Weekly Update

C0 | EXTERNAL PUBLICATION

Power grab or purge in Riyadh?


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Since June's lows for the year to date, oil prices have rallied hard, taking Brent up over 40% to a two-year high above USD 60 per barrel. Has the oil market entered a new bull market?

One of the driving factors behind the rally has been the steady improvement registered in global economic growth. Investors have begun to speculate that this would shift the market balance away from the oversupply which has depressed prices since the peak in mid-2014. However, supply/demand data do not suggest so far that there are bottlenecks in supply. As illustrated by the left-hand chart, the oil supply still outstrips rising demand. In addition, this week's EIA report showed a rise in crude oil inventories, which remain well above the average for the last decade.

Another supportive factor for prices has been the agreement signed between major OPEC producers – led by Saudi Arabia – and non-OPEC members – such as Russia – to cut output by 1.8m b/d. Compliance with the quotas has been patchy, but EIA data show that recent well closures for maintenance work in Russia and Azerbaijan have enabled targets to be reached in the last two months. In addition, Riyadh and Moscow have signalled willingness to extend the quotas through to end 2018.

Then last week-end brought news of an ostensible crackdown on corruption in Saudi Arabia. Large numbers of members of the royal family and business leaders have been imprisoned and their assets frozen, in line with earlier statements by the Crown Prince that no-one should be above the law. Whether this proves to be an attempt to reduce the extended royal family's influence and consolidate power with the King and Crown Prince or a pre-emptive move to quell protests against corruption, the balance of power has shifted in the Persian Gulf. This has fostered fears that regional instability will lead to supply disruptions.

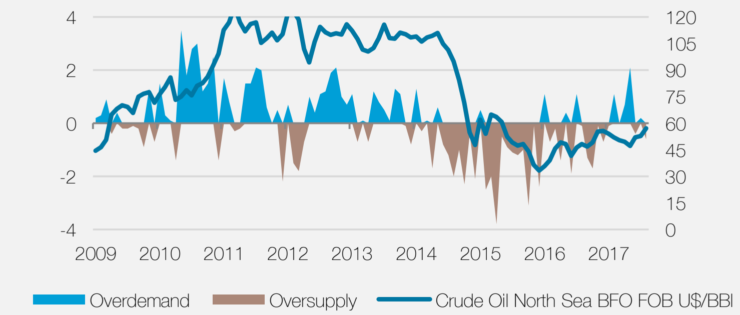
Whatever their ulterior motives, the rulers in Riyadh face a number of challenges. Public finances remain weak – despite swingeing spending cuts, the budget deficit is projected at 9.3% this year. The country can ill afford to lose a substantial portion of oil revenues. Further, the mooted flotation of Saudi Aramco – a cornerstone of the plan to finance the Vision 2030 transformation of the economy – would be compromised by any disruption to production. While uncertainties have risen, it remains in the kingdom's interests to keep oil output flowing.

A major new source of crude supply has emerged in recent years – shale oil in the US. The right-hand chart shows how quickly output has been ramped up, and how resilient it has been in the face of the post-2014 slump in prices. The EIA forecasts further increases next year – to 9.9m b/d on average – putting the US in the same league as Russia and Saudi Arabia (10.9m b/d and 10.0m b/d respectively in September). This autumn's higher prices could enable further production gains.

Putting it all together, we continue expect that global output will comfortably meet additional demand for oil over the next twelve months. This should push Brent prices back below $60 per barrel.

Oil rebalancing likely to be slow

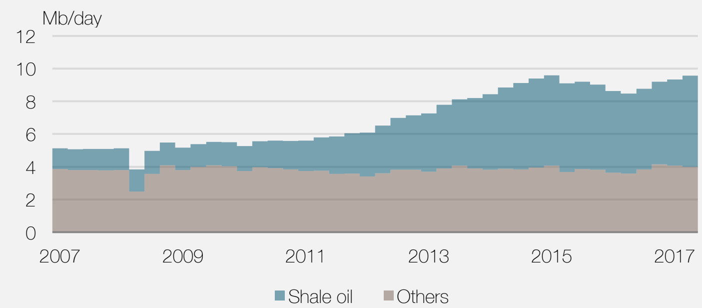
Oil overdemand & oversupply, crude oil North Sea BFO FOB ($ per barrel)



Sources: Societe Generale Private Banking, Bloomberg, Datastream (data as of 08/11/2017)

Rising production of US shale oil

Shale oil production versus other oil sources (million barrels per day)



Sources: Societe Generale Private Banking, Datastream (data as of Q4 2017)

This week and next

EUROZONE

- Producer price index rose from 2.5% to 2.9% YoY in September beating market expectations of 2.7%.
- Eurozone retail sales jumped from 2.3% to 3.7% YoY in September, while the consensus was only for 2.8%.
- In France, industrial and manufacturing production both rose 1.1% in September.

Next week's key events		Per.	Prev.	Cons.
15 Nov	France: Consumer Price Index (YoY)	Oct	1.1%	--
16 Nov	Consumer Price Index (YoY)	Oct	1.5%	--
17 Nov	Construction Output (YoY)	Sep	1.6%	--

UNITED KINGDOM

- Industrial output and manufacturing production surprised to the upside, both rising 0.7% MoM in September versus an expected 0.3%.
- However, construction woes are deepening with a 1.6% MoM drop in September. This points to a sharp slowdown to 1.1% YoY from 3.5% YoY the previous month.

Next week's key events		Per.	Prev.	Cons.
14 Nov	Consumer Price Index (YoY)	Oct	3%	3.2%
15 Nov	Jobless Claims Change	Oct	1.7k	--

UNITED STATES

- The unemployment rate eased down from 4.2% to 4.1% in October. The underemployment rate fell further to 7.9% from 8.3% in September.
- Factory orders improved, rising from 1.2% to 1.4% in September.
- Durable goods orders were down from 2.2% to 2% in September in line with market expectations.
- The non-manufacturing ISM index rose from 59.8 to 60.1 in October, although expectations were for a modest easing to 58.5.

Next week's key events		Per.	Prev.	Cons.
15 Nov	Consumer Price Index (MoM)	Oct	0.5%	0.1%
16 Nov	Industrial Production (MoM)	Oct	0.3%	0.5%

ASIA & EMERGING COUNTRIES

- In Japan, the composite PMI strengthened further from 51.7 to 53.4 in October.
- In China, the consumer price index improved slightly from 1.6% to 1.9% in October while the producer price index remained unchanged at 6.9% against expectations of 6.6%.

Next week's key events		Per.	Prev.	Cons.
13 Nov	Japan: Producer Price Index (MoM)	Oct	0.2%	-0.1%
14 Nov	China: Industrial Production (YoY)	Oct	6.6%	6.3%
15 Nov	Japan: Industrial Production (YoY)	Sep	2.5%	--

Sources: Datastream, Bloomberg, 10 November 2017, Note: YoY = year-on-year; QoQ = quarter-on-quarter; MoM = month-on-month, P = preliminary figure, A = advanced figure, F = final figure, seasonally adjusted, ECB = European Central Bank

Our 6-month targets

CURRENCIES & COMMODITIES

	Thursday close	6mth target
EUR/USD	1.16	1.20
GBP/USD	1.32	1.28
USD/RUB	59.3	60
AUD/USD	0.77	0.72
EUR/CHF	1.16	1.15
USD/CNY	6.64	7.10
USD/CAD	1.27	1.37
USD/JPY	113	115
Brent	$64.2	$55
Gold	$1284	$1225

Forecast figures are not a reliable indicator of future performance

Question time

Past performance should not been seen as a guarantee of future returns.

MACROECONOMICS

Global trade – the recent upturn hides growing threats

10 November 2017

The Great Financial Crisis saw global trade weaken as major exporters experienced soft growth. Faced with shrinking foreign demand, Chinese authorities have chosen to have growth result from private consumption and the domestic services sector rather than exports. As a consequence, global trade struggled to keep pace with global growth while its elasticity was almost two in the early 2000s.

Global trade is now picking up thanks to stronger growth and capital spending. This could be viewed as encouraging, as we celebrate the 70th birthday of the General Agreement on Tariffs and Trade (GATT). However, trade liberalization is still under threat. The US President has been elected on protectionist measures. Although unilateral tariffs were not imposed on Chinese and Mexican imports, the US administration is clearly targeting the World Trade Organisation (WTO) that replaced the GATT in 1995. The United States strongly oppose the WTO's dispute-settlement procedure and its binding consequences. Any removal would severely damage the body's ability to keep the global trade system afloat.

Furthermore, a projectionist wave has been observed since 2009. Although G20 countries refrained from falling in the trap of economic selfishness – which would only have made things worse – trade-distorting measures are spreading. Think tank Global Trade Alert has shown that tariffs now account for a small part of trade distortions and most measures have more to do with anti-dumping, financial incentives, trade finance, public procurement localization or standards.

In the service sector, trade flows are increasingly subject to local regulatory standards and this could have considerable influence on the digital economy for instance.

The United States have shifted from free trade to protectionism, leaving other countries to fill the gap. Regional trade agreements have become more common since the WTO failed to reach more global deals. For instance, the European Union has signed a trade treaty with Canada, the CETA. Pacific Rim countries are still supporting the TPP although Donald Trump decided to withdraw from the initiative. Conversely, the UK and Japan have refused to sign bilateral trade deals with the United States as global trade deals tend to be more effective economically.

Luckily enough, Trump's mercantilist approach to trade has failed to spread to other countries, so far. However, if the WTO was to disappear, countries would favour the tit-for-tat approach in the absence of a strong global trade arbiter, triggering a dangerous downward spiral that would hit growth and only worsen trade tensions.

Market performance

Past performance should not been seen as a guarantee of future returns.

Interest rates

Interest rates	Last	1wk		3mth	YTD	12mth
EONIA (EUR)	-36 bp	0 bp	➡	0 bp	-3 bp	0 bp
3mth Euribor (EUR)	-33 bp	0 bp	➡	0 bp	-1 bp	-2 bp
3mth Libor (USD)	141 bp	2 bp	⬆	10 bp	42 bp	53 bp
3mth Libor (GBP)	53 bp	6 bp	⬆	25 bp	16 bp	13 bp
10-year US Treasury bond	234 bp	-1 bp	➡	10 bp	-10 bp	27 bp
10-year German bond	38 bp	1 bp	➡	3 bp	27 bp	28 bp
10-year French bond	63 bp	0 bp	➡	-10 bp	-6 bp	13 bp
10-year UK bond	131 bp	1 bp	➡	15 bp	7 bp	7 bp

Credit

Credit	1wk		3mth	YTD	12mth
BAML EURO Corp. IG	-0.1%	⬇	0.9 %	2.8 %	2.5 %
BAML EURO Corp HY	-0.3%	⬇	1.7 %	7.1 %	8.5 %
BAML GBP Corp IG	-0.1%	➡	-0.5 %	4.1 %	5.3 %
BAML US IG	-0.2%	⬇	0.8 %	5.7 %	5.0 %
BAML US HY	-0.8%	⬇	0.8 %	6.6 %	8.9 %
JPM Global EM Sov. Plus	-1.5%	⬇	0.4 %	9.6 %	6.4 %

Exchange rates

Exchange rates	Last	1wk		3mth	YTD	12mth
EUR/USD	1.16	-0.1 %	⬇	-1.0 %	10.7 %	6.7%
EUR/CHF	1.16	-0.7 %	⬇	2.1 %	8.0 %	7.8%
GBP/USD	1.32	0.7 %	⬆	1.1 %	6.6 %	6.0%
USD/JPY	113	-0.5 %	⬇	3.1 %	-2.9 %	7.4%
USD/BRL	3.25	-0.5 %	⬇	3.0 %	-0.1 %	1.1%
USD/CNY	6.64	0.5 %	⬆	-0.5 %	-4.4 %	-2.1%
USD/RUB	59.3	1.8 %	⬆	-1.4 %	-3.3 %	-7.2%

Government bonds*

Government bonds*	1wk		3mth	YTD	12mth
United States (3-7yr)	0.0 %	➡	-0.3 %	1.8 %	0.3 %
United Kingdom (3-7yr)	-0.1 %	➡	-0.8 %	0.0 %	0.5 %
Germany (3-7yr)	0.0 %	➡	0.2 %	-0.5 %	-0.1 %
Japan (3-7yr)	0.1 %	⬆	0.2 %	0.0 %	-0.5 %

Equities*

Equities*	Last	1wk		3mth	YTD	12mth
MSCI AC World	499	0.1 %	➡	4.9 %	20.8 %	24.3 %
Eurostoxx 50	3 612	-2.1 %	⬇	4.4 %	13.2 %	22.2 %
DAX	13 183	-1.9 %	⬇	8.5 %	14.8 %	23.8 %
CAC 40	5 408	-1.8 %	⬇	5.3 %	14.5 %	22.8 %
S&P 500	2 585	0.2 %	⬆	5.0 %	17.4 %	21.9 %
FTSE 100	7 484	-0.8 %	⬇	1.0 %	8.6 %	12.7 %
SMI	9 178	-1.1 %	⬇	1.8 %	15.3 %	20.0 %
Topix	1 813	1.1 %	⬆	13.0 %	21.8 %	42.3 %
IBOV Brazil	72 931	-1.2 %	⬇	7.8 %	21.1 %	15.3 %
MICEX Russia *	2 184	5.3 %	⬆	10.5 %	-2.2 %	8.6 %
MSCI EM	1 134	0.6 %	⬆	6.5 %	34.4 %	32.2 %
SENSEX 30 India	33 251	-0.9 %	⬇	4.9 %	26.5 %	23.6 %
Hang Seng (H-K)	29 137	2.2 %	⬆	6.0 %	37.4 %	35.1 %
Shanghaï Composite	3 428	1.3 %	⬆	4.6 %	10.4 %	9.6 %

Commodities

Commodities	Last	1wk		3mth	YTD	12mth
Brent	$64	6.0 %	⬆	22.7 %	13.2 %	39.5 %
Gold	$1 284	0.6 %	⬆	0.9 %	10.9 %	-0.4 %
Silver	$17.0	-0.8 %	⬇	0.7 %	5.8 %	-9.2 %

Source: Datastream, on 9 November 2017 1wk = 1-week change, 3mth = 3-month change, 12mth = 12-month change, YTD = year-to-date change, YoY = year-on-year change, BAML = Bank of America Merrill Lynch, JPM = JP Morgan, IG = Investment Grade, EM = emerging markets. * Price return for MICEX equity index. Equities; total return in local currency. Government bonds = 3-7 year returns. Figures are rounded.

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*Source: Societe Generale Group, June 2016

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