November 2022

Economic Outlook: GCC & Egypt 2022-2023

National Bank of Kuwait
Economic Research Department

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2022-2023
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GCC & Egypt Outlook

Global growth in 2023 will slow to weak levels as the post-Covid demand boom fades and as high prices and interest rates pressure consumer incomes. Oil prices are projected to ease slightly in this climate, but uncertainties are high given potential loss of Russian supply and OPEC policy cuts. GCC economies, after outperforming this year, should continue to do well so long as oil prices remain historically high and supported by progress on economic reforms and government initiatives to boost investment. Downside risks include a soft world economy triggering lower oil prices, interest rates remaining high and inflation proving persistent. The main upside risk is from higher oil prices, which would deliver stronger economic and fiscal outcomes across the Gulf region.

Global growth to slow, oil price uncertainties remain high

As we enter 2023, the mood surrounding the global economy is gloomy, with the post-pandemic demand boom fading, policy support being withdrawn or reversed, consumer wallets squeezed by high inflation in major economies and the Russia-Ukraine conflict weighing on energy markets and the broader geopolitical climate. The IMF in October cut its world growth forecast for 2023 to 2.7% (from 2.9% in July), which would be the weakest outturn since 2001 barring two exceptional years related to Covid and the global financial crisis. A flat-line-to-narrow-recession over the next few quarters in western countries is now a central theme, with risks being further on the downside if inflation remains elevated or energy prices surge due to fresh supply problems. However, the job market has thus far remained robust, which, if sustained, should help cushion against a harder landing for major economies. Emerging markets are projected to see stable if historically soft growth of 3.7% in 2023, though this hinges on a pick-up in growth in China which could yet disappoint if it extends its tough anti-Covid policy through next year.

Major central banks will continue to ratchet up benchmark policy rates at least until early next year as they look to bring inflation – currently running at 8-11% in the US and Europe – back under control. Futures markets see the US Fed funds target rate peaking at 5% in mid-2023 (+100 bps from current levels), despite the Fed's acknowledgement of the downside risks to growth. But we expect rate cuts to be on the agenda in 2H23 as inflation eases and economic growth remains soft. In Europe, the ECB's tightening cycle may persist for longer than the Fed's given its later start and potentially more enduring inflation problem reflecting high regional energy prices. We would also expect signs of a turn in the rate hike cycle to start to reverse the surge in the US dollar seen in 2022, although further global uncertainties and – for a given interest rate path – a drop in US inflation to well below European levels could still provide some support for the greenback.

In the oil market, OPEC+'s decision in early October to target crude output cuts of 2 mb/d starting November seem to put a floor under prices, leaving Brent in the $90-100/bbl range. Our base case is for prices to average slightly lower in 2023 at $90 than this year's projected $100, given weakness in global economic growth. However, we see risks to prices as tilted to the upside, given potential loss of Russian supply from the EU's oil embargo commencing December 2022, OPEC+'s limited spare capacity constraining its ability to respond to any market tightness and a potential end to China's zero-Covid policy, which would lead to a rebound in Chinese oil demand.

Gulf economic performance to hold up well in 2023

This year has been one of strong outperformance for GCC countries relative to most international economies. High oil prices and rising oil output will push Gulf-wide GDP growth to a more than decade-high of 6.9% and deliver fiscal surpluses across the region. Given less support from the oil sector due to output cuts, a growth slowdown is inevitable in 2023. However, we expect the non-oil economy to fare reasonably well, with a combination of still-high oil prices, ongoing structural reforms and government initiatives to support investment providing some resilience to the global headwinds described above, as well as higher interest rates. The reform agenda is most prominent in Saudi Arabia and the UAE, but smaller Gulf countries including Bahrain and Oman are also making some progress, with steps to boost fiscal resilience, labor market competitiveness and openness to FDI. Following the World Cup, growth in Qatar will decelerate but medium-term prospects remain strong given huge investments including on expanding gas production. Kuwait's economic growth will drop back from this year's rapid 8% rate, and slower reform progress points to growth remaining skewed towards consumer spending for now.

We see the main positive risk to the outlook stemming from the upside potential for oil prices mentioned above, which if it materializes would point to stronger economic and fiscal outcomes across the Gulf next year than we currently project. However, there are also downside risks including from a weaker world economy triggering lower oil prices, trade and investment, and from interest rates remaining high, weighing on demand and asset prices. Inflation – although overall much lower than in Europe and the US this year – could prove persistent, affecting household spending and business costs. Economic expansion in some countries could be challenged by labor market tightness or skills shortages, especially given a reliance on overseas workers.

Finally, in Egypt, the IMF deal struck in October triggered a sharp currency decline and higher consumer prices, with a challenging period of reforms likely ahead in 2023. However, while longer-term external funding challenges have not yet disappeared completely, the deal will help ease FX shortages, support a return of investor confidence and together with reform steps provide for an improvement in economic growth the following year.

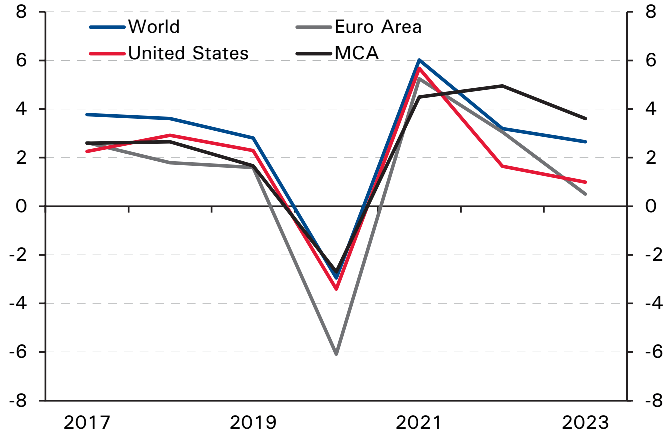
GCC key economic indicators

		2020	2021	2022f	2023f
Nominal GDP	$ trillion	1.4	1.7	2.1	2.0
Real GDP	% y/y	-4.6	3.0	6.9	2.3
- Oil	% y/y	-5.5	0.0	11.2	0.0
- Non-oil	% y/y	-4.1	4.6	4.6	3.7
Inflation	% y/y	0.7	1.9	3.3	2.8
Fiscal balance	% of GDP	-10.0	-1.0	5.9	3.0
Current acc. bal.	% of GDP	-1.1	9.2	18.6	14.0

Source: Official sources, NBK estimates and forecasts

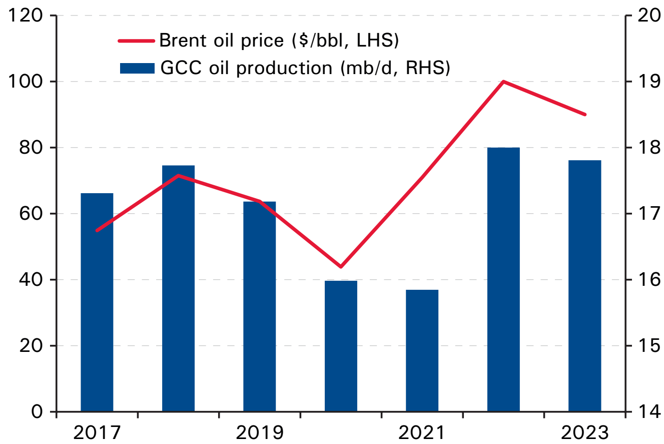
Chart 1: International GDP

(% y/y)



Source: IMF WEO October 2022; MCA=Middle East & Central Asia

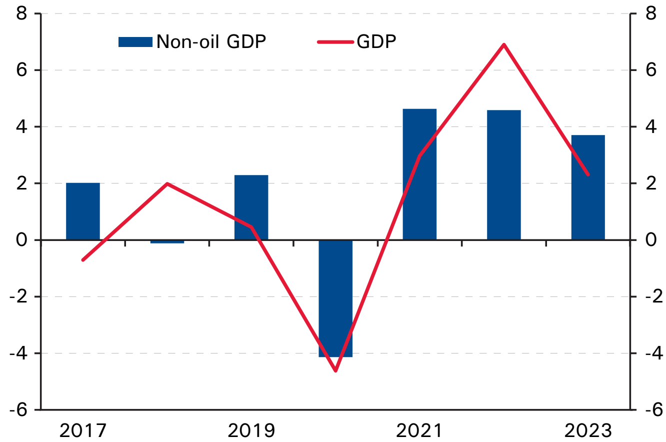
Chart 2: Brent oil price & GCC oil production



Source: EIA, OPEC, NBK estimates and forecasts; oil data is year average

Chart 3: GCC GDP

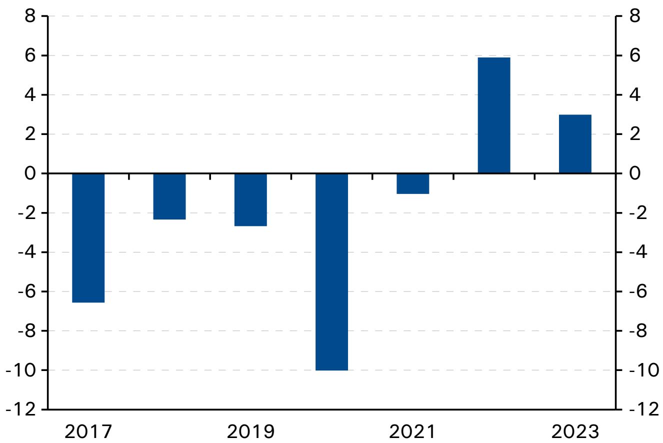
(% y/y)



Source: Official sources, NBK estimates and forecasts

Chart 4: GCC fiscal balance

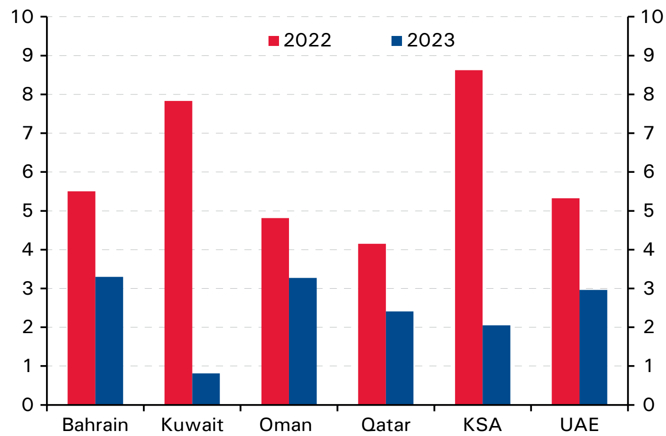
(% of GDP)



Source: Official sources, NBK estimates and forecasts

Chart 5: GCC GDP growth by country

(% y/y)



Source: NBK estimates and forecasts

Bahrain, Oman & Qatar

Higher oil revenues and progress on economic reforms have improved economic prospects in Bahrain and Oman, with Covid-era financial vulnerabilities giving way to fiscal surpluses and solid projected economic growth rates. After the boost this year from hosting the World Cup, growth in Qatar will slow in 2023, but the longer-term outlook is well supported by investments linked to Vision 2030 and the expansion of LNG capacity due by 2027. For Bahrain and Oman, downside risks are mostly linked to lower oil prices and delays to ongoing reforms, which could push fiscal balances back into deficit. In Qatar, risks include near-term economic overheating and logistical challenges related to hosting the World Cup and later on, delays in gas megaprojects. On the upside, higher energy prices would improve economic prospects.

Bahrain: Oil windfall boosts recovery, reforms still a priority

Bahrain's post-pandemic economic recovery has accelerated on the back of higher oil prices and a robust pick-up in consumer and hospitality-oriented sectors. GDP growth reached 6.2% y/y in 1H22, albeit boosted by net taxes (probably related to January's VAT hike), with the gross value added measure up a more modest 3.8%. Oil output is seeing little growth due to capacity constraints, and this will affect overall GDP growth outcomes for this year (5.5%) and next (3.3%). But the outlook for non-oil growth is positive given the easing of fiscal pressures and the government's commitment to its $30 billion Economic Recovery Plan launched late last year, which includes infrastructure investments, expanding sectors such as tourism, hospitality and finance, simplifying government procedures and developing the local workforce. In 2Q22, Bahraini employment rose 4.3% y/y in the private sector and 3.2% in the public sector, suggesting some progress towards the labor market goal.

Longer-elevated oil and aluminum prices will help the government record a fiscal surplus of 0.6% of GDP this year, two years ahead of the updated Fiscal Balance Program target. But with commodity prices seen lower next year, fiscal consolidation will remain an important theme. We expect the budget to be broadly in balance in 2023, based upon further spending control (but no large spending cuts). This will help stabilize the debt to GDP ratio (now 112% of GDP based on the government definition), which nevertheless alongside limited FX reserves remains a concern for the credit rating agencies, and absorb the impact of rising interest rates on the debt service bill. But given the still fragile financial position, a fresh drop in oil prices that results in renewed fiscal deficits, spending cuts and rising public debt remains the key downside risk to the economic outlook.

Oman: Growth to slow but reform drive offers positive outlook

High energy prices and the government's reform program have improved Oman's economic outlook and reduced fiscal pressures. GDP is forecast up 4.8% this year, led by oil and gas but also improved non-oil activity. Initiatives to lift growth include expanding key sectors such as manufacturing, logistics and tourism, boosting investment and the labor supply (especially female participation), improving the business climate, but preserving key parts of social spending. Reforms this year included scrapping foreign ownership limits for listed firms, with the aim of attracting funds ahead of a planned privatization drive over the next few years. We expect further reform progress next year, though GDP growth will slow as oil output levels off and non-oil activity softens due to global factors, lower oil prices, a fading post-Covid bounce and higher interest rates.

The public finances have improved in line with higher energy prices and the government's medium-term fiscal adjustment program, which prioritized spending restraint but also included the introduction of VAT in 2021 that (including excise duties) added 2% of pro-rated GDP to revenues in 1H22. The budget should post a surplus of 5.5% of GDP this year, the first since 2008, narrowing to 3.2% of GDP in 2023. Despite a planned 3% decrease in the 2022 state budget, spending is forecast to increase slightly this year as the as the authorities cushion the impact of higher energy prices through subsidies, as they have indicated. Public debt has been cut to 55% of GDP from 69% in 2021, reducing funding risks and exposure to rising interest rates. Both Fitch and S&P raised the government's credit rating one notch this year reflecting these improved metrics.

Qatar: World Cup and gas investments help drive growth

Qatar's economy is on track to expand at a fast pace in 2022, driven by strong growth in the non-oil sector, which was up 7.2% y/y in 1H22, and should remain robust in H2 given the boost from business preparations, increased tourism and related spending from the World Cup in November. More than 1 million spectators will flock to the country (33% of Qatar's population of 3 million), with potentially 0.2 million present at any one time. Bullish sentiment is reflected in PMI survey numbers, which reached as high as 67.5 in May, though has cooled of late. Changes in hydrocarbon sector output will be minimal given that production is already at capacity levels, and that Qatar is not part of the OPEC+ group. Overall, we forecast GDP to grow by 4.1% in 2022, easing to 2.4% in 2023 as the World Cup impetus fades. Further out, non-oil expansion will be well supported by sizeable Vision 2030-linked investments and the targeted completion of $30 billion of gas megaprojects in 2027, after which the hydrocarbon sector should return as the main growth engine.

This year's spike in gas prices provides further general support for economic sentiment and especially government finances, though the impact is limited by Qatar's relatively small exports to Europe (estimated at 14% of all gas exports) where prices rose furthest, and longer-term oil-linked LNG contracts. We forecast large fiscal surpluses in both 2022 (16.0% of GDP) and 2023 (9.2%), which will also enable a sizeable reduction in public debt (from 58% of GDP in 2021), addressing previous calls by credit rating agencies in this regard. In addition to global factors, logistical challenges relating to the World Cup, rising inflation (currently 6%), post-World Cup spare capacity and delays in gas megaproject execution are near-to-medium term risks, though mitigated by Qatar's large external reserves, good reform progress, and solid credit rating.

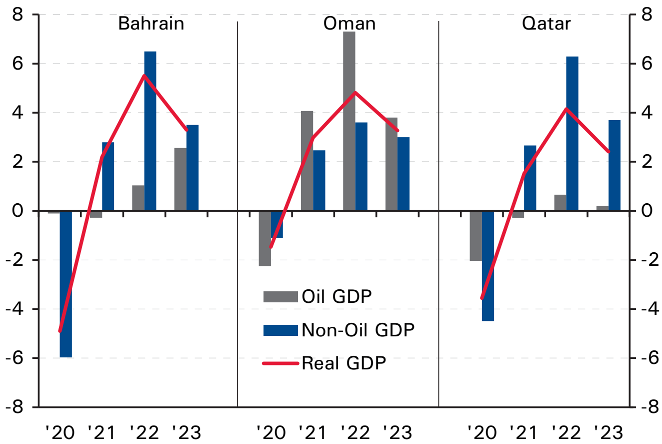
Key economic indicators

		Bahrain			Oman			Qatar		
		2021	2022f	2023f	2021	2022f	2023f	2021	2022f	2023f
Nominal GDP	$ billion	38.9	43.6	44.7	85.8	103.9	104.5	176.5	209.8	204.3
Real GDP	% y/y	2.2	5.5	3.3	3.0	4.8	3.3	1.5	4.1	2.4
- Oil sector	% y/y	-0.3	1.0	2.6	4.1	7.3	3.8	-0.3	0.7	0.2
- Non-oil sector	% y/y	2.8	6.5	3.5	2.5	3.6	3.0	2.7	6.3	3.7
Inflation (average)	(% y/y)	-0.6	3.6	2.8	1.5	3.0	2.3	2.3	4.3	3.2
Budget Balance	(% of GDP)	-6.5	0.6	0.1	-3.7	5.5	3.2	0.2	16.0	9.2
Current account balance	(% of GDP)	6.7	9.4	7.5	-3.8	5.7	2.1	14.6	18.8	12.1

Source: Official sources, NBK estimates

Chart 1: Real GDP

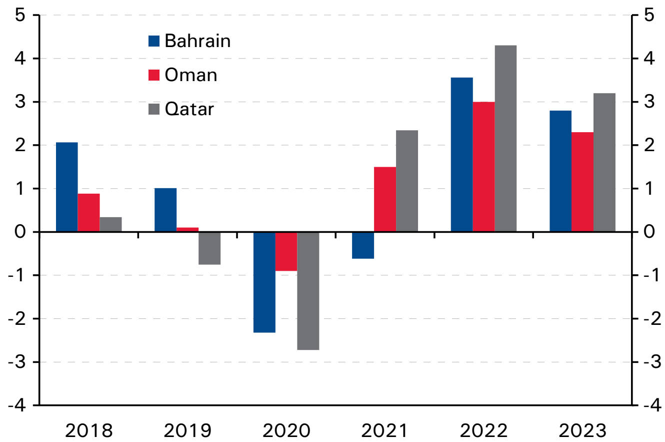
(% y/y)



Source: Government authorities, NBK forecasts

Chart 2: Inflation

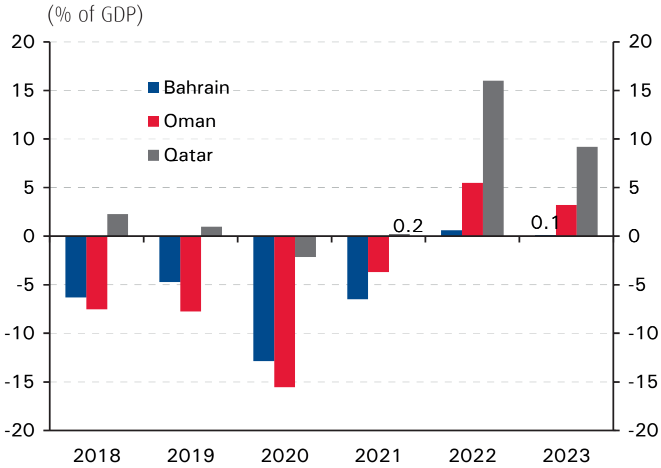
(% y/y)



Source: Government authorities, NBK estimates/forecasts

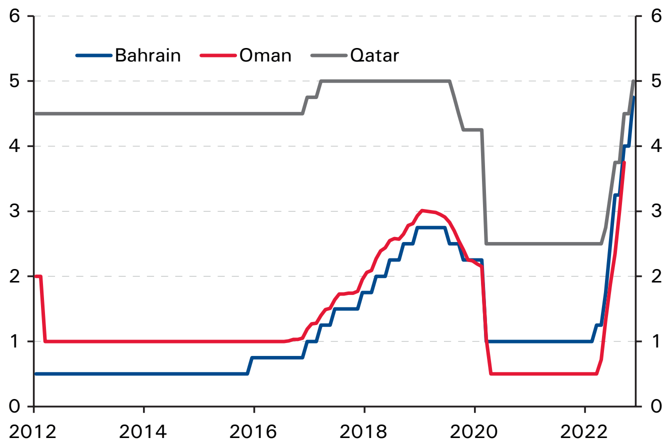
Chart 3: Budget balance

(% of GDP)



Source: Government authorities, NBK forecasts

Chart 4: Key policy interest rates*



Source: Haver *2022 figure as of Nov 6

Kuwait

The short-term macroeconomic outlook is positive thanks to higher oil production and robust private consumption, the latter seen in the strong consumer spending, real estate sales and household credit figures. High oil prices have bolstered the fiscal position—with the government expected to post its first fiscal surplus this year since 2014—as well as substantially easing previous liquidity constraints. Negative risks to the outlook are more acute in the medium-to-long term and center on limited progress on a comprehensive, reform-focused fiscal and economic diversification agenda to lessen dependence on the oil sector.

Oil production, consumer gains boost growth

Economic activity continues to recover post-pandemic, driven by output gains in both the oil and non-oil sectors and supported by firm government spending amid markedly higher oil prices. GDP growth is expected at 7.8% this year, largely due to double-digit increases in oil production (+12.1% y/y), before slowing in 2023 (+0.8%) on the back of OPEC+ output cuts. Kuwait's output quota for 2023 is 2.68 mb/d (-30 kb/d from the 2022 average), which would result in oil GDP falling by 1.1% y/y. Still, there is scope for a reversal in OPEC+ policy in 2023 if, as expected, the global oil market tightens significantly. In real terms, GDP should finally be back at pre-pandemic levels next year.

Buoyant consumer spending and relatively strong real estate activity have been major contributors to the expansion in non-oil output, estimated at an average of 3.1% in 2022-23. Demand for household (+12.8% y/y in August) and corporate credit (+6.4%) have also been supportive, the latter taking longer to recover due to still soft investment and pandemic-linked shortages in materials and labor. We expect the robust consumer activity to ease in 2023 as the post-pandemic bounce fades and interest rates rise. However, non-oil GDP could see a further boost next year as the 615 kb/d Al-Zour oil refinery – one of the world's largest refineries – begins ramping up output.

A notable weak spot is the projects market, where new awards have fallen to multi-year lows. This is a legacy of the pandemic, cost rationalization and bureaucratic impasse. Government tenders have been sparse, with adverse effects for a private sector still dependent on them for business. The authorities are preparing a new reform plan ('Program of Action') under the umbrella of Kuwait's Vision 2035 strategy to empower the private sector and spearhead economic diversification. A draft could be presented to the new parliament in the current legislative session, though swift progress will depend upon government-parliament relations being substantially improved.

Inflation slows as pandemic, Ukraine pressures lessen

Inflation appears to be moderating, as pandemic-era supply chain disruptions and pent-up demand slowly unwind. Inflation slowed to 4.1% y/y in August, having been as high as 4.7% in April on food, transportation and education price rises. Favorable base effects, tighter monetary policy, the strong dinar and easing global commodity prices and pressures should help trim inflation further, to 2.7% in 2023 from 3.9% in 2022.

Further monetary tightening ahead

The Central Bank of Kuwait (CBK) has loosely tracked the US Fed in tightening monetary policy this year, raising its discount rate by a cumulative 150 bps since March to 3.0%. The CBK has been more measured than GCC peers in responding to US rate rises, balancing the need for alignment with Fed policy, control of inflation and continued support for the non-oil economy. We expect further tightening ahead, with the now narrowed spread between Kuwaiti and US policy rates providing a higher chance of the CBK aligning more closely with Fed hikes going forward.

A first fiscal surplus in 8 years, easing liquidity constraints

The increase in oil prices since 2021 has dramatically improved the public finances. We forecast a budget surplus of KD5.3bn (9.6% of GDP) this year (FY22/23), the first surplus since 2014, and also next year (4.3% of GDP). The government is committed to fiscal restraint, even as it may reverse spending cuts penciled-in to the still-to-be approved draft budget from January, given that oil prices have exceeded the budget's oil price assumption of $65. We project modest, though positive, expenditure growth of 4.5% on average in 2022-23, with capex spending likely to be restrained, though development plan goals will necessitate this rising from current lows. Successive fiscal surpluses will help recapitalize the General Reserve Fund, which had been close to depletion. External buffers remain extremely strong, with $46bn in CBK reserves and around $700bn in assets held by the Kuwait Investment Authority. Public debt is also extremely low at 3.5% of GDP. An improvement in executive-legislative relations could see the long-delayed debt law passed in 2023, which would expand the available financing options.

Outlook positive, longer-term success hinges on reforms

Kuwait's near-term outlook is generally positive, thanks to the expectation of elevated oil prices and continued gains in private consumption, which should help see the country through the challenging external economic environment. Nevertheless, medium-to-longer term growth prospects hinge on the capacity to deliver structural reforms to lessen reliance on oil prices and shift the locus of economic growth to the private sector. These will need to encompass doing business, the labor market, education and fiscal sustainability among others. Measures to raise nationals' private sector participation rates are also essential, as are incentives to stimulate both domestic and foreign investment.

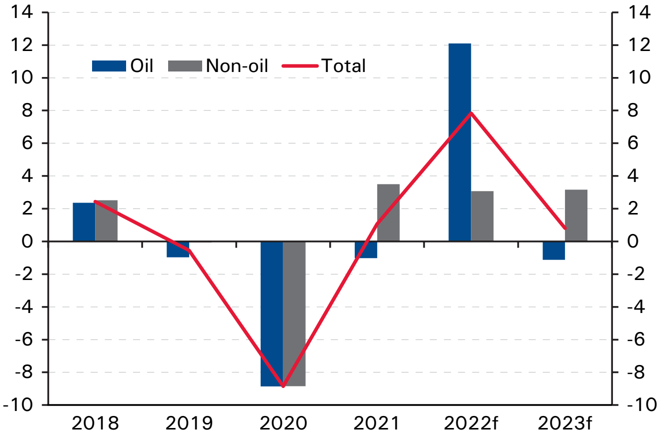
Kuwait key economic indicators

		2019	2020	2021	2022f	2023f
Nominal GDP	$ billion	136	106	136	175	169
Real GDP	% y/y	-0.6	-8.9	1.1	7.8	0.8
- Oil sector	% y/y	-1.0	-8.9	-1.0	12.1	-1.1
- Non-oil sector*	% y/y	-0.1	-8.8	3.5	3.1	3.2
Budget bal. (FY)	% of GDP	-9.5	-33.2	-6.9	9.6	4.3
Current act. bal.	% of GDP	10.1	1.4	27.0	33.3	27.5
Inflation (avg)	% y/y	1.1	2.1	3.4	3.9	2.7

Source: Official sources, NBK forecasts; *Includes refining

Chart 1: Real GDP

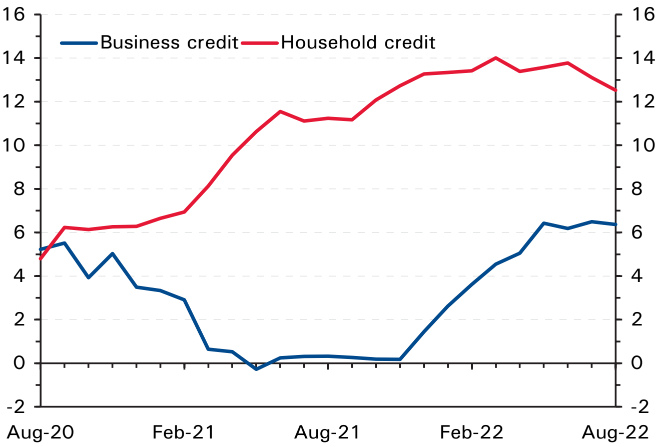
(% y/y)



Source: Central Statistical Bureau (CSB), NBK forecasts

Chart 2: Credit growth

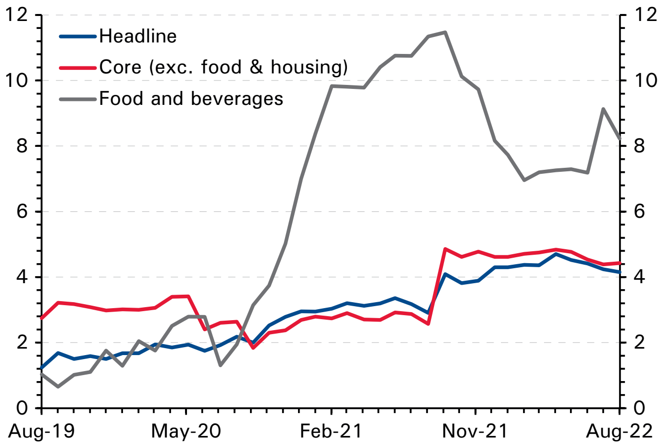
(% y/y)



Source: Central Bank of Kuwait (CBK)

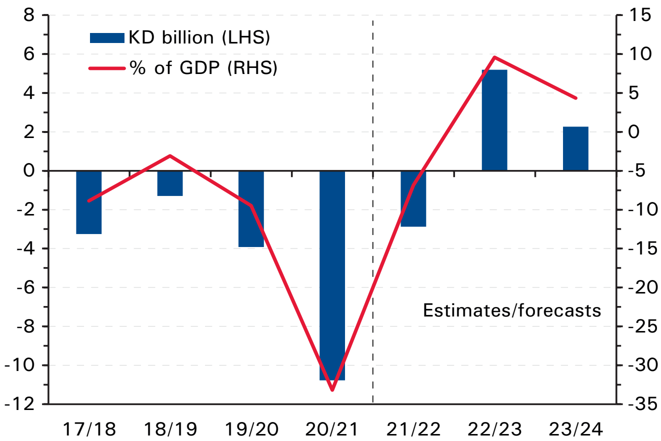
Chart 3: Inflation

(% y/y, avg.)



Source: CSB, NBK forecasts

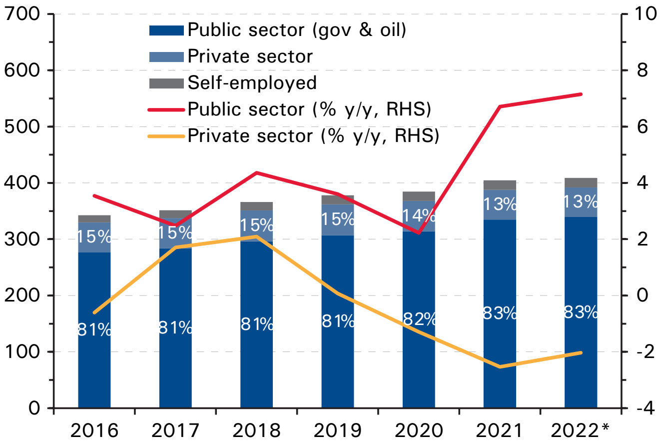
Chart 4: Fiscal balance



Source: Kuwait Ministry of Finance (MOF), NBK forecasts; fiscal year basis

Chart 5: Kuwaiti employment trends

('000', at year-end; % share of employed Kuwaitis labelled in chart)



Source: Public Institute for Social Security (PIFSS);* as of end-March

Saudi Arabia

Non-oil economic growth continued to be solid so far this year, led by the private sector (+5.9% y/y in 1H2022). Importantly, investment picked up strongly, auguring well for future growth as it indicates a solid expansion in production capacity. The positive momentum is expected to be sustained in the remainder of this year and in 2023, despite higher interest rates, lower oil prices, and some (likely easing) inflationary pressures. Despite an increase in budgeted spending and lower projected oil prices and production, we forecast another fiscal surplus next year. Lower-than-forecast non-oil growth, which could result for example from a weaker-than-expected resilience to a deteriorating global economic backdrop, is a main downside risk.

Robust non-oil sector to drive growth in 2023

Non-oil economic growth continued to be solid so far this year standing at 5% in 1H2022, following the 4.9% expansion in 2021. The private sector (+5.9% in H1) remained the main driver of growth, although the government sector's expansion picked up to 2.4% from 1.5% in 2021. Trade/restaurants/hotels witnessed the highest growth rate of 10.8% in H1, following a robust 8.7% expansion in 2021. Importantly, in terms of expenditure on GDP, gross fixed capital formation (i.e. investment) was by far the fastest growing, surging by 24% y/y in H1. This augurs well for future growth as it indicates a solid expansion in production capacity.

The positive momentum is expected to be sustained in the remainder of this year and in 2023, despite higher interest rates, lower oil prices, and some inflationary pressures. Consumer spending remains robust with the value of POS transactions up around 19% y/y through September. Credit growth remains solid at around 16% y/y as higher growth in corporate credit (+12% y/y) is compensating the softer expansion in mortgage lending. The latter, while beyond peak-growth, is still expanding at high rates of around 29% y/y through August. PMI levels are solid (latest at 57.2), with the new orders index at a strong 62.9. Given all that, we forecast the non-oil sector to finish 2022 with 4.7% growth, softening to 4% in 2023 on higher interest rates and a weaker global economic backdrop.

The ongoing reforms and effective policymaking remain key drivers of this favorable growth outlook. Recent reforms and strategic initiatives include the National Investment Strategy (targeting to push investment/GDP to 30% in 2030 from less than 24% in 2021), the Financial Technology Strategy, establishing a Saudi Investment Marketing Authority, and launching the new Companies Law. Meanwhile, given a 3.75% increase in the US federal funds rate since March, SAMA has hiked its policy rates by a similar 3.5% with further hikes expected given that US rates are seen rising by another 50-75 bps before year-end. Higher policy rates and a much faster expansion in credit than in deposits led to a surge in interbank rates, prompting SAMA to inject liquidity in the banking sector.

As for the oil sector, following the production surge this year, a low single-digit contraction is projected next year given the recent OPEC+ production cuts. We think it will be unsurprising if KSA continues to take a proactive and leading role, within OPEC+, in managing the global oil supply, including cutting or increasing production as need be. It is important to mention, especially given the oil market's potential tightness and OPEC's limited spare capacity, Aramco's plans to increase its sustainable capacity from its current 12 mb/d to 12.3 mb/d as early as 2025 and up to 13 mb/d by 2030. All in all, total GDP is expected to grow by a whopping 8.6% in 2022, falling to 2.1% next year, dragged down by the oil sector.

Inflation close to peak; unemployment continues to drop

Inflation continued to creep higher, standing at 3% y/y in October, but we project the peak will be reached later this year, and the average for the year will stand at 2.6%, before softening to 2.2% in 2023. Solid economic growth and steadfast Saudization initiatives continued to push the unemployment rate among Saudis lower, dropping to 9.7% in 2Q2022, down from a recent peak of 15.4% two years ago.

Budget surpluses are expected despite higher spending

The fiscal position improved sharply in 9M2022 on higher oil prices, increasing oil production, and despite higher-than-expected spending. Revenues increased by 36% y/y in 9M2022 as oil revenues soared 67%, while non-oil revenues fell by 4%. Expenditures increased by 14%, resulting in a fiscal surplus of around 5% of GDP in 9M2022 compared with a deficit of 2.3% in 2021. Looking ahead, given still relatively-elevated oil prices, ongoing growth in non-oil revenues, and despite the recent increase in budgeted spending over the forecast horizon, we forecast fiscal surpluses, standing at 2.9% and 0.8% in 2022 and 2023, respectively. The Public Investment Fund continues to play a central role in the economic diversification drive, by investing in promising sectors and companies, and whereby its investments can be seen as complementary to the government's fiscal expenditures. Surpluses are expected to be mostly used to beef up government deposits at SAMA rather than reduce debt levels, and accordingly we forecast the debt/GDP ratio to stabilize at around 24%, down from 30% in 2021.

The current account continued to expand (16% of GDP in H1) on higher oil prices, and we forecast it will remain comfortably in surplus over the forecast horizon. Lower-than-forecast non-oil growth, which could result from a weaker-than-expected resilience to a deteriorating global economic backdrop, is a main downside risk. In contrast, higher-than-forecast oil production, due to, for example, a partial reversal of the recent aggressive OPEC+ production cuts is an upside risk. Moreover, higher-than-projected oil prices (our house view is that Brent will average $90 in 2023) is another upside risk to our forecasts.

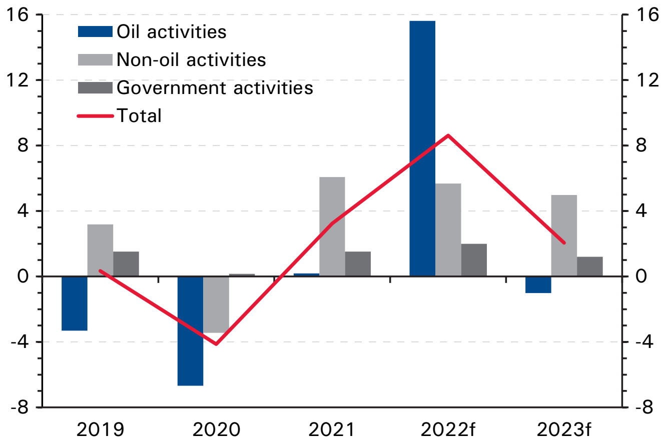
Saudi Arabia key economic indicators

		2020	2021	2022f	2023f
Nominal GDP	$ billion	703	834	1,032	1,028
Real GDP	% y/y	-4.1	3.2	8.6	2.1
- Oil	% y/y	-6.7	0.2	15.6	-1.0
- Non-oil	% y/y	-2.5	4.9	4.7	4.0
Inflation (average)	% y/y	3.4	3.1	2.6	2.2
Fiscal balance	% of GDP	-11.1	-2.3	2.9	0.8
Government debt	% of GDP	32.4	30.0	24.2	24.3
Current acc. bal.	% of GDP	-3.2	5.3	16.5	13.6

Source: National authorities, NBK forecasts

Chart 1: Real GDP

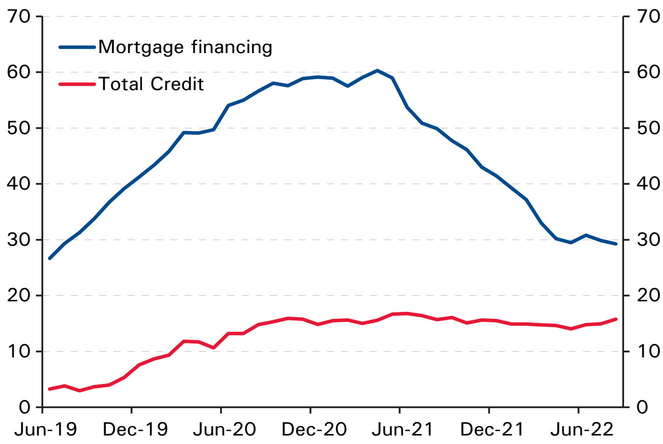
(% y/y)



Source: General Authority for Statistics (GASTAT), NBK forecasts

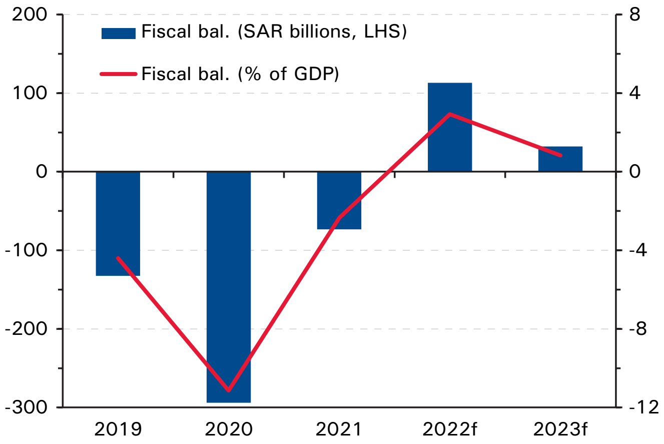
Chart 2: Credit growth

(% y/y)



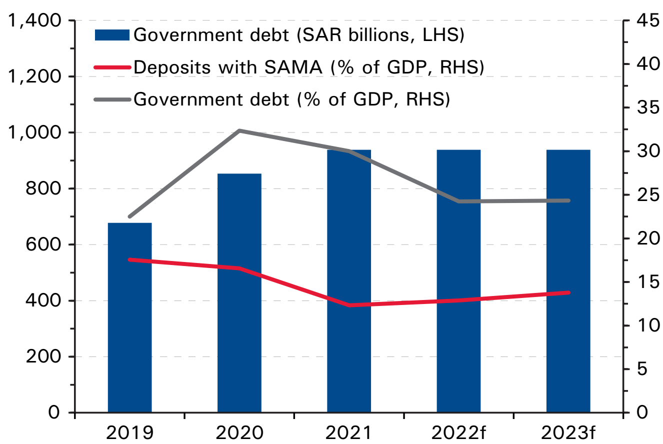
Source: SAMA

Chart 3: Fiscal balance



Source: Ministry of Finance, NBK forecasts

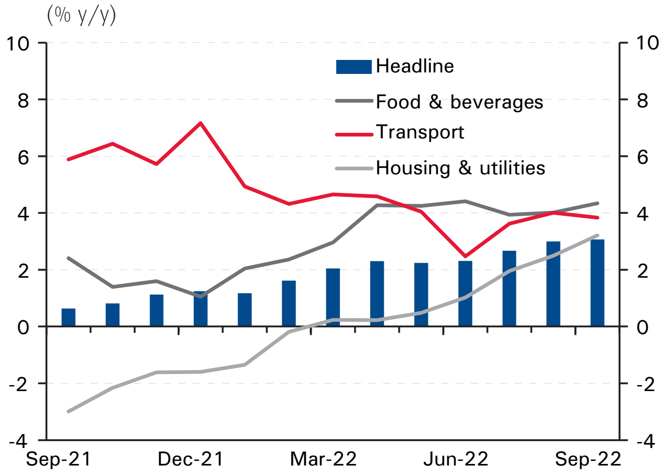
Chart 4: Government debt and deposits with SAMA



Source: GASTAT, Ministry of Finance, SAMA, NBK forecasts

Chart 5: CPI inflation

(% y/y)



Source: GASTAT

UAE

A strong rebound in tourism, buoyant real estate demand, high oil prices and rising oil output have helped deliver strong economic growth this year and although an easing is seen in 2023, our base case is for a further solid expansion of 3%. The positive medium-term outlook is reinforced by plans by ADNOC to ramp-up oil production capacity to 5 mb/d potentially to an accelerated time schedule. Downside risks include exposure to slowing global growth, tightening financial conditions, and a loss in competitiveness due to the strong dirham. The main upside risk would be higher oil prices lifting regional growth, optimism and liquidity.

Slower but still solid growth expected for 2023

GDP growth this year is expected to reach its strongest since 2016 at 5.3%, and although a slowdown is projected for 2023 underlying economic performance should remain solid, building on the UAE's position as a leading hub for regional business activity and investment, strong infrastructure, the government's pro-growth reform initiatives and plans to ramp up capacity in the hydrocarbon sector. Oil GDP is forecast up 8.7% this year reflecting OPEC+ production policy and a more modest 1.7% in 2023, which would leave oil output at 3.1 mb/d by next year-end. (Chart 1.) State oil firm ADNOC has reportedly brought forward plans to expand capacity to 5 mb/d (from 4 mb/d currently) to 2025 versus 2030 before, reflecting a desire to monetize oil and gas reserves more quickly ahead of the global energy transition. This goal looks ambitious, but the potential acceleration of its five-year $127 billion investment program (which covers both upstream and downstream sectors) provides a significant upside risk to the medium-term growth outlook.

Meanwhile, non-oil GDP enjoyed a post-Covid bounce to 8.8% y/y in 1Q22, taking output back above pre-pandemic levels. While this strength will not be sustained, the PMI activity gauge has drifted higher this year, reaching a three-year best of 56.7 in August signaling robust expansion despite sluggishness in export conditions. Supportive factors include a strong rebound in tourism, spillovers from the upcoming World Cup in Qatar, rising real estate demand, and high oil prices. We see non-oil growth at 4% overall this year. Slowing global growth, lower (though still high) oil prices and rising interest rates point to a softer performance in 2023, though our base case is still for a decent 3.4% expansion. Key strategic policy initiatives driving the medium-term outlook include the 'Circular Economy Policy' 2021-31 to encourage sustainable use of natural resources, the 'Digital Economy Strategy' aimed at doubling the sector's GDP contribution to 19.4% in 10 years, and 'Operation 300bn', which looks to double the industrial sector's GDP to AED 300 billion by 2031 especially via SMEs.

CPI inflation and house price rises to ease next year

Strong demand, supply chain disruptions, rising food and oil prices and a recovery in housing rents pushed inflation in Dubai to 6% y/y in August and 4.5% in the first 8M22 (up to date nationwide figures were not available). However, given the softer growth outlook, declining input costs, strong dirham and rising interest rates (the central bank has matched aggressive Fed policy tightening so far this year), we expect inflation to ease going forward and average 3.8% in 2022 and 3.6% in 2023 for the UAE overall. (Chart 2.) Residential real estate demand remains strong for prime properties with the large influx of investors, especially from Eastern Europe, helping push prices up 1.8% and 10.8% y/y in 1H22 in Abu Dhabi and Dubai, respectively. (Chart 3.) Demand next year could soften as this influx fades, interest rates rise and growth slows, and together with rising supply (a yearly average of 40,000 units, or 4.3%, in 2022 and 2023) will take some heat out of the Dubai market, leading to smaller price rises. Meanwhile, private sector credit growth has recovered to pre-pandemic levels this year, and the central bank's survey shows firms' lending demand at strong levels in Q2, with property and construction firms doing well though showing signs of softening looking forward. (Chart 4.)

Fiscal surpluses provide room for increased spending

The overall fiscal position remains solid, with the government recording only one relatively modest annual deficit (2.5% of GDP in 2020) through the pandemic period and now set to post large surpluses in 2022 (8.9%) and 2023 (6.4%). (Chart 5.) Key to this has been spending control, with cuts in both (non-wage) current and capital spending seen during the pandemic, the recovery in oil prices but also revenue diversification, which has limited the downside from volatile oil receipts. We project spending increases averaging 5% in 2022-23, covering wages and social welfare but also capital spending to support government-led initiatives. Aside from still-high oil prices, revenues will be boosted by the 9% tax on corporate earnings set for introduction in June 2023, yielding estimated annual receipts of 1.5-2% of GDP. The external accounts meanwhile are very strong, with the current account in persistent large surplus and the huge combined SWF assets of ADIA and Mubadala (estimated at around $1 trillion) providing a buffer against external shocks.

Outlook and risks

Despite this broadly positive base case picture, risks are skewed to the downside including the UAE's relatively high exposure to a potentially sharp slowdown in global growth, tighter financial conditions, the impact of dirham strength on competitiveness and inward investment, debt rollover at GREs and a flare up in regional geopolitical tensions. The main upside risk would be higher oil prices lifting regional growth, optimism and liquidity.

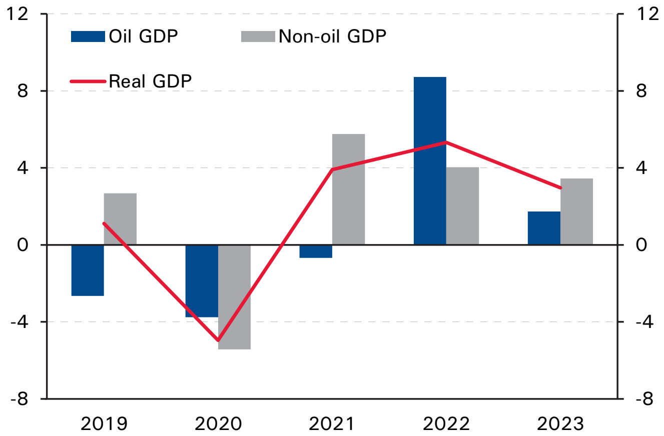
UAE key economic indicators

		2019	2020	2021	2022f	2023f
Nominal GDP	$ billion	418	349	415	487	482
Real GDP	% y/y	1.1	-5.0	3.9	5.3	3.0
- Oil sector	% y/y	-2.6	-3.8	-0.7	8.7	1.7
- Non-oil sector	% y/y	2.7	-5.4	5.8	4.0	3.4
Headline inflation	% of GDP	-1.9	-2.1	0.2	3.8	3.6
Budget Balance	% of GDP	2.6	-2.5	4.1	8.9	6.4
Current acc. bal.	% y/y	8.9	6.0	11.6	21.0	14.2

Source: Official sources, NBK estimates

Chart 1: Real GDP

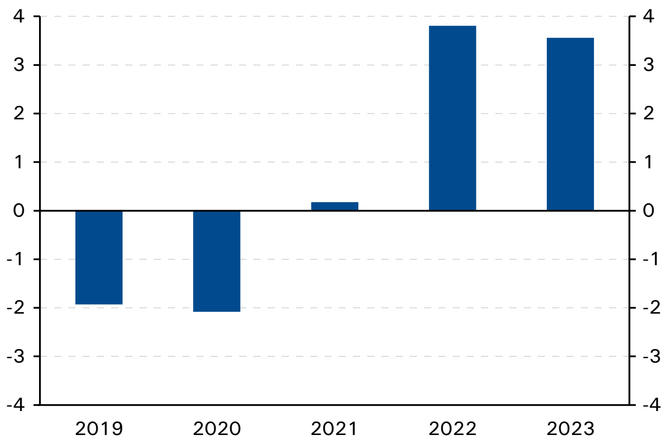
(% y/y)



Source: Federal Competitiveness & Statistics Centre (FCSC), NBK estimates

Chart 2: Headline inflation

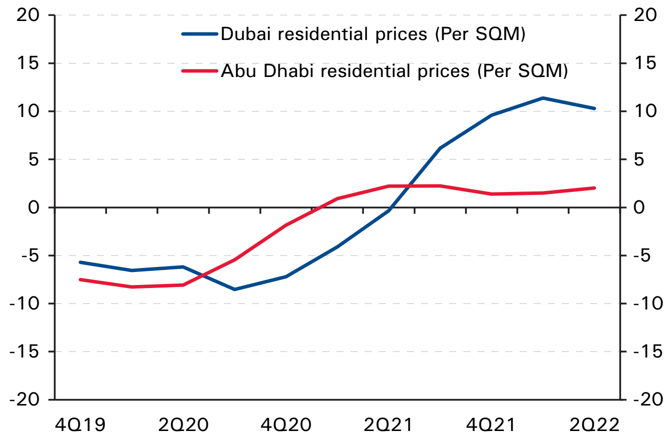
(% y/y)



Source: Federal Competitiveness & Statistics Centre (FCSC), NBK estimates

Chart 3: Abu Dhabi and Dubai residential prices

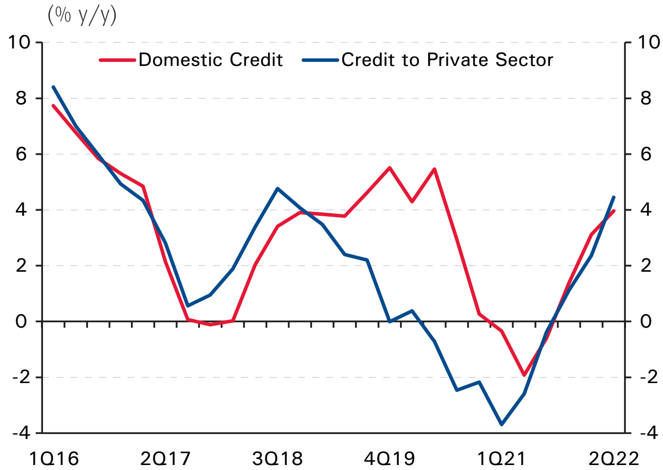
(% y/y)



Source: Bank of International Settlements

Chart 4: Credit growth

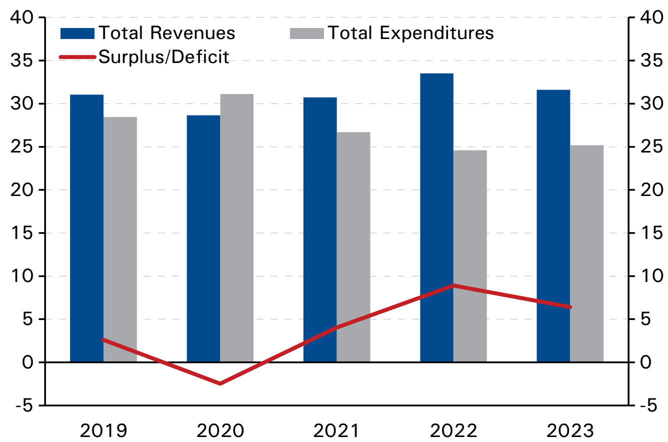
(% y/y)



Source: Central Bank of UAE

Chart 5: Fiscal balance

(% of GDP)



Source: Ministry of finance, NBK forecasts

Egypt

A combination of external pressures, domestic imbalances and a sharply lower currency have hit growth in 2022. But with the announcement of a new IMF deal in October, the path to recovery is now more visible. Monetary and fiscal reform measures tied to the deal will weigh on economic performance in 1H CY23, but this should give way to a stronger CY 2024-2025 on the back of lower inflation and availability of foreign currency. A key upside risk is a better-than-expected global economic environment allowing for a recovery in foreign investment and easier access to eurobonds. Downside risks include a delay in implementing the IMF program, a jump in international commodity prices that keeps inflation high and slow progress on structural reforms, even with the IMF deal.

Growth to pick up in 2023 as reforms proceed

Economic activity has been hit by a challenging external backdrop and as the sharp (and ongoing) drop in the currency – driven also by the economy's structural vulnerabilities – that began in March works its way through the system, pushing prices and interest rates up and weakening household and business spending. GDP growth had slipped to 3.2% y/y in 2Q22 (well below pre-pandemic levels), with recent PMI survey readings consistent with 3-4% growth in 2H CY22. This is still well clear of recession, but insufficient to absorb high population growth and make serious inroads into poverty levels. We see a gradual improvement in 2024, with the IMF financing deal announced in October helping to plug the external funding gap and re-catalyze the economic reform process – necessary both to improve economic growth and rebuild investor confidence. These reforms took a back seat to macroeconomic stabilization efforts during the pandemic. Alongside a more flexible currency, reforms should include steps to improve the business climate, increase the private sector's share of GDP and strengthen the public finances. Many of these objectives feature in the government's National Structural Reform Programme that aims to boost GDP growth to 5-6% by 2024/25.

Fiscal deficit to widen on lower growth, higher interest bill

Despite the tough economic climate, the government has managed to maintain overall control of the fiscal position, benefitting from reforms started in earlier years including subsidy cuts, a broadening of the tax base and improved debt management. In the first eleven months of FY21/22 (i.e. July-May) for example, revenue growth at 12% outpaced spending growth of 11% on strong tax revenues (+16%), partly driven by a Covid-related rebound in taxes on spending. Our base case is that the deficit narrowed slightly to 7.2% of GDP in FY21/22 and remains on a downward path in FY22/23. This also reflects expected conditionality from the IMF deal, which will help maintain reform momentum. However, this assumes that the government can contain growth in debt interest payments, which equate to around 8% of GDP and benefitted during Covid from interest rate cuts which are now going into reverse. According to the Minister of Finance, each 100 bps rate hike adds EGP30 billion to the fiscal deficit, equivalent to 0.3-0.4% of GDP.

Public debt stood at about 87% of GDP in June 2022, with external debt accounting for about one-fifth of this. The near-35% currency drop (versus the US dollar) this year has added around 7-8% of GDP to debt in local currency terms. Still, given high nominal GDP growth and a narrowing fiscal deficit, the debt ratio is projected to come down over time: the government is targeting 80% of GDP by 2026. The government also plans $40bn or 7% of FY22/23 GDP in privatizations over the next four years which could help cut the debt burden, although previous initiatives have been delayed due to execution challenges and unfavorable market conditions.

IMF $3-4bn loan to help plug external financing gap

Egypt reached a deal over a $3bn loan with the IMF in the form of a 3.8 years Extended Fund Facility (potentially rising to $4bn under an additional program being discussed). The loan will unlock further international and regional financial support which would be crucial to fill a large financing gap of $27bn over the coming 12 months. We expect the current account deficit to narrow in FY22/23 to 3.5% of GDP versus 3.7% in FY21/22 on possible import compression and a strong recovery in tourism. However, global monetary tightening is limiting access to international markets, thus larger GCC investments are crucial to cover the majority of the external gap.

Following the deal announcement, the pound fell by 18% to EGP24/$1, bringing its total year-to-date drop to 35%. While the pound could weaken over time if inflation is not brought under control (see below), there is also some upside in 2023 from a) a rebound if the pound reaches oversold levels, b) a possible Fed pivot (softening the US dollar), c) a recovery of foreign portfolio investment, and d) a return to the international bond market.

Central bank raised interest rates by 2% amid high inflation

Inflation accelerated to a three year high of 15.1% y/y in September as the pass-through effect of a weaker pound and the global inflationary wave continued to kick in. We see inflation rising further over the coming six months to average 17% for FY22/23 versus 8.5% for FY21/22 mainly on local factors such as the weakening of the pound and fiscal consolidation measures (potentially to include cuts in bread, electricity and petrol subsidies). The central bank raised policy rates by 2% as the IMF deal was announced and further tightening is possible over coming months. However, we expect that a window to cut rates could emerge from mid-2023 as inflation starts to fall.

The major risk surrounding this outlook is a delay in the implementation of the IMF program. Upside risks would include a stronger global economy, benefiting foreign investment and access to international capital markets.

Egypt key economic indicators

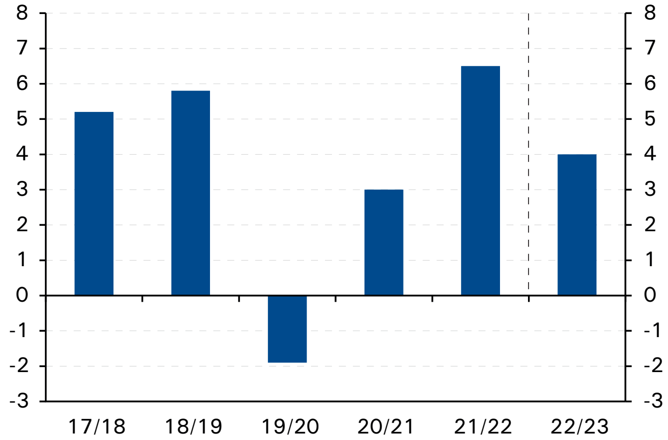
(year averages unless stated)

		FY20/21	FY21/22	FY22/23
Nominal GDP	$ billion	403	445	424
Real GDP	% y/y	3.3	6.6	4.0
Fiscal balance	% of GDP	-7.4	-7.2	-6.8
Inflation	% y/y	4.5	8.5	17.0
Current account	% of GDP	-4.6	-3.7	-3.5

Source: Official sources, NBK estimates

Chart 1: Real GDP

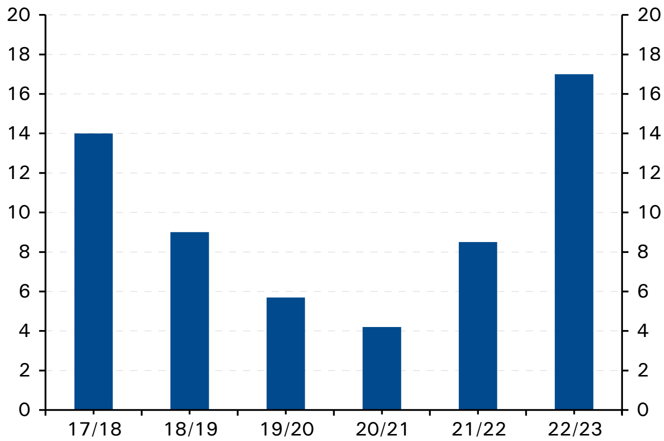
(% y/y)



Source: Refinitiv / Central Bank of Egypt, NBK estimates

Chart 2: Inflation

(% y/y)



Source: Capmas, Central Bank of Egypt, NBK estimates

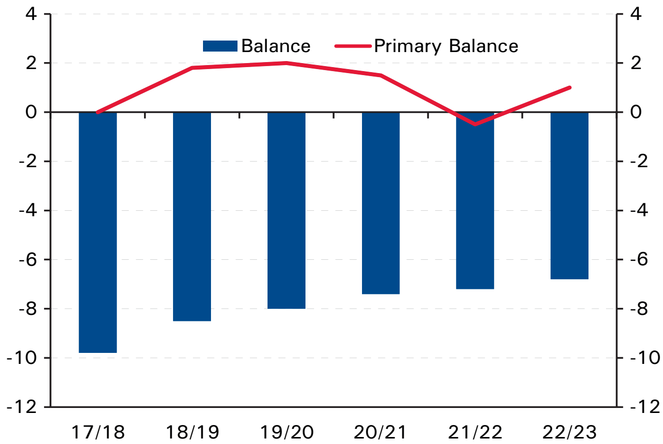
Chart 3: Interest rates

(Discount rate, %)

Source: Refinitiv / Central Bank of Egypt / NBK

Chart 4: Fiscal balance

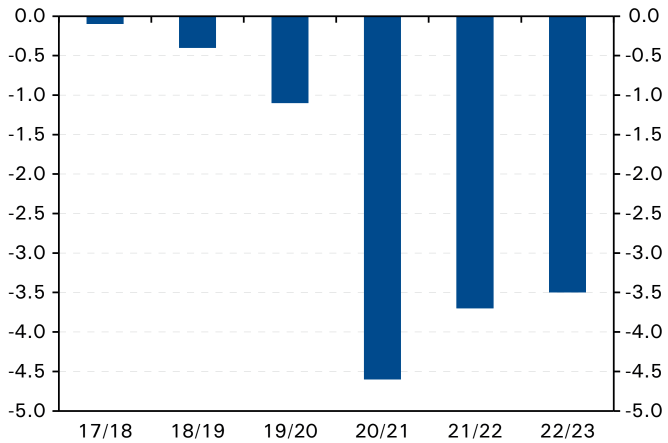
(% of GDP)



Source: Refinitiv / Central Bank of Egypt, NBK estimates

Chart 5: Current account balance

(% of GDP)



Source: Refinitiv / Central Bank of Egypt, NBK estimates

Regional economic data and forecasts

	Unit	2017	2018	2019	2020	2021	2022f	2023f
Bahrain								
Nominal GDP	USD bn	35.4	37.7	38.6	34.7	38.9	43.6	44.7
Real GDP	% y/y	4.3	2.2	2.3	-4.9	2.2	5.5	3.3
Hydrocarbon sector	% y/y	-0.7	-1.3	2.2	-0.1	-0.3	1.0	2.6
Non-hydrocarbon sector	% y/y	5.5	2.9	2.1	-6.0	2.8	6.5	3.5
Budget balance	% of GDP	-10.0	-6.3	-4.7	-12.9	-6.5	0.6	0.1
Current account balance	% of GDP	-4.5	-6.5	-2.1	-9.4	6.7	9.4	7.5
Inflation	% y/y	1.4	2.1	1.0	-2.3	-0.6	3.6	2.8
Kuwait								
Nominal GDP	USD bn	120.7	138.1	136.2	105.8	136.5	175.5	169.1
Real GDP	% y/y	-4.7	2.4	-0.6	-8.9	1.1	7.8	0.8
Hydrocarbon sector	% y/y	-9.2	2.4	-1.0	-8.9	-1.0	12.1	-1.1
Non-hydrocarbon sector	% y/y	1.3	2.5	-0.1	-8.8	3.5	3.1	3.2
Budget balance	% of GDP	-8.9	-3.1	-9.5	-33.2	-6.9	9.6	4.3
Current account balance	% of GDP	3.4	11.2	10.1	1.4	27.0	33.3	27.5
Inflation	% y/y	1.5	0.6	1.1	2.1	3.4	3.9	2.7
Oman								
Nominal GDP	USD bn	80.7	91.4	87.9	73.9	85.8	103.9	104.5
Real GDP	% y/y	0.3	1.4	-1.1	-1.5	3.0	4.8	3.3
Hydrocarbon sector	% y/y	-2.6	3.0	-2.6	-2.2	4.1	7.3	3.8
Non-hydrocarbon sector	% y/y	1.7	0.7	-0.4	-1.1	2.5	3.6	3.0
Budget balance	% of GDP	-12.1	-7.5	-7.7	-15.5	-3.7	5.5	3.2
Current account balance	% of GDP	-13.6	-4.7	-4.8	-11.7	-3.8	5.7	2.1
Inflation	% y/y	1.6	0.9	0.1	-0.9	1.5	3.0	2.3
Qatar								
Nominal GDP	USD bn	161.1	183.3	172.8	141.9	176.5	209.8	204.3
Real GDP	% y/y	-1.4	1.2	0.7	-3.6	1.5	4.1	2.4
Hydrocarbon sector	% y/y	-2.3	-0.3	-1.7	-2.0	-0.3	0.7	0.2
Non-hydrocarbon sector	% y/y	-0.9	2.2	2.2	-4.5	2.7	6.3	3.7
Budget balance	% of GDP	-6.8	2.3	1.0	-2.1	0.2	16.0	9.2
Current account balance	% of GDP	4.0	9.1	2.4	-2.1	14.6	18.8	12.1
Inflation	% y/y	0.4	0.3	-0.8	-2.7	2.3	4.3	3.2
Saudi Arabia								
Nominal GDP	USD bn	688.6	816.6	803.6	703.4	833.5	1031.9	1027.8
Real GDP	% y/y	-0.7	2.5	0.3	-4.1	3.2	8.6	2.1
Hydrocarbon sector	% y/y	-3.1	2.3	-3.3	-6.7	0.2	15.6	-1.0
Non-hydrocarbon sector	% y/y	1.3	-1.6	2.8	-2.5	4.9	4.7	4.0
Budget balance	% of GDP	-8.1	-5.7	-4.4	-11.1	-2.3	2.9	0.8
Current account balance	% of GDP	1.5	8.8	4.8	-3.2	5.3	16.5	13.6
Inflation	% y/y	-0.8	2.5	-2.1	3.4	3.1	2.6	2.2
UAE								
Nominal GDP	USD bn	390.8	427.3	418.3	349.7	415.3	487.6	482.6
Real GDP	% y/y	0.7	1.3	1.1	-5.0	3.9	5.3	3.0
Hydrocarbon sector	% y/y	-6.9	4.5	-2.6	-3.8	-0.7	8.7	1.7
Non-hydrocarbon sector	% y/y	4.2	0.1	2.7	-5.4	5.8	4.0	3.4
Budget balance	% of GDP	-0.2	3.8	2.6	-2.5	4.1	8.9	6.4
Current account balance	% of GDP	7.0	9.5	8.9	6.0	11.6	21.0	14.2
Inflation	% y/y	2.0	3.1	-1.9	-2.1	0.2	3.8	3.6
Egypt (fiscal year)								
Nominal GDP	USD bn	252.3	250.2	302.2	363.8	402.8	445.0	424.0
Real GDP	% y/y	4.1	5.3	5.6	3.6	3.3	6.6	4.0
Budget balance	% of GDP	-10.6	-9.0	-8.2	-7.9	-7.4	-7.2	-6.8
Current account balance	% of GDP	-6.1	-2.4	-3.6	-3.1	-4.6	-3.7	-3.5
Inflation	% y/y	23.3	22.0	13.9	6.0	4.5	8.5	17.0

International data

	Unit	2017	2018	2019	2020	2021	2022f	2023f
Brent crude oil (year average)	$ p/b	54.9	71.5	63.7	43.9	71.0	100.0	90.0
Rogers International Commodity Index*	Index	2,415.9	2,194.3	2,454.4	2,265.6	3,196.8	---	---
Eur/USD*	1$ = €	0.83	0.87	0.89	0.82	0.85	---	---
US Fed Fund Rate	%	1.50	2.50	1.75	0.25	0.25	---	---
MSCI World stock market index*	Index	2,103.4	1,883.9	2,358.5	2,690.0	3,231.7	---	---
MENA real GDP (IMF)	% y/y	1.9	1.4	1.0	-3.1	4.1	5.0	3.6
World real GDP (IMF)	% y/y	3.8	3.6	2.8	-3.0	6.0	3.2	2.7

Source: Refinitiv, Haver, official sources, IMF, NBK estimates; * latest available data

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