

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

- **Key Global Developments Over the Past Week**
- **From the International Press: Britain's budget: optimism in 2017 ... then 3 years of austerity**
- **Special Analysis: Protectionism Divides the World and Breaks Ranks in the US**
- **An Analysis of Global Financial Market Performance and Changes in Prices of Goods and Raw Materials**

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## Key Global Developments

# Report: Hedge Funds Exit Emerging-Market Assets

### Argaam

Short-term investors are escaping emerging markets ahead of a likely U.S. interest-rate hike this week amid concern a strengthening dollar will undermine credit quality in developing nations. Meanwhile, longer-term investors have increased their exposure, pointing to equity and currency valuations that linger below their five-year averages and arguing developed nations from the U.S. to France carry greater political risks.

Hedge funds and other leveraged investors posted their biggest emerging-market currency outflows since early December, while institutional money managers such as pension funds boosted their inflows to near the highest level in 16 months, according to data from Citigroup Inc.

The biggest dichotomy was seen in Poland's zloty, where real-money flows rose to near the highest in more than 18 months as indexed flows for hedge funds decreased to the lowest level this year.

## U.S. shale oil output to soar in April

### Reuters

Total U.S. shale oil production was expected to rise 109,000 barrels per day to 4.96 million bpd, its biggest monthly increase since October as output in the Permian Basin, America's fastest growing shale oil region, was expected to hit another record high, government data showed.

According to the U.S. Energy Information Administration's drilling productivity report, oil production in the Permian Basin in Texas and New Mexico, the largest U.S. shale oil field, was set to rise 79,000 bpd to 2.29 million bpd, the highest level on records dating back to 2007. In the Eagle Ford region in Texas, output was expected to grow nearly 28,000 bpd to 1.14 million bpd, the highest level since November.

Production in the Bakken, however, was set to drop 10,000 bpd to 964,000 bpd, the only month-on-month decline across all seven basins used in the report. That would be the third consecutive monthly decline in the North Dakota basin.

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## **Mario Draghi affirms the ability of the euro area to enhance productivity**

### **Argaam**

ECP President Mario Draghi warned against pessimism about long term growth in Europe. He noted that there are several possible ways to increase productivity.

The comments came at a time when skeptics argue that increased productivity can not return to the levels reached in the decades before the financial crisis, and that the gains from business such as electricity, railways can not be compared with those obtained from modern technological innovations.

However, in his speech in Frankfurt, "Draghi" added that productivity growth depends not only on the creation of new ideas, but also on their dissemination. He added that although some progress can be made in the field of innovation, it is not the only goal. Facilitating and encouraging the spread of modern technologies in the Eurozone is also important. This would enable the Eurozone to achieve significant gains in productivity.

## **UK parliament gives final approval for Brexit bill**

### **Reuters**

Parliament gave its approval for Prime Minister Theresa May to start Britain's withdrawal from the European Union, after the House of Commons voted against changes by the House of Lords to amend a bill empowering May to begin Brexit, paving the way for it to become law as early.

Brexit minister David Davis welcomed MPs approval of the bill, saying that Britain is about to enter the most important negotiations in a generation.

Article 50 will be triggered by end of this month as intended, and benefits will be achieved for the UK.

According to the Times, British Prime Minister Theresa May is preparing to reject the Scottish Prime Nicola Sturgeon's request to hold a referendum on independence on the eve of Brexit. The newspaper quoted a British government source as saying that the Prime Minister said that this would mean a vote while negotiating Brexit, and would be taken as a clear message, the timing is totally unacceptable. The newspaper

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quoted an ally of May saying that she was ready to be clearer in the coming weeks to say that preparing for a referendum on Scottish independence would undermine the negotiating position of Britain with the rest of the European Union.

### Global public debt \$44 trillion

#### Al-Hayat

Experts in Switzerland announced that global public debt is rising steadily due to random expansionary policies adopted by governments in the last ten years to deter the financial crisis. There is no doubt that the spending budgets allocated by US President Donald Trump to revive the country will push this debts into a deeper tunnel. Swiss experts estimated the value of accumulated public debt around the world about at \$44 trillion end of this year. Talking about public debts moves attention to the treasury bills of about 133 countries, usually issued to cover the domestic deficit, and their dues are payable to the buyers of these bills, whether local or foreign investors. Global public debt increased by 2.3 percent last year.

The US public debt reached \$14.5 trillion, putting it at the top of indebted countries, followed by Japan with its debts exceeding \$9.5 trillion. Italy comes in third with debts amounting to two trillion dollars. If central banks around the world didn't cut interest rates, which contributed to reduce the global debt burden by 3 percent, the reputation of some of the industrialized nations would have been affected in the capital markets. The governments of industrialized nations will not cease to issue treasury bills this year, but the issuance pace will be lower compared to last year.

Globally, experts predicted the total value of these bills to amount to about \$6.8 trillion this year, compared with more than 7 trillion last year. The US and Japan, once again, will top the list of countries with the most issuance as both would account for about 60 percent of issuances in dollars this year. Financial researchers in the city of Zurich said that credit quality is eroding slowly around the world. The bonds of many countries are now classified as worthless, noting that 7.5 percent of the world's debt is of countries rated BB, such as Brazil, whose T-Bills issuances amount to \$191 billion.

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## U.S. government posts \$192 bln deficit in February

### News agencies

The U.S. government had a \$192 billion budget deficit in February as outlays far outstripped receipts, the Treasury Department said.

The budget deficit was \$193 billion in February 2016, according to Treasury's monthly budget statement.

The fiscal 2017 year-to-date deficit was \$349 billion compared with \$353 billion in the same period of fiscal 2016.

Receipts last month came to \$172 billion, a 2 percent increase from February 2016, while outlays stood at \$364 billion, up 1 percent from the same month a year earlier.

### Implications for Egypt:

Recent global economic volatility points to escalating pressures on global economic growth opportunities. This requires Egypt to enhance measures taken to increase economic growth, such as the promotion of domestic production, especially among SMEs. Therefore, Egypt has to take more robust actions through economic reform packages that focus on reducing government expenditure and rationalizing consumption, encouraging certain productive sectors, and revitalizing marginalized investment economic sectors. These actions could help reduce the deficit and improve the economy

Egypt should develop plans and scenarios for dealing with the current situation and its possible developments, along with a comprehensive assessment of the map of foreign transactions in light of the changes that occur, whether at the level of oil markets or the potential for structural changes in the EU in the coming period. This would allow greater flexibility in Egypt's alternatives in dealing with any repercussions of those situations in the future. We should also be aware that traditional exports will not grow continuously like in the early stages of development, because business opportunities will continuously be reduced and wages will rise, implying reduced competitiveness. Export growth depends on the introduction of new processes and exploring new markets, not just expansion of sales of existing products in the market. To achieve this, innovation and product differentiation to meet the needs of the market is a target in itself for middle-income countries

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## From the International Press

### Britain's budget: optimism in 2017 ... then 3 years of austerity

#### Asharq Al-Awsat

UK Chancellor of the Exchequer, **Phillip Hammond**, delivered his first budget after Brexit. Growth rates are better than outlook for this year, but growth outlook for the next three years declined. It seems that Hammond is preparing the British for austerity in anticipation of Brexit repercussions.

Hammond said that his country raised its official forecast for economic growth for 2017 but lowered it for the next three years. He seemed loyal to his firm line, and did not deviate from the framework set by the Conservatives since their return to power seven years ago. He added that the country should revert to live according to its potentials.

The Office for Budget Responsibility forecasts a GDP growth of two percent in 2017, up from estimated growth of 1.4 percent in November, but lower than the 2.2 percent growth forecast issued a year ago before the vote for Brexit.

Hammond told the House of Commons that the Office for Budget Responsibility expects 1.6 percent in growth in 2018 compared with the November forecast of 1.7 percent.

Growth forecasts for 2019 and 2020 amounted to 1.7 percent and 1.9 percent respectively compared with the previous growth forecast of 2.1 percent for both years. Growth outlook for 2021 amounts to two percent, unchanged from the outlook issued in November.

The UK economy was expected to slow down strongly after the vote for Brexit in June, but consumers continued to spend strongly and helped the economy to grow 1.8 percent faster than the rest of the major economies in the G7 in 2016 with the exception of Germany.

However, there are increasing signs that shoppers are becoming more cautious at a time the devaluation of the sterling pound after the referendum pushes inflation higher.

British Prime Minister Theresa May intends to launch Brexit negotiations before the end of March, starting a process that is expected to make companies cautious about long-term investments.

Brexit negotiations between London and Brussels are scheduled to take two years to arrange a full exit, and will start as of March.

Britain has been witnessing a favorable economic situation since the referendum, as the economic activity did not see the slowdown predicted by the catastrophic scenarios that have spread with the organization of the referendum.

Thus, attention is not focused on the budget itself, but rather on the growth forecasts that it is based on, after verified by the Office for Budget Responsibility. The forecasts for 2017 are high, while those for the three following years are low.

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### Implications for Egypt:

Egypt should pay attention that the state budget shows increased spending on a number of items such as wages and debt servicing. This reduces the fiscal space that could otherwise be directed to spending on health, education and scientific research. The growing budget deficit is mainly due to the fact that the budget included exaggerated revenues at the time of its drafting with regards to tax revenues in spite of the relative economic slowdown caused by internal and external factors.

It is possible to secure real savings from subsidies, if the relevant mechanisms are rationalized, especially through better targeting, reducing waste that results from inaccurate data, which will improve the subsidy system and reflect positively on citizens' lives.

It is necessary to change the current approach of preparing the budget to start implementing program and performance budgeting on a number of budget entities and ministries, linking budget implementation to targeted economic performance indicators.

The British budget attracts attention to the fact that drafting the Egyptian budget requires resolving one of the major problems, namely, lacking expenditure ceilings for the various sectors that provide their budgets to the Ministry of Finance, causing failure to identify spending priorities. Therefore, it is necessary to make a thorough review of public spending items, whether bonuses or purchase of goods and services.

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## Special Analysis

### Protectionism Divides the World and Breaks Ranks in the US

Al-Sharq Al-Awsat

Sharp divisions appeared in the US over the past few days about some points of the economic program of President Donald Trump, especially those threatening to impose tariffs on imports from China by 45 percent, and from Mexico by 35 percent, in addition to 10 percent in general, while exempting US exporters from duties and taxes.

Internal opposition in the US came first from large stores such as Wal-Mart and Target, and large sectors such as clothing and furniture. Even the automotive sector expressed caution.

Trade sources said pressure groups are now shaping up to be part of the debate, noting that a number of pressure groups are not far from the Republicans, because the business community in general and employers in particular are historically Republican voters who do not want to see their margins shrink or evaporate due to actions against their interests. To them, if President Trump addresses workers and employers affected by imports, he might as well listen to merchants.

Furthermore, agencies concerned with consumer protection in the US have warned of the possibility of higher prices after increasing customs, threatening the purchasing power of large segments of low-income Americans. In this segment, there are those who voted strongly for Trump. There are also fears that there will be a shortage of goods not produced in the US, because industrial specialization is now spread among developed countries.

Moreover, industrial exporters expressed concern that countries whose exports to the US will be affected will take counter-measures by imposing additional duties on the import of US goods. Other industrialists are concerned they'll pay high duties on their imported intermediate inputs.

US media reports, based on warnings issued by the International Monetary Fund and the World Trade Organization, refer to the possible negative impact resulting from the sharp customs measures that would be matched by similar

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counter-measures in what looks like a trade war. There are studies that now focus on the legal basis of the customs and tax procedures to see if they conflict with the obligations of WTO commitments.

On the other hand, there are big companies that support the Trump, believing that the tax breaks announced by Trump for US exporters would encourage them to create jobs.

Congress received a letter last week from Boeing, General Electric, Caterpillar and other companies, calling for speeding up the adoption of these exemptions for exporters even if the package of legislations includes raising the duties on imports. This is countered by a warning that «preferential treatment» may render the US liable to lawsuits before the World Trade Organization. If the US loses those suits, the Peterson Institute, specialized in trade disputes, believes the fines would amount to \$385 billion.

The EU has also vowed to respond in the event of a breach of the rules of global trade. A source in the EU said that all the necessary legal preparations are in place in addition to WTO rules. The source warned Americans of the discrimination game because it may elicit reprisals from affected countries. But a leaked document from the US Department of Commerce published by the Wall Street Journal late February notes that appealing to US law, not others, would help counter unfair trade practices, as in several similar cases. This is a reference to a law passed in 1974 allowing the President to impose sanctions if he deems the trade practices as unfair to the US. The US Treasury is trying in the midst of this controversy to calm opponents, noting it is still exploring matters, stressing the importance of economic growth, besides budget and revenues.

In parallel, large banks, most notably Goldman Sachs, said that there would be discrimination between exporters and importers, but the most dangerous point is the appreciation of the dollar as a result of exempting exporters while raising the import duty. This appreciation would be against the interests of US exporters, because their products would be more expensive than others and hence lose their competitiveness in international markets. It is worth noting the US currency appreciated against the Chinese yuan, the euro and the pound sterling by 5.8, 4.6 and 13.5 percent, respectively. It also appreciated by similar or more percentages against the currencies of many emerging countries that export to the US.

Trump hinted several times that countries such as China, Germany and Japan are using their weak currencies to boost exports. But experts point out that the President forgot that the problem also lies in the dollar, which appreciated against other currencies, hence increasing US imports while exports suffered.

Monetary experts also noted the huge debts of US households and how they have accumulated, threatening to explode as happened in 2008. They conclude that Americans are living beyond their means and consume more than any other people in the world. To finance consumption, loans grow at rates higher than the rate of economic growth. Nothing new in the US trade deficit because it has been going on for 40 years, they said.

Another study by Pantheon Macroeconomics refers to what looks like a «trap». It explains that the program is integrated, promising to cut corporate taxes and to spend hundreds of billions on infrastructure. The funding comes from items such as raising of customs. Any retraction on the customs procedures will drag behind a radical change in

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both the tax cuts promised to companies, and government investment spending, thus turning the Trump program upside down.

Republicans excited about the Trump program estimate revenues at a trillion dollars in 10 years, because US exports more than it imports. Duties would bridge the resulting shortfall resulting from exempting exporters from taxes and the lack of tax revenue resulting from the reduction of corporate income tax from 35 percent to 20 percent.

Republican proponents of the Trump program base their support on the huge gap in the US trade balance, which registered a deficit of about US\$502 billion in 2016, the highest since 2012.

Regarding details, the trade of goods recorded a deficit of US\$750 billion, while the balance of services recorded a surplus of US\$248 billion. The commodity trade deficit with China was the largest (US\$347) billion, against US\$146 billion with the EU, 45 percent of which with Germany alone (65 billion) compared to 69 billion with Japan, and 63 billion with Mexico. Republicans say that former President Barack Obama was aware of the magnitude of the problem when he promised in 2010 to double US exports by 2015, but failed because exports increased only 20 percent in five years.

Concerning countries affected by the implementation of Trump's policy of protectionism, reports say that Mexico will inevitably be affected, because 80 percent of its exports go to the US. Total exports account for 25 percent of Mexico's GDP. But US manufacturers will be affected as well, because part of Mexico's exports are spare parts and components imported from the US and then assembled in Mexico.

China's exports to the US constitute 4 percent of its GDP, but that GDP constitutes 18 percent of the global economy and 30 percent of emerging countries' GDP. Any tariff increase will have repercussions on the global production chains, particularly Southeast Asia chains, specifically in Taiwan, the Philippines, Thailand and South Korea. China is also an important center for the US assembly industries of electronic and electrical devices. The affected countries also include Vietnam, because its exports to the US constitute 23 percent of its GDP, while the exports of Thailand to the US account for 11 percent of its GDP.

IMF experts call for re-reading what happened in 1930 when the US increased duties from 38 percent to 50 percent on 20,000 commodities, driving other countries such as France, Germany, Britain, and Canada to take countermeasures. This decreased world trade by 70 percent in subsequent years and increased unemployment in the US from 9 percent to 25 percent in a few years.

IMF experts note that the increase of customs by an additional 10 percent in the US and China will decrease global economic output by 1.5 percentage points in three years and then 1.75 percentage points in 5 years. Exports and imports between the two countries will decline by 16 percent and investments by 5 percent. Goldman Sachs points out a possible decline in US and Chinese growth, albeit the former will suffer more.

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A research paper by the Peterson economic think tank noted that Trump's promise caters to the Americans who have been affected by globalization, especially when he pressures US factories to return home, and when he focuses on American job losses, blaming China, Mexico and others. However, who rejects globalization will eventually fall like North Korea and the Soviet Union compared to the rise of China.

According to Peterson, isolation is useful to a segment but harmful to many others. In addition to the 12 million Americans working in export-related sectors, a multiple of that figure are working in trade. It added that the harmful effects of increased customs include hitting the existing world production map, which now relies on the manufacture of one product in different areas of the globe. The boundaries on the manufacturing maps are not as clear as they were before. Therefore, the potential damage will be like a billiard ball hitting 4, 5 or 6 other balls. This view is supported by Oxford Economics, which says that exports of Japan, South Korea, and Taiwan will be affected by the increase of duties on Chinese and Mexican exports.

#### Implications for Egypt:

These global developments affect chances to increase the fair volume of trade worldwide, which requires Egypt to pay particular attention, and to take serious actions in this respect. However, Egypt must take into account that many measures still increase the cost of foreign trade transactions, especially in relation to exports. It is important to address these measures to stimulate export growth, such as facilitating licensing, customs clearance procedures and taxation, as well as reducing the cost of financing transactions and the number of required procedures and approvals.

In light of the recent actions taken by the government or the Central Bank of Egypt, it has become necessary to conduct a thorough sensitivity analysis of the effects of changes in the exchange rate on export indicators and on the cost of imports, which have yet to appear in full. It is likely that recent changes in the exchange rate will improve Egypt's competitiveness. But the conduct of a sensitivity analysis of the detailed impact of changes in the value of the US dollar on exports and imports from the different sectors will facilitate developing policies that aim to increase exports and reduce imports.

It is also necessary to finalize and to start implementing a strategy for industrial development. The focus of the export development strategy so far has been on market access procedures and giving incentives for export development, whether through the export refund program or changing the exchange rate without dealing with the larger challenge of production impediments to exports.

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## Global Financial Market Performance

### Reuters/ Argaam

Chinese stock indices declined during Friday trading, marking the worst daily loss since last December, after one day of the Chinese Central Bank's raising of interest rates.

At the end of the session, the "Shanghai" Composite Index fell 0.96 percent, or (-31 points) to 3237 points, while the "CSI 300" index of large companies listed in Shanghai and Shenzhen fell by 1.03 percent or (- 35 points) to 3445 Points.

On the weekly level, the "Shanghai" Composite Index posted 0.8 percent in gains, while "CSI 300" index posted a gain of 0.5 percent.

In an attempt to control capital flows and maintain the yuan stable, the People's Bank of China raised short-term interest rates, hours after a similar move by the US Federal Reserve.

The Japanese stock indexes also fell during Friday trading, following their US counterparts, with markets continuing to absorb the decisions of the Federal Reserve and the Bank of Japan.

At the end of the session, the Japanese "Nikki" index fell by 0.35 percent or 68 points to 19,521 points, while the broader "Topix" Index fell 0.43 percent or 7 points to 1565 points.

In terms of trading, the "Toshiba" share rose 3.54 percent to 190.1 yen at the close, after media reports referred to the company's success in attracting 10 potential buyers for its activities in the field of electronic chips, including US financial institutions.

US stocks stabilized during Friday trading after a volatile session in which investors watched signals from the meetings of the G20 summit and the first meeting between president "Donald Trump" and German Chancellor "Angela Merkel," but the major indexes posted weekly gains.

The "Dow Jones" Industrial Average dropped 20 points to 20,914 points, after gains of more than 35 points, while the "S & P 500" benchmark dropped (- 3 points) to 2378 points, and the "Nasdaq" index rose (0.2 points) to 5901 Points.

On the weekly level, the "Dow Jones" was up 0.1 percent, while the broader "S & P" posted gains of 0.2 percent, and "Nasdaq" posted weekly gains of 0.7 percent.

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In the European markets, the "Stoxx Europe 600" index rose by 0.2 percent or 0.6 percent to 378 points, the highest close since the beginning of December 2015.

On the other hand, Gold futures for April delivery settled up by 0.30 percent, or about \$3.10 to \$1230.20 an ounce. The precious metal recorded a weekly gain of 2.4 percent, the highest since February the third.

In the oil markets, the US crude, "NYMEX", rose less than 0.1 percent or three cents to close at \$48.78 a barrel, posting a weekly gain of 0.6 percent. Also, crude "Brent" index rose less than 0.1 percent, or by about two cents, and closed at \$51.76 a barrel to score a weekly gain of 0.8 percent.

With regards to economic data, US industrial production stabilized in the past month compared to expectations of rising by 0.3 percent.

#### Implications for Egypt:

Global markets overcame the effects of the Fed's decision regarding interest rates despite expectations of similar hikes of the US interest rate over the year, with mostly minor gains during the week.

The Egyptian Stock Exchange achieved market capitalization gains during the trading week of around LE11.7 billion to reach about LE 647.5 billion compared to LE 635.8 billion in the previous week, with a rise of 1.8 percent.

The weekly report of the Egyptian Stock Exchange noted that its main indices rose collectively, with the main EGX30 index rising by 1.02 percent to reach 12,984 points. Secondary market indices also tended to increase, with the EGX70 for small and medium shares rising by 2.65 percent to close at 532 points. The wider EGX100 index rose by about 2.04 percent to reach 1260 points. EGX20 recorded a rise of about 0.94 percent to close at 12,304 points.

The report noted a decline in total value of trading during the week to LE 6.2 billion pounds, while the total volume of trading reached 1.184 billion securities executed over 155 thousand transactions, compared with a total value of trading of LE 12.5 billion and traded volume of 1.653 billion securities executed over 161 thousand transactions during the previous week.

This relative improvement comes after the situation stabilized with respect to the tax stamp on transactions and the initial improvement in foreigners' trading indicators at the Egyptian Stock Exchange because of an appreciating US dollar against the Egyptian pound during the week.

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