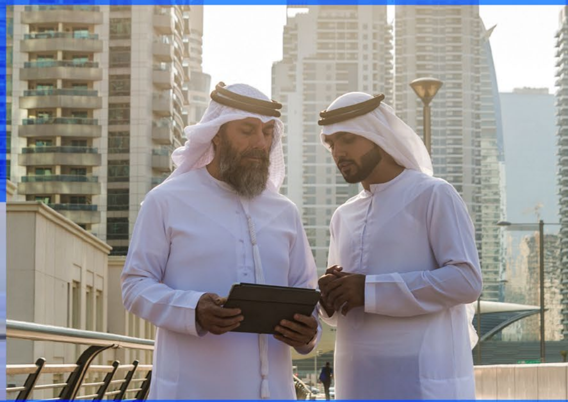
KPMG

Middle East Economic Outlook



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- The Gulf Cooperation Council (GCC) region is expected to be relatively less impacted by global trade frictions and enjoy relatively robust growth. In Saudi Arabia in particular, diversification efforts should continue to drive strong growth in the non-oil sector.
- Alongside longer-term structural reforms, near term activity will also be supported by a strong labour market and muted inflationary pressures. This favourable backdrop could see household consumption continue to rise over the coming years.
- While cost pressures are prevalent in specific sectors, headline inflation across much of the GCC remains relatively low. The latest data shows inflation hovering around 2% and, in some cases such as in Bahrain, falling into deflationary territory.
- Interest rates are expected to fall further in the region over the coming year. While this will be welcomed by both households and businesses, interest rates remain a long way off neutral levels. The tight monetary policy stance represents a downside risk for the domestic economy by constraining activity.
- Market expectations point to oil prices remaining below their 2024 level, and below break-even levels for several GCC economies' public finances. This could pose a challenge for governments if fiscal policy is to act as a stabilisation tool.
- Structural reforms in the Saudi labour market have driven unemployment rates to record lows and increased participation. However, the depreciation of the Saudi riyal could make it more expensive to attract and retain high skilled expats, requiring further contribution from local population.

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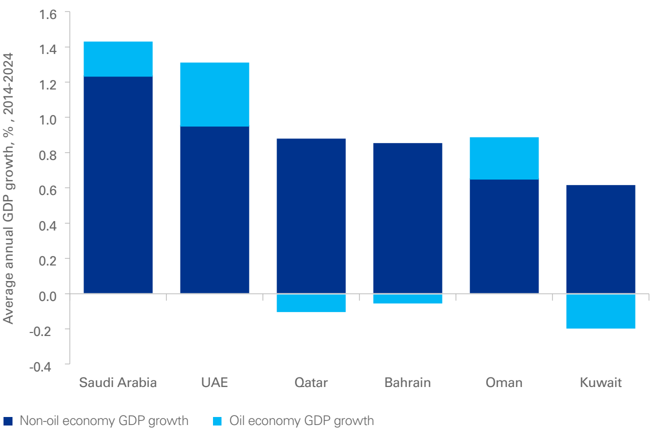
Growth outlook remains robust despite challenges

The growth outlook for the Gulf Cooperation Council (GCC) region is strong despite the backdrop of global headwinds. Economic activity is set to be supported by continued structural reforms and diversification efforts by governments. In recent years, the GCC has attempted to move away from oil dependency, with policies aimed at growing the size of the non-oil economy. Since 2014, growth in the non-oil economy has outpaced the oil economy across the GCC (see Chart 1). In Saudi Arabia, the non-oil economy has seen its share of Gross Domestic Product (GDP) increase from 40% in 2010 to 55% in 2025. This has been underpinned by robust economic growth over the past 14 years in the non-oil economy, growing almost twice as fast as the oil-economy during that period.

Chart 1: Growth over the past decade has been driven by the non-oil sectors of the economy across the GCC



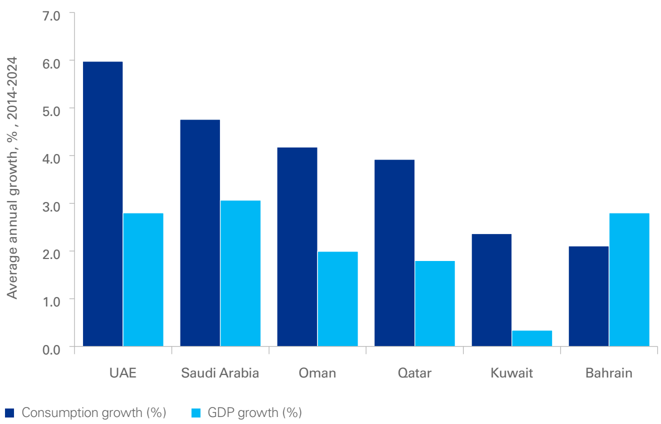
Source: National Statistical Agencies, Haver Analytics, KPMG analysis

Investment is set to continue to be a key driver of activity in the region over the coming years. The GCC region faces significant demand for investment both to support the rapid pace of population growth, which is projected to increase at more than double the world average, as well as to continue diversifying the structure of its economies away from a reliance on energy exports. GCC sovereign wealth funds have played a key role in driving investment activity in the region, particularly in the non-oil sectors as part of the region's wider diversification strategy. In Saudi Arabia, the Public Investment Fund (PIF) currently holds nearly $US950 billion in assets and given the large size of its balance sheet and the mandate to drive investment in the non-oil sector of the economy, it is expected to drive activity in the non-oil sectors of the economy.

Trade activity is set to provide additional support to the GCC's growth outlook. The decision by GCC OPEC members to raise oil production will mechanically lift headline GDP by increasing export volumes, even if weaker oil prices dampen revenues. Beyond hydrocarbons, strong external demand for petrochemicals, metals, and transport services will also contribute to trade-driven growth. Importantly, the region has thus far avoided the worst of the trade frictions affecting other economies, with energy exports remaining exempt from US tariffs. Looking ahead, ongoing investments in ports, logistics, and free zones are expected to further integrate the GCC into global supply chains, strengthening its position as a hub for both east–west trade and non-oil exports. The outlook for tourism in the GCC remains broadly positive over the coming year. In 2024, the sector contributed nearly US$250 billion to regional GDP, according to the GCC Statistical Centre, reflecting both a rebound in visitor arrivals and sustained investment in hospitality and infrastructure. Tourism has become a central pillar of the region's economic diversification agenda, with each member state embedding ambitious targets within their respective Vision programmes.

Looking ahead, unemployment is expected to remain low, supported by robust near-term economic growth and sustained investment across key sectors. With domestic inflationary pressures muted and unemployment low across the region, real household incomes are set to rise over the coming years. This favourable backdrop should underpin continued strong growth in household consumption, which has been a key driver of overall expansion. Over the past decade, real consumption growth has averaged 3.9% across the GCC, compared with GDP growth of just 2.1% over the same period. (see Chart 2).

Chart 2: Consumption has been a key driver of growth for the GCC

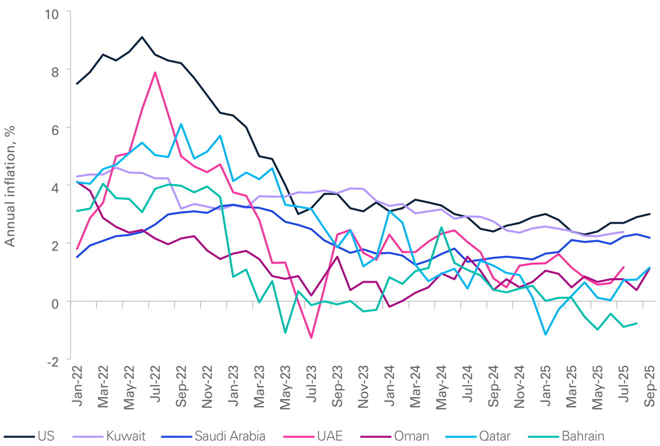


Source: National Statistical Agencies, Haver Analytics, KPMG analysis

Inflation is broadly subdued across GCC although localised cost pressures persist

Headline inflation across much of the GCC remains relatively low, with half of the region's economies experiencing inflation rates below 1% and, in some cases, such as in Bahrain, falling into deflationary territory. In Saudi Arabia, headline inflation stood at 2.2% in September 2025, up from 1.6% at the start of 2025 (see Chart 3).

Chart 3: Inflation is relatively low across the GCC



Source: National Statistical Agencies, Haver Analytics, KPMG analysis

Despite headline inflation remaining relatively low, there are a few upside risks to the outlook. The depreciation of the US dollar since the start of 2025 has impacted the region, with five out of the six of the region's economies currently maintaining a peg with the dollar. Market expectations point to continued weakness for the US dollar over the coming year. For GCC countries who are maintaining a currency peg, this could potentially lead to a rise in costs, particularly in sectors such as construction and hospitality which are dependent on imported goods and materials.

The housing market is also contributing to households' cost pressures, particularly in Saudi Arabia, where rental prices increased by 7% in September 2025 on an annual basis. While this represents an easing from a peak of 11% recorded in January 2024, the current rate of growth still indicates a heated residential property market (see Chart 4). A significant driver behind this is the sharp uptick in demand for housing, particularly concentrated in major urban centres in Saudi Arabia, thanks to a substantial influx of expatriates drawn by expanding job opportunities.

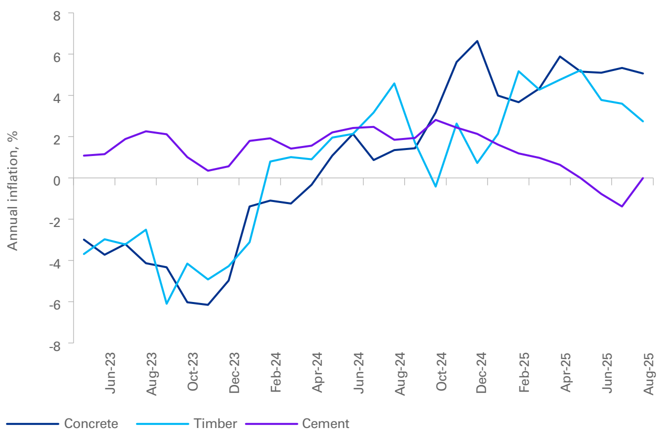
Chart 4: Saudi rental price inflation has slowed but remains elevated

Source: General Authority for Statistics, Haver Analytics

The Saudi government has taken measures to improve housing affordability, including increasing the supply of housing and implementing rent freezes. However, the recent depreciation in the Saudi riyal could increase the cost of imported construction materials and overseas labour, potentially slowing down projects. The latest data from the Saudi General Authority for Statistics shows the price of concrete and timber, key inputs for construction, increased by 5% and 3% respectively in September 2025 **(see Chart 5)**. Part of the increase is driven by global factors; however, the depreciation of the riyal is likely also adding to the upward pressure on input costs.

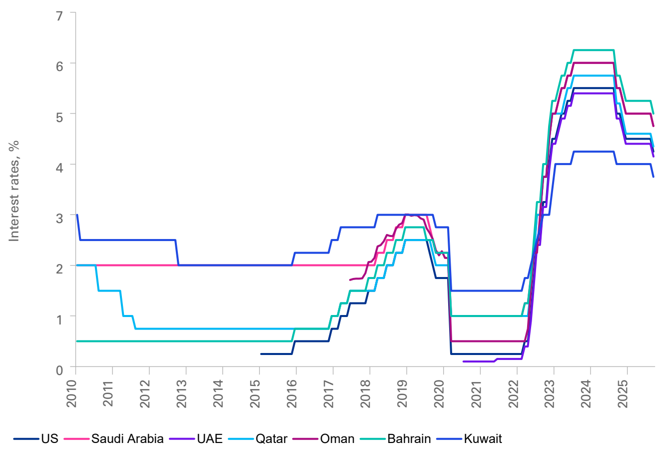
The Federal Reserve began cutting interest rates in September 2025, and the GCC central banks have followed suit, easing their respective interest rates for the first time since the end of 2024 **(see Chart 6)**. Market expectations point to further interest rate cuts by the Federal Reserve over the coming year, that will likely see interest rates continue to fall across the region. A looser monetary policy would be a more appropriate stance by the domestic central banks given the muted price pressures in the region. Nonetheless, interest rates remain restrictive, and further easing may be needed to move rates closer to neutral levels.

Chart 5: Timber and concrete prices have outpaced headline inflation in Saudi Arabia



Source: General Authority for Statistics, Haver Analytics

Chart 6: Interest rates could fall further across the region

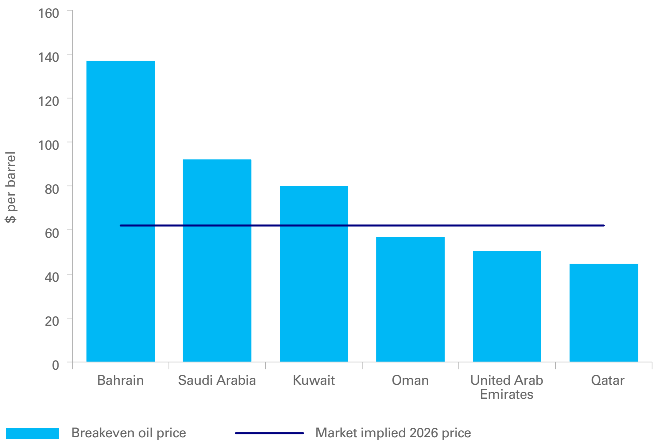


Source: Haver Analytics

Low oil prices are a downside risk for public finances outlook

The prevailing level of global oil prices remains a key driver of the economic outlook across GCC region. Recent evidence points to the global crude market being well supplied, as steady increases in oil production have led to a gradual accumulation of global crude inventories. Furthermore, demand conditions remain muted, with tariff announcements in April causing a sharp decline in oil prices to the US$60-70 range. Market expectations point to prices remaining in this range, well below the average price of US$80 per barrel recorded in 2024. The outlook for oil prices has significant implications for public finances in the region. With oil potentially set to average around US$62 over the coming year, this will be below the breakeven level necessary to achieve a balanced budget in half of the GCC economies (see Chart 7).

Chart 7: Oil prices could average below fiscal breakeven levels for some GCC economies



Source: IMF, Haver Analytics, KPMG analysis. Note: Breakeven oil price represents the oil price at which a country's oil revenues are sufficient to run a balanced budget.

In 2024, the GCC economies ran modest deficits, averaging 0.3% across the region. With oil prices set to average 15% lower this year, some governments across the region could run higher deficits in the absence of fiscal tightening. While robust growth in the non-oil sectors across the GCC, driven by structural reforms has seen oil dependency fall, the energy sector continues to represent a disproportionate share of the tax base in the region. Oil receipts account for 70% of total government revenue across the GCC, with the share of oil revenue highest in Kuwait, at 88%.

In the wider policy context, lower oil prices, implies a potentially more limited level of fiscal policy space and a slower pace of public investment throughout the region, which could hamper diversification efforts. In its pre-Budget statement, the Ministry of Finance of Saudi Arabia reported its latest forecast for the fiscal deficit to fall from 5.3% in 2025 to 3.3% in 2026. The impact of lower oil prices could see further cutbacks in spending by the country's sovereign wealth fund, which reported investments fell by more than 12% in 2024.

Policies to broaden the tax base and target activity in the non-oil sectors of the economy could help reduce dependency on oil revenues more quickly, potentially reinforcing the diversification gains already made since 2016. As the share of non-oil sectors in GDP continues to expand, capturing more of this activity within tax receipts would allow government revenues to reflect the growing diversity of the broader economy.

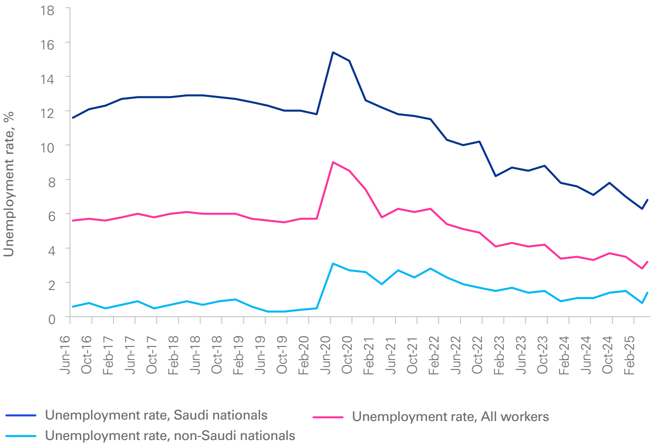
Box: Structural reforms and robust growth to provide boost for Saudi labour market

Unemployment has declined across the GCC in recent years, reflecting stronger private sector activity and ongoing economic diversification efforts. The structural reforms undertaken under the region's Vision programmes have also strengthened labour markets, particularly in Saudi Arabia.

The Saudi unemployment rate fell to its lowest level on record in Q1 2025, reaching 2.8%. That was accompanied by an increase in the number of Saudi nationals entering the labour market over the past decade. The Vision 2030 programme originally set a target of 7% unemployment among Saudi nationals by 2030 **(see Chart 8)**. Over the past decade, the unemployment rate for Saudi nationals has fallen from 12% in 2016 to 6.8% as of Q2 2025. This target was achieved ahead of schedule, prompting a downward revision to a new target of 5% by 2030.

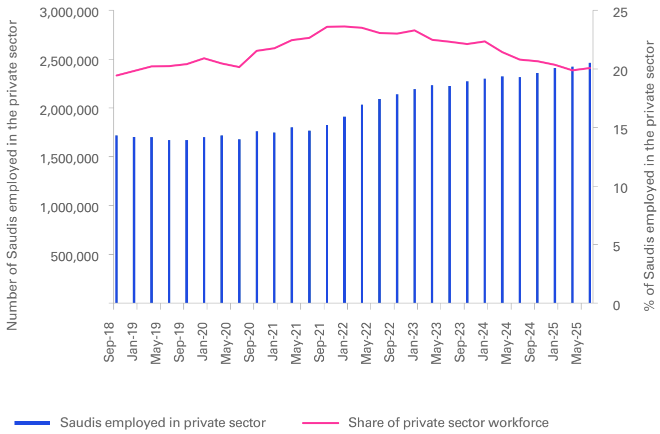
The fall in unemployment has also been accompanied by a rise in the participation rate, particularly among women. The Vision 2030 programme originally set a target of 30% female labour force participation in 2016. This goal was achieved as early as 2020 as the labour force participation rate amongst women increased from 18% in 2016 to 30% in 2020. This led to an upward revision of the target in 2023 to 35% by 2030. Several policy reforms, including the Saudization of key sectors, have supported the increase in both participation and employment rates among Saudi nationals. The private sector has been the main absorber of new entrants to the labour market, with the number of Saudis employed in the sector rising by 43% since 2018 **(see Chart 9)**.

Chart 8: Strong labour market activity has driven Saudi unemployment to a record low



Source: General Authority for Statistics, Haver Analytics

Chart 9: The overall number of Saudis employed in the private sector has risen sharply but share of private sector workforce has remained constant



Source: General Authority for Statistics, Haver Analytics, KPMG analysis

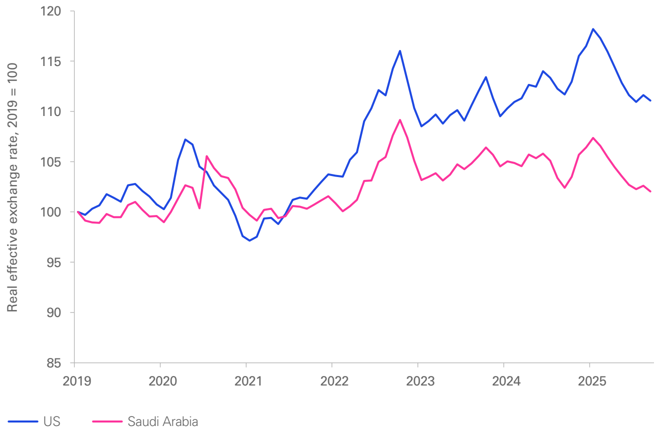
Despite the overall increase in participation, the share of Saudi workers in the private sector has remained broadly unchanged, edging up only from 19% in 2018 to 20% in 2025. This highlights the continued reliance on expatriate workers, particularly in industries where skills gaps persist and demand outpaces the domestic supply of labour.

Expats remain a major source of labour especially in construction, healthcare, hospitality, and specialised technical fields. Strong population growth, large-scale infrastructure projects, and the rapid expansion of service-oriented industries are all expected to sustain demand for foreign workers in the years ahead. At the same time, diversification efforts under Vision 2030 are creating new roles in knowledge-intensive sectors that will require expertise not yet fully developed within the domestic workforce.

However, the recent depreciation of the Saudi riyal against has introduced new challenges for the expatriate workforce. For many overseas workers, a weaker currency reduces the value of remittances sent home, particularly in sectors such as construction, care, and hospitality. To offset this loss, some workers may seek higher wages, potentially increasing labour costs in these industries (see Chart 10).

The impact could be even more pronounced in attracting and retaining high-skilled expatriates, especially in globally competitive sectors such as finance, technology, and healthcare, where internationally mobile talent has greater bargaining power. These pressures could make it more difficult to attract expats in the absence of higher pay.

Chart 10: The Saudi riyal has depreciated alongside the US dollar since the start of the year



Source: Bank of International Settlements, Haver Analytics, KPMG analysis kpmg.com/uk/en/**macroeconomics**

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