BAHRAIN

Table 1	2020
Population, million	1.7
GDP, current US$ billion	34.0
GDP per capita, current US$	20000.0
School enrollment, primary (% gross)[a]	98.0
Life expectancy at birth, years[a]	77.3
Total GHG Emissions (mtCO2e)	47.6

Source: WDI, Macro Poverty Outlook, and official data.
(a) Most recent WDI value (2019).

The economy will see a return to moderate growth in 2021, with the ease in restrictions helped by a rapid vaccination rollout. Fiscal and external deficits are expected to narrow, reversing their expansion observed in 2020. Debt to-GDP-ratio will remain above 130 percent during the forecast period, highlighting the priority of fiscal adjustment to put debt on a downward path. Downside risks arise from prolonged pandemic effects, oil price volatility and inadequate fiscal adjustment to contain the twin deficits which could lower growth outcomes and risk social tensions.

Key conditions and challenges

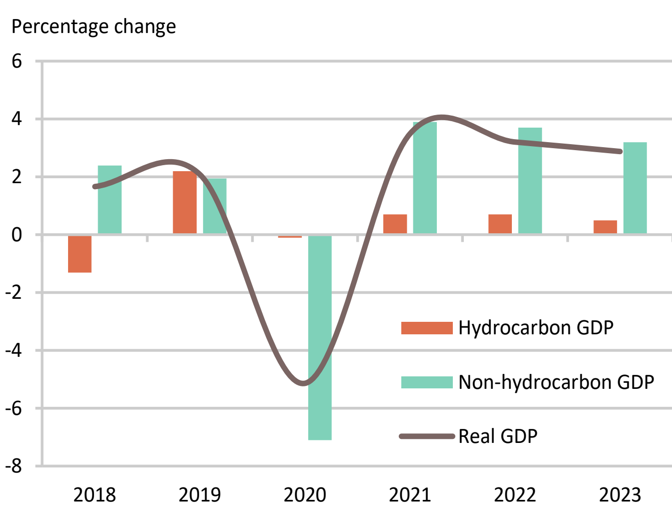
Bahrain entered the COVID-19 crisis with weak macroeconomic conditions. Even before, the fiscal and external deficits deteriorated following the 2014 oil price shock, and remained weak, notwithstanding progress under the 2018 Fiscal Balance Program (FBP), whose implementation was halted due to the pandemic and related oil price shock. The substantial pandemic-related crisis package of US$11.3 billion introduced in March 2020, and an additional US$1.3 billion stimulus package in June 2021 to support the sectors hardest-hit by COVID-19, have further limited the country's fiscal space, and aggravated already weak growth dynamics. Meanwhile, more is needed to facilitate private investment and trigger more private business development, strengthening the education system and support female labor force participation.

While the authorities remain committed to achieving the key reforms of the FBP, challenges remain. Achieving an FBP balanced budget by 2022 is unfeasible, following the pause of the fiscal consolidation caused by the pandemic, insufficient fiscal adjustment measures and considering that the FBP excludes extra budgetary spending financed by the budget. The authorities could also face the challenges of renewed oil price volatility and prolonged pandemic which could slow the pace of reforms. Phasing out of the temporary supporting measures and/or resuming the fiscal adjustment could spur social tension and delay the reform agenda, thus amplifying vulnerabilities. Advancing structural reforms including these related to supporting business environment, investing in renewable energy and digital solutions, would attract foreign investment, and increase employment opportunities, particularly among women and youth.

Recent developments

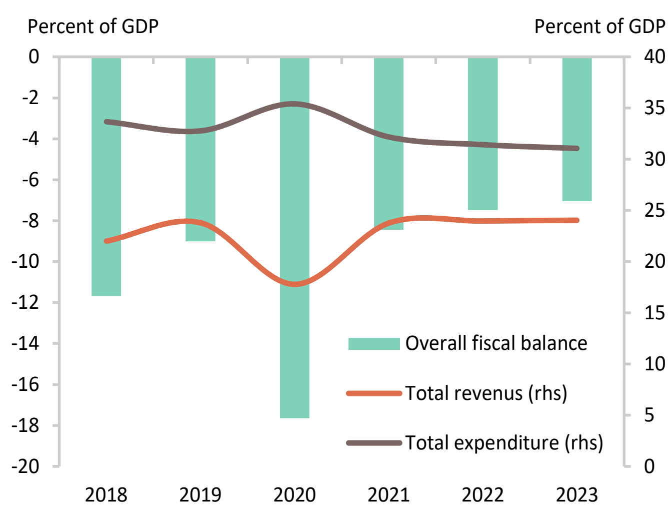
Preliminary official data reveals that the economy contracted by 2.1 percent year on year (y/y) in the first quarter 2021 (Q1-21), compared to the 5 percent contraction in 2020. The rebound is driven by the recovery of the oil sector, which grew by 2 percent (y/y) in Q1-21. This recovery outperformed the slowdown in the non-oil sector, down by 3 percent in Q1-21, as containment measures and travel restrictions hit hard services and tourism sectors where Bahrain has heavily invested. However, the overall growth will rebound by end-21 on the back of rising hydrocarbon output and further easing in lockdown. Disruption in economic activity caused by the COVID-19 pandemic brought 1.3 percent (y/y) deflation in the first half 2021 (H1-21). Official figures for the first half 2021 (H1-21) indicate that government revenues increased by 23 percent (y/y) primarily due to 33 percent increase in oil revenues. Other gains are related to non-oil revenues which increased by 4 percent mainly on the back of

FIGURE 1 Bahrain / Real annual GDP growth



Sources: Bahrain authorities, World Bank, and IMF staff projections.

FIGURE 2 Bahrain / General government operations



Sources: Bahrain authorities, World Bank, and IMF staff projections.

the VAT proceeds introduced in 2019. This will aid the fiscal deficit to narrow by end-2021, which may help to bring the total debt slightly down by end-2021. As a result, the central government debt is expected to slightly decline by 3.5 percentage points of GDP in 2021. High frequency data disclose that Bahrain's trade deficit slightly narrowed to 1.0 percent of GDP in Q2-21, as the value of exports increased by 75 percent (y/y) driven by hydrocarbon exports revenues.

According to the most recent data from the Labor Market Regulatory Authority (LMRA), total employment in Q1-21 fell with respect to the 2020, driven by lower foreign employment. The number of new work visas decreased by 10.6 percent in Q1-21 (y/y), and visa renewals fell by 27.9 percent. The number of foreign workers reached 531,447 in Q1-21, declining by 9.4 percent (y/y), and accounting for 77.6 percent of the country's total employment. Bahraini employment reached 153,757 during the same period in 2021. However, median monthly wages for Bahrainis reached BHD 556, a 3.2 percent increase (y/y).

Outlook

The economic outlook hangs on oil market prospects, the global path of the pandemic, and the government's commitment to the reforms plan. The hydrocarbon GDP is estimated to recover reaching almost 1.0 percent growth in 2021 and to remain stable in the forecast period with the unwinding OPEC+ deal by 2022 and further expanding the gas output from new fields. Non-hydrocarbon GDP is forecast to accelerate to almost 4 percent in 2021 as rapid vaccination deployment boosts activity in the services sectors, before bouncing back to an average of 3.5 percent in 2022-23 with the uncertainties on the path of delta variants and the need for fiscal consolidations. The swift rollout of 5G services last January coupled with a robust digital infrastructure in e-commerce and ICT sectors are likely to be important drivers of growth going forward. Inflation is estimated to increase to 1.5 percent in 2021 as aggregate demand improves and pandemic-related subsidies are phased out.

More favorable oil market conditions are projected to narrow the fiscal deficit to 8.4 percent of GDP in 2021. Resuming spending restraints under the FBP along with more hydrocarbon-driven revenues would help the fiscal deficit to further narrow in 2022-23. In the absence of significant reforms, the public debt-to-GDP ratio will remain over 130 percent in 2021-23 and the gross financing needs above 30 percent of GDP. Adherence to FBP accompanied by higher oil and non-oil revenues, will improve the outlook. Higher exports from oil and aluminum will narrow the current account deficit to 4.2 percent of GDP in 2021. While continue narrowing, the deficit is projected to persist in 2022-23 given high debt service payments and increased imports to boost oil production. The narrowing path of the current account deficit will in turn mitigate pressures on foreign exchange reserves. Risks to the outlook are looming on the downside. Oil market uncertainties and insufficient fiscal consolidation would further worsen the twin deficits, making medium-term debt sustainability harder to achieve. The prolonged impact of the pandemic would intensify economic scarring of the most affected sectors, and spark social unrest. On the upside, additional reform effort, anchored in a transparent medium-term framework, and strengthening PFM to reduce the fiscal risks from off-budget expenditures will help to improve Bahrain's outlook. The government has made efforts aimed at reducing unemployment by promoting the hiring of Bahrainis in the private sector through incentives to firms and increasing the local skill base. The strengthening of market-relevant skills among the Bahraini workforce would contribute to, gradually, help reduce unemployment among nationals as well as the demand for foreign labor.

TABLE 2 Bahrain / Macro poverty outlook indicators (annual percent change unless indicated otherwise)

	2018	2019	2020	2021 e	2022 f	2023 f
Real GDP growth, at constant market prices	1.7	2.1	-5.1	3.5	3.2	2.9
Private Consumption	1.4	-1.4	-4.2	4.0	4.2	3.4
Government Consumption	1.8	-1.5	7.6	4.3	1.7	-1.2
Gross Fixed Capital Investment	9.5	-4.7	-7.0	2.3	4.2	4.5
Exports, Goods and Services	3.3	0.4	-10.3	6.5	4.5	4.3
Imports, Goods and Services	5.7	-5.3	-9.7	6.5	5.6	4.2
Real GDP growth, at constant factor prices	1.7	2.1	-5.1	3.5	3.2	2.9
Agriculture	3.8	-1.0	0.1	1.5	2.2	2.4
Industry	1.1	2.3	-1.2	2.4	3.0	3.7
Services	2.1	1.9	-8.1	4.4	3.4	2.2
Inflation (Consumer Price Index)	2.1	1.0	-2.3	1.5	2.0	2.0
Current Account Balance (% of GDP)	-6.5	-2.4	-9.6	-4.2	-3.7	-3.4
Net Foreign Direct Investment (% of GDP)	3.7	3.1	1.2	1.3	1.9	2.6
Fiscal Balance (% of GDP)	-11.7	-9.0	-17.6	-8.4	-7.5	-7.0
Primary Balance (% of GDP)	-7.3	-4.5	-12.8	-3.7	-2.9	-2.7
GHG emissions growth (mtCO2e)	2.0	1.6	-4.1	9.0	3.9	4.1
Energy related GHG emissions (% of total)	61.8	61.3	60.2	58.8	58.2	57.5

Source: World Bank, Poverty & Equity and Macroeconomics, Trade & Investment Global Practices. Emissions data sourced from CAIT and OECD.
Notes: e = estimate. f = forecast.