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Our Economy & the World

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

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- **Special Analysis: Looming EU-US Divorce … Will China Reap the Benefits**
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Key Global Developments

South Africa has first recession since 2009

Asharq Al-Awsat

South Africa’s economy fell into a recession for the first time since 2009 in the first quarter of 2017, after it contracted for two consecutive quarters.
Gross domestic product receded an annualized 0.7 percent in the first quarter from a contraction of 0.3 percent in the previous three months, Statistics South Africa said in a report.
S&P Global Ratings and Fitch Ratings Ltd. affirmed South Africa’s debt at the highest non-investment grade last week, with both companies saying policy uncertainty, political turmoil and slow economic growth pose a risk to fiscal consolidation.

Trafigura says no impact on gas trading so far from Gulf crisis

Reuters

A political dispute between Qatar and several Middle Eastern countries including Saudi Arabia has had no impact so far on Qatari gas exports, trading house Trafigura said.
"The developments in Qatar have so far not impacted at all our trading business. It's much too early to say if there could be a disruption," Trafigura Chief Financial Officer Christophe Salmon told Reuters.
"We generally see any geopolitical event as an opportunity for trading rather than a threat," he added.
Several Middle Eastern countries, including Saudi Arabia, Egypt and the United Arab Emirates cut ties with the tiny Gulf state on Monday over what they say is Qatar's support for terrorism, an accusation Qatar vehemently denies.
Trafigura has boosted its liquefied natural gas (LNG) trading aggressively in recent years and is a supplier of Qatari gas, including to Egypt.
"The LNG market is an oversupplied market ... the main focus is to secure customers," Salmon said.
"Egypt has been a very good business for us - both on the gas and products side. Last year we had a very significant market share in Egypt. It is lower this year. It's a profitable business but not without a risk, credit risk," he added.
He said Trafigura planned to negotiate access to LNG volumes from Australia, the United States and Africa.

EIA cuts oil price forecast for 2018

Argaam

The U.S. Energy Information Administration lowered its crude-oil price forecast and raised its U.S. production outlook for 2018, according to a monthly report .
The government agency said it expects NAYMEX prices to average $53.61 a barrel next year, down 2.7 percent from its previous forecast. For 2017, it raised its WTI forecast by 0.2 percent to $50.78.
The EIA also said it expects Brent crude to average $55.61 a barrel in 2018, down 2.6 percent from the previous forecast.
U.S. crude production, meanwhile, is forecast at 10.01 million barrels a day for 2018, up 0.4 percent from the previous outlook.

Foreign investors to pour nearly $1 trillion into emerging markets in 2017 –report

Reuters

Non-resident capital inflows to emerging markets should reach $970 billion this year, a 35 percent increase from 2016, the Institute of International Finance said in a report.
The projection follows a strong first quarter for emerging market investment that saw the strongest portfolio inflows since 2014.
The IIF's projection is $290 billion higher than its estimate just four months ago, shortly after Donald Trump took office as U.S. president and the organization listed possible American protectionism as its top threat to emerging market portfolio flow growth.
The IIF projects non-resident inflows to increase by $252 billion this year from 2016.
Non-resident portfolio inflows are expected to rise to more than $1 trillion in 2018, IIF also said, the first time inflows have breached that level since 2014.
Capital inflows from non-residents had fallen to a 12-year low in 2015.
The organization expects resident capital outflows to hit $892 billion this year, a decline by $141 billion from 2016, and for outflows to reduce further in 2018.
Outflows from China alone, which leads emerging market economies in capital leaving local markets, rose to a record $725 billion last year.

World Bank keeps 2017 global growth forecast unchanged

Asharq Al-Awsat

World Bank maintained its forecast for global growth, depending on accelerated pace of economic activity despite trade barriers that the US is threatening to impose.
A bright spot in the outlook is a recovery in trade growth to 2.7 percent (in 2017) and to 2.9 percent in 2018, an increase from the 2.5 percent recorded in 2016, said the World Bank in its flagship Global Economic Prospects (GEP) report.

The IMF was optimistic in mid March and raised its forecasts for global economic growth for the first time in two years.
"For too long, we've seen low growth hold back progress in the fight against poverty, so it is encouraging to see signs that the global economy is gaining firmer footing," Jim Yong Kim, World Bank president, said in a statement.
On the Middle East and North Africa, the bank predicted a growth rate of 2.1 percent in 2017 and a recovery in 2018 to 2.9 percent. The negative impact of OPEC member countries' production cuts on oil-exporting countries slightly exceeds the improved conditions In oil-importing countries. "
In Saudi Arabia, the region's largest economy, growth is expected to fall to 0.6 percent due to production cuts before recovering to 2 percent in 2018, the report said.
In Egypt, the economic growth is expected to decline in the current fiscal year, before improving steadily in the medium term, thanks to the implementation of business climate reforms and improved competitiveness of the economy, the report said.
The report warned that there are significant risks to overshadow these growth prospects, especially because of the protective measures that may be taken by some countries, particularly the United States.
According to the report, increased trade protectionism could derail the trade growth momentum; elevated policy uncertainty could dampen confidence and investment.
The Bank also warned that a sudden reassessment of markets of policy risks or the pace of monetary policy returns in developed economies could lead to financial turmoil.
Over the longer term, the World Bank warned that continued weak productivity and investment growth rates could erode long-term growth prospects in emerging market countries and developing economies, which are key to poverty reduction efforts.
"With a fragile but real recovery now underway, countries should seize this moment to undertake institutional and market reforms that can attract private investment to help sustain growth in the long-term," said Kim.

US productivity flat in first quarter

Argaam

The productivity of American workers was flat in the first three months of this year, while labor costs rose at the fastest pace since the second quarter of last year.
Productivity growth was zero in the January-March quarter but fell 0.6 percent per year in the fourth quarter, the Labor Department reported.
The growth in production or the number of goods and services produced by companies rose to 1.7 percent from 1 percent. At the same time, the number of staff hours was adjusted to slightly increase by 1.7 percent instead of 1.6 percent.
Data showed that labor costs rose at a slower pace than expected, suggesting that companies continue to cut costs despite the steady expansion of the economy and the growing shortage of skilled labor.
Work unit costs rose by 2.2 percent compared to primary data of 3 percent. Over the past year, labor unit costs rose 1.1 percent, well below the historic 2.8 percent since the end of the Second World War.
Hourly wages rose by 2.2 percent in the first quarter, while real wages fell by 0.9 percent. the annual productivity rate was 1.2 percent well below the average of 2.1 percent during 1947 - 2016, or an average of 2.6 percent during 2000 - 2007.

Implications for Egypt:

Attention should be given to the Gulf-Egyptian economic and commercial relations, which are strategic. This requires developing the concept of integration and going beyond the status quo. The establishment of joint economic zones, expanding the scope of bilateral trade agreements and the introduction of new sectors therein such as services, and the establishment of joint industries that are directed to import substitution and dependent on Gulf-Egyptian raw materials will be a basis for developing trade and economic relations over the coming period.

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.

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 recession in Britain 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.

From the International Press

Cotton prices rise and resist counter factors

Asharq Al-Awsat

Despite the decline in the global cotton price in the New York Stock Market over the past few days, it remains high to the end of May by more than 30 percent.

The price of a pound of white threaded yarns rose to 85.57 cents on May 15, then fell last week to about 77.33 cents, prices that were not recorded since June 2014.

At the beginning of the year, the price was between 61 and 63 cents per pound, after it rose by 36 percent in 2016.
Investors, producers and speculators held their breath during the second half of 2016 and the first quarter of 2017, in parallel with China's fulfillment of its promise to dispose part of its huge stock ... there were concerns given that this could affect prices. In 2016, China sold about 3 million tons of its huge stock, which accounted for 60 percent of the world's stock. It announced that it will sell about 3.75 million tons in 2017, a 25 percent increase compared to last year. Since March, China has been carrying out auctions that will continue until the end of the year. However, prices were relatively flat, then they rose.
According to analysts, Chinese manufacturers are buying up because they need 2 million tons a year. Global investors are betting on price rises in parallel to increased demand driven by the global economic growth at higher rates than in previous years.
The Chinese have become market makers in this sector because their stock allow them to have relative control over the course of trading and prices. Total global stock is now estimated at about 10 months of consumption, 19 to 20 million tons. Despite the weekly auctions for sale from its stock, China still has 45 percent of the total stockpile of all the countries that stock ginned cotton. "

In contrast, speculators are betting on lower prices this year, arguing that additional US farmland has entered the production line. Expectations indicate that the US production will rise by 12 percent by end of the coming harvest season. Global production amounts to 24 million tons in 2016, India has surpassed China in production since 2014 to rank first at the world level. and the United States comes in third place, followed by Pakistan and Brazil.
A report by a global committee suggests that cotton prices are spinning in a vicious circle, because talking about producers, exporters and consumers in this sector is unlike talk in any other sector. If India and China produce 46

percent of the world total, they consume 53 percent of that production. If the United States is in the third place in terms of production, it is the first in cotton export.

China used to import 4 million tons a year, but now it imports 4 times less because some textile and clothing factories have moved to other Asian countries where the cost of labor is very low, so Bangladesh and Vietnam are at the top of global importers of raw cotton and yarns.

According to a market expert, the demand for cotton will remain consistent, and may even rise, despite competition from synthetic fibers such as polyester. There are several reasons, including pollution and temperature problems, as well as the sensitivity of many people to garments manufactured from synthetic fibers. Cotton can not be dispensed with as many have predicted, and the expectation is that the next five years may see an increase in demand on the supply side. Since its emergence in the 1960s, the polyester has posed a fierce competition for cotton, and global consumption of cotton has not risen, but rather stood at an average per capita consumption of only 3.2 kg per year.

Pessimists raise questions about the sustainability of cotton growing against synthetic fibers. In 20 years, the use of cotton in textiles and clothing has dropped from 50 percent to only 25 percent, compared to a 500 percent increase in synthetic fibers usage. Producers seek to focus on the so-called "excellent cotton", which has a cultural and developmental identity, pesticides are not used in its growing, it does not drain water resources, and children are not used in its growing.

A segment of farmers and producers are counting on an international action led by 13 major global companies such as H & M, Nike, Levi's, IKEA and others to commit to using organic cotton in their products by 100 percent to promote sustainable development in producing countries, and combat pollution resulting from environmentally poor methods in agriculture and production. The companies that signed the commitment in London last week consume 300,000 tons a year.

The document states commitment until year 2525 to the cultivation of organic cotton, especially in developing countries, and to protecting the environment. Organic agriculture reduces emissions that exacerbate global warming, reduces water consumption and preserves the soil. If there is a future for this sector, it is embedded in those undertakings that return the white thread to its luster and nobility.

Implications for Egypt:

Egypt used to lead the production of long-staple cotton and high-length in the world. The Egyptian cotton was a key pillar for the national economy, when Egypt was growing 2 million feddens, reduced in recent years to less than 10 percent due to the drop in global demand for ready-made garments and textiles made of long-staple cotton. Also, some countries developed cotton breeds to compete with Egyptian cotton in spinning characteristics and productivity per fedden, such as the American pima cotton. There is also the deterioration of public sector companies, lower private sector participation and lack of strong foreign investments necessary to absorb the domestic production of cotton, in addition to the high cost of harvesting, transportation and labor. There is also the difficult competition from China, India and Pakistan in the cotton textile industry and the deterioration in Egyptian cotton quality.

Addressing the current situation in the Egyptian cotton market requires an integrated package of procedures, most importantly:

- Formulating a new strategy for managing the Egyptian cotton in light of global developments, the change in the behavior of the Egyptian cotton in the export markets and the technological changes in the textile industry.

- Proposing new marketing methods that would contribute to increasing cotton exports and restoring its share in the global market.

- Studying methods of improving the productivity of the Egyptian cotton, benefiting from the success stories of countries that increased their cotton productivity. This will help increase farmer revenues and stimulate farmers to grow cotton on the appropriate dates, thus reducing the risk of being affected by pesticides.

- Developing a program through the Ministry of Agriculture to improve the quality of long staple Egyptian cotton lost due to poor agricultural extension and overlapped breeds. The main reason for the inability to market long staple cotton is its poor quality.

- Establishing a new relationship between the state and the farmer by providing non-financial support, technical assistance and guidance for the cotton crop.

- Introducing new breeds of long-stapled and short-lived cotton, especially that current market conditions put an end to the adherence to growing low productivity breeds, while no longer getting the price discrimination that deserves this adherence. The cultivation of short-lived cotton will also contribute to the cultivation of other winter crops before planting.

- Developing a strategy for improving local cotton gin spindles appropriate for the new breeds that will be introduced.

Special Analysis

Looming EU-US Divorce … Will China Reap the Benefits

CNN

The United States and Europe appear to be hurtling toward a messy breakup. China, meanwhile, is ready to pounce. Beijing is in prime position to capitalize on major policy fissures that have emerged between Europe and the Trump administration on climate, trade and defense.

The new dynamic will be on full display on Thursday in Brussels, when Chinese Premier Li Keqiang meets with EU counterparts at the annual EU-China Summit. Hours later, President Trump is expected to announce the withdrawal of the U.S. from the Paris climate agreement.

"If peace and prosperity are the object of the global economic order, the Trump administration offers neither to Europeans," wrote analysts at High Frequency Economics, a research firm. "A new axis of power, based on economic power, will form between Europe and China if the U.S. continues to shirk its role as global leader".

A closer relationship between the two giant economies is easier said than done, however. There are major questions over the compatibility of the economic systems promoted by Europe and China, as well as differences over flashpoint issues including human rights.

With the United States fueling fears of protectionism, Brussels and Beijing are advocating free trade. But that doesn't mean they're on the same page.

Chinese President Xi Jinping has styled himself as a defender of globalization, making a keynote speech at Davos and hosting an international summit about China's grand plan to foster more trade.

Top European leaders were absent from a Beijing summit in May that focused on the plan, and a key lobby group expressed doubts publicly.

"Trade must flow in both directions to make the new trading routes both economically viable and politically acceptable to the foreign countries through which it will pass," Jorge Wuttke, the president of the EU Chamber of Commerce in China at the time, wrote in an opinion article for the Financial Times.

He said that for every five trains full of cargo that leave the Chinese city of Chongqing for Germany every week, only one full train returns.

One of the most sensitive issues in the EU is the increasing number of European companies being bought up by Chinese firms.

Chinese direct investment in EU countries soared 77 percent last year to $35 billion, according to a study by Rhodium Group and the Mercator Institute for China Studies. That's more than five times the total for 2013.

By contrast, direct investment from EU companies in China dropped to $8 billion in 2016, the fourth consecutive year of decline.

Implications for Egypt

According to a report by CNN Money published by Argaam, German Chancellor Angela Merkel said that Europe must fight for its future and fate. She made these comments after the recent G7 summit, which was dominated by friction with President Trump about climate, trade and defense. "We Europeans truly have to take our fate into our own hands," she said.

This statement indicates that Trump, who questions the utility of the Atlantic alliance and encouraged the UK to leave the EU, is rallying political leaders of the old continent to converge with each other.

But EU member states are very different on how to solve the EU's structural problems due to the euro-zone debt crisis, while divisions between rich nations in northern Europe and southern countries, plagued by deteriorating public finances and rising unemployment, are widening.

In January, Emmanuel Macaron, who was elected president of France earlier this month, said: "The truth is that we have to collectively realize that the euro is incomplete and cannot go without major reforms and that Berlin has benefited from the currency by using it such as a "weak DM".

Macron wants to create a "fiscal union" with a common budget for the euro area and will use this budget for investment and emergency economic assistance to member countries. Germany, which boasts the strongest economy in the region, resists this idea for fear of using such a union to transfer funds to the poorest countries.

To be sure, Britain's exit from the EU, which will continue to be negotiated over the next two years, as well as Trump's surprises about trade, climate and security can distract attention from reforms in the EU.

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.

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Global Financial Market Performance

Argaam/ Reuters/ Al-Youm El-Sabe'

Chinese stocks rose at the end of the session, following data on producer and consumer price inflation, and recorded the best weekly gains from April.

At the end of the session, the Shanghai Composite Index rose 0.25 percent to 3,158 points, recording a weekly gain of 1.7 percent, the strongest gain since April.

Official data showed that China's producer price index rose 5.5 percent in May on an annual basis, compared to expectations of a 5.6 percent rise and after a 6.4 percent growth in April.

Data also showed that consumer prices rose 1.5 percent in the same period as expected, after growing by 1.2 percent in April.

Analysts believe that political developments around the world will positively affect the Chinese market, unlike most of the world markets, citing China's political stability and calmness.

Japanese stocks also rose at the end of trading, with the yen falling against the dollar and following comments by the central bank governor on inflation, but recorded weekly losses.

At the end of the session, Japan's Nikkei rose 0.50 percent to 20013 points, but recorded weekly losses of 0.8 percent, while the TOPIX rose 0.10 percent to 1,591 points.

The country's industrial activity grew by 1.2 percent in April from expectations of only 0.5 percent growth, while M2 rose 3.9 percent in May from 4.3 percent.

Bank of Japan Governor Haruhiko Kuroda said his country had escaped the downturn but still had much to gain before reaching its goal of raising inflation to 2 percent.

On the other hand, the performance of US stocks changed after rising on Friday. The Dow Jones jumped to a new closing record, while the impact of Apple's weak performance reflected on NASDAQ, which recorded the biggest daily loss since May 17.

The Dow Jones Industrial Average rose 89 points to 21,272 points, the NASDAQ fell 2 percent or 114 points to 6208 points, and the Standard & Poor's 500 index fell 2 points to 2431 points.

On a weekly basis, the Dow Jones industrial average gained 0.3 percent, while NASDAQ recorded a 1.6 percent loss, and the broader S & P recorded weekly losses of 0.3 percent.

In the trading session, Apple (AAPL.O) fell 3.8 percent to $148.9 after a report that the next version of iPhone will include chips that are less rapid in downloading data from competing mobile phones.

In Europe, the STOXX Europe 600 index rose 0.3 percent or one point to 390 points, but recorded weekly losses of 0.6 percent.

The British FTSE 100 index rose 77 points to 7,527 points, while the German DAX rose 102 points to 12,815 points, and France's CAC rose 35 points to 5299 points.

On the other hand, gold futures for August delivery fell by 0.6 percent or $8.10 to $1271.40 an ounce. The precious metal recorded losses of 0.7 percent this week.

In the oil markets, the US NYMEX rose 0.4 percent or 19 cents to close at 45.83 dollars a barrel, recording a loss of 3.8 percent this week. Brent climbed 0.6 percent or 29 cents to close at 48.15 dollars a barrel, recording weekly losses of 3.6 percent.

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Our Economy & the World

Markets absorbed the results of the general election in Britain, which resulted in conservatives losing the majority and a suspended parliament, turning attention to the Federal Reserve meeting next week to decide on the interest rate.

Implications for Egypt:

A report by the Office of Strategic Studies at ADS Securities said that the US labor market is witnessing further positive development in line with the strength of the economy, which has been growing in various sectors for two years. The report also noted that the recently published data about US jobs were lower than expected and were treated by financial markets in a negative light, but in fact they are positive and reflect the strength of the US labor market.

The US dollar is affected by job-report tensions and the investigations of former US FBI director, as investors await the implications thereof on Trump's economic projects and his proposals to Congress such as tax cuts, budget and so on. The euro has gained new levels against the US dollar as the positive atmosphere continues in the Eurozone, whose economy is making notable progress over the previous period. But the euro continues to be affected by the divergence of positions of the European Central Bank's (ECB), which suggests a hike in growth expectations but at the same time intends to cut the inflation target until 2019. This led to a lack of clarity among investors regarding the future of monetary policy of the ECB.

On the other hand, the market capitalization of the Egyptian Stock Exchange increased to EGP 7.71 billion during the week, ending at EGP 686.339 billion. Its gross profit since the beginning of the holy month of Ramadan has increased by EGP 15.4 billion to close at EGP 686.339 billion amid a collective rise of all indices.

The total value of transactions traded on the Egyptian Stock Exchange reached EGP 1.8 billion during Thursday's trading session. The transactions of Egyptians, Arabs and Arab institutions tilted toward selling, with a net value of EGP 140.2 million, EGP 794 thousand and EGP 23.6 million, respectively. The transactions of foreigners, and Egyptian and foreign institutions tilted toward purchasing, with a net value of EGP 5.9 million, EGP 155.3 million, EGP 3.5 million, respectively.

The EGX30 index rose 0.37 percent to close at 13,683 points. The EGX 50 index rose 0.64 percent to close at 2,095 points. The EGX20 index jumped 0.25 percent to close at 12,483 points. The index of small and medium enterprises "EGX70" rose by 0.54 percent to close at 609 points, and the broader "EGX 100" index by 0.46 percent to close at 1,435 points.

The Egyptian Stock Exchange benefited from the activity of foreign institutions during the week, driven by re-formation of portfolios and financial positions in the market, which raised the average values of trading during the week.