

Distr.
LIMITED
E/ESCWA/EDID/2017/Technical Paper.3
7 June 2017
ORIGINAL: ENGLISH

Economic and Social Commission for Western Asia (ESCWA)

The impacts of the introduction of value added tax in Gulf Cooperation Council countries



**United Nations
Beirut, 2017**

17-00357

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Introduction

Creating a value added tax (VAT) in Gulf Cooperation Council (GCC) countries is a recurrent idea, which has recently re-emerged with insistence. The budgetary difficulties faced by GCC countries in the aftermath of the 2014 oil price shock convinced them to reform their existing tax systems. As recommended by the International Monetary Fund (IMF), they agreed to introduce new tax instruments to compensate for reductions in government revenues resulting from falling oil prices, and to strengthen their financial systems. Each member State is expected to issue its own national VAT legislation, based on agreed common principles. Qatar and the United Arab Emirates have publicly committed to a 5 per cent VAT rate, and other countries are expected to introduce a similar rate. At the end of January 2016, the Saudi Cabinet had given its final approval for a region-wide VAT.¹

Over the past 50 years, VAT has become a major source of government funding for many countries. VAT has existed in France in some form since 1948; its modern version was introduced in April 1954. VAT is currently levied by 150 countries, and contributes to around 20 per cent of global tax revenues.² Nevertheless, its implementation in GCC countries raises several questions. It is no easy task to create a taxation mechanism in countries that have marketed themselves as service hubs, and used their tax-free status to attract businesses and consumers from across the world. Critics argue that VAT will increase the cost of doing business and should be integrated in the business models of established companies. It is also an additional cost for consumers, and can have a one-off inflation impact. However, VAT supporters maintain that the economic literature shows that countries with VAT tend to have a lower variance in tax revenues as a share of gross domestic product (GDP) relative to countries without VAT³ - a strong argument in the GCC region, where oil price variations have severely impacted fiscal positions.

This dilemma has caused heated debate between experts and officials. The present paper sets out the contribution of the Economic and Social Commission for Western Asia (ESCWA) to this debate. It provides a micro-founded estimation of the overall impact of this reform on the six GCC countries. In contrast to studies by IMF⁴ and Deloitte,⁵ the present paper does not focus only on the fiscal impact of VAT introduction, but also assesses its overall macroeconomic, trade and sectoral implications using the global computable general equilibrium (CGE) model Mirage.⁶

The first section sets out the current taxation system in GCC countries. The second section reviews the economic and fiscal difficulties encountered by the six GCC countries in the aftermath of the 2014 oil price drop. The third section offers economic and fiscal assessments of the implementation of a 5 per cent VAT in GCC countries.

1. TAXATION SYSTEM IN GULF COOPERATION COUNCIL COUNTRIES

Efforts to introduce taxes in the GCC region go back to the 1950s. Since then, several taxes have been introduced and abandoned. In general, when oil prices are down, GCC countries opt for income or corporate taxation, mainly targeting foreigners. Those instruments are abandoned when oil prices rise and/or the exodus

¹ <http://gulfbusiness.com/saudi-cabinet-gives-final-approval-5-vat/>.

² www.oecd.org/mena/competitiveness/45573808.pdf.

³ <http://cerdi.org/uploads/ed/2010/2010.25.pdf>.

⁴ www.imf.org/external/np/pp/eng/2015/111015.pdf.

⁵ www2.deloitte.com/content/dam/Deloitte/xs/Documents/tax/countriesvatimplementation/Deloitte-VAT-in-the-Gulf-countries-infographic.pdf.

⁶ www.cepii.fr/PDF_PUB/wp/2002/wp2002-17.pdf.

of foreign labour is felt in the labour market⁷ and business community. In 2014, total tax revenue in GCC countries was equivalent to 1.6 per cent of GDP, while oil revenue represented 37.5 per cent of GDP (table1).

Table 1. Structure of government revenue in GCC countries (% of GDP)

	2012	2013	2014
Total revenue	48.9	47.6	44.0
Non-oil revenue	8.6	9.6	9.9
Tax revenue	1.6	1.5	1.6
Oil revenue	40.3	38.0	37.5

Source: www.imf.org/external/np/pp/eng/2015/111015.pdf.

Most non-oil revenue comes from tax on trade (table 2), since no personal income tax exists and corporate taxes are levied only on foreign-owned companies. Bahrain, Oman and the United Arab Emirates have taxes below 10 per cent on hotels, entertainment, property rents, and government services (table 3). The GCC official journal of 15 January 2016,⁸ announced the creation of a unique VAT rate at 5 per cent.

Table 2. Structure of non-oil tax revenue in GCC countries

	Total	Income	Goods and services	Corporate	Trade	Property	Other
Bahrain	0.6	...	...	...	0.6	0.3	-0.3
Kuwait	0.8	...	...	...	0.6	0.03	0.2
Oman	2.8	...	...	1.4	0.7	...	0.6
Qatar	1.7	...	...	1.3	0.4	...	0.0
Saudi Arabia	1.4	...	...	0.0	0.9	...	0.5
United Arab Emirates	2.5	...	...	1.0	0.7	...	0.7

Source: www.imf.org/external/np/pp/eng/2015/111015.pdf.

⁷ For a detailed description of the history of taxation in GCC country see Harrison, M (2010), Taxation and the GCC States, Gulf One Lancaster Center for Economic Research.

⁸ www.gcc-sg.org/ar-sa/CognitiveSources/DigitalLibrary/Lists/DigitalLibrary/%D8%A7%D9%84%D8%AC%D8%B1%D9%8A%D8%AF%D8%A9%20%D8%A7%D9%84%D8%B1%D8%B3%D9%85%D9%8A%D8%A9/1454231181.pdf (in Arabic).

Table 3. Structure of taxation systems in GCC countries

Country	Companies and businesses	Withholding tax	VAT and goods and services	Labour tax/fees	Social security tax	Other
Bahrain	<ul style="list-style-type: none"> • 46 per cent tax rate on hydrocarbon companies. • No tax on other corporates. 	<ul style="list-style-type: none"> • No withholding tax. 	<ul style="list-style-type: none"> • Hotel, short-term lease apartment rents and certain restaurants are subject to 5 per cent tourism levy on the gross income. • 12 per cent sales tax on gasoline included in the price. 	<ul style="list-style-type: none"> • \$26.5 monthly fee per foreign worker used to provide on-the-job training and job search assistance for nationals. 	<ul style="list-style-type: none"> • 9 per cent employer's contribution. • 6 per cent employee's contribution. • 3 per cent insurance against employment injuries. • 1 per cent unemployment insurance. 	<ul style="list-style-type: none"> • 10 per cent on the monthly rental of residential and business property. • 5 per cent government levy on gross turnover of hotel services and entertainment. • 1.5-3 per cent stamp duty on transfer of land and property.
Kuwait	<ul style="list-style-type: none"> • 15 per cent flat tax rate on non-GCC companies. • 15 per cent tax rate on capital gains. • 1 per cent tax rate on Kuwaiti shareholding companies to support the Kuwait Foundation for the Advancement of Science. 	<ul style="list-style-type: none"> • No withholding tax. • Tax retention of 5 per cent from each payment due to foreign companies until they present a tax clearance from the Department of Inspections and Tax Claims. 	<ul style="list-style-type: none"> • No tax. 	<ul style="list-style-type: none"> • 2.5 per cent tax imposed on the annual net profits of Kuwaiti companies listed on stock market as national labour support tax. 	<ul style="list-style-type: none"> • 11.5 per cent employer's contribution. • 8 per cent employee's contribution. 	<ul style="list-style-type: none"> • None
Oman	<ul style="list-style-type: none"> • No tax for any business establishment, Omani company or permanent establishment (i.e. foreign branch) if taxable income is under OMR 30,000. 	<ul style="list-style-type: none"> • 10 per cent withholding tax. 	<p>Consumption taxes include the following:</p> <ul style="list-style-type: none"> • 3 per cent tax rate on annual rental of leased premises and cinema tickets. 	<ul style="list-style-type: none"> • 7 per cent levy on the wages of foreign workers used to finance the training of nationals. 	<ul style="list-style-type: none"> • 10.5 per cent employer's contribution. • 7 per cent employee's contribution. • 1 per cent insurance against risks of 	<p>Municipal taxes in Muscat and Salalah. Muscat municipal taxes are:</p> <ul style="list-style-type: none"> • 5 per cent tax rate on hotel income. • 3 per cent tax rate on property rents.

Country	Companies and businesses	Withholding tax	VAT and goods and services	Labour tax/fees	Social security tax	Other
	<ul style="list-style-type: none"> 12 per cent flat tax rate for taxable income over OMR 30,000. 12 per cent tax rate on capital gains. 55 per cent tax rate for companies engaged in petroleum exploration. Individual persons conducting professional business in their individual capacities are taxable at a rate of 12 per cent on income over OMR 30,000. 		<ul style="list-style-type: none"> 2 per cent tax rate on electricity bills in excess of OMR 50. 5 per cent tax rate on hotels and restaurant bills. 		occupational injuries and diseases.	<ul style="list-style-type: none"> 10 per cent tax rate on leisure and cinema income. 10 per cent tax rate on home owners using the drainage system. 3 per cent stamp duty on transfer of land and property.
Qatar	<ul style="list-style-type: none"> 10 per cent general tax rate. 35 per cent tax rate for companies engaged in petroleum exploration. 10 per cent tax rate on individuals conducting business as professionals or sole traders on net business income. 	<ul style="list-style-type: none"> 5 per cent of gross amount of royalties and technical fees. 7 per cent of gross amount of interest, commission, brokerage fees, director's fees, attendance fees, and other fees. 	<ul style="list-style-type: none"> No tax 	<ul style="list-style-type: none"> No tax or fee 	<ul style="list-style-type: none"> 10 per cent employer's contribution. 5 per cent employee's contribution. 	<ul style="list-style-type: none"> None
Saudi Arabia	<ul style="list-style-type: none"> 30-85 per cent tax rate on companies engaged in natural gas investment activities based on internal rate of return. 85 per cent tax rate on entities engaged in oil 	<ul style="list-style-type: none"> 5 per cent on dividends. 5 per cent on interest. 15 per cent on royalties. 	<ul style="list-style-type: none"> No tax. 	<ul style="list-style-type: none"> \$53.3 monthly fees per foreign worker (if firm employs majority of foreign workers) used to finance training for nationals. 2 per cent salary tax for nationals in the 	<ul style="list-style-type: none"> 9 per cent employer's contribution. 9 per cent employee's contribution. 	<ul style="list-style-type: none"> None

Country	Companies and businesses	Withholding tax	VAT and goods and services	Labour tax/fees	Social security tax	Other
	<p>and other hydrocarbon production.</p> <ul style="list-style-type: none"> • 20 per cent tax rate on other companies. • 20 per cent tax rate on capital gains. • 20 per cent tax rate on non-Saudi and non-GCC nationals conducting business or professional activities. 			private sector to provide unemployment compensation.	<ul style="list-style-type: none"> • 2 per cent occupational hazards insurance. 	
United Arab Emirates	<ul style="list-style-type: none"> • No taxes levied by Federal Government and no tax on capital gains. • Except for oil companies, individual Emirates impose income tax up to 55 per cent on taxable income of corporate bodies (not enforced thus far). • 55-85 per cent tax rates on oil companies. • 20 per cent tax rate on foreign banks' taxable income. 	<ul style="list-style-type: none"> • No withholding tax. 	<ul style="list-style-type: none"> • No tax. 	<ul style="list-style-type: none"> • Biannual work permit fees ranging from \$80 to \$1,350, based on certain criteria. 	<ul style="list-style-type: none"> • 15 per cent employer's contribution. • 5 per cent employee's contribution. 	<ul style="list-style-type: none"> • Up to 10 per cent tax rate on hotel services and entertainment. • 5 per cent municipal tax on the annual rental of residential property. • Property registration fee of 2 per cent for Abu Dhabi, and 4 per cent for Dubai.

Sources: Countries' official resources, PKF Worldwide Tax Guide, and EY Worldwide Corporate Tax Guide.

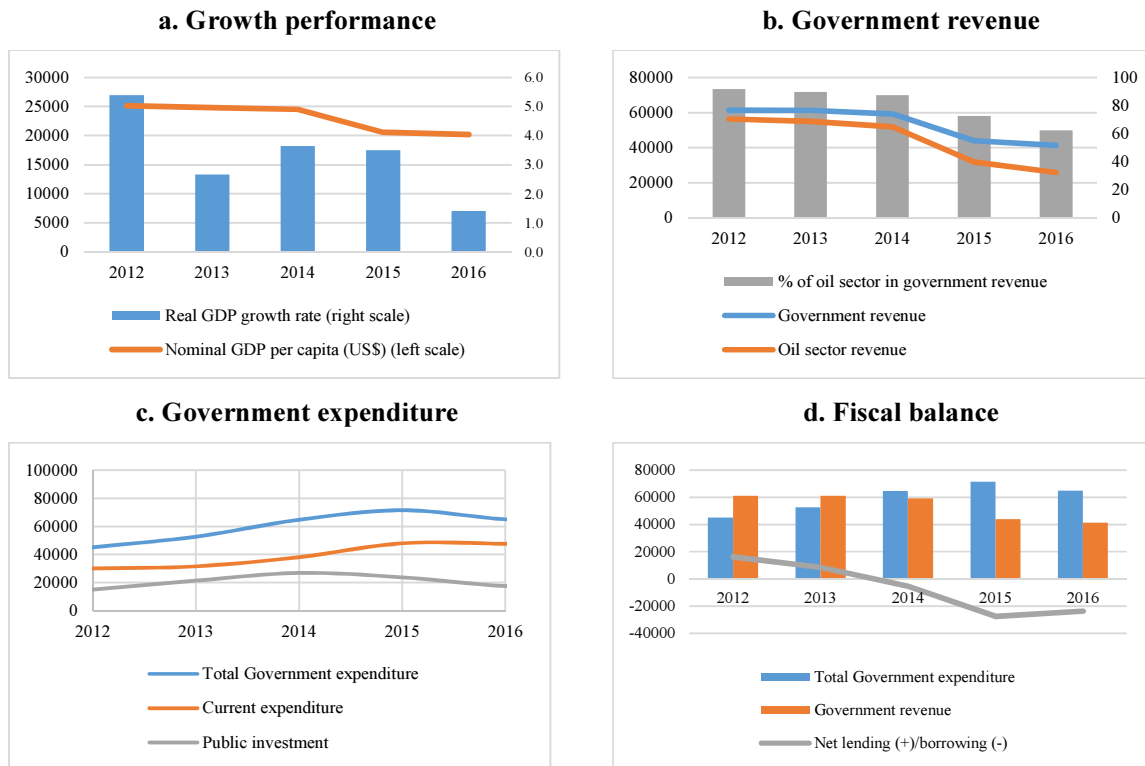
2. ECONOMIC AND BUDGETARY DIFFICULTIES IN GULF COOPERATION COUNCIL COUNTRIES AFTER THE 2014 OIL PRICE DROP

As predicted by ESCWA,⁹ all GCC countries have suffered a drop in their economic activities and considerable tensions in their fiscal situations. Circumstances vary between countries, but growth and fiscal balance have been severely affected across the board. The latest IMF article IV reviews for the six countries provide a comprehensive view on the macroeconomic and fiscal difficulties registered in the six countries.

2.1 SAUDI ARABIA

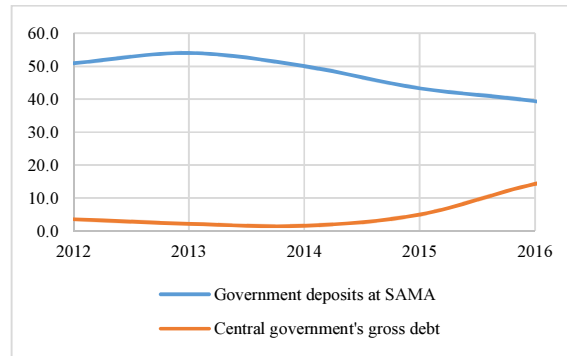
Saudi Arabia, the largest GCC economy, has seen its growth performance decline from 3.5 per cent in 2015 to 1.4 per cent in 2016 (figure 1.a), owing to a drop in oil sector revenues constituting 92 per cent of total government revenue in recent years. Oil revenues dropped by 38 per cent in 2015 and by 19 per cent in 2016 (figure 1.b). Over the same period, the Government was unable to reduce its expenditure. Fiscal adjustment was partially made on public investment, reduced by 11.6 per cent in 2015 and by 26.3 per cent in 2016 (figure 1.c). This situation generated a large deficit, reaching 15.3 per cent of GDP in 2015 and 12.4 per cent of GDP in 2016 (figure 1.d). The public deficit increase has had grave implications in terms of debt and use of foreign reserves. Government deposits at the Saudi Arabian Monetary Agency (SAMA) as a percentage of GDP decreased from 50 per cent in 2014 to 39.4 per cent in 2016, while the central government's gross debt as a percentage of GDP increased from 1.6 per cent in 2014 to 14.2 per cent in 2016.

Figure 1. Economic and fiscal situation in Saudi Arabia



⁹ www.unescwa.org/publications/survey-economic-and-social-development-arab-region-2014-2015.

e. Debt and deposits

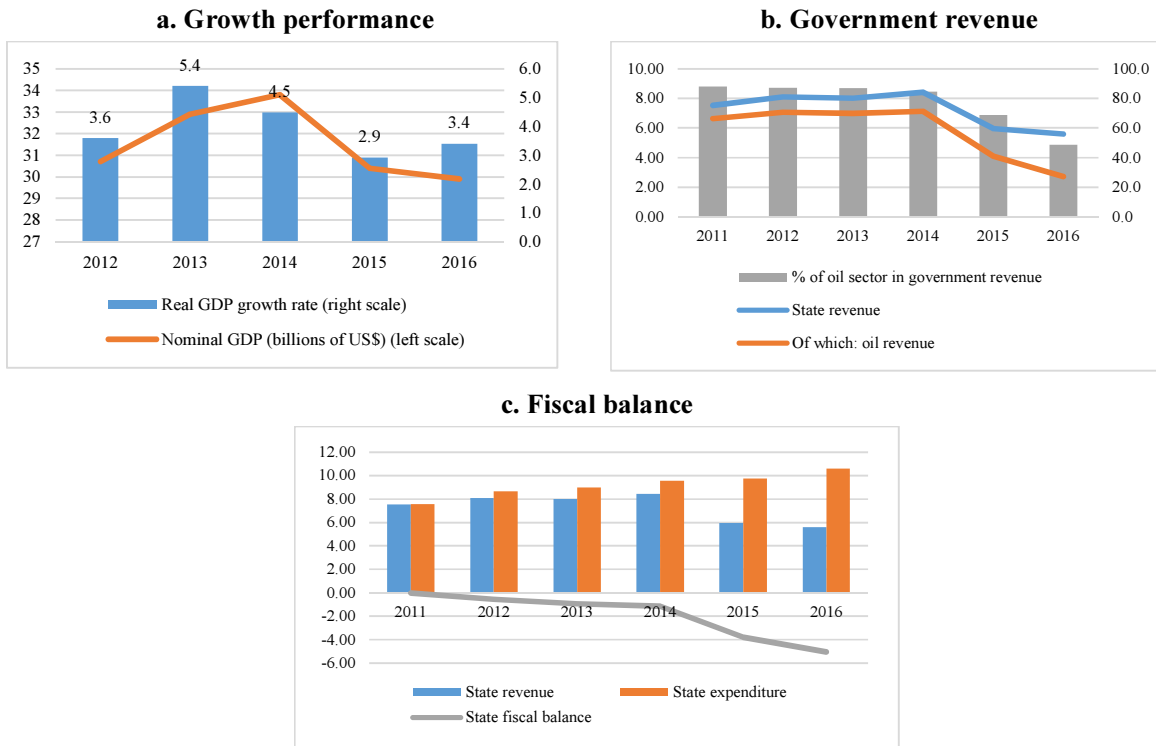


Source: Saudi Arabia 2016 Article IV consultation; and ESCWA estimates based on national sources.

2.2 BAHRAIN

In Bahrain, registered growth performances over the period 2013-2014 have significantly dropped (figure 2.a) owing to the fall in oil prices. Similarly to other oil dependent economies in the region, Bahrain's oil-generated revenue constituted, on average, 84.7 per cent of total government revenue in 2014. Government revenues declined by 42 per cent in 2015 and by 33 per cent in 2016 (figure 2b). As a result of reduced oil prices, the total budget declined by 29 per cent in 2015 and by 6 per cent in 2016. Over the same period, government expenditure increased by 2 per cent of GDP in 2015 and by 8 per cent of GDP in 2016; consequently, the fiscal deficit of 3.4 per cent of GDP in 2014 reached 12.5 per cent of GDP in 2015 and 16.9 per cent of GDP in 2016.

Figure 2. Economic and fiscal situation in Bahrain

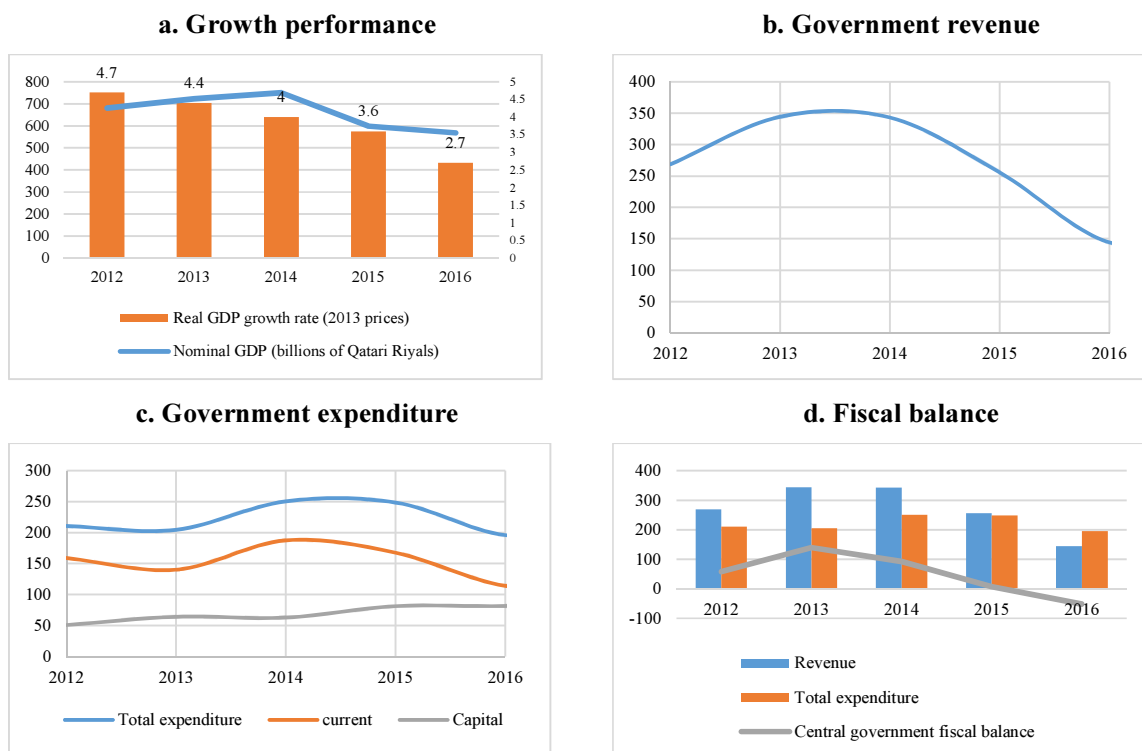


Source: IMF Staff Concluding Statement of the 2016 Article IV Mission; and ESCWA estimates based on national sources.

2.3 QATAR

Qatar's growth dropped from 4 per cent in 2014, to 3.6 per cent in 2015 and to 2.7 per cent in 2016 (figure 3.a). The decrease in oil and gas prices reduced government revenue by 9.1 per cent of GDP in 2015, and by 7.5 per cent of GDP in 2016 (figure 3.b). In parallel, total expenditure fell in 2016 because of a contraction in public current expenditure. However, the Government was not able to reduce its capital expenditure, which increased by 2.6 per cent of GDP in 2015 and by 1.5 percent of GDP in 2016 (figure 3.c). This situation adversely affected the country's fiscal performance, registering a negative balance of 9 per cent of GDP in 2016 (figure 3.d).

Figure 3. Economic and fiscal situation in Qatar

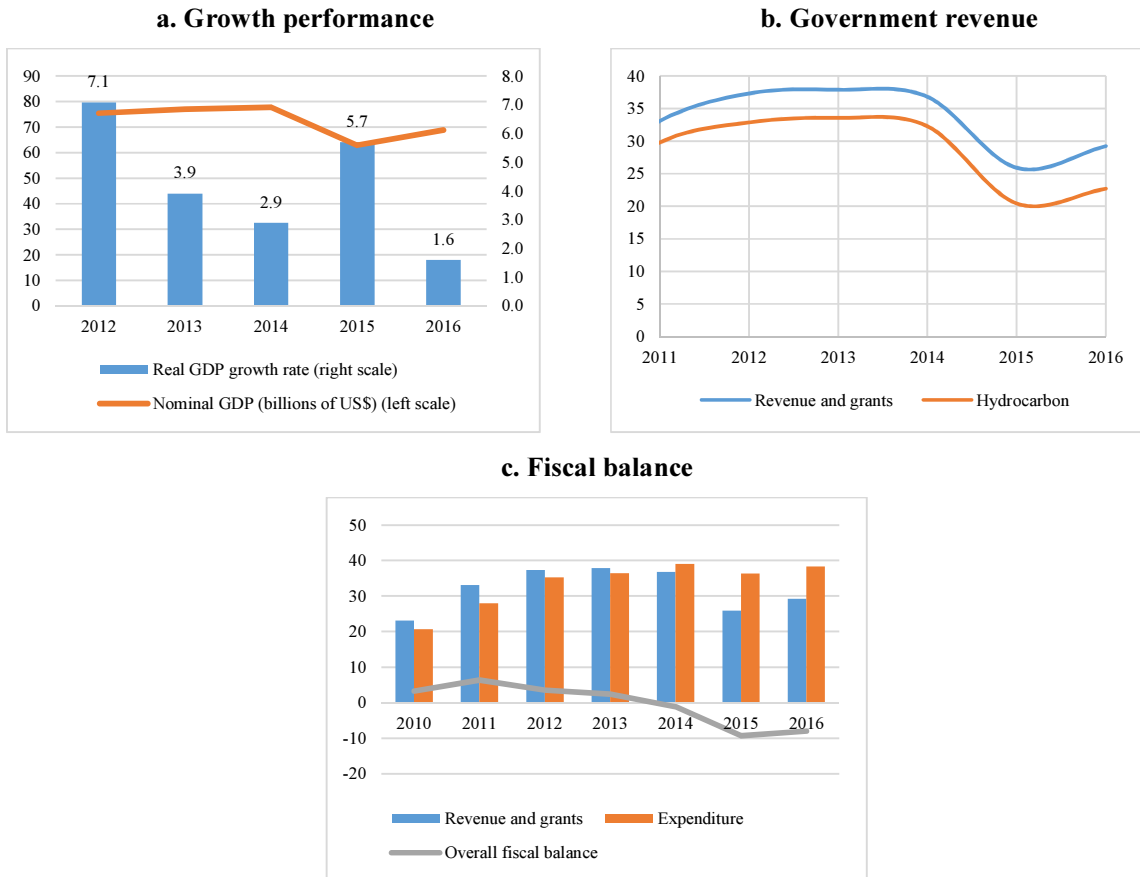


Source: Qatar IMF Country Report No. 15/86, 2015 Article IV Consultation-Staff Report; Press Release March 2015; and ESCWA estimates based on national sources.

2.4 OMAN

In Oman, the economy was less affected in 2015, as growth rates reached 5.7 per cent; however, its 2016 performance was less impressive. Growth dropped by 4.1 per cent compared with 2015 (figure 4.a). Similarly to Bahrain and Qatar, the decline in oil prices significantly impacted government revenues. Oil revenue in Oman represented 88 per cent of total government revenue in 2014. The oil price drop resulted in a 46 per cent decrease in government revenues in 2015 (figure 4.b). On the other hand, the Government increased its total expenditure by 2.9 per cent of GDP in 2015, but reduced it by 6.1 per cent of GDP in 2016. Nevertheless, the fiscal balance remained under severe pressure. The country registered an 18.7 per cent of GDP deficit in 2015, and a 17.9 per cent of GDP deficit in 2016.

Figure 4. Economic and fiscal situation in Oman



Source: Press Release: IMF Staff Completes 2016 Article IV Mission to Oman, May 9, 2016, and ESCWA estimates based on national sources.

2.5 KUWAIT

Despite positive real growth performance, nominal GDP in Kuwait decreased by 30 per cent in 2015, and by 2.4 per cent in 2016 (figure 5.a). Government oil revenue decreased by 52 per cent in 2015, and increased slightly by 1.4 per cent in 2016. The 2015 drop affected total government revenue, with oil revenue constituting 77 per cent in 2014. Total government revenue decreased by 18.7 per cent in 2015, and increased by 11.7 per cent in 2016 (figure 5.b). In response to this shock, the Government increased its total expenditure by 12.2 per cent of GDP in 2015 and by 7.7 per cent of GDP in 2016. As a result, the fiscal deficit reached 11 per cent of GDP in 2015 and 7 per cent of GDP in 2016. However, when taking into account transfers to the Future Generations Fund, the government deficit becomes 17.5 per cent of GDP in 2015, and 17.3 per cent of GDP in 2016 (figure 5.d). Part of this deficit translated into a government debt increase, from 3.4 per cent of GDP in 2014 to 12 per cent of GDP in 2016 (figure 5.e).

Figure 5. Economic and fiscal situation in Kuwait



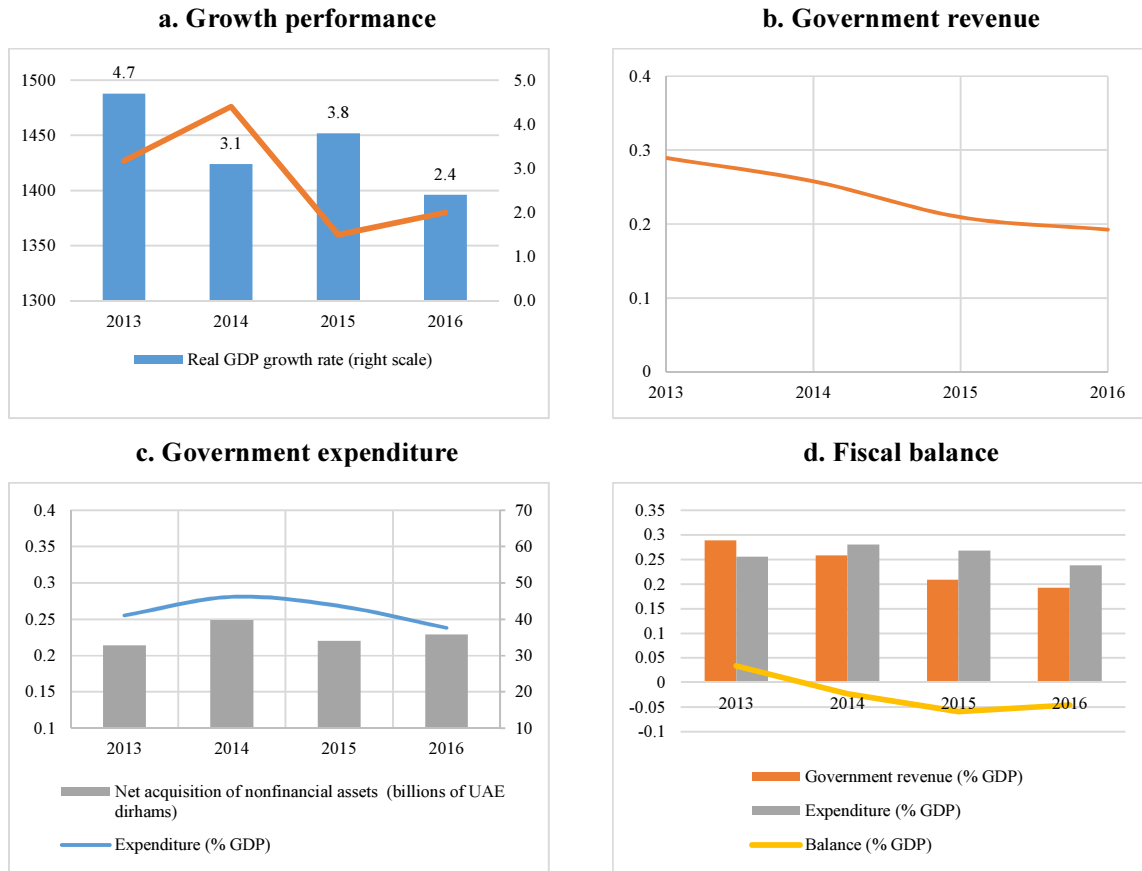
Source: Kuwait 2016 Article IV Consultation-Press Release; Staff Report, IMF Country Report No. 17/15, January 2017; and ESCWA estimates based on national sources.

2.6 UNITED ARAB EMIRATES

Unlike its GCC counterparts, the United Arab Emirates is the most diversified economy among resource-rich countries. The drop in oil prices did not translate into reduced economic activity. The country registered a 3.8 per cent growth in GDP in 2015, dropping to 2.4 per cent in 2016. Meanwhile, in nominal terms, GDP shrank by 8 per cent in 2015, and marginally increased by 1.4 per cent in 2016. Within this context, government revenue decreased by 4.9 per cent of GDP in 2015 and by 1.7 per cent of GDP in 2016. Meanwhile,

expenditure decreased by 1.3 per cent of GDP in 2015 and by 3 per cent of GDP in 2016 - a decrease that affected both current and capital expenditure (12.7 per cent and 14.7 per cent, respectively, in 2015). As a net result, the fiscal situation registered a deficit of 5.9 per cent of GDP in 2015 and 4.6 per cent of GDP in 2016.

Figure 6. Economic and fiscal situation in the United Arab Emirates



Source: United Arab Emirates 2016 Article IV Consultation - Press Release; Staff Report; Statement by the Executive Director for the United Arab Emirates, IMF Country Report No. 17/15, July 2016; and ESCWA estimates based on national sources.

3. ECONOMIC IMPACT OF THE INTRODUCTION OF VALUE ADDED TAX IN GULF COOPERATION COUNCIL COUNTRIES

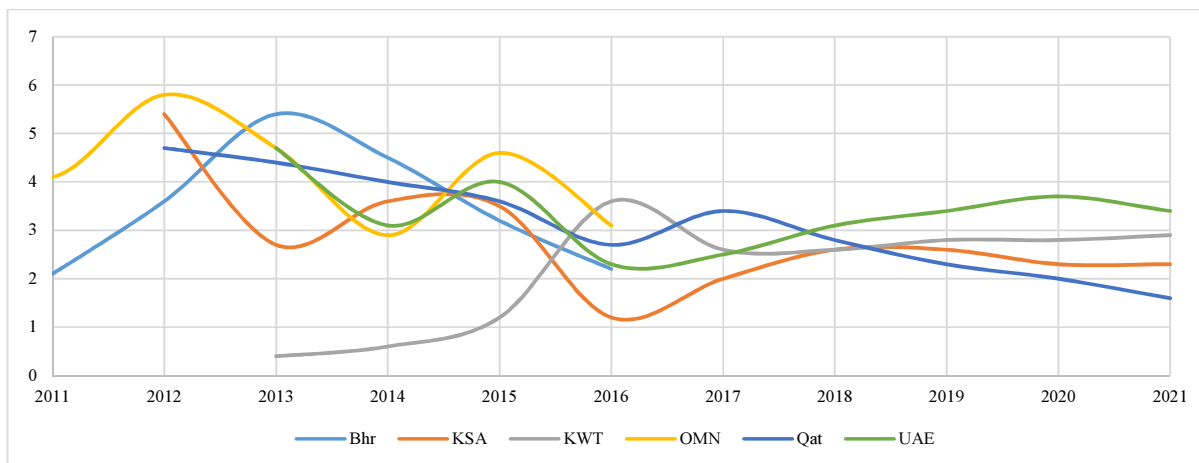
Economic theory predicts that the creation (or change) of a tax instrument creates a distortion in the current economic equilibrium. A new equilibrium is reached through new allocations and distributions of resources among economic actors. Policymakers and professionals evaluate those effects on economic outcomes; they are interested in the assessment of actual and future impacts of various reforms. The CGE model is one of the best instruments to capture the differences between the two equilibriums paths. Since the beginning of 1980s, CGE models have been widely used to analyse various taxation reforms, and to assess their impact in terms of fiscal, growth, trade and sectoral implications.

The economic literature is clear: the implementation of VAT has no systematic effects on the economy. It has an impact on relative prices and, in turn, on households' consumption paths, but its effects on growth, trade and sectoral production depend on Government use of the revenue it generates. Those funds could be used either to reduce the public deficit (which is the aim in GCC countries), or to increase public expenditure. The Government could also implement a mix of such policies. CGE models are suitable tools to assess each

one of these possibilities. By changing the type of closure rules, these models assess the implications of each type of VAT revenue use.

Following this methodology, we used the MIRAGE global CGE model to assess the implications of the implementation of a 5 per cent value added tax in the six GCC countries, starting from 2018. The model assesses the net impact of the reform by comparing variations between the business-as-usual scenario (figure 7), and the simulation results. We simulate the shock with two closure rules. In the first, we suppose that public expenditure remains unchanged and that public deficit is exogenous, so VAT revenue is directly used to reduce public deficit. In the second, we suppose that the fiscal deficit is exogenous and that government expenditure is endogenous, so VAT revenue is directly used to increase public expenditure.

Figure 7. Growth rates for the business-as-usual scenario



Source: ESCWA calculations using Mirage CGE model.

3.1 USE OF VAT REVENUE TO REDUCE THE PUBLIC DEFICIT

The simulations show that the implementation of VAT could generate fiscal revenue of 1.96 per cent of total GCC GDP. At the national level, revenue will vary between 0.86 per cent and 3.12 per cent of GDP. The United Arab Emirates, whose share of consumption in GDP is the highest in the region, could collect the equivalent of 3 per cent of its GDP per year. However, the revenue collected in Qatar will not exceed 0.9 per cent of GDP per year (table 4).

Table 4. VAT revenue as a percentage of GDP in scenario 1

	2018	2019	2020	2021
Total GCC	1.96	1.97	1.98	1.98
United Arab Emirates	3.12	3.12	3.12	3.13
Bahrain	2.38	2.38	2.37	2.37
Kuwait	1.58	1.62	1.65	1.69
Oman	1.74	1.75	1.75	1.75
Qatar	0.86	0.86	0.87	0.87
Saudi Arabia	1.71	1.71	1.71	1.70

Source: ESCWA calculation using Mirage CGE model.

When supposing that the additional fiscal revenue generated by VAT will be used only to reduce fiscal balances, the implication of the implementation of VAT on growth is negative. GCC GDP could drop by around 1.3 per cent. The United Arab Emirates could lose 2.15 per cent of GDP, while Saudi Arabia could lose 1 per cent of its GDP (table 5).

Table 5. Relative variations of GDP following the implementation of VAT

	2018	2019	2020	2021
Total GCC	-1.29	-1.30	-1.30	-1.31
United Arab Emirates	-2.15	-2.16	-2.17	-2.18
Bahrain	-1.63	-1.63	-1.63	-1.63
Kuwait	-0.87	-0.90	-0.93	-0.95
Oman	-1.04	-1.04	-1.05	-1.05
Qatar	-1.06	-1.06	-1.06	-1.06
Saudi Arabia	-0.99	-1.00	-1.00	-1.00

Source: ESCWA calculations using Mirage CGE model.

Simulations also show that the largest effects of the shock are absorbed in 2018 (the implementation date). Figure 8 shows that the the whole region will loose 1.32 growth points in 2018. After the first year, the difference is almost nil. The same conclsn applies to the inflationary impact of this reform. The large effect will occur in the first year. Afterwards, the economy will adapt, with a deflationary effect in Bahrain during the second year (figure 9). The impact on unemployment is important: the region could see its unemployment rates for both skilled and unskilled labour increase by 1-6 per cent (figure 10).

Figure 8. Difference in growth rate, 2018-2021

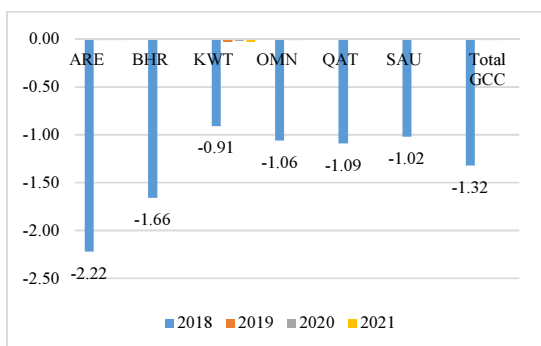


Figure 9. Difference in inflation rate, 2018-2021

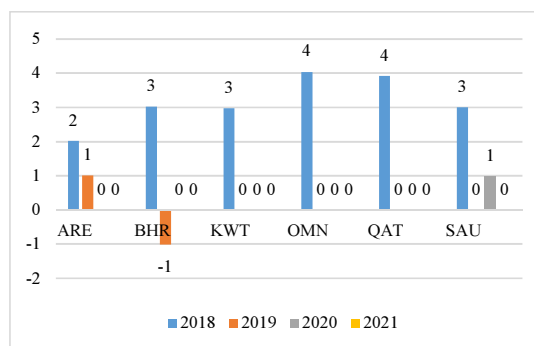
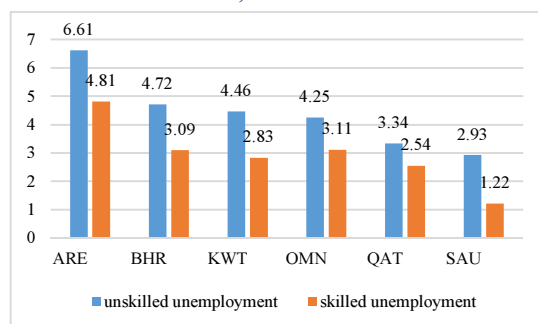


Figure 10. Difference in unemployment rate, 2018-2021



Source: ESCWA calculations using Mirage CGE model.

Decreases in economic activity, increases in unemployment and inflation rises affect the evolution of household consumption. Over the the four years covered by the simulation (2018-2021), household consumption could be reduced by 7 per cent across the region (figure 11). This reduction, in a context where public spending remains unchanged, reduces total imports by an average of 7 per cent (figure 12), which implies a real depreciation of exchange rates and, in turn, an increase in total exports (figure 13).

Figure 11. Cumulative variation of household consumption, 2018-2021

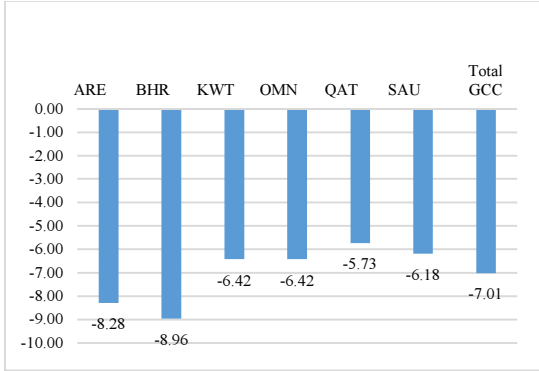


Figure 12. Cumulative variation of total imports, 2018-2021

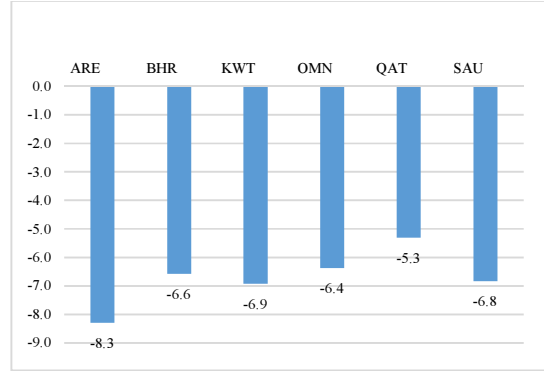
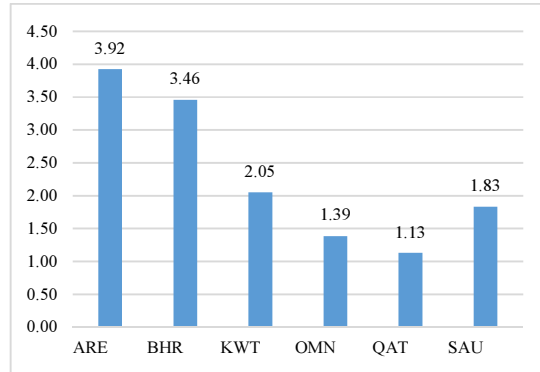


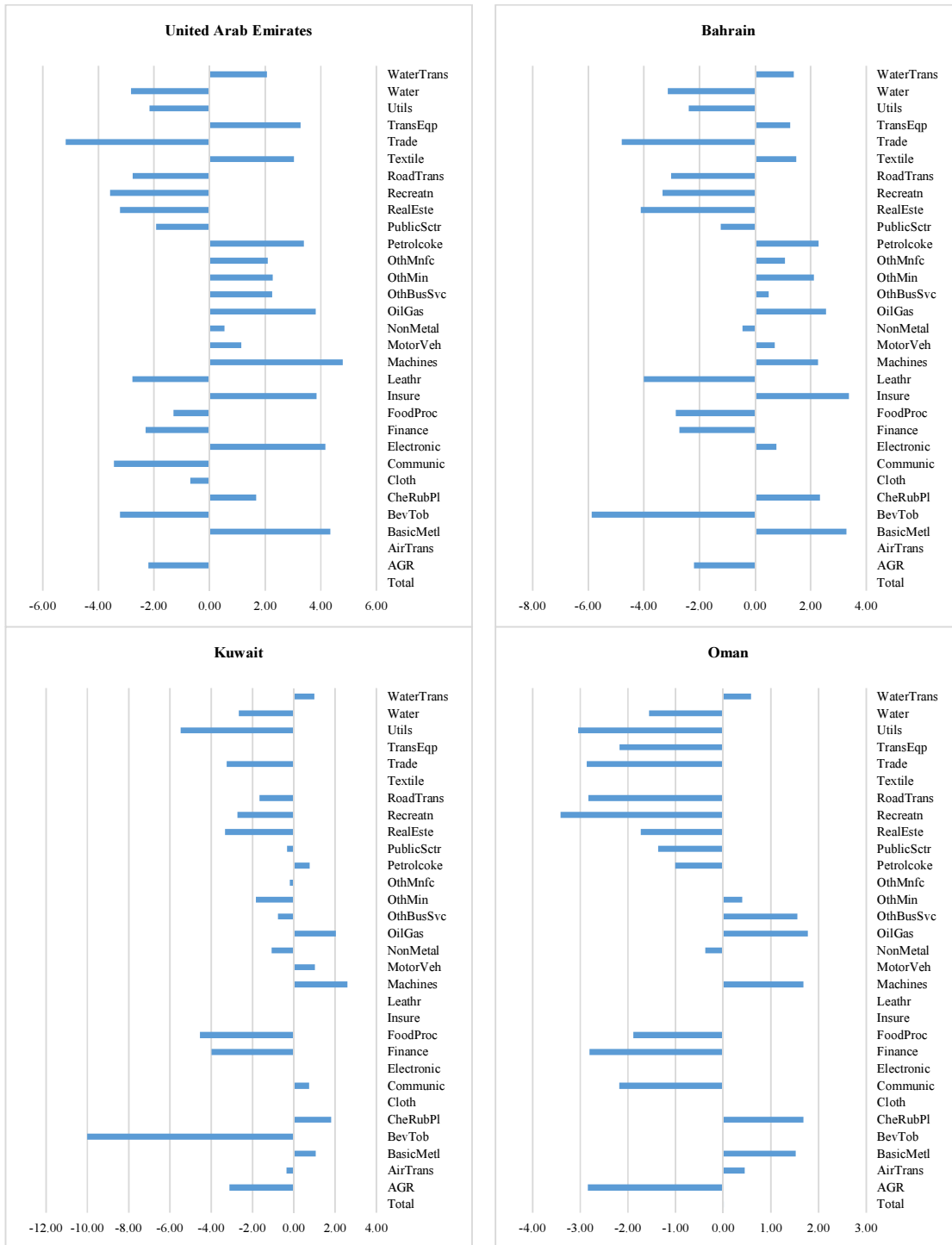
Figure 13. Cumulative variation of total exports, 2018-2021

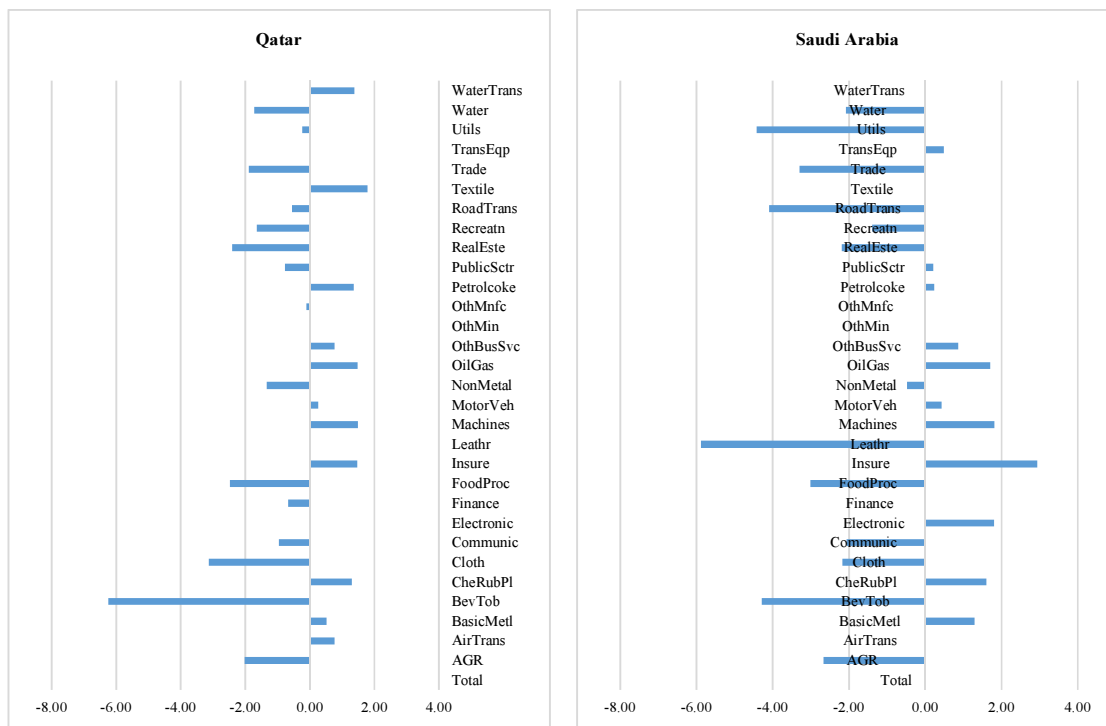


Source: ESCWA calculations using Mirage CGE model.

At the sectoral level, figure 14 shows that the introduction of VAT leads to a new reallocation of resources among sectors in all the countries. Given that the same rate will be implemented in the six GCC countries on the same date, some sectors (oil and gas, machinery and basic metallurgy) will see their production increase, while others (real-estate, road transport and finance services) will witness a shrink in their activities.

Figure 14. Cumulative variations of production by sector





Source: ESCWA calculations using Mirage CGE model.

3.2 USE OF VAT REVENUE TO INCREASE GOVERNMENT EXPENDITURE

The results completely change if the additional revenue is used to increase government expenditure. The net impact of the introduction of VAT will be positive, with a growth gain ranging from 0.08 percentage points in Qatar to 0.51 percentage points in Bahrain (table 6).

Table 6. Relative variation of GDP following the implementation of VAT

	2018	2019	2020	2021
United Arab Emirates	0.39	0.39	0.39	0.39
Bahrain	0.53	0.53	0.52	0.51
Kuwait	0.31	0.32	0.33	0.34
Oman	0.81	0.81	0.82	0.82
Qatar	0.08	0.08	0.08	0.08
Saudi Arabia	0.56	0.57	0.58	0.58
Total GCC	0.45	0.45	0.46	0.46

Source: ESCWA calculations using Mirage CGE model.

This gain is mainly driven by the Keynesian multiplier which increases local demand, especially in the first year where growth gain could reach a 0.46 basis point for the whole region (figure 15). Increases in demand could generate more inflationary pressure than in the previous simulation (figure 16). Inflation increases will range between 4 per cent and 5 per cent in the first year but will range between 1 per cent and minus 1 per cent in the final year. Additional growth will also enhance labour market conditions. Unemployment rates could drop by between 0.4 and 4, thus increasing households revenue and consumption

(figure 17). Figure 18 shows that household consumption could increase by 0.53 per cent in the whole region. Imports could increase by between 0.1 per cent and 0.8 per cent (figure 19), while exports could increase by between 0.17 per cent and 0.48 per cent (figure 20).

Figure 15. Difference in growth rate, 2018-2021

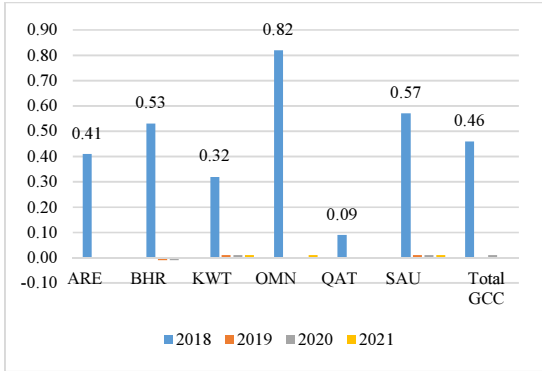


Figure 16. Difference in inflation rate, 2018-2021

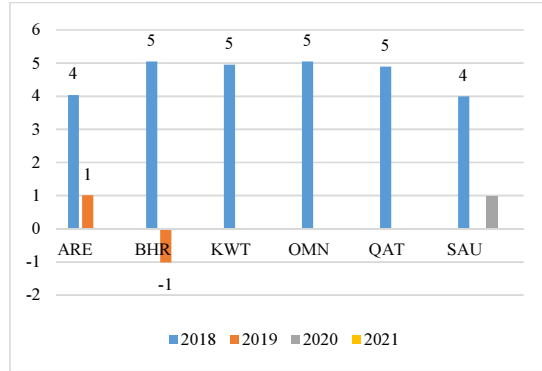


Figure 17. Difference in unemployment rate, 2018-2021

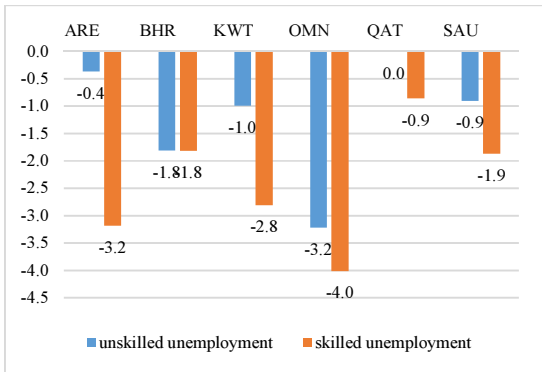


Figure 18. Cumulative variation of household consumption, 2018-2021

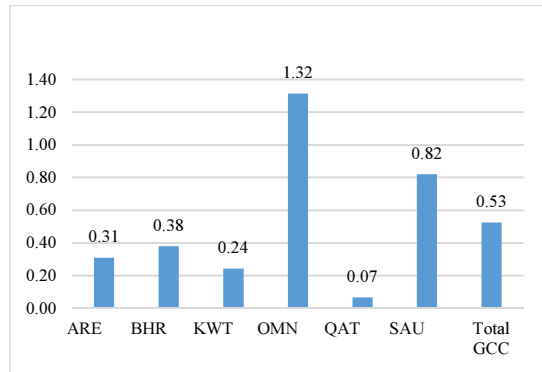


Figure 19. Cumulative variation of total imports, 2018-2021

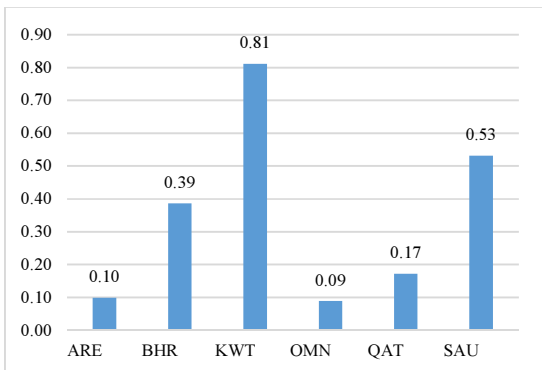
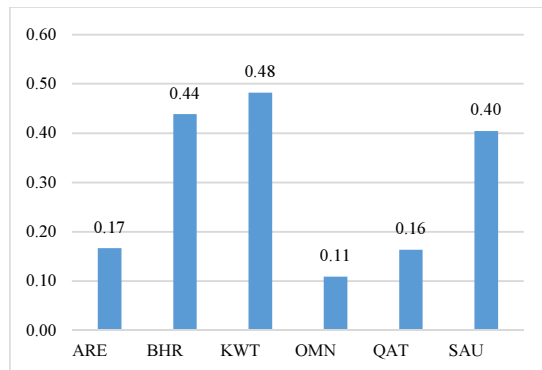


Figure 20. Cumulative variation of total exports, 2018-2021



Source: ESCWA calculations using Mirage CGE model.

On the fiscal side, the creation of additional economic activities and the increase in imports causes a fiscal multiplier that generates higher fiscal revenue when compared with the first scenario. At the global level, the revenue could represent more than 2.1 per cent of GDP, which is 0.3 per cent higher than the first scenario (table 7).

Table 7. VAT revenue as a percentage of GDP in scenario 2

	2018	2019	2020	2021
United Arab Emirates	3.41	3.41	3.41	3.42
Bahrain	2.62	2.62	2.61	2.61
Kuwait	1.70	1.74	1.77	1.81
Oman	1.93	1.94	1.94	1.94
Qatar	0.91	0.92	0.92	0.92
Saudi Arabia	1.84	1.84	1.83	1.83
Total GCC	2.13	2.14	2.14	2.15

4. CONCLUSION

The model shows that the introduction of VAT could generate considerable revenue in GCC countries - how this revenue is used will have crucial economic implications. If the revenue generated by VAT is used only to decrease the fiscal balance, the creation of this tax will reduce growth and job creation. However, if the revenue is earmarked for public expenditure, its impact on unemployment and job creation will be positive.