GCC MACRO OUTLOOK 2022:
FROM TROUGH TO PEAK AND BACK TO U

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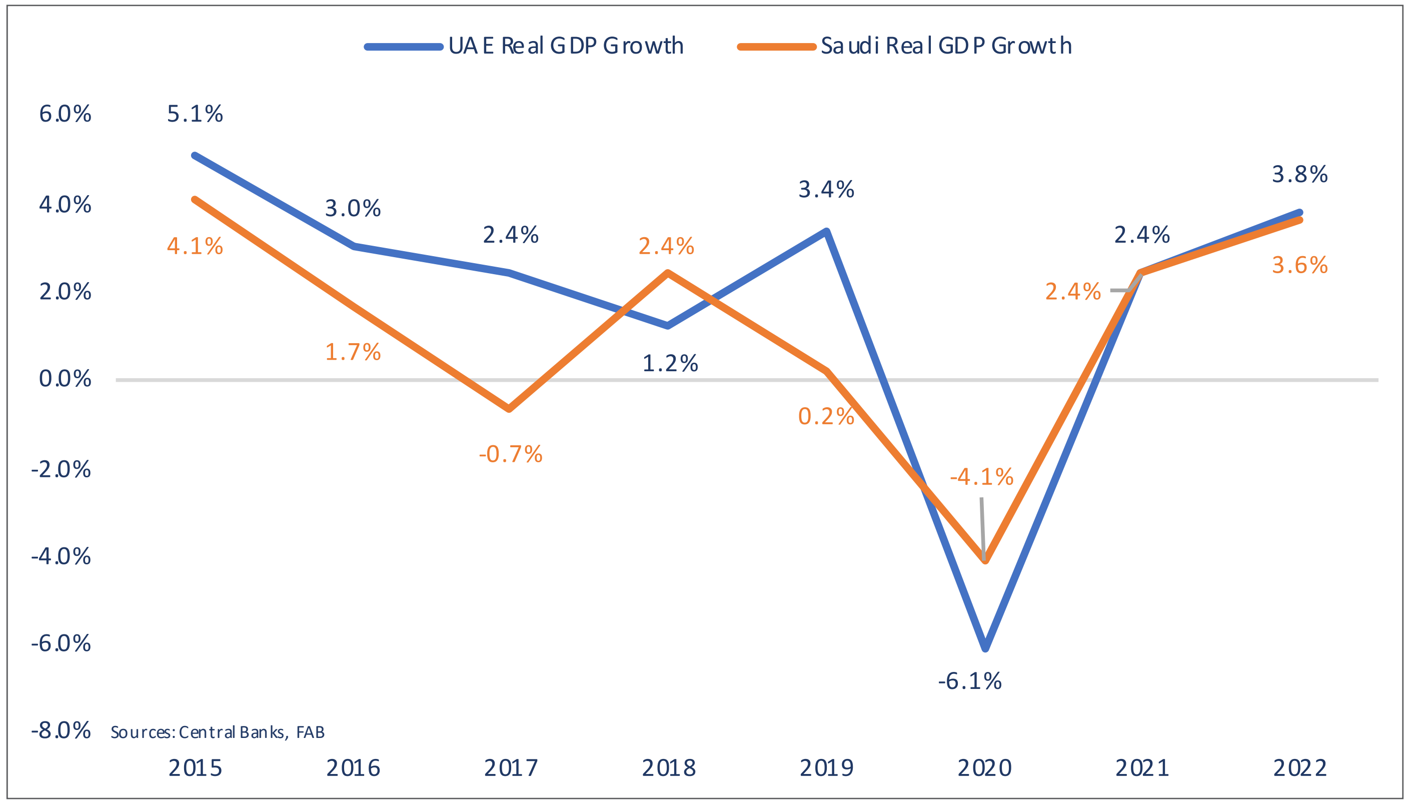
After the anticipated rebound in economic activity across the Gulf Cooperation Council (GCC) region in 2021, when growth recovered sharply from the recessionary nadir of the cycle in Q2 2020, the six GCC countries should see further positive advances in economic growth in 2022. Beyond that, we anticipate an easing in the rate of improvement and that the trajectory of the medium-term economic advance will be more of a 'shallow U shape' in nature. We believe that this will be the most sustainable outcome for reflation across the region.

UAE vs KSA GDP 'It's all about U'

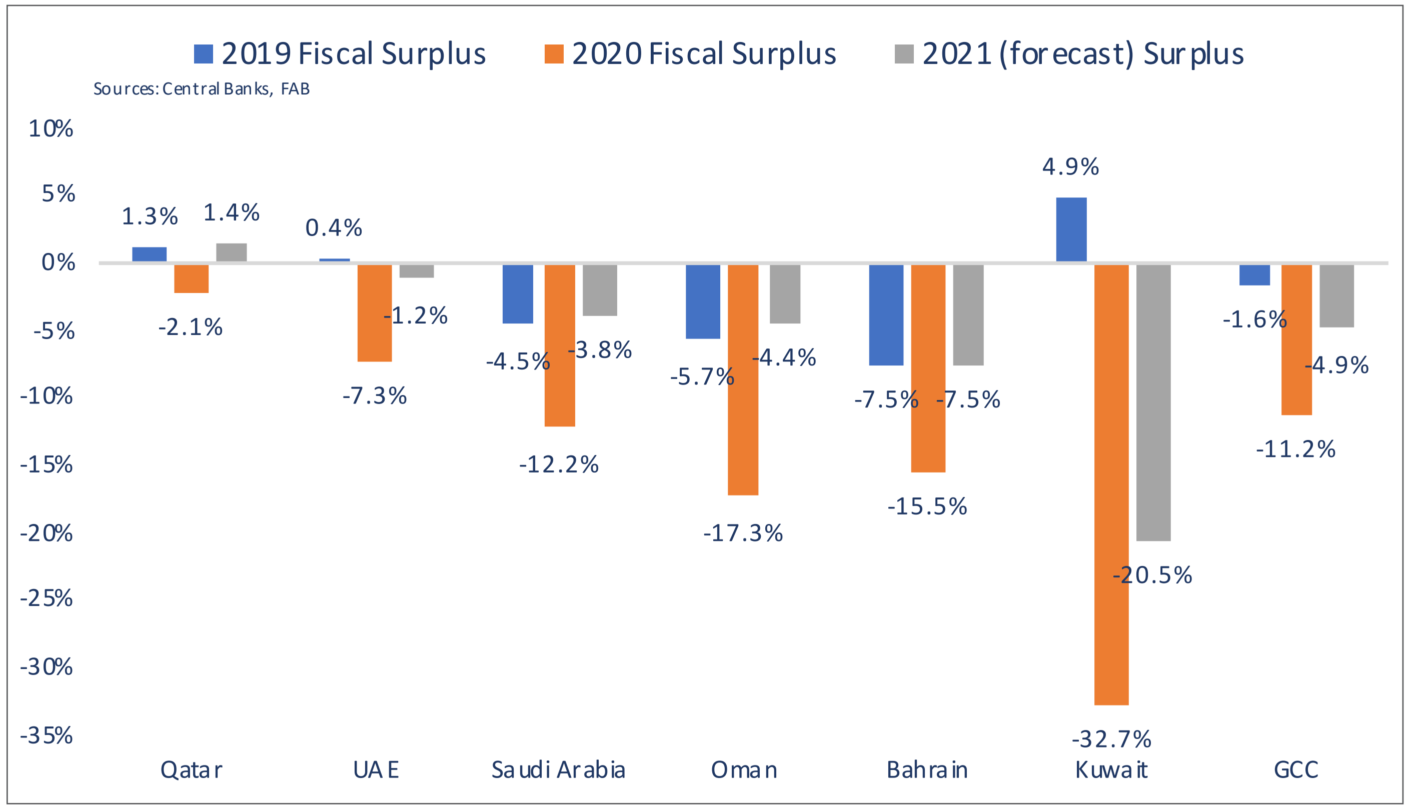


Economic performance across the region is forecast to strengthen as a result of the widespread vaccination programme that has helped to revive domestic activity and consumption and supported the re-opening of tourism -- which is particularly important to the United Arab Emirates (the UAE) --, and of the implementation of deeper structural reforms.

On balance, we believe that the aggregate GCC economy expanded by 2.1% during 2021. As global reflation continues to gain cautious momentum over the coming months, GCC economic growth should improve further and settle around a 4.4% growth rate for 2022. In the context of OPEC+ oil production cuts possibly ending by mid-2022, we assume that the private sector will be particularly important to the overall annual economic growth rate, particularly in Saudi Arabia (KSA), the UAE and Qatar.

With oil prices remaining buoyant, the fiscal and external sovereign positions in the region are expected to improve substantially over the coming years; the UAE and KSA expect their fiscal deficit positions of 2021 to move back towards balance or into surplus during 2022. In aggregate, we believe that while the fiscal deficits of KSA, Oman and Bahrain should continue to narrow during 2022, the fiscal positions of the UAE, Qatar and Kuwait should improve and return to a (small) surplus over the coming months.

GCC government fiscal balance positions
'The post-pandemic (gradual) road to recovery'



That said, at least across the major economies of the UAE and KSA, we expect to see the maintenance of modestly expansionary fiscal strategies that will be made possible by the large financial buffers, spare capacity and enhanced government revenues from firm oil prices.

As is the case in many regions around the world at present, inflation will remain a key threat to the monetary and fiscal status quo across the GCC during much of early 2022. However, while elevated commodity valuations will bolster price pressures, we continue to subscribe to the view that the latter will begin to recede as 2022 evolves and as we move further away from the inflation low point seen in the first half of 2020.

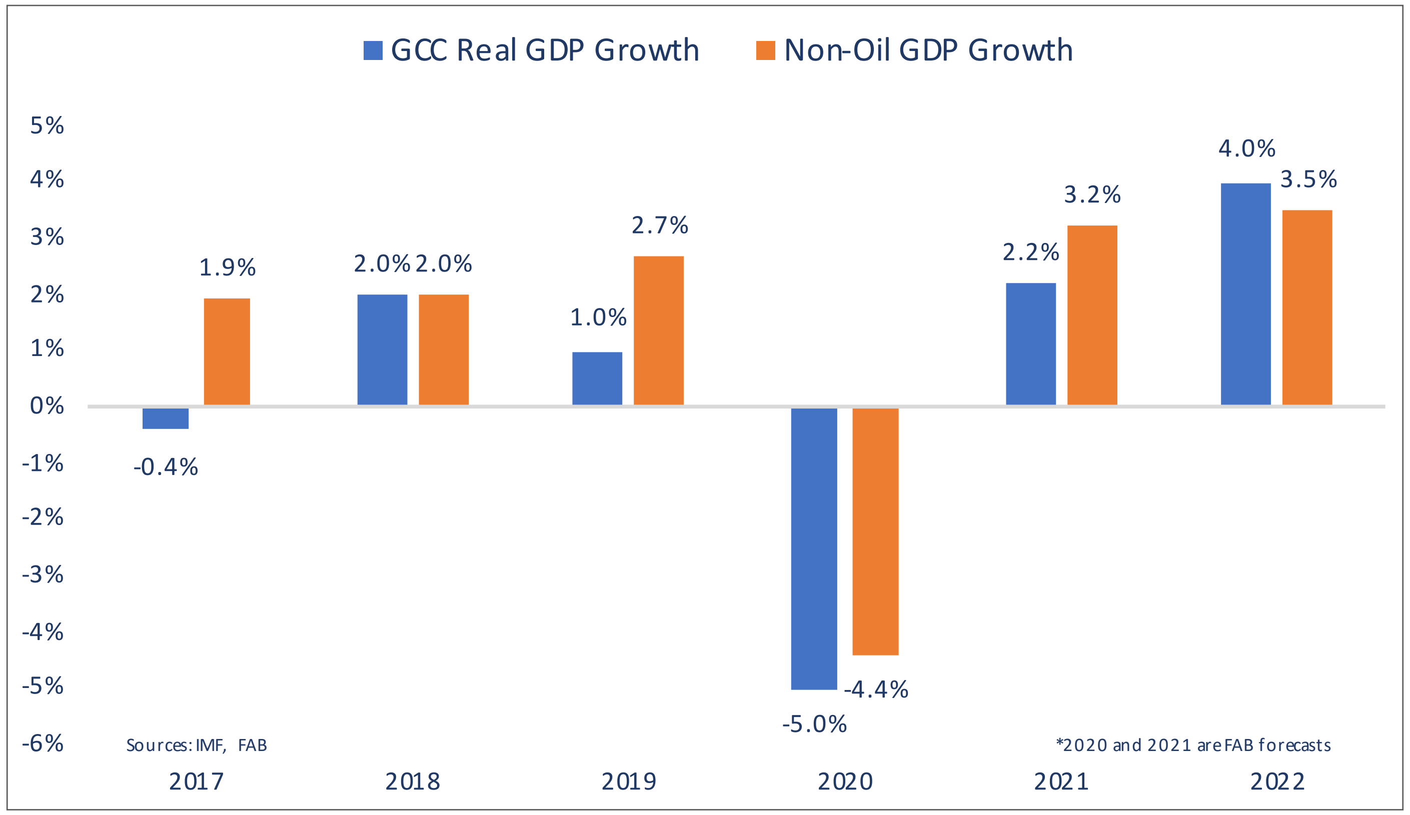
Moreover, we would conjecture that generic inflation pressures should remain relatively contained over the coming months as a result of pegged exchange rates across the region (with the exception of Kuwait, of course). Inflation can vary greatly from member state to member state though, albeit running on average between 2%-3% in 2021, buoyed by the strength in the oil price. Consequently, we do not anticipate any change in GCC central banks' policy rates during 2022; they will remain anchored to and continue to track US rates.

Structural reform will remain a key focus for governments across the region and a key foundation for improving economies during the coming year in the wake of what has unarguably been major progress on that front over the past several years. We have seen some major improvements in the business environment, including the promotion of a more favourable regulatory landscape across much of the GCC region in recent years and this, coupled with an acceleration in digital transformation, should help to further bolster the outlook for businesses and SMEs in the region. Similarly, strategies to promote new investments, including the relaxation of residency rules and longer-term Golden visas for expatriates, should help to enhance the UAE's status on the global corporate stage and to promote the country as a global hub for business and finance and an attractive tourist destination.

That said, there is a clear need for further reforms across the region, particularly across the non-financial sectors. While the GCC's financial environment continues to look robust to us, benefitting from a high-quality asset base, strong capitalisation and adequate liquidity, in the non-financial space, reforms will be key to achieving individual countries' economic diversification aspirations, but they will also serve as the foundations for improving and sustaining economic growth rates over the medium-term.

At the country level, Moody's Investors Service affirmed its A1 long-term issuer and senior unsecured ratings for Saudi Arabia on November 5th, 2021. At the same time, Moody's revised the outlook from negative to stable. To us, this reflects what we have long held as a positive macro fundamental outlook for the major GCC sovereigns (KSA and the UAE) through 2022.

GCC GDP growth trend
'A cautiously optimistic horizon'



Indeed this structural strength was also reflected in Fitch's affirmation of the UAE's AA credit rating in November, 2021, with the agency attributing the rating of the federal government to the country's moderate consolidated public debt, strong net external asset position and high GDP per capita. Recognising the ongoing global macro challenges to the reflation narrative, while we generally expect GCC sovereign fundamentals to remain robust over the coming years, which in turn will help to drive improving FDI flows into the region, we do anticipate a degree of continuing consolidation in growth rates during these still early stages of rebound from the economic nadir of the pandemic.

And, in this respect, we also note the subliminal risk to the outlook that could stem from any weakening of fiscal discipline if higher oil prices were to result in complacency, especially if it were to coincide with a weakening in the pace of economic growth. While inadvisable, this is a pro-cyclical strategy that one might be sympathetic to at the time and one that we have seen evidence of before, although (the UAE and KSA) governments do seem committed to medium-term fiscal responsibility as they aim to redress the costs and ballooning public debt incurred during the pandemic.

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