



EU - Gulf Cooperation Council (GCC) Dialogue on Economic Diversification

EU – GCC Dialogue on Economic Diversification Gulf Cooperation Council (GCC) countries

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Global and Regional Prospects and Policy Actions for Post-Pandemic Recovery

Briefing on International Monetary Fund (IMF) World Economic Outlook (WEO) - Recovery During a Pandemic, 2021, IMF WEO Update 2022, IMF Regional Economic Outlook Middle East and Central Asia 2021

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1 Purpose

This briefing on the International Monetary Fund (IMF) World Economic Outlook (WEO) 2021 and the update published by IMF WEO Update in January 2022, and the IMF Regional Economic Outlook for Middle East and Central Asia 2021, includes the global prospects related to economic growth and inflation, as well as IMF recommended policy actions for post-pandemic recovery, with specific recommendations for Middle Eastern countries.

In addition, the briefing provides visual representations created by the EU-GCC Dialogue on Economic Diversification project for Gross Domestic Product (GDP), exports and imports, pre-COVID-19 and forecasts to 2026 based on the IMF WEO data.

2 Global and Regional Prospects – Economic Growth and Inflation

- The global economy enters 2022 in a weaker position than expected. Rising energy prices and supply disruptions have resulted in higher and more broad-based inflation than anticipated, notably in the United States and many emerging market and developing economies. The ongoing retrenchment of China's real estate sector and slower-than-expected recovery of private consumption also have limited growth prospects.

- Inflation is expected to remain elevated in the near term, averaging 3.9 percent in advanced economies and 5.9 percent in emerging market and developing economies in 2022, before subsiding in 2023. Assuming medium-term inflation expectations remain well-anchored, and the pandemic eases its grip, higher inflation should fade as supply chain disruptions ease, monetary policy tightens, and demand rebalances away from goods-intensive consumption towards services.

- The rapid increase in fuel prices is also expected to moderate during 2022–23, which will help contain headline inflation.

- Futures markets indicate oil prices will rise about 12 percent and natural gas prices about 58 percent in 2022 (both considerably lower than the increases seen in 2021) before retreating in 2023 as supply-demand imbalances recede further.

- Food prices are expected to increase at a more moderate pace of about 4.5 percent in 2022 and decline in 2023.

- In many countries, nominal wage growth remains contained despite employment and participation returning almost to pre-pandemic levels. However, in the United States, a sharp decline in unemployment has been accompanied by buoyant nominal wage growth. This suggests a degree of tightening in US labor markets not evident elsewhere.

- Less accommodative monetary policy in the United States is expected to prompt tighter global financial conditions, putting pressure on emerging market and developing economy currencies. Higher interest rates will also make borrowing more expensive worldwide, straining public finances.

- For countries with high foreign currency debt, the combination of tighter financial conditions, exchange rate depreciations, and higher imported inflation will lead to challenging monetary and fiscal



policy trade-offs. Although fiscal consolidation is anticipated in many emerging market and developing economies in 2022, high post-pandemic debt burdens will be an ongoing challenge for years to come.

According to the IMF Regional Economic Outlook for Middle East and Central Asia 2021, in the Middle East region, over the medium term, GDP levels are expected to remain below those implied by pre-pandemic projections, partly reflecting some lasting damage from the crisis through high unemployment, slower capital accumulation, and weak productivity, among other factors. The amount of scarring (persistent effects on the economy) is expected to be the largest for tourism-dependent countries and smallest for oil exporters, in line with global trends.

The Middle East region remains vulnerable to a rapid rise in US bond yields. Further rapid increases in US rates could lead to tighter global financial conditions, renewed capital outflows, and higher sovereign spreads. Although comfortable reserve levels provide support for the region's emerging markets, vulnerabilities for countries with elevated external debt and limited fiscal space are higher.

3 Gross Domestic Product (GDP) and Trade Forecasts for the GCC countries

This section provides the GDP and trade volumes pre-COVID-19, during the crisis, and the forecasts for GDP growth, imports and exports for each of the GCC countries to 2026.

Note for following charts:

- Annual percentages of constant price GDP are year-on-year changes; the base year is country-specific.
- Percent change of volume of imports/exports of goods refers to the aggregate change in the quantities of imports/exports of goods whose characteristics are unchanged. The goods and their prices are held constant, therefore changes are due to changes in quantities only.
- 2018 to 2020 values are actual, 2021 to 2026 are forecasted.



Bahrain



Figure 1 Bahrain GDP growth, percent change

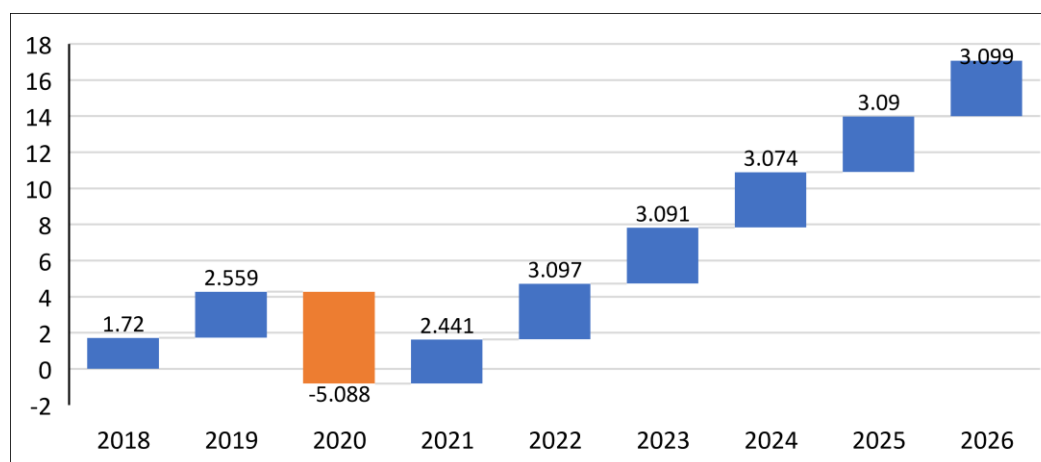
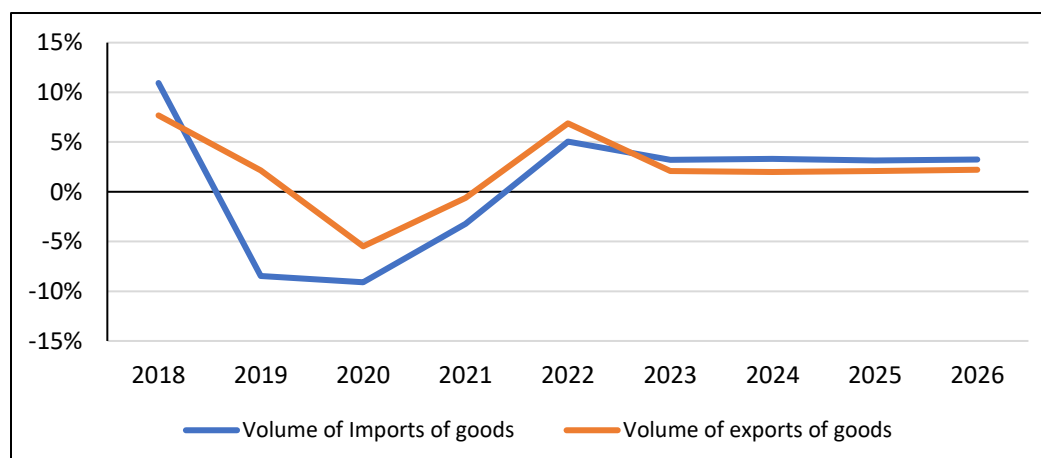


Figure 2 Bahrain volumes of imports and exports, percent change



Source: Author's charts, based on IMF World Economic Outlook data



Kuwait



Figure 3 Kuwait GDP growth, percent change

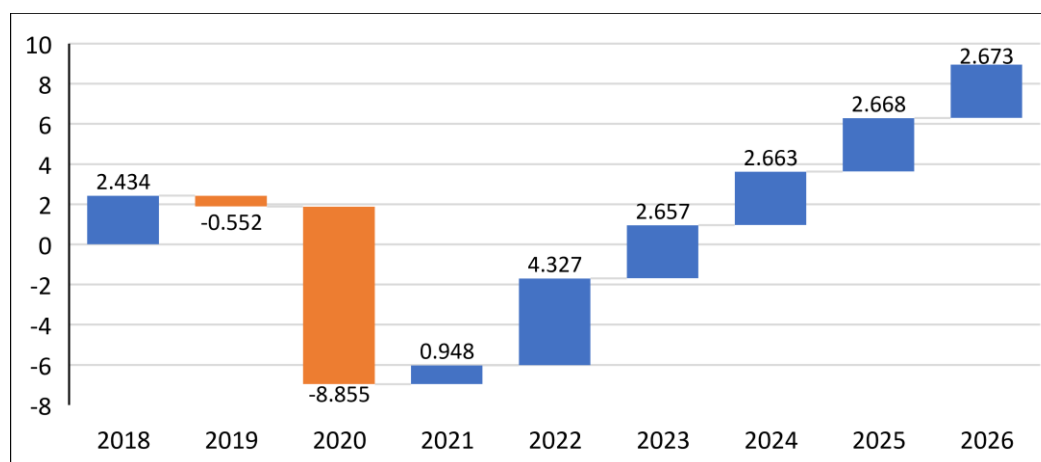
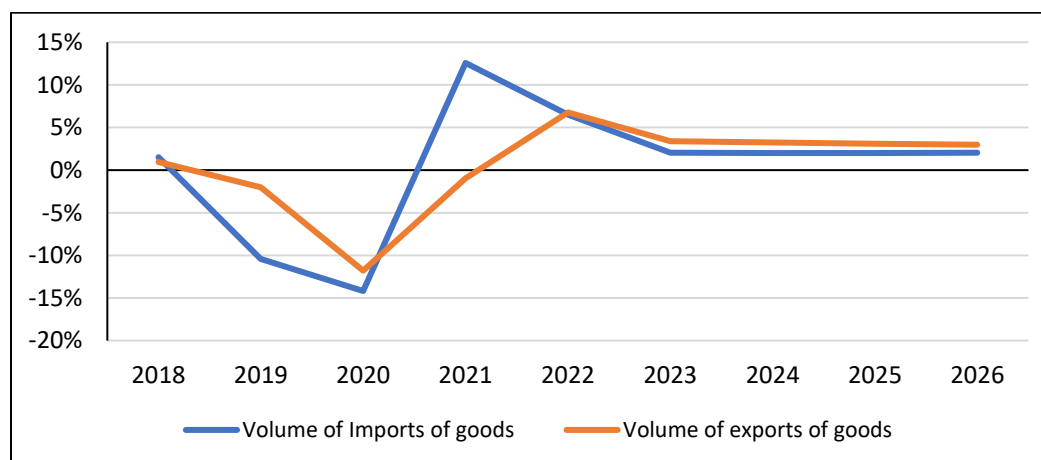


Figure 4 Kuwait volumes of imports and exports, percent change



Source: Author's charts, based on IMF World Economic Outlook data



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Oman



Figure 5 Oman GDP growth, percent change

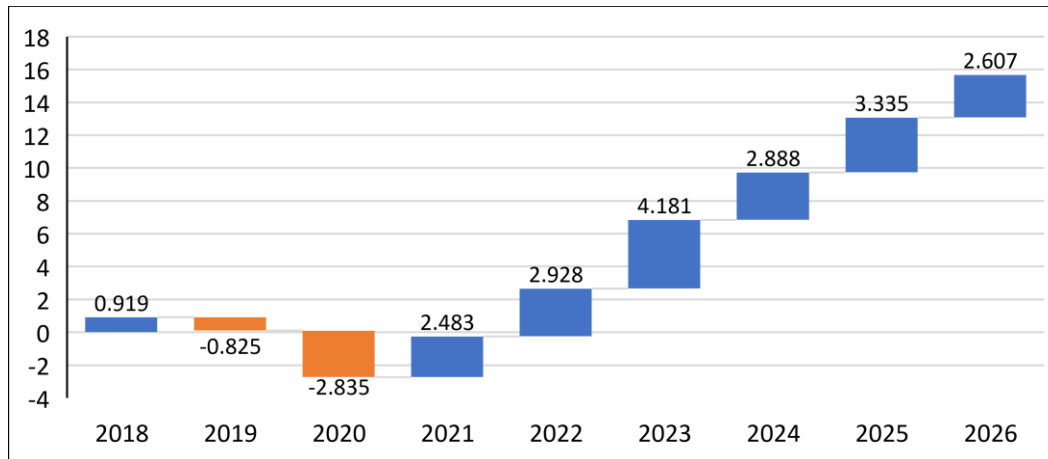
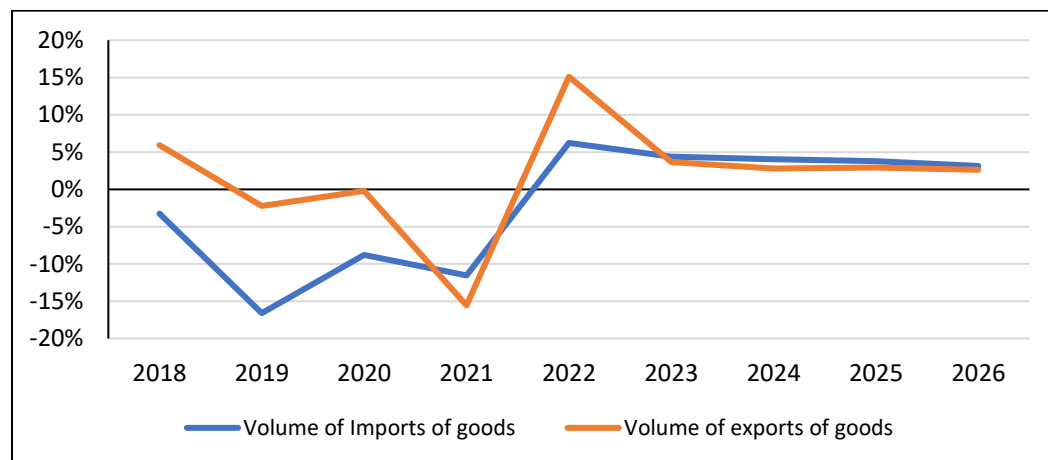


Figure 6 Oman volumes of imports and exports, percent change



Source: Author's charts, based on IMF World Economic Outlook data



Qatar



Figure 7 Qatar GDP growth, percent change

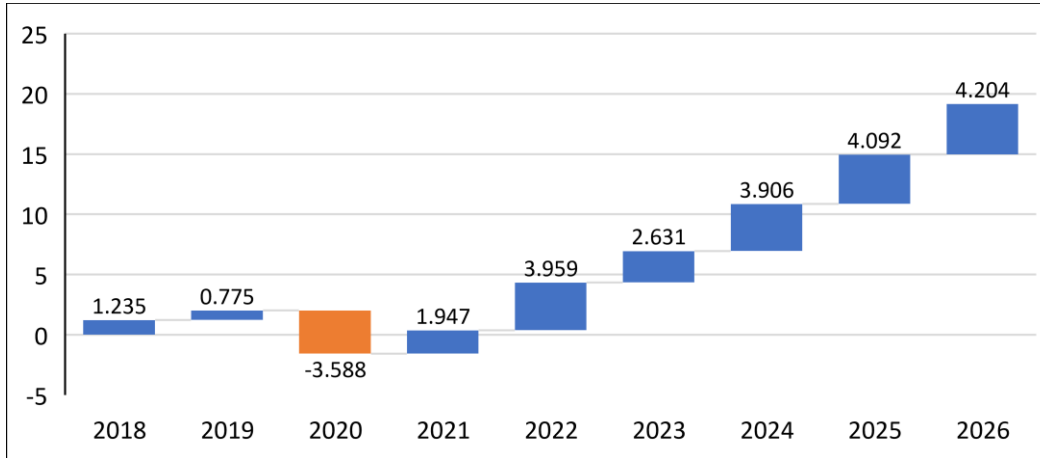
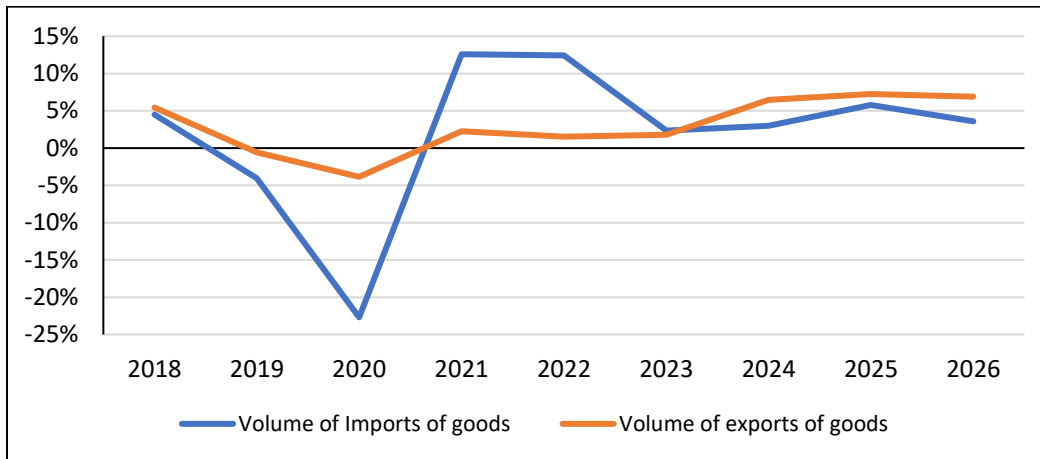


Figure 8 Qatar volumes of imports and exports, percent change



Source: Author's charts, based on IMF World Economic Outlook data



Saudi Arabia



Figure 9 Saudi Arabia GDP growth, percent change

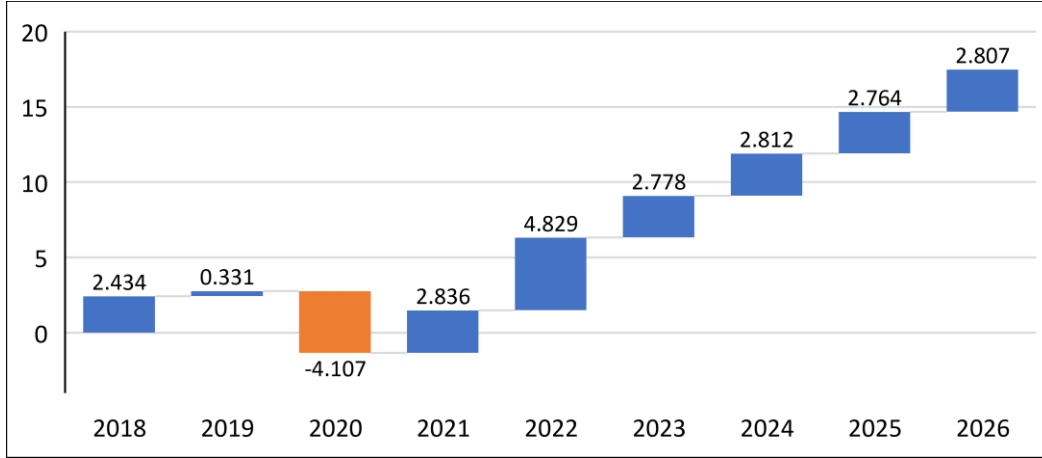
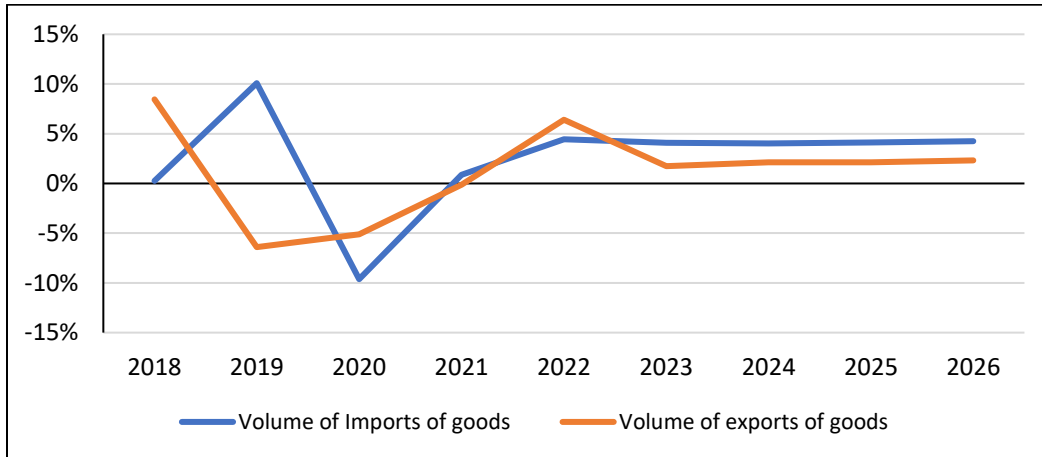


Figure 10 Saudi Arabia volumes of imports and exports, percent change



Source: Author's charts, based on IMF World Economic Outlook data



United Arab Emirates



Figure 11 United Arab Emirates GDP growth, percent change

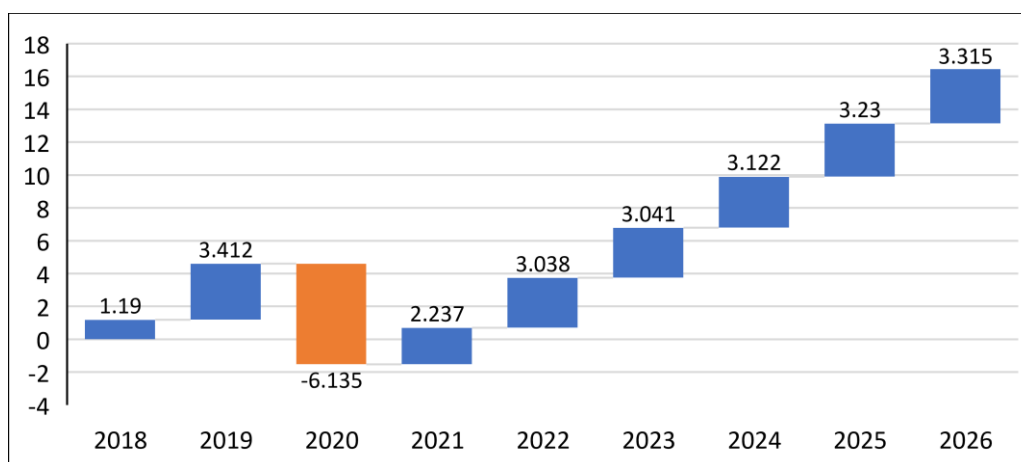
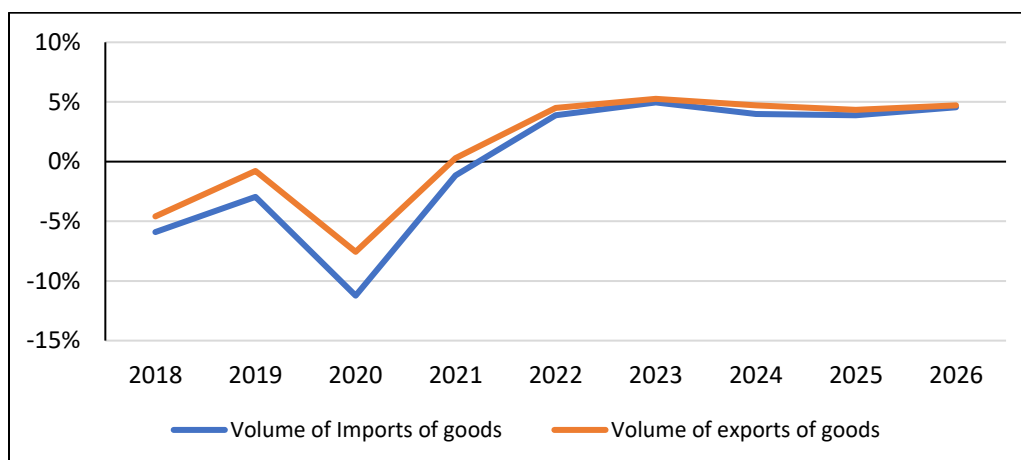


Figure 12 United Arab Emirates volumes of imports and exports, percent change



Source: Author's charts, based on IMF World Economic Outlook data



4 Policy Actions to Strengthen the Recovery

4.1 Multilateral Actions with Positive Spillovers

- **Accelerating global vaccine deployment** - would save millions of lives by reducing risks of severe health outcomes and deaths, lower the risks of new variants emerging, and thereby add trillions of dollars to the global economic recovery.
- **Mitigating and adapting to climate change** – reduce greenhouse gas emissions through emission control schemes and by implementing aggregate policy measures such as taxes linked to environmental policy objectives (e.g., carbon tax¹)
- **Easing financial constraints** of struggling countries and tackling debt vulnerabilities, to assist countries that entered the pandemic with already-limited fiscal space.
- **Defusing trade and technology tensions** and instituting an international minimum corporate tax.

4.2 National-Level Policies Adjusted to Pandemic Conditions and Policy Space Constraints

- **A policy approach tailored to a country's pandemic and economic conditions:**
 - The priority must remain critical health care spending.
 - The longer the pandemic persists, resources will also need to be increasingly devoted to worker retraining and support for reallocation away from sectors struggling to regain pre-pandemic vitality.
 - Governments could take the opportunity to advance long-term goals and improve the economy's potential and resilience. Health metrics can help policymakers recognize how and when to adapt policies.
- **Recognizing the constraints by country: near-term macroeconomic policies should aim for the maximum level of employment** without compromising the credibility of policymaking institutions while ensuring fiscal sustainability and financial stability. Near-term policies should be designed to work seamlessly alongside measures to promote longer-term objectives of stronger fiscal policies and monetary policy.
- **Financial sector policies and resolution frameworks:** measures to support credit and stabilize balance sheets—including credit guarantees, debt moratoria, and release of capital and liquidity buffers—should become more targeted. Support can be focused, for example, on smaller but viable banks and firms in sectors where the recovery is lagging because of ongoing health-related concerns.

¹ Under a carbon tax, the government sets a price that emitters must pay for each ton of greenhouse gas they emit.



- **Preparing for a possible tightening of external financial conditions:** emerging market and developing economies should prepare for a possible increase in advanced economy interest rates through debt maturity extensions where feasible.

4.3 Preparing and Investing for the Longer-Term, Post-Pandemic Economy

- **Facilitating new growth opportunities by greening the economy and through digitalization:** a green investment push would aid the transition to a cleaner economy while catalyzing new growth opportunities, for example, in the construction and energy sectors. Moreover, investing in broadband to improve access to the internet can help bridge the digital divide.
- **Reversing the setback to human capital accumulation:** the pandemic-induced global loss of learning from temporary school closures could have long-lasting effects on individual earnings and aggregate productivity growth. To reverse the setback to human capital accumulation and long-term potential, policymakers may need to try a variety of strategies:
 - greater time in school over the next few years
 - additional teacher training on methods to aid catch-up
 - expansion of extracurricular tutoring programs
 - educational and vocational programs may need to be adapted to evolving post-pandemic labor demand, with digital technologies becoming a feature of more jobs and greater anticipated employment needs in sectors requiring more specialized skills (such as health care)
- **Reducing inequality:** design and implement policies to improve educational achievement, and spending measures that can improve the resilience of individuals and households and lower inequality.

Due to climate change challenges, there is an urgent need to identify policy priorities for adaptation and invest in climate-resilient infrastructure in the Middle East region. The region's oil exporters face the additional challenge of making the transition away from oil dependence as the world progressively shifts away from fossil fuels. Rebuilding financial buffers and pursuing economic and fiscal diversification while ameliorating any negative distributional impact on households, are key policy priorities in this regard. The current juncture provides an opportunity to leverage recovery programs, public spending, and regulations to help mitigate the impact of climate shocks. The green transition could provide important employment and investment opportunities for the region.



5 Research and Innovation: Fighting the Pandemic and Boosting Long-Term Growth

IMF World Economic Output report 2021 **explores whether public policy should support basic scientific research to boost growth during the exit from the global pandemic.**

The difference between the two types of research – basic and applied - is that the former is undirected, theoretical, or experimental, whereas the latter is aimed at bringing products to market.

The study finds that:

- **Basic scientific research is a key driver of innovation and productivity**, and basic scientific knowledge diffuses internationally farther than applied knowledge. A 10 percent increase in domestic (foreign) basic research is estimated to raise productivity by about 0.3 (0.6) percent, on average. International knowledge spillovers are more important for innovation in emerging markets and developing economies than in advanced economies. Easy technology transfer, collaboration, and the free flow of ideas across borders should be key priorities.
- **A decoupling of basic scientific research between the United States and China could have big negative effects on global productivity**, with an estimated first-round decline of up to 0.8 percent.
- **Basic scientific research in advanced economies is underfunded.** As a result, policies that fund public research and subsidize private research will have positive payoffs. A model estimated on three advanced economies suggests that subsidy rates for private research should be approximately doubled and public research expenditure increased by about one-third. Targeting support to basic scientific research will deliver the greatest return but, where this is not possible, more public-private partnerships may be a partial substitute.

In conclusion, investment in basic science boosts productivity and pays for itself over the long term.

The benefits of basic research are diffuse and long-lasting, making it an unattractive proposition for private firms. This creates an opportunity for policy intervention. Based on the above-mentioned study, doubling subsidies to private research and boosting public research expenditure by one-third could increase annual growth per capita by around 0.2 percent.

Better targeting of subsidies and closer public-private cooperation could boost this further, at lower public expense. Such investments could start to pay for themselves within a decade or so. Scientific knowledge travels far over time and distance and that it is a key driver of innovation in both advanced economies and emerging markets.

Beyond its impact on growth, basic science is likely to be a key contributor to a greener future. The fight against climate change requires drastic cuts in global emissions. New clean technologies will be central to this effort. Evidence suggests that investment in frontier science—especially in natural sciences and engineering—could help speed the transition toward a cleaner economy.



Recommended policy actions:

- Public funding for research is too low. Gains can be made from both subsidizing more private research and doing more public research.
- The ability to discriminate among various types of research is very valuable. If possible, governments could achieve similar outcomes to the baseline at roughly half the cost.
- Better connections between public and private researchers might be able to substitute for targeted subsidies, which can be hard to implement.
- Regarding firms' ability to protect their discoveries, if basic research spillovers decline, then the social gains from research will fall. This suggests that reducing overbearing market power or excessively broad patenting can boost productivity and growth.



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