

# Market Review and Outlook

NCB Weekly Views on Global, Regional and Local Economic and Financial Developments

November 22, 2009

## Special Focus: The Unfounded Fear of Inflation

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### Saudi Arabia Leading Economic Indicators

	2008	Latest	Period
Average WTI, Cushing 1M, USD/bbl	99.67	60.4	09YTD
Weighted Average Arabian Light, USD/bbl	94.8	58.0	09YTD
Average 3M USD LIBOR	2.93%	0.74%	09YTD
Average 3M SAR SAIBOR	3.41%	0.93%	09YTD
Average Spread, in Basis Points, SAIBOR-LIBOR	48.2	19.0	09YTD
Y/Y Growth in Monetary Base (M0)	-0.35%	16.8%	Aug09
Y/Y Growth in Money Supply (M3)	17.6%	12.3%	Aug09

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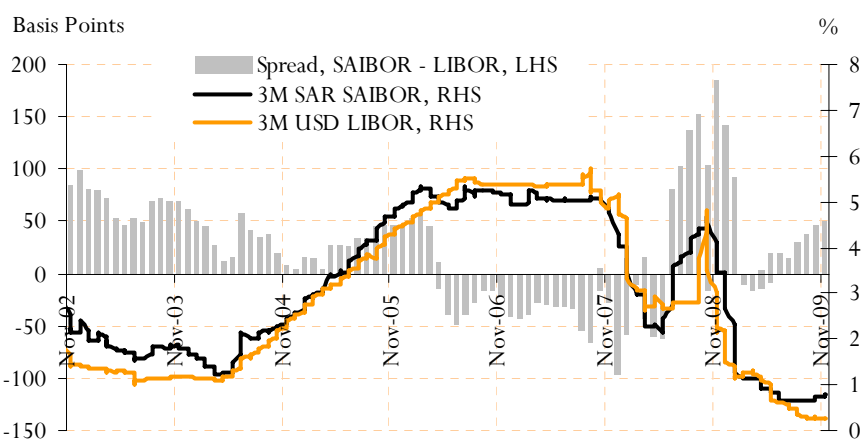
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### Saudi Arabia Liquidity and Risk Detector



Sources: Reuters and NCB

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# Saudi Macro and Equity Market

## Saudi Fast Food Sector is Enjoying Rapid Growth

Changes in the lifestyles and demographics of affluent economies have resulted in increasing demand for fast foods over the last 10 years. KSA is no exception to this trend. In 2008, the Kingdom's consumers made purchases of fast foods (both Arabian delicacies and Western styles) valued at SAR12bn, which is about 10.2% of total food and beverage market. Saudi Arabia currently accounts for 75% of fast food consumption in the Gulf. This increase in demand has been stimulated by increasing personal incomes, more prosperous lifestyles and steady developments in Kingdom amidst the global economic downturn. Given the total population of 24.8mn, of which nearly 54.5% fall below the age group 29 years, average per capita expenditure on the purchase of fast foods reached SAR485, or SAR1.33 per person per day in 2008 and is expected to rise by about SAR639 in 2012. The demand for fast foods is further fueled by booming Hajj industry with more than 4 mn pilgrims expected to visit Kingdom in the coming years and creating seasonal demand for fast food worth around SAR2bn per annum. Going forward, the combined business size of the fast foods is expected to rise by nearly 6% annually to reach SAR17.6bn by 2012.

### Key Macroeconomic and Equity Market Indicators

	Last	Previous	Y/Y Growth in Credit (Private Sector)	Tadawul All Share Index: 31 Dec 08 = 0%
	YTD	2008		
Oil Price, \$bbl <sup>1</sup>	58.0	94.8		
	Sep	Aug		
Oil Production, mmbd <sup>2</sup>	8.1	8.12		
	2008	2007		
Real GDP	4.4%	3.3%		
	Sep	Aug		
CPI Inflation, Y/Y	4.4%	4.1%		
	Sep	Aug		
Broad Money (M3), Y/Y	12.5%	12.3%		
	Sep	Aug		
Credit, Private Sector	2.0%	4.7%		
	2Q09	1Q09		
Credit, Corporate	9.1%	25.0%		
	2Q09	1Q09		
Credit, Households	-0.7%	-2.6%		
	Sep	Aug		
Net Claims on Government <sup>3</sup>	-156.64	-736.88		
	Sep	Aug		
Loan-to-deposit Ratio <sup>4</sup>	79.2%	79.4%		
	Sep	Aug		
Excess Reserves/Total <sup>5</sup>	58.4%	57.5%		
	9M2009	9M2008		
Import LCs, SARbn <sup>6</sup>	90.34	140.29		

Sources: SAMA, Reuters.

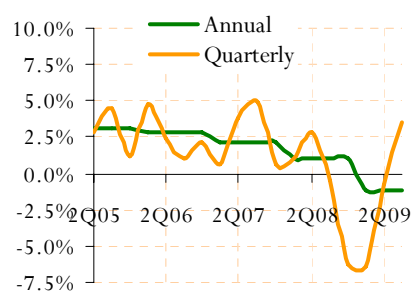
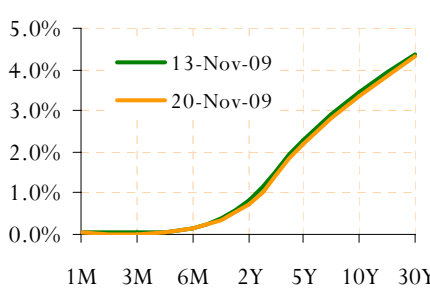
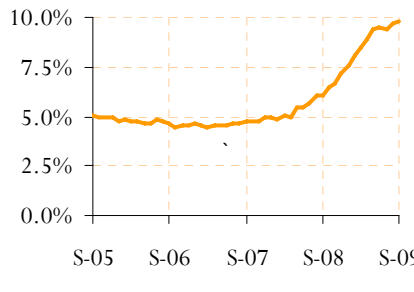
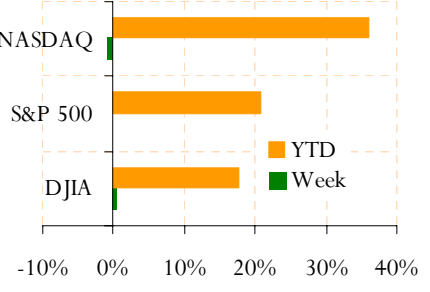
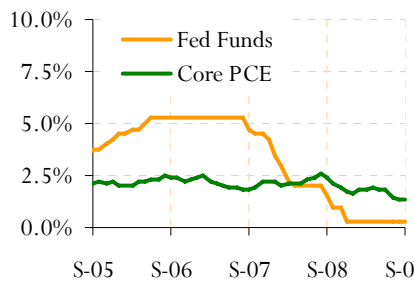
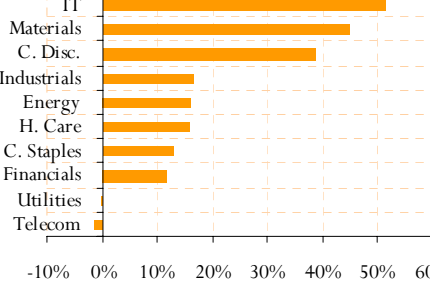
Notes: 1/Oil price: Weighted Average Arabian Light. 2/Oil production: Million barrels per day of crude oil. 3/Net claims on government: Banking sector claims on the central government less central government deposits in the banking system in SAR bn. 4/Loan-to-deposit ratio: The ratio of bank claims on the private sector (excluding investments in private securities) to total deposits, as reported on the consolidated balance sheet of banks. 5/ Excess reserves/total: The ratio of excess reserves held by commercial banks in SAMA to total bank deposits in SAMA. 6/ Import LCs: The cumulative value of letters of credit opened by banks to finance private sector imports.

# US Macro and Equity Markets

## The Unfounded Fear of Inflation

We have already outlined in last week's section that the steepening of the yield curve, with the short-end falling more than the long-end, is a symptom of banks aggressively buying short-term securities to boost their balance sheets by year-end. We also mentioned that this might be a reflection of investors' fear of inflation, given the Fed's commitment to keep rates low for an "extended period". So, should we be concerned about inflation? A large fiscal deficit and solid economic recovery over the next two years will eventually lead to inflation in the US, but not for now. It is difficult to see any inflation pressures in the near-term, given the currently high unemployment rate (10.2%) and low capacity utilization level (70.7%). These are not suitable conditions for a demand-pull scenario. Admittedly, headline inflation rose from -1.3% Y/Y to -0.2% Y/Y in Oct (due to a slight increase in energy prices and base effects from late 2008), while core inflation strengthened to 1.7% Y/Y. Nevertheless, core inflation will likely moderate ahead, as wages decelerate and business pricing power remains weak. So, while the Fed plans to pull-out gradually from quantitative easing in 2010, it will not raise key interest rates before 2011.

## Key Macroeconomic and Capital Market Indicators

	Latest	Next		
	3Q09(A)	4Q09(P)		
Real GDP	3.50%	24-Nov	Real GDP Growth, Annualized	Benchmark Yields, Annualized
	Oct	Nov		
Unemployment	10.20%	4-Dec		
	Oct	Nov	National Unemployment Rate	Benchmark Equity Indices
A. H. Earnings, M/M	0.30%	4-Dec		
CPI Inflation, Y/Y	-0.20%	16-Dec		
	Sep	Oct	Target Fed Funds Rate/Core PCE	MSCI US Sector Indices
Core PCE, Y/Y	1.30%	24-Nov		
Existing Home Sales, M/M	9.4%	23-Nov		
	Sep	Oct		
Housing Starts, M/M	0.5%	23-Nov		
	Sep	Oct		
Trade Balance, \$bn	-36.47	11-Dec		
	Oct	Nov		
Retail Sales, M/M	1.40%	16-Dec		
	Oct	Nov		
Industrial Production, M/M	0.1%	15-Dec		
	Oct	Nov		
Capacity Utilization	71%	15-Dec		
	Oct	Nov		
Fed Funds Rate	0.25%	14-Dec		
	Sep	Dec		

Sources: Reuters, Bureau of Labor Statistics (BLS), and Bureau of Economic Analysis (BEA).

Notes: A/ Advance estimate, P/Preliminary estimate, F/Final estimate.

# Commodity Markets

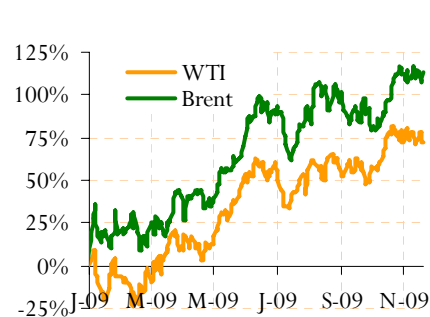
## The Tides May Finally Be Beginning To Turn for Wheat

Wheat prices edged higher in November to reach USD560 cents a bushel, a 3.8% increase over the week. However, market watchers are concerned the latest rally is not justified by fundamentals. The big driver of the market has been outside fund investments urged on by low US interest rates and the weakening dollar. Investors with access to cheap money are eyeing wheat as they look to catch the next wave of the commodities rally. Inflows into ETFS wheat, a product which tracks wheat futures trends, have more than doubled since May to a cumulative total of USD140 mn. Meanwhile on CBOT, the world's largest grain exchange, wheat prices were trading at five-month highs on Wednesday, up 30% from two and a half year lows set two months ago. In its report the World Wheat Council raised world wheat production estimates by 136 mn bushels to 24.7 bn bushels. On a positive side, world wheat usage was also raised to 23.8 bn bushels. As the year goes on, record demand will help put more fundamental strength into the market. In the meantime producers should top up sales on near term rallies and look to protect against another slump below USD500 cents.

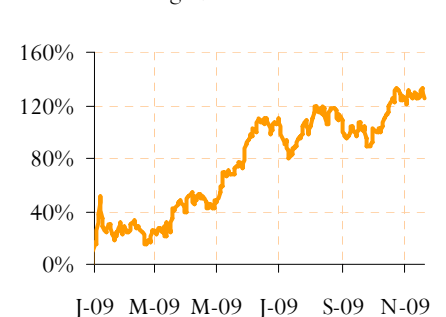
### Key Commodity Prices and Indices

	Last	Week
	20-Nov	%
WTI, Spot, \$/bbl	76.8	0.6
	20-Nov	%
Brent, Spot, \$/bbl	75.9	1.2
	20-Nov	%
Gold, LME, \$/Oz	1149.6	2.7
	20-Nov	%
Silver, LME, \$/Oz	18.5	6.2
	20-Nov	%
Platinum, \$/Oz	1444.5	3.8
	20-Nov	%
Palladium, \$/Oz	362.0	2.4
	20-Nov	%
Aluminum, LME, \$/t	2033.0	4.8
	20-Nov	%
Copper, LME, \$/t	6845.0	5.0
	20-Nov	%
Nickel, LME, \$/t	16600.0	3.1
	20-Nov	%
Zinc, LME, \$/t	2255.0	3.7
	20-Nov	%
Wheat, Dec, \$/Bushel	5.6	3.8
	20-Nov	%
Com, Dec, \$/Bushel	3.9	0.1
	20-Nov	%
Soybeans, Jan, \$/Bushel	10.5	6.0

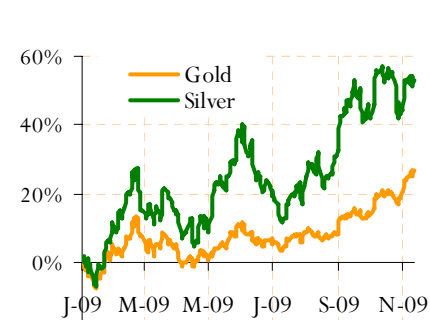
Benchmark Crude Oil Prices



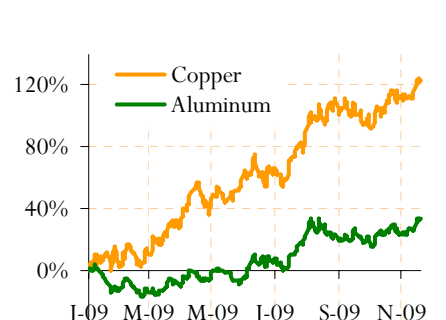
Saudi Arabian Light, Asia Deliveries



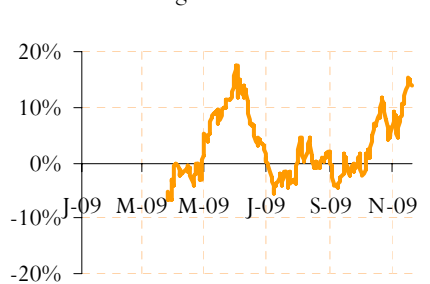
Precious Metals



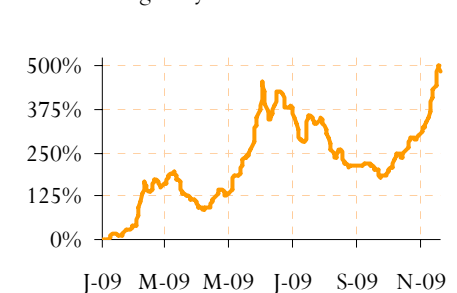
Base Metals



Goldman Sachs Agriculture Index



Baltic Exchange Dry Index



**Notes:** All variables depicted in the charts above are rebased to 0% in the last trading day in 2008.

# Global Macro

## Policy Tensions Ahead

The UK economy has been heavily impacted by the financial crisis owing to its highly leveraged financial sector, overheated property market and high household debt-to-income levels. Accordingly the Bank of England engaged in aggressive monetary policy, slashing interest rates to a low of 0.5% and embarking on the policy of quantitative easing. Until date the committee has unanimously agreed to inject GBP175 bn into the economy through asset purchases in hope to avert systemic risk. However, recently, a divide has emerged between policy makers over the suitability of extending the bond purchase program by GBP25 bn. The majority favored an expansion of liquidity to hedge against risks to growth, as GDP remains weak, having declined at an annual rate of 5.2% in 3Q09. While the proposition did pass, one member stressed that monetary policy was already extraordinarily stimulatory and a further expansion could trigger unwarranted rises in some asset prices. This divide, the first since Aug08, is indicative of forthcoming tensions regarding the future of monetary policy. Having exited economic free-fall, the trade-off between unemployment and inflation becomes a paramount issue dividing policy makers.

### Selected Global Macroeconomic Indicators

	Growth*			Inflation*			Policy Rate*			Policy Rate Change
	2007	Last	Period	Last	Date	Target	Last	Decision	Date	Cumulative 09YTD
<b>Europe/Japan/Oceania</b>										
Euro Zone	2.6%	-4.8%	3Q09	-0.1%	Nov-09	2.0%	1.00%	Hold	5-Nov-09	E. Zone
UK	3.0%	-5.2%	3Q09	1.5%	Nov-09	2.0%	0.50%	Hold	5-Nov-09	UK
Japan	2.4%	3.7%	2Q09	-2.3%	Oct-09	0-2.0%	0.10%	Hold	19-Nov-09	Japan
Australia	4.0%	0.6%	2Q09	1.5%	Jul-09	3.0%	3.50%	0.25%	3-Nov-09	Australia
New Zealand	3.2%	-2.1%	2Q09	1.7%	Sep-09	3.0%	2.50%	Hold	28-Oct-09	NZ
<b>Latin America /Caribbean</b>										
Mexico	3.2%	-8.1%	3Q09	6.3%	Nov-08	3.0%	4.50%	Hold	16-Oct-09	Mexico
Brazil	5.7%	-1.2%	2Q09	0.3%	Nov-09	4.0%	8.75%	Hold	21-Oct-09	Brazil
Chile	5.1%	-1.6%	3Q09	0.0%	Nov-09	3.0%	0.50%	Hold	13-Nov-09	Chile
<b>Asia/Southeast Asia</b>										
China	11.9%	8.9%	3Q09	-0.5%	Nov-09	4.80%	5.31%	-0.27%	22-Dec-08	China
India	9.0%	6.1%	1Q09	-0.1%	Sep-09	5.50%	5.50%	-1.00%	2-Jan-08	India
Hong Kong	6.4%	-2.4%	3Q09	-1.6%	Sep-09	-	1.50%	-0.50%	30-Oct-08	H. Kong
Singapore	7.7%	0.8%	3Q09	-0.4%	Oct-09	-	-	-	-	Singapore
South Korea	5.0%	0.6%	3Q09	2.0%	Nov-09	3.50%	2.00%	Hold	12-Nov-09	S. Korea
Indonesia	6.3%	6.1%	3Q08	2.6%	Nov-09	7.00%	6.50%	Hold	4-Nov-09	Indonesia
Thailand	4.9%	-4.9%	3Q09	0.4%	Nov-09	3.50%	1.25%	Hold	21-Oct-09	Thailand
Malaysia	6.3%	-1.2%	3Q09	-1.6%	Oct-09	-	1.25%	Hold	26-Aug-09	Malaysia
<b>Eastern Europe /Central Asia</b>										
Russia	8.1%	-8.9%	3Q09	0.0%	Oct-09	8.50%	6.75%	1.00%	28-Nov-08	Russia
Turkey	4.6%	-7.0%	2Q09	5.1%	Nov-09	-	6.50%	-0.25%	19-Nov-09	Turkey
<b>Middle East/Africa</b>										
Saudi Arabia	3.4%	4.5%	2008	4.4%	Sep-09	-	2.00%	-0.50%	19-Jan-09	KSA
Kuwait	9.9%	6.3%	2006	11.1%	May-08	-	4.25%	-0.25%	30-Oct-08	Kuwait
Qatar	8.0%	8.5%	2007	14.8%	Mar-08	-	5.50%	Hold	20-May-08	Qatar
UAE	9.4%	5.2%	2007	11.1%	2007	-	1.50%	-0.50%	8-Oct-08	UAE
Oman	7.2%	6.0%	2007	13.2%	May-08	-	2.00%	Hold	20-May-09	Oman
Bahrain	7.9%	6.5%	2006	4.4%	Oct-08	-	0.75%	Hold	21-May-09	Bahrain
Jordan	8.1%	6.2%	2007	13.3%	Jun-08	-	6.00%	-0.50%	25-Nov-08	Jordan
Egypt	6.9%	7.1%	2006/07	21.5%	Sep-08	-	10.50%	-0.50%	30-Jul-09	Egypt
South Africa	5.0%	-2.8%	2Q09	6.1%	Oct-09	3-6%	7.00%	Hold	19-Nov-09	S. Africa

**Notes:** 1/ Growth: Real GDP Growth Rate, 2007: Y-o-Y % change in full year GDP, Last/Period: Quarterly GDP growth rate annualized unless otherwise indicated. 2/ CPI Inflation: Y-o-Y % Change in CPI, Target: Central bank/monetary authority inflation target. 3/ Policy Rate: Last: Current policy rate, Decision/Date: Decision taken in latest meeting/Date of latest meeting.

# FOREX Market

## GBP Under Pressure

While other central banks (CBs) are poised to begin unwinding monetary easing measures, the BOE has announced that it will inject a further GBP25 bn into its economy. This raises the total of asset purchases to GBP200 bn, equivalent to 16% of GDP. Is this the BoE's last step on the path of quantitative easing? Officials have stated that the door to further easing remains "slightly ajar". Accordingly we expect the interest rate to remain exceptionally low, and although unlikely, do not rule out any expansion of liquidity. This carries implications for the direction of the GBP, which has only started to recover from its significant depreciation in 1Q09. Over the short-term, the increase in money supply will likely exert downward pressure on the GBP. Moreover, the policy carries a significant risk to the CB's balance sheet, as it threatens fiscal sustainability. The HM Treasury, which has already forecasted that net government debt will amount to 55.4% of GDP in 2009-10 and rise to 76.2% by 2013-14, will have to raise forecasts in its next pre-budget report. Over the long term, without a credible commitment to reverse the deterioration in fiscal position, the high debt level will exert downward pressure on the Sterling.

## Key Spot Foreign Exchange Rates

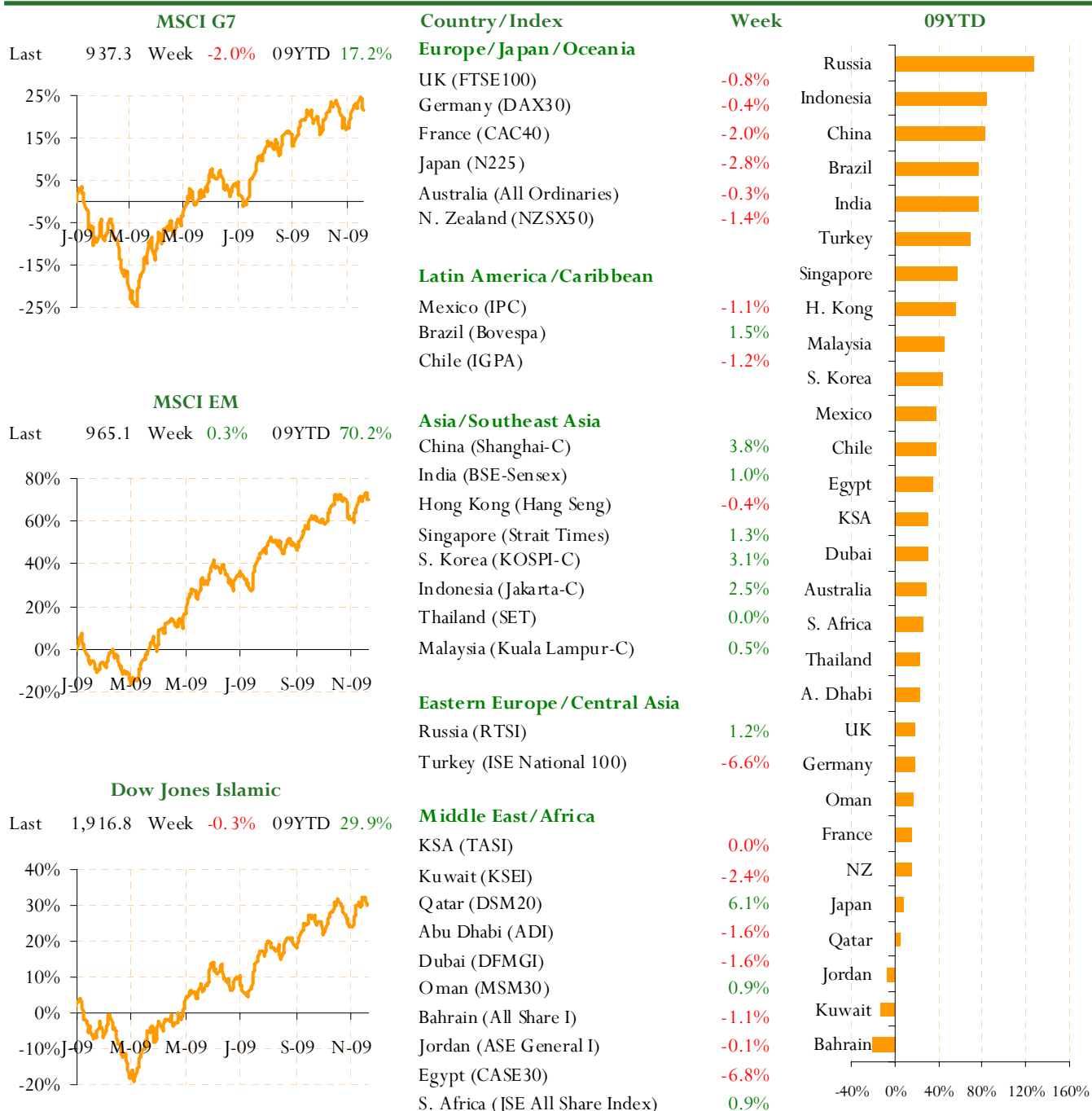
\$ per €		Rate versus \$	Last	Week	
Last 1.4863	Week -0.4%	09YTD 6.3%	<b>Europe/Oceania</b>		
		Swiss Franc (CHF)	1.0179	-0.6%	BRL
		Australian Dollar (AUD)	0.9158	-1.9%	AUD
		New Zealand Dollar (NZD)	0.7250	-2.6%	CLP
		<b>Latin America/Caribbean</b>			ZAR
		Mexican Peso (MXN)	13.0785	-0.4%	NZD
		Brazilian Real (BRL)	1.7330	-0.7%	IDR
		Chilean Peso (CLP)	501.7000	0.1%	KRW
		<b>Asia/Southeast Asia</b>			RUB
		Chinese Yuan (CNY)	6.8280	0.0%	THB
		Indian Rupee (INR)	46.6000	-0.9%	CHF
		Hong Kong Dollar (HKD)	7.7505	0.0%	MXN
		Singaporean Dollar (SGD)	1.3889	-0.2%	INR
		South Korean Won (KRW)	1,159.90	-0.2%	SGD
		Indonesian Rupee (IDR)	9,475.00	-1.0%	TRY
Thai Baht (THB)	33.2300	0.1%	MYR		
Malaysian Ringgit (MYR)	3.3870	-0.3%	EGP		
		<b>Eastern Europe/Central Asia</b>			JOD
		Russian Rouble (RUB)	28.9966	-0.4%	SAR
		<b>Middle East/Africa</b>			QAR
		Turkish New Lira (TRY)	1.4995	-1.4%	BHD
		Saudi Riyal (SAR)	3.7503	0.0%	OMR
		Kuwaiti Dinar (KWD)	0.2857	-0.2%	AED
		Qatari Riyal (QAR)	3.6411	0.0%	HKD
		UAE Dirham (AED)	3.6732	0.0%	CNY
		Omani Riyal (OMR)	0.3850	0.0%	KWD
		Bahraini Dinar (BHD)	0.3770	0.0%	
		Jordanian Dinar (JOD)	0.7090	0.0%	
		Egyptian Pound (EGP)	5.4578	0.0%	
South African Rand (ZAR)	7.6190	-2.5%			

# Global Equity Markets

## FTSE 100: Testing Levels

This week the UK's FTSE breached the 5300 level, last reached in Sep before the collapse of Lehman Brothers. Although the index did close lower at 5251.4, the flirting with significant psychological barriers reflects a marked improvement in investor confidence. Until date the FTSE has increased a hefty 18.4%, in par with the performance of its European counterparts. Among the drivers of this slower paced rally are miners and financials, which have both benefited from renewed risk appetite among investors. Miners have taken the lead, as a weaker USD increases metal prices, boosting profitability. On the financial side, banks have reported improved 3Q09 earning mainly because: 1) most banks have taken various measures to improve their capital positions and rebuild public confidence, and 2) banks have undergone extensive stress tests and have received much support from the government, particularly in the removal of toxic assets, allowing them to improve their balance sheets and move forward. Nevertheless, downside risks are still prominent and the recovery remains fragile. More importantly, the stock market is still driven by sentiment and speculation, rather than fundamentals, rendering the future path uncertain.

## Major Global Equity Markets and Indices, Local Currency (LC) Terms



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