

# Bahrain Business Forecast Report Q2 2014

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## Abstracts

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### Core Views

We expect Bahrain's economy to expand at a moderate pace over 2014 and forecast real GDP growth of 3.4%, down from an estimated 4.3% in 2013. Business activity in the non-oil sector will be underpinned by elevated public spending and GCC aid, but will remain subject to political risk. Output gains in the hydrocarbon sector will be more limited than in 2013, weighing on the headline growth figure.

A return to pre-crisis rates of real GDP growth above 7% remains off the cards in the near term. In light of record oil revenues and the weakness of private investment, we expect public spending to outperform over the coming quarters, which should support activity in the non-hydrocarbon economy. Efforts to address the shortage of affordable housing will see government CAPEX accelerate.

Bahrain's reputation as a stable and welcoming location to do business in the Gulf has suffered as a result of the volatile political climate. At the moment, it remains to be seen if Manama will be able to compete with Doha and Dubai in attracting investment into the all-important hospitality and financial services industry.

The economy's medium-term outlook remains contingent upon a lasting solution being found to the current political crisis. Unfortunately, we maintain our relatively guarded outlook on the prospects that the government and opposition can come to some form of agreement in the near term. Bahrain's weak medium-term fiscal prospects will force the government to make difficult choices. We believe that Manama will have little option but to introduce new taxes over the coming years, while the issue of spending consolidation will loom large on the agenda. Support from Saudi Arabia could delay these pressures,

but would entail a significant loss of sovereignty.

### **Key Risks To Outlook**

A more pronounced regional crisis stemming from an uptick in tensions between Iran and the West could see risk premiums spike higher, particularly for Bahrain.

A marked drop in oil prices concomitant with a slowdown in growth in Europe, the US and China would pose a significant risk to the country's near-term growth outlook, and likely lead to a marked deterioration to the country's balance of payments and fiscal dynamics. In terms of the latter, Bahrain's breakeven oil price is now around US\$120/bbl, which is by far the highest in the Gulf. Failure to find a lasting solution to the political crisis could see the opposition becoming increasingly radicalised, and resort to militant tactics such as improvised explosive devices. This would result in Bahrain's 'safe haven' status suffering irreparable damage.

## Contents

Core Views

Key Risks To Outlook

### **CHAPTER 1: POLITICAL OUTLOOK**

SWOT Analysis

BMI Political Risk Ratings

Domestic Politics

End To Political Impasse Looking Ever More Distant the failure to make progress in national reconciliation talks between Bahrain's Sunni-dominated government and the Shi'a opposition leaves the regime with ever fewer options to end the country's political crisis. We retain our view that a breakthrough is unlikely over the year, with moderate figures on both sides now largely marginalised.

Table: POLITICAL OVERVIEW

Long-Term Political Outlook

Sun, Sea, And Sectarianism: Prospects For Future Stability Assessed

Bahrain's political future is complicated by growing tensions between the Sunni elite and the Shi'a majority, labour and population imbalances, the need to stay on side with both Iran and Saudi Arabia, and economic vulnerability. We believe the most likely long-term scenario is for democratisation to be brought about by political and economic necessity, although there is no guarantee that this would be peaceful.

### **CHAPTER 2: ECONOMIC OUTLOOK**

SWOT Analysis

BMI Economic Risk Ratings

Economic Activity

GCC-Financed Projects To Support Growth

We expect economic growth in Bahrain to be relatively robust over 2014, supported by GCC-financed infrastructure investments. We retain our forecast for real GDP growth of 3.4% this year, after an estimated 4.3% in 2013. However, output gains from the oil sector will be limited, while lower oil prices and the continuing political crisis present downside risks to growth.

Table: ECONOMIC ACTIVITY

Fiscal Policy

Difficult Fiscal Decisions Ahead

Bahrain's weak medium-term fiscal prospects will force the government to make difficult

choices. We believe that Manama will have little option but to introduce new taxes over the coming years, while the issue of spending consolidation will loom large on the agenda.

Support from Saudi Arabia could delay these pressures, but would entail a significant loss of sovereignty.

Table: FISCAL POLICY

Banking Sector

Banking Sector: On The Recovery Path

We see growth in the Bahraini commercial banking sector picking up slightly over 2014. We expect a number of public infrastructure projects to be initiated over the coming quarters, helping to widen banks' lending opportunities, while conditions in the real estate sector are improving. We forecast lending growth of 10.0% by the end of 2014, above the four-year average of 6.7% recorded in 2009-12.

Table: BANKING SECTOR OVERVIEW

Regional Outlook: GCC Subsidies

GCC Subsidies: Change At Last? the increasing willingness of officials from the Gulf Cooperation Council (GCC) to publicly criticise the region's long-established subsidy schemes represents a change in rhetoric, yet we note that few policy changes have so far been announced. Domestic political tensions will continue delaying the passage of reforms affecting nationals over the coming years, although the provision of subsidies to expatriate workers faces a more limited future. Reform will proceed first in Bahrain and Oman, given their more precarious fiscal positions.

Table: GCC – A CHANGING MENTALITY?

Table: OMAN GAS PRICES FOR INDUSTRIAL CONSUMERS

Table: GCC – INCENTIVES AND ROADBLOCKS TO SUBSIDY REFORM

Bahrain Q2 2014

Regional Outlook: Islamic Banking

Islamic Banking: New Markets To Emerge

We expect 2014 to be a key year for the global Islamic finance industry as several new markets come to the fore. It has been our longheld view that rather than becoming an integrated global financial system, Islamic banking will see the creation of regional hubs. Even with this slightly fragmented outlook, we still expect significant growth for the sector. That said, we think the impact of low base effects is beginning to wear off and we expect to see lower growth rates in the coming years.

Table: Islamic Bonds & Loans (2013)

## **CHAPTER 3: 10-YEAR FORECAST**

the Bahrain Economy to 2023

Assuming oil prices do not collapse and political stability is eventually restored,

Bahrain's economy will be able to post relatively moderate levels of real GDP growth over the coming decade. That said, the ongoing political crisis has raised a host of questions surrounding Bahrain's long-term outlook, with concerns growing that the country's financial services and tourism sectors will suffer heavily.

Table: Long-Term Macroeconomic Forecasts

## **CHAPTER 4: BUSINESS ENVIRONMENT**

SWOT Analysis

BMI Business Environment Risk Ratings

Business Environment Outlook institutions

Table: BMI BUSINESS AND OPERATION RISK RATINGS infrastructure

Table: BMI LEGAL FRAMEWORK RATING

Market Orientation

Table: LABOUR FORCE QUALITY

Table: MENA – ANNUAL FDI INFLOWS

Table: TRADE AND INVESTMENT RATINGS

Operational Risk

Table: Top Export Destinations, 2001-2009

## **CHAPTER 5: KEY SECTORS**

Autos

Table: Autos Sales, 2010-2017

Table: Food Consumption Indicators, 2010-2017

Table: Soft Drinks Value Sales – Historical Data & Forecasts, 2010-2017

Other Key Sectors

Table: Freight Key Indicators

Table: Oil and Gas Sector Key Indicators

Table: Infrastructure Sector Key Indicators

Table: Pharma Sector Key Indicators

Table: Telecoms Sector Key Indicators

## **CHAPTER 6: BMI GLOBAL ASSUMPTIONS**

Global Outlook

Fairly Benign Prognosis... With Risks

Table: Global Assumptions

Table: Developed States , Real GDP Growth, %

Table: BMI VERSUS BLOOMBERG CONSENSUS REAL GDP GROWTH  
FORECASTS, %

Table: Emerging Markets , Real GDP Growth , %

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