Issue: 41

Date : 15 January 2017

ECES
The Egyptian Center for Economic Studies

Our Economy & the World

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

- **Key Global Developments Over the Past Week**
- **From the International Press: Arab economies grow by 2.9 percent in 2017**
- **Special Analysis: The Economic legacy that will Face "Donald Trump**
- **An Analysis of Global Financial Market Performance and Changes in Prices of Goods and Raw Materials**

Key Global Developments

Study: Global Petrochemical industry to spend $201.3 billion by 2020

Argaam

Global petrochemical industry is planning to spend around $201.3 billion by 2020 on different future projects, according to a recent study.

According to a new report by BMI Research firm based in South Africa, large capacity additions with more than 700 planned projects are expected to come online in the next five years.

It noted that the US, China and Russia are the top three countries by capital expenditure for projects by 2020.

The report expects global petrochemicals capacity to experience considerable growth in the next five years with increase from 1,457 million metric tonnes per annum (mmtpa) in 2015 to 1,735 mmtpa by 2020.

World Bank: Global Growth Edges Up to 2.7 Percent Despite Weak Investment

Al Youm Al-Sabe'

Global economic growth is forecast to accelerate moderately to 2.7 percent in 2017 after a post-crisis low last year as obstacles to activity recede among emerging market and developing economy commodity exporters, while domestic demand remains solid among emerging and developing commodity importers, the World Bank said in a report.

Growth in advanced economies is expected to edge up to 1.8 percent in 2017, the World Bank's January 2017 *Global Economic Prospects* report said. Fiscal stimulus in major economies—particularly in the United States—could generate faster domestic and global growth than projected, although rising trade protection could have adverse effects.

Growth in emerging market and developing economies as a whole should pick up to 4.2 percent this year from 3.4 percent in the year just ended amid modestly rising commodity prices.

Nevertheless, the outlook is clouded by uncertainty about policy direction in major economies. A protracted period of uncertainty could prolong the slow growth in investment that is holding back low, middle, and high income countries.

"After years of disappointing global growth, we are encouraged to see stronger economic prospects on the horizon," **World Bank Group President Jim Yong Kim** said. "Now is the time to take advantage of this momentum and increase investments in infrastructure and people. This is vital to accelerating the sustainable and inclusive economic growth required to end extreme poverty."

Oil Discoveries Hit A 65-Year Low In 2016, But Should Rebound

Argaam

The amount of oil discovered last year was the lowest since the 1950s as explorers slashed spending amid the worst downturn in a generation.

According to Wood Mackenzie data, oil companies found only 3.7 billion barrels of so-called conventional crude in 2016, down 14 percent from the previous year, a little more than one-tenth of the yearly average since 1950.

Spending on exploration has been gutted since oil prices started falling in 2014 from $100 billion to about $40 billion last year, and may drop further this year, said Andrew Latham, Wood Mackenzie's vice president for global exploration.

Wood Mackenzie's data pointed out also that fewer wells were drilled: 431 in 2016, or about one third of the activity two years earlier.

If exploration remained at current levels, the world could see a supply shortfall of 4.5 million barrels a day by 2035, Wood Mackenzie estimates.

Trump and Brexit put global economic growth at risk

AlMal

2016 has been the weakest year for global economy since 2008 due to the political uncertainty unleashed by Brexit and the arrival of Donald Trump in the White House, the World Bank has said in a report published by the Guardian.

Announcing the findings of its annual Global Economic Prospects (GEP), the bank said global growth had failed to meet its forecast every year since 2011. A sluggish performance by the US and recessions in large commodity-dependent economies kept expansion in the world economy to 2.3 percent, down from 2.7 percent in 2015.

The Bank warned that the tax cuts and trade policy Trump has promised might result in lower growth. Hard Brexit will slower global economic growth, which is facing great challenges.

The bank predicted that increased oil prices will lead three countries out of recession, namely, Russia, Nigeria and Brazil. However, it didn’t refer to the impact on the consumer countries.

China vows to contain corporate debt levels

Argaam

China vowed to contain high company debt levels and further cut excess coal and steel capacity, as Beijing attempts to maintain solid and more balanced economic growth while avoiding destabilizing asset bubbles.

The world's second-largest economy likely grew around 6.7 percent last year, the head of the country's state planning agency told a news briefing.

Global investors are buzzing over whether China's leaders will be willing to accept more modest growth this year, amid worries about the risks from years of debt-fueled stimulus driven by the political obsession with meeting official targets.

Xu said China will not allow debt of non-financial firms to rise beyond current levels, and will step up efforts to encourage companies to restructure their debts. China's corporate debt has soared to 169 percent of gross domestic product (GDP).

Theresa May: we seek the best possible agreement to gain access to the common market

Argaam

U.K. Prime Minister Theresa May said Britain would make a definitive break with the European Union while still seeking to negotiate the best possible access to the bloc's common market.

"Often people talk in terms as if somehow we are leaving the EU, but we still want to kind of keep bits of membership of the EU," May said in an interview with Sky News. "We are leaving. We are coming out," she said, adding that London still "wants the best possible deal" in terms of trade.

May reiterated earlier comments that the U.K. would have control over its borders once outside the EU.

Argentina, Saudi Arabia and 4 countries sell bonds in international markets

Al-Youm Al-Sabe'

Patrick Esteruelas, head of research at EMSO Asset Management in New York, pointed out that there was likely to be a flurry of issuance from emerging markets in January, with Brazil, Honduras, Nigeria, Egypt, Saudi Arabia and the Philippines all sounding out investors.

According to a Financial Times report, Argentina is looking to sell up to $10bn of debt, many emerging markets are racing to raise finance to mitigate risks stemming from the uncertainty over the direction of US policy with Donald Trump set to be sworn in as US president on January 20.

The election of Mr Trump in November sparked hefty selling across emerging markets, with sentiment rattled by his talk of trade protectionism and increasing customs on imported goods. A stronger US dollar and higher bond yields also sapped appetite for EM.

Dollar to hit parity with euro during 2017, says Goldman Sachs' chief economist

Argaam

The dollar is likely to hit parity with the euro during 2017 driven by diverging paths for interest rates, according to Goldman Sachs' chief economist.

The Federal Reserve (Fed) is likely to hike interest rates three times in 2017, pushing it even further from the rate positioning stance of Europe during the course of the year, Jan Hatzius told CNBC.

The primary driver here is not valuation but really interest rate differentials. If we are right that the Fed moves the funds rate up more than what the markets currently pricing … that's generally a relatively good indicator to watch," he posited.

Goldman Sachs' base case estimate that the Fed will follow through with rate rises in June, September and December this year is more hawkish than current market consensus which is pricing in two hikes for 2017.

There is a weak likelihood that a rate increase will be announced by the Fed as early as this March.

Implications for Egypt:

The recent fluctuations in the global economy indicate increased pressure on opportunities for the global economic growth. This calls for an Egyptian action to enhance economic growth. In particular, it requires increasing domestic production, especially with regards to SMES, in light of the expected recession in Britain and shifts in the movements of global investment cash flows. There is also the escalated trade war between the US and China under a slowing global economy. Thus, Egypt has to move further to encourage domestic consumption rates while supporting its presence in regional Arab and African markets in order to seize larger market shares over the medium, term and benefit from the common trade agreements with these countries.

Egypt should also start activating reforms implemented through packages of economic programs that focus on adjusting government spending, rationalizing consumption, specific productive economic sectors, and reviving some of the marginalized investment economic sectors. This will reduce the deficit and improve the economic capacity.

Attention must be paid to the strategic economic and the commercial link between Egypt and the Gulf, which calls for the development of integration concepts. Establishing joint economic zones, expanding bilateral trade agreements, introducing new sectors such as services and establishing joint industries devoted to replace imports in the Arab region and relied on raw materials and Egyptian-Gulf economic diversification will be an economic foundation for the development of trade and economic relations over the coming period.

From the International Press

Arab economies grow by 2.9 percent in 2017

UAE Etihad

The Arab Foundation for the Insurance of Investment and Export Credit (DHAMAN) predicts that the Arab economy will relatively improve in 2017. Average growth rate is expected to reach 2.9 percent, bringing Arab GDP up to about $2.7 trillion. Thus, the average income of the Arab citizen will reach $7,750 annually, inflation rates will rise to 5.9 percent and the region's population growth will reach 372 million people.

As part of its last quarterly bulletin in 2016, DHAMAN said in a report that since the beginning of the third millennium, the Arab economies have been witnessing many fluctuations that influenced their developmental indicators and the overall balances, differing from one country to another in terms of the severity of these fluctuations and their implications. The report pointed out that the risks surrounding the economic outlook in the region have increased due to internal political events and external implications caused by global economic developments, especially the fluctuations of the Chinese economy, the repercussions of Brexit and the changing political orientation of the US under the new Republican president.

The report, which is based on the statistics of the International Monetary Fund and other entities, pointed out that despite significant uncertainty regarding the future course of oil prices and growth prospects in emerging markets in general and in China in particular, 2017 is likely to witness a relative improvement in the performance of internal and external balances. The report predicted that the deficit in the total net government budgets of the Arab countries would decline to $200 billion, and the current account deficit to $104 billion. However, a likely rise in foreign indebtedness of the Arab countries to about $1140 billion is expected as a result of some countries resorting to external borrowing and issuing bonds in global markets.

On the trade side, the report captured signs of improvement in the exports of goods and services exceeding $1 trillion caused by relatively rising oil prices. However, the international reserves fell by $112 billion to one trillion dollars, enough to cover 12.3 months of imports of Arab goods and services, as a result of some governments using reserves to finance part of their budgets.

According to the report, it is normal for the capital and investment movements in the region to be affected. Total net capital accounts of the Arab countries' balances of payments rose from $4.5 billion in 2013 to $22.2 billion in 2015. The report added that donor countries continued to provide developmental aid and formal assistance to a number of countries in the region settling at about $22 billion in 2014. Total aid received by countries in the region from 2000 to 2014 amounted to more than $213 billion.

The report argues that the data on Arab economic situation in the future stress that the region's economy is still mostly affected by developments in oil prices, production and exports. Oil still represents 85 percent of the region's exports, more than 60 percent of governmental revenues, and over 35 percent of output.

The report stressed that with the continuously increasing political, security and economic challenges in the region and their entailed uncertainties and risks, it is important that governments in the region neutralize the potential negative implications of these developments for the investment climate and business environment as a whole. This should be a first and necessary step on the road to enhance the attractiveness of the region as a global destination for foreign investments and international trade in goods and services. This will eventually enhance the plans and programs of economic reform and development, which became necessary to improve the living standards of the populations in the region.

Implications for Egypt:

Domestic demand has been the main driver of economic growth in Egypt for many years, according to a report of the Ministry of Planning. Though it is in line with the global trend of some countries such as China and the United States as a result of slowing global economic growth, the Egyptian situation reflects a completely different economic nature. Consumption exceeded 94 percent in the third quarter of FY2015/2016 and 95 percent in the first nine months of the same year. This increased the savings gap 11.2 percent in the third quarter. Savings rate amounted to 5.8 percent compared with an investment rate of 17 percent. This situation calls for a strategic approach to reduce reliance on consumption as a driver for growth and rely on other growth engines such as investment and exports instead.

Solving the current problems of the Egyptian economy requires a sustainable industrial development under an economic restructuring to prepare industries for replacing imports and increase exports. Signs of this strategy are currently evident in a development and funding strategy for SMEs, and establishing integrated agro processing complexes as part of the one and a half million feddens project. This strategy requires complementary reforms in economic areas to remove export and investment constraints through real economic reforms.

However, low FDI growth in Egypt is not only due to the geopolitical factors of the region or the global financial crisis, but also to internal factors related to the management of the investment climate, addressing its obstacles, eliminating administrative overlapping and lengthy licensing procedures and approvals, despite reform efforts made at this level.

Special Analysis

The Economic legacy that will Face "Donald Trump

Argaam

While the US president-elect, "Donald Trump", is expected to start his term of office in the White House this January, a quarterly economic growth of 3.5 percent that is the largest in two years has been recently announced for the third quarter.

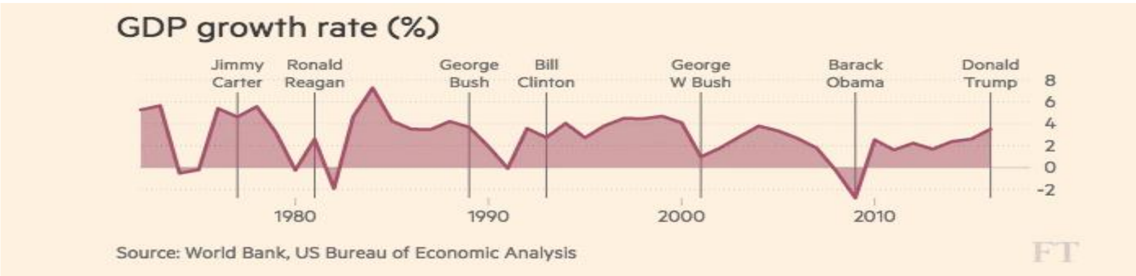
Recent economic data are significantly different from those when former president, "Barack Obama", came to power in 2009. The US economy then was losing 800 thousand jobs per month, but significantly recovered from the crisis. Stock indexes also hit record highs to coincide with the recovery of the housing market.

This comes in conjunction with a decline in unemployment rate to its lowest level in nine years. The "Financial Times" published a report of seven charts for the economic legacy, which will face US President-elect "Trump".

Economic growth

In modern history, former presidents, "Jimmy Carter" and "George Bush," entered the White House when the US economic growth was at high levels.

Economic growth data for the third quarter showed a growth above expectations that is the largest quarterly growth in two years. Thus, "Trump" will follow "Carter" and "Bush" in taking office with a recovered economy.

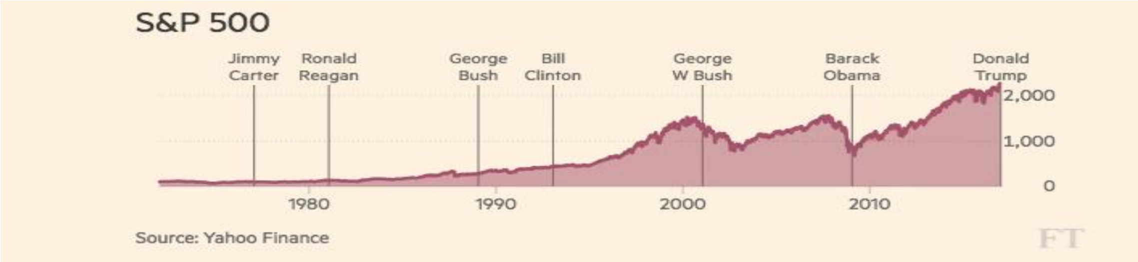


The Stocks market

After recovering from the global financial crisis in 2008, the US stock market headed towards record highs as of the beginning of 2013.

US indexes hit record levels after the announcement of the victory of "Trump" of the presidency, backed by pledges he made during his campaign to cut corporate taxes and increase spending on infrastructure.

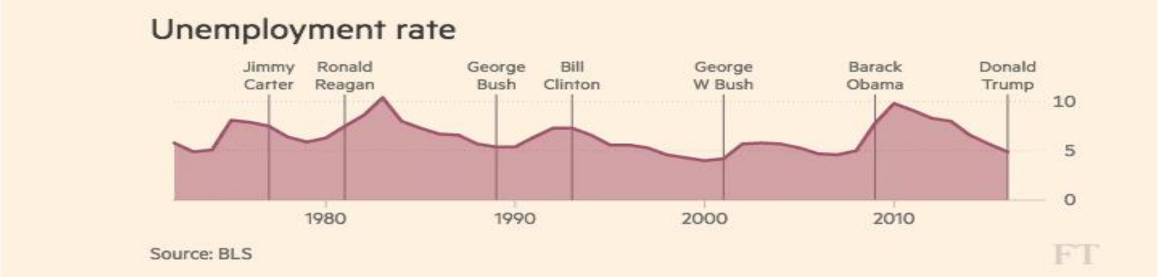
Nevertheless, there are some other proposals haunting investors, such as the imposition of tariffs on imports from Mexico and China.



Unemployment rate

The unemployment rate fell to 4.6 percent. "George W. Bush resembles "Trump" in assuming presidency of the country in the face of lower unemployment rates."

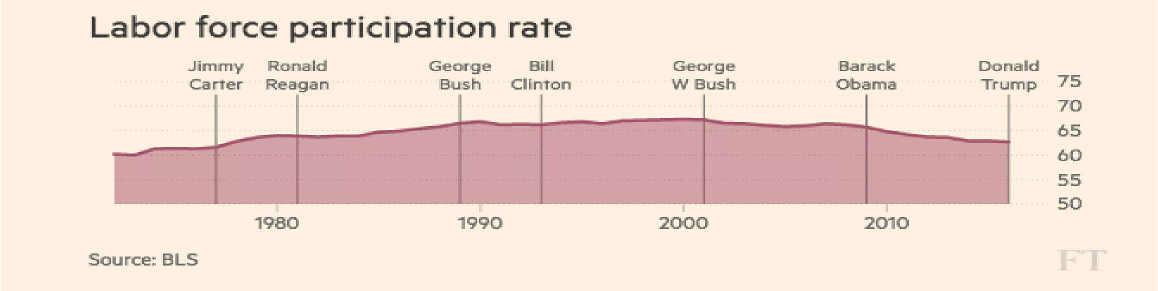
The unemployment rate jumped to 10 percent in October 2009 after "Obama" started his term in the White House. He was preceded by "Ronald Reagan" only, whose presidency saw a drop in unemployment from 10.8 percent in 1982 to 5.3 percent in 1988.



Labor force participation rate

"Obama" opponents argue that despite the drop in the unemployment rate, labor force participation is still low, and lower than its level in the mid-nineties.

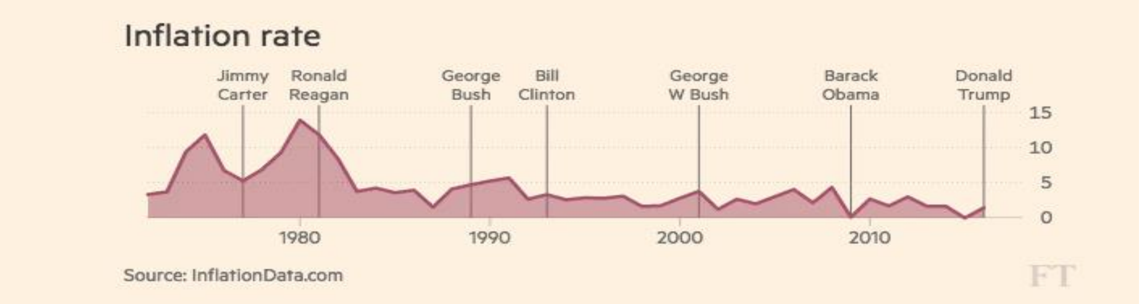
Many workers exited the labor market during the global financial crisis. Today, it is difficult to know how many will reenter the labor market in light of increased birth rates, which forced some families to stay at home for child care.



The inflation rate

The Federal Reserve targets an inflation rate of 2 percent per annum in conjunction with price stability and increased employment. With the inflation rate approaching the target, the Federal Reserve decided to raise the interest rate in December, with expectations of raising it three more times in 2017.

"ABN AMRO" Bank is expecting the US Federal Reserve to raise interest rates four times rather than 3 times next year.



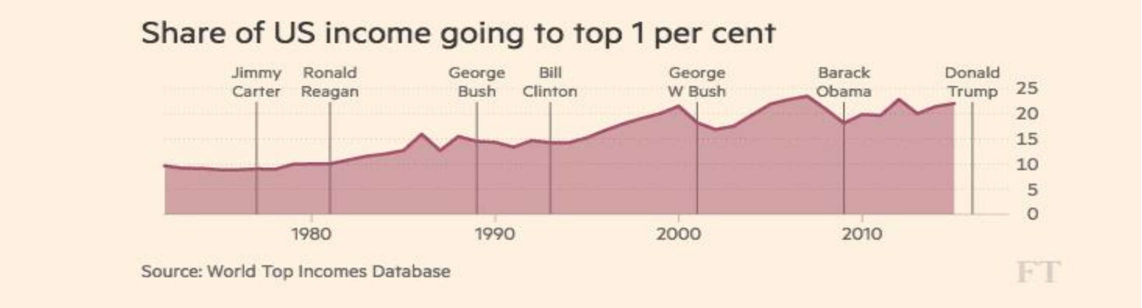
Inequality

In spite of the above, the road is not fully paved in front of "Trump". Inequality remains at levels that are the highest in a decade and that the federal budget deficit is still larger than before.

Levels of inequality in the US rose to their highest since the twenties of the last century before the Great Depression because the wealthy are taking the lion's share of income.

Studies have shown that increasing inequality leads to political polarization, low economic recovery and low participation of the middle class and less educated people.

It would be difficult to confront inequality, but in light of the policies proposed by "Trump", the problem may worsen especially if a corporate tax cut is in effect, which means that the rich will be richer.

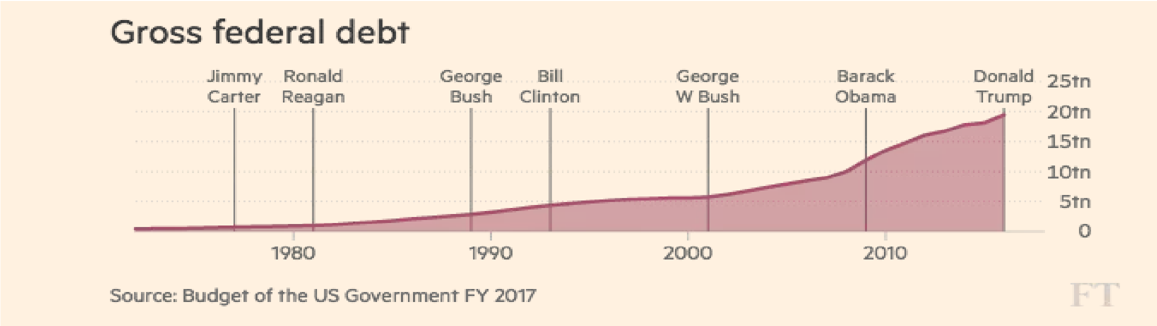


Public debt

"Trump" is facing a big problem, namely the public debt, which stands at its highest level ever at more than $19 trillion, to coincide with the president-elect's pledges to increase spending on infrastructure by about $550 billion, and to support the defense industries.

Additional government spending in conjunction with the decline in revenues from the tax reduction plans may lead to a rise in public federal debt by about $7.2 trillion over the next ten years.

These are not the only problems, there is also the stagnant growth in the emerging markets and advanced economies, and the decline in the number of jobs in the industrial sector in conjunction with the dollar rising to its highest level in 14 years, which will reflect negatively on exports.



Implications for Egypt:

The Egyptian economic policy needs to re-balance urgently in light of the triplet risks it is facing currently, represented in high debts, low productivity growth and diminishing CBE tools. There are worrying developments that call for monitoring.

Risks are concentrated in the unusually low productivity growth, casting a shadow on improved living standards in the future, and in historically high domestic and foreign debts, increasing risks to financial stability and room for maneuver given a notable tightened monetary policy.

Thus, the Egyptian economy can no longer rely on the current growth model which drove it to the current crossroad. There is an urgent need to rebalance the economic policy in order to move to a stronger and more balanced and sustainable growth. It is necessary to abandon the growth model, which caused that dilemma and to alleviate the burden on the monetary policy, which has been burdened for a long time.

This calls for substantial adjustments in both fiscal and monetary policy orientations, for redesigning the fiscal policy to cope with the boom-bust cycles more systematically and that the monetary policy monitors those cycles in terms of overall risks to maintain the balance of the financial part of the economy.

Global Financial Market Performance

Reuters/ Argaam

Japanese stock indexes rose at the close of trading and erased weekly losses, with the depreciation of the yen against the dollar and despite weak expectations about inflation and consumer prices.

At the end of the session, the Japanese "Nikki" index rose by 0.8 percent to 19,287 points, while the "TOPIX" index rose by 0.6 percent to 1544 points.

A survey of the Central Bank of Japan showed the lowest inflation expectations in four years, after only 64.7 percent of those surveyed said that consumer prices are on their way to rise over the coming years, the lowest level since the fourth quarter of 2012.

Chinese stock indices fell at the close of trading, for the fourth straight session, the longest series of losses since October, following the release of weak economic data.

At the end of the session, the "Shanghai" Composite Index fell 0.2 percent to 3112 points, marking the longest series of daily losses since October.

Chinese exports denominated by the yuan dropped by 2 percent in 2016 compared to a decrease of 1.8 percent in 2015. Imports rose 0.6 percent after falling by 13.2 percent in 2015.

According to official data released, trade balance surplus dropped by 9.1 percent to 3.35 trillion yuan ($486.1 billion).

Most US stock indices also stabilized during Friday's trading, giving up the gains recorded earlier in the session following positive economic data, while "Nasdaq" achieved sixth record close in the last seven sessions.

The Dow Jones industrial average dropped five points to 19,885.7 points, the broader S & P 500 index rose (+4 points) to 2274 points, while NASDAQ rose (26.6 points) to 5574 points, posting a new record closing.

On the weekly level, the "Dow Jones" recorded losses of 0.4 percent, "S & P" recorded losses of 0.1 percent, while "Nasdaq" posted weekly gains of 0.1 percent.

In the European markets, "Stoxx Europe 600" benchmark index rose 0.9 percent, or 3.43 points, to 366 points.

The British "FTSE" Index rose (+45 points) to 7338 points, while the French "CAC" index rose (58.5 points) to 4922.5 points, and the German "DAX" index rose (+108 points) to 11629 points.

On the other hand, Gold futures for February delivery settled down 0.3 percent or $3.60 to $1196.20 an ounce. The precious metal made about 1.9 percent in gains this week.

In the oil markets, the US "NYMEX" fell by 1.2 percent or 64 cents to close at $52.37 a barrel and recorded a weekly loss of about 3 percent, while crude "Brent" fell by 1 percent or 56 cents to close at $55.45 a barrel, recording a weekly loss of about 2.9 percent.

As for economic data, the US producer prices index rose 0.3 percent in December, and retail sales rose 0.6 percent in the same month, while the Michigan/ Reuters consumer confidence index declined to 98.1 points this month.

Next Monday, the sixteenth of January, is an official holiday in the US and the stock exchange will close, celebrating Martin Luther King Day, and will resume work on the following day.

Implications for Egypt:

The global financial markets continued to rise, benefiting from the depreciation of global currencies against the dollar. Analysts believe that the stock markets were able to absorb the Fed's decision to raise interest rates and the start of Trump's term of office, looking forward to the future with good prospects backed by the US plans to promote economic growth.

On the other hand, the Egyptian stock indexes rose for the second week in a row and the main index, "EGX 30", closed on a weekly rise of 3.12 percent, representing 399.58 points, at 13,223.9 points.

"EGX 70" rose by 1.9 percent at 473.1 points over the week, while "EGX 100" rose by 3.71 percent at 1154.37 points. Similarly, "EGX 50 equal weights" rose by 2.43 percent at 2040.77 points.

Market capitalization rose by about LE 14.9 billion over the week to close at LE 629.7 billion, compared with the previous close.

We emphasize that the Egyptian Stock Exchange is in dire need to diversify new products and securities, to enhance its ability to increase its stability and attract liquidity and new investors. However, it is important to choose the right time to start these offerings following achieving stability of the stock market's internal conditions to ensure greater success. This will represent a message of reassurance to investors and foreign institutions. The overall performance of the stock market faces many challenges on the road to stability and growth due to financial and economic direct justifications. The stock market has not yet reached harmony with the financial and economic data in the absence of institutional investment based on values and financial and development goals.

It is also important to develop new stimulus measures for the Egyptian Stock Exchange to increase its financial depth and investment flexibility by completing the required legislative amendments and taking faster steps towards the offering of companies and new financial instruments at the Stock Exchange.