

## The Week Ahead: Turkey crisis generating global jitters

### ► **EM: Turkey emergency rate hike, Egypt central bank on hold**

In Turkey, we envisage the CBRT will likely have to implement an inter-meeting emergency rate hike to provide some vital support to the TRY, which continues to face immense selling pressure. The TRY weakened to a low of 7.23 against the USD after the US doubled tariffs on steel and aluminium from Turkey at the end of last week and is down 45.4% YTD. The next scheduled MPC meeting for the CBRT is on 13 September. Meanwhile, we expect the CBE to keep benchmark policy rates steady at its 16 August meeting. This would be the third consecutive meeting with rates on hold, after 200 bps of cumulative rate cuts at the January and February meetings. We believe that the CBE will need to see further signs of inflation decelerating after the government implemented another round of subsidy reforms mid-year. In line with our expectation, these latest increases in administered prices have had a relatively contained impact on inflation, including secondary. Headline inflation moderated to 13.5% y-o-y in July, from 14.5% in the previous month and we see further softening in inflation in the upcoming months. The year-end CPI print should be well within the CBE's target range of 13%  $\pm$ 3%. We believe that the central bank will also take into account portfolio flows amidst tightening US monetary policy before resuming its rate-cutting cycle.

### ► **US: Rise in core retail sales growth forecast for July**

Trade tensions with China continue to escalate, with the US announcing that it will implement 25% tariffs on 279 Chinese goods worth USD16 billion from 23 August (proposed in June). China will retaliate with measures of similar magnitude against US goods – with tariffs to come into effect on the same day. However, there are some indications that the US is willing to defuse tensions with other key trading partners, including Mexico, Japan and the EU. Data wise, key releases this week will be US retail sales and housing data for July. Consensus estimates core retail sales growth (ex-auto and gas) strengthened to 0.4% m-o-m in July (June: 0.3%), likely bolstered by Amazon's prime day sales. This is also expected to boost the retail sales control group (feeds into GDP data), with an acceleration to 0.5% m-o-m in July (June: 0%). Notably, core inflation strengthened to a near 10-year high of 2.4% y-o-y in July, with broad-based increases in both goods and services inflation (page 2).

### ► **EM: India inflation and China retail sales data**

July CPI data for India (due 13 August) will be closely watched after the RBI raised its repo rate in two consecutive meetings citing upside risks to inflation. Consensus forecasts headline inflation decelerated to 4.5% y-o-y in July (June: 5%) after three successive months of strengthening. However, core inflation is envisaged to remain close to 6% due to the recent INR depreciation and rise in housing costs. In China, July retail sales and industrial production data are due this week. Chinese trade data released last week suggests that export growth strengthened in July, implying a limited impact from the first round of tariffs. We believe that this is partly due to the sharp CNY depreciation since mid-June and as exports were frontloaded ahead of further increases in tariffs.

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# I. Recent Events and Data Releases

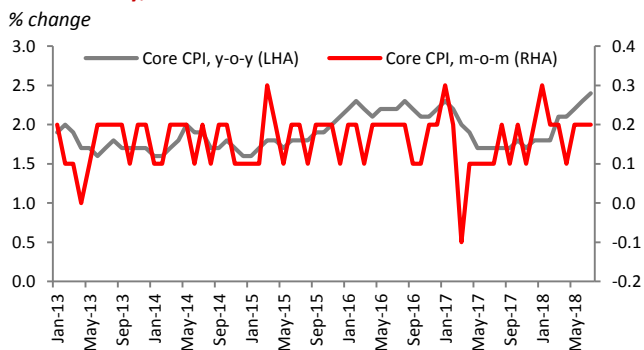
## A. G4 Economies

### US: Annual core inflation reaches 10-year high of 2.4% y-o-y in July

The inflation report for July was solid, with both annual and monthly core inflation showing signs of strong momentum. Annual core inflation accelerated to 2.4% y-o-y in July, from 2.3% in June – the highest point since October 2008 – though monthly core inflation remained steady at 0.2% m-o-m (0.243% unrounded). The m-o-m rise in core inflation was driven by both goods and services inflation. Notably, the deflation in goods has continued to moderate since September 2017 and reached zero y-o-y growth for the first time since February 2016 (Fig. 2). The key driver of goods inflation in July was a pickup in used-car prices (1.3% m-o-m), following a soft trend in early 2018 due to a post-hurricane slowdown. Core services inflation was driven by the shelter component, up 0.3% m-o-m in July from 0.1% in June. Both rent of primary residence and "owners' equivalent rent of primary residence" rose by 0.3% m-o-m. We believe that rental inflation will remain firm given the rising demand for housing, alongside signs of a shortage of housing inventories. Meanwhile, headline inflation also strengthened to 0.2% m-o-m in July led by food prices. However, energy prices dropped in July, with contractions seen in both electricity and gasoline prices.

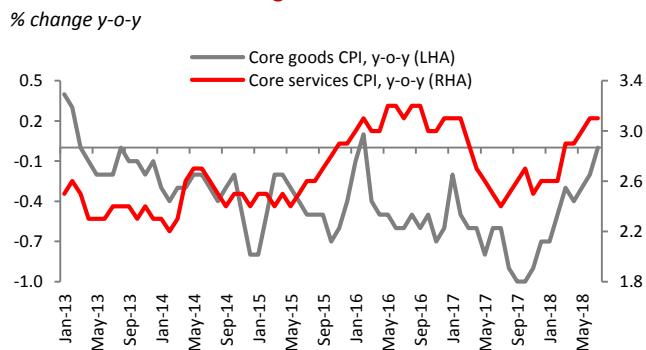
*Core inflation strengthens to 2.4% y-o-y in July, driven by shelter and used car prices*

**Fig. 1. US: Annual core inflation accelerates to 2.4% y-o-y in July, from 2.3% in June**



Source: Bureau of Labor statistics

**Fig. 2. US: Core services inflation rising in tandem with lower deflation in core goods**



Source: Bureau of Labor statistics

We believe that the rise in inflation was due to a combination of factors, including solid economic activity and jobs growth supporting demand for single-unit housing, and the rise in crude oil prices. However, there were no signs that these factors will lead inflation to overshoot the Fed’s target significantly in the near term. We expect inflation to rise modestly on the back of rising wages and higher tariffs on some consumer goods but remain close to 2%. Moreover, we envisage that the wider corporate profit margins following tax reform will allow producers to absorb some of the rising costs arising from trade tariffs. Thus, we expect inflationary pressures to remain anchored, allowing the Fed to continue to hike steadily in 2H2018 and 2019. We note that core PCE was weaker at 1.9% y-o-y for June, with a lower weighting for the shelter component than core CPI.

*Inflation to remain anchored in near term, allowing Fed to raise FFTR steadily*

## US: June JOLTS data continue to signal solid labour market

The JOLTS data for June continued to reflect solid labour market conditions, with job openings increasing to 6,662K in June (consensus: 6,625K) from 6,659K in May. Private sector and government job openings were largely unchanged in July. However, there were some notable changes in the sub sectors, with job openings increased in educational services (20K) and trade (47K), whereas openings in transportation, warehousing, and utilities fell by 84K. Despite the modest increase in job openings, the hiring rate decelerated to 3.8% in June from 3.9% in May. Meanwhile, the quits rate remained steady for a fourth consecutive month at 2.3% in July.

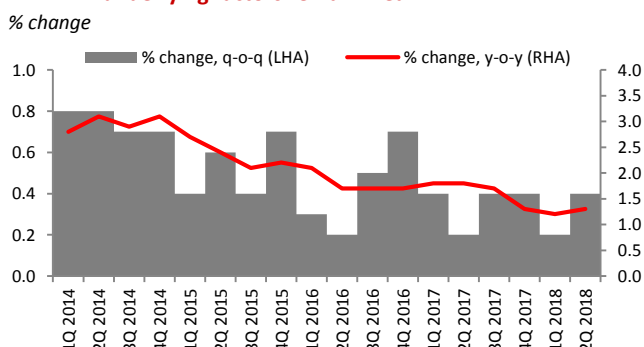
*Job openings rose modestly in June, indicating healthy labour market conditions*

## UK: Economic activity loses some momentum at end of 2Q

UK GDP growth accelerated to 0.4% q-o-q in 2Q (unrounded: 0.36%), from 0.2% in 1Q, in line with market expectations. This was mainly due to a moderate uptick in domestic demand. Private consumption strengthened marginally to 0.3% q-o-q in 2Q (1Q: 0.2%), though came in lower than the consensus estimate of 0.4% growth. This suggests that the weak consumer confidence remains a headwind for household spending. Gross fixed capital formation growth rebounded to 0.8% q-o-q in 2Q, (1Q: -1.3%), the same level as in 4Q2017, indicating that investment activity just about recovered from the lost ground in 1Q. Meanwhile, net trade contributed negatively to the growth with a contraction in both exports (3.6% q-o-q) and imports (0.8% q-o-q). Moreover, June monthly GDP data surprised to the downside and decelerated to 0.1% m-o-m (consensus: 0.2% and May: 0.3%), suggesting that economic activity slowed down markedly at the end of 2Q. We believe that economic activity in 2H will remain relatively soft on the back of increasing Brexit uncertainty, weakening of the GBP impacting private consumption and potentially rising global trade tensions.

*2Q GDP growth strengthens to 0.4% q-o-q in 2Q, despite soft economic activity in June*

**Fig. 3. UK: 2Q GDP growth rebounds to 0.4% q-o-q, though underlying factors remain weak**



Source: Office for National Statistics

**Fig. 4. UK: GBP weakens further against USD with markets trying to price in 'no deal' Brexit**



Source: Bloomberg

**Brexit negotiations:** GBP continued to weaken against the USD last week amid increasing uncertainty over whether the UK will leave the EU with a deal (Fig 4). This was after UK Prime Minister Theresa May wrote to Conservative Party members that negotiations with the EU had reached an impasse and that the EU's trade offers – either i) a standard free-trade deal, or ii) membership of the customs union plus an extended version of the European Economic Area – are not acceptable to the UK. Moreover, there were news reports that the UK is planning for a no-deal Brexit, with Theresa May likely organising a cabinet summit on that issue in early September. With the Brexit negotiations entering

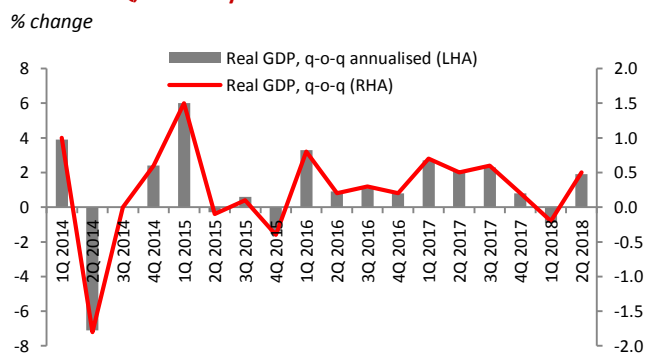
a crucial phase, we expect no-deal rhetoric to dominate market sentiment until the EU summit in October. The latest round of Brexit talks between the EU and the UK resumes in Brussels on 16 August.

### Japan: GDP growth accelerates in 2Q, led by robust domestic demand

Japan’s 2Q GDP data confirmed that the contraction in 1Q was due to one-off weather related factors and had no meaningful impact on the second quarter activity. Growth rebounded to 0.5% q-o-q in 2Q, after contracting by 0.2% in the previous quarter. This was higher than the consensus estimate of 0.3% q-o-q. The better-than-expected result was largely due to robust consumption and investment activity. Private consumption accelerated to 0.7% q-o-q (consensus: 0.2% and 1Q: -0.2%), reflecting a steady recovery in household spending on the back of rising wages. Business spending growth also strengthened to a six-quarter high of 1.3% q-o-q, from an upwardly revised 0.5% in 1Q. Non-residential investment activity remains the key driver of investment growth, whilst residential investment continued to contract, prolonging the negative growth for a fourth successive quarter. However, net exports contributed negatively to the growth, with exports growth decelerating to 0.2% q-o-q in 2Q (1Q: 0.6%), whereas imports grew by a robust 1% (1Q: 0.2%). We expect investment activity to remain the key driver of growth in 3Q. However, the heat waves and floods seen in 3Q are likely to have some negative impact on household consumption.

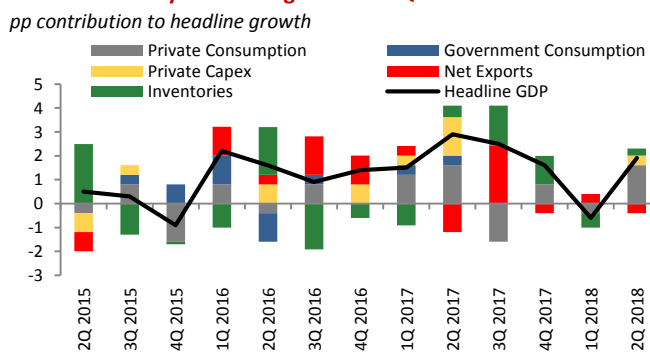
*2Q GDP growth rebounds to 0.5% q-o-q, driven by domestic demand*

**Fig. 5. Japan: Real GDP growth strengthens to 0.5% q-o-q in 2Q, driven by domestic demand**



Source: Economic and Social Research Institute Japan

**Fig. 6. Japan: Personal consumption and business spending the key drivers of growth in 2Q**



Source: Economic and Social Research Institute Japan

## B. Emerging Market Economies

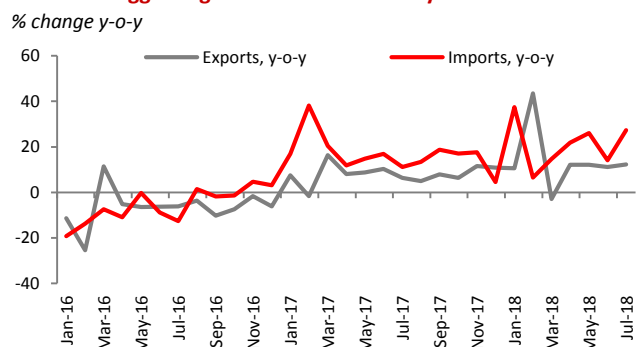
### China: July export growth solid – no impact of trade tariffs yet

China’s July trade data released last week showed that trade tariffs are yet to have any meaningful impact on the economy. Notably, the US and China levied 25% tariffs on each other’s imports worth USD34 billion, effective from 6 July. Nonetheless, export growth accelerated to 12.2% y-o-y in July from 11.2% in June, beating the consensus expectation of 10%. The growth was largely driven by high-tech goods (12% y-o-y), which are under review by the US administration. We believe that this is likely due to manufacturers rushing to buy before the proposed tariffs on USD200 billion worth of Chinese goods, likely to come into effect in September. In addition, the US announced last week that it will implement 25% tariffs on 279 Chinese goods worth USD16 billion, effective from 23

*Export growth strengthens to 12.2% y-o-y in July from 11.2% in June*

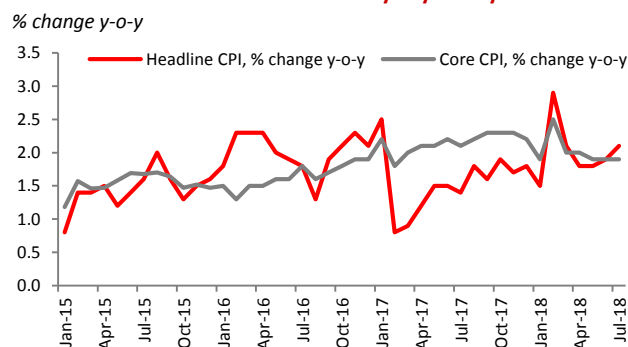
August. Thus, we believe that the impact of all these tariffs will become more visible in the 4Q2018 and early-2019. Meanwhile, import growth also strengthened, to 27.3% y-o-y in July from 14.1% in June, reflecting continued robust domestic demand. With imports growing at a faster pace than exports, the trade surplus narrowed to USD28.1 billion in July from USD41.5 billion in June.

**Fig. 7. China: Exports growth surprises to upside in July, suggesting that trade tariffs are yet to feed into data**



Source: Customs General Administration PRC

**Fig. 8. China: Core inflation remains steady for the third consecutive month at 1.9% y-o-y in July**



Source: National Bureau of Statistics of China

Meanwhile, China's headline inflation accelerated to 2.1% y-o-y in July, higher than both the consensus estimate of 2% and June print of 1.9%. This was mainly driven by the rise in transportation and recreational prices. However, core inflation remained steady for the third consecutive month at 1.9% y-o-y in July. We believe that China's retaliatory tariffs on US goods are likely to have limited additional impact given that most of the targeted US goods do not fall into the CPI basket. Moreover, this could be partially offset by China's counter measures to lower tariffs on selected household goods, autos and agricultural imports from non-US countries. We believe that the recent CNY depreciation will remain one of the key factors for the near-term inflation outlook. Overall, we expect headline inflation to remain well below the PBoC's 3% target, allowing the central bank to further reduce the reserve requirement ratio (RRR) by at least 100 bps for selected industries in 2H2018.

*PBoC to further reduce RRR by at least 100 bps in 2H2018*

## II. Economic Calendar

Fig. 9. The week ahead

Time*	Country	Event	Period	Prior	Consensus
<b>Expected this week</b>					
	UAE	M2 Money Supply, m-o-m	Jul	-0.3%	
	UAE	Central Bank Foreign Assets	Jul	331.1B	
	UAE	Dubai Economy Tracker SA	Jul	56	
	Saudi Arabia	CPI, y-o-y	Jul	2.1%	
	Oman	CPI, y-o-y	Jul	1.4%	
	Qatar	CPI, y-o-y	Jul	0.1%	
	Egypt	Trade Balance	Jun	-3842M	
	China	Money Supply M2, y-o-y	Jul	8%	8.2%
	China	New Yuan Loans CNY	Jul	1840B	1275B
	India	Exports, y-o-y	Jul	17.6%	
<b>Monday, 13 August</b>					
16:00	India	CPI, y-o-y	Jul	5%	4.5%
<b>Tuesday, 14 August</b>					
6:00	China	Retail Sales, y-o-y	Jul	9%	9.1%
6:00	China	Industrial Production, y-o-y	Jul	6%	6.3%
8:30	Japan	Industrial Production, m-o-m	Jun F	-2.1%	
10:00	Germany	GDP SA, q-o-q	2Q P	0.3%	0.4%
12:30	UK	Jobless Claims Change	Jul	7.8K	
12:30	UK	Average Weekly Earnings 3M/y-o-y	Jun	2.5%	2.5%
12:30	UK	Weekly Earnings, ex-bonus 3M/y-o-y	Jun	2.7%	2.7%
12:30	UK	ILO Unemployment Rate 3M	Jun	4.2%	4.2%
13:00	Eurozone	Industrial Production SA, m-o-m	Jun	1.3%	-0.4%
13:00	Eurozone	GDP SA, q-o-q	2Q P	0.3%	0.3%
13:00	Eurozone	GDP SA, y-o-y	2Q P	2.1%	2.1%
16:30	US	Import Price Index, m-o-m	Jul	-0.4%	0%
<b>Wednesday, 15 August</b>					
11:00	Turkey	Unemployment Rate	May	9.6%	
12:30	UK	CPI, m-o-m	Jul	0%	0%
12:30	UK	CPI, y-o-y	Jul	2.4%	2.5%
12:30	UK	CPI Core, y-o-y	Jul	1.9%	1.9%
16:30	US	Empire Manufacturing	Aug	22.6	20
16:30	US	Retail Sales Advance, m-o-m	Jul	0.5%	0.1%
16:30	US	Retail Sales, ex-Auto, m-o-m	Jul	0.4%	0.3%
16:30	US	Retail Sales Control Group	Jul	0.0%	0.4%
17:15	US	Industrial Production, m-o-m	Jul	0.6%	0.3%
<b>Thursday, 16 August</b>					
3:50	Japan	Trade Balance	Jul	¥721.4B	-¥41.2B
11:00	Turkey	Industrial Production, y-o-y	Jun	6.4%	5%
12:30	UK	Retail Sales, ex-Auto Fuel, m-o-m	Jul	-0.6%	0%
12:30	UK	Retail Sales, Incl-Auto Fuel, m-o-m	Jul	-0.5%	0.2%
16:30	US	Housing Starts	Jul	1173K	1260K
16:30	US	Building Permits	Jul	1273K	1310K
	Egypt	Lending Rate	16-Aug	17.75%	
	Egypt	Deposit Rate	16-Aug	16.75%	
<b>Friday, 17 August</b>					
11:00	Turkey	Consumer Confidence Index	Aug	73.1	
13:00	Eurozone	CPI Core, y-o-y	Jul F	1.1%	1.1%
13:00	Eurozone	CPI, y-o-y	Jul F	2%	2.1%
18:00	US	Leading Index	Jul	0.5%	0.4%
18:00	US	University of Michigan Sentiment	Aug P	97.9	98

\* UAE time

Source: Bloomberg

Fig. 10. Last week's data

Time*	Country	Event	Period	Prior	Consensus	Actual
<b>MENA Economies</b>						
	Kuwait	Annual GDP Constant, y-o-y	2017	2.9%		-3.5%
	Qatar	Qatar PMI	Jul	51.8		52
	Egypt	Urban CPI, y-o-y	Jul	14.4%		13.5%
	Egypt	Urban CPI, m-o-m	Jul	3.5%		2.4%
<b>Monday, 6 August</b>						
10:00	Germany	Factory Orders, m-o-m	Jun	2.6%	-0.5%	-4%
12:30	Eurozone	Sentix Investor Confidence	Aug	12.1	13.4	14.7
	China	BoP Current Account Balance	2Q P	-\$34.1B		\$5.1B
<b>Tuesday, 7 August</b>						
10:00	Germany	Industrial Production SA, m-o-m	Jun	2.4%	-0.5%	-0.9%
11:30	UK	Halifax House Prices, m-o-m	Jul	0.9%	0.2%	1.4%
18:00	US	JOLTS Job Openings	Jun	6659	6625	6662
	China	Foreign Reserves	Jul	\$3112.1B	\$3107B	\$3117.9B
<b>Wednesday, 8 August</b>						
3:50	Japan	BoP Current Account Balance	Jun	¥1938.3B	¥1222.2B	¥1175.6B
	China	Trade Balance	Jul	\$41.5B	\$38.9B	\$28.1B
	China	Imports, y-o-y	Jul	14.1%	16.5%	27.3%
	China	Exports, y-o-y	Jul	11.2%	10%	12.2%
	China	Foreign Direct Investment, y-o-y CNY	Jul	0.3%		
<b>Thursday, 9 August</b>						
3:50	Japan	Money Stock M2, y-o-y	Jul	3.1%	3.1%	3%
3:50	Japan	Core Machine Orders, m-o-m	Jun	-3.7%	-1%	-8.8%
5:30	China	PPI, y-o-y	Jul	4.7%	4.5%	4.6%
5:30	China	CPI, y-o-y	Jul	1.9%	2%	2.1%
10:00	Japan	Machine Tool Orders, y-o-y	Jul P	11.4%		13%
16:30	US	PPI Final Demand, m-o-m	Jul	0.3%	0.2%	0.3%
16:30	US	PPI Final Demand, y-o-y	Jul	3.4%	3.4%	3.3%
18:00	US	Wholesale Inventories, m-o-m	Jun F	0%	0%	0.1%
<b>Friday, 10 August</b>						
3:50	Japan	GDP SA, q-o-q	2Q P	-0.2%	0.3%	0.5%
3:50	Japan	GDP Annualized SA, q-o-q	2Q P	-0.9%	1.4%	1.9%
8:30	Japan	Tertiary Industry Index, m-o-m	Jun	0.2%	-0.3%	-0.5%
11:00	Turkey	Current Account Balance	Jun	-6.2B	-3B	-3B
12:30	UK	Trade Balance	Jun	-£3141	-£2500	-£1861
12:30	UK	Industrial Production, m-o-m	Jun	-0.2%	0.3%	0.4%
12:30	UK	Manufacturing Production, m-o-m	Jun	0.6%	0.3%	0.4%
12:30	UK	GDP, q-o-q	2Q P	0.2%	0.4%	0.4%
12:30	UK	GDP, y-o-y	2Q P	1.2%	1.3%	1.3%
12:30	UK	Private Consumption, q-o-q	2Q P	0.2%	0.4%	0.3%
12:30	UK	Government Spending, q-o-q	2Q P	0.4%	0.3%	0.4%
12:30	UK	Gross Fixed Capital Formation, q-o-q	2Q P	-1.3%	0.7%	0.8%
12:30	UK	Exports, q-o-q	2Q P	0%	0.7%	-3.6%
12:30	UK	Imports, q-o-q	2Q P	-0.2%	0.8%	-0.8%
16:00	India	Industrial Production, y-o-y	Jun	3.9%	5.5%	7%
16:30	US	CPI, m-o-m	Jul	0.1%	0.2%	0.2%
16:30	US	CPI, ex-Food and Energy, m-o-m	Jul	0.2%	0.2%	0.2%
16:30	US	CPI, y-o-y	Jul	2.9%	2.9%	2.9%
16:30	US	CPI, ex-Food and Energy, y-o-y	Jul	2.3%	2.3%	2.4%
22:00	US	Monthly Budget Statement	Jul	-\$42.9B	-\$75.4B	-\$76.9B

\* UAE time

Source: Bloomberg

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