Foreign & Commonwealth Office

GCC Economics Summary

July and August 2014

MACROECONOMICS

Kuwait's Parliament Passes Annual State Budget...

1. On 3 July the Kuwaiti Parliament passed the 2014/15 state budget. Total planned expenditure of $80.95bn represents a record high for the country and is projected to result in a $10.95bn deficit. Planned oil income was $65.57bn (94% of total revenue), though this was based on a conservative oil price of $75 per barrel (up $5 per barrel from the last FY). Despite the state projecting deficits every year since 2000, the low budgetary oil price has resulted in 14 successive annual budget surpluses totalling over $300bn. A full breakdown is yet to be released but initial figures indicate that public sector salaries of $19.53bn and subsidies $20.58bn will account for around half of total spend with capital investment allocated 10% ($8bn).

...Whilst the Cabinet Approves New Five Year Development Plan for Kuwait

2. Kuwait's Cabinet has debated and approved the state's new five-year (2015-2020) development plan and have now referred it to the Parliament for consideration. The plan has a two-pronged approach. The first is to free the private sector to play a greater role in development through economic reform. The second is to realise Kuwait's long term strategic vision through implementation of mega-projects. Full details of the plan remain undisclosed ahead of parliamentary scrutiny but several of the very delayed mega-projects from the former development plan are confirmed to be included, such as the $3.35bn metro project and $27.8bn rail project (part of the GCC-wide plans for a connected rail network). Other areas reportedly included relate to a new media city, education privatisation and further development of Kuwait's Mubarak al-Kabeer port on Boubiyan Island.

Infrastructure Projects Fail to Prevent Qatari Spending Growth Hitting an 11 Year Low ...

3. Qatari government data shows that state expenditure increased 12.7% in the last fiscal year (ending March 2014), the lowest rate in 11 years. Total actual expenditure reached a record high of $63.3bn (31% of GDP), 10% greater than planned and up from $56.5bn the previous year. But the margin by which actual expenditure overshot planned was the lowest in five years. In the previous four years, expenditure had exceeded plans by an average of 25%.

4. The slowdown was primarily due to reduced growth in current expenditure, which rose by only 6% to $44.8bn in FY2013/14, compared with increases of over 24% in each of the previous two years. The decline was primarily due to reduced interest repayments, and lower bills for services. In keeping with previous years, Qatar's state sector wage bill continued to rise. The slowdown in spending also reflects that the government has shifted away from the pattern of the previous four years when on average it spent almost a quarter more than originally planned.

5. The slowdown in current expenditure was partly offset by project spending increasing by 32.7% to $18.8bn, compared with growth of just 1.9% the year before. Whilst work on some infrastructure projects worth up to $220bn to deliver its 2030 National Vision and the 2022 World Cup appears to have accelerated, bottlenecks in planning and logistics remain. Qatar has scaled down or divided into phases some big-ticket projects, such as a metro, a port and airport facilities, to reduce overcapacity risks. It has also established the Central Planning Office and Public Investment Management unit at the Ministry of Finance to oversee and co-ordinate these projects.

... Whilst Risk of Budget Deficit in Medium Term Remains

6. Whilst Qatar's state revenue reached a record high of $95.2bn in FY 2013/14, its growth slowed to 21.9%, compared with 27.8% the previous year. The decline in growth would have been even greater

if Qatar Petroleum (QP) had not started transferring its entire financial surplus to the government in 2013. (Previously, part of QP's revenue went to the government as investment income, part was retained on the company's balance sheet, and part was used to provide fresh capital to the Qatar Investment Authority). QP's injection of cash helped Qatar's most recent budget surplus to a record high of $31.6bn (15.6% of GDP), up from $21.6bn (11.4% of GDP) the previous year.

ENERGY

QPI and ExxonMobil seek US approval for $10bn LNG export project

7. Qatar Petroleum International (QPI) and ExxonMobil formally applied in July to the US Federal Energy Regulatory Commission (FERC) to construct and operate an LNG export terminal at the existing Golden Pass LNG import facility at Sabine Pass, Texas. This was through their joint venture Golden Pass Products LLC (70% QPI and 30% ExxonMobil). The export terminal would have a production capacity of 15.6m tonnes of LNG per year.

8. Sabine Pass cost $2bn and received its first shipment of Qatari LNG in 2010. But the US shale gas boom has led to it (and other LNG import terminals in the US) being underutilised. The FERC approval process will involve an environmental impact study, multiple agency regulatory reviews and the input of views from the public. The project has already received US Department of Energy authorisation for exports to Free Trade Agreement (FTA) countries and is awaiting Department of Energy approval to export to non-FTA nations. This would allow exports to Europe, including QPI and ExxonMobil's joint venture LNG import terminal at South Hook in Wales and Adriatic terminal in Italy. A final investment decision is likely in 2015, after which Golden Pass would invest $10bn over five years to build the proposed facility.

Total Wins Deals for Gas and Oil Recovery in Qatar

9. QatarGas has announced plans for a $800m Jetty Boil-off Gas Recovery (JBOG) plant in partnership with Total. The project aims to recover gas currently being flared during LNG ship loading at Ras Laffan port and be used either as feedstock to LNG trains or as fuel gas. The project is likely to be commissioned formally later this year, and when fully operational will recover around 0.6m tonnes of LNG per annum, equivalent to approximately 1tn cubic feet of gas over 30 years.

10. Total has also signed a deal with Qatar Patroleum (40% and 60% shares, respectively) for enhanced oil recovery from the al-Khalij offshore field. The field started producing 17 years ago, and has a current output of around 23,000 barrels per day.

Saudi Arabia's Summer Domestic Energy Consumption

11. Figures released by the Saudi government show that domestic electricity consumption was 7.7% higher in August 2014 compared with August 2013. The summer months see the highest levels of energy consumption in the Gulf as residents turn up their air conditioners to cope with the brutally hot weather. Saudi Arabia has ambitious plans to reduce this consumption through energy efficiency measures (including new building codes), and preserve its oil exports by substituting oil for gas and/or renewable in electricity generation.

FINANCE

Saudi Council of Ministers Permits Direct Foreign Ownership of Saudi Equities

12. The Saudi Council of Ministers has announced that it will lift its ban on non-GCC ownership of companies listed on the Saudi stock exchange. Regulations to enable the change are now being worked out, and the Capital Markets Authority (CMA) has begun a 90 day consultation period. To date, unconfirmed reports have suggested that:
- foreign ownership would likely be limited to between 10% and 30% of Saudi equities;
- only foreign investors with major asset bases (some reports suggest in excess of $1bn) would be eligible to purchase Saudi shares;
- foreigners would be prohibited from owning shares in businesses based in Macca and Madina (consistent with existing foreign ownership rules); and
- the rules would probably come into effect in the first half of 2015.

13. As things stand, non-GCC individuals and entities are only able to purchase Saudi equities indirectly (through swaps or exchange transaction funds). The cost and inconvenience of these means that foreigners probably own less than 2% of current market value. Most estimates suggest that permitting direct foreign trading would inject $40bn-$50bn into the market rapidly. This would be a major boost to what is already the Arab world's largest stock market, and which according to the Saudi Arabian Monetary Agency (the Kingdom's central bank) had a total market capitalisation of $467bn at the end of 2013. The TASI (Tadawul All Share Index) jumped 2.8% on news of the Council of Ministers decision, with most of the increases driven by major government-backed companies (eg. SABIC, who's shares climbed 6.9%).

14. Lack of liquidity hasn't been a problem in recent years and this July (TASI closed at its highest level since October 2006). One factor behind this recent move is an attempt by the CMA to promote a culture of longer term investment in the market by encouraging the entry of foreign institutional investors (at present, the majority of market participants are retail traders). Another possibility is that the authorities hope foreign equity holders will inject a degree of free market rigour into an economy that remains dominated by the government and hydrocarbons (hydrocarbons accounted for c.50% of GDP in 2013 and over 90% of state revenue; government expenditure was c.35% of GDP. This would be consistent with wider efforts to develop the non-oil economy, increase competitiveness, and get more Saudis into work.

Will New Saudi Retail Lending Regulations Stimulate of Dampen Consumer Borrowing?

15. The Saudi Arabian Monetary Agency (SAMA) has issued new rules which will cap retail lending in the Kingdom, but at the same time reduce borrowing costs faced by consumers. As things stand, banks are only permitted to lend consumers up to 30% of their existing salary. The new rules stipulate that SAMA can, at its discretion, impose limits on the proportion of individual banks' retail lending portfolios relative to their total lending portfolio. Separately, the new rules state that fees, costs and charges associated with loans cannot exceed $1,333, or 1% of the total loan value, whichever is the lower.

BUSINESS ENVIRONMENT AND DIVERSIFICATION

Changes to Oman's Commercial Law Herald Progress Towards Reform of Consumer Protection Body

16. Our June summary reported the postponement of planned changes to the remit of the Omani Public Authority for Consumer Protection. In announcing the postponement, the Sultan said three laws (covering commercial agencies, competition and consumer rights) would need be amended or enacted before the consumer protection changes were implemented. In July, the first amendment was made. Changes to the Commercial Agency Law (which govern the relationship between foreign companies and local agents) remove some of the privileges offered to Omani agents, and allow parties to commercial agency agreements greater freedom in deciding the terms of renewal and termination.

The new law will enable foreign companies to sell directly to customers in Oman or through non-agent merchants, and will allow the Cabinet to determine the number and types of agencies allowed to be controlled by each agent, in order to reduce the likelihood of monopolies forming.

Streamlining of Saudi Arabian General Investment Authority Regulations

17. The Saudi Council of Ministers has asked the Saudi Arabian General Investment Authority (SAGIA) to streamline the process for granting licences to major established companies wanting to continue or expand their operations in the Kingdom. The situation regarding smaller companies that are yet to establish track records remains unclear, as are the timings on when any new rules are likely to be implemented.

Gulf Air's Drive to Profitability Continues...

18. Bahraini carrier Gulf Air has announced that it has reduced its year on year losses in the first half of 2014 by 30% (down from $833m). The achievement is the result of an aggressive re-structuring and cost-cutting policy announced in late 2012, which included reducing staff levels by almost 30%, renegotiating supply contracts, retiring older aircraft, and concentrating on higher yield routes.

19. Gulf Air is the second oldest of the region's major airlines (the oldest being Saudia), and in the past was owned jointly by Bahrain, Qatar, the UAE and Oman. Bahrain took full control of the airline in 2007. These latest results are the airline's best in eight years, but it still has a long way to go if it is to return to its glory days of the 1980s and 1990s, and challenge younger rivals such as Emirates, Qatar Airways and Etihad.

...Whilst Etihad Completes Takeover of Alitalia

20. Alitalia and Etihad signed a long-awaited deal (see our February 2014 summary), under which Etihad became Alitalia's largest shareholder. In addition to acquiring a 49% stake, Etihad purchased a number of take-off and landing slots held by Alitalia at London's Heathrow airport, worth over $77m, which Etihad is reportedly planning on leasing back to the Italian carrier.

21. Whilst the deal helps Etihad's expansion into Europe by tapping into Alitalia's network, it also saves Alitalia from bankruptcy. Abu Dhabi Airport's success is closely linked to Etihad's growth and hence, Etihad is an integral part of Abu Dhabi's long-term economic development strategy. Etihad, which is the UAE's second largest carrier after Emirates, is following an ambitious global growth strategy, launching new routes and increasing frequency on existing routes. It now has shareholdings in nine airlines, including Air Berlin (29%), Air Seychelles (40%), Aer Lingus (35%), Air Serbia (49%), Jet Airways (24%) and Virgin Australia (20%).

INFRASTRUCTURE

Oman Completes Transfer of Cargo Operations from Muscat to Sohar...

22. Commercial cargo shipments to Muscat's Sultan Qaboos Port (SQP) formally ceased on 31 August, with most now redirected to Sohar Industrial Port (c. 230km north-west along the coast). The move is part of a plan to replace SQP's aging cargo handling infrastructure with the much newer facilities in Sohar, which in turn will support the region's development as an industrial and logistics hub. The region already boasts a growing free trade zone. Future developments are likely to include a 60% expansion of the port, an international airport and links to the planned GCC rail network. SQP will serve from now on as a dedicated passenger terminal (part of the Sultanate's aim to develop its tourism sector).

...Whilst Entry into Service of Qatar’s New Port Set for End of 2016

23. The Qatari authorities have announced that the first phase of the $7.4bn Doha New Port Project will be operational by the end of 2016. It will have an initial capacity of two million containers, rising to six million containers once the project is completed in 2020. The New Port will have different sections, including an economic zone, commercial port, and naval base. The project timetable had been brought forward from 2030 to 2020 in a bid to keep pace with Qatar’s other major infrastructure projects. Following recent international concern around migrant workers’ rights, the authorities stressed that the project has so far recorded 45m accident-free working hours among a workforce of up to 18,000.

UAE Consolidates its Position as a Global Transport Hub

24. Throughout the first half of 2014, the UAE’s major sea ports and airports witnessed growth in the movement of passengers and cargo shipments. Dubai International Airport (DXB) saw 34.6m passengers passing through, a 6.2% increase compared to the same period last year. Passenger traffic in Abu Dhabi international airport (AUH) increased by 19.4% to 9.5m during H1 2014 (year-on-year), compared to 6% in H1 2013 (year-on-year). London Heathrow was among the top five routes from Abu Dhabi International. As for cargo shipments through UAE ports, they went up by 14.1% year-on-year in Dubai (Jebel Ali port) and 37% year-on-year in Abu Dhabi (Mussafah, Khalifa and Zayed ports).

25. These increases reinforce forecasts of continuously strong non-oil economic growth, which is expected to reach 5.5% this year (2013: 5.4%). They are also spurring further expansion projects in each of the seven emirates. Abu Dhabi Airport is currently expanding its capacity to 40m passengers a year building a new Midfield Terminal Complex (MTC). Dubai is progressing swiftly with its project to expand capacity to 90m passengers a year and even some of the Northern Emirates (most notably Ras al-Khaima) recently announced plans to boost capacity at its airport. But all these plans have given rise to concerns around unnecessary duplication prompted by inter-Emirate rivalry, which in the long run could lead to under-utilisation of existing ports and airports.

INTERNATIONAL TRADE

Signature on Gas Transit Corridor Linking Oman with Iran, Turkmenistan and Uzbekistan...

26. In August, Oman signed an MOU with Iran, Turkmenistan and Uzbekistan on an international transit corridor between the four states. The four states agreed to the concept of a transit corridor in 2011. If built, the main item of trade would most likely be gas. Favourable terms on other goods would also apply, though the scope of what these would be, and how estimates for how much additional trade might be generated by the corridor remains unclear

...But Latest on Iranian Gas Import Deal Suggests Progress Likely to Slow

27. The Undersecretary of Oman’s Ministry of Oil and gas recently announced that Oman has not yet appointed a consultant to conduct a feasibility study for the pipeline from Iran, making the planned in service date of end 2017 seem rather optimistic.

Qatar Mining wins four mining concessions in Mali

28. Mali in July awarded four mining permits to Qatar Mining as it seeks to boost exploration to offset ageing mines. The IMF forecasts a steady decline in gold output from 2015 in Mali, Africa's third-largest gold producer after South Africa and Ghana. The permits are for greenfield projects in Tabako,

Mininko Nord, Netekoto, and Linguekoto. The agreement follows a meeting in June between Malian President Ibrahim Boubacar Keita and a visiting Qatari investment delegation. Qatar Mining also plans to take a share in a mining site in Mali that is already operational.

29. The award to Qatar Mining is in the context of the Mali government also in July revoking 130 licences, or about 30% of existing permits, as it completed an inventory of mining contracts first announced last year, with plans to renegotiate concessions that are not considered to be in the country's interests.

30. Qatar Mining was established four years ago to invest in mining and metals. In 2012, Qatar International, a joint venture by Qatar Steel and Qatar Mining, secured a deal to build, own and operate a $2bn steel plant in Algeria.