Arab Economic Outlook Annual Report 2015

The General Union of Chambers of Commerce, Industry & Agriculture for Arab Countries (GUCCIAAC)

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I. Economic Overview

a. Diverse Economic Scene

The Arab region has seen, on average, a positive economic expansion over the last few years, despite geopolitical tensions, political instability and social unrest.

Nevertheless, the economic scene in the region currently reveals an exceptionally diverse picture. Four Arab countries, namely Syria, Iraq, Libya and Yemen are suffering from violent conflicts that have devastated people's lives and national economies, with spillovers to neighboring countries, while Egypt and Tunisia are showing strong positive signs of gradual exist from the political transition tunnel. Other oil-rich countries are experiencing reasonable growth and macroeconomic stability, although they too face surrounding threats and undiversified economies.

The World Bank estimates a modest growth for the Arab region that will range between 3.1% and 3.3% in 2015, below the already low growth of 2014 that was approximately 3.5%[1]. It is estimated that the same path will continue in 2016. If the security situation improves, the regional average will surge to 4 to 5% in 2016[2].

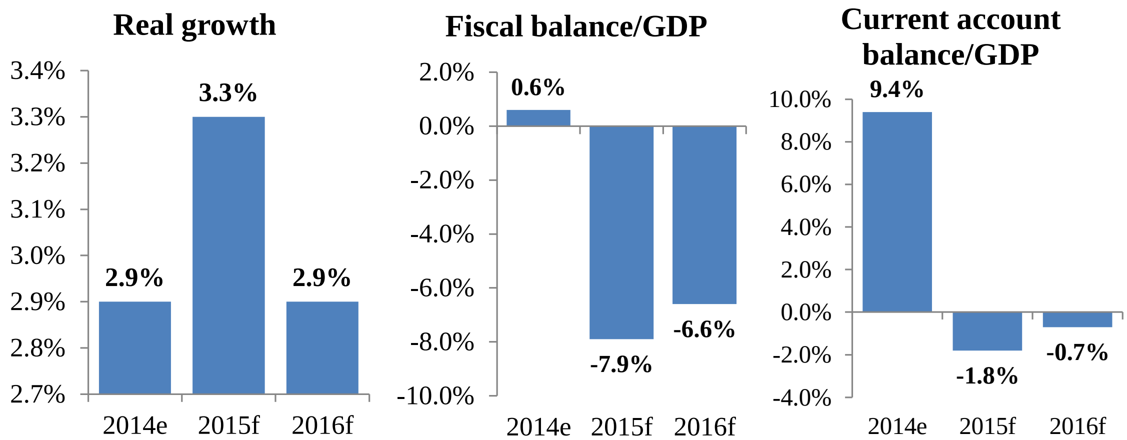
In addition to security troubles and conflicts in the region, a significant fall in oil prices in 2014 adds to the existing economic challenges. The international oil prices decreased by 60 percent in January 2015 compared to the level registered in June 2014[3]. Moreover, oil prices remained below 55 dollar/barrel during the first quarter of 2015.

b. Moderate growth and financial constraints

International financial resources forecast growth in the Arab region to increase modestly from 2.9% in 2014 to 3.3% in 2015, before slowing down to reach the same previous level of 2.9% in 2016[4].

It is also expected that the region may face budget and current account deficits, as oil prices fall well below fiscal breakeven levels. The slump in oil receipts will lead to significant slowdown in economic growth as spending slows and liquidity tightens.

Selected Economic Indicators



Source: HSBC

c. Impact of declining oil revenues

According to the World Bank, the Gulf countries could lose about US $ 215 billion in oil revenues in 2015, equivalent to 14% of their combined GDP[5]. The region's proven crude oil reserves reached 694.8 billion barrels in 2014, equivalent to 57.61% of OPEC's oil proven reserves. Saudi Arabia alone held 267 billion barrels at the end of 2014, corresponding to 38.4% of total proven oil reserves in the Arab region. It was followed by Iraq with 143.1 billion barrels, accounting for 20.6% of total, Kuwait with 101.5 billion barrels, contributing for 14.6% of total, and the UAE with 97.8 billion barrels, with a share of 14.1%.

The decline in oil revenues is expected to affect the economic growth of Arab oil-exporting countries, which contribute around 78 percent of the total gross domestic product of the Arab economies in constant prices[6], besides the expected effects in terms of declining capital and remittance flows from these countries to other countries in the region. Already the armed conflicts are increasingly disrupting intraregional economic activities and flows of trade and investment, one of the main sources for economic stabilization in the entire region.

On the other hand, the Arab oil importing countries are benefiting from the low oil prices, which are easing their balance of payments, fiscal constraints and cost of production and transport.

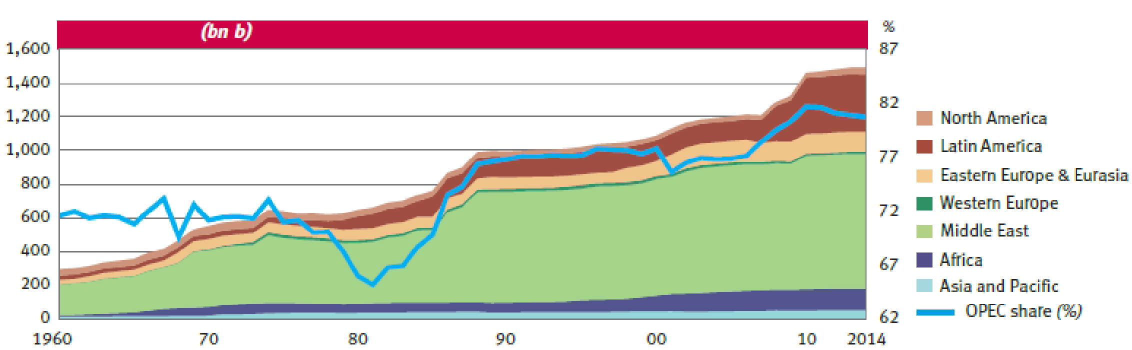
Major Oil Resources Indicators, 2014

	Proven Crude Oil Reserves (m barrels)	Natural Gas Reserves (billion cubic m)	Crude Oil Production (1000 b/d)	Crude Oil Exports (1000 b/d)	Natural Gas Exports (million cubic m)
Algeria	12200	4504	1193	623	44190
Iraq	143069	3158	3110	2516	...
Kuwait	101500	1784	2867	1995	…
Libya	48363	1505	480	41	4962
Qatar	25244	24531	709	595	122628
Saudi Arabia	266578	8489	9713	7153	…
UAE	97800	6091	2794	2497	15302
Total	694754	50062	20866	15420	187082
Total OPEC	1206004	95129	30683	22644	222219
% to OPEC	57.61	52.63	68.01	68.10	84.19

OPEC, **Annual Statistical Bulletin**, 2015.

The following Chart illustrates the significant climbing share of Arab oil wealth in comparison with the world reserves.

World Proven Crude Oil Reserves, 1960 – 2014



OPEC, **Annual Statistical Bulletin**, 2015.

d. Political troubles weigh on economic performance

The political troubles that the region faces weigh heavily on broader performance. Syria, Yemen, Libya and Iraq remain caught in conflicts, which in addition to disrupting their own economies, have profound implications for neighboring Arab countries.

Sluggish growth due to prolonged conflicts and slow pace of reforms that are necessary to attract investment are aggravating poverty and already high rate of unemployment in the region.

The total population of the Arab countries is estimated at about 370 million in 2013. The average population growth rate during 2000 – 2013 at 2.2% is considered as the highest rate across all world major regions[7]. Workforce was about 130 million in 2012, representing 36.1% of total population. The number of unemployed was estimated at 18.1 million and the average unemployment rate at 17.4%, the highest across world regions and almost three times the average global unemployment rate. This average entails great disparities that range from around 40% in Yemen to 0.3% in Qatar.

II. Hardships in foreign and regional trade

a. Implications on foreign trade

The regional conflicts led to major interruptions and deterioration in trade in many Arab countries. They also added to the impacts of declining oil prices and fragile growth in the world economy, especially in the Euro zone area. In 2014 Arab exports declined by 5.1% from previous year to US $1497 billion, while Arab imports expanded by 5.6% to US $1172 billion for the same period.

Arab Foreign Trade
($ Billion)

	Average 2000-2010	2011	2012	2013	2014	% Change 2013-2014
Arab Exports	639	1346	1508	1502	1497	-5.1
% of World Exports	4.9	6	6.7	6.4	6.2	-0.3
Arab Imports	485	921	1042	1110	1172	5.6
% of World Imports	3.8	4.2	4.7	4.9	5	0.1

Source: Arab Institute for Guaranteed Investment and Export Credit, ***Quarterly Bulletin***, January 2015, from IMF.

In many Arab countries trade is quite far from being an engine for growth and development. Its percentage share of GDP is way below other emerging and developing economies, while the technological ingredient and the value added component in the exported goods are quite minimal.

Efficiency in trade logistics varies largely between the Arab countries. The UAE ranks in the first place in the region and assumes the 27th rank between 160 world countries, while Somalia occupies the bottom of the world list[8]. Obstacles that face land-transported trade increase trade costs by an average of 40%[9].

Although maritime trade is the major vehicle for international trade, it is only marginal in the Arab region. Only six Arab countries rank relatively well in terms of the logistics performance index, namely UAE, Saudi Arabia, Egypt, Morocco, Oman and Lebanon[10]. Improving maritime logistics must be a major investment affair for the Arab Governments, in addition to provide the necessary incentives for the private sector to investment in this vital sector.

b. **Repercussions of conflicts on regional trade**

The continuing conflicts in a number of countries in the region levied heavily on trade activities in the region, especially the intra-regional trade between the Arab countries. The latest wave of violence has in fact brought about a real trade shock by redrawing the region's economic boundaries, the true scale and significance of which are still unfolding. The consequences are being felt most acutely in the Levant that used to have strong economic ties between Iraq, Jordan, Lebanon and Syria. Trade among these countries had been higher, on average, than among other Arab countries, but it has collapsed as violence has mounted. In particular, Syria's border recurrent closures have impeded regional trade, by discontinuing or cutting off a key route connecting the wider Levant and the Gulf States.

Consequently Lebanon was the first to suffer and manufacturers and farmers lost most of its markets in Jordan, Iraq and the Gulf. With the closure of Jordan's last border crossing with Syria in 2015, it is now facing a similar fate. A recent World Bank study estimates that the Levant region has lost nearly US $35 billion over the first three years of Syria's war crisis[11]. Now the conflict in Syria is in its fifth year and is spreading its domination in neighboring countries' outlook. In Lebanon, refugees now comprise over one quarter of the population[12] and are suffering hardships and straining local communities, adding to poverty and unemployment, and placing further pressure on the economy's already weak public finances and infrastructure.

c. GAFTA structural impediments

In 1997 the Arab States established the Greater Arab Free Trade Area (GAFTA) for gradually exempting goods of Arab origin from customs duties and other fees and charges, in addition to lifting of all non-tariff barriers on trade between member countries. Although its requirements were supposed to be completely fulfilled in January 2005, it is still facing many restrictions. Although elimination of tariffs achieved significant progress, a number of countries are still applying long negative lists of exceptions that significantly reduce the number of exchanged goods benefiting from GAFTA preferential advantages.

According to a survey conducted in 2014 by the General Union of Chambers of Commerce, Industry and Agriculture in Arab Countries (GUCCIAAC), non-tariff barriers stood as major obstacles to the free movement of trade between the Arab Countries[13]. The number of companies participating in the survey totaled 172 from 16 Arab countries, and it covered the following categories:

- Customs tariffs.
- Fees equivalent to customs tariffs.

- Non-tariff barriers, including seven items, namely: time to cross borders, technical barriers, financial barriers, barriers on licenses, monopolies, price control and restrictions on quantities.
- Cost of transportation of goods.
- Entry Visas to GAFTA member States.

The results of the survey showed that four major impediments received 50% or more of negative responses from participants, as follows;

- In the 1st place was the cost of transportation of goods, with negative replies coming from 70.93% of participants, as compared with 51.69% corresponding to the survey of the previous year 2014. The relatively high transportation cost is largely due to poor and inefficient infrastructure between the Arab countries.

- The 2nd most important obstacle was the time to cross borders, with 65.12% of the participants reported negatively on this issue, against 52.81% for the previous year. This is mainly due to inefficient handling and execution of transactions, manual inspections, repetition of procedures at different borders and poor infrastructure.

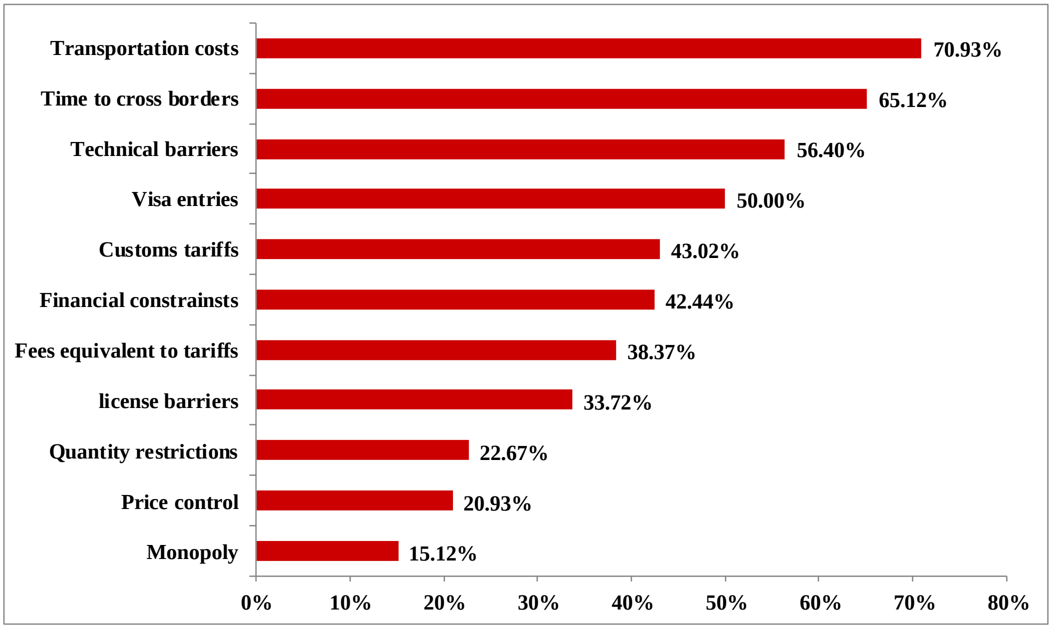
- In the 3rd place came the technical barriers, with those negatively responding accounting for 56.4% of total responses, compared with 46.07% for the previous year.

- The 4th rank was for Visa entries, where 50% of participants reported to face difficulties in this respect. This was higher than the previous year results that were at 47.19%.

The difference in results between the questionnaire of 2015 and that of the previous year can be largely attributed to the increase in number of participating companies, as their total was almost double the total of the previous survey, providing more dependable results.

The following Chart shows the relative importance of trade barriers facing regional trade according to the results of the questionnaire of 2015.

Major barriers to regional merchandise trade exchanges (% of negative responses)



Source: General Union of Chambers of Commerce, Industry & Agriculture for Arab Countries, "**Greater Arab Free Trade Area, 2015-2016: Evolving challenges from Arab and international developments**", May 2015.

III. The investment scene

a. Foreign direct investment

The latest United Nations Conference on Trade and Development (UNCTAD) World Investment Report, revealed that FDI inflows to the Arab Region declined by 7.5% in 2014 to US$ 43.9 million, from US$ 47.5 million in 2013, and US$ 66.8 million in 2010, as shown in the following Table. Such declines have negative repercussions, implicating a decrease in economic activity and a rise in poverty and unemployment rates. They were also accompanied by a declining Arab share in global FDI inflows from 4.9% in 2010 to 3.6% in 2013 and further to 3.2% in 2014.

Likewise, FDI outflows from the Arab countries declined by 12.7% to US$ 33.3 billion in 2014, although 58.1% more than the level achieved in 2010.

The Table also reveals that the United Arab Emirates remains the highest recipient of foreign investments for the second consecutive year, despite a decline from US $10488 million in 2013 to US $10066 million in 2014. Saudi Arabia came in the second place, with FDI also declining from US $8865 million to US $8012 million for the same period, and well below the levels recorded in the period 2009 – 2012. Within the non-GCC group, Egypt registered the highest increase in FDI, followed by Morocco and Lebanon.

As for FDI outflows, Kuwait occupied the first rank and contributed for around 40% of the total FDI Arab outflows, followed by Qatar and Saudi Arabia.

FDI Inflows and Outflows in the Arab Countries, 2010, 2013 – 2014 ($ million)

	FDI Inflows to Arab Countries			**FDI Outflows from the Arab Countries**		
Country	**2010**	**2013**	**2014**	**2010**	**2013**	**2014**
UAE	5500	10488	10066	2015	2952	3072
Saudi Arabia	29233	8865	8012	3907	4943	5396
Egypt	6386	4192	4783	1176	301	253
Iraq	1396	5131	4782	125	227	242
Lebanon	3748	2880	3070	487	1962	1893
Morocco	1574	3208	3582	589	332	444
Jordan	1651	1747	1760	28	16	83
Algeria	2300	2661	1488	220	117	-
Sudan	2064	1688	1277	-	-	-
Oman	1243	1626	1180	1498	1384	1164
Tunisia	1513	1117	1060	74	22	39
Qatar	4670	-840	1040	1863	8021	6748
Bahrain	156	989	957	334	1052	-80
Mauritania	131	1126	492	4	4	4
Kuwait	1305	1434	486	5890	16648	13108
Djibouty	37	286	153	-	-	-
Somalia	112	107	106	-	-	-
Palestine	206	176	124	84	-48	-32
Libya	1909	702	50	2722	180	940
Comoros	8	9	14	-	-	-
Yemen	189	-134	-578	70	73	73
Syria	1469	-	-	-	-	-
TOTAL	**66800**	**47458**	**43904**	**21086**	**38186**	**33347**

Source: Unctad, **World Investment Report 2015**, June 2015

b. Mergers and acquisitions

Investors' activities of mergers and acquisitions in the region witnessed resilience performance in the Gulf Cooperation Council (GCC) countries, while the remaining countries of the region attracted a smaller share of the flow, except for some countries like Egypt and Morocco that witnessed a sustained uptrend.

In 2014, MENA mergers and acquisitions deals went up by 6% to 468 deals, while their value dropped by 11% from 2013 levels to US $44.9 billion[14]. The positive trend is expected to continue up by 10% in 2015, as most of the transactions occur in consumption led sectors, such as food and beverages, retail, healthcare and education, which have little correlation to economic activity and changes in oil price.

IV. Private Sector Prospects amidst rising challenges

a. Repercussions of turbulences

The private sector in the Arab Mashreq sub region suffered from the consequences of armed conflicts and associated violence. Iraq and Syria were hit from economic infrastructure destruction and supply chain disruption. Private sector activities were severely constrained because of frequent disruptions in energy supply and logistical chains. Jordan and Lebanon maintained moderate domestic demand expansion, although the growth potential of both countries dropped critically, given the growing number of residents owing to high influx of Syrian refugees. Egypt has regained stability with increasing business confidence and improved foreign capital inflows. The Mashreq countries are likely to benefit from lower oil and commodity prices, but an economic slowdown in GCC countries is expected to weaken positive spillovers and transfers.

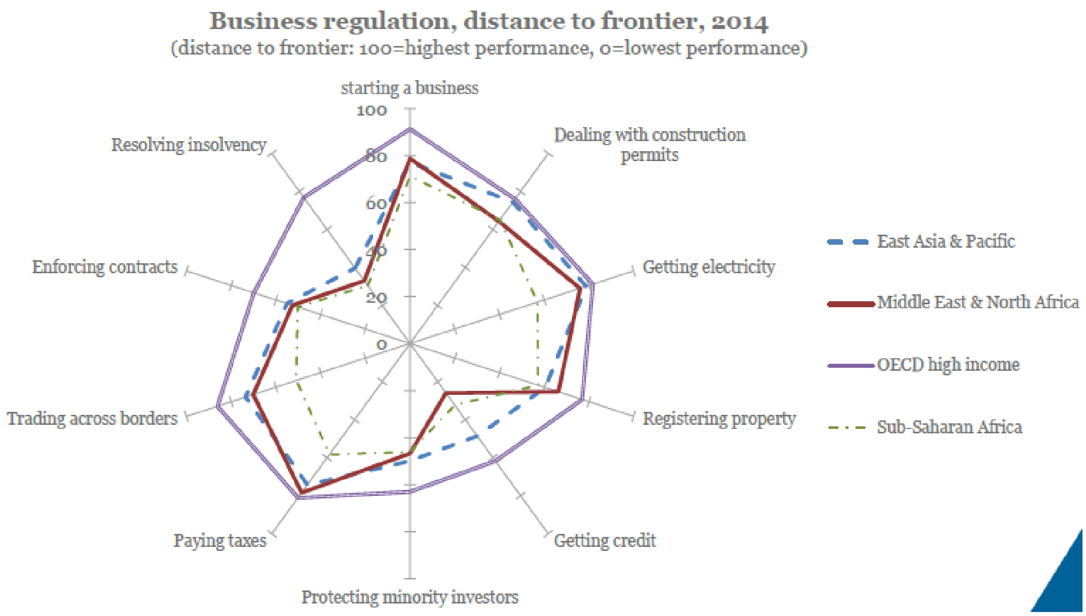
b. Investment climate

Improving the investment climate by enhancing the business and regulatory environment is necessary for maximizing the role of the private sector, repatriating some of the Arab investments abroad and enhancing foreign direct investment that acts, not only as an external source of financing for development, but also as a conduit for the transfer of modern technology and sophisticated production and management methods, and which significantly contributes to labor force training. In this regard, foreign direct investment that follows social and environmental standards and supports sustainable industrialization and the creation of decent jobs should be promoted.

Promoting competitive trade and investment regimes and regional investment integration are key elements to raise FDI inflows, stimulate intra-regional investment and integrate with global value chains.

Reform is imminent for providing the proper investment climate for the private sector and for an environment conducive to innovation and the development of new economic sectors. Currently, the private sector in most Arab countries does not create enough jobs. Around 30%[15] of the Arab world youth is unemployed - the highest rate in the world. Enterprise creation falls behind other world regions and women are underemployed. The World Bank estimates that closing the gender gap could increase GDP by 25%.

The Arab Governments need to build a better regulatory, legal and financial system for innovation and entrepreneurship. The following Chart identifies two major key areas for reform to improve the business regulation. The first one is resolving insolvency of enterprises and the second is getting credit. Other areas for reform in relative importance include trading across borders, enforcing contracts, protecting minority investors, followed by starting a business, then dealing with construction permits, registering property, getting electricity and paying taxes.



Source: World Bank, Doing Business 2015.

The public sector is requested to provide an enabling domestic environment, including good governance, sound economic policies, solid democratic institutions responsive to people’s needs, improved infrastructure, rule of law and the adoption of national sustainable development financing strategies. Although there is a need to mobilize both public and private finance to achieve the sustainable development goals, private finance is not a perfect substitute for public finance, but rather complementary to it.

Nevertheless the private sector is a driver of growth and a major partner for development financing; increased investments in productive sectors with high job creation potential is essential for sound and inclusive development.

Exploring forms of innovative financing and the promotion of blended finance, in particular the development of new models for public-private partnerships should be encouraged. However, public-private partnerships are not equally suitable for all sectors and should therefore not been seen as a perfect substitute for the role and responsibilities of the public sector, but rather as complementary to it.

Improving the investment legal and institutional grounds is crucial to attract foreign and local investors. The Arab world is well abundant with private financial wealth which is estimated at $4.2 trillion in 2014 and projected to expand at an annual rate of 9.3% between 2014 and 2019 to reach $6.8 trillion in 2019, to account for 3.5% of global private financial wealth[16]. It is expected that private financial wealth in Saudi Arabia will reach $2 trillion in 2019, to account for 22.7% of projected wealth in the region, followed by the United Arab Emirates with $1 trillion and 11.4% of the total[17].

In 2014, Bahrain had the second highest density of millionaires in the world after Switzerland, with 123 millionaires per 1000 households. Qatar had the third highest density with 116 millionaires per 1000, and Kuwait had the fifth highest rank with 99 millionaires as Singapore took the fourth place in the list.

V. Fields of opportunity

a. Infrastructure

Infrastructure plays a vital role for growth, job creation and regional integration. It is expected that more than US$ 228 billion worth of contracts are to be awarded in the Middle East & North Africa region[18]. The Arab world infrastructure needs through 2020 are estimated at 7% of annual regional GDP[19].

With countless opportunities available, the private sector will be the key to closing the infrastructure gap in the Arab region. Public-Private-Partnerships (PPPs) are fundamental elements for infrastructure procurement. Equally, legal and institutional frameworks are critical factors to move forward in this respect.

In the Gulf Cooperation Council (GCC) alone, it is estimated that the new awarded construction and infrastructure projects will reach US $ 173 billion in 2015, an annual increase of 1.4% and a relative compound annual growth rate of 5% between 2008 and 2014[20]. Projects include various infrastructure sectors, from roads to rails, hotels to hospitality, education to electricity and telecoms, fresh water to sewerage facilities, and city engineering to airports and Expos.

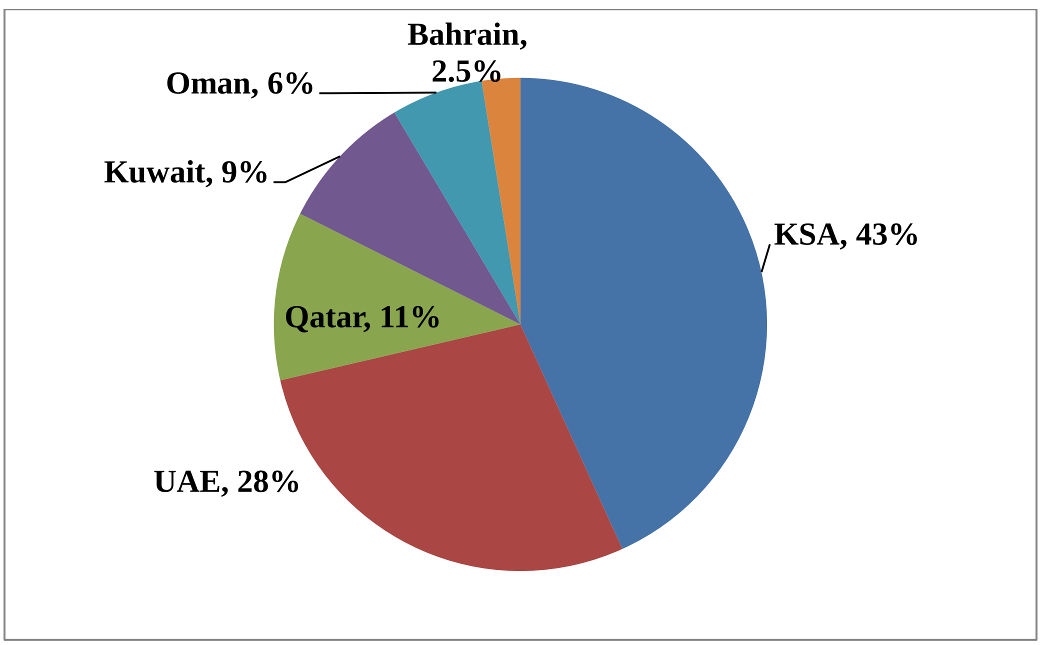
The following Table illustrates the distribution of planned and underway projects in GCC countries valued at US $2.8 trillion. Saudi Arabia accounts for 43% of the total, followed by UAE with 28%, then Qatar at 11%, Kuwait at 9%, Oman at 6% and Bahrain at 2.5%. The projects are mainly in the construction sector, followed by transport, power, oil, chemicals, natural gas, water and industry.

Projects Planned and Underway in GCC Countries (US $ million)

	Chemical	Construction	Gas	Industrial	Oil	Power	Transport	Water	Total
KSA	64916	475218	25402	28717	23409	332305	217569	36035	**1203571**
UAE	24809	539793	21083	8996	50899	35055	99226	6253	**786114**
Qatar	1484	139843	12889	970	16559	8785	103083	16098	**299711**
Kuwait	565	80080	11848	250	55188	29019	46876	8732	**232558**
Oman	15450	43160	25712	12179	14659	9039	36506	6860	**163565**
Bahrain	5000	30967	1258	4656	5025	6148	11050	1778	**65882**
TOTAL	**112224**	**1309061**	**98192**	**55768**	**165739**	**420351**	**514310**	**75756**	**2751401**

Source: Deloitte GCC Powers of Construction 2015.

Infrastructure Projects by Country



Source: Deducted from ibid.

However, other Arab countries suffer from a huge spending deficit on infrastructure. According to the World Bank, the MENA countries taken together invest only about 5% of their collective GDP in infrastructure, compared with a world average of 10%[21]. Investment in infrastructure provides healthy returns for investors ranging from 5% to 25%, and creates much needed jobs for the region[22]. It is estimated that for every US $1 billion invested in infrastructure approximately 26 thousand jobs are created in GCC countries[23]. The number of job opportunities created for the same expenses rises to more than that in other Arab countries and can reach 40 thousand jobs in Iraq, and much more in oil-importing countries such as Jordan where it is estimated to create 100 thousand jobs[24].

b. Digital market

The Arab world digital economy is expected to double within the next three years[25]. The region is quickly adopting latest internet and mobile innovations and technologies in business and economic life in general to capture increasing accessibility of information on markets.

Nevertheless, there are wide disparities between the Arab countries with respect to the network readiness index. The UAE stands on top of the region and ranks in the 23rd place among 143 global countries, followed by Qatar at the 27th rank, then Bahrain at the 30th place, then Saudi Arabia (35th), Oman (42nd) and Kuwait (72nd)[26]. In the rest of the region, only Jordan (52nd) features in the top half of the world rankings. Morocco follows at the 78th rank, then Tunisia (81st), Egypt (94th), Lebanon (99th), Algeria (120th), Libya (131st), Yemen (136th), and Mauritania (138th).

The new Digital economy in the Middle East is set to exceed US $30 billion by 2018, following almost 30 per cent growth in 2015[27]. The emergence of the digital economy is backed by initiatives such as ‘smart cities’, thus increasing the demand for a holistic ICT approach to digitize business processes across platforms, cloud-services, analytics and citizen-oriented applications. It is anticipated that the need of ICT skills will increase. Therefore, public and private sectors must be prepared to invest in ICT learning, training and e-business skills.

c. Focus on Egypt

Since the second half of 2014, the new administration in Egypt was highly successful in restoring political stability and security and managed to draw international attention to reforms and recovery. Many new reforms were introduced and helped the economy reach spectacular numbers that haven’t been seen since the beginning of the political crisis in 2011.

The Egyptian State has embarked on a number of national large-scale projects that aim at enhancing the competitiveness of the economy, creating employment opportunities and attracting foreign and domestic private investments. The Suez Canal Development Project (SCDP) capitalizes on Egypt’s strategic location at a crossroads for international trade. It includes expanding the capacities of a number of existing sea ports, establishing large-scale logistics areas and state-of-the-art industrial zones.

The project will position Egypt as a regional and international industry and trade hub. The targeted industries include, but not limited to, logistics, pharmaceuticals, automotive, textiles and ship building and maintenance. It will also benefit from the ongoing expansion of the Suez Canal, whereby a 72 km long parallel is expected to significantly cut transit time and increase daily traffic.

In addition to large scale industrial projects, the government is developing 15 new roads with a total distance of 3200 KMs to ensure improve connectivity and facilitate the movement of goods and services across the different governorates. This will help improve the economics of many industries and allow investors to access new internal and external markets.

Over the past 5 years, annual oil and gas production grew on average by 1% compared to annual average consumption growth of 5.3%. Hence, bridging the energy supply/demand gap became at the forefront of Egypt's economic reform agenda, which includes a 5-year plan to increase energy efficiency by 10-15% with estimated annual savings of US $6-8 bn.

The Egyptian economy is becoming more reliant on private investments over time. Private sector's share in total investments increased from 50% in 2002 to 62.2% in 2013/14 indicating a maintained policy commitment to enhance private sector's role in the economy. Leveraging investments into infrastructure is one of the top priorities of the government's economic agenda, which will enable private investors to access new sectors and markets.

Though private investments are significant in most sectors, there's still a strong potential for higher private investments especially in previously untapped sectors.

The renewable power sector is a one example where the government encourages more private sector investments by introducing a rewarding feed-in tariff structure.

VI. **Conclusion**

In spite of deepening and spreading conflicts in the region, as well as, in many cases, a challenging internal socio-political environment, the Arab countries, in general, have broadly maintained macroeconomic stability. At the same time, however, their economies are not delivering the growth rates needed for a meaningful reduction in unemployment.

Notwithstanding diversity of conditions and uneven economic growth, countries should quickly advance structural reforms to foster higher and more inclusive growth, and continue to strengthen fiscal and external buffers to maintain stability amid heightened uncertainty.

Coordinated support from the international community will be crucial in the form of financing, improved trade access, and capacity building assistance. Policy coordination efforts through regional cooperation are urgently needed to optimize the use of the region's human capital and financial wealth so as to reach a higher sustainable regional growth path.

The development of financial systems in Arab countries by promoting sound banking practices and expanding debt and equity markets and other financial institutions, including the insurance industry, is a priority. Enhancing the capital market infrastructure is vital for attracting long-term investments, at the regional and national levels.

Ensuring financial inclusion through innovative tools, such as digitized payments and mobile banking, eliminating gender-based financial discrimination and empowering small and medium enterprises, constitutes a strong base for generating employment and economic growth. It is essential to increase microfinance, provide access to credit for all and grant technical assistance to small and medium enterprises.

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