

# GCC Round Up 2016

## Executive Summary

- GCC economies continue to adapt to the new low oil price environment, with a focus on cutting capital spending, and pressing ahead with reforms to subsidies and measures aimed at raising non-oil revenues. The pace of fiscal consolidation varies between countries, as those with larger fiscal buffers take a more gradual approach in order to limit the impact on growth. However, economic activity in all countries is slowing and overall GCC growth is projected to dip under 2 percent this year, before reviving to around 2.5 percent next year.
- Despite diversification and fiscal consolidation efforts, the outlook for the GCC will remain heavily dependent on developments in oil markets. Oil prices have been volatile as markets look for a clear sign, or otherwise, that fundamental balances are tightening. Surging OPEC production and signs of resilience in non-OPEC supply, suggest this will take longer than expected, and we have revised down our price projections for 2017-18.
- Sustained low oil prices have led to a weakening of fiscal and external positions, and pushed a number of GCC governments into large borrowings to fund deficits and support spending. Last year, the focus was on domestic sources of finance, but the mix is now shifting to incorporate greater recourse to external funding and draws on large external assets. In a global low interest rate environment, investors have happily absorbed large sovereign bond issuance from the region this year, and more is expected as Saudi Arabia prepares its first bond issuance.
- The collapse of oil prices has led to some elevation of risk perceptions of the GCC states, though this has not been uniform with the UAE, Qatar and Kuwait retaining their AA ratings from rating agencies. In contrast Saudi Arabia and Bahrain, have been downgraded by 3 notches, and Oman 4 notches. Despite these downgrades, GCC countries maintain similar ratings to the best-regarded developed countries, which is largely a reflection of their comparatively small debt levels.
- Reduced state oil revenues have led to a tightening of liquidity throughout the GCC and a rise in interbank rates. Public deposits have been run down, and in some states liquidity has been further drained by the issuance of government debt, most of which has been taken on by commercial banks. The situation should ease as oil prices recover and governments look to external sources to fund reduced deficits so as to avoid further tightening banking system liquidity and crowding out credit to the private sector.
- Currency pegs remain under pressure in the region compared to historical standards, particularly for the Saudi riyal. However, the most intensive period of government debt financing and related drawdown of reserves has probably passed, and with fiscal buffers still sizeable, GCC pegs are expected to remain in place.

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## The Global Economy

### Growth will remain sluggish

The global economy remains on track for steady if muted growth of around 3 percent a year, although downside risks are elevated, with political and policy uncertainty high on the agenda. With monetary policy close to its limits in advanced economies, attention is shifting to fiscal policy, where low interest rates provides some space for increased spending, and governments look for ways to support still fragile economies. However, a shift away from ever more monetary easing, particularly in the US where rates are expected to rise, will require possibly uncomfortable adjustments. Meanwhile, both the UK and Eurozone appear to be coping well with the initial shock of Brexit, suggesting that growth will hold up this year. However, the uncertainty over what kind of relationship the UK will eventually negotiate with the EU is expected to be a significant headwind through 2017-18, leading us to revise down our growth projections. Across the Atlantic, the US looks set to continue posting modest growth, but also faces some election related policy uncertainty. More positively, emerging markets have started to revive, supported by stronger commodity prices, and stimulus policies in China appear to be having the desired effect, although concerns remain over continuing imbalances in the economy.

### Record low interest rates continue to distort risk perceptions

Having recovered strongly from Brexit, **financial markets** have been more volatile and sold off in recent weeks as investors reassess the prospects of monetary policies in the G3. Concerns over the adverse impact of negative interest rates are rising, and a US rate hike is seen as increasingly likely in December. Markets are also now less sure of the ECB's willingness to expand monetary stimulus. Equities have generally suffered in this more uncertain policy climate, while bond yields have risen and yield curves steepened.

### Oil market

#### Markets lack conviction

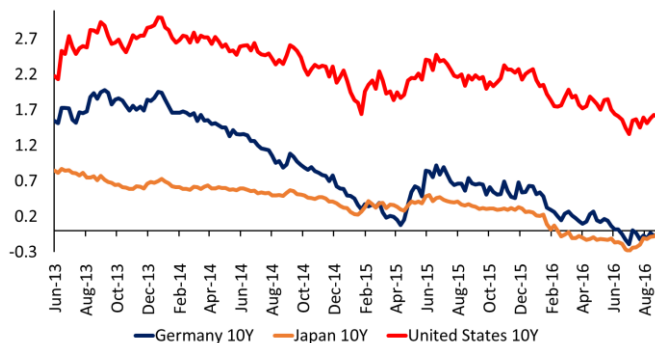
Prices have been volatile over the last few months as markets look for clear signs, or otherwise, that fundamental balances are tightening. However, the outlook remains uncertain and data signals unconvincing. While global demand seems to be holding up (expected to grow by 1.3mb/d), there are so many variables at play on the supply side; ranging from the resilience of US shale oil producers, the shifting prospects for production in countries like

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World Economic Outlook					
	2014	2015	2016f	2017f	2018f
Real GDP (percent change)					
World	3.1	3.0	2.8	3.0	3.0
US	2.4	2.4	1.6	2.2	2.0
Japan	-0.1	0.5	0.5	0.7	0.7
Euro area	0.9	1.5	1.6	1.1	1.5
China	7.3	6.8	6.2	6.0	6.0
Emerging Markets	4.0	3.3	3.3	3.8	4.0
Saudi Arabia	3.6	3.4	0.8	2.6	3.6
Official policy rate (end period)					
US	0.25	0.50	0.75	1.25	1.75
Japan	0.10	0.10	-0.10	-0.10	-0.10
Euro area	0.15	0.05	0.00	0.00	0.00
Oil Price (\$/b period average)					
Brent	100.0	58.0	45.0	57.0	62.0

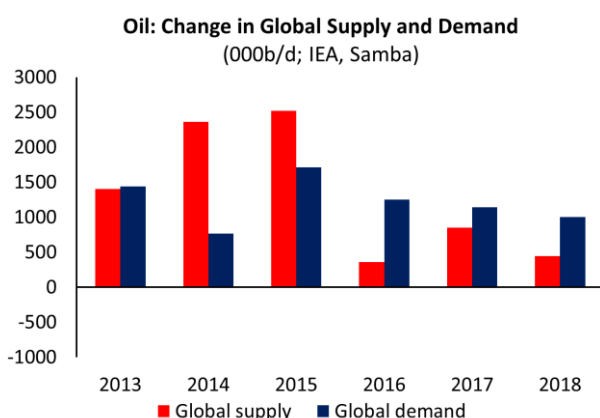
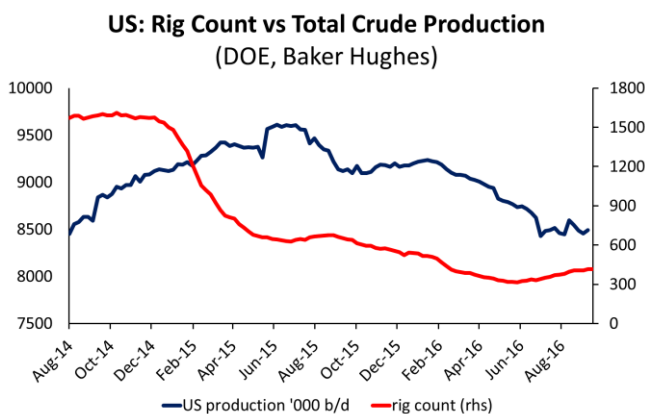
Samba estimates and forecasts

**Sovereign Bond Yields**  
(percent; Bloomberg)



**Oil Price**  
(Brent, \$/b; Bloomberg)





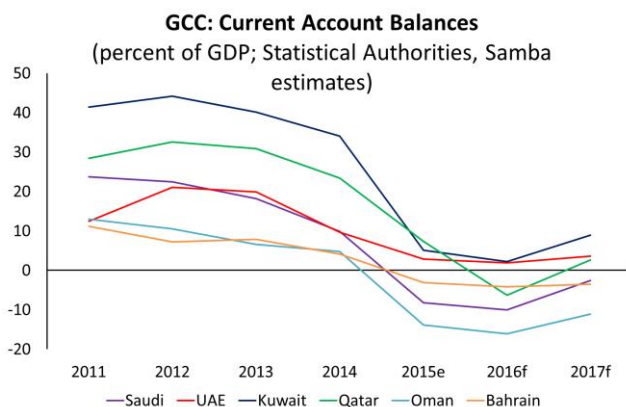
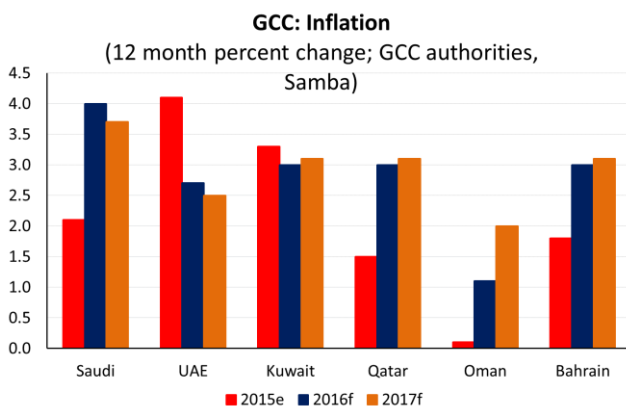
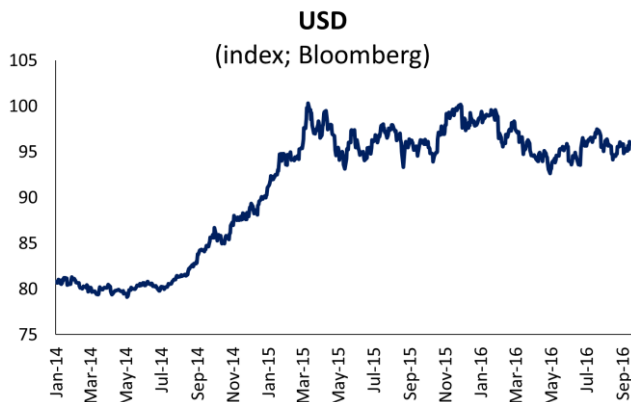
Libya, Nigeria, Iran and Iraq, and talks about a potential OPEC output freeze as well as coordination between Saudi Arabia and Russia. Meanwhile, the widely anticipated drawdown in stocks is happening much more slowly than expected, and is being interrupted by weeks of gains which are unnerving markets. Thus, while prices for Brent have recovered from their near \$40/b lows in July/August, they have been volatile in a \$45-50/b trading range since. Nonetheless, developments to date have caused us to revise up our 2016 average price projection to \$45/b.

### ***OPEC supply still soaring***

Since OPEC abandoned its traditional role of trimming supply to balance the market and support prices back in November 2014, crude oil supply from the organisation has soared. It is now running at nearly 33.7mb/d according to Bloomberg data, up from under 30m/b at the start of 2014. Most of the increase has come from Iraq, Saudi Arabia, and Iran which have boosted average annual output levels by 1.1mb/d, 0.7mb/d and 0.5mb/d respectively over 2015-16. Given that OPEC production is now likely very close to maximum capacity (KSA output hit a record 10.8mb/d this summer), it may be that OPEC does not need a formal agreement for there to be an effective freeze on output. At the least it appears that, absent a surprise restoration of full Libyan production, there is not much room for further large production gains in 2017-18.

### ***A slow rebalancing***

Elevated OPEC production and a smaller decline in non-OPEC output than anticipated, are delaying the expected rebalancing of the market. However, while lower costs producers have been maintaining or even increasing production, the large scale cuts in new investment will eventually impact market balances – the big question is when? It is now increasingly thought that non-OPEC supply will grow (by a small amount) in 2017 after a large contraction this year. Meanwhile, demand growth is expected to slow (to around 1.1mb/d for 2017) as the boost from lower prices fades, and global growth prospects remains muted. Under the circumstances we have revised down our price projection for 2017 to \$57/b, and will examine our projections in more detail in our Oil Market Outlook due in October/November. By then we should have more of a sense of where stocks are heading, and what OPEC's intentions may be.



## Implications for the GCC

### GCC Key Macro Indicators and Forecasts

GCC	2011	2012	2013	2014	2015	2016f	2017f
Real GDP (% change)	8.2	5.6	3.3	3.2	3.4	1.6	2.6
Nominal GDP (\$ billion)	1,437	1,583	1,623	1,647	1,432	1,402	1,571
CPI (ave. % change)	2.9	2.2	2.8	2.6	2.5	3.3	3.2
Budget Balance (% GDP)	12.3	12.7	9.4	2.7	-9.9	-10.3	-4.6
Current Account (% GDP)	22.7	24.9	21.8	13.8	-2.3	-5.5	0.3
Oil production (mb/d)	16.2	16.9	16.6	16.9	17.6	18.0	18.1
Oil price (US\$/b)	110.0	111.0	107.0	107.0	58.0	43.0	60.0
Population (million)	44.7	46.6	48.4	50.8	52.4	54.0	55.7

### Global monetary policy environment

Continued monetary easing by the ECB, the Bank of Japan and more recently the Bank of England contrasts with the tightening bias in the US. This divergence in monetary policy should strengthen the USD over the next eighteen months or so and by consequence the GCC's pegged currencies. Although the situation is nuanced, we think this will have a net negative effect on the region's economies, primarily because of the dollar's long-standing inverse relationship with the oil price, but also because of the hit to nonoil export competitiveness. More positively, the fact that hydrocarbon exports are priced in dollars should be a boon to the external accounts in terms of the purchasing power they provide and the currency strength will at least keep a lid on imported inflation – especially pertinent for Qatar which is in the midst of an infrastructure investment drive.

### Brexit impact

The impact of Brexit on the region has been, and is likely to remain, modest. GCC stocks quickly retraced their immediate post-Brexit losses, and the Bloomberg GCC index (regional average weighted by market cap) showed relatively little reaction compared to the MSCI emerging market index. Looking ahead, Dubai appears the most vulnerable to any sustained downturn in sterling given the importance of UK tourists to the Emirate's economy.

### Oil price impact

The main challenge that GCC countries face is the lower oil price environment. GCC economies are highly dependent on oil and gas exports: during 2011–14, hydrocarbons accounted for some 70 percent of total export earnings and around 80 percent of fiscal revenue, on average. After years of large current account and fiscal surpluses, lower oil revenues have now pushed most GCC fiscal balances into deficit, and only the UAE and Kuwait

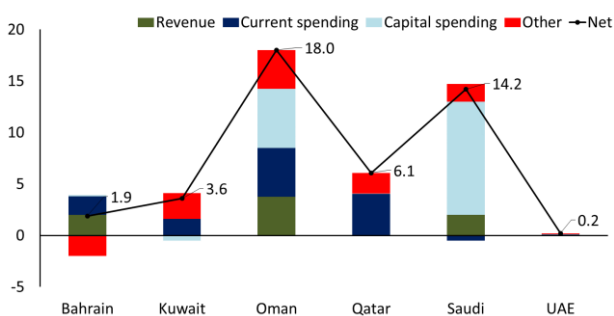
**GCC: Dependence on Oil Revenues**

	2000-05	2006-10	2011-14
<i>Oil export revenues as percent of total exports of goods and services</i>			
Bahrain	58.7	60.5	65.1
Kuwait	82.7	80.5	87.6
Oman	76.9	69.4	64.3
Qatar	88.5	85.9	88.9
Saudi Arabia	83.4	83.1	83
UAE	45	38.7	32.6
<i>Fiscal oil revenues as percent of total fiscal revenues</i>			
Bahrain	71.7	82.2	87.2
Kuwait	72.7	79.2	83.6
Oman	83.4	83.4	88.7
Qatar	90.5	88.3	90.7
Saudi Arabia	82.8	88.3	90.3
UAE	60.2	65.1	69.9

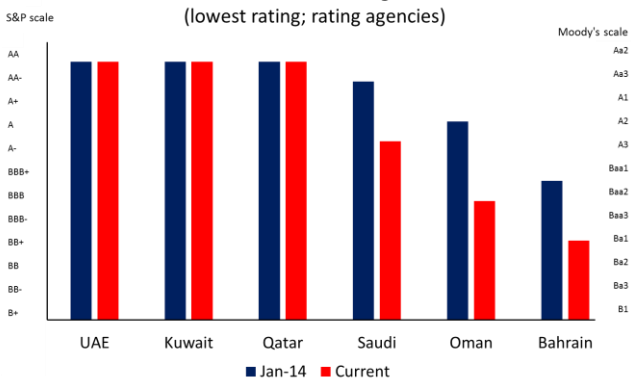
Source: IMF

**Planned Fiscal Adjustment in 2016**

(contribution to the change in non-oil fiscal balance in 2016, percent of non-oil GDP; IMF)



**GCC: Credit Ratings**  
(lowest rating; rating agencies)



seem likely to avoid current-account deficits. Prospects for a return to twin surpluses rest heavily on a recovery in oil prices, and fiscal consolidation efforts.

Financial linkages in the GCC amplify the effects of oil price movements, with changes in fiscal spending creating feedback loops between asset prices and credit. Equity markets have fallen (the GCC index is down 27.8 percent since June 2014) as investors worry that lower government spending will impair corporate earnings. Meanwhile, reduced government spending has undermined bank deposit growth, tightened liquidity and pushed up interbank rates—exacerbated by government debt issuance for example in Saudi Arabia. In some countries, private sector credit has also been squeezed, though in others government payment delays have increased demand for additional credit lines. Consumption and investment have also been hit as lower oil prices have put downward pressure on asset prices and confidence.

## Regional themes for the GCC

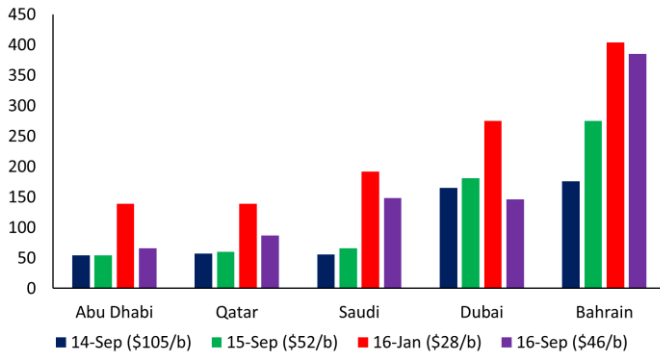
### *Reduced state spending lowers growth*

In general, governments have reduced spending in line with oil prices, with an initial focus on capital investments, including those sponsored by government-related entities (GREs). The extent of cuts has varied between countries: those with the largest fiscal buffers have been able to take a more gradual approach. Qatar intends to protect its key infrastructure spending ahead of the FIFA 2022 World Cup, and Kuwait is actually increasing capital spending, although current spending is being reined in. Saudi Arabia has targeted capital spending, though all areas of government spending will continue to be rationalised, with particular focus on those that create a draw on foreign reserves. As well as reducing investment spending, Oman is looking to trim operating expenses and cut defence outlays. Meanwhile, the UAE has cut transfers to GREs. In general, governments are stopping short of cutting public sector employment and wages.

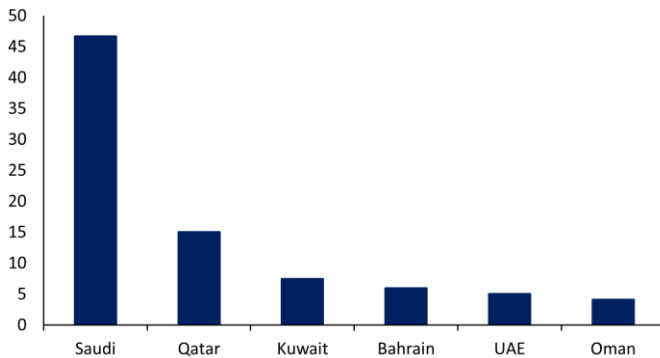
Fiscal consolidation has had, and will continue to have, a strong negative impact on non-oil economic output, in turn dragging down overall GDP growth rates. Last year a boost in hydrocarbon production helped keep aggregate GCC growth at over 3 percent, but this is now projected to slip to 1.6 percent this year, with a forecast recovery to 2.7 percent in 2017 heavily dependent on a recovery in oil prices supporting a moderate revival in public spending.



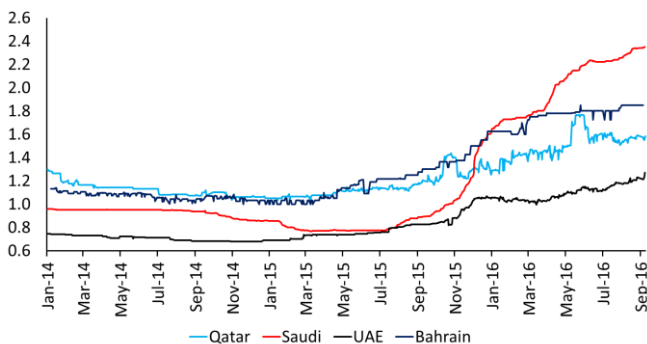
**Sovereign CDS**  
(5 year, bps; Bloomberg)



**Sovereign Bond Issuance**  
(since Jan-15, \$bn; Zawya)



**Interbank Rates**  
(3 month, percent; Bloomberg)



### *A new dawn of fiscal reforms*

In tandem with cuts in investment spending, GCC governments have also embarked on broader fiscal reforms and consolidation. In general, subsidies are being reduced, including for energy; fees are being raised and new ones introduced; and new taxes and excises contemplated. Most radically, VAT is set to be introduced across the GCC in 2018, probably at an initial rate of 5 percent. There are no plans to introduce personal income taxes at this time and these would probably be contemplated only as a last resort, given the long-standing nature of the political relationship between ruler and ruled in the GCC. Having said that, an income on expatriates shouldn't be ruled out.

### *Elevated risk perception in some GCC states*

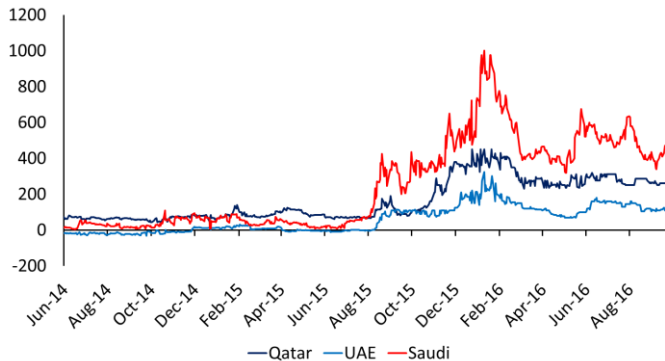
The collapse of oil prices has led to some elevation of risk perceptions of the GCC states, though this has not been uniform. The UAE, Qatar and Kuwait are still rated the same (AA S&P) as they were back in 2014 when oil prices averaged around \$100/b, although all three have been given a negative outlook by Moody's. In contrast Saudi Arabia and Bahrain, have been downgraded by 3 notches, while Oman is down 4 notches since 2014. CDS rates mirror these ratings in so far as Bahrain and Saudi Arabia have seen their spreads widen. Despite these recent downgrades, GCC countries maintain similar ratings to the best-regarded developed countries, which is largely a reflection of their comparatively small debt levels.

### *Increase in debt issuance*

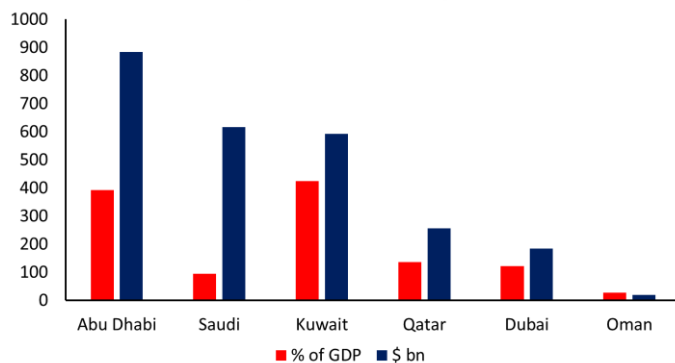
Bond markets have seen a flurry of sovereign issuance as GCC governments look to plug the holes in their finances resulting from the fall in hydrocarbon revenues. Since January 2015, GCC sovereigns have raised \$87 billion in both domestic and international bonds and sukuks, according to data from Zawya. The largest international issuance so far is the \$9 billion offering from Qatar in late May. Abu Dhabi also issued eurobonds worth \$5 billion in May in both 5 and 10 year tenors, while Oman issued \$2.5 billion of bonds in May, in its first international bond sale in almost two decades. The markets are waiting on a Saudi issuance, which we think will be around \$15 billion later this year, though the government has already secured a syndicated loan worth \$10 billion.

Corporate international debt issuance is also on the rise, with the vast majority of offerings coming from financial institutions. Since January 2015, UAE banks (and a small number of corporates) have issued \$10.9 billion in bonds, the largest in the GCC by a distance.

**Forward Exchange Rates**  
(12 months, bps; Bloomberg)



**GCC external assets are large**  
(IIF, SWF Institute)



**GCC Equity Index**  
(cap-weighted top 200 equities; Bloomberg)



In general, bank issuance has been designed to shore up capital positions in anticipation of an increase in bad loans.

### ***Liquidity pressures in domestic banking systems***

Interbank rates have risen across the region as liquidity has tightened. This has been caused by the slowdown or reversal of deposit growth, caused in turn by governments running down their domestic savings. In some countries liquidity has been further drained by the issuance of government debt, most of which has been taken on by commercial banks. This in turn has meant less credit for the private sector, though as noted above, in some countries where the government has been delaying payments to private contractors credit growth has remained quite firm (albeit more expensive).

### ***Pressure on currency pegs***

Currency pegs remain under pressure in the region compared to historical standards, particularly the Saudi riyal's peg to the USD. Pressure on the riyal has abated from its early-year intensity, but has not gone away. Speculators are wondering whether local banks have the capacity to absorb sufficient amounts of government debt to relieve pressure on international reserves. Our view is that the most intensive period of government debt financing has probably passed, and with fiscal buffers still sizeable, the peg is expected to remain in place. More generally, GCC governments are now more willing to draw on some of their large external savings held in sovereign wealth funds, although data on such actions are not publicly available.

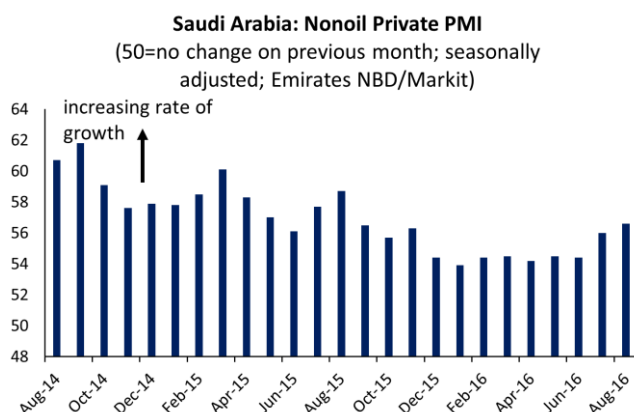
### ***Weaker asset prices***

GCC stock markets suffered large losses (some as much as 20 percent) at the beginning of the year, owing to the generalised risk-off sentiment, which pervaded global financial markets, and a further decline in oil prices. Much of these losses were recovered in the second quarter as oil prices recovered, but from May onwards the long-standing correlation between the markets' performance and oil prices began to breakdown. Thus, even though oil prices continued to rise (albeit modestly) GCC bourses trended down again.

This is probably attributable to the growing realisation among investors that the recovery of oil prices is unlikely to herald a meaningful increase in government spending—for this year at least. Given the close links between government spending and private sector performance, corporate earnings seem likely to remain under pressure.

Saudi Arabia	2011	2012	2013	2014	2015	2016f	2017f
Real GDP (% change)	9.9	6.2	2.7	3.6	3.4	0.6	2.6
Nominal GDP (\$ billion)	669.5	733.9	744.3	746.2	653.3	624.1	718.6
CPI (ave. % change)	3.7	2.9	3.5	2.7	2.1	4.0	3.7
Budget Balance (% GDP)	11.1	12.0	5.8	-3.5	-15.9	-14.7	-6.6
Current Account (% GDP)	23.7	22.4	18.2	9.9	-8.2	-10.1	-2.5
Oil production (mb/d)	9.30	9.80	9.38	9.67	10.24	10.47	10.57
Population (million)	29.2	30.0	30.6	31.5	32.5	33.5	34.5

Rating	S&P	Moody's	Fitch
Saudi Arabia	A-	A1	AA-



UAE	2011	2012	2013	2014	2015	2016f	2017f
Real GDP (% change)	4.0	4.2	4.3	3.0	4.0	2.3	2.5
Nominal GDP (\$ billion)	345.7	377.0	388.9	408.2	371.6	365.2	402.3
CPI (ave. % change)	0.9	0.7	1.5	2.33	4.1	2.7	2.5
Budget Balance (% GDP)	11.0	10.9	10.4	4.9	-2.3	-3.8	-0.5
Current Account (% GDP)	12.5	21.1	20.0	9.7	2.9	1.9	3.6
Oil production (mb/d)	2.55	2.63	2.73	2.77	2.88	2.89	2.89
Population (million)	6.0	6.5	7.1	7.8	8.0	8.2	8.5

Rating	S&P	Moody's	Fitch
UAE		Aa2	
Abu Dhabi	AA	Aa2	AA

Other asset price data are hard to come by. Real estate data are available for Qatar and for the UAE, though they can be inconsistent. These data suggest that Dubai's property prices have fallen back to 2012 levels, though the decline in Abu Dhabi has not been as dramatic. In Qatar, the central bank's real estate index posted a second consecutive monthly decline in May for the first time since 2009.

### Key forecast for individual countries

#### Saudi Arabia

In Saudi Arabia economic policy is being guided by the National Transformation Plan, unveiled earlier this year, and closely identified with the Deputy Crown Prince, Mohammed bin Salman. The overriding objective is to make the private sector and productivity growth the drivers of economic activity, rather than oil-fuelled state spending. The process is not without its challenges, and there does seem to be a tension between the Saudiisation drive and a broader liberalisation agenda, but overall the NTP is an appropriate framework to guide the country away from its long-standing dependence on oil and move the fiscal position on to a sustainable footing.

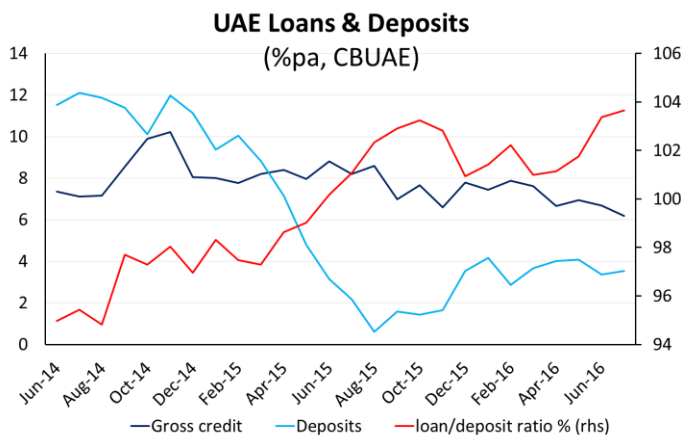
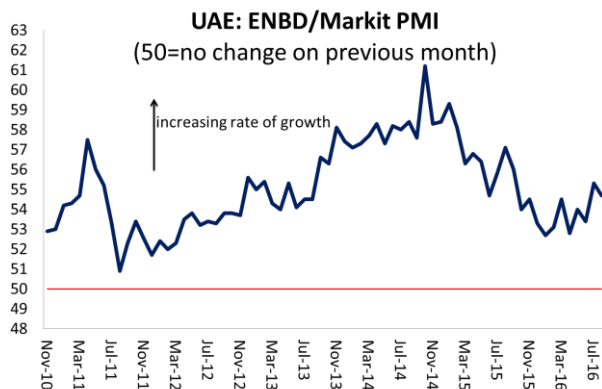
For the moment, the budget deficit is commanding a lot of attention. The government has tightened its spending stance considerably, but the oil price collapse means that a deficit of some 15 percent of GDP is in prospect this year—similar to last year's outcome. Nevertheless, fiscal buffers are large and the local banking sector has strong appetite for domestic debt issuance. And based on our forecast for gradually recovering oil prices, and at least partial implementation of the NTP agenda, we think the fiscal outlook is manageable.

That said, fiscal financing has tightened domestic liquidity, which has put further pressure on a private sector that is feeling the strain of reduced government spending. We expect nonoil GDP growth of only around half a percentage point this year, with some recovery in 2017 as oil prices pick up and the government loosens its stance somewhat. Assuming the privatisation process gathers momentum, we think nonoil growth should be back above 5 percent by 2020.

#### UAE

Supported by its large fiscal buffers, the UAE is managing the sharp decline in oil prices reasonably well. That said, GDP growth is slowing and the budget has moved into deficit, despite cuts in transfers to GREs and new subsidy reforms. Real GDP growth is estimated to have risen to 4 percent in 2015, boosted by an





Qatar	2011	2012	2013	2014	2015	2016f	2017f
Real GDP (% change)	13.4	4.9	4.6	4.2	3.7	3.5	3.6
Nominal GDP (\$ billion)	169.8	189.9	201.9	210.1	188.5	186.8	213.5
CPI (ave. % change)	1.9	1.9	3.1	3.0	1.5	3.0	3.1
Budget Balance (% GDP)	6.4	8.9	14.4	9.6	1.8	-5.8	-3.9
Current Account (% GDP)	28.4	32.6	30.9	23.5	7.3	-6.3	2.6
Oil production (mb/d)	0.74	0.73	0.70	0.67	0.66	0.61	0.60
Population (million)	1.7	1.8	2	2.2	2.4	2.5	2.62

Rating	S&P	Moody's	Fitch
Qatar	AA	Aa2	AA

increase in hydrocarbon production. However, non-hydrocarbon sector growth is slowing as project spending is curbed, credit growth slows, and the stronger US dollar to which the dirham is pegged, hurts exports. Nonoil growth came in at around 3.7 percent last year, but is projected to slip to around 2.5 percent during 2016-17. The 2018-20 period should be more dynamic, as government spending revives and construction and services benefit from the Dubai 2020 Expo in 2020.

Lower oil revenues have put public finances under strain, pushing UAE governments to curb spending, issue debt, and draw on savings. Last year, the focus was on domestic sources of funds, but the mix is now shifting to incorporate greater external borrowing (Abu Dhabi's \$5 billion bond issue) and draws on large external savings. The UAE consolidated fiscal deficit is projected to rise to 3.8 percent of GDP this year (\$14 billion), but should be close to balance next, and return to surplus from 2018 as oil revenues recover, and fiscal consolidation measures take effect.

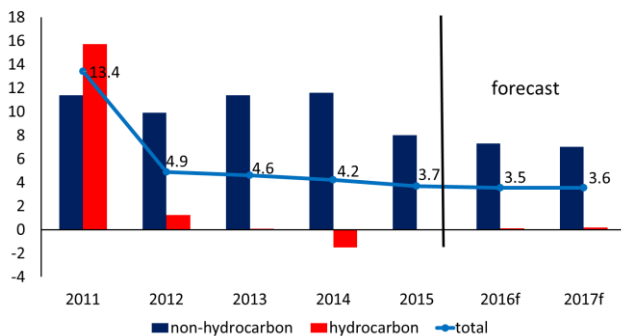
Despite declines in public sector deposits, banking liquidity is still comfortable and banks are well capitalised. The overall liquid asset ratio stood at 16 percent in June according to central bank data, while banks' excess deposits at the central bank plus their CD holdings had recovered to \$34 billion by end-July, from a \$30 billion low in August last year. But with loan growth (6.2 percent y-o-y July) outstripping deposit growth (3.5 percent y-o-y), the loan-to-deposit ratio is back above 100 percent and interbank rates have risen. In the circumstances we expect a further softening of loan growth and NPLs are like to rise as the operating environment weakens.

External balances remain healthy, with the current account expected to remain in surplus this year, despite the further slump in oil prices. External debt levels are nudging 60 percent of GDP, but are dwarfed by external savings, which are widely estimated at over 200 percent of GDP. Meanwhile central bank reserves continue to hold up and were back approaching \$90 billion in June. However, there are lingering concerns over the large debts of GREs, which makes them vulnerable to external shocks, a weaker real estate market, and roll-over risks. This is more apparent in Dubai where GRE debt stands at around 70 percent of GDP, than Abu Dhabi (27 percent of GDP).

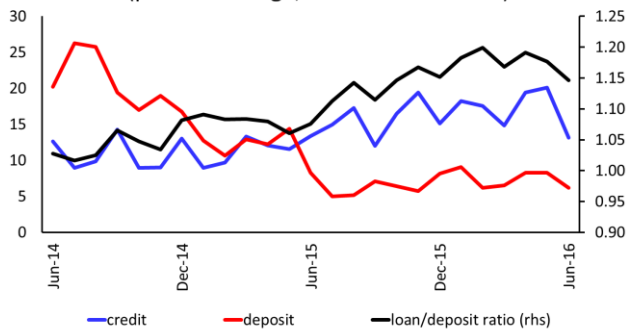
## Qatar

Qatar's investment spending was the main driver of GDP growth of almost 4 percent in 2015, with a non-hydrocarbon expansion of 7.8 percent, partly offset by a contraction in the oil sector. Growth in the first quarter of 2016 came in at 1.1 percent, with a healthy expansion in the non-hydrocarbon sector (5.5 percent)

**Qatar: Real GDP Growth**  
(12 month percent change; QSA, Samba)



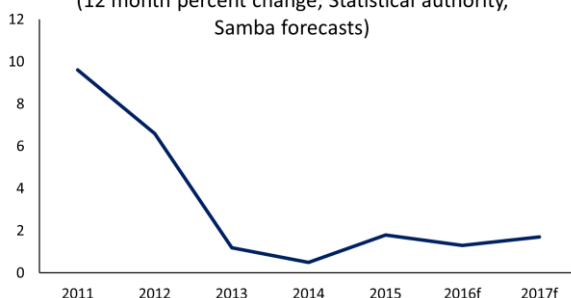
**Qatar: Bank Loans & Deposits**  
(percent change; Qatar Central Bank)



Kuwait	2011	2012	2013	2014	2015	2016f	2017f
Real GDP (% change)	9.6	6.6	1.2	0.5	1.8	1.3	1.7
Nominal GDP (\$ billion)	154.1	174.1	175.8	165.5	118.3	122.5	127.5
CPI (ave. % change)	4.9	2.9	2.6	2.9	3.3	3.0	3.1
Budget Balance (% GDP)	35.6	32.8	23.1	20.5	-11	-10.3	-2.8
Current Account (% GDP)	41.4	44.2	40.1	34.1	5.1	2.2	8.9
Oil production (mb/d)	2.54	2.63	2.71	2.62	2.64	2.89	2.91
Population (million)	3.7	3.8	3.9	4.0	4.1	4.2	4.3

Rating	S&P	Moody's	Fitch
Kuwait	AA	Aa2	AA

**Kuwait: Real GDP**  
(12 month percent change; Statistical authority, Samba forecasts)



dragged down by a 3 percent contraction in the hydrocarbon sector. We expect growth of around 3.5 percent for 2016 and 2017 as a reduced but still robust level of project spending is supported by a small contribution from the hydrocarbon sector towards the end of this year as the Barzan gas project is commissioned.

Qatar's current account moved into deficit (\$2.3 billion) in the first quarter of 2016. The deficit was caused by a 35 percent y-o-y fall in the value of exports and a 23 percent increase in the import bill. We foresee a small current account deficit this year, turning to a surplus next as oil prices improve and the strong dollar reduces the cost of imports.

We expect a fiscal deficit this year of around 5 percent of GDP, and 2 percent in 2017, before the recovery of oil prices allows a small surplus in 2018. The total deficit over the two years will be around \$18 billion, which the ministry of finance has stated will be funded entirely by debt issuance, as opposed to drawing down the substantial reserves at the QIA. Issuance since September 2015 is already at \$21.8 billion (including the record \$9 billion international issuance in May of this year). Although the need for fresh capital does not appear particular pressing, the authorities may well decide to take advantage of extremely high international appetite for Gulf debt and make a further issue.

Liquidity remains tight in the banking sector with the loan-to-deposit ratio standing at 115 in June, down slightly on May (118). The improvement in the ratio may have been a result of some of the \$9 billion in foreign capital the sovereign raised in May finding its way into the local banking system. Government-related deposits (circa 30 percent of total deposits) continue to fall, although overall deposit growth is still positive thanks strong non-resident deposit growth. Despite constrained liquidity the government issued \$1.3 billion of domestic bonds and sukuks in August for which it received offers totalling \$2 billion.

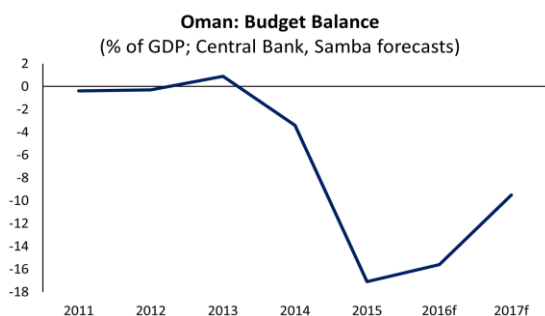
## Kuwait

Kuwait is in a good position to weather the low oil price environment thanks to its large external savings, relatively low break-even oil price for the fiscal/ current accounts and low levels of government debt (currently around 14 percent of GDP).

Despite official figures showing substantial fiscal deficits of over 10 percent of GDP for 2015/16 – this is somewhat misleading as the authorities automatically deduct between 10-25 percent of revenues for transfers to the Reserve Fund for Future Generations and do not include income from the Kuwait Investment Authority. Indeed, the external picture looks robust

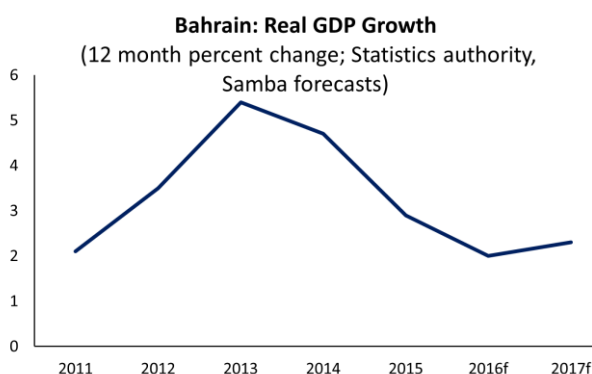
Oman	2011	2012	2013	2014	2015	2016f	2017f
Real GDP (% change)	-1.1	7.1	3.9	2.9	3.1	1.5	1.8
Nominal GDP (\$ billion)	69.4	77.2	79.3	81.7	69.5	70.3	74.5
CPI (ave. % change)	4.0	3.0	1.3	1.0	0.1	1.1	2
Budget Balance (% GDP)	-0.4	-0.3	0.9	-3.4	-17.1	-15.6	-9.5
Current Account (% GDP)	13.0	10.5	6.6	4.8	-13.9	-16.1	-11.1
Oil production (mb/d)	0.88	0.92	0.94	0.94	0.98	0.95	0.91
Population (million)	3.0	3.3	3.6	4.1	4.2	4.4	4.5

Rating	S&P	Moody's	Fitch
Oman	BBB-	Baa1	



Bahrain	2011	2012	2013	2014	2015	2016f	2017f
Real GDP (% change)	2.1	3.5	5.4	4.7	2.9	2.0	2.3
Nominal GDP (\$ billion)	28.7	30.4	32.5	35.0	30.8	33.2	35.0
CPI (ave. % change)	-0.4	2.8	3.3	2.5	1.8	3.0	3.1
Budget Balance (% GDP)	-0.3	-2.0	-3.3	-4.0	-13.5	-14.3	-11.2
Current Account (% GDP)	11.2	7.2	7.9	4.1	-3.1	-4.2	-3.5
Oil production (mb/d)	0.18	0.18	0.19	0.19	0.19	0.19	0.19
Population (million)	1.1	1.2	1.2	1.2	1.2	1.2	1.3

Rating	S&P	Moody's	Fitch
Bahrain	BB	Ba2	BB+



as huge external savings accumulated from years of current account surpluses, most of which are held by the KIA are estimated at around \$500 billion (500 percent of GDP).

The government is using external savings and proceeds from borrowing to boost capital spending in support of its long-term development plans. This has helped support growth which came in at 1.8 percent last year and is expected to hold at 1.5 percent over the next couple of years. The Government is also attempting to reform its generous welfare and subsidy system to cut costs, and is planning to raise utility charges later this year and introduce VAT in 2018. However, perennial opposition to wage freezes and subsidy cuts suggests progress with fiscal consolidation will be slow.

### Oman

Oman's budget deficits will be in excess of 10 percent this year and next thanks to the lower oil price environment. Covering these deficits will require a mix of domestic and external borrowing, coupled with drawing down government financial assets – as mentioned earlier the \$2.5 billion issuance in May was the sovereign's first international offering in two decades. The authorities have stepped up their fiscal consolidation efforts, and plan to make sizeable cuts to defence, operating expenditures, and workers' fringe benefits. These efforts will take their toll on GDP growth, and the economy is expected to expand by 1.5 percent this year and 1.8 percent in 2017, down from the circa 3 percent growth over the past couple of years.

### Bahrain

Bahrain's economy expanded 4.5 percent on a year-on-year basis in the first quarter of the year. This was an unexpectedly robust performance, but we do expect growth to slow in the remaining three quarters as the lower oil prices and related sizeable fiscal deficits dampen government spending.

At the end of June, ratings agency Fitch downgraded Bahrain's sovereign credit rating to BB+ citing the country's fiscal position. While noting that the government is making progress in fiscal consolidation, including activating new revenue generation streams and reducing outlays, Fitch said it expected government debt to rise from 62% of GDP last year to almost 80% this year.

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