



KUWAIT

2013 ARTICLE IV CONSULTATION

November 2013

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2013 Article IV consultation with Kuwait, the following documents have been released and are included in this package:

- The **Staff Report** for the 2013 Article IV consultation, prepared by a staff team of the IMF, following discussions that ended on September 23, 2013, with the officials of Kuwait on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on November 4, 2013.
- An **Informational Annex** prepared by the IMF.
- A **Press Release** summarizing the views of the Executive Board as expressed during its November 25, 2013 discussion of the staff report that concluded the Article IV consultation.
- A **Statement by the Executive Director** for Kuwait

The document listed below has been or will be separately released.

Selected Issues Paper

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

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International Monetary Fund
Washington, D.C.



KUWAIT

STAFF REPORT FOR THE 2013 ARTICLE IV CONSULTATION

November 4, 2013

KEY ISSUES

Context. High oil prices and increased production have enabled the government to continue to record high fiscal and external surpluses and build strong buffers. Large infrastructure investments are expected to support the growth momentum.

Outlook and risks. Overall real non-oil gross domestic product (GDP) growth is projected to increase modestly to 3 percent in 2013, driven by an increase in domestic consumption and pick-up in public investment and to 4.4 percent in 2014. The overall average consumer price inflation (CPI) is projected at 3 percent in 2013. The fiscal and external surpluses are projected at 27 percent of GDP and 39 percent of GDP, respectively, in 2013, reflecting high oil prices. The main downside risks to the outlook are a sustained fall in oil prices and renewed political gridlock.

Macroeconomic policy mix. The government should increase capital spending, while over the medium- to longer-term, oil wealth should be conserved for future generations through lower current spending growth, particularly in wages and public employment, and higher non-oil revenues. Monetary conditions are expected to remain supportive of credit growth.

Financial stability. The banking system is resilient to credit and market risks. Investment companies (ICs) are still deleveraging and restructuring. Providing greater institutional and functional autonomy for the central bank, and developing a more formal macroprudential institutional and policy framework would help strengthen macroeconomic and financial stability. A review of the investment companies (ICs) segment, with particular focus on their objectives and role in the economy, and financial viability is needed.

Diversifying the economy and creating jobs for nationals in the private sector. Reducing Kuwait's dependence on oil in the future will require economic diversification, particularly in export-oriented industries, which calls for further structural reforms to improve the business environment and governance. Creating incentives for employment of nationals in the private non-oil sectors would entail containing growth in public sector wages and jobs. An integrated plan for job creation in the private sector is called for, some elements of which will include enhancing the educational quality and vocational training, promoting female labor force training, and encouraging entrepreneurship by developing the small and medium-sized enterprises (SMEs) sector.

Approved By
**Alfred Kammer and
 Taline Koranchelian**

Discussions were held in Kuwait during September 10–23, 2013. The mission comprised Ms. Colacelli, Messrs Hasanov, Prasad (Head), and Santos (all MCD). The mission met with H.E. Minister of Finance and Deputy Prime Minister, Sheikh Salem Abdulaziz Al-Sabah, H.E. State Minister for Planning and Development Affairs and State Minister for Parliament Affairs, Rola A. Dashti, H.E. Minister of Commerce and Industry, Anas K. Al-Saleh, H.E. Governor of the Central Bank of Kuwait, Mohammad Al-Hashel, Undersecretary of the Ministry of Finance, Khalifa Hamada, and other senior government and central bank officials, representatives from the financial community, and Members of Parliament.

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BACKGROUND

- 1. Kuwait is an oil-rich and high-income country, but it lags behind internationally on many economic and social indicators.** Kuwait has the sixth largest proven oil reserves in the world at 102 billion barrels, which at the current rate of production would last for 90 years. Kuwaitis comprise 32 percent of the total population of 3.8 million. The labor market is highly segmented. About 70 percent of government employees are Kuwaitis, while 95 percent of private-sector employees are non-Kuwaitis (Figure 2). Kuwait fares relatively low in international comparison in social and governance indicators (Figures 3 and 4), and relatively high in financial inclusion indicators (Figure 5). Kuwait's per capita income was about \$48,000 in 2012 with an unemployment rate of 3 percent for Kuwaitis.
- 2. Recent domestic political developments have had an adverse impact on fiscal and economic developments in Kuwait.**¹ The implementation of the 2010–14 Development Plan (DP) has lagged behind, and large increases in the public-sector wage bill have undermined the government's efforts to encourage Kuwaitis to join the private sector.² The financial situation of banks is strong, and the banking system is well-regulated by the Central Bank of Kuwait (CBK). Investment companies are still deleveraging, and further restructuring, consolidation, and exit are needed in this sector.
- 3. It is vital to agree on an agenda to place the DP on track, improve the business environment and investment climate, and boost non-oil growth.** The long-term objective should aim toward diversification and job creation for Kuwaitis in the private sector. Building human capital, improving the efficiency of public administration, and removing impediments to physical, legal, and business infrastructure would support these goals. High per capita income and large external wealth should provide support for the transformation needed.

RECENT DEVELOPMENTS

- 4. Kuwait's economic performance has lagged behind its GCC peers and its own past performance.** Since the global financial crisis of 2008, non-oil growth has been negative or low (Figure 1). Public investment as percent of GDP has been below the GCC average because of delays in the implementation of economic reforms and infrastructure projects. Social and global

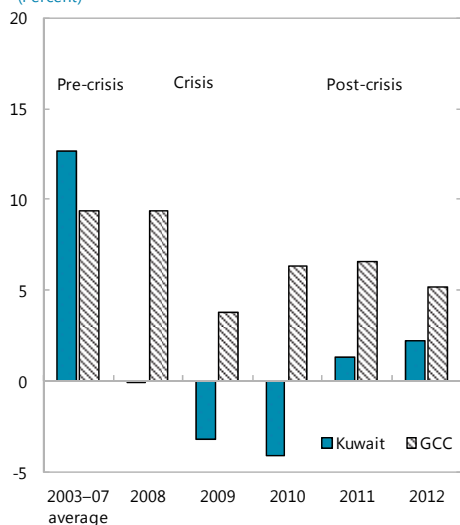
¹ The political environment has remained highly contentious since 2006, as tensions between parliament and the government led to six parliamentary elections since June 2006, with the most recent held on July 27, 2013.

² The Kuwait Development Plan is a series of five-year plans approved by parliament in February 2010, stretching to 2035 and aimed at converting Kuwait into a trade and financial hub of the region. A Plan of about \$130 billion was to be implemented with private-sector participation, including a variety of Public-Private Partnership (PPP) mechanisms, with the objectives of increasing the private sector's contribution to the economy, creating jobs, and providing long-term investment opportunities. Investment is envisaged in projects across a variety of sectors, including oil, utilities, infrastructure, and services (especially healthcare and education).

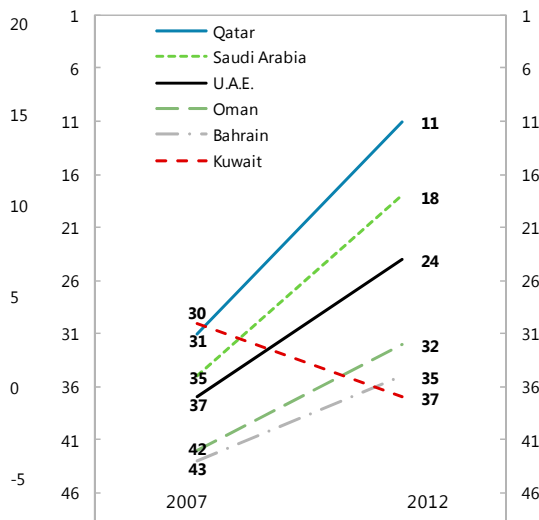
competitiveness (e.g., ease of doing business) indicators have also been lagging behind other GCC countries.

Figure 1. Recent Developments

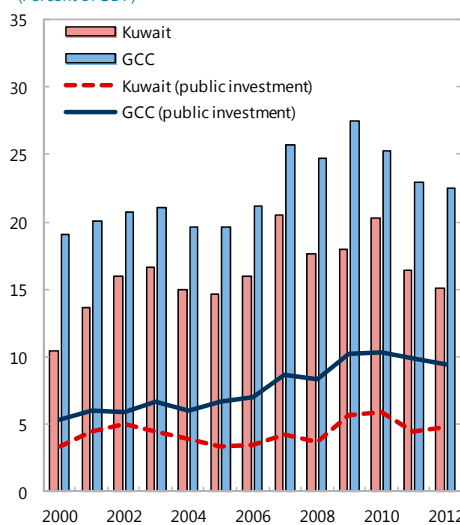
Real Non-oil GDP Growth, 2003–12
(Percent)



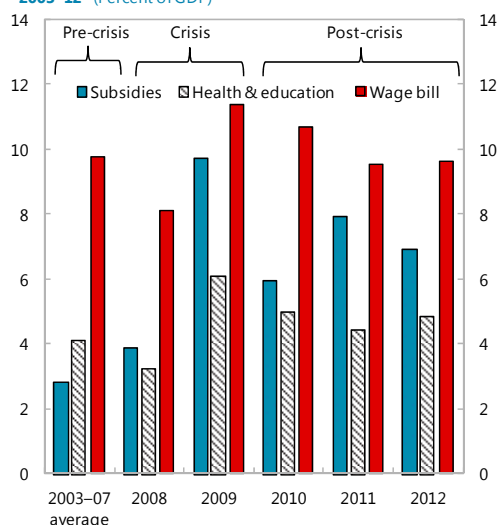
GCC: Global Competitiveness Rank, (2007 and 2012)



Total and Public Investment, 2000–12
(Percent of GDP)



Fiscal Expenditure on Subsidies, Health and Education, 2003–12
(Percent of GDP)



Sources: Country authorities; World Economic Forum; and IMF staff calculations.

5. The non-oil economy is projected to continue its recovery in 2013. Non-oil growth is expected to increase modestly to 3 percent, driven by a combination of a continued increase in domestic consumption as a result of the 2012 public wage hike and some pick-up in government capital spending. A slight reduction in oil production would bring down total real GDP growth below 1 percent. The average inflation in September 2013 was about 3 percent year-on-year (y-o-y) and is projected to remain stable at 3 percent. Current account surplus is expected to remain large in 2013 at 39 percent of GDP.

6. Despite rising current expenditures, the fiscal surplus is projected to remain high at 27 percent of GDP in 2013, reflecting high oil prices. Spending is projected to rise by 13 percent, mainly because of increased public employment, subsidies and social benefits, and capital spending (Figures 6 and 7). Capital expenditure, which underperformed the budget allocation in 2012, as continued political uncertainty stalled the implementation of investment projects, is expected to increase by 47 percent in 2013/14 compared to 2012/13.

7. Monetary policy has remained accommodative and bank credit growth has picked up. The Central Bank of Kuwait (CBK) reduced the benchmark discount rate to 2 percent in October 2012, which brought down the weighted average deposit and lending rates to 1.53 percent and 4.63 percent, respectively at end-June 2013 (from 1.60 percent and 4.86 percent, respectively in October 2012). Bank credit grew y-o-y by 6.2 percent in June 2013, reflecting strong growth in personal loans (Figure 8). Excess liquidity of the banking system—bank reserves at the central bank—has been steadily rising as total deposits increased by 9 percent y-o-y in June 2013. Bank lending to non-bank financial institutions contracted by about 19 percent y-o-y in June 2013, representing 6.3 percent of banks' total credit portfolio.

8. Bank profitability has remained stable (Figure 8) and soundness indicators appear strong. Some ICs continued to record losses in 2012, though of a lower order. Overall, since their peak in 2008, investment companies' (ICs) proprietary assets shrank by 32 percent, and assets under management shrank by 15 percent. The nonfinancial corporate sector continued to record profits in 2012 although a number of companies in the real estate sector posted losses.

OUTLOOK AND RISKS

9. The economic outlook is expected to improve further in 2014 and over the medium term. In 2014, non-oil growth is expected to increase to 4.4 percent supported by public capital spending, driving average inflation to 3.5 percent. A constant level of oil production would keep total real GDP growth below 3 percent. Fiscal and current account surpluses are expected to remain large in 2014. Over the medium term, non-oil growth is projected to accelerate to about 5 percent. A moderate increase in oil production is expected to further support overall growth. Inflation is projected to increase slightly as growth picks up. The fiscal and current account surpluses are projected to taper if spending continues on the current growth trajectory. The authorities agreed with staff's projections.

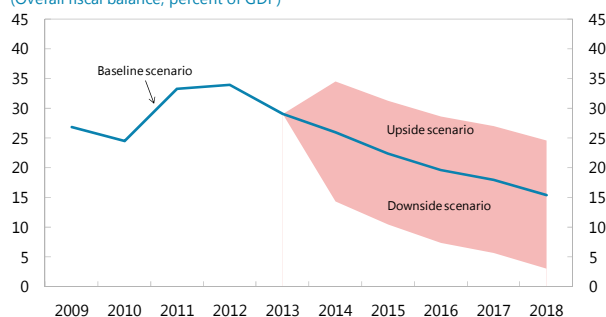
10. Achieving the projected baseline growth in the medium term requires that there is a political consensus to place public investment and structural reforms on track. The authorities agreed with staff's assessment that protracted political uncertainty would adversely affect overall business confidence and the investment climate and result in lower non-oil growth than projected. They, however, felt that inclusiveness of the new parliament raises the prospect of improving its working relationship with the new government, although recent inquiries of some members of parliament into the legality of some major public investment projects highlight the risk of potential political gridlock.

11. Downside external risks to the outlook could arise from a worsening of global economic conditions, including a lower than anticipated growth potential in key emerging market countries, that would translate into lower oil demand and prices (Risk Assessment Matrix below). However, fiscal buffers are large, and the authorities have space to smooth public spending in the medium term in the event of an oil price drop.³ The breakeven oil price—the price needed to balance the budget at current expenditure levels—has risen to \$70 in 2013/14 (excluding investment income), which is still relatively low compared to the current level of oil prices.⁴ However, reflecting the recent sharp increases in current

expenditures—most of which are hard to reverse—and relatively small non-oil revenues, government expenditure in the baseline would exceed oil revenues by 2017/18, thus increasing the fiscal risk from a sustained drop in oil prices, a concern that the authorities shared.

Fiscal Balances Sensitive to Oil Prices, 2009–18

(Overall fiscal balance, percent of GDP)

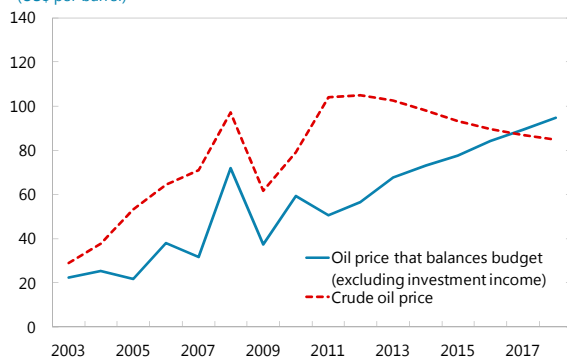


Sources: Country authorities; and IMF staff estimates.

Note: Upside scenario shows fiscal balance for the oil price up to \$25 (one standard deviation) higher than the forecasted oil price and downside scenario is up to \$25 lower.

Breakeven Oil Prices, 2003–18

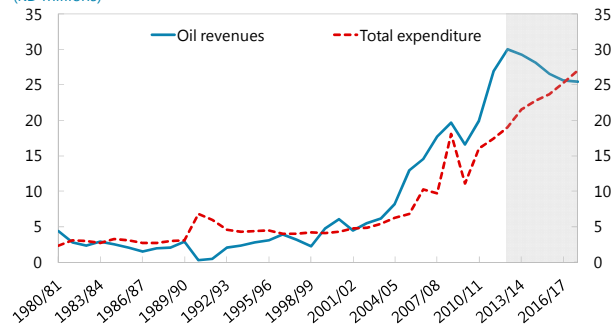
(US\$ per barrel)



Sources: Country authorities; and IMF staff calculations.

Oil Fiscal Revenues and Total Government Expenditure, 1980/81–2017/18

(KD millions)



Sources: Country authorities; and IMF staff estimates.

³ A one standard deviation decline in oil prices (\$25) relative to the baseline between 2014–18, a one-in-nine probability based on option markets, will result in a decline of the current account and fiscal surplus to 16 percent and 3 percent of GDP, respectively, in 2018.

⁴ The production level is assumed at 2.93 million barrels per day in 2013.

Risk Assessment Matrix¹

Nature/source of main threats	Likelihood of Risk	Expected impact on the economy if risk is realized	Recommended Policy Response
<p>Financial stress in the euro area re-emerges (triggered by stalled or incomplete delivery of national and euro area policy commitments).</p>	<p>Medium</p>	<p>Medium</p> <p>Uncertainties in the euro area and a related tightening of global capital markets would pose funding and market risks for ICs, which have large exposures to global and regional financial, and real estate markets, and continue to be dependent on foreign financing. Banks have direct exposures to the real estate sector in addition to equity and real estate collaterals. The Kuwait Investment Authority (KIA) also has substantial investments.</p>	<p>Banks' provisions would need to increase if NPLs increase, tightening domestic lending conditions because of risk aversion. Nonetheless, the banking system would likely remain sound, because banks have been making specific and general provisions that cover the existing nonperforming loans. The impact on KIA's assets is expected to be manageable.</p> <p>Adjust macroprudential policies as needed to limit risks to the financial system.</p>
<p>Lower-than-anticipated growth potential in emerging markets (earlier maturing of the cycle and incomplete structural reforms with spillovers to low income countries and advanced economies)</p>	<p>Medium</p>	<p>Medium</p> <p>Could lead to a decline in oil demand and prices. The economy remains highly dependent on oil for its fiscal and external revenues.</p>	<p>Even though the government has significant buffers, it should contain current expenditures and explore avenues to increase non-oil revenues, particularly by broadening the corporate income tax base, to insulate the economy from dependence on oil, and to increase buffers while oil prices are still high.</p> <p>If risk materializes and the oil price drop is sustained, some further consolidation in expenditure would be required, which would affect non-oil activity.</p> <p>Undertake structural reforms, including improving the investment climate, and support diversification to reduce oil dependence.</p>
<p>Distortions from unconventional monetary policy (continued mispricing of risk)</p>	<p>Low</p>	<p>Medium</p> <p>Could lead to temporary liquidity tightening in banks, and force further deleveraging</p>	<p>Complete the restructuring process of ICs.</p> <p>Establish a macroprudential framework and a coordinating mechanism to assess</p>

assets followed by market broad-based correction in valuations; delays in fiscal and structural reforms)		of investment companies.	incipient risks. Adjust the implementation of macroprudential instruments, such as liquidity and credit ratios, exposure norms, capital buffers, etc., as needed to ensure bank liquidity and credit growth.
A large and prolonged decline in oil prices (triggered by a global recession or an increase in oil supply).	Low	High Fiscal and external revenues would fall, and private sector confidence is likely to decline.	Even though the government has significant buffers, it should contain current expenditures and explore avenues to increase non-oil revenues, particularly by broadening the corporate income tax base, to insulate the economy from dependence on oil, and to increase buffers while oil prices are still high. If risk materializes and the oil price drop is sustained, some further consolidation in expenditure would be required, which would affect non-oil activity. Undertake structural reforms, including improving the investment climate, and support diversification to reduce oil dependence.
Slow implementation of the Development Program (DP)	Low	Medium Political gridlock has already delayed legislative reforms and slowed the implementation of the DP. Non-oil growth is highly dependent on government expenditures, particularly in the context of the DP.	Resolve the political gridlock. Integrate the DP into a medium-term budgeting framework. Monitor the implementation of capital expenditure. Improve the investment climate through structural reforms and passage of pending legislation.
<p>¹ The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path discussed in this report (which is the scenario most likely to materialize in the view of IMF staff). The relative likelihood of risks listed is the staff's subjective assessment of the risks surrounding this baseline. The RAM reflects staff's views on the source of risks and overall level of concerns that will be discussed with the authorities.</p>			

12. Tighter financial conditions due to quantitative easing (QE) tapering and/or reemergence of financial stress in the euro area may increase vulnerabilities and result in market and credit risks for banks and non-bank financial institutions, forcing further deleveraging by ICs, and increasing banks' risk aversion. Banks have direct exposures to the real estate sector (18.5 percent of total loans in June 2013 on a consolidated basis), in addition to

equity and real estate collaterals. While the central bank is monitoring the banking system to ensure that they don't take on excessive risks in these circumstances, the banking system is adequately capitalized and has ample liquidity to withstand shocks under severe macro scenarios. The recovery of investment companies which are exposed to market risk, particularly those under restructuring, would be further delayed, however.

13. In the medium to long term, global oil market developments will affect Kuwait's economic outlook. Over the next five years, Kuwait's oil output is projected to grow modestly, and the non-oil sector will be the main driver of growth, albeit supported by government investment. However, the projected increases in the production of unconventional oil in the United States and other parts of the world, and the recovery in production in Iraq and Libya, could result in a lower path for oil production in Kuwait than is assumed in the baseline or a larger drop in oil prices.⁵ The authorities felt that the emerging scenario in the global market was not clear and that the call on OPEC to fill the demand gap in crude oil would depend on the ability of non-OPEC suppliers to sustain shale oil production, as well as the cost of production. They agreed that both scenarios would see a more significant decline in oil export revenues, and if sustained would eventually result in a bigger adjustment in fiscal spending. Thus, in the current situation where oil prices are high, the authorities recognize that it will be important to save the additional oil revenues to further build fiscal buffers and develop the non-oil economy.

POLICY CHALLENGES

Staff and the authorities agreed that the main priorities were: (i) strengthening non-oil growth while continuing to save for intergenerational equity; (ii) aiming toward diversification and creating jobs for Kuwaitis in the private sector; and (iii) continuing to strengthen macroeconomic and financial stability to ensure a conducive climate for private investment.

A. A Macroeconomic Policy Mix to Strengthen Non-oil Growth

14. Staff and the authorities agreed that government will need to increase capital spending to advance social and physical infrastructure projects and boost non-oil growth.⁶ Benefiting from high oil prices in recent years, the government has been running large budget surpluses over the last decade. To determine the mix of investment and current expenditure, staff used a model-based analysis indicating that the government has the space to undertake this increased capital spending, while underlining the need to contain current spending further

⁵ In 2014, and over the medium term, the International Energy Agency's projections show that demand for OPEC crude is expected to fall in absolute terms, putting pressure on oil exporters to scale back output. Under a scenario of constant crude oil production of 2.8 million barrels a day (mbd) between 2014–18, the fiscal balance will still record a surplus of about 11 percent of GDP in 2018.

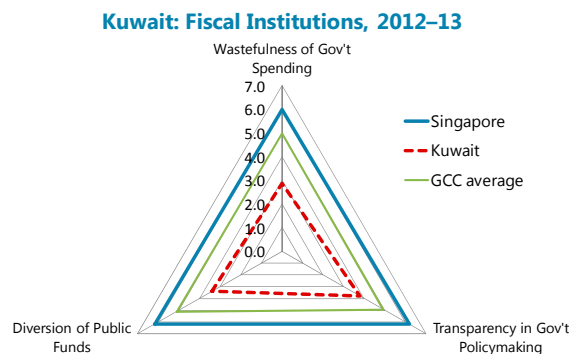
⁶ A previous staff study (IMF Country Report 11/217) has estimated an expenditure multiplier of 0.9–1.3 for Kuwait, with a higher effect of capital expenditure.

(discussed below).⁷ The investment profile projected by staff in the baseline is consistent with the authorities' plans and drives the medium-term non-oil growth projections. The overall fiscal stance (based on the non-oil balance as percent of non-oil GDP, excluding pension recapitalization) is expansionary until the beginning of FY 2014/15 and thereafter indicates consolidation, mitigating concerns of overheating.

15. Staff emphasized the importance of ensuring the quality and efficiency of spending.

Staff also stressed the importance of establishing a framework for coordination among the agencies responsible for the delivery of infrastructure projects to ensure timely implementation.

This would among others, call for a plan for prioritizing and sequencing capital projects that are growth creating. The authorities have identified and completed feasibility studies for a few priority projects such as power stations, water waste management, and schools and hospitals that can attract private sector participation. Staff highlighted the need for a review of the projects that have been identified but not yet been implemented as part of the next DP, with a view to achieve greater prioritization.



Sources: Global Competitiveness Report, 2012–13; and IMF staff calculations.

16. Over the medium to longer term, oil wealth should be conserved for future generations.

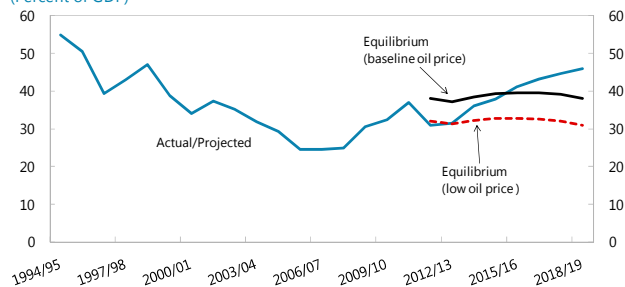
Kuwait's non-oil primary deficit is currently in line with the estimated baseline benchmark indicated by intergenerational equity considerations. However, in the medium term,

staff's analysis suggests that rising spending would lead to a non-oil primary deficit that exceeds the long-term sustainable level by 8 percent of GDP. Fiscal restraint through lower current spending growth and higher non-oil revenues is required to reduce the non-oil deficit gradually over the medium term. The implementation of the proposed measures to contain the non-oil deficit, however, should commence in the near term, since delays would result in the

widening of this deficit and require larger adjustment in the future. The need for medium-term fiscal restraint would be larger and more urgent in a scenario of lower oil prices. The authorities agreed that the structural imbalances in the government budget, inefficiencies in the labor market

Government Non-oil Primary Deficit, 1994/95–2018/19

(Percent of GDP)



Sources: Ministry of Finance of Kuwait; and IMF staff estimates.

Note: The baseline calculations assume long-term values of the real rate of return of assets, inflation, and population growth of Kuwaiti nationals of 4 percent, 2 percent, and 1.4 percent, respectively. Oil reserves are assumed to be depleted in 65 years and the oil price to be at \$89 per barrel in 2018 and remain constant in real terms thereafter. The lower oil price scenario assumes oil prices are 20 percent lower than in the baseline scenario (which leaves the 2013 average at around \$83 and the 2018 price at around \$71).

⁷ Optimal Fiscal Policy for Kuwait: How Much to Save and How Much to Invest, Selected Issues Paper I.

and the limited role of the private sector were the most prominent challenges facing the Kuwaiti economy, and a medium-term fiscal policy agenda together with a communication strategy will guide the reform process.

17. The authorities agreed with the policy measures proposed by staff to gradually reduce the non-oil fiscal deficit over the medium term and beyond.

- Containing the increase in government jobs and wages should remain the key focus. Curtailing the increase in government jobs and keeping the growth in government wages below inflation would result in saving of at least 0.7 percent of GDP per year, as well as reset expectations and realign incentives for Kuwaitis to work in the private sector.
- Developing non-oil revenue sources is important. Little progress has been made in building the non-hydrocarbon tax system. The only major reform took place in 2008, when the corporate income tax (CIT) rate was changed from a progressive to a flat rate of 15 percent for foreign companies. The existing CIT that is now imposed only on foreign companies could be applied to Kuwaiti companies. The Ministry of Finance is considering and internally discussing the recommendations of Fund TA in this regard. Staff also encouraged the authorities to work in concert with the other GCC countries in the implementation of the value added tax (VAT). The authorities are improving tax administration with the support of Fund and Bank TA for preparing the ground for introduction of VAT in the future.
- Subsidies, particularly for electricity and fuel (over 6 percent of GDP) engender wasteful consumption and need to be targeted. A gradual alignment with international prices while ensuring that a social safety net is in place, would in the long run increase overall efficiency and generate more fiscal space. The Ministry of Finance is planning to evaluate the existing subsidies. Conservation-oriented tariff structures could boost efficiency in power and fuel consumption. A communications campaign that raises awareness about the cost of subsidies and the benefits of reform is essential to generate broad public support.

18. The authorities agreed that it is time to restrain current spending and they intend to develop a realistic and pragmatic medium-term policy document to drive reforms. They agreed that rising current expenditures, particularly on account of wages and fuel and electricity subsidies had led to a significant increase in the size of the budget over the past few years. The increase in the government wage bill has been compounded by the need to absorb Kuwaitis entering the workforce, since the private sector is not absorbing them. On the revenue side, they explained that any increase in the fee structure, for example with regard to electricity charges, would need an amendment to existing legislation.⁸ They, however, stressed that Kuwait's financial strength afforded the adoption of a gradualist approach to reforms that takes into consideration, among others, absorption capacity and an appropriate communication strategy to generate broad public

⁸ In the meantime, the government is in the process of implementing an invoice system for electricity bills to improve service collection, and to increase greater transparency in the billing process.

support. They emphasized that fiscal reforms would need to be complemented by changes in the entitlement culture of the people, enhanced education, and promotion of entrepreneurship.

19. The authorities recognize the benefits of developing a formal medium-term budget framework, strengthening the capacity of the macro-fiscal unit, and publishing fiscal data in GFSM 2001 format over the medium term. These reforms would better integrate the five-year DP into the annual budget planning process, look at the impact of current year commitments in a multi-year context, and identify fiscal risks on the revenue and expenditure sides. To support this framework and strengthen controls on line ministries, the introduction of Government Financial Management Information System (GFMIS) is important. The macro-fiscal unit in the Ministry of Finance, established with Fund TA, needs to be strengthened in analysis and capacity, to help link budget policies to macroeconomic objectives and to deepen the understanding of how fiscal decisions affect the real economy.⁹ The Fund resident advisor can help achieve these objectives. Lastly, fiscal planning and transparency would be helped by the production and publication of data in line with GFSM2001 standards.

20. The current accommodative monetary policy stance is appropriate. Current liquidity conditions are supportive of emerging demand for credit. Banks should continue to be vigilant toward credit risks and continue to strengthen risk management. In the context of the currency basket exchange rate peg, in the event of a tightening of global financial conditions, the authorities should continue to be proactive in liquidity management and the use of macroprudential policies to contain emerging financial risks. The central bank has a range of instruments in its macroprudential toolkit, including limits on debt service-to-income ratios, time-varying loan-to-deposit ratios, sectoral concentration limits, and differential risk weights for loans, which it is ready to use flexibly as the situation warrants. The authorities saw merit in staff's advice to further deepen the domestic money market in a phased manner, but felt that CBK bills issuances of 3- and 6-month maturity are presently serving the purpose of absorbing liquidity from the market.

21. Staff supports maintaining the exchange rate peg to a basket, as it has provided a strong and credible monetary anchor. Assessment of the exchange rate using the macrobalance approach (MB) suggests that the currency is broadly in line with fundamentals (Appendix I). The equilibrium real effective exchange rate (EREER) approach suggests that the real exchange rate is currently in line with its estimated long-run equilibrium. The MB estimate is very close to the projected current account and implies no misalignment either. The external sustainability (ES) approach shows a wide range of current account benchmarks, implying both undervaluation (based on real annuity) and overvaluation (based on real per capita annuity) and making it difficult to draw any definitive conclusions using this methodology (Appendix I). The

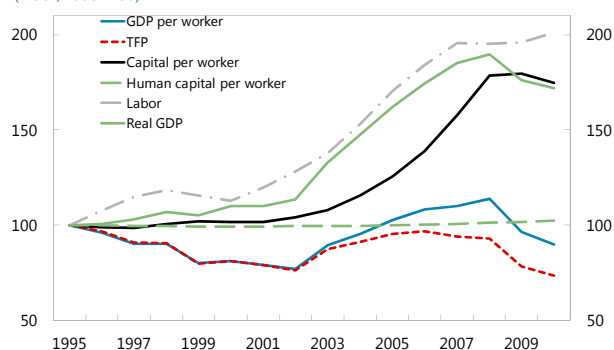
⁹The macro-fiscal unit, which was established in 2011, is staffed and operational. The unit issues regular reports on fiscal performance, inflation developments, and the oil sector. In addition, the Unit was responsible for preparing a Citizen's Budget, the first of its kind in the GCC. The focus of the Unit is on refining forecasting and macroeconomic analysis, as well as providing support to the planned introduction of medium-term budget framework in Kuwait.

authorities indicated that the basket peg has served them well, among others, in managing the impact of imported inflation, ensuring the stability of the Kuwaiti Dinar against major currencies, and simplifying government budget formulation process. In the meantime, reforms that would support a more flexible arrangement if it becomes appropriate at a later date, such as further deepening the money market and developing the local bond market, should continue.

B. Diversification and Job Creation for Nationals in the Private Sector

22. The authorities recognize the challenges to diversifying the economy. Despite a less concentrated output structure—hydrocarbon accounts for about 63 percent of output—export diversification is lacking: oil and oil products constitute more than 95 percent of goods exports (Figure 9) (Selected Issues Paper II). The current model supporting growth by importing cheap labor has worked well so far. Non-nationals represent a significant share of the labor market. However, this has created distortions in the form of low productivity growth and lack of economic diversification. Moreover, strong reliance on oil revenues has increased income volatility and risks to long-run growth.

Growth Decomposition, 1995–2010
(Index, 1995=100)



Sources: Country authorities; and IMF staff calculations.

23. Economic diversification into areas with potential for greater national employment requires an integrated strategy and continuing efforts. The rapidly increasing national youth labor force calls for a sustained increase in non-oil growth, investment in education, and labor market reforms (Box 1). At the same time, reducing Kuwait's dependence on oil requires reforms to spur diversification. In addition to identifying strategic areas for diversification, structural reforms will be required for improving the business environment, and promoting a greater role for small and medium enterprises (SMEs). The authorities are creating special economic zones, which will partly alleviate the scarcity of land availability to the private sector and attract investment. A strategy for making land available for investment would be desirable. Promotion of export-oriented industries would further support diversification efforts. An avenue to improving export diversification would be to enhance current non-oil exports and support the entry into new product markets to generate productivity gains. Manufacturing has strong potential to create a mix of various tradable goods, and there is also scope to expand the role of tradable services. Mainly to provide financing to the SME sector, the authorities recently set up a national fund for SMEs with a corpus of KD2 billion (approximately \$7 billion). Efforts are also being directed toward mitigating the nonfinancing barriers such as land availability and support services.

24. The passage of a number of new laws is a step in the right direction to encourage private sector development. The passage of the new Company law, the establishment of an institutional framework for public-private partnerships (PPPs) and the recently introduced Direct Investment Promotion Law are aimed at enhancing the confidence of investors and increasing investments in Kuwait. Several new pieces of legislation that are still in development, including laws for bankruptcy, transparency, public tenders, and competition need to be promulgated. At the same time, measures such as the writing-off of interest payments and rescheduling a part of the household debt create moral hazard for banks and borrowers, are counterproductive to building an efficient financial culture and a credible business environment, and in staff's views, should be avoided in the future (Box 2).

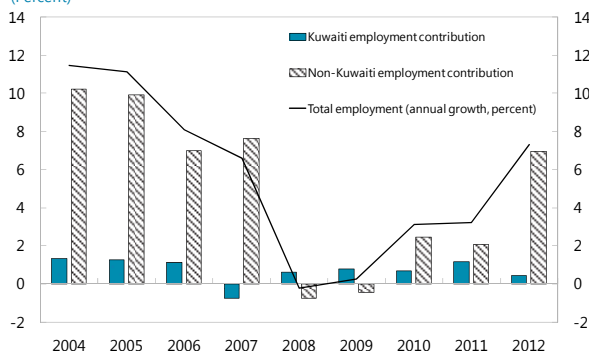
25. Staff welcomes the authorities' efforts to increase the transparency, governance and effectiveness of public administration. The adoption of the anti-corruption and anti-money laundering and countering the financing of terrorism (AML/CFT) laws and the establishment of the anti-corruption authority are part of the authorities' efforts to address these issues. The authorities are streamlining some bureaucratic processes, and have made progress to reduce the lag for issuing licenses for new businesses through the establishment of a single-window system. The momentum in these reforms needs to be sustained to enhance investor confidence.

Box 1. Kuwait Labor Market Reforms

Between 2012–16, staff projects 74,000–112,000 Kuwaitis would enter the labor market. The private sector is projected to create 17,000 jobs for Kuwaitis, and without significant structural reforms, the government will feel the pressure to absorb the remaining entrants at a faster pace than in the past, further increasing government employment by 13–22 percent (with a fiscal cost of less than one percent of GDP per year).¹ Currently, 90 percent of Kuwaiti workers are employed in the public sector and 90 percent of non-Kuwaiti workers are in the private sector.²

Employment Growth and Contributions, 2004–12

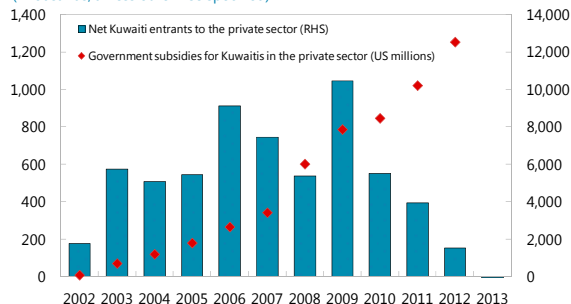
(Percent)



Sources: Country authorities (Table 11, Statistical Appendix); and IMF staff calculations.

Net Kuwaiti Entrants to the Private Sector, 2002–13

(Thousands; unless otherwise specified)



Sources: Country authorities; and IMF staff calculations.

Note: Entrants include employed and job seekers in the private sector. 2013 entrants are those up to mid-September.

The current labor market structure is not providing incentives for Kuwaitis to work in the private sector.

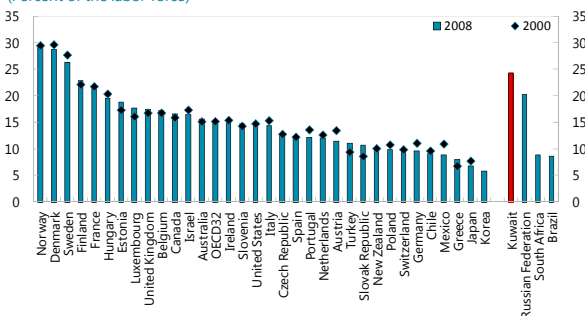
Currently, there is a large wage differential between public and private sector jobs, which creates a disincentive to work in the private sector. While existing subsidies for Kuwaitis working in the private sector (in the form of permanent allowances offered to all nationals in the private sector) partly alleviate the wage differential, frequent increases in government wages (like the 25 percent increase in 2012) erode the subsidy.³ Job security and higher benefits (including less hours of work) will continue to attract Kuwaitis to the public sector. In addition, the generous Kuwaiti pension system (paying around \$125,000 per year to a retiree) stipulates a low retirement age (40 for women and 49 for men) decreasing the incentive to pursue higher education and a career in the private sector where relatively higher wages are achieved only after years of experience.

Kuwaitis need appropriate incentives in order to pursue private sector employment. To help attract Kuwaitis to the private sector, it is important to contain wages of public employees and to further develop the work culture among Kuwaitis. Moreover, subsidies could be better targeted by excluding high earners in the private sector where the subsidy is not needed.

Box 1. Kuwait Labor Market Reforms (concluded)

Employment in General Government, 2000 & 2008

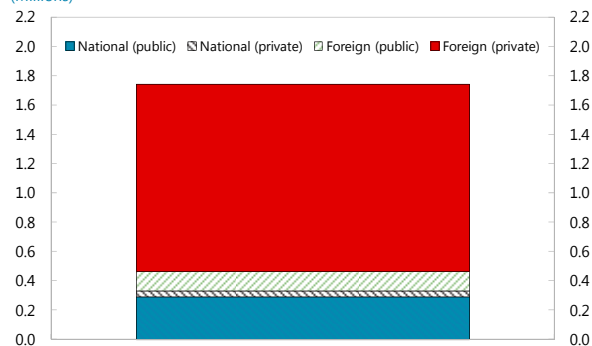
(Percent of the labor force)



Sources: OECD/Library; International Labor Organization (ILO) and LABORSTA database. Note: Data for Turkey are from the Ministry of Finance and the Turkish Statistical Institute. Data for Japan for employment are from the Establishment and Enterprise Census. Data for Korea were provided by government officials. 2011 data for Kuwait were obtained from 2011 Annual Statistical Abstract from CSB.

Employment by Sector and Nationality, 2011

(Millions)

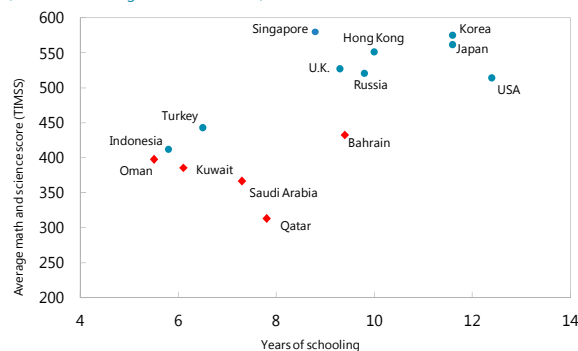


Source: Country authorities.

The government is initiating labor market reforms aimed at reducing the share of foreign workers in the labor force and absorbing Kuwaiti entrants. Recent policies include expelling illegal foreign workers, centralizing the administration of work permits in the private sector for foreign workers to better regulate the inflow of labor, and updating the quotas system to ensure that jobs exist for Kuwaitis in the private sector. In addition, the government is pursuing diversification policies to enhance the private sector and SMEs.

Length and Quality of Education, 2011

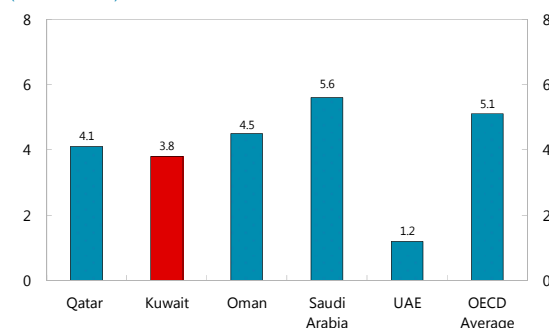
(Years of schooling and TIMSS scores)



Sources: Country authorities; UNDP; and IMF staff calculations.

Education Expenditure, 2010

(Percent of GDP)



Sources: Country authorities; UNDP; and IMF staff calculations.

Proper training of Kuwaitis is essential to increase employment opportunities for Kuwaitis in the private sector. Kuwait shows relatively low public spending in education and weaker educational achievement suggesting that there is scope for the government to contribute to enhancing Kuwaiti’s human capital. Moreover, like in other GCC countries, larger government training programs could be put in place in Kuwait, to help Kuwaitis succeed in private sector jobs. Following Bahrain’s successful 2004 labor market reform, Kuwait could consider the adoption of an unemployment insurance scheme that requires participation in training.

1/ Projection for private sector employment for nationals is linked to projected 5 percent non-oil GDP growth. 2012 Selected Issues Paper “Population and Employment Trends in Kuwait” provides further details on the estimation.

2/ Foreigners amount to 68 percent of the population, and foreign workers are 78 percent of the labor force: around 70 percent of government employees are Kuwaitis while about 95 percent of private sector employees are non-Kuwaitis (2011 Annual Statistical Abstract, Central Statistical Bureau).

3/ The 2013/2014 government budget provides for \$1.6 billion in subsidies for Kuwaitis in the private sector. As of mid-September 2013, approximately 55,500 Kuwaitis working in the private sector received government subsidies, while approximately 7,400 Kuwaitis received subsidies as job seekers in the private sector.

Box 2. Bank Household Debt Restructuring

In April 2013 the government passed the Family Support Fund Law, under which the government will buy an estimated \$2.6 billion of outstanding non-Islamic banks' and investment companies' consumer and installment loans and reschedule repayment after waiving interest.¹ The government will set up the Family Support Fund to buy from banks outstanding loans taken before March 30, 2008. This would constitute 10 percent of total outstanding consumer and installment loans of banks at end-June 2013. The scheme is estimated to benefit around 50,000 Kuwaitis (4 percent of nationals). These loans will be rescheduled over a period not exceeding 15 years. The motivation for this law relates to the fulfillment of a debt-relief election promise from December 2012.

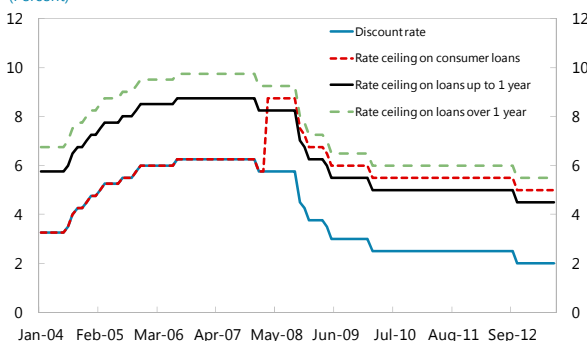
The direct initial financial cost of the plan is small, in terms of its limited impact on public debt sustainability and the available fiscal space. The restructured debt constitutes about 1.6 percent of GDP, amounting to 2.2 percent of total revenues and 2.6 percent of hydrocarbon revenues in 2012. The cost to the government is frontloaded and is expected to be amortized over the rescheduled period of the loan.

The projected cost for banks is not expected to be high. Banks will benefit from the restructuring to the extent the restructuring would remove nonperforming loans from their balance sheets.² Banks will bear minor administrative costs for transferring the loans to the government and also the return differential between the loans repaid by the government and banks' related new assets. The cost to the financial system is estimated by staff at \$185 million (small compared to \$4 billion in pre-tax net income in 2012 for the top 7 banks).³

Good principles for household debt restructuring include restoring viability of borrowers while mitigating moral hazard, minimizing the direct fiscal cost by targeting borrowers, reducing bank failure risks, and transparency and accountability in the use of public funds.⁴ While Kuwait's restructuring restores viability of borrowers, it only partly mitigates moral hazard as the targeting still includes borrowers who were fully performing. There is no evidence that NPLs on the restructured loans were high or that financial stability was at risk although targeted loans were issued during the pre-crisis period when consumer and installment loans were growing strongly at around 15 percent per year.

CBK Discount and Lending Rates' Ceilings, 2004–13

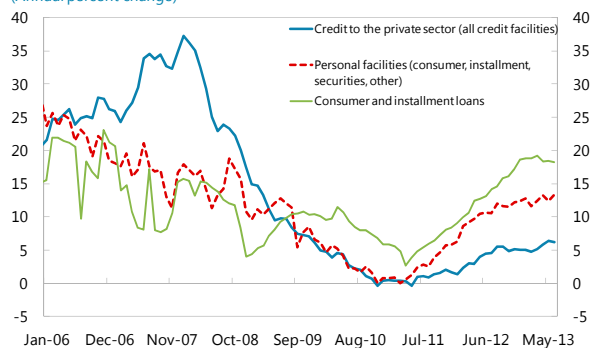
(Percent)



Sources: Country authorities; and IMF staff calculations.

Private Credit, 2006–13

(Annual percent change)



Sources: Country authorities; and IMF staff calculations.

Box 2. Bank Household Debt Restructuring (concluded)

The restructuring is counterproductive to building an efficient financial culture. The write-off of interest payments and debt restructuring for Kuwaiti nationals would create moral hazard for banks and borrowers, thereby undermining the development of a sound credit culture. While CBK regulation caps total loan installments at 40 percent of salary, the restructuring creates incentives for excessive borrowing by households and excessive risk taking by banks at a time when consumer and installment loans are already growing strongly (see figure). It will be important in Kuwait to strengthen the legal, institutional and regulatory framework for an effective personal bankruptcy framework and enforcement of creditor rights.

^{1/} CBK defines "Consumer Loan" as a loan granted by local banks to the customer with the purpose of financing purchase of his/her personal needs in terms of consumable and durable commodities, or for covering expenses for education or medication. An "Installment Loan" is a loan utilized by the customer for non-commercial purposes, particularly for restoration or purchase of private residence.

^{2/} Overall NPLs are 4.6 percent while net NPLs for targeted loans are 1.2 percent as of mid-2013.

^{3/} This assumes that all targeted loans join the fund and that they had interest rates of 7 percent, while the new assets generate a 4.5 percent return to the banks over a remaining maturity of 5 years (included figure shows prevailing ceiling rates).

^{4/} "Principles of Household Debt Restructuring," by Luc Laeven and Thomas Laryea, IMF Staff Position Note, SPN/09/15, June 2009.

26. Well-functioning local debt markets can make a vital contribution to the efficiency of financial intermediation. A deep and liquid domestic debt market will provide longer-term or more competitive sources of funding for public debt as well as corporate, housing, and infrastructure investment than may be available from the banking system. The government and the central bank have an important role to play in the process of developing the legal, institutional and regulatory infrastructure. The central bank has taken initiatives to develop the yield curve by issuing 3- and 6-month maturity CBK bonds and 1- to 10-year maturity Treasury bonds. These bonds are issued based on liquidity needs of the banking system, with a preannounced coupon rate. Staff encouraged the authorities to consider publishing an issuance calendar, increasing the size of issuances, and activating a price-based auction system in the future to create a more liquid benchmark yield curve. The authorities did not see the immediate need for an issuance calendar in view of the lack of sustained demand by banks for long-term bonds, but indicated that they would be willing to consider these options when circumstances warrant a change.

27. Staff and authorities agreed that an active labor market policy is required to encourage nationals to enter private sector jobs. The success of recent policies aimed at increasing the share of Kuwaitis in the labor force hinges on providing Kuwaitis with incentives to work in the private sector. While the existing subsidy system enhances the salaries of Kuwaitis working in the private sector and encourages job search by Kuwaitis in the private sector, the recent increase in government salaries has once again widened the wage gap between the public

and the private sectors and eroded the subsidy.¹⁰ The large wage differential poses strong incentives for nationals, particularly those who are less educated to prefer public-sector employment.

28. The authorities recognized that closing the gap between public and private sector wages by containing the growth of public-sector jobs and wages was necessary, but noted the pressure to create government jobs for nationals if private sector job opportunities did not materialize. To increase the role of the private sector in the economy, the authorities underscored the importance of developing a good work culture, improving education, and fostering entrepreneurship and SMEs. An integrated plan that coordinates the efforts from involved institutions for job creation in the private sector is called for, some elements of which will include coordinating with the private sector in setting up skill improvement programs, enhancing the educational quality and vocational training, promoting female labor force training and participation, and encouraging entrepreneurship. The government's focus on developing SMEs and existing programs to raise awareness of private sector jobs has the potential to enhance private sector employment.

C. Strengthening Macroeconomic and Financial Stability

29. High capitalization, continued profitability, declining NPLs, and high provisioning of the banking system support financial stability. Credit risk is the most significant risk for the Kuwaiti consolidated banking system, a natural outcome of the business model of banks, accounting for 90 percent of their risk-weighted assets. The risk is concentrated in the real estate sector, as banks direct exposures to this sector constitute 18.5 percent of total loans at end-June 2013. The banking system's exposure to the equity market makes up for 23 percent of its total investments (total investments make up for 12 percent of total assets), and the use of firms' shares as collateral accounts for 32 percent of total collateral, the remaining predominantly in real estate. The banking system's exposure to ICs has been contained at 4.8 percent of total loans at end-June 2013, and they are fully provisioned against the troubled ICs, mitigating credit and investment risks from the ICs sector. Liquidity risk of the banking system is well contained as one-third of banks' assets are liquid. Moreover, wholesale foreign liabilities of banks were only 6 percent of the total balance sheet size at end-May 2013.

30. The banking system is resilient to potential shocks. Banks are well regulated by the CBK and had an average capital adequacy ratio of 18.3 percent (Tier 1 capital of 16.6 percent) at end-June 2013. Gross NPLs declined to 4.6 percent at end-June 2013 from 5.2 percent at end-2012 (Figure 10).¹¹ Banks had a provisioning ratio of 107 percent at end-June 2013. Staff's analysis shows that even under severe stress testing scenarios with credit risk mitigants and loss given default, the combined tier-1 capital of the banking system will remain above the regulatory

¹⁰ The subsidy was meant to be temporary but it has become open-ended and proliferated in the budget.

¹¹ The CBK has an additional category of NPLs called "Special mention" (with delinquency of less than 90 days).

minimum of 8 percent on average (Selected Issues Paper III).¹² Results of the central bank's stress testing exercise also show that banks are well placed to withstand credit, market, and liquidity shocks under a wide range of micro- and macroeconomic scenarios. Recent regulations introduced by the central bank, such as a stable funding ratio requirement replacing the loan-to-deposit ratio, corporate governance code, draft guidelines for the implementation of Basel III, stricter provisioning norms, will further strengthening risk management by banks.

31. ICs have large exposures to domestic, regional, and international equity and real estate markets, which make them vulnerable to market swings.¹³ The ICs sector continued to record losses in 2012, though progressively lower since 2008. They are also exposed to regional and global asset markets, with foreign assets constituting 48 percent of total assets. Despite considerable deleveraging, foreign liabilities of ICs account for 22 percent of total liabilities at end-May 2013. In the absence of an adequate bankruptcy/restructuring framework, the timeframe and the legal process under which weak and unviable ICs have been restructuring have remained protracted. The liquidation/foreclosure proceedings have been lengthy and Kuwait's performance compares less favorably with the experience of GCC countries and international experience. The CBK emphasized that the risks posed by the ICs sector to financial stability are contained by the lower exposure of the banking system to the ICs sector. The CMA has delisted ICs from the stock exchange when restructuring and recapitalization have not been possible. The authorities agreed that the progress in restructuring a few companies was slow, and are currently working towards implementing a resolution framework in consultation with the World Bank.

32. The authorities and staff agreed that notwithstanding the strength of the banking system, there is room for improving asset quality, profitability, liquidity and capital adequacy. The interconnectedness among banks, industrial and commercial groups, sovereign and investment companies can pose a risk to the financial system and the economy during periods of stress.

- **There is scope for refining the existing macroprudential toolkit.** The CBK has many of the tools that can help address vulnerabilities at an early stage, as well as help build buffers to absorb shocks ex post. In the area of building and maintaining buffers, the CBK has been relying strongly on high capitalization of banks and building provisions. This would be usefully complemented by an enhanced role for Pillar 2, and a further strengthening of risk-based supervision. While CBK already has time-varying loan-to-deposit ratios to alleviate procyclicality, time-varying loan-to-value ratios could help contain exposure to the real

¹² To assess the sensitivity of banks' capital ratios to credit risk mitigants, a 15 percent and 50 percent reduction in the value of collateral was assumed. Stress tests were also conducted based on Loss-Given Default (LGD) at about 50–60 percent and Probabilities of Default (PoDs) of 0.1–10 percent in the central scenario and 0.15 to 25 percent in the severe stress scenarios.

¹³ The total on-balance sheet exposure of conventional and Islamic ICs stood at \$25 billion at end-May 2013. In addition, total assets under management by ICs were \$67 billion at end-May 2013.

estate sector and reduce credit concentration. CBK is developing its regulation to comply with Basel III requirements by end-2013.

- **The independence of the central bank needs to be strengthened, a view that the authorities welcomed.** The CBK should be provided with an enhanced mandate for institutional and functional autonomy, balanced by strengthened governance and accountability. Staff welcomes the publication of the first Financial Stability Report. Staff and the authorities agreed that to build on the current progress in improving regulation and supervision, the development of a more formal macroprudential policy framework would be desirable. It should entail the inclusion of a financial stability mandate to the CBK, and defining a coordination framework between the relevant supervisory institutions. Strengthening the CBK's autonomy along with the legal underpinnings to establish and chair an appropriate form and mechanism of coordination for financial stability, with both preventive and crisis management responsibilities would enhance the ability of the authorities to deal with systemic risk.
- **The expansion of Kuwaiti banks abroad is an opportunity to diversify their portfolio and earnings but also poses risks.** CBK is conducting onsite supervision of banks' foreign branches and subsidiaries and collaborating, engaging, and sharing information with other host supervisors. In line with the Basel Committee views, further strengthening cooperation with the most important host supervisors of Kuwaiti banks would be desirable. Going forward, improvements in the resolution framework, consistent with the Financial Stability Board guidelines would help facilitate the coordinated resolution of financial institutions that are active in multiple countries.
- **The current restructuring of ICs needs to be expedited.** Further strengthening the regulatory oversight, greater information disclosure, and consolidation are needed to strengthen the ICs sector. Staff recommended the initiation of a thorough review of the investment companies segment, with particular focus on their objectives and role in the economy, and financial viability. Some consolidation would be desirable for reducing ICs' operating and regulatory compliance costs and increasing efficiency, which staff and the authorities agreed should be market based. Currently, the CMA is focused on strengthening the regulation of ICs and implementing corporate governance codes, but it does not have plans to initiate a review to evolve an integrated strategy for this sector (Appendix II).¹⁴
- **Greater information disclosure is needed to help assess and monitor risks in the ICs sector.**

33. The new AML/CFT law is a welcome development. The Kuwaiti cabinet recently discussed a draft decree, authorizing the creation of a new financial intelligence unit (FIU). Staff

¹⁴ It has issued new regulations on investment funds (including on asset managers, custodians, controllers, permissible funds and activities, investment guidelines, valuations, alternative managers), brokerage activity, information disclosure, and corporate governance.

looks forward to the development of procedures to freeze terrorist assets, and the establishment of a fully operational and independent FIU.

D. Other Issues

34. While there has been good progress in improving Kuwait's statistical system, staff encourages the authorities to continue their efforts in all areas of economic data. In addition, Kuwait would benefit from the cooperation with GCCStat, the new statistical agency of the Gulf countries, in standardizing and disseminating the data.

STAFF APPRAISAL

35. The economic outlook is expected to improve in 2013 and remain robust in the medium term. During 2014–18, a large public investment program will support an average real growth of close to 5 percent in the non-oil sector. Achieving this growth rate requires political commitment to place the public investment program and structural reforms on track. In addition, it is important to establish a framework for coordination among the agencies responsible for the delivery of infrastructure projects to ensure timely implementation.

36. The fiscal position is strong, but a sustained drop in oil prices would deplete fiscal surpluses. While there is fiscal space to increase capital spending, intergenerational equity considerations warrant containment of current spending. Overall, a phased reduction in the non-hydrocarbon fiscal deficit by 8 percent of GDP (16 percent of non-oil GDP), relative to the projected path, is essential over the medium term to continue saving for future generations. Fiscal restraint through lower current spending growth, particularly wages and subsidies, and higher non-oil revenues is required to reduce the non-oil deficit gradually over the medium term. The implementation of the proposed measures to contain the non-oil deficit should, however, commence in the near term, since delays would result in the widening of this deficit and require larger adjustment in the future.

37. Strengthening the macro-fiscal unit would support fiscal policy making and the development of a medium-term budget framework to ensure the efficiency of public spending. A solid medium-term expenditure framework would help manage the path of fiscal spending consistent with Kuwait's Development Plan.

38. Expediting the restructuring, further implementing the regulatory oversight, greater information disclosure, and consolidation are needed to strengthen the ICs sector. An integrated strategy is required to ensure the sustained financial viability of these companies, and to determine their role in the economy.

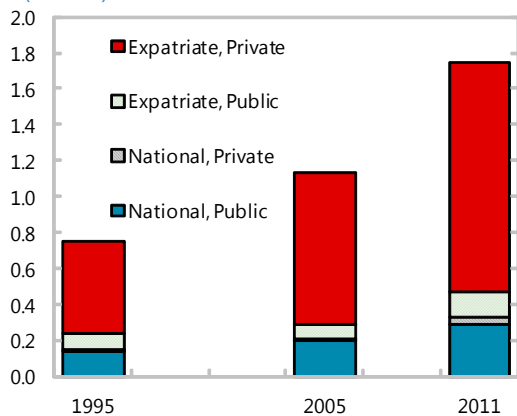
39. The banking system is well regulated and resilient to risks. Nevertheless, there is scope for continuous refining of the macroprudential toolkit to sustain the strength of the banking system and mitigate systemic risks. Strengthening the central bank's autonomy and legal underpinnings for macroprudential supervision would enhance the ability of the authorities to deal with systemic risk.

- 40. An active labor market policy is required to encourage nationals to enter private sector jobs.** Additional reforms would help in containing growth in public-sector employment and wages, to reset and realign incentives toward private sector employment, setting up skill improvement programs, enhancing the educational quality and vocational training, promoting female labor force training and participation, and encouraging entrepreneurship.
- 41. Economic diversification into areas with potential for greater national employment should constitute a key priority.** Structural reforms will be required for improving the business environment, and promoting a greater role for SMEs. Manufacturing has strong potential to create a mix of various tradable goods, and there is also scope to expand the role of tradable services.
- 42. More needs to be done for improving the investment climate, including through streamlining bureaucratic practices.** Infusing greater transparency, governance and effectiveness of public administration will help increase confidence of investors. While the adoption of the anti-corruption and anti-money laundering laws and the establishment of the anti-corruption authority are welcome developments, establishment of an operationally independent FIU will contribute to bolstering the authorities' and improving the business climate.
- 43. Well-functioning local debt markets can help the diversification process** by providing longer-term or more competitive sources of funding for corporate, housing, and infrastructure investment than may be available from the banking system. The government and the central bank have an important role in this process of strengthening the legal, institutional and regulatory infrastructure.
- 44. There is scope for further improvements in economic statistics,** particularly in the area of national accounts, compilation of the International Investment Position, application of a budget classification consistent with GFSM 2001, labor market statistics and real estate statistics.
- 45. It is recommended that the next Article IV consultation take place on the standard 12-month cycle "in accordance with the *Decision on Article IV Consultation Cycles* (Decision No.14747-(10/96) as amended."**

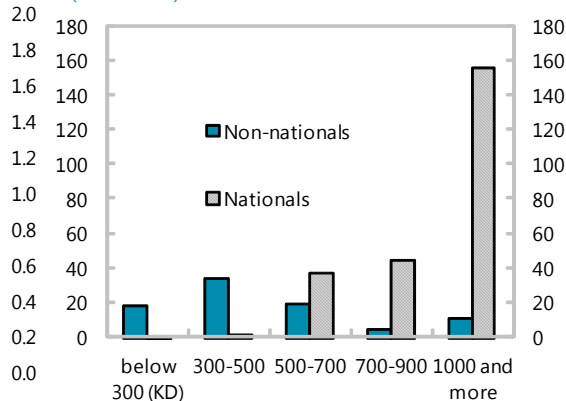
Figure 2. Labor Market Indicators

Kuwaitis are employed mostly in high-earning public sector jobs

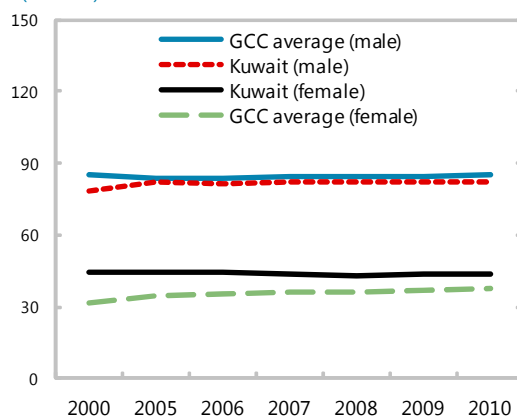
Employment by Sector and Nationality, 1995–2011
(Millions)



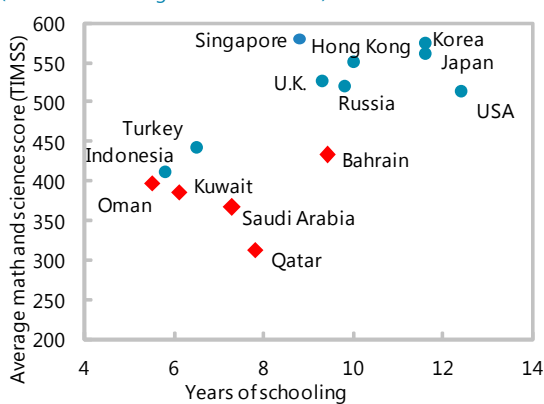
Public Sector Employees by Wage Group, 2012
(Thousands)



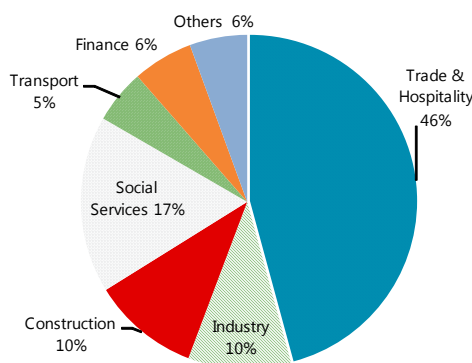
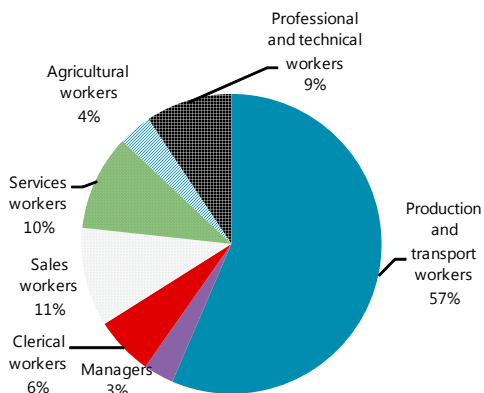
Labor Force Participation, 2000–10
(Percent)



Length and Quality of Education, 2011
(Years of schooling and TIMSS scores)



Expatriate Workers in the Private Sector by Occupation, 2012 **Expatriate Workers in the Private Sector by Sector, 2012**

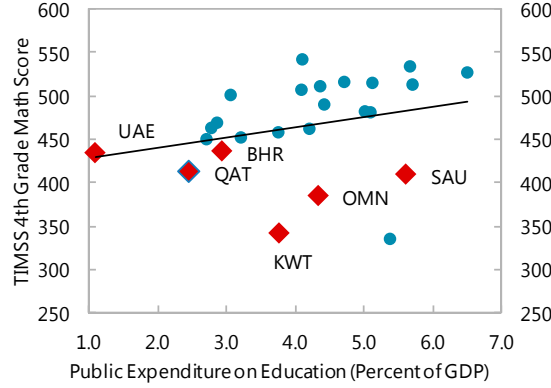


Sources: Country authorities; UNDP; and IMF staff calculations.

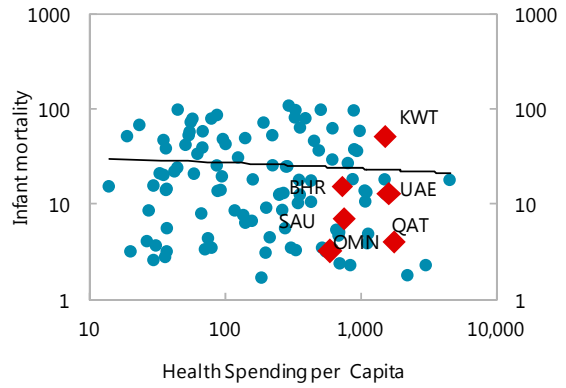
Figure 3. Social Indicators

Kuwait has improved in social indicators but is lagging behind given its high income

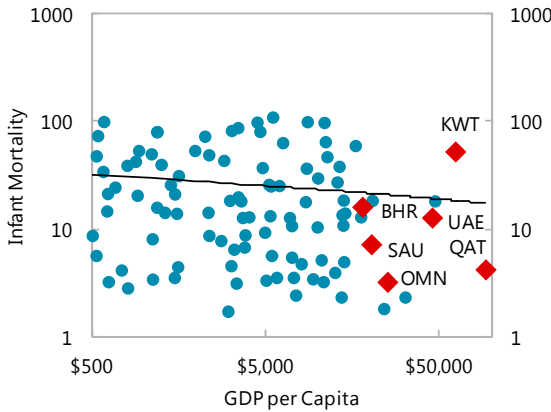
Public Expenditure on Education and GDP per capita, 2008 (Or latest)



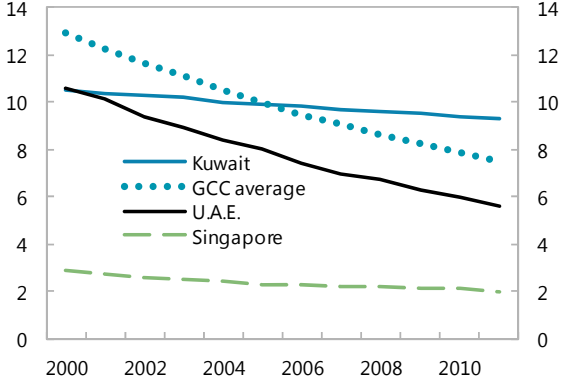
Public Expenditure on Health and Infant Mortality, 2011 (Or latest)



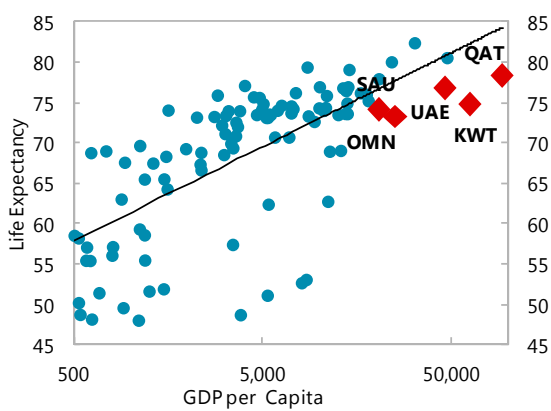
Infant Mortality and GDP per capita, 2008



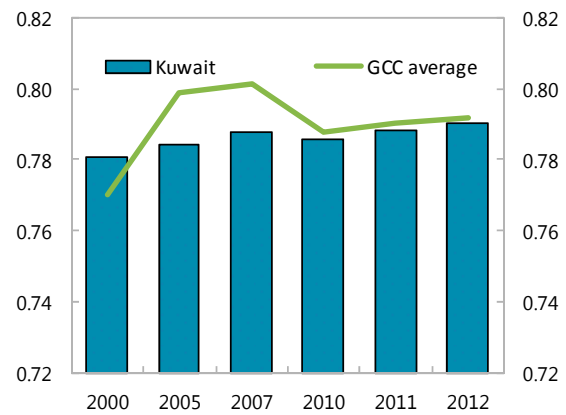
Infant Mortality, 2000–11 (Per 1000 live births)



Life Expectancy at Birth and Per Capita GDP, 2011 (Or latest)



Human Development Index, 2000–12

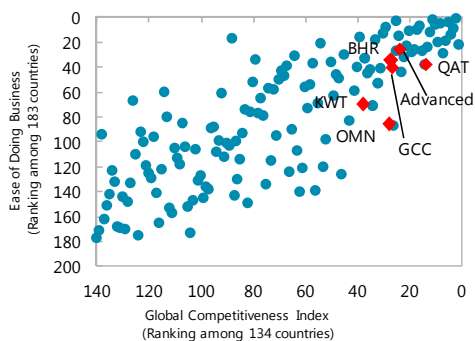


Sources: Country authorities; UNF; and IMF staff calculations.

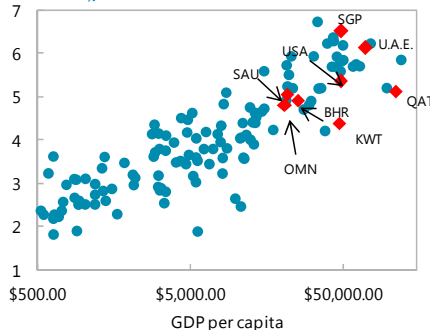
Figure 4. Institutions and Governance

Kuwait has lagged behind in the quality of its institutions and regulations

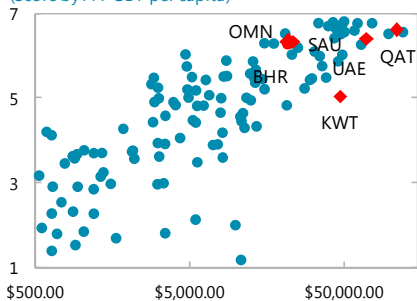
Doing Business vs. Global Competitiveness Index, 2012



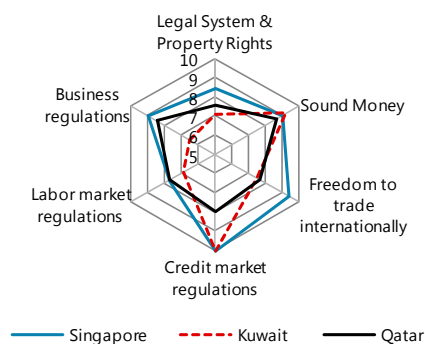
Quality of Infrastructure (7 - "meets the highest standards in the world"), 2012



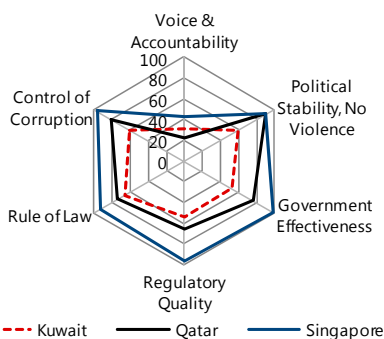
Quality of Electricity Supply (7 - "meets the highest standards in the world"), 2012
(Score by PPP GDP per capita)



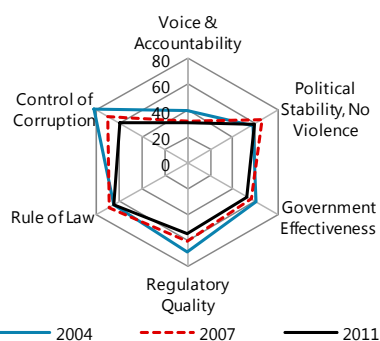
Economic Freedom Indicators, 2012



World Governance Indicators, 2011



Kuwait: Governance Indicators 2004-11

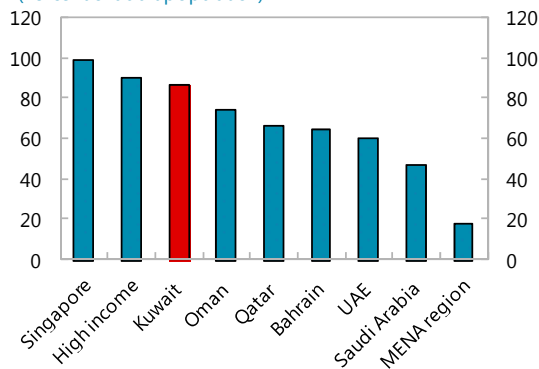


Sources: World Bank: *World Governance Indicators*; Fraser Institute: *Economic Freedom in the World*; UNDP: Human Development Index, TIMSS.

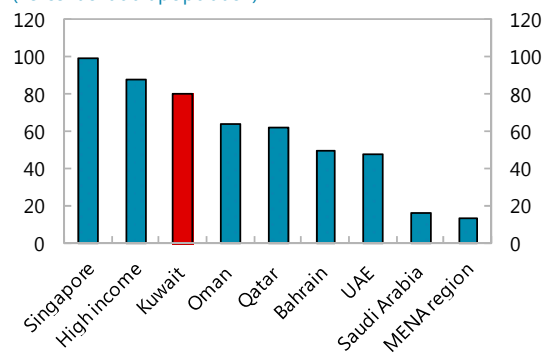
Figure 5. Financial Inclusion Indicators

Kuwait has done comparatively well in providing financial services to the population

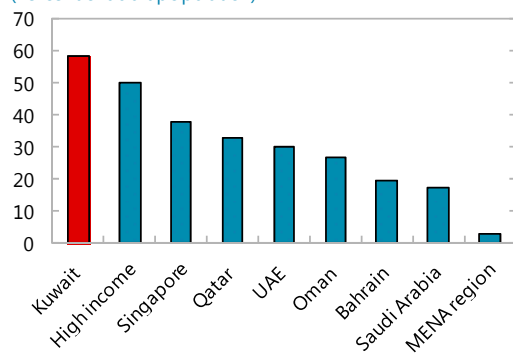
Account at a Formal Financial Institution, 2011
(Percent of adult population)



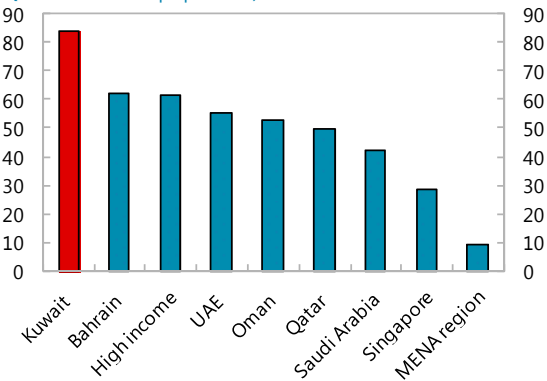
Account at a Formal Financial Institution (Female), 2011
(Percent of adult population)



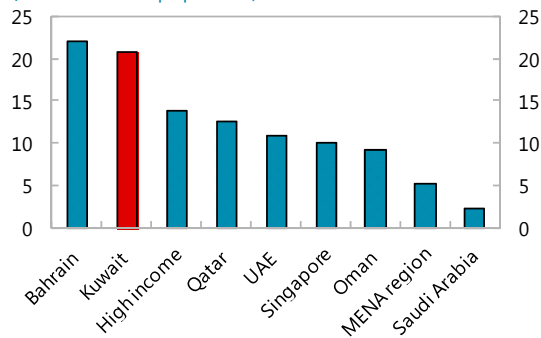
Credit Card, 2011
(Percent of adult population)



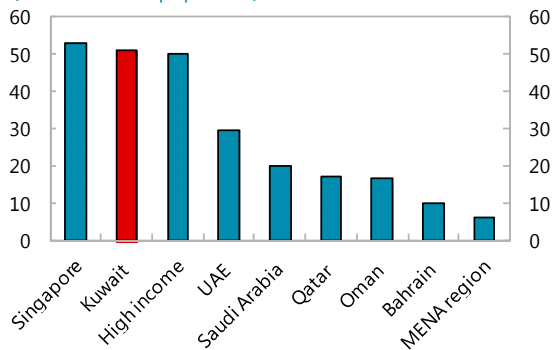
Debit Card, 2011
(Percent of adult population)



Loan From a Financial Institution in the Past Year, 2011
(Percent of adult population)



Account Used to Receive Wages, 2011
(Percent of adult population)

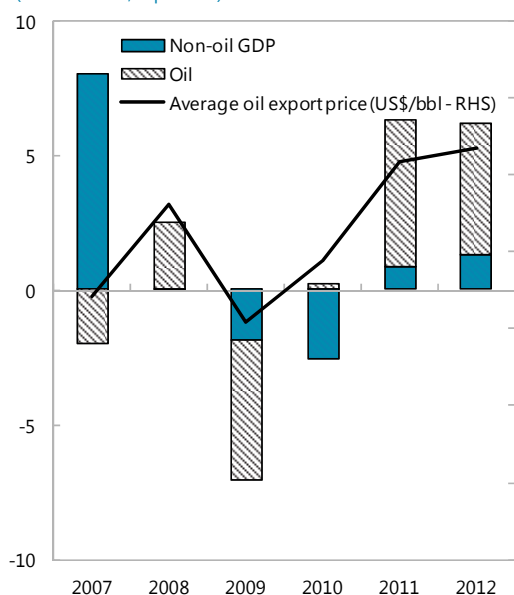


Source: Global Financial Inclusion Database, World Bank.

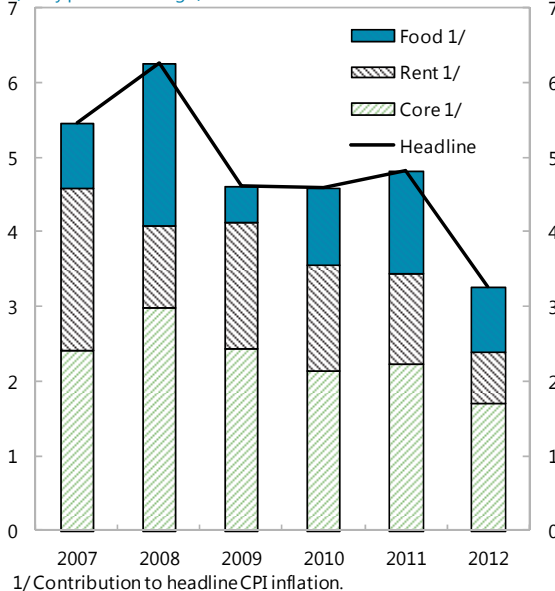
Figure 6. Recent Macroeconomic Developments

Non-oil growth picks up as spending increases, inflation is stable, and twin surpluses are large

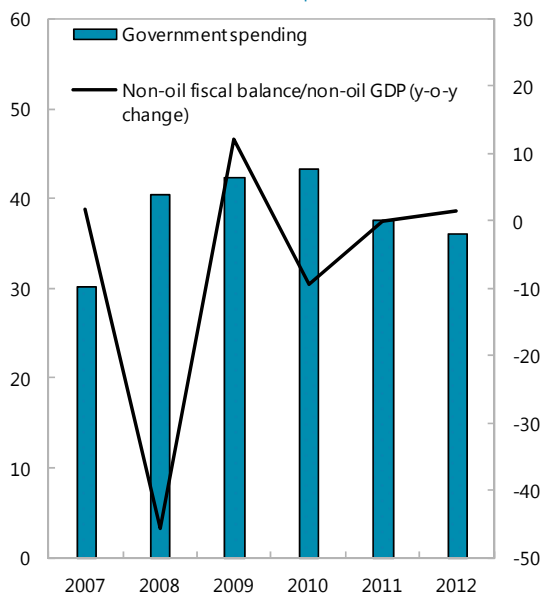
Real GDP Growth, 2007–12
(Contribution; in percent)



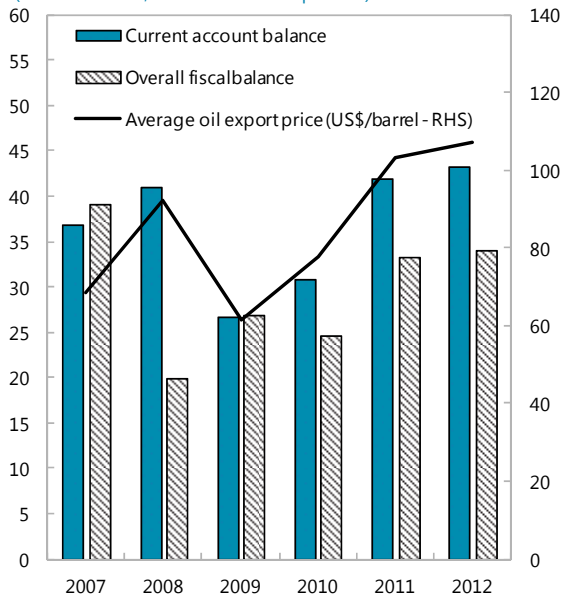
Headline and Core Inflation, 2007–12
(Y-o-y percent change)



Government Spending, 2007–12
(Percent of GDP; unless otherwise specified)



Fiscal and Current Account Balances, 2007–12
(Percent of GDP; unless otherwise specified)

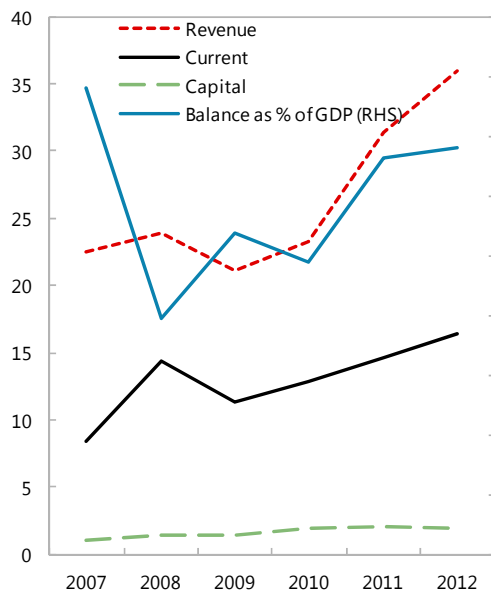


Sources: Country authorities; and IMF staff calculations.

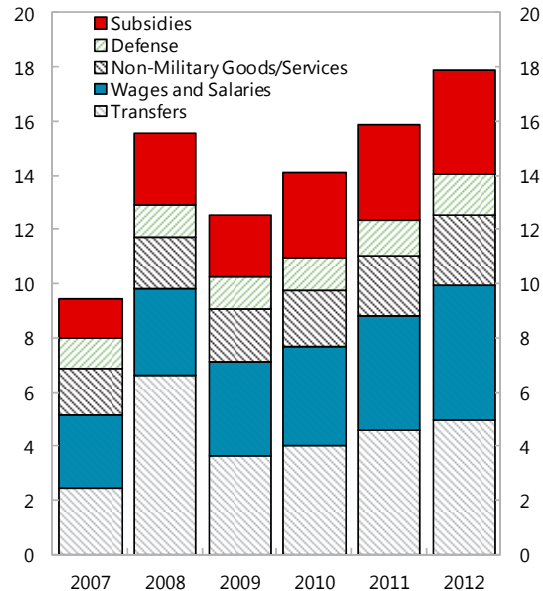
Figure 7. Fiscal Indicators

Despite an increase in current spending, fiscal surpluses are high due to high oil prices

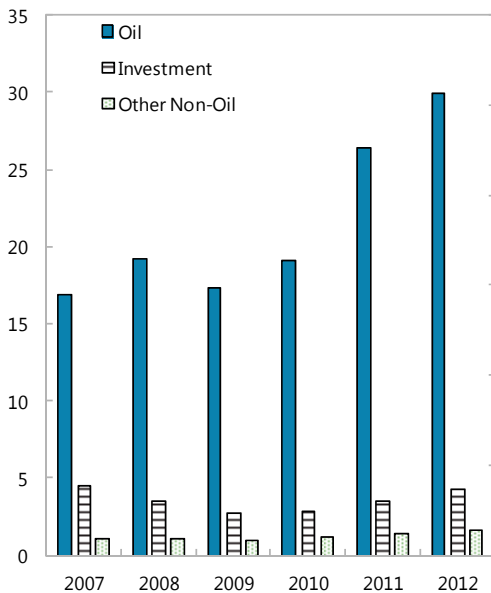
Spending, Revenue and Overall Balance, 2007–12
(KD billions)



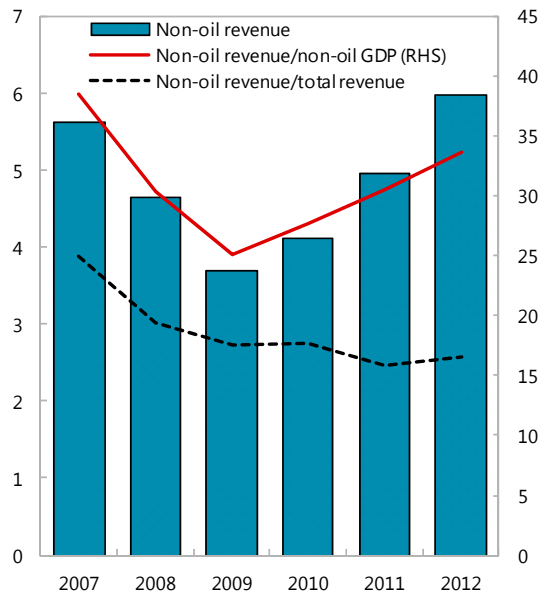
Current Spending Composition, 2007–12
(KD billions)



Kuwait Government Revenues, 2007–12
(KD billions)



Non-Oil Revenue, 2007–12
(KD billions)

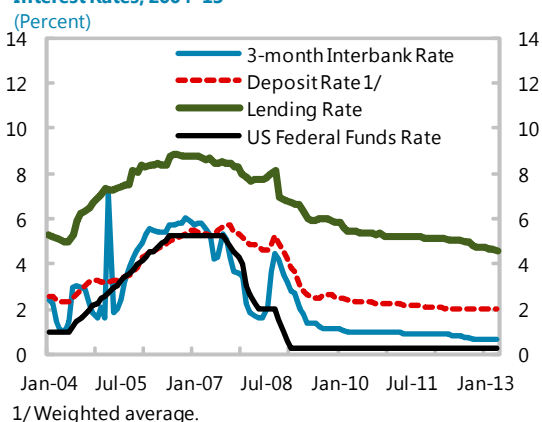


Sources: Country authorities; and IMF staff calculations.

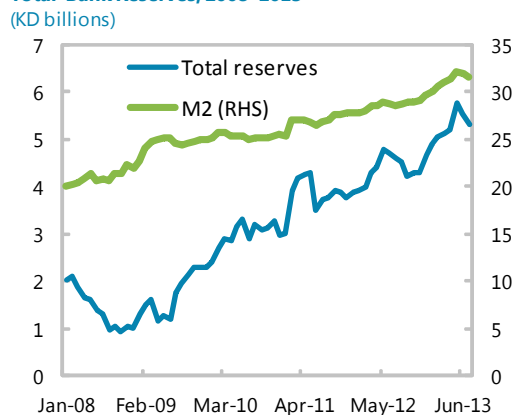
Figure 8. Monetary Developments

Deposits, liquidity and bank credit have picked up as interest rates declined

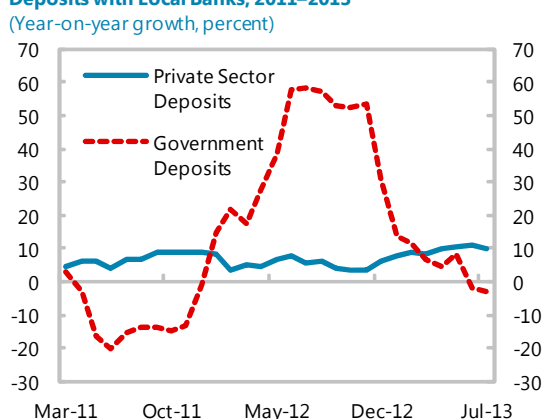
Interest Rates, 2004–13



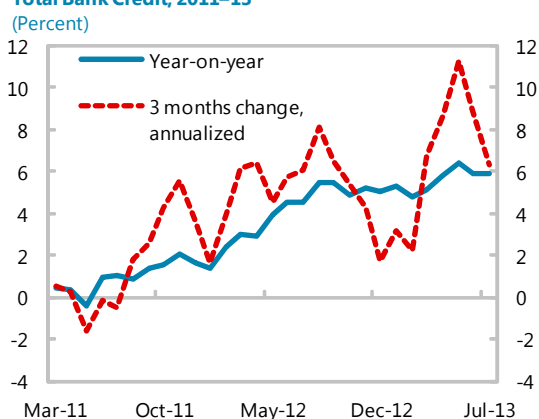
Total Bank Reserves, 2008–2013



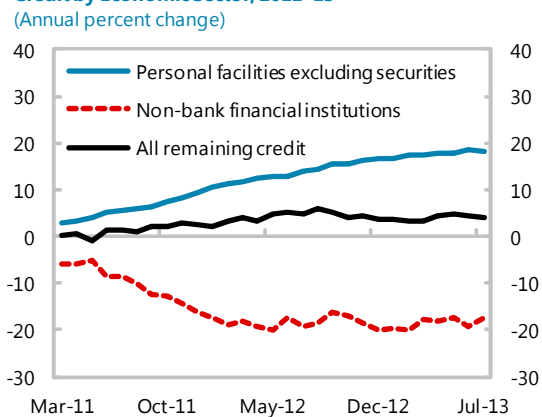
Deposits with Local Banks, 2011–2013



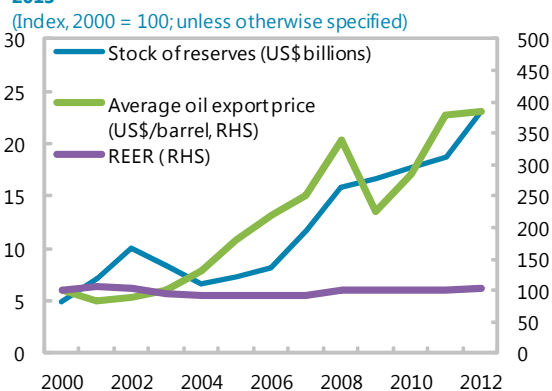
Total Bank Credit, 2011–13



Credit by Economic Sector, 2011–13



Total International Reserves, Oil Prices, and REER 2000–2013

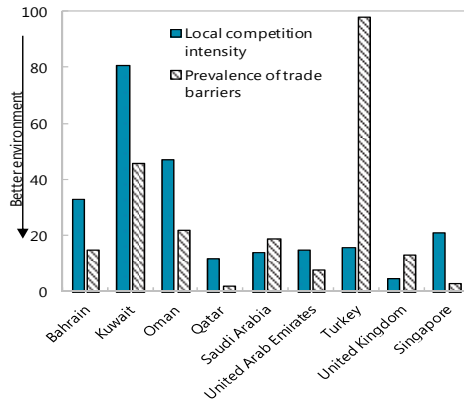


Sources: Country authorities; EDSS; Haver; and IMF staff calculations.

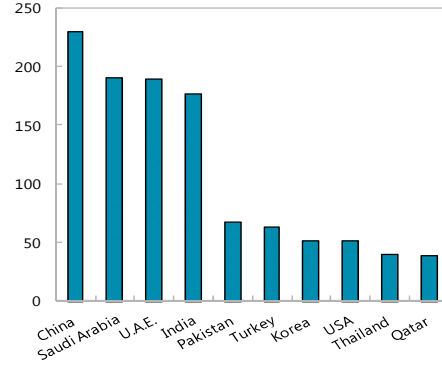
Figure 9. Output, Trade, and Exports

Export diversification is lacking and output structure is heavily mining based

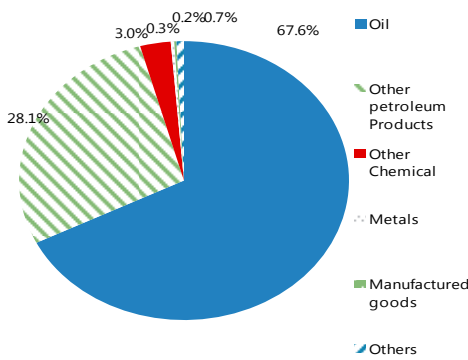
Anti-monopoly Policy Effectiveness and Trade Barriers
(Global Rank)



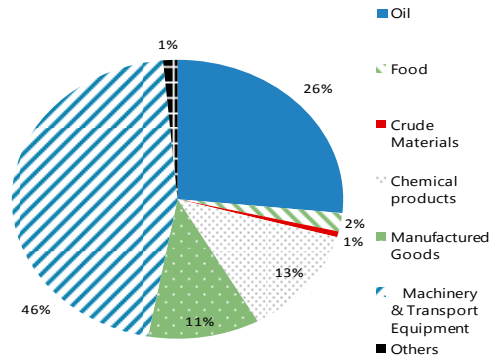
Kuwait: Non-Oil Exports by Destination (top 10), 2011
(KD millions)



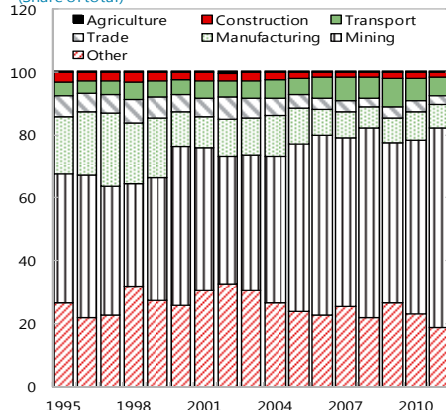
Kuwait, Top 50 Exports of Goods, 2011
(Percent of total exports of goods)



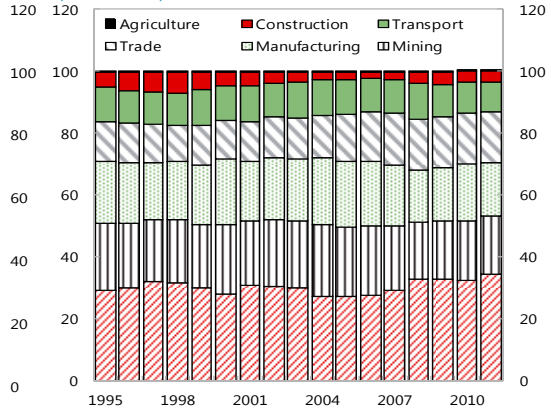
Singapore Exports by Sector, 2011
(Percent of total exports of goods)



Kuwait - GDP by Sector, 1995–2011
(Share of total)



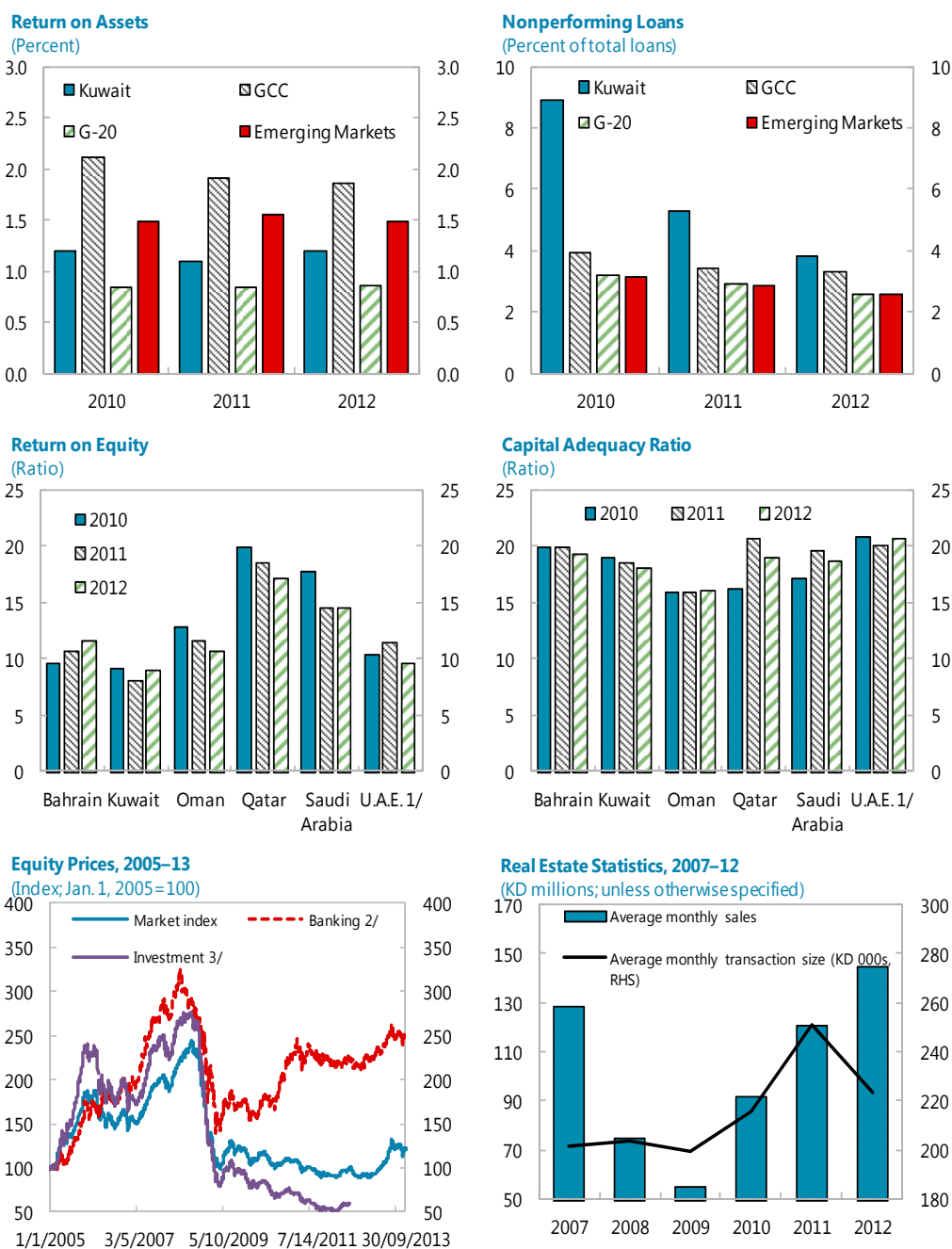
Singapore - GDP by Sector, 1995–2011
(Share of total)



Sources: World Economic Forum; Haver Analytics; United Nations Statistics Division; country authorities; and IMF staff calculations.

Figure 10. Financial Developments

Banking sector is sound while stock and real estate markets have been improving



Sources: Country authorities; Kuwait Stock Exchange; NBK reports; and IMF staff estimates.

1/ Local banks only.

2/ Previous banking index has been discontinued and the new index starts from May 12, 2012.

3/ The Investment index has been discontinued.

Table 1. Selected Economic Indicators, 2007–14

(Quota: SDR 1,381.1 million) (Population: 3.8 million; Dec. 2012) (Per capita GDP: \$48,260; 2012 estimate) (Poverty rate: n.a.) Main exports: oil and gas								
	2007	2008	2009	2010	2011	Prel. 2012	Proj. 2013	2014
Oil and gas sector								
Total oil and gas exports (billions of U.S. dollars)	59.1	82.6	48.9	61.8	96.7	113.7	108.3	104.9
Average oil export price (U.S. dollars/barrel)	68.4	92.2	61.5	77.7	103.3	107.1	107.1	104.0
Crude oil production (millions of barrels/day)	2.57	2.68	2.26	2.31	2.66	2.98	2.93	2.93
(Annual percentage change, unless otherwise indicated)								
National accounts and prices								
Nominal GDP (market prices, in billions of Kuwaiti dinar)	32.6	39.6	30.5	34.4	44.3	51.3	51.7	52.3
Nominal GDP (market prices, in billions of U.S. dollars)	114.7	147.4	106.0	119.9	160.7	184.5	186.1	188.1
Real GDP (at factor cost)	6.0	2.5	-7.1	-2.4	6.3	6.2	0.8	2.6
Real oil GDP	-4.7	6.5	-12.9	0.5	14.2	11.7	-2.0	0.0
Real non-oil GDP	14.7	-0.5	-3.5	-3.9	0.9	2.2	3.0	4.4
CPI inflation (average)	5.5	6.3	4.6	4.5	4.9	3.2	3.0	3.5
Unemployment rate (Kuwaiti nationals)	6.1	4.9	3.6	2.9	3.4 ...	...	...	...
(Percent of GDP at market prices)								
Investment and savings								
Investment	20.5	17.6	18.0	20.3	16.4	15.1	16.4	18.1
Public	3.3	3.5	4.8	5.5	4.5	3.8	5.3	6.6
Private ¹	17.1	14.1	13.2	14.8	11.9	11.3	11.1	11.5
Gross national savings	57.2	58.5	42.3	52.6	59.5	58.3	55.2	55.8
Public	55.2	46.8	50.6	50.3	55.8	54.9	53.5	51.5
Private ¹	2.1	11.7	-8.3	2.3	3.7	3.4	1.7	4.3
(Percent of GDP at market prices)								
Budgetary operations ²								
Revenue	67.9	64.3	63.8	65.9	73.2	70.4	68.9	68.6
Oil	51.6	52.8	52.7	54.1	62.0	58.3	56.4	53.8
Non-oil, of which:	16.3	11.5	11.1	11.7	11.2	12.1	12.5	14.8
Investment income	13.1	8.7	8.2	8.1	8.1	8.8	9.1	11.3
Expenditures	28.1	48.5	35.3	43.5	36.5	37.0	41.5	43.5
Expense ³	24.0	44.1	30.7	38.0	32.2	33.0	35.7	36.6
Capital	4.1	4.4	4.6	5.6	4.4	4.1	5.9	6.9
Balance	39.8	15.8	28.4	22.3	36.7	33.4	27.4	25.1
Domestic financing	-3.1	-4.6	-1.8	1.1	-0.2	-1.8	-3.2	-1.7
External financing	-36.7	-11.2	-26.7	-23.4	-36.5	-31.7	-24.2	-23.4
Non-oil balance (percent of non-oil GDP) ⁴	-50.2	-56.4	-77.5	-89.6	-86.1	-89.9	-97.0	-95.1
Total gross debt (calendar year-end) ⁵	7.0	5.3	6.7	5.9	4.5	3.4	2.4	2.4
(Percent change; unless otherwise indicated)								
Money and credit								
Net foreign assets ⁶	3.1	33.1	24.1	-0.5	21.1	21.3	17.5	8.7
Claims on nongovernment sector	35.1	16.7	6.1	1.9	2.6	3.2	7.7	8.0
Kuwaiti dinar 3-month deposit rate (year average; in percent)	5.0	3.4	1.7	1.3	1.1	1.0	...	...
Stock market unweighted index (annual percent change) ⁷	24.7	-38.0	-10.0	-0.7	-16.4	2.1	...	...
(Billions of U.S. dollars, unless otherwise indicated)								
External sector								
Exports of goods	62.6	87.0	54.4	67.1	103.0	120.1	115.1	111.9
Of which: non-oil exports	3.5	4.4	5.5	5.3	6.2	6.4	6.7	7.0
Annual percentage change	6.4	25.1	26.5	-3.4	17.0	2.7	4.9	3.9
Imports of goods	-19.1	-22.9	-18.5	-19.4	-22.1	-22.6	-24.0	-25.9
Current account	42.2	60.2	28.3	37.0	67.2	79.8	72.1	71.0
Percent of GDP	36.8	40.9	26.7	30.8	41.8	43.2	38.7	37.7
International reserve assets ⁸	15.9	16.7	17.7	18.7	23.0	25.8	27.6	29.4
In months of imports of goods and services	5.9	5.3	6.6	6.4	6.9	7.3	7.4	7.3
Memorandum items:								
Exchange rate (U.S. dollar per KD, period average)	3.52	3.72	3.48	3.49	3.63	3.60		
Nominal effective exchange rate (NEER, period average)	-2.1	2.9	-3.6	-0.3	0.5	1.6		
Real effective exchange rate (REER, period average)	-0.3	7.8	-1.0	0.9	1.6	1.6		
Sovereign rating (S&P)	AA-	AA-	AA-	AA-	AA	AA		

Sources: Data provided by the authorities; and IMF staff estimates and projections.

¹ Also includes government entities.² Kuwaiti fiscal year ending March 31, e.g. 2007 refers to fiscal year 2007/08.³ In 2006/07 KD 2 billion was transferred to partly cover the actuarial deficit of the Public Pension Fund.⁴ In 2008/09, KD 5.5 billion was transferred. KD 1.1 billion is budgeted for each year from 2010/11 to 2014/15.⁵ Excludes investment income and pension recapitalization, and after transfers for FGF (fiscal year).⁶ Excludes debt of Kuwait's SWF related to asset management operations.⁷ Excludes SDRs and IMF reserve position.⁸ Change in the KSE as of May 9 2012 for 2012.⁹ Does not include external assets held by Kuwait Investment Authority.

Table 2. Summary of Government Finance, 2007/08–2014/15

	2007/08	2008/09	2009/10	2010/11	2011/12	2012/13	Proj.	
							2013/14	2014/15
	(Billions of Kuwaiti Dinars)							
Revenue (includes grants) (A)	23.3	24.0	20.1	24.3	33.7	36.2	35.8	35.8
Taxes	0.4	0.3	0.3	0.3	0.3	0.3	0.4	0.4
Social contributions								
Grants								
Other revenue	23.0	23.7	19.8	24.0	33.4	35.9	35.4	35.5
Oil and gas	17.7	19.7	16.6	19.9	28.6	30.0	29.3	28.1
Investment income and transfer of profits of public entities ¹	4.5	3.2	2.6	3.0	3.7	4.5	4.7	5.9
Other ²	0.8	0.7	0.6	1.0	1.1	1.4	1.4	1.4
Total expenditure (B=C+D)	9.7	18.1	11.1	16.0	16.8	19.0	21.5	22.7
Expense (C)	8.2	16.5	9.7	14.0	14.8	17.0	18.5	19.1
Compensation of employees	2.8	3.4	3.5	3.7	4.4	5.1	5.6	6.2
Purchases/use of goods & services ³	1.8	1.9	1.9	2.1	2.3	2.7	3.0	3.3
Interest ⁴	0.1	0.1	0.1	0.0	0.0	0.0	0.0	0.0
Subsidies and social benefits ^{5,6}	2.4	9.7	3.1	5.7	6.6	7.1	7.4	7.6
Subsidies	1.5	2.6	1.8	2.5	2.4	3.2	3.3	3.2
Oil-related subsidies	1.4	2.6	1.8	2.5	2.4	3.2	3.3	3.2
Other subsidies	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Social benefits	1.0	7.1	1.3	3.2	4.2	3.9	4.1	4.4
Payments to social security fund	0.7	6.4	0.8	1.8	2.7	2.7	2.8	2.9
Transfers to social security fund	0.7	0.8	0.8	0.7	1.7	1.7	1.7	1.8
Fund recapitalization	0.0	5.6	0.0	1.1	1.1	1.1	1.1	1.1
Other social benefits	0.3	0.7	0.5	1.4	1.5	1.1	1.4	1.4
Oil-related	0.0	0.3	0.1	0.9	0.9	0.6	0.6	0.6
Others	0.3	0.4	0.4	0.4	0.6	0.5	0.7	0.8
Grants								
Expense not elsewhere classified	1.1	1.5	1.0	2.5	1.5	2.0	2.4	2.0
Net acquisition of nonfinancial assets (D)	1.4	1.6	1.5	2.0	2.0	2.1	3.0	3.6
Purchases of nonfinancial assets	1.4	1.6	1.5	2.0	2.0	2.1	3.0	3.6
Sales of nonfinancial assets	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Gross operating balance [=A-C]	15.1	7.5	10.4	10.3	18.9	19.2	17.3	16.7
Net lending / borrowing [=A-B]	13.7	5.9	9.0	8.2	16.9	17.2	14.2	13.1
Non-oil balance	-4.0	-13.8	-7.6	-11.7	-11.7	-12.8	-15.0	-15.0
excluding investment income	-8.5	-17.1	-10.2	-14.7	-15.4	-17.3	-19.8	-20.9
excluding recapitalization of pension	-8.5	-11.4	-10.2	-13.6	-14.3	-16.2	-18.7	-19.8
excluding oil-related subsidies and benefits	-7.1	-8.6	-8.3	-10.2	-11.0	-12.4	-14.8	-16.0
Financing	-13.7	-5.9	-9.0	-8.2	-16.9	-17.2	-14.2	-13.1

Table 2. Summary of Government Finance, 2007/08–2014/15 (concluded)

	2007/08	2008/09	2009/10	2010/11	2011/12	2012/13	Proj.	
							2013/14	2014/15
	(Percent of GDP)							
Revenue (includes grants)	67.9	64.3	63.8	65.9	73.2	70.4	68.9	68.5
Taxes	1.0	0.9	0.9	0.9	0.7	0.7	0.7	0.7
Social contributions								
Grants								
Other revenue	66.9	63.4	62.8	65.0	72.5	69.8	68.2	67.8
Oil and gas	51.6	52.8	52.7	54.1	62.0	58.3	56.4	53.8
Investment income and transfer of profits of public entities	13.1	8.7	8.2	8.1	8.1	8.8	9.1	11.2
Other	2.2	1.9	1.9	2.7	2.4	2.6	2.7	2.7
Total expenditure	28.1	48.5	35.3	43.5	36.5	37.0	41.5	43.5
Expense	24.0	44.1	30.7	38.0	32.2	33.0	35.7	36.6
Compensation of employees	8.1	9.0	11.1	10.1	9.5	10.0	10.9	11.8
Purchases/use of goods & services	5.2	5.1	6.2	5.6	5.0	5.3	5.8	6.3
Interest	0.4	0.2	0.2	0.1	0.1	0.1	0.1	0.1
Subsidies and social benefits	7.1	25.9	10.0	15.3	14.4	13.8	14.2	14.5
Subsidies	4.2	7.0	5.9	6.7	5.3	6.2	6.3	6.2
Oil-related subsidies	4.2	6.9	5.8	6.7	5.2	6.2	6.3	6.2
Other subsidies	0.1	0.1	0.1	0.0	0.0	0.0	0.0	0.0
Social benefits	2.9	18.9	4.1	8.6	9.2	7.6	8.0	8.3
Payments to Social Security Fund	1.9	17.1	2.5	5.0	5.9	5.3	5.3	5.6
Transfers to Social Security Fund	1.9	2.0	2.5	2.0	3.6	3.2	3.2	3.5
Fund recapitalization	0.0	15.1	0.0	3.0	2.4	2.1	2.1	2.1
Other social benefits	0.9	1.8	1.6	3.7	3.2	2.2	2.6	2.7
Oil-related	0.1	0.7	0.4	2.5	1.9	1.3	1.2	1.2
Others	0.8	1.1	1.2	1.1	1.3	1.0	1.4	1.5
Grants								
Expense not elsewhere classified	3.2	3.9	3.2	6.8	3.2	3.9	4.7	3.9
Net acquisition of nonfinancial assets	4.1	4.4	4.6	5.5	4.3	4.0	5.8	6.9
<i>Gross operating balance</i>	43.9	20.2	33.1	27.9	41.0	37.4	33.3	32.0
<i>Net lending / borrowing</i>	39.8	15.8	28.4	22.3	36.7	33.4	27.4	25.1
<i>Non-oil balance</i>	-11.8	-37.0	-24.3	-31.8	-25.3	-24.9	-29.0	-28.7
excluding investment income	-24.8	-45.7	-32.4	-39.9	-33.4	-33.7	-38.1	-40.0
excluding recapitalization of pension	-24.8	-30.6	-32.4	-37.0	-31.0	-31.6	-36.0	-37.9
excluding oil-related subsidies and benefits	-20.5	-23.0	-26.3	-27.8	-23.9	-24.1	-28.5	-30.5
	(Percent of nonoil GDP)							
Revenue (includes grants)	157.8	158.7	136.1	159.6	203.0	200.7	185.8	172.1
Total expenditure	65.3	119.8	75.4	105.5	101.2	105.4	111.8	109.1
<i>Gross operating balance</i>	102.0	49.8	70.6	67.6	113.8	106.7	89.6	80.3
<i>Net lending / borrowing</i>	92.5	38.9	60.7	54.2	101.7	95.2	73.9	63.0
<i>Non-oil balance</i>	-27.3	-91.4	-51.8	-77.0	-70.3	-70.9	-78.1	-72.1
excluding investment income	-57.7	-112.8	-69.3	-96.7	-92.6	-96.0	-102.7	-100.3
excluding recapitalization of pension	-57.7	-75.5	-69.3	-89.6	-86.1	-89.9	-97.0	-95.1
excluding oil-related subsidies and benefits	-47.7	-56.8	-56.1	-67.3	-66.2	-68.7	-76.9	-76.6
Memorandum items:								
Expenses excl. recapitalization of pension fund (percent of nonoil GDP)	55.7	71.7	65.6	84.9	82.6	88.0	90.4	86.5
Oil-related subsidies and benefits (percent of nonoil GDP)	10.0	18.7	13.2	22.3	19.8	21.2	20.2	18.5
Kuwait Crude oil price, USD per barrel	74.4	84.5	65.5	84.1	104.3	107.1	106.3	102.6

Sources: Ministry of Finance; Central Bank of Kuwait; and IMF staff estimates and projections.

¹ Excluded from the national budget presentation. Estimated by Fund staff.

² Includes UN (Iraq) compensations

³ Includes other miscellaneous expenditures in FY 07/08 and 08/09.

⁴ Covers interest payments on the treasury bills and bonds, and on the DCP bonds. Only the latter is included in the national budget presentation.

⁵ In 2006/07 KD 2 billion was transferred to partly cover the actuarial deficit of the social security fund.

In 2008/09, KD 5.5 billion was transferred. KD 1.1 billion is budgeted for each year from 2010/11 to 2014/15.

⁶ The 2006/07 budget reflects KD 195 million on account of a KD 200 one-off grant transfer to each Kuwaiti citizen. The 2010/11 budget reflects KD 1,120 million on account of a KD 1,000 one-off grant transfer to each Kuwaiti citizen.

Table 3. Summary Balance of Payments, 2007–14

	2007	2008	2009	2010	2011	Prel. 2012	Proj. 2013	2014
(Billions of U.S. dollars, unless otherwise indicated)								
Current account	42.2	60.2	28.3	37.0	67.2	79.8	72.1	71.0
Goods (trade balance)	43.4	64.0	35.9	47.8	80.9	97.5	91.0	86.0
Exports	62.6	87.0	54.4	67.1	103.0	120.1	115.1	111.9
Oil exports	59.1	82.6	48.9	61.8	96.7	113.7	108.3	104.9
Non-oil exports including re-exports ¹	3.5	4.4	5.5	5.3	6.2	6.4	6.7	7.0
Of which: re-exports	1.2	1.7	1.6	1.8	2.1	2.1	2.2	2.2
Imports	-19.1	-22.9	-18.5	-19.4	-22.1	-22.6	-24.0	-25.9
Services	-3.2	-3.8	-2.3	-6.7	-8.0	-9.6	-10.2	-11.0
Transportation	-0.1	-0.6	-1.4	0.2	0.2	0.2	0.2	0.2
Insurance	-0.1	-0.1	0.0	0.0	0.0	0.0	0.0	0.0
Travel	-6.4	-7.3	-5.8	-6.1	-8.0	-8.6	-9.2	-9.9
Other services	3.4	4.3	4.9	-0.8	-0.2	-1.2	-1.3	-1.3
Investment income	12.4	10.7	7.7	8.5	9.0	9.3	10.7	15.8
Receipts	16.3	14.0	8.9	9.7	10.4	10.7	11.4	16.6
General government ²	8.5	8.8	6.3	6.1	6.6	6.7	10.3	14.7
Other sectors ³	7.8	5.1	2.6	3.6	3.9	4.0	1.1	1.9
Payments	-3.9	-3.2	-1.2	-1.3	-1.4	-1.4	-0.7	-0.8
General government	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other	-3.9	-3.2	-1.2	-1.3	-1.4	-1.4	-0.7	-0.7
Current transfers ⁴	-10.5	-10.7	-13.0	-12.5	-14.7	-17.3	-19.4	-19.9
Capital and financial account	-33.4	-49.6	-25.6	-43.8	-61.1	-82.5	-70.2	-69.2
Capital account ⁵	1.5	1.7	1.0	2.1	3.5	4.2	3.4	4.5
Financial account	-34.9	-51.3	-26.6	-45.9	-64.6	-86.7	-73.6	-73.7
Direct investment	-9.7	-9.1	-7.5	-1.1	-8.0	-5.8	-5.2	-5.1
Abroad ⁶	-9.8	-9.1	-8.6	-1.5	-8.9	-7.6	-6.4	-6.4
In Kuwait	0.1	0.0	1.1	0.5	0.9	1.9	1.2	1.2
Portfolio investment	-34.9	-28.1	-8.2	-21.6	-7.5	-25.8	-16.0	-20.1
Other investment (net)	9.7	-14.1	-10.9	-23.2	-49.0	-55.2	-52.5	-48.5
Net errors and omissions ⁷	-5.5	-10.0	-1.0	7.4	-1.6	6.0	0.0	0.0
Overall balance	3.3	0.7	1.7	0.6	4.5	3.3	1.8	1.8
Memorandum items								
Current account/GDP (in percent)	36.8	40.9	26.7	30.8	41.8	43.2	38.7	37.7
Current account (excl. oil)/GDP (in percent)	-14.7	-15.2	-19.5	-20.7	-18.4	-18.4	-19.5	-18.0
Investment income/GDP (in percent)	10.8	7.3	7.3	7.1	5.6	5.0	5.8	8.4
WEO oil price (dollars per barrel)	71.1	97.0	61.8	79.0	104.0	105.0	104.5	101.3
Import growth (in percent)	17.7	20.0	-19.2	4.5	14.1	2.4	6.2	7.7
International reserve assets (billions of U.S. dollars) ⁸	15.9	16.7	17.7	18.7	23.0	25.8	27.6	29.4
In months of imports of goods and services	5.9	5.3	6.6	6.4	6.9	7.3	7.4	7.3

Sources: Central Bank of Kuwait; and IMF staff estimates.

¹ Also includes unrecorded oil exports.

² Kuwait Investment Authority, Kuwait Petroleum Corporation, Kuwait Fund for Arab Economic Development, Public Institute for Social Security, Kuwait Airways Corporation, and Bank of Savings and Credit.

³ CBK, local banks, investment companies, exchange companies, insurance companies, and the nonfinancial private sector.

⁴ From 2007, based on a new, more comprehensive methodology to estimate outward workers' remittances.

⁵ Includes UN war compensation.

⁶ For 2010, includes a projection of the net inflow from the sale for \$10.6 billion of a foreign asset owned by a Kuwaiti company.

⁷ Includes other unclassified private-sector flows.

⁸ Includes SDRs and IMF reserve position.

Table 4. Monetary Survey, 2007–14

End of period	2007	2008	2009	2010	2011	2012	Proj.	
							2013	2014
(Millions of KD)								
Foreign assets (net) ¹	5,718	7,610	9,441	9,395	11,379	13,805	16,221	17,631
Central bank	4,327	4,510	5,009	5,183	6,397	7,317	8,496	8,999
Local banks	1,392	3,100	4,432	4,212	4,982	6,487	7,725	8,632
Domestic assets (net)	13,269	14,341	15,455	15,784	16,367	15,736	16,819	18,044
Claims on government (net)	-968	-2,675	-3,227	-2,830	-2,906	-3,814	-4,460	-4,729
Central bank (net)	-920	-1,124	-1,165	-533	-682	-543	-838	-757
Claims	0	0	0	0	0	0	0	0
Deposits	920	1,124	1,165	533	682	543	838	757
Local banks (net)	-47	-1,550	-2,063	-2,297	-2,223	-3,271	-3,622	-3,972
Claims	1,912	1,985	1,922	1,910	1,887	1,684	1,183	1,183
Government debt bonds	0	0	0	0	0	0	0	0
Public debt instruments	1,912	1,985	1,922	1,910	1,887	1,684	1,183	1,183
Other claims	0	0	0	0	0	0	0	0
Deposits	1,959	3,535	3,984	4,208	4,011	4,955	4,805	5,155
Claims on nongovernment sector	21,822	25,460	27,019	27,527	28,230	29,119	31,372	33,874
Credit facilities	20,139	23,660	25,108	25,201	25,612	26,895	29,077	31,396
Local investments	1,683	1,800	1,911	2,326	2,618	2,224	2,295	2,478
Other items (net)	-7,585	-8,336	-8,336	-8,918	-9,115	-8,995	-9,769	-10,855
Broad money ²	18,987	21,950	24,896	25,179	27,747	29,541	33,040	35,675
Money	4,147	4,370	4,714	5,152	6,365	7,526	8,992	9,709
Quasi money	14,841	17,580	20,182	20,027	21,381	22,015	24,048	25,966
Of which: Foreign currency deposits	1,710	1,899	2,753	2,081	2,078	2,272	3,000	3,239
(Annual percentage change)								
Foreign assets (net)	3.1	33.1	24.1	-0.5	21.1	21.3	17.5	8.7
Central Bank	26.6	4.2	11.1	3.5	23.4	14.4	16.1	5.9
Local banks	-34.6	122.8	43.0	-5.0	18.3	30.2	19.1	11.7
Domestic assets (net)	27.9	8.1	7.8	2.1	3.7	-3.9	6.9	7.3
Claims on government (net)	-953.4	176.4	-20.7	12.3	-2.7	-31.3	-16.9	-6.0
Claims on nongovernment sector	35.1	16.7	6.1	1.9	2.6	3.2	7.7	8.0
Other items (net)	-28.9	-11.3	1.3	-6.9	-0.5	-6.8	-5.5	-10.0
Broad money	19.3	15.6	13.4	1.1	10.2	6.5	11.8	8.0
Money	16.8	5.4	7.9	9.3	23.6	18.2	19.5	8.0
Quasi money	20.0	18.5	14.8	-0.8	6.8	3.0	9.2	8.0
Of which: Foreign currency deposits	-23.8	11.1	45.0	-24.4	-0.1	9.3	32.0	8.0
(Change in percent of beginning of period broad money stock)								
Foreign assets (net)	1.1	10.0	8.3	-0.2	7.9	8.7	8.2	4.3
Central bank	5.7	1.0	2.3	0.7	4.8	3.3	4.0	1.5
Local banks	-4.6	9.0	6.1	-0.9	3.1	5.4	4.2	2.7
Domestic assets (net)	18.2	5.6	5.1	1.3	2.3	-2.3	3.7	3.7
Claims on government (net)	-6.8	-9.0	-2.5	1.6	-0.3	-3.3	-2.2	-0.8
Claims on nongovernment sector	35.6	19.2	7.1	2.0	2.8	3.2	7.6	7.6
Other items (net)	-10.7	-4.5	0.5	-2.3	-0.2	-2.2	-1.8	-3.1
Broad money	19.3	15.6	13.4	1.1	10.2	6.5	11.8	8.0
Money	3.7	1.2	1.6	1.8	4.8	4.2	5.0	2.2
Quasi money	15.5	14.4	11.9	-0.6	5.4	2.3	6.9	5.8
Of which: Foreign currency deposits	-3.4	1.0	3.9	-2.7	0.0	0.7	2.5	0.7
Memorandum items:								
Non-oil GDP/M2	77.0	69.6	59.0	59.1	58.5	60.1	57.1	57.1
Foreign currency deposits/M2	9.0	8.7	11.1	8.3	7.5	7.7	9.1	9.1
Private credit/non-oil GDP	135.5	151.2	166.6	167.6	158.9	149.2	151.3	163.4

Sources: Central Bank of Kuwait; and IMF staff estimates.

¹ Excludes SDRs and IMF reserve position.² Excludes deposits with financial institutions which are marginal.

Table 5. Illustrative Macroeconomic Baseline Scenario, 2007–18

	2007	2008	2009	2010	2011	Prel. 2012	2013	2014	Projections		2017	2018
									2015	2016		
(Percentage change, unless otherwise specified)												
Production and prices												
Nominal GDP (KD billions)	32.6	39.6	30.5	34.4	44.3	51.3	51.7	52.3	52.3	53.2	55.2	57.7
Nominal GDP	10.6	21.6	-23.0	12.7	29.0	15.7	0.8	1.1	0.1	1.6	3.8	4.5
Nominal non-oil GDP	20.3	4.4	-3.8	1.2	9.1	9.5	6.2	8.0	9.0	9.1	9.2	9.2
Real GDP	6.0	2.5	-7.1	-2.4	6.3	6.2	0.8	2.6	3.0	3.0	3.9	3.9
Real oil GDP	-4.7	6.5	-12.9	0.5	14.2	11.7	-2.0	0.0	0.2	0.2	2.2	2.2
Real non-oil GDP	14.7	-0.5	-3.5	-3.9	0.9	2.2	3.0	4.4	4.9	4.9	4.9	4.9
Kuwait crude export price (U.S. dollars per barrel)	68.4	92.2	61.5	77.7	103.3	107.1	107.1	104.0	98.1	94.1	91.4	89.6
Crude oil output (millions of barrels per day)	2.57	2.68	2.26	2.31	2.66	2.98	2.93	2.93	2.94	2.94	3.01	3.07
Consumer price index	5.5	6.3	4.6	4.5	4.9	3.2	3.0	3.5	4.0	4.0	4.0	4.1
(Percent of GDP, unless otherwise specified)												
Public finance ¹												
Revenue, of which:	67.9	64.3	63.8	65.9	73.2	70.4	68.9	68.6	66.8	66.3	66.1	64.6
Oil and gas	51.6	52.8	52.7	54.1	62.0	58.3	56.4	53.8	50.5	47.8	45.6	43.9
Investment income ²	13.1	8.7	8.2	8.1	8.1	8.8	9.1	11.3	12.7	14.9	16.9	17.2
Expenditure	28.1	48.5	35.3	43.5	36.5	37.0	41.5	43.5	45.1	47.1	48.5	49.6
Expense ³	24.0	44.1	30.7	38.0	32.2	33.0	35.7	36.6	36.8	38.3	39.2	40.0
Capital	4.1	4.4	4.6	5.6	4.4	4.1	5.9	6.9	8.3	8.8	9.3	9.6
Fiscal balance (deficit -)	39.8	15.8	28.4	22.3	36.7	33.4	27.4	25.1	21.7	19.2	17.6	14.9
Exchange rates												
Exchange rates (U.S. dollar per KD, period average)	3.52	3.72	3.48	3.49	3.63	...	...	...	...	...	...	...
Nominal effective exchange rate	-2.1	2.9	-3.6	-0.3	0.5	...	...	...	...	...	...	...
Real effective exchange rate	-0.3	7.8	-1.0	0.9	1.6	...	...	...	...	...	...	...
(Percent of GDP, unless otherwise specified)												
Balance of payments												
Exports of goods and services excl. re-exports	59.7	62.7	56.8	58.3	65.7	66.5	63.5	61.6	58.8	56.2	54.3	52.6
Of which: oil and refined products	51.5	56.0	46.1	51.5	60.2	61.6	58.2	55.8	52.5	49.5	47.3	45.3
Imports of goods and services excl. re-exports	-24.6	-21.9	-25.1	-24.1	-20.3	-18.9	-20.1	-21.7	-23.5	-24.9	-26.0	-26.9
Investment income (net) ⁴	10.8	7.3	7.3	7.1	5.6	5.0	5.8	8.4	10.4	13.3	15.9	16.3
Current account	36.8	40.9	26.7	30.8	41.8	43.2	38.7	37.7	34.2	32.3	31.1	28.4
Current account (excluding oil exports)	-14.7	-15.2	-19.5	-20.7	-18.4	-18.4	-19.5	-18.0	-18.2	-17.2	-16.1	-16.9
(Percent of GDP, unless otherwise specified)												
Saving-investment balance												
Final consumption	44.4	41.5	52.0	44.8	38.2	37.3	40.1	42.0	44.5	47.6	49.5	51.0
Government	14.0	13.4	18.5	17.3	15.0	15.2	16.0	17.3	18.9	20.1	20.9	21.5
Private	30.4	28.1	33.5	27.5	23.3	22.1	24.2	24.7	25.6	27.4	28.7	29.5
Gross domestic investment	20.5	17.6	18.0	20.3	16.4	15.1	16.4	18.1	20.1	21.1	22.2	23.4
Government	4.3	3.7	5.7	5.9	4.5	4.9	6.4	7.6	8.7	9.3	9.8	10.1
Private	16.2	14.0	12.3	14.4	11.9	10.3	10.0	10.5	11.5	11.8	12.4	13.3
Savings	57.2	58.5	42.3	52.6	59.5	58.3	55.2	55.8	54.4	53.4	53.3	51.8
Government saving	55.2	46.8	50.6	50.3	55.8	54.9	53.5	51.5	48.4	46.3	45.3	43.3
Private savings	2.1	11.7	-8.3	2.3	3.7	3.4	1.7	4.3	6.0	7.2	8.0	8.5

Sources: Kuwait authorities; IMF World Economic Outlook; and IMF staff estimates and projections.

¹ Fiscal year ending March 31.² Includes profits of public enterprises.³ In 2006/07 KD 2 billion was transferred to partly cover the actuarial deficit of the Public Pension Fund. In 2008/09, KD 5.5 were transferred. KD 1.1 billions are budgeted for each year from 2010/11 to 2014/15.⁴ Assuming return on foreign assets close to the LIBOR.

Table 6. Financial Soundness Indicators of the Banking Sector, 2006–13(Percent unless specified otherwise) ¹

	2006	2007	2008	2009	2010	2011	2012	Jun-13
Capital adequacy								
Regulatory capital to risk-weighted assets	20.2	19.3	15.6	16.7	18.9	18.5	18.0	18.3
Regulatory Tier I capital to risk-weighted assets	17.7	17.2	14.3	14.9	17.3	16.9	16.0	16.6
Capital to assets	12.6	12.3	10.9	11.4	12.6	12.4	12.6	12.5
Loan composition and quality								
Oil/gas	0.7	0.8	0.9	1.2	1.2	1.1	1.6	1.6
Trade	11.8	10.4	10.2	10.6	10.0	10.5	12.1	12.2
Industry	5.0	5.9	6.8	6.5	7.0	7.1	7.9	7.9
Construction	13.4	12.6	11.9	11.4	12.7	12.1	12.6	12.4
Real estate	17.5	19.2	18.1	20.6	20.0	19.6	19.2	18.5
Equity purchase loans (corporate)	5.4	4.5	5.8	5.9	5.7	5.8	3.5	3.4
Agriculture/fishing	0.2	0.1	0.7	0.3	0.4	0.2	0.3	0.2
Financial Institutions	14.6	15.9	12.8	12.7	14.1	13.1	11.2	11.0
<i>Of which</i> : investment companies	5.3	7.9	7.5	8.0	8.7	6.1	4.3	4.8
<i>Of which</i> : banks	0.0	0.0	0.0	0.0	4.6	3.7	6.7	6.2
Public services	1.6	2.2	1.9	1.6	1.6	1.7	2.6	1.7
Households	20.3	19.1	16.0	16.1	16.3	17.0	19.4	20.0
<i>Of which</i> : credit card advances	1.0	0.8	0.6	0.5	0.5	0.5		
<i>Of which</i> : installment loans	13.7	12.1	10.9	12.7	12.1	12.9	13.2	13.9
<i>Of which</i> : consumer loans	3.7	4.1	2.5	1.0	2.2	2.2	2.9	3.0
<i>Of which</i> : equity purchase loans (individuals)	1.8	2.1	2.0	1.9	1.4	1.4	2.9	2.8
Other	9.6	9.2	14.8	13.3	11.1	11.8	9.5	11.1
Gross non-performing loans to total loans	4.6	3.8	6.8	11.5	8.9	7.3	5.2	4.6
NPLs net of specific provisions to total loans net of specific	2.5	2.1	4.9	7.4	6.1	5.3	3.8	3.3
Specific provisions to gross NPLs	47.4	47.2	29.0	38.3	33.9	29.5	95.1	107.2
NPLs net of specific provisions to Tier I capital	12.6	10.8	31.5	46.2	33.8	28.7	22.4	18.9
Loans to shareholders, parent companies, & directors to total loans	4.9	4.2	4.9	6.4	2.0	2.3	2.6	4.5
Large exposures to Tier I capital	147.6	141.6	212.4	165.1	124.3	105.3	100.4	101.0
Specific provisions to gross loans	2.2	1.8	2.0	4.4	3.0	2.1	1.4	1.3
Profitability								
Return on Average Assets (ROAA) ²	2.7	3.3	0.8	0.7	1.2	1.1	1.2	1.2
Return on Average Equity (ROAE) ²	20.1	24.3	6.5	6.1	9.1	8.1	9.0	8.9
Net interest income to gross income	33.9	29.0	36.6	44.5	49.9	47.6	48.1	48.3
Non-interest income to gross income	29.0	29.0	21.6	25.3	24.6	33.1	33.4	33.9
Trading and foreign exchange income to gross income	13.7	15.1	6.7	6.0	4.1	10.0	14.9	15.3
Non-interest expenses to gross income	27.6	23.9	26.4	36.9	37.7	36.1	34.0	31.4
Non-interest expenses to average assets ²	1.4	1.5	1.6	1.9	1.6	2.1	1.9	1.9
Personnel expenses to non-interest expenses	50.7	49.6	48.0	42.9	48.7	36.8	39.0	41.7
Liquidity								
Core liquid assets to total assets ³	29.3	26.9	20.8	20.4	17.7	22.1	21.0	22.7
Core liquid assets to short-term liabilities	38.6	34.1	28.0	28.6	27.8	36.3	34.8	37.2
Liquid assets to total assets	34.5	32.9	28.4	27.9	22.8	26.5	27.3	26.7
Liquid assets to short term liabilities	45.3	41.7	38.4	39.2	35.7	43.7	45.2	43.8
FX- loans to total loans	19.7	23.3	24.9	25.8	25.5	25.8	28.1	28.0
FX- deposits to total deposits	28.8	34.9	35.1	32.7	30.7	33.8	34.6	35.5
FX- liabilities to total liabilities	23.2	27.8	24.2	22.6	11.2	11.4	14.5	14.3
Deposits to assets	59.3	56.4	59.2	58.8	56.7	58.3	63.3	62.6
Loans to deposits	96.1	103.1	109.0	113.0	116.5	110.9	100.5	98.8
FX- loans to FX-deposits	65.5	68.9	77.3	89.1	96.8	84.6	81.5	77.8
Sensitivity to market risk								
Net open FX position (overall) as percent of Tier I capital	0.0	0.0	11.2	10.7	8.7			
Off-balance sheet operations as percent of assets	32.1	34.7	32.5	25.3	26.2	25.4	26.3	26.7
Gross asset position in derivatives as a percentage of tier I capital	77.9	90.9	71.1	46.9	33.6			
Gross liability position in derivatives as a percentage of tier I capital	77.9	91.0	71.1	46.8	39.4			
Equity exposure to capital	40.6	42.4	47.1	45.4	39.1	43.7	37.5	36.9

Source: Central Bank of Kuwait

¹ Data are on consolidated basis.² Averaging was not applied in 2006 indicators.³ Core liquid assets include: cash and cash equivalents, deposits with CBK, government securities, CBK bills, deposits with banks, certificates of deposit with other banks which mature within three months. The data were extracted from CBK prudential report.

Annex I. Status of Staff Recommendations Made in the 2012 Article IV Consultation

Containing fiscal spending, in particular public wage bill and unfunded pension liabilities, and reallocating spending toward capital	Public employment increased further in 2012. The 2013/14 budget has envisaged a large increase in capital spending.
Revisiting energy subsidies	The government did not initiate any concrete plans to review subsidies.
Building institutional capacity to improve tax system and introduce VAT and strengthen budget framework	In line with the recommendations of the Fund and the World Bank TA in the past year, some progress has been achieved in modernizing the tax administration system. A macro-fiscal unit has been established with the support of Fund resident advisor.
Improving governance and auditing/reporting standards	New corporate governance guidelines have been issued for banks and investment companies.
Modernizing legislation to improve business climate and efficiency of government procedures	Company law, Direct Investment Promotion law, and Commercial License law were passed.
Enhancing ICs' resolution, developing needed tools to do it, and coordinating between CBK and CMA on ICs' supervision	Restructuring of some ICs is protracted. Coordination exists between CBK and CMA, but there is no formal structure. CMA has introduced corporate governance guidelines for ICs; capitalization ratios are under consideration.
Modernizing restructuring resolution	Bankruptcy law is under preparation.
Improving AML/CFT framework	A new Anti-Money Laundering Law has been passed.

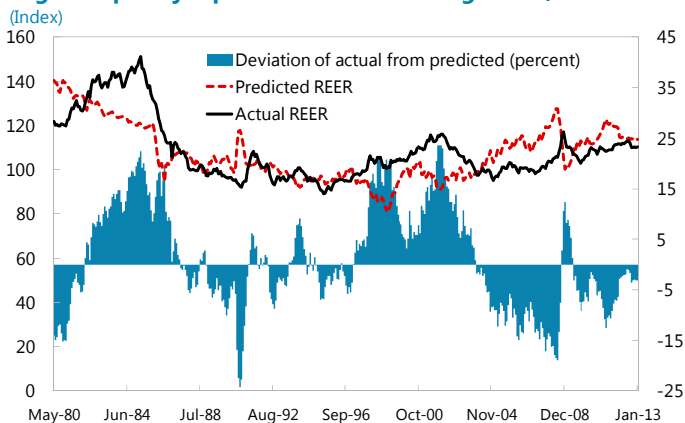
Appendix I. Exchange Rate Assessment

The real exchange rate is currently estimated to be in line with fundamentals. Medium-term estimates produce mixed results but overall suggest no misalignment of the currency.

1. The equilibrium real effective exchange rate (EREER) approach suggests that the real exchange rate is currently in line with its estimated long-run equilibrium.

Computations of the equilibrium real effective exchange rate are based on the estimation of a long-run relationship between the real effective exchange rate (REER) and real oil prices. Under/over valuation is calculated as the deviation of the actual value of the REER from the fitted value using the estimated cointegration relationship based on monthly historical data for 1980–2013. The REER has been declining and rising in the past few decades and is currently at the level seen in the early 2000s. The long-run equilibrium path (predicted REER) was declining until the late 1990s and has been increasing slowly since. In early 2013, the real exchange rate is close to its estimated equilibrium value.

High Frequency Equilibrium Real Exchange Rate, 1980–2013

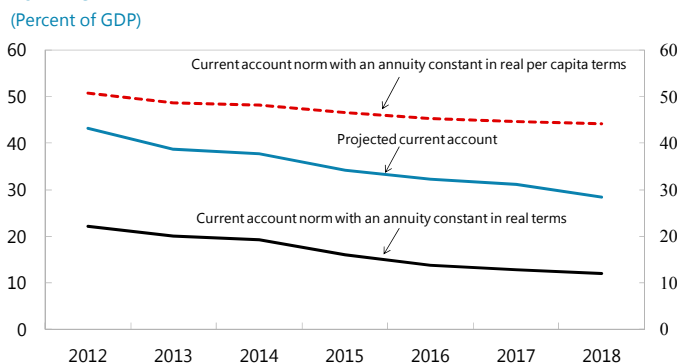


Sources: Country authorities; and IMF staff calculations.

2. The external sustainability (ES) and macroeconomic balance (MB) approaches show mixed results but suggest that overall the real exchange rate is not misaligned in the medium term.

The macroeconomic balance approach indicates that the medium-term current account norm, based on medium-term fundamentals (and an estimated historical relationship between the current account and fundamentals), is about 26 percent of GDP (see Beidas-Strom and Cashin, IMF WP/11/195, Table 2.A, specification IV), close to the surplus of 28 percent of GDP in 2018. Two other specifications result in similar current account norms (23–24 percent), and one specification shows much lower estimate (14 percent). The external sustainability approach shows a wide range of current account benchmarks, at about 12 percent of GDP and 44 percent of GDP, implying both overvaluation and undervaluation. The benchmark based on real per capita annuity implies an overvaluation of about 25 percent, while that based on

External Sustainability's Current Account Norms vs. Projections, 2012–18



Sources: Country authorities; and IMF staff estimates and projections.

real annuity indicates that REER is undervalued by about 26 percent. The more stringent rule (real per capita) would suggest less spending in the medium term (in line with the PIH fiscal sustainability benchmark), but on average, the ES approach indicates no misalignment. The MB estimate based on the most comprehensive specification is very close to the projected current account and implies no misalignment, either. Examining various external indicators, international reserves have been in the range of about 6.5–7 months of imports for the past few years while the international investment position has decreased to about 51 percent of GDP in 2012, below its 2005–2011 average of about 70 percent. Overall, the above estimates suggest that the real exchange rate is not misaligned.

Appendix II. Status of Implementation of FSAP 2010 Recommendations

No	Recommendation	Status	Update
1	Clarify regulatory and supervisory responsibilities for financial institutions between the CBK, CMA and MOCI and initiate coordination for transition process to new oversight architecture.	Completed	A Memorandum of Understanding (MOU) was signed with CMA. Amendments to be made to the MOU in respect of the joint issues between Ministry of Commerce and Industry and CBK, are under consideration.
2	Perform periodic stress tests of real estate and other major sectoral credit risk concentrations and review existing assessment of the way banks consider these risk concentrations in their Internal Capital Adequacy Assessment Process (ICAAP).		The Financial Stability Office performs regular stress tests on all Kuwaiti banks. The Supervision Sector reviews and suggests revisions for stress tests and ICAAPs prepared by banks.
3	Extend viability assessment to all systemically important ICs.	Completed	Since the supervisory responsibility on the investment companies was shifted to the CMA, it is suggested to address the CMA, in this respect in order to take the necessary action from its side.
4	Complete integration of ICAAP in an on-site manual and start on-site examination on ICAAP in one bank as a pilot project.	Completed	The On-site Supervision Department prepared a manual for the work procedures to include the ICAAP. A professional team was formed to undertake an inspection program with the specific purpose to focus on the local banks for examining the ICAAP.
5	Finalized qualitative and quantitative staffing enhancement program for the banking supervision department.	Completed	The qualitative and quantitative capabilities of all staff working in the supervision department shall be developed on regular basis.
6	Enhance framework for macroprudential surveillance by establishing the FSU and initiate integrated supervision of systematically important sectors.	Completed	Financial Stability Office was established and supervision has been integrated. The first Financial Stability Report has been published.
7	Strengthen corporate governance rules by applying "fit and proper" test on board and management of new conventional banks.	Completed	Article (68) of Law NO. (32) of 1968 refers to the conditions to be met by a person who becomes a board member of a bank or executive authority, in addition to the resolution passed by the CBK Board of directors in this respect.
8	Issue directive on conflict of interest requiring board members and senior management and staff to abstain from participating in decisions on credit	Completed	CBK in June 2013 issued the revised principles of Corporate Governance.

	granting in their favor and reduce the individual and aggregate limit for credit to related parties.		
9	Continue the migration process from compliance-based supervision to risk-based supervision.	Completed	Risk-based supervision system has been implemented in the supervision Sector. Where, on-site inspections, in accordance with this method, have started. And the study of banks' data, using the Off-site Surveillance System (OSS), has started as well.
10	Introduce quantitative and qualitative regulation to better monitor ICs' financial soundness and improve corporate governance. Develop new licensing regime for ICs.	In progress	A comprehensive study was prepared about the evaluation and classification of ICs according to the level of risk on the basis of six qualitative factors (Stage One). Since ICs are no longer subject to the supervision of CBK, the application of (Stage Two); preparing corporate governance instructions, will be limited to finance companies.
11	Establish funding and operational arrangements for deposit insurance and cap coverage.	Not implemented	This recommendation has not been implemented because it is not suitable for the present circumstances.
12	Establish an MOU on financial crisis management between key agencies such as the CBK, MOF, CMA, and KIA.	In progress	A Memorandum of Understanding (MOU) for financial crisis management was prepared by CBK with all related authorities (MOF, CMA, and KIA) and a work team from CBK was formed that includes the Financial Stability Office, Supervision Department, Research Department, Foreign Operations Department and the Legal Office.
13	Consider widening collateral acceptance for ELA operations.	Completed	Collateral acceptance was widened for Emergency Lending Assistance operations for banks, under the CBK Board Resolution No. (91/377/2011) in its session held on 18/12/2011. The list of guarantees, issued under CBK Board Resolution dated 17/02/1979, was annulled.
14	Establish a special resolution regime that sets out a set of distinct bankruptcy.	In progress	Ministry of Commerce and Industry (MOCI) assigned the World Bank to revamp the insolvency and creditor/debtor laws in Kuwait. As a part of this project, the World Bank team has drafted the law and which has been distributed to stake holders for comments.



KUWAIT

STAFF REPORT FOR THE 2013 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

November 4, 2013

Prepared By

Middle East and Central Asia Department

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FUND RELATIONS

(As of October 3, 2013)

Membership Status: Joined September 13, 1962
Article VIII on April 5, 1963

General Resources Account:	SDR Million	% Quota
Quota 1,381.10	100.00	
Fund holdings of currency	967.41	70.05
Reserve position in Fund	413.95	29.97

SDR Department:	SDR Million	% Allocation
Net cumulative allocation	1,315.57	100.00
Holdings	1,445.56	109.78

Outstanding Purchases and Loans: None

Financial Arrangements: None

Lending to the Fund and Grants: SDR million 26.3 (New Arrangements to Borrow)

Kuwait has made a contribution to the PRGF-HIPC Trust in support of Fund's concessional assistance to low-income countries. These include an interest-free deposit of SDR 4.2 million with a maturity at end-2018, and a grant contribution of SDR 0.1 million to the PRGF-HIPC Trust.

Exchange Rate Arrangement:

Since May 2007, the Kuwaiti dinar has been pegged to an undisclosed currency basket, reverting to the exchange system before January 2003. Between January 1, 2003 and May 2007, the Kuwaiti dinar had been pegged to the U.S. dollar with a margin of 3.5 percent on either side around the parity exchange rate of 299.63 fils/U.S. dollar. Kuwait has accepted the obligations of Article VIII, Sections 2 (a), 3, and 4, and maintains an exchange system free of restrictions on payments and transfers for current international transactions, other than those notified to the Fund pursuant to Decision 144-(52/51). On April 2, 2002 Kuwait notified the Fund, under Decision 144-(52/51), of exchange restrictions it introduced in order to implement UN Security Council resolutions 1373 (2001), 1333 (2000) and 1267 (1999).

Article IV Consultations:

- The last Article IV consultation was completed on June 13, 2012 on LOT basis (Published June 18, 2012). The staff report is available at:
<http://www.imf.org/external/pubs/cat/longres.aspx?sk=26007.0>

FSAP Participation

An FSAP Update was conducted in March 2010. It included an updated assessment of a selected number of Basel Core Principles. An FSSA report was discussed by the Executive Board along with the staff report for the 2010 Article IV consultation and it is available at:

<http://www.imf.org/external/pubs/cat/longres.aspx?sk=24096.0>

Technical Assistance:

STA	Seminar on GDDS	February 2000
STA	National Accounts and Price Statistics	June 2001–June 2002
FAD	Restructuring Budget Processes	January/February 2002
FAD	A Program for Tax Reform	December 2002
MFD/LEG	Bank Insolvency	October 2004
FAD	Macro Fiscal Unit	February 2009
STA	External Sector Statistics	February 2009
STA	External Sector Statistics	December 2009
FAD	Value-Added Tax	October 2011
FAD	Macro-Fiscal Unit	September 2012
FAD	Tax Policy and Administration	April 2013
LEG	Central Bank Law	April 2013
LEG	Central Bank Law	September 2013

Resident Representative: None

Kuwait has consented to the quota increase under the Fourteenth General Review of Quotas.

RELATIONS WITH THE WORLD BANK

(As of September 10, 2013)

The World Bank and the Government of Kuwait developed a four-year Country Partnership Strategy (CPS) 2010–13, which leverages the setup of a World Bank Country Office in Kuwait (inaugurated in January 2009).

The Kuwait CPS and program emphasize implementation of reforms. Hence all programs are grounded in the Government five-year plan, and are developed closely with the line ministry/agency as well as with the Ministry of Finance (MoF), which plays the coordinator role and the Bank's central counterpart.

The CPS focuses on Fee-Based Services laying the ground for Bank provision of advisory and analytical support to Kuwait. Program priorities are driven and guided by CPS and revolve around the following three pillars:

- (i) ***Improving public sector performance***, with activities in the areas of reforming procurement; fiscal management, including support for tax modernization efforts; technical advice to streamline outdated procurement and project cycle regulation and practices, support for several environmental initiatives, support government efforts to strengthen policy, institutional and regulatory framework, and information systems to improve public land management and land delivery.
- (ii) ***Economic diversification through increased private sector development***, with support for implementation of Kuwait's recently passed privatization law, support to Kuwait's Oil Company (KPC) as it implements an ambitious privatization program, TA for a number of public-private partnerships and the creation of a more conducive environment for private sector development and foreign direct investment, including activities with Kuwait's Foreign Investment Bureau (KFIB) and an ambitious program with the *Ministry of Commerce and Industry*, in support of the design and implementation of an Insolvency and Creditors Rights framework (based on recommendations from a recent ROSC).
- (iii) ***Human development***, with a major program to support the quality of education, including having an international expert based in Kuwait. Potential Bank support in this area would also include social protection and labor.

Activities for the FY 2013–14

I – Improving public sector performance

- **Environmental Compliance Fund (ECF)**. This activity responds to a request from the Kuwait Supreme Council for the Environment, and subsequently from the Ministry of Finance, for World Bank support in promoting improved environmental performance from point-source/industrial

polluters in Kuwait through the establishment of an ECF. Bank support is consisting of helping the EPA design an environment compliance system to assist the polluting enterprises reduce pollution to the level required by the national standards and guidelines. Such system would consist of the design of the following activities: (i) A Compliance Action Plan (CAP) to be prepared by each of the polluting enterprises to reduce pollution; and (ii) A Financing Window to be established in selected commercial banks to provide a combination of loans and grants to the polluting enterprises in order to implement part or all the activities in the compliance action plans (CAPs).

- **Project Cycle.** At the request of the Ministry of Finance, the World Bank has conducted a review of the government project cycle. Bank work helped explore ways to shorten the project cycle and improve project management practices in Kuwait. As part of this activity, the Bank team has reviewed and analyzed a selection of projects in government entities at three stages: concept, implementation and evaluation. This review is helping identify bottlenecks and areas that need amendments in procedures or regulation/legislation. The Bank is also making recommendations to strengthen the capacity of the Government agencies to implement projects through adequate training.
- **Tax Modernization Support.** The World Bank is supporting efforts by the Kuwaiti Government to modernize tax administration. The project evolved from a technical assistance activity originally designed to help implement a Value Added Tax system in Kuwait as part of its GCC trade union obligations. The activity aims to build capacity, which is where the involvement of the World Bank is critical. This is being achieved through intensive training in tax operations and modern techniques of tax administration, as well as through on-the-job training by the experts hired by the project. This focus on strengthening a critical public sector function – tax administration –in the context of fiscal reform makes the Bank a natural partner for the government. An international resident advisor has been placed in Kuwait to work on this activity.
- **Solid Waste Management II.** This activity is a follow-up to a first phase solid Waste Management program, which aimed at improving Kuwaiti authorities understanding of the current challenges of the solid waste sector and incited them to promote reforms to enhance cost effectiveness of private sector participation, particularly in collection, sorting and recycling of waste. At the request of the Municipality of Kuwait City, the Bank is engaged through this second phase of the program to help implement the main recommendations of the first phase, namely: (i) preparation & implementation of a national priority project for the closure and rehabilitation of existing dumpsites, (ii) elaboration and adoption of a solid waste master plan consistent with Kuwait Land-Use Master plan, to identify national policy & investment priorities for the solid waste sector, (iii) completion & harmonization of existing legal instruments, starting with a Solid Waste Law, and (iv) establishment of a municipal solid waste agency under the municipality's authority.
- **Kuwait Environmental Action Plan.** This activity represents the Kuwaiti national component of the regional initiative for the Gulf Environment Action Program (GEPAP) launched in 2009 by the World Bank, at the meeting of the Gulf Cooperation Council (GCC) Environment Coordination

Committee in Muscat, Oman. The objective of this activity is to support Kuwait's efforts focus on environmental sustainability that could generate financing and economic benefits in addition to protecting Kuwait's natural resources in line with the State's regional and national priorities; and to help establish clear, transparent and predictable environmental regulations that would improve the investment climate in Kuwait. The activity comprises three main components, which are: (i) Implementing a cost assessment of environmental degradation as a decision making tool for delineating policy and investment priorities based on economic and social costs of the various forms of environmental degradation; (ii) Carrying out a pollution load assessment as a decision support system for monitoring and enforcement of environmental regulations; and (iii) Strengthening the environmental impact assessment system as a preventive tool for reducing environmental and social impacts and risks.

- **Follow-up to the Country Procurement Assessment Report (CPAR).** Building on the Bank's 2010 CPAR report for Kuwait, the Bank is supported the MoF procurement team draft a new comprehensive procurement law as a first step in implementing the recommendations and action plan of the CPAR. The Bank team prepared and submitted a draft consolidated Public Procurement Law and supported the MoF in the ratification process. The Bank team has also provided comments on Tendering Legislation presented to the Parliament and is discussing with MoF counterparts future capacity building support activities.
- **Reorganization of State Property.** The objective of the activity is to assist the State of Kuwait in the strategic understanding of the institutional and regulatory issues related to state land policy management in Kuwait. Bank work helped develop a clear understanding of the roles and responsibilities of various entities involved in state land management and identifying the barriers and constraints to effective land management. Bank work is gaining prominence among key decision makers and a presentation for the Ministerial Cabinet is planned for November 2013.
- **Assessment of 'Digital Oasis' project idea and support to the preparation of ICT-SME and Outsourcing Framework.** The Bank is supporting Kuwait's Central Agency for Information Technology (CAIT) with: (i) the assessment of the feasibility of a 'Digital Oasis' project; and, (ii) the preparation of a framework for IT Outsourcing; and (iii) the promotion of SME's in ICT.
- **Public Expenditure and Financial Accountability (PEFA – Phase II)** – In follow up to the PEFA exercise conducted in FY11, MoF requested Bank support to help build capacity and improve Ministry teams understanding of the PEFA framework and help them play a more active role in the preparation of future PEFA assessments. The Project also aims at improving the comprehension of the PEFA framework at the senior leadership level to help them better utilize the framework and make informed and strategic public financial management (PFM) reform policies that will serve the interest of the State of Kuwait.

II – Economic diversification through increased private sector development

- **Kuwait Foreign Investment Bureau (KFIB) Support.** The World Bank is supporting KFIB in developing feasibility studies and master plan(s) for three new economic zones for foreign investors (Wafra, Abdali, and Shegaya). KFIB has contracted a private consulting firm to conduct the feasibility study and a World Bank team is supporting KFIB during the implementation of the study, through review of the consultant's outputs and providing comments to ensure quality output:
- **Privatization Support.** At the request of the Minister of Finance the World Bank has been supporting the implementation of a recently passed Privatization Law. Bank support included helping draft By-Laws for the law and a policy (vision) statement to provide additional rationale and explanation for the draft By-Laws. Bank support also included Portfolio development through sector assessments. Further Bank assistance may include transaction support, public education, and support to enhance corporate governance and post-privatization reforms.
- **ROSC Insolvency & Creditor Rights.** Ministry for Commerce and Industry (MoCI) requested Bank's support in moving forward with a number of reforms to help improve Kuwait's investment climate starting with a review of Insolvency and Creditors Rights in Kuwait (ICR). Bank work led to a recommendation for the need for new laws regulating Enterprise Rehabilitation and Liquidation in Kuwait. Subsequently, a World Bank TA program has been agreed with MoCI for the Bank to support: (i) the development of a functional workout framework to stabilize and help recovery of Investment Companies and the enterprise sector; (ii) reforms to improve liquidation and rehabilitation procedures, including the promotion of more reliable access to credit information for credit providers, wider access to credit based on security interests in movable assets, and a registry governing security interests in movable assets; and (iii) enhancing professional development of commercial judicial specialization.
- **Preparation of a CDM Project for Kuwait Gulf Oil Company (KGO) – the Central Gas Utilization Project.** Under this TA the supporting KGO with the preparation of a CDM project: "KGO Central Gas Utilization Project (CGUP)", which will capture and utilize associated gases that otherwise would have been flared. This TA is based on specific request from KGO and is being delivered primarily in the form of support in preparing a CDM Project Design Document (PDD), selecting and contracting of a DOE for validation of the CDM activity, and submission of the CDM project for registration at the UNFCCC.

III – Human development

- **Education Sector TA.** Building on the success of the *School Education Quality Improvement (SEQI)* Program - designed to support the Ministry of Education (MoE) to implement selected critical elements of its own 4-year Government Program, the World Bank is partnering with MoE in expanding the cooperation program to improve the output of the education process, including through work on curriculum, and developing a school leadership framework. The World Bank work in the education sector has further expanded to

include support the work of the National Center for Assessment and Evaluation (NCAE) as well as support for the development of a strong higher education sector strategy, which will include a sector review and benchmarking to regional and more global standards.

- **Development of Social Safety Net Strategic Framework.** Kuwait's Ministry of Social Affairs and Labor (MOSAL) requested World Bank support to develop a more coherent Social Safety Net Strategic Framework. Under this activity the Bank is supporting the Government of Kuwait in undertaking an assessment of existing social policies and programs in Kuwait, and developing a Social Safety Net Strategic Framework that is consistent with international practices, and grounded within the socio-economic context of Kuwait.
- **Labor Market Information System (LMIS).** Under this activity the World Bank is supporting the government of Kuwait with the establishment of an LMIS through the set-up of institutional arrangements, processes, and tools for the collection, integration, analysis, policy formulation, and dissemination of labor market information.

STATISTICAL ISSUES

(As of October 3, 2013)

I. Assessment of Data Adequacy for Surveillance

General: Data provision has some shortcomings, but is broadly adequate for surveillance. Despite further improvements in the current year, there is scope for improved compilation of the national accounts and balance of payments statistics through better coordination among statistical agencies. Timeliness, particularly for the national and fiscal accounts, is an area of concern.

National Accounts and Production: Past improvements of national accounts include: change of the base year for the constant price data to 2000 and the estimates of value added for subsidized goods and services of the public utilities sector through the use of input costs (the household expenditure survey was used previously). Continued progress, especially in the estimation of value added for the oil sector, requires the dedication of adequate resources and improved coordination between the Ministries of Planning, Oil, and Finance. The IMF's statistics department (STA) has provided technical assistance to the Ministry of Planning to improve national accounts and price data. It would be useful if the Central Bank of Kuwait (CBK) would publish oil sector information in the *Quarterly Statistical Bulletin* pertaining to output, refining, domestic consumption, export price for crude and refined products and the domestic price of petroleum products. These data are available from the Ministry of Oil. Timeliness of the data needs to be improved. In the last few years, delays in the production of price indexes caused long lags in the production of real GDP data. Recent improvements in the compilation of statistics are expected to reduce publication lags and produce quarterly data.

Price statistics

CPI weights are based on the 2007 household expenditure survey and were introduced into the index for a reference year of 2007. An improved monthly CPI based on a revised basket has been published in monthly CPI bulletins with about a one-month lag. The wholesale price index (WPI) needs to be developed into a producer price index (PPI) which is consistent with the national accounts and includes all domestically produced goods, ex-factory, for the export and the domestic market.

Government finance statistics: Annual GFS data are reported for publication in the *Government Finance Statistics Yearbook (GFSY)*. The major components of extrabudgetary revenues (investment income and transfers of profits of public institutions), extrabudgetary expenditures (interest on foreign debt and treasury paper), and financing operations conducted by two reserve funds are not reported. Data on interest on foreign debt and treasury paper are usually provided to Article IV consultation missions, but the regular provision of data on investment income is lacking.

The authorities have made some progress in fiscal data presentation, but the lack of a suitable classification of data on the execution of the budget remains a constraint on monitoring effectively fiscal developments during the year. The authorities' presentation is not yet fully compliant with the GFSM 2001 guidance, but progress is being made in terms of creating a new chart of accounts and moving reporting to an accrual basis.

Data on the operations of the Public Institute for Social Security are not made available. Sharing of information between various government agencies could be improved. STA has indicated to the authorities that operations of the two reserve funds should be classified as part of government, as they perform activities for public policy purposes (management of debt and assets, and financing of the budget). An additional extension of coverage would be to report GFS in the form of the Statement of Sources and Uses of Cash for the consolidated central government. The authorities have also been briefed on the IMF's ongoing work to enhance the transparency of fiscal accounts and presentations detailed in the "Code of Good Practices on Fiscal Transparency" and were encouraged to adopt some of the practices recommended in the Code.

Monetary and financial statistics

The CBK reports monetary data to STA on a regular and timely basis based on the Standardized Report Forms (SRFs). CBK needs to work further to distinguish a number of investment companies that accept deposits from other investment companies that do not accept deposits. Investment companies that accept deposits should appropriately be classified as part of the depository corporations sector. In the current SRFs, all investment companies (including those that accept deposits) are classified as other financial corporations. However, the amount of deposits accepted by investment companies is considered as not significant. The Capital Markets Authority needs to collate and disseminate information related to investment companies.

Balance of Payments Statistics: The CBK compiles and disseminates detailed annual data in accordance with the methodology of the *BPM6*, while trade data estimates are disseminated monthly. However, data on capital flows of the nonfinancial private sector are limited. To improve coverage for inward foreign direct investment, the CBK is making efforts to obtain more data by surveying direct investment enterprises. The Central Statistical Office (CSO), working with the CBK, implemented the IMF's Coordinated Direct Investment Survey in 2010-12. This initiative should improve foreign direct investment statistics. Enhancements have been made in the estimation of travel services and communication services, but further improvements are needed in compilation practices and in the estimation of data on several service items and private transfers.

A major step forward in 2007 was the dissemination of IIP data for 2001 onwards in STA publications. However, the information on IIP data made available to staff is incomplete as it excludes the external assets held by the general government due to domestic legal constraints on dissemination (however, loans granted by the Kuwaiti Fund for Arab Economic Development and general government trade credits are included).

The CBK also participates in the Coordinated Portfolio Investment Survey (CPIS) with data reported for 2003 onwards, and in the recently introduced Coordinated Direct Investment Survey. These data are for the financial sector acting as end-investors or as intermediaries on behalf of residents and do not include holdings of foreign securities held by government agencies, which comprise the bulk of Kuwait's cross-border holdings.

In 2009, STA provided TA on improving external accounts data. The CBK has made good progress since then, particularly in the substantial revisions to report forms, including the separate reporting of financial transactions in the BOP and other changes in volume in the international investment position. It has also made progress in the estimation of remittances data. Yet, major delays and data gaps remain. In particular, major government entities do not report quarterly data to the CBK in time to compile timely quarterly statistics. Trade data are compiled by the CSO annually and provided to the CBK with a time lag of well over one year. Furthermore, the response rate for the private nonfinancial sector is low.

II. Data Standards and Quality

Kuwait is one of the first GDDS participants. However, most of its metadata, with the exception of the real sector and socio-demographic metadata, have not been updated since October 2002. The CBK maintains its own webpage where it provides the following data to the public: money and banking statistics; balance of payments statistics; trade balance statistics; exchange rate; GDP by sector and expenditure at current and constant prices; public finance statistics; CPI and WPI; and security market indicators. Similarly, the Ministry of Planning has a webpage where the CSO publishes data on national accounts, prices, and other related statistics. The Ministry of Finance webpage includes detailed data for actual and estimated budget operations. In addition, the Kuwait Stock Exchange webpage provides data on stock market indices, volume and value of securities traded, as well as privatization schedules and other related information.

No data ROSC is available.

TABLE OF COMMON INDICATORS REQUIRED FOR SURVEILLANCE
(As of October 3, 2013)

	Date of latest observation (For all dates in table, please use format (dd/mm/yy))	Date received	Frequency of Data ⁷	Frequency of Reporting ⁷	Frequency of Publication ⁷	Memo Items: ⁸	
						Data Quality Methodological soundness ⁹	Data Quality Accuracy and reliability ¹⁰
Exchange rates	02/10/2013	02/10/2013	D	D	D		
International reserve assets and reserve liabilities of the monetary authorities ¹	30/06/2013	10/09/2013	M	M	M		
Reserve/base money	30/06/2013	10/09/2013	M	M	M		
Broad money	30/06/2013	10/09/2013	M	M	M		
Central bank balance sheet	30/06/2013	10/09/2013	M	M	M		
Consolidated balance sheet of the banking system	30/06/2013	10/09/2013	M	M	M		
Interest rates ²	30/06/2013	10/09/2013	M	M	M		
Consumer price index	31/08/2013	01/10/2013	M	M	Q		
Revenue, expenditure, balance and composition of financing ³ —general government ⁴	31/03/2013	10/09/2013	Q	Q	Q	Not published on Fund standards	Not published on Fund standards
Stocks of central government and central government-guaranteed debt ⁵	31/12/2012	10/09/2013	M	M	M		
External current account balance	31/12/2012	09/04/2013	A	A	A		
Exports and imports of goods and services	31/12/2012	09/04/2013	A	A	A		
GDP/GNP	31/12/2011	31/12/2012	A	A	A		
Gross external debt	31/12/2012	09/04/2013	A	A	A		
International investment position ⁶	31/12/2012	10/09/2013	A	A	A		

¹ Any reserve assets that are pledged or otherwise encumbered should be specified separately. Also, data should comprise short-term liabilities linked to a foreign currency but settled by other means as well as the notional values of financial derivatives to pay and to receive foreign currency, including those linked to a foreign currency but settled by other means.

² Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.

³ Foreign, domestic bank, and domestic nonbank financing.

⁴ The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.

⁵ Including currency and maturity composition.

⁶ Includes external gross financial asset and liability positions vis-à-vis nonresidents.

⁷ Daily (D); weekly (W); monthly (M); quarterly (Q); annually (A); irregular (I); and not available (NA).

⁸ These columns should only be included for countries for which Data ROSC (or a Substantive Update) has been published.

⁹ Reflects the assessment provided in the data ROSC or the Substantive Update (published on ..., and based on the findings of the mission that took place during...) for the dataset corresponding to the variable in each row. The assessment indicates whether international standards concerning concepts and definitions, scope, classification/sectorization, and basis for recording are fully observed (O); largely observed (LO); largely not observed (LNO); not observed (NO); and not available (NA).

¹⁰ Same as footnote 9, except referring to international standards concerning (respectively) source data, assessment of source data, statistical techniques, assessment and validation of intermediate data and statistical outputs, and revision studies.



Press Release No. 13/479
FOR IMMEDIATE RELEASE
December 2, 2013

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Executive Board Concludes 2013 Article IV Consultation with Kuwait

On November 25, 2013, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with Kuwait.¹

High oil prices and increased production have enabled the government to continue to record high fiscal and external surpluses and build strong buffers. Overall real non-oil gross domestic product (GDP) growth is projected to increase modestly to 3 percent in 2013, driven by an increase in domestic consumption and pick-up in public investment. A slight reduction in oil production would bring down total real GDP growth below 1 percent. The overall average consumer price inflation (CPI) is projected at 3 percent in 2013. The fiscal and external surpluses are projected at 27 percent of GDP and 39 percent of GDP, respectively, in 2013, reflecting high oil prices. Monetary policy has remained accommodative and bank credit growth has picked up.

Bank profitability has remained stable and soundness indicators appear strong. Banks had an average capital adequacy ratio of 18.3 percent (Tier 1 capital of 16.6 percent) at end-June 2013. Gross nonperforming loans declined to 4.6 percent at end-June 2013 from 5.2 percent at end-2012. Banks had a provisioning ratio of 107 percent at end-June 2013. Some investment companies continued to record losses in 2012, though of a lower order compared to 2008; a few of these are still deleveraging and restructuring their balance sheets.

The economic outlook is expected to improve further in 2014 and over the medium term. In 2014, non-oil growth is expected to increase to 4.4 percent supported by public capital spending, driving average inflation to 3.5 percent. A constant level of oil production would keep total real GDP growth below 3 percent. Fiscal and current account surpluses are expected to remain large in 2014. Over the medium term, non-oil growth is projected to accelerate to about 5 percent as large infrastructure investments are expected to support the growth momentum. A moderate increase in oil production is expected to further support overall growth. Inflation is projected to increase slightly as growth picks up. The fiscal and current account surpluses are projected to taper if spending continues on the current growth trajectory. The main downside risk to the outlook is a sustained fall in oil prices.

¹ Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

Executive Board Assessment²

Executive Directors welcomed Kuwait's recent economic performance. High oil prices and increased production have enabled the build-up of large fiscal and external buffers, and the non-oil sector is continuing its recovery. Nevertheless, the outlook is subject to risks from global and regional developments, and the economy remains highly oil-dependent. Directors therefore encouraged the authorities to make further efforts to promote economic diversification, particularly in areas with potential for greater national employment.

Directors noted that while the fiscal position is strong, a sustained period of low oil prices could deplete fiscal surpluses. To contain risks, free up resources for increased capital spending, and to save for future generations, Directors agreed that it will be important to restrain current expenditure growth, including the public sector wage bill and generalized subsidies, and to enhance non-oil revenues. They considered that strong fiscal frameworks will be needed to guide public spending in the medium term. In this context, strengthening the macro-fiscal unit would support the development of a medium-term budget framework and greater efficiency of public spending.

Directors agreed that the current accommodative monetary stance remains appropriate and the exchange rate peg to a basket has provided a strong and credible monetary anchor. They noted that the banking system is well regulated and resilient to shocks, and welcomed continued steps to strengthen financial regulation and supervision. Continuous refining of the macroprudential toolkit and greater central bank autonomy would enable the authorities to better deal with systemic risk. Directors cautioned that the recent large consumer debt relief program could give rise to moral hazard. Noting the continued weak balance sheets of some investment companies, they called for the completion of the restructuring process and a review of the sector.

Directors welcomed the recent passage of important legislation that will enhance the investment climate and forge partnerships with the private sector, and encouraged further steps in this direction. To foster Kuwaiti employment in the private sector, Directors underscored the need to contain public sector wage and employment growth, enhance educational quality, further promote female labor force participation, and create an enabling environment for small and medium enterprises. Well-functioning local debt markets could help the diversification process. Directors also encouraged continued efforts to improve effectiveness in public administration, and the establishment of an independent Financial Intelligence Unit.

² At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: <http://www.imf.org/external/np/sec/misc/qualifiers.htm>.

Kuwait: Selected Economic Indicators, 2007–14

(Quota: SDR 1,381.1 million)
 (Population: 3.8 million; Dec. 2012)
 (Per capita GDP: \$48,260; 2012 estimate)
 (Poverty rate: n.a.)
 Main exports: oil and gas

	2007	2008	2009	2010	2011	Prel. 2012	Proj. 2013	2014
Oil and gas sector								
Total oil and gas exports (billions of U.S. dollars)	59.1	82.6	48.9	61.8	96.7	113.7	108.3	104.9
Average oil export price (U.S. dollars/barrel)	68.4	92.2	61.5	77.7	103.3	107.1	107.1	104.0
Crude oil production (millions of barrels/day)	2.57	2.68	2.26	2.31	2.66	2.98	2.93	2.93
(Annual percentage change, unless otherwise indicated)								
National accounts and prices								
Nominal GDP (market prices, in billions of Kuwaiti dinar)	32.6	39.6	30.5	34.4	44.3	51.3	51.7	52.3
Nominal GDP (market prices, in billions of U.S. dollars)	114.7	147.4	106.0	119.9	160.7	184.5	186.1	188.1
Real GDP (at factor cost)	6.0	2.5	-7.1	-2.4	6.3	6.2	0.8	2.6
Real oil GDP	-4.7	6.5	-12.9	0.5	14.2	11.7	-2.0	0.0
Real non-oil GDP	14.7	-0.5	-3.5	-3.9	0.9	2.2	3.0	4.4
CPI inflation (average)	5.5	6.3	4.6	4.5	4.9	3.2	3.0	3.5
Unemployment rate (Kuwaiti nationals)	6.1	4.9	3.6	2.9	3.4	...	...	...
(Percent of GDP at market prices)								
Investment and savings								
Investment	20.5	17.6	18.0	20.3	16.4	15.1	16.4	18.1
Public	3.3	3.5	4.8	5.5	4.5	3.8	5.3	6.6
Private ¹	17.1	14.1	13.2	14.8	11.9	11.3	11.1	11.5
Gross national savings	57.2	58.5	42.3	52.6	59.5	58.3	55.2	55.8
Public	55.2	46.8	50.6	50.3	55.8	54.9	53.5	51.5
Private ¹	2.1	11.7	-8.3	2.3	3.7	3.4	1.7	4.3
(Percent of GDP at market prices)								
Budgetary operations²								
Revenue	67.9	64.3	63.8	65.9	73.2	70.4	68.9	68.6
Oil	51.6	52.8	52.7	54.1	62.0	58.3	56.4	53.8
Non-oil, of which:	16.3	11.5	11.1	11.7	11.2	12.1	12.5	14.8
Investment income	13.1	8.7	8.2	8.1	8.1	8.8	9.1	11.3
Expenditures	28.1	48.5	35.3	43.5	36.5	37.0	41.5	43.5
Expense ³	24.0	44.1	30.7	38.0	32.2	33.0	35.7	36.6
Capital	4.1	4.4	4.6	5.6	4.4	4.1	5.9	6.9
Balance	39.8	15.8	28.4	22.3	36.7	33.4	27.4	25.1
Domestic financing	-3.1	-4.6	-1.8	1.1	-0.2	-1.8	-3.2	-1.7
External financing	-36.7	-11.2	-26.7	-23.4	-36.5	-31.7	-24.2	-23.4
Non-oil balance (percent of non-oil GDP) ⁴		-56.4	-77.5	-89.6	-86.1	-89.9	-97.0	-95.1
Total gross debt (calendar year-end) ⁵	7.0	5.3	6.7	5.9	4.5	3.4	2.4	2.4
(Percent change; unless otherwise indicated)								
Money and credit								
Net foreign assets ⁶	3.1	33.1	24.1	-0.5	21.1	21.3	17.5	8.7
Claims on nongovernment sector	35.1	16.7	6.1	1.9	2.6	3.2	7.7	8.0
Kuwaiti dinar 3-month deposit rate (year average; in percent)	5.0	3.4	1.7	1.3	1.1	1.0	...	...
Stock market unweighted index (annual percent change) ⁷	24.7	-38.0	-10.0	-0.7	-16.4	2.1	...	...
(Billions of U.S. dollars, unless otherwise indicated)								
External sector								
Exports of goods	62.6	87.0	54.4	67.1	103.0	120.1	115.1	111.9
Of which: non-oil exports	3.5	4.4	5.5	5.3	6.2	6.4	6.7	7.0
Annual percentage change	6.4	25.1	26.5	-3.4	17.0	2.7	4.9	3.9
Imports of goods	-19.1	-22.9	-18.5	-19.4	-22.1	-22.6	-24.0	-25.9
Current account	42.2	60.2	28.3	37.0	67.2	79.8	72.1	71.0
Percent of GDP	36.8	40.9	26.7	30.8	41.8	43.2	38.7	37.7
International reserve assets ⁸	15.9	16.7	17.7	18.7	23.0	25.8	27.6	29.4
In months of imports of goods and services	5.9	5.3	6.6	6.4	6.9	7.3	7.4	7.3

Kuwait: Selected Economic Indicators, 2007–14 (concluded)

(Quota: SDR 1,381.1 million)
 (Population: 3.8 million; Dec. 2012)
 (Per capita GDP: \$48,260; 2012 estimate)
 (Poverty rate: n.a.)
 Main exports: oil and gas

	2007	2008	2009	2010	2011	Prel. 2012	Proj.	
							2013	2014
Memorandum items:								
Exchange rate (U.S. dollar per KD, period average)	3.52	3.72	3.48	3.49	3.63	3.60		
Nominal effective exchange rate (NEER, period average)	-2.1	2.9	-3.6	-0.3	0.5	1.6		
Real effective exchange rate (REER, period average)	-0.3	7.8	-1.0	0.9	1.6	1.6		
Sovereign rating (S&P)	AA-	AA-	AA-	AA-	AA	AA		

Sources: Data provided by the authorities; and IMF staff estimates and projections.

¹ Also includes government entities.

² Kuwaiti fiscal year ending March 31, e.g. 2007 refers to fiscal year 2007/08.

³ In 2006/07 KD 2 billion was transferred to partly cover the actuarial deficit of the Public Pension Fund.

In 2008/09, KD 5.5 billion was transferred. KD 1.1 billion is budgeted for each year from 2010/11 to 2014/15.

⁴ Excludes investment income and pension recapitalization, and after transfers for FGF (fiscal year).

⁵ Excludes debt of Kuwait's SWF related to asset management operations.

⁶ Excludes SDRs and IMF reserve position.

⁷ Change in the KSE as of May 9 2012 for 2012.

⁸ Does not include external assets held by Kuwait Investment Authority.

**Statement by Mr. Shakour Shaalan, Executive Director for Kuwait
November 25, 2013**

1. On behalf of the Kuwaiti authorities, I would like to thank staff for their continued constructive engagement with Kuwait. The authorities appreciate the helpful discussions which focused on further strengthening macroeconomic and financial stability, diversifying the economy, and promoting job creation.

Recent developments

2. While Kuwait's strong GDP growth reflected high oil production and prices in recent years, the non-hydrocarbon sector has become a key contributor to growth in 2013, driven by an increase in domestic consumption and a pick-up in public investment. The fiscal and external accounts continued to post large surpluses, reflecting high international oil prices. The economic outlook is expected to improve further in 2014 and over the medium term, as large infrastructure projects are implemented. Notwithstanding this performance, the authorities are committed to further developing the non-oil economy while continuing to strengthen macroeconomic and financial stability.

Macroeconomic policy mix

3. While the fiscal position is strong, the authorities are aware that increased capital spending warrants containment of current expenditure to maintain intergenerational equity. In order to enhance non-hydrocarbon revenue, they are in the process of implementing an invoice system for electricity bills to improve service collection. They are also considering the introduction of a value-added tax in coordination with other GCC countries. On the expenditure side, the authorities concur with staff on the importance of better targeting subsidies, and the Ministry of Finance is planning to evaluate the existing subsidy system. They acknowledge the importance of containing wages of public employees, but are faced with continued pressures to absorb Kuwaitis entering the workforce, since the private sector is currently not absorbing them. The authorities consider that garnering broad public support is important for the success of their fiscal reforms.

4. The authorities are committed to increasing capital spending to advance social and physical infrastructure projects and promote non-oil growth. In this connection, they are determined to ensure the quality and efficiency of government spending, which entails clear prioritization and sequencing of infrastructure projects. They have already identified and completed feasibility studies for a number of priority projects including power stations, water waste management, and schools and hospitals that can attract private sector participation.

5. Monetary policy remained accommodative in the past year, in line with the domestic and external environments. The Central Bank of Kuwait (CBK) plays a proactive role in managing liquidity through the short- and long-term bill and bond markets. The authorities see merit in staff's advice to further deepen the domestic money market, but feel that CBK transactions are currently serving the purpose of managing liquidity in the market. The current basket pegged exchange rate regime continues to serve the Kuwaiti economy well.

Financial stability

6. The Kuwaiti banking system is well-regulated, well-capitalized, liquid, and profitable. Moreover, staff's analysis and the CBK's stress testing results point to the resiliency of the banking sector to severe shocks. Recent regulations introduced by the central bank, including guidelines for the implementation of Basel III and stricter provisioning rules, are aimed at further strengthening risk management by banks.

7. The central bank has a range of macroprudential instruments to contain emerging financial risks. It sees merit in staff's recommendations to develop a more formal macroprudential policy framework to support financial stability and to promote the independence of the CBK. Risks to financial stability posed by investment companies (ICs) are very negligible in view of the low exposure of banks to this sector. Local banks' funding to ICs has continued to decline, while exposure to troubled ICs has been contained through full provisioning. Efforts are ongoing to strengthen ICs regulations. Recent indicators show that ICs continued to deleverage in 2013, relying on equity-debt swaps and asset sales, and their losses in 2012 were low relative to previous years.

Economic diversification and job creation

8. The authorities focused in recent years on further diversifying the economy and promoting private-led growth. On the legislative front, several laws were passed that are expected to boost private sector investments, especially the Company Law, the Direct Investment Promotion Law, and the institutional framework for public-private-partnership. Significant progress was also achieved in improving Kuwait's business environment, with the creation of special economic zones, a one-stop system to expedite the issuance of business licenses, and a fund to finance SMEs. The authorities are committed to further encouraging nationals to seek private sector jobs. They believe that their focus on increasing the role of the private sector would be helpful in this regard.