Full customs union ready by early 2015

#Kuwait

#SaudiArabia

#Qatar

#Bahrain

#Oman

#UnitedArabEmirates

GCC

Gulf Cooperation Council

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The six robust economies of the Gulf Cooperation Council, apart from venturing away from oil into new business sectors, are cementing plans for a customs union to commence next year, which will enable the creation of a full economic union in the future

At the upcoming 2014 GCC Summit, the leaders of one of the world's most economically and politically newsworthy regions will focus primarily on formalizing the Gulf Customs Union. The new trading bloc has been more than a decade in the making and will enable the free movement of goods and services within the region. First agreed in 2003, full implantation of the union has been delayed because of disagreements between GCC member states – Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the United Arab Emirates – on the distribution of customs revenues, among other issues, yet the concept has never lost its staunch support from certain corners.

At the 2011 GCC Summit, Saudi King Abdullah Bin Abdul Aziz Al Saud had strongly expressed his desire for this six-way alliance to "transition from the stage of cooperation to the stage of the union." Two years later, Saudi State Minister for Foreign Affairs Nizar Bin Obaid Madani reiterated the importance of expediting the process, saying: "Moving to the union has become a necessity imposed by the great importance of the Gulf region and the strategic political and economic aspects that have also brought numerous risks and problems."

At the regular meeting of GCC finance ministers in May this year, a consensus was finally reached to remove all obstacles to the full implementation of the customs union. Barring any last-minute disputes, the December GCC Summit will see that the union goes into effect early next year.

Already, the partial application of the customs union contributed to tripling inter-GCC trade between 2005 and 2012 – from $32 billion to $100 billion. This represents a low proportion of the GCC's total foreign trade (it stands at some 10% while intra-EU and intra-Asean trade account for 60% and 25%, respectively), due in large part to the similar nature of its export commodities. However, a fully-fledged customs union will, perhaps more importantly, facilitate more joint ventures and in turn, contribute to greater economic diversification. This is one of the top priorities among member countries, whose economies (with the exception of UAE) depend largely on hydrocarbons. Indeed, together the GCC countries produced 24% of global total crude oil production last year and control 30% of the world's crude oil reserves, according to a 2014 British Petroleum report.

In fostering new industries and sectors, GCC member states are creating ever-growing demands for power. So as to not diminish revenues from hydrocarbon exports, alternative sources – including coal and nuclear, wind, hydro and solar power – are being increasingly harnessed. Meanwhile, the countries are also looking at ways to increase generation efficiency. Saudi Arabia, for example, is converting single-cycle plants to combined-cycle, which will increase thermal efficiency from 30-35% to a forecast 40-45%.

In its 2014 report on the region, engineering and consulting firm Black & Veatch identified the GCC's power segment as a potential area for foreign entrepreneurs to get involved. Meeting and managing the region's expanding needs, the report said, "will increasingly require companies that have expertise in delivering both water and energy projects, and successfully combining insights from both".

"GCC states have made major investments in energy infrastructure during the last decade, and high levels of spending are forecast in order to meet growing demand. Asset creation, however, is only half the story," the report continues.

"To deliver the levels of customer service and environmental performance that end-users and governments seek, GCC states' infrastructure asset base needs to be managed effectively. We see this as a growth area."

This coincides with the substantial business reforms the GCC members have been passing over the past several years. As a region, the GCC boasts one of the most favorable tax regimes in the world, while the reforms have made it easier to start a business, obtain credit, and conduct cross-border trade. Saudi Arabia, for example, is embarking on one of the world's most ambitious infrastructure programs now, and to help attract foreign direct investment (FDI), its Council of Ministers has recently removed many barriers to bidding for government projects.

Yet in spite of these virtues, last year marked the fifth consecutive year that FDI inflows to the GCC dropped – from more than $60 billion in 2008 to $24 billion in 2013, according to a National Bank of Kuwait report. The report attributes this partly to the completion of major projects, such as Qatar's liquefied natural gas expansion program and several petrochemical and construction projects in Saudi Arabia.

Kicking the negative group trend, however, Bahrain and the UAE have recorded four consecutive years of growing FDI inflows, "as investors return to the property, manufacturing and services sectors", which augurs well for the region's economic diversification ambitions.

The drop in FDI to the GCC has done little to harm the region's economic growth so far. "The growth outlook for the GCC is positive, but will be affected by global and regional developments. While growth has slowed from the exceptionally strong rates in 2010-2011, it remains robust," the International Monetary Fund reported last year.

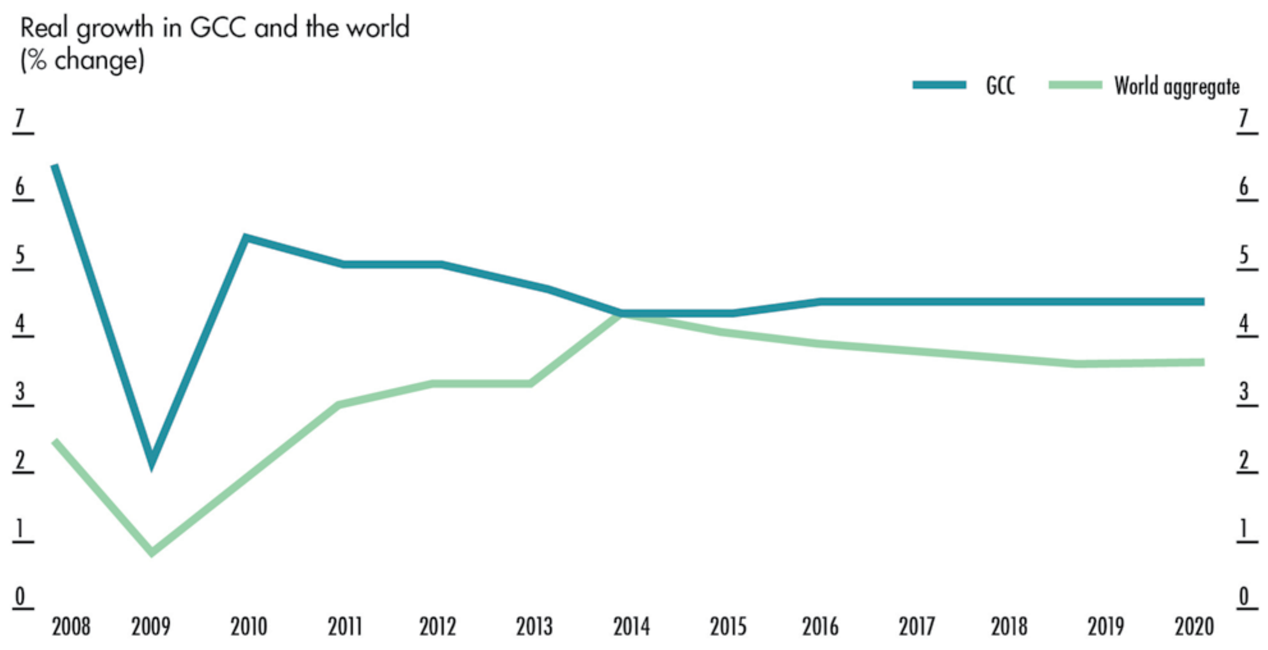
At a recent conference of the International Institute for Strategic Studies, Kamal bin Ahmed, Bahrain's Minister of Transport and Acting Chief Executive of the country's Economic Development Board, argued that the GCC has the strongest economic fundamentals of any region in the world. These include, he said, robust and resilient economic growth, sustainable public finances and household balance sheets, current account surpluses and great prospects for continued growth through investment and the diversification of member economies.

The rest of the world has certainly taken note of the GCC, and not just for its economic might. Member countries such as Saudi Arabia, Kuwait and Qatar wield significant influence in diplomacy, and Oman has acted as a go-between for sometimes confidential negotiations involving the West and Iran.

Qatar and other members have hosted major international sporting events, including the 2006 Asian Games, and Qatar has signed on to host the 2022 FIFA World Cup, creating air-conditioned stadiums and all. Dubai is a byword for luxury, Oman is becoming a tourism magnet, and regional carriers like Emirates Airlines, Etihad Airways, Gulf Air and Qatar Airways are expanding their routes worldwide with their home airports as major hubs.

At the same time, prestigious Western universities, museums and other institutions are setting up branches in several of the Gulf countries, bringing the finest minds and best art to a new, appreciative population.

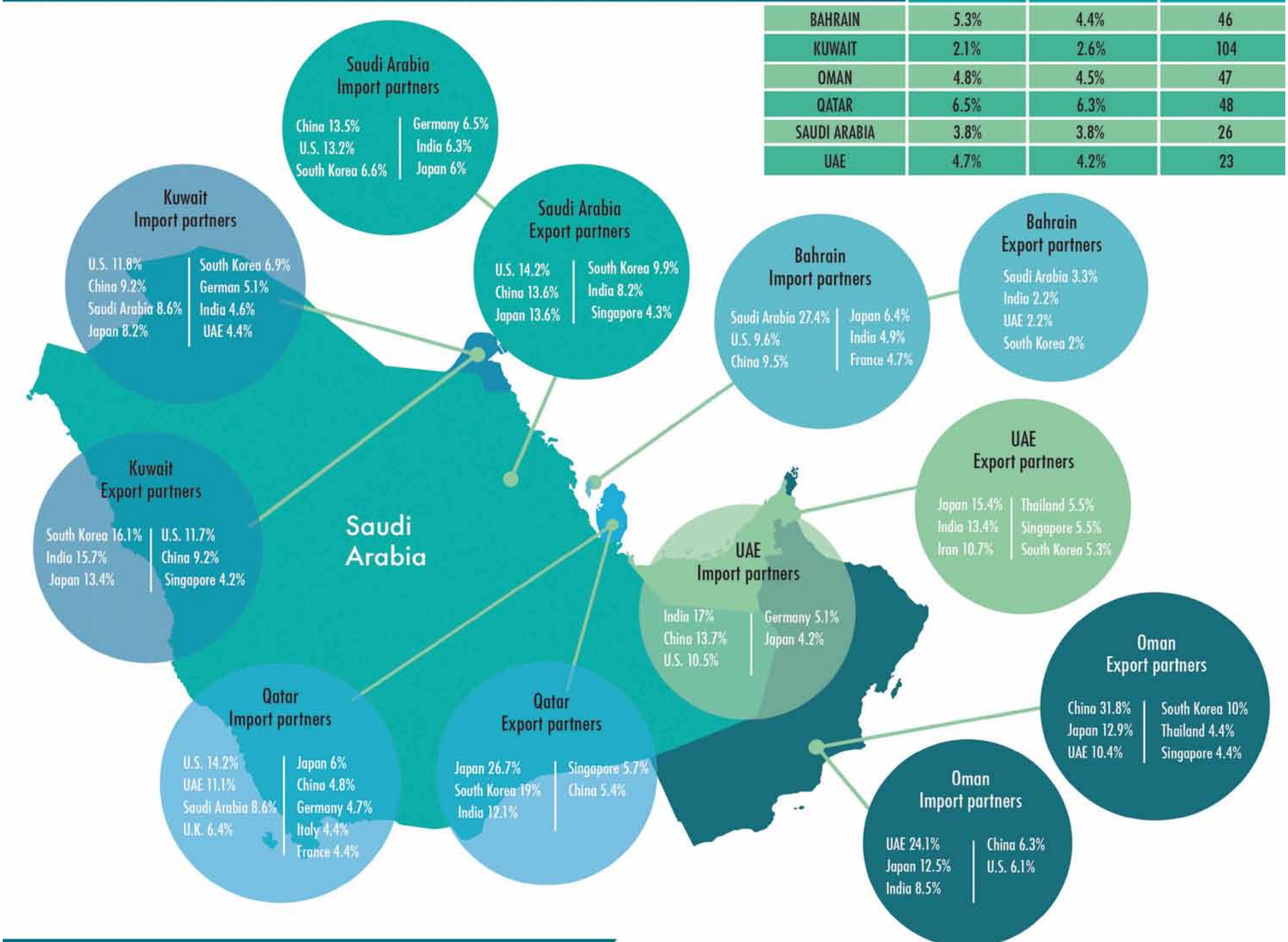
At a time when the world seems to be in perpetual crisis involving unrest across parts of the Middle East, a frightening health epidemic with its economic impact still unclear, uncertainty on the U.S. political horizon and so much more, the GCC leaders are making an extra effort to ensure that their countries continue on the current path of peace and prosperity.



Source: Economist Intelligence Unit

GCC economic and trade landscape

	2013 GDP growth estimate	2014 GDP growth forecast	Ease of Doing Business rank 2013
BAHRAIN	5.3%	4.4%	46
KUWAIT	2.1%	2.6%	104
OMAN	4.8%	4.5%	47
QATAR	6.5%	6.3%	48
SAUDI ARABIA	3.8%	3.8%	26
UAE	4.7%	4.2%	23



Source: CIA World Factbook, the Institute of International Finance (IIF) and national sources

Falling oil prices fuel diversification drive

The Gulf Cooperation Council countries have taken a hard look at their dependence on one economic sector – hydrocarbons – and are taking action to diversify their economic activities

FOR THE GCC members, the problem of the "resource curse", or over-reliance on oil, is becoming acute. Most pressing is the fact that the price of their principle export commodity, oil, has fallen by 23% since June and there is little hope that prices will again rise anytime soon to the $100 per barrel enjoyed in recent years.

"The GCC countries have grown strongly and seen huge improvements in their development indicators, but they remain susceptible to fluctuations in oil markets," International Monetary Fund Deputy Managing Director Min Zhu said earlier this year. These countries "need greater economic diversification to help boost productivity and living standards, create jobs, and reduce the fiscal and external risks associated with the heavy reliance on oil revenues."

GCC economic planners have already instigated some diversification programs. Saudi Arabia is spending tens of billions of dollars to establish so-called "economic cities" around the kingdom, designed to enhance competitiveness, create jobs, improve Saudi skill levels, develop the regions where they are located and, most importantly, foster economic diversity.

Each city is to be developed by the private sector and generate major private investment opportunities in infrastructure, real estate and industry, according to the Saudi government.

Private public partnerships are key to the scheme with the government acting as the regulator, facilitator and promoter, while the private sector takes care of providing capital, land ownership and development.

Over the past 20 years, the UAE has been successful in transforming itself into a world-class passenger and cargo transport hub and a chic, international tourism destination boasting luxury hotels, restaurants and shops.

In Qatar, the government has worked to promote major international cultural and sporting events, created a financial center, and established a well-respected airline and air transport logistics.

Kuwait and Oman are promoting small and medium businesses, while Bahrain has important steel, petrochemical and metal industries, including the ninth-largest aluminum smelter in the world.

But more needs to be done. Ernst & Young has noted in its October Growth Drivers report that harnessing the potential of the alliance could very well be a key in expediting diversification.

"Each of the Gulf states has developed long-term strategies, using different combinations of vertical and horizontal diversification," writes Advisory Partner Michael Hasbani. "But the region has yet to take advantage of coordinated diversification to leverage each other's strengths and maximize the power and attractiveness of the economic bloc. Better coordination would lead to greater efficiencies and reduce the duplication of economic activities."

Furthermore, boosting the GCC's private sector and employment in private enterprises, instead of the traditionally better-paying and more benefit-rich public sector, is vital, along with new markets for non-oil goods. Linked to this is improving the quality of education in the GCC member states, another must to guarantee that workers have the required skills to operate and prosper in the private sector.

"Educational reform is vital. Improving the quality of outcomes from the education and training system for nationals is imperative to creating a local workforce," says EY Advisory Partner Will Cooper. "The focus must be on developing the right skills for young nationals and encouraging an enterprise mindset as they progress from education to work."

EY goes on to recommend the GCC promptly welcome more global talent to lend their expertise and work in league with GCC nationals. "The Gulf opportunity is large, but it is time-bound," writes Gerard Gallagher, MENA Advisory Managing Parner at the consulting firm.

"Now is the time to take advantage of the region's short-term attractiveness to become a long-term global magnet. Fine-tuning the Gulf states global positioning, through country branding, improving regulatory environments while maintaining a sense of security and contentment for their citizenry during a period of economic growth and social change, will carry their existing successes into the future."

% change in hydrocarbon and non-hydrocarbon GDP

		2011	2012	2013	2014 forecast	2015 forecast
BAHRAIN	HYDROCARBON	3.6	-8.5	15.3	0.3	4.8
	NON-HYDROCARBON	1.7	4.5	4.5	4.8	2.5
KUWAIT	HYDROCARBON	15.4	11.7	0.7	1.1	0.8
	NON-HYDROCARBON	4.3	4.1	4.0	4.5	5.5
OMAN	HYDROCARBON	2.0	3.8	2.4	1.5	1.2
	NON-HYDROCARBON	-0.1	7.4	6.8	7.0	6.2
QATAR	HYDROCARBON	15.7	1.2	0.1	-0.6	0.0
	NON-HYDROCARBON	10.8	10.3	11.4	11.0	11.0
SAUDI ARABIA	HYDROCARBON	11.0	5.7	-0.6	0.5	-0.6
	NON-HYDROCARBON	7.9	5.8	5.0	4.6	4.6
UAE	HYDROCARBON	6.6	4.9	4.4	2.3	2.5
	NON-HYDROCARBON	2.6	4.1	4.9	5.2	5.2

SOURCE: National sources and IIF

Allied against Islamic State

The past year has seen tensions among the council's member countries, yet the six-member alliance has pulled together to support the U.S. in its fight against the rapidly spreading jihadist group, ISIS

THE GCC is still patching up the cracks in its fairly solid façade caused by Qatar's reluctance earlier this year to abide by an agreement to sever ties with the radical Muslim Brotherhood organization. The agreement had also called for ending broadcasts by the Egyptian cleric Sheikh Yusuf al-Qaradawi and curtailing activities by suspected Iranian agents in the GCC.

Saudi Arabia, the UAE and Bahrain recalled their ambassadors from Doha in March in protest and out of concern for their security. Despite rising tensions, negotiations eventually kicked in and compromises were discussed. In September, Qatar, according to press reports, expelled leaders of the Muslim Brotherhood resident in the country and made other pledges to smooth things over with its GCC partners, thus bringing to a near-close what has proved to be perhaps the worst intra-GCC dispute in the council's history. The ambassadors, however, have yet to return to their embassies in Qatar.

This resolution, albeit partial, had come just in time to allow the six-member alliance to once again stand united against another threat to the Middle East: the Islamic State in Iraq and the Levant (ISIL), which is also referred to as the Islamic State of Iraq and Syria (ISIS). The GCC has been joined by Egypt, Lebanon, Iraq and Jordan – thus earning the nickname GCC+4 – in its stance against the Sunni extremist organization. On September 11, leaders from the 10 countries met with U.S. Secretary of State John Kerry in Jeddah to state their support and intention to "do their share" for the U.S. coalition fighting ISIS.

The resulting communiqué from this high-level meeting stated that all countries are "to stand united against the threat posed by all terrorism, including the so-called Islamic State in Iraq and the Levant (ISIS), to the region and the world."

During the meeting, Saudi Arabia agreed to provide the U.S. with bases for the training of moderate Syrian rebels, who are fighting against both ISIS on one side and the government of Assad on the other.

After the meeting, Saudi Foreign Minister Prince Saud al-Faisal told the press, "There is no limit to what the kingdom can provide." This has become evident over the following weeks; as well as assisting the coalition, the kingdom has contributed half a billion dollars to UN humanitarian aid agencies in Iraq.

The GCC+4 communiqué also went on to cover other aspects of the struggle against the ISIS, saying steps would be taken "to stop the flow of foreign fighters through neighboring countries, countering financing of ISIS and other violent extremists, repudiating their hateful ideology, ending impunity and bringing perpetrators to justice, contributing to humanitarian relief efforts, assisting with the reconstruction and rehabilitation of communities brutalized by ISIS, supporting states that face the most acute ISIS threat, and, as appropriate, joining in the many aspects of a coordinated military campaign against ISIS."

In late September, Jordan plus four GCC members (UAE, Saudi Arabia, Qatar and Bahrain), helped the Pentagon carry out air strikes against ISIS targets, while Qatar has also carried out several humanitarian flights. Nevertheless, Qatar seems to be sitting on the fence, as it has not fully cut ties with all hard-line Islamists and their supporters, and has been accused of affording them safe haven within its borders.

Time, and the coalition's efforts, will tell if ISIS can be stamped out. And time, and the yet-to-be-seen extent of the GCC's influence over its own members, will tell if the alliance will remain united and strong in the future. But what is certain is that the GCC as a whole remains a strategic and friendly ally for the U.S. in this troubled region of the world.