The Week Ahead: Fed to remain on hold, important data week for US and Eurozone

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US: Labour data, PCE inflation and FOMC meeting

The Fed is expected to keep the FFTR on hold with the upper bound rate set to remain at 1.75% in its 1-2 May meeting. The main communication will come from the statement, as there will be no post-meeting press conference. We do not expect any meaningful changes in language, though do foresee some reference to the recent uptick in core CPI inflation (core PCE remains below the Fed's 2% target). The FOMC is likely to continue to highlight the tight labour market conditions and healthy economic growth outlook. We expect the FOMC to reiterate interest rate hikes will be gradual. The focus will be on any indications for the June meeting where markets see a 93% chance of a 25 bps rate hike. The upcoming week will also be important on the data front, with releases including PCE inflation (March), non-farm payrolls and ISM surveys (both April). Consensus estimates some rebound in the labour data, with jobs growth strengthening to 195K in April following the soft 103K in March. Unemployment is forecast to have fallen to 4% (March: 4.1%), though average weekly earnings growth is expected to have decelerated to 0.2% m-o-m in March (February: 0.3%) keeping the y-o-y rate steady at 2.7%. Meanwhile, consensus estimates real personal spending growth picked up to 0.5% m-o-m in March, which was already reflected in the solid retail sales for the month.

Europe: Eurozone 1Q GDP estimate and April inflation

The EUR and GBP weakened against the USD at the end of last week, following the bearish tone of the ECB meeting and lacklustre 1Q GDP growth in the UK (pages 3& 4). The ECB highlighted the softening in economic momentum. Thus, focus will be particularly on the Eurozone's 1Q GDP estimate (first print) and April inflation data. Consensus expects a deceleration in GDP growth to 0.4% q-o-q in 1Q2018, from 0.6% in 4Q2017, with the strong EUR weighing on exports. The recent high-frequency data, including industrial production growth and retail sales, suggests that activity softened further into 2M2018. Meanwhile, core inflation is also forecast to moderate to 0.9% y-o-y in April (March: 1%), with softer imported inflation and some payback from the early Easter effect. Headline inflation is seen steady at 1.3% y-o-y in April, supported by higher energy prices. The unemployment rate for March is estimated to have held at 8.5% in March, after decelerating from 8.6% in January.

Turkey CBRT inflation projections and April inflation in focus

The CBRT will release its latest inflation projections this week and we expect the bank to raise its forecasts for 2018 and 2019 on the back of recent TRY weakness. We saw this as a central factor in the CBRT raising the late liquidity window rate by 75 bps to 13.5% last week (page 5), with high crude prices and persistent food inflation also contributing. The CBRT currently sees end-2018 and end-2019 inflation at 7.9% and 6.5%, whereas inflation expectation surveys are forecasting above 10% headline inflation for 2018. Consensus envisages that headline inflation accelerated to 10.5% in April, from 10.2% in March, driven by TRY weakness adding further upward pressure to fuel prices.

I. Recent Events and Data Releases

A. MENA Economies

Saudi Arabia: SAMA looking to reduce excess banking sector liquidity

SAMA looking to reduce some deposits from banking sector

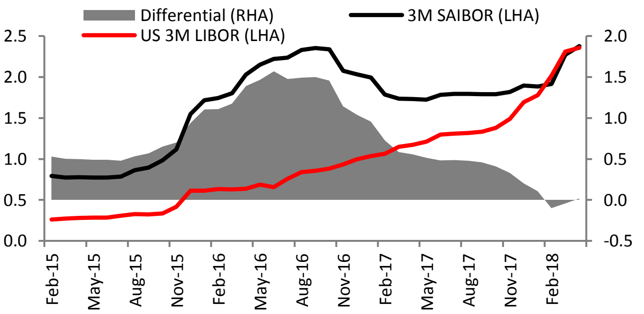
SAMA Governor Ahmed Abdulkarim Alkholifey indicated last week that the central bank is planning to remove excess liquidity from the banking system to mitigate pressure on Saudi Arabia's currency peg as US interest rates rise. SAMA is planning to withdraw a number of deposits that were placed with commercial banks in 2016 when liquidity conditions were tightening. We see Alkholifey's comment being related to the spread between domestic and US interbank rates, with Saibor having traded at a discount to US Libor since end-February. As we have previously highlighted in our research, SAMA has been proactive in reducing the negative spread between Saibor and Libor, having raised benchmark interest rates and suspended the repo facility in March. Reducing the central bank's deposits in the banking system should also help to raise interbank rates. The government can also help to absorb excess liquidity if required, either through reducing deposits or increasing borrowing from the banking sector. The latter would also provide some boost to credit growth, especially as private sector loan demand remains weak. The Ministry of Finance raised SAR5 billion (USD1.3 billion) in domestic sukuk at its sixth monthly offer.

Saibor-Libor differential removed at end-April, Saibor again at premium

Notably, Saibor rates had converged and risen slightly above Libor at end-April (Fig. 1). This was likely supported by the measures mentioned above alongside the earlier comments by the central bank governor. In addition, the pace of increase of US Libor has slowed, showing some signs of flattening since mid-April. We believe that Saudi policy makers will watch developments closely to ensure that a discount does not re-emerge. However, we do not think SAMA wishes to see Saibor much higher than Libor while economic activity in KSA remains weak.

Fig. 1. Saudi Arabia: Saibor moves slightly above US Libor at end-April

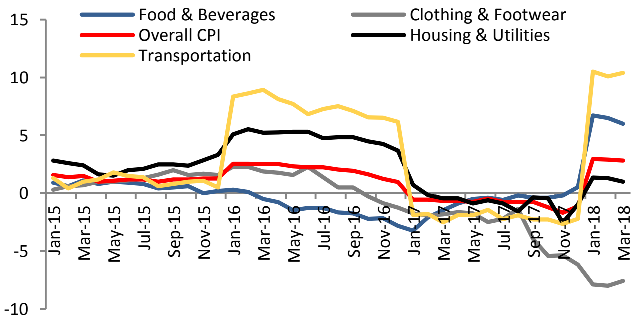
% (LHA); pp differential (RHA)



Source: Bloomberg, ADCB calculations

Fig. 2. Saudi Arabia: Headline inflation softens moderately in March due to weaker food inflation

% change y-o-y



Source: General Authority for Statistics, ADCB calculations

Saudi Arabia: Inflation still elevated in March

Softer food price inflation largely behind headline deceleration

Annual inflation remained elevated in March, printing at 2.8% y-o-y, albeit decelerating moderately from 2.9% in February and 3% in January. This deceleration was largely due to weaker food inflation, which softened to 6% in March from 6.5% in February. Nevertheless, the inflation data continues to reflect the introduction of VAT and the increase in fuel and electricity prices at the beginning of the year, which is resulting in substantially higher inflation than in 2017. We continue to highlight that Saudi Arabia has changed the weighting of its inflation basket since January and we believe that the impact of fiscal reform measures will likely be greater than that suggested by the headline print. We expect private consumption to remain weak, though the impact of the government's fiscal reforms to be partly negated by its handout packages to Saudi families. There are no signs of secondary inflation from the fiscal reforms due to the weak domestic demand environment. The soft consumer demand is partly reflected in the yearly contraction in clothing prices, which widened following the introduction of VAT.

B. G4 Economies

Eurozone: Dovish tone to April meeting; QE extension likely in July

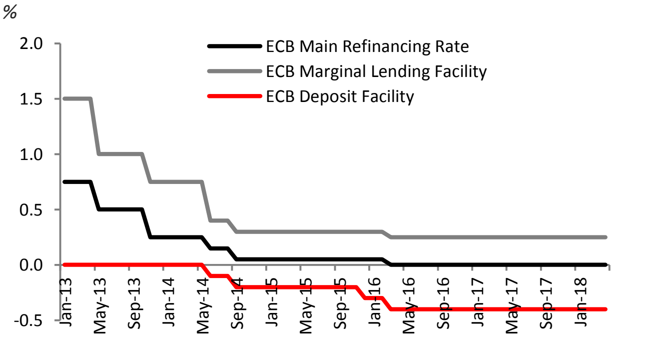
No changes to monetary policy but acknowledged the softening economic momentum in 1Q2018

The EUR weakened against the USD after the tone of last week's ECB meeting was more dovish than market expectations. The central bank made no changes to the pace of its monthly asset purchases, and continued to insist on "patience and persistence" regarding monetary policy. The ECB noted that core inflation remains subdued and yet to show convincing signs of a sustained upward trend. We believe that inflation will pick up only gradually given the existing slack in the Eurozone economy. ECB President Mario Draghi highlighted at the post-meeting press conference that there was no discussion about future monetary policy, suggesting that further adjustments to the QE programme could be delayed until the July meeting. Draghi also acknowledged that there was some moderation in economic activity in early 2018 but expressed confidence on the Eurozone's economic growth outlook and its capacity to bring inflation back to target.

We expect ECB to extend asset purchases programme at its July meeting

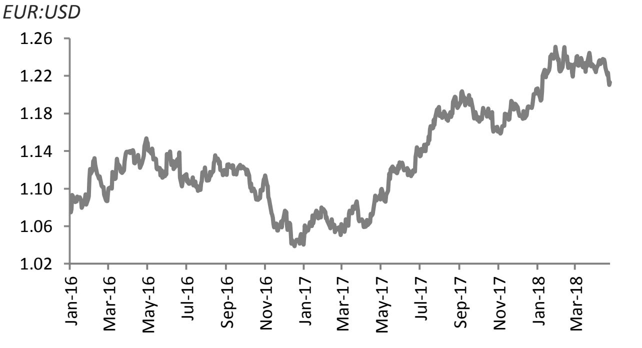
The Governing Council (GC) will have new economic projections at its June meeting, which will likely reflect the recent softening in economic momentum. Any downward revisions to growth and inflation projections could lead the ECB to tread cautiously over the timing and pace of tapering of the QE programme. We expect the GC to announce an extension of the asset purchase programme at its July policy meeting for another three months to December, albeit at a slower pace of EUR15 billion per month (currently EUR30 billion). We also see the QE programme coming to an end by December 2018, with the first interest rate hike only in 2Q2019.

Fig. 3. Eurozone: ECB keeps monetary policy steady at April meeting



Source: ECB

Fig. 4. Eurozone: EUR weakens against USD after ECB's dovish tone last week



Source: Bloomberg

US: 1Q GDP growth beats expectations, solid investment activity

Domestic demand remains healthy, despite seasonal slowdown in 1Q2018

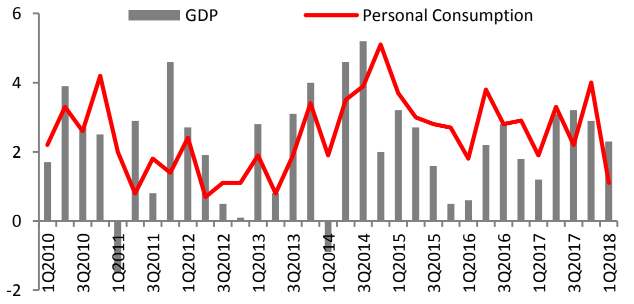
US economic activity was solid in 1Q2018, albeit still seeing the seasonal slowdown in consumer spending which is usual in the first quarter. Real GDP growth printed at 2.3% q-o-q SAAR, higher than the consensus estimate of 2% though softening from the 2.9% in 4Q2017. Moreover, the growth drivers were broad-based, with all the major sub-components seeing positive expansion despite some segments decelerating. Non-residential investment grew by a healthy 6.1% (4Q2017: 6.8%) and investment in structures rose by a robust 12.3%, though investment in equipment decelerated. Inventories also contributed (0.4 pps) to the headline growth, though are unlikely to see the same support in 2Q2018 especially if the economy gains momentum (our core scenario). The upside surprise to GDP growth was largely due to net exports, which contributed positively (0.2pp) to the headline growth. Consensus was expecting a negative contribution from the net exports segment.

Underlying drivers of personal spending solid

However, personal consumption growth softened to 1.1% in 1Q2018 (in line with consensus) after recording solid 4% growth in 4Q2017. The moderation in personal spending came as consumers tried to boost their savings in 1Q2018, after strong holiday seasonal expenditure in 4Q. The slowdown in purchases of motor vehicles in 1Q was also a factor, after robust hurricane-related replacement sales in 4Q. We see solid personal spending activity for the remainder of 2018, supported by a healthy labour market.

Fig. 5. US: Real GDP grows by healthy 2.3% q-o-q SAAR in 1Q2018, despite slower consumer spending

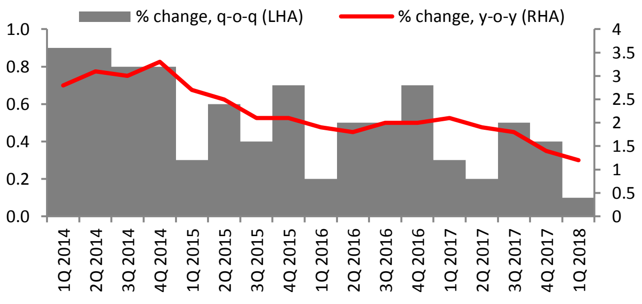
% change y-o-y



Source: US Bureau of Economic Analysis

Fig. 6. UK: 1Q GDP growth moderates sharply to 0.1% q-o-q, from 0.4% in 4Q2018

% change



Source: UK Office of National Statistics

UK: 1Q GDP growth falls to 0.1% q-o-q – slowest in five years

Broad-based slowdown in economic activity in 1Q2018

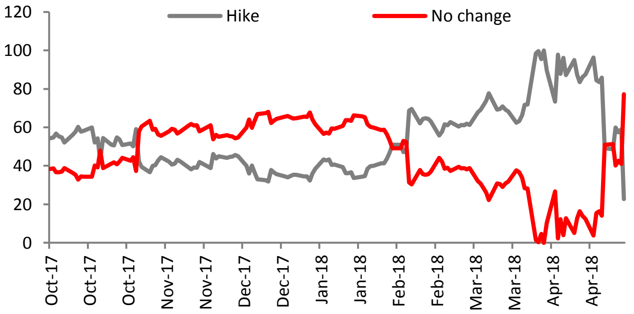
UK GDP growth decelerated sharply in 1Q2018, raising doubts about the underlying health of the economy. Real GDP growth came in at 0.1% q-o-q, markedly lower than the consensus estimate of 0.3% and the 0.4% growth in 4Q2018. This is the slowest pace of expansion since 4Q2012 and below the BoE's expectation of 0.3% (including the impact of snow-related slowdown). The moderation in activity was broad-based, with contraction in the construction sector, a slowdown in manufacturing growth and a squeeze on consumer spending. The Office for National Statistics (ONS) highlighted that snow-related disruption was most evident in the construction and retail sectors but argued that their impact on growth was relatively limited. The ONS also underlined that the slowdown in activity could have been due to the loss of underlying growth momentum. Looking at the components, the construction sector contracted by 3.3% (4Q:-0.1%), subtracting 0.2 pp from GDP growth. Services growth also softened to 0.3% (4Q: 0.4%), reflecting weak domestic demand. Manufacturing output growth also slowed though total production rose on the back of a rebound in energy supply (mining and quarrying) following the Forties oil pipeline shutdown in 4Q2017.

May rate hike expectations fell to 23% following weak 1Q GDP growth

Following the weak GDP data release, market expectations of a May rate hike fell to 23% as compared to above 90% in early-April. The recent comments from Mark Carney also suggested that a 25bps rate hike in May is not a done deal. Thus, we now see an increased chance of a rate hike being postponed to August or November, which also provides more time for the MPC to assess the extent of the slowdown in economic activity. Moreover, the broad-based moderation in activity will also make it increasingly hard for the BoE to justify its hawkish stance.

Fig. 7. UK: Market expectations of May rate hike fall below 23% at end of last week

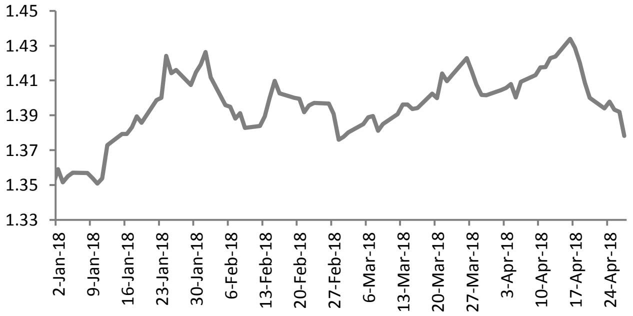
Probability of 25 bps rate hike



Source: Bloomberg

Fig. 8. UK: GBP weakens further against USD last week following release of soft 1Q GDP growth data

GBP:USD



Source: Bloomberg

C. Emerging Market Economies

Turkey: CBRT delivers "measured" hike at April meeting

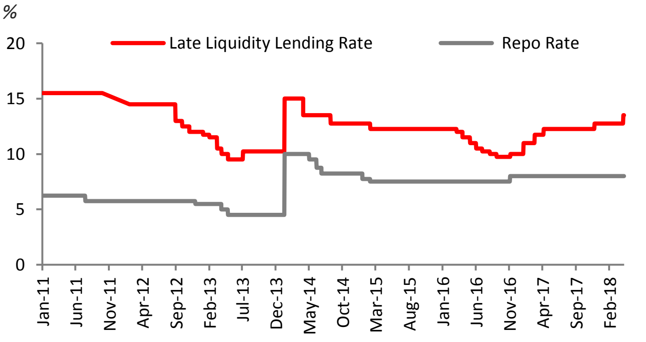
Late liquidity window lending rate raised by 75 bps to 13.5% from 12.75%

The CBRT raised its late liquidity window (LLW) lending rate by 75 bps to 13.5% from 12.75% at its April meeting. This was greater than the consensus estimate of a 50 bps hike but lower than our expectation of a 100 bps hike. However, the other benchmark rates, including one-week repo, overnight borrowing and overnight lending, remained unchanged at 8%, 7.25% and 9.25% respectively. The tone of the meeting was hawkish with the committee deciding to implement “measured monetary tightening” to support price stability. We believe that the hawkish decision was aimed at supporting the TRY. Moreover, the central bank’s forward guidance was unchanged with the post-meeting statement underlining that its “tight stance in monetary policy will be maintained decisively until [the] inflation outlook displays a significant improvement”.

CBRT highlights upside risks to inflation outlook from imported inflation

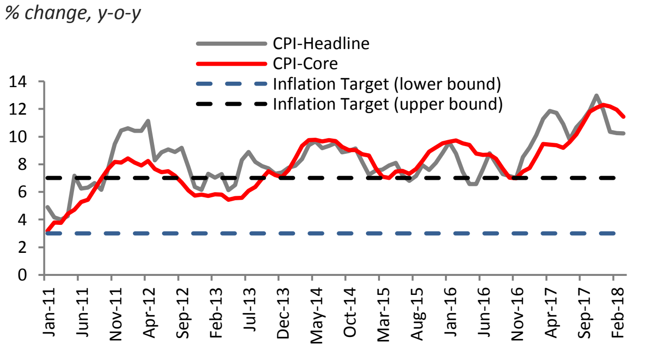
The CBRT also expressed increasing concern over the elevated levels of inflation with inflation expectations posing upside risks to pricing behaviour. The MPC included a new phrase in its post-meeting statement, explaining that “upside movements in import prices have increased such risks”. We believe that this was particularly referring to upside risks from the weak TRY and high crude oil prices. However, the CBRT continued to sound positive on the growth outlook given the solid domestic and foreign demand. We continue to see the CBRT maintaining its hawkish stance with the risks being tilted towards further tightening in monetary policy via liquidity measures. TRY developments remain critical to the CBRT’s actions, in our view.

Fig. 9. Turkey: CBRT raises its late liquidity lending rate by 75 bps to 13.5% in April



Source: CBRT

Fig. 10. Turkey: Headline inflation persists in double digits in 3M2018



Source: CBRT; Turkey's Central Statistics Office

II. Economic Calendar

Fig. 11. The week ahead

Time*	Country	Event	Period	Prior	Consensus
GCC Countries					
	UAE	UAE PMI	Apr	54.8	
	UAE	Dubai Airport Cargo Volume, y-o-y	Mar	-0.6%	
	Saudi Arabia	Saudi Arabia PMI	Apr	52.8	
	Saudi Arabia	Non-Oil Exports, y-o-y	Feb	18%	
	Saudi Arabia	M2 Money Supply, y-o-y	Mar	0.3%	
	Saudi Arabia	SAMA Net Foreign Assets SAR	Mar	1798.3B	
	Egypt	Egypt PMI	Apr	49.2	
	Egypt	Gross Official Reserves	Apr	42.6B	
	Qatar	M2 Money Supply, y-o-y	Mar	15.7%	
Monday, 30 Apr					
5:00	China	Manufacturing PMI	Apr	51.5	51.3
12:00	Eurozone	M3 Money Supply, y-o-y	Mar	4.2%	4.1%
16:00	Germany	CPI EU Harmonized, y-o-y	Apr P	1.5%	1.5%
16:30	US	Personal Income	Mar	0.4%	0.4%
16:30	US	Real Personal Spending	Mar	0%	0.5%
16:30	US	PCE Core, m-o-m	Mar	0.2%	0.2%
16:30	US	PCE Core, y-o-y	Mar	1.6%	1.9%
18:00	US	Pending Home Sales, m-o-m	Mar	3.1%	0.5%
Tuesday, 1 May					
12:30	UK	Mortgage Approvals	Mar	63.9K	63K
12:30	UK	Markit UK PMI Manufacturing SA	Apr	55.1	54.8
17:45	US	Markit US Manufacturing PMI	Apr F	56.5	56.5
18:00	US	ISM Manufacturing	Apr	59.3	58.5
Wednesday, 2 May					
5:45	China	Caixin China PMI Manufacturing	Apr	51	50.9
12:30	UK	Markit/CIPS UK Construction PMI	Apr	47	50.5
13:00	Eurozone	Unemployment Rate	Mar	8.5%	8.5%
13:00	Eurozone	GDP SA, q-o-q	1Q A	0.6%	0.4%
13:00	Eurozone	GDP SA, y-o-y	1Q A	2.7%	2.5%
16:15	US	ADP Employment Change	Apr	241K	198K
22:00	US	FOMC Rate Decision (Upper Bound)	2-May	1.75%	1.75%
22:00	US	FOMC Rate Decision (Lower Bound)	2-May	1.5%	1.5%
Thursday, 3 May					
13:00	Eurozone	CPI Core, y-o-y	Apr A	1%	0.9%
13:00	Eurozone	CPI Estimate, y-o-y	Apr	1.4%	1.3%
13:00	Eurozone	European Commission Updates Its Economic Forecasts			
16:00	Eurozone	ECB's Constancio Speaks in Frankfurt			
16:30	Eurozone	ECB's Coeure Speaks in Frankfurt			
16:30	US	Trade Balance	Mar	-$57.6B	-$50B
18:00	US	ISM Non-Manufacturing Composite	Apr	58.8	58.1
18:00	US	Factory Orders	Mar	1.2%	1.4%
Friday, 4 May					
13:00	Eurozone	Retail Sales, m-o-m	Mar	0.1%	0.5%
16:30	US	Change in Nonfarm Payrolls	Apr	103K	195K
16:30	US	Change in Manufacturing Payrolls	Apr	22K	20K
16:30	US	Unemployment Rate	Apr	4.1%	4%
16:30	US	Average Hourly Earnings, m-o-m	Apr	0.3%	0.2%
16:30	US	Average Hourly Earnings, y-o-y	Apr	2.7%	2.7%
16:30	US	Average Weekly Hours All Employees	Apr	34.5	34.5
20:00	US	Fed's Dudley Speaks with Bloomberg's Matthew Winkler			

* UAE time

Source: Bloomberg

Fig. 12. Last week's data

Time *	Country	Event	Period	Prior	Consensus	Actual
GCC Economies						
	UAE	M2 Money Supply, m-o-m	Mar	0.6%		0.7%
	UAE	CPI, y-o-y	Mar	4.5%		3.4%
	Saudi Arabia	CPI, y-o-y	Mar	2.9%		2.8%
Monday, 23 Apr						
4:30	Japan	Nikkei Japan PMI Manufacturing	Apr P	53.1		53.3
11:30	Germany	Germany Manufacturing PMI	Apr P	58.2	57.5	58.1
12:00	Eurozone	Markit Eurozone Manufacturing PMI	Apr P	56.6	56.1	56
16:30	US	Chicago Fed Nat Activity Index	Mar	1	0.3	0.1
17:45	US	Markit US Manufacturing PMI	Apr P	55.6	55.2	56.5
18:00	US	Existing Home Sales	Mar	5.54M	5.55M	56M
Tuesday, 24 Apr						
10:00	Japan	Machine Tool Orders, y-o-y	Mar F	28.1%		28.1%
12:00	Germany	IFO Business Climate	Apr	103.3	102.8	102.1
12:30	UK	PSNB, ex-Banking Groups	Mar	1.2B	3B	1.3B
17:00	US	FHFA House Price Index, m-o-m	Feb	0.9%	0.6%	0.6%
18:00	US	New Home Sales	Mar	667K	630K	694K
18:00	US	Richmond Fed Manufacturing Index	Apr	15	16	-3
18:00	US	Conference Board Consumer Confidence	Apr	127	126	128.7
Wednesday, 25 Apr						
8:30	Japan	All Industry Activity Index, m-o-m	Feb	-1.1%	0.5%	0.4%
Thursday, 26 Apr						
10:00	Germany	GfK Consumer Confidence	May	10.9	10.8	10.8
15:45	Eurozone	ECB Main Refinancing Rate	26-Apr	0%	0%	0%
15:45	Eurozone	ECB Marginal Lending Facility	26-Apr	0.25%	0.25%	0.25%
15:45	Eurozone	ECB Deposit Facility Rate	26-Apr	-0.4%	-0.4%	-0.4%
16:30	US	Advance Goods Trade Balance	Mar	-$75.9B	-$75B	-$68B
16:30	US	Wholesale Inventories, m-o-m	Mar P	1%	0.7%	0.5%
16:30	US	Durable Goods Orders	Mar P	4%	1.6%	2.6%
16:30	US	Durables, ex-Transportation	Mar P	0.9%	0.5%	0.0%
16:30	US	Cap Goods Shipments, Nondef, ex-Air	Mar P	1%	0.3%	-0.7%
19:00	US	Kansas City Fed Manufacturing Activity	Apr	17	17	26
Friday, 27 Apr						
3:30	Japan	Jobless Rate	Mar	2.5%	2.5%	2.5%
3:30	Japan	Tokyo CPI, y-o-y	Apr	1%	0.8%	0.5%
3:50	Japan	Retail Trade, y-o-y	Mar	1.7%	1.5%	1%
3:50	Japan	Retail Sales, m-o-m	Mar P	0.4%	0%	-0.7%
3:50	Japan	Industrial Production, m-o-m	Mar P	2%	0.5%	1.2%
3:50	Japan	Industrial Production, y-o-y	Mar P	1.6%	2%	2.2%
12:30	UK	GDP, q-o-q	1Q A	0.4%	0.3%	0.1%
12:30	UK	GDP, y-o-y	1Q A	1.4%	1.4%	1.2%
16:30	US	GDP Annualized, q-o-q	1Q A	2.9%	2%	2.3%
16:30	US	Personal Consumption	1Q A	4%	1.1%	1.1%
16:30	US	Core PCE, q-o-q	1Q A	1.9%	2.5%	2.5%
18:00	US	University of Michigan Sentiment	Apr F	97.8	98	98.8
	Japan	BOJ 10-Yr Yield Target	27-Apr	0%	0%	0%
	Japan	BOJ Policy Balance Rate	27-Apr	-0.1%	-0.1%	-0.1%

* UAE time
Source: Bloomberg

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