Risks highlighted in the April 2022 WEO have materialized—commodity prices remain high, global financial conditions have tightened faster and by more than previously expected, and a worldwide slowdown is underway.

Economic activity in the ME&CA has been resilient thus far, but inflation surprised on the upside, and the region is facing exceptional uncertainties and downside risks. Multispeed recovery continued in early 2022. Activity in oil exporters is benefiting from still-high energy prices, while the pace of expansion in emerging market and middle-income economies (EM&MIs) appears to be slowing, as these economies face a deep terms-of-trade shock, higher sovereign spreads, and eroded market access. The impact of the war in Ukraine on the CCA has been so far milder than forecast, with some unexpected positive spillovers, including significant inflows and the relocation of workers and firms from Russia, supporting domestic activity. Meanwhile, inflation across ME&CA continued to increase through July and has become broad-based.

MENA countries face diverse prospects. Real GDP is forecast to grow 5.0 percent in 2022, up from 4.1 percent in 2021. However, worsening global conditions will weigh on the outlook for 2023, with growth slowing to 3.6 percent. Forecasts for 2022-23 are unchanged from April.

- For oil exporters, high oil prices and robust non-oil GDP growth are offsetting the impact of high food prices, with their economies foreseen to grow 5.2 percent, up from 4.5 percent in 2021. Growth will likely slow to 3.5 percent in 2023 as OPEC+ production increases wane, oil prices decline, and global demand slows.

- Real GDP growth in EM&MIs is forecast at 4.9 percent in 2022, a 0.5 percentage point upward revision from April, driven by Egypt’s performance during fiscal year 2022. Growth will slow to 3.9 percent in 2023, reflecting decelerations in Egypt and Tunisia.

- Growth in LICs is expected to remain weak at 0.8 percent in 2022 (a 0.3 percentage point downward revision from April), reflecting country-specific fragilities and the impact of high commodity prices.

Headline inflation for MENA (excluding Sudan) is expected to remain in double digits in 2023 for the third consecutive year. Forecasts for 2022–23 (12.1 and 11.2 percent, respectively) are revised up from April, reflecting the lagged effects of higher food prices and, in some cases, exchange rate depreciations with broadening inflationary pressures.

Oil exporters’ external accounts are projected to improve further in 2022–23 as oil and gas prices remain considerably higher than their 2020–21 levels. Their primary non-oil fiscal balances are also projected to improve, with most GCC countries expected to continue to save a substantial share of their oil revenues. Overall, oil exporters are projected to accrue a cumulative oil windfall of about $1 trillion over 2022–26.

Despite high commodity prices and the global slowdown, EM&MIs’ current account deficits are projected to remain roughly at their 2021 levels this year, reflecting robust remittance flows and resurgent tourism in some countries. However, lower foreign exchange reserves amid global financial tightening indicate an
increase in their external vulnerabilities. Their primary fiscal deficits are projected to improve slightly relative to 2021 despite higher subsidies due to offsetting measures amid weakened fiscal space. Nonetheless, continued primary deficits, higher interest payments, and in some cases increased reliance on short-term financing will raise public gross financing needs to $384 billion in 2022–23.

**LICs** are projected to face a large deterioration in their external accounts, with higher imports concentrated on essential food and energy items. They are likely to experience severe food security challenges. With limited access to financing and drought in some, these countries will need international aid to secure staple food imports.

**CCA countries are holding up well, but uncertainty lies ahead.** Growth is expected to slow to 3.8 percent in 2022 from 5.6 percent in 2021. Yet, projections were upgraded by 2.0 and 5.6 percentage points in LICs and EM&MIs, respectively, relative to April, reflecting an upward revision to Russia’s real GDP growth forecast, unexpected inflows, resilient trade, and fiscal stimulus in some countries. These factors are expected to fade over time—growth in 2023 is foreseen at 4.0 percent and will likely narrow to 3.5 percent (below the historical average of almost 7 percent) in the medium term. Inflation is also forecast to remain in double digits during 2022–23 (at 12.9 percent in 2022 and 10.5 percent in 2023), with upward revisions from April for both years.

Higher oil prices and spillovers from the war in Ukraine dominate near-term external account forecasts, with oil exporters continuing to benefit from high oil and gas prices and increased money inflows and tourism receipts to some EM&MIs offsetting external headwinds. In turn, countries benefitting from the positive terms-of-trade shock (Azerbaijan, Kazakhstan) and unanticipated positive spillovers from the war in Ukraine (Armenia, Azerbaijan, Georgia, Uzbekistan) are expected to see improved fiscal performances over 2022–23.

**ME&CA is facing exceptional uncertainties and downside risks.**

- **Persistently high commodity prices and more pervasive food shortages could lead to food insecurity, social unrest, and fiscal pressures.** Rising fertilizer costs amid low strategic reserves could present risks to the 2023 agricultural harvest, reducing food security. Together with employment gaps, potential declines in remittances, and limited policy space, high commodity prices could worsen poverty and lead to social unrest.

- **Tighter-than-expected financial conditions could trigger debt and financial stability risks.** This could translate into higher government debt service costs and worsening debt dynamics, further complicating market access and raising the risk of a funding crunch for EM&MIs.

- **Broadening inflation.** Risks to the inflation outlook could become unusually large amid large external cost-push shocks, tightening global financial conditions leading to exchange rate pressures, and weak anchoring of inflation expectations.

- **Disinflationary policies could be more costly than expected.** Globally, this could trigger a severe slowdown in economic activity, further worsening external conditions for the region. Domestically, high dollarization, shallow financial markets, and underdeveloped monetary policy frameworks could require large increases in policy rates to make a dent in inflation, risking tipping economies into recession.

- **Spillovers from the war could put the CCA’s progress toward reducing poverty and inequality at risk.** Poorer households are most at risk from rising food prices and a potential decline in
remittances from Russia. The war risks raising poverty by about 1 percentage point and inequality by about 1 percent and reducing real household consumption by about 2 percentage points, on average, with larger impacts in poorer countries.

Upside risks include a larger-than-expected moderation in food commodity prices, supported by the resumption of Ukrainian grain exports, and, for oil importers, a greater-than-expected decline in oil prices.

**Mitigating a cost-of-living crisis while preserving fiscal sustainability is the most pressing policy priority.** This entails:

- **Restoring price stability** by tightening monetary policy in countries where inflation is becoming broad-based or where there are signs of de-anchoring of inflation expectations.

- **Tackling food insecurity**, including by decisive global efforts to lift trade restrictions and reduce excess storage reserves, while improving access to fertilizers and investing in climate-resilient agriculture.

- **Protecting the vulnerable while ensuring fiscal sustainability.** Targeted support should be deployed, where available; temporary food subsidies can be used when targeted assistance is not feasible and food insecurity looms large. However, countries should avoid regressive energy subsidies, tax cuts, and tax exemptions. Accelerating fiscal adjustment in countries where fiscal space is limited will be critical to maintaining debt sustainability. Oil exporters should maximize the benefits of the oil windfall by building buffers and avoiding procyclical spending, keeping fiscal reform momentum, and progressing with their diversification plans.

**In parallel, countries should move on a variety of fronts to strengthen resilience and growth prospects.**

- **Building resilience to future shocks.** Completing energy subsidy reforms in conjunction with enhancing social safety nets will be key to free up resources for expanding the reach of social protection and investing in energy efficiency. Strengthening medium-term fiscal frameworks is critical to anchor confidence in fiscal sustainability.

- **Pressing ahead with structural reforms for inclusive and resilient growth.** Accelerating structural reforms has become even more urgent to mitigate any potential adverse effects on growth and bolster productivity. Priorities include removing barriers to private firms, enacting reforms that reduce informality and improve tax equity, and investing in climate-resilient technology and infrastructure.

**IMF support remains steadfast.** The IMF has supported ME&CA members with $21.3 billion in financing since 2020 and allocated $49.3 billion special drawing rights to boost the region’s reserve assets. The IMF is also adapting its toolkit to address members’ emerging needs by establishing the Resilience and Sustainability Trust, which will support low-income and vulnerable middle-income countries build resilience to external shocks and address longer-term challenges, including climate change. To help address the food crisis facing our most vulnerable members, the IMF has enhanced its emergency financing facilities by establishing a new “food shock window”.