# The Week Ahead: ECB to stay on course; CBRT to hike again

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## Contents



## Eurozone: No change to ECB policy, dovish tone to continue

The ECB is expected to keep its monetary policy steady at its 26 July meeting after announcing in the previous meeting that its asset-purchase programme would end by Dec-2018. We believe that market attention will be particularly on Draghi's comments on the interpretation of the guidance that rates will be unchanged "at least through the summer of 2019". However, we expect the ECB to keep the forward guidance unchanged in the post-meeting statement, despite the market's varying interpretations of the "summer" rate hike timing. The tone of the meeting is likely to be moderately dovish as core inflation remains subdued despite headline inflation reaching the ECB's 2% target in June. Market focus will also be on the rising trade tensions across the globe and their likely impact on the growth and inflation outlook. However, we envisage the GC will reiterate its confidence in the medium-term growth outlook with risks remaining broadly balanced. The ECB is also expected to reiterate that reinvestments will continue for "an extended period of time".

## US: First print of 2Q GDP and WTO general council meeting

The key US data releases this week will be the first print of 2Q GDP, durable goods sales and home sales for June. Consensus forecasts 2Q GDP growth accelerated to a 15-quarter high of 4.3% q-o-q SAAR, up from 2% in 1Q. We envisage a broad-based strengthening in economic activity supported by the government's tax cuts and increased spending. Personal consumption will likely be the key driver of the growth, which is estimated to have strengthened to 3.1% q-o-q in 2Q, up from a muted 0.9% in 1Q. Incoming data, including retail sales and industrial production, also suggest that economic activity grew at a solid pace in 2Q (page 3). Residential investment, government spending and trade are also seen rising in 2Q. However, inventories are likely to have contributed negatively to the headline growth. Separately, the WTO will hold its general council meeting on 26-27 July. It remains to be seen how the WTO will respond to the recent complaints filed by the US and China accusing each other of violating trade rules.

## Turkey: Further rate hike expected in July

We expect the CBRT to raise its one-week repo rate by 100 bps to 18.75% at its 24 July MPC meeting. The tone of the meeting is likely to remain hawkish as the inflation outlook deteriorated further in June. Notably, headline inflation accelerated to an almost 15-year high of 15.3% y-o-y in June with price pressures remaining broad-based. We believe that headline inflation will rise further in the coming months and reach a high of 17% y-o-y in 3Q. The surge in inflation in June has already reduced the real one-week repo interest rate to 250 bps. Moreover, the government's announcement of amendments to central bank law also augmented foreign investors' concerns related to central bank independence. Given the overall deterioration in the inflation outlook, increasing policy uncertainty and rising external risks, we do not rule out the possibility of the CBRT raising its policy rate more steeply than our expectation of a 100 bps hike.

# I. Recent Events and Data Releases

## A. G4 Economies

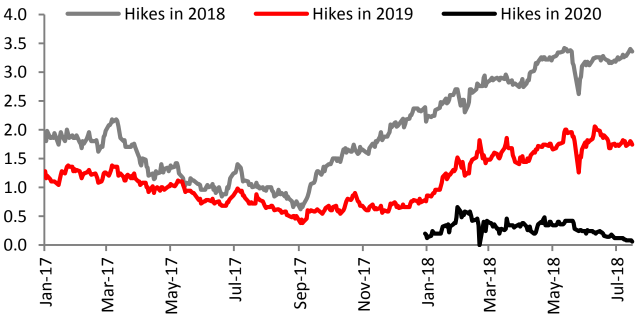
### US: Powell retains optimistic tone on economic outlook

*Powell expresses increasing confidence in economy*

There were limited new details in Fed Chair Jerome Powell's semi-annual Humphry Hawkins testimony to Congress on monetary policy. Powell highlighted that with a strong job market, inflation close to the Fed's objective and the risks to the outlook roughly balanced, the FOMC "believes that - for now - the best way forward is to keep gradually raising the federal funds rate". Notably, Powell emphasised that fiscal stimulus is likely to remain supportive of economic growth for the next few years, echoing his increasing confidence in the economy. On the inflation front, he said that it is too early to declare victory on achieving the inflation goal. He also added that wage growth is only rising at a moderate pace due to low productivity and hence there is limited upside pressure on inflation.

**Fig. 1. US: Market expectation of four rate hikes in 2018 remains intact, supported by hawkish Fed tone**

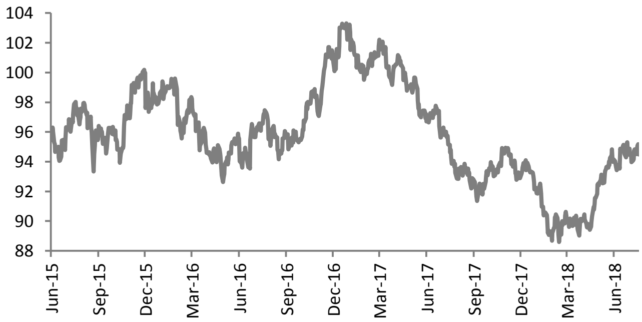
*Number of 25 bps hikes*




Source: Bloomberg, ADCB estimates

**Fig. 2. US: Dollar index continues to strengthen amid rising rate hike expectations and increasing trade tensions**

*DXY index*




Source: Bloomberg

*Fed communication consistent with two additional rate hikes in 2H2018*

However, Powell acknowledged that trade protectionism and weaker-than-expected overseas growth pose downside risks to the outlook. He highlighted that trade-related issues are dealt with by Congress and that the Fed will not get involved. However, he stressed that protectionism could have significant effects on the economy. Moreover, he highlighted that those countries that have remained open to trade "have grown faster, have had higher incomes, higher productivity, and countries that have gone in a more protectionist direction have done worse". With respect to the flattening yield curve, Powell stated that "what matters is [the] neutral rate". In our view, the Fed's message is that the inverted yield curve is unlikely to alter its steady rate-hiking guidance. Overall, we believe that Powell's comments during his testimony were largely in line with the FOMC's median dot plot projections presented in June. The Fed's outlook is consistent with our expectation of two additional 25 bps rate hikes in 2H2018 (September and December).

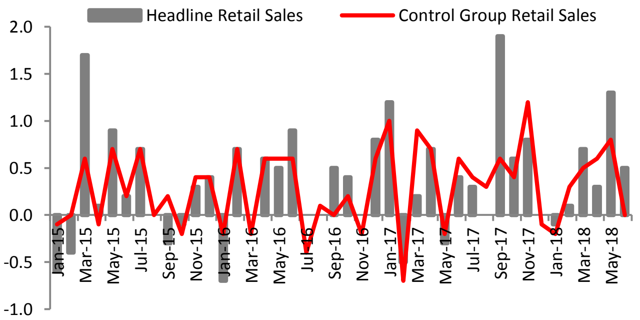
## US: Retail sales and industrial activity point to solid 2Q GDP growth

*High-frequency data points to solid 2Q GDP growth*

Strong retail sales and industrial output figures for June suggest that economic growth accelerated sharply in 2Q2018. Headline retail sales grew by a healthy 0.5% m-o-m in June after rising by 1.3% in May (upwardly revised). Auto and gasoline sales were the key drivers of the retail activity, suggesting that consumer spending remained robust. We believe that higher after-tax disposable income continued to support consumption. The retail sales control group, which feeds into personal consumption, was flat in June, though the May print was revised up sharply to 0.8% m-o-m from 0.5% in the first estimate. Meanwhile, industrial production rebounded in June and grew by 0.6% m-o-m (May: -0.5%), beating the consensus estimate of 0.5%. The rise in industrial activity was largely driven by manufacturing output, which rose 0.8% m-o-m after contracting 1% in May. The key drivers of industrial growth have been demand-driven motor vehicle production and parts production, suggesting that the appetite for inventory accumulation remains strong in the auto industry.

**Fig. 3. US: Headline retail sales remain healthy in June, boosted by auto and gasoline spending**

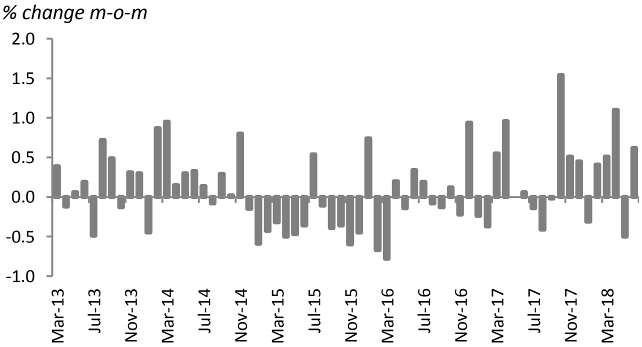
*% change m-o-m*




Source: US Census Bureau

**Fig. 4. US: Industrial production rebounds in June, driven by robust manufacturing activity**

*% change m-o-m*




Source: Federal Reserve

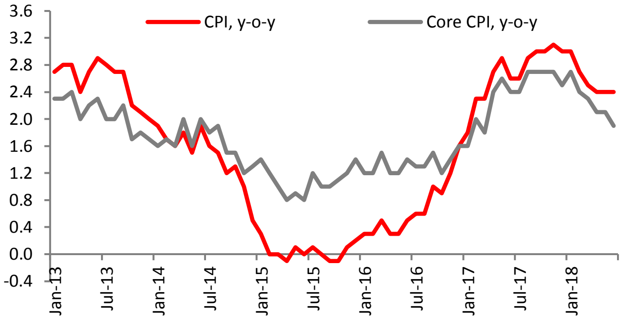
## UK: June inflation softer than expected; wage growth subdued

*Weak inflation and wage data unlikely to stop BoE's 25 bps rate hike in August*

The inflation and labour market data released last week provided further evidence of relatively subdued wage growth and weaker underlying inflation in the UK in June. This supports our view that there are no compelling reasons for the BoE to hike interest rates. However, with BoE members' comments already pointing towards a 25 bps rate hike in August, we expect the central bank to proceed with a hike at its next meeting and then remain on hold for the rest of 2018. Both headline and core inflation came in weaker than the market's expectations in June. Core inflation decelerated to 1.9% y-o-y, lower than both the consensus estimate and the previous month's 2.1%. This was due to a moderation in volatile air fares, clothing and a contraction in computer games. We believe that air fares and gaming prices are likely to reverse back in July but clothing prices are likely to remain subdued due to ongoing summer discount offers. However, headline inflation remained steady at 2.4% y-o-y in June, albeit below the market's expectation of 2.6%. Higher energy prices were the key driver of headline inflation.

**Fig. 5. UK: Core inflation surprises to downside and decelerates to 1.9% y-o-y in June**

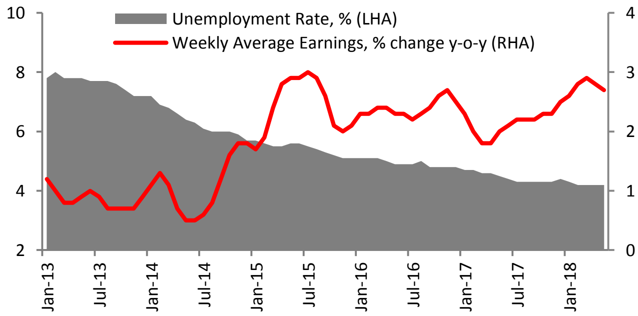
*% change, y-o-y*




Source: UK Office for National Statistics

**Fig. 6. UK: Wage growth remains subdued in May, though unemployment rate steady**

*% (LHA); % change y-o-y (RHA)*



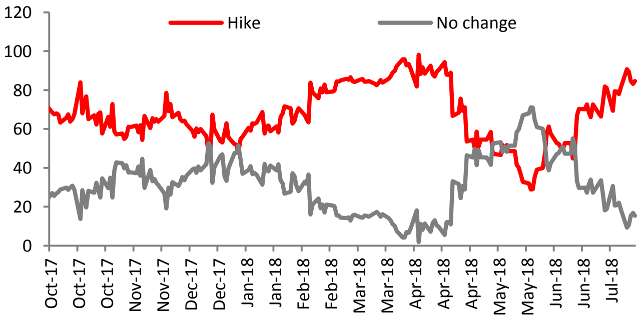

Source: UK Office for National Statistics

Labour market data for May came in line with the market's expectations but there were no signs of wage growth rising. Headline wage growth decelerated to 2.5% y-o-y in the 3M period to May from an upwardly revised 2.6% in April. This is the softest pace of annual headline wage growth since December, suggesting that wage growth could have peaked already. Average weekly earnings excluding bonuses, also softened in May. We believe that wage growth will remain muted in the near future until corporates have more clarity regarding any Brexit deal. Meanwhile, unemployment rate remained unchanged for the fourth consecutive month at 4.2% in May.

*Wage growth to remain subdued in coming months*

**Fig. 7. UK: Market expectation of August rate hike is intact, despite data surprising to downside**

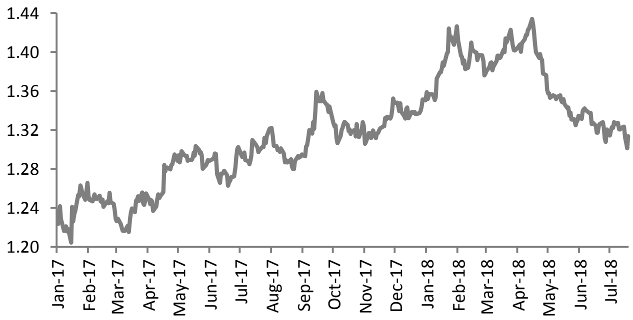
*%*




Source: Bloomberg

**Fig. 8. UK: GBP remains under pressure driven by both political uncertainty and weak data**

*GBP:USD*




Source: Bloomberg

# B. Emerging Market Economies

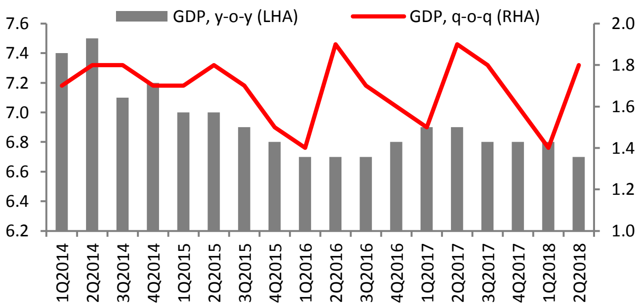
## China: GDP growth moderates in 2Q, in line with expectations

China's GDP growth softened to 6.7% y-o-y in 2Q from 6.8% in 1Q18 – in line with the market's expectations. The slowdown in activity was largely due to the secondary sector, which decelerated to 6.1% y-o-y in 2Q from 6.3% in 1Q. However, this was partially offset by growth in the services sector, which strengthened to 7.6% y-o-y in 2Q (1Q: 7.5%). The moderation in 2Q growth was largely consistent with the downtrend seen in the high

*China's GDP growth likely to decelerate further in 2H2018, albeit in a gradual manner* frequency data, including industrial production, fixed asset investment and retail sales. We expect GDP growth to decelerate further in a gradual manner in 2H on the back of rising trade tensions and the government's targeted deleveraging process. However, we do not expect any sharp slowdown in activity and believe that the Chinese government will be able to achieve its target of 6.5% growth for 2018.

**Fig. 9. China: Annual GDP growth softens to 6.7% y-o-y in 2Q2018, from 6.8% in 1Q**

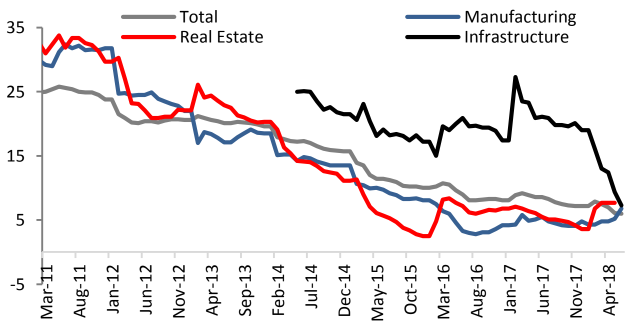
*% change*




Source: National Bureau of Statistics of China

**Fig. 10. China: Infrastructure investment continues to decelerate sharply in 2018**

*% change y-o-y*




Source: National Bureau of Statistics of China

*We expect PBoC to cut RRR by at least 100 bps in 2H2018*

We believe that the PBoC will further reduce its reserve requirement ratio (RRR) by at least 100 bps in 2H2018 to support the weakening economic momentum. Thus, we expect the CNY to depreciate further in 2H. Moreover, the government is anticipated to review its 1H economic activity and discuss its outlook for 2H at the upcoming Politburo meeting in July. We believe that the PBoC and the government will work together to counter the likely impact of trade tariffs on specific industries.

# II. Economic Calendar

**Fig. 11. The week ahead**

| Time* | Country | Event | Period | Prior | Consensus |
|---|---|---|---|---|---|
| **Expected this week** | | | | | |
| | UAE | Dubai Airport Cargo Volume, y-o-y | Jun | -4.9% | |
| | UAE | CPI, y-o-y | Jun | 3.5% | |
| | Saudi Arabia | CPI, y-o-y | Jun | 2.3% | |
| | Saudi Arabia | Non-Oil Exports, y-o-y | May | 26.5% | |
| | Bahrain | CPI, y-o-y | Jun | 2.8% | |
| | Kuwait | Annual GDP Current, y-o-y | 2017 | -2.8% | |
| | Qatar | Trade Balance Month | Jun | 14880M | |
| **Monday, 23 July** | | | | | |
| 13:00 | UK | German, U.K. Foreign Ministers Hold Talks in Berlin | | | |
| 16:30 | US | Chicago Fed National Activity Index | Jun | -0.2 | 0.3 |
| 18:00 | Eurozone | Consumer Confidence | Jul A | -0.5 | -0.7 |
| 18:00 | US | Existing Home Sales | Jun | 5.4M | 5.5M |
| 21:00 | UK | BOE's Broadbent Speaks in London | | | |
| **Tuesday, 24 July** | | | | | |
| 4:30 | Japan | Nikkei Japan PMI Manufacturing | Jul P | 53 | |
| 9:00 | Japan | Leading Index CI | May F | 106.9 | |
| 12:00 | Eurozone | Markit Eurozone Manufacturing PMI | Jul P | 54.9 | 54.7 |
| 15:00 | Turkey | One-Week Repo Rate | 24-Jul | 17.75% | 18.75% |
| 17:00 | US | FHFA House Price Index, m-o-m | May | 0.1% | 0.3% |
| 17:45 | US | Markit US Manufacturing PMI | Jul P | 55.4 | 55.1 |
| 17:45 | US | Markit US Services PMI | Jul P | 56.5 | 56.5 |
| 17:45 | US | Markit US Composite PMI | Jul P | 56.2 | |
| 18:00 | US | Richmond Fed Manufacturing Index | Jul | 20 | 18 |
| **Wednesday, 25 July** | | | | | |
| 12:00 | Eurozone | M3 Money Supply, y-o-y | Jun | 4% | 4% |
| 12:00 | Germany | IFO Business Climate | Jul | 101.8 | 101.5 |
| 12:00 | Germany | IFO Expectations | Jul | 98.6 | 98.3 |
| 12:00 | Germany | IFO Current Assessment | Jul | 105.1 | 104.9 |
| 15:00 | US | MBA Mortgage Applications | 20-Jul | -2.5% | |
| 18:00 | US | New Home Sales | Jun | 689K | 669K |
| **Thursday, 26 July** | | | | | |
| 10:00 | Germany | GfK Consumer Confidence | Aug | 10.7 | 10.7 |
| 15:45 | Eurozone | ECB Main Refinancing Rate | 26-Jul | 0% | 0% |
| 15:45 | Eurozone | ECB Marginal Lending Facility | 26-Jul | 0.25% | 0.25% |
| 15:45 | Eurozone | ECB Deposit Facility Rate | 26-Jul | -0.4% | -0.4% |
| 16:30 | Eurozone | ECB President Draghi Holds Press Conference in Frankfurt | | | |
| 16:30 | US | Wholesale Inventories, m-o-m | Jun P | 0.6% | 0.5% |
| 16:30 | US | Durable Goods Orders | Jun P | -0.4% | 3% |
| 16:30 | US | Durables, ex-transportation | Jun P | 0% | 0.5% |
| 16:30 | US | Cap Goods Shipments, non-defence, ex-air | Jun P | 0.2% | 0.4% |
| **Friday, 27 July** | | | | | |
| 3:30 | Japan | Tokyo CPI, y-o-y | Jul | 0.6% | 0.6% |
| 3:30 | Japan | Tokyo CPI, ex-Fresh Food, y-o-y | Jul | 0.7% | 0.7% |
| 12:00 | Eurozone | ECB Survey of Professional Forecasters | | | |
| 16:30 | US | GDP Annualized, q-o-q | 2Q A | 2% | 4.3% |
| 16:30 | US | Personal Consumption | 2Q A | 0.9% | 3.1% |
| 16:30 | US | GDP Price Index | 2Q A | 2.2% | 2.3% |
| 16:30 | US | Core PCE, q-o-q | 2Q A | 2.3% | 2.2% |
| 18:00 | US | University of Michigan. Sentiment | Jul F | 97.1 | 97.1 |

* 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 | Jun | -0.7% | | -0.3% |
| | UAE | Central Bank Foreign Assets | Jun | 326.6B | | 331.1B |
| | Qatar | CPI, y-o-y | Jun | 0.5% | | 0.1% |
| | Egypt | Trade Balance | May | -3315M | | -3842M |
| | Oman | Budget Balance Month | May | -56.9M | | -287.5M |
| | Kuwait | CPI, y-o-y | Jun | 0.4% | | 0.5% |
| **Monday, 16 July** | | | | | | |
| 6:00 | China | GDP, y-o-y | 2Q | 6.8% | 6.7% | 6.7% |
| 6:00 | China | GDP SA, q-o-q | 2Q | 1.4% | 1.6% | 1.6% |
| 6:00 | China | Retail Sales, y-o-y | Jun | 8.5% | 8.8% | 9% |
| 6:00 | China | Industrial Production, y-o-y | Jun | 6.8% | 6.5% | 6% |
| 10:30 | India | Wholesale Prices, y-o-y | Jun | 4.4% | 5.2% | 5.8% |
| 16:30 | US | Retail Sales Advance, m-o-m | Jun | 1.3% | 0.5% | 0.5% |
| 16:30 | US | Retail Sales Control Group | Jun | 0.8% | 0.4% | 0% |
| 16:30 | US | Empire Manufacturing | Jul | 25 | 21 | 22.6 |
| **Tuesday, 17 July** | | | | | | |
| 12:30 | UK | Claimant Count Rate | Jun | 2.5% | | 2.5% |
| 12:30 | UK | Jobless Claims Change | Jun | -3K | | 7.8K |
| 12:30 | UK | Average Weekly Earnings, 3M/y-o-y | May | 2.6% | 2.5% | 2.5% |
| 12:30 | UK | Weekly Earnings ex-Bonus, 3M/y-o-y | May | 2.8% | 2.7% | 2.7% |
| 12:30 | UK | ILO Unemployment Rate, 3M | May | 4.2% | 4.2% | 4.2% |
| 17:15 | US | Industrial Production, m-o-m | Jun | -0.5% | 0.5% | 0.6% |
| 17:15 | US | Capacity Utilization | Jun | 77.9% | 78.3% | 78% |
| **Wednesday, 18 July** | | | | | | |
| 12:30 | UK | CPI, m-o-m | Jun | 0.4% | 0.2% | 0% |
| 12:30 | UK | CPI, y-o-y | Jun | 2.4% | 2.6% | 2.4% |
| 12:30 | UK | CPI Core, y-o-y | Jun | 2.1% | 2.1% | 1.9% |
| 13:00 | Eurozone | CPI, y-o-y | Jun F | 2% | 2% | 2% |
| 13:00 | Eurozone | CPI, m-o-m | Jun | 0.5% | 0.1% | 0.1% |
| 16:30 | US | Housing Starts | Jun | 1337K | 1320K | 1173K |
| 16:30 | US | Building Permits | Jun | 1301K | 1330K | 1273K |
| **Thursday, 19 July** | | | | | | |
| 3:50 | Japan | Trade Balance | Jun | -¥580.5B | ¥531.2B | ¥721.4B |
| 12:30 | UK | Retail Sales, ex-Auto Fuel, m-o-m | Jun | 1.4% | 0.1% | -0.6% |
| 12:30 | UK | Retail Sales, ex-Auto Fuel, y-o-y | Jun | 4.5% | 3.7% | 3% |
| 12:30 | UK | Retail Sales, incl.-Auto Fuel, m-o-m | Jun | 1.4% | 0.2% | -0.5% |
| 12:30 | UK | Retail Sales, incl.-Auto Fuel, y-o-y | Jun | 4.1% | 3.5% | 2.9% |
| 16:30 | US | Philadelphia Fed Business Outlook | Jul | 19.9 | 21.5 | 25.7 |
| 18:00 | US | Leading Index | Jun | 0% | 0.4% | 0.5% |
| **Friday, 20 July** | | | | | | |
| 3:30 | Japan | National CPI, y-o-y | Jun | 0.7% | 0.8% | 0.7% |
| 3:30 | Japan | National CPI, ex-Fresh Food, y-o-y | Jun | 0.7% | 0.8% | 0.8% |
| 8:30 | Japan | All Industry Activity Index, m-o-m | May | 1% | 0% | 0.1% |
| 12:00 | Eurozone | ECB Current Account SA | May | 29.6B | | 22.4B |
| 12:30 | UK | PSNB ex-Banking Groups | Jun | 4.7B | 5B | 5.4B |

* UAE time
Source: Bloomberg

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