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Session 2 - Industry Outlook in Light of World Economic Situation
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The Likely Impact of a Twin Crisis on MENA Macroeconomic and Energy Investment Outlooks

An Abridged Version to Support Session Two's Panel Discussion

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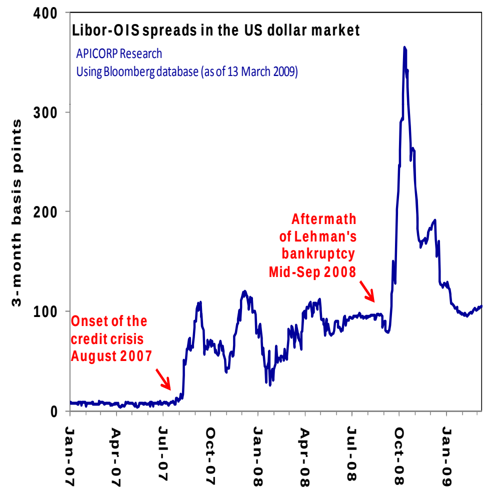
Outline of presentation

- One crisis then another…
  - The credit market crisis
  - The oil market crisis
- Impact on the macroeconomic outlook
- Impact on the investment outlook
- Conclusions and policy recommendations

The credit crisis: Drastic and decisive policy measures have had little impact so far

- Libor-OIS spread – a key measure of risk and liquidity in he money market – has fallen back to its pre-Lehman levels
- However, it is still too high to infer any momentous improvement of the interbank market



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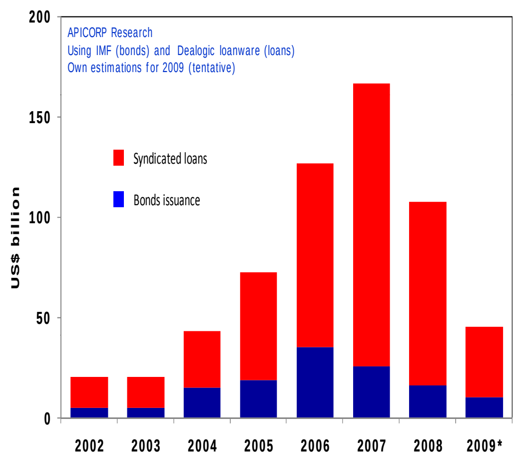
The most notable and measurable impact of the crisis on MENA has been…

- A significant contraction of capital inflows (bonds issuance and syndicated loans) in 2008
- This contraction is most likely to continue into 2009



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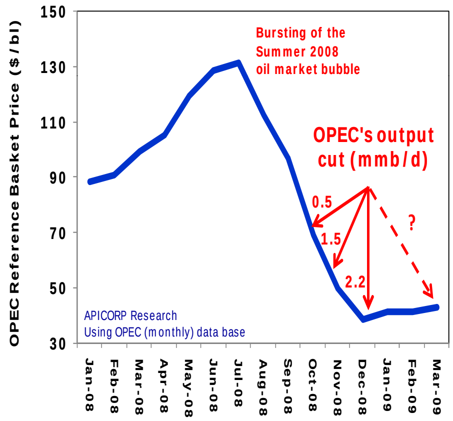
The oil market crisis: The bursting of the Summer 2008 bubble has thrown OPEC into crisis management mode

- Cutting output three times since September has set a floor of $40/bl
- A fourth cut will be needed to drive prices higher towards a "fair" $75/bl



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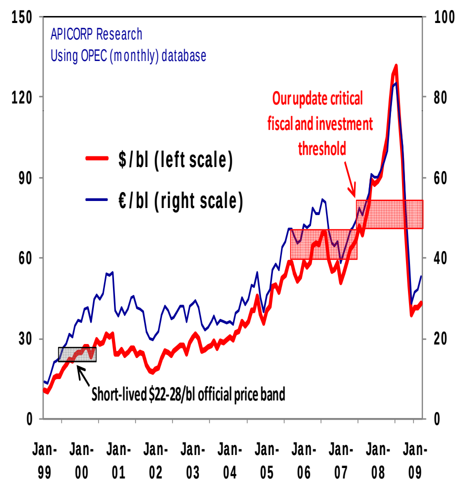
What is a fair price for oil and what makes $75/bl seem fair?

- The value of a barrel of oil a dysfunctional market is unable to determine
- The price needed to keep costly new projects at the margins of world supply
- Lies within our OPEC fiscal and investment threshold of $70-80/bl



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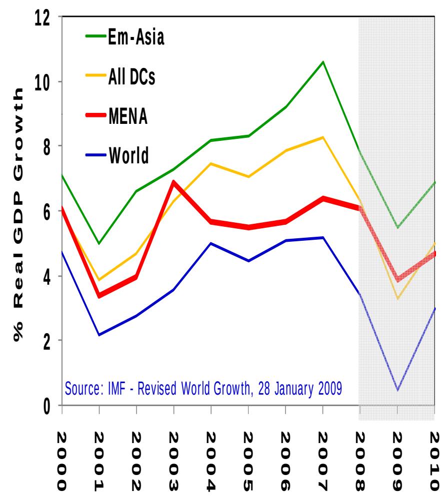
Macroeconomic impact of the twin crises: Have we been “behind the curve” in our anticipations?

- The IMF went through two revisions of its Oct. 2008 forecasts before acknowledging the depth of global recession
- Our forecast assumes a 4% growth for the period 2009-2013, which implies lower rates for 2009 and 2010 than the IMF’s



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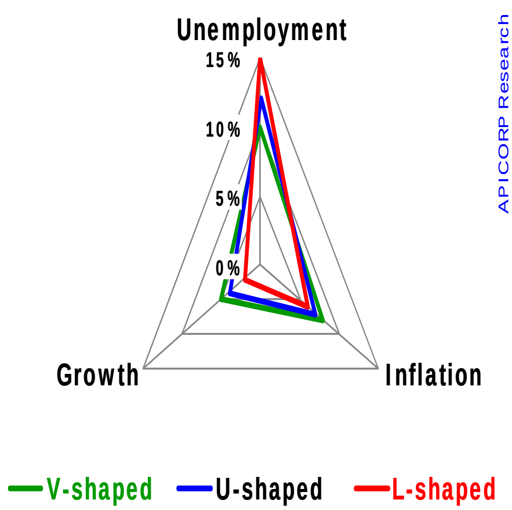
Whatever the length and depth of MENA economic contraction (V, U or L-shaped)

- Recent trends of rising inflation and strengthening job markets are likely to reverse
- As a result, unemployment is expected to move up the region’s socio-economic policy agenda



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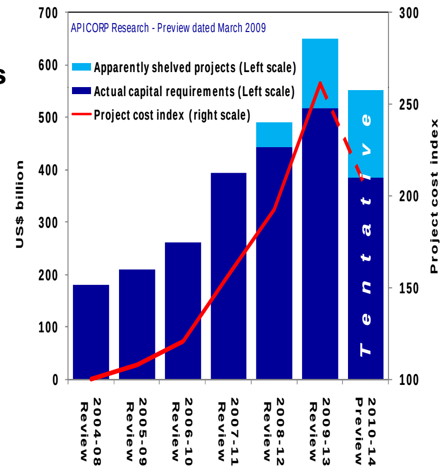
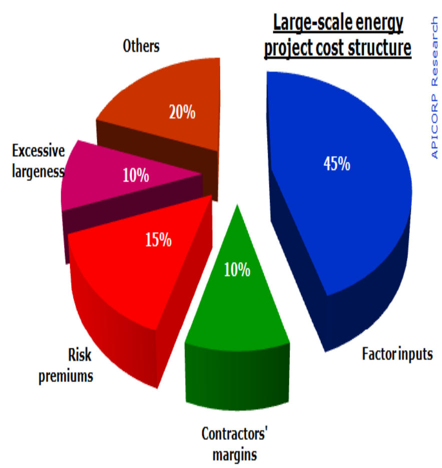
The impact on energy investments is shown in our 5-year period review (2009-2013) and tentative preview (2010-2014)

- In a context of lower demand, our preview points to lower potential capital requirements resulting mainly from lower costs
- Both the review and the preview point to the upside likely to be capped by further shelving or suspension of key projects



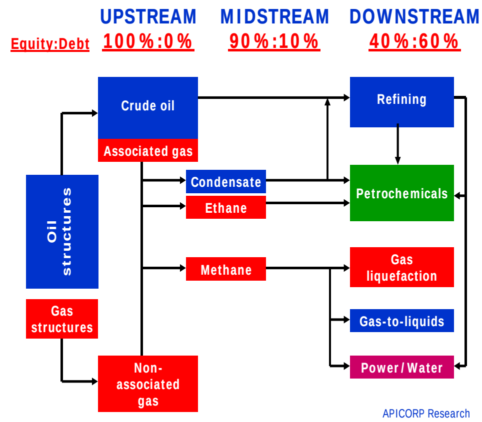
Lower project costs than what has so far been assumed are a key factor in the outlook. Using IPA's parameters we expect:

- Lower costs of factor inputs
- Stable to lower contractors' margins
- Stable to higher risk premiums
- And, adding our own parameter: Stable to lower cost of "excessive largeness"



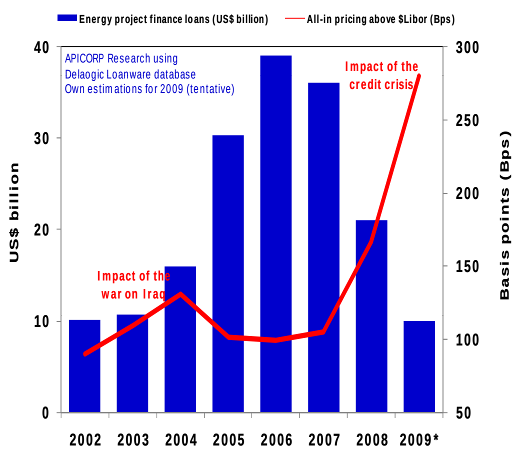
The shift towards more equity of the overall capital structure will make self-financing more challenging

- Current trends point towards more equity across all links in the oil and gas supply chains
- Oil prices below $70-80/bl, will make it difficult to fund equity through retained earnings



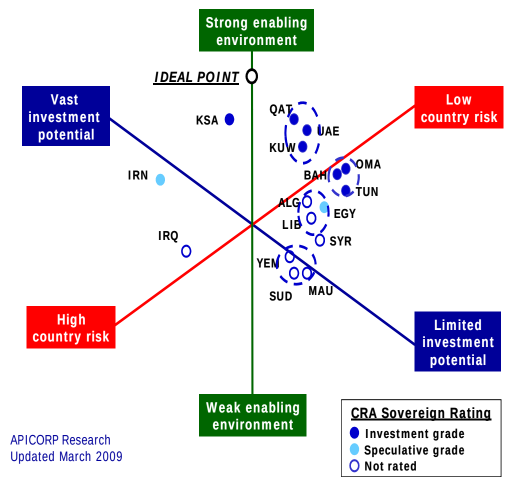
Considerably more challenging and costly will be securing the appropriate amount and mix of debt owing to...

- Lesser credit availability
- Higher costs of borrowing
- Tighter lending standards



In these conditions, the best policy response is to reduce perceived risks

- Our ***Perceptual Mapping***, which is based on three attributes, exhibits an ***Ideal Point***
- The farther from the ideal point the considerably more challenging will the task be



Conclusions

- The financial crisis has broadened, deepened and spread to gradually engulf MENA
- Downward trends in the credit and oil markets are taking a toll on both:
  - The MENA macroeconomic outlook, which is expected to deteriorate seriously
  - The energy investment outlook whose lower potential is likely to be capped further

Our policy recommendations

- ✓ **Making up for shrinking capital inflow** by reallocating internally the capital invested offshore (SFs and SWFs)
- ✓ **Supporting mainstay Regional Financing Institutions** with short term liquidity and eventual recapitalization
- ✓ **Reinforcing Development Funds** that promote growth in the private sector and reward job creation
- ✓ **Excluding from any "option to wait"** infrastructure energy projects in current reviews of investment strategies
- ✓ **Reducing perceived country risks** to avoid lower credit limits and higher costs of external borrowings