

Where is MENA Heading? Growth, Turmoil & Transformation

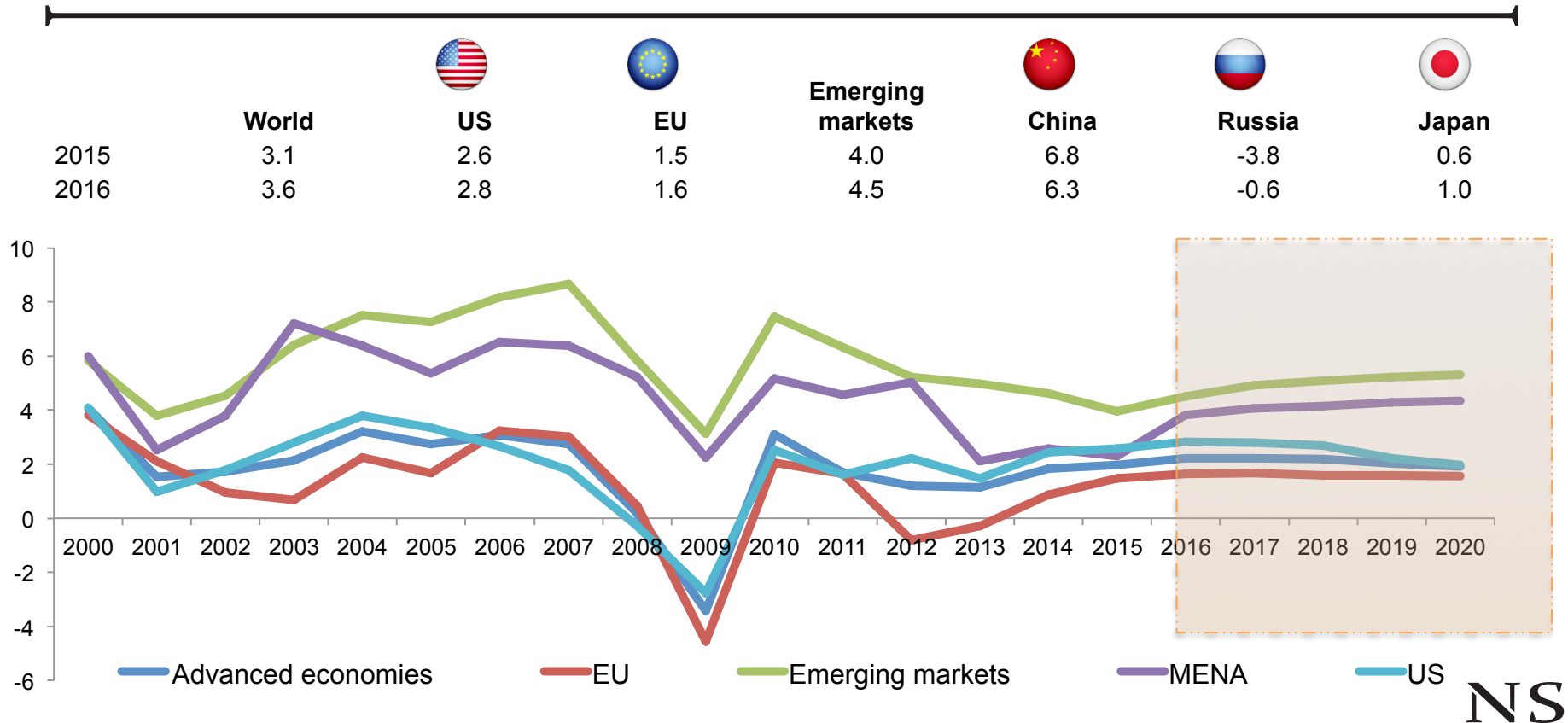
*Moving Forward
Baker Tilly International World Conference
11 October 2015*

Dr. Nasser Saidi

Agenda

- ✓ **Shifting Global Economic Geography & New Oil Normal**
- ✓ Regional Economic Fundamentals & Developments
- ✓ MENA Transformational factors & “Game Changers”
- ✓ Key Takeaways

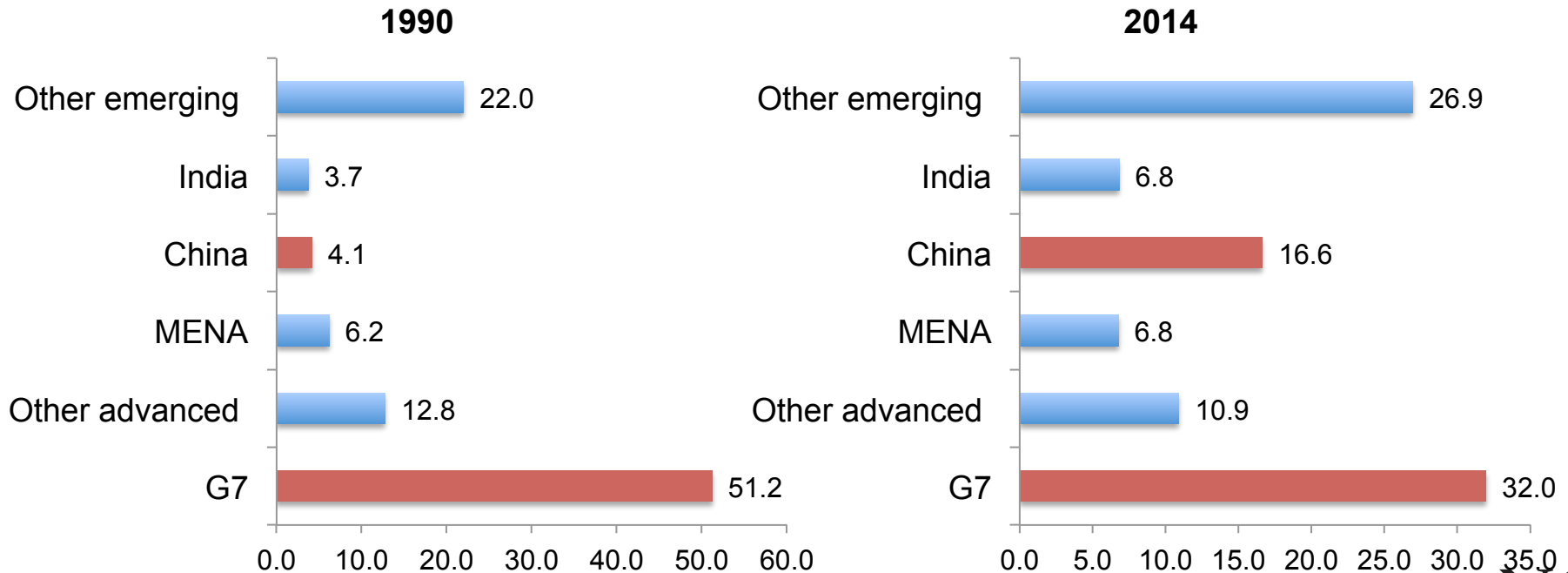
Global Recovery is Fragile & Uneven; 'Secular Stagnation' & New Economic Geography



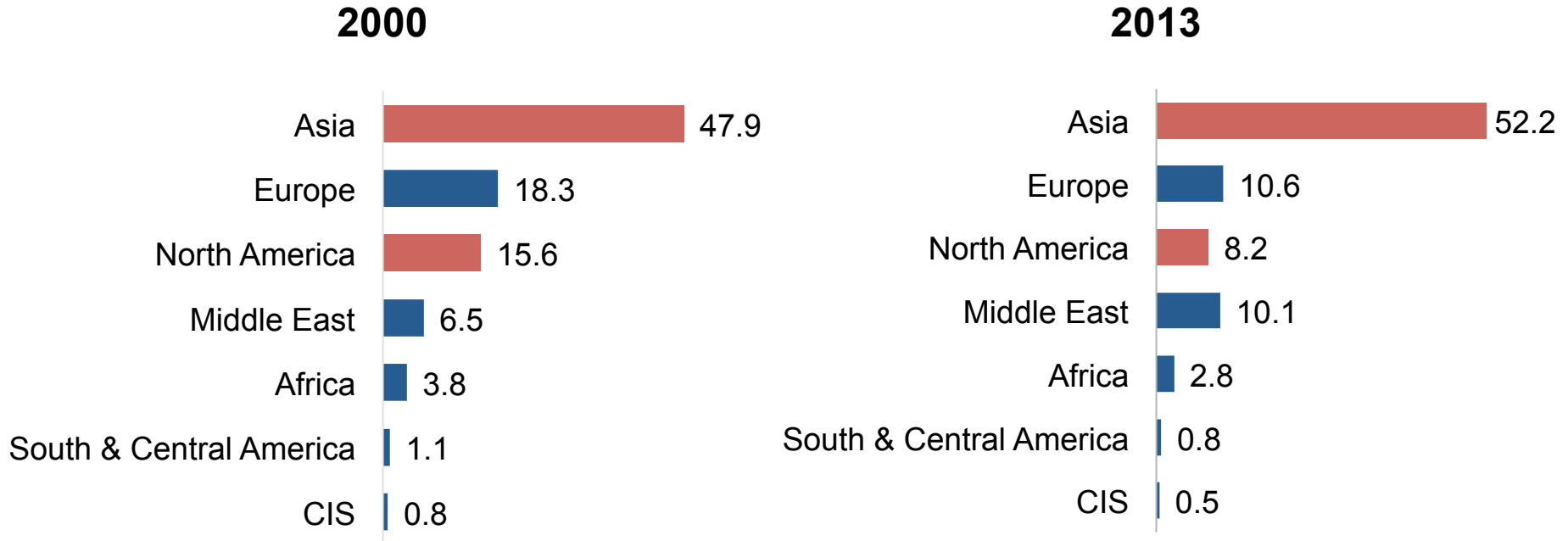
Source: IMF WEO, Oct 2015. GDP growth in yoy terms, shaded area denotes forecasts.

Tectonic Shift in global economic geography towards EMEs, Asia/China

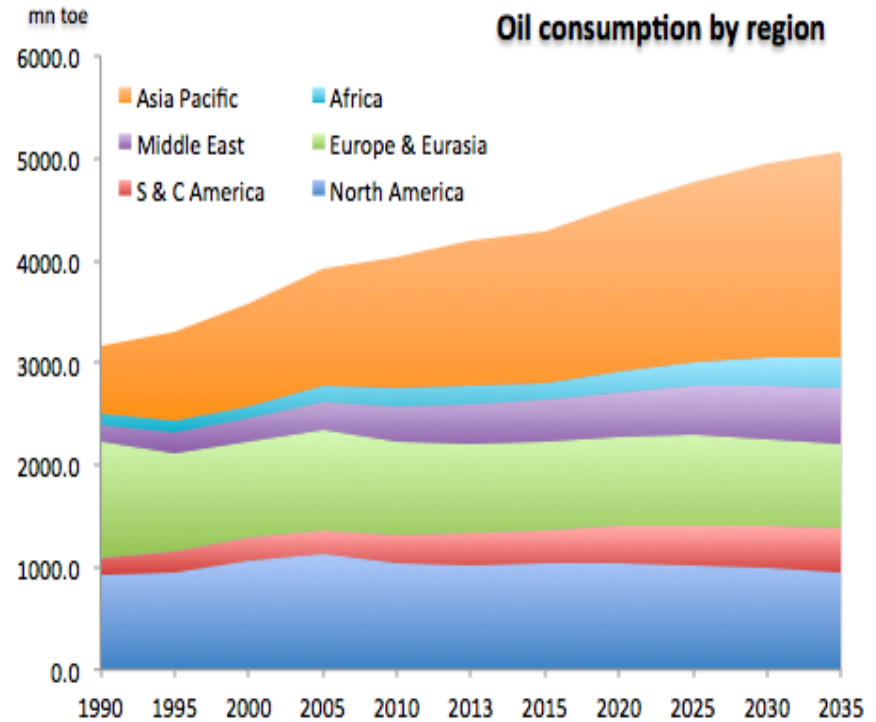
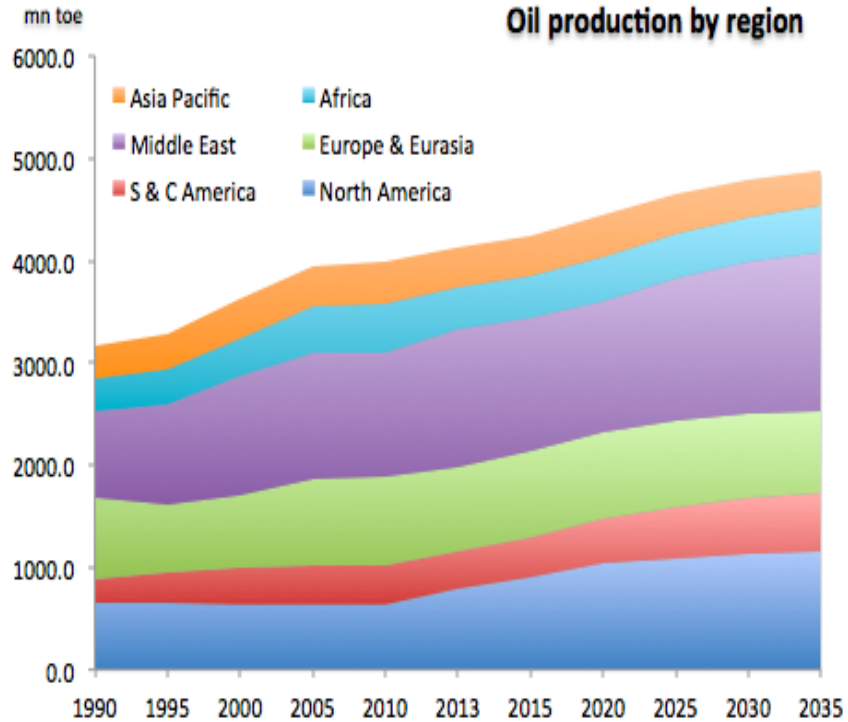
Shares of world total GDP based on purchasing power parity



Asia became Middle East's main trade partner; China main oil importer

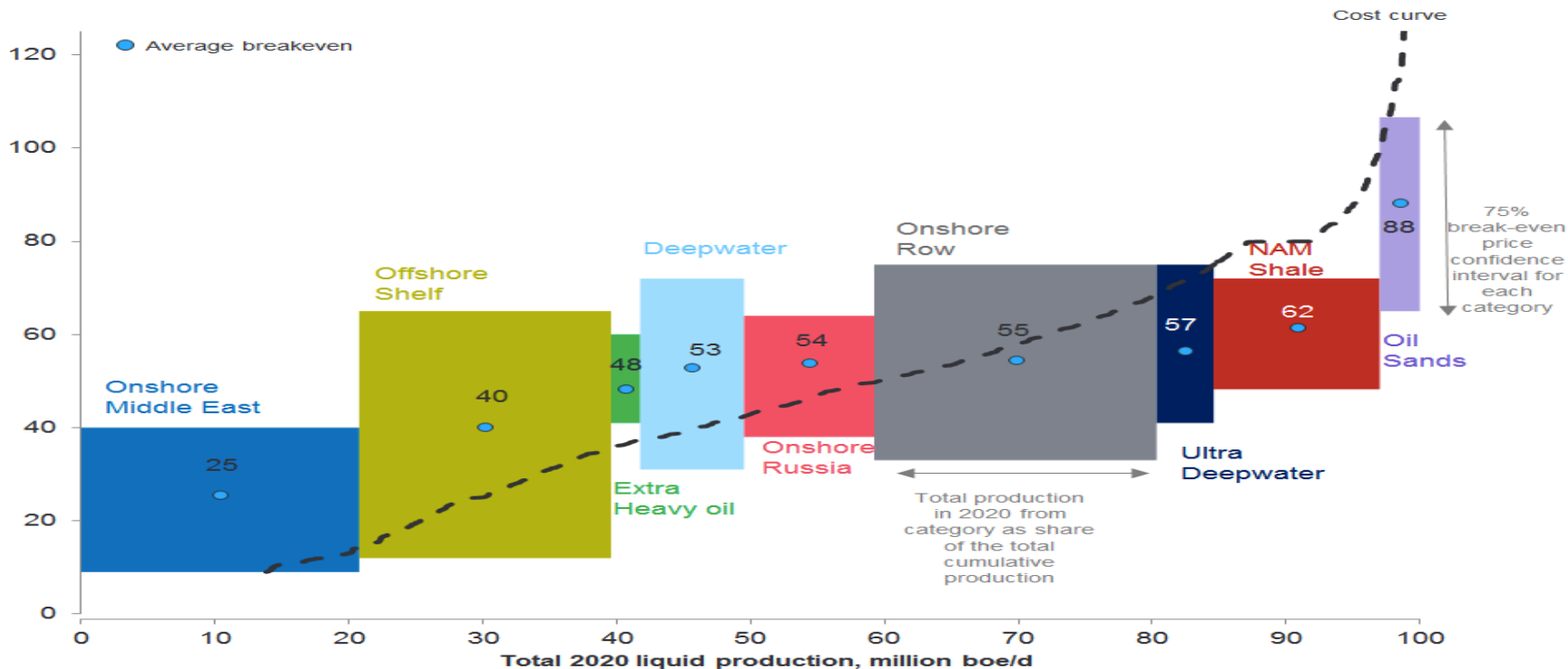


“New Oil Normal”: demand dynamics dominated by EMEs; new sources of supply



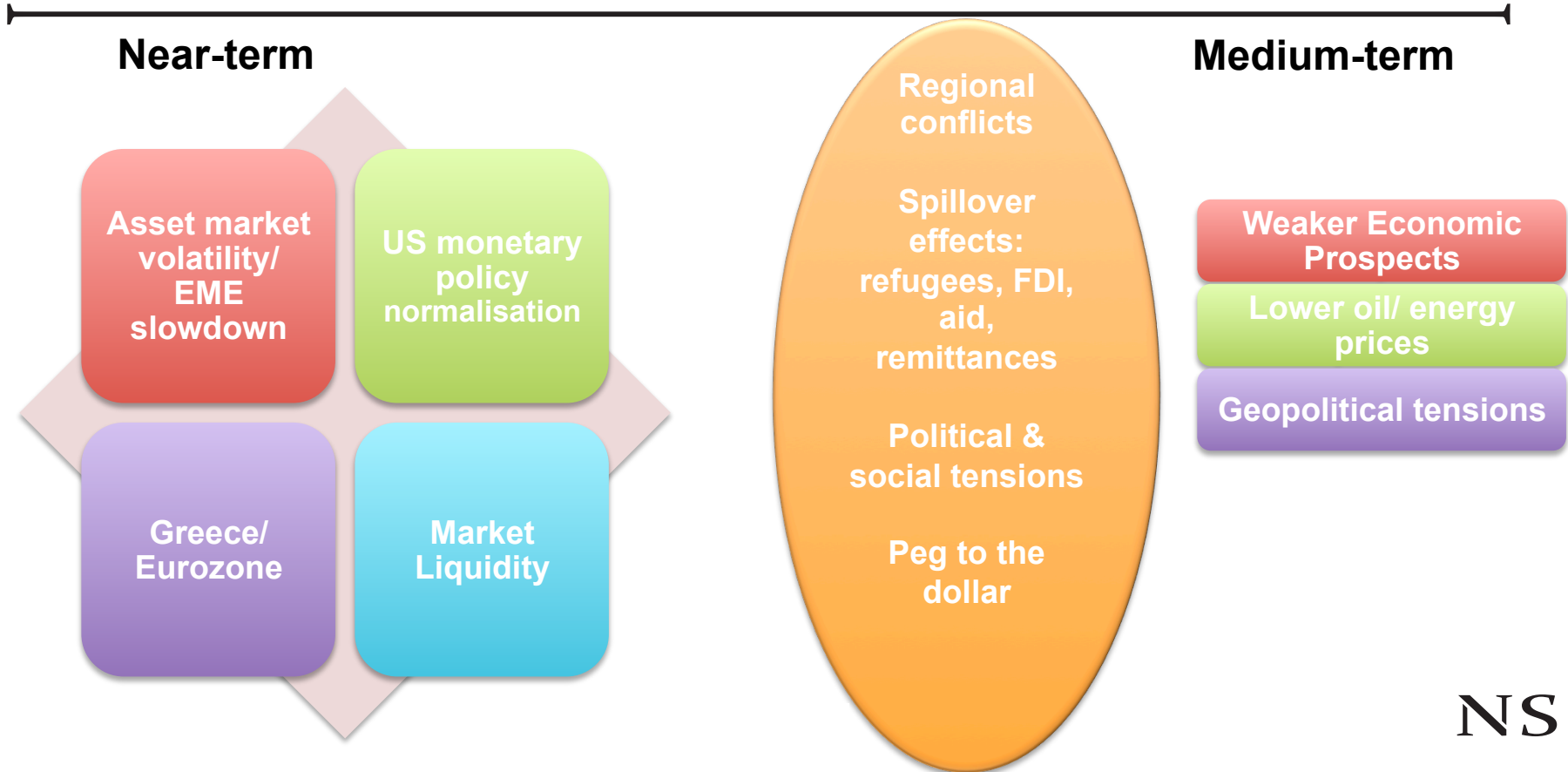
“New Oil Normal”: OPEC aims to drive out competition. Disruptive technology driving costs down for shale, RE

Global liquid supply cost curve
USD/bbl



Source: Rystad Energy estimates, Jan 2015

Risks facing MENA economies



Implications of changing Global Economic Geography for the GCC

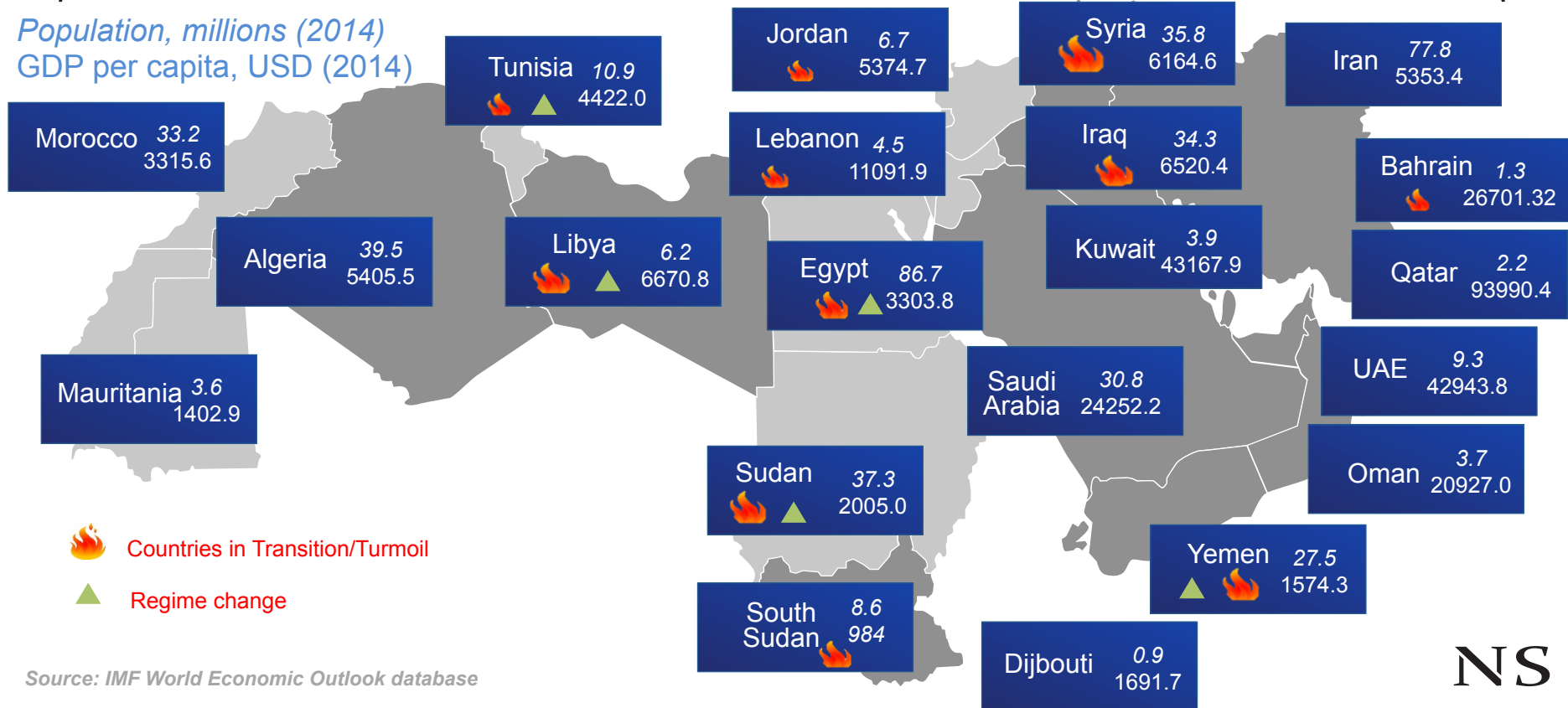
1. Rising levels of South-South trade, investment & tourism; Asia/China key players in New Global Value Chains
2. GCC economies benefiting from geographical proximity to Africa & Near Asia & increasingly integrated into 'Silk Road Economic Belt'
3. Structure & economics of energy markets has radically changed: "New Oil Normal"
4. Redback Zone emerging: Chinese Yuan will be 3rd global currency & used for energy trade; GCC peg to US\$ will come under pressure

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MENA: 47.7% of world's proven oil reserves & 42.7% of proven natural gas resources but wide inequality in wealth, resources & incomes. Many countries in turmoil

Population, millions (2014)
GDP per capita, USD (2014)



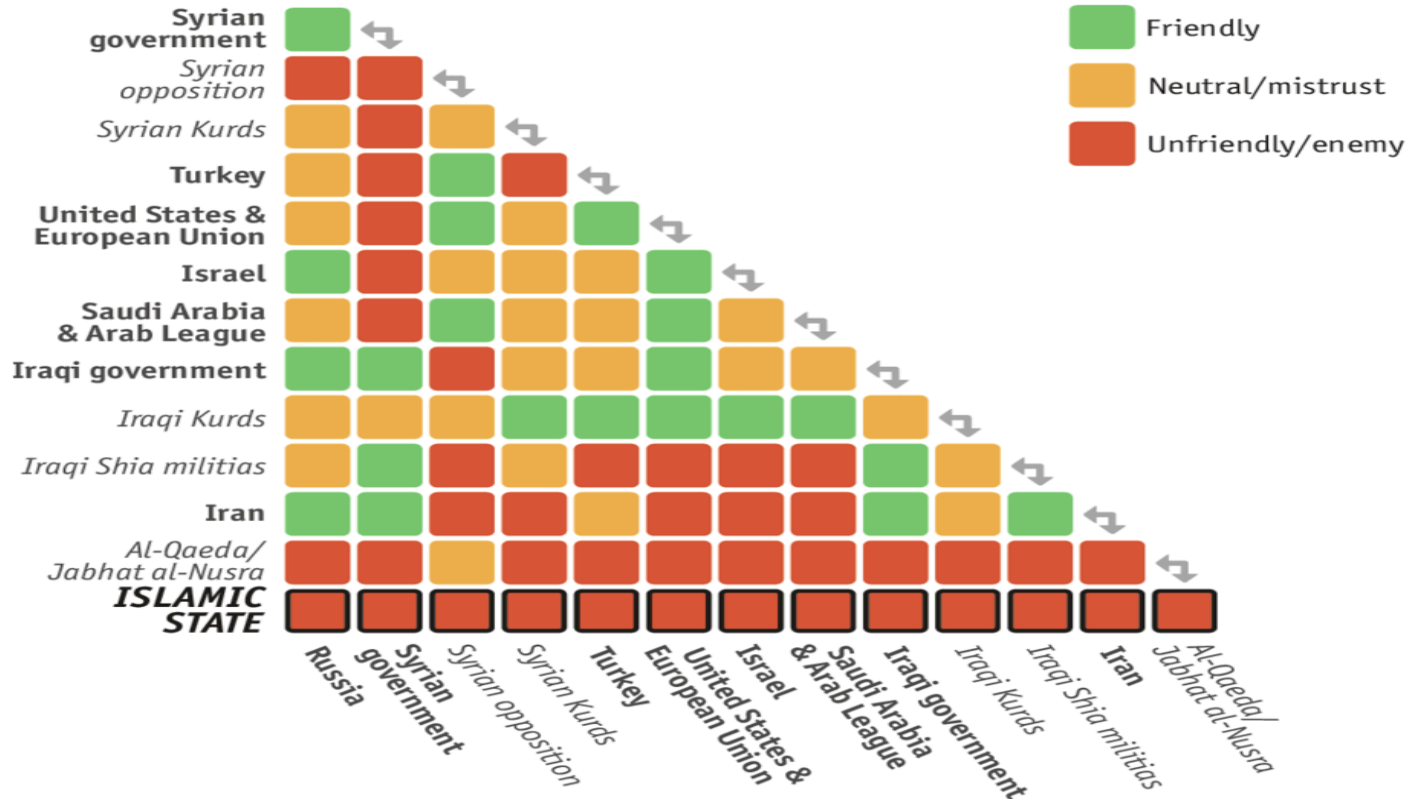
Source: IMF World Economic Outlook database

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Impact of Conflicts

- **Conflicts lead to:**
 - ✓ Destruction of physical & human capital; Contraction of output
 - ✓ Population displacement: internal & external
 - ✓ Large fiscal and current account deficits & loss of international reserves
 - ✓ Acceleration of inflation
 - ✓ Weaker financial systems
 - ✓ Spillovers into neighbouring countries (trade, tourism, migration flows, investment & fiscal pressures) => regional uncertainty
- Conflict countries take average 4-5 years **to recover from** start of conflict
- Of 9.2mn **displaced refugees** in 2014, 5.2mn stayed within the region

Geo-Political Landscape: عدو عدوي هو صديقي أنا وأخي على ابن عمي وأنا وابن عمي على الغريب



Source: The Economist (<http://www.economist.com/blogs/graphicdetail/2014/09/daily-chart-11>)

Arab Firestorm: Fault Lines

MENA region going through a historic transition period starting with fall of Ottomans & unraveling of Sykes-Picot (1916) with many 'fault lines':

✓ Role of Islam in Politics; 'Mosque or Secularism'?

✓ Growing Sunni-Shia Schism: a "Thirty Years War?"

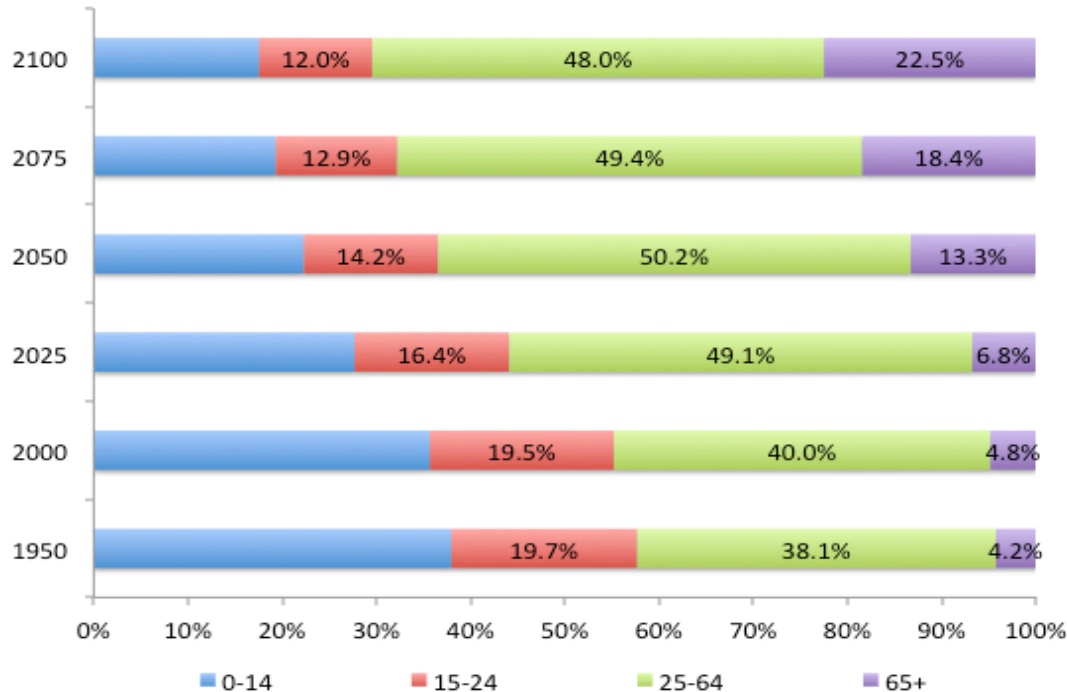
✓ Role of Government in Economy

✓ Urban-Rural Divide

✓ Role of Army/Security Forces in Politics

Arab countries experiencing a Youth Bulge: Demographics dominate growth prospects

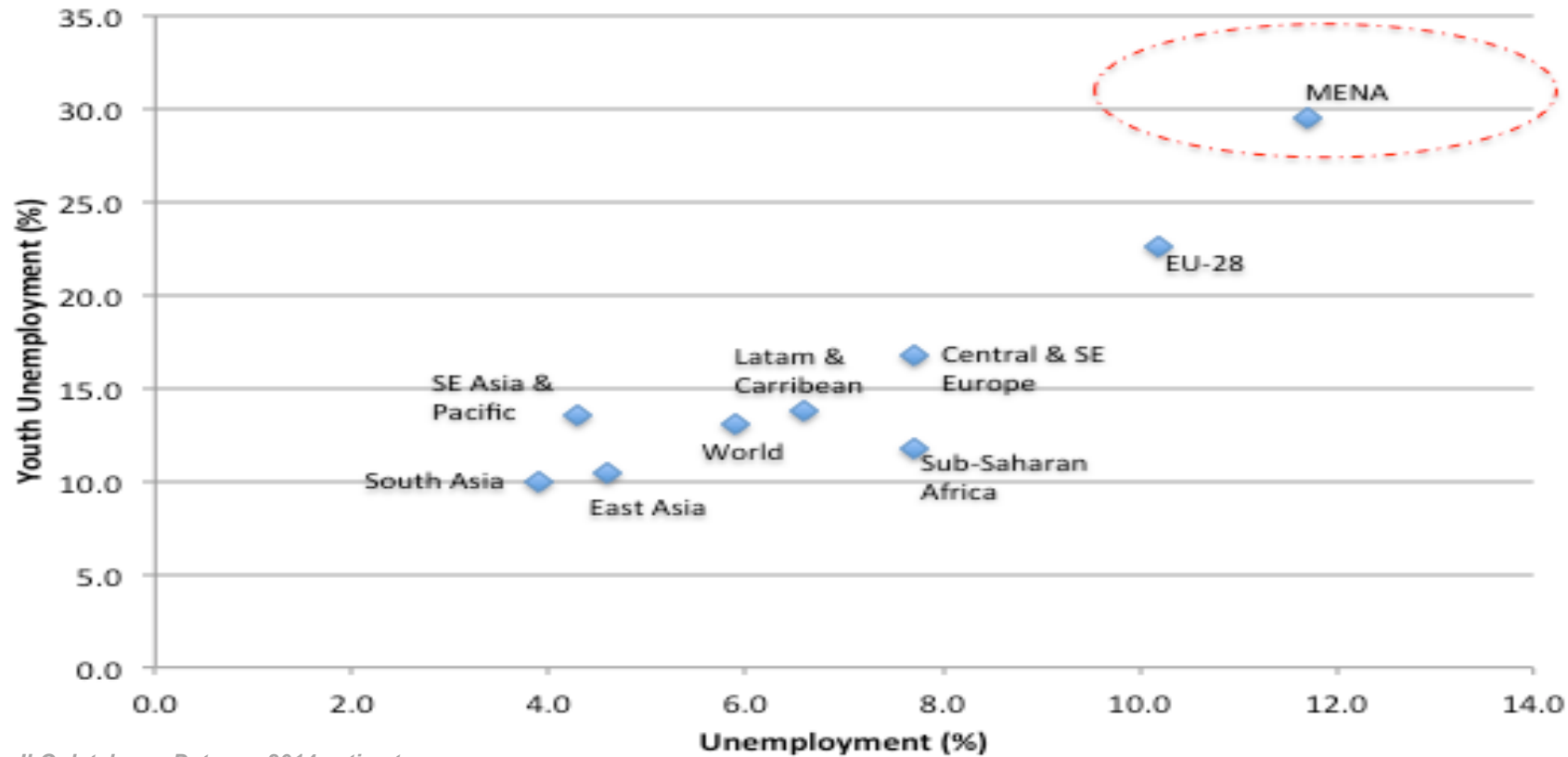
Arab Countries Population Age Distribution



Source: UN World Population Prospects 2015 revision

- **Population:** 257mn in 2015, rise to ~500 mn by 2100; ~50% < 24yrs, ~60% < 30yrs
- **Youth unemployment rate** is 3.7 times higher than for adults
- **Young women unemployment rate** twice higher than young men
- **Jobs:** need to create 100mn new jobs by 2020 or 130 if female LFPR rises to 50% of male LFPR
- **Growth rates** of 6%-7.5% p.a. needed to create jobs

ME has world's highest levels of youth & overall unemployment: Job Creation Priority!



Source: ILO database; Data are 2014 estimates

MENA macroeconomic outlook: growth below potential amidst turmoil & lower oil prices

	Real GDP			Consumer Prices			Current Account Balance		
	2014	2015f	2016f	2014	2015f	2016f	2014	2015f	2016f
Oil Exporters	2.6	1.8	3.8	5.6	5.8	5.1	8.9	-3.4	-4.3
Saudi Arabia	3.5	3.4	2.2	2.7	2.1	2.3	10.3	-3.5	-4.7
UAE	4.6	3.0	3.1	2.3	3.7	3.0	13.7	2.9	3.1
Iran	4.3	0.8	4.4	15.5	15.1	11.5	3.8	0.4	1.3
Oil Importers	2.9	3.9	4.1	9.1	7	6.1	-4.2	-4.2	-4.2
Egypt	2.2	4.2	4.3	10.1	11.0	8.8	-0.8	-3.7	-4.5
Morocco	2.9	4.9	3.7	0.4	1.5	2	-5.5	-2.3	-1.6
MENA	2.6	2.3	3.8	6.5	6.5	5.5	6.1	-4.0	-4.7
Maghreb	0.7	2.5	3.6	2.5	3.9	4	-8.1	-15.8	-13.8
Mashreq	2.2	3.9	4.1	8.9	9.4	7.8	-4.6	-6.3	-6.6

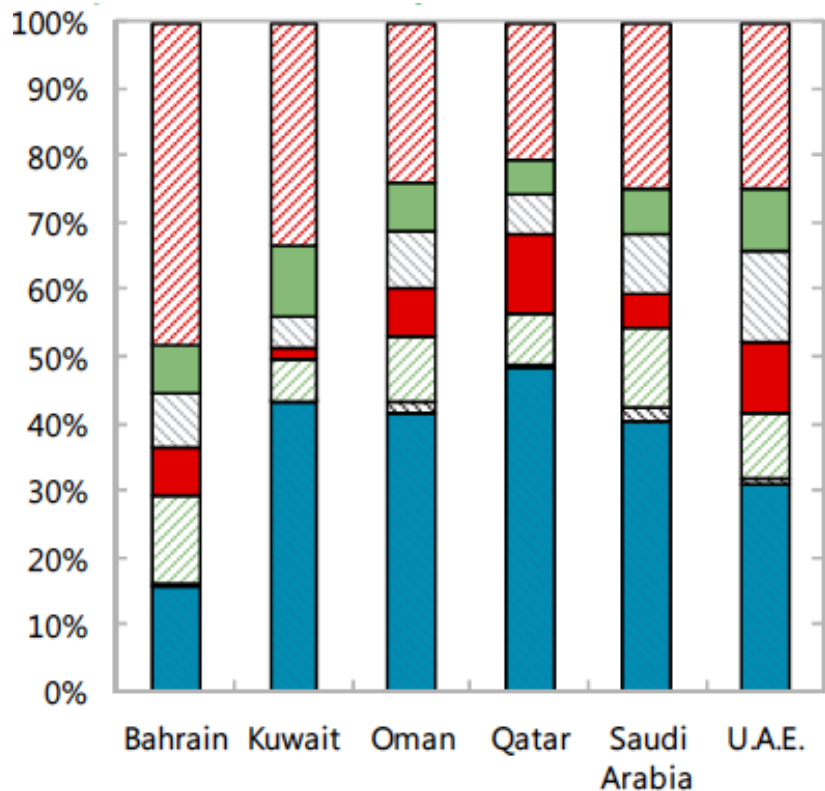
GCC: Economic Policy Challenges

New Oil Normal necessitates New Development Model

- 1. Economic Diversification**
- 2. Fiscal Reform & Government Revenue
Diversification**
- 3. Fossil fuel energy subsidies**
- 4. Food & Water Security**

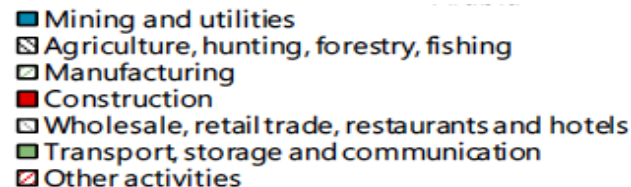
Economic Diversification requires shift to non-oil private sector for job creation

Composition of Real GDP by Sector



What is required?

- Privatisation & PPP
- Integrate into “New Silk Road”
- Need removal of barriers to competition; liberalisation; avoid “crowding out”
- Greater regional integration: FTAs; regional reconstruction

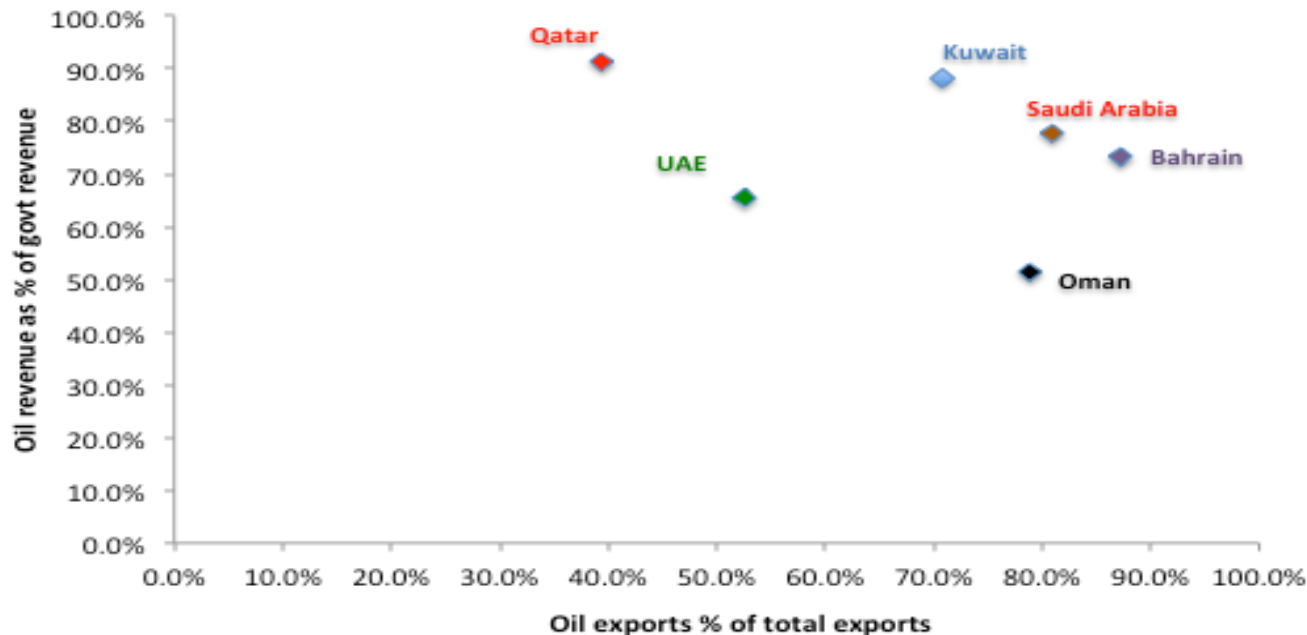


Source: “Economic Diversification in the GCC: The Past, the Present, and the Future” IMF Staff Discussion Note Dec 2014

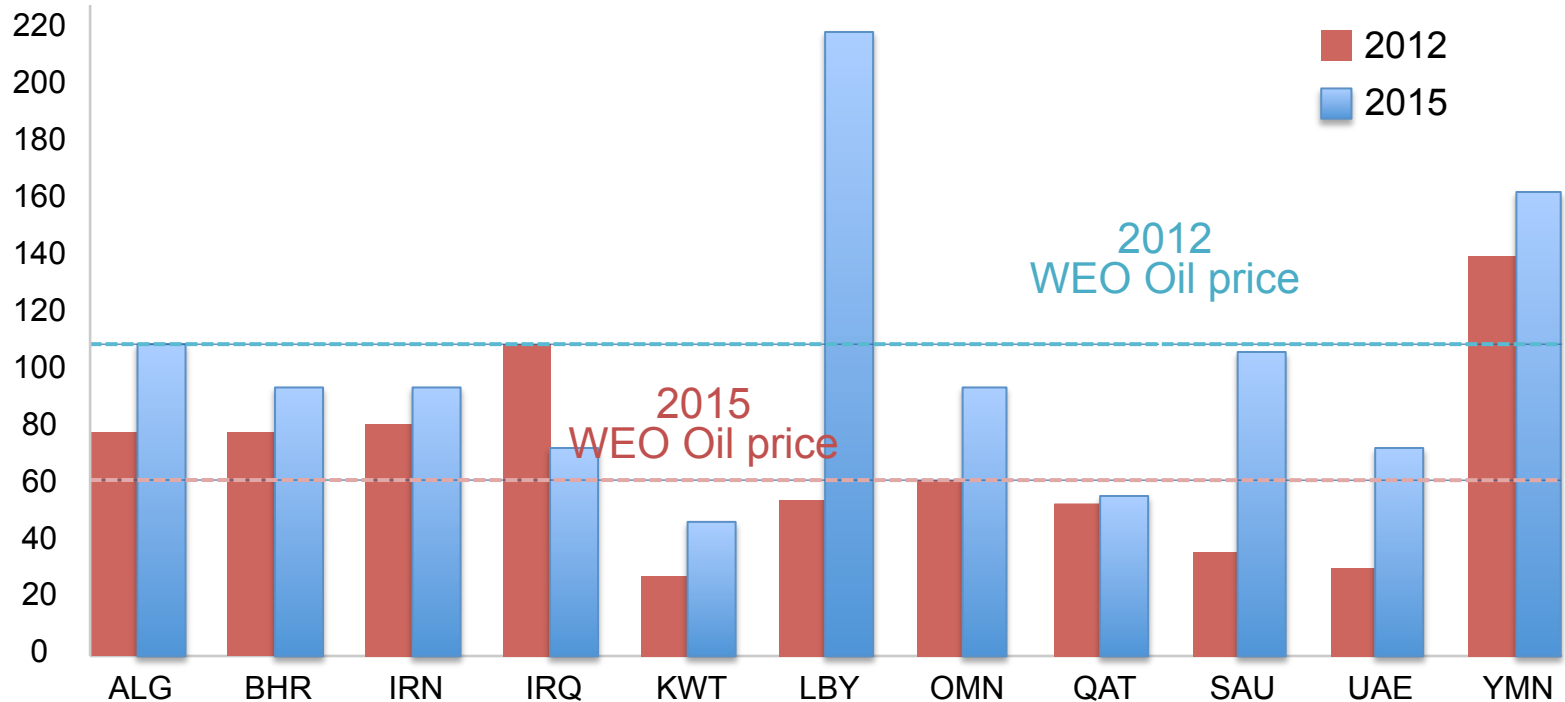
GCC Fiscal Reform: Consolidation required with increased Revenue Diversification

Hydrocarbon Dependence Generates External & Internal Vulnerabilities

Hydrocarbon dependence in GCC



Fiscal Breakeven Prices rising since Arab Spring: all except Kuwait & Qatar running deficits @ \$60



Consequences of lower oil prices amidst high oil dependence

- Large budget deficits; spending delays

GCC	Avg. 2000-11	2012	2013	2014	2015f	2016f
Budget bal (% of GDP)	12.4	15.1	12.1	4.6	-7.9	-3.6
Current account bal (% of GDP)	16.5	24.4	20.6	16.5	2.8	5.4

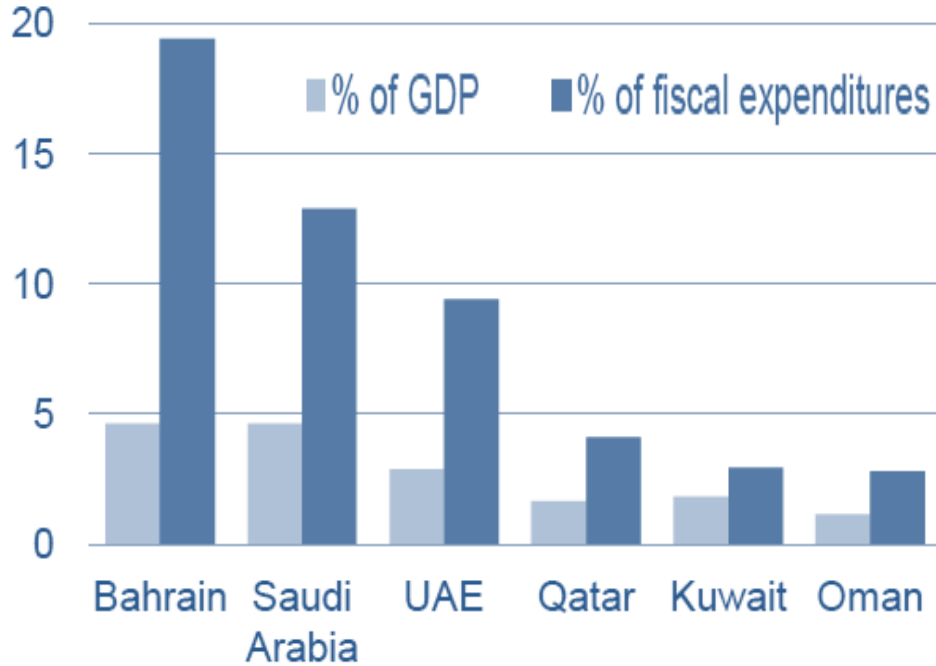
- Declining accumulation or drawdown of international reserves & net foreign assets
- Draw-down of fiscal buffers => decline in bank liquidity and lower credit growth
- Danger of financial crowding out as governments start borrowing from domestic banks and raising rates

GCC Economic Policy Reforms for Fiscal Sustainability

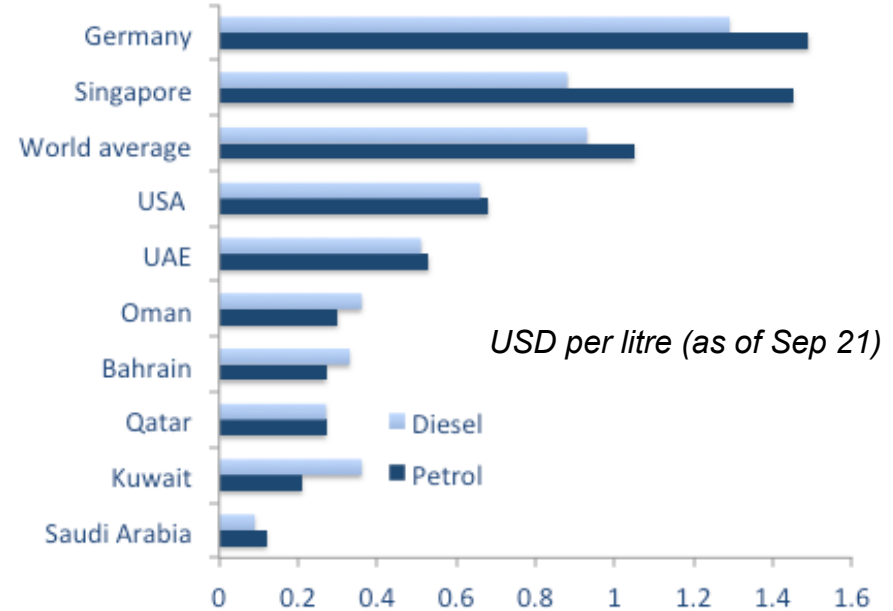
- 1. GCC economies require new fiscal policy tools for economic policy management:**
 - Broad-based taxation for fiscal stability & to provide elastic, buoyant sources of revenue: VAT/GST
 - Corporate Income Tax
 - Property Taxation
 - Excise Taxes on selected products: alcohol, gasoline, diesel, tobacco, automobiles
- 2. Use financial markets for development & infrastructure finance**
- 3. Efficient, equitable pricing of public services & utilities**
- 4. Maintain tax attractiveness** for investment & to support economic diversification policies
- 5. *Caveat emptor*:** Need to establish Tax & Revenue Agencies; Private sector needs training and investment in tax accounting, reporting & compliance

Fossil Fuel Subsidies need to be phased-out: distort production & consumption choices

Subsidies weigh on fiscal balances



Retail fuel prices heavily subsidised in UAE's GCC peers



USD per litre (as of Sep 21)

■ Diesel
■ Petrol

Water & Food In-Security

- **GCC has among lowest renewable water resources**; bulk of region's water is mismanaged & directed to agriculture contributing 5% of GDP
- **Challenges ahead:** 'Water Wars'; aquifer depletion; over-exploitation of freshwater resources; climate change & large carbon footprint
- **Growing reliance on desalinated water** (expensive & energy-intensive); GCC accounts for more than 40% of the world's water desalination capacity
- **Reforms required:**
 - Invest in efficient & effective water management systems; reform pricing
 - Review food security policies; Reform agriculture support policies;
 - Improve water efficiency of agriculture & all other activities

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Region at a turning point: way forward & game changers

1. Region-wide Infrastructure Investment & Reconstruction Programme
2. Building & Development of Local Financial Markets
3. Empowerment of Women
4. Rising Importance of the Islamic Economy
5. Détente with Iran

MENA Infrastructure investment gap: ~\$72bn annual shortfall

Five key infrastructure sectors



1. Extraction

- Oil and gas
- Other extraction (coal, metals, minerals)



2. Utilities

- Power generation
- Electricity T&D
- Gas
- Water
- Telecoms



3. Manufacturing

- Petroleum refining
- Chemical
- Heavy metals



4. Transport

- Rail
- Roads
- Airports
- Ports



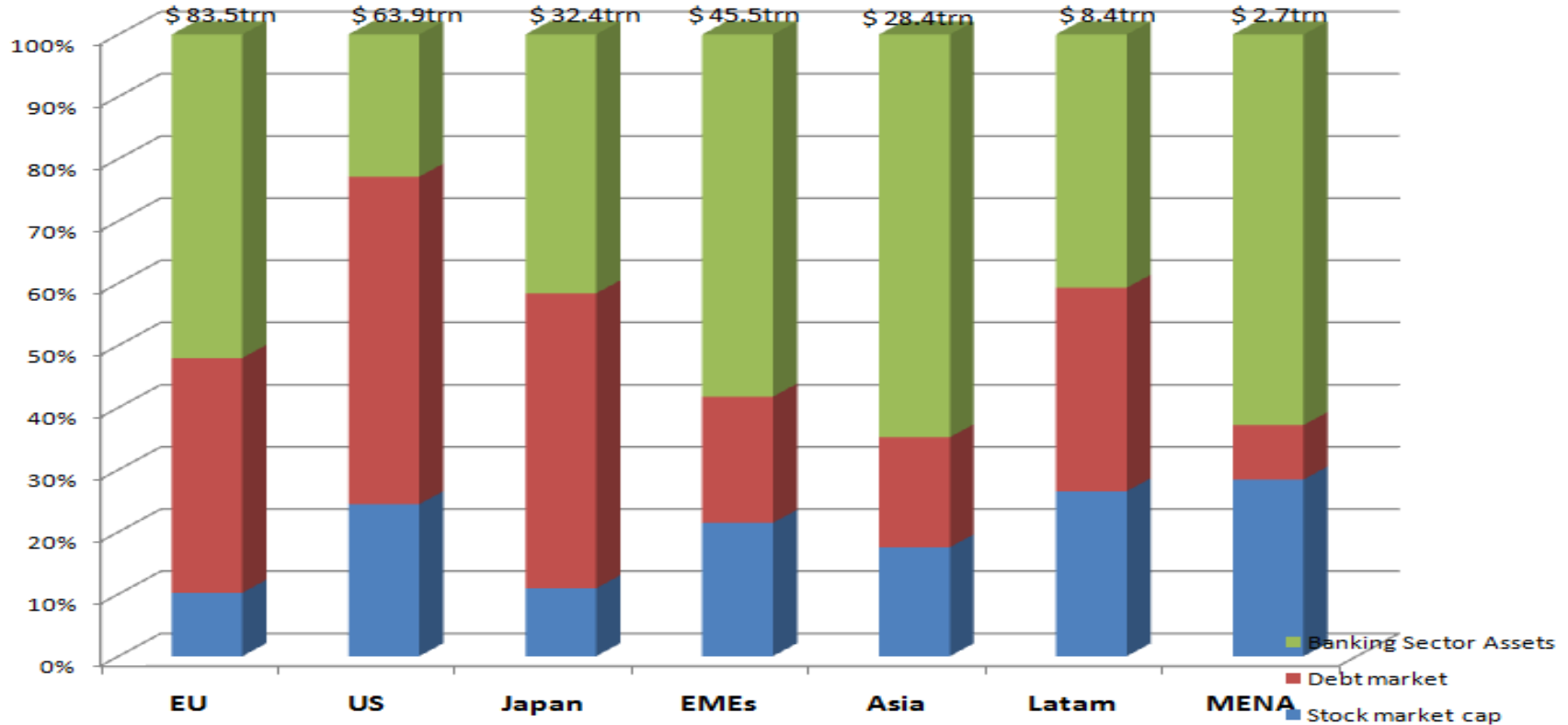
5. Social

- Hospitals
- Schools

Why investment in infrastructure?

- Job creation: create ~2.5 mn direct, indirect & induced infrastructure-related jobs in MENA
- Boost growth: by some 3%-pts among non-GCC oil exporters & ~1.5%-points among MENA oil importers in the short-term
- Rapid population growth + urbanisation
- Climate change => investments in water resources, renewable energy, & clean tech
- Technological breakthroughs & Innovation (shale, RE, desalination, mobile payments, smart cities etc.)

Banks continue to dominate the financial structure in MENA

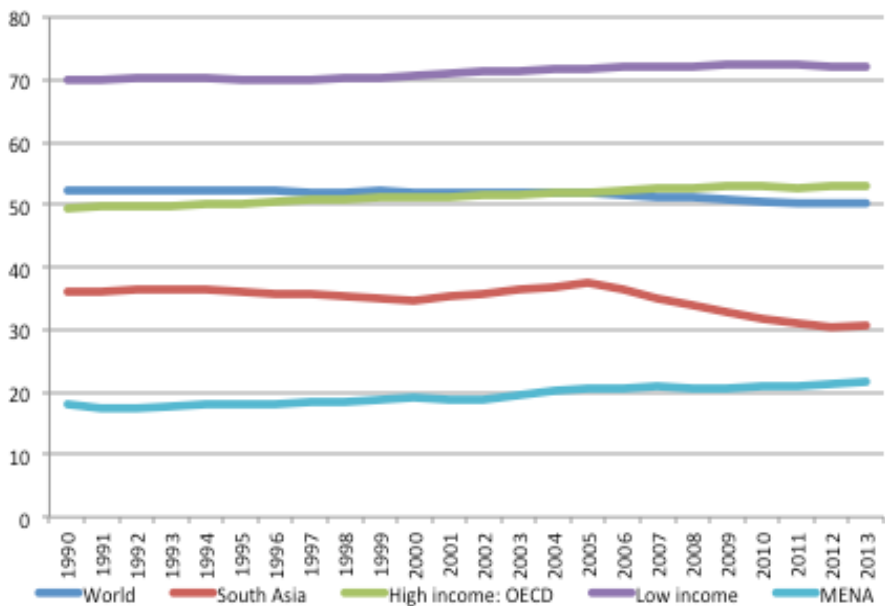


Local Financial Market Development

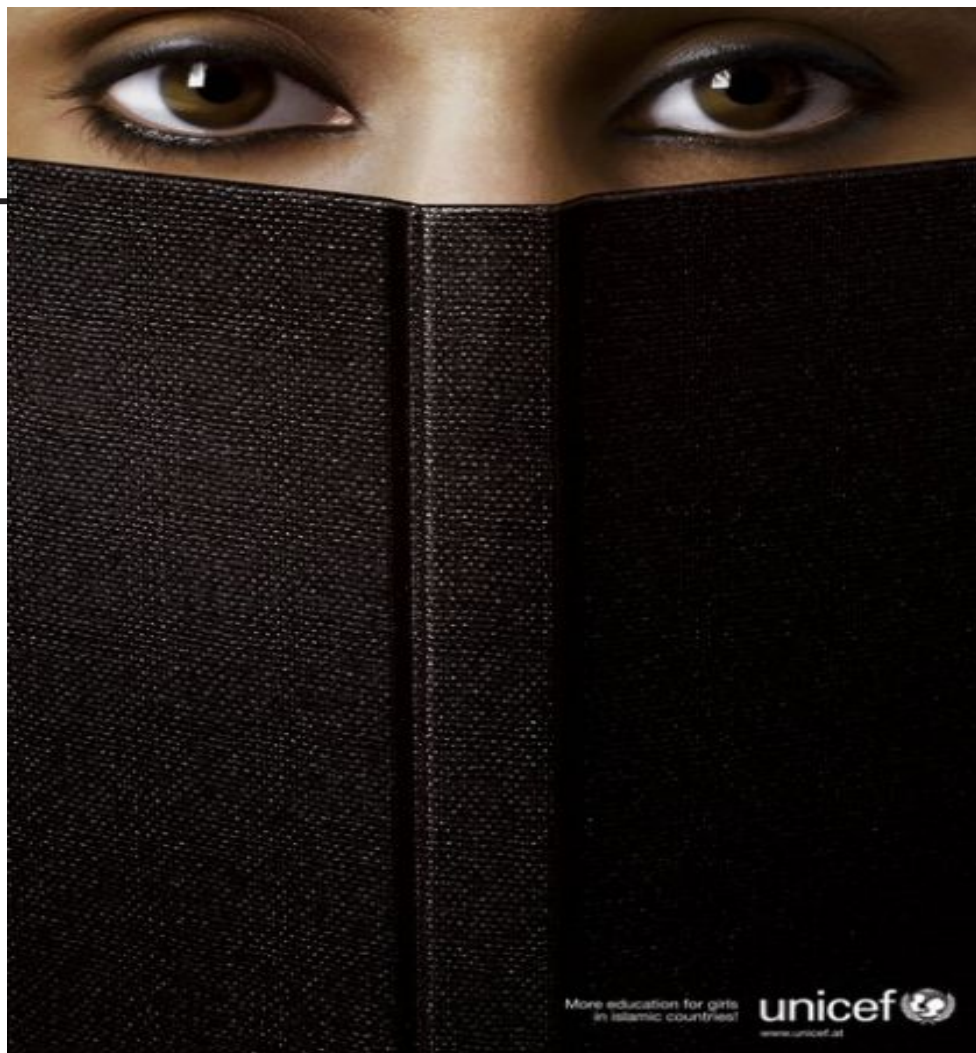
- Opening up of markets & liberalization can fuel growth
- MSCI Reclassification of Qatar, UAE can be transformational: attract institutional investors, encourage IPOs & privatisation, improve governance & liquidity
- Saudi liberalisation & opening up: Tadawul opened doors to foreign investors in June 2015. Reclassification in 2016?
- Scope for additional reforms is large:
 - Consolidation of GCC stock markets
 - Creation of Government debt & Sukuk markets
 - Improve corporate governance, transparency & disclosure
 - Build an institutional investor base: pension systems; insurance

Women, Education, Labour: MENA Lowest LFPR


Female Labour Force Participation 1990–2013



Source: World Bank database



More education for girls
in Islamic countries!

unicef 
www.unicef.org

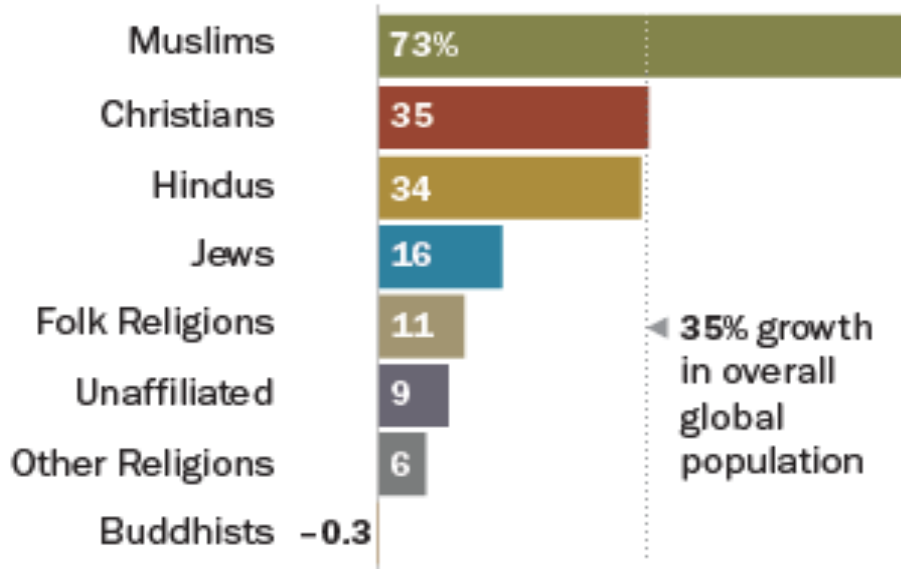
Reduction in MENA LFPR gap would generate a growth explosion!

			Projected average annual growth rate in GDP		
	Male LFPR	Female LFPR	Male and female LFPR gap reduced by 50%, by 2030	Male and female LFPR gap reduced by 75%, by 2030	Male and female LFPR gap reduced by 100%, by 2030
Algeria	75.4	15.7	8.73	9.25	9.78
Bahrain	88.5	40.6	7.00	7.42	7.85
Egypt	78.1	25.3	7.72	8.18	8.65
Iraq	71.7	15.2	8.26	8.76	9.26
Jordan	68.9	16.3	7.69	8.15	8.62
Kuwait	84.5	44.7	5.82	6.17	6.52
Lebanon	75.3	24.8	7.38	7.83	8.28
Libya	79.9	32.0	7.00	7.42	7.85
Morocco	78.3	26.4	7.59	8.04	8.50
Oman	81.6	29.2	7.66	8.12	8.59
Palestinian Authority	68.6	15.4	7.78	8.25	8.72
Qatar	95.6	53.0	6.23	6.60	6.98
Saudi Arabia	76.1	18.3	8.45	8.96	9.47
Syrian Arab Republic	74.7	13.7	8.92	9.46	10.00
Tunisia	74.0	27.5	6.80	7.21	7.62
United Arab Emirates	92.4	44.0	7.07	7.50	7.93
Yemen	73.6	25.8	6.99	7.41	7.83

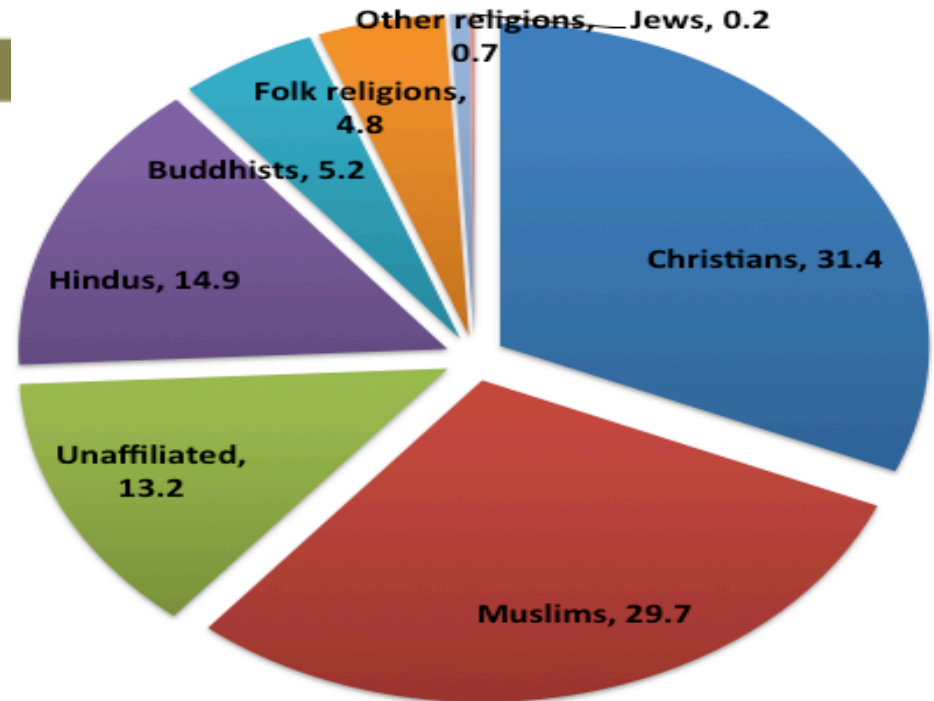
Source: Nasser Saidi & Associates (based on OECD estimates)

Rise Of Islam: Muslims are fastest growing religious group; 34% are below 15 Years

Estimated change in population size, 2010-2050



Share of Population, 2050



Islamic Finance & Halal Food: Large Growth Potential

Dubai aims to develop & promote the emirate as global capital of Islamic economy

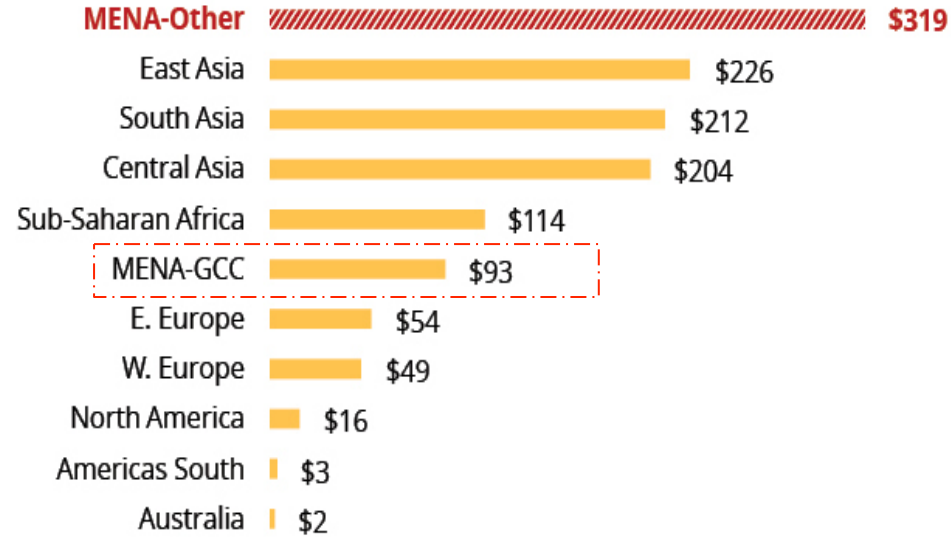
What countries have the best developed Islamic economy for Islamic finance?

TOP 10

- 1 Malaysia
- 2 Bahrain
- 3 United Arab Emirates
- 4 Oman
- 5 Saudi Arabia
- 6 Kuwait
- 7 Qatar
- 8 Pakistan
- 9 Jordan
- 10 Indonesia



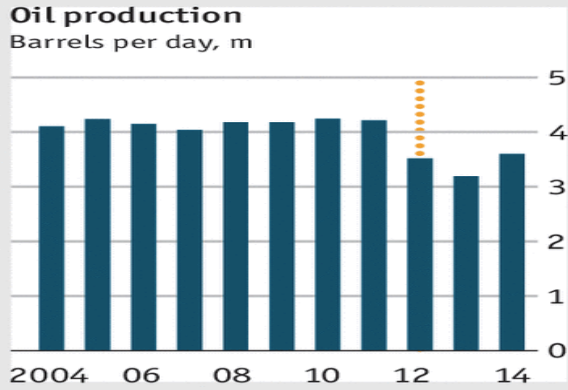
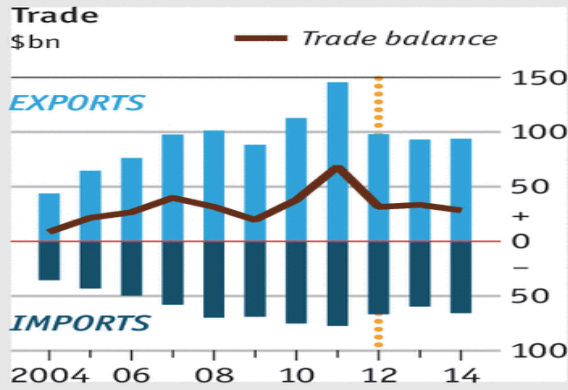
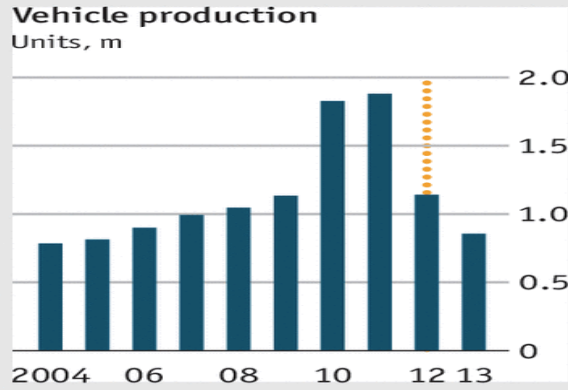
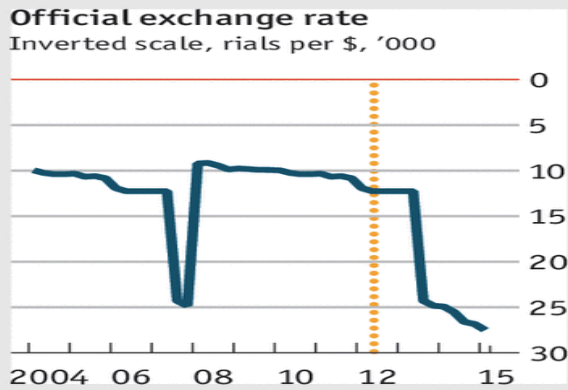
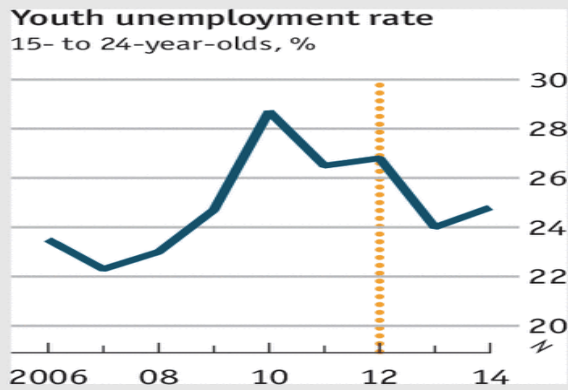
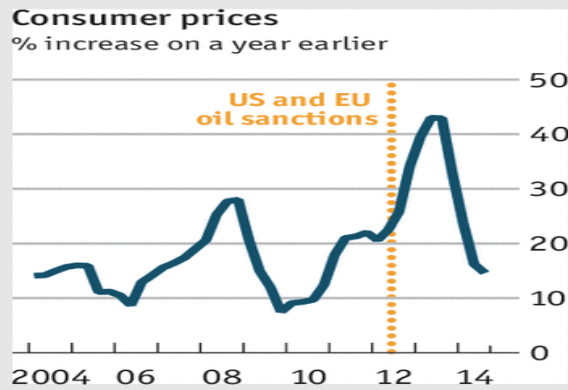
Halal Food: Regional Expenditure (\$mn)



Source: Thomson Reuters.

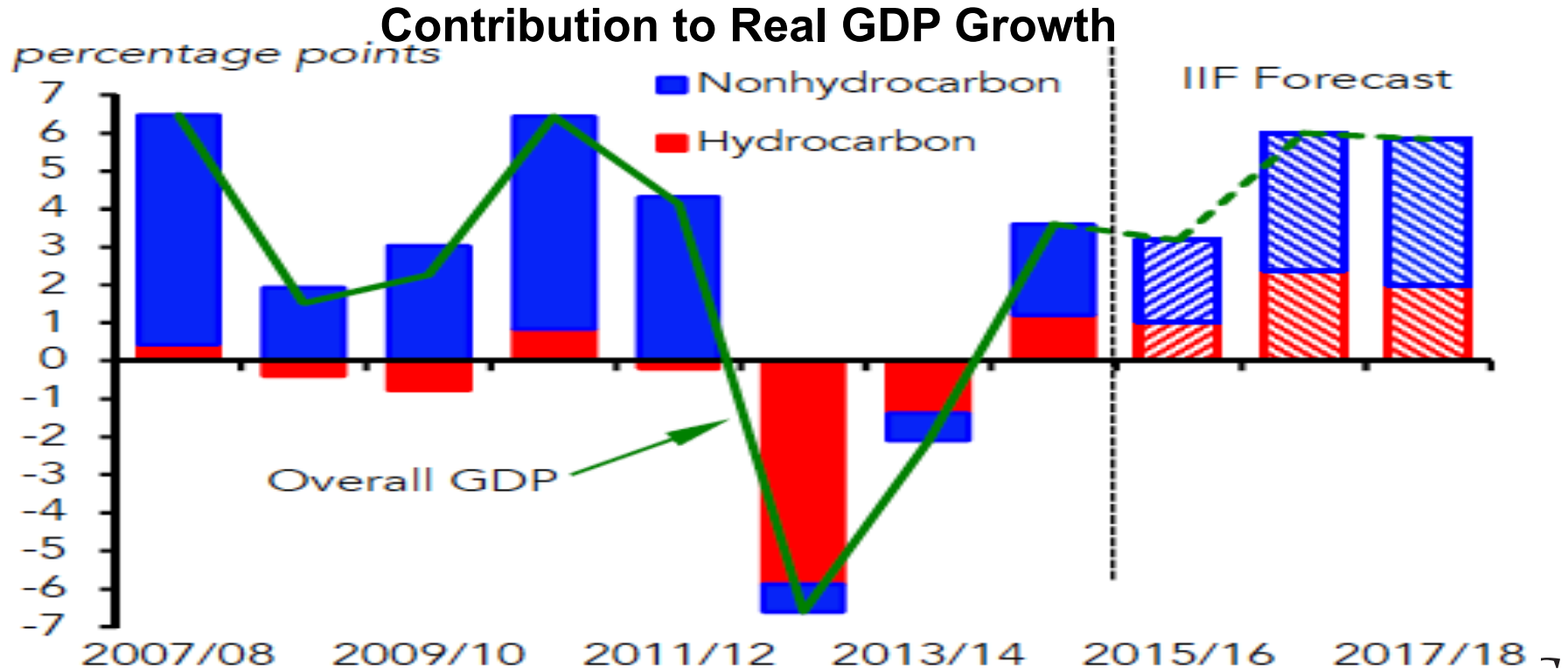
Iran is a large (1,648,195 sq.km), strategically located country, with a young population of about 80mn, an educated, productive labour force and a diversified economy based on oil & gas, manufacturing, industry and agriculture

Iran's indicators



Sources: Economist Intelligence Unit; EIA; Statistical Centre of Iran; Central Bank of Iran; BP

Removal of sanctions is necessary but economic and financial reforms are critical to sustain growth



Iran will require massive investments

...targeting oil and gas projects worth \$185 billion by 2020

...will buy up to 90 airplanes a year from Airbus and Boeing

Infrastructure spending: power, transport, water, ports, airports, housing etc.

Iran is the largest automotive market in the Middle East and roughly one-third the market size of Germany.

...expects to rejoin the SWIFT global electronic payments system 3 months after sanctions removal

...offering to sell State assets to foreigners

Consequences of détente with Iran

Benefits for Iran

- Access frozen foreign assets
- Restore oil & gas export capacity
- Recovery in trade, FDI, equity market, services, tourism, GDP
- Massive infrastructure spending: potential \$800 bn over 10 yrs
- Benefit from Iranian diaspora – human capital, business & financial resources
- But need domestic reforms!

Benefits for GCC/ wider region

- Greater trade & investment benefits
- High-return investment opportunity for GCC investors
- Potential for greater regional integration
- Global: lower oil prices
- Fight against extremism
- Potential “GCC 6+2” institutional cooperation framework?

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Key Takeaways I

- ✓ Region is in transformation, transition and turmoil. But there is no 'road map', no unified vision or leadership. No fast transitions. No Berlin Wall moment.
- ✓ Fundamentals remain strong but economic development paradigm must change to focus on private sector for job creation
- ✓ GCC is focus of MENA economic growth + regional economic & financial integration
- ✓ Economic diversification, fiscal consolidation & reform are imperative for fiscal sustainability in oil exporters
- ✓ GCC reforms include: Gradual Removal of Subsidies + Revenue Diversification +VAT/CIT/Excise taxes + Privatisation & PPP

Key Takeaways II

- ✓ Détente with Iran: a game changer for geopolitical & economic prospects
- ✓ Post-Conflict Reconstruction & PPP for infrastructure are necessary for speedy recovery & job creation
- ✓ Infrastructure & Reconstruction programme requires regional & international collective action: set-up of an Arab Bank for Reconstruction & Development (ABRD)

Thank you

Dr. Nasser Saidi



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