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IMF Regional Economic Outlook for the Middle East and Central Asia Sees Growth Higher Than Global Average, Emphasizes Downside Risks

The International Monetary Fund (IMF) today released the October 2008 *Regional Economic Outlook: Middle East and Central Asia.* Mr. Mohsin Khan, Director of the IMF's Middle East and Central Asia Department (MCD), outlined the report's main findings:

"The MCD region has continued to experience strong growth in 2008, outpacing global growth for the ninth year in a row. Growth is underpinned by high commodity prices, strong domestic demand, and also credibility of the authorities' economic policies. So far, the Middle East and Central Asia region has been largely resilient to the ongoing international credit crisis and the downturn in the US and other advanced economies. However, inflation has emerged as a key issue in the region, and is well above the average of all developing and emerging market countries.

"For 2008 we expect real GDP in the region to grow about 6½ percent. In 2009, growth is projected to continue at a slightly slower pace, around 6 percent. This is still significantly higher than the global average", Mr. Khan said.

The Regional Economic Outlook (REO) covers 30 countries, divided into three groups for analytical purposes: Oil exporters, low-income countries (LICs) and emerging markets[1]. For each of the three groups the REO presents key economic issues, and an assessment of growth prospects as well as policy challenges. In addition, the REO takes a closer look at topical issues related to individual countries or industries in the region.

Oil-exporting countries are expected to continue to expand in 2008 at about the same rate as in 2007, supported by oil prices that are still high relative to historical averages, and a pick-up in oil production compensating for a moderate slowdown in non-oil activity. However,

[1] ***Oil exporters*** comprise Algeria, Azerbaijan, Bahrain, Iran, Iraq, Kazakhstan, Kuwait, Libya, Oman, Qatar, Saudi Arabia, Syria, Turkmenistan, and the U.A.E.. ***Low-income countries*** *(LICs)* comprise Afghanistan, Armenia, Djibouti , Georgia, the Kyrgyz Republic, Mauritania, Sudan, Tajikistan, Uzbekistan, and Yemen. ***Emerging markets*** include Egypt, Jordan, Lebanon, Morocco, Pakistan , and Tunisia.

growth is expected to decelerate to 6 percent in 2009 in the wake of the global slowdown and lower oil prices.

Real GDP growth in **low-income countries** is projected to slow somewhat in 2008 before rebounding in 2009, as the recent spike in food prices comes to an end. **Emerging market countries** are expected to experience solid growth throughout the current year, before easing in 2009 due to the global economic slowdown.

Inflation in the region is projected to rise to 15 percent in 2008, before easing somewhat in 2009 as world food prices drop. The main sources of inflationary pressures differ, however, across country groupings. These range from the surge in food and fuel prices, which has affected mostly **low-income** and **emerging market countries**, to strong domestic demand pressures and supply bottlenecks in the Gulf Cooperation Council (GCC) countries, to the weakening of the U.S. dollar (through mid-2008), to which many MCD countries are pegged.

The REO sees **some downside risks** to the outlook in the Middle East and Central Asia region. Growth could be lower than forecast in case of a sharper and more protracted slowdown in advanced economies, and if the effects from the financial turmoil become more pronounced. Inflation could be higher, if international food and oil prices surge again, or if macroeconomic policy is eased too much. In contrast, a drop in commodity prices would lessen inflationary pressures in the region, as would a further recovery of the U.S. dollar for those countries that peg to the U.S. dollar. Although financial institutions in MCD countries are unlikely to suffer greatly from the global financial turmoil, a few countries are at risk from external contagion, and the financial sector in some countries has a significant exposure to regional real estate markets.

Two main policy challenges are facing the region in the short term, according to the report: the risk of rising inflation and the need to boost the resilience and flexibility of the region's financial sector.

Many central banks in the region have already raised interest rates in response to rising inflation, but policy responses so far have been modest and interest rates generally remain negative in real terms. All countries should be particularly attentive to potential second-round inflation effects, and for this reason should avoid further broad-based wage increases.

Strengthening the banking system should be considered an important objective, in particular given the global environment. Policymakers should also closely monitor developments in real estate prices and assess vulnerabilities of the financial system to property price corrections and liquidity pressures.

The full text of the October 2008 *Regional Economic Outlook: Middle East and Central Asia* can be found on the IMF's website, www.imf.org.