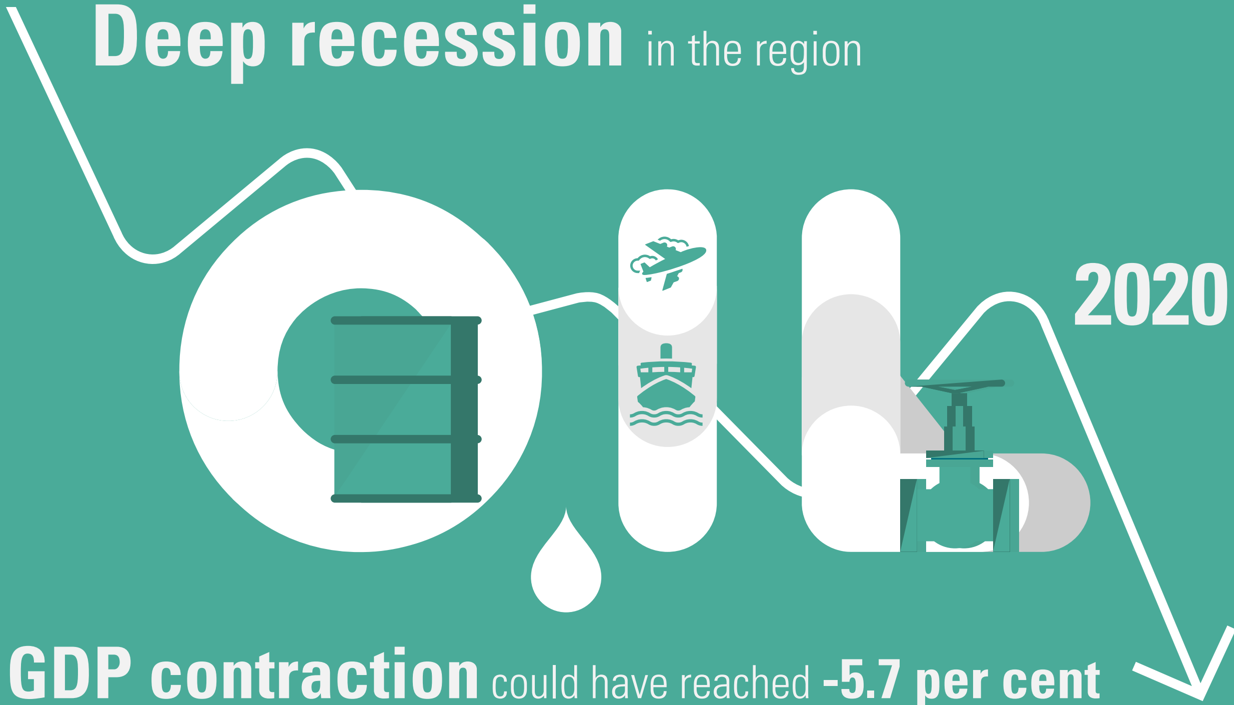
Deep recession in the region



GDP contraction could have reached **-5.7 per cent**

Length of the **recession** affected by:

- GCC countries'
- Arab MICs
- Arab LDCs
- Arab CACs

Economic recovery

would exceed

$180 billion

2 Regional Socioeconomic Trends

A. Overview of Arab subregions

The COVID-19 crisis came at a time when the region was already registering low growth performance. In 2019, the slowdown in global demand owing to trade tensions between China and the United States, coupled with the absence of a new production agreement among OPEC+, significantly affected growth in Arab countries. The GDP growth rate decreased from 2.3 per cent in 2018 to 1.9 per cent in 2019, with some disparities among Arab subregions.

In general, 2019 was a challenging year for all Arab subregions. From an economic perspective, Arab oil exporters are still dependent on oil and gas production, despite great efforts in recent years to diversify their economies. Additional economic pressures on budgets, rising external debts, and increased social expenses have worsened fiscal deficits and limited the fiscal space. Arab oil importers focused more on fiscal reforms, notably improving tax administration, rationalizing customs duties, and reducing public expenses by rationalizing social expenditures and reforming social security and pension systems.

The COVID-19 pandemic has affected Arab subregions in various ways. As a result of the decline in global demand, exports decreased drastically by almost 50 per cent for both oil-exporter and oil-importer countries. Oil exporters have been affected by a decrease in oil prices resulting from reduced global demand and increased supply. Oil importers suffered from the closure of European markets and from a reduction in remittances. All these factors combined contributed to a decline in the GDP growth rate to -3 per cent in 2020, with some disparities between Arab subregions. GDP is expected to rebound by 2.8 per cent in 2021 as a result of stimulus packages enacted by most Governments, and the resurgence in oil prices following monetary expansion. Arab countries' central banks and ministries of finance have adopted incentive packages valued at approximately $180

Key messages

- The global economic recession, the sharp decline in oil prices, the slowdown of transport and tourism activities, and the lockdown measures imposed in all the Arab countries plunged the region into a deep recession in 2020. Growth performance could have reached -3 per cent. In the pessimistic scenario, GDP contraction could have reached -5.7 per cent.
- The length of the recession depends on factors specific to each country subgroup. GCC countries' recovery will be shaped by the demand for oil and gas and their prices. Recovery in Arab MICs is contingent on the revival of tourism activities following the pandemic. Recovery in Arab CACs depends on the pandemic's impact on conflict dynamics. In Arab LDCs, recovery hinges on the willingness of donors and expats to channel ODA and remittances.
- The 2021 recovery depends to a large extent on the success of the stimulus packages enacted in the region, which exceed $180 billion. It also depends on the economic recovery of partner countries, and the success of their incentive packages.

billion to support affected groups and reduce the impact of the pandemic.[1] However, if these packages do not succeed, a pessimistic scenario may materialize where the Arab region might have lost 5.7 per cent of its GDP in 2020. Under this pessimistic scenario, recovery will be slightly faster (3.5 per cent instead of 2.8 per cent in 2021); however, this difference is far too low to compensate for the additional GDP lost.

Consumer price inflation in Arab countries declined to 5.4 per cent in 2019 from 6.7 per cent in 2018, resulting from a decrease in domestic demand in some countries, changes in international prices of oil and raw materials, and the fiscal reforms implemented by some Arab countries over the past two years. In 2020, inflation rates are estimated to have declined in most Arab countries because of low oil prices and the pandemic's effects on supply and demand. They are projected to rise in 2021 in view of the expected recovery of global and domestic demand and international oil prices.

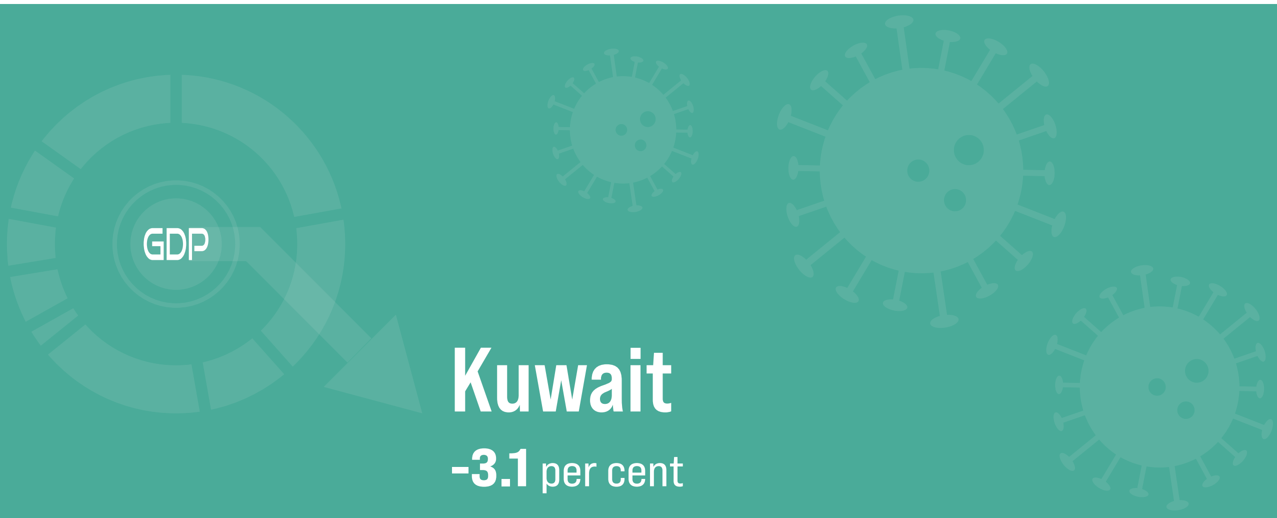
B. Gulf Cooperation Council countries

The COVID-19 pandemic is strongly affecting GCC countries. The sharp decline in global oil prices has worsened economic conditions in this subregion. GDP is estimated to have contracted by 3.2 per cent in 2020, but a gradual recovery is expected in 2021 considering anticipated improvements in global demand levels and an increase in international oil prices. If the crisis persists, the GDP loss could double and reach -7.1 per cent.

This COVID-19 crisis came at a time when the region was already facing a downward trend. GDP growth decreased from 1.9 per cent in 2018 to 0.6 per cent in 2019, as a result of the slowdown in global demand for oil and gas in the second half of 2019. A disagreement between the Russian Federation and Saudi Arabia in 2020 led to a collapse in oil prices, and created a large stock in the oil market. The situation worsened owing to the escalation of disputes between these two oil-producing giants, with oil prices plunging 80 per cent.

GDP in Saudi Arabia was expected to grow by 1.3 per cent in 2020 following a gradual recovery in the oil sector, including a rise in crude oil production following increased production capacity at the Jazan refinery and advanced discussions with OPEC+. However, global developments related to the pandemic and the fall in oil prices plunged growth estimations down to -3.3 per cent in 2020 (-6.8 per cent in the pessimistic scenario). Moreover, global lockdowns drastically decreased global demand, notably for hydrocarbon products. Oil represents more than 40 per cent of Saudi GDP, almost 70 per cent of government revenues, and over 83 per cent of total exports. A 1.8 per cent growth rebound (3.5 per cent in the pessimistic scenario) is expected in 2021, driven by a projected increase in global oil demand, mainly from China, and by stimulus packages adopted by the Government through the Saudi Arabian Monetary Agency and the Ministry of Finance worth 120 billion Saudi riyals to mitigate the impact of the pandemic on affected sectors and to support spending levels.

In Kuwait, GDP growth dropped to an estimated -3.1 per cent in 2020 owing to declining global oil demand and decreasing oil prices in the first half of the year (-7.0 per cent in the pessimistic scenario). This situation will increase pressure on the Kuwaiti economy and the public budget. In



addition, the country has taken drastic measures against the pandemic, which have slowed economic activity in general, including flight cancellations affecting the tourism and travel sectors, shopping centre closures and a ban on gatherings, which have had a direct impact on commercial markets, health institutions, restaurants and the retail sector. The rebound in 2021 is expected to be relatively modest at 2.7 per cent in the baseline scenario, and 2.9 per cent in the pessimistic scenario.

In Qatar and Oman, GDP growth is estimated to have further declined to -2.8 and -4.2 per cent, respectively, by 2020 (-6.3 and -9.5 per cent, respectively, in the pessimistic scenario), as a result of weak energy demand, especially for natural gas. In Qatar, growth will recover gradually in 2021 to achieve a 2.4 per cent growth rate (2.2 per cent in the pessimistic scenario), driven by the resumption of oil and non-oil sectors. Moreover, increased spending on infrastructure projects under the Qatar National Vision 2030 will support growth, as the vision includes a strategy to reinforce economic diversification to achieve sustainable long-term growth. New economic and fiscal reforms will attract foreign direct investment (FDI), including a law allowing foreigners full ownership of projects, and the establishment of the Investment Promotion Agency to coordinate investment promotion and marketing activities with key stakeholders.

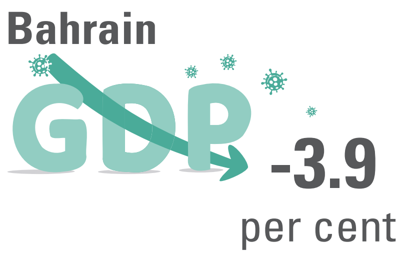
Prior to the pandemic, the GDP growth rate in Oman was expected to increase from 0.9 per cent in 2019 to 1.7 per cent in 2020, boosted by increased domestic oil production to meet increasing demand by local refineries, such as the Sohar Refinery Expansion Project. Natural gas production was also expected to increase, with the Khazan field reaching full capacity. However, as a result of the pandemic, GDP growth is estimated to have decreased to -4.2 per cent in 2020 (9.5 per cent in the pessimistic scenario), with the oil sector suffering the most because of decreases in global oil demand. The Central Bank of Oman announced a stimulus package to pump liquidity and support the private sector at a value of around $21 billion, and to reduce interest rates in view of this facilitative monetary policy. These quick actions and the gradual increase of global oil demand will help the Omani economy recover and achieve a growth rate of 3.8 per cent in 2021 (3.5 per cent in the pessimistic scenario).

QATAR and **OMAN**

-2.8 and **-4.2**

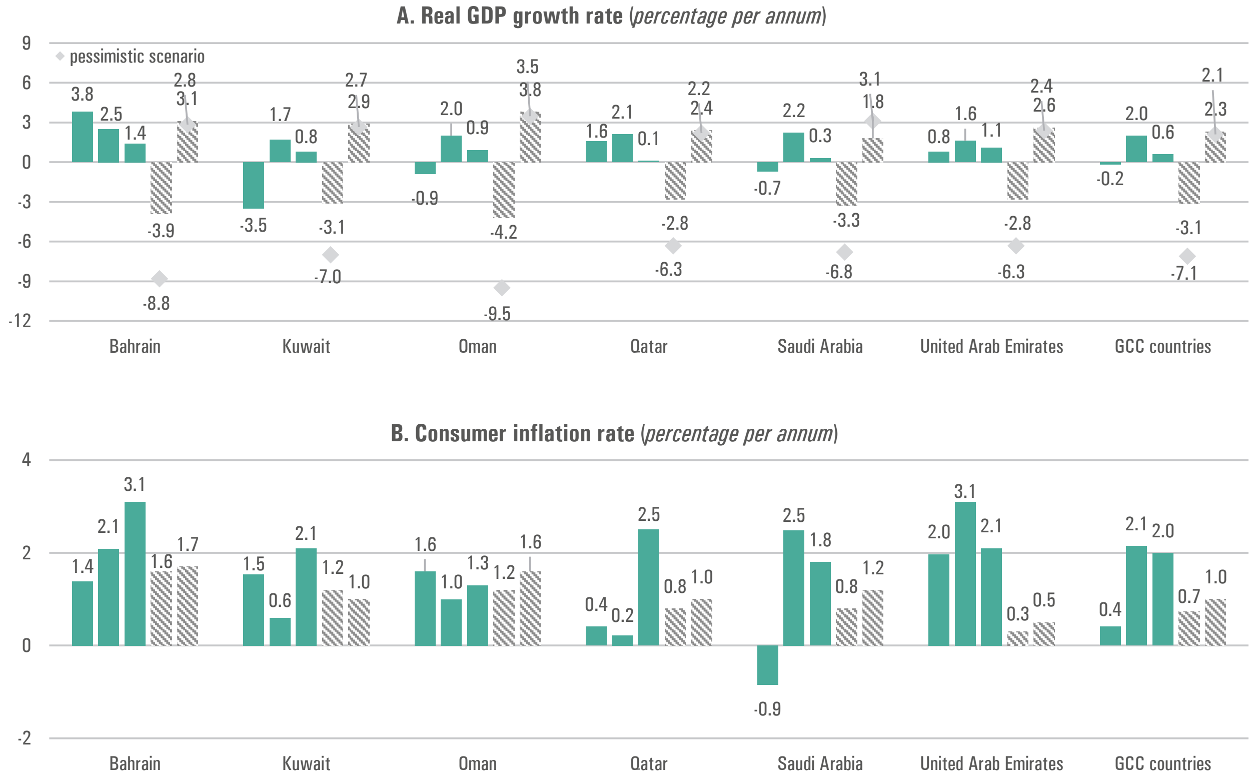
per cent

In Bahrain, growth is estimated to have decreased to -3.9 per cent in 2020 (-8.8 per cent in the pessimistic scenario), influenced by decreased global oil demand. Growth will increase to 3.1 per cent in 2021 (2.8 per cent in the pessimistic scenario). This recovery is expected to benefit from improved global demand in general and for aluminium in particular, and an increase in oil production capacity, notably owing to the expansion of the Sitra refinery owned by the Bahrain Petroleum Company.



As for inflation dynamics in GCC countries in 2019, consumer price inflation declined slightly to 2 per cent in 2019 because of the low impact of fiscal reforms in 2018, notably value added tax (VAT)

Figure 2.1 **GDP and inflation in GCC countries, 2017-2021**



Sources: ESCWA staff estimations/forecasts based on national statistical sources; DESA, *World Economic Situation and Prospects as of mid-2020, World Economic Situation and Prospects 2020*; and ESCWA, Statistics Information Portal.

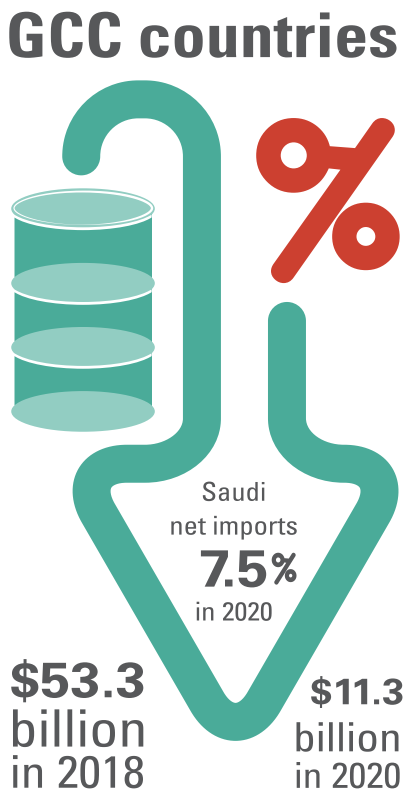
reforms in almost all GCC countries. Inflation in Saudi Arabia declined to 1.8 per cent in 2019 from 2.5 per cent in 2018 as result of a decrease in residential rents, which represent about 22 per cent of the overall general price index, and weak subsidy reforms initiated in 2018. In contrast, inflation rates increased in 2019 to 2.5 per cent in Qatar, 2.1 per cent in Kuwait, and 3.1 per cent in Bahrain owing to higher prices of food, clothing, health and education.

In GCC countries, the inflation rate is estimated to have decreased to 0.7 per cent in 2020, reflecting both the pandemic impact and the decrease in global oil prices. However, both trends are expected to be reversed in 2021, and the inflation rate is expected to rise to 1 per cent. The downward trend of oil prices since mid-2019 has affected the fiscal position of all GCC countries.

The decline in oil prices in 2019 affected total exports from GCC countries, which decreased by 8 per cent. This subregion is still a net exporter, with total exports of $651 billion and total imports of $514 billion in 2019. In terms of the geographical concentration of trade in 2019, Asia and the Pacific remains the main trading partner of GCC countries, capturing around 52 per cent of exports and around 44 per cent of imports. As for intraregional trade, exports increased by less than one percentage point to capture 14 per cent of total exports, while imports increased by more than one percentage point, reaching 15 per cent of total imports in 2019.

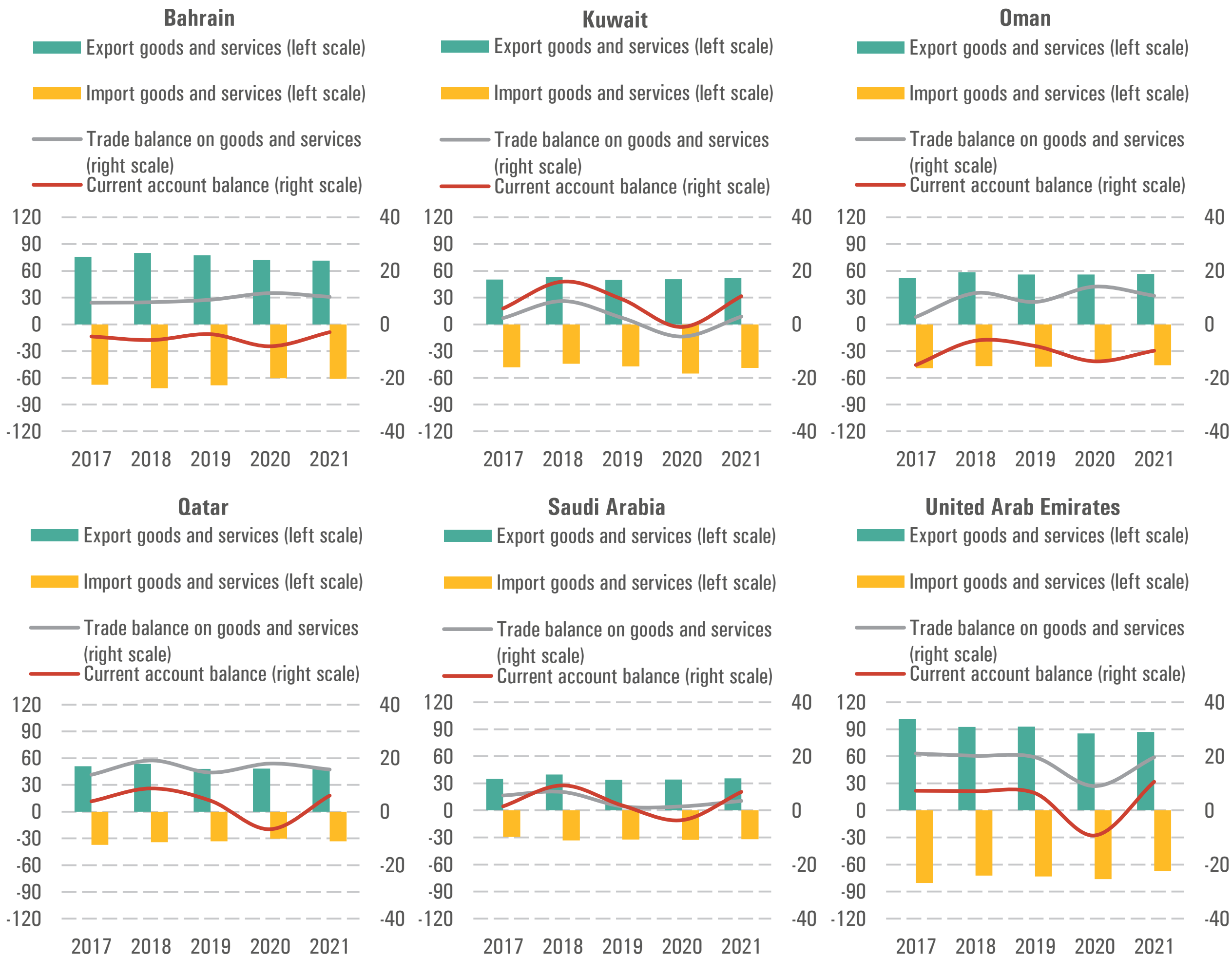
COVID-19 will have a significant impact on GCC countries. Their overall increase in imports is equivalent to the drop in exports, with considerable differences between countries. Saudi net imports and net exports of goods and services decreased by an estimated 7.5 per cent in 2020 owing to the pandemic's impact on global trade markets. Its net trade balance is estimated to have decreased from $53.3 billion in 2018 to only $11.3 billion in 2020. This sizable decrease had a direct impact on its current account balance, with a deficit of 3.6 per cent of GDP estimated in 2020. Kuwait and the United Arab Emirates were the worst hit, with exports decreasing by 8.7 and 10.7 per cent, respectively, in 2020. However, the global recovery in 2021 will increase the volume of exported goods back to pre-crisis levels. Imports to Kuwait and the United Arab Emirates are estimated to have increased in 2020, leading to a deterioration in their trade surplus. In contrast, imports to Bahrain, Oman and Qatar are estimated to have decreased more than the decline in exports, thus strengthening their trade balances.

The fiscal performance of GCC countries reflects high dependence on oil revenues, which significantly hinges upon oil price dynamics. Almost



all GCC countries have experienced a significant decrease in fiscal revenues. Two major factors generated this situation, namely tanking oil prices, and delays in implementing fiscal reforms, notably in Bahrain and Oman. In Saudi Arabia, the fiscal deficit declined to 4.2 per cent of GDP in 2019, down from 4.6 per cent in 2018, thanks to relatively stable oil revenues despite a tumultuous oil market by mid-2019, and the rapid implementing of a 5 per cent VAT and energy subsidy reforms, which have contributed to stabilizing its fiscal balance.

Figure 2.2 **Trade and current account balances in GCC countries, 2017-2021 (percentage of GDP)**



Sources: ESCWA staff estimations/forecasts based on national statistical sources; and *World Economic Situation and Prospects 2020.*

In Oman, Bahrain and Kuwait, the fiscal balance recorded a deficit of 9.2, 4.9 and 2.5 per cent of GDP, respectively, for 2019, reflecting the struggle of these economies since 2017. They have delayed implementing fiscal reforms initiated in other GCC countries, and have increased their social expenditure. In contrast, Qatar and the United Arab Emirates recorded a fiscal surplus of 5.1 and 1.8 per cent of GDP, respectively, as a result of increased natural gas revenues, and a significant rise in fiscal revenues from non-oil sectors such as tourism and services.

Figure 2.3 **Fiscal positions in GCC countries, 2017-2021 (percentage of GDP)**

Sources: ESCWA staff estimations/forecasts based on national statistical sources; and *World Economic Situation and Prospects 2020.*

The decline in oil prices had a significant effect on GCC countries' fiscal position in 2020. In Saudi Arabia, the fiscal deficit is estimated to have reached 16.3 per cent of GDP, while in 2021 the situation should improve to 4.7 per cent of GDP as a result of possible increases in oil demand and rising non-oil revenues, including VAT revenues and improvements in energy prices.

The fiscal position in Bahrain and Oman is estimated to have declined significantly to 15.7 and 17.7 per cent of GDP, respectively, in 2020 before a slight improvement forecasted in 2021. These countries have suffered from severe fiscal deficits in the last two years. The United Arab Emirates observed a slight fiscal deficit of 6.1 per cent of GDP in 2020 and will observe a deficit of 2.5 per cent of GDP in 2021, continuing the same trend of the last two years. Qatar could be the exception in this subregion, with a fiscal surplus of 5.6 per cent of GDP in 2020 and 2021. The favourable fiscal position of Qatar is mainly boosted by an abundant natural gas reserve. In Kuwait, the deficit is likely to have reached 6.3 per cent of GDP in 2020, dropping to 4.2 per cent in 2021.

C. Arab middle-income countries

Prior to the pandemic, MIC economies were growing by 3.4 per cent on average in 2019. This trend was expected to continue in 2020 and 2021, with growth rates of 3.5 and 3.6 per cent, respectively. COVID-19 constitutes a double negative shock for the region. Firstly, the interruption of international travel for several months, and the total or partial lockdown measures, have considerably affected the tourism sector – one of the most important sectors in the region. Secondly, the recession in European countries, MICs' main trading partners, has affected the export performance of manufacturing sectors. As a result, MIC economies are estimated to have contracted by 3.4 per cent in 2020 in the baseline scenario, and by 4.5 per cent in the pessimistic scenario. Recovery will be subject to developments at the global level, and the success of fiscal and monetary stimulus by the region's trading partners. In 2021, the economies of MICS are expected to record a 4.1 per cent growth rate on average (5 per cent in the pessimistic scenario).

In terms of individual economies, the Egyptian economy is estimated to have contracted by at least 1.1 per cent in 2020 before recovering by a projected 6.1 per cent in 2021 (a contraction of 2.1 per cent in 2020 followed by 7.5 per cent growth in 2021 in the pessimistic scenario). This comes after a good performance in 2019, when the economy grew by 5.9 per cent driven mainly by tourism, gas extractives, wholesale and retail trade, real estate, and construction. Prior to the pandemic, the Egyptian economy was expected to grow by 5.7 per cent in 2020, and 5 per cent in 2021. The recovery in 2021 will be fuelled by the revival of the tourism sector following the pandemic.

In Morocco, the economy is estimated to have witnessed a 2.1 per cent contraction in 2020 before recovering by a projected 2.8 per cent in 2021 (a contraction of 3.9 per cent in 2020 followed by 3.4 per cent growth in 2021 in the pessimistic scenario). In 2019, the economy was growing at a rate of 2.7 per cent because of the good performance of the agriculture sector. The outlook of the Moroccan economy prior to the pandemic was positive, and the economy was expected to grow by 3 and 3.8 per cent in 2020 and 2021, respectively. Revised forecasts expected a contraction in 2020 before a recovery in 2021, driven by the agriculture and tourism sectors and increased external demand for local products.

Jordan has witnessed a 3.6 per cent contraction in 2020 and will observe a 3.3 per cent recovery in 2021 (a contraction of 6.7 per cent in 2020 followed by 4.1 per cent growth in 2021 in the pessimistic scenario). Jordan is still facing significant regional challenges emanating from the crisis in neighbouring Iraq and the Syrian Arab Republic, the significant influx of refugees, the disruption of trade routes, and increases in health and education costs. In 2019, Jordan had a modest growth of 0.7 per cent and was expected to record a 2.2 per cent growth rate in 2020 and 2 per cent in 2021.

Similarly, Tunisia is estimated to have witnessed a severe contraction in 2020 of 3.8 per cent (a contraction of 7.1 per cent in the pessimistic scenario). The country is affected by the deep recession in Europe, which is its main trading partner and the main source of tourism in Tunisia. The Tunisian economy is expected to recover by 3.1 per cent in 2021, subject to the recovery of its partner countries and the resumption of tourism activities (3.8 per cent in the pessimistic scenario). In 2019, the country started to reap the results of its pension funds reform implemented in the previous years, and grew at a rate of 1.4 per cent. This trend was expected to continue growing at a rate of 2 and 3 per cent in 2020 and 2021.

Egypt

1.1 per cent contraction in 2020
6.1 per cent recovery in 2021

Morocco

2.1 per cent contraction in 2020
2.8 per cent recovery in 2021

Jordan

3.6 per cent contraction in 2020
3.3 per cent recovery in 2021

Tunisia

3.8 per cent contraction in 2020
3.1 per cent recovery in 2021

Lebanon

10.2 per cent contraction in 2020
1.5 per cent recovery in 2021

Lebanon has witnessed severe difficulties in 2020. Socioeconomic challenges surfaced in 2019 and the economy contracted by 1.1 per cent. These challenges have intensified considerably in 2020, with the economy contracting by 10.2 per cent before recording a modest recovery of a projected 1.5 per cent in 2021 (a contraction of 19.1 per cent in 2020 followed by modest growth of 1.8 per cent in 2021 in the pessimistic scenario). This contraction in growth was caused by a series of adverse events emanating particularly from weak business confidence and tight financial conditions, which led to widespread social instability starting in October 2019. This situation was further aggravated in 2020 by twin deficits, high public debt, a default on the repayment of Eurobonds in March, April and June 2020, a large depreciation in the local currency (between October 2019 and June 2020, the Lebanese pound depreciated by more than 200 per cent relative to the dollar), and a slowdown in economic activity owing to the COVID-19 lockdown. The modest recovery expected in 2021 is conditioned on successful structural reforms, restoring the trust of society and foreign stakeholders in Lebanese institutions, the success of measures to halt the deteriorating local currency and the outcomes of negotiations with IMF to obtain financial support. Even before the pandemic, the economy was expected to grow at a rate of only 0.4 per cent in 2020 and 1.4 per cent in 2021. However, the spread of the virus and the default on debt payments has aggravated the situation.

Algeria

2.1 per cent contraction in 2020
2.1 per cent recovery in 2021

In Algeria, following the outbreak of COVID-19 and the historic fall in oil prices in April 2020, the economy is estimated to have contracted by 2.1 per cent in 2020 and is projected to recover by 2.1 per cent in 2021 (a contraction of 3.9 per cent in 2020 followed by 2.6 per cent growth in 2021 in the pessimistic scenario). These developments follow a tumultuous 2019, when large demonstrations led to the departure of President Bouteflika. In 2019, the Algerian economy grew by 1.2 per cent and was expected to grow by 2.3 per cent in 2020. However, adverse effects in the hydrocarbon market and modest growth in the nonhydrocarbon sector resulted in the economy contracting.

Inflation rates in MICs are expected to decrease or stabilize in 2021 in all countries, except Lebanon. On average, the inflation rate is expected to decline to 5.8 and 5.5 per cent in 2021, down from 6.8 and 5.88 per cent in 2019 and 2020, respectively.

In Lebanon, uncertainties and vast socioeconomic challenges, particularly the substantial depreciation of the Lebanese pound, is estimated to have increased inflation to 16.4 per cent in 2020 up from 1.4 per cent in 2019, then a decrease to 5.2 per cent is expected in 2021. The challenging situation in the country was further complicated by the Beirut Port explosion on 4 August 2020 (box 2.1).

Box 2.1 **An assessment of the implications of the overlapping crises in Lebanon**

Before 4 August 2020, Lebanon was already witnessing one of the most severe economic crises in its modern history. It began with a social uprising on 17 October 2019, followed by two months of lockdown in response to the COVID-19 pandemic, and lastly the tragic explosion at the Beirut Port on August 2020 that deeply affected the country's already dire socioeconomic conditions.

According to the Rapid Damage Assessment conducted by the United Nations and the World Bank, the blast is estimated to have caused the following in the short run:

- Between 0.4 and 0.6 percentage points decline in the growth rate of real GDP in 2020 and 2021 as a result of the destruction of physical capital stock;
- An additional loss of 0.4 and 1.3 percentage points in GDP growth rate in 2020 and 2021 as a result of increased trade costs caused by the destruction of Beirut Port facilities.

These impacts further deepen the double-digit contractions in real GDP growth stemming from the pre-existing economic and financial crisis, and the repercussions of COVID-19. The explosion also had major social implications. General and extreme poverty rates hit 45 and 22 per cent, respectively, in 2020. The headcount poverty rate is estimated to have jumped from 28 per cent in 2019 to 55 per cent in May 2020. The corresponding increase in extreme poverty is from 8 to 23 per cent. This brings the total number of poor among the Lebanese population to 1.1 million and 2.7 million for the lower and the upper poverty lines, respectively. For the upper poverty line, this is an increase of 1.3 million poor from the reference growth scenario for 2020 (pre-COVID-19 and pre-explosion). The equivalent rise in the number of extreme poor is 750,000.

In addition, Lebanon has one of the most unequal wealth distributions in the region and the world, ranking twentieth globally with a wealth Gini coefficient of 81.9 per cent, and one of the highest concentrations of billionaires per capita. The top 10 per cent of adults owned 70.6 per cent, or $151.4 billion, of all estimated personal wealth ($232.2 billion) in the country in 2019, but these monetary figures are expected to have shrunk significantly in 2020.

This crisis could be the starting point to implement much-needed policy and social reforms, including the following:

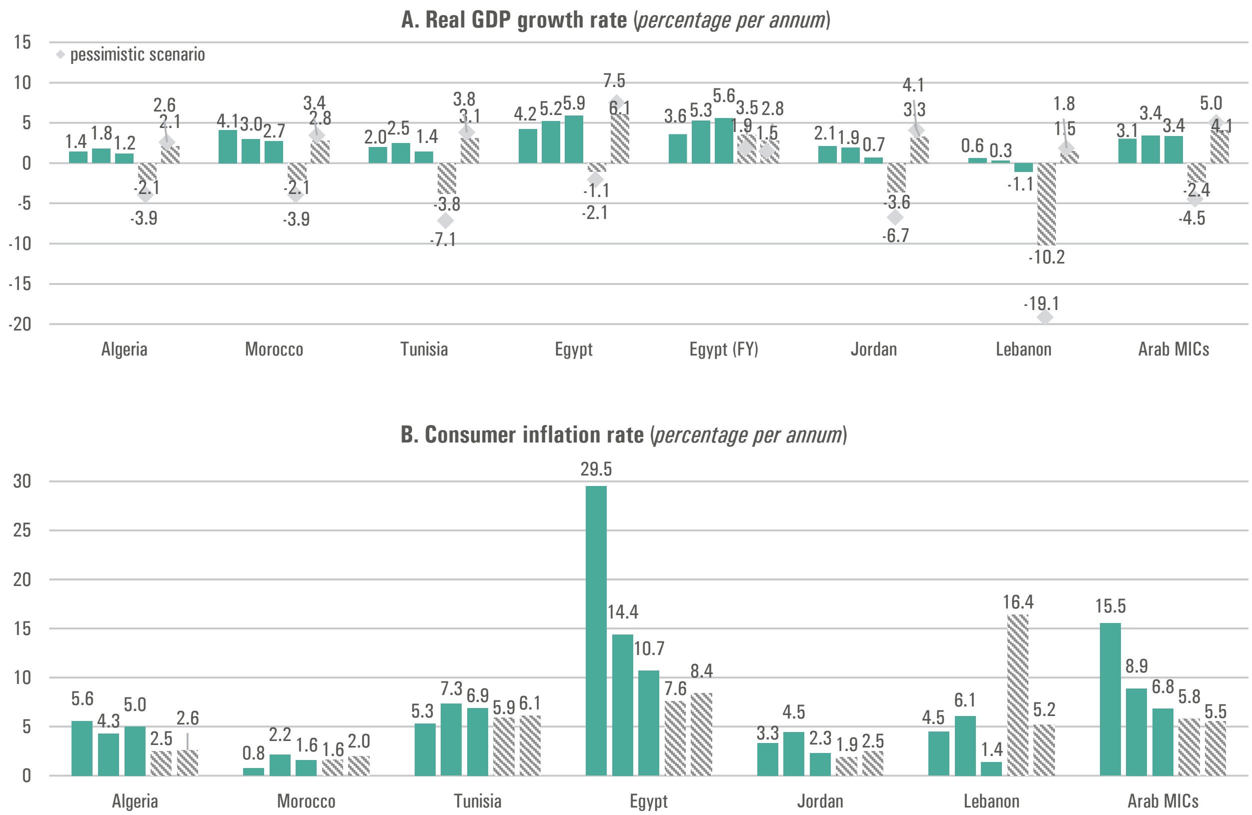
1. Establishing a national solidarity fund to tackle the country's humanitarian crisis and close the poverty gap. Lebanon should mobilize its own substantial resources, with a fair and progressive system of shared responsibility, supported by political will and strong institutional capacity to ensure societal solidarity. The solidarity fund should target the needs of vulnerable groups, including the most vulnerable affected by the explosion such as the poor, the displaced and older persons.
2. Bolstering food and health security and social protection, which urgently need donor support. Foreign assistance can play a vital role in supporting immediate responses, conditioned on ensuring it is directed towards providing adequate access to food, medication, unemployment benefits and cash.
3. Addressing this crisis requires the country to transform quickly and adopt various coping mechanisms. With shared responsibility and societal solidarity in place, especially between the wealthiest top decile and the poor, the bulk of the poverty impact can be absorbed. In Lebanon, and in other Arab MICs, the Economic and Social Commission for Western Asia (ESCWA) advocates for a solidarity fund to mitigate the expected rise in poverty as a result of the COVID-19 pandemic, and other natural or human-made disasters such as the Beirut Port explosion.
4. Enacting necessary economic governance reforms, limiting rent-seeking activities, and enhancing transparency and accountability. More transparency on income and wealth would allow the ministries of finance, social affairs and related institutions to improve poverty-targeting practices.

Source: World Bank, European Union in Lebanon, and United Nations, 2020; and E/ESCWA/CL3.SEP/2020/TP.8.

In Jordan and Morocco, inflation rates are controlled and are estimated to have declined in Jordan from 2.3 to 1.9 per cent between 2019 and 2020, and stabilized in Morocco at around 1.6 per cent. In Algeria, Egypt and Tunisia, inflation rates are estimated to have declined significantly following a number of reforms and measures adopted by Governments to control price increases; in Algeria, inflation is estimated to have declined from 5 to 2.5 per cent between 2019 and 2020, in Egypt from 10.7 to 7.6 per cent, and in Tunisia from 6.9 to 5.9 per cent.

Arab MICs are net importers, except Algeria. The region's total merchandise exports reached $130 billion in 2019 compared with total imports of $223 billion, and net imports of $93 billion. The region witnessed

Figure 2.4 **GDP and inflation in Arab MICs, 2017-2021**

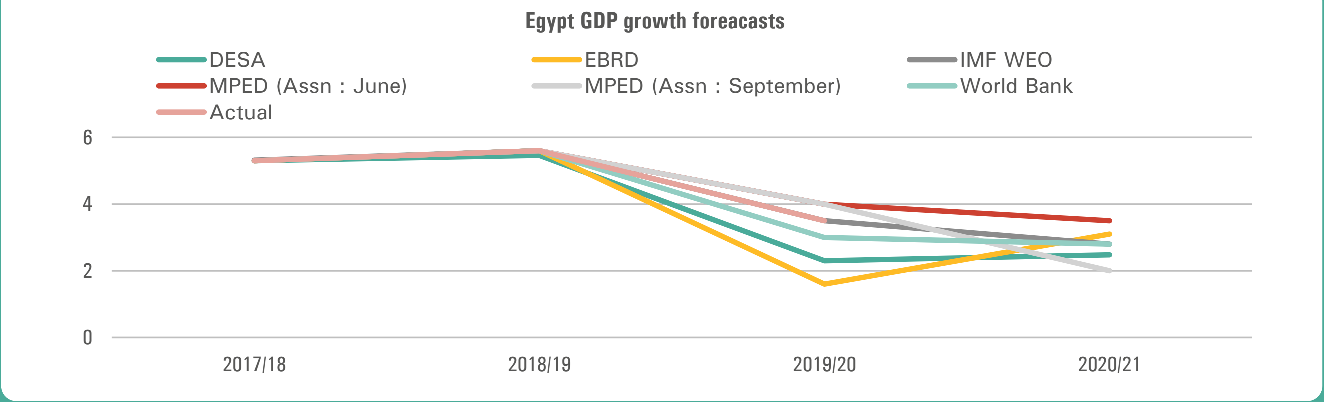


Sources: ESCWA staff estimations/forecasts based on national statistical sources; *DESA, World Economic Situation and Prospects as of mid-2020, World Economic Situation and Prospects 2020;* and ESCWA, Statistics Information Portal.

Note: FY: fiscal year.

Box 2.2 **GDP growth in Egypt: fiscal versus calendar year**

For comparability, the growth performance of Egypt is calculated in figure 2.4A within the calendar year to allow aggregation at the regional and subregional level. Meanwhile, when the estimation is realized within the fiscal year officially used in Egypt (July to June), growth is estimated to be 3.5 per cent for fiscal year 2019/2020 and 2.8 per cent for fiscal year 2020/2021. This performance is confirmed by all international organisations and makes the country one of the best performers worldwide.



This success is largely the consequence of stabilization policies enacted between 2016 and 2019. The devaluation of the Egyptian pound by 50 per cent caused a decrease in imbalances, thus attracting FDI, remittances and international assistance. Moreover, increased interest rates contributed to the inflow of capital, which helped boost GDP growth. Rapid inflation led to a fall in real wages, improving the economy's competitiveness. Imports were cut and tourism boomed, improving the current account balance.

These advancements continued during the COVID-19 pandemic. Remittances rose by 11 per cent in June and by another 11 per cent in July 2020. FDI inflows and Suez Canal revenues remained resilient (2019/2020 revenues dropped to $5.72 billion from $5.75 billion the previous fiscal year, despite growth in traffic). Tourism was the only sector severely affected with revenues expected to drop by 73 per cent, which translates into an expected 14.3 per cent decrease in employment.

Source: Based on PowerPoint presentation by Arun Jacob, "Economic Briefing COVID-19 and the State of the Egyptian Economy", 14 October 2020.

an improvement in its net export position, driven mainly by Algeria whose trade consolidated at $10 billion in net exports following several years of trade deficits. The region recorded an overall improvement in its trade balance in 2019, but is still showing a significant deficit and requires substantial amounts of foreign reserves to finance its imports, which it will meet by resorting to borrowing thus placing additional pressure on its public finances.

European countries remain the main trading partners of Arab MICs, with total exports of $75 billion and total imports of $105 billion. Algeria, Morocco and Tunisia trade mainly with European countries, particularly France, Germany, Italy and Spain. France alone received between 10 and 30 per cent of exports from these countries in 2019, which import mainly from China. Egypt, Jordan and Lebanon export mainly to the United States and other Arab countries, particularly GCC and neighbouring countries. Saudi Arabia, for example, attracted 11 per cent of Jordanian exports and around 6 per cent of exports from Lebanon and Egypt in 2019. These countries import mainly from China, the United States, Europe and other Arab countries.

Intraregional trade captured a significant share of Arab MICs' trade. The region exports around 16 per cent and imports around 13 per cent to and from neighbouring countries. Intraregional trade includes petroleum, and agricultural and food products. Oil and gas products capture the largest value share.

The unprecedented decline in oil prices in 2020 is expected to have a positive impact on the trade balance of MICs, as their import bill will significantly decrease. Imports will fall more than exports, leading to improvements in the trade balance and current account of most countries. Current account deficit is estimated to have decreased to $38 billion in 2020, and trade deficit to $58 billion. In 2019, most MICs saw a deterioration of their current account balance, with the deficit increasing from $41 billion in 2018 to $50 billion in 2019. This deterioration was mainly caused by a widening trade balance deficit from $59 billion in 2018 to $63 billion in 2019.

At the country level, Egypt managed to maintain a low current account deficit in 2019 at around 2.5 per cent of GDP thanks to its reduced trade deficit (around 7 per cent of GDP). Furthermore, in 2019, FDI inflow increased by 11 per cent to $9 billion, making Egypt the largest recipient in the region in 2019. Tourism generated around 16 per cent of the country's income. The external sector's performance improved further in 2020, and the current account is estimated to have recorded a positive balance of $8.6 billion (around 2.6 per cent of GDP) driven by an improvement in the trade balance, notably owing to a contraction of the economy, reduction in imports, and a positive FDI outlook, mainly in the oil and gas, telecommunications, consumer goods and real estate sectors.

Jordan benefited from positive economic growth in neighbouring Iraq and the Syrian Arab Republic, and the resumption of many sectors, which led to an improvement in its current account in 2019. This improvement has extended to 2020, recording a $1 billion current account surplus, driven mainly by a decline in the trade deficit, which is estimated to have dropped from 32 per cent of GDP in 2019 to 28 per cent in 2020.

Egypt

low current account deficit in 2019 at around **2.5 per cent**

Jordan

trade deficit dropping from **32 per cent** in 2019 to **28 per cent** in 2020

The situation in Lebanon is more complex, with significant twin deficits. In 2019, the country witnessed a slowdown in remittances, particularly in the last quarter of the year when banks started imposing capital controls on cash withdrawals and transfers, coupled with a considerable drop in FDI and high debt levels (around 160 per cent of GDP in 2019). Lebanon suffered from a large current account deficit in 2019, around 25 per cent of GDP. However, after the COVID-19 outbreak and the anticipated recession, the country witnessed a significant decline in its trade deficit (from $15 billion in 2019 to $12 billion in 2020) and an improvement in its current account position (from $15 billion in 2019 to $10 billion in 2020), which is estimated to have improved to 18 per cent of GDP in 2020.

In 2019, Algeria witnessed a deterioration in its current account deficit from $17 billion in 2018 to $24 billion in 2019, and $32 billion in 2020. This deterioration is mainly driven by a worsening trade balance. The trade deficit increased from $15 billion in 2018 to $23 billion in 2019, and $25 billion in 2020 as a result of the sharp decline in oil prices and in export revenues. Merchandise exports decreased from $41 billion in 2019 to $33 billion in 2020.

In Morocco, the current account deficit decreased from 4.1 per cent in 2018 to 3.7 per cent in 2019, and 1.7 per cent in 2020. These low current account levels are caused by a FDI inflow and significant tourism revenues.

Similarly, in Tunisia, the current account deficit declined between 2018 and 2019 from 10.7 to 9.2 per cent, driven mainly by a decrease in the trade deficit. This situation improved further in 2020, as the economic contraction caused by COVID-19 had dampened demand and would lead to further improvements in the trade deficit. The current account is estimated to have declined to 5.3 per cent of GDP.

The fiscal outlook for 2020 in Arab MICs clearly indicates a deterioration caused by the economic implications of COVID-19 and its repercussions in terms of declining government revenues and increased spending through stimulus packages. The pandemic slowed economic activity as all countries imposed total or partial lockdowns, which led to a contraction in economic growth and a decline in government revenues. Moreover, Governments of MICs implemented fiscal stimulus packages to mitigate the impact of the virus on their economies. However, with a limited fiscal space at their disposal to generously support their economies, these packages will pose an additional pressure on public finances by increasing government spending and leading to a tighter fiscal position. Policy measures adopted by MICs are different from those pursued in GCC countries.

Lebanon

current account deficit improved from **25 per cent** in 2019 to **18 per cent** in 2020

Algeria

deterioration in current account deficit from **$17 billion** in 2018 to **$24 billion** in 2019, and **$32 billion** in 2020

Morocco

current account deficit decreased from **4.1 per cent** in 2018 to **3.7 per cent** in 2019, and **1.7 per cent** in 2020

Tunisia

improvement in current account deficit from **10.7 per cent** in 2018 to **9.2 per cent** in 2019, and **5.3 per cent** in 2020

Figure 2.5 **Trade and current account balances of Arab MICs, 2017-2020 (percentage of GDP)**

Sources: ESCWA staff estimations/forecasts based on national statistical sources; *DESA, World Economic Situation and Prospects as of mid-2020, World Economic Situation and Prospects 2020;* and ESCWA, Statistics Information Portal.

Most MICs partly allowed businesses to defer tax payments, with varying degrees depending on the country, while others provided cash transfers or food distribution to the poor and unprivileged. Monetary policy in Arab MICs to a large extent followed the rest of the world, decreasing cash reserve requirements and cutting interest rates. The Egyptian Central Bank launched a share-purchase programme to buy stock market shares worth 20 billion Egyptian pounds to support the stock exchange, while banks in Jordan, Lebanon and Tunisia provided additional interest-free loans to affected businesses. The fiscal position is expected to improve in 2021, conditioned on the success of these measures and on resuming normal economic activity.[2]

In Algeria, the fiscal deficit increased from 5.5 per cent of GDP in 2018 to 9.3 per cent in 2019, driven partly by an increase in expenditure and a decrease in revenues, particularly oil revenues. This situation has worsened in 2020, with the fiscal deficit reaching 18 per cent of GDP in 2020 as a result of the unprecedented decline in international oil prices in the first half of the year. Revenues were estimated to have dropped from $6.5 billion in 2019 to $4.4 billion in 2020 (figure 2.6). The Algerian Government announced a plan to cut expenditures by 30 per cent in response to the fall in revenues caused by the oil price slump and to increase spending on its health sector, including spending on purchasing medical equipment. The situation is expected to improve in 2021 and the deficit will decrease to 8 per cent of GDP as signs of recovery in the global economy are expected to materialize and demand for oil is expected to resume.[3]

In Lebanon, the fiscal deficit decreased slightly between 2018 and 2019 from 9.6 per cent of GDP to 9.2 per cent. This deficit has widened in 2020, reaching 12 per cent of GDP as the country has been struggling with numerous challenges. Debt sustainability continued to be a significant challenge, especially after the Government defaulted on repayment of its issued Eurobonds over the period April-June 2020, with debt levels reaching around 159 per cent of GDP in 2019. Measures adopted by the Lebanese Government to mitigate the impact of COVID-19 included financial and in-kind support for those hit by the pandemic, in coordination with local authorities. This situation will improve slightly in 2021, with the fiscal deficit expected to decrease to 10 per cent conditioned on successful negotiations with IMF.

Similarly, Jordan is facing several socioeconomic challenges aggravated by the large number of refugees from neighbouring Iraq and the Syrian Arab Republic. The fiscal deficit, which decreased slightly between 2018 and 2019, is estimated to have increased from 2.1 per cent of GDP in 2019 to 7 per cent in 2020, and is expected to drop to 6 per cent in 2021.

In Egypt, the Government managed to increase its revenues from $989 billion in 2018 to $1,134 billion in 2019. As a result, the fiscal deficit declined from 8.3 per cent in 2018 to 7.1 per cent in 2019. The Government also managed to decrease debt levels from 95 per cent of GDP to 89 per cent in 2019. With the outbreak of COVID-19, the Government

Algeria

fiscal deficit estimated at
18 per cent in 2020

Lebanon

fiscal deficit estimated at
12 per cent in 2020

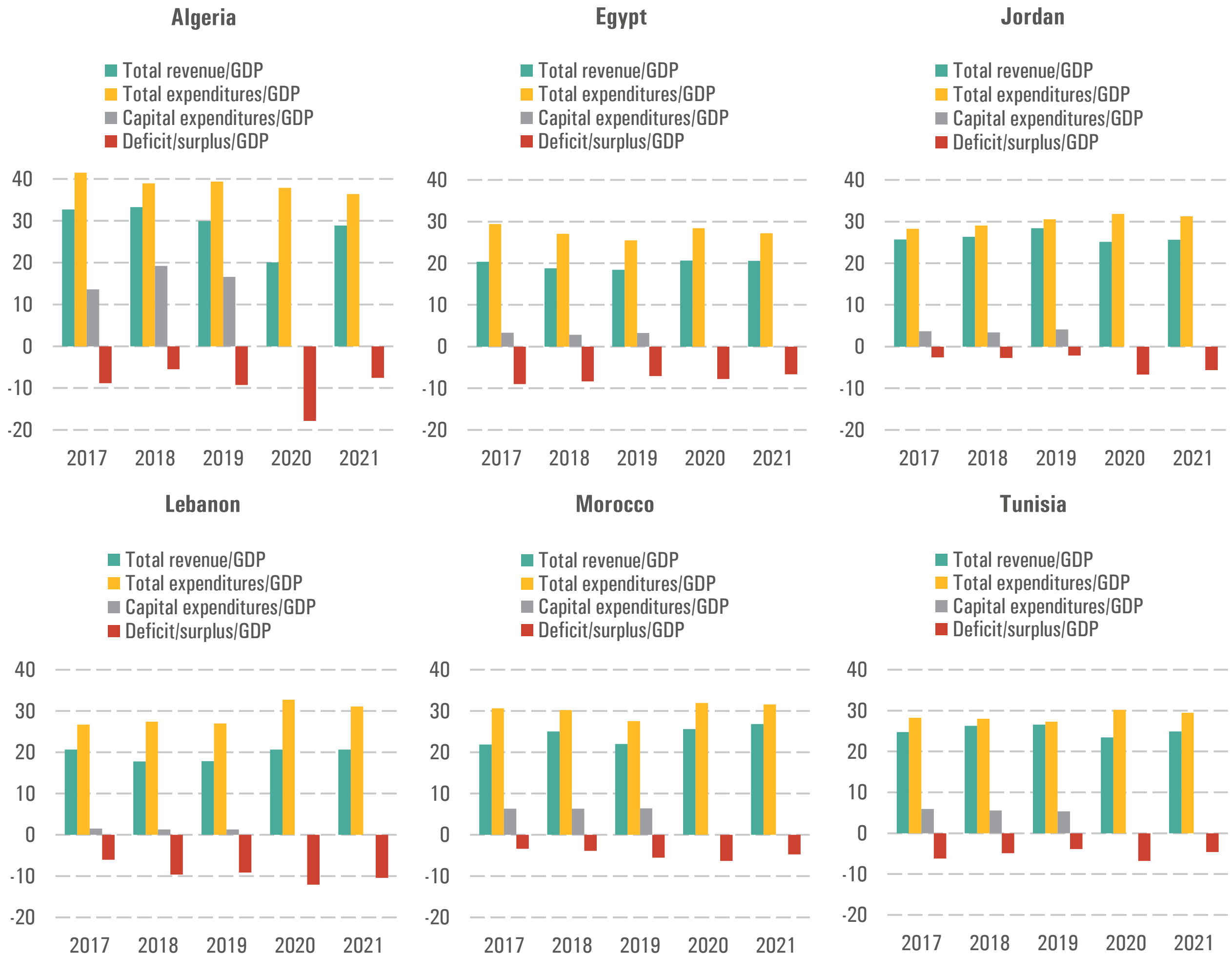
Jordan

fiscal deficit estimated at
7 per cent in 2020

Egypt

fiscal deficit estimated at
7.8 per cent in 2020

Figure 2.6 **Fiscal positions of Arab MICs, 2017-2021 (percentage of GDP)**



Sources: ESCWA staff estimations/forecasts based on national statistical sources; *DESA, World Economic Situation and Prospects as of mid-2020, World Economic Situation and Prospects 2020;* and ESCWA, Statistics Information Portal.

increased its expenditures substantially to finance measures to mitigate the impact of the pandemic. Consequently, the fiscal deficit is estimated to have increased to 7.8 per cent of GDP in 2020. The Government also created a special fund to support the tourism sector, responsible for 12 per cent of GDP and 10 per cent of employment. In May 2020, IMF approved a request by Egypt for assistance worth $2.77 billion in response to COVID-19 and in support of vulnerable groups and the most impacted economic sectors, notably the health sector.

In Morocco, government revenues decreased by 5 per cent in 2019 along with a 2 per cent decrease in expenditures, which led to a wider fiscal deficit from 3.9 per cent of GDP in 2018 to 5.5 per cent in 2019. This deficit increased further in 2020 to reach 6.3 per cent of GDP as a result of an 8 per cent increase in expenditures in 2020 (figure 2.6). The Government created a special fund financed by itself and tax-deductible voluntary contributions to support health infrastructure and help employees hit by the crisis.

In Tunisia, revenues increased by 10 per cent in 2019 along with a 6 per cent increase in expenditures, leading to a decrease in the fiscal deficit from 4.9 per cent of GDP in 2018 to 3.9 per cent in 2019. The debt-to-GDP ratio decreased from 76 per cent in 2018 to 73 per cent in 2019. However, with the outbreak of COVID-19, revenues are expected to drop by 9 per cent, while expenditures are expected to increase by 14 per cent to curtail the socioeconomic impact of the virus. The fiscal deficit is estimated to have increased to 6.8 per cent of GDP in 2020. The Government created a fund to cover expenditures related to mitigating the impact of COVID-19, and allocated 2 per cent of GDP to this fund.[4] In April 2020, IMF approved an emergency assistance loan of $745 million to support the Tunisian response to COVID-19 and to ease pressure on the country's public finances.

Morocco

fiscal deficit estimated at **6.3 per cent** in 2020

Tunisia

fiscal deficit estimated at **6.8 per cent** in 2020

D. Arab conflict-affected countries

Suffering from persistent unrest, the economies of conflict-affected countries are estimated to have contracted by 4.2 per cent in 2020 and are expected to recover by 3.1 per cent in 2021 (a contraction of 7.9 per cent in 2020 followed by 3.9 per cent growth in 2021 in the pessimistic scenario), following modest economic growth in 2019 of 1.4 per cent. Prior to the pandemic, the economies of conflict-affected countries were estimated to have grown by 4.5 per cent in 2020 and are expected to grow by 5.2 per cent in 2021.

The 2020 fall in oil prices and social unrest had a dire impact on the Iraqi economy, which is estimated to have contracted by 4.7 per cent in 2020 before recovering by a projected 4.2 per cent in 2021 (a contraction of 8.8 per cent in 2020 followed by 5.2 per cent growth in 2021 in the pessimistic scenario). In 2019, Iraq benefited from an increase in crude oil production (up by 6.3 per cent) and a rebound in non-oil economic activity, leading to an economic growth of 3.2 per cent in 2019. Before the outbreak of COVID-19, this trend was expected to continue in 2020 and 2021, with a projected growth rate of 4.8 and 5.8, respectively.

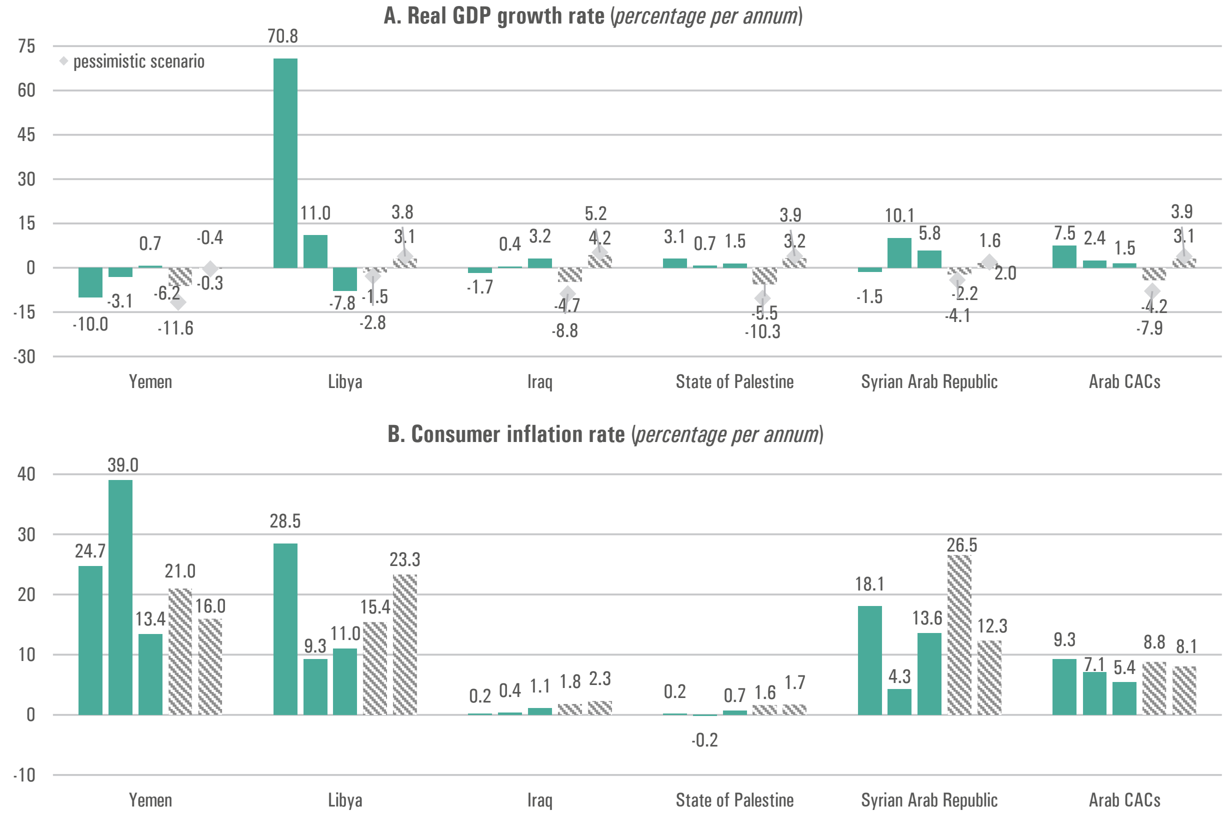
Prior to the pandemic, the Syrian Arab Republic was expected to grow at a rate of 3.7 per cent in 2020 and 3.3 per cent in 2021. However, these projections were affected by the outbreak of the virus and the revisions forecasted that the economy would contract by 2.2 per cent in 2020 before recovering modestly by 1.6 per cent in 2021 (a contraction of 4.1 per cent in 2020 followed by 1.6 per cent growth in 2021 in the pessimistic scenario). In 2019, many parts of the country were witnessing a relatively stable security situation, an increase in reconstruction activities and a gradual return of activity in certain sectors, such as agriculture and services. The economy grew at a rate of 5.8 per cent in 2019.

With the conflict unlikely to end in Libya in 2020, GDP was expected to shrink by 1.5 per cent in 2020 (2.8 per cent in the pessimistic scenario) compared with an estimated 4.5 per cent growth rate projected before the pandemic and the fall in oil prices. A recovery is expected in 2021, with a 3.1 per cent growth rate in 2021 (a contraction of 3.8 per cent in the pessimistic scenario). In 2019, the economy suffered from a severe contraction of 7.8 per cent in 2019 caused by increased conflict and the failure to reach an agreement between warring parties.

In Yemen, the economy is still suffering from fragmented national institutions and protracted armed conflict. In 2020, the economy is estimated to have contracted by 6.2 per cent (a contraction of 11.6 per cent in the pessimistic scenario), compared with a 3.6 per cent projection before COVID-19, and by 0.3 per cent in 2021 (a contraction of 0.4 per cent in the pessimistic scenario). In 2019, economic growth increased slightly by 0.7 per cent as a direct consequence of balance of payments assistance from Saudi Arabia and a gradual recovery of oil and gas production.

In the State of Palestine, GDP is estimated to have decreased by 5.5 per cent in 2020 (a contraction of 10.3 per cent in the pessimistic scenario) as a result of COVID-19 effects on donors and uncertainties about a resolution to the standoff on revenue clearance between the Palestinian and Israeli authorities. Prior to the pandemic, economic growth was expected to reach 2.6 per cent in 2020 and 2021. In 2021, the economy is projected to show signs of improvement, as the economies of donor countries begin to recover and aid flows resume. The Palestinian economy is expected to grow by 3.1 per cent in 2021 (3.8 per cent in the pessimistic scenario). In 2019, the economy grew at a rate of 1.5 per cent, suffering mostly from business, capital-flow and mobility restrictions under the Israeli occupation and a decline in aid levels.

Figure 2.7 **GDP and inflation in Arab CACs, 2017-2021**



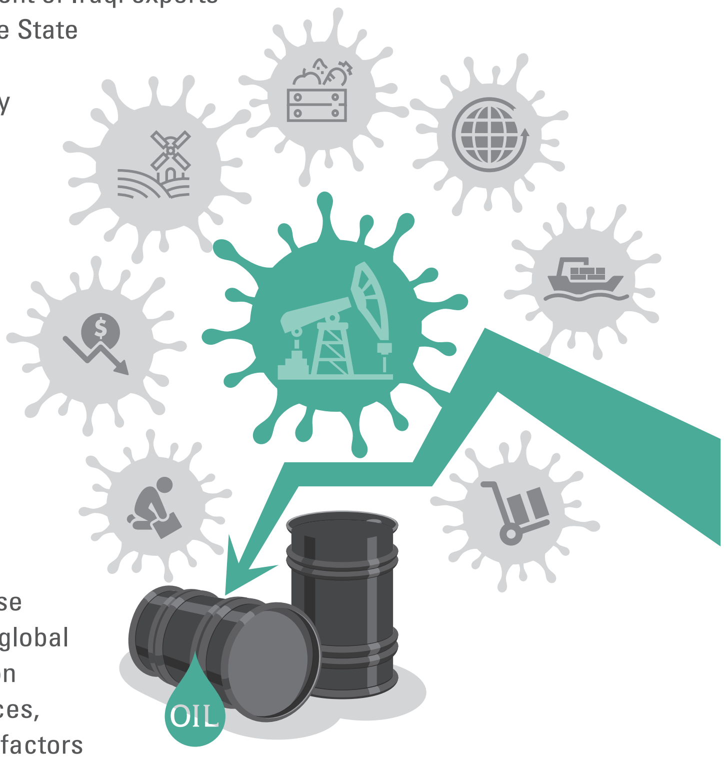
Sources: ESCWA staff estimations based on national statistical sources; *DESA, World Economic Situation and Prospects as of mid-2020, World Economic Situation and Prospects 2020;* and ESCWA, Statistics Information Portal.

The problems considered in the pessimistic scenario affect Arab conflict-affected countries similarly, doubling the expected GDP loss from 4.2 per cent to 7.9 per cent. The most significantly affected were the State of Palestine and Yemen. Even though projections for 2021 in the pessimistic scenario are slightly corrected upwards, this change does not compensate for the significant recession in 2020.Inflation rates in conflict-affected countries are estimated at 8.8 per cent on average in 2020 and are expected to decrease slightly to 8.1 per cent in 2021, with large disparities between countries. Libya, the Syrian Arab Republic and Yemen continued suffering from hyperinflation in 2020. Inflation is estimated to have increased from 11 to 15.4 per cent in Libya between 2019 and 2020, from 13.6 to 26.6 per cent in the Syrian

Arab Republic, and from 13.4 to 21 per cent in Yemen. In Iraq and the State of Palestine, inflation rates rose slightly but remained at low levels, increasing to 1.8 and 1.6 per cent, respectively.

With the return of oil production in Libya in 2017 and in Iraq in 2018, Arab conflict-affected countries have become net exporters since 2017. In 2019, their total exports amounted to $108 billion against $75 billion of imports. Exports from Iraq stood at around $86 billion and imports at around $39 billion in 2019, while exports from Libya reached $20 billion and imports hit $10 billion in the same year.

China was the main trading partner of Arab conflict-affected countries, particularly for oil products. Approximately 26 per cent of Iraqi exports and 19 per cent of Libyan exports went to China. The State of Palestine, the Syrian Arab Republic and Yemen exported mainly to other Arab countries, particularly neighbouring countries and Saudi Arabia. Their exports include agricultural and food products. All Arab conflict-affected countries import mainly from China and Turkey.



Ongoing conflict is affecting the external balance as a result of depressed business confidence and its negative impact on FDI inflow. Remittances and foreign aid play a key role in financing imports and in supplying foreign reserves. Lower oil prices recorded in 2020 are likely to improve trade balances for oil-importing conflict-affected countries, namely the Syrian Arab Republic and Yemen, as their import bill will decrease significantly. However, it is short-term relief, as the global economic recession will have severe implications on domestic unemployment and the inflow of remittances, and will contribute to increasing debt levels. These factors are likely to have adverse long-lasting implications.

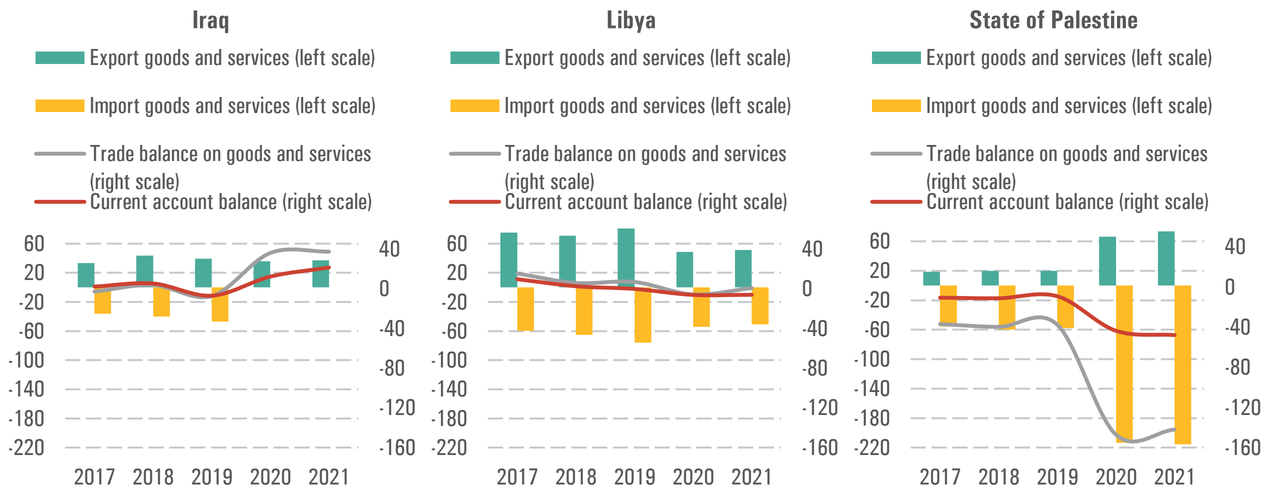
Social unrest in Iraq in 2019 affected trade, particularly merchandise exports. Trade surplus declined from $36 billion in 2018 to $17 billion in 2019. This decline was also reflected in the current account balance, which deteriorated from a surplus of 5.2 per cent to a deficit of 7.1 per cent of GDP between 2018 and 2019. The situation is likely to improve in the period 2020-2021, conditioned on a stable security situation, recovery of the global economy, and resumption of demand for oil exports.

In the State of Palestine, the current account deficit decreased from $1.7 billion in 2018 to $1.4 billion in 2019. The inflow of foreign aid and remittances play an important role in financing the external sector. In 2019, the current account deficit declined to 9.3 per cent, while the trade deficit reached 37.8 per cent of GDP.

In Libya, increased oil production since 2017 continued to have a positive impact on the trade balance, which recorded a surplus of 6.7 per cent of GDP in 2019. This situation changed in 2020, as the sharp decline in oil prices and the drop in global demand negatively affected export revenues, generating a trade deficit of 5.8 per cent. This deficit affected the current account, which is estimated to have recorded a deficit of 6.3 per cent of GDP in 2020.

Arab conflict-affected countries have limited fiscal capacity to deal with the pandemic and the fiscal repercussions of lockdowns. By mid-June 2020, the number of COVID-19 cases reported in these countries, except Iraq, was significantly lower than in other Arab countries. Their focus is therefore on preventing and containing the virus rather than dealing with its economic consequences.

Figure 2.8 **Trade and current account balances in Arab CACs, 2017-2021 (percentage of GDP)**



Sources: ESCWA staff estimations based on national statistical sources; *DESA, World Economic Situation and Prospects as of mid-2020, World Economic Situation and Prospects 2020;* and ESCWA, Statistics Information Portal.

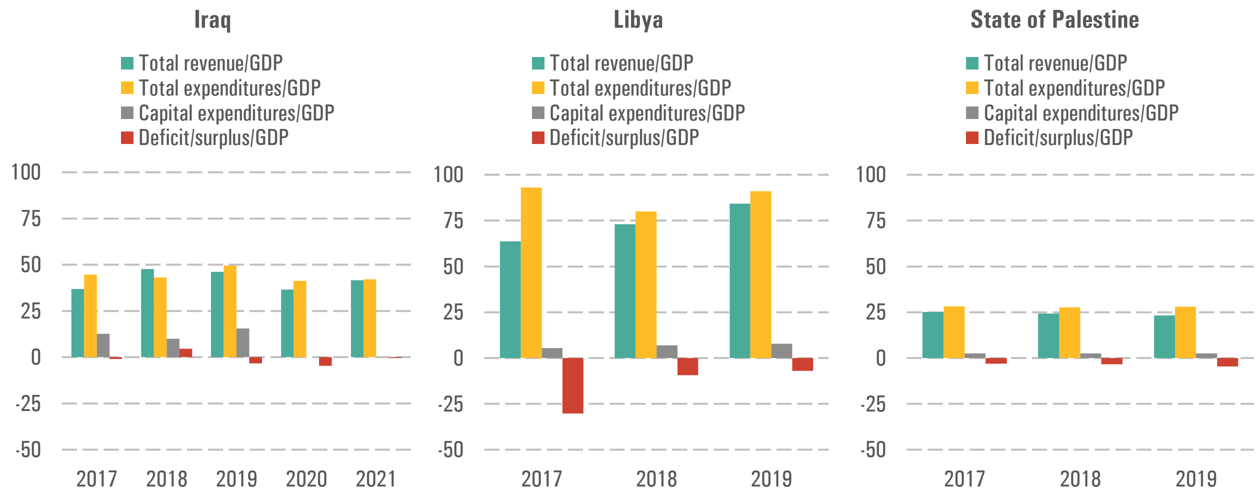
Note: Owing to a lack of official statistics, figures for the Syrian Arab Republic and Yemen are not presented.

Governments in conflict-affected countries have either allocated funds, or plan to increase spending on health. Iraq, for example, is in discussions with international organizations to obtain the necessary medical equipment to treat the virus.

The unprecedented decline in oil prices in 2020 has placed additional pressure on the public finances of Iraq and Libya, widening their fiscal deficit and increasing their indebtedness. In Iraq, the fiscal balance moved from a surplus in 2018 to a deficit in 2019. This deficit increased from 3.3 per cent to 4.7 per cent of GDP between 2019 and 2020, then it is expected to decrease to 0.4 per cent of GDP in 2021 as global demand for oil rises. In Libya, increased oil production contributed to closing part of the government deficit in 2019, which decreased from 9.4 per cent in 2018 to 6.9 per cent in 2019.

The Government of the Syrian Arab Republic is likely to increase expenditures on reconstruction activities. The fiscal deficit is estimated at 6.3 per cent of GDP in 2020 and is expected to reach 9.1 per cent in 2021.

Figure 2.9 **Fiscal positions of Arab conflict-affected countries (percentage of GDP)**



Sources: ESCWA staff estimations/forecasts based on national statistical sources; *DESA, World Economic Situation and Prospects as of mid-2020, World Economic Situation and Prospects 2020*; and ESCWA, Statistics Information Portal.

Note: Owing to a lack of official statistics, figures for the Syrian Arab Republic and Yemen are not presented.

Box 2.3 **COVID-19, conflict and risks**

Suffering from prolonged conflicts and occupation, Arab conflict-affected countries were witnessing health and economic crises before the outbreak of COVID-19. Largely cut off from international travel, these countries avoided the brunt of the virus at first, when many countries worldwide were under total lockdown. However, in the spring and summer of 2020, cases rose precipitously, particularly in Iraq, Libya, the State of Palestine and the Syrian Arab Republic.

COVID-19 poses a great threat to conflict-affected countries that were already suffering from many of the world's worst humanitarian crises. Around 80 per cent of the Yemeni population (24.1 million persons) required humanitarian assistance as at January 2020, while 11.1 million Syrians, 4.1 million Iraqis, 2.4 million Palestinians, and 900,000 Libyans were in need of emergency aid. Health-care systems were on the verge of collapse before the outbreak. These countries were suffering from a low density of medical doctors (Iraq and the Syrian Arab Republic) as a large number of them had migrated, destruction of health infrastructure (Syrian Arab Republic and Yemen), and occupation and blockades (State of Palestine). The pandemic has only exacerbated the plight of those caught up in humanitarian crises, while the living conditions of refugees and internally displaced communities have deteriorated markedly in recent months. The health sector is facing mounting challenges, and ensuring water security is more imperative than ever.

The pandemic struck at a time when conflict-affected Arab countries were already suffering from a series of structural challenges, including eroded social and institutional capacities, corrupt and fragmented governance, large-scale disasters induced by the climate crisis, and inequality and socioeconomic deprivation. In addition to humanitarian and public service crises, the economic situation in these countries has worsened in recent months, as the pandemic unleashed a global economic crisis unmatched since the Great Depression.

In the absence of peace, there is little hope of minimizing the effects of the pandemic in the short term, let alone of "building back better". The international community has a political role in encouraging and using its leverage to convince conflicting actors to heed the call of the United Nations Secretary-General made in March 2020, and its subsequent endorsement by the Security Council in resolution 2532 (2020) of 1 July 2020, for a global humanitarian truce that would help alleviate humanitarian crises and potentially create an opportunity for sustainable political resolution of ongoing conflicts.

Resolving conflicts and combating the pandemic require swift and coordinated global, regional and local action. Without such concerted intervention at these three levels, violence will persist and the pandemic will continue to spread, thereby deteriorating the governance capacity and socioeconomic conditions of Arab conflict-affected countries. Furthermore, the compounded crisis will exacerbate the risks of violence and its transboundary impact on neighbouring countries, and will undermine ability to confront other risks, such as climate change, water scarcity, and food insecurity. In addition, building local and national governance structures capable of mitigating different types of shocks, such as pandemics, violence and socioeconomic hardship, is essential for a sustainable reconciliation process and establishing peace.

Source: ESCWA, "COVID-19, conflict, and risks in the Arab Region: The need to end hostilities and invest in peace" (forthcoming).

E. Arab least developed countries

Arab LDCs face significant socioeconomic challenges that were exacerbated by the spread of COVID-19. Prior to the pandemic, the economies of Arab LDCs were expected to grow at a rate of 0.8 and 1.6 per cent in 2020 and 2021, respectively. However, the revised outlook is unfavourable. Economic growth is estimated to have contracted by 3 per cent on average in 2020 (a contraction of 5.5 per cent in the pessimistic scenario) and is expected to stabilize in 2021. In 2019, the economy witnessed a contraction of 0.6 per cent on average, marking the second consecutive year of negative growth, largely attributed to an economic deceleration in the Sudan, which is the largest economy in this group of countries. The Sudanese economy shrunk in 2019 by an estimated 2.5 per cent. Political uncertainty in the country has contracted growth in the services sector and investments in real estate and business sectors, while agriculture suffered from shortages of inputs, notably fuel. GDP is estimated to have contracted further by 3.3 per cent in 2020 (a contraction of 6.2 per cent in the pessimistic scenario), and will stagnate in 2021 owing to the political situation, a decrease in domestic demand, and weak private sector investments.

Djibouti was the only LDC to witness positive economic growth in 2020 (2 per cent growth rate in the baseline scenario), but at a slower rate than in 2019. In the pessimistic scenario, the Djiboutian economy is estimated to have slightly contracted by 0.1 per cent. Djibouti performed well in 2019 where GDP growth stabilized at 6.8 per cent, by taking advantage of the establishment of a free-trade zone, a desalination plant and road infrastructure. Before the pandemic, the 2019 rate was expected to persist for 2020 and beyond.

The Comoros has been mildly impacted by the COVID-19 crisis, with a 0.5 per cent loss in GDP in 2020 and 2 per cent projected growth in 2021 (a contraction of 0.9 per cent in 2020 followed by 2.5 per cent growth in 2021 in the pessimistic scenario). In 2019, economic growth in the Comoros increased at a slower pace because of a decrease in the agriculture and infrastructure sectors, which converted into an economic growth rate of 2.5 per cent in 2019 compared with 2.8 per cent in 2018.

Mauritania and Somalia also had relatively stable economic environments. In Mauritania, GDP growth in 2019 is estimated at 5.1 per cent, up from 3 per cent in 2018, as a result of mining sector development and a rise in fishing sector exports. The pandemic has affected projections and the economy is estimated to have contracted by 1.2 per cent in 2020 and is expected to grow by

Djibouti

2 per cent growth rate estimated in 2020

Comoros

0.5 per cent contraction in 2020
2 per cent recovery in 2021

3.1 per cent in 2021 (a contraction of 2.2 per cent per cent in 2020 followed by 3.8 per cent growth in 2021 in the pessimistic scenario). Somalia registered an increased growth rate from 3.1 per cent in 2018 to almost 3.5 per cent in 2019. The economy is estimated to have contracted by 1 per cent in 2020 before recovering by a projected 2 per cent in 2021 (a contraction of 1.9 per cent in 2020 followed by 2.5 per cent growth in 2021 in the pessimistic scenario). Differences between baseline and pessimistic forecasts are most significant for the Sudan, with more than a 6 per cent slump in GDP as a result of a recession year in 2019. This projection will be revised downwards in view of the devastating flood in September 2020 (box 2.4).

Inflation is still under control in all Arab LDCs, except the Sudan. Rates varied between 1.3 per cent in Somalia and 5.4 per cent in Mauritania in 2019, and are expected to stabilize or increase slightly over the period 2020-2021.

Mauritania

1.2 per cent contraction in 2020
3.1 per cent recovery in 2021

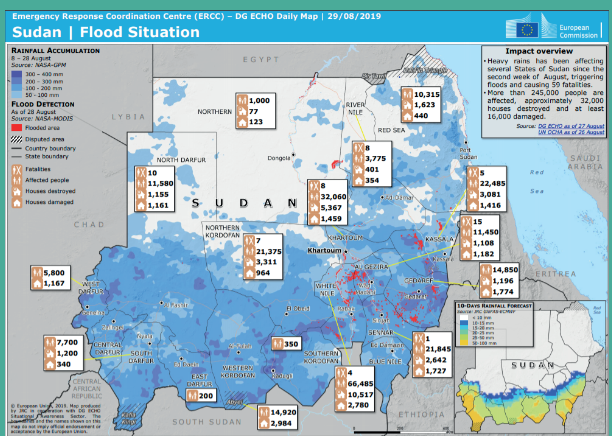
Somalia

1 per cent contraction in **2020**
2 per cent recovery in **2021**

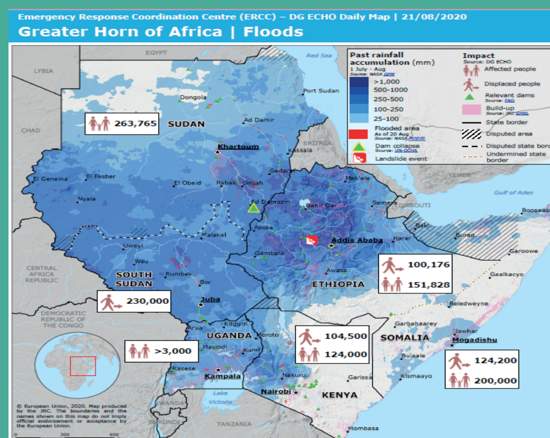
Box 2.4 **A devastating flood hit the Sudan**

Before the flood, the Sudan was already suffering rom a 50 per cent drop in its GDP, declining from $66.4 billion in 2011 to $33.68 billion in 2019. As a consequence of the COVID-19 lockdown, the economy is likely to further shrink by 3.3 per cent in 2020 on top of a 2.5 per cent loss to GDP in 2019. This growth loss is depriving the country from badly needed income, forcing it to resort to borrowing, although an unsustainable debt-to-GDP ratio of 212 per cent makes it one of the highest indebted countries worldwide. Moreover, owing to a structural trade imbalance, exports have been declining at a rate of 10 per cent a year since 2013, and imports were losing 8 per cent a year on average.

Map 1: 29 August 2019



Map 2: 21 August 2020



Source: Map 1: "Sudan, flood situation", Emergency Response Coordination Centre (ERCC) – DG ECHO Daily Map, 29 August 2019; Map 2: "Greater Horn of Africa, floods", Emergency Response Coordination Centre (ERCC) – DG ECHO Daily Map, 21 August 2020.

The floods have affected over 650,000 people to date, destroying or damaging more than 125,000 homes, with 39 people dead in 17 of the country's 18 States, leading the Government to declare a three-month state of emergency. The floods are impacting subsistence agriculture, cash crops and the food security of 8.1 million people, 2.7 of whom are internally displaced persons (IDPs) and refugees from South Sudan. The damage has not been limited to the agriculture and water sectors. A total of 2,671 health facilities have been damaged, significantly limiting capacity to respond to emerging needs on top of the strain already imposed by the pandemic. Schools serving as temporary shelters for displaced families have also reached maximum capacity.

Poverty rates were estimated at 53.4 per cent in 2020 and are expected to reach 55.6 per cent in 2021 owing to a fall in purchasing power, caused by high inflation rates that reached 136 per cent in 2020, thus undermining the purchasing power of those who still have incomes and impacting the livelihoods of tens of millions of Sudanese. If the economic slowdown continues unabated, it will negatively impact employment, real wages and the flow of remittances, which had already declined by $500 million in 2020. It is estimated that $10.2 billion will be needed to close the poverty gap. At this scale and depth of poverty, no domestic solidarity redistribution can achieve poverty eradication. Instead, international donor support is needed, both in the immediate and longer term, to facilitate recovery.

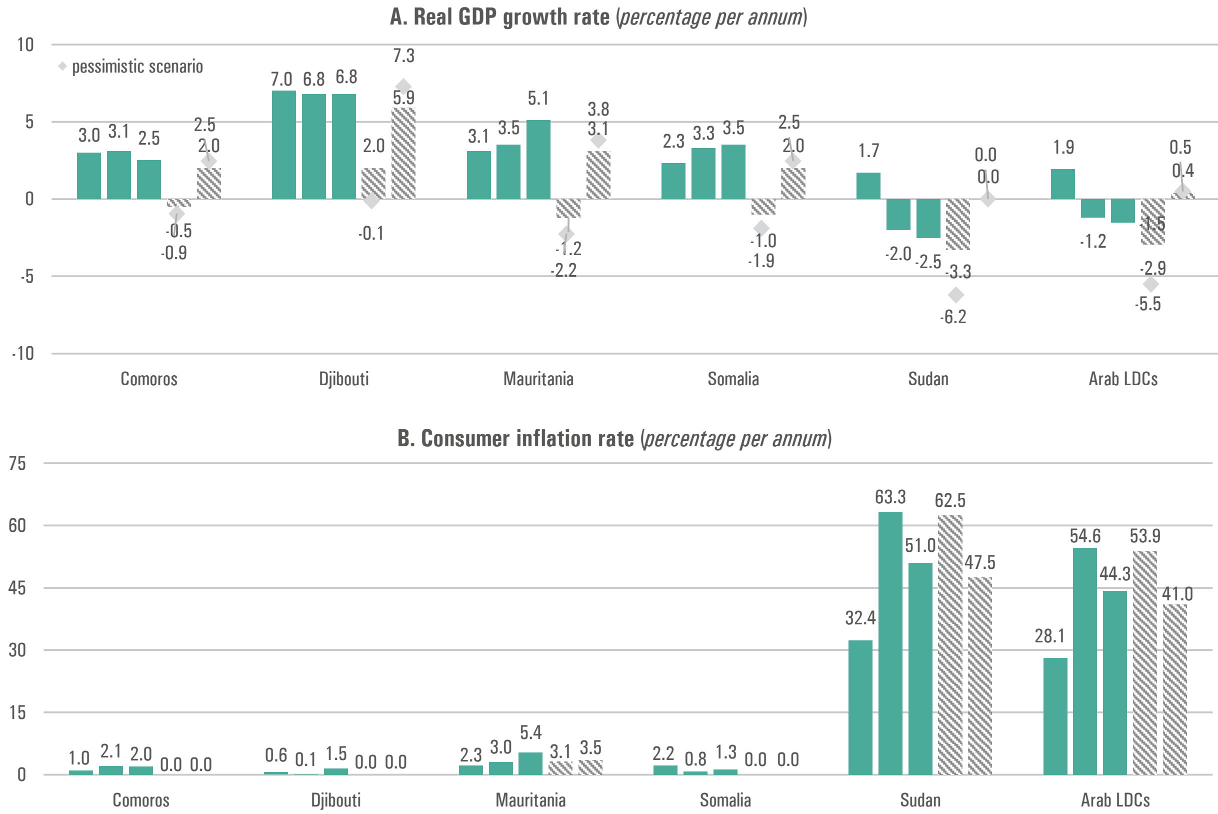
The inequality gap will increase and poor people will be disproportionately affected, not only because they are more exposed and more vulnerable to flooding, but also because they are highly dependent on unstable agricultural, fishing and other ecosystem-related income. Consequently, they have fewer resources and receive less support from the community, the financial system, and social safety nets.

Source: Food and Agriculture Organization of the United Nations, "Sudan revised humanitarian response Coronavirus disease 2019 (COVID-19)" May – December 2020; and E/ESCWA/CL2.GPID/2020/TP.10.

However, in the Sudan, hyperinflation is likely to persist, and rates, estimated at 62.5 per cent in 2020, are expected to reach 47.5 per cent in 2021. The devaluation of the currency in 2018 and the balance of payment constraints in the Sudan further exacerbated socioeconomic conditions. This was followed by hyperinflation that reached 63.3 per cent in 2018. Hyperinflation persisted in 2019, and fuelled demonstrations and political unrest that led to the departure of President Al Bashir.

Arab LDCs continue to be net importers, with merchandise exports amounting to $13 billion and imports to $18 billion in 2019. Intraregional exports represent around 52 per cent of total exports, driven mainly by exports from the Sudan, which exported around $4.8 billion to other Arab countries in 2019. Imports from Asia and the Pacific amounted to 43 per cent of total imports in 2019, driven mainly by Mauritania, Somalia and the Sudan. Together these countries imported around $6.7 billion in 2019. Other Arab and European countries together captured around 48 per cent of total imports in the same year.

Figure 2.10 GDP and inflation in Arab LDCs, 2017-2021



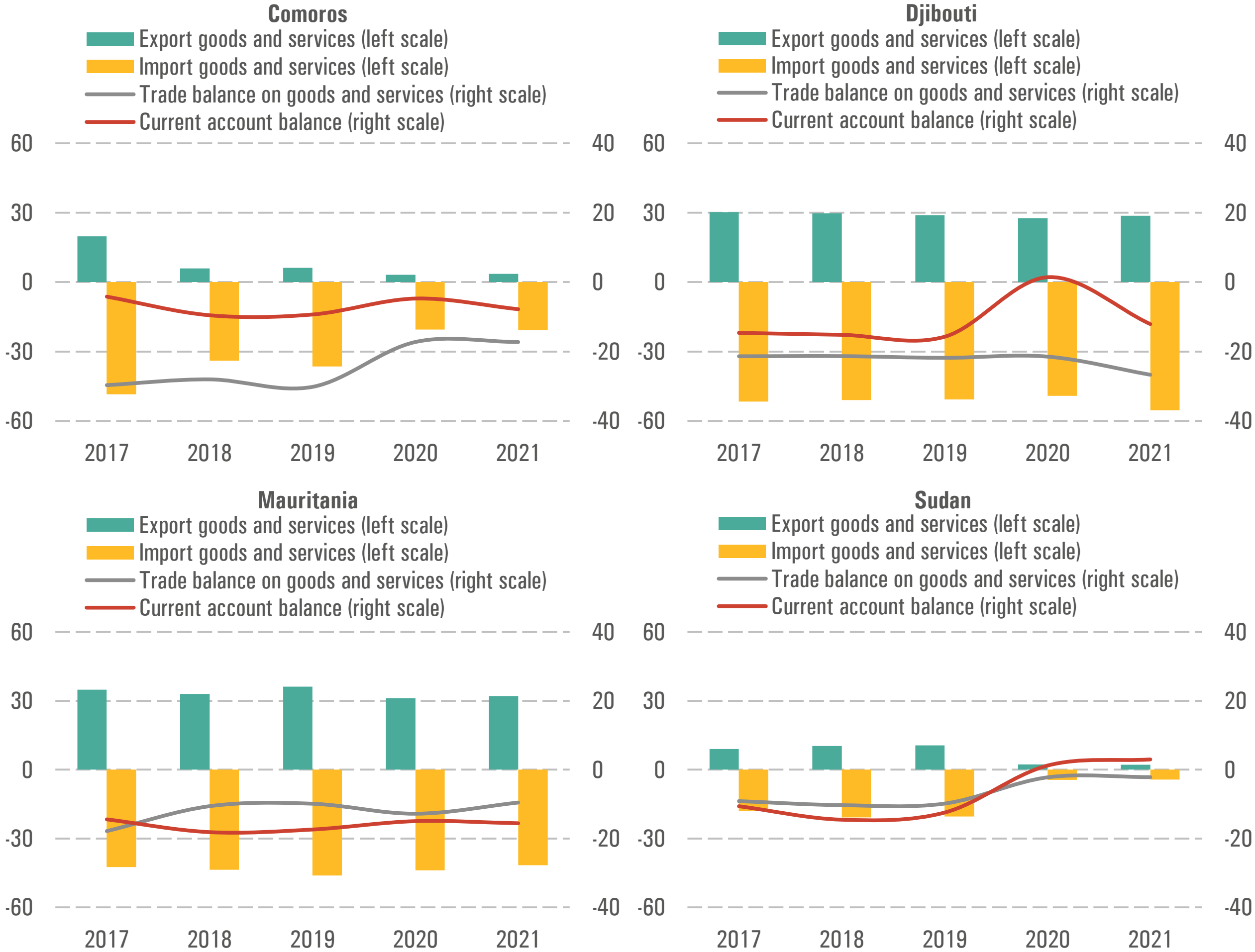
Sources: ESCWA staff estimations based on national statistical sources; *DESA, World Economic Situation and Prospects as of mid-2020, World Economic Situation and Prospects 2020;* and ESCWA, Statistics Information Portal.

Arab LDCs rely significantly on external support to address their socioeconomic challenges, particularly balance of payment constraints and debt sustainability. The consolidated current account recorded a deficit of 13.3 per cent in 2019. Trade is estimated to have deteriorated further, with exports losing 11.1 per cent on average in 2020, and imports falling by 6.6 per cent only. The rebound in 2021 will be slow, with a 7.2 per cent increase in exports and a 5.6 per cent rise in imports.

At the country level, all Arab LDCs were suffering from current account and trade deficits in 2019. The Comoros and Djibouti witnessed a large trade deficit in 2019, of around 30.2 and 21.8 per cent of GDP, respectively. In Mauritania and the Sudan, the deficit was around 9.9

per cent. In the Comoros and the Sudan, this deficit is estimated to have increased to 17.2 and 2.2 per cent, respectively, in 2020 because of a decline in imports. This would have a positive impact on the current account deficit, which is estimated to have decreased to 4.7 per cent in the Comoros in 2020. In Djibouti and the Sudan, the current account recorded a surplus of 1.4 and 1.2 per cent of GDP, respectively. Both the

Figure 2.11 **Trade and current account balances of Arab LDCs, 2017-2021 (percentage of GDP)**

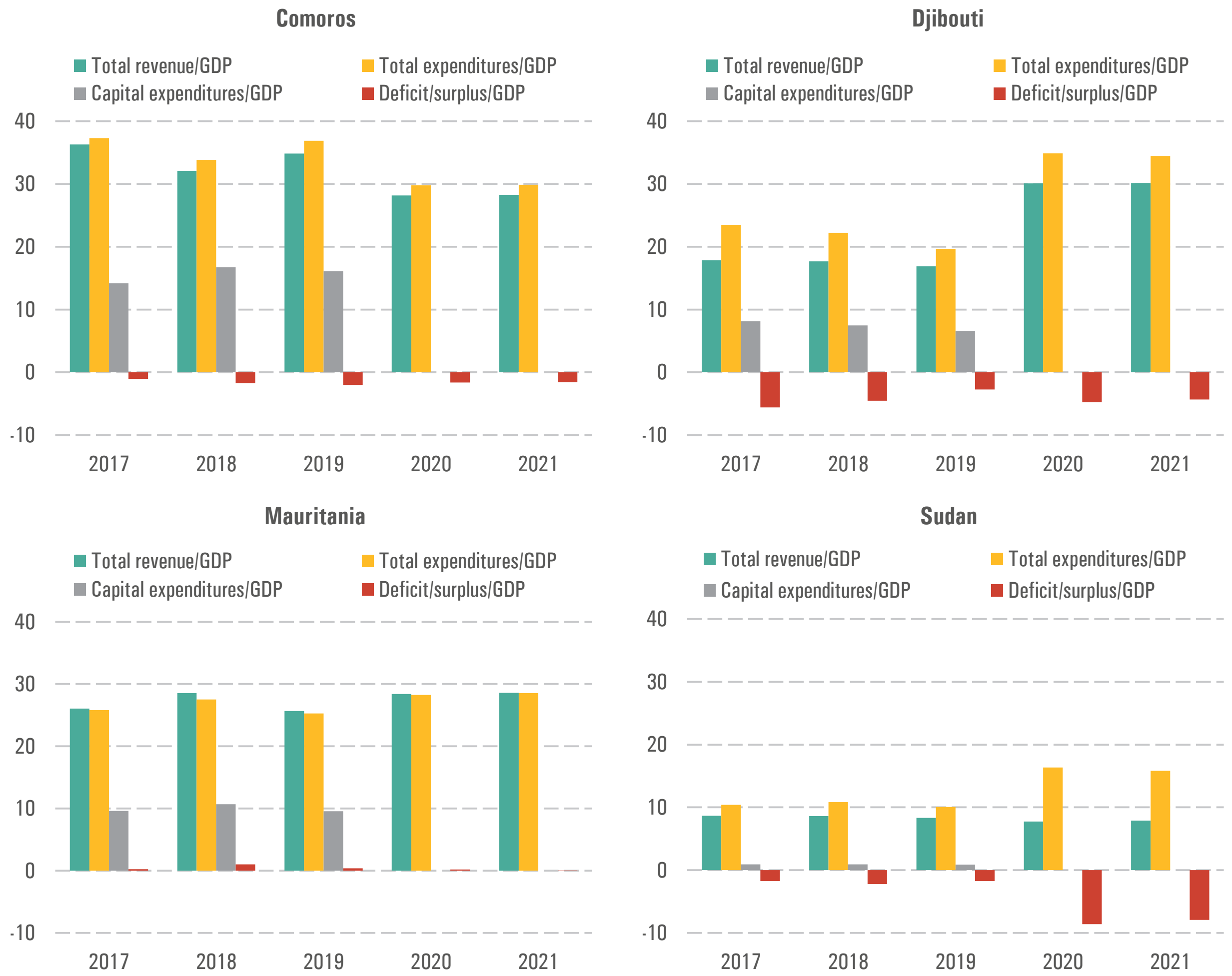


Sources: ESCWA staff estimations based on national statistical sources; *DESA, World Economic Situation and Prospects as of mid-2020, World Economic Situation and Prospects 2020;* and ESCWA, Statistics Information Portal.

Note: Owing to a lack of official statistics, figures for Somalia are not presented.

Comoros and Djibouti will benefit from IMF debt service relief under the Catastrophe Containment and Relief Trust, and from emergency assistance from IMF for balance of payment support and health spending ($12 million for the Comoros and $43 million for Djibouti). Mauritania received approval for a $130 million IMF credit facility.

Figure 2.12 **Fiscal positions of Arab LDCs, 2017-2021 (percentage of GDP)**



Sources: ESCWA staff estimations based on national statistical sources; *DESA, World Economic Situation and Prospects as of mid-2020, World Economic Situation and Prospects 2020;* and ESCWA, Statistics Information Portal.

Note: Owing to a lack of official statistics, figures for Somalia are not presented.

Arab LDCs are all suffering from severe budgetary constraints. With the spread of COVID-19, these countries have limited fiscal space to deal with the pandemic and the fiscal repercussions of lockdowns. Their policies are focused mainly on prevention and containment, rather than on dealing with economic consequences. In that regard, their Governments issued only broad declarations to increase spending on health. Part of the assistance received by the Comoros and Djibouti was earmarked to increase spending on the health sector to fight the virus. The Comoros also received $12 million in financial assistance from IMF to address the repercussions of the cyclone in 2019.

In 2020, fiscal deficits widened in Djibouti and the Sudan, with the deficit increasing from 2.8 to 4.8 per cent of GDP in Djibouti, and from 1.7 to 8.6 per cent of GDP in the Sudan. The significant deficit increase in the Sudan is also attributed to the depreciation of the local currency, and expenditures increasing by 125 per cent in 2020 along with only a 29 per cent increase in revenues. The Comoros witnessed a slight improvement in its fiscal deficit from 2 to 1.6 per cent of GDP thanks to the financial assistance it received. Mauritania seems to be less affected by COVID-19, and its fiscal balance showed a slight surplus of 0.2 per cent of GDP in 2020. The country has showed relatively high levels of resilience to external shocks, with a mastery of public expenditure and an increase in mining revenues.

F. Concluding remarks

The outbreak of COVID-19 has plunged the Arab region into a recession in 2020. In oil-exporter countries, an unprecedented drop in oil prices and accompanying supply shock will deepen the recession, while lockdowns worldwide and interruptions to supply chains and production generated a demand shock in the oil market.

MICs suffered from recessions affecting their trading partners, which negatively affected their export demand, tourism sectors and remittance inflows. The recession in developed countries also affected Arab conflict-affected countries and LDCs through a reduction in ODA.

The 2021 recovery largely depends on the success of the stimulus packages enacted in the region, which exceed $180 billion. It also depends on the recovery of trading partners, and the success of the announced incentive packages.