COVID-19 pandemic

Global recession deeper than **2008**

World GDP

contraction by
3.2%

Global growth
contraction by **4.9%**

Sharp decline in oil prices

2020

simultaneous demand
and supply shocks

Decreases

in tourism and transport activities

deeply affected
employment creation

1 The Global Context and its Implications for the Arab Region

A. Global context

The COVID-19 pandemic began in the context of a global economic slowdown. Growth fell from 3 per cent in 2018 to 2.6 per cent in 2019, and trade activity weakened as a result of prolonged tensions between China and the United States. In 2019, these tensions spilled over into other areas, including uncertainty resulting from the exit of the United Kingdom from the European Union, and allegations of protectionism between the United States and the European Union that led to a slump in global trade activity of 0.3 per cent from 3.9 per cent, which was the lowest value since the 2008 global financial crisis. These negative developments affected supply chains and depressed global demand, leading to a fall in manufacturing activity, especially in China, Africa and the Middle East.

Another unfortunate event was the increase in global debt amidst exceptionally low interest rates in developed countries, causing real yields on 10-year government bonds to fall below zero in six of the largest developed economies. Developed countries benefited from these conditions by pursuing a more active fiscal policy. However, these benefits could not be extended to developing countries, which still need to pay high interest on their debts. The number of low-income countries in debt distress rose from 19 to 34 between 2016 and 2019. The shift of debt composition from long-term borrowing from the Paris Club towards more expensive short-term lending led to a surge in interest payments, and increased the cost of debt servicing in developing countries. These countries entered 2020 with a lack of fiscal space, which significantly limited their ability to appropriately respond to the COVID-19 crisis.

Massive worldwide lockdowns, coupled with significant decreases in tourism and transport activity, will shape the world economy for the next few years. World gross domestic product (GDP) is estimated to have contracted by 3.2 per cent in 2020, and is projected to recover in 2021 with a growth

Key messages

- The COVID-19 pandemic will cause a global recession deeper than the 2008 global financial crisis.
- World GDP is estimated to have contracted by 3.2 per cent in 2020, and is projected to recover in 2021 if the necessary conditions are implemented. Otherwise global growth could have contracted by 4.9 per cent.
- In 2020, the oil market underwent simultaneous demand and supply shocks that led to a sharp decline in oil prices, which reached its peak on 21 April 2020 when the price of West Texas Intermediate (WTI) oil allocated for delivery in May 2020 plunged below zero.
- The current global crisis will have a deep impact on the Arab region. The fall in global demand for energy will affect Arab oil exporters. Furthermore, decreases in tourism and transport activities will have a deep impact on growth and employment creation in many middle-income countries (MICs). The deteriorating economic situation in developed countries will also affect the inflow of investments, remittances and official development assistance (ODA) to Arab least developed and conflict-affected countries.

rate of 4.2 per cent (baseline scenario). The recovery is conditioned on the speed at which economies will return to their long-term trends; the level of investor and consumer confidence; and the effectiveness of stimulus packages enacted by Governments in response to COVID-19. If these conditions are not met and a second wave of the pandemic occurs, the situation could be worse and the global economy could have contracted by 4.9 per cent in 2020 (pessimistic scenario). The recovery in 2021 will be only slightly better at 5.4 per cent, too low to compensate for the higher GDP loss witnessed in 2020.

In developed economies, growth slowed drastically from 2.3 per cent in 2018 to 1.9 per cent in 2019, even before the COVID-19 outbreak. This grim picture will not improve soon, as the United States is estimated to have contracted by almost 5 per cent in 2020 and is expected to moderately recover in 2021 with a growth rate of 3.9 per cent (8 per cent and 4.5 per cent, respectively, in the pessimistic scenario). Similarly, the European Union is estimated to have lost more than 5.5 per cent of GDP in 2020 and is expected to recover by 2.8 per cent in 2021 (-10.2 per cent and 6 per cent, respectively, in the pessimistic scenario). In developing countries, the outlook has also been revised downwards. In 2020, they are estimated to have lost 0.5 per cent of their GDP (-1 per cent in the pessimistic scenario). India is projected to avoid recession with a 1.2 per cent growth rate, owing to credit easing and fiscal stimulus in 2019 (the pessimistic scenario projects a 4.5 per cent recession). Southeast Asia is the only region to avoid recession in the baseline scenario, with 0.8 per cent growth projected despite a slump in tourist activities and disruptions to production chains (the pessimistic scenario envisages a 2 per cent recession). As Southeast Asian countries swiftly and effectively contained and managed COVID-19, they benefited from resuming production activities while other developed economies remained under lockdown.

The economic outlook for Africa and other economies in transition is affected by low commodity prices. African economies are estimated to have lost 1.6 per cent of their GDP in 2020 before recording a partial recovery in 2021, with a 3.4 per cent GDP growth rate (the slump is deeper in the pessimistic scenario at 3.2 per cent). The ability of developing countries to enact fiscal stimulus is an additional challenge as government revenues will decrease sharply owing to the commodity glut, leading to an inability to provide adequate support for societies hit by lockdown measures. Contrary to developed economies, these countries are also facing much stricter borrowing constraints, further reducing their ability to provide support for the most vulnerable.

In the context of this economic slowdown and falling commodity prices, global inflation remained low in 2019. In developed economies,

5% **2020**

The **United States** is estimated to have contracted by almost **5 per cent** in 2020 and is expected to moderately recover in 2021 with a growth rate of **3.9 per cent**

5.5% **2020**

The **European Union** is estimated to have lost more than **5.5 per cent** of GDP in 2020 and is expected to recover by **2.8 per cent** in 2021

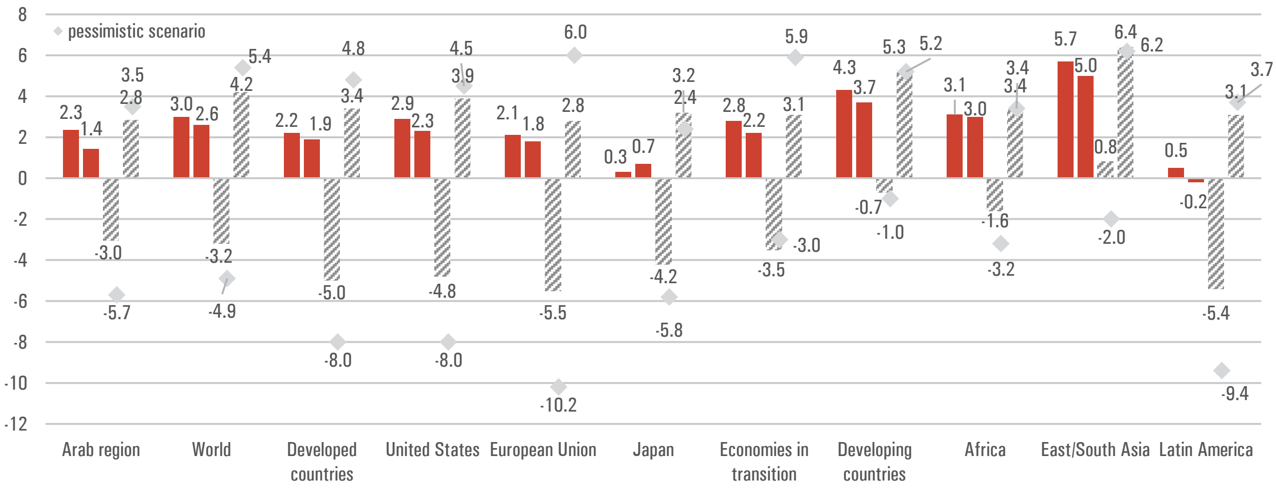
0.5% **2020**

Developing countries are estimated to have lost **0.5 per cent** of their GDP

0.8%

Southeast Asia is the only region to avoid recession, with **0.8 per cent** growth projected

Figure 1.1 **GDP in selected regions and countries, 2018-2021**



Sources: Based on the internal forecast received from DESA/Project LINK; and DESA, *World Economic Situation and Prospects 2020* (New York, 2020).

inflation weakened from 2.4 per cent in 2018 to 1.8 per cent in 2019. The escalation of tariffs in major economies pushed up producer prices in some sectors, but lower energy prices and low inflation in the services sector have generally reduced consumer price inflation. In some developed countries, low inflation rates coupled with declining inflation expectations have undermined the credibility of central banks to meet near-term inflation targets.

The pandemic will speed up this trend. Inflation slowed down in 2020 as a result of the slump in oil prices and the decline of global demand. In contrast, monetary stimulus, which will lead to significant increases in the money supply, may outweigh this effect in 2021, especially in developing countries where central banks would need to monetize additional expenditures given their inability to place debt on the financial markets. Consequently, after low inflation in 2020, a sharp increase in prices is expected towards 2021, provided that monetary stimuli enacted by developed countries worldwide are successful in restoring consumer and investment demand.

Interest rates were stable in the United States and the European Union in 2019, following an increase in 2018. However, bond yields fell, reflecting greater uncertainty resulting from trade tensions. Between November 2018 and February 2020, the two-year United States treasury bond yield

1.8%

In developed economies, inflation weakened from **2.4 per cent** in 2018 to **1.8 per cent** in 2019

1.2%

Two-year United States treasury bond yield decreased from **2.9 per cent** to **1.2 per cent** decreased by 1.7 percentage points from 2.9 per cent to 1.2 per cent, despite the constant target band. Increased uncertainty following the COVID-19 outbreak led to a rapid decrease in both two-year and 10-year bond yields. These developments were paired with a rapid and extensive decrease in the Federal Open Market Committee's target federal funds rate, meaning a significant expansion of open market operations and the purchase of Treasury and agencies' securities as needed. The two-year bond yield fell to near-zero, while the 10-year bond yield was around 0.7 per cent at the beginning of June 2020. Furthermore, the Federal Reserve pushed forward a large package of measures to facilitate the flow of credit, including facilities to ease the issuance of commercial papers by companies and municipalities, the provision of additional loans to depository institutions, and the purchase of loans from companies. This unprecedented set of instruments injected additional, almost unconstrained, liquidity to the market.

In 2019, the London Interbank Offered Rate (LIBOR) decreased in line with the treasury bonds rate. Between November 2018 and February 2020, LIBOR fell by 1.1 percentage points from 2.7 per cent to 1.6 per cent. Amidst uncertainty related to COVID-19, the volatility of the Treasury-Eurodollar (TED) spread (between the 3-month LIBOR and the 3-month United States Treasury Bill yield) increased, and reached 1.4 per cent in March and April 2020, levels unobserved since the global financial crisis in 2009. LIBOR also fell to 0.5 per cent, unobserved since 2015.

Low interest rates were unable to stimulate GDP and investment growth. Inflation rates worldwide remained low despite a few years of loose monetary policy. The European Central Bank's policy rate remained zero over the period 2019-2020. The yield of German bonds fell below zero at the beginning of 2019 and remained there over the period 2019-2020, reflecting investors' belief that low interest rates are here to stay over the next couple of years. Furthermore, the yield of two-year bonds fluctuated between -0.6 per cent and -0.8 per cent, leaving no space for further decreases to support companies following the COVID-19 crisis. A prolonged period of very low interest rates raised concerns among economists about the impact of these developments on efficiency.

Liu and others (2019) argue that persistently low long-term interest rates encourage market concentration, reducing business dynamism and productivity growth. Moreover, the Bank for International Settlements (2019) shows that prolonged low rates may also delay the shifting of resources from less productive sectors to more productive ones, which could result in an increase in zombie firms or overinvestment in private construction. These concerns will be even more pronounced following the 2020 stimulus packages enacted in developed economies to support businesses after the COVID-19 shock.

When exchange rates are considered, the euro continued its earlier depreciation against the dollar in 2019 and early 2020, reflecting differences in policy stance between European and American monetary authorities. It is

too early to judge whether COVID-19 has significantly affected the trend in the dollar/euro rate, but differences in developed economies' responses to COVID-19 increased the volatility of the exchange rate and presumably led to a reversal of the downward dollar/euro trend. Since late 2019, the dollar has depreciated against the Japanese yen. As in the case of the euro, the yen/dollar rates witnessed increased volatility following the COVID-19 outbreak. In contrast, the depreciation of the Chinese renminbi against the dollar was reversed following a trade deal signed in January 2020. In early 2020, the renminbi/dollar relationship remained relatively stable despite the COVID-19 turmoil.

Concerning global trade, 2019 was marked by heightened trade tensions between major actors in the global economy, which deeply disrupted the global value chain. Global trade grew at 0.3 per cent, the lowest level in a decade. Sectors with complex production chains, such as machinery, electronics and automotive industries, have been particularly affected. Some countries benefited from the redeployment of production sites, but the global economy was nevertheless negatively impacted. COVID-19 could represent an additional risk to globalization. The rapid spread of the virus that was attributed to globalization has strengthened anti-mundialization movements and intensified protectionist measures among member States of the World Trade Organization.

B. Natural resource commodities

Oil Natural gas and phosphate

Oil

In 2020, the oil market underwent simultaneous demand and supply shocks. In 2019, global oil demand was already low averaging an estimated 99.74 million barrels per day (Mb/d), lower than the projected demand of 100.5 Mb/d. Even before the COVID-19 shock, oil market prospects were rather grim: falling expectations of global growth amidst trade tensions decreased the global demand for oil. Political tensions in Iraq and Libya increased geopolitical uncertainty, leading to slight surges in oil prices at the turn of 2019 and 2020. Nonetheless, the assassination of General Qasem Soleimani, along with fears surrounding reduced oil demand from China, quickly contributed to the reversal of that increasing trend.

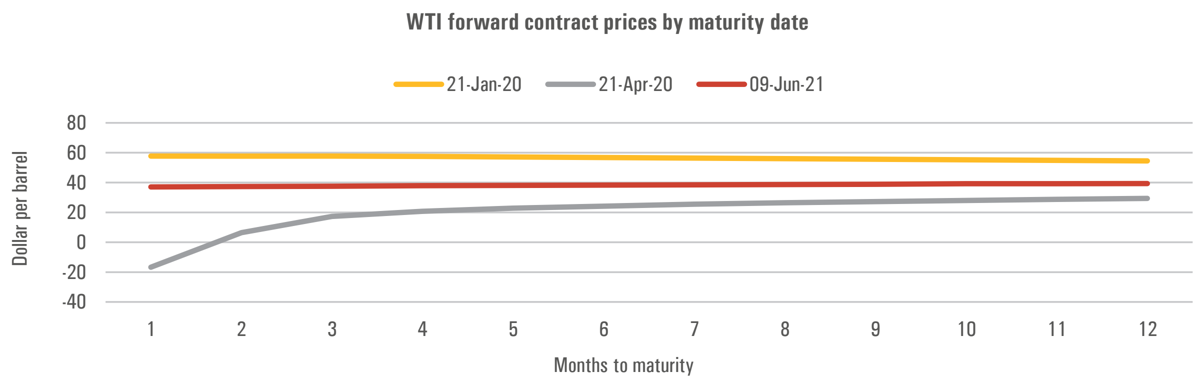
In the first quarter of 2020, oil prices reacted strongly to a demand shock resulting from the COVID-19 outbreak in China, the world's largest crude oil importer. Brent fell to $58/barrel in January and to $45.2/barrel in February. In view of market developments, the Heads of Delegation of the Organization for Economic Cooperation and Development (OPEC) Conference, held on 5 March 2020, recommended extending the duration of the proposed 1.5 Mb/d additional adjustment until the end of 2020, instead of 30 June 2020. On 9 March 2020, oil prices collapsed following a supply shock, resulting from a disagreement between the Russian Federation and Saudi Arabia. The latter promptly offered discounts to customers and announced an increase in outputs starting in April 2020. The price of Brent crude oil fell from almost $50/barrel on 5 March to below $32.02/barrel on 9 March 2020. Prices fell below $23/barrel by the end of the first quarter of 2020, and to less than $15/barrel a week later. This price war ended with an agreement on 12 April 2020, signed collectively by 23 countries, to cut global oil production by an unprecedented 9.7 Mb/d. Even though this measure stopped the rapid decrease in oil prices (in May 2020, the average price of Brent oil equalled $29/barrel), prospects for the first quarter of 2021 are unstable. Nevertheless, hopes for a quick rebound paired with monetary stimulus led to an increase in the price of Brent oil by 22 per cent between April and May 2020, the biggest percentage increase since 1999.

Given this volatility, predicting oil price developments has become increasingly difficult. To predict prices over the next few years, a vector autoregression (VAR) model was employed, including oil production, inventories and industrial production as a proxy of demand. The model predicts that oil prices will rebound slightly to $37/barrel in 2021 and $50/barrel in 2022, if the outbreak is contained and recovery follows. However, if this is not the case and a second COVID-19 wave hits the global economy, low oil prices may be here to stay in 2021 and 2022. However, if the stimulus packages employed worldwide are efficient in recovering demand, a return to pre-COVID levels may happen in 2021.

Box 1.1 **Negative oil prices**

The price of WTI oil allocated for delivery in May 2020 plunged below zero on 21 April 2020, with significant media coverage worldwide. This was the last day of trading for May 2020 contracts, when demand plummeted owing to the lockdown across the United States, and the fact that storage facilities in Cushing, Oklahoma, where the oil was supposed to be delivered, were already full. As there was no possibility to store such a huge oil surplus, investors had to pay to get rid of contracts that could not be executed, leading to negative oil prices. The negative oil prices were a one-off event, resulting from significant mismatch between oil production, consumption and storage capacities, not from fundamental changes in the global markets, and are unlikely to persist in the long term.

Source: Compiled by ESCWA.



Source: ESCWA staff calculations based on the Yahoo Finance database (accessed on 8 June 2020).

Table 1.1 OPEC basket prices, 2018-2022

				Forecast average		
Year	**Monthly minimum**	**Average**	**Monthly maximum**	**Lower bound**	**Average**	**Upper bound**
2018	56.9	69.5	79.4			
2019	58.7	64.1	70.8			
2020				20.6	32.6	44.6
2021				11.3	37.0	62.7
2022				24.3	50.0	75.6

Sources: Figures for 2016-2018 are "OPEC reference basket prices" (accessed on 8 June 2020); figures for 2019 and 2020 are ESCWA staff forecasts (as of May 2019) where a VAR model is employed with a method of least squares (Gauss-Newton/Marquardt steps), incorporating monthly variables of OPEC reference basket price, OPEC and non-OPEC production, industrial production indices for G7 and China as a proxy of demand, United States inventories, the Consumer Price Index and dollar-trade weighted basket exchange rate, most of which are based on national statistical sources. Lower and upper bounds are 95 per cent-confidence intervals.

Nevertheless, in May 2020, oil production was still well below the 2019 level at 88 Mb/d, more than 12 Mb/d below pre-crisis production and 9.5 Mb/d below May 2019. The decrease in production reported among OPEC countries is quite homogenous, a 17 per cent fall on average in comparison to May 2019 and 15 per cent relative to January 2020, except Libya that is experiencing civil unrest and an almost complete halt of production activity, and Venezuela that is struggling with a highly volatile political situation and a 29 per cent fall in production. Nigeria and Equatorial Guinea are on the other side of the spectrum, with a 1 per cent and 9 per cent reduction, respectively. Non-OPEC production cuts are smaller on average, with just 7.4 per cent year-on-year production cuts, with countries such as Australia and Norway showing production growth. Canada, the Russian Federation and the United States are in the middle of this spectrum, with 18, 15 and 7 per cent cuts, respectively.

In the Arab region, Qatar was the only country to increase production between May 2019 and May 2020. Other countries cut production by 14-19 per cent, while the decline in Egypt and Iraq was smaller at around 8 per cent and 10 per cent, respectively. Oil production in Libya almost halted. Non-OPEC oil production for 2020 has been revised down by 0.10 Mb/d and estimated at 2.25 Mb/d. This downward revision was partially affected by updates in the production estimations of Norway and Latin America. Production in the United States was revised down and is estimated at 166 tb/d. Columbia, Egypt, Indonesia and Thailand are estimated to have witnessed the largest declines in oil production.[1]

Arab region

Qatar was the only country to **increase production** between **May 2019** and **May 2020**. Other countries **cut production** by **14-19 per cent**, while the **decline** in **Egypt** and **Iraq** was smaller at around **8 per cent** and **10 per cent.**

Oil production in Libya almost halted

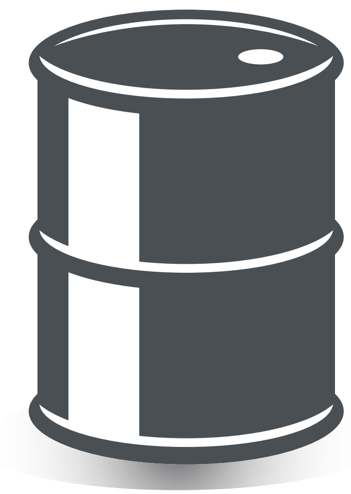
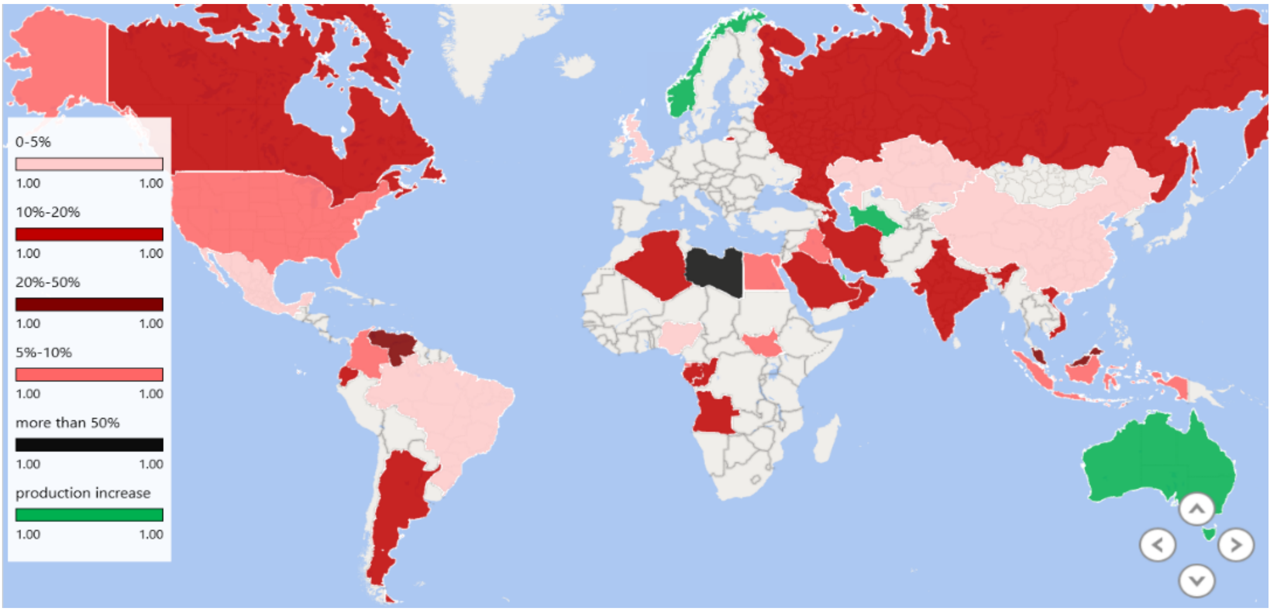


Figure 1.2 **Oil production cuts between May 2019 and May 2020**

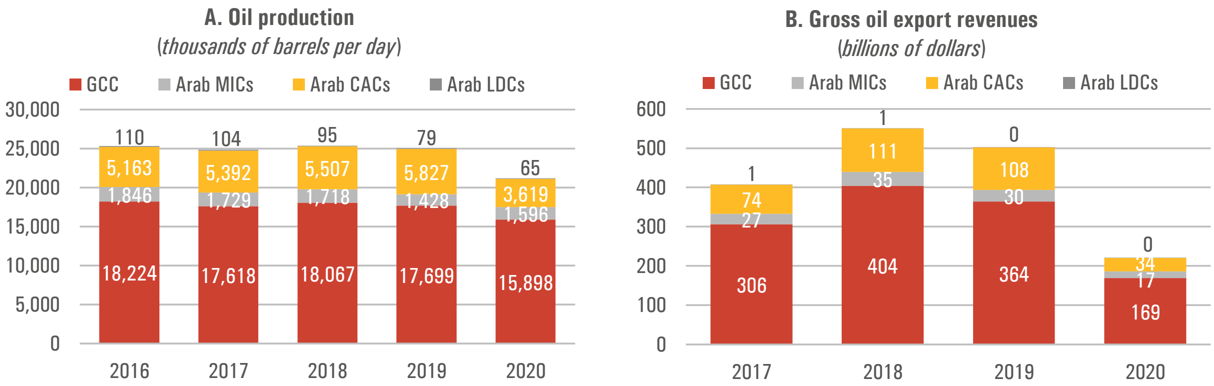


Sources: ESCWA staff estimations/forecasts based on national statistical sources; EIA, Short-Term Energy Outlook Data Browser (accessed on 3 June 2020).

In 2020, massive lockdowns and social distancing measures led people to avoid or minimize transport use, significantly decreasing demand for petroleum products and leading to the biggest oil glut in history. The aviation industry effectively stopped and its rebound prospects in the first half of 2021 are uncertain. Demand for oil in China in the first quarter of 2020 fell by 13 per cent. According to the International Energy Agency (IEA) projections, global demand for crude oil in 2020 was to fall by 8.3 Mb/d to 92.5 Mb/d overall, but demand in April 2020 was lower by a considerable 23.1 Mb/d, so demand is conditioned on developments over 2021. For instance, if the lockdown measures are eased and the global economy quickly rebounds, the annual decline in oil demand may be limited to 6.5 Mb/d.

The COVID-19 and oil price crises have had a devastating effect on Arab oil exporters' revenues. Average oil production over the first three months of 2020 was 15 per cent lower than in the previous year. This was already the case before OPEC's agreement signed on 12 April 2020, so further cuts are likely. With a 50 per cent fall in the average price of oil, revenues in 2020 are estimated to

Figure 1.3 **Oil production and export dynamics in the Arab region**



Sources: ESCWA staff estimations/forecasts based on national statistical sources; the OPEC, *Monthly Oil Market Report* (2019); the Joint Organizations Data Initiative database. Available at http://www.jodidb.org/TableViewer/tableView.aspx?ReportId=93904 (accessed on 3 June 2020); and the Organization of Arab Petroleum Exporting Countries databank (accessed on 3 June 2020).

Note: For 2020, only the first three months are considered. The developments over the remainder of the year will be crucial for the final result.

be at 44 per cent of 2019 income (figure 1.3B). Moreover, risks are skewed downwards given the international fear of a potential second COVID-19 wave, the highly uncertain global recovery, and a permanent fall in tourism caused by a drop in household disposable income, and strict COVID-19 regulations in the aviation sector. Furthermore, low oil prices and a lack of revenues may slow investments in the extraction sector, leading to limited production capacity in the Arab region. At the subregional level, all country groupings are significantly affected, with countries in conflict (mostly Iraq and Libya) losing 69 per cent of revenues, Arab least developed countries (LDCs) around 58 per cent, Gulf Cooperation Council (GCC) countries around 54 per cent, and Arab MICs (mostly Algeria and Egypt) around 43 per cent. The most affected, however, are GCC countries, given the importance of oil revenues for their State budgets.

Natural gas and phosphate

Natural gas is another important hydrocarbon-related source of income for the Arab region. Algeria, Egypt, Libya, Qatar and the United Arab Emirates are members of the Gas Exporting Countries Forum (GECF), which not only collectively controls nearly 70 per cent of the world's natural gas reserves but also accounts for over 40 per cent of global production. Over the past few years, the strategic importance of natural gas for many Arab countries has increased as global demand for natural gas rose in 2019 by 1.8 per cent, which is a slowdown from 2018 but in line with average demand increase over the period 2000-2017. Furthermore, the fall in demand for natural gas in 2020 is much smaller than that of oil, and is expected to equal 4 per cent or 150 billion cubic meters.[2] Constant growth in demand for natural gas is further supported by countries' collective need countries to improve environmental sustainability in the residential and industrial sectors. Given that COVID-19 may facilitate such a transition (since the recovery funds in the European Union would benefit from green investment), the change in demand may be less negative or even positive.

Global trade in liquefied natural gas (LNG) increased in 2019 by 12 per cent, or over 50 billion cubic meters, fuelled mostly by an increase in demand from Europe, which alone absorbed 80 per cent of incremental LNG trade. In addition, this growth was mostly due to a switch from coal towards cleaner natural gas, in line with global trends and should continue in the future. The output of gas-fired power plants in Europe and the United States increased in 2019 by 11 per cent and 8 per cent, respectively, mostly replacing old coal-fired units.

The COVID-19 pandemic and the global oil crisis continue to impact the natural gas industry given the tight relationship between these two markets. In the short term, the magnitude of gas demand will be a function of three factors, namely the impact of COVID-19 on the growth of the world economy, the advantages of gas compared to other fuels in terms of prices, and the potential advantages of natural gas as a clean alternative source of energy compared to other fossil fuels. According to IEA, the decline will be most significant in Europe and North America. In Asia, which is the main destination of LNG extracted by Arab countries, the fall in demand will be somewhat smaller, about 12 billion cubic meters compared with over 40 billion cubic meters in North America and Europe.

Amidst a mild winter in Europe, COVID-19 related lockdowns and continued supply growth, the European and American prices of LNG fell to levels not seen during the last decade. In Europe, they fell by more than three-quarters over the year and half, from $7.26/MMBtu in January 2019 to $1.58/MMBtu in May 2020.

In North America, the decline was smaller because of the lower base prices in January 2019, when gas was priced at $3.08/MMBtu. By May 2020, it fell to $1.75/MMBtu. Owing to the nature of Asian LNG contracts, which are indexed to oil prices with a three to six-month lag, gas prices fell by only 16 per cent between January 2019 and May 2020. Furthermore, global spread in gas prices is tightening, limiting the opportunities for arbitrage by sellers.

In the Arab region, GECF members are the most impacted by this crisis. In 2019, Qatar remained the largest global LNG exporter with a 21 per cent share in global exports, followed by Australia and the United States at 77.8 MT of LNG. Moreover, Algeria and Egypt added more than 2 MT of additional capacity each, with the Idku facility in Egypt reaching its full potential. Oman, Qatar and the United Arab Emirates also increased their capacity, but to a much smaller extent. Qatar has proposed a plan to increase liquefaction capacity by 49 MTPA to 126 MTPA by 2027. These developments should allow Qatar to remain among the world's most significant gas exporters. Oman announced a debottlenecking exercise to increase capacity of its three trains at Qualhat, from 10.4 MTPA to 11.5 MTPA by 2021.

Before COVID-19, the global phosphate rock supply was projected to increase from 235 to 255 MT between 2018 and 2023, and phosphoric acid from 101 to 111 MT with Africa being the largest contributor. The COVID-19 crisis will reduce supply of phosphate fertilizers from China, given production disruptions and lockdowns. However, demand for phosphates is also expected to decrease in line with a fall in production activities. In 2019, global prices of both phosphate rock and diammonium phosphate (DAP) fell by about 30 per cent from $102 and $382 to $72 and $238 per metric ton, respectively, because of an increase in production capacity paired with a sluggish demand surge. This recent price decline is the continuation of a longer trend that can be attributed to dynamics in China and other countries whose imports shrank due to their Governments lowering consumption of chemical fertilizers because of growing environmental concerns. Contrary to gas and oil, the COVID-19 did not significantly change the prices of both DAP and phosphate rock between January and May 2020. Production capacity in Arab countries increased, particularly in Algeria, Egypt, Morocco, Saudi Arabia and Tunisia. In Tunisia, the production of phosphate increased to 5.5 MT in 2019 compared with 4.1 MT in 2018, owing to the reopening of the Meknassy phosphate mine (Sidi Bouzid Governorate) that had been blocked since 2013, with a projected production of 600,000 tones, and the reopening of M'dhilla II in March 2020. Arab phosphate producers may benefit from the lower prices of oil and gas, which serve as a main source of sulphur and ammonia used as raw material in phosphoric acid and DAP production.

European and American prices of LNG fell to levels not seen during the last decade

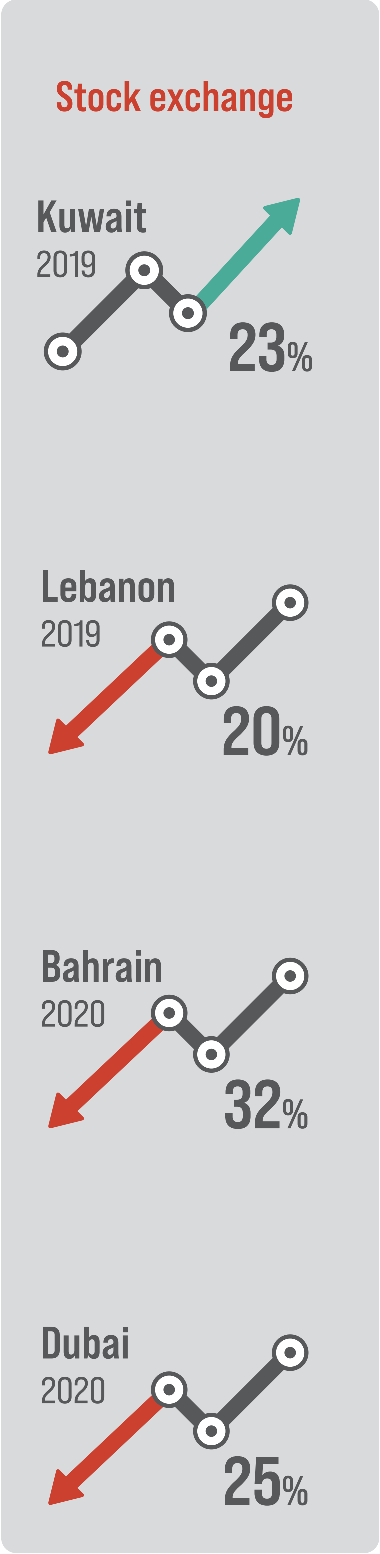
In the Arab region, GECF members are the most impacted by the crisis

C. Financial and trade linkages to the Arab region

Most GCC stock exchanges performed well in 2019, with Kuwait leading with a 23.7 per cent increase, probably owing to the decision by Morgan Stanley Capital International to include it as an emerging market. Bahrain rose by 20.4 per cent, Dubai 9.3 per cent, and Abu Dhabi and Saudi Arabia recorded modest increases of 3.3 and 7.2 per cent, respectively. In contrast, Oman lost 7.9 per cent. The most significant event for GCC countries' stock exchange was the initial public offering of Saudi Aramco, with the valuation briefly touching $2 trillion and increasing market capitalization of the Saudi stock exchange by 389 per cent. However, Saudi Aramco's stock fell by more than 20 per cent by the end of March 2020.

Other Arab stock markets fared much worse. Shares of Lebanese companies in 2019 were among the worst investments in the world, losing 20 per cent amidst protests and a deteriorating economic situation. The Amman Stock Exchange lost 4.9 per cent, and the Tunisia Stock Market dropped 2.6 per cent. The Egyptian and Moroccan stock markets, which rose by 6.6 per cent and 9.3 per cent, respectively, were star performers compared with other Arab MICs. Moreover, compared with the S&P 500 Index that rose by 28.9 per cent, and conflict-affected countries (CACs) 40, which rose by 26.4 per cent, the performance of Arab stock exchanges was poor. Arab financial markets (except GCC countries) did not manage to attract foreign investors. With the COVID-19 pandemic, these shortcomings may become even more pronounced. However, the value of shares traded in the Arab stock exchange as a percentage of GDP is relatively low (except for Saudi Arabia) and the financial interlinkages with the rest of the world are rather weak, which may limit the transmission of the COVID-19 shock to Arab financial systems.

COVID-19 caused further drops in the market capitalizations of stock exchanges in Arab countries over the first five months of 2020, especially in GCC countries. As of mid-June, Dubai had lost 25 per cent and Bahrain 32 per cent compared with 2019. Furthermore, Beirut, Iraq and Doha markets were down in mid-June by 27, 22 and 15 per cent, respectively. These losses are from an already low base and can be attributed to the fall in oil prices in Iraq and Qatar, and the dire economic situation in Lebanon. In addition, while GCC countries have some space to execute monetary stimulus (Saudi Arabia more than halved interest rates from January 2020, the United Arab Emirates lowered them by 36 per cent and Kuwait by 37 per cent), this is not possible in the case of Lebanon that is struggling with a massive debt crisis. These developments, and the return of oil prices to long run equilibrium, should lead to some rebound of GCC stock exchanges in 2021.

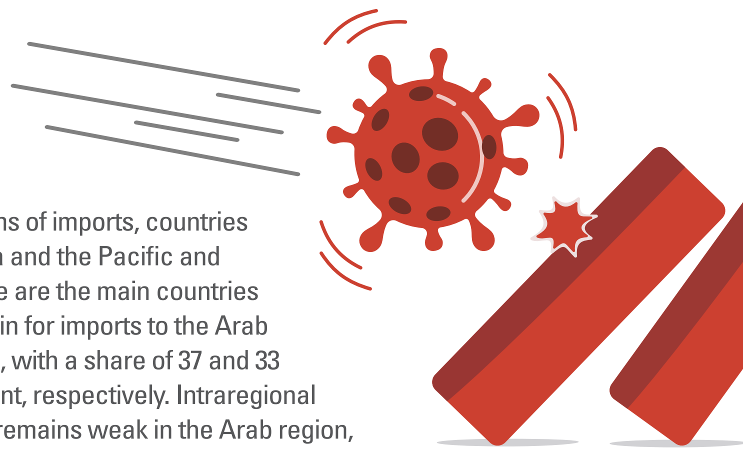


The external financial wealth of Arab countries can be explained by an evolution of total cross-border claims and total cross-border liabilities, based on data from the Bank for International Settlements. In 2019, total liabilities (Arab clients' deposits with main international banks) increased by 4.1 per cent, while total claims (borrowings by Arab clients from main international banks) increased by 7.5 per cent, indicating a decrease in the wealth of the Arab region compared with the rest of the world. However, the Arab region remained a net lender to the main international banks, with $131 billion as at December 2019. Saudi Arabia ($124.5 billion) and Kuwait ($73.9 billion) were the largest net lenders in 2019, whereas Qatar ($76.2 billion) and the United Arab Emirates ($15.4 billion) were the biggest net borrowers. However, all these numbers are smaller in 2019 than they were in 2018. Given the huge shock to oil prices in 2020, the net financial situation of Arab countries is estimated to have further deteriorated.

Financing costs in Arab countries slowly decreased over 2019 in line with a fall in the dollar three-month LIBOR. Moreover, the sudden cut in financing costs caused by the American Federal Reserve's unprecedented decision to reduce interest rates by 50 basis points on 3 March 2020 and a further 100 points on 16 March 2020 led to a parallel movement in Arab interest rates. While financing costs in GCC countries remained similar to the USD LIBOR, the spread between three-months JODIBOR (Jordan) and USD LIBOR remained at a relatively high level of 4 per cent.

Even though the financial condition of Arab banks remained stable in 2019, the pandemic will result in earning shocks that banks in Arab countries will have to manage. GCC countries will experience a slowdown in lending caused by a sharp decline in oil prices and COVID-19. As enterprises' financial indicators deteriorate, banks will need to focus on maintaining asset quality rather than on expanding their business. Nevertheless, the capital buffers of GCC banks are strong and banks should remain profitable. On the other hand, banks in countries such as Egypt, Jordan, Morocco and Tunisia will struggle to make profit given the rapid decline in tourism activity. The once thriving Lebanese banking sector is facing solvency risks owing to measures by the Lebanese Central Bank and currency depreciation, meaning that the country may be unable to meet its foreign currency obligations. Furthermore, Lebanese banks are directly affected by the Eurobond default, which represented 6 per cent of their balance sheets as of January 2020. Algeria will also face risks of downturn in oil and gas prices, and banks in other Arab MICs will have to bear the costs of decline in tourists inflow.

In terms of international trade, the Arab region continued to be a net exporter in 2019. Total exports reached around $902 billion, a 5 per cent decrease from 2018 mainly owing to a decline in oil exports in Algeria and Libya. Total imports reached around $830 billion, a 5 per cent increase from 2018. Asia and the Pacific is the main recipient of Arab exports, capturing around 46 per cent of total exports in 2019. China, India and Japan remained the main recipient of GCC countries' exports, while GCC countries and the United States were the main trading partners for other Arab countries, except Libya, Morocco and Tunisia which traded mostly with Europe. The main exported good for GCC countries is oil. The dependence of GCC countries on fuel revenues continues to be significant, ranging from 53 per cent in Bahrain to almost 91 per cent in Kuwait (as at 2018), posing huge challenges for government financing in 2021. Other Arab countries also heavily depend on commodity exports, like Mauritania which exports mineral ores, iron and copper. All Arab countries are high on the export diversification index, indicating a significant reliance on a small portfolio of products. Arab MICs exhibit a relatively more diversified range of exported goods, which makes them less prone to falls in demand and resource prices caused by COVID-19.



In terms of imports, countries in Asia and the Pacific and Europe are the main countries of origin for imports to the Arab region, with a share of 37 and 33 per cent, respectively. Intraregional trade remains weak in the Arab region, mainly owing to the similarity of traded products. In 2019, intraregional exports captured around 13.6 per cent of total exports, while intraregional imports captured 14 per cent of total imports, a slight increase from 2018.

COVID-19 has a tremendous impact on global trade, including trade with Arab countries in 2020. GCC countries are most affected by the fall in prices and demand for oil, losing on average 7.7 per cent of their real exports, which is still less than in other Arab countries.[3] The worst hit are Kuwait and the United Arab Emirates, losing 8.7 and 10.6 per cent of real exports, respectively, while Oman is estimated to have lost only 3.7 per cent of its real exports in 2020 compared with 2019. Recovery is projected in 2021, elevating the volume of exported goods back to pre-crisis levels. Among GCC countries, the change in imports is similar to the change in exports, but there are considerable differences between countries.

Imports in Kuwait and the United Arab Emirates are are estimated to have increased over 2020, leading to a deterioration in their trade surplus, while in Bahrain, Oman and Qatar imports are estimated to have fallen much more than exports, strengthening their trade balances. Arab MICs are affected by a fall in tourism and a decline in demand for their exports, as their main trading partners are witnessing a deep recession. This is expected to lead to a 17.1 per cent fall in real exports in Morocco, 17.3 per cent in Tunisia (which will be also affected by the fall in demand for phosphates),[4] while Algeria will be hurt by a fall in oil demand, losing 18.8 per cent of its real exports. Real imports will decrease more than exports, leading to improvements in the trade balance of most countries, except Algeria and Morocco. Recovery will be slow, as both exports and imports will increase by around 12 per cent in 2021.

Table 1.2 Real export and import growth rate in the Arab region, 2019-2021

	Exports			Imports		
	2019	2020	2021	2019	2020	2021
Bahrain	-0.7	-7.3	4.9	-2.0	-11.9	7.2
Kuwait	2.0	-8.7	10.9	2.6	4.6	-4.0
Oman	1.9	-3.7	6.9	0.7	-15.4	16.1
Qatar	1.1	-8.0	8.4	-1.3	-17.2	17.5
Saudi Arabia	1.3	-7.6	8.6	0.6	-7.5	2.3
United Arab Emirates	-0.1	-10.6	9.9	-0.2	1.4	-4.9
GCC unweighted average	**0.9**	**-7.7**	**8.3**	**0.1**	**-7.7**	**5.7**
Algeria	1.5	-18.8	14.3	-2.3	-7.6	3.2
Egypt	5.7	-11.0	13.9	4.0	-20.6	22.2
Jordan	0.9	-11.3	9.6	-0.7	-13.8	16.7
Lebanon	1.8	-7.9	8.1	2.9	-12.1	6.0
Morocco	2.0	-17.1	14.1	-0.5	-11.9	8.1
Tunisia	2.8	-17.3	13.1	1.5	-19.2	13.2
Arab MICs unweighted average	**2.4**	**-13.9**	**12.2**	**0.8**	**-14.2**	**11.6**
Iraq	2.5	-11.9	12.2	-1.1	-12.4	5.4
Libya	1.7	-21.5	18.0	0.4	-4.4	4.1
State of Palestine	3.8	-8.4	10.5	3.4	2.1	0.9
Syrian Arab Republic	0.9	-13.3	10.8	11.6	1.1	16.2
Yemen	-1.8	-13.8	9.4	6.1	-11.7	8.4
Conflict unweighted average	**1.4**	**-13.8**	**12.2**	**4.1**	**-5.1**	**7.0**
Comoros	2.2	-13.2	13.9	2.1	-5.4	5.8
Djibouti	4.3	-10.7	12.9	9.6	-9.6	22.6
Mauritania	2.0	-12.8	11.4	3.0	-3.3	2.4
Sudan	-1.2	-10.1	3.5	0.8	-7.4	3.9
Somalia	-1.5	-8.0	2.8	2.8	2.7	4.3
Arab LDC unweighted average	**1.1**	**-10.9**	**8.9**	**3.6**	**-4.6**	**7.8**
Arab unweighted average	**1.5**	**-11.6**	**10.4**	**2.2**	**-7.9**	**8.0**

Sources: DESA, based on data of the United Nations Statistics Division; and national sources.

In conflict-affected countries, already weak trade-balances are further deteriorating as real exports decreased by an estimated 13.8 per cent on average and real imports by 5.1 per cent. Iraq, the only conflict-affected country with a trade surplus, is estimated to have lost 12 per cent of its real exports owing to weak oil demand; Libya is estimated to have lost 21 per cent. At the same time, real imports decreased only slightly, and increased in the State of Palestine and the Syrian Arab Republic. In 2021, real exports are expected to rebound by 12.2 per cent on average in conflict-affected countries, while real imports are to increase by a modest 7 per cent. Similarly, the trade balance of Arab LDCs further deteriorated, with real exports losing 10.9 per cent on average and real imports falling by just 4.6 per cent in 2020. The rebound in 2021 will be slow, with an 8.9 per cent increase in exports and a 7.8 per cent rise in imports in 2021. The biggest impact of the COVID-19 pandemic is observed in the Comoros and Mauritania, with 13.2 and 12.8 per cent losses in real exports, respectively. These changes will significantly affect these countries' ability to support citizens who lost their income sources because of the COVID-19 pandemic.

D. Concluding remarks

The COVID-19 economic shock will exert incredible pressure on all sectors and dimensions of the global economy. It will depress global GDP growth, leading to a fall in demand for energy commodities and phosphate, affecting Arab oil exporters. Little tourism activity are taking place in 2020, affecting the revenues of Arab MICs where tourism is a key part of the economy, such as Egypt, Jordan, Morocco and Tunisia. COVID-19 losses are likely to contract the Lebanese economy further, triggering social unrest. Deteriorating economic situations in developed countries will affect the inflow of investments, remittances and ODA to Arab least developed and conflict-affected countries.

Except for wealthy GCC countries, Arab countries struggle to provide appropriate safety nets to protect their citizens against COVID-19 lockdown measures. Although global financing costs fell, most Arab countries will not benefit because of borrowing constraints. As Arab LDCs are more vulnerable to shocks resulting from global turmoil on resource markets and the fall in tourism, adequate support provided by international institutions will be crucial in lifting them out of the COVID-19 crisis.