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Economics in Brief

Recession in the Gulf spells trouble for many developing and emerging economies

One Pager

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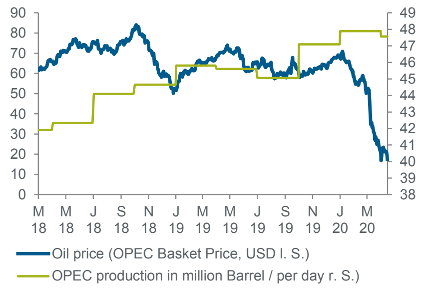
Dual crisis in the Gulf States

The Middle East is currently being hit by a twin crisis: the coronavirus pandemic and collapsing oil prices. The local and global measures implemented to contain the coronavirus pandemic are leading to a recession in the Gulf economies. The other key sectors behind oil – retail, hotels, transport and tourism – have been hit particularly hard. A prominent example is the emirate of Dubai, where tourism, retail and transport play a very large role. The airline Emirates alone contributes around 13% of the city-state's GDP. Global demand for oil is also falling because of the crisis. At the same time, the oil market is sitting on overcapacities (Figure 1).

Figure 1: Oil price is falling and supply is rising

In US-Dollar and millions of barrels per day



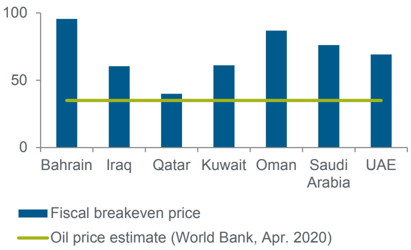
Sources: Macrobond, IMF, own rendition

Despite OPEC +2.0, oil price remains low

Although the OPEC members and Russia agreed on cutting oil output at Easter, this agreement is not very likely to lift the oil price. Global demand for oil has fallen by around 30% as a result of the coronavirus crisis. But the OPEC states and Russia agreed to cut output by only 10%. That is too little to offset the drop in demand, particularly since OPEC production at the beginning of the coronavirus crisis was at an all-time high (Figure 1). Production thus remains excessively high compared with the trend in demand, especially because the global economy will recover more slowly than initially expected. World Bank experts therefore expect the oil price to remain on a low level in 2020. This will exacerbate not just the economic but also the fiscal situation of oil exporting countries. That is because the oil price will remain below the fiscal break-even point, the price level required to fund state expenditures (Figure 2). This, in turn, will have economic consequences because the oil producing countries will have less money to invest.

Figure 2: Oil price is well below the fiscal break-even point

In US dollars per barrel



Sources: IMF, World Bank, own rendition

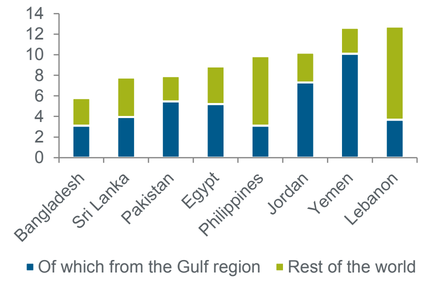
The wealthier Gulf States such as Abu Dhabi, Qatar and Saudi Arabia have launched economic stimulus programmes to prop up the local economy. Bahrain, Dubai and Oman do not have large financial buffers, which leaves them with less room for manoeuvre. During the financial crisis of 2007–2010, the financially strong states of Abu Dhabi and Saudi Arabia provided financial support to their neighbours, thereby contributing to overcoming the crisis. Given the situation described above, it is unclear whether this aid will now be provided as well. The crisis of the Gulf states will not remain confined to the region because the Middle East is globally interconnected through flows of money and capital.

Crisis with global implications

The Gulf region is one of the largest employers for migrant workers, who number around 23 million and come mainly from developing and emerging economies. They send much of their salaries back to their home countries. These remittances are an important source of income and foreign currency for many of their home countries. After the US, the Gulf region accounts for the second-highest share of global remittances. Yemen, Jordan, Egypt and Pakistan are particularly reliant on remittances from the Gulf economies (Figure 3).

Figure 3: Many developing countries rely heavily on Gulf remittances

In percentage of GDP, 2017



Source: World Bank Migration and Remittances Data, own rendition

As a result of the economic crisis in the Gulf, the World Bank expects remittances to decrease by around 20% this year. This will hit many recipient countries hard, leading to a decline in income and foreign currency. This is occurring at a time when the balance of payments of many countries is already under pressure, as exports and investment are also falling. At the same time, imports of food and medicine, for example, are becoming more expensive. The low price of oil thus affects not just the oil producing countries, but many economically weak developing and emerging economies.

Note: This paper contains the opinion of the authors and does not necessarily represent the position of KfW.