

[Steffen Hertog](#)

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State and private sector in the GCC after the Arab uprisings¹

Steffen Hertog

Introduction

While the private sector has been suffering economically and often politically in the Arab world's revolutionary republics, business in the GCC monarchies has been thriving: According to IMF estimates, non-oil growth in the GCC reached 5.9% in 2012, and similarly high 5.5% were expected for 2013.

Gulf business seems to have achieved unrivaled status in the region. Of the Arab world's 30 largest companies by market capitalization in 2011, 25 were GCC-based.² Gulf businesspeople have by far the largest overseas investments of all Arab businessmen, 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".

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 far jump to expect it to become a political player with leverage over government – in other words, a true "Gulf bourgeoisie".³ In the wake of the Arab uprisings, levels of political awareness have increased even in the most quiescent GCC states. Regimes are in need of social allies, both for direct political support and to safeguard the economic development and welfare that their legitimacy depends on. Local business seems destined to be a strategic negotiation partner of GCC regimes – be it as supporter or even as potential challenger.

How accurate is this picture of economic and political ascendancy? This article will argue that headline figures about private assets and investments, and state rhetoric about private-driven growth and development agendas, 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 article will document that Gulf business provides most of local employment and capital formation, and contributes to the provision of services that were previously the domain of

¹ 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 earlier drafts.

² <http://www.cashandtrademagazine.com/test/wp-content/uploads/2011/07/top-100-arab-companies.jpg>

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).

the state. Since the first oil boom era of the 1970s and early 1980s, it 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 taxes on local business activity, and whose payroll dwarves 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 diversification into new sectors has been driven by state-owned companies. Most private sector wealth is held privately and therefore beyond the reach of local investors. Business input to economic 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. Most important for its political role, 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, foreshadowing future conflict in an age of higher political awareness and mobilization.

The 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 – most notably during the recent regional unrest. 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, a pattern that is likely to repeat itself.

Gulf business has a chance for a greater developmental role and political autonomy only if it increases its inter-dependence 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. Otherwise, it could be shoved aside as has happened in poorer MENA states – even without a revolution.

Business in economic development and policy-making

Role in national economies

The GCC has gone 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;

different from 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. 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 2010, p. 81).

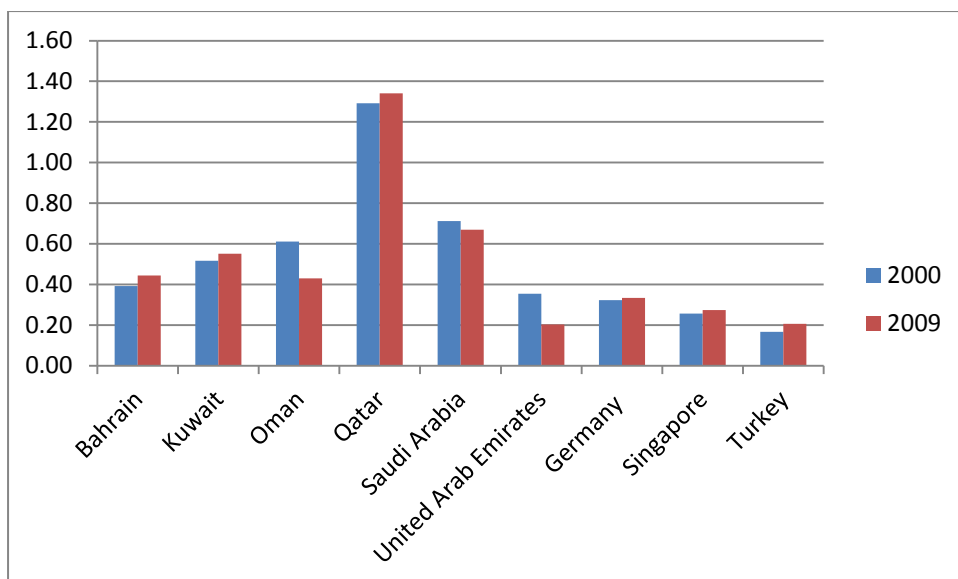
In the 1970s and 1980s, GCC merchants often just functioned as intermediaries and access brokers for international businesses who provided most of the actual goods and services the rapidly growing, oil-fed GCC economies demanded (Hertog 2010b; Field 1986). The operations of large local businesses are much more substantial now, operating 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% of the jobs in the region are provided by private business, albeit these are mostly held by foreign employees.

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 can be illustrated both with direct analysis of macro-data and a less obvious analysis of how demand is generated in GCC economies.

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

Graph 1: Ratio of Government to Private Consumption in GCC and select international cases⁴

⁴ Given the huge increases in government spending in the UAE during the 2000s, the figures appear improbably small, possibly due to exclusion of Emirate-level data.



Source: UNSTATS

Econometric tests show an abiding and strong impact of state spending on the size of business activity in the GCC. The two variables remain closely associated in the long run.⁵ 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.

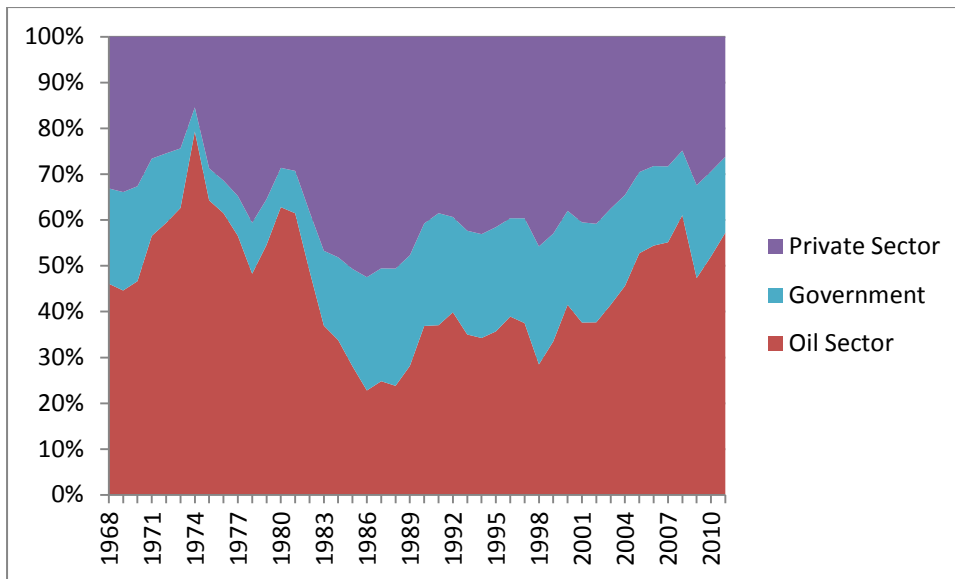
In the GCC by contrast, the only reasonable interpretation is that causality runs in one direction: As domestic economic activity creates very little tax income and states are for the most part financed by external rents, any correlation of state spending and business activity must be driven from the government side.⁶ This means that much of GCC business activity is fundamentally explained with state spending.

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 compared to that period. Despite rapid expansion of state spending on the back of increasing oil prices, local private sectors retained a larger share in GDP throughout the 2000s, as graph 2 illustrates for the Saudi case.

Graph 2: Composition of Saudi GDP since 1967

⁵ For econometric evidence cf. (Kireyev 1998) and (Treichel 1999). Recent econometric tests using time series regressions and error correction models confirm the findings on data up to 2008. A recent IMF report also provides evidence of strong fiscal multipliers in the GCC (Espinoza and Senhadj 2011).

⁶ For more details see (Hertog 2011).



Source: SAMA

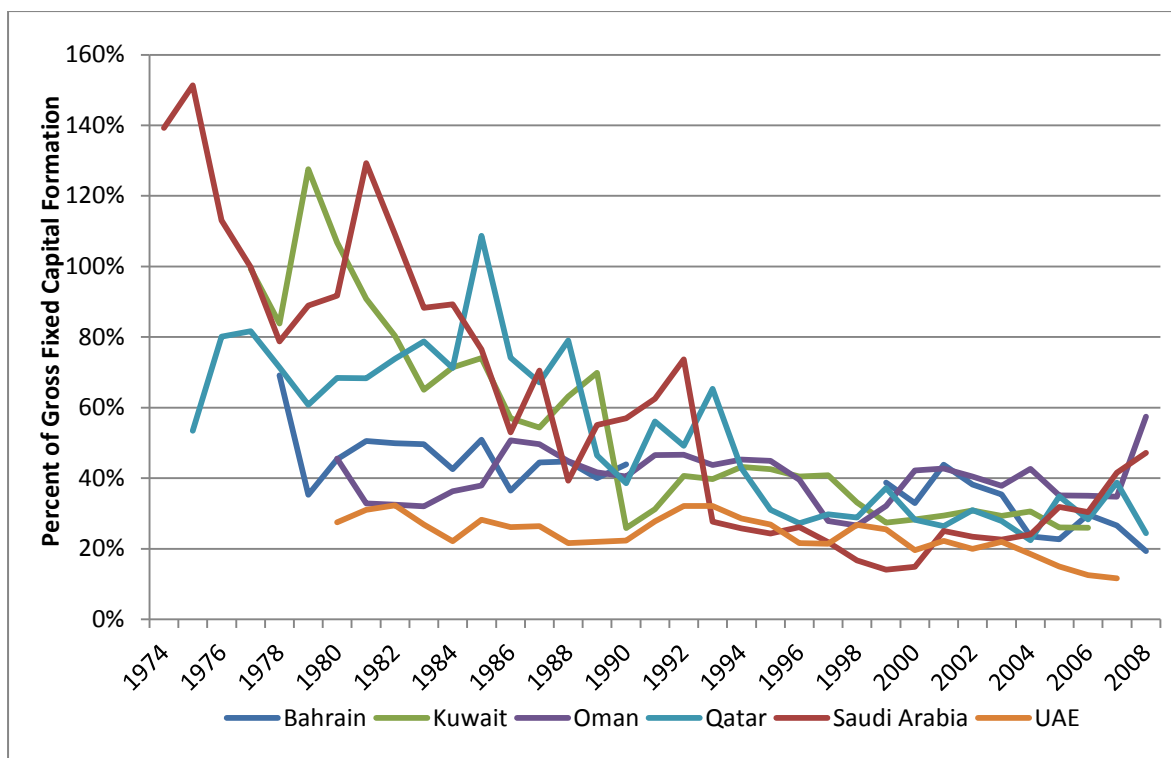
Moreover, although state spending and the volume of private economic activity remain closely linked in the long run, growth rates of the two now are less closely correlated in the short term, meaning that the growth path of business is relatively smoother and less affected by temporary spending fluctuations.⁷

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 most of this demand is indirectly created through state spending on salaries and benefits (see the subsequent section below), consumption decisions are nonetheless smoothed over time relative to state expenditure. GCC governments since the 1980s have devoted larger shares of their total budgets to current as opposed to capital expenditure. The former item is usually dominated by salaries, while the latter mostly results in direct contracts with private companies. Conversely, the private sector has stepped up its contribution to capital formation, which in all countries bar Qatar is larger than that of the public sector.

Graph 3: Share of Government Capital Spending in National Gross Fixed Capital Formation⁸

⁷ See Treichel (1999) and Kireyev (1998) for econometric evidence on such a structural shift after the 1980s in Oman and Saudi Arabia.

⁸ The ratios above 100% for some cases in the 1970s are due to inconsistencies in national fiscal and national accounts statistics.



Source: ESCWA and IMF

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 and are less directly reliant on state spending in the short run. As they depend relatively less on state direct procurement and more on consumer demand than in the 1970s and 1980s, they tend to operate on more competitive markets.

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 different from tax-based economies, Gulf businesses contribute practically nothing to sustaining the state demand they depend on, as they generate little or no tax income.

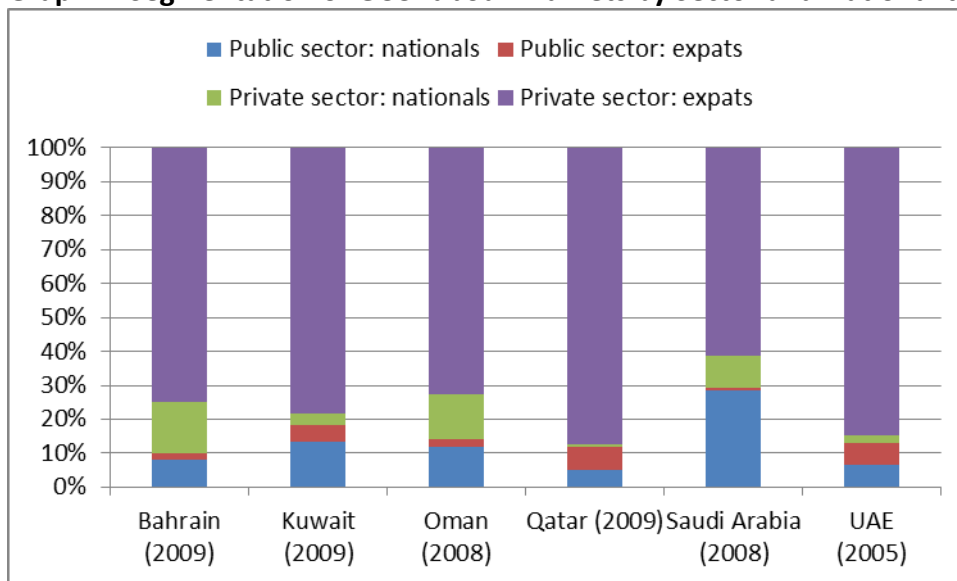
Contribution to national employment

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 important, 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).

GCC businesses’ preference for employing foreign workers is rational. Yet, the focus of private GCC businesses on short-term rent extraction from low-skill, low-cost foreign labour and an aversion to invest in long-term productivity upgrades and skills of local staff have contributed to the exclusion of large parts of GCC nationals from private labour markets (See Graph 4).

Graph 4: Segmentation of GCC Labour Markets by Sector and Nationality



Sources: national agencies

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 obligatory, a tax.⁹ Conversely, there is much popular disenchantment with a business class perceived as fat cats who do little to provide decent jobs for nationals.¹⁰ The dominance of foreigners on private labour markets means that much of the business diversification of the last 3 decades has passed by national populations.

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? That does not appear to be 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% in Saudi Arabia, with Saudis accounting for 3%, and

⁹ Interviews with businessmen in Kuwait, UAE, and Saudi Arabia, 2004-2011.

¹⁰ See for example Muhammad Al-Ehaidib, “Private companies undermine Saudization”, *Saudi Gazette/Okaz*, 10 August 2012.

expatriates for 4%. In the UAE, private salaries seem to have accounted for only about 11% of GDP in 2008, almost all of which is accounted for by foreign employment. Even in Bahrain, a country with a fairly small government sector and a comparatively developed private labour market, the private wage share only reaches 16% of GDP, more than half of which is again accounted for by foreigners. This compares with a private wage share around 50% 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.

Despite a sizeable private sector share in GDP, private demand generation hence remains quite limited. In several GCC countries, the larger 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. It also reflects abiding state dependence however.

Government employment is reaching its limits at least in Bahrain, Oman and Saudi Arabia. As national populations grow and seek employment but local business fails to deliver acceptable jobs, 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.

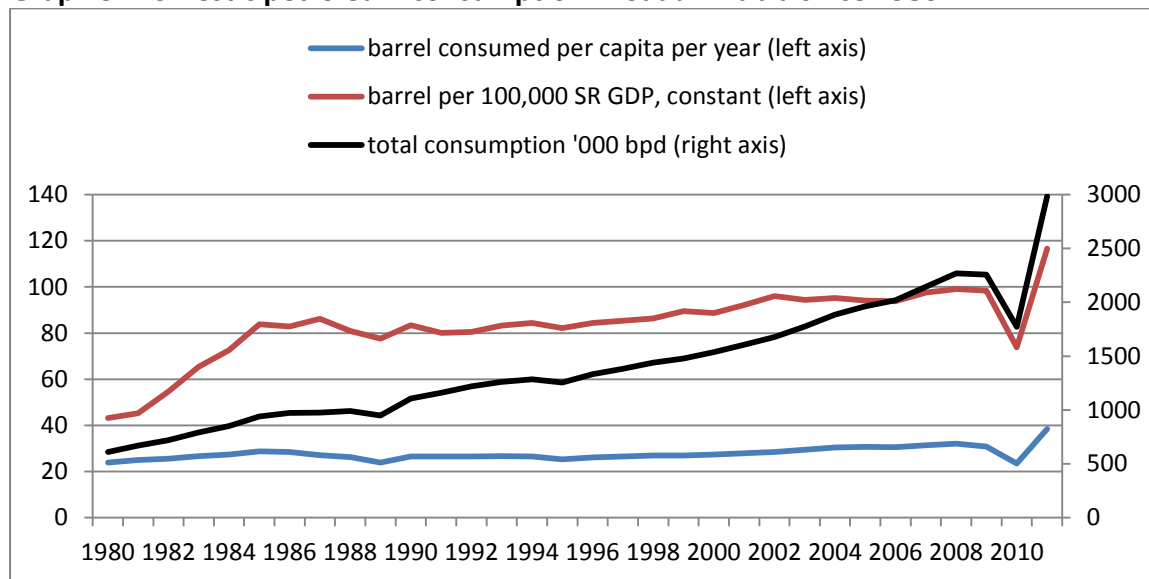
Input subsidies and other state support

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 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 resource-poorer countries.

Cheap capital and energy can be conceived as a comparative advantage resulting from the GCC's rich factor endowment, but their cheap supply comes at a long-term cost: Reliance on cheap feedstock and resource-intensive technology has sapped incentives to move into more efficient and technology-intensive production; as graph 5 below shows, the Saudi economy has become more rather than less energy-intensive since 1980. Domestic energy supplies moreover have hit hard constraints in recent years as gas – used for petrochemical production and electricity generation – has become scarce and expensive to produce, while quickly growing domestic oil consumption could soon eat into the region's export capacity.

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.¹¹

Graph 5: Domestic petroleum consumption in Saudi Arabia since 1980



Sources: EIA, SAMA

The businesses that are trying to move away from energy-dependence tend to be state-owned rather than private: Among all petrochemical companies, Saudi Arabia’s majority state-owned SABIC 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.

GCC manufacturing on many accounts is a success, but it continues to depend on contingent state support. Given capacity constraints, 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.

Contributions to knowledge economies and innovation

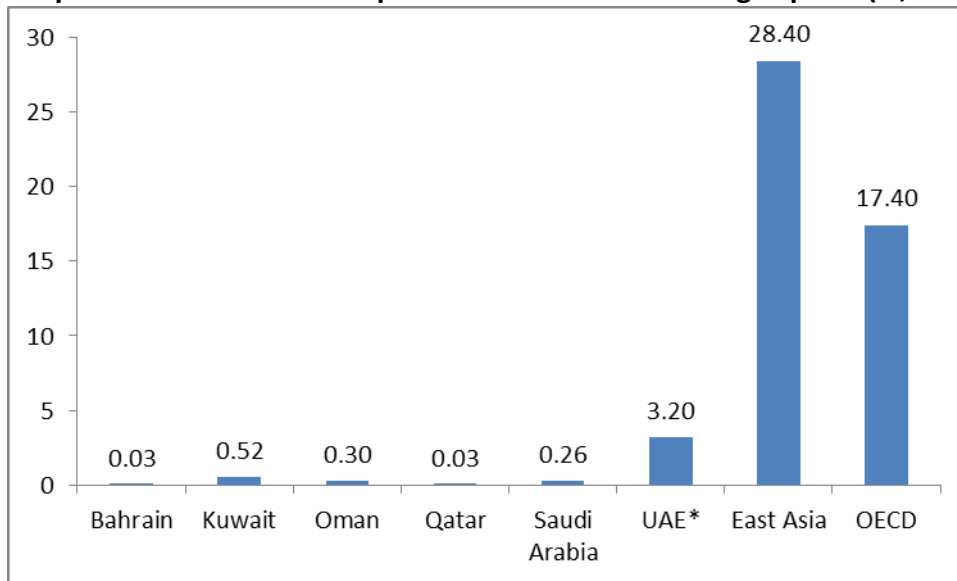
Private sector growth in the GCC has been factor-intensive, relying on comparative advantages in factor prices resulting from a number of state support policies. The flipside of this growth model are weak incentives for upgrading productivity, investing in technology and engaging in research and development – hallmarks of the “knowledge economy” all the region’s governments aspire to.

In fact, total factor productivity of GCC economies has by and large declined since the 1980s (International Monetary Fund 2011: 47f.). Open labor migration and cheap energy have allowed GCC businesses to expand production through increasing labor and energy inputs instead of augmenting productivity.

¹¹ For details on the Saudi case see (Stevens and Lahn 2011).

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. Different from 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 (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,¹² and in the cases where data are available, research and development expenditure constitutes around 0.1% of GDP, compared to about 2% in OECD economies.

Graph 6: Share of hi-tech exports in total manufacturing exports (% , 2009)¹³



* UAE data from 2008

Source: World Bank

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).

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 internationally recruit top talent and attract technology partners. 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

¹² The higher UAE figure might be explained with re-exports of technology goods via Dubai rather than with local production.

¹³ The World Bank defines high-technology exports as "products with high R&D intensity, such as in aerospace, computers, pharmaceuticals, scientific instruments, and electrical machinery."

of modern corporate governance structures harder, it also excludes the local public from partaking in the returns of the private sector.

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, p. 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 QNB – all have the government as a significant, often majority, shareholder, and most of them used to be fully state-owned. The introduction of this article mentioned that of the top 30 Arab listed companies, 25 are located in the Gulf – but 9 of these have local governments as majority shareholder, while 12 have minority government shareholdings.

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 (GCC Board of Directors Institute 2011). And even among listed companies, a limited number of families control a significant share of board seats (The National Investor, Hawkamah, and IOD Mudara 2008). This points to a fairly small, tightly knit and socially exclusive economic elite.

The local shareholder culture, which could force improvements in disclosure and governance, generally remains weak. It is again often the leading state-owned enterprises which are at the forefront of the disclosure and corporate governance debate in the Gulf through participation in e.g. the initiatives of the GCC Board of Directors Institute.

While global and local financial crises have led to some debate about corporate governance in the GCC, the 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. 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.

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 (Maxfield and Schneider 1997).

As we will see in the section subsequent to this, Gulf business has indeed played an important policy-making role in the pre-oil era. It has however lost much of its policy leadership role subsequently, 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 state-owned enterprises and regulatory agencies. In most cases, however, business holds a minority position, and representatives are chosen by the government.¹⁴

Chamber of commerce and industry 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.¹⁵ 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 defense of monopoly privileges, neglecting its tasks in education, product certification, price regulation and improving the private sector's competitiveness. The chamber has been ridiculed for not even publishing a journal.¹⁶

Other institutions have a stronger organizational tradition. Perhaps the most active one is the Jeddah Chamber of Commerce and Industry, Saudi Arabia's oldest chamber, whose programs 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.¹⁷ The poll, conducted under restrictive new rules imposed by the Ministry of Commerce, involved widespread allegations of vote-buying, damaging the institution's reputation.¹⁸

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.

What is the content policy lobbying in the GCC? While in the 1970s and 1980s, private sector elites often demanded increases in government support and protection,¹⁹ business

¹⁴ Interviews with senior businessmen in UAE and KSA, 2009-11.

¹⁵ For details on the Bahraini and Omani cases see (Valeri 2012).

¹⁶ "QCCI to avoid sponsorship issue at PM meet", *The Peninsula*, 23 May 2011; Mobin Pandit, "Why private sector is govt's favourite?", *The Peninsula*, 28 May 2011.

¹⁷ Diana Marwan Al-Jassem, "JCCI poll results out", *Saudi Gazette*, 16 October 2009.

¹⁸ Wikileaks cable 09Jeddah381, Quinn to Department of State, Allegations of vote buying and sorcery on even of Jeddah Chamber of Commerce Election (<http://wikileaks.org/cable/2009/10/09JEDDAH381.html>); Editorial: JCCI elections, *Arab News*, 16 October 2009.

¹⁹ See e.g. *Saudi Arabia Monitor*, May 1987, p. 24.

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.²⁰ Instead, exchanges are often ad hoc. A survey of local press reports on GCC business lobbying between mid-2009 and end-2012 reveals the piecemeal and largely defensive nature of (publicly reported) private sector policy input: Recurring themes are resistance to nationalizing private labor markets, lobbying against fees, taxes and increases in energy tariffs, protests against the potential abolition of the “sponsorship” system that allows easier control of foreign labor, and requests for the government to include local business in contracting arrangements.²¹

Defense of privileges dominated public demands. There is no record of the type of state-business coordination known from Asian “developmental states” focusing on joint information-gathering and coordinated planning of training and technological diversification. 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.

Summary

The preceding sections have shown that the GCC private sector is less immediately reliant on state spending than it used to be and has become the main contributor to national capital formation. 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, 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.

²⁰ For discussion along these lines covering the whole MENA region, see (World Bank 2009, pp. 187-191).

²¹ The survey included the leading one or two English-language newspapers of all GCC countries on a daily basis.

Business in the political arena

The article has so far discussed the role of Gulf business in economic development and economic policy-making. The remaining sections will discuss its contribution to politics strictly speaking, where its role is overshadowed by the state even more, and where business acts in relative isolation from other social forces.

Two larger issues bear detailed discussion: First, the strong decline of the Gulf merchant elites' 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 article, and which explains much of the fundamental shift from political vanguard to regime client.

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 cases also social elites and community leaders (Field 1986; Crystal 1995; Azoulay 2012b).

Merchant elites have 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. Business provided community services and infrastructure that were beyond the capacity of the embryonic states, furthering their 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; Onley and Khalaf 2006).

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, they were instrumentally involved in nationalist and parliamentary movements in the 20th 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 clientelist networks 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.²² But while large parts of the notable elites in the Arab republics were swept aside by the forces of populist Arab nationalism after WWII, Gulf merchant elites instead gradually became clients of the rapidly growing rentier state.

²² For the concept, see (Hourani 1968)

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.²³ Secondly, and less visibly, their remaining nationalist fervor 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". 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. Some of them also own media outlets. More recent arrivals among the business elite often aspire to "notabilization" and are hence especially active in the charitable sector.

Different from the notables of old, however, merchant elites now are unfailingly in hock 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).

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 them additionally – and has put them in a situation of structural opposition to the citizenry.

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" (Beblawi and Luciani 1987). 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).

²³ This best study of this process is (Crystal 1995).

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.²⁴ As Herb indicates, the fundamental tension between business and citizenry is further deepened by the fact that business growth in most countries hardly contributes to employment of nationals, as we have seen above.

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.²⁵ 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 to thereby 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 they destroy business, as the cost of the latter 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 the by far worst record of economic modernization. The Kuwaiti parliament has undermined most of the government's economic and infrastructural reform efforts of the last two decades 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 directly attack the commercial privileges of established merchants, 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 raises for state employees, direct handouts to citizens and reprieves on utility payments on numerous occasions.²⁶ Populist inclinations are however visible even in very tame (semi-)elected

²⁴ This is perhaps a subsidiary reason why broad salary spending has always been privileged over project spending in times of economic crisis.

²⁵ See, for example, Saleh Al-Zahrani, "Private sector can provide 250,000 jobs in six months", Saudi Gazette, 21 March 2011.

²⁶ "MPs' threat to veto Gulf Air bailout", Gulf Daily News, 25 April 2012; Habib Toumi, "Parliament pushes for marriage assistance grants", 8 May 2012; "Bonus for civil servants urged", Gulf Daily News, 2 November 2011; "BD2,000 incentive to pay bills...", Gulf Daily News, 11 January 2012.

institutions like the Federal National Council in the UAE.²⁷ The unelected Majlis Al-Shura in Saudi Arabia seems to have become more populist after the ruling family started to choose its membership along regional and tribal rather than purely technocratic criteria.²⁸ Generally speaking, however, government policy tends to be more pro-business in more authoritarian GCC states with less of a popular veto over economic issues.²⁹

In either type of 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.

Despite some private employment and some entrepreneurship among nationals, the majority of citizens all across the GCC continues 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 record, in a fiscal crisis, popular interests will be privileged over business interests, even in authoritarian rentiers: In times of austerity, GCC regime have cut capital and infrastructure spending, and increased industrial tariffs, while current spending on salaries and transfers as well as consumer tariffs have been protected³⁰ – another sign that the merchants are just a subordinate partner of the ruling elites. 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 beyond customary arguments of “cronyism” and “rentier bourgeoisie”. Business elites are not only 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.

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 several of the early national assemblies in the Gulf. Now business elites are either absent from the political stage or play

²⁷ Samir Salama, “Federal National Council wants petrol prices reduced”, Gulf News, 23 May 2012; Yasin Kakande, “Minimum housing grant 'should be lifted to Dh1m’”, Gulf News, 4 March 2012; Samir Salama, “FNC member urges higher housing loan limit for Emiratis”, Gulf News, 14 March 2012.

²⁸ Discussion with Majlis Al-Shura members, May 2011.

²⁹ On the UAE example, see (Herb 2009).

³⁰ Oxford Analytica, Gulf states' long-term fiscal sustainability in doubt, 21 September 2011; for a detailed account on Saudi Arabia, see (Hertog 2010a, pp. 118-125).

a subordinate loyalist role, usually without the ability to mobilize wider social support for the regime.

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 Bahrain Chamber of Commerce and Industry have publicly supported anti-democratic measures such as more restrictive assembly laws.³¹ 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).³²

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 businessmen 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.³³ Few business representatives have sat in Bahrain’s various post-2002 parliaments, a fact much lamented by business leaders.³⁴

With the outbreak of mass unrest in early 2011, business elites publicly pronounced their loyalty to the Al Khalifa.³⁵ MPs from the new “independent bloc”, which enjoys business support, called for the imposition of martial law in March 2011,³⁶ and businessmen publicly supported the state of emergency pronounced by government.³⁷ BCCI supported both the use of Saudi troops to support 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).³⁸ In September, a group of Bahrainis that included 40% businessmen created a new political group, the “Justice and Development Society” in a renewed attempt by business to counterbalance oppositional groupings.³⁹

³¹ Geoffrey Bew, “Protests law sparks row”, Gulf Daily News, 31 July 2006.

³² Habib Toumi, “Keep top national issues away from polls”, Gulf News, 25 November 2006.

³³ Erel 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>).

³⁴ Abbas Al-Mughni, “Demands for the representation of the merchants in order to protect economic activity”, Al-Wasat, 27 August 2009 (In Arabic); (<http://www.alwasatnews.com/2547/news/read/306113/1.html>)

³⁵ Mahmood Rafiq, “Bahrain chamber raps protesters”, Arab News, 18 February 2011; “Businessmen and traders will start signing the Loyalty Pledge and Swords of Allegiance”, Gulf Daily News, 29 April 2011.

³⁶ Habib Toumi, “Bahraini MPs call for imposing martial law”, Gulf News, 14 March 2011.

³⁷ “Emergency ‘may revive business confidence’”, Gulf Daily News, 16 March 2011.

³⁸ “Two sacked by Chamber”, Gulf Daily News, 28 April 2011. At the same time, Shiite business leaders have generally refrained from supporting the Shiite opposition; Laurence Louer, personal communication, July 2012.

³⁹ “Economy focus for new Bahrain society”, TradeArabia, 12 September 2011.

As a sop for business, fees on foreign labour were abrogated in early 2011;⁴⁰ beyond this, the regime had to do little else to assure 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 neither have they played a leadership role in the opposition, of which they had been critical even before the unrest.⁴¹ Critical voices like those of Shiite business leader Faisal Jawad have been the exception (Valeri 2012).

Kuwait

We have already mentioned the marginalization of Kuwaiti businessmen 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.⁴² As their grip on policy has slipped, business leaders have called for organized lobbying efforts⁴³ – a call that would have sounded strange 40 or 50 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 Mohammad Al Sabah (2006-2011), 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 have 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.

⁴⁰ Habib Toumi, "Community in Bahrain welcomes labour fee freeze on foreigners", 6 December 2011.

⁴¹ Laurence Louer, personal communication, July 2012.

⁴² "End growing political interference to turn Kuwait into economic hub", Arab Times (Kuwait), 11 March 2007; Rania El Gamal, "Politics 'choking' reform in Kuwait", Kuwait Times, 13 March 2007.

⁴³ "Kuwaiti businessmen have little influence over decision makers - Al-Shatti", Kuwait News Agency, 18 February 2007.

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 businessman has been just as limited. Even in the lackluster municipal elections in Saudi Arabia, Islamists have tended to win over business representatives. Business has been marginal in Qatari municipal council elections.⁴⁴ Many members of the elected half of the UAE's Federal National Council by contrast are from large business families (although they are not business leaders themselves).⁴⁵ The franchise for the FNC elections has been limited to a small, handpicked electorate, however. When in March 2011 more than 100 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).⁴⁶

In Oman, 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.⁴⁷ After the outbreak of popular protest in early 2011, the Sultan 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.

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 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.

Will the trend of marginalization in the public sphere 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 for the level and quality of public services is an unlikely prospect in the short to mid-term: GCC-wide proposals to introduce a value added tax have been postponed repeatedly; in the wake of the Arab

⁴⁴ Steven Wright, personal communication, July 2012.

⁴⁵ Khaled Almezaini, personal communication, July 2012.

⁴⁶ Impressionistically, UAE business leaders have retained more of their status as social elites than in other GCC countries – possibly explained with strong pre-oil merchant traditions, later development and a small local population. This does not give them any political autonomy, however.

⁴⁷ Marc Valeri, personal communication, July 2012.

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 on private labor 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.

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.

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 it remains dependent on the state, living off government support in both obvious and less obvious ways, and contributing almost no taxes in return. Business has used the GCC's comparative advantages well, but has not employed them as stepping stones into the much vaunted “knowledge economy” – instead, it has witnessed declining productivity and failed to provide quality jobs for GCC citizens. GCC governments continue to drive economic policy-making and –through state-owned companies – the diversification agenda, with business lobbying often limited to the defense 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 the absence of organic links to the wider society through employment, taxation or investment have further undermined the political autonomy of Gulf business elites.

While the regime requires minimal support or at least acquiescence from the masses even if these don't generate taxes or participate in local production, business has no essential structural role to fulfil. State support and a growth model built on privately held wealth, no taxation and cheap foreign labour make for good profits, but they also limit the political potential of business as either allies of the ruling elite or as autonomous political player.

If GCC business is to ever 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 relatively 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 likely 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 more so since rulers have become more attuned to popular welfare demands with the Arab uprisings.

The position of business as described in this article 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 however does not mean 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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