The Week Ahead: Brexit agreement vote and Indian state election results

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

Contents

UK: Brexit deal vote likely to fail, leading to uncertainty

Parliament will vote on the Brexit withdrawal agreement on 11 December, and the indications are that it will be rejected. There remains a high degree of uncertainty over what might follow with a number of possibilities including i) renegotiation of the deal, ii) a leadership challenge in the Conservative Party, iii) the UK leaving the EU without a deal, iv) a second referendum, or v) a general election. Consensus sees renegotiation of the proposed deal as the most likely option at this point. However, given the well-known divisions within the Conservative Party, there is no surety that May will be able to pass any revised deal negotiated with the EU. Thus, the level of opposition to the current bill will remain critical in determining May's next step. The GBP continues to reflect the high degree of uncertainty about what will happen after the vote.

Eurozone: ECB to announce reinvestment strategy

The ECB is expected to keep monetary policy steady at its 13 December meeting. We believe that the central bank will reiterate its guidance of i) ending its asset purchase programme by end-December; and ii) keeping interest rates unchanged "at least through the summer of 2019". We see the tone of the meeting to remain dovish, with the risks to the growth outlook shifting to the "downside" from "broadly balanced" currently. The focus will be particularly on the growth projection for 2019 which is likely to be revised down to 1.7%, from 1.8% given the soft domestic demand backdrop. Attention will also be on the reinvestment strategy, which is expected to be announced at the meeting and likely to be linked to the new capital key – the framework that governs the proportion of bonds the ECB can buy from each country. We expect the ECB to announce an open-ended time horizon to the reinvestment policy at this point, with flexibility to tweak the policy later based on evolving economic conditions.

EM: CBRT to stay on hold; India state election results

We expect the CBRT to remain on hold at its 13 December meeting, keeping the one-week repo rate at 24%. We see the deceleration in November inflation (page 5) and the strengthening of the TRY since early September as central to this decision. We believe that the CBRT will reiterate its tight monetary policy stance until there is a meaningful and sustained deceleration in inflation. In India, five state election results due on 11 December will be watched closely to gauge how likely the ruling Bharatiya Janata Party (BJP) is to win the general election in mid-2019. The elections were held in phases between November and early December, with exit polls indicating a close call in key states. On the data front, it is also an important week for the US (CPI and retail sales) India (inflation and industrial production) and China (CPI, retail sales and industrial production). Consensus estimates US CPI decelerated to 0% m-o-m in November (October: 0.3%); likely due to the drop in gasoline prices. Core CPI inflation is envisaged to remain steady at 0.2% m-o-m in November, taking the y-o-y print to 2.2%, from 2.1% in October.

I. Recent Events and Data Releases

A. MENA Economies

GCC: Opec+ agrees to cut output by 1.2 million b/d from January

Saudi Arabia to reduce oil production by c.900K b/d by January from November peak

Opec+ countries agreed to substantially cut oil production by 1.2 million b/d effective January from the October level. Opec countries are set to reduce output by 0.8 million b/d (against c.32.9 million b/d in October) while the 10 non-OPEC partners will lower production by 0.4 million b/d. These production targets will be reviewed at a meeting in April 2019, when there could be a greater indication on the outlook for Iranian exports vis-à-vis US export waivers. Opec did not release details of country-specific quotas, though the overall figure implies a cut of 3% for each member versus October production, excluding the three countries exempted from the production cuts (Iran, Libya and Venezuela). Saudi Arabia will take the lion's share of the Opec cut in absolute terms, especially considering the reduction in output outlined for this month. Oil Minister Khalid al-Falih indicated that Saudi Arabia's oil production is set to moderate from 11.1 million b/d in November to some 10.7 million b/d in December and 10.2 million b/d in January – thereby removing 900K of production from the November peak. Russia gave a commitment to reduce output by 228K b/d from the October level of 11.4 million b/d, though it said the cuts would be gradual and take place over several months due to conditions that affect oil fields during winter.

Fig. 1. Opec*: Proposed group production target in line with a 3% cut from October levels**

	Algeria	Angola	Ecuador	E. Guinea	Gabon	Iraq	Kuwait*	Nigeria	Saudi	UAE	Congo	Total**
October output, '000 b/d	1,054	1,533	525	131	186	4,653	2,764	1,751	10,630	3,160	324	26,711
Output - 3% reduction, '000 b/d	1,022	1,487	509	127	180	4,513	2,681	1,698	10,311	3,065	314	25,910
Difference, '000 b/d	(32)	(46)	(16)	(4)	(6)	(140)	(83)	(53)	(319)	(95)	(10)	(801)

* Kuwait production from September 2018
** Total production of Opec countries implementing production cuts
*** Qatar to leave Opec from January 2019. Iran, Libya and Venezuela excluded from production cuts
Source: Opec, Bloomberg, ADCB calculations

GCC - lower oil production forecast to lead to deceleration in real GDP growth in 2019 from 2018 levels

This significant reduction in output is expected to place a floor beneath the oil price and shift the global market towards balance (supply equalling demand) in 1H2019, from one of oversupply at end-2018. We see Brent crude averaging USD66.8 p/b in 2019, though see a number of upside and downside risks including global demand and US policy regarding Iranian export waivers. We continue to see US output rising further in 2019, though Canada's output should moderate. For the GCC countries, the lower oil production will be reflected in the real GDP growth forecast and we see real headline growth moderating in 2019 from 2018 levels. Meanwhile, the lower oil income (production and price) will be reflected in the nominal growth, whilst the regional fiscal and current account balances are forecast to deteriorate. We do not expect Qatar's decision to leave Opec in January 2019 to impact Opec+ cohesion or the group's overall position in the oil market. Qatar is a small oil producer within Opec and any marginal changes to output are relatively small within the group.

B. G4 Economies

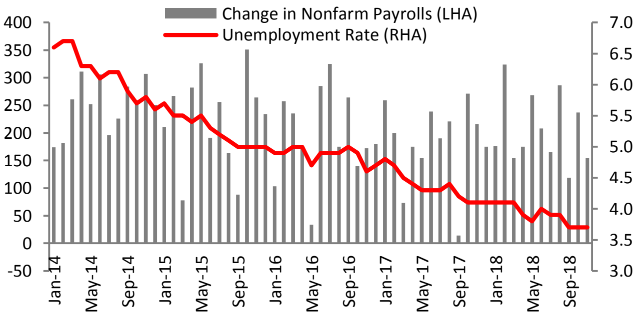
US: Decent labour report keeps December rate hike prospects intact

Healthy November labour report but below market expectations

The November employment report was weaker than expected, though still indicated a healthy labour market. The US economy added 155K jobs in November, albeit lower than the consensus expectation of 198K. The October figure was also revised down to 237K, from 250K in the first estimate. Despite the moderation, monthly job creation averaged 206K in 11M2018 vs 183K in 11M 2017. We believe that payroll growth in the range of 150K to 200K still looks impressive, though the maturing labour market and late business cycle conditions could lead to fewer jobs being created in 2019. Meanwhile, the moderation in the November jobs report was largely due to softness in construction (5K vs 24K in October), leisure and hospitality (15K vs 56K in October) and a fall in mining (-3K vs +3K in October). Less job creation in the construction sector could be due to i) unexpectedly colder weather conditions in November and ii) a slowdown in housing activity. We believe that the moderation in the hospitality sector could be due to one-off factors, though these are expected to reverse in December ahead of the Christmas holiday season. The other key sectors including manufacturing and transportation remained resilient.

Fig. 2. US: November moderation in jobs due to softness in construction and hospitality sectors

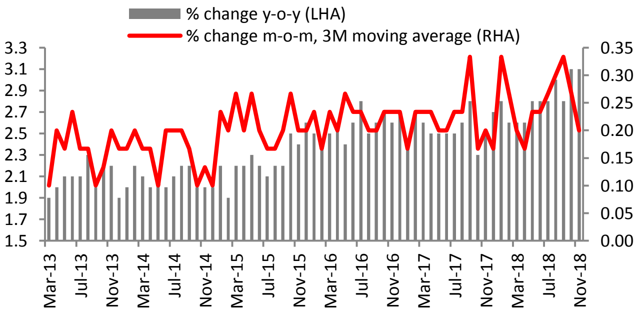
'000 (LHA); % (RHA)



Source: Bureau of Labor Statics

Fig. 3. US: Annual wage growth steady at 3.1% y-o-y in November, monthly wage growth remains soft

% change



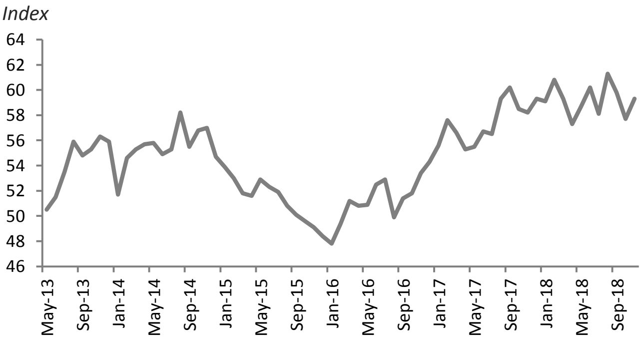
Source: Bureau of Labor Statics

We expect Fed to raise FFTR by 25bps in December, followed by two additional rate hikes in 2019

Meanwhile, the unemployment rate remained steady at a 49-year low of 3.7% in November, in line with market expectations. Monthly wage growth printed below market expectations at 0.2% m-o-m in November (consensus: 0.3%), with the October print also revised down marginally to 0.1% m-o-m. The monthly rise however kept the y-o-y print unchanged at 3.1% in November. Overall, the data suggests that the labour market continues to tighten with modest wage pressure. Indeed, we believe that the November labour report is unlikely to change the likelihood of a 25 bps rate hike in December, which is almost fully priced in (Fig. 5). Furthermore, we continue to see two additional 25 bps rate hikes in 2019 (March and June), which should bring the rate hiking cycle to an end.

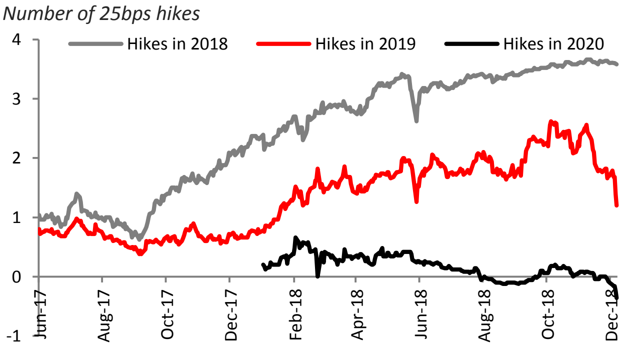
ISM manufacturing index: Manufacturing activity in November continues to suggest that economic momentum remained robust in 4Q. The ISM manufacturing index rose to 59.3 in November from 57.7 in October, which corresponds to real GDP growth of 4.9% on an annualised basis. The report highlights that 13 of the 18 industries recorded growth in November, with new orders the key driver of growth. The production and employment sub-components also remained supportive of growth in November. Meanwhile, anecdotal evidence continues to suggest that labour shortages and trade tariffs are having a greater impact on business activity. However, this was not evident in the prices sub-component of the index, which fell from 71.6 in October to 60.7 in November, the lowest level since June 2017.

Fig. 4. US: ISM manufacturing activity surprises to upside and rises to 59.3 in November from 57.7 in October



Source: Institute for Supply Management

Fig. 5. US: Market expectation of rate hikes in 2019 drops sharply in late November and early-December



Source: Bloomberg

Eurozone: 3Q GDP growth maintained at 0.2% q-o-q in final estimate

German and Italian economies contract in 3Q

The Eurozone's 3Q GDP growth rate was unrevised at 0.2% q-o-q (2Q: 0.4%) in the final estimate, though the y-o-y print was revised down to 1.6% from 1.7%. The slowdown in quarterly growth was broad-based, with all the sub-components growing at a slower pace than in 2Q. Net trade subtracted 0.3 ppt from the Eurozone's quarterly growth. Investment activity also slowed to 0.2% q-o-q in 3Q (2Q: 1.5%) likely due to a cutback in investments in Germany's automobile sector. Notably, the German economy contracted by 0.2% q-o-q in 3Q, likely due to the slowdown in the automobile sector. Recent high frequency survey indicators also point to further weakening in Eurozone growth in 4Q2018, led by softening household and government spending.

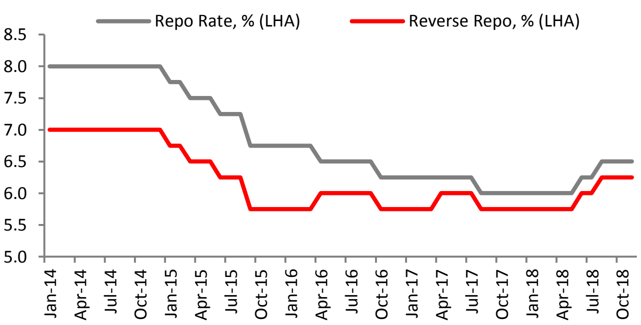
C. Emerging Market Economies

India: RBI on hold for second consecutive meeting with dovish tone

MPC votes unanimously to keep repo rate at 6.5%

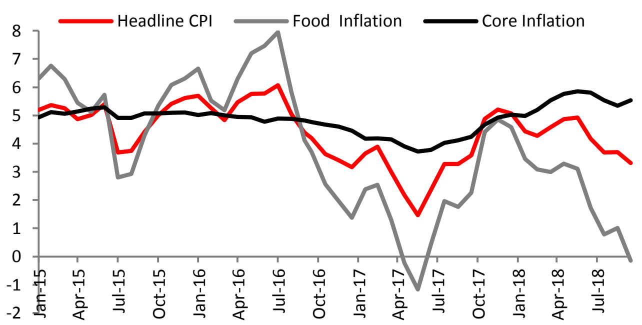
The RBI kept its repo rate unchanged at 6.5% at its December meeting, in line with our and market expectations. The monetary policy committee voted unanimously (6-0) to keep policy rates steady but was divided regarding the monetary policy stance. It voted 5-1 in favour of maintaining its "calibrated tightening" guidance, with one member voting to revert to a neutral stance. The overall tone of the meeting was dovish amid a downward revision of inflation projections. The RBI governor also highlighted that rate cuts could be back on the table if the inflation data are in line with the RBI's projections. We believe that the RBI will likely remain on hold in 1Q2019 if food inflation and oil prices stay subdued. We also envisage that the RBI will change its monetary policy stance to neutral in 1Q2019.

Fig. 6. India: RBI leaves benchmark policy rates unchanged at December meeting



Source: RBI

Fig. 7. India: Headline inflation moderating on softening food price growth; food price deflation in October



Source: India Central Statistical Organisation

Inflation forecasts revised down significantly but growth projections unchanged

The RBI revised down its inflation forecasts but kept its GDP growth estimates steady. The headline inflation projection was lowered significantly from 3.9-4.5% to 2.7-3.2% for 2H FY19 (April-March). Furthermore, the 1H FY20 inflation forecast was revised down to 3.8-4.2% from a previous estimate of 4.8%. However, the RBI emphasised that it still sees upside risks to its inflation projections stemming from oil prices and food inflation emanating from the increase in government procurement costs. Meanwhile, the RBI kept its GDP growth forecast unchanged at 7.4% for FY19, with the risks tilted to the downside.

SLR cuts proposed to tackle liquidity crunch in the economy

On the liquidity front, deputy governor Viral Acharya highlighted that the RBI will continue to inject liquidity through open market operation purchases rather than cash reserve ratio cuts. Indeed, to ease liquidity conditions, the RBI also announced that it will reduce the statutory liquidity ratio – banks' mandatory bond holding ratio – by 25 bps per quarter from January until it reaches 18% from the current 19.5%.

Turkey: CPI inflation surprises to downside in November

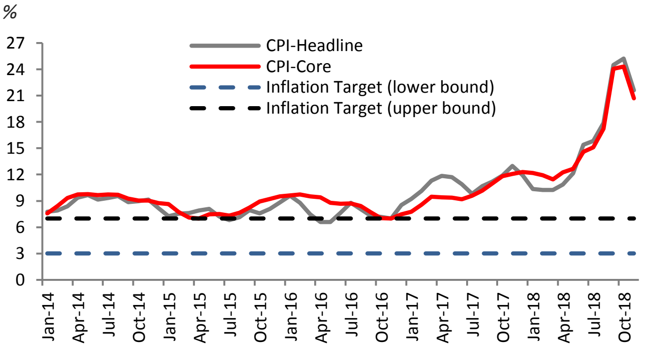
CPI inflation softens to 21.6% y-o-y in November from 25.2% in October

Headline inflation decelerated sharply to 21.6% y-o-y in November (consensus: 23%) after rising to a 15-year high of 25.2% in October. The moderation was largely led by the transportation and furnishing sub-components. We believe that the softer-than expected November inflation was mainly due to temporary tax cuts on some consumer durable goods and the government's measures to bring down food prices. Core inflation (excluding food, energy, tobacco, alcohol and gold prices) moderated to 20.7% y-o-y in November after October's 24.3%, led largely by core goods prices. Indeed, core goods inflation decelerated from 34.3% in October to 26.9% y-o-y in November, though services inflation was broadly steady at 14.7% after the previous month's 14.8%. We see the appreciation of the TRY (against the USD and EUR) from early September as a central factor for the disinflation.

We expect CBRT to remain on hold at its 13 December policy meeting

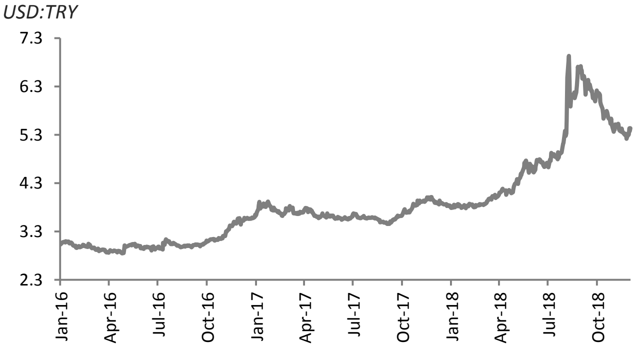
We believe that the November inflation print will prompt the CBRT to keep benchmark interest rates unchanged at its 13 December policy meeting. However, with headline inflation still above 20%, we expect the CBRT to reiterate its tight monetary policy stance while maintaining its hawkish tone. We also envisage that the central bank will retain its wait-and-see stance until there is evidence of a persistent downtrend in inflation. Nevertheless, a sharp slowdown in economic activity in 1H2019 could shift the CBRT's focus towards supporting growth from the current focus of containing inflation. Overall, we expect the growth and inflation mix to allow the CBRT to gradually tone down its tight monetary policy stance in 2019.

Fig. 8. Turkey: Headline inflation moderates in November, led by transportation and furnishing sub-segments



Source: Turkish Statistical Institute, CBRT

Fig. 9. Turkey: TRY appreciation against USD since early September providing support to inflation



Source: Bloomberg

II. Economic Calendar

Fig. 10. The week ahead

Time*	Country	Event	Period	Prior	Consensus
Expected this week					
	UAE	Dubai Economy Tracker SA	Nov	52.5	
	Bahrain	GDP Constant Prices, y-o-y	3Q	2.4%	
	Oman	CPI, y-o-y	Nov	1%	
	Qatar	CPI, y-o-y	Nov	-0.3%	
	Egypt	Urban CPI, y-o-y	Nov	17.7%	
Monday, 10 December					
3:50	Japan	GDP SA, q-o-q	3Q F	-0.3%	-0.5%
3:50	Japan	BoP Current Account Balance	Oct	¥1821.6B	¥1262.7B
11:00	Turkey	GDP, y-o-y	3Q	5.2%	2.2%
13:30	UK	Trade Balance	Oct	-£27M	-£1267M
13:30	UK	Industrial Production, y-o-y	Oct	0%	-0.1%
13:30	UK	Monthly GDP, 3M/3M Change	Oct	0.6%	0.4%
19:00	US	JOLTS Job Openings	Oct	7009	7100
Tuesday, 11 December					
3:50	Japan	Money Stock M2, y-o-y	Nov	2.7%	2.6%
11:00	Turkey	Current Account Balance	Oct	1.83B	2.5B
13:30	UK	Average Weekly Earnings, 3M/y-o-y	Oct	3%	3%
13:30	UK	Weekly Earnings, ex-Bonus, 3M/y-o-y	Oct	3.2%	3.2%
13:30	UK	ILO Unemployment Rate, 3M	Oct	4.1%	4.1%
17:30	US	PPI Final Demand, m-o-m	Nov	0.6%	0%
17:30	US	PPI Final Demand, y-o-y	Nov	2.9%	2.5%
Wednesday, 12 December					
3:50	Japan	Core Machine Orders, m-o-m	Oct	-18.3%	10.2%
16:00	India	CPI, y-o-y	Nov	3.3%	
16:00	India	Industrial Production, y-o-y	Oct	4.5%	
17:30	US	CPI, m-o-m	Nov	0.3%	0%
17:30	US	CPI, y-o-y	Nov	2.5%	2.2%
17:30	US	CPI, ex-Food and Energy, m-o-m	Nov	0.2%	0.2%
17:30	US	CPI, ex-Food and Energy, y-o-y	Nov	2.1%	2.2%
23:00	US	Monthly Budget Statement	Nov	-$100.5B	-$197B
Thursday, 13 December					
15:00	Turkey	One-Week Repo Rate	13-Dec	24%	24%
16:45	Eurozone	ECB Main Refinancing Rate	13-Dec	0%	0%
16:45	Eurozone	ECB Marginal Lending Facility	13-Dec	0.25%	0.25%
16:45	Eurozone	ECB Deposit Facility Rate	13-Dec	-0.4%	-0.4%
17:30	US	Import Price Index, m-o-m	Nov	0.5%	-1%
Friday, 14 December					
3:50	Japan	Tankan Large Manufacturing Index	4Q	19	18
3:50	Japan	Tankan Large Non-Manufacturing Index	4Q	22	21
3:50	Japan	Tankan Large All Industry Capex	4Q	13.4%	12.8%
6:00	China	Retail Sales, y-o-y	Nov	8.6%	8.8%
6:00	China	Industrial Production, y-o-y	Nov	5.9%	5.9%
12:15	Eurozone	ECB Vice-President Guindos Speaks in Frankfurt			
12:30	Eurozone	Markit Eurozone Manufacturing PMI	Dec P	51.8	51.8
17:30	US	Retail Sales Advance, m-o-m	Nov	0.8%	0.2%
17:30	US	Retail Sales, ex-Auto and Gas	Nov	0.3%	0.4%
17:30	US	Retail Sales Control Group	Nov	0.3%	0.5%
18:15	US	Industrial Production, m-o-m	Nov	0.1%	0.3%
18:45	US	Markit US Manufacturing PMI	Dec P	55.3	55.1

* UAE time
Source: Bloomberg

This report is intended for general information purposes only. It should not be construed as an offer, recommendation or solicitation to purchase or dispose of any securities or to enter in any transaction or adopt any hedging, trading or investment strategy. Neither this report nor anything contained herein shall form the basis of any contract or commitment whatsoever. Distribution of this report does not oblige Abu Dhabi Commercial Bank PJSC ("ADCB") to enter into any transaction.

The content of this report should not be considered legal, regulatory, credit, tax or accounting advice. Anyone proposing to rely on or use the information contained in the report should independently verify and check the accuracy, completeness, reliability and suitability of the information and should obtain independent and specific advice from appropriate professionals or experts regarding information contained in this report.

Information contained herein is based on various sources, including but not limited to public information, annual reports and statistical data that ADCB considers accurate and reliable. However, ADCB makes no representation or warranty as to the accuracy or completeness of any statement made in or in connection with this report and accepts no responsibility whatsoever for any loss or damage caused by any act or omission taken as a result of the information contained in this report.

Charts, graphs and related data or information provided in this report are intended to serve for illustrative purposes only. The information contained in this report is prepared as of a particular date and time and will not reflect subsequent changes in the market or changes in any other factors relevant to their determination. All statements as to future matters are not guaranteed to be accurate. ADCB expressly disclaims any obligation to update or revise any forward looking statements to reflect new information, events or circumstances after the date of this publication or to reflect the occurrence of unanticipated events.

This report is being furnished to you solely for your information and neither it nor any part of it may be used, forwarded, disclosed, distributed or delivered to anyone else. You may not copy, reproduce, display, modify or create derivative works from any data or information contained in this report.