

## The Week Ahead: US PCE inflation and global protectionism in spotlight

### ► US: February PCE inflation and Fed speakers

This week will be a quieter one following the FOMC meeting last week (page 3). The main data releases from the US will be February PCE inflation and final 4Q GDP. Consensus projects core PCE growth softened to 0.2% m-o-m in February, after the seasonal jump in January (0.3% m-o-m), normalising back to recent trend levels. Meanwhile, personal spending growth is expected to remain steady at 0.2% m-o-m in February, reflecting the subdued retail activity in recent months. Meanwhile, the final estimate of 4Q GDP growth is forecast to have accelerated to 2.7% q-o-q saar (2.5% previously), likely due to upward revisions in investment in structures and inventories. A number of FOMC members have speaking engagements this week, including Randal Quarles, William Dudley and Raphael Bostic. Fed speeches will be closely watched for possible details on dot plot projections vis-à-vis the views of both voting and non-voting members. We continue to expect a total of three 25 bps rate hikes in 2018, with one each in June and December.

### ► Global: Trade tensions escalate with US targeting China

The key concern of markets remains the escalation in trade tensions between the US and China. This is particularly after US President Donald Trump signed an executive order on 22 March imposing tariffs on Chinese imports worth at least USD50 billion. The detailed list of the affected products will be released within 15 days and then there will be a further 30-day public comment period before they take effect. China's response to the US has remained muted so far with tariffs of either 15% or 25% imposed on US products worth just USD3 billion (c. 128 items), though it has warned there could be a stronger response to US protectionist measures in the near future. We believe that any additional response from China is likely to be smaller in value than the proposed US measures, though a weakening of the CNY is a possibility. We believe that the total economic effect of the measures is likely to be minimal at this point, though the rise in protectionism is a concern. Meanwhile, the US announced a temporary exemption on aluminium and steel tariffs for the EU, alongside other countries including Argentina, Brazil and South Korea.

### ► MENA: Egypt rate decision and Saudi FTSE decision

We expect the Central Bank of Egypt (CBE) to again reduce benchmark interest rates by a further 100 bps at its 29 March MPC meeting, as it did at the February meeting. Inflation continues to decelerate, with the February print softening to within the central bank's year-end target of 13% ( $\pm 3$  pp). In total we expect 300-400 bps of rate cuts by the CBE in 2018 with a 100 bps cut already delivered. Egypt will also hold presidential elections on 26-28 March, with President Abdel Fattah el-Sisi expected to comfortably secure a second term. Thus, we see wider economic policy remaining steady. Meanwhile, Saudi Arabia is expected to be upgraded to the FTSE Russell emerging market index on 28 March (announcement after the close of the US market). Such an announcement, though not directly related, would also further boost market confidence in a similar move by MSCI in June.

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## I. Recent Events and Data Releases

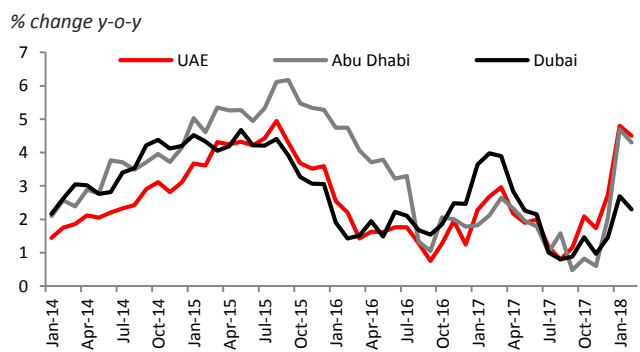
### A. MENA Economies

#### UAE: Abu Dhabi and Dubai inflation figures moderate marginally in February

Consumer price inflation in February moderated marginally in both Abu Dhabi and Dubai on a year-on-year basis, largely on the back of the transportation and housing sectors. In Abu Dhabi, headline inflation slowed to 4.3% y-o-y in February (January: 4.7%) after prices contracted by 0.3% m-o-m (January: 3.1%). The monthly contraction was mainly due to a 2.5% m-o-m drop in transportation prices. Other sectors also saw prices fall but at a more contained pace. In the case of Dubai, yearly inflation decelerated to 2.3% in February (January: 2.7%). Monthly inflation fell by 0.4% m-o-m with housing inflation contracting by 1% m-o-m. We believe that overall the data reflects the weak domestic demand in Dubai, which is resulting in an absence of signs of secondary inflation following the introduction of VAT. Rather, there were some signs of weakening prices of food (Abu Dhabi) and clothing (Dubai), which could be due to retailers reducing prices to support demand.

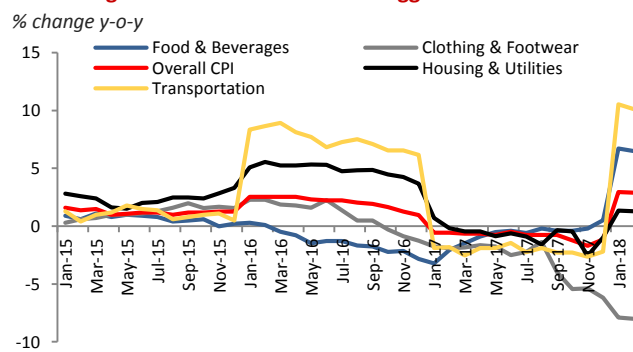
*Inflation data highlights weak underlying consumption backdrop*

**Fig. 1. UAE: Inflation softens moderately in February, though remains elevated due to VAT introduction**



Source: Federal Competitiveness and Statistics Authority; Statistics Centre Abu Dhabi; Dubai Statistics Center

**Fig. 2. Saudi Arabia: Rise in consumer prices expected to feel greater than inflation data suggests**



Source: General Authority for Statistics

#### Saudi Arabia: Headline inflation moderately softer in February

Annual inflation softened marginally in February to 2.9% from 3% in January though remained elevated due to the introduction of VAT. The deceleration was largely due to food inflation slowing to 6.5% y-o-y in February from 6.8% y-o-y in the previous month. We highlight that Saudi Arabia changed the weighting of its inflation basket from January and we believe that the impact of fiscal reform measures (5% VAT and reductions in fuel and electricity subsidies) will likely be greater than suggested by the headline print. We expect private consumption activity to remain weak, though the impact of fiscal reforms on Saudi families with government handout packages should be largely negated. As with the UAE data, there are no signs of secondary inflation from the fiscal reforms.

*Yearly moderation in CPI partly due to softening food price inflation*

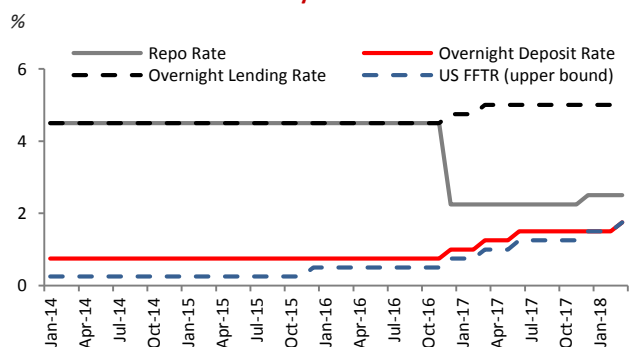
#### Qatar: Central bank raises benchmark deposit rate

The Qatar Central Bank followed the Fed at the end of last week by raising its benchmark discount rate by 25 bps to 1.75%. However, both the repo rate and the overnight lending rates were held steady at 2.5% and 5% respectively. These moves were in line with our

*Qatar keeps repo rate steady after raising in December*

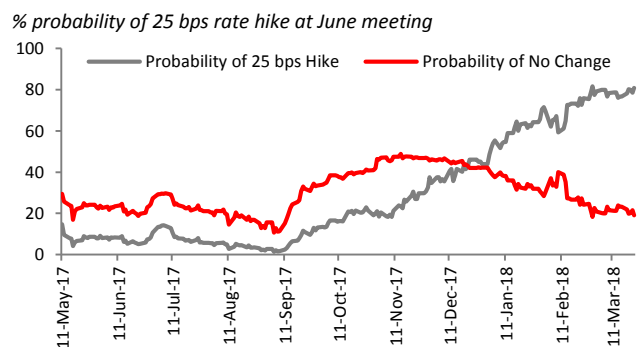
expectations. We had highlighted in our previous research that the repo rate might be held steady this time after some signs of stabilisation in the banking sector, including a gradual rise in non-resident deposits from end-2017. Moreover, weakness in the non-hydrocarbon economy continues. The decision last week was a departure from the December policy decision when the repo rate was raised by 25 bps. Please see our note, **GCC Economic Update – Regional central banks raise rates following Fed hike**, published on 22 March 2018.

**Fig. 3. Qatar: Central bank looks to limit impact of rate rises on economic activity**



Source: Qatar Central Bank, Federal Reserve

**Fig. 4. Market expectation of FFTR rate hike at June meeting above 75%**



Source: Bloomberg

## B. G4 Economies

### US: Fed raises FFTR in March; two more hikes expected in 2018

The Fed raised the FFTR by 25 bps to 1.75% (upper bound) on 21 March, in line with our and the market's expectations. The updated dot plot and economic projections presented a slightly hawkish tilt to the policy meeting though the tone of recently appointed Fed Chair Jerome Powell during the post-meeting conference was broadly balanced, in our view. The median 'dot plot' projections continued to suggest 75 bps of rate hikes in 2018, though the dot distribution suggested that it was a very close call between three or four rate hikes. Notably, three participants shifted their stance to the four rate hike camp at the March meeting from three hikes in December, taking the total to six members now expecting four rate hikes in the dot plot. Six FOMC members also expect a total of three increases in 2018. The 2019 median dot plot forecast was upgraded to three hikes (two previously) with two more rate hikes expected in 2020 (1.5 in December). Moreover, the long-term rate was revised up to 2.9% at the March meeting from 2.8% in December. A key take-away from the dot plot trajectory is that the FOMC participants are now expecting the FFTR in 2020 to be higher than the long-term rate, suggesting the need for a tighter monetary policy stance.

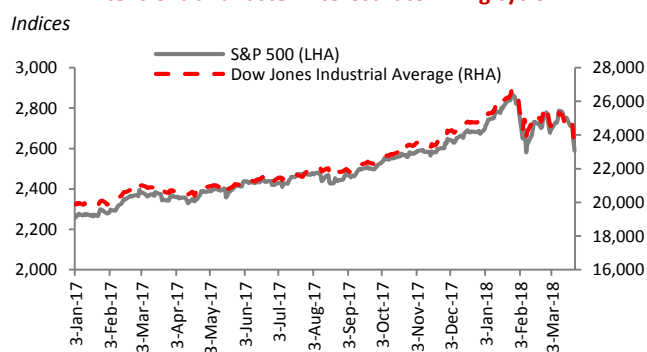
*Fed Chair Powell started with a 25 bps rate hike in March, taking FFTR upper bound target to 1.75%*

The FOMC statement highlighted that the Fed board members are increasingly confident about the near-term economic outlook for the US. The FOMC's growth and inflation forecasts were upgraded, whilst unemployment rate projections were lowered. The 2018 real GDP growth estimate was revised up to 2.7% (from 2.5% previously) with 2.4% forecast for 2019 (December: 2.1%) on the back of the expansionary fiscal backdrop. Given the stronger growth outlook, the FOMC now sees the unemployment rate to fall to 3.8% in 2018 (December: 3.9%) and 3.6% in both 2019 and 2020 (previously 3.9% for 2019 and 4% for 2020). Thus, the Fed board expects tight labour market conditions to feed into inflationary pressures gradually and has upgraded its 2019 and 2020 inflation

*Real GDP growth revised up to 2.7% and 2.4% in 2018 and 2019 respectively*

projections to 2.1% from 2% in December. Consensus was expecting the inflation estimate to have remained steady; the increase also contributed to the moderately more hawkish tone. However, the 2018 inflation forecast was left untouched at 1.9%. During the press conference, Fed Chair Powell emphasised that the Fed's inflation target is symmetric and that the board will be comfortable with inflation above target for a period of time.

**Fig. 5. US: Equity markets worry about increasing trade tensions and faster interest rate hiking cycle**



Source: Bloomberg

**Fig. 6. US: Dollar index continues its downtrend despite Fed rate hiking cycle**



Source: Bloomberg

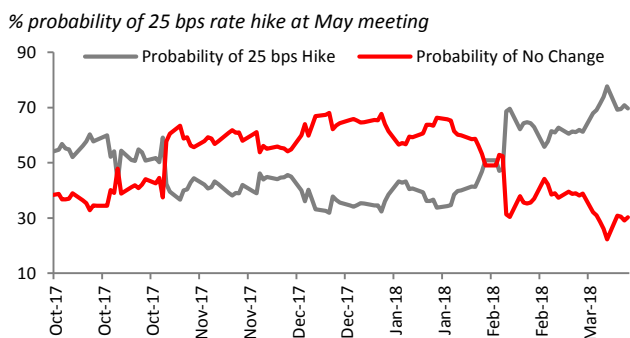
During the press conference, Powell noted that he is carefully considering holding more post-meeting press conferences but has not yet decided. He also added that more frequent press conferences do not signal anything about the path of policy rates. When asked about financial imbalances, Powell argued that the committee sees moderate vulnerabilities overall. On the whole, the communication suggests that financial market imbalances in some asset classes will not halt the interest rate hiking cycle. Looking ahead, we continue to see two additional 25 bps rate hikes in 2018 – one in June and the other in December – although upside risks to this view remain.

*We expect three 25 bps rate hikes in 2018*

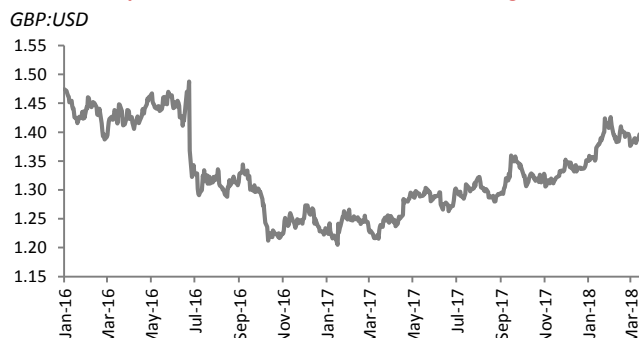
## UK: Hawkish tilt to BoE's March meeting

The BoE kept its policy rate steady at 0.5% at its 22 March meeting, in line with our and the market's expectations. The tone of the meeting was more hawkish than markets anticipated, with two out of seven MPC members voting for a 25 bps hike, compared with a unanimous vote in February to keep rates steady. We believe that the shift in voting pattern has considerably increased the chance of a 25 bps rate hike in May, though there was no explicit guidance regarding "the coming months" in the communication. Notably, the BoE added the "coming months" phrase to the September 2017 statement ahead of the November rate hike. We envisage that the BoE might have felt that explicit guidance was not necessary at this point given the markets have already priced in a May rate hike. Nevertheless, the BoE highlighted that "ongoing tightening of monetary policy over the forecast period will be appropriate", whilst underlining that the hikes will be gradual and limited. The BoE continued to base its rate hike guidance on wage growth and unit labour costs and expressed increasing confidence that both will pick up to target-consistent rates.

*We expect BoE to hike policy rate by 25 bps to 0.75% in May*

**Fig. 7. UK: Market expectation of May rate hike by BoE is around 70%**

Source: Bloomberg

**Fig. 8. UK: GBP continues to strengthen amid rising rate hike expectations and Brexit transition deal agreement**

Source: Bloomberg

The minutes of the March meeting highlighted that the BoE staff had lowered the 1Q2018 GDP growth forecast to 0.3% q-o-q (February: 0.4%), citing the effect of snow-related disruption on economic activity. The committee also acknowledged that the deceleration of headline inflation in February to 2.7% y-o-y was 0.2 pps lower than the BoE projection. The MPC underlined that the pass-through of the GBP depreciation continue to make a positive, but diminishing contribution to inflation in the upcoming period. However, the minutes noted that domestic price pressures “had picked up slightly” in recent months and further firming is expected in the coming months. This was largely based on the assumption that ‘the steady absorption of slack reduced the degree to which it is appropriate for the MPC to accommodate an extended period of inflation above the target’. We expect the BoE to hike the policy rate by 25 bps in May and remain on hold for the rest of the year.

*BoE lowers 1Q GDP growth forecast to 0.3% q-o-q, from 0.4% in February*

### UK: Mixed data – inflation softening but wage growth picking up

The UK data presented a mixed picture last week with inflation surprising to the downside whilst wage growth showed some signs of a pick-up. Headline inflation decelerated to 2.7% y-o-y in February – lower than the consensus estimate of 2.8% and the January print of 3%. Core inflation also softened to a seven-month low of 2.4% in February (January: 2.7%), again lower than the consensus estimate of 2.5%. The softening in January inflation was driven by three factors: (i) fading GBP pass-through effects; ii) weakness in underlying demand; and (iii) favourable base effects in the food, energy and hotel sub-components. Goods inflation, which reflects import costs and currency pass-through effects, decelerated for a second consecutive month, suggesting that the moderation is likely to continue in the near term. Moreover, services inflation recorded the lowest reading since March 2017, indicating that domestic price pressures remain subdued. Looking ahead, we envisage some volatility in the March and April inflation readings, largely due to the timing of Easter. Notably, core inflation is likely to accelerate to 2.6% y-o-y in March, driven by a sharp rise in airfares and increased hotel prices. However, we expect overall headline inflation to ease gradually and reach close to 2% by the end of 2018.

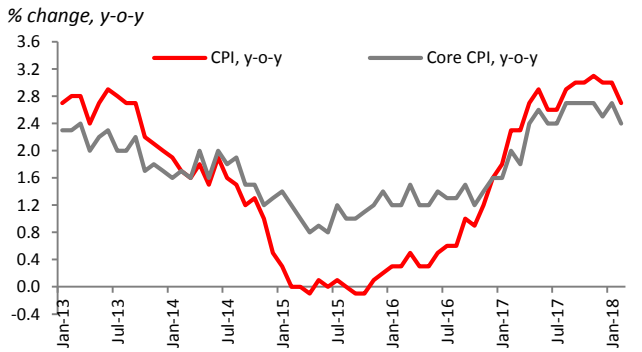
*Headline inflation moderates to 2.7% y-o-y in February from 3% in January*

Meanwhile, average weekly earnings accelerated to 2.8% in the 3M period to January – higher than both the consensus estimate (2.6%) and the upwardly revised December print (2.7%). Weekly earnings excluding bonuses also picked up to 2.6%, though came in line with market expectations. Moreover, the unemployment rate also fell back to a 42-year low of 4.3% in January after rising to 4.4% in December. We believe that the broad-

*Average weekly earnings pick up to 2.8% in January, beating consensus estimate of 2.6%*

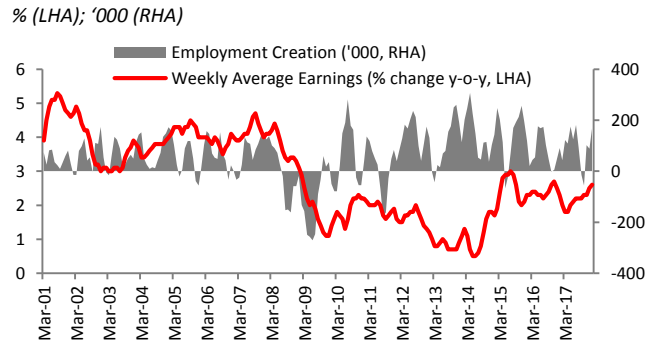
based pick-up in the labour market data in January was partly due to favourable base effects. Hence, we would like to wait for more data in the upcoming months to confirm any sustainable pick-up in wage growth.

**Fig. 9. UK: Both headline and core inflation fall more than expected in February**



Source: UK Office for National Statistics

**Fig. 10. UK: Wage growth picks up surprisingly in January on further gains in employment**



Source: UK Office for National Statistics

**UK-EU: Leaders approve UK transition deal**

EU leaders approved the UK transition deal last week, paving the way for a smooth exit from the EU. The transition will start from 31 March 2019 and remain in place for 21 months. According to the deal, the UK will continue to pay into the EU budget and will be permitted to initiate trade deal negotiations with third-party countries. However, any such trade deals cannot take effect until the transition period ends. Moreover, EU citizens entering the UK will continue to receive the same rights they do now. The issues related to the Irish border, the jurisdiction of the European Court of Justice and the status of Gibraltar are yet to be resolved. Notably, the negotiations over the Irish border remain a major sticking point, though both parties agreed to follow the EU rules and a customs union until there is mutual agreement on the issue. Looking ahead, we believe that attention will now shift to negotiating a trade deal between the UK and the EU. Given the positive political developments and hawkish BoE meeting last week, GBP:USD has strengthened to 1.417.

*Transition deal agreed and signed between EU and UK*

## II. Economic Calendar

Fig. 11. The week ahead

Time*	Country	Event	Period	Prior	Consensus
<b>MENA data</b>					
	UAE	Dubai Airport Cargo Volume, y-o-y	Feb	-2.9%	
	Saudi Arabia	Unemployment Rate (Saudis)	4Q	12.8%	
	Saudi Arabia	GDP Constant Prices, y-o-y	4Q	-0.4%	
	Saudi Arabia	M2 Money Supply, y-o-y	Feb	0.5%	
	Saudi Arabia	SAMA Net Foreign Assets, SAR	Feb	1825.2B	
	Bahrain	GDP Constant Prices, y-o-y	4Q	3.6%	
	Kuwait	M2 Money Supply, y-o-y	Jan	3.8%	3.4%
	Qatar	Trade Balance Month	Feb	16352M	
	Qatar	GDP Constant Prices, y-o-y	4Q	1.9%	
	Qatar	M2 Money Supply, y-o-y	Feb	19.6%	
	Egypt	Lending Rate	29-Mar	18.75%	
	Egypt	Deposit Rate	29-Mar	17.75%	
<b>Monday, 26 Mar</b>					
13:30	Eurozone	ECB's Weidmann Gives Speech in Austrian Central Bank			
16:30	US	Chicago Fed National Activity Index	Feb	0.1	0.2
20:30	US	Fed's Dudley Speaks on the Future of Financial Regulation			
<b>Tuesday, 27 Mar</b>					
0:30	US	Fed's Mester Speaks on Monetary Policy			
3:10	US	Fed's Quarles to Speak in Atlanta			
12:00	Eurozone	M3 Money Supply, y-o-y	Feb	4.6%	4.6%
13:00	Eurozone	Consumer Confidence	Mar F	0.1	0.1
18:00	US	Richmond Fed Manufacturing Index	Mar	28	22
18:00	US	Conf. Board Consumer Confidence	Mar	130.8	131
19:00	US	Fed's Bostic Speaks at Economic Conference in Atlanta			
<b>Wednesday, 28 Mar</b>					
5:00	China	PBoC Deputy Governor Pan Gongsheng speaks			
16:30	US	Wholesale Inventories, m-o-m	Feb P	0.8%	0.5%
16:30	US	GDP Annualized, q-o-q	4Q T	2.5%	2.7%
16:30	US	Personal Consumption	4Q T	3.8%	3.8%
18:00	US	Pending Home Sales, m-o-m	Feb	-4.7%	2%
20:00	US	Fed's Bostic Speaks to Finance Professionals in Atlanta			
<b>Thursday, 29 Mar</b>					
3:50	Japan	Retail Trade, y-o-y	Feb	1.5%	1.7%
12:30	UK	Mortgage Approvals	Feb	67.5K	66K
12:30	UK	GDP, q-o-q	4Q F	0.4%	0.4%
12:30	UK	GDP, y-o-y	4Q F	1.4%	1.4%
16:00	Germany	CPI EU Harmonized, m-o-m	Mar P	0.5%	0.5%
16:00	Germany	CPI EU Harmonized, y-o-y	Mar P	1.2%	1.6%
16:30	US	Personal Income	Feb	0.4%	0.4%
16:30	US	Personal Spending	Feb	0.2%	0.2%
16:30	US	PCE Core, m-o-m	Feb	0.3%	0.2%
16:30	US	PCE Core, y-o-y	Feb	1.5%	1.6%
17:45	US	Chicago Purchasing Manager	Mar	61.9	62
18:00	US	Univ. of Michigan Sentiment	Mar F	102	102
21:00	US	Fed's Harker Speaks on the Economic Outlook			
<b>Friday, 30 Mar</b>					
3:30	Japan	Jobless Rate	Feb	2.4%	2.6%
3:50	Japan	Industrial Production, m-o-m	Feb P	-6.8%	5%

\* UAE time

Source: Bloomberg

Fig. 12. Last week's data

Time *	Country	Event	Period	Prior	Consensus	Actual
<b>MENA data</b>						
	UAE	M2 Money Supply, m-o-m	Feb	0.1%		0.6%
	UAE	Central Bank Foreign Assets	Feb	326B		339.8B
	UAE	CPI, y-o-y	Feb	4.8%		4.5%
	Saudi Arabia	CPI, y-o-y	Feb	3%		2.9%
	Bahrain	CPI, y-o-y	Feb	2.8%		3.1%
	Qatar	CPI, y-o-y	Feb	0.9%		0.8%
	Kuwait	M2 Money Supply, y-o-y	Jan	3.8%		3.3%
	Kuwait	CPI, y-o-y	Feb	1%		0.8%
	Egypt	Trade Balance	Jan	-3294M		-3626M
<b>Monday, 19 Mar</b>						
3:50	Japan	Trade Balance	Feb	-¥944.1B	¥89.1B	¥3.4B
<b>Tuesday, 20 Mar</b>						
10:00	Japan	Machine Tool Orders, y-o-y	Feb F	39.5%		39.5%
13:30	UK	CPI, m-o-m	Feb	-0.5%	0.5%	0.4%
13:30	UK	CPI, y-o-y	Feb	3%	2.8%	2.7%
13:30	UK	CPI Core, y-o-y	Feb	2.7%	2.5%	2.4%
13:30	UK	PPI Output NSA, m-o-m	Feb	0.1%	0.1%	0%
19:00	Eurozone	Consumer Confidence	Mar A	0.1	0	0.1
<b>Wednesday, 21 Mar</b>						
13:30	UK	Claimant Count Rate	Feb	2.3%		2.4%
13:30	UK	Jobless Claims Change	Feb	-1.6K		9.2K
13:30	UK	Average Weekly Earnings, 3M/y-o-y	Jan	2.7%	2.6%	2.8%
13:30	UK	Weekly Earnings, ex-Bonus 3M/y-o-y	Jan	2.5%	2.6%	2.6%
13:30	UK	ILO Unemployment Rate 3Mths	Jan	4.4%	4.4%	4.3%
13:30	UK	PSNB ex-Banking Groups	Feb	-10.1B	1.8B	1.3B
16:30	US	Current Account Balance	4Q	-\$101.5B	-\$125B	-\$128.2B
18:00	US	Existing Home Sales	Feb	5.4M	5.5M	5.4M
22:00	US	FOMC Rate Decision (Upper Bound)	21-Mar	1.5%	1.75%	1.75%
22:00	US	FOMC Rate Decision (Lower Bound)	21-Mar	1.25%	1.5%	1.5%
<b>Thursday, 22 Mar</b>						
4:30	Japan	Nikkei Japan PMI Manufacturing	Mar P	54.1		53.2
8:30	Japan	All Industry Activity Index, m-o-m	Jan	0.6%	-1.8%	-1.8%
13:00	Eurozone	Markit Eurozone Manufacturing PMI	Mar P	58.6	58.1	56.6
13:00	Germany	IFO Business Climate	Mar	115.4	114.6	114.7
13:30	UK	Retail Sales, ex-Auto Fuel, m-o-m	Feb	0.2%	0.4%	0.6%
13:30	UK	Retail Sales, ex-Auto Fuel, y-o-y	Feb	1.3%	1.2%	1.1%
16:00	UK	Bank of England Bank Rate	22-Mar	0.5%	0.5%	0.5%
16:00	UK	BOE Asset Purchase Target	Mar	435B	435B	435B
16:00	UK	BOE Corporate Bond Target	Mar	10B	10B	10B
17:45	US	Markit US Manufacturing PMI	Mar P	55.3	55.6	55.7
18:00	US	Leading Index	Feb	0.8%	0.5%	0.6%
<b>Friday, 23 Mar</b>						
3:30	Japan	National CPI, y-o-y	Feb	1.4%	1.5%	1.5%
3:30	Japan	National CPI, ex-Fresh Food, y-o-y	Feb	0.9%	1%	1%
16:30	US	Durable Goods Orders	Feb P	-3.5%	1.6%	3.1%
16:30	US	Durables, ex-Transportation	Feb P	-0.2%	0.5%	1.2%
16:30	US	Capital Goods Ship Non-defence, ex-Air	Feb P	0.1%	0.5%	1.4%
18:00	US	New Home Sales	Feb	622K	620K	618K

\* UAE time

Source: Bloomberg

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