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ECES
The Egyptian Center for Economic Studies

Our Economy & the World

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Key Global Developments

How $10 drop in oil prices would affect Saudi economy?

Mubasher

A recent report by the Institute of International Finance (IIF) included scenarios for oil prices over the coming years and the impact thereof on the Saudi economy. The report presented predictions for Saudi economic performance if oil prices dropped by $10 a barrel.

"With still glut in the oil market and the potential of recovery in oil production in Libya and the increase in production in the U.S., lower oil prices remain a possibility," the report noted.

To assess the likely impact on the Saudi economy of lower oil prices, IIF used two scenarios for the period between 2018 and 2025.

In the baseline scenario, oil prices remain constant at $54 per barrel in real terms through 2025.

In the lower oil price scenario, IIF assumed that average oil prices would drop by $10 per barrel (pb).

The baseline scenario provides a relatively sustainable path.

"The fiscal deficit would narrow from 10.5 percent of GDP in 2017 to 3.4 percent by 2025. While government debt-to-GDP ratio would increase to 49 percent of GDP by 2025, it would remain manageable."

"Net foreign exchange reserves, while declining, would remain adequate at $442 billion in 2025, equivalent to 18 months of imports of goods and services."

OPEC and Non-OPEC producers are scheduled to hold discussions on extending oil production cuts on Thursday amid expectations of extending the agreement for an additional six to nine months.

On the other hand, in the low oil price scenario, exports and government revenues from oil would decline by about $30 billion as compared to the baseline scenario. According to this scenario, oil price will drop from $52.2 in 2017 to 43.7 in 2018.

"The fiscal deficits would remain large, government debt-to-GDP ratio would rise to 71.1 percent of GDP by 2025, borrowing costs would increase, and pressure on the peg to the dollar would increase."

"Official reserves would decline rapidly to $158bn by 2025, equivalent to only 6.4 months of imports of goods and services, compared to 28 months in 2017."

Sovereign Wealth Fund Assets down to $7.4 trillion

Argaam

Global sovereign wealth funds have recently been under pressure from lower oil and gas prices, leading to a decline in the value of funds managed by government investment institutions to $ 7.4 trillion, according to the Sovereign Wealth Funds Institute.

Between March 2015 and the same month in 2017, the value of assets overseen by sovereign wealth funds - the source of which is often excess oil revenues - fell by 0.5 percent, compared with a 14 percent increase in the two years to March 2015.

Oil prices fell more than half since their rise in 2014 to about $115 a barrel, to settle near $50 a barrel now, forcing governments to withdraw funds from sovereign wealth funds to support their economies.

Assets of the *Saudi Arabian Monetary* Authority (SAMA), the world's fifth-largest sovereign wealth fund, fell 14 percent to $514 billion in the year ending March 2017.

At the same time, assets of the Russian reserve fund fell by two thirds to $16.2 billion.

EIB offers €2 billion for urban development projects in southern Mediterranean countries

Akhbar Masr

The European Investment Bank (EIB) has invested approximately EUR 2 billion in urban development projects in the southern Mediterranean region since 2011, focusing on key urban infrastructure and mobility projects. The Bank’s strong commitment to support this important sector was reaffirmed during the second Union for the Mediterranean (UfM) ministerial conference held on 21st and 22nd of May 2017 in Cairo on “Sustainable urban development in the south Mediterranean countries”.

Recent examples of the Bank’s operations include the financing of micro and SME investments in conjunction with community development in Egypt, the upgrading of informal settlements and construction of urban railway lines in Tunisia, and construction of the Rabat Tram and the development of Zenata urban development, which is part of a regional development strategy in Morocco.

Report: Beijing's new weapon in economic war

Argaam

Slapping import bans on products like mangoes, coal and salmon has long been China's way of punishing countries that refuse to toe its political line.

But Beijing has shown that it can also hurt others by cutting a lucrative Chinese export: tourists who normally flock to South Korea or Taiwan.

China's recent boycott of South Korea over a US anti-missile shield on the Korean peninsula signals a growing aggression in the way it flexes its economic muscles, analysts say.

China has prevented tourist groups from heading south towards Taiwan or South Korea, causing damage to the tourist market of those countries and adversely affected their retail stores.

The "Trans-Pacific Partnership" countries keep the door open

AFP

As fears rumble of a new global era of protectionism, Asia Pacific trade ministers gathered agreed to exert efforts to save a huge trade deal.

The 12-nation TPP covered 40 percent of the global economy before Trump abruptly abandoned it in January as part of a campaign pledge to save American jobs he said had been sucked up overseas. Australia, Japan and New Zealand are at the forefront of efforts to save the deal, believing the pact will lock-in free trade as well as boost labour rights and environmental protections.

After the morning meeting, New Zealand’s trade minister, Todd McClay, told reporters that the TPP 11 “are committed to finding a way forward to deliver” the pact. Trade representatives in Hanoi have said they are ready to tweak the deal to leave room for a US return, pinning hopes on a U-turn in American policy.

The TPP ministers are meeting on the sidelines of a gathering of trade ministers from the Asia-Pacific Economic Cooperation (APEC). The newly-appointed US trade chief, Robert Lighthizer, attended the two-day gathering, where he was scheduled to meet one-on-one with several ministers, including from China, Canada and Mexico.

Report: OPEC net oil revenues in 2016 were the lowest in 12 years but will rise this year

Argaam

OPEC revenues declined notably in 2016 to the lowest level since 2004.

According to the EIA data, the Organization of the Petroleum Exporting Countries (OPEC) earned about $433 billion in net oil export revenues in 2016, the lowest since 2004. In real dollar terms, the 2016 revenue represents a 15 percent decline from the $509 billion earned in 2015.

EIA projects that OPEC net oil export revenues will rise to about $539 billion in 2017, based on the forecast of global oil prices and OPEC production levels.

For 2018, OPEC net oil export revenues are forecast to be $595 billion.

Saudi Arabia has consistently earned more oil export revenues than any other member of OPEC, with its share in total OPEC net oil export revenues ranging between 29 percent and 34 percent since 1996.

OPEC's revenues came close to the $1 trillion barrier for the first time in its history during the 2008 global financial crisis before falling back in the next two years, while it exceeded $1 trillion in 2011, 2012 and 2013 before falling sharply in 2015.

Implications for Egypt:

We reaffirm that 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, in light of the expected tensions and shifts in movement of global investment flows worldwide as well as the emergence of an escalating trade war between the US and China amid slow global economic growth. Against this backdrop, Egypt has to move more quickly to encourage domestic consumption while supporting its presence in the Arab and African regional markets in order to capture larger market shares in the medium term and to benefit from trade agreements with these countries.

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.

From the International Press

China's economy loses momentum as policymakers clamp down on debt risks

Reuters

China's growth took a step back in April after a surprisingly strong start to the year, as factory output to investment to retail sales all tapered off as authorities clamped down on debt risks in an effort to stave off a potentially damaging hit to the economy.

Data highlighted the broad economic impact of these regulatory curbs, with below-forecast factory output in April and fixed-asset investment in the first four months of the year reinforcing evidence of a weakening manufacturing sector and slowing momentum in the world's second-biggest economy.

Factory output was up 6.5 percent in April from a year earlier, down from 7.6 percent in March, and fixed-asset investment rose 8.9 percent in the first four months of the year, off the 9.2 percent pace in Jan-March.

Analysts polled by Reuters had predicted factory output would grow by 7.1 percent in April, and tipped fixed asset investment to rise 9.1 percent in Jan-April.

Fixed asset investment in the manufacturing sector also slowed over Jan-April, with growth of 4.9 percent down from 5.8 percent in the first quarter. Infrastructure spending, however, continued to grow over 23 percent year-on-year in the same period, supported by Beijing's Belt and Road initiative.

Data showed investment in property development picked up in April, although sales growth was significantly slower, suggesting investment in the sector remained robust even as intensified government controls to rein in the market began to take effect.

The area of property sold grew 7.7 percent year-on-year in April, the lowest since December 2015 and well short of the 14.7 percent increase in March.

Retail sales rose 10.7 percent in April from a year earlier, weaker than March's 10.9 percent gain as home appliances and automobile sales growth slowed from March.

At the same time, growth in the services sector slowed to 8.1 percent year-on-year, down from 8.3 percent growth in March and the slowest since December. The country's first quarter economic growth came in at a faster-than-expected 6.9 percent, the quickest since 2015 on higher government infrastructure spending and a gravity-defying property boom.

China has cut its economic growth target to around 6.5 percent this year to give policymakers more room to push through painful reforms and contain financial risks after years of debt-fueled stimulus.

Implications for Egypt:

Banking indicators show that the Central Bank of Egypt (CBE) continues to implement its announced strategy to strengthen the financial positions of banks; reform the monetary policy and strengthen its integration with the fiscal policy, increasing consistency between them, especially with the establishment and activation of the Coordinating Council for Fiscal and Monetary Policies. The Council plays a structural role in managing the economic process and leading sectoral reforms, resulting in actions and strategies to reduce imports, increase resources, stimulate investment and increase exports.

CBE's recent decision to strengthen banks' financial position is positive because it creates a barrier against any public or private crises. The strong financial position of banks over the past years maintained their position compared to other financial institutions. We believe that the buffer will not affect bank profits due to the annual increases in profits. After setting the buffer aside, profits may be equal to those of the previous year. This will not affect shareholders, while increased reserves will increase the value of banking units at assessment.

Current banking policies need a program to tackle the financial stalemate resulting from the banking process, which began in the aftermath of the global financial crisis in 2009 and increased following the January 25th Revolution. The program will unlock new economic and development capabilities and increase economic growth by restoring the operation of capital and complex investment assets. The different estimates of suspended investments due to stumbling economic activities clearly reflect the magnitude of possible impact on economic growth in the case of supporting monetary and economic policies to end the current financial crisis.

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Special Analysis

Bitcoin Balloons on Overheated Air

Nir Kaissar, Bloomberg

Ever since the dot-com and housing bubbles popped in 2000 and 2008, spotting bubbles has become a national obsession. Investors have spotted bubbles in bonds, credit, equities, gold -- you name it -- over the last several years.

I wouldn’t use the B-word to describe any of those investments -- yet. In fact, I wouldn’t even nominate any of them for Most Likely to Bubble Over. I would give that distinction to a certain cryptocurrency that is quickly making its name and fortune: Bitcoin. Bitcoin has all the attributes of a bubble in the making. First, it’s radically new. It’s a digital payment system that allows users anywhere in the world to transact directly without interference from intermediaries, governments, regulators or central banks -- at least for now. Transactions are administered by a decentralized network of computers, much like the internet.

In his book about the 17th-century tulip bubble in Holland, "Tulipmania," British journalist Mike Dash points out, “It is impossible to comprehend the tulip mania without understanding just how different tulips were from every other flower known to horticulturists in the 17th century.” The same could be said about the internet in the 1990s and about digital currency today. Second, Bitcoin is shrouded in secrecy. Buyers and sellers of Bitcoin can trade anonymously, which makes the digital currency a favorite of criminals and hackers demanding ransom. Its origins are shrouded in mystery. Its creator goes by the name of Satoshi Nakamoto, but it's unclear who that person is or if it's even one person. That, too, is reminiscent of another bubble. At the height of England’s South Sea Bubble in 1720, one company floated shares “"For carrying-on an undertaking of great advantage but no-one to know what it is." Of course, that didn’t stop investors from throwing money at the company.

Riding the Wave

In 1720, share prices of the South Sea Company rose 400 percent in three months and then collapsed just as quickly.

Third, Bitcoin has no value other than what a buyer is willing to pay for it, which makes it susceptible to the argument that underlies all bubbles. Namely, that any price is appropriate. But there’s already reason to worry that Bitcoin's price is excessive. An investment in Bitcoin has returned a breathtaking 351 percent annually since its inception in July 2010. To put that in perspective, an investment of $100 in Bitcoin from the beginning would be worth close to $3 million today. It’s not easy to justify that kind of return for any investment.

Digital Gold

The price of Bitcoin is up 3 million percent since July 2010.

Bitcoin is similar to other currencies and commodities such as gold, oil, potatoes or even tulips in that its intrinsic value is difficult -- if not impossible -- to separate from its price. But there are governments standing behind currencies and reliable currency markets for exchange. And with commodities, investors have something to hold at the end of the transaction. Bitcoin feels more speculative because it’s just digital ephemera.

That isn’t true for all investments. Stockholders are entitled to a share of a company’s assets, earnings and dividends, the value of which can be estimated independent of the stock’s price. The same can be said about a bond’s payments of principal and interest.

This distinction between price and value is what allowed many observers to warn that internet stocks were absurdly priced in the late 1990s, or that mortgage bonds weren’t as safe as investors assumed during the housing bubble. A similar warning about Bitcoin isn’t possible. During the dot-com craze, Warren Buffett was asked why he didn’t invest in technology. He famously answered that he didn’t understand tech stocks. But what he meant was that no one understood them, and he was right. Why else would anyone buy the NASDAQ 100 Index when its price-to-earnings ratio was more than 500 times -- a laughably low earnings yield of 0.2 percent -- which is where it traded at the height of the bubble in March 2000.

Thinking back on investors’ credulity during the last two bubbles, I can’t help but wonder if buyers of Bitcoin understand what they’re invested in. They would be wise to ask themselves that same question.

Implications for Egypt:

The phenomenon of virtual currencies has recently spread in the global economy, most notably bitcoin, which is an encrypted digital currency that is decentralized and is controlled by users only. Bitcoin is not subject to control by entities such as the government or central bank, unlike other currencies in the world. It is not tangible because it cannot be printed, and it is considered an outlet for money laundering.

The Central Bank of Egypt (CBE) Law No. 88/ 2003 prohibits the use of virtual currencies in the country, though this is did not explicitly stipulates. It has been observed recently that many Egyptians use virtual currencies. We believe that users of such currencies subject themselves to fraud due to the use of unsecured online payments, although CBE requires all banks operating in the country, including foreign banks, not to allow payments in virtual currencies, otherwise they will be held accountable. But these transactions are actually carried out outside the banking sector.

The CBE should issue a decision banning the use of all virtual currencies in the country, notably Bitcoin, in order to protect traders from fraud, especially that it is the authority vested with enforcing the foreign exchange law in Egypt.

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Global Financial Market Performance

Argaam/ Reuters

Chinese stocks rose marginally at the end of trading, with gains in newly offered stocks and increased prices of iron ore, despite being pressured throughout the session against the background of economic concerns and losses of courier service providers.
At the end of the session, the Shanghai Composite Index rose 0.10 percent to 3105 points and recorded a weekly loss of 0.1 percent.
SF Holdings led the losses of courier service providers after Alibaba's Cainiao Network said it had asked traders to hire other companies.

For the first time in the Chinese mainland markets, three shares rose on Friday by the maximum of 44 percent. The three companies are involved in the manufacture of automotive equipment, telephone equipment and film production.
The Japanese stocks also rose at the end of trading, driven by the depreciation of the yen against the dollar. The Nikkei index managed to exceed 20 thousand points for the first time since 2015, posting weekly gains and gains at the end of the session. While the Nikkei index rose 1.60 percent to 20177 points, the highest level since August 2015 and posted 2.5 percent in weekly gains, the TOPIX index rose 1.65 percent to 1612 points. This progress comes in line with the increasing demand from investors on Japanese stocks, driven by higher corporate profits to record levels, and continued moderate economic recovery reflected in the data.
US stocks rose on Friday after absorbing the employment situation monthly report and increasing speculations that the Federal Reserve may raise its interest rate just one more time this year. Key indexes hit record highs at closing and posted weekly gains..

The Dow Jones Industrial Average rose 62 points to 21,206 points, while the NASDAQ Composite Index rose (+ 59 points) to 6306 points, and the Standard & Poor's 500 Index rose (+ 9 points) to 2,439 points.
On the weekly level, the Dow Jones posted 0.6 percent in gains, while the NASDAQ index gained 1.5 percent, and the broader S & P 500 recorded weekly gains of 0.9 percent.
In the European markets, the STOXX Europe 600 index rose 0.2 percent or about 1 point to 392.5 points. The FTSE 100 index rose 4 points to 7547 points, while the German DAX rose (+158 points) to 12823 points, and the French "CAC" rose (+ 24 points) to 5343 points.
On the other hand, gold futures for August delivery rose 0.8 percent or $10.10 to $1280.20 an ounce. The precious metal gained around 1 percent this week.
In the oil markets, the US NYMEX fell 1.5 percent or 70 cents to close at $47.66 a barrel, the lowest close since May 10, recording a weekly loss of 4.3 percent, while Brent fell 1.3 percent or 68 cents, closing at $49.95 a barrel and recorded a weekly loss of 4.9 percent.
In terms of economic data, the US economy added 138,000 jobs in May, compared with expectations of 185,000 jobs. The unemployment rate fell from 4.4 percent to 4.3 percent, while the trade deficit rose 5.2 percent to $47.6 billion in April.

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Implications for Egypt:

Global financial markets have been affected by recent economic developments, starting with the negotiations of Greek creditors, the announcement by the US to withdraw from the Paris climate agreement, and the fluctuations witnessed by a number of markets against the backdrop of business results of major companies and the status of their debts.

A report by the Office of Strategic Studies at ADS Securities said positive steps have been taken to revive Trump's economic plan after it faced many challenges and obstacles from the US Congress and the implications of the FBI case. But approval of the draft budget proposal the new Trump administration will present to Congress is a prerequisite for launching the practical phase of the project system intended by the US President.

The report said US companies are the biggest beneficiaries of Trump projects and plans. If implemented, they will be its biggest supporter. This also requires a weak dollar to support Tramp's economic projects, as the US President pointed out last month.

The report pointed out that global financial markets are awaiting a serious clarification about what is happening with the Trump economic projects, with the current stage being very critical as investors are at a crossroads regarding the direction of investment over the coming period. The Fed should also determine the monetary policy the markets are anticipating and whether there will be agreement with the new Trump programs remains to seen.

On the other hand, market capitalization of the Egyptian Stock Exchange increased EGP 7.7 billion during the trading session of the week ended, closing at EGP 678.625 billion, up by 1 percent from last week.

The market capitalization of the Egyptian Stock Exchange gained about 2.7 billion pounds at the close of Thursday trading, the end of the week, to close at EGP 678.625 billion pounds, amid a collective rise of indices.

The total value of transactions traded on the Egyptian Stock Exchange reached LE 1.1 billion during Thursday's trading. The transactions of Egyptian individuals and Arab institutions tended towards selling, with a net of EGP 55.6 million and EGP 45.6 million, respectively. The transactions of Arab and foreign individuals as well as Egyptian and foreign investors tended towards buying, with a net of EGP 8.4 million, EGP 1.8 million, EGP 81.3 million and EGP 9.7 million, respectively.

The EGX30 index rose by 0.96 percent to close at 13,467 points. The EGX50 index rose by 0.72 percent to close at 2,053 points. The EGX20 index jumped 1 percent to close at 12,260 points.

The index of medium and small enterprises, EGX70, rose by 0.33 percent to close at 573 points, and the broader EGX 100 index rose by 0.37 percent to close at 1,369 points.

The Egyptian Stock Exchange got over the approval of parliament of slapping a stamp duty on transactions with an increasing value in light of activity by foreign institutions in the purchase of leading stocks.