

Monthly Economic Update –August2011

Executive Summary

Sovereign debt crisis in the Eurozone and downgrade of the US credit rating by S&P has brought into focus solvency of national governments. Signs of a debt crisis first surfaced in Greece, a nation plagued with misreported statistics, prolonged deficit spending, high tax evasion and slowdown in growth. Thereafter, the crisis spread to other Eurozone nations including Portugal, Ireland, Italy and Spain, while others countries are also at risk.

- Following the financial crisis in 2008, economies recovered through strong fiscal stimulus measures. This, in turn, led to a rise in government debt and deficit levels, especially in several advanced economies. Structural economic rigidities—particularly burgeoning entitlements and labor market rigidities (mainly in the Eurozone)—as well as political incompetency across the Atlantic have added to the concerns. Recently, US lawmakers barely managed to raise the debt ceiling in time even as they retained tax cuts to the rich and continued with entitlement payments.

In Qatar, the situation remains diametrically opposite as it has strong economic and structural fundamentals. The country continues to capitalize on rising hydrocarbon prices and rapid economic diversification. Consequently, real GDP grew 16.3% in 2010; also, Qatar has one of the highest per capita income worldwide. Real GDP growth is set to be higher this year, supported by an increase in the production of oil and gas as well as higher investments in physical and social infrastructure.

- Of late, Qatar's fiscal balance has been in surplus, benefiting from a secular rise in gas prices and volumes since the early part of the last decade. At the same time, investments in gas infrastructure translated into higher product sales across the globe.
- Qatar has utilized rising hydrocarbon revenues prudently. Also, the government lowered its overall debt to 17.8% of GDP in 2010 from 55.0% in 2000.
- The country enjoys a healthy external balance. Qatar's current account surplus constituted 18.7% of GDP in 2010 and is expected to rise to 36.1% in 2011.

Shifting focus to economic developments in Qatar

According to the IMF estimates, Qatar's real GDP is expected to grow 20% in 2011, largely driven by an expansion in the hydrocarbons sector (estimated to accelerate to 29.5 % in 2011 from 22.2%). The pace of activity in the non-hydrocarbon sector is also set to gather momentum with Industries Qatar planning to invest an additional QAR12 billion over the next five years. The GCC region is likely to witness large-scale investments in infrastructure projects that, in turn, are expected to generate employment in the region, fuel growth and raise inflationary pressures among GCC economies. Other economic news is as follows.

MENA

- Inflation in the GCC region has been receding over the past few months; however, the weak global scenario may result in a further decline in commodity prices worldwide. In Kuwait, budget surplus surged significantly during the last fiscal year with oil revenues aggregating USD73.3 billion. Oman reported a 43% rise in hydrocarbon income during the first half of the year, pushing the GDP to 3.6%. In Saudi Arabia, demand-supply mismatch in terms of residential properties continues to widen, with prices increasing as much as 60% during the first half of the year.
- Lately, Saudi authorities decided to build 500K units as part of its fiscal policy measures to counter the mismatch of demand – supply in the residential sector.

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Advanced Economies

- Series of weak housing and labor market data from the US cast a bleak outlook for the country. At the same time, Manufacturing PMI in the Eurozone contracted for the first time since September 2009. An uncertain global economic scenario increased demand for safe-haven instruments (especially gold) and resulted in a decline in yields and stock markets worldwide.

Emerging Economies

- Central banks in Asia continue to grapple with the problem of rising inflation amid a slowdown in economic growth. In China, inflation rose to its highest level in three years in July; in India, RBI raised the repo rate (the lending rate) for the 11th successive time (since March 2009) to 8% to curb the persistent rise in prices.

Theme discussion: Fiscal Solvency – Qatar’s lead over the West**Fiscal health – A threat to solvency of nations**

Sovereign debt crisis in the Eurozone and downgrade of the US credit rating by S&P has brought the focus back on solvency of national governments. Although the issue has often been mentioned in the chronicles of developing countries in Asia, Africa and Latin America, for the first time it has been mentioned in the context of the Western world – at a scale previously unheard of. Greece sparked the fire that now threatens to engulf the Eurozone. Political wrangling also enabled the US to avoid a default on federal government debt, arguably the world’s safest asset, albeit at a cost. As lawmakers in Washington failed to agree on the terms of a bailout, markets held on with bated breath. Due to a last minute compromise, the core reasons behind burgeoning debt and deficit levels still remain unaddressed. This, in turn, could lead to medium- to long-term consequences unless addressed at the earliest and in a non-partisan way. In line with this, our theme for August focuses on fiscal solvency of nations; we are considering the situation in advanced economies, and how Qatar is better placed vis-à-vis its peers in the West.

Factors determining the solvency of nations

Government debt and fiscal balance, both relative to GDP, are the two most important factors governing fiscal solvency of a nation. For countries with a fiscal deficit, the key is whether they have a primary deficit or not. If the government has a primary deficit, it indicates that even without having to make interest payments, it does not have enough revenues to cover expenditure. When a primary deficit continues for long, there is a threat that the government would move into a debt trap. Current account balance is the third critical factor, especially while measuring the ability to pay back debt raised in a foreign currency (mainly US dollars).

Generally, credit rating agencies are the most important guide to sovereign risk perceptions regarding nations. Three of the most recognized agencies are S&P, Moody’s and Fitch. However, rating agencies have been criticized of late, but not least due to downgrade of the US credit rating by S&P. Analysts have been most critical of the high ratings these agencies provided on mortgage backed securities (MBS), the root cause of the credit crisis during 2007–08.

Greece to the US: What ails the West?

Although governments actively intervened to revive economic activity (through a fiscal stimulus) following the downturn in 2008, the balance sheet of companies was adversely impacted. However, the problem was not a cyclical one. In many of these economies, it was more structural. Relatively lower retirement age translated into a rise in funding burdens for pension, while a host of non-essential entitlement benefits also exerted pressure on government finances. In addition, low growth in many of these economies led to a slower rise in government revenues through taxes. In the US, while prolonged military campaigns and a series of tax cuts meant that a surplus budget turned into deficit, factors such as social welfare entitlements and slow growth have been ascribed to deteriorating public finances in European countries.

Greece – A tragedy that threatens Eurozone’s existence

Greece, where the problem commenced, was an extreme case of fiscal irresponsibility. The quantum of entitlement benefits for public sector employees was unheard of in most parts of the world. Though the average age for retirement was 61 years, it was not uncommon for public sector workers to retire in their early 50s. Generous bonuses, in some cases amounting to two months of basic salary, were also offered in the public sector. The rich continued to evade taxes. Tax-evasion alone is estimated to cost the government at least EUR20 billion a year. Furthermore, fuzzy statistics by authorities misled private sector analysts as well as pan-European organizations such as Eurostat. By the time a new government was in place in early 2010, official fiscal deficit figures increased almost twofold from pre-election days to nearly 13.6% of GDP (2010). Also, debt levels rose sharply due to the recession in 2009. General government debt moved up from 110% of GDP in 2008 to 142% by 2010.

Markets reacted to the bad news by punishing Greek debt. Government bond yields rose and it became apparent that the country would need a bailout by the Eurozone and other partner institutions. Eurozone nations and the IMF provided a EUR110 billion bailout package. In keeping with the covenants of the bailout, Greece enacted a number of austerity measures including reducing spending, freezing public sector wages, increasing the retirement age, raising the value-added tax (VAT) rate and cutting down tax evasion.

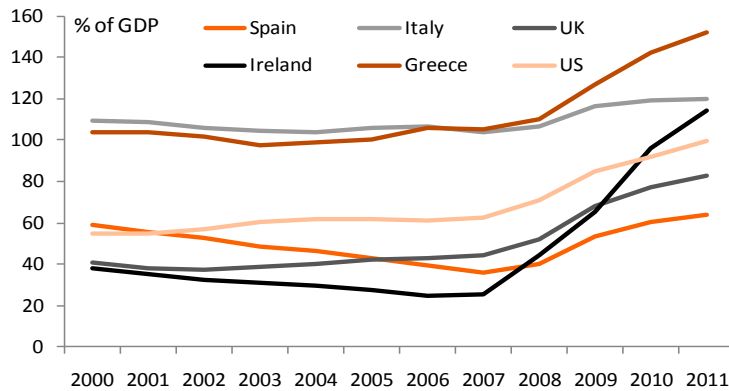
Theme discussion: Fiscal Solvency – Qatar’s lead over the West

Although the rescue package for Greece brought in a bit of calm, markets were not entirely convinced. Over time, attention was diverted to other Eurozone periphery nations such as Ireland, Portugal and Spain. Bailout of Ireland’s banking sector proved detrimental. In September 2010, the Irish government had to infuse more money for its beleaguered banks that had been active participants during the real estate boom of 2006–07. This, in turn, increased the cost of bailing out the banking sector to EUR45 billion. Consequently, the budget deficit moved up from 14.3% of GDP in 2010 to 32.4%. As expected, bond markets reacted negatively and the country—once known as the Celtic tiger for its fast-paced growth—had to seek emergency aid from its Eurozone peers and the IMF. By that time, Portugal and even Spain, the fourth largest economy in the Eurozone, were also impacted. High debt and deficit levels coupled with stagnant economic growth and structural rigidities meant that bond yields on sovereign debt rose while credit default swap (CDS) spreads widened. Also, Portugal had to tap into the Eurozone-IMF funds.

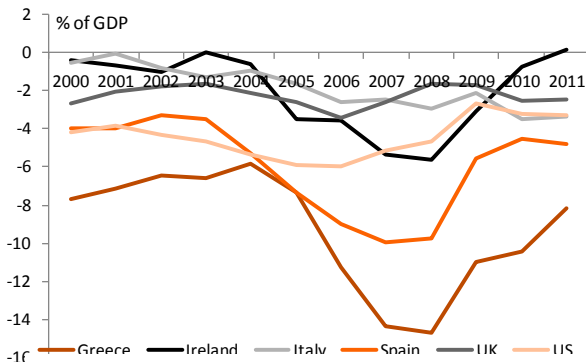
This year around, the issue has resurfaced. Greece had to seek a second bailout; concerns persist over the finances of Italy and Belgium. Prior to the second bailout for the former, there were concerns over a German proposal to involve the private sector in a bailout. However, taxpayers in the country have strongly opposed the bailout of profligate countries. But, with a number of French and German banks holding Greek bonds, any default by Greece would have resulted in a sudden loss of capital, thereby destabilizing the banking system in these countries. Therefore, both countries had to agree to a second bailout package for the country without compulsory involvement of the private sector.

However, rising sovereign risk perceptions still exist. Markets are particularly worried about Italy and its capacity to tackle increasing debt; on the other hand, structural rigidities (especially in labor markets) continue to thwart economic growth. Even if debt-related concerns diminish in the short-term, fundamental concerns related to fiscal governance are likely to continue in the near term. It has become increasingly clear to policymakers in the region that a monetary union with disparate fiscal strategies would be hard to pursue. Restructuring rules in the Eurozone as well as reorganization of the 17-member bloc itself cannot be ruled out in the medium term. For the GCC region, the European example could hold vital clues on any future monetary union.

Government balance

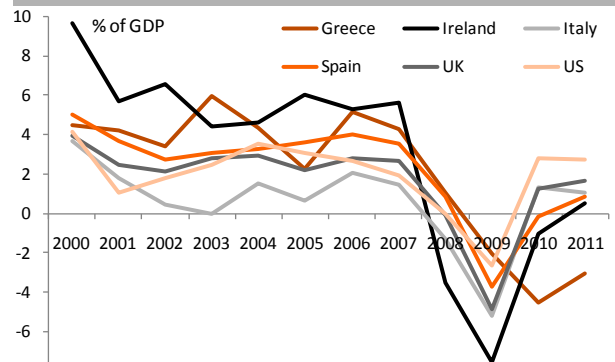


Current Account Balance



Source: IMF

GDP growth



Source: IMF

Theme discussion: Fiscal Solvency – Qatar’s lead over the West

United States – A problem long in the making

In the US, political wrangling was ascribed to the raising of the debt limit and a subsequent downgrading of the US credit rating by S&P. On August 2, US lawmakers finally agreed to raise the Federal government’s debt ceiling of USD14.3 trillion and approved expenditure cuts of USD2.4 trillion over the next 10 years. However, the run-up to a rise in the debt ceiling did not inspire much confidence. Huge political differences deflated the plan to lower the deficit by cutting expenditure and raising taxes. Of greater concern were the decisions to retain Bush-era tax cuts as well the structure of entitlement benefits.

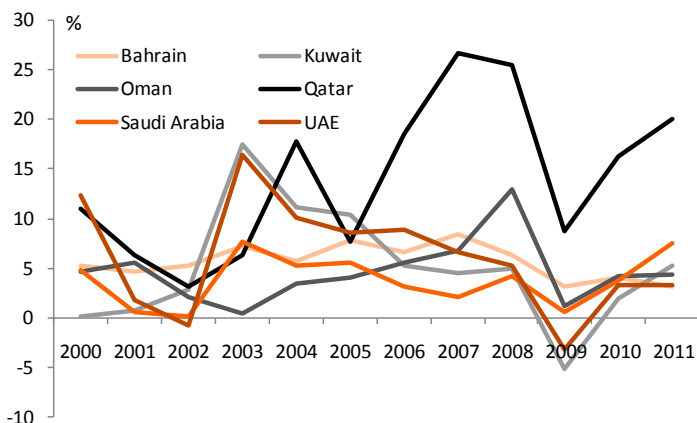
Deteriorating US government finances have been a cause for concern for economists. A surge in military spending and a series of tax cuts implemented over 2000–08 translated that a fiscal surplus of 1.5% of GDP in 2000 turned into a deficit of 2.9% by 2007. This was followed by the downturn in 2008 which meant lower revenues through taxes and higher spending on unemployment benefits. To counter the recession, the US government enacted strong fiscal stimulus measures. Consequently, the deficit reached 6.3% of GDP by the end of 2008 and rose to 10.6% by 2010. Also, government debt expanded from 54.8% of GDP in 2000 to 91.6% in 2010. By the end of 2011, the IMF expects government debt to be almost 100% of GDP.

In that context, the debt ceiling debate was an excellent opportunity for both Democrats and Republicans in Congress to earmark fiscal reforms. Instead, there was a ruckus with the Congress passing a bill almost at the 11th hour. Even then, reductions agreed to (USD2.4 trillion) fell far short of an ideal sum; analysts were expecting more than USD4 trillion in savings. Consequently, on August 6, S&P downgraded US’ AAA credit rating by one level to AA+ with a negative outlook. Moreover, the rating agency stated that any failure on the part of US authorities to put a credible deficit reduction plan in place would lead to a further downgrade of ratings (to AA) within the next two years. The reason rating agencies have not downgraded US Treasuries until now is because they are considered a safe asset. This is particularly relevant now given the concerns of a double-dip recession in some parts of the Western world, especially key Eurozone economies. On August 8, the first day of trading following the announcement of a downgrade by S&P, the yield on 10-year Treasuries fell 24 basis points to 2.4%. Failure to get a proper debt-reduction plan in place could affect the government’s fiscal health and slower economic growth is expected to accentuate it. This, in turn, could lead to further downgrades by S&P. Other rating agencies could also follow suit, thereby exerting pressure on long-term bond yields. Consequently, consumption and investment could be impacted, resulting in slow jobless growth over the next five years.

Qatar – Riding high on strong fundamentals

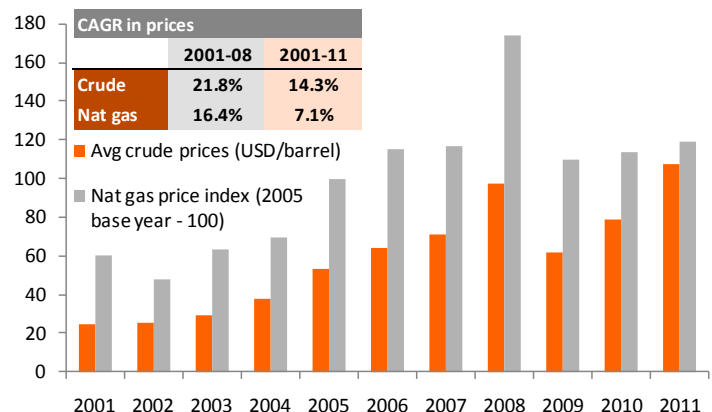
Qatar continues to enjoy strong fundamentals and rapid economic growth. Driven by a secular trend of rising hydrocarbon prices and volumes since 2001–02 and a range of economic diversification measures, GDP growth in Qatar has been one of the highest worldwide. According to the IMF, GDP grew 16.3% in 2010 and is set to rise to 20.0% in 2011. The country’s per capita income is one of the highest across the globe; as the government continues to aggressively invest in economic and social infrastructure, income and general welfare levels are expected to increase further.

GDP growth in GCC economies



Source: IMF

Growth in prices of crude oil and natural gas



Source: Bloomberg

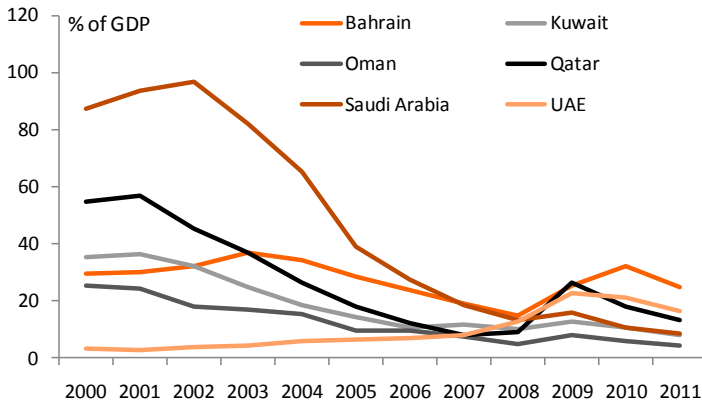
Theme discussion: Fiscal Solvency – Qatar’s lead over the West

Qatar’s structural fundamentals are the most impressive. The country enjoys strong external balances and a healthy government balance sheet. The general government balance has been strengthening of late. This is primarily ascribed to high hydrocarbon revenues (an increase in sales and price) and prudent spending. Though the government responded to the global economic downturn with a range of fiscal measures, it reported a surplus in 2009 and 2010 (15.2% and 12.8% of GDP, respectively). In 2011, the balance sheet is set to improve to 13.8% of GDP. Interestingly, Qatar’s surplus has not come at the cost of cuts in key government expenditure. In fact, government investments in infrastructure and social welfare have increased steadily over the years. This is set to continue in the short- to medium-term and is contrary to patterns witnessed in several developed nations, where essential spending (such as child welfare) has been impacted. While some critics have pointed out that strong oil and gas revenues are a steady source of income for Qatar and its energy-rich GCC peers, there is no doubt that the country has been more prudent vis-à-vis its Western counterparts in terms of handling its balances.

A good example of this is total government debt. In the late 90s, there were concerns within a number of quarters regarding rising government debt levels in Saudi Arabia and, to a lesser extent, Qatar. For example, in 2000, total government debt in the Kingdom stood at 87.2% of GDP, while the corresponding figure in Qatar was 55.0%. However, over the decade that followed, GCC countries capitalized on an increase in oil and gas prices. For instance, average crude prices have risen almost four times over the past decade. Saudi Arabia, with the largest oil reserves worldwide, has been a key beneficiary. On the other hand, Qatar has also benefited from its vast reserves of natural gas that are estimated to be the third-largest known reserves in the world after Russia and Iran. Significant investments in natural gas have ensured an ever-growing capacity to extract and export gas to other countries. Consequently, inflows from hydrocarbon sales have been rising.

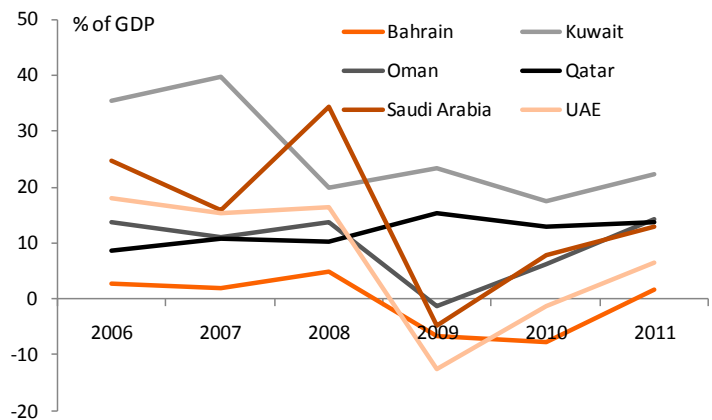
Across the GCC, authorities utilized their increasing hydrocarbon revenues for infrastructure investments and foster economic diversification, boost social welfare projects and devise new ways of using some revenues for the benefit of future generations. In Qatar and Saudi Arabia, authorities also resorted to lowering overall debt levels. Consequently, by 2010, government debt in Qatar fell to 17.8% of GDP, while that in the Kingdom declined to 10.8%. In 2011, debt levels are expected to reduce further in both countries –13.3% of GDP in Qatar and 8.3% in Saudi Arabia.

General government debt



Source: IMF

Government balance



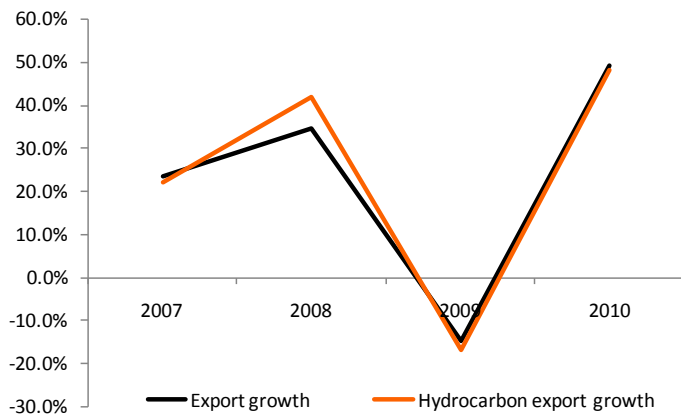
Source: IMF

In line with several other countries, Qatar has set aside a part of its hydrocarbon revenues to be managed under a sovereign wealth fund (SWF). Qatar Investment Authority (QIA) is responsible for the SWF and invests in a mix of equity and debt investments worldwide. QIA also acts as a second line of defense for the economy, aiding different sectors at the time of crisis. This was most evident during the global downturn of 2008–09, when it directed funds to support the banking system. This coupled with a host of other measures stabilized the banking system and ensured continued economic growth at a time when some of the most renowned financial centers were facing a crisis.

Qatar’s external balances are also strong. In 2010, the surplus stood at 18.7% of GDP and the IMF expects it to increase to 36.1% in 2011.

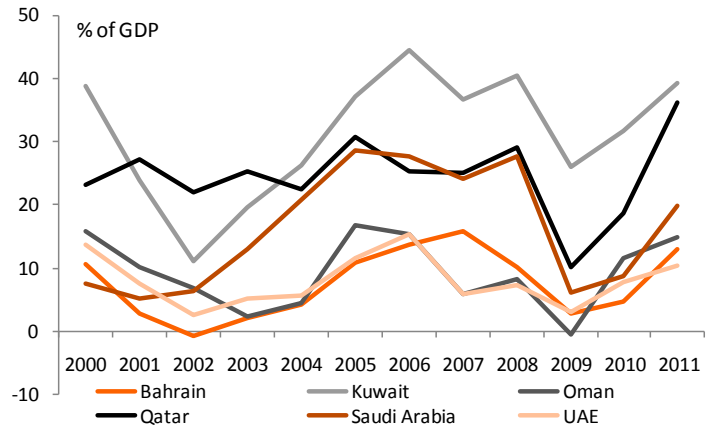
Theme discussion: Fiscal Solvency – Qatar’s lead over the West

Export growth in Qatar



Source: IMF

Strong external balances



Source: IMF

Sovereign ratings of key global economies

Rating Agency	Bahrain	Kuwait	Oman	Qatar	Saudi Arabia	UAE	Portugal	Ireland	Greece	Spain	Germany	France	UK	US
S&P	BBB	AA	A	AA	AA-	-	BBB-	BBB+	CC	AA	AAu	AAu	AAu	AA+u
Moody's	Baa1	Aa2	A1	Aa2	Aa3	Aa2	Ba2	Ba1	Ca	Aa2	Aaa	Aaa	Aaa	Aaa
Fitch	BBB	AA	-	-	AA-	-	BBB-	BBB+	CCC	AA+	AAA	AAA	AAA	AAA

Source: Bloomberg

Qatar has won accolades from rating agencies for its strong fundamentals, a stark contrast to downgrades and credit warnings for key advanced economies. Qatar enjoys the highest sovereign ratings among GCC countries due to strong fiscal and external balances. Apart from a steady rise in oil prices, the country also appears to be judiciously deploying its hydrocarbon revenues for economic diversification and creating avenues for sustaining high growth levels. On July 5, 2010, S&P raised Qatar’s long-term sovereign ratings to AA from AA- with a stable outlook. Also, Moody’s upgraded the sovereign ratings from Aa3 to Aa2 on July 25, 2007, due to the government’s large-scale investments to expand LNG production capacity; this, in turn, is expected to further boost hydrocarbon revenues.

Economic Developments

Qatar- Major macroeconomic events

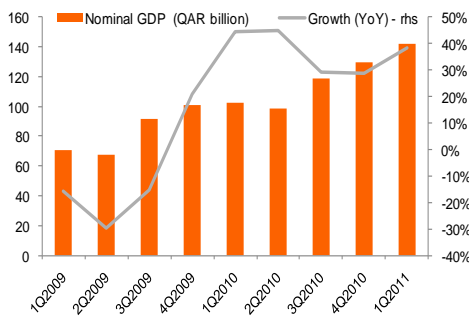
Strong GDP growth in Qatar: Qatar leads GCC nations in terms of economic growth. The IMF expects the country's GDP to grow approximately 20% in 2011 after increasing 16.3% in 2010. Expansion of LNG capacity to 77 million tonnes per annum earlier this year from 54 million tonnes in 2009 and improved momentum in the non-hydrocarbon sector continue to boost growth. Growth in the hydrocarbon sector is estimated to accelerate to 29.5% in 2011 from 22.2% in 2010.

Decline in Qatar's budget surplus: The Qatari government's budget surplus fell to QAR13.5 billion (2.9% of its GDP) in fiscal 2010/11 from QAR54.1 billion (15.2% of GDP) in 2009/10 as spending increased 24% to QAR142.4 billion. Simultaneously, due to large-scale spending, inflation in the country rose to a 19-month high of 1.9% YoY in July.

Qatar to focus on expanding non-hydrocarbon business: Expansion in the non-hydrocarbon space would be led by state-supported Industries Qatar (IQ), which controls a major part of the country's petrochemical and metal production capacity. IQ plans to invest QAR12 billion (USD3.3 billion) over the next five years to ensure growth momentum in the sector continues.

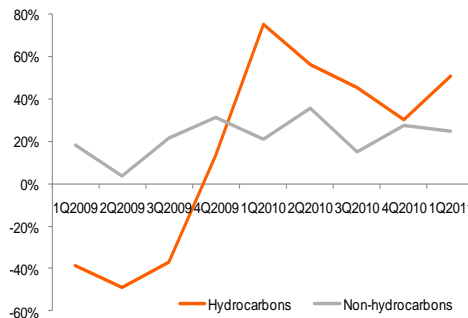
Qatar cuts interest rates to boost economy: The Qatar Central Bank reduced its overnight lending rate or repurchase rate to 4.5% from 5% and deposit rate by 25 basis points to 0.75%. Through this move, it aims to give a boost to the domestic banking sector and revive credit growth in the private sector so as to increase spending on planned infrastructure and real estate projects.

Nominal GDP growth in Qatar



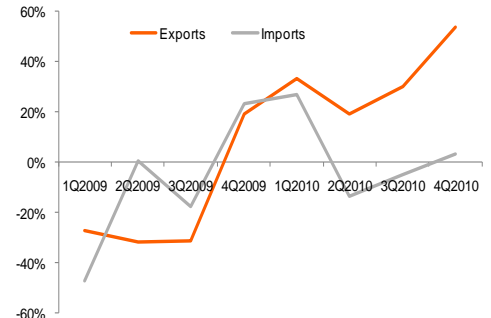
Source: Qatar Statistics Authority

Qatar nominal GDP growth: individual sectors



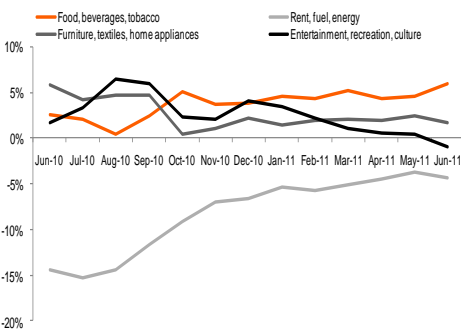
Source: Qatar Statistics Authority

Qatar foreign trade



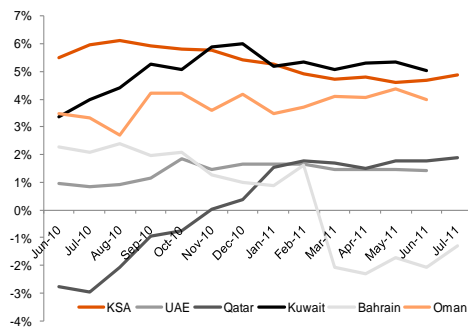
Source: Qatar Statistics Authority

Inflation in Qatar



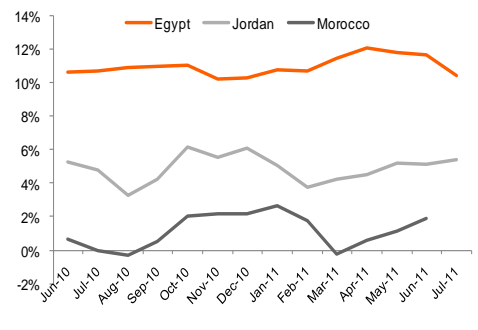
Source: Qatar Statistics Authority

Headline (CPI) inflation in the GCC



Source: Qatar Statistics Authority

Headline (CPI) in MENA



Source: Qatar Statistics Authority

Economic Developments

MENA

- **Inflation to fall further in GCC region:** In view of the decline in inflation in most oil-rich Gulf States over the past few months, analysts at Capital Economics expect average inflation in the region to fall further. Amid the weak global economic scenario, prices of commodities, including agricultural, worldwide are likely to decline even more, moderately easing inflationary pressure in the region.
- **Saudi Arabian construction sector to expand significantly in 2H 2011:** The Saudi Arabian construction sector is expected to witness a boom in 2H 2011 with several mega infrastructure projects scheduled to commence soon. One such bid expected to be awarded is Phase 2 (worth SAR30 billion) of the Haramain high-speed railway project. Besides this, construction of 500,000 housing units under King Abdullah's royal decree is likely to start during this period.
- **Saudi Arabia to invest in education:** Saudi King Abdullah approved a proposal to restructure the college of physical education at King Saud University. He also sanctioned the establishment of certain institutes and centers at some universities, including an institute of research and consultative studies at King Khaled University in Abha.
- **Saudi Arabian residential property prices skyrocket in 1H:** Due to robust growth in population and limited supply of low and middle income houses in Saudi Arabia, the gap between demand and supply in the domestic residential market is widening. Consequently, property prices in the Saudi residential sector increased as much as 60% in 1H. Amid rising demand, but constrained purchasing power, demand for all types of properties in the Saudi rental market continued to surge in 1H.
- **Kuwaiti budget surplus surges on higher oil revenues:** Kuwait reported a budget surplus of KWD5.3 billion (USD19.5 billion) in the last fiscal year due to record revenues owing to rise in oil prices. Revenues in the year ended March 31 reached a high of KWD21.5 billion (USD79 billion), while income from oil totaled USD73.3 billion (more than twice the estimate in the budget).
- **Iraq's proposed rail project:** The Iraqi Ministry of Transport is awaiting approval from the cabinet on the proposed plan to build a USD70billion rail network to link Iraqi provinces with high-speed trains travelling at 240 km per hour. This initiative is aimed at boosting economic growth.
- **Lower food prices ease inflation in the UAE:** Due to declining housing costs in the UAE, annual inflation in the country fell to 1.28% in July from a six-month high of 1.73% in June. The cost of housing, water, electricity and gas (accounts for nearly 40% of the UAE's consumer price index) fell 1.61% MoM in July and 2.43% YoY.
- **Hydrocarbon earnings boost Oman's GDP:** Real GDP growth in Oman, led by the hydrocarbon sector, stood at 3.6% in 1H 2011. The nation's oil income, at OMR4.1 billion (USD10.5billion) over January–June, was 43% above that in the same period last year.

Economic Developments

GCC economies	Qatar		Saudi Arabia		UAE		Kuwait		Oman		Bahrain	
	2010	2011F	2010	2011F	2010	2011F	2010	2011F	2010	2011F	2010	2011F
Real GDP growth (%)	16.3	20.0	3.7	7.5	3.2	3.3	2.0	5.3	4.2	4.4	4.1	3.1
Oil sector growth (%)	22.7	29.5	2.3	13.3	5.3	3.4	2.2	6.6	6.5	4.1	0.1	6.2
Non-oil sector growth (%)	10.0	9.5	4.3	5.4	2.1	3.3	1.8	4.5	3.0	4.5	4.6	2.7
Inflation (%)	-2.4	4.2	5.4	6.0	0.9	4.5	4.1	6.1	3.3	3.5	2.0	3.0
Fiscal balance (% of GDP)	12.8	13.8	7.7	12.8	-1.3	6.5	17.4	22.3	6.2	14.2	-7.8	1.6
Current account (% of GDP)	18.7	36.1	8.7	19.8	7.7	10.4	31.8	39.4	11.6	14.9	4.6	13.0
Other MENA economies	Egypt		Jordan		Morocco		Tunisia		Syria		Lebanon	
Real GDP growth (%)	5.1	1.0	3.1	3.3	3.2	3.9	3.7	1.3	3.2	3.0	7.5	2.5
Inflation (%)	11.6	11.8	5.0	6.1	1.0	2.9	4.4	4.0	4.4	6.0	4.5	6.5
Fiscal balance (% of GDP)	-8.1	-9.7	-5.4	-6.8	-4.2	-4.9	-1.2	-4.3	-4.8	-6.8	-7.2	-10.5
Current account (% of GDP)	-2.0	-2.7	-5.4	-8.5	-4.2	-5.7	-4.8	-7.8	-4.4	-4.6	-10.2	-12.9

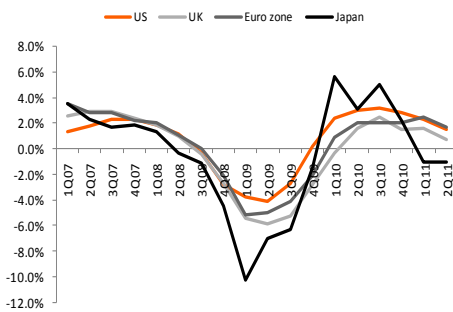
Source: IMF World Economic Outlook, April 2011

Economic Developments

Advanced Economies

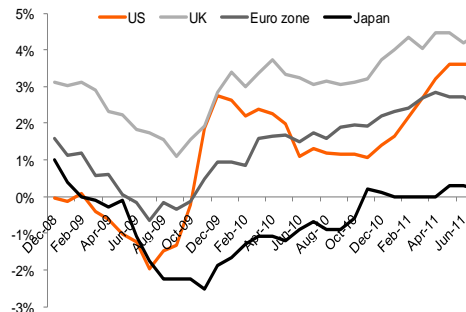
- **US housing starts decline in July:** Construction of new homes in the US dipped more than expected by 1.5% to 604,000 in July from June's downward revised number of 613,000 as higher inventory levels and persistent weakness in the economy weighed on demand for property.
- **Philly Fed Factory Index slumps:** Philadelphia Federal Reserve Bank's business activity index slipped to minus 30.7 from positive 3.2 the month before and was way below economists' expectation of a positive 3.7; this is the index's biggest MoM drop since October 2008.
- **US labor market data continues to disappoint:** According to latest data, initial jobless claims rose more than expected by 9,000 to 408,000 in the US, casting a bleak outlook for the US job market.
- **Demand for 'safe haven' bonds surge amid global uncertainties:** In an environment of weak economic growth globally and amid expectation of interest rates remaining low for long, yields on benchmark 10-year US and UK government bonds fell to record lows of 1.97% and 2.24%, respectively, in August, while German bund yields declined to 2.09%.
- **Concerns over Eurozone economy increase:** Economic activity in the Eurozone appears to have slowed considerably—the manufacturing PMI for Germany indicated a reversal in trend for the first time in two years in August. The manufacturing index dropped below 50 for the first time since September 2009, indicating a contraction in activity. Although the composite index covering services and manufacturing remained flat at 51.1 in August, it was at a two-year low.
- **Greek banks aid recapitalization of Porton Bank:** Greece's four largest banks – National Bank of Greece, Alpha Bank, EFG Eurobank, and Piraeus Bank – came together to buy a EUR50 million convertible bond to recapitalize Proton Bank in an attempt to save the nation's fragile banking system.
- **UK unemployment surges amid slowing growth:** Unemployment in the UK rose from 7.7% in the 1Q to 7.9% in the 2Q—the number of people claiming jobless benefits rose by 37,000 in July, nearly twice the estimate. Moreover, the number of people claiming unemployment benefits in June was revised upwards to 31,000 from 25,000.
- **UK inflation edges higher in July:** In the UK, higher prices of clothes, shoes, bank fees and rents pushed the annual inflation rate to 4.4% in July, way above the central bank's target of 2%. Amid slowing domestic as well as global growth and rising inflation, the Bank of England is in a dilemma over the monetary policy to be adopted.
- **Bank lending picks up slightly in the UK:** Bank lending rose in the UK—banks approved 74,590 mortgages in July compared to the average of 69,803 per month for the previous six months. However, corporate and household borrowings continued to remain subdued at half the levels seen in 2006–07.

GDP growth in advanced economies



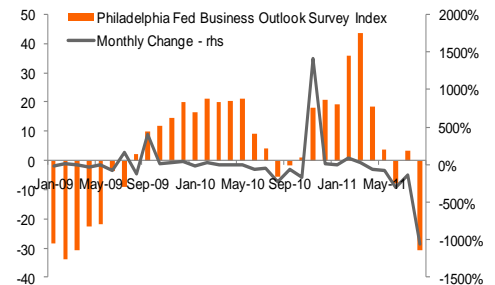
Source: Bloomberg

Inflation in advanced economies



Source: Bloomberg

US Philadelphia Fed



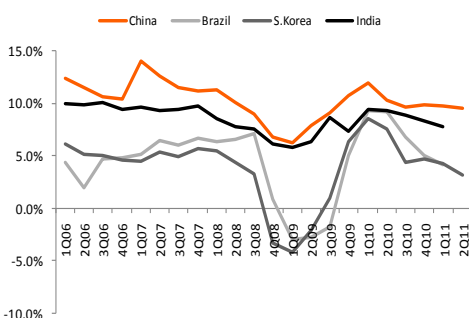
Source: Bloomberg

Economic Developments

Emerging Economies

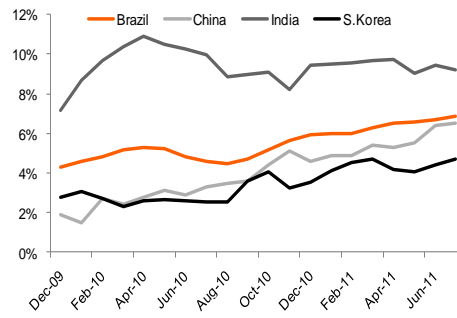
- **China's HSBC PMI index reflects improvement in activity:** HSBC's China Flash Purchasing Managers' Index (PMI), which is an indicator of China's factory output, edged up to 49.8 in August, from July's final reading of 49.3. However, the index remains below the 50 mark, reflecting contraction in activity.
- **Chinese inflation surges to a three-year high:** Chinese consumer prices climbed 6.5% from a year earlier in July, the most since June 2008, reflecting strong economic activity in the nation.
- **Rising concerns over swelling bad loans among Indian banks:** The aggressive hike in lending rates by RBI in the past 18 months to curb inflationary pressures in the economy has raised concerns about worsening credit condition in the economy. Crisil, the Indian arm of the S&P rating agency, expects the overall bad loans held by Indian banks to rise from 2.3% to 2.6 % in the year ending in March 2012, higher than the 2.4 % rise in 2008.
- **India reports a surprise rise in IIP number:** Despite successive interest rate hikes by the RBI, India's industrial production grew at 8.8% in June, the fastest pace in three months.
- **Russia Bank eyes investment opportunity in Poland:** OAO Sberbank is seen exploring the possibility of buying Poland's Kredyt Bank, controlled by KBC, and Bank Millennium, controlled by Banco Comercial Portugues, values of which are presently quoted at about USD1.3 billion and USD1.8 billion, respectively.
- **Turkey to set up free economic zones:** Turkish authorities remain keen to maintain the steady pace of growth of above 10%, with the government set to facilitate foreign trade and investment by upgrading Turkey's current free zones to free economic zones. These zones will provide an opportunity to set up varied business on a common land and the area will be well connected to all routes of commutation (air, sea and road).
- **Inflation in South Korea surges amidst dipping investor confidence:** South Korean consumer confidence dipped to 99 in August from 102 in July. This is only the second time that the index has come below 100 since early 2009. Meanwhile, inflation expectation rate for the next 12 months rose beyond the 4% target of the Central Bank, increasing the problems of the Central bank that is trying to establish a healthy growth rate and price stability in the nation.
- **South African economy continues to face challenges:** Even as IMF forecasts the economy to grow by 4% this year, South African policy makers continue to grapple with two serious problems existing in the economy; rising inflation, which reached 5.3% in July and a high unemployment rate of 25.7%.
- **Surging domestic currency hurts Australian manufactures:** The Australian dollar has strengthened over 18% over the past 12 months, hurting the manufacturing industry. The Australian Industry Group-PricewaterhouseCoopers Performance of Manufacturing Index (PMI) fell 9.5 points in July to 43.4, indicating a contraction in activity.

GDP growth in key emerging economies



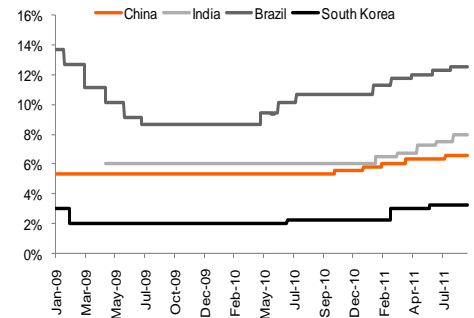
Source: Bloomberg

Inflation in key emerging economies



Source: Bloomberg

Policy rates in key emerging economies



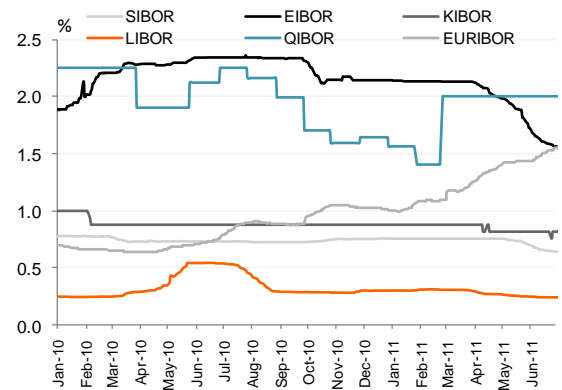
Source: Bloomberg

Banking and Financial Services

Qatar

- **Steady growth in credit:** Overall bank credit in Qatar increased 16.02% YoY to QAR278.16 billion in July 2011. Credit grew in double digits for four consecutive months, mainly led by the private sector; it rose 16.96% YoY to QAR213 billion in July. A 50 bps cut in repurchase rate by the Qatar Central Bank in early August is likely to further spur lending activity in the private sector.
- **Personal loan rate to decline in Qatar:** Following the recent cut in repurchase rate by the Qatar Central Bank, commercial banks in the country are expected to reduce interest rates on personal loans to 6% from 6.5%.
- **Abu Dhabi Islamic Bank to start operations in Qatar:** Qatar Financial Centre Regulatory Authority (QFCRA) has authorized Abu Dhabi Islamic Bank to start Sharia-compliant banking operations in the country. The bank would accept deposits, provide and arrange financing facilities, and manage investments in Qatar in compliance with the Sharia law.
- **Fitch affirms Qatar National Bank's rating at A+:** Fitch Ratings affirmed Qatar National Bank (QNB)'s Long-term Issuer Default Rating (IDR) at 'A+' with a stable outlook. This rating was derived considering the bank's strong asset quality, liquidity and capitalization ratios. Fitch also considered QNB's QAR12.7 billion rights issue during 1Q11, which increased the bank's capital by 25% and lent support to its aggressive domestic expansion plans.
- **QFCRA signs an information sharing agreement with the RBI:** The Qatar Financial Centre Regulatory Authority (QFCRA) signed an MoU to promote greater cooperation and share supervisory information with the Reserve Bank of India (RBI).

3-month inter bank offered rates



Source: Bloomberg

Interbank offered rates (average for July)

	1M	3M	12M
Qatar	0.34	2.00	2.40
Saudi Arabia	0.33	0.60	0.85
Kuwait	0.56	0.81	1.31
UAE	1.47	1.47	1.94
USD LIBOR	0.21	0.29	0.78
EURIBOR	1.38	1.55	2.10

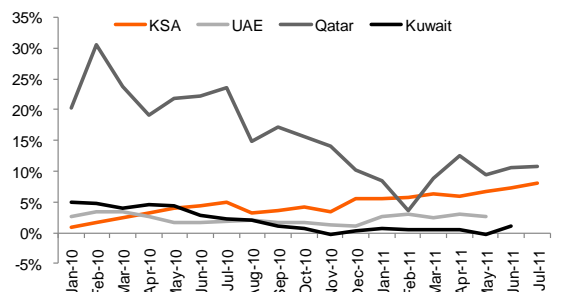
Source: Bloomberg

Qatar

Stocks	Last Close	MTD %	YTD %	3YR %	PE Ratio
Qatar National B	138	-2.1%	6.1%	60.7%	11.7
Al Ahli Bank	78	10.4%	34.2%	53.7%	10.9
Masraf Al Rayan	23	-3.0%	22.2%	24.7%	12.0
Doha Bank Qsc	59	9.9%	-1.7%	20.6%	10.1
Comm Bank Qatar	79	6.6%	-5.4%	-16.6%	10.4
Qatar Islamic Ba	79	0.9%	3.6%	-25.6%	12.3
Qatar Internatio	49	1.5%	8.0%	-30.1%	11.7
Al Khaliji Bank	17	-0.1%	7.1%	-36.3%	14.4
Dlala Holding	14	-5.0%	-0.5%	-62.6%	14.4

Source: Bloomberg

Credit growth

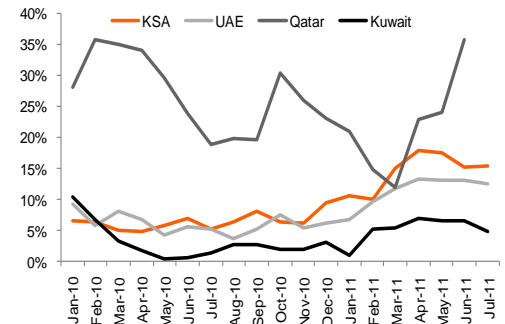


Source: Bloomberg

MENA-Banking and Financial Services

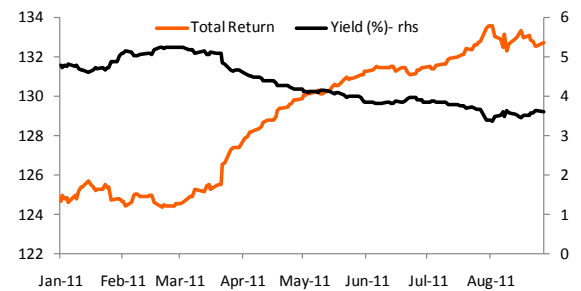
- **Net profit of GCC banks surges 28% in 2Q:** Gulf banks reported a nearly 28% rise in net profit during 2Q. Net interest income for the region also increased during the quarter; Qatar and Kuwait recorded the highest growth on YoY basis (13%), followed by the UAE (12%).
- **Saudi Arabia reports strong credit growth:** Saudi Arabia's credit growth recovered steadily, led by strength in oil prices and improvement in economic fundamentals. The Kingdom's credit grew at an annual rate of 7.2% in June 2011, taking the total domestic bank credit to SAR814.2 billion (USD217 billion).
- **Saudi Arabian banks likely to benefit from lower provisions:** Profits of Saudi Arabian banks increased in the second quarter of 2011 due to lower provisions and higher income from lending activities. Although banks are likely to continue to benefit from lower provisioning in 2H this year, cautious approach adopted by lenders could dent profitability.
- **Bad checks issuance drops 56%:** The year 2011 saw a reduction in the issuance of bad checks in Saudi Arabia; the number of bad checks issued fell to 13,000 in the second quarter of 2011 from 29,000 during the year-ago period.
- **Private sector drives growth in the Omani banking sector:** Backed by higher oil prices and improved economic conditions in Oman, net profit of the country's banks rose around 7% in 1H2011. Activity in the private sector showed signs of revival after being hit by the global economic crises of 2008—private sector credit increased about 8.6%, taking the Omani banking sector's overall credit to OMR11.45 billion at the end of June.
- **MENA banks better capitalized than their western peers:** With an estimated average core Tier-1 of around 13% under Basel III, banks in the Middle East and North Africa are much better capitalized than their US or European peers.
-
-
- as part of its US\$ 4billion medium-term notes program initiated in 2008.

Broad money (M2) supply growth



Source: Bloomberg

Movement in HSBC DIFX sukuk index



Source: Bloomberg

MENA private equity activity in 2011

Status	Private Equity Fund Name	Size (USD million)	Geographical Focus
Fund Raising	Samena Special Situation Fund II	350	MENA
Fund Raising	DB Masdar Clean Tech	290	Asia, Europe, North America
Announced	Gulf Credit Partners	250	MENA, Turkey
Announced	Invest AD and SBI Holding	100	Turkey
Fund Raising	Siraj Palestine Fund I	60	Palestinian Territories
Fund Raising	ADCM Secondary	45	Europe, MENA, US
Fund Raising	FINCORP Oman	31	Oman

Source: Bloomberg

Hydrocarbon sector

Qatar

- **QP raises Qatar Land crude price:** State-owned Qatar Petroleum raised its crude oil official selling price by USD1.85 for July term supply, pushing Qatar Land price to USD113.50 a barrel.
- **Lack of gas stalls Industries Qatar's steel projects:** Qatari steel-to-fertilizer conglomerate, Industries Qatar (IQIQ), has put its two planned steel plants (valued at QAR8.1 billion or USD2.22 billion) in the industrial city of Mesaieed on hold due to problems in securing natural gas. This move has been bothersome, especially because domestic demand for steel is on the rise.
- **France Technip bags Qatar refinery expansion project:** Technip has won the engineering design contract for the expansion of Qatari firm Laffan Refinery Company's Ras Laffan refinery. The refinery is expected to be fully operational by the first quarter of 2016, doubling the capacity of the unit to 292,000 bpd (barrels per day).

MENA

- **Saudi Arabian oil production jumps 10%:** Oil production in Saudi Arabia increased 10.3% to 9.813 million barrels a day in June from 8.90 million barrels a day in the previous month. The nation's export of crude oil and condensate rose to 7.38 million barrels a day in June from 6.84 million barrels a day in May.
- **Kuwait to examine the proceedings of the contract with Shell:** The Kuwaiti ministry has set up a committee to probe an USD800 million contract between state-owned Kuwait Oil Company and Shell to review the implementation of the Enhanced Technical Services Agreement awarded in February 2010.
- **Iran to invest USD1.6 billion to develop the third phase of the Darkhovin oilfield:** The National Iranian Oil Company (NIOC) and a consortium of Iranian companies have signed a USD1.6 billion contract to develop the third phase of the Darkhovin oilfield, which is projected to produce 71,000 barrels of crude oil per day, taking the combined capacity of all three phases to 231,000 barrels of oil per day.

Non-hydrocarbon sector

Qatar

- **Qatar Airways joins hands with Brazil's Gol Linhas Aéreas Inteligentes:** The two firms have collaborated to implement a new code share agreement to connect travelers from Doha to 46 cities across Brazil through Sao Paulo Guarulhos International Airport.
- **Real estate arm of Qatar's sovereign wealth fund and a British developer to buy the 2012 Village:** Delancey and Qatari Diar have entered into a deal worth USD907 million to convert the Olympic Village to 1,439 private homes (with the possibility of 2,000 more) after the 2012 London games.
- **Qatar Shipping wins QAR1.88 billion Port Services Contract:** Qatar Petroleum awarded Qatar Navigation's fully-owned subsidiary Qatar Shipping a QAR1.88 billion (USD516 million), 20-year contract to provide and operate harbor tugs, pilot boats and mooring gangs at

MENA

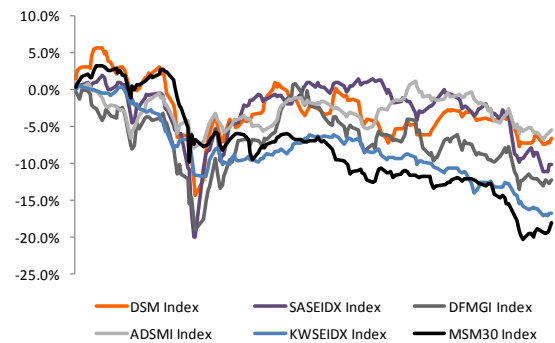
- **'Stan-si' acquires stake in a Saudi Arabian construction products company:** Standard Chartered Private Equity has acquired a minority stake in Construction Products Holding Co. (CPC) by making an equity investment of SAR281.5 million (USD75 million). The deal reveals increasing foreign investment in the Kingdom due to robust economic growth.
- **Iran to privatize national airlines:** The Irani government hopes to privatize its national airline, Iran Air, for more than USD1.5 billion. The country intends to avert the impact of tightening US sanctions that bar it from buying aircraft and spare parts.
- **UAE investment firm buys stake in Dhofar Fisheries:** Flag Holding, an Abu Dhabi-based investment firm, bought a 39.12% stake (993,811 shares) in Dhofar Fisheries Industries (DFIC) from Oman Emirates Investment Holding Company (OEIH) for a consideration of OMR899,399 based on an enterprise valuation of OMR2.3 million.

Equity Markets

Qatar

- **Qatar Exchange recovers:** After declining to its lowest level in two years on August 11 due to worries over global economic downtrend, the Qatar Exchange gained some ground and recorded marginal gains as investors bought battered stocks at lower levels.
- **Qatari companies may be burdened with tax soon:** With the Ministry of Economy and Finance issuing a circular that makes it mandatory for 100% Qatari-owned companies with either over QAR2 million in share capital or more than QAR10 million in yearly turnover to file tax return, many local companies fear coming under the tax bracket soon.

MENA equity indices (TTM, rebased)

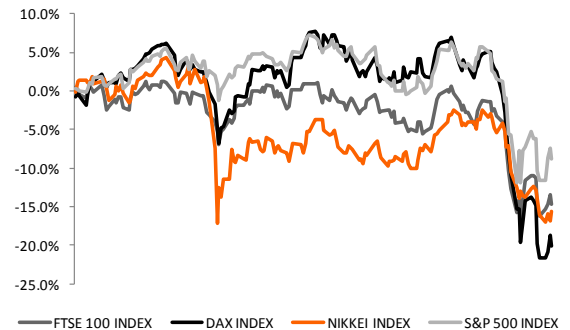


Source: Bloomberg

MENA

- **Gulf stocks end marginally higher:** Most Gulf stocks edged higher at the close of the month, tracking gains in the US equities. However, volumes remained thin as markets were closed for a few days towards the end of the month due to religious holidays.
- **Gulf IPO market less active in 1H2011:** Total value and number of initial public offerings (IPOs) in the GCC fell sharply in the first half of the year. Just four companies were listed (with a value of USD358 million) during the period compared to eight listings (USD830 million) in the same period last year. Three companies debuted on the UAE bourse, while just one company was listed on the Saudi Arabian exchange.
- **MENA region witnesses increased M&A activity in 1H2011:** Despite the political unrest in the MENA region, M&A deal volumes increased 33% in 1H2011, with the number of deals rising to 173 from 130 in the year-ago period. In terms of total value, deals worth USD21.17 billion were concluded in 1H2011 compared to USD16.26 billion in 1H2010, implying an increase of 30%.

Advanced markets equity indices (TTM, rebased)

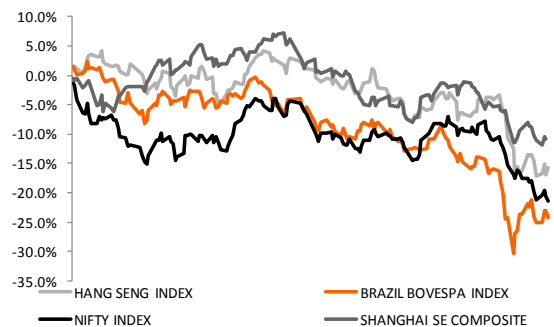


Source: Bloomberg

Global

- **Asian markets fall on mounting concerns over the health of the US economy:** Asian markets were volatile throughout the month of August due to rising concerns over the health of the US economy. Markets turned more cautious towards the end of the month as investors awaited Fed Chairman Bernanke's speech to gauge if the US authorities would undertake any steps to save the US economy from once again falling into recession. Also, disappointing earning reports from Chinese firms in the second quarter added further pressure on the country's stock market.
- **European markets end lower:** On August 25, Germany's DAX declined 4% in 15 minutes on speculation that regulators planned to impose further restrictions on equity markets. Also, markets were rife with rumors that the French and Spanish regulators would extend the ban on short selling, thereby reducing the scope for trading in European markets.

Emerging markets equity indices (TTM, rebased)



Source: Bloomberg

QE 30: Top gainers for the month

Top 5 Gainers	Last Close	MTD %	YTD%
MERS QD Equity	129.5	29.4%	121.0%
ABQK QD Equity	77.5	10.4%	34.2%
DHBK QD Equity	58.8	9.9%	-0.9%
QMLS QD Equity	21.2	3.5%	48.6%
QGRI QD Equity	45.0	7.1%	-6.6%

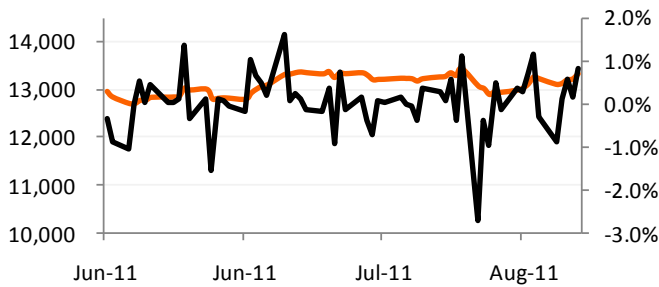
Source: Bloomberg

QE 30: Top losers for the month

Top 5 Losers	Last Close	MTD %	YTD%
GISS QD Equity	24.6	-12.8%	-9.0%
IQCD QD Equity	123.0	-12.1%	-7.2%
MRDS QD Equity	7.8	-10.8%	-23.0%
QCFS QD Equity	55.9	-9.8%	91.0%
AHCS QD Equity	16.6	-8.4%	-19.8%

Source: Bloomberg

Qatar Banking Sector Index - MTD



Source: Bloomberg

QE 30: 3 Month Movement and Turnover



Source: Bloomberg

Qatar Banking Sector Index - MTD

Index	Last Close	MTD %	YTD %	3YR %	PE Ratio
Qatar (DSM)	8,171.5	-2.9%	-5.9%	-23.6%	10.7
KSA (TASI)	5,979.3	-7.6%	-9.7%	-32.8%	13.8
UAE (DFM)	1,457.3	-4.5%	-10.6%	-70.2%	29.7
Abu Dhabi (ADSM)	2,582.1	-2.1%	-5.1%	-42.6%	15.3
Kuwait (KSE)	5,785.6	-4.2%	-16.8%	-60.3%	NM
Oman (MSM)	5,584.7	-4.2%	-17.3%	-45.2%	7.6
Bahrain (BSE)	1,261.0	-2.3%	-12.0%	-53.4%	11.1
Egypt (CASE)	4,676.1	-7.8%	-34.5%	-42.7%	9.8
Turkey (ISE 100)	52,967.7	-14.5%	-19.8%	30.2%	10.4
Jordan (Amman)	2,028.1	-2.3%	-14.6%	-52.4%	NM
DJMENA Index	473.1	-5.5%	-13.8%	-41.6%	NM
MASI INDEX	23,152.4	0.6%	-11.6%	-17.7%	NM

Source: Bloomberg

QE 30: 3 Month Movement and Turnover

Index	Last Close	MTD %	YTD %	3YR %	PE Ratio
US (S&P 500)	1,159.3	-9.9%	-7.8%	-8.5%	12.7
UK (FTSE)	5,131.1	-11.1%	-13.0%	-6.2%	10.2
Germany (DAX)	5,584.1	-19.7%	-19.2%	-11.3%	9.9
Japan (Nikkei)	8,772.4	-12.0%	-14.2%	-31.9%	16.5
Hong Kong (HSI)	19,752.5	-12.8%	-14.1%	-6.4%	9.2
S. Korea (KOSPI)	1,764.6	-18.8%	-14.0%	17.5%	11.7
Brazil (IBOV)	52,953.3	-9.5%	-23.6%	-2.8%	8.1
India (NIFTY)	4,839.6	-12.3%	-20.7%	11.6%	13.9
China (SCI)	2,615.3	-3.3%	-5.2%	8.4%	14.2

Source: Bloomberg

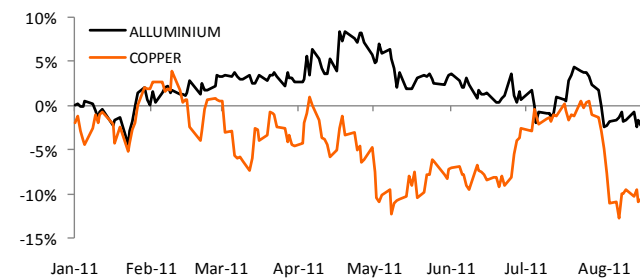
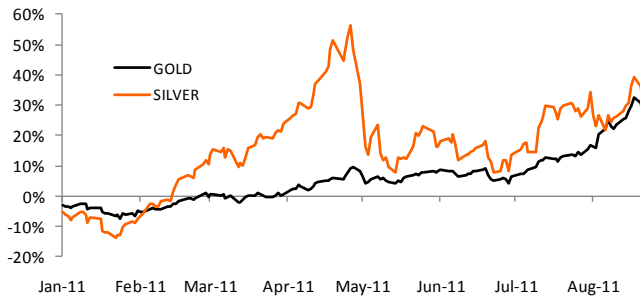
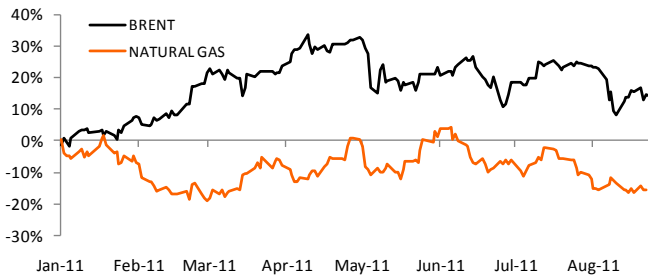
Commodities and Currencies

Commodities

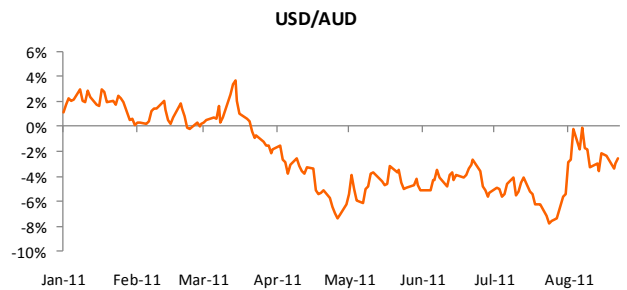
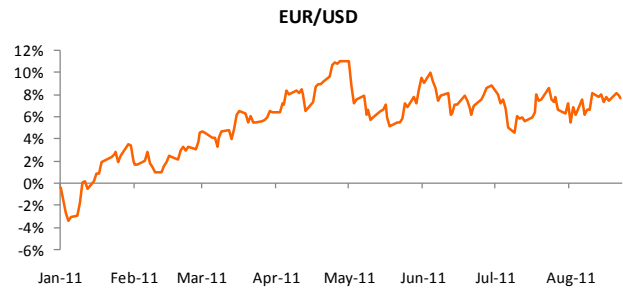
Index	Last Close	MTD %	YTD %	3YR %
WTI Crude (\$/bbl)	85.3	-10.1%	-6.7%	-25.9%
Brent Crude (\$/bbl)	110.6	-5.3%	16.7%	-3.0%
Nat. Gas (\$/mmbtu)	3.9	-6.1%	-10.8%	-49.8%
Gold (\$/oz)	1,759.8	8.7%	23.8%	114.7%
Silver (\$/oz)	40.7	3.7%	31.8%	204.7%
Copper (c/lb)	407.9	-7.4%	-8.1%	15.9%
Aluminium (\$/MT)	2,275.0	-4.5%	-0.9%	-8.0%
Wheat (c/bu)	757.3	11.9%	-4.7%	-9.9%
Rice (\$/cwt)	16.8	3.1%	19.7%	-8.2%
Corn (Usd/bu)	732.3	7.5%	16.4%	26.2%

Currencies

Main Currency Pair	Last Close	MTD %	YTD %	3YR %
EUR/USD	1.4	0.9%	7.4%	-2.5%
GBP/USD	1.6	-0.1%	4.3%	-12.1%
USD/JPY	77.5	0.3%	-4.5%	-29.1%
USD/KWD	1.3	-1.2%	17.9%	38.2%
Emerging market	Last Close	MTD %	YTD %	3YR %
USD/INR	46.1	4.5%	3.0%	5.2%
USD/CNY	6.4	-0.7%	-3.3%	-6.7%
USD/BRL	1.6	2.8%	-3.1%	-1.3%
USD/TRY	1.8	3.7%	13.7%	47.8%
MENA Currency	Last Close	MTD %	YTD %	3YR %
SAR	3.8	0.0%	0.0%	0.0%
AED	3.7	0.0%	0.0%	0.0%
QAR	3.6	0.0%	0.0%	0.0%



Source: Bloomberg



Source: Bloomberg

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