MENA Update:
Twin Shocks: COVID-19 and Plunging Oil Prices

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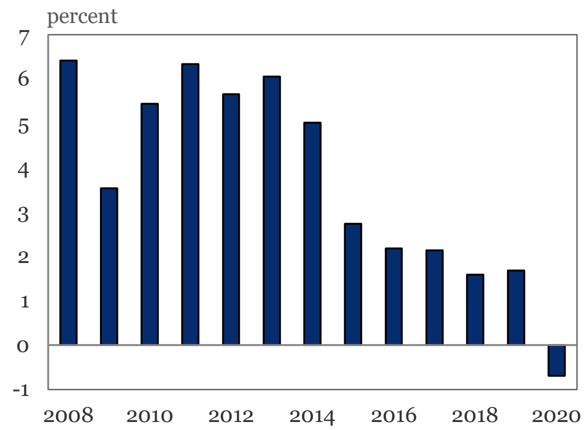
- Our MENA growth forecast now stands at -0.3 percent with additional downside risks.
- Uncertainty is high regarding the duration of the shutdown and the scope for an additional fall on oil prices.
- We project recessions in most oil exporters and the lowest growth in oil importers since the early 1990s.
- MENA's current account is set to shift from a surplus of $28 bn in 2019 to a deficit of $92 bn in 2020, ...
- ... with the fiscal deficit widening from 3.7% of GDP in 2019 to 8.8% in 2020.
- The fall in non-resident capital inflows will be more than offset by the drop in resident outflows.

Quarantines, disruption in supply chains, the crash in oil prices in light of the breakdown of OPEC+, travel restrictions, and business closings point to a recession in the MENA region, the first in three decades. Governments are trying to mitigate the economic damage with stimulus packages, but many are starting from a weak position. Central banks in the region have cut policy rates and announced plans to provide liquidity to financial institutions, particularly those lending to SMEs. MENA countries with limited fiscal space to ramp up public services and support affected sectors (including Algeria, Iraq, Bahrain, Oman, Lebanon and Tunisia) would face substantial pressure.

Hydrocarbon exporters in the region face an additional direct hit from the crash in oil prices. We downgraded non-oil growth in Saudi Arabia from 3% to 0.8%, and deepened the recessions in Algeria, Iraq, and Iran. We assume modest increases in oil production in Saudi Arabia, the UAE and Kuwait, leading to higher headline growth. The service sector activity will be hit the hardest as a result of containment efforts and social distancing. All exporters are likely to record large fiscal deficits due to the collapse in oil revenue, leading to a rise in public debt.

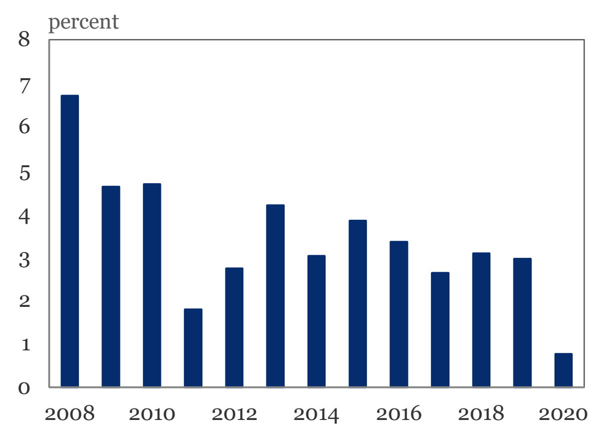
Based on our baseline scenario of an average oil price of $40/bbl, the nine MENA oil exporters would see a fall in hydrocarbon earnings in 2020 of $192 billion (11% of GDP). Consequently, the cumulative current account balance would shift from a surplus of $65 billion in 2019 to a deficit of $67 billion in 2020, and the fiscal deficit would widen from 2.9% of GDP to 9.1%. Unlike the previous four years, more than two-thirds of the financing need would be raised domestically and by tapping large financial buffers (particularly SWFs). Liquidity in banks could tighten as oil-related bank deposits decline, and NPLs could rise. Still, most GCC banks are well-positioned to absorb the shocks.

Exhibit 1: Real non-oil GDP in oil exporters is on track to contract by 0.6% in 2020.



Source: IIF

Exhibit 2: Real GDP growth in oil importers will likely fall below 1% in 2020.

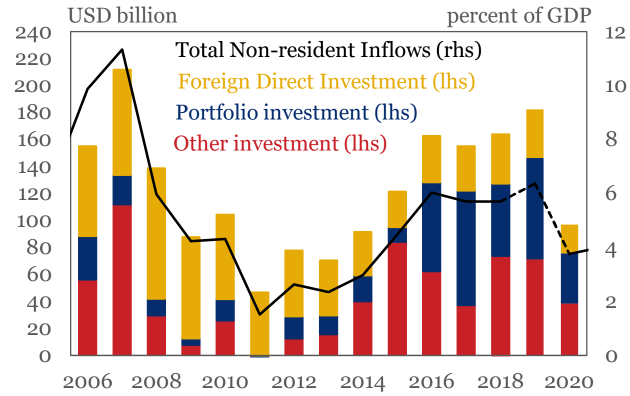


Source: IIF

We expect growth in MENA oil importers to decline by 2.4pps to 0.8% in 2020, the lowest since the early 1990s. The potential benefits of lower oil prices are unlikely to overcome the drag from dramatic limits on movement of people and goods within national borders to prevent unchecked spread of the virus, along with deep ties to oil exporters in the region as well as to economies elsewhere that are already seeing rapid contraction. A global recession will lead to a reduction in trade, foreign direct investment, tourism flows, and remittances to Egypt, Jordan, Morocco, and Lebanon. Egypt also stands to see a significant drop in Suez Canal transit revenue.

Non-resident capital flows to the MENA region are expected to decrease from $182 billion in 2019 to $101 billion in 2020, on the back of lower equity and debt flows. As in 2008 and 2009, resident outflows (mostly in the form of SWFs) will also decline sharply (from $215 in 2019 to $136 billion in 2020) reflecting the increasing need to tap SWFs to finance the large deficits. Nonetheless, official reserves are expected to drop by $120 billion (mostly in Saudi Arabia, Algeria, Iraq, and Iran). We also project a sharp decline in the cumulative SWFs of Kuwait, Qatar, and the UAE.

Exhibit 3: Non-resident flows to MENA are likely to fall markedly in 2020.



Source: IIF

Exhibit 4: Economic Fallout of COVID-19 and Plunge in Oil Prices, Real GDP Growth

	2016	2017	2018	2019	2020 old	2020 new
World	**2.7**	**3.2**	**3.1**	**2.6**	**2.6**	**-1.5**
Mature Markets	**1.6**	**2.2**	**2.2**	**1.6**	**1.5**	**-3.3**
Ow United States	1.6	2.2	2.9	2.3	2.0	-2.8
Euro Area	2.0	2.4	1.8	1.1	1.2	-4.7
Emerging Markets	**4.3**	**4.7**	**4.5**	**3.8**	**4.2**	**1.1**
EM excluding China	**3.0**	**3.4**	**3.2**	**2.3**	**3.1**	**0.0**
MENA	**3.8**	**0.7**	**1.3**	**0.8**	**1.8**	**-0.3**
GCC oil exporters	**2.4**	**-0.3**	**2.0**	**0.9**	**2.2**	**0.6**
Bahrain	3.5	3.8	1.7	1.5	2.0	-0.7
Kuwait	2.9	-4.7	1.2	0.3	2.8	0.8
Oman	5.1	0.3	1.8	0.7	2.5	0.2
Qatar	2.1	1.6	1.5	0.8	2.6	0.4
Saudi Arabia	1.7	-0.7	2.4	0.2	2.0	0.7
UAE	3.1	0.5	1.7	2.5	1.9	0.6
Non-GCC oil exporters	**9.3**	**1.3**	**-1.6**	**-1.6**	**-0.9**	**-3.8**
Algeria	3.2	1.3	1.4	0.3	1.6	-1.5
Iran	12.5	3.7	-4.6	-8.1	-5.1	-8.4
Iraq	10.2	-2.5	-0.6	3.4	3.2	-0.3
Oil importers	**3.3**	**2.6**	**3.1**	**3.0**	**3.2**	**0.8**
Egypt	4.3	2.7	5.3	5.6	5.4	2.7
Jordan	2.0	2.1	1.9	2.0	2.3	0.6
Lebanon	1.5	0.9	-1.9	-6.1	-5.2	-13.3
Morocco	1.1	4.2	3.0	2.7	3.2	1.1
Tunisia	1.3	1.8	2.5	1.7	2.5	0.5
Sudan	4.7	0.7	-2.4	-1.7	-0.8	-1.5
Memo: Brent oil prices, $ pb	45.0	54.8	71.5	64.2	60.0	40.0

Source: Haver, IIF

Exhibit 5: Policies Implemented to Limit the Economic Fallout of COVID-19 and Plunge in Oil Prices

	Total stimulus, thrust/repress, in % points of GDP	Central Bank	Government
Algeria	-2.5		The government is expected to cut public spending by 30% and delay state projects to cope with financial pressures. In this regard, the state-owned energy company (Sonatrach) will reduce planned investment by half.
Egypt	2.2	The CBE cut interest rates by 300bps and took actions to support households and businesses, such as the removal of fees on ATM withdrawals and e-payments. While the coronavirus outbreak is expected to hurt banks' profitability, asset quality and credit growth, the banking system is sound and should be able to withstand crisis.	The government increased wages and bonuses of public employees in the 2020/21 budget and increased the tax exemption ceiling to EGP 15,000, up from EGP 8,000, in addition to raising the personal exemption ceiling. The 2020/21 budget will also offer a new tax bracket of 2.5% for people with annual incomes below EGP 35,000, down from 10% previously. The government cut electricity and natural gas prices for heavy industry users, lowered tax on company dividends, and postponed the tax on property for factories and tourism companies by 3 months.
Morocco	1.2	The central bank cut the base rate by 25bps to 2.0% at its Mar 17 meeting. The rate cut takes place amid substantial economic risks stemming from unfavorable weather, which will weigh on agricultural output, and the global COVID-19 pandemic.	The King ordered the establishment of a USD 1bn fund (1% of GDP) to fight the COVID-19 pandemic. The fund will be targeted at upgrading the health infrastructure and supporting the economy, including the tourist sector. Part of the funds will be spent on job preservation.
Qatar	3.0	The central bank reduced the lending rate by 100bps to 2.50% and reduced the repurchase rate (repo) by 50bps to 1.00%. The central bank will also provide additional liquidity to local banks and set up a mechanism to encourage banks to postpone private sector loan repayments for six months.	The government announced a 3-year stimulus package in the amount of USD 20.6bn (12.5% of GDP) to the private sector to mitigate the effects of the spread of the coronavirus.
Saudi Arabia	1.0	SAMA cut its policy rate by 75bps and announced a private sector financing program of USD 13.3bn (1.9% of GDP). SAMA's program also includes deposits of $8 billion in banks to finance companies, provides for increased lending facilities to SMEs at concessional terms, and allows a delay in payments by SMEs for a period of six months.	The government cut non-priority spending (with least social and economic impact) allocated in the 2020 budget by 5%. Capital expenditures will be rationalized.
UAE	1.6	The central bank has cut its policy rate by 75bps, reduced the amount of capital banks have to hold for their loans to SMEs to 25%, and revised the existing limit for maximum exposure that banks can have to the real estate sector. The central bank also announced a $27.2bn Targeted Economic Support Scheme and other measures to reduce the economic effects of COVID-19. The scheme provides funding for banks to grant relief from principal and interest payments for up to six months on loans to the private sector.	The government announced a stimulus package of $34 billion (9% of GDP).

Source: IIF