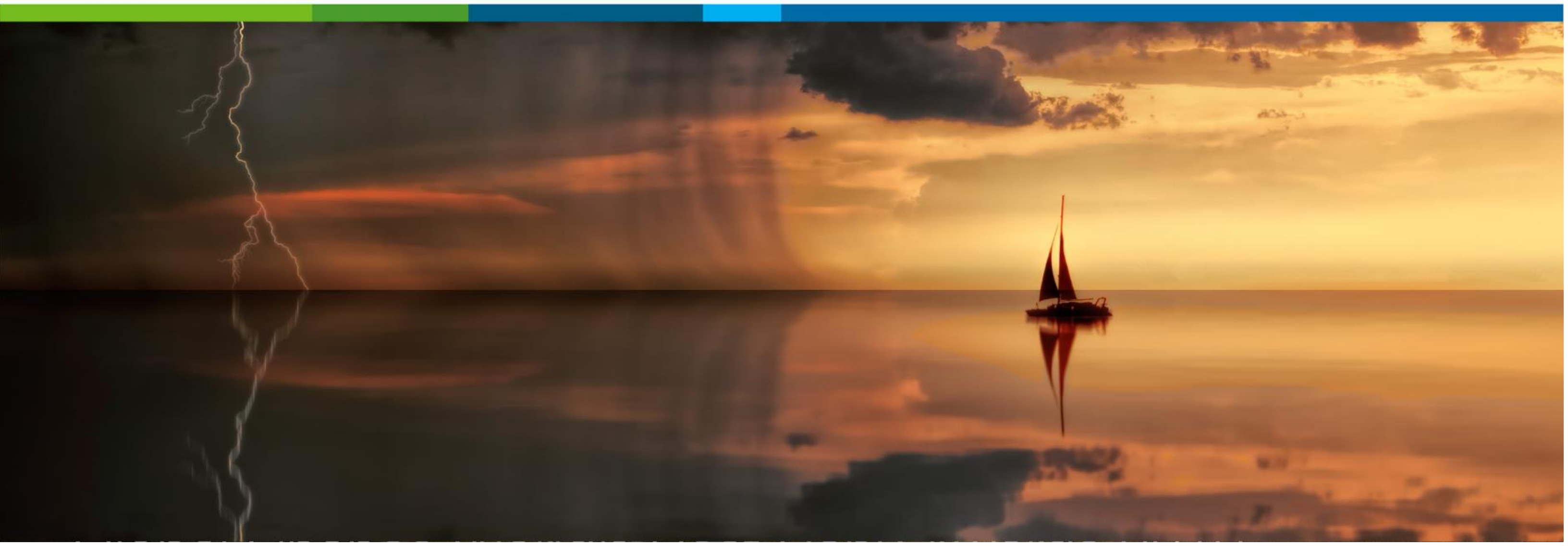

Middle East, North Africa and Pakistan: batten down the hatches

The 2020 global recession will impact the Middle East, North Africa and Pakistan (MENAP) region via the oil market, global trade, tourism and capital flows. We have lowered our MENAP GDP growth forecast for this year to 2.5 per cent from 3.4 per cent.

Travel restrictions and quarantines could deal a material blow to growth and foreign exchange earnings in the second quarter of the year.

For the GCC countries (Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the UAE), we expect significantly weaker non-oil activity in 2020. Major oil-importing economies (such as Egypt and Pakistan) which rely on private domestic demand to drive growth will be hard hit by virus-related disruptions and quarantines in the second quarter.

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GCC – back to the future

Hydrocarbon production is set to boost headline growth in some GCC countries, even as non-oil growth weakens. We now expect the price of Brent crude oil to average just USD35/bbl in 2020 (we previously expected USD64/bbl). While the current surge in oil production (if sustained through 2020) is likely to prop up GDP growth in some GCC countries, notably Saudi Arabia, this is the result of higher oil production rather than underlying economic activity.

Egypt and Pakistan which rely on private domestic demand to drive growth will be hard hit by virus-related disruptions and quarantines in the second quarter.

Major events such as the Expo 2020 in the UAE are likely to be delayed. GCC authorities have outlined targeted fiscal and monetary stimulus packages. However, the decline in global oil prices significantly limits the government's ability to scale up spending.

All GCC sovereigns entered this oil-market downturn with significantly higher public debt and weaker external buffers than in 2014. In addition to fiscal deficits, we expect most GCC countries to run current account deficits in 2020.

Oil importers – balancing act

Beyond COVID-19's direct disruption to economic activity, the hit to trade, travel and tourism could have a multiplier effect on economic activity in many of the region's markets. Central banks in Egypt, Turkey and Pakistan have responded with rate cuts and targeted financial support, including deferred payments for bank customers and concessional financing for the health-care sector.

While additional rate cuts are likely in 2020, central banks will have to balance measures to support growth against the likely financial-market reaction, particularly in currency markets, in our view.

Costlier financing, weaker foreign exchange earnings could pressure exchange rates and fiscal deficits may widen: we expect the Egyptian pound and Pakistani rupee to weaken in 2020.

IMF financing is likely to play a bigger role in helping to fight the crisis in the coming months. The IMF recently approved a new programme for Jordan, and Pakistan has requested assistance under the IMF's Rapid Financing Instrument.

Within the GCC, we detail the impact of COVID-19 on some key markets:

Saudi Arabia – oil surge

We expect headline GDP growth to accelerate to 5.0 per cent in 2020, reflecting plans to significantly increase Saudi oil production. We expect hydrocarbon GDP to expand more than 16 per cent, and the non-oil economy to contract by over 3 per cent on coronavirus-related disruptions and the hit to consumer and investor sentiment from weaker oil prices. The uncertain outlook for the annual Hajj pilgrimage – should travel restrictions remain in place – poses additional downside risks to non-oil growth.

We expect a fiscal deficit of 11.6 per cent of GDP in 2020, which could reduce if there is a potential interim agreement to lower oil output (supporting prices); bigger spending cuts; dividend payments or further divestment of state assets.

The current account is likely to swing to a deficit in 2020 at 3.3 per cent of GDP. We lower our end-2020 forecast for the repo rate (the rate at which the central bank lends to commercial banks) to 1 per cent (from 2.25 per cent) to reflect recent rate cuts in response to moves by the US Federal Reserve but expect the Saudi Arabian Monetary Authority to stay on old for the rest of the year.

The UAE – choppy waters

The UAE is likely to see a decline in economic activity, which will be masked by higher oil production to take GDP higher by 1.4 per cent in 2020. The COVID-19 outbreak and ensuing global recession is likely to exacerbate economic difficulties of the two biggest economies – Abu Dhabi and Dubai. Imports and outwards remittances will be slowed, taking the current account surplus forecast from 1.3 per cent to 2.6 per cent. The non-oil economy is vulnerable to a recession.

Policy approach

The federal and emirate governments have announced fiscal stimulus packages: the federal government has announced an AED16 billion package to mitigate the economic impact of the coronavirus. This is in addition to measures announced at the emirate level. Dubai has announced a stimulus package worth AED1.5 billion that includes cutting fees to lower the cost of doing business. Abu Dhabi's plans include specific measures to support SMEs and lower utility bills for citizens, as part of its already-announced AED50 billion, three-year 'Tomorrow 2021' package.

The Central Bank of the UAE (CBUAE) has announced a financial relief packages and lowered interest rates, announcing a 'Targeted Economic Support Scheme' (TESS) totalling AED100 billion (approx. USD27 billion) to contain the impact of the pandemic on the real economy and preserve financial stability. TESS will provide AED50 billion of collateralised loans at zero cost to banks and free up an additional AED50 billion of funds from banks' capital buffers. The CBUAE recently announced additional measures to improve liquidity in the banking system, in order to provide relief to borrowers and the real economy.