

Gulf states' partners will fear an extended war

A few states rely heavily on Gulf loans, investment and support that looks vulnerable if the war continues

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In the first ten days of July, no Gulf state invested in Pakistan's bond market while Bahrain withdrew USD30mn.

Pakistan, Egypt and Ethiopia are among a handful of states heavily reliant on support from Gulf Cooperation Council (GCC) states via loans, investments, currency swaps and remittances. The prospect of an extended US-Iran conflict, weakening GCC economies, underscores the vulnerability of those reliant on Gulf support.



The Central Bank of Egypt (Amir Makar/AFP/Getty Images)

What next

An extended, damaging war would increase the pressure on existing GCC support. Strategic investments will be less vulnerable than portfolio or bond investments, while currency swaps are likely to prove durable. Remittances will suffer if GCC economic activity stalls. The greater risk is that Gulf support will not be forthcoming if its partners need fresh assistance to offset the next wave of war shocks.

Subsidiary impacts

- For business, energy prices in emerging economies are likely to remain high this year, curtailing profits and undermining balance sheets.
- Institutional investors with exposure to Egypt and Pakistan are likely to face portfolio retrenchment if the Iran war becomes prolonged.
- Regional governments that rely on GCC economic support for political reasons could face challenges maintaining the level of this backing.
- A loss of GCC support could expose some of their partners to greater conditionality by international lenders.

Analysis

The impact of the Iran war has not hit emerging and developing economies (EMDEs) as hard as could have been expected. Forecasts have only suffered modest downgrades. The IMF's July 2026 World Economic Outlook sees EMDE growth in 2026 at 3.8%, versus a 4.2% forecast in January.

GCC sovereign wealth reaches EMDEs through sovereign wealth funds (SWFs), bilateral loans and bodies such as the Arab Coordination Group (ACG), a mainly GCC-backed group that deployed USD25.7bn in development capital in 2025, up 31% from 2024. However, there is a strong political element to this lending which renders it potentially vulnerable to shifts in priority, policy or sentiment.

Recipients

GCC capital is concentrated among a few recipients. The Kuwait Fund has granted Egypt 54 loans across the agricultural, transport, energy and water sectors since the ACG was established in 1975. The Saudi Fund for Development plans to give Pakistan USD6.5bn in 2026, including USD5.0bn in central bank deposits, making Riyadh Islamabad's biggest external financier.

| GCC capital support is often politically motivated

Egypt is heavily reliant on Gulf capital and central bank deposits to support its debt-laden economy ([see EGYPT: War will increase economic uncertainty – March 13, 2026](#) and [see EGYPT: External shocks will weigh on budget – June 17, 2026](#)). In recent years, the focus of support has been rebalanced, with less focus on aid and more on trade, investment and other forms of support. In February 2024, the UAE concluded a deal worth USD35bn to develop Ras al-Hikma into a tourist resort. In November 2025, Qatari Diar, the real estate arm of Qatar's SWF, announced it would invest USD29.7bn to develop an area on Egypt's northern coast into a tourist and residential project.

The UAE deal included a transfer of USD11bn into Egypt's central bank which was converted into a grant. Markets reacted positively to the news, with the Egyptian pound strengthening on the parallel market to EGP57:USD1 from EGP62:USD1.

Egypt also received a record USD43.1bn — a year-on-year increase of 31.2% — in remittances in the first eleven months of fiscal year 2025/26 (ending June 30), with much of it from workers in the Gulf. Cairo's external risk is now more tied to GCC goodwill and economic outlook than it was two years ago.

Ethiopia's GCC exposure is evolving from aid to trade and investment. The UAE had provided USD5bn in aid to 2023. Thereafter, it signed a series of agreements to build on existing investment worth USD2.9bn, mainly in sectors such as chemicals, food and beverages, aluminium and pharmaceuticals.

In July 2024, the two countries announced a currency swap with a nominal value of up to AED3bn (USD817mn) and ETB46bn (USD285mn). The deal aimed to boost bilateral trade while giving support to the Ethiopian currency. Nevertheless, Ethiopia is attempting to reduce reliance on GCC capital ([see ETHIOPIA: Reform progress will buoy the economy – January 23, 2026](#)). Earlier this year, it received USD13.1bn in investment agreements from China, India, Kenya, Poland and Singapore.

War impact

As the Strait of Hormuz crisis reignites, the fiscal position of GCC states will come under increasing pressure as export revenues fall and spending increases on security and infrastructure repairs, along with extra support for domestic businesses and households ([see IRAN/US: Escalation and talks see familiar constraints – July 15, 2026](#)). Governments could reprioritise external funding ([see GULF STATES:](#)

[Fiscal stimulus could be an option – July 20, 2026](#)). The likely impact will result in the GCC SWFs reducing their overall level of foreign investment, while seeking better returns. Economic aid will also come under pressure. However, deposits and currency swaps with central banks are likely to continue in the short term for political purposes.

Furthermore, remittance outflows from the GCC countries are set to fall in the near term as government spending plans are altered towards domestic welfare spending and projects aimed at increasing domestic employment and giving speedier returns. Countries such as Egypt and Pakistan are heavily dependent on remittances inflows.

| GCC support for central banks is difficult to replace

Some types of GCC support can be hard to replace, like-for-like. The IMF, World Bank and Western lenders usually attach governance and reform conditions, which take time to negotiate and can be politically costly.

In April 2026, Pakistan completed the repayment of USD3.5bn of central bank deposits to the UAE, at the insistence of Abu Dhabi. The repayment was probably a sign of the UAE's displeasure over Pakistan's closer ties with Iran and Saudi Arabia. Significantly, Saudi Arabia — sensing an opportunity to draw Pakistan closer — immediately replaced the UAE deposits. Meanwhile, Egypt has no real alternative to GCC deposits at its central bank.

Fiscal pressures in the GCC as a result of the Iran war could lead to less politically inspired support in the medium term, exposing Egypt and Pakistan among others to increased risks ([see PAKISTAN: Budget may suit IMF, without boosting growth – June 22, 2026](#) and [see PAKISTAN: Deal will help keep IMF programmes on track – January 9, 2026](#)). On July 17, the newspaper Dawn reported that no GCC state had invested in Pakistan's bond market in the first ten days of the new fiscal year (starting on July 1) and that Bahrain had withdrawn USD21mn from treasury bills and USD9mn from bonds.

Risks

GCC competition can be useful for some emerging states, as Pakistan's experience with Saudi Arabia in the wake of the UAE's funding repatriation underscores. However, the general dependence on GCC economies themselves facing shocks remains a risk factor.

Moreover, Gulf loans are generally priced in US dollars, or in GCC currencies pegged to the US currency. Currency depreciation on the part of a recipient makes servicing Gulf debt more expensive. Egypt experienced this between March 2022 and March 2024. A series of sharp devaluations resulted in the exchange rate deteriorating from EGP15.7:USD1 to around EGP49:USD1. This made Cairo's debt servicing significantly more expensive without taking on more debt.

The near-term path for Gulf capital will depend on how the present Strait of Hormuz standoff unfolds. Oman and Saudi Arabia have gained some upside from higher oil prices and lower export exposure, compared with Bahrain, Qatar, Kuwait and to a lesser degree the UAE ([see GULF STATES: Economic outlook is challenging – May 21, 2026](#)). If the GCC states suffer further infrastructure damage while

exports volumes fall, they will have more reason to keep capital at home. Egypt and Pakistan, two of their most prominent recipients, would be particularly exposed.