GCC FISCAL DEVELOPMENTS & CHALLENGES

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GCC FISCAL DEVELOPMENTS & CHALLENGES

- **GLOBAL FISCAL DEVELOPMENTS**
  - **ADVANCED ECONOMIES VS EMERGING ECONOMY CONTRASTS**
  - **DEBT CRISES & INFLATION RISKS**

- **GCC FISCAL DEVELOPMENTS & CHALLENGES**
  - **RECENT DEVELOPMENTS SINCE 2002**
  - **OIL REVENUE DEPENDENCE**
  - **GENERATIONAL ACCOUNTING**
  - **NEW HORIZONS & POLICY CHALLENGES**

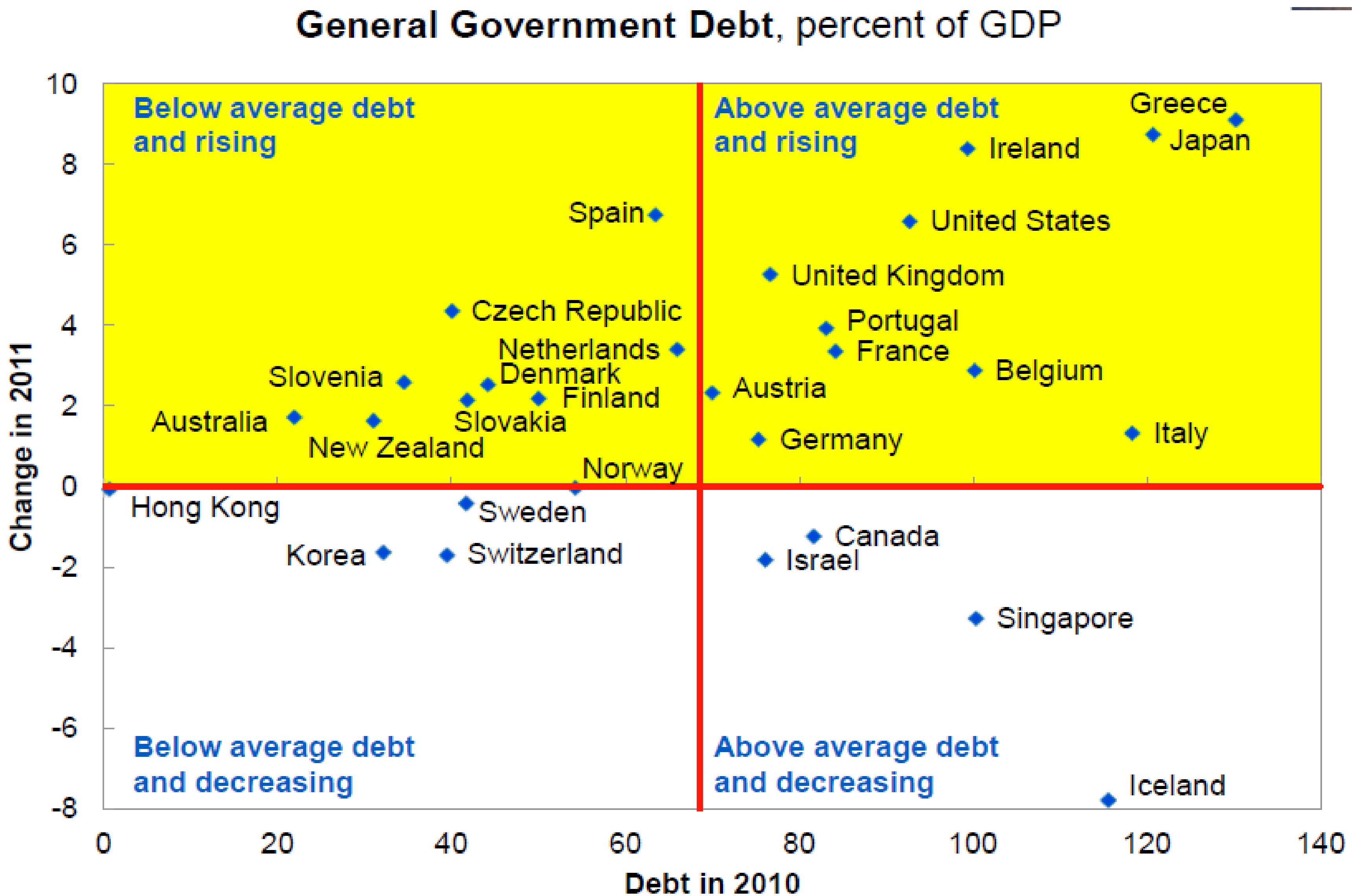
Fiscal Divide between Advanced & Emerging Economies

- Fiscal Divide emerging due to:
  - Divergent Growth Patterns
  - Entitlement Programmes
  - Demographics

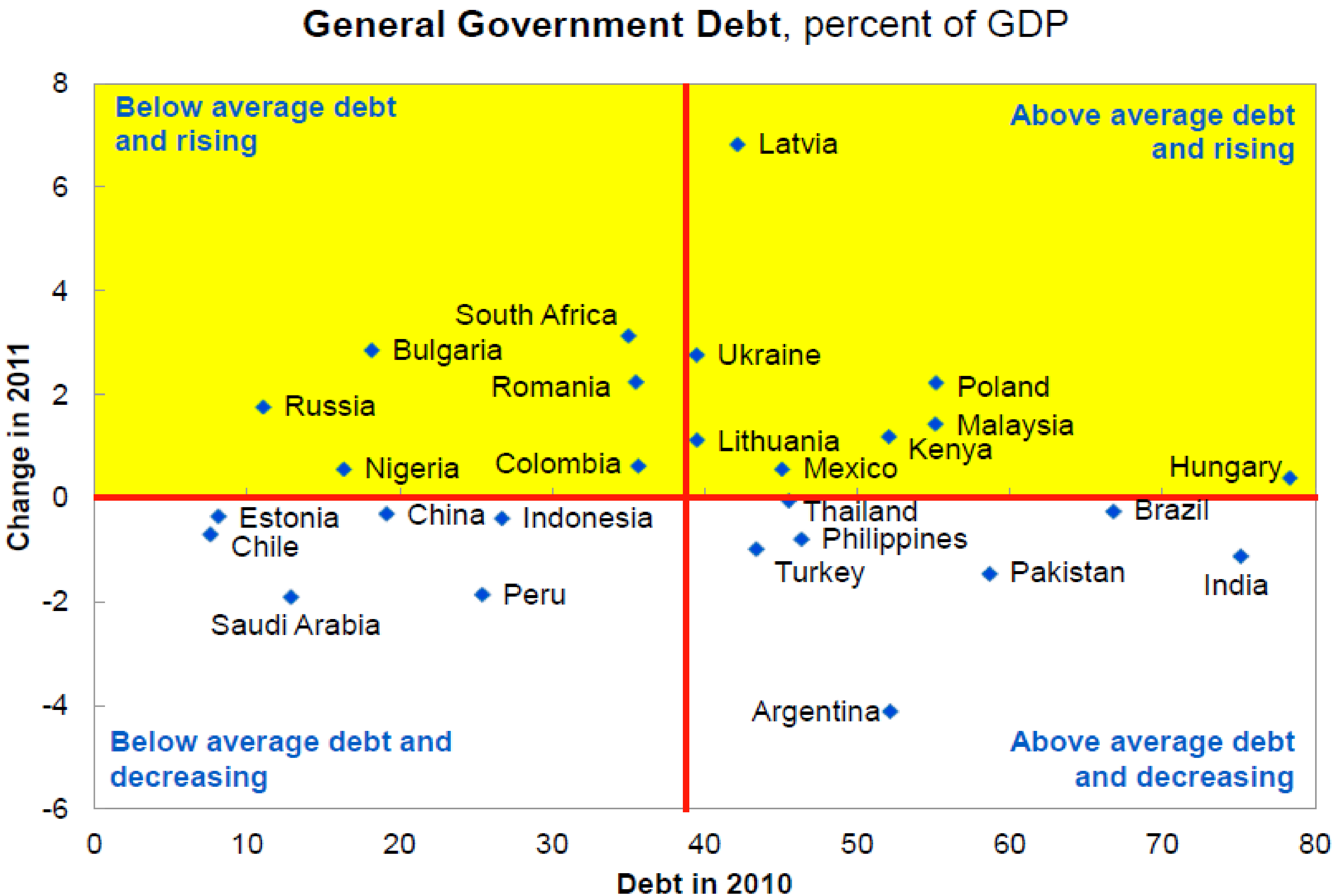
- “Great Recession” & Financial Crisis has exacerbated the Fiscal Divide:
  - Structural
  - Cyclical
  - Bailouts & Fiscal Stimuli

  - Fiscal Divide is the “Great Fiscal Crisis” for advanced economies:
    - Budget Deficits
    - Debt Levels

DEBT IN ADVANCED ECONOMIES (IMF-FAD)



DEBT IN EMERGING ECONOMIES (IMF-FAD)

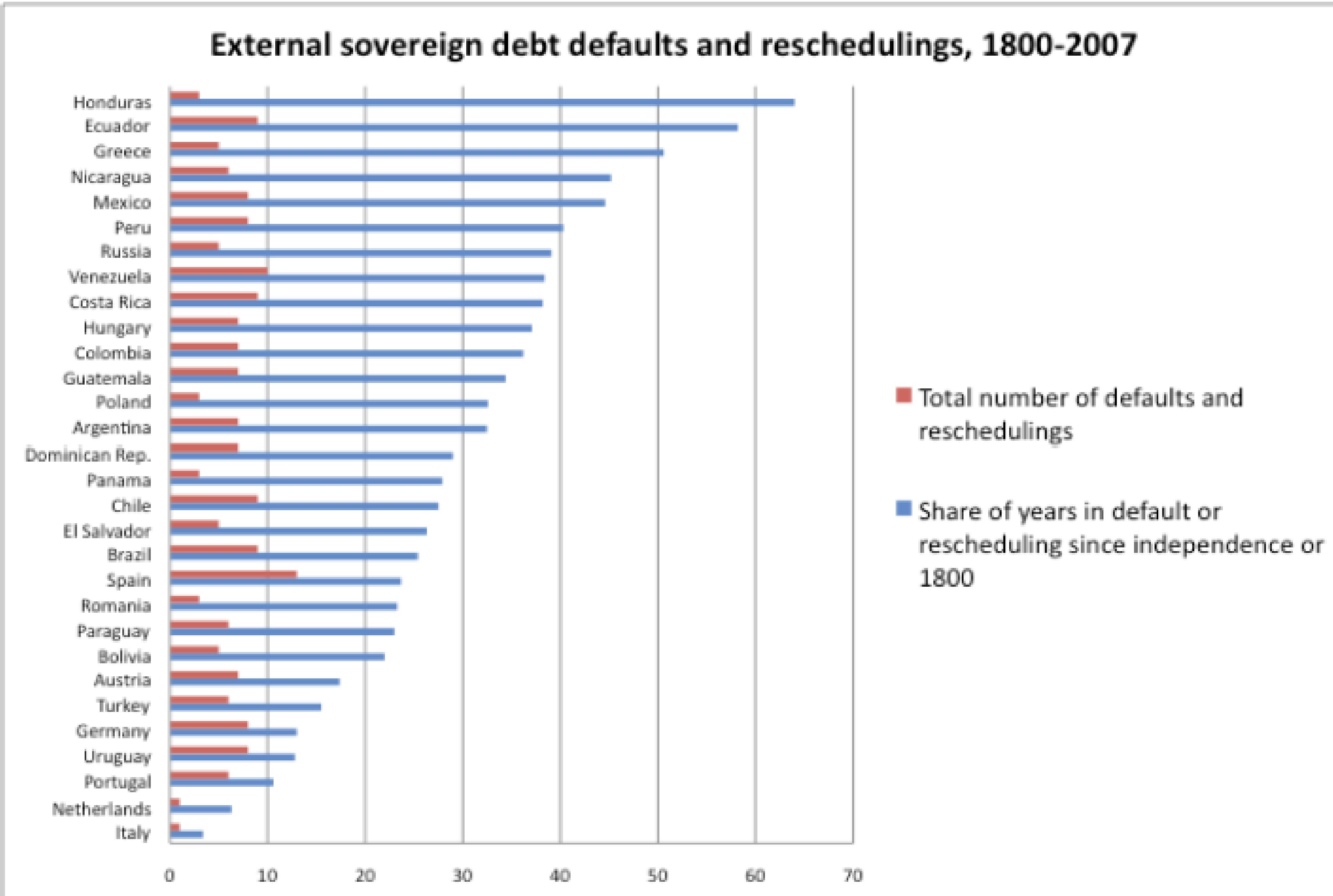


How do you get out of a crisis?

1. A higher growth rate of GDP
2. A lower interest rate on the public debt
3. A bailout, meaning either a current transfer payment or a capital transfer from abroad
4. Fiscal pain, meaning an increase in taxes and/or a cut in public spending
5. Increased recourse to seigniorage (revenues from monetary issuance) by the central bank
6. Default, including every form of non-compliance with the original terms of the debt contract, including repudiation, standstill, moratorium, restructuring, rescheduling of interest or principal repayment etc.

Source: Buiter (2010)

Sovereign Debt Defaults & Rescheduling, 1800-2007



Source: Reinhart and Rogoff (2009)

Everyone in Europe has been at it!

DIFC

	Since independence or 1800			Since 1800*		
	Share of years in a banking crisis	Share of years in default or rescheduling	Total number of defaults and reschedulings	Share of years in which inflation exceeded 20%	Share of years in which inflation exceeded 40%	Number of hyperinflation years
Austria	2	17	7	21	12	2
Belgium	7			10	7	
Denmark	7			2	1	
Finland	9			6	3	
France	12		8	6	2	
Germany	6	13	8	10	4	2
Greece	4	51	5	13	5	4
Hungary	7	37	7	16	4	2
Italy	9	3	1	11	6	
Netherlands	2	6	1	1		
Norway	16			5	2	
Poland	6	33	3	28	17	2
Portugal	2	11	6	10	4	
Spain	8	24	13	4	1	
Sweden	5			2		
United Kingdom	9			2		

Source: Reinhart and Rogoff (2009)

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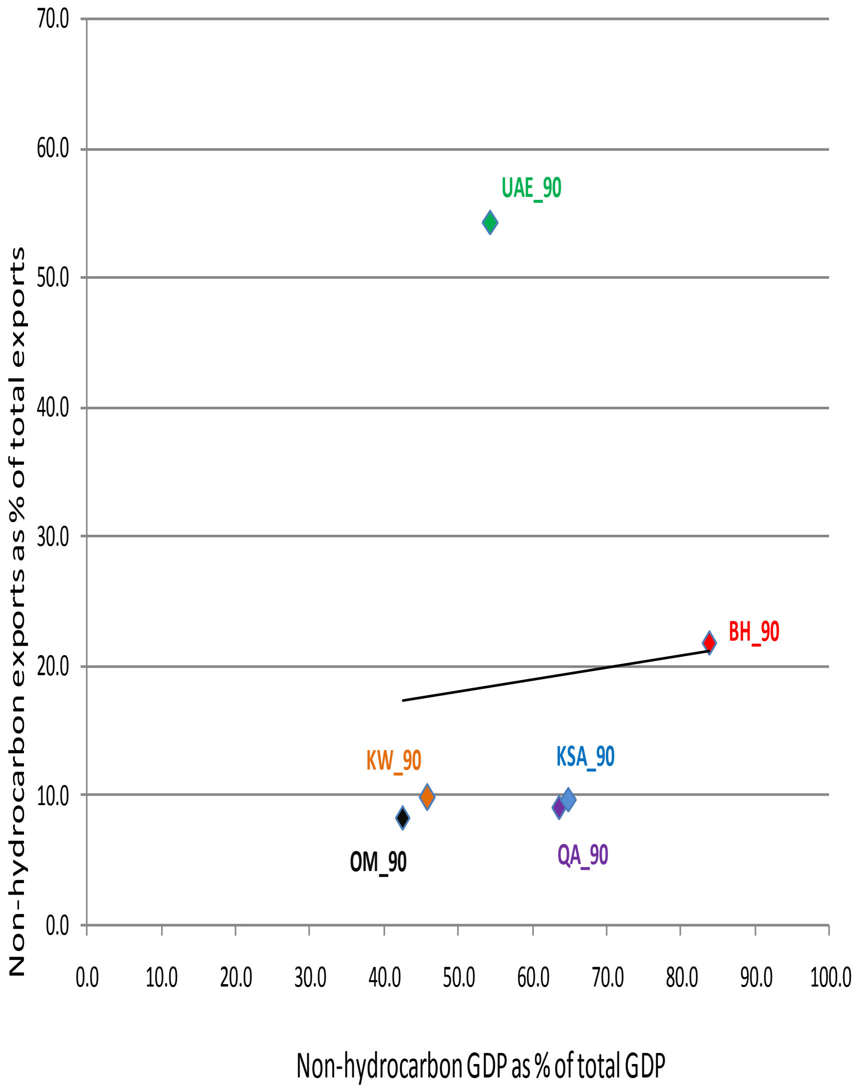
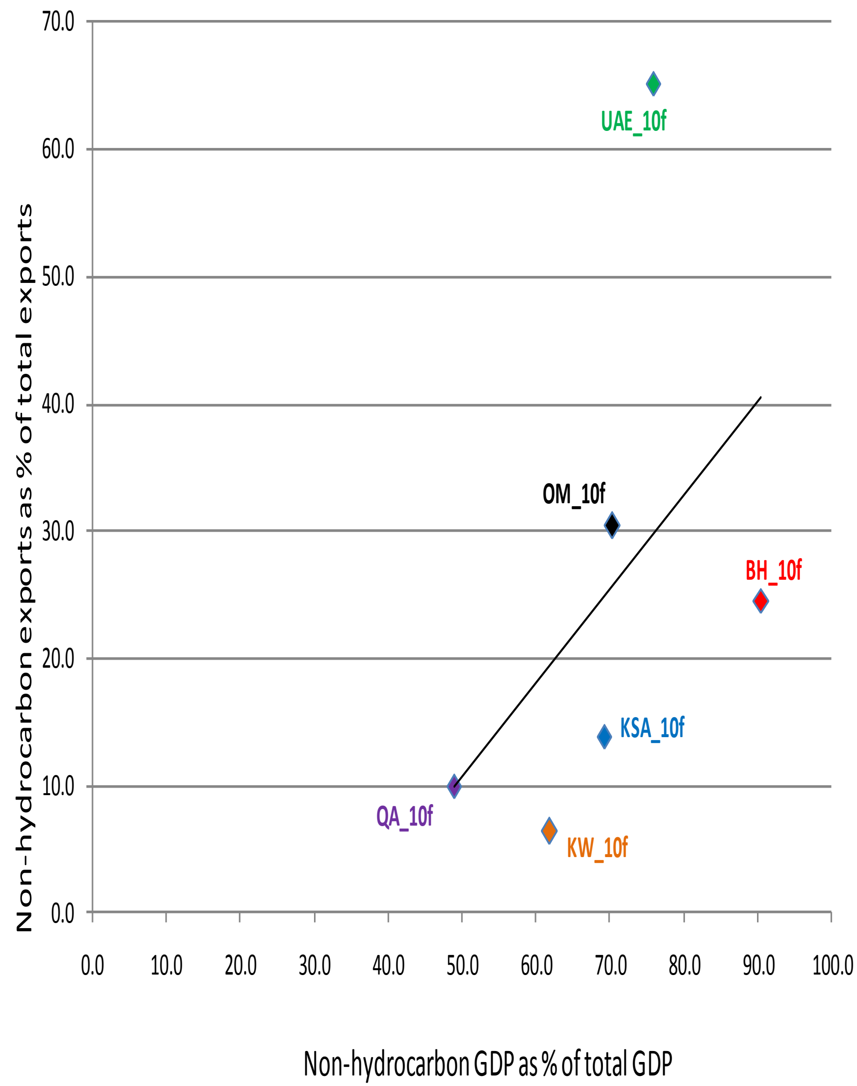
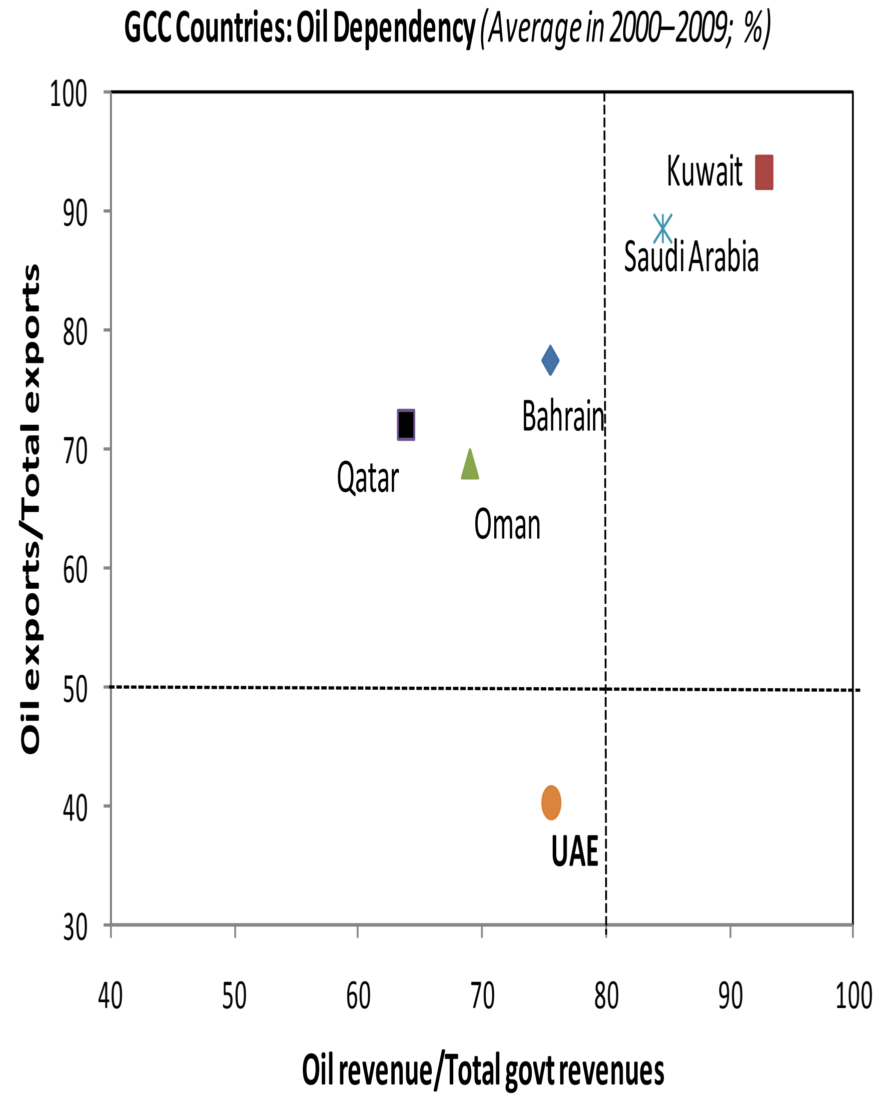
GCC Economic Diversification: 1990-2010



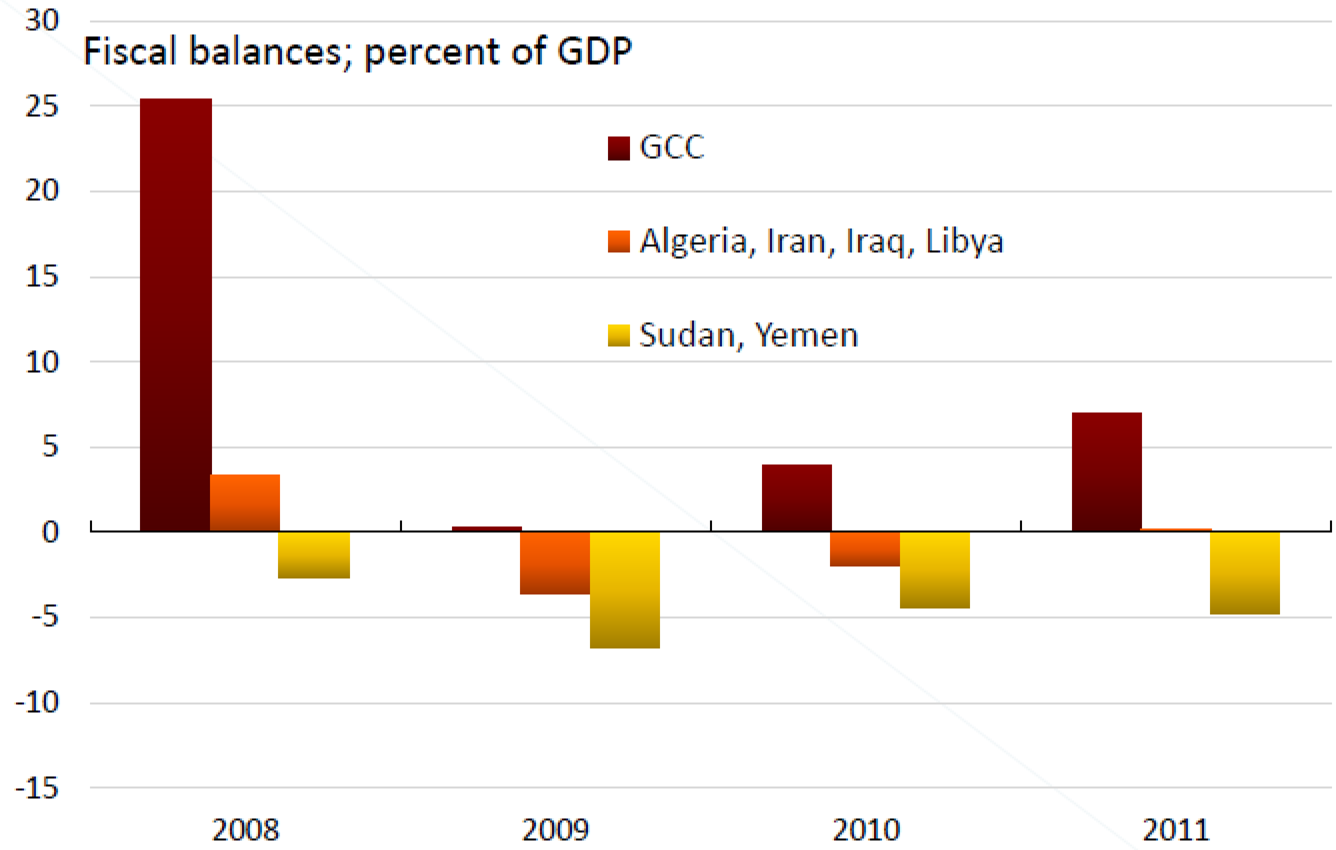


Despite diversification GCC Gov Budgets are oil-dependent

- Oil price boom led to strong fiscal and external balance surpluses in 2002-08
- Surpluses provided the fiscal space to promote economic diversification.
- Oil proceeds have been used to modernize infrastructure, create employment, and improve social indicators.
- But fiscal policy has been constrained by the still-heavy dependence of government revenues on volatile oil export receipts

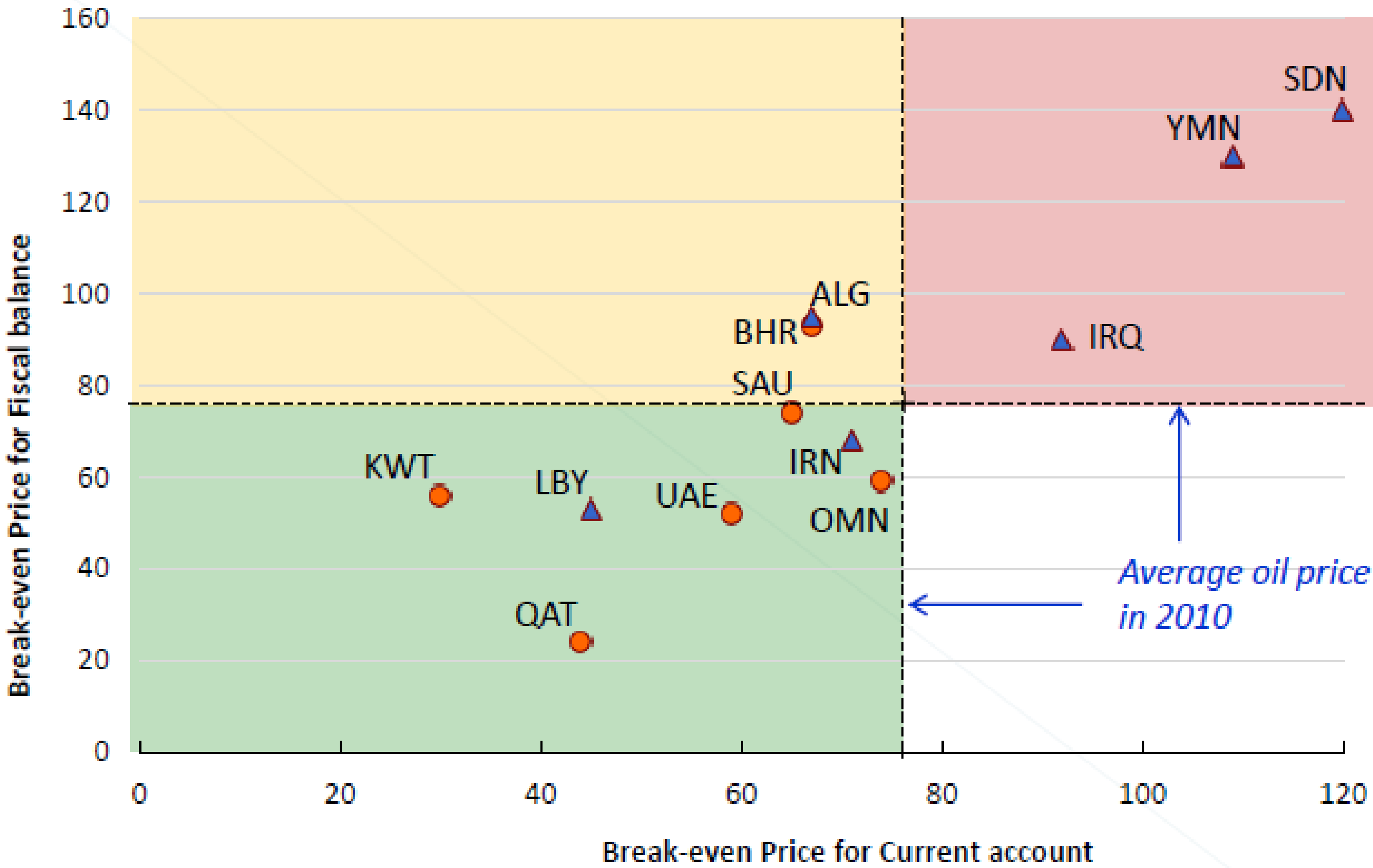


Volatile Oil Prices= Volatile Fiscal Balances



Sources: National authorities; and IMF staff estimates.

Countries Approaching Break-Even Oil Prices

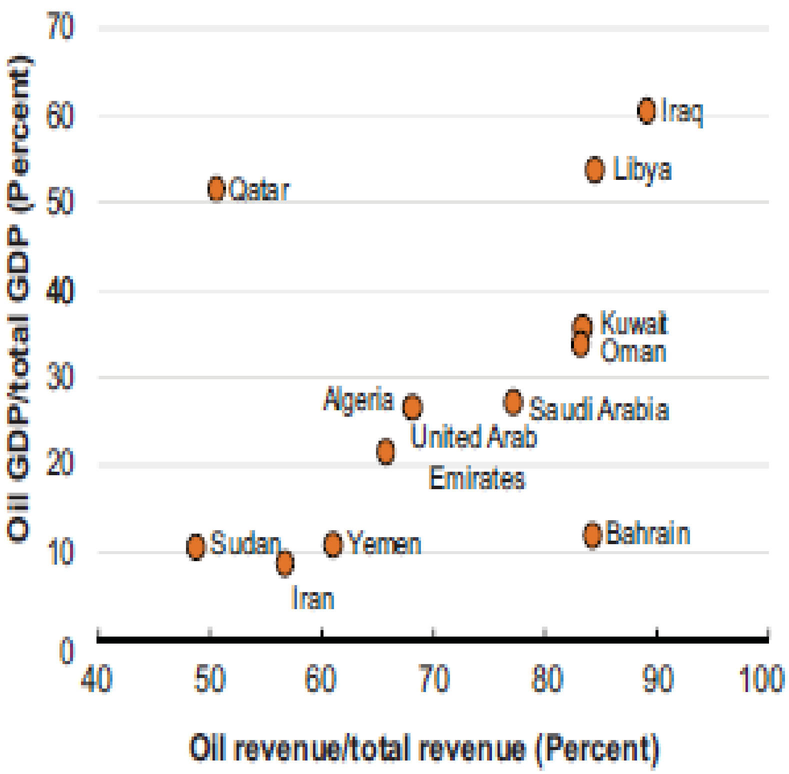


Sources: National authorities; and IMF staff estimates.

Oil Dependence has Increased

Figure 1

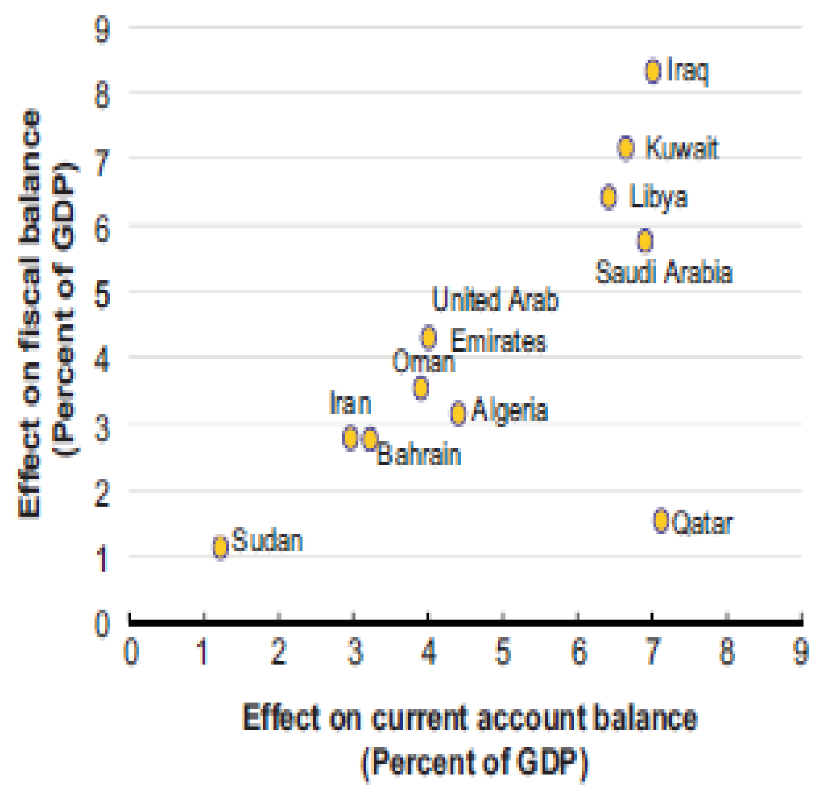
Fiscal and Economic Activity: Dependence on Oil, 2010



Sources: National authorities; and IMF staff estimates.

Figure 2

Impact of a US$10 per Barrel Increase in Oil Prices, 2010



Sources: National authorities; and IMF staff estimates.

General Government Non-Oil Fiscal Balance (% non-oil GDP)

	Average 2000–05	2006	2007	2008	2009	Proj. 2010	Proj. 2011
MENAP oil exporters	-34.1	-40.1	-41.9	-50.5	-47.4	-49.1	-46.1
Algeria	-31.5	-35.6	-45.7	-54.1	-45.3	-56.2	-54.7
Bahrain[1]	-29.0	-28.3	-29.6	-31.9	-34.3	-34.8	-32.1
Iran, I.R. of	-18.9	-28.2	-26.2	-23.6	-18.9	-18.3	-16.1
Iraq	...	-101.0	-126.0	-215.0	-165.4	-174.7	-157.5
Kuwait[1]	-35.9	-30.3	-27.7	-76.1	-69.8	-69.9	-70.6
Libya	-76.1	-135.3	-124.7	-167.0	-137.9	-128.5	-124.8
Oman[1]	-56.6	-54.5	-47.5	-54.8	-52.0	-58.1	-56.3
Qatar	-45.6	-40.6	-30.7	-20.4	-9.3	-17.4	-23.4
Saudi Arabia	-40.9	-44.8	-51.3	-49.8	-63.4	-65.7	-61.2
Sudan	-9.5	-18.5	-20.9	-20.1	-13.8	-14.5	-15.0
United Arab Emirates[2]	-27.9	-13.7	-14.2	-27.9	-37.3	-31.8	-22.9
Yemen	-35.4	-42.6	-43.1	-46.3	-31.3	-32.6	-28.2
CCA oil and gas exporters	-7.2	-10.9	-12.2	-21.1	-21.2	-24.1	-22.4
Azerbaijan[1]	-12.2	-31.2	-28.6	-38.4	-38.7	-38.6	-34.7
Kazakhstan	-5.5	-4.2	-6.5	-15.9	-15.0	-19.7	-18.3
Turkmenistan[3]	-10.0	-7.4	-6.5	-6.8	-9.4	-11.7	-14.7
Uzbekistan	...	...	...	...	...	...	...
Memorandum							
GCC	-39.3	-37.8	-39.9	-46.9	-53.5	-54.6	-51.1

Sources: National authorities; and IMF staff estimates and projections.

[1]Central government.

[2]Consolidated accounts of the federal government and the emirates Abu Dhabi, Dubai, and Sharjah.

[3]State government.

Cyclicality of Fiscal Policy in MENA & Central Asia

Abdih Y., Lopez-Murphy, P. et al (2010) use government spending as the main indicator to assess the cyclical properties of fiscal policy.

A. Fiscal policy is predominantly pro-cyclical in the region.

i. The result holds for both the MENA oil exporters (MOE) and the CCA but, interestingly, it does not hold for the MENA oil importers (MOI). The absence of pro-cyclicality for oil importers is probably driven by Egypt, the largest economy within the subgroup, where fiscal policy has been uncorrelated with the cycle.

B. Testing correlations between the cyclical components of real GDP and real government spending in good and in bad times at both regional and sub-regional levels =>

i. The correlation coefficient is about 0.8 and is statistically significant at the 1% level.

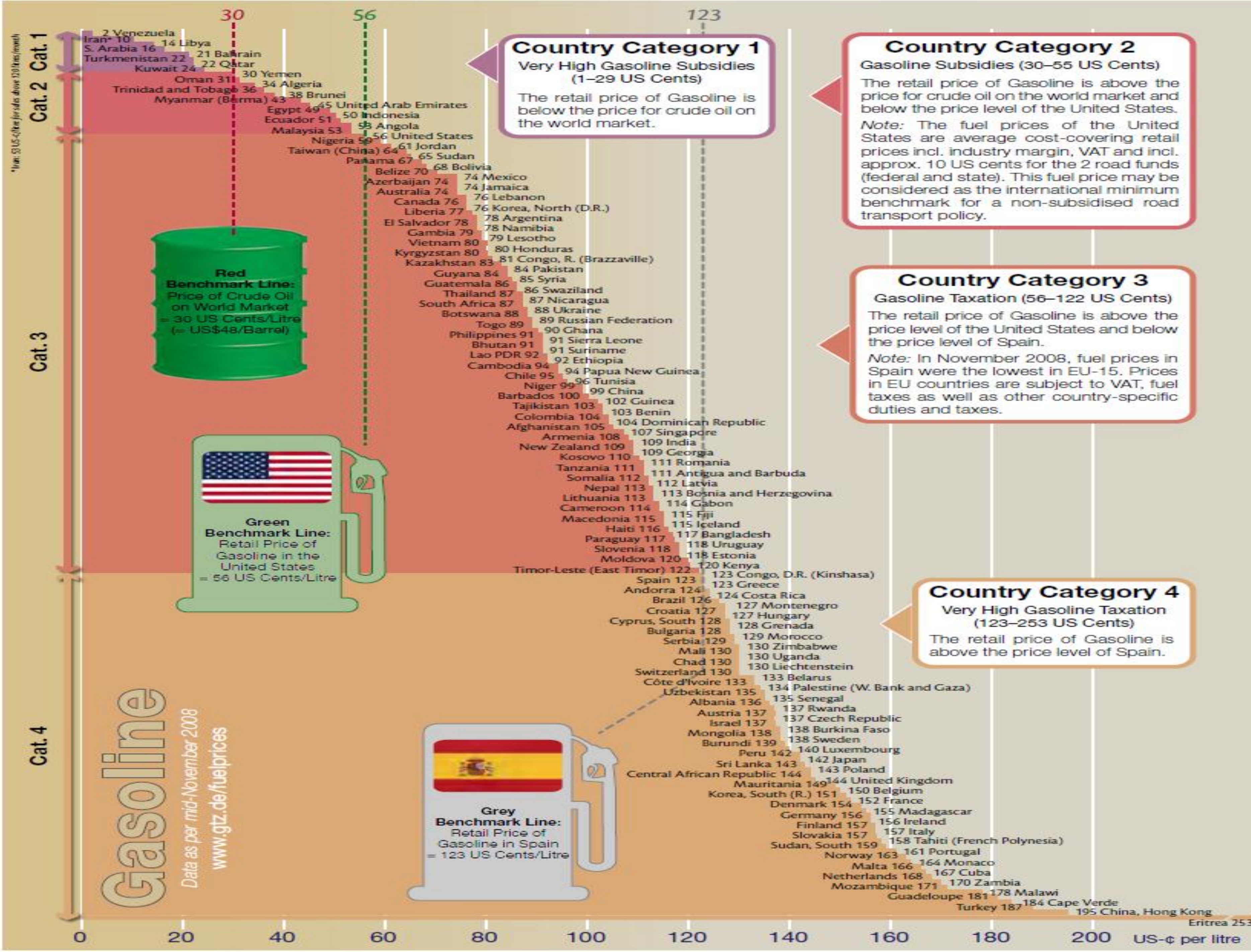
ii. In contrast, while the correlation coefficient is still positive in bad times, it is not statistically significant.

•**<u>Key Finding</u>: MENA oil exporters appear to have more scope to pursue expansionary fiscal policy than the MENA oil importers.**

Pricing of Public Utilities & Gov't Provided Commodities

- GCC countries heavily subsidise gasoline & diesel, water, power
- Subsidies have led to:
  - Surging domestic energy demand
  - Affects availability and product mix of oil exports
  - Consumption & production distortions
  - Environmental deterioration

- GCC countries should consider a 'carbon tax'



30
56
123
Cat. 1
Cat. 2
Cat. 3
Cat. 4
2 Venezuela
Iran* 10
14 Libya
S. Arabia 16
21 Bahrain
Turkmenistan 22
22 Qatar
Kuwait 24
Oman 31
30 Yemen
34 Algeria
Trinidad and Tobago 36
38 Brunei
Myanmar (Burma) 43
45 United Arab Emirates
Egypt 49
50 Indonesia
Ecuador 51
53 Angola
Malaysia 53
56 United States
Nigeria 59
61 Jordan
Taiwan (China) 64
65 Sudan
Panama 67
68 Bolivia
Belize 70
74 Mexico
Azerbaijan 74
74 Jamaica
Australia 74
76 Lebanon
Canada 76
76 Korea, North (D.R.)
Liberia 77
78 Argentina
El Salvador 78
78 Namibia
Gambia 79
79 Lesotho
Vietnam 80
80 Honduras
Kyrgyzstan 80
81 Congo, R. (Brazzaville)
Kazakhstan 83
84 Pakistan
Guyana 84
85 Syria
Guatemala 86
86 Swaziland
Thailand 87
87 Nicaragua
South Africa 87
88 Ukraine
Botswana 88
89 Russian Federation
Togo 89
90 Ghana
Philippines 91
91 Sierra Leone
Bhutan 91
91 Suriname
Lao PDR 92
92 Ethiopia
Cambodia 94
94 Papua New Guinea
Chile 95
96 Tunisia
Niger 99
99 China
Barbados 100
102 Guinea
Tajikistan 103
103 Benin
Colombia 104
104 Dominican Republic
Afghanistan 105
107 Singapore
Armenia 108
109 India
New Zealand 109
109 Georgia
Kosovo 110
111 Romania
Tanzania 111
111 Antigua and Barbuda
Somalia 112
112 Latvia
Nepal 113
113 Bosnia and Herzegovina
Lithuania 113
114 Gabon
Cameroon 114
115 Fiji
Macedonia 115
115 Iceland
Haiti 116
117 Bangladesh
Paraguay 117
118 Uruguay
Slovenia 118
118 Estonia
Moldova 120
120 Kenya
Timor-Leste (East Timor) 122
123 Congo, D.R. (Kinshasa)
Spain 123
123 Greece
Andorra 124
124 Costa Rica
Brazil 126
127 Montenegro
Croatia 127
127 Hungary
Cyprus, South 128
128 Grenada
Bulgaria 128
129 Morocco
Serbia 129
130 Zimbabwe
Mali 130
130 Uganda
Chad 130
130 Liechtenstein
Switzerland 130
133 Belarus
Côte d'Ivoire 133
134 Palestine (W. Bank and Gaza)
Uzbekistan 135
135 Senegal
Albania 136
137 Rwanda
Austria 137
137 Czech Republic
Israel 137
138 Burkina Faso
Mongolia 138
138 Sweden
Burundi 139
140 Luxembourg
Peru 142
142 Japan
Sri Lanka 143
143 Poland
Central African Republic 144
144 United Kingdom
Mauritania 149
150 Belgium
Korea, South (R.) 151
152 France
Denmark 154
155 Madagascar
Germany 156
156 Ireland
Finland 157
157 Italy
Slovakia 157
158 Tahiti (French Polynesia)
Sudan, South 159
161 Portugal
Norway 163
164 Monaco
Malta 166
167 Cuba
Netherlands 168
170 Zambia
Mozambique 171
178 Malawi
Guadeloupe 181
184 Cape Verde
Turkey 187
195 China, Hong Kong
Eritrea 253
Country Category 1
Very High Gasoline Subsidies (1–29 US Cents)
The retail price of Gasoline is below the price for crude oil on the world market.
Country Category 2
Gasoline Subsidies (30–55 US Cents)
The retail price of Gasoline is above the price for crude oil on the world market and below the price level of the United States.
Note: The fuel prices of the United States are average cost-covering retail prices incl. industry margin, VAT and incl. approx. 10 US cents for the 2 road funds (federal and state). This fuel price may be considered as the international minimum benchmark for a non-subsidised road transport policy.
Country Category 3
Gasoline Taxation (56–122 US Cents)
The retail price of Gasoline is above the price level of the United States and below the price level of Spain.
Note: In November 2008, fuel prices in Spain were the lowest in EU-15. Prices in EU countries are subject to VAT, fuel taxes as well as other country-specific duties and taxes.
Country Category 4
Very High Gasoline Taxation (123–253 US Cents)
The retail price of Gasoline is above the price level of Spain.
Red Benchmark Line: Price of Crude Oil on World Market = 30 US Cents/Litre (= US$48/Barrel)
Green Benchmark Line: Retail Price of Gasoline in the United States = 56 US Cents/Litre
Grey Benchmark Line: Retail Price of Gasoline in Spain = 123 US Cents/Litre
Gasoline
Data as per mid-November 2008
www.gtz.de/fuelprices
0
20
40
60
80
100
120
140
160
180
200
US-¢ per litre

Taxation in GCC: stylised facts

- In the GCC region, non-oil taxation is low, consisting mainly of income tax on foreign corporations—except in Oman, where local corporations are also taxed.
  - Oman, Qatar, Kuwait and Saudi Arabia have in recent years initiated tax reforms by reducing corporate tax rates.
  - For instance, Kuwait has reduced corporate tax from a high of 55% to 15%, Oman from 30% to 12%, Qatar from 35% to 10% and Saudi Arabia from 30% to 20%.
  - The UAE and Bahrain are largely tax-free jurisdictions.
  - No corporate income tax, capital gains tax or withholding tax rates are imposed by the UAE Government (except for taxation of profits of foreign banks), although most of the individual Emirates have issued corporate tax decrees, which theoretically apply to all businesses established in the UAE.
- Issues:
  - Current tax regimes do not provide revenue buoyancy or broad based revenue source
  - What is the best form and source of taxation?
  - How to address tax equity in the presence of large, mobile, expatriate communities?

GCC: Fiscal Policy Issues

1. Diversify revenue sources away from dependence on oil revenues
2. Replace and develop alternatives to trade taxes (custom duties) to increase openness & maintain competitiveness
3. Finance infrastructure –including maintenance- on a sustainable basis
4. Provide efficient, equitable pricing of public services & utilities
5. Maintain foreign investment tax attractiveness in order to support economic diversification policies

GCC Fiscal Reform is Imperative, Medium Term

- GCC economies are maturing: they require stable, wide-based sources of revenue to finance investment & economic development requirements: argues in favour of VAT or a General Sales Tax (less preferable)
- Fiscal policy has been perverse: largely pro-cyclical and therefore aggravating the boom-bust cycle resulting from oil price fluctuations.
- Recent global crisis and its consequences for the GCC demonstrated the need for developing new tools to support counter-cyclical fiscal policy
- Develop Public Debt Markets & Management to:
  - Allow governments to smooth volatile energy revenues
  - Enable conduct of counter-cyclical policies, including deficit financing
  - Finance infrastructure and public works

1. Separation of Energy Wealth from Government Revenues

2. Diversification of Government Revenues

3. Phasing Out Oil Subsidies

4. Developing Public Debt Markets & Management

Thank You!

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