Introduction: Regional events continue to affect the short-term economic prospects in the Middle East and North Africa (MENA), while major developments in the global economy over the past six months have put the region on a two-track growth path for 2012. These developments include a significant rise in crude oil prices on fears of oil supply disruptions and weak economic activity in the Eurozone.

Strong Growth in the Oil Exporting Economies: Economic growth of MENA’s oil exporting countries will be strong as it rebounds from the average of 3.4 percent in 2011 to 5.4 percent in 2012. In contrast, oil importers in the region will grow at about half that rate, although the pace of economic expansion will accelerate slightly relative to 2011. Overall growth in the region is expected to be 4.8 percent in 2012, surpassing the 3 percent growth achieved in 2011.
Improvement in the growth prospects of oil exporters is due to strength in oil markets. Crude oil prices have been buoyed on the supply side by fears of oil supply disruptions and on the demand side by a pickup in economic activity in the US as well as the shift away from nuclear energy in Japan. Oil exporters with available capacity will expand output, while buoyant oil revenues will finance additional public spending expected to boost domestic demand and investment. If sustained, high oil prices will enlarge oil exporters’ fiscal space, although not necessarily translate into increased fiscal surpluses. Many of the oil exporting economies will choose to scale up social programs; however, Iran, Syria and Yemen will be constrained by a difficult economic and political environment.

**Figure 3 – Fiscal Outlook (Percent of GDP)**

Subdued Growth in the Oil Importing Economies: Oil importers, especially those recovering from political turbulence, remain in vulnerable positions with widening risk premia, diminished foreign reserves and increasing difficulty financing fiscal and current account deficits. Furthermore, net oil importers will be affected negatively by high oil prices, and those with strong EU links will be impacted by the weak growth expected in the Eurozone. Still, oil importers with GCC links will benefit from strong growth in the GCC group of countries through trade, investment and remittances.

Domestic and regional factors will also play a role and shape country-specific outlooks. In Egypt and Tunisia, the pace of recovery and its sustainability will depend largely on domestic political developments, while in Morocco growth will moderate due to an expected decline in agricultural production. Economic activity in Lebanon could be hurt through the trade channel if the situation in Syria deteriorates, while the situation in Jordan will reflect the ability of the government to convince investors of economic stability.

**Figure 4**

**Industrial Production in Oil Importers**

The fiscal situation is expected to remain tenuous for oil importing countries, especially those going through transitions. In Tunisia, the fiscal deficit will worsen as a result of the expected increase in public expenditures envisaged in the new supplementary budget law, expanding social spending and public investment. In Egypt, the fiscal deficit in 2012 is unlikely to increase relative to 2011, but it is expected to exceed the budgeted target for the fiscal year 2012, due to increased public spending, especially on wages and social benefits, and a revenue shortfall as a result of economic weakness.

Overall, inflation is expected to remain subdued in 2012, with the notable exceptions of Iran and Egypt. Subsidies are currently dampening the effects of increased global food and energy prices in many MENA countries. However, the
pass-through from global to domestic food prices has been sizable in some MENA countries over time, and increases in wages and salaries, could stoke inflationary pressure in the medium-run.

The macroeconomic outlook remains highly uncertain and is contingent on political developments in the region and beyond. While political transitions and economic challenges remain and continue to cloud the short-term growth prospects in parts of the region, external downside risks also alter the regional macroeconomic outlook. These include volatility in oil markets, a deeper than expected slowdown in Europe, and potentially weaker growth in the US and developing countries.

**Conclusion:** In sum, growth in MENA will rebound and approach 4.8 percent in 2012, rising about 2 percentage points relative to growth in 2011. This aggregate outcome however hides a two-track growth forecast. Oil exporters will grow much faster relative to oil importers and relative to 2011, provided oil prices remain strong. Oil importers, especially those recovering after political turbulence, remain in vulnerable positions and will grow at half the pace registered by oil exporters. Risks are multiple and reflect the heterogeneous domestic conditions across MENA, especially in the oil importers and in the global economy.

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