Fed goes in March; EU numbers firm up; Oman issues USD 5 billion in bonds

Key market indicators

Stock markets	Index	Change (%) weekly	Change (%) YTD
Regional			
Abu Dhabi SM	4,596	-1.22	1.10
Bahrain ASI	1,342	-0.58	9.92
Dubai FM	3,584	-1.38	1.49
Egypt EGX 30	12,310	0.57	-0.28
KSA Tadawul	7,017	-0.42	-2.69
Kuwait SE	6,767	-0.63	17.73
Muscat SM 30	5,815	-0.59	1.23
Qatar Exchange	10,721	-1.87	2.72
MSCI GCC	479	-1.00	0.80
International			
DAX	12,027	1.89	4.76
DJIA	21,006	0.88	6.29
FTSE 100	7,374	1.80	3.24
Nikkei	19,469	0.96	1.86
S&P 500	2,383	0.67	6.44

Commodities	$/bbl	Change (%) weekly	Change (%) YTD
Brent crude ($/bbl)	55.9	-0.68	-1.62
KEC ($/bbl)	54.1	0.17	4.20
WTI ($/bbl)	53.3	-1.61	-0.73
Gold ($/t oz.)	1234.1	-1.72	6.72

Exchange rates	Rate	Change (%) weekly	Change (%) YTD
KWD per USD	0.306	0.08	0.07
KWD per EUR	0.324	0.37	1.79
USD per EUR	1.062	0.49	1.02
JPY per USD	113.99	1.66	-2.46

Interbank rates	%	Change (bps) weekly	Change (bps) YTD
Kibor – 3 month	1.44	0.0	0.0
Qibor – 3 month	1.88	0.0	9.4
Libor – 3 month	1.10	0.0	10.4

Bond yields	%	Change (bps) weekly	Change (bps) YTD
Regional			
Abu Dhabi 2021	2.42	14.2	-12.4
Dubai 2021	3.14	2.2	-18.3
Qatar 2021	2.69	13.2	-26.0
Saudi Arabia 2021	2.93	25.5	-12.1
International			
UST 10 year	2.48	16.5	5.0
Bunds 10 year	0.36	17.0	14.9
Gilts 10 year	1.18	10.5	-5.6
JGB 10 year	0.08	1.6	2.8

Source: Thomson Reuters Datastream

> Economic Research Department
+965 2259 5500
econ@nbk.com

Summary

The US dominated the news. US equity markets keep grinding higher and breaking record highs, supporting along the way many of their counterparts, including in Europe and the GCC. The background is twofold: solid economic data in the US and in the EU, and the advent of the Trump administration. Away from the hoopla in the non-financial media and the circus atmosphere in some cases, price action and financial commentary strongly suggest that the US markets assess the Trump election to be a seismic game changer, on the positive side. The concerns are certainly there, especially when it comes to international trade. Nonetheless, for now, the markets and the administration are primarily focused on the clear pluses of the Trump administration: tax reform and deregulation.

On many parts of the new administration's policy, details are lacking, which is normal at this early stage, but as we go forward the markets will come to demand more clarity. In his first formal address to Congress on 28 February, Mr. Trump gave some broad policy lines, but the fiscal details (taxes, spending) remain to be filled later. The Republicans and Mr. Trump are planning to tackle healthcare/Obamacare reform first, which may take some time. Treasury Secretary Mnuchin had earlier mentioned that the new tax legislation may see the light by August 2017. The upcoming business-friendly legislation is expected to include a tax cut for businesses and the middle class, along with tax simplification, though a border adjustment tax (BAT) and the law's deficit implications may prove quite tricky and may temper enthusiasm. The speech was well received politically and by the markets, where equities soared the following day—the Dow Jones Industrials broke 21,000 for the first time ever.

In light of all that and the positive economic data, the Fed has been making more hawkish noises, upping the ante for a 15 March interest rate hike. While we were in the June-hike camp, we now think that the Fed will go in March; there is little reason to wait longer with the data that we, and the Fed, possess. The markets also appear ready now for a rate hike. We believe that, barring any surprises, the 10 March US employment (and wages) report will seal the fate of that move. The FOMC meets 14-15 March. We would still expect 2 rate hikes this year, though the risk of 3 hikes is rising. These developments helped the USD, while European interest rates were kept in check only by political worries in the EU (Dutch and French elections).

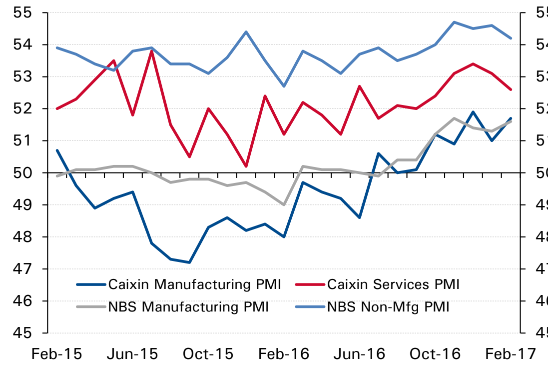
February PMIs pointed to improved growth in Saudi, the UAE and Egypt. Oman successfully issued international bonds.

International macroeconomics

USA: Mr. Trump's speech was well received by both the political establishment and the markets. The Dow industrials broke 21,000 the next day, for the first time ever. The speech (see Summary above) provided broad lines but many details remain to be filled, especially on taxes and spending. The optimism and stellar performance of the equity markets should make it easier for the Fed to raise rates; this week's employment (and wages) report for February, due on Friday 10 March, should seal the

Chart 1: China PMI (Caixin & NBS)

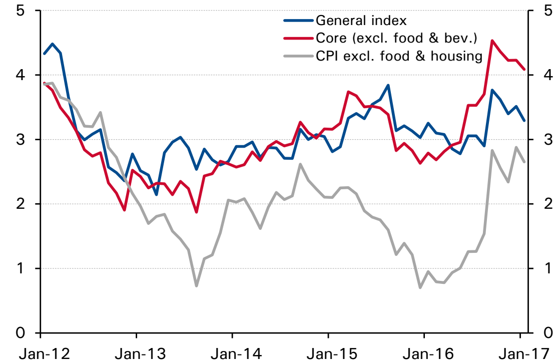
(index)



Source: Thomson Reuters Datastream

Chart 2: Kuwait consumer price inflation

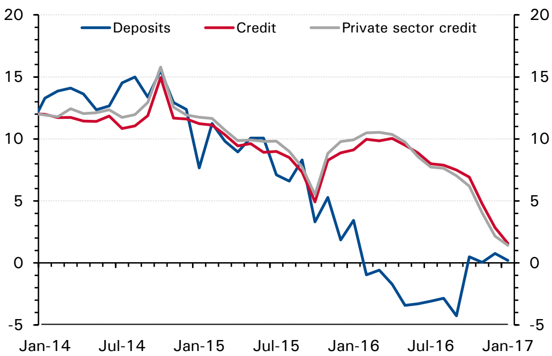
(% y/y)



Source: Central Statistical Bureau, NBK estimates

Chart 3: Saudi deposit and credit growth:

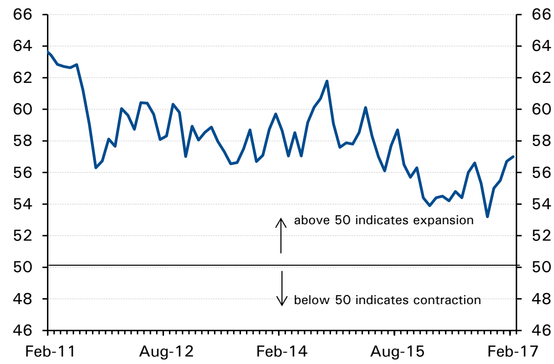
(% y/y)



Source: SAMA

Chart 4: Saudi PMI

(index)



Source: Emirates NBD/Markit

fate of that March rate hike. In fact, unemployment claims hit their lowest level since 1973!

Data continued strong or firm and Fed officials ratcheted up the likelihood of a 15 March hike by the FOMC. Q42016 GDP was unrevised at 1.9% (both q/q annualized and y/y), leaving the year at 1.6%. The indications are for 2.0% or higher in 2017. The manufacturing PMI was 57.7 in February, the highest in 2.5 years. Inflation, which saw the CPI at 2.5% y/y in February, also saw the January data for the PCE deflator firm up as well. The PCE deflator for the previous month of January was at 1.9% y/y; while the core deflator was at 1.7% y/y. The Fed's target for the latter is 2.0%.

Eurozone: Eurozone manufacturing PMI was revised slightly lower to 55.4 for February, though this is still the strongest reading in six years. The services PMI was a steady 55.5. Spain's index disappointed, coming in at 54.8 (expected at 56). Meanwhile, Germany's PMI, despite being revised lower, still registered a 69-month high of 56.8.

The Eurozone CPI inflation registered 2.0% y/y in February, the highest in 4 years which was further confirmation of firm economic conditions on the continent.

Greece resumed talks this week, with its government seemingly willing to accept more austerity measures. The government agreed to pre-legislate economic reforms that would take effect in 2019.

UK: Britain's upper house of parliament, the House of Lords, voted overwhelmingly to amend the recently passed Article 50 bill in order to protect the rights of EU citizens already resident in the UK after Brexit. The amendment is a blow to PM Theresa May's government, which had argued that Britain needed to see simultaneous reciprocal guarantees by EU members over the status of British citizens living in Europe. The unelected House of Lords found the argument unpersuasive, however, and has therefore sent the bill back to the House of Commons for further debate. Despite approving the bill the first time without amendments, opposition Labor MPs have now said that they will back the Lords' amendment. This could possibly delay the triggering of Article 50 this month.

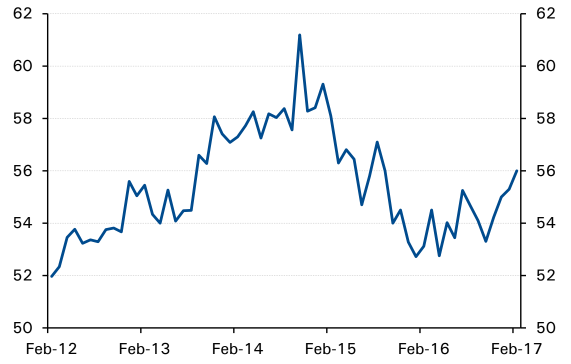
China: Beating expectations, China's manufacturing sector continues to expand, as shown by the Caixin PMI survey results for February. The Caixin index rose to 51.7 from 51.0 in January. (Chart 1.) The Caixin PMI differs from the official manufacturing PMI in that it monitors small to medium-sized firms in China rather than large, state-owned enterprises. The official manufacturing PMI was in line with Caixin at 51.6 in February, extending the index's period of expansionary activity to seven consecutive months. The Caixin services index in February, though in solid expansionary territory at 52.6, was the lowest in four months. Official numbers represented a similar easing trend.

GCC & regional macroeconomics

Kuwait: Inflation in consumer prices (CPI) steadied at 3.3% year-on-year (y/y) in January, as inflation across most components remained stable or unchanged. (Chart 2.) Looking at the two major components: inflation in housing costs was unchanged, while food inflation maintained its weakness as global food inflation remained soft. Core inflation, which excludes food prices, also held steady at 4.1% y/y after surging following the fuel price hike at the start of September 2016.

The government approved increases in electricity and water tariffs that

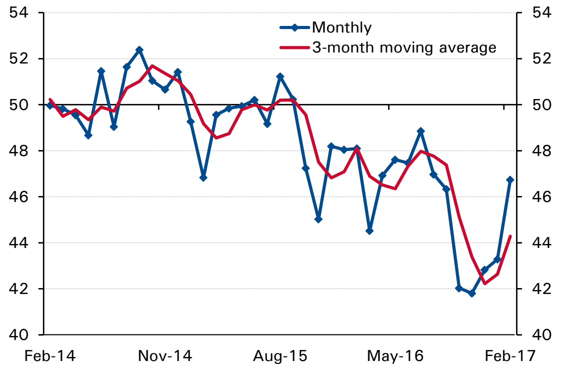
Chart 5: UAE PMI



Source: Markit/Emirates NBD

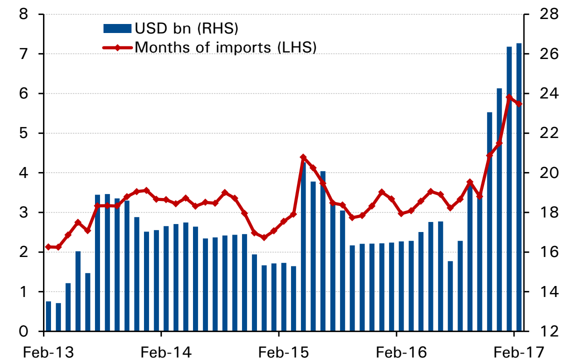
Chart 6: Egypt PMI

(index)



Source: Markit

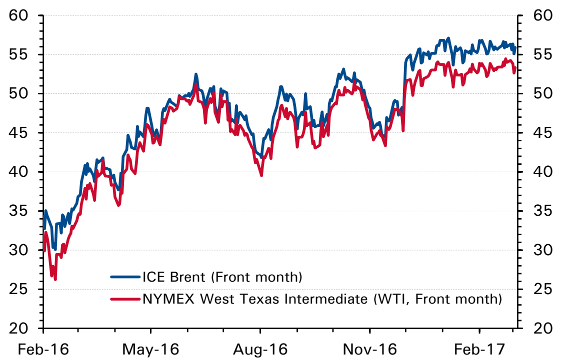
Chart 7: Egypt official reserves



Source: CBE, Thomson Reuters Datastream, NBK estimates

Chart 8: Crude oil prices

($/bbl)



Source: Thomson Reuters Datastream

were significantly lower than those mandated in law 20/2016 that was passed in May 2016. Electricity rates for the investment and commercial sectors will increase to 5 fils per kilowatt-hour (kWh) and for the industrial and agricultural sectors to 3 fils from the current 2 fils. The water tariff will rise to KD 2 per 1000 imperial gallons for all sectors from the current KD 0.8. We estimate that the revenue increase from the new utility prices will be around 0.5% of GDP. The new utility prices will be less disruptive than those initially approved in last year's legislation.

Saudi Arabia: Lending and deposit conditions in the Saudi banking sector continue to weaken despite the improvement in oil prices and overall business sentiment. Total and private sector credit growth slowed in January to 1.6% y/y and 1.4% y/y, respectively. (Chart 3.) This is the slowest rate of growth since 2010 when the economy was just emerging from the global financial crisis. The lackluster expansion in credit is a particular worry given the authorities' hopes of stimulating the non-oil economy. Deposits, meanwhile, barely increased on a y/y basis, rising by 0.2%; deposits actually contracted on a m/m basis for the second month in a row in January, by -1.0%.

However, according to the latest survey of Saudi purchasing managers, the softness in borrowing does not seem to have filtered through into consumer activity. February's headline PMI of 57.0 was the fourth consecutive reading to show improvement in business conditions. (Chart 4.) Indeed, conditions improved at the fastest rate since August 2015, helped by sharp rises in output and new orders. The rate of expansion in new orders increased to an 18-month high in February.

UAE: The UAE's headline PMI climbed to a strong and over one-year high of 56.0 in February as both new export orders and new orders remained solid and as output trekked even higher, thanks to ongoing improvements in both domestic and external demand. (Chart 5.)

Qatar: Qatar's Ministry of Energy and Industry announced that fuel prices will increase this March, in line with the government's efforts to reduce subsidies and consolidate spending. This is the fifth consecutive monthly hike in gasoline prices and the third consecutive hike in diesel prices. Qatar began reducing fuel subsidies in May of 2016.

Oman: Oman eased its fiscal and debt need situation by the successful sale of $5 billion of international bonds, which almost covered its entire international borrowing plan for the year. Moody's provisionally rated the bond as investment grade (Baa1) despite the negative outlook it holds (see fixed income section below).

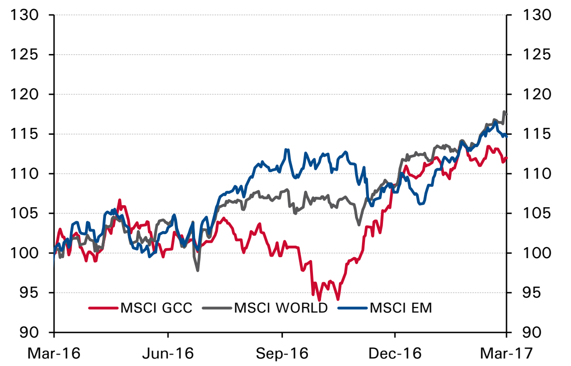
Egypt: The February PMI rose over 3 points to 46.7, its best reading in six months, as economic activity appeared to be seeing the first signs of recovery following the November 2016 currency float. (Chart 6.) Despite the improvement, activity remains subdued with the February PMI figure consistent with economic growth of around 2%. Price pressures also appeared to diminish noticeably following record highs in recent months.

The Central Bank of Egypt's foreign reserves were mostly steady in February, rising slightly to $26.5 billion by the end of the month or an estimated 5.7 months of import cover. (Chart 7.) Reserves have risen noticeably since Egypt floated its currency in November 2016, and the IMF agreed to lend the country $12 billion in conjunction with an ambitious economic reform program.

The finance minister will propose re-introducing a stamp duty on stock

Chart 9: Global stock markets

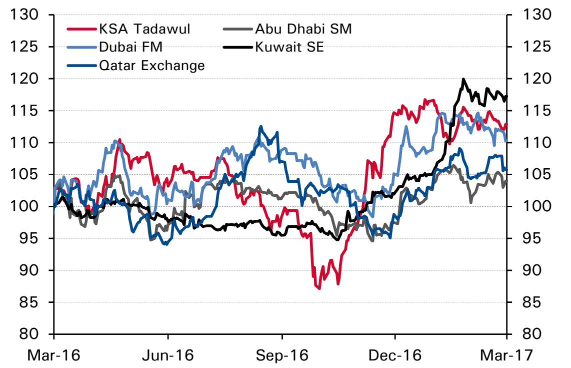
(rebased, 3 Mar 2016=100, total return)



Source: Thomson Reuters Datastream

Chart 10: GCC stock markets

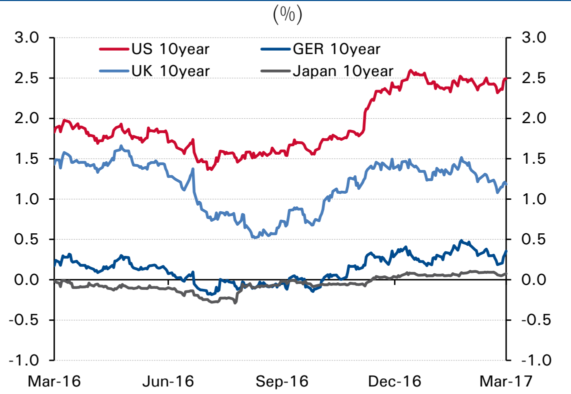
(rebased, 3 Mar 2016=100))



Source: Thomson Reuters Datastream

Chart 11: Global bond yields

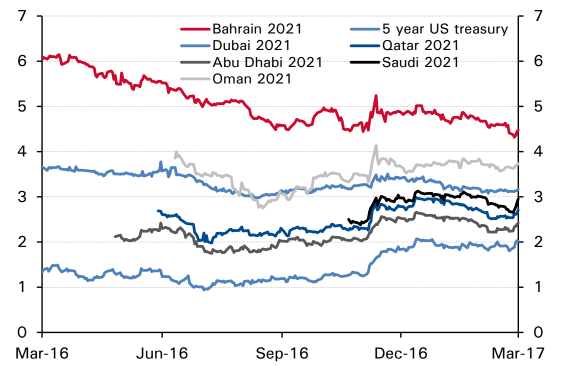
(%)



Source: Thomson Reuters Datastream

Chart 12: GCC bond yields

(%)



Source: Thomson Reuters Datastream

market transactions as a temporary measure pending the capital gains tax. The duty will start at EGP 1.25 per 1000 and will increase to EGP 1.5 and to EGP 1.75 in the following two years. The government had introduced a capital gains tax in 2014 but decided to postpone its implementation for two years in 2015 following investor pressure.

Markets – oil

Brent crude moved a little more into the $56/bbl range last week before closing on Friday at $55.9/bbl. Key price triggers remain absent. (Chart 8.) US shale production gains continue to fly under the radar, under cover of the OPEC/non-OPEC output agreement. US crude production broke through the symbolic 9.0 mb/d level last week, rising to an 11-month high of 9.03 mb/d, while US crude stocks rose to a 6-month high of 520 million barrels. Yet this clearly bearish data failed to exert any down pressure on oil prices.

Markets – equities

It was a generally good week for world equities, with the MSCI World gaining 1%. Markets were excited ahead of President Trump's speech, expecting to get more clarity, especially on taxes. While the speech disappointed on the level of detail, it calmed the political tone and provided a positive vision. US markets were able to hold on to their weekly gains, with the S&P 500 and the DJIA up 0.7% and 0.9%, respectively. The markets were further supported by positive data releases, and seemed unfazed by a likely interest rate hike in March. European equities outperformed on the week, with the Euro Stoxx 50 closing up a strong 3%. European markets were buoyed by the positivity in the US and got a further boost from firming economic figures. Meanwhile, emerging market equities saw some profit-taking with the MSCI EM losing 0.6%. (Chart 9.)

Regional markets underperformed this week, with the MSCI GCC index down 0.8%. The Qatari and Dubai markets lagged the region, losing 1.9% and 1.4%, respectively, as a result of the MSCI rebalancing. In Qatar, the MSCI rebalancing temporarily shifted focus away from the upcoming phase 2 of the FTSE upgrade. All other markets were off on the week. (Chart 10.)

Also in market-related news, this week saw the launch of Saudi's parallel equity market, Nomu. The new market, with easier listing requirements, is to serve as an alternative platform for companies wanting to go public.

Markets – fixed income

After global markets started off the week on a risk-off tone, bond markets suffered throughout the week as a combination of more hawkish Fed talk and Mr. Trump's speech buoyed equities and heightened the likelihood of a March rate hike in the US. The sell-off saw 10-year US treasuries add 17 bps Monday through Friday. Bunds were similarly affected, up 17 bps as inflation in the Eurozone accelerated to 2% in February, its fastest pace in four years. (Chart 11.)

GCC yields on paper that matures in 2021 rose in line with international markets. Yields for Saudi jumped 26 bps on the week. Yields for Abu Dhabi and Qatar also saw notable increases of 14 bps and 13 bps, respectively. Meanwhile, yields for Dubai edged up a mere 2 bps. (Chart 12.)

Oman's $5 billion sale of international bonds last week was in tranches of 5, 10 and 30 years. The issue was four times oversubscribed, with the 5-year bond priced at 190 basis points over mid-swaps, the 10-year at 300 bps over and the 30-year at 387.5 bps over.

Head Office

Kuwait
National Bank of Kuwait SAKP
Abdullah Al-Ahmed Street
P.O. Box 95, Safat 13001
Kuwait City, Kuwait
Tel: +965 2242 2011
Fax: +965 2259 5804
Telex: 22043-22451 NATBANK
www.nbk.com

International Network

Bahrain
National Bank of Kuwait SAKP
Zain Branch
Zain Tower, Building 401, Road 2806
Seef Area 428, P. O. Box 5290, Manama
Kingdom of Bahrain
Tel: +973 17 155 555
Fax: +973 17 104 860

National Bank of Kuwait SAKP
Bahrain Head Office
GB Corp Tower
Block 346, Road 4626
Building 1411
P.O. Box 5290, Manama
Kingdom of Bahrain
Tel: +973 17 155 555
Fax: +973 17 104 860

United Arab Emirates
National Bank of Kuwait SAKP
Dubai Branch
Latifa Tower, Sheikh Zayed Road
Next to Crown Plaza
P.O.Box 9293, Dubai, U.A.E
Tel: +971 4 3161600
Fax: +971 4 3888588

National Bank of Kuwait SAKP
Abu Dhabi Branch
Sheikh Rashed Bin Saeed
Al Maktoom, (Old Airport Road)
P.O.Box 113567,Abu Dhabi, U.A.E
Tel: +971 2 4199 555
Fax: +971 2 2222 477

Saudi Arabia
National Bank of Kuwait SAKP
Jeddah Branch
Al Khalidiah District,
Al Mukmal Tower, Jeddah
P.O Box: 15385 Jeddah 21444
Kingdom of Saudi Arabia
Tel: +966 2 603 6300
Fax: +966 2 603 6318

Jordan
National Bank of Kuwait SAKP
Amman Branch
Shareef Abdul Hamid Sharaf St
P.O. Box 941297, Shmeisani,
Amman 11194, Jordan
Tel: +962 6 580 0400
Fax: +962 6 580 0441

Lebanon
National Bank of Kuwait
(Lebanon) SAL
BAC Building, Justinien Street, Sanayeh
P.O. Box 11-5727, Riad El-Solh
Beirut 1107 2200, Lebanon
Tel: +961 1 759700
Fax: +961 1 747866

Iraq
Credit Bank of Iraq
Street 9, Building 187
Sadoon Street, District 102
P.O. Box 3420, Baghdad, Iraq
Tel: +964 1 7182198/7191944
+964 1 7188406/7171673
Fax: +964 1 7170156

Egypt
National Bank of Kuwait - Egypt
Plot 155, City Center, First Sector
5th Settlement, New Cairo
Egypt
Tel: +20 2 26149300
Fax: +20 2 26133978

United States of America
National Bank of Kuwait SAKP
New York Branch
299 Park Avenue
New York, NY 10171
USA
Tel: +1 212 303 9800
Fax: +1 212 319 8269

United Kingdom
National Bank of Kuwait
(International) Plc
Head Office
13 George Street
London W1U 3QJ
UK
Tel: +44 20 7224 2277
Fax: +44 20 7224 2101

National Bank of Kuwait
(International) Plc
Portman Square Branch
7 Portman Square
London W1H 6NA, UK
Tel: +44 20 7224 2277
Fax: +44 20 7486 3877

France
National Bank of Kuwait
(International) Plc
Paris Branch
90 Avenue des Champs-Elysees
75008 Paris
France
Tel: +33 1 5659 8600
Fax: +33 1 5659 8623

Singapore
National Bank of Kuwait SAKP
Singapore Branch
9 Raffles Place # 44-01
Republic Plaza
Singapore 048619
Tel: +65 6222 5348
Fax: +65 6224 5438

China
National Bank of Kuwait SAKP
Shanghai Representative Office
Suite 1003, 10th Floor, Azia Center
1233 Lujiazui Ring Road
Shanghai 200120, China
Tel: +86 21 6888 1092
Fax: +86 21 5047 1011

NBK Capital

Kuwait
NBK Capital
38th Floor, Arraya II Building, Block 6
Shuhada'a street, Sharq
PO Box 4950, Safat, 13050
Kuwait
Tel: +965 2224 6900
Fax: +965 2224 6904 / 5

United Arab Emirates
NBK Capital Limited - UAE
Precinct Building 3, Office 404
Dubai International Financial Center
Sheikh Zayed Road
P.O. Box 506506, Dubai
UAE
Tel: +971 4 365 2800
Fax: +971 4 365 2805

Associates

Turkey
Turkish Bank
Valikonagl CAD. 7
Nisantasi, P.O. Box. 34371
Istanbul, Turkey
Tel: +90 212 373 6373
Fax: +90 212 225 0353