Monthly Insights

28 November 2019

This page is intentionally left blank

Preface

Recession risks continue to be priced out in the US and 2020 is likely to be a year of stabilization albeit at relatively low levels of growth in other parts of the world. Event risk will remain prominent next year, with trade tensions not fully resolved and a pivotal US election, but strong directional market moves may be lacking.

The next Monthly Insights will be released in January 2020.

Global macro: 'Mediocre growth with downside risks', was the common characterization of US growth that we received on our recent trip to the US, in contrast to the Fed's description of the US economy as being 'in a good place'.

GCC macro: We expect regional growth to accelerate in 2020 although it is likely to remain modest relative to other emerging markets. Lower oil prices are likely to weigh on government spending, although in our view the UAE has room to provide additional fiscal stimulus.

MENA macro: Monetary policy in North Africa will continue on divergent paths in 2020. Egypt has further rate cuts to come, Morocco will remain in its holding pattern, while Tunisia looks to have reached the peak of its hiking cycle and will likely remain on hold next year.

Pakistan macro: Pakistan's IMF-sponsored reform programme has made headway over recent months, but efforts to implement some deeper structural reforms will likely see increasing popular pushback as they weigh on disposable incomes.

Currencies: Looking forward to 2020, trade tensions are likely to remain a theme although some alleviation is likely as a Phase 1 deal is eventually agreed, which could reduce some of the upward pressure on the dollar. As we are retaining one Fed rate cut in our forecasts this could also at the margin cause the dollar to soften slightly, as it seems much less likely that other major central banks will be able to follow suit.

Financial Markets: The performance of financial markets in 2019 was driven by manifestation of slowing economic growth on account of trade conflicts and natural attrition and a dovish shift in global monetary policy. 2020 could well be defined by how these factors play out. Further, the probable crystallization of an unfinished agenda from 2019 (Brexit & Phase 1 trade deal) and challenges of key geopolitical event (US election) could also weigh on financial markets in 2020.

Commodities: Commodity markets face several familiar themes in their outlook for 2020—trade, central banks, global growth. But new factors are growing in importance and will present a challenge for the sector to absorb.

Sector Report: Dubai's tourism sector has seen growth in 2019 with international visitor numbers continuing to rise.

Timothy Fox
Chief Economist & Head of Research

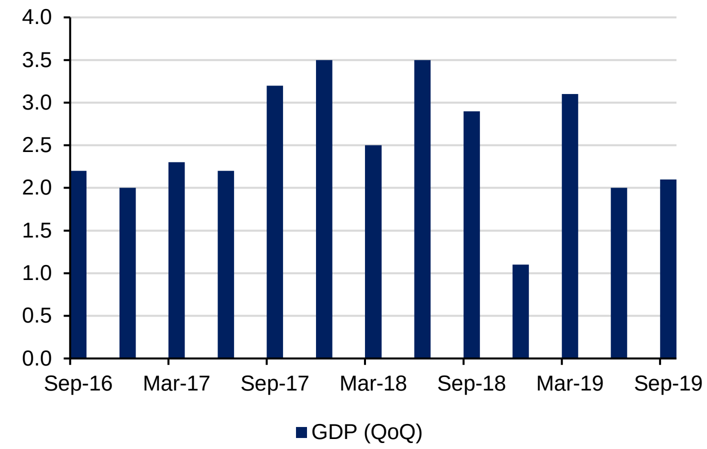
Contents

Global Macro

Fed Chair Jerome Powell this week saw 'the glass as more than half full' in a speech he gave in Rhode Island, and 'the current stance of monetary policy as likely to remain appropriate as long as incoming information remains consistent with our outlook.' According to Powell, the three 25 basis point cuts implemented over July-October are already having a positive effect on consumer and business sentiment 'and boosting spending in interest-sensitive sectors, such as housing and consumer durable goods.'

Our recent visit to the US provided a slightly more circumspect view of the outlook for 2020, however, with economic growth slowing around the world and US private sector surveys signaling that the US is not immune. Consequently we still see downside risks in view of ongoing uncertainty over US-China trade tensions which we think could extend through 2020 especially in a pivotal US election year. For this reason we are retaining a forecast for one more rate cut in 2020, although this could get taken out depending on the progress made over trade in the coming months.

US growth slowing to trend



Source: Bloomberg, Emirates NBD Research

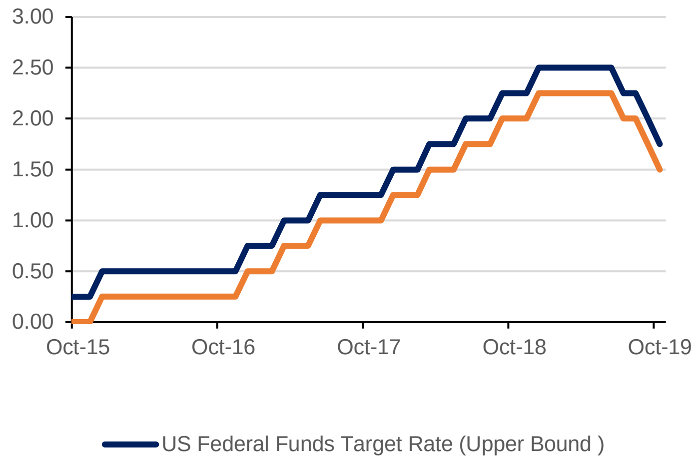
US growth to slow in 2020

While consumption has been strong in 2019, business investment and capex have been less so, with core capital goods orders having decelerated in the US, and residential construction has been a modest drag on growth for the past year and a half. Employment growth, while still solid, has also begun to slow a little this year, although unit labour costs have picked up. US growth is expected to be in a 1.5%-2.0% range for the most part in 2020 after 2.0% in 2019 according to most analysts we met, assuming that the trade war does not get a lot worse, and this is consistent with our own 1.7% forecast for 2020. In 2019 the economy benefited from the lagged effects of expansionary fiscal policy, which is probably going to dwindle next year, while corporate profit margins continue to be squeezed. 'Mediocre growth with downside risks', was the common characterization of US growth that we received in contrast to the Fed's description of the US economy as being 'in a good place'.

Further Fed rate cut in the balance

The main call from our meetings with US banks was that the Fed is likely to sit on its hands in 2020, although there is a better chance of a rate cut than of a hike. We have retained another rate cut in our central forecasts too, with the Fed likely to be increasingly tolerant of any inflationary overshoot. However, if a trade deal is reached in December, we may remove this cut from our forecasts depending on the details of the deal reached.

One more Fed rate cut is our base case



Source: Bloomberg, Emirates NBD Research

Trade tensions to continue

At the moment there is no end in sight to the trade war as most imbalances are still growing. The US trade deficit with China is large relative to America's other major trading partners, which is driving a fundamental review of the US's strategic relationship with its biggest global competitor. While a phase one deal does appear to be in sight, the elements of such a deal are likely to be quite limited which is why it is increasingly referred to as a 'skinny deal'. China has been hurting economically for a long time and probably wants to avoid the addition of further tariffs, and now the US is also weakening it can also do without the prospect of more politically dangerous consumer tariffs being imposed next month.

The basis for a phase one deal would be China buying more agricultural products, continuing to work on intellectual property protection and on financial sector opening and more transparency on reserve management. US concessions will likely revolve around canceling the October and December tariffs, and dropping China from the currency manipulator designation, but notably not reversing the tariffs already introduced. Such a compromise should be enough to underpin markets for a while but do not address the bigger structural differences that exist between the two countries over industrial subsidies, intellectual property theft and technology transfers.

As such the prospect for a more substantial and permanent deal appears unclear. This is because the USD trade gap is huge, the US has always been skeptical of China and Chinese trust in the US has also deteriorated over the course this year. Furthermore bi-partisan support for getting tough on China is increasing, especially in view of recent events in Hong Kong, and an election year makes the US more sensitive to strategic trade related issues. From China's viewpoint giving Trump a more substantive deal could help him politically but it runs the risk of being reversed after the election. In the run-up to the mid-term elections last year China stopped negotiating, so a similar position may be adopted next year as their policymakers wait and see to potentially negotiate with a new president after the election.

China feels the effects of tariffs

Source: Bloomberg, Emirates NBD Research

Political risks

The impeachment process going ahead in the House of Representatives is a significant challenge to President Trump's authority, but it will likely make little difference to the political landscape in election year if a Senate trial fails to convict him in the end. Q1 of next year will likely be dominated by the Senate trial, generating plenty of headlines and tweets which will keep sentiment nervous. However, with voting likely to be on party lines in the end the outcome may well be an anti-climax, similar to the outcome of the Mueller Report this year. More important implications for the US Presidential elections next November will probably flow from the Democrat nominee who will be chosen in H120. Michael Bloomberg's decision to enter the contest could have a significant bearing on the outcome, and on the likelihood of the Democrats unseating President Trump. The result of the election should not be seen as predetermined therefore, as it will take only a few votes in a number of key states to swing it to the Democrats.

Brexit should get resolved

Our current assumption based on opinion polls is that the Conservative Party will win the UK general election on December 12th with an outright majority. Polling gives Boris Johnson's Conservatives in excess of 40% of the electorate, while the main opposition Labour Party is on around 30%, with the smaller parties generally losing support. Should this outcome transpire then Johnson's Brexit deal will likely get support in the House of Commons in time for the 31st January deadline. While markets will then redirect their focus to whether a trade deal can be reached between the EU and the UK by the end of next year, there would likely be considerable relief that further delays to Brexit will be avoided and that a Labour government under Jeremy Corbyn has also not transpired. There may also be upside revisions to UK growth forecasts in the event of such a result, and speculation may quickly revert back to how long it will be before the Bank of England turns more hawkish. The main risk to this analysis, however, lies with the reliability of the opinion polls which have been shown to be faulty in the past. In particular another Conservative led government without a complete majority would pose questions about the Johnson Brexit deal leading to a further extension and/or a second referendum. The extension of such uncertainty would undoubtedly add to the downside risks for the economy and would complicate the outlook for its markets especially the pound. Needless to say a Corbyn led Labour government would quickly see UK equity markets unravel and the pound fall as well.

EU vulnerabilities persist

The Eurozone being a relatively open economy, it will be vulnerable to any fallout from the US-China trade war given its close ties to China, as well as from the possible risk of auto tariffs being imposed if the US focus on trade switches away from China and towards the EU. Political risk from any continued Brexit hangover could also influence negatively, while other specific regional risks also exist in Belgium, Italy and Spain for example. With very little policy ammunition left, as negative rates cannot fall further and with fiscal policy frozen, the scope for a meaningful recovery from the 1.1% growth rate assumed for this year looks quite limited at this point.

China transitioning lower

China's growth meanwhile is still slowing and will probably ease further in 2020 as it transitions towards a more sustainable long term rate of between 5.5%-6.0%. Chinese policymakers continue to face the need to balance the need to meet its economic targets while also preventing debt imbalances from building up. While fiscal stimulus has been ramped up this year and monetary policy has been eased there is probably scope for both approaches to continue being used.

Tim Fox
+9714 230 7800

Key Economic Forecasts - Global

US	2014	2015	2016	2017	2018	2019f	2020f
Real GDP %	2.5	2.9	1.6	2.4	2.9	2.3	1.7
Current A/C % GDP	-2.1	-2.2	-2.3	-2.3	-2.4	-2.5	-2.6
Budget Balance % GDP	-2.7	-2.6	-3.1	-3.4	-4.2	-4.5	-4.7
CPI %	1.6	0.1	1.3	2.1	2.5	1.8	2.0
Eurozone							
Real GDP %	1.4	2.1	1.9	2.5	1.9	1.1	1.1
Current A/C % GDP	2.5	2.7	3.1	3.2	2.9	3.0	2.7
Budget Balance % GDP	-2.5	-2.0	-1.6	-1.0	-0.5	-1.0	-1.1
CPI %	0.4	0.2	0.2	1.5	1.8	1.2	1.3
UK							
Real GDP %	2.9	2.3	1.8	1.8	1.4	1.2	1.1
Current A/C% GDP	-4.9	-4.9	-5.2	-3.3	-3.9	-4.3	-4.0
Budget Balance % GDP	-5.2	-4.1	-2.8	-1.9	-2.3	-1.5	-1.6
CPI %	1.5	0.0	0.7	2.7	2.5	1.9	2.0
Japan							
Real GDP %	0.4	1.3	0.6	2.0	0.8	0.9	0.3
Current A/C % GDP	0.8	3.1	4.0	4.2	3.5	3.3	3.2
Budget Balance % GDP	-5.4	-3.6	-3.5	-3.0	-2.5	-3.5	-3.0
CPI %	2.7	0.8	-0.1	0.5	1.0	0.7	1.0
China							
Real GDP %	7.3	6.9	6.7	6.8	6.6	6.2	6.0
Current A/C % GDP	2.3	2.8	1.8	1.6	0.4	0.6	0.0
Budget Balance %GDP	-1.8	-3.4	-3.8	-3.7	-4.2	-4.5	-4.4
CPI%	2.0	1.4	2.0	1.6	2.1	2.4	2.3
India*							
Real GDP%	6.4	7.4	8.0	8.2	7.3	6.6	6.5
Current A/C% GDP	-1.4	-1.1	-0.6	-1.5	-2.5	-2.5	-2.6
Budget Balance % GDP	-4.3	-3.5	-3.7	-3.9	-3.6	-3.5	-3.7
CPI %	6.7	4.9	5.0	3.3	4.0	3.0	3.4

Source: Bloomberg, Emirates NBD Research
**For India the data refers to fiscal year (April – March)*

GCC Macro

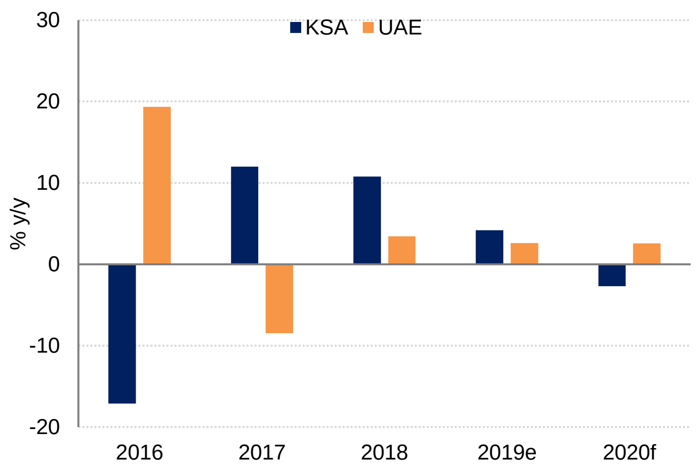
2019 has been a challenging year for the GCC, with growth likely to come in well below our forecasts at the start of the year. Indeed, we revised down our 2019 growth estimates in October, as the extent of oil production cuts and production disruptions became more evident, and as regional PMIs softened in the third quarter.

The global macro environment as we head into 2020 remains uncertain on several fronts, including on global trade, Brexit and US domestic politics. In the GCC too, geopolitical tensions remain elevated while the outlook for oil prices allows little room for further fiscal stimulus in some countries. Lower interest rates should provide some boost to economic growth, but the US dollar remains relatively strong on a trade weighted basis, despite 75bp in rate cuts by the Fed this year, and this has continued to be a headwind for the GCC countries with their pegged exchange rates.

Nevertheless, there are some reasons to be optimistic as we head into 2020. We expect oil production to rise across the major GCC oil producers in 2020, even as the OPEC+ agreement is likely to be extended through H1 2020. This year, most of the GCC oil producers have over-complied with the OPEC targets, allowing room for Saudi Arabia, the UAE and Kuwait to boost production while still complying with the agreement.

The outlook for non-oil sector growth is more varied across the GCC. In Saudi Arabia, the release of the pre-budget statement earlier this month indicated a shift to a tighter fiscal policy, following 3 years of spending growth. The pre-budget statement shows a -2.7% decline in total expenditure next year, with an even sharper drop in projected revenues.

Budget spending growth



Source: Haver Analytics, UAE Ministry of Finance, Emirates NBD Research

The government expects the private sector to contribute more to GDP growth, and has indicated that privatisation of state-owned assets across a wide range of sectors will support private sector investment in the kingdom. Notwithstanding the upcoming IPO of Saudi Aramco, progress on privatisation in other sectors has been slow, and we think a tighter fiscal policy in 2020 will likely weigh on non-oil sector growth. Consequently we have revised our forecast for non-oil sector growth down to 2.3% from 2.9% previously. However, the hydrocarbons sector is likely to expand next year, following this year's sharp contraction. As a result, we expect headline GDP growth of 2.0% in Saudi Arabia next year.

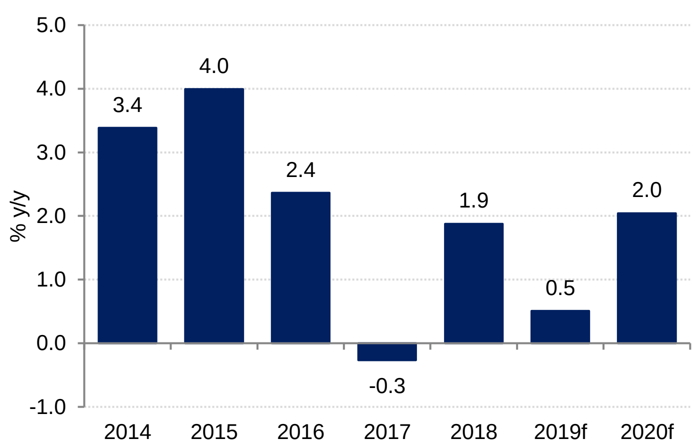
The UAE has been relatively cautious with regards to its fiscal stance over the last few years. Total expenditure in 2018 was just 3.5% higher y/y, after declining in 2017 (ministry of finance figures). The non-oil budget deficit has also narrowed since 2016. Data for H1 2019 shows the non-oil deficit was only marginally wider than in H1 2018, while the overall budget posted a surplus of AED 26.4bn in H1 2019. In our view, the UAE has room to boost stimulus next year, should the authorities choose to do this.

While we have revised down our estimate for Dubai's GDP growth this year to 2.0% from 3.0%, following the release of official H1 GDP figures, we retain our 2019 UAE GDP growth forecast of 2.0% as slower non-oil sector growth has been offset by stronger than expected hydrocarbons sector growth. Q1 GDP show the hydrocarbons sector expanded 12.4% y/y, and the UAE's crude oil output is up 2.8% in the year to October.

In 2020, we expect non-oil sector growth in the UAE to accelerate on the back of Expo 2020-related spending and tourism growth, while the hydrocarbons sector should also contribute positively to headline GDP growth. We have pencilled in 2.4% real GDP growth in 2020.

Growth in Qatar, Kuwait, Oman and Bahrain is also expected to improve off a low 2019 base, and we forecast the weighted average GDP growth for the GCC next year will rise to 2.0% from an estimated 0.5% in 2019. This is by no means stellar growth relative to pre-2016 levels or compared with other emerging markets, but it suggests a moderate improvement from this year.

Weighted average of GCC GDP growth

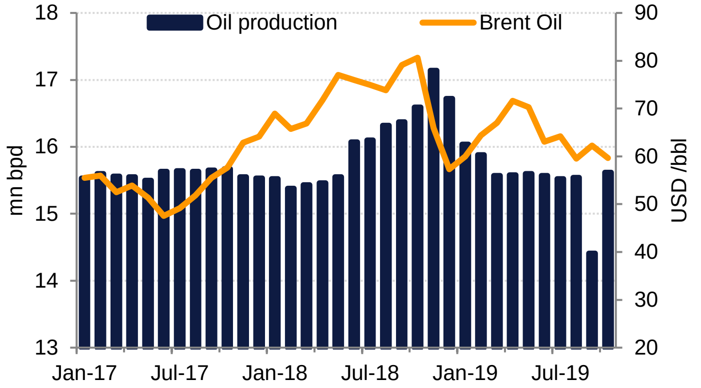


Source: Haver Analytics, Emirates NBD Research

Khatija Haque
+971 4 230 7803

GCC in Pictures

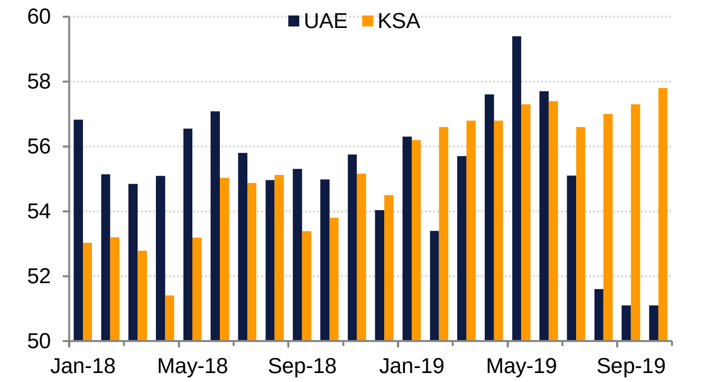
GCC Oil Production and Oil Price



Excludes Qatar, Bahrain and Oman

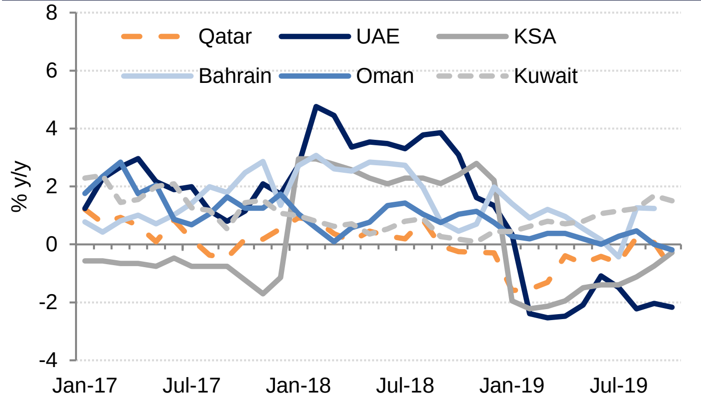
Source: Bloomberg, Emirates NBD Research

Purchasing Managers' Index



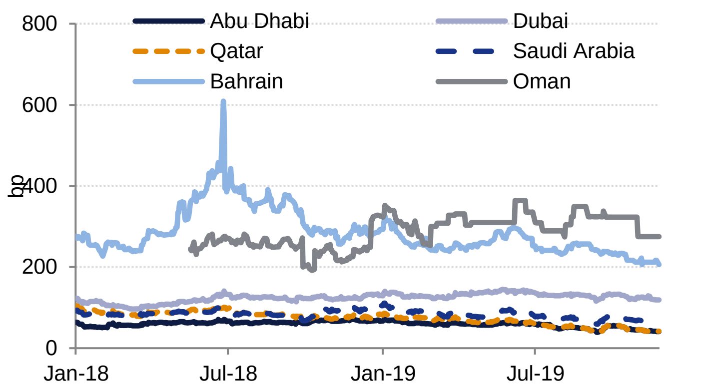
Source: IHS Markit, Emirates NBD Research

Inflation



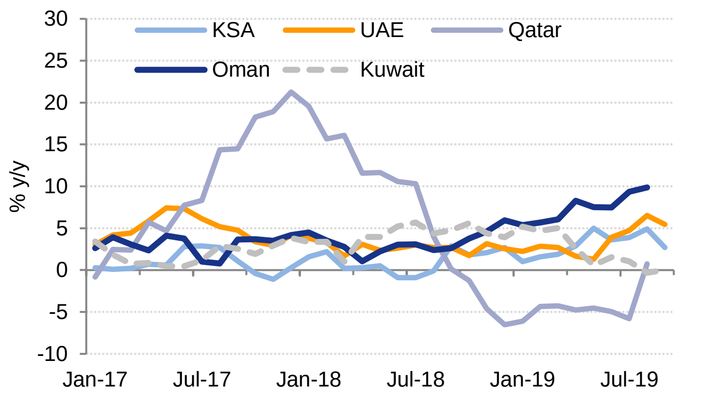
Source: Haver Analytics, Emirates NBD Research

CDS Spreads



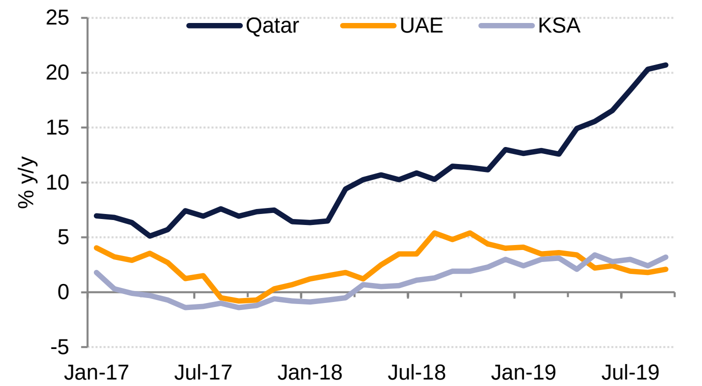
Source: Bloomberg

Money supply (ex government. deposits)



Source: Haver Analytics, Emirates NBD Research

Private sector credit*



**Qatar data is bank loan growth to private sector, not total private sector credit. Source: Haver Analytics, Emirates NBD Research*

Key Economic Forecasts - GCC

United Arab Emirates	2016	2017	2018e	2019f	2020f
Nominal GDP $bn	357.3	378.0	414.5	415.1	419.8
Real GDP %	3.1	0.5	1.7	2.0	2.4
Current A/C % GDP	3.7	7.3	9.1	7.6	5.2
Budget Balance % GDP	-2.0	-1.4	1.2	-1.6	-2.8
CPI %	1.6	2.0	3.1	-1.6	2.0
Saudi Arabia					
Nominal GDP $bn	644.9	688.6	782.5	772.4	786.9
Real GDP %	1.7	-0.7	2.2	-0.4	2.0
Current A/C % GDP	-3.7	1.5	9.0	4.8	6.1
Budget Balance % GDP	-12.9	-9.2	-4.6	-6.7	-8.2
CPI %	2.1	-0.8	2.5	-1.0	2.0
Qatar					
Nominal GDP $bn	151.7	166.9	191.4	186.3	194.6
Real GDP %	1.8	1.1	1.4	0.7	2.0
Current A/C % GDP	-5.5	3.8	8.7	4.3	1.1
Budget Balance % GDP	-9.2	-6.6	2.2	1.9	-0.1
CPI %	2.7	0.4	0.2	-0.5	2.0
Kuwait					
Nominal GDP $bn	109.4	119.5	141.5	139.9	145.4
Real GDP %	2.9	-3.5	1.2	0.1	1.4
Current A/C% GDP	-4.6	8.0	14.4	7.2	8.8
Budget Balance % GDP	-13.9	-9.0	-3.0	-5.6	-7.0
CPI %	3.2	1.6	0.6	1.0	1.5
Oman					
Nominal GDP $bn	65.4	70.5	79.2	79.2	81.3
Real GDP %	5.1	0.3	1.8	1.1	1.7
Current A/C % GDP	-19.2	-15.6	-5.5	-6.0	-5.4
Budget Balance % GDP	-21.1	-13.9	-6.6	-8.2	-9.0
CPI %	1.1	1.6	0.9	1.0	2.5
Bahrain					
Nominal GDP $bn	32.3	35.4	37.7	39.0	40.6
Real GDP %	3.5	3.8	1.8	2.0	2.4
Current A/C % GDP	-4.6	-4.5	-5.9	-6.3	-7.1
Budget Balance % GDP	-13.5	-10.0	-6.3	-6.6	-5.8
CPI %	2.8	1.4	2.1	1.5	2.0
GCC (Nominal GDP weighted avg)					
Nominal GDP $bn	429	456	515	509	517
Real GDP %	2.4	-0.3	1.9	0.5	2.0
Current A/C % GDP	-0.3	8.1	15.7	11.0	8.8
Budget Balance % GDP	-9.6	-6.8	-2.7	-4.0	-5.1
CPI %	2.6	0.1	2.4	0.1	2.7

Source: Haver Analytics, National sources, Emirates NBD Research

MENA Macro : Mixed monetary policy in North Africa

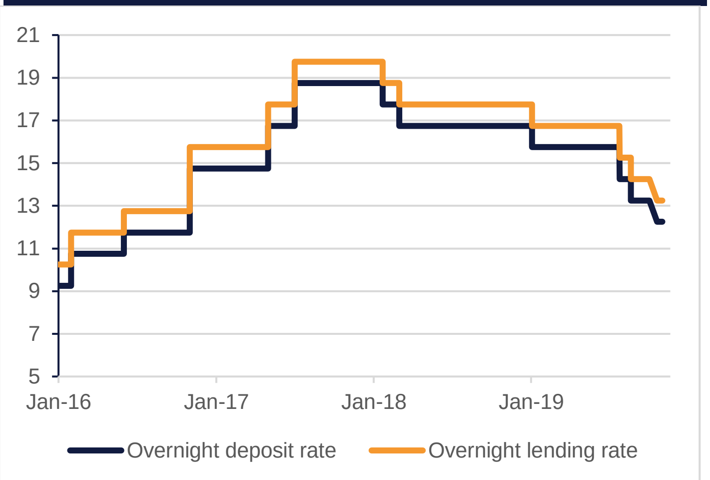
The policy direction change from the US Federal Reserve this year, as it went from tightening in December to three 25 basis point cuts over July to October, is only the most prominent loosening of monetary policy globally in 2019. The ECB has cut rates further into negative territory and resumed quantitative easing, and a host of emerging markets around the globe, from Brazil to India, have also loosened policy. The global environment has given many economies that had been struggling to boost growth room to stimulate demand through lower rates, without running the risk of prompting large hot money outflows.

In North Africa the story has been somewhat more nuanced, with Egypt taking the opportunity to slash its benchmark rates, Morocco holding rates steady, and Tunisia forced to hike. In 2020, we anticipate that these trends will largely continue on the same path.

Egypt has further room to ease

While the pace of monetary easing in Egypt will slow in 2020, we nevertheless anticipate that there will be further cuts to the benchmark overnight deposit rate between now and the end of next year. As the negative effects of the economic reform programme have passed through the economy, inflation has slowed sharply, dropping to just 3.1% y/y in November. This compares to an average of 29.6% in 2017, in the wake of currency devaluation and subsidy reforms. While the disinflation trend has likely reached its bottom, we nevertheless believe that there remains room for the CBE to implement further rate cuts, albeit at a more measured pace.

Rate-cutting in earnest now



Source: Haver Analytics, Emirates NBD Research.

There remains one more MPC meeting for the CBE before the end of the year, and while the outcome is less certain than it was prior to the last rate decision, we still think it likely that the bank will implement one more 100 bps cut on December 26, which would take the overnight deposit rate to 11.25%. In 2020, we forecast a further 100-125 bps of cuts, although these will likely be implemented in smaller moves than those seen over 2019, and will remain data dependent. The CBE will be keen to maintain attractive real rates in order to not deter the strong portfolio investor interest seen over this year. Luckily for the bank, the global easing trend has been adopted by other EM carry trade competitors such as Turkey, which allows Egypt to remain competitive even if it implements further rate cuts. In November, real interest rates in Egypt were 9.2%, compared with 5.4% in Turkey. Combined with a strengthening currency and political stability, the trade will remain of interest even as the CBE cuts further.

Morocco holding steady

Morocco is quite a different story from Egypt, where the order of the day has been monetary policy stability, which we forecast will continue through next year. Morocco's benchmark interest rate has been on hold at 2.25% for three and a half years since 2016, and we do not anticipate any change in 2020. Inflation has been almost flat, averaging just 0.2% y/y over the first 10 months of the year, and while we anticipate a modest strengthening in 2020 – we forecast an average 0.7% in 2020 – it will not be of a magnitude to prompt tighter policy. In its communiqué following its September 24 rate decision, the Bank al-Maghrib reiterated that 'based on the medium-term prospects for inflation, growth, external accounts, monetary conditions and public finance', the current level remained 'appropriate.'

MAD/USD could see greater volatility

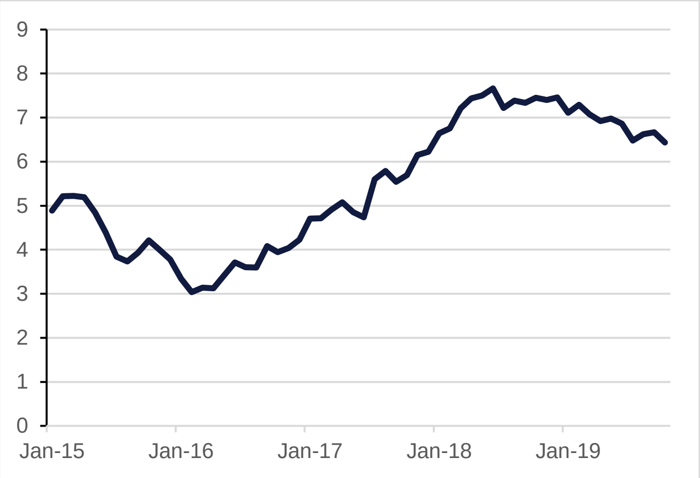
Source: Haver Analytics, Emirates NBD Research

While the benchmark interest rate is staying stationery, the BAM has been adjusting monetary policy in other arenas, and at the September meeting it sought to boost liquidity by reducing the reserve ratio from 4.0% to 2.0%. In 2020, the key factor to watch for is whether or not the central bank ploughs ahead with its plan to move the dirham towards a floating rate – something the IMF has long been pressing for. In 2018, the currency's trading band was widened to a 5% range around a target level (the currency's basket is 60% EUR, 40% USD), as compared to the previous 0.6%, but progress has been measured so far. As it stands, there is little indication that there will be any further exchange rate liberalisation in 2020.

Tunisian hiking cycle has run its course

Finally, Tunisia is something of a global outlier in that is has raised its benchmark interest rate in 2019, with a February hike the third in 12 months. The 100 bps hike took the benchmark rate to 7.75%.This tightening cycle was done with the explicit support of the IMF, which urged tighter monetary policy in order to curb rising inflation and keep real interest rates in positive territory – inflation has averaged 6.8% y/y over the first 10 months of 2019, compared to 7.3% in 2018 and 5.2% in 2017.

CPI inflation (% y/y) has peaked



Source: Haver Analytics, Emirates NBD Research

Indications are that price growth has peaked, with the trend having been towards disinflation since June – the 6.4% print in October was the slowest inflation rate since December – and oil prices set to average moderately lower in 2020 according to our forecasts. As such, we anticipate that there will be no more interest rate hikes in the current cycle. Nevertheless, the support of the IMF for high interest rates, and the still relatively high pace of price growth, will preclude any cuts for the time being.

Daniel Richards
+971 4 609 3035

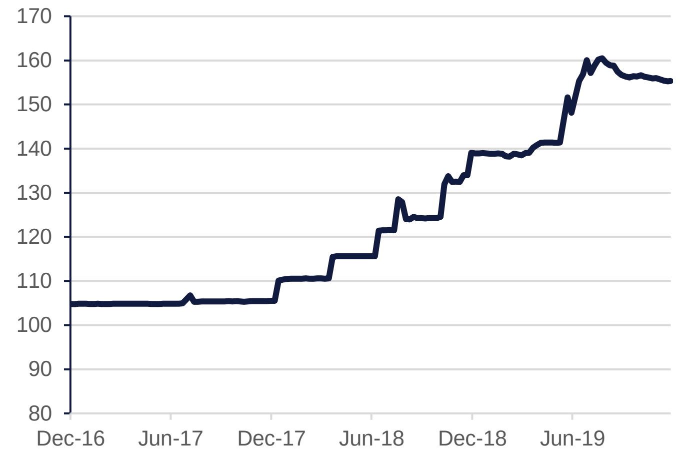
Pakistan Macro: Reform programme in progress

The Pakistani economy is looking far more stable than it did some six months ago, when a balance of payments crisis was driving a rapid run-down in reserves and increasing investor wariness towards the country. A series of currency devaluations and entering into an agreement with the IMF has helped stabilise matters, although this has come at a cost to inflation and growth, which has the potential to fuel rising discontent.

Prone to crises

With inelastic imports and exports highly reliant on favourable weather (textiles and foodstuffs account for around 80% of exports), Pakistan has long been prone to balance of payments crises. Over the past several years these dynamics were exacerbated by both an overvalued currency and low interest rates – which contributed to higher consumer imports – and capital imports related to infrastructure projects; Pakistan is a key state in China's massive Belt and Road Initiative (BRI). The situation came to a head as despite several currency devaluations, inflows failed to pick up and FX reserves fell to just two months' import cover earlier this year, notwithstanding external assistance from the UAE, Saudi Arabia and China. Newly elected prime minister, Imran Khan, was eventually forced to go to the IMF for support – the 22nd arrangement the country has had with the Fund (*see our May 2019 Monthly Insights publication for more detail*).

PKR/USD stable after multiple devaluations

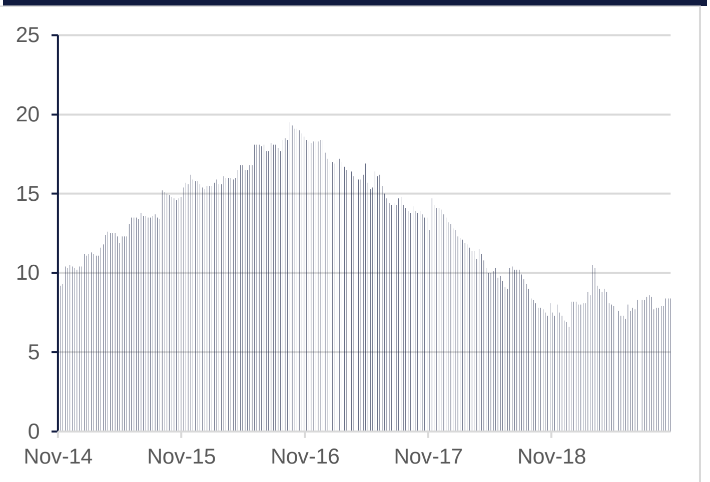


Source: Bloomberg, Emirates NBD Research.

Since the start of the Extended Fund Facility – worth USD 6bn over three years – Pakistan's macroeconomic metrics have improved somewhat, and this was reflected in the IMF's first review of Pakistan's progress on the programme, published November. According to the Fund, all performance criteria 'were met with comfortable margins and progress continues towards meeting all structural benchmarks.' Crucially, the review highlighted that the external and fiscal imbalances were narrowing, and that progress was being made on a transition to a 'flexible, market-determined exchange rate.' Once the review is signed off by IMF management and directors, USD 450mn of the EFF will be released. In addition, the completion of the review will also 'help unlock significant funding from bilateral and multilateral partners.' As ever, the value of an IMF programme is not solely in the funding provided by the body itself, but the policy anchor and legitimacy it provides, which helps assure other investors that the economy is on the right track.

From the multi-year low of USD 6.6bn at the start of the year, foreign exchange reserves at the central bank have ticked up to USD 8.4bn in November. Some of this has been attributed to the repayment of embezzled funds by corrupt officials (despite Imran Khan repeating that he will not reopen the controversial NRO amnesty programme), but the key driver has been a narrowing of the current account deficit and mounting interest in Pakistani local debt, in a similar way to that seen in Egypt as it began its own EFF programme some three years ago.

Decline in reserves staunched (USDbn)



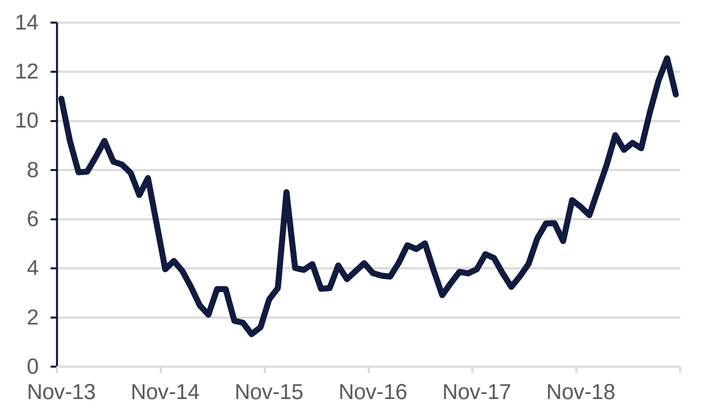
Source: Bloomberg, Emirates NBD Research

Over the first quarter of the fiscal year started in July, net foreign investment into Pakistan hit USD 1.1bn, compared to an outflow of USD 77.5mn in the corresponding period a year earlier. USD 436.7mn of this has been foreign public investment into debt securities, attracted by the comparatively high interest rates (the State Bank of Pakistan is a global outlier in that it has hiked rates this year while the rest of the world is loosening policy) and the stability seen in the rupee since July, since when it has seen some modest appreciation. At the same time, the current account has improved to the extent that October saw a surplus for the first time in over four years. Although the rolling four-month position was a deficit of USD 1.5bn, this compares favourably to the shortfall of USD 5.6bn over the first four months of the previous fiscal year. The improvement has largely been driven by slower imports, but exports have also picked up, boosted by the more competitive currency.

Inflation the cost of devaluations

While the external position has been improved by the currency devaluations, they have also served to push up inflation, meaning that the more disadvantaged in Pakistan are taking the brunt of the reforms. Inflation has averaged 9.7% y/y this year, compared to 4.8% over 2018, and stood at 11.1% at the latest print in October – though this was down marginally from the September peak of 12.6%. While the IMF believes that inflation will slow from hereon in, the slow recovery from the crisis will risk mounting street protests, such as that seen in November when thousands staged a sit-in in Karachi.

CPI inflation (% y/y) has soared



Source: Bloomberg, Emirates NBD Research

While some comparisons with Egypt's recent macroeconomic reform programme are apt, President Sisi had, and has, more political capital and security than Khan currently enjoys. As such, whether or not his administration will be able to stay the course and implement some of the more structural reforms necessary is unclear. Pakistan's tax base is woefully small, contributing to the government's perennial fiscal deficits and escalating debt levels – and attendant debt servicing costs. However, in the current climate it will be difficult for Khan to implement any more meaningful structural reforms without facing popular pushback.

Daniel Richards
+971 4 609 3035

Key Economic Forecasts – Non-GCC Oil Importers

Egypt*	2016	2017	2018e	2019f	2020f
Nominal GDP $bn	332.4	225.8	241.6	299.2	368.4
Real GDP %	4.3	4.1	5.3	5.6	5.8
Current A/C % GDP	-6.0	-6.4	-2.5	-2.7	-2.8
Budget Balance % GDP	-12.05	-10.83	-9.83	-8.27	-7.30
CPI %	13.7	29.6	14.4	9.5	7.0
Jordan	332.4	225.8	241.6	299.2	368.4
Nominal GDP $bn	39.2	40.7	41.5	42.5	43.5
Real GDP %	2.1	2.1	2.0	2.3	2.3
Current A/C % GDP	-9.4	-10.6	-6.9	-3.2	-3.0
Budget Balance % GDP	-3.2	-2.7	-2.6	-2.2	-2.3
CPI %	-0.8	3.3	4.5	0.5	1.3
Lebanon					
Nominal GDP $bn	51.1	52.1	62.3	66.1	70.5
Real GDP %	1.6	0.6	0.2	0.2	1.3
Current A/C % GDP	-20.5	-23.3	-19.9	-19.8	-19.4
Budget Balance % GDP	-9.6	-7.0	-10.8	-8.7	-7.7
CPI %	-0.8	4.5	6.1	2.9	2.9
Morocco					
Nominal GDP $bn	1013.2	1063.4	1106.8	1141.4	1189.5
Real GDP %	103.3	109.6	117.9	119.2	124.2
Current A/C % GDP	35.3	35.7	36.2	36.6	37.1
Budget Balance % GDP	2928	3066	3257	3253	3351
CPI %	9.9	10.6	9.9	9.5	9.0
Tunisia	103.3	109.6	117.9	119.1	123.7
Nominal GDP $bn	41.7	36.8	34.5	31.9	33.5
Real GDP %	1.0	1.7	2.5	1.5	2.3
Current A/C % GDP	-8.9	-11.1	-12.9	-12.0	-10.3
Budget Balance % GDP	-6.2	-6.7	-5.5	-5.1	-4.6
CPI %	3.7	5.3	7.4	6.8	6.3
Oil Importers (GDP weighted avg)					
Nominal GDP $bn	223.8	147.8	158.8	198.4	248.6
Real GDP %	3.05	3.38	3.66	3.85	4.33
Current A/C % GDP	-7.4	-8.3	-6.5	-5.8	-5.2
Budget Balance % GDP	-9.4	-7.6	-7.5	-6.8	-6.2
CPI %	8.5	15.8	9.1	5.9	4.9

Source: Haver Analytics, National sources, Emirates NBD Research
**Egypt data refers to fiscal year (July-June)*

Key Economic Forecasts – Non-GCC Oil Exporters

Algeria	2016	2017	2018e	2019f	2020f
Nominal GDP $bn	160.2	167.6	165.5	165.0	166.6
Real GDP %	3.2	0.4	1.6	1.0	2.0
Current A/C % GDP	-12.3	-13.3	-10.4	-8.7	-7.9
Budget Balance % GDP	-13.0	-6.5	-9.2	-9.5	-10.5
CPI %	5.8	6.0	3.5	2.6	3.3
Iran					
Nominal GDP $bn	441.8	446.9	422.4	493.2	604.6
Real GDP %	12.4	3.3	-4.2	-7.6	0.5
Current A/C % GDP	3.7	3.5	3.7	-0.2	-1.4
Budget Balance % GDP	-4.8	-5.1	-4.2	-4.4	-3.9
CPI %	8.7	10.0	21.0	38.7	25.0
Iraq	441.8	446.9	433.4	494.1	586.2
Nominal GDP $bn	165.2	166.2	215.5	243.3	250.7
Real GDP %	9.6	1.0	0.3	4.2	4.1
Current A/C% GDP	1.3	9.0	16.3	11.4	10.9
Budget Balance % GDP	-15.0	-1.8	8.3	-3.8	-3.4
CPI %	1.3	0.7	0.4	0.0	0.6
Libya					
Nominal GDP $bn	43.6	63.3	76.1	88.2	104.2
Real GDP %	-6.9	34.8	7.6	5.4	10.4
Current A/C% GDP	-10.2	-9.5	-2.1	-2.6	-2.9
Budget Balance % GDP	-18.1	-10.6	-7.1	-6.3	-5.9
CPI %	9.5	25.0	11.5	10.0	8.5
Oil Exporters (GDP weighted avg)					
Nominal GDP $bn	312.4	307.4	293.2	340.9	414.8
Real GDP %	8.7	5.3	-0.7	-2.2	2.4
Current A/C % GDP	0.5	0.4	3.4	0.2	-0.1
Budget Balance % GDP	-8.0	-6.9	-3.0	-4.8	-4.8
CPI %	6.1	8.2	12.3	21.1	14.9

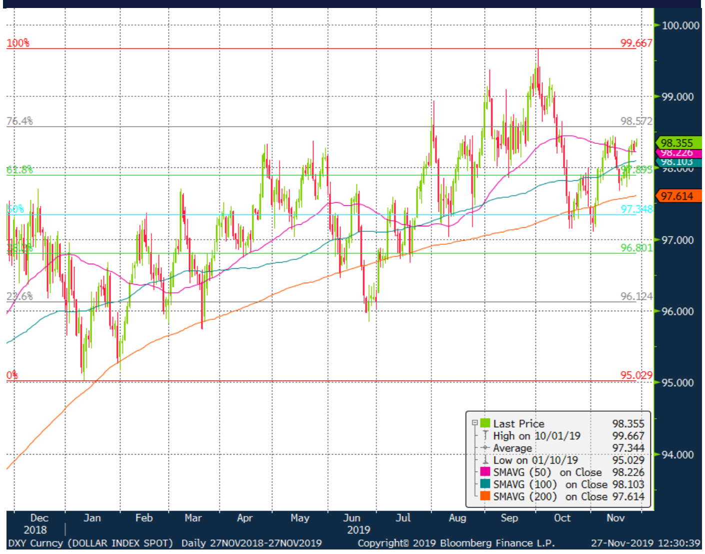
Currencies

Dollar to weaken slightly in 2020

As we cross the midpoint of the final quarter of 2019, we see that the dollar has firmed against a basket of the other major currencies. Year to date, the Dollar Index (DXY) has risen 2.19% to its present level of 98.281. These gains have happened despite the three interest rate cuts in 2019 (for a total of 75bps) from the Federal Reserve and can be attributed to two main issues. Despite growth slowing to trend, the United States economy continues to outperform rival developed economies. Secondly, the dollar has benefited from safe haven bids on the back of global concerns over escalating trade tensions between the United States and China.

Looking forward to 2020, trade tensions are likely to remain a theme although some alleviation is likely as a phase one deal is eventually agreed, which could reduce some of the upside pressure on the dollar. As we are retaining one Fed rate cut in our forecasts this could also at the margin cause the dollar to soften, as it seems much less likely that other central banks will be to follow suit.

DXY continues to remain supported



Source: Bloomberg

Technical analysis of the weekly candle chart reveals that over H2 2019, any weekly declines have been halted by support at the 50-week moving average (currently 97.359). While the price remains above this level, dollar firmness is likely to persist in the short-term. In order to indicate that a reversal in the dollars uptrend has commenced, one would need to see a weekly close below this key level to be the first technical indicator.

EUR continues to be hit from all sides

As 2019 nears its twilight, the single currency continues to find itself pressured by the usual culprits, a slowdown in growth and negative interest rates. Aggregate data in the Eurozone has continued to show that growth remains under pressure with the manufacturing sector continuing to contract. The PMI surveys indicate that growth in Q4 2019 may be even slower than the 0.2% q/q headline figure for Q3. Under these circumstances and an absence of inflationary pressures, investor expectations from the ECB are that interest rates are likely to stay negative for the foreseeable future. These expectations have been reinforced by Mario Draghi's replacement and current ECB President Christine Lagarde. Lagarde has consistently been describing Eurozone and global growth prospects as marked with doubt and has called on fiscal policy support from various members of the Eurozone.

EURUSD maintains downside risks

Source: Bloomberg

Not much is likely to change in next year. There is unlikely to be a sudden acceleration in growth and risk of the continent going into recession will remain present. While we expect the EURUSD cross to strengthen gradually and modestly over the next 12 months, we believe that this will be more attributed to the US economy losing its edge, rather than the a significant reversal in Eurozone fortunes.

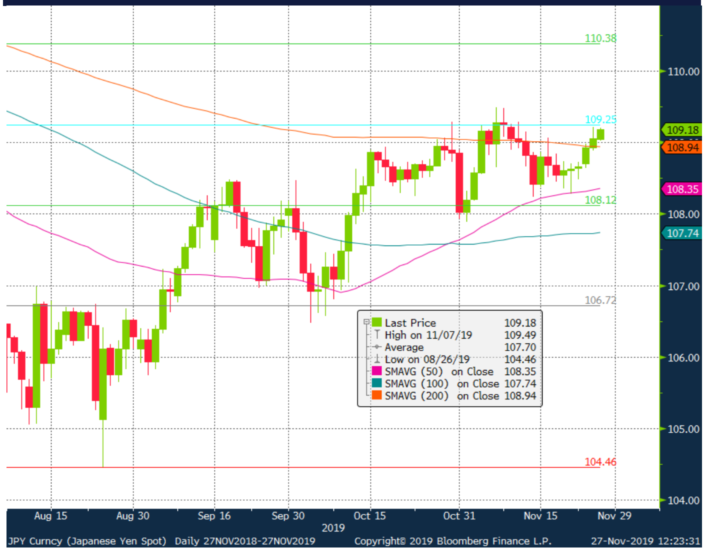
Year to date, EURUSD has declined by almost 4% and currently trades at 1.1015, a level which is below the crosses 23.6% one-year Fibonacci retracement (1.1042). In addition to this, technical analysis of the weekly candle charts shows that the prices has been in an weekly downtrend since February 2018. In the short-term we believe this leaves the euro vulnerable to further downside, however in the medium term, we expect a break of the 23.6% one-year Fibonacci retracement to initiate a gradual climb towards the 50-week moving average (1.1209) by Q1 2019.

USDJPY to remain subdued

The Japanese yen has had a strong 2019 and remained propped up by safe haven bids that have accompanied widespread geopolitical uncertainty that has persisted through much of 2019. In addition to this, the relationship between USDJPY and Treasury yields remains significant and the multiple FOMC cuts of 2019 have kept the price in check.

Looking forward to next year, we do not expect a major change in USDJPY and expect that JPY will continue to be supported by the yen's appeal as a safe haven and may also benefit from a decline in yields should the Federal Reserve cut interest rates further which we still expect.

USDJPY remains between retracements



Source: Bloomberg

For much of November, the USDJPY cross has remained in a range from 108.50 to 109.50 and we expect this range to hold for the most part. Analysis of the weekly candle chart shows that a close above the 50% one-year Fibonacci retracement (109.25) or below the 38.2% one-year Fibonacci retracement (108.12) will be required in order for the price to break out of this range.

GBP likely to benefit from Brexit deal

In 2019, the pound has continued to largely be immune to economic data, which has been for the most part better than expected. Instead, the main driver behind sterling has been sentiment surrounding the outcome of Brexit. Originally extending the March 31st deadline, the Brexit headlines have caused great volatility for GBP as markets continued to adjust their views based on expectations of the timing and nature of Brexit. Looking forward, we assume that the Conservative Party will win the UK general election held on December 12th with an outright majority. Such an outcome would likely result in Prime Minister Boris Johnson's current Brexit deal winning support in the House of Commons before the January 31st 2020 deadline. Such an outcome would be constructive for the pound as it would reduce Brexit uncertainties. In addition the relief will likely increase investor risk appetite for UK assets and result in improved growth expectations and a more positive economic environment. In such an environment, we would expect the Bank of England to adopt a more hawkish stance. All of these factors in 2020 would combine and result in GBP regaining much of the ground lost over the last 24 months.

GBPUSD benefits from deal potential

Source: Bloomberg

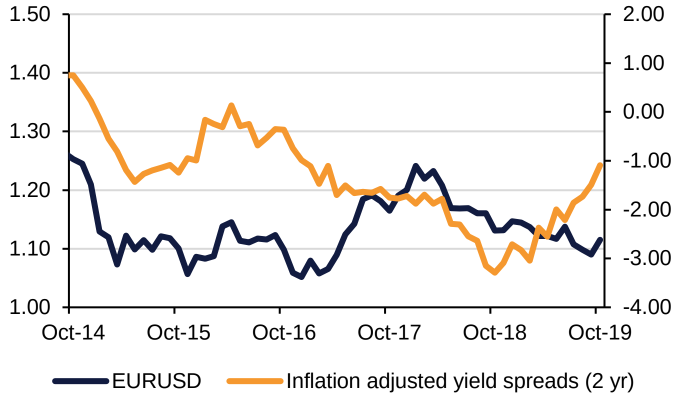
CAD, 2019's outperformer

The Canadian dollar has been the strongest performing major currency in 2019. Over the course of the year, USDCAD has fallen by 2.50% to reach its current levels of 1.3309. There are several catalysts behind the CAD's appreciation. Firstly, having raised interest rates five times (for a total of 125 bps) since 2017, policy makers at the Bank of Canada did not cut interest rates in 2019. This yield benefit has helped the CAD against the other major currencies. Secondly, the cross remains closely correlated with oil prices, which have steadied in the second half of 2019 and have actually posted a modest gain during this period. Thirdly, BOC Governor Stephen Poloz has taken a less dovish tone, which has reduced market expectations from the central bank to loosen monetary policy over the next 12 months.

Mohammed Al Tajir
+9714 609 3005

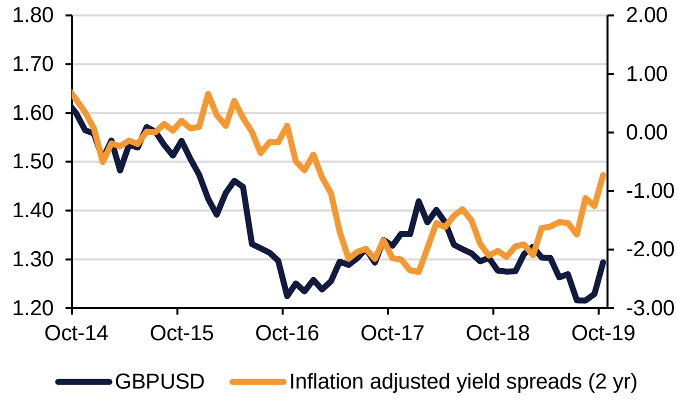
FX–Major Currency Pairs & Real Interest Rates

Interest Rate Differentials–EUR



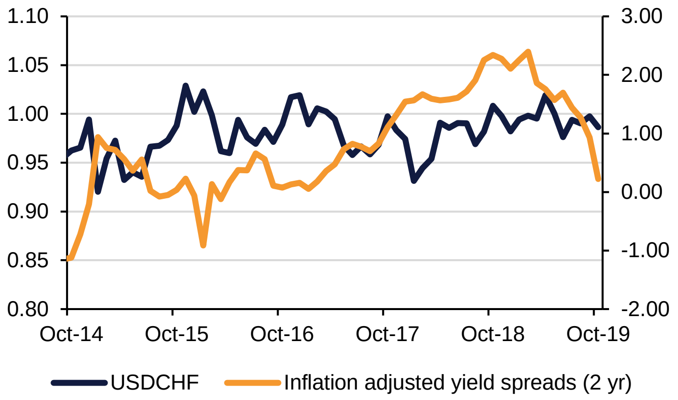
Source: Bloomberg, Emirates NBD Research

Interest Rate Differentials-GBP



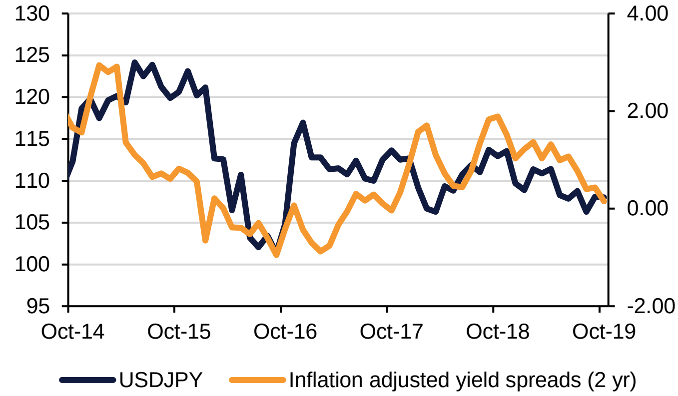
Source: Bloomberg, Emirates NBD Research

Interest Rate Differentials-CHF



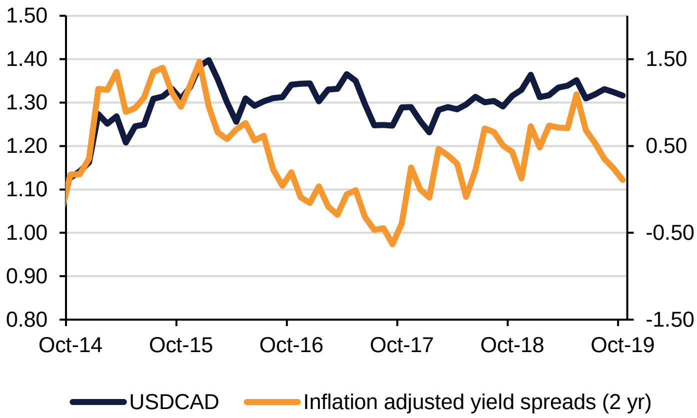
Source: Bloomberg, Emirates NBD Research

Interest Rate Differentials-JPY



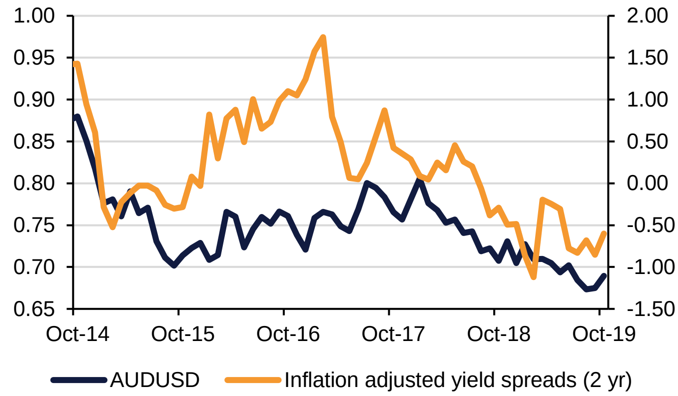
Source: Bloomberg, Emirates NBD Research

Interest Rate Differentials-CAD



Source: Bloomberg, Emirates NBD Research

Interest Rate Differentials-AUD



Source: Bloomberg, Emirates NBD Research

FX Forecasts

FX Forecasts - Major						Forwards		
	26-Nov	Q4 2019	Q1 2020	Q2 2020	Q3 2020	3m	6m	12m
EUR/USD	1.1017	1.1000	1.1200	1.1400	1.1500	1.1086	1.1148	1.1269
USD/JPY	108.96	110.00	110.00	108.00	107.00	108.31	107.74	106.65
USD/CHF	0.9970	0.9700	0.9500	0.9400	0.9300	0.9900	0.9836	0.9713
GBP/USD	1.2855	1.2700	1.3300	1.3600	1.4000	1.2894	1.2926	1.2985
AUD/USD	0.6778	0.7000	0.7100	0.7200	0.7300	0.6794	0.6808	0.6834
NZD/USD	0.6420	0.6300	0.6500	0.6600	0.6700	0.6429	0.6437	0.6449
USD/CAD	1.3313	1.2800	1.2600	1.2400	1.2400	1.3307	1.3305	1.3307
EUR/GBP	0.8570	0.8661	0.8421	0.8382	0.8214	0.8597	0.8624	0.8679
EUR/JPY	120.04	121.00	123.20	123.12	123.05	120.04	120.04	120.04
EUR/CHF	1.0985	1.0670	1.0640	1.0716	1.0695	1.0975	1.0965	1.0947
FX Forecasts - Emerging						**Forwards**		
	26-Nov	Q4 2019	Q1 2020	Q2 2020	Q3 2020	3m	6m	12m
USD/SAR*	3.7501	3.7500	3.7500	3.7500	3.7500	3.7509	3.7516	3.7543
USD/AED*	3.6729	3.6730	3.6730	3.6730	3.6730	3.6744	3.6760	3.6792
USD/KWD	0.3040	0.3020	0.3020	0.3020	0.3020	0.3044	0.3049	--
USD/OMR*	0.3850	0.3850	0.3850	0.3850	0.3850	0.3855	0.3861	0.3883
USD/BHD*	0.3770	0.3770	0.3770	0.3770	0.3770	0.3761	0.3761	0.3779
USD/QAR*	3.6641	3.6400	3.6400	3.6400	3.6400	3.6621	3.6594	3.6538
USD/EGP	16.1036	17.7500	17.7500	17.7500	17.7500	16.5250	16.9150	17.7050
USD/INR	71.536	72.000	71.000	70.000	68.000	72.1900	72.9600	74.4300
USD/CNY	7.0406	7.1000	7.2000	7.2000	7.2000	7.0540	7.0726	7.1106
USD/SGD	1.3662	1.3000	1.2900	1.2900	1.2900	1.3649	1.3631	1.3610

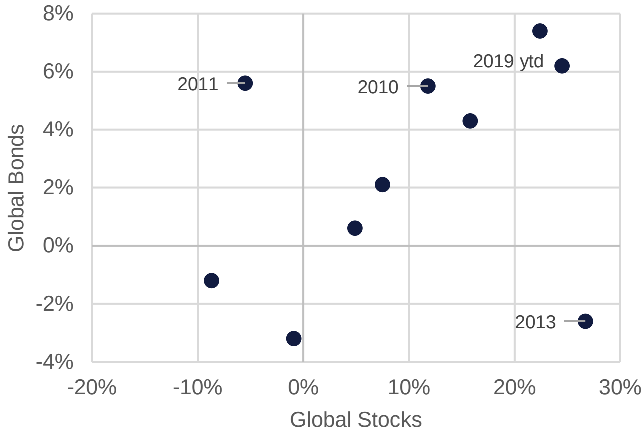
FX Forecasts - MENA					
	26-Nov	Q4 2019	Q1 2020	Q2 2020	Q3 2020
USD/MAD	9.6475	9.7000	9.8500	9.9000	9.9000
USD/TND	2.8510	2.8500	2.8500	2.9000	2.9000
USD/TRY	5.7526	5.8000	6.1000	6.2000	6.2000

Data as of 26 November 2019
Source: Bloomberg, Emirates NBD Research

Financial Markets

The current year, 2019, has been a standout year for most asset classes in financial markets. The combination of resilience and multi-year high returns become even more remarkable when put in context of episodic bouts of economic and geopolitical uncertainty. At the time of this writing, the Bloomberg Barclays Global Aggregate bond index has returned +6.2% ytd and the MSCI World net total return index has delivered +24.1% ytd. In simple words 2019 could be described as year of 'melt-up'.

Performance (2019)



Source: Bloomberg, Emirates NBD Research
Global Stocks refer to MSCI All Country World Total Return Index and Global Bonds refer to Bloomberg Barclays Global Aggregate index

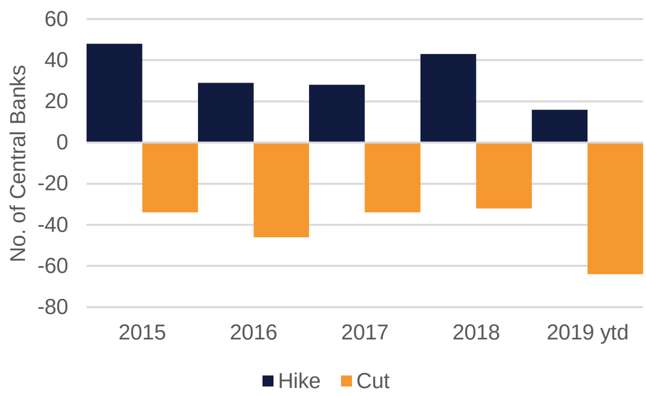
What about 2020?

The performance of financial markets in 2019 was driven by manifestation of slowing economic growth on account of trade conflicts and natural attrition and a dovish shift in global monetary policy. 2020 could well be defined by how these factors play out. Further, the probable crystallization of an unfinished agenda from 2019 (Brexit & Phase 1 trade deal) and challenges of key geopolitical event (US election) would also weigh on financial markets in 2020.

Monetary Policy

Global central banks made a surprise pivot to easy monetary policy at the start of 2019 relative to expectations of tightening. The Federal Reserve, which was projected to tighten interest rates by as much as 100 bps over 2019, actually reduced rates by 75 bps. So far this year, 64 central banks have eased their monetary policy while 16 have tightened their stance out of 494 policy decisions. This is in comparison to 2018 when 43 central banks tightened and 32 eased.

Shift in global monetary policy



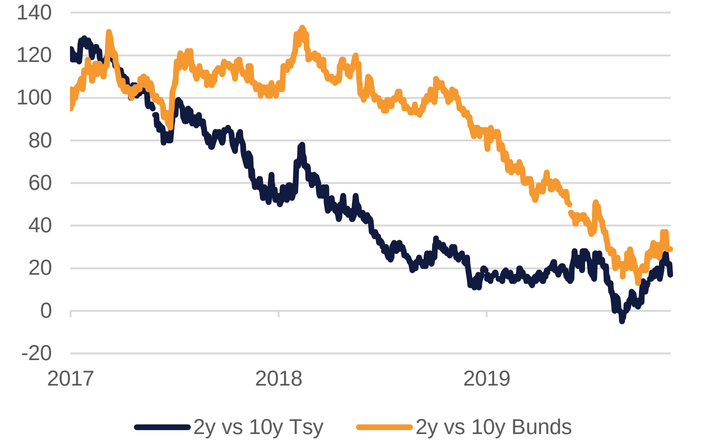
Source: www.centralbanknews.info

However, as the year progressed most central banks started telegraphing the declining efficacy of further easing monetary policy even as they dropped hints of holding back some in preparation of sharper slowdown in economic activity. We expect central banks to move to a more neutral gear in 2020 with most global central banks maintaining a holding pattern at least in first half of next year. Market participants appeared to have grasped the shift as indicated by steepening in developed market sovereign curve.

Having said that, we are likely to see continued divergence between developed market and emerging market policy makers with most EM central banks remaining aggressive in cutting interest rates. The divergence could also extend to style of easing wherein developed market central banks continue to expand balance sheet even as they put interest rates on hold. A considered view would also indicate that inflation could perhaps start weighing on EM rates in the second half of 2020 as aggressive easing in 2019 filters into the real economy and low base effect kicks in. The mitigating view to that theory could be our view that oil prices will continue to remain low in 2020. *(see Oil Outlook 2020)*

The current year, 2019, has been a standout year for most asset classes in financial markets. The combination of resilience and multi-year high returns become even more remarkable when put in context of episodic bouts of economic and geopolitical uncertainty

Developed market sovereign curve steepens



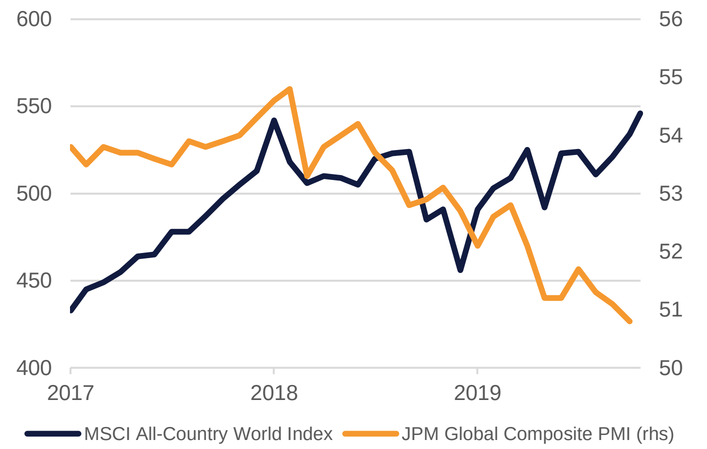
Source: Bloomberg

Overall, monetary policy may not be as much as a support for financial markets in 2020 as they have been in 2019. However, that may not be a bad thing as it would imply that fundamentals of global economy are in better shape than currently expected.

Economic growth

One consistent feature of 2019 was weak economic growth across economies. In fact, most agencies lowered their GDP forecast for 2019 and 2020 as the year progressed. However, what is interesting is that weak economic activity had no impact on financial assets. In fact, for the first time in many years we saw the correlation between growth and return break down with the MSCI All Country Word index trading near 21-month high despite the global composite PMI close to neutral level. The divergence stands out more when considered that the global manufacturing PMI index is actually in contraction territory.

Global equities rallied despite weak economic growth

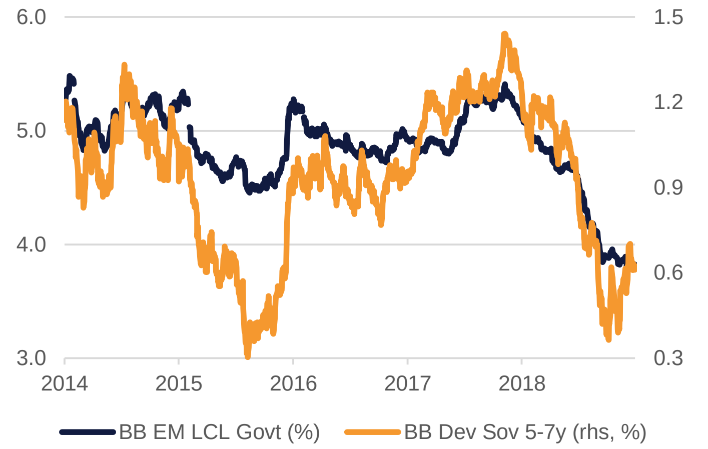


Source: Bloomberg

The natural conclusion which can be drawn is that financial markets will mean-revert to economic activity and hence boosts the case to be defensive. More so when technical factors are fading away, central banks are showing an inclination to stay put and global growth is expected to be the weakest in the current economic cycle in key economies. For example, the US economy is expected to grow at 1.7% in 2020, below the 2.2% average growth in this cycle. It is also worth highlighting that economic activity has a direct impact on corporate earnings which has been declining across economies on a y/y basis. The same when juxtaposed with high valuations reinforces the defensive view. The MSCI World index is currently trading at 16.4x 2020E earnings relative to 10y average of 14.4x.

However, we do not subscribe to the view in its entirety. Primarily because we believe that economies across the world will embark on expansionary fiscal policies. The current state of global economy wherein interest rate are low and inflation benign seems like a perfect launch pad for it to happen. However, we concede that the spending could be gradual and unlike a game-changing move like the tax cuts in the US 2 years ago. There is also a strong case to make that much of fiscal stimulus will happen in silos and not necessarily be coordinated.

Sovereign bond yields at their multi-year lows



Source: Bloomberg

Also, there is some merit to be found in the argument that the monetary policy easing in 2019 will aid economic activity in 2020. Further, we expect central banks to remain pro-active on monetary policy front on thr first instance of weakening economic profile.

Geopolitics

2020 will be punctuated with geopolitical events which include the never-ending Brexit negotiation, multi-phase trade negotiation between the US and China and the US Presidential election. Each of these events has the potential to increase volatility in financial markets. This in our view is the biggest risk to financial market performance next year even after considering the counter argument that much of it is a carryover agenda from 2019. The impact of these events in 2019 could not be sustained over an extended period because of mitigating factors which would be absent in 2020.

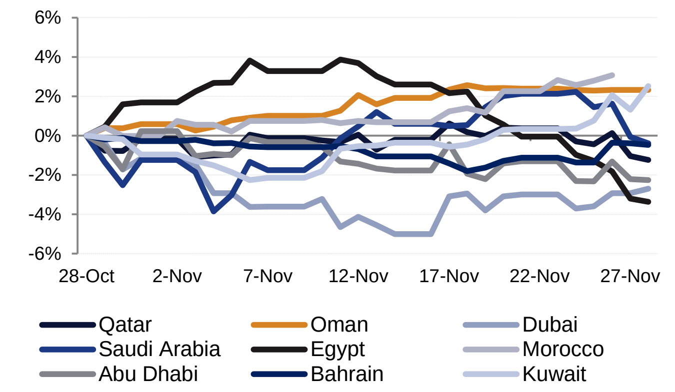
The trade talks between the US and China is the most important one followed by the US Presidential elections. However, both events are interlinked and therein lies the catch. The common refrain in investor mind remains that the President Trump needs a win ahead of election and hence a deal will be reached. The argument is buttressed further as the current US President appears to benchmarks his performance with financial market returns and hence is unlikely to allow markets to underperform ahead of election. If 2019 is any guide then these arguments do hold ground and could well be a key factor next year. However, as 2020 progresses, it is likely that the focus will shift to his opponent and his ability to get re-elected and that could ensue heightened volatility in financial markets. Needless to add that a failure to reach a Phase 1 deal with China which includes partial roll-back tariffs will be a worst-case scenario for global financial markets.

Much of the impact of Brexit has already been flagged multiple times last year. None of those have changed. However, it can be said that longer the negotiations last, the more durable the impact will be. Hence the need for the new government to expedite the same one way or the other. The impact of Brexit is likely to be limited to EU and UK equities unless there is no-deal exit. We expect the Brexit hangover to be more dominant in the first half next year and get diluted thereafter.

Aditya Pugalia
+9714 609 3027

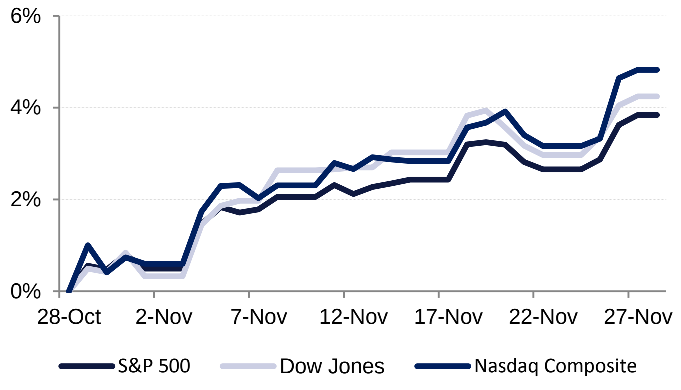
Major Equity Markets

MENA Equity Markets



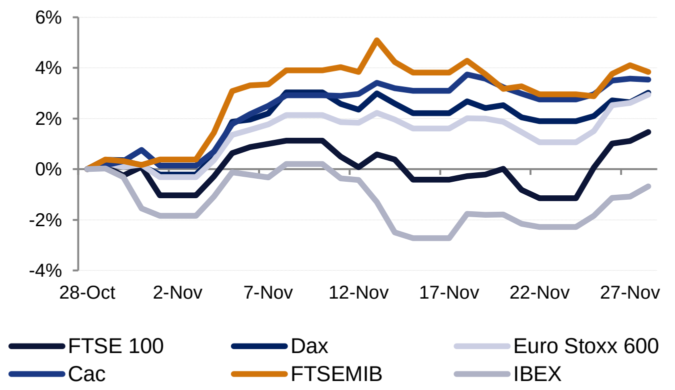
Source: Bloomberg, Emirates NBD Research

US Equity Markets



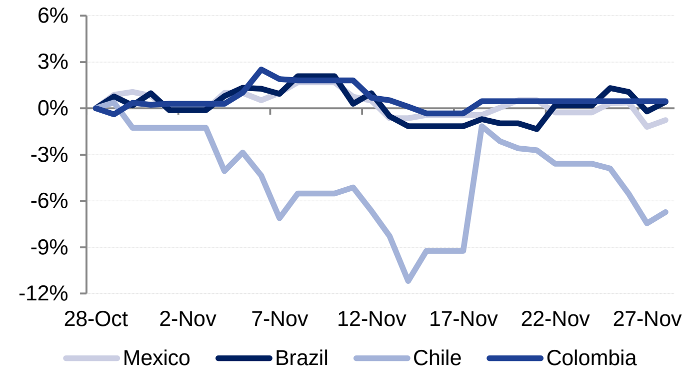
Source: Bloomberg, Emirates NBD Research

European Equity Markets



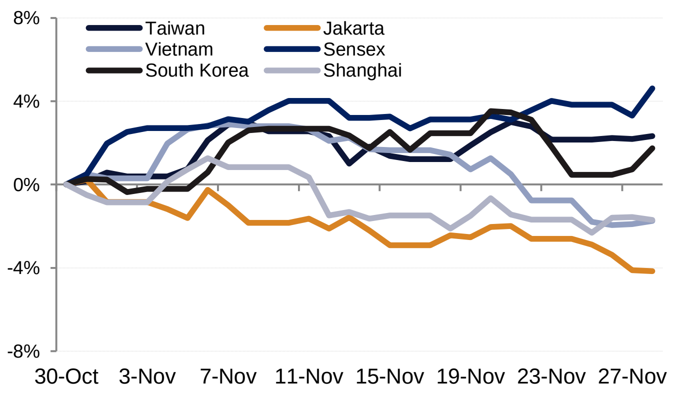
Source: Bloomberg, Emirates NBD Research

Latin American Equity Markets



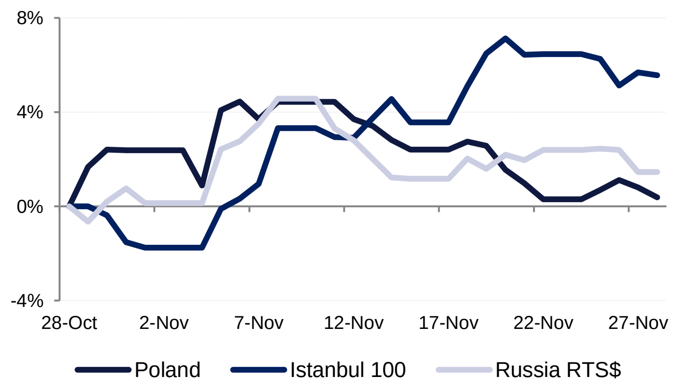
Source: Bloomberg, Emirates NBD Research

Asian Emerging Equity Markets



Source: Bloomberg, Emirates NBD Research

Emerging Europe Equity Markets



Source: Bloomberg, Emirates NBD Research

Interest Rate Forecasts

US Treasuries Forecasts							
	Current	3M	6M	12M			
2y	1.62	1.65	1.75	1.80			
10y	1.76	1.90	2.00	2.00			
2s10s (bp)	14	15	25	20			
3M Libor							
3m	1.91	2.00	2.00	1.85			
3M Eibor							
3m	2.17	2.25	2.25	2.00			
Policy Rate Forecasts							
	Current %	3M	6M	12M			
FED (Upper Band)	1.75	1.75	1.50	1.50			
ECB (deposit rate)	-0.50	-0.50	-0.50	-0.50			
BoE	0.75	0.75	0.75	0.75			
BoJ	-0.10	-0.10	-0.10	-0.10			
SNB	-0.75	-0.75	-0.75	-0.75			
RBA	0.75	0.75	0.50	0.50			
RBI (repo)	5.15	4.90	4.90	4.90			
SAMA (reverse repo)	2.00	1.75	1.50	1.50			
UAE (Repo rate)	2.25	2.00	1.75	1.75			
CBK (o/n repo rate)	2.50	2.50	2.50	2.50			
CBB (o/n depo)	2.00	1.75	1.50	1.50			
CBO (o/n repo)	2.77	2.52	2.52	2.25			
CBE (o/n depo)	13.25	11.25	10.25	9.25			

Source: Bloomberg, Emirates NBD Research
As at 28 November 2019

Commodities

As we look ahead to 2020 we outline some of the factors we think will push and pull commodity markets in varying directions over the year. Some variables will be, unfortunately, familiar such as the US-China trade war while others will be pronounced by their relative absence, the minimal impact we expect from central banks for instance. But new dynamics such as mounting social pressure on resource companies to operate on a more sustainable basis will grow in importance and present new challenges for commodity markets.

US-China trade relations remain rancorous

The trade standoff between the US and China will remain a spectre haunting commodity markets in 2020. False dawns on negotiations, acrimonious tit for tat tariffs and trade brinksmanship set the tone for much of 2019 and we don't expect to see much improvement in relations in 2020. Neither China nor the US appears willing to make concessions on the critical barriers to an all encompassing deal, such as an end to Chinese government support for industry or the removal of US tariffs, effectively cementing the trade war in place. The 'phase 1' deal under consideration is modest in scope and unlikely to significantly affect commodity demand, whether in China, the US or other economies caught in the cross-fire.

Beyond the specifics of US-China trade flows, bilateral relations between both countries are fraught, compounded most recently by the US Senate affirming symbolic support with protesters in Hong Kong. Moreover, were President Trump to lose the 2020 election to a Democrat we see little chance any of the current candidates would be more accommodative on China trade issues, risking relations deteriorating further.

Base metals respond to trade disputes

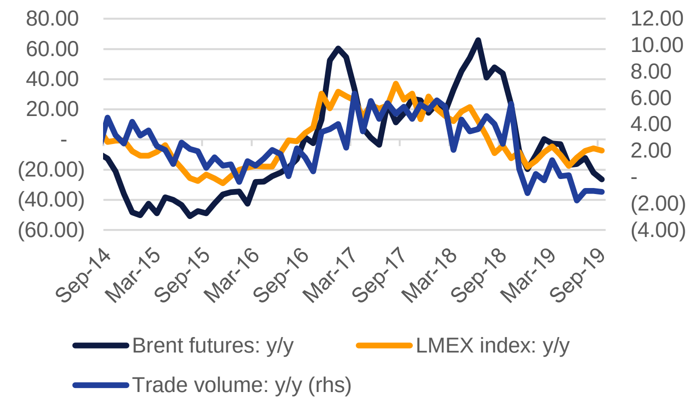
Source: Bloomberg, Emirates NBD Research. Jan 1 2019 = 100.

The back and forth in trade relations has hit nearly all commodity markets and the LMEX index of base metals neatly presents changes in the tenor of trade talks. The index soared in Q1 as markets priced in the prospect of a trade agreement being reached only for the index to slump in Q2 as new tariff rates were introduced. Prices have failed to recoup their Q1 gains and have instead displayed a high beta to the dynamics of trade talks, even as underlying metal market fundamentals may be more supportive.

Contraction in trade and industry

Beyond only affecting sentiment, the introduction of trade barriers by both the US and China has contributed to a slowdown in the volume of global trade. Volume of trade in manufactured goods has declined by an average of 0.4% y/y in the first nine months of the year, its weakest performance since the global financial crisis. Trade has bumped around at 0 growth several times in the past few years—notably 2015 to early 2016—but that period was hardly glorious for commodity prices: Brent futures were in free fall while metals prices hit multi-year lows.

Weak trade, weak prices



Source: Bloomberg, Emirates NBD Research.

Fewer goods many be crossing borders as a result of trade barriers but also because fewer goods are being made. Industry globally appears to be flat or in recession. Emerging market conditions began to soften from the start of 2018 as the China-US trade war ratcheted up but domestic factors have been underperforming too. China's fixed asset investment is growing at essentially its slowest pace on record while industrial production in India has fallen to global financial crisis levels as the economy endures a slump. In both countries, vehicle sales are also in a sharp decline from recent levels.

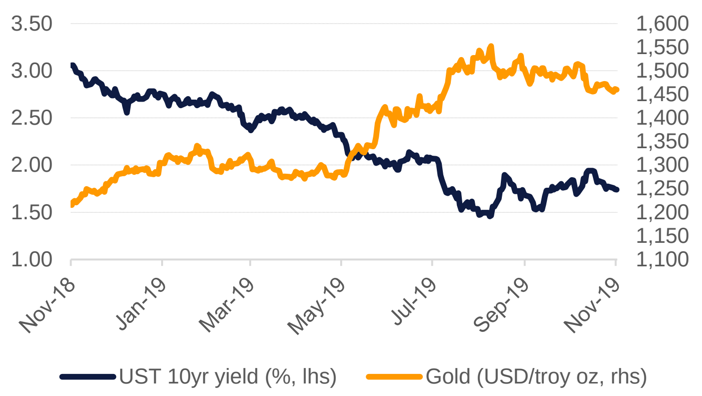
Meanwhile, developed markets have caught up with the slump in emerging economies, with manufacturing PMIs across the developed world below 50 for most of 2019 while business confidence in key markets is plummeting. We expect growth in most major economies to slow or at best flatten in 2020, keeping many of these negative trends for industry intact (see macro section above).

FX and rates to stand aside

Monetary policy is unlikely to have a significant direct impact on commodity markets in 2020. We expect the US Federal Reserve to hold rates steady for much of next year, with an additional cut of 25bps in reserve if conditions in the economy warrant it (a severe drop in employment for instance or weakness in the consumer sector). As a result we don't expect to see a substantial gain in the dollar that would act as a headwind to commodity prices. Additionally we expect a relatively modest gain in the rates market. Over the next 12 months we anticipate yields on 10yr USTs to gain by around 25bps from current levels of roughly 1.75%. That compares with a drop of around 130bps from year ago levels to the time of publication.

FX and rates markets exert the most direct impact on precious metals prices but we expect gold to be relatively steady in 2020 as rates stay on hold. Gold often benefits from uncertainty in financial markets but in 2020 the variables affecting uncertainty—US trade policy, rate decisions, global growth conditions—are so well known that a new 'uncertain' uncertainty will need to hit markets to shift gold prices out of their current range.

Rates and gold to find new partners



Source: Bloomberg, Emirates NBD Research.

Social unrest facing producers and consumers

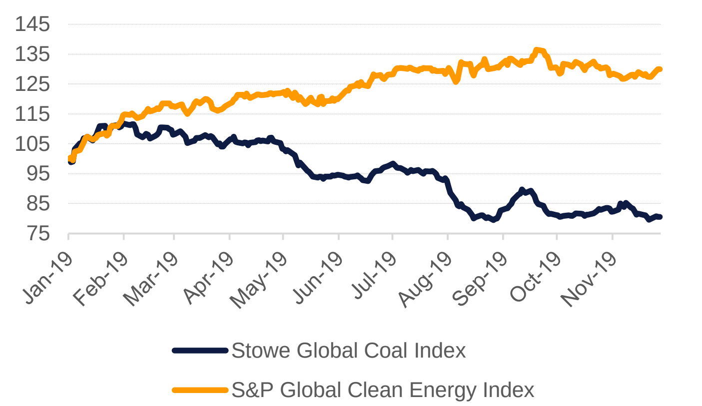
Social unrest spread widely in 2019, affecting Hong Kong, Lebanon, Barcelona, Sudan among others. The impact on economic growth has largely been localized to the countries or regions enduring the unrest, not posing a general threat to global growth or flows of commodities. But several key producing countries find themselves in the throes of significant social and political pressures.

For oil markets, Iraq's government has been under assault from street protesters demanding an end to corruption and inefficient services. So far there has not been a significant disruption to oil production or exports but there have been protests close to Iraq's southern ports that could interrupt oil flows. In Iran, major street protests have erupted in response to changes in fuel pricing while Algeria remains without a clear political trajectory following the resignation of long-serving president Abdelaziz Bouteflika in April. Outside of the Middle East, Ecuador, a small oil producer, also endured significant anti-austerity protests this year. While there has been little direct impact on oil markets in terms of volumes as a result of these protests, and there origins are highly varied, the threat of social unrest will keep geopolitical concerns even more front of mind for oil markets in 2020.

But it's not just oil exporters that are under significant social strain. In Chile, protests over the rising cost of living and inequality threaten the world's largest source of mined copper. Some mining companies in the country have reported reduced operations as union workers strike in solidarity with protesters while ports represent an acute point of sensitivity in maintaining flows of metal out of the country. Elsewhere, the possible independence of Bougainville, an island part of Papua New Guinea, sets an uncertain outlook for the restart of one of the world's largest copper mines.

Outside of commodity producers, climate change activists will continue to mount pressure on resource companies—whether oil and gas, utilities or metals and mining—and the financial services that support them. We expect messaging from resource company executives to keep highlighting their ESG achievements as they try and maintain a social license to operate from customers, protesters and governments.

Clean energy vs coal



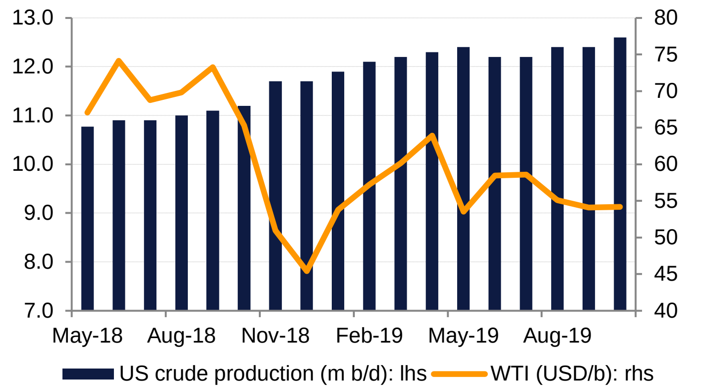
Source: Bloomberg, Emirates NBD Research. Note: Jan 1 2019 = 100

These social factors will be difficult for commodity markets to "hedge" but markets may do some of the adjustment that activists are calling for. For example, natural gas prices are converging in most regions on coal prices, allowing the cleaner burning fuel to displace coal while restrictions on financing fossil fuel projects are gathering pace, particularly in Europe. To be clear, oil, coal and gas will continue to dominate the world's energy mix next year, and probably the year after that too. But incorporating social and environmental pressures into the balance of forces that influence commodity markets will be of increasing necessity.

Edward Bell
+971 4609 3055

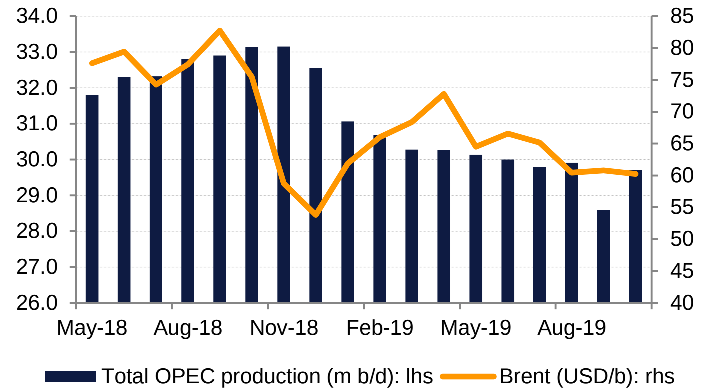
Major Commodities Markets

US oil production and price



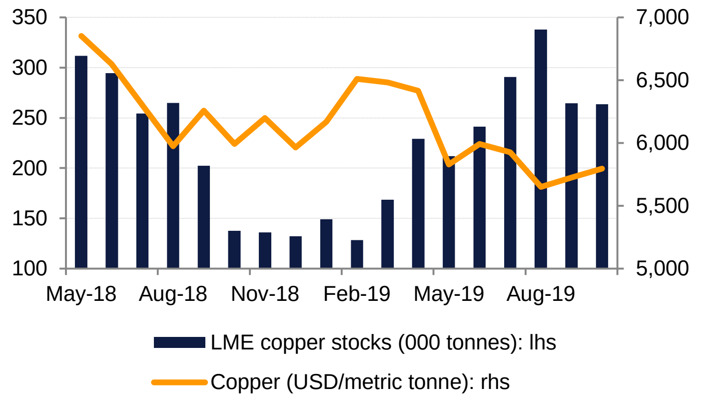
Source: EIKON, Emirates NBD Research

International oil production and price



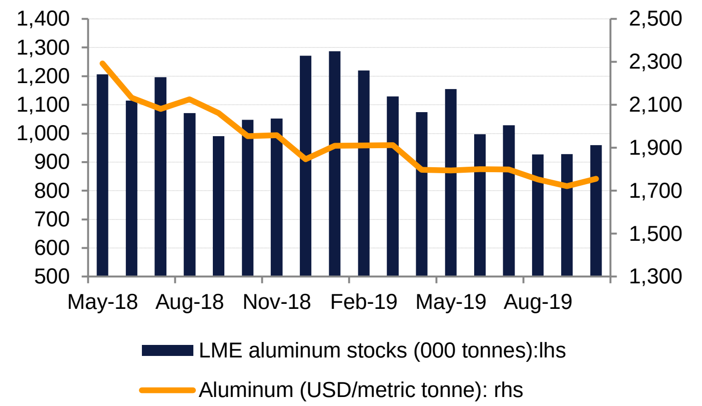
Source: EIKON, Emirates NBD Research

Copper stocks and price



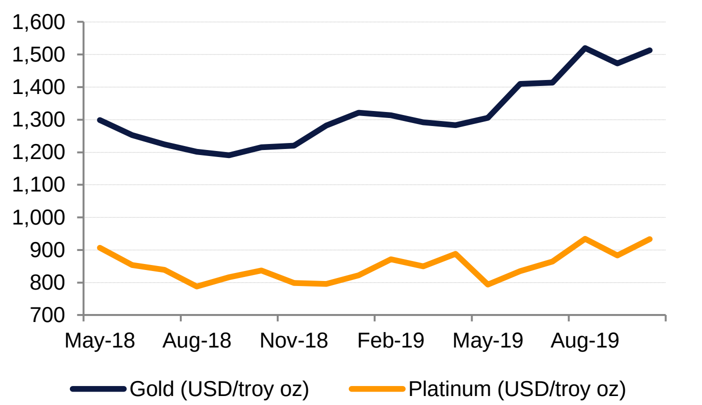
Source: EIKON, Emirates NBD Research

Aluminum stocks and price



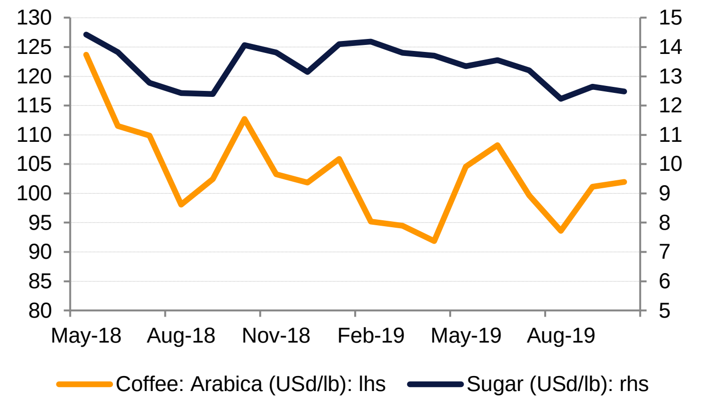
Source: EIKON, Emirates NBD Research

Precious metals prices



Source: EIKON, Emirates NBD Research

Agriculture prices



Source: EIKON, Emirates NBD Research

Commodity Forecasts

Global commodity prices							
	Last	2019Q4	2020Q1	Q2	Q3	2019	2020
Energy							
WTI	57.85	55.00	52.00	55.00	56.50	57.81	54.63
Brent	63.88	58.00	55.00	57.50	58.00	64.33	57.13
Precious metals							
Gold	1,456.78	1,450.00	1,475.00	1,450.00	1,450.00	1,384.00	1,456.25
Silver	17.00	17.00	16.50	16.00	15.75	16.11	16.31
Platinum	894.06	1,000.00	900.00	950.00	975.00	872.59	956.25
Palladium	1,829.08	1,650.00	1,600.00	1,550.00	1,500.00	1,522.75	1,575.00
Base metals							
Aluminum	1,764.00	1,800.00	1,850.00	1,900.00	1,950.00	1,816.95	1,875.00
Copper	5,945.00	6,000.00	5,800.00	5,750.00	5,750.00	6,044.30	5,825.00
Lead	1,943.00	2,084.79	2,023.64	2,008.29	2,008.29	2,014.47	2,031.25
Nickel	14,380.00	17,500.00	16,000.00	15,000.00	14,500.00	14,457.82	15,750.00
Tin	16,400.00	16,500.00	17,000.00	17,750.00	18,000.00	18,688.90	17,312.50
Zinc	2,297.00	2,405.13	2,338.59	2,321.85	2,321.85	2,520.74	2,346.86
Iron ore	84.75	90.00	85.00	75.00	70.00	93.32	80.00

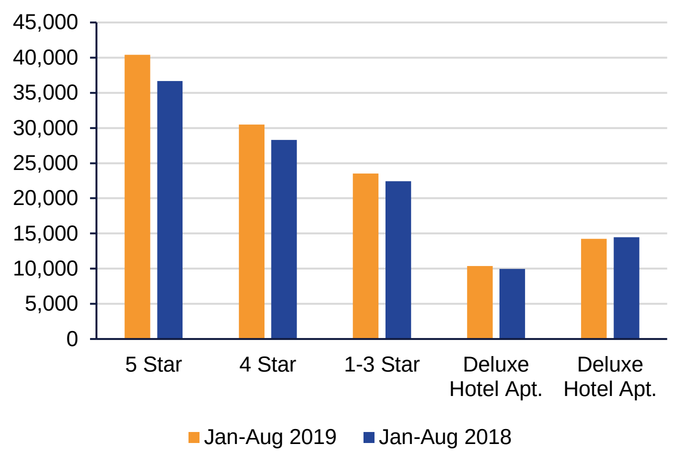
Prices as of 28 November 2019. Note: prices are average of time period unless indicated otherwise.
Source: EIKON, Emirates NBD Research

Sector Report

Dubai's tourism sector picks up in 2019

In the first half of 2019 Dubai's hospitality and tourism sector saw growth of 2.7%, which chimes with the tourism figures released for the year to September, reflecting that international visitor numbers to Dubai grew 4.3% y/y in an improvement on the fractional growth recorded in the same period last year. While India remains the largest source market, visitor numbers from there have declined by more than -5% in the first nine months of this year. Average occupancy for the hotel sector stood at 73%, with establishments registering 23.12 million occupied room nights during that nine month period.

Hotel room supply by type

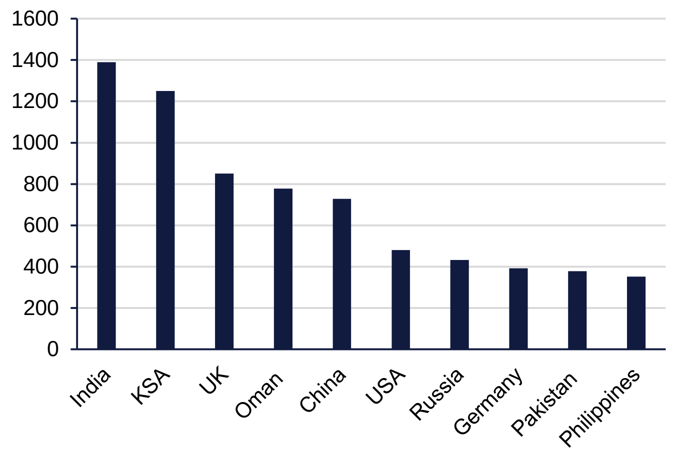


Source: DTCM

Where growth in India has slowed down, that has been somewhat offset by increased numbers of visitors from Saudi Arabia, Oman and China. The number of visitors from Saudi Arabia grew 2% y/y to 1.25 million, making it the second-largest source market. Oman ranked fourth as the number of visitors from there jumped 28% to 778,000, while the arrivals from China ranking fifth increased 14% to 729,000. While the United Kingdom remains the 3rd biggest market of tourists, the numbers from there also dropped 2%, to 851,000.

Smaller markets that reported strong double digit growth were the Philippines (up 29% to 352,000), Nigeria (34% to 168,000) and Kazakhstan (24% to 106,000). Other Markets including The United States, Germany and Pakistan retained their positions in the top 10. An official from Dubai Tourism commented "As we head into 2020, our efforts will remain focused on attracting new, first-time and repeat visitors from emerging, as well as established markets.

Visitors by country 000's (Jan-Sep 2019)

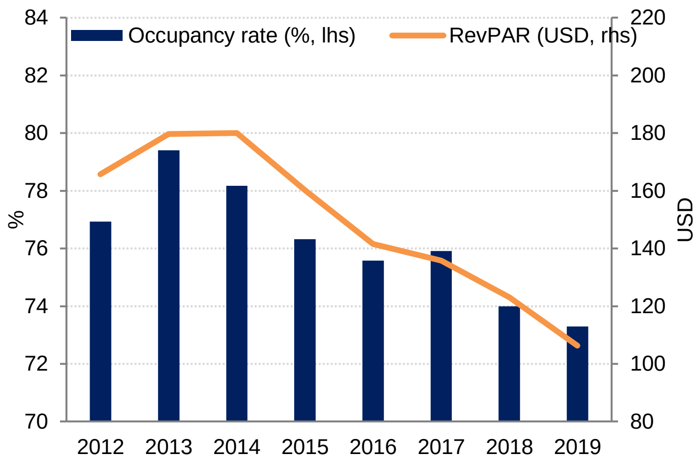


Source: DTCM

Strategies to attract growth

Dubai has been working on specific strategies to attract growth from new markets. For example to attract more tourists from China the government developed a four tier approach: (i) regulatory changes such as granting Chinese citizens free visa-on-arrival access to the UAE, (ii) programs aimed at retaining relevance and attractiveness for this market through platform-based awareness programs, (iii) using social and digital ecosystem tailored trip-planning (iv) in-city experiences through its 'China Readiness' initiative aimed at offering Chinese visitors experiences across all tourism touchpoints.

Revenue per room vs Occupany rate



Source: STR Global, Emirates NBD Research

Furthermore Dubai has worked on a number of destination-focused campaigns and strategy initiatives across it's global source markets through a combination of customised programmes, stakeholder and trade partnerships.The campaigns reflect a strategy by the Dubai government to actively deepen its key source markets while broadening supply from new geographies. In addition to attracting growth from those new markets, it picks up slack from some of the larger source markets, and reflects a healthy diversification.

Building up to Expo 2020

Dubai's supply of new hotel rooms kept on rising in the run-up to Expo 2020, which is targeted to bring 25 million visitors to the emirate over a six-month period, reaching to 119,779 available rooms in the emirate as of September 2019, a 7% increase over the same period last year. The increase in hotel room supply in the run up to Expo 2020 has been applying downward pressure on room pricing. However we expect this margin pressure to ease as demand grows during the Expo 2020, and as Dubai continues to work towards boosting long term in bound tourism numbers.

Shady Elborno
+971 4609 3015

Disclaimer

PLEASE READ THE FOLLOWING TERMS AND CONDITIONS OF ACCESS FOR THE PUBLICATION BEFORE THE USE THEREOF. By continuing to access and use the publication, you signify you accept these terms and conditions. Emirates NBD reserves the right to amend, remove, or add to the publication and Disclaimer at any time. Such modifications shall be effective immediately. Accordingly, please continue to review this Disclaimer whenever accessing, or using the publication. Your access of, and use of the publication, after modifications to the Disclaimer will constitute your acceptance of the terms and conditions of use of the publication, as modified. If, at any time, you do not wish to accept the content of this Disclaimer, you may not access, or use the publication. Any terms and conditions proposed by you which are in addition to or which conflict with this Disclaimer are expressly rejected by Emirates NBD and shall be of no force or effect. Information contained herein is believed by Emirates NBD to be accurate and true but Emirates NBD expresses no representation or warranty of such accuracy 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 the publication. The publication is provided for informational uses only and is not intended for trading purposes. Charts, graphs and related data/information provided herein are intended to serve for illustrative purposes. The data/information contained in the publication is not designed to initiate or conclude any transaction. In addition, the data/information contained in the publication 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. The publication may include data/information taken from stock exchanges and other sources from around the world and Emirates NBD does not guarantee the sequence, accuracy, completeness, or timeliness of information contained in the publication provided thereto by or obtained from unaffiliated third parties. Moreover, the provision of certain data/information in the publication may be subject to the terms and conditions of other agreements to which Emirates NBD is a party.

None of the content in the publication constitutes a solicitation, offer or recommendation by Emirates NBD to buy or sell any security, or represents the provision by Emirates NBD of investment advice or services regarding the profitability or suitability of any security or investment. Moreover, the content of the publication should not be considered legal, tax, accounting advice. The publication is not intended for use by, or distribution to, any person or entity in any jurisdiction or country where such use or distribution would be contrary to law or regulation. Accordingly, anything to the contrary herein set forth notwithstanding, Emirates NBD, its suppliers, agents, directors, officers, employees, representatives, successors, assigns, affiliates or subsidiaries shall not, directly or indirectly, be liable, in any way, to you or any other person for any: (a) inaccuracies or errors in or omissions from the publication including, but not limited to, quotes and financial data; (b) loss or damage arising from the use of the publication, including, but not limited to any investment decision occasioned thereby. (c) UNDER NO CIRCUMSTANCES, INCLUDING BUT NOT LIMITED TO NEGLIGENCE, SHALL EMIRATES NBD, ITS SUPPLIERS, AGENTS, DIRECTORS, OFFICERS, EMPLOYEES, REPRESENTATIVES, SUCCESSORS, ASSIGNS, AFFILIATES OR SUBSIDIARIES BE LIABLE TO YOU FOR DIRECT, INDIRECT, INCIDENTAL, CONSEQUENTIAL, SPECIAL, PUNITIVE, OR EXEMPLARY DAMAGES EVEN IF EMIRATES NBD HAS BEEN ADVISED SPECIFICALLY OF THE POSSIBILITY OF SUCH DAMAGES, ARISING FROM THE USE OF THE PUBLICATION, INCLUDING BUT NOT LIMITED TO, LOSS OF REVENUE, OPPORTUNITY, OR ANTICIPATED PROFITS OR LOST BUSINESS. The information contained in the publication does not purport to contain all matters relevant to any particular investment or financial instrument and all statements as to future matters are not guaranteed to be accurate. Anyone proposing to rely on or use the information contained in the publication 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 the publication. Further, references to any financial instrument or investment product is not intended to imply that an actual trading market exists for such instrument or product. In publishing this document Emirates NBD is not acting in the capacity of a fiduciary or financial advisor.

Emirates NBD and its group entities (together and separately, "Emirates NBD") does and may at any time solicit or provide commercial banking, investment banking, credit, advisory or other services to the companies covered in its reports. As a result, recipients of this report should be aware that any or all of the foregoing services may at times give rise to a conflict of interest that could affect the objectivity of this report.

The securities covered by this report may not be suitable for all types of investors. The report does not take into account the investment objectives, financial situations and specific needs of recipients.

Data included in the publication may rely on models that do not reflect or take into account all potentially significant factors such as market risk, liquidity risk and credit risk. Emirates NBD may use different models, make valuation adjustments, or use different methodologies when determining prices at which Emirates NBD is willing to trade financial instruments and/or when valuing its own inventory positions for its books and records. In receiving the publication, you acknowledge and agree that there are risks associated with investment activities. Moreover, you acknowledge in receiving the publication that the responsibility to obtain and carefully read and understand the content of documents relating to any investment activity described in the publication and to seek separate, independent financial advice if required to assess whether a particular investment activity described herein is suitable, lies exclusively with you. You acknowledge and agree that past investment performance is not indicative of the future performance results of any investment and that the information contained herein is not to be used as an indication for the future performance of any investment activity. You acknowledge that the publication has been developed, compiled, prepared, revised, selected, and arranged by Emirates NBD and others (including certain other information sources) through the application of methods and standards of judgment developed and applied through the expenditure of substantial time, effort, and money and constitutes valuable intellectual property of Emirates NBD and such others. All present and future rights in and to trade secrets, patents, copyrights, trademarks, service marks, know-how, and other proprietary rights of any type under the laws of any governmental authority, domestic or foreign, shall, as between you and Emirates NBD, at all times be and remain the sole and exclusive property of Emirates NBD and/or other lawful parties. Except as specifically permitted in writing, you acknowledge and agree that you may not copy or make any use of the content of the publication or any portion thereof. Except as specifically permitted in writing, you shall not use the intellectual property rights connected with the publication, or the names of any individual participant in, or contributor to, the content of the publication, or any variations or derivatives thereof, for any purpose.

YOU AGREE TO USE THE PUBLICATION SOLELY FOR YOUR OWN NONCOMMERCIAL USE AND BENEFIT, AND NOT FOR RESALE OR OTHER TRANSFER OR DISPOSITION TO, OR USE BY OR FOR THE BENEFIT OF, ANY OTHER PERSON OR ENTITY. YOU AGREE NOT TO USE, TRANSFER, DISTRIBUTE, OR DISPOSE OF ANY DATA/INFORMATION CONTAINED IN THE PUBLICATION IN ANY MANNER THAT COULD COMPETE WITH THE BUSINESS INTERESTS OF EMIRATES NBD. YOU MAY NOT COPY, REPRODUCE, PUBLISH, DISPLAY, MODIFY, OR CREATE DERIVATIVE WORKS FROM ANY DATA/INFORMATION CONTAINED IN THE PUBLICATION. YOU MAY NOT OFFER ANY PART OF THE PUBLICATION FOR SALE OR DISTRIBUTE IT OVER ANY MEDIUM WITHOUT THE PRIOR WRITTEN CONSENT OF EMIRATES NBD. THE DATA/INFORMATION CONTAINED IN THE PUBLICATION MAY NOT BE USED TO CONSTRUCT A DATABASE OF ANY KIND. YOU MAY NOT USE THE DATA/INFORMATION IN THE PUBLICATION IN ANY WAY TO IMPROVE THE QUALITY OF ANY DATA SOLD OR CONTRIBUTED TO BY YOU TO ANY THIRD PARTY. FURTHERMORE, YOU MAY NOT USE ANY OF THE TRADEMARKS, TRADE NAMES, SERVICE MARKS, COPYRIGHTS, OR LOGOS OF EMIRATES NBD OR ITS SUBSIDIARIES IN ANY MANNER WHICH CREATES THE IMPRESSION THAT SUCH ITEMS BELONG TO OR ARE ASSOCIATED WITH YOU OR, EXCEPT AS OTHERWISE PROVIDED WITH EMIRATES NBD'S PRIOR WRITTEN CONSENT, AND YOU ACKNOWLEDGE THAT YOU HAVE NO OWNERSHIP RIGHTS IN AND TO ANY OF SUCH ITEMS. MOREOVER YOU AGREE THAT YOUR USE OF THE PUBLICATION IS AT YOUR SOLE RISK AND ACKNOWLEDGE THAT THE PUBLICATION AND ANYTHING CONTAINED HEREIN, IS PROVIDED "AS IS" AND "AS AVAILABLE," AND THAT EMIRATES NBD MAKES NO WARRANTY OF ANY KIND, EXPRESS OR IMPLIED, AS TO THE PUBLICATION, INCLUDING, BUT NOT LIMITED TO, MERCHANTABILITY, NON-INFRINGEMENT, TITLE, OR FITNESS FOR A PARTICULAR PURPOSE OR USE. You agree, at your own expense, to indemnify, defend and hold harmless Emirates NBD, its Suppliers, agents, directors, officers, employees, representatives, successors, and assigns from and against any and all claims, damages, liabilities, costs, and expenses, including reasonable attorneys' and experts' fees, arising out of or in connection with the publication, including, but not limited to: (i) your use of the data contained in the publication or someone using such data on your behalf; (ii) any deletions, additions, insertions or alterations to, or any unauthorized use of, the data contained in the publication or (iii) any misrepresentation or breach of an acknowledgement or agreement made as a result of your receiving the publication.

Emirates NBD Research Team

Tim Fox
Head of Research & Chief Economist
+9714 230 7800
timothyf@emiratesnbd.com

Khatija Haque
Head of MENA Research
+9714 230 7803
khatijah@emiratesnbd.com

Shady Shaher Elborno
Head of Macro Strategy
+9714 609 3015
shadyb@emiratesnbd.com

Mohammed Altajir
FX Analytics and Product Development
+9714 609 3005
mohammedtaj@emiratesnbd.com

Edward Bell
Commodity Analyst
+9714 230 7701
edwardpb@emiratesnbd.com

Aditya Pugalia
Director, Financial Markets Research
+9714 609 3027
adityap@emiratesnbd.com

Daniel Richards
MENA Economist
+9714 609 3032
danielricha@emiratesnbd.com

Other key contacts

Group Head – Treasury Sales
Tariq Chaudhary
+971 4 230 7777
tariqmc@emiratesnbd.com

Investor Relations
Patrick Clerkin
+9714 230 7805
patricke@emiratesnbd.com

Group Corporate Affairs
Ibrahim Sowaidan
+9714 609 4113
ibrahims@emiratesnbd.com