

The Week Ahead: Fed meeting and India budget in focus

► US: Fed meeting and State of the Union address

We expect the Fed to remain on hold at its 30-31 January meeting after raising the FFTR by 25 bps in December. The focus will be on the tone of the post-meeting statement (a press conference is not scheduled), particularly in gauging the likelihood of a March rate hike. We believe that the Fed's language will continue to outline the solid economic momentum and tight labour market conditions. However, attention will be on the inflation outlook, as any hawkish tilt in inflation expectations would further boost market expectations of a March rate hike. We continue to forecast two 25 bps FFTR hikes in 2018, albeit with the risk leaning towards an additional rate hike. Meanwhile, the key data releases this week will be December PCE inflation (29 January), ISM manufacturing (1 February) and NFP data for January (due 2 February). Consensus expects a healthy labour report with 180K jobs created (December: 146K), with the unemployment rate and wage growth unchanged at 4.1% and 0.3% m-o-m respectively. Core PCE inflation is seen rising to 0.2% m-o-m in December (November: 0.1%), driven by shelter and medical services prices, albeit with the yearly rate remaining steady at 1.5% y-o-y. Focus will also be on President Donald Trump's State of the Union address (30 January), especially any comments related to infrastructure spending and protectionism.

► India: Expansionary budget expected

India's union budget for FY2019 (April-March) will be presented on 1 February with a likely focus on rural and infrastructure spending. We expect an expansionary budget with a fiscal deficit target of 3.2% of GDP for FY2019 compared to the 3% target set previously. The government is likely to shift its attention towards rural voters ahead of the next general election (May 2019), with spending to increase on irrigation projects, affordable housing and rural development. Corporate taxes could be reduced moderately from the existing 30%, particularly to promote investment activity, which has been impacted by a number of factors including implementation of GST. However, the rising oil prices could reduce the pace of fiscal loosening, with the government likely to be unable to raise administered prices fully. On balance, we expect the government to look to reiterate its medium-term fiscal consolidation stance, albeit at a slower pace than envisaged previously.

► Eurozone: 4Q GDP and January inflation

Consensus expects the Eurozone economy to have grown at a solid pace of 0.6% q-o-q in 4Q as in 3Q. High frequency data (retail sales and industrial production) continue to suggest that economic momentum remains robust with a pick-up spreading to peripheral economies. We expect private consumption to remain the main driver of economic growth with additional support from external demand. The first estimate will be based on the data from six countries (including Spain and France) with additional non-disclosed inputs from five other countries. Meanwhile, January core inflation is likely to accelerate to 1% y-o-y from 0.9% in December, as higher recent oil prices feed into airfares.

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

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I. Recent Events and Data Releases

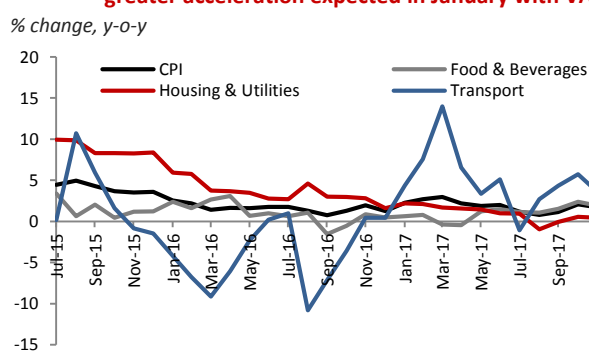
A. MENA Economies

UAE: Inflation accelerates to 2.7% in December

The pace of the UAE's inflation growth picked up in 4Q2017, particularly in December. The headline inflation rate strengthened to 2.7% y-o-y in December from 1.7% in the previous month. This rise in inflation was largely driven by higher food and transportation prices. We believe that the pick-up in food prices likely reflected the weakening in the USD, which pushed up imported inflation. Moreover, some frontloading of expenditure in non-perishable items in December ahead of the introduction of VAT is also likely to have occurred. Food prices rose by 3.2% y-o-y in December from 1.7% in November. The rise in transportation inflation was more marked at 9.3% y-o-y in December (November: 3.7%) on the back of rising fuel prices. We expect inflation in the UAE to accelerate further in January with the introduction of VAT and the further rise in fuel prices. We estimate that inflation will jump to around 3.6% in January.

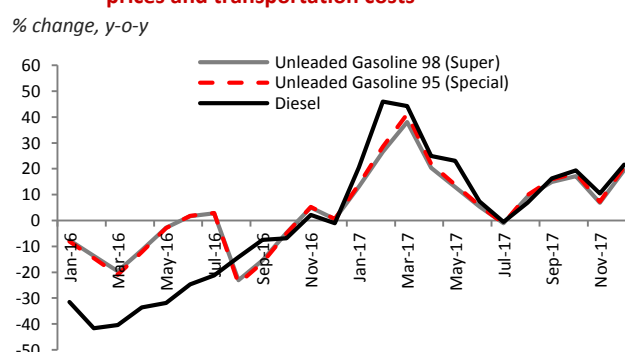
Food and transportation components drive inflation up in December

Fig. 1. UAE: Headline inflation strengthened in December; greater acceleration expected in January with VAT



Source: National Bureau of Statistics

Fig. 2. UAE: Rise in global oil prices feeds into domestic fuel prices and transportation costs



Source: Ministry of Energy

Saudi Arabia: IMF lifts growth forecast; focus on reforms going forward

The IMF raised its GDP growth forecast for Saudi Arabia last week in its World Economic Outlook Update. It noted that "While stronger oil prices are helping a recovery in domestic demand in oil exporters, including Saudi Arabia, the fiscal adjustment that is still needed is projected to weigh on growth prospects". The IMF now estimates real GDP growth of 1.6% for 2018, up from 0.5% in its October 2017 forecast. The growth estimate for 2019 was also increased to 2.2%, up from 0.6%. The IMF's forecasts are above our expectations, though we also see a pick-up in economic activity with the higher forecast government revenue translating into higher government spending. We see headline real GDP growth at 0.7% in 2018 after contracting by 0.7% the previous year. We see some upside risk from higher oil production to our forecast for 2018 growth compared to 2017, albeit production should still comply with the OPEC target.

We remain more conservative with our growth forecast than the IMF

Meanwhile, Prince Alwaleed bin Talal and several prominent businessmen were released over the weekend from detention linked to the anti-corruption drive, which started in early November. The media has highlighted that these latest developments indicate that the graft probe is winding down. The speed and breadth of the anti-corruption drive were

Attracting FDI is vital for Saudi Arabia's transformation objectives

widely seen as affecting private investment sentiment, including related to FDI. We believe that the government will be looking to focus on the economic reform story, improving the investment environment, and making progress with the investment programme, which will be crucial for attracting FDI. The policy emphasis will be on reviving economic activity and starting to work towards key objectives of the National Transformation Plan, including investment to diversify the economy. These aims underpin the 2018 government budget, which reflects a shift to an expansionary fiscal stance.

B. G4 Economies

Eurozone: ECB expresses concerns over rapid EUR appreciation

The ECB kept monetary policy steady at its 25 January meeting, including interest rates and the asset purchase programme for 2018, in line with our and the market's expectations. The market viewed the overall tone as moderately bearish with a gradual approach to policy adjustment highlighted, though they were expecting more on limiting the EUR. Forward guidance was left unchanged, while keeping open the option of future tweaks in language. ECB President Mario Draghi reiterated that he sees little chance of an interest rate hike this year, suggesting that the sequencing of monetary policy will remain in place. Moreover, the focus of the meeting was largely on the EUR appreciation, with Draghi citing past international commitments to avoid competitive devaluations. EUR volatility has returned to the introductory statement, with the ECB seeming particularly concerned over the medium-term impact of the strong EUR on the inflation outlook. During the post-meeting press conference, Draghi also noted that several members of the governing council (GC) expressed their concern, and claimed that it was not just about the exchange rate, but about the overall status of international relations right now.

Forward guidance unchanged, with option for tweaks left open

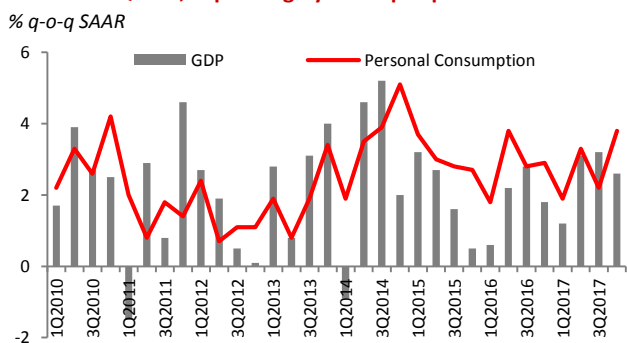
The ECB strengthened its language on growth, highlighting that the economy expanded more than expected in 2H2017. Meanwhile, the inflation outlook was left unchanged but the bank reiterated its conviction that inflation will converge towards 2%. We believe that EUR appreciation is likely to keep the underlying inflationary pressure subdued despite oil prices supporting headline inflation in the near future. The ECB will remain cautious in its communication strategy with very subtle and gradual changes to its forward guidance, particularly to avoid further rapid appreciation in the EUR. We expect the bank to maintain its 'lower for longer' quantitative easing programme, with an increasing likelihood of a further QE extension beyond September 2018 and interest rate hikes only in 1H2019.

We expect very gradual changes in forward guidance, mainly to avoid any further EUR appreciation

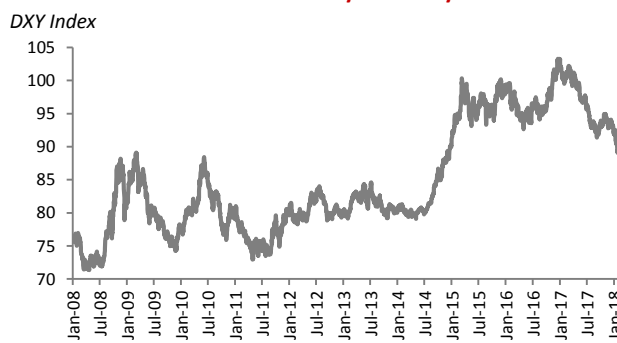
US: Rising concerns over protectionism and trade disputes

A short-term government funding deal was agreed last week, ending on 8 February. However, negotiations on funding for a border wall (a Republican demand) and a DACA (immigration legislation) protection deal were inconclusive. Thus, there remains a risk of another government shutdown. The DACA protections expire in early March and remain important for Democrats ahead of the mid-term elections in November. Separately, the government will also have to raise the debt ceiling limit by late-February. Treasury Secretary Steven Mnuchin has already requested that the Republicans raise the limit by 28 February, though the cut-off date could be a little later than that. Overall, we expect political developments to remain in focus over the next two months.

Government funding and debt ceiling extension will return to table in a few weeks

Fig. 3. US: Underlying real GDP growth remains healthy in 4Q2017, expanding by 2.6% q-o-q SAAR

Source: Bureau of Economic Analysis

Fig. 4. US: DXY index weakens following weak dollar policy comments from Treasury Secretary Steven Mnuchin

Source: Bloomberg

Furthermore, concerns over protectionism have increased after the US imposed import tariffs on solar panels and washing machines. This has opened up fresh tensions between the US and China and South Korea in particular. The impact of these tariffs is expected to be very minor but it opens up the possibility of new tariffs being imposed on steel and aluminium imports by the US. We believe that any such tariffs are likely to have a considerable impact on the global economy, if introduced. Notably, the commerce department has submitted its Section 232 reports on steel (11 January) and aluminium (22 January) to President Donald Trump, who will now have 90 days to take action on them. Meanwhile, Treasury Secretary Mnuchin, while speaking in Davos, noted that the weaker USD is good for the US as it stimulates trade and opportunities. This is the first time since 1995 that a treasury secretary has openly argued for a weaker dollar. Meanwhile, Brent crude touched USD71 p/b last week, in part driven by weak dollar sentiment and the fall in US inventories for a 10th consecutive month. Overall, any escalation in trade tensions, the NAFTA negotiations or open currency wars could adversely impact current business sentiment.

Brent touches USD71 p/b driven by weak dollar sentiment and fall in inventories

US: 4Q GDP growth supported by key economic drivers

Real GDP growth came in at 2.6% q-o-q SAAR in 4Q2017, lower than the consensus estimate of 3% and 3Q GDP growth of 3.2%. This was largely due to a drag from net exports and inventories. However, personal consumption remained solid and accelerated to 3.8% q-o-q in 4Q (3Q: 2.2%), beating the consensus estimate of 3.7%. Non-residential business fixed investment was also robust, driven by equipment investment in the petroleum sector, particularly to expand production capabilities. Residential investments and government spending also remained supportive. However, net exports subtracted 1.1pp growth from headline GDP growth in 4Q, driven by higher imports. This import growth was likely supported by the expectations that government policy could shift to new tariffs being introduced, after tax reform legislation was passed. The weak USD and strong domestic demand backdrop would also have supported imports in 4Q. The drawdown in inventories also lowered headline GDP growth by 0.7pp, though this should be attributed to the positive impact of strong economic activity. Overall, the economic momentum remained robust and we expect it to feed into 2018.

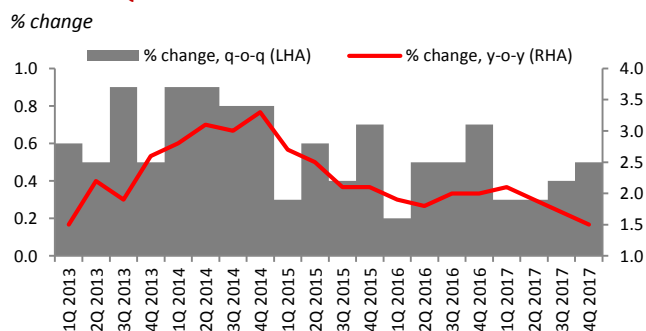
Domestic demand remains strong, with household spending strengthening more than market expectations

UK: Employment bounces back in November; 4Q GDP growth solid

Labour market conditions in the UK tightened in November with solid employment activity and wage growth showing some first signs of a pick-up. Employment growth rebounded to 102K on a 3m/3m basis (consensus: -12K; October: -56K), suggesting robust hiring. The November employment print should be read with caution as it remains to be seen whether this trend will continue in the coming months. Weekly earnings (ex-bonuses) growth also picked up for a second month, rising to 2.4% in November (October: 2.3%) after remaining largely subdued in 10M2017. However, the unemployment rate remained steady at 4.3%, suggesting that employment gains came through a higher participation rate. Despite the strong report, we are still not confident that this trend will persist and feed positively into domestic inflationary pressure. We continue to believe that there is no urgency for the BoE to raise interest rates in 2018. Meanwhile, the UK economy also ended 2017 on a positive note as growth surprisingly accelerated to 0.5% q-o-q in 4Q, from 0.4% q-o-q in 3Q. This was mainly driven by the services sector, which grew by 0.6% q-o-q in 4Q. Manufacturing activity also remained solid with support from rising global demand. However, the construction sector contracted for the third consecutive quarter, weighed down by Brexit-related uncertainty.

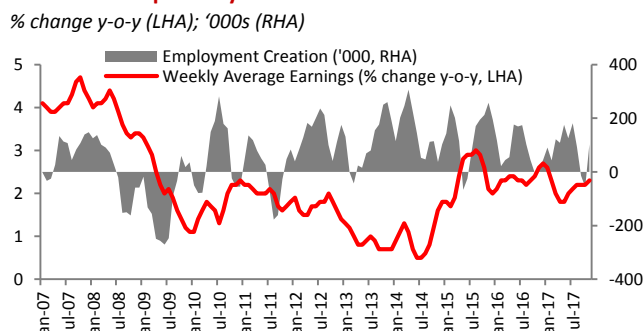
Solid hiring activity in November, adding 102K jobs on a 3m/3m basis

Fig. 5. UK: Quarterly real GDP growth picks up moderately in 4Q



Source: UK Office for National Statistics

Fig. 6. UK: Labour market conditions strengthened unexpectedly in November



Source: UK Office for National Statistics

Japan: Kuroda allays market fears of exit talks

The BoJ kept its monetary policy steady at its January meeting, in line with our and the market's expectations. This includes the short-term policy rate of -0.1%, the 10-year government bond yield target of 0% and the targeted pace of asset purchases of long-term JGBs and ETFs. The tone of the meeting was dovish with Governor Haruhiko Kuroda reiterating the central bank's commitment to maintaining accommodative monetary policy. He also argued that exit talks are not appropriate at this point as inflation is still well below the 2% target. Regarding the tapering concerns, Kuroda highlighted that any changes to open market operations do not indicate a shift in the bank's policy stance. Overall, the communication clearly suggests that the BoJ is unlikely to withdraw from its loose monetary policy stance anytime soon.

Accommodative monetary policy to continue in 2018

The BoJ also published its outlook report with no revisions made to its median inflation or growth projections. Moreover, the timing to achieve the inflation target was retained at around FY2019. Nevertheless, the bank upgraded its language on inflation expectations, stating that 'medium to long-term inflation expectations have been more or less unchanged recently, after having remained in a weakening phase since summer

Re-appointment of deputy governors likely by end-February or early March

2015'. Nevertheless, we expect underlying price pressures to remain subdued in the near future as there were no signs of a pick-up in labour costs. Looking ahead, the market's attention will now shift to the composition of the BoJ policy board with the terms of two deputy governors, Kikuo Iwata and Hiroshi Nakaso, ending on 19 March. Governor Kuroda's term also ends on 8 April. Government communications still suggest that Kuroda is most likely to be reappointed for another term at this point. We expect the government to make an announcement on the BoJ's leadership in either late-February or early March.

II. Economic Calendar

Fig. 7. The week ahead

Time*	Country	Event	Period	Prior	Consensus
EM data					
	UAE	M2 Money Supply, m-o-m	Dec	0.4%	--
	UAE	Dubai Airport Cargo Volume, y-o-y	Dec	0.4%	--
	Saudi Arabia	Non-Oil Exports, y-o-y	Nov	13.1%	--
	Qatar	M2 Money Supply, y-o-y	Dec	18.9%	--
	Egypt	Production Index, m-o-m	Dec	3.8%	--
	India	Eight Infrastructure Industries	Dec	6.8%	--
	India	GDP Annual Estimate, y-o-y	2017	8%	--
Monday, 29 Jan					
17:30	US	Personal Income	Dec	0.3%	0.3%
17:30	US	Personal Spending	Dec	0.6%	0.4%
17:30	US	PCE Core, m-o-m	Dec	0.1%	0.2%
17:30	US	PCE Core, y-o-y	Dec	1.5%	1.5%
Tuesday, 30 Jan					
3:30	Japan	Jobless Rate	Dec	2.7%	2.7%
3:50	Japan	Retail Trade, y-o-y	Dec	2.2%	2.2%
13:30	UK	Mortgage Approvals	Dec	65.1K	63.5K
14:00	Eurozone	GDP SA, q-o-q	4Q A	0.6%	0.6%
14:00	Eurozone	GDP SA, y-o-y	4Q A	2.6%	2.7%
14:00	Eurozone	Consumer Confidence	Jan F	1.3	1.3
17:00	Germany	CPI EU Harmonized, y-o-y	Jan P	1.6%	1.6%
19:00	US	Conference Board Consumer Confidence	Jan	122.1	123
19:30	UK	Bank of England Governor Carney Speaks Before Lawmakers			
	US	President Trump's first State of the Union address			
Wednesday, 31 Jan					
3:50	Japan	BOJ Summary of Opinions			
3:50	Japan	Industrial Production, m-o-m	Dec P	0.5%	1.5%
4:01	UK	GfK Consumer Confidence	Jan	-13	-13
5:30	Japan	BOJ Iwata makes a speech in Oita			
14:00	Eurozone	Unemployment Rate	Dec	8.7%	8.7%
14:00	Eurozone	CPI Core, y-o-y	Jan A	0.9%	1%
14:00	Eurozone	CPI Estimate, y-o-y	Jan	1.4%	1.3%
17:15	US	ADP Employment Change	Jan	250K	185K
19:00	US	Pending Home Sales, m-o-m	Dec	0.2%	0.5%
23:00	US	FOMC Rate Decision (Upper Bound)	31-Jan	1.5%	1.5%
23:00	US	FOMC Rate Decision (Lower Bound)	31-Jan	1.25%	1.25%
Thursday, 1 Feb					
5:45	China	Caixin China PMI Manufacturing	Jan	51.5	51.5
13:30	UK	Markit UK PMI Manufacturing SA	Jan	56.3	56.5
17:30	US	Nonfarm Productivity	4Q P	3%	1%
17:30	US	Unit Labor Costs	4Q P	-0.2%	0.9%
19:00	US	ISM Manufacturing	Jan	59.3	58.6
Friday, 2 Feb					
3:50	Japan	Monetary Base, y-o-y	Jan	11.2%	--
17:30	US	Change in Nonfarm Payrolls	Jan	148K	180K
17:30	US	Change in Manufacturing Payrolls	Jan	25K	20K
17:30	US	Unemployment Rate	Jan	4.1%	4.1%
17:30	US	Average Hourly Earnings, m-o-m	Jan	0.3%	0.3%
17:30	US	Labor Force Participation Rate	Jan	62.7%	--
19:00	US	Factory Orders	Dec	1.3%	1.2%
19:00	US	University of Michigan Sentiment	Jan F	94.4	95
19:00	US	Durable Goods Orders	Dec F	2.9%	--

* UAE time

Source: Bloomberg

Fig. 8. Last week's data

Time*	Country	Event	Period	Prior	Consensus	Actual
MENA data						
	UAE	CPI, y-o-y	Dec	1.7%	--	2.70%
	Saudi Arabia	CPI, y-o-y	Dec	0.1%	--	0.4%
	Bahrain	CPI, y-o-y	Dec	2.9%	--	1.4%
	Bahrain	M2 Money Supply, y-o-y	Nov	3.3%	--	2.8%
	Kuwait	CPI, y-o-y	Dec	1.5%	--	1.1%
	Oman	Nominal GDP YTD, y-o-y	3Q	12.3%	--	10.1%
Monday, 22 Jan						
17:30	US	Chicago Fed Nat Activity Index	Dec	0.1	0.2	0.3
Tuesday, 23 Jan						
	Japan	BOJ 10-Yr Yield Target	23-Jan	0%	0%	0%
	Japan	BOJ Policy Balance Rate	23-Jan	-0.1%	-0.1%	-0.1%
8:30	Japan	All Industry Activity Index, m-o-m	Nov	0.3%	0.8%	1%
14:00	Germany	ZEW Survey Expectations	Jan	17.4	17.7	20.4
19:00	US	Richmond Fed Manufacturing Index	Jan	20	19	14
19:00	Eurozone	Consumer Confidence	Jan A	0.5	0.6	1.3
Wednesday, 24 Jan						
3:50	Japan	Trade Balance	Dec	112.2B	535B	359B
13:30	UK	Claimant Count Rate	Dec	2.3%	--	2.4%
13:30	UK	Jobless Claims Change	Dec	12.2K	--	8.6K
13:30	UK	Average Weekly Earnings, 3m/y-o-y	Nov	2.5%	2.5%	2.5%
13:30	UK	ILO Unemployment Rate, 3mths	Nov	4.3%	4.3%	4.3%
18:45	US	Markit US Manufacturing PMI	Jan P	55.1	55	55.5
19:00	US	Existing Home Sales	Dec	5.8M	5.7M	5.6M
Thursday, 25 Jan						
13:00	Germany	IFO Business Climate	Jan	117.2	117	117.6
16:45	Eurozone	ECB Main Refinancing Rate	25-Jan	0%	0%	0%
16:45	Eurozone	ECB Marginal Lending Facility	25-Jan	0.25%	0.25%	0.25%
16:45	Eurozone	ECB Deposit Facility Rate	25-Jan	-0.4%	-0.4%	-0.4%
19:00	US	New Home Sales	Dec	689K	675K	625K
19:00	US	Leading Index	Dec	0.5%	0.5%	0.6%
Friday, 26 Jan						
3:30	Japan	Natl CPI, y-o-y	Dec	0.6%	1.1%	1%
13:00	Eurozone	M3 Money Supply, y-o-y	Dec	4.9%	4.9%	4.6%
13:30	UK	GDP, q-o-q	4Q A	0.4%	0.4%	0.5%
13:30	UK	GDP, y-o-y	4Q A	1.7%	1.4%	1.5%
17:30	US	GDP Annualized, q-o-q	4Q A	3.2%	3%	2.6%
17:30	US	Personal Consumption	4Q	2.2%	3.7%	3.8%
17:30	US	Durable Goods Orders	Dec P	1.7%	0.8%	2.9%
17:30	US	Cap Goods Orders, Non-defence - ex air	Dec P	0.2%	0.6%	-0.3%
17:30	US	Cap Goods Shipments, Non-defence - ex-air	Dec P	0.4%	0.4%	0.6%

* UAE time

Source: Bloomberg

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