Economic Research

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The Week Ahead: US political developments and RBI meeting in spotlight

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Contents

US: Democratic Party primaries begin on 3 February

All eyes will be on US political developments this week with the beginning of the Democratic Party presidential primaries in Iowa on 3 February. Recent polling data shows a tight race between Bernie Sanders and Joe Biden, with Elizabeth Warren and Pete Buttigieg also in contention. The Iowa primaries are likely to give us an initial idea of the front runner, but this may not translate into the final nominee. The critical date will be 3 March (Super Tuesday) when 15 states and territories hold their primaries. Putting this into context, 17 of the last 18 Super Tuesday winners (across both the Republican and Democratic parties) have gone on to win their party nomination. It is also possible that the Democratic primary race could stretch until June if it remains a tight contest, as was the case between Barack Obama and Hillary Clinton in 2008. Data-wise, key releases due this week are NFP and ISM. Consensus expects a respectable 160K jobs to have been created in January following the 145K print for December. Wage growth is also forecast to have accelerated to 0.3% m-o-m in January, from 0.1% in December.

China: PBoC cuts rates; January trade data due this week

The Chinese stock market reopened today after the Lunar New Year much lower, down 8.3% at the time of writing. The PBoC cut rates by 10 bps (seven-day reverse repo to 2.4% and 14-day to 2.55%) and injected liquidity into the financial system to provide vital support. Brent crude has softened to USD56.1 p/b amidst increased concerns over the global impact of the coronavirus. The World Health Organisation (WHO) declared a public health emergency at the end of last week, following the sharp increase in new cases within and outside of China. The negative impact of the coronavirus on 1Q data releases is likely to be significant in our view. As such, the focus in the coming week will be on China's trade data for January. Consensus forecasts exports to have contracted by 4.5% y-o-y, after rising by 7.6% in December – the first increase in five months. Import growth is estimated to have softened to 2.0% y-o-y in January (December: 16.3%), likely reflecting reduced household spending during the holiday season as people stayed home and events were cancelled. Elsewhere, headline inflation in Turkey is expected to have accelerated in January to 11.9% y-o-y (December: 11.8%), driven by food and transportation.

India: RBI likely to remain on hold; comments in focus

We and the consensus expect the RBI to keep its benchmark policy rate steady at 5.15% at its 6 February meeting. The MPC is likely to maintain a cautious tone at this meeting, with headline inflation having risen above the RBI's upper bound target of 6.0% in December 2019. Agricultural market prices are indicating that vegetable prices eased somewhat in January, but they are unlikely to help headline inflation fall back within the RBI's target range 4% (+/-2 pp) before February, in our view. The RBI is also likely to wait and see the impact of the personal income tax cuts announced in the FY2021 budget (page 5) on inflation. Overall, we now expect the RBI to remain on hold in 1H2020 but still see the possibility for a 25 bps rate cut in 2H2020.

I. Recent Events and Data Releases

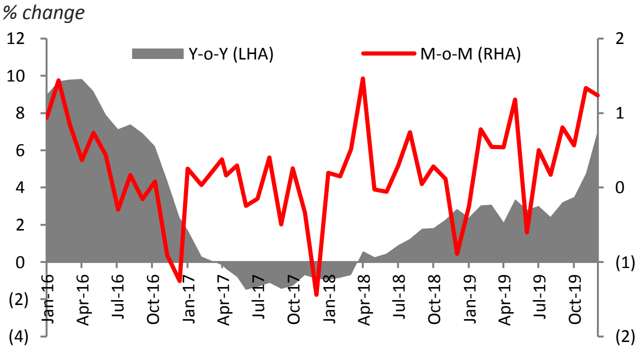
A. MENA Economies

Saudi Arabia: Sharp rise in December private credit with Aramco IPO

Lending conditions eased to support domestic demand for IPO

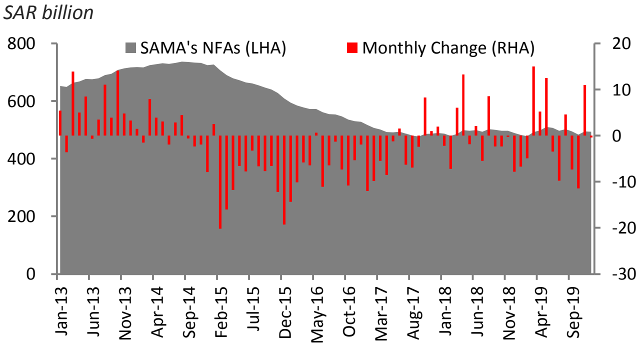
Private sector credit growth accelerated further in December following a pick-up in November. We believe that this strengthening in November and December was linked to the Aramco IPO and the strong domestic interest it attracted. Moreover, SAMA relaxed its lending limits to boost domestic demand for the IPO, with banks permitted to provide leverage to retail customers investing in Aramco at a ratio of 2 to 1 for every SAR, up from the normal regulatory limit of 1 to 1. For more details, please see our note – **Saudi Arabia Economic Update: The big picture after the Aramco IPO**, published on 6 December 2019. Private sector loan growth strengthened to 1.3% m-o-m in November and 1.2% in December, resulting in the annual growth rate accelerating to 4.8% y-o-y and 7.0%, respectively. This was up from a monthly rise of 0.6% m-o-m and 3.5% y-o-y in October. We expect a normalisation in monthly credit growth in the subsequent months with potential for a contraction in January and perhaps February. However, the Aramco-led spike in credit demand will continue to be reflected in the annual private sector loan growth data for most of 2020, albeit dropping out of the data at the end of the year. Nevertheless, we continue to see solid underlying demand for private sector credit with economic activity continuing to gain traction, led by the PIF's investment programme. Demand for mortgage loans is also likely to continue its strong growth in 2020 as the government looks to increase the home ownership of nationals. Total mortgage loans rose to SAR9.3 billion in December 2019 from SAR3.4 billion a year earlier.

Fig. 1. Saudi Arabia: Private sector credit growth expands by 7.0% y-o-y in December – highest since August 2016



Source: SAMA, ADCB calculations

Fig. 2. Saudi Arabia: SAMA's NFA position broadly stable in 2019, albeit fluctuating on monthly basis



Source: SAMA, ADCB calculations

Proxy indicators suggest further rise in economic momentum at end-2019

The sharp rise in loan growth in December did not result in tightening banking sector liquidity, with the Aramco IPO likely also supporting a marked increase in system-wide deposits. Total deposits rose by USD18.2 billion (4.0% m-o-m and 7.3% y-o-y) in December, with the PIF likely placing a significant part of the amount raised with domestic banks rather than with SAMA. Meanwhile, proxy indicators of economic activity continued to point to building economic momentum. Combined points of sale transactions and ATM withdrawals strengthened to 18.3% y-o-y (November: 17.0%) whilst new letters of credit opened rose by 20.9%. Separately, SAMA's net foreign asset (NFA) position was broadly stable in 2019, rising by just 0.9% y-o-y in December to USD494.0 billion. We believe that this stability largely reflects foreign borrowing to help reduce the drawdown in FX reserves. Nevertheless, the need to cover the fiscal deficit was reflected in a number of monetary indicators, with government deposits falling by 5.0% y-o-y in December and loans to the government rising by 25.7% y-o-y.

B. G4 Economies

US: No significant change to Fed monetary policy stance

We expect FOMC to remain on hold throughout 2020

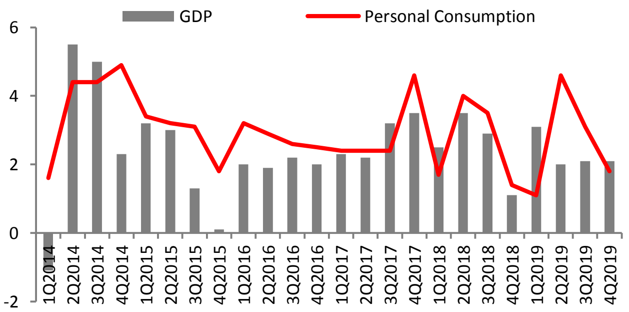
The Fed left the fed funds target rate (FFTR) steady in the range of 1.50%-1.75%, whilst raising interest on excess reserves by 5 bps to 1.60% at its January meeting, as was widely expected. The tone of the overall meeting was neutral in our view. Fed Chair Jerome Powell reiterated that the current stance of monetary policy remains appropriate and a "material reassessment" of the outlook would be necessary for any change in stance. Changes to the January FOMC statement were minimal, with the description of household spending downgraded to "moderate" from "strong" in the December statement. We believe the "moderate" description is a more accurate characterisation and reflects the slowing pace of personal consumption growth since 2Q2019. The second tweak underlined that inflation is expected to return to the FOMC's 2.0% target rather than "near" to its goal in the December statement. During his press conference, Fed Chair Jerome Powell highlighted that the FOMC is not satisfied with inflation running below 2% given the US' prolonged economic expansion and very low unemployment. Overall, the Fed communication was broadly steady and we continue to believe that the FOMC will remain on hold throughout 2020.

Pace of T-bill purchases to continue at USD60 billion per month at least until April

Regarding Treasury Bill purchases, Powell highlighted that repo operations will continue at least through April at the current pace of USD60 billion per month. Subsequent to that, the Fed is likely to adjust the size of purchases to gradually reduce these operations. Powell also noted that the Fed would like to maintain ample reserve balances to support liquidity conditions and indicated that the lower bound for reserves should be USD1.5 trillion. Market economists believe that the pace of T-bill purchases is likely to be slowed to around USD20-30 billion per month from May 2020.

Fig. 3. US: Personal consumption growth slows to 1.8% q-o-q SAAR in 4Q, from 3.2% in 3Q

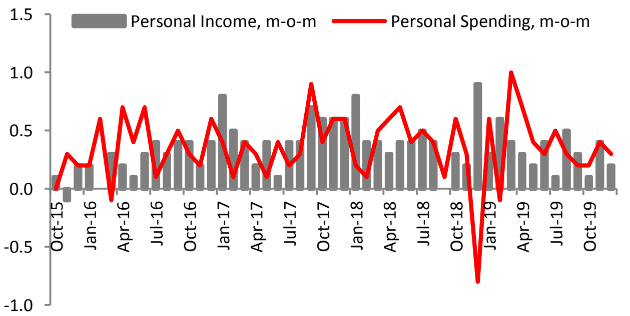
% q-o-q SAAR



Source: Bureau of Economic Analysis

Fig. 4. US: Both personal income and spending growth decelerate in December

% change m-o-m



Source: Bureau of Economic Analysis

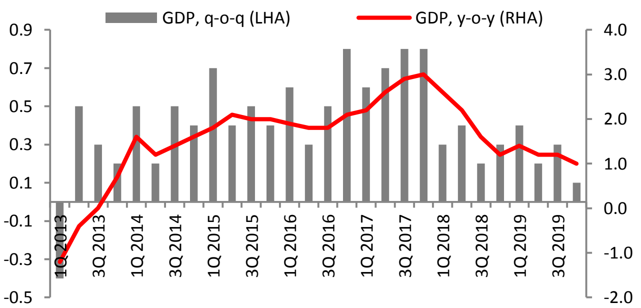
US: Real GDP growth steady at 2.1% in 4Q2019

Headline GDP growth steady, but signs of softening domestic demand

The US economy expanded at a solid pace of 2.1% q-o-q SAAR in 4Q2019 (3Q2019: 2.1%), marginally higher than the consensus expectation of 2.0%. The upside surprise was mainly due to a 1.5 ppt boost from net exports to headline GDP growth, as imports fell by 8.7% q-o-q SAAR in 4Q and exports rose by 1.4%. However, the support from net exports was partly offset by a slowdown in inventory accumulation, which subtracted 1.1 ppt from the headline reading. The fall in imports growth and a slowdown in stock building in 4Q suggests that corporates maintained a cautious approach despite the positive US-China trade developments in the quarter. Personal consumption growth, the key driver of economic activity in previous quarters, slowed to 1.8% in 4Q (3Q: 3.2%). Weakening household spending alongside an ongoing contraction in business investments suggests that domestic demand is witnessing a softening in momentum. The December PCE data released after the 4Q GDP data also showed that personal income growth decelerated to 0.2% m-o-m, from a revised down 0.4% in November. We believe that slowing personal income growth may result in some softening of household activity in 2020, albeit gradual. As such, we expect real GDP growth to decelerate further to around 1.9-2.0% in 2020, from 2.3% in 2019 and 2.9% in 2018. Elsewhere, Eurozone GDP growth slowed to 1.0% y-o-y in 4Q2019, from 1.2% in 3Q.

Fig. 5. Eurozone: Real GDP growth decelerates to 1.0% y-o-y in 4Q2019, from 1.2% in 3Q

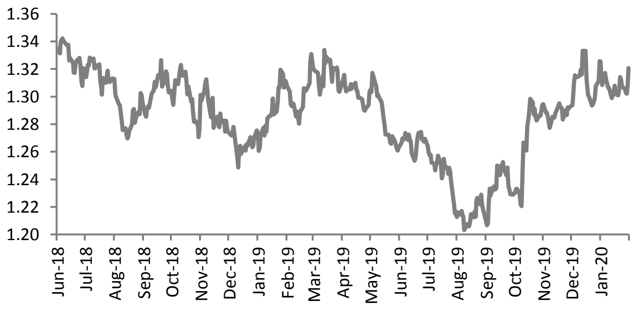
% change



Source: Eurostat

Fig. 6. UK: GBP strengthens against USD at end of last week after BoE leaves policy rate unchanged

GBP:USD



Source: Bloomberg

UK: BoE leaves rates on hold with neutral stance

We retain our call for 25 bps rate cut at BoE's May policy meeting

The BoE kept interest rates steady at its January policy meeting, in line with our expectations. Consensus was divided over the decision. The voting pattern remained unchanged at 7-2, as in the December meeting, suggesting that the MPC members prefer to maintain the status quo for now despite sounding more dovish and highlighting downside risks to the growth outlook ahead of the meeting. We believe that the mixed incoming data prior to the meeting probably played a critical role in causing the majority of the MPC to adopt a wait-and-see stance. The forward guidance maintained an optionality for either a rate cut or rate hike in the near term. However, the earlier forward guidance for a "gradual and limited" rate hike was removed from the MPC statement. The overall tone of the statement and the voting pattern were neutral in our view. Markets are now pricing in a full 25 bps rate cut only in 3Q2020. Our base case remains for the MPC to cut the policy rate by 25 bps at its May meeting, for which the market currently assigns a 57.1% probability.

GDP growth revised down to 0.8% for 2020, from 1.3% in December

Despite adopting a wait-and-see monetary policy stance, the MPC revised down its GDP growth forecasts sharply across the forecast period (2020-2022). The BoE now projects the UK economy to expand at a slower pace of 0.8% in 2020 (December: 1.3%) and 1.5% in 2021 (December: 1.8%). The inflation forecast was also lowered for 2020 to 1.4%, from 1.5% in December, whilst leaving the 2021 estimate steady at 2.0%. The BoE highlighted that the downgrading of the 2020 inflation forecast reflects the expected reduction in water bills and the prevailing excess slack in the economy. We believe that domestic price pressures will be weaker than the MPC's baseline projection of 1.4% in 2020. The recent drop in crude oil and industrial commodity prices also points to increasing downside risks to the inflation outlook, in our view.

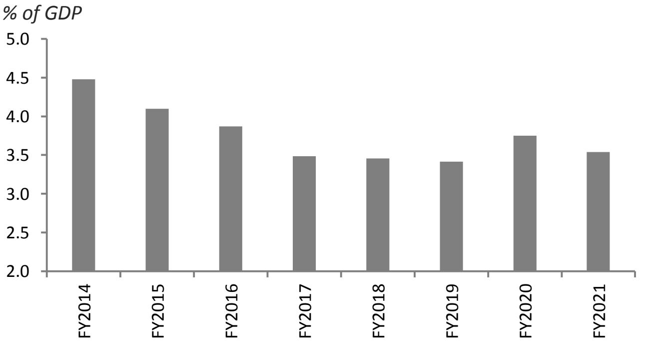
C. Emerging Market Economies

India: Income tax cuts announced in FY2021 budget, as expected

Nominal GDP growth of 10.0% assumed in fiscal deficit calculations

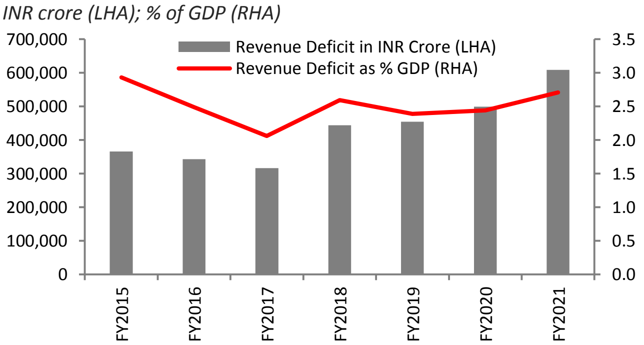
The Indian government announced a fiscally prudent budget for FY2021 (April 2020 - March 2021) on Saturday, along with a number of targeted measures to revive the weak domestic demand. The government aims to narrow the fiscal deficit to 3.5% of GDP, from an estimated 3.8% for FY2020, in line with our expectations. The government deficit forecasts assume a more realistic 10.0% nominal GDP growth, with previous estimates tending to be on the optimistic side. Assuming headline inflation averages close to the RBI's mid-range target of 4.0%, the government is expecting c.6.0% real GDP growth for FY2021. We believe that the real GDP growth forecast of 6.0% is achievable given the government's gradual fiscal consolidation approach. We see a gradual pick-up in economic momentum from 2H2020 driven by increased household spending and a tick-up in private investment activity. However, the revenue assumptions look optimistic in our view, as the government is aiming for an ambitious disinvestment plan of INR2.1 trillion for FY2021 (double than in FY2020). Within this target, the government plans to sell part of its holding in the Life Insurance Corporation of India (LIC), which may face opposition from some senior ruling party members and employees of the organisation. Note that the government failed to issue a foreign-denominated bond this year amidst opposition from market participants and ruling party members, despite announcing that it would in the FY2020 budget. We envisage a higher deficit than the planned 3.5% for FY2021 if the government fails to proceed with the LIC IPO or other asset sales.

Fig. 7. India: Budget sees fiscal deficit narrowing to 3.5% of GDP for FY2021, from 3.8% in FY2020



Source: India Budget, Ministry of Finance, ADCB calculations

Fig. 8. India: Revenue deficit* is unlikely to improve in FY2021 despite expected narrowing of fiscal deficit



* Revenue deficit is current expenditure over total revenue receipts (minus areas such as interest income from grants)

Source: India Budget, Ministry of Finance, ADCB calculations

Disinvestment plans look ambitious

The key policy announcement in the FY2021 budget was income tax cuts for lower and middle-income households (up to INR 1.5 million) to boost their disposable income and help revive the soft domestic demand. On the expenditure side, the government adopted a targeted spending approach to bolster growth, with some moderate increase in capital expenditure. We believe that the increased capex spending will not be sufficient to revive investment activity meaningfully, but should result in a gradual pick-up. The Indian equity market reacted negatively to the budget announcement on Saturday and dropped by 2.5%, after limited support measures to the economy were announced. On the currency front, we see potential for the INR to weaken from the current level of 71.35 against the USD in the upcoming months.

II. Economic Calendar

Fig. 9. The week ahead

Time*	Country	Event	Period	Prior	Consensus
Expected this week					
	UAE	CPI, y-o-y	Dec	-1.4%	
	Qatar	GDP Constant Prices, y-o-y	3Q	-1.4%	
Monday, 03 February					
11:00	Turkey	CPI, y-o-y	Jan	11.8%	11.9%
11:00	Turkey	CPI Core Index, y-o-y	Jan	9.8%	9.7%
13:00	Eurozone	Markit Eurozone Manufacturing PMI	Jan F	47.8	47.8
13:30	UK	Markit UK PMI Manufacturing SA	Jan F	49.8	49.8
18:45	US	Markit US Manufacturing PMI	Jan F	51.7	51.7
19:00	US	ISM Manufacturing	Jan	47.2	48.5
19:00	US	ISM Prices Paid	Jan	51.7	51.5
22:00	Eurozone	ECB President Lagarde Attends Reception in Frankfurt			
Tuesday 4 February					
1:00	US	Fed's Bostic Discusses Big Data, AI and Machine Learning			
8:15	Saudi Arabia	IHS Markit Saudi Arabia PMI	Jan	56.9	
8:15	UAE	IHS Markit UAE PMI	Jan	50.2	
8:15	Egypt	IHS Markit Egypt PMI	Jan	48.2	
19:00	US	Factory Orders	Dec	-0.7%	1.2%
19:00	US	Durable Goods Orders	Dec F	2.4%	2.4%
19:00	US	Capital Goods Shipments, Non-defence, ex-Air	Dec F	-0.4%	
Wednesday, 5 February					
5:30	Japan	BOJ's Wakatabe Speech in Ehime			
5:45	China	Caixin China PMI Services	Jan	52.5	52.0
12:10	Eurozone	ECB Vice President Guindos Speaks in Frankfurt			
13:30	UK	Markit/CIPS UK Services PMI	Jan F	52.9	52.9
14:00	Eurozone	Retail Sales, y-o-y	Dec	2.2%	2.3%
14:00	Qatar	Qatar Financial Center PMI	Jan	49.4	
15:30	Eurozone	ECB Chief Economist Lane Speaks in Berlin			
17:15	US	ADP Employment Change	Jan	202K	158K
17:30	US	Trade Balance	Dec	-$43.1B	-$48.1B
19:00	US	ISM Non-Manufacturing Index	Jan	55.0	55.1
Thursday, 6 February					
10:15	India	RBI Repurchase Rate	6-Feb	5.15%	5.15%
10:15	India	RBI Reverse Repo Rate	6-Feb	4.9%	4.9%
10:15	India	RBI Cash Reserve Ratio	6-Feb	4.0%	4.0%
12:20	Eurozone	ECB President Lagarde Speaks in Brussels			
18:15	US	Fed's Kaplan Speaks on Economic Outlook in Dallas			
Friday, 7 February					
4:15	US	Fed's Quarles Discusses Monetary Policy and Economic Outlook			
9:00	Japan	Leading Index	Dec P	90.8	91.3
17:30	US	Change in Nonfarm Payrolls	Jan	145K	160K
17:30	US	Change in Manufacturing Payrolls	Jan	-12K	-10K
17:30	US	Unemployment Rate	Jan	3.5%	3.5%
17:30	US	Average Hourly Earnings, m-o-m	Jan	0.1%	0.3%
17:30	US	Average Hourly Earnings, y-o-y	Jan	2.9%	3.0%
17:30	US	Labor Force Participation Rate	Jan	63.2%	63.2%
19:00	US	Wholesale Inventories, m-o-m	Dec F	-0.1%	-0.1%
20:00	US	Fed Releases Semi-Annual Monetary Policy Report to Congress			
	China	Exports, y-o-y	Jan	7.6%	-4.5%
	China	Imports, y-o-y	Jan	16.3%	2.0%
	China	Trade Balance	Jan	$46.79B	$36.8B
	China	Foreign Reserves	Jan	$3107.9B	$3095.0B

* UAE time
Source: Bloomberg

Fig. 10. Last week's data

Time*	Country	Event	Period	Prior	Consensus	Actual
GCC Economies						
	Saudi Arabia	SAMA Net Foreign Assets SAR	Dec	1854.1B		1852.6B
	Saudi Arabia	M3 Money Supply, y-o-y	Dec	5.2%		7.1%
	Qatar	QCB Int'l Reserves & Foreign Currency Liquidity QAR	Dec	197.6B		198.4B
Monday, 27 January						
19:00	US	New Home Sales	Dec	697K	730K	694K
19:30	US	Dallas Fed Manufacturing Activity	Jan	-3.2	-2.0	-0.2
Tuesday, 28 January						
17:30	US	Durable Goods Orders	Dec P	-3.1%	0.3%	2.4%
17:30	US	Durables, ex-Transportation	Dec P	-0.4%	0.3%	-0.1%
17:30	US	Cap Goods Orders, Non-defence, ex-Air	Dec P	0.1%	0.2%	-0.9%
17:30	US	Cap Goods Shipments, Non-defence, ex-Air	Dec P	-0.3%	0.2%	-0.4%
19:00	US	Conf. Board Consumer Confidence	Jan	128.2	128.0	131.6
19:00	US	Richmond Fed Manufacturing. Index	Jan	-5.0	-3.0	20.0
Wednesday, 29 January						
13:00	Eurozone	M3 Money Supply, y-o-y	Dec	5.6%	5.5%	5.0%
17:30	US	Wholesale Inventories, m-o-m	Dec P	0.1%	0.1%	-0.1%
19:00	US	Pending Home Sales, m-o-m	Dec	1.2%	0.5%	-4.9%
23:00	US	FOMC Rate Decision (Upper Bound)	29-Jan	1.75%	1.75%	1.75%
23:00	US	FOMC Rate Decision (Lower Bound)	29-Jan	1.5%	1.5%	1.5%
23:00	US	Interest Rate on Excess Reserves	30-Jan	1.55%	1.55%	1.6%
Thursday, 30 January						
14:00	Eurozone	Economic Confidence	Jan	101.3	101.8	102.8
14:00	Eurozone	Unemployment Rate	Dec	7.5%	7.5%	7.4%
16:00	UK	Bank of England Bank Rate	30-Jan	0.75%	0.75%	0.75%
16:00	UK	BOE Corporate Bond Target	Jan	10B	10B	10B
16:00	UK	BOE Asset Purchase Target	Jan	435B	435B	435B
17:30	US	GDP Annualized, q-o-q	4Q A	2.1%	2.0%	2.1%
17:30	US	Personal Consumption	4Q A	3.2%	2.0%	1.8%
17:30	US	Core PCE, q-o-q	4Q A	2.1%	1.6%	1.3%
Friday, 31 January						
3:30	Japan	Tokyo CPI, ex-Fresh Food, y-o-y	Jan	0.8%	0.8%	0.7%
3:50	Japan	Retail Sales, y-o-y	Dec	-2.1%	-1.6%	-2.6%
3:50	Japan	Industrial Production, m-o-m	Dec P	-1.0%	0.7%	1.3%
3:50	Japan	Industrial Production, y-o-y	Dec P	-8.2%	-3.6%	-3.0%
5:00	China	Manufacturing PMI	Jan	50.2	50.0	50.0
5:00	China	Non-manufacturing PMI	Jan	53.5	53.0	54.1
13:30	UK	M4 Money Supply, y-o-y	Dec	4.5%		3.8%
14:00	Eurozone	GDP SA, q-o-q	4Q A	0.3%	0.2%	0.1%
14:00	Eurozone	GDP SA, y-o-y	4Q A	1.2%	1.1%	1.0%
14:00	Eurozone	CPI Estimate, y-o-y	Jan	1.3%	1.4%	1.4%
14:00	Eurozone	CPI Core, y-o-y	Jan P	1.3%	1.2%	1.1%
17:30	US	Personal Income	Dec	0.4%	0.3%	0.2%
17:30	US	Personal Spending	Dec	0.4%	0.3%	0.3%
17:30	US	PCE Deflator, m-o-m	Dec	0.1%	0.2%	0.3%
17:30	US	PCE Deflator, y-o-y	Dec	1.4%	1.6%	1.6%
17:30	US	PCE Core Deflator, y-o-y	Dec	1.5%	1.6%	1.6%
17:30	US	PCE Core Deflator, m-o-m	Dec	0.1%	0.1%	0.2%
18:45	US	MNI Chicago PMI	Jan	48.9	48.9	42.9
19:00	US	University of Michigan Consumer Sentiment	Jan F	99.1	99.1	99.8

* UAE time

Source: Bloomberg

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