Geopolitics at the forefront

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- **Oil prices hit 15-year highs this month. The outlook remains bullish, which will catalyse regional economic growth.**
- **Political risks abound across the MENA region. Protests and fractious politics jeopardise stability in both Iraq and Tunisia.**
- **The UAE's image as a safe destination for foreign investment and tourism was marred by two Houthi strikes this month.**
- **Following landmark visits to China by MENA foreign ministers, it is clear that the People's Republic will maintain its neutral stance in a bid to spark significant diplomatic developments.**

UAE: Houthis hit growth

The UAE is set to witness favourable economic conditions this year, with higher oil prices and rising foreign capital inflows driving economic recovery. However, two attacks by the Yemen-based Houthi group may have dampened growth prospects.

- The banking sector is well-equipped to navigate a post-COVID-19 economic recovery.
  - The central bank's Targeted Economic Support Scheme (TESS) is set to continue. It will provide pragmatic relief measures to banks throughout the UAE regarding liquidity measures and capital buffers.
  - The UAE's banking assets are expected to grow between 8-10%, with GDP and non-oil GDP forecast to grow by 4.2% and by 3.9% this year, respectively.
- Non-oil activity is set to drive economic growth, with rising regional economic competition compounded by economic reforms and high vaccination rates.
  - Non-oil sectors are expected to expand by about 4% this year.
  - The latest Purchasing Managers' Index (PMI) outlook forecasts growth developing at a marked pace throughout the fourth quarter.
- Oil prices recovered sharply in 2021, with the sector benefiting from rising production amid easing OPEC curbs.
  - With OPEC production levels expected to continue increasing, and in line with elevated prices, the UAE's projected real oil GDP growth for 2022 is 5%.
  - Nevertheless, oil GDP projections are subject to uncertainties in light of political tensions and the possibility of new COVID-19 variants.
    - Concerns about new variants do not appear to be pressing; the UAE has highly accelerated vaccination and testing programmes.
    - Supply chain concerns were heightened earlier this month following a Houthi attack near the capital Abu Dhabi on 17 January. The incident resulted in Brent crude reaching a high of USD 88 pb, a figure not seen since October 2014.
    - This compares with December's average of USD 74.17 pb.
- The Houthis conducted a further attack against the UAE on 24 January, launching two ballistic missiles over Abu Dhabi. Both projectiles were intercepted.

Table 1: MENA Dashboard[1]

MENA Oil Exporters	Real GDP Growth (%)		Fiscal Balance (% of GDP)	
	2021e	2022f	2021e	2022f
Algeria	3.4	1.9	-13.4	-10.1
Bahrain	2.4	3.1	-8	-8
Iran	2.5	2	-6.5	-7.3
Iraq	3.6	10.5	-1.5	-2.5
KSA	2.8	4.8	-3.1	-1.8
Kuwait	0.9	4.3	-1.5	1
Libya	123.2	5.3	6.8	12.5
Oman	2.5	2.9	-2.6	1.1
Qatar	1.9	4	2.8	5.7
UAE	2.2	3	-0.5	-0.2
Yemen	-2	1	-5.2	-5.2
Average Ex-Libya	**2**	**3.8**	**-4**	**-2.8**

MENA Oil Importers	Real GDP Growth (%)		Fiscal Balance (% of GDP)	
	2021e	2022f	2021e	2022f
Djibouti	5	5.5	-1.7	-1.6
Egypt	3.3	5.2	-7.5	-6
Jordan	2	2.7	-7.7	-5.9
Lebanon	...	...	...	...
Mauritania	2.7	5	-0.7	-1.1
Morocco	5.7	3.1	-6.5	-5.9
Palestine	4.4	6	-10.5	-9.4
Somalia	1.6	3.9	-1.7	-0.2
Sudan	0.9	3.5	-2.9	-1.5
Syria	...	...	...	...
Tunisia	3	3.3	-8.3	-7.6
Average Ex-Syria & Lebanon	**3.2**	**4.2**	**-5.3**	**-4.4**

[1] Arabia Monitor; IMF.

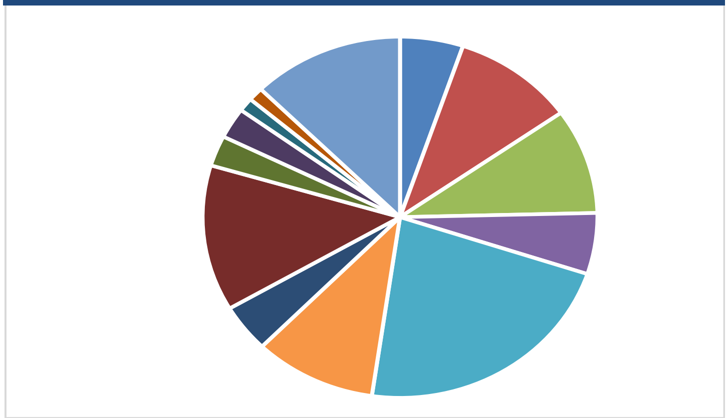
- This latest event is significant. It suggests that last week's attack against an oil facility (where civilians were working) was not intended to be a one-off incident.
  - Air traffic over Abu Dhabi was suspended after both attacks.
  - The Houthis intend to harm the UAE's economy by exacerbating the concerns of foreigners and investors with regard to the emirates' security environment. In light of the number of foreigners in the UAE, as well as Dubai's role as a tourism hub, the latest attacks could be significant.
- The Houthis have vowed to continue using force in response to the UAE's operations in and over Yemen.
- Until now, the Houthis' offensive largely involved drones targeting Saudi Arabia's infrastructure.
  - The UAE will feel the impact of this approach much more accutely than Saudi Arabia. It is a relatively small country and its economy relies heavily on services.
- Last week's attack was the most serious of its kind to take place on Emirati soil.
- Further such attacks could have a significant impact on the UAE's growth. Oil facilities and critical national infrastructure could be seriously damaged in the event of larger and more sophisticated attacks. Tourism is likely to be impacted due to increased security concerns.

Iraq: Sectarianism sustained

Following the first official parliamentary session earlier this month, the formation of Iraq's government is underway. As with most places in the MENA region, the process is set to be fraught and drawn out. Among other complications, the various factions and groups that comprise Iraq's complex political landscape must be considered.

➢ The first parliamentary session was held on 9 January.
- 329 MPs were sworn in, of whom more than 250 are new to the job. There are also 100 women and several independents.
  - Emtidad, a new party born out of the October protest movement, will be vying for representation in parliament.
  - Amid the plethora of new parliamentary personalities, the government's formation could take months.

Figure 1: Parliamentary make-up in Iraq (329 seats) [2]



➢ Negotiations are always necessary, as it is unlikely that one party will ever win a parliamentary majority.
- A power-sharing agreement known as Muhasasa is set to complicate matters even more.
  - Muhasasa has been a fixture in the country's political system following the US occupation. It involves proportional government representation among Iraq's various ethnic and sectarian groups.
- While the party of the Shia cleric Muqtada al-Sadr won the most parliamentary seats, Kurdish and Sunni groups will ultimately dictate the composition of the new government.
  - Mohamed Al-Halbousi, the leader of the Sunni Taqaddum (Progress) Party, was re-elected as speaker of the new parliament.
  - Shakhawan Abdullah, the most popular Kurdish representative, was nominated as deputy speaker.

➢ The issues surrounding the formation of a new government have manifested at street level in the form of demonstrations. Elsewhere, various political groups have used violence in an attempt to exert influence.

➢ Several Sunni and Kurdish groups were attacked across Iraq after the first parliamentary session.
- A hand grenade was thrown into the office of Abdul Karim Abtan Jabouri in Saydiya district (south-western Baghdad). Jabouri represents the Taqaddum Party.
  - Grenades were also thrown at the party's political headquarters in the capital.
- In addition, attacks took place against the office of the Sunni Azim alliance leader, Khamis al-Khanjar.

[2] Arabia Monitor; INA.

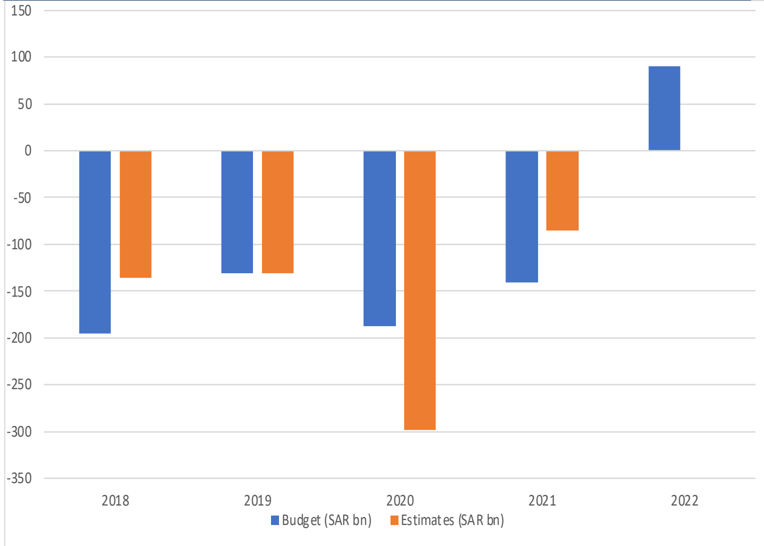
  - A bomb attack on 19 January targeted the office of the Kurdistan Democratic Party (KDP) in Kirkuk.
  - Bombs were also detonated at branches of both Cihan Bank and the Kurdistan International Islamic Bank, both of which are owned by Kurdish businessmen.
- Rocket attacks continue to target the US embassy and the wider Green Zone compound in Baghdad. These attacks show no signs of abating.
  - Iran-backed militias and other affiliated groups have claimed responsibility for similar attacks in the past and are likely to have launched the latest rockets.
    - Although these attacks may not be formally endorsed by Iran's leadership, it is possible that they were carried out or encouraged by the Iran-backed Fatah alliance (the party which lost the most parliamentary seats).
    - Fatah has long disputed the parliamentary election results and will continue to demand more representation.

Saudi Arabia: The Kingdom strikes back

Amid surging oil prices, Saudi Arabia is anticipated to experience a budget surplus in 2022. Furthermore, the Saudi Stock Exchange (Tadawul) has enjoyed a boom due to family-owned businesses going public. Efforts to diversify the economy are ongoing, as evidenced by the latest developments regarding the kingdom's Vision 2030.

- Saudi Arabia posted 5.8% growth in Q3 2021, the fastest quarterly growth rate since 2012. Growth is forecast to continue amid swelling oil prices.
- The kingdom is set to record its first budget surplus in eight years (around USD 24B), which can be attributed to oil revenues, non-oil revenues and reduced government spending.
  - Total revenues for 2022 are set to be 12.4% higher than those in 2021.
  - Tax revenues are expected to amount to around USD 75.5B. Non-tax revenues, which consist of oil profits, returns on government investments and sales of goods and services, are expected to reach around USD 203B.
  - Operating expenses are projected to amount to almost USD 230B, 4.4% lower than 2021.
- The finance ministry expects GDP to grow at a rate of 7.4% in 2022.
  - Although oil continues to be the key growth driver, the kingdom's non-oil GDP grew by 3.9% in 2021.
    - Growth for 2022 is forecast at 3.6%. Nevertheless, the kingdom's performance could exceed expectations if its diversification measures remain on track.
- In addition to this strong economic performance, the Tadawul index has been trending upwards with the benchmark index holding steady at a 15-year high.
  - The All-Share Index is up by around 7% since the start of the year.

Figure 2: Saudi budget vs estimates [3]



  - This is likely due to private sector businesses going public and listing in the capital markets.
    - Although family-owned businesses have long been skeptical about making such a move, the adverse impact of COVID-19 on balance sheets seems to have incentivised businesses to diversify their financing options.
    - Non-family-owned companies in the private sector also have listing ambitions.
- The kingdom's industry and mineral resources minister, Bandar Alkhorayef, announced USD 170B of investments by 2030, in line with Vision 2030 aspirations.
  - The kingdom plans to increase the mining industry's contribution to its GDP by more than 300% (from USD 17B to USD 64B) by 2030.
- The move should provide Saudi Arabia with an opportunity to capitalise on the increasing global demand for minerals and clean energy metals, in line with the worldwide energy transition.

Tunisia: Prolonged protests post power grab

Following President Kais Saied's dismissal of the prime minister and the suspension of parliament in July 2021, political tensions have boiled over in Tunisia. Protests show no signs of abating.

- Soon after his power grab, Saied announced that Tunisia would hold a constitutional referendum in July 2022. He also scheduled a series of consultations to assess constitutional amendments.
  - The potential outcomes of these constitutional amendments include early legislative elections based on a new electoral law, as well as reforms to the penal code.
  - By suspending parliament, Saied has essentially negated the influence the Islamist Ennahda political party. The party was a part of every government coalition since the removal of Zine El Abidine Ben Ali in 2011.
    - Supporters of the Ennahda party, which held the largest number of seats in the now-suspended parliament, believe

[3] Arabia Monitor; Ministry of Finance.

that the president's roadmap will lead to a one-sided electoral system, in which political parties and national organisations are prohibited from taking part. The party will continue to accuse the president and his government of corruption.

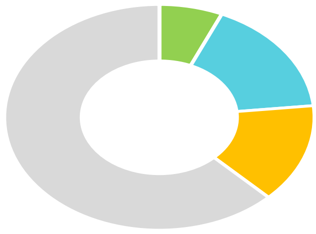
- More than 6.5K protests were recorded during the first ten months of 2021. They mostly took place against socio-economic policies, according to the Tunisian Forum for Economic and Social Rights.
- Demonstrators have regularly taken to the street since the power grab, where they have clashed fiercely with the security forces.
  - The authorities have used tear gas and water cannon against protesters, who often number in the hundreds.
  - Protesters are largely aged between 15 and 20. They continue to demand jobs, better government services and an end to police violence, among other changes.
    - Demonstrators reflect Tunisian society as a whole, as they include members of opposition parties as well as supporters of the president.
- The government recently exacerbated the situation by announcing that it expects to borrow around USD 7B from foreign lenders to stimulate Tunisia's economy.
  - Turning to international lenders such as the IMF could entail painful austerity measures, including a reduction in subsidies on basic goods and decreased wages for thousands of public sector workers. We assess that protests will be a fixture in Tunisia's social fabric for some time to come.

Sino-MENA: Maintaining middle ground

This month, China's foreign minister, Wang Yi, met with his counterparts from Bahrain, Iran, Kuwait, Oman, Saudi Arabia, Turkey, as well as the GCC's general secretary. The meetings mark one of the most significant diplomatic developments involving China and the MENA region in years.

- The meetings took place in Wuxi (Jiangsu province) rather than in the capital Beijing. This is most likely due to strict COVID-19-related restrictions in the capital, which is preparing to host the Winter Olympics.
  - The meetings have consolidated China's relationships with the various MENA countries represented by their foreign ministers.
  - China and the MENA region recognise the need to deepen co-operation. Free trade was a key topic of discussion, and all parties expressed hope that an agreement can be signed quickly.
  - China underscored that regional players must help to facilitate the Joint Comprehensive Plan of Action (JCPOA) negotiations between Iran and the US. China continues to support Iran via purchasing its crude both directly and indirectly (via Oman and Malaysia). However, it also sympathises with regional players who are calling for a seat at the negotiation table to address regional security issues.

Figure 3 -Share of net-zero targets in law, policy, and pledges, from 82 countries[4]



- A closer analysis of the diplomatic event illustrates that China does not group MENA countries under one diplomatic umbrella. Rather it recognises their different economic and political characters and adopts distinct approaches to different players.
- It is worth noting the following developments which emerged from the diplomatic visits:
  - China and Kuwait agreed to intensify efforts to establish a five-year plan based on bilateral co-operation. China also hopes that Bahrain will continue to offer an open business environment; it will encourage Chinese companies to set up in the Gulf kingdom.
  - Oman and China agreed on the need to implement a visa waiver.
  - According to Iran's foreign ministry, a 25-year co-operation agreement which it signed with the People's Republic last year is now ready to be implemented.
  - China underlined the need to understand culture and history with regard to its Uighur population and the Uighur diaspora in Turkey. The two countries also discussed a recent currency swap and security issues. [4]

Stakeholders apply pressure to transition

The 26th UN Climate Change Conference of Parties (COP26) in Scotland marked the transition of the historic COP21 Paris Agreement (2015) from a rule-making event to one with plans for implementation.

- COP26 made progress on specific Paris goals, such as rules for emissions trading and a common timeframe for reviewing Nationally Determined Contributions (NDCs).
  - Negotiations at previous COPs on Article 6 of the Paris Agreement for emissions trading did not reach an agreement on the balance between workable rules and undermining climate ambitions.
- At COP26 negotiators agreed to eliminate double counting, a critical step to making real progress on an effective system of international carbon trading and offsets.
- Meanwhile NDC target dates were aligned around 5-year cycles to spur ambition and action in the near-term, and ensure countries keep pace with Paris' five-year review cycle to strengthen plans.

[4] Qamar Energy; IEA.

- Dialogue around financing and targets for deeper emissions cuts (for 2030 and net-zero 2050) were not as successful, however.
  - Since committing at COP15 in Copenhagen to mobilise USD 100 b annually for developing countries by 2020 through 2025, total climate finance managed to reach only USD 79.6 b in 2019, with developed countries failing to support least developed countries' (LDCs) climate efforts.
  - By the end of the summit, the LDCs' Fund received USD 413 m, while the climate Adaptation Fund received USD 356 m, both woefully insufficient amounts to assist in managing the impact of climate change.
  - Also, many of the new NDCs submitted at the summit fell short of the Paris Agreement's 1.5˚C temperature limit or were unclear or non-specific.
    - For example, Saudi Arabia increased its emissions reduction target two-fold to 278 $MtCO_2e$ annually till 2030 compared to its previous NDC. However, it did not provide a baseline projection to which its emissions' reduction target could be applied.
- External pledges and announcements were the more noteworthy outcomes of the summit, especially with regards to the fossil fuel industry.
  - For example, nearly 200 nations agreed to phase-down unabated coal-fired power plants and most fossil fuel subsidies while pledging to submit more ambitious emissions reduction targets in 2022.
  - The Powering Past Coal Alliance, launched at COP26 and co-chaired by the UK and Canada, saw more than 160 signatories (countries, sub-nationals and businesses) pledge to phase-out coal globally.
  - A group of 31 countries including COP26 partners Italy, Canada, the US, and Denmark together with public finance institutions signed a UK-led joint statement committing to ending international public support for the unabated fossil fuel energy sector by the end of this year.
    - Collectively, this could shift an estimated USD 17.8 b annually in public support out of fossil fuels and into the clean energy transition.
  - 34 countries also signed the Glasgow Accord on Zero Emissions Vehicles, which unites governments, auto manufacturers, and fleet vehicle owners to phase out internal combustion engine (ICE) vehicles by 2035.
  - 109 countries signed up to the Global Methane Pledge, committing to slash methane emissions by 30% by 2030, which could eliminate over 0.2˚C of warming by 2050. These included countries like Saudi Arabia and Brazil, although the absence of China and Russia, some of the world's largest methane emitters, limits potential emissions' savings.
  - Over 140 countries signed the Deforestation Pledge (or the Glasgow Leaders' Declaration on Forests and Land Use) to halt and reverse forest loss and land degradation by 2030, backed by USD 19.2 b in funding.
  - Over 450 financial firms, which control over USD 130 t in assets, also committed to aligning their portfolios to net-zero by 2030, under the Glasgow Financial Alliance for Net Zero (GFANZ). These commitments can deliver an estimated USD 100 t of finance needed to achieve net-zero over the next three decades.
- For fossil fuel producers, these external developments, alongside new rules on NDCs and carbon trading, highlight the extent to which stakeholder pressure is increasing for a low-carbon path.
  - More ambitious NDCs means added pressure on corporates to act, including commitments on indirect Scope 3 emissions reductions. Scope 3 emissions can ultimately only be reduced by selling less product – not an appealing prospect for oil- and gas-producing countries and companies – or by targeting only non-emitting uses of petroleum.
- Offsetting carbon emissions could offer a lifeline to the oil and gas sector.

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