East meets East: Economic links between the Middle East and China

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Executive summary

Middle Eastern economies are on an Economic Diversification 2.0 path focusing on 1) Financial market reforms; 2) Fintech and digitalization development; 3) Diversification into non-oil sectors such as renewable energy, tourism, and infrastructure; and 4) Greater regional integration.

We believe China fits right into this new economic growth model. The country is developing stronger ties with the Middle East region on the back of a few building blocks: trading partnerships and cooperation in areas such as energy, finance, infrastructure, the Digital Silk Road, clean energy, and tourism.

We believe the strategic China-Middle East alliance can reshape regional capital flows and the economic outlook of both markets. We anticipate rising investment flows between the two regions and higher growth potential for select sectors such as clean energy, fintech, and digital and traditional infrastructure. In our view, investors should pay close attention to the related investment opportunities emerging from this trend.

Economic Diversification 2.0 in the Middle East

The Middle East's economic growth model relies heavily on oil as the main source of exports and fiscal revenue for countries in the region. Over the past several decades, Middle Eastern governments have used their oil wealth to develop their economies, increase public sector employment and boost spending on infrastructure, health, and education in order to raise living standards for their residents. However, the current growth model is vulnerable given the region's dependence on oil. Volatility and uncertainty in the global oil market can negatively influence economies in the Middle East, as evidenced by oil price shocks during the COVID-19 pandemic and Russia's invasion of Ukraine. As such, it's necessary for Middle Eastern economies to diversify their revenue sources and reduce their reliance on oil.

Economies in the region have therefore been on an Economic Diversification 2.0 path with an emphasis on four areas: 1) Financial market reforms; 2) Fintech and digitalization development; 3) Diversification into non-oil sectors such as renewable energy, tourism, and infrastructure; and 4) Greater regional integration.

1. Financial market reforms

Middle Eastern economies have increasingly been implementing financial market reforms in the region to enable increased access by foreign investors.

<u>Index inclusion</u>

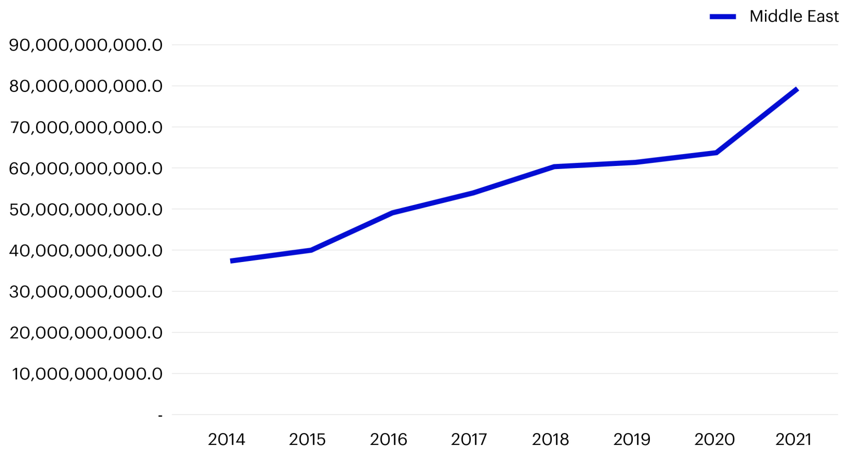
Following a number of regulatory and operational enhancements in local markets in certain Middle Eastern economies, major global index providers have started to include these countries into their major indices. For example, MSCI added Qatar and the UAE into its Emerging Markets Index in 2014 and added Saudi Arabia in 2019. These steps have positively impacted the domestic capital markets of these economies by enhancing market depth and liquidity. Index inclusion has also driven sustainable capital inflows into the region from the passive portfolio managers.

Attracting foreign investment

Over the past decade, governments in the Middle East have revised investment legislation and eased market entry for foreign investors. The region continues to open up to foreign investment, subject to licensing approvals and ownership thresholds for certain business sectors and in certain geographic zones. Several countries have also created free economic zones with looser foreign direct investment (FDI) restrictions than are typically in place. The general trend toward an investment-friendly environment in the Middle East continues as local governments aim to attract more inbound investment by foreign investors. For example, Egypt recently announced the launch of a "golden license" for certain categories of investment projects. In late 2020, the UAE removed the requirement for an Emirati partner for foreign entrepreneurs setting up businesses in the country, opening the way for 100% foreign ownership of firms across the Emirates.

Attracting foreign investment is a key part of Saudi Arabia's "Vision 2030" plan. In 2021, Saudi Arabia introduced a new national investment strategy that set an FDI goal of more than US $100 billion annually by 2030. Saudi Arabia unveiled its first integrated economic zone in Riyadh in late 2022, which is tax-free for companies for up to 50 years, in order to position itself as the region's leading logistics hub and attract foreign investment. On the back of all these efforts, net FDI into Middle Eastern economies has been on an upward trend since 2014 (Figure 1). The region is forecast to have a record year of FDI inflows once again in 2023 according to a report published by Lumina Capital Advisors in January this year.[1]

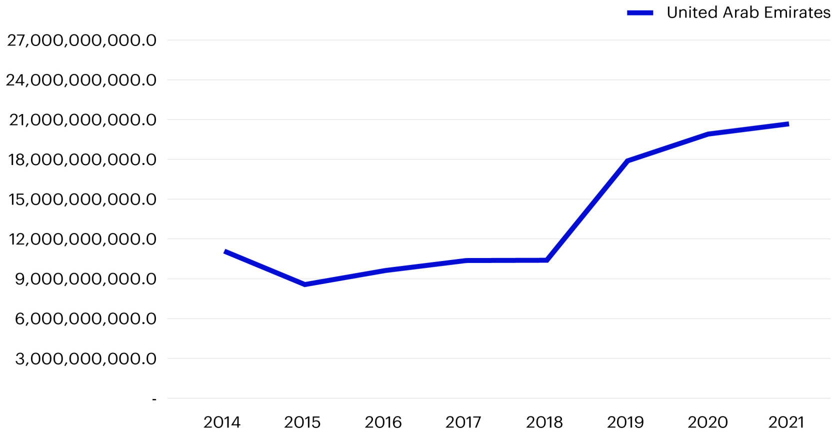
Figure 1 - Net FDI in the Middle East (2014-2021)



Source: World Bank World Development Indicators, data as of December 31, 2021. Note: The Net FDI is in USD. Middle East countries in scope here include UAE, Bahrain, Djibouti, Algeria, Egypt, Iran, Iraq, Israel, Jordan, Kuwait, Lebanon, Syria, Morocco, Malta, Oman, West Bank and Gaza, Qatar, Saudi Arabia, Libya, Tunisia, Yemen.

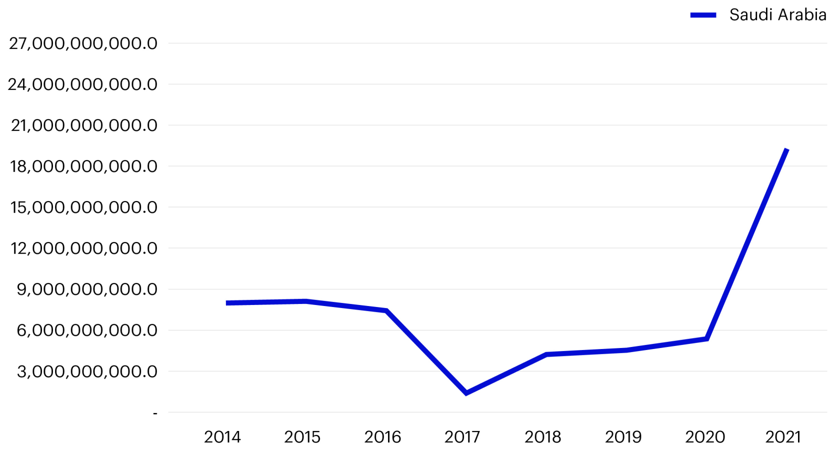
1. FDI round-up: China growth stalls, Middle East set for FDI boost, Bank of England flags 'Truss effect', January 2023, https://www.fdiintelligence.com/content/news/fdi-roundup-china-growth-stalls-middle-east-set-for-fdi-boost-bank-of-england-flags-truss-effect-81911

Figure 2 - Net FDI in the United Arab Emirates (UAE) (2014-2021)



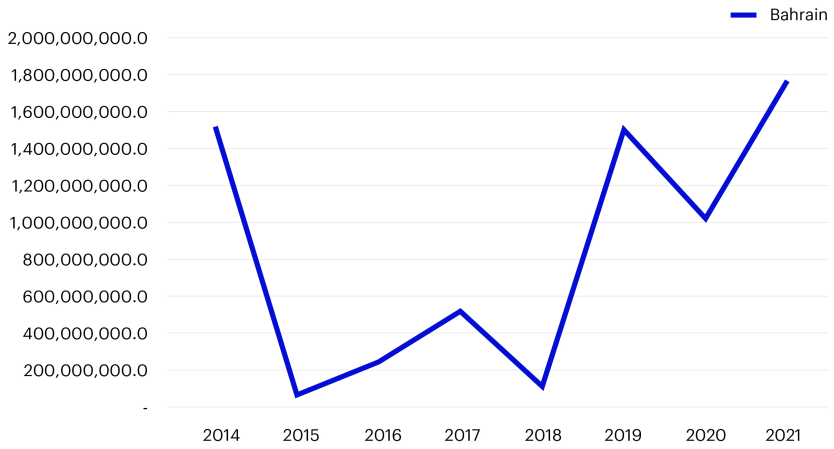
Source: World Bank World Development Indicators, data as of December 31, 2021.

Figure 3 - Net FDI in Saudi Arabia (2014-2021)



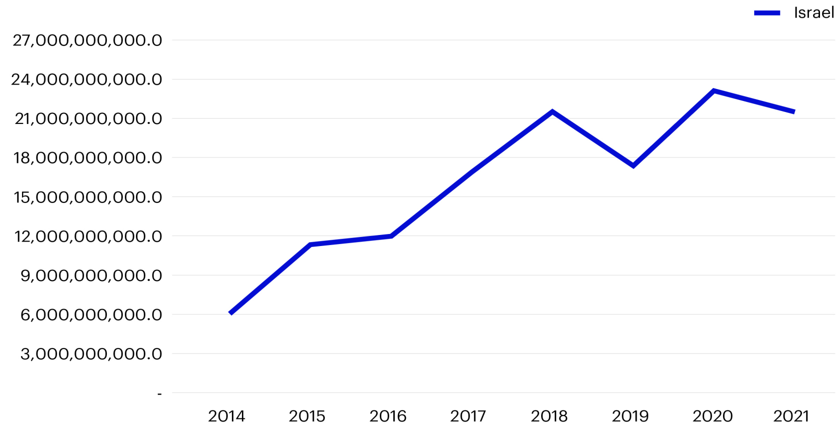
Source: World Bank World Development Indicators, data as of December 31, 2021.

Figure 4 - Net FDI in Bahrain (2014-2021)



Source: World Bank World Development Indicators, data as of December 31, 2021.

Figure 5 - Net FDI in Israel (2014-2021)



Source: World Bank World Development Indicators, data as of December 31, 2021.

Privatization drive and the listing of SOEs and family-owned businesses

Middle Eastern economies have shifted their focus toward privatization in order to create more job opportunities and improve the level of public services. For example, in 2021 Saudi Arabia announced a plan to raise about US $55 billion through its privatization program by 2025.[2] The country also announced the approval of the Private Sector Participation Law in 2021 to adopt legislation governing public-private partnerships (PPPs). The law aims to modernize the Saudi economy with a goal of increasing the private sector's contribution to GDP from 40% to 65%.[3]

Saudi Arabia is not alone in the push for privatization in the region. The Oman government sold 49% of its state-owned electricity transmission company to China's major state-owned electric utility firm in 2019, which marked the first major privatization by the country. Oman's government has also been reported to be exploring the sale of its stake in a cement company for a further privatization drive.[4] Similarly, Abu Dhabi has been reported to be considering the sale of around 10% of its state-owned utility company.[5] We anticipate that privatization will continue to play a significant role for Middle Eastern economies down the road as part of their long-term diversification efforts. There have also been signs of more listings from SOEs and family-owned businesses in Middle Eastern economies, such as the IPO in 2017 of a large conglomerate, the first family business in Qatar to go public.[6]

Capital market developments

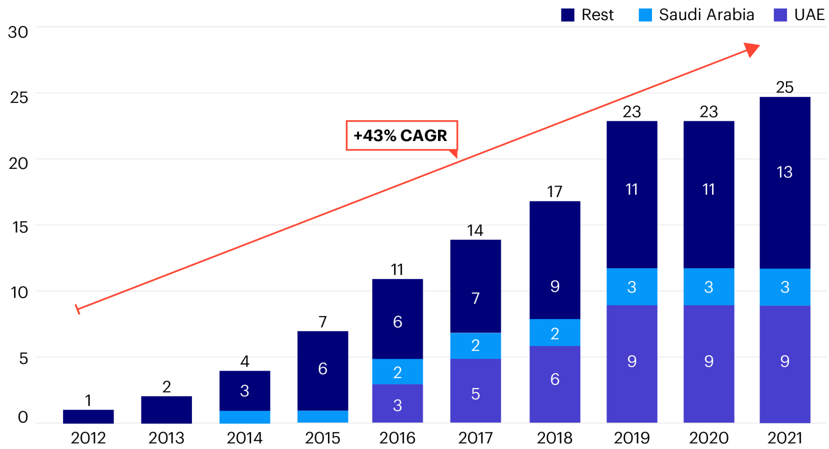
Debt market development in Middle Eastern economies has gathered pace recently. The market for green and sustainable bonds and sukuks in the GCC (Gulf Cooperation Council) economies set a record in 2022, with total issuances reaching US $8.5 billion from 15 deals, compared with US $605 million from six deals in 2021.[7] S&P Global Rating has also predicted strong pipeline of sustainable bonds coming from the Middle East in 2023.[8] The UAE Federal Government raised US $4 billion in its debut dollar bond sale in October 2021.[9] The stock market in Middle East has also had more enhancements. Examples include the establishment of Nomu in Saudi Arabia, an alternative stock exchange with lighter listing requirements[10] and the launch of the Nasdaq Dubai Growth Market, which focuses on supporting SMEs (small and medium enterprises)[11].

2. Saudi Arabia aims to raise $55bn by 2025 through privatization program, May 2021, https://www.arabnews.com/node/1863731/business-economy
3. Issuance of the Private Sector Participation Law in Saudi Arabia, March 2021, https://www.dentons.com/en/insights/articles/2021/march/17/issuance-of-the-private-sector-participation-law-in-saudi-arabia
4. Oman is said to explore cement stake sale in privatisation drive, April 2021, https://www.arabianbusiness.com/industries/banking-finance/462593-oman-is-said-to-explore-cement-stake-sale-in-privatisation-drive
5. Abu Dhabi Plans To Sell $4bn Stake In TAQA, April 2021, https://bondevalue.com/news/abu-dhabi-plans-to-sell-4bn-stake-in-taqa/
6. IHG becomes the first family business in country to go public, January 2017, https://www.gulf-times.com/story/527345/IHG-becomes-the-first-family-business-in-country-to-go-public
7. GCC green bond and sukuk issuances hit a record in 2022, January 2023, https://www.thenationalnews.com/business/markets/2023/01/04/gcc-green-bond-and-sukuk-issuances-hit-a-record-in-2022/
8. 'Strong pipeline' of green bonds likely from Middle East in 2023, S&P says, February 2023, https://www.thenationalnews.com/business/markets/2023/02/09/strong-pipeline-of-green-bonds-likely-from-middle-east-in-2023-sp-says/
9. UAE federal government secures $4bn in first US dollar bond sale debut, October 2021, https://english.mubasher.info/news/3860548/UAE-federal-government-secures-4bn-in-first-US-dollar-bond-sale-debut/
10. Nomu - Parallel Market, 2023, https://www.saudiexchange.sa/wps/portal/saudiexchange/rules-guidance/capital-market-overview/Equities?locale=en
11. Nasdaq Dubai Growth Market, 2023, https://www.nasdaqdubai.com/products/nasdaq-dubai-growth-market

2. Fintech and digitalization development

Middle Eastern economies have seen a rapid rise in fintech and digitalization in recent years. Since 2012, the Middle East digital banking market has experienced sustained growth, rising at a 43% compound annual growth rate (CAGR) (Figure 6)[12].

Figure 6 – Number of digital banks in the Middle East from 2012-2021



Sources: Digital Banking in the Middle East, BPC Group/Fincog, 2022; Fincog Challenger Bank Database, Company websites, public sources. Note: Rest includes Bahrain, Kuwait, Israel, Turkey, Iran, and Egypt.

The region is now home to 25 digital banks serving a combined 25 million people.[13] Fintech investment in the Middle East and North Africa (MENA) region reached US $819 million in the first half of 2022 with a strong focus on payment solutions.[14] Saudi Arabia also set a new national strategy in 2022 to increase the number of fintech companies in the kingdom by threefold by 2025.[15] The development of fintech and digitalization in the Middle East economies are supported by government regulations shown in the below table.

Table 1 – Regulations supporting fintech and digitalization in Middle Eastern countries

Country	Regulatory Support
UAE	Regulatory sandboxes introduced in 2016 in Abu Dhabi and 2017 in Dubai. Federal government is developing legislative framework to regulate fintech and related financial services, with seven digital banks recently licensed and ten fintech accelerators put in place. Virtual Assets Regulatory Authority was established in 2022.
Saudi Arabia	SAMA+ Capital Markets Authority launched the Fintech Saudi initiative in 2018. Three digital banks were granted licenses as of February 2022.
Bahrain	The central bank established a dedicated Fintech and Innovation unit and introduced a regulatory sandbox encouraging fintech firms.
Qatar	A national fintech strategy was announced, and the Qatar Fintech Hub (QFTH) was launched in 2019.
Kuwait	Fintech regulatory sandboxes were introduced in 2018.
Oman	Fintech regulatory sandboxes were introduced in 2020.

Source: UAE: https://thefintechtimes.com/an-overview-of-regulatory-sandboxes-in-the-middle-east-and-africa-region/, https://www.centralbank.ae/en/licensing/, https://fintechnews.ae/12186/fintechdubai/10-fintech-accelerators-to-know-in-the-uae/, https://www.reedsmith.com/en/perspectives/2023/02/dubai, introduces-new-virtual-asset-regulatory-framework; Saudi Arabia: https://www.sama.gov.sa/en-US/News/Pages/news30042018.aspx, https://www.reuters.com/business/finance/saudi-cabinet-approves-licensing-third-digital-bank-central-bank-2022-02-15/; Bahrain: https://www.cbb.gov.bh/fintech/; Qatar: https://fintech.qa/wp-content/uploads/2020/07/A-report-on-the-state-of-FinTech-in-Qatar-1-Oct-2021.pdf; Kuwait: https://thefintechtimes.com/central-bank-of-kuwaits-regulatory-sandbox-to-prioritise-esg-products/; Oman: https://ifnfintech.com/omans-accelerator-program-seeks-to-support-fintech-start-ups-including-islamic-fintech/

12. Middle East Digital Banking Sector Growing at a 43% Annual Rate, December 2022, https://fintechnews.ae/14536/fintech/middle-east-digital-banking-sector-growing-at-a-43-annual-rate/
13. Ibid.
14. What's Powering the Fintech Revolution in the Middle East?, February 2023, https://fintechnews.ae/14896/sponsored/whats-powering-the-fintech-revolution-in-the-middle-east/
15. Saudi Arabia to raise FinTech companies by threefold under new strategic plan, June 2022, https://www.arabnews.com/node/2109006/business-economy

3) Diversification into non-oil sectors such as renewable energy, tourism, and infrastructure

Middle Eastern economies are starting to put more emphasis on non-oil sector growth. For example, Saudi Arabia set a goal in 2022 to increase its share of non-oil exports in non-oil GDP from 16% to 50%.[16] In the UAE, the non-oil sector's contribution to GDP has already started to pick up, which amounted to 72.3% in 2021, compared to 71.3% in 2020.[17]

The push in the tourism sector has been a notable example. Saudi Arabia has set a plan to attract 100 million visitors yearly by 2030. The kingdom targets to increase the tourism sector's GDP contribution from 3% to 10% by 2030.[18] Egypt targets to double its tourism figures to reach 25 to 30 million by 2028.[19] Data from the United Nations World Tourism Organization (UNWTO) World Tourism Barometer (per below table) noted that while all regions enjoyed a significant increase in international arrivals in 2022 over the previous year, the Middle East recorded the strongest relative increase as international tourist numbers climbed to above 80% of pre-pandemic numbers in 2022[20], driven by large events such as Expo 2020 Dubai and the FIFA World Cup in Qatar.

Table 2 – International tourism in 2019 and 2022

Region	International Tourism in 2019 (in million)	International Tourism in 2022 (in million)	2022/2019
Europe	744.5	584.9	78.6%
Asia Pacific	359.6	84.4	23.5%
Americas	219.3	142.4	64.9%
Africa	68.8	45.0	65.4%
Middle East	73.3	60.3	82.3%

Source: World Tourism Organization (UNWTO), data as of December 31, 2022

Middle Eastern economies also stepped up investments into infrastructure projects. Saudi Arabia launched a national infrastructure fund in 2021 to invest over US $50 billion in infrastructure projects over the next decade.[21] One of the UAE's largest conglomerates has been reported to have invested US $3 billion in the real estate sector in 2023 year-to-date.[22] There are also four iconic giga-projects being constructed as part of Saudi Arabia's Vision 2030, funded by the Public Investment Fund (Table 3).

Table 3 - Giga-projects of Saudi Arabia

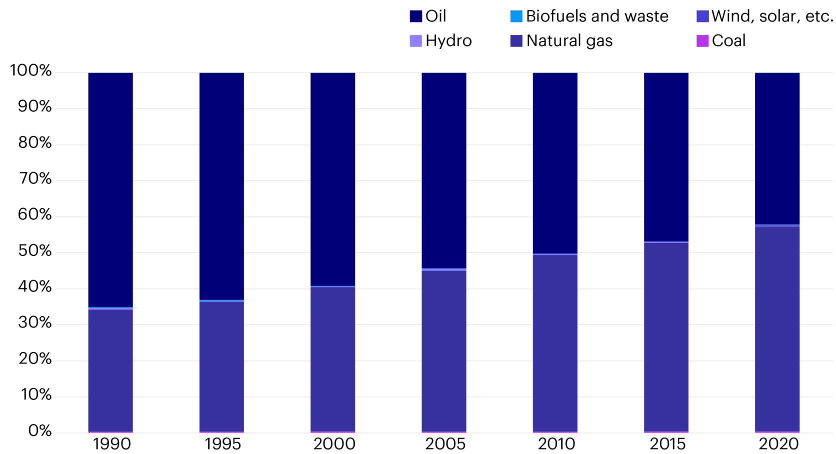
NEOM Smart City	Amaala Red Sea Riviera	Red Sea Resort Project	Qiddiya Entertainment City
26,500sq km project area	3,300 sq km project area	34,000 sq km project area	334 sq km project area
AI enabled smart city as a hub for innovation and sustainable ecosystem for living and working.	Ultra-luxury wellness tourism consisting of 2,500 hotel rooms, 200 retail establishments, an art gallery, marinas, 700 villas, and a dedicated commercial airport.	Consists of an archipelago of more than 90 unspoiled islands, inland resorts, marinas, luxury residential properties, recreation facilities and a commercial airport to serve the destination.	Fully self-contained recreational and entertainment city.

Source: The ' Giga-Projects' of Saudi Arabia, October 2019, https://www.driver-group.com/en/europe/news/the-giga-projects-of-saudi-arabia

16. Opening Up To The World: Saudi Arabia's Tourism Goals, August 2022, https://www.entrepreneur.com/en-ae/growth-strategies/opening-up-to-the-world-saudi-arabias-tourism-goals/434447
17. UAE reports slight growth of non-oil GDP, April 2022, https://www.al-monitor.com/originals/2022/04/uae-reports-slight-growth-non-oil-gdp
18. Saudi seeks to attract 100 million visitors yearly by 2030, February 2023, https://economymiddleeast.com/news/saudi-visitors-2030/
19. Egypt hopes to double tourists figures to 25-30 mln per year by 2028, minister tells Senate, January 2023, https://english.ahram.org.eg/NewsContent/1/1238/484710/Egypt/Tourism/Egypt-hopes-to-double-tourists-figures-to--mln-per.aspx
20. UNWTO World Tourism Barometer, January 2023, https://webunwto.s3.eu-west-1.amazonaws.com/s3fs-public/2023-01/UNWTO_Barom23_01_January_EXCERPT.pdf?ww.petroplan.com/blog/2023/01/the-rapid-rise-of-renewable-energy-in-the-middle-east-/94
21. Saudi Arabia launches national infrastructure fund, October 2021, http://www.news.cn/english/2021-10/25/c_1310267820.htm
22. UAE's Al Habtoor Plans to Invest $3 Bn in Real Estate Sector in 2023, January 2023, https://invest-gate.me/news/uaes-al-habtoor-plans-to-invest-3-bn-in-the-real-estate-sector-in-2023/

Another key area of focus is the renewable energy and clean technology sector. Currently the region still relies heavily on its vast reserves of oil and gas, with over 98% of the Middle East's total energy supply coming from oil and natural gas[23] (Figure 7).

Figure 7 – Total energy supply for Middle Eastern countries



Source: IEA World Energy Balances 2022, https://www.iea.org/data-and-statistics/data-product/world-energy-statistics-and-balances.

But the Middle East has gradually shifted to target to become a leader in renewable energy. Clean energy capacity in the region doubled between 2010 and 2020 to 40GW and is set to double again by 2024.[24] The UAE, a leader for renewables in the region, aims to increase the contribution of clean energy in the total energy mix to 50% by 2050 and targets to have a 25% share of the global low-carbon hydrogen market by 2030.[25] The UAE also launched a national plan to achieve net-zero emissions by 2050.[26] Clearly, the UAE is not the only Middle Eastern economy that is focused on green energy. Jordan, for example, has more than 20% of its electricity grid powered by solar or wind energy and has set a target to achieve 31% by 2030.[27] The charts[28] below show the renewable energy targets and additions in Middle Eastern economies as they make joint efforts to go green.

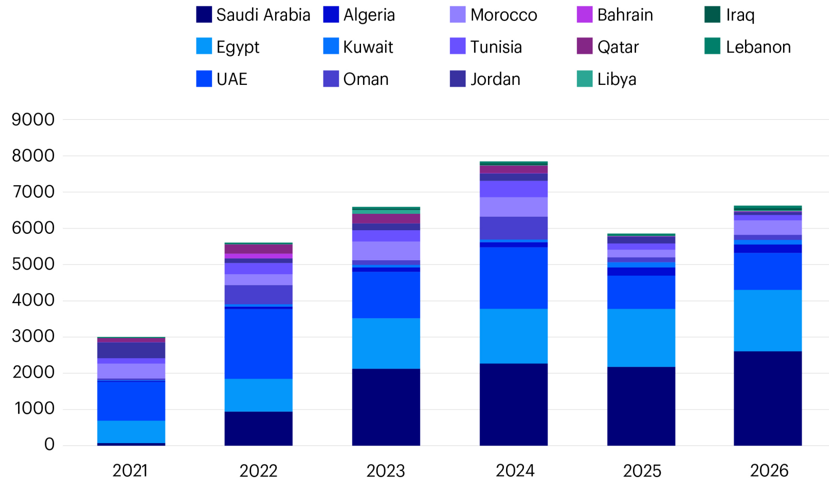
Figure 8 – Renewable energy targets in select MENA countries

Country	RE policy targets	Progress '21
Saudi Arabia	10% of generation by 2025, 50% by 2030	< 1% of generation
UAE	44% of generation mix by 2050 (federal)	≈ 5% of generation (federal)
Oman	10% of generation by 2025, 30% by 2030	< 1% of generation
Qatar	20% of generation by 2030	< 1% of generation
Kuwait	15% of generation by 2030	< 1% of generation
Jordan	31% of generation mix by 2030	≈ 20% of generation
Iraq	5% of generation by 2025, 20% by 2030	< 1% of generation
Lebanon	30% of generation mix by 2030	≈ 7% of installed capacity
Egypt	20% of generation by 2022, 42% by 2035	≈ 11% of generation
Morocco	52% of installed capacity by 2025, 70% by 2040	≈ 40% of installed capacity
Algeria	37% of installed capacity by 2030	< 1% of installed capacity

Source: APICORP

23. The rapid rise of renewable energy in the Middle East, January 2023, https://www.petroplan.com/blog/2023/01/the-rapid-rise-of-renewable-energy-in-the-middle-east-/94
24. The rapid rise of renewable energy in the Middle East, January 2023, https://www.petroplan.com/blog/2023/01/the-rapid-rise-of-renewable-energy-in-the-middle-east-/94
25. Saudi seeks to attract 100 million visitors yearly by 2030, February 2023, https://economymiddleeast.com/news/saudi-visitors-2030/
26. Egypt hopes to double tourists figures to 25-30 mln per year by 2028, minister tells Senate, January 2023,
27. Jordan - Country Commercial Guide – Renewable Energy, December 2022, https://www.trade.gov/country-commercial-guides/jordan-renewable-energy
28. MENA Energy Investment Outlook 2022-2026, June 2022, https://www.apicorp.org/wp-content/uploads/APICORP-Annual-MENA-Energy-Investment-Outlook-2022-26_EN.pdf

Figure 9 – Renewables additions by select MENA countries (recent and projected)



Source: APICORP

As the push for renewable energy and clean technology illustrates, ESG is becoming a more important factor and Middle Eastern economies are taking this into account. Since 2021, the United Arab Emirates Securities and Commodities Authority (SCA) required public joint stock companies listed in the UAE to adhere to specific ESG disclosure requirements.[29] Based on a survey done by a management consulting firm in 2022, over 70% of companies in the Middle East reported their financials by accounting for material ESG factors. Close to 50% of companies have stand-alone sustainability reporting. Most of the companies are also in the process of establishing formal ESG reporting frameworks to catch up with their global peers regarding ESG efforts.[30] It's expected that more ESG government policies and regulations will be introduced to better guide company management and capital investment in the region.

4) Greater regional integration

Middle Eastern economies in general have welcomed a changing geopolitical landscape to develop their regionalization strategy. Progress has been seen on both the regional political stance and regional globalization perspective.

In terms of the regional political stance, there have been positive developments in the region, as evidenced by the deal to restore ties between Saudi Arabia and Iran brokered by China in 2023. Economies in the region have also accelerated joint industrial partnerships.[31] Diplomatic openings such as the signing of the Abraham Accords in 2020 also forged new links for countries within the region.

On the regional globalization front, the Middle East has embraced greater regional integration such as by the formation of the Red Sea Council in 2020. More cross-border trade and investment agreements have been signed in recent years such as the UAE's FTAs (Free Trade Agreements) with India and Indonesia. The development of the renewable energy sector also links the Middle East countries with other economies globally, for example UAE's tight cooperation with India on clean energy and the growing cooperation to develop green energy between the European Union and Middle East.

29. Legal Update: The rise of ESG in the UAE: Mandatory ESG reporting for all USE listed companies, April 2021, http://mobile.chinagoabroad.com/en/knowledge/show/id/32076
30. A Snapshot of ESG in the Middle East, January 2023, https://humancapital.aon.com/insights/articles/2022/a-snapshot-of-esg-in-the-middle-east
31. UAE, Jordan, Egypt, and Bahrain to accelerate industrial partnership, February 2023, https://fastcompanyme.com/news/uae-jordan-egypt-and-bahrain-to-accelerate-industrial-partnership/

How does China fit into the Economic Diversification 2.0 plan?

The Middle East and China's economic relationship has been growing in recent years. With the region pushing for economic and strategic diversification, we believe its ties with China will undoubtedly strengthen over time. There are a few building blocks for a strategic China-Middle East alliance, which we believe will likely further drive the future cooperation between the two parties. These include trading partnerships and cooperation in areas such as energy, finance, infrastructure, the Digital Silk Road, clean energy, and tourism.

1) Energy cooperation

China is the largest customer for Saudi crude oil and the largest purchaser of Middle Eastern oil globally.[32] Middle Eastern producers account for half of China's total oil imports.[33] Despite the push toward diversification, energy remains a major source of income for the region's economies. We expect cooperation in the energy sector to remain active for the two parties. A recent example of such close cooperation was the 27-year deal agreement signed by a Chinese state-owned energy giant to buy liquified natural gas from Qatar, marking the longest term for such a gas deal that has ever been brokered.[34]

2) Trading partnerships

China's trade with Middle Eastern countries doubled between 2020 and 2021. China accounted for 16.7% of the Middle East's total trade in 2021. It also supplanted the EU as the Gulf's largest trading partner in 2020.[35] Without doubt, China is a major trading partner for Middle Eastern economies. The China-GCC FTA negotiations have been ongoing since 2004. With Chinese President Xi's historic visit to Saudi Arabia in 2022 signalling a major shift in the strategic relationship between China and the GCC, it's likely that there will be more progress on the FTA discussion. If the agreement is realized, trading relationships between China and the region could be strengthened further.

3) Financial cooperation

Middle Eastern economies and China have stepped up their banking and payments systems integration to support trade and investment flows. Notably, Saudi Arabia was reported to consider accepting yuan instead of dollar payments for oil sales in 2022.[36] Chinese President Xi also called for the adoption of the PetroYuan at the Gulf summit in Riyadh in 2022.[37] Both parties have also worked towards expansion of central bank swap agreements, including China's RMB 35 billion currency swap agreement with UAE [38] and China's RMB 35 billion currency swap agreement with Qatar.[39] Apart from this, China is actively promoting its cross-border payment system CIPS (Cross-border Interbank Payment System) internationally, which could be extended to the Middle Eastern economies in the future.

32. Russia surpasses Saudi Arabia as China's top oil supplier, March 2023, https://www.middleeasteye.net/news/russia-surpasses-saudi-arabia-chinas-top-oil-supplier
33. Is China Overly Reliant On Middle Eastern Oil?, January 2023, https://oilprice.com/Energy/Energy-General/Is-China-Overly-Reliant-On-Middle-Eastern-Oil.html
34. Sinopec signs 27-year LNG deal with QatarEnergy, to improve energy supply security, November 2022, https://www.globaltimes.cn/page/202211/1280095.shtml
35. Source: UBS, IMF, data as of December 31, 2021
36. Saudi Arabia reportedly considering accepting yuan instead of dollar for oil sales, March 2022, https://thehill.com/policy/energy-environment/598257-saudi-arabia-considers-accepting-yuan-instead-of-dollar-for-oil/
37. China's Xi calls for oil trade in yuan at Gulf summit in Riyadh, December 2022, https://www.reuters.com/world/saudi-arabia-gathers-chinas-xi-with-arab-leaders-new-era-ties-2022-12-09/
38. China, UAE sign 35 billion yuan currency swap: PBOC, January 2012, https://www.reuters.com/article/us-china-uae-currency-idUSTRE80G19020120117
39. Qatar Becomes Centre For Renminbi Clearing And Settlement, November 2014, http://www.qcb.gov.qa/English/News/Pages/chinamouagreement.aspx

Overall, the banking payment systems integration between China and Middle East could see further improvement and drive more flows between the two parties. Moreover, it's likely that there could be further financial markets linkages between the Middle East and China. The two parties share similar economic governance models where state-owned enterprises play major roles in their economies. Their steps toward capital market liberalizations are also similar and there is rooms for collaboration in this process for both parties. Lastly, there are growing linkages between China's state capital and the Middle East's sovereign wealth funds. In 2015, a US $10 billion UAE-China Joint Investment Fund was established by Mubadala, China Development Bank Capital and the Chinese State Administration of Foreign Exchange.[40]

4) Infrastructure cooperation

The Middle East provides a market for Chinese goods, construction contracts and investment opportunities in infrastructure, manufacturing and the digital economy which fits right into China's Belt and Road Initiative. China has signed Belt and Road cooperation documents with 21 Arab countries and the League of Arab States.[41] Saudi Arabia alone received US $5.5 billion in investments and contracts through China's Belt and Road Initiative in the first half of 2022, more than any other country.[42] Under the Belt and Road Initiative, many projects in Middle Eastern economies have been backed by Chinese money, such as Qatar's Lusail Stadium, hotels in Oman, and auto-manufacturing in Saudi Arabia. China is also helping to build Cairo's new administrative capital[43] and is constructing the new metro in Mecca[44]. In our view it would be in both parties' interests to continue their cooperation in infrastructure development in the region.

5) Digital Silk Road cooperation

The Digital Silk Road was endorsed by Chinese officials in 2015 and further promoted at the second Belt and Road Forum in 2019. The strategy aims to promote digital infrastructure, smart city and cross-border e-commerce in the Belt and Road region. The strategy fits in well with the Economic Diversification 2.0 path given its focus on fintech and digitalization. China and the Middle East have worked closely in terms of digital cooperation, as evidenced by the presence of major Chinese technology giants that are bringing their knowhow to the region. During Chinese President Xi's visit to Saudi Arabia in 2022, Saudi Arabia signed a memorandum with China's major information and communications technology company on cloud computing and building high-tech complexes in Saudi cities.[45] The same firm has participated in building 5G networks in most Gulf states. In 2018, a UAE technology-enabled payments solution provider announced a partnership with a major Chinese tech giant on payment services.[46] In 2022, a company owned by Saudi Arabia's sovereign wealth fund announced a USD 207 million joint venture with a major Chinese AI firm to build an AI lab in the kingdom.[47] We expect Middle Eastern institutions to continue to be interested in advanced Chinese technologies and expect digital cooperation between both markets to continue.

40. UAE-China Joint Investment Fund, https://www.mubadala.com/en/what-we-do/uae-china-joint-investment-fund Foreign Ministry Spokesperson Mao Ning's Regular Press Conference on December 8, 2022, December 2022, http://melbourne.china-consulate.gov.cn/eng/fyrth/202212/t20221208_10987235.htm
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42. Chinese-constructed CBD project in Egyptian capital boosts local development, August 2022, http://english.scio.gov.cn/beltandroad/2022-08/23/content_78384445.htm
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46. Network International to support Alipay in the UAE, July 2018, https://www.network.ae/en/news/view/network-international-to-support-alipay-in-the-uae
47. Saudi Sovereign Wealth Fund Partners With China's SenseTime, October 2022, https://www.asiape.com/publication/saudi-sovereign-wealth-fund-partners-with-china-s-sensetime

6) Clean energy and tourism cooperation

Like digital development, clean energy is another area where Chinese policy makers are putting significant emphasis. China dominates the global manufacturing industry for renewables as it accounts for 72% of global solar manufacturing and 50% of global wind turbine manufacturing.[48] Under China's Green Silk Road push, the country has actively cooperated with local governments to build green infrastructure. This could become a major sector where we see partnership between the Middle East and China going forward. Europe and India are already cooperating with Middle Eastern economies on green initiatives. Aside from cooperation in clean energy, tourism is another key area where both markets can collaborate as Chinese tourists represent a huge market for the Middle East. Chinese tourists to the UAE already surpassed 1 million in 2017 and China has accounted for the largest share of overseas tourists in Abu Dhabi since 2017, overtaking India.[49] As China has reopened since Covid-19 in 2023, the tourism sector could see yet another boost.

Investment Implications

We believe the strategic China-Middle East alliance can reshape regional capital flows and the economic outlook of both markets. We expect investment flows between the two regions to rise. In recent years, officials from Middle Eastern sovereign wealth funds have focused a larger proportion of their portfolios on Asian economies, especially China.[50] A notable example in 2023 has been the US $300 million funding round co-led by Abu Dhabi's sovereign fund Mubadala for one of China's largest industrial supply chain technology companies through its China investment program.[51] All evidence is also pointing toward more capital and trade flows from China to the Middle East as a part of this long-term strategic partnership. We expect these positive investment flows to support asset prices in both regions. We also anticipate higher growth potential for selected sectors such as clean energy, fintech, and digital and traditional Infrastructure. In our view, investors should pay close attention to the related investment opportunities emerging from this trend.

48. What's After Coal? Accelerating China's Overseas Investment in Renewables, January 2023, https://www.wri.org/insights/whats-after-coal-accelerating-chinas-overseas-investment-renewables
49. Chinese tourists to UAE exceed 1mln in 2017, https://petra.gov.jo/Include/InnerPage.jsp?ID=10306&lang=ar&name=en_news
50. Source: UBS, data as of January 8, 2023
51. Abu Dhabi's Mubadala co-leads $300m round for China's JD Industrials, March 2023, https://www.thenationalnews.com/business/2023/03/22/abu-dhabis-mubadala-co-leads-300m-round-for-chinas-jd-industrial/

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