see wage growth developments before raising rates. The BoE also lowered its near-term inflation and growth outlooks, though it noted that overall, there had been no significant change from the November Inflation Report. The bank highlighted that it expects only a slight drag on inflation from the renewed plunge in oil prices.

BoE unlikely to move ahead of Brexit referendum

Nevertheless, we now expect the BoE to raise rates in 4Q2016, versus 2Q previously. This expected delay is due to the latest leg-down in oil prices, the softening in UK growth indicators (including wages), and the prospect of a Brexit referendum. The MPC next meets on 4 February, when the new quarterly Inflation Report will be released and inputs to BoE models updated. This could trigger changes to the Bank's economic projections and forecasts, in our view. We still expect a rate hike in 2016 on the back of the anticipated pickup in wage growth and ongoing above-trend GDP growth. Meanwhile, markets are now pricing a rate hike in 2Q2017.

C. Emerging Market Economies

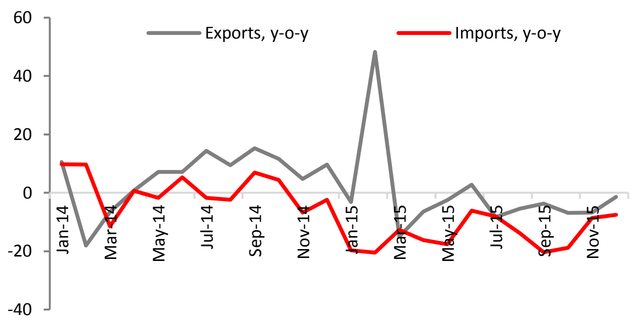
China: December trade data show some improvement

Both exports and imports come in above market expectations

Trade data for December came in better than markets had expected, with improvements on both the export and import sides. The data pointed to some initial stabilisation in domestic demand and a pickup in external demand. We nonetheless remain cautious, especially regarding the external outlook, with global demand projections remaining subdued. Moreover, we would need to see further signs of a buildup in domestic demand, supported by fiscal and monetary loosening measures, before becoming more bullish. Nevertheless, the trade data suggest that despite the financial market turmoil, the real economy has not deteriorated. The trade surplus widened to USD60.1 billion in December from USD54.1 billion in November.

Fig. 3. China: Contraction in both export and import growth narrows in December

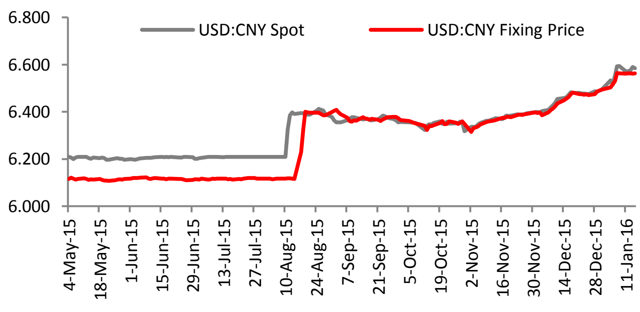
% change y-o-y



Source: Bloomberg

Fig. 4. China: CNY still overvalued despite weakening since August 2015

USD:CNY



Source: Bloomberg

Volume of commodity imports increases, possibly supported by stronger public investment

Exports contracted by -1.4% y-o-y, substantially less than the market's expectation of -8% and the -6.8% seen in November. This relative improvement came despite a high base: export growth was 9.7% y-o-y in December 2014 versus 4.7% in November 2014. The narrower contraction in exports was due largely to stronger demand from developed economies, notably the EU. There could also have been some support from the CNY's weakening against the EUR in December. Meanwhile, the narrowing in import contraction to -7.6% y-o-y (consensus -11%) from November's -8.7% was led by commodities, despite the weaker prices. The import volume growth of copper and crude oil increased to a respective 25.8% and 9.3% y-o-y in December, from 11% and 7.6% in November. Commodity imports were likely supported partly by stronger public investment.

Low inflation environment supports further monetary loosening and CNY weakness

We expect the persistently weak inflation outlook to lead to further monetary easing, despite some tentative signs of stabilisation in economic activity. This includes an expectation of a -25 bps cut in benchmark interest rates and a -50 bps reduction in the RRR in 1Q. Meanwhile, the CNY's recent movements suggest that the Chinese authorities are looking to weaken the currency more aggressively, possibly front-loading the moves. The CNY remains overvalued despite the devaluation in 2H2015. Moreover, the low inflation environment supports the outlook for further CNY weakening.

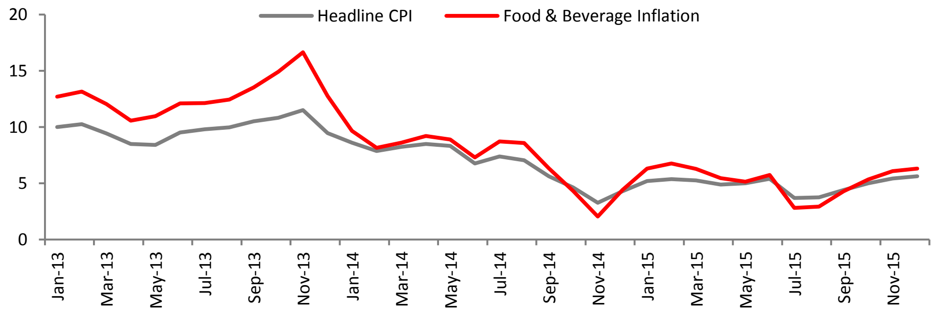
India: Inflation accelerates to 5.6% in December

Food prices largely behind acceleration, though core prices also increase

India's December CPI inflation surprised on the upside at 5.6% y-o-y, against the consensus expectation of 5.5% and up from 5.4% in November. The rise was due largely to the increase in pulse prices (which contributed 1.1 ppt to December headline inflation), though core prices also increased. Agflation strengthened to 6.3% y-o-y, from 6.1% in November. The rise in core inflation (yearly and monthly) was largely a result of increases in public transportation fares. A moderate pickup in economic activity also supported the increase in non-food inflation, in our view.

Fig. 5. India: Headline inflation accelerates to 5.6% in December on stronger food and core inflation

% change y-o-y



Source: Bloomberg

Further rate cuts unlikely until budget announcement at end of February

Inflation accelerated from a low of 3.7% y-o-y in July 2015, due partly to the removal of the favourable base effect. However, there are signs that food inflation growth is likely to moderate in the coming months on the back of government measures and the new harvest. The renewed fall in oil prices should also help to limit the upward pressure on inflation. Even if the recent pace in the pickup of inflation is maintained in January, CPI will still be well within the RBI's target of 6% in January 2016. Nevertheless, we believe that the RBI will keep rates on hold at its 2 February meeting. We see the government's FY2016/17 budget as critical, with the RBI looking to gauge its impact on inflation. The budget is due to be released on 28 February.

II. Economic Calendar

Fig. 6. Upcoming events and data releases

Time*	Country	Data point	Period	Prior	Consensus
Expected this week					
	UAE	CPI, y-o-y	Dec	3.5%	--
	UAE	CPI, m-o-m	Dec	-0.3%	--
Monday 18 Jan					
4:00	UK	Rightmove House Prices, m-o-m	Jan	-1.1%	--
4:00	UK	Rightmove House Prices, y-o-y	Jan	7.4%	--
8:30	Japan	Industrial Production, m-o-m	Nov F	-1%	--
8:30	Japan	Capacity Utilisation, m-o-m	Nov	1.3%	--
Tuesday 19 Jan					
6:00	China	Industrial Production YTD, y-o-y	Dec	6.1%	6.1%
6:00	China	Industrial Production, y-o-y	Dec	6.2%	6%
6:00	China	Retail Sales, y-o-y	Dec	11.2%	11.3%
6:00	China	Retail Sales YTD, y-o-y	Dec	10.6%	10.7%
6:00	China	Fixed Assets Ex Rural YTD, y-o-y	Dec	10.2%	10.2%
6:00	China	GDP SA, q-o-q	4Q	1.8%	1.8%
6:00	China	GDP, y-o-y	4Q	6.9%	6.9%
13:30	UK	CPI, m-o-m	Dec	0%	0%
13:30	UK	CPI, y-o-y	Dec	0.1%	0.2%
13:30	UK	CPI Core, y-o-y	Dec	1.2%	1.2%
14:00	Eurozone	ZEW Survey Expectations	Jan	33.9	--
14:00	Eurozone	CPI, m-o-m	Dec	-0.1%	0%
14:00	Eurozone	CPI, y-o-y	Dec F	0.2%	0.2%
14:00	Eurozone	CPI Core, y-o-y	Dec F	0.9%	0.9%
	UK	BoE Governor Mark Carney Speaks in London			
Wednesday 20 Jan					
13:30	UK	Jobless Claims Change	Dec	3.9K	2.8K
13:30	UK	Weekly Earnings ex-Bonus, 3M/y-o-y	Nov	2%	1.8%
13:30	UK	ILO Unemployment Rate, 3Mths	Nov	5.2%	5.2%
16:00	US	MBA Mortgage Applications	15-Jan	21.3%	--
17:30	US	Housing Starts	Dec	1173K	1200K
17:30	US	Housing Starts, m-o-m	Dec	10.5%	2.3%
17:30	US	CPI, m-o-m	Dec	0%	0%
17:30	US	CPI, ex-food and energy, m-o-m	Dec	0.2%	0.2%
17:30	US	CPI, y-o-y	Dec	0.5%	0.8%
17:30	US	CPI, ex-food and energy, y-o-y	Dec	2%	2.1%
Thursday 21 Jan					
16:45	Eurozone	ECB Main Refinancing Rate	21-Jan	0.05%	0.05%
16:45	Eurozone	ECB Deposit Facility Rate	21-Jan	-0.3%	-0.3%
16:45	Eurozone	ECB Marginal Lending Facility	21-Jan	0.3%	0.3%
17:30	US	Philadelphia Fed Business Outlook	Jan	-10.2	-5
17:30	US	Initial Jobless Claims	16-Jan	284K	280K
19:00	Eurozone	Consumer Confidence	Jan A	-5.7	-5.7
Friday 22 Jan					
13:30	UK	Retail Sales, ex-auto and fuel, m-o-m	Dec	1.7%	-0.3%
13:30	UK	Retail Sales, ex-auto and fuel, y-o-y	Dec	3.9%	3.5%
13:30	UK	Retail Sales, inc. auto and fuel, m-o-m	Dec	1.7%	-0.3%
13:30	UK	Retail Sales, inc. auto and fuel, y-o-y	Dec	5%	1.4%
19:00	US	Existing Home Sales	Dec	4.76M	5.2M
19:00	US	Existing Home Sales, m-o-m	Dec	-10.5%	9.2%

* UAE time
Source: Bloomberg

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