BAHRAIN

Table 1	2020
Population, million	1.7
GDP, current US$ billion	33.3
GDP per capita, current US$	19589.5
School enrollment, primary (% gross)[a]	98.0
Life expectancy at birth, years[a]	77.2

Source: WDI, Macro Poverty Outlook, and official data.
Notes:
(a) WDI for School enrollment (2019); Life expectancy (2018).

Significant disruptions related to COVID-19 compounded by sharp fall in oil prices weighed heavily on Bahrain's economy in 2020. Fiscal and external deficits worsened, reversing the narrowing path observed in 2019. Widespread access to the vaccine, higher oil prices, and commitment to implement policies under the Fiscal Balance Program, particularly those pertaining to tackling budget rigidities and providing fiscal support to the most vulnerable, will improve the outlook. Downside risks arise from further resurgence of COVID-19 outbreaks, volatility in hydrocarbon prices, and delays in fiscal reforms.

Key conditions and challenges

The COVID-19 crisis and ensuing oil price slump have highlighted the vulnerability of the country's over-reliance on oil exports for non-oil growth and fiscal revenues. Even prior to the pandemic, lower oil prices since 2014 have generated sizable fiscal and external imbalances and resulted in large financing needs and borrowing costs. The authorities responded by announcing Fiscal Balance Program (FBP) in 2018 supported by US$10 billion commitment from GCC peers, which aims to achieve a balanced budget by 2022. While fiscal reforms under the FBP helped to narrow the fiscal deficit prior to COVID-19, protracted low oil prices and large off-budgetary spending kept the fiscal deficit over 9 percent of GDP in 2019. Lingering fiscal deficits led to rapid debt accumulation that exceeded 100 percent of the GDP in 2019 and is expected to rise in the coming years with sizable gross financing needs.

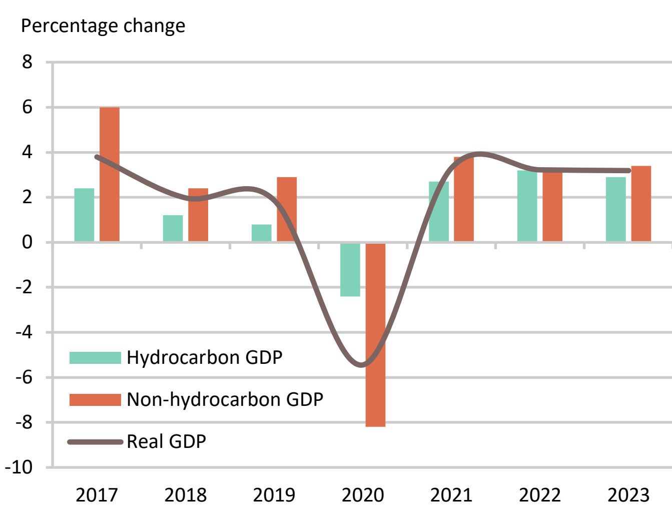
This difficult macro-fiscal situation was significantly worsened by the hit of lower oil prices and the health and economic fallout of COVID-19. The government responded quickly to deliver liquidity support to sectors and households affected by lockdowns and more recently with brisk access to vaccination to limit the spread of the virus. However, the fiscal and monetary stimulus package of headline size over BHD4.5 billion (36 percent of GDP) introduced cumulatively in March and July 2020 to mitigate the impact of the pandemic put additional pressure on an already precarious fiscal position, and will make the pre-pandemic FBP targets more difficult to achieve on time.

The shocks underscore the importance of accelerating key reforms envisaged under FBP, including reduction of the twin deficits to ensure debt sustainability and ease pressures on reserves. Meanwhile, reforms to address the weak fiscal position and lift the growth will be challenging given the government's generous subsidy system amidst limited financial resources, large public debt and bulky gross financing needs. While Bahrain is rapidly rolling out vaccines, the services-based non-oil sector will face a balancing act between resumption of travel and containment of the virus, especially new variants. The dynamism in diversification has come from Bahrain's footholds in global innovator services and labor-intensive tradable services, but these are areas in which other countries are putting considerable effort and comparative advantage can be eroded quickly.

Recent developments

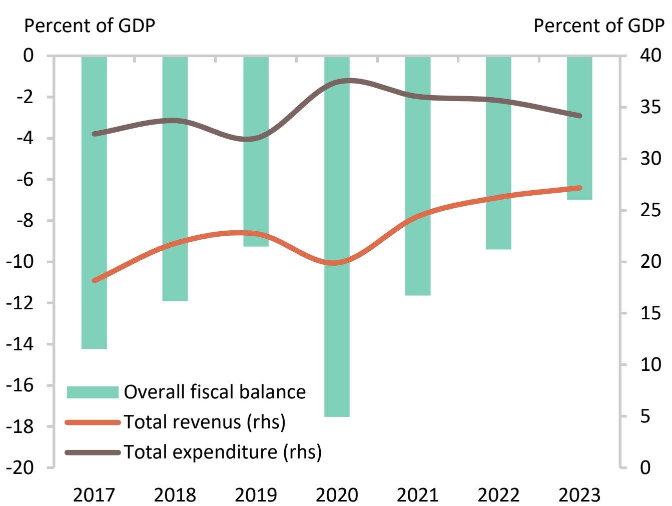
Faced with this multifarious crisis, the economy is estimated to have contracted by 5.4 percent in 2020 weighed down by sharp 8 percent (y/y) contraction in non-oil economy, mainly that related to the all-important services and tourism. Oil GDP saw a 2.0 percent decline as oil production remained capped by the OPEC+ cut agreement.

FIGURE 1 Bahrain / Real annual GDP growth



Sources: Bahrain authorities, World Bank; and IMF staff projections.

FIGURE 2 Bahrain / General government operations



Sources: Bahrain authorities, World Bank; and IMF staff projections.

Weak consumer demand led to 2.6 percent (y/y) deflation in 2020.

The unprecedented fiscal and monetary mitigation measures introduced to lessen the fallout brought by COVID-19, along with the sharp plunge in oil prices and the concomitant constrained oil production capacity have rapidly widened the overall fiscal deficit to over 17 percent of GDP, reversing the narrowing path observed in 2019. The public debt-to-GDP ratio is estimated to have reached 133 percent in 2020, reflecting the highly strained fiscal position; financing needs are correspondingly sizable.

The current account deficit is estimated to have worsened from 2.1 percent of GDP in 2019 to more than 9 percent of GDP in 2020 primarily due to a sharp decline in oil exports, which accounts for over 55 percent of total exports (2019). Foreign reserves are estimated to have declined to almost 1.4 months of non-oil imports at end-2020.

Poverty data is sparse. The most recent labor data available for Bahrain corresponds to the second quarter of 2019. According to the Labor Market Regulatory Authority (LMRA), foreign workers accounted for 80 percent of the country's total employment. The number of employed Bahrainis had been falling prior to the pandemic (2019 Q2 compared to 2018). Similarly, median monthly wages among Bahrainis fell 1.1 percent between the second quarter of 2018 and 2019.

Outlook

The outlook for Bahrain's hinges on the uncertainty related to the pandemic, the effectiveness of the vaccine, evolution of global oil markets and the reforms process. Economic growth is expected to gradually rebound to 3.3 percent in 2021, underpinned by the rebound in non-oil activity as rapid rollout of the vaccine will boost the sectors most impacted by the pandemic. Growth is projected to remain modest at an average of 3 percent over the medium term as fiscal austerity measures will act as a headwind to post-pandemic catch-up.

In the absence of structural reforms, the fiscal deficit is projected to remain sizable at 11 percent of GDP in 2021 amidst modest recovery in oil prices. In the aftermath of the pandemic, steadfast fiscal reforms and better-targeted subsidies under the FBP, accompanied with development of new oil and gas resources will gradually narrow the fiscal deficit. However, debt to -GDP ratio is expected to increase to over 133 percent in 2021, and to remain elevated in the forecast period implying still large financing needs. Large current account deficits are likely to persist in 2021-23 albeit at slightly moderated levels thanks of modest oil price gains.

Key risks to the outlook arise from the possibility of recurring COVID-19 outbreaks that could force retightening of containment measures and harm the non-oil growth prospects. A further downturn in hydrocarbon prices (e.g. if global supply gets too far ahead of demand recovery) will limit fiscal space to absorb further shocks.

The COVID-19 pandemic and the measures to mitigate the outbreak had a negative impact in sectors such as tourism and services, that are important sources of employment and diversification. The recovery of the labor market will depend on the speed of the rollout of the vaccine not only domestically but, in the case of tourism, in Saudi Arabia and other large markets that are traditional sources of business and leisure travel to Bahrain. These countries are also augmenting their homegrown portfolio of services sectors that increasingly compete with Bahrain.

TABLE 2 Bahrain / Macro poverty outlook indicators (annual percent change unless indicated otherwise)

	2018	2019	2020 e	2021 f	2022 f	2023 f
Real GDP growth, at constant market prices	2.0	1.9	-5.4	3.3	3.2	3.2
Private Consumption	1.4	-1.0	-4.0	3.9	2.9	2.7
Government Consumption	1.8	-1.5	6.5	3.3	1.4	1.2
Gross Fixed Capital Investment	9.5	1.4	-6.8	2.3	4.4	4.5
Exports, Goods and Services	3.3	0.4	-10.4	5.0	5.5	5.7
Imports, Goods and Services	5.7	-5.5	-10.0	6.0	4.2	3.4
Real GDP growth, at constant factor prices	2.0	1.9	-5.4	3.3	3.2	3.2
Agriculture	3.8	-1.0	0.8	1.5	1.6	1.5
Industry	0.2	2.3	-4.8	2.5	3.0	3.7
Services	3.3	1.6	-5.9	3.8	3.4	2.8
Inflation (Consumer Price Index)	2.1	1.0	-2.6	2.5	2.3	2.2
Current Account Balance (% of GDP)	-6.6	-2.2	-9.6	-6.9	-4.6	-3.5
Net Foreign Direct Investment (% of GDP)	3.7	3.0	1.1	1.3	1.9	2.6
Fiscal Balance (% of GDP)	-11.9	-9.3	-17.6	-11.7	-9.4	-7.0
Primary Balance (% of GDP)	-7.5	-4.8	-12.6	-6.9	-4.7	-2.6

Source: World Bank, Poverty & Equity and Macroeconomics, Trade & Investment Global Practices.
Notes: e = estimate. f = forecast.