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War in the Middle East: Economic Spillovers and Policy Challenges[1]

The war in the Middle East that started on February 28, 2026, has inflicted profound human suffering and significantly affected the outlook for the Middle East, North Africa, Afghanistan, and Pakistan (MENAP) region. Earlier in 2026, economic activity was gaining momentum and inflation was easing in most MENAP economies. However, the closure of the Strait of Hormuz, the disruption of oil and natural gas production, and the severe impact on air traffic to and through the Gulf have all had immediate economic consequences. The war started as a regional shock but soon became a global one: the price of Brent crude has risen above $100 per barrel, and prices have spiked for natural gas, fertilizers, and metals, tightening supply chains and raising production costs across the region and globally. The ceasefire agreement announced on April 7 is a welcome development and an important step toward a de-escalation of the war. However, uncertainty remains exceptionally high and much depends on whether the ceasefire holds and global and regional stability is restored.

Even in the reference scenario that assumes that trade resumes and production normalizes by the middle of 2026, MENAP growth is expected to slow markedly to 1.4 percent in 2026, a downgrade of 2.3 percentage points relative to October 2025 projections. This aggregate number masks substantial differentiation within the region. Oil exporters around the Gulf that are directly affected by the war face steep downward revisions of up to 15 percentage points this year, with five out of eight seeing outright contractions, before experiencing a rebound in 2027. Growth for MENAP oil importers is downgraded by a more moderate 0.3 percentage points this year and the next, amid strong economic developments before the onset of the war. Inflation is expected to increase, but again quite unevenly across the region.

As the war continues and damages to energy infrastructure increase, expectations for a return to normal energy production and exports by the middle of 2026 are becoming less likely. A protracted or more intense war would weigh heavily on MENAP oil importers through a variety of channels, including the terms-of-trade shock and loss of remittances: on average, every 10 percent rise in crude oil prices trims GDP growth by about 0.5 percentage point while lifting inflation by a full percentage point. For oil exporters directly affected by the war, continued disruptions to energy production and exports would outweigh the windfall from higher energy prices and, together with lower activity in non-energy sectors such as tourism, worsen both fiscal and external balances. Further deterioration in financial market sentiment would accelerate capital flight and increase borrowing costs.

Mitigating the impact of the shock requires disciplined yet agile policy responses. Countries should resist the temptation to sustain aggregate demand through generalized fiscal easing and should refrain from reintroducing broad-based subsidies. Rather, fiscal policy should support those most affected by higher commodity prices through targeted and temporary cash transfers and mitigate the risk of medium-term scarring on economic activity. Countries with fiscal buffers should let automatic stabilizers work fully, whereas those without fiscal space should ensure that their response is consistent with debt stability, which may require reprioritizing spending and mobilizing revenues. Central banks confronting second-round effects from higher commodity prices must tighten monetary policy or maintain restrictive stances, and inflation targeters should allow exchange rates to act as shock absorbers. Financial sector supervisors will need to sharpen their

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oversight of liquidity and currency risks and stand ready to deploy liquidity support and adjust macroprudential policies as needed. Over the longer term, diversifying trade routes, strengthening critical infrastructure, and deepening regional cooperation on essential goods and energy will be essential for building lasting resilience, especially across Gulf Cooperation Council economies.

In stark contrast to the MENAP region, growth projections for the Caucasus and Central Asia region have been revised slightly upward since last October for both 2026 and 2027 (by 0.1 percent in both years), after another year of above-projected growth in 2025. The region is still expected to experience slower growth going forward, from about 6 percent in 2025 to under 5 percent in 2026 and 2027, as domestic demand weakens amid the fading effect of Russia's invasion of Ukraine and generally tighter policy stances. Lower growth should also facilitate a gradual easing of inflationary pressures. However, the spillovers from the war in the Middle East place risks firmly to the downside, as the region remains vulnerable to commodity price volatility and trade and tourism disruptions. Prudent macro policies and firmer bank supervision will be needed to ensure a soft landing toward a more sustainable pace of growth and inflation, while further efforts at diversifying the economy and developing the private sector will sustain growth over the longer term.

Another Test for the Global Economy

The outbreak of war in the Middle East in late February 2026 represents a further test of the resilience of the global economy. In 2025, the world economy managed to weather challenges stemming from trade tariffs and an exceptional increase in policy uncertainty. Robust technology-related investment, supportive financial conditions, adaptive corporate responses, and fiscal and monetary policy support helped offset these headwinds. However, the war-related spike in commodity prices, damage to energy infrastructure, and trade disruptions through the Strait of Hormuz risk overwhelming these forces, casting a shadow over the global economic outlook in both the near and longer term. The ceasefire agreement announced on April 7 is a welcome development and an important step toward a de-escalation of the war. However, uncertainty remains exceptionally high and much depends on whether the ceasefire holds and global and regional stability is restored.

Given the high uncertainty surrounding the duration and severity of the war, constructing a realistic baseline projection is exceptionally difficult. Therefore, the IMF's April 2026 *World Economic Outlook* presents a reference scenario alongside alternative, more adverse scenarios. The reference scenario assumes that war-related economic disruptions fade by the middle of 2026 and that oil prices average about $82 per barrel in 2026. Under these assumptions, global growth is projected to be only marginally affected, at 3.1 percent in 2026 and 3.3 in 2027, below the recent pace of about 3.4 percent in 2024–25 and well under the historical (2000–19) average of 3.7 percent. Global headline inflation increases to 4.4 percent in 2026 before declining to 3.7 percent in 2027.

If energy disruptions were to persist and oil prices remained much higher for longer, the impact on global activity would be more pronounced. In a more adverse scenario in which oil prices average about $110 per barrel in 2026, global growth falls to 2.6 percent, while inflation reaches 5.4 percent. An even more severe scenario—characterized by greater damage to energy infrastructure and more persistent, large-scale trade disruptions—would entail larger negative impacts (see Chapter 1 of the April 2026 *World Economic Outlook*. Global growth would drop to about 2 percent in 2026, while headline inflation would rise to just above 6 percent by 2027. The impact on emerging market and developing economies would be almost twice that on advanced economies.

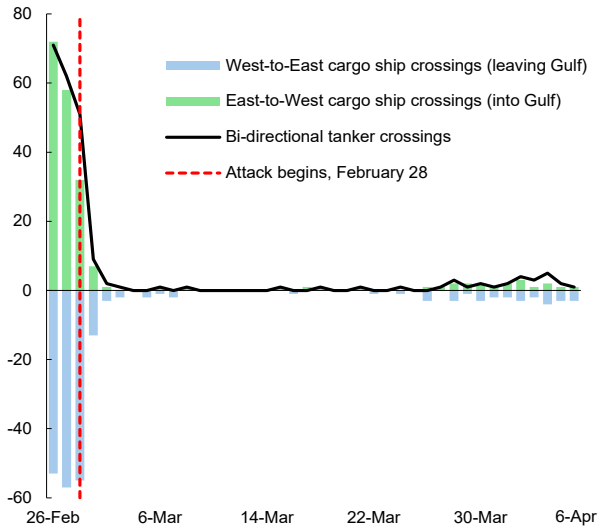
Middle East Rocked by Another Massive Shock

Many economies in the Middle East, North Africa, Afghanistan, and Pakistan (MENAP) region closed 2025 with strong performances. Economic growth remained solid through the second half of the year, underpinned by strong nonhydrocarbon activity in parts of the Gulf Cooperation Council (GCC) and resilient domestic demand elsewhere in the region. High-frequency indicators pointed to continued strong activity in early 2026, particularly in services, tourism, and logistics sectors. Inflation was stable or declining in most countries, reflecting easing food price pressures and tighter macroeconomic policies.

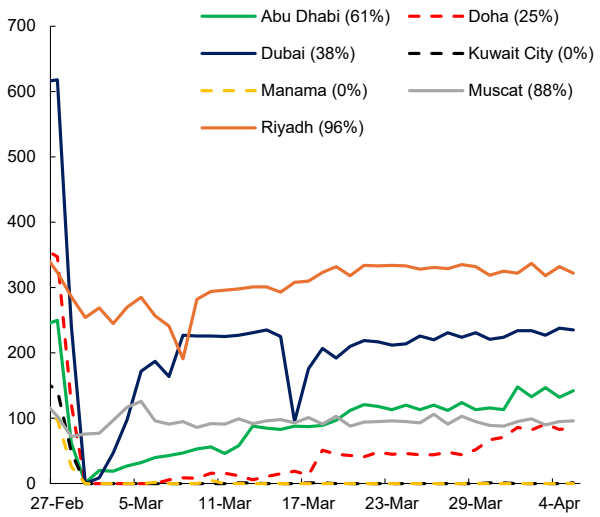
A significant share of global trade in key commodities typically transits through the Strait of Hormuz each day, including roughly one-fifth of global oil supply (about 20–21 million barrels per day), about one-quarter of global liquefied natural gas (LNG) trade, and one-third of global fertilizer and helium trade. As of early April, more than one month into the war, maritime traffic through the Strait of Hormuz remains nearly at a halt, with tanker crossings falling from roughly 70 vessels per day to near zero after the onset of hostilities (Figure 1, panel 1). Air traffic has also declined sharply at key regional hubs, with departures down by roughly one-third in Abu Dhabi, about two-thirds in Dubai, and about three-quarters in Doha, while Kuwait City and Manama experienced complete suspensions (Figure 1, panel 2). Maritime insurance premiums have surged, shipping costs have increased as routes have lengthened, and logistics activity has weakened, particularly in economies that are also more reliant on reexports, tourism, and transport services.

Figure 1. Trade, Transport, and Energy Market Disruptions in the Wake of War

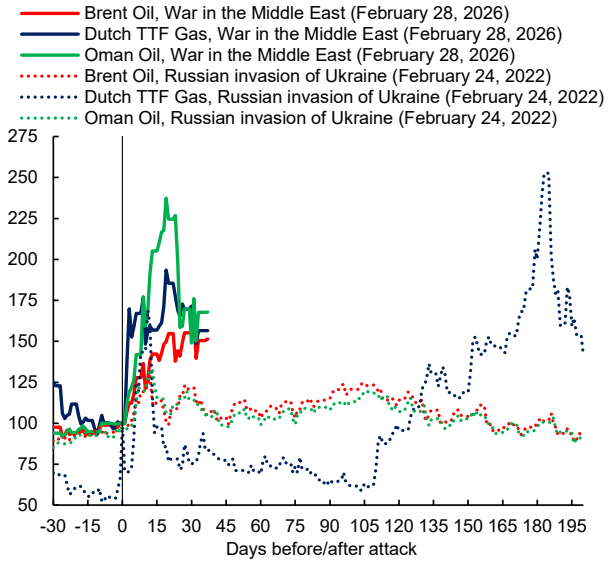
1. Daily Traffic through the Strait of Hormuz
(Number of vessels)



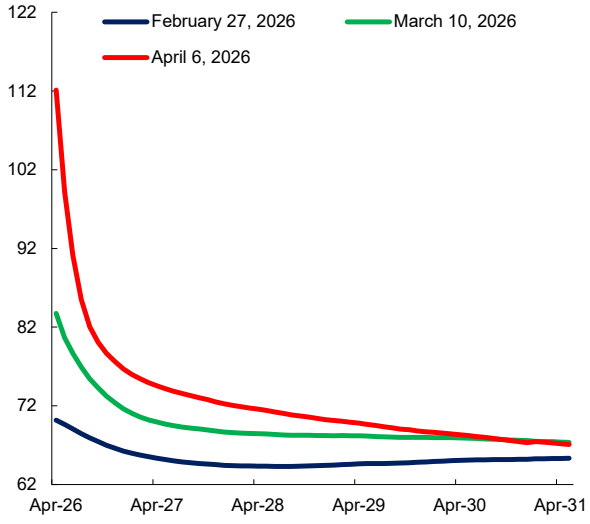
2. Operations at Key GCC International Airports
(Number of daily departures)



3. Oil and Natural Gas Prices after Recent Conflicts
(Index; February 28, 2026 = 100, February 24, 2022 = 100)



4. Oil Prices: Futures Curves
(US dollars per barrel; average of WTI, Brent, Dubai futures price)



Sources: Bloomberg Finance L.P.; Flightradar24; and IMF staff calculations.
Note: Data are as of April 6, 2026. In panel 2, percentages in the legend indicate the latest number of flights as a share of the average daily flights in the week preceding the onset of the war. GCC = Gulf Cooperation Council; WTI = West Texas Intermediate.

The war has severely curtailed energy production. Strikes and precautionary shutdowns have reduced oil and gas production and export capacity across several Gulf producers—affecting oil infrastructure in Iraq, Kuwait, and the United Arab Emirates—and disrupted LNG operations at Qatar's Ras Laffan complex. The estimated loss of capacity exceeds 10 million barrels per day of oil and about 500 million cubic meters per day of natural gas.

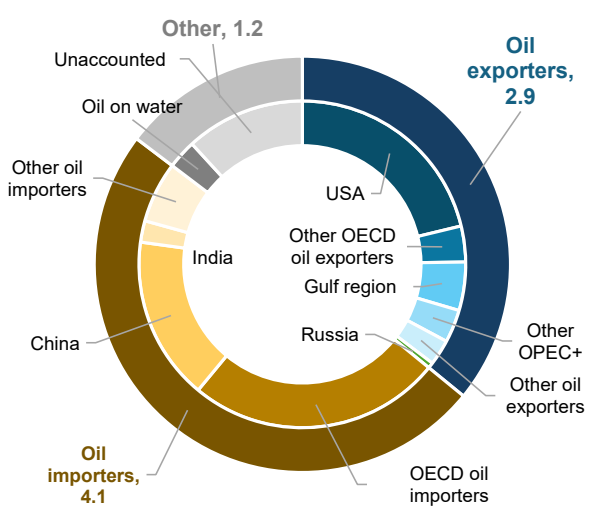
The collapse in transit and production sharply tightened global energy markets, spiking prices. After the onset of the war, the price of Brent crude rose above $100 per barrel and remains elevated, while European gas prices jumped by roughly 60 percent amid disruptions to LNG exports, which is more than what was observed immediately after Russia's invasion of Ukraine (Figure 1, panel 3). At the onset of the war, the shock also created segmentation across crude benchmarks, with Oman crude rising much more than other benchmarks, reflecting increased demand for grades not dependent on transit through the Strait of Hormuz and limited alternative export routes. Global hydrocarbon stocks provide only limited and dwindling buffers (Box 1). Oil futures curves moved upward with the start of the conflict, suggesting market expectations of prices settling at higher levels compared to pre-war expectations. However, the market initially projected a relatively rapid decline in oil prices, reflecting the belief that the conflict would be short-lived (the futures curve of March 10, shown in Figure 1, panel 4, is behind this REO reference scenario). As time went by, the curve moved progressively upward, reflecting rising concerns about persistent supply disruptions, limited spare production and transport capacity, and heightened risk premiums associated with uncertainty over transit through key shipping routes.

Box 1. Hydrocarbon Stocks: Limited Buffers against Prolonged Disruptions

Global hydrocarbon inventories entered the conflict at relatively elevated levels, providing some short-term cushion against supply disruptions. Total global oil stocks were estimated at about 8.2 billion barrels in 2025—roughly 1.3 million barrels per day, on average—the highest level since 2021. This buildup reflected softer demand growth and precautionary stock accumulation in several oil-importing economies. Approximately 25 percent of these total global stocks are "oil on water," that is, oil in transit by sea, according to the International Energy Agency.

Box Figure 1.1. Global Oil Inventories

(Billions of barrels)



Sources: IEA; JODI; and KPLER.
Note: OECD = Organisation for Economic Co-operation and Development; OPEC+ = Organization of the Petroleum Exporting Countries and other non-OPEC oil-producing countries.

The geographic distribution of inventories, however, limits their effectiveness as a buffer. Roughly two-thirds of global oil stocks are held in oil-importing economies, with exporters accounting for the remaining one-third. Among importing countries, Organization for Economic Co-operation and Development economies hold about 2 billion barrels in commercial and strategic reserves, equivalent to roughly one-quarter of global inventories. China alone is estimated to account for approximately 1.3 billion barrels—including both commercial stocks and estimated strategic reserves—although the precise size and accessibility of these inventories remain uncertain (Box Figure 1.1).

Even under a coordinated release, available inventories would only partially offset supply disruptions. Strategic and commercial stocks in importing economies could cover global supply shortfalls for roughly 40–45 days, assuming current disruption magnitudes. Moreover, logistical constraints—including transport bottlenecks, refinery compatibility, and drawdown limits on strategic reserves—would slow the pace at which inventories could be mobilized.

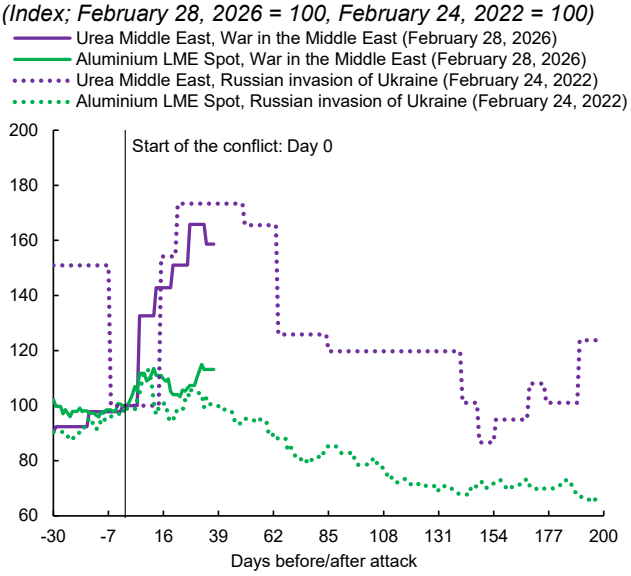
Gas markets are even less well buffered. Liquefied natural gas inventories in Europe and Asia remain below the peak levels observed after the supply shocks of 2022–23, while storage withdrawals are constrained by seasonal demand patterns and regasification capacity. The limited spare shipping capacity of liquefied natural gas further reduces the ability to redirect supplies quickly.

Overall, elevated inventories can provide a temporary cushion. If disruptions persist, continued stock drawdowns would tighten market balances, amplify price volatility, and increase competition for available supplies, particularly for crude grades and gas flows that can bypass affected transit routes.

Exports of other commodities—such as aluminum, fertilizer inputs, and refined fuels—have also been disrupted, pushing up their prices worldwide. The Gulf region is a key supplier of fertilizer inputs, aluminum, and petrochemicals. Urea prices have risen by roughly 40 percent in futures markets, while prices of diammonium phosphate and aluminum have also increased by double digits, similar to what happened in response to Russia's invasion of Ukraine (Figure 2). GCC countries account for more than 40 percent of global sulfur exports and roughly 20 percent of ammonia and nitrogen fertilizer exports. These disruptions risk tighter worldwide agricultural input markets and higher food production costs, particularly for import-dependent economies in the MENAP, South Asia, and sub-Saharan Africa regions, and could exacerbate food insecurity in vulnerable economies.

Figure 2. Urea and Aluminum Prices after Recent Conflicts

(Index; February 28, 2026 = 100, February 24, 2022 = 100)



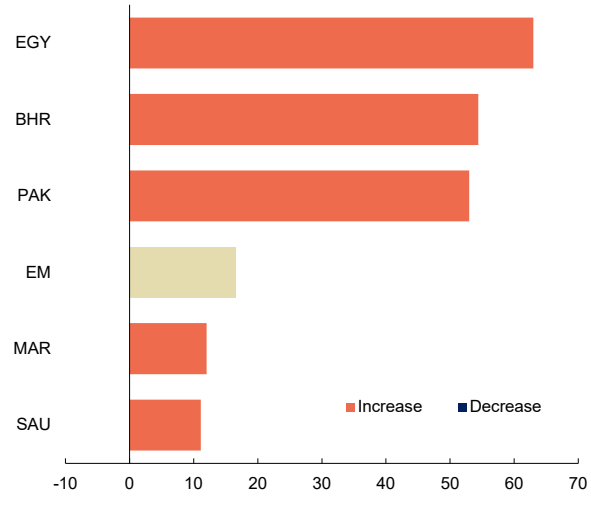
Sources: Bloomberg Finance L.P.; and IMF staff calculations.
Note: Data are as of April 6, 2026.

Financial markets reacted to the war in a typical risk-off fashion, with a moderate tightening of global financial conditions from lower global equities, higher bond yields, and a stronger US dollar. MENAP countries with preexisting vulnerabilities have been affected more. Exchange rate movements have been modest across most countries; however, Egypt allowed the exchange rate to act as the main shock absorber, with the Egyptian pound depreciating more than 13 percent as of early April. Sovereign spreads widened moderately, although by more than the average for other emerging markets, with Bahrain and Pakistan increasing by over 50 basis points and Egypt by more than 60 basis points (Figure 3, panel 1), as of early April. Portfolio outflows have occurred across several markets—including Egypt, Qatar, and the United Arab Emirates (Figure 3, panel 2)—but remain limited relative to previous episodes of global financial stress.

Figure 3. Investor Risk Sentiment and Capital Flows

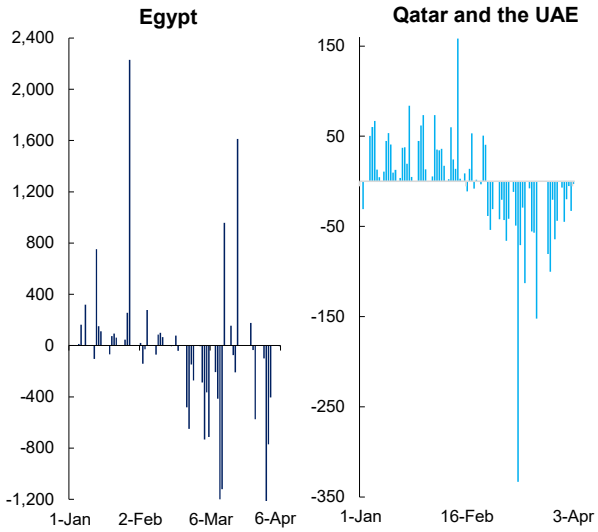
1. JP Morgan EMBIG Spreads

(Basis points; change since February 27, 2026)



2. Portfolio Flows

(Millions of US dollars)



Sources: Bloomberg Finance L.P.; Haver Analytics; and IMF staff calculations.
Note: Data are as of April 6, 2026. In panel 2, data for Qatar and the United Arab Emirates are only for equity flows. Data labels in the figure use International Organization for Standardization (ISO) country codes.

An Outlook Clouded by War

Overall, the impact of the war on MENAP economies depends critically on the duration and intensity of the war. Given the high uncertainty surrounding the war and in line with the April 2026 *World Economic Outlook*, this update reports a reference scenario—in lieu of the traditional baseline set of economic projections—and emphasizes the key channels through which downside risks can materialize. The reference scenario assumes that the trade and production disruptions related to the war fade by the middle of 2026, consistent with the view from commodity futures prices as of the middle of March, which anchor the scenario.

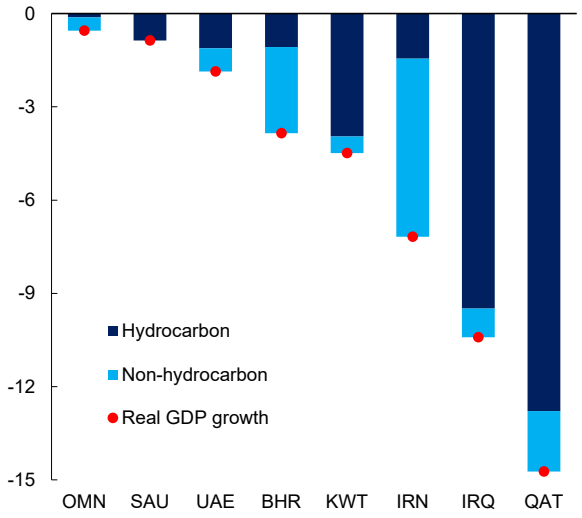
Even under the assumptions of a short-lived conflict under the reference scenario, the group of directly affected MENAP oil-exporting economies experiences a significant downward revision in real output growth in 2026 compared with the October 2025 *Regional Economic Outlook: Middle East and Central Asia*.[2] The negative impact on growth this year varies widely across countries and ranges from about 0.5 to almost 15 percentage points (in Oman and Qatar, respectively; Figure 4, panel 1). Five out of the eight economies (Bahrain, Iran, Iraq, Kuwait, and Qatar) in this group are projected to experience a contraction of GDP (Table 1). The greater economic damage they are expected to experience primarily reflects their heavy reliance on the Strait of Hormuz for the transit of traded goods, and the higher incidence of infrastructure damage from attacks. Although the damage to hydrocarbon production and exports is the primary factor, the large downward revisions also reflect lower nonhydrocarbon economic activity, as manufacturing and services (for example, tourism and logistics) are also hurt. Moreover, the adverse impacts under the reference scenario are anticipated to be long-lasting (Figure 4, panel 2). Despite some recovery of economic activity anticipated over the coming years, output levels in 2030 will remain about 2 percent below their pre-war trends for the median economy in this group.

The near-term inflationary impact of the shock is positive, relative to the October 2025 *Regional Economic Outlook: Middle East and Central Asia*, as imported goods' prices rise across the directly affected MENAP oil exporters under the reference scenario (Figure 5). However, the magnitude of the impact varies widely across countries, reflecting differences in exposure (shares of affected imported goods in the consumption basket) and domestic factors (for example, stronger-than-expected momentum in domestic prices in Iran and energy subsidy reforms in Bahrain). However, the magnitude of the impact varies widely across countries, reflecting differences in exposure (shares of

Figure 4. Impact of War in the Middle East on Growth Prospects

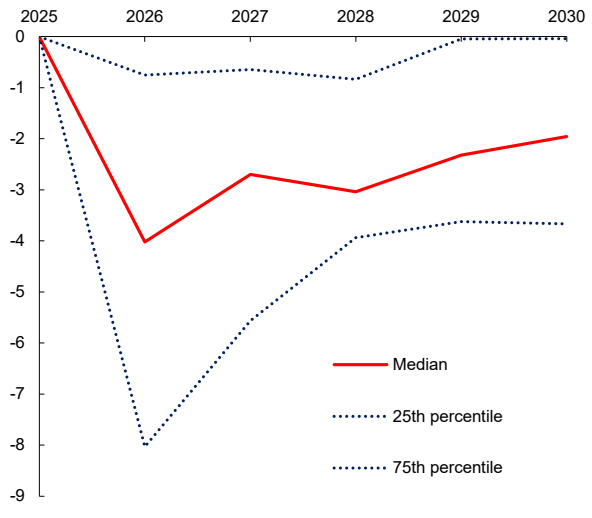
1. 2026 Growth Forecast Revisions

(Percentage point change compared to October 2025 forecast, by contribution to overall growth)



2. Projected Conflict-Related Real GDP Losses of Directly Affected Economies

(April 2026 forecast in percent of October 2025 forecast)



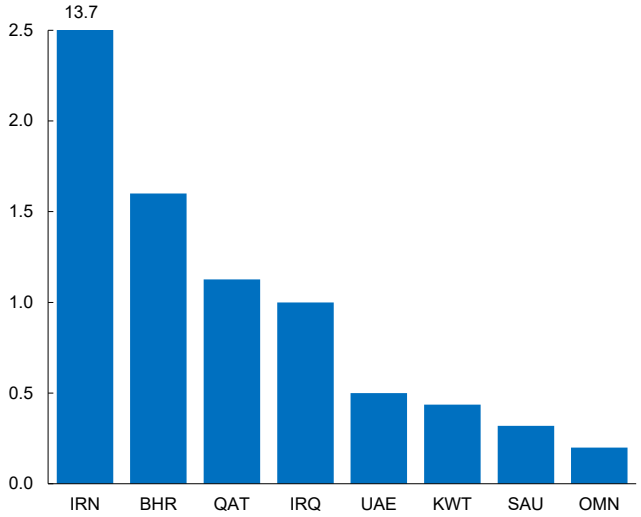
Sources: IMF, World Economic Outlook database; and IMF staff calculations.
Note: Data labels in the figure use International Organization for Standardization (ISO) country codes.

[2] The group of directly affected MENAP oil exporters includes the Gulf Cooperation Council (GCC) countries of Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates, as well as the Gulf-bordering countries of Iraq and Iran.

affected imported goods in the consumption basket) and domestic factors (for example, stronger-than-expected momentum in domestic prices in Iran and energy subsidy reforms in Bahrain). The shock contributes to an upward revision of inflation of over 13 percentage points in Iran, but about 0.2 percentage point in Oman. For the other economies of the GCC and Iraq, upward inflation revisions range from about 0.5 percentage point in Saudi Arabia to about 1.5 percentage points in Bahrain, primarily because of higher trading costs.

Figure 5. 2026 Inflation Forecast Revisions

(Percentage points, change between October 2025 and April 2026 forecasts)



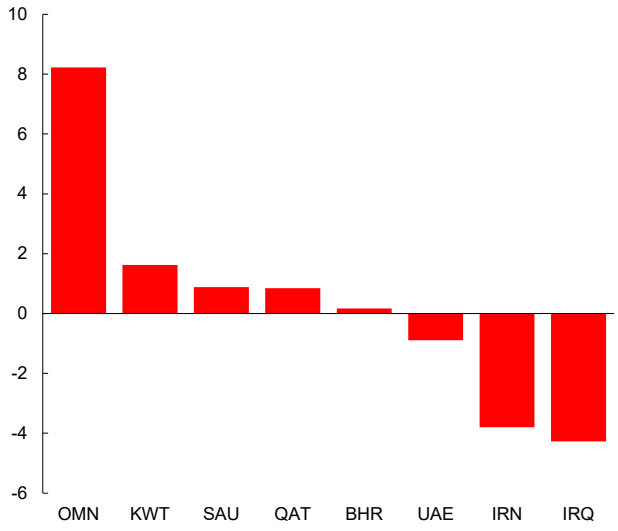
Sources: IMF, World Economic Outlook database; and IMF staff calculations.
Note: Data labels in the figure use International Organization for Standardization (ISO) country codes.

Similarly, relative to the October 2025 *Regional Economic Outlook: Middle East and Central Asia*, the impacts on the current accounts and primary fiscal balances across directly affected MENAP oil exporters vary markedly, depending on whether the export and production quantity effects of the war dominate the rise in oil prices or vice versa, as well as how other exports and import demand are affected (Figures 6, panels 1 and 2). For example, in the case of Oman where trade and production disruptions have been minimal because of its sea access lying completely outside the Strait of Hormuz, the increase in oil prices is expected to boost both the current account and primary fiscal balance by several percentage points compared to pre-war levels. By contrast, for the economies of Iran and Iraq, the trade and production disruptions from hostilities and the closure of the Strait of Hormuz more than offset the oil price rises, contributing to downward revisions in both their current accounts and fiscal balances. As highlighted earlier, exports of other goods—aluminum, fertilizer inputs, and other refined oil products—are also being affected. Weaker growth in some economies also entails import compression, offsetting some of the inflationary pressures.

Figure 6. Revisions to External and Fiscal Balances for 2026

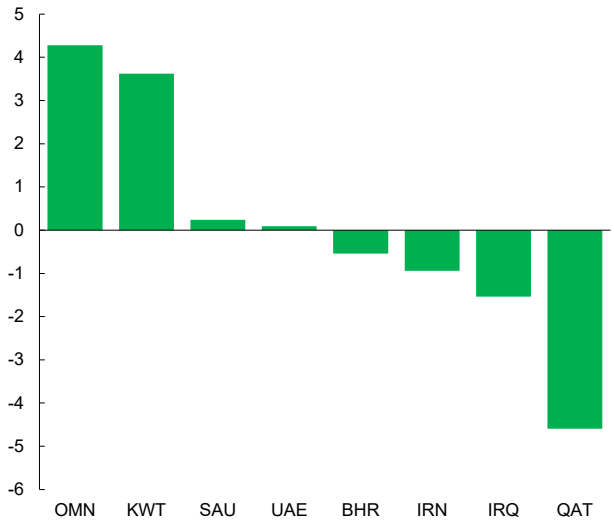
1. Current Account Balance Forecast Revisions

(Percentage point change versus October 2025 forecast)



2. Primary Fiscal Balance Forecast Revisions

(Percentage point change versus October 2025 forecast)



Sources: IMF, World Economic Outlook database; and IMF staff calculations.
Note: Data labels in the figure use International Organization for Standardization (ISO) country codes.

Unlike the directly affected oil exporters, MENAP oil exporters outside the conflict zone benefit from higher hydrocarbon prices, which strengthen export receipts, fiscal revenues, and external balances. In Libya, where oil accounts for most exports and government revenue, growth in 2026 is revised up by 2.5 percentage points (Table 1). Algeria also benefits from improved hydrocarbon revenues, with growth revised up by nearly 1 percentage point. However, these upside effects are highly uncertain. In Libya, the outlook remains dependent on oil production stability and is vulnerable to domestic political and security developments that have historically led to disruptions in output and exports. In Algeria, continued reliance on hydrocarbons amid ongoing fiscal pressures limits the durability of gains and leaves the outlook sensitive to oil price volatility.

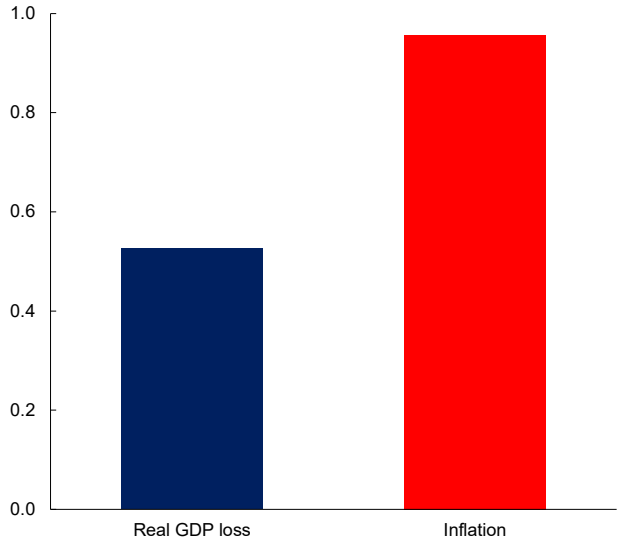
At the same time, GDP growth in MENAP oil importers has been downgraded more moderately. Compared to October, aggregate growth for this group of countries was revised downward by a mere 0.3 percent in both 2026 and 2027, amid positive economic developments in late 2025 and early 2026. Compared to projections made immediately before the war, growth was revised down by almost a full percentage point cumulatively across 2026 and 2027 (1.1, 0.6, and 0.8 percentage points in Egypt, Pakistan, and Tunisia, respectively), reflecting the impact of the commodity supply shock. Compared to October, the growth downgrade was more pronounced for low-income MENAP countries, but this mainly reflects the downward revision in Sudan, unrelated to the war in the Middle East and instead caused by the worsening economic situation amid an internal conflict that shows no sign of abating. Compared to projections made immediately before the war, GDP growth for this group of countries is revised down by almost 1 percent cumulatively across 2026 and 2027.

Risks and Channels of Contagion Stemming from the War

The downside risks to the economies of the region rise materially the longer that the war continues. A longer or more severe war exacerbates the adverse effects and their persistence, particularly for more exposed economies with limited policy space or high external vulnerabilities:

- **Oil prices could see further increases and volatility or remain elevated for longer in the event of a more extended or intense war.** Longer trade disruptions or greater damage to oil production capacity raises the possibility of higher and more sustained oil prices and a larger risk premium than is currently embedded in oil futures prices:
    - For the average MENAP emerging market and developing economy oil importer, IMF estimates suggest that a 10 percent rise in the average annual oil price leads to output losses of about 0.5 percentage point, and inflation increases of about 1 percentage point (Figure 7). The terms-of-trade shock would also contribute to a deterioration in current account balances, from over 1 percentage point (West Bank and Gaza) to about 0.3 percentage point (Pakistan), and in fiscal balances, from about 0.5 percentage point (Egypt, Jordan, and Tunisia) to 0.1 percentage point (Pakistan). For Lebanon, the ongoing war poses acute risks by intensifying pressures on trade, foreign reserves, and humanitarian conditions, for example, stemming from internally displaced people, while further heightening uncertainty.

Figure 7. GDP and Inflation Impacts on MENAP Oil Importers of a 10 Percent Oil Price Rise
(Percentage points, current year)



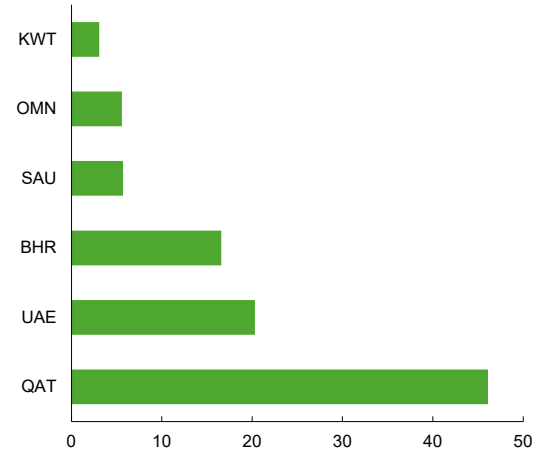
Source: IMF staff calculations.

    - For the GCC economies and other oil exporters, external and fiscal balances may improve or worsen in response to a more protracted or severe war, depending on the relative magnitudes of the increase in prices versus the decline in volumes (all else equal). For example, among the GCC economies, Kuwait is assessed to be more sensitive to such swings, reflecting its heavier reliance on oil-related export earnings: a 10 percent rise in the oil price

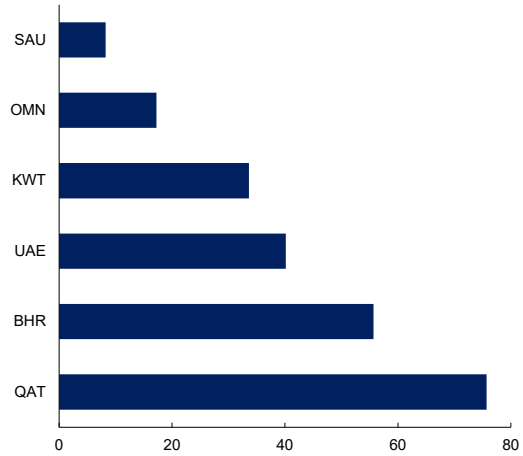
improves the current account balance by about 4 percentage points, while a 10 percent decline in export volumes lowers it by nearly 3 percentage points. By contrast, Saudi Arabia is assessed to be less sensitive: a 10 percent increase in oil prices or a 10 percent decline in export volumes has roughly symmetric—but opposite-signed—effects on the current account, of slightly more than 1 percentage point.

Figure 8. Exposure and Vulnerabilities of MENAP Economies to War-Related Downside Risks

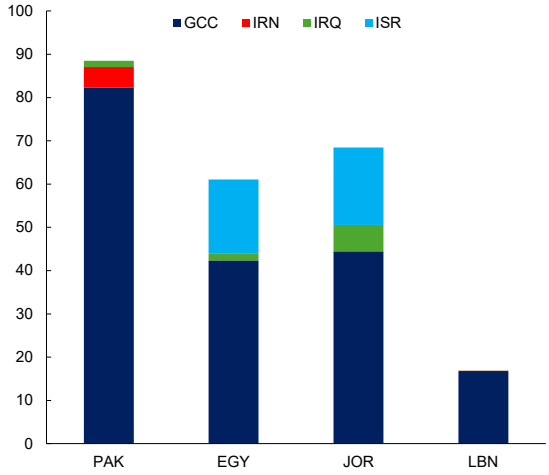
1. Pre-War Annual Tourism Expenditure
(Percent of domestic household expenditure, average of 2021–24)



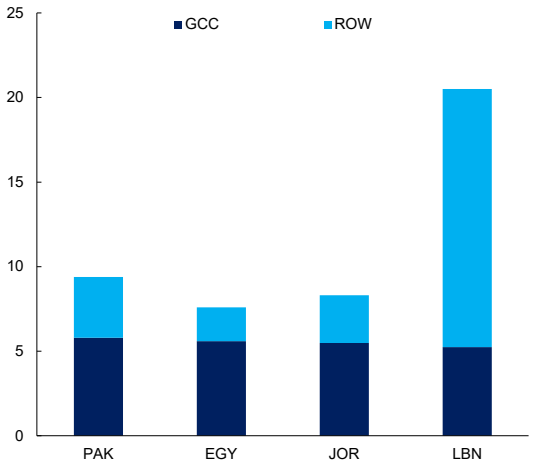
2. Share of Desalinated Water in Water Supply
(Percent, 2022)



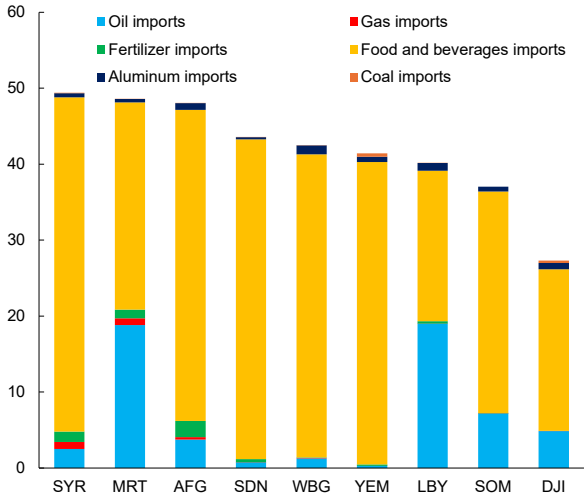
3. Select MENAP Oil Importers: Imports of Oil and Gas from Countries Affected by the War
(Percent of total oil and gas imports, 2024)



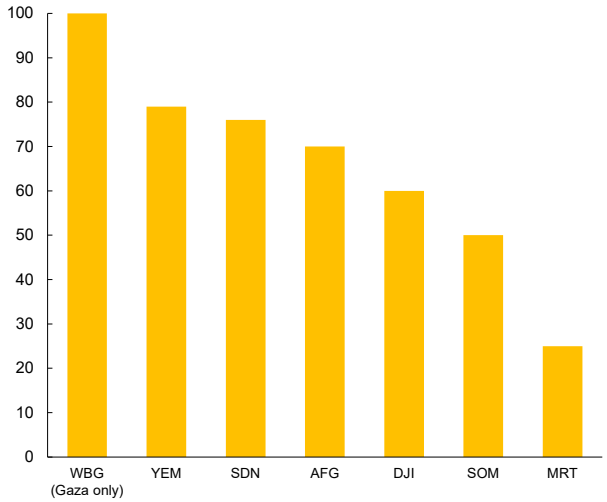
4. Select MENAP Oil Importers: Remittances
(Percent of GDP, 2024)



5. Select MENAP LICs and FCS: Imports of Key Commodities
(Percent of total goods imports, 2024)



6. Select MENAP LICs and FCS: Population under Food Insecurity
(Percent of total population, 2025)



Sources: CEPII, BACI database; FAO Aquastat; Haver Analytics; IMF, World Economic Outlook database; The KNOMAD/World Bank Bilateral Remittance Matrix; World Bank, Global Food and Nutrition Security Dashboard; and IMF staff calculations.
Note: In panel 1, averages are calculated over the available data for 2021–24. In panel 3, data for Jordan is from 2023. In panel 4, countrywide shares of inward remittances are based on the 2021 KNOMAD/World Bank Bilateral Remittance Matrix, while total remittance values for each country in 2024 are taken from the World Bank. In panel 5, Djibouti's fertilizer imports are excluded because they capture regional transit to Ethiopia. Yemen's imports reflect data for the overall territory of Yemen and exclude hydrocarbon imports because of data limitations. In panel 6, the latest available data are shown. Food insecurity is defined as IPC Phases 2–5 under the Integrated Food Security Phase Classification. Data labels in the figure use International Organization for Standardization (ISO) country codes. FCS = fragile and conflict-affected state; LIC = low-income country; MENAP = Middle East, North Africa, Afghanistan, and Pakistan.

- **A prolonged and more severe conflict would hurt directly affected MENAP oil exporters well beyond the hydrocarbon sector, through mutually reinforcing transmission channels,** including the following:
    - *Tourism*. Inbound tourist spending is large in several GCC economies (Qatar, the United Arab Emirates, and Bahrain; Figure 8, panel 1). For example, in Qatar, inbound tourists spend about half of what domestic households spend. The sharp decline in regional air traffic risks spilling over to retail, transport, and business services. More broadly, damage to logistics infrastructure—ports, airports, and trade corridors—could prolong disruptions to trade and services, even if security conditions improve. At the same time, elevated uncertainty could weigh on foreign direct investment, delaying investment decisions and reducing medium-term growth prospects.
    - *Food imports*. Import shares of food consumption are above 80 percent for four of the GCC members (Bahrain, Kuwait, Qatar, and the United Arab Emirates) and above 50 percent for the remaining two (Oman and Saudi Arabia), making them more exposed to higher transport costs and supply disruptions. Large domestic food inventories estimated to last many months provide some near-term buffer, but a prolonged war could deplete these stocks, putting upward pressures on food prices.
    - *Water*. Several Gulf economies are heavily reliant on desalinated water for their water supplies—at about 40 percent of total water supply or above for Qatar, Bahrain, and the United Arab Emirates—creating an additional infrastructure vulnerability (Figure 8, panel 2).
- **Among emerging markets and developing MENAP oil importers, a few are highly dependent on Gulf economies for both energy imports and financial flows, leaving them exposed to a longer or more intense war.** Egypt, Lebanon, and Pakistan import substantial amounts of oil from the GCC—roughly between 15 and 80 percent of total oil and gas imports—while Egypt and Jordan rely on natural gas from Israel, accounting for just under 20 percent of total oil and gas imports (Figure 8, panel 3). Egypt, Jordan, Lebanon, and Pakistan are also big recipients of remittance inflows—at about 5 percent of GDP from the GCC, which have large expatriate shares of their labor forces (Figure 8, panel 4).[3] Lower trade and income flows pose greater risks the longer the war goes

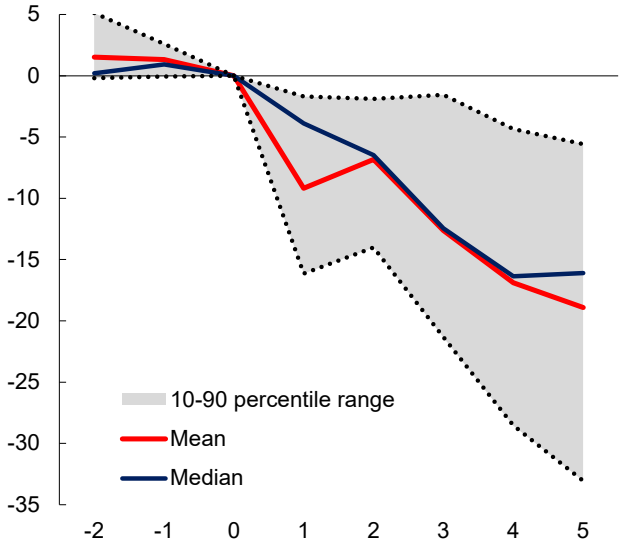
[3] It should be noted that this risk may be asymmetric, as GCC labor nationalization or fiscal adjustment could weigh on inflows even without a larger downturn.

on. These risks are amplified by preexisting macroeconomic pressures, including elevated financing needs and limited reserve buffers in many of these countries. These features raise the likelihood that even higher energy and food prices could complicate ongoing disinflation efforts. Moreover, if global sentiment deteriorates further, financing and market risks could intensify. Although financial market reactions have been contained so far, a more adverse scenario could involve a sharper tightening of global financial conditions, capital outflows, and more pronounced exchange rate pressures. This would increase refinancing risks for highly indebted sovereigns and could deepen the sovereign–bank nexus in some countries.

- **Low-income countries and other fragile and conflict-affected states in the MENAP region are especially vulnerable to higher energy, fertilizer, and food prices.** These economies tend to rely heavily on imports of the key commodities being most affected by the war, with between about 30 percent (Mauritania, Somalia) and almost 50 percent (Sudan, Syria, West Bank and Gaza, Yemen) of their goods imports consisting of food and beverages (Figure 8, panel 5). With weaker social protection systems, these shocks could worsen inflation and increase food insecurity, which is afflicting more than half the population already in some of these economies (West Bank and Gaza, Yemen, Sudan, and Afghanistan; Figure 8, panel 6). Higher import prices could also widen current account deficits and put pressure on exchange rates and reserves. In countries already facing humanitarian challenges, higher import costs and potential supply disruptions could also strain public finances, amplify social pressures, and increase risks to macroeconomic stability.

- **For the whole MENAP region, more persistent and larger economic scarring could also materialize if the war intensifies**. Evidence from past long or severe conflicts in the MENAP region suggests that they can have lasting effects on economic activity, leaving income per capita about 15 percent below its pre-conflict trend five years after the conflict's start on average (Figure 9). Moreover, severe conflicts can also scar investment, exports, and even institutional quality, leaving them markedly lower or worse than they would have been in the absence of the conflict. Severe conflicts also tend to have large negative impacts on bordering countries, with an immediate drop of about 1.5 percent in output per capita and a further drop of about 6 percent about a decade after on average (see Chapter 2 of the April 2024 *Regional Economic Outlook: Middle East and Central Asia*). In the current context, it is important to note that most GCC countries have large buffers that could be deployed to help mitigate medium-term risks. Nevertheless, the longer the war persists, the greater the likelihood that short-term disruptions translate into persistent output and employment losses.

Figure 9. Real GDP per Capita Effects after Intense and Prolonged Conflicts in MENAP Economies
(Percent difference between actual and pre-conflict forecasts)



Sources: April 2024 *Regional Economic Outlook: Middle East and Central Asia*; and IMF staff calculations.
Note: MENAP = Middle East, North Africa, Afghanistan, and Pakistan.

With Limited Policy Buffers, MENAP Policymakers Face Tougher Choices

The appropriate policy response will depend on several factors including the magnitude and persistence of the shock, country-specific vulnerabilities, and the available space across fiscal, monetary, and financial policy. However, the overall environment has become considerably more challenging. The priority for policymakers is to contain macroeconomic instability, protect the most vulnerable population, and ensure their resilience if downside risks materialize.

Fiscal Policy

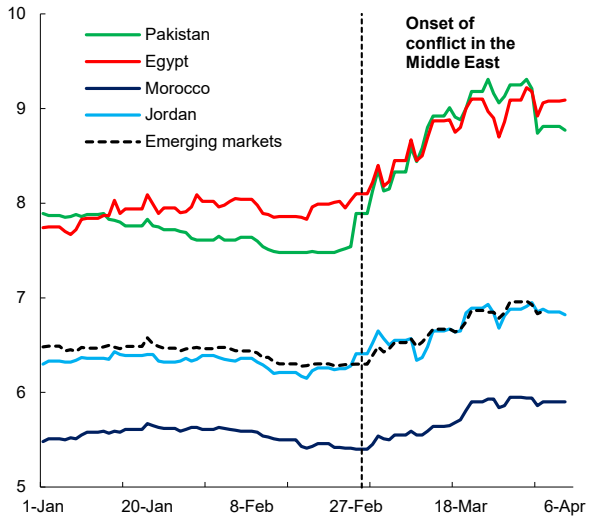
The war in the Middle East is likely to add fiscal pressures across the MENAP region through four main channels: lower revenues, larger energy subsidy bills, potential refugee-related spending, and higher borrowing costs. These pressures come at a time when fiscal space is already more constrained than before the pandemic in many economies, making policy trade-offs more difficult, especially for energy importers and low-income countries, where support from overseas development assistance has declined:

- **Higher energy prices can quickly widen fiscal costs in economies where domestic prices are partially insulated from international markets.** Energy subsidies remain large in several MENAP economies (Figure 11, panel 1). As of 2024, among directly affected countries, estimated subsidies were about 5 percent of GDP on average in the GCC, at about 5 percent in Iran, and just under 6 percent in Iraq. Subsidies are also large in Algeria and Egypt (about 10 percent of GDP), and Libya (about 16 percent). In countries where retail fuel and electricity prices are subsidized, the recent rise in oil and gas prices could therefore translate rapidly into higher budgetary costs or larger quasi-fiscal losses in state-owned utilities. This is especially relevant for net energy importers and for countries with already weak public finances.

- **Refugee inflows, should they occur, could create substantial fiscal needs for host countries near the war.** In past episodes, the adjusted fiscal cost of hosting refugees reached about 5 percent of GDP in Jordan and Lebanon. Official development assistance covered an important share of these costs, but not all (Figure 11, panel 2). If the war were to generate new large cross-border flows, frontline host countries could face immediate spending pressures on health care, education, housing, water, sanitation, and security, putting additional strain on fiscal positions.

- **Sovereign financing conditions have already tightened.** Since the start of the war, external sovereign bond yields have risen notably in several MENAP economies (Figure 10). Pakistan and Egypt saw the sharpest increases, from roughly 8 percent before the war to above 9 percent by the end of March. Jordan's yields also increased, from about 6 percent to nearly 7 percent, while Morocco's yields rose from about 5.5 to about 6 percent. These increases are meaningful, given already large financing needs and elevated debt burdens in many economies. For example, compared with 2019, gross public debt in 2026 is expected to be markedly higher in Bahrain (more than 150 percent versus less than 100 percent of GDP) (Figure 11, panel 3), and also in Egypt, Iraq, and Jordan. Interest payments have risen sharply in some cases, reaching just under 15 percent of GDP in Egypt and over 7 percent in Bahrain (Figure 11, panel 4).

Figure 10. Sovereign Bond Yields
(Percent, external composite bonds)



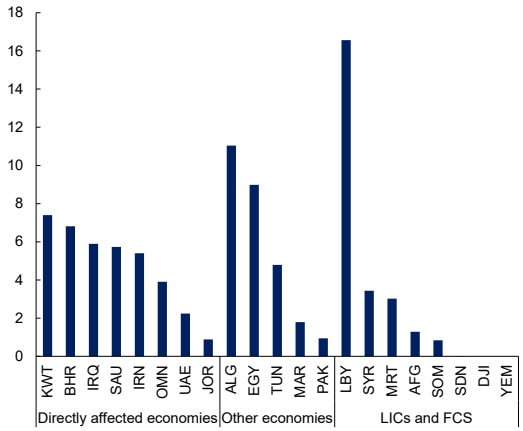
Source: Bloomberg Finance L.P.
Note: Data are as of April 6, 2026.

In this environment, fiscal policy should be carefully calibrated to the scale and persistence of the shock and aligned with available fiscal space, while taking due account of the high downside risks to the outlook (and the potential need to use additional space going forward).

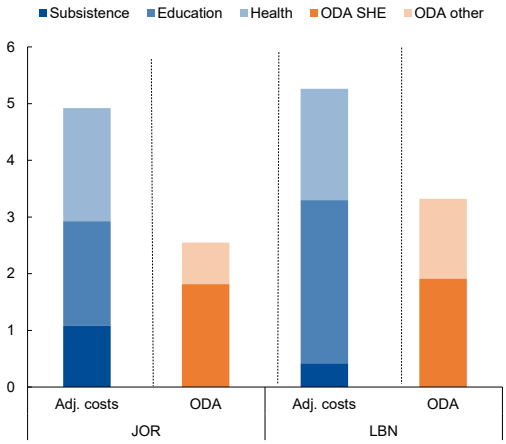
- **Countries with fiscal buffers can allow automatic stabilizers to operate and, if needed, deploy limited, well-targeted transfers to protect the most vulnerable population, while keeping the overall fiscal stance consistent with stable debt levels.** Where conflict-related damage occurs, buffers may also be used to support critical reconstruction and maintain essential services. However, such measures should remain time-bound, transparently costed, and anchored in credible medium-term fiscal frameworks to ensure that buffers are rebuilt once conditions normalize. Oil exporters not directly affected by the war should use fiscal windfalls to build buffers given the high global uncertainty and risks going forward.

Figure 11. Fiscal Pressures and Vulnerabilities in MENAP

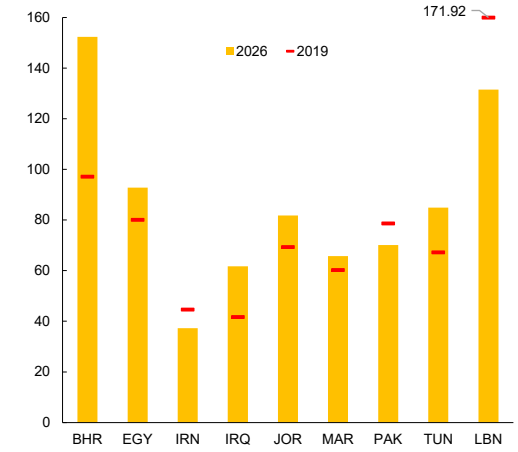
1. MENAP: Explicit Energy Subsidies
(Percent of GDP, 2024)



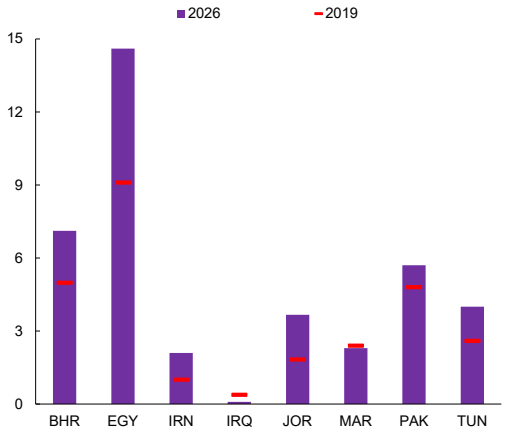
2. Potential Recurrent Cost of Hosting Refugees and Donor Support in Past Crises
(Percent of GDP, average of 2010–21)



3. Gross Public Debt
(Percent of GDP)



4. Interest Payments
(Percent of GDP)



Sources: Bloomberg Finance L.P.; IMF Fossil Fuel Subsidies Data 2025 Update, OECD, UNHCR, UNRWA, World Bank, and World Health Organization; IMF, World Economic Outlook database; and IMF staff calculations.
Note: In panel 1, energy subsidies refer to explicit subsidies, that is, undercharging for supply costs. They reflect both direct fiscal costs (in the budget) and indirect losses/reduced profits of energy state-owned enterprises. Fuel products include petroleum, natural gas, coal and electricity. The value for Iran reflects a desk estimate for 2023. In panel 2, refugees include those under the mandate of UNRWA. ODA SHE includes the ODA for refugee situations more directly related to spending subsistence needs and health and education services; ODA Other comprises the remaining ODA. Data labels in the figure use International Organization for Standardization (ISO) country codes. FCS = fragile and conflict-affected state; LIC = low-income country; MENAP = Middle East, North Africa, Afghanistan, and Pakistan; ODA = official development assistance; OECD = Organization for Economic Co-operation and Development; UNHCR = United Nations High Commissioner for Refugees; UNRWA = United Nations Relief and Works Agency for Palestine Refugees in the Near East.

- **Countries with limited fiscal space should adopt a more cautious approach.** Support, if needed, should be narrowly targeted, temporary, and preferably budget-neutral, financed through expenditure reprioritization, improved revenue mobilization, or reductions in poorly targeted subsidies. Deficit-financed, broad-based measures should be avoided, as they risk undermining debt sustainability and complicating monetary policy efforts to contain inflation. In addition, a tighter fiscal stance may be required to contain macroeconomic imbalances. For oil-importing economies in particular, policy responses should focus on targeted assistance rather than generalized price support. Oil-exporting economies benefiting from higher energy prices should avoid procyclical spending, but instead, they should save windfalls, rebuild fiscal buffers, and strengthen resilience against future shocks.

- **Across all scenarios, generalized price controls or untargeted energy subsidies should be avoided because they distort incentives, are costly, and become politically difficult to unwind.** Instead, assistance should concentrate on those least able to bear higher prices and on otherwise-viable firms facing temporary liquidity pressures. The policy menu evolves with the intensity of the shock (Figure 12). Oil importers with limited fiscal space should make efforts to limit the increase in energy subsidies, both through allowing meaningful energy price adjustments and through committing to maintaining these adjusted prices for a while after the shock has subsided. Countries with automatic price adjustment mechanisms should assess whether the mechanism in place allows a pass-through (in terms of size and speed) that is commensurate with the available fiscal space. If need be, these countries can consider a one-time price adjustment on top of what is suggested by the mechanisms to preserve fiscal space.

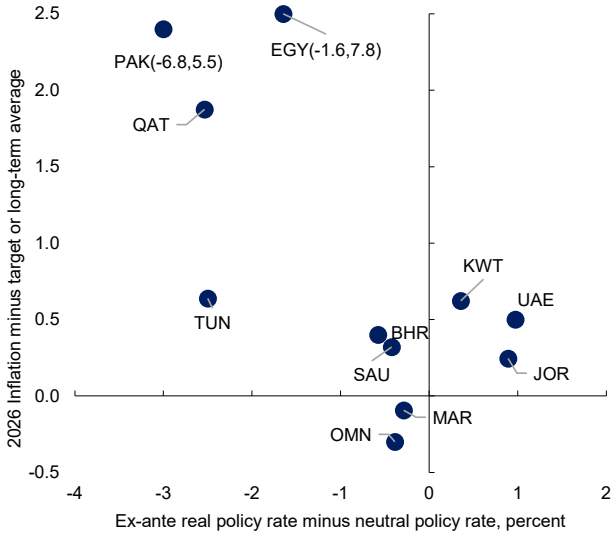
Figure 12. Pecking Order of Fiscal Support Measures

Shock Severity	For Households	For Firms
	Expand existing program focused on vulnerable	
	- One-off cash transfers to affected middle class - Targeted, temporary reductions in regulated tariffs of basic goods	Compensate affected firms for regulated tariffs
	Smooth energy bills or temporary bill discounts	Temporary government-guaranteed loans for viable firms
	If food security at risk, price subsidies (price caps or reduced taxes) with sunset clauses	Temporary credit lines; deferrals of tax and social security payments

Sources: Amaglobeli, David, Emine Hanedar, Gee Hee Hong, and Celine Thevenot (2022). "Fiscal Policy for Mitigating the Social Impact of High Energy and Food Prices." IMF Notes 2022/001; and Jeasakul, Phakawa (2020). "Considerations for Designing Temporary Liquidity Support to Businesses." IMF Special Series on COVID19, Monetary and Capital Markets.

Figure 13. Inflation and Monetary Policy Stance

(percentage points deviation)



Sources: Haver Analytics; IMF, World Economic Outlook database; and IMF staff calculations.
Note: The latest ex ante real policy rate by country is equal to the difference between the latest nominal policy rate and the end-of-period inflation projection for 2026. For countries pegged to the US$, a 2 percent inflation target is assumed, and for countries without an explicit inflation target, a 10-year average of inflation outturns is assumed. Neutral policy rates are estimated by the IMF as in Chapter 2 of the April 2023 *Regional Economic Outlook: Middle East and Central Asia.*

Monetary Policy

Inflationary pressures stemming from higher energy and food prices may warrant a prompt monetary policy response, which would need to be consistent with the fiscal policy response. However, the appropriate speed and magnitude of action will depend on country-specific monetary policy frameworks and starting conditions—most importantly, the level and persistence of inflation (which,

for example, is expected to reach almost 8 percent in Egypt and 5.5 percent in Pakistan in 2026; Figure 13). Clear communication remains essential to prevent market overreaction to new data and to keep inflation expectations anchored, especially for central banks with imperfect credibility.

- **Whether central banks should look through the supply shock will vary across countries, depending on inflation dynamics and the stance of monetary policy.** In economies where inflation is already high and the monetary policy stance remains accommodative, room for a wait-and-see approach is limited. An immediate tightening—or at least maintaining a restrictive stance for longer—could be needed to contain second-round effects and keep inflation expectations anchored. By contrast, countries that entered the shock with inflation close to target and policy rates already firmly above neutral may be able to look through part of the supply shock, provided that expectations remain well anchored and exchange rate pressures are limited. Countries that are well positioned, with inflation near target and rates above neutral, should regularly reassess their policy stance to ensure it is consistent with anticipated developments.
- **Countries with flexible exchange rates should allow the currency to act as a shock absorber, thereby facilitating relative price adjustment and reducing the need for large reserve losses.** For example, Egypt allowed the exchange rate to act as a shock absorber, with the currency depreciating by about 13–15 percent since February 18. However, depreciation risks should be closely monitored, especially where exchange rate pass-through to inflation is high or expectations are fragile. In such cases, a tighter policy stance may be warranted to prevent a de-anchoring of inflation expectations. Excessive or disorderly foreign exchange movements could amplify the impact of higher commodity prices on inflation and financial stability. The IMF's *Integrated Policy Framework* provides useful guidance for tailoring policy responses in instances where these risks are imminent.
- **For countries operating fixed or tightly managed exchange rate regimes, policy should remain aligned with the requirements of the peg.** Interest rates will typically need to move in line with anchor currencies to preserve credibility, while maintaining adequate foreign exchange reserves to withstand potential capital outflows. Policy rates may need to rise relative to the anchor currency if country risk premiums rise. If external pressures intensify, temporary liquidity-management measures—such as open market operations or higher reserve requirements—can help preserve orderly market conditions without undermining the exchange rate regime.

Financial Sector Policies

Financial sector policies should be recalibrated to the strength of capital buffers and the stability of external funding across banking systems. In MENAP, vulnerabilities vary widely—from well-capitalized, deposit-funded banking systems in several GCC countries to systems in some oil-importing and fragile economies that face higher sovereign exposure, tighter liquidity conditions, or reliance on external inflows. Heightened vigilance is particularly warranted in economies with elevated public debt and large bank holdings of domestic sovereign securities (for example, Egypt, Jordan, Pakistan, and Tunisia), where rising borrowing costs could quickly translate into pressures on bank balance sheets:

- **Supervisors should strengthen monitoring and risk assessment.** This includes intensifying scrutiny of foreign currency liquidity positions and short-term external funding gaps, closely monitoring rollover risks and foreign exchange mismatches, and assessing concentrated credit exposures to sectors most affected by the shock. These risks may rise quickly in environments of higher borrowing costs, exchange rate pressures, and weaker growth. In MENAP oil importers, higher energy import bills and exchange rate pressures could strain borrowers and increase credit risk, particularly in sectors such as tourism, trade, and transport (in, for example, Morocco, Jordan, and Tunisia). In fragile and conflict-affected economies, delayed payments and weaker economic activity could further weigh on asset quality. Early identification of vulnerabilities is essential to prevent localized strains from spreading across the financial system.
- **Preserving liquidity and ensuring crisis preparedness should also be priorities**. Authorities should closely track funding pressures, particularly in foreign currency, and stand ready to contain emerging liquidity strains. This is particularly important in economies with sizable external financing needs or limited reserve buffers (such as Egypt and Pakistan), where capital flow volatility could tighten domestic liquidity conditions. Central banks should ensure that solvent institutions have ready access to liquidity facilities, which can help

stabilize markets and prevent temporary pressures from becoming systemic. Clear operational frameworks and communication can strengthen confidence and reduce the likelihood of disorderly adjustments.

- **Policies should limit the buildup of balance sheet risks and avoid tightening the sovereign–bank nexus.** Supervisors should discourage excessive bank exposure to sovereign debt, especially in contexts of rising government financing needs, as this could amplify vulnerabilities in both the financial sector and public finances. This risk is particularly relevant in several MENAP oil importers, where banks already hold large shares of domestic public debt and may face increased demand for government financing. In environments with large government financing needs and elevated sovereign yields, banks may further shift portfolios toward government securities, crowding out private credit and weighing on nonhydrocarbon activity, warranting close monitoring.

Structural Policies

The rupture of regional supply chains has exposed how heavily many MENAP economies still rely on narrow sets of suppliers, transit routes, and critical infrastructure. Therefore, the immediate priority is to embed resilience at the heart of trade and diversification strategies. Over the medium term, policies should aim to mitigate scarring, including by implementing measures to promote private sector development, attract foreign direct investment, strengthen governance and institutions, and support productivity growth.

For oil-importing countries, particularly low-income and fragile states, this means building diversified energy systems, including clean energy. Establishing multiple fuel-import corridors, investing in LNG storage facilities, and joining cross-border electricity-trade arrangements can all reduce the macrofinancial damage from future disruptions. Parallel efforts to expand strategic fuel and grain reserves, diversify food-import origins, and upgrade storage and distribution networks will help insulate households and firms from sudden shortages or price spikes. In addition, low-income and fragile states such as Sudan and Yemen would need to secure additional official development assistance and leverage humanitarian aid, as the implementation of reforms needed to strengthen long-term resilience would require investments that exceed the fiscal and financial capacity of many of these countries.

GCC exporters face a distinct set of challenges. Their diversification agendas must focus on building more resilient economies by strengthening regional infrastructure and better integrating transport, energy, and critical supply-chain infrastructure. This entails reducing dependence on vulnerable transport and critical-infrastructure nodes by developing extra storage capacity, alternative ports, pipelines, and overland corridors; accelerating regional logistics coordination for essential goods; and ensuring priority customs clearance for food, fuel, and medicines during crises. Given that GCC countries account for nearly half of the world's desalination capacity, bolstering the resilience of water, power, and digital networks is essential; any disruption to these systems would reverberate across economies and societies almost immediately.

Deepening regional integration offers a further buffer against external shocks. Cross-border electricity and gas markets can pool spare capacity and enable emergency power sharing, harmonized trade standards and single-window customs systems can expedite the movement of critical supplies, and central bank swap lines or regional liquidity facilities can mitigate sudden funding squeezes.

IMF Intensifying Engagement and Ready to Step Up Support

The IMF is stepping up its engagement with MENAP economies—providing policy advice, technical assistance, and, where needed, financial support. After the onset of the war, the IMF has maintained close engagement with country authorities, providing timely policy advice. Capacity development remains a central pillar of support, with over 380 technical assistance projects delivered in fiscal year 2025, totaling $17.6 million, and delivery modalities being adapted in fiscal year 2026 to ensure continuity in the face of security and logistical constraints.

Since early 2020, the IMF has approved nearly $46 billion in financing across the region. Program engagement has deepened across several countries. In Egypt, the IMF-supported Extended Fund Facility (EFF), amounting to about $8.1 billion, continues to anchor macroeconomic stabilization, with a focus on exchange rate flexibility, fiscal consolidation, and structural reforms to support private sector–led growth. In Jordan, the four-year EFF arrangement approved in 2024 (about $1.2 billion) supports fiscal sustainability and reform efforts to strengthen resilience, and a 2025 Resilience and Sustainability Facility (RSF) focuses on addressing vulnerabilities in the energy and water

sectors. In Morocco, the Flexible Credit Line, with an access of about $4.8 billion, provides an important external buffer, complemented by an RSF arrangement of about $1.3 billion to support climate-related reforms. Mauritania continues to benefit from combined ECF/EFF and RSF support totaling about $0.5 billion, aimed at strengthening macroeconomic stability and advancing structural transformation. IMF engagement with Pakistan remains critical. The IMF-supported program under the EFF in Pakistan, amounting to about $7.2 billion, focuses on restoring macroeconomic stability, rebuilding external buffers, and advancing reforms in fiscal management, energy pricing, and governance.

Fragile and low-income states remain a priority. Somalia continues to receive support under a new Extended Credit Facility arrangement (about $0.1 billion) after debt relief under the HIPC Initiative. The IMF also maintains close engagement with Lebanon and Syria through intensive technical assistance and policy dialogue. The IMF continues supporting Sudan through technical assistance and capacity development. More broadly, given the substantial investments required by Low-Income Countries and Fragile and Conflict-affected States to achieve resilience, capacity development and policy guidance for establishing medium-term frameworks are intended to assist authorities in evaluating both the costs and sequencing of potential investment strategies.

The IMF has further strengthened its regional presence, including through a new office in Riyadh and expanded technical assistance. It stands ready to scale up support—through financing and capacity development—as needed if downside risks materialize.

The Caucasus and Central Asia: Continued Resilience

The war in the Middle East has had a limited impact on the Caucasus and Central Asia (CCA) economies so far. The region is still transitioning from above-potential GDP growth and high inflation toward a more moderate and sustainable trajectory. The elevated commodity price volatility and supply-chain disruptions associated with the war add an extra layer of uncertainty to the economic prospects of the region. As they continue to manage a soft landing from the robust economic performance over the past few years, CCA policymakers will also need to prepare for the potential impact of the war on growth, inflation, and fiscal sustainability.

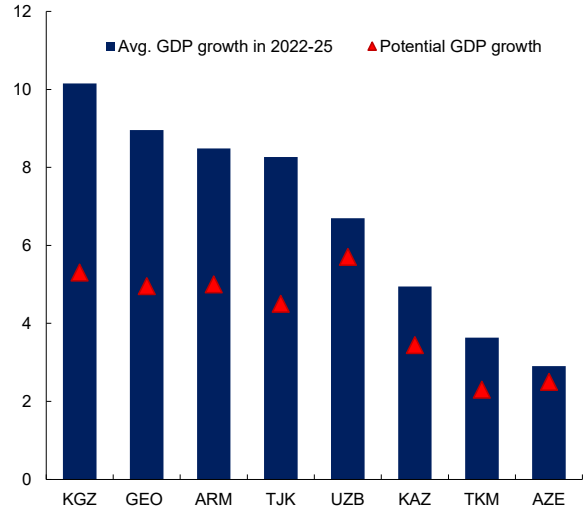
Another Year of Better-Than-Expected Growth

In 2025, the CCA region grew by 6.2 percent, about half a percent above what was projected in the October *Regional Economic Outlook: Middle East and Central Asia*. GDP growth remained above the region's estimated potential rate (Figure 14, panel 1), as continued real wage growth, sustained government spending, and buoyant remittances all boosted aggregate demand, while Kazakhstan benefited from strong activity in the extractive sector. Almost all countries in the region witnessed an upward revision in growth, with the only exception being Azerbaijan, where growth was affected by weaker-than-expected oil and gas production and investment.

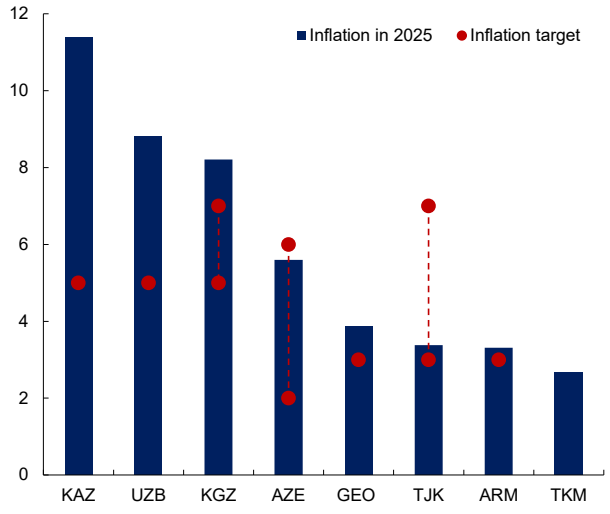
Sustained by rising food prices and domestic demand pressures, inflation increased and remained above central bank targets in several countries, leading central banks in Kazakhstan, the Kyrgyz Republic, and Uzbekistan to tighten the monetary policy stance (although the real interest rate is still negative in the Kyrgyz Republic) (Figure 14, panel 2). In a few countries, central banks eased monetary policy stances as inflation remained close to the lower bound of the target range (Tajikistan) or was still expected to converge close to the middle of the target range (Azerbaijan).

Figure 14. Macroeconomic Slack and Inflationary Pressures

1. Realized and Potential GDP Growth
(Percent)



2. 2025 Inflation versus Targets
(*Percent)*



Sources: IMF, World Economic Outlook database; and IMF staff calculations.
Note: Data labels in the figure use International Organization for Standardization (ISO) country codes.

Fiscal policy appropriately turned countercyclical in 2025 in most CCA countries, as primary fiscal balances were generally better than what was expected in October. Oil exporters narrowed their non-oil primary deficits by 1.5 percent of non-oil GDP on average, driven both by spending compression and overperformance of non-oil revenue (Azerbaijan, Kazakhstan), aided also by fast nominal growth. Among oil importers, the fiscal deficit narrowed in Armenia, Georgia, and Uzbekistan, reflecting higher revenues and some delays in capital spending (Armenia, Georgia). Fiscal deficits rose only in the Kyrgyz Republic and Tajikistan, albeit by less than expected, because of higher capital and current expenditures. Robust growth and lower-than-expected deficits caused public debt-to-GDP ratios to fall in all CCA countries.

Low oil prices and robust import growth (Kazakhstan) led to a deterioration in the external positions of CCA oil exporters in the region. By contrast, CCA oil importers experienced stronger external balances, driven by continued export growth and robust net remittance inflows (Georgia, Kyrgyz Republic, Tajikistan, Uzbekistan), and lower imports amid weaker oil prices (Georgia). Reserve coverage continued rising in the majority of CCA countries, supported by the revaluation of gold holdings amid rising gold prices and, in the case of Georgia, strong inflows.

Growth Expected to Slow

Growth is projected to slow to 4.8 percent in 2026 for the CCA region, approximately as projected in October 2025. This primarily reflects the anticipated weakening of external tailwinds, while the war in the Middle East is assumed to weigh on activity through heightened uncertainty and the terms-of-trade shock for oil importers. Among oil and gas exporters, only Turkmenistan is projected to benefit from an increase in energy production, because of its spare capacity, while Kazakhstan is expected to benefit from the indirect effects of higher prices on non-oil output. Among oil importers, a few country-specific factors are expected to offset the negative impact of the terms-of-trade shock on economic activity in 2026, including the carryover of growth surprises in late 2025 in Georgia and public expenditure increases in the Kyrgyz Republic.

Higher commodity prices from the war in the Middle East are expected to slow the fall in inflation in 2026, but not to reverse it. End-year headline inflation is projected to decrease from 8.5 percent in 2025 to 8.1 percent in 2026 on average for the CCA region (0.3 percentage point less than what was expected in October). However, the average projection masks significant heterogeneity across the region, with half of the CCA economies showing higher inflation next year. This reflects disparities in projected policy stances (with tighter monetary and fiscal policy stances expected to drive inflation down in Kazakhstan), regulatory environments (with price regulations expected to contain the impact of higher commodity prices in Azerbaijan and Turkmenistan), and import arrangements (with long-term, fixed-price natural gas contracts providing a partial buffer against energy price shocks, for example, in Armenia).

Fiscal positions are expected to diverge between oil importers and oil exporters in 2026. In hydrocarbon-exporting countries, higher oil and gas prices are expected to drive an improvement in the overall fiscal balances, but non-oil fiscal deficits are also expected to shrink, reflecting continued spending restraint despite the windfall gains. By contrast, primary fiscal balances are projected to deteriorate in all oil importers, except in Uzbekistan, where robust growth and elevated gold prices will support revenue growth. In other countries, expenditure pressures are expected to outweigh revenue gains, with capital spending set to rebound in Georgia as procurement backlogs clear, and procyclical expenditure increases in Kyrgyz Republic. A slower but still robust growth momentum is expected to counterbalance the effect of higher financing needs on public debt, with the CCA-wide public debt-to-GDP ratio projected to fall to 23.4 percent in 2026, about 3 percentage points lower than what was anticipated in October.

Current account balances in CCA oil and gold exporters are forecast to benefit from the commodity price increases amid the war in the Middle East, while higher energy prices will put pressure on current account deficits in oil importers. In the medium term, current accounts in the CCA region will be driven by more moderate trade and remittance flows, tighter fiscal policies, and, for oil exporters, increasingly binding hydrocarbon production constraints. Reserve coverage is expected to gradually decline but remain adequate for most countries.

Risks on the Downside

Trade disruptions from the war in the Middle East are the key risk for the region, with effects varying across countries as a function of their trade links with Iran and their economic specialization. The countries that are geographically closer to Iran are net commodity importers, and those that rely more on tourism are more vulnerable. High import dependency and elevated inflation expose the region to rising global commodity and food prices. Prolonged inflation could force tighter policy stances, especially for oil importers. Heightened geopolitical uncertainty and tighter global financial conditions could reduce foreign investment and business confidence. On the other hand, some countries, such as Armenia and Georgia, might benefit from tourism and capital diverting from the Middle East. The CCA also remains exposed to further developments of the Ukraine war. A lifting of sanctions on Russia could improve the overall sentiment toward the CCA region, thereby reducing risk premiums and lowering external borrowing costs. At the same time, these upsides may be partly diluted by shifts in trade patterns and supply chains established since the onset of the war. Similarly, remigration of Russian nationals established in the region, should it occur, could affect key sectors, consumption, and labor markets, especially if capital inflows and remittances decline.

Policy Priorities: Build Buffers and Strengthen Resilience

Policies should focus on mitigating short-term risks while pursuing medium-term, growth-enhancing reforms:

- *Monetary policy* should promptly address second-round effects from inflationary pressures, by appropriately tightening the stance. In countries experiencing elevated inflation levels above the central bank target (Kazakhstan, Kyrgyz Republic, Uzbekistan), the renewed inflationary pressures from the war in the Middle East will require the authorities to clearly communicate their willingness to tighten, even though the first-round impact of imported commodity inflation may be temporary. In the presence of second-round inflationary effects, a restrictive stance should be maintained until there is clear evidence that underlying inflation and inflation expectations are close to target levels. In countries where inflation is on a clear path to target or historical averages over the forecast horizon, central banks might have more space to see through the first-round effect of higher commodity prices, but if the shock begins to affect underlying inflation or inflation expectations, they should tighten or remain more restrictive than envisaged before the shock. In CCA economies facing relatively high levels of dollarization, building and maintaining a stock of international reserve buffers will help guard against abrupt exchange rate movements.
- *Fiscal policy* should maintain a prudent fiscal stance to preserve buffers and strengthen resilience to downside risks. Commodity exporters should save windfalls from elevated global commodity prices, while any fiscal support to mitigate the impact of high oil and food prices should be targeted, time-bound, and consistent with fiscal sustainability. Strengthening fiscal institutions by improving macro-fiscal capacity, addressing fiscal risks, enhancing medium-term fiscal planning, adopting well-designed, robust fiscal rules, and reducing the government footprint in the economy would help ensure fiscal policy effectiveness and sustainability.

- *A stable financial regulatory framework* is crucial for mitigating policy uncertainty. Supervisors must monitor geopolitical and traditional financial risks to address vulnerabilities swiftly and help guard against abrupt exchange rate movements.
- *Continued structural reforms* are crucial for lifting medium-term growth prospects and mitigating potential longer-lasting impact of geopolitical uncertainty on investor sentiment about the broader region. Structural reforms should accelerate to diversify trade, strengthen institutions, improve governance and the rule of law, promote competition and digitalization, reduce state dominance, and support labor participation, while investing in skills for long-term productivity. These efforts will build resilience and boost inclusive growth by integrating into global value chains and reducing reliance on hydrocarbons.

Table 1. Real GDP Growth

(Year-over-year percent change)

	April 2026					Revision since October 2025			
	2025	2026	2027	2030	2031	2025	2026	2027	2030
Middle East and North Africa Region, Afghanistan, Pakistan (MENAP)[1,2]	**3.2**	**1.4**	**4.6**	**3.8**	**3.7**	**0.0**	**–2.3**	**0.8**	**0.1**
MENAP oil exporters	**2.8**	**–0.1**	**4.8**	**3.3**	**3.2**	**–0.2**	**–3.5**	**1.6**	**0.3**
Gulf Cooperation Council (GCC)	**4.4**	**2.0**	**4.8**	**3.7**	**3.7**	**0.5**	**–2.3**	**0.9**	**0.3**
Bahrain	3.1	–0.5	4.5	3.1	3.3	0.2	–3.8	1.2	–0.1
Kuwait	3.5	–0.6	2.8	2.4	2.4	0.9	–4.5	0.5	0.1
Oman	2.4	3.5	3.4	3.3	2.7	–0.5	–0.5	–0.3	–0.3
Qatar	2.8	–8.6	8.6	5.9	5.0	–0.1	–14.7	0.8	2.5
Saudi Arabia	4.5	3.1	4.5	3.5	3.6	0.5	–0.9	1.3	0.2
United Arab Emirates	5.8	3.1	5.3	4.0	4.0	1.0	–1.9	0.6	0.1
MENAP non-GCC oil exporters	**0.6**	**–3.1**	**4.8**	**2.6**	**2.6**	**–1.2**	**–5.3**	**2.5**	**0.0**
Algeria	3.8	3.8	2.9	2.6	2.6	0.4	0.9	0.2	0.1
Iran	–1.5	–6.1	3.2	2.1	2.1	–2.1	–7.2	1.6	0.1
Iraq	–0.4	–6.8	11.3	3.4	3.5	–0.9	–10.4	7.7	–0.7
Libya	15.9	6.7	4.5	4.0	3.8	0.3	2.5	2.2	1.8
MENAP oil importers[1,2]	**3.8**	**3.8**	**4.3**	**4.5**	**4.4**	**0.3**	**–0.3**	**–0.3**	**–0.2**
MENAP emerging market and middle-income economies	**3.9**	**3.9**	**4.2**	**4.5**	**4.4**	**0.3**	**–0.2**	**–0.1**	**–0.2**
Egypt	4.4	4.2	4.8	4.8	4.8	0.1	–0.3	0.1	–0.5
Jordan	2.7	2.7	3.1	3.0	3.0	0.0	–0.2	0.1	0.0
Lebanon	4.0	…	…	…	…	0.0	…	…	…
Morocco	4.9	4.9	4.5	4.1	4.0	0.5	0.7	0.5	0.3
Pakistan	3.1	3.6	3.5	4.5	4.5	0.4	0.0	–0.6	0.0
Tunisia	2.5	2.1	1.6	1.5	1.5	0.0	0.0	0.0	0.1
West Bank and Gaza	…	…	…	…	…	…	…	…	…
MENAP low-income countries[1,2]	**3.0**	**1.8**	**5.9**	**4.9**	**4.1**	**0.8**	**–3.8**	**–3.9**	**0.0**
Afghanistan	3.0	…	…	…	…	…	…	…	…
Djibouti	6.0	6.0	6.0	5.5	5.5	0.0	0.0	0.0	0.0
Mauritania	4.2	4.4	4.5	3.0	3.0	0.2	0.1	0.1	0.0
Somalia	3.0	2.6	3.1	4.1	4.2	0.0	–0.7	–0.5	0.0
Sudan	3.2	0.7	8.1	6.0	4.5	0.0	–8.8	–6.8	0.5
Syria	…	…	…	…	…	…	…	…	…
Yemen	–0.5	0.5	1.5	2.5	2.5	1.0	0.5	–4.5	–2.5
Middle East and North Africa (MENA) region[1]	**3.2**	**1.1**	**4.8**	**3.7**	**3.6**	**–0.1**	**–2.6**	**1.1**	**0.1**
Caucasus and Central Asia (CCA)	**6.2**	**4.8**	**4.5**	**4.1**	**4.1**	**0.6**	**0.1**	**0.2**	**0.1**
CCA oil exporters	**5.1**	**3.9**	**3.8**	**3.2**	**3.3**	**0.2**	**–0.1**	**0.2**	**0.1**
Azerbaijan	1.4	2.2	2.5	2.5	2.5	–1.6	–0.3	0.0	0.0
Kazakhstan	6.5	4.6	4.4	3.6	3.6	0.6	–0.2	0.2	0.2
Turkmenistan	3.6	2.6	2.0	2.3	2.3	1.3	0.3	–0.3	0.0
CCA oil importers	**7.9**	**6.1**	**5.6**	**5.4**	**5.4**	**1.1**	**0.4**	**0.1**	**0.0**
Armenia	7.2	5.3	5.5	5.0	5.0	2.4	0.4	0.0	0.5
Georgia	7.5	5.3	5.0	5.0	5.0	0.3	0.0	0.0	0.0
Kyrgyz Republic	11.1	6.1	6.1	5.3	5.2	3.1	0.8	0.3	0.0
Tajikistan	8.4	6.0	4.8	4.5	4.5	0.9	0.5	0.0	0.0
Uzbekistan	7.7	6.5	5.9	5.7	5.7	0.9	0.5	0.2	0.0

Sources: National authorities; and IMF staff calculations and projections.
Note: Data refer to the fiscal year for Afghanistan and Iran (March 21/March 20), and Egypt and Pakistan (July/June). The 8.8 percentage points downward revision of 2026 GDP growth (versus October 2025) mainly reflects the delayed end of Sudan's internal war from the end of 2025 to late 2026.
[1] Excluding Syria.
[2] Excluding Afghanistan in 2026–31.

Appendix 1. Country Groupings

Middle East and North Africa (MENA) includes Algeria, Bahrain, Djibouti, Egypt, the Islamic Republic of Iran, Iraq, Jordan, Kuwait, Lebanon, Libya, Mauritania, Morocco, Oman, Qatar, Saudi Arabia, Somalia, Sudan, the Syrian Arab Republic, Tunisia, the United Arab Emirates, West Bank and Gaza, and Yemen.

MENAP oil exporters include Algeria, Bahrain, the Islamic Republic of Iran, Iraq, Kuwait, Libya, Oman, Qatar, Saudi Arabia, and the United Arab Emirates.

MENAP oil importers include Afghanistan, Djibouti, Egypt, Jordan, Lebanon, Mauritania, Morocco, Pakistan, Somalia, Sudan, the Syrian Arab Republic, Tunisia, West Bank and Gaza, and Yemen.

MENAP emerging market and middle-income economies include Egypt, Jordan, Lebanon, Morocco, Pakistan, the Syrian Arab Republic, Tunisia, and West Bank and Gaza.

The Gulf Cooperation Council comprises Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates.

Non-Gulf Cooperation Council oil-exporting countries include Algeria, the Islamic Republic of Iran, Iraq, and Libya.

MENAP Low-income developing countries include Afghanistan, Djibouti, Mauritania, Somalia, Sudan, and Yemen.