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The Saudi Arabian Economy

Policies, Achievements and Challenges

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CHAPTER 14

SAUDI ARABIA'S GLOBAL RELATIONS: GCC AND BEYOND

Overview

- Over the past three decades the Kingdom has **deepened its economic, political and military relationship with its immediate neighbors of the Gulf Cooperation Council (GCC).**
- More recently, under King Abdullah, Saudi Arabia has **expanded its economic and geo-political relationship with key emerging global economic powers, especially China and India.**
- At the same time, Saudi Arabia has tried to **maintain** friendly relations with long established western and USA trading partners.
- The GCC bloc remains a key strategic economic bloc policy for Saudi Arabia.

Table 14.1. Regional bloc membership competitiveness upgrading benefits.

<i>Business Environment</i>	<i>Macroeconomic policies</i>	<i>Political Institutions and Governance</i>
<ul style="list-style-type: none"> ▪ Improving efficiency and interconnectivity of transportation infrastructure ▪ Enhancing regional communications ▪ Creating an efficient energy network ▪ Linking financial markets ▪ Opening the movement of students for training or higher education ▪ Eliminating trade and investment barriers within the region ▪ Simplifying and harmonizing cross-border regulations, paperwork and visas ▪ Coordinating antitrust and competition policies ▪ Harmonizing environmental and energy standards ▪ Harmonizing product safety standards ▪ Establishing reciprocal consumer protection laws ▪ Opening government procurement within the region 	<ul style="list-style-type: none"> ▪ Coordinating macroeconomic policies ▪ Regional development banks – or Central bank. ▪ Coordinated capital requirements ▪ Coordinated monetary policy intervention or policy signed. 	<ul style="list-style-type: none"> ▪ Sharing best practices in government operations ▪ Creating regional institutions <ul style="list-style-type: none"> - Dispute resolution mechanisms - Harmonizing economic statistics ▪ Developing a regional position with international organizations ▪ Having one voice on international issues of importance to bloc.

Source: Adapted from Porter, 2010

The first milestone: the GCC

- On **25 may 1981** in **Abu Dhabi**, the **GCC** was formed encompassing Saudi Arabia, UAE, Kuwait, Qatar, Oman and Bahrain.
- **The objectives of the GCC were:**
 - To effect coordination and interconnection between member states in all fields.
 - To achieve unity between them.
 - To deepen and strengthen relations and cooperation between their peoples.
 - Formulating similar economic and financial affairs, agriculture, industry, commerce, customs, communications, education, culture, social and health, information and tourism.
 - Coordinated military and political affairs.

- Administratively, the GCC is managed through the Secretariat General, **headquartered in Riyadh.**
- This Secretariat is headed by a Secretary General who is appointed by the Supreme Council on a 3 year term, renewable only once.
- The Supreme Council is the GCC's highest authority and is composed of the member states.
- Since 1981, the GCC has evolved into a **powerful economic bloc with strong negotiating authority with other economic blocs such as the European Union.**
- There have been various phases of evolution of the GCC bloc since its establishment that reflects regional and international economic and political events.

The GCC in a “Snapshot” – economic and social indicators

- The six member GCC bloc **exhibit different economic and social characteristics** such as population, adult literacy, life expectancy, infant mortality and unemployment indicators.
- Saudi Arabia's GDP by far dwarfs the other GCC economies, representing 47% of combined GDP for 2008, followed by the UAE's 22% and Kuwait at 14%. Both Oman and Bahrain represent around 5% of the combined GDP.

(Contd....)

- In terms of **GDP per capita**, the highest level is for Qatar (\$ 65,000), followed by the UAE (\$ 43,000) and Kuwait (\$ 35,000). Saudi Arabia's GDP per capita was \$ 18,000, about the same level as Bahrain.
- In all the GCC countries, the **government sector** plays an important economic role.

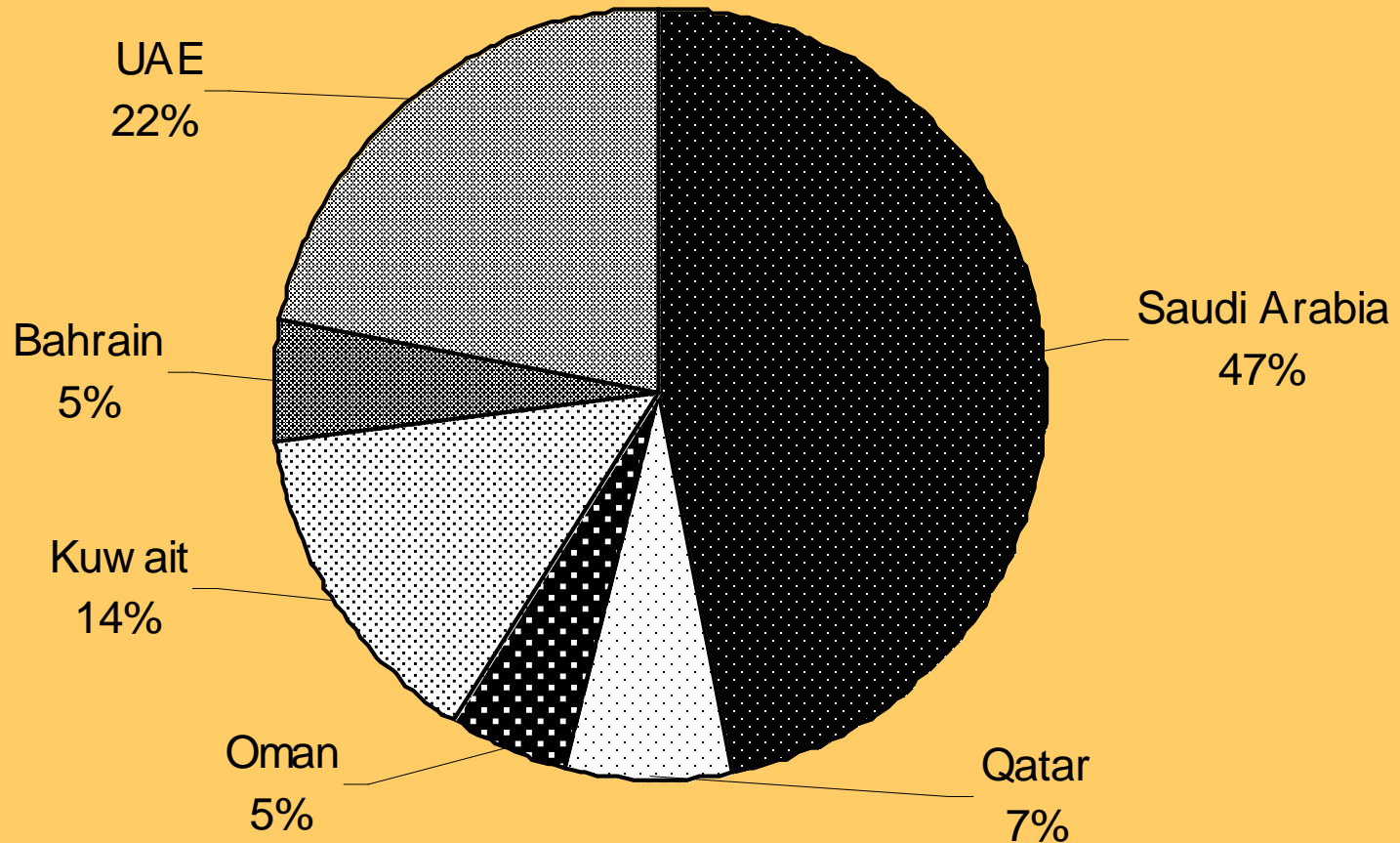
Table 14.2. GCC Countries: Population, Labour Force, and Social Indicators (1997 or most recent year)

	Bahrain	Kuwait	Oman	Qatar	Saudi Arabia	U.A.E
Demographic indicators						
Population (million)	1.1	3.4	2.9	0.8	24.2	5.6
Aged 0-14 (percent of total)	27.3	17.8	31.6	22.5	33.9	19.5
Aged 15 and over (percent of total)	72.7	82.2	68.4	77.5	66.1	80.5
Population growth (percent, 1997-2008 average)	2.0	3.10	4.7	6.0	2.2	4.9
Population gender ratio (men: women)	57:43	56:44	53:47	63:37	55:45	63:37
Age dependency ratio (1)	0.6	0.6	1.0	0.5	0.9	0.5
Urban population (percent of total)	90	97	32	94	82	92
Labour force indicators						
Total labour force (millions)	0.35	1.68	0.66	0.09	7.58	2.56
Male (percent of total)	76.8	77.6	75.3	69	84.5	86.5
Female (percent of total)	23.2	22.4	24.7	31	15.5	13.5
Labour force growth (percent, 1993-1999 average)	2.3	-1.6	5.2	3.9	3.3	3.9
Participation rate (percent)	54	49	25	52	33	46
Unemployment %	4.0	0.7	8.0	---	13.0	2.3
Social indicators						
School enrolment (percent)						
Primary	100	100	90	100	100	100
Secondary	100	100	65	99	95	75
Tertiary	30	30	15	40	35	35
Adult literacy rate (percent)	92	90	45	80	80	82
Population per physician	760	650	1200	667	749	1208
Access to safe water (percent of population)	100	100	85	100	93	98
Life expectancy at birth (years)	76	78	70	76	73	79
Infant mortality rate (per 1,000 live births)	19	11	18	18	20	16

Sources: *World Bank, Social Indicators of Development, UNDP, Human Development Report, Arab World Competitiveness Report.*

(1) Population under the age of 15 and over the age of 65 as a share of the total working-age population

Figure 14.1. Country share of total GCC GDP: 2008



Source: SAMA

Table 14.3: GCC countries: economic indicators 2008

	Bahrain	Kuwait	Oman	Qatar	Saudi Arabia	UAE
Nominal GDP (\$ billion)	18.5	148.8	53.1	104.6	468.8	239.5
Real GDP Growth (%)	6.1%	6.3%	6.2%	16.4%	4.4%	7.4%
GDP per capita (\$)	\$18,810	\$35,930	\$19,480	\$65,060	\$18,700	\$43,350
Inflation (%)	7.0%	10.8%	12.5%	15.1%	9.9%	14.0%
Imports (\$ billion)	14.6	26.1	16.7	21.2	100.6	116.6
Exports (\$ billion)	16.9	88.8	33.3	53.2	313.3	180.9
Current Account (\$ billion)	1.3	59.5	4.8	18.3	134.0	28.7
Government Balance (% of GDP)	2.7%	30.8%	4.2%	9.6%	33.6%	12.2%
Oil and gas reserves (Billion boe)	1.6	112.7	11.8	174.7	308.8	135.9
Oil sector (% of nominal GDP)	33%	55.8%	47.2%	62.1%	56%	34.4%
Net foreign assets (\$ billion)	3	295	23	100	403	272
External debt to GDP ratio (%)	157%	25%	16%	87%	23%	76%
Cross border foreign claims / GDP (%)	70%	21%	25%	51%	12%	67%
Ease of doing business (2009) (1=best, 178 = worst)	20	61	65	39	13	33
Global competitiveness ranking	37	30	38	31	35	37
Rating (S&P)	A	AA-	A	AA-	AA-	AA

Source: *GCC Central Banks, IMF, World Bank.*

Economic diversification and economic integration

- A key aspiration for many of the GCC economies that are dependent on the oil sector, is to **reduce their overwhelming dependence on oil revenues.**
- Some have argued that oil revenue is the “**glue**” that holds the GCC together and that a collapse in oil prices could put pressure on the bloc.

(Contd.....)

- All of the GCC states, except Bahrain, **have large oil reserves, and together account for around 45% of world oil reserves.** Saudi oil reserves are the largest, followed by Kuwait and the UAE while Qatar's gas reserves dwarfs all others.
- The contribution of the oil sector to the different GCC economies varies from around 80% for the UAE over the period 2003-2005, to 23% for Bahrain.

Table 14.4: GCC hydrocarbon indicators 2008

	<i>Bahrain</i>	<i>Kuwait</i>	<i>Oman</i>	<i>Qatar</i>	<i>Saudi Arabia</i>	<i>UAE</i>	<i>Global share %</i>
A. Proven oil reserve (Billion Barrels)	0.12	101.5	5.3	15.2	262.9	97.8	45%
B. National gas reserves (Billion cubic meters)	102	1,784	690	25,466	7,570	6,091	22.8%
C. Export of crude oil ('000 barrels/day)	0.1	1,738	592.7	703	7,321	2,334	20%
D. Gross oil exports revenues (\$ billion)	0.3	57.2	14.9	15.4	207.1	60.7	N/A
E. Contribution of the energy sector to GDP (%)	13.3%	78%	48.9%	55%	60.7%	35.8%	N/A

Soruce: GCC Secreteriat, OPEC, OAPEC, BP.

Table 14.5. Contribution of the oil sector to GDP 1977-2005

<i>Country</i>	<i>1977</i>	<i>1986-1990</i>	<i>1996-1998</i>	<i>1992-2002</i>	<i>2003-2005</i>
Bahrain	27	12.8	16.8	21.5	23.6
Kuwait	61	37.2	38.7	45.5	45.9
Oman	61	47.2	37.7	24.9	30.9
Qatar	68	34.7	38	35.3	29.1
Saudi Arabia	63	28.9	34.4	24.7	36.4
UAE	59	38.1	28.2	16.6	79.7

Sources: *ESCWA and the League of Arab States, Statistical Indicators of the Arab World for the Period 1970-1979*, ESCWA, *Statistical Abstract of the ESCWA Region*, 17th and 19th issues, 1999, GCC Central Banks Annual Reports.

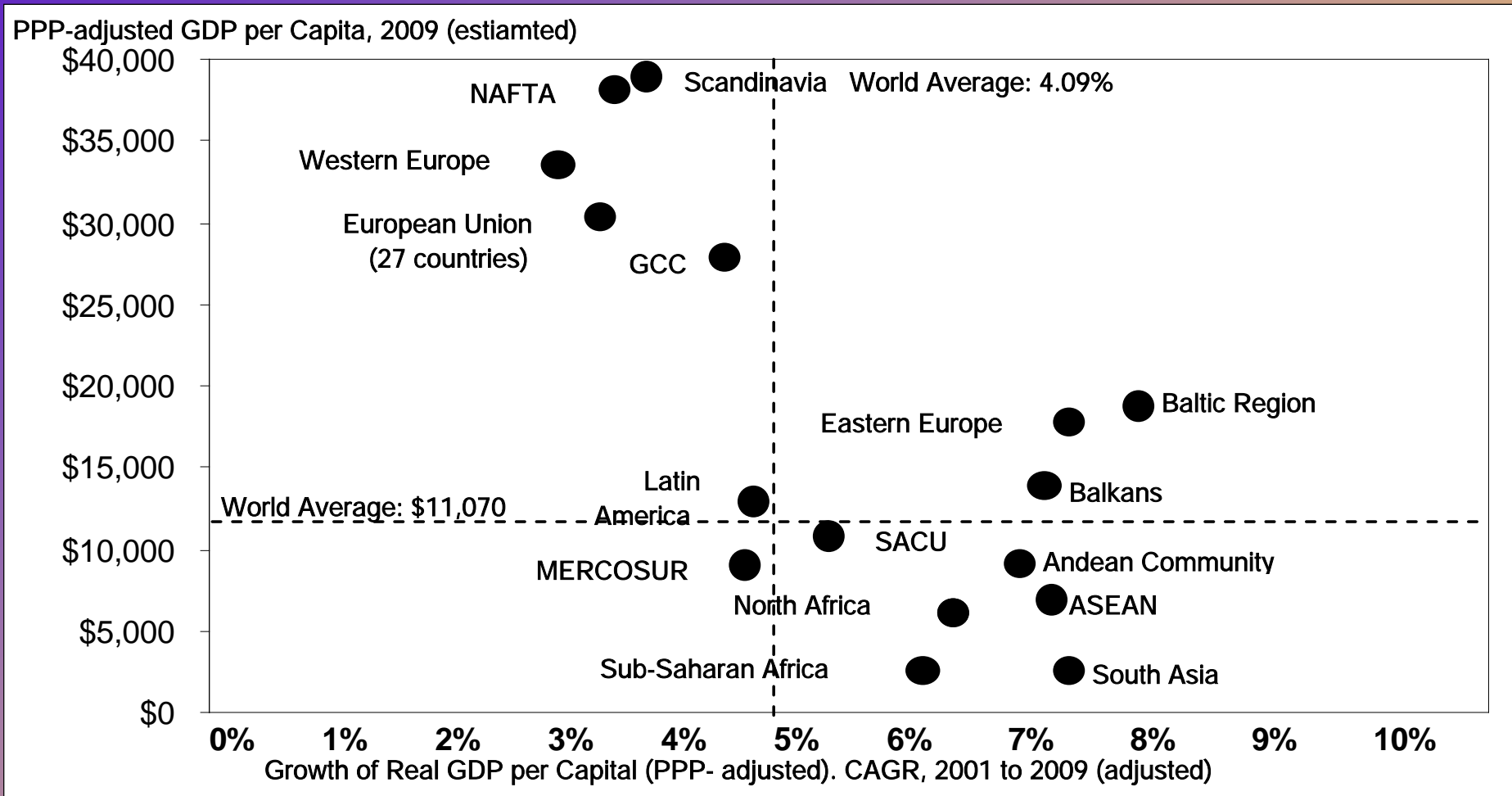
GCC comparative performance rankings

- In comparison with other regional trade blocs such as the **EU, North American Free Trade Association (NAFTA), Latin America**, the GCC bloc is below the EU in terms of growth of real GDP per capita adjusted for purchasing power parity (PPP).
- The GCC bloc does better against the Latin American and African blocs, as well as ASEAN (Association of South East Asian Nations) although ASEAN does not include China.
- One major ingredient to achieve growth in real GDP is through “***ease of doing business***” in a country and in this respect the GCC countries reflect differences.
- Saudi Arabia ranks the ***highest*** in terms of ease of doing business for 2009, compared with the other GCC countries.

Saudi ease of doing business

- The surprise Saudi ranking (13th World ranking against 20th for Bahrain and 33rd for UAE) is due to **some high rating in such factors as:**
 - Protecting investors, registering property, starting a business and getting credit.
- The more problematical areas for Saudi Arabia were in employing workers, enforcing contracts, closing a business and dealing with licenses.

Figure 14.2. Comparative performance of GDP growth rates for selected regional groupings (2001-2009)



Source: Porter, 2010, Economist Intelligence Unit, 2009.

Table 14.6. Ease of doing business: GCC countries 2009 rankings

<i>Country</i>	<i>Ease of doing business</i>	<i>Starting a business</i>	<i>Dealing with licenes</i>	<i>Employ. workers</i>	<i>Regist. property</i>	<i>Getting credit</i>	<i>Protect. investors</i>	<i>Paying taxes</i>	<i>Trading across borders</i>	<i>Enforcing contracts</i>	<i>Closing a business</i>
<i>Saudi Arabia</i>	13	13	33	73	1	61	16	7	23	140	60
Bahrain	20	63	14	13	22	87	57	13	32	117	26
UAE	33	44	27	50	7	71	159	4	5	134	143
Qatar	39	68	28	68	55	135	93	2	41	95	33
Kuwait	61	137	81	24	89	87	77	11	109	113	69
Oman	65	62	130	21	20	127	93	8	123	106	66

Soruce: *Global Competitiveness Report, Global Economic Forum, 2009.*

Diversifying the economic base: manufacturing

- Some progress has been made in the GCC to **diversify the economic base** into high value manufacturing.
- Analysis of value-added by manufacturing sector to GCC countries' GDP for the period 1980-2008, reveals that it ranges from 7-12% ,**with Bahrain having the highest, and Kuwait the lowest ratio.**
- The Saudi ratio for the period was 9.3%.

Table 14.7. GCC: Value added by manufacturing sector to GDP 1980-2008 (\$ billion and % of GDP)

Country	1980	1991	1998	2008
Bahrain	558 (18.0%)	517 (11.2%)	788 (12.7%)	1,705 (12.8%)
Kuwait	1,609 (5.9%)	536 (3.0%)	3,009 (11.9%)	5,866 (7.2%)
Oman	45 (0.8%)	390 (3.4%)	669 (4.7%)	2,566 (8.2%)
Qatar	410 (5.2%)	852 (12.4%)	718 (7.4%)	3,582 (8.4%)
Saudi Arabia	6,555 (4.2%)	9,559 (8.1%)	12,542 (9.7%)	29,522 (9.3%)
UAE	1,142 (3.8%)	2,661 (7.8%)	5,500 (11.8%)	16,663 (12.2%)

Source: *ESCWA, SAMA, UNDP.*

The GCC manufacturing base: by sector, investment and labor force

- The **GCC manufacturing sector** exhibits **wide sectoral diversification**, with chemical production, metal fabrication and food products accounting for around 61% of all sectors. Other significant sectors are building materials and wood and furniture.
- In terms of **investment made** into the manufacturing sector, the main investments have been in chemicals (55%), building materials (13%) and metal production and food (around 8% each).
- The **employment profile** of these industries reveals that metal fabrication employed 25% of the labor force, followed by 21% in chemicals, and 15% in building materials, although textiles accounted for 10%.

Figure 14.3: GCC manufacturing sector breakdown (2008)

(A) By different manufacturing sector firms

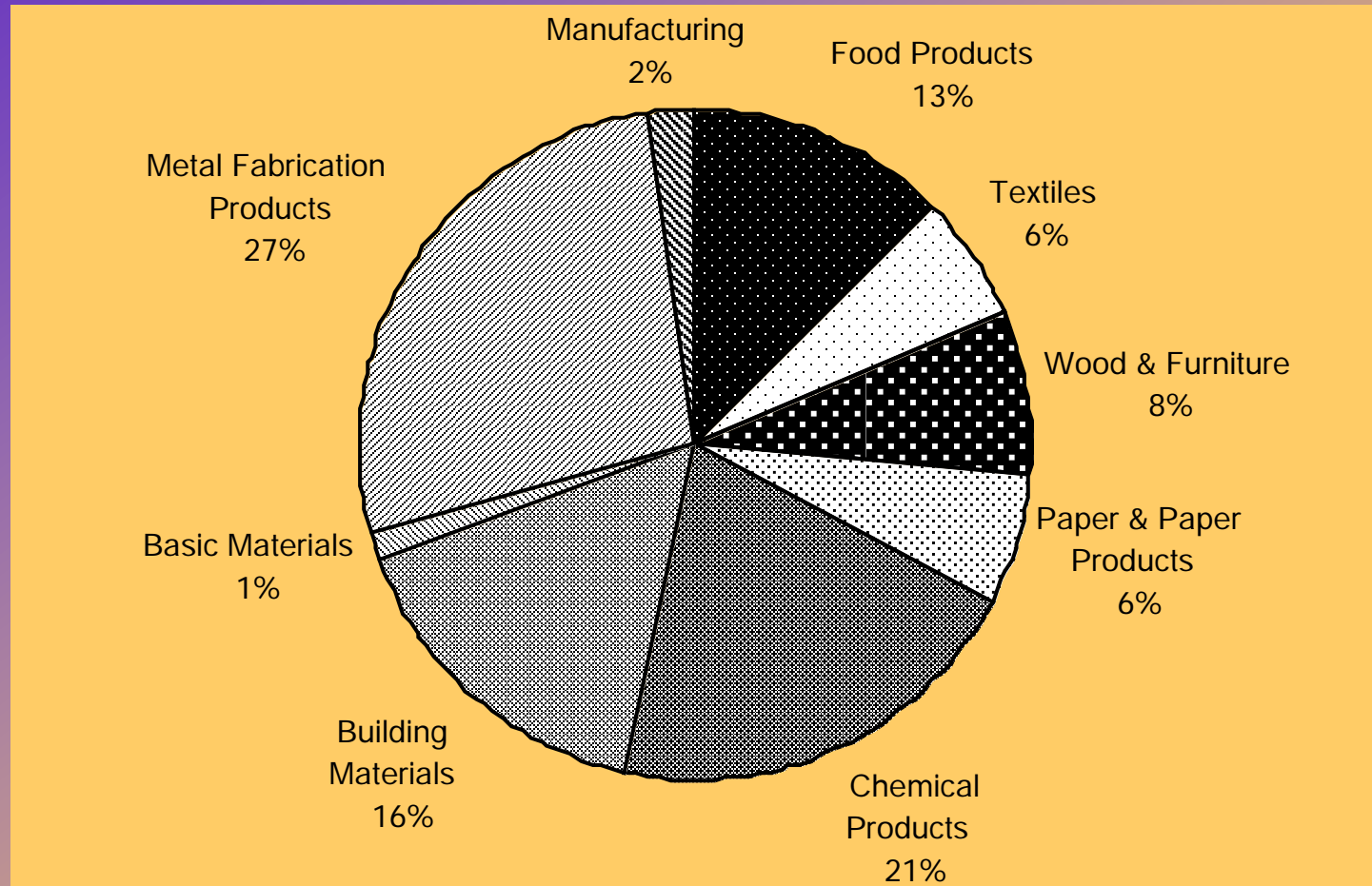
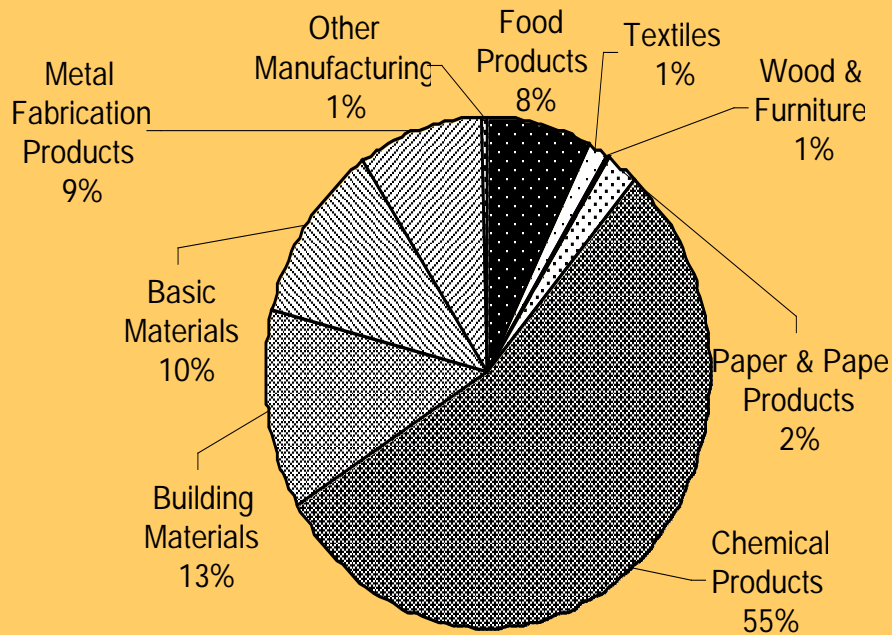
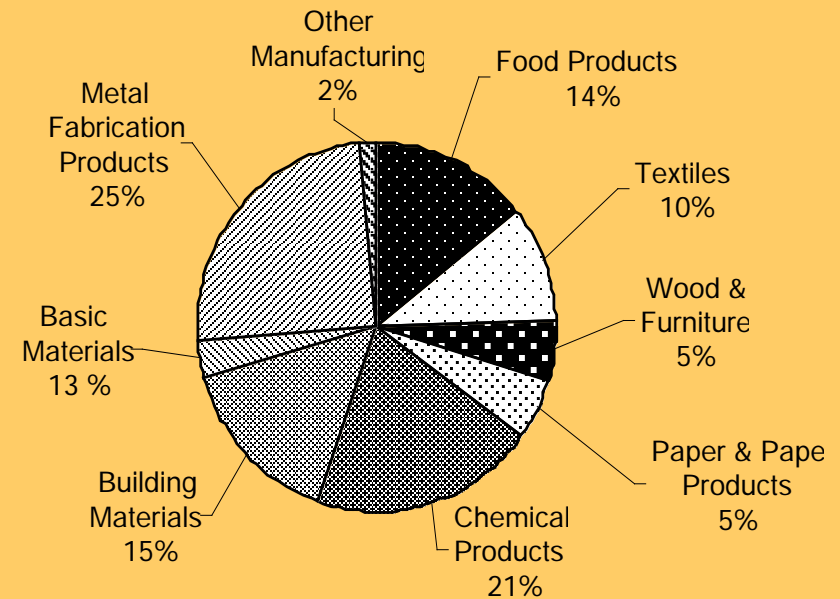


Figure 14.3: GCC manufacturing sector breakdown (2008) Contd....

(B) By Investment



(C) By Labor force

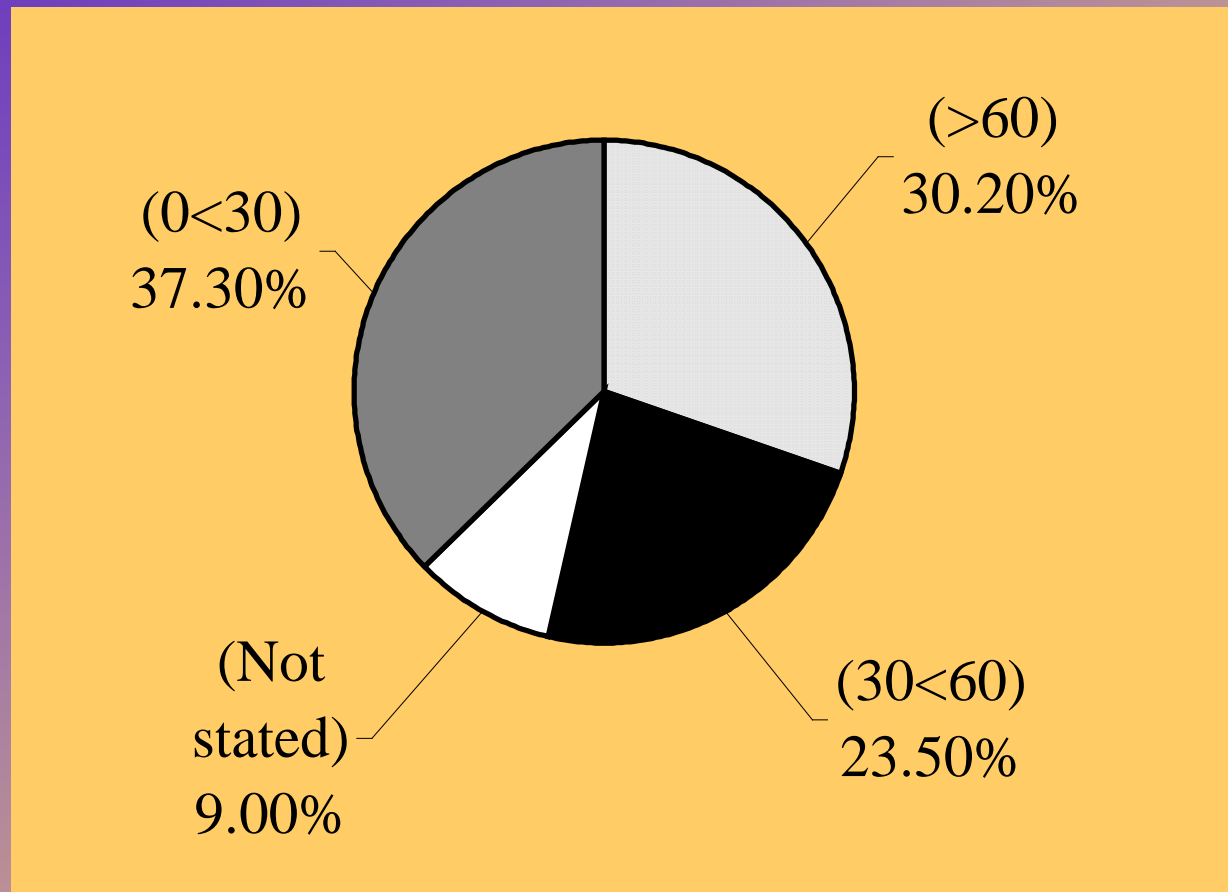


Source: GOIC, 2009

Majority of GCC manufacturing units employ few workers

- Breakdown of the GCC manufacturing units according to the distribution of the work force by different categories, indicates that nearly 60% of the labor force were employed in units employing **less** than 60 employees.
- Only 30% of manufacturing units employed more than 60 workers.
- The above indicates that throughout the GCC, the **importance of SME's (Small and Medium Sized Enterprises)** is evident.

Figure 14.4. Gulf Cooperation Council: % distribution of manufacturing firms according to size of work force (2007)



Source: Gulf Organization for Industrial Consulting, 2008.

GCC projects: construction and hydrocarbon sectors lead the way

- A breakdown of the **ongoing GCC projects** reveals that **construction** plays an important role in the number of projects, but **petrochemicals and oil projects** are important sectors, especially in Saudi Arabia, Qatar and Oman.
- The UAE has the majority of GCC projects as of 2009, valued at \$865 billion (or 45% of all project value), followed by Saudi Arabia at \$468 billion or 25%.
- Bahrain projects were the lowest valued at \$33 billion.
- Declining costs and new techniques in mining engineering have contributed towards reduced costs in exploration and production.

Figure 14.5. GCC Projects: Share by Country and Sector (2009)

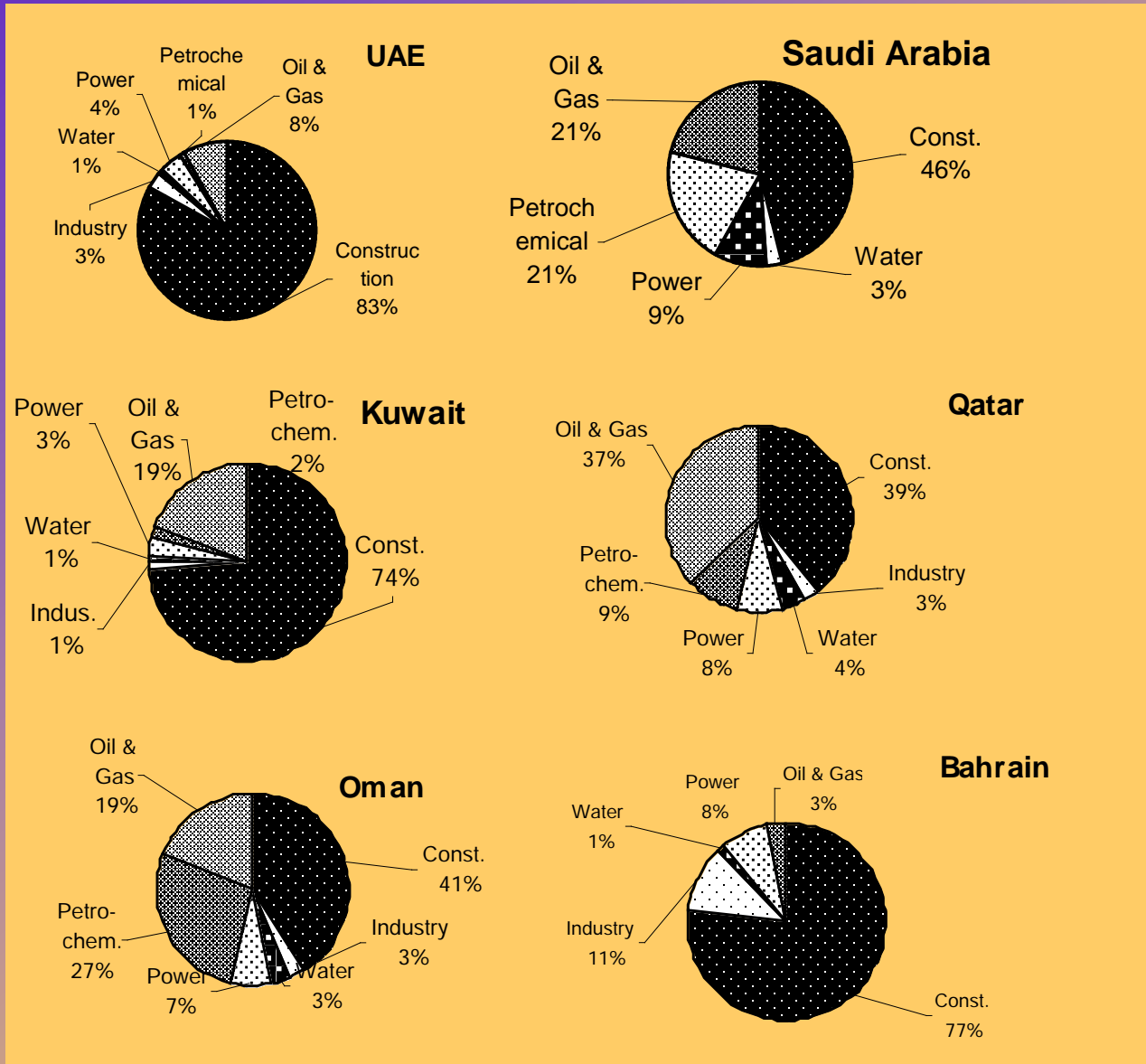


Table 14.8 Selected major upstream oil and gas projects in the GCC 2009

<i>Country</i>	<i>Project</i>	<i>Cost (\$ Million)</i>	<i>Scope of Work</i>	<i>Status</i>
<i>i. Saudi Arabia</i>				
•Saudi Aramco	Khurais Field Development	3,000	Full Field Development	Gas project.
•Saudi Aramco	Eastern Province Straddle Plant	1,100	Construction of 800 million cu. ft./day plant to handle NGL	Jacobs Engineering . In production
•Saudi Aramco	Haradh Gas Plant Expansion	400	Increasing capacity by 500,000 cu. ft/day	In production
•Saudi Aramco	Hawiyah Gas Plant Expansion	400	Increasing capacity by 800,000 cu. ft/day	Jacobs Engineering. In production
•Saudi Aramco-Total	Refinery. Jubail	10,000	Refinery capacity 400,000 b/d to process Arabian heave crude	2013 commissioning of plant.
•Saudi Aramco-Sumitomo Petro Rabigh	Petro-Chemical	10,000	World's largest integrated petrochemical complex	Ethylene/propylene contractor-foster wheeler ethylene process technology show stone & Webster operation since 2008.
•Saudi Aramco	Ras Tanura refinery/ petrochemical complex	N/A	Upgrade of existing refinery capacity by 400,000 bpd and build new petrochemical complex	At FEED stage, completed 2009. Production 2013.
<i>ii. Qatar</i>				
• Qatargas II	Trains 4 & 5	12,000	Two trains of 7.8 million tons/year each	Chiyoda doing downstream feed, while McDermott upstream. First gas production in 2008
• Rasgas III	Trains 5 & 6	12,000	Two trains of started 7.8 million tons/year each	Qatar Petroleum and Exxon Mobil. First gas 2008/2009
• QP/Royal Dutch/Shell	Ras Laffan GTL Plant	5,000	140,000 barrel/day	First production started 2008/2009
• QP/DEL	Dolphin Gas Pipeline.	3,500	120 km. Pipeline	Gas pipeline to Dubai operational.
<i>iii. UAE</i>				
• GASCO/ ADCO	NGL feed gas	2,300	Additional volumes of NGL/Gas	Tenders submitted
• ADMA/OPCO	Umm Shaif Gas Re-injection	1,200	600 million cu. ft./day GAS	Company selection
• ADNOC	District gas grid	380	Construction of new LPG train on Das Island	Chiyoda
• GASCO	Habshan gas expansion	350	350 million cu. ft./day train	Fluor Daniel

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iv. Kuwait

• KPC	Project Kuwait	7,000	Doubling oil production from fields to 900,000 barrel/day	International Oil Companies
• KOC	Flowlines replacement	800	Replacement of flowlines	Operational
• KOC	Water Disposal	150	Western oil fields	Operational

v. Oman

• PDO	Haweel Phase II gas injection	850	Construction of gas injection in seven fields	AMEC Operational
• PDO	48 inch loop	350	265 km. gas pipeline	Operational
• PDO	Kawther Field Development	250	Gas field development	New gas project

Source: *Middle East Economic Digest.*

The GCC financial sector: surviving the global turmoil

- Over the past decade, the **GCC financial system** has become more integrated with international markets.
- Several countries such as Dubai and Bahrain have established themselves as world financial centers, and Qatar and Saudi Arabia are also aiming to do the same with Saudi Arabia setting King Abdullah Financial City in Riyadh.

(Contd....)

- **Global integration brings both benefits and threats, as evidenced by the contagion of the global financial crisis of 2007/2008 and which affected Dubai.**
- **While there has been significant advances in the GCC financial markets, the overall financial system still lacks depth and diversification. Overall the six GCC countries have adopted an open economic system with free movement of capital and fixed exchange rate systems.**

Table 14.9 The Gulf Cooperation Council: exchange rate and capital restrictions

<i>Index</i>	<i>Saudi Arabia</i>	<i>UAE</i>	<i>Bahrain</i>	<i>Qatar</i>	<i>Oman</i>	<i>Kuwait</i>
<i>Exchange Rate Arrangement</i>						
Currency	<i>Saudi Riyal</i>	<i>UAE Dirham</i>	<i>Bahrain Dinar</i>	<i>Qatar Riyal</i>	<i>Omani Riyal</i>	<i>Kuwait Dinar</i>
Exchange Rate Structure	Unitary	Unitary	Unitary	Unitary	Unitary	Mixed currency
Classification	Conventional Pegged	Conventional Pegged	Conventional Pegged	Conventional Pegged	Conventional Pegged	Conventional Pegged
Exchange Tax	No	No	No	No	No	No
Exchange Subsidy	No	No	No	No	No	No
Forward Exchange Market	Yes	Yes	Yes	Yes	Yes	Yes
<i>Controls on Current Payments and Transfers</i>						
Arrangements for Payments and Receipts	No	No	No	No	No	No
Control on Payments for Invisible Transactions and Current transfers	No	No	No	No	Yes	No
Proceeds from Exports and/or Invisible Transactions	No	No	No	No	No	No
<i>Capital Controls</i>						
Capital Market Securities	Yes	Yes	Yes	No	Yes	Yes
Money Market Instruments	Yes	Yes	No	No	No	Yes
Collective Investment Securities	Yes	Yes	No	No	No	Yes
Derivatives and other instruments	Yes	No	No	No	No	Yes
Commercial Credit	Yes	No	No	No	No	No
Financial Credit	Yes	No	No	No	No	No
Direct Investment	Yes	Yes	Yes	Yes	Yes	Yes
Liquidation of Direct Investment	Yes	Yes	Yes	Yes	No	No
Real Estate Transactions	Yes	Yes	Yes	No	Yes	Yes
Personal Capital Movement	Yes	No	Yes	Yes	No	No
Provisions specific to commercial banks	Yes	Yes	Yes	No	Yes	Yes
Provision specific to institutional investors	No	No	No	No	No	No

Source: *World Economic Forum “Arab World Competitiveness Report*

Not all GCC central banks have the same operating instruments

- Despite having roughly similar foreign exchange regimes and capital controls in place, **not all the GCC central banks have used similar monetary policies.**
- Some have relied more on “**open market**” instruments to control money supply and interest rates.
- **With the exception of Saudi Arabia’s SAMA**, all the other GCC central banks support their commercial banks through overnight lending, discount window facilities or certificates of deposit.
- During the global financial crisis of 2007/2008 all GCC central banks **actively intervened** to provide liquidity injections and foreign exchange SWAPS, and also guaranteed commercial bank deposits.

Table 14.10 GCC central banks' main operating instruments

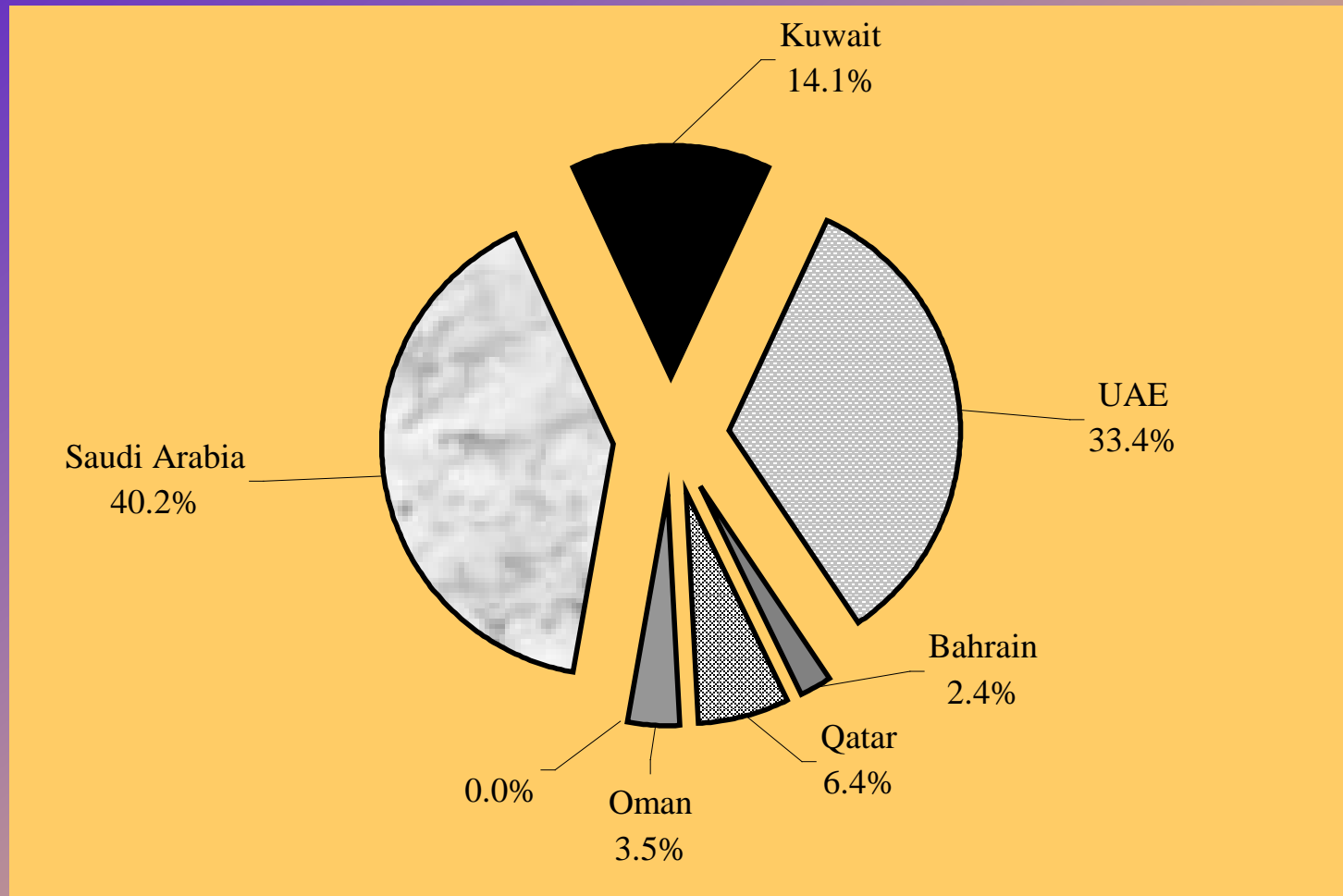
<i>Bahrain:</i>	Open market operations (purchase/sales of government securities, <i>repos</i> of government securities); open-market type operations (outright sales in the primary market); Central Bank lending operations (overdraft window, overnight lending)
<i>UAE:</i>	The UAE Central Bank relies mainly on purchases of foreign exchange and swap facility in Central Bank Certificates of Deposit
<i>Qatar:</i>	Same as UAE, plus a discount window facility
<i>Saudi Arabia:</i>	<i>Repo</i> operations in government and reverse <i>repos</i> for liquidity investments; foreign exchange swaps and government deposits with banks
<i>Oman:</i>	Mixture of FX purchase/sales and discount window
<i>Kuwait:</i>	Same as Bahrain; Central bank of Kuwait also has a “liquidity scheme” in the form of one month deposits with the Central Bank

Source: *Annual Reports, IMF*.

GCC banking sector

- The GCC banking sector is **a relatively new one** established since the 1950's, but today plays a vital development role in the GCC.
- In terms of GCC banking assets, **the Saudi banking sector dominates the other countries**, with over 40% of the total assets, followed by the UAE at 33% and Kuwait at 14%.
- In terms of **return on assets** Bahraini, Omani, and UAE banks outperformed the other GCC.
- In terms of **return on equity** Bahraini and Omani banks showed the best returns.
- The GCC banking sector is **highly concentrated** with Kuwait's 3 bank concentration ratio (ie the largest three banks in the sector) having a 78% concentration, 82% for Qatar, and 50% for Saudi Arabia.

Figure 14.6. GCC countries distribution of GCC banks private sector assets(2007): banking sector indicator



Source: GCC Secretariat, GOIC.

GCC capital markets

- **Equity markets in the GCC are expanding** as scope for private enterprises is increasing and demand for equity investment is rising.
- The **Saudi equity market is the largest in the GCC** in terms of capitalization, (\$ 333 billion as of June 2009 or 52% of the total GCC market capitalization).
- In all the GCC capital markets, the financial, telecom and industrial sectors are the primary sectors, but basic materials, consumer goods and services are also important players.
- In common with Saudi Arabia, GCC equity markets **exhibit few traded companies** and low turnover ratios, and foreign access is still limited.

Table 14.11. GCC stock market by capitalization , % of GDP, P/E ratios and sector weighting (June 2009)

	Stock Market Capitalization		
	<i>\$ billion</i>	<i>% of GDP</i>	<i>PIE*</i>
Saudi	333	90	16.2
UAE	102	47	9.3
* Abu Dhabi	68	52	9.2
* Dubai	34	39	9.5
Kuwait	93	93	13.4
Qatar	80	94	11.7
Oman	18	33	12.1
Bahrain	17	101	9.4
GCC	643	77	13.2

Sector Weight In GCC Stock Market Indices			
	Financials	Telecom	industry
Saudi	45.3	8	10.8
UAE	54.8	27.7	8
* ADX	43.9	39	5.5
* DFM	76.5	5	13
Kuwait	42.3	3.4	24
Qatar	71.4	0.0	25.9
Oman	51.7	9.5	23
Bahrain	79.2	14.6	1.8

Table 14.11. Contd.....

	Basic Material	Con. Goods	Con. Services
Saudi	23.9	4.2	3.9
UAE	1.7	0.8	3.4
* ADX	2.6	0.9	2.3
* DFM	0.0	0.0	5.5
Kuwait	3.7	5.1	10.9
Qatar	0.0	0.2	2.4
Oman	0.6	2.6	1.7
Bahrain	0.0	0.4	4.0

Source: *Bloomberg, CMA*

GCC debt market is expanding

- From 2007, the pace of **debt security** issuance in the GCC picked up, despite the global financial crisis.
- The GCC was also a prime issuer of **SUKUK** or Islamic bonds, mostly issued by UAE and Saudi Arabian prime government owned institutions such as **SABIC and the Saudi Electricity Corporation.**

Table 14.12. Top 10 Sukuk and conventional bond issues in the GCC 2007-2008

(A) Top 10 *Sukuk* issues.

Issuer	Sukuk	Country	Year	Issue (S mn)	Currency
Nakheel Dev. Ltd.	Ijarah	UAE	2006	3,520	USD
Ports Customs and Free Zone Corp.	Musharakah	UAE	2006	3,500	USD
Aidar Funding Ltd	Mudarabah	UAE	2007	2530	USD
Saudi Basic Industries Corp	Al istithmar	Saudi Arabia	2007	2,133	SAR
JAFZ Sukuk Ltd.	Musharakah	UAE	2007	2,043	AED
DP World Sukuk Ltd.	Mudarabah	UAE	2007	1,500	USD
Saudi Electricity Co.	ijarah	Saudi Arabia	2007	1,333	SAR
Saudi Basic industries Corp	Al Istithmar	Saudi Arabia	2008	1,333	SAR
Dubai Sukuk Centre	Mudarabah	UAE	2007	1,250	USD
Aider Sukuk Funding (No 2) Ltd	Ijarah	UAE	2008	1,021	AED
Saudi Electricity Co.	Ijarah	Saudi Arabia	2010	1,870	SAR

Table 14.12. Contd.....

(B) Top 10 Conventional bond issues

<i>Issuer</i>	<i>Industry</i>	<i>Country</i>	<i>Maturity year</i>	<i>Issue year</i>	<i>Amount (5 mn)</i>
DP World	Corporate	UAE	2037	2007	1748
TAQA	Corporate	UAE	2012	2007	1500
TAQA	Corporate	UAE	2036	2006	1500
RAS LAFFAN LNG 5	Corporate	Qatar	2020	2005	1400
Emirates Airlines	Corporate	UAE	2013	2006	1380
DP World	Corporate	UAE	2037	2007	1115
Dubai	Sovereign	UAE	2013	2008	1088
TAQA	Corporate	UAE	2016	2006	1000
ABU DHABI COM BK	Corporate	UAE	2010	2005	1000
TAQA	Corporate	UAE	2013	2008	999

Source: NCB Capital Research

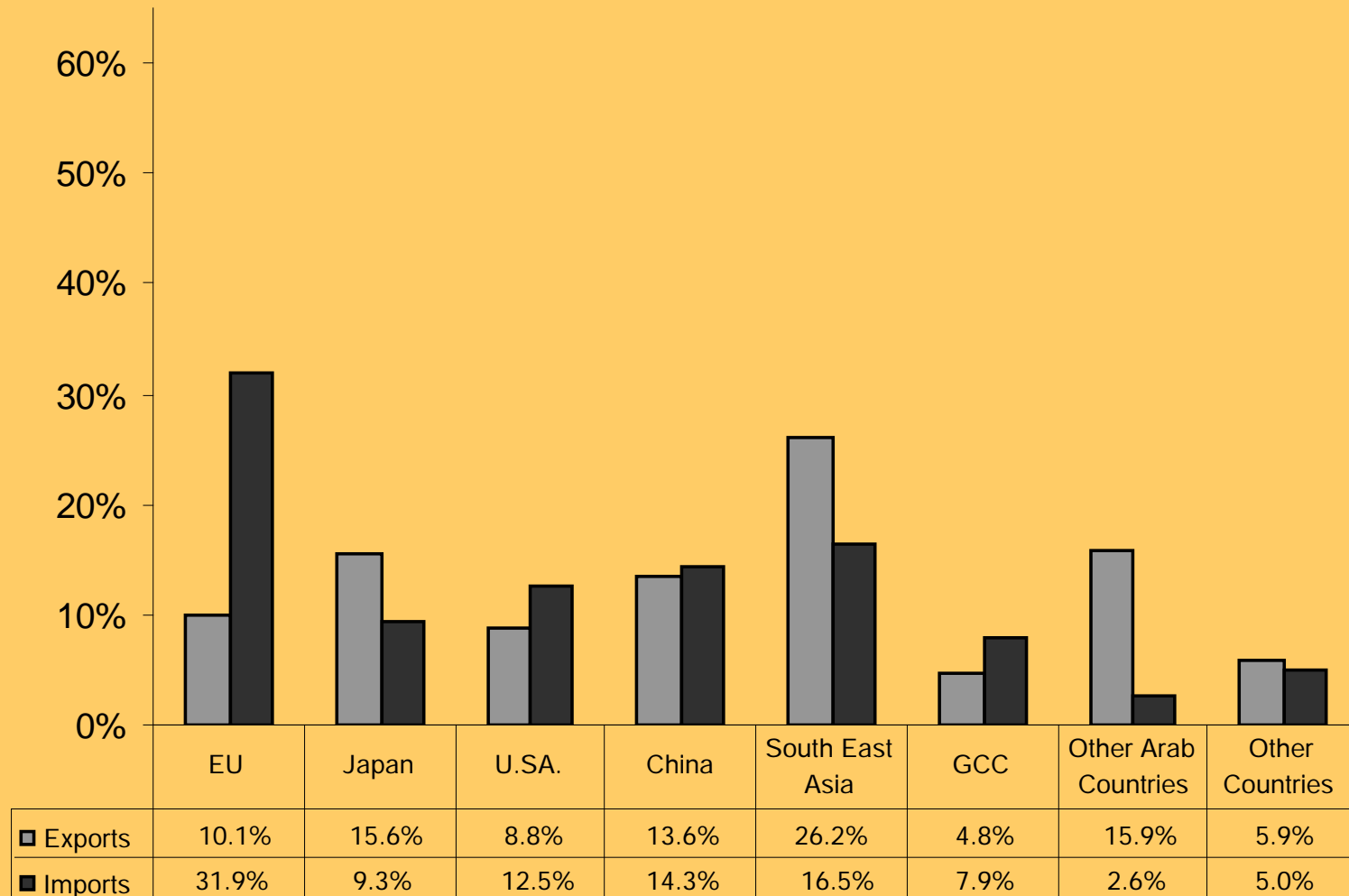
GCC capital market developments

- **The GCC capital markets are evolving but some further developments are required:**
 - A greater need for **effective disclosure** by local companies and a reliable data base and international accounting standards.
 - Strengthening independent regulatory authorities.
 - Deepening current stock markets by listing privately held and family owned companies.
 - Linking the GCC stock markets and cross-listing key stocks.
 - Establishing new specialist investment banks to provide stronger financial analysis and underwriting of share issues.
 - Continuing GCC efforts at economic and financial integration and monetary union.

GCC trade: non-regional bound.

- The trade composition of GCC economies is **“asymmetrical”** – exports are concentrated largely in crude oil and petroleum products, **while imports are more diversified.**
- This translates into the GCC being **vulnerable** to pricing developments in international commodity prices over which they have limited control.
- The **GCC economies are amongst the most open in the world**, with no foreign exchange controls, and relatively low tariff and quota protection.
- The current major export markets are Japan, China, South East Asia, the European Union, and the USA.
- The EU tends to dominate imports (32% of total) while South East Asia, China, USA and Japan follow in importance.

Figure 14.7 Geographical distribution of GCC foreign trade in 2007 (%)

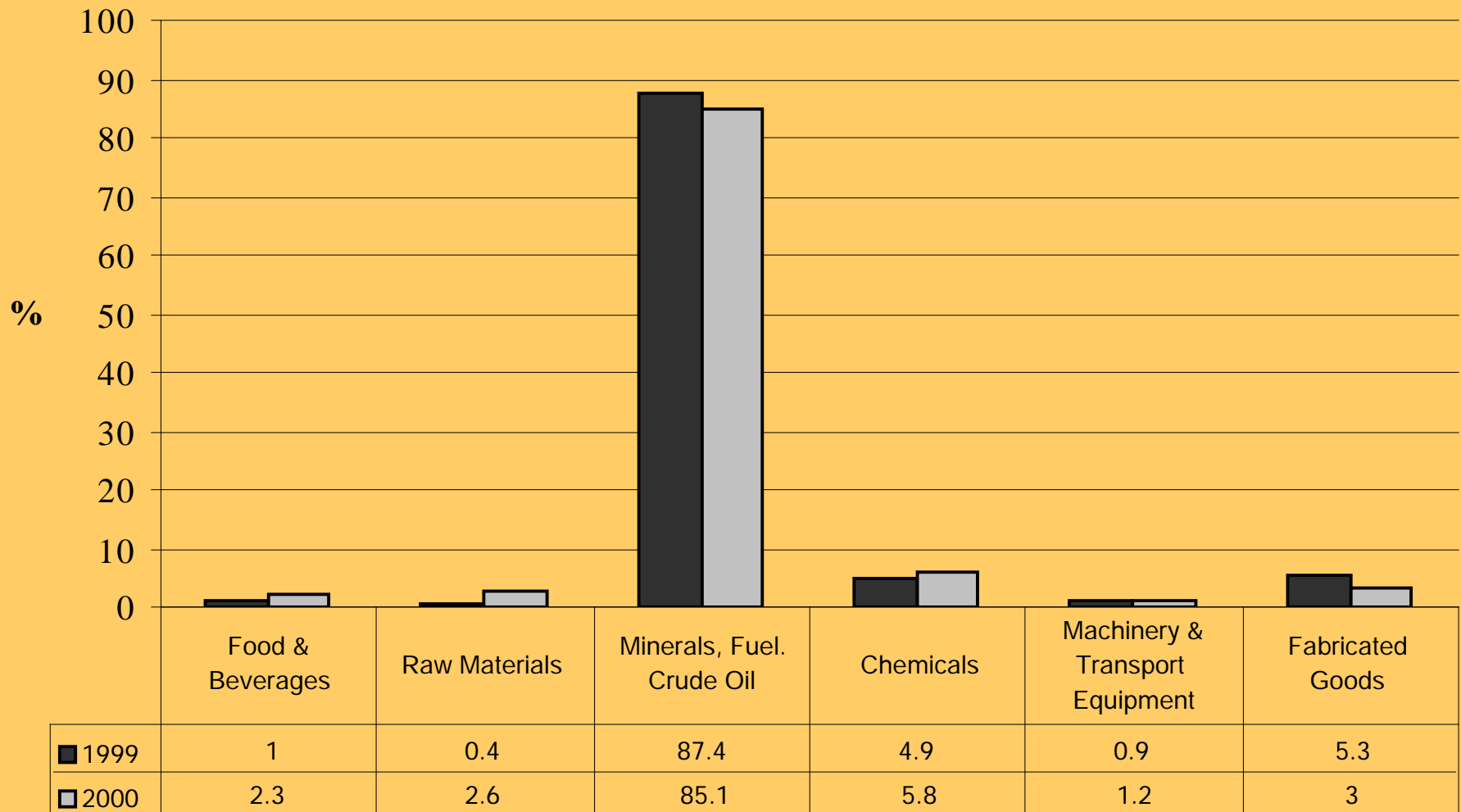


Source: Gulf Organization for Industrial Consulting

Lack of export diversification is worrying.

- There is a **lack of meaningful diversification in the pattern of GCC exports.**
- The minerals, fuel and crude oil sector are **over 80%** of total exports, with chemicals, fabricated goods and raw minerals accounting for around 10% of exports.
- Only Bahrain has a more diversified export clusters compared with the GCC countries.

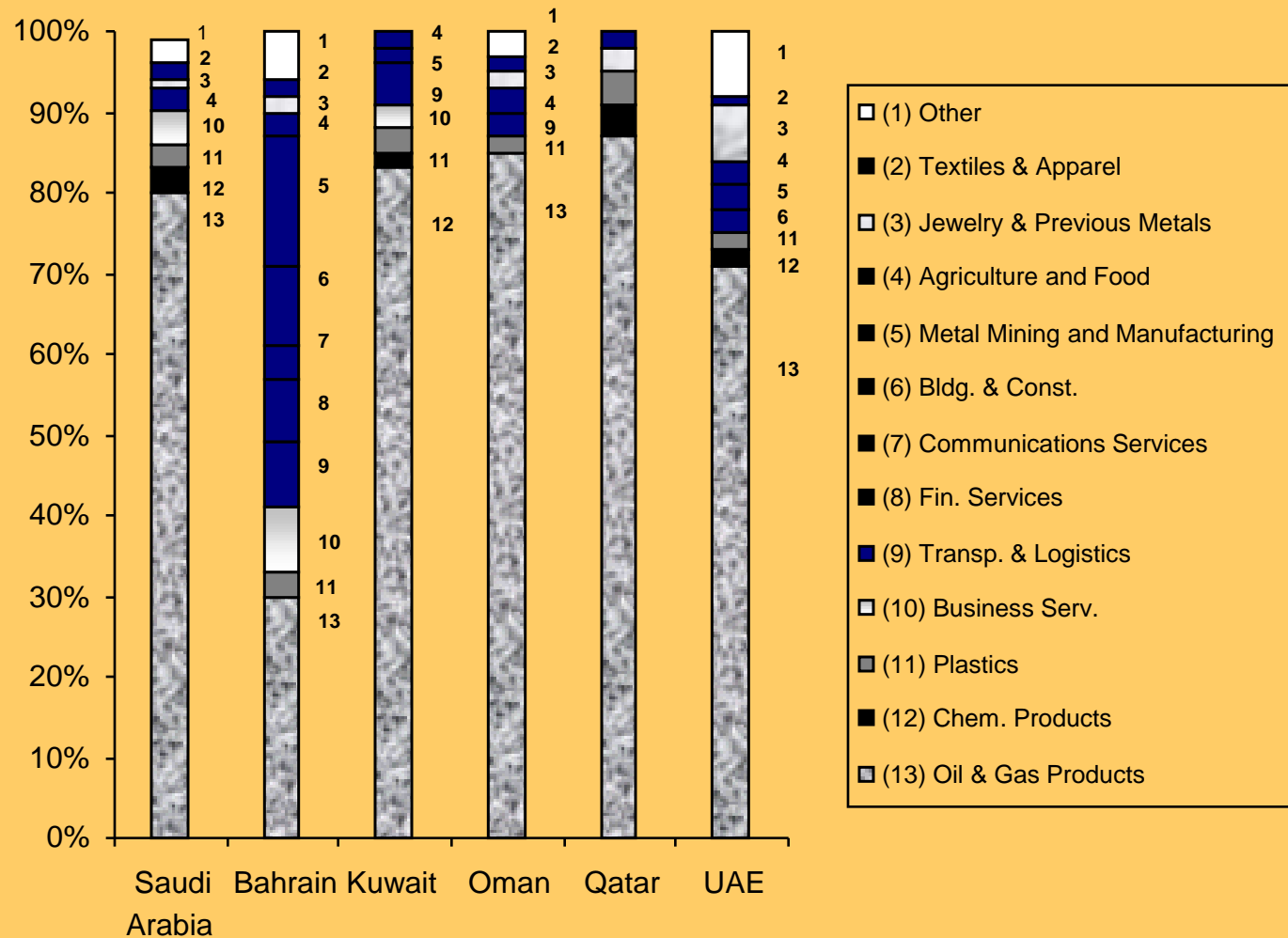
Figure 14.8 GCC commodity exports by major commodities (%)



Source: Gulf Organization for Industrial Consulting, 2002, 2009.

Figure 14.9. GCC: Share of total exports by broad cluster for individual countries (2007).

Export Share of Total



Source: GOIC, GCC Secretariat Riyadh

GCC demographics and the labor market.

- The **GCC countries** have one of the highest **population growth rates** in the world.
- The GCC also has a **large proportion of expatriates**, reaching around 67% for the UAE and Qatar, and 23% for Oman as percentage of the total population.
- The situation becomes even more **unbalanced** when the expatriate labor force is calculated as **percentage of total labor force**. The UAE's ratio rises to 92%, Kuwait 82%, and 68% for Oman. The Saudi ratio is around 51%.

Figure 14.10. GCC demographics and labour force (2003 or latest)

(A) Expatriate as percentage of total population

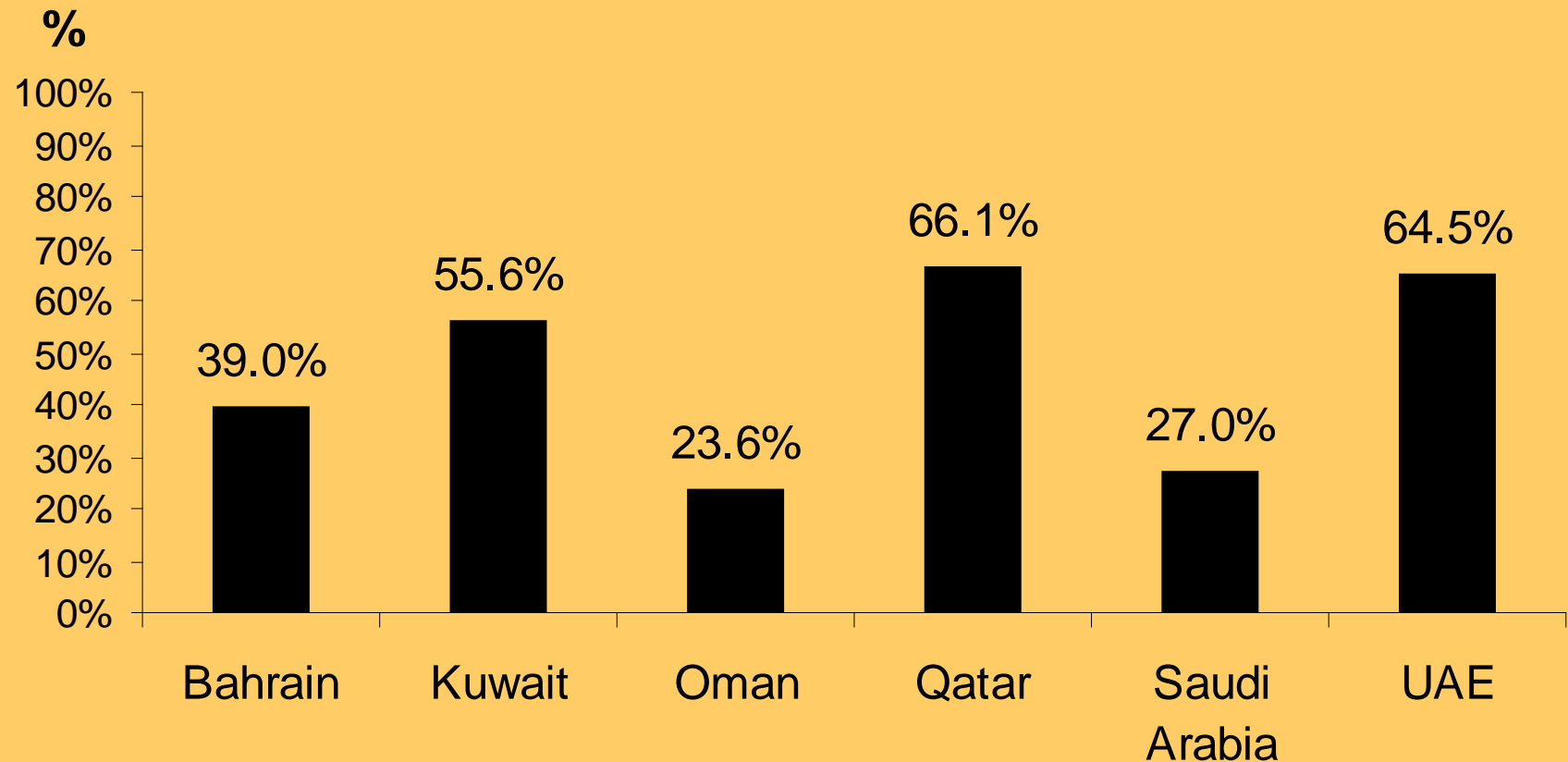
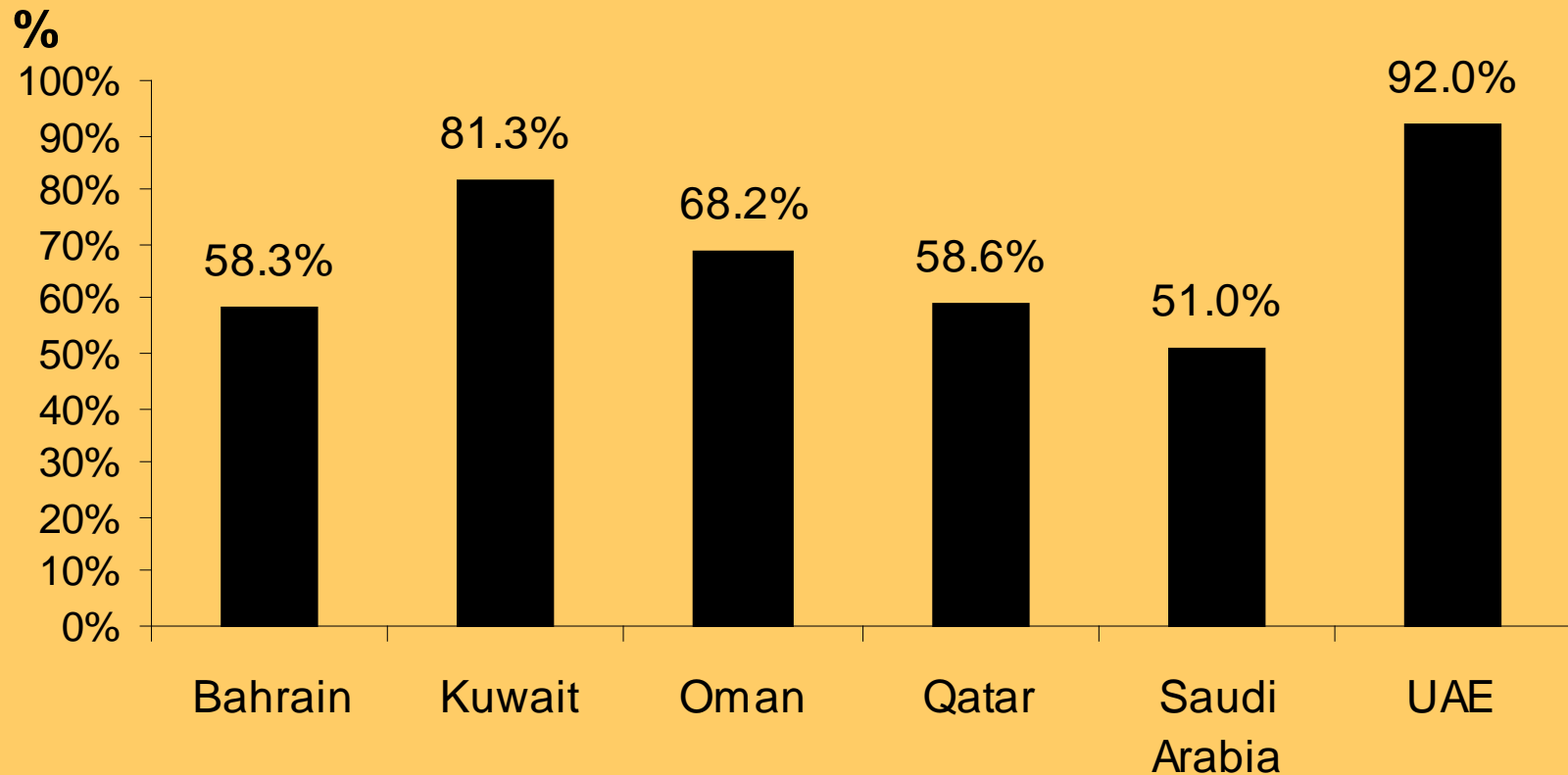


Figure 14.10. GCC demographics and labour force (2003 or latest)

(B) Expatriate labour as percentage of total labour



Source: World Bank, ESCWA, World Health Organization

GCC monetary union: a long and hard road.

- During the annual GCC summit of December 2001, the GCC countries signed an economic agreement that laid out some specific steps to achieve **Monetary Union by 1st January 2010.**
- The target date was not met, as **Oman opted** out in December 2006, and **Kuwait declared** that it would abandon the dollar peg in May 2007.
- In May 2009, the GCC rulers agreed to locate the proposed **GCC Monetary Council** (the forerunner of a GCC central bank) in **Riyadh.**
- This promoted the **UAE to withdraw from the GCC common currency in November 2009.**

GCC common currency – where next?

- Following Oman and UAE withdrawal from the planned common currency, **what are the chances of a GCC common currency?**
- In most probability, the **issue will be shelved** amongst the four remaining members, and instead the focus will be on strengthening monetary union of the GCC.
- This could involve the following:
 - **Harmonizing regulatory policies and risk management practices.**
 - **Deepening economic ties.**
 - **Liberalizing inter-region trade and capital movement.**
 - **Full labor movement.**
- The above could follow the European Union model as there are some **CONVERGENCE CRITERIA** that needs to be adopted before monetary union could be established.

Table 14.13. Monetary union convergence criteria: Maastricht and GCC comparative analysis (2008)

<i>Criterion</i>	<i>Maastricht</i>	<i>GCC</i>	<i>GCC Compliance*</i>
Exchange rates	Fluctuations within normal margins for two years; no devaluation against any other member states currency	Long-term stability of GCC exchange rates means that this criterion has not been an issue	N/A Compliance
Foreign reserves	No such criterion	To cover four months of Imports	Bahrain X Qatar ✓ Oman ✓ Kuwait ✓ KSA ✓ UAE ✓
Interest rates	Long-term rates must not exceed a margin of 2 percentage points over the average of the three lowest - inflation members	As Maastricht but for short term rates (3 months)	Bahrain ✓ Oman ✓ Kuwait ✓ UAE ✓ Qatar ✓ KSA ✓
Inflation rates	Must not exceed more than 1.5 percentage points of the average of the three lowest-inflation members.	As Maastricht	Bahrain ✓ Qatar X Kuwait ✓ KSA ✓ Oman ✓ UAE X
Fiscal deficits	Must not exceed 3 percent of GDP	As Maastricht when OPEC basket oil price is \$25/b or more	Bahrain ✓ KSA X Kuwait ✓ UAE ✓ Qatar ✓ Oman ✓
Government debt	Must not exceed 60 percent of GDP	As Maastricht	Bahrain ✓ Oman ✓ UAE ✓ Kuwait ✓ KSA ✓ Qatar ✓

Note: ✓ = criteria met

X = criteria not met.

Source: Adapted from Rutledge, 2009.

To peg or not to peg against the dollar?

- One issue that the remaining GCC members who are still interested in establishing a common GCC currency is **whether to peg (fix) against the dollar or to establish other exchange rate regimes.**
- The opting out of the fixed dollar peg by Kuwait makes agreeing on a dollar peg even more difficult.
- **The options for the GCC are:**
 - Fixed Dollar Peg
 - Managed Floating
 - Peg to Oil Prices
 - Basket Peg
- Each option has advantages and disadvantages.

Table 14.14. GCC: pros and cons of possible exchange rate regimes for a unified currency.

<i>Exchange Rate Regime</i>	<i>Pros</i>	<i>Cons</i>
1. Fixed Dollar Peg	<ul style="list-style-type: none"> ▪ Provides a credible and easily understood anchor for monetary policy and simplifies trade and financial transactions and business planning. ▪ Provides certainty about the future ▪ Labour market flexibility can support international competitiveness ▪ Preferred by major oil exporters. 	<ul style="list-style-type: none"> ▪ No flexibility to adjust to real shocks. ▪ Imports monetary policy from USA not appropriate to local needs. ▪ Dollar weakness can be easily transmitted to domestic prices – imported inflation triggering price-wage spirals, generate low interest rates and increase risk of asset price bubbles.
2. Managed Floating	<ul style="list-style-type: none"> ▪ Ability to use monetary policy to smooth business cycles, by absorbing real shocks (negative or positive change in terms of trade) and more appropriate to globalization trends. ▪ Potential to increase competitiveness of non-oil sector 	<ul style="list-style-type: none"> ▪ Institutional weaknesses may inhibit adoption of either inflation targeting or monetary targeting. ▪ Possibility of large and frequent FX intervention in face of large swings in oil prices. ▪ Complicates budgetary accounting and business planning.
3. Peg to oil prices	<ul style="list-style-type: none"> ▪ Would allow real exchange rate to move in line with price of the dominant export. 	<ul style="list-style-type: none"> ▪ Rising oil prices would mean real appreciation of currency, damaging competitiveness of non-oil sector. ▪ Would introduce greater volatility in the exchange rate, leading to lower government revenues and higher government debt.
4. Basket peg	<ul style="list-style-type: none"> ▪ Useful “halfway” solution offering some nominal flexibility to contain shocks, while retaining main anchor properties of a fixed peg. ▪ Can help in short term to contain imported inflation. 	<ul style="list-style-type: none"> ▪ Does not give monetary independence and would not address the management of oil price volatility or increase of liquidity arising from high oil prices. ▪ Undisclosed basket (such as Kuwait’s) could invite speculation and complicate future business planning.

Source: Khan, 2008.

Thinking West but moving East: Saudi Arabia's new strategic partnerships.

- There has been a significant deepening of relationship between Saudi Arabia and emerging world economic powers such as China and India, as well as Brazil and Russia (the so-called BRIC economies).
- King Abdullah made his first overseas official visit to China and India in January 2006, which was reciprocated by the Chinese President in April 2006.
- The issue of diversification of emerging markets for Saudi Arabia, and ensuring secure of supplies for China are important elements for both countries.
- Over the past few decades, China and Saudi Arabia have increased the scope and size of bilateral energy related cooperation, as well as bi-lateral trade which rose sharply.

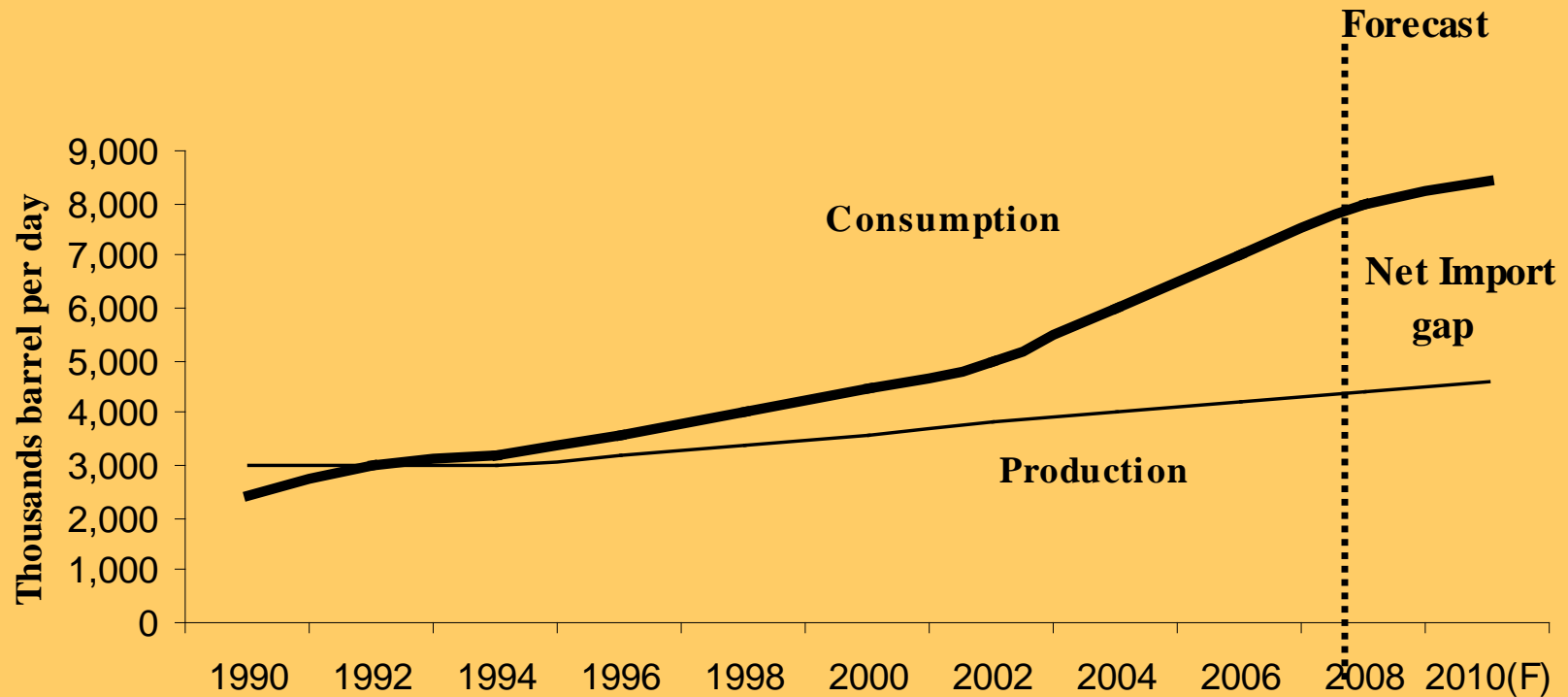
- The **bi-lateral trade relations with India** has also risen. In 2008, exports to China represented around 9% of total exports, while exports to India represented 7.2%.
- Imports from China represented 11% of total imports, while those from India represented 4.2% for 2008. Saudi Arabia enjoys substantial trade surpluses with both countries.
- **Energy security** remains at the heart of the Asian relationship, especially for China, which is the second largest oil consuming nation after the USA, and faces a net import gap of oil demand.

Table 14.15. Saudi trade with China and India 1984-2008 (\$ millions)

<i>Year</i>	<i>Exports to China</i>	<i>Imports from China</i>	<i>Exports to India</i>	<i>Imports from India.</i>
<i>1984</i>	6.4	183.4	1,119	265.9
<i>1991</i>	92.2	625.0	1,094	292.5
<i>1998</i>	328.0	958.0	1,622	815.1
<i>2002</i>	2,885.3	1,718	3,931	2,630
<i>2006</i>	15,957	8,710	17,098	3,074.4
<i>2008</i>	27,987	12,677	22,744	4,803.2
<i>(2008) % to Total Saudi Export/Imports</i>	<i>8.9%</i>	<i>11.0%</i>	<i>7.2%</i>	<i>4.2%</i>

Source: SAMA

Figure 14.11. China's oil production and consumption, 1990-2010*



*** Forecast.**

Source: IEA, 2009.

The Middle East remains China's main oil import region

- Despite import diversification from different regions, especially Africa (Angola and Sudan), the **majority of Chinese oil imports comes from the Middle East.**
- Saudi Arabia and Iran are the largest exporters followed by Oman and Kuwait.
- **Saudi-Chinese relations are not only concentrated on oil supplies, but involves a range of bi-lateral relations, including:**
 - Security and defense.
 - Health.
 - Petrochemical joint ventures in China between SABIC and Aramco with Chinese companies.
 - Oil exploration joint ventures.

**Figure 14.12. China's crude oil imports by source
(Thousand barrels per day)**

2008 (Total 3,568)

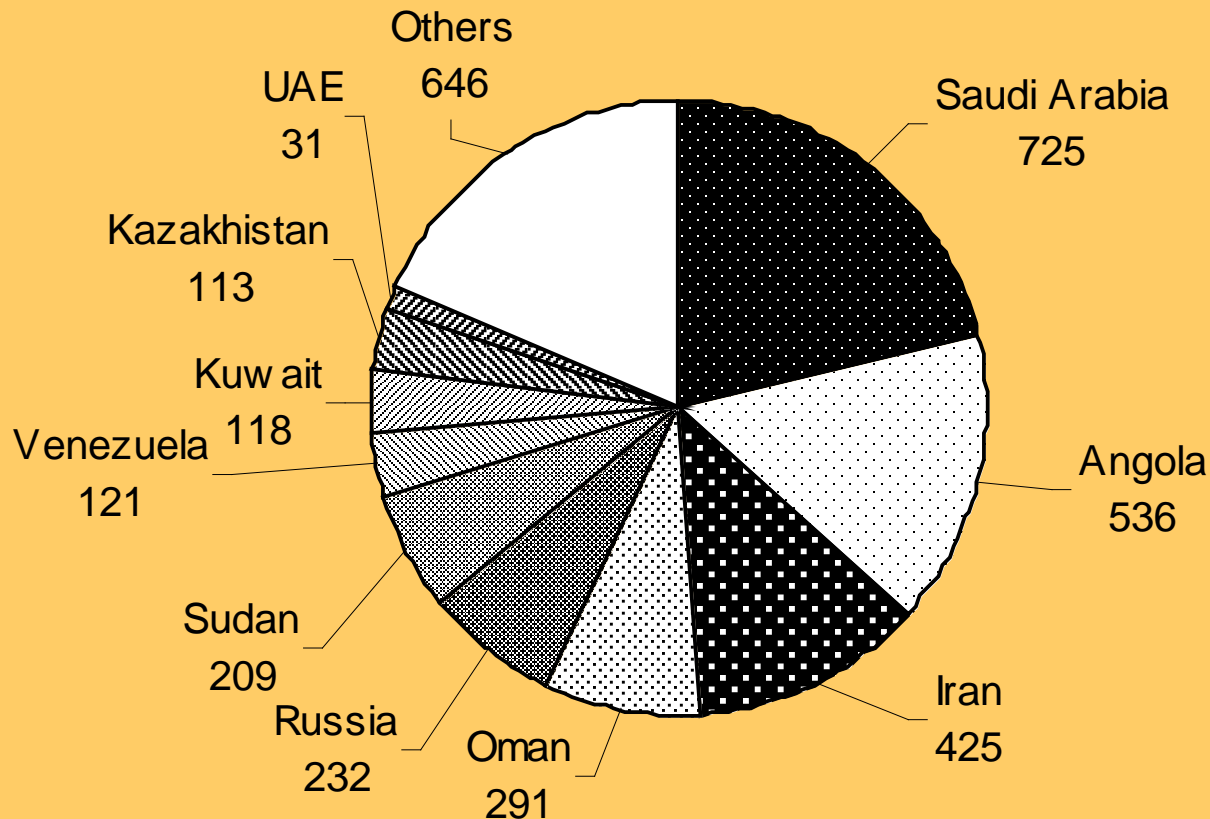
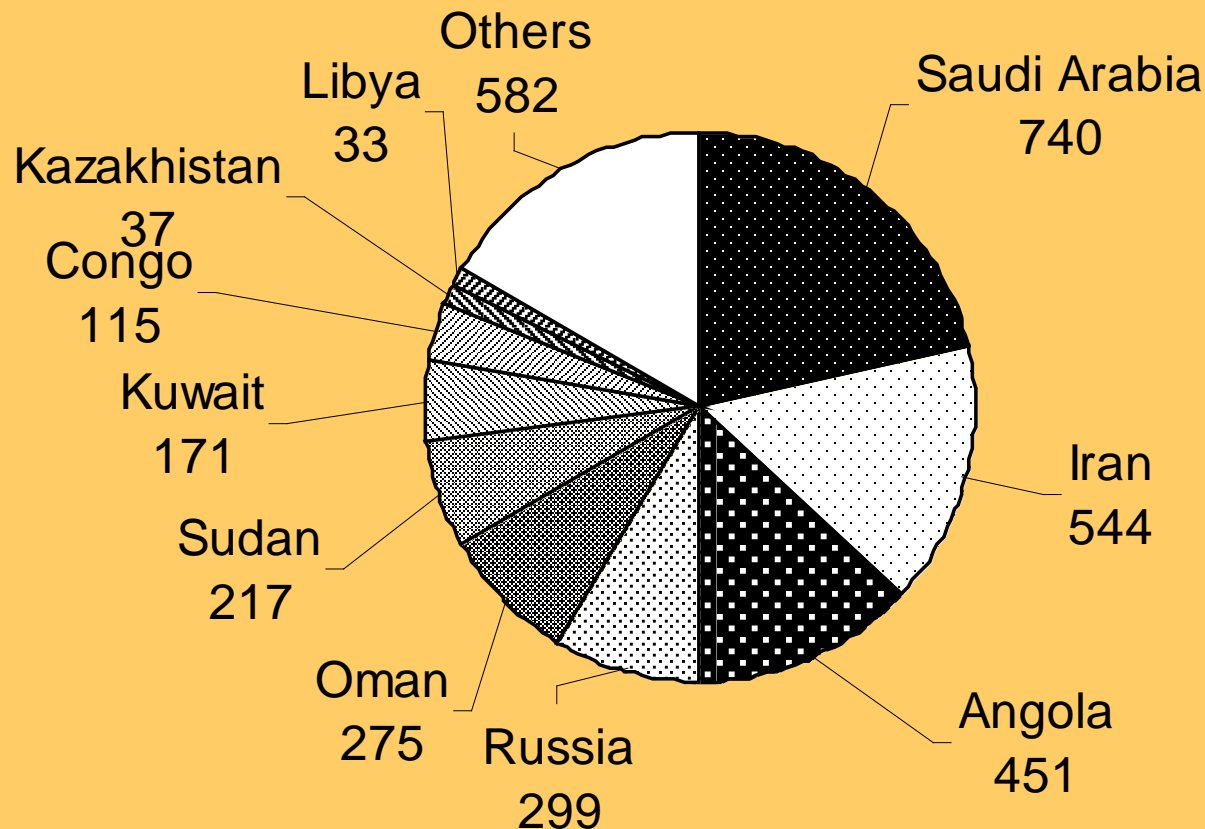


Figure 14.12. Contd.....

2009 (Jan-May) Total 3,505



Source: FACTS Global Energy, 2009.

Saudi-India relations: technology and trade

- **Saudi Arabia and India share long trading and cultural links**, as India is home to about 170 million Muslims, second largest after Indonesia.
- **Indian expatriates represent around 20% of Saudi Arabia's expatriate population.**
- **Indian companies are evident in technology and IT, and have established joint ventures in Saudi Arabia following Saudi WTO accession.**
- **In 2010 a high level Saudi-Indian Economic Agreement further cemented the relationship in IT and renewable energy research.**

Conclusion

- The GCC countries have come a long way since 1981 and had to deal with the most **radical economic, social and political transformation in their history.**
- They are all facing similar issues of finding employment for their nationals, **introducing domestic reforms and meeting the challenges of globalization.**

(Contd....)

- There is still more coordination required, especially for **labor mobility** within the GCC, and in managing their expatriate labor force.
- The **GCC Monetary Union** is going ahead, minus two member states concerning the common currency.
- Saudi Arabia is also developing **new global strategic alliances with Asian countries**, which will become a more prominent feature of Saudi economic and foreign policy in the years ahead.