INTERNATIONAL MONETARY FUND

IMF Country Report No. 18/21

KUWAIT

January 2018

2017 ARTICLE IV CONSULTATION—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR KUWAIT

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 2017 Article IV consultation with Kuwait, the following documents have been released and are included in this package:

- A **Press Release** summarizing the views of the Executive Board as expressed during its January 12, 2018 consideration of the staff report that concluded the Article IV consultation with Kuwait.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on January 12, 2018 following discussions that ended on November 13, 2017, 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 December 22, 2017.
- An **Informational Annex** prepared by the IMF staff.
- A **Statement by the Executive Director** for Kuwait.

The document listed below will be separately released.

Selected Issues

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

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INTERNATIONAL MONETARY FUND
COMMUNICATIONS DEPARTMENT

Press Release No. 18/26
FOR IMMEDIATE RELEASE
January 24, 2018

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

IMF Executive Board Concludes 2017 Article IV Consultation with Kuwait

On January 12, 2018, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with Kuwait.[1]

Non-oil growth has picked up modestly over the past two years, and inflation has moderated. After coming to a standstill in 2015, real non-hydrocarbon growth has recovered and is set to reach 2.5 percent this year, driven by improved confidence. However, a cut in hydrocarbon output by close to 6 percent, reflecting implementation of the OPEC+ deal, will bring overall real GDP down by about 2.5 percent in 2017. Notwithstanding the impact of higher energy and water prices, inflation is on track to reach a multiyear low of 1.75 percent in 2017, due to a decline in housing rents and favorable food price developments.

The government's underlying fiscal position has improved on the back of spending restraint, but financing needs have remained large. While overall fiscal accounts remained broadly balanced in 2016/17, the fiscal balance which excludes mandatory transfers to the Future Generations Fund (FGF) and investment income posted a large deficit (17.5 percent of GDP) for a second year in a row. The corresponding financing needs were covered through a drawdown in readily available General Reserve Fund (GRF) assets, domestic borrowing at various maturities, and a successful debut international sovereign bond sale. The external current account recorded its first deficit in many years in 2016.

The banking sector has remained sound, and deposit and credit growth have slowed somewhat. As of Q2 2017, banks featured high capitalization (CAR of 18.3 percent), steady profitability (ROA of 1.1 percent), low non-performing loans (ratio of 2.4 percent), and high loan-loss provisioning (over 200 percent coverage). Moreover, banks have maintained strong liquidity buffers. Private sector deposit growth has declined in recent years, but this has partly been offset by an increase in public sector deposits. While the growth of credit to the private sector has also slowed mildly on a year-on-year basis since July 2016, the underlying trend (i.e. after adjusting for a large one-off loan repayment) has remained above 5.5 percent.

[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 Assessment[2]

Executive Directors concurred that Kuwait is facing "lower-for-longer" oil prices from a position of strength given large financial buffers, low debt, and sound financial sector. Directors noted that non-oil growth is expected to continue to recover gradually over the medium term, with the fiscal and external positions remaining broadly balanced. While acknowledging short-term upside risks from the recent recovery in oil prices, they saw a further drop in oil prices over the medium term, tighter global financial conditions, heightened regional security and geopolitical risks, and delays in project and reform implementation as the main risks to the outlook.

Directors noted that the sharp decline in oil prices had adversely affected fiscal and current account balances. They commended the government's recent efforts to streamline current spending, diversify revenue, and improve the business climate, and stressed that the new environment calls for deep and sustained reforms.

Directors encouraged the authorities to proceed with the planned introduction of excises and the VAT and to further curtail current expenditure. Highlighting the need for deeper reforms to reduce financing requirements more rapidly, create space for growth-enhancing capital outlays, and achieve intergenerational equity, they recommended further steps to contain the wage bill. They stressed that better aligning public and private sector compensation would enhance nationals' incentive to consider private sector jobs and support competitiveness, and recommended limiting public sector employment growth as more private sector jobs are created. They saw reducing the large subsidy and transfer bills while protecting the most vulnerable as important.

Directors commended the introduction of medium-term expenditure ceilings and encouraged the authorities to further strengthen the medium-term fiscal framework to help underpin consolidation. They welcomed the government's balanced financing approach and noted that further strengthening of the related institutional and legal frameworks would make debt management more effective and support the development of capital markets.

Directors welcomed the banking system's sound position and the authorities' prudent regulation and supervision. Given the downside risks to asset quality, high loan concentrations, common exposures, and interconnectedness of the financial sector, they welcomed ongoing initiatives to identify and address emerging pressures. To further enhance financial sector resilience, Directors saw scope to strengthen the crisis management and preparedness and the liquidity forecasting frameworks.

Directors stressed that moving from a public sector-led growth model to one driven by the private sector requires creating incentives for risk-taking and entrepreneurship. They emphasized the importance of education reform to equip new graduates with the relevant skills for private sector jobs and saw merit in greater use of privatization and partnerships with the

[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.

private sector to boost productivity, investment and job creation. They agreed that this should be complemented by further steps to improve the business environment, including reforms to facilitate access to land, reduce the burden of administrative procedures and excessive regulations, and foster competition. Given their potential for job creation, they welcomed the authorities' focus on SMEs.

Directors concurred that the peg to a basket remains appropriate for the Kuwaiti economy, as it continues to provide an effective nominal anchor. They noted that the recommended fiscal adjustment would largely close the moderate current account gap over the medium term.

Kuwait. Selected Economic Indicators 2013–22

				Est.	Proj.					
	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Oil and gas sector										
Total oil and gas exports (billions of U.S. dollars)	108.6	97.6	48.5	41.5	45.3	47.4	49.4	51.5	53.8	56.3
Average oil export price (U.S. dollars/barrel)	105.5	96.5	49.0	41.7	49.1	49.0	49.4	50.0	50.8	51.9
Crude oil production (millions of barrels/day)	2.93	2.87	2.86	2.95	2.71	2.83	2.93	3.02	3.10	3.18
	(Annual percentage change, unless otherwise indicated)									
National accounts and prices										
Nominal GDP (market prices, in billions of KD)	49.4	46.3	34.5	33.5	35.9	38.1	40.5	43.1	46.1	49.3
Nominal GDP (market prices, in billions of U.S. $)	174.2	162.7	114.6	110.9	117.3	124.3	132.3	140.9	150.6	160.9
Real GDP [1]	0.4	0.6	-1.0	2.2	-2.5	3.9	3.3	3.2	3.3	3.1
Real oil GDP	-1.8	-2.1	-1.7	2.3	-6.0	4.6	3.5	3.0	2.8	2.5
Real non-oil GDP	4.0	5.0	0.0	2.0	2.5	3.0	3.0	3.5	4.0	4.0
CPI inflation (average)	2.7	3.1	3.7	3.5	1.8	2.5	3.7	3.2	3.0	2.7
Unemployment rate (Kuwaiti nationals)	4.7	5.0	4.7	3.3	...	...	...	...	...	...
	(Percent of GDP at market prices)									
Budgetary operations [2]										
Revenue	73.7	67.4	52.1	52.5	52.5	51.4	50.9	50.1	48.8	47.5
Oil	60.3	51.9	35.3	34.3	35.2	34.6	33.9	33.3	32.6	32.1
Non-oil, *of which:*	13.4	15.4	16.9	18.2	17.4	16.8	17.0	16.9	16.1	15.4
Investment income	8.9	10.6	13.3	14.6	13.7	13.2	12.8	12.3	11.7	11.1
Expenditures [3]	38.3	48.8	52.5	51.7	50.9	49.9	49.7	49.3	48.7	47.1
Expense	34.1	43.3	44.8	44.0	43.2	42.2	41.8	41.3	40.6	39.1
Capital	4.1	5.4	7.6	7.7	7.7	7.8	7.9	8.0	8.1	8.0
Balance	35.4	18.6	-0.3	0.8	1.7	1.5	1.3	0.9	0.1	0.4
Balance (excl. transfer to FGF and inv. income)	20.0	2.4	-17.5	-17.6	-15.9	-15.5	-15.3	-15.3	-15.3	-14.3
Non-oil balance (percent of non-oil GDP) [4]	-91.2	-102.5	-87.7	-80.8	-79.4	-76.9	-74.5	-72.4	-70.7	-67.5
Excluding oil-related subsidies and benefits (percent of non-oil GDP)	-70.7	-81.2	-77.0	-72.0	-71.2	-69.9	-67.8	-65.8	-64.3	-61.3
Total gross debt (calendar year-end) [5]	3.1	3.4	4.7	9.9	19.1	27.0	32.3	36.8	40.5	43.5
	(Percent change; unless otherwise indicated)									
Money and credit										
Net foreign assets [6]	11.4	3.6	-2.1	8.7	-3.4	-0.4	-0.4	0.5	0.7	-0.1
Claims on nongovernment sector	7.2	5.2	7.6	2.9	5.1	7.1	7.9	8.0	8.3	8.1
Kuwaiti dinar 3-month deposit rate (year average; in percent) [7]	0.7	0.8	0.8	1.1	1.7	...	...	...	...	
Stock market unweighted index [7]	27.2	-13.4	-14.1	2.4	25.0	...	...	...	...	
	(Billions of U.S. dollars, unless otherwise indicated)									
External sector										
Exports of goods	115.8	104.5	54.5	46.5	50.7	53.1	55.5	58.0	60.7	63.6
Of which: non-oil exports	7.2	7.0	6.0	5.0	5.4	5.8	6.1	6.5	6.9	7.3
Annual percentage change	6.6	-2.8	-14.1	-15.7	7.0	6.6	6.2	6.1	6.1	6.1
Imports of goods	-25.6	-27.0	-26.5	-26.4	-27.0	-28.0	-28.8	-29.8	-31.0	-32.3
Current account	70.2	54.4	4.0	-5.0	0.1	-0.6	-0.3	0.2	0.1	0.3
Percent of GDP	39.9	33.4	3.5	-4.5	0.1	-0.5	-0.2	0.1	0.1	0.2
International reserve assets [8]	32.2	32.3	28.3	31.2	31.8	32.9	34.5	36.4	38.7	40.6
In months of imports of goods and services	7.5	7.4	6.4	6.8	6.7	6.7	6.7	6.8	6.9	6.9
Memorandum items [7]:										
Exchange rate (U.S. dollar per KD, period average)	3.53	3.52	3.32	3.32	3.31	...	...	...	...	...
Nominal effective exchange rate (Percentage change)	1.0	1.4	3.1	0.9	-0.1	...	...	...	...	...
Real effective exchange rate (Percentage change)	0.8	1.9	4.8	2.9	-0.7	...	...	...	...	...

Break-even oil price (overall balance; U.S. dollar per barrel)	42.5	54.3	47.7	42.5	46.8	47.0	47.7	48.8	50.9	51.5
Break-even oil price (overall balance - after transf. to FGF and excl. inv. income; U.S. dollar per barrel)	79.6	98.0	73.2	68.4	73.8	73.6	74.4	75.7	77.7	78.1
Sovereign rating (S&P)	AA	AA	AA	AA	AA	...	...	...	...	...

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

[1] Calculated on the basis of real oil and non-oil GDP at factor cost. Staff estimates for 2015.
[2] Based on fiscal year cycle, which starts on April 1 and ends on March 31.
[3] Starting in FY 2016/17, there has been a reclassification of expenditure items.
[4] Excludes investment income and pension fund recapitalization.
[5] Excludes debt of Kuwait's SWF related to asset management operations.
[6] Excludes SDRs and IMF reserve position.
[7] For 2017, based on latest available data.
[8] Does not include external assets held by Kuwait Investment Authority.

KUWAIT

STAFF REPORT FOR THE 2017 ARTICLE IV CONSULTATION

December 21, 2017

KEY ISSUES

Context. Kuwait is facing "lower-for-longer" oil prices from a position of strength, owing to large financial buffers, low debt, and a sound financial sector. Nonetheless, lower oil prices have weakened fiscal and external positions and generated large fiscal financing needs. The key challenge for the authorities is to accelerate reforms that underpin fiscal consolidation, while creating incentives for private initiative and investment and fostering job creation for nationals.

Outlook and risks. The fiscal position is projected to remain broadly balanced, but financing needs (after transfers to the future generations fund and excluding investment income) will remain large. If sustained, the recent rebound in oil prices may present upside risks, although these might be partly offset by lower oil output than presently assumed. Downward risks to the outlook include lower oil prices over the medium term, tighter global financial conditions, heightened regional security and geopolitical risks, and delays in project and reform implementation.

Macroeconomic policies. Notwithstanding plans to further curtail current spending and introduce revenue measures, including a value-added tax, more ambitious efforts are needed to bring the fiscal balance closer to levels implied by intergenerational equity considerations, reduce financing needs more rapidly, and create space for growth-enhancing capital outlays. The bulk of the additional effort should be underpinned by reforms tackling spending rigidities (wage bill, subsidies and transfers). Further strengthening the medium-term fiscal framework would help limit implementation risks.

Financial sector. The banking sector is sound, with high capitalization, steady profitability, and good asset quality. The CBK has been proactive in improving supervision and regulation. Enhancing the crisis management and preparedness and the liquidity forecasting frameworks would help further strengthen financial sector resilience.

Private-sector led growth and economic diversification. Addressing labor market inefficiencies, including by better aligning public sector compensation with that in the private sector and improving skills through education reform, accelerating privatization and public-private partnerships, and further improving the business climate are paramount to create private sector jobs for nationals and promote diversification.

Approved By
Aasim M. Husain and Sanjaya Panth

Discussions were held in Kuwait during October 31–November 13, 2017. The staff team comprised Stéphane Roudet (head), Botir Baltabaev, Phil de Imus, Anastasia Guscina, and Vahram Stepanyan (all MCD). Aasim Husain (MCD) and Fouad Al-Kohlany (OED) attended some of the meetings. The team met with Minister of Finance Al-Saleh, Governor of the Central Bank of Kuwait Al-Hashel, Minister of Social Affairs and Labor and Minister of State for Planning and Development Al-Subaih, Minister of Education and Minister of Higher Education Al-Fares, other senior officials, parliamentarians, and private sector representatives. Research assistance was provided by Tucker Stone. The team also benefited from editorial support by Diana Kargbo-Sical.

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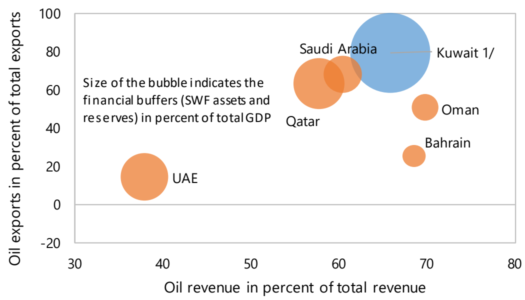
CONTEXT

1. **Kuwait is facing "lower-for-longer" oil prices from a position of strength.** Given the country's high oil-dependency, the 2014 oil price shock led to a sharp deterioration in fiscal and external balances. Nonetheless, large financial buffers—which staff estimates have reached about 470 percent of GDP—and low debt have provided ample space to smooth fiscal consolidation. While an initial drop in confidence slowed down activity in the non-oil sectors, there have been signs of recovery. Resilient non-oil activity and strong financial sector oversight have in turn kept the banking system sound.

Dependence on Oil: Kuwait and GCC
(2016)



Source: Sovereign Wealth Fund Institute; and IMF staff calculations.
1/ For Kuwait, the size of the bubble includes KIA (470 percent of GDP) and CBK (28 percent of GDP) assets.

Selected Financial Soundness Indicators
(Latest available)

	Capital Adequacy Ratio	Gross NPLs to total loans	Return on Assets
Kuwait	18.3	2.4	1.1
GCC (excluding KWT)	18.0	2.9	1.5
Emerging Markets	18.9	7.0	1.8
Advanced Economies	18.5	6.6	0.7

Sources: Country authorities; Haver; and IMF staff calculations

2. **The government has launched a comprehensive reform strategy aimed at reducing dependence on hydrocarbons and boosting growth and job creation for nationals** (Box 1 in Country Report No. 17/15). This was followed by significant fuel, electricity, and water price increases and other steps to raise government saving and improve the business environment (Annex I).

3. **The main challenge for the authorities is to formulate a sequence and pace of reforms that generate concrete results under a reasonable timeframe while maintaining consensus in favor of economic transformation.** The government resigned at end-October 2017, amid tensions with the parliament. The Prime Minister has been reappointed to form a new cabinet, and the new government has reaffirmed its commitment to the reform strategy.

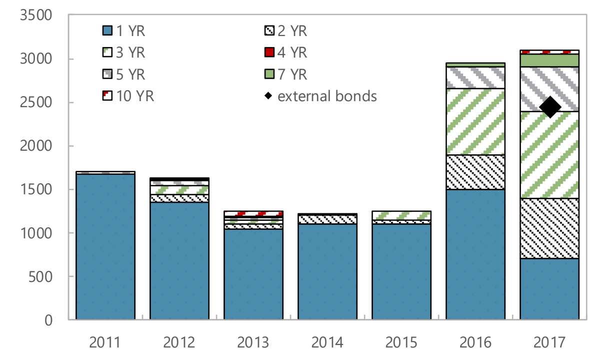
RECENT MACRO-FINANCIAL DEVELOPMENTS

4. **Non-oil growth has picked up modestly over the past two years, and inflation has moderated.** After coming to a standstill in 2015, real non-hydrocarbon growth has recovered and is set to reach 2½ percent this year, driven by improved confidence. However, a cut in hydrocarbon output by close to 6 percent, reflecting implementation of the OPEC+ deal, will bring overall real GDP down by about 2½ percent in 2017. Notwithstanding the impact of higher energy and water prices, inflation is on track to reach a multiyear low of 1¾ percent in 2017, due to a decline in housing rents and favorable food price developments.

5. The government's underlying fiscal position has improved on the back of spending restraint, but financing needs have remained large. Further efforts to curtail current expenditure, combined with the impact of lower oil prices on energy subsidies (some KD 2 billion), reduced current spending by about KD 3¼ billion over the past two years. While overall fiscal accounts remained broadly balanced in 2016/17, the fiscal balance which excludes mandatory transfers to the Future Generations Fund (FGF) and investment income posted a large deficit (17½ percent of GDP) for a second year in a row. The corresponding financing needs were covered through a drawdown in readily available General Reserve Fund (GRF) assets, domestic borrowing at various maturities, and a successful debut international sovereign bond sale.[1]

Domestic and External Bond Issuance, 2011–17

(KD million, maturity at issuance)



Sources: CBK and MOF.

Fiscal Developments, 2014–17

	2014/15	2015/16	2016/17	2014/15	2015/16	2016/17
	Percent of GDP			Percent of Non-oil GDP		
Revenue	67.4	52.1	52.5	166.9	93.6	88.3
Oil	51.9	35.3	34.3	128.7	63.3	57.6
Non-oil	15.4	16.9	18.2	38.3	30.3	30.7
Expenditure 1/	48.8	52.5	51.7	120.8	94.2	86.9
Current	43.3	44.8	44.0	107.4	80.5	73.9
Capital	5.4	7.6	7.7	13.5	13.7	13.0
Overall balance 2/	18.6	-0.3	0.8	46.1	-0.6	1.4
Excluding oil, investment income, recapitalization of pension	-41.4	-48.9	-48.0	-102.5	-87.7	-80.8
Excluding subsidy	-32.8	-42.9	-42.8	-81.2	-77.0	-72.0
Overall balance (after transfers to FGF and excl. investment income) 3/	2.4	-17.5	-17.6	5.8	-31.4	-29.5
Memo items:						
Nominal GDP (KD billion)	46.3	34.5	33.5			
Nominal Non-oil GDP (KD billions)	17.5	19.1	20.3			
Break-even oil price (overall balance; U. S. dollar per barrel)	54.3	47.7	42.5			
Break-even oil price (overall balance - after transfers to FGF and excl. investment income; U. S. dollar per barrel)	98.0	73.2	68.4			
Stock of GRF assets 4/	118.3	144.0	137.1			
Stock of FGF assets 4/	227.3	316.0	333.1			

Sources: Country authorities; and IMF staff estimates.

1/ Starting in FY 2016/17, there has been a reclassification of expenditure items.
2/ The sharp decline in the non-oil balance as a share of non-oil GDP in 2015/16 reflected mainly the non-recurrence of one-off transfers (large increase in foreign aid and recapitalization of the pension fund) in 2014/15, a reduction in the subsidy bill, and cuts in non-essential spending. The decline in non-oil revenue in relation to non-oil GDP reflects a lower return on foreign assets than nominal non-oil GDP growth.
3/ Excludes 10 percent of total revenue transferred to the Future Generation Fund (3.8 percent of GDP in 2016/17) and investment income (14.6 percent of GDP in 2016/17).
4/ Estimated by staff.

[1] In March 2017, the government issued USD 3.5 billion of a 5-year bond at a yield of about 2.9 percent and USD 4.5 billion of a 10-year bond at a yield of about 3.6 percent.

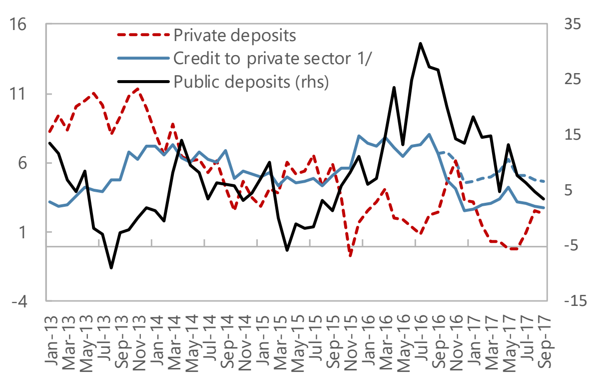
6. The external current account recorded its first deficit in many years in 2016 (of about 4½ percent of GDP). This was largely driven by the further decline in oil prices. As oil prices recover this year, the current account is expected to be broadly balanced.

7. The banking sector has remained sound. As of Q2 2017, banks featured high capitalization (CAR of 18.3 percent), steady profitability (ROA of 1.1 percent), low non-performing loans (ratio of 2.4 percent), and high loan-loss provisioning (over 200 percent coverage). Moreover, banks have maintained strong liquidity buffers. Their deposits at the CBK have declined since 2015, as their holdings of Treasury bonds have increased.

8. Deposit and credit growth have somewhat slowed. Private sector deposit growth has declined in recent years, but this has partly been offset by an increase in public sector deposits, and some banks have also raised funding in international markets. While the growth of credit to the private sector has also slowed mildly on a year-on-year basis since July 2016, the underlying trend (i.e. after adjusting for a large one-off loan repayment) has remained above 5½ percent. Over the past couple of years, the Central Bank of Kuwait (CBK) has raised its policy rate in tandem with the U.S Federal Reserve—except after the June 2017 Federal Open Market Committee (FOMC) meeting, when it adjusted the rates on its market operations instead of the discount rate, and after the December 2017 Federal Reserve rate hike. This has pushed interbank market rates up. Bank lending rates have risen to a lesser extent.

Bank Deposits and Credit

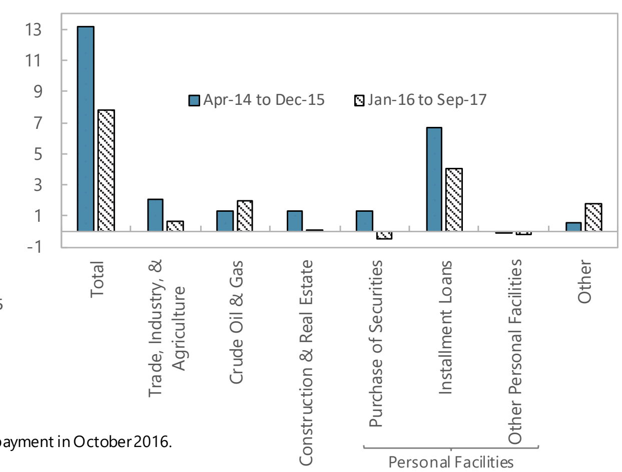
(y-o-y percent change)



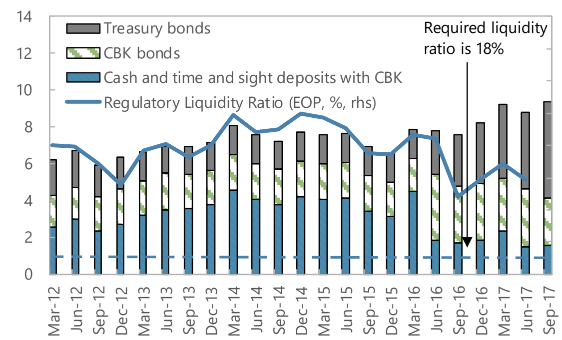
Sources: Country authorities; Haver; and IMF staff calculations.
1/ Dotted line represents credit to private sector, adjusted for a large one-off repayment in October 2016.

Bank Deposits and Credit

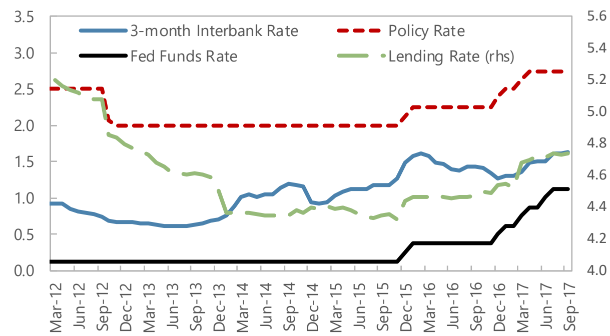
(y-o-y percent change)



Bank Liquidity, Reserves, and Holdings of Securities
(In KD billions unless otherwise noted)



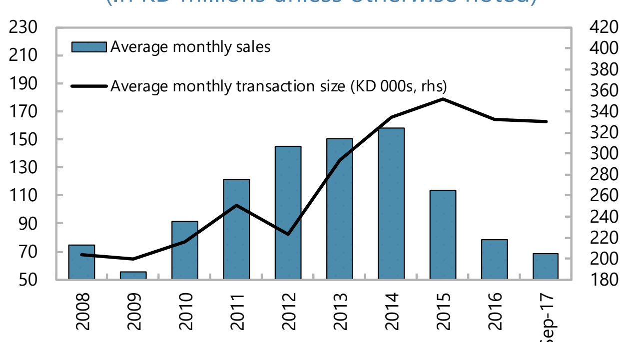
Interest Rates
(Percent)



Sources: Central Bank of Kuwait; Haver; and IMF staff calculations.

9. The sectors which banks are highly exposed to have had mixed performance. Real estate has experienced a significant slowdown over the past few years, leading to a small uptick in the sector's nonperforming loans.[2] Real estate credit growth has, however, been driven mainly by installment loans, which are secured by salary assignment, and present a lower risk profile. Equity markets have staged a recovery since early 2016, but have remained very volatile. Banks' exposure to Investment Companies (ICs) has been reduced to some 2½ percent of total loans.

Real Estate Statistics, 2008–Sep. 2017
(In KD millions unless otherwise noted)



Equity Prices, 2012–Nov. 2017
(Index; May 12, 2012=100)

Source: National Bank of Kuwait; Haver; and IMF staff calculations.
Note: Calculated by combining monthly average prices (per sqm when possible) in select, more active, areas of Kuwait; it is then adjusted for volatility. The indexes are based in 2012, i.e. 2012 price index equals 100. The index is not adjusted for seasonality nor the number of business days.

[2] Close to one fifth of banks' lending is to the real estate sector. About 65 percent of banks' collateral and one percent of banks' investment portfolio consists of real estate.

OUTLOOK, RISKS, AND SPILLOVERS

10. Medium-term macro-financial prospects are broadly favorable, although financing needs will likely remain large.

- *Overall real GDP growth is expected to pick up over the medium term.* Driven by accelerated project implementation under the 5-year development plan and improved confidence, non-oil growth is projected to increase gradually to about 4 percent. Hydrocarbon output is forecast to increase by 4½ percent in 2018—as staff's baseline, which is consistent with the October World Economic Outlook assumptions, was established before the recent extension of the OPEC+ agreement—and to expand gradually afterwards in line with investment plans in the sector. Inflation is expected to rise to 2½ next year and to peak at 3¾ percent in 2019, due to the introduction of the new taxes, before stabilizing below 3 percent. The gradual pickup in oil production and prices will keep the current account broadly balanced over the forecast period.
- *The overall fiscal balance is projected to remain nearly balanced.* The mission's baseline scenario assumes oil prices at around \$49 per barrel in 2017–19, increasing to about \$52 per barrel over the medium-term. It also accounts for the introduction of a value-added tax (VAT) and excises on tobacco and sugary drinks, some increases in the price of government services, and full compliance with the new three-year expenditure ceilings. The latter, which were recently approved at the cabinet level, are indicative medium-term caps imposed on the aggregate government spending. They entail annual real expenditure increases of about 1¼ percent a year on average.
- *Gross financing needs will, however, remain large.* After transfers to the FGF and excluding investment income, a fiscal deficit of about 15 percent of GDP annually will generate cumulative financing needs of some US\$ 100 billion over 5 years. The financing needs will continue to be met through a limited amount of domestic borrowing, external borrowing, and drawdown of GRF assets. While this would bring readily available GRF buffers down under the baseline, total KIA assets would continue to increase in nominal terms.

Financing Needs, 2016–22

(In percent of GDP unless otherwise noted)

	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	Cumulative 2017/18-21/22
Overall balance	0.8	1.7	1.5	1.3	0.9	0.1	
Overall balance (after transfer to FGF and excl. inv. income) 1/	-17.6	-15.9	-15.5	-15.3	-15.3	-15.3	
Non-oil balance (% of non-oil GDP)	-80.8	-79.4	-76.9	-74.5	-72.4	-70.7	
Gross financing in KD billion	6.0	5.8	6.0	6.3	6.7	7.2	32.0
Domestic (net issuance)	2.2	1.5	1.0	1.0	1.0	1.0	5.5
External (net issuance)	2.4	2.4	1.8	1.8	1.8	1.8	9.6
Drawdown of GRF	1.4	1.9	3.2	3.5	3.9	4.4	16.9
Public debt 2/	9.9	19.1	27.0	32.3	36.8	40.5	
Stock of the GRF assets 2/ 3/	137.1	126.2	113.8	101.0	88.4	75.4	
Stock of the FGF assets 2/ 3/	333.1	323.3	316.8	309.2	302.0	294.0	
Stock of the KIA assets 2/ 3/	470.2	449.5	430.6	410.2	390.3	369.4	
Current Account balance 2/	-4.5	0.3	-0.3	-0.1	0.2	0.1	

Sources: IMF staff estimates.

1/ Excludes 10 percent of total revenue transferred to the Future Generation Fund and investment income.

2/ It is referring to calendar years.

3/ The stock of assets are staff estimates and projections.

- *This macro-fiscal environment is expected to remain broadly supportive of financial stability and credit growth.* Credit to the private sector is expected to grow broadly in line with non-oil GDP growth, driven by installment loans and project financing. Stepped up project implementation will support bank profitability and internal capital generation.

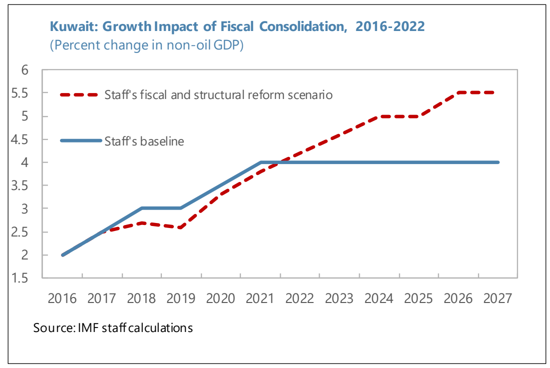
11. Kuwait remains exposed to external and domestic risks (Annex II). Lower oil prices over the medium-term could generate unfavorable macro-financial dynamics, with higher deficits and financing needs making the government susceptible to shifts in market sentiment. Should investors' appetite for GCC international sovereign bonds decline in this environment, the government could be faced with a choice between issuing more domestic debt, at the risk of crowding out private sector credit and slowing growth, or allowing financial buffers to run lower. Heightened security risks in the region and a volatile geopolitical environment could also affect confidence, investment, credit, and growth. Tighter global financial conditions, against the backdrop of U.S. monetary policy normalization, could raise funding costs and risks for both the sovereign and banks. Domestically, the main risks include possible delays in project and reform implementation, which could entail slower growth and larger fiscal deficits. Loss absorption buffers are high and banking sector liquidity is ample, but there are downside risks to asset quality. These could be exacerbated should some of these domestic and external risks materialize, with potential implications for credit to the private sector and growth.

12. Staff highlighted the large potential growth dividends from additional fiscal and structural reforms. While fiscal adjustment may dampen non-oil growth in the short-term, a rebalancing of government outlays towards growth-enhancing investment, more effective government spending, and confidence gains would boost non-oil growth to 4¼ percent by 2022. In the longer-term, structural reforms have the potential to raise Kuwait's non-oil long-term growth to well above 5 percent by boosting investment and raising total factor productivity growth. The mission's illustrative scenario (Box 1) assuming the fiscal adjustment and structural reforms recommended below suggests that, after 10 years, non-oil output would be between 5 to 10 percent higher than under the baseline, resulting in greater economic diversification.

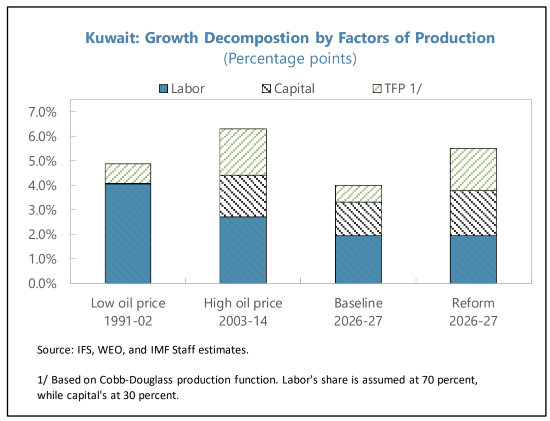
13. The authorities were broadly in agreement with staff's assessment of economic prospects and risks, but saw oil price projections under the baseline as overly conservative. In particular, Ministry of Finance officials were of the view that the recent recovery in oil prices would help bolster fiscal and external positions and reduce financing needs significantly. Staff acknowledged that, if sustained, the recent rebound in oil prices may present upside risks, although these might be partly offset by lower oil output than presently assumed. Indeed, the recent extension of the OPEC+ agreement underscores the uncertainty around the pace oil production may recover. Staff's analysis indicates that, should current oil prices of about $59 per barrel be sustained throughout 2018 and Kuwait's production be maintained at the present level, the fiscal balance (after transfers to the FGF and excluding investment income) and the current account balance would reach -10½ and 5¼ percent of GDP, respectively (compared to -15½ and –¼ percent of GDP, under staff's baseline). The authorities concurred with staff's analysis of the large potential benefits associated with fiscal and structural reforms.

Box 1. Impact of Fiscal and Structural Reforms on Growth

While the additional fiscal consolidation recommended by staff may dampen growth prospects in the short term, the combination of an improvement in the composition and quality of expenditure and the confidence boost from sustained reforms would generate significant growth dividends over time. Based on recent estimates for GCC countries, staff applied medium term multipliers of 0.4, 0.4 and 1.0 for tax revenues, current expenditures and capital expenditures, respectively.[1] On this basis, the fiscal path recommended in this paper would reduce non-oil growth by about ½ percent in the short- to medium-run compared to staff's baseline. However, the gradual rebalancing of expenditure towards higher-multiplier, growth-enhancing capital expenditure, combined with enhancements to the quality of fiscal outlays would help partly offset this impact. At the same time, staff envisages a significant boost to growth due to confidence gains from sustained structural reforms.



In the longer-term, structural reforms could raise potential growth significantly by improving the contributions of capital and total factor productivity. Accelerated reforms to tackle labor market inefficiencies, boost productivity growth through increased reliance on privatization and public-private partnerships, and improve the business climate have the potential to unlock significant additional private sector investment and productivity growth. Staff's reform scenario assumes an increase in the average annual growth of private-sector investment from about 4.7 percent in 2026–27 under the baseline to close to 6.3 under the reform scenario, bringing the contribution of capital to annual growth up by ½ percentage point. Staff also envisages an increase in the contribution of total factor productivity of at least 1 percentage point, an increase somewhat modest in regard to past experience in Kuwait and to the windfalls that EMs typically experience after comprehensive reform programs (some 2 percentage points on average).[2]



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[1] International Monetary Fund, 2016, "More Bang for the Buck in the GCC: Structural Reform Priorities to Power Growth in a Low Oil Price Environment."

[2] International Monetary Fund, 2015, "Structural Reforms and Macroeconomic Performance: Initial Considerations for the Fund."

POLICY DISCUSSIONS

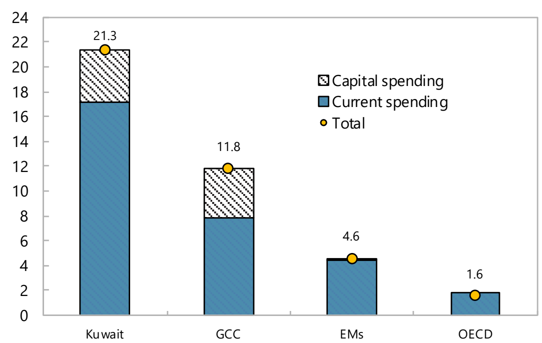
Discussions focused on the appropriate pace and depth of fiscal reforms, steps to bolster financial sector resilience, and reforms to encourage private investment and promote job creation.

A. Preserving Long-term Fiscal Sustainability

14. Staff welcomed the government's planned fiscal reforms and encouraged early steps to limit implementation risks.

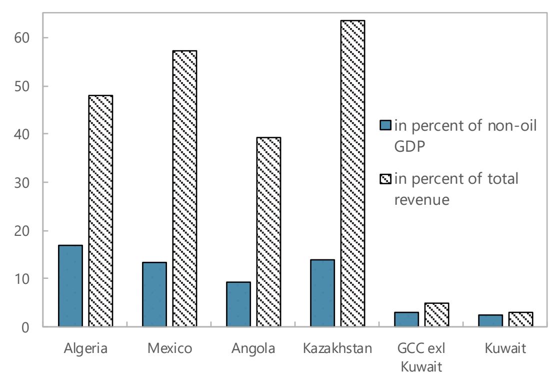
- *Streamlining government spending, while enhancing public financial management.* Given the large increase in government expenditure during the period of high oil prices, there is significant scope for expenditure savings. The authorities have identified a comprehensive menu of possible streamlining options to achieve the newly established expenditure ceilings, including through tightening controls over transfers, reducing inefficiencies in other current and capital spending, controlling wage bill growth, and improving procurement processes. Staff welcomed the progress made in identifying saving areas. There was agreement that efforts to strengthen controls over spending would help limit implementation risks as the ceilings become more binding over time. Reforms to improve the effectiveness of government spending would also facilitate reprioritization of expenditure.

Change in Total Spending, 2004–16
(In percent of GDP)[1]



Sources: IMF FAD Expenditure Assessment Tool (EAT); and World Economic Outlook.
1/ Change in spending is calculated by subtracting the spending to GDP ratio of 2004 from the spending to GDP ratio of 2016.

Tax Revenues, 2016



Sources: OECD; IMF Article IV reports; and IMF staff calculations.

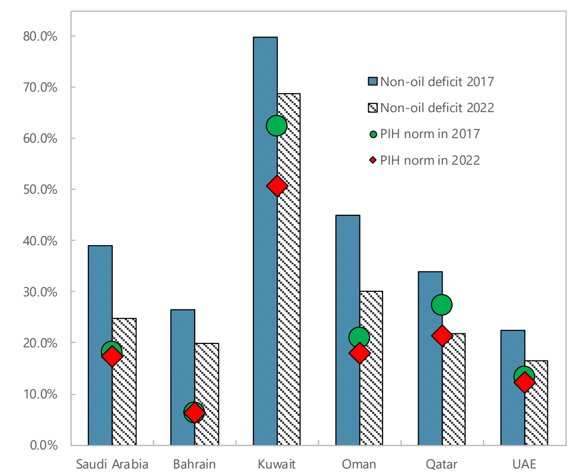
- *Diversifying the revenue base, while strengthening tax administration.* Considering the significant susceptibility of government revenue to oil price fluctuations, staff welcomed the planned introduction of new taxes and repricing of government services to create a larger non-oil revenue base. Given the complexity and scope of the VAT and excise reforms, staff recommended speeding up the preparatory work to avoid implementation delays once the GCC agreement is ratified by parliament. In this context, the authorities may consider IMF technical assistance to help strengthen tax administration capacity and maximize the revenue impact of the measures.

15. **Staff advocated for more ambitious efforts to bring the fiscal balance closer to levels implied by intergenerational equity considerations.** Notwithstanding the impact of the tax reforms and spending restraint assumed under staff's baseline, the government's non-oil balance is projected to fall well short of levels needed to ensure equally high living standards for future generations—by close to 18 percent of non-oil GDP by 2022.[3] Additional fiscal consolidation is

[3] The intergenerational equity level of the non-oil primary fiscal deficit is derived from the permanent income hypothesis (PIH), which estimates a constant real per-capita annuity of the sum of discounted values of future oil revenue receipts and financial assets.

PIH Levels and Non-Oil Deficit

(As a share of non-oil GDP)



Souce: IMF Staff estimates.

therefore needed to close this gap. This would also help reduce financing needs, preserve liquid buffers, and curb the projected buildup in government debt (Annex III). In addition, staff's external sector assessment (Appendix V) suggests a moderate current account gap, most of which would be closed by bringing the fiscal balance to levels consistent with intergenerational equity.

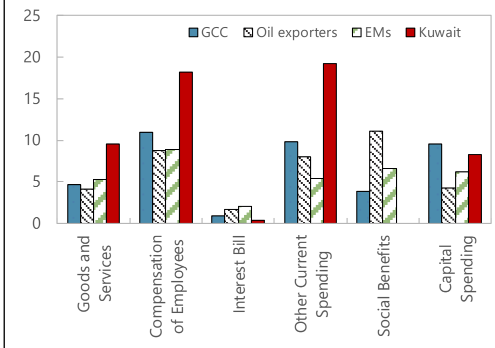
16. **The authorities also saw a need for bringing the government deficit down significantly, but thought this would be partly achieved through higher oil prices.** Staff acknowledged that Kuwait's large fiscal buffers and low starting debt position provide fiscal space to carry out the recommended adjustment at a measured pace to alleviate the potential adverse impact on economic activity and the financial sector. In light of this, staff suggested gradual additional adjustment at a pace that achieves intergenerational equity within ten years. This adjustment path would have modest costs for short-run growth, which would be reversed over time as dividends from higher investment bear fruit (Box 1). The recommended fiscal path would nonetheless entail more rapid consolidation than currently projected under the staff's baseline—reducing the government deficit (after transfer to the FGF and excluding investment income) from a projected 17½ percent of GDP in 2016/17 to about 9 percent by 2022 (Annex IV). Ministry of Finance officials envisaged a more rapid reduction in the government deficit and financing needs. However, this largely reflected a difference in oil price assumptions. They also flagged that the expenditure ceilings had been set based on conservative assumptions regarding the savings from identified reforms, leaving room for possibly faster consolidation.

17. **While other revenue-diversifying measures would help achieve staff's recommended fiscal consolidation objective, the bulk of the additional effort should come from curtailing current expenditure.** Staff supported more ambitious targets for the repricing of government services. While recognizing the authorities' concerns about the potential economic impact of introducing several taxes in a short period, staff also flagged that the business profit tax reform initially envisaged by the government—aimed at broadening the tax base to encompass all enterprises operating in Kuwait—would help enhance non-oil revenue over the medium-term while leveling the playing field. At the same time, the large increase in government spending over the past decade, biased toward rigid current expenditures—particularly the wage bill, energy subsidies and transfers to households and enterprises—calls for addressing these rigidities and reducing waste (Box 2).

Box 2. Expenditure Reforms in Support of Fiscal Consolidation and Growth[1]

Staff's analysis suggests there remains substantial room to streamline current spending. The level of government expenditure in Kuwait is large by international standards. The bulk of it is concentrated on current spending, mostly compensation, subsidies and other transfers. Not only does this entail significant budget rigidities, it also contributes to labor market distortions. For example, relatively high wages and benefits, combined with quasi-guaranteed public employment for Kuwaiti nationals, reduces incentives for nationals to seek private sector jobs or business opportunities, increases reservation wages, and has a negative impact on private sector competitiveness.

Comparison of Spending
(percent of GDP)

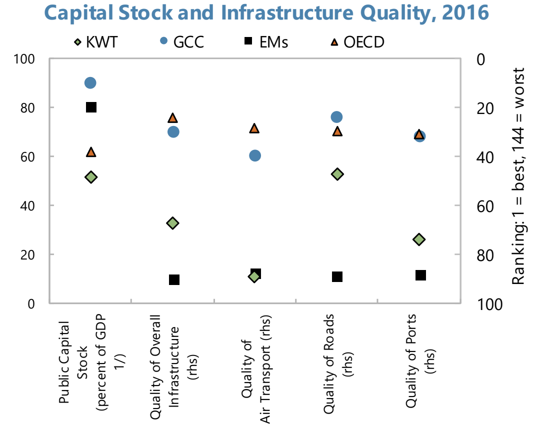


Source: OECD; Country authorities; and IMF staff calculations.

At the same time, capital spending has lagged peers despite public infrastructure gaps. These suggest that there is significant scope to tackle the rigidities in current spending while generating space for higher growth-enhancing expenditure such as public investment.

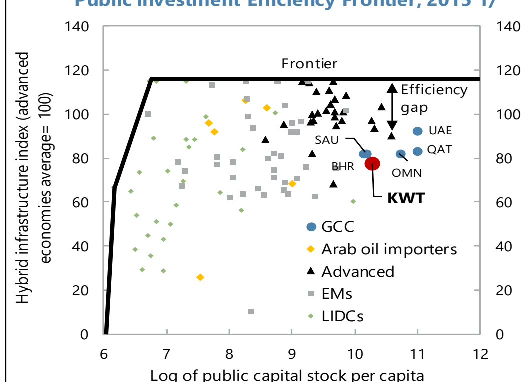
Potential gains from reforms aimed at enhancing spending efficiency, including in areas such as education, health and investment, are also large. Kuwait fares weakly on various measures of spending efficiency. For example, education and health outcomes do not compare well to that of peers once accounting for the amounts spent. Similarly, measures of quality of—and access to—infrastructure do not rank well for a country of this income level. These results suggest large potential gains from reforms aimed at improving public investment management.

Capital Stock and Infrastructure Quality, 2016



Sources: IMF FAD Expenditure Assessment Tool (EAT), IMF Investment and Capital Stock Dataset; and World Economic Forum.

Public Investment Efficiency Frontier, 2015 1/



Source: IMF staff calculations.
1/ The frontier is defined by the countries with the highest infrastructure quality and access (output indicator based on a hybrid index made of physical and survey-based measures) for a given level of public capital stock (input). The greater the distance from the frontier, the less efficient is public investment.
Note: Arab oil importers includes EGY, JOR, LBN, MAR, MRT, and TUN.

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[1] See accompanying Selected Issues Paper "Fiscal Expenditure Reform Options."

Cumulative Fiscal Saving Under the Baseline and Reform Scenarios 1/

(In percent of GDP)

	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23
Baseline reforms						
Fuel price reform	0.2	0.2	0.2	0.2	0.2	0.2
Electricity and water subsidy	0.6	1.1	1.1	1.1	1.1	1.1
VAT and excise		0.0	0.6	1.0	1.0	1.0
Total	**0.8**	**1.3**	**1.8**	**2.2**	**2.2**	**2.2**
Additional reforms under the adjustment scenario						
Fuel price reform 2/		0.1	0.2	0.3	0.4	0.4
Electricity and water subsidy 2/		0.5	1.0	1.4	1.9	2.0
Coprorate Profit tax		0.0	0.0	0.0	0.7	0.6
Wage control		0.4	0.8	1.3	1.7	2.3
Household compensation		-0.1	-0.1	-0.1	-0.1	-0.1
Capital expenditure		-0.1	-0.1	-0.2	-0.3	-0.4
Other 3/		0.2	0.4	0.6	0.8	1.0
Total		**1.1**	**2.1**	**3.3**	**5.0**	**5.8**

Source: Authorities, Kuwait's vision, and IMF staff calculations.

1/ See annex IV for the baseline and adjustment scenario assumptions that were used to derive these estimates.

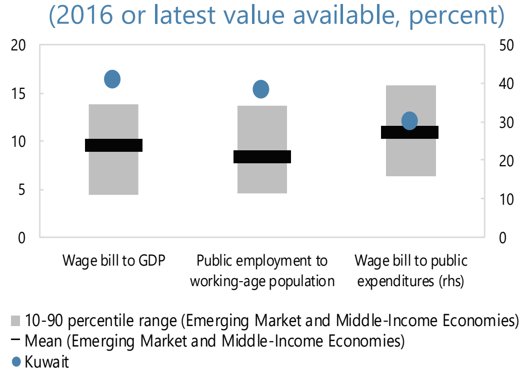
2/ In addition to what is assumed in the baseline.

3/ Other includes (i) lower growth in goods and services and transfers in line with the authorities announced Kuwait's vision and (2) changes in interest payments, investment income and fees, and automatic changes associated with changes in inflation and GDP growth.

18. **Controlling the wage bill is paramount to underpin fiscal adjustment and boost private sector growth and job creation.** Staff encouraged the authorities to implement comprehensive reform aimed at simplifying and harmonizing the public wage grid, fostering merit-based compensation, and realigning public and private sector compensation for equal competencies. This would not only generate savings—as the wage bill has increased significantly over the past decade and is high by international standards—but would also help enhance nationals' incentives to consider private sector opportunities, thereby supporting private sector competitiveness. The authorities also saw scope for tackling wage bill rigidities and thought significant progress could be achieved by rationalizing allowances and benefits. Staff stressed that limiting public sector employment growth—and communicating clearly about the new policy to reset public expectations—should also be part of broader public sector reforms, and agreed with the authorities that this should be accompanied by efforts to boost private sector job and entrepreneurship opportunities for the youth.

Wage Bill and Public Employment

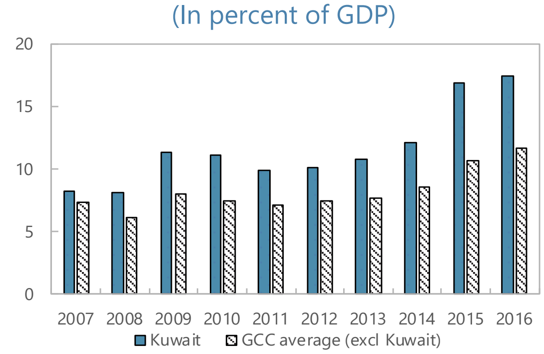
(2016 or latest value available, percent)



Sources: Country authorities; IMF FAD Expenditure Assessment Tool (EAT).

Evolution of Wage Bill

(In percent of GDP)



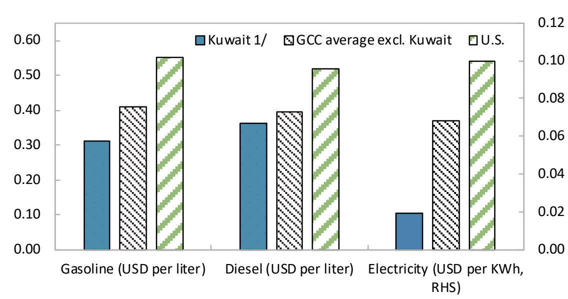
Source: Country authorities; and IMF staff calculations.

19. Reducing subsidies—including for energy products—and transfers is a key potential source of savings and efficiency gains. Important initial steps were taken in recent years to advance energy and utility price reforms and rationalize other subsidies and transfers, including for medical treatment abroad. Nonetheless, the subsidy and total transfer bills remain large (respectively 5.7 and 10.3 percent of GDP in 2016/17). In addition to being costly, subsidies and certain transfers encourage excessive consumption and inefficient allocation of capital. Because they are not targeted, they benefit the wealthiest more than the vulnerable. Given the significant steps taken over the past couple of years to adjust energy prices, the authorities indicated their intention to focus on better controlling eligibility requirements to limit unwarranted transfers going forward rather than making new policy changes. Staff encouraged deeper reforms and highlighted that a well-designed communication strategy, highlighting the cost and distortions generated by current policies as well as possible compensatory measures to protect the most vulnerable from the impact of reforms, would help build consensus for more ambitious reforms.

20. Deeper fiscal reforms would also create more space for growth-enhancing outlays. There was agreement that rebalancing the composition of public spending toward capital spending was important to improve infrastructure, encourage productivity gains, and support long-term growth. This should be complemented by public investment management reforms targeting improved project selection and implementation, including through enhanced coordination among various stakeholders and effective implementation of the anti-corruption framework.

21. Staff commended the authorities' progress toward establishing a medium-term fiscal framework. The ongoing move from incremental annual budgets to medium-term expenditure ceilings will help improve budget planning and underpin medium-term consolidation. To further strengthen the fiscal framework, staff recommended improving top-down processes, including by anchoring the expenditure ceilings to a long-term fiscal policy objective (for example based on intergenerational equity considerations) and setting a consistent path for an intermediary target which would further help delink spending from oil revenue volatility (Box 3). The authorities agreed with staff's views that medium-term budget planning should also consider fiscal risks, including those stemming from the public pension fund's potential actuarial gaps, and foster coordination with institutions involved in the implementation of the development plan.

Price for Energy Products
(Aug 2017 or latest available)



Sources: Prices for GCC countries come from country authorities and are averages for 90 and 95 octane gasoline. U.S. gasoline (average for mid and high grade) and diesel prices come from the U.S. Energy Information Agency (EIA) and are adjusted for taxes. Electricity tariffs for the United States include taxes and come from EIA.
1/ For Kuwait, nationals were exempt from the August 2017 electricty price increases. The overall price is a weighted average of differentiated prices across different sectors.

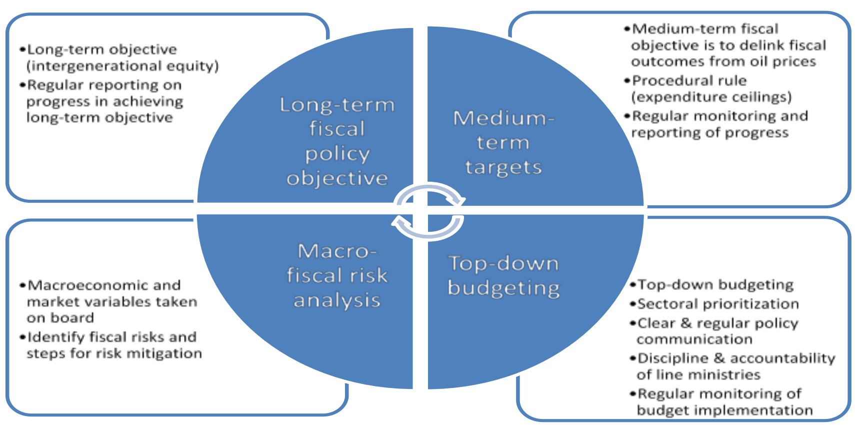
22. Staff supported the authorities' balanced approach to fiscal financing and the ongoing strengthening of related institutional and legal frameworks. To sustain transfers to the FGF while the fiscal position is being adjusted, the authorities' financing strategy consists of limited domestic borrowing to avoid crowding out private sector credit, external bond issuance, and drawdown of GRF liquid assets. This allows the government to preserve adequate buffers against shocks while taking advantage of favorable borrowing conditions and relatively higher returns on FGF assets. Staff welcomed the authorities' efforts to continue strengthening capacity at the debt management unit and to address legal hurdles to maintaining the government's ability to borrow and issuing longer-dated bonds and Sukuk. There was agreement this would encourage broader capital market development. In this context, staff suggested that introducing regular domestic debt auctions that allow for price discovery and developing secondary markets would facilitate issuance of corporate bonds as well as liquidity management. The authorities agreed in principle, highlighting the need to consider the limited competition in the banking system in designing such auctions.

Box 3. Strengthening the Medium-Term Fiscal Framework (MTFF)

An effective MTFF is important to anchor fiscal policy and reduce implementation risks. The high degree of susceptibility of government finance to oil prices in Kuwait has made the conduct of fiscal policy challenging. While the requirement to transfer a minimum of 10 percent of total revenues to the FGF has helped dampen fiscal procyclicality, it has constrained the government's asset-liability management strategy rather than fiscal policy per se, as evidenced by the run up in spending during the oil price boom (2005–14).

The authorities have made progress toward establishing a MTFF. A macro-fiscal unit is in place to help track fiscal performance and analyze macro-fiscal issues. Recently, the government introduced three-year expenditure ceilings to limit the procyclicality of spending and started to put in place a top-down process for budgetary allocations to the line ministries.

Elements of Effective Medium-Term Fiscal Frameworks[1]



[1] See IMF, 2012, "Macroeconomic Policy Frameworks for Resource-Rich Developing Countries," International Monetary Fund, Washington D.C.

Looking ahead, reforms along several dimensions would help further strengthen the MTFF. Adoption of a formal long-term policy objective would better link fiscal policy with the government's strategic vision. A natural objective would be an intergenerational equity benchmark. Introducing a formal intermediary target (e.g. non-oil primary balance) consistent with the long-term objective would help set expenditure ceilings through a reliable top-down process, while further avoiding procyclicality. Considering the impact of reforms and policy decisions at an earlier stage of the budget process and communicating them to line ministries would also help in this respect. Finally, enhanced fiscal reporting (frequency, timeliness, and analysis) would also strengthen accountability and transparency.

23. Staff shared the authorities' assessment that the peg to an undisclosed basket remains appropriate. The exchange rate arrangement has provided an effective nominal anchor for the Kuwait economy (Annex V). The CBK is fully committed to the exchange rate regime and uses its various monetary policy instruments to maintain an adequate short-term interest rate differential with the U.S. Staff noted that over the longer term, as the economy diversifies, the benefits of greater exchange rate flexibility may increase.

B. Safeguarding Financial Stability

24. The banking system is prudently regulated, and the CBK has been proactive in strengthening supervision. Banks are under Basel III regulations for capital, liquidity, and leverage, and are resilient to various stress tests, including credit, liquidity and market shocks.[4] A comprehensive set of macro-prudential measures is being enforced to minimize systemic risks. Staff welcomed the CBK's continuous work to review the scope of its macro-prudential policy and tools, with a view to maintaining a balance between preempting a buildup in risks and stifling credit growth. There was agreement that establishing a financial stability committee including all relevant stakeholders would help in this regard. Given the downside risks to asset quality, high loan concentrations, common exposures, and interconnectedness of the financial sector, staff welcomed ongoing initiatives to identify emerging pressures, including those related to the real estate sector and the impact of U.S. monetary policy normalization. It recommended conducting reverse stress testing as a complementary tool.

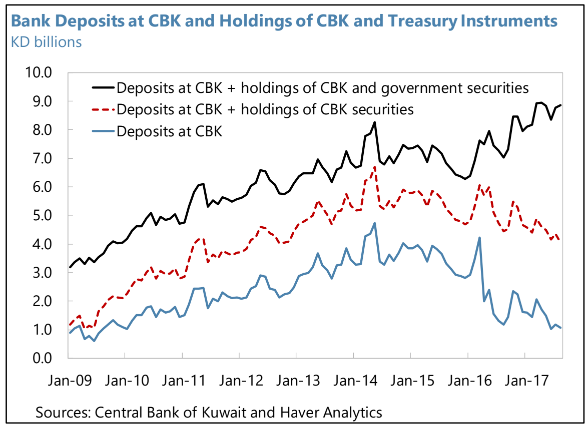
25. Staff and the authorities agreed that the current ample liquidity environment offers a window of opportunity to enhance the liquidity management framework (Box 4). With the Basle III liquidity standards still relatively new, staff concurred with the CBK's prudent policy to maintain its existing five liquidity requirements and encouraged periodic reassessments to maintain an appropriate balance between sound regulation and compliance costs. As far as systemic liquidity management is concerned, enhancing the CBK framework by extending its assessment of liquidity conditions beyond the short-run via liquidity forecasting would facilitate anticipating and planning for potential system-wide pressures. There was agreement that a formal information-providing agreement with relevant entities and better cashflow information would help in this regard.

[4] The CBK's stress tests indicate that banks would maintain a high capital adequacy in the face of severe and protracted credit and market shocks under different scenarios (2016 Financial Stability Report). The results are consistent with staff's analysis (IMF Country Report No. 17/16), which found the banking system resilient, although loan concentrations (particularly in the real estate sector) are a source of vulnerability.

Box 4. Liquidity Conditions and Forecasting Framework [1]

Current liquidity conditions in Kuwait are ample. Local banks maintain liquidity ratios that exceed regulatory requirements (at close to 30 percent, well above the 18 percent requirement). Although central bank domestic currency liabilities vis-à-vis commercial banks in the form of deposits have fallen significantly since early 2016, if CBK bonds and tawarruq are included, bank reserves remain high. Moreover, banks have increased their holdings of Treasury bonds, which can be converted into cash through CBK's repurchase operations. Under prevailing conditions, banks' use of repurchase operations is low and relatively infrequent.

Nonetheless, more volatile oil prices and rising short-term interest rates have increased focus on the central bank's liquidity management framework. The CBK has an adequate set of tools to manage systemic liquidity using central bank securities and standing facilities to guide money market rates to be consistent with monetary policy. Moreover, the stepped-up issuance of Treasury bonds has provided banks with further options to invest their liquid funds.



The CBK should take advantage of this ample liquidity period to further enhance its liquidity management framework. The CBK currently assesses bank liquidity conditions on a short-term basis. However, a liquidity forecasting framework that goes beyond the near-term assessment would improve the planning of central bank operations and concurrently support Treasury debt management operations. Moreover, given the central role of the State in the economy and the liquidity system, strong coordination between State entities and the CBK is paramount for the smooth functioning of the system. While the CBK has established relationships with the Kuwait Investment Authority and the Ministry of Finance, more formal agreements may be needed to ensure the CBK has the necessary data to more accurately forecast liquidity conditions.

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[1] See accompanying Selected Issues Paper "Liquidity Conditions, Regulation, and the Central Bank Liquidity Management Framework".

26. To further bolster financial sector resilience, the CBK has been assessing options to strengthen the crisis management and resolution frameworks. Staff recommended that efforts should focus on enhancing the existing corrective action framework, establishing a special resolution regime for banks, strengthening the emergency liquidity assistance framework, mandating bank recovery planning, and reforming the current blanket guarantee of deposits. Reforms in these areas would promote orderly resolution of banks, promote market discipline, and help safeguard fiscal resources. Formalizing arrangements between key regulators would also help improve crisis preparedness. The authorities noted the legal complexity of formulating meaningful resolution and deposit insurance frameworks and welcomed further engagement with the Fund on these issues.

27. The CBK has continued to take preemptive steps aimed at limiting the risk of withdrawals of correspondent banking relationships (CBRs). Kuwaiti banks have not experienced any withdrawals of CBRs, but several of them have preemptively severed links with a few domestic charities and foreign exchange houses to reduce the perception of risk by global banks. The CBK has been actively participating in international forums aimed at clarifying international standards as well as regulatory expectations in jurisdictions which are home to correspondent banks. It has also maintained open channels of communication between domestic and foreign banks and relevant regulators.

28. The AML/CFT framework is being strengthened. Kuwait's Financial Intelligence Unit (FIU) has recently joined the Egmont Group, an international platform for the secure exchange of expertise and financial intelligence to combat money laundering and terrorism financing (ML/TF). The ongoing ML/TF national risk assessment (NRA), conducted with assistance from the World Bank, is nearing completion. The results will facilitate risk-based AML/CFT efforts and help reallocate resources accordingly, in the context of a revised national strategy that focuses on proceeds of corruption and terrorism financing.

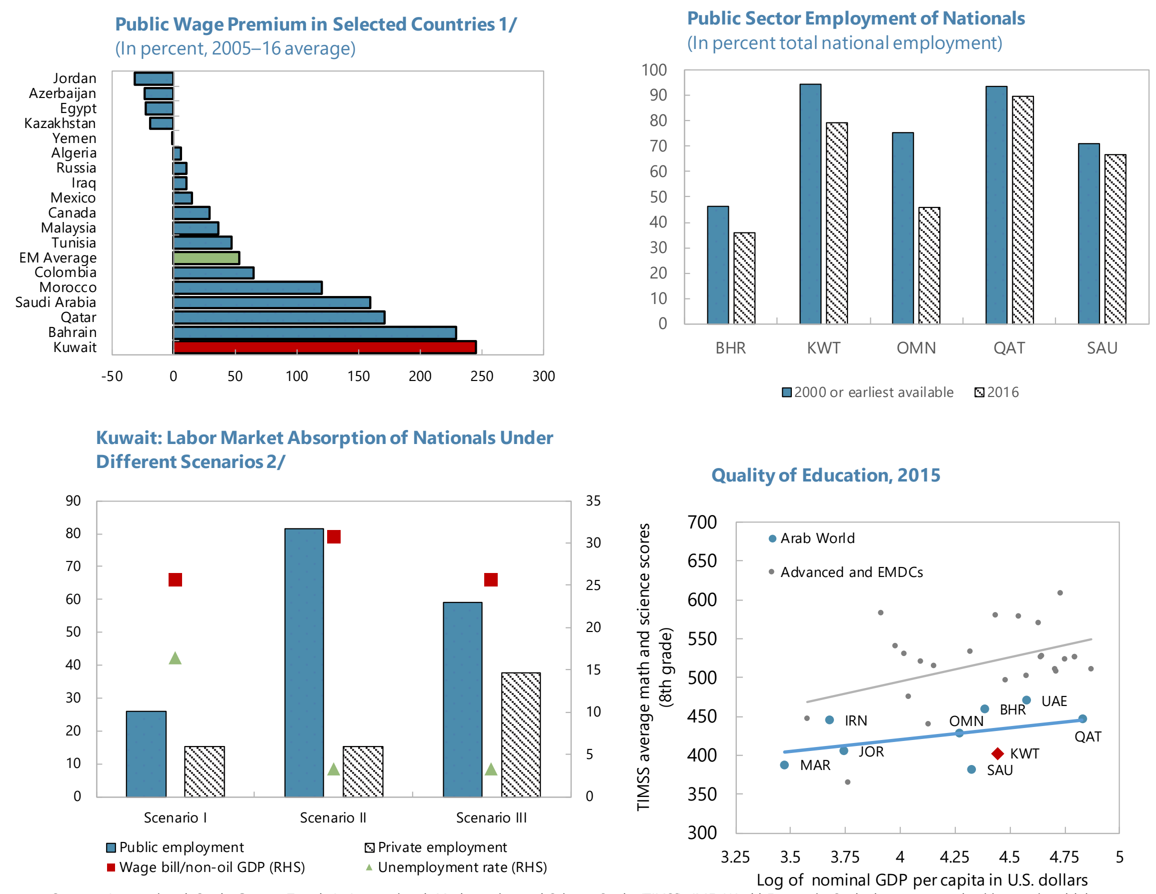
29. Effective implementation of the anti-corruption framework is key. The Anti-Corruption Agency (ACA), which is now fully operational, was recently vindicated by a constitutional court decision which rejected a petition challenging the constitutionality of the ACA framework law establishing financial disclosure principles. Amendments to the ACA law are also being prepared to strengthen the framework, and the ACA is spearheading the development of a national strategy for anti-corruption efforts. The strategy should focus on effective implementation and seek concrete and measurable results. It should also foster synergies between the AML and anti-corruption frameworks, including by encouraging information sharing between the FIU and ACA.

C. Private Sector-led Growth and Economic Diversification

30. The more constrained budgetary environment puts a premium on structural reforms that promote private sector development, diversification, and job creation. Moving from a public sector-led growth model to one driven by the private sector requires creating incentives for risk-taking and entrepreneurship, fostering productivity and competitiveness, and encouraging private initiative and investment.

31. Addressing labor market inefficiencies is paramount. Under current trends, less than 15 percent of new nationals entering the labor market over the next 5 years would be absorbed by the private sector. Given the limited scope for new public sector jobs going forward, labor market and civil service reforms should encourage nationals to create and seek private sector jobs. This requires managing expectations about the limited availability of public sector jobs going forward and better aligning public and private sector wages and benefits. The latter will also help tame reservation wages, supporting private sector competitiveness. Together with the ongoing World Bank-supported education reforms to address skill mismatches, this would also encourage private sector firms to hire nationals. The authorities concurred with staff's views and highlighted the ongoing initiatives to rationalize public sector allowances and benefits as well as ongoing reforms to improve the employability of Kuwaitis in the private sector.

Labor Market Indicators



Sources: International Study Center, *Trends In International Mathematics and Science Study (TIMSS)*; IMF, *World Economic Outlook*; country authorities; national labor surveys, International Labour Organizations; and IMF staff calculations. Data for Morocco from World Bank (2011).

1/ Average public sector wage over average private sector wage, except for Iraq where the numbers represent wage premium estimates obtained after controlling for employee characteristics. The average public and private sector wages for GCC countries are for all employees, including expats. Due to data limitations, these measures fail to control for employee characteristics, such as higher education levels of nationals predominantly working for the public sector, compared to the vast share of expats working in the private sector. On the other hand, the estimated public wages in Kuwait do not include all public sector employee benefits.

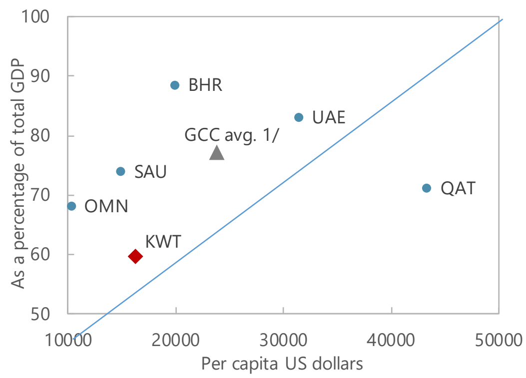
2/ The three scenarios illustrate the absorption of 117 thousand new labor force entrants by 2022. Under Scenario I, public sector absorbs only a small fraction of the new entrants to keep the wage bill lower, but unemployment rate rises; In Scenario II, government absorbs most of the new entrants to keep unemployment low at the expense of higher wage bill; and in Scenario III, government undertakes fiscal and structural reforms to boost higher private sector absorption of new entrants.

32. **Staff welcomed the government's focus on privatization and public and private partnerships**. Given their significant potential in raising productivity and encouraging a greater role for the private sector, staff encouraged the authorities to accelerate the execution of the planned privatizations and PPPs on a transparent and competitive basis. There was agreement that existing processes should be reviewed to identify and tackle hurdles, and that attention should be given to limiting hidden costs and contingent liabilities for the government.

33. **Sustained emphasis on improving the business environment is key.** Staff was encouraged by the progress being made in streamlining registration and licensing—which has led to a marked improvement in the latest World Bank Doing Business ranking—and alleviating restrictions on foreign direct investment. Continued efforts are necessary. Reducing the burden of customs compliance and easing trade barriers would help increase the speed and reduce the cost of

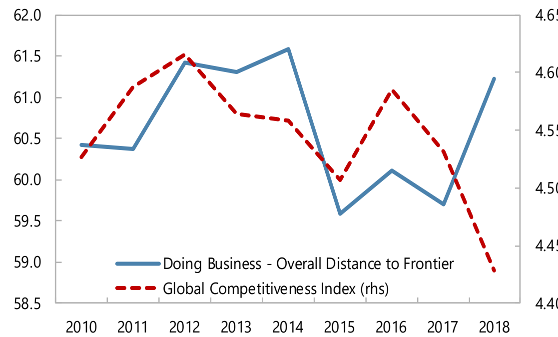
trade between Kuwait and its partners. Private enterprises also flag access to land as an important impediment to investment. The ongoing increased reliance on digitizing would help facilitate administrative procedures, while reducing excessive regulations would foster private sector opportunities, competition, and diversification. The authorities confirmed that addressing these challenges remained important government priorities.

Relative Size of the Non-Oil Economy
(2016)



Source: Country authorities; and IMF staff estimates.
1/ Excluding Kuwait.

Business Climate and Global Competitiveness Indicators
(Larger values indicate improvement)



Sources: World Bank, Doing Business Indicators; World Economic Forum, Global

34. The authorities' focus on SMEs is welcome given their potential for growth and employment generation. The ongoing revamping of the National Fund for SME Development will help in this respect, as it not only seeks to foster access to finance for small businesses, but also aims to train entrepreneurs and encourage better integration of SMEs into supply chains. The SME Fund is collaborating with various stakeholders to provide financial services to these enterprises, helping improve the quality of credit information, and is reviewing various means of financing, including equity participation. Indeed, venture capital and other equity finance could usefully complement bank lending to SMEs, especially for start-ups. In addition, the existing cap on banks' lending spreads may constrain banks' ability to price the higher risks inherent to SMEs.[5] Against this backdrop, staff also suggested focused relaxation of this cap to encourage bank lending to the sector.

D. Statistical Issues

35. Further efforts are being made to improve Kuwait's statistical system. Staff welcomed the recent rebasing of the consumer price index as well as the progress made toward producing quarterly national accounts. It encouraged the authorities to work with IMF staff to continue to improve the quality of annual national accounts.

[5] Banks in Kuwait are subject to a maximum 300 bps spread between their lending rates and the CBK's discount rate.

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36. Kuwait is facing "lower-for-longer" oil prices from a position of strength. The country's large financial buffers and low debt provide policy space to implement the necessary fiscal consolidation gradually. Non-oil growth is expected to continue to recover gradually to about 4 percent over the medium term; the fiscal and external positions are projected to remain broadly balanced, with possible upside risks in the short term if the recent increase in oil prices is sustained. Over the medium term, risks to the outlook stem mainly from a decline in oil prices. Slow project implementation, spillovers from heightened regional security risks, and more volatile global financial conditions could also affect economic prospects.

37. At the same time, the new environment calls for deep and sustained reforms. Lower oil prices have weakened fiscal and external positions and generated large fiscal financing needs. The government's reform strategy is rightly aimed at raising government savings and promoting a greater role for the private sector in generating growth and jobs for nationals. Recent efforts to streamline current spending and diversify revenue, and to improve the business environment are welcome. The key challenge for the authorities is to build consensus to accelerate reforms.

38. Fiscal reforms should focus on addressing underlying current spending rigidities and diversifying revenue. The authorities should proceed with their plans to introduce excises and the VAT, while further curtailing current expenditure. In addition, deeper reforms are necessary to reduce financing needs more rapidly, create space for growth-enhancing capital outlays, and achieve intergenerational equity levels over ten years. Further efforts to curtail the wage bill should be achieved by better aligning public and private sector compensation—which would also enhance nationals' incentive to consider private sector jobs and support competitiveness—and limiting public sector employment growth as more private sector jobs are created. Reducing the large subsidy and transfer bills through well-communicated reforms that protect the most vulnerable is also important. Building on the recent introduction of expenditure ceilings, further strengthening the medium-term fiscal framework by anchoring policies through clearly-specified long- and medium-term fiscal objectives and better accounting for possible fiscal risks would help underpin consolidation.

39. As the fiscal position is being adjusted, the government should maintain its current balanced financing approach. The latter combines drawdown of assets in the GRF, measured amounts of domestic bond issuance and some external borrowing to mitigate potential crowding out of private sector credit while maintaining a high level of liquid buffers. Continued progress toward strengthening related institutional and legal frameworks will make debt management more effective and support the development of capital markets.

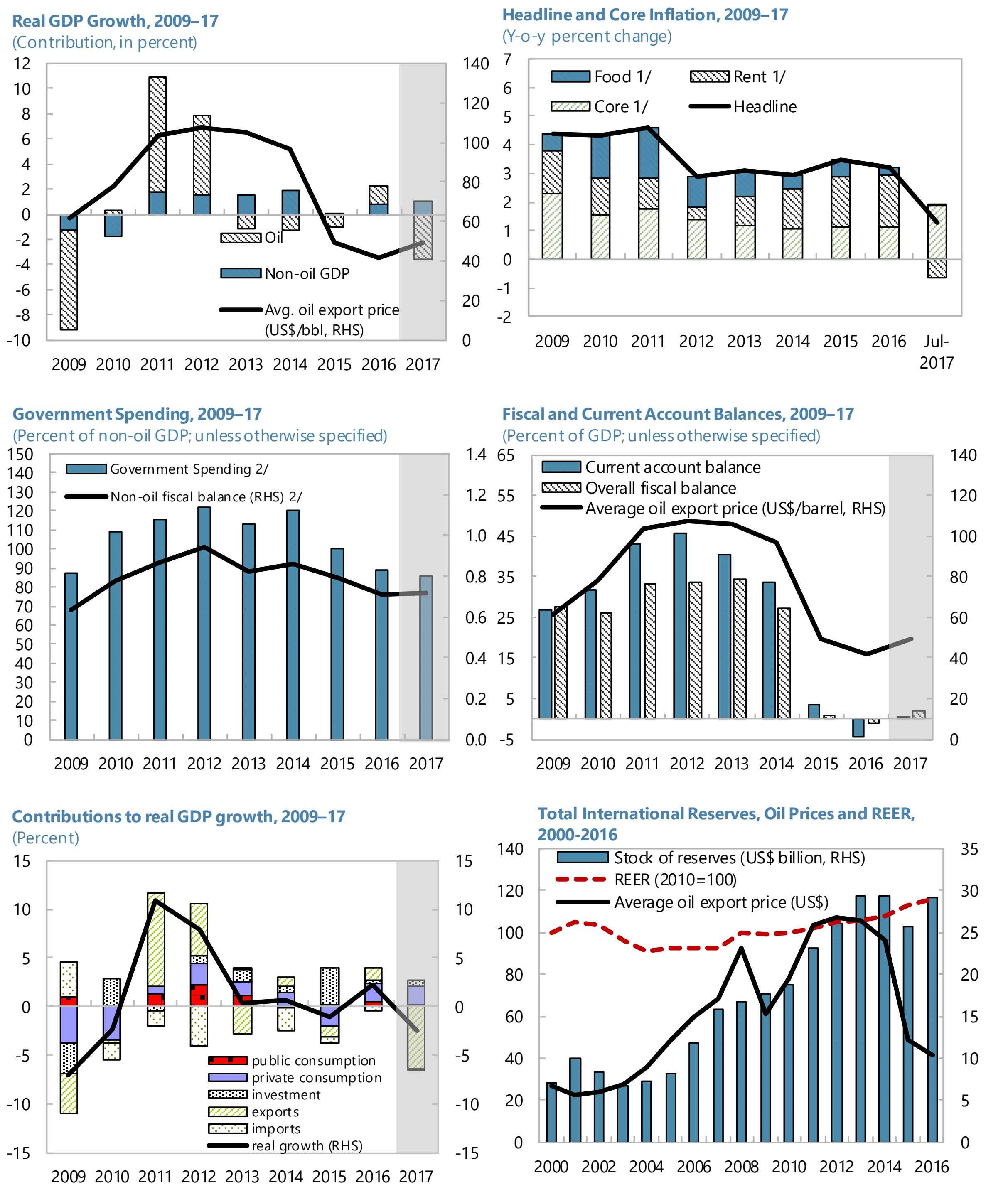
40. Ongoing efforts to strengthen financial sector resilience are welcome. The banking sector is sound, with high capitalization, robust profitability, and good asset quality, buttressed by prudent regulation. Nonetheless, given high loan concentrations, common exposures and interconnectedness, CBK initiatives to identify emerging pressures are commendable. Ample liquidity also provides a good opportunity to strengthen the liquidity forecasting framework to better underpin liquidity management operations. The authorities' plans to enhance the crisis management and preparedness framework, including by introducing a special resolution regime for banks and a deposit insurance mechanism, would also help further strengthen financial sector resilience.

41. The peg to an undisclosed basket of currencies remains appropriate. It has provided an effective nominal anchor. A moderate current account gap can largely be closed by increasing fiscal savings as recommended over the medium term.

42. Structural reforms that promote private sector development, diversification, and job creation are of the essence. Moving from a public sector-led growth model to one driven by the private sector requires creating incentives for risk-taking and entrepreneurship. Education reform is crucial to equip new graduates with the relevant skills for private sector jobs. Greater use of privatization and partnerships with the private sector is also important to boost productivity, private sector investment and job creation. This should be combined with further steps to improve the business environment, including reforms to facilitate access to land, reduce the burden of administrative procedures and excessive regulations, and foster competition. The government's focus on SMEs—by facilitating access to finance and creating a conducive environment from project design to development—is welcome.

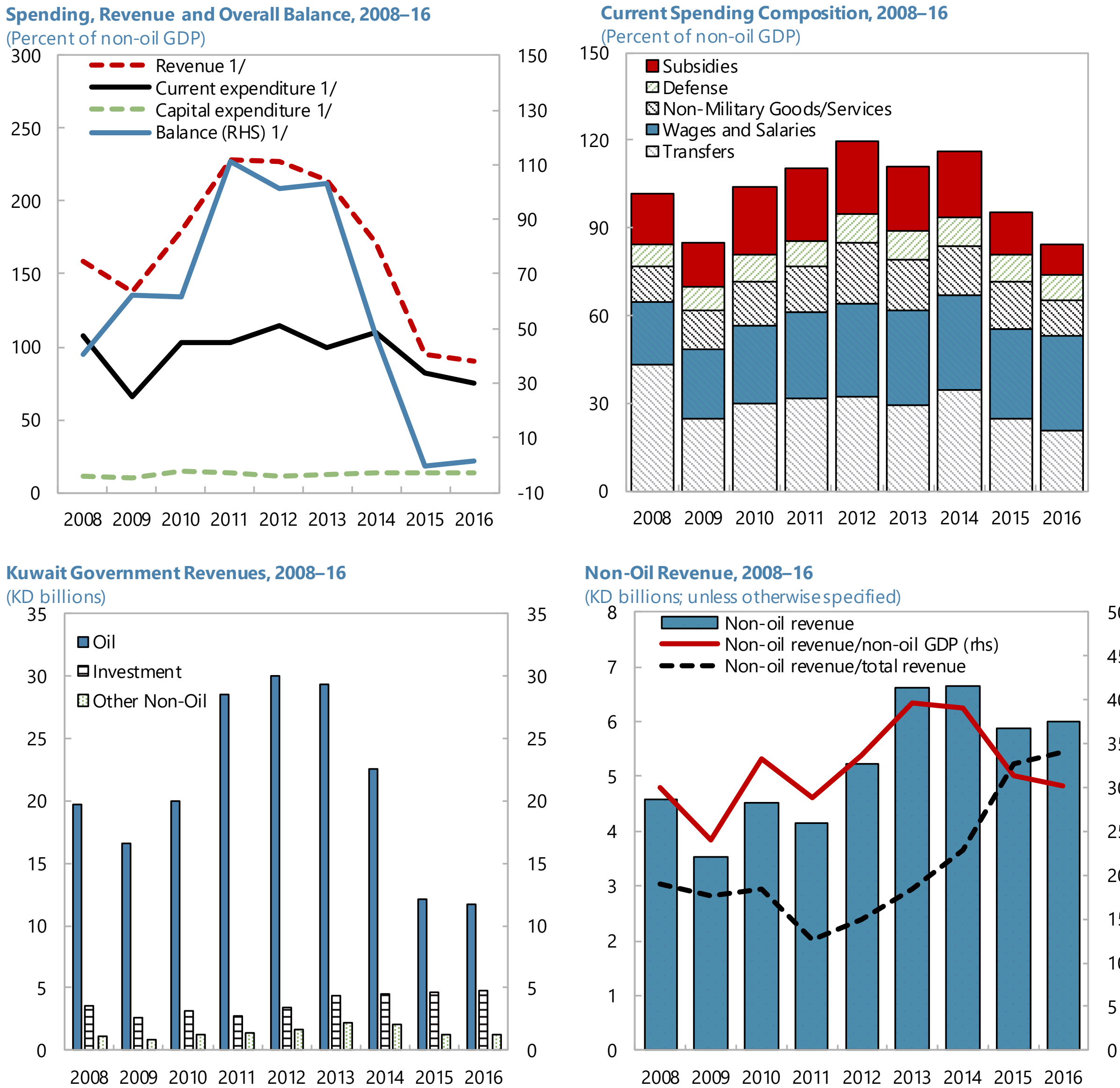
43. Staff recommends that the next Article IV consultation takes place on the standard 12-month cycle.

Figure 1. Recent Macroeconomic Developments



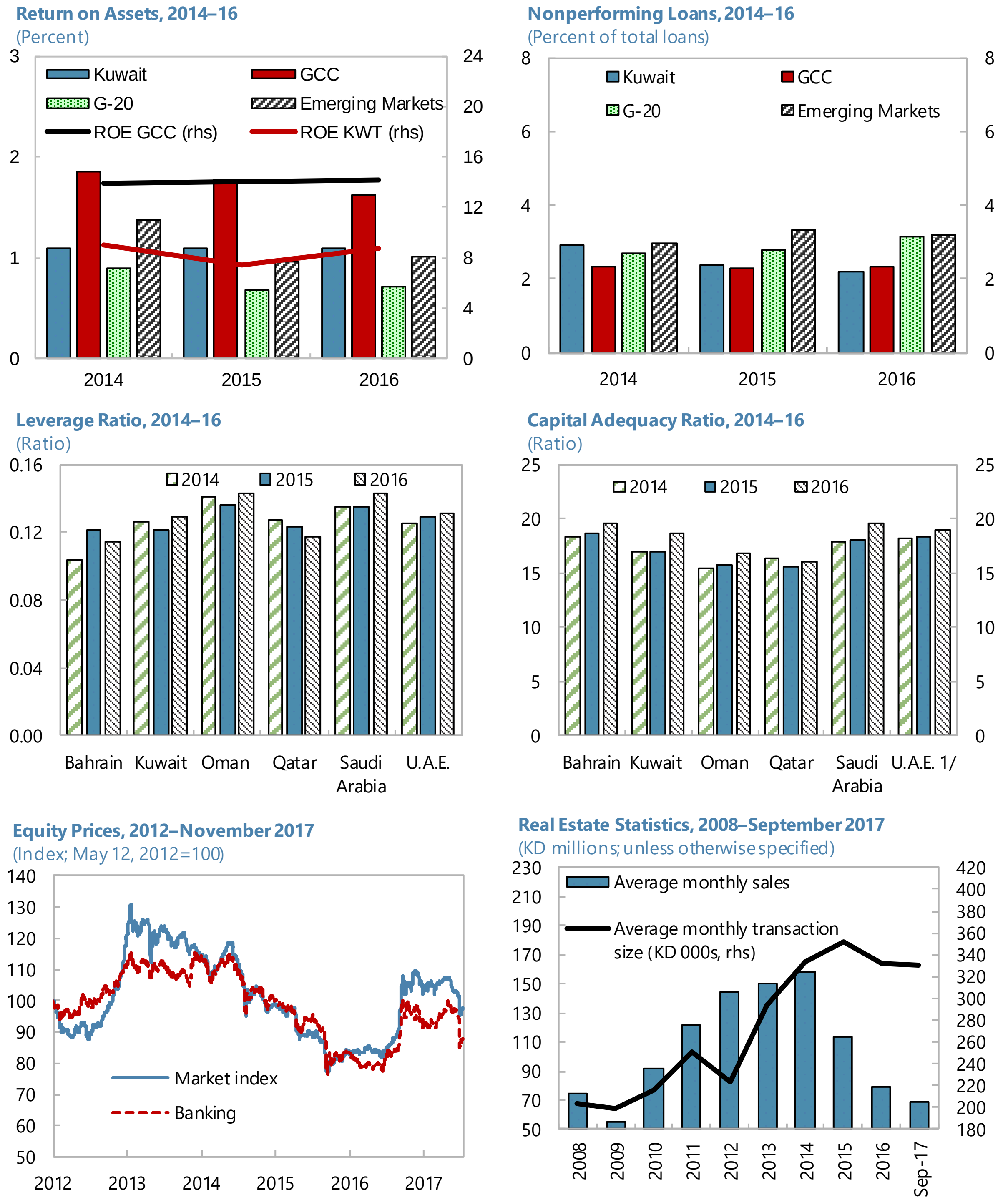
Sources: Country authorities; INS; Haver; and IMF staff calculations.
1/ Contribution to headline CPI inflation.
2/ Using calendar year.

Figure 2. Fiscal Developments



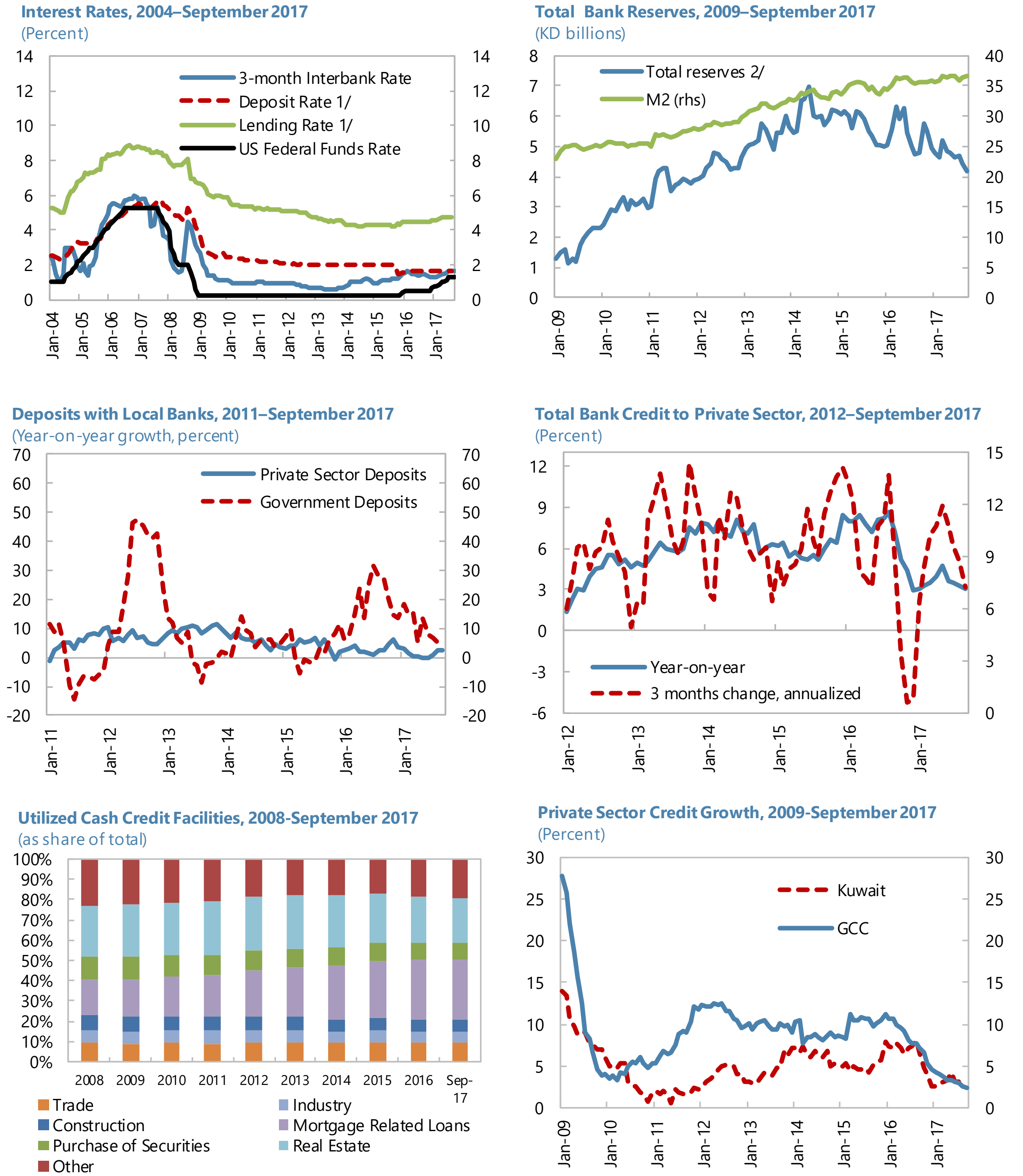
Sources: Country authorities; and IMF staff calculations.
1/ Using calendar year for non-oil GDP, while using fiscal year for revenue, current expenditure, capital expenditure, and the balance.

Figure 3. Financial Developments



Sources: Country authorities; Kuwait Stock Exchange; NBK reports; and IMF staff estimates.
1/ Local banks only.

Figure 4. Monetary Developments



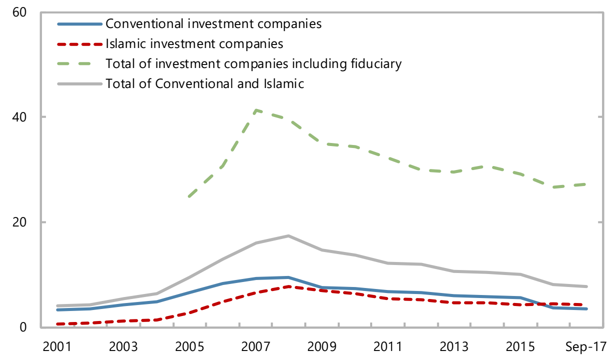
Sources: Country authorities; Haver; and IMF staff calculations.
1/ Weighted average. Data only available up to December 2015.
2/ Bank reserves consist of cash, sight deposits with CBK, time deposits with CBK, and CBK bonds.

Figure 5. Investment Companies Operations

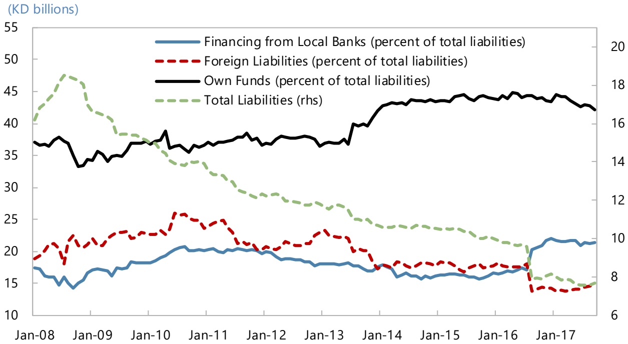
Investment Companies' Operations, 2002–2017
(KD billions)

	2002	2005	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	Sep. 2017
Investment companies													
Conventional													
Number	27	33	40	46	46	46	44	43	42	40	38	34	30
Assets	3.5	6.7	9.4	9.5	7.6	7.3	6.9	6.6	5.9	5.8	5.7	3.8	3.5
Islamic													
Number	11	23	38	53	54	54	51	50	50	49	47	44	39
Assets	0.9	2.8	6.6	7.8	7.0	6.5	5.4	5.2	4.8	4.7	4.3	4.4	4.3
Conventional + Islamic													
Number	38	56	78	99	100	100	95	93	92	89	85	78	69
Assets	4.3	9.4	16.0	17.3	14.6	13.7	12.3	11.9	10.7	10.5	10.0	8.2	7.7
Off-balance sheet													
Assets		15.5	25.4	22.2	20.4	20.6	20.1	18.1	18.9	20.2	19.2	18.5	19.5
Total Assets	4.3	25.0	41.4	39.5	35.0	34.3	32.4	30.0	29.6	30.8	29.2	26.7	27.2
Percent of GDP		105.8	127.0	99.7	114.9	103.7	76.0	61.6	59.9	66.4	85.1	79.7	71.9
Percent of banking assets 1/		115.6	116.4	100.7	86.9	82.9	76.6	64.7	58.9	56.0	49.8	44.2	43.1

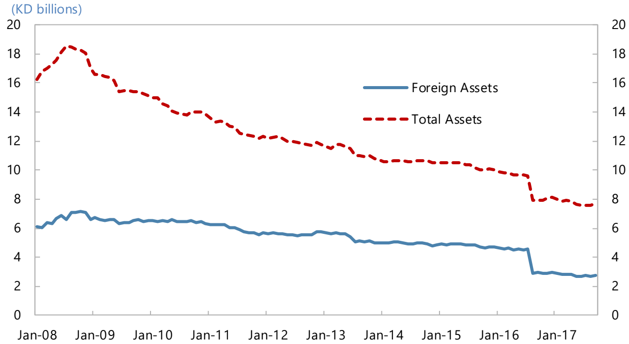
Assets, 2001–September 2017
(KD billions)



Liabilities, 2008–September 2017
(KD billions)

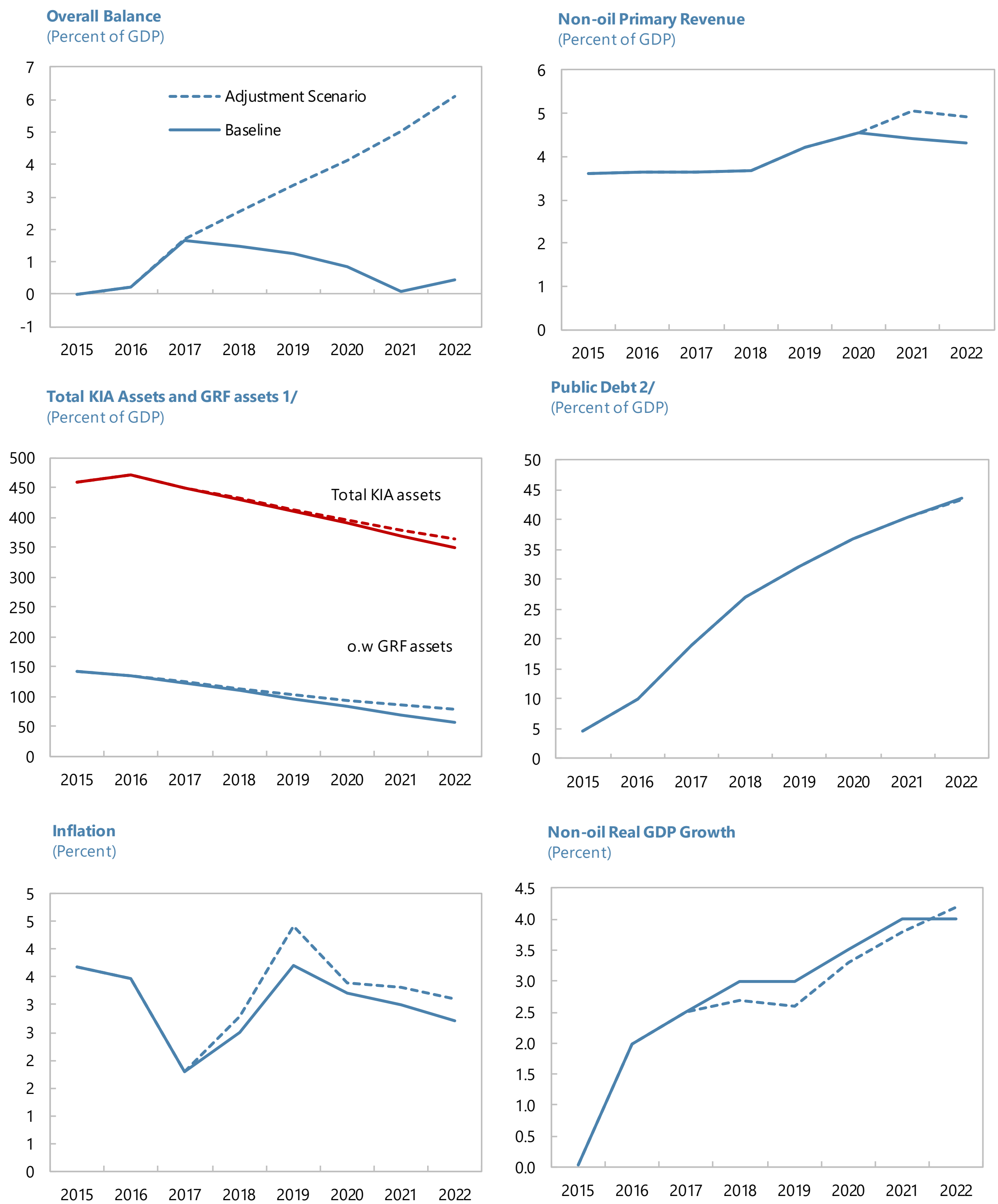


Foreign Assets, 2007–September 2016
(KD billions)



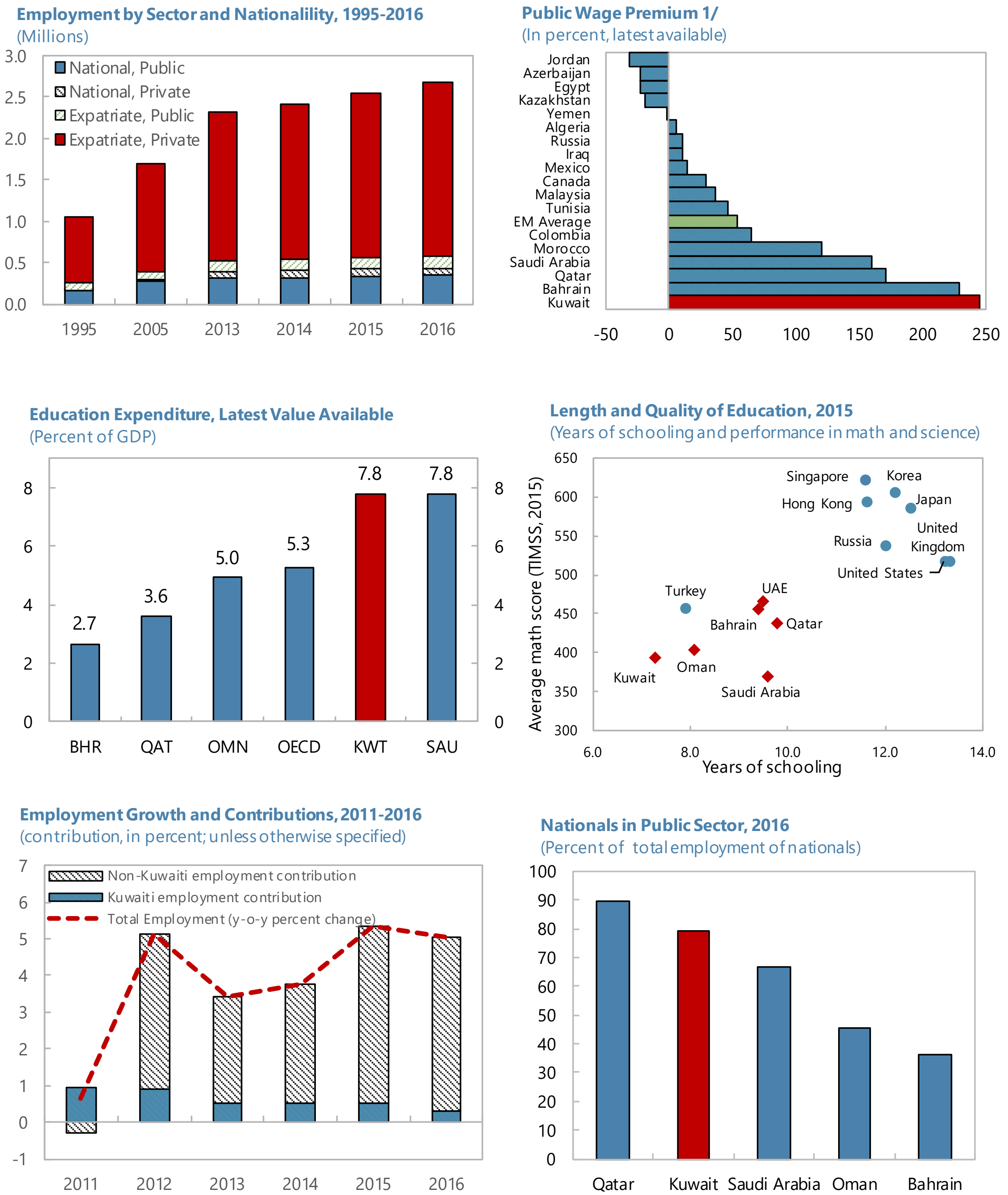
Sources: Country authorities; and IMF staff calculations.
1/ Indicates relative size and includes assets under management.

Figure 6. Economic Outcomes under Baseline and Reform Scenarios



Sources: IMF staff calculations.
1/ KIA and GRF assets are staff estimates and projections.
2/ Debt financing under baseline and adjustment scenarios are assumed to be the same.

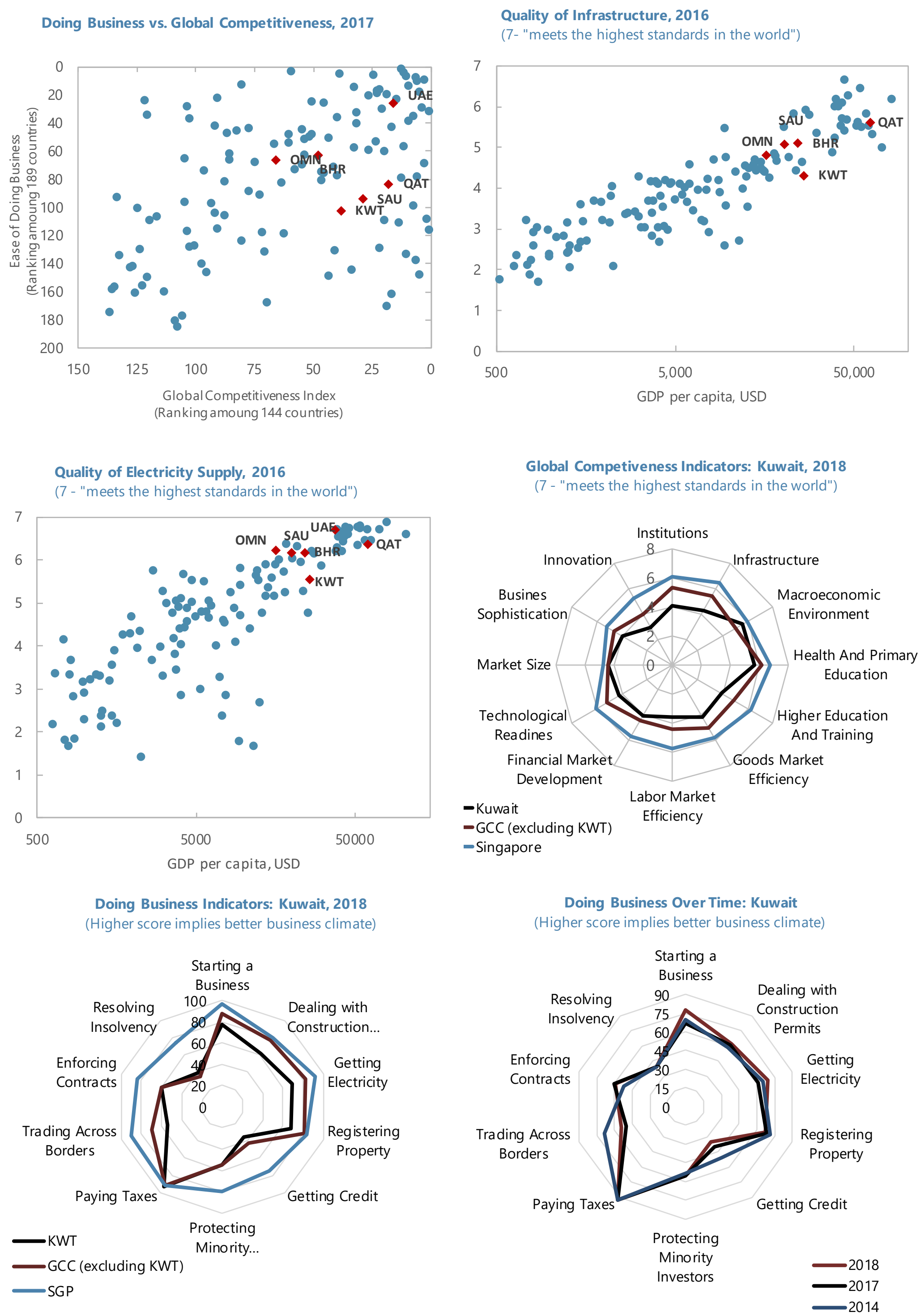
Figure 7. Labor Market Trends



Sources: Country authorities; UNDP; national labor surveys, International Labour Organizations; and IMF staff calculations.

1/ Average public sector wage over agverage private sector wage, except for Iraq where the numbers represent wage premium estimates after controlling for employee characteristics.

Figure 8. Institutions and Governance



Sources: World Bank: *Doing Business Indicators*; World Economic Forum: Global Competitiveness Index; World Economic Outlook.

Table 1. Selected Economic Indicators, 2013–22

				Est.	Proj.					
	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Oil and gas sector										
Total oil and gas exports (billions of U.S. dollars)	108.6	97.6	48.5	41.5	45.3	47.4	49.4	51.5	53.8	56.3
Average oil export price (U.S. dollars/barrel)	105.5	96.5	49.0	41.7	49.1	49.0	49.4	50.0	50.8	51.9
Crude oil production (millions of barrels/day)	2.93	2.87	2.86	2.95	2.71	2.83	2.93	3.02	3.10	3.18
	(Annual percentage change, unless otherwise indicated)									
National accounts and prices										
Nominal GDP (market prices, in billions of Kuwaiti dinar)	49.4	46.3	34.5	33.5	35.9	38.1	40.5	43.1	46.1	49.3
Nominal GDP (market prices, in billions of U.S. dollars)	174.2	162.7	114.6	110.9	117.3	124.3	132.3	140.9	150.6	160.9
Real GDP [1]	0.4	0.6	-1.0	2.2	-2.5	3.9	3.3	3.2	3.3	3.1
Real oil GDP	-1.8	-2.1	-1.7	2.3	-6.0	4.6	3.5	3.0	2.8	2.5
Real non-oil GDP	4.0	5.0	0.0	2.0	2.5	3.0	3.0	3.5	4.0	4.0
CPI inflation (average)	2.7	3.1	3.7	3.5	1.8	2.5	3.7	3.2	3.0	2.7
Unemployment rate (Kuwaiti nationals)	4.7	5.0	4.7	3.3	…	…	…	…	…	…
	(Percent of GDP at market prices)									
Budgetary operations [2]										
Revenue	73.7	67.4	52.1	52.5	52.5	51.4	50.9	50.1	48.8	47.5
Oil	60.3	51.9	35.3	34.3	35.2	34.6	33.9	33.3	32.6	32.1
Non-oil, *of which:*	13.4	15.4	16.9	18.2	17.4	16.8	17.0	16.9	16.1	15.4
Investment income	8.9	10.6	13.3	14.6	13.7	13.2	12.8	12.3	11.7	11.1
Expenditures [3]	38.3	48.8	52.5	51.7	50.9	49.9	49.7	49.3	48.7	47.1
Expense	34.1	43.3	44.8	44.0	43.2	42.2	41.8	41.3	40.6	39.1
Capital	4.1	5.4	7.6	7.7	7.7	7.8	7.9	8.0	8.1	8.0
Balance	35.4	18.6	-0.3	0.8	1.7	1.5	1.3	0.9	0.1	0.4
Balance (after transfer to FGF and excl. inv. income)	20.0	2.4	-17.5	-17.6	-15.9	-15.5	-15.3	-15.3	-15.3	-14.3
Non-oil balance (percent of non-oil GDP) [4]	-91.2	-102.5	-87.7	-80.8	-79.4	-76.9	-74.5	-72.4	-70.7	-67.5
Excluding oil-related subsidies and benefits (percent of non-oil GDP)	-70.7	-81.2	-77.0	-72.0	-71.2	-69.9	-67.8	-65.8	-64.3	-61.3
Total gross debt (calendar year-end) [5]	3.1	3.4	4.7	9.9	19.1	27.0	32.3	36.8	40.5	43.5
	(Percent change; unless otherwise indicated)									
Money and credit										
Net foreign assets [6]	11.4	3.6	-2.1	8.7	-3.4	-0.4	-0.4	0.5	0.7	-0.1
Claims on nongovernment sector	7.2	5.2	7.6	2.9	5.1	7.1	7.9	8.0	8.3	8.1
Kuwaiti dinar 3-month deposit rate (year average; in percent) [7]	0.7	0.8	0.8	1.1	1.7	…	…	…	…	
Stock market unweighted index (annual percent change) [7]	27.2	-13.4	-14.1	2.4	25.0	…	…	…	…	
	(Billions of U.S. dollars, unless otherwise indicated)									
External sector										
Exports of goods	115.8	104.5	54.5	46.5	50.7	53.1	55.5	58.0	60.7	63.6
Of which: non-oil exports	7.2	7.0	6.0	5.0	5.4	5.8	6.1	6.5	6.9	7.3
Annual percentage change	6.6	-2.8	-14.1	-15.7	7.0	6.6	6.2	6.1	6.1	6.1
Imports of goods	-25.6	-27.0	-26.5	-26.4	-27.0	-28.0	-28.8	-29.8	-31.0	-32.3
Current account	70.2	54.4	4.0	-5.0	0.3	-0.4	-0.2	0.2	0.2	0.3
Percent of GDP	40.3	33.4	3.5	-4.5	0.3	-0.3	-0.1	0.2	0.1	0.2
International reserve assets [8]	32.2	32.3	28.3	31.2	31.8	32.9	34.5	36.4	38.7	40.6
In months of imports of goods and services	7.5	7.4	6.4	6.8	6.7	6.7	6.7	6.8	6.9	6.9
Memorandum items [7]:										
Exchange rate (U.S. dollar per KD, period average)	3.53	3.52	3.32	3.32	3.31	…	…	…	…	…
Nominal effective exchange rate (Percentage change)	1.0	1.4	3.1	0.8	-0.1	…	…	…	…	…
Real effective exchange rate (Percentage change)	0.8	1.9	4.9	2.8	-0.7	…	…	…	…	…
Break-even oil price (overall balance; U. S. dollar per barrel)	42.5	54.3	47.7	42.5	46.8	47.0	47.7	48.8	50.9	51.5
Break-even oil price (overall balance - after transfers to FGF and excl. investment income; U. S. dollar per barrel)	79.6	98.0	73.2	68.4	73.8	73.6	74.4	75.7	77.7	78.1
Sovereign rating (S&P)	AA	AA	AA	AA	AA	…	…	…	…	…

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

1 Calculated on the basis of real oil and non-oil GDP at factor cost. Staff estimates for 2015-2016.

2 Based on fiscal year cycle, which starts on April 1 and ends on March 31.

3 Starting in FY 2016/17, there has been a reclassification of expenditure items.

4 Excludes investment income and pension fund recapitalization.

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

6 Excludes SDRs and IMF reserve position.

7 For 2017, based on latest available data.

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

Table 2a. Summary of Government Finance, 2013/14–2022/23
(Billions of Kuwaiti Dinars)

				Est.	Proj.					
	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23
				(Billions of Kuwaiti Dinars)						
Revenue (includes grants) (A)	**35.8**	**29.2**	**17.8**	**17.9**	**19.1**	**19.9**	**21.0**	**22.0**	**22.9**	**23.8**
Taxes	0.4	0.4	0.5	0.6	0.6	0.6	0.8	1.1	1.1	1.2
Other revenue	35.4	28.8	17.4	17.4	18.6	19.3	20.1	20.9	21.8	22.6
Oil and gas	29.3	22.5	12.1	11.7	12.8	13.4	14.0	14.6	15.3	16.1
Investment income and transfer of profits of public entities [1]	4.3	4.6	4.5	5.0	5.0	5.1	5.3	5.4	5.5	5.6
Other [2]	1.8	1.7	0.8	0.7	0.8	0.8	0.9	0.9	1.0	1.0
Total expenditure (B=C+D) [3]	**18.6**	**21.1**	**18.0**	**17.6**	**18.5**	**19.3**	**20.4**	**21.6**	**22.8**	**23.6**
Expense (C)	16.6	18.8	15.4	15.0	15.7	16.3	17.2	18.1	19.0	19.6
Compensation of employees	5.4	5.7	5.8	6.7	7.0	7.3	7.7	8.1	8.5	8.9
Purchases/use of goods & services	2.7	2.9	3.1	2.1	2.3	2.4	2.6	2.8	3.0	3.2
Interest	0.0	0.0	0.0	0.1	0.2	0.4	0.4	0.5	0.6	0.7
Subsidies and social benefits	6.8	7.6	4.8	4.5	4.6	4.5	4.7	4.8	5.0	5.0
Subsidies	2.8	2.4	1.7	1.6	1.6	1.5	1.5	1.6	1.7	1.8
Social benefits	4.0	5.2	3.1	2.9	2.9	3.0	3.1	3.2	3.3	3.2
Payments to social security fund	2.8	3.1	1.9	2.1	2.2	2.2	2.3	2.4	2.4	2.3
Transfers to social security fund	1.7	2.0	1.9	2.1	2.2	2.2	2.3	2.4	2.4	2.3
Fund recapitalization	1.1	1.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other social benefits	1.2	2.1	1.2	0.8	0.8	0.8	0.8	0.9	0.9	0.9
Oil-related	0.6	1.3	0.4	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Others	0.6	0.8	0.8	0.6	0.6	0.6	0.7	0.7	0.7	0.7
Expense not elsewhere classified	1.6	2.5	1.7	1.7	1.7	1.7	1.8	1.8	1.9	1.8
Net acquisition of nonfinancial assets (D)	2.0	2.4	2.6	2.6	2.8	3.0	3.2	3.5	3.8	4.0
Gross operating balance [=A-C]	**19.2**	**10.4**	**2.5**	**2.9**	**3.4**	**3.6**	**3.8**	**3.9**	**3.8**	**4.2**
Net lending / borrowing [=A-B]	**17.2**	**8.1**	**-0.1**	**0.3**	**0.6**	**0.6**	**0.5**	**0.4**	**0.1**	**0.2**
Overall balance (after transfers to FGF and excl. investment income) [4]	9.7	1.0	-6.0	-6.0	-5.8	-6.0	-6.3	-6.7	-7.2	-7.2
Non-oil balance	-12.1	-14.4	-12.2	-11.4	-12.2	-12.8	-13.5	-14.2	-15.3	-15.9
excluding investment income	-16.4	-19.0	-16.7	-16.4	-17.2	-17.9	-18.7	-19.6	-20.8	-21.4
excluding recapitalization of pension	-15.3	-17.9	-16.7	-16.4	-17.2	-17.9	-18.7	-19.6	-20.8	-21.4
excluding oil-related subsidies and benefits	-11.9	-14.2	-14.7	-14.6	-15.4	-16.3	-17.0	-17.9	-18.9	-19.5
Financing (net)	**-9.7**	**-1.0**	**6.0**	**6.0**	**5.8**	**6.0**	**6.3**	**6.7**	**7.2**	**7.2**
Domestic	-0.3	-0.3	-0.4	2.2	1.5	1.0	1.0	1.0	1.0	1.0
External	**-9.4**	**-0.7**	**6.4**	**3.8**	**4.3**	**5.0**	**5.3**	**5.7**	**6.2**	**6.2**
External bonds	0.0	0.0	0.0	2.4	2.4	1.8	1.8	1.8	1.8	1.8
Reserve funds	-9.4	-0.7	6.4	1.4	1.9	3.2	3.5	3.9	4.4	4.4

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) cmpensations.

[3] Starting in FY 2016/17, there has been areclassification of expenditure items.

[4] After 10 percent of total revenue transfred to the Future Generation Fund andexdudin investmentincome.

Table 2b. Summary of Government Finance, 2013/14–2022/23

(Percent of GDP)

				Est.	Proj.					
	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23
				(Percent of GDP)						
Revenue (includes grants)	**73.7**	**67.4**	**52.1**	**52.5**	**52.5**	**51.4**	**50.9**	**50.1**	**48.8**	**47.5**
Taxes	0.8	1.0	1.4	1.6	1.6	1.5	2.0	2.4	2.4	2.3
Other revenue	72.9	66.4	50.8	50.9	51.0	49.9	48.9	47.7	46.4	45.2
Oil and gas	60.3	51.9	35.3	34.3	35.2	34.6	33.9	33.3	32.6	32.1
Investment income and transfer of profits of public entities	8.9	10.6	13.3	14.6	13.7	13.2	12.8	12.3	11.7	11.1
Other	3.7	3.9	2.2	2.0	2.1	2.2	2.2	2.1	2.1	2.0
Total expenditure	**38.3**	**48.8**	**52.5**	**51.7**	**50.9**	**49.9**	**49.7**	**49.3**	**48.7**	**47.1**
Expense	34.1	43.3	44.8	44.0	43.2	42.2	41.8	41.3	40.6	39.1
Compensation of employees	11.2	13.1	17.1	19.5	19.1	18.8	18.7	18.5	18.1	17.8
Purchases/use of goods & services	5.5	6.7	8.9	6.3	6.2	6.3	6.3	6.4	6.4	6.3
Interest	0.1	0.1	0.1	0.3	0.7	0.9	1.1	1.2	1.3	1.4
Subsidies and social benefits	14.0	17.6	13.9	13.1	12.5	11.7	11.3	11.0	10.7	10.0
Subsidies	5.8	5.7	4.9	4.6	4.5	3.8	3.7	3.7	3.6	3.5
Social benefits	8.2	11.9	9.0	8.5	8.1	7.8	7.6	7.4	7.1	6.5
Payments to Social Security Fund	5.8	7.1	5.6	6.2	5.9	5.8	5.6	5.4	5.1	4.6
Transfers to Social Security Fund	3.6	4.6	5.6	6.2	5.9	5.8	5.6	5.4	5.1	4.6
Fund recapitalization	2.2	2.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other social benefits	2.4	4.8	3.4	2.3	2.1	2.1	2.0	2.0	1.9	1.9
Oil-related	1.3	3.0	1.1	0.6	0.4	0.4	0.4	0.4	0.4	0.4
Others	1.1	1.8	2.3	1.7	1.7	1.7	1.6	1.6	1.5	1.5
Expense not elsewhere classified	3.3	5.9	4.8	4.8	4.6	4.5	4.3	4.2	4.0	3.6
Net acquisition of nonfinancial assets	4.1	5.4	7.6	7.7	7.7	7.8	7.9	8.0	8.1	8.0
Gross operating balance	39.5	24.0	7.3	8.5	9.4	9.3	9.1	8.9	8.2	8.4
Net lending / borrowing	35.4	18.6	-0.3	0.8	1.7	1.5	1.3	0.9	0.1	0.4
Overall balance (after transfers to FGF and excl. investment income)	20.0	2.4	-17.5	-17.6	-15.9	-15.5	-15.3	-15.3	-15.3	-14.3
Non-oil balance	-24.9	-33.3	-35.6	-33.4	-33.5	-33.1	-32.7	-32.4	-32.5	-31.7
excluding investment income	-33.8	-43.9	-48.9	-48.0	-47.2	-46.3	-45.4	-44.7	-44.3	-42.8
excluding recapitalization of pension	-31.5	-41.4	-48.9	-48.0	-47.2	-46.3	-45.4	-44.7	-44.3	-42.8
excluding oil-related subsidies and benefits	-24.4	-32.8	-42.9	-42.8	-42.3	-42.0	-41.3	-40.7	-40.3	-38.9
Financing (net)	-19.7	-2.2	17.4	17.6	15.9	15.5	15.3	15.3	15.3	14.3
Domestic	-0.6	-0.7	-1.2	6.6	4.2	2.6	2.5	2.3	2.2	2.0
External	-19.0	-1.5	18.6	11.3	12.0	13.1	13.1	13.2	13.4	12.5
External bonds	0.0	0.0	0.0	7.2	6.7	4.7	4.4	4.2	3.9	3.7
Reserve funds	-19.0	-1.5	18.6	4.1	5.3	8.4	8.7	9.0	9.5	8.9
				(Percent of non-oil GDP)						
Revenue (includes grants)	**213.2**	**166.9**	**93.6**	**88.3**	**88.4**	**85.5**	**83.5**	**81.1**	**77.9**	**75.0**
Total expenditure	**110.8**	**120.8**	**94.2**	**86.9**	**85.6**	**83.1**	**81.5**	**79.7**	**77.7**	**74.3**
Gross operating balance	114.4	59.6	13.1	14.4	15.7	15.4	15.0	14.4	13.1	13.3
Net lending / borrowing	102.4	46.1	-0.6	1.4	2.8	2.5	2.1	1.4	0.2	0.7
Non-oil balance	-72.0	-82.6	-63.9	-56.2	-56.4	-55.0	-53.6	-52.4	-52.0	-49.9
excluding investment income	-97.7	-108.8	-87.7	-80.8	-79.4	-76.9	-74.5	-72.4	-70.7	-67.5
excluding recapitalization of pension	-91.2	-102.5	-87.7	-80.8	-79.4	-76.9	-74.5	-72.4	-70.7	-67.5
excluding oil-related subsidies and benefits	-70.7	-81.2	-77.0	-72.0	-71.2	-69.9	-67.8	-65.8	-64.3	-61.3
Memorandum items:										
Expenses excl. recapitalization of pension fund (percent of nonoil GDP)	92.3	101.1	80.5	73.9	72.6	70.1	68.5	66.8	64.8	61.7
Oil-related subsidies and benefits (percent of nonoil GDP)	20.5	21.3	10.7	8.8	8.2	7.0	6.8	6.5	6.3	6.2
Kuwait Crude oil price (USD per barrel)	103.2	84.6	47.2	43.6	49.1	49.1	49.5	50.2	51.1	52.2
Total gross debt (percent of GDP)	3.1	3.4	4.7	9.9	19.1	27.0	32.3	36.8	40.5	43.5

Table 3. Summary Balance of Payments, 2013–22

	2013	2014	2015	Est. 2016	Proj. 2017	2018	2019	2020	2021	2022
	(Billions of U.S. dollars, unless otherwise indicated)									
Current account	**70.2**	**54.4**	**4.0**	**-5.0**	**0.3**	**-0.4**	**-0.2**	**0.2**	**0.2**	**0.3**
Goods (trade balance)	90.2	77.5	27.9	20.1	23.7	25.1	26.7	28.1	29.7	31.3
Exports	115.8	104.5	54.5	46.5	50.7	53.1	55.5	58.0	60.7	63.6
Oil exports	108.6	97.6	48.5	41.5	45.3	47.4	49.4	51.5	53.8	56.3
Non-oil exports including re-exports[1]	7.2	7.0	6.0	5.0	5.4	5.8	6.1	6.5	6.9	7.3
Of which: re-exports	1.5	1.5	1.4	1.5	1.6	1.7	1.8	1.9	2.0	2.1
Imports	-25.6	-27.0	-26.5	-26.4	-27.0	-28.0	-28.8	-29.8	-31.0	-32.3
Services	-14.8	-18.1	-20.0	-21.0	-22.0	-23.0	-24.0	-25.0	-26.2	-27.4
Transportation	-4.0	-3.9	-3.8	-4.1	-4.3	-4.5	-4.7	-4.9	-5.1	-5.4
Insurance	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Travel	-9.4	-11.4	-12.6	-12.3	-12.9	-13.5	-14.0	-14.7	-15.4	-16.2
Other services	-1.5	-2.7	-3.6	-4.5	-4.8	-5.0	-5.2	-5.4	-5.6	-5.9
Investment income	14.0	15.7	12.7	13.3	16.3	16.0	16.0	16.2	16.0	15.9
Receipts	14.6	16.3	16.5	17.6	17.8	17.8	18.2	18.5	18.6	18.7
General government[2]	11.4	13.0	13.1	14.2	13.7	14.0	14.5	14.9	15.1	15.3
Other sectors[3]	3.2	3.3	3.4	3.4	4.1	3.8	3.7	3.6	3.5	3.4
Payments	-0.7	-0.7	-3.8	-4.4	-1.5	-1.8	-2.1	-2.4	-2.6	-2.8
General government	0.0	0.0	0.0	0.0	-0.3	-0.5	-0.8	-0.9	-1.1	-1.3
Other	-0.7	-0.7	-3.8	-4.3	-1.3	-1.3	-1.4	-1.4	-1.5	-1.5
Current transfers	-19.1	-20.7	-16.6	-17.3	-17.6	-18.5	-18.9	-19.1	-19.3	-19.5
Capital and financial account	**-64.2**	**-52.4**	**-11.1**	**6.3**	**0.2**	**1.6**	**1.7**	**1.7**	**2.1**	**1.7**
Capital account[4]	4.5	3.8	-0.3	-0.4	-0.5	0.0	0.0	0.0	0.0	0.0
Financial account	-68.7	-56.2	-10.8	6.7	0.7	1.6	1.7	1.7	2.1	1.7
Direct investment	-15.2	11.4	-5.1	-4.1	0.7	0.1	0.4	0.8	0.7	0.9
Abroad	-16.6	10.5	-5.4	-4.6	0.3	-0.4	-0.1	0.2	0.1	0.2
In Kuwait	1.4	1.0	0.3	0.4	0.4	0.5	0.5	0.5	0.6	0.6
Portfolio investment	-21.2	-62.0	-33.1	-18.8	-21.7	-20.8	-20.6	-20.4	-19.1	-7.0
Other investment (net)	-32.2	-5.4	27.2	29.8	21.6	22.3	21.9	21.3	20.5	7.8
Net errors and omissions[5]	-2.7	-2.0	3.1	1.6	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	**3.3**	**0.0**	**-3.9**	**2.8**	**0.6**	**1.2**	**1.5**	**1.9**	**2.3**	**1.9**
Memorandum items										
Current account/GDP (in percent)	40.3	33.4	3.5	-4.5	0.3	-0.3	-0.1	0.2	0.1	0.2
Current account (excl. oil)/GDP (in percent)	-22.0	-26.5	-38.8	-41.9	-38.3	-38.4	-37.5	-36.4	-35.6	-34.8
Investment income/GDP (in percent)	8.0	9.6	11.1	12.0	13.9	12.8	12.1	11.5	10.6	9.9
WEO oil price (dollars per barrel)	104.1	96.2	50.8	42.8	50.3	50.2	50.5	51.1	51.9	53.0
Import growth (in percent)	5.5	5.5	-1.6	-0.6	2.4	3.5	3.0	3.5	4.0	4.0
International reserve assets (billions of U.S. dollars)[6]	32.2	32.3	28.3	31.2	31.8	32.9	34.5	36.4	38.7	40.6
In months of imports of goods and services	7.5	7.4	6.4	6.8	6.7	6.7	6.7	6.8	6.9	6.9

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

[1] Also includes unrecorded 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] Includes UN war compensation.

[5] Includes other unclassified private-sector flows.

[6] Includes SDRs and IMF reserve position.

Table 4. Monetary Survey, 2013–22

End of period	2013	2014	2015	Est. 2016	Proj. 2017	2018	2019	2020	2021	2022
				(Millions of KD)						
Foreign assets (net) [1]	15,409	15,971	15,633	16,997	16,417	16,349	16,277	16,365	16,471	16,450
Central bank	8,250	8,588	7,774	8,693	8,887	9,249	9,723	10,315	11,008	11,603
Local banks	7,158	7,383	7,859	8,305	7,530	7,100	6,554	6,050	5,463	4,847
Domestic assets (net)	17,150	17,649	18,606	17,838	20,258	22,839	25,909	29,087	32,670	36,573
Claims on government (net)	-4,189	-4,340	-5,153	-4,370	-4,873	-3,924	-2,788	-1,573	-565	48
Central bank (net)	-635	-616	-854	-978	-1,974	-1,878	-1,593	-1,227	-1,063	-1,242
Claims	0	0	0	0	0	0	0	0	0	0
Deposits	635	616	854	978	1,974	1,878	1,593	1,227	1,063	1,242
Local banks (net)	-3,554	-3,723	-4,299	-3,393	-2,899	-2,046	-1,195	-347	498	1,290
Claims	1,502	1,563	1,580	3,287	4,412	5,412	6,412	7,412	8,412	9,362
Public debt instruments	1,502	1,563	1,580	3,287	4,412	5,412	6,412	7,412	8,412	9,362
Deposits	5,057	5,286	5,879	6,679	7,311	7,457	7,607	7,759	7,914	8,072
Claims on nongovernment sector	31,099	32,706	35,177	36,201	38,039	40,749	43,970	47,479	51,438	55,605
Credit facilities	28,911	30,737	33,210	34,307	36,233	38,815	41,882	45,225	48,996	52,965
Local investments	2,188	1,969	1,967	1,894	1,806	1,934	2,087	2,254	2,442	2,640
Other items (net)	-9,760	-10,717	-11,417	-13,993	-12,908	-13,986	-15,273	-16,818	-18,203	-19,080
Broad money [2]	32,558	33,620	34,239	34,835	36,675	39,188	42,185	45,452	49,142	53,023
Money	8,677	9,253	9,091	8,812	9,884	10,588	11,425	12,337	13,366	14,448
Quasi money	23,882	24,367	25,148	26,024	26,791	28,600	30,760	33,115	35,776	38,574
Of which: Foreign currency deposits	3,122	2,891	3,591	2,922	2,489	2,567	2,669	2,782	2,914	3,051
				(Annual percentage change)						
Foreign assets (net)	11.4	3.6	-2.1	8.7	-3.4	-0.4	-0.4	0.5	0.7	-0.1
Central Bank	12.7	4.1	-9.5	11.8	2.2	4.1	5.1	6.1	6.7	5.4
Local banks	10.0	3.1	6.4	5.7	-9.3	-5.7	-7.7	-7.7	-9.7	-11.3
Domestic assets (net)	8.3	2.9	5.4	-4.1	13.6	12.7	13.4	12.3	12.3	11.9
Claims on government (net)	-9.8	-3.6	-18.7	15.2	-11.5	19.5	29.0	-43.6	-64.1	-108.5
Claims on nongovernment sector	7.2	5.2	7.6	2.9	5.1	7.1	7.9	8.0	8.3	8.1
Other items (net)	4.2	9.8	6.5	22.6	-7.8	8.4	9.2	10.1	8.2	4.8
Broad money	9.7	3.3	1.8	1.7	5.3	6.9	7.6	7.7	8.1	7.9
Money	13.4	6.6	-1.7	-3.1	12.2	7.1	7.9	8.0	8.3	8.1
Quasi money	8.5	2.0	3.2	3.5	2.9	6.8	7.6	7.7	8.0	7.8
Of which: f oreign currency deposits	37.4	-7.4	24.2	-18.6	-14.8	3.1	4.0	4.2	4.7	4.7
				(Change in percent of beginning of period broad money stock)						
Foreign assets (net)	5.3	1.7	-1.0	4.0	-1.7	-0.2	-0.2	0.2	0.2	0.0
Central bank	3.1	1.0	-2.4	2.7	0.6	1.0	1.2	1.4	1.5	1.2
Local banks	2.2	0.7	1.4	1.3	-2.2	-1.2	-1.4	-1.2	-1.3	-1.3
Domestic assets (net)	4.4	1.5	2.8	-2.2	6.9	7.0	7.8	7.5	7.9	7.9
Claims on government (net)	-1.3	-0.5	-2.4	2.3	-1.4	2.6	2.9	2.9	2.2	1.2
Claims on nongovernment sector	7.0	4.9	7.3	3.0	5.3	7.4	8.2	8.3	8.7	8.5
Other items (net)	-1.3	-2.9	-2.1	-7.5	3.1	-2.9	-3.3	-3.7	-3.0	-1.8
Broad money	9.7	3.3	1.8	1.7	5.3	6.9	7.6	7.7	8.1	7.9
Money	3.4	1.8	-0.5	-0.8	3.1	1.9	2.1	2.2	2.3	2.2
Quasi money	6.3	1.5	2.3	2.6	2.2	4.9	5.5	5.6	5.9	5.7
Of which: Foreign currency deposits	2.9	-0.7	2.1	-2.0	-1.2	0.2	0.3	0.3	0.3	0.3
Memorandum items:										
Non-oil GDP/M2 (in peercent)	51.3	50.7	54.8	57.3	58.0	58.2	58.3	58.5	58.6	58.7
Foreign currency deposits/M2 (in percent)	9.6	8.6	10.5	8.4	6.8	6.5	6.3	6.1	5.9	5.8
Private credit/non-oil GDP (in percent)	186.1	191.7	187.4	181.5	178.7	178.7	178.7	178.7	178.7	178.7

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. Financial Soundness Indicators of the Banking Sector, 2006–17

(Percent unless specified otherwise)[1]

	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	Jun-17
Capital adequacy												
Regulatory capital to risk-weighted assets	20.2	19.3	15.6	16.7	18.9	18.5	18.5	18.9	16.9	17.5	18.6	18.3
Regulatory Tier I capital to risk-weighted assets	17.7	17.2	14.3	14.9	17.3	16.9	16.0	17.1	15.6	16.1	16.7	16.4
Capital to assets	12.6	12.3	10.9	11.4	12.6	12.4	12.6	12.2	11.1	11.8	12.8	12.5
Loan composition and quality [2]												
Oil/gas	0.7	0.8	0.9	1.2	1.2	1.1	1.6	1.5	2.2	2.4	3.4	4.1
Trade	11.8	10.4	10.2	10.6	10.0	10.5	12.1	13.0	12.8	11.7	11.8	11.9
Industry	5.0	5.9	6.8	6.5	7.0	7.1	7.9	7.8	7.3	6.9	6.7	6.7
Construction	13.4	12.6	11.9	11.4	12.7	12.1	12.6	12.2	11.9	12.0	12.3	12.0
Real estate	17.5	19.2	18.1	20.6	20.0	19.6	19.2	18.9	18.5	17.5	16.6	16.7
Equity purchase loans (corporate)	5.4	4.5	5.8	5.9	5.7	5.8	3.5	3.4	3.0	3.0	2.9	2.7
Agriculture/fishing	0.2	0.1	0.7	0.3	0.4	0.2	0.3	0.3	0.4	0.3	0.3	0.2
Financial Institutions	14.6	15.9	12.8	12.7	14.1	13.1	11.2	10.4	11.9	14.0	13.3	12.3
Of which: investment companies	5.3	7.9	7.5	8.0	8.7	6.1	4.3	4.0	3.1	2.9	2.6	2.5
Of which: banks	0.0	0.0	0.0	0.0	4.6	3.7	6.7	5.7	8.0	10.5	9.8	9.1
Public services	1.6	2.2	1.9	1.6	1.6	1.7	2.6	1.8	2.2	2.2	1.8	1.8
Households	20.3	19.1	16.0	16.1	16.3	17.0	19.4	20.0	20.2	20.5	20.7	20.5
Of which: credit card advances	1.0	0.8	0.6	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5
Of which: installment loans	13.7	12.1	10.9	12.7	12.1	12.9	13.2	14.4	14.8	15.5	16.1	16.2
Of which: consumer loans	3.7	4.1	2.5	1.0	2.2	2.2	2.9	3.0	2.9	2.5	2.4	2.3
Of which: equity purchase loans (individuals)	1.8	2.1	2.0	1.9	1.4	1.4	2.9	2.6	2.6	2.5	2.2	2.1
Other	9.6	9.2	14.8	13.3	11.1	11.8	9.5	10.7	9.7	9.6	10.3	11.1
Gross non-performing loans to total loans	4.6	3.8	6.8	11.5	8.9	7.3	5.2	3.6	2.9	2.4	2.2	2.4
NPLs net of specific provisions to total loans net of specific provisions	2.5	2.1	4.9	7.4	6.1	5.3	3.8	2.5	1.9	1.6	1.5	1.7
Specific provisions to gross NPLs	47.4	47.2	29.0	38.3	33.9	29.5	26.9	31.7	35.2	32.7	32.9	31.6
NPLs net of specific provisions to Tier I capital	12.6	10.8	31.5	46.2	33.8	28.7	51.6	34.0	11.2	9.5	8.3	9.4
Loans to shareholders, parent companies, & directors to total loans	4.9	4.2	4.9	6.4	2.0	2.3	2.6	6.3	3.6	3.7	3.8	3.6
Large exposures to Tier I capital	147.6	141.6	212.4	165.1	124.3	105.3	100.4	87.2	97.1	101.1	94.7	107.6
Specific provisions to gross loans	2.2	1.8	2.0	4.4	3.0	2.1	1.4	1.2	1.0	0.8	0.7	0.8
Profitability												
Return on Average Assets (ROAA) [3]	2.7	3.3	0.8	0.7	1.2	1.1	1.2	1.0	1.1	1.1	1.1	1.1
Return on Average Equity (ROAE) [3]	20.1	24.3	6.5	6.1	9.1	8.1	9.1	7.4	8.7	8.8	8.5	8.8
Net interest income to gross income	33.9	29.0	36.6	44.5	49.9	47.6	48.1	49.9	47.1	47.6	49.9	49.6
Non-interest income to gross income	29.0	29.0	21.6	25.3	24.6	33.1	33.4	32.8	30.8	30.5	22.1	22.8
Trading and foreign exchange income to gross income	13.7	15.1	6.7	6.0	4.1	10.0	14.9	10.4	12.5	12.1	6.8	6.4
Non-interest expenses to gross income	27.6	23.9	26.4	36.9	37.7	36.1	34.0	37.2	33.4	31.8	29.6	27.4
Non-interest expenses to average assets [3]	1.4	1.5	1.6	1.9	1.6	2.1	1.9	1.9	1.6	1.5	1.4	1.4
Personnel expenses to non-interest expenses	50.7	49.6	48.0	42.9	48.7	36.8	39.0	41.7	41.1	49.3	53.4	54.7
Liquidity												
Core liquid assets to total assets [4]	29.3	26.9	20.8	20.4	17.7	22.1	21.0	22.5	24.7	24.3	24.1	23.9
Core liquid assets to short-term liabilities	38.6	34.1	28.0	28.6	27.8	36.3	34.8	30.3	32.7	31.7	31.4	31.2
Liquid assets to total assets	34.5	32.9	28.4	27.9	22.8	26.5	27.3	25.4	30.7	29.8	30.1	31.5
Liquid assets to short term liabilities	45.3	41.7	38.4	39.2	35.7	43.7	45.2	34.1	40.6	38.9	39.1	41.1
FX- loans to total loans	19.7	23.3	24.9	25.8	25.5	25.8	28.1	28.2	26.0	30.5	29.1	29.2
FX- deposits to total deposits	28.8	34.9	35.1	32.7	30.7	33.8	34.6	30.7	37.0	38.8	33.2	37.8
FX- liabilities to total liabilities	23.2	27.8	24.2	22.6	11.2	11.4	14.5	18.9	18.8	30.2	…	…
Deposits to assets	59.3	56.4	59.2	58.8	56.7	58.3	63.3	62.2	59.4	59.2	58.4	59.0
Loans to deposits	96.1	103.1	109.0	113.0	116.5	110.9	100.5	99.5	103.6	108.3	108.9	108.1
FX- loans to FX-deposits	65.5	68.9	77.3	89.1	96.8	84.6	81.5	91.4	72.8	85.3	95.7	83.5
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		10.2	8.1	7.7	18.0	…	…
Off-balance sheet operations as percent of assets	32.1	34.7	32.5	25.3	26.2	25.4	26.3	27.8	28.5	28.2	32.1	31.3
Gross asset position in derivatives as a percentage of tier I capital	77.9	90.9	71.1	46.9	33.6		41.1	65.3	75.0	139.7	…	…
Gross liability position in derivatives as a percentage of tier I capital	77.9	91.0	71.1	46.8	39.4		40.9	65.1	75.0	139.7	…	…
Equity exposure to capital	40.6	42.4	47.1	45.4	39.1	43.7	37.5	35.3	29.6	28.1	24.8	23.0

Source: Central Bank of Kuwait

[1] Data are on consolidated basis.

[2] 2016 data for loan composition is as of June 2016.

[3] Averaging was not applied in 2006 indicators.

[4] 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's 2016 Article IV Recommendations

Recommendations	Current Status
Implement gradual fiscal adjustment and shift expenditure composition toward growth-enhancing investment.	Current expenditure has been further curtailed in 2016/17, driven mostly by a decline in subsidies and transfers, allowing for an improvement in the underlying (non-oil) fiscal position.
Further reform energy subsidies	Electricity and water prices were increased by about 180 percent cumulatively between May and August 2017.
Introduce excises and VAT and a business profit tax for domestic companies, and improve tax administration. Adjust prices of government services.	The MOF has prepared a draft excise tax bill, which targets selective goods, such as tobacco and sugary drinks. A number of government fees—including work permit and health care fees for expatriates—have been increased. The GCC regional agreement on VAT and excise is pending ratification by the Parliament.
Establish a medium-term fiscal framework and improve public financial management.	The government has started implementing 3-year rolling expenditure ceilings and a top-down approach to budgeting.
Further improve business environment to foster diversification (business climate, privatization, competition).	Kuwait's ranking in the WB Doing Business Indicators has improved by 6 positions this year, reflecting significant progress in streamlining procedures to start businesses.
Further strengthen AML/CFT and anticorruption frameworks.	Regulators are placing greater emphasis on risk-based AML/CFT inspections. The National Risk Assessment is close to completion. Its results will help concerned authorities place greater emphasis on risk-based AML/CFT efforts. After legal challenges, the constitutional court recently upheld the law pertaining to the mandate, powers, and organizational structure of the ACA.
Strengthen insolvency regime and crisis management framework, and develop special resolution regime for banks.	The authorities recently received Fund TA in this area.
Establish framework to operationalize macro-prudential measures.	Macroprudential measures are periodically reassessed by the CBK.
Develop a liquidity forecasting framework	Coordination between the CBK, the KIA and the DMO is ongoing.
Develop a medium-term debt management strategy, diversify investor base, introduce regular market-based auctions, increase coordination between MOF, CBK, and KIA.	The government has submitted to Parliament a law to extend the borrowing limit and allow the government to issue debt instruments with maturities up to 30 years (from a current limit of 10 years). The government is working on a law that would allow it to issue Sukuk.
Further improve annual national accounts; produce quarterly national accounts; rebase CPI	CPI data has been rebased using weights derived from the 2013 household survey. The authorities are working to produce quarterly national accounts and improve the methodology to estimate subsidies at constant prices.

Annex II. Risk Assessment Matrix[1]

Nature/source of main threats	Likelihood of Risk/Time Horizon	Expected impact on the economy if risk materializes	Recommended Policy Response
Lower energy prices	**Low/Short to Medium Term**	**High** Fiscal and external balances would deteriorate; government financing needs would increase. Should these would be funded domestically, this could crowd out credit to the private sector. Private sector confidence would likely decline and non-oil growth would soften. Lower oil prices would affect liquidity in the banking system and credit growth. Volatile equity markets and a further softening in the real estate markets would impact banks' asset quality. There could be second round effects on growth, asset quality and bank liquidity.	Financial buffers provide policy space for gradual fiscal adjustment. However, with a further sustained decline in oil prices, the government would need to implement a more ambitious fiscal consolidation. Increased efforts at diversification would also be important. Financing options should consider the need to maintain adequate liquidity in the banking system. Central bank liquidity management capabilities should be enhanced and supervisory vigilance is needed to identify emerging financial stability risks to facilitate a timely response.
Tighter global financial conditions	**High/Short term**	**Medium** This could pose funding, market and credit risks for investment companies (ICs) and banks. Selected banks, which have increased reliance on foreign liabilities, could face funding tightness. The government also has begun tapping international markets. Although the IC sector has been shrinking, some ICs have exposures to global and regional financial and real estate markets, and are dependent on foreign financing.	Enhanced surveillance of banking stability risks. Improved monitoring and risk-based supervision of ICs.
Deepening in Qatar diplomatic rift and slowdown in GCC integration.	**Low/Short to Medium Term**	**Low** Investor confidence across the GCC could be affected, leading to capital outflows or higher financing costs. Risks could increase for banks if growth slows down, but some protection given banks' large loss absorption buffers.	Enhanced surveillance of financial system.

Nature/source of main threats	Likelihood of Risk/Time Horizon	Expected impact on the economy if risk materializes	Recommended Policy Response
Slower and less effective implementation of the Development Plan (DP) 2015-19.	**Medium/Short to Medium Term**	**Medium** Lower non-oil growth prospects.	Better integrate the DP with the medium-term fiscal framework to ensure continued implementation. Improve performance of the budget through a public expenditure review to support prioritization of public spending and strengthen anticorruption efforts.
Reversal of fiscal reforms or slower adjustment of non-core government spending	**Medium/Short to Medium Term**	**Medium** Lower pace of underlying fiscal adjustment. Larger financing needs and need to rely more heavily on accumulated buffers.	Correct slippages. Implement medium-term fiscal framework to underpin fiscal adjustment and reduce risks over the medium term.
Severe property price correction	**Low**	**Medium** Though banks have substantial loss absorption capacity in terms of capital and loan loss provisioning, the losses could be significant given high exposures to the real estate sector, both directly and indirectly through collateral and common exposures.	Macro-prudential tools to limit exposures to real estate should be supported by improved real estate statistics. This will support monitoring of developments in the sector and enhanced techniques to capture banks' direct and indirect exposures to the real estate sector to facilitate timely supervisory response. Strengthen crisis preparedness and management framework.

[1] The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff). The relative likelihood is the staff's subjective assessment of the risks surrounding the baseline ("low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability between 30 and 50 percent). The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with the authorities. Non-mutually exclusive risks may interact and materialize jointly. "Short term (ST)" and "medium term (MT)" are meant to indicate that the risk could materialize within 1 year and 3 years, respectively.

Annex III. Public Sector Debt Sustainability Analysis (DSA)

(In percent of GDP unless otherwise indicated; on a calendar-year basis)

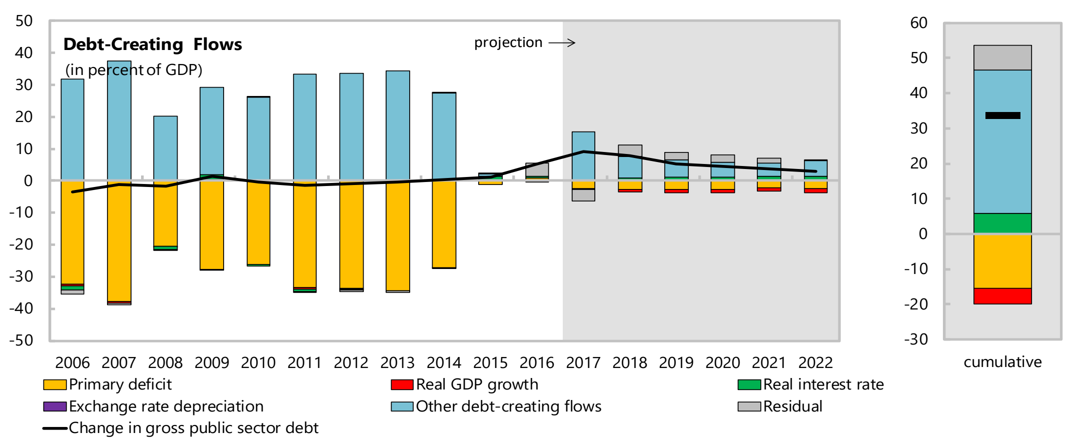
Debt, Economic and Market Indicators [1/]

	Actual			Projections					
	2006-2014 [2/]	2015	2016	2017	2018	2019	2020	2021	2022
Nominal gross public debt	5.4	4.7	9.9	19.1	27.0	32.3	36.8	40.5	43.5
Public gross financing needs	-29.6	-0.4	1.1	-1.8	-1.3	-0.9	-0.4	0.3	2.4
Real GDP growth (in percent)	2.9	-1.0	2.2	-2.5	3.9	3.3	3.2	3.3	3.1
Inflation (GDP deflator, in percent)	5.5	-24.8	-4.9	9.9	2.0	3.1	3.2	3.5	3.6
Nominal GDP growth (in percent)	9.0	-25.5	-2.8	7.1	6.0	6.5	6.5	6.9	6.8
Effective interest rate (in percent) [4/]	3.2	2.2	4.7	7.8	7.7	7.4	7.3	7.3	7.3

As of November 02, 2017		
Sovereign Spreads		
EMBIG (bp) 3/		293
5Y CDS (bp)		na
Ratings	Foreign	Local
Moody's	Aa2	Aa2
S&Ps	AA	AA
Fitch	AA	AA

Contribution to Changes in Public Debt

	Actual			Projections							
	2006-2014	2015	2016	2017	2018	2019	2020	2021	2022	cumulative	debt-stabilizing primary balance [9/]
Change in gross public sector debt	-0.9	1.2	5.2	9.2	7.9	5.3	4.5	3.7	3.0	33.6	
Identified debt-creating flows	-0.6	1.2	1.0	12.7	4.3	2.9	2.2	2.1	2.6	26.7	
Primary deficit	-30.3	-1.1	0.9	-2.6	-2.7	-2.8	-2.7	-2.2	-2.5	-15.4	5.0
Primary (noninterest) revenue and gra	69.0	55.4	51.7	52.8	51.7	51.0	50.3	49.1	47.8	302.8	
Primary (noninterest) expenditure	38.7	54.3	52.6	50.3	49.0	48.3	47.7	46.9	45.3	287.5	
Automatic debt dynamics [5/]	-0.4	1.3	0.4	0.1	0.3	0.2	0.3	0.1	0.2	1.2	
Interest rate/growth differential [6/]	-0.4	1.3	0.4	0.1	0.3	0.2	0.3	0.1	0.2	1.2	
Of which: real interest rate	-0.2	1.2	0.5	-0.2	1.0	1.1	1.2	1.3	1.4	5.8	
Of which: real GDP growth	-0.2	0.0	-0.1	0.2	-0.7	-0.8	-1.0	-1.1	-1.2	-4.6	
Exchange rate depreciation [7/]	0.0	0.0	0.0	…	…	…	…	…	…	…	
Other identified debt-creating flows	30.1	1.0	-0.3	15.2	6.7	5.4	4.6	4.2	4.9	40.9	
Privatization/Drawdown of Deposits	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Asset accumulation requirement	30.1	1.0	-0.3	15.2	6.7	5.4	4.6	4.2	4.9	40.9	
Residual, including asset changes [8/]	-0.4	0.0	4.3	-3.5	3.6	2.4	2.4	1.6	0.4	6.9	



Source: IMF staff.

1/ Public sector is defined as general government.

2/ Based on available data.

3/ Long-term bond spread over German bonds.

4/ Defined as interest payments divided by debt stock (excluding guarantees) at the end of previous year.

5/ Derived as $[(r - \pi(1+g) - g + ae(1+r)]/(1+g+\pi+g\pi))$ times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; a = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

6/ The real interest rate contribution is derived from the numerator in footnote 5 as $r - \pi (1+g)$ and the real growth contribution as $-g$.

7/ The exchange rate contribution is derived from the numerator in footnote 5 as $ae(1+r)$.

8/ Includes asset changes and interest revenues (if any). For projections, includes exchange rate changes during the projection period.

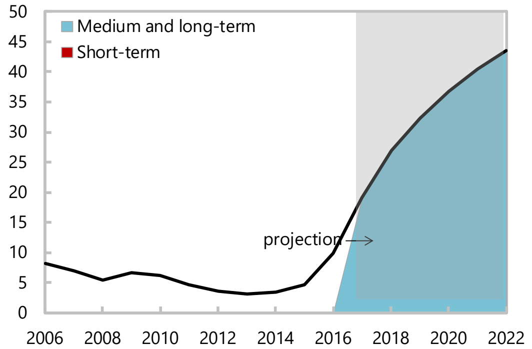
9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year. The debt stabilizing primary balance under the assumed asset accumulation of 4.9 percent of GDP in 2022 is equal to 5 percent. Under no asset accumulation, the debt-stablizing primary balance would have been -0.2 percent of GDP.

Kuwait Public DSA - Composition of Public Debt and Alternative Scenarios

Composition of Public Debt

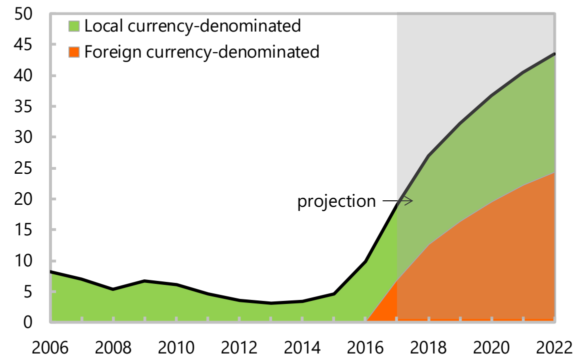
By Maturity

(in percent of GDP)



By Currency

(in percent of GDP)

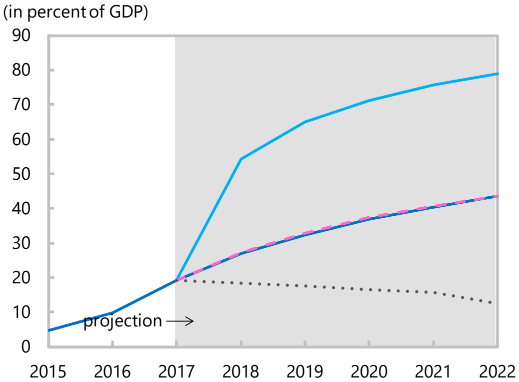


Alternative Scenarios

Baseline
Contingent Liability Shock
Historical
Constant Primary Balance

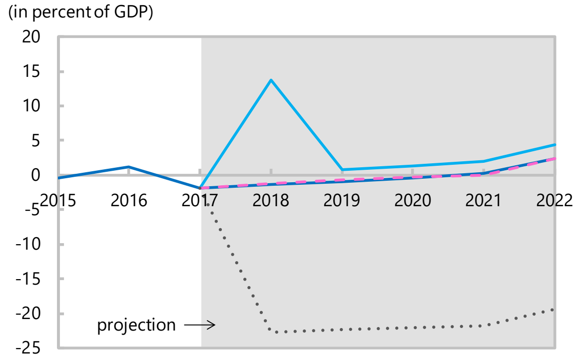
Gross Nominal Public Debt

(in percent of GDP)



Public Gross Financing Needs

(in percent of GDP)



Underlying Assumptions

(in percent)

Baseline Scenario	2017	2018	2019	2020	2021	2022
Real GDP growth	-2.5	3.9	3.3	3.2	3.3	3.1
Inflation	9.9	2.0	3.1	3.2	3.5	3.6
Primary Balance	2.6	2.7	2.8	2.7	2.2	2.5
Effective interest rate	7.8	7.7	7.4	7.3	7.3	7.3
Constant Primary Balance Scenario						
Real GDP growth	-2.5	3.9	3.3	3.2	3.3	3.1
Inflation	9.9	2.0	3.1	3.2	3.5	3.6
Primary Balance	2.6	2.6	2.6	2.6	2.6	2.6
Effective interest rate	7.8	7.7	7.3	7.2	7.2	7.2

Historical Scenario	2017	2018	2019	2020	2021	2022
Real GDP growth	-2.5	2.0	2.0	2.0	2.0	2.0
Inflation	9.9	2.0	3.1	3.2	3.5	3.6
Primary Balance	2.6	24.1	24.1	24.1	24.1	24.1
Effective interest rate	7.8	7.7	10.0	12.2	14.3	16.4
Contingent Liability Shock						
Real GDP growth	-2.5	-1.3	-1.9	3.2	3.3	3.1
Inflation	9.9	0.7	1.8	3.2	3.5	3.6
Primary Balance	2.6	-11.9	2.8	2.7	2.2	2.5
Effective interest rate	7.8	9.7	6.6	6.4	6.3	6.3

Source: IMF staff.

Annex IV. Baseline and Reform Scenario

I. Assumptions

Baseline scenario

Based on enacted and announced policies and reforms, and assumes expenditure restraint.

- Non-oil revenues are assumed to increase as a result of introducing excises and VAT (2019) at 5 percent (estimated together to generate around 1 percent of GDP of additional revenue).
- Savings from the fuel price increases (about 0.2 percent of GDP by 2022) and the electricity and water tariff adjustments (1.1 percent of GDP) are included.
- Spending restraint: wages and transfers are assumed to grow with inflation, while public employment expands at a rate of 2 percent annually; goods and services expand in line with non-oil GDP.
- Capital expenditure is assumed to grow in line with non-oil GDP.

Reform scenario

Assumes a gradual reduction of expenditure as a share of non-oil GDP to 54 percent by 2022. The target is derived from a historical normal level and would result in a gradual reduction of the gap from intergenerational equity level of the non-oil primary balance.

- Further to the baseline, fuel prices are assumed to gradually increase starting from fiscal year 2018/19 to reach international or cost recovery levels by 2022 (elimination of fuel subsidy will save 0.4 percent of GDP).
- Water and electricity tariffs are assumed increase gradually to cut the subsidy in half by 2022 (2 percent of GDP savings by 2022).
- Compensation for fuel prices changes is assumed to be paid to the most vulnerable households. Staff assumed compensation will take up about one fourth of the projected saving from reform (cost of 0.1 percent of GDP).
- The wage bill is driven by stable public employment and wages increasing by slightly less than inflation. The wage reform under consideration will lead in the first year to an increase in the wage bill by KD 320 million due to standardization of the salary structure, and annual wage increases below inflation—consistent with staff advice to allow flexibility to increase wage by less than inflation if macroeconomic conditions warrant (2.3 percent of GDP savings by 2022).
- Goods and services, transfers, and other current spending items are projected to increase by a slower rate than in the baseline (non-oil GDP growth) by 2.5 percent to help achieve the expenditure target and reflect the authorities' objectives in the Vision to rationalize spending (1 percent of GDP savings).
- The reform scenario makes room for additional allocations for capital spending (1 percent above nominal non-oil GDP growth), costing 0.4 percent of GDP by 2022.
- Non-oil revenues increase as a result of introducing the corporate profit tax on domestic corporates starting in 2021 (estimated additional revenue of 0.7 percent of GDP every year).

II. Key Indicators, 2015–22
(In percent of GDP)

	Est.		Proj.						Cumulative
	2015	2016	2017	2018	2019	2020	2021	2022	2017-22
Baseline Scenario									
Overall balance	-0.3	0.8	1.7	1.5	1.3	0.9	0.1	0.4	
Overall balance (after transfer to FGF and excl. inv. income)	-17.5	-17.6	-15.9	-15.5	-15.3	-15.3	-15.3	-14.3	
Non-oil primary balance									
(Percent of non-oil GDP)	-87.7	-80.8	-79.4	-76.9	-74.5	-72.4	-70.7	-67.5	
Non-oil primary revenue	3.6	3.6	3.7	3.7	4.2	4.5	4.4	4.3	
Primary spending	52.4	51.4	50.2	49.0	48.6	48.0	47.3	45.7	
Total government debt	4.7	9.9	19.1	27.0	32.3	36.8	40.5	43.5	
Total buffer by the KIA 1/	460.0	470.2	449.5	430.6	410.2	390.3	369.4	349.9	
of which GRF assets	144.0	137.1	126.2	113.8	101.0	88.4	75.4	63.6	
Net government financial assets	455.3	460.4	430.4	403.6	378.0	353.5	328.9	306.5	
Current account balance	3.5	-4.5	0.3	-0.3	-0.1	0.2	0.1	0.2	
International reserves (in months of imports)	6.4	6.8	6.7	6.7	6.7	6.8	6.9	6.9	
Credit to the private sector (percentage change)	7.6	2.9	5.1	7.1	7.9	8.0	8.3	8.1	
Real GDP growth (percent)	-1.0	2.2	-2.5	3.9	3.3	3.2	3.3	3.1	
Real oil GDP growth (percent)	-1.7	2.3	-6.0	4.6	3.5	3.0	2.8	2.5	
Real non-oil GDP growth (percent)	0.0	2.0	2.5	3.0	3.0	3.5	4.0	4.0	
Fiscal Adjustment Under the Baseline:									
Annual change in overall balance to GDP	-18.9	1.2	0.8	-0.2	-0.2	-0.4	-0.8	0.3	-0.4
Annual change in non-oil primary balance to non-oil GDP	14.8	6.9	1.4	2.5	2.4	2.2	1.7	3.2	13.3
Fiscal Anchor:									
Distance of projected NOBP from PIH (% non-oil GDP)			17.4	17.5	17.7	18.1	19.0	18.1	
Fiscal Reform Scenario									
Overall balance	-0.3	0.8	1.7	2.6	3.4	4.1	5.0	6.1	
Overall balance (after transfer to FGF and excl. inv. income)	-17.5	-17.6	-15.9	-14.5	-13.3	-12.1	-10.7	-9.0	
Non-oil primary balance									
(Percent of non-oil GDP)	-87.7	-80.8	-79.4	-75.3	-71.2	-67.4	-63.1	-58.7	
Non-oil primary revenue	3.6	3.6	3.7	3.7	4.2	4.5	5.1	4.9	
Primary spending	52.4	51.4	50.2	48.0	46.6	45.0	43.3	40.8	
Total government debt	4.7	9.9	19.1	27.0	32.3	36.8	40.5	43.4	
Total buffer by the KIA 1/	460.0	470.2	449.5	431.8	413.3	396.6	380.1	364.6	
of which GRF assets	144.0	137.1	126.3	114.9	104.1	94.6	86.1	79.0	
Current account balance	3.5	-4.5	0.3	-0.2	0.2	0.6	0.6	0.5	
International reserves (in months of imports)	6.4	6.8	6.7	6.7	6.7	6.8	6.9	6.9	
Credit to the private sector (percentage change)	7.6	2.9	5.1	7.0	8.0	7.9	8.3	8.6	
Real GDP growth (percent)	-1.0	2.2	-2.5	3.8	3.1	3.1	3.2	3.2	
Real oil GDP growth (percent)	-1.7	2.3	-6.0	4.6	3.5	3.0	2.8	2.5	
Real non-oil GDP growth (percent)	0.0	2.0	2.5	2.7	2.6	3.3	3.8	4.2	
Fiscal Adjustment Under the Reform Scenario									
Annual change in overall balance to GDP	-18.9	1.2	0.9	0.9	0.8	0.7	0.9	1.1	5.3
Annual change in non-oil primary balance to non-oil GDP	15.1	7.0	1.4	4.1	4.1	3.8	4.3	4.4	22.1
Fiscal Anchor:									
Distance of projected NOBP from PIH (% non-oil GDP)			17.4	15.8	14.4	13.1	11.5	9.6	

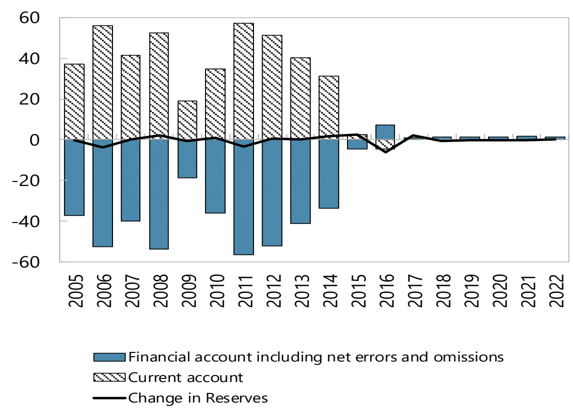
Sources: IMF staff estimates.
1/ Staff estimates and projections.

Annex V. External Sector Assessment

Staff considers the peg to a basket of currencies as appropriate for Kuwait. While the external position in 2016 was weaker than suggested by fundamentals and desirable medium-term policies, the recommended substantial fiscal adjustment over the medium-term would bring the current account broadly in line with the level implied by fundamentals.

Kuwait recorded its first current account (CA) deficit in over a decade last year. The large CA surpluses vanished in the wake of the 2014 oil price shock and turned into a deficit of 4.5 percent of GDP in 2016 driven by further decline in oil prices. The current account is expected to be broadly balanced this year, as the projected rise in oil prices more than offsets the drop in export volumes due to the OPEC+ agreement. The CA is projected to remain broadly balanced over the medium term.

Current and Financial Account Balances
(Percent of GDP)

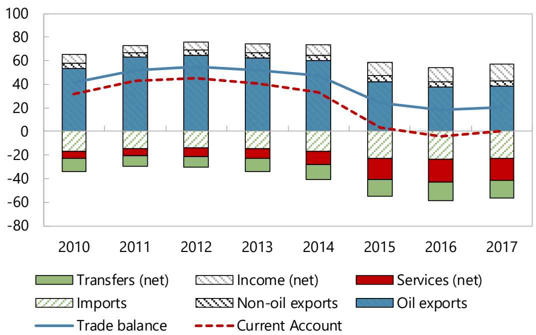


Sources: Country Authorities; and IMF staff calculations.

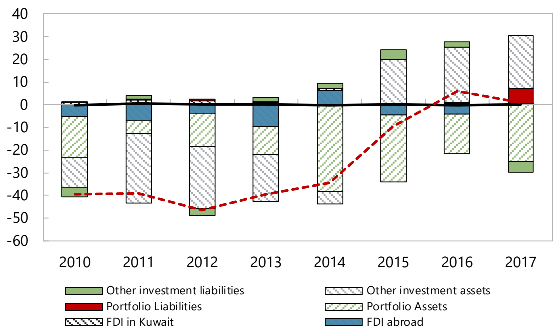
The capital and financial account (FA) balance was positive in 2016. FA balance movements in Kuwait mirror that of the CA as they reflect to a large extent the accumulated (or use of) foreign assets by the Kuwait Investment Authority (KIA). The decline in oil exports and related government revenue have slowed the pace of foreign assets accumulation in the past couple of years, leading to a decline in net portfolio outflows from US$33 billion to US$18.8 billion in 2016. Due to the need to finance the increasing fiscal deficit, other investment inflows continued to increase to nearly US$30 billion, as the government drew down GRF reserves. Overall, financial inflows were larger than the CA deficit, boosting the CBK foreign exchange reserves by US$3.2 billion in 2016. The FA surplus is expected to decline slightly in 2017, due to an improving CA balance.

Contributions to Current and Financial Account

Contribution to Current Account, 2010-2016
(Percent of GDP)



Contribution to Financial Account, 2010-2016
(Percent of GDP)



Sources: Country Authorities; and IMF staff calculations.

Kuwait: Foreign Reserve Adequacy Assessment

	2014	2015	2016	Proj. 2017
	(in millions of USD)			
External short term debt	18014	19797	20658	21991
Other liabilities (portfolio liabs + other invt liabs - STD) 1/	22629	25219	26975	36754
Broad Money	118178	113829	115270	119781
Exports of goods and services	110739	60476	52150	56580
Actual CBK Foreign Reserves	32278	28334	31173	31751
KIA Assets (estimates)	562227	527189	521366	527073
ARA metric	32822	28413	28334	31584
Foreign Reserves as a % of the ARA metric (in percent) 2/	**98**	**100**	**110**	**101**
Foreign Reserves (including KIA) as a % of the ARA metric (in percent)	**1811**	**1955**	**1950**	**1769**
Foreign Reserves in percent of GDP	**20**	**25**	**28**	**27**
Foreign Reserves in percent of broad money	**27**	**25**	**27**	**27**
Foreign Reserves in 3 months of imports of goods and services	**7.4**	**6.4**	**6.8**	**6.7**

1/ Based on SPR's calculation of reserves recommended for fixed exchange rate regimes.
2/ As a rule of thumb, reserves within 100-150 percent of the new ARA metric are considered adequate.

The level of CBK's gross international reserves is consistent with the IMF's standard reserve coverage metrics. Foreign reserves of the CBK reached $31.2 billion (28 percent of GDP, 6.8 months of imports, 27 percent of broad money) at the end of 2016, standing at 110 percent of the Fund's standard reserve adequacy level.[1] Prior to 2015, exports of goods and services and broad money contributed the most to the ARA metric, but since 2015 the share of exports dropped due to the decline in oil prices. As a result, the contribution from the three other components of the ARA metric (broad money, short term external debt, and other liabilities) increased. The reserve level is forecast

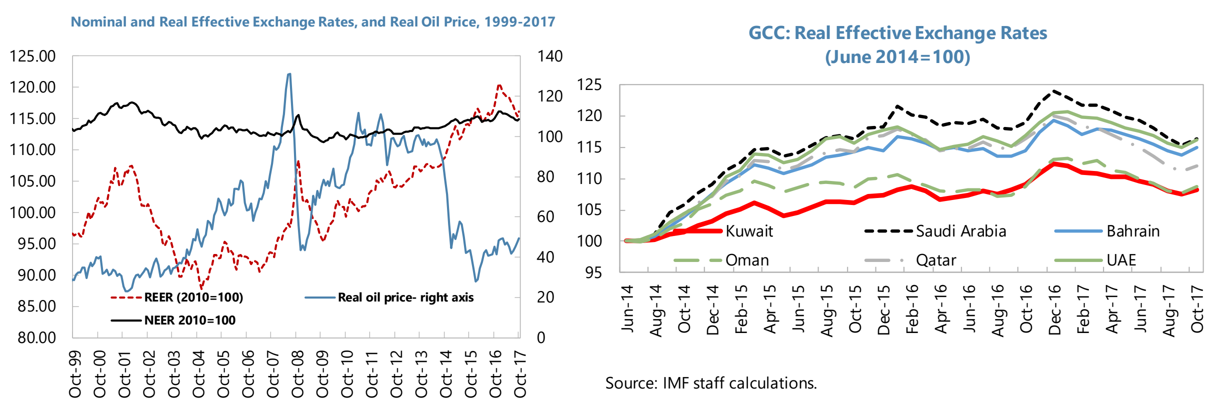
[1] The Fund's composite metric that measures the adequacy of precautionary reserves (developed for emerging markets) calculates the relative risk weights for each source of foreign exchange drain based on the 10th percentile of observed outflows from Emerging Markets (EMs) during exchange market pressure episodes. Reserves in the range of 100-150 percent of the composite metric are considered broadly adequate for precautionary purposes.

to rise to \$31.8 billion in 2017 (about 101 percent of the ARA metric), due to the increase in medium term external debt of the government. The ARA metric adjusted for commodity exporters—which assumes a need to hold additional buffers to account for oil price volatility—puts the adequacy of CBK reserves at about 83 percent in 2016. However, the CBK's international reserves only constitute a small part of country's net external buffers (see below).

In addition to CBK, the KIA also holds a substantial stock of external assets (which staff estimates at about 470 percent of GDP in 2016, with about 320 percent in the FGF and 150 percent in the GRF) on behalf of the government. The bulk of these financial resources, which are mainly invested in foreign assets, are held as savings for future generations, but some can also be used to bolster central bank reserves if needed.

Staff considers the exchange rate peg to an undisclosed basket of currencies as appropriate. The current arrangement, which has been in place since May 2007, has provided an effective nominal anchor. The NEER has remained largely unchanged over the past few years. The REER appreciated between mid-2014 and end-2016, but at a slower pace than in other GCC countries, while it has depreciated in the first half of 2017 in line with the US dollar.

GCC: Nominal and Real Effective Exchange Rates



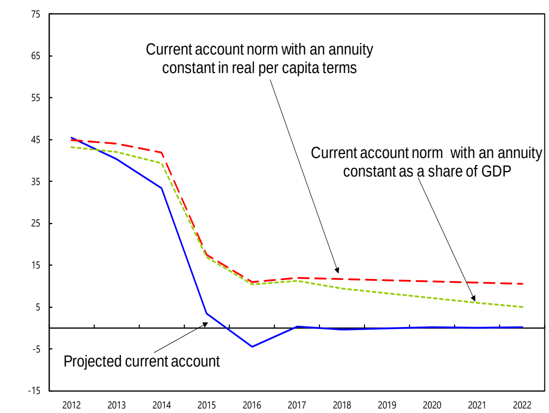
Source: IMF staff calculations.

The external sustainability approach, which in the case of Kuwait is based on intergenerational equity objectives, suggests that the current account balance is too low to provide equitable consumption for future generations. [2] Kuwait is not projected to run persistent CA deficits in the medium term. Hence, the sustainability of the external sector is not driven by the need to stabilize the NFA position as in most other countries, but is rather based on the objective to save oil resources for future generations. The analysis, which builds upon the

[2] The approach calculates the current account required for the net present value (NPV) of hydrocarbon and investment income to equal the NPV of imports net of non-hydrocarbon exports. To support intergenerational equity, the economy would need to choose a path for imports —and hence a current account norm—by accumulating net foreign assets at an appropriate pace. As with any analytical tool, results are sensitive to the choice of assumptions made (for instance, oil prices, return of assets, and population growth) as well as the targeted transfer to future generation (annuity).

the permanent income model (PIH), is the preferred method for analyzing Kuwait's external sustainability, as the CA gap reflects suboptimal saving of hydrocarbon revenues rather than reflecting traditional competitiveness issues. The implied current account norm, as per constant real per-capita annuity, is a surplus of 11.9 percent of GDP in 2017, compared to the baseline current account deficit of 0.1 percent of GDP, resulting in an estimated current account gap of about 12 percent of GDP that is projected to reduce to 10 percent of GDP by 2022. Since this imbalance in Kuwait is largely due to suboptimal saving by the public sector, the current account gap could be closed through fiscal consolidation. Indeed, closing the large PIH fiscal gap (estimated at 9¾ percent of GDP in 2016) over the next ten years would broadly eliminate the estimated current account gap.

Kuwait: Projected and Actual Current Account vs Norms
(Percent of GDP)



Source: Staff calculations and projections

Current and Fiscal Account Actuals and Norms
(In percent of GDP, unless otherwise specified)

External sustainability approach (2017)		
	Annuity real per capita	**Annuity constant to GDP**
Current account projected	0.3	0.3
Current account norm	11.9	11.2
Current account gap	-11.6	-10.9
Fiscal balance norm	10.6	
Actual fiscal balance	0.8	
Fiscal balance gap	-9.8	
EBA-lite approach (2016)		
Current account gap	**No Adj.**	**Ad-hoc Adj.**
Current account actual	-4.5	-4.5
Current account norm	14.8	14.8
Current account gap	-19.3	-8.5
Policy gap	-3.5	-3.5
CA-Fitted	11.2	
Residual	-15.7	
Additional temporary factors 1/		-6.0
Additional adjustments to norm 2/		-4.8
Real effective exchange rate gap	**REER**	**CA**
REER Elasticity (percent)	-	-35.0
REER gap (+ overvaluation, percent)	22.6	24.5

Source: IMF Staff calculations

1/ About 4.2 percent is due to very low oil prices in 2016, relative to current WEO forecasts, while 1.8 is due to possible errors in estimating services flows and non-oil exports.

2/ The adjustment was made to bring the cyclically-adjusted CA norm in line with the PIH norm.

Estimates based on the External Balance Assessment-lite (EBA-lite) methodology also show that the current account balance was lower than the norm in 2016. Imposing a fiscal policy consistent with intergenerational equity—which implies a fiscal balance that is 9¾ percent of GDP higher than in 2016 as per the PIH—brings the current account norm derived from the EBA-lite methodology to about 15 percent of GDP, resulting in a current account gap of about 19 of GDP. The policy gap, however, only explains about 3.5 percentage point of the estimated gap. The large residual (15.7 percent of GDP out of the 19.3 percent of GDP current account gap) appears to be an indication of an assessment method less adapted to undiversified commodity exporters such as Kuwait.[3] Given the large residual, staff has made an adjustment to the EBA-lite CA model, by estimating the impact of temporary and statistical factors on 2016 CA deficit as well as bringing the CA-norm to a level closer to the PIH estimates (to 12 percent of GDP). The adjusted results bring the current account gap to 8.5 percent of GDP, somewhat comparable to the PIH-based results. Assuming standard elasticities, the REER would have to depreciate significantly to close the adjusted EBA-lite CA gap. However, in practice staff is of the view that exchange rate depreciation would have a limited impact on the CA, given the structure of exports, which is dominated by oil. The substitutability of imports by domestic products is also very small, due to significant share of imported labor and intermediate inputs in domestic production, making exchange rate depreciation somewhat ineffective to compress imports. Instead, the CA gap could only be closed by recommended fiscal adjustment.

[3] The macro-balance approach based on the EBA-Lite employs a regression analysis for a large cross-section of countries to predict the current account consistent with a range of structural and policy factors, and estimates the impact of changes in these factors on the norm. While the EBA-lite model has the advantage of multilateral consistency, it is however estimated on a wide group of countries and may not fully capture all features of undiversified commodity exporters such as Kuwait.

INTERNATIONAL MONETARY FUND

KUWAIT

December 21, 2017

STAFF REPORT FOR THE 2017 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

Prepared By

Middle East and Central Asia Department

CONTENTS

FUND RELATIONS

(As of October 31, 2017)

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

General Resources Account:	**SDR Million**	**% Quota**
Quota	1,933.50	100.00
Fund holdings of currency	1777.79	91.95
Reserve position in Fund	156.68	8.10

SDR Department:	**SDR Million**	**% Allocation**
Net cumulative allocation	1,315.57	100.00
Holdings	1,327.80	100.93

Outstanding Purchases and Loans: None

Financial Arrangements: None

Lending to the Fund and Grants: SDR million 341.29 (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, Kuwait's exchange rate arrangement has been a conventional peg against an undisclosed currency basket. 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 January 6, 2017 (SM/17/15—Published January 17, 2017). The staff report is available at http://www.imf.org/en/Publications/CR/Issues/2017/01/17/Kuwait-2016-Article-IV-Consultation-Press-Release-and-Staff-Report-44532

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 since 2004:

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
FAD	Macro-Fiscal Unit (resident advisor)	October 2013
LEG	Central Bank Law	January 2014
FAD	Tax Policy and Administration	February 2014
MCM	Macroprudential Policy	March 2014
FAD	Fiscal Rule	February 2015
STA	National Accounts Statistics	March 2015
MCM	Deposit Insurance System	September 2015
FAD	Tax Policy and Administration	September 2015
LEG	AML/CFT ongoing TA project	May 2012–16
FAD	Establishing a Debt Management Office	November 2015
FAD	Debt Management Strategy	January 2016
MCM	Bank Stress Testing	May-June 2016
FAD	Macro-Fiscal Unit	November 2016
MCM	Crisis Management and Resolution	April-May 2017
FAD	Macro-Fiscal Unit	May 2017

Resident Representative: None

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

RELATIONS WITH THE WORLD BANK

(As of November 12, 2017)

The World Bank and the Government of Kuwait developed a rolling four-year Country Partnership Strategy (CPS), which leverages the setup of a World Bank Country Office in Kuwait (inaugurated in January 2009). The Kuwait program emphasizes implementation of reforms. Hence all activities are grounded in the Government's five-year plan, and are developed closely with the line ministry/agency as well as with the Ministry of Finance, which plays the role of a coordinator and key Bank counterpart. The current Reimbursable Advisory Services (RAS) program is structured around the following four strategic themes under the latest 2016–20 Country Partnership Strategy:

(i) ***Public sector performance and citizen accountability–*** Bank support in this area aims at ensuring that public services are delivered transparently, efficiently and effectively and that citizen accountability is enhanced. Key activities under this pillar include Bank support of a public expenditure and financial accountability (PEFA) project and an engagement to support the development of a guidebook for public private partnerships. Other pipeline engagements focus on providing capacity-building assistance to the Kuwait National Assembly, VAT implementation, as well as Public Financial Management (PFM). The latter is designed as a programmatic multi-year engagement to improve the quality of fiscal policies and the system of procedures governing public financial management in the country.

(ii) ***Private sector development -*** Aims to support reform efforts geared towards transforming Kuwait into a commercial and financial hub with diversified economic activities and the creation of a more conducive business environment for private sector development and foreign direct investment. Bank activities under this theme include: supporting the design and implementation of an insolvency and creditors rights framework, enhancing the institutional effectiveness of the new Competition Protection Authority and providing strategic implementation support to the National Fund for SME Development. Upcoming work for the Ministry of Commerce and Industry has been approved for an analysis of Kuwait trade outcomes in terms of diversification opportunities. Also, at the request of the Minister, a proposal has been submitted for a Kuwait Investment Road Map and Diversification Opportunities for the Kuwait Direct Investment Promotion Authority. In addition, at the request of the Capital Markets Authority, the World Bank has submitted a proposal to provide capacity development support in key institutional areas.

(iii) ***Human development -*** major program to enhance the quality of education as well as support in social protection, labor and health. The education program is the flagship program and has evolved into a $35 million multi-year strategic partnership between the Bank and the Ministry of Education in support of education reforms with emphasis on improving the quality of teaching and learning in schools. The Bank is also preparing large engagements in the areas of labor market reforms and social safety nets.

(iv) ***Infrastructure Development and Urban Management -*** aims to make significant improvements in its infrastructure and urban management sectors including land management and the environment. Current engagements include a multi-year land management modernization project with the Ministry of Finance and the State Property Sector and a disaster risk management project with the Kuwait Institute for Scientific Research. Pipeline activities include support to urban management and e-government services at the Kuwait Municipality.

ONGOING ACTIVITIES FOR FY17 AND BEYOUND

Counterpart Agency – Basic Activity Data	***Activity Description***
I. PUBLIC SECTOR PEFORMANCE & CITIZEN ACCOUNTABILITY	
Ministry of Finance (MoF) PEFA Capacity Building and PFM Reforms (P157053)	The Bank is providing further support on the PEFA framework and in light of the revisions undergone to PEFA.
Ministry of Finance (MoF) Kuwait National ML/TF Risk Assessment (P159136)	The aim of this one-year project is to assist Kuwait's efforts to enhance the capacity of relevant AML/CFT Kuwaiti agencies in carrying out an assessment of money laundering and terrorism financing (ML/TF) risks, and developing risk-based action plans to mitigate these risks, through the Bank's National Money Laundering / Terrorist Financing Risk Assessment (NRA) tool.
II. PRIVATE SECTOR DEVELOPMENT	
Ministry of Finance Insolvency and Creditors Rights – Phase II (P144858)	The Ministry of Commerce and Industry (MOCI) requested World Bank support in improving Kuwait's investment climate. Following a review of the insolvency and creditors rights regime (ICR), the World Bank recommended developing a new set of insolvency laws. The World Bank team supported the preparation of two draft laws on the liquidation and rehabilitation of companies and presented them to the Legal Committee of the Cabinet. Other activities include providing support for the preparation of a secured transaction law and a credit report law – as well as for the development of specialized commercial courts.
Kuwait Direct Investment Promotion Authority (KDIPA) Doing Business Reform (P155328)	In response to a continuing decline in ranking in the Doing Business Report, the Kuwait Direct Investment Promotion Authority (KDIPA) requested the World Bank Group's support on government-led measures to improve the country's business environment in areas measured by the World Bank's Doing Business Report. Their approach to the World Bank was motivated by the Kuwaiti government's own moves towards creating a more open, business-friendly and transparent environment for foreign and local firms to operate and prosper. Therefore, KDIPA led a series of workshops with the support of the World Bank Doing Business team to provide members of the Doing Business committee (Permanent Committee for Streamlining the Business Environment) the opportunity to better understand the Doing Business indicators, methodology and recommendations for reforms in areas measured by Doing Business
The Kuwait National Fund for SME Development SME Fund Support – Phase III (P154183)	Building on the previous Bank engagements with the national SME Fund - Phase I and Phase II - the Bank is supporting the Fund with organizational set-up and the implementation of its strategy (Phase III). The current engagement is focused on supporting: (i) organizational set-up and IT architecture, (ii) the SME business environment, (iii) SME business development, (iv) entrepreneurship culture development, and (v) data collection, and monitoring and evaluation.

Kuwait Competition Protection Agency Phase II: Implementation of Competition Program in Kuwait (P162614)	The goal of the Phase II Implementation is to have, by the end of the program, a fully functional, efficient, and effective Competition Protection Authority capable of carrying out its mandate and able to foster better functioning markets, productivity of firms, better services and prices for consumers, and an overall increase in private sector competitiveness. The four components include: (i) Designing and implementing a model competition framework; (ii) Embedding pro-competition principles in key sectors of the economy; (iii) Fostering agency effectiveness for the CPA; and (iv) Operational Setup, Automation and IT architecture.
III. HUMAN DEVELOPMENT	
Ministry of Education (MOE) School Education Quality Improvement (SEQI) – Phase II (P154848)	This engagement is the flagship project of the Kuwait Country Program and builds on the earlier success of the School Education Quality Improvement (SEQI 1) Technical Cooperation Program, designed to support the Ministry of Education (MOE) and the National Center for Education Development (NCED) in the implementation of a comprehensive education reform program. The current engagement consists of five main components: (i) curriculum development and enhancement; (ii) effective teaching; (iii) school effectiveness; (iv) system accountability and effectiveness and (v) education policy, decision-making and implementation support.
IV. INFRASTRUCTURE AND URBAN MANAGEMENT	
Ministry of Finance (MoF) Program for Modernization of Land Management in Kuwait (P151988)	This engagement builds on an earlier diagnostics phase which supported the State of Kuwait in developing a strategic understanding of the institutional and regulatory issues related to state land policy management. The current multi-year engagement on modernizing land administration builds on the work of this earlier phase and received formal approval from the Ministry of Finance in the third quarter of FY16. The engagement seeks to modernize the land management system in the country.
Municipality of Kuwait Solid Waste II (P122085)	This current engagement with the Kuwait Municipality related to solid waste focuses on: (i) the preparation and the implementation of a national priority project for the closure and rehabilitation of existing dumpsites, (ii) the elaboration and adoption of a solid waste master plan consistent with the Kuwait Land-Use Master Plan, (iii) the completion and harmonization of existing legal instruments, starting with a Solid Waste Law, and (iv) the establishment of a Municipal Solid Waste Agency.
Kuwait Authority for Partnership Projects (KAPP) Public-Private Partnerships Project Guidebook (P157147)	This reengagement with Kuwait Authority for Partnership Projects (formally known as PTB) came about after the PPP law (law 116/2014) and Executive Regulations were passed early 2015. KAPP requested the Bank's urgent support on revising the PPP Project Guidebook that was previously prepared by Aijaz and Paul Noumba in 2009. Overall, the one-year engagement covers 3 main components (i) inception report – comprehensive review of the new PPP law, (ii) Revised Guidebook, and (iii) Consultation and Dissemination of the revised Guidebook.

STATISTICAL ISSUES

(As of October 5, 2017)

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: Kuwait's national accounts are compiled by the Central Statistical Bureau (CSB). A number of areas could be improved based on international best practice, as suggested below. Annual GDP estimates are derived from a benchmark year of 2010 and considered broadly adequate for surveillance. The authorities are encouraged to select and implement a contemporary benchmark to rebase the GDP time series to ensure structural changes in Kuwait's economy are reflected in published estimates. Ongoing efforts to rebase the national accounts using 2013 as a base year are welcome in this regard. The sources and methods used to estimate individual components of GDP should be publicly disclosed to identify areas where further improvement is required. Two areas for improvement are being discussed between the CSB and IMF staff: (i) the methodology used to construct volume movements for subsidies on products, and (ii) the methodology used to aggregate financial services indirectly measured (FISIM) into GDP. A quarterly GDP time series for 2010–17 will be disseminated during 2018. A technical assistance mission conducted in March 2015 provided other recommendations to: enhance source data by improving coordination between government agencies; compile comprehensive estimates of informal activity; and implement methods consistent with international standards.

Price statistics: The Consumer Price Index (CPI) is published on a monthly basis (last observation for August 2017). The weights were revised in June 2017 based on the 2013 Household Income and Expenditure Survey (HIES). The Producer Price Index (PPI) covers selected Mining and Quarrying and Manufacturing industries as well as Utilities. The PPI should be further developed by updating the weights from the 2010 base year, by extending coverage to include services and construction and by compiling separate indexes for the domestic and export markets. Improvements in these dimensions are under consideration in coordination with other GCC countries.

Government finance statistics: Annual GFS data are reported for publication in the *Government Finance Statistics Yearbook (GFSY)*. The major components of extra-budgetary revenues (investment income and transfers of profits of public institutions), extra-budgetary 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. Progress is being made toward improving compliance with the GFSM 2001 guidance, particularly 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 sectoral balance sheet data for the Central Bank, other depository corporations and other financial corporations to STA based on the Standardized Report Forms (SRFs). However, the data submission could be improved as it is not always reported on a timely basis. A future work should be on expanding the coverage of the ODC sector by including investment companies that accept deposits as well as expanding the coverage of other financial corporations (insurance companies and other financial intermediaries).
Financial Surveillance: Kuwait is not reporting financial soundness indicators (FSIs) to STA for public dissemination. The authorities are encouraged to report FSIs for the deposit-taking sectors and other financial corporations.
Balance of Payments Statistics: From 2009 data, the CBK compiles and disseminates detailed annual balance of payments and international investment position data, and from 2015 – quarterly balance of payments data in accordance with the methodology of the BPM6, while trade data estimates are disseminated quarterly by the Central Statistical Bureau (CSB). 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. The information on IIP data made available to staff is incomplete as it excludes the external assets held by the general government (with the exception of loans granted by the Kuwaiti Fund for Arab Economic Development and general government trade credits). This data is expected to be reported to the Fund by the Executive Director for Kuwait at the time of the upcoming Article IV board meeting. 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. Kuwait is successfully reporting inward and outward direct investment data. As for CPIS data, 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, delays and data gaps remain. In particular, coordination among major government entities is needed to provide quarterly data to the CBK in time to compile timely quarterly statistics. Merchandise trade data are compiled monthly and published quarterly and annually by the CBK, monthly and annually by the CSB. The response rate for the private nonfinancial sector is low.

II. Data Standards and Quality	
Kuwait is one of the first GDDS participants. Its metadata were last updated in 2010 and 2011. 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 CSB 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

(Last updated on October 5, 2017)

	Date of latest observation (For all dates in table, please use format (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	Jul 2017	Sep 2017	D	D	D		
International reserve assets and reserve liabilities of the monetary authorities[1]	Jun 2017	Sep 2017	M	M	M		
Reserve/base money	May 2017	Sep 2017	M	M	M		
Broad money	Jun 2017	Sep 2017	M	M	M		
Central bank balance sheet	Jun 2017	Sep 2017	M	M	M		
Consolidated balance sheet of the banking system	Jun 2017	Sep 2017	M	M	M		
Interest rates[2]	Jun 2017	Sep 2017	M	M	M		
Consumer price index	Jul 2017	Sep 2017	M	M	Q		
Revenue, expenditure, balance and composition of financing[3]—general government[4]	Dec 2015	May 2016	M	M	M	Not published on Fund standards	Not published on Fund standards
Stocks of central government and central government-guaranteed debt[5]	Dec 2014	Sep 2015	M	M	M		
External current account balance	Mar 2017	Jul 2017	Q	Q	Q		
Exports and imports of goods and services	Mar 2017	Jul 2017	Q	Q	Q		
GDP/GNP	Dec 2015	Sep 2017	A	A	A		
Gross external debt	Dec 2014	Apr 2015	A	A	A		
International investment position[6]	Dec 2016	Jun 2017	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. Data made available to staff is incomplete as it excludes the external assets held by the general government (with the exception of loans granted by the Kuwaiti Fund for Arab Economic Development and general government trade credits)

[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 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.

Statement by Mr. Hazem Beblawi, Executive Director for Kuwait and Mr. Fouad Al-Kohlany, Advisor to the Executive Director January 12, 2018

On behalf of the Kuwaiti authorities, we thank staff for the constructive Article IV Consultation discussions and for the useful reports. The authorities were in general agreement with staff conclusions and recommendations, particularly, regarding sustaining fiscal consolidation, maintaining financial sector stability, and supporting long-term growth through economic diversification, promoting private sector development, and job creation.

Kuwait's non-oil GDP grew by 2.5 percent in 2017, driven by improved confidence, and is expected to increase further, benefiting from accelerated project implementation. Prudent policies over the past years, guided by the Kuwait Vision 2035 and the National Development Plan, and the accumulation of high financial buffers in two sovereign wealth funds, are enabling Kuwait to continue to support growth in the medium term.

Fiscal Policy and Reforms

Kuwait's fiscal position has stabilized due to a series of policy measures adopted in the past few years. Nonetheless, the authorities are fully aware that continued efforts are needed to preserve fiscal space for growth-enhancing spending, while maintaining fiscal sustainability, recognizing that oil resources are nonrenewable. Accordingly, fiscal consolidation and reforms continue to rank high on their agenda.

To ensure fiscal sustainability, the authorities intend to undertake additional measures to increase non-oil revenues and contain growth in spending. Diversifying the revenue base is a priority for them. Important actions in this regard include increasing the price of government services and the planned introduction of VAT and excise taxes within the framework of a GCC-wide tax reform initiative. On August 2017, the cabinet approved the Unified GCC VAT framework agreement and the Unified GCC Selective Excise Tax Agreement, which are now pending parliamentary ratification. Full implementation of these taxes will not only improve non-oil revenues, but will also strengthen the institutional structure needed to lessen Kuwait's dependence on oil.

Current expenditure was cut by KD 3.25 billion (about 17 percent of non-oil GDP), and capital investment was raised. The cost of subsidies continued to decline as electricity and water prices were raised by about 180 percent between May and August 2017, following a substantial increase in fuel prices starting in 2016. The authorities streamlined current spending, rationalized employment benefits, and improved the targeting of social benefits. They recognize that there is scope for additional consolidation and have already begun to further tighten controls over current transfers, simplify and harmonize the wage structure, and reduce inefficiencies in other current and capital spending with input from the ongoing comprehensive review of spending programs.

The authorities agree that reorienting public expenditure toward capital investment is important to support non-oil growth, improve infrastructure, and encourage productivity gains. Their national development plan includes as a central pillar the scaling up of infrastructure projects. To mitigate against the risk of possible delays in project implementation, the General Secretariat of The Supreme Council for Planning and Development (GSSCPD) monitors and regularly evaluates the implementation progress against key performance indicators and budget. In addition, the GSSCPD regularly publishes updates on projects' status and works with the relevant government agencies to improve the pace and quality of projects' implementation.

The authorities recognize that financing needs remain large in the coming period and take note of staff's recommendation for more ambitious consolidation efforts. Nonetheless, they believe that the adjustment should be carried out at a measured pace to alleviate the potential adverse impact on economic activity and the financial sector. Kuwait's fiscal balance—after transfers to the Future Generation Fund (FGF) and excluding investment income—can improve by about 5 percent of GDP compared to the staff baseline if current oil prices and Kuwait's production levels are sustained in 2018. The authorities expect a more rapid reduction in the government deficit and financing needs, reflecting the different oil price assumptions, and larger expected savings from expenditure rationalization measures.

The authorities are adopting a dynamic financing strategy, striking a balance between issuing external debt, domestic debt, and drawing down the General Reserve Fund. They are also strengthening the debt legal frameworks and related institutions. They established a debt management unit to coordinate the authorities' efforts in this regard, with the objective of maintaining Kuwait's debt sustainability.

They have also made good progress in developing a medium-term expenditure framework. The cabinet approved the implementation of three-year rolling expenditure ceilings and started to put in place a top-down process for budgetary allocations to the line ministries. These measures are strengthening the budget planning and execution processes and underpin the authorities' consolidation plans. The authorities agreed with staff on the importance of maintaining consensus on fiscal reforms. They are exerting a great effort to better communicate the objectives of the reform and cost of delays. They also pointed to Kuwait's vibrant democratic process as a key instrument to build and sustain a wide consensus around important reforms, as evidenced in the comprehensive reform strategy that was adopted and enacted during the recent episode of low oil prices.

Monetary and Financial Sector Policies

The Central Bank of Kuwait (CBK) has aimed to ensure that monetary conditions remain conducive to economic growth and financial stability. The authorities share the staff's assessment that the exchange rate peg continues to serve Kuwait well and provides an effective nominal anchor for monetary policy.

Kuwait's financial sector is sound and stable, with well capitalized, liquid, and profitable banks, whose asset quality is high and non-performing loan ratios are at historically low level. The CBK has taken several important steps on the regulatory front to safeguard the stability of Kuwait's financial sector, starting with enhancing the capital adequacy regime by setting out higher and better quality capital; the CAR of the banking sector stands at 18.3 percent, well above the Basel benchmark. The CBK also set additional capital requirements, up to 2 percent, for systemically important banks. Furthermore, capital conservation buffer and countercyclical capital buffer requirements aim to help banks maintain additional cushion and limit the buildup of systemic risk, and the simple leverage ratio is substantially higher than the global benchmark.

The CBK has weighed the compliance costs of each regulatory measure against its benefits, and regulations are set and periodically reassessed with the goal of not only making the sector resilient, but efficiently resilient. The authorities welcome the staff's assessment that the banking sector is prudently regulated and that the CBK has been proactive in strengthening its supervision. In this regard, the CBK has launched initiatives to identify emerging pressures on the banking sector, including those related to the real estate sector and the impact of U.S. monetary policy normalization.

The authorities appreciate staff's analysis in the Selected Issues Paper on the liquidity conditions and CBK's liquidity management framework. They concur with the staff assessment that banks maintain healthy liquidity and their reserves remain high. They agree that the current amble liquidity environment offers an opportunity to further enhance the liquidity forecasting framework. The CBK is coordinating closely with other stakeholders, including the Ministry of Finance and Kuwait Investment Authority, with whom it exchanges liquidity data and projections on regular basis.

The authorities take note of the staff recommendation to strengthen the crisis management and resolution framework. They aim to further enhance the crisis management and preparedness framework, including by introducing a special resolution regime for banks. Bank deposits are fully guaranteed.

Kuwaiti banks have not experienced withdrawals of correspondent banking relationships. Nonetheless, the CBK took preemptive steps aimed at limiting the risk of withdrawals of CBRs, and actively clarified to banks the international standards and regulatory expectations.

The CBK also maintained open channels of communication between domestic and foreign banks and relevant regulators. Continued efforts aim at strengthening the AML/CFT framework, and Kuwait recently joined the Egmont Group.

Boosting Private Sector Employment

The authorities agree with staff's view that the more constrained budgetary environment puts a premium on structural reforms that promote private sector development, diversification, and job creation. The Kuwait National Development Plan aims to create employment for Kuwaitis through private sector-led economic diversification, improving human capital development, and strengthening institutions.

Small and Medium Enterprise (SME) Development is recognized as a key priority for the authorities. The National Fund for SME Development, and the supporting legal and institutional framework, are key parts of the authorities' effort to support the creation of jobs for Kuwaitis in the private sector. The National Fund helps Kuwaiti entrepreneurs in more than just funding their business ideas, but also providing a host of services, including working with business development centers and universities in business incubation, capacity building, and encouraging better integration of SMEs into supply chains.

The ongoing business environment reforms have helped to improve Kuwait's ranking in the Doing Business Indicators. Achievements include the shortening of the time required to start a business, and shrinking the number of procedures needed to start a business or register a property.

The authorities established a one-stop-shop for investors and started an online establishment and registration of companies. They are committed to continue reforming the business environment, enhancing public private partnerships, and creating incentives for entrepreneurship, fostering productivity and competitiveness, and encouraging private initiative and investment. In this regard, their actions will include facilitating access to finance and land, and reducing the burden of administrative procedures.