

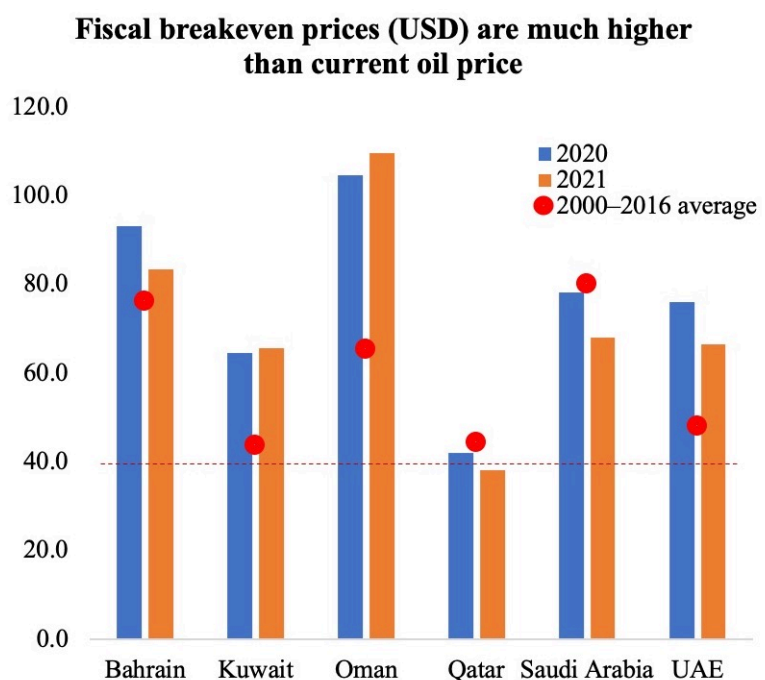
# Weekly Insights 4 Nov 2020: Rising budget deficits & debt levels in the Middle East/ GCC Require Sustained Fiscal Adjustment

Download a PDF copy of this week's insight piece [here](#).

As the world awaits results of the US election, oil prices have settled around the forty-dollar mark. Oil exporters in the region have had to deal with the Covid19 outbreak along with a global recession that have drastically reduced the demand for oil, as well as lower oil prices. Given the

resurgence in Covid19 cases and renewed lockdown measures and the global energy transition away from fossil fuels, it is unlikely that oil prices will revert to the levels seen a few years ago, given weaker demand – the IMF's latest World Economic Outlook puts oil prices, based on futures markets at USD 41.69 in 2020 and

USD 46.70 in 2021 (versus an average price of USD 61.39 last year). Fiscal breakeven oil prices in the GCC range between USD 42 for Qatar to USD 104.5 for Oman this year, exerting additional pressure on most oil producers as they ramp up



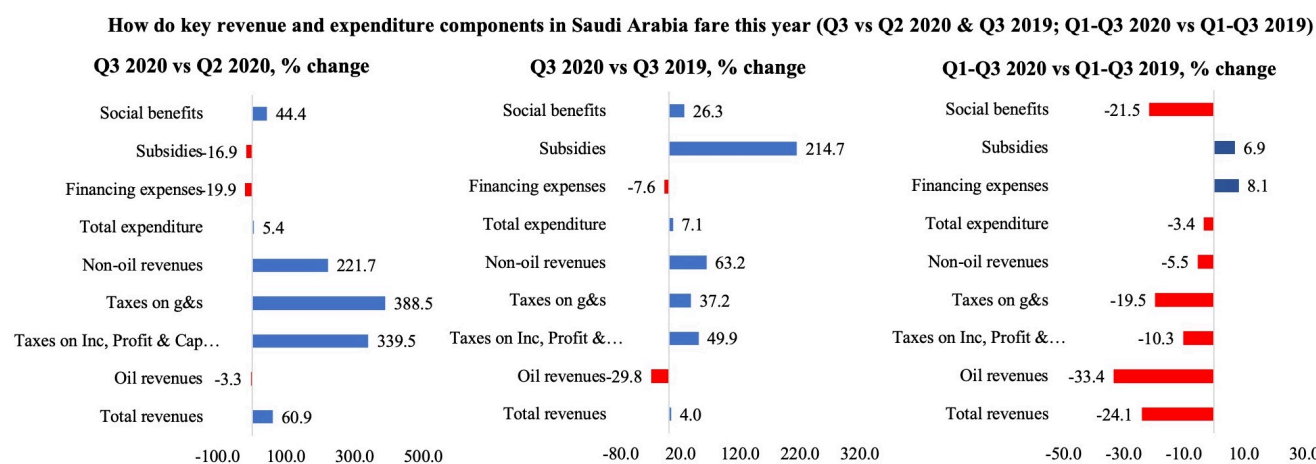
Source: IMF Regional Economic Outlook, Refinitiv, Nasser Saidi & Associates

Note: Kuwait's fiscal breakeven oil price is before the compulsory 10% revenue transfer to the Future Generations Fund including investment

spending to support the economy (UAE's emirates **Dubai** and **Sharjah** announced USD136Mn and USD139Mn respectively in additional stimulus in the last few days).

Oil exporters in the region are still highly dependent on oil revenues, with lower oil revenues implying limited fiscal room and higher fiscal deficits, which are averaging 10% in 2020 for the GCC countries. As real oil prices trend downward, fiscal sustainability becomes increasingly vulnerable.

The latest numbers from **Saudi Arabia** underscore the need to diversify away from dependence on oil revenues. Saudi Arabia managed to halve its fiscal deficit in Q3 compared to Q2, as overall revenues edged up by 4% yoy, thanks in part to the 63% surge in non-oil revenues (VAT rate was hiked to 15% From Jul onwards); however, spending increased by 7% yoy, driven by a massive surge in subsidies to SAR 8.2bn (From SAR 2.2bn a year ago) brought on by the need to support the economy during the Covid19 outbreak.

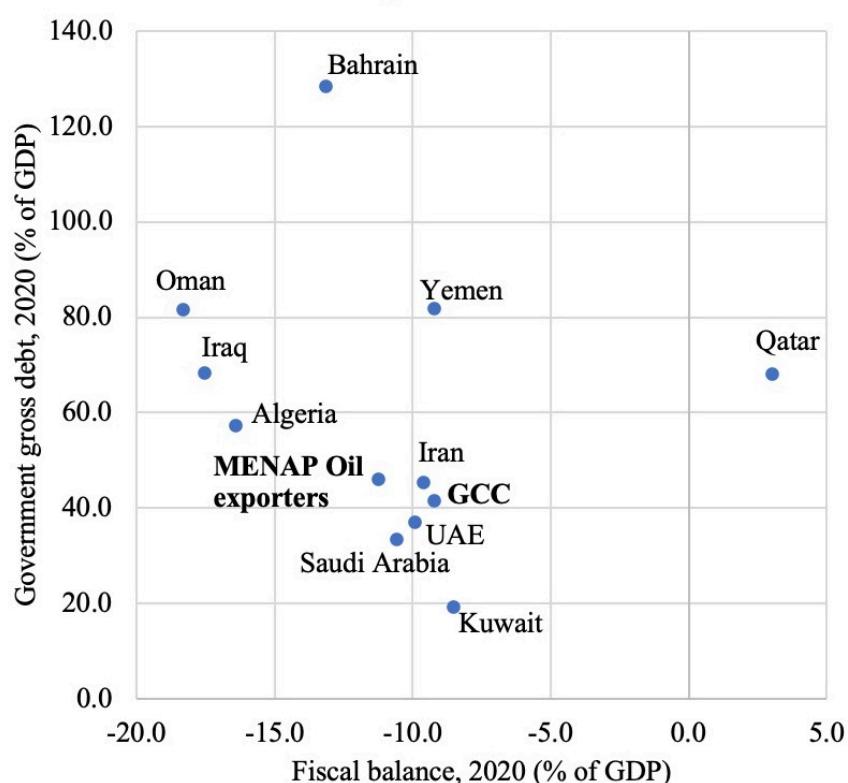


Source: Ministry of Finance, Saudi Arabia, Nasser Saidi & Associates

er GCC nations, **Oman**, in a bid to raise non-oil revenues, announced plans to introduce 5% VAT from next year, in addition to potentially introducing an **income tax** (currently being studied). Furthermore, costs of expatriates' employment visa and work permit renewals will be increased by 5%, with a plan to redirect additional funds towards financing its recently initiated Job Security System. **Kuwait** meanwhile is facing the highest budget deficit in its history<sup>[1]</sup>. In Aug this year, the national assembly approved a law that makes transfers to the Future Generations Fund dependent on budget

surplus, thus providing a much needed [\[2\]](#) but momentary respite. However, the Parliament is still holding the public debt law – which would allow the government to borrow KWD 20bn over 30 years – hostage. **Bahrain**’s deficit widened by 98% yoy in H1 this year (as oil revenues fell by 35% and overall revenues by 29%), leading it to issue a USD 1bn bond, while receiving a payment from its GCC neighbours (part of a support package approved in 2018).

**Rising debt burdens constrain spending capacities**



Source: IMF Regional Economic Outlook, Refinitiv, Nasser Saidi & Associates

Rising fiscal deficits following the previous decline in oil prices and lower growth have resulted in an accumulation of debt across all the MENA countries. The rising debt burdens and their servicing, leave limited space for increasing spending at a time when it is needed to support the economies. The IMF revealed that the median size of revenue and expenditure packages in the region’s **oil importing** countries this year was double that of oil exporters (2% of GDP versus 1% of GDP). For the GCC, adjustment has resulted from a combination of spending cuts, borrowing from commercial banks, tapping international/ regional markets (bond issuances [\[3\]](#), commercial loans) as well as drawing down from international reserves at the central banks and in Oman’s case direct external financial

support from Qatar (with talks ongoing with the UAE, reports FT). As for support from sovereign wealth funds, given lack of transparent data, it will be difficult to gauge the actual value of their support/ contribution, but their optimal role would be to: (a) tap into investments abroad (starting with sale of money market instruments like T-bills); (b) re-assess long-term investment strategies to play a larger role domestically in supporting local industries, innovation and developing digital assets.

Faced with a complex situation, it is little wonder that measures to increase non-oil revenue are being introduced – Oman’s plan to introduce VAT in 2021, rise in visa fees and a potential income tax on high income earners and Saudi Arabia’s VAT hike. To achieve and maintain fiscal sustainability in the long-run, oil exporters will need to move away from pro-cyclical policies, rationalise overly generous and unsustainable entitlement programs, alongside revenue-enhancing measures. The policy agenda is full in the coming years!

Expenditure reduction policies	Revenue enhancing measures	Other measures
Phase out subsidies Reduce current spending Reduce public sector wage bills	Raise non-oil fiscal revenues by raising taxes / introduce new taxes Improve efficiency in collecting taxes Consolidate/ rationalize fees/ charges on government services	Allow deficit financing / create local currency debt & mortgage markets Public investment towards infrastructure to ensure a steady pipeline Establish social safety nets / pensions scheme

[\[1\]](#) Kuwait posted a fiscal deficit of KWD 5.64bn in 2019-2020 (ending Mar 2020): this was higher by 69% yoy and inclusive of a KWD 1.72bn (10% of total annual revenues) transfer to the Future Generations Fund.

[\[2\]](#) The finance minister stated in Aug 2020 that the country has just KWD 2bn (USD 6.6bn) worth of liquidity in its Treasury and it was not enough to cover state salaries beyond

Oct.

[\[3\]](#) Abu Dhabi issued a USD 5bn multi-tranche bond; Dubai sold USD 2bn in bonds; Saudi Arabia sold USD 7bn in 3-part bonds; Qatar sold USD 10bn in USD-denominated bonds.

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## Weekly Insights 28 Oct 2020: US Presidential elections & impact on the Middle East/ GCC

Download a PDF copy of this week's insight piece [here](#).

FiveThirtyEight, in its extensive [analysis and simulations](#), favours Biden to win the election, barring a major polling error. A contested election is probably on the cards. But, with less than a week left for the US Presidential elections, what would a potential change of guard at the White House mean for the Middle East? Interestingly, a recent YouGov-Arab News survey shows that respondents have little confidence in either candidate: only 12% preferred Trump versus 40% for Biden.

First and foremost is a potential return to multilateralism and international cooperation from the current (unilateralism) policies of withdrawal from the Paris climate accord, the Trans-Pacific Partnership or the World Health Organization or the Iran nuclear deal. International, multilateral cooperation – such as the Global Access (COVAX) Facility – will be critical when effective Covid19 vaccines are available to be rolled out and need to be distributed globally. A discriminatory or preferential national treatment would be

detrimental to the global economy and recovery. More broadly, a US reversion to multilateralism would be welcomed internationally: less confrontation on trade/ tariffs and investment policies with China, the EU, Canada-Mexico and others would lead to a win-win globally and would lead to a cheaper dollar by encouraging non-US trade and investment.

Lower oil prices and a strong dollar along with US tariffs on aluminium and steel, have been strong headwinds and costly for the GCC. Currently, GCC members are pegged to the dollar (Kuwait pegs a basket dominated by US\$), oil is priced in dollars, financial assets are largely dollar denominated, trade is dollar denominated and dollar financing is popular, while bond issuances have been on the surge (taking advantage of globally low borrowing costs) as nations adjust to rising fiscal deficits. Given the Covid Great Lockdown, the energy transition away from fossil fuels, it is unlikely that oil prices will revert to prices seen a few years ago given weaker demand – the IMF's latest World Economic Outlook puts oil price, based on futures markets at USD 41.69 in 2020 and USD 46.70 in 2021 (versus an average price of USD 61.39 last year). But a cheaper dollar would support an economic recovery in the region driven by tourism and services exports, as countries reopen in phases.

More important, will be the impact on the oil market. A re-elected Trump administration would continue its policies supporting US shale oil, encourage drilling and roll back of climate-related regulations and support US oil & gas exports, weakening OPEC+ and oil prices. By contrast, a Biden Administration would be climate and environment policy friendly, revert back to the Paris Agreement, support renewable energy, including through "Green" and "Blue" New Deals. In a scenario where fossil fuel demand is already weak, an additional push towards renewables would tend to reduce US supply but also reduce demand, the oil price impact would depend on the balance between demand and supply effects.

Oil exporters in the region are still highly dependent on oil, with lower oil revenues implying limited fiscal room and

higher fiscal deficits which are averaging 10% in 2020 for the GCC countries. As real oil prices trend downward, fiscal sustainability becomes increasingly vulnerable. The elephant in the room remains the risk of being left with stranded assets. According to the IEA, stranded assets refer to “those investments which have already been made but which, at some time prior to the end of their economic life, are no longer able to earn an economic return”. The strategy imperative is the need to emphasise diversification policies, along with a policy to de-risk fuel assets. National oil companies and related state-owned enterprises, that are majority owners/operators of oil and gas assets, would need to pursue a low-carbon energy transition plan in addition to the privatisation of fossil fuel assets. Examples are the Aramco part-privatisation, and ADNOC’s part-pipeline privatisation. This should be complemented by a major drive to accelerate investment in and adoption of green/ clean energy policies by both government entities and the private sector.

The bottom line is that the outcome of the US elections will directly impact a host of global issues from dealing with Covid and climate change, de-escalating confrontation and preventing a Cold War with China, restoring confidence in multilateral agreements and institutions like the WHO, the WTO, the UN and geopolitics, with repercussions on regional power struggles involving Israel, Iran, Turkey and the Gulf states. Important as these issues are, the other bottom line is the need for a renewed focus of the GCC and the regions oil producers on economic diversification strategies and de-risking fossil fuel assets within a well-designed energy transition strategy.

*For additional views about this and the wider regional economic outlook, listen to the [IMF panel discussion from yesterday](#).*



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# Comments on Surviving the Covid-19 economic crisis in MEED, 24 Mar 2020

Dr. Nasser Saidi's comments appeared an article titled "Surviving the Covid-19 economic crisis" that appeared in MEED on 24th Mar 2020.

Comments from the article are posted below. The full article can be accessed [here](#).

*"It looks like the oil price war that is now launched is a strategic move by Saudi Arabia to weaken or destroy shale oil," says economist Nasser Saidi, founder and president of Nasser Saidi & Associates.*

*"It was bound to happen. There are two factors negatively effecting oil – renewables and shale. Shale was eating into the Opec plus share. They either wait and continue to lose market share or they act. They could choose now or later. They chose now."*

*"I estimate that because of the losses, the GCC needs to raise \$160bn-180bn in 2020 to maintain current spending deficits and provide financial support to some industries such as aviation," says Saidi.*

No significant announcements have been made about projects being delayed or cancelled in the region, but the projects sector will be significantly affected by cuts to capital spending. *"The likelihood is that many will be delayed or postponed," says Saidi. "And the net result is that structural adjustment, in terms of diversification, will be more difficult unless they bite the bullet and open up privatisation and public-private partnerships (PPPs). To me, this is the time to provide incentives."*