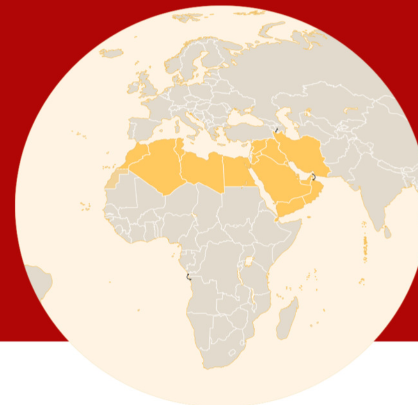
MIDDLE EAST and NORTH AFRICA



Economic activity the Middle East and North Africa is expected to contract by more than 4 percent in 2020, as consumption, exports, and services activity such as tourism are severely disrupted by the COVID-19 pandemic, and in oil exporters, export and fiscal revenues sharply fall with the plunge in oil prices. Fiscal and monetary policy support in response to the pandemic has been swift in large regional economies. Regional growth is expected to resume in 2021 as the impact of the pandemic subsides and investment improves. Risks to the outlook are heavily tilted to the downside and include much more widespread regional COVID-19 outbreaks, prolonged weakness in oil prices and global activity, and intensification of regional conflicts.

Recent developments

Economic conditions in the Middle East and North Africa (MENA) have worsened substantially as a result of the COVID-19 pandemic (Figure 2.4.1.A).[1] The outbreak has been the largest and had an earlier onset in the Islamic Republic of Iran, but other countries are also experiencing rapid increases in infections. The pandemic and the measures taken to stem the pandemic have steeply weakened activity, while increased investor risk aversion has tightened financial conditions. The sharp fall in global oil and export demand is curtailing exports in the region's oil exporters, with adverse spillovers to non-oil sectors (Figure 2.4.1.B). In addition, the region continues to suffer from challenges related to longstanding security strains and refugees, as well as large structural impediments to growth.

Widespread policy measures were implemented to help limit the spread of infection—these include large public events cancellations, air travel restrictions, and schools and government offices closures. Recent relaxations to mitigation measures have been gradual. Large economic stimulus packages have been announced in several major regional economies, including those in the Gulf Cooperation Council (GCC). These packages have included measures on health spending, social assistance, and small business support. Egypt's central bank has cut policy rates by 300 basis points in response to COVID-19 concerns, while central banks with pegs to the U.S. dollar (e.g., GCC) cut rates in tandem with emergency cuts by the U.S. Federal Reserve.

Activity among oil-exporting economies has decelerated across the board. Non-oil activity sharply slowed in large oil exporters (e.g., Saudi Arabia, United Arab Emirates) after the pandemic hit the region (Figure 2.4.1.C). The collapse in global demand due to the pandemic resulted in a steep fall in oil prices (Chapter 4). In an attempt to mitigate this, a new OPEC+ production cut agreement was renegotiated after a temporary collapse in March (Figure 2.4.1.D). Investment is also hindered by high uncertainty associated with pandemic-related disruptions.

Among oil importers, activity is decelerating in both large and small economies for reasons related and unrelated to COVID-19. Tourism prospects in these economies faded as domestic and international pandemic restrictions hold back arrivals and hotel occupancy. Exports have fallen

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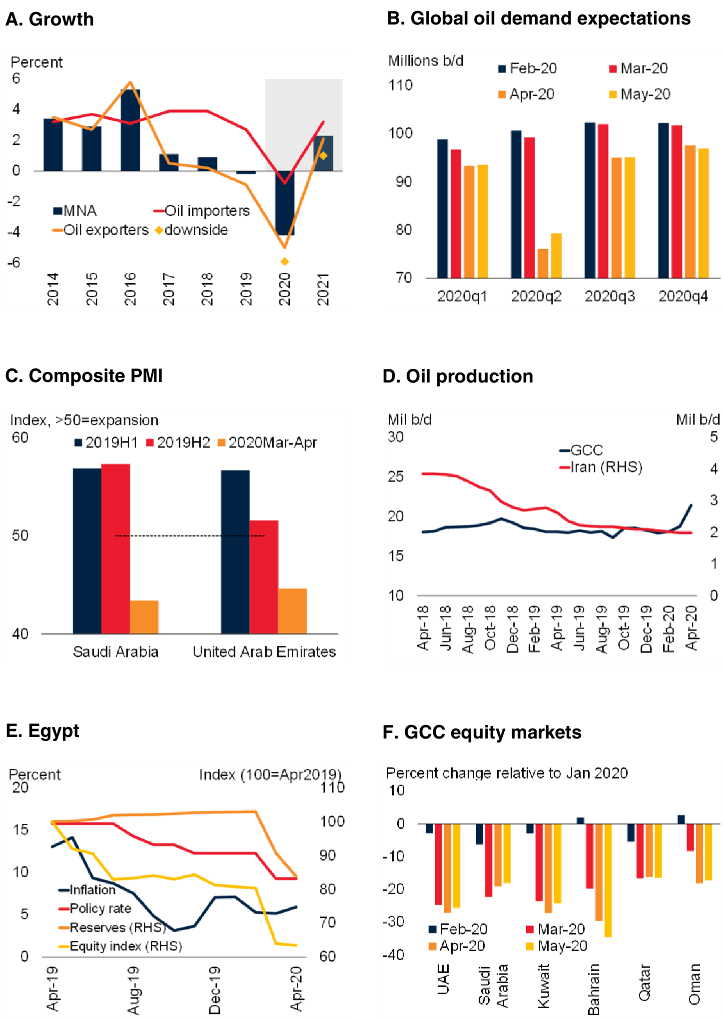
Note: This section was prepared by Lei Sandy Ye. Research assistance was provided by Heqing Zhao.

[1] The World Bank's Middle East and North Africa aggregate includes 16 economies. Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates comprise the Gulf Cooperation Council (GCC); all are oil exporters. Other oil exporters in the region are Algeria, Iran, and Iraq. Oil importers in the region are Djibouti, Egypt, Jordan, Lebanon, Morocco, Tunisia, and West Bank and Gaza. Libya, the Syrian Arab Republic, and Yemen are excluded from regional growth aggregates due to data limitations.

FIGURE 2.4.1 MENA: Recent developments

Regional output is expected to contract by more than 4 percent in 2020 in the face of the COVID-19 pandemic and the plunge in oil prices associated with collapsing global demand. Non-oil activity is decelerating in large GCC economies as pandemic concerns amplify. A new OPEC+ production cut agreement was negotiated to continue recently after earlier uncertainty. Egypt, the largest oil importer, has further cut policy rates in response to COVID-19 concerns amid moderating inflation. The spillovers of the recent global financial turbulence have also reached MENA.



Sources: International Energy Agency, Haver Analytics, World Bank.

A. Weighted average growth rate of real GDP. "downside" refers to downside regional growth scenario in 2020 and 2021.

B. Denotes IEA forecasts for global oil demand. X-axis denotes the forecasted quarter. Legend denotes month-year in which forecast is published.

C. H1 and H2 denote monthly period averages of the first and second half of 2019.

D. Crude oil production. GCC includes 6 economies.

E. Policy rate refers to overnight deposit rate. Inflation refers to year-on-year consumer price inflation. Reserves denote gross official reserves. Equity index denotes the EGY 100 index. Reserves are based on quarterly data.

F. MSCI emerging market share price indexes.

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sharply amid anemic external demand, including from the Euro Area (a major export partner). Domestic policy uncertainty is further weighing heavily on investment activity among smaller oil importers.

Inflation has continued to moderate in MENA. In Egypt, inflation has generally declined over the past year, partly owing to the stability of the exchange rate. In the GCC, inflation has averaged less than 1 percent and it has also been broadly contained in smaller non-GCC economies. Iran's inflation has been falling on a year-by-year basis, although it still remains elevated at about 20 percent. Moderating inflation has allowed monetary policy space for large economies like Egypt to aggressively cut policy rates in response to the pandemic (Figure 2.4.1.E).

The financial sector in MENA has been shaken in recent months by the broad-based erosion of investor sentiment toward EMDEs under the pandemic, leading to sharp falls in equity market indexes and capital outflows in large economies (Figure 2.4.1.F). In response to COVID-19, authorities have introduced financial stability and corporate sector support measures, including zero-interest collateralized banking sector loans in the UAE and measures to support lending to small and medium-sized enterprises in Saudi Arabia.

Outlook

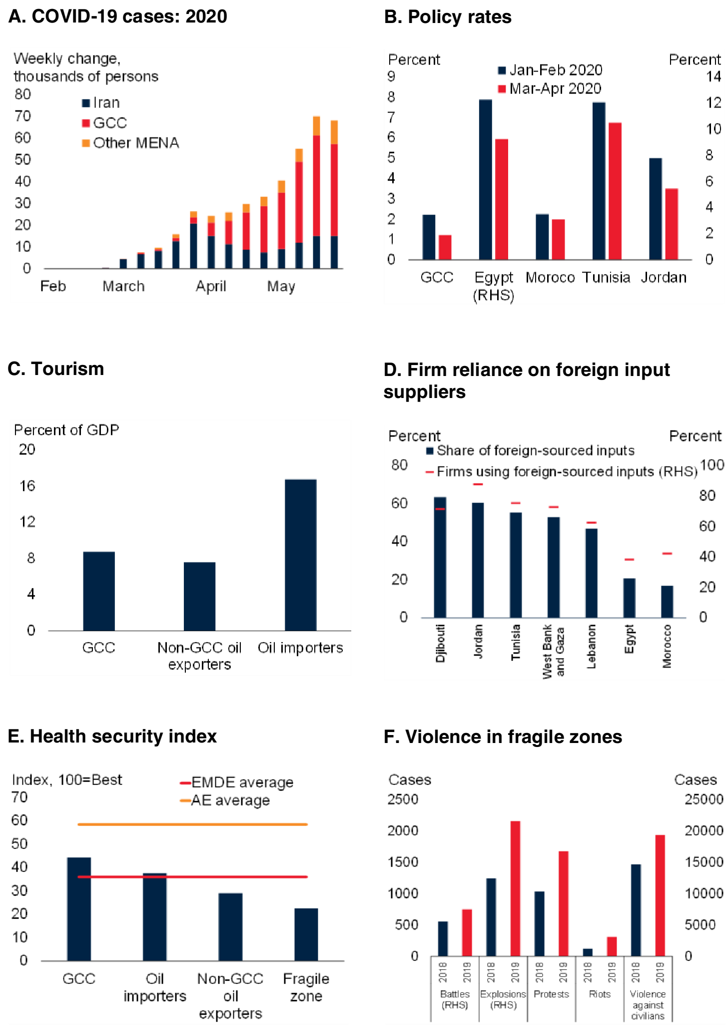
As a consequence of the pandemic and oil market developments, GDP in the region is forecast to contract sharply by 4.2 percent in 2020, although there is substantial uncertainty around this projection (Table 2.4.1). The forecasts have been further downward revised from those in January and April and reflect continued deterioration of the outlook in the global economy recently (Arezki et al. 2020; Chapter 1). Oil exporters suffer from the plunge in oil prices and ongoing domestic outbreaks of the pandemic (Figure 2.4.2.A). Oil importers suffer spillovers from weakness in advanced economies and major EMDEs, pandemic-related disruptions, and falling tourism. Moderating inflation in much of the region has provided room for monetary authorities in some economies to loosen policy rates to mitigate the impact of the pandemic on the real economy (Figure 2.4.2.B). The baseline outlook for the region rests upon the assumptions that the pandemic subsides somewhat later in the year, and that geopolitical tensions do not escalate further.

Among oil exporters, output in 2020 is expected to continue to contract from the previous year, as low oil prices also reduce non-oil activity via income effects. Iran's GDP—which had already fallen in each of the previous two years—is expected to shrink again in 2020, by 5.3 percent, partly reflecting the effects of the large-scale COVID-19 outbreak on domestic consumption and the services sectors (e.g., tourism) (Table 2.4.2). In many oil exporters, growth will be significantly constrained by renewed policy cuts in oil production. In Saudi Arabia and other GCC economies, low oil prices, elevated uncertainty associated with potential further spikes of COVID-19, and household level impacts of initial fiscal adjustments (e.g., VAT increase, payroll restraint) are expected to weigh heavily on non-oil activity. The economies of Algeria and Iraq continue to grapple with the consequences of low oil prices and structural vulnerabilities. Growth in oil exporters is expected to rebound in 2021, as the pandemic subsides and investment recovers, including large infrastructure investment in the GCC. Longer-term diversification programs, the recent relaxation of foreign investment restrictions, and improved regulatory environments should also support the rebound, including a recovery from adverse global spillovers and low confidence.

Among oil importers, output is expected to contract by 0.8 percent in 2020, reflecting a broad-based deceleration (and in many cases contraction) in both large and small economies. Tourism, which had previously been improving and supported by government promotion initiatives, is expected to suffer substantially. Oil importers are reliant on tourism revenues, and arrivals from the Euro Area and other key source areas are expected to fall (Figure 2.4.2.C). Investment and exports are expected to contract amid weak global and domestic confidence and high policy uncertainty. Generally supportive activity in Egypt before late FY2020 (ending in

FIGURE 2.4.2 MENA: Outlook and risks

The outlook in large MENA economies is weighed heavily by the pandemic, although moderate inflation in parts of the region allows some space for additional monetary easing. Oil importers are reliant on tourism activity and are vulnerable to further decline in tourist arrivals and global disruptions. The capacity for an effective response by health systems varies widely, making some large economies unprepared for an intensification of infection rates. Conflict-related risks in fragile economies have not subsided.



Sources: The Armed Conflict Location and Event Data Project, Global Health Security Index, Haver Analytics, World Bank, World Travel and Tourism Council.

A. Based on weekly data. Latest observation is week 4 of May 2020.

B. GCC denotes unweighted average rates of 6 GCC economies. Period averages.

C. Unweighted averages. Based on 2019 data.

D. Based on latest available year of data for each non-GCC economy. Data are based on survey responses for firms in the World Bank Enterprise Surveys. "Share of foreign-sourced inputs" denotes firms' average share of inputs from foreign sources.

E. Based on 2019 edition of Global Health Security Index (best=100). The index assesses countries' health capability and security in six categories: prevention, detection, response, health system, compliance, and risk. Unweighted averages. "Fragile zone" include Iraq, Syria, Libya, and Yemen. "AE" denotes advanced economies

F. "Fragile zone" includes Iraq, Libya, Syria, and Yemen. Y-axis denotes total number of incidents of conflicts of each type that are reported in the dataset.

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June) has been disrupted by the pandemic, while other smaller oil importers grapple with additional shocks to growth (e.g., balance of payments in Lebanon). Firms in smaller oil importers are also expected to suffer from anemic demand and global disruptions, given some reliance on foreign-sourced inputs (Figure 2.4.2.D). Weak financial system balance sheets and high public debt have further compounded the financial stability, growth, and humanitarian challenges faced by the smaller oil importers. Lower oil prices could provide some relief to oil importers' current accounts, but high volatility in oil prices is weighing on investment and confidence, limiting their benefits.

Medium-term growth prospects for the MENA region are contingent upon no amplification of regional conflicts or their spillovers. Continued structural programs in many economies (e.g., Egypt's private sector development, GCC's diversification programs; Youssef et al. 2019) are expected to encourage growth-enhancing structural reforms (e.g., stronger fiscal management framework, water access), and reforms in the financial sector are expected to continue to strengthen the investment climate in the region. But success is contingent upon a sustained commitment to reforms, including by newly formed governments (Mansour et al. 2020).

Risks

Risks to the outlook are heavily tilted to the downside. Thus far, Iran has experienced the largest number of reported COVID-19 cases in the region. Similar outbreaks in other economies could impose broad-based damage to their manufacturing and services sectors. Moreover, widespread infections could exact a humanitarian toll, especially among the fragile economies (e.g., Syria) where forced displacement and insecurity leave populations already highly vulnerable. Many non-GCC economies also are ill-equipped to respond owing to weak fiscal positions and inadequate health systems, leaving them in danger of negative feedbacks between economic activity and health outcomes (Figure 2.4.2.E). Moreover, the adverse impacts of the simultaneous public health and oil shocks are likely to be amplified by structural impediments (e.g., low diversification) and weigh on job creation and long-term growth prospects in the region (Arezki et al. 2020; Baduel, Geginat, Pierre 2019; Jaller, Sophia, Martin 2020). These shocks also increase the difficulty of implementing long-term growth strategies in the region, including those that foster energy sustainability (World Bank 2019d).

Negative spillovers from major trading partners are already significant and could intensify. The Euro Area is an important export destination for economies in the Maghreb region, and China is an important source of trade and investment for some large oil exporters. Larger-than-expected growth spillovers from outside the region could further set back MENA growth prospects via even lower oil demand, weaker foreign direct investment, and weaker intraregional remittance flows (for which oil importers are reliant on the GCC).

The recent sharp decline in oil prices and the continued high uncertainty about their future path also pose an important risk to MENA's short-term outlook. If this uncertainty lingers, business and consumer confidence would be dampened further, undermining efforts by oil importers to reform their energy subsidies and enact fiscal adjustment programs. Persistently low oil prices would also further erode MENA's already weak fiscal space and heavily constrain investment activity in the region, as oil prices and public investment often comove closely in MENA (Albino-War, et al. 2014).

In addition to the effects of the pandemic, conflict-related risks in MENA remain high (Figure 2.4.2.F). Conflicts in Syria and Libya have been complicated by military actions of external parties. The impact of conflict on Libya's oil production could further contribute to volatility in global oil markets. Yemen's peace prospects are heavily clouded by the instability of negotiated agreements among various parties. U.S.-Iran tensions have not eased appreciably even as both countries attempt to cope with the effects of the pandemic.

The pace of reform, especially in smaller oil importers, has been impeded by political challenges recently, including delays in the formation of governments. COVID-19 has further clouded the prospects of reforms, as it adds pressure to shift to non-reform policy priorities in the face of nearer-term pressures. If reform initiatives are not integrated as part of COVID-19 policy responses, further delays could hinder medium and long-term growth prospects in the region via lower rate of job creation and private sector development (Chapter 3).

TABLE 2.4.1 Middle East and North Africa forecast summary

(Real GDP growth at market prices in percent, unless indicated otherwise)

	2017	2018	2019e	2020f	2021f	Percentage point differences from January 2020 projections: 2020f	Percentage point differences from January 2020 projections: 2021f
EMDE MENA, GDP [1]	**1.1**	**0.9**	**-0.2**	**-4.2**	**2.3**	**-6.6**	**-0.4**
GDP per capita (U.S. dollars)	-0.8	-0.9	-1.9	-5.8	0.8	-6.6	-0.3
(Average including countries with full national accounts and balance of payments data only)[2]							
EMDE MENA, GDP [2]	1.4	0.9	-0.6	-3.8	2.3	-6.1	-0.4
PPP GDP	1.7	1.0	-0.7	-3.5	2.4	-5.9	-0.5
Private consumption	2.7	0.6	0.5	-1.8	1.6	-3.7	-0.6
Public consumption	5.0	3.6	-0.5	0.0	1.7	-2.1	-0.6
Fixed investment	2.1	1.2	3.0	-2.0	4.1	-7.2	-1.6
Exports, GNFS [3]	5.9	2.5	-5.4	-6.9	3.1	-9.9	-0.5
Imports, GNFS [3]	9.1	-2.1	-3.3	-3.5	2.5	-6.9	-1.5
Net exports, contribution to growth	-0.5	2.2	-1.6	-2.1	0.5	-2.4	0.1
Memo items: GDP							
Oil exporters [4]	0.5	0.2	-0.9	-5.0	2.1	-7.0	-0.2
GCC countries [5]	-0.4	2.0	0.6	-4.1	2.2	-6.3	-0.4
Saudi Arabia	-0.7	2.4	0.3	-3.8	2.5	-5.7	0.3
Iran	3.8	-4.7	-8.2	-5.3	2.1	-5.3	1.1
Oil importers [6]	3.9	3.9	2.7	-0.8	3.2	-5.2	-1.4
Egypt [7]	4.2	5.3	5.6	3.0	2.1	-2.8	-3.9

Source: World Bank.

Note: e = estimate; f = forecast. EMDE = emerging market and developing economies. World Bank forecasts are frequently updated based on new information and changing (global) circumstances. Consequently, projections presented here may differ from those contained in other Bank documents, even if basic assessments of countries' prospects do not differ at any given moment in time.

1. GDP and expenditure components are measured in 2010 prices and market exchange rates. Excludes Libya, Syria, and Yemen due to data limitations.
2. Aggregate includes all countries in notes 4 and 6 except Djibouti, Iraq, Qatar, and West Bank and Gaza, for which data limitations prevent the forecasting of GDP components.
3. Exports and imports of goods and non-factor services (GNFS).
4. Oil exporters include Algeria, Bahrain, Iran, Iraq, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates.
5. The Gulf Cooperation Council (GCC) includes Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates.
6. Oil importers include Djibouti, Egypt, Jordan, Lebanon, Morocco, Tunisia, and West Bank and Gaza.
7. Data for Egypt corresponds to the fiscal year. The fiscal year runs from July 1 to June 30 in Egypt; the column labeled 2018 reflects the fiscal year ended June 30, 2018.

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TABLE 2.4.2 Middle East and North Africa economy forecasts[1]

(Real GDP growth at market prices in percent, unless indicated otherwise)

	2017	2018	2019e	2020f	2021f	Percentage point differences from January 2020 projections: 2020f	2021f
Algeria	1.3	1.4	0.8	-6.4	1.9	-8.3	-0.3
Bahrain	4.3	1.8	1.8	-4.5	2.3	-6.6	-0.1
Djibouti	5.4	8.4	7.5	1.3	9.2	-6.2	1.2
Egypt[2]	4.2	5.3	5.6	3.0	2.1	-2.8	-3.9
Iran	3.8	-4.7	-8.2	-5.3	2.1	-5.3	1.1
Iraq	-2.5	-0.6	4.4	-9.7	1.9	-14.8	-0.8
Jordan	2.1	1.9	2.0	-3.5	2.0	-5.7	-0.4
Kuwait	-4.7	1.2	0.4	-5.4	1.1	-7.6	-0.9
Lebanon	0.9	-1.9	-5.6	-10.9	-6.3	-11.2	-6.7
Morocco	4.2	3.0	2.3	-4.0	3.4	-7.5	-0.2
Oman	0.3	1.8	0.5	-4.0	2.0	-7.7	-2.3
Qatar	1.6	1.5	-0.3	-3.5	3.6	-5.0	0.4
Saudi Arabia	-0.7	2.4	0.3	-3.8	2.5	-5.7	0.3
Tunisia	1.9	2.7	1.0	-4.0	4.2	-6.2	1.6
United Arab Emirates	0.5	1.7	1.7	-4.5	1.4	-7.1	-1.6
West Bank and Gaza	1.4	1.2	0.9	-7.6	5.1	-10.1	2.5

Source: World Bank.

Note: e = estimate; f = forecast. World Bank forecasts are frequently updated based on new information and changing (global) circumstances. Consequently, projections presented here may differ from those contained in other Bank documents, even if basic assessments of economies' prospects do not significantly differ at any given moment in time.

1. GDP and expenditure components are measured in 2010 prices and market exchange rates. Excludes Libya, Syria, and Yemen due to data limitations.

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