BAHRAIN

Table 1	2018
Population, million	1.6
GDP, current US$ billion	38.4
GDP per capita, current US$	24483
School enrollment, primary (% gross)[a]	101.1
Life expectancy at birth, years[a]	76.9

Source: WDI, Macro Poverty Outlook, and official data.
Notes:

(a) Most recent WDI value (2016)

Consumer spending and increased investment in the ALBA aluminum plant expansion supported an overall estimated growth of 2 percent in 2018. The government Fiscal Balance program (FBP) announced in 2018 accompanied by US$10 billion in GCC financial support will alleviate financing constraints in the aftermath of 2014 oil price shock. Key challenges facing Bahrain include the need to fully implement the FBP reforms. Bahrain will need to pursue energy subsidy reform and control large off-budget expenditures, while pursuing its diversification strategy.

Recent developments

Growth in 2018 is estimated at 2 percent, with relatively strong downstream energy investments and activity (oil refining and aluminum) offsetting the capacity-constrained crude oil sector. The first three quarters of 2018 showed a year-on-year 5 percent contraction in the oil sector, with slowdown in financial services, hospitality, and trade sectors. Non-oil growth is estimated to have decelerated to 2.5 percent, driven by slowdowns in retail, hospitality, and financial services sectors. Average inflation has increased from 1.4 percent in 2017 to an estimated 2.1 percent in 2018, due to higher food and transport prices.

While improved, fiscal and external deficits remain high. Higher oil prices and some tax and subsidy measures are estimated to have lowered the fiscal deficit to 11.7 percent of GDP in 2018, from 14.2 percent of GDP in 2017. Despite higher oil prices, the current account deficit is estimated to have increased to 5.8 percent of GDP in 2018, from of 4.5 percent of GDP in 2017, mainly due to an increase in workers' remittances outflows. Reserves are estimated to continue falling, to reach only US$2 billion in 2018 (or one month of non-oil imports), compared to US$2.6 billion in 2017 (or 1.5 months of imports). Recurring fiscal and external deficits have led to a further increase in public debt-to-GDP ratio, estimated at 93 percent in 2018, from 88 percent in 2017.

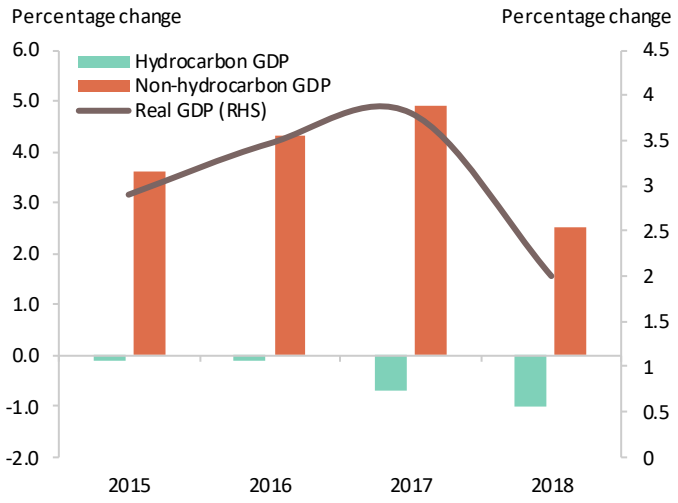
The recent announcement of US$10 billion in support from Saudi Arabia, Kuwait, and the UAE, linked to fiscal reforms, has alleviated gross financing concerns, and bond spreads have since declined.

Evidence on welfare impacts remain limited due to limited access to household survey. As for other GCC, unemployment among female youth (percent of female labor force ages 15-24) is high and stands at 14 percent, compared to only 3 percent among male youth. The generous state subsidies (for energy and food) form an important part of the social protection system. In January 2018, and in an attempt to limit social unrest, government officials announced that no new taxes or subsidy cuts would be implemented in the kingdom before compensatory measures for lower-income citizens are adopted. In late 2018, the government announced a series of reforms within the fiscal balance program that would affect households and their earning potential. Key among them, providing incentives for government workers to voluntarily retire or move to the private sector. However, given the voluntary nature of the reform, it is unclear what share of the large number of government workers in the country will accept the incentive.

Outlook

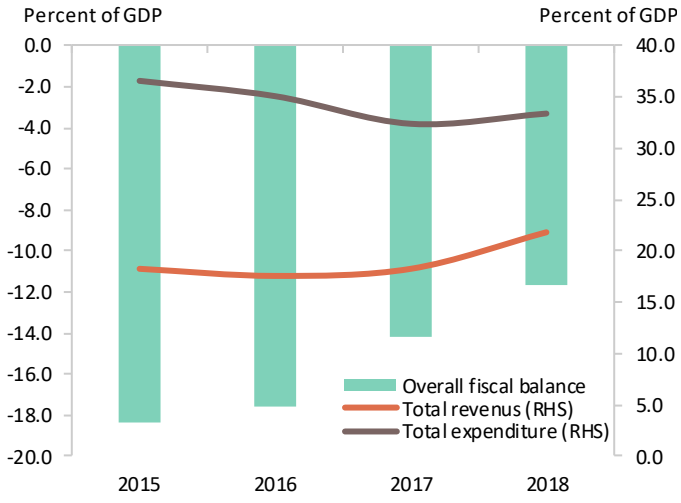
Overall growth is projected to remain at an average of 2.1 percent over 2019-2020, and non-oil growth to slow to 2.4 percent, due to front-loaded FBP fiscal measures and tapering megaproject investments. Growth will resume in outer years as efficiency

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.

gains from reforms materialize. Inflation is expected to increase to 3 percent in 2019-2020, given the imposition of the VAT in 2019 and additional proposed energy tariff hikes. Fiscal consolidation under the FBP would lower the fiscal deficit to an average of 8 percent of GDP in 2019-2020. Public debt will remain high, approaching 100 percent over the forecast period. The introduction of VAT and excise taxes would boost non-oil revenue by an average of 6.3 percent of non-oil GDP in the period 2019-2020, compared to less than 5 percent of non-oil GDP in 2018 – contributing to an improvement in the non-oil primary balance. The current account deficit is likely to persist in 2019-2020, albeit at moderate levels, as rising remittances and interest payment on the government's external debt offset the increase in net exports of goods and services. Reserves are expected to stay low at less than one month of prospective non-oil imports in the forecast period.

Given this outlook, people's welfare is likely to be negatively impacted unless more diversified sources of government revenue are found. Bahrain faces tough public policy choices as it implements the FBP, especially since cuts to social spending will likely affect delivery of public services and social safety net programs. The country also needs to create a vibrant environment for a diversified job-creating non-oil private sector.

Risks and challenges

While regional financial support has greatly reduced near-term pressures, risks to the outlook are on the downside. Despite the flexibility provided by the GCC3 package, the FBP will face implementation constraints. A key constraint is the limited room for budgetary expenditure cuts to achieve big gains, since they will largely need to come from reducing social spending. The second constraint relates to off-budget expenditures, which contribute around 5 percentage points to the overall deficit and may be difficult to cut. Third, the plan will need to be more ambitious on non-oil revenue generation. A sharp tightening of global financing conditions and lower oil prices could impede liquidity flows in the retail and wholesale financial sector, which remains Bahrain's main driver of diversification. While financing constraints have eased, a reduction in the level of debt is still unlikely in the near term given the size of fiscal deficit.

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

	2016	2017	2018 e	2019 f	2020 f	2021 f
Real GDP growth, at constant market prices	3.5	3.8	2.0	2.0	2.2	2.8
Private Consumption	0.5	-1.4	1.6	2.0	2.2	2.2
Government Consumption	-0.6	3.1	0.8	-1.6	0.4	0.4
Gross Fixed Capital Investment	10.8	11.0	3.3	5.7	5.1	5.1
Exports, Goods and Services	-1.8	2.8	4.5	3.5	2.2	2.2
Imports, Goods and Services	-3.4	7.8	4.1	3.5	2.0	2.0
Real GDP growth, at constant factor prices	3.5	3.8	2.0	2.0	2.2	2.8
Agriculture	6.9	-0.9	-0.9	-0.9	-0.9	-0.9
Industry	2.8	0.6	0.6	0.6	0.6	0.6
Services	4.0	6.3	3.0	3.0	3.3	4.3
Inflation (Consumer Price Index)	2.8	1.4	2.1	3.3	3.2	2.3
Current Account Balance (% of GDP)	-4.6	-4.5	-5.8	-3.9	-3.6	-3.4
Net Foreign Direct Investment (% of GDP)	3.5	0.8	1.0	0.8	0.8	0.8
Fiscal Balance (% of GDP)	-17.6	-14.2	-11.7	-8.4	-7.7	-7.4

Source: World Bank, Poverty & Equity and Macroeconomics, Trade & Investment Global Practices.
Notes: e = estimate, f = forecast.