Healthy appetites

GRAHAM BUCK DELVES INTO A SURVEY THAT PREDICTS CONTINUING GLOBAL DEMAND FOR OIL WILL BUOY THE ECONOMIES OF THE GCC OVER THE YEARS AHEAD.

World demand for oil will continue to rise, pushing prices even higher over the decade ahead and underpinning the economic outlook for the Gulf Cooperation Council (GCC) countries, predicts Standard & Poor's.

The ratings agency believes that the GCC's prospects are now healthier than they were in the initial phase of the global financial crisis in 2008–09. This is due in part to the rising demand for oil from the emerging economies, says S&P, which predicts that global demand for oil will rise about 1.75% a year over the next decade. Improved energy efficiency in the developed markets will be partly offset by the growing number of vehicles in fast-growing emerging markets such as China and India.

Yet the growth in the world oil supply over the same period is likely to increase by only 1% a year, according to the International Energy Agency (IEA).

As the report notes, the supply and demand balance will be determined by two very different groups of producers. The first group, which includes Saudi Arabia, Kuwait, Iraq and the UAE, have oilfields with relatively low production costs. The second, which includes the US and Canada, rely on "unconventional" oil derived from sources such as shale, with significantly higher production costs and a still relatively small share of the total world oil supply.

This means that the large producers of the first group, in which the GCC countries alone account for 40% of proven global oil reserves, will maintain their influence on pricing.

S&P believes the Gulf will gain most from the rising demand for oil from emerging markets, where growth has slowed since mid-2010 but will gradually recover this year on the back of easier monetary policies. By contrast, GDP growth in the OECD economies will remain weak in 2012 and 2013 due to tight fiscal policies.

As a result, oil demand growth in both years will be mainly dominated by China, Brazil, India and Saudi Arabia, while demand from OECD countries will contract slightly. This will benefit the GCC economies, as more than 70% of their exports (essentially crude oil) are destined for Japan and the developing Asian countries.

This positive scenario promises to bolster current account surpluses in the GCC countries, which felt the impact of the sharp drop in oil prices at the onset of the financial crisis in 2008 but quickly recovered. Sharp increases in oil production to offset losses in Libya pushed GDP growth across the GCC to 7% in 2011; S&P expects the rate to be a still healthy 5% this year and 4% in 2013.

Although the rate of inflation will vary, with Saudi Arabia and Kuwait at the upper end of the range and the UAE and Qatar at the lower end, declining prices for commodities other than oil should keep inflation restrained at about 3%.

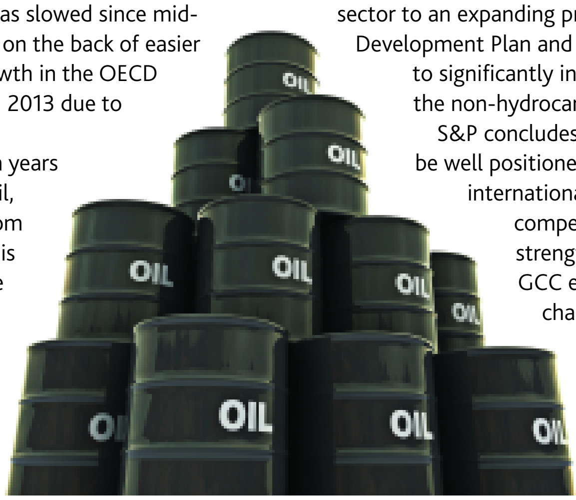
One feature of the oil sector is that it is more capital-intensive than labour-intensive, which makes economic diversification an imperative for GCC countries seeking to create more jobs. Over the past decade the GCC's population has grown by an average 4.2%, and 55% of the population is aged under 30.

Although unemployment data is scarce, Saudi Arabia's jobless rate reached 5.4% in 2009. This overall figure conceals a less reassuring picture: 10.5% of Saudi nationals were unemployed that year and 43.2% of Saudis aged below 24 were without a job. Figures for the UAE show a similar imbalance: the official unemployment rate of 4.2% divides between only 2.8% for non-nationals and 14% for nationals.

The report notes that the situation is complicated by the fact that nationals are principally employed in the public sector, while non-nationals work primarily in the private sector. About 90% of nationals in the UAE and 55% in Saudi Arabia work in the public sector, which generally offers superior wages and social benefits.

Most GCC governments aim to shift the workforce from the public sector to an expanding private non-oil sector. Both the Saudi Ninth Development Plan and Kuwait's Five-Year Development Plan aim to significantly increase the proportion of GDP derived from the non-hydrocarbons sector by 2014.

S&P concludes that the GCC economies will continue to be well positioned at a time when demand for funding on international debt markets becomes more competitive. However, it warns that these strengths should not lead to complacency: "The GCC economies face important demographic challenges… that can only be met through continuous efforts to diversify their structure away from hydrocarbons."



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