THE WORLD BANK

MENA Quarterly Economic Brief

Office of the Chief Economist Issue 2 January 2014

Growth slowdown heightens the need for reforms

HIGHLIGHTS Ongoing regional tensions, together with a challenging (albeit slightly improving) external environment, have hit the economies of the Middle East and North Africa (MENA) region hard. Economic growth is slowing, fiscal buffers are depleting, unemployment is rising, and inflation is mounting in seven of the region's most vulnerable economies-- Egypt, Tunisia, Iran, Lebanon, Jordan, Yemen and Libya. Short-term policy actions such as increasing public sector wages and subsidies—aimed at reducing social tensions--exacerbate the situation, which is driven by long-standing structural weaknesses, including labor market rigidities, complicated and opaque regulations, infrastructure deficiencies, regressive and inefficient subsidies, and inadequate social safety nets. While these countries face an unstable political and macroeconomic environment, the growth slowdown after the Arab Spring creates a unique opportunity to address these structural problems to both create fiscal space and restructure the economy towards job creation and inclusive growth.

Real GDP growth (%)							
	Egypt	Tunisia	Iran	Lebanon	Jordan	Yemen	Libya
2010 (Pre- Arab Spring)	5.1	3.1	5.9	7.0	2.3	7.7	5.0
2011	1.8	-1.9	1.7	3.0	2.6	-12.7	-62.1
2012	2.2	3.6	-3.0	1.4	2.7	2.4	104.5
Latest quarter	1.0	2.7	…	2.5	2.8	…	…
2013f	2.1	2.6	-2.1	1.5	3.1	3.0	-6.0
2014p	3.0	3.0	1.0	1.5	3.5	6.0	23.0
Unemployment rate (%)							
	Egypt	Tunisia	Iran	Lebanon	Jordan	Yemen	Libya
2011	11.8	18.9	12.3	…	12.9	…	20.7
2012	12.6	17.6	15.0	…	12.2	…	19.5
Latest quarter	13.4	15.7	…	…	14.0	…	…
2013f	13.3	16.7	15.3	13.0	…	…	15.0
2014p	13.9	16.0	15.0	…	…	…	…
Inflation rate (%)							
	Egypt	Tunisia	Iran	Lebanon	Jordan	Yemen	Libya
2011	11.0	5.0	20.6	5.7	4.4	19.5	15.9
2012	8.6	5.5	29.4	5.7	4.8	9.9	6.1
Latest quarter	11.7	6.1	…	…	6.1	14.1	3.6
2013f	6.9	6.2	35.7	3.8	5.2	12.0	4.2
2014p	10.2	5.5	22.5	3.2	3.8	12.0	4.9

Source: World Bank and national official sources.

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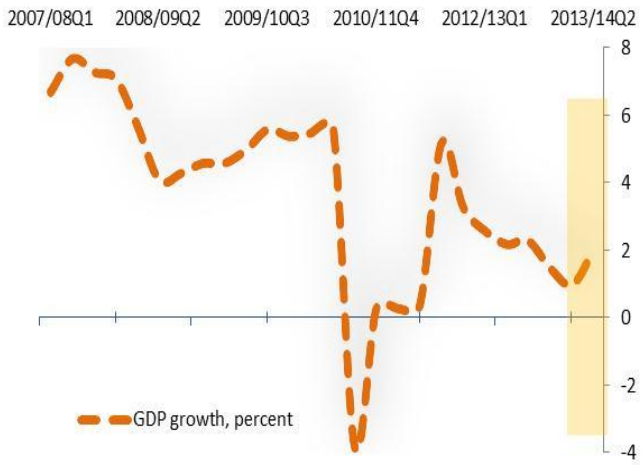
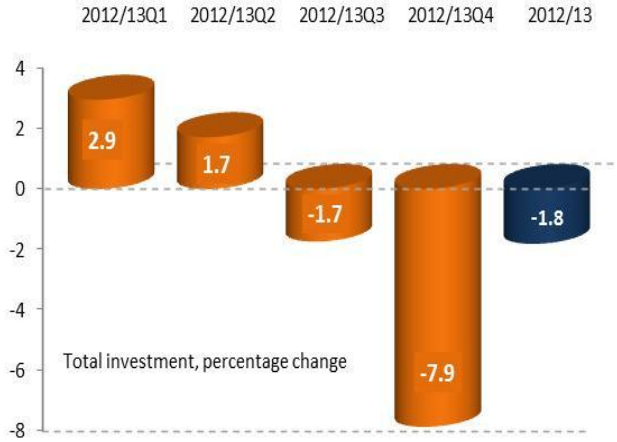
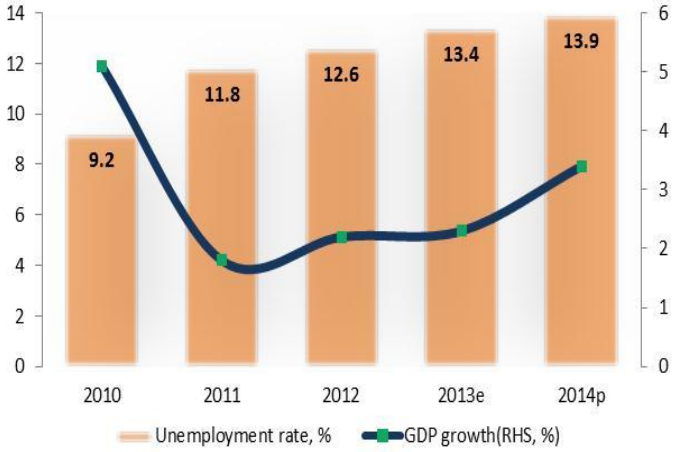
EGYPT

Since August 2013, the current interim government has announced two economic stimulus packages for a total of $8.7 billion. The first stimulus was launched in August and accounted for 1 percent of GDP ($4.3 billion); the second package is planned to be announced in early February 2014. These stimuli are financed by budget savings and aid from Saudi Arabia, Kuwait and the United Arab Emirates. Both packages seek a short-term expansion of the economy through higher public investment and public sector wages. The target is to boost growth to 3.5 percent in the current fiscal year (ending June 2014) and reduce the fiscal deficit from 13.7 to 9.1 percent of GDP. The stimulus packages are embedded in a development plan, Egypt 2022 vision, which aims at achieving sustainable and inclusive growth in the medium-term by investing in human capital especially education, training, healthcare and technology. Under the plan, the growth rate is expected to increase to 5-7 percent in the medium term through increases in private sector investment and enhanced information technology infrastructure.

Nevertheless, real GDP growth in Egypt has been stagnating at around 2 percent and is expected to remain weak in 2014. This was mostly due to the lower investment in fiscal year 2012/13 relative to previous years, reflecting the "wait-and-see" attitude of domestic as well as foreign investors. Total investment declined by 2 percent, reaching 14.2 percent of GDP in 2012/13 compared to 16.4 and 17.1 percent of GDP in fiscal years 2010/11 and 2011/12 respectively. Foreign direct investment has yet to recover to pre- revolution levels but has shown some signs of improvement. Official data show that Egypt attracted a total of $9.2 billion FDI inflows over the past three years ($3 billion in 2013). Historically, FDI inflows to Egypt were about $9 billion annually.





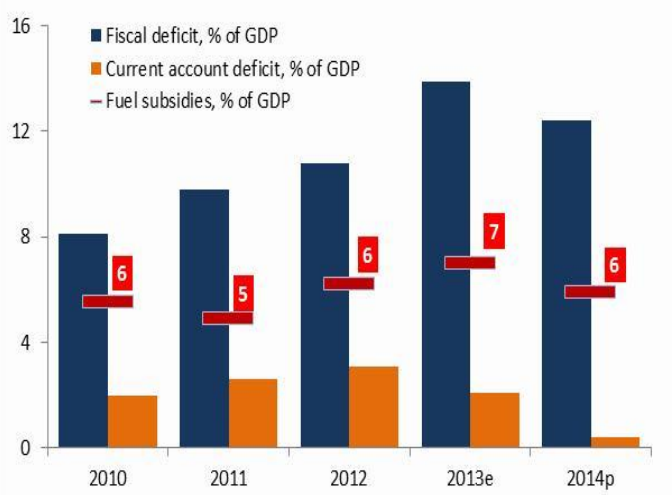


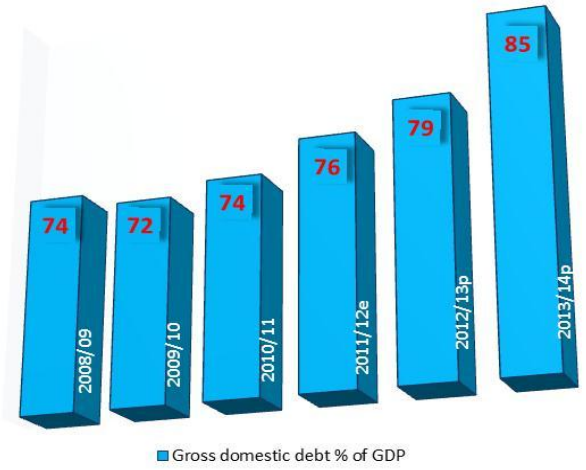
Source: National official sources.

Due to the weak economic growth, unemployment rates have been increasing, reaching 13.4 percent in the third quarter of 2013, an increase of 0.1 percent compared to the previous quarter. This figure includes only registered workers and does not take into account the informal economy where unemployment is believed to be higher than the official rate. The period July to September 2013 alone saw an additional 30,000 unemployed Egyptians due to ongoing political instability and escalated violence. Official data show between 700,000 to 800,000 new job seekers entering the job market every year, some of whom will add to the already large stock of unemployed standing at 3.6 million. Estimates by the World Bank show that the economy needs to grow by at least 6 percent to make a dent in the unemployment rate by 2020.

The gap between female and male unemployment rates, which pre-dates the 2011 revolution, has widened sharply. The male unemployment rate stood at 9.8 percent, while that of females reached 25.1 percent as of end-September 2013. Data from the recent labor survey in Egypt show that approximately 74 percent of the unemployed are between 15 and 29 years old, of which 42 percent are in the age group of 20-24 year-olds. More than 76 percent of the unemployed are educated, with 30 percent having university degrees and above.

The government's expansionary fiscal policy together with rising domestic debt over the last two years have left little room for private sector financing. Ballooning food and fuel subsidies (totaling about 9 percent of GDP and 30 percent of government expenditure) are keeping the fiscal deficit higher than before, reaching an unprecedented 13.7 percent of GDP in 2013, compared to 11 percent in 2012. Moreover these subsides were disproportionately distributed and benefitted the rich more than the poor. For example, a World Bank study showed that in rural Upper Egypt, the richest quintile received about 48 percent more in per





Source: National official sources.

capita benefits than the poorest group from the food subsidies.

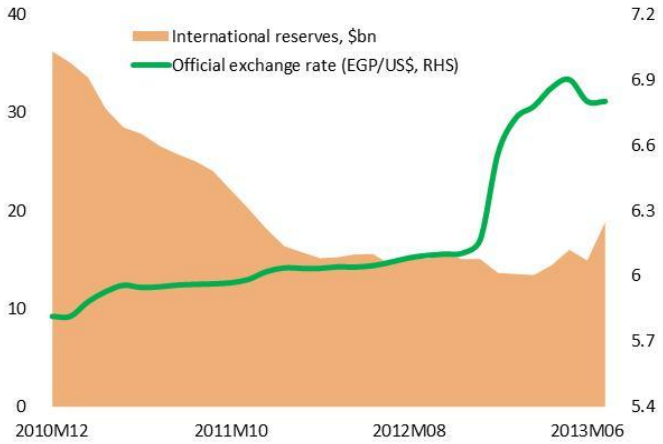
The country's financial needs are still large, despite US$16 billion worth of funds pledged by the Gulf countries. Financing is still met partially by drawing down international reserves (which, including aid received from the Gulf, covered 4 months of imports in December 2013) and by accumulating public debt. Official data show that government domestic debt alone has

increased by 6 percent in the third quarter of fiscal year 2013, relative to the second quarter of the same year, and is estimated to reach a record high of close to 85 percent of GDP by end of fiscal year 2013/14.

The Gulf funds have boosted reserves, creating space for monetary easing. In early December, the Central Bank reduced the overnight deposit and lending rate – for the third time since July 2013 - by 0.5 percent to promote investment. The domestic currency has slightly strengthened. Official data show that the Egyptian pound (EGP) rose to 6.89 pounds against the US dollar in late December after plunging to 7.03 in early August. Yet, little has changed in the parallel (black) and forward markets, where the EGP is still weaker than the official rate.

Inflation remains high. Monthly data produced by the Central Agency for Public Mobilization and Statistics (CAPMAS) indicate that the annual inflation rate has more than doubled to 11.7 percent in December 2013 (from 4.7 percent in the same month of the previous year). The increase in inflation is mainly due to increases in the prices of food, accommodation, and food services. Preliminary estimates from the World Bank show that, under the current economic situation, inflation will remain high at about 10.2 percent in fiscal year 2013/14, due to higher food prices, lower production, expansionary policies and spillover from higher public sector wages.

The Egyptian economy suffers from several long standing structural weaknesses. First, the economy has experienced decades of underinvestment especially in industry and infrastructure. Investment remains low and its share of GDP has continued to decline. Second, there is evidence (Diwan, Keefer and Schiffbauer, 2013)[1] that the private sector is



Source: World Bank and IMF.

dominated by politically connected firms who have virtually blocked entry and growth of new firms. Based on the Ease of Doing Business indicators, Egypt is in the bottom half of all ranked countries--109th out of 183 in 2013. One of the major constraints to private sector development is the lengthy bureaucratic procedures. For example, in procedures dealing with construction permits and enforcing commercial contracts, Egypt ranks close to the bottom of the list.

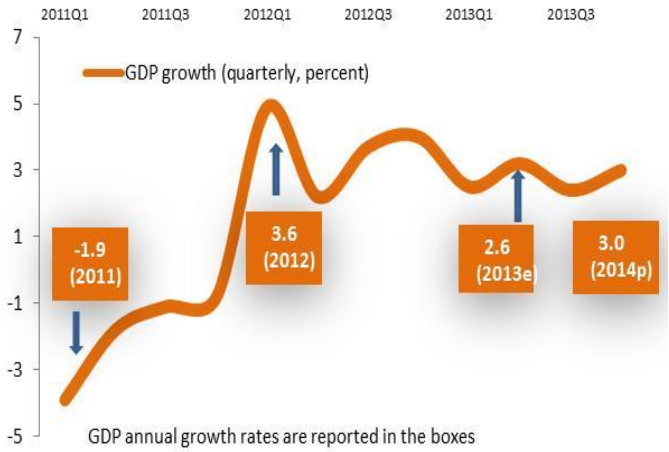
Finally, economic weaknesses across key sectors have constrained job opportunities for the large number of unemployed, as for new entrants to the labor market. A large proportion of people have moved to the informal sector, with no access to social security benefits. Furthermore, it has pushed large numbers of people to live closer to the poverty line, making them vulnerable to external shocks. Official data show that poverty rates are high, particularly in rural areas. The poverty headcount (number of people living under the national poverty line of EGP 3920 ($569) per person annually) has increased to 26.3 percent in 2012/13 compared to 25.2 percent in 2010/11. The extreme poverty headcount defined as EGP 3570 ($518) per person increased tenfold after the 2011 revolution reaching 4.4 percent in 2012/13.

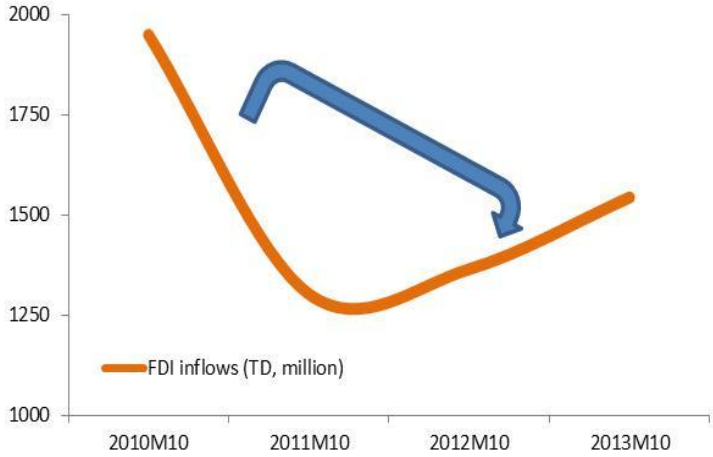
[1] Cronyism and private sector growth in Egypt, World Bank.

TUNISIA

After months of political deadlock that spanned over most of 2013, Tunisian politics is moving ahead. Following a consensus arrangement between the main political parties brokered by major civil society organizations in December, an interim Prime Minister was appointed in January, the Constitution has been approved by the National Constituent Assembly and a transition cabinet to finalize the new Constitution, the Electoral Law and arrange for new general elections has been announced. Nevertheless, political and security challenges still weigh heavily on the economy. The growth recovery that was observed in the second half of 2012 was unsustainable in 2013 with a marked slowdown in the third quarter of 2013, and the prospects for a rebound in 2014 remain bleak. Quarterly data show that real GDP growth declined to 2.8 percent on average in the first 9 months of 2013, compared to 3.8 percent in same period of 2012. The World Bank has lowered its growth forecast for 2013 from 3 percent to 2.6 percent. Under the scenario of easing political tensions and recovery in the Eurozone area, the Bank estimates a growth rate of about 3 percent in 2014.

Investment, particularly FDI, is stagnating as investors wait on the sidelines. Data published by the Foreign Investment Promotion Agency (FIPA) show that even though FDI inflows increased in the first ten months of 2013 compared to the same period in 2012, they are still lower than the pre-revolutionary period. Only a slight recovery was observed in the manufacturing industry, mainly in electricity and food-processing. The services sector experienced the largest decline in investment - down by 22 percent - followed by the industrial sector – down by 5 percent - and energy - down by 4.3 percent. The decline in FDI was mostly due to lower inflows from France, the largest source country for Tunisia between 2008 and





Source: National official sources.

2012. French FDI fell from 1,105 tracked projects in 2008 to 714 in 2012, a 35 percent drop.

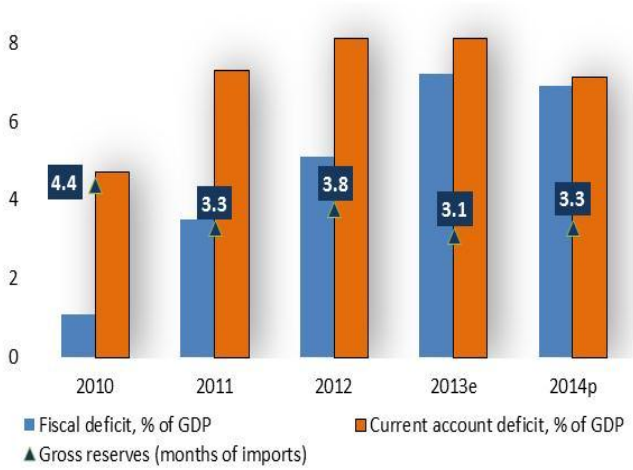
Tunisia's fiscal buffers are rapidly deteriorating as a result of the expansionary fiscal policy that was extended into 2013. Current expenditure has increased from 17.8 percent of GDP in 2010 to an estimated 24.6 percent in 2013, an increase of 7 percent, while total government revenues have been declining. The overall fiscal deficit has remained high and is estimated to reach 6.2 percent of GDP in 2013

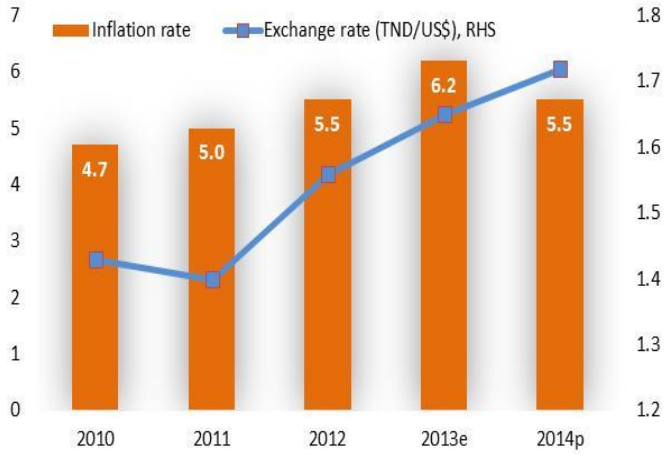
(commitment basis, up from 0.6 percent of GDP in 2010), mainly as a result of an increasing wage bill and higher subsidies. In fact, spending on transfers and subsidies has been skyrocketing, estimated to reach a record high of 7.6 percent of GDP in 2013 compared to only 3.6 percent in 2010.

Official data show that between 2010 and 2013, total subsidy expenditures more than tripled. More than two-thirds of the subsidies are allocated to energy and the other third goes toward staple goods. The World Bank estimates that the budget deficit could exceed 7 percent of GDP unless the government takes the initial steps to streamline energy subsidies and put budget controls in place. The rising deficit has added to inflationary pressures since 2012. At the end of 2013, inflation is estimated to have reached 6.1 percent compared to the 2012 average of 5.6 percent and 3.3 percent in the period between 2000 and 2010.

The current account deficit has continued to widen in 2012 and 2013 due to depressed European demand and stalled tourism receipts and remittances. In particular, textile exports, one of Tunisia's major exporting industries, contracted by 7.1 percent. Tourism receipts during the first eight months of 2013 were approximately 10 percent lower compared to a year earlier (in real terms). Gross reserves are expected to decline to $7 billion in 2013 (from $11 billion in 2009) covering 3 months of imports. As a result, the Tunisian Dinar depreciated by 6.6 percent against the Euro and by 7.1 percent against the US Dollar, as of August 2013.

There are some positive signs that the unemployment rate is declining from its post-Arab-Spring peak. Official data point to an unemployment rate of 15.7 percent (with 620,600 people unemployed) in the third quarter of 2013, a drop of 0.2 percent compared to the previous quarter and 1.3 percent compared to the same period in 2012.





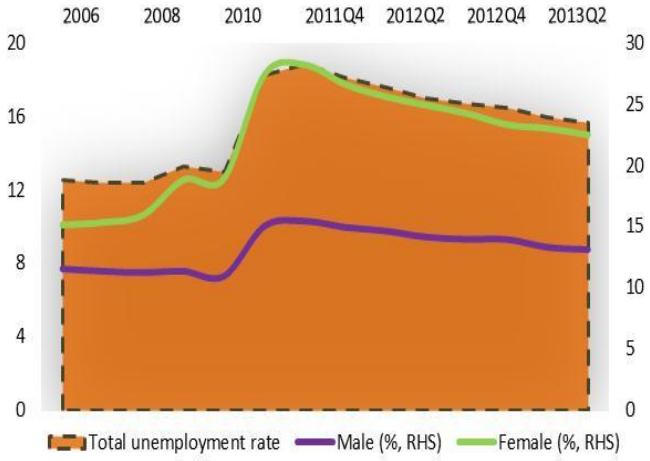
Source: National official sources.

Unemployment still remains high among university graduates, at 33.5 percent in the third quarter of 2013 compared to 31.6 percent in the second quarter. The rate is even higher for educated youth. The gender gap has increased. Unemployment rates are much higher for women (23 percent) and particularly for educated women (43.5 percent of female graduates) and in remote regions.

A large share of the increase in unemployment post the Arab Spring was due to the reduction in seasonal employment in the tourism sector, and the return of a large number of Tunisians

from Libya. It is estimated that the rate will stay high, between 15 and 16 percent in 2014, as the public sector and parastatal companies have been the main drivers of the reduction in unemployment over 2012-2013. The World Bank estimates that Tunisia needs to grow by at least 4.5 percent in order to reduce the unemployment rate by 2020. In the medium term, the government's goal is to reduce unemployment by creating 50,000 jobs in the next five years. For example, the project, Smart Tunisia, approved by the Cabinet in late November, aims to attract foreign and domestic investment especially in the ICT field and create jobs for educated youth.

Structural weaknesses remain, which, if not addressed promptly, could further delay the prospects of a growth recovery. Social and economic disparities across regions remain key economic challenges for Tunisia. Among structural priorities, a stronger banking sector and a deeper domestic financial market will be important to finance investment activities. This can be achieved by improvements in the environment for doing business to foster private investment.



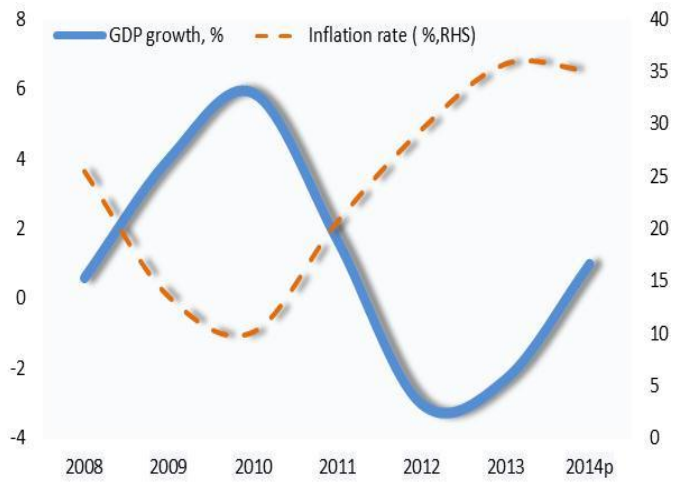
Source: National official sources.

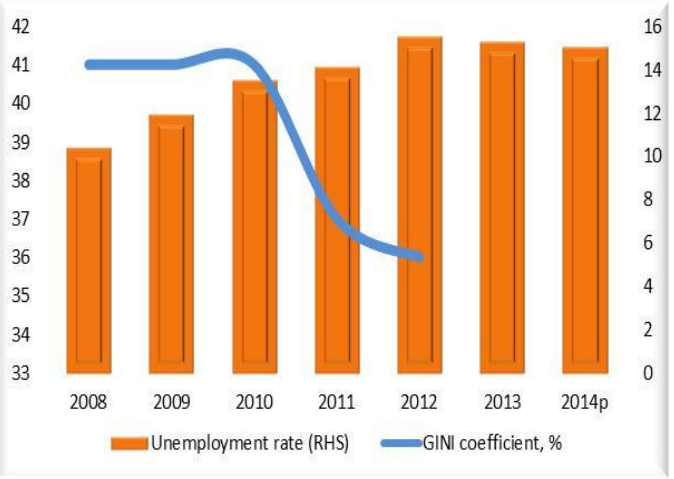
IRAN

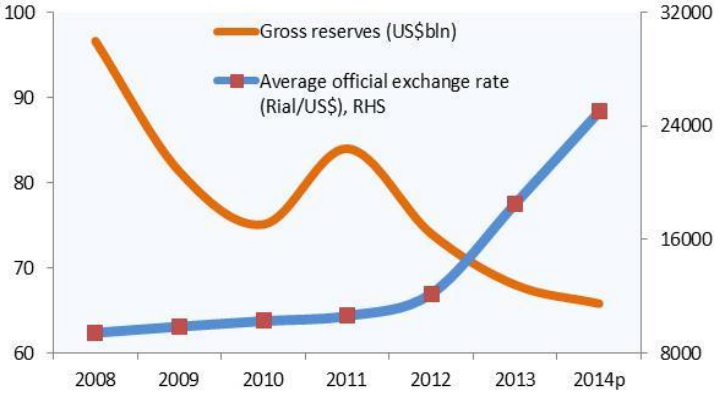
With the election of the reformist-backed President, Iran appears to have entered a new era of foreign policy. Since taking office, the new administration has been fostering a shift away from the previous government's "Look-to-the-East" policy. The priority has been on reducing misunderstanding and unnecessary tensions in relations with the West, particularly with the US, through confidence-building measures. In this regard, the P5+1 countries – the US, Britain, China, Russia, France and Germany – and Iran reached an interim deal on Iran's controversial nuclear program in late November in Geneva. The agreement lasts for 6 months and could lead to a long-term guarantee that Iran will not produce nuclear weapons. In return, Iran will receive some relief from international sanctions, including those on gold and petrochemical exports, and the release of Iranian oil revenues of about $4 billion.

In addition, there have been major developments on the domestic social front. The president has laid out a program for personal freedom and free private life for Iranians and has pledged to create a citizens' rights commission in the near future. A number of prominent activists and political prisoners have been released; internet speed and availability has improved as several new ministers have embraced Facebook and Twitter; restrictions on news agencies and newspapers have been eased; and a number of hardliners at the top of Iran's major universities have been replaced with technocrats.

To reverse the downward spiral of the economy, the cabinet has announced several measures. These include: giving greater autonomy to the Central Bank, reforming the tax system, stabilizing the domestic currency in the market, reinstating the Management and Planning Organization which was in charge of







Source: National official sources and EIU.

drafting the government budget and the country's five year development plans, and opening up the oil sector to foreign companies for investment and technical assistance.

Yet, a swift economic turnaround seems far-fetched as various indicators point to a dire economy. Growth has contracted for two consecutive years (-3 and -2.1 percent in 2012 and 2013 respectively) and the outlook for the next year is bleak. Oil exports have been halved and the financial system has remained constrained, partly by international sanctions. The economy is suffering from high inflation. Official data from the Statistical Center show that inflation reached 35 percent at the end of December and is estimated to stay at this level at the end of the current calendar year (ending March 2014). Food and real estate prices, in particular, have risen sharply. Unemployment rates are still in double digits, 12.2 percent in October, with youth unemployment at 26 percent. The rate for female unemployment reached 50 percent in some cities outside of the Capital (Tehran). The average official unemployment rate for females in Tehran is 21.6 percent. The fiscal deficit is set to widen to 5.2 percent of GDP in 2013 from 4.7 percent in 2012 due to the large drop in oil export receipts. On a positive note, the government's moderate approach towards domestic and external affairs has already revised market expectations, reducing speculations in the domestic exchange rate market. The Iranian currency, which lost 80 percent of its value against the dollar since March 2012, regained part of that value in December 2013.

Structural weaknesses, that pre-date the recent nuclear conflict, continue to hinder economic prospects. These include i) the mismanagement of the oil wealth and lack of economic diversification, ii) large public and quasi-public enterprises blocking private sector developments – barriers to doing business are numerous, iii) a high and chronic unemployment rate especially among females and youth, and, iv) a growing number of vulnerable people living just above the poverty line, despite a low poverty rate for the whole economy.

While there have been some efforts in diversifying the economy by expanding productions in other sectors, including petrochemicals, the economy is still largely dependent on oil. In 2012, oil constituted about 30 percent of GDP, 80 percent of exports and 70 percent of fiscal revenues. The Herfindahl index calculated by UNCTAD shows that, between 1995 and 2012, the index value has hovered around 0.7, which is substantially higher than the 0.1 calculated for developing countries and for the rest of the world, except for the countries in Western Africa.[2] Persistent dependency on oil receipts combined with high volatility in oil prices, in addition to various sanctions imposed on oil exports, have destabilized the economy. Real GDP growth has been fluctuating widely over the past decades, particularly after international sanctions were tightened in 2012.

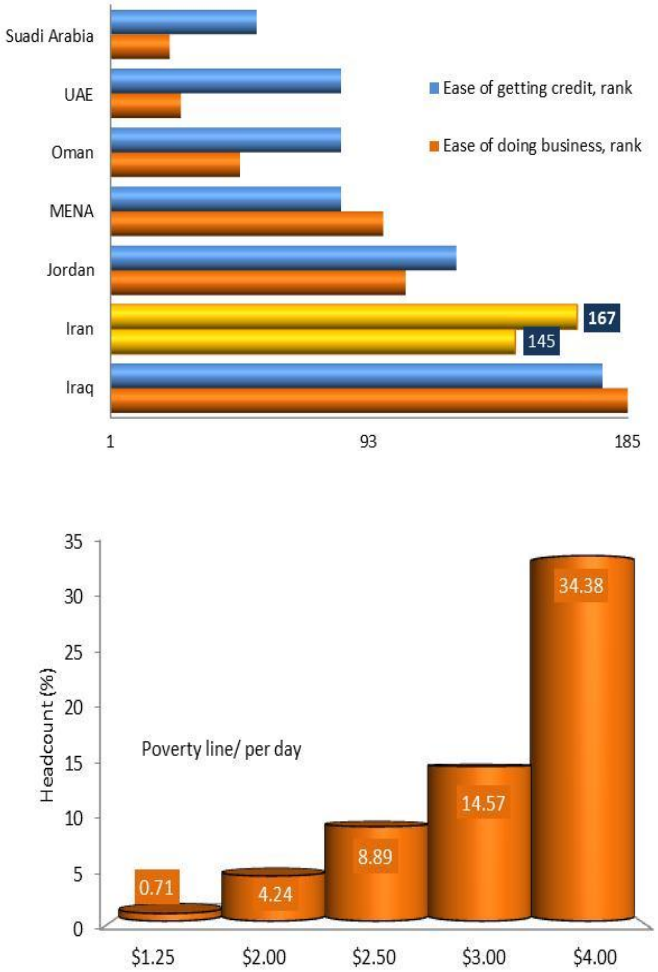
The private sector is the residual sector. The large size of the public as well as quasi-public sectors - Bonyads (charitable foundation) with their privileges has left little space for the private sector to grow. The ease of doing business indicators ranked Iran close to the bottom, 147th out of 183, in 2013. One of the constraints in improving private sector activity is access to credit and foreign exchange, which are mostly allocated to the elite in the public and quasi-public sectors. Furthermore, laws and regulations related to investor protections are not clear and in some instances limit the ability of investors to raise capital.

[2] The concentration index (ranges between 0 and 1) shows how exports and imports of a country are concentrated. An index value close to 1 indicates a very concentrated market and values closer to 0, indicates a homogeneous market.

The investment climate has not been attractive to foreign investors. World Bank data show that Iran had the lowest FDI share of GDP, about 1 percent, in the region.

Chronic unemployment is one of the vexing problems in the country. Official data indicate a 12.3 percent unemployment rate in 2012, which is probably an underestimate. The gap between female and male unemployment rates has also increased. The 21.6 percent female unemployment rate is double the rate for males. The unemployment rate is high for youth (15-24 years) at 26 percent in 2013 while the rate is much higher for female youth (at 42.7 percent). The underlying factors of the chronic unemployment include an unusually high rate of labor supply growth (3.5 percent on average) driven by the demographic bulge, increased women's participation in the labor force (at 15 percent) and a shift in the skill mix in the labor force towards the higher skilled which has not been matched with the sectoral mix of the economy. On the demand side, educated job seekers are constantly looking at public sector jobs because the private sector is small and has not been able to grow due to various constraints related to business regulations.

While the basic poverty rate is low, a large proportion of people are living close to the basic poverty line. World Bank data show that only 0.7 percent of population (half a million people) lived under the poverty line of $1.25 a day (PPP) in 2010. However, the number of vulnerable people living just above the poverty line increases as the poverty line rises slightly over the $1.25 a day. Although the removal of food and fuel subsidies in 2012 and their replacement with cash transfers to almost 80 percent of the population has improved the distribution of income (the Gini coefficient has declined slightly), a large number of people



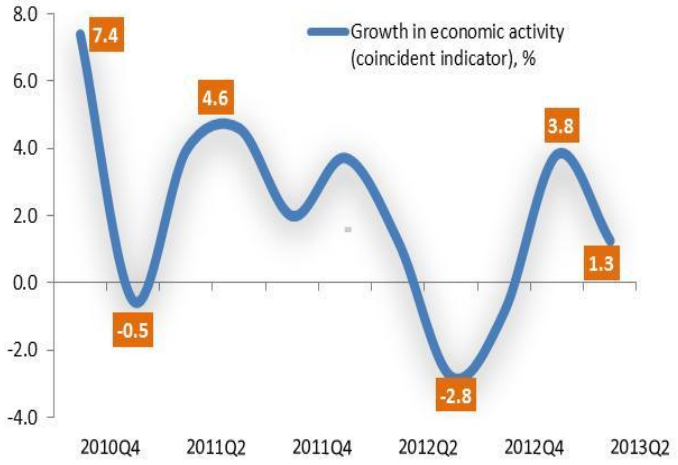
Source: World Bank.

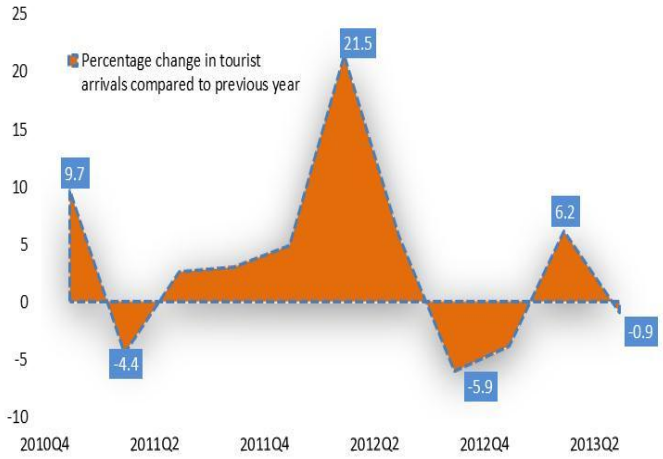
remain in a vulnerable condition. An increase of $0.5 a day in the poverty line (from $2 to $2.50 and from $3 to $3.50) could put between 4 to 6 percent of the population – over 4.5 million people - in to poverty. This suggests that many people are vulnerable to external shocks or change in their personal conditions. The rising unemployment and inflation rates with their immediate impacts on people's living conditions are the important factors, among others, contributing to the worsening of the poverty situation in Iran.

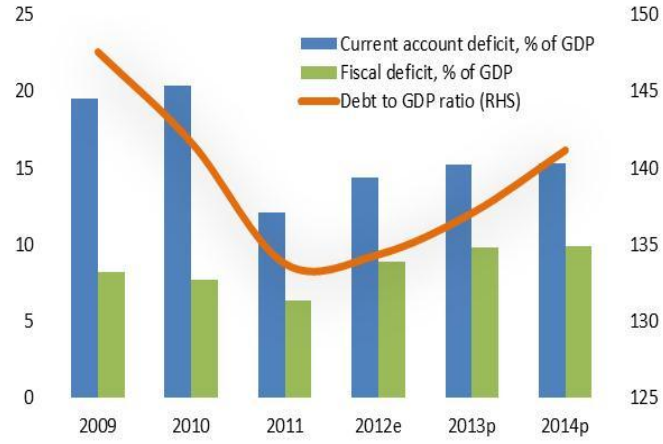
LEBANON

The economic situation in Lebanon has been increasingly affected by domestic and external tensions. On the domestic front, there is an institutional vacuum after the government resigned in March and the formation of a new government has been put on hold because of the regional situation and Syrian conflict. This situation is weighing heavily on the Lebanese economy which already suffers from anemic growth, a rising fiscal deficit and mounting public debt. The large influx of Syrian refugees, estimated at about 866,000 in 2013 (about 20 percent of Lebanon's total population), has intensified the already difficult economic situation. Refugees are across the country, with the largest concentrations in northern and eastern Lebanon, where poor, farming households reside. The growing size of the refugee population is expected to impact economic growth, increase poverty and unemployment among the Lebanese, and further increase the already high budget deficit - estimated at 10 percent of GDP in 2013 - in a country struggling with a high public debt estimated at about 137 percent of GDP in 2013. Under this situation, the Central Bank of Lebanon (Banque du Liban, BDL) intends to introduce a new package of $800 million to stimulate economic activity especially in the real estate sector.

Economic growth is still very slow. Official data show that economic activity measured by the coincident indicator (monthly estimates of GDP produced by BDL) has stagnated at around 2.5 percent in the first half of 2013, the same as the growth rate achieved in the first half of 2012. Activity in the real estate sector (accounting for 13 percent of GDP) has remained slow. Official data show that construction permits were down by 10 percent and the number of real estate transactions fell by 6 percent in the first 10 months of 2013 compared to the same period







Source: National official sources.

last year. The tourism sector is still suffering from heightened insecurity in the country. The number of tourist arrivals declined by 4.9 percent in the third quarter of 2013 compared with the same period in the previous year, largely as a result of the continued fall in visitors from Arab countries as governments warned citizens against travelling to Lebanon, particularly after the recent incident in the Iranian Embassy in Beirut, and the bomb that killed former finance minister, Mohamad Chatah. Preliminary estimates by the World Bank suggest that growth will remain low at about 1.5 percent in 2013 and 2014, well below its potential.

As in the rest of the MENA region, unemployment in Lebanon has remained high. Estimates from the Ministry of Labor point to the unemployment rate in the range of 12 to 13 percent in 2013. The rate is twice as high for the youth aged under 25 and also for the highly educated. The large number of Syrian refugees entering Lebanon's labor market continues to increase the labor supply, leaving little room for the unemployment rate to decrease. Estimates show that the influx of Syrians could increase labor supply by almost 30 and 40 percent in 2013 and 2014 respectively. Informal employment is high and has increased recently. IMF estimates show that more than one third of those employed are in the informal sector.

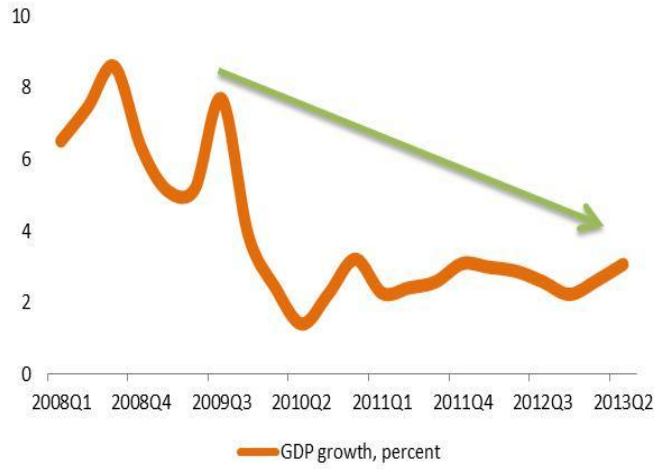
Current account and fiscal deficits and public debt as shares of GDP have remained persistently high, giving rise to large financing needs. The current account deficit has hovered at around 15 percent since 2009 and the debt to GDP ratio has exceeded 140 percent of GDP. The government's fiscal deficit has stayed in the range of 7 to 9 percent for the past five years. Quarterly data show that the fiscal deficit has increased by more than 67 percent in June as a result of the permanent fiscal spending increase that was introduced in 2012 and extended to 2013. According to the data from the Ministry of Finance, the deficit amounted to nearly $1.9 billion during the first six months of 2013, relative to a deficit of about $ 1.1 billion during the same period in 2012, an increase by 68 percent in only six months. For 2013 and 2014, the budget deficit is expected to remain elevated, approaching 10 percent of GDP.

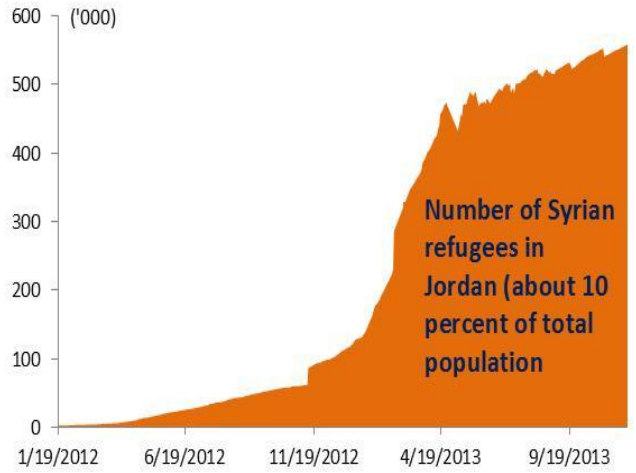
Long standing structural challenges are still unresolved. These include infrastructure deficiency, inadequate public services, overcrowded public schools and limited access to government clinics and hospitals for low income people especially in rural areas. Moreover, the flow of refugees is stretching all of these sectors to the limit. Skill mismatches, labor market rigidities, and high reservation wages have resulted in labor market inefficiencies. A survey showed that companies identify labor skills as a major constraint to business. Employers also identify labor regulations, including the design of the end-of-service coverage, as an impediment to employment. With the recently approved wage increase, the minimum wage would be among the highest in the region though, when adjusting for costs of living, it is broadly in line with the regional average. Lastly, high remittances and education costs contribute to voluntary unemployment by keeping reservation wages high. Thus reforms should be directed at creating a dynamic economy that can generate jobs that would help to reduce unemployment and poverty levels. This requires investment and reforms in infrastructure as well as improvements in the business climate and the labor market. A medium-term fiscal strategy anchored in reducing the debt-to-GDP ratio could revive market confidence and create fiscal space through revenue and expenditure measures for higher social and capital spending.

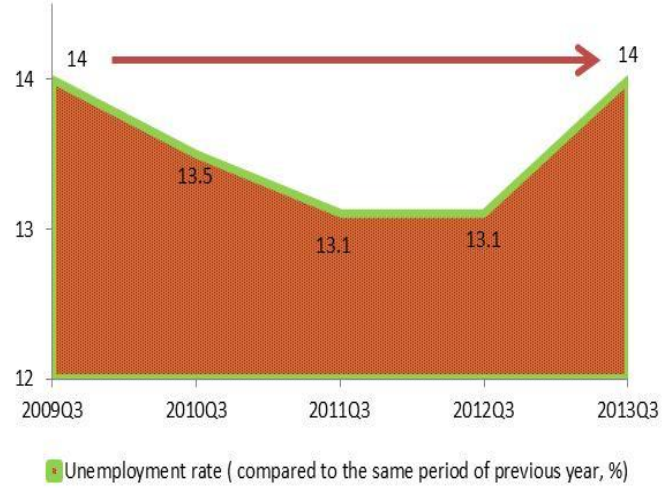
JORDAN

Regional tensions, cutoffs in gas from Egypt and the influx of Syrian refugees to Jordan continue to weigh on the Jordanian economy. Fiscal and external accounts are deteriorating, while the influx of refugees has constrained the labor and housing markets and restricted access to public services. As a result, the GDP growth rate is not expected to rise above the 3 percent level it has been at for nearly 3 years. Official data show that GDP growth reached 2.8 percent in the third quarter of 2013, (while higher than 2.6 percent in the first quarter of 2013) compared to the previous quarter of last year. However, on an annual basis, there have not been any improvements in real GDP growth in the first six months of 2013 as it has been standing at 2.8 percent in first half of 2013 relative to the same period in 2012. The preliminary estimates from the World Bank show that under the current situation, growth will remain within the 3 percent trajectory until 2015 when it is expected to surpass this rate.

With slow growth, unemployment continues to increase. Official data show that the unemployment rate for the third quarter of 2013 rose by 1 percent (to 14 percent) compared to the same period for 2012. This represents the highest increase in the number of unemployed over the past four years. Unemployment among men stood at 11.3 percent with that for women 26.8 percent. Unemployment among youth (15-19 and 20-24 years) is extremely high, standing at 37.9 and 34.9 percent respectively compared with 36.1 percent and 30.1 percent respectively for the last year. The data show that unemployment has remained high among university graduates, approaching 20.6 percent in the same period. The gap between the numbers of unemployed people in the different regions of the country has widened. The southern governorate of Aqaba recorded the highest unemployment ate at about 20.3 percent while the lowest rate







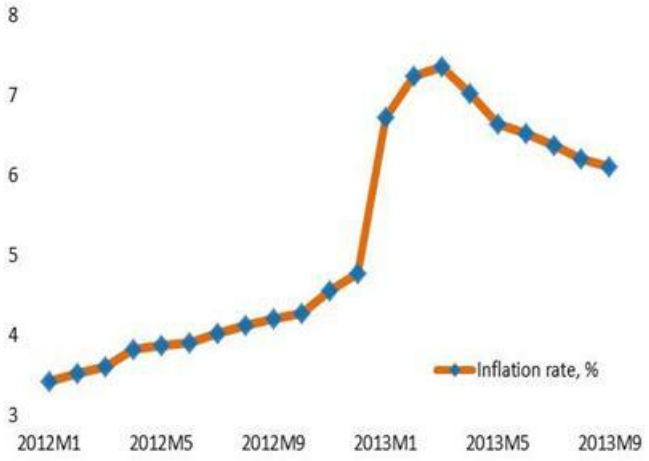
Source: National official sources

was recorded in Zarqa Governorate at 9.8 percent. There are signs that expansion in the GCC countries is helping to support overseas demand for skilled Jordanian workers, which could reduce some of the pressure on the domestic labor market in the short-term.

Inflation data from the Central Bank of Jordan (CBJ) show a declining trend in the monthly inflation rate. After peaking at 7.3 percent in March of 2013, the inflation rate declined to 6.1 percent in September 2013. The government's policy to liberalize fuel prices in November 2012 was a major contributor to the high inflation rate. Increases in electricity tariffs, which have targeted only large consumers of energy, have had minimal impact on prices. This forms part of a program to rein in losses at the National Electric Power Company (Nepco)—which have been made worse by the need to substitute fuel oil for Egyptian gas. The World Bank estimates that inflation will hover at around 5 percent in 2013 before falling to 4 percent in 2014.

On a positive note, foreign direct investment picked up in the first half of 2013. FDI inflows in the first six months of 2013 totaled about $1 billion, an increase of 34 percent compared to the same period last year, but it remains to be seen whether it will be sustained. Preliminary estimates from the World Bank shows that FDI could rebound to its pre-crisis level of about $2.5 billion in 2014 which shows an increase of 13 and 24 percent in 2013 and 2014 respectively compared to the 2012 level.

Overdue structural reforms, including streamlining business regulations, removing labor market rigidities, and improving the efficiency of public spending, are needed for macroeconomic stability. As yet, political and security matters have taken precedence, and economic reforms have not received sufficient attention.



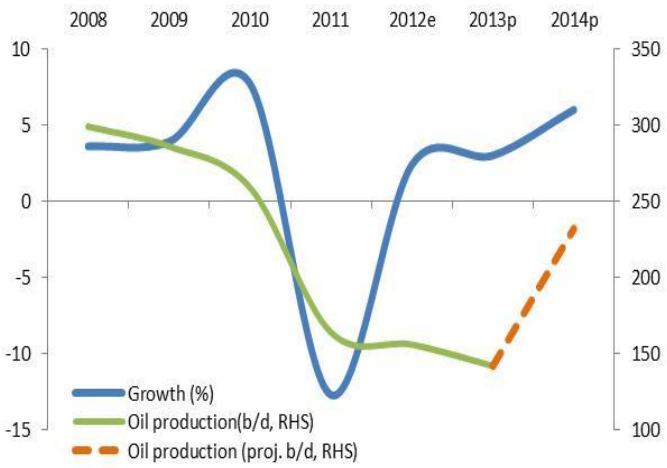
Source: World Bank.

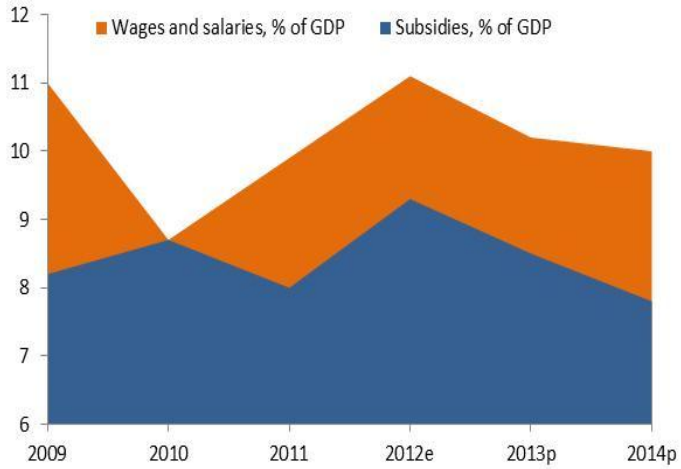
Yemen

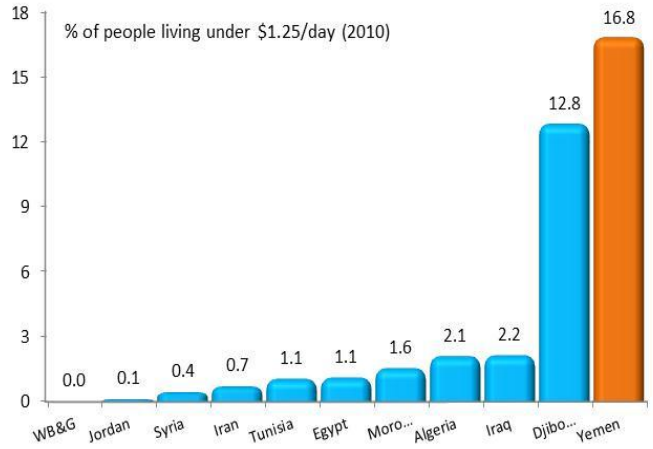
Economic growth is recovering slowly from the sharp slowdown in the aftermath of the 2011 revolution. Prior to the revolution, growth was at 8 percent (2010) as a result of increases in LNG exports, but in 2011 the economy shrank substantially and growth contracted by 13 percent. The rebound in 2012 was a result of improvement in economic activity in the major sectors of the economy, manufacturing, agriculture and trade. However, oil production, contributing to 30 percent of GDP and more than 75 percent of the government budget, is still below pre-revolutionary levels, due to frequent attacks on the energy infrastructure and oil fields. The World Bank estimates that growth could improve to 6 percent in 2014, helped by growth in non-oil sectors as well as donor funds. Oil production is also expected to rebound in 2014, if the political stalemate, violence, and insurgencies on oil fields subside, but will remain substantially below the pre-crisis level of about 400,000 barrels a day.

Unemployment in Yemen is the highest in the MENA region. Official estimates point to the unemployment rate of 17 percent in 2010 with over 54 percent for females and 12 percent for males. This rate has remained high for young people, reaching 60 percent, and is expected to have increased in the aftermath of the revolution. The situation has been worsened by the deportation of Yemenis working illegally in the Gulf, particularly Saudi Arabia. Official data show that, out of 2 million Yemenis working in Saudi Arabia, a total of about 700,000 will be deported in the coming months (200,000 have already arrived back in Yemen). The deportation is expected to exacerbate the already tough situation in the Yemeni's labor market and lower considerably the inflow of remittances to Yemen, which were about 10 percent of GDP before the revolution.

Yemen also has the highest poverty rate in the MENA region. The percentage of people living





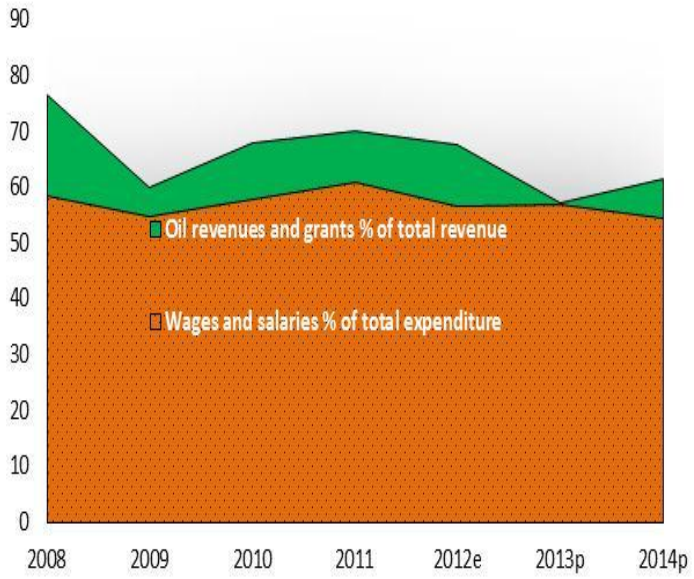


Source: National official sources.

under $1.25 a day has increased since 1998, from about 13 percent to 17 percent in 2010. Almost half of the population lived under the $2.00 a day rate in 2010. Estimates show that poverty worsened after the 2011 revolution, as a result of mismanagement of the economy, weakening of political unity, displacement of Yemenis due to internal fighting and also increasing refugees escaping crises in neighboring countries. Estimates by the United Nations reveal that about half of the population in Yemen is in need of humanitarian assistance.

The Yemeni government budget is extremely vulnerable and the high fiscal deficit is one of the main problems facing the economy. Oil revenues dominate fiscal revenues; subsidies and wages dominate government spending, leaving little room for capital spending. While oil revenues are expected to decline due to violence in the oil fields, spending on wages and subsidies continues to rise. Wages, standing at 8.7 percent of GDP in 2010, increased to about 11 percent of GDP in 2012, following the government's decision to increase wages in 2011 in response to demonstrations and mounting social tensions. Subsidies reached 9 percent of GDP in 2012, but have declined from their peak of 14 percent registered in 2008. In contrast, capital expenditures continue to suffer—declining from about 5 percent of GDP before the crisis to about 2 to 3 percent of GDP in 2011 and 2012.

There are major challenges to the outlook. The slow recovery is still at an early stage and could be weakened by the continued sabotage of key oil pipelines that curtail production. The government's fiscal position is deteriorating despite large grants, and near- and medium-term financing needs are great. The large share of wages and generalized energy subsidies in the budget constrains space for pro-poor and pro-growth expenditures. Unemployment is expected to remain very high, especially among the youth, and poverty and malnutrition are



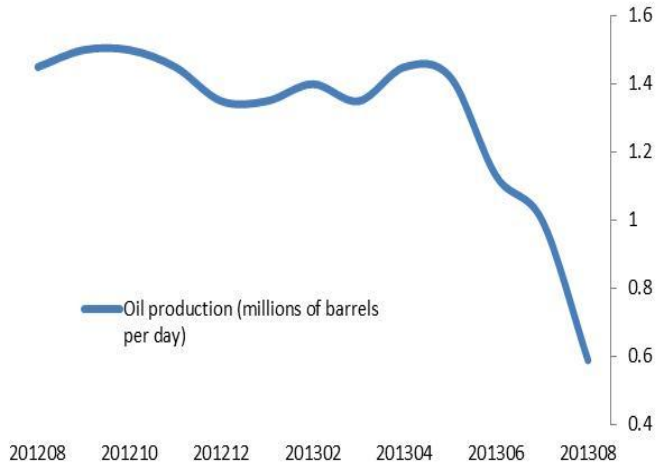
Source: World Bank and national official sources.

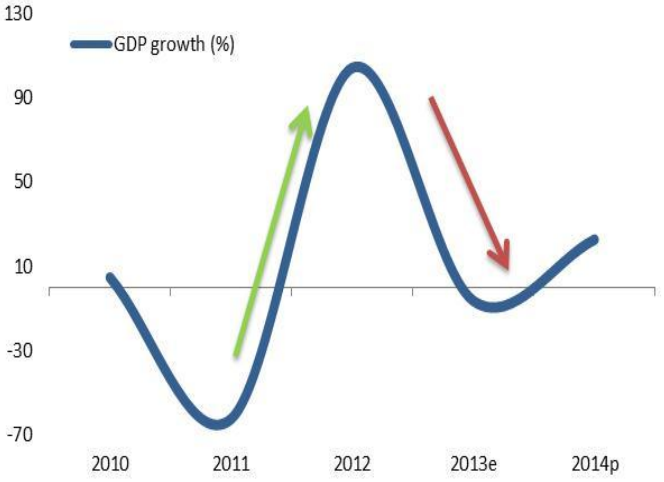
widespread. Serious environmental challenges, including the rapid extraction of ground water, pose economic and social risks to an already fragile recovery.

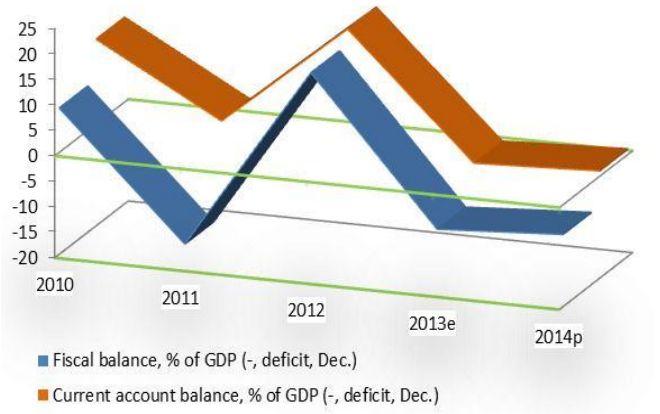
Libya

Economic growth in Libya is once again dipping into negative territory. After the sharp decrease of 62 percent in 2011, GDP rebounded sharply and growth reached 104 percent in 2012 as a result of massive oil production. But the recovery stalled in 2013 as the oil sector, the major contributor to growth and government revenue (accounting for about 70 percent of GDP and 95 percent of revenue) has been crippled by prolonged strikes at key oil terminals and loading ports since July, removing more than 1 million barrels per day (b/d) of crude oil production from exports. Militia blockages of oil production and export facilities along with strikes by oil workers, tribesmen and other protesters at oilfields across the country, have cut oil production to 224,000 b/d in early December from more than 1.4 million b/d in June and 1.6 million during the pre-revolutionary period.

Fiscal and current account balances have deteriorated sharply due to the oil blockade that has reduced oil revenue by 80 percent and also to continued expansionary fiscal policy. In September 2013, the government announced a 20 percent increase in salaries for public-sector workers and issued a separate decision to raise the wages of Judicial Council staff. The World Bank has revised its estimates for the fiscal stance of the government in 2013 and 2014. It is expected that the fiscal surplus of 2012 will turn into a deficit of about 5 percent of GDP for 2013 and 4 percent of GDP for 2014 respectively. The large current account surplus is also expected to fall sharply and reach near zero in 2013 and recover only slightly in 2014. Under the current situation, the government has had to dig deeper into its large stock of foreign reserves, which stood at $124 billion at end 2012, to finance its budget deficits in 2013 and 2014 (between $10 and $13 billion have already been used in 2013).



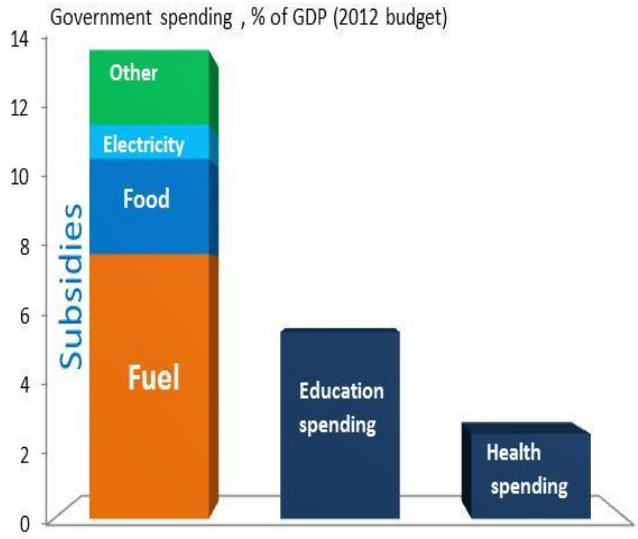




Source: World Bank.

Libya's labor market is skewed toward the public sector, which employs more than 80 percent of the formal workforce, while the private sector employs just 4 percent of Libyans. Furthermore, attractive wages and benefits offered by the public sector have resulted in high wage expectations among job seekers and university graduates. As a result, the unemployment rate has remained high across the board, though official estimates show a decline in the figures post 2011 revolution. Data released from the Ministry of Labor in September 2013 show that the unemployment rate has improved to 15 percent in 2013 from its high level of about 20 percent in 2010 and 2011. But unofficial estimates suggest that the actual figure is closer to 30 percent with higher rates for the youth. World Bank estimates show that youth unemployment has remained at about 50 percent with the majority of unemployed holding university degrees.

There are major challenges facing the Libyan economy which, if not addressed, could hamper the prospects of a growth rebound. First is the management of Libya's petroleum resources and the urgent need for economic diversification in order to ensure long-term financial and economic stability and Libya's unemployment challenge. Despite its large contribution to GDP, the oil and gas sector is highly capital intensive and contributes to less than 2 percent of total employment (according to the latest data). Second is streamlining general subsidies (estimated at 11 percent of GDP in 2013) and public-sector wages that impose fiscal pressures on the government. Subsidies are high and reduce the fiscal space available for spending priorities on health, education and investment in infrastructure. Third is the challenge of addressing skills mismatches and reforms to generate a vibrant private sector. In particular, the lack of access to financing, uncertainty in the legal environment and a fragile security situation are preventing private sector growth.



Source: World Bank and IMF.