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GCC
An Overview on Economic Trends

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6th Annual Conference on Trade Treasury and Cash Management in the Middle East

Dubai, 12 March 2008

Sub-Prime Blues or De-linking?

- **Investment, Infrastructure & Productivity**
- **Demographics, Migration & Remittances**
- **GCC: Structural Change & Drivers of Economic Growth**
- **Liquidity, Markets & Volatility**
- **Prospects & Challenge of Financial Markets**

A ME/GCC Economic & Financial Renaissance

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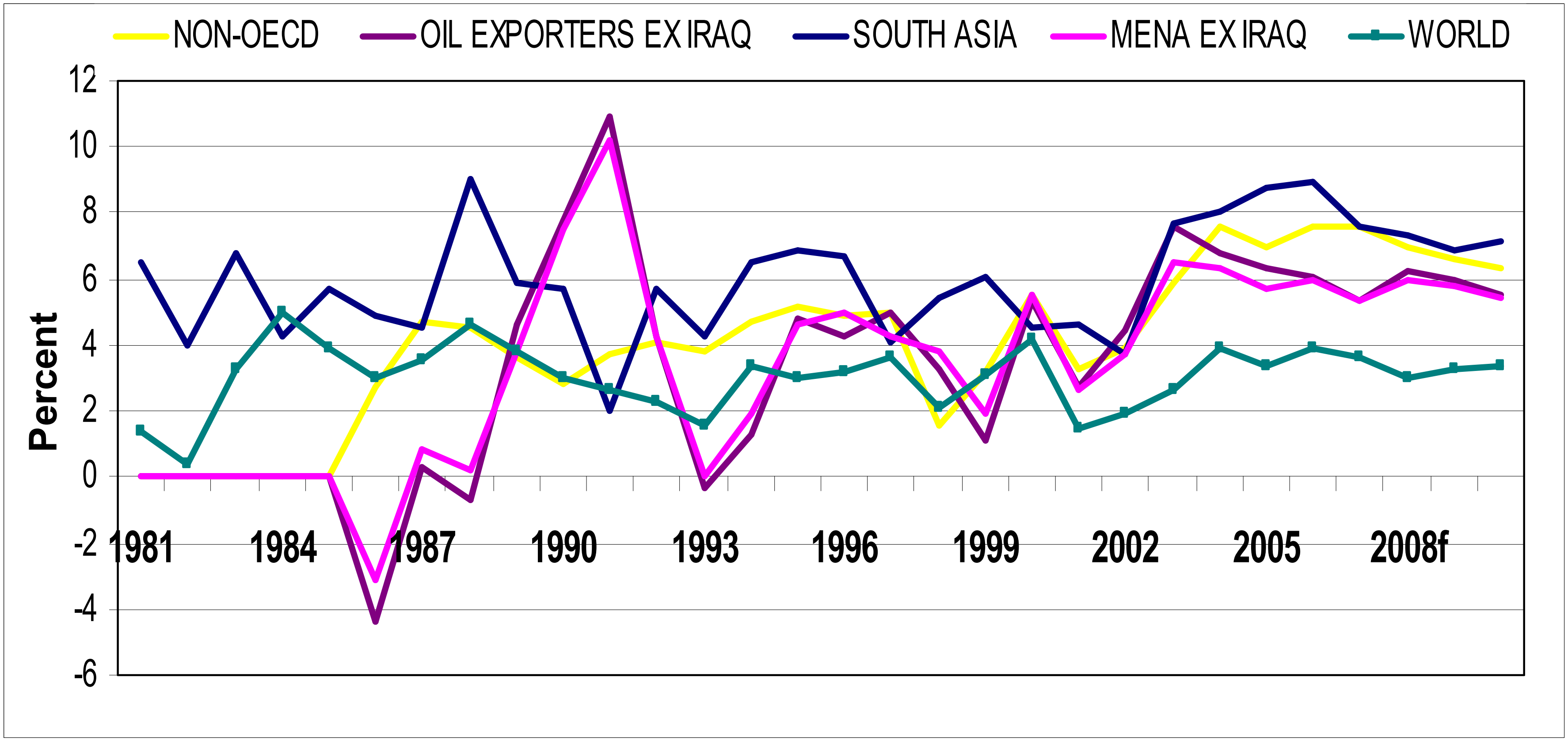
- MENA has achieved above trend economic growth rates:
  - Average real GDP growth 6.2% over 2004-2007 vs. 3.7% in 1998-2002
  - Growth resurgence has been investment led with increased infrastructure investment leading to ↑ in absorptive capacity and ↑ in productivity growth
  - Sustained by strong global growth led by Emerging Markets
- Private sector is leading and driving regional economic integration of markets, FDI, Tourism, labor flows
- Emergence of multinationals: DP, Etisalat, Emaar, MTC…
- Infrastructure investments with an estimated value in excess of USD 1.7 trillion are currently under development or planned in the GCC alone.
- Oil export receipts reached $381bn in 2007, up 8% from 2006
- Positive demographics & migration sustaining labour & output growth

Real GDP Growth: Actual & Forecast

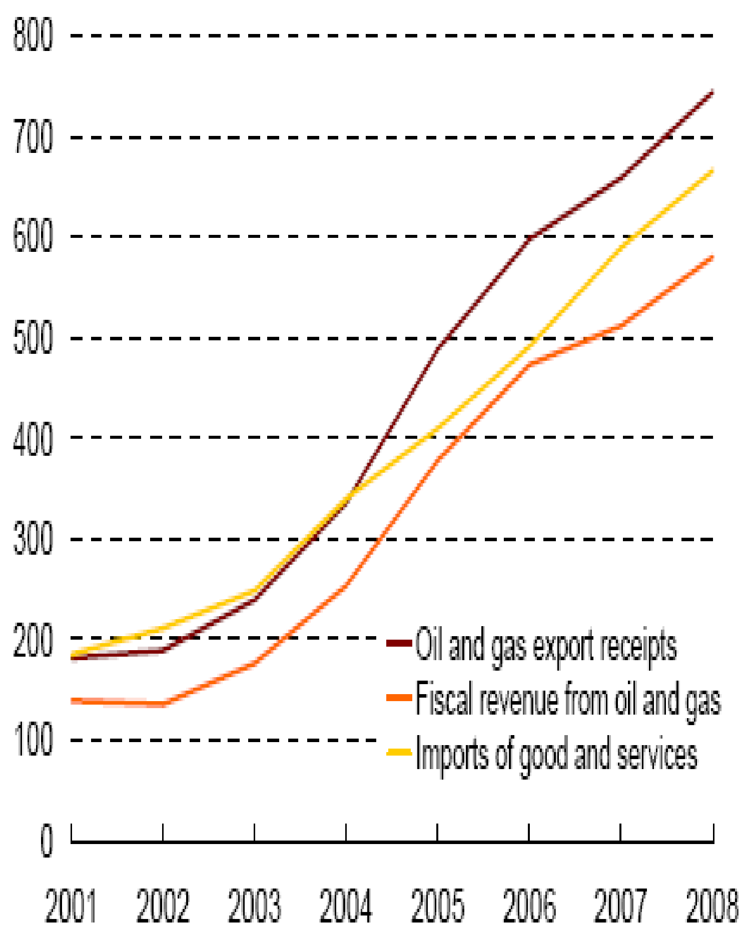


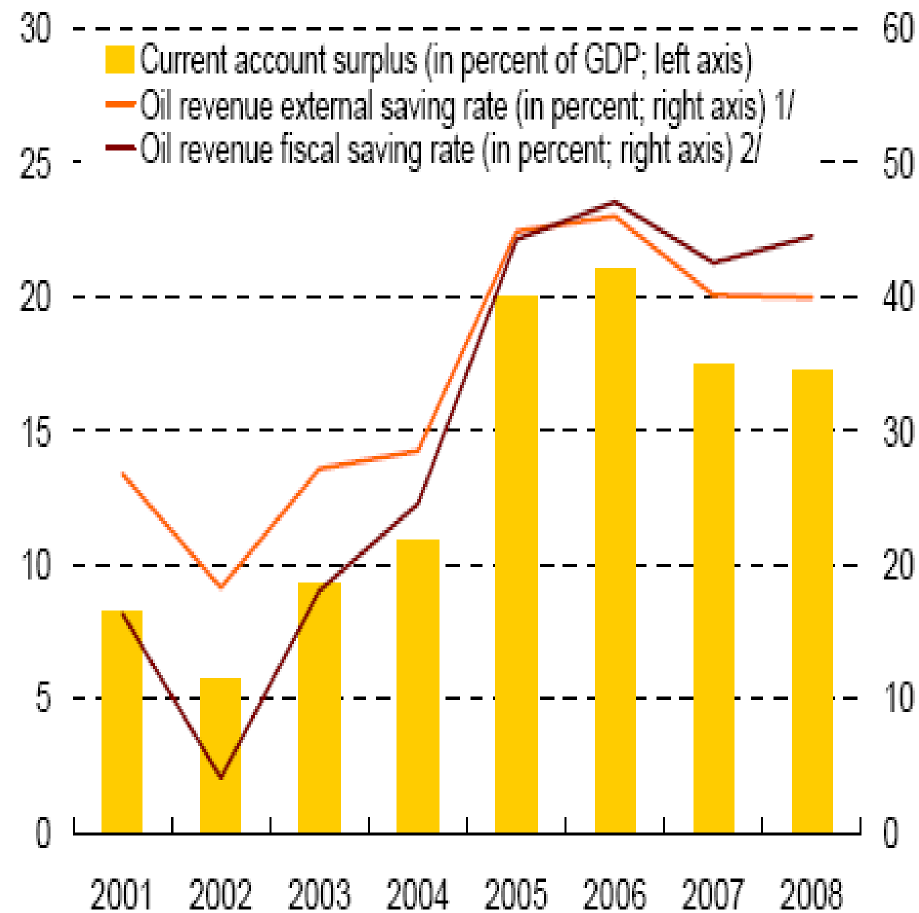
- ***Real GDP growth has been strong across the Middle East with emerging market countries in South Asia to continue to lead the way.***

Source: EIU, February 2008

Oil and Gas Exports

Region's oil and gas exports receipts look set to rise to near $800 billion in 2008 with current account surpluses running at 20-25% of GDP.

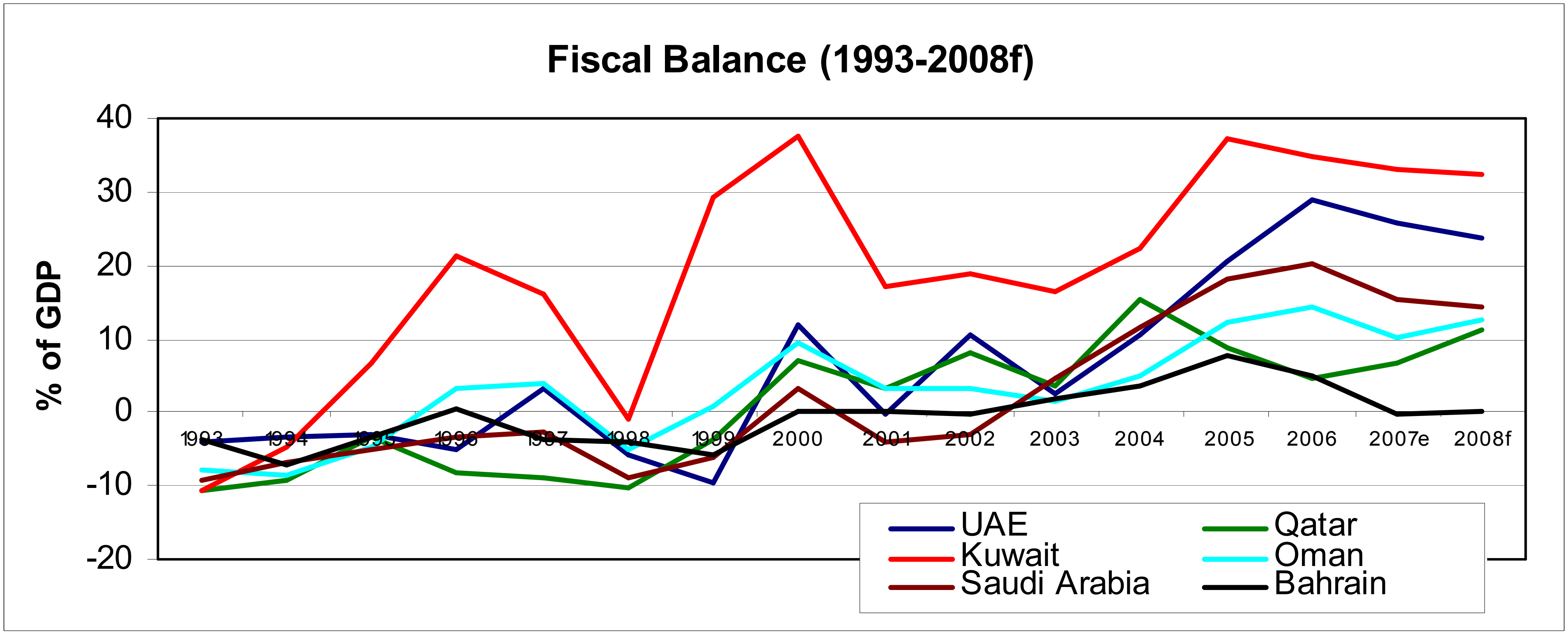




Source: IMF, REO October 2007

Large Fiscal Surpluses

- Oil producers policy reaction has been fiscally conservative: 60% of higher oil revenues have been saved.
- Substantial fiscal surpluses (19% of GDP in 2007) even as spending has picked up
- Fiscal position of GCC remains in surplus for an oil price in the range of $35-$38
- Investment policies less dependent on oil revenues

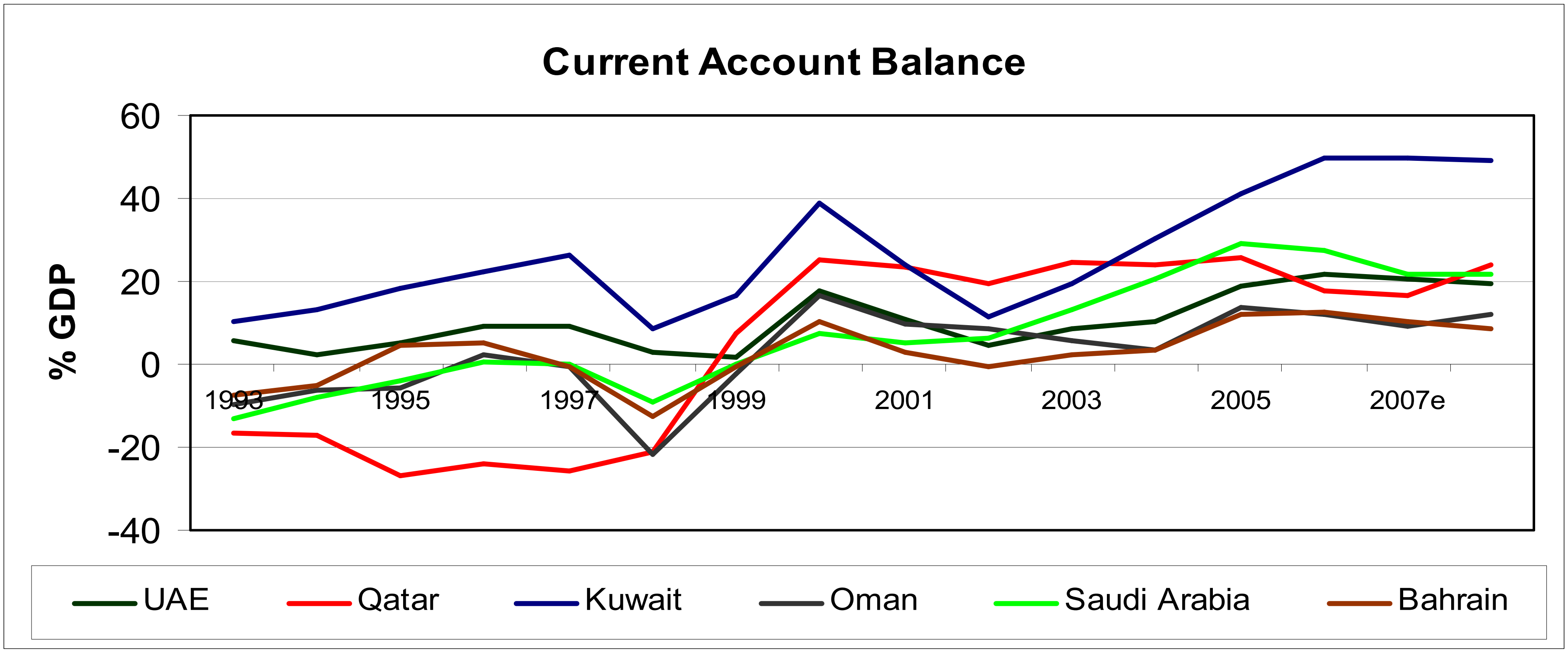


Source: IIF

Current Account Surpluses and Build Up of Foreign Assets

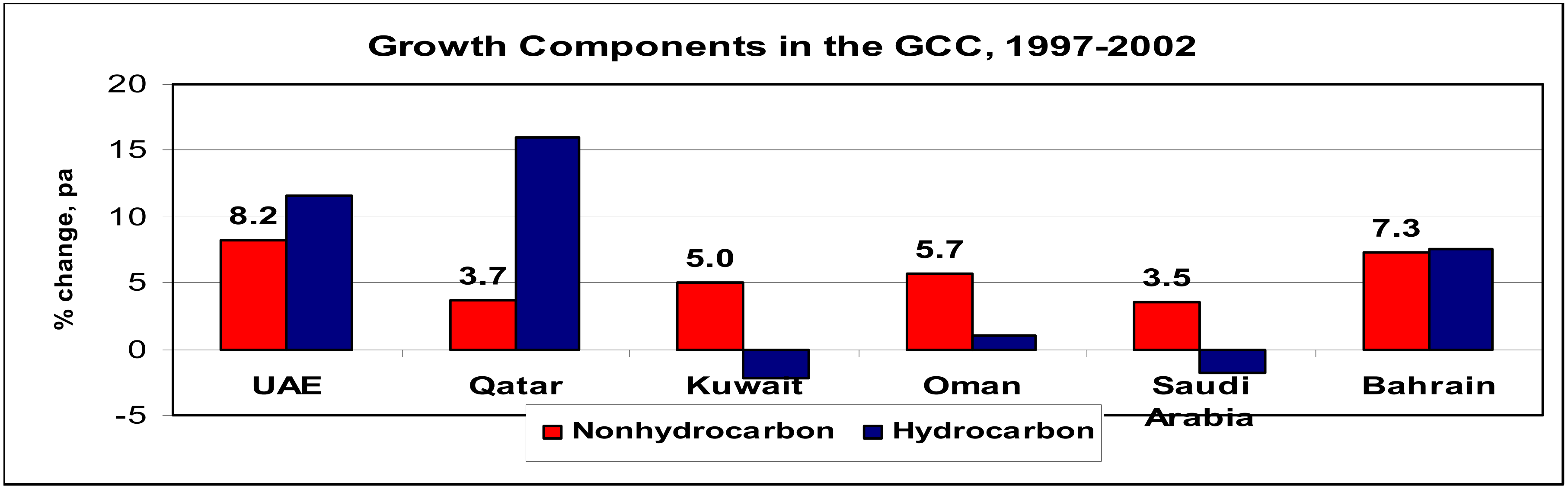
- **Current account surpluses running at 25-30% of GDP; increased recycling back into regional economies**

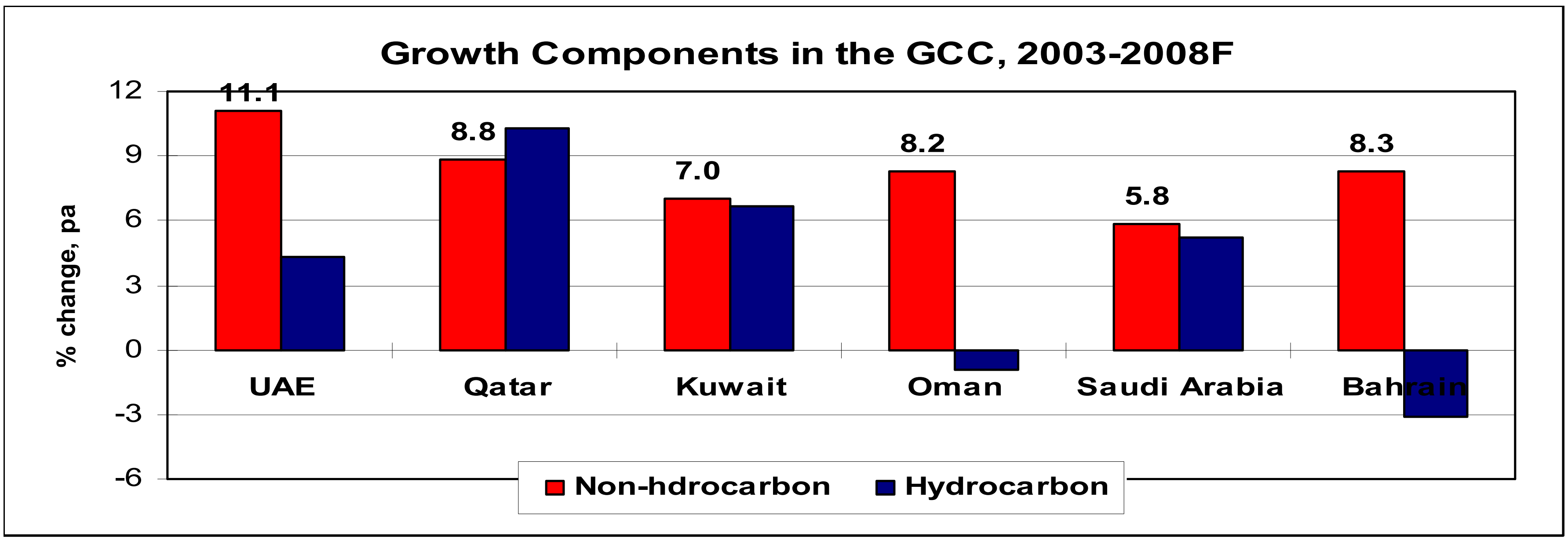
- **MENA international reserves have tripled between 2003 and 2007: $242.9bn (2003) to $776.6bn (2007) and forecast at $967.5 billion for 2008.**
- **For GCC international reserves have quadrupled from $90.5 (2003) to $365 (2007) and forecast at $ $455 billion by 2008.**



Source: IIF

GCC Increasingly Diversified





Source: IIF

A GCC Growth Resurgence and Economic Renaissance

- **MENA international reserves have tripled between 2003 and 2007: $242.9bn (2003) to $776.6bn (2007) and forecast at $967.5 billion for 2008. For GCC international reserves have quadrupled from $90.5 (2003) to $365 (2007) and forecast at $ $455 billion by 2008**
- **Fiscal Policy:**
  - **Oil producers policy reaction has been fiscally conservative: 60% of higher oil revenues have been saved**
  - **Substantial fiscal surpluses (19% of GDP in 2007) even as spending has picked up..**
- **Current account surpluses running at 25-30% of GDP much of which is being recycled back into regional economies**
- **Surge in Shari'aa compliant banking & finance**

Investment, Infrastructure & New Linkages

- Forecast EM infrastructure investment: Asia 67% of total, with China and India 43% and 13% of total; Russia 10%; Brazil 5%, Middle East 5%

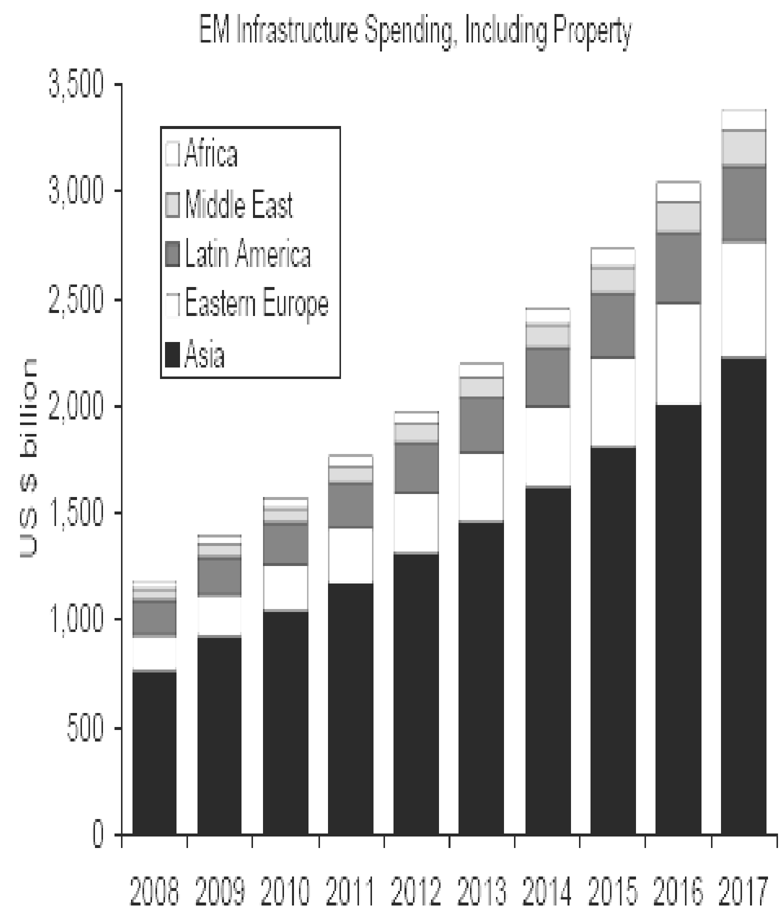
Infrastructure drivers:

- Demographics
- Urbanisation
- Policy reforms, Increased openness and move to market-based economies

Infrastructure investment will:

- Increase productive capacity and export capacity through improved logistics
- Enable economic diversification
- Underlie economic development and higher growth
- Lead to higher total factor productivity (TFP) and labour productivity growth
- Underpin growth of financial markets

US$21.7 trillion in EM Infrastructure Spending: 2008-17e



Source: World Bank, Global Insight, Morgan Stanley Research estimates

Infrastructure investments with an estimated value in excess of USD 1.7 trillion are currently under development or planned

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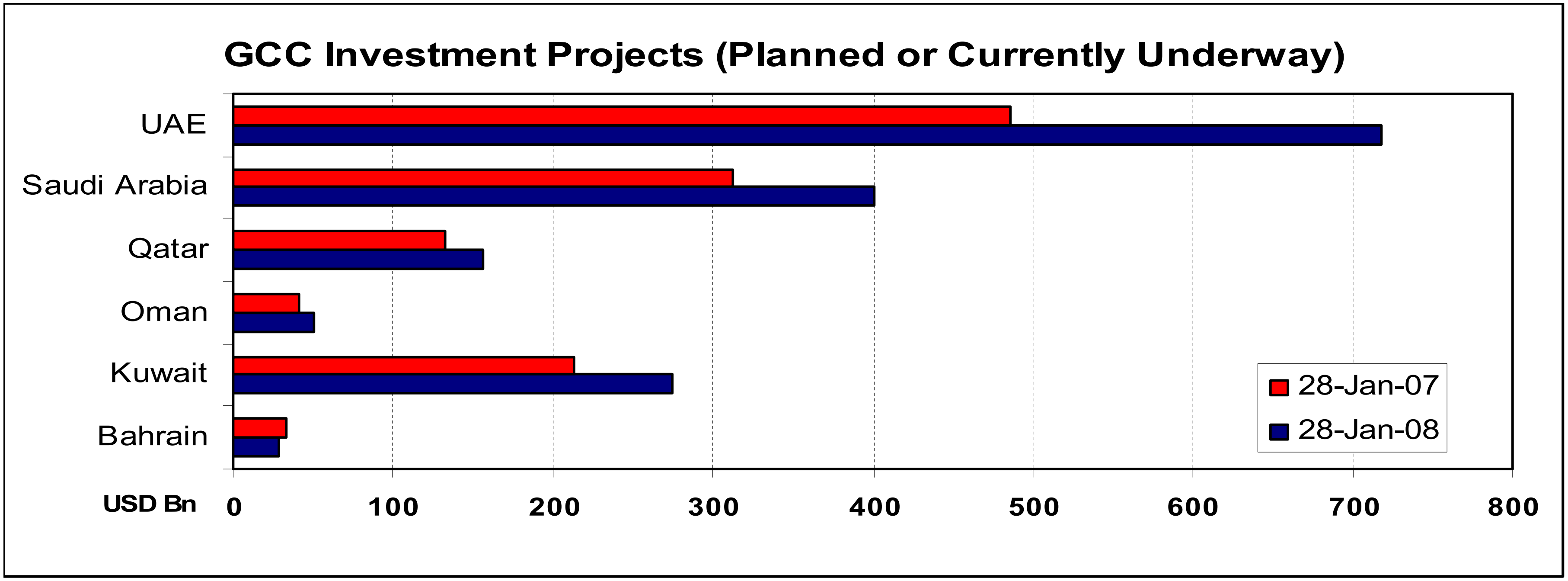
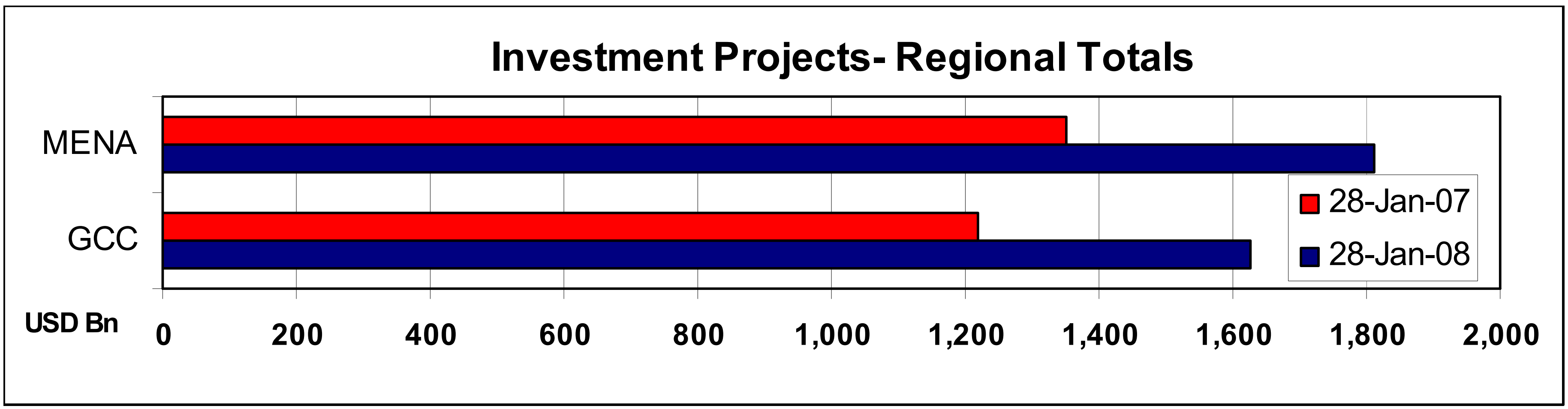




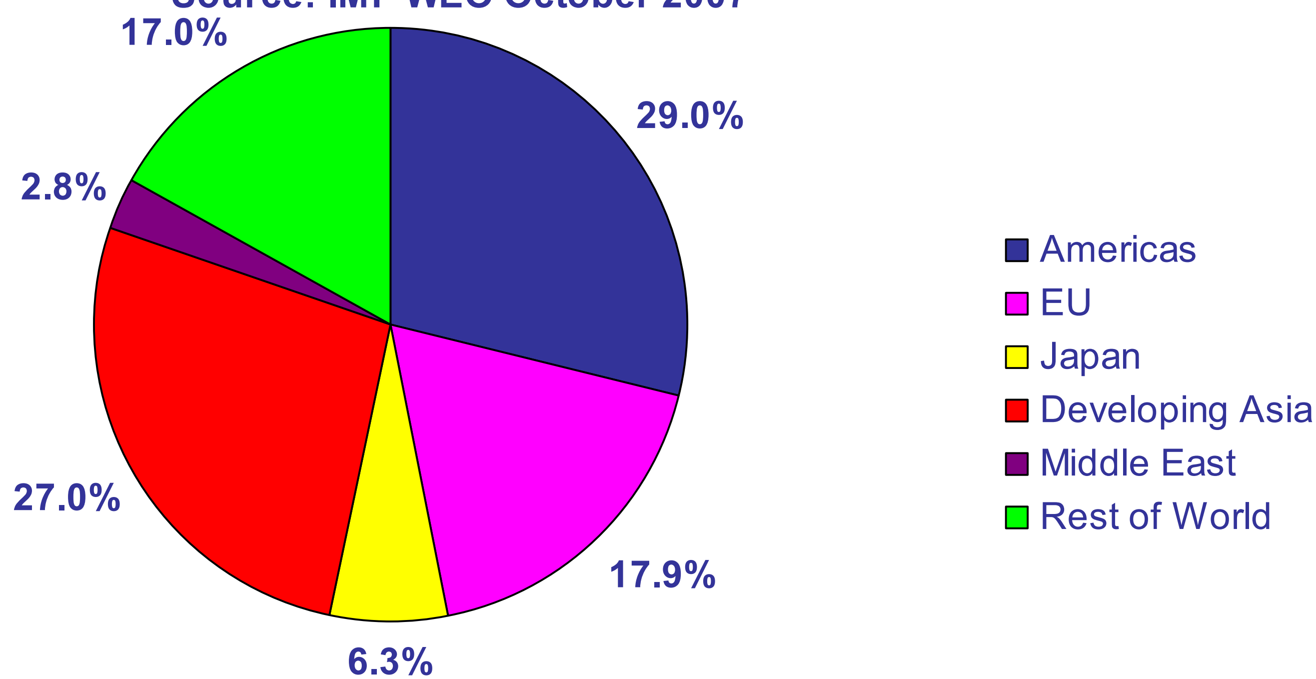
Source: MEED

Integrated Infrastructure basis for GCC Economic & Financial Integration

- Geography & proximity, density & intensity of traffic suggest high returns to integrated infrastructure investments: standards, policies, pricing; integrated network
- Transport: rail, road, air
- Energy: oil & gas, electricity
- Telecommunications & Infostructure (broadband+)
- Payment Networks: facilitate payments & settlements
- Financial Market Infrastructure: integrated capital markets

WEO Groups Share in Aggregate GDP-Based on PPP

Source: IMF WEO October 2007

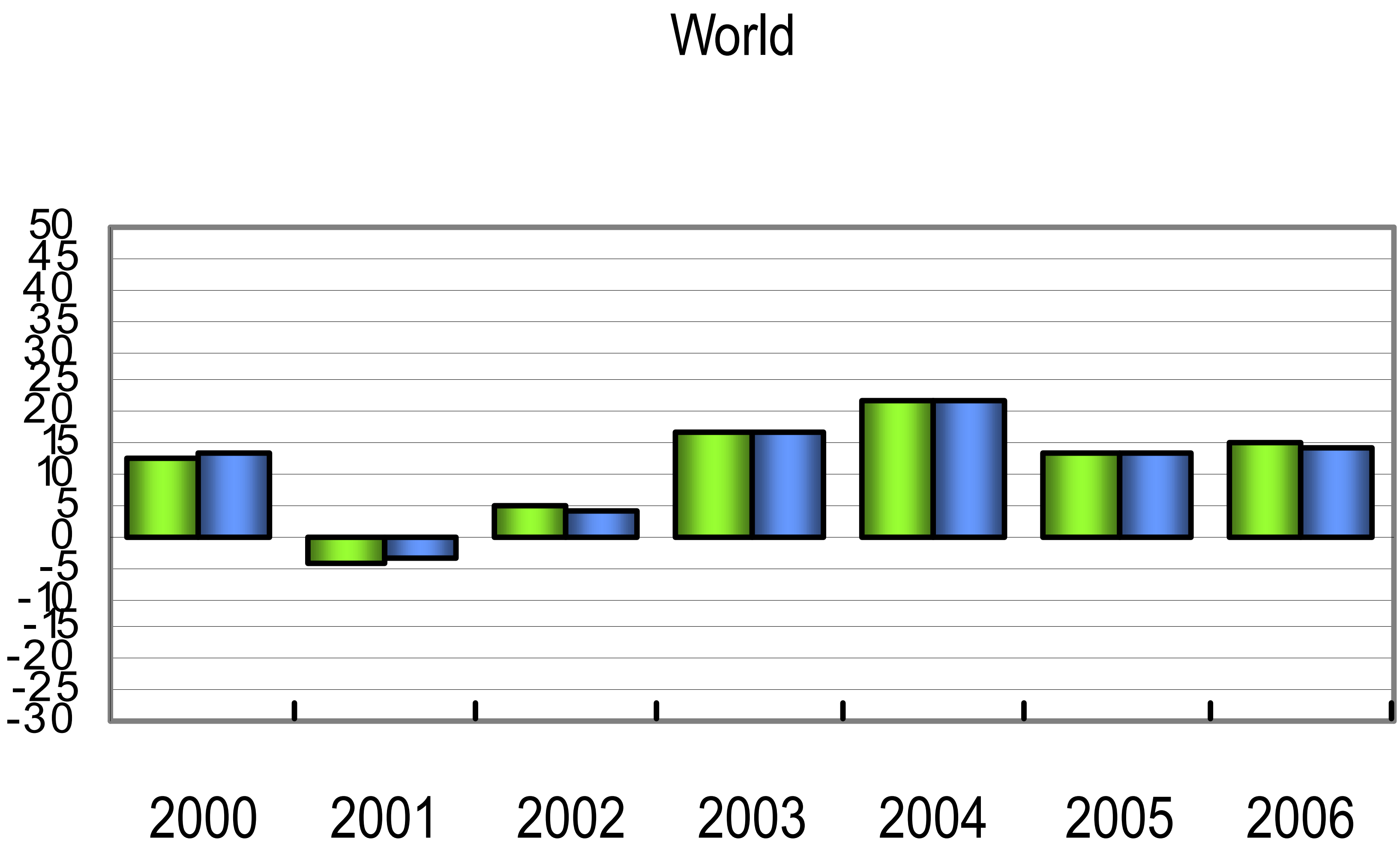


* includes US, Canada, Western Hemisphere

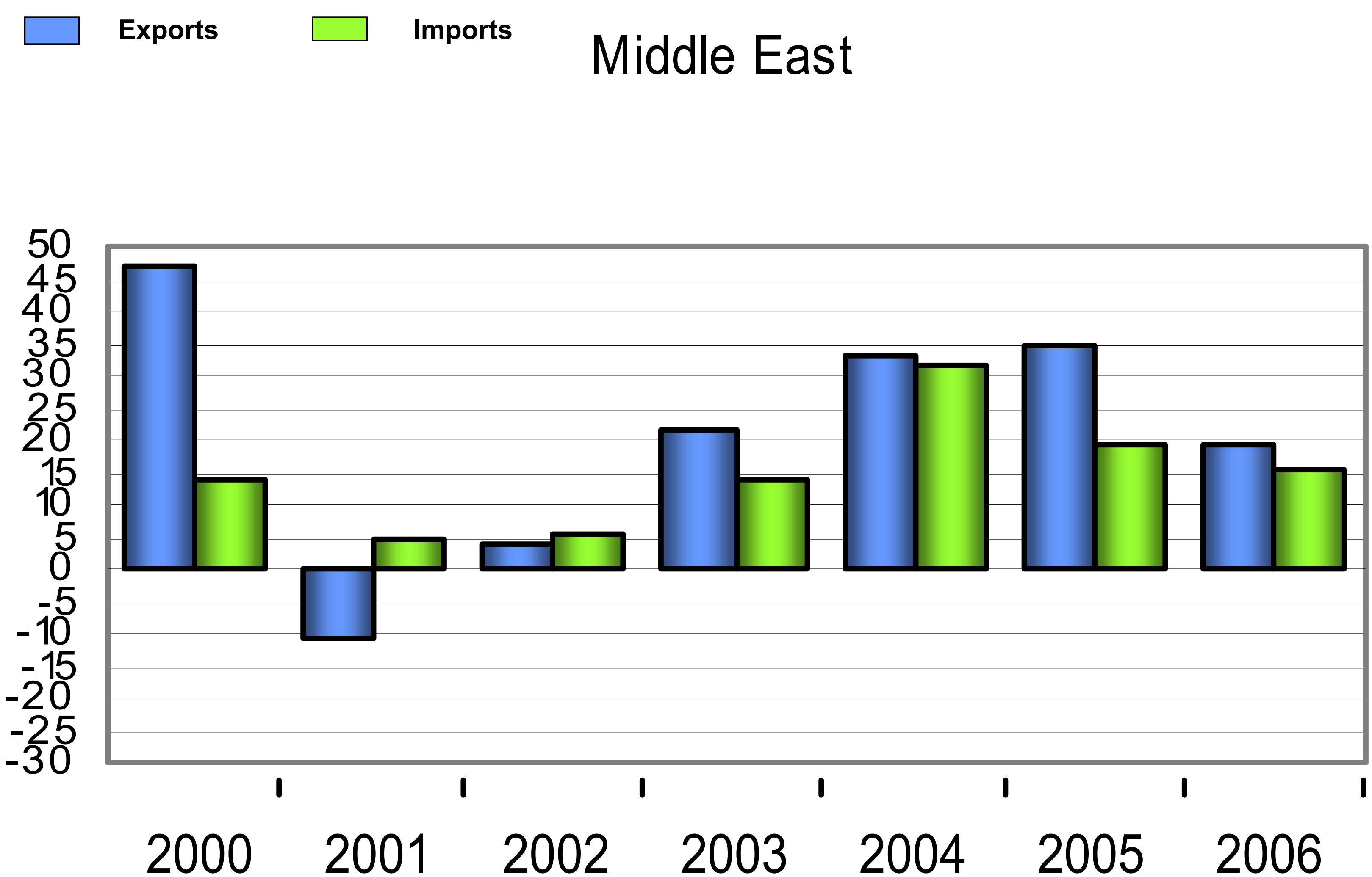
GCC: Power of Regionalism & Networks

- **Location & New Geography:**
  - GCC well located to benefit from relocation of trade & economic activity. Asia now represents about 40% of world GDP
  - Regionalism & investment in network infrastructure (power, telecoms, energy) permit economies of scale and scope in output and trade
  - Liberal Trade policies has increased openness through multilateral (WTO) and bilateral FTAs
  - Increased de-linking from the US business cycle
- GCC Common Market good start, but lack of GCC Financial Sector development is now a Barrier to sustained growth and competitiveness

Value of world merchandise trade Growth, 2000-2006, (% pa)



Value of world merchandise trade Growth, 2000-2006, ME (% pa)



Source of Imports

GCC Foreign Trade 2006

GCC Major Import Partners

	Partners	%
1	EU	31.3%
2	USA	11.5%
3	China	8.6%
4	Japan	7.3%
5	India	6.5%
6	Korea	3.5%
7	Saudi Arabia	3.5%
8	UAE	2.6%
9	Singapore	2.1%
10	Australia	1.9%

Destination of Exports

GCC Major Export Partners

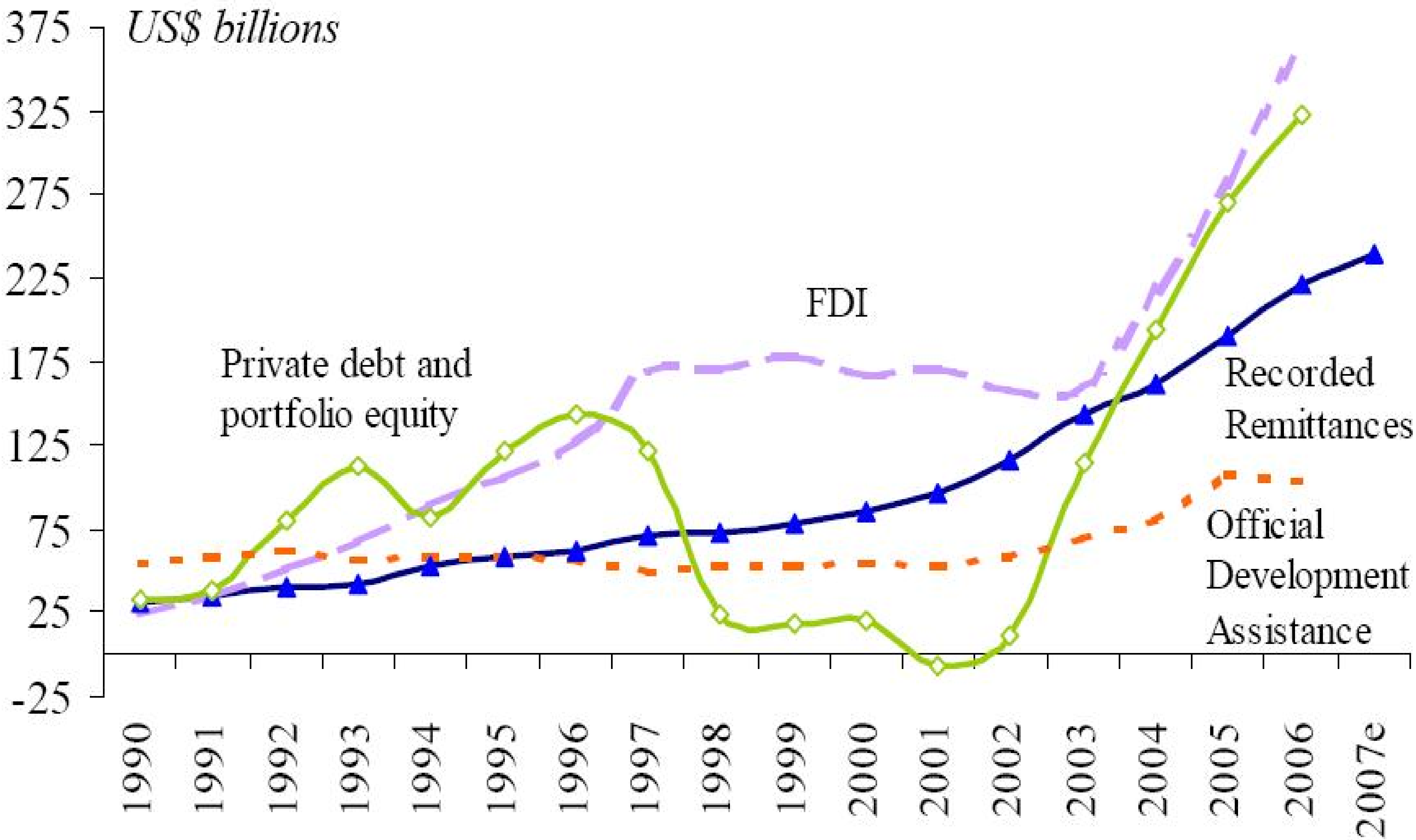
	Partners	%
1	Japan	21.6%
2	Korea	11.8%
3	EU	10.3%
4	USA	9.1%
5	China	6.0%
6	Singapore	4.7%
7	Thailand	3.7%
8	India	2.1%
9	Pakistan	2.0%
10	South Africa	1.5%

Demographics, Migration and Remittances

- **Higher growth in the oil producers has been transmitted to labour exporters:** India, Pakistan, Egypt, Jordan, Lebanon, South Asia, North Africa
- **Officially recorded inward remittance flows worldwide have risen from an estimated $131.5billion in 2000, to more than $317billion in 2007e; MENA: $12.9 billion to $28.5 billion in 2007e**
- **Inward remittance flows between 12%-15% of GDP for Egypt, around 5%, for India, and more than 22% for Lebanon.**
  - **India** world's top remittance recipient with $27.0 bn in 2007, or 5.7% of GDP.
  - **Saudi Arabia**: world's top 2nd remittance sender with $15.6bn in 2006 or 5.0% of GDP
  - **Lebanon**: world's top 8th recipient of remittances in 2006 (22.8%)
  - **India-UAE** is top migration corridor for high-income non-OECD countries. **India-Saudi Arabia**, comes in 2nd place.
- **Official remittances are likely to represent only a fraction of total remittances**

Source: ***Migration and Remittances Fact book 2008, World Bank.***

Remittances growing; more stable than capital flows, FDI or ODA



Sources: *Global Economic Prospects 2006: Economic Implications of Remittances and Migration* (World Bank), *World Development Indicators 2007*, and *Global Development Finance 2007*.

Transmission and new Regionalism

- Transmission effects and new linkages affecting labour exporters:
  - Higher incomes of migrant populations
  - ↑ Labour flows to oil exporters
  - ↑ remittances to labour exporting countries
  - FDI
  - Portfolio investment
- Oil producers more likely to retain migrants: reforms to property rights. People 'voting with their feet'
- Labour Force Skill Mix changing: more High-skill and professional categories
- **Reverse 'Brain Drain' & ↑ expenditure on human capital**
- ***Remittances leading to greater ME Economic & Financial Integration***

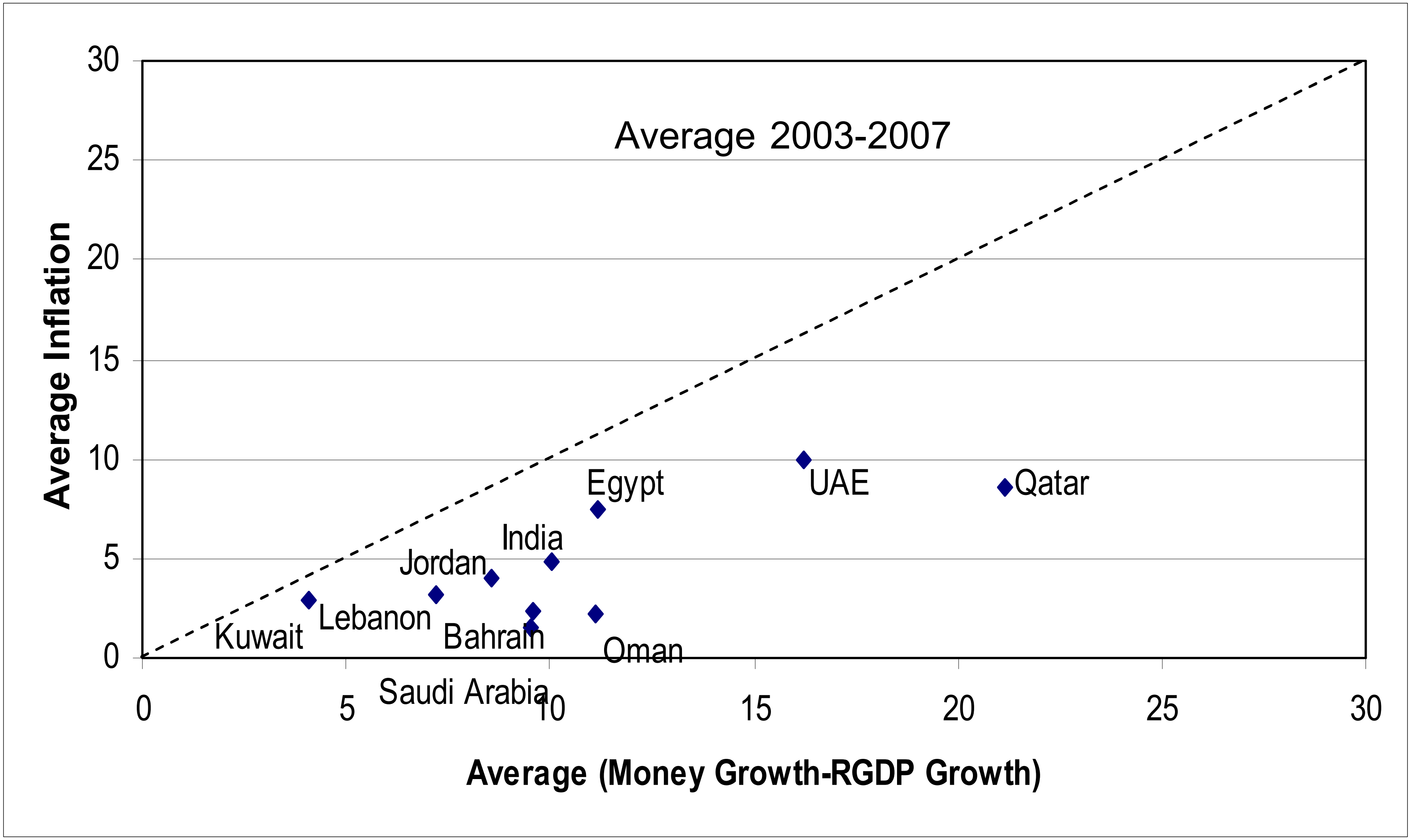
Increase in Wealth and Liquidity

Massive Wealth Creation.

- GCC $585bn current account surplus has outgrown those of China and Japan.
- Currently, the GCC region's proven oil reserves stand at 484.3 billion barrels and natural gas reserves at 41.4 trillion cubic meters accounting for 40.3% of the world's proven oil and 23% of natural gas reserves, respectively.
- Given global energy demand growth projections, using conservative estimates for oil prices at $48/bbl, the projected cumulative oil and natural gas revenues for the GCC in the 2005-2030 period totals $5.1 trillion.[1]

- Inflation and Rise in prices of non traded goods & services
- Accommodating monetary policies leading to high money and credit growth rates, and financing real estate and financial market booms with spectacular gains and excess returns in equity and debt market instruments
- Increased liquidity resulted in an investment driven boom:
  - Real estate boom and asset price appreciation
  - Stock market boom
  - Credit market boom
- Pressure on US$ Peg Exchange Rate policies

Money Growth and Inflationary Pressures



Author's Calculation of EIU Data, 2008

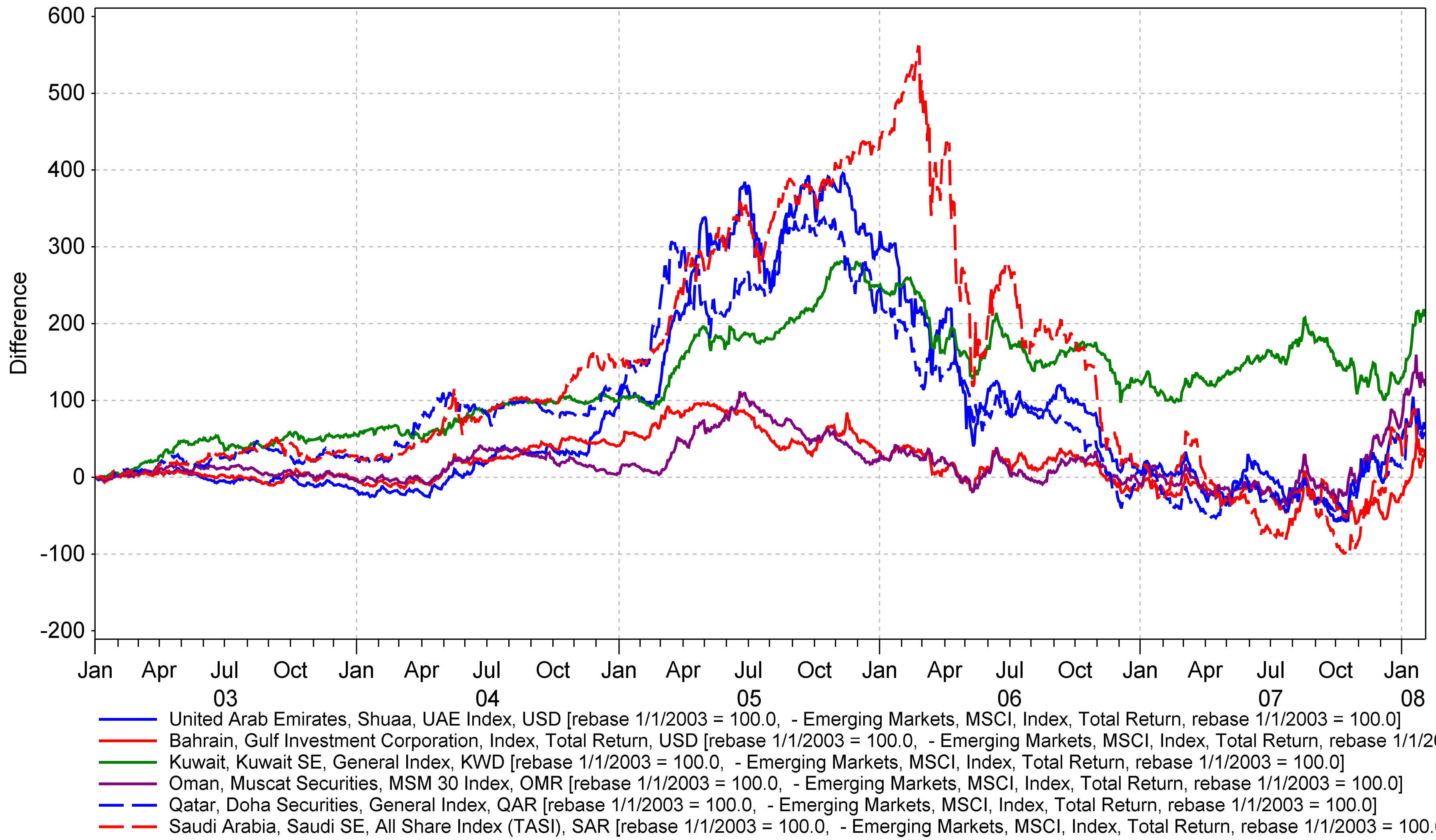
Liquidity & the Stock Markets

- Growth and abundant liquidity have fuelled a spectacular resurgence of the credit and equity markets in the SAMEA and the Middle East region.
- For the GCC, market capitalization grew from less than $200 billion in 2002 to about $1,039 billion by January 2008. GCC markets out-performed emerging and developed markets.
- Stock markets grew more rapidly than the economies: market capitalization jumped from an average of some 65% of GDP in the GCC countries to 149% of GDP between 2002 and early 2008.
- The correction of the overly exuberant equity markets in 2006 came as a wake-up call for action, signalling the need for reform to restore investor as well issuer confidence.
- Despite the growth in the number of companies, IPOs and higher valuations, markets remain fragmented, displaying high volatility of returns and lack of breadth, depth and liquidity.

GCC's Stock Market Performance, 2003-2008

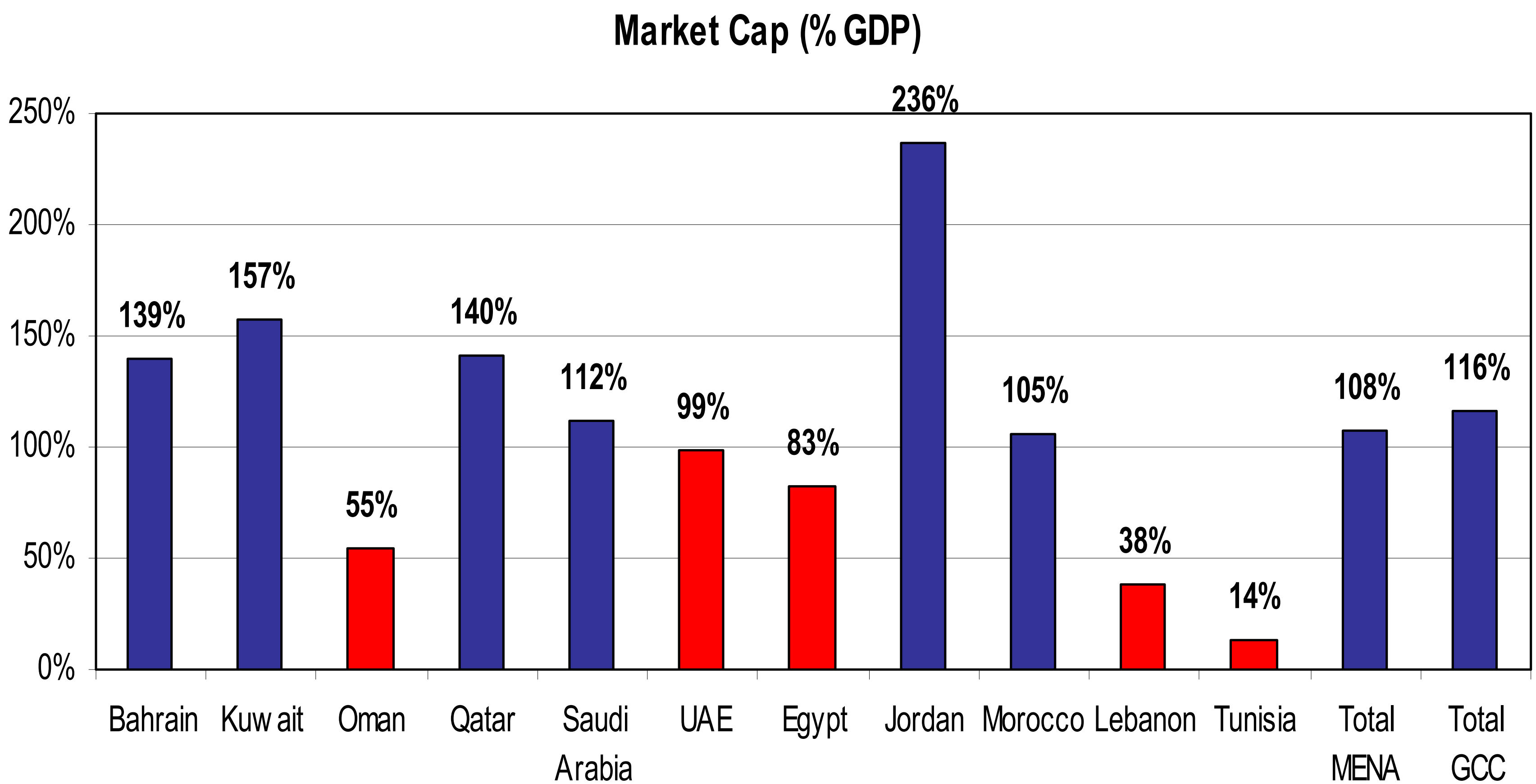
GCC Markets vs. MSCI Emerging Markets

Index Value 1/1/2003=100



Source: Reuters EcoWin

GCC Market Cap has doubled since 2002



Source: *DIFC Economics, Zawya, February 2008*

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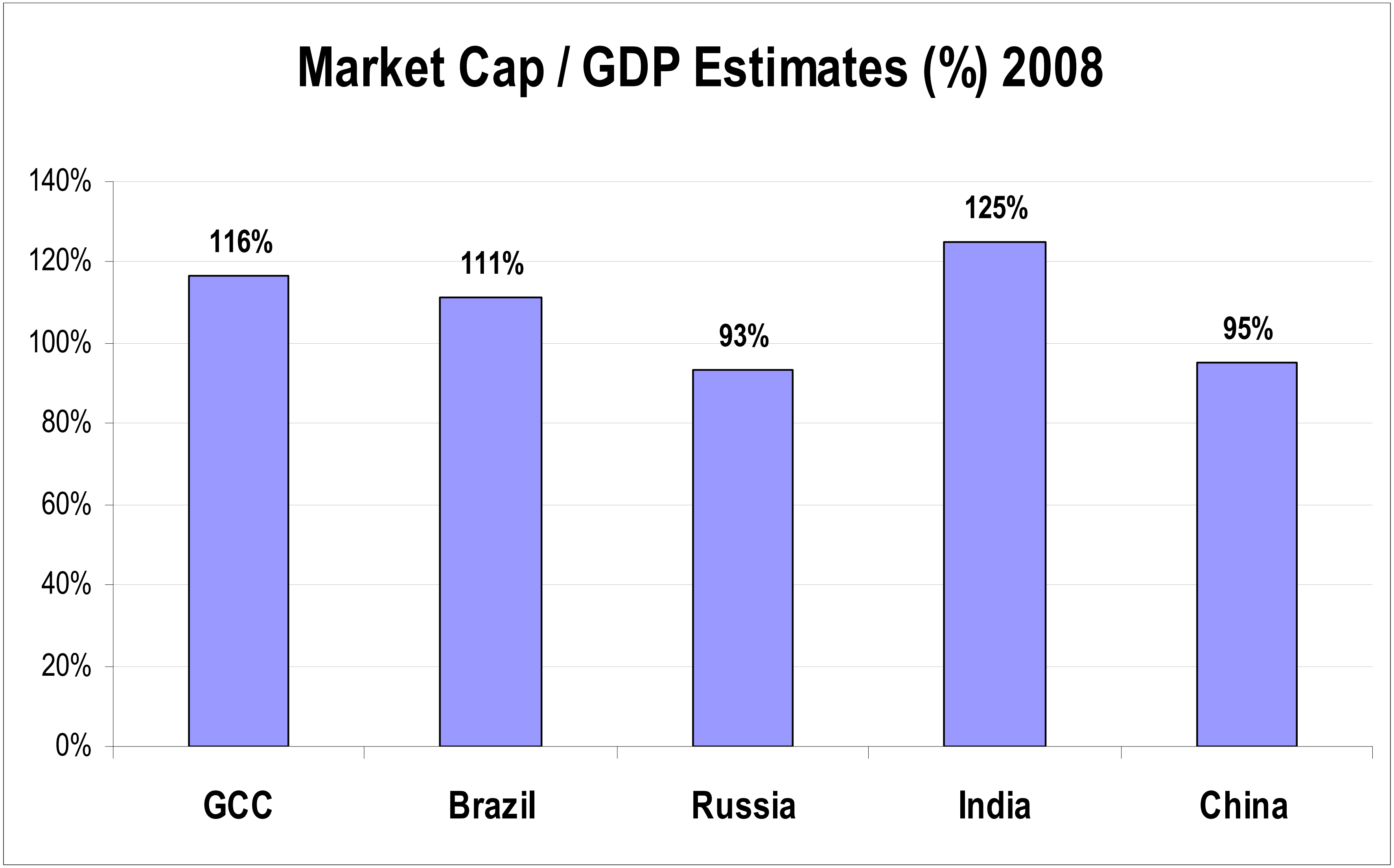
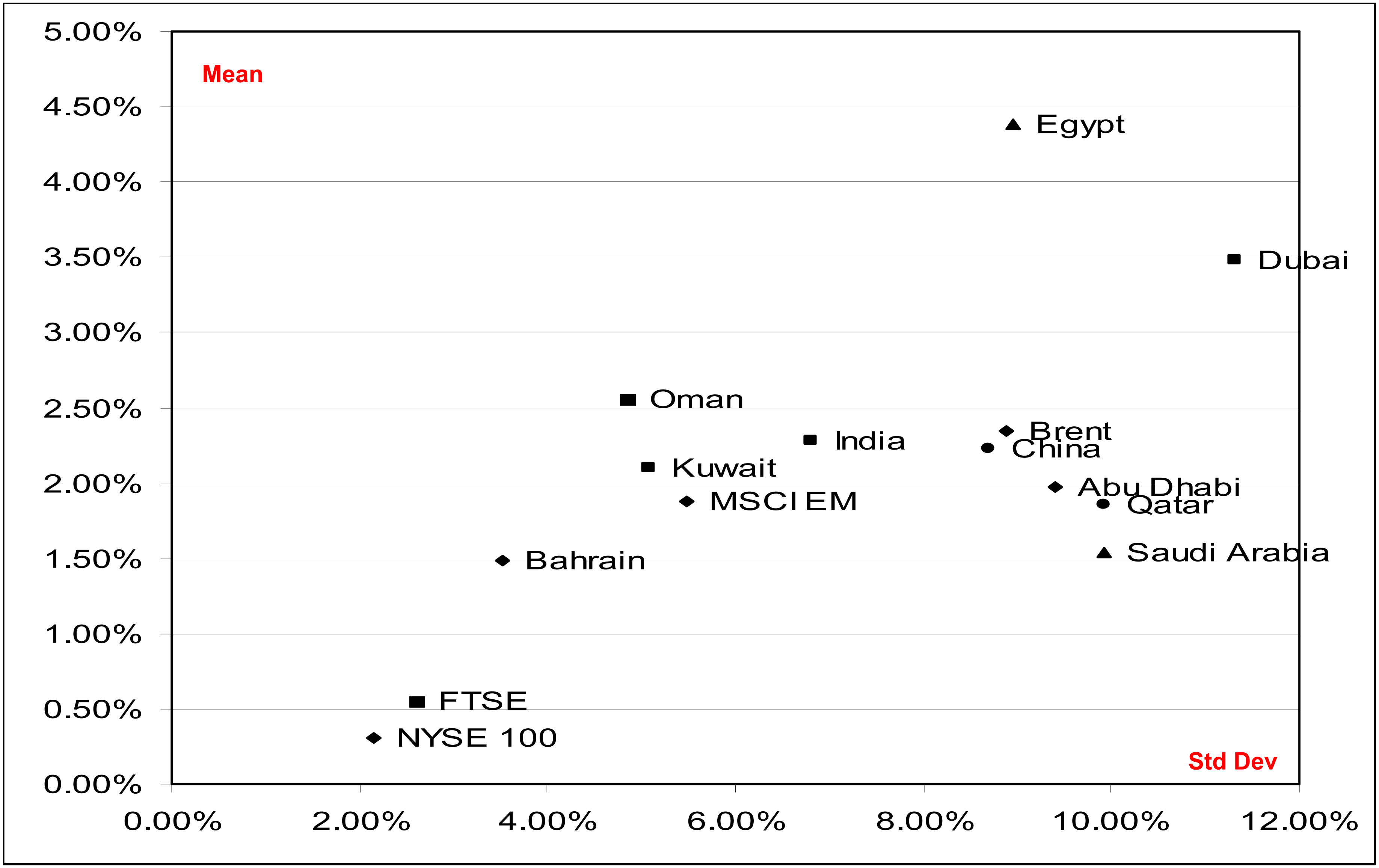


GCC Comparative Market Returns and Risk
Monthly Return& Risk (%), Dec 2003-Feb 2008



Source: Reuters, DIFC Economics

GCC markets show low correlation with developed markets, offering potential risk diversification benefits

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Monthly Return Correlations, Dec. 2003-Feb. 2008

	Bahrain	Kuwait	Egypt	Saudi Arabia	Dubai	Abu Dhabi	Qatar	Oman	Brent	NYSE 100	India	China	MSCI EM	FTSE
Bahrain	1.00													
Kuwait	0.55	1.00												
Egypt	0.51	0.14	1.00											
Saudi Arabia	0.35	0.31	0.21	1.00										
Dubai	0.40	0.46	0.35	0.48	1.00									
Abu Dhabi	0.38	0.46	0.11	0.45	0.76	1.00								
Qatar	0.29	0.21	0.38	0.29	0.39	0.42	1.00							
Oman	0.36	0.29	0.32	0.35	0.53	0.49	0.25	1.00						
Brent	-0.06	-0.12	0.19	0.04	-0.10	-0.10	0.24	-0.02	1.00					
NYSE 100	-0.02	-0.06	0.07	-0.18	-0.04	-0.12	0.05	-0.07	-0.19	1.00				
India	-0.04	-0.23	0.31	0.09	0.09	-0.04	0.19	0.08	0.11	0.49	1.00			
China	-0.06	-0.06	-0.10	-0.10	-0.16	-0.15	0.06	-0.15	0.08	0.40	0.23	1.00		
MSCI EM	0.15	-0.09	0.37	0.02	0.01	-0.13	0.18	-0.02	0.18	0.64	0.72	0.45	1.00	
FTSE	-0.06	-0.14	0.31	0.09	0.09	-0.06	0.27	0.07	0.19	0.69	0.68	0.26	0.71	1.00

Source: Reuters, DIFC Economics

Strong macroeconomic fundamentals imply low macro risks:

- High growth rates driven by higher oil prices, diversification and economic liberalization policies imply high expected corporate profits and investment returns
- Investment-led growth with large infrastructure component →increased productivity growth & ↑private sector investment
- Expectations of GCC Regional Economic Integration: lower the cost of equity capital and lead to convergence of asset prices
- Gradual Market de-segmentation & liberalization of access to real assets and financial markets, de jure & de facto: free zones, property freehold
- Safe haven: attracting capital and elites from neighboring countries.

CHALLENGES & POLICY ISSUES

- **Inflation & Exchange Rate Policy**
- **Capital Market Development**

CHALLENGE OF INFLATION

- **Two sources of inflation:**
  - Non-Traded Goods & Services: housing, services
  - Imported: international commodity prices, weak US$

- **Inflation & GCC exchange rate peg:**
  - Monetary Union in 2010 (?)
  - Misalignment of monetary policy
  - Pressure to move to currency basket
  - Adopt inflation targeting

But:

  - Build central banks' monetary & exchange rate management capacity;
  - Build money, debt markets
  - Requires GCC policy coordination

The Capital Market Development Imperative

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- GCC have become ‘asset-based economies’ with income from assets more important than oil & gas revenue
- Invest, Manage and Control region’s financial wealth of $2+ trillion and growing as a result of high energy prices
- Financing Infrastructure & Regional Economic Integration
- Enable & support economic and financial reforms:
  - Enable separation of oil revenue management from fiscal policy & investment
  - Lead to greater fiscal equity trough user fees & charges for infrastructure services
  - Privatisation and private sector participation in infrastructure
- Change in Global Economic Geography requires accompanying change in Global Financial Geography

ME/GCC Economic Outlook

- Continued high growth is forecast in 2008: ME/GCC at 6.2% with oil exporters (including Central Asia) growing at 6.8% and GCC at 5.8%
- Growth is investment led with strong private sector participation and record FDI levels.
- Investment is leading to diversification, increase in productivity and absorptive capacity.
- Inflationary pressures continue: from 8.8% in 2007 to 8.2% in 2008 for MENA and from 5.1% to 4.9% for GCC
- External position positive with MENA current AC surplus at 15.4% for 2007 and forecast at 14.8 for 2008; for GCC countries surpluses are running at 25.4% of GDP for 2007 and 24.8% in 2008.
- Surpluses are being recycled back into regional economies leading to greater regional & international economic integration. Cumulative current account surplus for the GCC countries is expected to grow to $954.6 billion by 2008.

GCC RENAISSANCE

A Time for Vision
A Time for Action
A Time for Architects and Designers
A Time for Builders & Investors

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March 2008