Impact of COVID-19 and OIL Market Shocks on the Economies of the GCC

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The pandemic & oil price volatility further strengthened the links between the public sector, the financial sector, and the real economy

1. The twin shocks of the pandemic and oil price collapse and government responses
2. The 2021 economic recovery in 2021 and oil price surge
3. Oil market supply shock of the Ukraine crisis and policy choices
4. Current oil price rally and the eventual energy transitions to a decarbonized world

The impact of the VOVID-19 and the oil price collapse

1. The pandemic's impact on the global economy and mobility caused 9% collapse in oil demand, impacting its production, exports and prices.
2. GCC fiscal and external deficits increased to 8.8% and 0.4% of GDP. Oil, non-oil and overall GDP contracted.
3. Policies had to balance fiscal expansion, declining oil revenues, and increasing public debt with the post 2015 fiscal, economic, financial, regulatory and labor market reforms.
4. Early lockdowns, widespread access to vaccines, improved quality of health services, and digital transformation and relatively low share of public debt in GDP helped the recovery from the pandemic
5. Enacted fiscal measures: increasing spending (especially on health and IT services) social transfers, extension and increasing subsidies, wage and unemployment support, concessionary loans, etc.
6. The COVID-19 related fiscal measures were relatively low (2.3% of GDP), reflect the large size of government spending to GDP, the concentration of working nationals in the public sector and the departure of expatriate workers, which indirectly helped labor markets to adjust.
7. Range of macro-financial targeted support measures: central banks eased financial conditions through lower interest rates and liquidity injections, loan payment deferrals, and relaxed prudential requirements on banks capital buffers and liquidity ratios.
8. Non-oil primary balances as a percent of non-oil GDP deteriorated reaching 30-38% of non-oil GDP, reflecting fiscal support measures and a contraction of non-oil economic activity

The recovery in 2021 benefited from oil market rally

- After the decline in 2020, crude oil prices rose by 70% in 2021, oil production, revenues and GDP start rising so did non-oil GDP
- Countries with larger shares of contact-intensive sectors in non-oil GDP (34-36%) such as Bahrain, Qatar, UAE experienced slower non-oil recoveries in 2021 compared to Saudi Arabia and Oman (26-28%).
- The banking system entered the COVID-19 with ample capital and liquidity buffers. Banks' total assets reached 180% of GCC GDP, at the end of 2020, up from 102% of GDP in 2013
- Inflation was relatively mild during and after the pandemic, due to the currencies' peg and the insulation of domestic energy markets from the global, which contributed to the quick recovery.
- Equity prices returned to near historically high levels, boosted by strong corporate earnings and the inclusion of GCC countries in major emerging market indices. Meanwhile, housing prices surged to record highs, supported by low borrowing costs and favourable environment.
- Policies had to balance the gradual phasing out of pandemic related support measures, enhancing non-oil revenues, rationalizing current spending and ensuring efficiency of capital spending.

Impact of the 2022 Russian-Ukraine crisis

- As oil demand recovery was underway, the Russian-Ukraine crisis caused further oil price escalation by 32% which might last longer with four transmission channels into the GCC economies: real oil market, fiscal, financial and monetary

- The supply induced crisis will pose few policy dilemmas and trade-offs:

  1. **The oil market trade-offs** between the short and medium-term responses to supply shortages by increasing investments in the upstream, midstream and downstream oil and gas to meet demand, and the long-term responses to the global energy transition away from fossil fuels.
  2. **Fiscal trade-offs**: use the increase in oil revenues to support public balance sheets and improve macroeconomic outlook on the one hand while avoiding the customary pro-cyclical fiscal policies on the other.
  3. **Economic Policies trade-offs:** Strengthening fiscal, monetary, and macroprudential frameworks induced by oil price swings and the rising global inflation, while reducing reliance on oil through economic and export diversification, building human capital, promoting competition, improving governance, and reducing distorting subsidies.

Policy conclusions

- **Fiscal policy** of oil exporting countries of MENA should aim to ensure long-term fiscal and external sustainability: strengthening fiscal frameworks, mobilizing non-oil revenues, increasing spending efficiency, reduce debt burdens, avoid past patterns of procyclical policies, use extra revenues to rebuild policy space, and enact credible medium-term fiscal frameworks and public outreach
- **Ensuring financial stability** and a dynamic financial sector: strengthening the insolvency and resolution frameworks and stepping up supervisory efforts.
- **Promote sustainable economic growth** to create jobs, enhance competitiveness and diversification especially in the context of a decarbonized world by incorporating the different scenarios, emissions and oil price paths into the macroeconomic and investment strategies and being part of the global framework to address climate change
- **Leveraging technology**, deepening regional integration, enhancing regulatory frameworks
- **Addressing labor market distortions**: raising female labor force participation, increasing work flexibility for expatriates, narrowing the expatriates/nationals wage gap, and improving education quality.