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The GCC economies are at a crossroads. Following low oil prices in 2016, the countries need to accelerate structural reforms to diversify their economies away from hydrocarbons, boost the role of the private sector, and create jobs for their rapidly growing labor force. The envisaged economic transformation, as reflected in country diversification plans, will take time. Careful and steady implementation and prioritization will be key to success. All the GCC countries have issued vision statements over the last few years, which describe their development aspirations either for the medium or long term. These visions guide current and future policy actions necessary for countries to achieve their development goals. The period covered varies by country and timing. The vision documents are well-written and cover different aspects of growth, such as entrepreneurship, small and medium scale development, productivity, nationalization of the workforce, national populations with skilled human capital working in the private sector, and development of high-productivity industries and services based on high-skilled labor and competitiveness.

Some countries have operationalized their vision framework through a series of development plans, which include policies to help achieve their long-term goals. The Kuwait Development Plan (KDP) 2015–20 and Saudi Arabia's National Transformation Program (NTP) are the most recent examples. The following analysis details the main pillars of each country's vision plan and assesses growth prospects over the short to medium term.

Bahrain

The Economic Vision 2030 for Bahrain, announced in 2008, targets economic diversification and is supported by a national development strategy (2015-18, similar to Saudi Arabia's NTP but less KPI-oriented and less state driven), which proposes actions aimed at improving the business environment. By 2030, it aims to double real disposable income for each Bahraini by building a productive and globally competitive economy driven by the private sector, and using competitiveness, fairness and sustainability as guiding principles. It acknowledges the increased global competition facing Bahrain and the role of innovation and productivity as critical sources of comparative advantage. The diversification strategy is embedded in three policy areas that support Vision 2030: Economy, Government, and Society. In the Economy category, the focus is on enhancing productivity and skills, capitalizing on existing high-potential non-oil sectors, and capturing emerging opportunities by expanding knowledge-based sectors. On Government, the Vision calls for an efficient and effective government that is more productive and accountable, provides for a regulatory system that facilitates growth, has public finances that are sustainable and depends less on oil revenues, and supplies world-class infrastructure. On Society, the Vision aims for high standards of social assistance to all Bahrainis, including access to quality healthcare, a first-rate education system, and a safe and sustainable living environment.

2017 Outlook

Bahrain's 2017 outlook points to slower growth, higher debt issuance, and high fiscal deficit. In early 2016, authorities announced significant fiscal measures to strengthen revenues, including increases in retail prices of fuel products, electricity, and water. However, real growth in 2017 will slow to 1.8 percent from 2.2 percent in 2016 due to lower capital spending which will impact investment and private consumption. Oil production is also expected to remain subdued as the current account deficit is projected at 3.9 percent for 2017, down from 5.2 percent in 2016. The financial sector which contributes roughly 16 percent of real GDP and is the second-largest sector after hydrocarbons is expected to see a year of slow growth due to greater competition from the UAE and Qatar as well as subdued region-wide liquidity. However, as oil prices begin to pick up in 2017, liquidity is expected to improve.

GCC funds directed toward major infrastructure projects, mainly from Kuwait and the UAE, will help prevent further economic slowdown in 2017. Of the $10 bn pledged by the GCC Development Fund to Bahrain by 2021, around $3.7 bn worth of projects have already started (an increase of 200 percent from the previous year). However, if fiscal constraints persist for regional economies, investments will be tougher to deliver, though Bahrain is looking for additional investments and growth.

Going forward, the upcoming expansion of an aluminum smelter and oil refinery are expected to support growth. A new potline at Aluminium Bahrain (Alba), which will increase the Kingdom's aluminum production capacity by over 50 percent, is expected to come online at some point in 2019, and a 100,000 barrel/day expansion of the Sitra oil refinery is likely to be operational by late 2020. Real GDP is expected to average 3.1 percent a year in 2018-2020.

Kuwait

Kuwait Vision 2035, announced in 2010, aims for a competitive and efficient private sector led economy transformed into a financial and trade center. It also aims to develop human capital, create a modern legal framework, and provide adequate infrastructure. Former UK Prime Minister Tony Blair, who commented on the Vision 2035 plan, said that Kuwait could be a "regional powerhouse of the future," but if reforms were not implemented, then "the future of this great country will be uncertain."

In February 2016, the government announced reform plans aimed at bolstering the fiscal position and fostering private sector development and diversification. The reforms, which are set to be implemented over the next five years under a schedule that remains to be fully specified, are organized around six main themes: (i) fiscal reforms, (ii) role of the State in the economy, (iii) private sector development, (iv) citizens' participation (v) labor market and civil service reform, and (vi) supporting institutional reforms. Fiscal reforms include current spending rationalization, reforms in wages and subsidies, introducing VAT, implementing

The diversification strategy for Bahrain is embedded in three policy areas that support Vision 2030: Economy, Government, and Society

a business profit tax reform, and increasing prices for government provided services. Economic reform also includes structural, legislative, and institutional reforms to improve the investment environment and attract national and foreign capital. Diversification and private sector development reforms are focused on privatization/PPPs, business climate reforms, and education overhaul.

2017 Outlook

Unlike many other governments in the region, Kuwait has committed to maintaining its capital spending program in a low oil price environment. This will help keep real growth at 2.5 percent in 2016 and 2.7 percent in 2017. Despite some spending cuts, the government will continue to invest in large-scale infrastructure and construction projects that will help sustain modest growth. The authorities' significant fiscal buffers, including the KIA's $592 bn sovereign wealth fund, will help sustain positive growth.

However, lower oil production in 2017 owing to an OPEC agreement to limit output will weigh on growth. The oil and gas sector still accounts for well over 50 percent of real GDP. Political stability will remain a key component for investor appetite that will determine the direction of many PPP deals. As oil prices recover in the next few years, there should be less resistance from parliament and greater non-oil private sector growth. Real GDP is expected to average 3.3 percent a year during 2018-2020.

At present, the government has a modest amount of debt (it is estimated that the public debt stock will have reached 13.5 percent of GDP in 2016, up from 10.5 percent of GDP in 2015), and this gives it latitude to increase borrowing as a way to cushion the impact of lower oil prices, although rising Fed Reserve rates in 2017 will increase the cost. The authorities have stated that they could issue (probably in 2017) up to $10 bn in external debt to cover the 2016-2017 budget deficit.

Oman

Vision 2020, launched in 1995, outlines the country's economic and social goals: maintain economic and financial stability, reshape the role of government and broaden participation of the private sector in the economy, diversify the sources of national income, globalize the economy, and upgrade the skills of the national workforce and develop human resources. Oman's 9th Development Plan (2016–20), the final component of Vision 2020, aims to tackle oil dependency by reducing the share of the oil sector in the economy through an ambitious diversification strategy.

Work has also started on a new long-term strategy, Vision 2040. The plan aims to boost the non-oil economy by targeting five sectors: manufacturing, logistics, tourism, fisheries, and mining. It emphasizes the need for the private sector to drive economic growth and job creation, which would be underpinned by improving the business environment, the development of SMEs, a privatization program, and further development of Public Private Partnerships (PPPs). In terms of job creation, the five targeted sectors are labor-intensive, and the strategy aims for higher participation of Omanis in the private sector, notably by targeting jobs currently occupied by foreign workers with a medium-level skill set.

One of the key economic targets of the Saudi NTP is to increase the share of the private sector to %65 from the current %40 and the SME sector's to %35 from %20

2017 Outlook

The government will continue to implement its austerity plan in 2017 on the back of its belt-tightening policy which was initiated in 2016. The government's plan to reduce spending by 11 percent in nominal terms will have a direct impact on real GDP growth but also an indirect impact, as private consumption is affected by slowing public sector wage growth and investment decelerates. It is anticipated that growth in 2016 will reach 1.6 percent and rise to 2.2 percent in 2017. Real GDP is expected to average 2.7 percent a year in 2018-2020.

Constrained government finances will lead to project delays, and capital spending in the oil industry will decline, impeding medium-term prospects of the sector. The government will continue to prioritize investment in infrastructure, focusing particularly on logistics and tourism, with the help of funding from the GCC Development Fund. Improved oil recovery techniques and greater production efficiency led to record oil output in 2015. Production has stayed at these levels in 2016, and we expect output to average a record 982,000 barrels/day in 2017.

The government has run down its reserves at the State General Reserve Fund (valued at an estimated $34 bn at end-2015), and it plans to use another $1.5 bn of reserves in 2016. However, given the dramatic widening of the deficit in 2015, and likely further deficits throughout the forecast period, the government will also turn to the debt markets. It has already borrowed $1 bn from a group of banks through a five-year loan and planned to borrow a total of $5 bn-10 bn from the international debt markets in 2016 alone. The government tapped the domestic market in 2015 by issuing its first sovereign Islamic bond (sukuk), but it will be increasingly reluctant to use domestic debt to avoid putting further pressure on banks' liquidity.

Qatar

Qatar's National Vision 2030, released in 2008, aims to transform the country into an advanced economy providing high standards of living for all its people, including future generations. It seeks to attain the right pace of economic growth in a country that has exceptionally high reserves of natural resources with a small national population. The Vision rests on four themes: human development, working towards an advanced educational and health system, with increasing participation of Qataris in the labor force; social development through pursuing an effective social protection system, a sound social structure, and a significant role in the international community; economic development, aiming for a sound economic management, responsible exploitation of oil and gas resources, and a suitable economic diversification; and, environmental development, seeking to preserve and protect Qatar's environment by balancing economic growth and social development needs.

The government has imposed a voluntary moratorium on further LNG exports, and has embarked on a public investment program to support diversification. Strategic priorities include education (Education City), sports (various championships including the 2022 FIFA), transport (Qatar Airways), finance (Qatar National Bank—the largest MENA bank), and culture (museums). Public finance reforms have also been implemented to increase spending efficiency, including an outline of the medium-term fiscal framework.

2017 Outlook

Growth in 2017 is expected to reach 3.4 percent, up from 2.5 percent in 2016. It will be supported by the arrival of the $10 bn Barzan natural gas development, which was initially due to come on stream before the end of 2016. High household incomes will also sustain private consumption, while government spending on capital projects should drive growth in local industries. However, import growth to meet industrial and consumer demand will outstrip the expansion in exports, which will weigh on real GDP growth. Real GDP is expected to average 3.7 percent a year during 2018-2020.

The authorities will continue to rein in current spending (and to limit non-essential public works) to accommodate rising capital expenditure as the World Cup nears. Fiscal consolidation continues: in mid-January 2016, the cabinet decided to raise fuel prices by around one-third. In May, it introduced a new system under which a committee at the Ministry of Energy and Industry sets the price at the start of each month on the basis of changes in the international energy market.

The government should be able to finance the bulk of its deficit via domestic and foreign borrowing — such as a $9 bn sovereign bond issued in May. However, one potential constraint on domestic deficit financing will be the banking sector's high loan/deposit ratio, which has remained well above 100 percent in recent years. This could impose limits on domestic banks' ability to purchase treasury bills and provide financing for major capital projects. Another complication will be the rising cost of borrowing facing emerging markets in 2017.

Saudi Arabia

Saudi Arabia Vision 2030, released in April 2016, is supported by three main themes: Saudi Arabia's status in the Arab and Islamic worlds, a determination to become a global investment powerhouse by diversifying revenue sources, and the transformation of the Kingdom into a global logistical hub exploiting its strategic location. The policies that will help achieve the goals of Vision 2030 are to be set out in a series of plans. The first — the National Transformation Program (NTP) — was released in early June. It lays out 178 strategic objectives with over 340 targets and benchmarks for 24 ministries and government entities to be achieved by 2020.

The goals in the NTP and other future policy plans that support Vision 2030 will broaden and deepen the ongoing reforms. Vision 2030 and the NTP set out an agenda to diversify the economy, increase the role of the private sector, and increase the employment of Saudis. Economic targets in labor market (unemployment), trade (non-oil exports), fiscal (debt and deficit), FDI and SME sectors have been announced.

One of the key economic targets of the NTP is to increase the share of the private sector to 65 percent of GDP from the current 40 percent; the SME sector's contribution is targeted to be increased from 20 percent of GDP to 35 percent. The plan envisages a greater role for the private sector, also through privatization and expanding the use of PPPs, with an aim to increase efficiency and productivity and increase job opportunities for nationals in the private sector. Fiscal consolidation is proceeding, energy and water prices have been increased, key performance indicators introduced for ministries, management of public investment strengthened, and reforms to increase foreign investor involvement in the capital markets announced.

2017 Outlook

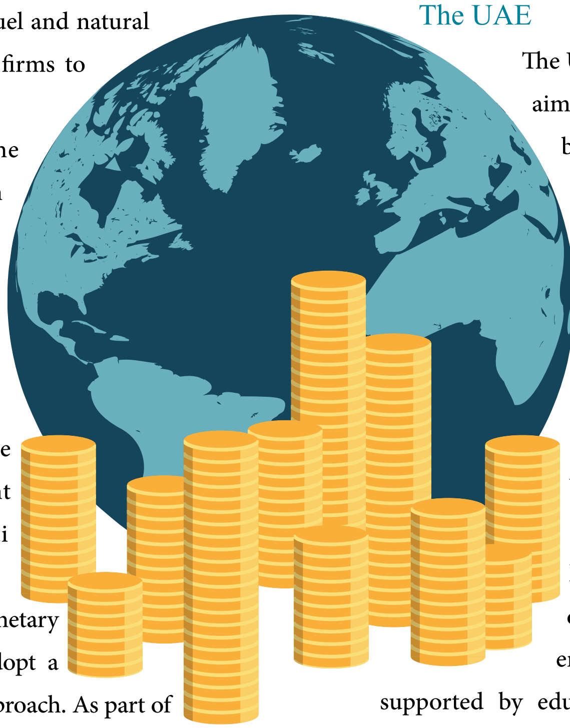
Economic growth is expected to slightly recover in 2017 to 1.5 percent from 0.9 percent in 2016, as some investments begin to return and confidence gradually builds up. With further subsidy reductions likely in 2017, and oil production declining slightly (in line with an expected OPEC quota deal), expect the economy to remain on a recovery path. Growth will be driven by progress on several infrastructure projects (including the Riyadh Metro and some forward movement in the government's affordable housing program) which will provide opportunities for the private sector. Real

GDP is expected to average 3 percent a year in 2018-2020. The NTP's focus on boosting the tourism sector will yield positive results following the introduction of new infrastructure and the expansion of the two major mosques in Makkah and Medina from 2017. However, a sharp slowdown in the issuance of new project contracts will hinder activity in the construction sector — although concerns about payment delays should be eased somewhat by government plans to pay down SR100bn ($37.5 bn) of its arrears by early 2017. In addition, business investment will be depressed by big increases in fuel and natural gas prices, which will also cause firms to rein in new hiring.

The Saudi riyal's peg to the US dollar means that the main policy rate must roughly track movements in US interest rates, even when the two countries' economic cycles are out of sync. With the Kingdom's oil exports denominated in US currency, we do not forecast any adjustment to or abandonment of the Saudi riyal's peg.

The Saudi Arabian Monetary Authority (SAMA) is likely to adopt a more flexible indirect monetary approach. As part of this shift, in September SAMA injected SR20 bn ($5.3 bn) into the banking system as time deposits on behalf of government institutions, and we expect further stimulus measures (such as an easing of banks' reserve requirements) in 2017.

The government has covered its budgetary shortfalls by dipping into its massive stock of reserves (which were worth $562 bn, or 28 months of imports, in August). However, aware of the need to protect its reserves, the government will finance its deficits to a greater degree by issuing debt, both to domestic banks and, — increasingly, on the international debt markets. In April, it agreed on a $10 bn loan with a syndicate of foreign banks, and the government successfully sold $17.5 bn in bonds in October (the largest ever issue by an emerging market country). As a result, we expect the public debt stock to soar from a negligible 5.9 percent of GDP at the end of 2015 to 41 percent of GDP at the end of 2021.



The UAE

The UAE Vision 2021, launched in 2010, aims for the country to be among the best in the world by its golden jubilee. Although considering new goals in terms of economic diversification by 2050, Vision 2021 is supported by four aspirational objectives for the UAE: to be an ambitious and confident nation grounded in its heritage, a strong union bonded by a common destiny, become a competitive economy driven by knowledge and innovation, and develop a nurturing and sustainable environment for quality living supported by education, healthcare, infrastructure, and the environment. The Vision rests on a sound results-oriented management framework.

The UAE has pursued an outward-oriented development strategy, based on an open trade regime and unrestricted capital outflows complemented with large strategic investments in ports, airports and airlines, an international financial center, and an active industrial policy in petrochemicals, aluminum, and steel.

Outlook 2017

Real GDP growth will ease slightly to 2.4 percent in 2017, from 2.1 percent in 2016, reflecting the impact of OPEC mandated production cuts, although these will have an effect on the UAE's more diversified economy than on some other GCC states such as Kuwait and Saudi Arabia. We expect oil prices to increase going into 2018 as the economy experiences higher growth, before slowing in 2019 as global demand growth subsides. Dubai's hosting of Expo 2020 will help increase government spending and investment. The event will draw a large number of visitors, boosting private consumption and services exports. However, the Expo also presents risks related to overcapacity, property prices, and debt. Real GDP is expected to average 3.5 percent a year during 2018-2020.

The UAE will continue to benefit from its safe haven status in a turbulent region and from the lifting of sanctions on Iran. Despite ongoing regional tensions, Dubai will benefit as a commercial hub for doing business in and trading with Iran. Manufacturing, trade, transport and tourism dynamics will be affected by the moderation in the global economic recovery and, increasingly, uncertainty in the US and China.

The expectation that oil prices are unlikely to return to their 2012-2014 peaks is helping restrain some spending, while cuts in subsidies introduced in 2015-2016 are likely to be maintained or even widened, helping to keep costs down. We do not expect the UAE to curtail infrastructure projects entirely, given large fiscal buffers in the form of sovereign wealth fund assets, estimated at over $1.1 trn. Like the rest of the GCC, both the federal government and individual emirates will also make greater use of international bond issuance to avoid draining liquidity from the domestic banking system. One of the main ways the government is improving fiscal sustainability is through reductions in fuel, electricity and water subsidies.

The public finances are managed largely at an emirate level, with the federal budget, predominantly funded by Abu Dhabi, representing only about one-tenth of total expenditure. The 2017-2021 federal budget program presents a cautious increase from the 2016 budget cuts and it is expected to rise by 1.5 percent in 2017. Dubai will continue to expand its budget in reaction to its more diversified revenue base. Abu Dhabi has announced new development spending plans that suggest its fiscal austerity drive is dissipating.

Conclusion

Despite recent increases, oil prices — the key driver of the outlook for GCC economies — are projected to remain low over the coming years. Economic activity in the GCC region is projected to pick up slightly in 2017 despite expected reduction in hydrocarbon output due to the 2016 OPEC agreement. Fiscal tightening and declining liquidity in the financial sector were expected to reduce non-oil growth in the GCC in 2016. However, non-oil growth is projected to pick up in 2017 as the pace of fiscal consolidation eases. Over the medium term, less fiscal drag and a partial recovery in oil prices are projected to raise GCC non-oil growth.

Risks are to the downside. The negative impact of fiscal consolidation and tightening liquidity on growth could be larger than anticipated. Regional conflicts could intensify. A deeper slowdown in China could further weaken commodity prices, while a faster-than-expected US monetary tightening could increase global financial volatility, thereby reducing the availability of international financing, especially for lower-rated issuers. Risks to medium-term growth are double-sided. Authorities could make faster-than-expected progress in implementing structural reform plans. However, considering the scope of the envisaged economic transformation, such plans could run into obstacles, which could lead to reform fatigue and domestic political constraints.

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