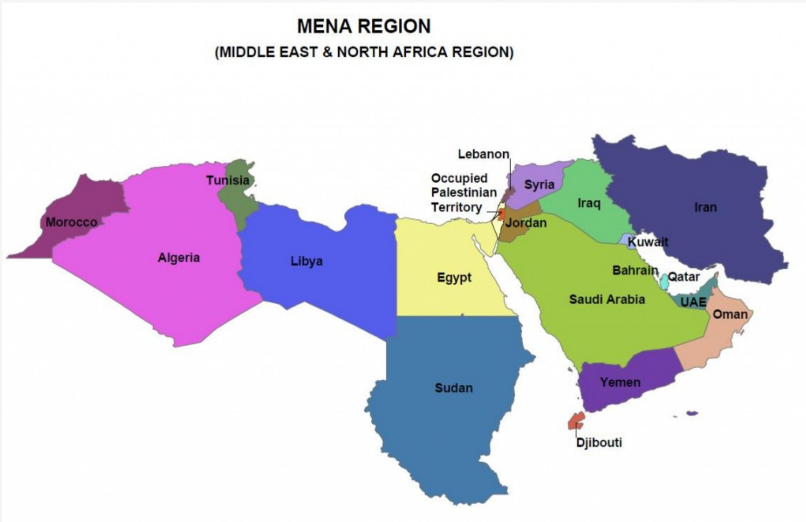
After the Arab Spring: Part 2 – the outlook for car markets in the Levant



The MENA Region

The Arab Spring began in 2010 in Tunisia,North Africa and travelled eastwards. First, into Egypt and Libya in 2011. Then, in 2012, into Syria, in the Levant. And, in this part of the world, as governments, rebels, terrorists and infiltrators arrived, it has caused chaos.
The modern Levant includes Lebanon, Syria, Jordan and the Palestinian Territories and – historically – Turkey as well. It has been described as the "crossroads of western Asia, the eastern Mediterranean and north-east Africa". It fringes the eastern Mediterranean over a distance of 1,100 miles, with a population of 35 MN, excluding Turkey.
The Levant economies share three common characteristics: they are net oil importers; they depend on other states or entities for their economic well-being – through remittances, exports or subsidies; and they share a politically unstable region. Consequently they are, more than usually, economically volatile and vulnerable.
In addition, they share exposure to economic downside risks:global economic slowdown: the continuing Euro Area crisis, weakness of Advanced Economy Sovereign risks and the volatile oil prices.

As a microcosm of the 'Arab Spring' they illustrate the consequences facing governments that both meet and fail the challenge of maintaining social cohesion amid economic turbulence. Counter-intuitively, in 2012, it is the oil exporting state – Syria – which is facing continuing turmoil rather than the oil-importing states: Jordan, Lebanon and Palestine.
What is the outlook for vehicle markets in the Levant region, excluding Turkey?
The immediate outlook is critically dependent on two factors, political stability and oil prices. Political stability impacts both directly and indirectly. Demand in Syria in 2012 will be subdued as consumer and business confidence ebbs and the crisis escalates. Lebanon, in contrast, may continue to benefit from capital flows out from its neighbour. Oil prices too, can be double-edged. In the case of Jordan, as an oil importer, high oil prices increase domestic inflation and, at the same time, remittances from Jordanians working in the oil-producing GCC area provides increased national income.

MENA OIL IMPORTERS: TOUGH ROAD AHEAD					
Overall Growth (GDP)					
	2008	2009	2010E	2011F	2012F
Egypt*	7.2	5.9	4.8	-1.4	2
Jordan	7.2	5.5	2.3	2.7	3.2
Lebanon	9.3	8.5	7	1.8	3.8
Morocco	5.6	4.8	3.8	4.3	3.9
Syria	5.2	4	3.5	-6	-3
Tunisia	4.5	3.1	3.7	-2	4
Inflation, Average, %					
Egypt*	11.7	16.2	11.7	11.5	7.9
Jordan	14	-0.7	5	4.8	4.6
Lebanon	10.8	3.1	4.4	5.8	7
Morocco	4	1.3	1	1.5	2.4
Syria	2.5	3.5	4.5	8	10
Tunisia	4.9	3.5	4.5	3.6	4.1
Current Account % GDP					
Egypt*	-6.8	-6.9	-8.1	-9.3	-10.2
Jordan	-2.2	-8.9	-5.6	-5.7	-4.7
Lebanon	-8.9	-7.9	-5.5	-8.3	-9.6
Morocco	0.4	-2.6	-4.5	-5.5	-5.1
Syria	-5.8	-4.8	-3.8	-6.7	-8.2
Tunisia	-0.4	-2.7	-1.4	-4.5	-3.1
Inflation, Average, %					
Egypt*	0.5	-2.3	-2	-1.6	-1.4
Jordan	-9.2	-4.7	-5	-9.6	-9.1
Lebanon	-13.6	-20.8	-20.7	-16.9	-15.3
Morocco	-6.4	-5.9	-4.7	-5.5	-5
Syria	-13.3	0	-3.5	-6.2	-7
Tunisia	-3.8	-2.6	-4.7	-6.6	-5.1

*Source: IIF; F = IIF forecast *Egypt growth rates have been adjusted to a calendar year basis to make them consistent with other countries, while figures for inflation and the fiscal & c/a accounts are on a fiscal year basis.*

According to its own statistics, Syria had 637,000 cars on its roads in 2009 and its vehicle parc was growing by over 8% pa. In 2010 its import statistics showed that 120,500 cars were imported. But, with the continuing Syrian Crisis the outlook for 2012 is pessimistic indeed. Few pundits expect car sales to exceed 40,000 to 60,000 in 2012, particularly as it's Syria's middle class elite – or at least much of their cash – that is leaving the stricken country. Not far behind, Lebanon imported around 80,000 cars in 2008 and 95,000 in 2009 to add to the 1.4MN vehicles on the road in 2007, of which an estimated 50% – 700,000 vehicles – are passenger cars. Jordan, with 825,000 vehicles in use in 2007 (506,000 cars) does not publish new car registration statistics. However, based on its neighbours and its GDP, the annual new car market is probably in the 30,000 – 50,000 range and there are probably 600,000 cars in use in 2011. The Palestinian Territories statistical bureau reported that in 2010 their were 181,000 vehicles, of which 116,000 were cars, over 64%. The vehicle parc appears to be growing at 8% – 9% per year suggesting a new vehicle market of 10,000 – 15,000 per year.

Customs Duties

However, the management of demand in each state also varies. In Syria, demand is distorted to favour those needed by the regime; in the rest, it is more widely spread as economic wealth is distributed more evenly. However, across the Levant, significant customs duties are as important in distorting demand as political priorities.

In Jordan aggregate duties exceed range from 60% – 120% depending on engine size. In Lebanon import duties range between 20% and 35%. Customs duties in Syria for cars range between 40% and 60% plus a surcharge of up to 35%.

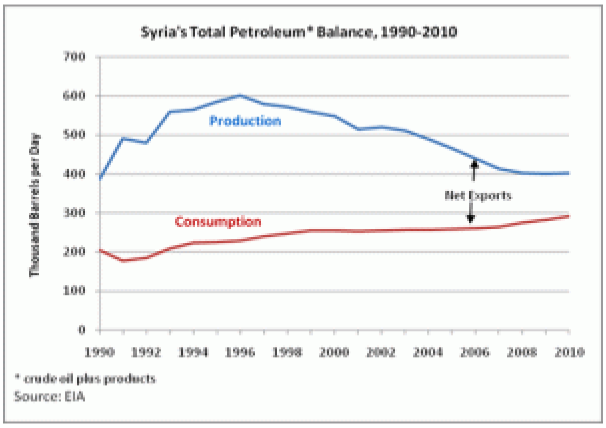
SYRIA

The final outcome of the Syrian Revolution remains unclear but it underlines the significance of the Arab Spring in shaping the future of the MENA region in general and the Levant in particular.

Syria has a nominal population of 22MN (2010) – nominal because millions of Syrians are displaced and living in other countries in the region – while Lebanon at 4MN, Palestine at 3.5MN and Jordan at 6MN are all much smaller. However, all of these populations are growing fast: at 40% – 106% between 1990 and 2008, according to OECD/World Bank population statistics.

Syria – under normal circumstances – is a middle-income country (GDP 2009 $5,293 per cap at PPP), with an economy based on agriculture, oil, industry, and tourism. Between 2000 and 2010 the GDP tripled from $20BN to $60BN, fuelling a consumer boom for its elite middle class, as the Al Assad regime introduced important economic reforms. However, Syria's economy faces serious problems, challenges and impediments to growth, including: a large and poorly performing public sector; declining rates of oil production and net exports; a widening non-oil deficit; wide scale corruption; weak financial and capital markets; and high rates of youth unemployment tied to the high population growth rate. It is widely reported that the backbone of the Syrian protesters are the disaffected and Sunni rural poor, not the urban and Alawite elite.

The IMF estimates that the economy has contracted 2%, at best, since the start of the Syrian Crisis in January 2011. Others are less optimistic. Business Monitor International estimated shrinkage at -9.6 percent, while Damascus-based economist Jihad Yazigi, author of the Syria Report, thinks that -15% is nearer the mark! Tourism employed 16% of adults in 2010 but the 8.5MN tourists of 2010 are a trickle in March 2012. Manufacturing incomes have fallen, as local products are displaced by imports, and agricultural incomes have dwindled under increased transportation costs. Syria's role as a transport route to the Gulf has all but disapeared, along with the border tax it enjoyed. Its continuing role as a transit route for oil from Iraq and Iran to Turkey is increasingly problematic and future oil transit fees are unpredictable. Its oil income – worth $400MN a month – is at a standstill.



Aleppo..before the war.

Its political dimension is just as fragile as its economy . Many observers recognise that Syria lies at the centre of a dense network of Middle East relationships, and the crisis is likely to have a major impact on the regional structure of power and economic prosperity. Less often noted is that the Syrian Crisis illustrates that even a country with an extensive security apparatus cannot lock-down its youth and poor forever. The implication for the entire MENA region is that employment of the young will move much higher up the political agenda, irrespective of its short-term impact on corporate productivity and profits. Expect many ex-patriates, especially non Arabs, across the region, to be displaced from their jobs in the years to come.

What will happen to the Syrian new car market in 2012? Expect a fall to less than 30,000 vehicles, even though there is pent-up demand due to delayed purchases and a heavy toll of destroyed vehicles. The unofficial exchange rate of the Syrian Pound has slumped to SYP90 to 1US$, from SYP47 before the crisis. This has translated into a 16%+ inflation rate already. In addition, if the Al-Assad regime is displaced, expect a dilution of the premium car market as wealth is spread more widely. Although Iran remains a supporter, they too may find 2012 a tough year due to increasing sanctions and have little economic surplus available to help Syria. Continuing political instability in Syria is also likely to undermine confidence in neighbouring Lebanon, Jordan and the Palestinian Territories.

Long term, the outlook is no less bleak. The Syrian government needs US$21BN a year to pay bills. It probaly has half of that in reserves – US$11BN. The only way to bridge the gap is to print money. Eventually, those bills will have to be repaid leading to a long period of austerity. The longer the crisis lasts, the worse it gets.

LEBANON

The economy of Lebanon has seen above-average growth in recent years. From 1998 to 2006 sluggish growth – 2.7% a year – was the norm, due to continued economic crises, political assassinations, and armed conflict. Since then, the GDP growth rate has trebled, averaging 8.5%, even with the global economic downturn, on the back of the wholesale and retail trade, telecoms, banking, tourism and remittances. Keep in mind that total disposable income is estimated at 150% of GDP. Lebanon’s primary economic driver is private consumption funded through remittances. In fact, the Lebanese economy is much larger than its territory owing to the Lebanese diaspora.

GDP per Cap US$	2009	2010	2011
Lebanon	14,600	15,500	15,600
Jordan	5,900	5,900	5,900
Syria	5,100	5,200	5,100

To quote one Lebanese economist, Ghazi Wazneh, “GDP in 2011 was less than 2 percent, banking growth less than 8 percent, tourism – many from Syria – down by more than 20 percent, capital inflows declined by 20 percent and investments fell by 15 percent. The only positive thing is the stability of the Lebanese pound.” While the Lebanese economy in 2012 may remain as weak as in the second half of 2011, as farmers and manufacturers struggle with the collapse of demand from Syria, almost 80% of the economy is services-based. These are much more flexible in the face of continued problems from Syria – it is neither an important import or export partner for Lebanon. Barring a flood of refugees, at worst, the economy may weaken still further in the face of sluggish Eurozone demand.

The consensus view from Lebanese economists is that the Syrian crisis had minimal effects on Lebanon in 2011. Concerns about the credibility of their government's reassurances pushed many Syrians to seek a safer place for their assets and Lebanon seems to be a favoured location due to long, well-established ties with local banks there. According to unofficial estimates, about 5 percent of all bank deposits in the Lebanese banking sector belong to Syrian clients. In its July 2, 2011 edition, British magazine *The Economist* reported that more than US$ 20BN had been transferred from Syrian banks to Lebanese ones since March 2011.

The Lebanese economic outlook for 2012 may not be so rosy if its finds itself cornered between a Syrian wild card and a helplessly ineffective public sector. Observers see 2012 as challenging at best, although they confess a difficulty in unravelling the impacts of a post-crisis Middle East, a complex Syrian dilemma, and a fractious Lebanese political environment. Oil prices above $120per barrel don't help Lebanon which has been subsidising its electricity provider to the tune of $1.5BN a year since the end of the civil war in 1990. So, the potential income from successful oil and gas exploration would be very welcome. If the oil and gas fields can be exploited, the current Prime Minister has earmarked a large slice for a sovereign wealth fund aimed to reduce national debt from 125% of GDP (US$ 52.6BN) down to 60%. However, the most recent Consumer Confidence Index for Lebanon from Byblos Bank shows consumers are less optimistic than at any time since 2007. That may damp down demand for new cars.

Lebanon's Internal Security Forces (ISF) listed 1.4MN registered vehicles in 2007 with a population of only 4MN, which suggests that by 2012 the country must be close to vehicle saturation. The Ministry of the Interior statistics suggested there were 89,500 newly recorded private cars and an additional 1,350 newly registered rental vehicles in 2009. With an uncertain regional economic and political background, the downside risks marginally outweigh the upside opportunities in the outlook for new car sales in 2012 with new car registrations in the 75,000 – 85,000 zone

JORDAN

Jordan has few natural advantages: inadequate water supply, 70%+ desert, and no oil or energy resources. But it does have a large – 6.2MN – youthful, expanding and educated population. So Jordan exports people – often highly educated – and receives in return – remittances, FDI and general government transfers — often from the oil-exporting GCC economies. Is this relationship stable? Probably. In 2008, the GCC production to reserves ratio stood at 73 years. In this economic relationship, real oil prices remain one of the main long-run drivers of real output for Jordan.

The Jordanian economy is no slouch. It has grown at 7% pa since 1999 and was worth $34.6BN in 2010. GDP per capita is 2 times that of Syria.

On the other hand, the Jordanian economy appears to be more vulnerable to oil price shocks than political instability. While the current oil price boom ensures that Jordan experiences a direct negative effect, through the increase in its oil import bill due to higher oil prices, the indirect positive effect is larger inflows of external income from remittances. If the ratio of external income to GDP remains relatively stable (or increases) over time, the positive effect outweighs the negative one.

But, as a consequence of the 'Arab Spring', the economic outlook for Jordan is uncertain for the first time for a decade. Until 2010, Jordan's economic recovery appeared on track, on the back of rising (albeit slow) domestic activity. Fiscal prudence and credible monetary management, reinforced by strong supervision and regulation of the financial sector, provided a solid platform for a robust upturn in 2011, the IMF argued.

With 70,100 newly registered vehicles in 2009, of which 27,275 were passenger cars and another 25,000 taxis and micro-buses, added to the 506,000 passenger cars (2007) on the road you might think Jordan has enough cars. In fact it has fewer than 90 cars per 1,000 people on average, But, for anyone who has ever been caught in the daily Amman gridlock, you'll recognize that the national average figure is largely irrelevant. The car density figure for the Amman metropolitan area was over 235 per 1,000 by 2009!

PALESTINIAN TERRITORIES

The Palestinian Authority's Ministry of National Economy describes the economy as follows, "Unemployment currently stands at 40% of the labour force, almost one half of the population lives below the poverty line of $2 a day, and investment is virtually non-existent."

With 182,000 passenger cars in 2010, the vehicle parc has grown steadily by almost 9% since 2000. The 4-year import ban by Israel imposed on Gaza ended in 2010 and released significant pent-up demand for new and low-mileage used vehicles. But with a price tag of $25,000 few Palestinians can afford them – the average GDP per head is a little over $2900 (CIA World Factbook- 2009).

The Outlook for the Levant Car Markets: Gridlock or Reform?

In the short term political instability, economic policies and demographics are all drivers of car markets in the Levant.

However, over the medium and longer term, transport infrastructure is the critical factor. Take Jordan, for example. Over half of Jordan's cars and 33% of its 6MN people are in Amman while the city's population is growing by 6% a year. It has no significant public transport infrastructure – except for roads. Between 2004 and 2007 the amount of gasoline sold in the city reflected the fact that the number of cars in use increased by 250%! At its current rate of traffic growth – estimated at 6% a year – the city will be paralysed within a decade. The solution is neither easy to implement nor cost free: new road systems, road widening, significant public transport investment and new road traffic management governing bodies.

If possible, traffic problems are even worse in Lebanon where sitting on average 3 hours a day in traffic is commonplace. In Lebanon the extent of the gap in road traffic governance is truly breathtaking. In 2000 the World Bank publicised their Beirut Urban Transport Project study, for which they were stumping up the cash. By 2010 the project manager reported that he was only half way through the implementation and had not started on any of the difficult tasks! The biggest improvement has been the installation of traffic lights – although no-one enforces them. The income from parking meters simply disapears. With a national average of 350 cars per 1,000 inhabitants entire areas of the city are grid-locked. The solution?

Investment in public transport or simply price people out of their cars.
‘Business as usual’ isn’t a viable option. Lebanon’s Nafi‘a, the infamous vehicle registration and driver licensing institution, aggravates the congestion through its shady or lax measures on granting “driving schools” permission to operate, awarding driver’s licenses, and controlling the number of taxis, vans and trucks. In addition the police simply offer no punishment for drivers who violate the law.
Since antiquity, Syria has served as a major crossroads for international trade and Syrian

[illegible] prospered from the east-west and north-south movement of goods and people. However, at independence, the country's transportation routes were fractured. France split off Beirut, its main port, into

Lebanon and gave its second port, Iskenderun, to Turkey. Not a great start. but it has focused the authorities on strategic transportation planning, especially for Damascus, a city of 6MN people, almost 1/3 of the total population.

Damascus is a Unesco World Heritage Site and is thought to be one of the oldest continually inhabited cities on the planet. For almost the same length of time, traffic congestion has been a problem. Perfect traffic chaos is created daily by opposing traffic flows. For example at the western end of the Old Town, vehicles want to travel north-to south – to the airport, to the coast or wherever – from Aleppo to Beirut. Pedestrians want to travel east-to-west – from Hariqa and Hamidiyeh suqs to the Suq Midhat Pasha and the Bab al-Zabieth suq. The irresistable meets the immovable.

Shoved off course by the crisis, the Directorate of Traffic and Transport Engineering in Damascus expected to announce the financing plan for its USD1.6 billion Green Line project for the Damascus metro in September 2010. France-based Systra Group carried out the feasibility study for the line between 2007 and 2009 , funded by the European Investment Bank. The Green Line was planned to connect the southwest (Moadamiyeh) and northwest (Qaboun) areas of the city- over 16.5 km with 17 stations. It was to have been the first of four lines covering a total of 52 km planned for the city. The metro rail had been planned to reduce congestion in Damascus and, eventually, to link up with the planned Moadamiyeh railway, the Hijaz railway, Damascus international airport and the next proposed metro line, the Red Line, that will run north-south across the city. All a pipe dream for the present!

The underlying problems, however, won't evaporate. Road systems in most major cities of the MENA Region are heavily overloaded, impacting on economic growth. MENA governments recognise this and are developing plans to tackle the challenge. The question is, where to find the money? The solution is probably road charging.

Successful projects in large European cities have proven that congestion charging encourages more travellers to use public transport. The United Arab Emirates, Qatar, Egypt, Syria, Tunisia and Morocco have all signalled that it's the way to go, driven by a growing awareness that electronic toll collection (ETC) is a sustainable fund raising source for development of infrastructure.

Far fetched? Road tolling projects already in place include the King Fahd Causeway connecting Saudi Arabia and Bahrain and the Cairo-Alexandria Toll Road. ETC is in use on the Turkish road network and the Dubai Salik highway – Shaikh Zayed Road. Total revenues from road toll/road charging collection in the MENA region was estimated at $1 billion in 2010. This equates to 0.8% of global toll collection revenues, estimated at $125 billion in 2010. At an estimated growth rate of 15%, MENA's tolling revenues are expected to be $2.1 billion in 2015 and $5.1 billion in 2020.

Given the choice of more cars moving on higher-priced roads or fewer cars stuck on gridlocked ones, which would you choose?