

BAHRAIN

Table 1	2021
Population, million	1.7
GDP, current US\$ billion	38.8
GDP per capita, current US\$	22823.5
School enrollment, primary (% gross) ^a	98.0
Life expectancy at birth, years ^a	77.3
Total GHG Emissions (mtCO ₂ e)	52.4

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

The economy is gradually picking up as pandemic pressures fade, non-oil economy recovers, and hydrocarbon production increases. The fiscal deficit remains high as emergency crisis-spending persists but is expected to narrow gradually. The external balance will noticeably improve. The debt to-GDP-ratio is expected to remain elevated during the forecast period to meet fiscal needs. Downside risks arise from oil price volatility, and insufficient fiscal adjustment that could worsen fiscal and external positions and intensify pressure on already high public debt, thereby threatening macroeconomic sustainability.

Key conditions and challenges

The Bahraini economy is relatively diversified, reflecting the authorities' considerable efforts to boost manufacturing, refining, tourism, and trade. Nevertheless, the hydrocarbon sector remains a strong driver of the economy accounting for 20 percent of GDP and over 60 percent of total revenues, thereby making the economy extremely vulnerable to energy prices shocks. As such, the pandemic and related oil price shock have exacerbated Bahrain's large pre-existing fiscal and external imbalances, with a surge in public debt levels and gross financing needs. Bringing the fiscal position to a balance by 2022 according to 2018 Fiscal Balanced Program (FBP) proved challenging due to the pause of fiscal consolidation caused by the pandemic and insufficient fiscal adjustment measures.

At end-2021, the country announced new measures to curbe the fiscal deficit, including the doubling of the VAT rate to 10 percent from January 2022 and actions to reduce the deficit related to electricity and water authority.

However, challenges remain. Delays in reforms and persistent off-budget spending may imply higher debt and financing needs. Additional efforts are needed to unleash more fiscal space to meet the increased challenges posed by climate change and an expected long-term decline of demand for fossil fuels. On the upside,

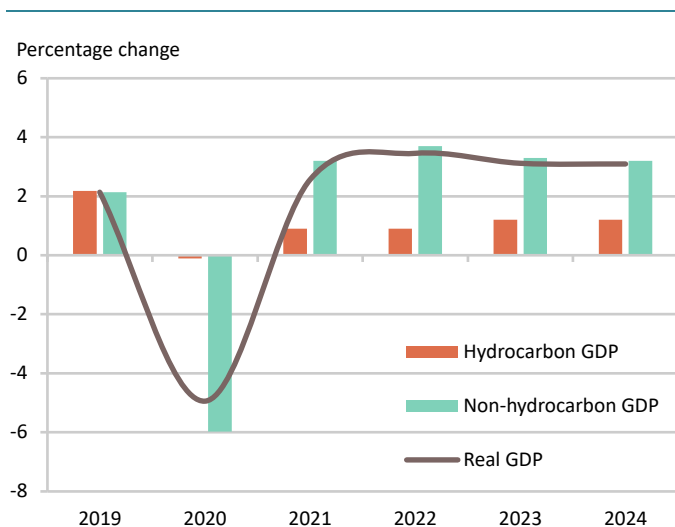
adherence to consolidation efforts, and reducing the fiscal risks from off-budget expenditures will help to improve Bahrain's outlook. Advancing structural reforms including these related to investing in renewable energy and digital solutions, would attract foreign investment, and increase employment opportunities, particularly among women and youth. While soaring oil prices caused by the economic consequences of the war in Ukraine are expected to further strengthen Bahrain's fiscal and external balances, there is a risk that strong fiscal buffers might lead to an increase in already high off budget spending.

The government has made efforts to reduce unemployment by promoting the hiring of Bahrainis in the private sector through incentives to firms and increasing the local skills base to gradually lower unemployment among nationals as well as the demand for foreign labor.

Recent developments

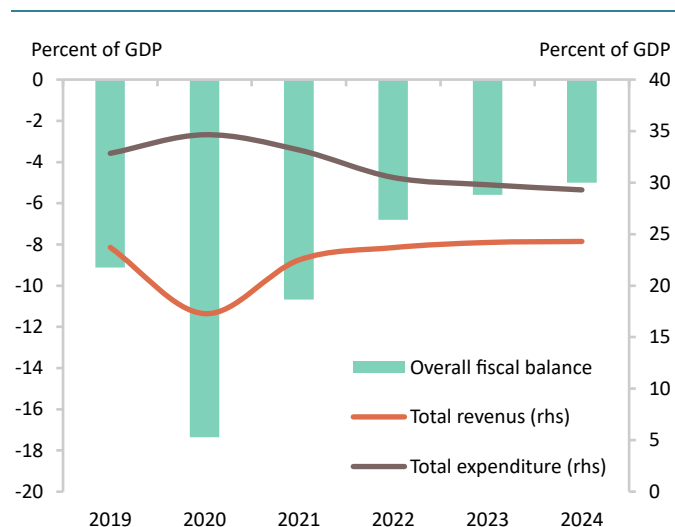
Bahrain's economy is gradually emerging from the pandemic-caused recession. Latest official data indicate that the economy grew by 1.5 percent (y/y) in the first nine months of 2021 (9M-2021), after nearly a 5 percent contraction in 2020. The rebound was mainly underpinned by 2.3 percent growth in non-hydrocarbon aided by a strong expansion in the transportation and communication sector—one of the hardest-hit by the pandemic—as well as increased agricultural and fishing activity.

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 hydrocarbon sector contracted by almost 2 percent (y/y) in the same period. Growth is estimated to have registered 2.6 percent by end-2021 driven by the non-hydrocarbon activities. Inflation remains in negative territory, averaging at -0.6 percent, due to weaker demand and lower prices for rents compounded by the departure of expatriates caused by the pandemic.

The fiscal deficit is estimated to have narrowed, from over 17 percent of GDP in 2020 to almost 11 percent in 2021, thanks to improved revenue from higher oil and aluminum prices despite high pandemic-related emergency spending. Public debt remained elevated at above 120 percent of GDP, although the better fiscal outcome helped to lower it by 6 percentage points.

The external sector exhibited a strong performance in the first 9M-2021 driven by solid rebound in both oil and non-oil exports, including service receipts, aided by the relaxation of COVID-19 restrictions. As a result, the current account balance is estimated to switch into a surplus of over 4 percent of GDP by end-2021, mitigating pressures on foreign reserves, which doubled to US\$4 billion in 2021, up from US\$2 billion in 2020.

According to the Labor Market Regulatory Authority, total employment in Q1-2021 fell with respect to 2020, driven by lower foreign employment. Data from the Social Insurance Organization indicate a recovery in Bahraini employment by the end of 2021. The number of Bahraini employees increased by 2.7 percent in Q4-2021 (y/y), 2.9 percent in the private sector and 2.3 percent in the public sector. The number of foreign employees has continued to decrease since Q4-2020 (y/y).

Outlook

Bahrain's economic outlook hangs on oil market prospects, pandemic conditions, and reform implementation. Growth is projected to accelerate to 3.5 percent in 2022, boosted by the surging energy prices caused by the economic consequences of the war in Ukraine. Recovery of the non-oil economy is likely to continue thanks to successful vaccination rollout and further relaxation of movement restrictions. Over the medium-term, however, non-oil economic activity would be dampened by

fiscal consolidation. The expansion of the Sitra oil refinery and development of the Khaleej al Bahrain shale oil project will support the growth outlook going forward. Inflation is expected to increase to 2.5 percent in 2022, fueled by the doubling of the VAT rate to 10 percent and a continued recovery of domestic demand.

While the pandemic related spending continues, the fiscal deficit is projected to continue narrowing over the medium term, supported by high hydrocarbon revenues and implementation of fiscal adjustment measures under the FBP. Yet public debt is projected to remain above 120 percent of GDP throughout 2022-24. Adherence to the FBP accompanied by higher hydrocarbon and non-hydrocarbon revenues, would improve the fiscal outlook.

Higher exports from oil and aluminum along with the revival of the tourism sector are forecast to keep the current account in surplus at nearly 5 percent of GDP in 2022, but to decelerate in the 2023-24 given high debt service payments and increased capital imports to boost oil production. The anticipated external account surplus will help mitigate pressures on the foreign exchange reserves.

TABLE 2 Bahrain / Macro poverty outlook indicators

(annual percent change unless indicated otherwise)

	2019	2020	2021e	2022f	2023f	2024f
Real GDP growth, at constant market prices	2.1	-4.9	2.6	3.5	3.1	3.1
Private Consumption	0.5	-4.4	3.1	3.7	3.2	2.9
Government Consumption	-1.5	-2.1	2.3	1.1	-0.8	-1.3
Gross Fixed Capital Investment	-2.8	-3.8	2.2	3.7	3.9	4.0
Exports, Goods and Services	0.4	-2.5	5.5	6.2	6.3	6.5
Imports, Goods and Services	-5.6	-0.7	6.2	6.4	6.4	6.5
Real GDP growth, at constant factor prices	2.1	-4.9	2.6	3.5	3.1	3.1
Agriculture	-1.0	0.1	2.2	2.4	2.7	2.6
Industry	2.3	-1.2	1.8	3.0	3.7	4.4
Services	2.0	-7.7	3.2	3.8	2.7	2.1
Inflation (Consumer Price Index)	1.0	-2.3	-0.6	2.5	2.7	2.5
Current Account Balance (% of GDP)	-2.1	-9.3	4.3	4.6	3.4	3.1
Fiscal Balance (% of GDP)	-9.1	-17.4	-10.7	-6.8	-5.6	-5.0
GHG emissions growth (mtCO2e)	6.1	-2.0	3.1	3.5	3.3	3.3
Energy related GHG emissions (% of total)	63.3	62.2	62.9	63.7	64.2	64.7

Source: World Bank, Poverty & Equity and Macroeconomics, Trade & Investment Global Practices. Emissions data sourced from CAIT and OECD.