

MACROECONOMICS

Oman Predicts Deficit in 2014 Draft Budget...

1. Darwish al-Balushi, the Omani Minister for Financial Affairs, addressed the Omani Consultative Council on 26 November to outline the draft 2014 budget. The Minister said the state's general expenditure has surged 70% over the last three years, rising from \$20.5bn in 2011 to a record \$35.1bn in 2014. He warned that the government is facing a real challenge to sustain the current level of spending, and forecasted GDP growth of 5% and a fall in inflation to 1.5%. The Minister estimated the budget's deficit for next year at \$4.68bn which amounts to 15% of the total revenues and 6% of the GDP. The Consultative Council has approved the general budget for 2014 and referred it to the State Council.

...but the Government Hints at Possible Reform of Fuel Subsidies

2. The Omani Minister for Oil and Gas, Mohammad al-Rumhy, has made two widely covered public statements within the space of three weeks warning that fuel subsidies are a threat to economies across the GCC. More recently, Mohammed bin Abdullah al-Mahrouqi, Chairman of the Public Authority for Electricity and Water, said his organisation has been asked to carry out a wide ranging survey of energy usage in Oman with a view to establishing a National Energy Strategy. Fuel subsidies will come under the review.

Qatar Aims to Increase Macroeconomic Discipline

3. Qatar's Emir gave his first major economic policy speech since taking office in June, when he opened the 42nd ordinary session of the Advisory Council and the first under his rule. For Qatar to achieve sustainable and balanced growth, the Emir argued that Qatar needs to increase productivity and efficiency, promote economic diversification, encourage the private sector and entrepreneurship, reduce barriers to competition, tackle inflation, and focus on research and development, education, and health.

4. Qatar is investing significantly ahead of hosting the Fifa World Cup 2022, with up to \$220bn on infrastructure, which is bringing debt and price pressures. Qatar's gross debt reached 36% of gross domestic product last year, the highest among the six GCC members and more than Iraq's 34%, according to the International Monetary Fund. Inflation was at 2.7% year-on-year in September. To combat this, Qatari authorities in November announced that state-owned companies, excluding Qatar Petroleum (QP) (the state-owned energy firm) and its subsidiaries, must now seek approval from the Ministry of Finance before undertaking any borrowing activity. A government committee has also been set up to propose ways to tackle inflationary pressures.

5. These moves have been welcomed by analysts and investors, and follow-on from similar steps taken by Qatar's GCC neighbours. The UAE central bank in April 2012 barred banks from lending more than 100% of their capital to local administrations or government-related entities. Abu Dhabi has also set up a debt management office to coordinate borrowing by government-related entities after the crisis in neighbouring Dubai, which resulted in a \$20 billion bailout and massive debt restructurings at state-linked entities.

ENERGY

A Busy Month for Qatar's Gas Industry

6. November has been a busy month for Qatar as it seeks to maximise returns from the supply of gas, whilst simultaneously expanding into higher yield areas of the global energy supply chain. Developments have included:

- Centrica signing a \$7.23bn deal with Qatar to import 3m tonnes of liquefied natural gas (LNG) per year over four and a half years (equivalent to about 13% of UK's annual residential gas demand). The deal extends a \$3.2bn, three-year LNG supply agreement between Centrica and Qatargas, which expires in July 2014;
- the President of Congo visiting Qatar to sign a framework agreement on co-operation between Qatar Petroleum International and Total E&P Congo;
- reports suggesting that Ivory Coast is close to finalising an agreement with Qatar for LNG supplies from 2015;
- negotiations between Qatar and India on a deal covering LNG and air transport, with India seeking discounts on gas imports in exchange for concessions on Qatar Airways increasing its capacity between the two countries;
- an announcement from Poland's Supreme Audit Office that it would look into the country's deal to import LNG from Qatargas, whose supplies could potentially be more expensive than existing sources of gas.

Kuwait Oil Company Invites Tenders for Off-Grid Solar Power

7. The Kuwait Oil Company (KOC) has issued an invitation to tender for a five megawatt solar power plant at its Umm Gudair field. The electricity generated by the plant is intended to power KOC's gas and oil extraction equipment, and is in line with attempts by oil producers across the region to preserve as much as possible of their hydrocarbon resources for export (Kuwait, for example, currently produces 2.8mbpd total petroleum liquids, and plans to increase this to just over 3.6mbpd by 2020).

LABOUR MARKETS

Saudi Labour Market Crack Down

8. On 3 November, the seven month amnesty period offered by the Saudi government to illegal foreign workers in the Kingdom ended. During this period, foreigners without work permits corresponding to their actual job were given the opportunity to exit the Kingdom penalty-free, correct their paperwork, or find a job with a company that had a sufficient proportion of Saudi workers (as defined by the Ministry of Labour's 'Nitaqat' system).

9. Following the end of the amnesty period, Saudi police, accompanied by Ministry of Interior and Labour officials have been inspecting workplaces and carrying out spot-checks on streets to identify illegal workers. Those without the correct paperwork have been arrested, transferred to detention centres and deported. So far it appears that up to 140,000 people have been arrested since early November, with around 120,000 of those already deported.

Tougher Rules on Industrial Action in Oman

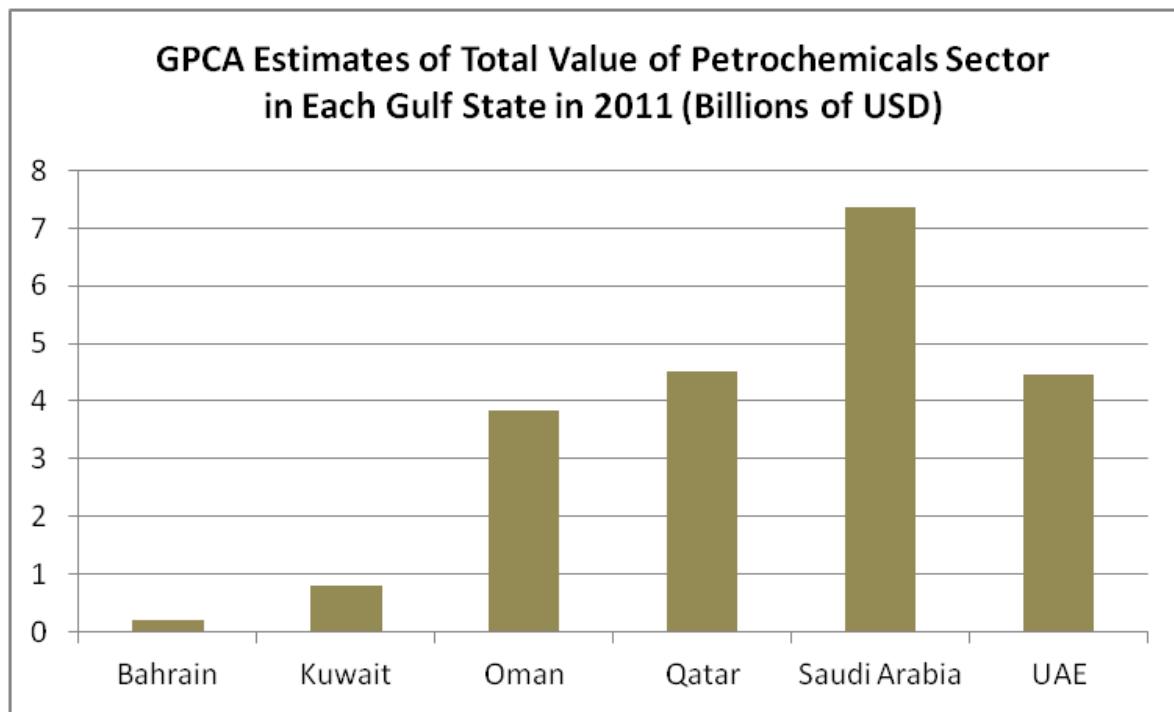
10. In mid-November, the Omani Ministry of Manpower amended the rules on collective bargaining and strikes, making it illegal to hold or incite strikes at “establishments that provide essential public services”. News reports specified that this applies to oil facilities, ports and airports, but it is not clear whether schools are also included in the category. The teachers strike has ended and legal action is reportedly being taken against some of the ring leaders.

DIVERSIFICATION

Growth in the GCC Petrochemicals Sector...

11. The Gulf Petrochemicals and Chemicals Association (GPCA) has revealed that in 2011, petrochemical production accounted for 1.5% of aggregate GCC GDP. Petrochemicals' share of member states' output varied from 5.5% of Omani GDP to 0.49% of Kuwaiti GDP. To illustrate what this means in terms of value added, petrochemicals accounted for 53% of the value of Omani manufacturing in 2011, compared with 4.6% for Bahrain. In terms of absolute value, Saudi Arabia topped the charts with \$7.36bn worth of petrochemical output in 2011, whilst Bahrain was at the bottom of the scale with \$0.207bn.

12. In terms of export earnings, petrochemicals represented 43% of GCC non-oil exports in 2011, compared with 41% in 2010. Broken down by state, this represented 72% of Saudi non-oil exports compared with 8.6% for Bahrain.



...But Competition from the US Looks Set to Increase

13. Existing petrochemical producers and exporters the world over are likely to face increased competition from the US in the years ahead, owing to increased production of shale gas. Gulf producers currently supply just over 10% of the \$600bn global petrochemical market, but with some reports suggesting the US planning to invest over \$100bn in production facilities, the US has the

potential to become the world's lowest-cost producer. Everything, of course, will depend on domestic US gas prices (which in turn will depend upon the future of the US's gas distribution infrastructure and LNG export policies). But the most obvious market for increased US petrochemical output is East Asia, which would place American producers in direct competition with their Gulf counterparts. This would leave Gulf producers with three overlapping options:

- compete with the US in East Asian markets;
- attempt to expand their share of other emerging markets; and
- develop and produce more specialist petrochemical products that attract higher margins.

14. From an economic sustainability point of view, the third option is the most attractive for the Gulf. Competing with the US on volume and price of existing products will do little to broaden the productive bases of regional economies, nor offer many jobs to qualified graduates. Opening new markets would be slightly more labour intensive, but again, would likely entail a degree of price and volume competition. The third option would make best of the Gulf's growing engineering and scientific talent, and offer opportunities for Gulf citizens to actively participate in the development of knowledge economies. Outside help may be required, providing opportunities for UK companies which are willing to base themselves in the region long-term, and develop mechanisms to transfer developmental and engineering know-how to their Gulf hosts.

FINANCE

Close Co-operation Among Gulf Stock Markets?

15. Saudi Stock Exchange Tadawul (which means 'dealing') has signed memoranda of understanding (MOUs) with the Abu Dhabi Securities Market (ADX), and the Bahraini stock market Bursa (which means 'stock market'). The MOUs focus mainly on the operation of the three markets, and cover staff development and operational knowledge exchange.

16. People working across the region's finance sectors have been discussing for years now the possibility of a combined Gulf stock exchange. While this is unlikely to become a reality in the short to medium term, clauses in the MOUs covering market development and policy alignment may serve as a foundation on which more focused discussions at some point in the future could build.

Qatari Telecoms Company Issues \$1.25bn Sukuk

17. Ooredoo, Qatar's biggest phone operator with revenues of US\$9.3 billion in 2012 and operations across the Middle East, North Africa and Southeast Asia, launched a \$1.25 bn, five-year sukuk. This was the firm's first Islamic bond under its recently established US\$2 billion Trust Certificate Programme, which was four times over-subscribed. The Ooredoo offering was Qatar's first corporate Islamic bond sale in two years, with the last country's last Shari'a-compliant corporate issue being the US\$215m sale from Almana Group in June 2011. The move illustrates Qatar's desire to compete with Kuala Lumpur, Manama and Dubai as a global centre of Islamic Finance, and may herald a shift towards Islamic finance as Qatar's government and private sector look to tap debt markets to finance up to \$220bn of investments in preparation for the 2022 World Cup.

INTERNATIONAL COMMERCE

Dubai to Host 2020 World Expo Trade Convention

18. Dubai has beaten Yekaterinburg in Russia, Ismir in Turkey and Sau Paulo in Brazil to host the 2020 World Expo trade convention. This will not only reinforce the emirate's position as a global trade and business hub, but also boosts Dubai's future economic performance. Experts estimate that the global event will add 0.5 percentage points per year to real GDP growth over 2015 -2017, rising to 1.0 percentage points per year over 2018-2020. Dubai's trade, tourism and transport sector will benefit the most from the event, and 277,000 new jobs will likely be created. Infrastructure spending is expected to be around \$5.45bn and investments will be directed mostly towards the addition of 80,000 additional hotel rooms, and the development of tourist attractions and transport facilities (eg. the metro extension). There will of course be opportunities for British companies.

19. Winning the Expo has crowned a strong year for Dubai. The Emirati Central Bank estimates growth during the first half of 2013 was 4.9% (the highest in six years and 0.2 percentage points better than expected). Most of the growth has come from growth in non-hydrocarbon industrial, hospitality and tourism sectors, and Dubai's success in being chosen as the venue for the 10th World Islamic Economic Forum will provide a further boost to the emirate's financial sector. But some analysts fear the additional stimuli risks generating another property bubble. Careful macro-level policy making will help lessen the risks of a return to boom-and-bust, and ensure that the major international events the emirate is hosting contribute to sustainable growth.

Dubai Air Show Highlights Growth in Regional Civil Aviation...

20. Boeing and Airbus's order books at the Dubai Airshow have illustrated once again the enormous growth anticipated by the region's air carriers over the next two decades. Between them, Emirates, Etihad, Fly Dubai and Qatar Airways announced orders for a combined total of 623 new aircraft (including options) with a total list price value of over \$200bn. A summary of the orders is below.

- Emirates placed the largest order in civil aviation history for 250 aircraft (including 50 options), worth a combined total of \$99bn. The orders comprised:
 - 50 Airbus A380s valued at \$23bn; and
 - 150 Boeing 777-Xs (plus 50 options) valued at \$76bn.
- Etihad ordered 199 aircraft (143 firm with 56 options) and 294 engines. The total value of purchases is worth \$67bn at list prices includes:
 - 36 Airbus 320 Neos;
 - 1 Airbus 330 Freighter;
 - 50 Airbus 350s;
 - 25 Boeing 777-Xs;
 - 30 Boeing 787-10s;
 - 1 Boeing 777 Freighter;
 - 52 engines from CFM;
 - 127 engines from GE; and
 - 115 engines from Rolls Royce.
- FlyDubai ordered 111 Boeing 737s (100 737 MAX 8s and 11 737-800 NGs) valued at \$11.4bn.
- Qatar Airways ordered 63 aircraft (including options) with a total list value of \$21.8bn. The order comprised:

- five Airbus 330 Freighters (with options on eight more) valued at \$2.8bn (plus a \$300m for Rolls Royce engines); and
- 50 Boeing 777-9X passenger aircraft, valued at \$19bn.

21. Kuwait Airways was expected to announce a deal for Airbus aircraft at the show, but instead the deal was signed a couple of weeks after. The airline ordered 15 A320s and 10 A350-900s with a list price of \$3.4bn (with options to order a further five of each). It also struck a deal to lease 7 A320s and 5 A330-200s to cover the time period before the new aircraft are delivered.

...But Will Inefficient Use of Airspace Act as an Airbrake?

22. Gulf air carriers' ambitious expansion plans face challenge from the way in which airspace over the Gulf is managed. At present, different blocs of airspace are controlled by a range of national air traffic services, both civilian and military. This places constraints on the number of aircraft that can transit through any given patch of sky, and means aircraft sometimes have to follow inefficient routes. With aircraft movements per annum set to double to 1.62m by 2030 in Emirati skies alone, GCC aviation authorities will have to look seriously at merging their regional control centres, and accepting a greater degree of shared responsibility for managing their airspace.

Kuwait Airways Flights to Iraq

23. On 22 November, a Kuwait Airways scheduled flight landed for the first time at an Iraqi airport since the 1990 invasion. The flight marks the beginning of a twice-weekly service between Kuwait City and Najaf. Flights to other Iraqi cities will be subject to passenger demand and security.

24. Iraqi Airways resumed flights from Baghdad to Kuwait City in February this year, following the end of legal dispute between Kuwait Airways and the Government of Iraq dating back to 1991. In June, Kuwait supported Iraq's exit from UN Chapter VII Sanctions on the repatriation of missing people from the 1990/91 conflict, and the return of its national archive. In early November, both Governor of Basra and President of the Kurdistan Regional Government visited Kuwait, and Kuwait has plans to open Consulates in Basra and Erbil.

25. Improving links between Iraq and Kuwait will offer both countries valuable trade and investment opportunities, which will support infrastructure renewal and economic diversification.

ECONOMIC AID

Kuwait to Fund Construction of Jordanian LNG Terminal

26. The Kuwait Fund for Arab Economic Development (KFAED) has agreed to finance the construction of a jetty and (liquefied natural gas) LNG receiving terminal 18km south of the Jordanian port city of Aqaba. The project is expected to cost \$65m, and will be completed by a joint venture between UK-based BAM International, and Jordanian MAG Engineering and Contracting.

27. The Kuwaiti grant to finance the terminal forms part of a framework agreement worth a total of \$1.25bn signed in September 2012 between Jordan and the KFAED. It should help diversify Jordan's energy imports, and together with other infrastructure funding from Kuwait and the rest of the Gulf, help the Jordanian economy transition to a model of greater value-added output.

Qatar provides \$500m of financial support to Tunisia...

28. Qatar has given Tunisia's central bank \$500m to support its foreign currency reserves. The plan is for Tunisia to pay back the loan to Qatar over five years with an interest rate of between 2.5 and 3 percent. This builds on earlier announcements of economic aid from Qatar to Tunisia, including \$1bn in April 2012, \$500m in November 2012, and \$1bn in April 2013.

...and \$150m to Palestinian Authority

29. Qatar in November also pledged \$150m to the Palestinian Authority (PA). The announcement came during a visit to Doha by the Palestinian Prime Minister, Rami Hamdallah, and follows Qatar's pledge in Paris in October to provide the PA with \$150m of debt relief.