The GCC post-pandemic: Massive and fast transformation

Tomorrow starts today

April 2021

pwc

Introduction

As our region emerges from the immediate impact of the COVID-19 pandemic, driven by the imperatives to repair, rethink and reconfigure our economies and societies, we are entering a new phase of transformation that will be massive in scale and extremely fast moving.

Over the past year, I have worked closely with our clients – governments, health authorities, government-related entities, corporates and family businesses – in tandem with steering our own firm through the crisis and anchoring our regular "COVID-19 – Transitioning to the New Normal" webcasts.[1] This has given me a privileged and at times humbling position from which to see how the region has responded, and now to assess how we move forward.

Faced with the double shock of the pandemic and an oil price collapse, our economies have proved to be highly resilient, dynamic and digitally capable. Yet this is not the moment to let up – this is the time when we must reinvent the future, pressing on with transformational change at scale and at speed.

In this short paper, I explore our region's transformation pre-crisis, the impact of COVID-19 on the forces reshaping our world, the lessons learnt and pick out my top five areas where an accelerated cycle of repair, rethink and reconfigure will be vital to achieving the required massive and fast transformation in our region.

Stephen Anderson
Strategy and Markets Leader

To summarise in one line:
a new kind of tomorrow starts today.

[1] https://www.pwc.com/m1/en/publications/covid-19/transitioning-to-new-normal-middle-east-updates-webcast-series.html

Demographic and social change

Unemployment reached 8.2% in KSA in 2020

60
percent of GCC citizens are under the age of 30

89%
of the population of the UAE are expatriates

The number of people under 30 in GCC countries is expected to reach 65 million by 2030

Resource scarcity and climate change

The Sweihan solar power park in Abu Dhabi was the largest in the world when it started operating in 2019, generating enough power for 90,000 people

13 out of 22 Arab countries
are classed as having severe water scarcity, with less than 500 m³ water per inhabitant per year, compared to the world average of 6,000 m³

GCC countries import about 85% of their food, including close to 100% of all rice consumed, 93% of cereals, and approximately 62% of meat

Shift in power east

China, India, Japan and South Korea are KSA's biggest export markets

3
of the GCC countries are in the top 10 of the world's largest oil producers (Saudi Arabia, UAE, Kuwait)

The GCC is positioned at the heart of trade flows between the fastest-growing regions of the world: Asia and Africa

Rise of Technology

^93%
of KSA citizens between the ages of 10 and 73 are internet users

$70bn
will be invested by MENA countries in mobile infrastructure between 2019 and 2025

^40% of shoppers in the UAE and KSA buy online via their smartphone daily or weekly, compared to 33% globally

Urbanisation

2.5 million pilgrims travelled to Mecca for the Hajj in 2019

$1.6 trillion
of infrastructure investment is required in the GCC to support the growing population

Brand new cities being created, such as the $500bn investment to build NEOM, a zero-carbon city in Saudi Arabia

The GCC is at the epicentre of the megatrends

***Sources:** Please check references page 19

Transformation in the GCC pre-COVID-19

Back in 2013, we identified five long-term trends that would reshape the world over the next 50 years – the “megatrends”. The GCC was, and still is, at the epicentre of these transformational forces, as the facts above demonstrate.

What we hadn’t anticipated was the speed with which these long-term trends were already impacting the region, and the need for leaders to change their strategies and approach to address the challenges created by the rapid pace of change. There were a multitude of second order factors already impacting society, business and individuals. We captured these in our ADAPT framework.

The combination of fiscal pressures after the 2014 oil price crash combined with those of the megatrends, meant governments in the GCC had to take action. Saudi Arabia responded with Vision 2030, the wide-ranging strategic framework to diversify the Kingdom’s economy away from oil and future-proof the country by addressing each of the megatrends. Other GCC countries also set out their own strategic and transformational programmes.

As a result, over the following five years the region went through an unprecedented period of economic and social change. Then COVID-19 happened.

Asymmetry

Increasing wealth disparity and the erosion of the middle class

A

Disruption

The pervasive nature of technology and its impact on individuals, society and the climate

D

Age

Demographic pressure on business, social institutions and economies

A

Polarisation

Breakdown in global consensus and a fracturing world, with growing nationalism and populism

P

Trust

Declining confidence in the institutions that underpin society

T

Impact of COVID-19

COVID-19 is first and foremost a health crisis, and citizens in GCC countries have not escaped its impact. Governments in the GCC moved quickly in March and April 2020 to bring in travel restrictions and other measures to contain the spread of the virus as it swept across the globe, and while economies opened up later in the year, social distancing and other preventative measures have remained in force.

In addition to the COVID-19 crisis, the region was hit by a second shock when it was severely impacted by the drastic fall in oil prices to their lowest level in 17 years. State revenues in the region are oil-dependent, and if prices had stayed at their lows of around $20 a barrel, GCC governments faced the prospect of losing $554m a day, according to Strategy& estimates.[2]

At the same time, decisions taken on health grounds took a severe toll on the region's economy, particularly in the tourism[3] and service sectors, prompting governments to deliver economic stimulus packages worth an initial $122bn, with further support following to help ease some of the burden where possible.

$122bn

prompting governments to deliver economic stimulus packages worth an initial $122bn

[2] https://www.strategyand.pwc.com/m1/en/covid-19-oil-price-drop-gcc.html
[3] In the GCC, the tourism sector alone lost $60 bn: https://gccstat.org/images/gccstat/docman/publications/GCC_Economic_Performance_and_Outlook__2020.pdf

Both globally and locally, the impact of COVID-19 has made a significant, and generally negative, impact on each of the ADAPT forces.

COVID-19 has the overall impact of speeding up the ADAPT forces

Asymmetry

Global impact

- The poor (people, regions, countries) will get hit the hardest
- Unemployment at the bottom of the wealth pyramid, which will also grow
- Massive failure of small business
- Sovereign debt and GDP growth issues

Local impact

- Exposure of structural economic weaknesses
- Competitive edge for large companies
- Pressure in urban infrastructure and resources

Disruption

Global impact

- Strength and influence of big technology platform companies will grow faster
- In the short-term, climate worries are forgotten as the world deals with the crisis, but in the medium/long-term people are likely to become more socially conscious

Local impact

- Increased adoption of Industry 4.0
- Dominance of major tech players
- New ways of living, working and consuming

Age

Global impact

- Increased pressure on young countries as there are fewer job opportunities
- Increased pressure on pensions and social welfare systems in older countries
- Challenges stimulating job creation in developing markets compounds the issue
- Intergenerational debate

Local impact

- Youth bulge and unemployment challenges
- Ageing population and the looming pensions crisis
- Shift to preventive and personalised healthcare

Polarisation

Global impact

- Increased localisation of economies due to supply-chain issues
- Heightened nationalism as nation states look to blame “others” and protect themselves
- The potential for humanity to come together after the crisis to solve important problems

Local impact

- Jockeying among superpowers
- Slowbalisation and localisation
- Challenges of global and regional integration

Trust

Global impact

- Distrust in institutions and their ability to respond fairly will grow
- Some institutions and leaders will come out of the crisis with a stronger reputation

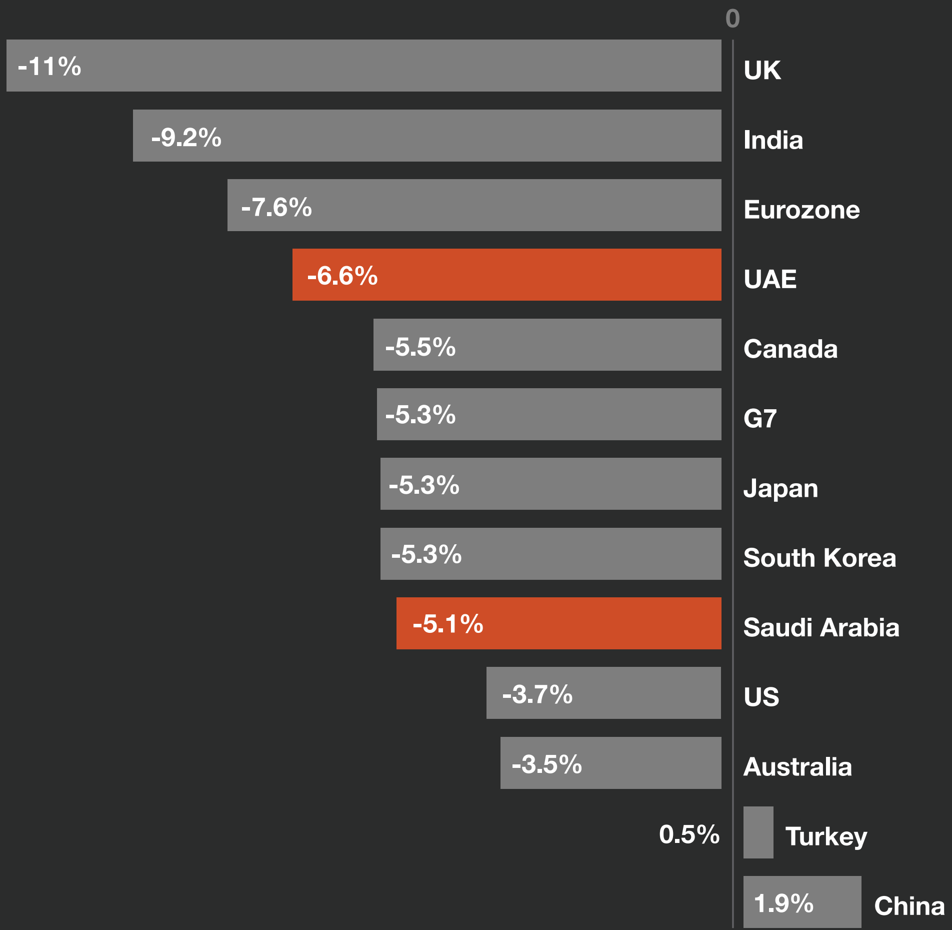
Local impact

- Citizen-centric and platform governments
- Transition to a sustainable, low-carbon future
- Integrated safety and security management

Our Strategy& colleagues will shortly launch an **Ideation Center paper** that identifies these local ADAPT impacts and explores in detail the various policy challenges and potential solutions

Despite the twin shock, the GCC economy still showed itself to be at least as resilient as other regions in 2020:

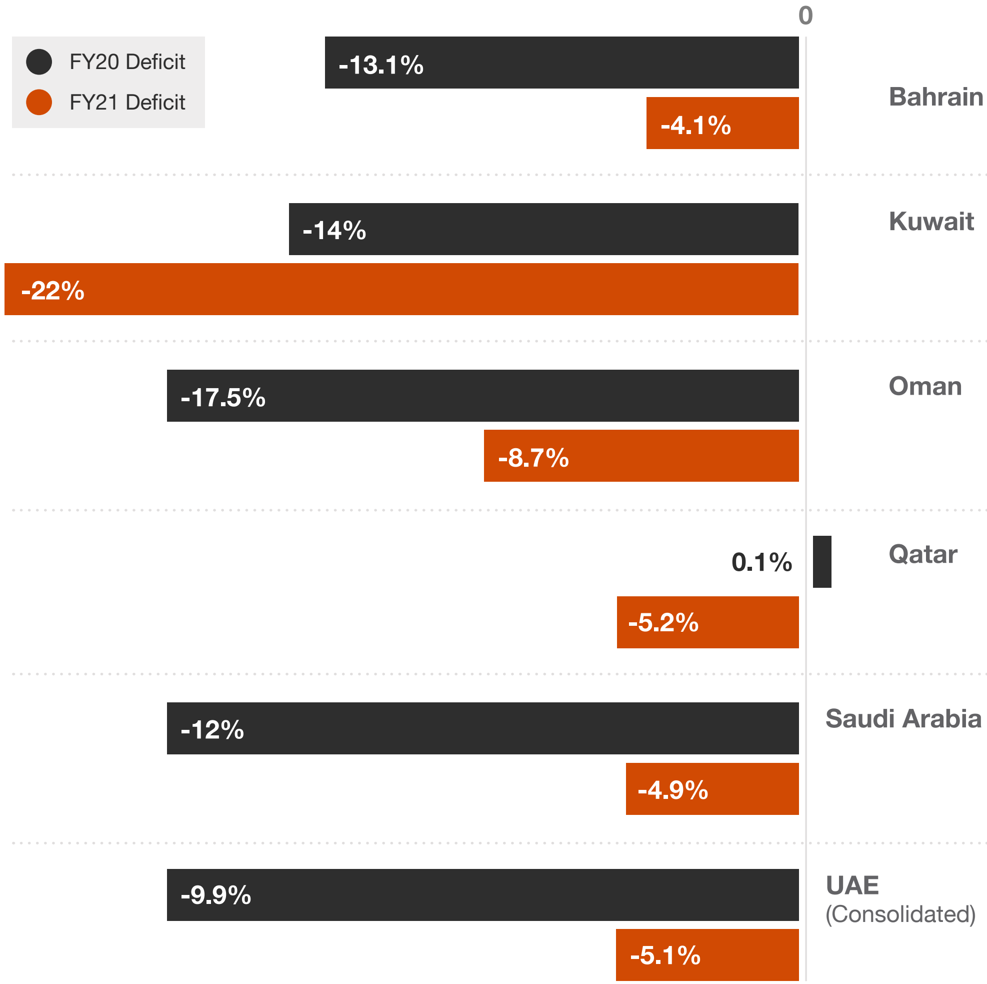
Projected 2020 GDP relative to 2019 GDP (%)



Source: PwC analysis, IMF

The damage to government balance sheets from the two crises means tackling fiscal deficits will be a top priority in the short to medium term, and makes transformative change to diversify the economy and spur growth more important than ever.

Fiscal balance as a share of GDP, fiscal year 2020 vs fiscal year 2021



Source: PwC/IMF/IHS Markit

Reasons for confidence

Despite the unprecedented damage and disruption of 2020, our 2021 Middle East CEO Survey shows a highly optimistic outlook among the region's corporate leaders – 72% believe that worldwide economic growth will improve in 2021, in line with a record 76% among global CEOs. In the Middle East 52%, compared with 47% globally, are very confident that their organisation's revenue will grow over the next three years.[4]

There are certainly reasons for optimism in the GCC, which fall into five broad categories:

1. The strong **health response** in the GCC is likely to accelerate the repair and recovery phases across the region. As of April 2021, the UAE had the third-highest vaccination rate in the world.[5]

2. **Trust** in institutions has remained strong – 81% of citizens in key Middle East cities believe their city is effectively managing the impact of COVID-19. Here, and across the world, the government will play a central role in driving the recovery of economies post-crisis.

3. With an increased focus on the **energy transition** away from fossil fuels and into renewables, hydrogen and electrification, the GCC is in the fortunate position of once again having abundant natural resources.

Middle East urban consumers believe that their city is effectively managing the impact of COVID-19

My city was well prepared to deal with the impact of COVID-19

46%
All territories

76%
Middle East

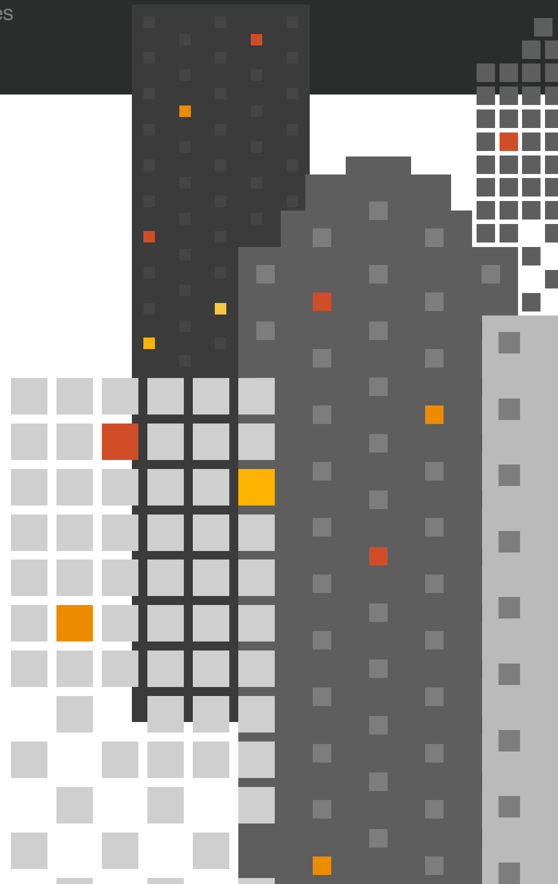
My city is effectively managing the impact of COVID-19

56%
All territories

81%
Middle East

4. The GCC is home to several of the world's largest **sovereign wealth funds**, with the Abu Dhabi Investment Authority holding $579.6bn in assets, for example.[6] This considerable quantity of dry powder will drive investments and support economic transformation plans.

5. Finally, there have been important **positive diplomatic changes** in the region, with the normalisation of relations between the UAE and Israel agreed in September 2020 (the Abraham Accords), and the reconciliation between GCC countries and Qatar agreed in January 2021 (the Al Ula Accord).



[4] https://www.pwc.com/me/ceosurvey
[5] https://www.nytimes.com/interactive/2021/world/covid-vaccinations-tracker.html
[6] https://www.statista.com/statistics/276617/sovereign-wealth-funds-worldwide-based-on-assets-under-management/

Personal reflections

5

Five key lessons we've learned over the past year

Stephen Anderson

Strategy and Markets Leader

1

Real-time management

We've never managed the firm so closely as during the initial wave of COVID-19, when there was such a high degree of uncertainty in every aspect of our working lives. Understanding in detail, on a daily basis, the location and wellbeing of our people, alongside the business metrics of the pipeline of new work, cashflow and utilisation, required real-time data and insight. This demonstrated the value of our cloud infrastructure and real-time, anytime, anywhere access to data dashboards, and we have carried on with these habits and practices.

2

Trusted relationships

It is very difficult to build new relationships online, no matter the extent to which we've managed to digitalise our interfaces and delivery models. Relationships remain central to work, particularly here in the region, and as restrictions ease, it is vital to incorporate relationship building into your future strategy and ways of working.

3

Productivity and global insight

Remote working can be highly efficient if managed in the right way. With so many stereotypes about working from home debunked, we saw five years of transformation in the first two months of lockdown. We've also realised it is possible to have real-time access to the best global expertise on any topic instantly, rather than expecting them to fly in to talk to us.

4

Engagement, communication and empathy

We've never communicated more with our people and have placed a far greater emphasis on empathy and two-way communication. The vital importance of wellbeing and mental health – for too long seen as something not to speak about openly – is now very clear.

5

Rapid innovation and change management

A major change that will come out of COVID-19 will be companies' approach to change itself, and particularly digital adoption. Even the most technology-averse people can now seamlessly manage on-line meetings and workshops. During COVID-19 restrictions, we showed that people and organisations adapt very quickly through necessity, meaning the days of long-winded IT and change management programmes may be over. A new blueprint is under construction to drive change and adoption.

Five key transformation themes in the GCC

Just as the 2014 oil crisis was the driving force for the initial wave of transformation in the region, COVID-19 and its aftermath will also accelerate progress. The region has proved it can deliver ambitious and wide-ranging changes, and now needs to take its achievements to the next level. While many of the issues governments tackle will be similar to the last decade, there are three key differences in 2021:

Stronger burning platforms

The combination of pressures created by COVID-19, the oil price drop and accelerating megatrends/ADAPT forces are much stronger than in 2014.

Digital

The transformation will be digitally led – 59% of Middle East CEOs in our latest survey aim to increase their investments in digital transformation by 10% or more over the next three years, compared with only 11% in our 2010 survey, after the global financial crisis.

Sustainability

Sustainability will play a far stronger role, as governments worldwide, investors and consumers make environmental, social and governance (ESG) factors a cornerstone of their decision-making.

Both globally and here in the region, in the aftermath of the pandemic governments and societies will re-evaluate what success looks like in the future. In the past, putting GDP growth and shareholder value above all other measures resulted in unprecedented globalisation and wealth creation, and lifted many people out of poverty. But over time, this model has produced extreme disparities, put jobs at risk in many countries, weakened communities and social cohesion and damaged the environment. Going forward, we need to define a local-first and more interdependent and inclusive definition of success.

To achieve this new definition of success in the GCC region, many interdependent factors must be considered. However, in five key areas an accelerated cycle of **repair**, **rethink** and **reconfigure** will be vital to achieving massive and fast transformation:

- Digital
- Local-first and employment
- Energy transition and sustainability
- Fiscal innovation
- Value creation

Digital

A great deal has been written about how the pandemic has accelerated digital transformation, but what does that mean on the ground?

There are five things governments and businesses must do:

Reimagine their organisation for the digital age:

Companies and governments don't need a separate digital strategy, they need to refocus on the purpose of the organisation, develop the platforms they need, build on their unique capabilities (behaviour, cognitive and network capital) and build the digital infrastructure that supports these elements.

Use technology to engage:

Organisations must fully engage citizens/customers to become demand-driven rather than supply-driven. There have been great examples in the health and social sector during the pandemic, such as non-urgent doctors' appointments moving to video calls, and apps being used to recruit volunteers or provide access to safe spaces.

Transform their operations:

Companies and governments can use the cloud and emerging technology such as AI to transform the way they operate, automating routine processes and generating, analysing and communicating data seamlessly at every stage to respond to challenges in real-time.

Build trust:

As more companies and government departments use the technology described above, cybersecurity, data privacy and trust in the reliability of data become a vital operational concern.

Digital upskilling

Recruiting people with the right digital skills remains a challenge in the region, however a large majority (85%) of respondents to our Hopes and Fears survey[7] of Middle East employees are confident that they can learn further digital skills to increase their employability. Organisations must harness this enthusiasm by making the right investment to train their people.

[7] https://www.pwc.com/m1/en/issues/upskilling/gcc-hopes-and-fears-2021.html

See how we have worked with our region's major organisations to put transformation into action, together

Reimagine | Engage | Trust | Transform

Local-first and employment

COVID-19 has forced manufacturers worldwide to conduct emergency reviews of their supply chains as entire economies locked down and companies suddenly faced national and international markets where they could no longer reliably source components, manufacture products or distribute their goods to customers. In the GCC, the priority is to localise supply chains in critical sectors including agritech and pharmaceuticals, and to foster employment and private-sector competitiveness by building up local capabilities.

Glocalisation means organisations look to combine the benefits of globalisation (cost efficiencies and scale) with the advantages of localisation (flexibility and resilience) in order to be more agile and provide a better customer experience, enabled by digitisation. The key drivers that enable successful glocalisation are: regionalising the company's supply footprint; increasing the use of robotics and technology to reduce costs when manufacturing and the supply chain moves from lower-cost countries closer to the end market; and changing the overall cost model for production and sourcing.

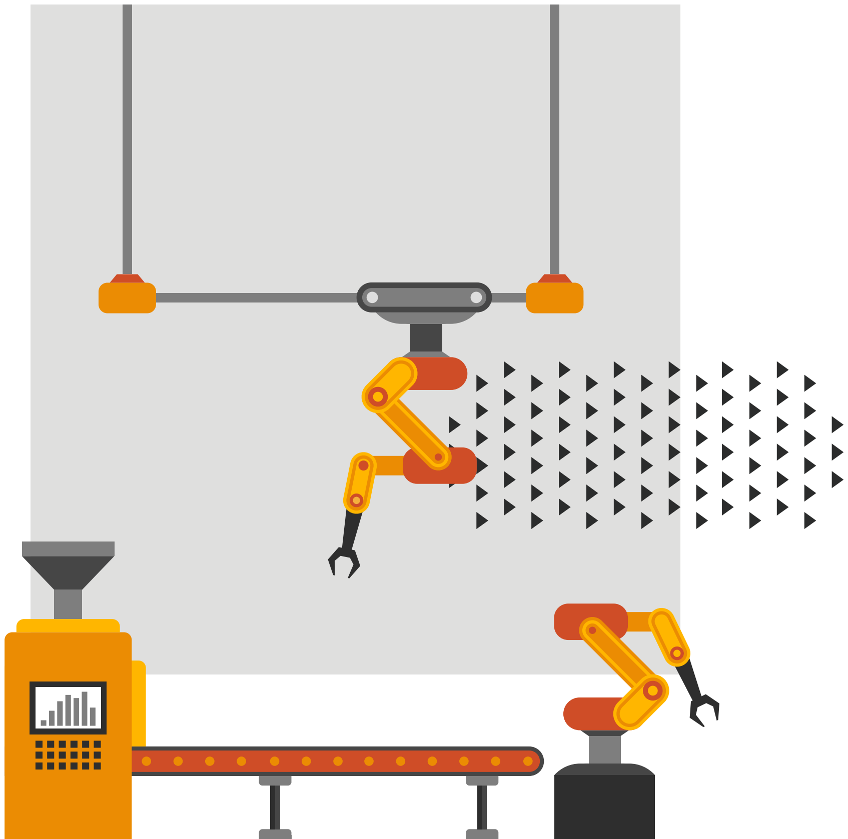
The GCC is very well-placed to take advantage of glocalisation for the following reasons:

Infrastructure: The region has invested heavily in infrastructure projects that support trade, including roads, airports, ports, industrial cities and free zones.

Technology and innovation: Governments are investing in data centres for cloud computing and providing regulatory support for installing 5G networks. The private sector is investing in the necessary technology too, including Big Data analytics, 3D printing and IoT platforms.

Youthful Workforce: Across the broader Middle East, regional governments are partnering with the private sector to diversify the economy and create jobs, as 40% of the population is in the working age category and 2.8 million more job seekers join the labour market each year.

Policies and Incentives: Regional governments in the GCC are putting in place policies and developing incentives to attract foreign and domestic investors, including tax deferrals or exemptions, marketing support and offtake agreements, access to funds, and subsidies.



Energy transition and sustainability

As identified above, our region has a tremendous opportunity to play a key role in the world's energy transition, with vast potential for solar power, and opportunities to develop a green hydrogen economy. Some GCC countries have launched initiatives, including the UAE's Energy Strategy 2050[8] and Saudi Arabia's Vision 2030, that feature ambitious targets for adding renewable and clean energy to their energy mix. For example, the UAE is investing more than $163bn to use clean energy for half of its energy mix by 2050. Establishing public-private infrastructure partnerships (PPPs) as part of post-COVID economic stimulus plans is of crucial importance.

Adopting a circular economic model could also save the GCC $138bn between 2020 and 2030.[9] GCC governments and major industrial players have realised that the traditional and dominant linear economic model of "take, make, use, and waste" is unsustainable. The chemicals industry, for example, can use lighthouse projects such as the reconditioning and reuse of barrels or recycling worn-out tyres to inspire trust in the circular economic approach and to form a more holistic ESG strategy.[10]

[8] https://www.trade.gov/knowledge-product/united-arab-emirates-renewable-energy
[9] https://www.strategyand.pwc.com/m1/en/press-releases/2019/adopting-circular-economic-model.html
[10] https://www.strategyand.pwc.com/m1/en/ideation-center/ic-research/2019/circular-chemistry.html

Fiscal innovation

All GCC countries plan to scale back government spending in their 2021 budgets, compared to pre-COVID levels. Nevertheless, fiscal deficits will continue for most countries in the region in 2021; KSA for example, is expected to run a fiscal deficit of 6% of GDP. This year also marks the beginning of a large amount of Gulf sovereign debt reaching maturity – more than $100bn between 2021 and 2025, according to the IMF.[11]

As countries look to improve their fiscal balance following the dual shock of 2020, fiscal policy in the region is also likely to start to focus on revenue increases. Changes include Oman's planned personal income tax, subsidy reforms in a range of countries and even corporate income tax.[12]

Public policy positions are also being revisited, with the UAE making several innovations including 100% foreign ownership of companies in the base economy,[13] Dubai's remote worker visa and an expansion of the 10-year long-term visa programme. Saudi Arabia announced that by 2024 companies would be required to house their regional headquarters in Riyadh in order to do business with state entities. The government is also establishing special economic zones (SEZ) to stimulate the manufacturing, trade and logistics sectors.[14]

[11] https://www.imf.org/en/Publications/Policy-Papers/Issues/2020/12/08/Economic-Prospects-and-Policy-Challenges-for-the-GCC-Countries-49942
[12] https://english.alarabiya.net/en/business/economy/2020/11/02/Oman-to-introduce-high-earners-income-tax-in-2022-Finance-minister
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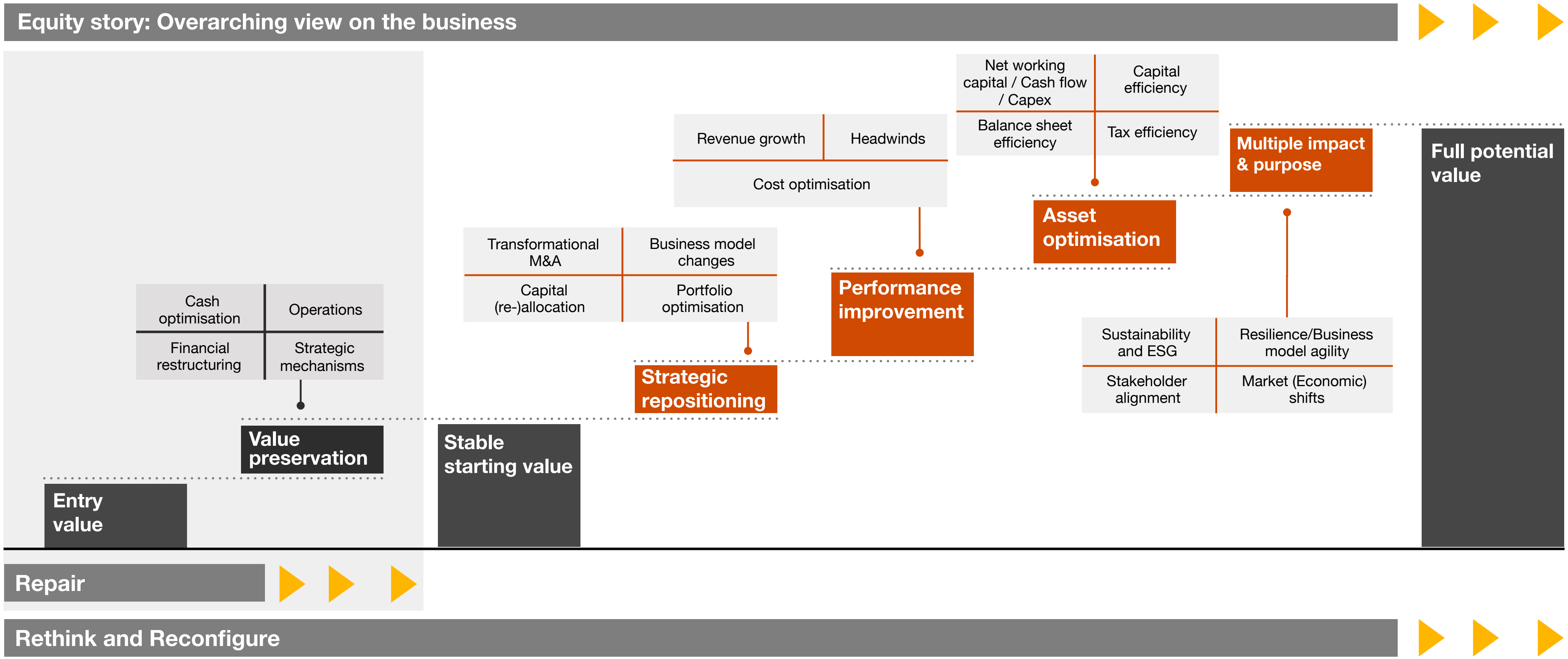
Value creation:

Portfolio and company transformation

As organisations go through the cycle of repair, rethink and reconfigure at speed, they will need to look fundamentally at how they preserve and create value.



Because of the scale and urgency of change, divestitures and acquisitions will be an important trend. Indeed, in 2020 transactions in the Middle East were up 6% compared to a decline of 9% globally, as companies across the region looked to adapt quickly through strategic M&A.[15]

From our client conversations there are five themes emerging in value creation:

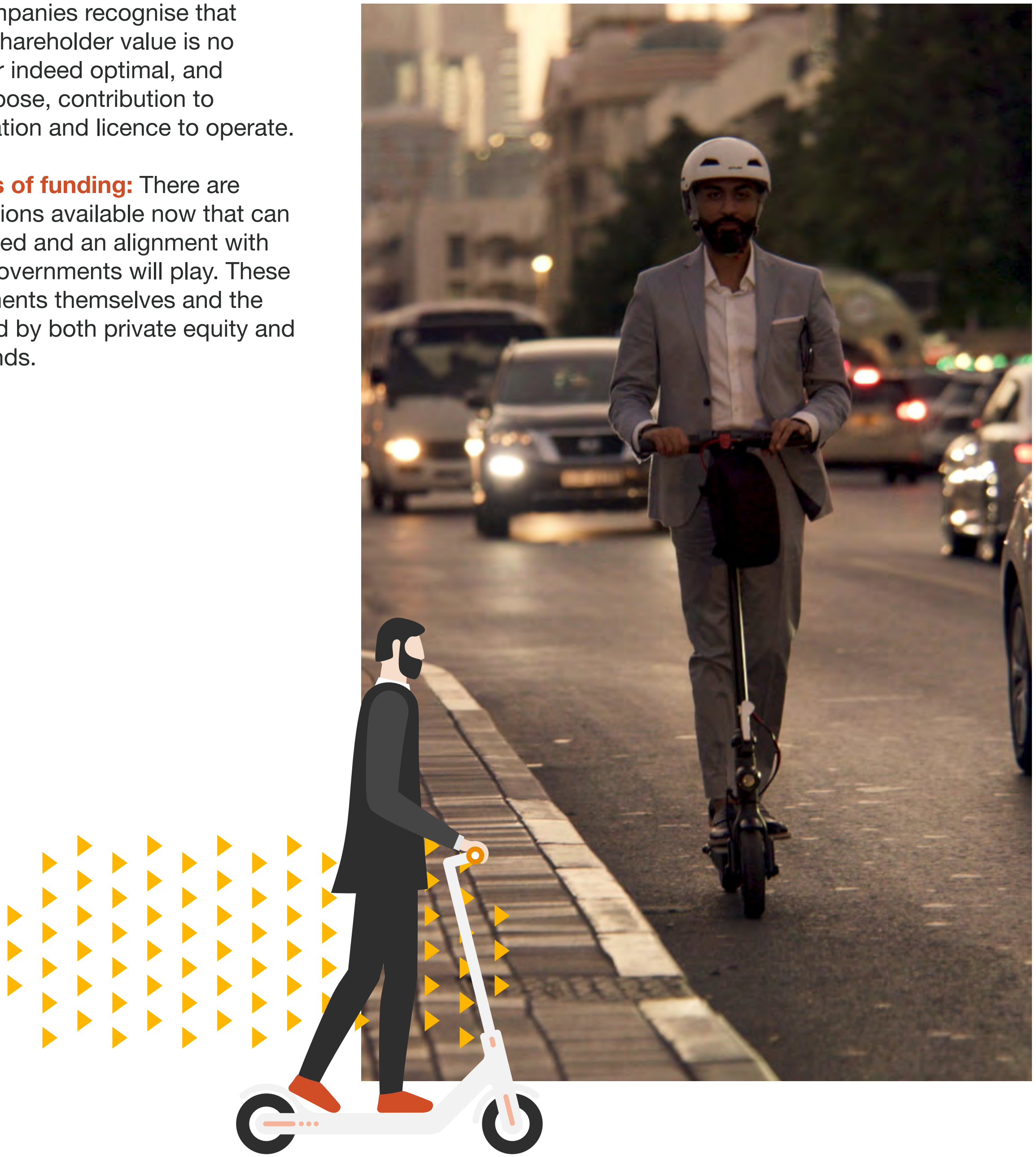
Resilient growth: The need to rethink and plan for future growth, whether organic or inorganic (M&A), is more important than ever, yet the luxury of long-term strategic planning with linear moves is no longer available. Companies need to scenario plan for different alternatives but also carry out regular pulse checks to change course as required.

Capabilities driven: Companies are refocusing on the capabilities that will give them the right to win, which can be achieved by acquiring businesses that fill their future capability needs and by divesting businesses that no longer fit.

Alliances and partnerships: Companies are challenging traditional business models by using alliances and partnerships to gain greater agility and better serve local markets.

Societal value: Companies recognise that a myopic focus on shareholder value is no longer acceptable or indeed optimal, and are reassessing purpose, contribution to sustainability, reputation and licence to operate.

Alternative sources of funding: There are different funding options available now that can create flexibility, speed and an alignment with the enhanced role governments will play. These include the governments themselves and the vast dry powder held by both private equity and sovereign wealth funds.



[15] https://www.pwc.com/m1/en/publications/transact-middle-east-2021.html

Conclusion

As Saudi Arabia made clear during January’s virtual World Economic Forum, Vision 2030 is just the beginning, with $6 trillion of investment opportunities planned in the Kingdom over the next 10 years. The GCC as a whole has the resources, both in terms of its accumulated know-how and experience and natural resources, including renewable sources, for an electrified future, to undertake transformation at the speed and scale that will be required.

To achieve the new local-first, interdependent and inclusive definition of success, governments must harness their existing progress in transforming their societies and economies and move even faster, as a new kind of tomorrow starts today.

A new kind of tomorrow starts today

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