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THE UNITED STATES AND THE GCC: ECONOMIC CHALLENGE AND RESPONSE

By

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In the past half century, Saudi Arabia has helped to establish the world's oldest and newest regional organizations. In February 1945, the Kingdom, along with Egypt, Iraq, Syria, and North Yemen, formed the League of Arab States. The only organization of its kind at the time, various aspects of the League's preamble, charter, and structure were later examined and adapted by the United Nations. Saudi Arabia's King Fahd was a delegate to the conference in San Francisco that founded the UN in 1945.

King Fahd, together with the heads of state of Kuwait, Bahrain, Qatar, the United Arab Emirates (UAE), and Oman, is also a co-founder and leader of the Gulf Cooperation Council, established in May 1981. Just as the establishment of the UAE from seven independent entities demonstrated the art of the possible in 1971, so the GCC, inspired in part by that example, has constituted a building block for additional, albeit nascent, movements which seek regional cooperation and integration among other Arab countries. (See essay on "Geopolitics").

The GCC's founders were inspired by knowledge that each of the members would be able to enhance various aspects of its national interests through participation in the Council. The GCC's continuing ability to protect and promote the mutual interests of its member countries and the consensus of the members that they could better advance their common interests collectively have played an integral role in the success of the organization.

The Quest for Economic Cooperation

In contrast to the perception among many that the GCC as an institution is preoccupied with defense and security matters, the day-to-day activities of the organization are centered far more on a broad range of economic, infrastructural, and developmental issues. Many of these, to be sure, have a defense or security component. However, as a dimension of the GCC Secretariat's processes and objectives overall, these components are more often incidental and nascent than causal or central. Indeed, the questions that animate the daily dynamics of the group are generally linked more to coordinating administrative and technical issues related to the GCC region's economic resources, plus administrative and planning mechanisms, than they are to defense or security, per se.

The GCC's economic mission is to coordinate and integrate the policies of the six member countries toward a common market with the prospect of an eventual merger into a single economic entity. Within this context, the major goals are to diversify the six economies away from dependence on crude oil exports for national income; to industrialize, both "downstream" in the petroleum sector and into non-oil sectors; and to increase exports and reduce the heavy reliance on imported goods.

The position and role of the GCC in the development planning of the member countries is critical to these goals. Consolidation of the local markets is necessary to support import substitution industries, and all the industrial schemes will depend on economic cooperation to avoid duplication.

Opening up foreign markets to GCC industrial exports -- a far more difficult task -- will necessitate the combined bargaining power of the entire group. To be sure, significant further penetration of the U.S. and EC markets in categories other than petroleum currently constitutes the greatest challenge to GCC export efforts.

Joint ventures between GCC and foreign firms offer a quite different set of opportunities. Such ventures will benefit from location in the GCC country with the greatest economic rationale for the particular industry, a lack of local competitors, an enlarged local market protected from foreign competition, and assistance in reaching potential customers overseas.

Investors and potential economic and trading partners are becoming increasingly aware of the GCC countries' comparative economic advantages, not only in energy and capital, but also in low-cost loans, full repatriation of profits, free land, and tax-free incentives as well as the free enterprise philosophy that prevails throughout the GCC.

In its earliest meetings, when general goals and guidelines were being formulated, the GCC's leaders focused on standardizing subsidies for basic commodities; unifying rates for water, electricity, and gasoline; eliminating trade barriers; and increasing the economic rights and privileges of the GCC citizenry. While major progress has been registered in each of these fields, it is at the level of the individual that the most remarkable breakthroughs have occurred. With reference to this category, Saudi Arabia's Prince Saud, Chairman of the Ministerial Council for 1987-1988, has remarked that, "In the final analysis, it's the economic aspects that will benefit the GCC citizens the most."

In contrast to the situation prevailing when the GCC began, the situation today is one where a doctor, lawyer, engineer, or accountant certified in any GCC state is free to practice in any of the other member countries. Individuals, moreover, can now own land, open businesses, obtain loans and development funds from banks, and attend schools in member countries other than their own on an equal basis with that country's citizens.

These breakthroughs have increased substantially the volume of human interaction and trade between and among the six countries. In only a few years' time since the implementation, in stages, of the Unified Economic Agreement of 1981 -- an agreement which, inter alia, calls for intra-GCC freedom of travel for the citizens of each member country, freedom of commerce between member states, and the construction of a common economic infrastructure as stepping stones on the path to economic integration -- nearly a thousand GCC citizens, by 1988, had taken advantage of the provisions permitting the practice of the aforementioned professions.

The emphasis on joint projects as a means of attaining integration and development appears to have been vindicated. The number of joint ventures between member states has also increased at a rate higher than anticipated. In 1988, the number of joint Gulf Arab industrial projects implemented in the private sector totalled 95 with an investment of more than $2 billion. Of these, 37 of the projects were underway in Saudi Arabia, 28 in the UAE, 11 in Bahrain, eight in Oman, six in Kuwait, and three in Qatar. Those between citizens of Saudi Arabia and other GCC citizens, for example, are up more than 25% since the agreement.

The GCC's International Economic Relationships

The GCC has been edging its way toward a breakthrough with one of its most important trading partners, the European Community (EC). The eighth GCC summit in 1987 authorized the Ministerial Council to negotiate a draft agreement with the EC on the subject of the EC's protective tariffs against GCC-produced fertilizer, plastics, and chemicals. The EC agreed to freeze tariffs at the 1987 levels and conclude a wide-ranging agreement, on the basis of preferential treatment, to rationalize the tariff structure. An interim draft "agreement to agree," freezing EC tariffs at their existing levels in anticipation of negotiation of their steady reduction, and of a possible free trade agreement, was signed in 1988.

The GCC makes no effort to hide the fact that its ultimate objective in negotiating with the EC and, eventually, with the U.S. is a free trade agreement much like that which exists between the U.S. and Canada and the U.S. and Israel. While the concept gives cause for concern among many Europeans and Americans, the GCC, realistic about the prospects in the short run, is determined that there must be steady, incremental progress toward the goal of placing its relationship with all of its major trading partners on firmer footing.

On the U.S.-GCC side of the ledger, the consultations have proceeded to a stage where the American and GCC participants have established three areas of focus: trade and commerce, investment, and energy. One of the main agenda items is the exchange of trade data between the GCC and the U.S. as a prelude to any major trade agreement. Major roadblocks, however, lie in the path of any true Free Trade Agreement. One such problem continues to be American and Arab laws on boycotts.

GCC officials are keenly aware of the hurdles that lie in front of them in their trading relationship with the United States. As one of the participants in the talks remarked, "From where we sit, the U.S. Congress appears to be as protectionist as those between the two World Wars. We have reason to fear such sentiments, especially those that relate to our exports. These appear to be threatened by talk that surfaces from time to time about an import tax on crude oil, refined products, and petrochemicals. At least with Europe we have reached a stage where we can negotiate an agreement in which we can both begin to plan with confidence for the future. We want to achieve the same kind of understanding with the U.S."

Some of the participants in the economic consultations believe there is more likelihood the GCC and the U.S. will make progress on investment issues than on the trade front. All the GCC countries are anxious to promote investment.

Progress on the GCC's interest in negotiating a bilateral investment treaty with the U.S., however, is likely to come slowly, if at all. It's not so much that there is opposition to such a treaty in the U.S. Executive Branch, although some opposition exists, and it remains uncertain whether a consensus in favor of such a treaty will emerge. Rather, the more formidable short-term obstacles have been the existence of close to a dozen draft treaties with other countries ahead of the GCC and the Bush Administration's preference for pursuing a multilateral rather than a bilateral approach to GCC investment and trade issues.

The GCC countries, despite whatever disadvantages that may occur in their relationships with specific trading partners, are likely to remain influential participants in international finance, investment, and developmental assistance. Together they function as a force to be reckoned with in the World Bank and IMF, in OPEC and OAPEC, and in such organizations as the Arab Monetary Fund, the Arab Fund for Social and Economic Development, and the GCC's own investment body, the Gulf Investment Fund.

Moreover, in international deliberations in search of ways for dealing with the indebtedness of developing countries, GCC and Western ministers of finance are increasingly seating themselves on the same side of the table. The number of shared perspectives and agendas between GCC and Western financial institutions, borne of common concerns and mutual interests, is growing.

Three other factors have added to the GCC's expanded economic significance in regional and international affairs. Although the overall GCC market, at roughly 12 million people, is small -- a quarter the size of Egypt's and half that of Canada's -- the member countries themselves have become major actors in international trade. Collectively, in a nation-state system of more than 155 countries, they've been for most of the 1980s America's sixth largest trading partner and of even greater importance to the European Community.

Domestically, the changes in the GCC's position in the global market place have led to a vast new range of economic opportunity for their citizens. Each of the member countries' economies has evolved to a sophisticated production stage: in the past, they exported oil with a minimum of effort and intermediaries. Their modern and largely complete infrastructures permit an unprecedented productive capacity in a variety of traditional and non-traditional areas.

This has fundamentally altered the domestic business environment, allowing for the expansion of an influential private sector characterized by a free-wheeling capitalist style. As a consequence, "It's not surprising," says one GCC official, "that a growing number of our citizens want a piece of the action."

At the regional level, the export-oriented sectors of the GCC's economies have already made impressive strides. GCC countries have shown an increasing capacity to sell their products and services to the sizeable neighboring markets of Egypt, Iraq, Jordan, and the Yemens, as well as those of the Indian subcontinent and parts of East Africa and South Asia. American firms, such as Proctor and Gamble, have realized the advantages to be gained in working with and through the GCC to reach neighboring markets and, accordingly, are relocating more and more of their regional production and marketing facilities to GCC countries.

Also, in good times as well as bad, the GCC countries have continued to denominate their exports in dollars, which, in turn, has contributed to the ongoing preeminence of American banking and finance worldwide. And in terms of investment in the United States, the GCC stands as a group second only to Japan in the purchase of U.S. Government securities which are used to finance the U.S. national deficit.

All these reasons indicate that, for the forseeable future, the GCC is likely to remain an integral part of the world economic order. As a former U.S. Ambassador to one of the GCC countries commented, "This is the bedrock that will help us withstand future strains in the international energy situation."

Prognosis

Although the commercial climate overall was cautious and conservative during the Iran-Iraq war from 1980 to 1988, business confidence has been rapidly returning to the region since the cessation of hostilities nearly a year ago. The GCC private sectors, with easy access to first class export and re-export facilities, are especially well-positioned to participate actively in the reconstruction of both the Iraqi and Iranian economies.

In addition, GCC stock market prices, which have increased steadily since 1986, and the growing trend towards privatization continue as positive indicators of the GCC's economic health. Indeed, the number of GCC citizens who have invested in what were previously 100% government-owned companies, the speed and enthusiasm with which they have subscribed to the shares when offered, and the profitability of many of the companies, have surprised everyone.

Moreover, oil revenues for both 1987 and 1988 exceeded $30 billion, a level quite adequate to maintain a healthy economic environment for a total GCC population of about 12 million. Of related importance, according to studies by the Gulf International Bank (GIB) in Bahrain, GCC per capita public sector expenditures in the late 1980s -- at an average of $5,500 compared to $4,000 for the U.S., $2,000 for West Germany, and $350 for South Korea -- and per capita income, at an average of $10,000, continued to rank the highest in the world.

Additional factors augur well for further GCC economic growth in the period ahead. For example, beyond having 50% of the world's petroleum resources beneath its lands (See essay on "Energy"), and, according to GIB figures, total external government assets in excess of $180 billion -- most of which is believed to be in liquid assets -- GCC private sector assets placed abroad exceed an estimated $100-150 billion.

Other factors include the ongoing movement among GCC countries toward a common market and a unified exchange rate system; continuing internal stability of a kind unmatched by any six geographically contiguous countries elsewhere in the developing world; the steadfast adherence of the GCC governments to the economic philosophy of the free enterprise system; and, directly related to the high priority assigned to the GCC's human resource development programs, the rapidly declining illiteracy rates, the annual 3% population growth, and, in terms of local market potential, an anticipated population approaching the 1980s population of Canada, America's number one trading partner, by the end of the century.

As one looks to the 1990s, Western and American economic and related interests in the GCC are likely to remain primarily of a strategic nature, stemming from what the GCC has, where it is, and what it does. It has an abundant supply of vital energy, it lies astride a crossroads between Europe, Asia, and Africa, and is critical to the Western alliance. As to what it does, it acts conventionally, conservatively, responsibly, and, within the limits of its means, generously. In terms of what it brings to the table, the GCC's style, its resources, and its international situation distinguish it from any other regional organization.

Few who work the issues on a day-to-day basis will deny that the U.S. and numerous other countries need to tend their relations with the GCC better than they have, and must, with regard to the future. As for the GCC, that it has come this far in the face of unprecedented adversity, and managed not only to survive but to thrive, is itself an important accomplishment in the annals of other experiments in international organization. Whatever else it may yet achieve in the future, in the economic arena alone it can already be reckoned as the most ambitious multi-country undertaking in the history of regional cooperation and integration in the Arab world.

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