ARABIA MONITOR
ECONOMIC RESEARCH & STRATEGY

The Desert & the Dragon: New synergies, old challenges

Middle East & North Africa Outlook

Q4 2019

Florence Eid-Oakden, Ph.D
info@arabiamonitor.com
Tel: +44 203 239 4518

With Charlene Rahall, Robin Mills,
Roa Ibrahim, Mingqiao Zhao, Ghalia Bajali.

Outline

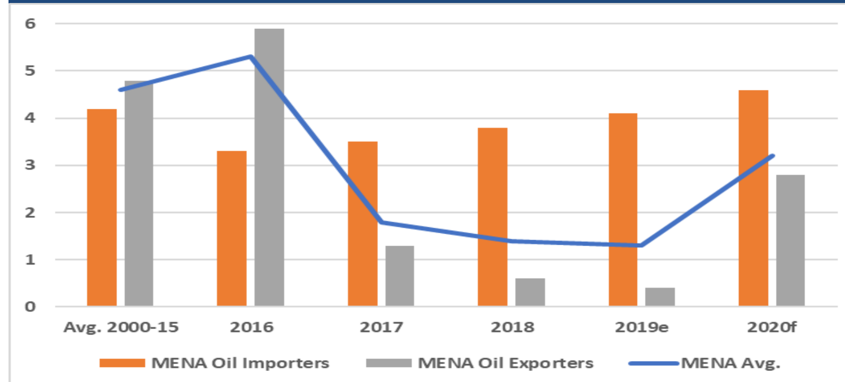
Outline

Outline

Our View: Though still unfamiliar to many, China's Belt & Road reaps benefits

- **Our quarterly regional theme reviews MENA-China relations in light of the Belt & Road Initiative (BRI). We analyse BRI investments in the MENA region since its 2013 inception, and report on the findings of our survey into the familiarity of Arab businesses with BRI and its benefits and challenges. We also evaluate the effect of the yuan devaluation on the region and outline sectors where BRI is bringing diversification beyond oil and construction. Our regional pages also review Sino-Iranian relations in light of recent tensions with the US and the ongoing trade war.**
  - MENA countries have been among the major beneficiaries of China's Belt & Road Initiative, unveiled by President Xi Jinping in 2013 as the Silk Route Economic Belt and the 21st-century Maritime Silk Route.
    - To date, the region has received 14% of the global BRI outlay. The impact will grow as China sharpens its BRI focus and MENA economies redouble their diversification efforts, prompting new synergies.
    - The USD 96B spent on BRI investments and construction projects in MENA from October 2013 has already exceeded non-BRI Chinese spending from January 2005 to September 2013 (USD 93.3B).
  - While China has a long history of interacting and engaging with MENA, our latest survey found that Arab business executives are still not wholly familiar with BRI nor do they view it in the overwhelmingly positive light hoped for by Beijing.
    - While we find this result slightly surprising given the double-digit growth in trade and investment exchanges between China and MENA, we believe it could partly be due to the fact that most projects signed under BRI have been G-to-G (between state-owned companies on both sides) rather than with the local businesses.[1]
    - This may change as Chinese provincial and city governments have started seeking partnerships with local business associations and entities in MENA countries.
  - We view China's recent devaluation of the yuan as two-sided for MENA, but perhaps more negative than positive. We highlight the MENA winners and losers.

Figure 1 – GDP Growth (%)[2]



- **Although growth in MENA will be broadly stable this year, economic activity among oil exporters will moderate, while those powered by domestic demand will strengthen.**
  - Egypt is expected to be a regional outperformer. But despite stronger growth, declining inflation and fiscal account deficits, the private sector remains under pressure and remittances into Egypt and net FDI remain lower than in peak years. We are monitoring political developments carefully.
  - The Saudi Arabian Ministry of Finance is now expecting economic growth to be slower than it had assumed for the year, although it has given no forecasts.
    - In July, the IMF forecast 1.9% growth for 2019, unchanged from its April estimate.
    - But the uncertainty regarding supply disruptions following the attacks on Saudi oil fields -- as well as the global economic slowdown and its potential effect on the oil market -- could soften growth.

[1] Government-to-Government.
[2] Arabia Monitor; IMF.

Global Outlook: Slower growth & lower interest rates

- **Many countries are facing an economic slowdown after a period of steady growth. Global trade volumes are set to decline (partly due to political tensions), perhaps to their lowest level since the financial crisis of 2008. So, here come lower interest rates again.**
  - Overall, the IMF expects global economic activity to slow this year to 3.2% from 2018's estimated 3.6%. It sees world merchandise trade volume growth slowing to 2.5% in 2019, from 3.7% in 2018 and 5.5% in 2017.
  - In the US, economic activity is expected to ease to 2.6% from 2.9% in 2018 but will be higher than the 2.2% in 2017.
    - Trade war uncertainty and slower global growth led the Federal Reserve to cut interest rates by 25 basis points to a target between 1.75% and 2% on 18 September, for only the second time since 2008 (last cut in July). US President Donald Trump is calling for more cuts.
    - Growth was at an annualised 2% in Q2, down from 3.1% in Q1, while the US manufacturing PMI was 49.9 in August. This was below the neutral 50 threshold that signals expansion, for the first time since September 2009.
  - China's GDP is forecast to slow to 6.2% in 2019 (from 6.6% in 2018) as a result of financial regulatory tightening and trade tensions with the US.
    - In its latest attempt to shore up growth, the People's Bank of China on 20 September lowered its loan prime rate by 5 basis points to 4.2%, the second cut in two months.
    - The lower interest rate comes at a welcome time given that the country's Industrial output growth slid to an almost 18-year low in August as the trade war with the US continued to weigh on manufacturers.
  - In the euro zone, the European Central Bank (ECB) cut its growth projection for 2019 to 1.1% and for 2020 to 1.2% from 1.2% and 1.4%, respectively. This prompted the ECB to cut its deposit rate to a record low of -0.5% from -0.4%.
- **Risk appetite could be supported by monetary policy easing, but heightened military tensions in MENA will weigh on investor confidence.**
  - Stepped-up rhetoric between the US and Iran as well as the drone missile attacks on the Saudi oil facilities on 14 September and US deployment of military personnel into Saudi Arabia raise concerns about an outright conflict.

Table 1 – Interest Rate Changes (2019)[1]

Country	Current Rate	Direction	Previous Rate
United States	2.00%	↓	2.25%
Australia	0.75%	↓	1.00%
Chile	2.00%	↓	2.50%
Brazil	5.50%	↓	6.00%
China	4.20%	↓	4.25%
Czech Republic	2.00%	↑	1.75%
India	5.40%	↓	5.75%
Mexico	7.75%	↓	8.00%
Euro Area	-0.50%	↓	-0.40%
Norway	1.50%	↑	1.25%
Russia	7.00%	↓	7.25%
Saudi Arabia	2.50%	↓	2.75%
Turkey	16.50%	↓	19.75%
Qatar	4.50%	↓	4.75%
UAE	2.25%	↓	2.50%
Jordan	4.25%	↓	4.50%

- We believe that current tensions will continue to cause volatility, particularly in oil markets.
  - We estimate the chance of confrontation between the two sides at only 10%, but chance of a settlement through talks between Iran and the US is even lower, at 5%.
  - While there is common support among US Democrats and Republicans for imposing additional sanctions on Iran, support for military options is substantially lower.
  - Any further actions could either constitute carefully limited or covert strikes via proxy activities.

[1] Arabia Monitor; Central banks of respective countries.

Global Energy Outlook: US tariffs open door on MENA oil & gas flows

- **Chinese tariffs, imposed in response to the US trade war, threaten US oil and gas flows to Beijing. Tariffs on LNG rose to 25% in January from 10% in September 2018. A 5% tariff on crude oil was introduced this September.**
  - With the US's trade deficit with China reaching USD 32.8B in July, China will have to target most goods it imports from the US to retaliate fully, so it is likely the crude oil tariff will increase. A 25% tariff on propane was raised to 30% from December 2018.
  - These tariffs have already had an effect. Chinese imports of US crude oil were 190 Kb/d in June, below the 2018 average of 249 Kb/d.
  - MENA crude exporters have avoided gaining a rival. US crude exports to China were never very large, but there was the prospect of substantial gains as overall American exports ramped up. Instead, the gap left by sanctions on Iran has largely been filled by increased shipments from Iraq and Saudi Arabia.
  - Saudi Arabia and Russia have continued to trade places as China's largest supplier, but Iraq is catching up.
- **The impact on LNG has been greater. As its LNG plants start up, the US is on its way to becoming one of the world's top three exporters, alongside Qatar and Australia.**
  - But its companies are now shut out almost entirely from the Chinese market. Exports boomed in early 2018, but fell close to zero from 4Q 2018 onwards. In addition, Chinese companies have mostly cancelled plans to invest in US LNG plants, casting doubt on whether some will go forward.
  - MENA countries and Australia are gaining in LNG market share. Qatar has increased its exports to China, and its planned capacity expansion from 78 Mt/year to 110 Mt/year by 2024 will allow it to raise shipments further.
    - Oman and Egypt are much smaller exporters but also gained market share in 2019.
    - Abu Dhabi, after the expiry of its main sales contracts to Japan in March 2019, also has the chance to turn to the Chinese market.
  - The US will now seek other markets. This could lead to a growing share of US LNG exports coming to MENA, particularly since the UAE and Saudi Arabia (if it starts buying LNG) have barred imports from Qatar.

Figure 1 – China Oil Imports by Country (Kb/d)[1]

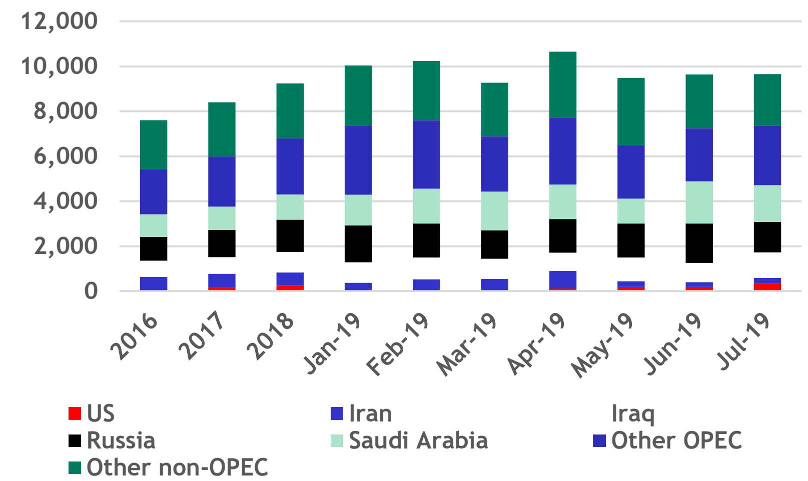
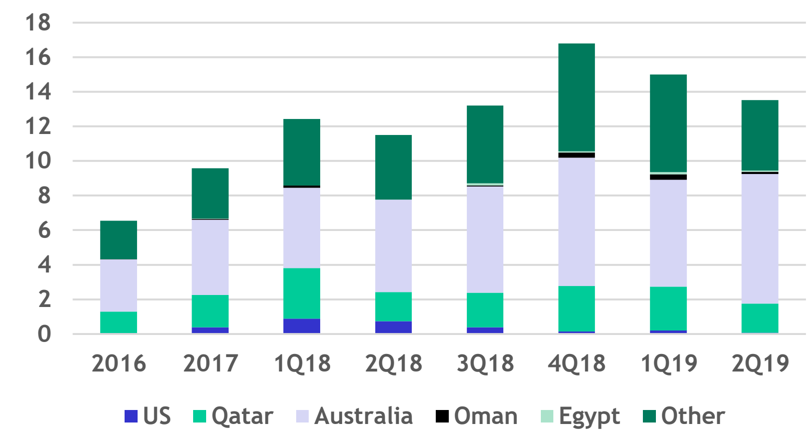


Figure 2 – China LNG Imports by Country (Millions Tonnes)[2]



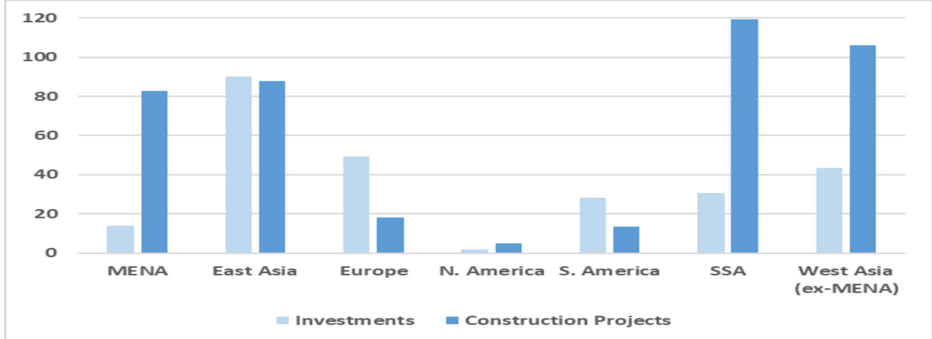
* This page is a guest author contribution courtesy of Robin Mills, Energy Analyst.

[1] Data from China General Administration of Customs
[2] Data from China General Administration of Customs

China's Belt & Road creating wealth & influence in MENA

- **MENA countries have been among the major beneficiaries of China's Belt & Road Initiative (BRI), unveiled in 2013 as the Silk Route Economic Belt and the 21st-century Maritime Silk Route. To date, the region has received 14% of the global BRI outlay. The impact is bound to grow if China sharpens its BRI focus and MENA economies redouble their diversification efforts, prompting new synergies.**
  - BRI is the most far-reaching international initiative that China has ever put forward in modern time. Its five major goals include policy coordination; facilities connectivity; unimpeded trade; financial integration; and people to people bonds.
  - In its current shape, the initiative touching 65 countries seeks to forge closer connectivity between more than half of the world's population, 30% of the global economy with a total infrastructure investment need of around USD 5T.[1]
  - The Chinese government has created specific vehicles to help allocate financing to appropriate projects and initiatives. These include the New Silk Road Fund, the Asian Infrastructure Investment Bank and the steering of large sums of foreign exchange reserves and the resources of several of its largest state-owned banks to the initiatives.
  - BRI is targeted to be "completed" in 2049, the 100th anniversary of the establishment of the People's Republic of China.
- **From October 2013 to June this year, BRI investments and construction projects worth USD 690B had been made by China, accounting for 57% of the value of all transactions by China globally.**
  - MENA's 14% makes it the fourth largest recipient of BRI investments and construction projects after East Asia (26%), sub-Saharan Africa (SSA) and West Asia (22% each) and ahead of Europe (10%), South America (6%) and North America (1%).
  - By country breakdown, the UAE has been the largest recipient with some 24% of the total, followed by Saudi Arabia and Egypt at 17% respectively.
    - Broken down, it is the same order for Chinese construction activity, but in terms of non-construction, Iraq and Jordan take the second and third spots, respectively.

Figure 1 - BRI Investments & Construction Projects in MENA (By Country, % of Total)[2]



- On a sectoral basis, energy has been the largest beneficiary of MENA BRI spending: the sector accounts for about 48% of the total regional funding. At 18.6%, spending on real estate construction is second, followed by transport (17.4%), utilities (5.6%) and chemicals (2%).
  - Within energy, the UAE was the largest recipient of investments (29.2% of the total), followed by Egypt (15.7%) and Iraq (16.4%).
  - The UAE is also the largest recipient of real estate construction transactions (28.4%), followed by Egypt (25.1%) and Saudi Arabia (20.6%).
  - All BRI transactions into transport and utilities in MENA have gone to the UAE with the most spent on the shipping and autos sub-sectors, mainly by China's State Construction Engineering.
  - In the chemicals sector, Saudi Arabia and Jordan are the two main destinations with 58% and 42% of the total, respectively.
- Spending on BRI investments and construction projects in MENA from October 2013 (USD 96B) has already exceeded non-BRI Chinese spending from January 2005 to September 2013 (USD 93.3B).[3]
  - This compares with USD 178B in BRI investments and construction projects into East Asia versus USD 91B in non-BRI Chinese spending.

[1] According to the Global Infrastructure Hub, the MENA infrastructure gap has been estimated at USD 3T over the next two decades, with USD 230B needed for Egypt, USD 115B for Saudi Arabia, USD 37B for Morocco and USD 18B for Jordan.
[2] China Global Investment Tracker (CGIT), The American Enterprise Institute and The Heritage Foundation.
[3] Since October 2013, all investments and construction projects by China in the MENA region have been categorised as BRI-related.

Sino-MENA Survey: Arab views of China's Belt & Road

- **Arabia Monitor has conducted a new survey on how Arab business leaders perceive China's Belt and Road Initiative (BRI). The main finding is that despite its six-year lifespan many respondents remain unaware or only partially aware of the initiative.**
  - The survey of 72 business leaders is the first to gauge Arab views on BRI.
  - It follows on from our 2017 survey of 31 Chinese companies in the UAE and Saudi Arabia, in which we sought to understand their level of optimism about the business environment in the GCC, investment and expansion plans, and their concerns when doing business in both countries.[1]
- **Sixty-seven percent of respondents in this second Arabia Monitor survey were from Egypt, the UAE and Saudi Arabia.**
  - These were the top three countries of interest among Chinese businesses we surveyed in 2017, and not surprisingly are the largest three trade partners of China within the MENA region.
  - About 20% of total respondents were from Morocco, Oman, Jordan, Qatar, Bahrain and Lebanon. Kuwait, Palestine and Sudan had only one respondent each.
  - Respondents were heavily weighted towards the finance, trade, infrastructure and construction sectors.
    - Energy & petrochemical, culture, media & education, technology, telecom, cosmetics, tourism and logistics were also featured, although representation was lower.
- **Some 51.4% of respondents represented local/privately owned, companies, 23.6% were from multinationals, 9.7% from the public sector, and 8.3% in family office businesses.**
  - The rest came from limited partnerships and semi-governmental organisations.
  - Surveying took place in the fourth quarter of 2018.

Figure 1 - Sectoral Distribution of Respondents[2]

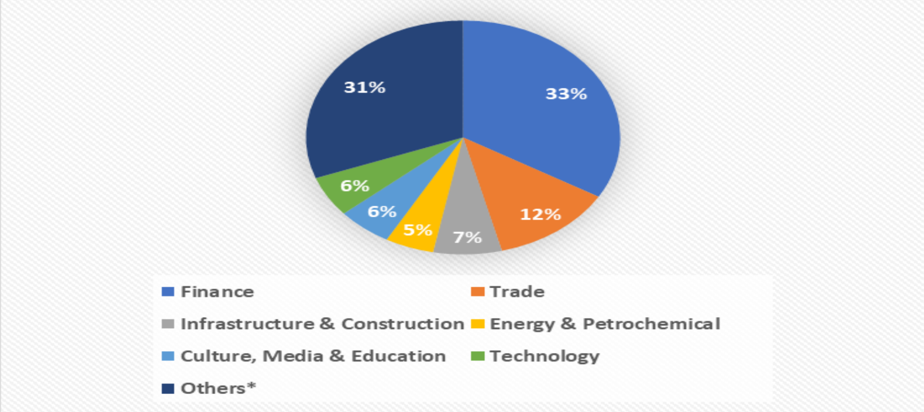
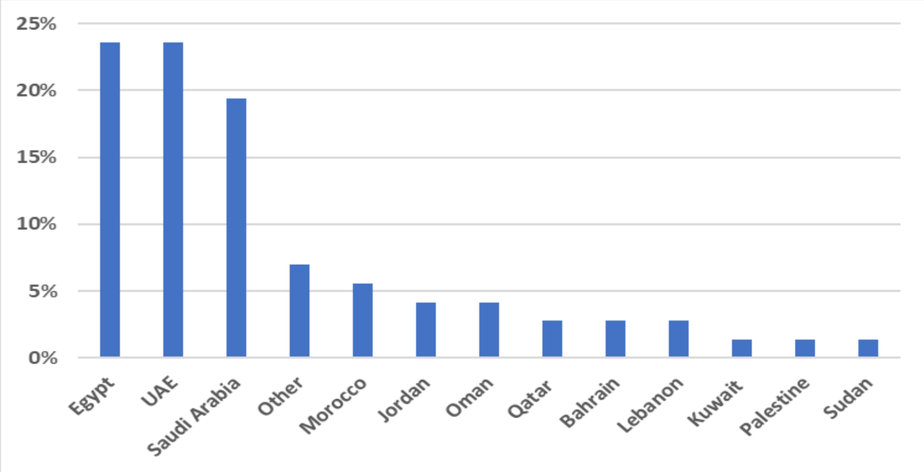


Figure 2 - Geographical Distribution of Respondents[3]



[1] Arabia Monitor. Regional Views Issue #83,"Survey Spotlight: Chinese companies optimistic amidst new risks".
[2] Arabia Monitor. *Others includes telecom, cosmetics, tourism and logistics sectors.
[3] Arabia Monitor.

Sino-MENA Survey: More needed to build BRI awareness

- **While China has a long history of interacting and engaging with MENA, the survey found that Arab business executives are still not wholly familiar with BRI (launched six years ago) nor do they view it in the broadly positive light hoped for by Beijing.**
  - When asked how aware they were about the BRI, only 36.1% of survey respondents said they were familiar with it. Another 27.8% said they were somewhat familiar, but 16.7% said they were not very familiar with it and 19.4% knew nothing at all.
  - Of those familiar with BRI, 69% said BRI is impacting the Arab world "a lot/great deal" while 19% said "a moderate amount". The rest saw "little impact" or "none at all" (Figure 1).
  - While we find this result slightly surprising given the double-digit growth in trade and investment exchanges between China and MENA, we believe it could partly be due to the fact that most projects signed under BRI have been on G-to-G (between state-owned companies on both sides) rather than with the local businesses.[1]
    - This may change as Chinese provincial and city governments have started seeking partnerships with MENA countries -- for example Shenzhen with Bahrain and Jordan, and Ningxia with Oman -- leading to more local-level and private enterprise engagement, particularly in building joint industrial parks and economic zones.
- **Asked if their organisations trade or work with any Chinese entities, 33.3% of respondents said yes, 51.4% no, and 15.3% did not know.**
  - Respondents working in multinationals and the public sector were more likely to work with China and Chinese entities, vs. those working in the smaller private sector or local companies.
  - Asked about integration with BRI, only 6.9% said they already had a formal link and 30.6% said their organisations had had informal discussions. Some 62.5% said they would consider BRI but it was only of passing interest.
  - Part of the response may be down to respondents thinking in terms of BRI as an announced Chinese policy rather than a concrete investment initiative.
  - If China is to improve BRI perceptions, more effort is needed to focus on the benefits of Chinese outward FDI to the Arab world, as well as on differentiating BRI from traditional European and US sources of FDI.

Figure 1 - BRI Impact from Familiar Group of Respondents[2]

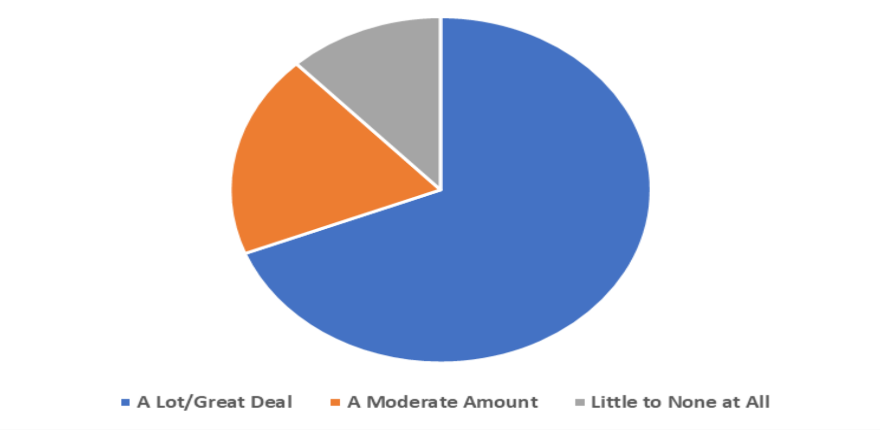
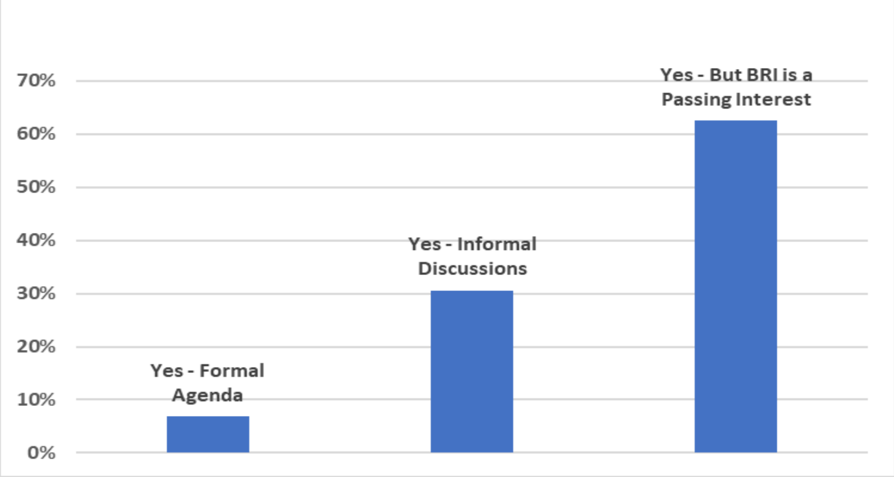


Figure 2 - BRI Integration[2]

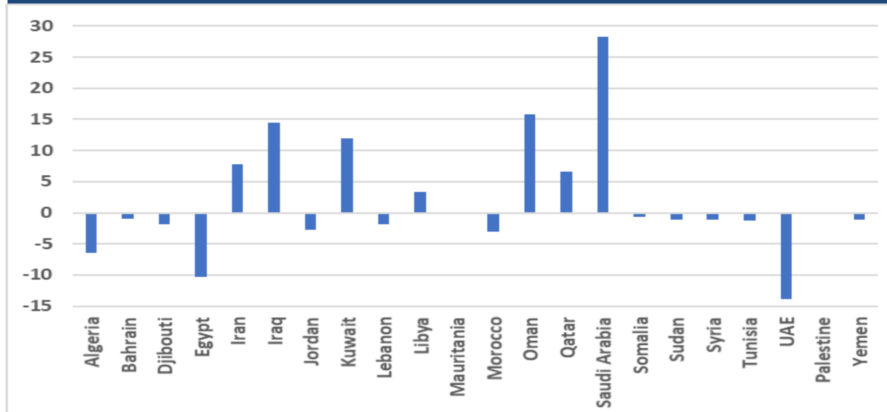


[1] Government-to-Government.
[2] Arabia Monitor; IMF.

Sino-MENA Survey: Business opportunity or political threat?

- **When asked about the most important benefit that BRI can bring to the Arab World, 47.2% said new business opportunities. Bilateral trade, higher Chinese FDI & financing, products and new technology followed. The remainder cited other benefits, including setting up SMEs.**
  - Forty percent of respondents believed that the infrastructure and construction sectors will benefit the most from BRI, followed by technology, trade, finance, culture & education, energy & petrochemicals, agriculture and others.
  - Chinese FDI and financing were not given much weight as an overall BRI benefit, which is surprising given the growing financing trends of Sino-MENA trade and investment relations.
    - Inbound FDI to the Arab world has been instrumental in modern economic development and new business opportunities. China has injected multi-billion-dollar credit lines, loans and investments into MENA that often have multi-decade maturity.
    - Business executives are clearly not aware yet of the strength and recent growth in financing engagement, particularly between Chinese government organisations and banks, and MENA governmental entities.
  - When we compare the responses of business professionals from multinational corporations and from the public sector about BRI benefits, the answers are very similar: business opportunities 44% vs. 47%, respectively; bilateral trade 24% vs. 21%; and FDI 16% vs. 14%.
- **Almost 40% of respondents believe that the biggest challenge that BRI will bring to the Arab world is increased Chinese political influence.**
  - This is followed by trade imbalances and environmental concerns, plus a series of other concerns including legal risks and difficulty maintaining relations with the US and its allies.
  - Political influence is viewed as a challenge most probably because of prior experience with US and European influence in MENA.
    - Much of the region was under colonial control in the 20th century and later, US engagement has often come with political strings.

Figure 1 - China Trade Balance with MENA Countries (USD, B)[1]



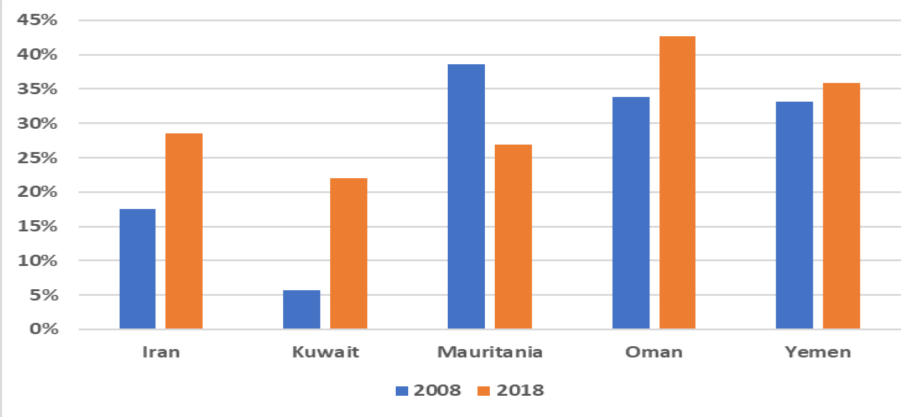
    - It is too early to say whether China will be different and seek influence beyond protecting and extending its economic and security interests, but this is certainly the worry.
    - So far, China's foreign policy has generally emphasised development and economic cooperation.
      - This has led China to carefully manoeuvre the political waters and maintain a neutral, or pro-status quo position in regional affairs, as exemplified recently by exercising its veto power when it came to the UN Security Council resolutions to impose sanctions on Syria.
      - Another example is China's stance on the ongoing Qatar rift. In addition to urging peace and dialogue, China is working with all parties involved to minimise disruption to its trade and investment relationships in the GCC.
  - On the trade imbalance, China is in surplus with MENA oil importers, and in deficit with exporters with the exception of Algeria and the UAE (Figure 1). We do not expect this to change, for now.

[1] Arabia Monitor.

Yuan Devaluation: A double-edged sword for MENA

- **We view China's recent devaluation of the yuan as two-sided for MENA, but perhaps more negative than positive.**
  - The drop in Chinese export prices will lead to a more competitive market for MENA buyers of Chinese goods, including industrial parts. But the cheaper yuan means exports from MENA countries (particularly those with currencies pegged to the USD) will be more expensive to Chinese buyers and we expect a softening of trade as a result.
  - The escalation of the US-China trade war with a new 10% tariff imposed by Washington on an additional USD 300B of Chinese imports pressured China in early August to set the yuan's rate below RMB 7 per dollar, a drop of 1.4% in value to the lowest level since 2008.
    - The People's Bank of China (PBOC) sets a stricter exchange rate on its onshore yuan, fixing the rate within a 2% daily midpoint band to avoid volatility.
    - Offshore trading of the yuan moves more freely, as the currency is traded internationally.
  - History suggests a significant hit to Sino-MENA trade is possible.
    - When China devalued the yuan in 2015, Sino-MENA trade posted a 20% drop to a 10-year low. This was far greater than the 9.5% decline in China's total trade with the world that year.
    - Although 2015 also marked the collapse of global oil prices, which undoubtedly contributed to the drop in total trade.
- **As ever, there will be winners and losers. We highlight the MENA countries in the frontline of the yuan devaluation:**
  - Those that rely most on China as a percentage of their total imports include Djibouti, whose imports from China make up 34% of its total global total, followed by Mauritania (29%), Iran (27%), Iraq (24%) and Somalia, Sudan and Syria with 23% respectively.
  - As most of these countries have struggling economies, the devaluation may be a welcome fillip.

Figure 1 - Exports to China as % of Total Exports to the World[1]



- On the export side, Oman is most vulnerable to Chinese demand, taking up the most out of all MENA countries as a percentage of total exports (43%), followed by Yemen (36%), Iran (29%), Mauritania (27%) and Kuwait (22%).
- For Saudi Arabia, the UAE and Egypt -- among China's key partners with strong bilateral investment and trade agreements -- the yuan depreciation will have much lower impact.
  - This is due to the diversified trade basket the key partners enjoy; the UAE and Egypt's imports from China as a percentage of their total imports outweigh their exports to China -- 13% and 14% respectively.
  - Saudi Arabia's exports to China make up 16% of the kingdom's total (imports are at 15%).
  - But exports reflect a high volume of Saudi crude oil, so it is unlikely that the overall trade balance between the two countries will be significantly impacted unless the yuan devaluation leads to the unlikely effect of lower Chinese demand for oil, significantly.

[1] Arabia Monitor; IMF Direction of Trade Statistics.

Sino-MENA Trade: Back to 2014 levels

- **China's non-oil economic strategy towards MENA is multifaceted and shows obvious continuities from the Hu Jintao administration (2002-2012) to the current Xi Jinping one.**
  - Firstly, its strategy is aimed at facilitating greater inter-regional trade and investment to sustain continued economic growth in China.
    - This strategy is partly accomplished via institutional and commercial platforms for engagement between China and regional blocs.
  - Secondly, it seeks to support the internationalisation of Chinese companies under the umbrella of the so-called "Going Out" policy which was launched in 2000.
    - This policy is geared towards increasing the competitiveness of Chinese companies including state-owned enterprises and showcasing national brands on a global scale.
  - Third, the strategy seeks to attract greater MENA investment into China, and more specifically, into its Muslim regions located in the Northwest which remain relatively undeveloped.
    - This complements Beijing's broader Asia policies, which seek to promote greater infrastructure and logistics linkages regionally.
- **The volume of trade between China and Arab countries amounted to USD 244.3B in 2018, a level it stood at before the oil price drop of 2014 and exceeding our estimate of USD 202B for last year.**
  - Sino-Arab bilateral trade grew from USD 86B in 2007 to USD 250B in 2014, averaging 19% per annum.
  - But since then trade value declined by an average of 17% over 2015-2016 as the oil price dropped. It then picked up 12% in 2017 to USD 191B (our forecast was USD 189B) and jumped 28% YoY by 2018.
  - Taking the recovery growth rate in bilateral trade over 2017-2018, Sino-Arab trade has the potential to reach an all-time peak of USD 350B by 2020. But a slowdown in global growth could limit this increase.
  - Over half of Sino-Arab trade is with GCC countries given the dominance of their energy exports.

Figure 1 – Sino-Arab Bilateral Trade[1]

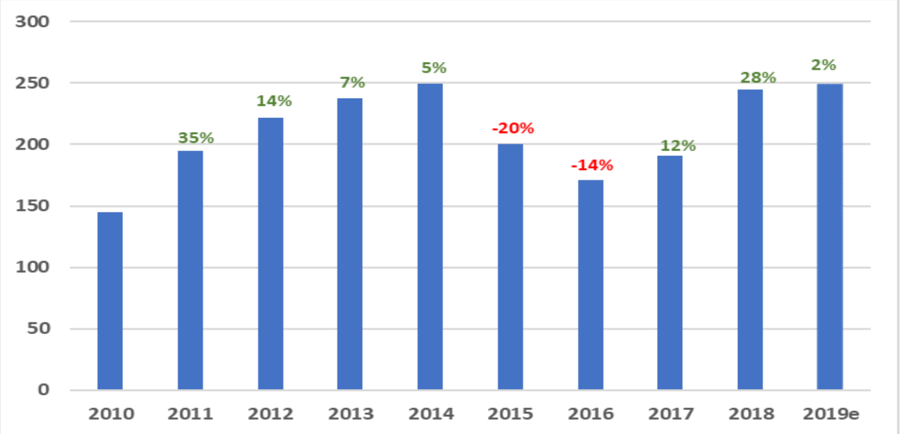
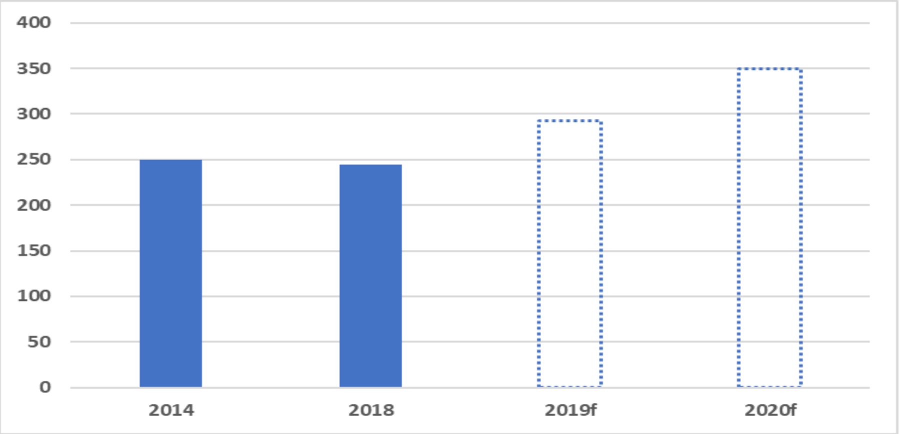


Figure 2 – Sino-Arab Trade Forecast (USD, B)[2]

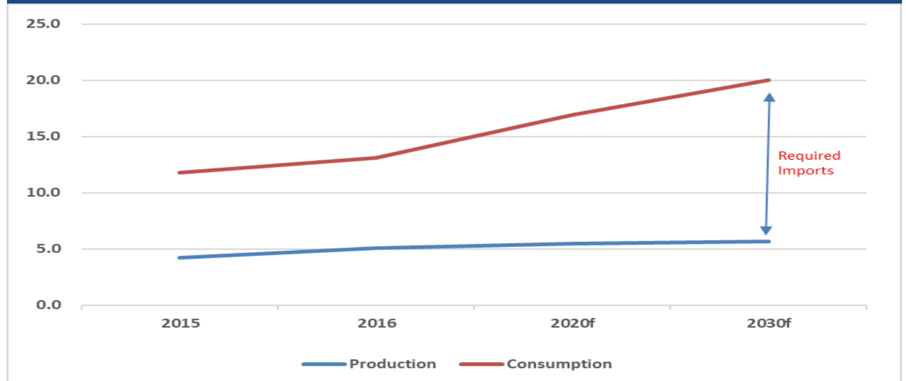


[1] Arabia Monitor; IMF Direction of Trade Statistics.
[2] Arabia Monitor; IMF Direction of Trade Statistics. Forecasts are based on average annual growth rate of 20%.

Sino-MENA: Energy is at the heart of relations

- **China remains the number one crude oil importer in the world after surpassing the United States in 2017.**
  - ➢ China's crude oil imports as a ratio of total demand rose from 30% in 2000 to 72% by 2018.
    - Oil demand is driven by a confluence of factors including domestic economic growth and trade, transportation sector shifts, refining capabilities, and inventory builds.
  - ➢ Crude oil imports rose 10.1% YoY in 2018 to a record 9.24 Mb/d.
    - New refinery capacity and strategic inventory stockpiling, combined with declining domestic oil production, are the major factors contributing to the recent increase in China's crude oil imports.
    - Together, five of China's leading crude petroleum suppliers (Russia, Saudi Arabia, Angola, Iraq plus Oman) represented over half (55.2%) of overall Chinese crude oil imports for 2018.
      - This mainly resulted from an increase in Russian ESPO pipeline blend crude exports and from Saudi Arabia's commitments to OPEC cuts.
      - Chinese imports of Russian oil made up 16% of China's total imported crude in 2018.
    - But YTD, China has increased its imports of Saudi Arabian oil, and in March 2019, these reached 1.7 Mb/d, the highest level for any month since at least 2004. Latest data for July shows imports from Saudi Arabia were 1.65 Mb/d versus 1.34 Mb/d from Russia.
      - Saudi Arabian crude oil exports to China increased recently, in part, because of the start-up of a new 0.4 million b/d refinery in Dalian, Liaoning Province, which has a supply agreement with Saudi Aramco.
      - Aramco has also been in talks with Hengli and Zhengjiang Shihua since 2015 and began its supply from May 2019, pushing up its crude export levels to China.
- **To manage its oil dependence, China has already been diversifying the sources of its crude imports from both within and beyond the MENA region. But we expect MENA to remain a top choice for China in the short-to-medium term at a time when Chinese demand is growing.**
  - ➢ One major factor is that Beijing has been actively substituting coal with oil and gas as part of its environmentally friendly drive to cap coal use to 62% of total energy consumption by 2020.
  - ➢ In addition, Chinese refineries' preferences for the GCC's medium-to-heavy grade to which their production lines are geared will mean China's demand for Saudi oil is expected to remain relatively inelastic for some time to come.
    - Saudi Arabia was the largest MENA oil exporter to China, accounting for 12.4% of the country's oil imports in 2018, but lower compared with 19% in 2013, as Saudi Arabia lost the top oil supplier position to Russia from 2016 to 2018.

Figure 1 – Oil Production & Consumption (Mb/d)[1]



[1] Arabia Monitor; EIA.

Sino-MENA: The road toward diversification

- **Sino-MENA relations are extending beyond traditional sectors to investments by China into industrial zones, as well as investments by MENA countries in China. A recent example is the USD 10B investment by China's East Hope Group in the UAE's Khalifa Industrial Zone Abu Dhabi (Kizad) in three phases over 15 years.[1]**
  - An aluminium facility is planned in phase one, while a bauxite research centre and recycling project will be part of phase two. The third and final phase is to bring large upstream and downstream facilities together for the processing of non-ferrous metals.
  - More than 15 Chinese companies have invested in Kizad, including COSCO Shipping, which opened a terminal last year at Khalifa Port, just north of Abu Dhabi city and around 100 km from Dubai.
  - Prior to East Hope Group's foray, other privately-owned Chinese conglomerates have been exploring opportunities in MENA, but some mega projects have not materialised.
    - This includes Haite Group's USD 1B plan to build a manufacturing and technology hub (Mohammed VI Tangier Tech City) in Morocco in partnership with BMCE Bank.
    - Haite withdrew from the scheme last year, reportedly over problems with its scale and a dispute over who would own the completed city.
  - We believe the new Kizad venture is more likely to succeed, primarily because:
    - Abu Dhabi and North Africa offer different policy, economic and market conditions to investors.
    - The nature of business is also different. While East Hope Group focuses on heavy industries, Haite and CFLD were building an industrial park and a new city, respectively, which require detailed coordinating efforts.
- **In addition to Chinese investments going to MENA, we are observing increasing MENA initiatives in China.**
  - In June, Dubai-based global developer Emaar signed an MoU with Beijing New Aeropolis Holdings.

Figure 1 - MENA Businesses Pivot East[2]

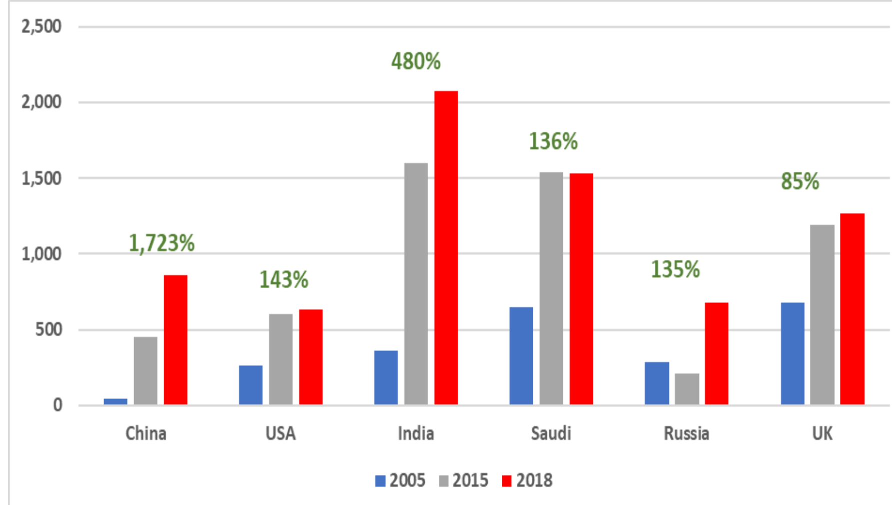
    - The plan is to jointly develop a business and tourism complex, integrating retail, entertainment, office, hotel hospitality, and lifestyle functions within the Aero-Economic Area of Beijing Daxing International Airport, which is set to become the largest in the world.
  - In February, Saudi Aramco agreed to form a joint venture worth about USD 10B with Chinese defence conglomerate Norinco to develop a refining and petrochemical complex in the northeastern Chinese city of Panjin.
    - Aramco also signed an agreement to buy a 9% share in Zhejiang Petrochemical. The partners will form a new company called Huajin Aramco Petrochemical Co as part of a project that will include a 300 Kb/d refinery with annual production of 1.5 million metric tonnes of ethylene cracker.

[1] East Hope is a Shanghai-based manufacturing giant, privately-owned by Yongxing Liu, one of China's richest men. It has diversified business portfolios.
[2] Arabia Monitor.

Sino-MENA: Tourism is a key pillar of BRI-led growth

- **Sino-MENA relations span myriad strategic partnerships, including tourism, which is now not only an economic link but a key sector for strengthening bilateral ties. We analyse the impact on two key markets -- the UAE and Morocco -- as case studies for others in the region.[1]**
  - ➢ A policy to do away with visas (also put forward by several other MENA countries) as part of their response to BRI, has served the overall tourism sector well.
  - ➢ Latest official data from Dubai ranks China fourth after India, Saudi Arabia and the United Kingdom in terms of the numbers of arrivals.
    - In the first half of this year, 501,000 Chinese nationals entered Dubai, an 11% growth over the same period in 2018.
      - For comparison, this was around half of the arrivals from India (997,000), but close to those from the UK (586,000) which has been one of the mainstays of Dubai tourism.
    - The number of Chinese tourists to Dubai has risen by around 80% overall since the visa-free policy was implemented in 2016, making for an annual average increase of 26%.
    - There is an opportunity to scale up, given both the potential numbers of Chinese visitors (149.7 million globally in 2018, up from just 10.5 million in 2000) and the low base from which the UAE can build (Figure 1).
  - ➢ The visa relaxation policy also has become a key driver for the UAE's economic diversification, encouraging China to adopt similar measures.
    - Since January 2018, UAE nationals holding regular passports have been exempted from pre-entry visas to China, allowing for a stay up to 30 days.
    - As a result, we expect the number of UAE visitors to China to rise beyond the annual 10,000 level at which it now stands. Again, this scale-up will in part come from a low base.

Figure 1 - Dubai Tourist Arrivals by Nationality (Thousands; Growth 2018/2005)[2]



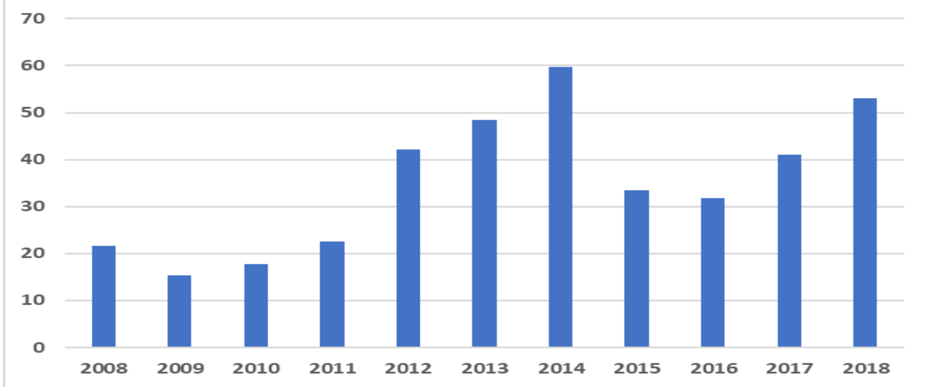
- **Growing links between both countries and rising tourism have led the UAE to promote the teaching of the Chinese language.**
  - ➢ The initiative, proposed by Abu Dhabi's Crown Prince Mohammed bin Zayed Al Nahyan, aims to set up Chinese teaching classes in 100 UAE schools.
  - ➢ Progress is underway, with 20 out of the 150 required Chinese teachers already recruited into 11 schools YTD.
  - ➢ While growth is usually driven by sustained economic diversification plans and heavy infrastructure projects, ongoing efforts to introduce Chinese culture into the UAE will increase the number of UAE nationals and residents capable of deepening sources of growth from Chinese trade and investment. The geostrategic positive externalities are equally valuable.

[1] Sino-Morocco tourism on page 21.
[1] Arabia Monitor; China Customs Statistics.

Sino-UAE: Leveraging advanced logistics capabilities

- **China's role as the UAE's largest trading partner is deepening. It recently invested USD 3.4B into shipping and food investments in Dubai as part of BRI.**
  - The two UAE deals, signed during the second Beijing BRI Forum in April 2019, amounted to 5.3% of the total deals China agreed with BRI countries.
  - A USD 2.4B deal was signed between China's Ningbo Port, the world's busiest in terms of cargo tonnage, and the UAE's DP World, to build a "Traders Market", a 5.5 million square metre logistics station to store and ship Chinese exports to the rest of the world from Dubai's Jebel Ali port.
    - Dubai already hosts the world's largest Chinese product market outside China at Dragon Mart at International City, home to more than 4,000 Chinese SMEs.
    - The UAE allows duty free imports of raw materials to manufacture, giving it a distinct advantage over other GCC countries, to become a regional food and beverages hub for imports, exports and re-exports.
      - It is the largest re-exporter of food products, including coffee, to other GCC countries, East Africa, India, Pakistan and Russia.
  - A second deal was signed for a USD 1B investment to build a "Vegetable Basket" food manufacturing and processing plant in Dubai.
    - The deal -- which involves China-Arab Investment Fund Management, Winland Investment Holding, China Co-op Group and Ocean Economic Development -- is aimed at importing, processing and exporting fishery, agricultural and livestock products.
    - It will allow the UAE to leverage its strategic geographical location, making Dubai a key link in the BRI supply chain and allowing the emirate to strengthen even further its position as a regional and global trade hub.

Figure 1 - Sino-UAE Trade (USD, B)[1]



- **We see plenty of room for growth. For instance, agricultural exports from China to the UAE make up 15.5% of total exports to the Middle East yet only 0.1% of China's total global exports, 1.8% of total Chinese exports to BRI countries and 1.7% of the UAE's total imports of such products.**
  - Agricultural exports from China to the UAE have grown by 1% annually since 2012 to reach USD 461M in 2018. They stood at USD 390M in the first five months of 2019.
  - The UAE is also considered a gateway for about 60% of China's exports to regional markets, at an annual volume of exchange worth USD 70B including re-exports. Sino-UAE bilateral trade stood at USD 53B in 2018.
    - Trade with Dubai accounts for over 80% of total Sino-UAE trade; the emirate handles 60% of China's exports throughout the MENA region.
    - The UAE itself is expecting to see UAE-China bilateral trade grow to reach USD 106B within the next three years, with growth driven by food, energy and technology sectors.

[1] Arabia Monitor; China Customs Statistics.

Sino-UAE: New technology boosts transport & logistics

- **Chinese investments are also flowing into the UAE's growing autonomous transport sector. Chinese Tech company Neolix has partnered with Noon, a Middle East e-business owned by Saudi Arabia's Sovereign Public Investment Fund and Dubai businessman Mohamed Alabbar, to trial the first autonomous delivery vehicles.**
  - The UAE, in line with its 2030 Dubai Smart City project, launched the Dubai Autonomous Transportation Strategy, which is aiming to make a quarter of all transportation trips in Dubai smart and driverless.
    - This is forecast to generate annual revenue of USD 6B from lower transportation costs and carbon emission reductions by 2030.
    - The main sectors identified for the application of the strategy are metro trains, buses and taxis.
  - To meet its goal, the UAE is also setting up tests on the roads of Dubai. In April, UAE sports car developers W Motors, in partnership with Iconiq Motors, unveiled their first autonomous vehicle, Muse, at Auto Shanghai. The company plans for this vehicle to be fully operating on designated roads during Dubai 2020 Expo.
  - New technologies should play a significant role in shaping the future of the automobile industry in the region.
    - The UAE has been embracing artificial intelligence (AI) and new digital developments. Businesses have been investing heavily in new technologies, supported by the government as an early consumer of the technology.
    - AI is already playing a significant role in the transport system in Dubai. The Dubai Metro for instance is the world's longest driverless train network driven by AI.
  - Following the announcement of new regulations for autonomous vehicle testing in April, Noon and Neolix signed a preliminary agreement for the latter to customise delivery vans, with last-mile delivery trials commencing in Dubai and Abu Dhabi in the next few weeks. The partnership plans to reduce 90% of associated delivery costs, while improving e-commerce efficiency.

Table 1 - % of Total Trips by Self-Driving Transport[1]

	2016	2030
Metro	8.8%	12.2%
Tram	0.0%	0.2%
Shuttle & Cable-cars	0.0%	2.5%
Marine Transport	0.0%	2.0%
Taxi/Rideshare	0.0%	3.5%
BRT, Rider & Runner	0.0%	6.4%

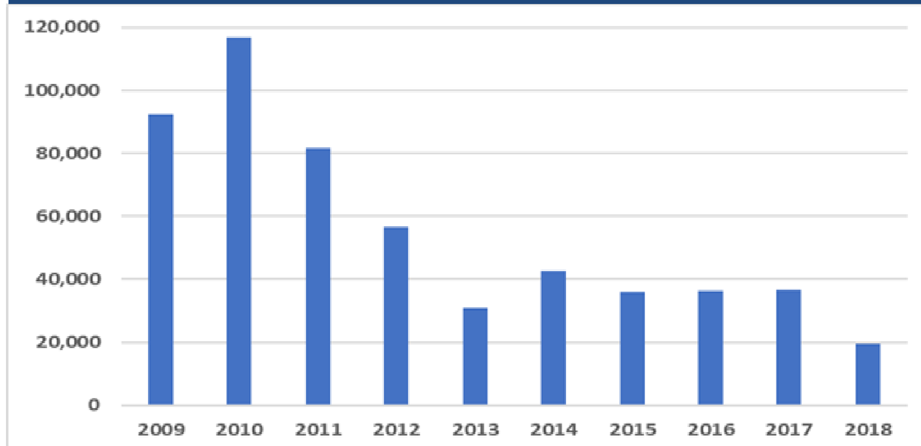
- **The Middle East has seen a boom in e-commerce -- especially in the UAE -- over the past few years, with China playing an important role in furthering the growth of the industry.**
  - The UAE is the largest e-commerce market in MENA, with USD 6.2B in business-to-consumer turnover (22% of the MENA total), followed by Saudi Arabia and Egypt with USD 6B (21%) and USD 5B (17.5%), respectively.
  - The Neolix deal was not the first signed within this sector.
    - Last year, SkyCargo, the freight arm of UAE flagship carrier Emirates Airlines, signed an MoU with China's e-commerce giant Alibaba Group's logistics arm, Cainiao Smart Logistics Network Ltd, to work together on cross-border logistics.
    - The deal aims to support Cainiao's broader business efforts. It has recently unveiled plans to develop six global hubs in six cities worldwide including Dubai.
    - SkyCargo and Cainiao will manage e-commerce shipments in the Middle East and to neighbouring regions via Dubai. This is expected to pose challenges to established players in the logistics and transport segments.

[1] Arabia Monitor; The Roads and Transport Authority, UAE.

Sino-Egypt: Private sector active on the road

- **Construction, infrastructure and transport are the major pillars of the China-Egypt economic relationship in light of BRI. We believe Egypt follows the UAE closely in its attractiveness to a large number of private sector players and investors.**
  - China's automaker Foton Motor signed an agreement in March with Egypt's Ministry of Military Production and Ministry of Local Development to jointly manufacture electric public buses.
    - The joint venture entails manufacturing 2,000 electric buses over four years, with 45% of components coming from domestic Egyptian manufacturing.
    - The goal is to boost the electric vehicle industry and localise and improve public transportation.
    - Following a Chinese delegation visit in June to production plants owned by the Egyptian military, Foton Motors agreed to deliver the first 48 buses in December 2019.
      - For testing purposes, Foton Motor has already delivered a 180-seater electric bus.
  - Sino-Egyptian deals are also focused on launching electric cars by Q1 2020 for an investment of USD 120M.
    - Brilliance Auto, a Chinese auto-manufacturer, will assemble its vehicles in Egypt, and start manufacturing on a BMW assembly line (with which it has a joint venture) until its new plant is complete.
    - The target output for the first year is 10,000 vehicles.
    - The Brilliance Auto deal follows the Egyptian-European Partnership Agreement, which removed customs duties on European and Turkish cars.
      - This, in turn, lowered imported car prices significantly, disrupting the market and pushing Asian and US automakers to also cut prices.
- **Chinese investments and the shift to localising auto-manufacturing in Egypt should revitalise the industry and reduce prices.**

Figure 1 - Vehicle Production in Egypt (Thousand Units)[1]



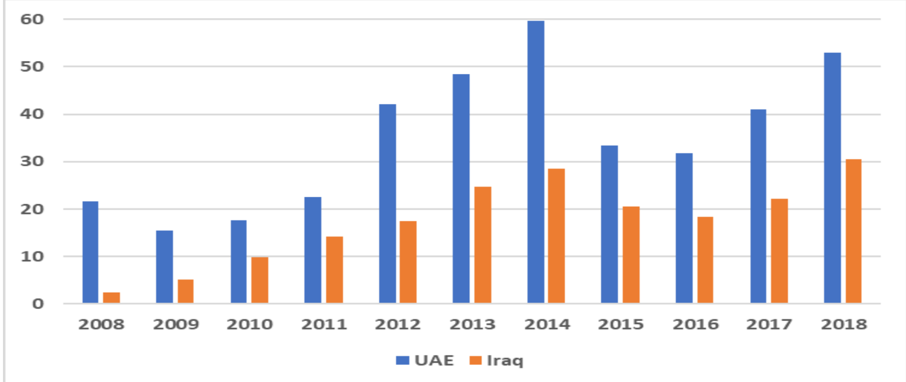
- So, there are opportunities for scaling up, as demand for vehicles far exceeds production.
  - The auto sector in Egypt is valued at USD 13B (3.5% of GDP) with vehicle imports accounting for about 5% of Egypt's total imports.
  - Exports of auto goods only account for 0.5% of Egypt's total exports.
- Data from the International Organization of Motor Vehicle Manufacturers show that Egypt produced only 19,500 vehicles in 2018 versus 36,000 in 2017 and compared with a peak of 116,683 in 2010.
  - The Ministry of Trade and Industry (MTI) wants to boost local production annually to 500,000 units by 2022 to match the number of vehicles imported, and business with China will help achieve this.
  - The BRI emphasis on electric cars means MTI goals can potentially be met despite the stricter environmental regulations implemented by the Ministry of Environment on air pollution.

[1] Arabia Monitor; The Roads and Transport Authority, UAE.

MENA banks branch out in China, driving trade relations

- **The MENA banking sector is pivoting east, accompanying the overall shift in economic geography. A presence in China provides corporate banking services to MENA companies and trade finance to Sino-MENA counterparties. Traditionally, MENA banks have operated out of Singapore for their Asia-Pacific markets.**
  - Iraq is the latest to join the expansion and we expect others to follow. Recent links between Iraq and China are related to developing projects under BRI. To promote this, government-owned Trade Bank of Iraq (TBI) is expending beyond its current GCC range to open a representative office in China next year.
  - TBI, founded in 2003, is one of Iraq's largest financial institutions. It funds about 80% of Iraq's trade finances, with assets in 2018 of around USD 30B, 8% higher than in 2017.
  - In April this year, TBI opened its first branch in Riyadh focused on trade finance, with full operations to begin in September. The bank is also in the process of upgrading its representative office in Abu Dhabi to an asset management company.
  - TBI Chairman Faisal Al Haimus forecasts the expansions to raise revenue from the bank's retail and international banking sector to 30% of total revenue, from the current 25%, by 2022.
  - In February, Iraq and China signed an agreement including establishing a committee for BRI projects with investments totalling around USD 10B. The deal involves China working on the reconstruction of Iraq's economy, while also focusing on energy and infrastructure projects.
    - Iraq and China had been in discussions to build a 300 Kb/d refinery and petrochemical complex in Fao, southern Iraq, which could well cover the USD 10B mentioned in the February agreement.
  - Bilateral trade rose 10% YoY to stand at USD 30B in 2018. Chinese imports of Iraqi crude oil made up 67% of this (24% of Iraq's overall exports), while the rest were Iraqi imports of Chinese products (24.3% of Iraq's overall imports), mainly including machinery and electronic equipment.

Figure 1 - China Trade with UAE & Iraq (USD, B)[1]



- **China-UAE relations are on the rise with banking ties involved in a large share of bilateral transactions. China's four largest banks in terms of total assets signed a new partnership agreement with the UAE's export credit agency, Etihad Credit Insurance (ECI) in July.**
  - ECI and SINOSURE will cooperate in shari'a-compliant investments in insurance, commercial information and trade promotion, while, Industrial and Commercial Bank of China (ICBC), Bank of China (BOC) and the Agricultural Bank of China (ABC) will cover trade credit insurance and export financing in conventional and shari'a-compliant murabahah banking.
  - These partnerships are set to strengthen non-oil investments between both countries, while also advancing ECI's market presence by making it the first export credit agency to partner with major Chinese state-owned financial institutions.
  - Bilateral trade stood at USD 53B in 2018, with plans to expand to USD 70B by 2020.
    - Opening a mutually beneficial source of services through the banking sector is a promising step to achieve such a trade target.

[1] Arabia Monitor; IMF Direction of Trade Statistics.

Sino-Oman: From fishing town to Asian industrial hub

- **Duqm Industrial Park on Oman's central coast, plays a significant role in strengthening economic cooperation and expanding production capacity between the two countries, and is transforming Duqm from a fishing settlement to a new non-oil industrial hub.**
  - The partnership was launched in 2015, with construction of the Wanfang Residential and Commercial complex beginning in April 2018.
    - The complex will have a total area of 40,000 square metres, comprising commercial buildings.
    - The first phase, which spans 15,000 square metres, is set to be completed in 2022.
  - Total investment by Oman Wanfang, a subsidiary of Wanfang LLC from Ningxia region, is forecast to reach USD 10.7B spread across power generation, chemical production, seawater desalination and vehicle assembling.
- **Other Chinese investments are smaller, but nonetheless significant and also focused along Oman's eastward-facing Arabian Sea coastline.**
  - A 1,000 MW solar power plant in Duqm signed in 2017 between Oman Investment Fund (OIF) and Ningxia Zhongke Jiaye New Energy is under construction, and is set to be completed by year-end. The Chinese firm holds a 51% stake in the USD 94M investment, with the remaining held by OIF.
  - Duqm Hongtong Pipes Company, a Chinese-Omani partnership, is building a polyethylene pipe factory to meet demand in the oil and gas industry for non-metal pipes.
    - The partnership is owned by Duqm Hongtong Pipes Company (51%), with shares owned by Blue Ocean International (44%) and Omani shareholder Daoud Alfarsi (5%).
    - Located south of Muscat in the Special Economic Zone of Duqm, construction began in August and will be completed in around 10-12 months with the first batch of pipes to be produced in Q2 of 2020.
    - Initially, production will be used to serve the local Omani market to meet demand for non-metallic pipes for the transfer of hydrocarbon fluids in the oil and gas industry. It will then be used to supply regional and international markets.

Table 1 - Chinese Projects in Duqm[1]

Project	Chinese Entity	Investment (USD)
Methanol	Dalian Mingyuan Holdings Group Company Ltd.	2.8B
Power Plant	Hebei Electric Power Kance Design & Research Institute	425M
The Industrial Park	Oman Wanfang	138M
Solar Panel	Ningxia Zhongke	94M
Desalination and Bromine Plant	Ningxia Water Investment Group	89M
SUV Manufacturing Plant	Wuhan Xiaolong Automotive Technology Co	84M
Distribution Facility for Building Materials	Ningxia Ningqiao Commercial Investment and Operation Ltd	46M
Polymer Manufacturing Plant	ZL EOR Chemicals Oman	20M
Polyethylene Pipe Factory	Duqm Hongtong Pipes Company	6M

  - Petroleum Development Oman and ZL EOR Chemicals Oman, China ZL EOR Chemicals, have recently set up a USD 20M polymer manufacturing plant in Salalah.
    - The manufacturing unit, the first in the GCC, is set to begin operations before the end of Q3 2019 and will initially produce over 13,600 tonnes of polymers annually.
- **However, while Chinese and Omani entities have been particularly active in forming joint ventures in the past few years, the two countries are yet to benefit materially from this mutually important growing relationship.**
  - Most Chinese entities entering the Omani market are at sub-state level, with limited experience in dealing with international players.
  - Until the Chinese players have fully adapted to the specification of Omani business conditions, it could be a few more years before these high potential projects yield fruits.

[1] Arabia Monitor.

Sino-Morocco: Renewables, manufacturing & FTZs

- **China is carving a deeper presence in Morocco, as the kingdom's geostrategic positioning is increasing the interest of investors and now generating economic cooperation opportunities. The big focus is on Morocco's infrastructure and renewable energy industry.**
  - The Moroccan government plans to meet 42% of its energy requirements using renewable resources (4.6 GW solar, 4.2 GW wind and 1.3 GW hydro) by 2022 and 52% by 2030. The kingdom has the highest renewable energy target among North African countries.
    - It is currently investing more than USD 13B in developing its renewables capacity, and short-term ambitions are for solar and wind to provide 28% of power capacity by next year.
    - Morocco's potential in wind energy is largely untapped; 10% of electricity produced is generated through wind power while wind energy potential in the country is estimated at 25,000 MW.
  - Platinum Power, a Moroccan energy operator has partnered with China Communications Construction Company (CCCC) subsidiary, China First Highway Engineering Company, to build and finance renewable energy projects across Africa.
    - Plans are to begin with a 108 MW hydropower plant worth USD 300M in central Morocco.
    - Platinum will also develop a 365 MW plant in Cameroon and several plants amounting to 300 MW in Côte d'Ivoire.
  - Morocco imports more than 90% of its energy resources, the largest energy importer in MENA, comprising up to 12% of its GDP.
    - This project will allow Morocco to meet its renewable energy goals of exceeding a 53% share in its energy mix by 2030 and reduce its reliance on fossil fuels.
- **CCCC's presence in Morocco extends to projects in manufacturing and technology. Following the withdrawal of the former Chinese sponsors of Mohammed VI Tangier Tech City, Haite Group, CCCC became the major player.**

Table 1 - North Africa Renewable Energy Targets (% of Total)[1]

Country	By 2022	By 2030
Algeria	6%	40%
Egypt	20%	N/A
Libya	7%	10%
Morocco	42%	N/A
Tunisia	N/A	30%

- The original financier, Haite Group, an aviation company in China, left a joint venture with BMCE that was to have invested USD 1B in the project.
  - Haite withdrew last year, reportedly over problems with the project's scale and a dispute over who would own the completed Tech City.
- If all proceeds as planned, Tangier Tech City will be the second economic zone in MENA to be partly funded by Chinese investors, with the first being the China-Egypt TEDA Suez Economic and Trade Cooperation Zone.
  - An important achievement and a successful example of such cooperation between China and Egypt was the Jushi Egyptian fibreglass production base.
  - It is the world's largest fibreglass production base outside China, making Egypt the world's fifth largest fibreglass producer.

[1] Arabia Monitor; International Renewable Energy Agency.

Sino-Morocco: Visa exemption triggers Chinese tourism boom

- **In pursuit of stronger economic ties with China, Morocco exempted Chinese citizens from visa-entry requirements in June 2016, allowing them to stay for up to 90 days. Following the decision, Morocco witnessed a massive influx of Chinese tourists to the kingdom. Other MENA countries seeking a China tourism boost should take note.**
  - Arrivals from China increased 75% over three years. They hit 43,000 the year the visa was lifted, followed by 127,000 and 180,000 in 2017 and 2018, respectively. By contrast, arrivals from China were only 10,000 in 2015, the year before the exemption.
  - Tourism is the second largest contributor to Morocco's GDP, accounting for 11% while also employing 5% of the workforce.
    - According to Morocco's Tourism Observatory, more than 12 million tourists visited Morocco, in 2018, an 8.3% increase over 2017.
    - The surge appears to be continuing this year. Some 3.6 million tourists arrived in the first six months of 2019, an increase of 6% from the same period in 2018.
  - Morocco's strongest inbound travel market remains France, representing over 17% of 2018 total arrivals, followed by the United States (14%), Italy (12%) and Spain (7%).
    - Despite the increase, Chinese tourists still only made up about 1.5% of international visitors to Morocco in 2018, underpinning significant potential for Morocco to attract more.
    - A direct flight connecting Morocco and China -- set to begin between end-2019 and Q1 2020 -- is expected to boost this trend. The flights will link either Morocco's economic hub Casablanca or its tourist hotspot Marrakech with either Beijing or Shanghai.
    - In the meantime, Morocco has established partnerships with key international airlines to improve connectivity from China, by code-sharing flights with Etihad Airways, Turkish Airways and Air France.
- **Part of Morocco's Vision 2020 and economic diversification plans are to improve the quality of its tourism sector and double revenue to USD 14B. The goal is also to attract 500,000 Chinese visitors by 2020, followed by 1 million in the next 10 years.**

Table 1 - Morocco Tourist Arrivals by Country[1]

	2015 Total Arrivals	Growth 2016-2018
France	1,563,568	162%
US	181,468	90%
Italy	227,961	125%
Spain	626,896	304%
China	10,000	75%

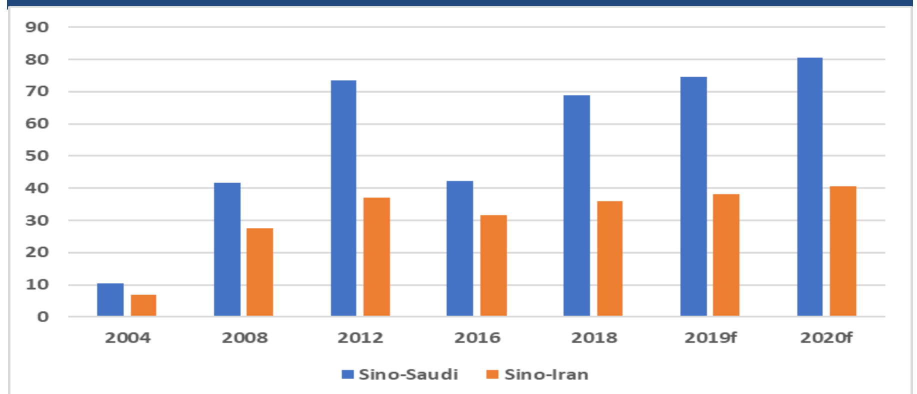
- The goal is also to attract 500,000 Chinese visitors by 2020, followed by 1 million in the next 10 years.
  - We think this is likely as it implies 33% annual growth over 2018 numbers compared with an annual average growth rate of 25% over 2016-2018 (from a low base).
  - Morocco sees enormous opportunities in the Chinese market, which has 130 million tourists traveling abroad annually and spending generously.
  - In September, Morocco's Ministry of Tourism signed a "co-marketing partnership" agreement with Ctrip, China's largest online travel agency, to promote Chinese tourism in Morocco, as part of broader China-Morocco bilateral tourist connections
- The government is also aiming for 20 million global tourists next year. Between 2000 and 2018, Morocco has averaged an annual growth of 6% in tourist arrivals, two percentage points higher than global tourism growth.
  - In support of its Vision 2020 programme, Morocco is planning to expand its existing hotel supply by adding 200,000 hotel beds by 2020 (a 50% increase from current supply).

[1] Arabia Monitor; Ministry of Tourism, Morocco.

China-Iran: A new era in defiance of the US?

- **The Sino-Iranian relationship is at a crossroad. Given the overall trade battle with Washington, China does not want to ramp up even more tension. But with Iran's withdrawal further from the JCPOA, the stakes are too high for China not to engage with Iran when it is in need of friendship.**
  - To avoid escalating tensions while a potential trade deal with the US is still on the table, we expect Beijing to continue to comply with US sanctions on oil imports from Iran, overtly, as a bargaining chip in the much larger potential trade dispute.
    - This will continue to impact the Iranian economy severely as oil and gas account for 82% of Iran's export revenue, and in 2018 Iran's top export destination was China (21% of total exports).
    - From January through July this year, China imported 414 Kb/d of Iranian crude, 37% less than the same period of the previous year.
    - It remains to be seen what the more conciliatory tone from President Trump at the G7 on the trade war, and suggestions that Iran and the US could meet to resolve the US-Iran crisis, will mean.
  - In early September 2019, China announced USD 440B in investments to Iran, of which USD 280B will go into the oil, gas and petrochemical sectors, while the remainder will be invested into industrial infrastructure, in the next five years.
    - The key is that, in return, Iran will grant Chinese companies the priority right to participate in tenders for any new, frozen or incomplete projects to develop oil and gas fields, as well as all petrochemical projects, including the provision of technology and staff to implement these projects.
    - With US-China trade tensions expected to continue, China is eyeing opportunities in Iran beyond Trump's presidential term(s), as it reinforces its energy security and overseas contracting market for the large state-owned enterprises.
- **On its side, Iran is also pulling in Chinese interest and money.**

Figure 1 - China Trade with Saudi Arabia & Iran (USD, B)[1]



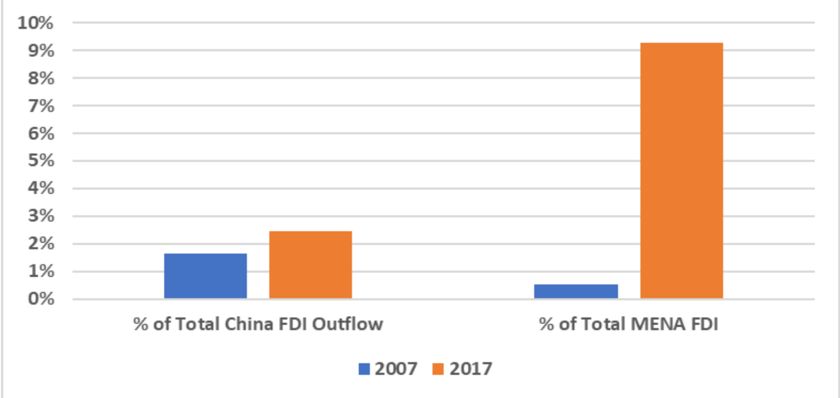
  - In June, Iran exempted Chinese nationals from visas and declared it would no longer require passports to be stamped, bypassing a US ban.
    - Through this, Iran seeks to offset the economic burdens the country is facing and boost its tourism sector, hoping to attract two million Chinese tourists by 2020.
  - Chinese tourists are the largest Asian group in terms of arrivals by region to Iran with around 52,000 visiting Iran in 2018.
  - Iran's plan to attract two million Chinese tourists by 2020 is a challenge given the low base figure of Chinese arrivals and the state of the country's infrastructure, low investment and lacklustre advertising. But the government is trying to redress decades of neglect.
    - Plans are being drafted to construct dozens of five-star hotels around the country, funded in part by cheap government-backed loans and tax incentives for private-sector developers.
    - Under Iran's 2025 vision, the government has planned for certain key structural improvements (through incentives) for the privatisation of the hotel and hospitality industry.

[1] Arabia Monitor; IMF Direction of Trade Statistics.

Sino-MENA: Bilateral FDI small but rising

- **Foreign direct investment flows from China to MENA are still fairly small but play a decisive role in their quest for economic transformation and diversification.**
  - Chinese investment activity in MENA relative to world FDI into MENA has been consistently on the rise accounting for 9.3% of total flows into the region in 2017 from 0.5% in 2007.
    - This was a 61% average annual growth rate in ten years, while GDP growth rate in the region over this period averaged 4.2%.
  - In 2017, Chinese investments in MENA (USD 3B) still constituted a small proportion of total Chinese FDI (~2.5% of a total Chinese FDI outflow of USD 125B) from about USD 0.5B (1.6% of total Chinese FDI outflow of USD 27B in 2007).
  - On a country level, Saudi Arabia only captures 3% of China's FDI in MENA. This compares poorly with Iran for example (39% of China's MENA FDI).
- **Although the United States and European Union have been the main destinations of MENA countries' FDI, the latter have been trying to tap into Asia as well. The financial crisis of 2007-2008, the 2011 Arab Spring and the 2014 oil price drop, however, halted progress sharply. But post-crisis rebounds in FDI lead us to believe that in the absence of upheavals, Arab money to China will increase.**
  - Interest in China has picked up not only because China is slowly becoming attractive as an investment destination, but also because it sits hand in hand with cooperation under China's BRI Initiative.
  - It has been a rocky road, however. First up, then down, then up and down again.
    - FDI from Arab countries to China increased at a steady rate between 2003 and 2008 to reach a then-record level of USD 498M, even if this only accounted for 0.44% of China's total FDI inflows.
    - In 2009, however, Arab FDI declined to USD 26M due to the sluggish global economy, specifically hit by the Dubai debt crisis. Collectively, FDI flows from Arab countries to China declined by 38% in 2008-2009, much sharper than the global 3% decline. As a result, Arab countries' share of China's total inflows declined to a meagre 0.27%.

Table 1 – China Outward FDI to MENA[1]



- After the financial crisis, outflows to China started to rebound, hitting USD 66M in 2010.
- But then the 2011 Arab Spring upheaval throughout North Africa and the Middle East took its toll. Overall FDI from Arab states dropped to USD 12.7M.
- By 2012, FDI from Arab states to China picked up by 78% from a low base to USD 22.6M, driven largely by the UAE and Saudi Arabia, who increased flows to China by 82% and 108% respectively.
- Underscoring an earnest desire to invest in China, FDI from the Arab region shot up to a peak of USD 822M in 2013, with major flows from Saudi Arabia, Morocco, Qatar and Oman.
- But the 2014 drop in oil prices shrank many Arab states' current account surpluses, sovereign wealth reserves and company earnings. This caused FDI to China to decline by 99% to USD 7.6M in 2015 and further to just USD 6.7M in 2016.

[1] Arabia Monitor; MOFCOM China. Latest data available.

Iran Market Monitor: Meeting with US possible, positive outcome not

NR/NR

- **We do not expect any material change in Iran's relations with Washington under the Trump administration, either diplomatically or militarily. The best-case scenario would be a constructive meeting that leads to other meetings, and we expect further escalation of regional tensions.**
  - Iran has enriched about 10% of its uranium stockpile, above the 3.67% limit stipulated in the 2015 nuclear deal that the US has left. It has also increased its stockpile of uranium beyond the 300kg limit in the deal. This makes any renegotiation of a deal harder, but these are not irreversible steps.
  - The US has insisted the nuclear deal can only be revived if Iran renegotiates the terms of the accord, promises to end its "regional aggression" and curtails its ballistic missile programme.
    - We note that "regional aggression" is not a straightforward concept. Iran can have leverage directly through financing proxies and indirectly through centuries-old influence and affinity (cultural and otherwise).
    - It is also not a one-way concept. Others could be accused of similar behaviour.
  - The chance of some kind of meeting is high, but that of a good outcome from it is low under the current White House given that the US and Iran are miles apart in terms of world view and outlook.
- **Continued fractious relations with the US, regional geopolitical tensions and vulnerability to oil price swings are downside risks to Iran's economic outlook.[1]**
  - We, like the IMF, see the economy contracting by 6% this year. This would be Iran's worst recent economic performance since it shrank by 7.7% in 2012.
  - Oil GDP is expected to shrink by 22.3% in 2018/19 as a result of declining exports brought on by US sanctions.
  - As the economy contracts, inflation is expected at 34.1% in 2019/20 from 28.1% in 2018/19.
  - With oil exports declining, the fiscal deficit is expected to rise to 4.2% of GDP in 2019/20 from 3.2% of GDP in 2018/19.

Iran Macroeconomic Indicators[2]

	2015/16	2016/17	2017/18	2018/19	2019/20f
Real GDP Growth (%)	-1.6	12.5	3.7	-3.9	-6.0
Crude Oil Production (M Bpd)	2.9	3.6	3.8	3.4	2.5
CPI Inflation (%)	11.9	9.1	9.6	28.1	34.1
Fiscal Balance (% of GDP)	-1.8	-2.3	-1.4	-3.2	-4.2
C/A Balance (% of GDP)	0.3	4.0	3.8	4.3	-0.4
Total Gov't. Gross Debt (% of GDP)	38.4	47.5	39.5	33.2	30.0
Total Gross Extrn'l Debt (% of GDP)	5.6	2.1	2.0	2.0	2.0
Gross Official Reserves (Mos. of Imports)	19.4	15.5	15.2	16.8	16.2
Nominal GDP (USD B)	375.4	404.4	430.7	452.3	484.7
Population (Millions)	79.3	80.2	81.1	82.0	83.2

- **The Central Bank of Iran (CBI) wants to devalue the rial and rename it the toman (currently the term for 10 rials). The bill has been sent to Parliament, but we do not expect it to pass anytime soon.**
  - At present, there is both an official exchange rate set by the CBI and a market rate that is used in regulated exchange houses.
    - For years, the CBI has been operating an official rate of IR 42,000 to the USD for imports of goods.
    - It trades around IR 116,500 on the black market. In 2015, when the Joint Comprehensive Plan of Action was agreed, the rial traded at 32,000 to the USD.
  - The CBI proposed a similar move in 2017 but this was not approved by the government for fear of raising inflationary pressures.
  - With parliamentary elections scheduled for March 2020, it is unlikely for a decision to be made before the new Parliament takes over.

[1] The Iranian fiscal and calendar year starts on 21 March.
[2] Arabia Monitor; IMF.

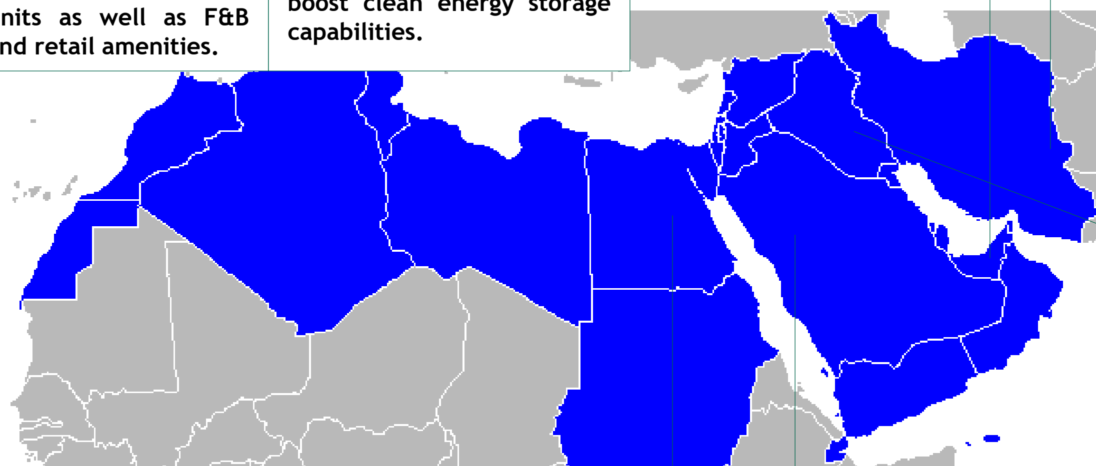
Sino-MENA Deal Tracker: Major deals & projects July-September 2019

USD 400B pledged for Iran's oil, gas, petrochemical and infrastructure sectors in exchange for priority right of Chinese companies to participate in tenders for any new, frozen or incomplete projects in these fields.

MAG Property Development appointed China National Chemical Engineering Group for the construction of MAG City phase 1, featuring over 5,100 units.

Imkan appointed CNTC as main contractor for Pixel project on Reem Island Project to provide 525 residential units as well as F&B and retail amenities.

Abu Dhabi Department of Energy signed a preliminary agreement with State Grid Corporation of China the to boost clean energy storage capabilities.



Construction has resumed in projects awarded pre-war in Iraq, while new players enter the post-war reconstruction market.

Egypt is in talks with auto companies including Geely, Ankai and Foton on producing electric vehicles

Aramco is continuing its downstream push in the Chinese market, acquiring 9% of a local Zhejiang refinery.

MENA Macro Dashboard

Table 1 – MENA Oil Exporters[1]

	Real GDP Growth (%)		CPI Inflation		Fiscal Balance (% of GDP)		C/A Balance (% of GDP)		External Debt (% of GDP)		Reserves (Mos. of Imports)	
	2019e	2020f	2019e	2020f	2019e	2020f	2019e	2020f	2019e	2020f	2019e	2020f
Algeria	2.3	1.8	5.6	6.7	-11.5	-6.4	-12.5	-9.3	2.1	1.9	11.5	8.3
Bahrain	1.8	2.1	3.3	3.2	-8.4	-7.7	-3.6	-3.4	189.9	188.5	0.9	0.8
Iran	-6.0	0.2	37.2	31.0	-4.1	-4.2	-0.4	-0.6	2.0	2.0	16.2	15.8
Iraq	4.6	5.3	2.0	2.0	-4.1	-3.5	-5.2	-4.2	32.1	30.9	6.8	6.2
KSA	1.9	3	-1.1	2.2	-6.5	-5.1	6.9	6.0	40.2	42.2	26.5	25.8
Kuwait	2.5	2.9	2.5	2.7	-10.4	-11.6	7.4	8.0	45.0	48.7	6.8	6.8
Libya	4.3	1.4	15.0	15.0	-10.9	-14.9	-0.2	-7.8	...	...	...	...
Oman	0.3	5.9	1.5	1.8	-9.9	-7.0	-5.9	-4.0	80.2	86.8	5.2	4.9
Qatar	2.6	3.2	0.1	3.7	6.1	6.6	4.6	4.1	106.7	98.3	7.8	7.0
UAE	2.8	3.3	2.1	2.1	-0.8	-1.7	5.9	5.1	68.7	66.4	4.3	4.6
Yemen	2.1	...	20.0	...	-4.5	...	-7.4	...	15.3	...	1.0	...

Table 2 – MENA Oil Importers[1]

	Real GDP Growth (%)		CPI Inflation		Fiscal Balance (% of GDP)		C/A Balance (% of GDP)		External Debt (% of GDP)		Reserves (Mos. of Imports)	
	2019e	2020f	2019e	2020f	2019e	2020f	2019e	2020f	2019e	2020f	2019e	2020f
Djibouti	6.7	6.0	0.8	1.2	-2.1	-1.6	-14.9	-15.4	105.6	106.8	6.1	5.9
Egypt	5.5	5.9	14.5	10.7	-8.3	-6.7	-2.5	-1.8	34.4	31.3	6.6	6.3
Jordan	2.2	2.4	2.0	2.5	-4.0	-3.7	-8.2	-8.0	72.1	75.3	8.0	8.3
Lebanon	1.3	2.0	2.0	2.3	-7.0	-11.0	-28.2	-28.4	191.3	199.4	10.6	10.1
Mauritania	6.4	4.7	3.6	3.9	0.6	0.5	-17.1	-17.8	60.6	62.6	3.8	4.3
Morocco	3.0	3.8	0.6	2.0	-3.7	-3.3	-4.4	-3.5	32.7	34.1	5.2	5.3
Palestine	0.1	...	1.5	...	...	...	-10.4	...	-13.4	...	...	...
Somalia	2.9	3.5	4.0	2.7	0.1	0.2	-8.3	-8.3	...	...	...	...
Sudan	-2.3	-1.3	49.6	58.1	-2.9	-2.5	-9.9	-10.0	177.6	183.6	1.1	1.1
Syria	...	...	...	...	...	...	...	...	...	...	...	...
Tunisia	2.7	3.2	7.5	5.9	-3.7	-2.8	-10.1	-9.1	98.4	107.8	3.0	3.3

[1] Arabia Monitor; IMF.

Algeria: Economy stumbles as impasse continues

NR/NR

- **Eight months since the effective overthrow of decades-long ruler Abdelaziz Bouteflika, protestors have not backed down and the military-backed government appears determined to keep its grip on power. The power struggle threatens an economy that is already slowing, creating hardships that are likely to exacerbate unrest.**
  - Protests in Algeria have been taking place for more than 30 weeks despite elections set for 12 December. They are a clear message to the regime that the popular protest movement Hirak will not easily go away.
    - Hirak have rejected elections under the current government and are still calling for the removal of General Ahmed Gaid Salah, the de facto leader who has so far failed to control the unrest.
    - The election could yet be called off, as were the ones scheduled for 18 April and 4 July.
  - In the meantime, in a move to show that the authorities are following through on promises to crack down on corruption, the trials of Saïd Bouteflika (the ex-president's son), Mohamed Toufik Mediène (a former intelligence chief), Athman Bachir Tartag (a former deputy to Mediène) and Louisa Hanoune (the Algerian Workers' Party president) began on 23 September.
    - All four are charged with plotting against the state and undermining the army. They could face up to 10 years in prison if found guilty.
- **There is growing evidence that the prolonged power struggle could cause a weakening of the economy through higher imports and lower foreign currency reserves.**
  - In April, the IMF revised its Algerian economic growth forecast down to 2.3% for this year from the 2.7% it projected in October 2018 (although still up a bit from 2.1% in 2018).
    - In Q1 2019, the economy grew by 1.5% YoY, the lowest such rate in 20 years, driven by a decline in the real value added from the hydrocarbons sector (-7.7%).
  - Inflation fell to an annual rate of 3.1% in June from 3.6% the previous month due to lower prices for some food items.

Algeria Macroeconomic Indicators[1]	2016	2017	2018	2019e	2020f
Real GDP Growth (%)	3.2	1.4	2.1	2.3	1.8
Crude Oil Production (M bpd)	1.0	0.9	0.9	0.9	0.9
Oil GDP Growth (%)	7.7	-2.4	-3.5	1.9	1.5
Non-oil GDP Growth (%)	2.2	2.2	3.4	2.4	1.8
CPI Inflation (%)	6.4	5.6	4.3	5.6	6.7
Fiscal Balance (% of GDP)	-13.4	-8.6	-6.0	-11.5	-6.4
C/A Balance (% of GDP)	-16.5	-13.2	-9.1	-12.5	-9.3
Total Gov't. Gross Debt (% of GDP)	20.4	27.5	36.9	46.9	48.9
Total Gross External Debt (% of GDP)	2.4	2.5	2.2	2.1	1.9
Gross Official Reserves (Mos. of Imports)	22.5	19.3	15.0	11.5	8.3
Nominal GDP (USD B)	160.1	167.6	180.4	183.7	193.1
Population (Millions)	40.5	41.3	42.2	43.1	43.8

    - But the IMF forecasts that inflation will rise to 5.6% this year from 4.3% in 2018 partly driven by expansionary fiscal policy. The government's target is around 4.5% for this year.
  - In the first half of the year, the trade deficit stood at USD 3.2B, 12% higher than the same period of the previous year mainly due to 6.3% lower energy revenue. Algeria imports 70% of what its population of 42 million consumes.
  - Algeria's foreign exchange reserves were USD 72B (14 months of imports) by end-April compared with a peak of USD 177.4B (33.4 months) in 2014.
    - Reserves are forecast to decrease further to USD 55.6B (11.5 months) in 2019 and USD 39.1B (8.3 months) in 2020.
  - Algeria has signalled it will remove the current cap on foreign ownership of 49% of companies.
    - While we expect this to be lifted for non-strategic sectors, key ones such as oil and gas, defence and manufacturing are likely to still require a controlling local partner.

[1] Arabia Monitor; IMF.

Bahrain: Opening its doors to crypto

B2/B+

- **Overall GDP growth is expected at 1.8% this year, on par with 2018, but slower than 2017's 3.8%. It will be supported by the launch of Aluminium Bahrain's Line 6 Expansion Project, which could make the company the world's largest aluminium smelter.**
  - Non-oil growth is forecast at 2.2%, down from 2.5% in 2018 and 4.9% in 2017.
    - Though lower, growth will be supported by infrastructure projects, notably the Bapco Modernization Program (to allow for expanded refined oil output) and the Khalij al Bahrain oil field development.
  - The Ministry of Finance (MoF) says the kingdom is "well ahead of its projected deficit-reduction schedule". But keeping it going will be tricky, particularly implementing the Fiscal Balance Program's (FBP) goal of lowering subsidies. The second half of 2019 will provide a better opportunity to evaluate progress as reforms take shape.[1]
    - Bahrain's budget deficit narrowed to USD 1.1B (2.8% of GDP) in H1, 35% lower than the same period a year ago.
    - Total revenue for H1 rose by 19% YoY to USD 3.3B driven by 47% YoY higher non-oil revenue, while expenditure for the period was USD 4.4B, 2.5% lower YoY.
    - This follows on, the MoF says, from a full year 2018 budget deficit of USD 2.3B (6% of GDP), 34% lower than the government's previously forecast deficit.[1]
  - The 2019-2020 national budget was approved by the consultative Shura Council in May, with deficits for the two years forecast at 4.6% and 4% of GDP, respectively.
    - We estimate, however, that deficits this year and next will be closer to the IMF forecasts of 8.4% and 7.7% of GDP, respectively, given that the FBP is expected to weigh on the non-oil economy, which comprises over 80% of total economic activity.
    - Introduced in October 2018, the FBP aims to balance state finances by 2022, while reducing existing pubic debt. Key to this is lowering government spending, largely through a voluntary retirement scheme for public sector employees.

Bahrain Macroeconomic Indicators[2]

	2016	2017	2018	2019e	2020f
Real GDP Growth (%)	3.5	3.8	1.8	1.8	2.1
Crude Oil Production (M bpd)	0.20	0.20	0.19	0.19	0.19
Oil GDP Growth (%)	-0.1	-0.7	-1.2	0.2	0.2
Non-oil GDP Growth (%)	4.3	4.9	2.5	2.2	2.5
CPI Inflation (%)	2.8	1.4	2.1	3.3	3.2
Fiscal Balance (% of GDP)	-17.6	-14.2	-11.7	-8.4	-7.7
C/A Balance (% of GDP)	-4.6	-4.5	-5.8	-3.6	-3.4
Total Gov't. Gross Debt (% of GDP)	81.3	88.2	93.4	100.2	103.6
Total Gross Extrn'l Debt (% of GDP)	183.6	181.2	184.7	189.9	188.5
Gross Official Reserves (Mos. of Imports)	1.2	1.2	0.9	0.9	0.8
Nominal GDP (USD B)	32.3	35.4	38.3	39.0	40.7
Population (Millions)	1.4	1.4	1.5	1.6	1.7

- **In July, Bahrain-based Rain became the first cryptocurrency exchange to be regulated in the MENA region, with a funding round of USD 2.5M.**
  - In February, the Central Bank of Bahrain (CBB) approved its final set of rules to regulate trading and other activities involving digital currencies, which are growing in popularity across the region in tandem with global trends.
  - The CBB's introduction of crypto-asset rules is in line with its goal of developing a comprehensive framework for FinTech that will support Bahrain's position as a financial hub in MENA.
  - Bahrain's FinTech Bay, inaugurated in February 2018 on an island in Manama, is already home to more than 30 companies working to develop cryptocurrencies, blockchain systems, digital payments and other financial technologies.
  - In June, UAE-based Souqalmal.com received regulatory approval from the CBB, making it the first to receive an e-broker licence in Manama, and is planning to launch its online insurance comparison services.

[1] Bahrain's Minister of Finance, Sheikh Salman bin Khalifa, made the announcement on 6 September during a periodic review of the USD 10B funding and loans package from its GCC neighbours.
[2] Arabia Monitor; IMF.

Djibouti: Sustained growth, but heavy debt to China

B2/NR

- **Growth in Djibouti is expected to remain above 6% this year and next, a continuous trend from 2016.**
  - It has been driven by several factors, including public sector investments such as a railway to Ethiopia, construction of new ports and a water pipeline from Ethiopia. Foreign direct investment inflows, largely from China, the rent from foreign military bases and Djibouti's strategic geographic location have all added to growth.
  - Inflation is expected to remain steady at 0.8% for 2019, and is projected at 1.2% for 2020, a rise from the 0.1% deflation in 2018. This will be driven by higher food prices and the anchoring of the Djiboutian franc to the US dollar.
  - Djibouti relies mostly on imports of food and petroleum products as well as capital goods.
    - It exports only a small amount, mostly cattle to GCC countries, with 80% of exports being re-exports, mainly to Ethiopia.
    - As a result of the structural deficit in the balance of trade, the current account deficit is expected at 14.9% for 2019, a slight increase from 2018's 14.3% and from 9.4% in 2016.
  - External debt is expected at 105.6% of GDP for 2019 and 106.8% in 2020 from 87.8% in 2016.
    - The IMF estimates debt to China at about USD 1.1B, equivalent to 50% of Djibouti's GDP and over 40% of Djibouti's government-guaranteed external debt.
    - China could eventually seek key strategic assets in return (as it has done elsewhere).
- **Momentum is growing in the Islamic finance sector, a young industry in Djibouti that we believe will continue to expand, driven by the untapped demand of a 90% Muslim population, low financial participation and the introduction of new Islamic banking regulations.**
  - As per latest available figures from 2013 to 2017, Islamic banks increased their market share from 16% to 36%, with ATM ownership growing from 28% to 33% and bank accounts from 42% to 50% in the same period.

Djibouti Macroeconomic Indicators[1]

	2016	2017	2018	2019e	2020f
Real GDP Growth (%)	6.5	6.7	6.7	6.7	6.0
CPI Inflation (%)	0.4	0.8	-0.1	0.8	1.2
Fiscal Balance (% of GDP)	-11.5	-6.1	-4.4	-2.1	-1.6
C/A Balance (% of GDP)	-9.4	-13.8	-14.3	-14.9	-15.4
Total Gov't. Gross Debt (% of GDP)	67.6	69.0	67.4	63.0	58.7
Total Gross Extrn'l Debt (% of GDP)	87.8	97.4	102.9	105.6	106.8
Gross Official Reserves (Mos. of Imports)	4.8	6.4	6.2	6.1	5.9
Nominal GDP (USD B)	1.9	2.0	2.2	2.4	2.6
Population (Millions)	0.9	0.9	0.9	0.9	0.9

- Currently, Islamic banking reflects a significant contribution to the banking assets of the country, improving financial inclusion from 10% in 2006 to a still low 25% in 2017.
- Three Islamic banks -- SABA Islamic Bank, East Africa Bank and Salaam African Bank -- out of a total of 11 in the country account for 21% of total banking assets.
- There are, of course, challenges to this growth. These include overly concentrated geographical, sectoral and commercial reach, and the lack of adequate regulations.
  - Product limitations and the absence of non-banking instruments are also key constraints.
  - Musharakah and Murabaḥah -- products based on the sharing of losses and profits -- account for two-thirds of Islamic financing in Djibouti.
  - Non-banking instruments such as Islamic insurance (Takaful) and project financing through Sukuk are not operational due to the absence of legal frameworks.

[1] Arabia Monitor; IMF.

Egypt: Sisi faces critical test

B3/B

- **Implementing the agreed IMF reforms has already paid dividends. Central Bank of Egypt (CBE) data shows growth of 6.8% for the fiscal year 2018/19, the highest since 2007/08.[1]**
  - ➢ Growth was driven by higher offshore gas production, sustained government investment, and looser monetary policy. The 6.8% growth was in line with both the IMF and government forecasts for that period, significantly higher than the 4% range before the IMF programme.
    - The government expects growth at 6% in 2019/20, close to the IMF's forecast of 5.9%. We have no reason to believe this is not achievable.
  - ➢ In response to inflation sinking to its lowest levels in at least a year, the Central Bank of Egypt (CBE) cut key policy rates by 100 bps on 26 September following a 150 bps reduction on 22 August.
    - The overnight deposit and lending rates were lowered to 13.25% and 14.25%, respectively. The discount rate was also cut by 100 bps to 13.75%.
    - The cuts were supported relatively lower monthly inflation figures, and by favourable base effects.
    - In August, core inflation dropped to 4.9% from the previous month's 5.9%, and a significant drop from the 35.5% peak in July 2017.
    - The Monetary Policy Committee reiterated after its August and September meetings that its moves were consistent with achieving the inflation target of 9% (±3 percentage points) in Q4 2020, and price stability over the medium term.
  - ➢ The state's 2019/20 budget aims to raise GDP by 6% and lower the deficit to 7.2%, down from the 8.4% targeted in FY 2018/19.
- **However, progress on economic reform has not prevented people from taking to the streets again. Small and scattered protests have broken out across Cairo, Alexandria, Damietta and Suez, and demonstrators are echoing the 2011 Arab Spring's chants calling for the fall of the regime.**
  - ➢ Their demand appears to be the immediate resignation of President Abdelfattah el Sisi.
  - ➢ One trigger for this wave of unrest was a series of videos denouncing regime corruption by Mohamed Aly, a construction entrepreneur currently exiled in Spain.

Egypt Macroeconomic Indicators[2]

	2015/16	2016/17	2017/18	2018/19e	2019/20f
Real GDP Growth (%)	4.2	4.3	5.2	5.5	5.9
CPI Inflation (%)	14.0	29.8	13.1	14.5	10.7
Fiscal Balance (% of GDP)	-12.5	-10.9	-8.1	-8.3	-6.7
C/A Balance (% of GDP)	-6.0	-5.6	-2.6	-2.5	-1.8
Total Gov't. Gross Debt (% of GDP)	96.9	103.2	86.2	86.0	83.3
Total Gross Extrn'l Debt (% of GDP)	18.3	41.3	29.9	34.4	31.3
Gross Official Reserves (Mos. of Imports)	3.0	5.0	6.1	6.6	6.3
Nominal GDP (USD B)	332.0	256.0	306.0	303.0	336.0
Population (Millions)	93.7	95.6	97.5	99.3	101.4

- ➢ We do not adhere to the statement that Islamists were behind the protests, but we were not surprised in the sense that these protests are a natural reaction to austerity from the IMF programme and highlight that the fruits of reforms are yet to be delivered to the average citizen. We are watching carefully how the government handles the crowds.
  - Security forces have increased their presence across the country, but they have so far not used any live rounds to disperse crowds.
- ➢ Despite the relatively small size of these demonstrations, the fact they even took place at all is a loud alarm bell for the regime.
- ➢ Even more troubling for Sisi are rumours that sectors of the regime may have incited the protests.
  - While impossible to corroborate, it highlights the possibility that Sisi might be struggling to control even his closest allies, despite several rounds of purges and reshuffles.

[1] Fiscal year beginning 1 July.
[2] Arabia Monitor; IMF; Central Bank of Egypt.

Iraq: Power sector getting much needed attention

Caa1/B-

- **The IMF expects real GDP to rebound strongly by 4.6% this year after a 0.6% contraction in 2018. This is based on oil exports rising 1.5% and reconstruction picking up.**
  - Iraq's oil production capacity is nearing 5 Mb/d and it aims to add another 2 Mb/d over the next few years, according to Minister of Oil Jabbar Alluaibi.
    - Three major fields are currently in the spotlight -- Rumaila (operated by BP), West Qurna 1 (operated by ExxonMobil), and Gharraf (operated by Petronas) -- with more key fields to be announced soon.
    - Infrastructure constraints, however, may continue to prevent the realisation of expansion plans on schedule.
  - The IMF estimates that non-oil growth will increase to 5.4% in 2019 from a 0.6% contraction in 2018, on the back of higher public and private reconstruction investment.
  - The 2019 budget of USD 113B (52.7% of GDP) is 27% higher than last year's, allowed for by higher oil exports.
    - The deficit is projected at USD 23B (10.6% of GDP) this year, double that of 2018.
- **On 14 September, the Ministry of Electricity signed a deal with Siemens and Orascom for the rebuilding of Baiji 1 and Baiji 2 power plants in northern part of the country.**
  - The two power plants -- with a combined generation capacity of 1.6 GW -- were severely damaged during the war with ISIS.
  - Work on the two power plants is expected to be completed within 28 months, once the Iraqi Cabinet approves the contracts and a financing agreement is reached.
  - Restoring the power plants at Baiji will be significant given Iraq's grid has been ravaged by decades of conflict and poor maintenance, causing chronic power cuts across the country.
    - Iraq has been importing electricity from neighbouring Iran, as well as using Iranian natural gas to feed its power plants.
    - Under its Iran embargo, the US has allowed Iraq to import Iranian power, but insists that Baghdad seek alternative sources, which are not immediately available.

Iraq Macroeconomic Indicators[1]

	2016	2017	2018	2019e	2020f
Real GDP Growth (%)	15.2	-2.5	-0.6	4.6	5.3
Crude Oil Production (M bpd)	4.6	4.5	4.4	4.6	4.8
Oil GDP Growth (%)	24.6	-3.5	-1.3	1.3	10.0
Non-oil GDP Growth (%)	1.3	-0.6	0.8	5.4	5.0
CPI Inflation (%)	-1.5	0.2	-0.1	2.0	2.0
Fiscal Balance (% of GDP)	-13.9	-1.6	7.9	-4.1	-3.5
C/A Balance (% of GDP)	-8.3	1.8	6.9	-5.2	-4.2
Total Gov't. Gross Debt (% of GDP)	64.2	58.9	49.3	51.4	50.5
Total Gross Extrn'l Debt (% of GDP)	38.1	36.0	30.4	32.1	30.9
Gross Official Reserves (Mos. of Imports)	7.8	7.3	8.0	6.8	6.2
Nominal GDP (USD B)	175.2	195.5	224.2	224.1	241.5
Population (Millions)	37.2	38.2	38.4	39.3	39.5

    - Iraq receives about 28 million cubic metres of Iranian gas a day for power generation and also directly imports up to 1,300 megawatts of Iranian electricity.
    - The Ministry of Electricity says Iraq's power needs are growing by 7% annually and that there is currently no alternative to importing gas from Tehran.
- **With the 2020 budget allocation legislation looming, time is running out for Baghdad and the Kurdistan Regional Government to hammer out their differences over the latter's share.**
  - The two sides have met since July but only agreed to further dialogue and to form sub-committees to look into oil and gas issues, revenue-sharing and matters of security.
  - In our view, even if a deal were to be negotiated, Prime Minister Adel Abdel Mahdi would struggle to convince his parliamentary opponents to endorse it.
    - Many MPs have previously criticised Abdel Mahdi for being too lenient towards the Kurdistan Regional Government.
    - The region voted for independence in 2017 in a referendum, discouraged by the international community, and deemed illegal by Baghdad.

[1] Arabia Monitor; IMF.

Jordan: Supporting tech businesses & social enterprises

B1/B+

- **The IMF forecasts Jordan's GDP growth for 2019 at 2.2%, an increase from 2018's 2%, yet the economy remains on a slow-growth path compared with 6.5% annual growth in the 10 years prior to 2009.**
  - ➢ Inflation is expected at 2% in 2019, but during the first five months of 2019 it increased by only 0.5% compared with the high of 4.1% in the same period of 2018.
    - The drop in inflation occurred as the effect of price and tax measures undertaken by the government in early 2018 faded out.
    - On 18 September, in response to recent changes in international and regional interest rates, and to boost domestic spending and the availability of credit, the Central Bank of Jordan cut 25 basis points from its benchmark interest rate to 4.25%.
  - ➢ Overall, the fiscal deficit in the first five months reached 3.8% of GDP, compared with 3.5% during the same period of 2018.
  - ➢ While the reopening of the Jordanian-Iraqi border in February increased local exports by 13% in Q1, Jordan's trade with GCC countries remains low.
    - It sends only 10% of its exports to Saudi Arabia and 3.4% to the UAE, compared with exports to Jordan of 13.3% and 4.7%, respectively.
- **In July, the World Bank Group approved a USD 200M grant to support the development of economic opportunities and creation of jobs in technology-enabled activities for Jordanian youth.**
  - ➢ The Ministry of Digital Economy and Entrepreneurship, the implementing agency for the investment, is focusing on three main areas:
    - The first will target digital skills development, which is set to receive USD 150M of the total funding in order to create a mandatory digital skills curriculum for high school students in all public schools across the kingdom.
    - The second, an expected USD 30M over a five-year period, will be used to train Jordanians and Syrian refugees in digital skills including cybersecurity and advanced AI.
    - The third is dedicated to stimulating and growing tech businesses and tech-related social enterprises in Jordan.

Jordan Macroeconomic Indicators[1]

	2016	2017	2018	2019e	2020f
Real GDP Growth (%)	2.0	2.1	2.0	2.2	2.4
CPI Inflation (%)	-0.8	3.3	4.5	2.0	2.5
Fiscal Balance (% of GDP)	-3.6	-3.3	-4.6	-4.0	-3.7
C/A Balance (% of GDP)	-9.4	-10.6	-7.4	-8.2	-8.0
Total Gov't. Gross Debt (% of GDP)	93.8	94.3	94.2	94.8	95.0
Total Gross Extrn'l Debt (% of GDP)	66.3	69.6	67.6	72.1	75.3
Gross Official Reserves (Mos. of Imports)	8.1	8.1	7.4	8.0	8.3
Nominal GDP (USD B)	39.3	40.8	42.4	44.3	46.5
Population (Millions)	9.1	9.4	9.7	10.1	10.2

  - ➢ The information and communications technology sector already makes up over 12% of Jordan's total GDP. The sector also employs around 7% of the total workforce, compared with the region's 4%.
- **With the aim of bolstering the investment climate in Jordan, King Abdullah inaugurated a new free zone at Queen Alia International Airport in early September.**
  - ➢ The free zone is designed to serve as a trade and investment hub by offering logistic services and tax incentives to support investments, imports and exports of various sectors.
  - ➢ Extending over 247 acres of land, the new free zone revamps an older 1988 one, at a cost of more than USD54M.
  - ➢ It is projected to increase direct employment to 3,500 (from a current 300 positions) over the next five years, while raising indirect employment to 4,000 from around 600.
  - ➢ Currently, the free zone houses around 60 local, regional and international investment entities spanning commercial offices, administrative buildings, custom clearance units, banks, restaurants and a one-stop shop for investors.

[1] Arabia Monitor; IMF.

Kingdom of Saudi Arabia: Growth under attack

A1/A-

- **The Ministry of Finance is now expecting economic growth to be slower than it had assumed for the year, although it has given no forecasts. In July, the IMF forecast 1.9% growth for 2019, unchanged from its April estimate. But the uncertainty regarding supply disruptions following the attacks on Saudi oil fields -- as well as the global economic slowdown and its potential effect on the oil market -- could soften growth.**
  - ➢ Major oilfields were attacked on 14 September (blamed, internationally, on Iran), halving output. On 25 September, Aramco said it had restored oil production capacity to 11.3 Mb/d.
    - The fiscal impact could well lead to a revision of the growth forecast for 2019.
    - On 30 September, Saudi Arabia was downgraded for a third time since 2016 by Fitch Ratings, citing the kingdom's vulnerability to military threats following the attack on its oil industry.
  - ➢ The IMF, based on an assumption that Saudi Arabia produces oil at its agreed level under the current OPEC+ agreement in H2, projects oil GDP growth at 0.7% in 2019.
  - ➢ For the non-oil sector, growth is expected to be stimulated by expansionary fiscal policy as the budget for 2019 shows a significant increase in capital expenditure.
  - ➢ While continued structural reforms will place some pressure on growth in the short-term, recent data on non-oil indicators have been positive.
    - The PMI rose to a solidly expansionary 57.7 in August from a five-month low of 56.6 in July, driven by stronger domestic demand.
  - ➢ A budget deficit of USD 8.9B (1.1% of GDP) was posted in Q2 compared with a surplus of USD 7.4B (0.9% of GDP) in Q1 (its first since 2014).
    - Higher expenditure than revenue so far this year pushed H1 2019 accounts into a mild deficit of USD 1.4B (0.2% of GDP). This was is 87% lower than that of H1 2018.
- **The kingdom has made significant progress on key areas of its Financial Sector Development Program (FSDP), especially in terms of SME financing, capital markets and housing. In addition, there have been major moves to attract tourists to the kingdom.** [1]

Saudi Arabia Macroeconomic Indicators[2]

	2016	2017	2018	2019e	2020f
Real GDP Growth (%)	1.7	-0.7	2.2	1.9	3.0
Crude Oil Production (M Bpd)	10.5	10.0	10.3	10.2	10.5
Oil GDP Growth (%)	3.6	-3.1	2.8	0.7	3.5
Non-oil GDP Growth (%)	0.2	1.3	2.1	2.9	2.7
CPI Inflation (%)	2.0	-0.9	2.5	-1.1	2.2
Fiscal Balance (% of GDP)	-17.2	-9.2	-5.9	-6.5	-5.1
C/A Balance (% of GDP)	-3.7	1.5	9.2	6.9	6.0
Total Gov't. Gross Debt (% of GDP)	13.1	17.2	19.1	23.0	24.7
Total Gross Extrn'l Debt (% of GDP)	24.6	34.8	37.0	40.2	42.2
Gross Official Reserves (Mos. of Imports)	31.7	27.9	26.7	26.5	25.8
Nominal GDP (USD B)	645.0	689.0	782.0	786.0	813.0
Population (Millions)	32.4	33.1	33.7	34.2	34.8

- ➢ Reforms to improve SME financing have been stepped up, especially with the introduction of a bankruptcy law. There has been a 5.9% increase in loans granted to SMEs, exceeding the FSDP target of 5% (over a 21 month period).
- ➢ A notable development in stock markets has been the MSCI & FTSE inclusion of the Saudi Stock Exchange (Tadawul) into both indices in March and June, respectively. This has resulted in inflows of over USD 20B so far this year.
- ➢ In the housing sector, new residential mortgages provided by banks reached USD 9.3B in July, 157% growth from the start of this year.
- ➢ On the social reform front, several new decrees have been issued, including:
  - In August, restrictions were removed on women travelling without a "male guardian";
  - Women are also now allowed to get passports without permission from a male guardian;
  - The kingdom launched a new tourist-visa system to allow citizens of 49 countries to visit. Valid for one year, the visa can be applied for via an electronic platform or on arrival.

[1] The FSDP is part of the kingdom's Vision 2030 programme.
[2] Arabia Monitor; IMF.

Kuwait: After ETF & market upgrade, time for a bourse IPO Aa2/AA

- **Kuwait's GDP rate is growing at 2.5% for 2019 as result of an expansion in oil production and higher non-oi activity, according to IMF projections, up from 1.7% in 2018 and a 3.5% contraction in 2017. Fiscal financing remains large, however.**
  - Kuwait, OPECs fifth largest oil producer, benefited from the increase in oil prices stemming from OPEC+ output cuts, to register the highest in Q1 growth since 2009.
    - According to the IMF, crude oil production is expected to rise to 2.79 Mb/d for 2019 from 2.74 Mb/d in 2018 and 2.70 Mb/d in 2017.
    - In turn, the Fund projects Kuwait's oil GDP to recover to 2% for year and rally up to 2.5% in 2020 (up from 1.2% in 2018 and a 7.2% contraction in 2017).
  - Overall growth is also expected to be supported by the non-oil sector as a result of ongoing development plans.
    - While Kuwait is facing delays in the introduction of VAT and tobacco tax, non-oil activities -- particularly in construction and the wholesale and retail trade sectors -- witnessed a boost to 2.5% in 2018 from 2017's 2.1%. They are seen strengthening by 3% this year.
  - Inflation is projected to rise to 2.5% for 2019 from 2018's 0.7% multi-year low. This is the result of price rises in the food, beverages, housing services sectors, as well real-estate rent.
  - Meanwhile, Kuwait's current account surplus is expected to narrow this year to 7.4% of GDP from 12.7% as the value of oil export revenue declines, according to the IMF.
  - The fiscal surplus is projected to drop to 9.5% of GDP this year from 11.3% in 2018, before mandatory transfers to the Future Generations Fund.
    - However, after transfers, the fiscal balance is expected to turn to a deficit of 10.4% of GDP this year from 5.2% of GDP last year.

Kuwait Macroeconomic Indicators[1]

	2016	2017	2018	2019e	2020f
Real GDP Growth (%)	2.9	-3.5	1.7	2.5	2.9
Crude Oil production (M Bpd)	2.95	2.70	2.74	2.79	2.86
Oil GDP Growth (%)	3.9	-7.2	1.2	2.0	2.5
Non-oil GDP Growth (%)	1.4	2.1	2.5	3.0	3.5
CPI Inflation (%)	3.5	1.5	0.7	2.5	2.7
Fiscal Balance (% of GDP; After FGF Transfer)	-17.9	-12.6	-5.2	-10.4	-11.6
C/A Balance (% of GDP)	-4.6	5.9	12.7	7.4	8.0
Total Gov't. Gross Debt (% of GDP)	10.0	20.7	14.8	17.8	21.0
Total Gross Extrn'l Debt (% of GDP)	38.4	45.2	41.4	45.8	48.7
Gross Official Reserves (Mos. of Imports)	6.5	6.6	7.0	6.8	6.8
Nominal GDP (USD B)	109.4	119.5	141.1	136.9	143.0
Population (Millions)	3.9	4.1	4.1	4.2	4.3

- **Following recent developments in Kuwait's capital market, including the launch of an exchange-traded fund and an MSCI market status upgrade, Kuwait's Capital Markets Authority (CMA) has given Boursa Kuwait the greenlight to launch an IPO.**
  - The CMA, current owner of 50% of Boursa Kuwait, said in early September its shares would be offered up on the stock exchange next month. The Kuwait All-Share Index is up around 10% YTD.
  - Added to the sale of 44% of its shares in February to a consortium of investors including Kuwaiti Arzan Financial Group, National Investments Company, Athens Stock Markets and others, Boursa Kuwait will then be 94% privately owned by the end of 2019 with 6% retained for government ownership.
  - The privatisation is part of Kuwait's Vision 2035 to strengthen its positioning on a regional financial front, while also strengthening the contributing role of the private sector to the country's GDP and overall competitiveness and transparency.

[1] Arabia Monitor; IMF.

Lebanon: Banking sector will withstand storms

Caa1/B-

- **The IMF expects the economy to grow by 1.3% in 2019 from 0.3% in 2018, driven by tourism and exports but offset by lagging private investment.**
  - Improved tourism performance -- especially an increase in GCC tourist arrivals (up by 70% YoY in H1) -- is supporting higher private consumption.
    - Overall, tourist arrivals grew by 8.3% YoY in H1 to 923,820. A breakdown of tourist spending for H1 shows that the highest share was from Saudi tourists (15%), followed by the UAE (10%), Kuwait (8%) and Qatar (8%).
    - Accordingly, the occupancy rate of four- and five-star hotels reached 67.8% in H1 compared with 58.6% in the same period last year.
  - Trade data also shows a 19% YoY growth in exports during the first seven months, especially driven by land exports through Syria rising to USD 184M from USD 100M with the gradual reopening of trade routes.
  - The first five months of this year have seen a noticeable improvement in the fiscal balance driven by lower public expenditures (including a 3.6% contraction in transfers to utility Electricité du Liban) as policymakers seek to ensure fiscal consolidation amid a challenging debt trajectory.
    - The deficit stood at USD 2.4B in the first five months, 18.3% lower than the same period last year.
    - For this period, the deficit to GDP ratio was 4%, lower than the 7% deficit budgeted for the whole year.
    - We note that the fiscal balance during this period was the lowest in the last five years.
  - Lebanon's credit rating could be upgraded if the new government does as promised and starts to implement structural reforms needed to secure funds from the international donor conference CEDRE.[1]
    - While the historical track record on reforming these areas remains mixed, even partial implementation could support the disbursement of some donor funds.
- **While Lebanese banks are operating amid local political bickering and regional geopolitical tensions as well as US anti-Hezbollah sanctions, they remain asset-rich and stable.**

Lebanon Macroeconomic Indicators[2]

	2016	2017	2018	2019e	2020f
Real GDP Growth (%)	1.7	1.5	0.3	1.3	2.0
CPI Inflation (%)	-0.8	4.5	6.1	2.0	2.3
Fiscal Balance (% of GDP)	-8.8	-6.0	-9.7	-7.0	-11.0
C/A Balance (% of GDP)	-23.1	-25.7	-27.0	-28.2	-28.4
Total Gov't. Gross Debt (% of GDP)	146.1	149.0	150.9	157.8	162.7
Total Gross Extrn'l Debt (% of GDP)	182.0	183.1	184.7	191.3	199.4
Gross Official Reserves Ex. Gold (Mos. of Imports)	14.9	13.9	12.0	10.6	10.1
Nominal GDP (USD B)	51.5	54.2	56.7	58.3	60.6
Population (Millions)	6.7	6.8	6.8	6.8	6.8

  - Highlighting the challenging environment, data on the banking sector's domestic profits show a 14% YoY decline in H1 to 933M.
  - However, banks had a large and resilient customer deposit base amounting to USD 172B at end-June, equivalent to about 67% of total assets and a huge 300% of GDP.
    - Comparatively, the deposits-to-GDP ratio in MENA stands at 82%. It is just 40% in emerging markets and 52% globally.
  - Loans-to-GDP rates are around 100%, compared with a regional average of 58%, 31% for emerging markets and 44% globally.
  - Aggregate bank assets stood at USD 6.5B in H1, compared with a 5-year average of USD 13.5B.
    - As a percentage of GDP, Lebanon ranks 4th globally in terms of bank assets (after Hong Kong, Cyprus and Denmark).
  - The ratio of non-performing loans to gross loans stood at 6.95% by end of the first half of this year compared with 4.30% in the same period last year. This is relatively high (although for comparison's sake, India is at about 10%), but should be manageable given the large deposit base.

[1] CEDRE ("Conférence économique pour le développement, par les réformes et avec les entreprises").
[2] Arabia Monitor; IMF.

Libya: Little sign of an end to conflict

NR/NR

- **Six months after Khalifa Haftar's offensive, the situation remains very fluid. The extent of foreign intervention is one factor that could determine the end-game for the post-revolution civil war.**
  - Neither the internationally recognised Government of National Accord (GNA) in Tripoli nor the Libyan National Army (LNA) of General Khalifa Haftar have the military wherewithal to defeat each other decisively.
  - Our best-case scenario sees Haftar resuming talks with the GNA under intense international pressure.
  - Our worst-case scenario sees increasing clashes between the GNA and Haftar's forces as the latter attempts to expand his territory. This would undermine efforts to unify the oil sector.
  - Currently, any attempts to tackle the conflict in Libya must address the active role foreign powers are playing in sustaining the war, especially through aerial support.
- **The IMF expects real GDP growth at 4.3% this year based on oil production at around 1 Mb/d. The fall from an estimated 17.9% of GDP in 2018 is exaggerated by the latter's huge bounce from earlier chaos. But such growth will be difficult to attain in a country in conflict and with the oil sector subject to constant supply disruptions.**
  - The ongoing conflict is naturally causing economic damage, taking its toll on civilians, disrupting water and electricity infrastructure, and imperilling the oil production upon which Libya relies.
  - Oil output has been hampered by technical breakdowns, protests and sabotage. Production averaged 952 Kb/d in 2018, up from 811 Kb/d in 2017.
    - More recently, national output reached a five-month low of 950 Kb/d in August compared with a recent five-year peak of around 1.17 Mb/d in April and May. The largest oilfield, Sharara, has been under force majeure since July.
  - The IMF also expects inflation to slow this year, forecasting 15%. This is still unsustainable, but down from 23.1% in 2018, partly as a result of efforts by the Central Bank of Libya (CBL) to stabilise the currency.

Libya Macroeconomic Indicators[1]

	2016	2017	2018	2019e	2020f
Real GDP Growth (%)	-7.4	64.0	17.9	4.3	1.4
Crude Oil Production (M Bpd)	0.3	0.8	0.9	1.0	1.0
Oil GDP Growth (%)*	-5.4	116.8	10.5	12.4	...
Non-oil GDP Growth (%)*	-2.0	0.0	5.0	3.0	...
CPI Inflation (%)	25.9	28.5	23.1	15.0	15.0
Fiscal Balance (% of GDP)	-113.3	-43.0	-7.4	-10.9	-14.9
C/A Balance (% of GDP)	-24.7	7.9	2.0	-0.2	-7.8
Total Gov't. Gross Debt (% of GDP)	189.7	140.8	102.5	104.8	111.6
Total Gross Extrn'l Debt (% of GDP)	20.6	...	...	...	...
Gross Official Reserves (Months of Imports)	19.8	...	...	...	...
Nominal GDP (USD B)	18.5	30.6	43.6	45.0	50.4
Population (Millions)	6.4	6.5	6.6	6.7	6.8

- The imposition of a 163% fee on dollar purchases and foreign exchange transactions along with 24% higher oil revenue (which make up about 90% of total revenues and about 50% of GDP), contributed to a budget surplus last year, the first after five years of deficit. But political instability, the volatility of oil revenues and high state expenditures will make this hard to maintain.
  - Spending in 2019 is set 10% higher than last year with a balanced budget being sought by the government. But having projected a breakeven oil price of USD 71.3 pb, the IMF expects a deficit of 10.9% of GDP, higher than 2018's 7.4%.
  - The rising public-sector wage bill, which is currently the highest rate in the world at 55.2% of total expenditures and 48% of GDP, reflects the overreliance on government.
  - Moreover, the government's payroll and hiring have significantly increased, threatening further stress on the budget.

[1] Arabia Monitor; IMF.

Mauritania: Gold & iron ore prices to the rescue

NR/NR

- **In April, the IMF revised Mauritania's growth forecast down to 6.4% for 2019 (from an earlier 6.7% in May) and projected a drop in 2020 to 4.7%. We remain bullish, however, on prospects for the mining sector providing a positive economic windfall for the country.**
  - ➢ Growth remains strong as a result of higher exports of iron ore, which make up 26% of GDP and of gold, which contribute 20%.
    - There has also been a recovery in the agriculture sector, which brings in 25% of GDP.
  - ➢ Inflation reached an average of 3.1% in 2018 due to the rise of food prices, but started to trend downwards during Q1 of 2019 to 1.8% YoY.
    - Nonetheless, the IMF projects inflation at the end of 2019 to rise to 3.9% and reach 4% in 2020.
    - This will be driven by lower interest rates: the Central Bank of Mauritania eased monetary policy last year for the first time in 10 years to boost credit to enterprises and households.
      - The policy rate is now 6.5%, down from the 9% in place for most of former leader Mohamed Ould Abdel Aziz's decade in office. It is likely to have led to a rise in consumption as money has been cheaper to borrow.
  - ➢ According to the IMF, total gross external debt to GDP is projected to decline to 60.6% for 2019 from 2018's 81.7%, driven by a slowdown in project loan disbursements for public investment.
- **According to the IMF, mining revenue is projected to reach USD 22.6B, a slight decline compared with 2018 estimates of USD 22.9B. However, this can potentially grow as investments from the World Bank flow in and global prices rises.**
  - ➢ Gold is currently trading up around 17% YTD; iron ore has gained around 36% since the end of 2018.
  - ➢ A USD 300M investment in the open-pit gold mine Tasiast region in Mauritania (300 kms north of the capital Nouakchott) is pending approval by October from the World Bank's International Finance Corporation (IFC).

Mauritania Macroeconomic Indicators[1]

	2016	2017	2018	2019e	2020f
Real GDP Growth (%)	1.8	3.0	3.0	6.4	4.7
CPI Inflation (%)	1.5	2.3	3.1	3.6	3.9
Fiscal Balance (% of GDP)	-0.5	0.0	1.6	0.6	0.5
C/A Balance (% of GDP)	-15.1	-14.4	-18.0	-17.1	-17.8
Total Gov't. Gross Debt (% of GDP)	78.5	76.8	83.9	80.6	82.0
Total Gross Extrn'l Debt (% of GDP)	87.8	87.7	81.7	60.6	62.6
Gross Official Reserves (Mos. of Imports)	3.5	3.3	3.2	3.8	4.3
Nominal GDP (USD B)	4.7	4.9	5.2	5.6	5.7
Population (Millions)	4.2	4.3	4.4	4.5	4.6

- ➢ The mine is owned by Tasiast Mauritania Limited, a subsidiary of Kinross Gold Corporation, a Canada-based mining company.
  - The new investment will include a joint venture, with IFC investing a total of USD 155M and USD145M from a consortium including Canada Export Development, part of the Canadian Development Finance Institution.
- ➢ Such a large investment will spur further economic development.
  - Since the presence of Kinross Gold Corporation, Mauritania has benefited from a total of USD 1.6B in subcontractors' payments between 2011 to 2017, along with a further USD 580M paid in taxes, duties and royalties which contributed 5.5% to the country's revenue.
  - Gold production at the Tasiast gold mine is expected to increase from 12,000 kg/yr this year to exceed 24,000 kg/yr by 2020.
- ➢ Majority government-owned Societe Nationale Industrielle et Minière is also planning to increase its capacity to produce iron ore from 25 Mt/yr this year to 40 Mt/yr by 2025.

[1] Arabia Monitor; IMF.

Morocco: Becoming MENA’s renewables superpower

Ba1/BBB-

- **Both the Moroccan government and the IMF revised down their GDP forecasts for 2019 by 0.2 percentage points, reflecting slower agricultural growth. But overall economic activity is expected to be supported by non-agricultural sectors, including fisheries and renewable energy.**
  - ➢ The government revised its 2019 economic growth forecast to 2.7% from 2.9%, while the IMF changed its estimate to 3% in July from 3.2% in its April Regional Economic Outlook.
    - According to data from the country’s economic planning agency, the Haut-commissariat au plan (HCP), growth slowed to an annualised rate of 2.6% in Q2 from 2.8% in Q1.
    - The Moroccan economy posted 3% growth in 2018 according to both the HCP and IMF, but lower agricultural production -- driven by late rainfall and the lack of a sound irrigation system -- has squeezed growth so far this year.
    - As a result, the Ministry of Agriculture expects cereal production to reach 6.1M tonnes in 2019, 40.7% lower than in 2018.
    - According to HCP, economic growth is expected to remain moderate in the Q3, hurt by a 2.5% decline in agriculture's contribution. This decline would be accompanied by an increase in farmers' expenses, mainly due to higher feed prices, particularly for barley and straw.
  - ➢ As economic growth remains relatively slow, overall inflation is forecast at 0.6% this year from 0.1% in 2018, driven by the rise in agriculture prices.
  - ➢ The government is considering reforms to make taxes more efficient with an eye to lowering the fiscal deficit and gross debt to 3.3% and 64.3%, respectively, in 2020. The budget deficit is expected to remain at 3.7% this year.
- **Renewable energy is boosting Morocco’s electricity production to meet national needs and those of others.**
  - ➢ The kingdom became a net exporter of electricity to Spain in 2018.
  - ➢ Several renewable power generation projects (solar and wind) have come online, notably the Safi Thermal Power Plant and solar energy stations in the Midelt and Ouarzazate in the Atlas regions. They have increased Morocco’s capacity to nearly 3,500 MW.

Morocco Macroeconomic Indicators[1]

	2016	2017	2018	2019e	2020f
Real GDP Growth (%)	1.1	4.1	3.0	3.0	3.8
CPI Inflation (%)	1.8	1.9	0.1	0.6	2.0
Fiscal Balance (% of GDP)	-4.5	-3.5	-3.7	-3.7	-3.3
C/A Balance (% of GDP)	-5.0	-4.5	-5.8	-4.4	-3.5
Total Gov’t. Gross Debt (% of GDP)	64.9	65.1	64.9	65.1	64.3
Total Gross Extrn'l Debt (% of GDP)	33.7	34.5	31.1	32.7	34.1
Gross Official Reserves (Mos. of Imports)	6.1	5.7	5.2	5.2	5.3
Nominal GDP (USD B)	103.3	109.7	118.6	120.7	129.1
Population (Millions)	35.2	35.7	36.0	36.4	36.9

- ➢ The country has the most ambitious clean energy target in the MENA region, and is on track to gain 52% of its energy generation from renewable sources by 2030.
  - It is the only country in North Africa without significant fossil fuel reserves, and it imports over 90% of its energy, making up to 12% of its GDP.
  - Morocco's goal is to produce 42% (6,000 MW) of its electricity mix from renewables by next year (with solar and wind providing 28% of power capacity).
- ➢ Morocco’s potential in wind energy is largely untapped. About 10% (750 MW) of electricity produced is generated through wind power while wind energy potential in the country is estimated at 25,000 MW.
- ➢ The kingdom is currently investing more than USD 13B in developing its renewables capacities with USD 30B in total due in the next 15 years.
- ➢ The impressive progress that renewable energy projects in Morocco have made is the result of the favourable legal, institutional, and financial framework offered by the government. A recognised example is Noor Ouarzazate, the first solar mega-project launched by the Moroccan Agency for Sustainable Energy (Masen) which came online in February 2016.

[1] Arabia Monitor; IMF.

Oman: Stable, slow and hostage to oil price

Ba1/BB

- **The IMF forecasts Oman's economic growth at 0.3% for 2019, a sharp cut from the 5% estimate in October 2018 and the 1.1% in April.**
  - Oil will be the key. The Fund, for example, revised up its Oman GDP growth forecast to 5.9% for 2020 from its previous estimate of 2.7% because of government plans to increase investment significantly in the Khazzan gas field
  - Inflation is forecast at 1.5% this year and 1.8% for 2020, a leap from 2018's 0.9% estimate, driven by higher prices of food, clothing and restaurants and hotels.
  - Supported by a significant rise in government revenues and a slight decrease in total spending, Oman's budget deficit dropped to the lowest level in five years in H1 2019.
    - The sultanate's budget deficit declined by 53% to USD 1.7B (2.1% of GDP), according to latest figures released by the National Centre for Statistics and Information. Boosted by higher income from oil, gas and corporate tax, the government's total revenues grew 11.4% YoY. Net oil revenues rose 5% YoY, gas revenues increased 9.3% YoY and revenue from corporate income tax jumped more than 45% YoY.
    - On the spending side, Oman's total public expenditure decreased 2.8% YoY in H1 2019, mainly due to a significant reduction in investment expenditure, which dropped 13.5% YoY. Current expenditure remained almost flat during this period.
    - Even before the H1 figure was announced, the government published data for the first five months of 2019 showing a 67% YoY drop in the deficit, resulting in a credit rating affirmation by Fitch in late July.
    - Taking advantage of this, and of overall positive conditions in the regional debt market, the sultanate issued USD 3B in bonds at the end of July, its first issue this year.
    - The sale was 4.6 times oversubscribed, leaving the yield for the five-year bonds at 4.95% and the 10-year paper at 6%. The yields were slightly higher than the 4.12% and 5.62%, respectively, achieved last year when the sultanate issued a record USD 6.5B in bonds that were 2.3 times oversubscribed.

Oman Macroeconomic Indicators[1]

	2016	2017	2018	2019e	2020f
Real GDP Growth (%)	5.0	-0.9	2.2	0.3	5.9
Crude Oil Production (M Bpd)	1.0	0.9	0.9	0.9	1.1
Oil GDP Growth (%)	3.6	-2.5	3.1	-1.1	10.0
Non-Oil GDP Growth (%)	6.2	0.5	1.5	1.5	2.5
CPI Inflation (%)	1.1	1.6	0.9	1.5	1.8
Fiscal Balance (% of GDP)	-21.2	-12.9	-7.7	-9.9	-7.0
C/A Balance (% of GDP)	-18.7	-15.2	-4.7	-5.9	-4.0
Total Gov't. Gross Debt (% of GDP)	32.5	46.9	53.3	58.7	61.1
Total Gross Extrn'l Debt (% of GDP)	44.2	64.2	74.7	80.2	86.8
Gross Official Reserves (Mos. of Imports)	7.0	5.5	5.8	5.2	4.9
Nominal GDP (USD B)	65.9	70.8	79.3	77.6	80.3
Population (Millions)	4.4	4.6	4.8	4.9	5.1

  - However, Oman's general budget is still facing challenges posed by oil price fluctuations and by rising debt levels since 2016 that remain a concern of ratings agencies.
  - Total government debt is estimated at 50.9% of GDP in 2018 with most of it sourced externally (35% of GDP).

- **In an increasingly competitive market, with an ever-changing risk and technological landscape, Oman has been piloting innovation in its banking sector.**
  - In line with Oman's diversification reform plans, the Ministry of Commerce and Industry hosted an e-commerce conference in cooperation with Innovex Company and Omani investment holding company Ominvest in September.
  - Among the ventures announced at the symposium, the National Bank of Oman (NBO) launched prepaid banking cards known as "Badeel" to be open to both NBO customers and non-customers.
  - According to NBO data, over 60% of all its customer service transactions are done using digital banking solutions, while the number of customers using digital banking services rose by 90% YoY in 2018.

[1] Arabia Monitor; IMF.

Palestine: Economy "near collapse"

NR/NR

- **The IMF expects economic growth in Palestine to fall to 0.1% this year from 0.4% in 2018 and 3.1% in 2017 as reconstruction activity and private consumption slow, and lower overseas aid arrives. UNCTAD has gone further, warning of economic collapse.**
  - The grim economic outlook comes with a liquidity squeeze and high credit spending and debt.
  - Alleviating some pressure, on 22 August the Palestinian National Authority (PNA) reached an agreement with the Israeli government for the latter's release of part of the "clearance" revenues it had held since March totalling USD 568M.
    - The funds represent fuel taxes that Israel has been collecting on behalf of the PNA for the past seven months as part of the usual clearance tax arrangements.
    - The disbursement will allow the PNA to pay public sector employees and to settle some of the PNA's debts to the Israeli Electricity Company.
    - While this will reduce the burden, around two thirds of the clearance revenues continue to be withheld by Israel.
  - UNCTAD, the United Nations development agency, said on 10 September that without clearance revenues (and with overseas aid declining), there was a danger of economic "collapse". It said Gaza was increasingly "unliveable".
  - A major unknown at this stage is the impact of the Israeli election, which is likely to take some time to play out as major players seek coalitions.
    - Prime Minister Benjamin Netanyahu pledged to annex Israeli settlements on the West Bank if re-elected, but failed to win a ruling majority.
  - Inflation is expected to rise to 1.5% for 2019, from 2018's 0.8%, due to the higher cost of imports and global food prices.
- **On 17 September, the West Bank hosted the International Conference on Entrepreneurship, its first on the subject, focusing on facilitating entrepreneurship through a more conducive regulatory environment and greater access to capital.**

Palestine Macroeconomic Indicators[1]					
	2015	2016	2017	2018	2019e
Real GDP Growth (%)	3.4	4.1	3.1	0.4	0.1
CPI Inflation (%)	1.4	-0.2	0.2	0.8	1.5
Fiscal Balance (Ex-support, % of GDP)	39.2	35.2	37.5	39.5	...
Recurrent Budget Support (% of GDP)	-11.4	-8.1	-8.1	-8.3	-10.4
C/A Balance (% of GDP)	-16.3	-10.1	-10.9	-12.7	-13.4
Nominal GDP (USD B)	7.1	12.7	13.4	14.5	15.0
Population (Millions)	4.6	4.7	4.9	5.0	5.1

  - The conference was organised by the Global Shapers Community Palestine, an offshoot of the World Economic Forum, and supported by the Ministry of Entrepreneurship & Empowerment and various international companies.
  - Held in Bethlehem, the conference brought together Palestinian entrepreneurs, technology and business entities in finance along with international experts from Germany and prominent companies including Orange and Dell.
  - On average, over 10% of the population is involved in entrepreneurial ventures versus a 12% MENA average. Some 20% of Palestinian start-ups last year are estimated to have involved women entrepreneurs.
  - Venture capital and microfinance institutions account collectively for less than a third of start up financing, with banks following at 13%.
  - Over 40% of Palestinian entrepreneurs typically require less than USD 5K in start-up capital vs. USD 9.2K on average in MENA.
    - Opportunities abound for funds looking to invest in diversified small to medium sized portfolios, given some risk appetite.

[1] Arabia Monitor; IMF.

Qatar: One step forward, two steps back in rift with neighbours

Aa3/AA-

- **We maintain our view that Qatar's rift with its GCC neighbours will not be solved with any "big bang" announcement, but via a very slow and subtle normalisation that will be uneven in pace and will sometimes reverse.**
  - We have seen in the past couple of months that a slow normalisation has begun on the commercial side. such as the move in February by Dubai's largest port operator, DP World, allowing third-party shippers to move cargo to and from Qatar.
  - In contrast, and in what could exacerbate the rift, Turkey announced that the number of Turkish soldiers in Qatar was expected to increase this year with the opening of a second military base. Closing the first Turkish base in Qatar was one of the 13 demands of the Saudi-led Arab Quartet when its embargo began.
  - Qatar and Saudi Arabia are also in danger of engaging in another power struggle, this time over Somalia, a strategic country in the Horn of Africa.
    - Qatar has said it will build a new seaport in Hobyo, up the coast from Mogadishu in Somalia. The seaport would be relatively close to the Bab-el-Mandeb Strait, which is one of the most significant sea crossing points in the region.
    - Saudi Arabia, however, has recognised passports from the self-declared state of Somaliland, viewed internationally as only an autonomous region of Somalia.
  - Overall, we see steps constituting normalisation coming over the next several quarters before things get back to normal without fanfare, perhaps over the next couple of years.
- **Real GDP growth is forecast by the IMF at 2.6% this year from 2.2% in 2018 and 1.6% in 2017. This is not far from the 2.8% average over 2018-2020 estimated by Qatar's Planning and Statistics Ministry for 2019.**
  - Growth this year will be driven by a recovery in oil output and robust non-oil activity from ongoing infrastructure projects related to World Cup 2022, as well as from higher gas production.

Qatar Macroeconomic Indicators[1]	2016	2017	2018	2019e	2020f
Real GDP Growth (%)	2.1	1.6	2.2	2.6	3.2
Crude Oil Production (Mb/d)	0.6	0.6	0.6	0.6	0.6
Oil GDP Growth (%)	-0.9	-0.7	-1.1	0.4	1.8
Non-oil GDP Growth (%)	5.3	3.8	5.3	4.6	4.3
CPI Inflation (%)	2.7	0.4	0.2	0.1	3.7
Fiscal Balance (% of GDP)	-5.4	-2.9	5.3	6.1	6.6
C/A Balance (% of GDP)	-5.5	3.8	9.3	4.6	4.1
Total Gov't. Gross Debt (% of GDP)	46.7	49.8	48.4	52.7	45.9
Total Gross Extrn'l Debt (% of GDP)	127.2	99.6	101.1	106.7	98.3
Gross Official Reserves (Mos. of Imports)	6.1	2.8	5.5	7.8	7.0
Nominal GDP (USD B)	151.7	166.9	192.4	193.5	204.0
Population (Millions)	2.5	2.6	2.7	2.8	2.8

    - These will continue to fuel the expansion of the non-oil sector and provide employment for Qatar's growing population.
    - In Q1 2019, real GDP growth stood at 0.9% YoY, and compares with 0.7% in Q3 2017 after the boycott began.
  - Inflation is low in Qatar (0.1%) and price controls have prevented extortionary profiting from the sale of goods in high demand, especially food items. But next year, the inflation rate is projected to rise sharply to 3.7% if a planned introduction of VAT goes ahead.
  - Despite immediate pressure when the rift began, foreign exchange reserves stood at USD 52.4B in April 2019 (more than eight months of import cover), compared with USD 45.2B in June 2018 (seven months' cover) and a five-year low of USD 24B in June 2017 when the boycott was imposed (three months of imports).
  - The latest data available for Q2 2019 suggests real estate prices were up 2% YoY compared with a 0.4% YoY decline in Q1 2019.
    - According to the Qatar Central Bank's real estate price index, the rebound follows a decline of 15% during 2017-18. Over 2012-16, real estate prices rose by 82%.

[1] Arabia Monitor; IMF.

Somalia: Still over-reliant on agriculture

NR/NR

- **Risks ahead are on the downside as growth remains fragile and vulnerable to climate and security shocks.**
  - The IMF projects steady GDP growth of 2.9% this year (if normal rains resume) and 3.5% in 2020. This follows 2.8% GDP growth last year when the agricultural economy rebounded from drought.
    - Growth is being supported by heightened activity in the construction, financial services and telecommunications sectors.
    - But the economy remains dangerously vulnerable to its over-reliance on agriculture, which comprises 75% of Somalia's GDP and 93% of its exports.
    - Heavy rainfall in May had a relatively adverse effect on livestock and crops, for example.
  - Inflation is forecast to increase to 4% this year, from 3.2% in 2018 and 5.2% in 2017 as a result of higher food prices, again weather-related.
  - Fiscal progress is encouraging, driven by reforms to expand the tax base and strengthen tax policies.
    - Taxes contributed 29% of domestic revenue (around USD 184M in 2018 and USD54M in Q1 of 2019).
    - Most of the revenue is spent on salaries and other operating costs, especially on security-related expenditures, with little space for critical social and development programmes.
  - Without debt relief, Somalia's external debt -- equivalent to its nominal GDP -- is unsustainable, and the country's reserves are minimal (less than one month of import cover).
  - The IMF expects the current account deficit to shrink slightly to 8.3% of GDP this year from 9% of GDP in 2018 and 9.4% of GDP in 2017, as imports and official grant inflows ease.
- **International investments into Somalia having been mounting. Qatar, for example, is planning to establish a strategic partnership and build a seaport in Hobyo.**

Somalia Macroeconomic Indicators[1]

	2016	2017	2018	2019e	2020f
Real GDP Growth (%)	4.9	2.3	2.8	2.9	3.5
CPI Inflation (%)	1.3	5.2	3.2	4.0	2.7
Fiscal Balance (% of GDP)	0.0	-0.6	0.0	0.1	0.2
C/A Balance (% of GDP)	-6.0	-9.4	-9.0	-8.3	-8.3
Total Gov't. Gross Debt (% of GDP)	…	…	…	…	…
Total Gross Extrn'l Debt (% of GDP)	105.3	103.3	99.5	99.5	99.5
Gross Official Reserves (Mos. of Imports)	…	…	…	…	…
Nominal GDP (USD B)	4.1	4.5	4.7	4.9	5.2
Population (Millions)	14.3	14.7	15.1	15.6	16.0

  - Qatar-Somalia relations have grown this year. In February, Qatar launched a USD 200M highway project to connect Mogadishu, the capital of Somalia, with several agricultural towns including Jowhar and Afgoye.
  - Following Foreign Minister Sheikh Mohammed bin Abdulrahman bin Jassim Al Thani's visit to Somalia in August, Qatar's port management company Mwani announced a USD 173M investment to construct a new seaport in Hobyo.
    - The port of Hobyo is one of Somalia's oldest ports, located on northeast coast near the Gulf of Aden.
    - The investment will allow Somalia to penetrate new markets and expand commercial relations.
  - It will also help increase trade between East Africa and Qatar which has been expanding its presence in the region.
    - The Qatar Fund for Development has contributed grants and concessional loans to East Africa that exceeded USD 4B over the last eight years.

[1] Arabia Monitor; IMF.

Sudan: Economists take top posts in new government NR/NR

- **Talks are still ongoing with civilian representatives to fill the final two ministerial positions in Prime Minister Abdalla Hamdok's 20-member Cabinet, which was formed on 5 September, just shy of four months after President Omar al-Bashir was ousted.**
  - ➢ The government is part of a three-year power-sharing agreement between the military, civilian representatives and protest groups.
    - Under the agreement, the military will head a transitional authority for 21 months, with a civilian figure in charge for the following 18 months after which elections will be held.
    - The Cabinet was largely selected by the prime minister, an economist and former diplomat. Only the interior and defence ministers were chosen by the military members of Sudan's ruling body.
  - ➢ Former World Bank economist Ibrahim Elbadawi was appointed as Minister of Finance.
    - Among the 18 ministers announced were four women -- including Sudan's first female foreign minister, Asma Mohamed Abdallah.
    - Madani Abbas Madani, the leader of the civilian coalition that negotiated the power-sharing deal, was named Minister of Industry and Trade.
    - Police Lieutenant General Idriss al-Traifi was named Minister of Interior, while Army Lieutenant General Jamal Omar took on the post of defence portfolio.
  - ➢ Under agreed timelines, a Transitional Legislative Council is to be formed before the end of November.
    - It will have no more than 300 members, with 201 seats allocated to the Forces for Freedom and Change, which spearheaded the protests against al-Bashir.
- **Hamdok's Cabinet faces the daunting task of dealing with Sudan's mounting economic problems -- including very high inflation and unemployment -- after decades of poor governance.**
  - ➢ A key challenge will be integrating the country into the international economy after 20 years of crippling US trade sanctions, most of which have now been lifted.

Sudan Macroeconomic Indicators[1]

	2016	2017	2018	2019e	2020f
Real GDP Growth (%)	2.9	1.7	-2.1	-2.3	-1.3
CPI Inflation (%)	17.8	32.4	63.3	49.6	58.1
Fiscal Balance (% of GDP)	-1.7	-1.5	-3.1	-2.9	-2.5
C/A Balance (% of GDP)	-7.6	-10.5	-11.5	-9.9	-10.0
Total Gov't. Gross Debt (% of GDP)	99.9	122.0	163.2	177.9	182.4
Total Gross Extrn'l Debt (% of GDP)	93.9	117.0	161.2	177.6	183.6
Gross Official Reserves (Mos. of Imports)	0.9	0.9	1.0	1.1	1.1
Nominal GDP (USD B)	55.6	45.7	33.9	31.5	31.1
Population (Millions)	39.8	40.8	41.8	42.8	43.8

- ➢ Sudan's economy is expected to sink deeper into recession with a contraction of 2.3% this year, worse than previously forecast.
  - The revised IMF forecast reflects the recent political upheaval in the country.
  - The IMF view was already bleak (a 1.9% contraction) due to the demonstrations which started in December 2018.
- ➢ Inflation remains high at a projected 49.6%, although it is below last year's staggering 63.3%.
  - This is due to measures undertaken by the central bank, most notably lowering the exchange rate to SDG 15 to the dollar from SDG 18 to the dollar.
- ➢ The fiscal deficit is also set to improve slightly from 3.1% last year to 2.9% this year, driven by ongoing subsidy cuts.
- ➢ The youth unemployment rate stands at 27%, with a quarter being university graduates.

[1] Arabia Monitor; IMF.

Syria: Pound continues to slide

NR/NR

- **The war in Syria has been grinding on at a relatively low level in recent months -- "a forgotten war" is how some commentators have described it -- but the probability of an escalation around Idlib is rising. A ceasefire option put forward at the United Nations Security Council on 19 September was vetoed by Russia and China.**
  - The Syrian government is renewing its offensive on Idlib, the last major stronghold of rebel and jihadist groups seeking to overthrow President Bashar al-Assad.
  - There is a large risk of a new humanitarian crisis and of a potential clash between major powers.
    - Idlib is home to some 2.9 million people, including 1 million children. Almost half of the civilians come from other previously rebel-held parts of Syria from which they either fled or were evacuated.
    - The province borders Turkey to the north, spans major highways running south from Aleppo to Hama and the capital Damascus, and stretches west to the Mediterranean coastal city of Latakia.
  - In one positive move towards peace, UN Secretary-General Antonio Guterres announced on 23 September the creation of a constitutional committee comprising of government and opposition representatives to resume the political process.
    - Various peace initiatives have been tried since 2014, essentially all failing.
- **Recent economic data for Syria is hard to come by, including from the IMF and World Bank. There is no evidence to suggest, however, that the 2010-17 decline did not continue last year and will not prevail this year. Hit by sanctions, the country is also grasping with a lower value of the Syrian pound and a central bank with little in its toolbox.**
  - Fitch Solutions recently forecast that Syrian economic growth could rebound by 5.8% this year, while The Economist has projected 9.9% (both of course from a very low base). We note that even if either of these forecasts materialises (and if all fighting stopped), there is no chance of Syria returning to its pre-war state in the short- or medium-term.
  - The economy was relatively stable with annual GDP growth averaging around 5% before the war began in 2011. It has since been devastated. From 2010 to 2017, economic activity shrank by more than 70%, so there is probably more than a decade of quite robust growth needed just to get it back to where it was.

Syria Macroeconomic Indicators[1]

	2012	2013	2014	2015	2016
Real GDP Growth (%)	-18.9	-18.7	1.8	-15.0	-4.0
CPI Inflation (%)	36.7	91.7	36.4	15.2	40.0
Fiscal Balance (% of GDP)	-16.9	-12.3	-8.6	-7.3	…
C/A Balance (% of GDP)	-15.3	-12.2	-10.5	-10.8	…
Total Gov't. Net Debt (%of GDP)	54.1	52.5	53.2	58.7	…
Total Gross External Debt (% of GDP)	19.2	23.1	26.9	31.1	…
Gross Official Reserves (USD B)	4.8	1.8	1.8	1.7	…
Nominal GDP (USD B)	44.0	42.8	43.4	20.0	15.0
Population (Millions)	19.2	18.7	18.4	18.2	18.2

- The loss of exports due to sanctions and the conflict have led to a severe foreign currency crisis.
  - The pound now trades at around SYP 650 to the US dollar on the black market, compared with SYP 47 to the dollar before initial anti-Assad protests erupted in March 2011.
  - The official rate adopted by the Central Bank of Syria (CBS) for remittance exchange purposes is around SYP 435. This had lowered the value of foreign inflows by around 30% compared with the original rate of SYP 195 to the dollar.
  - The CBS continues to provide dollars for imports of essential goods but other than that has allowed market forces to be in control.
    - Part of the reason the CBS has not intervened much is the lack of enough liquidity to pump into the market under war conditions.
  - The pound's slide will continue as long as the CBS FX reserves remain low, especially in the absence of a political or military solution to the conflict on the horizon.

[1] Arabia Monitor; EIU. Figures subject to downward revision.

Tunisia: A snub to the establishment

B2/NR

- **In the first round of presidential elections on 15 September (Tunisia's second since the Arab Spring), two populist candidates received the majority of votes, easily displacing the candidates from three largest parties -- Nidaa Tounes, Ennahda and Tahya Tounes -- in a clear display of voter dissatisfaction.**
  - ➢ Going through to the second round run-off are independent conservative candidate and former law professor Kais Saied and still-jailed media magnate Nabil Karoui of the Qalb Tounes party. Saied led with 18.4% of the vote and Karoui, who denies accusations of tax fraud and money laundering, took 15.6%.
    - The democratic Islamist party Ennahda received 11% of the votes and, on 24 September, backed Saied in the run-off on 13 October.
    - Former Defence Minister Abdelkarim Zbidi, an independent supported by the previously ruling Nidaa Tounes took 10%. Prime Minister Yousef Chahed won only 8% representing his new party Tahya Tounes.
  - ➢ Whoever wins the presidency, the Assembly elections in October are expected to result in the formation of a broad coalition government of largely business-friendly parties, which should encourage the return of foreign investors even though the pace of economic reform could be slow and uneven.
  - ➢ Turnout was 45% compared with the post-Arab Spring election of 2014, when it reached 64%.
- **The first task of the president-elect will be to fix the economy. According to the IMF, Tunisia's growth this year -- driven by tourism and an increase in FDI inflows -- should be 2.7%, a boost from the 2.5% and 1.9% rates of the past two years. This has not been enough to defuse public unrest.**
  - ➢ The tourism sector, which contributes 15% to the country's GDP, has been enjoying an upward trend in performance following a slump caused by terrorists attacks.
    - This year, 9 million tourists are expected to visit the country, a 12.5% increase from last year's record 7.8 million and more than the five-year average of 6.2 million.
  - ➢ Likewise, FDI inflows continue to grow, increasing 15% YoY to 280M in Q1 2019 but comprising only 28% of the government FDI target for this year. Manufacturing (46%) and the energy industry (38%) took the lion's share.

Tunisia Macroeconomic Indicators[1]

	2016	2017	2018	2019e	2020f
Real GDP Growth (%)	1.1	1.9	2.5	2.7	3.2
CPI Inflation (%)	3.6	5.3	7.3	7.5	5.9
Fiscal Balance (% of GDP)	-6.2	-5.9	-4.6	-3.7	-2.8
C/A Balance (% of GDP)	-9.3	-10.2	-11.2	-10.1	-9.1
Total Gov't. Gross Debt (% of GDP)	62.3	70.3	77.0	81.5	82.2
Total Gross Extrn'l Debt (% of GDP)	66.9	81.7	83.1	98.4	107.8
Gross Official Reserves (Mos. of Imports)	3.1	2.7	2.6	3.0	3.3
Nominal GDP (USD B)	41.8	40.0	39.9	36.2	35.1
Population (Millions)	11.4	11.5	11.7	11.8	11.9

    - Tunisia received an average USD 1.2B in FDI inflows in the last ten years, about 10% of the North African total and 3% of the MENA total.
  - ➢ Inflation is projected at 7.5% for this year, an increase from 2018's 7.3% and 2017's 5.3%, brought in by an appreciation in food and transport prices.
    - In February, the Central Bank of Tunisia increased its benchmark interest rate to 7.75% from 6.75% to combat inflation. It has since kept interest rates unchanged.
  - ➢ The government expects its fiscal deficit to decline to 3.7% of GDP this year from 4.6% in 2018. However, wage increases demanded by the powerful General Union of Tunisian Workers (UGTT) and already obtained by many of its members make the target harder to meet.
    - UGTT demands and strikes underscore the dissatisfaction of ordinary Tunisians and will continue to represent a major challenge for the new government when it is eventually formed.

[1] Arabia Monitor; IMF.

UAE: Light at the end of the real estate tunnel

Aa2/NR

- **The latest GDP growth forecast of 2.4% released by the Central Bank of the UAE suggests a more cautious outlook than the IMF projection of 2.8% for this year, supported by public spending as well as external factors.**
  - ➢ The central bank revised its growth forecast for the economy upward from an earlier projection of 2% in May this year.
    - The oil sector is expected to grow by 5% in 2019, compared with 2.8% in 2018, while the non-oil sector will grow by 1.4%, slightly faster than last year.
    - Growth in Q1 2019 stood at 2.2% YoY, supported by the oil sector (4.2% YoY) with non-oil edging up 1.6% YoY.
    - In Q2, growth was also estimated at 2.2% YoY, with non-oil real GDP up 1.5% and the oil sector posting 4%.
    - Economic sentiment improved in Q2 as the Purchasing Managers' Index recorded an average reading of 58.2, its highest quarterly reading since the end of 2014.
  - ➢ By contrast, the IMF, in its April Regional Economic Outlook, had forecast a pickup of 2.8% from 1.7% last year.
  - ➢ Following a big jump in 2018 after the implementation of VAT, inflation is expected to be lower this year, pulled down by weak overall housing and fuel prices, as well an oversupply in the retail and hospitality sectors.
    - Inflation, on an annual basis, fell 1.5% in June, a stronger drop than May's 1.1% fall, driven by lower utility prices.
- **Dubai's real estate sector is showing signs of recovery, but recent reform packages need time to work.**
  - ➢ Data from Real Estate Information & Analytics points to price increases of up to 15% in areas such as Dubai Marina and the nearby tree-shaped Palm Jumeirah island, popular with celebrities.
  - ➢ Residential sales transactions in Dubai in June to August hit a four-year high, according to Property Finder.
    - It noted that 8,833 transactions, together worth USD 3.9B, were recorded during this period.

UAE Macroeconomic Indicators[1]	2016	2017	2018	2019e	2020f
Real GDP Growth (%)	3.0	0.8	1.7	2.8	3.3
Crude Oil Production (M Bpd)	3.0	2.9	3.0	3.1	3.2
Oil GDP Growth (%)	2.6	-3.0	2.6	3.2	1.7
Non-oil GDP Growth (%)	3.2	2.5	1.3	2.7	4.0
CPI Inflation (%)	1.6	2.0	3.1	2.1	2.1
Fiscal Balance (% of GDP)	-2.0	-1.6	-1.8	-0.8	-1.7
C/A Balance (% of GDP)	3.7	6.9	6.6	5.9	5.1
Total Gov't. Gross Debt (% of GDP)	20.2	19.7	18.7	19.2	19.0
Total Gross Extrn'l Debt (% of GDP)	69.6	72.6	68.6	68.7	66.4
Gross Official Reserves (Mos. of Imports)	3.3	3.7	3.8	4.3	4.6
Nominal GDP (USD B)	357.0	382.6	424.6	427.9	449.1
Population (Millions)	9.2	9.4	9.5	9.7	9.8

  - ➢ Dubai's off-plan housing market -- residences before construction -- also clocked sales worth USD 1.9B over summer, 46% higher than in the same period of 2018.
  - ➢ Factors that will support a revival include visa reforms, price corrections, Expo 2020, rent-to-own options and long-term payment plants up to 20 years.
  - ➢ Dubai has also taken recent steps to restructure its real estate regulatory body as well as forming a high-level committee for real estate, with the aim of balancing the market.
    - A new law was passed on 15 September making the Real Estate Regulatory Agency part of the Dubai Land Department (DLD).
    - The DLD will now be in charge of registering rental contracts and regulating the relationship between property owners and tenants.

[1] Arabia Monitor; IMF.

Yemen: Some growth amid the ravages of war

NR/NR

- **Five years into the war in Yemen, any chance of rebuilding the devastated country hangs on a fragile truce, but the chances of peace talks succeeding are far from certain.**
  - ➢ On 21 September, the Houthis said they plan to halt attacks on Saudi Arabia if the latter ceases attacks on Yemen.
    - The announcement -- welcomed by the UN -- followed Saudi-led air strikes against the Houthis in Hodeidah in retaliation for attacks on 14 September on two major oil facilities in Saudi Arabia.
  - ➢ Our baseline scenario is that fighting will continue in many parts of the country, despite the recent truce efforts.
  - ➢ Worst-case scenario: a hardening of positions as fighting between pro-government forces and Houthi rebels escalates, in turn, leaving little room for compromise.
  - ➢ Best-case scenario: the two sides implement confidence-building measures to help facilitate an agreement on Yemen's political transition.
- **In July, the IMF revised its growth forecast for Yemen to a more realistic 2.1% for this year from a 14.7% rebound initially predicted in its April Regional Economic Outlook. The IMF forecast is in line with that of the World Bank and our view.**
  - ➢ After peaking at 41.8% in 2018, inflation is expected to drop to 20%, this year but remains much higher than the 5% posted in 2016.
  - ➢ The Yemeni rial continues to lose its value against the dollar.
    - It now trades at YER 450 per dollar at the benchmark rate set by the Central Bank of Yemen (CBY).
    - This compares with YER 215 riyals to the dollar before the start of the crisis four years ago.
    - It is YER 602 to the dollar on the black market.

Yemen Macroeconomic Indicators[1]	2015	2016	2017	2018	2019e
Real GDP Growth (%)	-16.7	-13.6	-5.9	-2.6	2.1
Crude Oil Production (M bpd)	0.1	0.0	0.0	0.1	0.1
CPI Inflation (%)	12.0	-12.6	24.7	41.8	20.0
Fiscal Balance (% of GDP)	-8.7	-8.9	-4.7	-10.7	-4.5
C/A Balance (% of GDP)	-6.2	-5.1	-4.0	-9.3	-7.4
Total Gov't. Gross Debt (% of GDP)	55.2	68.1	74.5	62.5	48.8
Total Gross Extrn'l Debt (% of GDP)	12.8	15.8	18.0	19.4	15.3
Gross Official Reserves (Mos. of Imports)	2.5	1.4	0.8	0.5	1.0
Nominal GDP (USD B)	45.6	36.4	31.3	28.5	34.3
Population (Millions)	26.9	27.5	28.2	28.9	29.5

    - The CBY reached a deal with the World Bank on 9 September wherein the bank will help improve the CBY's abilities to steady the currency, as well as assist in incentivising the return of foreign investment into the country by offering investment insurances.
      - o The bank plans to launch an electronic network next year that links businesses to money exchange organisations to maintain currency stability.
- **President Mansour Hadi appointed new foreign and finance ministers in a reshuffle on 20 September of his Aden-based and internationally recognised government.**
  - ➢ Former ambassador Mohammed Al-Hadrami was appointed Minister of Foreign Affairs while Salem bin Breik was given the finance portfolio.
  - ➢ A new central bank governor -- Ahmed Obaid Al-Fadhli -- was also appointed.

[1] Arabia Monitor; IMF.
[*] To be revised significantly downwards.

GCC Sovereign Ratings Update

	Moody's		Last Moody's action		S&P		Last S&P action		Rating Change Considerations
	Rating	O/L*	Action	Date	Rating	O/L	Action	Date	
Bahrain	B2		Affirmed O/L Stable	17-Dec-18	B+		Downgraded O/L Stable	01-Dec-17	If Bahrain materially outperforms fiscal and external forecasts, upward pressure on ratings could emerge. Conversely, if these constraints intensify, downward pressure will continue.
Kuwait	Aa2		Affirmed O/L Stable	02-May-19	AA		Affirmed O/L Stable	02-Jul-18	Ratings could be lowered if a renewed fall in oil prices or slow growth were to undermine Kuwait's revenue and fiscal profile or if parliamentary resistance blocks or reverses planned reforms.
Oman	Ba1	(-)	Downgraded O/L (-)	05-Mar-19	BB		Affirmed O/L (-)	19-Apr-19	Ratings could dip if debt as a share of GDP remains on an upward trend or if the net external asset position were to weaken at a faster pace. Signs that succession risks have risen could be perceived as disrupting governance standards or institutional functioning.
Qatar	Aa3		Affirmed O/L Stable	13-Jul-18	AA-		Affirmed O/L Stable	07-Dec-18	Ratings could come under pressure if developments in oil production and prices, or in the banking sector, were to significantly weaken the country's external or fiscal positions; for example, if the government's gross liquid assets fall significantly below 100% of GDP.
Saudi Arabia	A1		Affirmed O/L Stable	01-May-19	A-		Affirmed O/L Stable	30-Mar-19	Ratings could be lowered again if sizable and sustained reductions in the deficit are not achieved, or if liquid fiscal financial assets fell below 100% of GDP. Ratings could also come under pressure if domestic or regional events compromised political and economic stability.
UAE	Aa2		Affirmed O/L Stable	26-Mar-19					Reducing the debt of government-related enterprises of Abu Dhabi banks and of the government of Dubai could support upgrade considerations in the medium term.

Bloomberg; Moody's; S&P; JPMorgan.
*O/L stands for outlook.
Note: Political & institutional factors, rather than just fiscal & economic performances, constrain GCC ratings starting from Moody's Aa & S&P's A categories.

MENA exc. GCC Sovereign Ratings Update

	Moody's		Last Moody's action		S&P		Last S&P action		
	Rating	O/L*	Action	Date	Rating	O/L	Action	Date	Rating change considerations
Algeria	N/R				N/R				Sovereign rating on hold due to domestic and energy market conditions.
Egypt	B2		Affirmed O/L Stable	29-Aug-19	B		Affirmed, O/L Stable	11-May-18	A delay or reversal in implementing fiscal and economic reforms agreed upon under the IMF programme and renewed intensification of political turmoil and instability would be credit-negative.
Jordan	B1		Affirmed O/L Stable	08-Nov-18	B+		Affirmed O/L Stable	16-Mar-19	Successful implementation of key political and structural economic reforms, favouring more sustainable growth and further easing fiscal and external vulnerabilities would support an improvement in the ratings outlook.
Lebanon	Caa1		Downgraded O/L Stable	21-Jan-19	B-	(-)	Affirmed O/L (-)	25-Aug-19	Ratings could be lowered if over the next 12 months economic growth is slower than anticipated, or if the current political upheaval escalates, resulting in domestic conflict or acute risks to institutional stability.
Morocco	Ba1		Affirmed, O/L Stable	20-Nov-18	BBB-	(-)	Affirmed O/L (-)	05-10-18	If higher economic growth were to exceed forecasts, exchange rate flexibility to increase markedly, and Morocco's institutional and governance quality to rise above that of similarly rated peers, this would be supportive of a ratings upgrade.
Tunisia	B2	(-)	Affirmed O/L (-)	16-Oct-18	N/R				Implementing structural reforms agreed under the extended IMF programme, including public bank recapitalisation and governance reform would be credit positive. A sustained fiscal and external rebalancing would also exert upward pressure on ratings.

Bloomberg; Moody's; S&P.
*O/L stands for outlook.

About Arabia Monitor

Arabia Monitor is an independent research firm specialised in economic and market analysis, and strategy advisory on the Middle East and North African region, which it views as the new emerging market. Arabia Monitor's in-depth, locally informed analysis by Arab, Persian and Chinese speakers has placed it consistently ahead of the curve in identifying new trends within and around the region, and understanding its geopolitics.

Arabia Advisors specialises in portfolio strategy and private placements. It works with firms, family offices and government related organisations that are looking to streamline, re-balance or diversify their asset portfolios. Based in the UAE as an off-shore company, Arabia Advisors services a regional and international client base with interest in the Arab countries.

Arabia Monitor
Aston House| Cornwall Avenue| London L3 1LF
Tel +44 203 239 4518
info@arabiamonitor.com
www.arabiamonitor.com