Issue : 3

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ECES
The Egyptian Center for Economic Studies

Our Economy & the World

This week's issue of "Our Economy and the World" includes:

- **An analysis of global financial market performance and changes in commodity prices**
- **Key global developments in the past week**
- **Overview from the international press about what the future holds for "OPEC" after five decades of influencing the oil market**
- **Special analysis about differences of opinions of G-20 members yielding disappointing results**
- **Weekly commentary about Egypt's participation in the G-20 meetings**

Global Market Performance

Reuters - Argaam - news agencies:

Chinese stocks rose at the end of Friday trading session, recording their best weekly gains this year. The rise was supported by speculations of further government stimulus for the economy. Chinese stocks recorded gains for the fourth session in a row, after a sharp decline exceeding over 4.6 percent last Monday, supported by investor expectations for another intervention by the Chinese government to support the economy.

The "Shanghai" Composite Index rose by 0.5 percent to close at 2874 points, up by about 3.9 percent this week.

Japanese stocks rose for the fourth session in a row at the end of Friday trading, recording weekly gains, supported by the rise in oil prices, and anticipation of global economic data. Also, the Japanese "Nikki" index rose by 0.3 percent to 17014 points, recording weekly gains of about 5 percent. The "TOPIX" index rose by about 0.5 percent to 1375 points.

European stock indices also rose during Friday trading, backed by the US monthly jobs report and the rise in oil prices, which positively affected the performance of the energy sector. At the end of the session, the "Stoxx Europe 600" benchmark rose by 0.7 percent or by 2.4 points to 341.8 points, recording weekly gains of 3.1 percent.

The British "FTSE 100" index also rose by +67 points to 6199 points. The French "CAC" index rose by 40.5 points to 4456.6 points. The German "DAX" index rose by +72 points to 9824 points, and the "FTSEurofirst" 300 of major European company stocks rose by 0.7 percent to close at 1344.62 points, recording its third weekly gain in a row.

The US stocks rose during Friday trading after release of the monthly jobs report and the rise in oil prices, positively affecting the performance of the energy sector. Major indices also recorded gains for the third

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week in a row. The industrial index "Dow Jones" increased by 62.8 points to 17,006.7 points. The "NASDAQ" index rose by +9.6 points to 4717 points. The "S & P 500" benchmark index rose by 6.59 points to 1999.9 points.

Additionally, gold futures for April delivery rose at settlement by 1 percent or by $12.50 to $1270.70 an ounce, which is the highest closing since February 2nd, 2015. The yellow metal recorded weekly gains of 4.1 percent.

In oil markets, the US "NYMEX" jumped 3.9 percent, or by $1.35, and closed at $35.92 a barrel, which is the highest closing since January 5th, recording weekly gains of 9.5 percent. The "Brent" benchmark index rose by 4.5 percent or by $1.65, closing at $38.72 a barrel, which is the highest closing level since last December 10th, recording weekly gains of 9.3 percent.

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Key Global Developments

Moody's Downgrades China's Credit Outlook to "Negative"

Beijing (DPA): Moody's downgraded China's credit outlook from "stable" to "negative" in light of concerns about the slowing down of the second largest economy in the world. Moody's attributed the downgrade to rising government debts, falling reserves and uncertainty about the authorities' ability to implement reforms. It is noteworthy that Chinese government debts rose to 40.6 percent of GDP at the end of 2015, compared to 32.5 percent in 2012, according to Moody's estimates. Moody's expects debts to rise to 43 percent of GDP by 2017.

Iran Complains about Oil Export Restrictions ... and Increases Production by 400,000 Barrels!

Dubai, Tehran, Reuters, AFP: While Iran is still complaining about oil export restrictions, Iranian Oil Minister Bijan Zangeneh declared that Iran's oil exports rose by 400,000 barrels per day during the month of Bahman (January 21-February 19). He told the media that total oil exports and derivatives reached 1.75 million barrels a day during the month of Bahman. He explained that this represented an increase of 400,000 barrels per day compared to the same period last year. Iran's oil production, which was slightly over 2.8 million barrels per day, exceeded 3.2 million barrels. The entire surplus in production went to exports.

Sovereign Funds Sold Stocks on a Large Scale in 2015

London – Reuters: New data showed that the sales by sovereign wealth funds of assets worth $46.4 billion in 2015 included intensive exits by inactive investments that track stock indices in both developed and emerging markets. After last week's report, which included a total value of exits of $46.4 billion, E-vestment Research revealed more details this week, noting that sales were focused on stocks, and were significantly non-selective, and in the sectors with high liquidity of sovereign funds investments.

Funds withdrew more than $17 billion from global equity portfolios, and $10.5 billion from US equity funds, and $3.5 billion from emerging-markets stocks. The largest exits were concentrated in the strategies of inactive investments in each category.

According to data from the Bank of America Merrill Lynch, total withdrawals from equity funds since the beginning of the year amounted to about $55.7 billion, in the longest wave of capital exits since 2008. Sovereign funds withdrew about $4.1 billion of fixed-income instruments strategies in emerging markets, overseen by external asset managers. Capital exits accelerated in the last quarter of 2015, after a poor performance of various asset categories.

Gulf Countries' Debts Increased 10 Times in Two Years
Kuwaiti Al-Qabas newspaper:

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Standard & Poor's expected a rise in total long-term commercial borrowing by governments of the Gulf Cooperation Council (GCC) countries to $45 billion during 2016, up from $40 billion in 2015 and 4 billion in 2014, noting that the desire of governments in the region to reduce the debt burden is very limited. Standard & Poor's said in a report that the drop by more than 70 percent in oil prices since mid-2014 weakened the public finances of the Gulf countries, resulting in a deficit for most governments. It added that some governments clearly needed financing, but it is not very clear how the deficit would be financed in terms of a combination of withdrawing assets and issuing debt securities. The large accumulated financial assets of Abu Dhabi, Kuwait, Qatar and Saudi Arabia allow them to choose between issuing debt securities and liquidating some of these assets.

FAO: Food Prices Stabilize in February Near Lowest Level in 7 Years
Rome – Reuters:

The United Nations Food and Agriculture Organization (FAO) said that global food prices stabilized in February near their lowest level in seven years as rising vegetable oil and meat prices offset the impact of declining cereal, sugar and dairy product prices.

The average FAO food price index, which measures monthly changes for a basket of cereals, vegetable oils, dairy products, meat and sugar, registered 150.2 points in February compared to 150.0 points, after adjustment, in the previous month.

The slight rise in prices in January came after a drop of nearly 19 percent in 2015, the fourth annual decline in a row. Prices experienced a larger decline in January.

FAO said that world food prices fell in February by 14.5 percent compared to their level a year ago.

IMF: Oil Exporters Should Adjust to Low Prices
New York – MENA

Director of the Middle East and Central Asia Department at the IMF, Masood Ahmed, said that no one expects oil prices to return to triple digits (higher that 100 dollars per barrel) in the near future. Therefore, oil-exporting countries should adapt to the new reality of prices instead of waiting for the end of this period of low prices.

In an article published in "Finance and Development" magazine, a quarterly magazine published by the IMF, Masood Ahmed said that in the early 1986s, following a decision by OPEC members to undertake a significant increase in supply, the price of oil fell sharply from around $30 a barrel to around $10 a barrel.

Survey: Growth of World Business Activity in February at Lowest Level in 3 years
LONDON (Reuters)

A survey showed that world business activity witnessed in February its weakest pace of growth in more than three years, despite the fact that companies cut prices for the first time since September.

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The JP Morgan Stanley All–Industry Output Index, prepared jointly with Markit, fell to 50.6 in February compared to 52.6 in January, registering its lowest reading since October 2012, when it rose above the 50 level—the dividing line between growth and contraction.

The producer price index registered 49.7, down from 50.1 in January, but the discount failed to stop the slowdown in new orders.

The purchasing managers' index, which covers the service sector, fell to 50.7 from 52.8—its lowest level in 40 months.

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From the International Press

What Does the Future Hold for "OPEC" after Five Decades of Influencing the Oil Market?

Source: http://www.argaam.com/ar/article/articledetail/id/410677

OPEC plays a key role in controlling the price of oil in world markets. With the recent decline in crude oil prices, OPEC is receiving unprecedented global attention as all markets are monitoring its movements and every word coming from it.

Origin

OPEC was created at the Baghdad Conference on 14 September 1960 by the then five major oil-producing countries, namely, Saudi Arabia, Iran, Iraq, Kuwait and Venezuela. The five founding members were later joined by nine other members: Qatar (1961); Indonesia (1962); Libya (1962); United Arab Emirates (1967); Algeria (1969); Nigeria (1971); Ecuador (1973); Angola (2007) and Gabon (1975), whose membership was terminated in 1994, thus bringing the number of OPEC members down to 13 countries after Indonesia reactivated its membership last year.

OPEC membership is open to any country that has an abundant surplus of crude oil provided the approval of the founding members and three-quarters of the members with full membership.

OPEC had its headquarters in Geneva, Switzerland, in the first five years of its existence. Then, it was moved to Vienna, Austria, on 1 September 1965.

Objective

The primary objective of OPEC is to coordinate and unify petroleum policies among the member countries, and ensure the stabilization of oil markets in order to secure an efficient, economic and regular supply of petroleum to consumers, a steady income to producers and a fair return on capital for those investing in the petroleum industry.

The decision of OPEC formation occurred at a time of transition in the international economic and political landscape, with the decolonization and birth of many new independent states. The international oil market was dominated by what was called the “seven sisters,” which were multinational companies that monopolized all petroleum phases from extraction from the well do its delivery to the consumer.

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These “seven sisters” monopolized all privileges in the Middle East, while the producing countries, which were producing crude oil from its grounds, got the crumbs of production profits only.

These companies were "the Anglo-Persian Oil Company" (BP now), "Gulf Oil," "Standard Oil of California," (Chevron), "Texaco," (later merged with Chevron), "Royal Dutch Shell," "Standard Oil of New Jersey"(Esso/ Exxon) and "Standard Oil of New York," (Mobil).

These companies had controlled 85 percent of global stocks since the mid-1940s to 1970s. However, the influence of these companies declined significantly in the wake of the 1973 oil crisis due to increased influence of "OPEC" and governmental companies in emerging markets. OPEC countries decided to set their pricing policies by themselves after prices were significantly reduced due to the seven sisters’ monopoly.

Unrivaled Success

In just one decade, OPEC managed to change from a limited organization comprising five developing countries into one of the most powerful and influential institutions in the world. Experts tried to analyze the secrets of the success of this small group of developing countries in achieving their objective in a world dominated by major industrial powers.

The primary secret is the role OPEC plays in the global oil market, which is still valid and important in the 21st century just as it was 50 years ago and is expected to remain so for decades to come, according to optimistic forecasts.

OPEC enjoys wide geographic diversity that extends from Latin America in the west to Southeast Asia in the east through the Middle East and Africa. The total population of OPEC countries is estimated at half a billion people. In spite of cultural, religious and linguistic differences, OPEC countries share being the major source of oil and the objective of maintaining their market share and ensuring market stability.

The Return of Indonesia

The decision of reactivating Indonesia’s membership in OPEC raised wide debate worldwide. Indonesia’s membership, the only Asian country within OPEC, had been suspended for nearly seven years since the beginning of 2009 after it became an oil importer.

World analysts raised doubts about the organization’s objectives. Indonesia consumes about double its oil production, with its oil imports’ bill reaching $13 billion last year. Since the suspension of its membership, the country has seen no change that justifies its joining the group of exporters.

According to Citigroup experts, the decision to reactivate Indonesia’s membership indicates “marginalized” role of OPEC and deviation from its main objective of preserving market stability, as it preferred to maintain its market share at the expense of price control, which showed in the continued pumping of oil despite the supply glut.

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Other experts, however, believe that the return of Indonesia carries great benefits for both parties. Indonesia is a link between OPEC and Asian countries that are witnessing growing energy demand. Being both a producer and consumer of oil makes Indonesia a promising market that helps filling the gap resulting from lower demand in the US and increased competition from Russia.

On the other hand, by joining OPEC, Indonesia will secure its oil imports at lower costs in light of its growing energy needs; as it is expected to be the world's largest importer of gasoline by 2018. Also, the new ties with the Middle Eastern producers will help it secure a stable supply of energy and eliminate the "oil mafia" in its domestic market.

The Future of "OPEC"

In spite of the panic sweeping the world due to the decline in oil prices, it is expected that the current crisis would enhance the impact of OPEC and restore its influence at the international level. The organization has faced significant threats to its influence in recent years as a result of intensive oil production by the US. But now only OPEC has the necessary tools to change prices.

US production saw a continued rise during the 1920s-1970s, but began to slow down afterwards despite rising demand, which made the US a major importer of crude oil. However, the situation changed dramatically with the discovery of new technologies that succeeded in extracting oil from great depths, leading to the flow of the so-called "shale oil". As a result, US production returned heavily to the markets.

Now the decline in oil prices has forced many shale oil producers to reduce their production. The policy of targeting market shares rather than prices, which was adopted by Saudi Arabia and the rest of the Gulf States, have succeeded in increasing pressure on the sector globally and caused losses to shale oil producers that would hinder their movement for some time.

It is expected that the production of non-members, especially the US, would decline in 2016. OPEC, however, continues to pump its production at will, while dominating a significant share of global production that is expected to increase after the return of Iranian production.

Experts' expectations for oil movements differ, but they all agree that OPEC decisions are currently the main determinant of market trends. Members do not seem to be in a hurry to change this situation, as they did not call for any emergency meetings, and the first meeting in their current agenda is scheduled for next June.

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Special Analysis

Differences of Opinions of G-20 Members Yield Disappointing Results

News agencies – Al-Sharq Al-Awsat Newspaper:

The G-20 members agreed in their meeting in Shanghai to adopt stimulus monetary and tax policies to support a slowing global economy, while global recovery seems uneven and less than expected. They said that global recovery is ongoing, but is still irregular and does not meet aspirations to achieve strong, sustainable and balanced growth.

They cited a number of key weaknesses afflicting the global economy, especially volatility of capital flows, the decline in commodity prices, rising geopolitical tensions, the possible exit of the UK from the EU, and the increase in the number of refugees.

They said that in order to promote confidence, monetary policy should continue to support economic activity and ensure price stability, noting that monetary instruments alone cannot lead to balanced growth. In this regard, they stressed the need for a flexible fiscal policy to boost growth, create jobs and build confidence.

In their final statement, finance ministers of the richest states in the world noted the risks to growth and the shock that could result from the possible exit of the UK from the EU.

The statement stressed the need to use all means, including stimulus monetary and tax policies, and structural reforms individually and collectively. It added that central banks have to continue, and even enhance their policies, deemed lenient originally. The statement went on to say that monetary policy would continue to support activity and ensure price stability, but it would not lead alone to sustainable growth, pointing out the need for a fiscal policy that is based on increased public spending to stimulate activity in a flexible manner.

The statement stressed the commitment of the G-20 members to what was previously agreed upon regarding exchange rates, i.e., to refrain from competitive devaluations, not to target the exchange rate for competitive purposes, and to communicate with each other regarding macroeconomic and structural policies to reduce uncertainty, minimize negative effects and enhance transparency.

In their final statement, the G-20 members added that anxiety indicators are increasing, pointing to the erosion of capital movement and the collapse in raw material prices. However, they acknowledged that severe turmoil in the financial markets does not reflect the fundamentals of the global economy. Added to this are the geopolitical tensions, the growing influx of immigrants in some areas, and the shock that can result from the UK's possible exit from the EU.

According to G-20 members, priority should be given to embarking (cautiously) on correcting public accounts, because "the debt-funded growth model" reached its maximum potential as noted by the German Finance Minister Wolfgang Schaeuble, who quipped that if they continued in this direction, debt-funded

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growth would lead to “zombifying the economy.” This problem appears sharply in China's heavy industry, as the Asian giant suffers growing indebtedness and faces the risk of default. China’s Finance Minister Lou Jiwei said that they have probably come to the brink and they have two options: either fall or continue the painful process of reform. Although the IMF encouraged easy monetary policies and plans for financial recovery, where appropriate, he expressed concern about growing financial risks all over the world, noting that the G-20 should urgently focus its efforts on ways to strengthen global «financial safety nets».

The IMF warned that the outlook for global economic growth could drift off course, because of market turmoil, the collapse in oil prices and political conflicts, calling on the G-20 to develop a plan for new mechanisms aimed at protecting the most vulnerable states.

The next meeting of G-20 is scheduled to be held in Washington, D.C. at the time of the IMF-World Bank spring meetings.

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Weekly Commentary

Despite frustrations resulting from the G-20 meetings, Egypt's participation contributed to the formulation of a vision focusing on structural reforms in all fields, most importantly, taxation and information exchange among countries to eliminate tax avoidance and the erosion of the tax base in tax compliant countries. This topic is a priority, because smuggling profits across countries to reach so-called tax havens causes serious damage to any economy, including that of Egypt.

According to the Egyptian delegation, the G-20 meetings focused on global economic performance, characterized by a period of slowdown as well as significant fluctuations in global markets. The delegation pointed out the challenges faced by emerging economies, whose obligations are increasing at a time they are suffering from erosion in the value of their assets, which are mostly financial. This implies serious ramifications for state budgets, which need to be addressed quickly and in a fully coordinated way to avoid future crises.

The meetings also addressed the importance of developing labor capacities, highlighting the OECD slogan "Skills, Skills, kills" in an intervention by its delegation. This topic is particularly crucial to Egypt in its pursuit to enhance production efficiency, competitiveness and the skills of its labor so they can find their rightful place in both the local and regional markets.

According to the Egyptian delegation, other topics related to the global financial system and institutions—such as international financial organizations and regional development banks—were no longer in forefront of issues as was the case during the 2008 global financial crisis. The focus then was on increasing the voting power and quota of emerging and developing countries in these organizations. However, this issue is still a subject of discussion as it relates to permanent calls for reforming international financial organizations.

As for Egypt, it still has to develop plans and strategies to promote its production sectors in order to benefit from its wealth and produce at affordable prices, and hence become more competitive in foreign markets. This way Egypt can protect its economy against global fluctuations and improve its economic efficiency to be able to cope with markets and their constant changes.

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