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IIF REGIONAL OVERVIEW

The Arab World in Transition: Assessing the Economic Impact

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George T. Abed

SENIOR COUNSELLOR AND DIRECTOR
Africa/Middle East Department

1-202-857-3644
gabed@iif.com

Garbis Iradian

DEPUTY DIRECTOR
Africa/Middle East Department

1-202-857-3304
giradian@iif.com

David Hedley

DEPUTY DIRECTOR
Africa/Middle East Department

1-202-857-3605
dhedley@iif.com

Nafez Zouk

SENIOR RESEARCH ASSISTANT
Africa/Middle East Department

1-202-857-3621
nzouk@iif.com

EXECUTIVE SUMMARY

The popular uprisings in the Arab world represent a historic turning point and could constitute a structural break with decades of authoritarian rule, weak institutions and poor governance, mediocre growth, and chronic unemployment. While the origins of the uprisings were similar across the region, the transitions are taking different paths.

The transitions will be shaped principally by the strength (or weakness) of the forces of social cohesion and the robustness of state and civil society institutions in each of the countries. In Egypt and Tunisia, the transitions have been orderly, while in Libya and Yemen the challenge to the regimes has turned into open conflict (Libya) or a drift to an uncertain future (Yemen). In other countries, grievances are being addressed where regimes are not fundamentally challenged (Jordan, Morocco, Saudi Arabia), or remain unresolved (Bahrain), or are being suppressed with force (Syria). The ultimate outcomes of the current turmoil remain uncertain. While the new order in the region could bring about more open, inclusive, and accountable governments, the achievement of stable democracies with robust and effective institutions will require fundamental political and economic reforms and will take time.

The economic impact on the countries themselves has shown clear divergence, reflecting in large part the repercussions of the crisis on global oil markets, as seen in the sharp run-up in oil prices and the shifts in the pattern of oil production. Arab oil exporters (except Libya and Yemen) have seen a surge in revenues and a pickup in growth while oil-importing countries will experience slower growth and weaker fiscal and external outcomes.

In the group of Arab oil exporters, Iraq and Qatar are projected to record double-digit growth, underpinned by large increases in crude oil and LNG production, respectively. For GCC countries, average growth is projected to rise from 5.1% in 2010 to 6.5% in 2011, buoyed by higher oil production and large increases in government spending. Higher oil prices (up from $80 per barrel in 2010 to $115 in 2011 and $110 in 2012) and production levels should help lift the GCC's budget revenues from hydrocarbon exports from $362 billion in 2010 to $533 billion in 2011. This surge in revenues far exceeds the increases in government spending and underlies the widening of the consolidated fiscal surplus from 8.0% of GDP in 2010 to 13.2% in 2011.

The combined external current account surplus of the GCC is projected to rise from $129 billion in 2010 to $292 billion in 2011. Consequently, gross foreign assets of the GCC countries in 2011 are projected to rise to $1.7 trillion (against foreign liabilities of $0.5 trillion) and of the Arab countries to $2.2 trillion (against total foreign liabilities of $0.7 trillion). More than one-third of the region's gross assets are held by sovereign wealth funds (SWFs). Despite the turmoil in the region, we do not expect to see significant shifts in funds managed by the sovereigns as a specific response to the crisis.

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Executive Summary

In the oil-importing countries, the economic toll from the political turmoil will translate into a sharp drop in growth rates in 2011, with a likely rebound in 2012. For the countries affected by the turmoil, we expect no increase in real output this year. Real GDP growth in several nonoil countries—Egypt, Jordan, Lebanon, Morocco, Syria, and Tunisia—will slump from an average of 4.4% in 2010 to be -0.5% in 2011. Furthermore, inflationary pressures are expected to rise, and current accounts to weaken, while some countries will see the erosion of reserves and pressures on their currencies. Nonetheless, these countries are buffered by adequate reserves and therefore not expected to suffer serious external vulnerabilities, although the risks will remain on the downside.

Regional financial markets have reacted negatively. Stock market indices suffered, with some differentiation, in comparison with the overall emerging market benchmark. As expected, the turmoil has raised risk premia, leading to some widening of spreads for credit default swaps and for both fixed-income securities and (Islamic) sukuks. These, however, have remained far below comparable measures for, say, the peripheral Euro-area countries. Nonetheless, funding costs have risen for those countries having to refinance maturing debt this year.

It is clear that for the affected countries, restoration of internal stability and an overwhelming political and constitutional agenda will occupy the transition leaderships for some time. Economic issues are therefore likely to take a back seat. However, for countries seeking external assistance, notably Egypt and Tunisia, an economic policy framework will be needed to reach agreement with the international donor community. At the same time, most countries in the region, especially nonoil producers, are in urgent need of taking up economic reforms so as to help shore up their weakening economies and to speed up a return to higher and, it is now hoped, more equitable growth.

As momentous as the current security and political restructuring challenges may be, it is absolutely critical that the transition authorities also place a high priority on deepening and accelerating structural economic reforms. Among the populations of countries such as Egypt, Tunisia, Jordan and Morocco, expectations are that change will bring about a revival of growth that will be more widely shared, improved job opportunities and, in general, a better life.

To this end, transition and subsequent governments must articulate a credible medium-term reform and stabilization framework that addresses the need for higher growth and job creation. Given the relatively large size and low productivity of public sectors in the region, the reform agenda would need to focus on creating the legal and institutional environment for fostering entrepreneurship, investment, and market-driven growth. This task must be addressed without delay, for the longer reforms are postponed, the further economic performance will weaken and the more painful the adjustment will have to be when available policy margins are exhausted. Moreover, there is a real risk of a second wave of protests if the prospects for improvement in living conditions remain dim.

Some of the affected countries are already in discussions with bilateral donors and/or with the international financial institutions (IFIs) on aid packages to see them through a difficult transition. It is important that financial support from the IFIs, regional multilaterals, and the region's oil exporters be provided in the context of such a medium-term reform framework.

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Executive Summary

Arab World Outlook: Main Macroeconomic Indicators

	GDP ($ billion)	Real GDP Growth (% change)			Unemployment, 2009 (% of Labor Force)		Fiscal Balance (% GDP)		Current Account Bal. (% GDP)	
	2010e	2010e	2011f	2012f	Overall	Youth	2010e	2011f	2010e	2011f
Arab World	**1911**	**4.6**	**4.7**	**4.6**	**11.5**	**25.2**	**2.5**	**6.7**	**6.4**	**13.1**
GCC	**1024**	**5.1**	**6.5**	**4.3**	**...**	**...**	**8.0**	**13.2**	**12.5**	**21.9**
Bahrain	23	4.5	2.9	5.2	3.8	...	-6.6	1.3	3.4	11.0
Kuwait	127	2.0	4.4	4.3	...	...	28.9	31.2	30.7	40.4
Oman	57	4.8	4.6	5.0	...	...	3.2	11.9	11.6	21.9
Qatar	129	18.5	18.1	6.1	...	...	11.9	10.6	16.8	26.4
Saudi Arabia	437	3.5	5.3	3.8	10.2	23.2	7.2	12.7	8.9	19.8
UAE	251	2.7	3.8	4.0	...	...	-0.9	7.1	8.6	14.1
Non-GCC Oil Exp.	**409**	**3.6**	**5.2**	**6.0**	**14.1**	**26.2**	**-1.4**	**2.4**	**3.7**	**7.2**
Algeria	149	3.2	3.3	3.6	9.7	21.5	-2.6	2.7	7.5	16.0
Iraq	81	0.8	11.0	11.3	14.3	26.8	-11.4	6.4	-7.2	2.6
Libya*	83	4.6	...	...	...	...	13.0	...	19.8	...
Sudan	66	5.0	4.5	5.0	16.2	27.1	-3.0	-1.0	-8.0	-4.2
Yemen	30	7.0	-4.0	3.0	15.7	26.2	-4.5	-7.0	-4.3	-4.7
Oil Importers	**478**	**4.4**	**-0.5**	**4.2**	**11.1**	**26.5**	**-6.0**	**-7.5**	**-4.3**	**-5.7**
Egypt**	218	5.0	-2.5	4.2	9.5	27.2	-8.1	-9.4	-2.0	-2.5
Jordan	28	3.1	2.8	4.0	12.5	26.8	-5.4	-6.7	-4.3	-9.0
Lebanon	39	7.0	4.0	5.7	8.0	21.5	-7.5	-9.5	-16.1	-18.1
Morocco	90	3.4	3.3	4.5	9.1	24.9	-4.5	-5.2	-4.8	-5.9
Syria	60	3.5	-3.0	2.0	11.0	23.0	-3.1	-5.0	-4.5	-5.4
Tunisia	44	3.4	-1.5	5.2	13.3	28.47	-1.4	-4.5	-4.7	-7.5
Memoranda:										
South and East Asia	...	9.1	8.2	8.1	4.8	11.3	-4.0	-3.6	7.0	6.2
Latin America	…	6.0	4.1	4.4	7.7	15.7	-2.9	-2.2	-1.3	-1.7

e = estimate; f = IIF forecast
* Absence of projections for Libya due to lack of political certainty.
** Egypt growth rates have been adjusted to a calendar year basis to make them consistent with other countries, while figures for inflation and the fiscal and current accounts are on a fiscal year basis.

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Regional Overview

THE ARAB WORLD: A REGION IN TURMOIL

The IIF is launching its Arab World report at a time of unprecedented change in the region. In this report we assess the short-term implications of the events since the beginning of the year. The analysis focuses exclusively on the Arab countries rather than the MENA region, which also includes Iran and Pakistan according to the IMF classification. The Arab countries can be divided into three distinct groups: (i) GCC (Saudi Arabia, the UAE, Kuwait, Qatar, Oman, and Bahrain); (ii) non-GCC oil exporters (Algeria, Iraq, Libya, Sudan, and Yemen); and (iii) oil importers (Egypt, Jordan, Lebanon, Morocco, Tunisia, and Syria). The GCC countries have not been as vulnerable as other Arab countries to the unrest that is sweeping the region, thanks to their ample hydrocarbon resources, small populations (except Saudi Arabia), leading to a greater reliance on foreign labor, and generous social benefits. Bahrain has been an exception, where calls for reforms were shaped in part by sectarian tension.

Our projections in this report are based on a forecast of **global** growth of 3.7% in 2011 and 4.1% in 2012, using market exchange rates weights, and average Brent **oil prices** of $115 per barrel in 2011 and $110 in 2012. We also assume that the current conflicts in Libya, Syria, and Yemen will be resolved before the end of this year.

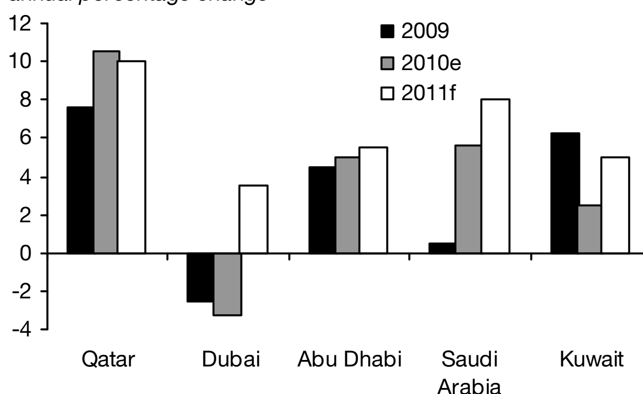
For the **oil importers** as a group, the economic toll from the political upheaval will translate into a small contraction in output of 0.5% in 2011 before a rebound to 4.2% in 2012, depending on the duration of the upheaval (Table 1). In particular, tourism, foreign direct investment, and local private investment will be hard-hit. In addition to domestic disorder, Egypt and Tunisia have been adversely impacted by the civil war in Libya and the resultant return of about 120,000 migrant workers. Output in Egypt, Tunisia, and Syria is expected to contract between 1% and 3%, while growth in Lebanon and Jordan will decelerate to 4% and 2.8%, respectively. Growth in Morocco is projected at 3.3%, driven in part by a rebound in agricultural output. In general, the banking system in these countries have so far been resilient to the crisis, given their high liquidity. However, nonperforming loans could rise significantly, particularly in Egypt and Tunisia. The projection of growth in 2012 in Table 1 assumes that the unrest in the region will come to an end before end-2012.

Table 1
Arab World: Real GDP

	Population (million)	GDP ($ bn)	Real GDP Growth (% change)		
	2010e	2010e	2010e	2011f	2012f
Arab World	**338.6**	**1912**	**4.6**	**4.7**	**4.6**
GCC	**40.3**	**1024**	**5.1**	**6.5**	**4.3**
Bahrain	1.2	23	4.5	2.9	5.2
Kuwait	3.5	127	2.0	4.4	4.3
Oman	2.7	57	4.8	4.6	5.0
Qatar	1.7	129	18.5	19.0	6.1
Saudi Arabia	26.6	437	3.5	5.3	3.8
UAE	4.6	251	2.7	3.8	4.0
Non-GCC Oil Exp.	**139.3**	**410**	**3.6**	**5.2**	**6.0**
Algeria	35.4	149	3.2	3.3	3.6
Iraq	31.4	82	1.3	11.1	11.5
Libya*	6.5	82	4.6	...	...
Sudan	42.3	66	5.0	4.5	5.0
Yemen	23.6	30	7.0	-4.0	3.0
Oil Importers	**159.1**	**478**	**4.4**	**-0.5**	**4.2**
Egypt**	83.5	218	5.6	-2.5	4.2
Jordan	6.3	28	3.1	2.8	4.0
Lebanon	4.3	39	7.0	4.0	5.7
Morocco	32.4	90	3.4	3.3	4.5
Syria	21.9	60	7.0	-3.0	2.0
Tunisia	10.7	44	3.1	-1.5	5.2

e = estimate; f = IIF forecast
* Absence of projections for Libya due to lack of political certainty.
** Egypt growth rates have been adjusted to calendar year basis to make them consistent with other countries, while figures for inflation and the fiscal and current accounts are on a fiscal year basis.

Chart 1
GCC: Credit to the Private Sector Will Recover Gradually
annual percentage change



e = estimate; f = IIF forecast

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GCC: GROWTH ACCELERATES, SURPLUSES WIDEN

By contrast, growth in the GCC will accelerate from an estimated 5.1% in 2010 to 6.5% in 2011, driven by expansion in crude oil production and larger increases in public spending. The GCC growth average masks wide variations in prospects for individual countries (Table 2).

Saudi Arabia is expected to return to strong growth of 5.3% in 2011, underpinned by a significant increase in oil production and a substantial increase government spending (around 30%). Nonhydrocarbon real GDP growth is projected at 5.1% for this year, driven mainly by private consumption and government investment. In the **UAE**, growth is expected to accelerate from 2.7% in 2010 to 3.8% in 2011 and to 4.0% in 2012. The turmoil in the Arab world could indirectly boost the Emirates' economy through the following channels: (i) higher production of crude oil in Abu Dhabi; (ii) higher revenues due to a spike in oil prices; and (iii) a diversion to the UAE of some of the regional trade, transportation, tourism, and finance. Dubai's economy is expected to recover significantly, growing by 3.5% in 2011 as compared to 1.7% in 2010.

The strongest performer in the region is again **Qatar**, where overall real GDP is projected to grow by 19% in 2011, driven by further large expansion in natural gas production and public investment expenditures. In **Kuwait** growth is projected to accelerate from 2.0% in 2010 to 4.4% in 2011—spurred by government spending in the context of the government's $107 billion investment plan (2010-2014). **Bahrain's** economic recovery has been interrupted and growth could slow to 2.9% in 2011 from 4.5% in 2010, with considerable downside risk if the situation goes unresolved for an extended period.

For 2011 and beyond, we expect a small improvement in private credit growth as GCC banks' deleveraging tapers off (Chart 1). The provisioning for nonperforming loans will also slow, following the increases of the past two years. As capital inflows to the region are likely to remain weak, the funding of credit growth will have to rely more on domestic deposit growth, and this is feasible. The U.S. Fed continues to signal that monetary policy will remain on hold until there are stronger signs that excess capacity in product and labor markets is falling more rapidly. Continued low interest rates will therefore support some recovery in private sector credit growth, boosting nonhydrocarbon growth in the GCC.

Table 2
GCC: Growth, Inflation, and Current Account

	2008	2009	2010e	2011f	2012f
			Overall Growth		
GCC	6.8	-0.2	5.1	6.5	4.3
Saudi Arabia	4.5	0.6	3.5	5.3	3.8
UAE	5.4	-3.0	2.7	3.8	4.0
Kuwait	5.0	-5.1	2.0	4.4	4.3
Qatar	25.4	8.6	18.5	18.1	6.1
Oman	12.8	1.1	4.8	4.6	5.0
Bahrain	6.3	3.1	4.5	2.9	5.2
			Hydrocarbon Growth, %		
GCC	6.0	-5.3	6.6	8.9	2.7
Saudi Arabia	4.2	-7.5	2.2	6.0	2.0
UAE	2.4	-8.5	3.4	4.5	3.7
Kuwait	4.4	-10.2	1.4	5.0	2.7
Qatar	23.1	7.7	27.9	26.3	3.9
Oman	6.2	4.9	6.7	5.0	2.0
Bahrain	0.4	-0.3	1.5	2.5	3.5
			Nonhydrocarbon Growth, %		
GCC	8.1	1.6	3.9	4.7	5.1
Saudi Arabia	4.3	3.4	4.0	5.1	4.5
UAE	6.3	-1.3	2.5	3.6	4.1
Abu Dhabi	7.0	2.6	3.5	3.7	4.2
Dubai	5.7	-4.5	1.7	3.5	4.0
Kuwait	5.4	-1.9	2.3	4.0	5.2
Qatar	27.8	9.6	9.2	8.5	8.9
Oman	15.7	-0.3	4.0	4.5	6.3
Bahrain	7.0	3.4	4.8	2.9	5.4
			Inflation, Average, %		
GCC	11.1	2.8	2.9	4.4	4.8
Saudi Arabia	9.9	5.1	5.4	5.7	6.3
UAE	12.3	-0.7	0.6	1.9	3.3
Kuwait	10.6	4.0	4.0	6.2	4.2
Qatar	15.2	-4.9	-2.4	3.0	4.0
Oman	12.4	3.5	3.3	3.7	3.4
Bahrain	3.5	2.8	1.9	2.4	2.2
			Current Account Balance, $ billion		
GCC	248.0	67.0	128.5	292.3	234.8
Saudi Arabia	135.3	21.0	38.8	113.9	86.4
UAE	23.0	8.2	21.6	42.6	36.9
Kuwait	58.7	26.7	39.1	67.9	58.9
Qatar	33.1	10.9	21.6	48.9	37.4
Oman	5.0	-0.3	6.6	16.4	11.5
Bahrain	2.3	0.6	0.8	2.9	3.7

e = estimate; f = IIF forecast

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CURRENT ACCOUNT SURPLUS WIDENS IN GCC, WHILE DEFICITS RISE IN OIL IMPORTERS

The GCC's overall current account balance is expected to widen from an estimate of $129 billion in 2010 to $292 billion (equivalent to 22% of GDP) in 2011 (Table 3). Hydrocarbon exports will rise from $448 billion in 2010 to $681 billion in 2011. Nonhydrocarbon exports will also increase significantly to $214 billion (mainly petrochemicals from Saudi Arabia and re-exports from the UAE). Imports of goods are projected to increase by 18% to $414 billion, well above the previous peak of $368 billion reached in 2008.

Consequently, gross foreign assets of the GCC are projected to rise from $1.5 trillion to $1.7 trillion in 2011, against foreign liabilities of $0.5 trillion (Table 4). At least three-quarters of the region's financial assets are held by countries that are not subject to unrest, including Saudi Arabia, the UAE, Qatar, and Kuwait. More than one-third of these assets are held by (SWFs). While most of these assets are currently invested in the international financial system, there had also been a rising interest in the domestic and regional markets until recent events. With relatively low external debt, the large net foreign assets ($1.2 trillion) of the GCC will continue to provide governments with the flexibility to support growth through robust government spending levels in the next few years.

In the oil importers, the external current account deficit is projected to widen from 4.3% of GDP in 2010 to 5.7% in 2011. This deterioration is due to a sharp drop in earnings from tourism, particularly in Egypt, Lebanon, Syria, and Tunisia, and a substantial increase in the import bill as a result of high oil prices (particularly in Jordan, Morocco, and Lebanon). In Egypt, the disruption to exports and drop in tourist arrivals will widen the current account deficit. This, together with portfolio outflows and a reduction in FDI, has put increased pressure on the balance of payments.

Both Egypt and Tunisia (and soon perhaps other countries in the region) are in discussions with potential multilateral and bilateral donors, including countries of the GCC, on possible aid programs. Undoubtedly, financial resources are important at this pivotal moment in these countries' transitions. However, it is equally important that these countries also commit to a medium term framework of reforms that would help secure their long-term growth and prosperity.

Table 3
Arab World: Current Accounts

	Current Account Bal. (% GDP)		Current Account Bal. ($ billion)	
	2010e	2011f	2010e	2011f
Arab World	**6.4**	**13.1**	**123.4**	**292.6**
GCC	**12.5**	**21.8**	**128.5**	**292.3**
Bahrain	3.4	11.0	0.8	2.9
Kuwait	30.7	40.4	39.1	67.9
Oman	11.6	21.9	6.6	16.4
Qatar	16.8	26.4	21.6	48.9
Saudi Arabia	8.8	19.6	38.8	113.9
UAE	8.6	14.1	21.6	43.6
Non-GCC Oil Exp.	**3.7**	**7.2**	**15.6**	**29.4**
Algeria	7.5	16.0	11.9	31.0
Iraq	-7.2	3.1	-6.0	3.7
Libya	19.8	...	16.5	…
Sudan	8.0	-4.2	-5.7	-3.4
Yemen	-4.3	-4.7	-1.5	-1.9
Oil Importers	**-4.3**	**-5.7**	**-20.7**	**-28.5**
Egypt	-2.0	-2.5	-4.3	-5.9
Jordan	-4.3	-9.0	-1.2	-2.7
Lebanon	-16.1	-18.3	-6.2	-7.6
Morocco	-4.8	-5.8	-4.3	-5.6
Syria	-4.5	-5.4	-2.7	-3.4
Tunisia	-4.7	-7.5	-2.1	-3.2

e = estimate; f = IIF forecast

Table 4
Arab World: Foreign Assets and Liabilities

	2008	2009	2010e	2011f
		$ billion		
Total Foreign Assets	1807	1860	2053	2228
Oil Exporters	1668	1701	1882	2074
GCC	1332	1350	1511	1706
Algeria, Iraq, Libya	336	351	371	368
Oil Importers	139	159	171	153
Total Foreign Liabilities	667	676	724	734
Oil Exporters	541	549	586	593
GCC	439	446	488	507
Algeria, Iraq, Libya	103	103	98	86
Oil Importers	126	127	138	141
		% GDP		
Total Foreign Assets	95	112	107	96
Total Foreign Liabilities	35	41	38	32

e = estimate; f = IIF forecast

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INFLATION RISES ACROSS THE REGION, OIL IMPORTERS' BUDGETS WEAKEN

Inflation is on the rise across the Arab region, led by higher global food prices and substantial increases in government spending. To forestall discontent arising from political and economic conditions, most governments in Arab countries announced supplementary spending programs. In Saudi Arabia and Kuwait, the spending increase will generate more inflationary pressures as domestic demand was already strong. The year-on-year (yoy) inflation rate is expected to rise to 5.7% by end-2011 in Saudi Arabia, and to 6.2% in Kuwait. In the UAE and Qatar, inflationary pressures will remain limited as a further fall in rents, albeit at a slower pace, will partly offset the rise in food and other items (Table 5).

The consolidated fiscal surplus of the GCC will widen from 7.9% of GDP in 2010 to 13.2% in 2011 under the assumption of an average oil price of $115 per barrel for Brent. The sharp increase in government revenue from oil and gas due to higher oil prices, and an expected 5% increase in export volumes for the GCC as a whole (28% increase in LNG exports in Qatar), will more than offset the substantial increase in government spending in Kuwait, Qatar, and Saudi Arabia. In the UAE also, the consolidated fiscal balance (the federal budget, Abu Dhabi's budget, and Dubai's budget) will show a large surplus equivalent to 7.2% of GDP in 2011, as compared to a small deficit of less than 1% in 2010. Consolidated government spending in the GCC is expected to increase by 25% in 2011.

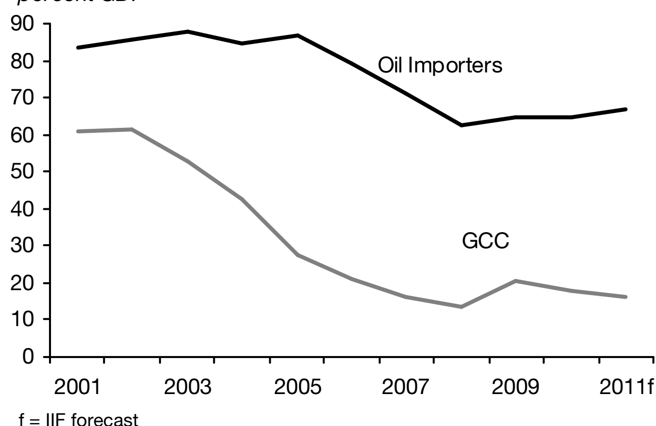
The political upheaval in the region will widen the fiscal deficits of the oil importers and postpone the much-needed fiscal reforms. To help mitigate the adverse impact of the spike in global food and oil prices, most oil importers increased food and fuel subsidies, raised wages and pensions, and expanded employment in the public sector. This, combined with weaker economic activity will widen the fiscal deficits for oil importers as a group from 6.0% of GDP in 2010 to 7.4% in 2011. The fiscal deficits are projected to widen to 9.4% of GDP in Egypt, 9.5% in Lebanon, 6.5% in Morocco, and 4.5% in Tunisia (Table 5). In these countries deficit financing usually comes from domestic sources and should not pose an undue problem this year, although risks could rise over the medium term. Government debt for oil importers is projected to increase from 65% of GDP in 2010 to 67% in 2011 (Chart 2).

Table 5
Arab World: Inflation and Fiscal Balances

	CPI Inflation (average, % chg.)		Fiscal Balance (% GDP)	
	2010e	2011f	2010e	2011f
Arab World	**4.5**	**5.7**	**2.5**	**6.7**
GCC	**2.9**	**4.4**	**7.9**	**13.2**
Bahrain	1.9	2.4	-6.6	1.0
Kuwait	4.0	6.2	28.9	31.2
Oman	3.3	3.6	3.2	11.9
Qatar	-2.4	3.0	11.9	10.6
Saudi Arabia	5.4	5.7	7.2	12.7
UAE	0.6	1.9	-0.9	7.2
Non-GCC Oil Exp.	**5.9**	**7.2**	**-1.4**	**2.4**
Algeria	4.3	5.1	-2.6	2.7
Iraq	4.5	7.0	-11.5	6.3
Libya	2.5	…	13.0	...
Sudan	13.0	10.0	-3.0	-1.0
Yemen	12.0	15.0	-4.5	-7.0
Oil Importers	**7.2**	**8.1**	**-6.0**	**-7.4**
Egypt	11.7	11.5	-8.1	-9.4
Jordan	5.0	6.1	-5.4	-6.7
Lebanon	4.4	6.5	-7.5	-9.5
Morocco	1.0	3.3	-6.0	-6.5
Syria	4.5	8.0	-3.1	-5.0
Tunisia	4.5	4.2	-1.4	-4.5

e = estimate; f = IIF forecast

Chart 2
Arab World Government Debt
percent GDP



f = IIF forecast

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Regional Overview

ARAB WORLD ROLE IN THE ENERGY MARKET

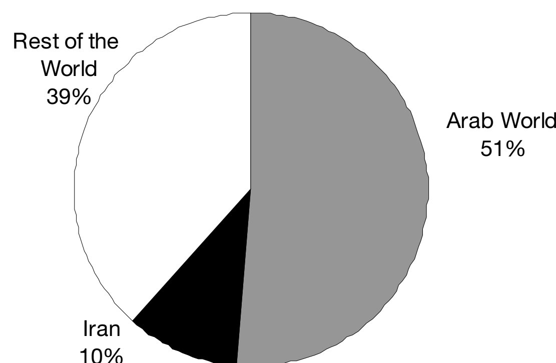
The Arab world is endowed with 51% of the world's proven oil reserves and 22% of proven gas reserves (Chart 3). The Arab world as a group remains the world's largest producer of crude oil (accounting for 30% of global exports). Over the medium term, most of the increase in the global production of crude oil is expected to come from the region, mainly from Saudi Arabia and Iraq.

With its current production of 8.9 million barrels a day (mbd) and production capacity of 12.1 mbd, Saudi Arabia accounts for more than half of the world's spare production capacity (Table 6). Unconfirmed reports indicate that its production capacity will increase further to around 15 mbd by end-2015. Qatar's natural gas production will increase further this year to about 16 billion cubic feet per day, making it the second largest producer of natural gas after Russia (Table 7).

The oil market is currently tight. In 2010, global demand increased by 3.2%, the second highest in the last 15 years. Oil prices have risen due to some supply disruptions and increased supply risks. Declines in Libyan production equivalent to 1.5% of global supply have been broadly offset by higher production in Saudi Arabia, Kuwait, the UAE, and Iraq. The IIF's average oil forecast is $115 per barrel for 2011 and $110 per barrel in 2012. This forecast is based on the assumption that political conditions in the Arab region eventually improve, allowing supply-side pressures to subside and oil prices to come down during the second half of the year.

The call on OPEC (global demand minus non-OPEC supply) will likely increase markedly in the coming years. At the same time, the earthquake in Japan may increase oil demand gradually, due to reconstruction and substitution away from nuclear power generation. Futures markets anticipate a very gradual reduction in oil supply uncertainty, partly reflecting the continued unrest in the Arab world and the threat of spillover to other oil exporters in the region. This would imply that oil prices could stay over $100 per barrel for some time.

Chart 3
Geographical Distribution of Proven Oil Reserves, 2010
percentage share in world



Source: British Petroleum.

Table 6
OPEC Crude Oil Production and Spare Capacity
million barrels/day

	OPEC Target	2011f	Capacity in 2011	Spare Capacity
Arab OPEC	...	19.35	22.80	4.11
Saudi Arabia	8.05	8.85	12.10	3.25
Iraq	n/a	2.75	3.00	0.25
UAE	2.22	2.48	2.60	0.12
Kuwait	2.22	2.42	2.65	0.23
Qatar	0.73	0.83	0.85	0.02
Libya	1.50	0.70	...	...
Algeria	1.25	1.28	1.40	0.12
Iran	3.33	3.70	3.70	0.00
Other OPEC	...	6.53	7.20	0.85

f = IIF forecast

Table 7
Natural Gas Production and Reserves, 2010

	Production (billion cubic feet/day)	Reserves (trillion cubic feet)
Global Total	289.0	187.5
Russia	51.0	44.4
Iran	12.7	29.6
Qatar	12.4	25.4
Saudi Arabia	7.5	7.9
Algeria	7.9	4.5
Egypt	6.1	2.2
Norway	10.0	2.1

Source: Energy Information Administration, BP, and IIF.

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HIGHER RISK PREMIA IN FINANCIAL MARKETS

The turmoil has raised risk premia in the region's financial markets (Table 8). This could lead to more challenging market conditions for the corporate sector in the region, including public enterprises, and for countries in need of refinancing external debt. Spreads on sovereign bonds and credit default swaps (CDS) have widened throughout the region, although to varying degrees depending on the risks arising from transition conditions.

Bahrain's 5-year sovereign CDS spread has risen from 186 bps at end-2010 to 266 bps as of April 29, 2011. In contrast, market sentiment has improved in Dubai, as indicated by the narrowing of its CDS spreads from 415 bps at end-2010 to 350 bps as of April 29, 2011. Abu Dhabi's and Qatar's CDS spreads remain the lowest among all Arab countries, and well below the average for other emerging economies. Among oil importers, CDS spreads have widened for Egypt (351 bps) and Lebanon (361 bps), but remain well below the spreads in Ireland, Portugal, and Greece.

Table 8
Selected CDS Spreads
basis points, 5-year maturities

	Dec 31, 2011	Peak	(Date)	April 29, 2011
Abu Dhabi	94	119	(3/15)	94
Qatar	88	120	(3/17)	94
Saudi Arabia	75	143	(2/21)	111
Tunisia	120	217	(1/31)	170
Morocco	126	215	(1/31)	169
Bahrain	186	359	(3/15)	266
Lebanon	305	396	(1/31)	361
Egypt	243	450	(1/28)	351
Dubai	415	460	(2/28)	350
Ireland	609	674	(1/10)	661
Portugal	501	681	(4/26)	649
Greece	1010	1356	(4/26)	1300

Source: Bloomberg

WEAK EQUITY MARKETS, NO PRESSURE ON PEG

The equity markets in the region were hit hard by the Arab unrest, particularly in the first half of March of this year. While rebounding since then, the weighted average Arab world stock index remains below its level as of end-2010, and well below other emerging markets (Chart 4). The rally since mid-March has been driven partly by government purchases of shares, particularly in Saudi Arabia, and increasing confidence following the announcement of additional spending packages. Saudi Arabia's and Dubai's stock markets outperformed other Arab markets since the beginning of the year, rising by 4% and 2%, respectively.

We do not expect any pressures on the GCC pegged exchange rates. Forward exchange rate premia have been very small on the Saudi riyal, the Emirates' riyal, and the Kuwaiti dinar (Chart 5). They point to no change for the local currencies. The flexibility of labor markets, prices, and wages—due to a flexible supply of expatriate workers—ensures that any potential misalignment is addressed through price or labor force adjustments. In the GCC region, the latter adjustment is affected by the officially regulated immigration channels, rather than changes in the employment of nationals.

Chart 4
Arab World Stock Market Performance
Dow Jones indices, rebased end-2010=100

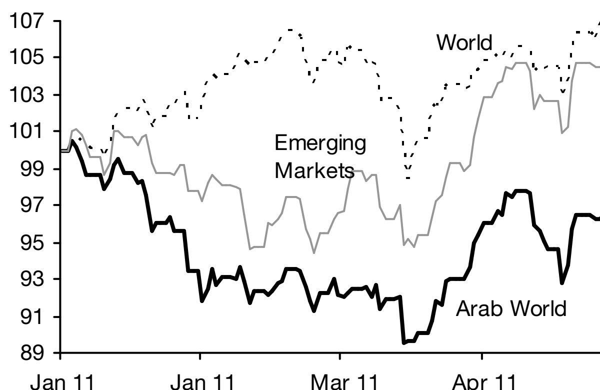
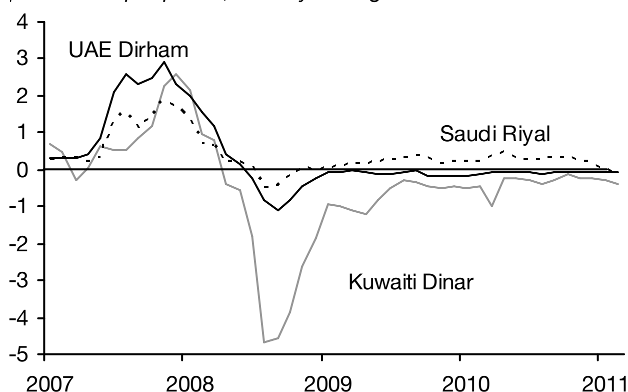


Chart 5
GCC: Currencies' Forward Premium Spreads
percent of spot prices, monthly averages



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WEAK GOVERNANCE, NEED FOR INCLUSIVE HIGH GROWTH TO REDUCE UNEMPLOYEMENT

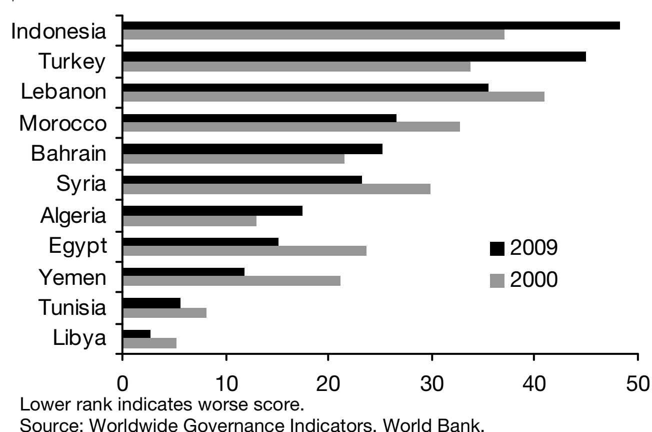
Arab governments score lower on governance indicators than other countries with comparable income levels. On voice and accountability, for example, the Arab world scores very poorly (Chart 6). Over the past decade these scores have deteriorated in most Arab countries, while improving in other comparable emerging economies, such as Indonesia and Turkey. Poor governance in the Arab world has adversely affected the business climate and hampered growth through its detrimental effect on capital accumulation and productivity.

The Arab world has the highest unemployment among developing regions; the highest jobless rates among youth; and the lowest economic participation rate among women (Table 9). Although economic growth has picked up since 2002, the longer–term growth record has been weak. Between 1980 and 2010, annual real per capita GDP growth was less than 1%, well below the average per capita annual growth of 4.5% in South and East Asia. Given the Arab world's relatively strong labor force growth, an average annual growth of 3.3% in the past three decades was not sufficient to prevent a sustained rise in unemployment. Furthermore, because of corruption and, more generally, weak institutions, the benefits of growth were poorly distributed within society. Without broad-based or inclusive growth, Arab countries will continue to face social tensions.

Meeting the employment challenge will require the transformation of the region's societies and economic structures. Most countries in the region prefer a stronger role for the state rather than the market in managing the economy. The public sector has essentially played the role of employer of last resort in several countries. The region lacks vibrant manufacturing and service sectors that can provide adequate, quality jobs to new entrants to the labor force (Chart 7).

Private investment averages less than 15% of GDP in the region, compared to more than 20% in other regions. The government's dominant role in the economy has tended to undermine productive private sector activities. Arab countries can put their economies on a higher growth path by rationalizing the role of government and improving institutional quality.

Chart 6
Voice and Accountability in the Arab World
percentile rank



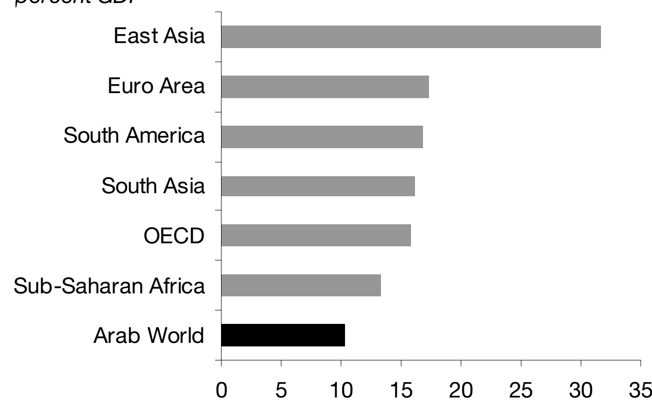
Lower rank indicates worse score.
Source: Worldwide Governance Indicators, World Bank.

Table 9
Growth, Labor Force, and Unemployment (%)

	Real GDP Growth 1980-2010	Labor Force Growth 1980-2010	Participation Rate 2009	Unemployment Overall 2009	Unemployment Youth 2009
Arab World	**3.2**	**3.3**	**50.8**	**11.5**	**25.2**
o/w: Egypt	4.6	3.4	50.1	11.5	26.3
Algeria	2.7	2.9	56.4	10.0	21.5
Morocco	3.7	3.2	53.2	9.1	24.9
Tunisia	4.1	3.0	50.5	13.3	28.7
Saudi A.	2.4	3.5	48.4	10.2	23.2
Latin America	3.1	2.3	65.6	7.7	15.7
South Asia	6.4	2.1	69.5	5.2	13.9
East Asia	6.7	1.5	73.2	4.4	8.9

Source: IIF Calculations, World Bank, and ILO.

Chart 7
Manufacturing, Value Added
percent GDP



Source: World Bank Human Development Indicators.

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SAUDI ARABIA: RESILIENT TO REGIONAL UNREST

Saudi Arabia has so far been spared the upheavals taking place in the region. King Abdullah is popular, but calls for reform could intensify in the medium to long term. The Kingdom does, however, have massive financial resources to meet social needs. The Saudi regime is well-entrenched with a well trained and equipped army and an effective internal security establishment. King Abdullah has voiced a commitment to reform, but large uncertainties remain.

We have revised our real GDP growth forecast for 2011 up from 3.5% before the regional crisis to 5.3% now, due mainly to higher crude oil production and a substantial increase in government spending. Nonhydrocarbon real GDP growth is projected at 5.1% for this year, driven mainly by a large increase in government consumption and investment, at around 5.8% growth in real terms (Table 10). We expect the 12-month inflation rate to rise from 4.7% in March 2011 to 7.5% by end-2011 (an average inflation rate of 5.7% in 2011 and 6.5% in 2012), due to stronger domestic demand and higher global commodity prices. The inflationary impact of the new government spending could be manageable if the productive capacity of the economy, particularly the prospects for the supply of housing, improves. The external current account balance will remain in a large surplus of 19.8% of GDP in 2011 and 14.2% of GDP in 2012.

Substantial increases in government spending, largely in the form of new social benefits to Saudi nationals, should further buffer the Kingdom against potential unrest in the short term. Table 11 lists the measures that were announced by King Abdullah on February 24 and March 18. The total value of these supplementary spending packages is estimated at SR467 billion, equivalent to 27% of 2010 GDP. The largest component of the new spending is SR250 billion for the construction of 500,000 public housing units, which, for purposes of this analysis, we assume will be spread over five years. The fiscal balance will remain in a large surplus of 12.7% of GDP in 2011, under the IIF assumption of an average oil price of $115 per barrel for Brent, or $113 per barrel for Saudi crude (Table 12). The sharp increase in government revenue from oil due to higher oil prices, and an expected 5% increase in export volumes, will more than offset the substantial 31% increase in government spending.

Table 10
Saudi Arabia: Growth, Inflation, and Current Account

	2008	2009	2010e	2011f	2012f
Nominal GDP, $ billion	473.0	372.8	436.6	581.7	599.0
Population, million	25.3	25.6	26.6	27.2	27.9
Real GDP, % change	4.2	0.2	3.5	5.3	3.8
Hydrocarbon	4.2	-7.5	2.2	6.0	2.5
Nonhydrocarbon	4.3	3.4	4.0	5.1	4.4
Private	4.6	2.8	4.1	4.7	4.5
Government	3.7	5.0	3.9	5.8	4.3
Consumer Prices, avg, %	9.9	5.1	5.3	5.7	6.5
Consumer Prices, eop, %	9.0	4.2	5.7	7.5	4.4
Current Acct. Bal., % GDP	28.6	5.6	8.9	19.8	14.2
Crude oil production, mbd	9.1	8.2	8.4	8.9	9.1

e = estimate; f = IIF forecast

Table 11
Saudi Arabia: New Government Spending Measures
SR billion

	February 24, 2011 Package	
Real Estate & Housing	Housing loans	40.0
	Support for General Housing Authority	15.0
Saudi Credit Bank	Capital increase	20.0
	Conversion of deposits to equity	10.0
Social Security	Increase in family dependents	1.0
	More support for utilities & schools	3.5
	Care services	1.2
Education	Financial support for low-inc. students	5.5
Public Sector Wages	15% cost of living allowance fixed*	0
Social Clubs	Literary, sports, and other	2.2
Sub-Total		**98.4**
	March 18, 2011 Package	
Real Estate & Housing	Construction of 500,000 housing units	250.0
	Increase in maximum loan amount	30.0
Social Security	Unemployment benefits (start Nov'11)	10.0
Education	2-month bonus student allowance	1.0
Wages	Min. monthly wage raised to $800	7.6
	2-month bonus for all public workers	35.0
Reduce Corruption	Creation of National Commission to Fight Corruption	1.0
Health	Building and expansion of hospitals	16.0
	Financing of private hospitals	2.0
Defense	60,000 new military jobs	15.0
Religion	Mosques and religious institutions	1.4
Sub-Total		**369.0**
GRAND TOTAL		**467.4**

* No additional cost to budget, since benefits and allowances will be replaced by a permanent increase in base salary.

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Saudi Arabia

One important implication of the two supplementary spending packages is that government spending has shifted to a higher path for the coming years. A significant portion of the increase in spending this year is likely to be permanent and difficult to reverse in the coming years. Evidence from many countries shows that once such benefits are in the budget, they could be hard to withdraw without facing strong resistance.
We estimate that the breakeven price of Saudi oil that balances the budget will jump from $68 per barrel in 2010 to $85 per barrel in 2011, and then continue rising, but at a slower pace to $110 per barrel by 2015 (Chart 8). Government spending will also jump from 79% of nonoil GDP in 2010 to 94% in 2011, and then gradually fall to 86% by 2015, which is still higher than the 82% recorded in 2009 (Chart 9).

While the current account surplus is projected at $114 billion in 2011, the foreign assets managed by the Saudi Arabian Monetary Agency (SAMA) are projected to increase by a smaller amount (perhaps $70 billion) to $527 billion by end-2011. The capital and financial account deficit in 2011 is projected to widen due partly to larger capital outflows for the purchase of assets abroad. There have been some signs that individual GCC investors have become somewhat concerned about the upheavals in the region.

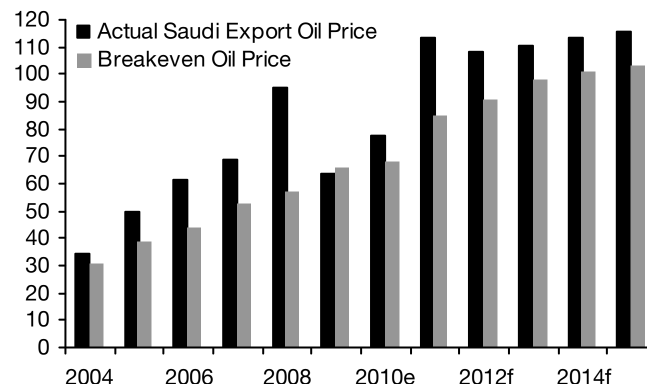
There has been significant improvement in the credit conditions. The year-on-year (yoy) growth in credit to the private sector accelerated from 2.7% in March 2010 to 6.5% in March 2011. Broad money (which includes currency outside banks, demand deposits, and time and savings deposits) growth also accelerated, rising by 14.5% (yoy) in March 2011, due mainly to the sharp increase in demand deposits in banks, following the payment of the two-month salary bonus for public sector workers. A large number of private sector companies have also granted salary bonuses to their employees. The ratio of demand deposits in total deposits has risen steadily from 40% in early 2009 to 55% in March 2010. The sharp increase in deposits led to a further decline in the loan-to-deposit ratio of 76.5%, lowest since 2004. SAMA may need to mop up the excess liquidity in banks, particularly when stronger domestic demand starts to contribute to inflationary pressures. Beyond 2011, the expected increase in domestic interest rates, with the unwinding of support from the United States, should help contain inflation.

Table 12
Saudi Arabia: Fiscal Accounts of the Central Government

	2008	2009	2010e	2011f	2012f
Revenue (SR billion)	1100	521	747	1102	1077
Oil	983	445	661	1005	967
Nonoil	117	75	86	97	110
Expenditure (SR billion)	520	588	629	826	878
Current Expenditure	389	417	440	503	521
Capital Expenditure	131	171	189	323	357
Overall Balance (SR billion)	580	-68	118	276	199
Overall Balance (% GDP)	32.7	-4.8	7.2	12.7	8.9
Expenditure (% change)	11.5	13.1	7.0	31.3	6.3
Expenditure (% nonoil GDP)	75.4	81.1	79.2	93.6	89.4
Saudi Price of Oil ($/barrel)	95	60	78	113	108

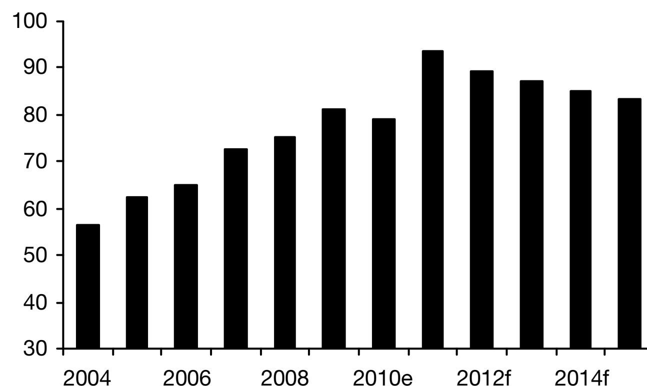
e = IIF estimate; f = IIF forecast

Chart 8
Saudi Arabia: Actual and Breakeven Oil Prices
$ per barrel



e = IIF estimate; f = IIF forecast

Chart 9
Saudi Arabia: Government Spending
percent of nonhydrocarbon GDP



e = estimate; f = IIF forecast

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UAE: SAFE HAVEN IN THE ARAB WORLD

The UAE has been spared the political turmoil in the Arab world. The economic and social factors that have contributed to the unrest in other parts of the region are not significant in the UAE. The country's small native population of less than one million (more than 85% of the labor force are expatriates) is amply provided for. The high standard of living and relatively open and tolerant society are important factors reinforcing social stability. Dubai, with the best infrastructure in the region, is viewed as a relatively safe haven for business. Trade, hospitality, and finance have begun to recover significantly in Dubai, offsetting further contraction in the real estate sector. Abu Dhabi's five-year CDS spreads, which measures the cost of insuring against a sovereign default, stood at 94 bps as of April 29, the lowest in the region. Dubai's CDS spread, while still high, has declined from 415 bps at end-2010 to 350 bps as of April 29, 2011 (Table 13).

We estimate that the UAE economy registered a modest recovery in 2010 with real GDP growth of 2.7%, following a contraction of 3.0% in 2009. The recovery in 2010 was driven by an increase in oil production and high spending on infrastructure in Abu Dhabi, while in Dubai growth was driven by a pickup in trade, transportation, logistics industries, and tourism. The turmoil in the Arab world could indirectly boost the Emirates' economy through the following channels: (i) higher production of crude oil in Abu Dhabi; (ii) a spike in oil prices and hence revenues (oil prices are assumed to rise from an average of $80 per barrel in 2010 to $115 per barrel in 2011); and (iii) a diversion to the UAE of some of the regional trade, transportation, tourism, and possibly finance.

Consequently, growth is projected to accelerate from 2.7% in 2010 to 3.8% in 2011 and to 4.0% in 2012 (Table 14). Hydrocarbon real GDP is expected to grow at 4.5%, driven by the increase in production of crude oil. Nonhydrocarbon real GDP will accelerate from an estimate of 2.6% in 2010 to 3.6% in 2011. In Abu Dhabi, nonhydrocarbon growth will be supported by high public spending on infrastructure, including through government-related entities (GREs). Inflation is expected to remain subdued, rising from 0.6% in 2010 to 1.9% in 2011, the lowest among the GCC countries. The further small decline in rents in the UAE as a whole will help to offset the significant rise in the price of food and other items in the CPI basket (Charts 10 & 11).

Table 13
Selected CDS Spreads
basis points, 5-year maturities

	Dec 31, 2011	Peak	(Date)	Apr 29, 2011
Abu Dhabi	**94**	**119**	**(3/15)**	**94**
Qatar	88	120	(3/17)	94
Saudi Arabia	75	143	(2/21)	111
Tunisia	120	217	(1/31)	170
Bahrain	186	359	(3/15)	266
Lebanon	305	396	(1/31)	361
Egypt	243	450	(1/28)	351
Dubai	**415**	**460**	**(2/28)**	**350**
Ireland	609	674	(1/10)	661
Portugal	501	681	(4/26)	649
Greece	1010	1356	(4/26)	1300

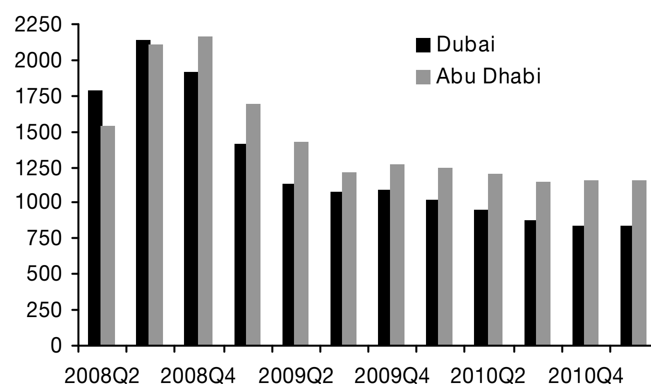
Source: Bloomberg.

Table 14
UAE: Selected Macroeconomic Indicators

	2008	2009	2010e	2011f	2012f
Nominal GDP, $ billion	261.4	230.1	251.2	305.3	321.9
Real GDP, % change	5.4	-3.0	2.7	3.8	4.0
Hydrocarbon	2.4	-8.5	3.2	4.5	3.7
Nonhydrocarbon	6.3	-1.3	2.6	3.6	4.1
Abu Dhabi	7.0	2.6	3.5	3.7	4.2
Dubai	5.7	-4.5	1.7	3.5	4.0
CPI Inflation Rate, avg., %	12.3	-0.7	0.6	1.9	3.3
Bank Lending, % change	45.0	2.4	1.3	5.0	8.0
Deposits, % change	21.0	6.5	6.8	12.0	14.0
Fiscal Balance, % GDP	12.3	-10.5	-0.9	7.1	5.6

e = IIF estimate; f = IIF forecast

Chart 10
UAE: Residential Prices
AED/square foot, quarterly data



Source: National Bank of Abu Dhabi.

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UAE

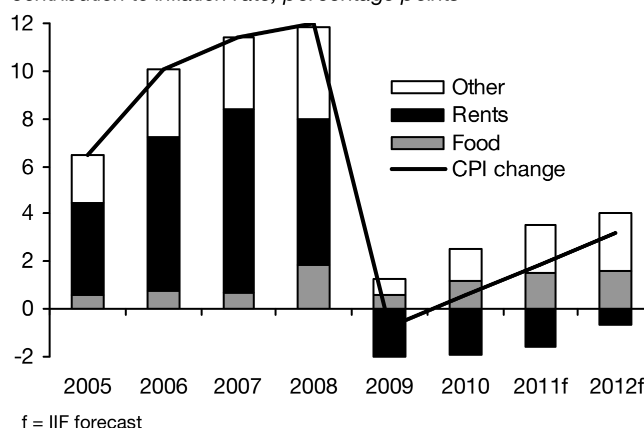
The current upheaval in the region may also have benefited the banking system in the UAE because of some diversion of capital from troubled countries. Total deposits (including resident, nonresident, and government) have risen significantly in recent months, up by 14.3% in the year to March 2011. More than half of the increase was in time and savings deposits in local and foreign currencies. In our view, this increase in longer-term deposits reflects improved confidence in the UAE economy following Dubai World's (DW) successful debt restructuring and the subsequent bond issues by the government of Dubai and a number of GREs.

We expect credit growth to improve gradually in 2011 and 2012, supported by strong growth in deposits, lower interest rates in real terms, improvement in the liquidity of banks, and a pickup in domestic demand. We therefore expect the 12-month credit growth to accelerate from 2.5% in March 2011 to about 6% by end-2011 and 8% at end-2012 (Chart 12).

The UAE banks remain well capitalized and profitable. The combined provisions of banks more than doubled, rising from the equivalent of $6.8 billion at end-2008 to $16.2 billion at end-March 2011. The nonperforming loans (NPLs) to total loans for all UAE banks rose from 4.3% at end-2009 to an estimate of 6.0% at end-2010, partly due to a change in the reclassification of NPLs from 6 months to 3 months. Provisions now cover about 95% of NPLs. The liquidity of the banking system has also improved, as indicated by the steady decline in the loan-to-deposit ratio, from 108% at end-2008 to 95% at end-March 2011 (Table 15). Most banks have reported higher profits during the first quarter of this year, as compared with the same quarter of the previous year.

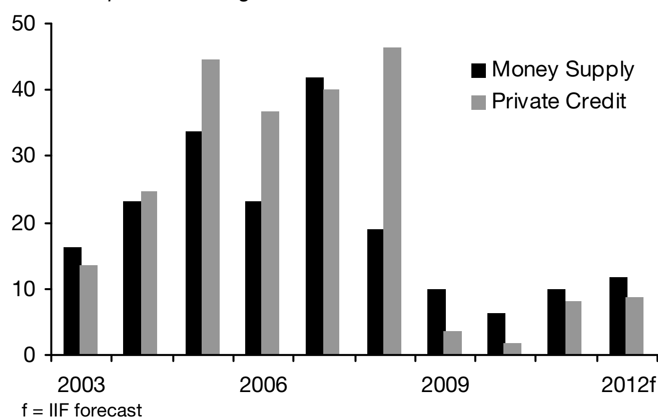
The UAE's current account was in a surplus of $22 billion in 2010 (8.6% of GDP) due to an increase in oil exports resulting from higher oil prices and a modest increase in production. With oil prices at $115 per barrel in 2011, that surplus is set to widen to $43 billion, 14.1% of GDP (Chart 13). In the absence of detailed official data, our estimates of the consolidated fiscal data (including Abu Dhabi Investment Authority's (ADIA) investment income and Abu Dhabi National Oil Company's profit transfers) show a small deficit of less than 1% of GDP in 2010, as compared to a large deficit of 10.5% of GDP in 2009. This improvement in fiscal performance is explained by a sharp increase in Abu Dhabi's government revenue from oil, and, on the expenditure side, a decrease in lending and equity outlays

Chart 11
UAE: Components of Inflation
contribution to inflation rate, percentage points



f = IIF forecast

Chart 12
UAE: Money Supply and Credit Growth
12-month percent change



f = IIF forecast

Table 15
UAE: Financial Sector Soundness Indicators*
percent

	2007	2008	2009	2010	March 2011
Capital to Risk-Weighted Assets	14.0	13.3	19.0	20.8	20.7
NPLs/Total Loans	2.9	2.5	4.8	6.0	6.0
Provisions to NPLs	100	101	89	92	95
Return on Assets	2.0	1.8	1.3	1.4	...
Loans to Deposits	97.5	107.7	103.6	97.2	94.8

*IIF estimates and forecasts based on partial information from the central bank and financial statements of individual banks.

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UAE

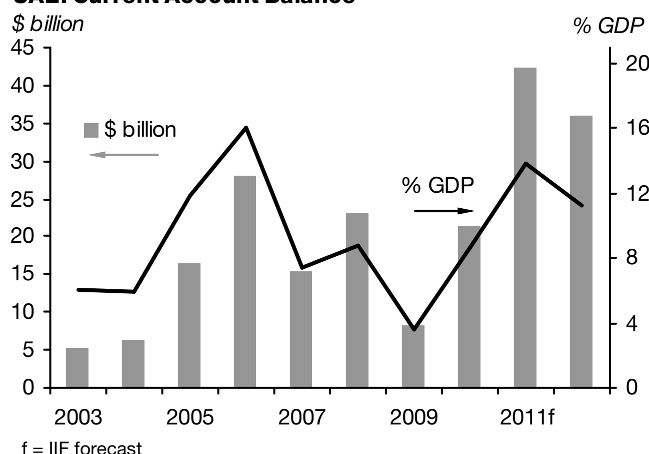
as compared with 2009 when the Abu Dhabi government provided substantial equity and loans (equivalent to 6% of GDP) to GREs. For 2011, we forecast a consolidated fiscal surplus of 7.6% of GDP, despite the projected small deficits of the federal government and Dubai's budgets for 2011 (Chart 14). This surplus is explained by the large increase in the government of Abu Dhabi's revenue from oil, which is expected to more than offset our projected increase of 8% in consolidated spending. Also, there are indications that fiscal consolidation in Dubai (mostly cuts in government spending) that started in 2010 will continue in 2011 as the Emirate continues to shore up its fiscal health.

The external debt of the UAE as a whole is estimated at $157 billion, of which about $90 billion is owed by Dubai. It should be noted that Dubai's total debt of $120 billion, mentioned in the previous section, also includes domestic debt vis-à-vis local banks. We estimate total gross foreign assets of the UAE at about $449 billion at end-2010. These include foreign assets held at the central bank of the UAE ($43 billion), commercial banks' foreign assets ($64 billion), and foreign assets of ADIA ($330 billion). These would result in an overall net external asset position of $292 billion, equivalent to 116% of 2010 GDP (Table 16). The net external position of the UAE is projected to improve further given the large fiscal and current account surpluses expected in 2011.

Dubai's debt crisis was a sort of wake-up call for the UAE economy. Dubai's rapid development model, which depended on leverage, is gradually changing. While DW successfully restructured its debt, worries persist about the debt overhang in Dubai. Other GREs are also undergoing debt restructuring, including Dubai Holding. The restructuring terms granted to Dubai give it enough time to improve the cash flows of the GREs under hopefully better market conditions.

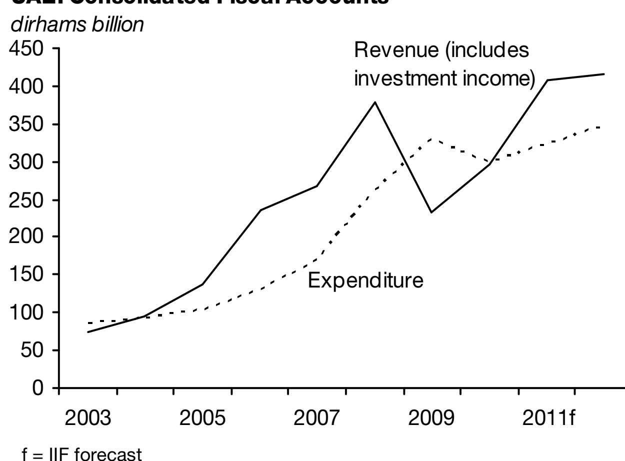
Dubai has regained market access, but the cost of borrowing remains high, reflecting the rollover needs of the total of $31 billion falling due in 2011/12, as well as concerns about the solvency of restructured GREs. Progress in structural reforms over the next few years (mostly in the legal and regulatory environment), the strengthening of federal institutions, and the enhancement of transparency and governance in the corporate sector could accelerate the pace of economic growth to over 4% in the medium term.

Chart 13
UAE: Current Account Balance



f = IIF forecast

Chart 14
UAE: Consolidated Fiscal Accounts



f = IIF forecast

Table 16
UAE Net External Assets

	2008	2009	2010e	2011f
Net External Assets, $ billion	246	246	292	344
% GDP	94	107	116	112
External Debt, $ billion	151	144	157	161
Foreign Assets, $ billion	397	390	449	505
Central Bank	32	36	43	58
Commercial Banks	55	57	64	66
Nonbanks	30	34	37	38
ADIA*	280	263	305	342

e = estimate; f = IIF forecast
*Revised time series based on revised larger consolidated government expenditures. These revisions resulted in smaller fiscal surpluses during the boom years, and, therefore, small increases in ADIA's foreign assets.

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QATAR: HIGHER GAS PRODUCTION ALLOWS LARGE SPENDING INCREASE AND DOUBLE-DIGIT GROWTH

Qatar has been buffered from the adverse impacts of the turmoil in the Arab world. Its small native population of about 0.3 million out of a total of 1.8 million (more than 90% of the labor force are expatriates) has benefited from the country's prosperity. The IIF estimates real GDP growth in 2010 to have been 18.5%, with real hydrocarbon GDP growth of 27.9% and real nonhydrocarbon growth of 9.2% (Table 17). Growth is expected at 18% in 2011, driven by further expansion in natural gas production. Beyond 2011, growth is projected to decelerate to 6% in 2012 and to 4% in 2013 and onwards, with growth tapering off in the hydrocarbon sector (Chart 15).

The 12% decrease in rents in 2010, due to a continued excess supply of housing, has more than offset the rise in food and other components of the CPI, resulting in average headline CPI deflation of 2.4%. The year-on-year inflation rate was 1.7% in March 2011 (an increase of 3.2% in food; a decrease of 10.6% in rents). Looking ahead, a continued, yet smaller decline in rents will shift the CPI deflation of last year to a low average inflation rate of 3.0% in 2011.

The fiscal and external current account balances will remain in surplus in 2011, at 10.6% of GDP and 26.4% of GDP, respectively. The sharp increase in government revenue from hydrocarbons, due to higher oil prices and an expected 30% increase in exports of LNG, will more than offset the substantial increase in government spending.

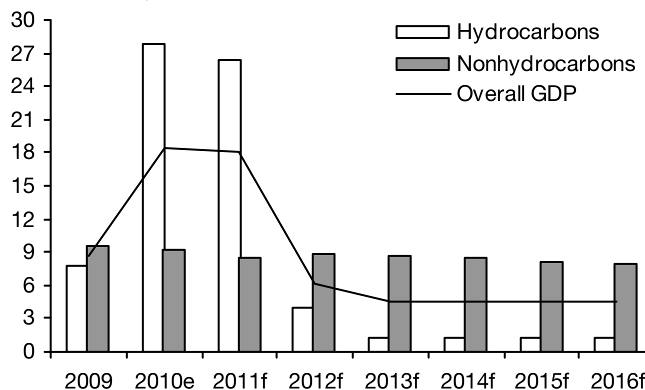
External debt more than doubled in the past three years to $104 billion at end-2010, equivalent to 81% of GDP, and is projected to fall to 60% by end-2012 (Chart 16). A large portion of public enterprises' external debt reflects hydrocarbon investment requirements. Given the projected large twin surpluses, Qatar's total foreign assets are projected to rise from $133 billion in 2010 to $186 billion by end-2012. The main downside risks to the outlook remain low but their impact could be considerable, as Qatar's prosperity depends critically on gas and oil production for export. A sudden collapse, especially a drop by more than half, in LNG prices due to technological or other reasons (an unlikely scenario), would sharply lower hydrocarbon revenues and shift the external current account and fiscal balances to large deficits, depending on the government expenditure profile.

Table 17
Qatar: Selected Economic and Financial Indicators

	2008	2009	2010e	2011f	2012f
Nominal GDP, $ billion	110.7	98.3	128.6	183.5	193.0
Real GDP (% change)	25.4	8.6	18.5	18.1	6.1
Hydrocarbon GDP	23.1	7.7	27.9	26.3	3.9
Nonhydrocarbon GDP	27.8	9.6	9.2	8.5	8.9
CPI Inflation, avg., % change	15.2	-4.9	-2.4	3.0	4.2
Fiscal Balance, % GDP	10.6	14.1	12.0	10.6	6.9
Current Account Bal., % GDP	29.9	11.1	16.8	26.4	19.4
Gross Foreign Assets, $ billion	90.9	106.9	130.6	156.4	175.7
Gross External Debt, $ billion	57.1	83.8	103.9	109.4	114.9
Crude Oil Production, mbd	0.79	0.81	0.82	0.83	0.83
LNG Production, mboed	1.39	1.62	2.20	2.93	3.08

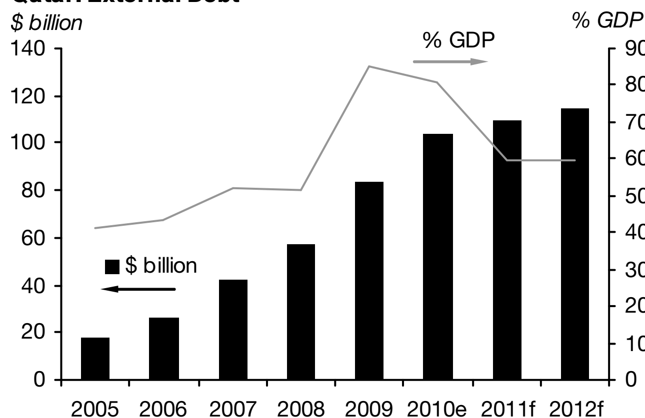
e = IIF estimate; f = IIF forecast

Chart 15
Qatar: Real GDP Growth
percent change



e = IIF estimate; f = IIF forecast

Chart 16
Qatar: External Debt
$ billion *% GDP*



e = IIF estimate; f = IIF forecast

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Kuwait

KUWAIT: GROWTH DRIVEN BY PUBLIC SPENDING

The turmoil in the Arab world has had little direct impact on Kuwait, partly due to a prevailing political consensus and a tradition of representative politics. The political structure in Kuwait consists of an elected parliament with legislative powers tasked with keeping the executive branch of government in check. This has eased the pressure for change that has built up in other Arab countries. Nevertheless, in response to the turmoil spreading in the region, the Kuwaiti authorities have done the following: (i) given a cash grant of $3500 to every Kuwaiti national (amounting to a total of about $4 billion, equivalent to 3% of GDP); (ii) raised salaries in the public sector by an average of $440 per month; (iii) reduced utilities rates; (iv) raised the retiree wage limit to qualify for social security benefits; and (v) granted free medical treatment and education to residents that are not citizens.

Growth is projected to accelerate from an estimate of 2% in 2010 to 4.4% in 2011, driven by expansion in crude oil production and a large increase in government spending (Table 18). The spike in global food and other commodity prices combined with the expansionary fiscal policy in Kuwait will raise inflationary pressures. Inflation is projected to rise from 4.1% in 2010 to an average of 6.2% in 2011.

Our estimates show that the supplementary public spending discussed above combined with the investment commitment in the context of the five-year development plan (KD 31 billion in 2010-2014, equivalent to 90% of 2010 GDP), will result in an increase in total government spending of 25% in the current fiscal year (Chart 17). Nonetheless, the fiscal surplus is projected to widen from 29% of GDP in 2010/11 to 31% of GDP in 2011/12, under the assumption of an average Brent oil price of $115 per barrel in 2011 and $110 per barrel in 2012.

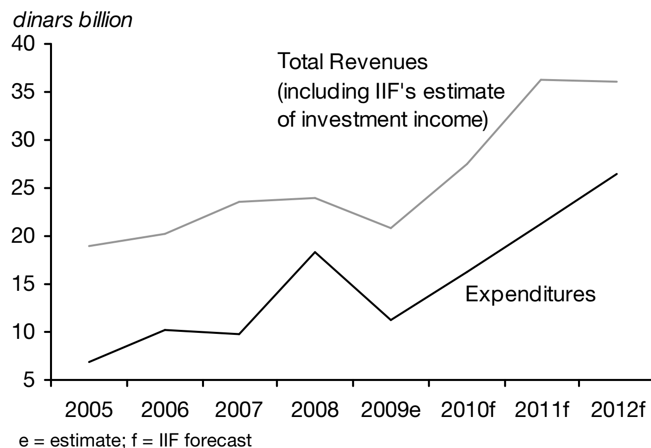
The breakeven price of oil that balances the Kuwaiti budget, while rising in recent years, is the lowest among Arab oil exporters, at around $40 per barrel for 2011 compared to $85 per barrel in Saudi Arabia (Chart 18). This is explained by the following two factors: (i) Kuwait has the highest production of crude oil per capita; and (ii) investment income on foreign assets (mostly on the country's well-established sovereign wealth fund) is high, estimated at 8% of GDP in fiscal year 2010/11.

Table 18
Kuwait: Selected Macroeconomic Indicators

	2008	2009	2010e	2011f	2012f
Nominal GDP, $ billion	148.8	109.5	127.4	167.4	171.0
Real GDP, % change	5.0	-5.1	2.0	4.4	4.3
Hydrocarbon	4.4	-10.2	1.4	5.0	3.0
Nonhydrocarbon	5.4	-1.9	2.3	4.0	5.2
Inflation Rate, average, %	10.6	4.0	4.1	6.2	4.1
NPLs, % total loans	5.3	9.7	9.0	...	...
Current Acct Bal, % GDP	39.5	24.4	30.7	40.4	34.5
Fiscal Balance, % GDP*	15.2	29.4	28.9	31.2	26.6
Foreign Assets, $ billion	331.2	362.0	387.9	422.0	445.9
Foreign Liabilities, $ billion	61.1	57.5	60.4	63.4	66.6

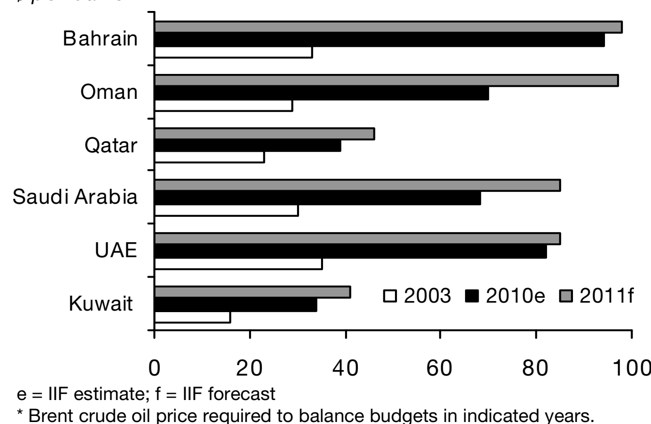
e = estimate; f = IIF forecast
* Fiscal Years ending March 31 of the following year.

Chart 17
Kuwait: Fiscal Account
dinars billion



e = estimate; f = IIF forecast

Chart 18
GCC: Breakeven Oil Prices Rise Sharply*
$ per barrel



e = IIF estimate; f = IIF forecast
* Brent crude oil price required to balance budgets in indicated years.

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BAHRAIN: NO EARLY RESOLUTION TO THE IMPASSE

After several weeks of mostly peaceful protests, which resulted in a stalemate in Bahrain, the government implemented a new military crackdown to quell demonstrations in late March. Although some economic concessions were made, negotiations between the ruling elite and opposition groups never got off the ground, reflecting stiff preconditions laid down by the protesters, and a lack of consensus on measures in the government. No early resolution to the impasse seems likely.

The tourism and business conference sectors (with knock-on effects in hotels and restaurants) have been hit hard, with the cancellation of the Formula 1 Grand Prix having a major impact. Retail trade has also been adversely affected, and the banking sector, which had recovered well from the global financial crisis, will suffer tangentially. Other key sectors, such as oil and gas and manufacturing, are unlikely to be impacted significantly. As a result, we think that more than 2.0% will be shaved off growth in Bahrain this year, with considerable downside risk if the situation goes unresolved for an extended period. Our forecasted growth of 2.9% for 2011 would be the weakest since the mid-1990s (Table 19).

The surge in oil prices is providing some fiscal relief. Although spending will be higher than originally budgeted due to increased allocations to social benefits and low-cost housing, this will be more than offset by a sharp increase in oil revenue. We therefore expect the budget to remain in surplus at around 1% of GDP (Chart 19). However, Bahrain's fiscal vulnerability has increased, as the breakeven oil price that balances the budget has now moved above $100 per barrel. The tripling of oil production at the onshore Awali oil field over the next seven years will help to alleviate budget pressures, even though not all the extra revenue will accrue to the government.

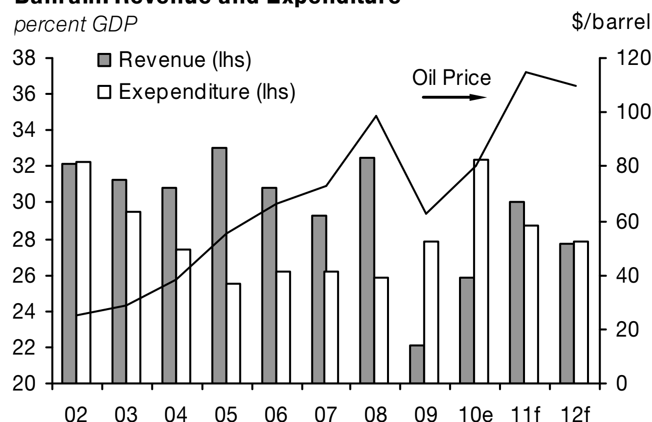
High oil prices will also keep the current account in large surplus this year and next. The trade surplus is forecast to reach a record $5.5 billion in 2011, which will easily offset a larger deficit in services, income and transfers due to a sharp drop in tourism and travel receipts. As a result, we expect the current account surplus to widen to about 11% of GDP this year and to remain in double digits in 2012 (Chart 20). This will help counterbalance any capital flight this year and underpin the exchange rate.

Table 19
Bahrain: Selected Macroeconomic Indicators

	2008	2009	2010e	2011f	2012f
Nominal GDP, $ billion	21.9	20.6	22.9	26.1	27.7
Real GDP, % change	6.3	3.1	4.5	2.9	5.2
Hydrocarbon	0.4	-0.3	1.5	2.5	3.5
Nonhydrocarbon	7.0	3.4	4.8	2.9	5.4
Inflation Rate, average, %	3.5	2.8	1.9	2.4	2.2
Current Acct Bal, % GDP	10.3	2.7	3.4	11.0	13.2
Fiscal Balance, % GDP	6.6	-5.8	-6.6	1.0	1.2
Official Reserves, $ billion	3.94	3.80	5.14	5.00	5.60
Months of Imports	1.9	3.0	3.6	3.1	3.3

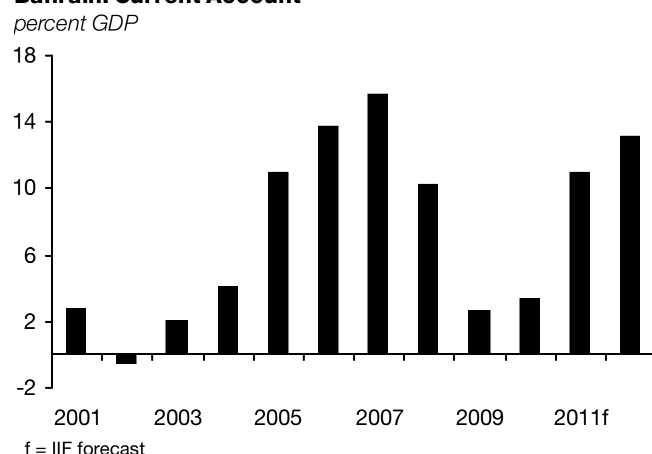
e = estimate; f = IIF forecast

Chart 19
Bahrain: Revenue and Expenditure
percent GDP



e = estimate; f = IIF forecast

Chart 20
Bahrain: Current Account
percent GDP



f = IIF forecast

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Oman

OMAN: BENEFITING FROM HIGHER OIL OUTPUT

Oman has also had protests, but they have been less intense than in other troubled countries, while political grievances have been addressed swiftly and more comprehensively. Economic measures to address social issues have been implemented, and the government has committed to creating 50,000 jobs (35,000 in the public sector and 15,000 in the private sector). The minimum wage was raised to RO 200 (about $520) per month, and anyone out of work but looking for a job (and registered with the Manpower Ministry) is to receive unemployment benefits of RO 150 per month.

The unrest is not likely to have had a significant impact on growth, which is forecast to be similar to last year at about 4.6% (Table 20). With no OPEC restrictions, crude oil output is projected to rise by 3.9% in 2011, and gas production by 12.0% as past investments in enhanced oil recovery continue to bear fruit (Chart 21). The nonhydrocarbon sector should also continue to recover from a downturn in 2009, with new capacity coming online in downstream gas industries. The tourism sector has been largely unaffected by the social unrest and looks set to perform well this year. The construction sector will be boosted by ongoing development and infrastructure projects.

High oil prices should ensure sizable budget and current account surpluses in 2011. Although extra spending has been authorized, which will boost both current and capital expenditures, the fiscal position remains strong and the budget surplus may exceed 10% of GDP this year. As a result, government debt should fall below 5% of GDP. The authorities will have plenty of scope to transfer funds to the State General Reserve Fund (SGRF) and other reserve accounts. Government debt remains relatively low (Chart 22).

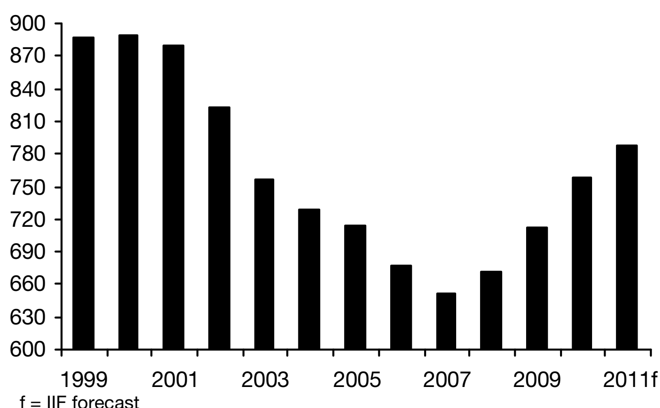
The surge in oil prices and increase in tourism will likely produce a record current account surplus of over 20% of GDP in 2011, resulting in a further increase in foreign exchange reserves to about $16 billion. This is sufficient to cover about six months' worth of imports. More buoyant domestic demand and higher food prices exerted upward pressure on inflation in the second half of last year and by December the 12-month rate had reached 4.2%. Since then, inflation has eased back and we do not expect it to become a policy issue this year.

Table 20
Oman: Selected Macroeconomic Indicators

	2008	2009	2010e	2011f	2012f
Nominal GDP, $ billion	60.6	46.9	57.2	74.8	77.0
Real GDP, % change	12.8	1.1	4.8	4.6	5.0
Hydrocarbon	6.2	4.9	6.7	5.0	2.0
Nonhydrocarbon	15.7	-0.3	4.0	4.5	6.3
Inflation Rate, average, %	12.4	3.5	3.3	3.7	3.4
Current Acct Bal, % GDP	8.3	-0.6	11.6	21.9	15.0
Fiscal Balance, % GDP	13.0	-3.1	3.2	11.9	6.3
Foreign Assets, $ billion	25.2	24.7	27.2	30.2	33.0
Foreign Liabilities, $ billion	12.3	11.6	14.4	12.7	13.3

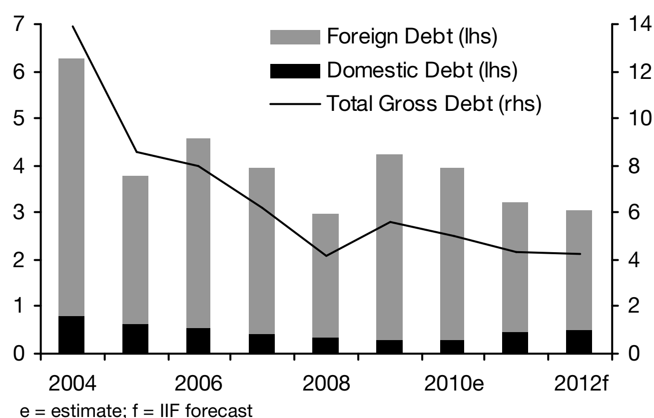
e = estimate; f = IIF forecast

Chart 21
Oman: Crude Oil Production
thousand barrels/day



f = IIF forecast

Chart 22
Oman: Government Debt
rials billion *percent GDP*



e = estimate; f = IIF forecast

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Egypt

EGYPT: MAJOR CHALLENGES AHEAD

The situation in Egypt has stabilized for now. The military council that took over power following the ousting of Hosni Mubarak in February recently announced that parliamentary elections will be held in September, and presidential elections will follow a few months later. Egypt faces many challenges in the post-Mubarak era, not least of which is developing an economic strategy that closes the gaping budget gap and tackles structural reforms while addressing the social and economic aspirations of its people.

The sharp drop in economic activity will hit output hard in the first half of 2011, dragging down growth for the financial year 2010/11 as a whole (note that Egyptian economic data are typically quoted on a financial year basis, which runs from July to June). Projections for calendar years show a contraction in output of 2.5% in 2011, and a growth of 4.2% in 2012. While the economy will contract in real terms, nominal GDP growth is projected to be close to 10% in calendar year 2011, reflecting the persistently high rate of inflation (11.5%). Most sectors should rebound in 2012, although tourism and related industries will likely be slower to recover. Furthermore, based on past experience in Egypt and other countries, it could be a while before foreign tourists feel safe to return, and so recovery in this sector is likely to be protracted (Table 21).

The disruption to exports and drop in tourist arrivals will widen the current account deficit in 2011. This, together with portfolio outflows and a reduction in foreign direct investment, will put increased pressure on the balance of payments. Prior to the crisis, the central bank had built up its official reserves and held sizable foreign exchange deposits in the banking system. It has managed the ensuing outflows reasonably well, avoiding major realignment of the exchange rates. However, official reserves have fallen by $6 billion to about $27 billion (Chart 23).

The budget deficit is likely to rise to about 10% of GDP in FY 2011/12, and the consolidation timetable will again slip, perhaps significantly (Table 22). Tax revenue will be adversely impacted and expenditure will likely be even higher than the previously anticipated overrun. Reforming and reducing subsidies through better targeting to needy people had been a key element of fiscal consolidation. Even before the crisis, subsidies were a large drain on the budget and were projected

Table 21
Egypt: Key Macroeconomic Variables

	2008/09	2009/10	2010/11f	2011/112f
Growth, % change*	4.7	5.3	1.5	2.3
Inflation, eop, %	10.0	10.7	11.8	9.2
Current Account, % GDP	-2.3	-2.0	-2.5	-2.4
Tourism Receipts, $ billion	10.5	11.6	8.5	10.0
FDI, $ billion	8.1	6.8	5.0	4.5
Portfolio Equity, net $ billion	-8.6	7.0	-5.1	1.9
Official Reserves, $ billion	29.4	32.8	26.9	28.5
Budget Balance, % GDP	-6.9	-8.1	-9.5	-10.0
Gross Public Debt, % GDP	73.0	73.1	74.5	76.9

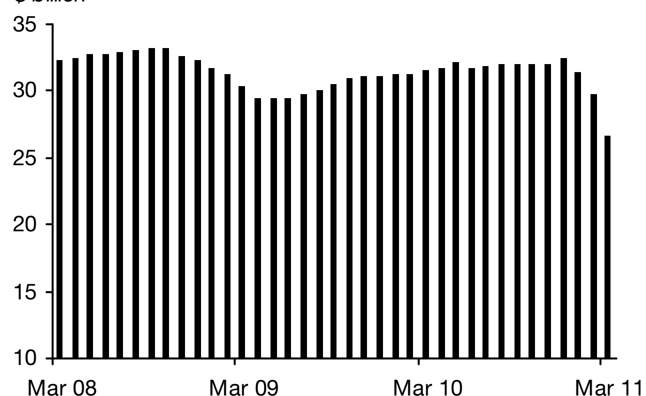
f = IIF forecast
* Fiscal year calculations. On a calendar year basis, real GDP growth in Egypt will decline by 2.5% in 2011 and recover to 4.2% in 2012.

Table 22
Egypt: Central Government Fiscal Operations
LE billion

	2008/09	2009/10	2010/11f	2011/12f
Total Revenues & Grants	283	268	276	312
o/w: Tax Revenues	163	171	191	210
Total Expenditures	354	366	405	463
o/w: Wages and Salaries	76	85	100	120
Interest Payments	53	72	88	100
Subsidies	94	94	110	125
Capital Expenditures	46	49	34	30
Fiscal Balance	-72	-98	-129	-152
(% GDP)	(-6.9)	(-8.1)	(-9.5)	(-10.0)

f = IIF forecast

Chart 23
Egypt: Foreign Exchange Reserves
$ billion



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Egypt

to rise to LE101 billion in FY 2010/11, accounting for 25.2% of total expenditure and equivalent to 7.3% of GDP. No budget for FY 2011/12 has been published yet, but the new Finance Minister, Samir Radwan, indicated that the deficit could widen to 9.5% of GDP. Our own projections suggest the deficit will be a bit larger at about 10%, with higher spending outweighing a modest pickup in revenue growth.

The higher level of spending on wages and salaries, locked in by measures implemented over the past couple of months, will have a major impact on expenditure next year. Subsidies, grants and social benefits, which together form the largest component of spending, will also rise sharply based on government promises to take care of the needs of the poorer segments of society. Social benefits will probably see the biggest increase. Interest payments will also increase, reflecting the rise in outstanding public debt as well as higher funding costs in the market. In an effort to contain the increase in total expenditure, the government may decide to scale back or slow down the implementation of development spending.

Deficit financing is mostly from domestic sources and should not pose an undue problem this year and next given the ample liquidity in the banking system. Direct borrowing from abroad to finance the deficit tends to be small. Heavy selling of Treasury bills (Chart 24) this year has pushed up yields, as reflected in higher funding costs. Large budget deficits will push up the government debt-to-GDP ratio, which had been declining steadily for a number of years. We expect general government debt as a percentage of GDP to rise to 75% by the end of FY 2010/11, up from 73% the previous year, and to reach nearly 77% in 2011/12 (Chart 25).

Risks are heavily skewed on the downside. Further deterioration due to a potential second wave of social upheaval, given high expectations and the difficulty of delivering results in the short term, cannot be ruled out. The political reform process may not be smooth and could drag on beyond 2011, slowing any economic recovery and further delaying investment decisions (Chart 26). Meanwhile, investigations into political corruption and the tangential impact on some private sector businesses will add to uncertainty. These downside risks to growth also have implications for the budget as weaker-than-anticipated economic activity would likely result in lower tax revenue and an even larger deficit than we are forecasting.

Chart 24
Egypt: Foreign Holdings of Treasury Bills
LE billion

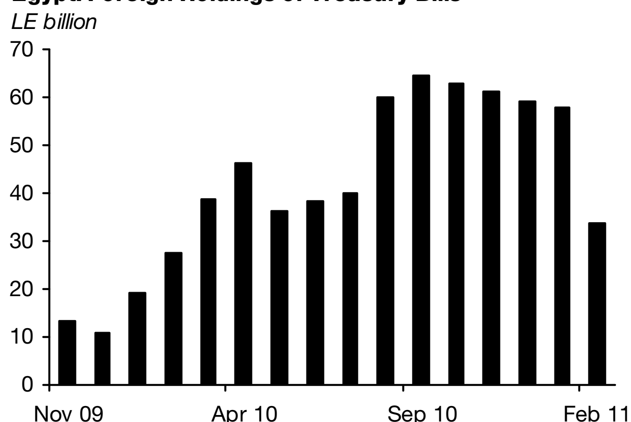
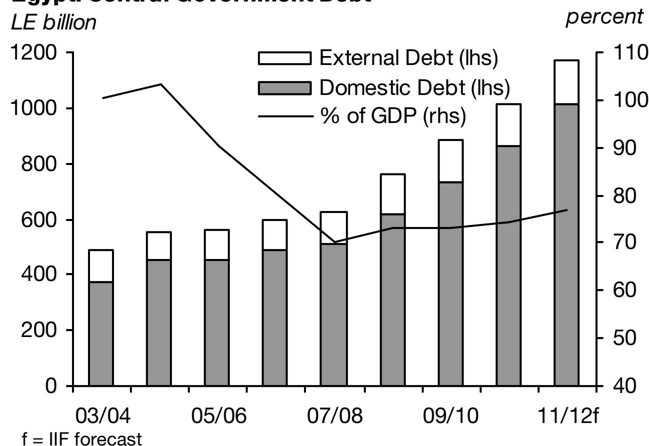
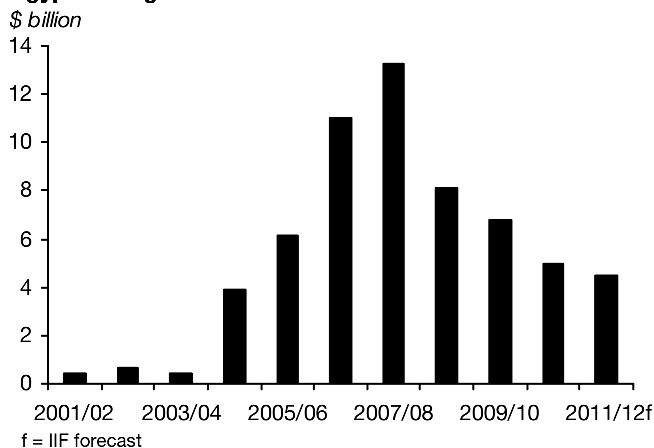


Chart 25
Egypt: Central Government Debt
LE billion *percent*



f = IIF forecast

Chart 26
Egypt: Foreign Direct Investment
$ billion



f = IIF forecast

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Tunisia

TUNISIA: SHORT-TERM CHALLENGES, LONG-TERM OPPORTUNITIES

Tunisia has entered a difficult transition phase toward a more open and democratic political system. Elections for a constitutional council are scheduled for July of this year, to be followed by presidential elections. Overall growth may contract this year before a strong rebound, assuming that all relevant institutional arrangements for a new political order are in place by the end of this year.

The disruption of economic activity resulting from the political turmoil will impact especially the first half of 2011, leading to a contraction of 1.5% in overall real GDP for 2011. Banks are likely to suffer from a significant increase in NPLs due to the failure of some large businesses owned by the family and close associates of the former president, who controlled a large share of the Tunisian economy. Several factories were set on fire, large numbers of employees were laid off, and exports of goods and services suffered significantly. The tourism industry, a large provider of jobs and a main source of foreign currency (equivalent to 6% of GDP), will remain under intense pressure for much of this year (Table 23).

The current account deficit is expected to widen significantly, as the slowdown in exports of goods and services more than offset the deceleration in import growth due to weak domestic demand. Weaker tax revenues resulting from a slowdown in economic activity, combined with pressures to increase government spending to create new jobs and to restore food and petroleum subsidies, will also widen the fiscal deficit from 1.4% of GDP in 2010 to 4.5% of GDP in 2011 (Chart 27).

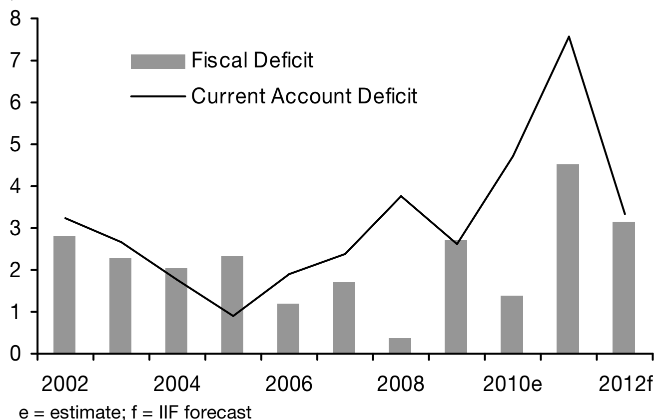
The external debt will remain manageable at 46% of GDP (Chart 28). The composition of the debt (mostly on concessional terms) and its size provide Tunisia the capacity to manage persistent but moderate deficits through 2015. The external debt falling due in 2011 (interest plus principal) is about $2.4 billion, equivalent to 11% of exports of goods and services, and $2.5 billion in 2012, equivalent to 10% of exports of goods and services. Tunisia's debt to BIS reporting banks has been declining in recent years to $3.9 billion as of end-September 2010 (equivalent to 9% of GDP, or 17% of exports of goods and services). Also, the level of official foreign exchange reserves, while declining, appears to be adequate at 180% of total short-term debt.

Table 23
Tunisia: Main Economic and Financial Indicators

	2008	2009	2010e	2011f	2012f
Nominal GDP, $ billion	42.4	40.9	41.5	40.1	47.8
Real GDP, % change	4.5	3.1	3.4	-1.5	5.2
Agriculture and Fishing	-0.6	6.0	-7.5	5.0	4.0
Nonagricultural	5.3	2.7	4.8	-2.2	5.3
CPI Inflation, avg., % change	5.0	3.7	4.5	4.2	3.2
Current Account Bal., % GDP	-3.8	-2.6	-4.7	-7.5	-3.3
Gross Official Reserves, $ billion	8.8	11.1	10.1	8.0	8.8
Months of Imports	3.6	5.6	4.3	3.3	3.3
Budget Balance, % GDP	-1.0	-3.0	-1.4	-4.5	-3.6
Unemployment Rate (%)	12.4	13.3	13.0	14.5	13.0

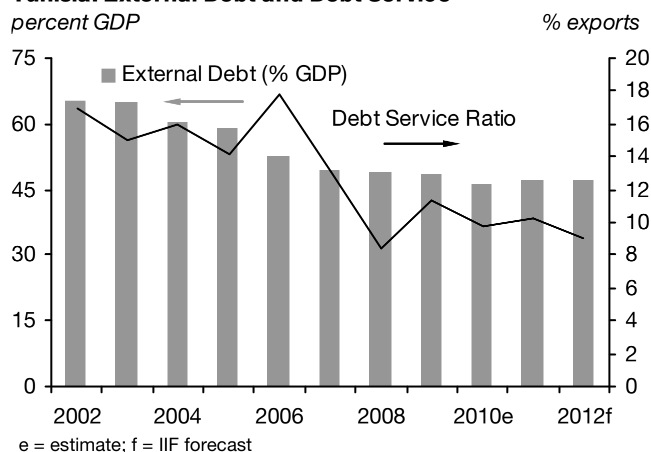
e = estimate; f = IIF forecast

Chart 27
Tunisia: Fiscal and Current Account Deficits
percent GDP



e = estimate; f = IIF forecast

Chart 28
Tunisia: External Debt and Debt Service
percent GDP *% exports*



e = estimate; f = IIF forecast

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Tunisia

The country faces a major challenge in reducing the chronically high unemployment rate, which is particularly acute among college and high school graduates. High labor force growth has caused the unemployment rate to remain roughly unchanged at around 13%, despite significant job creation growth of 2.0% per year over the past decade (Chart 29). The unemployment rate among graduates has increased steadily to 24% in 2010.

Beyond the immediate challenges of political and institutional transformation, Tunisia needs to diversify target markets and products. The country has managed to successfully break into light manufacturing since the mid-1970s, and this has helped to diversify its production base (away from oil) and to create medium- and low-skilled jobs in large numbers. In the past decade, however, a significant portion of new entrants into the labor market were university graduates, and the current production structure is not suitable for the skill set they offer. In this context, the country needs to shift from a low value-added and low-cost economic model to a higher value-added, knowledge-intensive economy in order to reduce unemployment, especially among the young and educated.

The current political and constitutional transformation needs to be accompanied by structural economic reforms to put the economy on a higher and sustainable growth path in order to reduce high unemployment. Economic output in Tunisia has to grow at least by 6-7% on a sustainable basis (growth has averaged only 4.7% from 1990-2010) in order to provide jobs for new entrants and to materially reduce the high unemployment rate to upper single-digit levels by 2015, and close to the average for emerging markets (6%) by 2020 (Chart 30). Higher and more inclusive growth requires higher investment and good governance, which could be achieved via improvement in the business environment, more efficient resource allocation, and reduced corruption.

Because of corruption and, more generally, weak institutions, the benefits of growth were poorly distributed within society in the last two decades. Like other countries in the region, Tunisia's population is young (Chart 31). The decline in population growth from 2.6% per year in the 1980s to 1.6% in the 1990s and to 1.2% in 2000-2010 will translate into lower labor force growth over the medium and long term.

Chart 29
Tunisia: Unemployment Rates
percent of labor force, latest available data

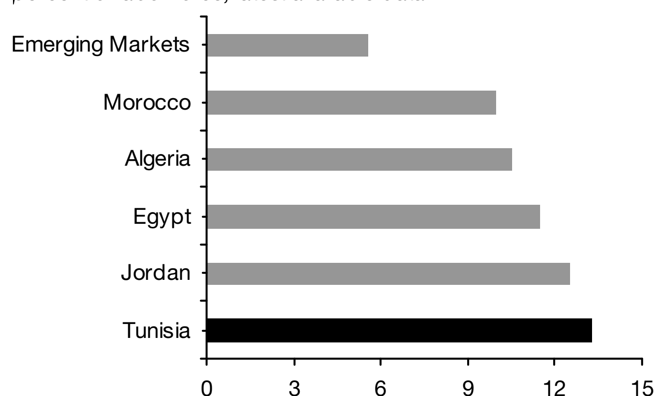
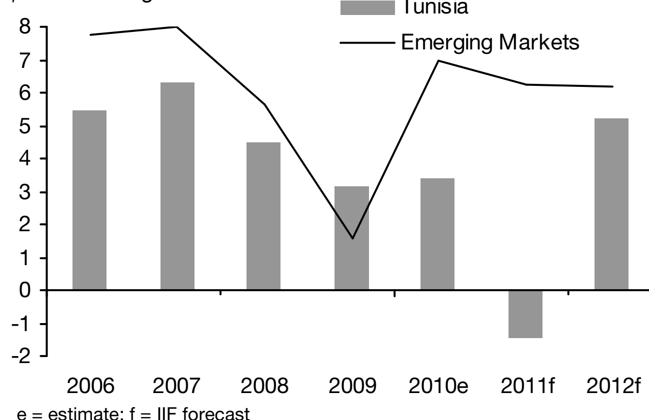
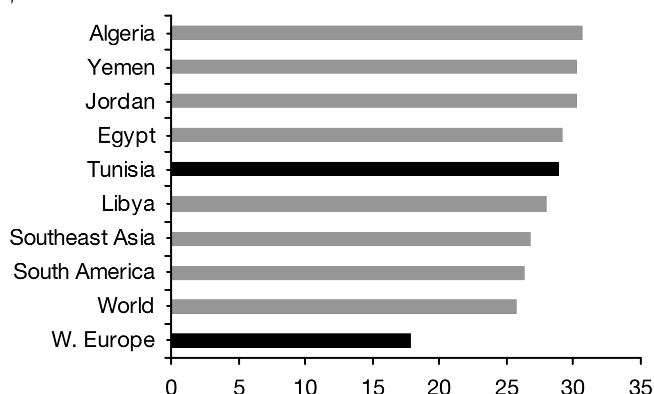


Chart 30
Tunisia: Real GDP Growth
percent change



e = estimate; f = IIF forecast

Chart 31
Tunisia: Population Aged 15-29 Years
percent of total



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LIBYA: NO CLEAR END IN SIGHT

Libya continues to be in a state of armed conflict, with no clear end in sight. The imposition of a no-fly zone on March 17, 2011 and the ensuing air strikes by the coalition have strengthened the opposition forces, but have not done enough to tip the military balance on the ground, leading to a de facto stalemate that could endure for some time. Oil and gas production and exports have effectively ceased, even in the rebel-controlled, oil-rich East, where damage to oil infrastructure from the fighting has halted oil production for at least four weeks. The global energy market has already priced in a shutdown of oil and gas production in Libya, but prevailing political uncertainties will sustain the risk premium and keep crude oil prices at or near current levels. Due to political uncertainty, we have not prepared forecasts for 2011 and 2012 (Table 24).

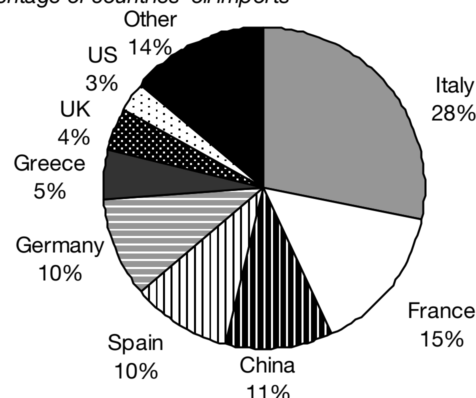
Table 24
Libya: Selected Economic and Financial Indicators*

	2008	2009	2010e	2011f	2012f
Nominal GDP, $ billion	95.4	68.9	83.2	...	...
Population, million	6.28	6.41	6.54	...	...
Real GDP, % change	2.7	-0.7	4.6	...	...
Hydrocarbon GDP, % chg	-0.5	-7.7	3.5	...	...
Nonhydrocarbon GDP, % chg	5.9	5.8	5.5	...	...
Crude Oil Production, mbd	1.8	1.6	1.7	...	...
Gas Production, mtoe	14.3	13.8	14.6	...	...
Current Account Bal., % GDP	38.7	13.6	19.8	...	...
Total External Debt, % GDP	4.7	6.9	6.0	...	...
Deposits in BIS banks, $ bn	72.5	66.1	64.0	...	...

e = estimate; f = IIF forecast
* Absence of projections for Libya due to lack of political certainty

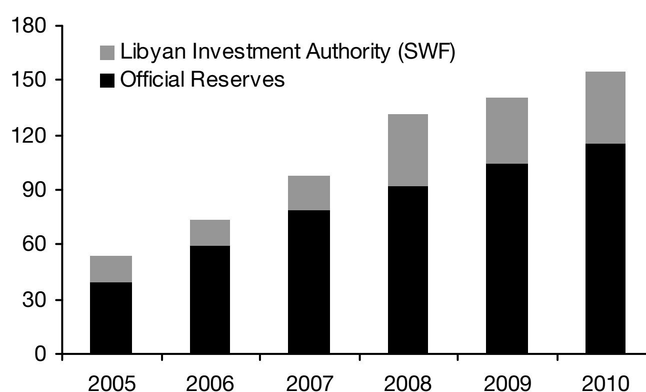
Libya is the world's 17th-largest oil producer, Africa's third-largest, and home to the continent's largest crude oil reserves, estimated at about 44.3 billion barrels and equivalent to around 67 years at current production levels. Libya is an OPEC member and, prior to recent events, produced about 1.8 mbd, of which it exported about 1.5 mbd, or just under 2% of global demand. About 85% of Libya's oil is exported to Europe, mainly to Italy (Chart 32).

Chart 32
Libya: Oil Exports by Destination, 2010
percentage of countries' oil imports



As a major oil and gas exporter, Libya has generated a current account surplus for decades and, as a result, has built up considerable foreign assets, most recently estimated at about $150 billion at end-2010 (Chart 33). Libya's foreign assets fall into three categories: (i) reserves and other financial assets managed by the country's central bank, about $110 billion; (ii) a wide range of investments in financial and real estate assets spread around the globe, about $36 billion, controlled by the Libyan Investment Authority (LIA), Libya's sovereign wealth fund; and (iii) commercial banks' (largely government owned) foreign assets, around $4 billion. Typical investments of the LIA include 3% of British publisher Pearson; several choice properties in London; a 2.6% share in UnitCredit, Italy's largest bank (a further 5% is owned by the central bank); a 7.5% stake in Juventus; and a 2% stake in both Fiat and Finmeccanica SpA, an Italian aerospace company. Libya also has substantial investments in Africa.

Chart 33
Libya: Official Foreign Assets
$ billion



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MOROCCO: NEED TO FOCUS ON REFORMS

The direct impact on Morocco of the recent political turmoil in the region is expected to be contained. King Mohammed VI is popular and there are no risks to the monarchy itself. In March of this year, the King announced a package of reforms, including the formation of a committee to recommend constitutional changes by June to help secure an independent judiciary, a freely elected parliament, a government elected by parliament, and greater powers for political parties. These reforms will be voted on in a popular referendum in June.

The country suffers from poverty and unemployment, as well as allegations of high-level corruption. It faces a major challenge in reducing the high levels of unemployment and poverty. Higher and sustainable growth rates are needed to provide jobs for new entrants into the labor market and to improve living standards. Also, growth needs to be broadly based, benefiting large segments of the population. Because of weak institutions, wealth concentration and lack of transparency, the benefits of growth are poorly distributed within Moroccan society.

Overall growth in 2011 is projected at 3.3%, driven in part by a rebound in agricultural output (Table 25). Nonagricultural growth is expected to decelerate from 4.9% in 2010 to 3.0% in 2011, because of uncertainty about social and political events in the region, which is adversely impacting tourism and private investment. Subsidies on food and petroleum products, combined with a stable exchange rate, have helped maintain inflation at a low 12-month rate of 1.6% in March 2011. Spending on subsidies and other social transfers is expected to rise to 4.5% of GDP in 2011. As a result, the fiscal deficit will remain large at 5.3% of GDP in 2011 (Chart 34).

Several indicators show that gains in external competitiveness in Moroccan goods appear to have been eroded in recent years. According to the Trade Performance Index (TPI), Morocco falls behind Tunisia, Turkey, Poland, and Romania in basic manufacturing and textile exports. In addition, the Global Competitiveness Index (GCI) ranks Morocco 73rd out of 133 countries, also placing it well behind the same group (Table 26).The authorities have adopted a range of structural reforms to improve the business environment, strengthen physical infrastructure, and improve the competitiveness of key sectors.

Table 25

Morocco: Selected Economic and Social Indicators

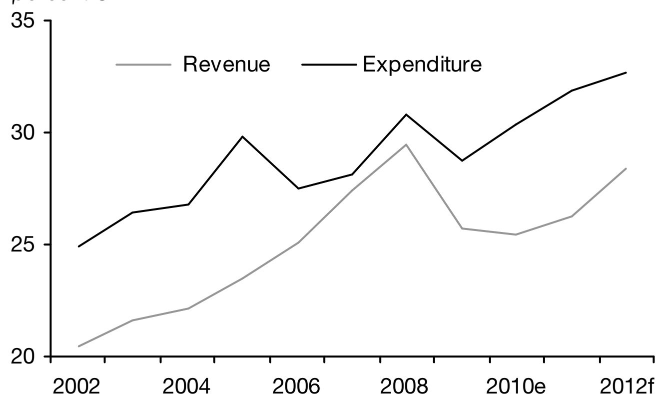
	2008	2009	2010e	2011f	2012f
GDP, $ billion	88.9	90.3	89.6	96.7	102.8
Real GDP (% change)	5.6	4.9	3.4	3.3	4.0
Agriculture	16.6	29.0	-8.0	5.0	4.0
Nonagricultural	4.1	1.5	4.9	3.0	4.0
Consumer Prices, avg., %	3.8	1.1	0.8	2.5	3.2
Fiscal Balance, % GDP	0.4	-2.6	-4.3	-5.3	-4.6
Government Debt, % GDP	47.3	48.2	49.8	51.8	51.3
Current Account, % GDP	-6.1	-5.0	-4.8	-5.9	-4.2
Reserves, Months Imports	7.0	6.4	6.4	5.7	5.5
Unemployment, %	9.6	9.0	9.2	9.2	9.0
Illiteracy Rate, % of Pop.	40.5	39.7	38.6	37.0	37.0

e = estimate; f = IIF forecast

Chart 34

Morocco: Government Revenue and Expenditure

percent GDP



e = estimate; f = IIF forecast

Table 26

Competitiveness Rankings, 2010[1]

	TPI		GCI[4]
	Textiles[2]	Manufacturing[3]	
Poland	34	29	46
Turkey	4	15	61
Tunisia	74	29	40
Romania	41	45	64
Morocco	82	88	73

[1] The higher the less competitive.
[2] Out of 129 countries.
[3] Out of 147 countries.
[4] Out of 133 countries.
Source: UN and WTO for TPI; WEF for GCI.

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IRAQ: OIL PRODUCTION TO DOUBLE WITHIN 5 YEARS

Iraq's experiment with democracy is still in its infancy, and the country is not immune to the calls for political reform sweeping the region. After nine months of political stalemate following elections held in March 2010, a national unity government comprising a broad coalition of all of Iraq's main factions was finally announced in December of last year. The new cabinet, however, remains incomplete. Certain key ministries, including those for interior, defense, and other key security posts, remain unfilled. The security situation remains volatile, and widespread protests against government corruption, high unemployment (estimated at 14%), and poor basic services have added to the challenges facing the government.

Iraq's oil production has increased significantly in the first quarter of this year to an average of 2.70 million barrels per day (mbd), as compared with 2.36 mbd in 2010. Assuming consumption of oil increases by 5% a year, exports of crude oil in 2011 are projected at 2.15 mbd (Table 27). The increase in oil production during the first quarter of this year is in response to strengthened global demand occasioned by Libya's shortfall. It was also aided by three successful bidding rounds held since 2008, which drew in international oil companies to develop and/or rehabilitate Iraq's vast oil fields. The government has set ambitious plans to increase oil output to 11 mbd by 2020. We believe that this target is unlikely to be met. Instead, in our conservative scenario, we expect crude oil production to gradually rise to around 4.5 mbd by 2015 (Chart 35).

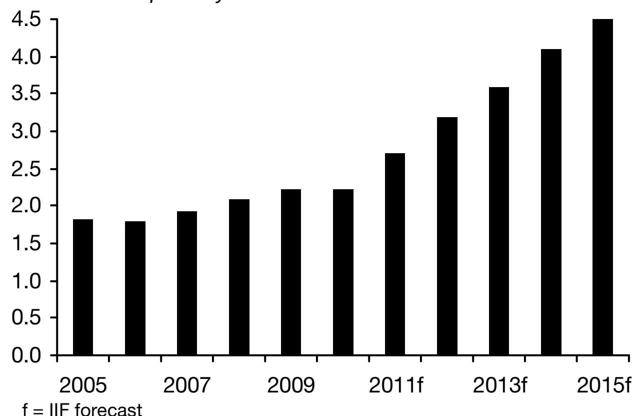
The sharp increase in oil production, combined with higher oil prices, will shift the external current account and fiscal deficits of 2010 to large surpluses of 7.6% of GDP and 6.4% of GDP, respectively, in 2011 (Table 27 and Chart 36). Overall, real GDP is projected to grow by 11.0% in 2011 as a result of the large increase in crude oil production. Growth in nonoil real GDP will depend on improvements in the security situation. If oil prices remain above $100 per barrel, and if the production of crude oil continues to increase over the coming years to about 4.5 mbd by 2015, then official foreign exchange reserves could almost triple, rising from $50 billion at end-2010 to $143 billion by 2015, equivalent to 78% of projected GDP, or 15 months of import cover.

Table 27
Iraq: Main Macroeconomic indicators

	2008	2009	2010e	2011f	2012f
Nominal GDP, $ billion	82.9	65.9	80.7	114.4	127.1
Real GDP Growth, %	9.0	4.7	0.8	11.0	11.3
Oil	12.1	5.6	-1.9	16.6	16.1
Nonoil	5.4	3.7	4.2	4.5	5.0
CPI Inflation, average, %	2.7	-2.8	5.0	6.0	5.0
Crude Oil Production, mbd	2.28	2.40	2.36	2.75	3.20
External Debt, % GDP	111.6	135.3	107.7	64.2	45.8
Current Account, % GDP	15.1	-26.0	-7.4	2.6	3.9
Fiscal Balance, % GDP	-1.3	-22.2	-11.4	6.4	2.9
Official Reserves, $ billion	49.9	44.1	50.4	52.8	54.4

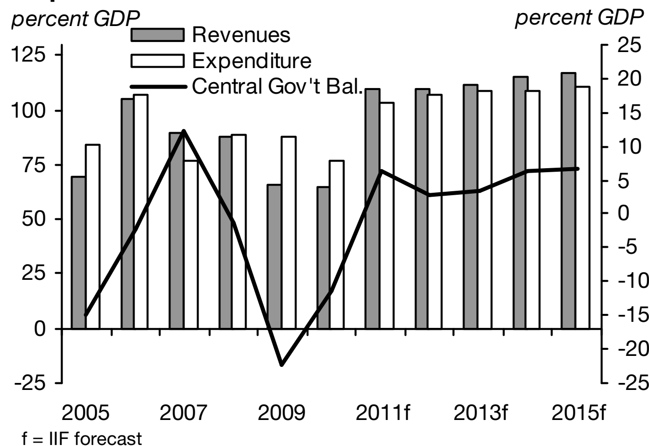
f = IIF forecast

Chart 35
Iraq: Oil Production
million barrels per day



f = IIF forecast

Chart 36
Iraq: Fiscal Indicators
percent GDP *percent GDP*



f = IIF forecast

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LEBANON: GROWTH SLOWS, DEFICIT WIDENS

Lebanon has one of the longest traditions of democracy in the Arab world and has not witnessed the kind of internal calls for change and freedom taking place in other Arab countries. However, the turmoil in the region, particularly the crisis in Syria, coupled with domestic political paralysis, is starting to weigh on Lebanon's economy.

Following the collapse of the government triggered by the resignation of ministers from Hizbullah and its allies on January 12, Lebanon was plunged into renewed political crisis. Prime Minister-designate Najib Miqati has charted an independent path for himself, winning adherents on both sides of the political spectrum. However, his efforts to form a new cabinet have reached a stalemate aggravated by the impact of regional events. Achieving a political consensus remains elusive, with no agreement in sight.

Domestic and regional events have taken a toll on the Lebanese economy. Tourist arrivals and foreign direct investment are projected to decline significantly as compared with 2010. Also, in the absence of a new government, urgent structural reforms (including addressing the bottlenecks in the energy, telecommunications, transportation, and water sectors) will be postponed, jeopardizing prospects for rapid medium-term growth. Consequently, we project real GDP growth to decelerate from 7.0% in 2010 to around 4.0% in 2011 (Table 28). The fiscal deficit is projected to widen from 7.5% of GDP in 2010 to 9.5% in 2011 due to weaker tax revenue, particularly taxes from property and gasoline, as a result of the slowdown in construction activity and a 50% reduction in the excise tax on gasoline in February.

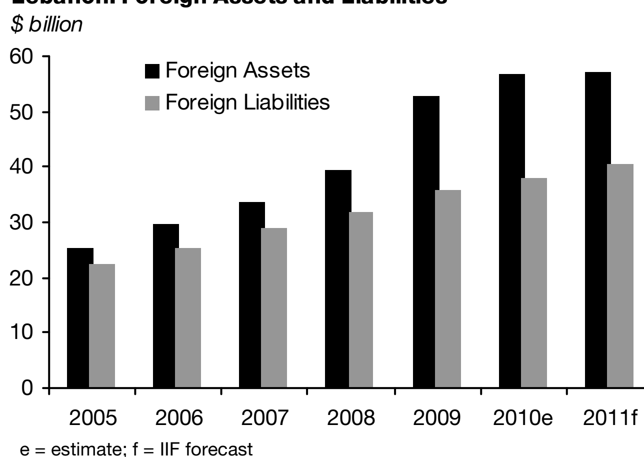
Risks to the stability of the exchange rate and the banking system will remain minimal. The current level of official exchange reserves of $30 billion, plus gold holdings at Banque du Liban (valued at about $13.5 billion), exceed the estimated GDP for 2010 and are equivalent to more than one year of import cover of goods and services (Chart 37). Lebanon's public debt is intermediated mostly through domestic banks that have a vested interest in the stability of the system and are, therefore, willing to roll over their exposure to the sovereign (Chart 38). The debt is ultimately financed through bank deposits from residents, the Lebanese Diaspora, and investors from the GCC countries.

Table 28
Lebanon: Main Macroeconomic Indicators

	2008	2009	2010e	2011f	2012f
Nominal GDP, $ billion	29.9	34.2	38.6	41.6	46.4
Real GDP Growth (%)	9.3	8.6	7.0	4.0	5.7
Tourism, % GDP	7.5	8.1	8.2	7.8	8.5
FDI, % GDP	11.2	13.0	12.9	7.2	9.2
CPI , % change, average	6.4	3.1	4.4	6.2	4.0
Overall Balance, % GDP	-9.9	-8.7	-7.5	-9.5	-8.2
Primary Balance, % GDP	1.1	2.6	3.5	0.4	1.5
Government Debt % GDP	158	150	136	135	131
Gross Reserves, $ billion	20.2	29.1	31.5	29.7	29.0

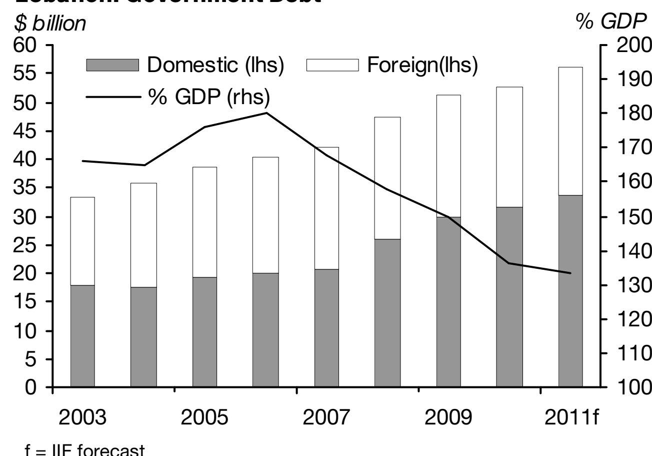
e = estimate; f = IIF forecast

Chart 37
Lebanon: Foreign Assets and Liabilities
$ billion



e = estimate; f = IIF forecast

Chart 38
Lebanon: Government Debt
$ billion *% GDP*



f = IIF forecast

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