# Global Developments and Outlook: Implications for the Middle East and Central Asia Regions

Global growth for 2018–19 is projected to remain steady at its 2017 level of 3.7 percent (see table). However, this projection is 0.2 percentage point lower than the April 2018 *World Economic Outlook*, with the growth outlook marked down for a number of major economies. In the United States, while the outlook for 2018 is unchanged at 2.9 percent, the forecast for 2019 has been revised down due to recently announced trade measures. Growth projections have also been marked down for the euro area and the United Kingdom, following surprises that suppressed activity in early 2018. The outlook for emerging and developing economies is also weaker, reflecting downward revisions for some large emerging market economies due to country-specific factors, tighter financial conditions, geopolitical tensions, and higher oil import bills. For instance, China is projected to experience somewhat weaker growth in 2019 in the aftermath of recently announced trade measures.

**Real GDP Growth, 2017–23**

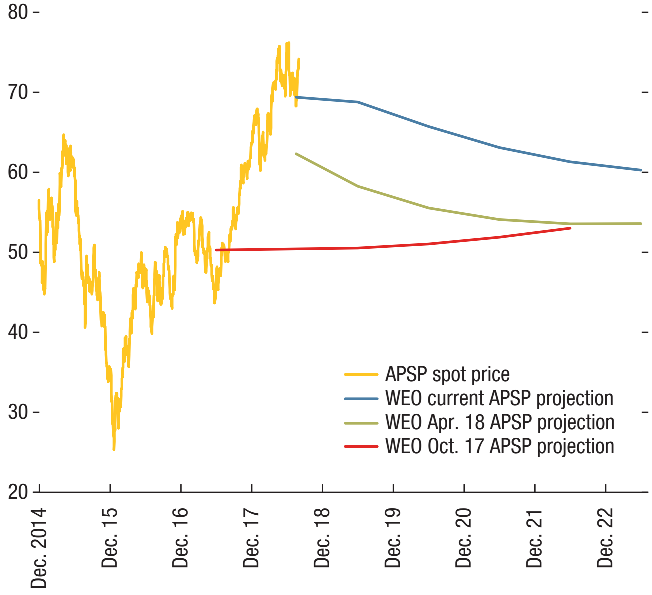
| | 2017 | 2018 | 2019 | 2020–23 |
|---|---|---|---|---|
| **World** | 3.7 | 3.7 | 3.7 | 3.6 |
| Euro Area | 2.4 | 2.0 | 1.9 | 1.5 |
| United States | 2.2 | 2.9 | 2.5 | 1.6 |
| China | 6.9 | 6.6 | 6.2 | 5.9 |
| Russia | 1.5 | 1.7 | 1.8 | 1.5 |
| **MENAP** | 2.2 | 2.4 | 2.7 | 3.0 |
| MENAP oil exporters | 1.2 | 1.4 | 2.0 | 2.3 |
| *of which: non-oil GDP growth* | 2.4 | 2.3 | 2.4 | 3.1 |
| MENAP oil importers | 4.1 | 4.5 | 4.0 | 4.3 |
| **CCA** | 4.1 | 4.0 | 4.0 | 4.2 |
| *CCA oil and gas exporters* | 3.9 | 3.8 | 3.9 | 4.2 |
| *of which: non-oil GDP growth* | 2.9 | 3.8 | 3.8 | 4.1 |
| *CCA oil and gas importers* | 6.0 | 5.0 | 4.8 | 4.6 |

Sources: National authorities; and IMF staff calculations.

The weaker outlook for the euro area could pose challenges for some countries in the Middle East, Afghanistan, North Africa, and Pakistan (MENAP) and the Caucasus and Central Asia (CCA) regions, particularly for oil importers with strong trade ties. The regions may also face headwinds from the projected moderation in activity in China.

**Evolution of Oil Prices**

*(APSP,[1] US dollars a barrel)*



Sources: Haver Analytics; and IMF staff calculations.
Note: APSP = average price of spot prices; WEO = IMF, *World Economic Outlook.*
[1] The average of UK Brent, Dubai Fateh, and West Texas Intermediate crude oil prices.

Oil prices rose above $75 a barrel in June 2018—the highest level since November 2014—reflecting the collapse in Venezuela's production and unexpected outages in Canada and Libya. Prices dropped back to about $70 a barrel following the June 2018 decision by the Organization of the

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See the October 2018 *World Economic Outlook*, *Global Financial Stability Report*, and *Fiscal Monitor* for a more comprehensive discussion of the global outlook.

Petroleum Exporting Countries (OPEC) and other major oil-exporting countries (together OPEC+) to increase production, but prices have increased recently due to geopolitical tensions. While the impact of US sanctions on Iranian exports could further lift prices in the near term, oil prices are expected to decline over the medium term due to increased production by US shale producers and OPEC+ members (see figure). Nevertheless, medium-term futures prices have firmed significantly relative to the baseline in the May 2018 *Regional Economic Outlook: Middle East and Central Asia Update*.

Although still supportive of growth, global financial conditions have started to tighten. Between March and September, the US Federal Reserve has raised the federal funds target rate by 75 basis points and has signaled additional tightening of 100 basis points by the end of 2019. With higher US interest rates, a stronger US dollar, and some episodes of financial market volatility, pressure points have emerged in some emerging market and developing economies. Following a sharp rebound early in 2018, capital flows to these economies have weakened considerably since mid-April, although they stabilized somewhat in July. Policy reactions so far have been varied, including a mix of exchange rate flexibility and interest rate hikes, and intervention in the foreign exchange market.

Market sentiment remains vulnerable to uncertainties stemming from global trade tensions and geopolitical developments, including related to Iran and Turkey. A systemic escalation of trade tensions would further dampen the global recovery and depress medium-term growth (see the “Scenario Box—Global Trade Tensions” in the October 2018 *World Economic Outlook*). Sanctions against Iran will undercut its near-term trade and growth prospects, increasing the risk of spillovers, while developments in Turkey could impact the region through trade and financial linkages, as well as through market confidence effects (see Box 1). A worsening of these developments, or faster-than-anticipated monetary policy tightening in advanced economies, increases the risk of a sudden reversal in global risk appetite. The MENAP and CCA regions would be vulnerable in this environment, especially those countries that rely heavily on international capital to meet external financing needs.

In this context, policy uncertainty has increased and near-term risks to global growth have shifted to the downside. Tightening global financial conditions and softening growth in large economies limit prospects for upside surprises, while risks highlighted in the April 2018 *World Economic Outlook* have become more pronounced or have partially materialized. Medium-term risks remain skewed to the downside, reflecting the continued buildup of financial vulnerabilities and the possibility of shifts to unsustainable policies in the face of weaker growth prospects. The materialization of these risks would have significant implications for countries in the MENAP and CCA regions through their impact on external demand, remittances, capital flows, commodity prices, and financing conditions.

## Box 1. Global Financial Market and Trade Pressures and Transmission to MENAP and CCA Countries

As in other regions in the world, countries in the Middle East, North Africa, Afghanistan, and Pakistan (MENAP) and Caucasus and Central Asia (CCA) regions are exposed to tightening in global financing conditions and ongoing global trade tensions. The former has already begun to impact several emerging market economies in MENAP and could have more severe implications should financial market sentiment suddenly deteriorate. Escalating global trade tensions will have a limited direct and immediate impact on these regions but could impart significant strains over time through negative effects on trading partners and through market confidence effects.

### Exposure to Emerging Market Contagion

Countries in the MENAP and CCA regions are exposed to potential contagion from current financial market pressures in emerging markets. Following recent developments in Argentina, Turkey, and other emerging markets, sovereign spreads of MENAP oil-importing countries have moved broadly in line with other emerging markets, rising by about 100 basis points between April and August. This illustrates the region's exposure to financial market volatility and raises new challenges, particularly for countries in need of international borrowing.

Moreover, there could be additional spillovers from Turkey to the MENAP and CCA regions through banking sector linkages and trade channels. MENAP-owned banks represent 7 percent of Turkish banking assets (as of March 2018), with shareholder equity of US$5.3 billion—of which the largest share represents Qatari interests, followed by those of Lebanon, Kuwait, and Libya. This has contributed to declines in these countries' equity indices in recent months. Nevertheless, as direct banking exposures represent less than 1 percent of these countries' GDP on average, the risk of broad-based financial stress is relatively small.

On the trade side, while Azerbaijan would be most affected by reduced demand for exports from Turkey, the impact of the depreciation of the Turkish lira on the region is more uncertain. Given the proportion of imports from Turkey, a sustained 20 percent depreciation of the Turkish lira (as occurred between July and September) would suggest that the current account deficits of Djibouti, Iraq, the Kyrgyz Republic, and Libya could narrow by about 1 percent of GDP (assuming no change in import volumes). However, Turkish products will become more competitive, which could trigger a combination of an increase in Turkish imports to the region and a reduction in the region's exports to markets where they compete with Turkish exports. This makes the overall impact more indeterminate.

### Escalating Trade Tensions

The October 2018 *World Economic Outlook* analyzes the potential impact on global growth of five scenarios related to an escalation of trade tensions. The combined impact of these scenarios indicates that the level of global GDP could fall by more than 0.75 percent in the short term and remain about 0.4 percent lower in the long term, with the impact on China, the United States, and emerging markets relatively more pronounced.

Overall, the direct impact of the trade measures recently imposed and those trade measures that have been announced or considered, but not yet imposed, on countries in the MENAP and CCA regions is likely to be small. For example, Bahrain's exports of aluminum to the United States constitute less than 5 percent of its total exports, and there remains the prospect of an exemption from the tariffs. Similarly, while exports of cars and car parts are significant for Georgia (9 percent of total exports) and Morocco (14 percent of total exports), most are destined for other CCA or euro area countries (about 50 and 45 percent, respectively). However, there could be an indirect impact of potential product tariffs on MENAP and CCA countries through their impact on demand from more directly affected trading partners—for instance, through countries' participations in global value chains (see the October 2017 *Regional Economic Outlook: Middle East and*

**Box 1** *(continued)*

*Central Asia*).

More importantly, there could be a significant impact on growth in key trading partners and on global growth more generally. If this is translated into lower demand for exports from MENAP and CCA countries, it would slow economic activity and add to external pressures. Specifically, a slowdown in demand from China and the euro area would be of concern for Mauritania (minerals, fish) and Tunisia (cars, electronics, food, textiles), where the current account deficits are already wide (Table 1). Oil exporters would be exposed to a slowdown in economic activity in China, the euro area, and the United States, given the concentration of their oil exports to these countries, as well as the impact of lower oil prices triggered by a slowdown in global growth. And all countries would be hit, especially those with large financing needs, if investor confidence was affected or financing conditions tightened sharply (see the October 2018 *Global Financial Stability Report*).

### Table 1. MENAP and CCA Export Intensity by Recipient 2016

*(Exports of goods, percent of GDP)*

**MENAP Oil Exporters**

| | Algeria | Bahrain | Iran | Iraq | Kuwait | Oman | Qatar | Saudi Arabia | United Arab Emirates |
|---|---|---|---|---|---|---|---|---|---|
| China | 0 | 2 | 6 | 6 | 6 | 19 | 3 | 4 | 5 |
| Euro Area | 10 | 1 | 2 | 6 | 0 | 1 | 2 | 1 | 2 |
| Turkey | 1 | 0 | 2 | 0 | 0 | 0 | 0 | 0 | 1 |
| United States | 2 | 4 | 0 | 4 | 3 | 1 | 0 | 3 | 1 |
| Combined | 13 | 7 | 11 | 17 | 10 | 21 | 6 | 8 | 9 |

**MENAP Oil Importers**

| | Afghanistan | Djibouti* | Egypt | Jordan | Lebanon | Mauritania | Morocco | Pakistan | Somalia* | Sudan* | Tunisia |
|---|---|---|---|---|---|---|---|---|---|---|---|
| China | 0 | 0 | 0 | 0 | 0 | 11 | 0 | 1 | 0 | 1 | 0 |
| Euro Area | 0 | 1 | 1 | 1 | 1 | 6 | 11 | 2 | 0 | 0 | 22 |
| Turkey | 0 | 0 | 0 | 0 | 0 | 0 | 1 | 0 | 0 | 0 | 0 |
| United States | 0 | 2 | 0 | 4 | 0 | 0 | 1 | 1 | 0 | 0 | 1 |
| Combined | 0 | 3 | 2 | 6 | 1 | 17 | 12 | 4 | 0 | 1 | 24 |

**CCA**

| | Armenia | Azerbaijan | Georgia | Kazakhstan | Kyrgyz Republic | Tajikistan* | Uzbekistan* | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| China | 1 | 1 | 2 | 3 | 1 | 0 | 3 | | 🟥 | >20 |
| Euro Area | 3 | 13 | 3 | 12 | 1 | 1 | 0 | | 🟥 | 10–20 |
| Turkey | 0 | 4 | 2 | 1 | 1 | 2 | 1 | | 🟧 | 5–10 |
| United States | 0 | 0 | 1 | 0 | 0 | 0 | 0 | | 🟨 | 3–5 |
| Combined | 4 | 19 | 7 | 17 | 3 | 3 | 5 | | | 0–3 |

Source: UN COMTRADE.
Note: CCA = Caucasus and Central Asia; MENAP = Middle East, North Africa, Afghanistan, and Pakistan.
*Using mirror data.