

Distr.
LIMITED
E/ESCWA/EDGD/2009/Technical Paper.4
7 December 2009
ORIGINAL: ENGLISH

ECONOMIC AND SOCIAL COMMISSION FOR WESTERN ASIA (ESCWA)

REGIONAL ECONOMIC FORECAST
(November 2009)

The designations employed and the presentation of the material in this publication do not imply the expression of any opinion whatsoever on the part of the Secretariat of the United Nations concerning the legal status of any country, territory, city or area or of its authorities, or concerning the delimitation of its frontiers or boundaries.

Mention of commercial names and products does not imply the endorsement of the United Nations.

The opinions expressed in this technical paper are those of the authors and do not necessarily reflect the views of the United Nations Secretariat.

This document has been reproduced without formal editing.

09-0525

CONTENTS

<i>Chapter</i>	<i>Page</i>
I. GLOBAL CONTEXT	1
II. REGIONAL OUTLOOK FOR THE ESCWA REGION 2009-2010	1
A. General overview	1
B. Gulf Cooperation Council economies	5
C. More diversified economies	6
III. CONCLUDING REMARKS	9

LIST OF TABLES

1. Real GDP growth rate and consumer inflation rate, 2006-2010	2
2. Crude oil price estimation and forecast	3

LIST OF FIGURES

I. GDP and oil price forecast for 2010	3
II. Interest rate developments of selected ESCWA countries	4

I. GLOBAL CONTEXT

After the sharp and abrupt downturn of economic activities observed since the third quarter of 2008, the world economy started to show a sign of improvement in the second quarter of 2009. The phase of credit crisis of the global financial crisis was promptly stabilized by the second quarter of 2009 by which the US dollar money markets and the world stock market have shown a sign of recovery. Rapid inventory adjustments and other cost control measures at the corporate level of the world economy contributed to the recovery in terms of growth rate. Active fiscal and monetary measures that were taken by major economies have also contributed to sustain the global demand. Moreover, and most notably, the resilient positive economic growth in developing countries, particularly in China and India, sustained the world demand level from collapsing further. The global imbalance that was represented particularly by a significantly high level of current account deficits of the United States started to narrow.

The world economy can be discerned to be on a recovery path. This recovery is happening slowly, however, and the world economy is still fragile. Despite active fiscal measures, the United States, the European Union and Japan fell into a state of deflation. The declining price level could be beneficial as it may contribute to improving income in real terms. However, the declining price level indicates a weak state of domestic demand, despite active expansionary fiscal and monetary measures taken in those countries. Moreover, the decline in the general price level represents a decline in the nominal wage level. The consistently rising unemployment rates in the major developed countries indicate the absence of negotiation on the side of labour. The prompt cost adjustment measures, which include substantial layoffs, could indeed contribute to an improvement in the growth rate, but this type of recovery can only be achieved at the cost of a high unemployment rate. Furthermore, the declining general price level may increase the debt burden in real terms for commercial banks, business entities and households.

The resilience of developing countries, including the member countries of the Economic and Social Commission for Western Asia (ESCWA), becomes apparent through the prompt policy responses of policymakers to the initial phase of the global financial crisis. However, several risk factors remain due to the fragile condition of the present recovery of the world economy, which is dependent on: (i) a smooth balance sheet adjustment of major economic actors; (ii) a recovery of asset prices, particularly of real estate; and (iii) a significant reduction of unemployment that is most crucial to stabilize the world demand growth.

II. REGIONAL OUTLOOK FOR THE ESCWA REGION 2009-2010

A. GENERAL OVERVIEW

As the world economy indicated a recovery from recession throughout the second and third quarters of 2009, the economic sentiment of the ESCWA region has improved from pessimism to cautious optimism. In the region where the major crude oil exporters are located, the strong recovery of crude oil prices, at around US\$65 to 70 per barrel in the second and third quarters of this year, contributed to an optimistic projection. Moreover, several worst-case scenarios have not happened at the present phase of the global financial crisis. A balance-of-payment crisis and associated currency devaluation did not materialize even in the countries where the current account positions were weak. The once feared reverse mass migration of expatriate workers from the member countries of the Gulf Cooperation Council (GCC)¹ did not take place.

¹ The ESCWA region consists of two sub-regional groupings: (a) GCC countries stands for the Council's member countries, namely, Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates; and (b) the more diversified economies (MDEs) for the rest of the ESCWA members, namely, Egypt, Iraq, Jordan, Lebanon, Palestine, the Sudan, the Syrian Arab Republic and Yemen.

The monetary authorities in the region successfully defended the respective banking sector from the global financial crisis of the fourth quarter of 2008. The fiscal authorities in the region successfully took an active stance to cushion the impact from the global recession. The region's strategic geographical location has been re-approved in the efficiency drive of international investors and traders. The average real gross domestic product (GDP) growth for 2009 for the region is estimated to be at 1.4 per cent, compared to 5.8 per cent in 2008. The forecast for 2010 is at 4.3 per cent (table 1). The recovery of both external as well as domestic demand with the support of active fiscal measures is expected to lead the recovery. The average crude oil price in the Reference Basket of the Organization of the Petroleum Exporting Countries (OPEC) is forecasted for 2010 between US\$45.6 and US\$83.2 per barrel, with a median forecast of US\$63.7 per barrel (table 2). Against the median forecast, the oil export revenue in the region is forecasted to recover with a positive growth of 9.6 per cent in 2010, after having contracted by 38.0 per cent in 2009.

TABLE 1. REAL GDP GROWTH RATE AND CONSUMER INFLATION RATE, 2006-2010
(Annual percentage change)

Country/Area	Real GDP growth rate					Consumer inflation rate				
	2006	2007	2008 ^{a/}	2009 ^{b/}	2010 ^{c/}	2006	2007	2008	2009 ^{b/}	2010 ^{c/}
Bahrain	6.7	8.4	6.3	2.8	3.6	2.1	3.3	3.5	2.5	3.6
Kuwait	5.2	4.4	6.3	-1.2	4.1	3.0	5.5	10.6	3.5	4.7
Oman	6.0	7.7	7.8	2.4	3.5	3.4	5.9	12.4	4.5	3.2
Qatar	12.2	9.5	16.4	8.9	12.5	11.8	13.8	15.0	-1.4	4.1
Saudi Arabia	3.1	3.3	4.4	-0.8	3.1	2.2	4.1	9.9	4.5	4.0
United Arab Emirates	9.4	5.2	7.4	-1.5	3.8	9.3	11.1	12.3	1.5	4.2
GCC countries ^{d/}	5.3	4.5	6.1	-0.2	3.9	4.3	6.3	10.7	3.4	4.1
Egypt ^{e/}	7.1	7.2	4.7	4.5	5.5	7.6	9.5	17.1	10.5	11.0
Iraq	6.2	5.0	7.5	5.2	6.1	53.2	30.8	2.8	3.5	6.1
Jordan	8.0	8.9	7.9	2.8	3.0	6.3	4.7	13.9	1.7	4.5
Lebanon	0.0	7.5	6.2	4.8	3.1	1.5	6.7	10.0	1.5	3.9
Palestine	-8.3	0.6	-1.7	-1.0	0.5	3.8	2.7	9.8	1.5	3.0
The Sudan	10.0	10.2	6.0	4.5	5.0	7.2	8.1	14.9	9.5	9.0
Syrian Arab Republic	5.2	6.3	4.8	2.5	3.5	10.0	4.5	15.2	3.7	5.0
Yemen	3.8	4.4	4.7	2.0	4.8	10.8	7.9	19.0	4.2	11.5
MDEs ^{d/}	5.9	6.8	5.3	4.1	4.9	14.2	11.5	13.8	7.1	8.5
Total ESCWA region ^{d/}	5.5	5.3	5.8	1.4	4.3	7.9	8.2	11.9	4.8	5.7

Source: National sources unless stated otherwise.

a/ The estimated figures for Kuwait, Oman, Qatar, Iraq, Lebanon, Palestine and Syrian Arab Republic as of 31 October 2009.

b/ October 2009 estimations.

c/ October 2009 forecasts.

d/ Figures for country groups are weighted averages, where weights for each year are based on GDP in 2000 constant prices.

e/ For the GDP growth rate of Egypt, the figures are for the country's fiscal year which starts in July of the year and ends in June of the following year.

However, downside risks remain. The crude oil price level is discerned to be fragile as it has been mainly supported by the significant reduction of the OPEC production quota and the compliance of its member countries. Moreover, despite the establishment of a firm price range around US\$70 per barrel of crude oil since the second quarter of 2009, the demand for such fuel products as gasoline, naphtha and heating oil remained weak. A prolonged low refining margin may affect the price of crude oil in 2010. Commercial banks in the region have weathered the global liquidity crisis, but the issue has been shifted to the problem of liquidity at business entities and households for which a sufficient level of liquidity may not be transferred. A low level of liquidity circulation can depress the level of asset price that may force commercial banks into another series of balance sheet adjustments. In fact, the property prices in the region

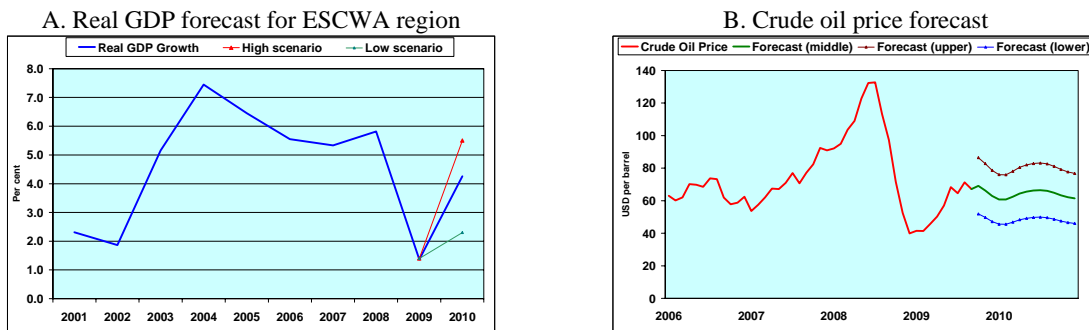
are still weak and fragile, and a strong recovery in 2010 is not assured albeit forecasts of the region's economic recovery.

TABLE 2. CRUDE OIL PRICE ESTIMATION AND FORECAST
(OPEC Reference Basket: US dollars per barrel)

	Minimum	Maximum	Annual average	Forecasted annual average for 2010		
				Lower	Median	Higher
2008	33.36	140.73	94.45			
2009	38.14	78.0	60.50			
2010				45.6	63.7	83.2

Source: OPEC for 2008. Figures for 2009 and 2010 are forecasts as of the end of October 2009.

Figure I. GDP and oil price forecast for 2010



Meanwhile, the consumer price inflation was peaked out in the second half of 2008. As a general trend, the rate of consumer inflation has declined since, and rapidly in several countries. It has not been shown in official statistics, but policymakers in several countries also mentioned a possibility of deflation in 2009 and 2010. The rapid decline in the consumer inflation rate has been led by the price of food and property rentals, which were the factors that led a historically high consumer inflation rate in 2008. The anticipated second-round effect of the inflation pressure of 2007-2008 did not materialize. The upward wage adjustments, particularly in the public sector in 2007-2008, did not influence general price levels to the extent expected. Traditionally, the region had experienced a low-inflation regime and the present trend may point to the convergence into the historical trend. The consumer inflation rate, on average, is estimated at 4.8 percent for 2009, compared to 11.9 per cent in 2008. The forecast for 2010 is at 5.7 per cent (see table 1).

The current account balance of the countries in ESCWA region is deteriorating, even though it has not been a threat to respective growth performance at the end of the third quarter of 2009. In the GCC member countries, the moderate growth in domestic demand pinned the import level from declining while the decline in crude oil prices from the level of 2008 caused a substantial decrease in the export level. The weak global asset markets contributed to a weak income account surplus in spite of highlighted activities of sovereign wealth funds. The current account surplus of the GCC member countries is estimated to decline sharply in 2009. In the two non-oil-exporting countries in the region, namely Jordan and Lebanon, the current account position is estimated to deteriorate further. However, the deterioration of current account positions was supported by the strong capital account positions well into 2009.

The exchange rates of the ESCWA countries stayed stable as of the end of the third quarter of 2009. A sign of fragility has been observed in Yemen, whose national currency was depreciated against the US dollar at 2.5 percent since the start of the year. Despite the decision at the 29th GCC Summit in December 2008, the target to create a GCC currency union by January 2010 has been challenged from the outset as the United Arab Emirates opted not to participate in the currency union from its inception. Oman had already made the

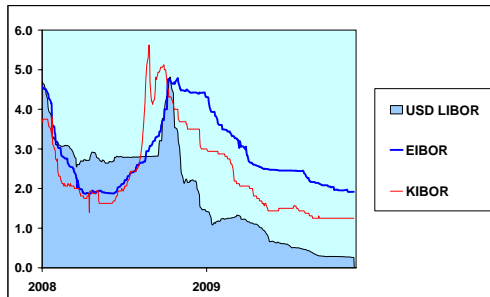
same decision in 2006. Policymakers in the GCC have indicated a phased introduction of the currency union, considering the balance between technical feasibility and the potential economic merit of the creation of the currency union that was highlighted in the course of the global financial crisis.

Extreme troubles with the balance of payments are likely to be averted in most ESCWA countries in 2010, albeit a potential vulnerability remaining for those countries with a weak current account position. For Egypt, Jordan, and Lebanon, the high level of foreign reserves will help offset a contingency of external shock. For the Sudan and the Syrian Arab Republic, an orderly restriction on foreign currency transaction will keep the stability. Yemen's current account position will be improved through the export of liquefied natural gas (LNG) that initiated its shipping in November 2009.

A series of reduction in policy interest rates has been observed in the region since October 2008 (see figure II.B) together with the reduction in the reserve requirements of commercial banks and the provision of extra liquidity facilities. The funding liquidity stayed relatively tight in Kuwait and the United Arab Emirates as their interbank money market rates hovered above the US dollar LIBOR² since August 2008 (figure II.A). Historically, the rates had been at the same level as the US dollar LIBOR. Nevertheless, the banking sector in the region successfully weathered the funding liquidity crisis by the third quarter of 2009, and attention of monetary authorities was shifted from the issue of funding liquidity to the issue of balance sheet adjustments of commercial banks and businesses. The support of balance sheet adjustments of commercial banks has been continued, mostly notably through the rapid responses in GCC countries.

Figure II. Interest rate developments of selected ESCWA countries

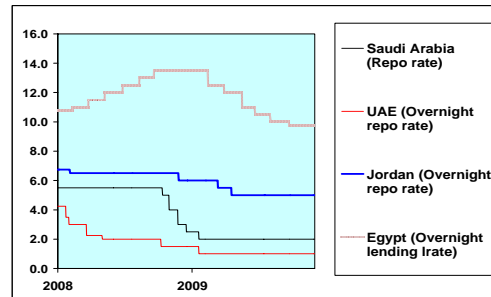
A. Three-month money market rates of Kuwait, the United Arab Emirates and US dollar LIBOR 2008-2009



Sources: Central Bank of Kuwait, NBD Emirates, British Bankers Association.

Notes: Emirates interbank offered rate (EIBOR).
Kuwaiti interbank offered rate (KIBOR).

B. Policy interest rates of selected ESCWA member countries 2008-2009



Sources: Central banks of Egypt and the United Arab Emirates and Saudi Arabian Monetary Agency.

Fiscal response to the global financial crisis varied among countries. For the fiscal year covering 2009, an expansionary fiscal stance has been sought particularly by GCC countries, backed by the sizeable fiscal surpluses accumulated since 2002. In the latest GCC countries' budget formation, infrastructure investment, health and education, and social provisions were emphasized. Fiscal stances have been more cautious in the non-oil-exporting countries in the region, namely Jordan and Lebanon, which faced weak revenue prospects and public debt constraints. Despite the importance of fiscal stimulus as the key to safeguard economic growth from the aftermath of the financial crisis, the countries in the ESCWA region are facing: (i) a voluntary fiscal constraint of the culture of fiscal prudence (mostly in GCC countries); and (ii) an actual fiscal constraint in need of additional international support for their contribution to the fiscal stimulus at global level (MDEs).

² London Interbank Offered Rate (LIBOR).

B. GULF COOPERATION COUNCIL ECONOMIES

In the GCC member countries, despite the weak performance of stock markets and the real estate sector, the delay in private sector projects, and the rapid decline in commercial and residential rental prices, a considerable portion of economic actors and policymakers in the subregion still regarded economic fundamentals as sound. This optimism is a crucial drive for forward-looking behaviour of consumption and investment. For 2009, GCC countries are estimated to mark a contraction of 0.2 per cent in real GDP on average. This weak estimation is mainly due to the prompt compliance to the significant cut in the production quota of OPEC member countries in the subregion, namely Kuwait, Qatar, Saudi Arabia and the United Arab Emirates. Due to the readiness of fiscal authorities to provide fiscal support, domestic demand in the subregion is not estimated to shrink in parallel with the GDP estimates. It is the component of significant reduction in net exports that caused the real GDP estimation. Non-OPEC member countries in the subregion are estimated to show a more modest decline in growth performances in 2009. Resilient business and consumer confidence has been observed in the GCC economies despite pockets of weakness in certain sectors of the economy, particularly the real estate sector. The prospects for 2010 depend on: (i) a recovery of external demand and crude oil prices; (ii) a continuous active fiscal stance; and (iii) a smooth balance sheet adjustment of economic actors, particularly commercial banks, business entities and households. The forecast of real GDP growth of GCC economies for 2010 is at 3.9 per cent.

Qatar marked an exceptional position with its estimated GDP growth of 8.9 per cent in 2009. Continuous investment activities in its energy sector and urban infrastructure sustained a high GDP growth level. Moreover, its position as the world largest LNG exporter contributed to maintaining its margin in net exports. The growth for 2010 is forecasted at 12.5 per cent, counting on continuing active investment activities, strong net exports and active support for the balance sheet adjustments of commercial banks. A rapid fall in the general price level is observed, where consumer inflation rate is estimated at -1.4 per cent in 2009, compared to 15.0 per cent in 2008. This fall in the price level has been led by food and rental price. A recovery in domestic demand is forecasted to raise the inflation rate in 2010, with the forecast at 4.1 per cent.

Kuwait, Saudi Arabia and the United Arab Emirates are estimated to experience a contraction in GDP growth in 2009. However, as it is noted, the contraction has not been caused by the weak domestic demand but by the reduction in their oil production under the OPEC production quota. Kuwait is estimated to mark a contraction of GDP growth at 1.2 per cent in 2009. In addition to the reduction of the crude oil production level, the weak refinery margin for fuel products and the declined profit level of the financial sector contributed to the growth performance. The effect of the fiscal measure taken in April 2009 is expected to show by the fourth quarter of 2009 and into 2010. A resumption of active investment in the energy sector and the sustained domestic demand growth is forecasted for 2010 with a 4.1 per cent growth in real GDP rate. Kuwait has also experienced a rapid fall in the general price level, but not to the extent of Qatar. The consumer inflation rate is estimated at 3.5 per cent in 2009, compared to 10.6 per cent in 2008. The inflation rate in 2010 is forecasted at 4.7 per cent based on the recovery of the domestic economy.

The real GDP growth of Saudi Arabia is also estimated to contract by 0.8 per cent in 2009, which is mainly due to the reduction of the crude oil production level for the OPEC production quota. However, stable domestic demand growth has been observed. An exceptionally strong fiscal commitment by the Government sustained the domestic demand. It has also been observed that the real estate sector of the country was resilient due to a consistent demand growth. Saudi Arabia is one of few economies in the region that has not experienced a decline in residential rental prices during 2009. Moreover, the financial sector remained relatively active on the recent liberalization of the markets to foreign investors. The economy is forecasted to recover with a growth of 3.1 per cent in 2010. Saudi Arabia also experienced a decline in the general price level in 2009. Consumer inflation rate is estimated at 4.5 per cent in 2009, compared to 9.9 per cent in 2008. This decline was in line with the international and regional trend of commodity prices. A further decline of the price level is forecasted for 2010 with a consumer inflation rate of 4.0 per cent as the economy is returning to its historical trend.

The United Arab Emirates is estimated to record a contraction of real GDP at a rate of 1.5 per cent in 2009. The decline in net exports attributed to the reduction of the crude oil production level for the OPEC production quota. The active fiscal measures were implemented for 2009 and were announced for 2010. The fiscal support for domestic demand was particularly felt in Abu Dhabi, where the accumulated wealth of the fiscal authority was readily available. Its high exposure to international economic trends led Dubai into an abrupt slowdown in the financial and real estate sectors, with a sharp reduction observed in the construction activity. However, an efficiency drive of international trade activities retained Dubai's strategic regional advantage. In general, business sentiment and consumer confidence have been resilient in 2009, which will lead to a positive adjustment and forward-looking economic behaviour. The economy is forecasted to recover with a growth of 3.8 per cent in 2010. Due to the rapid decline in residential and commercial rent, as well as the internationally declining commodity prices, consumer inflation rate is estimated to mark 1.5 per cent in 2009, compared to 12.3 per cent in 2008. The economic recovery is forecasted to lead consumer inflation to 4.2 per cent in 2010.

Non-OPEC members of the GCC countries, namely Bahrain and Oman, are estimated to mark a modest real GDP growth in 2009. Bahrain is estimated to register 2.8 per cent real GDP growth. The crude oil production level of Bahrain is estimated to increase moderately. As to other GCC countries, active fiscal measures already in place supported the domestic demand. Investment activities in the energy sector as well as the aluminium industry have been ongoing, which supplemented the weakened activities in the financial and real estate sectors. The sustained growth in the crude oil production level of the country warrants a positive growth. Moreover, the recovery in domestic demand is forecasted to enhance the growth path. The real GDP growth is forecasted at 3.6 per cent for 2010. A relative stability in the general price level has been observed in Bahrain. Consumer inflation rate is estimated at 2.5 per cent in 2009, compared to 3.5 per cent in 2008. The stable trend is forecasted to continue into 2010 with a 3.6 per cent consumer inflation rate.

Oman is estimated to register a modest real GDP growth of 2.4 per cent in 2009. A consistent increase in crude oil as well as LNG production level contributed to the positive growth level. Moreover, the expansion of domestic demand continued owing to the fiscal measures of the Government. As the international exposure of the financial sector has been limited, the economy could weather a radical contraction of international trends. With the consistently growing crude oil and LNG production levels and the continuing active fiscal measures, the economy is forecasted to growth at 3.5 per cent in 2010. Oman's consumer inflation rate is estimated at 4.5 per cent in 2009, compared to 12.4 per cent in 2008. The declining trend is forecasted to continue in 2010 with a 3.2 per cent in the consumer inflation rate.

C. MORE DIVERSIFIED ECONOMIES

The more diversified economies (MDEs) showed resilience in their growth performance in 2009. The MDEs are estimated to register an average growth of 4.1 per cent in real GDP in 2009. Despite a potential fragility in external balances in terms of relatively weak current account positions, domestic demand continued to grow with strong capital account positions. Moreover, oil exporters in the subregion, Egypt, Iraq, the Sudan, the Syrian Arab Republic and Yemen, were not under the OPEC production quota and could avert a sharp decline in crude oil production levels. The lower reliance on manufacturing exports and international capital markets saved the subregion from the initial impact of the global financial crisis. The export level to the United States and Europe was severely affected, but the effect on the aggregated economy is limited. Moreover, the funding liquidity stayed available due to the limited exposure to international money markets. It must be noted that economic development in the subregion mostly remained structural, covering such issues as chronically high unemployment. Property markets were affected, but by a moderate decline at the most. The prospects for 2010 depend on: (i) a recovery of external demand from the United States, European Union countries and GCC economies; (ii) a sufficient margin against the potential foreign exchange constraint; and (iii) active fiscal measures with international and regional support. The forecast of real GDP growth of the MDE economies for 2010 is at 4.9 per cent.

Egypt is estimated to register a real GDP growth in 2009 of 4.5 per cent. A stable expansion of domestic demand has been observed, owing to the US\$2.75 billion fiscal package (LE 15 billion in local currency) that was announced in the previous year. Despite a sharp decline of exports to the United States and European Union countries, Egypt's largest trading partners, and the decline of service trade represented by the proceeds of Suez Canal, the potential weakness of the current account position was offset by the growing exports of natural gas and a relatively strong capital account position. The level of foreign reserves and the national currency exchange rate have remained stable throughout 2009. The recovery of external demand as well as a stable domestic demand growth with a planned second fiscal package for the fiscal year 2009-2010 will contribute to a forecasted growth in terms of real GDP at 5.5 per cent in 2010. Egypt's consumer inflation rate is estimated at 10.5 per cent in 2009, compared to 17.1 per cent in 2008. With the recorded firm foreign exchange rate against the US dollar, the high inflation rate is envisaged to have been caused by the weakness of the national currency against the euro and the ongoing growth of domestic demand. The Central Bank of Egypt will be active in aggregate demand management in order to keep the inflation rate under control. However, as the growth in domestic demand is expected to continue, consumer inflation is forecasted to be at 11.0 per cent for 2010.

Iraq is estimated to register a real GDP growth of 5.2 per cent in 2009. Crude oil production has maintained its course of recovery due to continuing investments in the production capacity. Iraq has not been under the OPEC production quota in 2009 and the drop in oil export revenues was not as extreme as in other OPEC member countries. The improved security situation, albeit still fragile, enabled economic activities that were supported by active fiscal measures. Moreover, the Iraqi economy started to widen its international exposure by non-oil trading activities, particularly with Jordan. The real estate sector has been increasingly active and the financial sector marked a consistent, albeit still limited, growth. The fragile economic condition, including the increasing fiscal deficits, is expected to prevail over 2010, but the recovery in crude oil production, domestic economic activities and the resumed inflow of foreign investments will ensure a positive growth in 2010 at 6.1 per cent. Consumer inflation rate is estimated to be at 3.5 per cent in 2009 in line with the regional trend. With an expected consistent growth in domestic demand, the forecast for 2010 is at 6.1 per cent.

Jordan is estimated to mark a real GDP growth in 2009 of 2.8 per cent. The decline in the mining and financial services sectors as well as a slow growth in domestic demand led the growth rate, which was modest compared to the 7.9 per cent growth in 2008. The Government has been active in supporting domestic demand to its fiscal ceiling by increasing capital spending in the first half of the year. The exports of apparel products from the qualifying industrial zones (QIZs)³ to the United States marked a rapid decline, but the export performance in total was supplemented by growing exports to Iraq. The decline in energy price and raw material imports for QIZs reduced the total imports, whereby the current account deficit in terms of GDP has narrowed from the level of 2008. The real estate sector has been resilient due to the active Government measure of tax exemption to households purchasing residential real estate. However, the economy is under a fiscal constraint as the Government is considering austerity measures in order to maintain its fiscal prudence. The decline in foreign grants has become another uncertain factor in light of the Government's latitude to provide fiscal support to buoy domestic demand. A moderate growth of 3 per cent is forecasted for 2010. The general price level has rapidly come down in 2009, with the consumer inflation rate estimated to mark 1.7 per cent, compared to 13.9 per cent in 2008. The consistent growth in domestic demand and such external factor as the national currency weakness against the euro is forecasted to lift the price level. Consumer inflation rate is forecasted to be at 4.5 per cent in 2010.

Lebanon is estimated to mark a real GDP growth of 4.8 per cent in 2009. The improvement in the security situation since May 2008 continued to attract foreign funds and tourists. Construction activity maintained the level of the previous year, but a modest decline in the real estate sector has been observed in

³ Qualifying industrial zones (QIZs) are designated industrial zones from which products that satisfy certain conditions with respect to material inputs and local contents can enter the United States freely, without quotas or duty being imposed upon them. Among ESCWA member countries, Egypt and Jordan are eligible to negotiate QIZ protocols.

light of the stagnating real estate prices. The current account deficit continued to deteriorate in terms of percentage over GDP. The trade deficit has widened in terms of percentage over GDP, but the decline in the inflows of workers remittances, which had been feared as one of the factor negative to the Lebanese economy following the global financial crisis, turned out to be moderate. The weak current account position was well supported by the strong capital account position, which led to a remarkable growth of foreign reserves throughout 2009. A further slowdown in real GDP growth is forecasted for Lebanon caused by an increasing fiscal constraint and a delayed moderate adjustment in real estate sector. Nevertheless, the economy is expected to maintain a positive growth path at the forecasted growth rate of 3.1 per cent. The general price level has sharply come down in 2009 with a consumer inflation rate estimated at 1.5 per cent, compared to 10 per cent in 2008. As is the case with Jordan, the consistent growth in domestic demand and such external factors as the national currency weakness against the euro is forecasted to lift the price level. Consumer inflation rate is forecasted to be at 3.9 per cent in 2010.

Palestine is estimated to mark a contraction of real GDP at 1 per cent in 2009. The physical blockades, continuing security instability and hostilities have imposed severe constraints on the economic activities. A sharp decline of the Israeli economy depressed the economic situation in Palestine even further. Moreover, the intensity of Israeli military actions in the Gaza Strip during a period of 22 days in December 2008 and January 2009 caused devastating destruction to human and physical capital. Reconstruction efforts have been hampered by unpredictable flows of international development aid and a weak fiscal infrastructure in the territory. Such non-economic factors as the security issues still dominate the situation and prospects of the Palestinian economy. However, as reconstruction efforts continue with regional and international support, the economy is forecasted to register a modest 0.5 per cent recovery for 2010. Consumer price inflation has come down to 1.5 per cent in 2009, compared to 9.8 per cent in 2008. Following international trends, the general price level is forecasted to pick up to 3.0 per cent in 2010.

The Sudan is estimated to mark a 4.5 per cent growth in 2009. On the production side, the steadily growing crude oil production and a stable agricultural sector contributed to the positive growth in spite of the decline in crude oil prices and oil export revenues. Moreover, an increasing inflow of foreign investments to the agricultural and energy sectors has been observed. However, the economy remained under a foreign exchange constraint, following which the Central Bank of Sudan placed a restriction on foreign currency transactions. Despite the significant foreign exchange ceiling, the growth in domestic demand has been consistent. Growing activities in services and the real estate sector have been observed both in Khartoum and Juba. However, the economy remains far from fully utilizing its potential due to non-economic factors in the country. Thus, the forecast for 2010 remains modest in light of a moderate growth of crude oil prices. The real GDP growth for 2010 is forecasted at 5 per cent. Due to the supply constraint of the foreign exchange ceiling, the consumer inflation rate is estimated to remain relatively high in 2009 at 9.5 per cent. This general trend is forecasted to continue in 2010, but a higher level of oil export revenues is estimated to relax the foreign exchange ceiling to have a slight decline in the general price level. Consumer inflation rate is forecasted at 9.0 per cent for 2010.

The Syrian Arab Republic is estimated to register a 2.5 per cent growth in 2009. The decline in the crude oil production level as well as crude oil prices stood as the main negative factor for the economy's growth performance. However, domestic demand has continued to grow steadily in combination with accelerating economic liberalization measures. This was particularly the case in the financial sector as the Damascus Stock Exchange opened for trading in March 2009. A set of reform measures have gradually increased the fiscal and monetary authorities latitude for demand management. Nevertheless, the economy is under foreign exchange constraints. Relatively stringent foreign exchange restrictions, in spite of recent liberalization measures, could function to defend the domestic economy from negative external shocks, but it would also limit the scope for rapid growth in domestic demand with a tighter foreign exchange ceiling. With recovering crude oil prices, real GDP is forecasted to be at 3.5 per cent for 2010. The resilient domestic economy is in a position to attract foreign investments, but it depends on the speed of economic liberalization. Consumer inflation rate has come down from 15.2 per cent in 2008 to 3.7 per cent in 2009. It should be noted that the high inflation rate in 2008 is attributed to a one-time effect caused by the reduction

of fuel subsidies. The foreign exchange ceiling and consistent domestic demand growth are forecasted to raise consumer inflation rate to 5.0 per cent in 2010.

Yemen is estimated to mark a 2 per cent growth in 2009. Despite the recovery in crude oil prices since the second quarter of the year, the decline in crude oil export revenues from the level of 2008 caused a significant foreign exchange ceiling that limited the scope of growth of domestic demand. The national currency of Yemen is the only currency in the region that marked a significant depreciation against the US dollar. The reduction in crude oil export revenues accentuated the fiscal constraint for which international support was pledged in 2006. However, the disbursed international and regional support has not been sufficient to relax the foreign exchange and fiscal constraints to allow a sustainable growth in domestic demand. The completion of the LNG projects and the LNG export initiated in November 2009 are forecasted to relieve both constraints to a certain extent in 2010. The growth forecast for 2010 is at 4.8 per cent. Consumer inflation rate has come down from 19.0 per cent in 2008 to 4.2 per cent in 2009. This decline is attributed to the fall in commodity prices. The forecast of consumer inflation is at 11.5 per cent for 2010 due to the existence of supply constraints against the growing domestic demand and to a continuing gradual depreciation of the national currency against major international currencies.

III. CONCLUDING REMARKS

In spite of the regional economic recovery forecasted in this paper, it should be noted that several downside risks remain. A possible decline in crude oil prices represents the main external downside risk for the economies in the ESCWA region. Crude oil prices are not only an indicator of the income and wealth of oil exporting countries, but also an indicator to determine the economic sentiment that influences forward-looking economic behaviour in the whole region.

A main internal factor for downside risk rests on the prospects of smooth balance sheet adjustments of commercial banks, business entities and households. Since the second quarter of 2009, the monetary authorities in the region have repeatedly claimed the existence of sufficient liquidity. During the same period, commercial banks and business entities often pointed to the lack of liquidity as major challenge for economic recovery. It is worth noting that what monetary authorities mentioned as “liquidity” is the “outside liquidity” for commercial banks, by which commercial banks are able to borrow funds. Meanwhile, what commercial banks and the business sector mentioned as “liquidity” is the “inside liquidity” represented by cash reserves and by an assured projection of future cash inflows. The shortage of outside liquidity for commercial banks is a symptom for the early stage of a financial crisis, during which the systemic risk of the financial sector prevails. The remedy for this systemic risk by a monetary authority is a liquidity injection into the banking system. However, against the shortage of inside liquidity of commercial banks and business entities, a different set of policy interventions is required. This is because the shortage of inside liquidity implies a necessity of balance sheet adjustments by which commercial banks and business entities can wind down the indebtedness in line with the value of assets.

As the property prices and associated rental prices came down, at various degrees, in the region, the deterioration on the asset side of the balance sheets may require substantial balance sheet adjustments. Repeated claims of lack of liquidity from commercial banks and business entities since the second quarter of 2009 are a proof for the need of such adjustments. A smooth facilitation of balance sheet adjustments will be a challenge for the policymakers in the region during the phase of regional economic recovery in 2010.