STANDARD & POOR'S SOVEREIGNS

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Qatar (State of)

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Credit Ratings

A+/Positive/A-1

Default History Since 1975
None
Year
2004
Population
0.66 million
Per Capita GDP
$32,165
Current Government
Sheikh Hamad bin Khalifa al-Thani is the Emir and head of state.
Election Schedule
Parliamentary
Next......expected in 2005

Major Rating Factors

Strengths:

- Prudent fiscal policy.
- Substantial external liquidity.
- Strong economic prospects and high per capita income.

Weaknesses:

- Relatively high public sector external debt.
- Developing political and economic institutions.

Rationale

The ratings on the State of Qatar primarily reflect the country's very strong economic prospects--driven largely by the gas industry--combined with continuous prudence in fiscal policy and the ongoing improvement in domestic political institutions.

Standard & Poor's expects Qatar's prudent fiscal policy to continue. The State's budget for 2004-2005 assumes an average oil price of $19.0 per barrel and targets a deficit of about 2.5% of GDP. By contrast, taking a baseline assumption of an average Brent crude price of about $34.5 per barrel, there will be a fiscal surplus of about 11.6% of GDP in 2004-2005. General government debt has declined in recent years to 50.2% of GDP at the end of fiscal year 2003-2004 (March 31, 2004), with a further improvement to about 44.0% of GDP expected for the end of fiscal year 2004-2005. The government has substantial financial assets. Qatar's debt and debt-service burdens have continued to decline and are projected to maintain their downward trend. Moreover, taking into account the government's domestic bank deposits would reduce its debt burden to about 27.0% of GDP in 2003-2004, a projected 22.7% in 2004-2005, and 19.0% in 2005-2006.

The ratings on Qatar also benefit from a strong external liquidity position, which was further bolstered in 2003 by a current account surplus estimated at 33% of GDP. The current account could again register surpluses of about 45%-48% of GDP in 2004-2006. These improvements have been driven mainly by increases in export receipts from liquefied natural gas (LNG), which should continue to grow over the next few years thanks to strong net foreign direct investment inflows in the sector and growing production and export capacities.

Qatar's GDP per capita, estimated at $32,165 in 2004, places it among the world's wealthiest nations. Growth is expected to maintain its high pace, at about 7.0% in 2005 and 5.0% in 2006, compared with a projected 8.2% in 2004. This performance is driven by gas and gas-related industries and the development of the private sector.

The ratings are constrained, however, by relatively high public sector external debt and still-evolving political and economic institutions. Project-related borrowing in the past few years led to a build-up of public sector external debt that peaked at 167% of external current account receipts in 1997, but declined to less than 74% by 2003. This ratio is expected to decline further to 56% by 2005. Plans for substantial increases in natural gas export capacity will also need considerable financing. Based on the financing schemes used in the past few years, however, the potential contingent liabilities for the government should be limited.

Qatar's political system is evolving slowly from traditionally tribal structure to a modern one, and has a history of difficult succession. The new constitution promulgated by the Emir, Sheikh Hamad bin Khalifa al-Thani, in June 2004 is, however, expected to enhance government accountability and transparency, and to strengthen the predictability of decision-making. Nevertheless, there is a shortfall in the institutions needed to improve the functioning of a market economy. Despite very positive advances in political liberalization, notably compared with other Gulf Cooperation Council countries, the process of strengthening institutions is slow, particularly with regard to the challenges of maintaining high economic growth and implementing the new constitution.

Outlook

The positive outlook assumes higher budgetary revenues, on the back of higher-than-expected hydrocarbon exports and continued fiscal prudence. This is underpinned by ongoing important institutional reforms, especially with the expected implementation of the new constitution and parliamentary elections in 2005. Although the maturing of the domestic political environment and diminished geopolitical risks reduce the likelihood of political and economic shocks, institutions are not yet sufficiently developed to support a fully efficient market economy. The ratings could be raised if the government effectively strengthens the country's political system and institutions, notably by implementing the new constitution and enhancing the transparency of its public finances.

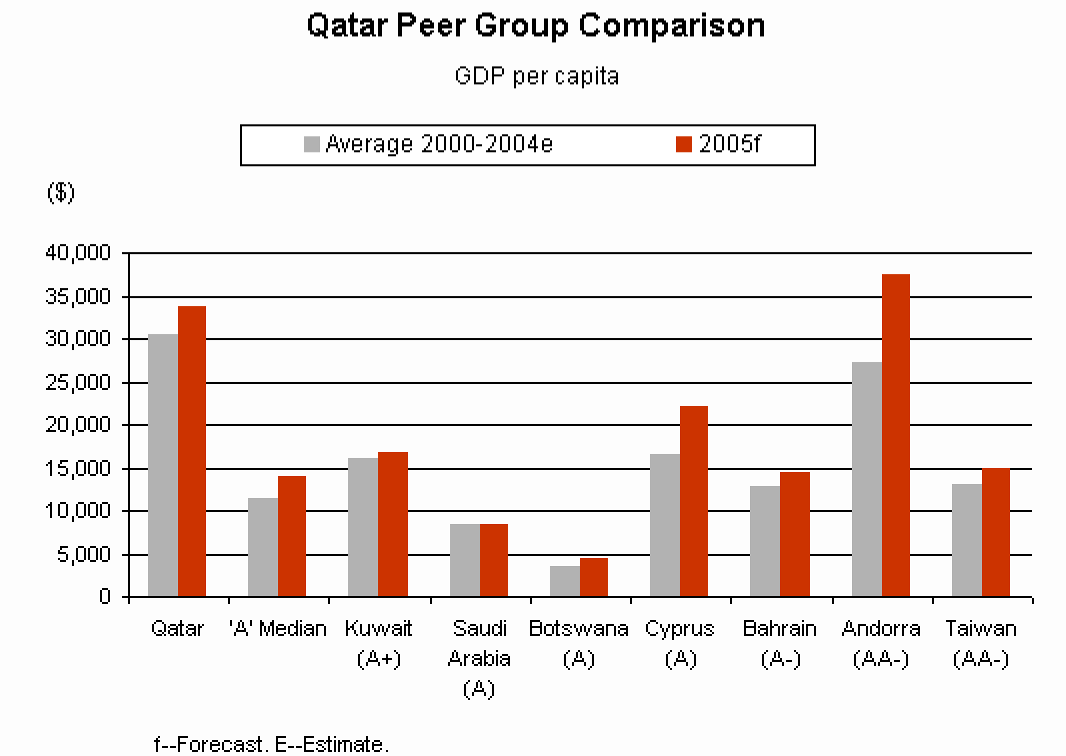
Table 1 State of Qatar Selected Indicators							
	2007f	2006f	2005f	2004e	2003	Average 2000-2004e	'A' median 2003
GDP per capita ($)	37,793	34,046	33,772	32,165	30,595	30,421	13,338
Real GDP (% change)	11.1	5.0	6.9	8.2	8.4	6.9	3.8
Real per capita GDP (% change)	8.0	2.1	3.8	5.1	5.3	4.0	3.2
General government balance (% of GDP)	7.9	10.1	11.6	10.5	8.1	5.3	(0.8)
General government debt (% of GDP)	34.5	41.6	45.4	50.8	55.1	55.9	44.6
Net general government debt (% of GDP)	(123.2)	(127.1)	(117.2)	(110.0)	(101.1)	(96.6)	26.4
General government interest expenditures (% of revenues)	5.4	6.0	6.3	7.4	9.5	9.9	4.8
Consumer price index (average; % change)	2.0	2.0	2.0	2.8	2.3	1.7	2.1
Domestic credit to private sector (in % of GDP)	39.0	40.9	38.9	38.6	38.4	33.2	64.1
Gross external financing gap* (% of reserves)	(120.7)	(114.6)	(140.2)	(164.2)	(129.5)	(180.4)	124.0
Public Sector net external debt (% of CARs)	(13.6)	(5.1)	3.3	12.0	26.2	43.0	(14.3)
Financial sector net external debt (% of CARs)	(37.5)	(34.2)	(29.2)	(25.1)	(26.0)	(23.6)	(1.9)
Nonfinancial private sector net external debt (% of CARs)	(13.1)	(12.7)	(12.5)	(12.3)	(7.0)	(11.1)	3.7
*Current account balance plus amortizations plus short-term debt. CARs--Current account receipts. f--Forecast. e--Estimate							

Comparative Analysis

- Within its peer group, Qatar has the smallest and wealthiest population and the most streamlined policy-making process, but its institutions are still developing.
- Compared with peers, Qatar's economy depends more heavily on a single economic activity (oil and gas). Nevertheless, because the public sector has a majority stake in this activity, public finances are very strong.
- Qatar's total external debt stock and debt-service payments relative to its export earnings have been higher than those of its peers, but are now on a downward trend.

The population is small and wealthy compared with peers.
Qatar's population of about 655,000 in 2003 is one of the smallest rated sovereigns. There are no published official figures on the number of nationals, but independent estimates put this figure at 150,000-250,000. The rest are foreign workers--both Arab and non-Arab--who are employed by both the government and the private sector. There is no registered unemployment among Qataris. GDP per capita is expected to reach $32,165 in 2004, which makes the sovereign one of the wealthiest nations in the world (see Chart 1). This measure suffers from the usual shortcoming of concealed income inequality. Moreover, in the case of Qatar and other Gulf states, it should be used with additional care because of the presence of a large foreign labor force that earns much less than the national labor force.

Chart 1



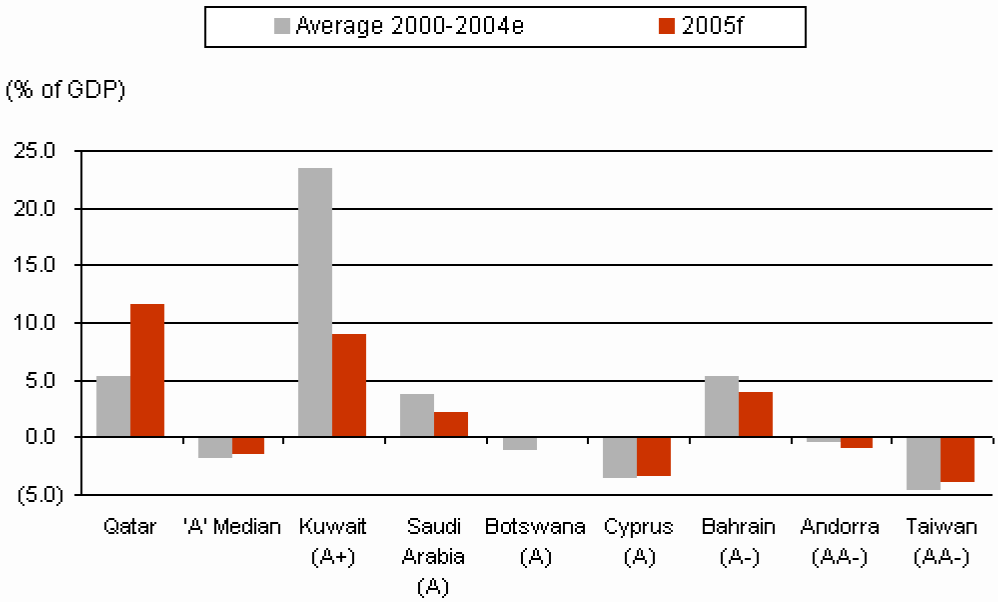
A new constitution will usher in democracy.
Qatar is a member of the Gulf Cooperation Council (GCC), along with the Kingdom of Bahrain (foreign currency A-/Positive/A-2; all references to ratings hereafter are to foreign currency sovereign credit ratings), the State of Kuwait (A+/Stable/A-1+), the Sultanate of Oman (BBB/Stable/A-3), the Kingdom of Saudi Arabia (A/Stable/A-1), and the United Arab Emirates (UAE). Like certain other GCC members, Qatar's political system has been evolving from a traditional tribal system to a modern democratic one. Qatar's political evolution, however, accelerated after the present Emir came to power in 1995. The new constitution was approved by a 97% majority vote in a referendum held in April 2003, and was ratified by the Emir in June 2004. The constitution is set to come into force in June 2005 and parliamentary elections will be held the same year. Both men and women will have equal political rights, as they did in the municipal elections of 1999 and early 2003.

Costs and benefits of energy dependence.
Qatar's economy is highly dependent on oil and gas exports and is therefore greatly vulnerable to oil price shocks. In this sense, the country's economy is narrowly based, and is comparable to Kuwait, the Republic of Iceland (A+/Positive/A-1+) and Saudi Arabia. The public sector has a majority stake in this highly successful industry, however, and so prudent fiscal policy has mitigated the impact of price shocks and enabled the government to accumulate a comfortable cushion of reserves, which probably exceeds that of Oman, although it is not as large as that of Kuwait. As in Kuwait, and to a lesser extent Saudi Arabia, the current high oil prices and prudent price assumption in planning budget expenditures have led to comfortable surpluses since 2000 (see Chart 2).

Chart 2

Qatar Peer Group Comparison

General Government Balance



f--Forecast. E--Estimate.

Moreover, Qatar's industrial base is modern and competitive and does not face the type of restructuring challenges that confront its larger and more diversified peers such as the Republic of Korea (A-/Stable/A-2) or the Czech Republic (A-/Stable/A-2). In addition, Qatar does not have an unemployment problem, which distinguishes it even from Bahrain and Oman. Unemployment is estimated at 2% of the total labor force, and the public administration could easily afford to absorb more Qataris by reducing the number of non-Qataris in its ranks.

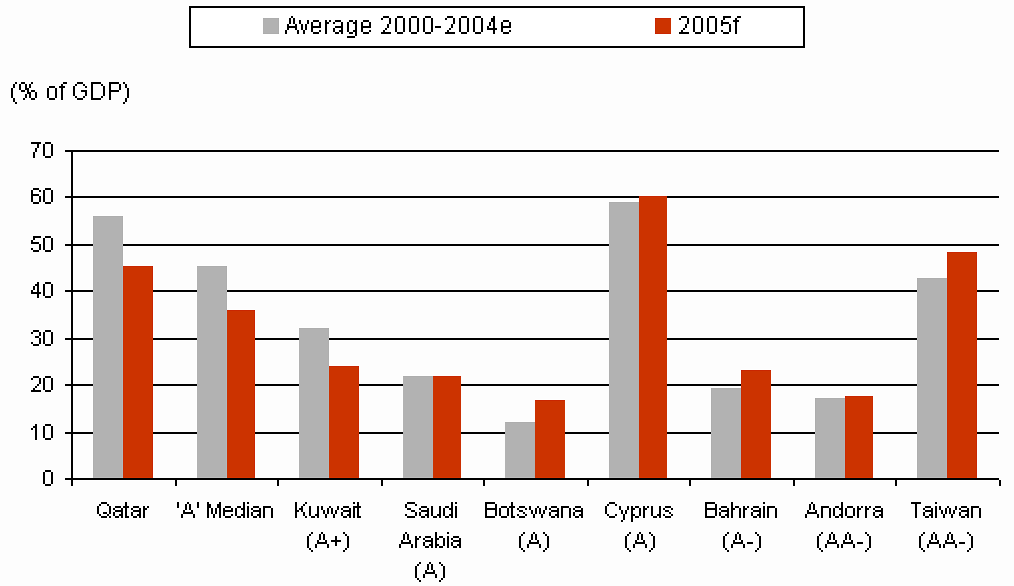
Debt indicators are less favorable than those of peers.

Qatar's government has been bold and decisive in developing the country's natural resources in partnership with major international companies. It borrowed heavily to build up its natural gas industry rather than financing budget deficits, and it is now reaping the rewards. Consequently, its external debt indicators, which are now less favorable than those of certain peers, have begun to improve since 2002 (see Charts 3 and 4). At 98.3% of GDP in 2004, however, total public sector debt remains one-third more than the 'A' median, which is 65.1% of GDP.

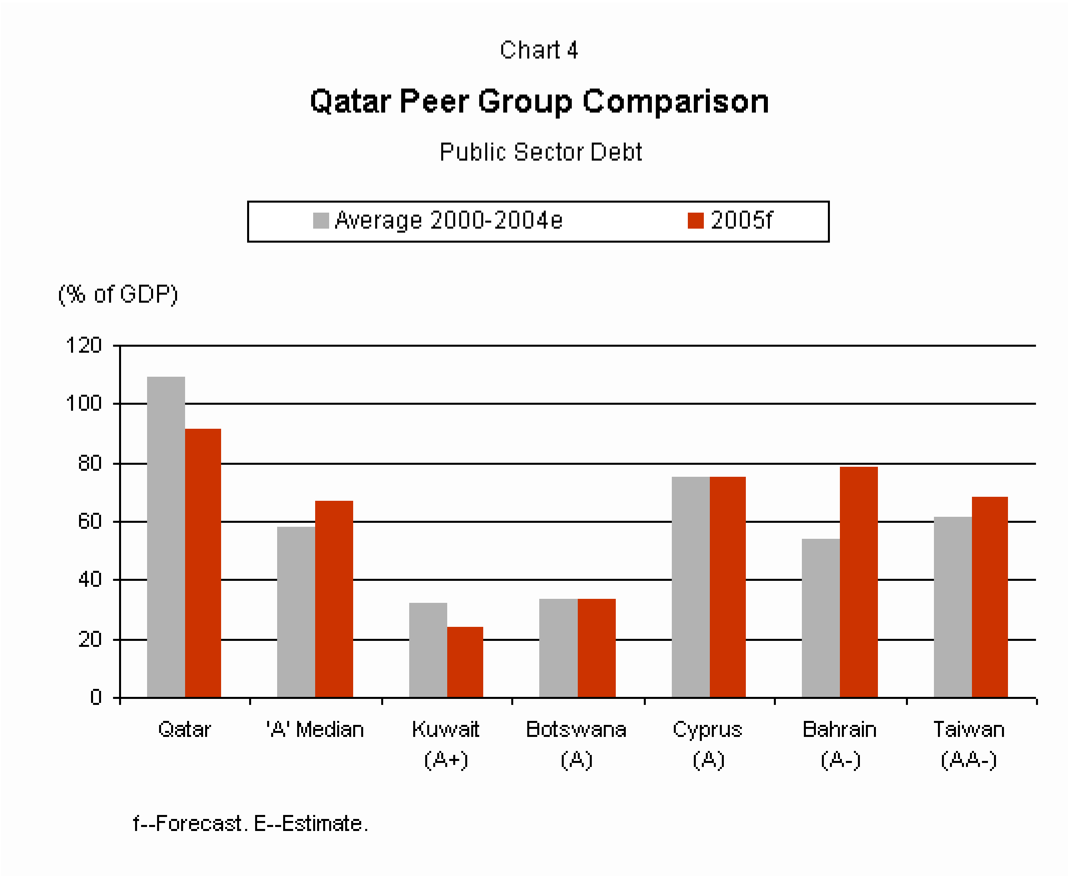
Chart 3

Qatar Peer Group Comparison

General Government Debt



f--Forecast. E--Estimate.



Political Environment

- A constitution providing for modern state institutions with separate powers is set to go into force in June 2005, exactly one year after its promulgation by the Emir.
- The new constitution should minimize the risk of a disputed succession.
- Nevertheless, reforms are slow and the institutions for a better functioning market economy are lacking.
- Adept foreign policy, including a defense agreement with the U.S., should ensure Qatar's security from external threats.

New constitution lays the foundations of a modern state.
Executive power is concentrated in the hands of the Emir, Sheikh Hamad bin Khalifa al-Thani, who is aided by one of his brothers as prime minister in a cabinet comprised of members of his clan and other prominent clans. To ensure continued political stability and modernize the institutions of the state, the Emir ratified a new constitution on June 8, 2004. This established greater representation of the population in governing institutions--notably through a fully-fledged parliament--and set guarantees on civil rights and the freedom of individuals, and the basic principle of a market economy.

Legislative power will be vested in a Shura Council made up of 45 members, two-thirds of whom would be elected and the rest appointed by the Emir (compared with 100% appointees until now). Originally planned in 2004, Qatar will have its first parliament by 2005. This new constitution, along with greater independence for the judicial system, will strengthen the quality of Qatar's governance and enhance its transparency, but the extent of change will depend crucially on the powers conferred on the parliament.

Institutional shortfalls.
Despite very good progress toward political liberalization, notably compared to other GCC countries, the process of strengthening institutions is slow, particularly with regard to the challenges that face the

economy and the new constitution. In particular, Qatar still lacks a constitutional court, an electoral commission, and proper parliamentary infrastructure. One of the most important expectations from a parliamentary election is for the establishment of a commission headed by parliament to audit public finances, and in particular Qatar's foreign assets. A similar system already exists in Kuwait.

The constitution should minimize succession risk.
Since the recent nomination of the fourth son as the new heir, the Emir has decreased the risk of a disorderly succession. In particular, the new crown prince, Sheikh Tamim bin Hamad bin Khalifa al-Thani--unlike the previous heir, who was the Emir's third son--is in good health and is reportedly more in agreement with his father's reform-led policies.

The constitution will also enshrine the current system of succession and bolster the legitimacy of the new heir. This is important because, although the Emir is only in his fifties, there have been concerns about his health. The adoption of a constitution and the strengthening of the country's political and legal institutions are designed to mitigate the risk of a disputed succession and the extent to which this might affect the functioning of the government. In addition, the Emir has reached an amicable settlement with his father, who could return home.

External threats minimized by good regional relations.
Qatar's prosperity depends on the continued integrity of its oil and gas installations and the security of the shipping lanes through the Strait of Hurmuz. Its foreign policy, therefore, plays a crucial role in maintaining stability in the Gulf and in ensuring the State's security. Qatar has settled its border disputes with Bahrain, Saudi Arabia, and UAE. It also has cordial relations with Iran. The American military presence in Qatar grew significantly in 2002 when the U.S. relocated most of its forces there, from bases in Saudi Arabia. In addition to this, the Qatari authorities have strengthened defenses at the country's oil and gas facilities.

Economic Prospects

- Qatar has extremely large oil and gas reserves and is about to increase and diversify its energy exports substantially.
- Higher capital expenditure by the energy sector and the government will fuel private sector growth.
- The government will continue to encourage the growth of the private sector through privatization, the outsourcing of public services, and the development of industrial zones for small and midsize enterprises (SMEs).

Table 2 State of Qatar Economic and Financial Indicators								
	--Year ended Dec. 31--							
	2007f	2006f	2005f	2004f	2003e	2002	2001	2000
GDP (bil. $)	27.0	23.6	22.7	21.1	19.5	17.9	17.7	17.8
GDP per capita ($)	37,793	34,046	33,772	32,165	30,595	28,934	29,718	30,694
Real GDP (% change)	11.1	5.0	6.9	8.2	8.4	7.5	4.5	9.1
Of which oil-related GDP	0.8	2.8	2.9	5.5	4.5	2.2	(0.7)	5.4
Of which LNG-related GDP	35.4	6.2	15.3	21.8	27.7	0.9	19.3	66.5
Oil production (000 bpd)	848.8	841.8	818.6	795.6	754.4	722.1	706.8	711.8
Oil exports (000 bpd)	722.8	715.5	696.9	687.4	667.7	640.9	580.1	667.7
LNG production and exports (mil. tons)	33.2	24.5	23.1	20.1	16.5	12.9	12.8	10.6
Consumer price index (average; % change)	2.0	2.0	2.0	2.8	2.3	0.2	1.4	1.7
Monetary aggregate (broad money M2; % change)	15.8	15.8	15.8	15.8	15.8	11.8	(0.0)	10.7
Domestic credit to public sector and NFPEs (% of GDP)	39.0	40.9	38.9	38.6	38.4	32.5	28.5	27.8
Domestic credit to public sector and NFPEs (% change)	9.0	9.0	8.9	8.8	28.6	15.0	2.5	10.9
Real effective exchange rate (% change)*	N.A.	N.A.	N.A.	(7.9)	(8.7)	(0.5)	5.5	(16.2)
Qatar Central Bank refinancing rate (year-end; %)	N.A.	N.A.	N.A.	2.5	1.5	2.0	2.5	6.7

*Total trade weighted; a decrease means an improvement in competitiveness. bpd--Barrels per day. NFPE--Nonfinancial public enterprise. f--Forecast. e--Estimate. N.A.--Not available.

Economic structure.

Qatar's economy is based on the exploitation of its vast reserves of oil and gas and is expected to remain so for the foreseeable future. At 27.6 billion barrels, oil reserves will last for at least 80 years. Gas reserves of 915 trillion cubic feet (tcf) place Qatar third in the world in terms of this resource, behind The Russian Federation (BB+/Stable/B) with 1,659 tcf, and Iran with 942 tcf. At the current pace of gas production, Qatar's reserves could last for more than 200 years. The share of the oil and gas sector in nominal GDP averaged of 59% in 2002-2003, up from an average of 40% in 1995-2000, as a result of the strength of oil and gas prices since 2000.

Qatar's economy is still dominated by the public sector, which accounts for about 70% of GDP. Nevertheless, the state sector, itself dominated by Qatar Petroleum (QP; A+/Positive/--) and its subsidiaries, is efficient and profitable, and the economy is diversifying with rapid growth in construction, services, and petrochemicals and other downstream industries. The country's high per capita income is underpinned by the well-maintained competitiveness of Qatar's economy, which is based on cheap energy supply, low labor costs, flexible labor supply from abroad, and prudent macroeconomic policies.

Economic growth.

In 2003, production of crude oil averaged 720,700 barrels per day, increasing only marginally from 694,000 barrels per day in 2002, as a result of OPEC quota restrictions (see Chart 5). Overall LNG production and export is expected to increase sharply in the next few years (see Chart 6). The government is targeting output of 60 million tons per year (tpy) by 2010. This level of production would make it the largest LNG producer in the world. Several Heads of Agreements have also been signed, and if these should be transformed into Sales and Purchase Agreements, it is possible that the planned exports of more than 60 million tpy may be raised easily to about 70 million tpy (see Chart 6) by 2010. This would be easily absorbed by demand for natural gas that is expected to quadruple from now until 2020.

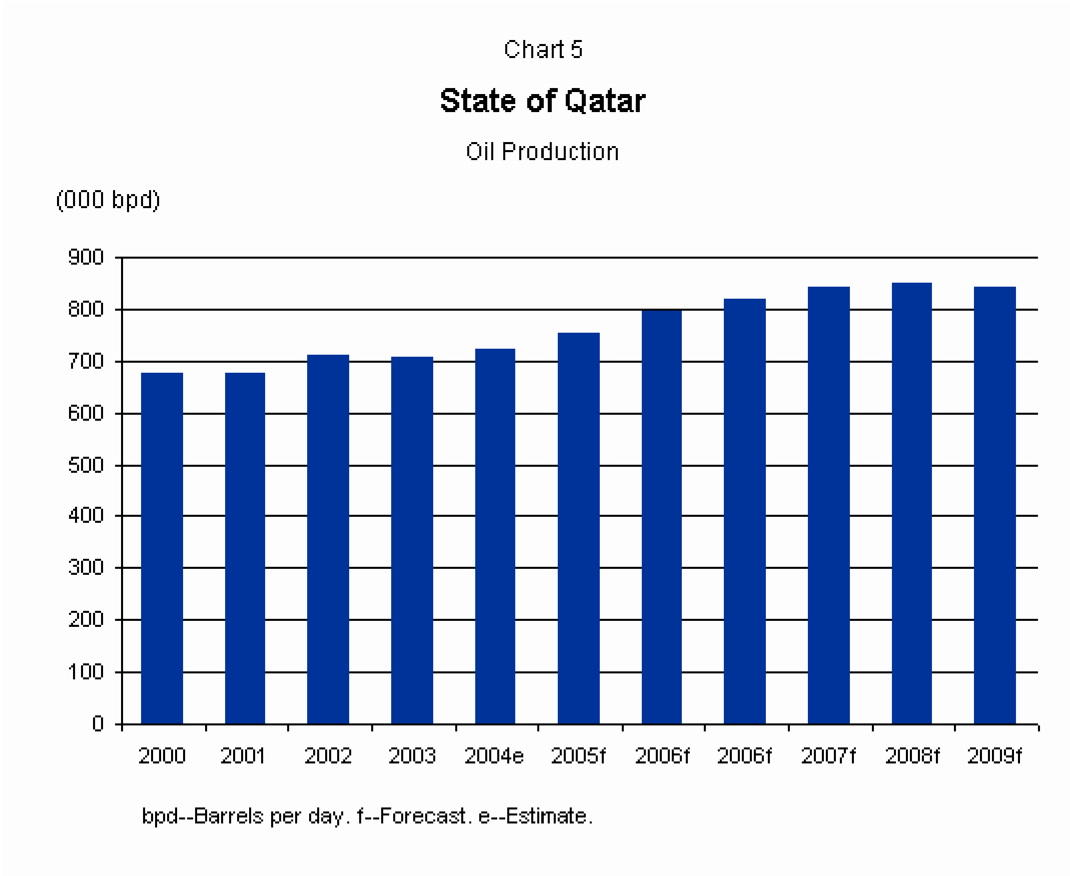
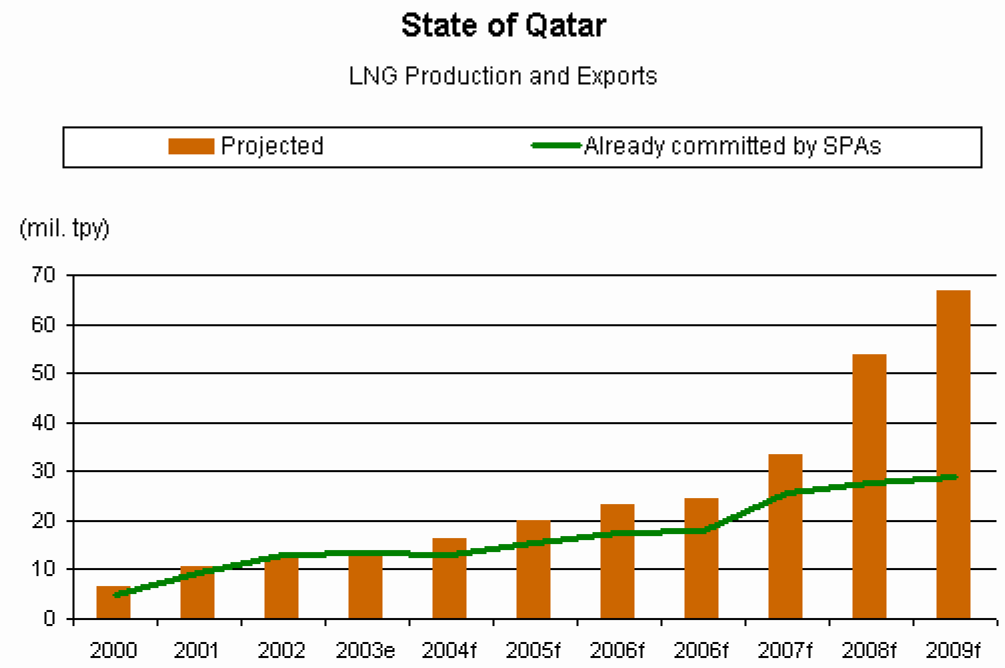


Chart 5
State of Qatar
Oil Production
(000 bpd)
900
800
700
600
500
400
300
200
100
0
2000
2001
2002
2003
2004e
2005f
2006f
2006f
2007f
2008f
2009f
bpd--Barrels per day. f--Forecast. e--Estimate.

Chart 6



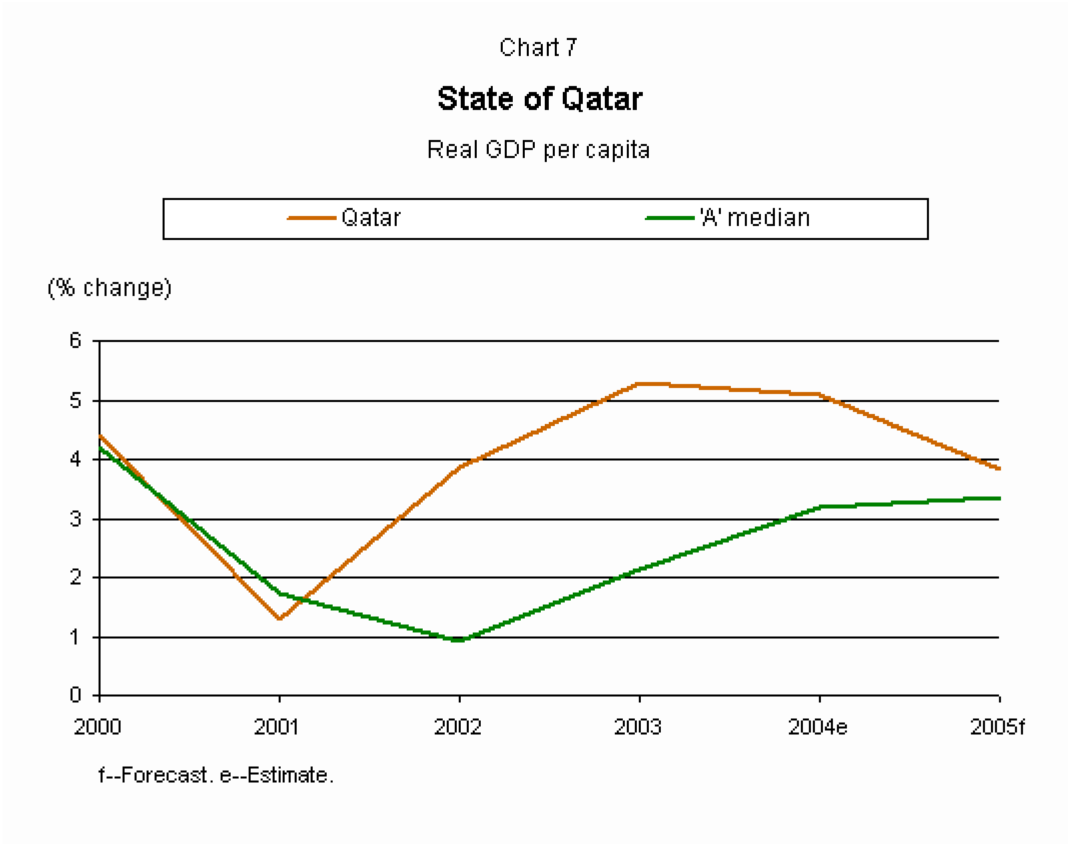
tpy--Tons per year. SPAs--Sales and purchasing agreements. f--Forecast. e--Estimate.

Moreover, whereas oil quotas exist to prevent oversupply and a fall in price, there is no such limitation on the production of natural gas. Finally, the production cost of gas production in Qatar is one of the lowest in the world and continues to decrease. Gas trains' capacities are constantly rising toward an expected 7.8-8.0 million tpy in 2008-2010, thereby increasing economies of scale. Condensates and petrochemicals, together with other associated industries such as construction, are also benefiting from the diversification program and will witness concurrent growth.

The economy will continue to diversify.

Qatar is aiming to be a world leader in the export of ultra-clean fuels such as diesel, naphtha, and liquefied petroleum gas, using new technology to transform gas to liquids. These products, which are sold as premium-refined products, will be marketed in Japan and Europe. Furthermore, the QP subsidiaries that produce petrochemicals have all significantly increased their production and exports.

Overall, the growth rate in 2004 is estimated at about 8.2% and forecast at more than 5.0% per year until 2007, reflecting the current boom in the gas sector, growth in the construction sector resulting from continued investment in oil and gas, and government infrastructure projects (see Chart 7). The private sector will also benefit from plans to reduce the size of the public sector through privatization, and from initiatives to promote SMEs and foreign direct investment.



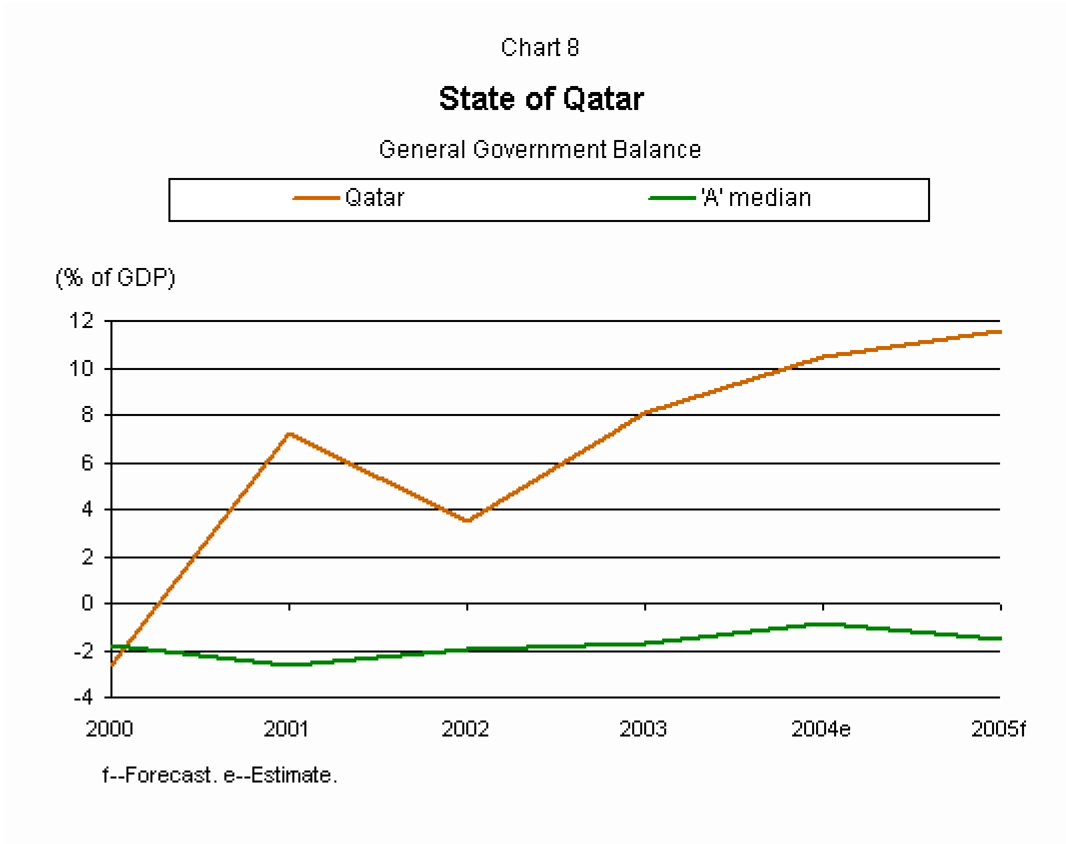
Fiscal Flexibility

- The government relies heavily on oil revenues, but prudent budgeting based on low prices and expenditure restraint minimizes the downside risks.
- The official presentation of the fiscal accounts understates their true strength by excluding foreign investment income and surpluses retained by QP.
- The government's domestic and undisclosed foreign assets make it a net creditor.

Table 3 State of Qatar Fiscal Indicators								
	--Year ended March 31--							
	2006/2007f	2005/2006f	2004/2005f	2003/2004e	2002/2003	2001/2002	2000/2001	1999/2000
(% of GDP)								
Public sector balance	13.0	16.0	17.6	17.0	15.1	11.1	15.0	5.8
General government balance	7.9	10.1	11.6	10.5	8.1	3.5	7.2	(2.6)
General government revenue	40.0	44.9	45.8	43.4	40.3	35.0	38.6	24.4
General government expenditure	32.1	34.8	34.2	32.9	32.2	31.5	31.4	27.0
General government debt (fiscal year)	33.3	40.1	43.9	50.2	54.6	52.5	59.1	48.8
(% of general government revenues)								
General government balance	19.9	22.6	25.3	24.2	20.0	9.9	18.7	(10.7)
General government interest	5.4	6.0	6.3	7.4	9.5	12.0	8.9	11.4
	--Year ended Dec. 31--							
(% of GDP)								
General government debt*	34.5	41.6	45.4	50.8	55.1	60.3	64.1	49.3
General government debt net of government deposits¶	14.4	19.1	22.7	27.0	30.2	36.3	40.0	34.9
Net general government debt	(123.2)	(127.1)	(117.2)	(110.0)	(101.1)	(97.3)	(85.2)	(89.6)
Public sector debt	76.5	88.1	91.3	98.3	106.8	113.4	123.0	103.4
Nominal GDP (bil. QAR)	98.1	85.9	82.8	76.6	70.8	65.1	64.6	64.6
*Adjusted for calendar year data. ¶General government debt net of deposits in the domestic banking system only. QAR--Qatari riyal. f--Forecast. e--Estimate.								

Revenue, expenditure, and balance performance.
Standard & Poor's expects Qatar's prudent fiscal policy to continue. The State has budgeted on the basis of conservative oil price assumptions and tight expenditure allocations. These may be relaxed in the course of each fiscal year for priority development programs, provided that oil prices turn out to be higher-than-budgeted. At the same time, the government is decreasing expenditure by contracting out public services such as education. This expenditure restraint is also planned in other ministries as part of an ambitious public sector development project, set out in an Emir's decree signed in 2002, which aimed at increasing the efficiency of public services.

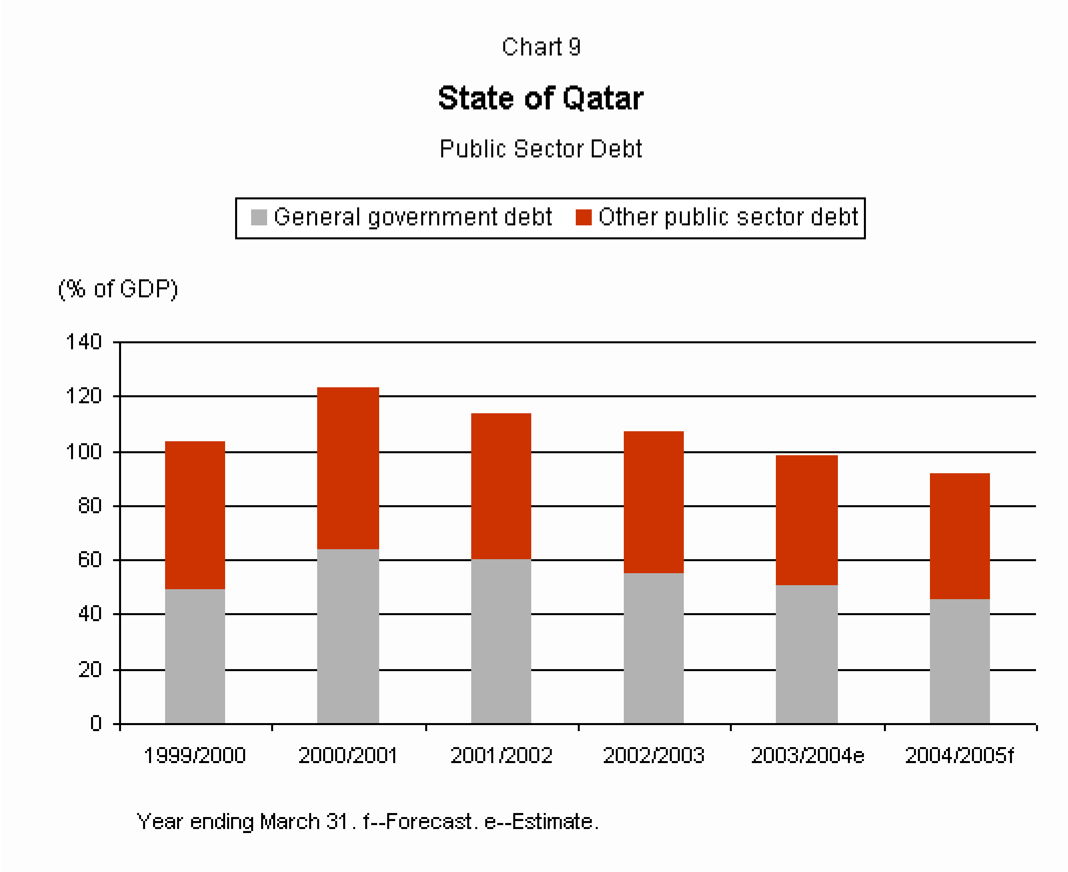
The budget for fiscal year 2004-2005 (ending March 31, 2005) assumes an average oil export price of $19 per barrel, an increase in investment income from the LNG industry, and higher spending, mainly on infrastructure projects such as schools, roads, the sewerage system, the Medical City, and other facilities for the 2006 Asian Games. The budget targets a deficit of about 2.5% of GDP, but based on a Brent crude price assumption of about $34.5 per barrel, Standard & Poor's projects a budget surplus of about 11.6% of GDP (see Chart 8). Consolidating the balances of the government and QP, Standard & Poor's projects the public sector to record a surplus of 17.6% of GDP in 2004-2005, compared with 15.0% in 2002-2003.



Government debt and interest burden.
The government holds a State Reserve Fund, which contains an undisclosed amount of foreign assets, estimated by Standard & Poor's to amount to at least $13.2 billion at year-end 2003. The government also has a Stabilization Fund, which was established in fiscal year 2000-2001 and has now reached about $1.1 billion. The government has formulated rules for using the Fund. The main principle is that the Fund would provide short-term loans to the budget in the case of a severe decrease in oil prices. As a remunerated financing facility, the Fund would stabilize the financing of the budget and would have to be repaid as a priority. This will prevent any risk of an erosion of creditworthiness due to increases in debt, because these budget credits would automatically be granted from the Fund.

Other government external assets include the assets of the Qatar Foundation ($ 1.7 billion at March 31, 2004), which was established by the government in 2001-2002 to develop the education system in partnership with the private sector. In addition, the general government's total deposits with domestic banks are estimated at about $5.0 billion. Finally, the government has other substantial domestic assets, which currently include equity in QP worth about $5.5 billion, equities listed on the Doha Securities Market (DSM) of $6.0 billion, and equity in various unlisted companies. The government has recently sold the Qatar Steel Company steel plant to QP, and this facility was then added to the portfolio of the new holding company Industries of Qatar (IQ).

The government's borrowing follows multiple objectives.
General government debt has declined in recent years to 50.2% of GDP at the end of fiscal year 2003-2004 (March 31, 2004), with a further improvement to about 44.0% of GDP expected for the end of fiscal year 2004-2005 (see Chart 9). The government's borrowing strategy includes raising funds when conditions are appropriate to build up a cushion of reserves and to create a yield curve with long maturities to act as a benchmark for project borrowing. By issuing US$700 million with an Islamic finance instrument (Sukuk) in 2003, the government implemented this policy and developed the Islamic finance market as well.



The government has also been refinancing part of its expensive syndicated bank loans. Its direct debt, external and internal, totaled $8.9 billion, or about 44.0% of GDP, at March 31, 2004, of which almost 53.0% was domestic debt. Its external debt comprises two Eurobonds, with the rest in the form of Sukuks ($0.7 billion) and medium-term syndicated loans. The last of these are mostly to finance equity contributions in gas projects. Interest payments on both domestic and external debt have declined to about 7.4% of revenues in 2003-2004 from their peak of 11.4% in 1999-2000, and should trend down to about 5.4% in 2006-2007 as the debt burden is reduced further to 40.5% of GDP. The State expects its gas, oil, and petrochemicals programs to cost about $54-$55 billion (about 260% of 2004 GDP) over the next decade. Although a large portion of this will be financed by the private sector, the government will not be able to finance its share from fiscal revenues alone, and will have to resort to borrowing. That said, given the expected private sector participation and QP's strong financial profile, the potential contingent liabilities for the government should be limited.

Off-budget and contingent liabilities

Qatari banks' nonperforming loans are low, estimated at a maximum of 8.8% of total loans in 2003, and are also adequately provisioned for. There is no deposit insurance scheme, although there has been an implicit government guarantee since the authorities fully bailed out depositors in a bank that failed in the early 1980s. Standard & Poor's estimates that, in the event of financial system stress, gross problematic assets in the banking sector could amount to 25.0%-40.0% of domestic credit to the nongovernment sector. The resulting contingent liability, however, is only 10.0%-16.0% of GDP. The public sector debt outside the general government is essentially that of QP and its subsidiaries and is not a contingent liability for the sovereign.

Monetary Policy

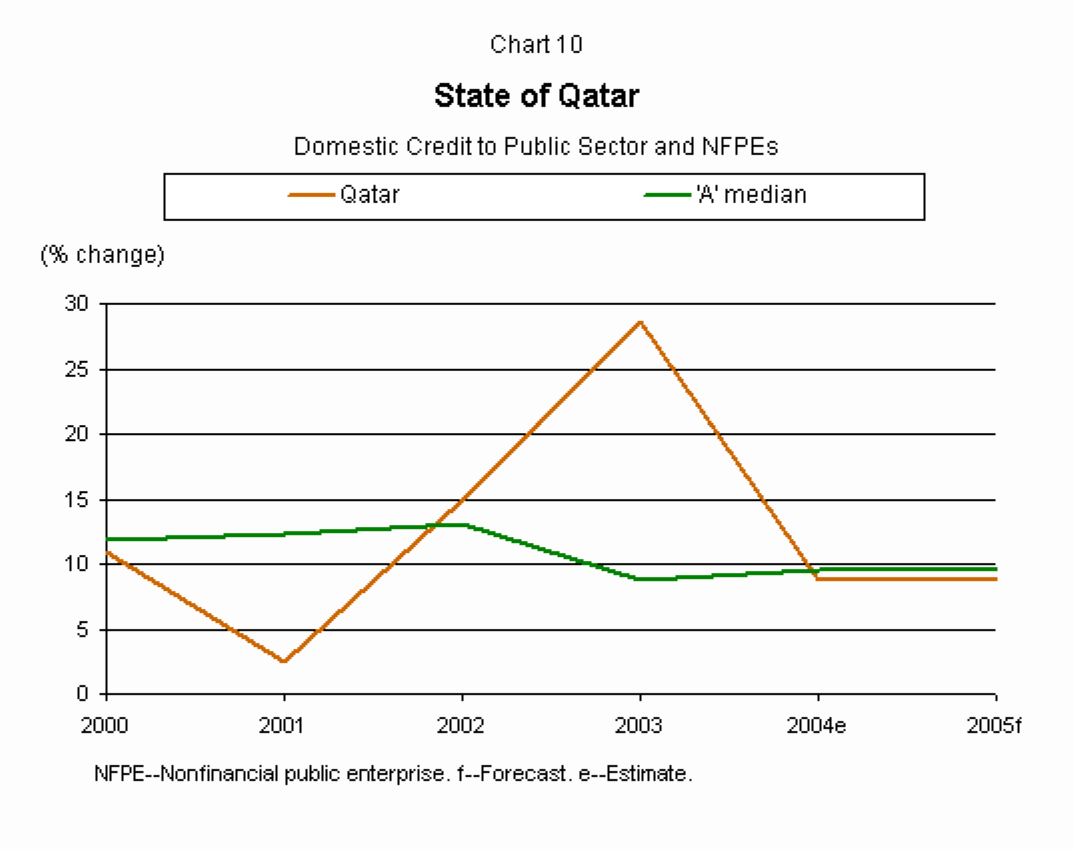
- The exchange rate peg to the U.S. dollar, supported by prudent macroeconomic policies, has served the country well in keeping inflation low.
- Qatar Central Bank (QCB), although passive regarding monetary policy, is developing market instruments aimed at increasing its liquidity.
- Financial intermediation is still modest.

A sustainable exchange rate policy.
The exchange rate for the Qatari riyal is expected to remain pegged to the U.S. dollar. This nominal anchor has served the authorities well in keeping inflation low, at an average of 1.6% per year in the past five years. The low rate of inflation also reflects the economy's high degree of openness to inflows of goods, capital, and labor. In the context of the pegged exchange rate and an open capital account, the Qatar Central Bank (QCB) is not in a position to pursue an active monetary policy apart from short-term liquidity management. Its role is confined to prudential regulation and supervision of the banking system, which includes several branches of foreign banks. Prudent macroeconomic policies, especially those maintaining fiscal discipline and a sound banking system in a environment of high capital mobility, ensure the sustainability of the longstanding peg to the dollar. A decision by GCC heads of state to form a monetary union with a single currency from 2010 should underpin exchange rate stability.

Moderate inflationary pressure in the short-term.
The increase of consumer price inflation to a still-moderate 2.3% in 2003 and expected 2.8% in 2004 is mainly due to a boom in the construction sector and the weakness of the dollar. The price pressures in the construction sector in 2003 started because of the high demand for construction materials and temporary lack of supply. Inflation is expected to return to about 2.0% in 2005-2007, however.

More active liquidity management.
Despite its passive role in monetary policy, QCB has tried to improve its liquidity management. To diversify its market instruments, QCB introduced a Qatar Monetary Rate in 2001 that allows the banks to borrow or deposit overnight funds with the QCB at fixed interest rates set on a daily basis. In 2004, the government announced that QCB's profits would no longer be transferred to the budget because the government is accumulating sufficient assets through the current surpluses in the budget. In addition to the increase in foreign exchange reserves coming from current account receipts (CARs), the government increased QCB capital and reserves by $1.0 billion in 2003 to $ 2.9 billion.

Stable but underdeveloped credit and capital markets.
Financial intermediation is still mainly limited to credits to the government, with total credit to the private sector and nonfinancial public enterprises representing only 38.4% of GDP in 2003 (see Chart 10). This, however, has grown rapidly from 21.0% of GDP in 2000. The DSM, created in 1995, is still small in terms of listings, capitalization, and turnover, but has no history of crashes or bailouts and is developing well. This trend is expected to continue with the privatization of high-value assets in the coming years. Equity and bond issuance by corporates is increasing and the market for government paper benefits from bonds with five-year maturities.

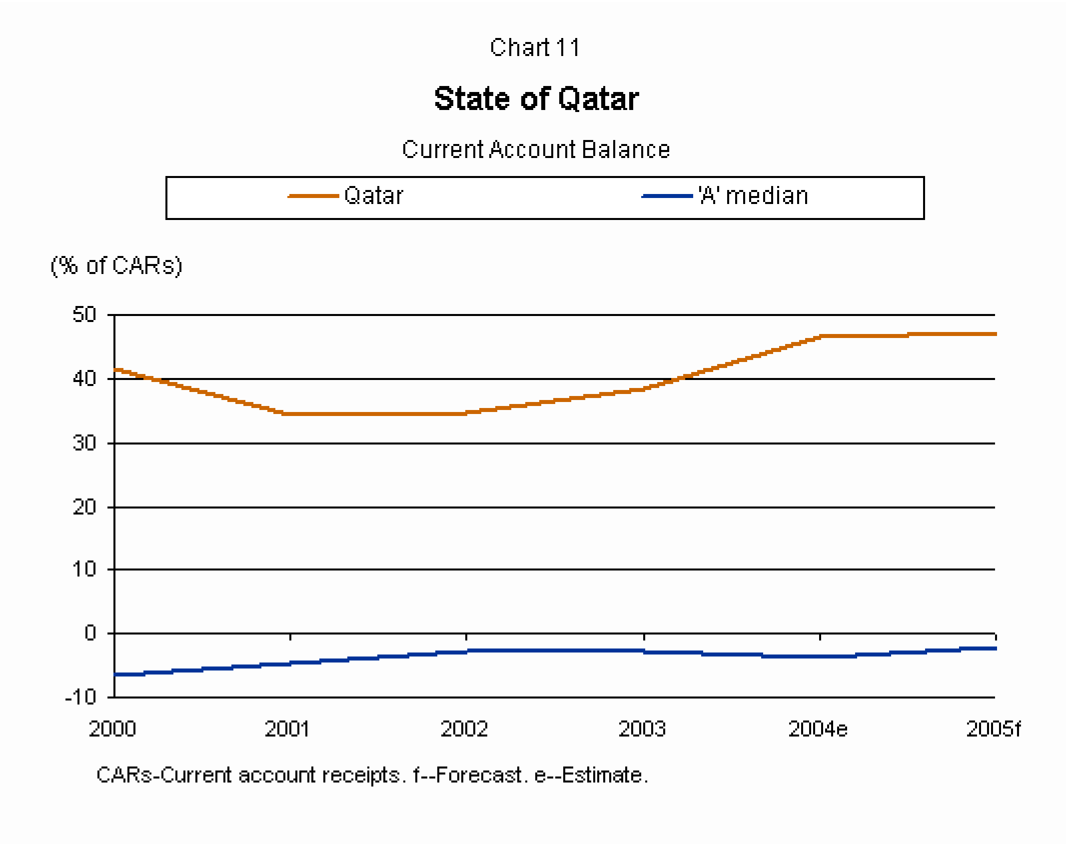


External Finances

- LNG exports should pick up and the current account balance should record surpluses of about 44%-45% of GDP in 2004-2005.
- Gross public sector external debt has declined in relation to exports and, on the basis of current contractual obligations, is projected to remain on a downward trend in the short term.
- The debt service ratio should also remain on a downward trend.

Table 4 State of Qatar External Indicators								
	'--Year ended Dec. 31--							
	2007f	**2006f**	**2005f**	**2004e**	**2003**	**2002**	**2001**	**2000**
(% of GDP)								
Current account balance	47.9	44.6	43.7	44.8	32.6	25.3	24.3	30.4
Trade balance	60.0	58.7	58.5	60.8	50.2	43.0	42.2	48.8
Total external debt	51.3	58.7	60.3	64.0	68.9	76.2	84.6	75.8
CARs	92.2	93.3	92.8	96.2	84.9	73.3	71.0	73.1
(% of CARs)								
Total external debt	55.6	62.9	65.0	66.5	81.1	104.0	119.2	103.7
Net external debt	(98.1)	(90.2)	(76.6)	(63.5)	(58.1)	(46.9)	(23.2)	(34.6)
Total public external debt	44.6	52.3	55.7	58.8	74.1	98.1	113.8	98.1
Of which general government external debt	13.8	17.2	19.8	21.8	25.8	35.2	37.9	31.0
Of which other public sector external debt	30.8	35.0	35.9	37.1	48.3	63.0	75.9	67.1
Net public external debt	(13.6)	(5.1)	3.3	12.0	26.2	50.6	68.9	57.5
Net non bank private debt	(13.1)	(12.7)	(12.5)	(12.3)	(7.0)	(4.2)	(20.7)	(11.3)
Net banking sector external debt	(37.5)	(34.2)	(29.2)	(25.1)	(26.0)	(26.3)	(20.5)	(19.9)
Debt service (excluding short-term debt)	7.0	8.2	7.6	9.8	12.3	15.9	7.9	22.7
Central bank reserves/imports (months)	6.8	6.1	5.2	4.3	3.3	1.9	1.8	1.7
Central bank reserves/external financing gap* (%)	(82.9)	(87.3)	(71.3)	(60.9)	(77.2)	(67.1)	(42.0)	(45.2)
CARs (mil. $)	24,870.9	22,021.6	21,111.5	20,254.6	16,517.6	13,101.6	12,596.8	12,990.3
*Current account balance plus amortizations plus short-term debt. f--Forecast. e--Estimate.								

External liquidity.
Exports of refined petroleum products, petrochemicals, aluminum, steel, and other energy-related commodities will increase, but Qatar's export receipts will continue to be highly sensitive to movements in the price of oil, and this will be an important source of continued volatility in the current account balance (see Chart 11). Another source of volatility is the level of capital goods imports for energy projects. Standard & Poor's estimates the current account surplus to have been about 32.8% of GDP in 2003 and forecasts even higher surpluses in 2004-2005 of around 45.0% of GDP.



As a result, Qatar's international liquidity position will continue to strengthen. The large projected current account surpluses will more than cover all projected loan principal repayments. International reserves are expected to continue to increase, by about $1 billion annually, in the next three years. Even assuming the same trend in current account payments, the coverage of reserves to these payments will reach a comfortable 6.8 months by 2007 from the 4.3 months expected in 2004. This represents a favorable level of international liquidity. In addition, the government is expected to increase its own foreign assets, which already exceed its foreign debt.

Public sector external debt.
Public sector external debt is export-related. Since 1997, exports have been increasing fast, and gross external public sector debt in dollars decreased slowly in nominal terms to about $13.4 billion at the end of 2003. As a percentage of CARs, the decrease was more significant: to 74.0%, from 167% in 1997. On the basis of current contractual obligations and planned new borrowing in the next few years, it is projected to remain on a downward trend. Taking into account liquid external assets, the net public sector external debt-to-CARs ratio stood at 26.2% in 2003, is estimated at 12.0% in 2004, and is projected to decline to 3.3% by 2005.

About $8.0 billion--or 65.0% of the total public sector external debt in 2003--was connected to the oil and gas industry and related downstream projects and is not guaranteed by the state or QP. Of this proportion, about $3.0 billion (38.0%), was in the form of structured debt, backed by either assets or future receivables, thereby limiting creditors' recourse to shareholders. Additionally, most of these projects are joint ventures with highly competitive Western oil companies with a strong interest in keeping projects on schedule and ensuring product delivery. Qatar's debt service ratio excluding short-term debt declined significantly to about 12.3% of CARs in 2003 and an estimated 9.8% in 2004, from 23.0% in 2000.

Private sector external debt.
Private sector external debt is limited to only a few sectors. Furthermore, at an estimated $1.6 billion in 2004, this is a negligible component of the $13.5 billion total Qatari external debt estimated for 2004. On a net basis, the private nonbank sector is in an asset position estimated at about 12.3% of CARs, and debt increases are mostly resulting from credit extended to Qatar Telecom, which is a highly profitable

company. In 2004, private banks are also in a net external asset position estimated at 25.1% of CARs, and are likely to remain in a healthy net asset position for the foreseeable future.

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