



KUWAIT INVESTMENT AUTHORITY,  
KUWAIT FUND FOR ARAB ECONOMIC DEVELOPMENT &  
OLIVER WYMAN JOINT COMPANY

# KUWAIT IN TRANSITION: TOWARDS A POST-OIL ECONOMY

## **AUTHORS**

Antonio Carvalho  
Jeff Youssef  
Joel Ghosn  
Lara Talih

## **CONTRIBUTORS**

Nicolas Dunais  
Jimmy El Gemayel



# ABSTRACT

Following the 2014 rout in oil prices, GCC economies have been struggling to adapt to the new oil reality. GCC countries experienced a direct hit on their fiscal balances as government expenditure had not been adequately controlled following years of abundant spend. With future deficits looming, Kuwait has followed the regional trend of pursuing economic and fiscal reform programs. These programs are comprised of multiple initiatives that seek to support economic diversification, strengthen private sector contribution to the economy and help maintain the deficit under control.

# EXECUTIVE SUMMARY

The discovery of oil in 1937 paved a path of socio-economic prosperity in Kuwait. Since then, the country's growth has primarily been driven by the petroleum industry, fuelling investment in public infrastructure and the development of the public labour force. The growth of the public sector has however come at the expense of private sector development, to the extent that private sector work and entrepreneurship practices are considered an exception in one's career. This has historically resulted in large economic imbalances; the public sector accounted for more than half of Gross Domestic Product (GDP) and around 90%<sup>1</sup> of state revenue came from oil exports.

The end of the last oil boom, followed by the normalization of the barrel price in 2014, have exposed the GCC's vulnerable oil dependency. Kuwait, in particular, suffered a deficit equal to 13% of its GDP in fiscal year 2015/16 - down from a fiscal surplus of 27% in 2013/14<sup>2,3</sup>. With no change in approach, it is expected that Kuwait will accumulate more than USD 75 Billion<sup>4</sup> of deficit in the next four years<sup>5</sup>.

Nevertheless, Kuwait remains in an economically favourable position. In addition to its extensive oil reserves, the country maintains large sovereign wealth reserves, significant treasury funds and a favourable access to debt markets to withstand the current hardships. Developing the rational strategies today and implementing them in the years ahead will ensure Kuwait emerges from the current situation in a considerably stronger position. The current hardships indeed provide a platform that could be the catalyst for embracing the transformation required to diversify the country's economy.

The National Program for Economic and Fiscal Sustainability (EFS) outlines concrete plans on how to transform the national economy through developing the private sector and reducing the fiscal deficit. Launched under Kuwait's national 2035 vision, "NewKuwait", EFS aims to dramatically improve the business environment, boost the private sector by enhancing foreign and local investments, vitalize the labour market, reduce fiscal imbalances by rationalizing government spend and increase non-oil revenue.

There are many challenges, however, in achieving the transformation required. Prior to 2014/15, Kuwait enjoyed sixteen consecutive years of fiscal surpluses, projecting an impression of unlimited abundance to government officials and citizens alike. Altering this perception and conveying the necessity for change will require significant efforts. In particular, such efforts will also have to be directed at Kuwait's National Assembly, whose directly-elected members have the power to block or influence many of the reform initiatives. Consequently, a national consensus on how to address the current situation is critical. This can only be achieved by involving different stakeholders in the process of developing and implementing the reform plan. Other challenges are likely to persist for several years, including motivating citizens to embrace self-reliance and aligning education and skills to the needs of an emerging private sector.

The current economic and fiscal challenges present an immense opportunity for Kuwait. Implementation of reforms will develop more efficient institutions and, ultimately, create a more dynamic and prosperous economy. If adequately managed, these challenges will help build a more sustainable future for Kuwait and its people.

1. Central Statistics Bureau and Kuwait Ministry of Finance

2. Oxford Economics

3. Excluding transfers to Kuwait's Future Generation Fund

4. Oliver Wyman analysis, excluding transfers to Kuwait's Future Generation Fund and excluding impact of current reform measures

5. For fiscal years 2017/18 until 2020/21

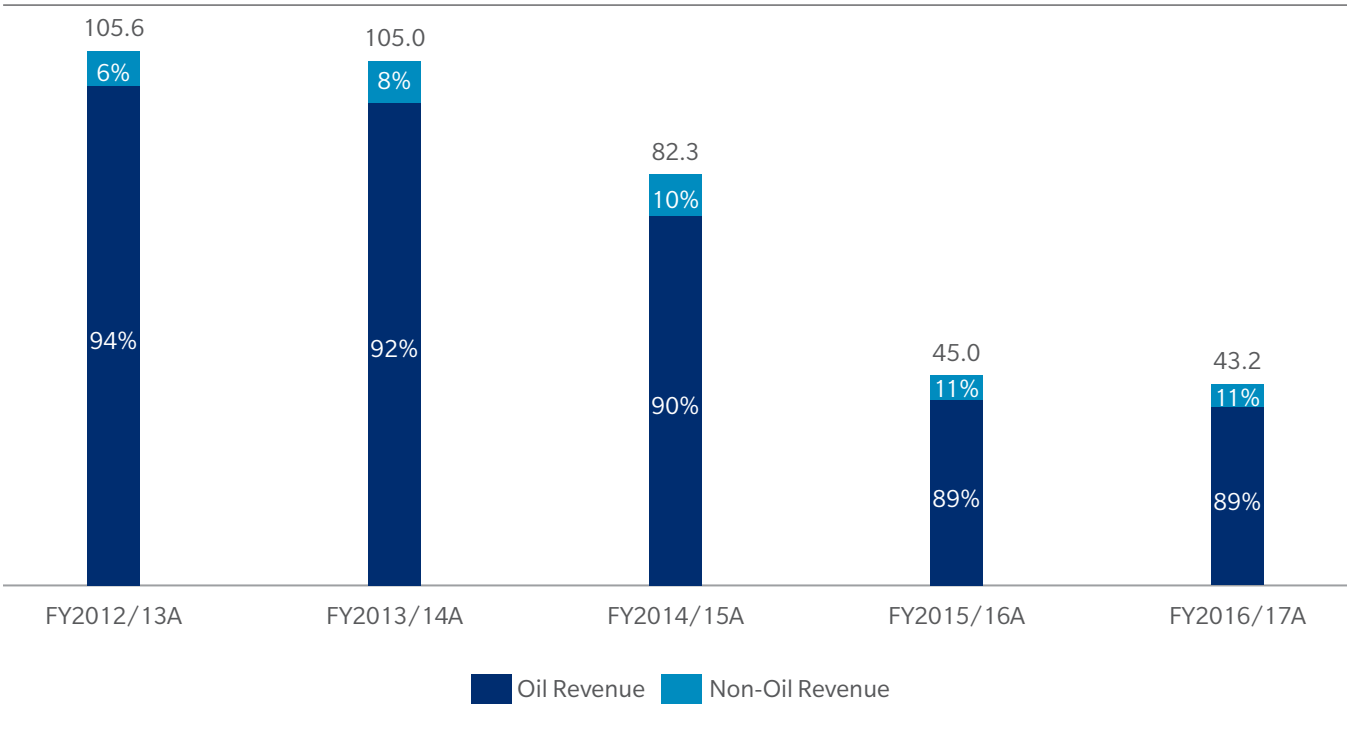
# 1. OIL-DRIVEN WELFARE STATES – AN OBSOLETE MODEL?

## 1.1. KUWAIT: A HIGHLY OIL-DEPENDENT ECONOMY

From its historically commercial role as a trade-port in the Gulf, Kuwait entered its “Golden Era” post-World War II. In 1937, large oil reserves were discovered in the Burgan field, igniting a flurry of capital investment which, in turn, paved the path to socio-economic prosperity. Oil revenue rose significantly in the following decades, attributable to growth in production and market price. The country was subsequently able to develop its infrastructure and redistribute part of its newfound wealth to citizens through various benefits. Oil revenue led to surpluses in the nation’s fiscal balance and gave birth to one of the oldest sovereign wealth funds in the world, with current assets estimated at well above USD 500 Billion<sup>6,7</sup>.

The nation currently relies heavily on oil. With 6.2%<sup>8</sup> of the world’s proven oil reserves, Kuwait ranks 6<sup>th</sup> globally. Kuwait is also the 9<sup>th</sup> largest oil producer in the world, producing at a rate of 3.0 million barrels per day<sup>9</sup> in 2016. As a result, the bulk of government revenue is generated by oil<sup>10</sup>, a level that has remained relatively unchanged in the past 6 years (**Figure 1**). The government-owned Kuwait Petroleum Corporation (KPC) controls the entire Oil and Gas industry in Kuwait and drives the majority of the nation’s GDP and exports, with levels up to 50% and 91%<sup>11</sup> respectively.

**FIGURE 1: GOVERNMENT REVENUE BREAKDOWN (USD BILLION)<sup>7</sup>**  
[KUWAIT MINISTRY OF FINANCE]



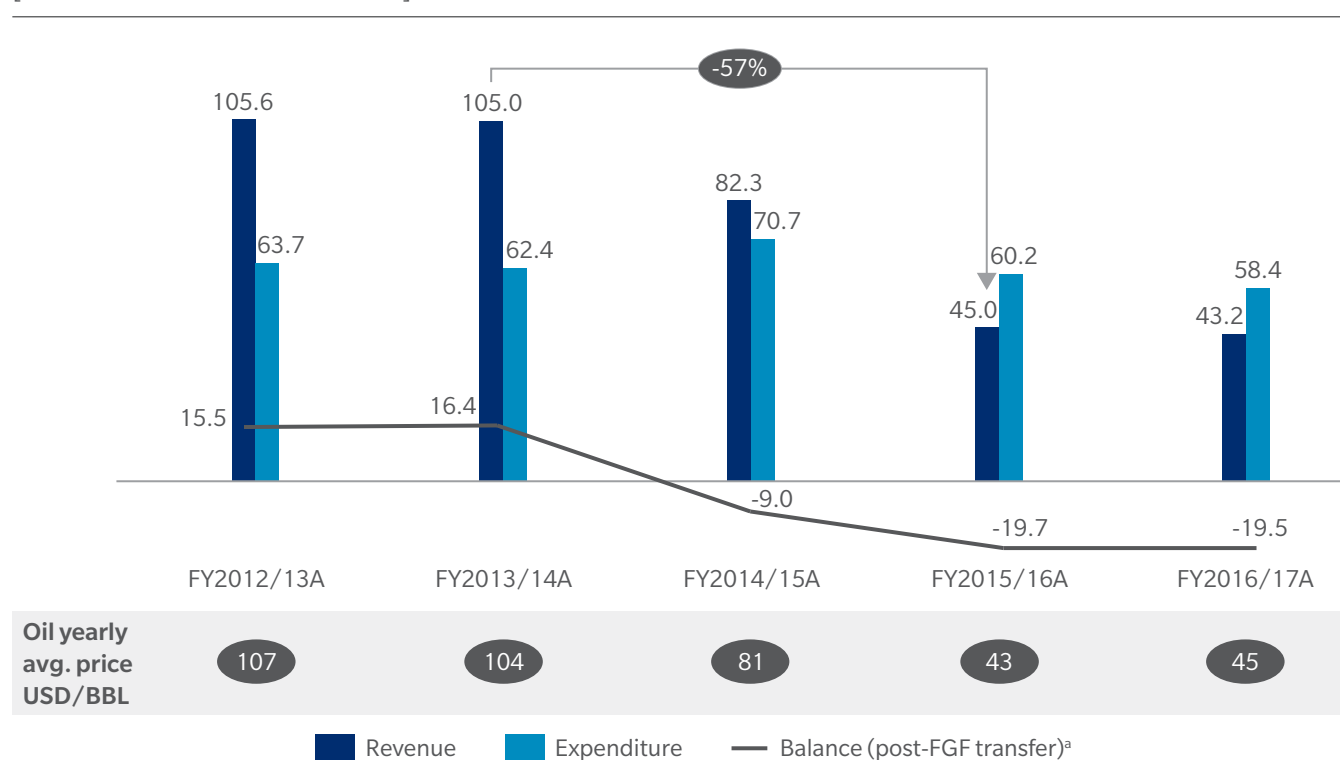
## 1.2. THE END OF THE GOLDEN ERA

The recent sharp decline in oil prices has shaken Kuwait's comfortable fiscal position. From a peak of well-above USD 100 per barrel<sup>12</sup> in Q2 2014, oil market prices fell below USD 30 per barrel in Q1 2016. The barrel has since maintained a USD 45-55 price range<sup>13</sup> - slashing Kuwait's revenue by around 60% between end of fiscal year 2013/14 and 2015/16 (Figure 2).

The unexpected fall in crude oil prices arrived at a time when government expenditure was in full swing. Between FY2012/13 to FY2014/15, government

spend rose to a high of USD 71 Billion in March 2015<sup>14</sup>. Government spending included investments in infrastructure and recurring costs such as generous social benefits and subsidies to the general population, and maintained an oversized and at times inefficient public sector. As a result, Kuwait's hydrocarbon-based economy experienced its first fiscal deficit in 15 years - with a budgetary shortfall of USD 9 Billion, after to transfers to Kuwait's sovereign wealth fund, the Future Generation Fund (FGF)<sup>15</sup> (Figure 2).

**FIGURE 2: GOVERNMENT REVENUE AND EXPENDITURE EVOLUTION (USD BILLION)**  
[KUWAIT MINISTRY OF FINANCE]



a. Transfers to the Future Generation Fund are respectively 25%,25%,25%,10%,10% for the FY 2012/13, 2013/14, 2014/15, 2015/16, 2016/17

6. Sovereign Wealth Fund institute (June 2016)

7. Foreign exchange rate is based on June, 2017 figure of 3.3 USD to 1 KWD

8. Central Intelligence Agency Factbook (2015)

9. Kuwait Petroleum Company production for year 2015/16

10. Around 89% to 90%, Kuwait Ministry of Finance

11. Average over 2013-2016, IMF article IV 2016

12. Oil prices shown throughout this publication are for Kuwaiti Crude (KEC), which trades historically lower than Brent

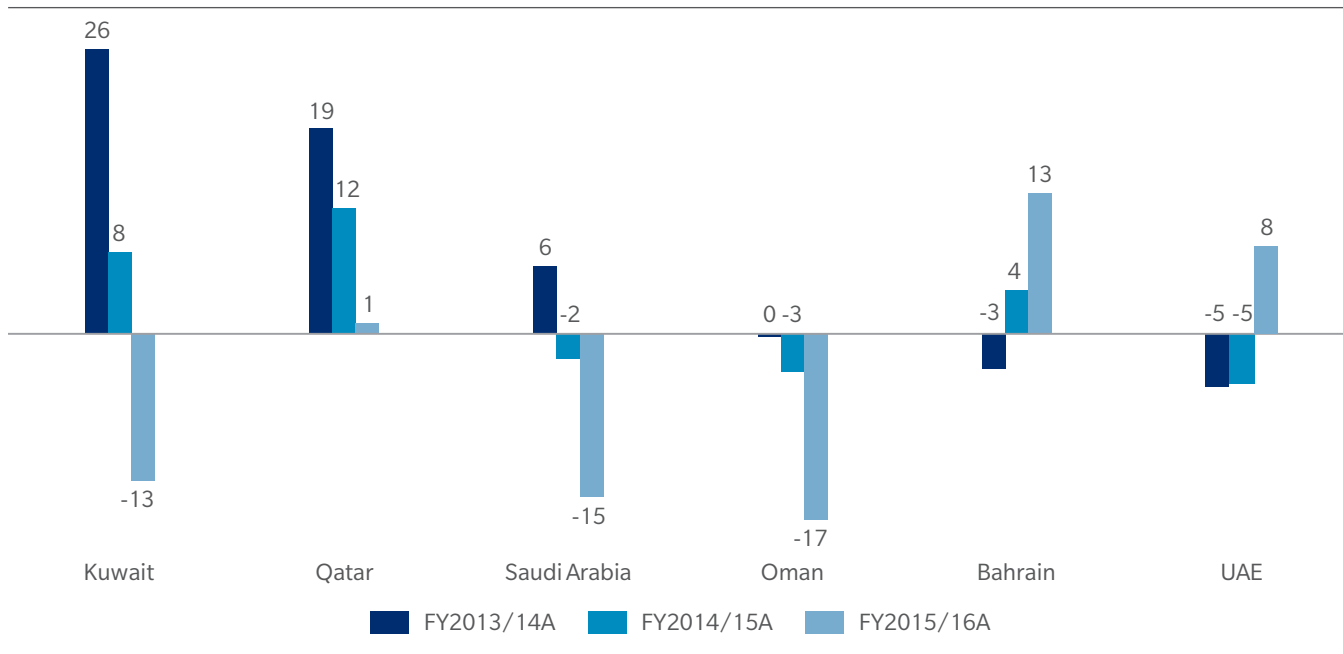
13. Energy Information Administration (2017)

14. Excluding transfers to Kuwait's Future Generation Fund

15. Unless otherwise stated the State's fiscal balance includes a 10% transfers to the Future Generation Fund

Similar to Kuwait, neighboring oil-rich GCC countries are experiencing unprecedented fiscal challenges. In Saudi Arabia, 2015/16 deficits reached over USD 95 Billion or 15% of GDP (Figure 3). These challenges thus heighten both the individual and regional urgency to react.

**FIGURE 3: FISCAL BALANCE IN GCC COUNTRIES AROUND THE OIL PRICE SHOCK (%GDP)**  
[OXFORD ECONOMICS]



### 1.3. THE ROOT CAUSES

The public sector wage bill accounts for the largest portion of Kuwait’s government expenditure, and has been growing at an 8% annualized rate between 2012 and 2015. In FY2016/17, around USD 35 Billion of expenditure were linked to government wages, constituting around 55% of the state’s total expenditure<sup>16</sup>. The wage bill consists of basic salaries, allowances, and other payments such as end of year bonuses and contribution to social security. Its structure has been clouded by ever-rising types of allowances for the public sector, which soared from 21 in 1960 to over 200 to date (Box 1).

Historically, the second largest driver of government expenditure is the generous allocation of government subsidies including fuel, electricity, water and food staples. Subsidies represent 22% of government spend<sup>17</sup>, with average annual benefits of approximately USD 10,000 per capita, out of which USD 2,500 are fossil-fuel subsidies<sup>18</sup>, ranking 2<sup>nd</sup> highest worldwide, after Qatar.

The GCC collectively represents approximately 0.7% of the world’s population yet provides 23% of the world’s oil, electricity and gas subsidies. In Kuwait, total direct

#### BOX 1: WAGE BREAKDOWN OF PUBLIC SECTOR IN KUWAIT

The basic salary of a government employee was defined by law in 1979, with an annual growth capped at ~USD 33 (KD 10) per year, and has not been amended since. To sidestep the law’s strict definition of salaries, public sector wages have increased through the issuance of numerous new wage allowances, which now exceed 200 different allowances, making compensation comparison between entities and employees anything but straightforward.

16. Kuwait Ministry of Finance

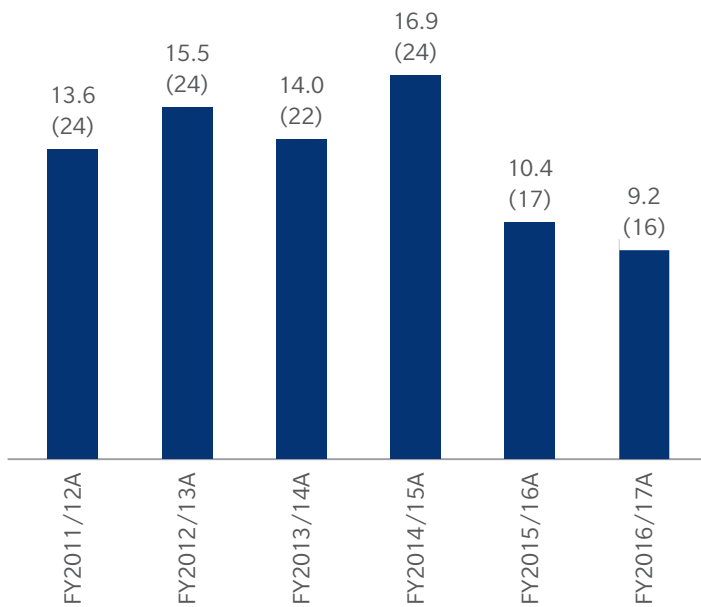
subsidies represent a cost of nearly 10% of the nation's GDP- corresponding to approximately USD 10.4 Billion for fiscal year 2015/16 (Figure 4)

**Capital expenditure (CapEx) and operating expenditure (OpEx), while remaining relatively controlled, both show inefficiencies and suboptimal spending.** CapEx remains a key spend area,

showcasing the government's commitment to develop the nation's infrastructure. Still, budgets are not always channeled to projects of true necessity and priority. Similarly, decentralized decision making, fragmented vendor relationships and lack of unified guidelines and indicators have been inflating OpEx spend beyond true needs.

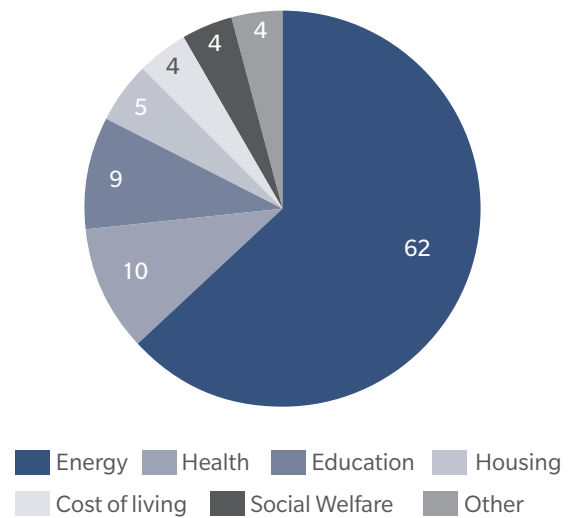
**FIGURE 4: SHARE OF SUBSIDIES IN STATE BUDGET (USD BILLION, % OF BUDGET)**  
[KUWAIT MINISTRY OF FINANCE]

**SUBSIDIES EVOLUTION AS SHARE OF TOTAL BUDGET**  
USD BN (% OF GOVERNMENT EXPENDITURE)



**SUBSIDIES BREAKDOWN**

%AVG. OF SUBSIDIES EXPENDITURE, FY2011-17A



## 1.4. THE CHANGE IMPERATIVE

The current run-rate of government expenditure and revenue is unsustainable. Numerous experts currently forecast an average oil-price of USD 43-66 per barrel over the next five years (Figure 5) with recent economic developments pushing forecasts downwards. Unless the situation is addressed, it is expected that Kuwait's fiscal deficit will continue to accumulate with a potential cumulative shortfall of higher than USD 75 Billion by the end of fiscal year 2020/21<sup>20</sup> (Figure 6).

Kuwait's oil dependency has been a source of profits but not as much prosperity – stricken by the proverbial "oil-curse". The national population has been accustomed to a welfare state granting unrestrained benefits stymying the development of the private sector and non-oil industries. The time to act is now. Kuwait's oil price slump must stand as a catalyzer to its long-needed transformation into a more balanced and sustainable economy, thus preventing the depletion of its accumulated assets and wealth.

17. Kuwait Ministry of Finance, average across 2012-2016

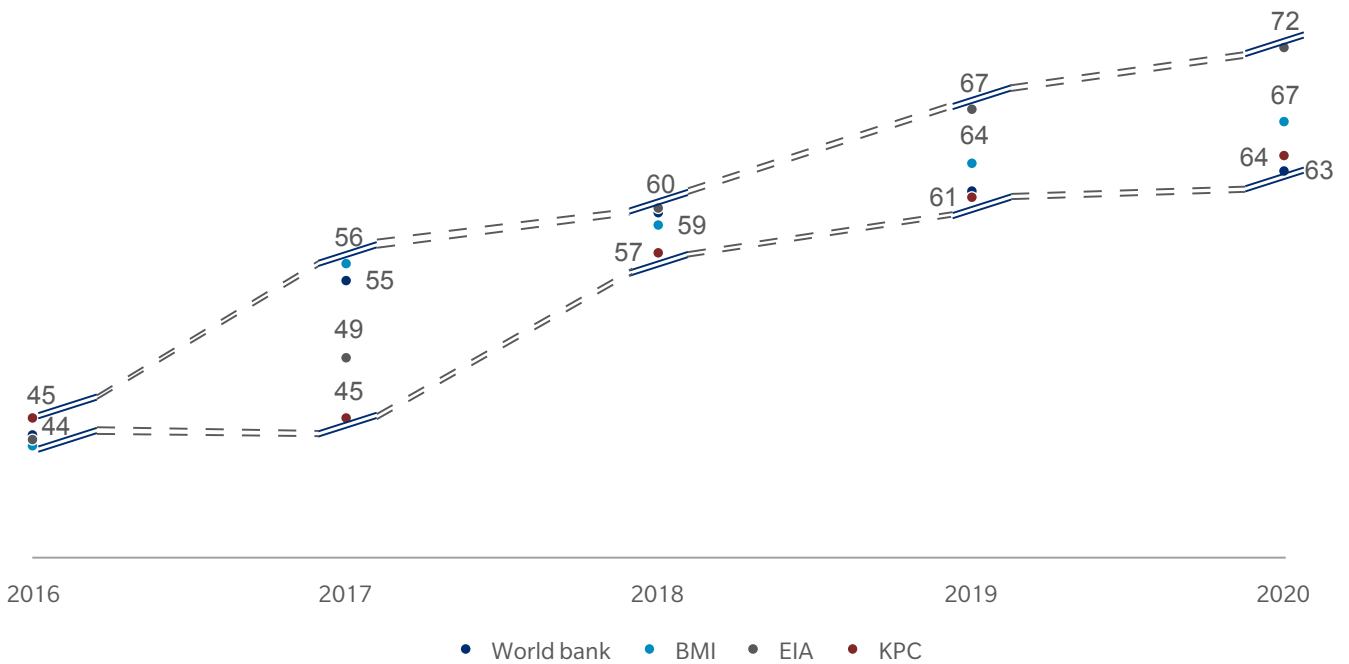
18. IEA/OECD fossil-fuel subsidies database, 2014

19. IEA/OECD fossil-fuel subsidies database, 2014

20. Oliver Wyman analysis, including transfer to Kuwait's Future Generation Fund

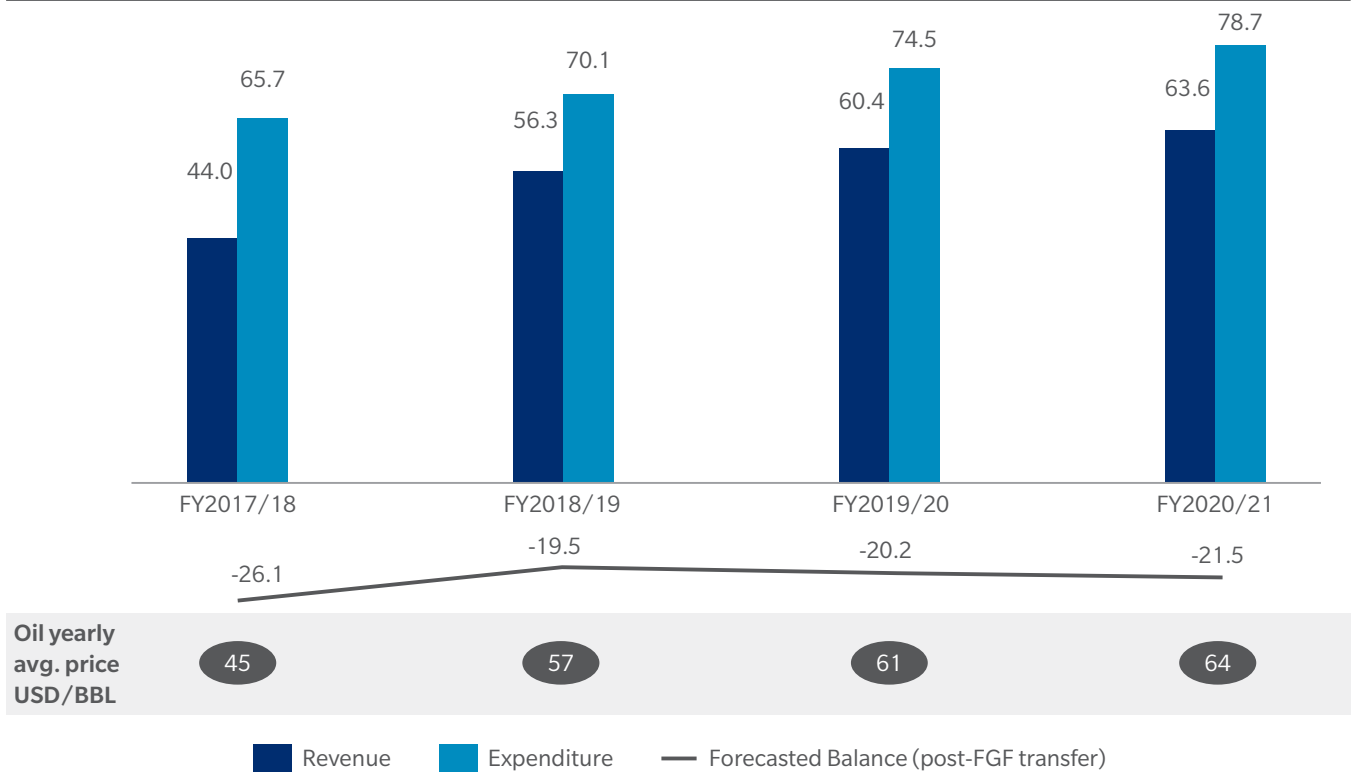
**FIGURE 5: OIL PRICE FORECAST, USD PER BARREL (MARCH 2017)**

[WORLD BANK, BMI, ENERGY INFORMATION ADMINISTRATION, KUWAIT PETROLEUM CORPORATION]



**FIGURE 6: FORECASTED BALANCE<sup>21</sup> – STATUS QUO, INCLUDING TRANSFERS TO FGF (USD BILLION)**

[KUWAIT MINISTRY OF FINANCE]



21. Assumes KPC/MoF oil price projections (March 2017), an oil production of 2.8 mmbbl/day, a 5% increase in gas revenue, a 2.5% increase in cost of oil production, a 5% growth of non-oil revenue and a status-quo increase in expenditure buckets, and no impact of reforms

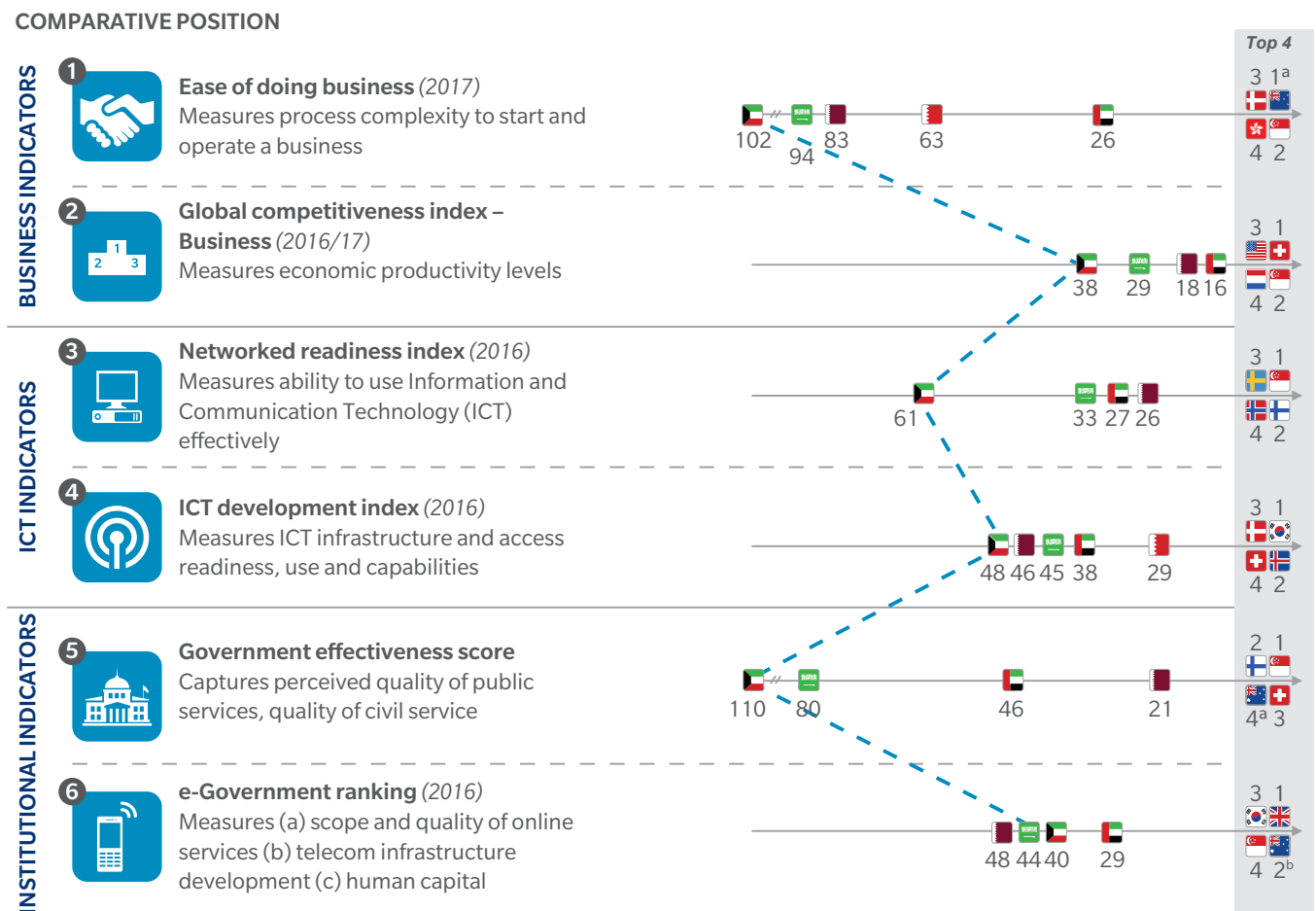


Oil dependency is not the only ailment from which Kuwait suffers. The private sector remains uncompetitive by both global and regional standards. The combination of administrative red tape and heavy regulatory constraints has made both local and foreign investors hesitant to pursue opportunities in Kuwait. Meanwhile, the overly generous public sector has kept Kuwaiti employees away from the private sector, by offering higher job security, greater compensation and better work-life balance.

Consequently, Kuwait's global ranking in competitiveness indicators has suffered. In the World Bank's Ease of Doing Business index, Kuwait ranks 102<sup>nd</sup> out of a total of 190 economies and last among GCC countries (Figure 7). At the time of measurement, the

administrative processes and regulatory requirements to start and operate a business are burdensome and involve multiple procedures and a lengthy time frame. For instance, opening a business takes an average of 60 days, in stark contrast to what it takes in other GCC economies. In comparison to GCC peers, Kuwait fares better in the World Economic Forum's (WEF) Global Competitiveness Index, but was still last in the Institutional sub-metric, and second-to-last in the Business sub-metric of the same index in 2016, ahead of Oman. The same pattern exists in the WEF's Networked Readiness Index and the UN's ICT Development Index, in which Kuwait ranks last or second to last in metrics related to the advancement of its ICT economy. As a result, the private sector's contribution to the economy remains the lowest in the GCC.

**FIGURE 7: KUWAIT'S INTERNATIONAL RANKING IN PERSPECTIVE**  
[VARIOUS SOURCES, 2016/2017]



a. New Zealand, b. Australia

Source: United Nations, WEF, World Bank

## 2. KUWAIT HAS INITIATED ITS TRANSFORMATION JOURNEY

In January 2017, Kuwait launched its development plan entitled “NewKuwait”. NewKuwait envisions a radical shift from the oil-fuelled and public sector-driven expansion, which has characterised the country’s development over the past decades. The plan aims to transform Kuwait from its current status into a regional financial, cultural and institutional hub by 2035. The objectives of NewKuwait derive from the vision of His Highness the Emir Sheikh Sabah Al-Ahmad Al-Jaber Al Sabah:

*“[To] transform Kuwait into a financial and trade centre, attractive to investors, where the private sector leads the economy, creating competition and promoting production efficiency, under the umbrella of enabling government institutions, which accentuate values, safeguard social identity, and achieve human resource development as well as balanced development, providing adequate infrastructure, advanced legislation, and an inspiring business environment.”*

Unlike previous attempts, NewKuwait was launched as a concerted effort involving all members of the government. This national plan created a clear sense of government ownership by involving different ministers and enforcing accountability for their respective development areas.

New Kuwait also followed with a concrete medium-term national transformation program with specific initiatives (highlighted in its seven-pillar framework<sup>22</sup>). Notably, The Economy and Public Administration pillars introduce a three-pronged approach for transformation:

- I. **Defining medium-term economic objectives and targets:** While oil reserves remain substantial, the objective is to ensure a smooth yet decisive transition from the current economic model. The government’s 2035 Vision sets long-term

objectives for the “post oil” era; however, shorter objectives ensure transformation targets remain not only ambitious but also realistic.

- II. **Launching an economic and fiscal reform program:** In 2016, Kuwait’s Council of Ministers introduced a reform plan entitled the National Program for Economic and Fiscal Sustainability (EFS). The program is presently driven by the Economic Affairs Committee (EAC), which consists of five Ministers: Finance, State for Economic Affairs, State Service Affairs, Commerce & Industry and Oil. Before launching the EFS, the EAC partook in numerous alignment meetings with stakeholders in the government and the civil society in an effort to develop a program reflecting the vision of all the involved parties. The newly introduced EFS builds upon the vision set out in NewKuwait and includes existing reform initiatives introduced as early as 2015.
- III. **Defining and executing a debt strategy to support the State’s financing needs:** Under the Ministry of Finance, a joint management structure (Central Bank, Kuwait Investment Authority, Ministry of Finance) was set up to coordinate macro-economic policies and build required capabilities to issue and monitor debt for the State of Kuwait.

In light of current fiscal challenges, all oil dependent GCC countries have initiated similar programs and measures to transition into a more solid economic model.

22. The seven pillars of NewKuwait are: Global Position, Infrastructure, Human Capital, Public Administration, Healthcare, Economy, and Living Environment: [www.newkuwait.gov.kw](http://www.newkuwait.gov.kw)

## 2.1. THE NATIONAL PROGRAM FOR ECONOMIC AND FISCAL SUSTAINABILITY (EFS)

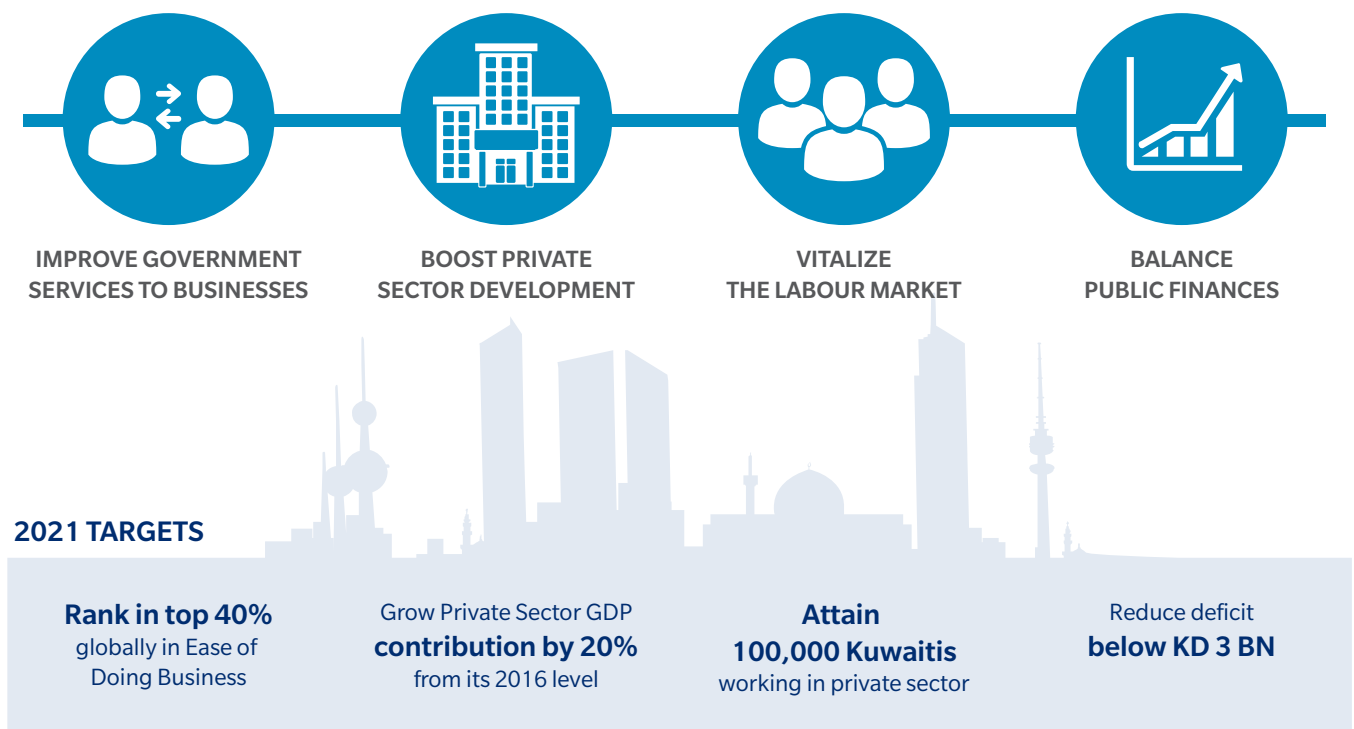
The National Program for Economic and Fiscal Sustainability (EFS) is an overarching program with two key objectives: (1) diversify the economy and notably increase the private sector’s contribution to GDP and (2) reduce the state’s fiscal deficit. Although launched under the umbrella of NewKuwait, EFS incorporates spend-rationalization and other labour reform measures that were initiated as of 2015.

The program reflects the economic imperatives of the country with a strong focus on the development

of the private sector and the overall economy while also addressing citizen concerns. EFS was developed following a rigorous effort to collect views from a wide section of civil society (e.g. non-governmental organizations, economic experts, etc.) and incorporate feedback into a nationwide program. The plan spans across four main themes, each paired with an ambitious overall target (**Figure 8**). The success of each of the initiatives is then assessed against its respective target, in both the short and medium term.

**FIGURE 8: OVERVIEW OF THE NATIONAL PROGRAM FOR ECONOMIC AND FISCAL SUSTAINABILITY**  
[ECONOMIC AFFAIRS COMMITTEE, COUNCIL OF MINISTERS]

### THEMES



## 2.1.1. IMPROVE GOVERNMENT SERVICES TO BUSINESSES

The first step for private sector growth is to lift several of the existing barriers to start and expand businesses in Kuwait. Many of these barriers relate to basic components of the World Bank's business environment index such as: processes for starting and administering a business, obtaining building permits and land allocations, trading across borders, as well as better regulating insolvency and competition.

The Kuwait Direct Investment Promotion Authority (KDIPA) has taken an active role in identifying the key bottlenecks in Kuwait's business environment and, in turn, coordinating projects to mitigate their effects. KDIPA has set a target to improve Kuwait's global position in the World Bank's Ease of Doing Business Index, from 54<sup>th</sup> percentile in 2017 to a 40<sup>th</sup> percentile by 2021, in conjunction with more than five different government entities<sup>23</sup>.

Changes to the regulatory and legislative business environment are also underway. Kuwait currently ranks poorly on the World Bank's Regulatory Quality Indicator

(lowest amongst the GCC) highlighting ineffective enablement of regulation and policy formulation in various industries. The EFS aims to conduct a detailed regulatory assessment of the policies and institutions by sector, to identify and address the existing regulatory gaps in the country. On the other hand, changes in the legislative framework are ongoing and include laws for intellectual property rights, commercial registration, insolvency, creditors' rights and others. Legislative and regulatory reforms are critical to create a transparent, competitive and fair environment where both national and international companies can co-exist and thrive.

In addition to enhancing services to businesses, the government is reassessing means to streamline service provision to citizens, through improving processes and reducing service lead times. Kuwait's Central Authority for Information Technology is leading the national e-Government vision not only to improve and increase e-services offered to citizens, but also to create a citizen centric e-Government.

## 2.1.2. BOOST PRIVATE SECTOR DEVELOPMENT

The second theme of the program aims to foster the expansion of the private sector. The approach includes developing the ecosystem for Small and Medium Enterprises (SME), expanding Foreign Direct Investment (FDI) inflows to the country, launching Public-Private Partnerships (PPP) projects, privatizing state-owned enterprises and revamping industrial grants.

At present, developing the SME sector is a core objective of the government. Established in January 2016, the National Fund for Small and Medium Enterprises and the Industrial Bank of Kuwait dedicate a pool of USD 6.5 Billion to fund SMEs. These dedicated entities aim to create an attractive ecosystem for Kuwaiti entrepreneurs by offering a mentoring, training and support platform, and to foster an adequate culture for the development of SMEs. These two entities combined aim to fund a total of 2,500 SMEs over the next 5 years.

On the other hand, FDI is considered an avenue to attract international enterprises and help build strategic

sectors of the economy, such as the petrochemical and manufacturing industries. KDIPA targets a cumulative amount of around USD 5.6 Billion of inbound FDI by 2021. Another key objective is to connect local SMEs with beneficiaries of the FDI program, thus fostering new relationships and increasing the number of Kuwaiti SMEs in the supply chains of multinational corporations.

In addition, more than 12 PPP projects are in the pipeline and under assessment. These projects are mainly centred on the energy and infrastructure sectors, aiming to build more eco-friendly and efficient power plants, as well as water and solid waste treatment plants. Current PPP projects will not only leverage international best practices, but also create job opportunities in the private sector, foster knowledge transfer and partially alleviate capital and operational costs from the state's budget. The government intends to share project ownership with citizens by awarding 50% of each project to Kuwaitis.

Privatisation also plays a key role in Kuwait's transformation. In an effort to redefine its role in the

23. Ministry of Electricity and Water, Ministry of Justice, Ministry of Commerce and Industry, Kuwait Municipality, General Administration of Customs

economy, the government developed a long term privatization strategy, covering recommendations on assets and services that should be privatized. The government’s primary objective is to accelerate the growth of, and the private sector’s contribution to, the economy. Privatization will also help shift a substantial share of the Kuwaiti labour force from the civil service market to the private sector. Privatization will help transfer inefficient and burdensome assets from the government to the private sector. In so doing, it

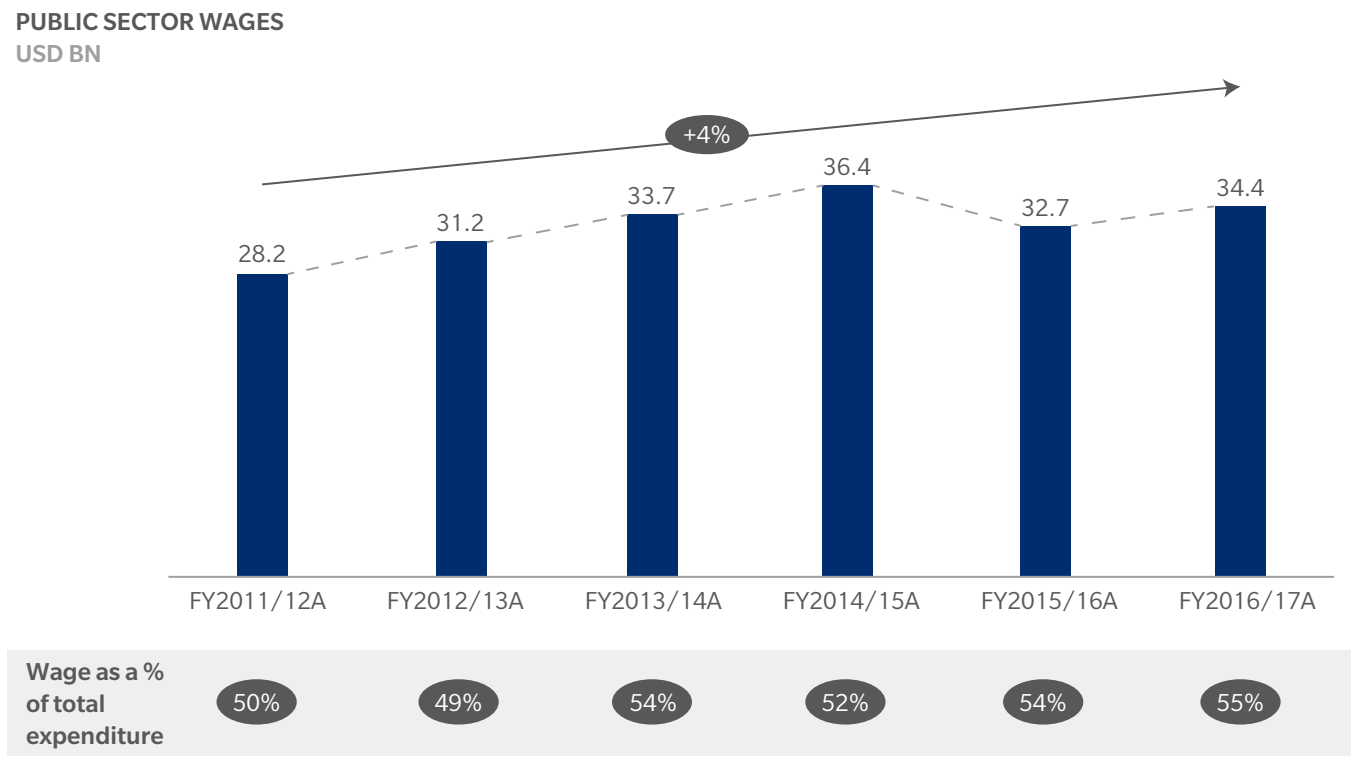
will shift a share of the Kuwaiti labour force from the public to the private sector, thus alleviating the budget expenditure. As such, the immediate focus is centred on infrastructure projects (e.g. ports, airports and broadband network) in an effort to enable the country’s future development. Similarly to PPP projects, special attention has been given to involving nationals in the economy by allocating 40% of the shares of each privatized asset directly to citizens.

### 2.1.3. VITALIZE THE LABOUR MARKET

In order to achieve a long-term shift towards private sector driven growth, both the public sector and private sector labour markets need profound transformation. Particularly, there is an imperative to establish a more balanced employment landscape with regards to the number of Kuwaitis working in the private and public sectors.

At the end of fiscal year 2016/17, more than 85% of the Kuwaiti labour force was employed in the public sector. In terms of government spend, this represented 55% of total expenditure, with expenses growing at a cumulative annual growth rate of 4% since 2011/12<sup>24</sup>. In the absence of change, this rate is expected to remain constant until 2020, driven by a likely overstaffing of government entities<sup>25</sup> (Figure 9).

**FIGURE 9: PUBLIC WAGE BILL, USD BN**  
[KUWAIT MINISTRY OF FINANCE]



24. Kuwait Ministry of Finance

25. A supply of 24,000 graduates each year, out of which more than half are expected to enter the already saturated public sector

Currently, two key factors drive labour market imbalances. On the one hand, nationals are disinclined to work for the private sector. The public sector offers better job security, a comfortable work-life balance, and competitive salaries. On the other hand, private sector employers prefer hiring an expatriate workforce, which is cheaper and committed in the absence of employment alternatives.

To achieve a new employment balance between the private and public sectors, particular effort will be required in changing the mindset of Kuwaitis and promoting the private sector as offering attractive career opportunities. To this end, the government is looking to (i) reform the public labour market by ensuring hires reflect true needs and compensation reflects true capabilities, and (ii) reform the private labour market by incentivizing the employment of nationals and ensuring citizens' skills match market needs.

### (i) Reforming the public labour market

Several measures are being implemented to reform the public labour market. Initiatives are mainly centered on gradually reducing the recruitment of new public sector servants and eliminating non standardized compensation.

Approximately 24,000 nationals enter the labour market every year; close to 18,000 join the public sector<sup>26</sup>. The public sector has historically hired workers well above its needs, with estimates pointing to 60% current overstaffing in some government entities. This practice has led to an oversized public sector, employing around 350,000 civil servants, 74% of whom are Kuwaiti (**Figure 11**). The private sector, in contrast, employs around 1.5 million workers of which only 5% are Kuwaiti nationals<sup>27</sup>.

Existing labour laws in Kuwait and its social contract, prohibit the lay-off of nationals from public sector employment. To contain the financial burden this presents, the government is seeking to limit the flow of new entrants to match its true needs through admission tests and minimum educational requirements. It is estimated that a successful implementation of this suite of measures would contribute to around 20% yearly decrease in new entrants. However, it could only be implemented under sufficient certainty that candidates

could find alternative employment in the private sector.

Wage standardization efforts across all entities are also under way, aiming to foster transparency and fairness. Currently, civil servants with the same profession and grade across different government entities can receive significantly different compensation. For instance, it is not uncommon to find differences of up to 40% in remuneration between two entities<sup>28</sup>. Some entities have thus become "preferred" among job seekers and are in high-demand, leaving the ones offering more modest salaries with a limited pool of candidates. To foster real ambition and career aspirations instead of pecuniary considerations, salaries are being realigned to a standard grid for each group of professions<sup>29</sup>. Unlike common perception, this calibration effort would not result in cuts in employee salaries but rather in a long term raise of "lower than average" salaries.

Wage standardization also involves normalizing allowances and bonuses granted to employees. Years of fiscal surpluses, coupled with decentralized and lenient decision making, created numerous opportunities for civil servant groups to lobby and create special cadres and allowances for their respective professions or entities (**Figure 10**). Currently, public sector employees may be entitled to over 200 different allowances on a monthly basis (**Box 2**). Such allowances represent a total monthly cost exceeding USD 800 Million<sup>30</sup>.

In parallel, bonuses are now considered an integral part of one's wage. Lack of oversight and complacency on government workers' individual job performance has resulted in around 90% of civil servants rated as "excellent performers"<sup>31</sup> during career reviews. Such reviews grant employees maximal bonuses on top of their basic salaries irrespective of actual performance. These issues hinder the government's ability to control and ultimately predict the amplitude and evolution of its wage bill. The government is currently considering freezing the creation of any new allowance or benefit, and simplifying the existing pool by grouping what remains into a coherent and manageable set. The government is also gradually mandating the ranking of employees according to performance and re-linking promotion rules to performance (currently linked to tenure).

26. Civil Service Commission

27. Civil Service Commission

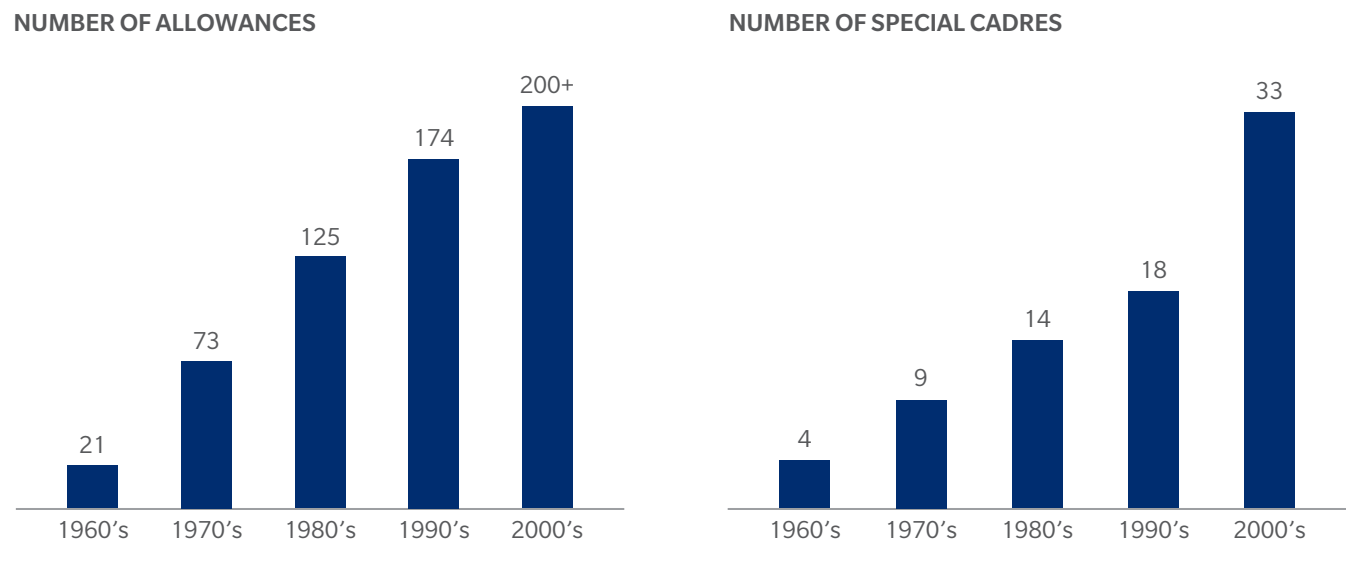
28. Civil Service Commission

29. 7,500 jobs titles are being organized into 9 professional groups, and further split into ~60 individual professions

30. Civil Service Commission database

31. Civil Service Commission database

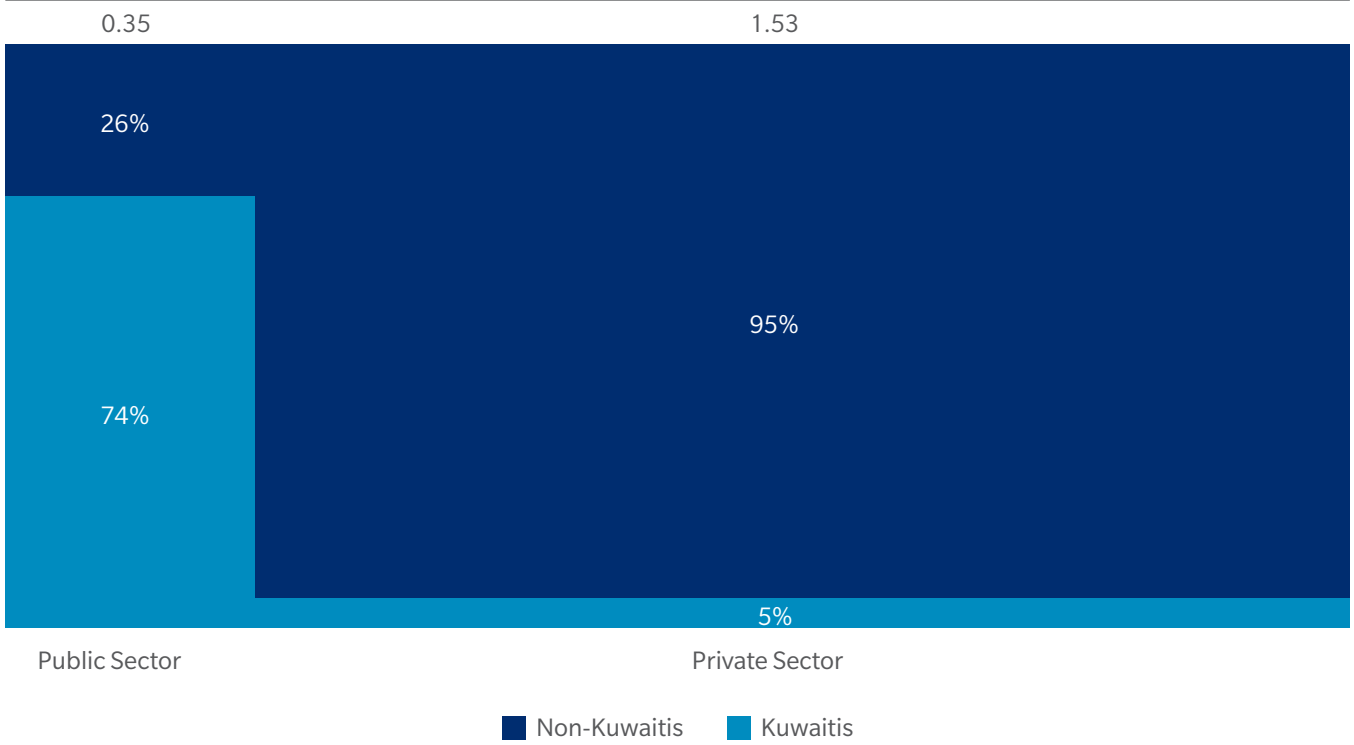
**FIGURE 10: EVOLUTION OF ALLOWANCES AND SPECIAL CADRES**  
[CIVIL SERVICE COMMISSION]



**(ii) Reforming the private labour market**

Reducing the flow of national employees to the civil sector is by no means a sufficient action. Opportunities need to be created in the private sector to absorb this workforce. The private sector is currently dominated by expats and Kuwaitis only account for 5% of employees (Figure 11).

**FIGURE 11: EMPLOYEES BY NATIONALITY AND SECTOR, IN MILLIONS**  
[KUWAIT CENTRAL STATISTICS BUREAU]



The labour market imbalance is driven by four factors outlined below:

- I. Nationals are not incentivized to work in the private sector** as the public sector remains the best alternative for employment. The public sector, for instance, pays an average of 46% more than the private sector on an hourly basis<sup>32</sup>. Additionally, some Kuwaitis are also reluctant to take on professions deemed unfit or degrading<sup>33</sup>.
- II. A large expatriate workforce dominates the private sector** as they are typically less costly for the jobs in demand. The cost of Kuwaitis vs expat manpower makes it economically unprofitable to hire nationals. At present, entry-level Kuwaitis cost employers roughly 40% more than expats<sup>34</sup>.
- III. Labour market governance is not sufficiently centralized** and, as such, a number of financial benefits offered to Kuwaitis in the private sector are currently abused.
- IV. Higher education enrollment by nationals is not aligned** with the needs of the labour market.

To drive Kuwaitization in the private sector, the government is looking at reducing current salary imbalances as well as improving the quality of the national workforce.

In order to reduce imbalances the government is first initiating a preferential recruiting process for select white collar professions for which a high supply of Kuwaitis exists. Work permits for professions such as management, administration and HR professions would be issued only when the employer has proven that no Kuwaiti was found to fill the vacancy. In addition, the government is reassessing the fees for expat employment permits, increasing the cost of foreign labour for the private sector, hence reducing the discrepancy between the cost of hiring expats and nationals.

In parallel, the Kuwaiti government has historically provided substantial financial incentives in the form of monthly pay-outs to nationals working in the private sector as a means to address the salary gap between private and public sectors. This compensation system has seen significant abuse notably through the practice of “phantom” employment: some nationals have colluded with private sector employers to appear on payroll while not doing any work. Through a detailed analysis of entity payrolls, phantom employees are being identified and necessary measures are underway to close those loopholes. In addition to detecting and controlling phantom employment, the government

plans on limiting this compensation to employees earning a salary above a determined threshold. The secondary objective is to then re-channel these savings into increased compensation for professions that have been labelled “unsuitable” for Kuwaitis.

Moreover, the government is seeking to improve the skillset of the Kuwaiti labour force. It is actively orienting students towards education programs that reflect labour market demand to address the mismatch between education and labour market needs. In parallel, apprenticeship programs are being subsidized for applied education students in the private sector to improve their employability through on-the-job training. The Manpower Government Restructuring Program is revamping its current job matching system to ensure that the requirements and skills of both the job seeker and the employer are more closely met.

## BOX 2: EXAMPLES OF ALLOWANCES

### Benefits

- ◆ Social allowance
- ◆ Inflation allowance
- ◆ Job position reward
- ◆ Nature of work
- ◆ Special reward combinable
- ◆ Special reward
- ◆ Children allowance
- ◆ Housing allowance

### Clothing, food and travel

- ◆ Food allowance
- ◆ Driving allowance
- ◆ Seminar attendance allowance
- ◆ Diving allowance

### Compensations

- ◆ Incentive reward
- ◆ Financial reward
- ◆ Late shift allowance
- ◆ Training and education allowance
- ◆ Personal monthly reward
- ◆ Special bonus/ during service

### Medical treatment and tuition

- ◆ Academic qualification reward
- ◆ Academic incentive



## 2.1.4. BALANCE PUBLIC FINANCES

Given the current oil-price outlook, the Ministry of Finance has set a target to reduce the fiscal deficit from its current USD 19.5 Billion in 2016/17 to lower than USD 10 Billion<sup>35</sup> in 2020/21. To this end, the government aims to reduce expenses in the next four fiscal years<sup>36</sup> by a cumulative of around USD 21.5 Billion and raise a cumulative of around USD 4 Billion in additional non-oil revenue, compared to status quo<sup>37</sup>. This target would be achieved through a combination of measures including “cleaning the government’s house”, streamlining subsidies and introducing new sources of revenue. The aforementioned changes to the labour market will also contain the wage bill growth and will hence have a considerable positive impact in meeting this target.

### (i) Rationalizing government spend

Rationalizing public spend involves reducing direct expenditure for government operations and reducing the cost of service provision to citizens without compromising the quality of offered services. At a time of extensive public scrutiny over a perceived waste in public finances, the government must demonstrate its commitment to rein in spending.

Measures are being taken to enforce discipline and control in public spending to help the government “put their house in order”. Top-down budget caps have been introduced at both the state and entity levels (Ministries, Authorities, Councils, etc), and new rules limiting public spend are being drafted and implemented (or enforced where they already exist). For instance, spend on items such as public sector missions, hospitality, conferences, committees and foreign trainings are being reduced. Ongoing spend is being rationalized via a thorough line-by-line spend review: every budget line item is analysed to identify potential cost cutting areas.

The government also aims to control procurement spend, which consists of around 20-30% of the government’s budget. Government procurement in Kuwait is characterized by a somewhat poor demand-planning, non-centralized spend and category management as well as limited procurement monitoring. In parallel, the Ministry is working on controlling the cost of government CapEx through identifying and streamlining projects that are unproductive or exceeding planned budget and timeframe.

The bulk of government savings is expected to stem from the gradual lifting of subsidies covering gasoline, utilities and other consumer staples. Kuwait, until recently, had avoided the GCC trend of partial or full deregulation of prices. The government has now implemented new and partially de-subsidized price levels for gasoline<sup>38</sup> and utilities<sup>39</sup>. The remaining product subsidies<sup>40</sup> are currently under assessment. The government is considering targeted compensation plans either by exempting citizens with less disposable income and/or changing the nature of subsidies from product-based to individual or household-based. Such measures will help improve social justice in the distribution of wealth.

To support the Ministry of Finance’s fiscal initiatives, a set of financial management reforms have been launched. These reforms seek to ensure greater accountability, transparency and predictability in government finances. Measures are being taken to improve budget setting through increased forward-planning. The Ministry of Finance has adopted medium-term (3-year) budgeting approach and has recently deployed the GFMS<sup>41</sup>, a new accounting system that allows more visibility and control on spending items.

32. Manpower and Government Restructuring Program and Public Authority for Manpower

33. Manpower and Government Restructuring Program and Public Authority for Manpower

34. Manpower and Government Restructuring Program and Public Authority for Manpower

35. Kuwait Ministry of Finance , including transfers to Kuwait’s Future Generation Fund

36. Fiscal years 2017/18, 2018/19, 2019/20, 2020/21 for respective oil price forecasts of USD/bbl 45, 57, 61 and 64

37. Kuwait Ministry of Finance

38. Launched as of September 1st of 2016

39. New Electricity & Water prices implementation in May 2017

40. The Kuwaiti government subsidizes products such as housing, education, cost of living, social welfare, etc.

41. Government Financial Management Information System

## (ii) Increasing government revenue

Initiatives from EFS aimed at increasing direct government revenue mainly cover the introduction of tax, the re-pricing of government services<sup>42</sup>, improving revenue collection and divesting underutilized government assets. In the coming years, Kuwait plans to introduce Value Added Tax (VAT) in alignment with the rest of GCC countries.

GCC member states agreed to introduce a VAT in early 2018 and preparations are in full swing. The 5% VAT will apply to the consumption of goods and services; excluding health services and basic goods. Kuwait, however, will likely require an extension to the VAT introduction as the present tax infrastructure, paired with public discontent, requires greater stakeholder alignment and preparation.

**FIGURE 12: LIST OF INITIATIVES OF THE EFS**  
[ECONOMIC AFFAIRS COMMITTEE, COUNCIL OF MINISTERS]

### THEMES

#### IMPROVE GOVERNMENT SERVICES TO BUSINESSES



- Streamline business registration and operations
- Improve land-allocation mechanism
- Streamline goods and passenger flow across borders
- Increase digitalization and government e-services
- Enhance industry transparency and regulatory infrastructure

#### BOOST PRIVATE SECTOR DEVELOPMENT



- Enhance size and quality of Foreign Direct Investment
- Promote and finance Small and Medium Enterprises
- Stimulate Public Private Partnerships projects
- Define privatization plan and implement sales
- Revamp industry subsidy grants

#### VITALIZE THE LABOUR MARKET



##### Public labour market

- Enhance training program
- Improve workforce planning and recruitment
- Develop performance management system
- Normalize job classification and compensation

##### Private labour market

- Incentivize employment of nationals
- Align education with market needs
- Improve labour market governance
- Regulate employment of expats

#### BALANCE PUBLIC FINANCES



##### Control Government Expenditure

- Rationalize government expenditures
- Streamline cost of government projects
- Merge public entities
- Control size of government structure
- Optimize government procurement
- Develop subsidy strategy

##### Increase non-oil revenue

- Improve State revenue collection
- Divest government real-estate assets
- Re-price state land properties
- Re-price public services
- Set-up and launch Tax

### ENABLERS

#### DEVELOP THE FINANCIAL ADMINISTRATION

- Introduce Medium Term Budgeting
- Improve budgeting and accounting system
- Review spending and budgeting procedures

#### DEVELOP THE LEGISLATIVE ENVIRONMENT

- Commercial registration
- Intellectual property rights
- Insolvency and creditors rights
- Civil aviation law
- Privatization law
- Insurance activity law
- Industrial law
- Tourism law
- Postal company establishment law
- General E&W corporation establishment law
- Mortgage law
- Competition law
- Credit bank law
- Civil Service wage reform law
- Utility fees and charges law
- Tax law

42. More than 7,500 government services are considered for an average tariff increase of 40%, such as administration fees, training fees, licenses customs brokers fees, etc.

At present, the Kuwaiti tax department is not equipped to collect taxes for the prospective registry. The department currently lacks the administrative infrastructure and necessary IT systems for a wider tax collection. The government must also develop a compliance framework to ensure companies observe new tax laws. Currently, many companies maintain improper record-keeping due to low compliance and regulation enforcement. Training companies will be vital as VAT collection will be impossible without proper accounting records.

Kuwaiti citizens are greatly accustomed to the country's welfare system and have historically met talks of taxation with disapprobation. Efforts, outreach and awareness are required to educate citizens on the necessity of VAT and how it plays a greater role in their country's economic stability. The government's extension signals an opportunity to establish proper systems and controls, train people and grant the public time to adapt from a change in their tax free lifestyle.

## 2.1.5. FINANCIAL IMPACT OF THE PROGRAM

While the need and commitment to reform is clear, the government is able to pace the implementation of the program to avoid shocks to the economy and minimize impact on its citizens. Fortunately, Kuwait's high fiscal buffers and resilient economy gives the government the opportunity to progressively narrow the deficit in the

medium term, rather than completely close it through launching drastic measures which could prove counter-productive. By the closure of the reform program in 2020/21, the government aims to reduce the annual deficit to below USD 10 Billion.

## 2.2. DEBT STRATEGY

In early 2016, the Ministry of Finance recognized the importance of diversifying its sources of budget funding. As such, on 24 February 2016, a Ministerial decree mandated the establishment of the Debt Management Committee (DMC). The DMC was established with the mandate of overseeing the management of public debt in Kuwait, including setting up and supervising a Debt Management Department (DMD) in the Ministry of Finance. The DMC includes representatives from the Ministry of Finance, the Central Bank of Kuwait and the Kuwait Investment Authority. The DMC ensures coherence and alignment of debt management policy, monetary policy, macro-prudential policy and the management of general reserves. Over the course of 2016, the DMC established the Debt Management Department (DMD) with the following responsibilities:

- ▶ Promote debt management transparency by enabling public access to relevant and accurate data
- ▶ Stimulate a feasible and risk averse diversification of both financing instruments and investor base
- ▶ Develop and maintain control systems to ensure best-in-class risk management
- ▶ Ensure coordination between Quasi-Sovereign entities and State Owned Enterprises in debt related matters.

Following the drop in oil prices in FY 2015/16, Kuwait opted to entirely fund its USD 19.7 Billion deficit<sup>43</sup> through General Reserve Fund (GRF) drawdowns. This stimulated the establishment of the DMD, after which the first debt management strategy was developed. The strategy for FY 2016/17 was guided by a set of critical principles; the primary being establishing Kuwait in the sovereign debt markets. Since Kuwait had not previously borrowed on international capital markets, establishing this initial

- ▶ Develop and recommend the State's long term financing strategy, by assessing available financing instruments
- ▶ Collaborate with concerned parties in view of developing a liquid secondary market for Kuwaiti sovereign bonds
- ▶ Promote improvements in issuance techniques and debt markets in an effort to lower the cost of public debt

43. Including transfers to Kuwait's Future Generation Fund

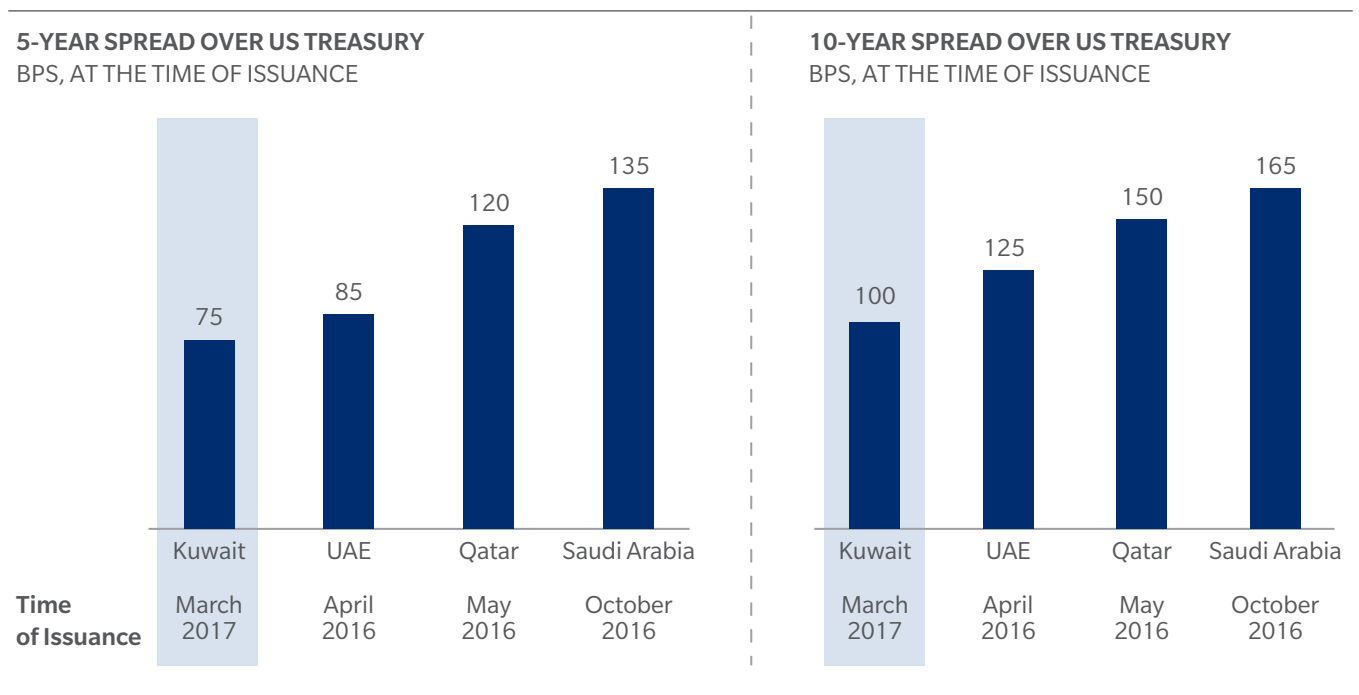
issuance was key, as it would ensure future access to a broader set of instruments. Secondly, Kuwait was keen on striking the adequate balance between ensuring issuances are liquid enough, and avoid flooding the markets with bonds. In parallel, Kuwait was guided by a crucial principle: preserving the GRF and maintaining a healthy emergency cash buffer.

In accordance with the above, the Ministry of Finance approved a financing strategy to fund the deficit in FY 2016/17, using a balanced mix of available instruments. The strategy allowed a debt issuance of up to USD 6.6 Billion locally and USD 9.5 Billion internationally, and dictated that the remainder be bridged by GRF drawdowns. In fact, the approved local issuance was continuously raised throughout the year, targeting local financial institutions, which in all occasions portrayed a healthy oversubscription amount. To raise international debt, senior representatives of the State of Kuwait went on an international roadshow in March 2017, covering the United Kingdom and the USA. The roadshow delegation held meetings with potential investors, including fund managers and other institutional nominees, and

presented the country’s economic state and future reform plans. Investors expressed confidence in Kuwait, which translated in a peak book size of USD 29 Billion, 3.6 times larger than the issuance size. Subsequently, Kuwait’s first debt issuance was a resounding success with USD 8 Billion raised, achieving the tightest credit spread at the time of issuance for any GCC sovereign. The issuances were allocated to more than 350 investors across both 5 and 10 year tenors<sup>44</sup> (Figure 13).

The DMD is now in the process of laying down the future debt strategy for the state of Kuwait. “The balanced strategy will rely on a selection of the most feasible financing instruments, including local and international debt issuances, as well as utilizing liquidities in the General Reserve. [...] This public debt strategy will continue to reflect a rational and prudent borrowing, maintain the appropriate level of liquidity in the domestic market while protecting [reserves] from any withdrawals that may harm the country’s credit rating”<sup>45</sup>.

**FIGURE 13: DEBT ISSUANCE RESULTS - COMPARED TO GCC PEERS**  
[DEBT MANAGEMENT DEPARTMENT]



44. Kuwait Ministry of Finance, Debt Management Department Data

45. Minister of Finance, National Assembly closing speech, June 2017

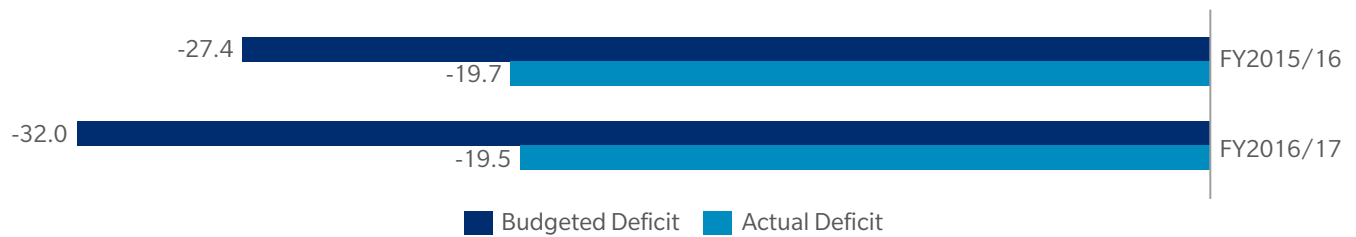
### 3. EFFORTS HAVE STARTED TO PAY OFF

The results of the reform program have started to show impact, with reduced expenditure and higher than expected revenue (due to increased oil production and oil price) driving a lower than budgeted deficit (Figure 14).

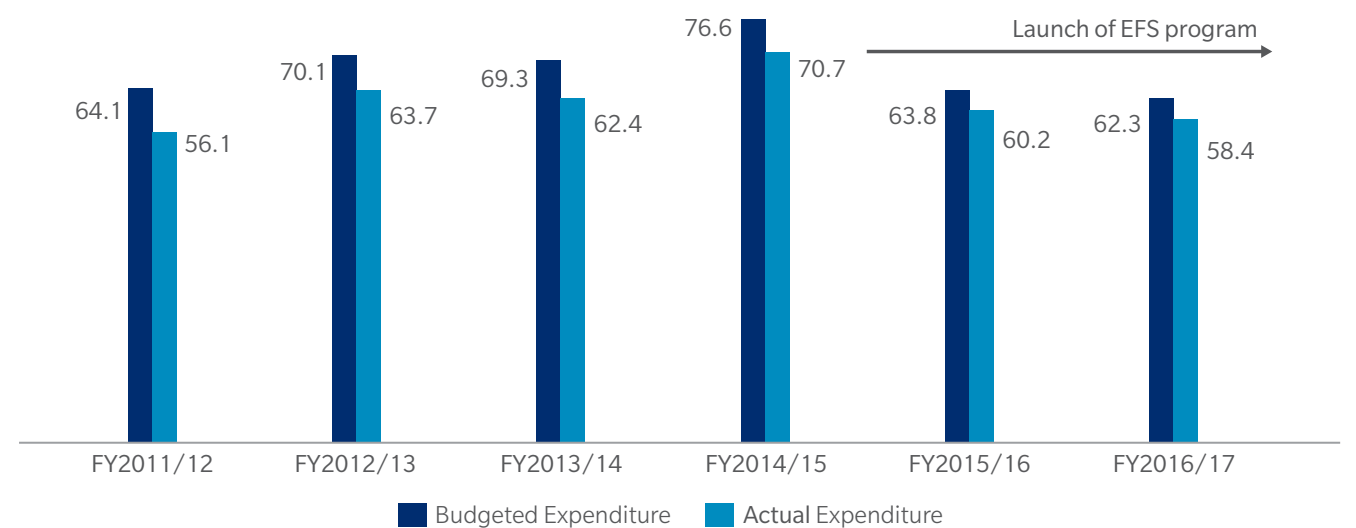
In the last five years, Kuwait has consistently achieved expenditure below budget. It is noteworthy, however, that since the launch of the EFS program, the trend has been reversed and government spend has

been decreasing (Figure 15)- indicating a serious commitment to meeting new directives. The State then maintained the reduced ceiling in 2016/17, in an effort to control budget growth going forward. The Ministry of Finance introduced Medium Term Budgeting for the first time, with the aim of capping expenditure for the coming three fiscal years<sup>46</sup>.

**FIGURE 14: BUDGETED VS. ACTUAL BUDGET DEFICIT, INCLUDING TRANSFERS TO FGF, USD BILLION**  
[KUWAIT MINISTRY OF FINANCE]



**FIGURE 15: EVOLUTION OF KUWAIT GOVERNMENT EXPENDITURE, USD BILLION**  
[KUWAIT MINISTRY OF FINANCE]



46. Fiscal years 2018/19, 2019/20 and 2020/21

A number of initiatives from the National Program for Economic and Fiscal Sustainability, concerned with reducing government expenditure, such as capping government entities' budget, were implemented to achieve this closing figure. Additionally, measures were developed and implemented to control budget adjustments and transfers in an effort to not only control wastage, but also instill discipline in spend.

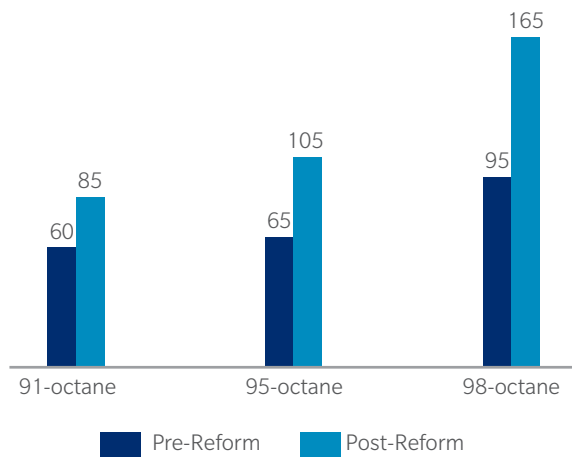
One key measure implemented was the partial lifting of fuel subsidies. On 1 September 2016, fuel

subsidies were partially removed. An analysis of consumption patterns conducted one month after the change, showed a clear shift in the grade of fuel consumed. Higher fuel prices warranted a shift in consumption from 95-octane to 91-octane, which is cheaper to produce (**Figure 16**). Moreover, in May 2017, new electricity tariffs have been launched and the government expects to generate close to USD 1.5 Billion in savings in the fiscal year 2017/18<sup>47</sup>.

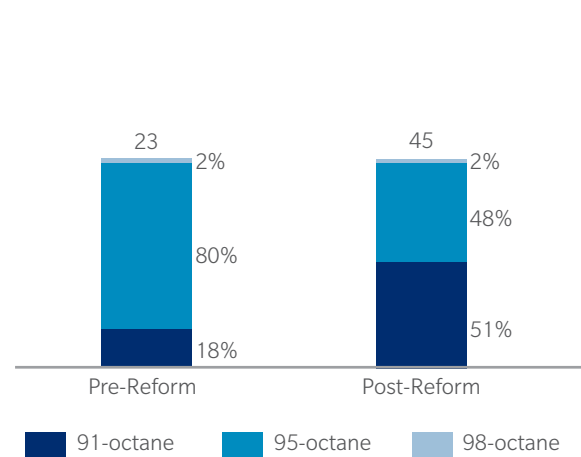
**FIGURE 16: ALIGNING KUWAIT'S FUEL SUBSIDIZATION WITH THE GCC**  
[KUWAIT CENTRAL STATISTICS BUREAU]

In September 2016, Kuwait became the last GCC state to partially remove fuel subsidies for the entire Kuwaiti population (citizens and residents alike). Prices rose between 42% and 74% depending on fuel grade. The immediate impact was a shift in consumption from 95-octane to the cheaper 91-octane, which in effect limited the incremental cost for consumers doing the shift to +40% (65 to 85 fils per liter), rather than the expected +62% (65 to 105 fils per liter)

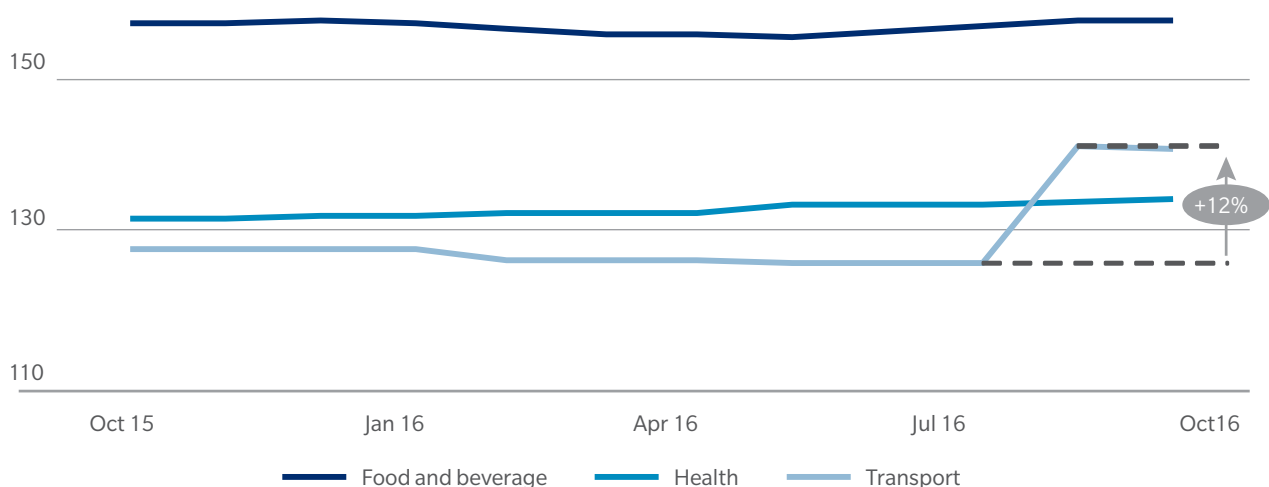
FUEL-PUMP PRICES ROSE  
(FIGURES IN KUWAITI FILS PER LITER)



CONSUMPTION SHIFTED MASSIVELY TO 91-OCTANE



THE PRICE INCREASE IMPACTED THE TRANSPORT COMPONENT OF THE CONSUMER PRICE INFLATION INDEX, BUT VERY MARGINALLY AFFECTED THE OTHER COMPONENTS



47. Kuwait Ministry of Finance

In parallel, the Civil Service Commission launched additional measures to control both salary and employee growth. Compensation caps were introduced on board members, committees and working groups, and existing allowances were revised to more reasonable figures. In parallel, a clear directive was issued to reduce the hiring of non-Kuwaitis in support roles. The wage reform law, aiming to increase fairness and transparency in the labour market and align public sector salaries, is close to being implemented and is pending parliamentary approval.

On the other hand, important advancements have been observed in Kuwait's economic landscape. The Supreme Council for Privatization developed and endorsed a 25-year privatization strategy. Currently, the privatization process has been initiated for four state owned enterprises: Fixed Line and Broadband Services, Airports, Seaports and Power Plants. Additionally, the first Public Private Partnership (PPP) Project achieved commercial closure in November 2016, and the plant's operations were officially initiated. The remaining PPP projects are under tendering, the majority of which are in the final contract awarding phases.

Kuwait is also well on its way to improving the business environment through the establishment of a robust institutional framework. The general law regulating the process for commercial registrations has been drafted and is pending approval. The intellectual property law was approved in 2015, paving the way for facilitating investment in the country. Legislation encouraging foreign direct investment is already in place to further stimulate the development of the private sector. Beyond legislation, concrete measures are being taken to facilitate private sector investment. In early October 2016, the Ministry of Commerce and Industry launched the Kuwait Business Centre (KBC), a "one-stop-shop" enabling new businesses to streamline their incorporation and ultimately, removing administrative burdens. In fact, in Q1 of 2017, the business process was revamped to reduce the number of steps required to set up a business from 15 to 4<sup>48</sup>.

48. Kuwait Ministry of Commerce & Industry

## 4. SIGNIFICANT CHALLENGES LIE AHEAD

It is vital to note, however, that there are many challenges Kuwait needs to address to achieve the required and envisioned transformation. After sixteen consecutive years of fiscal surpluses up to 2014/15, a significant communication effort is required to educate

officials, and the population at large, on the urgency of change. Kuwait's political system crucially requires the existence of a national consensus, aligning on how to address the current situation.

### 4.1. POLITICAL CHALLENGES: COMMITTING TO CHANGE

Reforming governments requires a sustained and unwavering political commitment. Unlike other GCC countries, Kuwait's democratically elected parliament (the National Assembly) must ratify major decisions and laws. The ability to pass and implement decisions could thus face bottlenecks not existent in other GCC countries. Although Kuwait's democratic system, in comparison to GCC peers, helps set a solid and lasting foundation for any decision taken, advancing on nationwide initiatives might come at a cost. In order to reach a unified consent, officials need not only to proactively socialize measures with different government stakeholders, but also ensure alignment and collaboration.

consumption bills. The action was subsequently met with strong opposition by citizens, government officials and members of parliament. Although the decision to raise prices falls within the cabinet's power, the government body was subject to heightened pressure.

Despite being driven by the executive branch of government, the reform plan requires broad support. This includes not only the support of ministers but also of the National Assembly, which has the power to repeal some or all of the plan's initiatives. While the reform does not require active lobbying, explaining the necessity and long-term benefits of the reform to other decision-makers is necessary to build support.

In September 2016, gasoline subsidies were partially lifted and citizens saw an increase in their fuel

### 4.2. OPERATIONAL CHALLENGES: HAVING THE CAPABILITY AND CAPACITY TO ACT

Operational challenges in Kuwait go beyond the standard capability and capacity issues. The country's bureaucratic process is typically very slow and hierarchical. Posts are generally occupied by employees who are not encouraged or incentivized to improve operational efficiency, making government activities often cumbersome and unreliable.

Nevertheless, this support can only compliment the current workforce rather than substitute the government's capability and capacity requirements. Hence the Kuwait government should actively continue to develop the capability, productivity and work ethic of its employees.

Kuwait has partly sought to address this problem through relying on third party independent advisors-targeting both capacity and capability issues.



## 4.3. COMMUNICATION CHALLENGES: EDUCATING THE PUBLIC

A pervasive perception of abundance by Kuwait's citizens is at the core of the challenges to implement reforms. Years of generous government pay-outs in the form of subsidies or other benefits have created a sense of self-entitlement, proven difficult to change. This perception, however, is not without foundations. There is a general awareness among the population of the impact high oil prices have had in previous years and a corresponding expectancy that the surpluses previously generated should be able to amply cover the shortages experienced today. As such, the historical generosity of the state should not show any alteration. The implicit social contract that has been a driving force between government and its citizens is well instilled. As a result, any proposed adjustment to existing social benefits risks being staunchly opposed.

In March 2017, a survey was conducted<sup>49</sup> across 16 different Arab countries to understand youth's views on the future of the region. When asked "Do you think the economy in your country is heading in the right direction?", 82% of GCC-ers believed that the country's direction points to better days ahead. Although this

indicates a level of optimism, it strongly reflects a lack of sufficient awareness on the reality of their economies. Kuwait's future challenges are very real, as driven by the reality of international oil prices, and paired with the country's underdeveloped private sector economy.

Overcoming these cultural challenges is no trivial task. A profound and generational change is required to re-educate citizens. Education stems through a sustained program that includes the broad spectrum of schooling and social institutions to maximize citizen reach. It is also important to also keep citizens informed about the scope of the reforms and the necessity driving their implementation. The government should continue to place necessary emphasis in establishing and maintaining an open and bidirectional communication channel, informing citizens of upcoming developments and conveying valuable citizen feedback to the government.

49. Arab Youth Survey conducted by ASDA'A (Burson-Marsteller)

# 5. NO TURNING BACK: KUWAIT NEEDS TO MAINTAIN MOMENTUM

The reform program will play a vital role in transitioning Kuwait towards economic diversification and private sector development. With the perspective of sustained depressed oil prices, Kuwait will not be able to count on its historical revenue driver for fiscal respite. Irrespective of oil price, however, reforms remain a must for Kuwait to address the structural imbalances of the economy.

The need to reform is not solely driven by considerations internal to Kuwait. International credit rating agencies such as Moody's, Fitch and Standard & Poor's wield a significant amount of influence in driving foreign investment and through that, economic prosperity in any country. To assess credit risk, rating

agencies look at economic, institutional and fiscal strength, in addition to susceptibility to event risk<sup>50</sup>. In the case of Kuwait, the reform program has a direct impact on most of these dimensions. The agencies are aware of the government's efforts to reform and thus closely monitor developments in this direction. Post debt issuance, the investors have also reinforced their levels of scrutiny on the government's ability to render Kuwait economically prosperous. The implementation and success of the reform program is therefore one of their fundamental inputs; the government needs to demonstrate its commitment as well as show results. Any disruption could put the sovereign rating at risk, with increased borrowing costs as main consequences of a downgrade (**Box 3**).

## BOX 3: RECENT DEVELOPMENTS ON KUWAIT'S CREDIT RATING

Kuwait has had its credit risk reviewed by both Fitch and Moody's. In November 2016, Fitch affirmed Kuwait's 'AA' rating, with a stable outlook. Cited as part of the key rating drivers were Kuwait's reform agenda and the Ministry of Finance's effort to reduce government spending. On the other hand, concerns surrounding implementation lead to a negative outlook from Moody's in May 2016. This was done on the basis of the uncertainties surrounding Kuwait's ability to implement the reform program, and notably the impact of the parliamentary elections.

However, Moody's latest rating round in May 2017, revised its past outlook to stable. The agency attributed this outlook to Kuwait's successful debt issuances and its solid government reserves, but also to the persisting seriousness that the government portrayed in implementing national reforms.

Similarly, in July of 2017, the credit rating agency S&P affirmed Kuwait's high quality AA/A-1+ rating with stable outlook expectations. This decision comes as a result of Kuwait's strong public and external balance sheets backed by significant financial assets, which are recognized as key ratings strengths.

Nevertheless, Kuwait could face a risk of potential downgrade in the future, as mentioned by rating agencies, if the government fails to implement reform measures in both a timely and decisive manner.

50. Moody's rating methodology, December 18 2015

A very infamous historical path resonates in the advent of the current economic challenges. “The natural resource curse” has been and remains a non-fictional fear of countries blessed with a generous geology.

In 1980, Nauru’s phosphate mines made the small island the wealthiest nation on the planet, with the highest recorded GDP per capita. It was only a matter of years before the resource was depleted and the country was hit by “The natural resource curse”. Today, Nauru ranks as one of the poorest economies in the world, paired with a grave socio-cultural crisis and a failed economy. Complacency in building a diversified and resilient economy back in the 80’s drove the country’s misfortune.

Nauru’s tale is telling of the dangers ahead. However unlike Nauru, Kuwait has realized the risks posed by a single income economy and initiated its transformation process. Still, the reform journey remains challenging. As such, the government’s ability to drive reform is not only a requirement but a necessity to ensure the future generation’s prosperity.

## ABOUT TICG

Tri International Consulting Group (TICG) is a world-class management consultancy that combines extensive industry knowledge and deep Kuwaiti market understanding with specialised expertise in strategy, operations, risk management, and organisation transformation. Our professionals help clients optimise their businesses, improve their operations and risk profile, and accelerate their organisational performance to seize the most attractive opportunities.

TICG was founded as a joint venture between the Kuwait Investment Authority (KIA), the first sovereign wealth fund in the world, the Kuwait Fund for Arab Economic Development (KFAED), the first Arab international development institution, and Oliver Wyman, a leading global management consulting firm.

[www.ticg.com.kw](http://www.ticg.com.kw)

## CONTACTS

For further information, please contact:

### **Tri International Consulting Group**

3<sup>rd</sup> floor, Global Tower  
Al Shuhada street  
Sharq, Kuwait  
PO Box 21744  
13087 Al Safat, Kuwait

Tel: +965 2241 5057

Fax: +965 2241 5470

[contact@ticg.com.kw](mailto:contact@ticg.com.kw)

Copyright © 2017 TICG. All rights reserved.

## REPORT QUALIFICATIONS/ASSUMPTIONS & LIMITING CONDITIONS

TICG shall not have any liability to any third party in respect of this report or any actions taken or decisions made as a consequence of the results, advice or recommendations set forth herein.

This report does not represent investment advice or provide an opinion regarding the fairness of any transaction to any and all parties. The opinions expressed herein are valid only for the purpose stated herein and as of the date hereof. Information furnished by others, upon which all or portions of this report are based, is believed to be reliable but has not been verified. No warranty is given as to the accuracy of such information. Public information and industry and statistical data are from sources TICG deems to be reliable; however, TICG, its employees and its advisers make no representation as to the accuracy or completeness of such information and has accepted the information without further verification. No responsibility is taken for changes in market conditions or laws or regulations and no obligation is assumed to revise this report to reflect changes, events or conditions, which occur subsequent to the date hereof.