

The Week Ahead: Yellen testimony to Congress and retail data in focus

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► US: Yellen testimony to take centre stage

Fed Chair Janet Yellen's semi-annual monetary policy testimony to Congress (10-11 February) will be the key event of the week. This is especially so after the January non-farm payrolls revived market confidence in the US's economic recovery. The unemployment rate fell to 4.9% and wage growth picked up to 0.5% m-o-m, despite job creation coming in below market expectations at 151K. We expect the testimony to be balanced but cautious. The tighter financial conditions and global market volatility are likely to be highlighted as risks to economic growth. The sharply lower energy prices and a further appreciation of the USD in trade-weighted terms will also likely be seen as having lowered the near-term inflation outlook. However, we do not expect Yellen to offer specific guidance on the timing of the next rate hike. Rather, we expect her to echo recent comments from other FOMC members indicating that the Fed will continue to monitor global economic and financial developments closely. We continue to expect the FOMC's next rate hike in June.

► US: Modest recovery in retail sales expected

In a relatively quiet week for data, the focus will be on US retail sales due to be released on Friday. Consensus expects a modest recovery, with expansion of 0.1% m-o-m in January (after a -0.1% fall in December). The January growth was likely supported by auto sales. However, this headline recovery will likely be dampened by the sharp drop in gasoline prices in January. The retail "control group" (which excludes autos, gasoline, building materials and restaurants) is forecast to grow by 0.3% m-o-m, from a -0.3% contraction in December.

► Eurozone: 4Q GDP growth expected to remain steady

Consensus believes Eurozone growth remained at 0.3% q-o-q in 4Q, as in 3Q. Country details are already available for some major economies, whilst Germany has already published 2015 full year GDP. The data indicate that the German economy expanded by 0.3% q-o-q in 4Q. Disappointing Eurozone retail sales suggest a moderation in private consumption growth in 4Q, despite continued labour market improvements and low oil prices. The Paris attacks and unseasonably warm weather likely contributed, with the latter leading to lower spending on clothing and heating.

► India: GDP and inflation data to be released

Consensus believes India's GDP growth moderated to 7.1% y-o-y in 4Q2015, down from 7.4% in 3Q. Weaker industrial and agricultural output were likely behind the deceleration. Meanwhile, January inflation is estimated to have slowed to 5.3% y-o-y, from 5.6% in December, on softer food and fuel price growth.

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I. Recent Events and Data

A. MENA Economies

GCC: PMI data indicate further softening in non-oil activity

The PMI indices for both Saudi Arabia and the UAE moderated in January, pointing to further deceleration in non-oil activity. The lower readings were in line with our expectations, following the further fall in oil prices in January and the contractionary budget announced by Saudi Arabia at the end of December. We forecast real non-oil GDP to decelerate across the GCC in 2016, and we expect this to be reflected in the PMI data for both Saudi Arabia and the UAE. Tightening liquidity and ongoing fiscal consolidation measures are also likely to contribute to a slowdown.

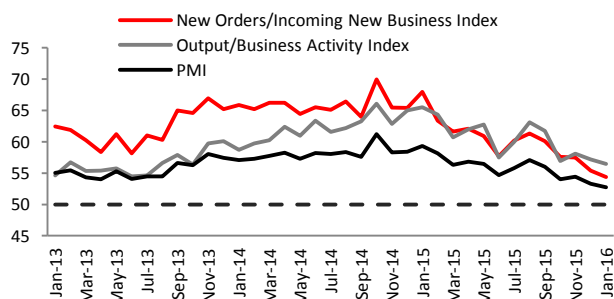
Further loss of economic momentum into 1Q2016

UAE: The headline index moderated to 52.7 in January from 53.3 in December (a reading above 50 indicates expansion). This was its lowest level since March 2012. The moderation was due partly to weaker (but still positive) activity in most of the PMI index's key components. These included new orders and new export orders, suggesting weaker domestic and external demand. Export orders stood at 50.2 in January, just above the key 50 level separating expansion from contraction. The still strong USD and weakening GCC demand were likely key factors.

Weakening GCC demand and strong USD dampening external demand

Fig. 1. UAE: Main PMI index components moderate in January

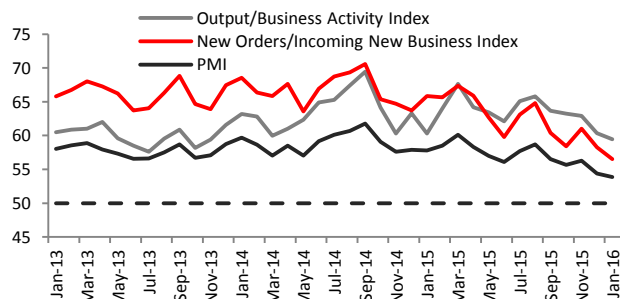
Index (readings above 50 indicate expansion)



Source: Markit Economics

Fig. 2. Saudi Arabia: Output and business activity remain better supported in January

Index (readings above 50 indicate expansion)



Source: Markit Economics

Saudi Arabia: Saudi Arabia's headline PMI softened to 53.9 in January from 54.4 in December. This suggested a further drop in private sector momentum into 1Q2016. This was the lowest reading since the index was launched in August 2009, though it remained expansionary. A number of key components fell, including new orders, new export orders and business activity. New export orders saw a particularly sharp fall to 50.3 from 57.6 in December. We believe this was likely due to the petrochemical sector (given the weak global demand) and December's increase in feedstock prices. The moderation in new orders was less pronounced (56.5 in January versus 58.3 in December). Employment growth accelerated (though it remained weak) likely supported by job creation programmes for Saudi nationals.

Saudi Arabia sees sharp fall in export orders in January, likely linked to petrochemical sector

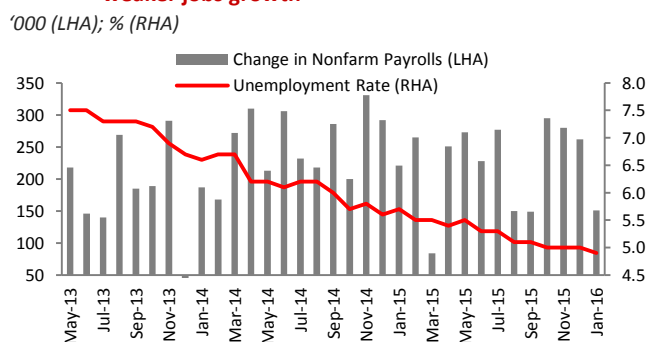
B. G4 Economies

US: Signs labour market tightening, despite jobs growth disappointing

Nonfarm payroll growth moderated to 151K in January, below consensus expectations of 190K and down from 262K in December (revised down from 292K). The softer January reading likely reflected a relative pause, after the strong growth in November and December (partly due to the unseasonably mild winter). Reflecting this, the three-month trend in payroll growth averaged a robust 231K. The weaker employment gain in January was also due to a seasonal reversal of the temporary holiday job creation that occurs in December.

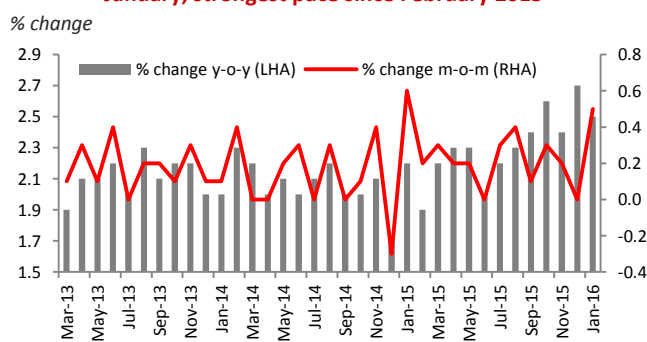
151K jobs created in January, with seasonal factors likely impacting

Fig. 3. US: Unemployment falls to 4.9% in January, despite weaker jobs growth



Source: Bloomberg

Fig. 4. US: Hourly wage growth accelerates to 0.5% in January, strongest pace since February 2015



Source: Bloomberg

Moreover, supporting signs of a tightening in the labour market, the unemployment rate fell to 4.9%. This is equal to the FOMC's median assessment of the longer-run or natural level of unemployment. A further decline in unemployment below this level should put pressure on employers to lift wages. Average hourly wage growth strengthened to 0.5% m-o-m in January, against the consensus forecast of 0.3% and zero growth in December. The participation rate also inched up to 62.7% in January, from 62.6% the previous month. Thus, the labour market remains reasonably strong and above trend, despite a smaller than expected rise in January. The ongoing labour market growth supports our outlook for a June rate hike. We expect the Fed to remain on hold in March, given the volatile start to the year.

Unemployment falls to 4.9% - the Fed's natural level of unemployment

ISM manufacturing: The January data pointed to tentative stabilisation in manufacturing activity. The ISM manufacturing index strengthened moderately to 48.2 in January, up from 48 in December. Areas related to the oil sector and exports remained weak. However, some sectors remained positive, and were less impacted by international developments; these included high end IT and medical equipment. Positively, the new orders index rose to 51.5 in January, from 48.8 in December, implying demand expansion. Manufacturing represents just 12% of GDP, and manufacturing industry employment accounts for around 9% of total nonfarm payrolls. The ISM non-manufacturing index for January raised concerns that weakness in the manufacturing sector may spread to the much larger service sector. The ISM non-manufacturing composite disappointed at 53.5 in January, down from 55.8 in December.

Manufacturing shows tentative signs of stabilisation

UK: BoE keeps rates on hold, downgrades growth outlook

The BoE kept interest rates on hold at its 4 February meeting, in line with expectations. Thus, the Bank Rate remains at 0.5% and the stock of asset purchases at GBP375 billion. However, there were a number of notable developments, indicating that monetary policy will not be tightened any time soon. The vote not to raise rates was unanimous (9-0), for the first time since July 2015, as Ian McCafferty dropped his vote for a hike on the weaker inflation outlook. Adding to the dovish slant, the growth and near-term inflation forecasts were both revised down. Inflation is now forecast to be below 1% in 2016. The inflation forecast for 4Q2016 was lowered by over 30 bps following the fall in energy prices, compared to the last Quarterly Inflation Report (QIR) released in November. The growth forecast for 2016 was reduced to 2.2%, down from 2.5% in November, while the 2017 forecast was lowered to 2.4% from 2.7%. The weaker picture was largely due to a softer global growth outlook (emerging market led), with fiscal expansion and a lower oil price supporting domestic growth. Meanwhile, the BoE now expects average weekly earnings to increase by 3% in 2016, down from the 3.75% in the previous QIR.

BoE votes unanimously to keep rates on hold in February

However, the dovishness of the report was partially counterbalanced by the BoE's medium-term inflation forecast. Inflation is still expected to overshoot the BoE's target in 2018, with an estimate of 2.2% (unchanged). Furthermore, during the press conference Governor Mark Carney pushed back against the market's dovish pricing for rate hikes. He reiterated, as did the MPC meeting minutes, that the next move in policy rates is most likely to be up, despite the market pricing in a good chance of a cut. We maintain our outlook for a November rate hike, though highlight the risk of a later start. A November hike would require the economy continuing to realise above-trend growth, unemployment falling further and the downside risks failing to materialise.

Inflation is still expected to overshoot the 2% target by the end of the forecast period

Japan: Further details of BoJ's negative interest rate policy

The BoJ provided further details of the new deposit rate policy that it announced on 29 January, which will result in negative rates for some bank reserves (please see our **Global Data Watch 1-5 February 2016**). The BoJ estimates the level of financial institutions' reserve balances that will be subject to the -10 bps negative deposit rate at around JPY10 trillion initially, or just 4% of total reserves. The policy becomes effective on 16 February. Moreover, Japanese media have reported that the BoJ's asset purchase programme will not be subject to the negative rate, but rather to a 0% rate (in line with the required reserves that banks are obliged to hold at the central bank). Overall, these indications suggest a relatively limited move into negative interest rate territory than markets had originally expected. We believe this will provide greater space for the BoJ to cut interest rates into negative territory.

Only 4% of total bank reserves at BoJ to be subject to negative interest rates initially

C. Emerging Market Economies

India: RBI remains on hold, fiscal developments critical

The RBI kept interest rates on hold at its 2 February meeting, in line with our own and the market's expectations. The repo rate remained at 6.75%, the reverse repo rate at 5.75% and the cash reserve ratio (CRR) at 4%. Overall, the RBI's statement was similar to that of the December meeting, with the critical difference being the focus on the fiscal budget. The RBI indicated that it will remain accommodative, even having left the policy rate unchanged. However, Governor Raghuram Rajan commented that the bank is awaiting further data on inflation and structural reforms in the FY2016-17 (April-

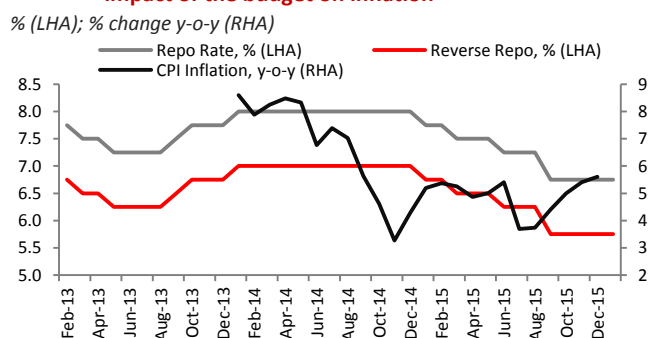
RBI awaiting further fiscal clarity before reviewing policy rates

March) budget. A budget focusing on structural reforms to boost growth, while controlling spending, would create more space for monetary loosening.

The RBI is looking for more evidence that the budget is in line with its January 2017 inflation target of 5%. Central to this will be additional details of the implementation of the seventh pay commission, in particular the size of the pay revisions for public sector employees. The pay commission has recommended a roughly 24% hike; a greater increase could exacerbate inflationary pressures. Given this uncertainty, the RBI did not lower its inflation forecast on the back of the weaker oil price, as some market participants had expected. However, it lowered its 2016-17 growth projection to 7.6% from 7.8% due to weaker investment and external demand. We continue to expect a 25 bps rate cut in April, though this will depend on the upcoming budget (to be released on 29 February).

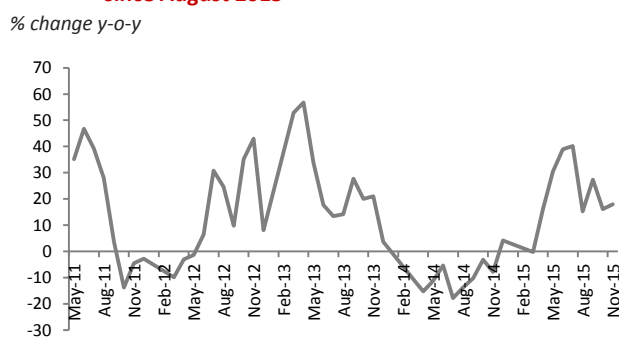
Size of public sector pay revision critical to inflation outlook

Fig. 5. India: RBI keeps rates on hold whilst waiting to gauge impact of the budget on inflation



Source: Bloomberg

Fig. 6. China: Residential property sales losing momentum since August 2015



Source: Bloomberg

China: Eases mortgage rules further to support growth

The PBoC reduced downpayment requirements for homebuyers in most cities last week in its latest effort to shore up the slowing economy. The minimum downpayment required for first time homebuyers seeking a mortgage was lowered to 20%, from 25%. The downpayment for those buying second homes was reduced to 30% from 40%. This was the third cut in the required mortgage downpayment in the past 12 months, with the previous reforms coming in March and September. The cuts in 2015 boosted housing sales, though the latest data show a loss in momentum. However, higher requirements will remain in place in Beijing, Shanghai, Shenzhen and Guangzhou, where demand remains strong. The relaxation of the mortgage policy should help bolster housing demand in lower-tier cities, though oversupply is likely to remain. A rising backlog of unsold new homes is hampering government efforts to spur investment.

Higher mortgage requirements remain for first-tier cities, where housing demand remains strong

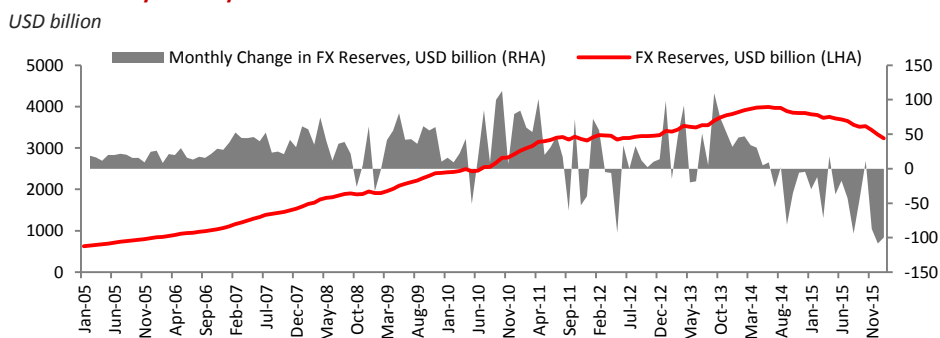
China: FX reserves fall by USD99.5 billion in January

China's FX reserves fell for a third straight month in January, as the PBoC sold USD to support the CNY and limit the pace of capital outflows. The reserves ended the month down -USD99.5 billion at USD3.23 trillion. This was the lowest level since May 2012, albeit higher than the median forecast of USD3.2 trillion expected by consensus (implying a -USD118 billion fall). The January drop was second only to the USD108.3

January drop the second largest monthly fall on record

billion fall in December, the largest monthly decline on record. The PBoC has intensified its efforts to defend the CNY after it staged a surprise devaluation in August 2015 and January 2016. The USD:CNY spot rate began to stabilise in January with strong intervention by the PBoC in the onshore market. We continue to see a gradual and controlled depreciation in the CNY in 2016, in order to support external demand. However, this will have to be managed with capital outflows.

Fig. 7. China: PBoC has intensified efforts to defend the CNY, after weakening the yuan in early January



Source: Bloomberg

II. Economic Calendar

Fig. 8. Upcoming events and data releases

| Time* | Country | Data point | Period | Prior | Consensus |
|---------------------------|--------------|--|--------|--------|-----------|
| Expected this week | | | | | |
| | Saudi Arabia | CPI, y-o-y | Jan | 2.3% | -- |
| | Saudi Arabia | Non-Oil Exports, y-o-y | Dec | -12.6% | -- |
| | Qatar | CPI, y-o-y | Jan | 2.7% | -- |
| Monday 8 Feb | | | | | |
| 16:00 | India | GDP, y-o-y | 4Q | 7.4% | 7.1% |
| 16:00 | India | GDP Annual Estimate, y-o-y | 1Q A | 7.2% | 7.4% |
| Tuesday 9 Feb | | | | | |
| 9:15 | UAE | Dubai Economy Tracker SA | Jan | 51.8 | -- |
| 10:00 | Japan | Machine Tool Orders, y-o-y | Jan P | -25.7% | -- |
| 19:00 | US | JOLTS Job Openings | Dec | 5431 | 5350 |
| 19:00 | US | Wholesale Inventories, m-o-m | Dec | -0.3% | -0.1% |
| Wednesday 10 Feb | | | | | |
| 3:50 | Japan | Housing Loans, y-o-y | 4Q | 2.4% | -- |
| 3:50 | Japan | PPI, y-o-y | Jan | -3.4% | -2.8% |
| 13:30 | UK | Industrial Production, m-o-m | Dec | -0.7% | -0.1% |
| 13:30 | UK | Industrial Production, y-o-y | Dec | 0.9% | 1% |
| 13:30 | UK | Manufacturing Production, m-o-m | Dec | -0.4% | 0.1% |
| 16:00 | US | MBA Mortgage Applications | 5-Feb | -2.6% | -- |
| 19:00 | US | Fed's Yellen to Appear Before House Financial Services Committee | | | |
| 22:30 | US | Fed's Williams Speaks on Health and the Economy in LA | | | |
| | Egypt | Urban CPI, y-o-y | Jan | 11.1% | -- |
| | Egypt | Urban CPI, m-o-m | Jan | -0.1% | -- |
| | Egypt | CPI Core, y-o-y | Jan | 7.2% | -- |
| Thursday 11 Feb | | | | | |
| 4:01 | UK | RICS House Price Balance | Jan | 50% | 52% |
| 17:30 | US | Initial Jobless Claims | 6-Feb | 285K | 280K |
| 17:30 | US | Continuing Claims | 30-Jan | 2255K | 2250K |
| 18:00 | Eurozone | Euro-Area Finance Ministers Meet in Brussels | | | |
| 19:00 | US | Fed's Yellen to Appear Before Senate Banking Committee | | | |
| Friday 12 Feb | | | | | |
| 12:00 | Eurozone | EU Finance Ministers Meet in Brussels | | | |
| 14:00 | Eurozone | Industrial Production SA, m-o-m | Dec | -0.7% | 0.3% |
| 14:00 | Eurozone | Industrial Production WDA, y-o-y | Dec | 1.1% | 0.9% |
| 14:00 | Eurozone | GDP SA, q-o-q | 4Q A | 0.3% | 0.3% |
| 14:00 | Eurozone | GDP SA, y-o-y | 4Q A | 1.6% | 1.5% |
| 16:00 | India | Industrial Production, y-o-y | Dec | -3.2% | -0.4% |
| 17:00 | India | CPI, y-o-y | Jan | 5.6% | 5.3% |
| 17:30 | US | Retail Sales Advance, m-o-m | Jan | -0.1% | 0.1% |
| 17:30 | US | Retail Sales, ex-Auto, m-o-m | Jan | -0.1% | 0% |
| 17:30 | US | Retail Sales, ex-Auto and Gas, m-o-m | Jan | 0% | 0.3% |
| 17:30 | US | Retail Sales Control Group, m-o-m | Jan | -0.3% | 0.3% |
| 19:00 | US | Fed's Dudley Answers Questions at Press Briefing in New York | | | |
| 19:00 | US | U. of Mich. Sentiment | Feb P | 92 | 92.5 |

* UAE time

Source: Bloomberg

Fig. 9. Last week's data

| Time* | Country | Data point | Period | Prior | Consensus | Actual |
|------------------------|--------------|-----------------------------------|--------|----------|-----------|----------|
| GCC Data | | | | | | |
| | UAE | Dubai Airport Cargo Volume, y-o-y | Dec | 3.8% | -- | 5.2% |
| | Qatar | M2 Money Supply, y-o-y | Dec | 3.1% | -- | |
| Monday 1 Feb | | | | | | |
| 5:00 | China | Manufacturing PMI | Jan | 49.7 | 49.6 | 49.4 |
| 6:00 | Japan | Nikkei Japan PMI Mfg | Jan F | 52.4 | -- | 52.3 |
| 9:00 | India | Nikkei India PMI Mfg | Jan | 49.1 | -- | 51.1 |
| 13:00 | Eurozone | Markit Eurozone Manufacturing PMI | Jan F | 52.3 | 52.3 | 52.3 |
| 13:30 | UK | Markit UK PMI Manufacturing SA | Jan | 52.1 | 51.6 | 52.9 |
| 17:30 | US | Personal Income | Dec | 0.3% | 0.2% | 0.3% |
| 17:30 | US | Personal Spending | Dec | 0.5% | 0.1% | 0% |
| 17:30 | US | PCE Deflator, m-o-m | Dec | 0.1% | 0% | -0.1 |
| 17:30 | US | PCE Deflator, y-o-y | Dec | 0.4% | 0.6% | 0.6% |
| 17:30 | US | PCE Core, m-o-m | Dec | 0.2% | 0.1% | 0% |
| 17:30 | US | PCE Core, y-o-y | Dec | 1.4% | 1.4% | 1.4% |
| 19:00 | US | ISM Manufacturing | Jan | 48 | 48.4 | 48.2 |
| Tuesday 2 Feb | | | | | | |
| 9:30 | India | RBI Cash Reserve Ratio | 2-Feb | 4% | 4% | 4% |
| 9:30 | India | RBI Repurchase Rate | 2-Feb | 6.75% | 6.75% | 6.75% |
| 9:30 | India | RBI Reverse Repo Rate | 2-Feb | 5.75% | 5.75% | 5.75% |
| 14:00 | Eurozone | Unemployment Rate | Dec | 10.5% | 10.5% | 10.4% |
| Wednesday 3 Feb | | | | | | |
| 5:45 | China | Caixin China PMI Composite | Jan | 49.4 | -- | 50.1 |
| 6:00 | Japan | Nikkei Japan PMI Composite | Jan | 52.2 | -- | 52.6 |
| 9:00 | India | Nikkei India PMI Composite | Jan | 51.6 | -- | 53.3 |
| 9:30 | Saudi Arabia | Emirates NBD Saudi Arabia PMI | Jan | 54.4 | -- | 53.9 |
| 9:30 | Egypt | Emirates NBD Egypt PMI | Jan | 48.2 | -- | 48 |
| 9:30 | UAE | Emirates NBD UAE PMI | Jan | 53.3 | -- | 52.7 |
| 13:00 | Eurozone | Markit Eurozone Composite PMI | Jan F | 53.5 | 53.5 | 53.6 |
| 13:30 | UK | Markit/CIPS UK Composite PMI | Jan | 55.3 | 55 | 56.1 |
| 14:00 | Eurozone | Retail Sales, m-o-m | Dec | 0% | 0.3% | 0.3% |
| 14:00 | Eurozone | Retail Sales, y-o-y | Dec | 1.6% | 1.5% | 1.4% |
| 16:00 | US | MBA Mortgage Applications | 29-Jan | 8.8% | -- | -2.6% |
| 17:15 | US | ADP Employment Change | Jan | 267K | 195K | 205K |
| Thursday 4 Feb | | | | | | |
| 16:00 | UK | BoE Bank Rate | 4-Feb | 0.5% | 0.5% | 0.5% |
| 16:00 | UK | BOE Asset Purchase Target | Feb | 375B | 375B | 375B |
| 17:30 | US | Initial Jobless Claims | 30-Jan | 277K | 278K | 285K |
| 19:00 | US | Factory Orders | Dec | -0.7% | -2.8% | -2.9% |
| 19:00 | US | Durable Goods Orders | Dec F | -5.1% | -4.5% | -5% |
| 19:00 | US | Durables, ex-Transportation | Dec F | -1.2% | -- | -1% |
| 19:00 | US | Cap Goods Orders, Nondef ex-Air | Dec F | -4.3% | -- | -4.3% |
| Friday 5 Feb | | | | | | |
| 17:30 | US | Trade Balance | Dec | -\$42.2B | -\$43.2B | -\$43.4B |
| 17:30 | US | Change in Nonfarm Payrolls | Jan | 262K | 190K | 151K |
| 17:30 | US | Unemployment Rate | Jan | 5% | 5% | 4.9% |
| 17:30 | US | Average Hourly Earnings, m-o-m | Jan | 0% | 0.3% | 0.5% |
| 17:30 | US | Average Hourly Earnings, y-o-y | Jan | 2.7% | 2.2% | 2.5% |
| 17:30 | US | Labor Force Participation Rate | Jan | 62.6% | 62.7% | 62.7% |

* UAE time

Source: Bloomberg

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