

# Mid. East & N. Africa

## GDF 2003 Summary



### Global themes

- Global growth is projected to accelerate steadily from 1.7% in 2002 to 2.3% in 2003 and 3.2% in 2004. Importantly, this view incorporates the effect of a relatively quick military conflict in Iraq. While very much a recovery, the expansion now underway is quite subdued by historic standards, especially given the sizeable stimulus from policy.
- The past few years has seen a fundamental shift in the pattern of private sector financing for developing countries, away from debt flows to equity-related FDI flows. The drop in debt finance has been partly driven by lower demand on the part of many developing countries seeking to lessen their vulnerability to swings in volatile debt finance, as well as a reduced supply of debt from banks and bondholders. The rise in FDI reflects greater optimism about globalization, the spread of FDI in services and heavy privatization.
- While this rotation from debt to equity should continue, the signs are that the low point in the current private debt cycle came in 2002Q3, and that net debt flows to developing countries are likely to turn positive again in 2003 for the first time in three years. While most likely, the overall buoyancy of FDI flows should not be taken for granted, however. Flows are already off their peak; privatization-related revenues have fallen sharply; and FDI in telecom and other areas of infrastructure has slumped. Moreover, rates of return on both FDI and in the corporate sectors of developing countries have generally fallen in recent years.
- Workers remittances have become an increasingly important component of global development finance, having risen to \$80 billion in 2002. They have some very attractive financial features. They are more stable than private debt flows and are less concentrated in the major middle-income countries than FDI flows.
- Aid flows to developing countries probably rose in 2002 and will continue to do so in 2003 and beyond, in line with the commitments made at the Monterrey Conference in March 2002. Emergency financial support (e.g. IMF) is likely to fall in 2003, on the presumption that no new major debt crises are in the offing. In between, official non-concessional lending (which includes the IBRD) is generally quite weak. Note that net IBRD lending was -\$4.1 billion in 2002 and is on track for an even larger decline in 2003.

### Regional themes

- The military intervention in Iraq represents the latest in a series of shocks to the region in recent years. Regional growth fell to 2.3 percent in 2002, from 3.2 percent in 2001. Diversified exporters (in the Maghreb, and Mashreq) experienced a sharp economic slowdown in 2002 as a result of lower export prices and lagging demand in the European market, plus the substantial negative shock to tourism linked to the September 11<sup>th</sup> attacks. Growth for this group halved from 4.3 percent in 2001 to 2.2 percent in 2002. For oil exporters, lower OPEC quotas were offset by marginally higher prices, and GDP growth remained virtually unchanged in 2002.

- Current projections for both oil producers and diversified exporters are for a modest pick up in economic growth to a range of 3.4 percent to 4 percent per year over the 2003-05 period, as exports rise and higher incomes stimulate domestic spending. There are, however, three main downward risks to this outlook: (i) the possibility that the pace of domestic reforms may slow down in the aftermath of the conflict, as governments find it difficult to address the more controversial structural reforms that are critical for raising productivity and promoting diversification; (ii) the persistence of a negative investor outlook toward the region, causing difficulties in attracting FDI and other forms of capital flows; and (iii) that the war itself lasts longer than is currently envisaged.
- Capital flows to the MENA region have traditionally been modest, with FDI flows estimated to be in the order of \$2 billion to \$3 billion per year in recent years, and net private debt inflows of \$2.9 billion and \$2.8 billion in 2001 and 2002, respectively. One implication of this modest scale of private capital flows has been that the region has been less exposed to sharp volatility and associated currency and financial crises.
- The MENA region is both an important source and an significant destination of workers' remittances. Saudi Arabia, Kuwait, Oman and Bahrain have in recent years been important sources of remittances to other developing countries, including to other countries in the MENA region. Countries receiving large remittance flows include: Morocco (\$3.3 billion), Egypt (\$2.9 billion), Lebanon (\$2.3 billion), Jordan (\$2 billion) and Yemen (\$ 1.5 billion). In 2002, the region received \$14 billion in remittances (2.2% of GDP), ranking third among regions, behind Latin America (\$25 billion), and South Asia (\$16 billion).
- The outlook for workers remittances for MENA recipient countries depends importantly on the path of oil prices. Remittance payments from Saudi Arabia rose during the oil boom years of the 1970s and early 1980s but declined in the mid-1980s as oil prices fell, the budget deficit mounted, and the government put limits on hiring foreign workers. Until the early 1990s, Saudi Arabia was the largest source of remittance payments in the world and is currently the largest source of capital on a per capita basis.

### **Other key regional points to note**

- An important threat to sustained FDI flows is the erosion of investor confidence in a market plagued by low investment returns in recent years. By region, measured returns on FDI were lowest were in the MENA region.
- There is some evidence that remittances have been increasingly used for investment purposes in developing countries, particularly in low-income countries; for instance, in Egypt, a large proportion of returning migrants in the late 1980s established their own enterprises using funds earned abroad. Given the geopolitical risks of war and conflicts, developing countries in the MENA region who provide workers to countries such as Kuwait and Saudi Arabia are likely to experience declines in remittance flows, e.g. remittance flows to Jordan and Yemen from Kuwait and Saudi Arabia declined during the Gulf War.
- The potential for larger private capital flows to the region in the future was highlighted by recent successful sovereign bond issues by Qatar, Bahrain, Iran, and Egypt. These have helped to broaden the region's investor base and have established benchmarks for the corporate sector to tap the market with greater confidence and market recognition.

Table A.5 Middle East and North Africa outlook in summary, 1981–2003

<b>Real economy</b> (percent change, unless stated)	1981–90	1991–00	1997	1998	1999	2000	2001	2002e	2003f
Real GDP growth	2.4	3.2	2.7	3.2	2.0	4.3	3.2	2.6	3.7
Private consumption per capita	1.5	0.2	-0.2	1.2	0.1	1.1	5.1	1.0	1.0
GDP per capita	-0.6	1.0	0.7	1.3	0.1	2.3	1.3	0.7	1.7
Population	3.1	2.2	2.0	2.0	1.9	2.0	1.9	1.9	1.9
Gross domestic investment/GDP <sup>a</sup>	26.7	21.2	21.1	21.5	21.5	21.4	21.5	21.9	22.2
Inflation <sup>b</sup>	8.4	6.4	5.0	0.1	5.7	7.7	3.3	3.8	4.0
Central government budget balance/GDP	-3.9	-0.9	-0.4	-2.5	-1.1	0.5	-0.9	-2.2	-2.2
Export market growth <sup>c</sup>	5.3	10.0	6.9	2.0	8.4	13.2	-1.1	2.3	7.9
Export volume <sup>d</sup>	0.7	5.0	2.6	-1.8	3.4	7.6	3.6	1.4	4.6
Terms of trade/GDP <sup>e</sup>	-0.9	0.5	-0.9	-5.1	5.4	8.7	-1.9	0.0	-2.3
Current account/GDP	-1.7	-2.0	0.5	-5.8	0.8	7.4	5.0	4.5	1.7
Workers remittances (billions of dollars)	—	—	9.4	10.3	10.5	10.9	12.1	14.7	—
<b>Memorandum items</b>									
GDP growth: oil exporters	1.0	2.8	2.4	1.2	-0.2	3.7	2.2	2.3	3.7
Diversified exporters	4.3	3.9	3.0	5.6	3.8	3.6	4.1	2.5	3.1
<b>External Financing and Debt</b> (billions of dollars unless stated)									
	1995	1996	1997	1998	1999	2000	2001	2002e	2003f
Net inward FDI	-0.6	0.7	6.2	7.5	3.2	2.5	5.5	3.0	3.0
Net inward portfolio equity flows	0.1	0.5	0.8	0.3	0.7	0.2	-0.1	0.0	-1.0
Net inward debt flows	2.7	-2.5	-4.4	8.3	-2.2	-6.5	1.7	-0.3	2.5
From public sources	-1.5	-0.8	-4.0	-1.7	-2.7	-2.9	-1.2	-1.6	0.0
From private sources	4.2	-1.7	-0.4	10.0	0.5	-3.6	2.9	1.3	2.5
Gross market-based capital inflows	11.3	4.5	18.7	12.1	13.6	8.9	12.1	14.7	16.0
Total external debt	212	204	195	210	214	202	201	—	—
Medium- and long-term	167	162	154	164	163	156	153	—	—
Short-term	45	42	41	46	50	47	47	—	—
Owed by public-sector borrowers	162	156	147	155	157	149	146	—	—
Owed by private-sector borrowers	50	48	48	55	57	53	55	—	—
Owed to public-sector creditors	118	117	109	112	107	101	98	—	—
Owed to private-sector creditors	94	87	86	98	106	101	102	—	—
Gross foreign exchange reserves	44.9	56.4	63.0	61.6	64.2	76.5	85.2	90.2	90.2

— Not available.

Note: e = estimate, f = forecast.

a. Fixed investment, measured in real terms.

b. Local currency GDP deflator, median.

c. Weighted average growth of import demand in export markets.

d. Goods and non-factor services.

e. Change in terms of trade, measured as a percentage of GDP.

Table A.26 External financing: Middle East and North Africa, 1997–2003

(billions of dollars)

	1997	1998	1999	2000	2001	2002e	2003f
Current account balance	2.3	-27.8	4.2	40.8	28.9	24.7	9.5
as a percentage of GDP	0.5	-5.8	0.8	7.4	5.0	4.5	1.7
<b>Financed by:</b>							
Net equity flows	7.0	7.8	3.9	2.7	5.3	3.0	2.0
Net FDI inflows	6.2	7.5	3.2	2.5	5.5	3.0	3.0
Net portfolio equity inflows	0.8	0.3	0.7	0.2	-0.1	0.0	-1.0
Net debt flows	-4.4	8.3	-2.2	-6.5	1.7	-0.3	2.5
Official creditors	-4.0	-1.7	-2.7	-2.9	-1.2	-1.6	0.0
World Bank	-0.3	-0.2	0.2	-0.3	-0.1	-0.3	—
IMF	0.3	0.0	0.0	-0.2	-0.1	-0.3	—
Others	-4.0	-1.5	-3.0	-2.4	-1.0	-1.0	—
Private creditors	-0.4	10.0	0.5	-3.6	2.9	1.3	2.5
Net medium- and long-term debt flows	0.2	5.4	-0.8	0.4	2.1	1.0	—
Bonds	1.5	1.3	1.4	1.2	4.4	2.3	—
Banks	0.1	3.8	-1.2	0.6	-1.4	-0.6	—
Others	-1.4	0.3	-1.1	-1.5	-0.9	-0.7	—
Net short-term debt flows	-0.6	4.6	1.3	-4.0	0.8	0.3	—
Balancing item <sup>a</sup>	1.7	10.3	-3.3	-24.8	-27.2	-22.4	-14.0
Change in reserves (- = increase)	-6.6	1.5	-2.6	-12.2	-8.8	-5.0	0.0
Memo items:							
Bilateral aid grants (ex. technical cooperation grants)	4.0	4.2	3.3	3.8	3.2	3.4	3.0
Net private flows (debt + equity)	6.9	17.8	4.4	-0.9	8.3	4.3	4.5
Net official flows (aid + debt)	0.0	2.5	0.6	0.9	2.0	1.8	3.0
Workers' remittances	9.4	10.3	10.5	10.9	13.1	14.0	—

— Not available.

Note: e = estimate; f = forecast.

a. Combination of errors and omissions and net acquisition of foreign assets (including FDI) by developing countries.