The Week Ahead: RBI expected to cut rates with dovish forward guidance

Economics Team

Monica Malik, Ph.D.
Chief Economist
+971 (0)2 696 8458
Monica.Malik@adcb.com

Thirumalai Nagesh
Economist
+971 (0)2 696 2704
Thirumalainagesh.venkatesh@adcb.com

Contents

India: RBI likely to cut rates with unanimous vote

We expect the RBI to cut its repo rate by 25 bps to 6% at its 2-4 April meeting with a unanimous vote. This would be the second rate reduction in as many meetings since the appointment of Governor Shaktikanta Das in mid-December. We believe that the tone of the meeting is likely to remain dovish with the MPC potentially opening the door for another 25 bps cut in June. With headline inflation remaining at the lower end of the RBI's 4% (+/- 2pp) target range and core inflation showing signs of easing in 2M2019, we expect the RBI to remain comfortable cutting rates to further support economic growth. We envisage that the Fed's more dovish tilt since January will also help the RBI to loosen monetary policy. That said, we do not rule out the possibility of the RBI front-loading its cuts with a single 50 bps move at its April policy meeting, although this is not our base case. On economic projections, we see the possibility of the RBI lowering its GDP growth forecasts for FY2020 (April 2019 - March 2020) to 7.3%, from the 7.4% estimated in February. The inflation forecast is likely to remain largely unchanged, with the MPC highlighting balanced risks to the price outlook. However, some MPC members could highlight the threat of an El-Nino effect (which usually leads to weaker than expected monsoon rainfall), which in turn could result in an increase in vegetable and fruit inflation.

US: Important data week – NFP and ISM manufacturing

A number of important US data releases, including the NFP report, ISM manufacturing (March), retail sales and durable goods (February), are scheduled for this week. The incoming data will be scrutinised closely, especially after 4Q GDP and January personal spending growth surprised to the downside (page 3). Consensus forecasts jobs growth to have rebounded to 175K in March after hitting just 20K in February. The sharp moderation in February hiring was due to temporary factors and is unlikely to have continued into March. Average hourly earnings growth is projected to grow by a healthy 0.3% m-o-m in March, albeit easing from 0.4% in February. Meanwhile, the unemployment rate is estimated to have held steady at 3.8%. The market's focus will also be on the ISM manufacturing data, which is forecast to rise to 54.5 in March from 54.2 in February. The February retail sales will also give an early indication as to whether consumption is showing signs of stabilisation or is continuing to slow.

Global: Turkey and Eurozone inflation

Turkey's March inflation report (3 April) and financial market conditions will also be on the market's radar this week after the TRY once again came under sell-off pressure last week. We expect the market to maintain a cautious approach to high-risk assets, including the TRY, amidst rising global growth uncertainty. Consensus forecasts headline inflation to have eased marginally to 19.6% y-o-y in March, from 19.7% in February, with a softening in food prices. In the Eurozone, the consensus estimates headline inflation to remain steady at 1.5% y-o-y in March, same as in February.

I. Recent Events and Data Releases

A. MENA Economies

Saudi Arabia: Aramco to purchase 70% of SABIC for USD69.1 billion

Funds raised by PIF from sale of SABIC will help fund investment programme

Saudi Aramco is set to purchase a 70% stake in SABIC from the PIF for USD69.1 billion in one of the biggest deals in the history of the global chemicals industry. An outline of the deal was announced in mid-2018, and from an economic perspective, it would provide significant funds to the PIF to progress with its broad-based investment programme. As we have highlighted in previous research, the PIF is set to implement much of the investment projects linked to Saudi Arabia's transformation plan – directly and with FDI. Central to our forecast pick up in Saudi Arabia's real non-oil GDP growth in 2H2019, but particularly from 2020, is higher investment activity supported by this sale of SABIC. The PIF investment programme has not started in a meaningful way, which is also partly due to the design and planning process. The sale will not generate any additional funds for Saudi Arabia, as it shifts the asset from one government entity (PIF) to another (Aramco). The main economic significance is the freeing up of considerable liquidity for PIF, which has been locked up with SABIC and can now be invested.

Purchase of SABIC central to Aramco's transformative downstream growth strategy

Moreover, the acquisition of SABIC will help to boost Aramco's downstream growth plans, with the aim of generating more revenue from high-value petrochemicals, alongside potentially paving the way for the much-awaited Aramco IPO (now slated for 2021). Aramco is looking to increase its global refining capacity from 4.9 million bpd to 8-10 million bpd by 2030, of which it plans to convert 2-3 million bpd into petrochemical products. Aramco will start meeting bond investors this week for its debut international bond, which will help fund SABIC's purchase. Aramco has only issued local currency bonds in the past. Saudi Arabia's energy minister previously said that Aramco's debt issuance would be around USD10 billion, although we believe strong demand could result in a larger size. The recent inclusion of Saudi Arabia in key bond market indices, and the strong fundamentals and creditworthiness of Aramco are key factors that will support demand. Aramco is also expected to raise loans for the acquisition. SABIC and Aramco have stated that the agreed purchase price is SAR123.39 per share – a slight discount from SABIC's closing price on the announcement date. SABIC's remaining 30% of shares will continue to be publicly traded on the Tadawul.

Saudi Arabia: Extending domestic debt curve with March sukuk issue

Ministry of Finance sells 15-year domestic debt for first time in March

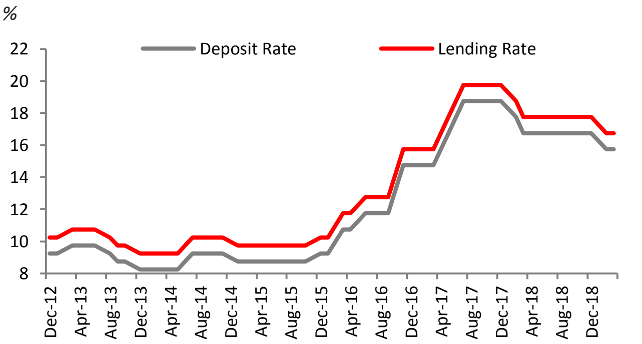
In March, the finance ministry sold some USD1.6 billion in SAR debt with maturities of 10 and 15 years as part of its sukuk issuance programme. Significantly, the 15-year issuance is the longest-dated public debt issued domestically by the government to date, with SAR2.395 billion raised in the 10-year tranche and SAR3.680 billion in the 15-year. The Debt Management Office (DMO) noted that the "the 15-year issuance represents a new benchmark for potential government and private sector issuers to enable them to price off the government's extended yield curve". Moreover, the DMO noted that the longer-dated debt "could be used to support financing long-term projects such as infrastructure projects, the mortgage market, and other types of long-term projects". Saudi Arabia began offering local currency bonds in monthly auctions in mid-2015 to help cover the huge budget deficit caused by low oil prices, although these were suspended in late 2016 as liquidity in the banking system tightened. The government launched monthly sukuk issues again in mid-2017 as domestic liquidity conditions improved.

Egypt: CBE keeps rates on hold at its March meeting

Rise in February headline inflation and last week's EM uncertainties likely to be key factors

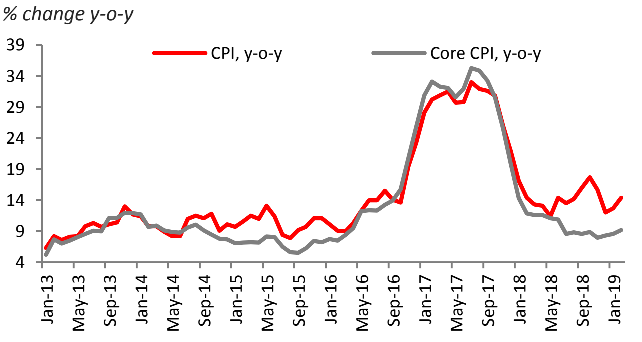
The CBE kept its policy rates steady at its 28 March meeting, with the deposit and lending rates maintained at 15.75% and 16.75% respectively. We and consensus had expected a 100 bps cut, in line with the February rate reduction. A central factor for the CBE remaining on hold was likely the rise in headline inflation in February to 14.4% y-o-y, up from 12.7% in January. The increase was mainly due to certain food items, particularly selected fresh vegetables, while there was limited upward pressure on non-food items. The recent sell-off in EM markets (Turkey-led) was also a potential factor in the decision to keep rates steady. The MPC's post-meeting statement highlighted the weakening global economic activity, ongoing global trade uncertainties and the easing of financial conditions. Given the outlook for mid-year fiscal reforms, including further fuel price liberalisation, we believe that any resumption of the easing cycle will probably be in 2H2019, potentially after the September meeting.

Fig. 1. Egypt: No change in March benchmark rates, after CBE lowers rates by 100 bps in February



Source: CBE

Fig. 2. Egypt: Strengthening of February inflation largely due to food prices



Source: CAPMAS, ADCB calculations

B. G4 Economies

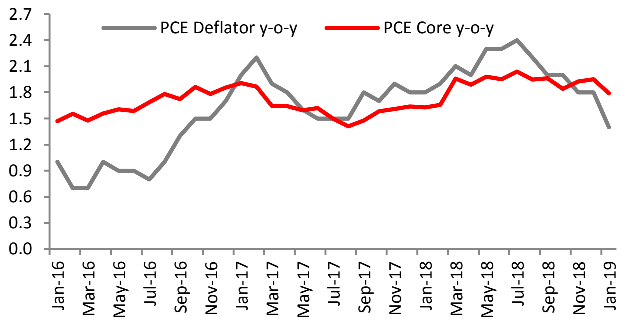
US: January personal spending and 4Q GDP data surprise to downside

Core PCE inflation decelerates to 1.8% y-o-y in January, from 2% in December

Incoming data suggests that the economic momentum in the US is slowing gradually, with both January personal spending and 4Q GDP data surprising to the downside. Personal spending grew by 0.1% m-o-m in January, reversing from a sharp drop of 0.6% in December. Nevertheless, the January print was below the consensus estimate of 0.3%, and showed that the soft consumption activity in late 2018 continued into early 2019. The weaker-than-expected print was largely due to a 0.2% fall in spending on goods, led by the auto component, which contracted by 5.3% m-o-m in January. On the inflation side, core PCE decelerated to 0.1% m-o-m in January, lower than both the consensus estimate and the December reading of 0.2%. This resulted in the y-o-y print slowing to 1.8% in January, from an upwardly revised 2% in December. The deceleration in both monthly and annual core PCE inflation should further support the Fed's patient approach and we believe that the FOMC would like to see inflation above 2% for some time in order to proceed with further rate hikes later in 2019.

Fig. 3. US: Both headline and core PCE inflation surprise to downside and decelerate in January

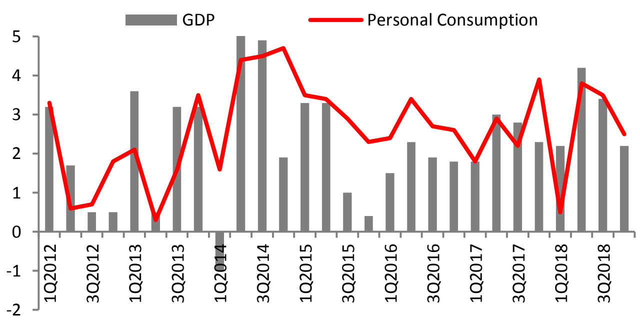
% change y-o-y



Source: Bureau of Economic Analysis

Fig. 4. US: GDP and personal consumption growth weaken for second consecutive quarter in 4Q

% change q-o-q, SAAR



Source: Bureau of Economic Analysis

4Q GDP growth decreases to 2.2% q-o-q SAAR in final estimate, from 2.6% in previous estimate

Meanwhile, the final estimate of 4Q GDP growth was revised down to 2.2% q-o-q SAAR, from 2.6% in the previous estimate. This was again weaker than the consensus expectation of 2.3% growth, although broadly reflecting the contraction in December retail sales. Indeed, the downward revision in 4Q was mainly due to personal consumption growth, which was lowered to 2.5% q-o-q SAAR, from 2.8% earlier. The other major components that saw downward revisions were business fixed investment (intellectual property and residential investment driven) and government spending (partial government shutdown effect).

Fed members reiterate need to remain on hold for now

Fed speak: FOMC members continued to highlight the need to remain patient amidst increasing downside risks to the growth outlook. Notably, Fed Vice Chair Richard Clarida noted that the FOMC can afford to be patient amidst downside global risks and limited inflationary pressures. Furthermore, some Fed members revealed their March 'dot-plot' projections, with Charles Evans and Robert Kaplan forecasting no rate hikes in 2019. Meanwhile, Patrick Harker stated that his current outlook expects "at most" one more hike this year and another in 2020. On rate cuts, a number of Fed speakers, including the dovish members, Neel Kashkari and James Bullard, have argued that it is premature to call for an interest rate reduction in the near term.

UK: Brexit uncertainty continues with failure of third Brexit vote

Third vote on withdrawal agreement fails, further complicating political situation

The UK's MPs last week rejected the Prime Minister Theresa May's Brexit withdrawal agreement for a third time, leading to further uncertainty ahead of the EU-imposed 12 April deadline. The situation is now even more unclear as PM May asked MPs to vote only on the Brexit "withdrawal agreement" rather than the full Brexit deal, which also includes a political declaration regarding the long-term economic relationship. There are indications that PM May could bring her deal for a fourth vote in the coming days, but we do not yet see enough support for the deal to get passed, given the lack of support from the coalition partner − the Democratic Unionist Party (DUP) − and some Eurosceptics. The failure of the fourth vote could result in PM May calling for a general election, although this would require a two-thirds majority in the House of Commons. The support for a general election could fall short of the cut-off mark if there is a serious revolt from the Conservative MPs against a snap election. However, a no-confidence motion against Theresa May would require only a simple majority of MPs and could get passed in Parliament, especially given the Labour party's support for a general election and PM May's lack of authority over divided Conservative parliamentarians. We believe that a general election before the Brexit issue is resolved will further complicate the already complex political landscape in the UK.

Indicative votes to continue on Monday; Special EU summit called for 10 April

The alternative to a general election is to delay Brexit for several months, potentially until end-2019. Given the majority of MPs are against a no-deal exit, a longer extension looks more likely in our view. However, the EU has indicated that the UK must indicate a direction forward for an extension. An extension request would require the UK to hold EU elections. Attention this week will again be on the indicative votes scheduled for Monday in the UK Parliament, after no exit scenario won a majority last week's indicative votes. Meanwhile, the EU President Donald Tusk has called for a special EU summit on 10 April, which is two days ahead of the EU-imposed 12 April deadline. With some EU member states already signalling that their patience is running out with the UK, the conditions for a long Article 50 extension could come with a strict and immovable deadline. With the clock ticking closer to the deadline, three options still look possible: i) a long extension until end-2019; ii) a general election with a long extension; or iii) a no-deal exit if the EU fails to approve a further extension (not our core scenario).

2018 full-year GDP growth unchanged at 1.4% - lowest print since 2012

4Q GDP data: The final estimate of the UK's 4Q GDP growth was kept steady at 0.2% q-o-q, in line with consensus expectations. Full-year 2018 GDP growth was also left unchanged at 1.4%, the weakest growth printed since 2012. However, GDP growth for 3Q was raised to 0.7% q-o-q, from 0.6% in the previous estimate, likely reflecting the positive one-off effects of the warm weather in the summer and increased spending during the football world cup. Overall, with Brexit related political uncertainty unresolved, we expect growth to remain subdued in the near term, led by weak business investments.

II. Economic Calendar

Fig. 5. The week ahead

Time*	Country	Event	Period	Prior	Consensus
Expected this week					
	UAE	UAE PMI	Mar	53.4	
	UAE	M3 Money Supply, m-o-m	Feb	0.1%	
	UAE	CPI, y-o-y	Feb	-2.4%	
	Saudi Arabia	GDP Constant Prices, y-o-y	4Q	2.5%	
	Saudi Arabia	Unemployment Rate (Saudis)	4Q	12.8%	
	Saudi Arabia	Saudi Arabia PMI	Mar	56.6	
	Bahrain	GDP Constant Prices, y-o-y	4Q	1.6%	
	Qatar	GDP Constant Prices, y-o-y	4Q	2.2%	
	Qatar	Qatar PMI	Mar	48.5	
	Egypt	Egypt PMI	Mar	48.2	
Monday, 1 April					
12:30	UK	Markit UK PMI Manufacturing SA	Mar	52	51.2
13:00	Eurozone	Unemployment Rate	Feb	7.8%	7.8%
13:00	Eurozone	CPI Core, y-o-y	Mar A	1%	0.9%
13:00	Eurozone	CPI Estimate, y-o-y	Mar	1.5%	1.5%
16:30	US	Retail Sales Advance, m-o-m	Feb	0.2%	0.3%
16:30	US	Retail Sales, ex-Auto and Gas	Feb	1.2%	0.3%
16:30	US	Retail Sales Control Group	Feb	1.1%	0.3%
17:45	US	Markit US Manufacturing PMI	Mar F	52.5	52.5
18:00	US	ISM Manufacturing	Mar	54.2	54.5
18:00	US	ISM Prices Paid	Mar	49.4	52.5
Tuesday, 2 April					
11:00	Eurozone	ECB's Praet Speaks in Frankfurt			
12:30	UK	Markit/CIPS UK Construction PMI	Mar	49.5	49.7
16:30	US	Durable Goods Orders	Feb P	0.3%	-1.8%
16:30	US	Durables, ex-Transportation	Feb P	-0.2%	0.2%
16:30	US	Cap Goods Shipments, Non-defence, ex-Air	Feb P	0.8%	0%
Wednesday, 3 April					
5:45	China	Caixin China PMI Manufacturing	Mar	49.9	50
11:00	Turkey	CPI, y-o-y	Mar	19.7%	19.6%
11:00	Turkey	CPI Core Index, y-o-y	Mar	18.1%	18%
12:30	UK	Markit/CIPS UK Composite PMI	Mar	51.5	51
13:00	Eurozone	Retail Sales, y-o-y	Feb	2.2%	2.2%
16:15	US	ADP Employment Change	Mar	183K	175K
16:30	US	Fed's Bostic Speaks at American Banker Association Summit			
18:00	US	ISM Non-Manufacturing Index	Mar	59.7	58
Thursday, 4 April					
1:00	US	Fed's Kashkari Speaks in North Dakota			
10:00	Germany	Factory Orders, m-o-m	Feb	-2.6%	0.3%
10:15	India	RBI Repurchase Rate	4-Apr	6.25%	6%
10:15	India	RBI Reverse Repo Rate	4-Apr	6%	5.75%
15:30	Eurozone	ECB Publishes Account of March Meeting			
21:00	US	Fed's Mester Speaks at Banking Conference			
Friday, 5 April					
9:00	Japan	Leading Index CI	Feb P	96.5	97.2
10:00	Germany	Industrial Production SA, m-o-m	Feb	-0.8%	0.5%
16:30	US	Change in Nonfarm Payrolls	Mar	20K	175K
16:30	US	Change in Private Payrolls	Mar	25K	178K
16:30	US	Unemployment Rate	Mar	3.8%	3.8%
16:30	US	Average Hourly Earnings, m-o-m	Mar	0.4%	0.3%
16:30	US	Average Hourly Earnings, y-o-y	Mar	3.4%	3.4%

* UAE time

Source: Bloomberg

Fig. 6. Last week's data

Time*	Country	Event	Period	Prior	Consensus	Actual
GCC Economies						
	Saudi Arabia	M2 Money Supply, y-o-y	Feb	1.1%		2%
	Saudi Arabia	SAMA Net Foreign Assets SAR	Feb	1810.8B		1792.4B
	Bahrain	M2 Money Supply, y-o-y	Jan	2.4%		3.5%
	Bahrain	CPI, y-o-y	Feb	1.4%		0.9%
	Kuwait	CPI, y-o-y	Feb	0.4%		0.6%
Monday, 25 March						
8:30	Japan	All Industry Activity Index, m-o-m	Jan	-0.6%	-0.4%	-0.2%
13:00	Germany	IFO Business Climate	Mar	98.7	98.5	99.6
Tuesday, 26 March						
11:00	Germany	GfK Consumer Confidence	Apr	10.7	10.8	10.4
16:30	US	Housing Starts	Feb	1273K	1210K	1162K
18:00	US	Conf. Board Consumer Confidence	Mar	131.4	132.5	124.1
Wednesday, 27 March						
16:30	US	Trade Balance	Jan	-$59.9B	-$57B	-$51.1B
18:00	US	Current Account Balance	4Q	-$126.6B	-$130B	-$134.4B
Thursday, 28 March						
13:00	Eurozone	M3 Money Supply, y-o-y	Feb	3.8%	3.9%	4.3%
16:30	US	GDP Annualized, q-o-q	4Q T	2.6%	2.3%	2.2%
16:30	US	Personal Consumption	4Q T	2.8%	2.6%	2.5%
16:30	US	Core PCE, q-o-q	4Q T	1.7%	1.7%	1.8%
17:00	Germany	CPI EU Harmonized, y-o-y	Mar P	1.7%	1.6%	1.5%
18:00	US	Pending Home Sales, m-o-m	Feb	4.3%	-0.5%	-1%
	Egypt	Lending Rate	28-Mar	16.75%		16.75%
	Egypt	Deposit Rate	28-Mar	15.75%	15%	15.75%
Friday, 29 March						
3:30	Japan	Jobless Rate	Feb	2.5%	2.5%	2.3%
3:30	Japan	Tokyo CPI, y-o-y	Mar	0.6%	0.9%	0.9%
3:50	Japan	Industrial Production, y-o-y	Feb P	0.3%	-1.1%	-1%
3:50	Japan	Retail Trade, y-o-y	Feb	0.6%	1%	0.4%
11:00	Turkey	Trade Balance	Feb	-2.5B	-2.2B	-2.1B
13:30	UK	Mortgage Approvals	Feb	66.7K	65K	64.3K
13:30	UK	GDP, q-o-q	4Q F	0.2%	0.2%	0.2%
13:30	UK	GDP, y-o-y	4Q F	1.3%	1.3%	1.4%
16:30	US	Personal Income	Feb	-0.1%	0.3%	0.2%
16:30	US	Personal Spending	Feb	-0.6%	0.3%	0.1%
16:30	US	PCE Deflator, y-o-y	Jan	1.8%	1.4%	1.4%
16:30	US	PCE Core, y-o-y	Jan	2%	1.9%	1.8%
18:00	US	New Home Sales	Feb	636K	620K	667K

* UAE time

Source: Bloomberg

This report is intended for general information purposes only. It should not be construed as an offer, recommendation or solicitation to purchase or dispose of any securities or to enter in any transaction or adopt any hedging, trading or investment strategy. Neither this report nor anything contained herein shall form the basis of any contract or commitment whatsoever. Distribution of this report does not oblige Abu Dhabi Commercial Bank PJSC ("ADCB") to enter into any transaction.

The content of this report should not be considered legal, regulatory, credit, tax or accounting advice. Anyone proposing to rely on or use the information contained in the report should independently verify and check the accuracy, completeness, reliability and suitability of the information and should obtain independent and specific advice from appropriate professionals or experts regarding information contained in this report.

Information contained herein is based on various sources, including but not limited to public information, annual reports and statistical data that ADCB considers accurate and reliable. However, ADCB makes no representation or warranty as to the accuracy or completeness of any statement made in or in connection with this report and accepts no responsibility whatsoever for any loss or damage caused by any act or omission taken as a result of the information contained in this report.

Charts, graphs and related data or information provided in this report are intended to serve for illustrative purposes only. The information contained in this report is prepared as of a particular date and time and will not reflect subsequent changes in the market or changes in any other factors relevant to their determination. All statements as to future matters are not guaranteed to be accurate. ADCB expressly disclaims any obligation to update or revise any forward looking statements to reflect new information, events or circumstances after the date of this publication or to reflect the occurrence of unanticipated events.

This report is being furnished to you solely for your information and neither it nor any part of it may be used, forwarded, disclosed, distributed or delivered to anyone else. You may not copy, reproduce, display, modify or create derivative works from any data or information contained in this report.