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Coronavirus, Oil and the Middle East

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As a result of the Covid-19 pandemic, the world is now experiencing the worst recession since that of 1929. It has developed with terrible speed, causing by May 21, the death of 330,000 people, with 5.1 million infected.[1]

Hundreds of millions, if not billions, of people have been put out of work and the result is a massive loss of output and a collapse in the demand for goods and services. There is great uncertainty regarding the development of therapeutics and prevention; health services face massive pressure and many countries have abandoned orthodox economic policies to support households, firms, and financial markets. Conventional economic theory has once again been put to the test and found wanting.[2] International economic cooperation is partial, at best. There is a widespread feeling that profound political and economic change will occur, but no one knows where it will lead.[3]

Covid-19 has widened economic gaps, reinforced authoritarian trends and nationalist tendencies. It has also revealed the differences between well-managed and badly-managed countries and regions.[4] In April 2020, the IMF summarized the economic situation as follows. Assuming that the pandemic and containment peaks in the second quarter of this year, for most countries in the world, and recedes in the second half, the global economy in 2020 would shrink by three percent. This was a reduction of 6.3 percent from the forecast made January 2020, a major revision over a very short period. In May, however, the Fund increased its estimate of the losses and suggested that world output will fall much more.[5]

The Middle East has been hit by two large overlapping shocks: COVID-19 and the collapse in oil prices. The COVID-19 epidemic has been reported throughout the region. Turkey had, by May 21, the ninth largest number of cases in the world with 152,587 and 4,222 deaths. Iran had the tenth, at 126,944 with 7,057 deaths. Saudi Arabia, Qatar, the UAE, Kuwait, Bahrain and Oman had a total of 157,328 cases and had reported 1,051 deaths. Egypt reported 14,229 cases and 680 deaths.[6] All these figures should be treated with caution as under reporting is considered widespread.

These developments have caused significant turmoil as a result of simultaneous shocks to supply and demand. The OPEC basket price fell from $67.12/barrel on January 1, 2020 to a low of $12.41 on April 28, and reached $24.93 on May 14.[7] In May, the US Energy Administration forecast that oil prices will average $34/barrel in 2020, down from an average of $64/barrel in 2019. (This forecast is for Brent and the OPEC basket is usually about $1/barrel less).[8] The outbreak of COVID-19 has had a massive impact on the crude oil market, as two-thirds of oil is used for transport. All crude oil benchmarks have seen sharp falls, with some briefly dropping to negative levels. World demand for crude is expected to decline by 9.9 million barrels a day in 2020, or 10 percent, over twice the size of any previous fall.[9]

COVID-19 has resulted in a massive disruption of world trade and has caused widespread losses, affecting job-rich sectors and businesses. The measures taken in major economies have significantly reduced demand. The resulting global slowdown has impacted global value chains in the region, as well as job-rich retail and manufacturing sectors, and small and medium enterprises in the informal sector. At the same time, restrictive containment measures introduced by governments in the region and fear of contagion have reduced consumer demand, particularly in tourism, hospitality, and retailing. Meanwhile, global financial conditions have tightened sharply, adding to the region's challenges.

Countries have been swift in their responses to the crisis. They have taken measures to protect lives, contain the spread of the virus, and support hard-hit sectors. While health spending was increased in all countries to support emergency needs and to enhance health care infrastructures, health-related responses varied depending on the state of preparedness and current levels of spending.

Many countries in the region have announced fiscal support packages, including revenue and expenditure measures, equal to an average of 3.8 percent of GDP. Liquidity support measures have been announced by central banks in seven countries, with an average of 3.4 percent of GDP. Monetary policy has been eased across the region, with the exchange rate used as a buffer where appropriate. Saudi Arabia is an important example**.** Having only first introduced a Value Added Tax two years ago, the government announced that the rate will be tripled to 15 percent from July 1, and that it will end a 1000 Saudi Riyals ($267) monthly living allowance for Saudi citizens from June 1.[10]

Saudi Arabia also announced a $13 billion package to support businesses and small and medium enterprises. The United Arab Emirates has issued a $27 billion stimulus plan to help boost the economy, including subsidies to water and electricity for citizens, as well as commercial and industrial activities. Qatar announced a similar package of $23 billion to support and provide financial and economic incentives to the private sector. Egypt unveiled a comprehensive plan costing $6 billion to combat the fast-spreading virus and support economic growth.[11]

In April, the chief economist of the IMF said that in 2020 economies in the Middle East would contract by an average of 3.1 percent. Most countries have revised growth down by more than 4 percentage points in one year, equivalent to a loss of $425 billion. For nearly all countries, these revisions are steeper than those seen during the global financial crisis in 2008 and the oil price shock of 2015. In April, the World Bank estimated the loss at 3.7 percent, based on an average oil price of $30/barrel in 2020.[12] Table 1 shows how the World Bank has changed its forecasts for economic growth in the Middle East.

Table 1: GDP growth estimates for 2020 (annual, percent)

Forecast made in:	October 2019	March 2020	April 2020	Difference between October and March
MENA	2.6	-2.1	-3.7	-6.3
GCC	2.2	-1.4	-2.6	-4.8
Saudi Arabia	1.6	-0.8	-1.4	-3.0
Iran	0.1	-1.9	-3.8	-3.9
Iraq	5.1	-9.0	-10.1	-15.2
Egypt	5.8	-0.3	-2.1	-7.9
Jordan	2.3	-0.4	-5.8	-8.1
Lebanon	0.3	-8.1	-11.2	-11.5
Tunisia	2.2	-1.4	-6.2	-8.4
WB and Gaza	-1.1	0	-1.4	- 2.5

Source: World Bank

Fragile and conflict-affected states have been affected particularly hard. These include oil producers such as Iraq and Algeria and oil importers such as Jordan and Tunisia. Yemen faces catastrophic conditions despite the reduction in fighting and in Syria the government is manipulating the flow of medical supplies for its own ends. The crisis in Lebanon, the origins of which preceded the outbreak of Corvid-19, has deepened. The economic downturn has exacerbated the already large humanitarian and refugee challenges facing these countries, especially given their weak health infrastructures and living conditions that may be conducive to a rapid spread of the pandemic.

According to the UN Economic and Social Commission for West Asia, the Arab region may lose 1.7 million jobs in 2020, thus increasing the unemployment rate by 1.2 percent. This is based on much lower falls in income than those cited here. The COVID-19 pandemic is severely damaging employment across all sectors because of social distancing policies, especially the services sector. Given that the service sector is the main employer in the Arab region, the adverse impact on its activities will result in significant job losses. The Arab region may witness further shrinking of the middle-income class, pushing 8.3 million people into poverty. The consequences of this crisis could be particularly severe for vulnerable groups, especially women and young adults, and those working in the informal sector who have no access to social protection and unemployment insurance. The challenge is further compounded by a lack of social protection floors in some Arab countries. Increased poverty could lead to an additional 1.9 million people becoming under nourished.[13]

The significance of oil income in the region is shown in Table 2. It shows that oil was far more important to the economies of Arab countries and Iran than to the world economy. This source of income was the result of the presence of natural resources rather than human production and is therefore called rent. The drilling, transport and refining of oil as well as gas employs only about one million people in the region. All the income earned goes to the government, if not the ruler himself. The government then reallocates it through the budget.

Oil-exporting countries have been hit by lower global demand and lower oil prices, with oil exports expected to decline by more than $250 billion. In 2019, Middle East oil revenues were estimated at about $600 billion and so this represents a fall of over 40 percent.[14]As a result, fiscal balances are expected to turn negative, exceeding 10 percent of GDP in most countries. Oil-importing economies would be adversely affected by a large decline in remittances and investment and capital flows from oil-exporting countries. The large deterioration in their fiscal deficit—due to the impact of lower growth on tax revenues and scaled-up spending—is expected to raise public debt to almost 95 percent of GDP.

Large forthcoming maturing debt presents financing risks in current market conditions. High public debt levels may limit the fiscal space available to undertake additional measures.[15]

Table 2: Oil income as share of GDP (%)

	2011	2012	2013	2014	2015	2016	2017
World	2.83	2.72	2.48	2.16	0.97	0.81	1.11
Arab states	33.85	32.98	30.11	26.76	15.34	12.85	16.42
Algeria	27.31	26.17	23.82	20.36	12.85	11.44	15.34
Egypt	9.76	8.38	7.78	6.75	2.96	2.26	4.08
Iran	24.7	20.20	22.89	22.36	12.81	11.44	15.34
Iraq	50.77	48.44	45.32	45.33	34.90	31.16	37.78
Kuwait	61.23	61.07	57.45	54.26	37.10	31.64	37.78
Saudi Arabia	49.23	47.23	44.19	40.01	23.29	19.43	23.10
UAE	28.78	28.50	25.78	23.05	13.13	10.83	13.13

Source: World Bank Data

In 2018, remittances accounted for 0.8 percent of world GDP while in the Middle East and North Africa, excluding the high income (oil-rich) states, the share was 5.7 percent. The significance of remittances in some the economies of the region is shown in Table 3.[16]

Table 3: Remittances and the economy

	2019 $ billions	2019 share of GDP%	2019 Growth %	2020 Growth %
Egypt	26.79	8.9	5	-21.5
Jordan	4.51	10.2	1	-22
Lebanon	7.47	12.7	7	-17
WB and Gaza	2.38	16.3		
Tunisia	1.90	4.9		-17 to -18

Source: World Bank data

2019=estimate

2020=forecast

Remittances are earned outside the economy in which they are received, and they are also considered a source of rental income. The two main sources of rental income, fossil fuels and remittances, play vital roles in the rich and poor economies of the region. Their collapse will put huge pressure on the Arab socio-economic system and may, in the longrun threaten political stability. The large tourist sectors in Lebanon, Egypt, Jordan, Morocco and Tunisia have been affected by the suspension of international flights and cruises.

Arab countries are, according to a UN report, dominantly rentier states with weak governance and institutional frameworks, crony capitalism, limited freedom, and low levels of political participation. This system of rule has deepened economic, social and political inequalities and reinforced arrangements that favor the interests of those with more influence creating and reinforcing an inequality trap. Natural resource endowments have shaped Arab economies for decades, especially in the resource-rich net oil-exporters where high per capita rents, in the form of government provision of subsidies, low tax rates and large-scale public-sector employment, have been a central part of development policy.

Natural resource riches have also influenced Arab oil-poor and non-oil exporting economies through capital flows from the resource-rich countries, especially investment, remittances and tourism inflows. These rents and their spillover effects have thus played the main role in promoting social and economic development over the past four decades across most Arab countries. They have also reinforced authoritarianism and, in some cases political instability and conflict.[17]

The medium-term outlook for oil prices is far from clear because of uncertainties about demand as well as those about the financing of supply. Covid-19 is increasingly being viewed as a part of humankind's neglect of the natural environment. The suspension of economic activity has in many countries literally cleared the skies and this poses the question of what will change, especially in oil-intensive transport systems. The consequences of changes in energy-use will be crucial for Middle East (and other) oil suppliers and thus for the political economy of the whole region.

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