INTERNATIONAL MONETARY FUND

IMF Country Report No. 12/18

QATAR

2012 ARTICLE IV CONSULTATION

January, 2012

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 2011 Article IV consultation with Qatar, the following documents have been released and are included in this package:

- **Staff Report** for the 2011 Article IV consultation, prepared by a staff team of the IMF, following discussions that ended on December 1, 2011, with the officials of Qatar on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on January 12, 2012. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.
- **Informational Annex** prepared by the IMF.
- **Public Information Notice** (PIN)summarizing the views of the Executive Board as expressed during its January 30, 2012 discussion of the staff report that concluded the Article IV consultation.

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

Selected Issues Paper

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

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INTERNATIONAL MONETARY FUND

QATAR

January 12, 2012

STAFF REPORT FOR THE 2011 ARTICLE IV CONSULTATION

KEY ISSUES

Economic prospects. Qatar is using its fiscal space, generated from an increase in hydrocarbon production and high prices, to implement a large public spending program to maintain strong growth in the nonhydrocarbon sector in the medium term and improving living standards. Real GDP growth is projected to accelerate to 19 percent in 2011 from 17 percent in 2010. Average headline consumer price inflation has remained contained in 2011 at 2 percent. The overall fiscal balance remained in a surplus of 2.7 percent of GDP in 2010/11. The current account balance is projected to record a surplus of 28 percent of GDP.

Risks to the outlook. The principal risks ahead are lower oil and gas prices as a result of a decline in global demand, and disruption in transportation of liquefied natural gas (LNG) due to increased geopolitical tensions, but the government has adequate financial cushions and a policy framework in place that would mitigate potential risks.

Sustaining economic and financial stability. The expansionary fiscal stance in 2011/12 warrants careful monitoring of aggregate demand to ward off risks of inflation. In the context of the peg, the Qatar Central Bank (QCB) would need to manage liquidity more actively. Monetary policy should support credit growth without fuelling inflationary pressures or attracting short-term capital inflows. Over the medium term, fiscal policy will need to balance sometimes competing objectives of stabilization, development and generating intergenerational savings.

Strengthening and developing the financial sector. The banking system remains resilient to shocks. Nevertheless, enabling a more robust risk assessment culture and conducting regular stress testing of banks, developing a more formal and transparent macroprudential policy framework, and putting in place a framework for early warning system would help mitigate risks to the banking system and strengthen financial stability. Efforts should continue to develop the domestic bond markets.

Building institutions. The authorities need to accelerate steps to establish a macro-fiscal unit that could develop a medium-term expenditure framework to ensure the efficiency of public spending.

Improving economic statistics. With data availability underpinning good policy-making, more progress is needed for timely compilation and dissemination of key statistics.

Approved By
Alfred Kammer and David D. Marston

Discussions were held in Doha from November 16–December 1, 2011. The staff team comprised Messrs. Prasad (head), Ribeiro da Silva, and Mmes. Arvai, Fayad, (all MCD), and Cardillo (STA). Mr. Kammer joined the team during November 30-December 1.

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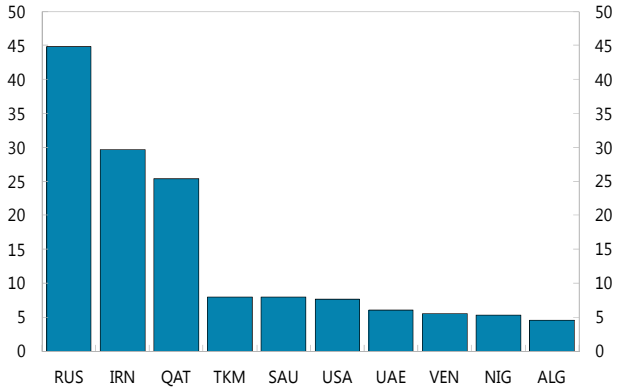
BACKGROUND AND CURRENT CONTEXT

1. **Qatar has the third-largest proven reserves of gas in the world, and is now the world's largest producer of LNG.** Qatar's 20-year investment program, which focused on a strategy to commercialize its large natural resources, culminated in 2011. The State has placed a moratorium on development of new hydrocarbon projects until 2015 to give itself time to assess its production performance and carry out a comprehensive study of its offshore North Field, where its gas is produced. Qatar has embarked on a huge infrastructure investment program over the medium term–including roads, completion of the port and airport, and metro—for which the budget allocation is expected to be close to $100 billion.

2. **Qatar has weathered the global crisis and the regional turmoil with high growth, and large external current account and fiscal surpluses.** The country's large wealth relative to the small Qatari population of less than a fifth of a total of 1.7 million has insulated it from a direct contagion from the political turmoil in the region. Annual per capita income is around $100,000, and the official unemployment rate is estimated at less than 1 percent.

Proven Gas Reserves, June 2011
(In trillions of cubic meters)



Source: BP Statistical Review of World Energy.

Qatar Economic Indicators, 2006 and 2010

	2006		2010		2006–10 Average	
	QAT	GCC	QAT	GCC	QAT	GCC
Nominal GDP (U.S. dollar billions)	60.8	793.8	127.3	1,090.8	96.1	968.3
Real GDP Growth[1] (percent)	26.2	6.5	16.6	5.4	18.1	4.7
Inflation (percent)	11.8	4.6	-2.4	3.2	6.7	5.7
Current Account Balance (U.S. $b)	15.3	201.4	33.5	164.7	22.4	172.8
Current Account Balance (% GDP)	25.1	25.4	26.3	15.1	23.2	17.9
Fiscal Balance (% GDP)	7.9	22.2	2.7	6.1	9.0	14.0

Sources: Country authorities; and IMF staff calculations.

[1] GCC growth averages are weighted using PPPGDP.

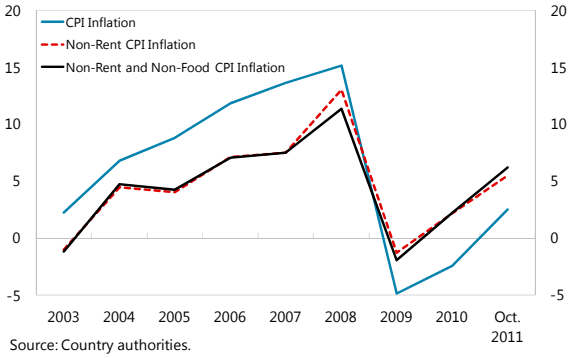
RECENT ECONOMIC DEVELOPMENTS, OUTLOOK AND RISKS

Rapid Growth with Financial Stability

3. **Real Gross Domestic Product (GDP) growth is projected to accelerate to 19 percent in 2011 from 17 percent in 2010—**as the production of LNG increased by 36 percent. Increased activity in manufacturing, financial services, and trade and hotels is driving growth in the nonhydrocarbon sector at 9 percent in 2011.

4. **Headline inflation has remained contained in 2011, but inflation excluding rent increased to 5.8 percent in October 2011.** Following an average deflation of around 2.5 percent in 2010, inflation is expected to average around 2 percent in 2011 (end-year 2.5 percent)—with negative rental inflation being more than offset by a general increase in all the other components of the CPI basket.

Headline, Non-Rent, and Non-rent Non-Food CPI Inflation
(In percent)



Source: Country authorities.

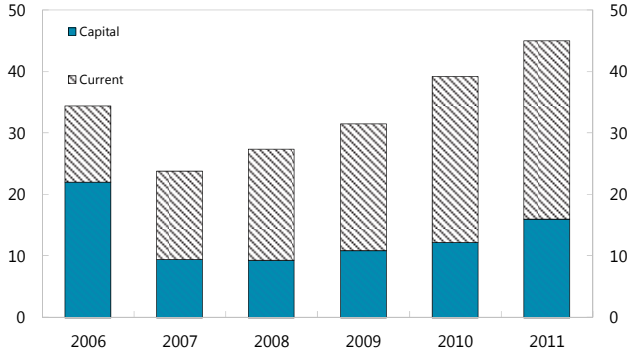
5. **The fiscal and external balances will remain in surplus in 2011.** Despite the sharp rise in current expenditure and lower than budgeted receipt of profit transfers from public enterprises, the overall fiscal balance (net lending/borrowing) remained in a surplus of 2.7 percent of GDP in 2010/11.[1] The government did not raise any new external borrowings in 2010/11, but issued domestic bonds and Treasury bills (T-bills) to facilitate sterilization and liquidity management against the backdrop of capital inflows. As a result the net debt of the government increased. The post-budget announcement of salary and pension hikes would add an estimated $1.6 billion to government expenditure in 2011/12.[2] Since oil prices have remained on average well above $55 a barrel in 2011, the actual fiscal balance is projected to record a surplus of 7.2 percent of GDP in 2011/12. The current account surplus is projected at 28 percent of GDP in 2011, up from a surplus of 26 percent in 2010, reflecting increased volume and prices of hydrocarbon exports.

[1] Qatar Petroleum (QP) transferred lower profits to the budget since it retained QR25 billion ($6.9 billion) of its profits to increase its capital. However, if the QR25 billion capital contribution to QP had been included in investment income and the transfer back to QP shown below the line as a financing item instead of being netted out of investment income, last year's overall surplus would have been 7.6 percent of GDP.

[2] Effective September 2011, the government announced a 60 percent increase in the basic salary and social allowance for Qatari state civilian employees, a 120 percent rise for military personnel of officer ranks, and a 50 percent rise for military personnel of other ranks. In addition, the pension of civilian retirees will increase by 60 percent, while that of retired military officers will rise by 120 percent and of other ranks by 50 percent.

Composition of Government Expenditure, 2006–11

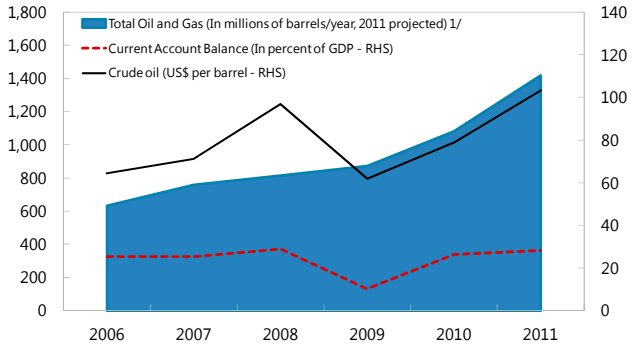
(In US dollar billions)



Source: Country authorities.

Current Account Balance, 2006–11

(In percent of GDP; unless otherwise specified)[1]



Sources: Bloomberg; country authorities; and IMF staff calculations.

[1]Includes crude oil, LNG, condensate, and LPG converted to oil barrels.

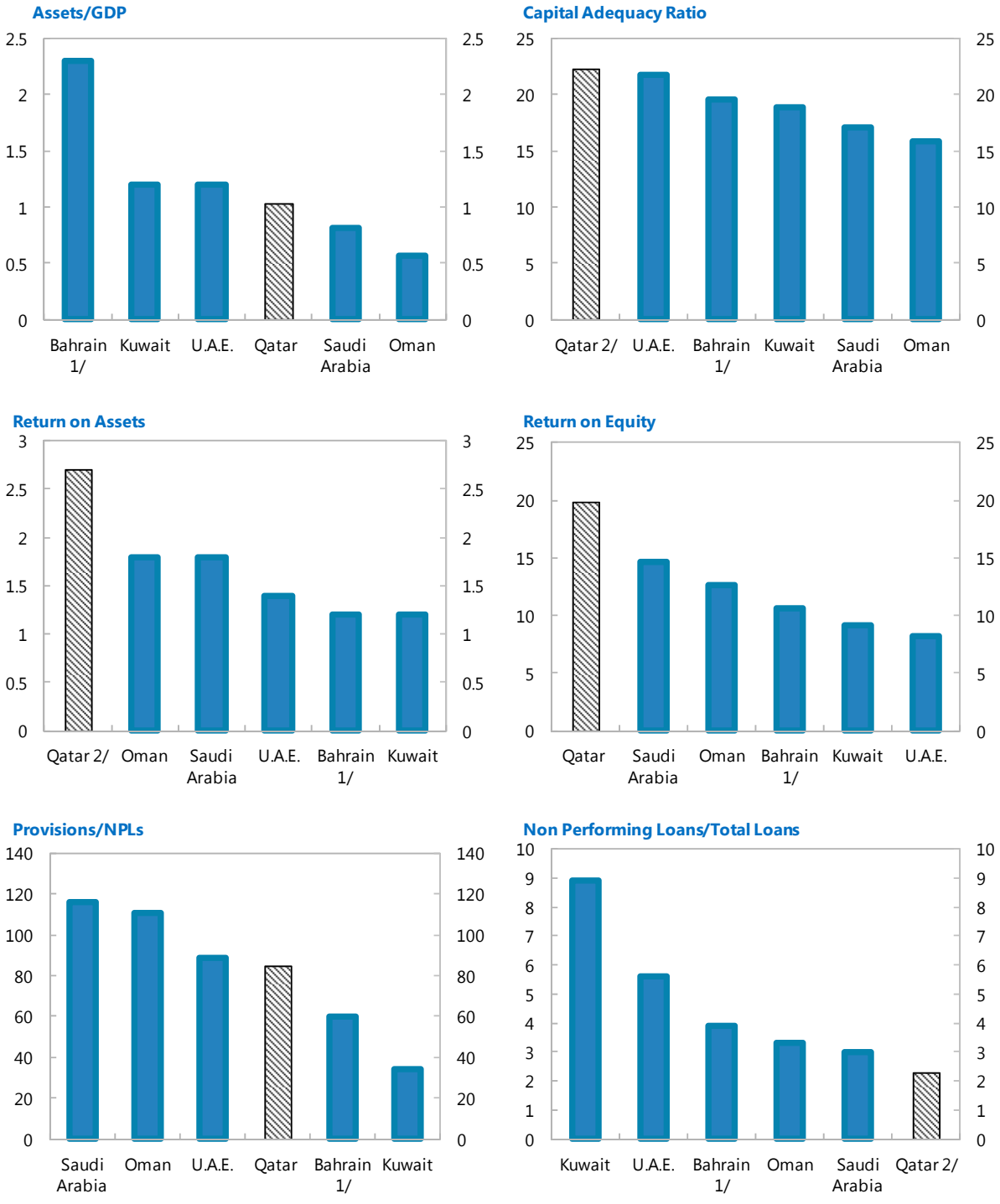
6. **Monetary and credit developments reflect easy conditions.** Commercial banks' claims on the private sector increased by 19 percent y-o-y in October 2011. The easing of monetary conditions in 2011 coincided with the launch of some infrastructure-related investments in the hydrocarbon and nonhydrocarbon sectors.

7. **The banking sector is well-capitalized.** Equity injections and asset purchases by the government strengthened confidence in the financial system. The Qatar Investment Authority (QIA) injected $2.8 billion of capital into the banking system in three tranches between 2009 and 2011. As a result, the capital adequacy ratio of the banking sector increased to 22.3 percent by end-June 2011. The average return on assets stood at 2.7 percent, and the non-performing loans ratio was 2.3 percent at end-June 2011 (Figure 1). The exposure of local banks to European banks is limited.[3]

[3] Local Qatari banks' cross-border exposures (loans and investments), to the European banking sector was approximately $3.3 billion at end-June 2011– constituting 2 percent each of 2011 GDP and banking system assets.

Figure 1. Banking Soundness Indicators, 2010

(Ratio)



Source: Country authorities.
1/ For all indicators except Assets/GDP, latest data available is 2009.
2/ Data is for June 2011.

SHORT-AND MEDIUM-TERM OUTLOOK IS FAVORABLE DESPITE GLOBAL UNCERTAINTY

8. **The economic outlook for 2012 remains positive, despite increased external risks.** Real GDP growth rate is projected to moderate to 6 percent in 2012, with real hydrocarbon GDP slowing down to less than 3 percent, as LNG production remains constant. Large infrastructure investment and increased production in the manufacturing sector will maintain real nonhydrocarbon GDP growth at 9 percent. Average headline CPI inflation is projected at 4 percent in 2012. The fiscal balance is still projected to record a surplus of over 7 percent, and the external balance is projected to post a surplus of $47 billion.

9. **Qatar is expected to continue recording a strong economic performance over the medium term.** The fiscal and external current account balances are projected to record surpluses, as hydrocarbon prices are expected to remain high. Large government investment would sustain growth in the nonhydrocarbon sector between 9 and 10 percent beyond 2012. Average headline inflation is projected at 4 to 5 percent over the medium term, as rents stabilize due to a gradual decline of the current excess capacity in real estate, and as the implementation of large investment projects lead to some overheating pressures.

Risks are manageable

10. **The principal risks ahead are lower oil and gas receipts as a result of a decline in global demand and potential disruption in transportation of LNG due to increased geopolitical tensions.** The government, however, has adequate financial cushions and a policy framework in place to mitigate the impact, and price risk is limited since Qatar's hydrocarbon exports are delivered under long-term contracts. Moreover, Qatar's low cost of LNG production, and the built-in diversion clauses in the gas contracts, give it additional flexibility to manage quantity and price risks.

11. **A large drop in hydrocarbon prices would have a significant impact on the fiscal and external current accounts but Qatar would still continue to generate surpluses.**[4] Staff's alternative macroeconomic scenario indicates that the external current account surplus would decline sharply from an average 25.6 percent

[4] A "crisis scenario" is generated by treating 2011/Q3 as being equivalent to 2008Q3 (oil price already slightly off its peak and about to crash in Q4) and then taking the quarter on quarter percentage changes from the previous crisis. This implies the oil price falling to $50 a barrel in 2011Q4, and averaging $55 in 2012 and $70 in 2013. In addition, LNG production, and hence exports, are estimated to be 15 percent below the benchmark scenario. Crude oil prices are used as a proxy for gas prices for this exercise, as all the LNG and gas-related products are converted to oil barrel equivalent.

of GDP in 2012–13 to 5.6 percent of GDP under the shock scenario without diversion of exports. The fiscal balance would turn from a surplus in 2011, to a deficit from 2012 onwards, and cash flows to the State would fall by $41 billion between 2012 and 2016, but still generate surpluses in each year. Real nonhydrocarbon GDP would reduce by half in 2012, due to delays in the implementation of transportation and other infrastructure projects (Figure 2). The authorities, however, do not see oil prices falling below $80 a barrel in the medium term due to the emergence of high demand for oil and gas from China and India.

12. **In addition, a deepening of the banking and sovereign debt problems in advanced economies could result in a tightening of global liquidity and impact Qatar through channels similar to those observed in 2008–09, particularly since banks have again expanded their real estate lending.** Nevertheless, risks to banking stability appear much lower now after three rounds of bank capitalization and asset restructuring since 2008. Qatar tapped the market with a $5 billion sovereign bond issuance at favorable yields in November 2011.[5]

Even so, the drying up of foreign funding channels could hinder the prospects of other borrowers by increasing the cost, and thereby affecting the infrastructure investment plans and nonhydrocarbon growth.[6] Spillovers through financial channels could impact Qatar's valuation of external portfolios and reduce the value of its foreign assets.

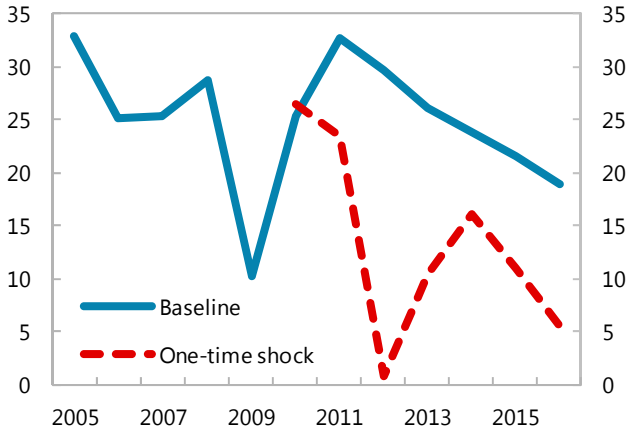
[5] The bond was issued in three tranches: a five-year $2 billion tranche at a yield of 3.184 percent, $2 billion with 10-year maturity at a yield of 4.63 percent, and $1 billion of 30 year-maturity yielding 5.825 percent.

[6] Many local banks have announced plans to raise an aggregate of about $20 billion through international bond issuances and Euro Medium-Term Notes.

Figure 2. Qatar: Macroeconomic Scenarios, 2005–16

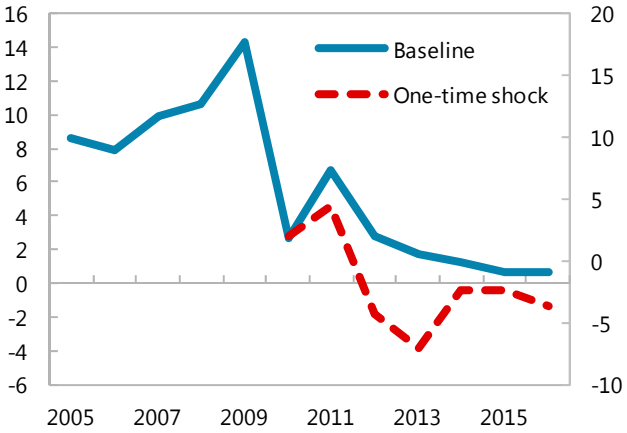
The current account balance declines sharply but remains in surplus.

External Current Account
(In percent of GDP)



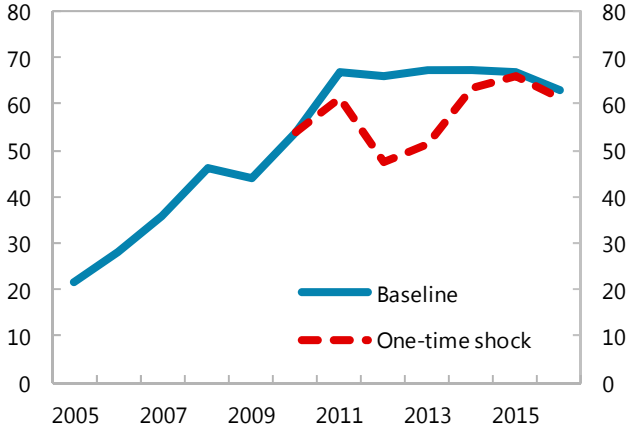
The fiscal balance shows deficits from 2012 onwards…

Overall Fiscal Balance
(In percent of GDP)



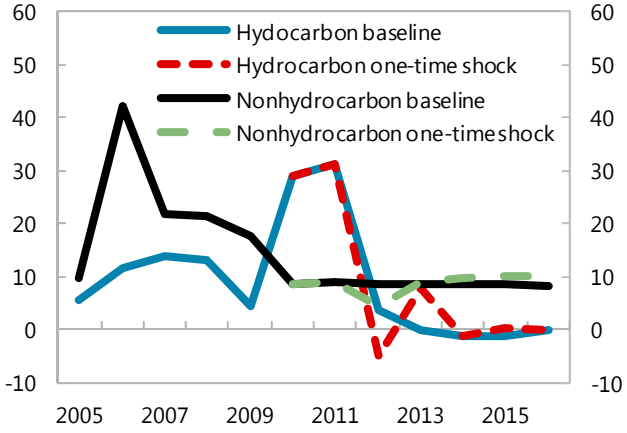
… and cashflows to the State dwindle by a cumulative $41 billion in 2012–16.

Cashflow to the State
(In U.S. dollar billions)



Real GDP growth falls by half in 2012.

Hydrocarbon and Nonhydrocarbon Growth
(In percent)



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

Qatar: Risk Assessment Matrix

Nature/Source of Main Threats	Likelihood of Realization in the Next Three Years	Expected Impact on Economy if Risk is Realized
A large and prolonged decline in the hydrocarbon prices	***Staff assessment: Low*** • Qatar remains heavily dependent on the LNG sector. A softening of global growth could lower the global demand for LNG and gas products with a negative impact on hydrocarbon prices.	***Staff assessment: Low to Medium*** • Will lead to lower external current account surpluses , affect public expenditures, with negative spillover effects on nonhydrocarbon growth. • Will affect the real estate sector, with negative spillover effects on banks' asset quality (increase in NPLs) and earnings outlook. • Low-cost of LNG production and built-in diversion clauses in the gas contracts provide flexibility to manage price and quantity risks (para 10). • Adequate financial cushions are available and a policy framework is in place to mitigate the impact.
A worsening of global liquidity and financing conditions	***Staff assessment: Medium to High*** • The likelihood of realization is related to a Eurozone crisis. • A tightening of global liquidity has occurred in the past, and necessitated the central bank to open a liquidity window.	***Staff assessment: Low to Medium*** • Individual banks, especially those that rely on large wholesale funding might face liquidity pressures and either have to resort to the central bank for dollar funding or deleverage. • Reduction in foreign reserves of the central bank. • Lower valuation of Qatar's external assets portfolio.
Financial contagion to Qatar's sovereign risk	***Staff assessment: Medium to High*** • The contagion for adverse global and regional events has adversely affected Qatar's equity markets and CDS speads in the past.	***Staff assessment: Low to Medium*** • Increase in cost to public enterprises and banks that have announced intention to issue international bonds. • Reduction in wealth due to fall in equity values in Qatar Exchange.
Inflation risk	***Staff assessment: Medium*** • Inflation has risen to high double-digits in 2007–08.	***Staff assessment: Low*** • The increase in public sector wages, the convergence of supply and demand in real estate, and possible overheating from large public investment could see headline inflation increase to 5 percent in the medium term.
Fiscal risk	***Staff assessment: Low*** • Hydrocarbon prices have been volatile historically.	***Staff assessment: Low*** • The net cash flows to the State could fall, but would remain in surplus (para 11). • The savings for intergenerational equity would fall. • The objective of financing expenditure from nonhydrocarbon revenues would face a temporary setback. • Qatar's fiscal break even prices are low at around $40 a barrel.

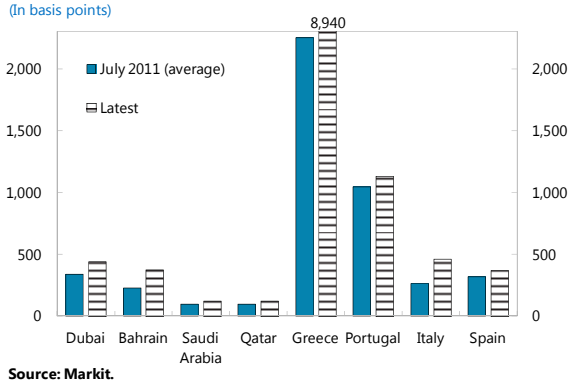
Box 1. Financial Contagion to Qatar's Sovereign Risk

The contagion from the recent global and regional developments has so far been confined to equity and CDS markets. Following a 25 percent increase in 2010, the local equity market index is now 4 percent below its level at the beginning of 2011 amidst volatility. CDS spreads also have increased, albeit modestly compared to regional peers.

The debt crisis in the Euro area has generated intense distress in international financial markets. This has been particularly evident in sovereign credit default swap (CDS) spreads. Using the methodology of Caceres, Guzzo and Segoviano (IMF WP 10/120), a measure of the vulnerability of one country to contagion from a group of countries–the Spillover Coefficient (SC)–is calculated, based on the CDS data of the countries in the group.[1] The SC measures the probability of a sovereign default in one country given default in the other countries in the group. It can thus be used to estimate cross-country contributions to financial stress.

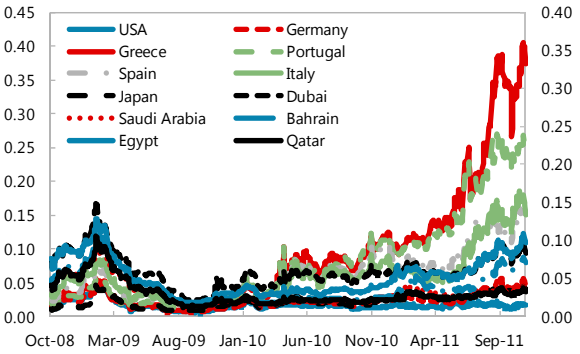
While the estimated level of financial spillovers to Qatar remains relatively low—and lower than during 2008–09—Europe has been a key contributor. The percentage contribution to the change in a country's SC is a measure of market-based contagion from the other countries in the sample. For the period since July 2011, when the Euro area debt crisis intensified, European countries are identified as explaining 90 percent of the contagion risk to Qatar. This stands in contrast to the period following the collapse of Lehman, where the contribution to financial stress was much more evenly spread across countries, with neighbors contributing more due to their regional ties.

5 year Sovereign Credit Default Swap Spreads
(In basis points)

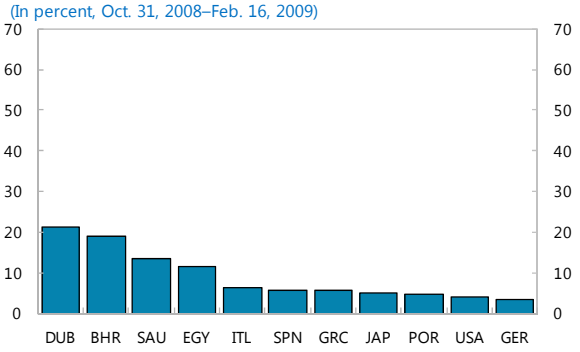


Source: Markit.

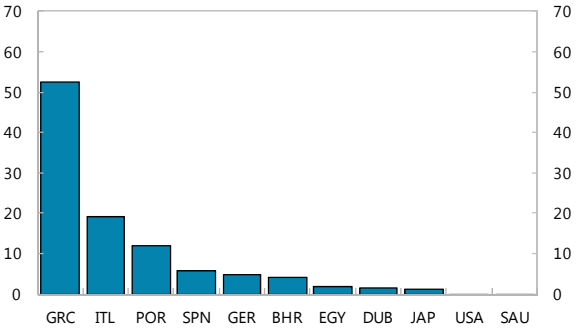
Spillover Coefficient



Contribution to changes in Qatar's Spillover Coefficient
(In percent, Oct. 31, 2008–Feb. 16, 2009)



Contribution to changes in Qatar's Spillover Coefficient
(In percent, Jul. 1, 2011–Sep. 13, 2011)



[1] See also Chapter V of Gulf Cooperation Council Countries: Enhancing Economic Outcomes in an Uncertain Global Economy.

POLICY PRIORITIES

A. Sustaining Economic and Financial Stability

13. **Headline inflation remains subdued, but inflation risks have risen due to an increase in public sector wages.** The authorities acknowledged that the economy could face potential inflationary pressures over the medium term from three channels, viz., the expansionary effect of the major Barzan gas project that will start in 2012, the implementation of major projects in the nonhydrocarbon sector, and the recent fiscal package. The former two channels pose little concern to the authorities as they are growth generating, while the impact of the public sector wage increase would depend on the marginal propensity for domestic consumption. Most of this inflation would come from the nontradable sector, notwithstanding the excess supply in real estate, which will keep rents depressed.[7] The authorities emphasized that the newly formed High-Level Committee on Prices would contain monopolistic price pressures, while the recently introduced limits on retail lending by banks against salary assignment preempted further leverage of the salary increase.[8] Staff projects a potential inflationary effect of the recent fiscal package of about one percentage point (Appendix 1).[9]

14. **The expansionary fiscal stance in 2011/12 thus warrants careful monitoring of aggregate demand to ward off risks of inflation.** The underlying fiscal stance for FY 2011/12 mainly reflects higher expenditure on account of the salary increase, one-off current expenditures related to the Arab Spring, and capital projects, which would be less than compensated by higher hydrocarbon revenues, expected additional profit transfers from public enterprises and higher corporate taxes.[10] Staff and the authorities agreed that fiscal policy needs to continue maintaining a careful balance between spending on infrastructure to sustain non-

[7] Inflation reached double digits in 2008, driven by supply bottlenecks and rising rents. In contrast, since 2009, rental inflation has been declining, and from the second half of 2011, food price inflation is expected to moderate. In addition, credit growth is not expected to reach the 2008 level.

[8] The authorities explained that the salary increase is expected to alleviate household debt to some extent, by inducing some individuals to repay part of their loans to banks.

[9] Staff estimated a simple model on annual 1990-2008 data. The analysis was not extended to 2010, since the last two years saw deflationary trends, mainly due to sharp declines in rents. The fall in rents might have been overestimated, as the measurement of rents (which account for approximately 30 percent of the consumption basket) is skewed towards new contracts. The model included non-oil real GDP and domestic credit growth, which are both endogenously determined with inflation. The model included as exogenous variables one-period lags of current and capital expenditure (to alleviate endogeneity concerns) as well as current international food prices, the nominal effective exchange rate, and an index for imports prices.

[10] The nonhydrocarbon deficit as a percent of nonhydrocarbon GDP, a better measure of the fiscal stance in a hydrocarbon economy, is projected to expand from 25.6 percent to 27.7 percent this fiscal year instead of contracting from 36.5 percent, had investment income been fully accounted for in FY 2010/11.

inflationary growth, and saving and investing hydrocarbon surpluses abroad in order to generate sufficient income to finance future budgets. The authorities do not anticipate any further one-off increases in current expenditure, and aim to allocate 40 percent of the total expenditure toward capital expenditure over the medium term.

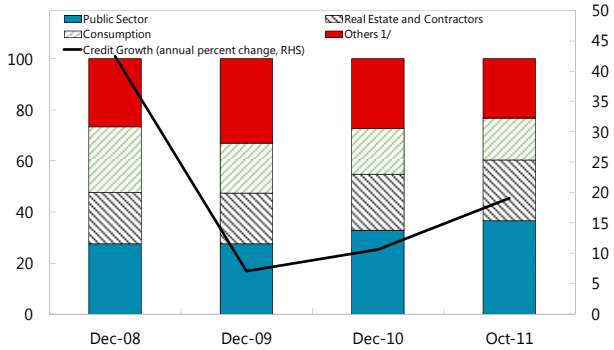
15. **The QCB should maintain its policy stance of driving out short-term speculative inflows and absorbing structural liquidity.** Beginning January 2011, the QCB imposed a cap on its remunerated deposits and reduced policy interest rates in phases to align them with US policy rates. These measures proved successful in driving out short-term arbitrage funds that were intermediated through the banking system (Appendix 2). Issuance of government bonds and sukuk coinciding with the imposition of the cap on central bank deposits, and issuance of T-bills in lieu of certificates of deposit (CDs) facilitated the mopping up of structural liquidity from the banking system over a longer period, while shifting the cost from the QCB's balance sheet to government expenditure. In the context of the peg, the central bank has limited flexibility in deviating from US interest rates, and would, therefore, need to manage liquidity more actively to keep inflation in check.

The QCB's main liquidity management instruments comprise reserve requirements, CDs, which have since been discontinued, and open market operations. The authorities noted that their experience so far with the issuance of T-bills has been positive. They plan to continue with regular issuance of T-bills with a view to managing liquidity and developing the short end of the yield curve.

16. **Developing a more formal and transparent macroprudential policy framework— notably with respect to the definition of objectives, the elaboration of analytical methods, and the policy toolkit— to enable a swift response when needed, would help achieve orderly credit growth without generating overheating.** The main challenges for monetary policy will be to support credit growth–particularly project related–without fuelling inflationary pressures or short-term capital inflows. Credit is already expanding at a fast clip, driven by the public sector, and real estate. Continued growth in the nonhydrocarbon sector and implementation of infrastructure related projects will provide additional demand for credit. Against this backdrop, staff cautioned that banks and the QCB need to ensure that the overall credit quality does not weaken, particularly in the real estate sector in view of the prevailing excess supply, and the precarious global economic outlook.

The authorities agreed with staff's suggestion and might seek our assistance in developing a macroprudential framework. They were, however, of the view that the current excess supply in real estate would gradually converge with demand as Qatar's infrastructure projects get completed and the construction workers are replaced by white-collar workforce. They illustrated that the completion of the construction of the new airport would entail additional jobs for about 30,000 service-oriented and skilled workers to run the facility. Such new workers, in contrast to the current construction workers, are expected to migrate with their families, which would generate demand for other services such as hospitals, schools, entertainment, etc. Thus, the multiplier effect of additional job creation in any service industry on other service industries would generate additional demand for housing.

Composition of Domestic Credit, 2008–11
(In percent of total credit)



Source: Country authorities.
1/ General trade, industry, services, others, and outside Qatar.

17. **The QCB should monitor individual bank liquidity conditions and stand ready to relieve potential pressures.** The interest rate differential between local and foreign currency lending has led to a high demand for bank credit in foreign currency by residents.[11] This has resulted in an increase in foreign currency liabilities from the interbank, corporate, and public segments. Staff was of the view that a global foreign funding shock may generate some liquidity tightening in the domestic banking sector, which would need to be managed, particularly at individual bank-level. The QCB is monitoring the liquidity of individual banks for signs of stress and is confident that its prudential regulation on the foreign asset-liability position of banks and the requirement that banks lend in foreign currency only if corporates are able to generate revenues in foreign currency, both provide a built-in safeguard against potential liquidity squeeze and credit risk. Moreover, QCB indicated that a large part of the foreign currency loans were extended to a few large government-owned enterprises that were profitable and generated earnings in foreign currency; hence they were not concerned about credit risk.

[11] Lending to residents in foreign currency increased by $31 billion between December 2010 and October 2011 to $49 billion (46 percent of total loans and 27 percent to total assets of the banking system). A large proportion of demand for loans in foreign currency has been driven by government and private enterprises, some of which is in the real estate sector. On the liabilities side, borrowings from non-residents in foreign currency increased by $6 billion, central bank reserves fell by $16 billion, and the balance was covered by foreign currency deposits of public enterprises over the same period.

Box 2. Interest Rate Pass-Through in the GCC

The pass-through of policy rates varies among countries and over different time spans. In some countries, deposit rates are stickier than lending rates while in others the reverse is true. The pass-through of policy rates to lending rates is on the low side, possibly reflecting the shallowness of money markets in the GCC countries and banking sector regulations. Estimates for four GCC countries suggest that the interest rate pass-through was 0.30 and 0.50 for lending and deposit rates, respectively.[1]

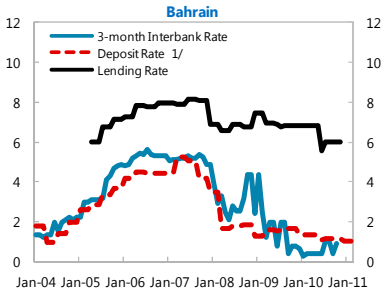
The long-term relationship between interbank rates and bank lending rates differs significantly between countries; it appears to be strongest for Bahrain and Kuwait; in Qatar, the relationship is weaker, though still significant for the deposit rate, while there is no relationship between rates in Oman.

Adjustment speeds implied by the short-term dynamics also differ across countries. Adjustment is relatively slow in Bahrain, with rates adjusting fully after 20 months; in Kuwait, the adjustment of deposit rates is also slow, with only half of the adjustment captured in the first 12 months after the shock; and in Oman and Qatar, an immediate effect on deposit and lending rates (albeit with a small sensitivity, of around 1/10th) is felt but most of the impact vanishes after six months.

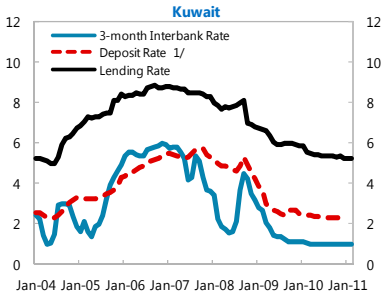
Continued efforts to develop the domestic financial markets will increase interest rate pass-through and strengthen monetary policy transmission. The narrowing of interest rate spreads between loans in foreign currency and local currency would also require reforms in the market to facilitate efficient pricing of risks for long-term borrowing by banks. To achieve this, there is a need to develop a well functioning money market and a liquid sovereign yield curve.

[1] Raphael Espinoza and Ananthakrishnan Prasad, Monetary Policy Transmission in the GCC Countries, IMF Working Paper, 2011, forthcoming.

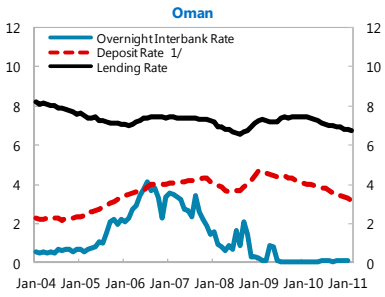
GCC: Interbank and Retail Interest Rates



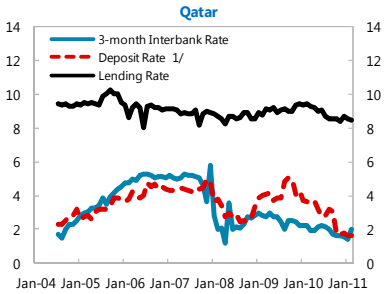
1/ Time deposit rate (3 month)



1/ Weighted average.



1/ Time deposit rate (weighted average).



1/ One year time deposit rate.

GCC: Long-term Sensitivity to Interbank Rate

Bahrain	0.63	0.29
Kuwait	0.8	0.74
Oman	-0.05	0.03
Qatar	0.02	0.01

Source: Espinoza and Prasad, IMF WP 2011, Forthcoming

18. **The exchange rate peg has served Qatar well as it provided a strong nominal anchor.** Preliminary estimates from CGER-type methodologies for exchange rate assessment broadly indicate an undervalued real effective exchange rate, narrowing over the medium term (Appendix 3).[12] The macroeconomic balance approach suggests that the Qatari Riyal is overvalued, which implies that Qatar should accumulate larger current account surpluses, given its fundamentals. The external sustainability approach suggests undervaluation, which would imply that Qatar should save less. The equilibrium real exchange rate approach also indicates undervaluation. The preconditions to sustain the peg, namely, a strong fiscal position, a sound banking system, and flexible labor and capital markets, are in place and should facilitate adjustment.

Results of CGER-type Analysis
(In percent of GDP)

	Projected CA	Norms	
		MB	ES
2010	26	33	18
2016	11	23	9

Source: IMF staff estimates and projections.

19. **Staff's medium-term fiscal sustainability exercise shows that compared to the last year, fiscal space has contracted somewhat because of the permanent increase in current expenditure.**[13] The bulk of government expenditure is still its current component, which has declined from its historical high of about 90 percent of total expenditure in 1990 to about 65 percent in FY 2010/11. The authorities are balancing the competing objectives of economic stabilization, development and generating intergenerational savings through fiscal policy. They pointed out that despite the increase in spending, the high hydrocarbon prices have enabled them to continue to generate cash flows to the State, and this trend would continue over the medium term.[14]

20. **Nevertheless, given the authorities' objective of fully financing the budget from 2020 onwards from its nonhydrocarbon revenues, and for building buffers for shocks, staff encouraged the authorities to save more (Figure 3).** With the nonhydrocarbon balance projected at around 25 percent of nonhydrocarbon GDP in 2016, this objective will take effort to be achieved. Staff pointed out that, in its benchmark scenario, projected nonhydrocarbon revenues financing of the total projected expenditure would increase from 52 percent to about 63 percent in 2016/17, implying additional efforts in the last four years. Expansion in the nonhydrocarbon sector and the eventual

[12] The model underpinning the macro balance relies on the methodology of Beidas-Strom and Cashin 2011, and yields a larger norm surplus for Qatar, compared to the analysis conducted during the 2010 Article IV Consultation, as it takes into account oil and gas wealth under the ground and the international investment position.

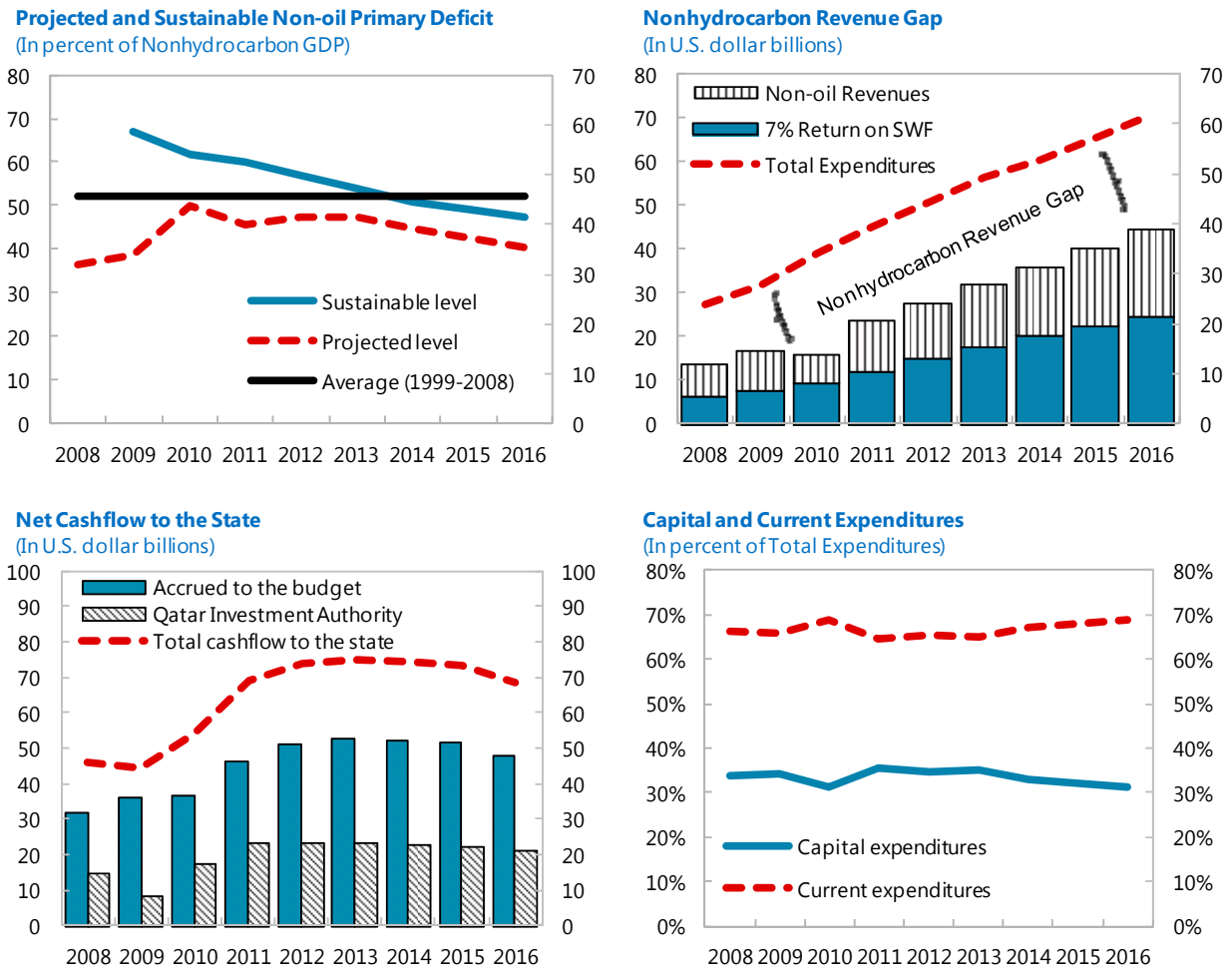
[13] The exercise targets a constant per capita annuity in real terms. The key parameters are calibrated as follows: (a) 27 billion barrels of oil reserves and 18.7 billion tons of gas reserves; (b) an initial government debt level of $36 billion; (c) annual population growth rate of 2.25 percent; and (d) a real interest rate of 4 percent.

(continued)

[14] Royalties from oil and gas revenues, corporate income taxes on oil revenues and net profits accrue from QP to the central government budget. The remaining oil and gas revenues accrue directly to the State of Qatar and are, among others, accumulated in the sovereign wealth fund (SWF). The combined royalties, corporate income tax, net profits of QP and the oil and gas revenues accumulated in the SWF comprise the cash flows to the State.

implementation of the value added tax (VAT) will significantly broaden the nonhydrocarbon tax base and therefore enable some increase in nonhydrocarbon fiscal revenues. On the expenditure side, given the plans for the announced large capital projects, adjustment in current expenditures would be the most feasible way to reduce the dependency of the budget on hydrocarbon revenues. The authorities are confident of achieving their objectives by 2020. They do not foresee any further adhoc increase in current expenditures, and remain committed to keeping capital expenditure at 40 percent of total expenditure in the medium term. The rationalization of the corporate tax rate, the broadening of the tax base, the non-renewal of tax holidays, and the introduction of the withholding tax, would increase corporate tax revenues in the future.

Figure 3. Qatar: Medium-Term Fiscal Stance, 2008–16



Sources: Country authorities; and IMF staff estimates.

B. STRENGTHENING AND DEVELOPING THE FINANCIAL SECTOR

21. **Staff's stress tests indicate that the banking system has the ability to withstand credit and market risks.** Nevertheless, as also highlighted in the Second Financial Stability Review of the QCB, staff underscored the need to monitor individual banks for stress, given the interlinkages in the financial system. Further, staff concurred with the QCB's analysis that banks' dependence on wholesale funding, though not significant, needs to be lowered to mitigate potential risks. Staff and the authorities agreed that enabling a more robust risk assessment culture, conducting regular stress testing of banks, and putting in place a framework for an early warning system would help mitigate risks to the banking system and strengthen financial stability.

Capital Adequacy Ratio of the Banking System December 2010

	NPLs			
Initial CAR= 17.1	5 percent	10 percent	15 percent	20 percent
Market down by 25 percent				
New banking system CAR	14.6	13.4	12.0	10.7
Number of banks below regulatory CAR	1	2	2	2
Recapitalization needs (in billions of U.S. dollars)	0.0	0.2	0.5	0.8
Market down by 50 percent				
New banking system CAR	13.3	12.0	10.6	9.2
Number of banks below regulatory CAR	2	2	3	5
Recapitalization needs (in billions of U.S. dollars)	0.2	0.5	0.8	1.7

Source: IMF staff calculations.

22. **Staff's analysis suggests that Qatari corporates also appear to be well-cushioned to withstand interest rate and income shocks.** Profits show a recovery compared to 2010. Interest Coverage Ratios (ICRs) for Q2 2011 were at 3.7 compared to 3.1 at end 2010, as a direct result of interest expenses decreasing by 43 percent (from $1.5 to $0.9) even though cash buffers decreased by 16 percent. ICRs with cash buffers stand at 18.3 in Q2 2011 compared to 13.1 at end-2010. The income shock—a 25 percent decline—also does not point to debt servicing pressures at the aggregate level.[15] Distance-to-default results indicate that default risks still remain low in 2011 compared to 2010.

GCC: ICR Performance Under an Interest Rate Shock, 2010-11

	200 bpts		500 bpts	
	ICR	ICR w/cash	ICR	ICR w/cash
Bahrain	17.9	25.5	7.9	14.7
Kuwait	2.5	7.6	1.9	5.7
Oman	5.3	9.4	3.7	6.5
Qatar[1]	2.2	9.1	1.4	6.8
Saudi Arabia	6.6	12.4	4.0	7.8
U.A.E.	2.0	34.7	0.1	0.3

Source: Renas Sidahmed; IMF Working Paper forthcoming.
[1]Qatar data is based on Q2 2011. All other countries are based on end 2010.

23. **Staff welcomes the steps taken to develop the money and bond markets.** Staff encourages the QCB to develop a formal liquidity management framework to facilitate a more proactive strategy in fine-tuning liquidity. In addition, coordination of debt management with the Ministry of Economy and Finance would be helpful in maintaining a stable and adequate stock of government securities for the further development of an interbank repo market, and also to provide a robust benchmark yield curve for the corporate bond market. In this context, staff welcomes the initiatives being taken by the High Level Financial Market Development Committee to list T-bills at

[15] By sectors: two (one industry and one services sector) out of the 34 listed companies have ICRs<1 or operating losses, with their debt accounting for 0.7 percent of the total debt.

Qatar Exchange from early 2012, and the efforts to develop a yield curve.

24. **Staff welcomes the progress toward the single regulatory regime.**[16] Other regulatory developments include the ban on Islamic banking windows in conventional banks (Appendix 4), and the imposition of quantitative and price ceilings on personal loans against salary assignment (Appendix 5). These changes seek to bring greater clarity to the regulatory framework, mitigate risks in the banking system as well as household debt, and usher in a more orderly credit growth. The approval by the Council of Ministers of the proposal to establish the single regulator is an encouraging development, and staff looks forward to its formal launch in early 2012.

25. **Staff noted that the authorities are considering strengthening the central bank law to address important legal issues arising in the context of the single regulatory regime.** They are also addressing issues related to Islamic banking to adapt to the new regulatory regime. Such refinements to address the Shariah dimensions of Islamic banking would help place the Islamic banking industry in Qatar on a firmer statutory footing.

26. **There is further scope to strengthen the supervision of real estate sector loans and improve the transparency of the real estate market.** Although prudential regulation for lending to real estate exists, given the existing excess capacity in real estate, staff is of the view that banks might be building up excessive risks in this sector, particularly in private real estate, which may materialize if the global economic and financial conditions worsen. The absence of comprehensive and timely data on the real estate market precludes banks from exercising proper risk assessment, and the central bank from conducting risk-based supervision. The QCB informed staff that it collects data at the municipality level, and is in the process of constructing a real estate price index, which would be ready for dissemination after three years. Staff suggested that collating and disseminating comprehensive price and volume data on Qatar's real estate market segments would help banks assess risks better and also enable the QCB to take informed preemptive regulatory measures to preserve financial stability. Additionally, staff encouraged the Qatari authorities to develop a corporate governance code for real estate developers that would contribute to the prevention of excessive risk-taking in the sector.

[16] The single financial regulator system would bring together the regulatory functions of the QCB, Qatar Financial Centre Regulatory Authority, Qatar Financial Markets Authority, and the insurance regulatory function.

C. BUILDING INSTITUTIONS AND ENHANCING TRANSPARENCY AND GOVERNANCE

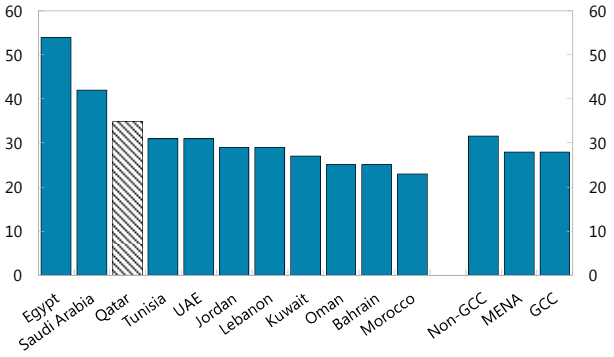
27. **Staff urged the acceleration of steps to establish a macro-fiscal unit that could develop a medium-term expenditure framework to ensure the efficiency of public spending.** The mission noted the steady progress being made in restructuring and modernizing operations in the Ministry of Economy and Finance. Important initiatives include the drafting of new financial and procurement laws (the latter to enable decentralized procurement and centralized monitoring); and developing an e-based tax system (currently at the tendering stage). The Ministry has initiated a move toward the preparation of a three-year budgeting framework. A solid medium-term expenditure framework would represent a critical building block for the eventual adoption of a fiscal rule to help manage the path of fiscal spending. In this context, accelerated steps should be taken to make the macro-fiscal unit operational to provide the foundation for the medium-term budgeting framework. The authorities are interested in receiving technical assistance (TA) from the Fund on setting up the macro-fiscal unit.

28. **Staff reiterated its recommendation to consolidate debt management and development functions in a debt office.** Currently, the debt office functions as a secretariat to the Ministerial State Finance Policy Committee. The maximum limit for borrowing is determined through an Emiri decree and the Committee decides on the timing, amount, maturity, and instrument type for each internal and external debt.

29. **Staff also encouraged the authorities to sustain efforts to strengthen public financial management.** In view of the large FIFA 2022 infrastructure-related expenditure, staff underscored the importance of adopting a Public Investment Management System to provide a coherent and rigorous set of procedures for project selection, appraisal, and programming that would enhance efficiency, accountability and governance. The authorities are reevaluating some of the major infrastructure projects (such as the metro) with a view to reassessing their size, structure, and financing and completion time, which in staff's view is a step in the right direction.

30. **Corporate governance practices need to be strengthened to help maintain financial stability.** The guidelines issued by the QCB in 2008 provide the framework for improving corporate governance in banks. Staff is of the view that the financial system would be strengthened by moving towards international good practices in some areas such as appointment of independent directors in bank boards. In light of the high credit concentration of Qatari banks, the mission encourages the authorities to have an in-depth diagnostic of bank governance that would highlight potential areas of improvement. This would be particularly useful since the QCB is rewriting the central bank Law—which addresses among others corporate governance issues—to make it more consistent with the single regulatory regime.

Bank Credit Concentration, 2010
(Top 20 Exposures/Total Loans)



Sources: Standard and Poor's, and The World Bank.

Box 3. Strengthening the Corporate Governance Code for Banks in Qatar

The global financial crisis has placed corporate governance (CG) firmly on the policy agenda. More than forty countries have issued new guidelines or amended corporate governance codes since the crisis.[1] The Basel Committee on Banking Supervision issued its Principles for Enhancing Corporate Governance in October 2010 identifying key areas of focus: board practices, senior management, risk management and internal controls, compensation, complex or opaque corporate structures, and disclosure and transparency.

The GCC countries have also issued corporate governance codes for banks: Bahrain issued a CG code in 2010, Kuwait issued its code for financial institutions in 2004, Oman in 2002, Qatar in 2008, Saudi Arabia has issued various guidelines over the years, and the UAE made its 2007 guidelines mandatory from 2010.

Select Corporate Governance Indicators for Qatari Banks in 2010

	Islamic	Conventional
Average total assets per bank (US $ Billion)	8.2	18.5
Average size of Board of Directors	9.0	9.5
Average number of executive members	3.8	4.5
Average number of members with expertise		
Banking and insurance	5.3	4.7
Petroleum and natural gas	0.3	0.5
Board meetings		
Average number of meetings	4.5	7.7

Source: Qatar Central Bank, Second Financial Stability Review

[1] Some examples being the corporate governance and stewardship codes and the Walker Report in the UK, green paper on CG in financial institutions by the European Commission, the US Dodd-Frank proposals in the U.S.

Despite considerable progress, there are still some gaps in implementation of the CG codes, including in transparency and disclosure, exemptions for related-party lending, and the structure of the board in the GCC countries.[2]

The guidelines issued by the QCB in 2008 provide the framework for improving corporate governance in Qatari banks, but some of the codes prescribed by the central bank are superseded by other laws, such as the Commercial Companies Law. The financial system would be strengthened by moving towards international good practices notably by implementing the necessary changes to the Commercial Companies Law to facilitate the appointment of independent directors to bank boards, and encouraging the continued strengthening of banks' risk management practices especially in the area of real estate lending.

[2] Hawkamah, The Institute for Corporate Governance.

D. ECONOMIC DIVERSIFICATION AND STRUCTURAL ISSUES

31. **Reducing Qatar's vulnerability to hydrocarbon price fluctuations will require, in addition to fiscal management, diversification into other sectors of the economy and reinforcing competitiveness.** This will necessitate raising productivity through greater use of the latest technologies, increasing the efficiency of investments, fostering more openness to foreign competition, and enhancing the quality of labor. These aspects have been articulated in the government's National Development Strategy (NDS) for 2011–16. Improving the efficiency of fiscal spending could help improve productivity during the transition.

32. **Opportunities for efficiency gains and reducing distortions in petrol, energy, and water use exist by reducing, among others, direct and indirect subsidies.** According to Qatar's NDS, a drive for efficiency is central to creating and capturing value, preserving and expanding a productive base, and encouraging the private sector to develop through economic diversification. Increasing petrol pump prices by 25 percent in January 2011 to QR1 per liter is a step in the right direction. Free electricity and water for nationals and subsidized tariffs for expatriates tend to increase inefficiency in the use of these resources. Fiscal expenditure to compensate for the losses of the water and electricity utility company is budgeted at QR1.8 billion in 2011/12 (0.3 percent of GDP), and is expected to grow in line with population growth and industrial development. Qatar has been rapidly developing its petrochemical industry based on local feedstock produced at low cost. Natural gas feedstock prices charged for Qatari petrochemical companies have been on the rise, but continue to be lower than spot and contracted Qatari export prices. The authorities reiterated that currently there are no plans to review any of the subsidies.

33. **Staff and the authorities agreed that it is opportune to consider options for deeper pension reforms.** The recent salary hike of 60 to 120 percent for civilian Qatari public sector employees and military personnel was also extended to pensioners. The authorities confirmed that transfers to the pension fund to meet the increased cash outflows and the actuarial deficit would be predominantly in the form of assets. Staff suggested that reforms to rebasing of pension payments over the average of the last few years of service instead of the last month's salary, increasing the retirement age, raising the early retirement age, and changes to the investment policy to improve the risk-return profile, need to be implemented in conjunction with the cash and assets transfers to the pension fund with a view to strengthening it.

E. STATISTICAL AND OTHER ISSUES

34. **Timely compilation and dissemination of key statistics remain essential for adequate economic management.** Significant progress has been achieved in the collation and dissemination of national accounts and inflation data, and sovereign external debt statistics. Since the September 2010 TA mission on balance of payments statistics, the authorities have made progress in implementing the mission's recommendations, including compiling balance of payments data in the international format needed for publication in the *International Financial Statistic (IFS)*. Staff encouraged the authorities to pursue their efforts in strengthening economic statistics, including working towards the compilation of an International Investment Position (IIP) statement.

35. **The mission commends the authorities on their ongoing efforts in strengthening Qatar's Anti Money Laundering (AML)/Combating Financing of Terrorism (CFT) framework.** The domestic financial supervisory authorities' legislation (Rules/Regulations) has been developed by adopting a coordinated approach, which has resulted in the legislation being consistent across each supervisory body. Following the adoption of the new reviewed AML/CFT rules/regulations, financial supervisory authorities have increased their offsite and onsite reviews of AML/CFT compliance at financial institutions that are subject to their supervision. Progress has also been achieved with regard to implementing the United Nations Security Council Resolutions in the areas of strengthening mechanisms for implementation and training of supervisors.

STAFF APPRAISAL

36. **Qatar is using its fiscal space, generated from an increase in hydrocarbon production and prices, to implement a large public spending program.** Large infrastructure investments are expected to sustain strong growth of 9 to 10 percent in the nonhydrocarbon sector in the medium term.

37. **Headline inflation is projected to remain subdued, but inflation risks have risen due to domestic factors.** The potential inflationary effect of the recent fiscal package is estimated to be around 1 percentage point. This underscores the need for fiscal policy to monitor aggregate demand and for the QCB to manage liquidity.

38. **The expansionary fiscal stance in 2011/12 thus warrants careful monitoring of aggregate demand to ward off risks of inflation.** Fiscal policy must continue to maintain a careful balance between spending on infrastructure to sustain non-inflationary growth, and saving and investing hydrocarbon surpluses abroad to generate sufficient income to finance future budgets.

39. **In the context of the peg, the QCB would need to manage liquidity more actively.** The QCB would need to develop a formal liquidity management framework to facilitate a more proactive strategy in fine-tuning liquidity. In addition, coordination of debt management with the Ministry of Economy and Finance would be helpful in maintaining a stable and adequate stock of government securities for the further development of an interbank repo market, and also providing a robust benchmark yield curve for the corporate bond market.

40. **Developing a more formal and transparent macroprudential policy framework to enable a swift response when needed, would help achieve orderly credit growth without generating overheating.** The main challenges for monetary policy will be to support credit growth without fuelling inflationary pressures or short-term capital inflows. Against the backdrop of increasing credit growth, banks and the QCB need to be cautious that overall credit quality does not weaken, particularly in the real estate sector in view of the prevailing excess supply. Collating and disseminating price and volume data on Qatar's real estate market segments would help banks assess risks better and also enable the central bank to take informed preemptive measures to preserve financial stability.

41. **The banking system has the ability to withstand credit and market risks.** Nevertheless, staff underscores the need to monitor individual banks for stress, given the interlinkages in the financial system. Further, individual banks' foreign currency liquidity conditions need to be monitored and the QCB should stand ready to relieve potential pressures. Enabling a more robust risk assessment culture, conducting regular stress testing of banks, and putting in place an early warning system would help mitigate risks to the banking system and maintain financial stability.

42. **In the medium term, fiscal policy will need to balance sometimes competing objectives of economic stabilization, development and generating intergenerational savings.** Fiscal space has contracted somewhat compared to last year, because of the permanent increase in current expenditure, according to staff's medium-term fiscal sustainability exercise. Given the authorities' objective of fully financing the budget from 2020 onwards from its nonhydrocarbon revenues, and for building buffers for shocks, the authorities will need to increase savings over the medium term. While the eventual implementation of VAT will increase fiscal revenues, on the expenditure side, given the plans for the implementation of large capital projects, adjustment in current expenditures would be the most feasible way to reduce the dependency of the budget on hydrocarbon revenues.

43. **Establishing a macro-fiscal unit would support fiscal policy making and the development of a medium-term budget framework to ensure the efficiency of public spending.** A solid medium-term expenditure framework would represent a critical building block for the eventual adoption of a fiscal rule to help manage the path of fiscal spending.

44. **Reducing Qatar's vulnerability to hydrocarbon price fluctuations will require, in addition to fiscal management, diversification into other sectors of the economy and reinforcing competitiveness.** Opportunities for efficiency gains and reducing distortions in petrol, energy, and water use exist by reducing, among others, direct and indirect subsidies. It is also opportune to consider options for deeper pension reforms.

45. **Further improvements in statistics will be essential, which will also require greater coordination across agencies**.

46. **It is recommended that the next Article IV consultation take place on the standard 12-month cycle.**

Table 1. Qatar: Selected Macroeconomic Indicators, 2007–12

(Quota: SDR 302.6 million)
(Population: 1.7 million, mid-2011 estimate)
(Per capita income: $98,000, 2011 estimate)

	2007	2008	2009	2010	Proj. 2011	Proj. 2012
National income, production, and prices			(Percent change, unless otherwise indicated)			
Nominal GDP (in million Qatari Riyals)	289,551	418,672	355,204	463,490	629,653	654,928
Nominal hydrocarbon GDP (in million Qatari Riyals)	150,014	230,312	159,467	239,745	388,409	387,348
Nominal GDP (in million U.S. dollars)	79,547	115,020	97,583	127,332	172,982	179,925
Nominal GDP per capita (in U.S. dollars)	64,872	79,409	59,545	74,901	97,840	97,853
Real GDP growth (in percent per annum)	18.0	17.7	12.0	16.6	18.8	6.0
Hydrocarbon 1/	13.8	13.2	4.5	28.8	31.1	2.9
Nonhydrocarbon	21.6	21.3	17.6	8.4	9.0	9.0
Crude oil output (in thousand barrels per day)	839	836	792	789	756	739
LNG production (in million tons per year)	29.9	31.5	36.0	55.0	74.8	77.0
Oil export price (in U.S. dollars per barrel)	70.0	96.9	62.6	77.4	101.1	97.94
CPI period average	13.8	15.0	-4.9	-2.4	2.0	4.0
Public finance			(In percent of GDP on fiscal year basis) 2/			
Total revenue	36.6	35.0	44.2	30.9	32.9	35.1
Hydrocarbon revenue	22.0	19.9	21.7	19.2	18.0	18.0
Other revenue	14.6	15.1	22.6	11.7	14.9	17.2
Total expenditure and net lending	26.8	24.7	30.0	28.2	25.7	28.0
Current expenditure	16.3	16.3	19.7	19.4	16.6	18.3
Capital expenditure (including net lending)	10.5	8.3	10.3	8.8	9.1	9.7
Overall fiscal balance	9.8	10.4	14.3	2.7	7.2	7.2
Excluding hydrocarbon revenue	-12.2	-9.5	-7.4	-16.5	-10.8	-10.8
Nonhydrocarbon fiscal balance in percent of nonhydrocarbon GDP	-25.8	-20.1	-14.0	-36.5	-27.7	-26.0
Money and credit			(Annual change in percent)			
Broad money	39.5	19.7	16.9	23.1	24.8	20.8
Net foreign assets	0.3	-20.5	-4.2	35.9	-24.3	25.8
Net domestic assets	88.6	47.0	24.0	19.5	40.4	20.0
Domestic credit	66.1	48.7	2.0	14.2	19.9	13.2
Claims on public enterprises	198.1	77.1	-16.1	30.5	35.9	4.0
Claims on private sector	51.3	42.4	7.0	10.6	15.8	15.9
External sector			(In million U.S. dollars, unless otherwise stated)			
Trade balance	24,318	42,077	24,476	51,834	76,836	74,425
Exports	44,142	67,212	46,928	79,070	106,202	106,997
Of which: Crude oil and refined petroleum products	21,083	29,438	18,384	29,099	35,249	35,534
LNG and related exports	18,710	32,267	23,947	43,535	61,938	61,330
Other	4,349	5,507	4,598	6,436	9,016	10,134
Imports	-19,824	-25,135	-22,452	-27,237	-29,367	-32,573
Current account	20,186	33,039	9,987	33,531	48,660	47,290
In percent of GDP	25.4	28.7	10.2	26.3	28.1	26.3
Central bank reserves, gross	9,753	9,837	18,352	30,720	20,703	24,412
In months of imports of goods and services 3/	3.3	3.9	5.8	8.4	5.4	5.8
			(In million U.S. dollars, unless otherwise stated)			
Total external debt (excluding banks)	24,762	33,453	50,259	70,757	87,409	89,535
In percent of GDP	31.1	29.1	51.5	55.6	50.5	49.8
Government external debt	2,871	3,868	12,760	16,995	21,397	22,710
In percent of GDP	3.6	3.4	13.1	13.3	12.4	12.6
Debt service (excluding banks, in percent of GDP)	4.2	2.8	3.3	4.9	3.1	2.7
Memorandum Items:						
Exchange rates (Riyal/U.S. dollars)	3.64	3.64	3.64	3.64	3.64	3.64
Real effective exchange rate (percent change, 2000=100)	5.1	6.3	-1.4	-5.1	...	...
Credit rating (Moody's investor services)	Aa2	Aa2	Aa3	Aa2	...	...
Stock market index (cumulative growth, 2001=100)	566	407	411	513		

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

1/ Staff estimates; include crude oil, LNG, propane, butane, and condensate.
2/ Fiscal year begins in April.
3/ Next 12 months.

Table 2a. Qatar: Summary of Government Finance, 2006/07–2011/12 1/

(In million Qatari Riyals)

	2006/07	2007/08	2008/09	2009/10	Prel. 2010/11	Proj. 2011/2012
Revenue	86,062	117,865	140,993	169,095	155,908	209,464
Hydrocarbon	55,429	70,748	80,009	82,807	96,849	114,687
Oil	48,181	60,050	61,245	61,742	58,639	67,603
LNG-related	7,248	10,698	18,764	21,065	38,210	47,084
LNG (royalties)	7,248	10,698	18,764	21,065	38,210	47,084
Non-hydrocarbon	30,634	47,117	60,984	86,288	59,059	94,777
Investment income from public enterprises 2/	20,702	30,346	33,271	53,879	36,090	53,165
Corporate tax revenue	4,562	8,939	14,629	21,575	14,524	33,891
Other nontax revenue	5,370	7,832	13,084	10,834	8,445	7,721
Expenditure	67,147	86,249	99,294	114,574	142,370	163,460
Expense	49,751	52,316	65,817	75,334	98,127	105,461
Compensation of employees	12,993	16,003	18,661	21,617	23,065	31,040
Interest payments	2,006	1,856	2,100	3,598	5,577	8,416
Interest on domestic debt	865	768	721	1,597	2,596	5,535
Interest on foreign debt	1,141	1,088	1,379	2,001	2,981	2,881
Foreign grants	1,978	1,476	1,115	592	1,061	516
Goods and services 3/	31,661	26,594	34,788	41,455	53,236	58,360
Other expense 4/	1,113	6,387	9,153	8,072	15,188	7,129
Net acquisition of nonfinancial assets	17,396	33,933	33,477	39,240	44,243	57,999
Gross operating balance	36,311	65,549	75,176	93,761	57,781	104,003
Net lending (+)/borrowing (-)	18,915	31,616	41,699	54,521	13,538	46,004
Nonhydrocarbon fiscal balance	-36,514	-39,132	-38,310	-28,286	-83,311	-68,683
Net acquisition of financial assets	16,370	36,490	53,984	117,114	69,979	108,136
Net incurrence of liabilities	-2,545	4,874	12,285	62,593	56,441	62,132
Total government debt	28,910	25,749	46,972	110,111	156,523	214,524
Government external debt	12,526	12,081	28,387	65,318	70,269	93,019
Government gross domestic debt	16,384	13,668	18,585	44,793	86,254	121,506
Government net domestic debt (net of deposits)	7,973	2,615	4,715	28,414	69,654	101,038
External debt service/total revenue (in percent)	1.3	0.9	1.0	1.2	1.9	1.4
Nominal GDP (on a fiscal year basis)	238,424	321,832	402,805	382,275	505,031	635,972

Sources: Ministry of Economy and Finance; and IMF staff estimates and projections.

1/ On a fiscal year basis, April–March. GDP is also converted into fiscal year basis.

2/ Includes investment income of state-owned hydrocarbon enterprises.

privatization receipts of Industries Qatar, shares of which were formerly owned by Qatar Petroleum.

3/ Includes transfers to ministries and public enterprises less interest payments and grants.

4/ Corresponds to Chapter III "Minor capital expenses" in the budget.

Table 2b. Qatar: Summary of Government Finance, 2006/07–2011/12 1/

(In percent of GDP)

	2006/07	2007/08	2008/09	2009/10	Prel. 2010/11	Proj. 2011/12
Revenue	36.1	36.6	35.0	44.2	30.9	32.9
Hydrocarbon	23.2	22.0	19.9	21.7	19.2	18.0
Oil	20.2	18.7	15.2	16.2	11.6	10.6
LNG-related royalties	3.0	3.3	4.7	5.5	7.6	7.4
Non-hydrocarbon	12.8	14.6	15.1	22.6	11.7	14.9
Investment income from public enterprises 2/	8.7	9.4	8.3	14.1	7.1	8.4
Corporate tax revenue	1.9	2.8	3.6	5.6	2.9	5.3
Other nontax revenue	2.3	2.4	3.2	2.8	1.7	1.2
Expenditure	28.2	26.8	24.7	30.0	28.2	25.7
Expense	20.9	16.3	16.3	19.7	19.4	16.6
Compensation of employees	5.4	5.0	4.6	5.7	4.6	4.9
Interest payments	0.8	0.6	0.5	0.9	1.1	1.3
Interest on domestic debt	0.4	0.2	0.2	0.4	0.5	0.9
Interest on foreign debt	0.5	0.3	0.3	0.5	0.6	0.5
Foreign grants	0.8	0.5	0.3	0.2	0.2	0.1
Goods and services 3/	13.3	8.3	8.6	10.8	10.5	9.2
Other expense 4/	0.5	2.0	2.3	2.1	3.0	1.1
Net acquisition of nonfinancial assets	7.3	10.5	8.3	10.3	8.8	9.1
Gross operating balance	15.2	20.4	18.7	24.5	11.4	16.4
Net lending (+)/borrowing (-)	7.9	9.8	10.4	14.3	2.7	7.2
Nonhydrocarbon fiscal balance	-15.3	-12.2	-9.5	-7.4	-16.5	-10.8
Nonhydrocarbon fiscal balance (in percent of nonhydrocarbon GDP)	-32.4	-25.8	-20.1	-14.0	-36.5	-27.7
Net acquisition of financial assets	6.9	11.3	13.4	30.6	13.9	17.0
Net incurrence of liabilities	-1.1	1.5	3.0	16.4	11.2	9.8
Memorandum items:						
Total government debt	12.1	8.0	11.7	28.8	31.0	33.7
Government external debt	5.3	3.8	7.0	17.1	13.9	14.6
Government gross domestic debt	6.9	4.2	4.6	11.7	17.1	19.1
Government net domestic debt (net of deposits)	3.3	0.8	1.2	7.4	13.8	15.9

Sources: Ministry of Economy and Finance; and IMF staff estimates and projections.

1/ On a fiscal year basis, April–March. GDP is also converted into fiscal year basis.
2/ Includes investment income of state-owned hydrocarbon enterprises.
3/ Includes transfers to ministries and public enterprises less interest payments and grants.
4/ Corresponds to Chapter III "Minor capital expenses" in the budget.

Table 3. Qatar: Depository Corporations Survey, 2007–12

	2007	Sep-08	2008	2009	2010	Proj. 2011	Proj. 2012
			(In million Qatari Riyals)				
Net foreign assets	61,444	79,696	48,869	46,835	63,637	48,175	60,587
QCB	34,747	39,154	35,790	66,800	111,821	75,357	88,860
Assets	35,500	39,221	35,808	68,252	113,262	76,798	90,301
Liabilities	753	67	18	1,452	1,441	1,441	1,441
Commercial banks	26,696	40,542	13,079	-19,965	-48,185	-27,183	-28,274
Assets	88,961	109,847	99,169	88,495	91,125	113,793	118,361
Liabilities	62,265	69,305	86,089	108,460	139,309	140,976	146,635
Net domestic assets	92,292	115,977	135,631	168,247	201,079	282,272	338,753
Claims on government (net)	-207	2,644	-7,223	18,843	55,849	95,271	101,354
Claims	13,822	19,135	13,206	34,722	75,004	120,006	126,006
Deposits 1/	14,029	16,490	20,429	15,880	19,154	24,735	24,652
Domestic credit	147,840	199,686	219,823	224,305	256,050	306,945	347,415
Claims on public sector (net)	26,545	35,849	40,161	58,578	107,698	165,707	174,617
Claims on public enterprises 2/	26,752	33,205	47,384	39,735	51,848	70,436	73,263
Claims on private sector	121,088	166,482	172,439	184,570	204,202	236,508	274,152
Other items (net)	-55,341	-86,354	-76,970	-74,900	-110,820	-119,944	-110,016
Broad money	153,735	195,672	184,005	215,082	264,716	330,447	399,340
Money	40,737	61,265	50,870	53,116	68,337	97,919	141,429
Currency in circulation	4,487	5,755	5,368	5,653	6,095	13,189	13,850
Demand deposits	36,250	55,510	45,501	47,463	62,242	84,730	127,578
Quasi-money	112,999	134,408	133,136	161,966	196,379	232,527	257,911
Savings and time deposits	64,349	84,010	85,676	133,193	166,995	190,093	215,084
Foreign currency deposits	48,650	50,398	47,459	28,773	29,384	42,434	42,827
			(Annual percent changes)				
Net foreign assets	0.3	48.0	-20.5	-4.2	35.9	-24.3	25.8
Net domestic assets	88.6	36.3	47.0	24.0	19.5	40.4	20.0
Domestic credit	66.1	47.2	48.7	2.0	14.2	19.9	13.2
Claims on public enterprises	198.1	19.4	77.1	-16.1	30.5	35.9	4.0
Claims on private sector	51.3	54.4	42.4	7.0	10.6	15.8	15.9
Broad money	39.5	28.7	19.7	16.9	23.1	24.8	20.8
Savings and time deposits	62.4	57.5	33.1	55.5	25.4	13.8	13.1
Memorandum items:							
Net claims on public enterprises	-9,350	-10,195	-9,038	-13,031	13,170	17,891	18,609
Velocity of broad money (to nonhydrocarbon GDP)	0.91	1.14	1.02	0.91	0.84	0.73	0.67

Sources: Qatar Central Bank (QCB); and IMF staff estimates and projections.

1/ Includes foreign and local currency deposits.

2/ Nonfinancial enterprises with government share.

Table 4. Qatar: Balance of Payments, 2007–12
(In million U.S. dollars)

	2007	2008	2009	2010	Proj. 1/ 2011	Proj. 1/ 2012
Current account	20,186	33,039	9,987	33,531	48,660	47,290
In percent of GDP	25.4	28.7	10.2	26.3	28.1	26.3
Trade balance	24,318	42,077	24,476	51,834	76,836	74,425
Exports	44,142	67,212	46,928	79,070	106,202	106,997
Hydrocarbon	39,793	61,705	42,331	72,634	97,187	96,863
Crude oil	19,181	26,270	16,217	21,951	24,952	23,631
LNG	10,524	17,640	13,074	23,394	36,775	36,697
Propane, butane	1,617	3,607	2,887	5,283	6,769	6,782
Condensates	6,569	11,020	7,986	14,858	18,394	17,851
Refined petroleum products	1,902	3,168	2,167	7,148	10,297	11,902
Non-hydrocarbon	4,349	5,507	4,598	6,436	9,016	10,134
Petrochemicals	2,385	2,908	2,141	4,045	6,401	7,115
Others	1,964	2,599	2,457	2,391	2,615	3,019
Imports	-19,824	-25,135	-22,452	-27,237	-29,367	-32,573
Non-LNG/QP goods	-11,791	-15,917	-16,793	-18,475	-19,920	-22,095
LNG related	-3,577	-4,364	-4,052	-2,805	-1,247	-2,935
QP project-related imports	-4,456	-4,855	-1,607	-5,956	-8,200	-7,543
Services (net)	-983	-4,096	-6,316	-8,132	-9,513	-7,976
Income (net)	1,297	1,762	-449	-1,633	-3,680	-2,727
Receipts 2/	3,740	4,250	1,674	1,567	8,207	8,643
Payments 3/	-2,443	-2,487	-2,123	-3,200	-11,888	-11,369
Transfers (net)	-4,446	-6,704	-7,724	-8,537	-14,982	-16,432
Of which: workers remittances	-3,827	-4,348	-8,848	-9,739	-10,508	-11,665
Capital account	-1,131	-1,360	-1,796	-1,976	-2,131	-2,363
Financial account	-16,148	-29,083	2,135	-7,800	-56,547	-41,217
Direct Investment, net	4,700	3,516	4,950	-664	512	439
Portfolio borrowing, net	794	-137	254	1,066	-7,465	-8,535
Assets	-780	-1,248	-1,248	-1,248	-9,797	-10,911
Liabilities	1,574	1,111	1,502	2,314	2,332	2,376
Other investment (net)	-12,361	-15,790	-6,516	1,967	3,233	-16,277
Assets	-17,637	-24,481	-23,322	-18,531	-13,419	-18,403
Trade credits	567	2,019	-1,026	4,075	5,421	2,579
Other government external assets 4/	-18,204	-26,500	-22,296	-22,606	-18,840	-20,983
Liabilities	5,276	8,691	16,806	20,498	16,652	2,126
Commercial banks, net	4,083	3,741	9,078	7,753	-5,770	300
Other capital, net	-13,363	-20,414	-5,631	-17,921	-47,057	-17,143
Errors and omissions	1,229	-2,310	-2,206	-11,384	0	0
Overall balance	4,136	286	8,120	12,371	-10,018	3,710
Change in QCB net foreign assets	-4,136	-286	-8,120	-12,371	10,018	-3,710

Sources: Qatar Central Bank; and IMF staff estimates and projections.

1/ Data related to income, transfers, services and capital and financial accounts reflect improved coverage; hence they may not be strictly comparable with previous years

2/ Includes staff estimates for QIA.

3/ Includes staff estimates for commercial banks.

4/ IMF staff estimates.

Table 5. Qatar: Vulnerability Indicators, 2006–11

(In percent; unless otherwise indicated)

	2006	2007	2008	2009	Est. 2010	Est. 2011
External solvency indicators						
REER (CPI based - end of period)	8.4	5.1	6.3	-1.4	-5.1	-
Total debt (in billion U.S. dollars, including commercial banks)	26.3	41.9	57.1	80.1	109.0	126.1
Of which: LNG-related	10.9	14.1	17.1	19.7	20.4	21.3
Total debt (in percent of GDP)	43.2	52.6	49.6	82.0	85.6	72.9
Debt service/exports of goods and services	14.8	19.9	27.6	54.8	40.6	36.6
Public sector solvency indicators						
Government gross domestic debt/GDP	6.9	4.2	4.6	11.7	17.1	19.1
Government net domestic debt/GDP 1/	3.3	0.8	1.2	7.4	13.8	15.9
Government external debt/GDP 2/	5.3	3.8	7.0	17.1	13.9	14.6
Total debt service/total revenue	7.2	3.0	2.6	2.4	8.6	7.9
Interest payments/total revenue	2.3	1.6	1.5	2.1	3.6	4.0
Hydrocarbon revenue/total revenue	64.4	60.0	56.7	49.0	62.1	54.8
External liquidity indicators (in million U.S. dollars)						
Central bank net reserves	5,410	9,546	9,832	18,352	30,720	20,703
In months of imports	2.4	3.3	3.9	5.8	8.4	5.4
Commercial banks net foreign assets (in million U.S. dollars)	11,417	7,334	3,593	-5,485	-13,238	-7,468
Foreign assets	18,217	24,440	27,244	24,312	25,034	31,262
Foreign liabilities	6,801	17,106	23,651	29,797	38,272	38,730
Crude oil exports/total exports	50.9	47.8	43.8	39.2	36.8	33.2
Financial sector indicators						
Foreign currency deposits/total deposits	34.9	32.6	26.6	13.7	11.4	13.4
Net domestic credit (percent change)	33.7	59.2	44.0	14.4	28.3	29.0
Private sector credit (percent change)	45.9	51.3	42.4	7.0	10.6	15.8
Net domestic credit/GDP	41.9	51.0	50.8	68.5	67.3	63.9
Private credit/total assets of banks	42.2	41.1	42.9	39.4	36.0	38.8
Market assessment/financial market indicators						
Stock market index (end of period)	7,133	9,580	6,886	6,959	8,682	…
Moody's investor services	Aa2	Aa2	Aa2	Aa3	Aa2	…
Standard and Poor's 3/	AA-	AA-	AA-	AA-	AA-	…

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

1/ Net of government deposits with resident banks.

2/ Fiscal year basis.

3/ Long-term foreign currency rating.

Table 6. Qatar: Medium-Term Baseline Scenario, 2008–16

(In million Qatari Riyals, unless otherwise indicated)

	2008	2009	2010	Projections 2011	2012	2013	2014	2015	2016
				(Percent change, unless otherwise indicated)					
National income, production, and prices									
Nominal GDP (in million Qatari Riyals)	418,672	355,204	463,490	629,653	654,928	680,880	708,441	754,818	801,830
Real GDP	17.7	12.0	16.6	18.8	6.0	4.6	4.6	5.9	5.9
Hydrocarbon 1/	13.2	4.5	28.8	31.1	2.9	-0.3	-1.2	0.3	0.0
Nonhydrocarbon GDP	21.3	17.6	8.4	9.0	9.0	9.0	9.5	10.0	10.0
Crude oil production, in thousand barrels per day	836	792	789	756	739	705	631	590	499
LNG Production (in million tons)	31.5	36.0	55.0	74.8	77.0	77.0	77.0	77.0	77.0
Qatar oil export price (in U.S. dollars per barrel)	96.9	62.6	77.4	101.1	97.9	97.4	95.5	94.5	93.5
CPI period average	15.0	-4.9	-2.4	2.0	4.0	4.0	4.0	5.0	5.0
Terms of trade	27.3	-26.2	14.1	17.5	-2.8	-0.1	-1.4	-0.9	-1.2
				(In million Qatari Riyals)					
Central government finances 2/									
Total revenue	140,993	169,095	155,908	209,464	232,446	241,740	244,174	251,410	266,379
Hydrocarbon revenue	80,009	82,807	96,849	114,687	118,730	121,177	114,897	112,352	116,792
Other revenue	60,984	86,288	59,059	94,777	113,715	120,563	129,277	139,058	149,587
Total expenditure	99,294	114,574	142,370	163,460	185,123	204,522	218,808	237,933	258,097
Expense	65,817	75,334	98,127	105,461	120,810	133,157	146,808	161,933	178,097
Net acquisition of non-financial assets	33,477	39,240	44,243	57,999	64,313	71,365	72,000	76,000	80,000
Net lending (+)/borrowing (-)	41,699	54,521	13,538	46,004	47,323	37,218	25,366	13,477	8,283
In percent of GDP	10.4	14.3	2.7	7.2	7.2	5.4	3.5	1.8	1.0
Nonhydrocarbon balance	-38,310	-28,286	-83,311	-68,683	-71,408	-83,959	-89,531	-98,875	-108,509
In percent of GDP	-9.5	-7.4	-16.5	-10.8	-10.8	-12.2	-12.4	-12.9	-13.2
In percent of nonhydrocarbon GDP	-20.1	-14.0	-36.5	-27.7	-26.0	-27.5	-26.2	-25.5	-24.7
Government net debt 3/	33,101	93,732	139,923	194,056	195,466	183,383	183,114	174,402	182,559
In percent of GDP	7.9	26.4	30.2	30.8	29.8	26.9	25.8	23.1	22.8
External debt service (percent of total revenue)	2.1	1.5	6.9	5.3	1.2	8.0	3.9	7.2	0.6
				(In million U.S. dollars, unless otherwise indicated)					
External sector									
Current account	33,039	9,987	33,531	48,660	47,290	46,710	40,663	33,827	25,108
In percent of GDP	28.7	10.2	26.3	28.1	26.3	25.0	20.9	16.3	11.4
Trade balance	42,077	24,476	51,834	76,836	74,425	70,874	64,238	56,905	46,993
Exports	67,212	46,928	79,070	106,202	106,997	106,966	104,444	102,003	97,538
Crude oil and refined petroleum products	29,438	18,384	29,099	35,249	35,534	34,631	30,491	28,135	23,985
LNG and related exports	32,267	23,947	43,535	61,938	61,330	61,085	62,457	61,760	61,493
Other exports	5,507	4,598	6,436	9,016	10,134	11,250	11,497	12,109	12,059
Imports	-25,135	-22,452	-27,237	-29,367	-32,573	-36,092	-40,206	-45,098	-50,544
LNG related	-4,364	-4,052	-2,805	-1,247	-2,935	-3,957	-4,957	-5,957	-5,957
Project related imports	-4,855	-1,607	-5,956	-8,200	-7,543	-7,653	-7,976	-8,181	-9,473
Other imports	-15,917	-16,793	-18,475	-19,920	-22,095	-24,482	-27,273	-30,960	-35,114
Volume of exports (percent change)	14.0	5.4	33.7	4.5	3.6	0.4	-0.6	-1.5	-3.5
Volume of imports (percent change)	20.8	-0.5	9.9	-1.4	10.9	11.2	11.9	12.2	11.7
Services, net	-4,096	-6,316	-8,132	-9,513	-7,976	-7,871	-7,681	-6,785	-5,888
Income, net	1,762	-449	-1,633	-3,680	-2,727	1,723	3,950	4,873	6,513
Current transfers, net	-6,704	-7,724	-8,537	-14,982	-16,432	-18,016	-19,844	-21,166	-22,511
Overall balance	286	8,120	12,371	-10,018	3,710	1,954	1,560	-203	-562
Central bank reserves, net	9,832	18,352	30,720	20,703	24,412	26,366	27,926	27,722	27,160
In months of imports of goods and services 4/	3.9	5.8	8.4	5.4	5.8	5.8	5.6	5.1	6.2
Total external debt (excluding banks)	33,453	50,259	70,757	87,409	89,535	93,405	94,824	92,403	91,101
Total external debt (excluding banks, in percent of GDP)	29.1	51.5	55.6	50.5	49.8	49.9	48.7	44.6	41.4
Total external debt service (excluding banks)	3,264	3,204	6,191	5,336	4,796	9,241	7,601	9,956	5,468
In percent of exports of goods and services	4.5	6.6	7.6	4.8	4.3	8.2	6.8	9.1	5.1
In percent of GDP	2.8	3.3	4.9	3.1	2.7	4.9	3.9	4.8	2.5
				(In Percent of GDP)					
Saving-investment balance									
Gross investment	29.4	36.0	30.4	26.0	27.3	28.4	28.9	29.2	29.7
Nongovernment sectors	21.4	25.3	21.1	17.3	17.7	18.2	18.8	19.3	19.8
Gross national saving	58.1	46.2	56.8	54.1	53.6	53.4	49.8	45.5	41.1
Nongovernment sectors	38.4	17.3	37.8	35.5	32.6	32.9	31.2	28.9	25.4

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

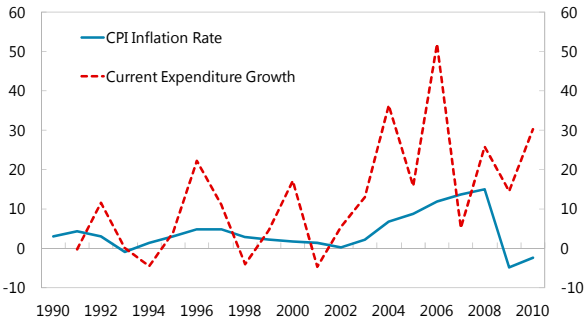
1/ Includes crude oil, LNG, propane, butane, and condensate.
2/ Fiscal year basis, April–March.
3/ Net of deposits in resident banks.
4/ Next 12 months.

APPENDIX 1. INFLATION IN QATAR: A VAR ANALYSIS OF THE EFFECT OF THE RECENT FISCAL PACKAGE[1]

Effective from September 1 2011, salaries and wages of Qatari civilian and military state employees have been permanently increased by sizeable amounts. We use historical data to estimate a simple VAR model for inflation in Qatar, and find that these increases in current expenditure have the potential to increase inflation in 2012 by one percentage point.

1. **The recent deflationary period in Qatar (average deflation of around 4.9 percent in 2009 and 2.5 percent in 2010) driven mainly by the roll out of infrastructure and increased supply of real estate inflation has been overturned by increased inflationary pressures. Inflation is expected to average around 2 percent in 2011 reflecting increases in domestic prices of petrol and steel, and the impact of global food prices.** The month-on-month core inflation (excluding food and rents) was 5.2 percent in September 2011. Potential inflationary pressures might arise in 2012 onwards from the recently announced sizeable increases in current public expenditure in Qatar.[2]

Figure 1. Inflation and Current Expenditure Growth, 1990-2010
(In percent)



Sources: Country authorities; and IMF staff estimates.

VAR model

2. **We estimate a simple VAR model and use the model's estimate of the elasticity of CPI inflation with respect to changes in current expenditure to infer the effect of the recent increases in current public expenditure on inflationary prospects in Qatar**. We focus our analysis on the inflationary effect of the fiscal package for 2012.[3]

3. **The model includes non-oil real GDP and domestic credit growth, which are both endogenously determined with inflation**. We include one-period lags of current and capital expenditure as well as current international food prices, imports prices and the nominal effective exchange rate as exogenous variables. The exogeneity assumption of the fiscal variables is based on the fact that budgets, which are voted much ahead of their implementation, are heavily reliant on fuel exports revenues and

[1] Prepared by Ghada Fayad.

[2] The government recently announced a 60 percent increase in the basic salary and social allowance for state civilian employees, a 120 percent rise for military personnel of officer ranks and a 50 percent increase for military personnel of other ranks. In addition, the pension of civilian retirees will increase by 60 percent, while the pension of retired military officers will rise by 120 percent and of other ranks by 50 percent.

[3] Since the planned increases have not been disbursed yet and with only three months remaining in 2011, we are not looking at the inflationary effect of such measures in 2011.

are thus less likely to be influenced by other factors. Nevertheless, periods of high prices and inflation can trigger a fiscal response of higher nominal wages and higher current expenditure, thus undermining our exogeneity assumption. Including the fiscal variables in lagged values helps alleviate such endogeneity concerns.

4. **In interpreting our VAR OLS coefficients below, we note that the inflation response to higher fiscal spending can be overestimated due to the above-mentioned reverse causality.** We can therefore think of our estimate as the upper bound or maximum value of the inflation response to current public expenditure increases. All the variables in the model are expressed in growth rates so that the estimated coefficients are interpreted as elasticities.[4] The model was estimated on annual 1990–2008 data[5], using one year lags.

5. **Our main result is reported in column (1) of Table 1.** The coefficient on current expenditure in the CPI inflation equation is highly significant and equal to 0.1. This suggests that a 1 percent increase in current expenditure is associated with a 0.1 percentage point increase in inflation in Qatar.[6]

6. **In computing the percent increase in current expenditure, we assume an increase of QR 10 billion in salaries of public sector employees.** With an estimated 8 percent increase in current expenditure in 2012 on account of the recent measures, we thus expect the inflationary impact of the salary increase in 2012 to be 1 percentage point.[7,8]

[4]These growth rates were showed to be stationary.

[5]We refrain from including 2009 and 2010 since the extent of deflation might be overestimated for those years, as the measurement of rents (which account for approximately 30 percent of the consumption basket) is skewed towards new contracts. Since new contracts have witnessed sharp falls in rents at the beginning of the year, the fall in average rents is likely to be less pronounced.

[6] Our results are robust to estimating the model after decomposing current expenditures to wages and salaries and its other components, then computing the elasticity of inflation to increases in wages and salaries.

[7] This does not take into account the transfers from government to the pension fund, as it is unclear in what form and when the transfer will take place.

[8] Additional channels that are not included in our analysis can lower or strengthen this estimate. First, our analysis assumes that the additional cash will be spent on goods and services domestically. Potential leakages however can occur and entail lower inflationary pressures. Examples include Qataris spending the additional money on travel or using it to pay off existing debt. Second, we do not tackle potential spillover effects on the wages of Qataris working in the private sector, and less likely on wages of expatriates. Inflationary pressures are expected to be higher if such wage spillovers materialize.

Table 1: VAR Model of Inflation in Qatar

	CPI Inflation	Non-oil Real GDP Growth	Domestic Credit Growth
	(1)	(2)	(3)
CPI Inflation (t-1)	1.42	1.71	2.46
	[5.52]	[1.31]	[1.04]
Non-oil real GDP growth (t-1)	-0.23	-0.79	-0.25
	[-2.41]	[-1.65]	[-0.29]
Domestic credit growth (t-1)	-0.07	-0.01	-0.29
	[-2.11]	[-0.08]	[-1.00]
Current expenditure growth (t-1)	***0.11***	0.48	0.66
	[2.46]	[2.04]	[1.54]
Capital expenditure growth (t-1)	0.00	0.08	0.22
	[0.05]	[1.11]	[1.79]
Nominal effective exchange rate growth (t)	-0.30	-0.27	-2.57
	[-2.11]	[-0.37]	[-1.98]
Imports price index growth (t)	0.12	0.35	-0.10
	[1.07]	[0.62]	[-0.10]
International food price index growth (t)	0.04	0.20	0.04
	[0.77]	[0.74]	[0.09]
Constant	0.01	0.02	0.05
	[1.04]	[0.68]	[1.03]
R-squared	0.96	0.78	0.83
Adj. R-squared	0.92	0.56	0.66

Note: t-statistics are reported in parentheses; Variables are differences in logs, and hence are growth rates

APPENDIX 2. MONETARY MANAGEMENT IN QATAR–EXPERIENCE WITH CAPITAL INFLOWS[1]

Limits on remunerated deposits of commercial banks with the central bank, and reduction in policy interest rates, coinciding with the issuance of longer-term government bonds, have been successful in driving out short-term speculative flows. The QCB needs to monitor the risk of rising inflation and be ready to use liquidity tools and macroprudential measures to manage the trade-offs between inflation and capital inflows.

1. **The independence of monetary policy in Qatar is limited by the peg to the US dollar.** The interest rate framework of the QCB encompasses two policy rates, viz., QCB Deposit Rate (QCBDR), and QCB Lending Rate (QCBLR). These rates are announced by the QCB on overnight deposit and loan transactions, respectively, between the QCB and local banks through the Qatar Money Market Rate (QMR) Standing Facility. The QCB also prescribes a reserve requirement (currently at 4.75 percent of total deposits). Another instrument available to the QCB is the issuance of CDs, which has been temporarily discontinued since 2011, and replaced by issuance of T-bills.

2. **Since 2008, the QCB has not fully aligned its policy rate with US interest rates, leaving scope for capital inflows.** Although monetary policy independence is constrained by the peg, the authorities had maintained higher interest rates compared to US interest rates—predicated on the objectives of containing inflation and preventing the expansion of bad loans—since September 2008. The QCB's net foreign exchange reserves increased by $8.6 billion to $18.4 billion in 2009; QMR deposits with the central bank, remunerated at 2.0 percent, had increased from $1.8 billion to $7.3 billion (Figures 1 and 2).[2]

3. **The reduction in policy rates in August 2010 was however not sufficient to arrest capital inflows.** In August 2010, the QCB reduced its policy deposit rate—by 50 basis points to 1.5 percent—the first time since April 2008. Between January and July of 2010, QMR deposits had increased to $11 billion, and the QCB's foreign exchange reserves to $23 billion. The QCB attributed the interest rate change to prevailing high real interest rates, reflecting persistent price deflation, alignment with the interest rates in major advanced economies and GCC countries, and Qatar's improved sovereign risk premium. The move was aimed at dissuading banks from placing deposits with the central bank and encouraging instead bank lending.[3] Given the pegged exchange rate regime, the QCB would have to rely increasingly on macroprudential instruments to manage the

[1] Prepared by A. Prasad

[2] IMF staff had at that time (Article IV Consultation 2009) cautioned that as investors reevaluate global risks, Qatar could attract speculative inflows. The QCB had indicated that it was monitoring inflows carefully and was ready to adjust interest rates if needed, while managing credit growth with its macroprudential instruments. Staff had also indicated that there is scope for improving liquidity management through liquidity forecasting and fine-tuning of the operations of the QMR facility.

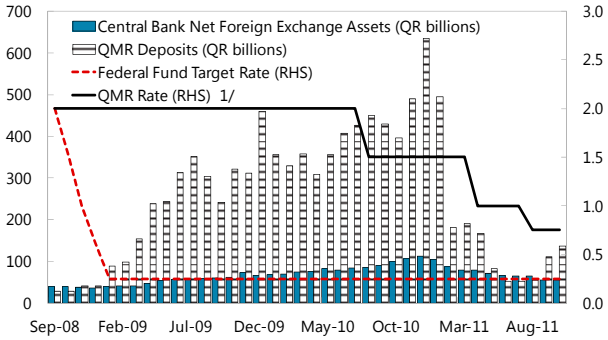
[3] Staff (Article IV 2010) supported the reduction in the rate, given the room to reduce interest rate differentials compared to U.S. and other GCC countries' interest rates, the benign headline inflation, and the relatively low credit growth in the economy. Staff had noted that the QCB had further scope to reduce policy rates in view of the existing high spreads compared with interest rates in the U.S.

credit cycle and to counter potential surges in capital inflows.

4. **Despite the reduction in interest rates, there were net capital inflows into the banking system, seeking to take advantage of interest rate arbitrage.** Banks continued to convert US dollars into Qatari Riyals and place them in the QMR facility. Thus, between April 2008, and December 2010, the QCB's net foreign exchange reserves had doubled to $31 billion.

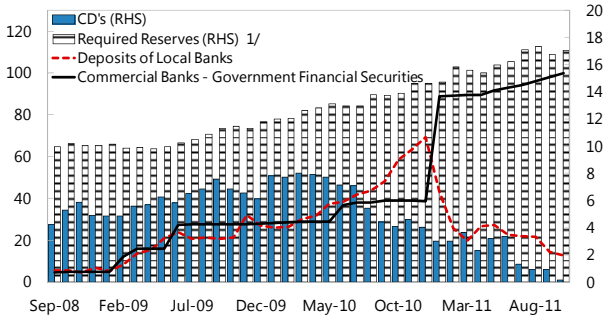
5. **The ceiling on remunerated deposits of commercial banks with the central bank resulted in a huge drawdown on QMR deposits and a reduction in the net foreign exchange of the central bank.** In January 2011, the central bank decided to set a new mechanism for banks for deploying funds under the QMR deposit facility and in CDs. According to this, QMR deposits and CDs are not allowed to exceed 100 percent of required reserves. Any maintenance of funds beyond 100 percent of required reserves would not be paid any interest by the QCB. At the same time, the QCB sold $13.7 billion (three-year maturity, with 5 percent coupon) government bonds to local banks. Combined, these measures resulted in the withdrawal of some arbitrage funds. Between December 2010 and March 2011, the QCB's net foreign assets had declined by $9 billion to $22 billion, and the deposits in the QMR facility dipped sharply from $19 billion to $5.5 billion, part of which is likely to have been invested in government bonds. In April 2011, the central bank reduced its QMR deposit rate to 1.0 percent, and in August 2011 by a further 25 basis points to 0.75 percent. The central bank's foreign reserves stood at about $16 billion at end-October 2011.

Figure 1. Change in Central Bank Reserves, 2008–11



Source: Country authorities.
1/ On January 17, 2011 the Qatar Central Bank annuonced that it would cap interest rates to match the reserve requirement.

Figure 2. Composition of Domestic Liquidity of Commercial Banks
(In QR billions)



Source: Country authorities.
1/ On January 17, 2011 the Qatar Central Bank annuonced that it would cap interest rates to match the reserve requirement.

6. **The recent measures of the central bank have been successful in driving out speculative short-term inflows; nevertheless, the reduction in policy rate has come at a time when the government announced large salary hikes for public sector employees and pensioners, which has the potential to increase inflation.** The central bank, therefore, needs to closely monitor inflation, and be ready to absorb liquidity through reserve requirements, issuance of T-bills, and open market operations. The central bank has already taken measures to ban personal credit for investment in equity, and imposed quantitative and price ceilings on personals loans assigned against salary.

Recent monetary policy measures

- **2007:** QMR Deposit rate was reduced to 4 percent while the required reserve ratio was increased from 3.25 percent to 3.75 percent.

- **Mid-February 2008:** Required Reserve Ratio was raised to 3.75 percent

- **Mid-April 2008:** Required Reserve Ratio was raised to 4.75 percent.

- **2008:** QMR deposit rate reduced in four tranches from 4 percent to 2 percent during 2008. Last changed on May 1, 2008 to 2.0 percent.

- **December 24, 2008:** Limit on QMR deposit withdrawn.

- **August 11, 2010:** QMR deposit rate reduced to 1.5 percent.

- **January 17, 2011:** Limit on QMR Deposit + CDs ≤ required reserves maintained with the QCB.

- **April 5, 2011**:
QMR Deposit rate reduced to 1.0 percent
QMR Lending rate reduced to 5.0 percent
QCB Repo rate reduced to 5.0 percent.

August 2011:
QMR Deposit rate reduced to 0.75 percent
QMR Lending rate reduced to 4.5 percent
QCB Repo rate reduced to 4.5 percent

Source: Annual Report of QCB, various issues

APPENDIX 3. EXCHANGE RATE ASSESSMENT[1]

Estimates from an application of CGER-type methodologies broadly indicate that the Qatari Riyal was undervalued during 2010 by 15 percent, with a need to decrease current account surpluses over the medium term.

Results of CGER-type Analysis
(In percent of GDP)

	(A)	(B)		
	Projected CA	Norms		
		MB[1]	ES[2]	ERER[3]
2010	26	33	18	
2016	11	23	9	
Difference (A-B)				
2010		-7	9	
2016		-12	2	
Percentage of ER overvaluation (-) / undervaluation (+)				
2010		-11	15	15
2016		-20	3	n/a

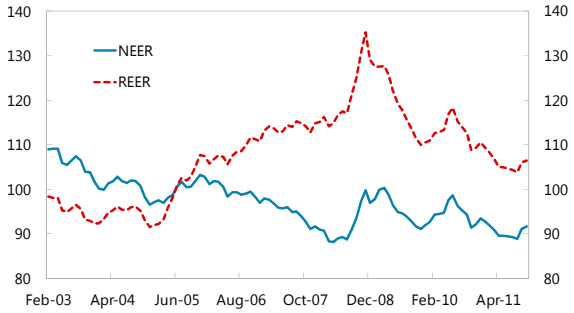
Source: IMF staff estimates and projections.

[1] Follows specification III of Beidas-Strom and Cashin (2011).

[2] Follows a constant real per captia allocation rule similar to Bems and Carvalho Filho (2009).

[3] Follows Cashin and Poghosyan (forthcoming).

Figure 1. Nominal and Real Effective Exchange Rates, Feb. 2003–Oct. 2011
(Index, 2005=100; increase represents an appreciation)



Source: INS.

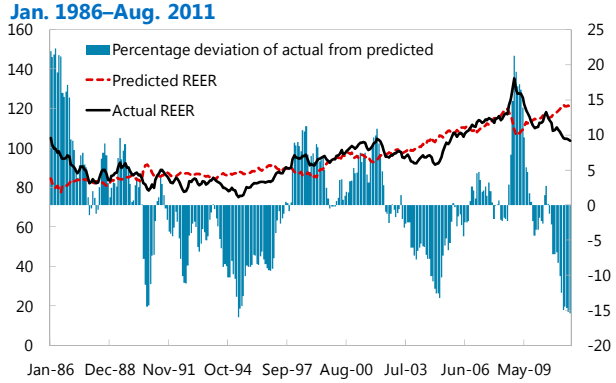
[1] Prepared by Samya Beidas-Strom

1. **Following terms of trade gains, the real exchange rate had appreciated 32 percent between the beginning of 2003 and end 2008, but two-thirds of this was eroded by a depreciation trend, which ensued since end 2008.** The trade-weighted real effective exchange rate (REER) index depreciated 19.1 percent between end 2008 and July 2011 (Figure 1). The nominal effective exchange rate diverged from the 2003–08 appreciation trend, owing to higher inflation relative to trading partners, but since end 2008 has followed the REER as deflation set in.

2. **The equilibrium real exchange rate approach indicates undervaluation**. This approach directly estimates the equilibrium real exchange rate (ERER) as a function of its underlying price-based fundamentals such as the terms of trade and relative productivity differentials between tradable and nontradable sectors. For the purpose of forming the exchange rate assessment, the adjustment to bring the exchange rate to the level consistent with these medium-term fundamentals is calculated as the difference between the estimated ERER and its current value. Absent data on the relative productivity differentials between tradable and nontradable sectors, the real effective exchange rate (REER) is estimated from monthly oil prices employing data going back to 1980. This high frequency estimation is based on a panel of 25 oil exporters employing monthly data between 1980Q1 to 2011Q3, with individual country regressions to account for country-specific heterogeneity. The premise of the estimation is that for

countries where primary commodities dominate exports, fluctuations in world commodity prices should explain most of the movements in their terms of trade yielding a "commodity currency" (Chen and Rogoff, 2002, and Cashin, Cespedes, and Sahay, 2002). Following this approach (Cashin and Poghosyan, forthcoming), a cointegration relationship between the logarithm of the REER and the logarithm of the real oil prices is found. A novel and robust band pass filter methodology (IBPF) for unit root testing indicates a statistically significant long-run cointegrating relationship between Qatar's REER and the real oil price, with an elasticity coefficient of 11 percent. It suggests that the Qatari Riyal is currently undervalued by 15 percent given trends in oil (and gas) prices (Figure 2).

Figure 2. Equilibrium Real Exchange Rate Assessment, Jan. 1986–Aug. 2011



Source: IMF staff estimates.

3. **The macroeconomic balance approach indicates overvaluation**. This approach calculates the difference between the current account balance projected over the medium term at prevailing exchange rates and an estimated current account norm. The exchange rate adjustment that would eliminate this difference over the medium term is then obtained using country-specific estimated responses of the trade balance to the real exchange rate. Past estimations have tended to employ pooled OLS or fixed effects estimations, which assume strict exogeneity of explanatory variables and entail that the error terms are uncorrelated with all past and future values of the regressors. This is a rather strong assumption and unlikely to hold. Along with similar recent studies, Beidas-Strom and Cashin (2011) address these shortcomings by employing generalized method of moments' (GMM) estimation, which controls for potential endogeneity of the regressors in a dynamic panel setting by applying the GMM-IV system estimator of Blundell and Bond (1998). GMM-IV uses additional moment conditions to explain equilibrium movements in the dependent variable. They also address the shortcomings raised in Bems et al (2009) and Arezeki and Hasanov (2009) by introducing specifications for the macroeconomic balance (Table 1), which include hydrocarbon reserves and financial assets held outside the central bank. In Qatar's case, similar to several commodity-exporters, only a modest amount of NFA is held at the central bank, and hence the choice of the preferred specification. This yields an average current account norm surplus of 22.7 percent of GDP in 2016. Contrasting the norm to the projected "underlying" current account position in 2016 (11.4 percent of GDP) suggests a 20 percent overvaluation of the REER; with the implication being that Qatar should accumulate larger current account surpluses given its fundamentals.

4. **The external sustainability approach indicates an undervaluation.** The underpinning of this approach is that the sustainability of the current account trajectory requires that the net present value (NPV) of all future oil and financial or investment income (wealth) be equal to the

NPV of imports of goods and services net of non-oil exports. Subject to this constraint, the economy would choose a path for imports, and hence a current account norm, that would support intergenerational equity given volatile oil prices and exhaustible oil reserves—through an appropriate pace of accumulation of net foreign assets. Estimating Qatar's wealth at $3.0 trillion[2] import trajectories ("annuities/income or allocation rules)" are calculated under three different policy scenarios: (a) a constant share of GDP annuity (red line); (b) constant real per capita annuity (green line); and (c) constant real annuity (black line) (Figure 3). All three types of annuities are used in the literature, and can be derived from the optimization of plausible utility functions. Choosing the constant real per capita annuity rule as a benchmark indicates a small undervaluation of 3 percent, as the implied norm (9 percent of GDP in 2016) is smaller than the projected current account (11 percent of GDP in 2016), with the implication being that Qatar could save less. Naturally, changing the oil production and price path, population growth, or initial NFA, could have a significant impact of the implied current accounts of each allocation rule, as they are sensitive to parameter assumptions.

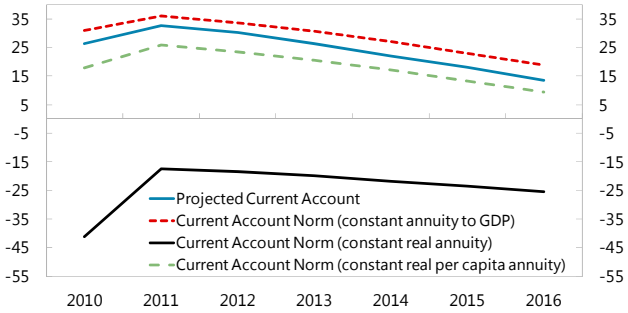
Table 1. Macroeconomic Balance: GMM Estimation and Implied Norms for Qatar
(Dependent variable: Current account balance, as a share of GDP)

	Prefered specification	
	GMM coefficients	Contribution to CA norm 2/
Core CGER Regressors 1/		
Constant	0.043	4.30%
Lagged dependent		
Non-oil fiscal balance/GDP	0.363	-4.80%
Oil and gas trade balance/GDP	0.469	8.26%
Old age dependency	-0.034	-0.04%
Population growth	-0.632	-2.53%
NFA/GDP		
Relative income	0.071	14.29%
Economic growth	-0.064	-0.38%
Net Oil-Exporter Specific Regressors		
Oil and gas reserves	0.0006	1.66%
Proxy for SWF/IIP	0.1601	1.92%
Estimated Current Account Norm (2016)		**22.7%**
Underlying Current Account Norm (2016)		**11.4%**

1/ Based on annual data from 1989-2009 from the WEO database Autumn 2010 vintage, 4-year non-overlapping averages. Projections are from the WEO Fall 2011 database. See Beidas-Strom and Cashin IMF Working Paper 11/195 for more details.

2/ Contribution to CA norm=coefficient*medium-term projection/steady state value (in percent).

Figure 3. External Sustainability's Current Account Norms vs. Projection, 2010–16
(Percent of GDP)



Source: IMF staff estimates.

[2] Assuming for illustrative purposes 864 billion barrels of reserves and a 4 percent recovery rate, oil and gas production would grow gradually (by 2 percent). Oil prices and the GDP deflator increase by about 2 percent after 2016, and real non-oil GDP grows by 5 percent. Future oil revenues are nominally discounted at 6 percent, the assumed rate of return on externally held financial wealth/NFA.

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APPENDIX 4. SEGREGATION OF ISLAMIC AND CONVENTIONAL BANKING IN QATAR[1]

In February 2011, the QCB directed its conventional banks that have Islamic windows, to stop opening new Islamic branches, accepting Islamic deposits, and extending new Islamic financing. The QCB has given until end-December 2011 for conventional banks to wind up their Islamic finance activities. As the directive is implemented, the following issues merit consideration by the QCB: (i) the costs of winding up; (ii) impact on banking sector competition, availability of Islamic products, and the banking sector's capacity to provide syndicated loans; (iii) development of Islamic liquidity management instruments; (iv) issues related to duration mismatch and funding gaps; and (v) harmonization of regulation and supervision in the GCC monetary union in the future.

Islamic financing in Qatar's banking system

1. **Islamic banking has been a fast-growing segment of the Qatari banking sector in recent years,** and Islamic assets accounted for 31 percent of total banking sector assets at end-2010. Islamic banking activity has been carried out both in standalone Islamic banks and in Islamic windows of conventional banks until recently. Total assets of Islamic windows in the conventional banks engaged in this activity reached 12 percent of the total balance sheet of conventional banks at end-2010, accounting for a similar share of profits (Table 1). Assets of standalone Islamic banks constituted 21 percent of total assets in the Qatari banking sector. Among conventional banks, Qatar National Bank's Islamic window overwhelmingly dominated the segment with QR30.2 billion in total assets at end-2010, followed by Commercial Bank of Qatar and Doha Bank. Among standalone Islamic banks, Qatar Islamic Bank had total assets of QR51.8 billion, followed by Masraf Al-Rayan (QR34.7 billion) and Qatar International Islamic Bank (QR18.2 billion).

Rationale for the new regulation

2. **The QCB recently directed conventional banks to close their Islamic operations.** The regulation directs conventional banks to stop opening new Islamic branches, accepting Islamic deposits, and dispensing new Islamic finance operations. The directive gives conventional banks until December 31, 2011 to collect balances in Islamic assets in accordance with the conditions and maturity dates agreed with customers, and to pay Islamic deposits upon maturity, with the exception of finance operations. After this deadline, conventional banks will have to continue to manage their remaining Islamic assets in a special portfolio with the possibility of transferring some of these assets to Islamic banks.

Table 1. Islamic and Conventional Activities of Qatari Banks, end 2010
(In million Qatari riyals)

	Islamic Branches of Conventional Banks	Conventional Business of Conventional Banks	Islamic Banks	Total Islamic Business of all banks
Total Assets	54,683	393,468	119,332	174,045
Total Profits	1,335	9,100	2,940	4,275

Source: Qatar Central Bank.

[1] Prepared by Zsofia Arvai.

3. **The QCB's decision was motivated by supervisory and monetary policy considerations.** In the QCB's view, the overlapping nature of non-Islamic and Islamic activities makes banks' risk management and compliance with prudential requirements more complex. The existence of Islamic windows complicates the preparation of financial reports governed by different international standards. It also makes the comparative analysis of financial reports more difficult at the domestic and international level. The QCB also argues that conventional banks cannot effectively separate capital for Islamic windows and conventional activities, an issue that is especially problematic for branches of international banks in Qatar with an Islamic window. Furthermore, the QCB believes that it is difficult to combine Basel and IFSB standards for capital adequacy. The segregation of Islamic and conventional activities is also aimed at improving the effectiveness of monetary policy, as it will enable the QCB to introduce different liquidity management instruments for the two types of activities.

4. **Leveling the playing field between Islamic and conventional banks was a further rationale behind the decision.** The QCB would like to see the orderly growth of Islamic banks in Qatar.[2] Since conventional banks were typically able to raise funds at lower rates, they were able to capture a large share of Islamic banks' business segment. Access to low-cost funding was an advantage, especially in the case of international banks, which were able to leverage their funds from the global markets to take positions in Islamic assets. The complete segregation of the two banking segments should also reduce the risk of contagion from one segment to the other in the case of banking troubles in any segment.

[2] The Governor informed staff that conventional banks would not be allowed to have Islamic subsidiaries, and they would not be allowed to invest in sukuk. Also, conventional banks with Islamic windows in other GCC countries will not be allowed to have an Islamic branch in Qatar.

Early impact of the segregation directive on the banking sector

5. **Conventional banks stopped initiating new Islamic business, but—with one exception—have not divested of their Islamic windows.** Following the issuance of the directive, conventional banks have ceased undertaking new financing activities and taking Shariah-compliant funding. Up to end-October, only one conventional bank divested of its Islamic unit: the International Bank of Qatar has sold off its Islamic retail portfolio to Barwa Bank, a local Shariah-compliant bank. Other conventional banks are still considering options for their Islamic windows, and there are indications that some banks will convert the infrastructure of their Islamic branches for conventional banking purposes.

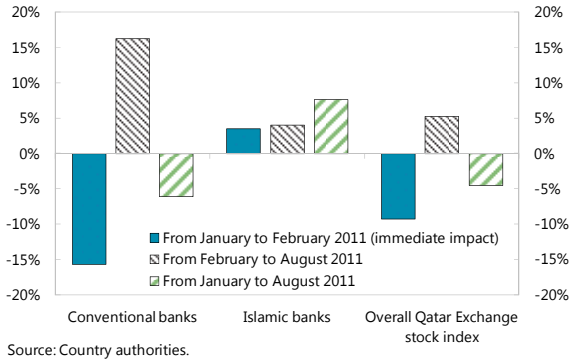
6. **Q2 2011 statements show the gradual adjustment of conventional banks' balance sheets**, though a complete picture of the change in Islamic banking activities of conventional banks is not available, as some banks, notably Qatar National Bank, the largest bank, do not report Islamic and conventional banking activities separately. At four other conventional banks, unrestricted investment accounts, the main Islamic item on the liability side of the balance

sheet, declined from QR7.2 billion to QR3.9 billion between Q4 2010 and Q2 2011, as contracts matured.[3]

7. **Conventional lending and Islamic financing activities by the Qatari banking sector continued to grow vigorously in the first half of 2011, although with a wide variation among banks.** On the aggregate, end-June data do not indicate a switch from conventional banks to Islamic banks by customers. The growth rate of total loans including Islamic financing of the five conventional banks was 12.7 percent in this period, while total financing activities by the three Islamic banks declined by 0.6 percent due to a contraction of Islamic financing in one of the larger Islamic banks. Total assets of Islamic banks grew faster in the first half of the year but this is due to a large increase of their financial investments in Islamic debt instruments, primarily sukuk issued by the QCB. Healthy growth in operating income in both Islamic and conventional banks in the first half of 2011 is also an indication that the segregation directive did not have a major impact on the banking sector yet. Q2 net operating income was 23 percent higher in 2011 than in 2010 for conventional banks and by 18 percent higher for Islamic banks.

8. **Investors' initial reaction at the Qatar Exchange reflected the expectation that Islamic banks would benefit from the directive at the expense of conventional banks.** The weighted stock price of Islamic banks registered an increase at the announcement of the new regulation in February, in contrast to stock prices of conventional banks which declined sharply (Figure 1). Although conventional banks' stock prices and the overall index recovered subsequently, Islamic banks significantly outperformed conventional banks and the overall Qatar Exchange index between January and August 2011. Investors' reaction indicates that the segregation directive is expected to provide further opportunities for Islamic banks to grow in a highly competitive banking environment.

Figure 1. Change in Stock Prices, 2011
(Percent; weighted by market capitalization)



Source: Country authorities.

Staff views

9. **International experience suggests that the treatment of Islamic banking activities is not uniform across countries.** Some countries, such as Saudi Arabia, Bahrain, Malaysia, the United Arab Emirates, and the UK have allowed Islamic windows, while e.g., Kuwait, Jordan, Syria, Yemen, and Turkey only allow standalone Islamic institutions. There are certain advantages to allowing Islamic windows in conventional banks. Islamic banking services and products often benefit from the experience and systems of conventional banks, potentially improving the quality of

[3] Central bank data reveals that Islamic assets of conventional banks as a share of total assets of conventional banks declined from 12.4 percent to 5.5 percent between December 2010 and September 2011. During the same period, Islamic credit facilities of conventional banks declined from 19.3 percent to 5.5 percent, and Islamic deposit facilities declined from 12 percent to 4.8 percent.

services and products and lowering their cost. Windows also facilitate liquidity management, especially in countries where Islamic liquidity instruments are limited, as windows usually have easy access to liquidity support from the conventional part of the bank. Islamic windows can enhance competition in the market, which could lower the cost of finance for Shariah-compliant products.

10. **Countries disallowing Islamic windows in conventional banks usually have several concerns.** First, they are often concerned about co-mingling of Islamic and conventional assets and liabilities as it increases reputational risk and raises issues related to consumer protection. Second, the windows could hinder the establishment of effective corporate governance and risk management systems. The management and board of a conventional bank may not be sufficiently attuned to the unique risks inherent in Islamic banking activities; thus their ability to oversee the risk management of the Islamic banking window may be compromised. Third, the operation of windows could open the door for regulatory arbitrage or unfair practices. Fourth, Islamic windows could hinder effective financial oversight and the preparation of proper financial statements. Some prudential ratios that might differ for Islamic banking could be difficult to monitor appropriately. The issue of resolution of Islamic windows is also often unclear. Finally, monitoring the impact of using Islamic monetary instruments could be difficult in the case of Islamic windows, which could hinder the design of appropriate monetary policy.

11. **Several issues merit future consideration by the QCB when implementing the directive, to ensure that the desired objectives are met.**

- Extend the timeline for unwinding Islamic operations if necessary, so as not to place unduly high costs on conventional banks with Islamic windows.
- Manage the impact on banking sector competition in view of the decline in the number of institutions providing Islamic banking services from 12 to 4. In order to reduce the risk of oligopolistic behavior among the remaining Islamic banks, the central bank could permit the reorganizing of Islamic windows as subsidiaries.
- Monitor the impact of the segregation on the availability of Islamic products and the banking sector's capacity to provide syndicated loans to ensure effective financial intermediation.
- Manage the impact on liquidity management, since the segregation could affect liquidity and rates in the interbank market and Islamic banks' capacity to engage in effective liquidity management.[4]
- Iron out the issues related to duration mismatch and funding gaps since conventional banks are permitted to retain assets until maturity but not renew deposits upon maturity.[5]
- Resolve potential issues of regulatory harmonization in the GCC monetary union, since other GCC countries continue to allow conventional banks to pursue Islamic banking activities.

[4] The QCB indicated that they are in the process of designing new Islamic liquidity management instruments.

[5] The QCB indicated that deposits behind Islamic assets in the special portfolios can be renewed, but the renewals cannot exceed the original maturity. In this respect, it is encouraging that the QCB's plans include the provision of funds by the central bank for conventional banks to fund their special Islamic asset portfolio if needed.

APPENDIX 5. QATAR CENTRAL BANK REGULATION OF PERSONAL LOANS BACKED BY SALARY ASSIGNMENT[1]

For macroprudential and consumer protection purposes, in April 2011, the QCB tightened its existing limits on personal loan amounts per borrower, and introduced a ceiling on interest rates on salary-assigned and credit card loans, including for existing loans. Limits on the absolute amounts of loans will help reduce household debt and moderate banks' balance sheet risks. The regulation, however, could distort product pricing, act counterproductively to building up of risk management capacity in banks, hinder efforts to develop the domestic debt market, increase moral hazard of borrowers, and affect the revenues of banks.

1. **The QCB has historically regulated bank lending for personal loans.** As in other GCC countries, the dominant retail product in Qatar is personal loans, in which the customer's salary is assigned to the bank (Table 1). The QCB first issued regulation on personal loans in 2007, and subsequently tightened it in March 2008 when the maximum debt service coverage ratio (monthly repayment as a percentage of the borrower's monthly salary) was reduced to 50 percent from 70 percent. At that time, the limit on credit extended to a Qatari national was maintained at QR2.5 million ($686,000) and the maximum tenor was kept at seven years.

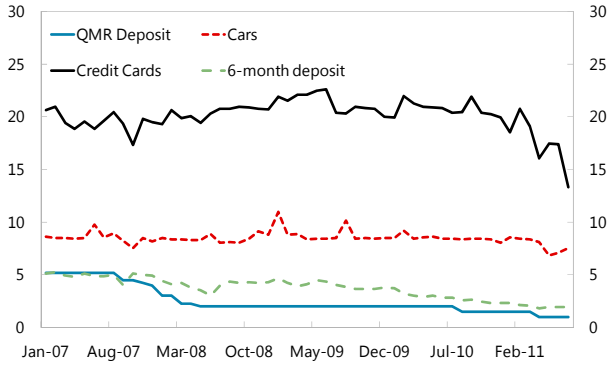
2. **The regulation limits the maximum amount of personal lending by banks and imposes a ceiling on interest rates on personal loans assigned against salary.** The new limits are QR2 million for nationals and 400,000 QR for expatriates. The maximum interest rate that banks can charge on salary-assigned loans is the QCB policy lending rate plus 1.5 percent, which worked out to 6.5 percent in April 2011. The new interest rate also applies to existing salary-backed loans contracted prior to the issuance of the new directive. Interest rates on credit card loans were also capped at 1 percent monthly. A February 2010 QCB directive set a ceiling on commission and fees on personal accounts and services which will help prevent circumvention of the interest rate ceiling.

3. **The interest rate ceiling seeks to correct the unresponsiveness of interest rates to the gradual decline in the cost of funding in recent years.** The QCB policy deposit rate has been reduced in several steps from 5.15 percent to 0.75 percent between September 2007 and August 2011, and commercial banks' deposit rates have also been on a declining trend, with an acceleration in the decline since early 2010 (Figure 1). At the same time, the level of personal loan rates has hardly moved in the last three years, with credit card rates fluctuating between 18 and 20 percent, and average car loan rates staying close to 8 percent. Thus, the spread between lending rates and the cost of funds has widened considerably. After a period of rapid build-up between 2005 and mid-2008, the total amount of personal loans in the Qatari banking system stabilized in the QR55–60 billion range ($16 billion). Thus, the tightening of personal loan regulation in March 2008

[1] Prepared by Zsofia Arvai.

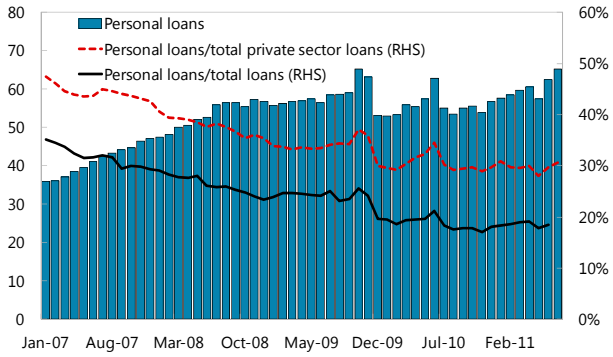
stabilized the absolute amount of personal loans, and led to a decline in these loans' share in total banking sector lending (Figure 2).

Figure 1. Policy and Bank Lending Rates
(In percent)



Source: Country authorities.

Figure 2. Personal Loans
(In QR billions)



Source: Country authorities.

4. **Bank rates started to adjust to the new limits, whereas the volume of personal loans continues to grow strongly.** In fact, some banks already lowered their retail loan rates months before the new regulation was announced in order to increase their market share. The fall has been especially pronounced for credit card rates, which were capped at 1 percent per month. The volume of personal loans dipped in May but consequently picked up strongly again. Nevertheless, the share of personal loans in the total loan book and as a percentage of private sector loans stabilized since Q3 2010 (Figure 2). This may be a sign that this market segment is saturated.

5. **The impact of the interest rate ceiling on banks' income is likely to be limited as the decline in the net interest margin will be offset by the strong growth in credit to the public and corporate sectors.** Since personal loans still account for approximately 18 percent of total banking sector lending, lower interest revenue from personal loans will be a significant upfront hit to banks' profitability, especially as existing contracts will have to be repriced as well. The effect on the pricing of other products is not straightforward. Banks may be tempted to reflect the lost interest income in the pricing of other products. On the other hand, corporate customers may exert pressure on banks to lower corporate lending rates as they compare spreads to retail spreads. The likely decline in the net interest margin notwithstanding, relatively strong credit growth (16 percent y-o-y in July 2011 for private sector loans) is likely to offset this effect.

6. **The interest rate ceiling would be counterproductive to the QCB's efforts to strengthen risk management of banks** that is backed up by the improving capabilities of the recently established credit bureau. The ceiling on interest rate implies that banks will not be able to apply risk-based pricing on salary-assigned loans. The limits on the absolute amounts of personal loans by themselves would have been adequate to bring down the levels of interest rates on such loans. While high interest rates, such as the prevailing levels prior to the introduction of the interest rate ceiling, might have resulted in adverse selection—an argument that supports the QCB decision—it would generally be desirable to let banks distinguish between

borrowers of different riskiness. Moreover, the interest rate ceiling has been imposed at a time when efforts are being made to develop the local debt market. Finally, imposing the interest rate ceiling on previously extended loans implies a subsidy for borrowers, including those whose repayment capacity is not in question, raising the issue of moral hazard.

Table 1. Regulations Pertaining to Consumer Lending in GCC Countries

	Bahrain	Kuwait	Oman	Qatar	Saudi Arabia	United Arab Emirates
Household Lending Limits						
Presence of lending limits to retail borrowers. Examples include Loan-to-value ratio, debt/income ratio, debt service/income ratio, an absolute amount limit, etc.	Max debt service ratio of 50%. Max term of 7 years.	Total monthly repayments should not exceed 40% of borrower salary and 30% of income for pensioners. Real estate mortgages are capped at KD 70,000 per person.	None	Credit to individuals capped at 50% of monthly salary and allowances, not to exceed QR 400,000 for expats and QR 2 million for nationals per person and for 7 years max.	Total monthly repayments (for both personal loans and credit cards) should not exceed 33% of a borrower's salary. Personal loan maturity should not exceed 5 years.	Personal loans to salaried individuals cannot exceed 250,000 Dirhams.
Year introduced	2005	2007/08		2011	2006	1993
Interest rate ceilings on personal loans	No.	Discount rate + 3 percent for personal loans.	8 percent for personal loans, and 18 percent on credit cards.	QCB lending rate plus 150 basis points	No.	No

Sources: Country authorities and Central Bank websites.

INTERNATIONAL MONETARY FUND

QATAR

STAFF REPORT FOR THE 2011 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

January 12, 2012

Prepared By | Middle East and Central Asia Department

CONTENTS

I. RELATIONS WITH THE FUND

(As of November 2011)

I. Membership Status: Joined 09/08/72; Article VIII, 06/04/73

II. General Resources Account:

	SDR million	Percent Quota
Quota	302.6	100.00
Fund holdings of currency	212.88	70.35
Reserve position in fund	89.72	29.65

III SDR Department:

	SDR Million	%Allocation
Net Cumulative allocation	251.40	100.00
Holdings	268.70	106.88

IV. Outstanding Purchases and Loans:

None.

V. Projected Obligations to the Fund:

(SDR Million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2011	2012	2013	2014	2015
Principal					
Charges/Interest	0.00	0.00	0.00	0.00	0.00
Total	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**

VI. Implementation of HIPC Initiative:

Not applicable

VII. Safeguards Assessments: Not applicable

VIII. Exchange Arrangements:

The Qatari riyal has been pegged to the U.S. dollar at QR 3.64 = $1.00 since July 2002, following an unofficial peg that was in effect since June 1980. Qatar has accepted the obligations under Article VIII, Sections 2, 3, and 4(a) and maintains an exchange system that is free of restrictions on the making of payments and transfers for current international transactions. Qatar maintains exchange restrictions for security reasons, based on UN Security Council Resolutions, that have been notified to the Fund for approval under the procedures set forth in Executive Board Decision No. 144-(52/51).

IX. Article IV Consultation:

The discussions for the previous Article IV consultation took place in Doha in November 2010. The Staff Report and its supplement were approved by the Executive Board on lapse of time basis on February 16, 2011. Qatar moved to a 12-month Article IV consultation cycle in 2007.

X. FSAP Participation, ROSCs, and OFC Assessments:

FSAP missions were conducted in January and May 2007. LEG conducted a detailed assessment of the Qatari anti-money laundering and combating the financing of terrorism (AML/CFT) framework against the Financial Action Task Force (FATF) 40+9 Recommendations, in February 2007. The report was also presented to the Middle East & North Africa Financial Action Task Force

(MENAFATF) and the FATF and adopted by these organizations as their own mutual evaluation at their respective plenary meetings of April 2008 and June 2008. The final report was published on the Fund website and a ROSC was circulated to the Executive Board for information in September 2008.

XI. Technical Assistance:

STA	November/December 1994	Multisector Statistics Mission
MAE	June 1995	Financial Sector Reform
MAE	April 1997	Reform of the Qatar Central Bank's legal framework
MAE	September 1998/January 1999	Introducing government bonds and Treasury-bills
STA	April 2000	Real Sector Statistics
STA	May 2001	Balance of Payments Statistics
STA	January 2005	Multisector Statistics
STA	April 2006	Government Finance Statistics
LEG	November 2006	AML/CFT Pre-assessment
STA	April 2007	GDDS Assessment
LEG	October 2009	Long-Term Advisor
STA	October 2010	Balance of Payments Statistics

XII. Resident Representative: None

II. RELATIONS WITH THE WORLD BANK GROUP

The program of cooperation with Qatar is relatively recent: starting from 2003, the Bank has been providing technical assistance in various strategically important development areas based on ad hoc requests from the government. In February 2010, government, represented by the Minister of Economy and Finance, signed the Framework Agreement for Advisory Services with the Bank, which facilitates further development of the program and expanding it into new areas by streamlining legal processing of each project.

The program began in April 2003 with a Public Transport Sector Reform study. A manpower planning exercise launched in 2003 with the support of the World Bank evolved in 2004 into a Labor Market Strategy for Qatar. The study was completed in June 2005 and could serve as a model for the GCC countries with similar labor issues. The project made a significant impact in Qatar and was widely publicized by the government. In 2007, WBI conducted a study on the Knowledge Economy (KE) Development in Qatar, the results of which were discussed at several high-level workshops. During 2008 and the first half of 2009, the Bank continued to support the implementation of the strategy; recently, the government decided to take over further implementation of this program but expected the Bank to continue its support in certain areas of the KE development.

In 2005, the World Bank provided technical assistance on payment systems to the Qatar Central Bank, in the context of supporting the development of payment and securities clearance and settlement systems in the Arab region through the Arab Payments and Securities Settlement Initiative, led jointly by the World Bank, the Arab Monetary Fund and the International Monetary Fund.

Moving forward, the Government expressed a strong interest in further collaboration with the World Bank on a number of strategic issues, i.e., public-private partnerships, fiscal management, and macroeconomic modeling (RMSM-X). A recently completed program with the Ministry of Business and Trade addressed the issues of improving business environment; the findings and major conclusions will be discussed at a government workshop in Doha in January 2012.

In addition, the Bank conducts regular workshops that discuss GCC–wide cross-cutting issues. The workshop *Partnering for Value, Innovation and Job Creation: PPPs in the*

GCC took place in May 2006; it concentrated on Public-Private Partnerships (PPPs) as an important tool for sustaining achievements of GCC economies. In February 2010, the Bank team helped the General Secretariat for Development Planning of Qatar to conduct a GCC-wide *Economic Diversification Forum* in Doha.

Ongoing projects

- **Environmental Action Program (Qatar National Component of the Gulf Environmental Program and Action Plan (GEPAP).** This technical assistance supports the Ministry of Environment in implementing the environmental policies to achieve the objectives detailed in Qatar National Vision 2030. This activity links with the regional GEPAP, the main objective of which is to preserve, protect and promote long-term sustainable development for the Gulf region and its waterway

- **Business and Trade Development**. The project objective is to develop specific policy measures and interventions for trade facilitation and export development to support high quality investments in Qatar. It aims to identify opportunities to (i) expand the range of markets into which existing export products are sold; (ii) upgrade the quality and value added of existing export products and (iii) expand exports of services.

- **PPP Development**. The Ministry of Business and Trade (MBT) has developed a partnership between its PPP department and the World Bank. The objectives of the recently established partnership are to strengthen the capacity of the PPP department and develop a world-class PPP framework in Qatar. The program started with the diagnostic report and moved on to the action plan design and implementation support.

- **Macro Capacity Development**. GSDP requested the Bank's assistance with developing macroeconomic capacity, in particular, using RMSM-X modeling. The Bank retained a macroeconomist who developed the flow-of-funds model and trained several GSDP staff. Follow-up capacity building exercise is currently underway.

Completed projects

- Linking Qatar's Medium-Term Development Strategy to the Annual Budget (FY10).

- Economic Diversification Forum (FY10)

- Support to Labor Market Strategy Action Plan: Implementation (FY10).
- Knowledge Economy Strategy and Implementation Assistance (FY09).
- Workshop on "Partnering for Value, Innovation and Job Creation: PPPs in the GCC" (FY06).
- A macroeconomic modeling workshop (FY06).
- Evaluation of Qatar's Payments System (FY05).
- Labor Market Strategy (FY04)
- Investment Climate Workshop (FY04).
- Public Transport Sector Study (FY03).

III. STATISTICAL ISSUES

(As of December 2011)

Assessment of Data Adequacy for Surveillance
General: Economic data are broadly adequate for surveillance, but there is substantial scope for improving their frequency, timeliness and coverage. The most affected areas are the real gross domestic product (GDP), financial accounts of the balance of payment, and external debt statistics.
National Accounts: Despite recent improvements, key aggregates are limited to quarterly estimates of GDP at current prices. The accuracy of data in the nonhydrocarbon sector is undermined by the lack of comprehensive source data. In July 2011, Qatar Statistical Authority published the final annual series of nominal and real GDP data for 2004 and 2009. **Price statistics:** There have been some improvements in the compilation of the consumer price index (CPI). The authorities are now publishing monthly CPI data based on a reweighted and rebased (2007=100) basket, but the index remains deficient. The information related to domestic rents—which form a sizeable share of the basket—constitutes only new rents, leading to overestimation of the current deflation.
Government finance statistics: The authorities presented to the mission, Government budget and outcomes data according to *Government Finance Statistics Manual 2001* (GFSM) guidelines. However, budget data should be rendered consistent with the data on public sector in the monetary survey and the balance of payments. Data on financing items in the budget are not up to date. Access to this information along with data on the budget outcome for previous fiscal years would enhance the basis for analysis.
Monetary statistics: Monetary data for Qatar Central Bank (QCB) and commercial banks are generally timely and of high quality. The QCB reports monetary data regularly to STA for publication in *International Financial Statistics* (IFS) on a monthly basis with a lag of about three weeks. Monthly and quarterly data are also published in the *Quarterly Statistics Bulletin*.
Financial Stability: Qatar Central Bank published and disseminated its second Financial Stability Report in 2011, and plans to make it an ongoing process.
Balance of Payments: Since the September 2010 technical assistance mission on balance of payments statistics, the authorities have made progress in implementing the mission's recommendations, including compiling balance of payments data in the international format needed for publication in the International Financial Statistic (IFS). The financial account has been developed and coverage improved for major public corporations, the Qatar Financial Center, and the Qatar Exchange. In addition, improvements have been made to the report forms used by banks to collect balance of payments transactions, primarily for the current

account. Continuing efforts are needed to further develop data sources, particularly for the private sector. To this end, close collaboration with the Qatar Statistics Authority in the development of surveys is strongly encouraged. In addition, close monitoring of investment income is needed, particularly for foreign investments in the hydrocarbon sector. Given the improvements made in the last year, the Qatar's balance of payments data for Q1 2011 are ready to be published in the IFS, with the caveat that that there will be revisions to the data as coverage is refined and improved. The authorities need to continue their efforts to develop their external sector statistics by working towards the compilation of an International Investment Position (IIP) statement.

External debt

Detailed data on the country's medium- and long-term external debt are provided to missions during the Article IV consultation discussions. In the recent period, Qatar has issued several international bonds. The authorities are disseminating data on external debt of the government through the central bank website. It is important to further improve the information flow on external debt and its maturity profile. The MOEF is giving priority to the collation and dissemination of complete data on external debt (including government, government enterprises, and non-government corporates).

Data Standards and Quality

Qatar is a General Data Dissemination System (GDDS) participant since December 2005. The GDDS mission of April 2007 updated the GDDS Summary Table II *Data Coverage, Periodicity, and Timeliness;* assessed dissemination practices relative to the requirements of the Special Data Dissemination Standard (SDDS) for coverage, periodicity, and timeliness; and identified major milestones that Qatar would have to reach to graduate from the GDDS to the SDDS. To enhance data dissemination practices, staff *assisted* the authorities in developing a National Summary Data Page (NSDP) and an Advance Release Calendar (ARC).

Qatar: Table of Common Indicators Required for Surveillance

(As of December 5, 2011)

	Date of latest observation	Date received	Frequency of Data[6]	Frequency of Reporting[6]	Frequency of Publication[6]
Exchange rates	Nov. 2011	Dec. 2011	M	M	M
International reserve assets of the monetary authorities[1]	Oct. 2010	Nov. 2011	M	M	M
Reserve/base money	Oct. 2011	Nov. 2011	M	M	M
Broad money	Oct. 2011	Nov. 2011	M	M	M
Central Bank balance sheet	Oct. 2011	Nov. 2011	M	M	M
Consolidated balance sheet of the banking system	Oct. 2011	Nov. 2011	M	M	M
Interest rates[2]	Oct. 2011	Nov. 2011	M	M	M
Consumer price index	Oct. 2011	Nov. 2011	M	M	M
Revenue, expenditure, balance and composition of financing[3] – general government[4]	...	...	NA	NA	NA
Revenue, expenditure, balance and composition of financing[3] – central government	2010/11	May 2011	Q	I	I
Stocks of central government and central government-guaranteed debt[5]	2011	Nov 2011	A	I	I
External current account balance	2010	March 2011	A	A	Q
Exports and imports of goods and services	2010	March 2011	A	A	Q
GDP/GNP	2011 (Q2)	Oct. 2011	Q	I	I
gross external debt	2011	Nov 2011	A	I	I
International investment position[7]	Sep. 2011 (incomplete)	Nov. 2011	I	I	NA

[1] Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[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] Daily (D), weekly (W), monthly (M), quarterly (Q), annually (A), irregular (I); and not available (NA).
[7] Includes external gross financial asset and liability positions vis-avis nonresidents.

INTERNATIONAL MONETARY FUND
Public Information Notice
EXTERNAL RELATIONS DEPARTMENT

Public Information Notice (PIN) No. 12/7
FOR IMMEDIATE RELEASE
January 31, 2012

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

IMF Executive Board Concludes 2011 Article IV Consultation with Qatar

On January 30, 2012, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV Consultation with Qatar on a lapse of time basis. Under the IMF's lapse of time procedures, the Executive Board completes Article IV Consultations without convening formal discussions.[1]

Background

Qatar has weathered the global crisis with high growth, and large external current account and fiscal surpluses. Government intervention in the banking system has ensured financial stability, and it is using its fiscal space to implement a large public spending program to maintain strong growth in the nonhydrocarbon sector. Real Gross Domestic Product (GDP) growth is projected to accelerate to 19 percent in 2011, up from 17 percent in 2010. The nonhydrocarbon sector is expected to grow by 9 percent, driven by manufacturing, financial services, and trade and hotels. Consumer Price Index (CPI) inflation excluding rent increased to 5.8 percent in October 2011. Following an average deflation of around 2.5 percent in 2010, average CPI inflation is expected to average around 2 percent in 2011 (end-year 2.5 percent)—with negative rental inflation being more than offset by a general increase in all the other components of the inflation basket.

[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. 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.

The banking sector remains profitable and strong with a capital adequacy ratio of 22.3 percent, average return on assets of 2.7 percent, and non-performing loans ratio of 2.3 percent at end-June 2011.

The economic outlook for 2012 and beyond looks favorable, despite increased external risks. The main downside risks are lower hydrocarbon prices and potential disruption in transportation of liquefied natural gas (LNG) due to increased geopolitical tensions. Real GDP growth rate is projected to moderate to 6 percent in 2012, with real hydrocarbon GDP slowing down to 3 percent, as LNG production remains constant due to the self-imposed moratorium on new hydrocarbon projects. Large government investment for infrastructure would sustain growth in the nonhydrocarbon sector between 9 and 10 percent beyond 2012. Average CPI inflation is projected at 4 percent to 5 percent over the medium term, as rents stabilize due to a gradual decline in excess capacity in real estate, and as the implementation of large investment projects lead to some overheating pressures. The fiscal and external accounts are projected to remain in surplus throughout the medium term, as oil prices are expected to remain high.

Executive Board Assessment

In concluding the 2011 Article IV consultation with Qatar, Executive Directors endorsed staff's appraisal, as follows:

Qatar is using its fiscal space, generated from an increase in hydrocarbon production and prices, to implement a large public spending program. Large infrastructure investments are expected to sustain strong growth of 9 to 10 percent in the nonhydrocarbon sector in the medium term.

Headline inflation is projected to remain subdued, but inflation risks have risen due to domestic factors. The potential inflationary effect of the recent fiscal package is estimated to be around 1 percentage point. This underscores the need for fiscal policy to monitor aggregate demand and for the Qatar Central Bank (QCB) to manage liquidity.

The expansionary fiscal stance in 2011/12 thus warrants careful monitoring of aggregate demand to ward off risks of inflation. Fiscal policy must continue to maintain a careful balance between spending on infrastructure to sustain non-inflationary growth, and saving and investing hydrocarbon surpluses abroad to generate sufficient income to finance future budgets.

In the context of the peg, the QCB would need to manage liquidity more actively. The QCB would need to develop a formal liquidity management framework to facilitate a more proactive strategy in fine-tuning liquidity. In addition, coordination of debt management with the Ministry of Economy and Finance would be helpful in maintaining a stable and adequate stock of government securities for the further development of an interbank repo market, and also providing a robust benchmark yield curve for the corporate bond market.

Developing a more formal and transparent macroprudential policy framework to enable a swift response when needed would help achieve orderly credit growth without generating overheating. The main challenges for monetary policy will be to support credit growth without fuelling inflationary pressures or short-term capital inflows. Against the backdrop of increasing credit growth, banks, and the QCB need to be cautious that overall credit quality does not weaken, particularly in the real estate sector in view of the prevailing excess supply. Collating and disseminating price and volume data on Qatar's real estate market segments would help banks assess risks better and also enable the central bank to take informed preemptive measures to preserve financial stability.

The banking system has the ability to withstand credit and market risks. Nevertheless, staff underscores the need to monitor individual banks for stress, given the interlinkages in the financial system. Further, individual banks' foreign currency liquidity conditions need to be monitored and the QCB should stand ready to relieve potential pressures. Enabling a more robust risk assessment culture, conducting regular stress testing of banks, and putting in place an early warning system would help mitigate risks to the banking system and maintain financial stability.

In the medium term, fiscal policy will need to balance sometimes competing objectives of economic stabilization, development and generating intergenerational savings. Fiscal space has contracted somewhat compared to last year, because of the permanent increase in current expenditure, according to staff's medium-term fiscal sustainability exercise. Given the authorities' objective of fully financing the budget from 2020 onwards from its nonhydrocarbon revenues, and for building buffers for shocks, the authorities will need to increase savings over the medium term. While the eventual implementation of large capital projects, adjustment in current expenditures would be the most feasible way to reduce the dependency of the budget on hydrocarbon revenues.

Establishing a macro-fiscal unit would support fiscal policy making and the development of a medium-term budget framework to ensure the efficiency of public spending. A solid medium-term expenditure framework would represent a critical building block for the eventual adoption of a fiscal rule to help manage the path of fiscal spending.

Reducing Qatar's vulnerability to hydrocarbon price fluctuations will require, in addition to fiscal management, diversification into other sectors of the economy and reinforcing competitiveness. Opportunities for efficiency gains and reducing distortions in petrol, energy, and water use exist by reducing, among others, direct and indirect subsidies. It is also opportune to consider options for deeper pension reforms.

Further improvements in statistics will be essential, which will also require greater coordination across agencies.

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Qatar: Selected Economic and Financial Indicators, 2007–12

	2007	2008	2009	2010	Proj. 2011	Proj. 2012
Production and Prices						
Real GDP (in percent per annum)	18.0	17.7	12.0	16.6	18.8	6.0
Hydrocarbon 1/	13.8	13.2	4.5	28.8	31.1	2.9
Nonhydrocarbon GDP	21.6	21.3	17.6	8.4	9.0	9.0
Nominal GDP (in billion U.S. dollars)	79.5	115.0	97.6	127.3	173.0	179.9
Consumer price index (period average)	13.8	15.0	-4.9	-2.4	2.0	4.0
	(In percent of GDP on fiscal year basis) 2/					
Public Finance						
Total revenue	36.6	35.0	44.2	30.9	32.9	35.1
Hydrocarbon revenue	22.0	19.9	21.7	19.2	18.0	18.0
Other revenue	14.6	15.1	22.6	11.7	14.9	17.2
Total expenditure and net lending	26.8	24.7	30.0	28.2	25.7	28.0
Current expenditure, *of which:*	16.3	16.3	19.7	19.4	16.6	18.3
Wages and salaries	5.0	4.6	5.7	4.6	4.9	5.9
Capital expenditure	10.5	8.3	10.3	8.8	9.1	9.7
Overall fiscal balance (deficit -)	9.8	10.4	14.3	2.7	7.2	7.2
	(Annual change in percent)					
Money						
Broad money	39.5	19.7	16.9	23.1	24.8	20.8
Claims on private sector	51.3	42.4	7.0	10.6	15.8	15.9
	(In million U.S. dollars, unless otherwise stated)					
External Sector						
Exports of goods and services, *of which:*	50,508	73,026	48,280	81,723	111,457	112,783
Crude oil and refined petroleum products	21,083	29,438	18,384	29,099	35,249	35,534
LNG and related exports	18,710	32,267	23,947	43,535	61,938	61,330
Imports of goods and services	-27,172	-35,045	-30,120	-38,021	-44,134	-46,334
Current account	20,186	33,039	9,987	33,531	48,660	47,290
In percent of GDP	25.4	28.7	10.2	26.3	28.1	26.3
Central Bank reserves, net	9,546	9,832	18,352	30,720	20,703	24,412
In months of imports of goods and services 3/	3.3	3.9	5.8	8.4	5.4	5.8
Exchange rates (Riyals/U.S. dollars)	3.64	3.64	3.64	3.64	3.64	…
Real effective exchange rate (percent change)	5.1	6.3	-1.4	-5.1	...	...

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

1/ Staff estimates; include crude oil, LNG, propane, butane, and condensate.

2/ Fiscal year begins in April.

3/ Next 12 months.