Focus on Middle East: Economic Perspective

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Chairman Roh, Distinguished Panelist Members, Colleagues, Participants, Ladies and Gentlemen.

Good Morning:

It is a pleasure to be here with you along with other colleagues, to update you on economic developments in the Middle East in the past year. More specifically on economic challenges and opportunities faced by the nation states of the Middle East.

The Middle East is a diverse region and consists of 20 countries, namely, Algeria, Bahrain, Iran, Iraq, Kuwait, Libya, Oman, Qatar, Saudi Arabia, The United Arab Emirates, Yemen, Egypt, Jordan, Lebanon, Mauritania, Morocco, Somalia, Sudan, Syria, and Tunisia. They constitute over 7% of the global population and over 6% of global GDP. Some countries in this region are oil exporters and others are oil importers. The region still suffers from full integration into the global economy.

While the global economy is rebuilding from the global financial crisis of 2007-2008, economies in the Middle East region have been slow to recover. Global growth improved from 3.2% in 2016 to 3.6% in 2017 (Real GDP), while the cumulative Middle East growth slowed from 5% in 2016 to 2.6% in 2017. Among the reasons for the subdued growth included the recent drop in oil prices and combined regional conflict. The oil exporters in the region were largely responsible for the slow growth, considering that they constitute for a majority of the percentage of the overall economy.

While the growth in oil importing economies improved from 3.6% in 2016 to 4.5% in 2017, growth declined from 5.6% to 1.7% respectively in oil exporting economies (IMF, 2018).
As I stated above, this group of economies were hit hard by the recent drop in oil prices.

The lack of sector diversification within those group made the decline in growth inevitable, because their heavy reliance on oil exportation.

A price drop in oil meant the the producers made less profit and their reduction in profit meant the producers had less incentive and less financial means, to produce. Furthermore, this decline in production meant that the prominent business sector in the economies generated less revenue, and thus growth followed this downward trend.

The combined geopolitical conflict in the region was and still is another cause for subdued recovery as many countries dedicated their factors of production to engage in warfare production, there are less economic resources available for production. The decline in production meant that the business sector in the economies generated less revenue thus growth followed a downward trend.

This year however, marks a turning point for the Middle Eastern economies as these countries as a result of surge in oil prices, strong demand generated exterrnally and reforms initiated by many are expanding at a stronger pace of 2.8% to 2.9% in the first quarter of 2018 to a sluggish growth of 1.1-1.2% in the last quarter of 2017.
It is projected that the growth will surpass 3.3% per year.

The factors that led to stronger growth can be attributed to:

1. An increase in oil prices ($67 per barrel in 2018) which has come about as a result of curtailment in oil supply and the output gap agreed and implemented by OPEC and Russia. In addition, the political conflict between the U.S and Iran are also contributing to the rise in oil prices. It is clear that oil exporting countries will be the beneficiary of the higher oil prices, while the oil-importing nations economic growth situation will deteriorate.
2. Reinstatement of sanction against Iran by the U.S will exacerbate the current conflict situation and add high degree of uncertainty to the region and will affect oil prices. Furthermore, Federal election in Iraq delivered a parliament that will be controlled by Shiite Clerk whose position against U.S presence in Iraq is well known as well as his position against Suunis. Election in Lebanon likewise indicated that Hezbollah and its allies which are backed by Iran garnered a majority in parliament. This could have multiple regional ramifications. (Israel has indicated that a future military, intervention against Lebanon is a possibility).
3. Strong external demand and strong global growth are also contributing to robust growth in this area, especially in China, India and Europe.
4. One of the biggest contributing factor to the improved growth was the implementation of business climate reforms in these economies. Measures were taken to ensure that entry into the busies markets were eased which , in turn, promoted competitivness and benefits for many.

However, political environment remains challenging and continue to pose a downward risk to higher growth, the wars in Syria and Yemen, the battle in Iraq, the tension between Saudi and Iran, the Qatar blockade, the political crisis in Libya could all contribute to downward pressure on growth.

To overcome some of these challenges, that exist in the region, these countries should embark on reforms:

- Transition to a more eco-friendly energies to achieve economic diversification which is crucial to developing a sustainable economy. Saudi Arabia move to build a $200 Billion dollar solar power is a good example of how this project could triple electricity generation capacity in that country.(Saudi Arabia)
- Improve business, investment and regulatory environment. Remove the barriers to entry to starting or closing a business High minimum capital requirements should be relaxed. For example, recent reforms in Egypt in the area of industrial licensing law and bankruptcy has resulted in higher investment.
- Greater trade and emphasis on trade both within the region and in the world economy, will be essential to increase growth. That is, liberating tariffs and non-tariff barriers internally and ask for reciprocal agreement with EU on reducing their high tariffs, quota restrictions and farm subsidies.
- Another major constraint on economic growth is lack of access to finance. Expand access to finance by developing and strengthening alternative to bank financing (only 10% of firms use banks to finance investment), strengthening competition in the financial actor and improve the financial infrastructure.
- Labor Market, jobs and eduction: Youth unemployment ranges from 18 to 30% in Egypt, Jordan, Morroco and Tunis, and women have difficult time finding employment. The labor force is inadequately educated and do not process technical skills. Schools should be reformed so that it is aligned better with the need of private employers, Government should reduce disincentives to hiring , while still protecting the workers and design policies that promote youth and female employment.
- Tax Reform, an implementation of a broad-based tax system that generates the necessary resources is essential to economic growth. Implementation of 5% VAT by Saudi and a sweeping anti-corruption crackdown generated more than $100billion for the Saudi government. UAE also implemented VAT in January 2018. As a result , growth initially slowed down during the first quarter but it has picked up momentum in the second quarter.
- Target subsidy to the poor. Offer subsidy to people who really need them.

Conclusion:

As stated above, most oil producing countries will see a slight increase in growth this year as the prices of oil will surge upward. Oil importing countries will be he beneficiary of improved growth as a result of implementation of business climate reform. Both oil-exporting and importing countries will achieve sustainable growth if reforms are implemented in diversify their economy, improve business investment and regulating environment, emphasis on trade, education and jobs, access to capital, tax and subsidies reforms. All of these reforms could bring stability in the Middle East and can boost the global economy too.

There are still risk factors that needs to be considered, however, that is the growth trajectory will continue as predicted as long as conflict ceases and oil prices continue its upward trends. Rising conflict would likely slow investment and oil prices volatility could undermine all the reforms outlined above.