Kuwait

Economic conditions will soften in 2023 as oil production is curtailed and the post-pandemic consumer boom abates, while ongoing political gridlock constrains investment. This said, gains in oil refining could push non-oil growth close to 4% this year. High oil prices will help the government sustain an accommodative fiscal policy, though with large, one-off spending items, last year's expected fiscal surplus will likely shift to a deficit in FY23/24. The executive and legislature need to work hand-in-hand to push through crucial economic reforms to boost growth and reduce oil dependency, emulating reform success in other GCC economies.

Economic activity normalizing, oil output down in 2023

Economic activity, though solid, is expected to slow in 2023 as the post-pandemic bounce in consumer spending, real estate and credit demand fades alongside lower oil output in accordance with OPEC+ production policy. GDP growth is forecast to moderate from an estimated 7.6% in 2022 to an average of 1.5% per year over the forecast period. In the oil sector, having risen to a five-year high of 2.82 mb/d in 3Q22, crude output fell to 2.68 mb/d in February 2023 – and will decline even further to 2.55 mb/d (-128 kb/d) after Kuwait agreed with the OPEC+ decision in April to deepen pre-existing cuts for the entirety of 2023. But in our view, tighter fundamentals (and higher oil prices) will likely compel OPEC+ to reverse some of these additional cuts before year-end and into 2024. We expect oil GDP to contract by 3.7% in 2023 before rising by 2.7% in 2024.

The solid performance of non-oil GDP post-pandemic, averaging growth of 3.2% per year in 2021-22, has largely been a tale of higher oil prices, government fiscal largesse, pent-up consumer demand and gains in oil refining, which more than offset a subdued projects market. Inevitably, however, the breakneck pace of consumer activity – cards data show spending growth peaked at 33% in 2021 – was difficult to sustain, especially against a backdrop of higher inflation and tighter global monetary policy. The government's draft budget for FY23/24 is expansionary (see below) and should support the economy in the near term. However, political gridlock and the prospect of fresh elections later this year after the Constitutional Court in March voided the 2022 parliament on procedural grounds will delay its approval and weigh on the previously hoped-for rebound in investment in 2023. Our base case is for non-oil growth of no more than 3.0% (3.8% after refining gains from the now fully operating Al-Zour refinery are included).

Inflation to slow as interest rates reach peak

We expect inflation to moderate from 4.0% (annual average) in 2022 to 2.5% in 2024 on slowing consumer activity and tighter monetary policy. As of mid-April 2023, the CBK had hiked its (discount) policy rate by 250 bps to 4.0% in the current tightening cycle versus +475 bps for the Fed. Although US and therefore Kuwaiti rates may now be close to their peak, the slower pace of tightening in Kuwait so far could lead to a correspondingly slower pace of loosening in 2024, especially if the Fed is forced to cut aggressively.

A first fiscal surplus in 8 years, easing liquidity constraints

Still-to-be finalized closing accounts for FY22/23 should reveal a first fiscal surplus in eight years for the government (KD5.2bn or 9.6% of GDP). This could be short-lived, however, after the authorities in their FY23/24 draft budget penciled in a budget-on-budget spending increase of 12% and a revenue decline of 17% (based on an oil price of $70/bbl), resulting in a fiscal deficit of KD6.8bn or 13% of GDP. But the underlying fiscal position is better since about half of the rise in spending is linked to one-off items (arrears for electricity, fuel subsidies and employee leave payments) and since oil prices are likely to come in higher than the budget's forecast. We forecast a deficit of 3.0% of GDP in FY23/24 (zero if the non-recurring items are stripped out), and a surplus of 1.0% of GDP in FY24/25.

Although the fiscal position has therefore improved sharply post-Covid, structural vulnerabilities remain, including limited revenue diversification and a budget weighted heavily towards wages and subsidies (80% of all spending). The latter means that when the government's long-delayed capital-intensive economic diversification program takes off, overall spending will be pushed higher. Nevertheless, in the short-to-medium term at least, fiscal and external buffers are ample. The General Reserve Fund (used to finance near-term deficits) has been recapitalized thanks to the recent spell of higher oil prices, and Kuwait's external assets, consisting of CBK foreign reserves and KIA's overseas assets, are in excess of $800bn (456% of GDP). Public debt, at about 3.0% of GDP, is extremely low by international standards, minimizing stress from higher interest rates.

Outlook shaped by oil prices and political economy

Higher oil prices, expansionary fiscal policy, increased traction on projects implementation and a further recovery in the labor force would all be positive for economic growth. Even more important would be the executive and the legislature working hand-in-hand to push through urgent fiscal and economic reforms to rationalize public spending, improve institutional efficiency and stimulate the private sector (as in the government's five-year 'Plan of Action'). Key draft laws covering mortgages and debt issuances are also pending. Reform-focused, effective policymaking is the key to minimize the intensifying risks of high oil price dependency, sub-optimal private sector development and employment of Kuwaiti nationals, and low foreign investment. These are the catalysts that would push the non-oil economy onto a sustainably higher growth path.

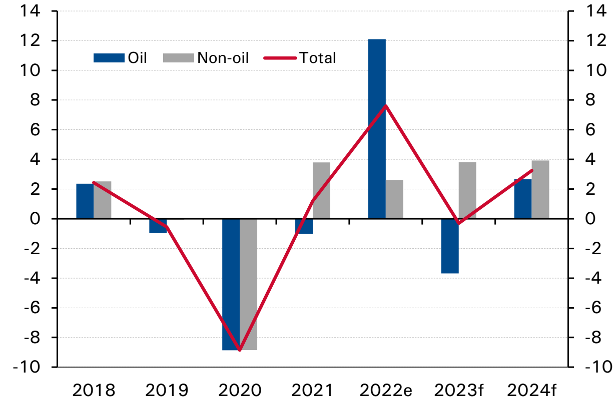
Table 1: Key economic indicators

		2020	2021	2022e	2023f	2024f
Nominal GDP	$ bn	106	139	176	170	172
Real GDP	% y/y	-8.9	1.2	7.6	-0.3	3.3
- Oil sector	% y/y	-8.9	-1.0	12.1	-3.7	2.7
- Non-oil sector	% y/y	-8.8	3.8	2.6	3.8	3.9
- Non-oil ex refining	% y/y	-8.6	3.4	3.2	3.0	3.0
Budget balance (FY)	% of GDP	-33.2	-7.1	9.6	-3.0	1.0
Current act. balance	% of GDP	1.4	26.9	34.1	30.8	32.3
Inflation (avg.)	% y/y	2.1	3.4	4.0	3.1	2.5

Source: Official sources, NBK forecasts

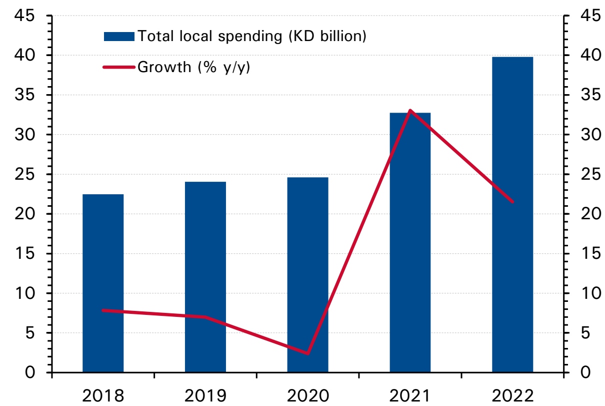
Chart 1: Real GDP

(% y/y)



Source: Central Statistical Bureau (CSB), NBK forecasts

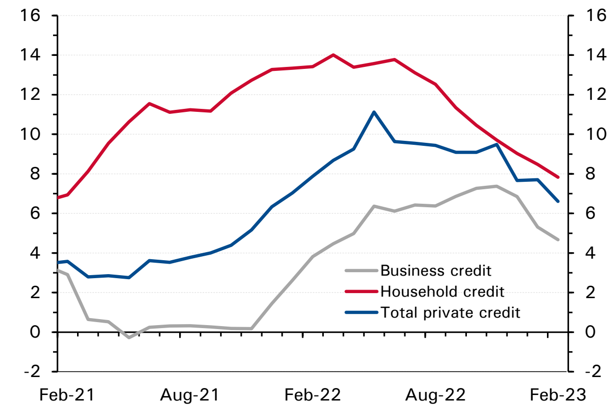
Chart 2: Consumer spending (cards)



Source: Central Bank of Kuwait (CBK)

Chart 3: Bank credit

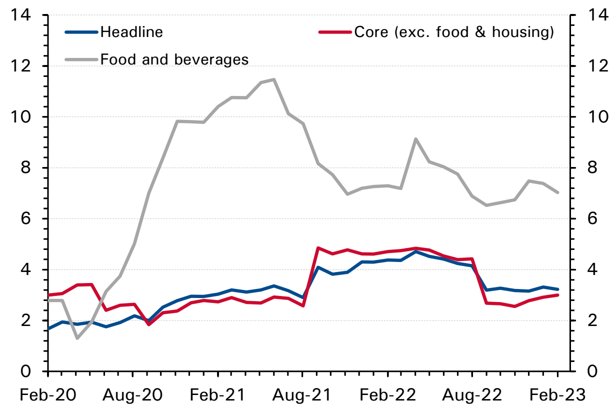
(% y/y)



Source: CBK

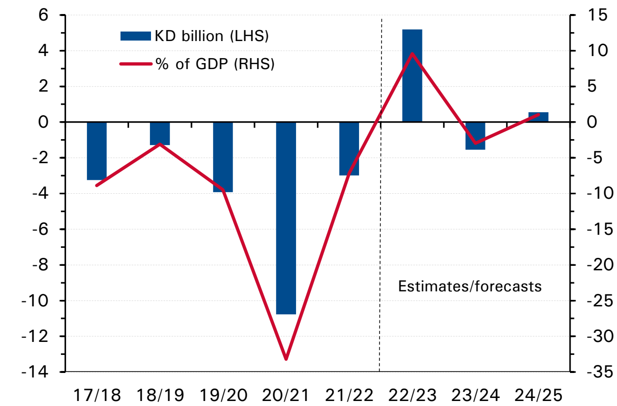
Chart 4: Consumer price inflation

(% y/y)



Source: CSB

Chart 5: Fiscal balance*



Source: Ministry of Finance (MOF), NBK forecasts; *on a fiscal year basis