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GCC Economics Summary

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MACROECONOMICS

IMF Article IV Surveillance on Bahrain

1. The IMF Executive Board published its report following its Article IV consultations with Bahrain in June. Real GDP growth reached a five year high in 2013 of 5.3%. But this was driven more by increased oil output than by the non-hydrocarbon sector. Inflation at the end of 2013 was only 2.3% (despite a final quarter increase driven by the property market), and the credit offered by Bahrain's banks to private industry increased by 6.6%. Bahrain's fiscal position at the end of 2013 was better than the government had expected. The deficit reached only 4.3% of GDP. But this was still an increase from 3.2% in 2012, and Bahrain's fiscal break even oil price increased to $125pb. Bahrain's gross debt stood at 44% of GDP. There was moderate improvement in the Bahraini financial sector, with a decline in the proportion of non-performing loans, consolidation in the Islamic finance sector, and good capital adequacy ratios. Externally, Bahrain's current account surplus increased slightly between 2012 and 2013 from 7.2% to GDP to 7.8%.

2. The IMF Board recommendations included: a gradual re-targeting of subsidies towards those on lower incomes; preserving existing levels of capital spending and better control of current spending; speedier implementation of GCC-funded projects; and the introduction of a corporate income tax, and GCC-wide sales tax.

IMF Article IV Surveillance on the UAE

3. As with Bahrain, the IMF Executive Board released its Article IV report for the UAE for 2014. Real GDP growth in 2013 had increased to 5% (compared with 4.3 % in 2012) driven by tourism, hospitality, and the property market. Future growth would probably remain strong at around 4.8% this year and 4.5% in the medium term. Year-on-year headline inflation in March 2014 increased to 1.9 % (compared with 1%) last year (due to the recovering property market in Dubai where prices have risen by 30% since March 2013). The UAE's overall fiscal surplus declined to 6.5% of GDP at the end of 2013 from 8.9% of GDP in 2012, and the fiscal break even oil price rose to US$ 84 in 2013.

4. The IMF's macroeconomic outlook for the UAE economy was positive. Future growth will mostly be driven by the non-hydrocarbon economy. It is likely to grow by 5.5% in 2014 (vs. 3% growth for the oil economy) as confidence in the market improves on the back of recently announced mega projects (eg. those around EXPO 2020). The main risks were a sustained decline in oil prices, and global financial market volatility. The Fund encouraged the UAE Government to implement prudent macroeconomic policy to manage these risks. On domestic risks, the IMF supported further fiscal consolidation and suggested stronger measures to curb real-estate speculation in Dubai. Whilst the IMF acknowledged the positive steps Dubai had taken last year (eg. introduction of mortgage caps, issuance of guidelines for banks' lending to government-linked companies and doubling of registration fees), they recommended even stronger measures, eg. a differentiated system of fees focused on cash buyers with a quick turnaround. The IMF also stressed the importance of coordinating and prioritising mega-projects in the run-up to Expo 2020, as well as managing upcoming debt maturities of government-related entities (GREs).

Partial Funding Sign Off as Kuwaiti Budget for 2014/15 Remains Delayed

5. Ahead of parliamentary approval of the full state budget for FY 2014/15, the Budget and Final Accounts Committee has signed off final approval for budgets of independent public bodies. These cover many areas of social welfare but also include significant funds for the Public Authority for the Encouragement of Direct Investment, the Kuwait Investment Authority (including the latest allocation to the Fund for Future Generations), Kuwait Fund for Arab Economic Development and the first

budget for the new National Fund for the Development of Small and Medium Enterprises. Dr Mohammed al-Zuhair, Head of the SME Fund, recently visited London to discuss UK/Kuwait business development collaboration opportunities ahead of receiving this first tranche of development funds of $1.7bn.

ENERGY

Saudi Arabia and UAE Sign Renewable Energy Co-operation Agreement

6. Abu Dhabi based Masdar and Saudi KACARE (King `Abdullag Centre for Atomic and Renewable Energy) have signed an agreement to co-operate on the development of renewable energy, and green investment funds. Both Saudi Arabia and the UAE need to reduce their domestic oil consumption in order to maintain export levels (their main sources of government income). The Kingdom plans to spend around $109bn on 54GW of renewable generating capacity by 2032, and the UAE plans to spend $102bn to increase its renewable capacity by 2020. Masdar has already installed more than 1GW of renewable generating capacity in the UAE, and has multiple investments further afield. But the heat and dust of the desert climate in Saudi Arabia and the UAE means achieving the nameplate capacity on renewable investments challenging. Carefully directed joint research and development to overcome these challenges would exportable, and so could benefit local engineering companies, as well as government finances.

DIVERSIFICATION

New Public-Private Partnership Law in Kuwait

7. One week ahead of the summer recess, Kuwait's National Assembly passed the new Public Private Partnership (PPP) law. The law (a modified version of the 2008 Build-Operate-Transfer law) provides greater incentives for local and foreign investors to get involved in planned mega projects under the government's National Development Plan (for example, by increasing the duration of project management from 40 to 50 years). It also mandates for the establishment of a PPP higher committee with the authority to review bids, award projects and sign contracts, which should speed delivery.

BUSINESS ENVIRONMENT

Upgrades for the Emirati and Qatari Stock Markets Herald Changes in Foreign Ownership Laws

8. Equity index provider Morgan Stanley Capital International (MSCI) has upgraded the Emirati and Qatari stock markets from 'frontier' to 'emerging market' status. The reclassification is a vote of confidence by MSCI in the Emirati and Qatari economies, and a recognition of the progress both Gulf states have made towards improving their business environments. By way of comparison, MSCI also classes Brazil, China and India as 'emerging markets.' The change will tend to increase institutional investors' propensities to invest in the UAE and Qatar, and allow companies registered in both countries to tap into the c.$1.4tr of capital that is at present invested in 'emerging markets' globally. It might also encourage Emirati and Qatari firms to float, thus deepening the region's capital markets.

9. An immediate consequence of the re-classification has been moves by the Emirati and Qatari authorities to increase the proportion of foreign ownership allowed of companies listed on their exchanges. In Qatar the level of permitted foreign ownership was increased from 25% to 49% (though foreign investors had previously been allowed to own more than 25% with special permission). Furthermore, the definition of 'Qatari' ownership has been broadened to include investors from elsewhere in the GCC. The changes to Emirati regulations are yet to be confirmed.

More High Profile Convictions in Omani Corruption Trials

10. The ongoing corruption trials in Oman saw their highest profile case thus far in late May, when Muhammad al-Khusaibi, a former Minister of Commerce, was sentenced to three years in prison and a $2m fine. He was charged with offering a $1m bribe to win a contract for his company, Consolidated Contractors Company (CCC), at Muscat International Airport. The recipient of this bribe, Mohammed al-`Amri, a former Under-Secretary at the Ministry of Transport and current member of the State Council (the upper chamber of parliament appointed by the Sultan) was sentenced to three years in jail and a fine of $3.2m. Around twenty other cases are still working their way through the Omani legal system.

Omani Decision on Consumer Protection Postponed Following Public Uproar
ECONOMIC AID

Saudis Invest in Egyptian Housing...

11. Saudi Arabia has injected $124m into the bi-national Saudi-Egyptian Construction Company. The additional money is likely to be used for new middle income housing.

... and the Islamic Development Bank Approves a $750m Loan to Egypt

12. As part of celebrations to mark the 40th anniversary of the Jedda-based Islamic Development Bank, the Bank announced projects worth just over $750m to fund infrastructure in Egypt. The allocations include $642m million for electricity generation across the country, and $110 million for improved irrigation in Egyptian agricultural areas.