Baker Ing

Middle East & North Africa Economic Outlook

Q2 2021

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Contents

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In association with CEDAR ROSE®

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Foreword by Cedar Rose

MENA Data Availability & Accessibility

The Middle East and North Africa (MENA) region can be construed as a difficult area to maximise business potential due to the lack of information, or more specifically, the lack of access to information.

Digitalisation of datasets, open-access to data framework and overall data availability is scarce in MENA, therefore, it requires a lot more research and innovation to utilise the hidden gems that this region has to offer.

The MENA economy is rapidly growing; innovation, sustainability and advanced technologies are spreading, from the likes of the Dubai 2020 expo, which focuses around sustainability, to the Saudi 2030 vision, which is set to transform the country, it is evident that the MENA region is rapidly transforming in some areas at least.

Henceforward, this region poses huge potential for investment, growth and sustainability; so how do we identify potential clients, onboard them swiftly while adhering to compliance and regulatory requirements, ensure they are credit worthy and remain compliant by monitoring them when reliable data seems elusive?

Data

The growth of data across the 2010s has placed a standard of data requirements that countries should meet for the best interests of their citizens. From the General Data Protection Regulation (GDPR) 2018 to the Consumer Data Privacy Legislation 2019, nations across the globe are putting together frameworks to not only provide users with valuable data but also to protect their sensitive data from unauthorised disclosure.

Open data provides citizens with a platform to hold and assess their governments, demand accountability and to ensure transparency. However, according to the Open Data Barometer, many governments fail to meet the basic Open Data Charter principles. Specifically, the Middle East and North Africa region, as a whole, is lagging behind a huge proportion of the world in regards to providing their citizens with an open data framework, accessible datasets and, therefore, the ability to demand accountability of governments.

The Open Data Charter

This charter, developed in 2015, consists of six core principles in which governments across the globe agreed upon. The charter laid out foundations and norms concerning how to publish data. The six core principles are:

Open by Default:
This principle assumes that governments should hold open publications for all to access and any governmental data that is private needs to be justified, such as security or privacy motives. Governmental norms tend convey the process that citizens must express a desire to have such information as a prerequisite,

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nonetheless, this charter rightly aims to hold governments responsible for displaying data open and publicly accessible for all.

Timely and Comprehensive:
Data held must be up-to-date and relevant for citizens to view. Although data should remain in its original unmodified state, it is only valuable if it is relevant.

Accessible and Usable:
Data must be easily accessible for citizens, for example displayed in a clear easy-to-use online portal as some nations currently have. Additionally, file formats and machine readability are two factors that must work with the user in order to benefit those accessing it.

Comparable and Interoperable:
Data is best organised when separated into relevant datasets with open access to all of them. The ability to compare across multiple datasets allows the user to gain more potential value from them.

For Improved Governance:
Citizens can hold governments accountable through open data, allowing them to see what the representatives are actually doing. Additionally, it creates a more transparent government, which can aid to public services and ensure correct accountability. Moreover, open data also created more informed voters, which can result in improved governance.

For Inclusive Development and Innovation:
Open data can have limitless implications for improving countries, socially, economically and politically. For example, data can highlight climate change actions or highlight the need for reforms to support climate change.

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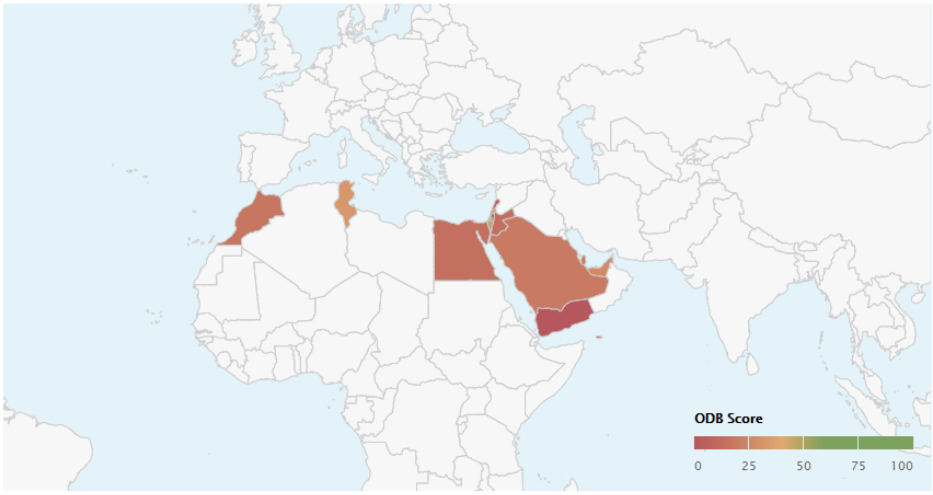
AVERAGE SCORE	READINESS AVERAGE	IMPLEMENTATION AVG	IMPACT AVERAGE
18 out of 100	34 out of 100	17 out of 100	10 out of 100



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MENA's Current Open Data Strategy

Unfortunately, the Middle East and North Africa region is as a whole failing to progress on open data. MENA countries show low rankings with all, except for one, of the nation's outside of the top 50 and, worryingly, little strategy in place to provide open data for their citizens.

The latest Open Data Barometer (4th Edition) analyses the following countries across the MENA region: Bahrain, Egypt, Israel, Jordan, Lebanon, Morocco, Palestine, Qatar, Saudi Arabia, Tunisia, United Arab Emirates and Yemen. The Open Data Barometer scores countries based on three factors, each weighted differently, Readiness, Implementation and Impact.

Readiness:
The measure of making a countries data readily available and open to the public. Additionally, if governments are working towards strategies to improve open data.

Implementation:
The implementation of datasets that are accessible across the region. To work towards opening platforms that display open data.

Impact:
Assessing the impact of open data, utilising the figures to create policy and positive progress within the region.
The MENA region's latest figures show a collective active score of 18/100, with Readiness 34/100, Implementation 17/100 and Impact 10/100. These figures immediately show a disinterest for the nations to enhance their open data availability to the public.

Almost all countries dropped in rankings, despite governmental initiatives and strategies, which had been implemented a few years ago. Although limited, a few nations have begun to enhance their open data, for example, the United Arab Emirates (UAE). The UAE has an open portal, Bayanat, which displays government data in their plea to enhance governmental transparency. Nonetheless, it is evident that the MENA region is in need of a strategy to bring about open data and enhance availability for their citizens.

Typically, due to a lack of civil society engagement with open data, citizens hold no desire to pressure governments to make data publicly available, especially in relation to social issues.

Cedar Rose's MENA Data

Cedar Rose has long understood and recognised the lack of data across the MENA region, the scarce datasets publicly available, the lack of strategy and technology in place to hold the data and the lack of desire for governments to openly display data. Therefore, over the last 23 years we have been committed to bringing MENA data to an online platform.

We believe in using data to make the best decisions, especially for economic reasons such as risk management, compliance, due diligence and credit control. Cedar Rose has compiled a database which holds data on over 13 million companies and over 23 million individuals across the MENA region. We

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have researched, collected, and cleaned data across MENA and compiled it into an easy-to-use database.

We have overcome major difficulties such as data that has not been digitalised, data that is not publicly available in the English language, data that is not standardised to internationally recognised formats such as UKSIC or IFRS and data that has been recorded incorrectly. We have rectified all of these issues to create an excellent quality database of businesses and associated people within the entire Middle East and North African region.

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Regional Overview: Middle East & North Africa

Macroeconomic Developments & Outlook

Context

Baker Ing divides the Middle East and North Africa (MENA) region into three broad sets of economies: oil exporters[1], oil importers[2] and fragile, conflict and violence (FCV) states[3]. Israel, because of its lack of integration into the regional economy, is considered on its own merits in this report. Even within the three groups there is considerable differences in the credit risk outlooks. The factor that draws the region together is oil revenues, which accrue to the oil exporting country governments and are then distributed through a number of channels to the rest of the region. These channels include trade, investment, economic assistance and remittances through the expatriate workforces.

Oil Revenues and Regional Growth Prospects

Oil revenues have fluctuated sharply in this century, dictated in part by production levels, which in turn are a function of global demand; thus, oil demand crashed in 2020 as the Covid-19 pandemic hit (see Chart 1). Output can also be subject to OPEC or as at present OPEC+[4] agreements (see Box). Revenues are also a function of the oil price; the inelasticity of the oil price has meant sharp swings over the years (see Chart 2).

Looking ahead, we expect oil demand to pick up over the next five years leading to increased output amongst most of regional countries; exceptions are liable to include Algeria, unless the government takes an unexpectedly sharp u-turn with its oil policy, and the FCV oil economies of Iraq, Yemen, Syria and Libya. Although demand will pick up as the global economy recovers from the pandemic, other factors will curtail growth potential, including the increasing move towards green energy – even oil dependent countries such as the UAE, Saudi Arabia and Qatar are increasingly looking at developing solar energy, nuclear power and green and blue hydrogen. These countries have also seen domestic demand surge as a result of the cheap, often subsidised supply curtailing export volumes; fiscal

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[1] Oil exporters include the Gulf Cooperation Council (GCC) countries, - Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates (UAE) - Iran, and Algeria.
[2] Oil importers include Morocco, Tunisia, Egypt, and Jordan.
[3] FCV states include Iraq, Syria, Yemen, Lebanon and Libya.
[4] OPEC+ is in informal group of countries comprising the 13 OPEC countries – Algeria, Angola, Equatorial Guinea, Gabon, Iran, Iraq, Kuwait, Libya, Nigeria, the Republic of the Congo, Saudi Arabia (the de facto leader), the United Arab Emirates and Venezuela - and ten non-OPEC countries - Azerbaijan, Bahrain, Brunei, Kazakhstan, Malaysia, Mexico, Oman, Russia, South Sudan and Sudan.

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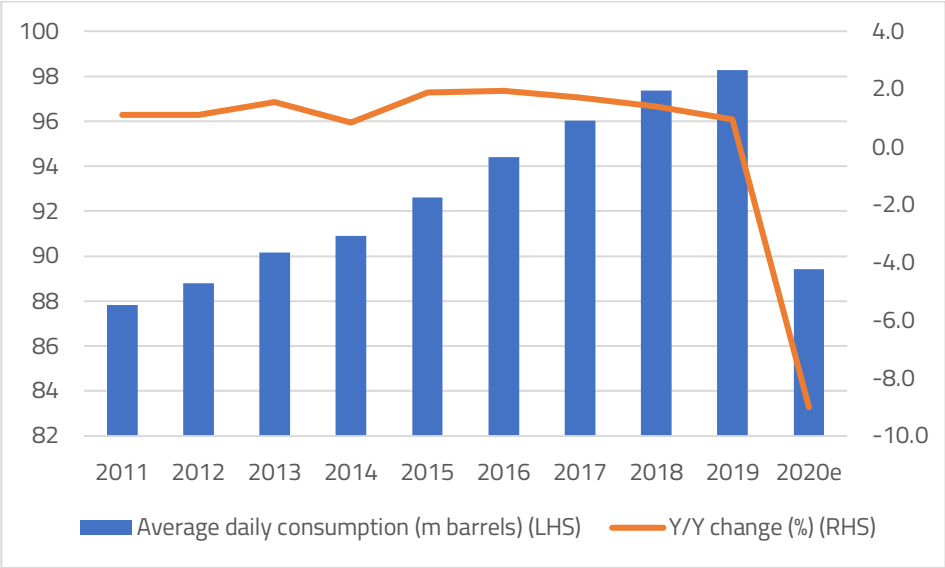
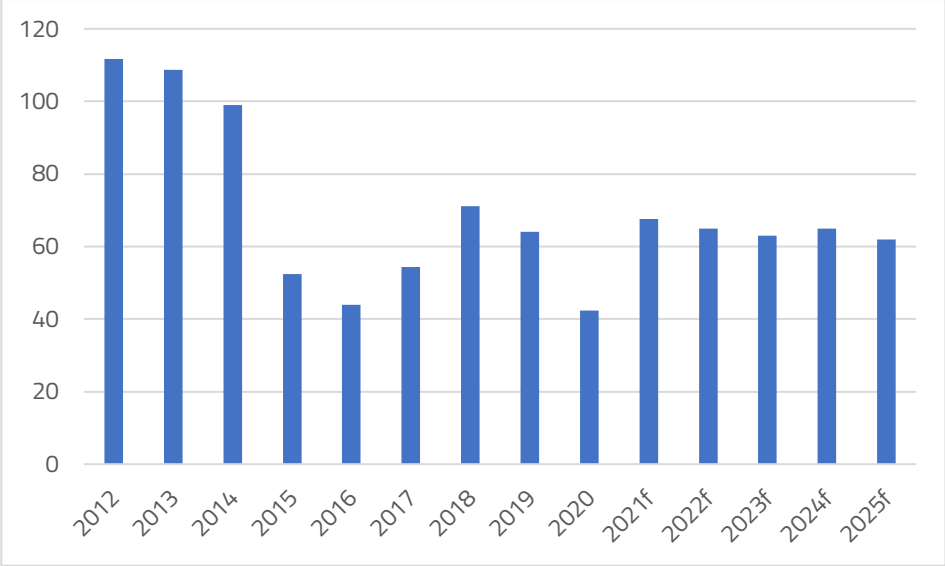
pressures will force the oil exporting countries to move towards global market pricing structures, which will eventually curtail domestic demand.

Chart 1: Global Annual Oil Consumption, 2011-2020



Source: BP Statistical Review/Baker Ing

Chart 2: Annual Average Brent Spot Oil Price, 2012-2025, USD/b



Source: World Bank/Baker Ing

Turning to the second element of the revenue equation, despite media-catching headlines of oil prices hitting the USD100 per barrel (/b) mark, we are less sanguine about the price over the next five years (see Chart 2). Oil prices in the short- to medium term will be constrained by increased output from conventional and non-conventional sources, such as US shale oil. However, beyond our five-year horizon, supply will be curtailed by the recent fall in investment in the sector. A further factor which is likely to boost short term supply and therefore put a ceiling on price is the easing of the OPEC+ agreement, which is due to end in April 2022. Furthermore, political and security will play an important role in the oil price

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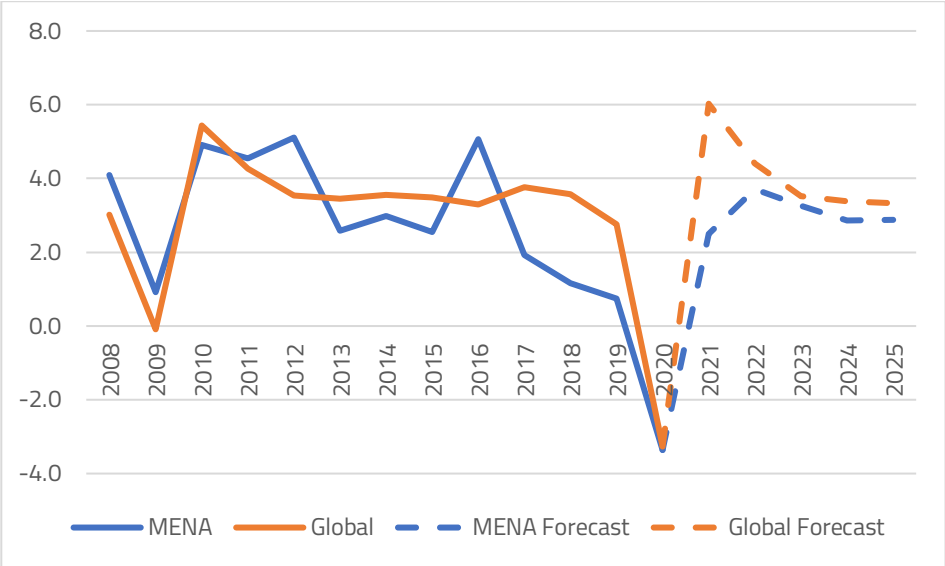
scenario. If the latest peace deal in Libya lasts, then the country should be able rapidly rebuilt its oil production levels. Similarly, Iraq has the potential to unleash significant volumes onto the market. However, the key market to watch is Iran, if the nuclear deal is re-negotiated then over 1m b/d could quickly return to the market. Meanwhile, a number of countries have ambitious plans to develop their capacity, believing there is little sense in locking in large volumes as the world moves away from its oil dependency.

The OPEC+ Agreements

The first OPEC+ agreement between the OPEC countries and non-OPEC countries, led by Russia, came into force in January 2017 in order to counteract surplus supply, brought on in large part by the surge in output from the US oil shale sector. The agreement covered the first half of 2017, but this was extended in May 2017 through to March 2018. In December 2017, the agreement was further prolonged to the end of 2018. In December 2018, the cuts were push through to the end of June 2019 but were again extended in March to the end of 2019. With prices still weak, in December 2019, the deepest cuts ever negotiated were agreed to the end of Q1 2020. When this agreement ended a price war broke out between Saudi Arabia and Russia leading famously to oil price briefly turning negative in mid-April. This quickly brought about another agreement, which remains in place today, and is due to end in April 2022.

Chart 3: Regional and World Growth, %, 2008-2025



However, fluctuations in oil revenues are not the only driver of changes in economic growth in the region. As can be seen in Chart 3 growth has fluctuated sharply since the 2008-09 global financial crisis, with growth tending to come in lower than global growth; a trend we forecast to continue over the next five years. This reflects a number of factors but the main one is widespread regional insecurity since the outbreak of the inappropriately named Arab Spring in late 2010.

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Risks to the Credit Risk Outlook

The on-going Covid-19 pandemic will be the main headwind over the next 12 to 24 months. Growth will be dependent on the success of the vaccine rollout, which in turn depends on governments getting access to the vaccines, then having the capacity to distribute them and the population taking them up. At present, the region has three countries, the UAE, Israel and Bahrain in the top five countries in terms of rolling out the vaccine. However, in countries such as Egypt the rollout is slow.

The second factor is (as discussed above) if oil prices and demand can continue to grow over the period. A sharp fall in the oil price would see credit risk deteriorate across the region. Other factors which mitigate a strong rebound include a lack of transparency in the business environment, which is reflected in the weak scores the region receives in international surveys by the likes of the World Bank and World Economic Forum (WEF). The high incidence of corruption is also a major risk as is the weakening of the social contract between the authoritarian states and their populace. This contract is being undermined by increasing levels of poverty, reduced employment opportunities and increased prices of food and basic needs as cash-strapped governments cut back welfare subsidies.

Finally, although insecurity appears to be improving in region, especially in the hotspots of Libya, Yemen and Iraq, the improvement is still tenuous. Furthermore, the situation in Syria remains unresolved, while the June 2021 election of a hard-line president in Tehran increases the risk of Iranian adventurism across the region. In addition, radical Islamist groups, although on the defensive regionally, could yet rebuild their support base and return in the FVCs.

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Sovereign Credit Ratings

Table 1 shows the sovereign credit ratings for the rated regional countries, from the big three credit rating agencies globally. Companies that have large public sector ownership, as well as those that borrow heavily from banks, are subject to sovereign risk via both the fiscal and financial channels. When investors believe a country is more likely to default on its debt, the interest rates paid on the debt of that country increase, in order to compensate investors for the higher perceived risk. In such situations, it is often the case that banks see their funding costs increase as well. As such, when sovereign credit risks are elevated, companies in that country can also see their credit risk increase, for example via less favourable bank lending conditions.

Table 1: Middle East and North Africa Sovereign Ratings

	S&P		Moody's		Fitch	
	Rating	Outlook	Rating	Outlook	Rating	Outlook
Oil Exporters						
UAE	AA	Stable	Aa2	Stable	AA-	Stable
Qatar	AA-	Stable	Aa3	Stable	AA-	Stable
Kuwait	AA-	Negative	A1	Stable	AA	Negative
Saudi Arabia	A-	Stable	A1	Negative	A	Negative
Oman	B+	Stable	Ba3	Negative	BB-	Negative
Bahrain	B+	Negative	B2	Negative	B+	Stable
Oil Importers						
Morocco	BB+	Stable	Ba1	Negative	BB+	Stable
Jordan	B+	Stable	B1	Stable	BB-	Negative
Egypt	B+	Stable	B2	Stable	B+	Stable
Tunisia	NR		B3	Negative	B	Negative
FVCs						
Iraq	B-	Stable	Caa1	Stable	B-	Stable

Legend

Investment grade
Speculative grade

Sources: S&P, Moody's, Fitch.
Retrieved 19 June 2021

Only four of the countries, UAE, Qatar, Saudi Arabia and Kuwait, are rated by all three credit agencies as investment grade; notably these four countries are all oil exporters. This suggests that the credit risks associated with doing business with entities in these four countries are generally minimal. Morocco, an oil importer, is rated at investment grade by two of the agencies, S&P and Fitch. The weaker ratings in the reminder of the countries highlight that credit risks are more elevated, even in Oman and Bahrain, which are oil exporters.

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The Oil Exporters

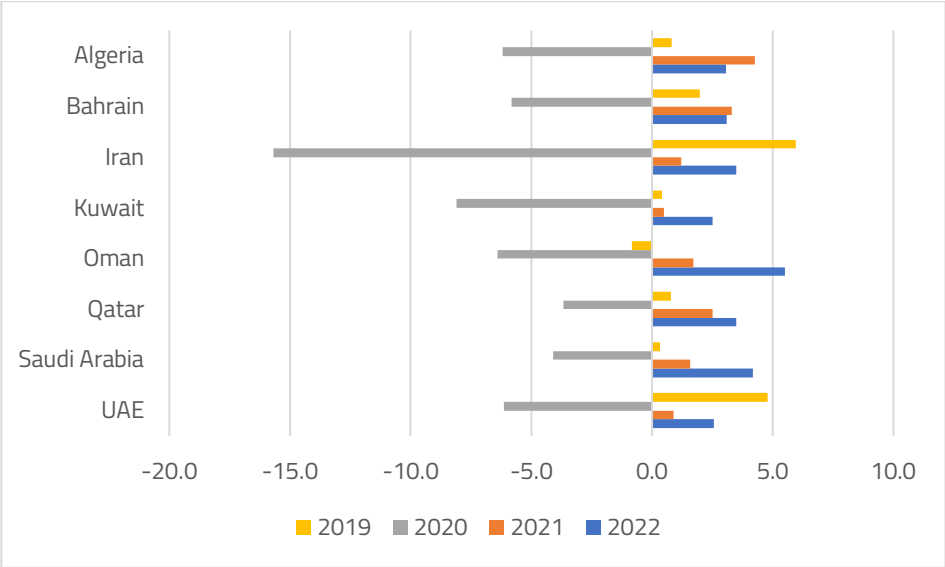
Economic Growth

In 2020, the economies of the oil exporters were hit by a triple whammy following the outbreak of the pandemic:

- the restrictions applied domestically, regional and globally reduced demand for goods and services;
- the collapse in the oil price, which was almost 34% lower than in 2019, and which was almost 10% lower than in 2018; and
- the collapse in demand for oil; oil consumption decreased by an estimated 9.0% in 2020. This saw the OPEC+ groups of countries voluntarily curtailing production in order to protect the oil price.

As a result, real GDP growth collapsed across all the oil exporting countries in the MENA region (see Chart 4). The worst hit was Iran, but this country also faced increasing primary and secondary sections as a result of US president Donald Trump's assertive policy towards Tehran's nuclear programme. Qatar escaped most lightly, in part because it was not part of the OPEC+ agreement.

Chart 4: Oil Exporters, Real GDP Growth, %, 2019-2022



Source: IMF/Baker Ing

Looking ahead, all the oil-exporters' economies will rebound in 2021, although the recovery will be weak as the OPEC+ production quotas, although easing, remain in place throughout the year. Growth will be driven by stronger oil prices, up by almost 60%; albeit these will still be below the 2018 outturn. Other supportive factors include government support packages, the global recovery from the pandemic, easing Covid-19 restrictions and the roll out of the vaccine programme. However, the speed of the vaccine programmes ranges from the UAE (145.2 doses per 100 residents) and Bahrain (116.8 doses per 100

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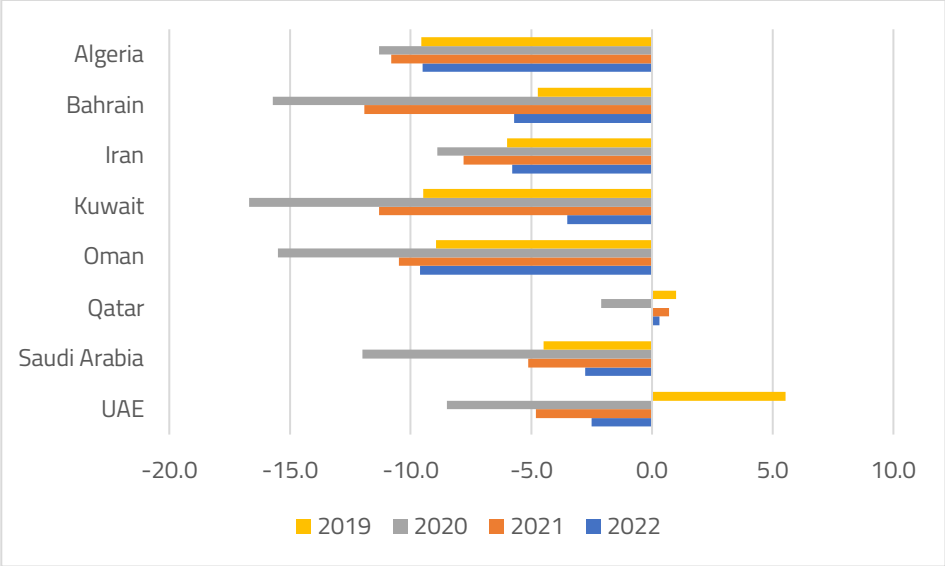
residents), which are in the top four of countries in the race to vaccinate, to Algeria and Iran where few have been vaccinated (5.8 doses per 100 residents)

Fiscal Developments

Chart 5 highlights that despite the high oil revenues accruing to the treasuries of the oil exporters, many of those countries were already facing fiscal problems before the outbreak of the pandemic. Only Qatar and the UAE recorded a surplus in 2019. The authoritarian nature of the political systems of the oil exporters has meant that an informal social contract exists between the rulers and the ruled. This pact implies that in return for a decent standard of living (in terms of jobs and subsidised goods and services) and limited taxation, the population will accept a lack of democracy.

Chart 5: Oil Exporters, Fiscal Position as % of GDP, 2019-2022



Source: IMF/Baker Ing

However, the 2008-09 global financial crisis which was followed by the outbreak of the Arab Spring in late 2010 has changed the dynamic as the oil-exporting governments have increased current spending against a background of broadly falling oil revenues. This pattern has been exacerbated by the Covid-19 pandemic, putting pressure on government finances in most countries. This, in turn, will see the oil-exporting governments having to introduce austerity measures which will further undermine the social contract, raising fears of anti-government demonstrations, along the lines of those seen in Algeria.

Furthermore, the weak fiscal position will put pressure on the credit risk environment in the short to medium term in the oil exporting countries, with Oman, Algeria, Bahrain and Iran under most pressure. According to the IMF, Algeria would need oil prices to average almost USD170/b in 2021 (our oil price forecast is USD67.5/b) before their budget would balance. Iran's position is even worse, with oil prices needing to average USD242.8/b before the budget is balanced, while Bahrain's breakeven point is USD88.2/b and Oman's USD72.3/b.

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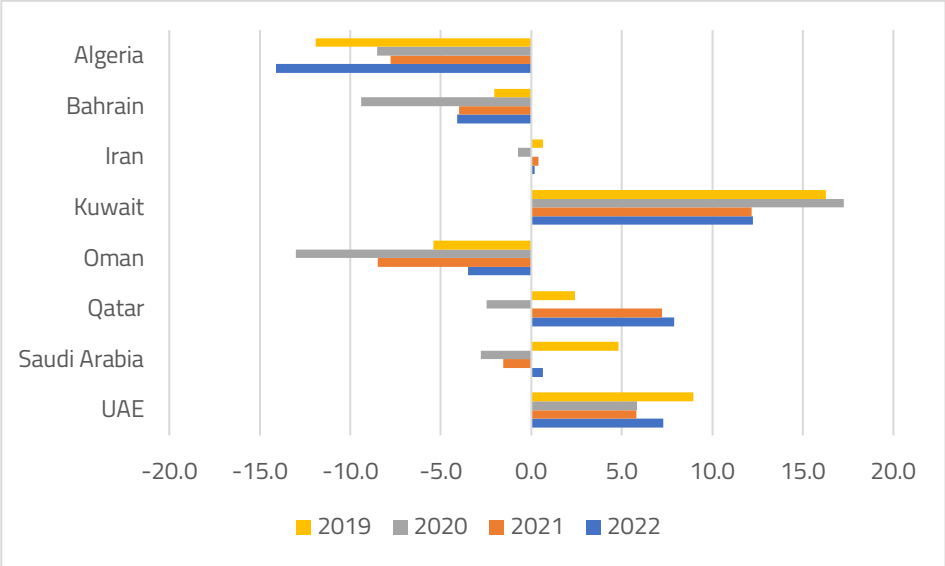
Positively, in the longer term, the oil-exporters' governments will adopt a more market-oriented approach to their economic decision-making; indeed, Saudi Arabia, the UAE and Qatar are already starting down this road. The change in policy will open these economies to cross-border opportunities as state and quasi-state entities are privatised, subsidies lifted, and trade and investment barriers eased. However, progress is liable to be slow and uneven while those countries that are less politically or economically stable – Algeria and Iran and to a lesser degree Bahrain and Oman - governments will be reluctant to radically change economic direction over the next two years, for fear of increasing political and security tensions.

External Developments

As with the fiscal position, the current account in the oil-exporting countries is heavily dependent on oil and gas revenues. Prior to the outbreak of the pandemic, most oil exporters were running a current account surplus; however, Bahrain (2.1% of GDP), Oman (5.4% of GDP) and Algeria (11.2% of GDP) were running deficits. The sharp fall in oil exporting revenues in 2020, more than counteracted any import compression amongst the oil exporters. As a result, only the UAE (5.9% of GDP) and Kuwait (17.2% of GDP) recorded surpluses on the current account.

Chart 6: Oil Exporters, Current Account as % of GDP, 2019-2022



Source: IMF/Baker Ing

Looking ahead, the increase in oil prices, along with the easing and eventual lifting of the OPEC+ production agreement, will see most countries recorded a surplus on the current account by 2022. However, three countries will still record deficits: Algeria (14.1% of GDP), Bahrain (4.1% of GDP) and Oman (3.5% of GDP). Importantly, the deficits on both the current account and the fiscal account for Algeria, Bahrain and Oman will ensure credit risks remain higher than would be expected for an oil exporting country.

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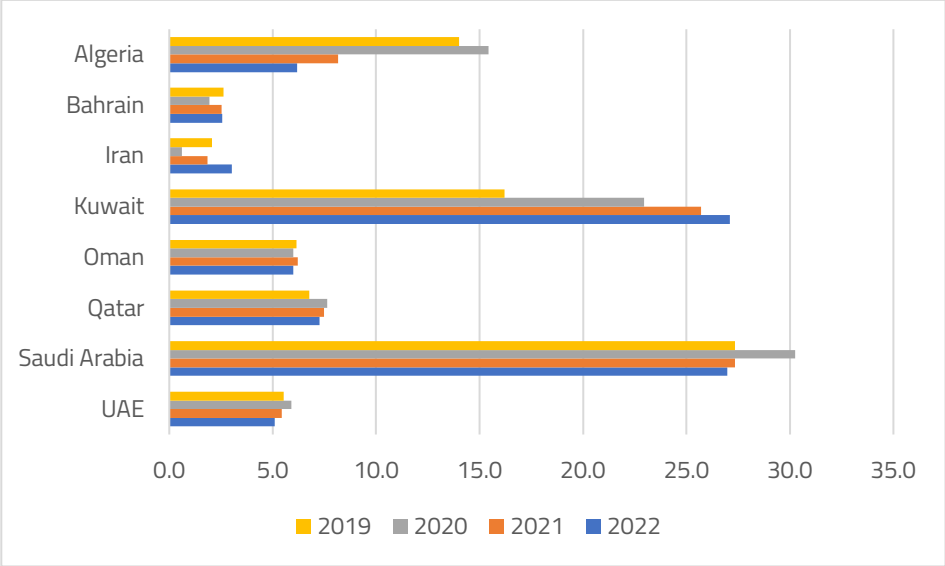
Currency Risk

Among the Gulf Cooperation Council (GCC) countries[5], only Kuwait has a currency that is not pegged to the US dollar. However, the Kuwaiti dinar is linked to an undisclosed basket of currencies, with the US dollar appearing to be the major element. As a result, the volatility of all six currencies reflect those of the US dollar; mitigating the need to hedge any transitions in US dollars. Although the pegs have been in place for years and are recognised by the IMF as positive, we feel that the Bahrain's peg and to a lesser degree that of Oman could come under pressure into the medium term as a result of their twin deficits. Furthermore, Bahrain's position is exacerbated by its weak FX reserves position as measured by import cover (see Chart 7), which will remain under the 3-month minimum recommended by the IMF for emerging economies. The remaining GCC countries have strong FX reserves and sovereign wealth fund (SWF) assets ensuring FX risk remains low.

Chart 7: Oil Exporters, FX Reserves in Months of Imports, 2019-2022



Source: IMF/Baker Ing

In the remaining oil-exporting countries, Algeria and Iran, FX risk is considerably higher. Iran is still facing a high level of US sanctions because of its nuclear programme. Until a new nuclear deal is in place, then FX risk in Iran will remain extreme. Iran operates multiple exchange rates: the official rate is pegged at IRR42,000:USD at which major imports are priced and is unsustainable. NIMA, the rate at which Iranian exporters are required to sell their hard currency, is at least 20% below SANA, which is used by the official currency exchanges. On 21 June 2021, the middle rate for these transactions was IRR239,800:USD. In addition, a black market also exists. In addition, Iran's FX reserve position is weak, at below the 3-month minimum. If a new nuclear deal were to be agreed with a consequent lifting of US sanctions, then Iran's FX risk would improve; albeit, it would be highly risky into the medium term.

[5] Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates (UAE)

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Algeria operates a manged float exchange rate, in which the central bank intervenes. There is also an active black market, with the differential between the two at about 30%. The IMF has recommended closing this gap. We estimate than the average annual exchange rate will depreciate by around 30% between 2020 and 2022, ensuring FX risk remains elevated. Furthermore, the risk will be exacerbated by the speed at which Algeria is burning through its FX reserves; although at present these remain well above the 3-month minimum. At the end of 2014, the import cover was over 30 months, by the end of 2020 it was just over 15 months and by end-2022, we forecast it will have fallen to just over 6 months.

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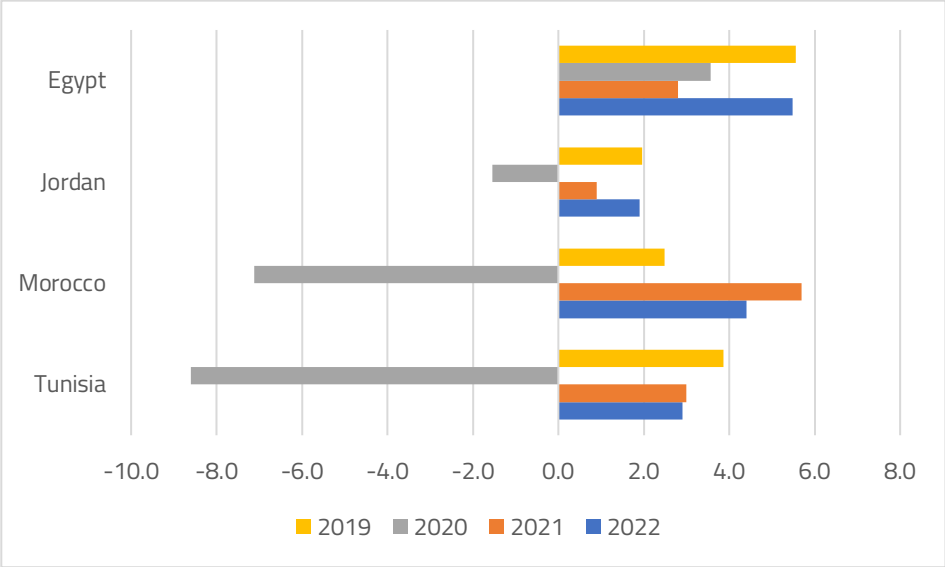
The Oil Importers

Economic Growth

As highlighted earlier, the oil importing countries in the region are indirectly reliant on the oil revenues earned by the oil exporting countries. Thus, the downturn in the oil exporting countries in 2020 fed through into the oil importers in terms of lower job opportunities and trade and investment flows. Another crucial factor was the stagnation of the tourist sector in all four economies. In 2019, tourism contributed 18.9% to GDP in Morocco, in Tunisia it was 16.1%, in Egypt it was 8.8%, and in Jordan 19.8%. Overall, Morocco and Tunisia were hardest hit in 2020 with the economies contracting by 7.1% and 8.6%, respectively. Jordan's economy only contracted by 1.6%, while the 2020 calendar year is spilt across the FY2020 (July 2019 to June 2020) and FY2021 (July 2020 to June 2021) for Egypt.

Chart 8: Oil Importers, Real GDP Growth, %, 2019-2022



Source: IMF/Baker Ing
Note: Egypt's data is for the fiscal year. Thus, 2019 refers to July 2018-June 2019.

Looking ahead, all four economies will grow in the two-year forecast horizon but as with the oil exporters forecasts, there is a high degree of uncertainty because of the path that the Covid-19 pandemic will take and the success of the vaccine rollout. As at 19 June, Morocco had dispersed the most doses per 100 residents at 47.8, followed by Jordan at 28.6, Tunisia at 12.5 and Egypt at 3.8.

Headwinds facing all four countries include their tourist sectors, which are unlikely to receive any significant number of visitors in 2021 and will face competition in 2022 from countries that are fully vaccinated. Morocco's growth will be dependent on its agricultural sector, which is heavily influenced by seasonal rainfall. In Tunisia, growth prospect will be impacted by the (in)ability of politicians to start addressing the structural impediments facing the economy and rising political protests. Politics will also be a key factor in Egypt, while

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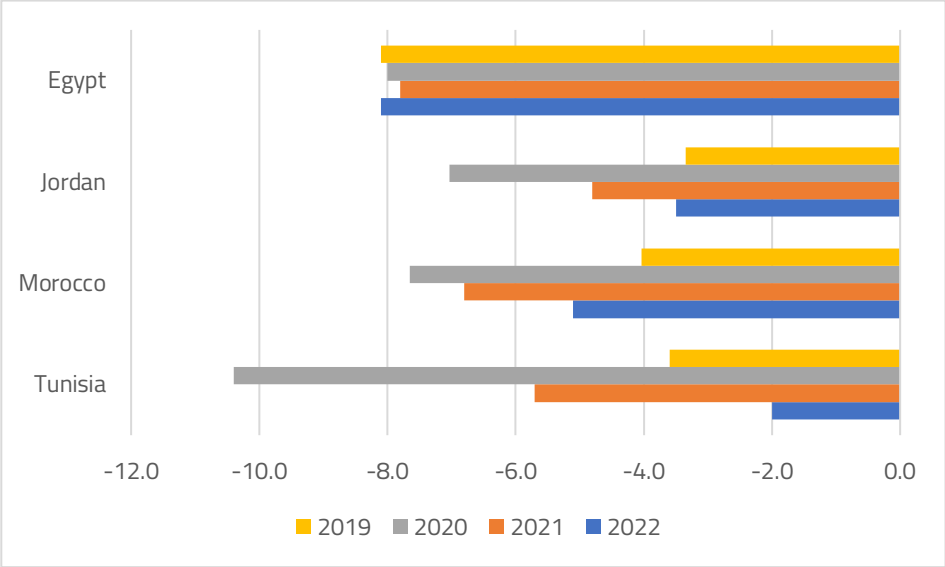
Jordanian growth will remain very anaemic as the country struggles to cope with the high number of refugees.

Fiscal Developments

All four of the oil importers were facing fiscal problems prior to the outbreak of the virus. Their situations, with exception of Egypt, were exacerbated in 2020 by government support to offset the impact of the Covid-19 restrictions and also falling revenues as taxation flows were hit. Egypt had less room for manoeuvre because of its already weak position (8.1% of GDP in FY2019). All four countries are dependent on IMF programmes, without this support credit risk would be significantly worse.

Chart 9: Oil Importers, Fiscal Position as % of GDP, 2019-2022



Source: IMF/Baker Ing
Note: Egypt's data is for the fiscal year. 2019 refers to July 2018-June 2019.

Looking ahead, at present, we only expect Tunisia's fiscal account to improve in 2022 relative to the pre-pandemic levels in 2019. Jordan will continue to suffer from hosting over one million refugees and violence in neighbouring countries, ensuring government spending on welfare remains higher than it can afford. Morocco had been slowly addressing its fiscal position, but the pandemic is likely to set it back four to five years. Egypt's fiscal position will remain the worst of the four countries at around the 8% of GDP level.

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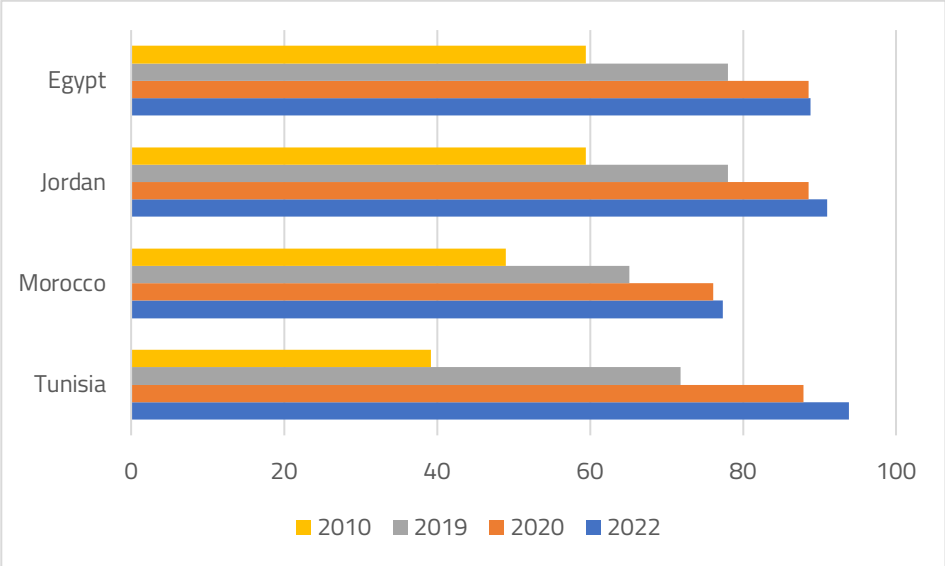
Government Debt

The deficits on the fiscal and current accounts have resulted in general government debt as a percentage of GDP trending upwards over the past decade (see Chart 10). This trend was exacerbated in 2020 by government responses to the pandemic. Egypt's data hides the fact that following its floating of the pound in late 2016, which resulted in a sharp devaluation of the currency, general government debt peaked at 103.0% of GDP, and had fallen to 84.2% of GDP by the end of 2019. Morocco's debt rose sharply in the first half of the decade then stabilised at just over 65% of GDP, before the pandemic responses saw it rise to 76.1% of GDP, making it the best placed of the four countries but still at a worrying level.

Chart 10: Oil Importers, General Government Debt as % of GDP, Various Years



Source: IMF/Baker Ing

Jordanian and Tunisian debt levels have risen consistently in the 2010s to worrying levels at over 90% of GDP. Jordan, which experienced a series of debt restructuring agreements between 1989 and 2002, is again on the edge of requiring debt restructuring, if not debt write-offs. Although Tunisia has not had to go to the Paris Club of Lenders, which comprises a group of official lenders with the task of resolving government debt problems, its rise in debt has been the sharpest of the four countries. The debt levels in all four countries signal problems for credit risk.

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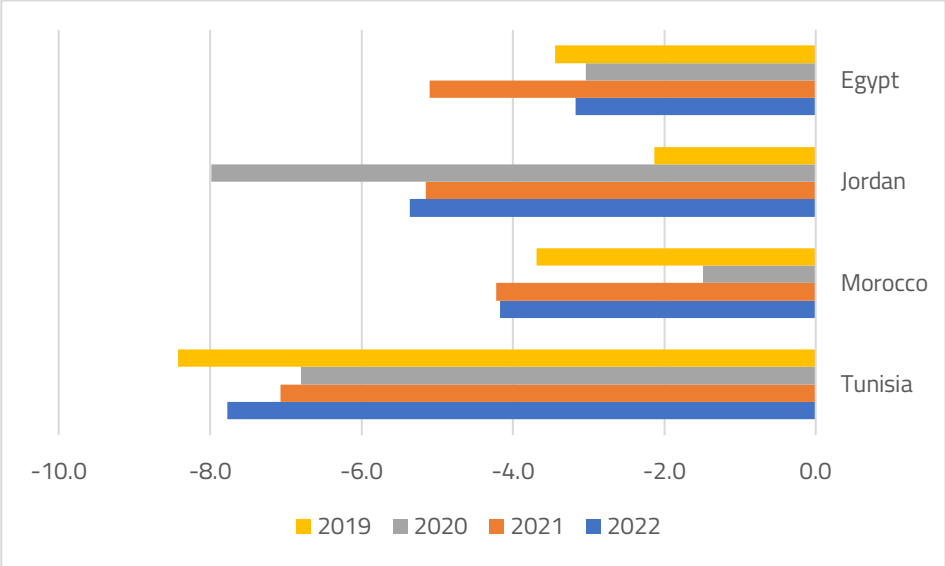
External Developments: Current Account Balance

All four countries run persistent current account deficits (see Chart 11), which add to the pressure on debt levels (see Charts 10 and 12). Import compression in 2020, because of the Covid-19 restrictions, saw the positions improve in Egypt, Morocco and Tunisia. However, despite import compression, Jordan's current account deficit worsened significantly.

Chart 11: Oil Importers, Current Account Deficit as % of GDP, 2019-2022



Source: IMF/Baker Ing
Note: Egypt's data is for the fiscal year. 2019 refers to July 2018-June 2019.

Looking ahead, we expect the current account deficit will widen from the pre-pandemic level in 2019 to 2022 in Jordan (from 2.1% of GDP to a worrying 5.4% of GDP) and Morocco (3.7% of GDP to 4.2% of GDP). However, the positions will improve in Egypt (3.4% of GDP to 3.2% of GDP) and Tunisia (8.4% of GDP to a still unsustainable 7.8% of GDP).

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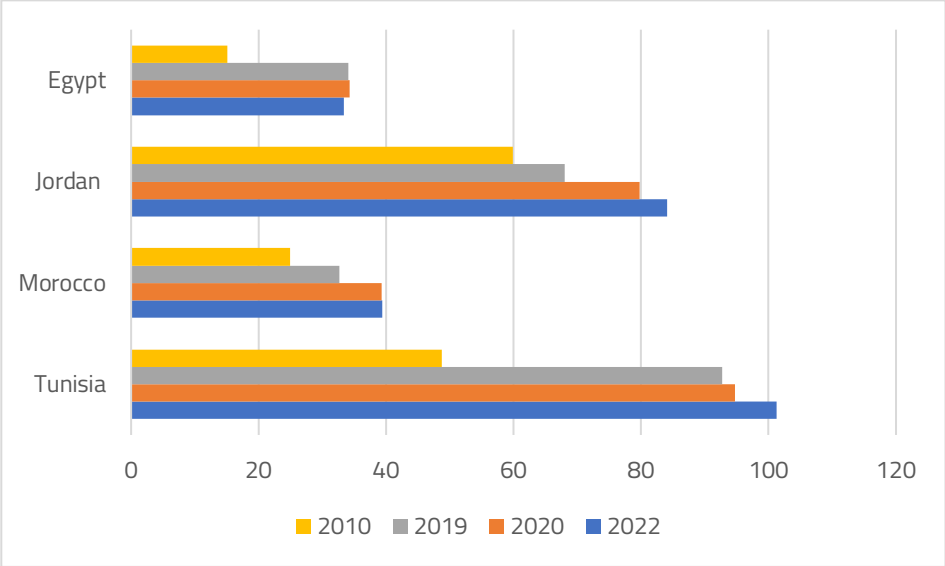
External Developments: External Debt

As highlighted above the persistent current account deficits have resulted in external debts climbing over the decade in all four countries. And, again, this trend was exacerbated by the Covid-19 pandemic. However, there are significant differences between the countries in the level of debt and the speed of change between 2010 and 2020.

Egypt's external debt increased sharply from 18.3% of GDP in FY2016 to 41.3% of GDP in FY2017 because of the floating of the pound in late 2016. Since then it was trending downwards until the pandemic, which caused it to rise to 38.1% of GDP at the end of FY2021. However, according to IMF forecasts, it will fall to a reasonable 33.4% in FY2022. Morocco's position, likewise, is not of concern, having trended upwards slowly between 2010 (25.0% of GDP) to 2019 (32.7% of GDP). The position worsened in 2020 to 39.3% of GDP, a level around which it will remain in 2021 and 2022.

Chart 12: Oil Importers: External Debt as % of GDP, Various Years



Source: IMF/Baker Ing

However, once again the data for Jordan and Tunisia sends worrying signals for credit managers. Although Jordan's external debt as a percentage of GDP did not rise quickly in the period between 2010 and 2019, it started at a concerning level (59.9% of GDP) and was boosted by the pandemic to 79.8% of GDP. Worryingly, the IMF forecast the level will top 84% of GDP in 2022. Meanwhile, Tunisia's position is even worse. In 2010, external debt as a percentage of GDP was 48.7% and by 2020 it had reached 94.7% of GDP. The IMF is forecasting that it be 101.2% of GDP in 2022.

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External Developments: Currency Risks

Three of the countries, Egypt, Morocco and Tunisia, have floating exchange rates, reducing credit risk to a degree. Egypt's currency was only floated in late 2016 after which it depreciated sharply. However, since July 2017, it has slowly appreciated to average EGY15.82:1USD in 2020; a trend which will continue in 2021 but the pound will weaken slightly in 2022 to average EGY15.91:1USD. Morocco's currency has tended to fluctuate between MAD9:1USD and MAD10:1USD, a range in which it will remain in until the end of 2022.

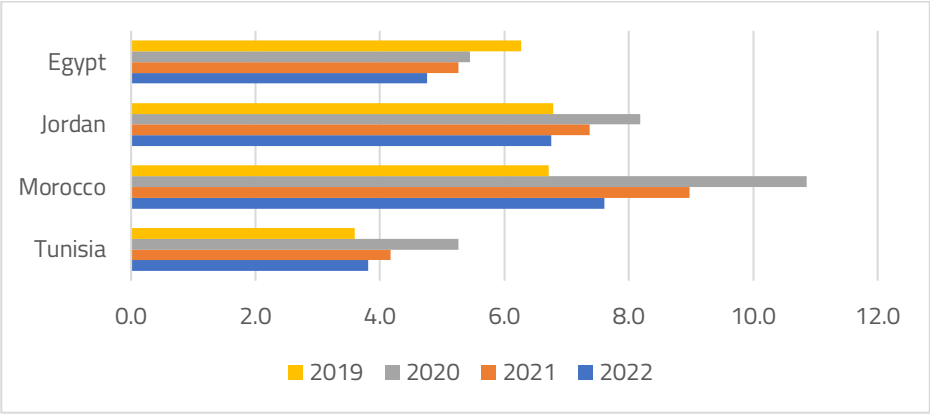
Tunisia's currency weakened consistently between mid-2011 and March 2019 (when it average TND3.054:1USD), with a sharper depreciation in the last nine months of the period. However, since then, despite the multiple problems facing the economy, the dinar has strengthened averaging TND2.744:1USD in May 2021. However, we believe this trend will reverse to the end of 2022, by which time the rate will be over TND3.10:1USD.

The Jordanian dinar has been pegged at JOD0.71:1USD for many decades. Although, the IMF has supported the policy, we feel that there is an increasing risk that Jordan will have to devalue the dinar as part of a package to reduce its unsustainable debt burden. It would be unclear if Jordan was merely re-peg at a lower rate or follow the Egyptian model of allowing the currency to float.

External Developments: FX Reserves

Importantly, FX reserves as measured in months' worth of imports for all four countries will remain over the 3-month minimum for emerging economies recommended by the IMF. The import compression experienced in 2020 as a result of the pandemic saw the levels improve in Jordan, Morocco and Tunisia. Indeed, we forecast the position will improve between 2019 and 2022 in Morocco (6.7 months to 7.6 months) and Tunisia (3.6 months to 3.8 months), while it will be unchanged in Jordan at 6.8 months. However, the worsening trend in Egypt will continue to leave import cover at 4.8 months.

Chart 13: Oil Importers, FX Reserves in Months of Imports, 2019-2022



Source: IMF/Baker Ing

Credit Risk

Credit risk in the five FCVs, Iraq, Lebanon, Libya, Syria and Yemen, will remain extreme over the next 12 months, at least. The future for credit risk in each case will be dictated by political actors and security events.

Iraq is probably the best placed for an improvement into the medium term due to its substantial oil revenues. However, progress will depend on whether Mustafa al-Kadhimi's government will be able to maintain a technocratic approach to the economy without alienating key ethno-religious political and militia groupings. Iraq's future prospects will also hinge on the policies of Ebrahim Raisi, the new hard-line president in Iran, towards its interests in Iraq, including the presence of Iranian militia groups.

Lebanon is in a critical position and the credit environment will only worsen until two events take place. First, a new, preferably technocratic, government needs to be formed; Lebanon has been without a government since August 2020. Second, the new government must conclude an agreement with the IMF, which is likely to include an end to the multiple exchange rates and an effective devaluation of the currency, as well as some form of debt rescheduling. However, the debt issue is opposed by the virtually bankrupt banking sector, which holds the vast majority of the government's debt.

Credit risk in **Libya** is slowly improving as the Government of National Unity (GNU), which was formed in March 2021, attempts to bridge the many divisions within the country. If the GNU can manage to keep the various militias onside and ensure that meddling by external actors, such as Turkey and Egypt, is kept to a minimum, then the prognosis is good. Like Iraq, Libya has plentiful oil reserves that could form the basis of economic growth, if used properly.

Syria is probably the worst placed of the five countries. Somehow, Bashar Al-Assad has survived a decade of civil war, outside intervention and the presence of radical Islamist groups. Until recently, in areas under his control, there was a nascent economic recovery but increased taxation in these areas, to fund his war effort, is starting to turn the population against him and see the economy start to struggle.

Yemen is another country where credit risk is nominally improving as external actors in the civil war, such as Saudi Arabia and the UAE, change tack and attempt to bring about reconciliation. However, as with Iraq, future prospects will be heavily influenced by the policies of Iran towards the Houthi rebels, which have been fighting the internationally recognised government since 2004. Another political issue that requires resolving is the claim by southern successionists to bring about a return to the two countries, North and South Yemen.

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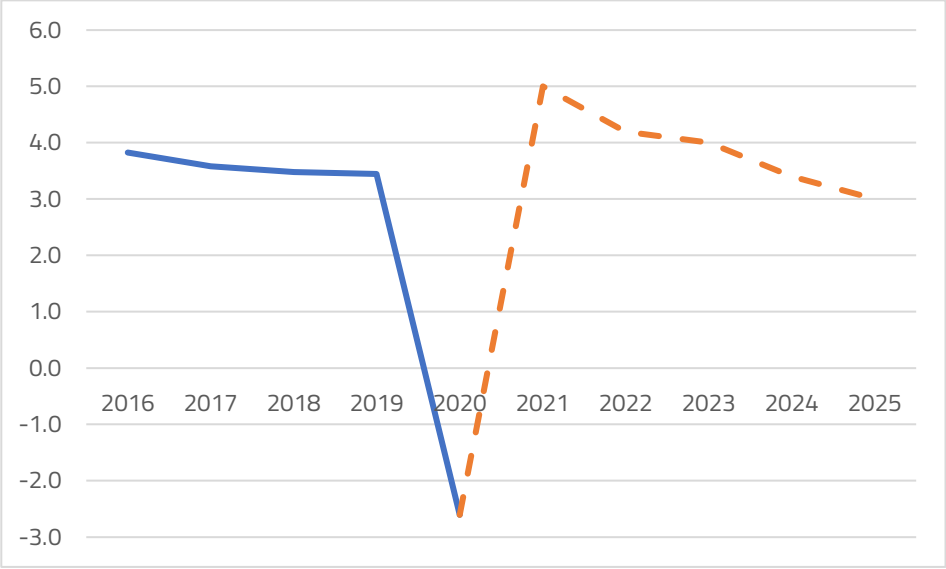
Israel

Economic Growth

Real GDP growth averaged 3.6% per year between 2016 and 2019. The sectors that contributed most strongly to growth in this period were information and communication, mining and quarrying, construction, wholesale and retail trade, and finance and insurance. As with most countries, Israel experienced a contraction in 2020 measuring 2.6%. The sectors that contributed positively towards growth in 2020 were mining and quarrying, and information and communications. However, construction, wholesale and retail trade, transportation and storage, and financial and insurance all contracted sharply.

Chart 14: Israel, Annual GDP Growth, %, 2016-2025



Source: IMF/Baker Ing

Looking ahead, we expect the economy to rebound strongly in 2021, growing by 5.0%. Israel has been a world leader in distributing the Covid-19 vaccines; as at 18 June, 56.9% of the population was fully vaccinated, which has enabled it to lift most restrictions. The structure of the economy will also support the rebound. The information and communication sector, in which Israel is a world leader, has weathered the pandemic globally because of the increased reliance on technology during working at home. The sector will continue to benefit in 2021 and 2022. In addition, the natural gas sector will continue to drive growth as domestic usage increase and exports to Egypt and Jordan increase. The tourism sector will also benefit from the success of the vaccine programme.

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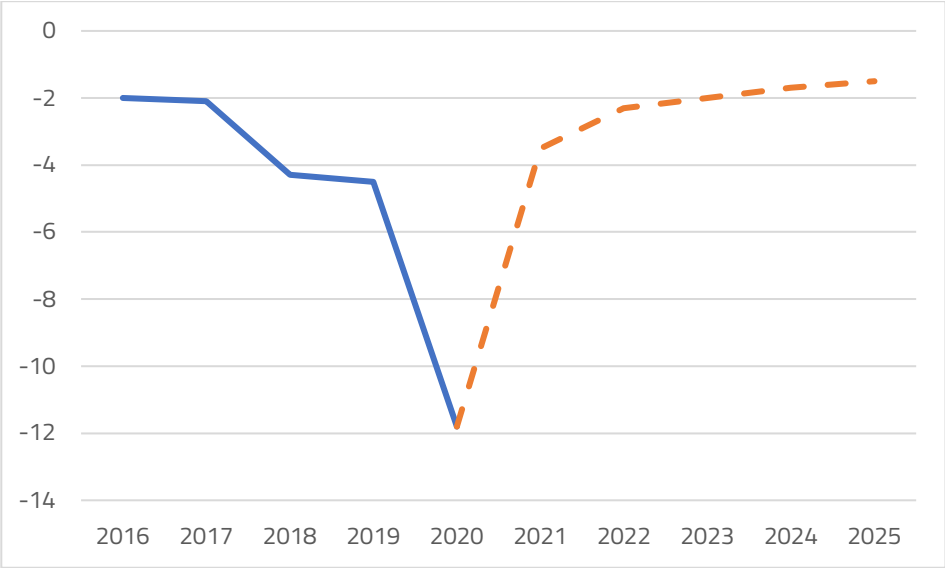
Fiscal Developments

Israel has a run a persistent low-level fiscal deficit in recent years. Since 2010, the government has run a two-year budget which has helped to boost market confidence. It is also committed to reducing its public debt levels to 60% of GDP, a target it had achieved in 2019. However, the cost of the policies to fight the pandemic saw the deficit rocket to 11.8% of GDP in 2020 as parliament approved fiscal packages totalling NIS202.3bn (equivalent to around 14.3% of GDP), of which NIS105.7bn were implemented in 2020 and NIS29.8bn in the first 4 months of 2021.

Chart 15: Israel, Fiscal Balance, % of GDP, 2016-2025



Source: IMF/Baker Ing

We expect the fiscal deficit to fall through to 2025, when it will be 1.5% of GDP. The sharp fall will be aided by the removal of restrictions in relation to Covid-19, which will boost business activity and therefore government revenues. However, as ever in Israel, if relations with the Palestinians result in military action being taken, as was the case in May this year, then the deficit will suffer on the back of the extra military spending.

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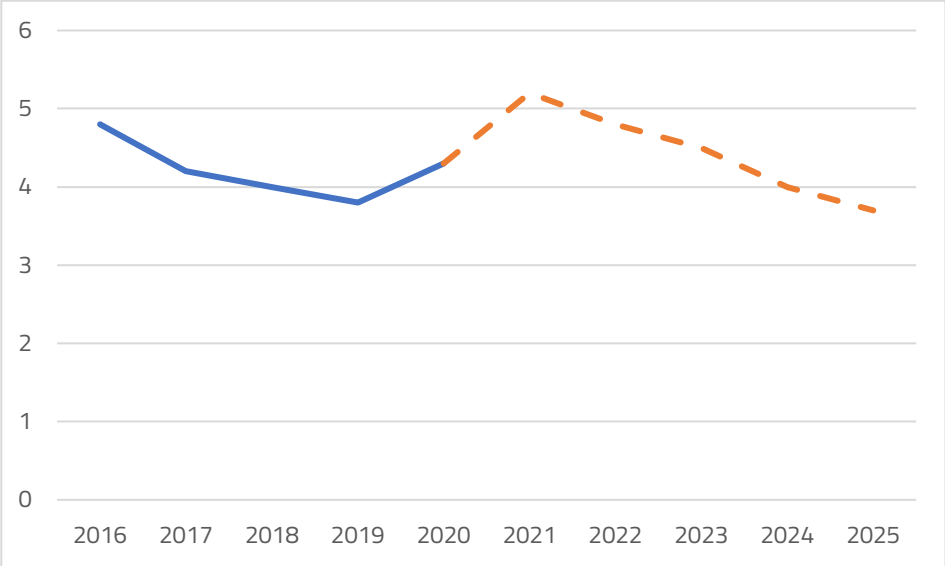
Unemployment

Unemployment in Israel increased from an annual average of 3.8% in 2019 (its lowest level this century) to an annual average of 4.3% in 2020 as a result of the slowdown in business activity following Covid-19 restrictions. In seasonally adjusted terms, full time employment in Israel was 3.7% lower in April 2021 than it was in January 2020, while part-time employment numbers had fallen by 9.9% in the same period. Unsurprisingly, those temporarily absent from work, which includes those furloughed, has risen by over 25% in the same period. Baker Ing predict that unemployment will rise further to 5.2% in 2021 as the government unwinds its furlough support before trending down to an annual average of 3.7% in 2025.

Chart 16: Israel, Annual Average Unemployment, %, 2016-2025



Source: IMF/Baker Ing

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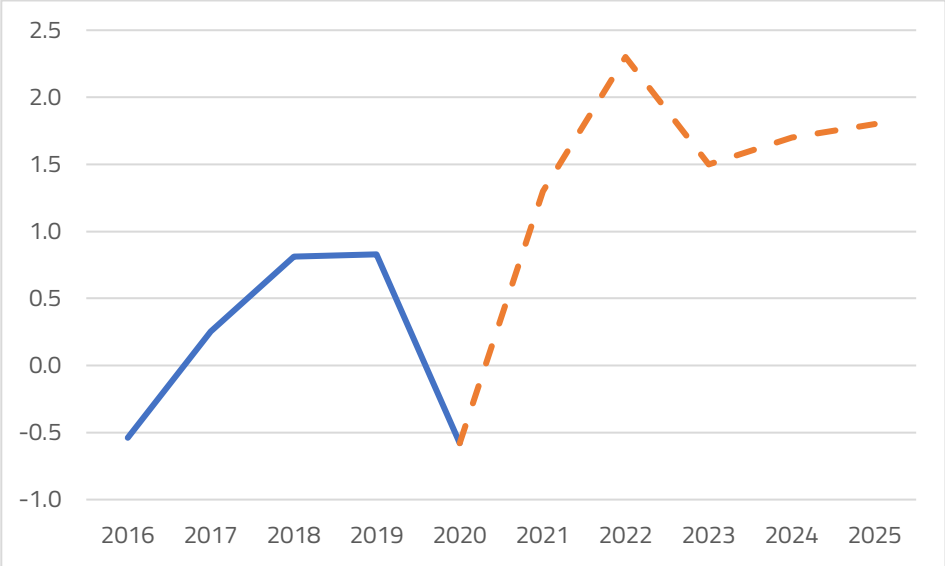
Inflation

In line with global trends Israeli inflation has been low over the past five years, with periods of deflation. Between March 2020 and January 2021 prices contracted in y/y terms each month, as demand was constrained by the pandemic. The demand weakness more than offset the impact of the strengthening shekel, which boosted import prices.

Chart 17: Israel, Annual Average Inflation, %, 2016-2025



Source: IMF/Baker Ing

Looking ahead, external drivers of inflation – increased commodity prices and transportation costs, alongside supply chain difficulties – and the strengthening of the shekel, adding to the cost of imports, as well as pent-up demand, will push prices upwards in 2021 (annual average of 1.3%) and 2022 (2.3%), before the supply side difficulties are resolved, and demand returns to levels nearer those experienced in the five years prior to the pandemic.

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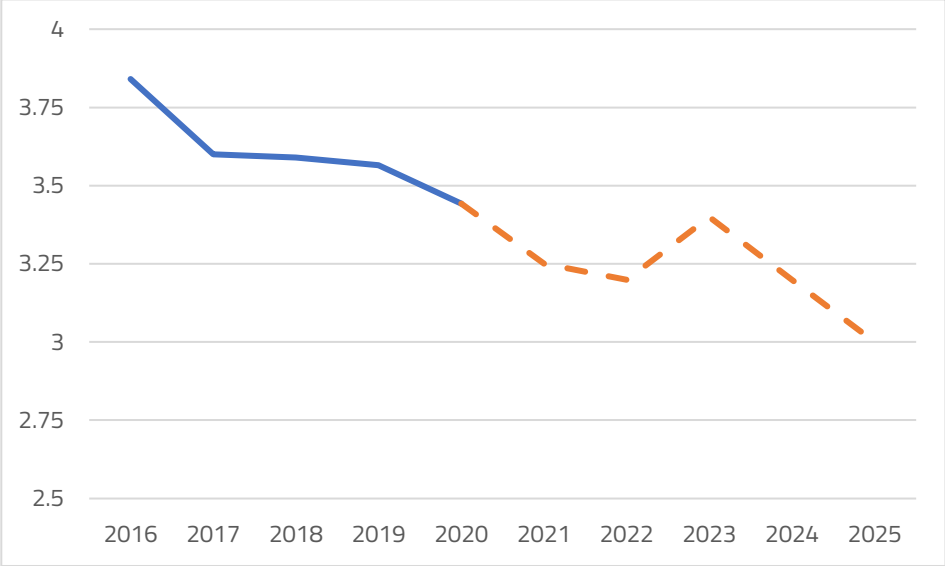
Currency Risk

The Israeli shekel slowly strengthened against the US dollar between 2015 when it averaged ISS3.89:1USD to 2019 when it was ISS3.56:1USD. Market uncertainty and a consequent flight to safety over the direction of the pandemic saw the appreciating trend reversed sharply in March 2021, when the average rate was ISS3.62:1USD. Although the shekel remained weak in April and May, by June it had appreciated to ISS3.46:1USD, stronger than in December 2019 (ISS3.47:1USD). It continued to appreciate throughout the rest of the year but weakened in Q1 2021.

Chart 18: Israel, Annual Average Exchange Rate, ISS:USD, 2016-2025



Source: IMF/Baker Ing

Looking ahead, we expect the shekel to appreciate to reach an annual average of ISS3.00:1USD in 2025. The strengthening will be driven by the strong current account surpluses, and strong macro-economic fundamentals including constrained fiscal deficits (see Chart 15).

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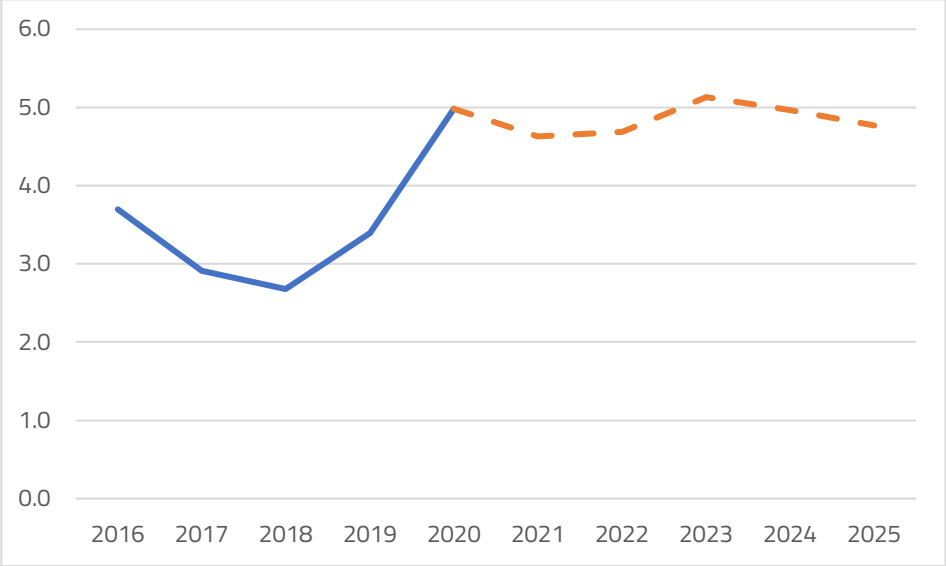
External Developments

Israel's external position is strong, supported by a persistent current account surplus, strong FX reserves as measured by months of imports (21.5 months at end of 2020 and forecast to climb to 28.9 months at end of 2025) and low (albeit climbing) external debt (32.9% of GDP at end of 2020).

Chart 19: Israel, Current Account, % of GDP, 2016-2025



Source: IMF/Baker Ing

In 2020, the current account surplus increased sharply to 5.0% of GDP (the highest level since 2015) due to import compression, while exports of gas and hi-tech equipment held up. As imports rebound in 2021 and 2022, we expect the surplus to fall to 4.6%-4.7% of GDP, before rebounding to average 5.0% of GDP between 2023 and 2025.

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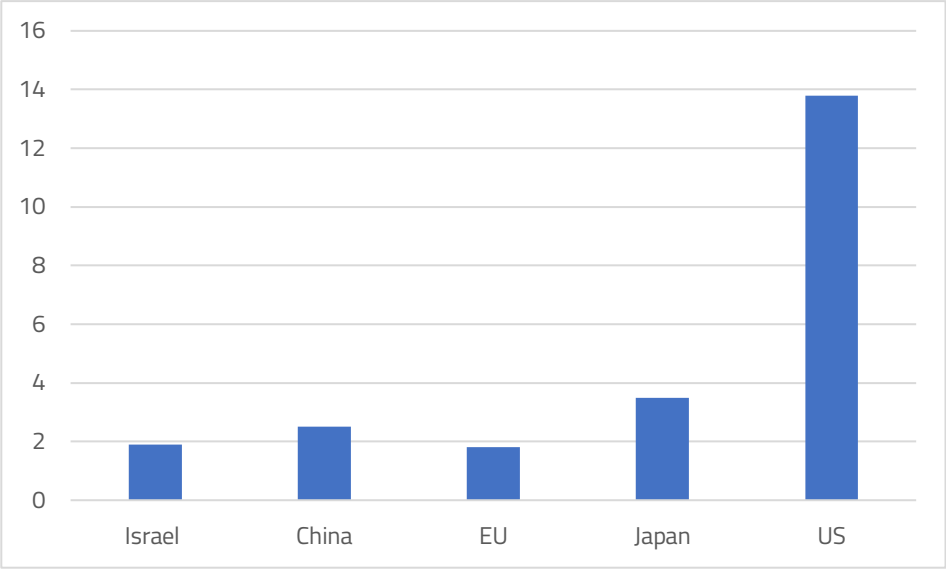
Trade Barriers

According to data for 2019 from the World Bank, trade barriers as measured by the applied weighted mean tariff rate are low in Israel. At 1.9%, they are better than the world average of 2.6%, China (2.5%) and Japan (3.5%). Furthermore, they are significantly better than the US at 13.8%, where Donald Trump applied significant tariffs on Chinese imports during his time as president. However, tariffs in Israel are higher than the countries in the EU (1.8%).

Chart 20: Tariff Rate, Applied Weighted Mean, %



Source: World Bank
Note: The weighted mean applied tariff is the average of effectively applied rates weighted by the product import shares corresponding to each partner country.

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Non-Trade Barriers

According to WTO data, Israel has applied very few non-tariff barriers in terms of anti-dumping (ADP) measures. In 2019, Israel introduced three ADP Final Measures, taking its cumulative total to 4. This compares very favourably with other large trading countries. Japan has only 7 measures in total, but China and the US were very active in 2019, implementing 12 and 33 respectively. China and the EU have over 100 ADP measures in total, while US is nearing 400 according to the latest data.

Table 2: ADP Final Measures

Non-Tariff Barriers	ADP Final Measures Implemented	ADP Final Measures Cumulative
Israel	3	4
China	12	107
EU	4	120
Japan	0	7
US	33	388

Source: WTO

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