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The private sector and reform in the Gulf Cooperation Council

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Abstract

While the Gulf private sector has made huge strides since the first oil boom, most of its activities still amount to more sophisticated rent recycling rather than autonomous diversification. Its interests are in stark opposition to those of the citizenry at large, as it provides no taxes, little employment and few investment opportunities for GCC nationals. Instead, business and other social forces face a zero-sum conflict over – in some cases increasingly scarce – state resources. This structural isolation of business goes some way in explaining Gulf capitalists' weak role in today's political arena despite a strong pre-oil history of collective action. In recent decades, business elites have either kept their heads below the parapet or have provided auxiliary public support to beleaguered local regimes. They have for the most part abstained from or failed in electoral politics; in austere times, regimes have privileged the distributional interests of the state salariat and consumers at large over those of business. Gulf business has a chance for a greater developmental role and political autonomy only if it increases its interdependence with society at large through providing a tax base, employment and investment opportunities for GCC citizens. Of the three, employment is the most important and could decide the political fate of private capital in the Gulf in the long run.

Keywords

Gulf business; Gulf politics; Gulf private sector; rentier state; state–business relations

1. Introduction

Of the Arab world's thirty largest companies by market capitalization in 2011, twenty-five were based in the states of the Gulf Cooperation Council (GCC).[1] Of all Arab businesspeople, those of the Gulf have by far the largest overseas investments, amounting to hundreds of billions of dollars, and have become increasingly active as investors in the wider Middle East region (Hertog 2007). Although GCC governments themselves are cash-rich after a decade of high oil prices, their development strategies increasingly rely on the local private sector for diversification, job creation and the building of a more productive and less oil-dependent 'knowledge economy'.[2]

I would like to thank Rivka Azoulay, Hasan Al-Hasan, Nathan Hodson, Jim Krane, Laurence Louer, Marc Valeri and Steven Wright for their invaluable contributions to and comments on this paper, and Jim Krane for sharing the data for Figures 18 and 19 with me.

[1] See http://www.cashandtrademagazine.com/test/wp-content/uploads/2011/07/top-100-arab-companies.jpg.

[2] Both the *Abu Dhabi Economic Vision 2030* (Government of Abu Dhabi 2009) and the *Qatar National Vision 2030* (General Secretariat for Development Planning 2008) mention increased reliance on the private sector as employer and driver of growth in the quest for a knowledge economy. The *Economic Vision 2030 for Bahrain*

At a superficial glance, the private sector seems to have become the driver of development in the Gulf. Given this strategic role, it is not a big jump to expect it to become a political player with leverage over government – in other words, a true 'Gulf bourgeoisie'.[3]

How accurate is this picture of economic and political ascendancy? This paper will argue that headline figures about private assets and investments, and state rhetoric about private-driven growth, are misleading: although Gulf business has largely moved beyond the stage of pure rent-seeking, it is still far from autonomous from local states either economically or politically, and its contributions to economic modernization and reform have been modest in international comparison. The reasons for this are numerous, some easily observable and others less so. In the Gulf with its pro-capitalist traditions and rhetoric, it is easy to under-estimate the capacities of the state and over-estimate those of business.

This paper will show that Gulf business provides most of local employment and capital formation, and contributes to the provision of services that were previously the domain of the state. Since the first oil boom era of the 1970s and early 1980s, Gulf business has become more sophisticated managerially, runs more substantial operations and is less immediately sensitive to fiscal shocks.

This appearance of autonomy is misleading, however, as GCC capitalists remain an appendix to the state in an analysis of the fundamental drivers of growth in Gulf economies – especially if the structural role of the bourgeoisie in tax-based economies is taken as a yardstick. The underlying driver of demand in Gulf economies is the government, whose spending is not financed through domestic taxes, and whose payroll dwarfs that of the private sector. Many business activities, in manufacturing in particular, depend on cheap state-provided energy, for which there is increasing rivalry between retail and industrial consumers. Much of the diversification into new sectors has been driven by state-owned companies, and the private sector has contributed little to either employment of locals or the desired move to a less oil-dependent 'knowledge economy'. Most private sector wealth is held privately and therefore beyond the reach of local investors; even publicly listed companies are often not run in line with international standards of corporate governance. Business input to economic

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aims at a knowledge-based economy 'driven by a thriving private sector' (Economic Development Board 2008), while Saudi Arabia's ninth development plan, 2010–14, projects private sector growth rates above those for the public sector, and sees the private sector as main job creator and crucial partner in the future 'knowledge economy' (Ministry of Economy and Planning n.d.). The unpublished 'Vision Kuwait 2030' report prepared by Tony Blair's office for the Kuwaiti government mentions a general consensus that 'economic diversification is urgent and that most of it needs to come from the private sector' (pp. 28f.).

[3] Authors recently proposing an emergent Gulf bourgeoisie or a newly empowered 'Gulf capital' include Adam Hanieh and Giacomo Luciani, although the latter's arguments are focused mostly on Saudi Arabia (Hanieh 2011; Luciani 2006).

policy is reactive and focused more on defending the status quo than on shaping the future agenda of diversification.

In sum, while the Gulf private sector has made huge strides since the first oil boom, most of its activities still amount to more sophisticated rent recycling rather than autonomous diversification. Its interests are in stark opposition to those of the citizenry at large, as it provides no taxes, little employment of nationals and few investment opportunities. Instead, business and other social forces face a zero-sum conflict over – in some cases increasingly scarce – state resources.

This structural isolation of business goes some way in explaining Gulf capitalists' weak role in today's political arena despite a strong pre-oil history of collective action. In recent decades, business elites have either kept their heads below the parapet or provided auxiliary public support to beleaguered local regimes. They have for the most part abstained from or failed in electoral politics; in austere times, regimes have privileged the distributional interests of the state salariat and consumers at large over those of business.

Gulf business has a chance for a greater developmental role and political autonomy only if it increases its interdependence with society at large through providing a tax base, employment, and investment opportunities for GCC citizens. Of the three, employment is the most important and could decide the political fate of private capital in the Gulf in the long run.

The arguments developed in this paper are derived from a survey of the GCC private sector's contribution to development and politics that is necessarily broad and extensive, as there is little existing research about Gulf business as an economic or political player that the paper could draw on. The last major books about the politics and sociology of Gulf merchant families are now some two or three decades old (Field 1986; Crystal 1995). Important work has more recently been done on the changing macro-economic position of the GCC private sector (Hodson 2012), and there are a number of more recent qualitative case studies about state–business relations in Bahrain, Kuwait and Oman (Azoulay 2012b; Valeri 2012). Yet there are many quantitative and qualitative aspects of today's Gulf state–business relations that have not been investigated and require the analysis of primary data.

2. Business in economic development and policy-making

2.1. Role in national economies

The GCC went through a decade of wide-ranging economic reforms and liberalization steps in the 2000s. The economic opening of new sectors and transfer of functions from state to business has generally benefited local business more than international players; unlike in other developing countries, multinational companies might be needed for their expertise, but not usually for their capital, which is locally abundant.

GCC business now plays a deeper role in sectors like education, health, telecoms, heavy industry and air transport, which until the 1990s were partly or completely state-controlled. The various long-term development visions that GCC governments have published since the early 2000s all state a clear willingness to delegate increasing development tasks to the private sector.[4] GCC business has been clawing back activities from the state that it last undertook in the pre-oil era, when the first power plants, manufacturing activities and even schools in GCC countries were often privately financed and operated (Hertog 2010a: 81).

Unlike most of the republican regimes of the Arab region, GCC governments have always pursued a pro-capitalist economic agenda, and local merchant classes never had to witness the waves of nationalizations that decapitated old business classes in countries like Algeria, Egypt or Syria in the post-World War II era. Yet the actual productive capacities of local capitalists were strictly limited in the early oil era, as there had been little economic differentiation before the inflow of oil rents. In the 1970s and 1980s, GCC merchants often just functioned as intermediaries and access brokers for international businesses which provided most of the actual goods and services the rapidly growing, oil-fed GCC economies demanded (Hertog 2010b; Field 1986).

The operations of large local businesses are much more substantial now, covering large manufacturing plants, private schools, clinics and universities, banks, high-class retail and hotel chains, and contracting businesses employing tens of thousands of construction workers. Perhaps 80 per cent of the jobs in the region are provided by private business, albeit these are mostly held by foreign employees. And while local capacities have expanded, overseas assets – whether generated through productive activities or rent-seeking – have grown during decades of accumulation. While rentier states have to draw down continuously their hydrocarbons and, in the long run, overseas assets due to increasing local spending needs, the rentier private sector can continuously grow its resources. Private overseas resources now have reached a level that gives local capitalists considerable short-term independence from governments, as their current income derived from local markets (private or public) has become smaller relative to their accrued assets. GCC businesses have also increased their share of foreign direct investment in the wider Middle East and North Africa (MENA) region,

[4] See n. 2.

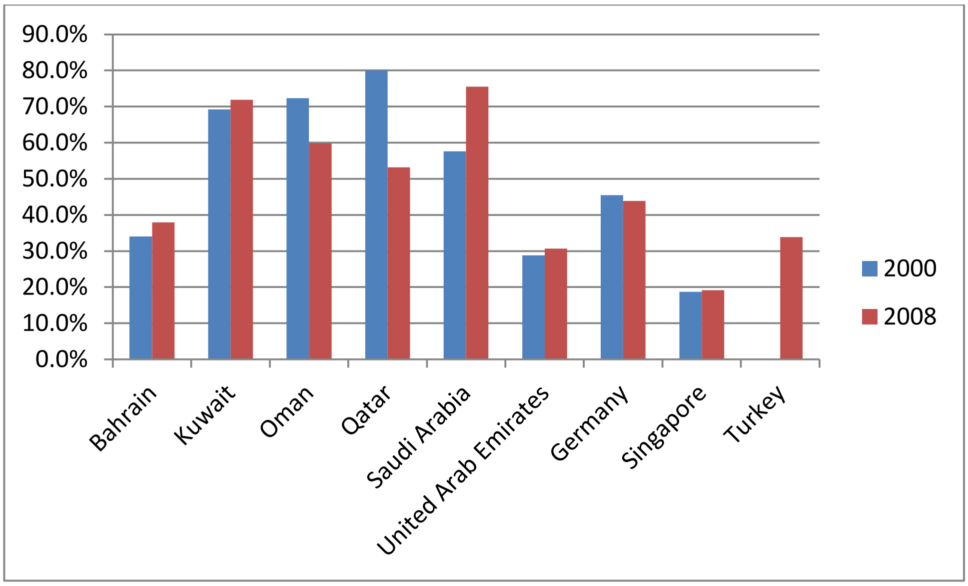
giving them an increasingly active role in the real estate, banking and manufacturing sectors of their poorer neighbours (Hertog 2007).

And yet the state remains stronger in GCC economies than in those of most other countries, and despite its greatly enhanced capacities, the private sector remains more dependent on government than almost anywhere else. This dependence can be exemplified both through an inspection of standard macro-economic variables, and even more so through a somewhat less obvious analysis of how demand in GCC economies is generated.

The share of state spending in non-oil gross domestic product (GDP), and of government consumption in total final consumption, for the most part remains considerably higher than in other world regions (see Figures 1 and 2). Much of the 2000s booms was driven by state spending, which has remained on a high level throughout. Perhaps more importantly, an unusually high share of private household consumption is financed through civil service wages, which dominate the total wage income of GCC nationals (see section 2.2 for details).

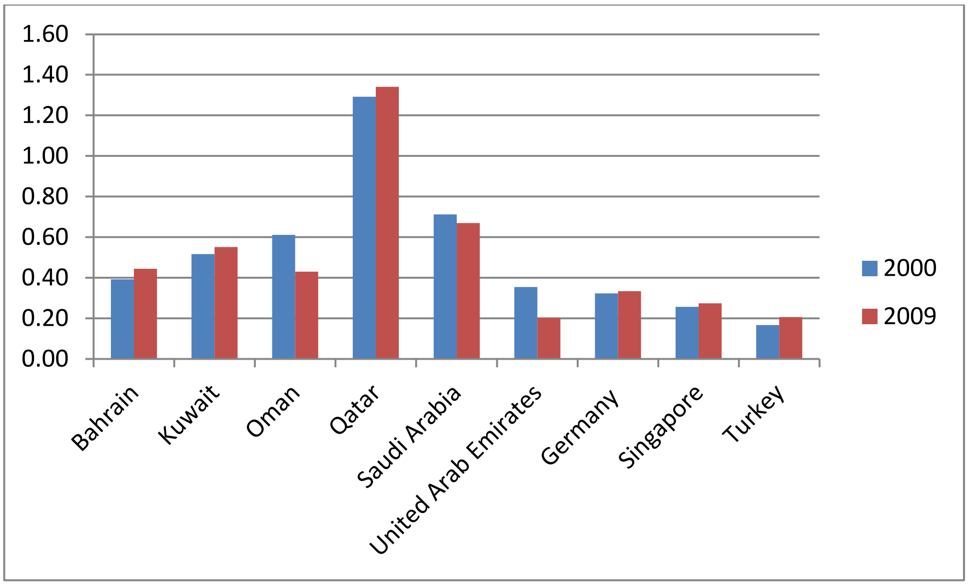
The two GCC countries that appear more diversified in terms of state spending and consumption patterns are Bahrain and the United Arab Emirates (UAE). In the Bahraini case, the figures appear plausible in view of the small economy's large private service sector, which is to a significant extent financed by private capital from other GCC countries. The UAE figures, however, might understate the government's role, as outside of Dubai private sector

Figure 1. *Share of state spending in non-oil GDP in the GCC and select international cases, 2000–8*



Sources: International Monetary Fund (IMF); United Nations Statistics Division (UNSTATS).
Note. Kuwaiti data are from 2007.

Figure 2. *Ratio of government to private consumption in the GCC and select international cases, 2000–9*



Source: UNSTATS.

activity is limited and it is not clear whether the UN figures for government spending and consumption include emirate-level and public company activities.

Growth patterns in the private sector at large still broadly follow state spending, as is illustrated in the Saudi and Kuwaiti examples in Figures 3 and 4.

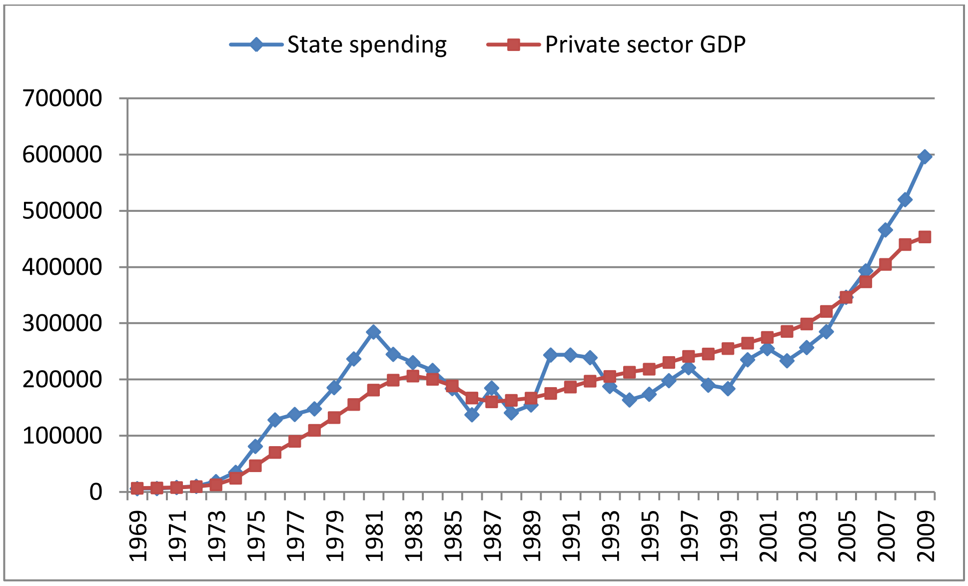
Levels of state spending and size of private sector are correlated closely in the GCC. While this is the case in many other economies, the causality usually is not obvious: public expenditure can drive business expansion, but business expansion in regular tax-based states also increases government revenue, which in turn allows higher expenditures. The two variables are interdependent.

In the GCC, by contrast, the only reasonable interpretation is that causality runs in one direction: as domestic economic activity creates very little tax income and states are for the most part financed by external rents,[5] in the correlation between state spending and business growth, fiscal policy appears the cause and business growth the outcome.[6] The channels of this process can be both direct (usually through larger spending through state contracts for

[5] Local corporates are not subject to conventional corporate tax, with the exception of Oman, where they are subject to a 12 per cent rate, while foreign companies pay between 5 and 30 per cent. Despite a long debate, none of the Gulf states imposes general sales or value added taxes (VAT), or personal income taxes on nationals (all of which would be income derived indirectly from business activity). See Fasano and Iqbal (2003) for a still broadly accurate survey of tax regimes, and Harrison (2010) for an overview of the more recent debate about (yet to be created) VAT and income taxes.
[6] For more details see Hertog (2011a).

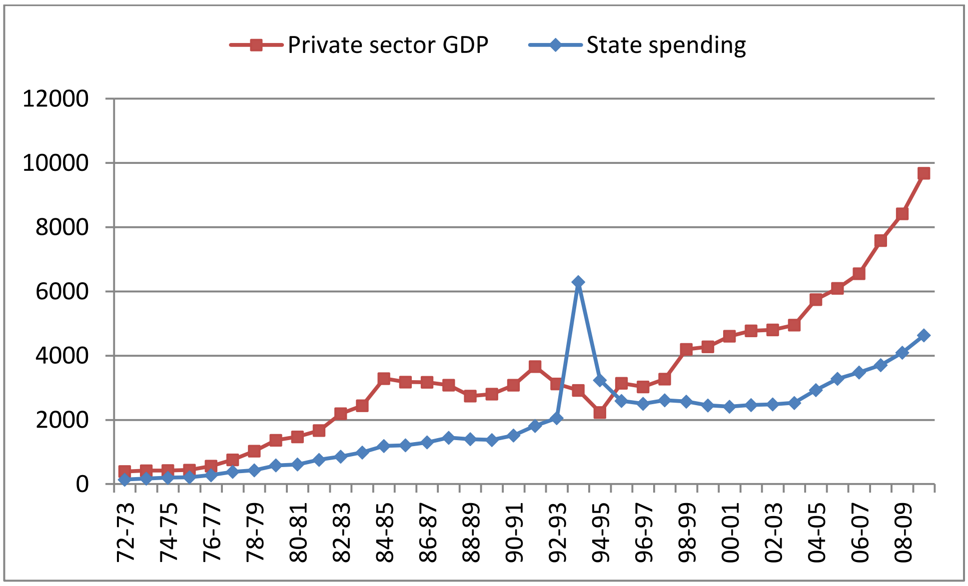
private businesses) and indirect (through expenditure on public salaries that increase consumption levels in the economy).

Figure 3. *Private sector contribution to Saudi GDP vs. total government expenditure (million SR), 1969–2009*



Source: Based on Saudi Arabian Monetary Agency (SAMA) data.

Figure 4. *Private sector contribution to Kuwaiti GDP vs. total government expenditure (million KWD), 1972/3–2008/9*



Source: Based on data from the Kuwaiti Central Bank.

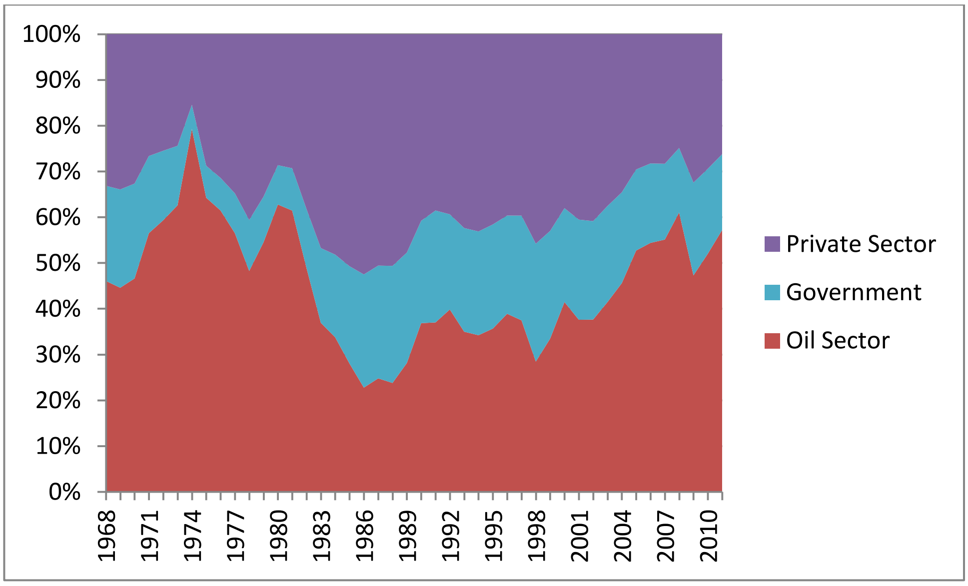
Econometric tests show an abiding and strong impact of state spending on the size of business activity. The two variables remain closely associated in the long run.[7] This means that much of GCC business activity is fundamentally explained by state spending and would suffer severely in its absence, as there are no sufficient private (or international) sources of demand for services and products provided by GCC businesses.

None of this is to say that GCC business is as dependent on the state as it was during the first oil boom in the 1970s and early 1980s. It does command a larger share of GDP than in that period. During the oil-fed boom of the 2000s, the private sector has not been as marginalized in the total economy as it was in the 1970s. Figure 5 illustrates this with data from Saudi Arabia, a country where state spending has increased particularly strongly during the 2000s (on the latter point, see Figure 10 below).

The sub-sectoral composition of GDP in at least the Saudi economy also seems to be more robust vis-à-vis short-term fiscal shocks than it used to be (Figure 6).

While government spending has reached levels similar to those of the peak of the oil boom in the 1970s and early 1980s, it has led to less of an inflation of boom-time sectors like 'construction' and 'ownership of dwellings'. These activities had proven to be almost completely state-dependent during the previous boom, collapsing in the mid-1980s as a result

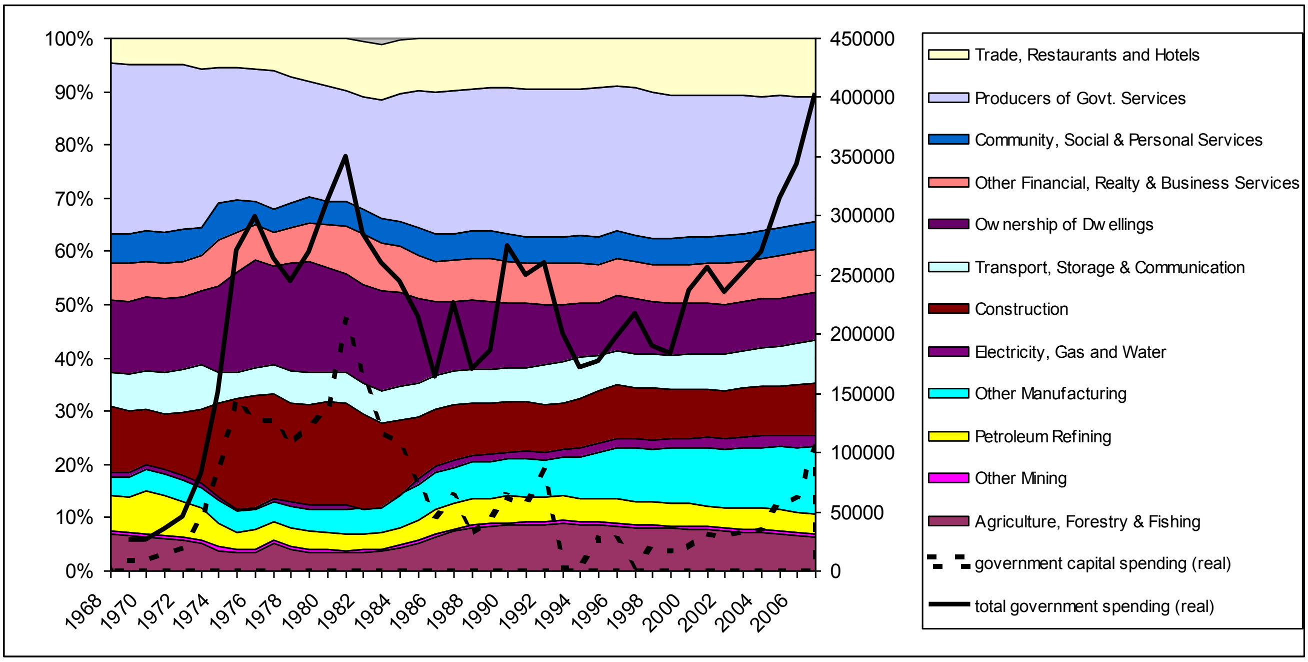
Figure 5. *Composition of Saudi GDP, 1967–2010*



Source: SAMA.

[7] For (somewhat dated) econometric evidence cf. Kireyev (1998) and Treichel (1999). More recent econometric tests using time series regressions and error correction models confirm the findings on data up to 2008. A 2011 IMF report also provides evidence of strong fiscal multipliers in the GCC (Espinoza and Senhadj 2011).

Figure 6. *Composition of non-oil GDP in Saudi Arabia vs. government spending (million SR), 1968–2006*



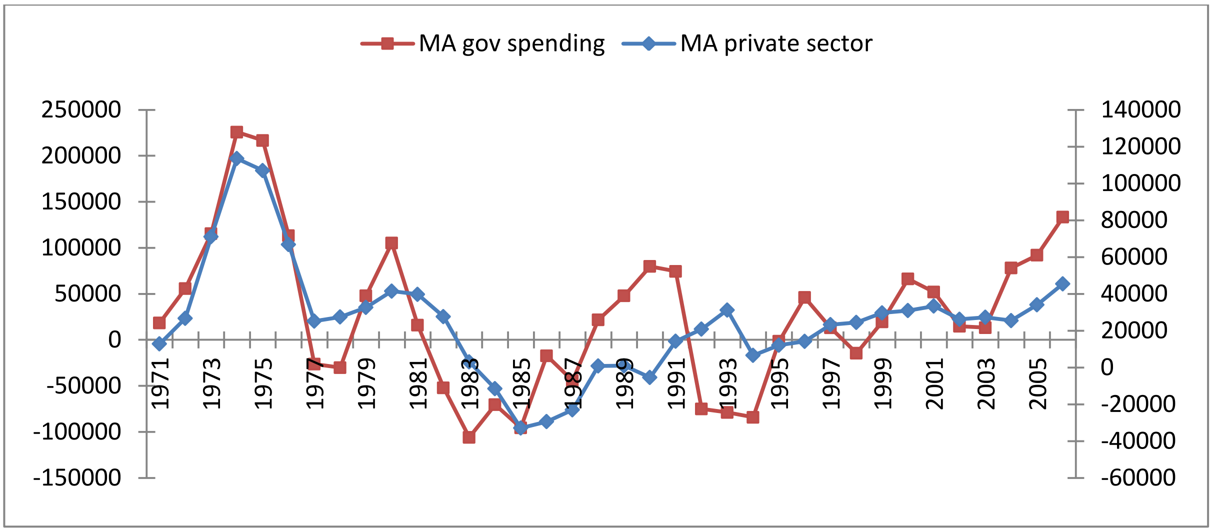
Source: SAMA.
Notes. Non-oil GDP is shown on the left-hand side, with government spending on the right.

of reduced government capital outlays, which led to the bankruptcy of tens of thousands of contracting companies (Vassiliev 2000: 454).

In at least some of the GCC countries, the short-term dependency of business on public expenditure is less pronounced than it used to be up to the mid-1980s: although the two remain closely linked in the long run, their growth rates now are less closely correlated in the short term, meaning that the growth path of business is relatively smoother and less affected by temporary spending fluctuations (see Figures 7 and 8 for illustrative data on Saudi Arabia and Kuwait, and Treichel (1999) and Kireyev (1998) for econometric evidence on Oman and Saudi Arabia).

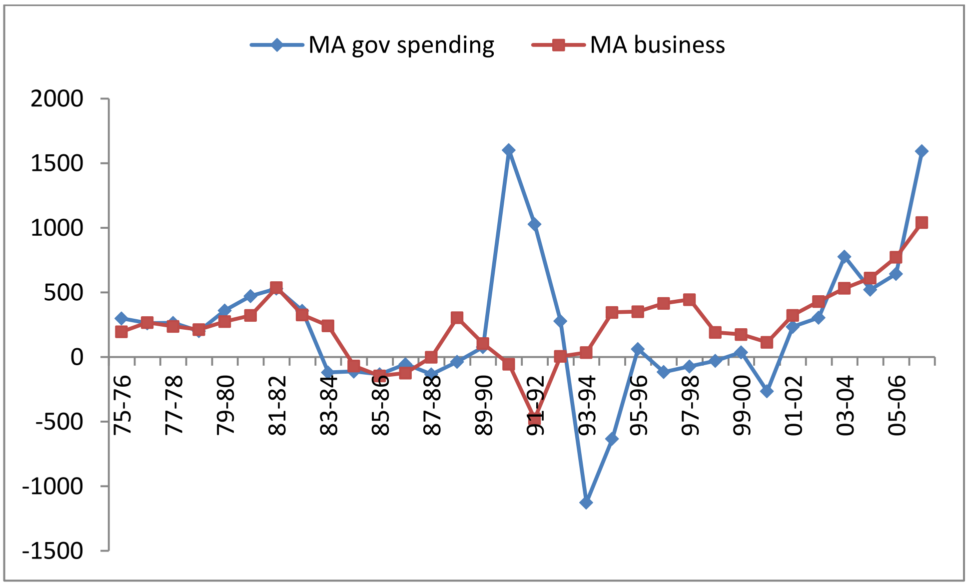
One reason for a less immediate dependence on state spending might be that demand is now more strongly driven by private consumer spending, which has grown significantly since the 1970s in line with local populations. Even if much or most of this demand is indirectly created through state spending on salaries and benefits (see section 2.2), consumption decisions are nonetheless smoothed over time relative to state expenditure. Figure 9 shows that GCC governments since the 1980s have devoted larger shares of their total budgets to current than to capital expenditure. The former item is usually dominated by salaries, while the latter mostly results in direct contracts with private companies.

Figure 7. *Changes in state spending and private sector size in Saudi Arabia (million SR, 3-year moving averages), 1971–2005*



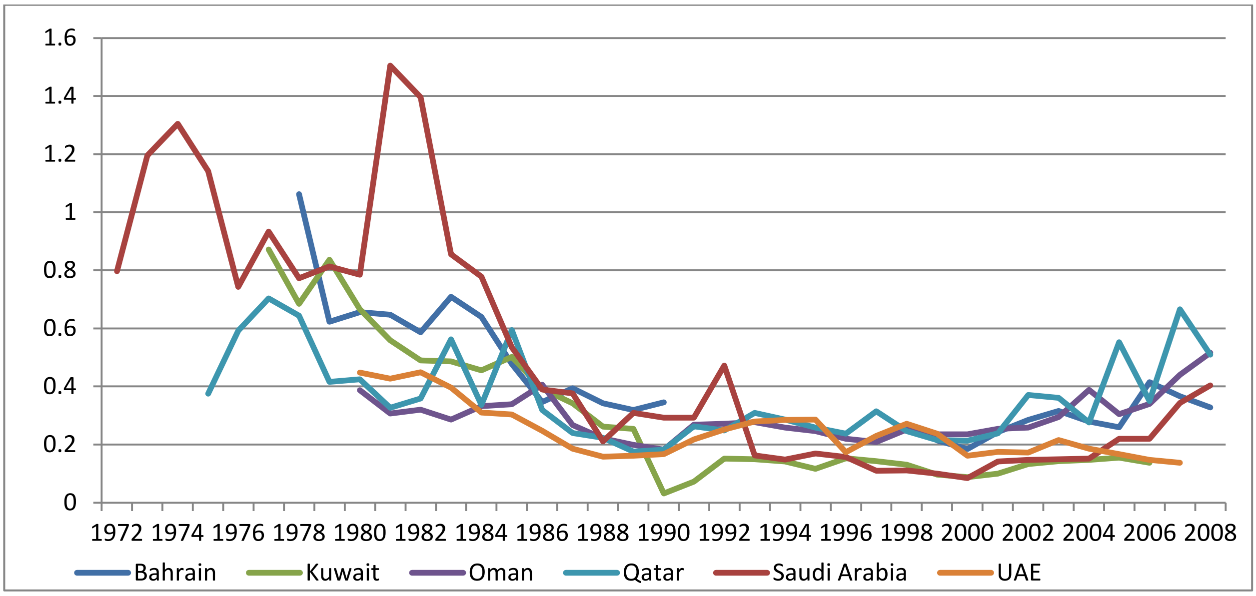
Source: SAMA.
Notes. State spending is shown on the left-hand side, with private sector size on the right. MA = moving average.

Figure 8. *Changes in state spending and private sector size in Kuwait (million KWD, 3-year moving averages), 1975/6–2005/6*



Source: Kuwait Central Bank.
Notes. State spending is shown on the left-hand side, with private sector size on the right. MA = moving average.

Figure 9. *Ratio of government capital to current expenditures in the GCC, 1972–2008*

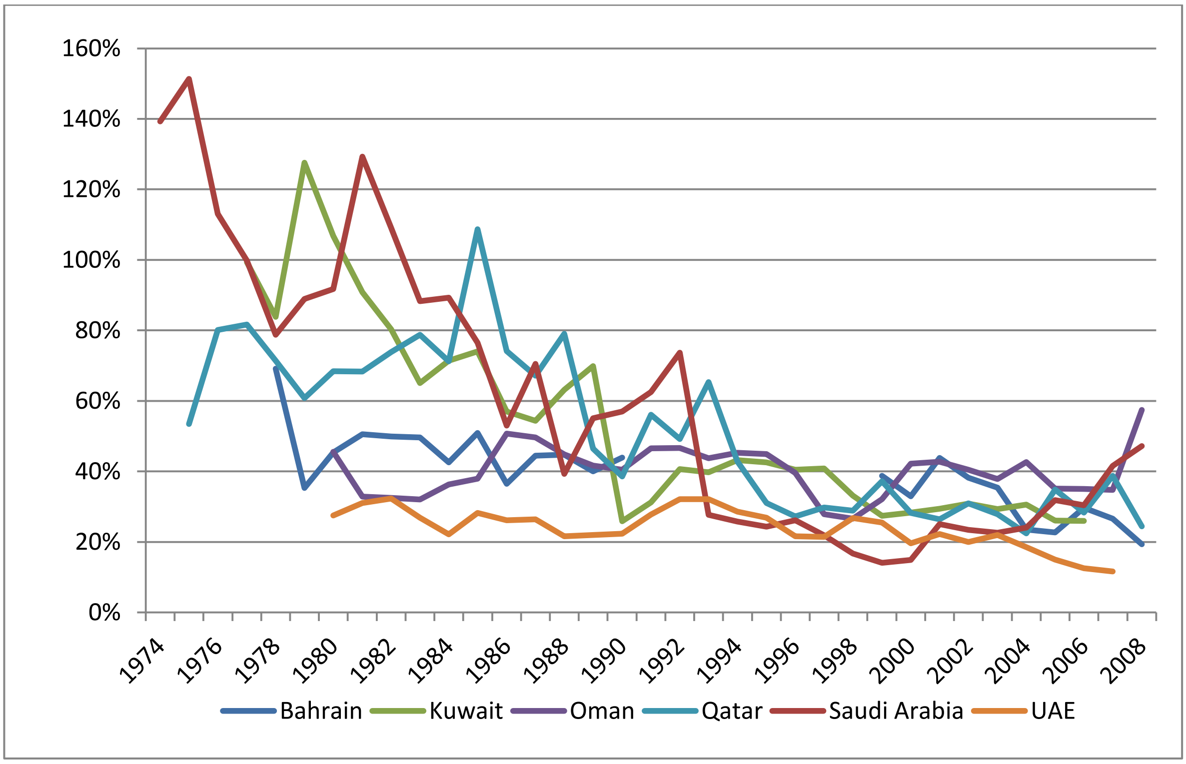


Sources: United Nations Statistical Abstract of the Economic and Social Commission for Western Asian (ESCWA) Region; various national reporting data; IMF Article IV Reports and Statistical Appendices.

State capital spending has picked up again with the 2000s oil boom, but has not reached the same levels relative to total spending that it did in the 1970s and early 1980s. At the same time, private capital formation has continued to increase, resulting in very high combined levels of capital formation in the late 2000s (Figures 10 and 11). In all countries bar Oman, the private sector continues to contribute more to capital formation than the public sector.

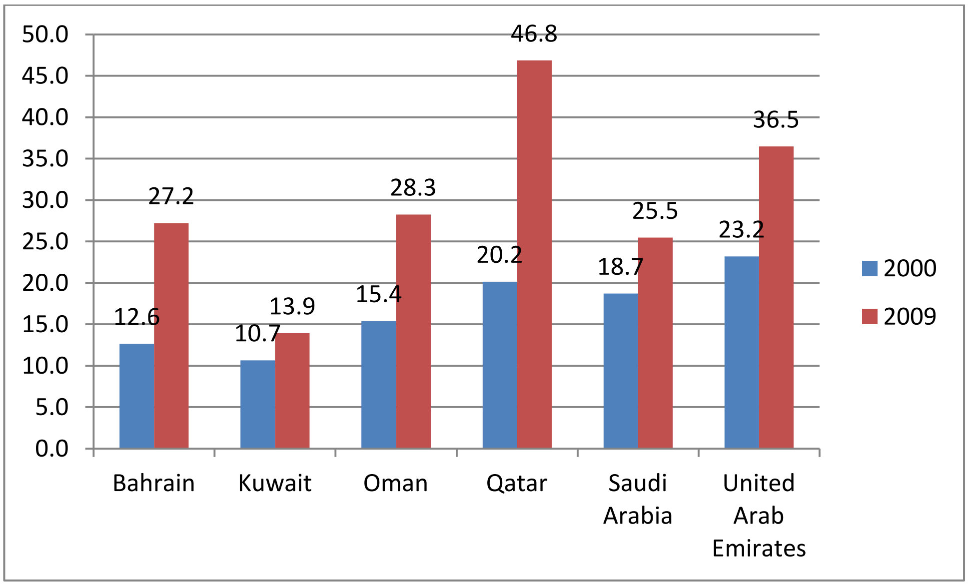
Thanks to decades of growth and the accumulation of large capital resources, many private businesses in the Gulf have matured in their managerial and technological capacity, are less directly reliant on state spending in the short run and contribute the majority share of national capital formation. As they depend relatively less on state direct procurement and more on consumer demand than in the 1970s and 1980s, they tend to operate in more competitive markets. GCC capitalists have moreover built up significant foreign direct investment (FDI) in the wider MENA region and beyond, and in some cases have become competitive exporters (Hertog and Luciani 2010: 2f.; Luciani 2006). At the same time, it appears that most of GCC business could not operate without the state's direct and indirect fiscal stimuli in the long run. The state's role remains larger in GCC economies than in most other regions of the world, and, unlike the case in tax-based economies, Gulf businesses

Figure 10. *Share of government capital spending in national gross fixed capital formation in the GCC, 1974–2008*



Sources: United Nations Statistical Abstract of the ESCWA Region for total fixed capital formation; national reporting data and IMF Article IV Reports for sector contributions to fixed capital formation.
Note. The ratios above 100 per cent for some cases in the 1970s are due to inconsistencies in national fiscal and national accounts statistics; unless the inconsistencies have changed strongly and consistently over time, this should not affect the general trend we observe.

Figure 11. *Capital formation as percentage of GDP in the GCC, 2000–9*



Source: UNSTATS.

contribute practically nothing to sustaining the state demand they depend on, as they generate little or no tax income.

2.2. Contribution to national employment

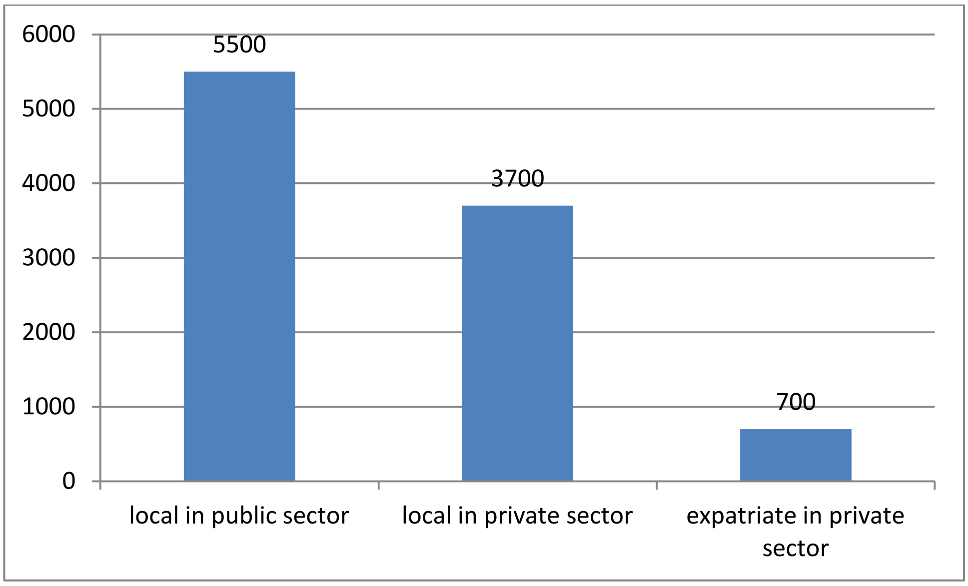
Long-term state dependence notwithstanding, the GCC private sector provides a significant contribution to GDP and capital formation. What about employment, arguably the politically most important function that capitalists play? The sheer number of jobs created by the private sector in the GCC is huge – but for the most part, these are low-paid, low-productivity positions held by foreigners, the result of a factor-intensive growth paradigm that limits private-driven diversification and is both economically and politically unsustainable in the long run. As importantly, the reliance on foreign workers in the private labour market isolates GCC businesses in the broader political economy of the Gulf monarchies: as few GCC nationals are employed by local capitalists, the national population shares few objective interests with them, making business reliant on political patronage from local regimes, their increased capacity and short-term autonomy notwithstanding.

The GCC is unique worldwide in having a migration regime that allows almost unlimited imports of workers from the developing world. Combined with the 'sponsorship' system that allows local employers to control foreign workers tightly, this leads to a private labour market in which most jobs are badly paid, onerous and held by expatriates. This contrasts with public sectors in which wages are higher, work conditions easier and most jobs are held by nationals (Hertog 2012a). The private sector provides little quality employment that would be acceptable to nationals (or indeed citizens of other rich countries).

Even after the 2000s boom decade, average wages in GCC private labour markets remain on levels that are uniquely low given the levels of development and relative technological sophistication of the GCC countries. Public sector wages are significantly higher in all cases on which we have data, resulting in higher reservation wages for nationals in the private sector. While nationals are generally paid better in the private sector than expatriates, their pay is for the most part still worse than in the public sector. Figure 12 illustrates this double wage gap in the example of the UAE.

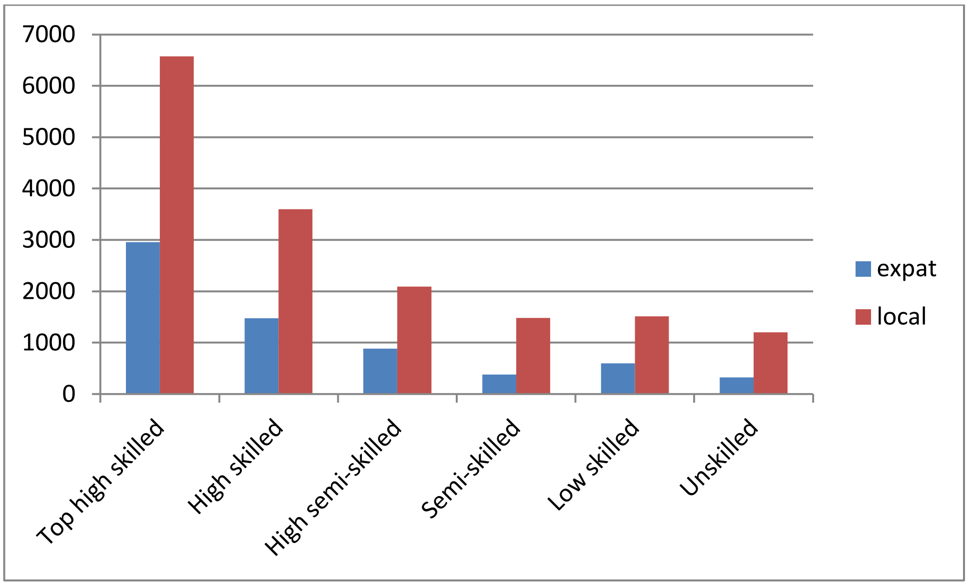
Even controlling for skill level, the gap between local and expatriate wages in the private sector remains considerable (Figure 13).

Figure 12. *Average earnings gaps in the UAE labour market (USD per month), 2008*



Source: Based on Employment Hours and Wage Survey 2008.

Figure 13. *Monthly earnings by skill segments in the UAE private sector (USD), 2008*



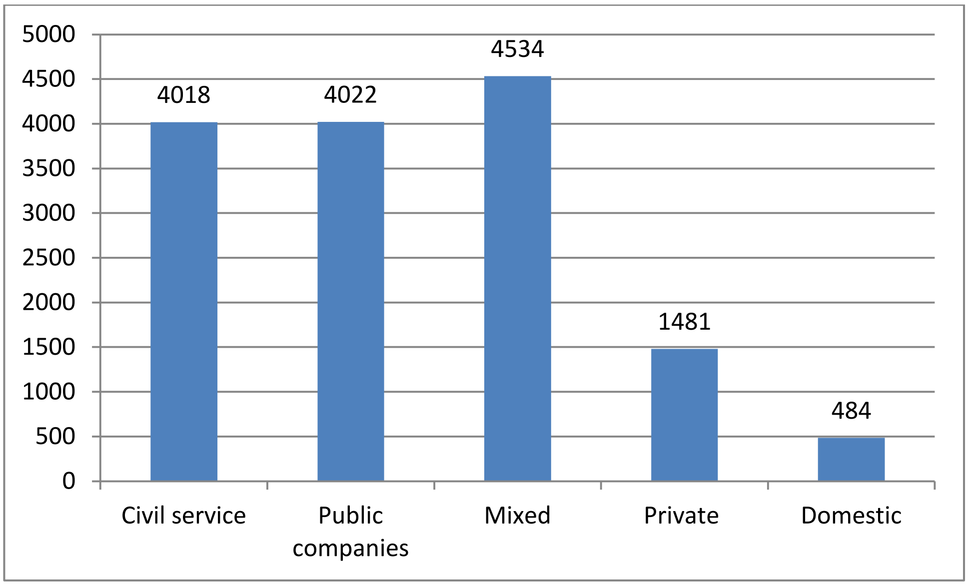
Source: BASED on UAE Employment Hours and Wage Survey 2008.

The wage gap between public and private sector is considerable in Qatar too (Figure 14).[8]

Kuwaiti data on national vs. expatriate wages in the private sector also confirms a deep segmentation of labour markets by nationality (Figure 15).

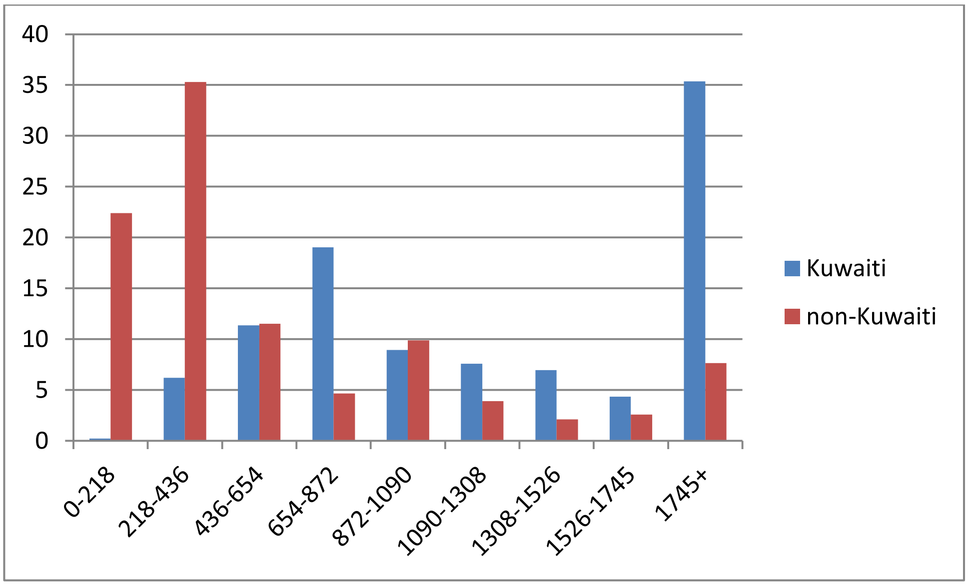
[8] Unfortunately, a breakdown of Qataris vs. foreigners is not available, but as most nationals work in the public sector and most foreigners in the private sector, the overall gap is likely to be similar.

Figure 14. *Average monthly wages in Qatar (USD), 2009*



Source: Qatar Labour Force Survey, 2009.

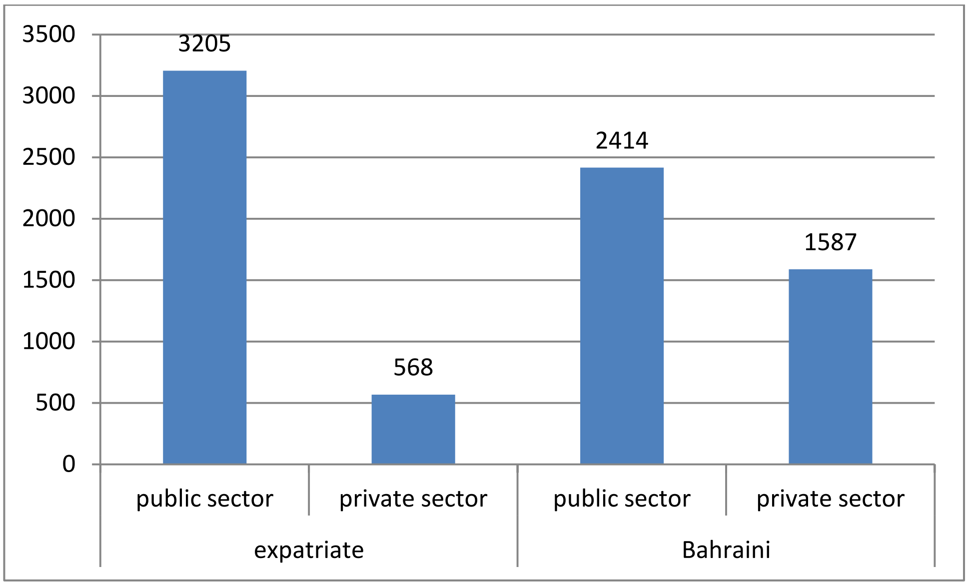
Figure 15. *Percentage distribution of private sector wages in Kuwait by nationality (USD), 2008*



Source: Kuwait Labour Force Survey, 2008.

The gaps are significant even in countries with lower oil rents per capita such as Saudi Arabia and Bahrain: the average salary for Saudi nationals in the private sector is about SR3,000 (USD800), while expatriates earn an average of SR1,000 (USD270). Average wages in the civil service are closer to SR7,000 (USD1,850). In Bahrain, private sector earnings for nationals are somewhat better, but still do not reach public sector levels (Figure 16).

Figure 16. *Monthly wages in Bahrain (USD), Q1/2011*



Source: Bahrain Labour Market Regulatory Authority.

While citizens tend to earn more in private jobs, many employers perceive a gap in productivity between expatriates, who can be hired with extensive training and experience from an international market, and locals, whose benchmark for effort and work conditions is the local public sector (Al-Waqfi and Forstenlechner 2010: 365, 367).

A preference for foreign workers is rational. Yet the focus of private GCC businesses on short-term rent extraction from low-skill, low-cost foreign labour[9] and an aversion to investing in long-term productivity upgrades and skills of local staff have contributed to the exclusion of large sections of GCC nationals from private labour markets (Figure 17). Levels of national labour participation generally are low, and the majority of GCC citizens in paid work are employed in the public sector, where politically determined over-employment is rampant (Tzannatos, Haq and Schmidt 2011: 12).

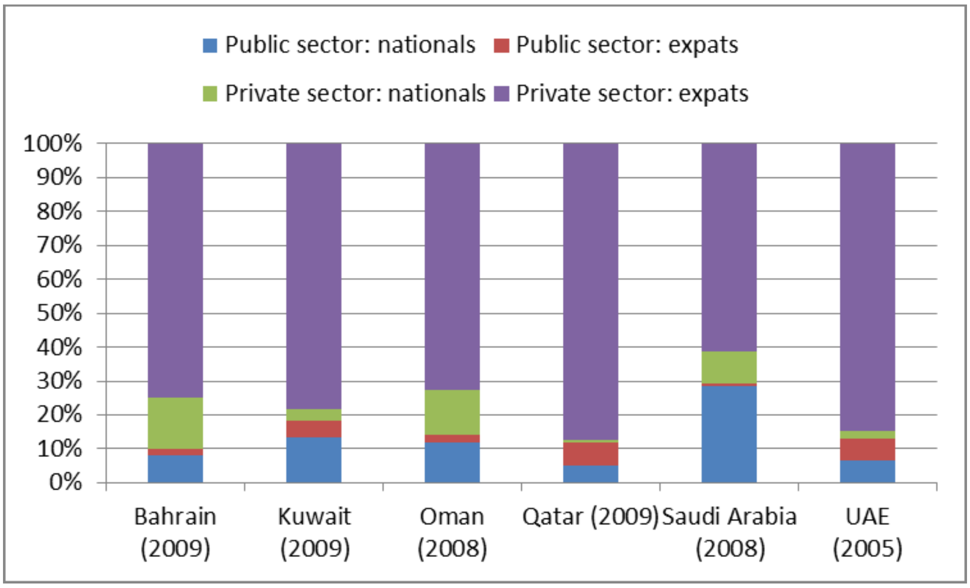
Most jobs that are created during periods of high growth tend to go to foreign workers, and to the extent that nationals are employed, this is as often the outcome of administrative interventions of forced 'Saudization', 'Kuwaitization', 'Omanization' etc. as it is of genuine job creation.[10] Business for the most part has been fighting this nationalization agenda tooth and nail, as it increases costs and saddles them with more demanding employees that are much harder to dismiss.

[9] Low-skill labour in the GCC by most estimates is paid far below its marginal productivity, even if the latter is low to start with.
[10] See Hertog (2012a) for an overview of nationalization policies. See also ch. 6 on Saudization in Hertog (2010a).

In the countries where nationals have at least some presence in the private labour market (Bahrain, Oman and Saudi Arabia), the work motivation of the national labour force ranks high on a list of fifteen business obstacles that local companies were surveyed about (Table 1).

GCC businesses' relationship with the (would-be) national working class is generally antagonistic, even more so than in other economies: local companies are trying to minimize the employment of nationals, which is often perceived as a burden and, to the extent that it is

Figure 17. *Segmentation of GCC labour markets by sector and nationality*



Sources: Bahrain Labour Market Regulatory Authority, Bahrain Labour Market Indicators, 2009; Kuwait Public Authority for Civil Information, 2009; Oman Annual Statistical Yearbook, 2009; Qatar Labour Force Sample Survey, 2009; SAMA Annual Report,2009 (Tables 18.8 and 18.10); UAE Tanmia Human Resource Report, 2005.

Table 1. *Ranking of 'poor work ethic in the national labour force' among fifteen obstacles to doing business in the GCC*

Country	Ranking
Bahrain	2
Kuwait	7
Oman	4
Qatar	10
Saudi Arabia	6
UAE	7

Source: World Economic Forum Arab World Competitiveness Report, 2010.

obligatory, a tax.[11] Conversely, there is much popular disenchantment with a business class perceived as fat cats who do little to provide decent jobs for nationals. As we will see in section 3, the once politically prominent merchant class has become marginalized in the public political space in the countries where there is a modicum of political contestation.

The dominance of foreigners in private labour markets means that much of the business diversification since the early 1980s has passed by national populations, especially in the richer GCC countries of Kuwait, Qatar and the UAE. In the UAE, even ‘good’ private sector jobs paying more than AED10,000 per month are occupied by foreigners in nineteen out of twenty cases.[12]

For nationals, the public sector remains the most promising employer and, in its more efficient bits, the most effective developer of the national labour force. Outside of finance, the only technologically advanced companies that provide high value added and remunerative jobs for a significant share of nationals are government-owned. They include heavy industry giants like Saudi Basic Industries Corporation (SABIC), Aluminium Bahrain and Dubal, technology companies like Abu Dhabi’s Mubadala and Advanced Technology Investment Company (ATIC) or service companies like Etisalat and DP World.[13] Most private sector jobs pay badly, demand low skills and are only marginally productive.

Do the huge numbers of employees in the private sector at least create local demand that could put the private sector on a more autonomous growth path? Unfortunately that is not the case: due to the very low prevailing salaries among expatriates, and the small number of privately employed nationals, the combined share of expatriate and local private sector wages in GDP is only 7 per cent in Saudi Arabia, with Saudis accounting for 3 per cent, and expatriates for 4 per cent. In the UAE, private salaries seem to have accounted for only about 11 per cent of GDP in 2008, almost all of which is accounted for by foreign employment.[14] Even in Bahrain, a country with a fairly small government sector and a comparatively

[11] Interviews with businesspeople in Kuwait, UAE and Saudi Arabia, 2004–11.

[12] Calculated based on data from the 2008 Employment Wage and Hours Survey.

[13] While nationalization levels in these entities there are generally lower than in the civil service, they are considerably higher than in the private sector (e.g. SABIC’s Saudi operations are more than 80 per cent Saudized, Abu Dhabi’s ATIC is 40 per cent Emiratized, while the ratio for Etisalat is 36 per cent). The experience of these ‘national champions’, which have helped to build up an impressive technocratic cadre of nationals, has by and large not spilled over into the private sector, however. They are in fact usually run largely separately from both the rest of business and the rest of the bureaucracy, and it seems to be this very insulation that explains some of their success (Hertog 2010c). Their total employment relative to both public and private sectors at large is small, moreover: e.g. Etisalat employed 3,600 UAE nationals in early 2010, ATIC employed 40 UAE nationals in 2011, and SABIC employed some 11,000 Saudis in 2006, which pales relative to total state employment estimated at above 2 million.

[14] Based on an average private sector salary for expatriates of AED2,600 per month and an estimated 4 million foreign workers (employment of nationals in the private sector is negligible, at about 20,000–30,000 individuals).

developed private labour market, the private wage share only reaches 16 per cent of GDP, more than half of which is again accounted for by foreigners. This compares with a private wage share of around 50 per cent in developed economies. The GCC ratios in fact overstate the importance for local demand creation, as the majority of expatriate wages are in fact remitted abroad and not recycled locally.[15]

Despite a sizeable private sector share in GDP, private demand generation hence remains quite limited. This means that in most GCC countries, an unusually large part of consumer demand is in fact financed through state salaries and transfers; in the Saudi case, the total size of state salaries is about twice as large as that of all private salaries combined. Despite huge private employment numbers, the private sector generates little autonomous demand. This has helped GCC economies during the recent crises, which did not affect state employment – instead, governments in fact increased salaries significantly across the region. At the same time, it means that the private sector relies on continuing large-scale indirect stimuli from government.

Cheap foreign labour has historically been a comparative advantage for the Gulf, and allowed the region to build up its infrastructure and public services rapidly during the first oil boom. Nowadays, however, local populations are much larger and there is a political need to accommodate growing numbers of nationals with higher wage expectations in the private sector. As the latter fails to deliver jobs for locals, there is increasing friction. Without significant employment for locals or tax contributions, GCC business has no organic function in the Gulf social contract, which is built on state employment and other forms of state-orchestrated rent distribution.

In addition to excluding nationals from the private economic cycle, current employment patterns also hinder productivity upgrades and moves into more technology-intensive production based on higher skills. It is too easy to generate returns by relying on unskilled and semi-skilled labour from the developing world as low-tech, but cheap and easily controlled input.

2.3. Input subsidies and other state support

Labour is not the only production factor that is available cheaply as a result of generous government policies. GCC governments have also made capital, energy and infrastructure

[15] By the end of 2009, an estimated USD32 billion were remitted out of the GCC by about 12 million workers, resulting in a per capita remittance of USD2,700 (Taghavi 2011: 12). This is close to the average wage of expatriate workers in Saudi Arabia (USD3,200), and the UAE (USD4,300), indicating that very little is consumed locally.

available at low or sometimes no cost, which has been especially important for the local manufacturing sector, and which has been used in lieu of the protective tariffs used to nurture industry in poorer jurisdictions.[16] Cheap capital and energy can again be conceived as a comparative advantage resulting from the GCC's rich factor endowment, but their cheap supply comes at a long-term cost and, in the case of energy, has recently met hard constraints. GCC economies rely on exhaustible resources; giving business incentives to focus on factor-intensive production is a policy that is not sustainable in the long run.

The GCC has a strong tradition of state-supported industrial infrastructure and inputs, which have been managed better than in most other oil-rich countries and have led to significant diversification in manufacturing. Industrial cities with very low rents, the provision of cheap utility services including gas, electricity and (desalinated) water, and concessionary loans have allowed both private and public companies to expand rapidly into areas like petrochemicals, aluminium, construction materials and plastics.[17]

Like East Asian 'developmental states', GCC governments have for the most part provided impressive industrial and transport infrastructure for their private sector (see the World Economic Forum (WEF) ranking in Table 2).

Industrial estates, ports, roads, airports, pipelines and utility networks have been expanding rapidly, in particular during the 2000s boom decade. While GCC governments only get middling scores for their regulatory capacity on most international rankings, they have traditionally been quite good at rolling out large infrastructure and industry projects, which can be initiated and steered by a small technocratic elite (Hertog 2010a, 2010c).

Table 2. *GCC infrastructure rankings among 139 countries*

Country	Ranking
Bahrain	27
Kuwait	60
Oman	33
Qatar	25
Saudi Arabia	28
UAE	3

Source: World Economic Forum Arab World Competitiveness Report, 2010.

[16] Applied weighted average tariff rates in the GCC in 2009 lay between 3 and 4 per cent, indicating low levels of customs protection (World Bank Development Indicators).
[17] For an overview of the Gulf industrialization model, see Luciani (2012a).

A potentially more problematic feature of state support is the provision of cheap loans to private companies through public funding agencies like the Emirates Industrial Bank, the Kuwait Industrial Bank, the Qatar Development Bank or the Saudi Industrial Development Fund, which have more recently been joined by a host of government funding agencies for small and medium enterprises.

Concessionary loans from such bodies have helped to create sizeable private industries within just a few decades. They have, however, arguably also crowded out private funding and have generally been less conditional on technological content and diversification than in non-oil developmental states.[18] Much of private manufacturing remains focused on basic products like cement, bulk petrochemicals, basic plastics or subsidy-dependent agro-industrial products (Mueller 2012; see the next section for statistics on the technology content of GCC non-oil exports).

Probably the most important form of state support for local industry, however, has not been infrastructure and loans, but the provision of cheap industrial feedstock, electricity and water – far below internationally customary market prices and often even local production costs.[19]

The price of gas as a feedstock has been kept particularly low, at less than 20 per cent of what is customary in other markets (Figure 18).

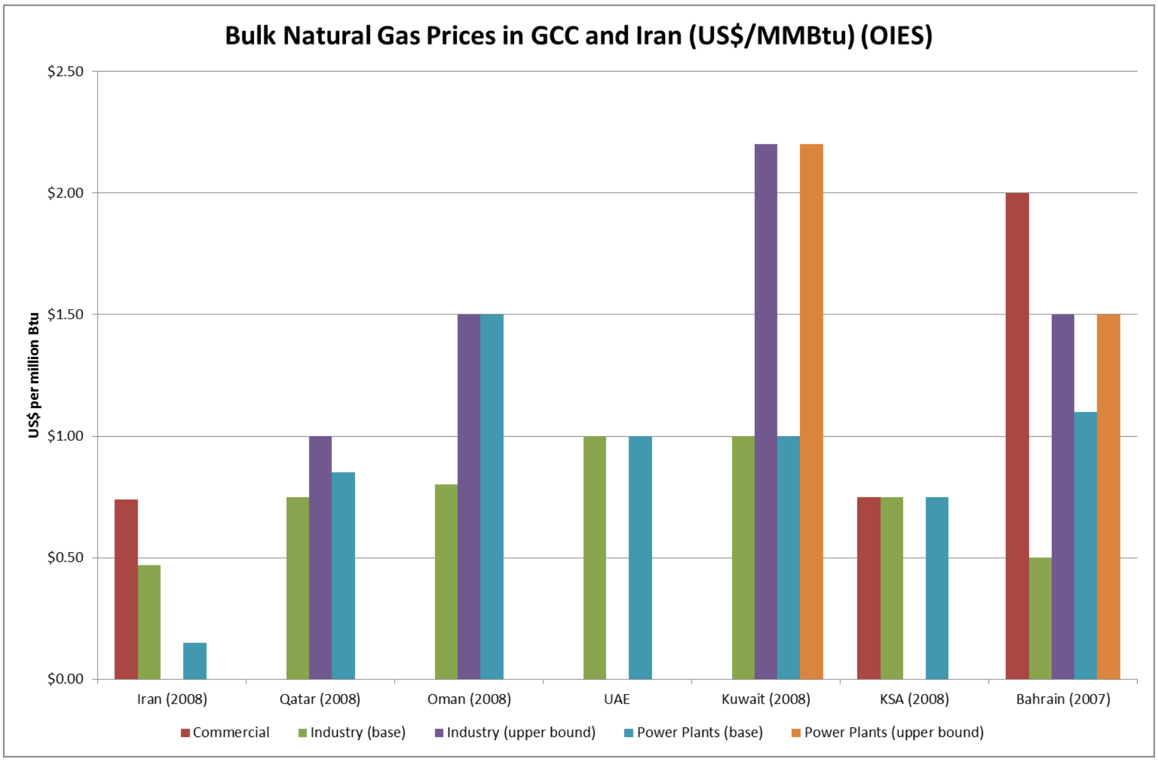
Cheap gas has been used both to produce electricity for energy-intensive manufacturing like aluminium production and as a bulk feedstock for petrochemicals industries, which in turn have spawned downstream industries like plastics, in which private players play a prominent role.

Electricity prices too have been kept far below international levels. While residential consumption by citizens is served at the cheapest prices, industrial prices are only marginally higher. Prices range from zero (e.g. for national residential consumption in Qatar) to about 10 cents per kWh, while European prices typically lie above 20 cents (Figure 19).

Prices for water (usually produced in energy-intensive desalination plants) and transport fuels are similarly low. Much of the growth in GCC manufacturing since the 1970s is attributable to such support policies.[20] Such heavy state support has been useful for kick-starting export-oriented industries, and for a long time faced low opportunity cost in an age of

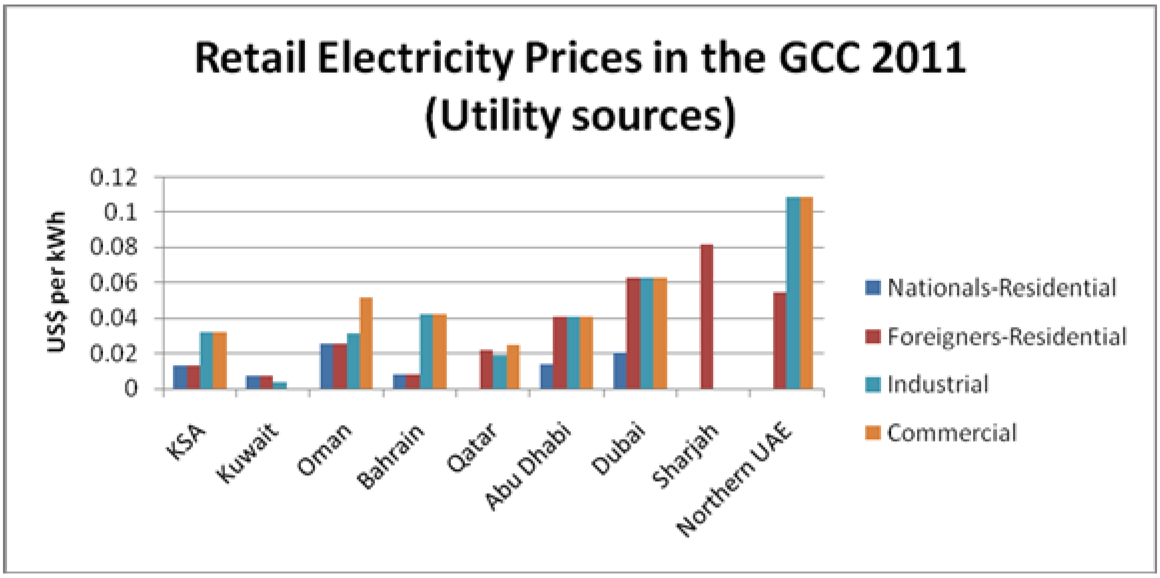
[18] On the importance of the state's capacities to target support policies and make them conditional on technological and sectoral upgrading, see Chibber (2006).
[19] For a differentiated discussion cf. Luciani (2012b).
[20] The share of manufacturing in GCC economies increased from 4.5 per cent of GDP in 1975 to 9.5 per cent in 2005 (Mueller 2012); unfortunately a breakdown into public and private is not available.

Figure 18. *Bulk natural gas prices in the GCC and Iran (USD/MMBtu)*



Source: Jim Krane/Oxford Institute for Energy Studies (OIES).

Figure 19. *Retail electricity prices in the GCC, 2011*



Source: Jim Krane.

low international oil prices, ample spare production capacity in the GCC hydrocarbons sector, and easy availability of associated gas as a by-product of oil production. The policy is now facing resource constraints, as gas is becoming scarce and expensive to develop, while domestic consumption of gas, both directly and for electricity generation, continues to rise rapidly (Table 3).[21]

While opportunity costs of heavy resource use are rising fast, user prices remain low, incentivizing the private sector to remain on a resource-intensive, low- to mid-tech development path. Much to the grief of national oil companies who have to provide domestic industry with low-price oil and gas, private industrialists remain for the most part focused on simple products with low technology content and limited value added, arguably deriving much of their profit from international factor price arbitrage (Mueller 2012).

This is not to say that the heavy industry in the GCC is not well run, and that there was no historical justification for low input prices. Yet current patterns of resource-intensive production remain dependent on continued low prices, while gas and electricity production have reached hard capacity constraints. It is worth pointing out, moreover, that despite the emergence of many mid-size private manufacturers in important areas like basic plastic products or construction materials, in most strategic areas of heavy industry, state companies continue to dominate. In Saudi Arabia, majority state-owned SABIC alone accounts for almost three quarters of all foreign earnings of all publicly listed companies (Jadwa Investment 2011), and in the UAE and Qatar, there is no significant involvement of the local private sector in petrochemicals at all. State-owned heavy industry is of course as dependent on cheap feedstock, but it is again a state-owned company, SABIC, that has made the most serious attempt to move away from bulk petrochemicals and feedstock price arbitrage towards technology-intensive production, through its acquisition of GE Plastics in 2007.

Table 3. *Domestic gas consumption in the GCC (billion cubic feet), 2000s*

Country	2000	2009	Growth
Bahrain	303	444	47%
Kuwait	339	437	29%
Oman	221	520	135%
Qatar	532	745	40%
Saudi Arabia	1759	2770	57%
United Arab Emirates	1110	2086	88%
Total	4264	7004	64%

Source: US Department of Energy-Energy Information Administration (DOE-EIA).

[21] While the rationale for cheap provision of energy varies from one type of industry to the next, the resource constraints on gas are general; see Luciani (2012b). On current and future domestic energy constraints in Saudi Arabia see Stevens and Lahn (2011).

GCC manufacturing on many accounts is a success, but it continues to depend on contingent state support. Given local capacity constraints on the oil and gas front, business consumption of cheap gas, gas-derived electricity, water and transport fuels is increasingly in rivalry with that of residential consumers – the same residential consumers who for the most part are excluded from private employment by local industrialists.

2.4. Contributions to 'knowledge economies' and innovation

We have seen that private sector growth in the GCC has been factor-intensive, relying on comparative advantages in factor prices resulting from a number of state support policies. The flipside of this growth model is weak incentives for upgrading productivity, investing in technology and engaging in research and development – the ingredients required for a move towards the much vaunted if ill-defined 'knowledge economy' that all GCC governments officially aspire to.[22]

In fact, the productivity of average jobs in the GCC has by and large declined since the 1980s (Figure 20),[23] as low-skill labour (often of Asian origin) has substituted for mid-skill labour (often of Arab origin; Kapiszewski 2006: 6–10). Open labour migration has allowed GCC businesses to expand production through increasing labour inputs instead of augmenting in the productivity of the existing labour force as is usually the case in the supply-constrained labour markets in the rest of the world.

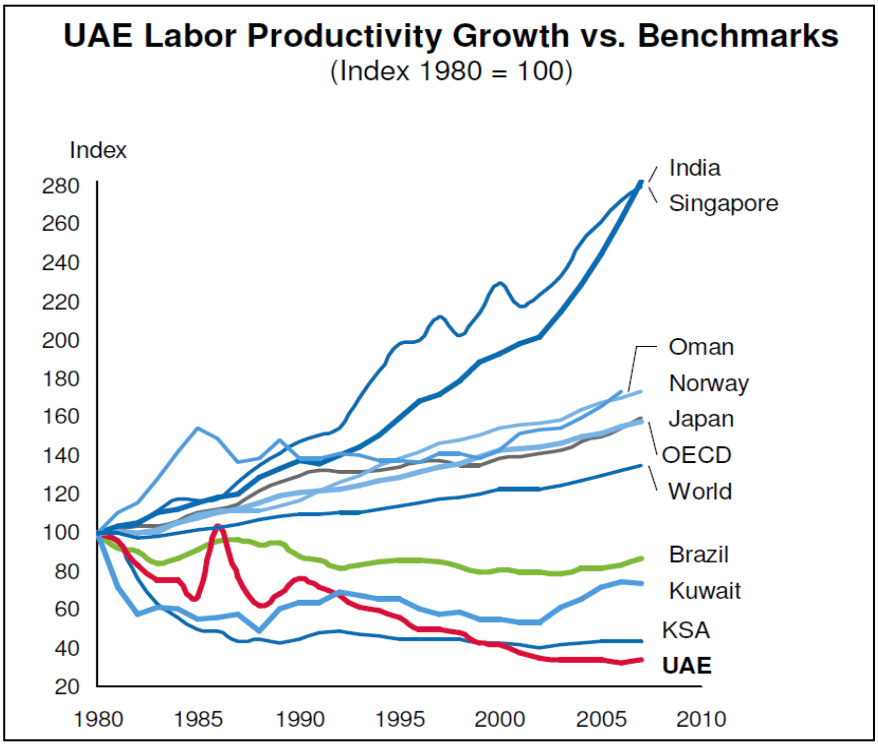
Tables 4 and 5 show that much of GDP growth in the GCC is historically explained by increased use of production factors like labour and capital, rather than improvements in human capital or in 'total factor productivity', a residual category that includes technological improvements. More recently, and after two decades of decline or stagnation, total factor productivity (TFP) has seen growth in some of the GCC countries (Bahrain, Kuwait and the UAE). Some of this could be caused by expansion in the oil sector, however, which is unfortunately not separated out in available analyses,[24] and in any case, labour productivity remains very low by international standards. The private sector's large capital outlays have

[22] For the purposes of the discussion here, 'knowledge economy' will be taken as forms of production characterized by high labour productivity and high technology content.

[23] The relative growth in Omanis likely to have to do with the very low starting point, as the country entered large-scale development later than its GCC peers. Private sector wages in general, but also for nationals, remain among the lowest in the region: 74 per cent of nationals earn less than OMR200 (about USD520) per month in the private sector, lower than anywhere else in the GCC (Sultanate of Oman 2010: ch. 5).

[24] GDP here is measured in real terms, and hence direct effects of the hydrocarbons sector on GDP occur only if produced quantities change (as they did in the 1980s and 1990s–2000s with production declines and increases respectively).

Figure 20. *Comparative labour productivity growth in four GCC states and select international cases, 1980–2010*



Source: Booz & Co.

Table 4. *Various production factors' contribution to GDP growth in the GCC and select international cases (IMF estimates), average growth rates 2000–7*

Country	GDP	Capital	Labour	Human capital*	TFP
GCC					
Bahrain	5.6	2.4	0.9	0.4	1.9
Kuwait	5.8	3.0	1.8	0.1	0.9
Oman**	4.4	3.3	1.8	0.4	−1.1
Qatar	9.2	7.2	2.8	0.5	−1.3
Saudi Arabia	3.5	2.0	1.9	0.7	−1.0
UAE	8.8	2.7	3.0	0.9	2.2
Select advanced countries					
Norway	2.6	0.9	0.5	0.7	0.6
Singapore	6.0	1.1	1.6	0.5	2.8
USA	2.4	1.2	0.7	−0.3	0.7

Source: Qatar: 2010 IMF Article IV Consultation –Staff Report.

Notes. The figures for the UAE (and to a lesser extent Saudi Arabia and Kuwait) in Tables 4 and 5 appear somewhat at odds with Figure 20, which is probably due to different assumptions made on the size and growth of the expatriate labour force. TFP = total factor productivity. .* Human capital is defined in terms of years of schooling of the workforce. ** Human capital growth for Oman is imputed from the GCC average.

Table 5. *Various production factors' contribution to GDP growth in the GCC (IMF estimates), 1970–99*

Country	GDP	Capital	Labour	Human capital*	TFP
1990–9					
Bahrain	3.4	0.5	1.5	1.0	0.4
Kuwait	−7.8	0.9	−2.2	0	−6.5
Oman**	5.6	1.7	2.8	0.5	0.6
Qatar	6.6	2	1.5	0.5	2.6
Saudi Arabia	3.2	0.8	2.1	0.6	−0.2
UAE	5.9	2.1	3.6	1.2	−1.0
1980–9					
Bahrain	1.3	1.4	2.7	0.8	−3.6
Kuwait	−0.7	2.4	3.3	0.7	−7.1
Oman**	6.4	4.9	2.6	0.7	−1.7
Qatar	2.6	0.0	4.4	0.4	−2.3
Saudi Arabia	−1.0	1.4	3.9	0.8	−7.1
UAE	1.4	3.6	3.3	0.9	−6.4
1970–9					
Bahrain	6.5	1.8	4.5	1.1	−0.8
Kuwait	1.2	3.1	3.6	0.8	−6.3
Oman**	10.6	4.6	2.5	0.8	2.8
Qatar	6.8	1.1	4.0	0.5	1.2
Saudi Arabia	13.6	2.8	2.8	0.7	7.3
UAE	-	-	-	-	-

Source: Qatar: 2010 IMF Article IV Consultation – Staff Report, pp. 47–8.
Notes. TFP = total factor productivity. * Human capital is defined in terms of years of schooling of the workforce. ** Human capital growth for Oman is imputed from the GCC average.

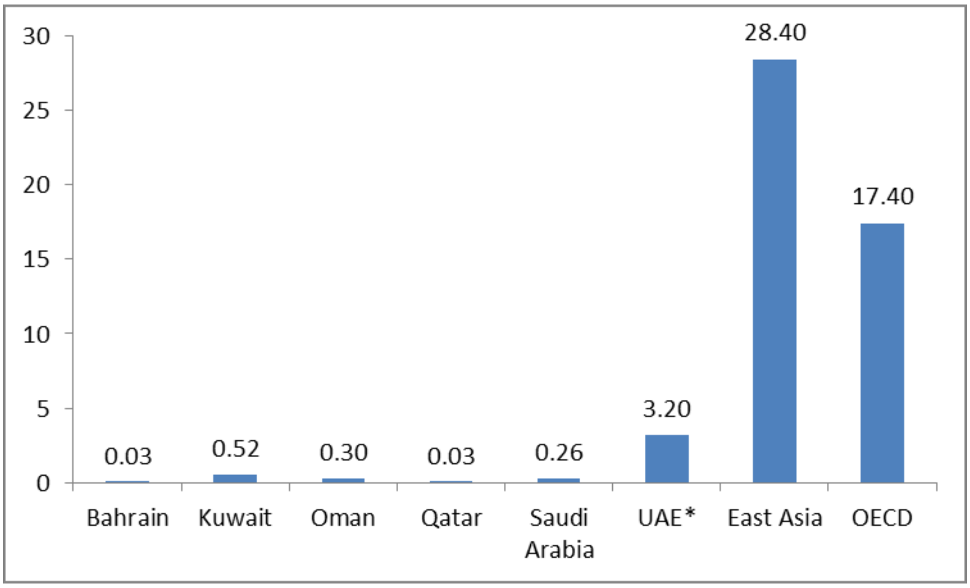
often gone into housing, land and real estate infrastructure rather than into technology acquisition.

None of this is to say that GCC businesses are run badly. But they by and large rely on simple technologies, and their contribution to knowledge economy, research and innovation is very limited. |Unlike the case with successful East Asian industrializers, state support in the GCC has by and large not been conditional on technology upgrades, and the GCC has witnessed none of the resource scarcity that has forced advanced Asian manufacturers to invest into technology (Chibber 2006; Evans 1995; Wade 2003). The share of high-technology exports in total GCC manufacturing exports is orders of magnitudes lower than in other world regions. This would be the case even if the analysis were limited to non-oil exports (Figure 21).[25]

Research and development (R&D) in the region is still inchoate. Technology clusters around specific industries have not yet developed, and links between business and local universities are weak. R&D expenditure was 0.11 per cent of GDP in Kuwait in 2009, 0.08 per cent in Saudi Arabia and less than 0.1 per cent in the UAE.[26] It is closer to 2 per cent in OECD countries. Very few international patents emerge from the GCC.

To date, more ambitious strategies of technological development and diversification into high-tech sectors are mostly limited to government-owned companies that can rely on implicit sovereign backing to engage in longer-term strategies of research and product development (Hertog 2010c). Examples include the investment of SABIC in materials research and national human resource development, or the efforts of Abu Dhabi's ATIC in building up a local semi-conductor industry through large-scale local recruitment and training

Figure 21. *Share of high-tech exports in total manufacturing exports in the GCC and select international cases (%), 2009*



Source: World Bank Development Indicators.
Notes. The World Bank defines high-technology exports as 'products with high R&D [research and development] intensity, such as in aerospace, computers, pharmaceuticals, scientific instruments, and electrical machinery'. * UAE data from 2008.

[25] The higher UAE figure might be explained with re-exports of technology goods via Dubai rather than with local production. The available annual figures for the country fluctuate wildly between 0.03 per cent and 3 per cent, with no clear trend discernible.
[26] Sources: UNESCO for Kuwait and Saudi Arabia; the *National*, 29 September 2011, for UAE.

efforts. These efforts to build up a knowledge economy might fail, but at least a serious attempt is made to push into high-tech production – something that cannot yet be said about the private sector.

2.5. Corporate governance and the public's exclusion from private sector wealth

Factor-intensive and relatively low-tech growth combines with corporate governance structures that also tend to lag behind international standards, which in turn makes it harder to recruit top talent and attract technology partners internationally. While recent economic crises have renewed local interest in governance issues, management structures often remain informal and business transactions relationship-based, which increases barriers of entry to newcomers. This is to some extent related to the fact that most corporate wealth in the GCC is privately held, often as part of informally governed family empires. The patrimonial nature of Gulf business wealth not only makes the adoption of modern corporate governance structures harder, it also excludes the local public from partaking in the returns of the private sector.

Some of the privately held family companies in the GCC are very well run, but others suffer from significant governance deficits. This has become obvious in the course of several recent high-profile scandals involving Gulf family businesses, most prominently the conflict between the Al-Gosaibi Group and the Saad Group in Saudi Arabia. Many family businesses are struggling to come to grips with succession issues as well as the separation of management and ownership, of family disputes from management decisions and of family from company assets. Many of them remain far-flung conglomerates without a clear sectoral focus or core competence. Many Gulf family businesses are currently approaching the transition to the third generation of owners, which due to the sheer number of individuals involved can be complex and has already led to the breakup of several companies.[27]

Initial public offerings for new public companies are still fairly rare in the region and often involve only peripheral parts of existing family businesses. In the wake of the global financial crisis, GCC stock markets have seen very few initial public offerings (IPOs). The total volume of GCC IPOs in 2010, 2011 and the first half of 2012 reached USD2 billion, USD800 million and USD1.2 billion respectively (GCC Financial Market Quarterly 2012; Sharrouf 2012; Basit 2012). Relative to a total capitalization of about USD800 billion, these are very small additions. A broader base for a 'popular capitalism' that could link the private sector with wider strata of shareholders is lacking to date, as is deeper involvement from

[27] Interviews and discussions with GCC family business leaders, 2008–11. For a general overview of Gulf family businesses, see Davis, Pitts and Cormier (2000).

institutional investors representing broader social interests such as pension funds. The latter often prefer to hold shares in larger companies that are part state-owned.

Most private sector companies remain financed through bank loans or retained profits. The 'free float' of actively traded shares on GCC stock markets remains relatively small (Sedik and Williams 2011: 20). Government still accounts for almost a third of total shareholdings (Raghu 2010). The seven largest listed companies in the GCC – SABIC, Al Rajhi Bank, Etisalat, Industries Qatar, Zain, Saudi Telecom and the Qatar National Bank (QNB) – all have the government as a significant, often majority, shareholder, and most of them used to be fully state-owned. The introduction to this paper mentioned that of the top thirty Arab listed companies in 2011, twenty-five were located in the Gulf – but nine of these have local governments as majority shareholder, while twelve have minority government shareholdings. Twelve of the twenty-five companies were originally set up by the government or as daughters of state-owned companies. There are few purely privately held blue-chip corporates in the Gulf; the largest private sector groups are not listed.

There are of course listed companies that are truly private, but many of those do not yet operate in accordance with international corporate governance standards. The GCC Board Directors Institute conducted surveys about disclosure and corporate governance practices of the 200 largest listed companies in the GCC in 2009 and 2011. Of these 200, only eighty-five provided annual reports on their website or on request from the Institute in 2011 (GCC Board Directors Institute 2011). Of these annual reports, many did not contain standard information that is usually made available to shareholders in mature markets[28] – although it is worth mentioning that non-disclosure has declined significantly since 2009, possibly as a result of the increased attention paid to governance issues in the wake of global and regional economic crises (Table 6).

Many GCC company board members also are unclear about the exact division of labour between board and management, and very few boards undergo performance evaluation (GCC Board Directors Institute 2011: 28, 42).

Even among listed companies, a limited number of families control a significant share of board seats: research by the Hawkamah Institute in Dubai shows that the top five families in the respective countries control between 10 per cent and one third of all board seats among listed companies; the top fifteen families between 18 and 50 per cent (TNI, Hawkamah and

[28] In Europe, most types of information mentioned in Table 6 are provided by at least 80 per cent of listed companies (GCC Board Directors Institute 2011: 19).

Table 6. *Share of listed GCC companies making different types of information publicly available (%, n = 85), 2009 and 2011*

Type of information	2011	2009
Remuneration of board members	76	81
Other positions held by board members	49	32
Frequency of board meetings	54	27
Number of independent directors	43	10
Board meetings attendance rate	39	8
Company shares held for each director	24	1
Instrument of remunerating directors	7	1

Source: Selection from GCC Board of Directors Institute (2011: 17).

IOD Mudara 2008). This points to a fairly small and tightly knit economic elite, which can give rise to potential conflicts of interest.

The local shareholder culture, which could force improvements in disclosure and governance, generally remains weak. It is again often the leading state-owned enterprises (SOEs) which are at the forefront of the disclosure and corporate governance debate in the Gulf. While many GCC SOEs suffer from significant governance problems, the better state companies are among the leaders of the regional corporate governance debate: most of the participants in the events of the GCC Board Directors Institute appear to have been SOE representatives, and four of the five founding partners are current or former state companies.[29]

To what extent do recent crises generate pressures for upgrading GCC corporate governance structures? We have already seen that disclosure practices have somewhat improved since 2009. Perhaps more importantly, banks have become much more reluctant to engage in 'name lending', that is, the provision of loans purely on the basis of a merchant family's name, without detailed checks of its accounts and business plans (Raghu 2012: 4). After defaults by several important family businesses like Gosaibi, Maan Al-Sanea and Al Jaber, as well as a number of investment houses backed by large families, there will be more stringent demands for information and accountability from creditors – even if most of this

[29] The vast majority of company participants on two photos of the main corporate governance events in the Board Directors Institute's 2011 report are SOE representatives (GCC Board Directors Institute 2011: 7, 15). Among the five founding corporate partners, one is fully state-owned, two are majority state-owned and one used to be majority state-owned; http://www.gccbdi.org/corporate-partners.

information will remain private. This could force businesses to consolidate, focus on and deepen core competences, and potentially go public with some of their operations.

There has also been some tightening of capital and real estate market regulation after recent crises. Due to credit constraints among large European banks, the local project finance market is gradually maturing to provide alternative sources of capital for capital-intensive projects, notably through Islamic sukuk bonds which in principle are available for retail investors (Hamdan 2012).

Broader financial alternatives that could shake up the private sector and enable the entry of new players however are still lagging: venture capital in the Gulf is almost non-existent with the exception of a few state-supported small and medium-sized enterprise (SME) investment programmes (Hertog 2010d). The Gulf private equity sector, which could lead to the emergence of new corporate champions and, in the mid-term, an increase in IPOs, remains in an anaemic state. Reasons for this include families who do not want to cede any control over their assets, tend to over-value their own companies, prefer to approach relatives for money rather than outsiders, and struggle to bring on board all major players within the family even if there is an interest in bringing in outside capital (Al-Sayegh 2012; Saudi Gazette 2012b). For similar reasons, markets for mergers and acquisitions in the region remain limited. GCC economies continue to be relationship-based and barriers to entry remain high.

Recent rounds of financing for local corporates reflect family preferences for retaining full control or at least not divulging any information to the public: many bond issues are private rather than public, reducing pressure for disclosure and modern corporate governance.[30] Under pressure due to tighter local credit markets and losses in their international investment portfolios, families now often draw on private family funds to sustain their businesses in order to avoid bank finance or equity dilution, resulting in further blurring of family and company governance (INVESCO 2012: 19–20). Many distressed GCC companies continue to exist in a zombie state instead of going through a modern insolvency procedure, which in most jurisdictions is not available. Even when governance reforms in the private sector happen, they are often focused on internal management practices, not public disclosure or listing of assets or debt that would link them to broader shareholders.

In the mid- to long run, there is potential for a bifurcation of the Gulf private sector, in which some remain in the mould of patrimonial conglomerates, while others adjust to global

[30] For an overview of private issues in the wake of the global financial crisis see Capital Standards (2010).

and local crises by focusing on core competences, admitting external shareholders and adhering to modern corporate governance standards.

For the time being, however, the corporate governance culture in the Gulf remains relatively weak, preventing the emergence of world-class private sector groups and also undermining the private sector's claim to be a leader of modernization and national development. Weak corporate governance, of course, is typical of emerging markets; moreover, recent trends in corporate disclosure of listed companies have been positive. Much of the push for better governance, however, has been led by state-owned companies rather than private sector leaders. Due to the large share of corporate wealth that is unlisted and private, nationals remain to a large extent excluded from investment in the local private sector. Among companies whose stocks are publicly traded, the most professional ones have often been set up by government rather than the merchant class.

2.6. Role in economic policy-making

Company-level governance of much of the GCC private sector might remain patrimonial. In other regions, this has not prevented the private sector from playing an important and proactive role in economic governance on a national level: family-based groups in Turkey or South Korea, for example, have led powerful business associations and negotiated complex policy deals with government.[31]

As we will see in section 3.1, Gulf business indeed played an important policy-making role in the pre-oil era. It lost much of its policy leadership role subsequently, however, when policy was about distribution rather than regulation. While some national business associations in the Gulf are fairly well organized, their lobbying tends to be reactive and piecemeal in nature. Business has more capacity for collective action than most other segments of society, but it still tends to follow the government lead on economic policy.

GCC governments formally include business in economic policy-making through a variety of corporatist mechanisms, including consultative economic councils and seats for business representatives on the boards of major SOEs and regulatory agencies. In most cases, however, business holds a minority position, and representatives are chosen by the government rather than by business associations, which means that their views do not necessarily reflect those of the larger business class.[32]

[31] For several case studies of well-organized and powerful business associations in the developing world, see Maxfield and Schneider (1997).
[32] Interviews with senior businesspeople in UAE and Saudi Arabia, 2009–11.

Chamber of commerce and industry (CCI) have a fairly long history in the Gulf. They were in most cases created by government, however, and while there are elections to CCI boards in all GCC countries, the government supervises these and in some cases appoints parts of the board membership, notably in Saudi Arabia, Abu Dhabi and Oman.

Chamber boards are often dominated by large local families and in some cases have been criticized as out of touch with the population as well as the business class at large.[33] The Qatar Chamber of Commerce and Industry (QCCI), which is headed by a member of the ruling family, has come under repeated attack from the generally docile local press. The charges include being interested only in the defence of monopoly privileges, thus neglecting its tasks in education, in product certification, in price regulation and in improving the private sector's competitiveness. The chamber has been ridiculed for not even publishing a journal (Peninsula 2011b; Pandit 2011).

Other institutions have a stronger organizational tradition. Perhaps the most active one is the Jeddah Chamber of Commerce and Industry (JCCI), Saudi Arabia's oldest chamber, whose programmes include SME support policies, labour market matching services and support for female entrepreneurship. Yet even JCCI has limited outreach in the wider business community. The last board elections in 2009 recorded the highest turnout to date of any Saudi chamber election, yet only 6,400 of a total of 32,000 chamber members went to the polls (Al-Jassem 2009). The poll, conducted under restrictive new rules imposed by the Ministry of Commerce, involved widespread allegations of vote-buying, damaging the institution's reputation (Arab News 2009).[34]

Chambers and other business associations in the GCC generally have limited policy research capacity and are not involved in the self-regulation and licensing activities that have been delegated to business organizations in some other emerging markets (see Maxfield and Schneider 1997). There are no private sector think tanks of any kind in the GCC. Beyond sector-specific committees within chambers, there are also few sectoral organizations that could represent the interests of specific clienteles like industrialists or the financial sector – possibly a result of many large companies being conglomerates that span many sectors, and of open labour migration obviating the need to coordinate local training initiatives.

[33] For details on the Bahraini and Omani cases see Valeri (2012).
[34] See also WikiLeaks cable 09Jeddah381, Quinn to Department of State, Allegations of vote buying and sorcery on eve of Jeddah Chamber of Commerce Election, http://wikileaks.org/cable/2009/10/09JEDDAH381.html.

What is the content of policy lobbying in the GCC? While in the 1970s and 1980s, private sector elites often demanded increases in government support and protection,[35] business lobbying now is more about preserving existing privileges and staving off government intervention.

In almost all cases, however, lobbying strategies still are reactive rather than proactive, and there are no major cases where organized lobbying with fully formed proposals on complex policy matters has taken place. Policy initiatives often still come from individuals, and state and business rarely engage in sustained, encompassing negotiations on policies.[36] Instead, exchanges are often ad hoc. A survey of local press reports on GCC business lobbying between mid-2009 and mid-2012 reveals the piecemeal and largely defensive nature of (publicly reported) private sector policy input:

- Qatari business politics probably remains the closest to the 1970s pattern of asking for ever-increasing support and privileges. Qatari contractors have repeatedly asked for more government contracts to be reserved for them, recently in the context of construction projects in preparation of the 2022 FIFA Cup (Peninsula 2010b, 2010c). QCCI and other business representatives have spoken out against liberalization of local FDI rules and against equal rights for GCC companies operating in Qatar (a stipulation of the GCC common market) (Oxford Analytica 2009; Peninsula 2011a). QCCI has fought for the retention of the sponsorship system that increases employers' control over foreign labour (Peninsula 2010a). Local press has criticized QCCI for its lack of policy vision and focus on rent-seeking activities (Pandit 2011).
- Bahraini business, most prominently represented through the Bahrain Chamber of Commerce and Industry (BCCI), has also mostly limited itself to defensive lobbying, speaking out against fees on foreign labour and against the relaxation of the sponsorship system (Gulf Daily News 2011c; Toumi 2009). It has repeatedly asked for preferential treatment for local business to compensate for the losses incurred in the course of the uprising that began in 2011 in Bahrain (Gulf Daily News 2011a).
- Saudi chambers have focused much political capital on fighting the (modest) increase of industrial electricity tariffs that happened in 2010 (Arab News 2010a,

[35] See e.g. *Saudi Arabia Monitor*, May 1987, p. 24.
[36] For discussion along these lines covering the whole MENA region, see Benhassine (2009: 187–91).

2010b; Al-Harthi 2010). Individual businesspeople have asked the government for the continued subsidization of local wheat production (Nazar 2010). Businesses have repeatedly spoken out against the government's 'Nitaqat' system of Saudization quotas in the private labour market (Al-Qahtani 2010; Saudi Gazette 2012a; Al-Abdullah 2012). The only proactive lobbying demand on record was one for the creation of specialized real estate courts (Al-Mutairi 2010).

- Like their Bahraini, Qatari and Saudi peers, UAE, Kuwaiti and Omani businesses have asked for the retention of the labour sponsorship system and a slower pace of forced nationalization on the private labour market (Toumi 2011a; Salem 2010; Issa and Al-Lawati 2009; Valeri 2012). While supporting the free trade agreement with the USA, the Omani Chamber of Commerce and Industry has opposed freehold real estate ownership for foreigners (Oxford Business Group 2009), and has asked for cheaper utility tariffs, lower taxes and wage subsidies in the wake of the 2011 political and labour unrest (Muscat Daily News 2011).

In sum, much of the visible economic policy lobbying of GCC business is focused on defending existing regulatory privileges as well as fighting forced increases in national employment in the private sector. There is no record of the type of state–business coordination known from Asian 'developmental states' focusing on joint information-gathering, policy planning and technological diversification. As mentioned above, SOEs tend to lead in the last area, as they do in corporate governance and corporate social responsibility.

Much of the weak coordination is probably also a result of disjointed and unaccountable policy-making on the government side; but business has done little to show that it could be a better policy leader than government. It by and large lacks the core ingredient that the literature on state–business relations posits as prerequisites for close policy coordination: strong peak associations able to represent and discipline their members, engage in credible commitments, gather reliable data and undertake quality policy research (Maxfield and Schneider 1997; Schneider 2004). Unlike what has happened in some other MENA countries, GCC countries have also not seen the emergence of younger, 'dissident' business associations with a more critical policy voice (Benhassine 2009: 188–90). While critical on individual policy initiatives, GCC business generally remains in the shadow of the state and closely linked to its elites.

2.7. Summary

The preceding sections have shown that the GCC private sector is less immediately reliant on state spending than it used to be, has become the main contributor to national capital formation and has been designated by local governments as the main future job provider and key driver of diversification. Yet it remains deeply dependent on direct and indirect recycling of state rents in the long run and thrives off state-provided cheap inputs. It also remains to an unusual extent structurally isolated from the citizenry at large, for which it provides little employment and few taxes or investment opportunities, and with which it competes for increasingly scarce low-price goods and services provided by the distributive state. Large parts of the Gulf private sector do not operate in line with modern standards of corporate governance, and its contribution to economic policy-making is for the most part piecemeal and dilatory. The most impressive corporates in the Gulf are often part or wholly state-owned.

Although much of this might go against conventional wisdom, none of it should really come as a surprise given the historical imbalance of resources between state and business in rentier states and the short history of modern capitalism in the Gulf. Given its late development and weak starting point at the outset of the 1970s oil boom, Gulf business has arguably been doing quite well. Yet it remains state-dependent and structurally isolated, which has important ramifications for the economic and political development outlook of the region.

3. Business in the political arena

This paper has so far discussed the role of Gulf business in economic development and economic policy-making. The remaining sections will discuss the contribution of business to politics strictly speaking. Against the above background, the reader might already expect that the private sector's role here is also overshadowed by the state and that it acts in relative isolation from other social forces. This is indeed the case: Gulf business elites' role as leaders in the wider political arena is quite limited, which explains the relative brevity of the rest of this paper.

There are, however, two larger issues that bear some detailed discussion: first, the strong decline of the Gulf merchant classes' autonomous political role in the longue durée, which reflects shifts in state–society relations and social mobilization after the onset of oil production more broadly; secondly, the recent deployment of private sector elites as frontline props of existing regimes against popular challenges before and during the Arab spring, through which merchant elites have, for better or worse, further tethered themselves to the *anciens régimes* of the region. These two themes will be linked through a short analysis of the private sector's role in the GCC's fiscal sociology which builds on results from the preceding sections of the paper, and which explains much of the fundamental shift from political vanguard to regime client.[37]

3.1. The political history of Gulf business

Compared to the Arab world's republics, which have gone through periods of nationalization and some degree of class warfare, the merchant classes of the Gulf have a longer uninterrupted history. Many of the big names in business go back several generations or even centuries and have historically been not only business leaders, but in many case also social elites and community leaders (Field 1986; Crystal 1995; Azoulay 2012b; Tétreault 2000). Several of the GCC ruling families themselves have a merchant background.

Merchant elites played a fairly well-documented role in pre-oil national politics, when ruling dynasties had to rely on tax contributions from local pearling, trade and agricultural sectors, and when merchants' high degree of mobility gave them considerable bargaining power. Their influence on local politics somewhat weakened when most of the Gulf rulers began to receive stipends and diplomatic support from the British imperial power in the nineteenth century. Yet, in the pre-oil era, local business continued to provide community services and infrastructure that were beyond the capacity of the embryonic states, furthering the businesses' social standing and independence. They were well organized and able to bargain collectively with local rulers over tariff, public service and regulatory issues (Crystal 1995; Davidson 2008; Vassiliev 2000; Onley and Khalaf 2006; Chaudhry 1997).

As hard as it might be to imagine now, merchant elites in the pre-oil era in several countries constituted the spearhead of political opposition against rulers. In as different cases as Bahrain, Dubai and Kuwait, these elites were instrumentally involved in nationalist and parliamentary movements in the twentieth century, pursuing an ostensibly liberal political agenda until the 1950s and 1960s (Crystal 1995; Khuri 1981; Moore 2009; Davidson 2007) – at a time when the wider population in most countries was desperately poor, tied up in networks of clientelism and not capable of independent political action.

The merchants' role in early nationalist movements is not unlike that of young notables and urban elites in other Arab countries in the pre-independence era[38] – who, however, unlike their counterparts in the Gulf, in several cases succeeded in challenging

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[37] The discussion has mostly focused on business elites rather than the private sector at large, because only the former have played any visible political role in the GCC.
[38] For the concept, see Hourani (1968).

incumbent regimes, inadvertently paving the way for the eventual emergence of authoritarian-populist regimes that would end up fighting them as representatives of the old order.[39]

While large parts of notable elites in the Arab republics were swept aside by the forces of Arab nationalism after World War II, Gulf merchant elites instead gradually became clients of the rapidly growing rentier state. Two forces undermined their independent political status: most obviously, the reversal of their role from a source of taxation to a recipient of the state's largesse deprived them of much of their bargaining power.[40] Secondly, and less visibly, their remaining nationalist fervour and taste for political independence were arguably snuffed out by the onset of mass politics and the related diminution of their role as community leaders, as a larger middle class with higher levels of education and direct access to the state and its resources emerged (Azoulay 2012b; Hertog 2012b). This has been salient especially in the countries with some degree of open parliamentary life, namely Bahrain and Kuwait, where merchants have ceased to play any role as parliamentary leaders, and where elected parliaments tend to pursue populist economic policies that are in opposition to merchants' interest.

Although Gulf regimes have historically 'bought off' private sector elites through various mechanisms of rent recycling, the older ones among the large merchant families have remained fairly visible as social elites or 'notables', though more in some countries (like the UAE) than others (like Qatar). Established elite clans often also have family members who are well placed in intellectual or administrative circles, and strive to maintain their social status through charitable work (although the latter is sometimes gently forced on them by ruling families).[41] Some of the clans also own media outlets. More recent arrivals among the business elite often aspire to 'notabilization' and are hence especially active in the charitable sector.

Unlike the notables of old, however, merchant elites now unfailingly side with ruling elites against new generations of populist oppositionist movements, in particular Islamist ones. Merchants by and large are politically conservative, and many of them now see electoral democracy as the biggest threat to their interests. Although traditions of constitutionalism run deep in Kuwait, large business families are deeply worried about their loss of control of parliament and the anti-business legislation emerging from it (Herb 2009). Albeit they are often socially conservative, merchant elites seem to perceive the Islamist opposition as a

[39] On the (passing) politics of the notables in the Levant, see Droz-Vincent (2004).
[40] This best study of this process is Crystal (1995).
[41] Interviews with businesspeople in Saudi Arabia and the UAE indicate that sheikhly patrons often expect businesses to provide the bulk of finance for charity operations for which sheikhs contribute seed money.

major threat all across the Gulf, and try to support counter-movements in the cases where elections are happening.

In the Gulf as elsewhere, the independent power of notables has eroded as societies have grown richer and more socially differentiated; the one-sided economic dependence on the rentier state has undermined the notables additionally – and has put them in a situation of structural opposition to the citizenry. While the dominant parts of the business class remain sociologically distinct from the state and are often opposed to its policies, they now operate in its shadow and have limited capacity for exerting political pressure or organizing resistance to state action.

3.2. Business and fiscal sociology in the GCC

In the political economy literature about rentier states, the absence of taxation in the GCC has traditionally been used to explain the authoritarian status of Gulf regimes: 'no taxation, no representation'.[42] As Michael Herb has pointed out more recently, however, it also gives business a peculiar position vis-à-vis the rest of society (Herb 2009): without taxes, private sector growth does not lead to an increase in state resources and hence does not benefit the general population via more public services. Conversely, however, much of business growth in the GCC remains *financed* through state spending and state provision of low-price inputs, which hence become unavailable for other forms of broader distribution. This situation creates an unusually harsh zero-sum game between business owners and citizens who are not businesspeople (or senior management).

Our above analysis of business growth shows that there is a certain asymmetry of interests here not pointed out by Herb: business still benefits somewhat from spending on public sector salaries which are subsequently spent in the local economy, while pro-business spending bypasses most citizens and leads to seepage of resources abroad. Business benefits at least from citizens' role as consumers, while business conversely does nothing to generate income for most of the citizenry.[43]

As Herb indicates, the fundamental tension between business and citizenry is further increased by the fact that business growth in most countries hardly contributes to national employment. We have seen above that most or at least most of the attractive jobs for nationals are still found in the public sector. The predominantly foreign employees of the private sector

[42] For classical statements of this argument, see Beblawi and Luciani (1987).
[43] This is perhaps a subsidiary reason why broad salary spending has always been privileged over project spending in times of economic crisis.

tend to remit a large share of their incomes to their home countries, contributing to a resource drain that bypasses citizens.

There is public awareness of this ‘missing link’ at least in the lower-rent countries. The tame Saudi press publishes regular complaints about the private sector’s failures to employ nationals (e.g. Al-Zahrani 2011; Al-Ehaidib 2012). The Shiite opposition movement Wifaq has criticized Bahraini business for insufficient employment of nationals; despite its generally anti-government stance, it was the main parliamentary ally for the government’s plan to tax foreign labour, hoping thereby to increase Bahrainis’ chances for employment – a policy fought tooth and nail by Sunni and Shiite businesspeople alike (Foucraut 2010; Al-Hasan 2012a).

Finally, as explained above (and not mentioned by Herb), organic links between private sector and population at large through national savings and investment are also weak, as most corporate wealth continues to be privately held and companies are privately financed. Policies that are detrimental to private business hardly affect nationals qua investors.

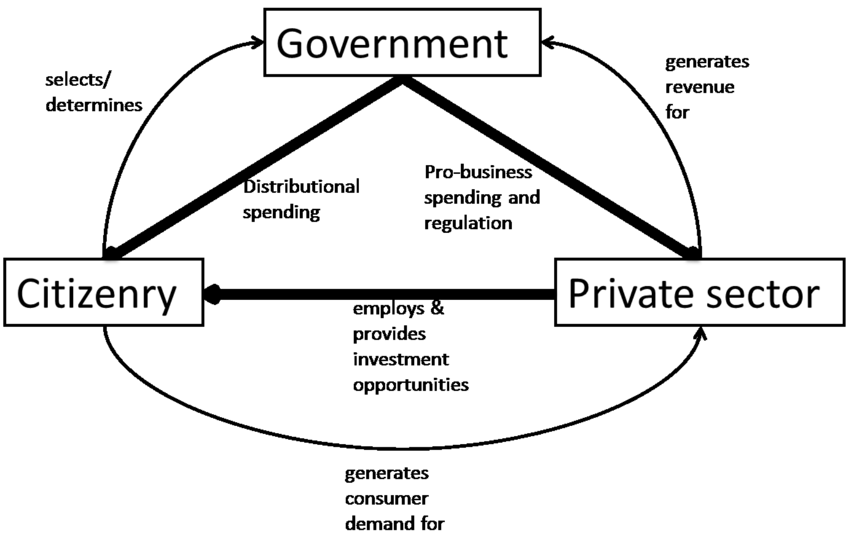
The overall situation is such that a rational national voter is likely to demand populist economic policies from the government, even if these destroy business, as the cost of such policies are only borne by the business class itself. This is exactly what has been happening in Kuwait, which is by far the most democratic GCC country, but also the one with by far the worst record of economic modernization. The Kuwaiti parliament has undermined most of the government’s economic and infrastructural reform efforts since the early 1990s and instead pushed for ever higher levels of direct rent distribution to the population (Herb 2009). Recently, tribal MPs have gone beyond patronage demands and have started to attack the commercial privileges of established merchants directly, proposing new legislation for opening up government tenders to foreign competition (Azoulay 2012a).

Elected bodies in all of the GCC appear to be systematically more populist and oriented towards the politics of distribution, while appointed bodies – often with a stronger representation of business – pursue a more technocratic and diversification-oriented policies broadly in line with business interests. Next to the Kuwaiti parliament, the Bahraini lower chamber has probably been the most populist body, asking for pay rises for state employees, direct handouts to citizens and reprieves on utility payments on numerous occasions (Gulf Daily News 2011f, 2012a, 2012b; Toumi 2012). Populist inclinations are, however, visible even in very tame (semi-)elected institutions like the Federal National Council (FNC) in the

UAE.[44] The unelected Majlis Al-Shura in Saudi Arabia seems to have become more populist after the ruling family started to choose its membership according to regional and tribal rather than purely technocratic criteria.[45]

Generally speaking, government policy tends to be more pro-business in more authoritarian GCC states with less of a popular veto on economic issues.[46] The forces at work are illustrated in Figures 22–4: in a conventional tax state, government, business and citizenry are linked through taxation, employment and political participation. In the stylized authoritarian rentier case, links between citizenry and business (employment), between citizenry and government (participation), and between business and government (taxation) are weakened. The citizenry has less political influence over government policy, while business has less economic influence and importance; as the source of economic resources, government can therefore play arbiter between rival interests. If a rentier state that retains elements of political participation, however, government is under more pressure to side with citizens, and to subordinate pro-business policies to the distributional demands of the citizenry. In all cases, there is an asymmetric link between citizens and business in that the latter benefits from the consumer spending of the former, further underlining the structural dependence and isolation of the merchant class.

Figure 22. *Fiscal sociology of a tax state – interdependence*



[44] The UAE's partially elected Federal National Council has recently demanded a decrease in the already low petroleum prices in the country, which would impose huge opportunity costs on the national oil company and the attached distribution companies (Salama 2012b). For further examples of parliamentary populism in the UAE in 2012 alone see Kakande (2012) and Salama (2012a).
[45] Discussion with Majlis Al-Shura members, May 2011.
[46] On the UAE example, see Herb (2009).

Figure 23. *Fiscal sociology of an authoritarian rentier state – government as arbiter*

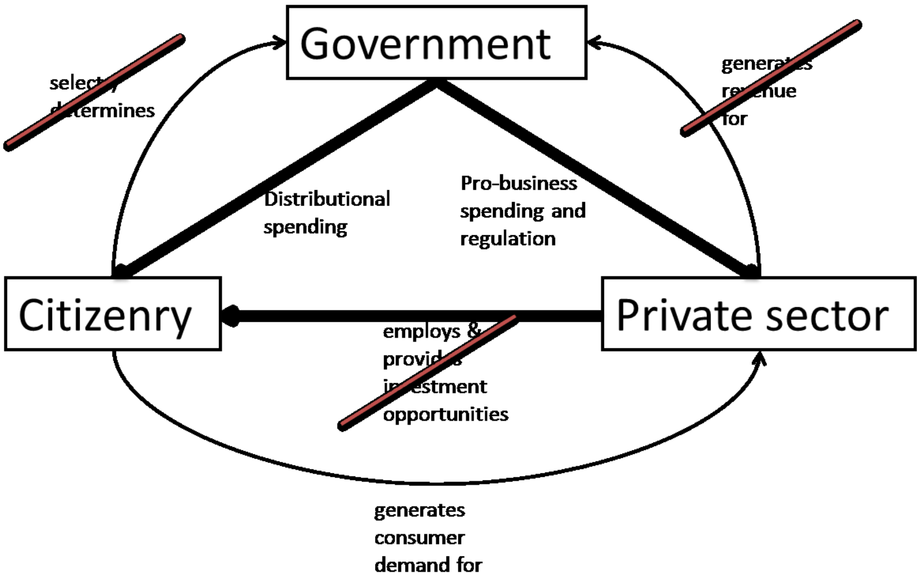
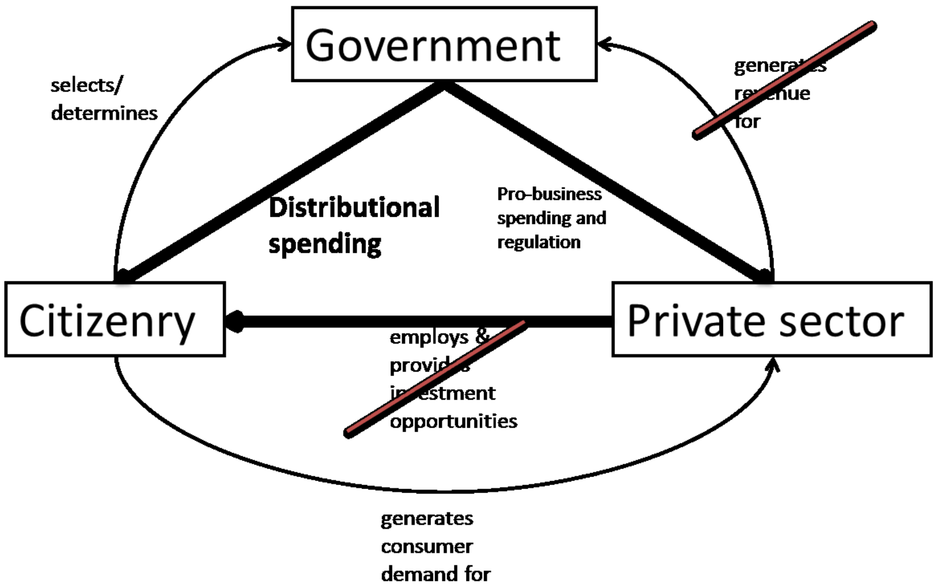


Figure 24. *Fiscal sociology of a participatory rentier state – one-sided pressure*



In either type of rentier state, the structural tension between business and population is partially counteracted by the community roots and notable traditions of merchant elites. But as has been argued above, these have been on the wane, and will continue to decline further with the emergence of middle-class identities – even if the latter are sometimes dressed up in tribal or religious garb.

It is also worth noting that the relatively poorer GCC states of Saudi Arabia, Bahrain and Oman have reached sizeable levels of national employment in the private sector, which gives some interest in business growth to at least a minority of the national population. Compared to Kuwait, there does indeed appear to be less anti-business populism in Bahrain's council of representatives. The chamber has pushed for more distribution than has the appointed upper house, but has not worked to undermine infrastructural modernization and diversification policies as systematically as the Kuwaiti national assembly – possibly because more nationals are employed in the Bahraini private sector and therefore have 'skin in the game' of economic development. That being said, many of the privately employed nationals in the GCC still hope for eventual state employment, which is contingent on increased distributional spending.[47]

Conversely, in the richer GCC rentiers of Kuwait, the UAE and Qatar, a higher share of nationals has some sort of business interest that could give them an interest in pro-business policies. Many of these citizens, however, limit themselves to acting as silent partners and renting out licences to foreign entrepreneurs for low-margin activities, which would also continue in the absence of economic reform and infrastructure spending.[48]

The majority of nationals all across the GCC continue to have no significant stake in private sector growth. In the long run, distributional conflict is set to grow, as demands on state resources will become ever larger due to both a growing business sector and a growing national population. On past form, in a fiscal crisis, popular interests will be privileged over business interests, even in authoritarian rentiers: in times of austerity, GCC regimes have cut capital and infrastructure spending, and increased industrial tariffs, while current spending on salaries and transfers as well as consumer tariffs have been protected (Oxford Analytica 2011)[49] – another sign that the merchants are just a subordinate partner of the ruling elites. One of the few sectors in which GCC regimes have created new corporatist interest groups in recent years is the area of consumer rights, an activity clearly directed against the business class (and, conveniently, away from the government). GCC rulers can live with an unhappy business class if need be – they would be much less comfortable with an unhappy population at large.

The visible tensions between business elites and the general population, as well as the closeness of business to local regimes, are structurally embedded in the political economies of the GCC, for reasons that have been neglected by most of the literature to date and which go

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[47] On preferences for public sector employment, see the various regional surveys by Silatech, http://www.silatech.com/index.php?option=com_content&view=article&id=121&Itemid=29.

[48] Due to the very high ratio of expatriates to nationals in the UAE and Qatar (at least 5:1), probably more citizens act as intermediaries for foreign entrepreneurs in these two countries than in Kuwait (where the ratio is closer to 2:1), increasing the share of notional 'businesspeople' in the national population.

[49] For a detailed account on Saudi Arabia, see Hertog (2010a: 118–25).

beyond customary arguments of 'cronyism' and 'rentier bourgeoisie'. Business elites not only are fiscally state-dependent, but also have to rely on the regime to arbitrate a zero-sum distributional conflict with the wider citizenry with which they share few objective economic interests. In terms of their fiscal sociology, GCC business elites are even more isolated than their counterparts in other MENA countries, and hence have every incentive to seek regime protection not only economically but also politically.

3.3. Business in electoral politics and other public contestation

A brief review of the role of business elites in electoral politics and other public contestation in the GCC will illustrate their relative isolation and proximity to governing elites. As mentioned above, merchants used to play a leading role in several of the early national assemblies in the Gulf. Now business elites either are absent from the political stage or play a subordinate loyalist role, usually without the ability to mobilize wider social support for the regime.

3.3.1. Bahrain

Merchant elites in Bahrain have been particularly visible as supporters of the embattled Al Khalifa regime. Many of the large Sunni families are known to be particularly close to the powerful prime minister Khalifa bin Salman (Al-Hasan 2012b; Louer 2012; Valeri 2012). Leading business players and the BCCI have publicly supported anti-democratic measures such as more restrictive assembly laws (Bew 2006). In 2006, the head of BCCI declared publicly that 'vital national issues' should be kept out of election campaigns (leaving it unclear what campaigns should be about) (Toumi 2006).

When important parts of the Shiite opposition decided to contest national elections in 2006, BCCI started backing pro-government parliamentary candidates, although apparently with limited success: the 'Meethaq' political group formed by wealthy businesspeople turned out to have no street influence, as a result of which the government shifted to supporting Sunni Islamists whose socially conservative policy demands constituted a threat to Bahrain's important tourism sector.[50] Few business representatives have sat in Bahrain's various post-2002 parliaments, a fact much lamented by business leaders (Al-Mughni 2009).

With the outbreak of mass unrest in early 2011, business elites publicly pronounced their loyalty to the Al Khalifa (Rafiqe 2011; Gulf Daily News 2011e). MPs from the new 'independent bloc', which enjoys business support, called for the imposition of martial law in

[50] Ereli to Department of State, A field guide to Bahraini political parties, 2008-09-04, US embassy cables, *Guardian*, http://www.guardian.co.uk/world/us-embassy-cables-documents/168471.

March 2011, and businesspeople publicly supported the state of emergency pronounced by government (Toumi 2011b; Gulf Daily News 2011b). BCCI supported both the use of Saudi troops to aid the Bahraini security forces against the protesters, and a boycott of Iranian products to retaliate against Iran's supposed assistance to the opposition (Valeri 2012).

As a further sign of business elites rallying around the Al Khalifa flag, in April 2011 two Shiite members of the BCCI board were sacked for their supposed involvement in the unrest (they were reinstated a year later) (Gulf Daily News 2011d).[51] In September, a group of Bahrainis that included 40 per cent businesspeople created a new political group, the 'Justice and Development Society', in a renewed attempt by business to counterbalance oppositional groupings (TradeArabia 2011).

As a sop to business, the fees on foreign labour were abrogated in early 2011 (Toumi 2011c); beyond this, the regime had to do little else to ensure the merchants' loyalty. While in private some Sunni business elites might have had misgivings about the regime's harsh crackdown, these were not voiced publicly. Shiite business leaders have been less visible in their support of the regime, but they have not played a leadership role in the opposition, of which they had been critical even before the unrest.[52] Critical voices like those of Shiite business leader Faisal Jawad have been the exception (Valeri 2012).

3.3.2. Kuwait

We have already mentioned the marginalization of Kuwaiti businesspeople in the parliamentary life they once dominated. As a result of increasing mobilization by middle-class opposition movements, the business community has even lost the speakership of the national assembly, which from 1999 to 2011 had been held by a member of one of Kuwait's richest families, Jassem Al-Khorafi. Business leaders have repeatedly and publicly complained about the deleterious effect of parliamentary politics on economic policy, but have been powerless to do much about it (Arab Times (Kuwait) 2007; El Gamal 2007). As their grip on policy has slipped, business leaders have called for organized lobbying efforts (Kuwait News Agency 2007) – a call that would have sounded strange forty or fifty years ago, when business was the main political lobby – but to little avail.

There is one instructive exception to the absence of business leaders from popular politics that confirms our general argument: that of a small number of newly rich Shiite merchants who came to prominence under the patronage of former prime minister Nasser

[51] 'At the same time, Shiite business leaders have generally refrained from supporting the Shiite opposition; Laurence Louer, personal communication, July 2012.
[52] Laurence Louer, personal communication, July 2012.

Mohammad Al Sabah (2006–11), and who for a while acted as representatives of the Shiite community in Kuwaiti politics. Two of them, Ali Al-Matruk and Mahmud Haider, were instrumental in brokering a cooperation deal between Shiite opposition group Al-Tahaluf and the government in 2008, and have worked towards the unification of Al-Tahaluf and other Shiite political groupings. Having failed to gain political traction with their support of moderate Shiite movements, they have been instrumental in convincing Al-Tahaluf MPs to support Nasser Mohammad's government against Sunni Islamist and tribal opposition in parliament.

Their role as community leaders, however, seems to have been temporary, as they lost much of their status and visibility after Sheikh Nasser's exit from office in November 2011. They could exert a role as 'notables' and community leaders only as representatives of a religious minority in need of political protection, thanks to direct regime support, and by allying with a more popular middle-class political movement (Azoulay 2012b). With the February 2012 election, popular politics was again dominated by tribal and Islamist MPs as well as a limited number of pro-government MPs who are not part of established business elites.

3.3.3. Other GCC countries

While electoral politics and public political life in the rest of the region have been less animated than in Bahrain and Kuwait, the role of businessperson has been just as limited. Elections in Saudi Arabia have been a lacklustre affair, limited to municipal polls for half of the seats of local councils with strictly limited powers. A good number of businesspeople have run in these polls, sometimes using considerable resources to finance their campaigns. For the most part, they have been unsuccessful, beaten by Islamist candidates in all of the kingdom's main cities – Riyadh, Dammam/Dhahran/Khobar and Jeddah – although the last is perceived as the kingdom's traditional hub of commerce and merchant politics (Kraetzschmar 2011; Menoret 2005).[53]

In Oman, as in Bahrain and Kuwait, there are few business MPs in the country's elected consultative assembly, despite the greater historical role of business clans as partners of the sultan in government.[54] After the outbreak of popular protest in early 2011, the sultan

[53] In Dammam/Dhahran/Khobar, at least two businesspeople seem to have made it to the seven-seat council in 2005, but due to their support by and allegiance to an Islamist group, not as representatives of the business sector; Stephane Lacroix, personal communication, July 2012.
[54] Few businesspeople decided to stand for election in the first place. The current speaker of the Majlis Al-Shura (the elected consultative council) has business interests, but is a member of the governing and tribal elite by background; Marc Valeri, personal communication, July 2012.

reshuffled his cabinet, dismissing a number of long-serving close allies with extensive business interests who had been under attack from protesters (Valeri 2012). Even in Oman, where business elites have been more important in government than in any other GCC country, leading merchants could be easily sacrificed when political stability demanded it.

There have been municipal elections in Qatar since 1995 with progressively declining levels of popular participation. Business elites have hardly been represented on the municipal council.[55] Many members of the elected half of the UAE's FNC, by contrast, are from large business families (although they are not business leaders themselves).[56] The franchise for the FNC elections has been limited to a small, handpicked electorate, however, so election results do not necessarily reflect popular preferences. When in March 2011 more than a hundred Emirati intellectuals submitted a petition to ask for more powers for the FNC, no members of the Emirati business elite were among the signatories (Almezaini 2012).

Impressionistically, business elites in the UAE seem to have more of a traditional 'notable' status as community leaders, as UAE ruling families are smaller and have left more space for other clans to develop their business interests and share in government (Almezaini 2012; Crystal 1995; Davidson 2008, 2011). Due to the small size of the population, such clans constitute a significant share of the citizenry. In Qatar, by contrast, the ruling family has an expansive presence in business, probably more so than in any other GCC country. The country has never developed a cohesive merchant community (Crystal 1995), which might explain some of the anti-business animus in the otherwise tame local press. In both countries, there has been little open contestation that would require business elites to rally openly around the flag, but it is obvious that they are close to government.

3.4. Summary

The GCC state looms ever larger in the political than in the economic arena; the client status of the business class, hence, is even more visible there. If business has become active in public political life in recent years, it has done so to support the regime, sometimes directly on behalf of specific regime players. To the extent that business elites have an independent political interest, this appears limited to fighting populist economic agendas and the social conservatism of Islamists that could damage the GCC as a hub for business and tourism. The observable political behaviour of business elites, of course, does not necessarily reflect the

[55] Steven Wright, personal communication, July 2012.
[56] Khaled Almezaini, personal communication, July 2012.

political positions of business at large. The almost complete invisibility of business players among popular movements and political opposition in the Gulf is nonetheless glaring.

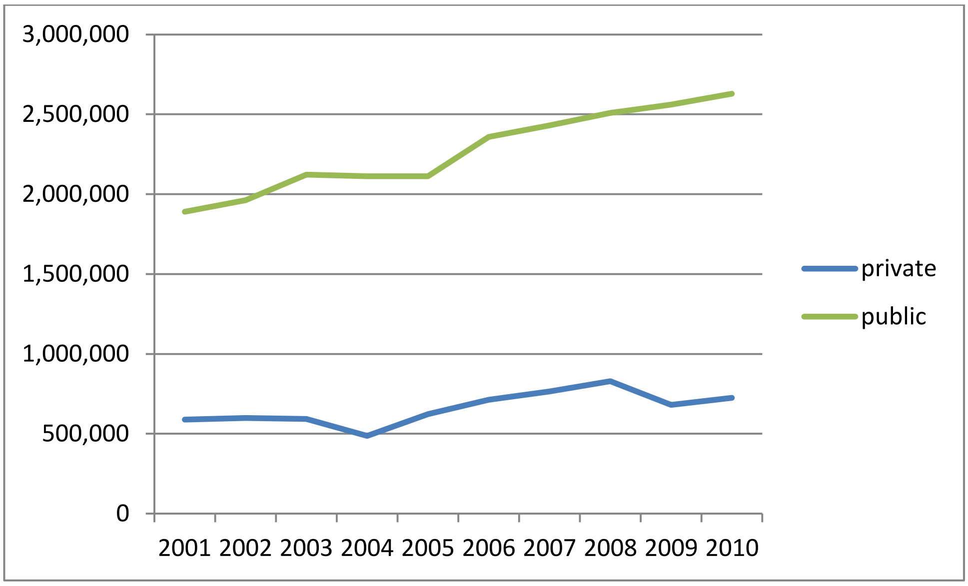
While their traditional notable status might somewhat counter business elites' structural isolation from the wider citizenry, this has not been enough to prevent their marginalization from electoral politics. In an age of mass politics, business elites all across the MENA region seem to have lost their role as political intermediaries speaking on behalf of larger communities. While there might be less mass politics in some of the GCC countries, at the same time business elites have fewer objective economic links to the national population at large.

Will the trend of political marginalization continue? Countervailing forces are at work: on the one hand, the more societies are differentiated and the more old urban social networks break down, the more structural conflicts between business and citizens will become salient. On the other hand, business might re-establish some of its functional links to the citizenry through employment, taxation, and more open capital structures allowing citizens to become participants in local capitalism.

Taxation on a level that would be sufficient to make a difference to the level and quality of public services is an unlikely prospect in the short to mid-term: GCC-wide proposals to introduce VAT have been postponed repeatedly; in the wake of the Arab uprisings, any increases in taxes or fees appear politically taboo. National employment is a more likely channel through which larger parts of the citizenry could be integrated into private economic circuits. Local business has strenuously resisted nationalization policies in private labour markets, but regime pressures on business are increasing. Higher levels of national employment are in many ways functionally equivalent to a tax: they increase the costs of business, while at the same time reducing the pressure on government to create surplus public sector jobs, thereby liberating resources for other uses.

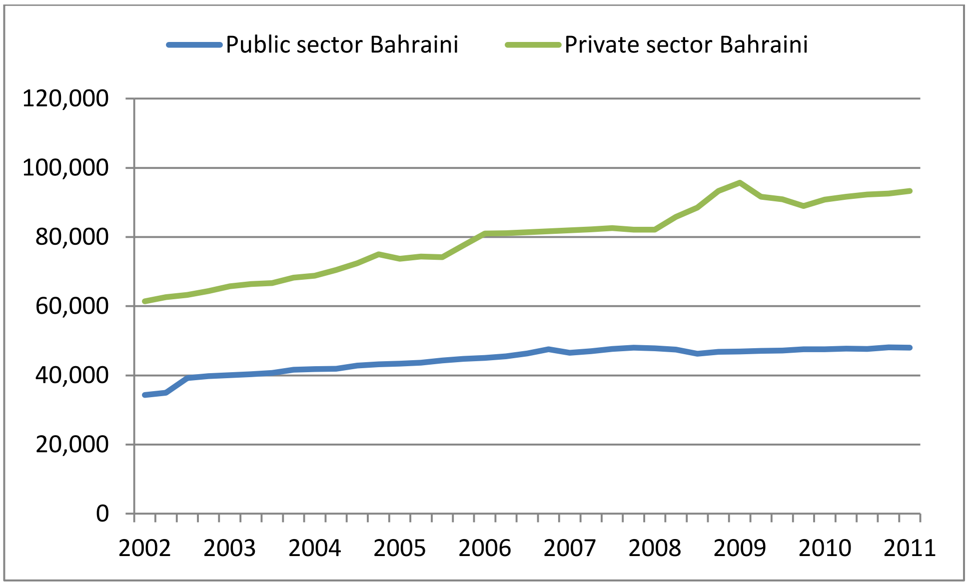
Recent trends in national job creation differ from country to country: while very few nationals are employed in the private sectors of the high-rent countries of Kuwait, Qatar and UAE, there are more citizens in private employment in Bahrain, Oman and Saudi Arabia. Among the latter three, however, only small Bahrain and Oman have seen significant growth in private jobs during the 2000s boom decade – and for the most part jobs that are much less attractive than public sector positions. The recent wave of public sector hiring and wage increases in the wake of the Arab spring has, moreover, undermined prospects for private sector employment (Hertog 2011b) (Figures 25–7).

Figure 25. *Saudi public vs. private employees, 2001–10*



Source: Ministry of Labour, Labour Force Survey

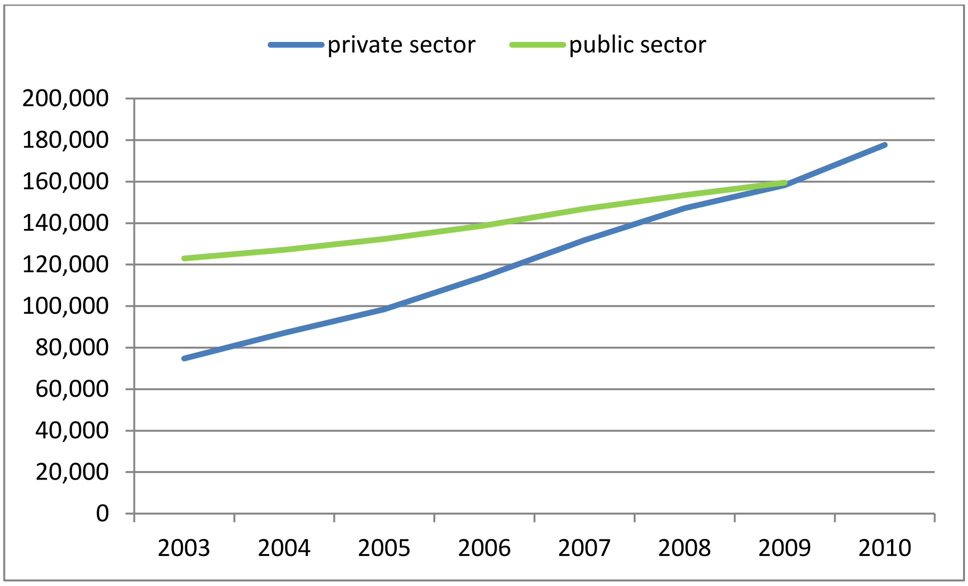
Figure 26. *Employment of Bahrainis by sector (quarterly data), 2002–11*



Source: Labour Market Regulatory Authority
Note. The public sector figures are quite likely to be an under-estimate as they exclude security agencies.

Until recently, from a purely structural viewpoint, Bahrain appeared to be in the best position for organic cooperation between private sector and population. Until the unrest in 2011, there was indeed less popular and parliamentary hostility to the government's project of turning the country into a business hub than in Kuwait. Since then, however, the situation has

Figure 27. *Number of Omani employees in public and private sector, 2003–10*



Source: Central Bank of Oman.

been dramatically complicated by the wider political and sectarian situation, which has ensured that business elites have remained close (and structurally isolated) clients of the state.

Bahrain was also the one country to experiment with a more ambitious, market-driven labour nationalization strategy that could have further increased popular interest in a thriving private sector – but this policy was defeated in 2011 (Al-Hasan 2012b). To date, the other governments across the Gulf Arabian Peninsula have pursued private labour nationalization policies in a top-down and interventionist fashion which has led to much evasion and many inefficiencies. More market-oriented policies involving fees for foreign labour or partial subsidies for national labour remain in their infancy (Hertog 2012a). Successful integration of nationals into private labour markets, however, is an essential precondition for linking the economic interests of citizens and business.

While the provision of investment opportunities is important, employment of nationals is a far more significant and palpable measure of the local private sector's contribution to national development. It is also a precondition for its potential transformation into a true bourgeoisie, capable of autonomous politics and social alliances with actors other than the regime. Even in the best of cases, however, this is a very long-term prospect.

4. Conclusions

The status of business in the Gulf rentier states is paradoxical: it operates on a large scale, is internationally integrated, contributes the bulk of national capital formation and has attained fairly high levels of managerial sophistication – often ahead of its peers in the wider MENA region. Yet business remains dependent on the state, living off government support in both obvious and less obvious ways. Business has used the GCC's comparative advantages well, but has not employed them as stepping stones to the much-vaunted 'knowledge economy' – instead, it has witnessed declining productivity and failed to provide quality jobs for GCC citizens. It is often state rather than private entities which are the leaders in technology development, the modernization of corporate governance, the build-up of a national managerial elite, and the provision of blue-chip investment opportunities for the wider population. GCC governments continue to drive economic policy-making, with business lobbying often limited to the defence of the convenient status quo.

Despite strong historical traditions of merchant politics in several GCC countries, Gulf business is even less of a leader in the political arena. This is to some extent due to reasons familiar from other regions and eras, notably the ascendancy of mass politics and middle-class identities that have undermined the authority of traditional merchant elites as community leaders. Beyond that, however, state dependency and structural isolation from wider society have additionally undermined the political autonomy of Gulf business elites. Gulf capitalists share few functional links with fellow citizens through employment, taxes or popular investment, resulting in an unusually stark opposition of business interests and those of the citizenry at large. While the popular franchise has made business a politically conservative force in most countries of the world, its structural isolation and lack of functions for wider society in the Gulf are unique to the region.

Due to a lack of linkages between national workers and capitalists, the scope for a European-style 'historical compromise' between different classes that would allow a consensus on growth-oriented economic policy is currently small.[57] Instead of conventional class relations based on interdependence in production, GCC political economies are characterized by the towering presence of the state as distributional arbiter on top of a zero-sum distributional conflict between its different social clienteles.

This hub-and-spoke system gives state elites ample opportunity to divide and rule. But while the regime requires minimal support or at least acquiescence from the masses even if these do not generate taxes or participate in local production, business has no essential structural role to fulfil. While state support and a growth model built on private wealth, no taxation and cheap foreign labour make for good profits, they also limit the political potential of business as either allies of the ruling elite or autonomous political player.

[57] See Przeworski (1986) on class compromise in conventional developed economies.

If GCC business is ever to emerge from the shadow of the state, it will first of all have to step up its employment of nationals. This will require a shift away from factor-intensive growth, a focus on technological upgrading and a concentrated effort to build local human resources. It would probably also require policy changes that are beyond the control of business, notably a reduction in public sector employment, which currently reduces nationals' education incentives and increases their wage expectations. Short of a fundamental redesign of the GCC social contract in which less distortive forms of distribution (such as wage subsidies or cash grants) are substituted for public sector employment, this is hard to imagine.

Stronger local employment would be likely to reduce business profits in the short run, but could give business a much safer and more autonomous political position in the long run: it could become a true bourgeoisie capable of negotiating with state and other social forces on a level playing field. Many factors would have to fall into place for this to happen, however. For the time being, GCC business will remain threatened by populist distributional policies, and pro-business spending is likely to be the first victim in a fiscal crisis.

The position of business as described in this paper is mostly an outcome of structural forces rather than a personal failure of business leaders. The best entrepreneurs would find it hard to emerge from the shadow of a state as capital-rich and omnipresent as in the GCC. This does not mean, however, that more forward-looking business leadership might not change things in the future. Such leadership would have to tackle questions of taxation, distribution and employment in a comprehensive fashion, and would require willingness to make short-term sacrifices for the sake of long-term development. For the time being, the position of Gulf business is probably too comfortable for such strategic moves to occur.

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