Qatar Economic Insight

September 2018

Executive Summary

Qatar's economic performance remains resilient. Despite the blockade imposed by some of its neighbours, the economy grew by 1.6% in 2017. Lower output in the hydrocarbon sector due to the 'OPEC+' deal and LNG maintenance work were the main headwinds to growth. Non-hydrocarbon GDP growth was a solid 3.8% in 2017.

Reflecting recent strength, our oil price forecasts are revised up to USD72/b in 2018 and USD69/b in 2019 (previously USD69/b and USD66/b). Strong global demand and various supply disruptions will keep prices firm heading well into 2019 before slowing global GDP growth and increased US shale supply damp prices somewhat.

GDP growth is forecast to gain by a solid 2.6% in 2018 as the drag from the hydrocarbon sector abates and the booming construction sector drives non-hydrocarbon growth. Government policies to promote private-sector development are also lifting domestic demand. We target non-hydrocarbon GDP growth of 5% in 2018, rising to 5.3% in 2019. Overall GDP growth of 3.2% is seen at 2019.

External finances will be robust. The current account surplus should approach 9% of GDP in 2018: an improvement of around 4% of GDP in 2017 before subsiding to around 7% of GDP in 2019 as oils prices slip. Import growth is expected to remain moderate.

Helped by higher hydrocarbon prices, government finances are expected to steadily improve with the budget seen in broad balance in 2018 before a larger surplus emerges in 2019. The introduction of VAT in 2019 will lift revenues and help diversify the tax base.

Reflecting deflation in rental prices and slower food inflation, overall CPI inflation is expected to remain damped until the anticipated introduction of VAT boosts inflation in 2019. We target average CPI inflation of 0.5% in 2018, rising to 1.9% in 2019.

Qatar's banking system remains healthy with ample liquidity, high asset quality and strong capitalisation. Deposit of 6% and loan growth of 5% is expected this year, which should result in a further decline in the loan-to-deposit ratio.

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Background

Qatar is endowed with the largest hydrocarbon reserves per capita in the world…

Qatar is endowed with major hydrocarbon reserves, especially in relation to the size of its population. Nearly all of its gas reserves are contained in an offshore gas field called the North Field which is the largest, single natural gas deposit in the world. Combining Qatar's reserves of gas, crude oil and condensates equated to 172bn barrels of oil equivalent (boe) in 2017. This corresponds to 62.8k boe per capita (Chart 1): easily the highest in the world.

…leaving it the world's largest LNG exporter and the world's richest country in terms of GDP per capita

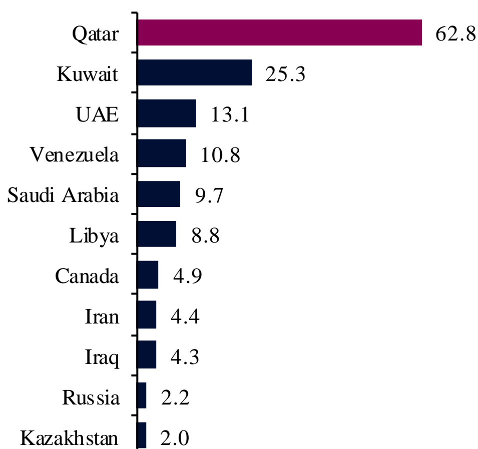
Qatar invested heavily in liquefied natural gas (LNG) in the early 1990s. The sector experienced rapid growth, particularly through continued investment in the first decade of the 2000s. Qatar has pioneered investments in LNG production with western partners and, as a result has become the world's top LNG exporter and the second largest gas exporter (after Russia if pipeline exports are included). The development of the hydrocarbon sector, in turn, has made Qatar the richest country in the world with GDP per capita standing at USD124.5k in purchasing power parity (PPP) terms in 2017 (Chart 2).

Qatar National Vision 2030 aims to transform the economy into a knowledge based economy

In 2005, the authorities imposed a moratorium on further development in the North Field. The hydrocarbon phase of development then plateaued in 2011 with the completion of most projects. Since 2011, the priority has been rising investment into the non-hydrocarbon sector in order to build the infrastructure needed to realise Qatar's National Vision (QNV 2030), which aims to transform Qatar into a knowledge-based economy by 2030 (Chart 3).

Chart 1: Oil and Gas Reserves Per Capita (2017)

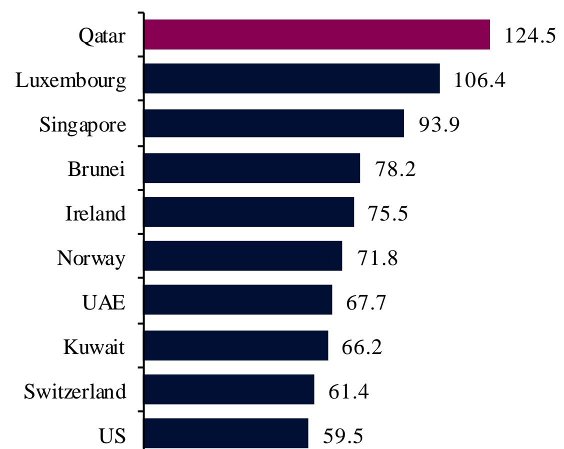
(k boe)



Source: BP, International Monetary Fund (IMF), QNB Economics

Chart 2: Real GDP Per Capita (2017)

(k USD, PPP terms)



Source: IMF, Haver Analytics, QNB Economics

Qatar's economic diversification is well advanced with the non-hydrocarbon sector's...

To that end, Qatar is using its significant hydrocarbon surpluses to undertake a major programme of infrastructure investments. Project spending, needed for the long-term development of the country and also to meet the deadlines ahead of the FIFA World Cup in 2022, has attracted a large influx of expatriate workers. Taken together, investment spending and population growth have boosted domestic demand and growth in the non-hydrocarbon sector allowing the economy to steadily diversify away from oil and gas.

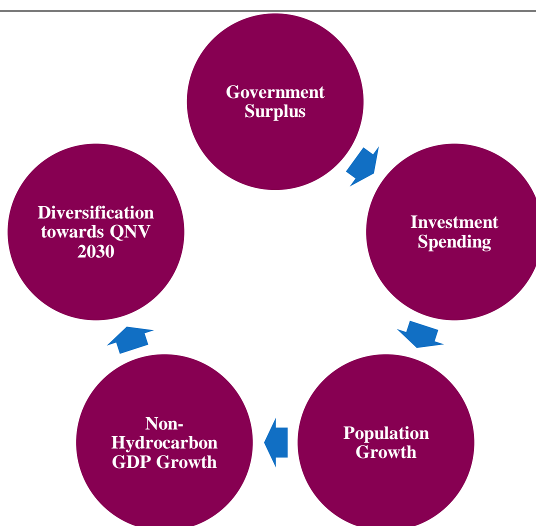
...share of overall GDP rising to just over 50% of GDP in recent years

GDP data already show Qatar's success in spurring economic diversification. While the economy has grown by a cumulative 22% between 2011 and 2017, the share of hydrocarbon GDP has declined from 60.1% (2011) to 48.2% (2017) as non-hydrocarbon GDP has grown significantly faster led by the manufacturing, construction and finance and insurance sectors (Chart 4).

End of the moratorium on North Field development will help power the next phase of Qatar's growth from 2020 onwards

Looking into the next decade, Qatar is expected to continue to grow via attracting, developing and retaining talent. The announcement last year that the moratorium on North Field development will be lifted with LNG output to rise by 30% by 2024 will also rekindle the expansion of the hydrocarbon sector driving another new phase of Qatar's development (see GDP section for more details).

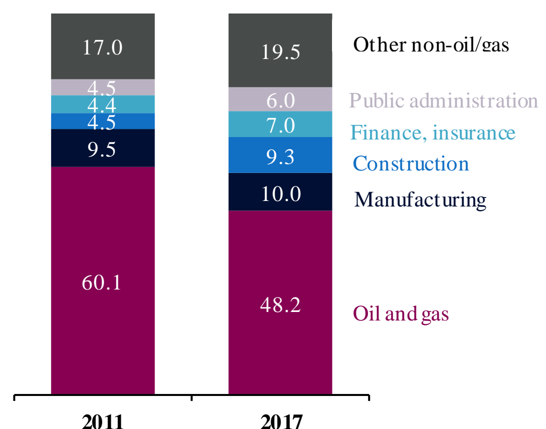
Chart 3: Qatar's Diversification Strategy



Source: QNB Economics

Chart 4: Real GDP Composition

(%)



Source: MDPS, Haver Analytics, QNB Economics

Oil prices increased significantly in 2017 and 2018

Brent crude oil prices were up a further 30% y/y in 2018H1…

Background: In 2017, Brent crude prices averaged USD55/b, up from USD44/b in 2016. And the oil price's recovery has continued in 2018. In the first six months of the year, Brent crude averaged USD71/b; an increase of 30% versus 2017's average.

Supported by robust global demand as global GDP growth reaches its fastest since 2011 …

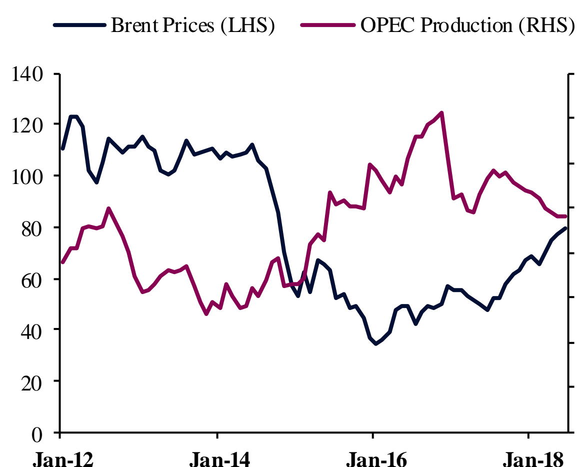
A number of factors have pushed oil prices up more than expected this year. First, with global GDP growth on course for its strongest year since 2011, oil demand growth has been robust. The International Energy Agency (IEA) estimates global demand to increase by 1.5 million barrels per day (m b/d) in 2018.

…and collapsing Venezuelan output which has exacerbated OPEC supply restraint

On the supply side, three factors have been key so far in 2018. The first factor is **continued steep falls in Venezuelan output**, down a further 320m b/d in the first six months of the year, as the country's economic crisis deepens. Second, the **re-introduction of US sanctions on Iran**, threatens to tighten supply further from November 2018 by removing up to 900m b/d of global supply. The spot oil price moved up on the news, reflecting the risk of a further large supply shock later in the year. However, the extent to which key importers such as China and India will comply with the sanctions and so fully cut off Iranian imports is unclear. Moreover, it is anticipated that KSA and Russia can also step up production further in the short-term to help fill the void.

Chart 5: OPEC Crude Output vs. Brent Crude Oil Price

(USD/b, LHS), (m b/d, RHS)



Source: Bloomberg, QNB Economics

Chart 6: Brent Crude Oil Price

(USD/b)

Source: Bloomberg, QNB Economics

Third, **infrastructure bottlenecks in the key US shale oil producing of the Permian Basin** region in west Texas threatens to restrain US supply growth. Pipeline capacity from the Permian is already close to full by most accounts with new capacity not expected to properly arrive until 2019Q3. A jump in 'drilled but uncompleted wells' in the Permian (a key gauge of delayed output for shale producers) points to slowing supply growth in the short term as producers delay output until takeaway capacity is boosted.

QNB's oil price forecasts revised up to an average of USD 72/b in 2018 & USD69/b in 2019

In response to the market's increasing tightness and the rising risk of further supply disruptions in the balance of 2018, OPEC and Russia agreed at the end of June to return the bloc's aggregate production back to the original targets agreed in late 2016, effectively lifting production by around 1m b/d in the second half of 2018. Production increases will be led by Saudi Arabia and Russia: the two producers with the greatest margin of spare capacity. The latest data show these two countries were lifting output in June ahead of the deal.

Outlook: As a result of the recent strength in oil prices, **we have revised up our forecasts for average annual oil prices to USD72/b for 2018 from USD69/b and to USD69/b in 2019 from USD66/b** (Chart 6). Both demand and supply factors however suggest a tilt towards lower prices in 2019 as global demand cools and infrastructure constraints on US shale supply fade.

Early signs of slower global GDP growth and the mounting risk of a trade war point to softer demand growth in 2019

On the demand front, global growth is set to soften. The euro-zone, Japan and China have all shown signs of slower growth in recent months, while the US Federal Reserve looks set to continue its steady drip-feed of interest-rate rises until US GDP growth, currently booming at a 4% annualised pace, pulls back to a more sustainable 2% annualised clip.

The mounting risk of a global trade war, with an escalating conflict between US and China in particular looking increasingly likely, adds to downside risks. Investment intentions in particular are likely to suffer from the increased uncertainty. In turn, risks to the IEA's forecast for a second successive year of oil demand growth of 1.4m b/d looks tilted to the downside.

Increased pipeline capacity in the Permian Basin should be in place by 2019H2

On the supply side, US shale output should re-accelerate with the increase in pipeline capacity from the Permian Basin in 2019Q3. US crude exports, which were 1.6m b/d in 2017 and are currently being capped around the 2m b/d by infrastructure constraints could reach 3 m b/d by end-2019. OPEC's output deal is also set to expire at the end of 2018 and, while some extension of production curbs is likely, the clear risk is that OPEC supply increases in 2019.

Led by the non-hydrocarbon sector, the economy was resilient in 2017

GDP growth to remain resilient, accelerating to 3.2% in 2019

Qatar's economic performance remains resilient. Despite the economic blockade imposed by some of its neighbours, the economy grew by 1.6% in 2017. An important drag on growth was the hydrocarbon sector, which contracted by 0.7% as a result of OPEC output cuts and maintenance on LNG trains (Chart 7). Growth in the non-hydrocarbon sector slowed from a buoyant 5.3% to a still-solid 3.8%, proving resilient to the temporary disruption by the economic blockade on Qatar by some of its neighbours.

The construction sector, which is worth over 20% of non-hydrocarbon GDP, remains the key growth driver

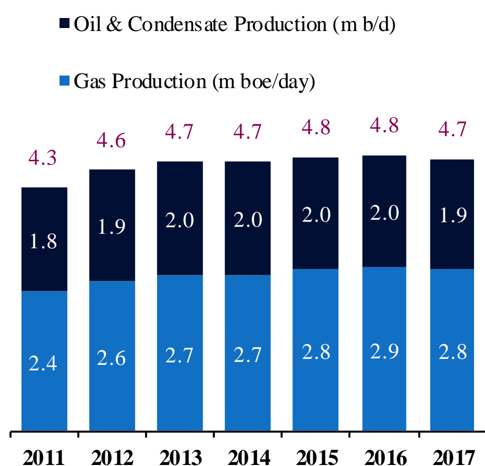
Construction, which accounts for 21% of non-hydrocarbon output, remained the key growth driver. Construction output was up 17.5% in 2017, supported by key infrastructure projects related to Qatar's Vision 2030 and also the 2022 World Cup. The construction sector's buoyancy has continued so far in 2018 with the latest data showing output up 17.2% y/y in the first quarter.

There are encouraging signs of acceleration in the manufacturing and logistics sectors as government policies start to bear fruit

Growth in the manufacturing sector, which accounts for a further 19.5% of non-hydrocarbon GDP, recovered to 1% as projects aimed at greater self-sufficiency and food security start to take effect. Their impact can be seen more clearly in recent quarters with manufacturing output growth up 3% y/y in 2018Q1. Total non-hydrocarbon GDP growth was a robust 4.9% y/y in 2018Q1, starting the year on a strong footing.

Chart 7: Hydrocarbon Production

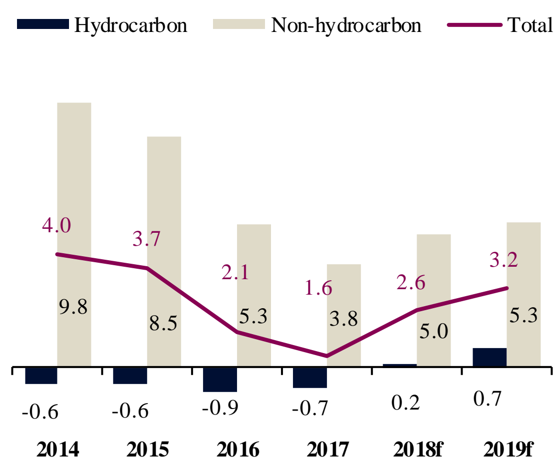
(*m boe/day*)



Source: BP, QNB Economics

Chart 8: Real GDP Growth

(%, y/y)



Source: MDPS, Haver Analytics, QNB Economics forecasts

Outlook: For 2018 as a whole, GDP growth is forecast to improve to 2.6% from 2017's 1.6% out-turn (Chart 8). On the hydrocarbon side, modest growth of 0.2% is anticipated, which would end four years of declines. The lifting of OPEC production cuts should modestly boost crude oil production, while the end of maintenance work and temporary shutdowns should start to spur a recovery in LNG output through the year. A further pick up of 0.7% in hydrocarbon output is then expected in 2019.

Non-hydrocarbon GDP is expected to gain by 5.0% in 2018

Non-hydrocarbon GDP is expected to gain by 5.0% in 2018. Continued infrastructure spending as the government focuses on completing major projects in key sectors will ensure that construction remains the backbone of the non-hydrocarbon sector with forecast growth of 15.5%. Higher oil prices will also allow for some positive multiplier effects on domestic demand.

Government policies aimed at strengthening the private sector and boosting self-sufficiency and food security will support demand growth

Government policies aimed at strengthening the private sector and boosting self-sufficiency and food security will also support demand growth. Agriculture (8.2% growth), manufacturing (3.2% growth), transportation and storage (3% growth) are expected to be the key beneficiaries with growth in these sectors expected to pick up further in 2019. Continued population growth, with mid-year population expected to hit a record 2.81 million in 2018 then rising further to 2.89 million in 2019, will also work to spur additional domestic demand. **For 2019 as a whole, we forecast non-hydrocarbon GDP growth of 5.3%, leaving overall GDP growth at 3.2%.**

From 2019 onwards, the decision to increase LNG output by 30% by 2024 will drive Qatar's next development phase

From 2019 onwards, **the decision to increase LNG output by 30% by 2024 will increasingly drive Qatar's next development phase** as the current multi-year wave of infrastructure spending begins to flatten out in terms of growth contribution. The 30% increase will boost Qatar's LNG capacity from 77 million tonnes currently to 100 million tonnes by 2024. This increase in capacity will require huge investments both onshore and offshore including the construction of three new LNG trains to process the gas. Beyond the direct impact on non-hydrocarbon GDP, this new investment phase, which should begin in earnest from 2020 onwards, will generate substantial multiplier effects on the wider economy, lifting demand for goods and services and driving the country's development in line with the Qatar National Vision 2030.

Recovery in hydrocarbon prices has seen the current account swing back into surplus

Higher hydrocarbon prices drive current account surpluses

Background: The current account returned to a surplus of 3.8% of GDP in 2017 on the back of higher energy prices. Exports saw robust growth of 17.5% reflecting the continued recovery in the oil price and booming LNG demand, particularly from China. Imports, meanwhile, were broadly flat for the year as a whole. The economic blockade by some of Qatar's neighbours produced a temporary disruption to trade but imports quickly bounced back to above pre-blockade levels as trade flows have been successfully re-routed. Imports from Turkey in particular have jumped and continue to show strong growth so far in 2018 (Chart 9)

Outlook: **Qatar's current account surplus is expected to rise further to close to 9% of GDP in 2018; an increase of around 5% of GDP**. Buoyant exports will remain the key driver. With oil prices expected to average USD72/b and LNG demand growth in Asia remaining vibrant, hydrocarbon exports should sustain strong growth. On the import side, the expected pick-up in non-hydrocarbon GDP growth should see moderate growth resume reflecting the twin drivers of steady population increase and continued investment spending. Government policies to promote self-sufficiency and food security will however help cap overall import growth.

For 2019, the current account surplus is expected to narrow back towards 7% of GDP as slightly lower oil prices crimp export revenues and moderate import growth continues.

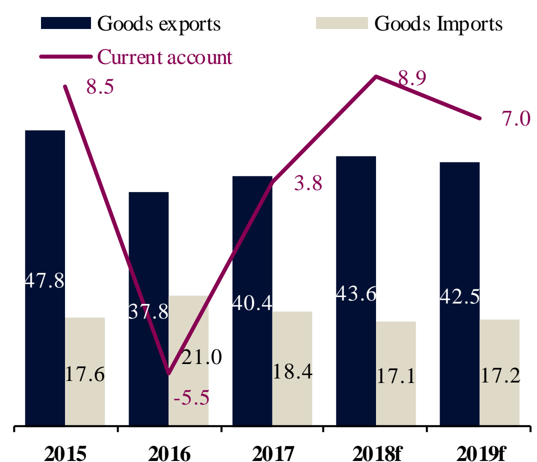
Chart 9: Qatar Imports From Turkey

(*USD bn, 12-month sum*)

Source: IMF, Haver Analytics, QNB Economics

Chart 10: Qatar External Balances

(*% of GDP*)



Source: QCB, Haver Analytics, QNB Economics forecasts

Government budget balance to move into surplus

Helped by higher hydrocarbon prices and spending restraint, budget expected to steadily improve

Background: The fiscal deficit narrowed to 1.6% of GDP in 2017 from 4.7% in 2016. The fall reflected government expenditure restraints in the face of slowing revenue growth.

Qatar's Ministry of Finance data shows that total expenditure slipped by 2% in 2017 versus 2016. Importantly, capital spending on major projects was sustained with growth of 2.6% last year. Revenues meanwhile grew by 9.0% in 2017 helped by the increase in hydrocarbon prices.

Budget seen in broad balance in 2018 followed by a return to healthy surplus in 2019

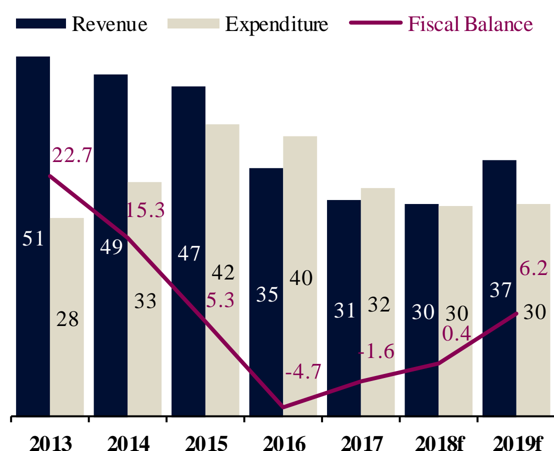
Outlook: **The budget is expected to improve further and be close to broad balance in 2018 before a return to a healthy surplus in 2019** (Chart 11). On the expenditure side, spending is expected to show modest overall y/y growth in 2018 as restraint in current spending continues and, as Capex spending on large infrastructure projects and the 2022 World Cup starts to flatten out. 2019's more relaxed climate should then allow for some pick up in current spending and increased transfers, such as to QIA or debt repayments, as the surplus grows.

Expected introduction of VAT will lift revenues in 2019 and help diversify tax base

On the revenue side, growth rates will be lifted by higher hydrocarbon revenues as the full benefit of the doubling of crude prices from June 2016's level is felt and the partial lifting of OPEC output caps spurs the modest output gains embedded in our GDP forecast. The expected introduction of VAT in 2019 will boost revenues by around 1¼% of GDP, helping diversify and reduce volatility in government revenues.

Chart 11: Fiscal Balances

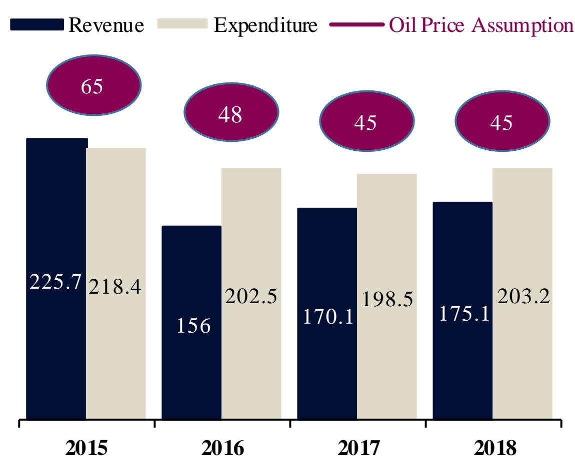
(% of GDP)



Source: IMF, Haver Analytics, QNB Economics forecasts

Chart 12: Budget & Oil Price Assumptions

(QAR bn, oil price in USD/b)



Source: Ministry of Finance

Damped headline CPI inflation reflects the interplay of a number of cross currents

Headline inflation to remain damped until VAT boost

Background: Over the last year, CPI inflation has been buffeted by a number of cross currents with a now ebbing spike in food inflation (12.6% of the CPI basket) and higher energy costs (6.1% of the CPI) militating against rental deflation (a 21.9% weight). The net result has been to leave headline inflation muted (Chart13).

Food inflation shock now fading

The increased short-term costs associated with the blockade, such as setting up new trade routes and importing food from outside the region saw domestic food prices temporarily spike higher. Food inflation jumped from -1.9% y/y in May 2017 to a peak of 5.8% y/y in January 2018 before subsiding to zero in June as the shock washes out.

Clear signs that real estate deflation is easing in 2018H1

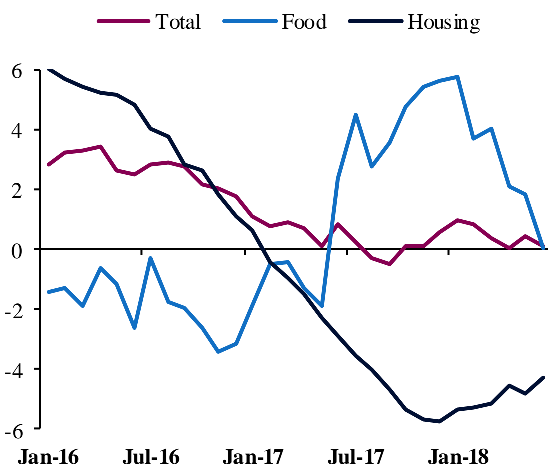
Meanwhile, transportation costs have risen in line with higher crude oil prices as the authorities now adjust petrol prices on a monthly basis. The other dominant feature of the CPI basket is lower rents, which have been falling in y/y terms since February 2017. The latest data suggest however that deflationary pressure in real estate has peaked. Housing inflation improved to -4.2% y/y in June versus a low of -5.8% y/y seen at the end of 2017.

VAT is expected to add around 2.5pp to y/y inflation from 2019Q2

Outlook: Headline inflation will remain muted in the balance of 2018. Inflation is expected to average of 0.5% for the year as a whole; little changed from 2017's average. Significantly higher inflation awaits 2019, when the expected introduction of VAT by Q2, at a rate of 5%, mainly on clothes, other durable goods and non-essential services

Chart 13: CPI Inflation

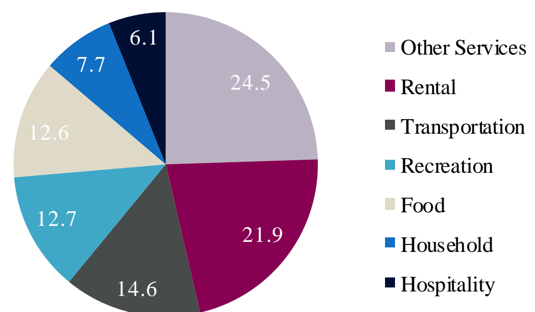
(% y/y)



Source: MDPS, Haver Analytics, QNB Economics

Chart 14: CPI Weights By Major Category

(% of total, 2017)



Source: MDPS, Haver Analytics, QNB Economics

such as restaurants, hotels as well as entertainment will temporarily add around 2.5pp to year-on-year CPI inflation lifting it to close to 3%.

QNB forecasts average CPI inflation of 0.5% in 2018 and 1.9% in 2019

From Q2 2020, annual CPI inflation will once again fall back as the VAT hike drops out of the annual comparison and with oil prices expected to slip back. **We forecast CPI inflation of 0.5% in 2018, rising to 1.9% in 2019**.

Banking system resilience with liquidity ample and asset quality and profitability high

Banking sector resilient and healthy

Background: Qatar's financial sector remains resilient and healthy with credit continuing to flow, liquidity ample and asset quality and profitability robust. Despite the economic blockade, deposit growth was a buoyant 13.2% in 2017 versus solid loan growth of 8.5%. With deposit growth outstripping loan growth, the system-wide loan-to-deposit ratio fell back to around 110% and the liquidity environment improved.

Public-sector deposit mobilization more than offset lower non-resident deposits in 2017

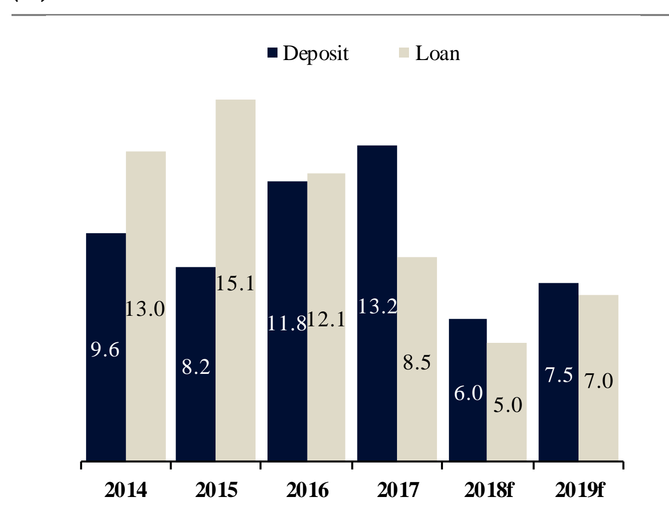
Timely intervention from the authorities supported the financial system's adjustment. Robust public-sector deposit mobilisation (up 69.6%) more than made up for the withdrawal of non-resident deposits from the blockading economies, underscoring the financial system's resilience. The funding structure of the banking sector also changed favourably in 2017 with the share of funded liabilities in long-term maturities rising to around 18% from around 11%.

Banking system remains well capitalized with high asset quality and profitability

Other indicators attest to the soundness of the financial system (see summary table below). The banking system remains well capitalized with banks' capital adequacy ratio (CAR) rising to 16.8% in 2017; up from 16.1% in 2016 and well above Basel III guidelines. Asset quality also remains high with non-performing loans (NPLs) steady at 1.7% of capital last year. Profitability remains solid with returns on equity (ROE) close to 14%.

Chart 15: Commercial Banks' Loan and Deposit Growth

(%)



Sources: QCB, Haver Analytics, QNB Economics forecasts

Table 1: Financial Soundness Indicators

(%)

Capital Adequacy	2015	2016	2017
Tier 1 capital/risk-weighted assets	15.2	15.7	16.5
Regulatory capital/risk-weighted assets	15.6	16.1	16.8
Asset Quality			
Non-performing loans/capital	1.9	1.7	1.7
Non-performing loans/total loans	1.6	1.3	1.6
Liquidity			
Liquid assets/total assets	28.5	29.6	28.2
Total loans/total deposits	112	114	109
Total loans/total assets	67.5	66.7	67.1
Profitability			
Return on assets	2.0	1.7	1.5
Return on equity	16.2	14.5	13.9

Sources: Qatar Central Bank (QCB), Haver Analytics, QNB Economics

Solid deposit and credit growth expected in 2018 and 2019

Outlook: Helped by higher hydrocarbon revenues, deposit growth of around 6% is expected in 2018, ticking higher to 7.5% in 2019. Solid loan growth of 5% is expected this year, firming to 7% in 2019 helped by higher credit demand in both the public and the private sector. Government policies targeted to strengthen the private sector and ongoing infrastructure projects will support credit demand. The loan-to-deposit ratio is expected to slip a little as deposit growth marginally outstrips loan growth (Chart 15).

Macroeconomic Indicators

	2012	2013	2014	2015	2016	2017	2018f	2019f
Real sector indicators								
Real GDP growth (%)	4.7	4.4	4.0	3.7	2.1	1.6	2.6	3.2
Hydrocarbon sector	1.2	0.1	-0.6	-0.6	-0.9	-0.7	0.2	0.7
Non-hydrocarbon sector	9.9	10.4	9.8	8.5	5.3	3.8	5.0	5.3
Nominal GDP (bn USD)	187	199	206	162	152	167	187	194
Growth(%)	11.4	6.4	3.8	-21.6	-6.2	10.0	12.3	3.5
Non-hydrocarbon sector (% of GDP)	42.0	44.3	47.5	62.5	70.3	67.7	65.0	67.8
GDP per capita (PPP, k USD)	147	143	136	130	125	125	134	134
Consumer price inflation (%)	1.9	3.1	3.3	1.9	2.7	0.4	0.5	1.9
Fiscal Indicators (% of GDP)								
Budget Balance	11.2	22.7	15.3	5.3	-4.7	-1.6	0.4	6.2
Revenue	42.2	51.0	48.7	46.8	35.2	30.7	30.3	36.5
Expenditure	31.0	28.3	33.4	41.5	39.9	32.4	29.9	30.3
Public debt	32.1	30.9	24.9	34.9	46.5	54.0	n.a.	n.a.
External sector (% of GDP)								
Current account balance	33.2	30.4	24.0	8.5	-5.5	3.8	8.9	7.0
Goods balance	54.7	51.3	46.3	30.2	16.7	22.0	26.5	25.4
Exports	71.2	67.1	61.4	47.8	37.8	40.4	43.6	42.5
Imports	16.5	15.8	15.1	17.6	21.0	18.4	17.1	17.2
International reserves (goods import cover)	12.5	9.0	8.7	6.6	8.8	9.8	10.0	9.7
External debt	50.7	49.3	48.6	73.8	110.9	88.0	86.7	82.7
Monetary indicators								
M2 growth	22.9	19.6	10.6	3.4	-4.6	21.3	n.a.	n.a.
QCB policy rate (end of period)	0.75	0.75	0.75	0.75	1.00	1.50	n.a.	n.a.
Interbank rate (%, 3 months, end of period)	1.1	1.1	1.5	2.5	2.0	2.5	n.a.	n.a.
Exchange rate USD/QAR (av)	3.64	3.64	3.64	3.64	3.64	3.64	3.64	3.64
Banking indicators (%)								
Return on equity	17.7	16.5	16.5	16.2	14.5	13.9	n.a.	n.a.
NPL ratio	1.7	1.9	1.7	1.6	1.3	1.6	n.a.	n.a.
Capital adequacy ratio	18.9	16.0	16.3	15.6	16.1	16.8	n.a.	n.a.
Deposit growth	26.0	19.7	9.6	8.2	11.8	13.2	6.0	7.5
Credit growth	26.0	13.1	13.0	15.1	12.1	8.5	5.0	7.0
Memorandum items								
Population (m)	1.83	2.00	2.22	2.44	2.62	2.72	2.81	2.89
Growth(%)	5.8	9.3	10.6	10.0	7.4	4.1	3.0	3.0
Oil and other liquids production ('000 bpd)	1931	1906	1886	1890	1899	1885	1888	1903
Average raw gas production (bn cf/d)	19.8	19.8	19.8	19.8	19.8	19.8	19.8	19.8
Average Brent crude oil price (USD/b)	111.6	108.6	99.0	52.4	43.5	54.2	72.0	69.0

Sources: BP, IMF, MDPS, QCB, Haver Analytics, QNB Economics forecasts

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