

## The Week Ahead: US labour data and FOMC minutes in spotlight

### ► **US: Solid labour market report expected for June**

The upcoming week will be busy with a number of US releases due including the June labour market report, ISM manufacturing data and the minutes of the FOMC's 12-13 June meeting. Consensus forecasts a solid 195K jobs were created in June, albeit down from 223K in May. The unemployment rate is estimated to remain steady at 3.8%, with the jobs growth expected to be offset by a marginal increase in the labour force participation rate. Average hourly earnings growth is also forecast to have remained unchanged at 0.3% m-o-m, taking the annual reading to 2.8% y-o-y in June, from 2.7% in May. We believe that the ongoing tightening in labour market conditions and rising wages will continue to support two further rate hikes in 2018 – one in September and one in December. We envisage the June FOMC minutes (due 5 July) to reiterate the committee's hawkish post-meeting communication. For further details please see our **Economic Research Weekly: Global Data Watch 18-22 June 2018**, published on 18 June 2018. However, recent comments from the FOMC members were slightly more dovish than the June meeting communication, amidst the rising trade tensions and their likely impact on growth and the inflation outlook.

### ► **UK: BoE comments and Brexit developments in focus**

A number of BoE members have speaking engagements this week, including Governor Mark Carney, Sam Woods and Vicky Saporta. We believe that the BoE will remain hawkish on the interest rate outlook, with the members expected to outline the possibility of a 25 bps rate hike in August. However, developments related to Brexit will also remain critical for the interest rate outlook, in our view. Notably, the European Council last week expressed concern that there had been little progress on the key Brexit issues and urged the UK to submit "realistic and workable proposals". For more clarity on the UK stance on key issues, we await the government's white paper on Brexit, expected to be published in the upcoming days, following cabinet approval at the Chequers summit. Within Europe, focus will also be on rising tensions within Angela Merkel's coalition government over her immigration policy.

### ► **Global: Trade tariffs come into effect this week**

Trade tariffs proposed by both the US and China will take effect this week (6 July). In the first round, both countries will impose a 25% tariff on each other's imported goods worth USD68 billion in total. The US administration is reviewing tariffs on an additional USD16 billion worth of imported Chinese goods - an announcement is likely to be made in the coming days. Moreover, Canada announced that it will impose a retaliatory tariff on US goods worth USD12.6 billion, effective from 1 July. We expect these measures to weigh negatively on the global growth outlook, if escalated further. Meanwhile, the PBoC announced a 50 bps RRR cut for most banks last week that will come into effect on 5 July (page 5). We believe that the PBoC will further reduce the RRR in the near term to support the enterprises affected by the US protectionist measures.

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## I. Recent Events and Data Releases

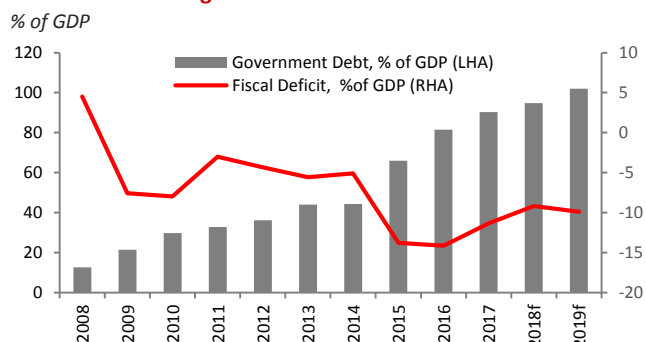
### A. MENA Economies

#### Bahrain: Economic support package from GCC countries expected soon

Bahrain is in talks with fellow GCC countries Kuwait, Saudi Arabia and the UAE regarding a reform and fiscal stability support package, according to the Saudi Press Agency. An “integrated” and “comprehensive” economic programme is expected to be announced shortly with the aim of supporting economic reforms in Bahrain and bringing the country’s fiscal position onto a sustainable path. We expect the package to include measures to directly bolster Bahrain’s short-term financial position, which in turn will also be crucial for Bahrain accessing the foreign debt capital market. These will likely include GCC deposits with the Central Bank of Bahrain alongside support for key projects in the country as well as other measures. The critical issues will be the potential medium-term reforms that Bahrain will need to implement to bring its fiscal position on to a more sustainable path. To meaningfully reduce its fiscal deficit, Bahrain will have to implement a deep fiscal adjustment programme including: i) a pullback in government expenditure; ii) subsidy reforms; and iii) deepening of the tax base (likely including the introduction of VAT). Notably, the announcement of a package would make financial support for Bahrain from the three GCC countries more explicit than the support that was previously implied, and potentially conditional. Following the announcement of the package, Bahraini Prime Minister Khalifa Bin Salman Al Khalifa established a committee to devise plans to balance the budget. So far, Bahrain has implemented relatively limited fiscal reforms.

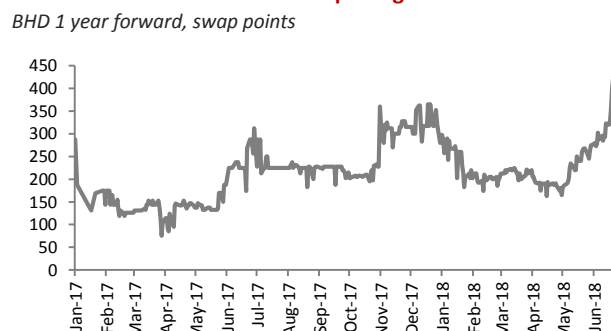
*Support package would indicate move to explicit support; reform in Bahrain critical*

**Fig. 1. Bahrain: Government debt rises to above 90% of GDP due to large recurrent fiscal deficits**



Source: Central Bank of Bahrain, IMF, ADCB estimates

**Fig. 2. Bahrain: BHD strengthens on forward market following announcement of GCC package**



Source: Bloomberg

The announcement of the package came after a substantial sell-off in Bahrain’s government debt, driven by concerns over the large external funding requirements, rising government debt levels and low FX reserve positions. Bahrain’s FX reserves at the Central Bank of Bahrain stood at USD2.1 billion in April, representing less than two months of import cover. Meanwhile, Bahrain’s government funding requirements for 2018 are estimated at c.USD5 billion. Restoring access to the international debt capital market would reduce the degree of direct support required from the GCC. In the more medium term, a credible reform programme and an improvement in the fiscal position will be important for maintaining investor interest. We expect that the package will be announced in time for Bahrain to refinance its seven-year USD750 million sukuk that matures in November 2018. The market had until recently largely shrugged off these fiscal concerns, though rising investor concerns were reflected in Bahrain abandoning

*Restoring access to debt market will reduce degree of direct GCC support required*

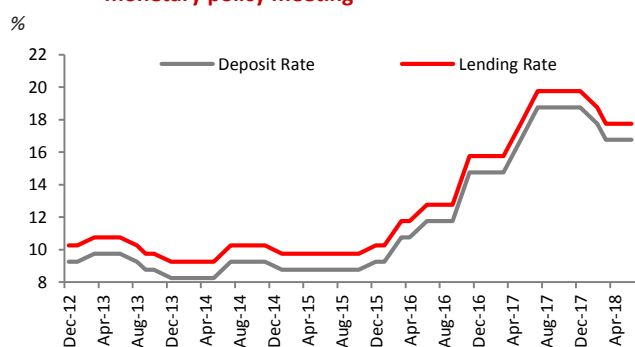
the issuance of a conventional bond in March 2018 due to insufficient demand. For further details, please see our previous research – **Economic Research Weekly: Global Data Watch 2-6 April 2018**, published on 2 April 2018. Meanwhile, the Central Bank of Bahrain continues to reiterate its commitment to the USD peg, though an increase in FX reserves is vital for raising investor confidence regarding the sustainability of the peg. CDS spreads and the downwards pressure on the BHD moderated substantially following the announcement of the package.

### Egypt: CBE keeps monetary policy steady at its June meeting

The CBE kept interest rates on hold at its 28 June meeting, as widely expected by consensus and ourselves. The benchmark deposit rate remained at 16.75% and the lending rate at 17.75%. This was the second consecutive meeting that rates were kept steady, following a cumulative 200 bps of rate cuts at the January and February meetings. In line with expectations, the central bank highlighted both domestic and external factors that could push up inflation in the near term. The CBE noted in its post-meeting statement that "fiscal consolidation measures are expected to lead to one-off increases in the price level, which translate into temporary higher inflation rates". On the international front, the tightening in financial conditions and higher oil prices were reiterated, as at the May meeting. We maintain our expectation that the CBE will remain on hold for the next few meetings (August and September) whilst it assesses the impact of the recently announced subsidy reforms on inflation, alongside factors such as global sentiment and portfolio flows to emerging markets, especially as the Fed continues to raise rates. However, we expect the CBE to resume its rate-cutting cycle in 4Q2018. Indeed, the bank highlighted in its statement that "single digit inflation is expected to be reached after the temporary effect of supply shocks dissipates".

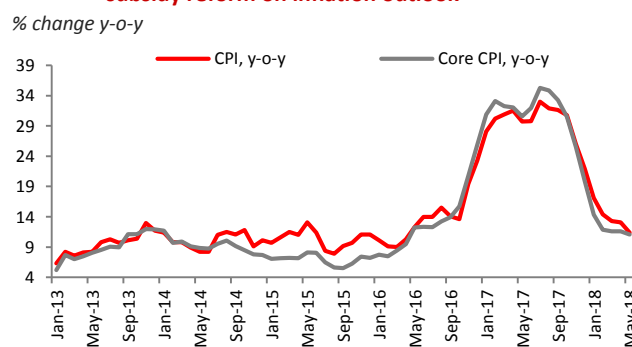
*CBE highlights both domestic and international drivers of upside risk to inflation*

**Fig. 3. Egypt: CBE keeps rates on hold for second consecutive monetary policy meeting**



Source: Central Bank of Egypt

**Fig. 4. Egypt: CBE looks to gauge impact of latest round of subsidy reform on inflation outlook**



Source: CAPMAS, ADCB calculations

**IMF disbursement:** The IMF approved a fourth payment to Egypt as a part of an economic reform programme. The disbursement will be USD2.02 billion, bringing the total received by Egypt so far from the IMF to c.USD8 billion. The total size of the package is USD12 billion.

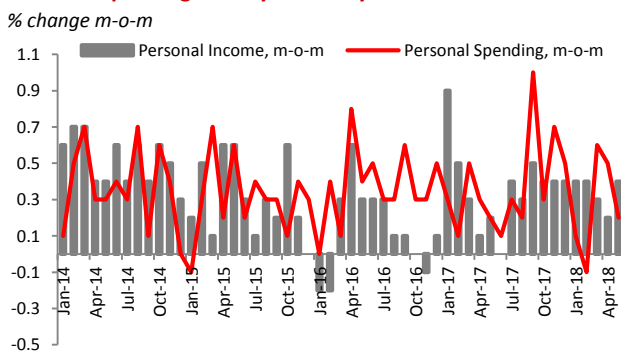
## B. G4 Economies

### US: Core PCE inflation hits Fed's 2% target in May

Incoming data continues to suggest solid 2Q GDP growth, with annualised growth of around 3%, despite a weakening in May consumer spending. Personal income growth accelerated to 0.4% m-o-m in May, from 0.2% in April, reflecting the increased pay received by employees on the back of tax reforms. The moderation in consumer spending growth in May was partly due to decreased spending on household utilities, including electricity and gas. We expect electricity consumption to bounce back in June due to warm weather conditions likely boosting demand for air conditioner usage. However, the outlook for 3Q remains uncertain at this point, with trade tensions expected to weigh negatively on the growth outlook. Meanwhile, core PCE inflation accelerated to 2% y-o-y in May, from 1.8% in April, beating the consensus estimate of 1.9%. This is the first time since April 2012 core PCE inflation has touched the Fed's 2% inflation target. The rise in core PCE inflation was led by core goods prices and health care costs. Headline PCE inflation also strengthened to 2.3% y-o-y in May (April: 2%; consensus: 2.2%), driven by energy prices. We believe that higher energy prices will continue to put upward pressure on headline PCE inflation. However, on a monthly basis, both core PCE inflation and PCE deflator remained steady at 0.2% m-o-m, in line with expectations.

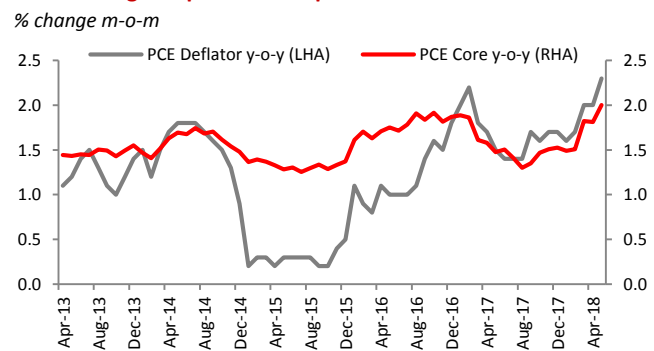
*Strong gains in personal income in May*

**Fig. 5. US: Personal income growth accelerates in May but spending activity relatively soft**



Source: Bureau of Economic Analysis

**Fig. 6. US: Core PCE inflation accelerates to 2% in May, the highest point since April 2012**



Source: Bureau of Economic Analysis

**US durable goods:** The durable goods report for May was mixed. Headline durable goods orders came in at -0.6% m-o-m in May – better than the consensus expectation of a 1% fall. The contraction in the headline figure was due to a 7% decline in volatile aircraft orders. The underlying data including core capital goods orders and capital goods shipments (which feeds into GDP data) contracted in May. However, on the positive side, weaker-than-expected core capital goods orders and shipments were partly offset by strong upwards revisions to the April figures.

*US durable goods data presents mixed picture in May*

**1Q2018 GDP:** US real GDP growth was revised down to 2% q-o-q SAAR in 1Q2018 in its third estimate, from 2.2% in the previous estimate. Consensus was expecting no revisions to the GDP print. The slowdown was mainly due to moderation in personal consumption to 0.9% q-o-q, from 1% earlier. Trade and inventories were also revised down. On the positive side, there were some upward revisions to government spending and fixed investment categories.

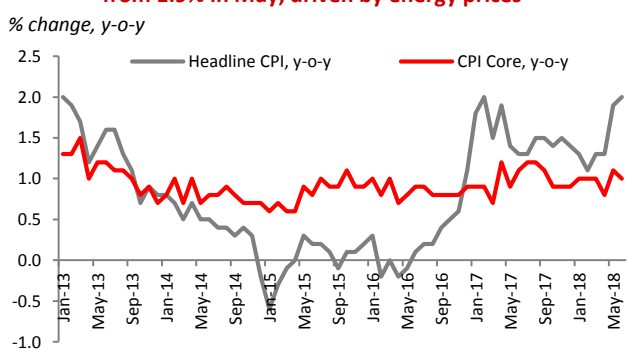
*1Q2018 GDP growth revised down to 2%, from 2.2% in second estimate*

## Eurozone: Headline inflation rises but core inflation remains subdued

Headline inflation rose to 2% y-o-y in June (May: 1.9%), in line with market expectations. The pick-up in headline inflation was driven mainly by energy prices, which strengthened to 8% y-o-y in June, from 6.1% in May. However, core inflation remained subdued and moderated to 1% y-o-y in June from 1.1% May, due to weak services inflation. This suggests that core inflation still lacks a convincing upward trend. However, non-energy industrial goods inflation strengthened to 0.4% y-o-y in June (April: 0.3%), likely reflecting the recent EUR depreciation. Given the recent moderation in domestic demand alongside the moderately less accommodative monetary policy, we see core inflation remaining weak in 2H2018. With the ECB already announcing an end to its QE programme by end-2018, we believe that the ECB will likely to stick to its normalisation plan even if core inflation undershoots in the near-term.

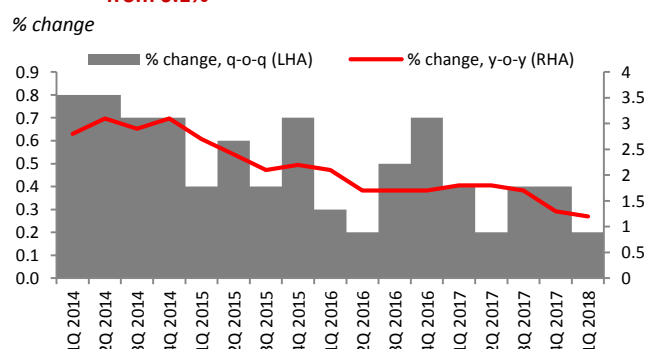
*Core inflation remains subdued in June despite headline inflation rising to ECB's 2% target*

**Fig. 7. Eurozone: Headline inflation accelerates to 2% in June, from 1.9% in May, driven by energy prices**



Source: Eurostat

**Fig. 8. UK: 1Q2018 GDP growth revised up to 0.2% q-o-q, from 0.1%**



Source: Office for National Statistics

## UK: 1Q GDP growth revised up to 0.2% q-o-q in final estimate

1Q2018 GDP growth was revised up to 0.2% q-o-q, higher than both the consensus expectation and second estimate of 0.1% growth. The upward revision was mainly due to stronger construction activity. Despite the upward revision, investment and consumption activity remained relatively weak. We believe that the upward revision in 1Q GDP data will further strengthen the BoE's argument that the 1Q slowdown was due to temporary factors. Thus, we see an increasing chance of a 25bps rate hike at its August meeting.

*1Q2018 GDP growth revised up to 0.2% q-o-q, from 0.1% in previous estimate*

## C. Emerging Market Economies

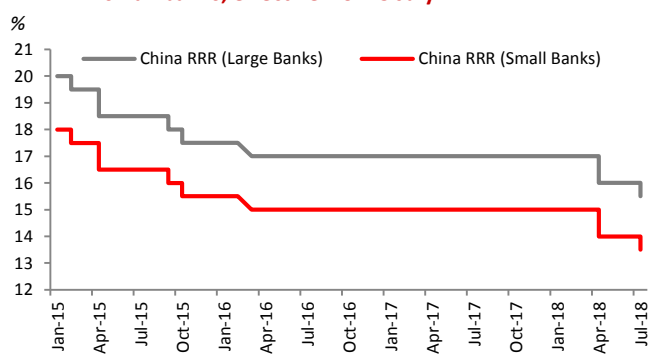
### China: PBoC cuts RRR to support debt-to-equity swap and SME loans

The PBoC announced a 50 bps Reserve Requirement Ratio (RRR) cut for most banks (state-run commercial banks, joint-stock commercial lenders, postal banks, city commercial lenders, rural banks and foreign banks) effective from 5 July. After the cut, the RRR will be 15.5% for large banks and 13.5% for small ones. The PBoC statement highlighted that this reduction will release about CNY700 billion of liquidity into the system. The freed-up reserves will be channelled to promote: i) a debt-to-equity swap programme to reduce the debt burden of large companies; and ii) increased funding support for small firms. According to the PBoC's calculations, CNY500 billion of reserves

*PBoC cuts RRR by 50 bps for most banks, effective from 5 July*

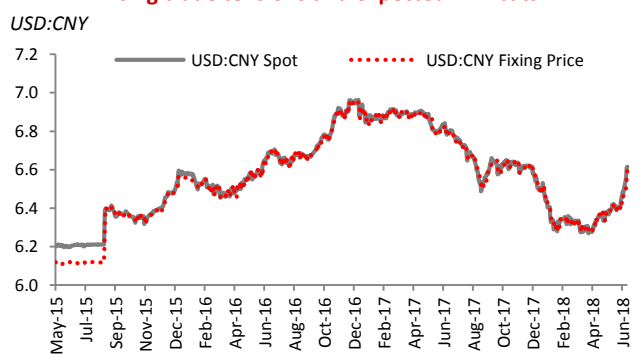
will be freed up for the five biggest state-run banks and 12 joint-stock commercial lenders, which should be used to support debt-to-equity swaps in a market-oriented manner. We believe that the key beneficiaries of this swap programme will be large companies, including state-owned enterprises. Moreover, the PBoC continued to provide support for SME funding and freed up CNY200 billion of reserves for small lenders (postal banks and city commercial lenders).

**Fig. 9. China: PBoC cuts RRR by 50 bps for both large and small banks, effective from 5 July**



Source: PBoC

**Fig. 10. China: CNY remains under pressure against USD due to rising trade tensions and expected RRR cuts**



Source: Bloomberg

We believe that the PBoC's decision to link the RRR cuts to debt-to-equity swaps has broadened the scope of the targeted RRR reductions. We expect the PBoC to use RRR cuts as one of its tools to further tighten financial regulations and limit leveraging. Thus, we see an increasing chance of additional RRR cuts in 2H2018, though the magnitude of the cuts is likely to vary according to the intended purpose. The CNY has depreciated against the USD over the last two weeks, likely due to the possibility of additional RRR cuts and increasing trade tensions with the US.

*We expect PBoC to make additional RRR cuts in 2H2018*

## Turkey: Erdogan wins presidential election

Recep Tayyip Erdogan won the Turkish presidential election with an absolute majority of 52.6% of the votes in the first round, according to the unofficial results published by the state-run Anadolu News Agency. Erdogan's Cumhur Alliance (AKP-MHP) also gained a parliamentary majority with 53.6% of the votes. The Cumhur Alliance won 343 of the 600 parliamentary seats, though this is still short of the 360 seats needed to make changes to the constitution through a referendum process. The win will allow Erdogan to start a new five-year term as president with additional powers granted under the new constitutional rules. The absolute majority for Erdogan and the parliamentary majority in the first round were positive surprises given that opinion polls were indicating that the presidential election would require a second round of voting and that the Cumhur Alliance would likely fall short of a parliamentary majority. However, President Erdogan's AK Party failed to gain a simple majority (>300) independently and won 293 of the 600 seats. The Supreme Election Board (YSK), the official election board, said that the final election results would be announced on 5 July. Parliament will convene on 8 July with new lawmakers taking their oath on the first day.

*Erdogan wins presidential election for another five-year term*

The market's attention will now be on the appointment of cabinet ministers, the government's fiscal consolidation plans and its commitment to keeping the central bank independent. We believe that the government's priority will be restoring investor

*Fiscal consolidation and central bank independence remain key to regaining investor confidence*

confidence with clear medium-term policy guidance to unwind the pre-election expansionary fiscal policies. Moreover, the central bank's independence and the ongoing tight monetary policy stance will remain critical for controlling Turkey's double-digit headline inflation.

## II. Economic Calendar

Fig. 11. The week ahead

Time *	Country	Event	Period	Prior	Consensus
<b>Expected this week</b>					
	UAE	UAE PMI	Jun	56.5	
	UAE	Dubai Airport Cargo Volume, y-o-y	May	-0.7%	
	Saudi Arabia	Unemployment Rate (Saudis)	1Q	12.8%	
	Saudi Arabia	Saudi Arabia PMI	Jun	53.2	
	Saudi Arabia	Non-Oil Exports, y-o-y	Apr	3.6%	
	Qatar	GDP Constant Prices, y-o-y	1Q	1.8%	
	Bahrain	GDP Constant Prices, y-o-y	1Q	3.4%	
<b>Monday, 2 Jul</b>					
3:50	Japan	Tankan Large Manufacturing Index	2Q	24	22
3:50	Japan	Tankan Large Manufacturing Outlook	2Q	20	20
5:45	China	Caixin China PMI Manufacturing	Jun	51.1	51.1
9:00	India	Nikkei India PMI Manufacturing	Jun	51.2	--
12:00	Eurozone	Markit Eurozone Manufacturing PMI	Jun F	55	55
12:30	UK	Markit UK PMI Manufacturing SA	Jun	54.4	54
13:00	Eurozone	Unemployment Rate	May	8.5%	8.5%
17:45	US	Markit US Manufacturing PMI	Jun F	54.6	54.7
18:00	US	ISM Manufacturing	Jun	58.7	58.5
18:00	US	ISM Prices Paid	Jun	79.5	74.8
<b>Tuesday, 3 Jul</b>					
3:50	Japan	Monetary Base, y-o-y	Jun	8.1%	
11:00	Turkey	CPI, y-o-y	Jun	12.2%	13.9%
13:00	Eurozone	Retail Sales, m-o-m	May	0.1%	0.1%
18:00	US	Factory Orders	May	-0.8%	0%
18:00	US	Durable Goods Orders	May F	-0.6%	-0.5%
18:00	US	Capital Goods Shipments, Non-def, ex-air	May F	-0.1%	
20:00	Eurozone	ECB Executive Board Member Praet Speaks in Bucharest			
<b>Wednesday, 4 July</b>					
4:30	Japan	Nikkei Japan PMI Composite	Jun	51.7	
12:05	UK	BOE's Woods Speaks in London			
14:55	UK	BOE's Saporta Speaks in London			
15:00	US	MBA Mortgage Applications	29-Jun	-4.9%	
<b>Thursday, 5 Jul</b>					
10:00	Germany	Factory Orders, m-o-m	May	-2.5%	1.1%
14:00	UK	BOE Governor Carney Speaks in Newcastle			
14:30	Eurozone	ECB's Mersch, Nowotny at Austrian Central Bank Conference			
16:15	US	ADP Employment Change	Jun	178K	190K
18:00	US	ISM Non-Manufacturing Composite	Jun	58.6	58.2
21:30	Eurozone	Bundesbank President Jens Weidmann Speaks in Linz, Austria			
22:00	US	FOMC Meeting Minutes	13-Jun		
<b>Friday, 6 Jul</b>					
10:00	Germany	Industrial Production SA, m-o-m	May	-1.0%	0.3%
11:00	Eurozone	ECB's Nouy, EU's Dombrovskis at Austrian C.Bank Conference			
12:30	UK	Unit Labor Costs, y-o-y	1Q	2.1%	
16:30	US	Change in Nonfarm Payrolls	Jun	223K	195K
16:30	US	Unemployment Rate	Jun	3.8%	3.8%
16:30	US	Average Hourly Earnings, m-o-m	Jun	0.3%	0.3%
16:30	US	Average Hourly Earnings, y-o-y	Jun	2.7%	2.8%
16:30	US	Trade Balance	May	-\$46.2B	-\$43.6B

\* UAE time

Source: Bloomberg



Fig. 12. Last week's data

Time*	Country	Event	Period	Prior	Consensus	Actual
<b>MENA Economies</b>						
	UAE	M2 Money Supply, m-o-m	May	1.5%	--	-0.7%
	Saudi Arabia	CPI, y-o-y	May	2.5%	--	2.3%
	Oman	Budget Balance Month	Apr	-140.7M	--	-56.9M
	Egypt	GDP Constant, y-o-y	1Q	4.1%	--	2.5%
<b>Monday, 25 Jun</b>						
12:00	Germany	IFO Business Climate	Jun	102.3	101.8	102.3
12:00	Germany	IFO Expectations	Jun	98.6	98	98.6
12:00	Germany	IFO Current Assessment	Jun	106.1	105.6	106.1
18:00	US	New Home Sales	May	646K	667K	689K
18:00	US	New Home Sales, m-o-m	May	-3.7%	0.8%	6.7%
18:30	US	Dallas Fed Manf. Activity	Jun	26.8	24.9	36.5
<b>Tuesday, 26 Jun</b>						
18:00	US	Richmond Fed Manufact. Index	Jun	16	15	20
18:00	US	Conf. Board Consumer Confidence	Jun	128.8	128	126.4
18:00	US	Conf. Board Present Situation	Jun	161.2	--	161.1
<b>Wednesday, 27 Jun</b>						
12:00	Eurozone	M3 Money Supply, y-o-y	May	3.8%	3.8%	4%
16:30	US	Wholesale Inventories, m-o-m	May P	0.1%	0.2%	0.5%
16:30	US	Durable Goods Orders	May P	-1%	-1%	-0.6%
16:30	US	Durables, ex-Transportation	May P	1.9%	0.5%	-0.3%
16:30	US	Cap Goods Orders, Nondef ex-Air	May P	2%	0.5%	-0.2%
16:30	US	Cap Goods Ship, Nondef ex-Air	May P	1%	0.3%	-0.1%
18:00	US	Pending Home Sales, m-o-m	May	-1.3%	0.5%	-0.5%
18:00	US	Pending Home Sales NSA, y-o-y	May	0.3%	--	-2.8%
<b>Thursday, 28 Jun</b>						
3:50	Japan	Retail Sales, m-o-m	May P	1.3%	-0.9%	-1.7%
3:50	Japan	Retail Trade, y-o-y	May	1.6%	1.4%	0.6%
13:00	Eurozone	Consumer Confidence	Jun F	-0.5%	-0.5%	-0.5%
16:30	US	GDP Annualized, q-o-q	1Q T	2.2%	2.2%	2%
16:30	US	Personal Consumption	1Q T	1%	1%	0.9%
16:30	US	GDP Price Index	1Q T	1.9%	1.9%	2.2%
16:30	US	Core PCE, q-o-q	1Q T	2.3%	--	2.3%
	Egypt	Lending Rate	28-Jun	17.75%	17.75%	17.75%
	Egypt	Deposit Rate	28-Jun	16.75%	16.75%	16.75%
<b>Friday, 29 Jun</b>						
3:50	Japan	Industrial Production, m-o-m	May P	0.5%	-1%	-0.2%
3:50	Japan	Industrial Production, y-o-y	May P	2.6%	3.4%	4.2%
12:30	UK	Mortgage Approvals	May	62.9K	62.3K	64.5K
12:30	UK	GDP, q-o-q	1Q F	0.1%	0.1%	0.2%
12:30	UK	GDP, y-o-y	1Q F	1.2%	1.2%	1.2%
13:00	Eurozone	CPI Core, y-o-y	Jun A	1.1%	1%	1%
13:00	Eurozone	CPI Estimate, y-o-y	Jun	1.9%	2%	2%
16:30	US	Personal Income	May	0.2%	0.4%	0.4%
16:30	US	Personal Spending	May	0.5%	0.4%	0.2%
16:30	US	PCE Deflator, m-o-m	May	0.2%	0.2%	0.2%
16:30	US	PCE Deflator, y-o-y	May	2.0%	2.2%	2.3%
16:30	US	PCE Core, m-o-m	May	0.2%	0.2%	0.2%
17:45	US	Chicago Purchasing Manager	Jun	62.7	60	64.1
18:00	US	U. of Mich. Sentiment	Jun F	99.3	99	98.2

\* UAE time

Source: Bloomberg

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