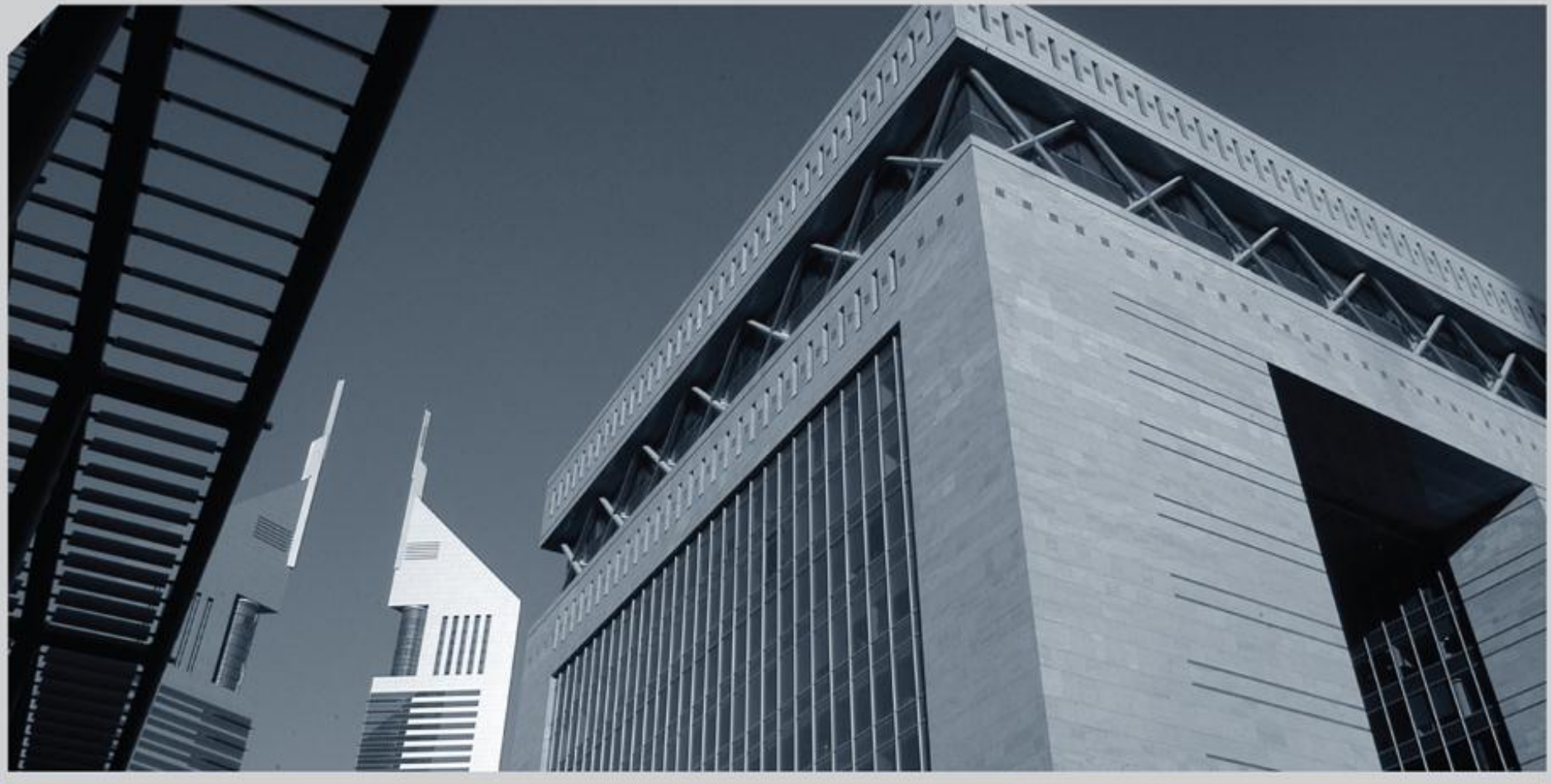


MENA: Turmoil, Infrastructure & Economic Integration

Power, Utilities, Infrastructure Finance & Investment MENA conference 4.10.11

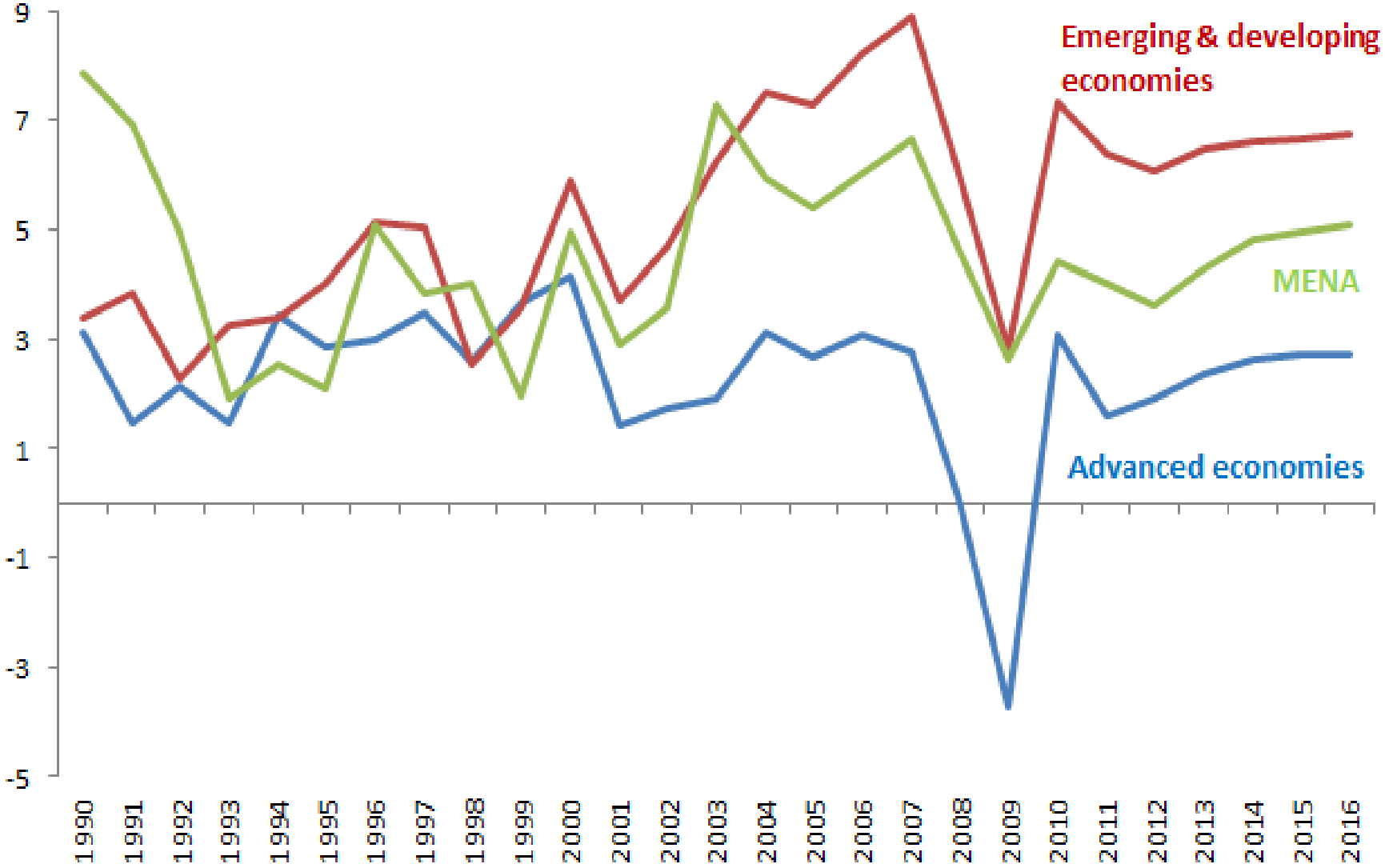
Dr. Nasser Saidi,
Chief Economist, DIFC

Dubai International Financial Centre

Agenda

- The “Arab Firestorm” & Impact of Political Instability
- Infrastructure & Regional Integration
- Renewable Energy Policies for a Sustainable Future
- Future perspective

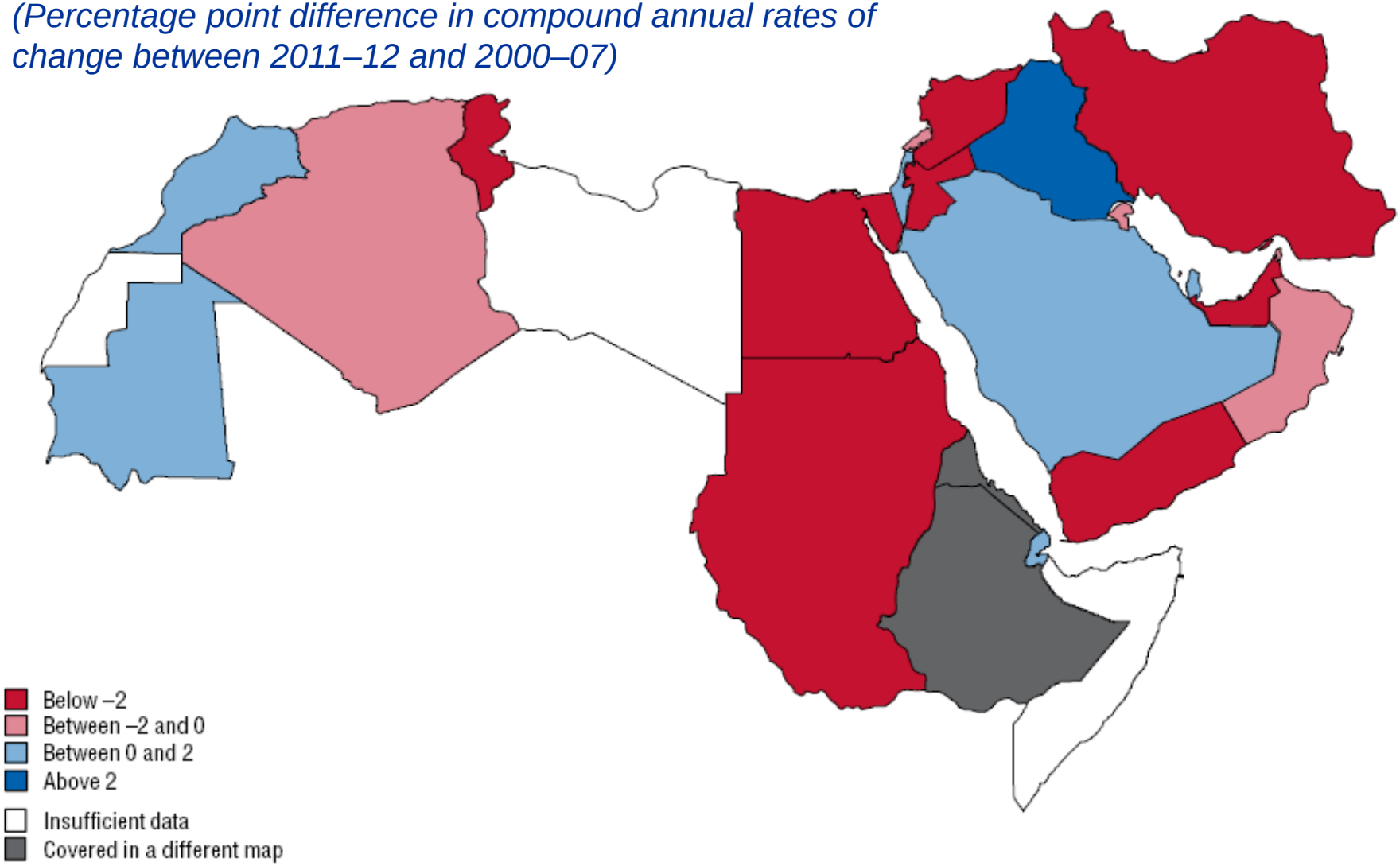
Increased Divergence in Economic Growth



Source: IMF World Economic Outlook, Sep 2011

MENA: Current Growth versus Pre-crisis Average

(Percentage point difference in compound annual rates of change between 2011–12 and 2000–07)



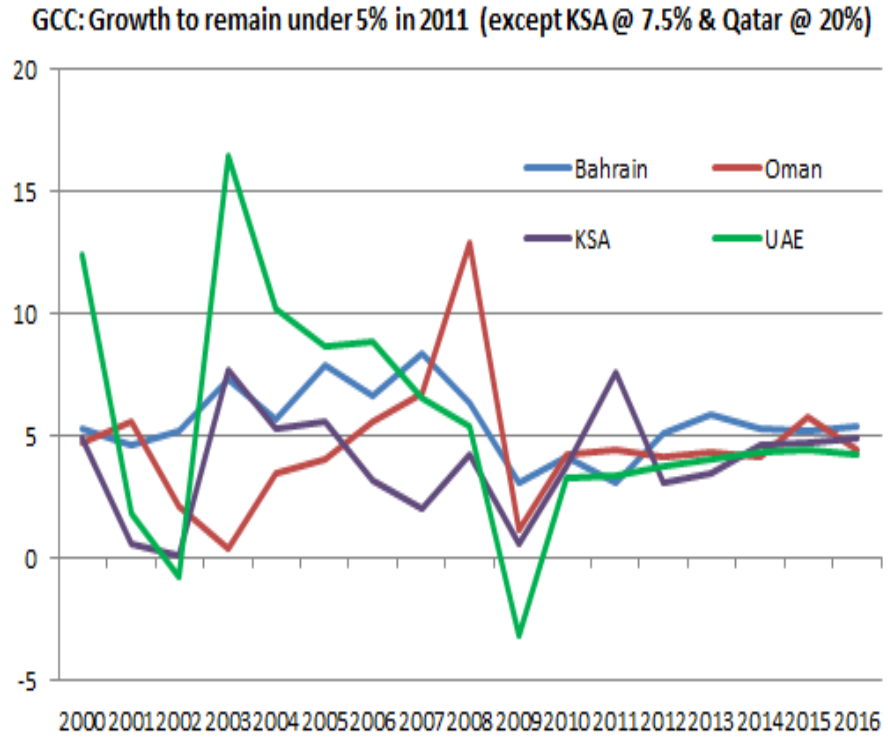
Source: IMF World Economic Outlook, Sep 2011

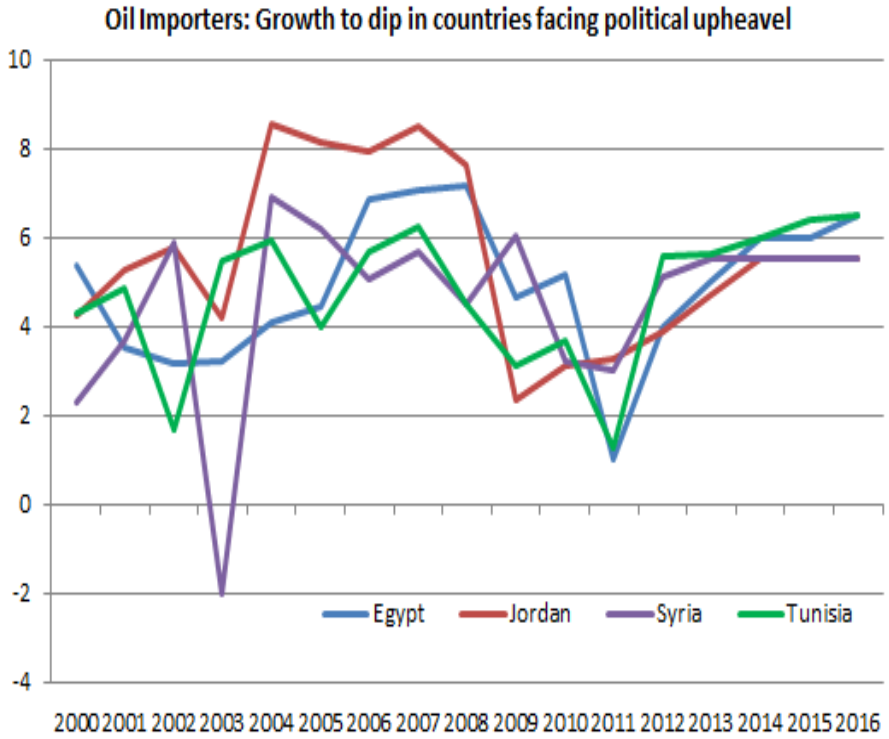
MENA Regional Turmoil: Disparate Outcomes

DIFC

Divergence b/n oil exporters, oil importers & labor exporters

- GCC growth - boosted by high oil output & prices; Bahrain's protests will impact growth in 2011 while in KSA, growth will be boosted by the populist fiscal measures.
- With private sector investment continuing to lag, government-supported consumption will remain the primary growth driver across the region.
- Downside risk remains that private sector activity will be subdued/crowded out.
- GCC announced that it has welcomed the bids of Jordan & Morocco to join the Union.



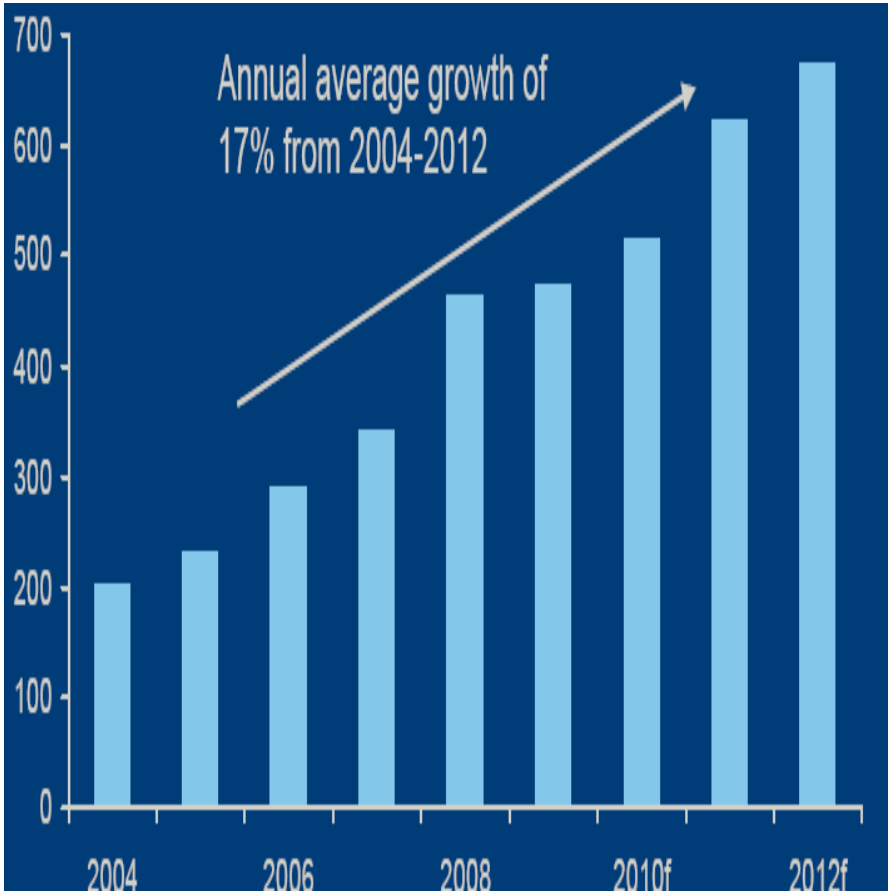


Source: IMF REO, Apr 2011

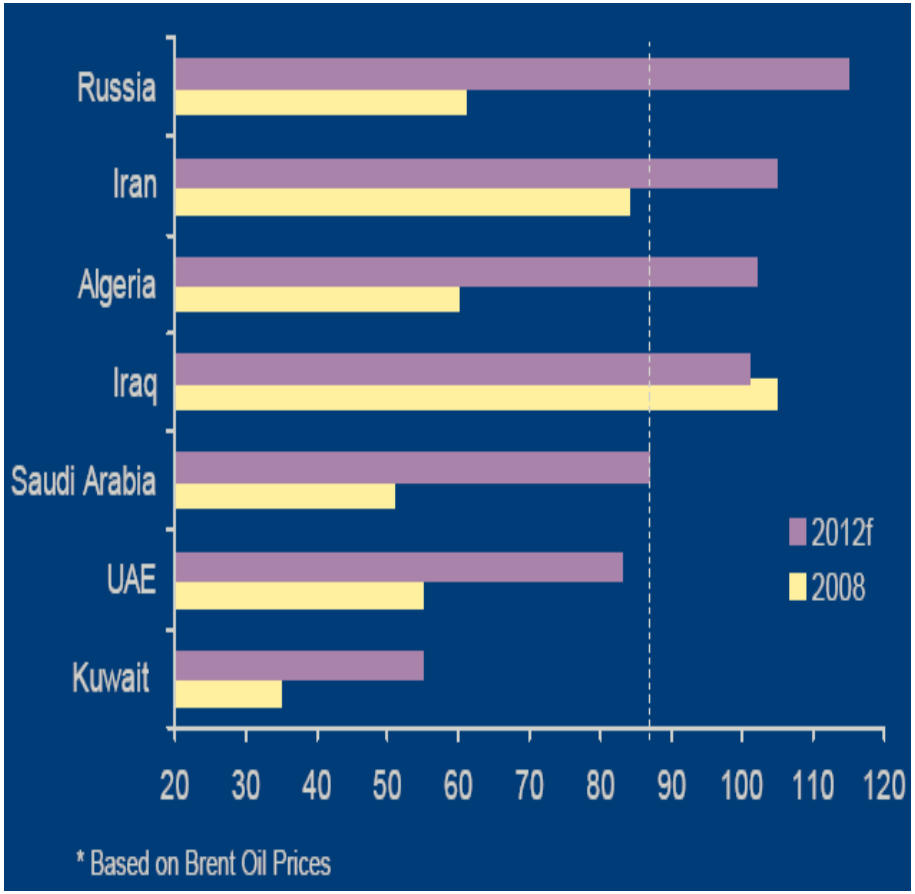
Government Spending & Fiscal Sustainability

Policy response has largely been populist spending encouraging consumption => Growing threat to fiscal sustainability & external balance

Oil exporters: Gov't spending ($bn)

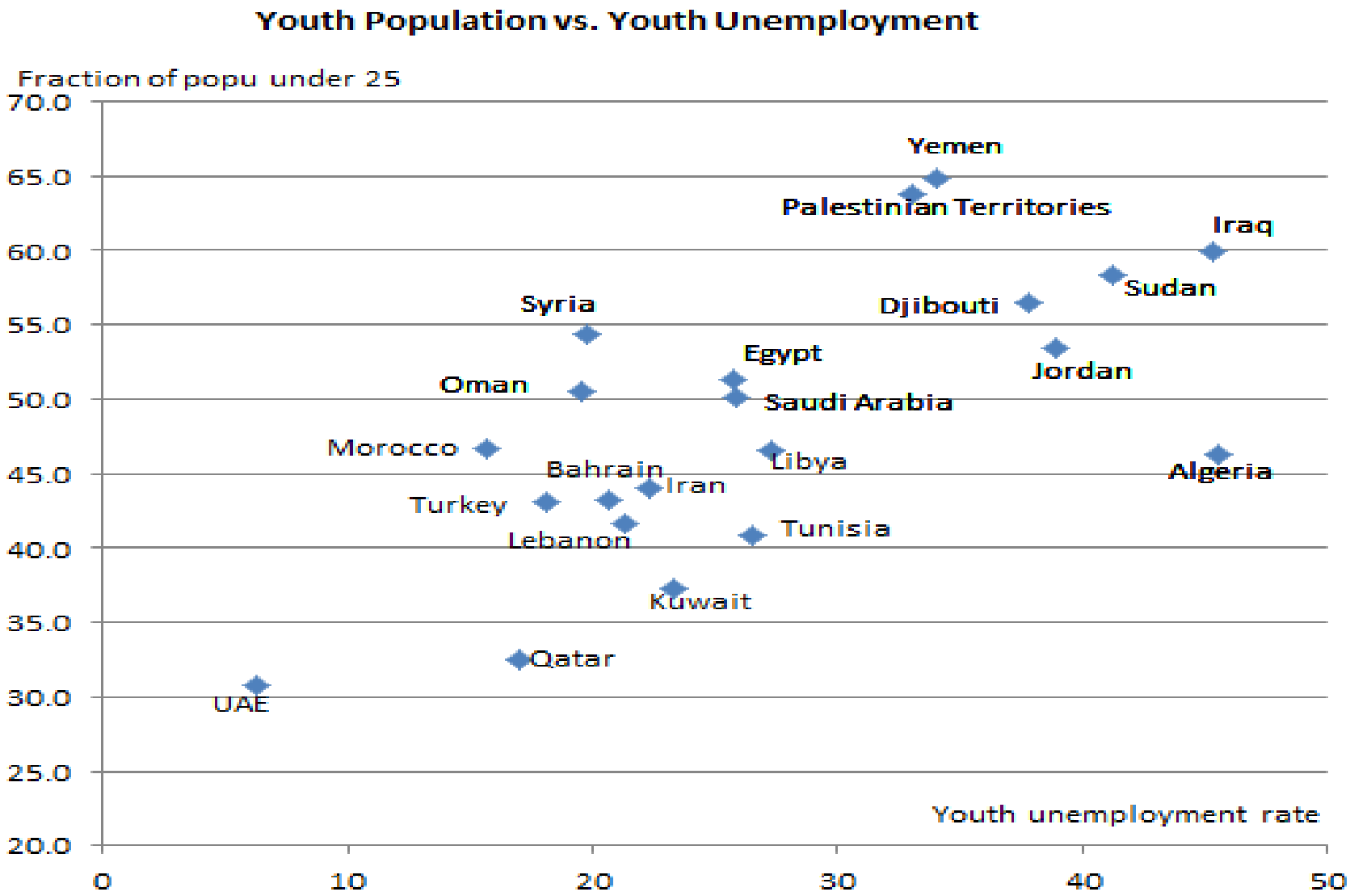


Breakeven Oil prices ($)



Source: IIF Annual Meetings, Sep 2011

Explosive Mix: Young & Unemployed Populations



Source: UN Population Division, DIFCA Economics

Recent MENA Regional Developments

DIFC

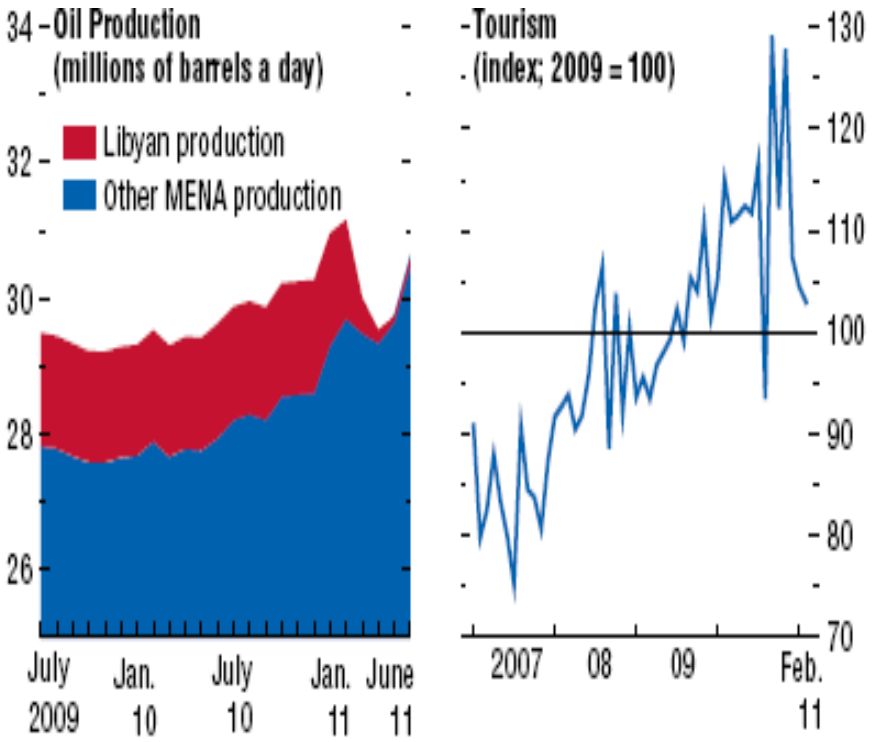
- Prior to recent events the **pace of economic activity** was set to continue to recover in the MENA region after the GFC & GR.
- MENA Growth is expected at 4.0% in 2011 compared to 4.4% in 2010 but with wide disparity in prospects between oil exporters & oil importers.
- Recent developments in the region highlight the need to ensure that economic growth is both ***inclusive*** and has a ***trickle-down*** impact.
- There is a need to **reduce chronically high unemployment and wide income inequality** within countries and across countries of the region.
- **Job creation is a priority** and this needs to come from the private sector for sustainable growth, innovation, economic diversification.
- Hence, there is a critical role for Family Owned Enterprises (FOEs) and Small & Medium Enterprises (SMEs) to engage in job creation and investment.
- While reinforcing the government sector has been the initial step, we should ensure it does not lead to a 'crowding out' of the private sector.
- Need to focus on: **structural reforms and developmental policies** (incl. infrastructure) that encourage private sector participation, tackle job creation and lift economies to higher growth trajectories over the longer term.

Bottomline: Middle East Economic Growth Outlook

DIFC

- Oil prices & stimulatory macroeconomic policies have helped growth
- Oil-exporters' growth is forecast to reach 5% in 2011 and about 4% in 2012: led by Qatar (natural gas exports), Iraq & Saudi Arabia.
- Lower tourism receipts, remittances, capital flows & investment interacting with high unemployment, growing social unrest & rising food prices to dampen growth prospects for oil importers
- Outlook for oil importers is much more subdued (especially for Egypt, Syria and Tunisia), with growth projected at 1.5% in 2011.
- Slow recovery in investment will raise oil importers' growth to 2.5% in 2012.

Need of the hour: fiscal consolidation + an inclusive medium-term growth agenda that establishes strong institutions to stimulate private sector activity, opens up greater access to economic opportunities and addresses chronically high unemployment, especially for youth.



Source: IMF World Economic Outlook, Sep 2011

Agenda

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- **Infrastructure & Regional Integration**
- Renewable Energy Policies for a Sustainable Future
- Future Perspective

Infrastructure + Logistics = Transform Economies

DIFC

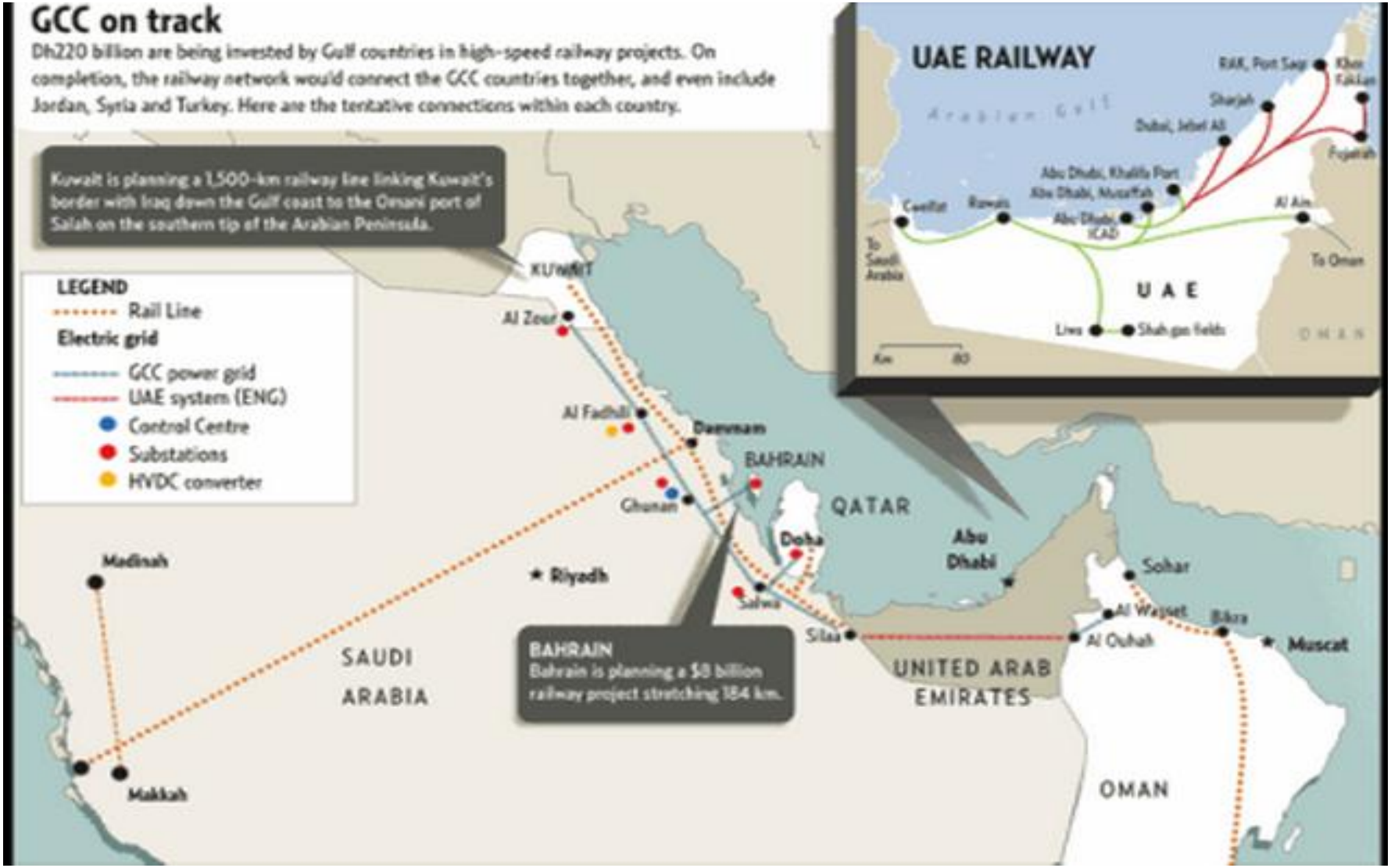
- The role of infrastructure in contributing to economic growth is well-documented
- Higher Infrastructure capital = Directly Productive + Increases productivity of private sector capital + Complementarity effects + Network Economies
- Investment in Infrastructure also:
  - **Improves productivity and returns on human capital investments** by improving health, longevity & quality of human capital
  - **Protects Environment** through waste management, water, sewage etc. with positive spillover effects on agriculture, tourism & overall quality of life
  - Generates **Network Economies** and Externality effects
  - Lowers Costs of Adjustment to structural changes and shocks
- Infrastructure + Logistics= Lower Cost of Doing Business
- Infrastructure + Logistics= Major determinants of Openness and Trade effectiveness

Untapped Potential of MENA Regional Integration

DIFC

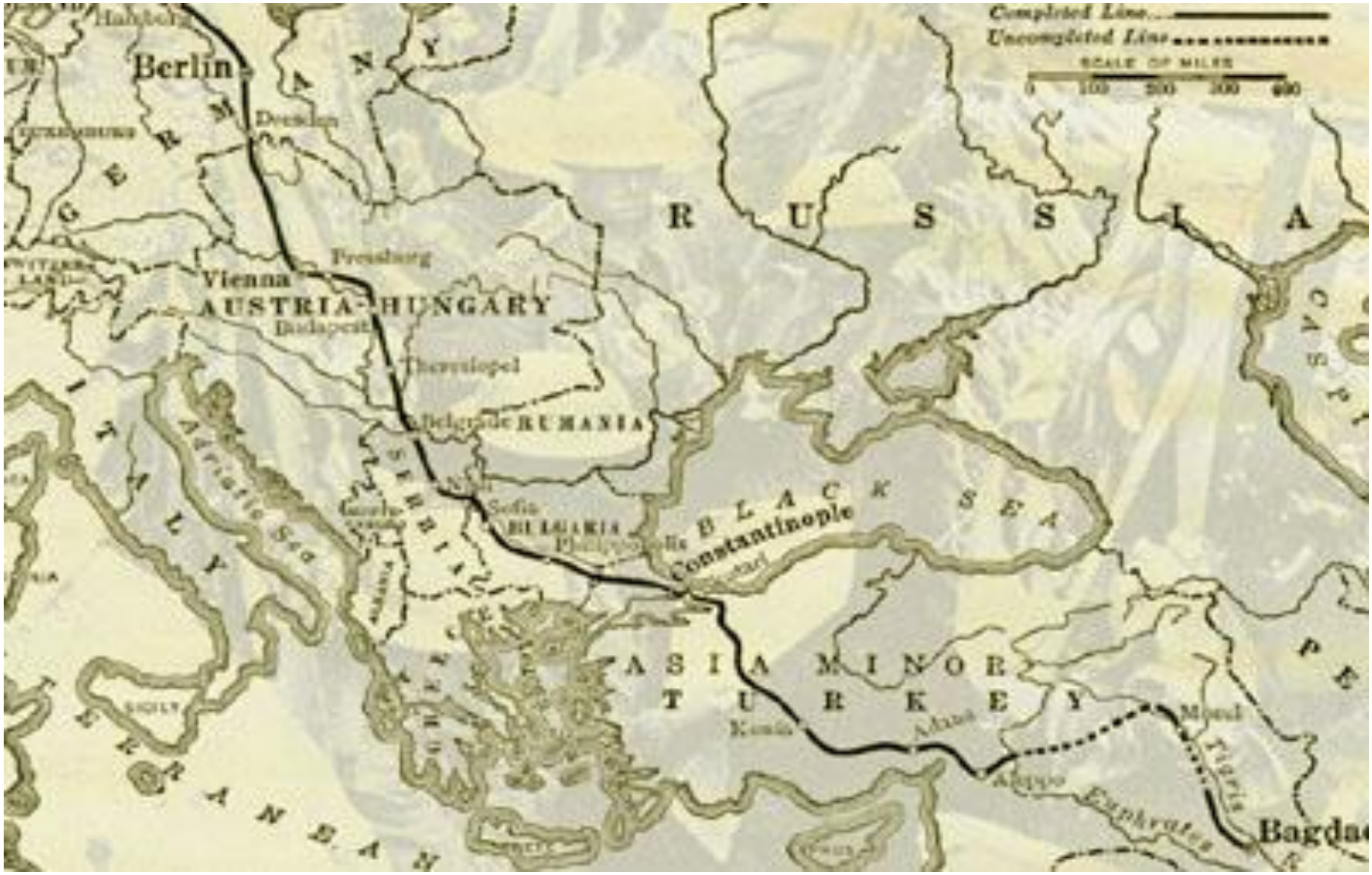
- Geography & proximity, density & intensity of traffic = **high returns to integrated infrastructure investments**: standards, policies, pricing, integrated network
- For the MENA region and particularly for GCC, the lessons are very clear - greater **regional economic integration** requires:
  - **Investment in Regional Infrastructure**:
    - **Transport:** rail, road, air
    - **Energy**: oil & gas pipelines, electricity
    - **Telecommunications & Infostructure** (broadband+)
    - **Payment Networks**: facilitate trade & markets payments & settlements
    - **Financial Market Infrastructure**: integrated capital markets
  - **Regional cooperation** on trade facilitation, streamlining & simplifying international trade procedures, customs and standards
- **Greater Regional Economic Integration / Network Economies:** Strategic & Economic interest of the GCC to invest in infrastructure & integrate non-GCC countries into its soft & hard infrastructure

GCC Infrastructure Integration

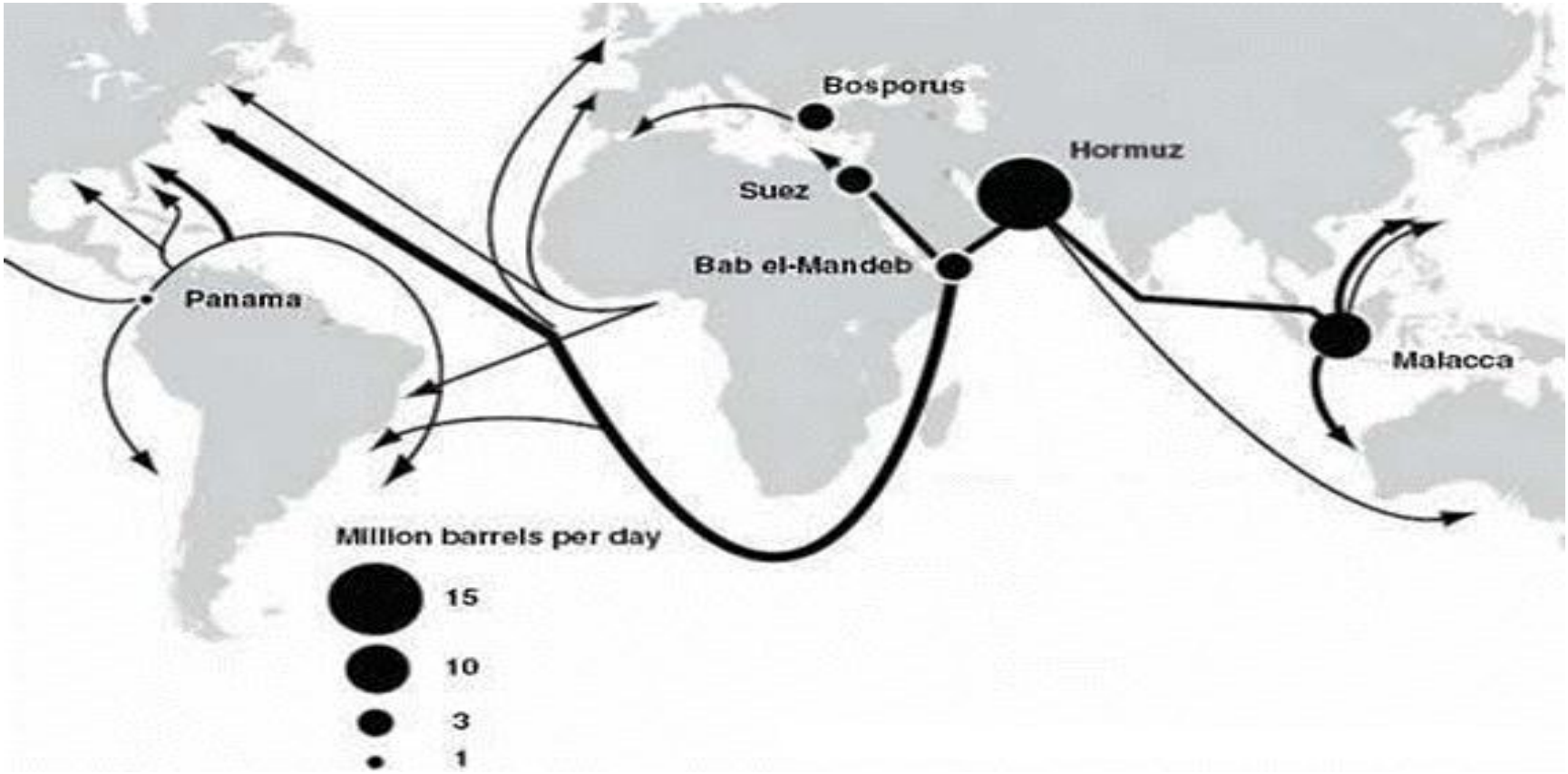


Source: Gulf News; http://goo.gl/NDIfB

Berlin to Baghdad Railway 1913



Maritime chokepoints critical to petroleum markets

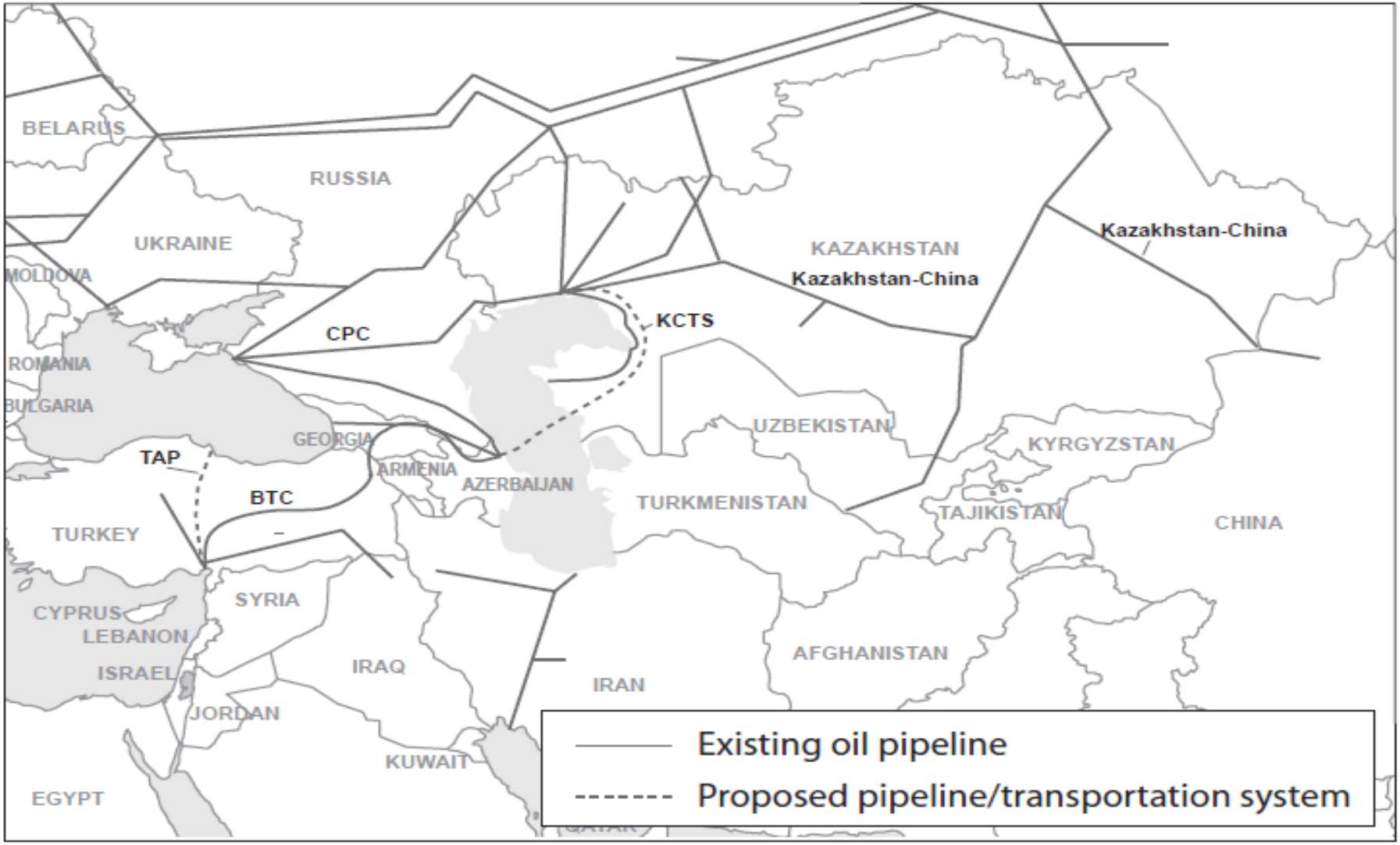


Source: EIA

Note: Circles represent millions of barrels per day transported through each chokepoint. Arrows represent common petroleum maritime routes

Maritime transit chokepoints are narrow channels along widely used global sea routes. Because about one half of the world's crude oil supply is moved by tankers on maritime shipping routes, world oil transit chokepoints are a critical part of global energy security.

Central Asia Oil pipelines: China's Growing Infrastructure



Source: Richard Jones, "The Politics of Central Asian and Caspian Energy"

Infrastructure Financing

DIFC

- Infrastructure investment is capital intensive, requires long gestation, has public goods dimension, with revenue generation subject to policy uncertainty => Higher risk
- Hence, bulk of financing has traditionally come from government or government owned companies such as public utilities.
- **MENA has Underinvested in Infrastructure: What is required?**
  - **Shift to Market Finance:** Develop local currency bond markets; housing finance
  - **Shift to Private Sector** via Privatisation and PPP projects: need to develop PPP framework of laws, regulations & regulatory agencies
  - **Shift to Institutional Investors:** SWFs investing in infrastructure has risen from 47% in 2010 to 61% at the beginning of 2011 (Preqin)
  - Role of IFIs & Development banks
- **A GCC/ MENA organization should be given the mandate to undertake regional projects**
- **<u>MENA needs a Bank for Reconstruction & Development</u>**

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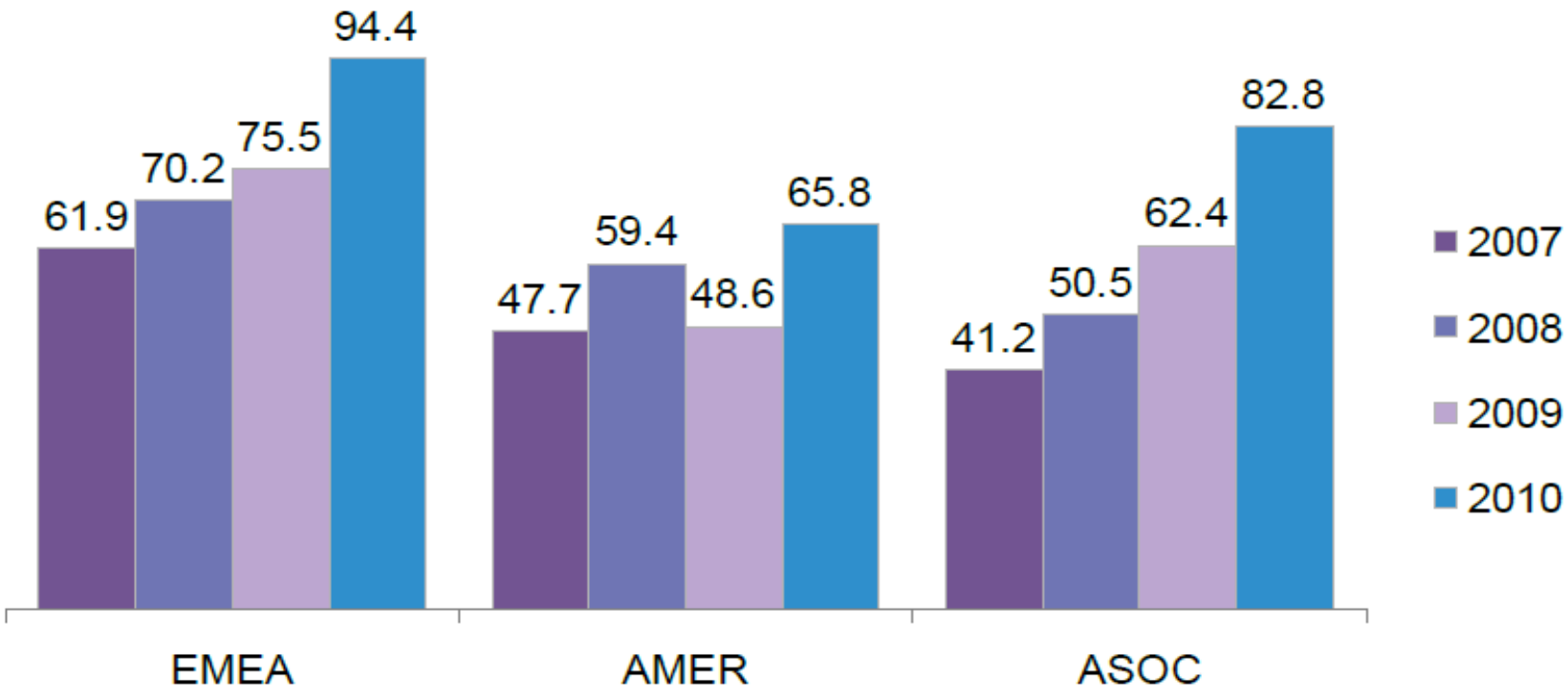
Clean Energy Investments by Region

DIFC

TOTAL NEW INVESTMENT IN CLEAN ENERGY BY REGION

2007–10 ($BN)

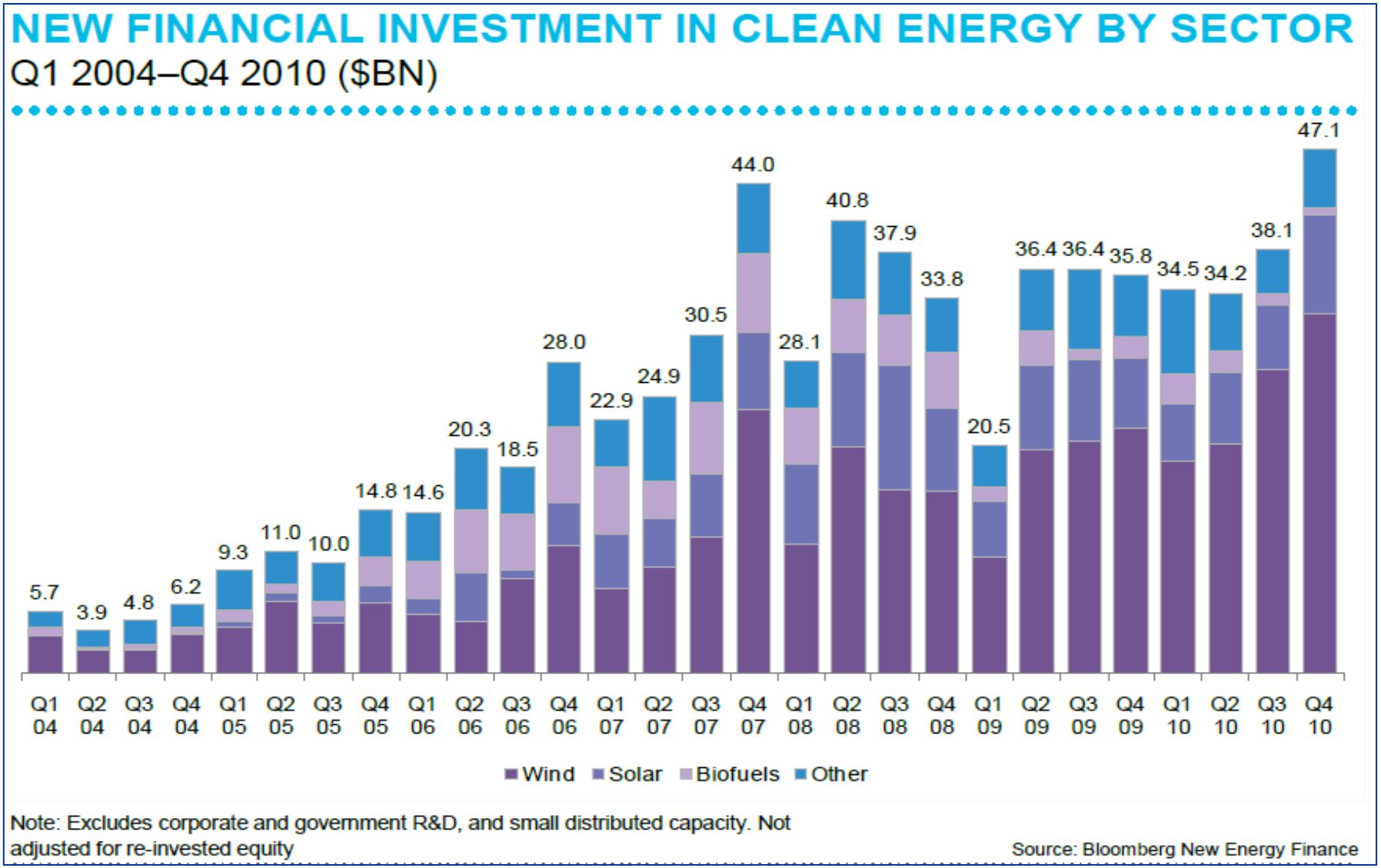
MENA' total new investment is estimated at $1.8 bn out of global share of $243 bn



Note: Includes corporate and government R&D, and small distributed capacity. Adjusted for re-invested equity. Does not include proceeds from acquisition transactions

Source: Bloomberg New Energy Finance

Clean Energy Investments by Sector



Renewable projects in MENA

- **United Arab Emirates** has a renewable energy target of 7% by 2020. The majority of this capacity is likely to be solar although there are also plans to develop some wind capacity as well. The country has also established a renewable energy agency **Masdar,** responsible for encouraging and developing projects within the country as well as overseeing investments in clean energy. Dubai, on the other hand aims to generate 5% of total power supply from alternative energy sources by 2030. It announced plans for the Gulf's first utility-scale solar plant.

- **Saudi Arabia** has not yet established a renewable energy target although a target of 10% of electricity consumption by 2020 has been provisionally mentioned by officials from Saudi Aramco. The government established the King Abdullah City for Atomic and Renewable Energy (KA-CARE) in 2010 to oversee all clean energy development in the country and it is expected to unveil a clean energy strategy before the close of 2011. Size of Saudi Arabia's energy market means that even a relatively low renewable energy target will result in considerable deployment of clean energy. Saudi Arabia also has the clearest fiscal incentives of the aforementioned countries to satisfy domestic energy consumption with sources other than its oil resources

Other renewable projects

- **Morocco** has a renewable energy target of 42% of total electricity capacity by 2020. This equates to roughly 2GW of solar, 2GW of wind, and 2GW of hydropower capacity. It is understood that the target will be met using the auctions and tenders mechanism. Prices will vary depending on each specific project.

- **Tunisia's** strategy is outlined in the Tunisian Solar Plan which is an initiative to commission 110MW of Solar Thermal Electricity Generation (STEG), 20MW of PV, 280MW of wind capacity by 2016, to be developed and financed by a combination of the private and public sectors. It also details a number of other initiatives including the construction of a PV manufacturing plant and a training and administrative centre.

- **Egypt** has a renewable energy target of 20% of electricity consumption to be developed from clean energy sources by 2020, of which 12% is to be from wind. This equates to around 7.2GW of wind energy – the government has also announced plans to develop 100MW PV project to add to the recently constructed Kuraymat STEG hybrid project.

Clean Energy Business Council

- An association of leading local and international organisations participating in MENA's emerging low carbon energy sector and clean technology.
- Unique in the region as a peak industry body for the clean energy sector and in its reach across the MENA region.
- An inclusive forum intended to harness the capacities of the private & public sectors at a local and regional level while benefiting from international knowledge, experience and best practices

"As developers, investors, and governments in MENA increasingly focus on low carbon energy solutions, an inclusive forum will help businesses and the public sector share ideas to promote effective policies and best practices."

Why CEBC..

- MENA has significant clean energy resources in solar, wind and CCS
- Growing populations and industry create significant demand for power generation
- Governments in the region are under pressure to meet that demand without increasing pollution or environmental impact, while fossil fuel subsidies are a growing burden on budgets and leading to consumption & production distortions
- Clean Energy sector is in the very early stages but is fast growing
- Given its climate and location region is becoming a centre for CE investment and trade, research and development
- It's also an emerging centre for international policy with the **IRENA HQ and the UAE"s MASDAR**
- R&D and investment opportunities abound

In this rapidly developing market, the private sector, through CEBC can help the governments of the region create a thriving sector.

CEBC membership

- CEBC is a membership based non-profit organization registered in the Masdar Free Zone in Abu Dhabi, UAE

- Members have access to technology based sub-committees, research and media networks, access to government and ability to influence government and policy development through a neutral forum

- Membership is currently 10,000 USD for Founding Members

- Companies can register their interest in becoming a Member of CEBC by visiting our website at www.cleanenergybusinesscouncil.com

- For more information email: info@cleanenergybusinesscouncil.com

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Middle East Economic Growth Outlook: Risks

DIFC

Upside Risks

- Stronger demand, particularly from China and other emerging markets, supports oil revenues, regional liquidity and capital inflows.
- Sufficient policy response in the EU, including delayed austerity in France and Germany and avoidance of a disorderly Greek (and other) default or exit, reduces the external demand slump.
- GCC government investment at home and in MENA, as well as multilateral bank support, offsets the lack of other capital and FDI.

Downside Risks

- Promised funds for North Africa and Jordan fail to materialize, or do so too slowly, putting pressure on domestic budgets and crowding out private investment.
- Insufficient reform and election delays reignite protests and strikes.
- Government spending keeps inflation high , weighing on consumption.
- A sovereign default crisis emanating from the Eurozone induces a major financial crisis and recession

Source: RGE MENA Outlook, Sep 2011

Future Perspective

- MENA is at historical crossroad & period of Transformation & Transition: Transition & its management will be critical to outcomes.
- Not a “Berlin Wall” Moment but Arab countries will need to ‘own’ their transformations and be “able to clean up their own backyard”
- International consequences: **oil price surge, increased energy insecurity & risk aversion** in financial markets.
- New **Energy Transport Infrastructure** is changing Energy Geography & Geo-Strategic importance of Marine Chokepoints
- MENA/GCC will increasingly **focus investments in Renewable Energy & Technology**
- Investment in Infrastructure is necessary for greater Regional Economic Integration
- Addressing vulnerability underlines the importance of **job creation, lowering income disparities, investing in infrastructure** and **promoting growth & development through institutional rebuilding** through a **MENA Bank for Reconstruction and Development.**


Thank You!
DIFC | Dubai International Financial Centre