ECONOMIC DIVERSIFICATION OF GCC STATES: PLANS AND POLITICS

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ABSTRACT

The GCC is an intergovernmental union of six Arab states in the Arabian Peninsula. It was established in 1981 to foster economic cooperation, protect their common interests and coordinate economic and social policies among the member countries. Due to the high abundance of hydrocarbon resources, the economies of GCC states have been highly dependent on oil and gas. However, recently we've seen immense volatility in oil prices which for a period of time resulted in a decrease in revenues of GCC states and posed a reason and challenge for them to accelerate their economic diversification efforts. In order to overcome this, they are investing heavily in diversifying their economies and reducing the reliance on oil and gas as a risk their countries are exposed to. This research paper will discuss the economic diversification efforts of the GCC states and how it will affect their political power in the future.

INTRODUCTION

The GCC states are defined as the member states within the Gulf Cooperation Council. The six countries are located in the Arabian Peninsula and border the Gulf. These countries include Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the UAE. This council was formed in 1981 and its main purpose is to maintain collective security and to maintain economic development organization between them. It also serves to strengthen the ties between these member states. The purpose as described by Britannica is, "to achieve unity among its members based on their common objectives and their similar political and cultural identities which are rooted in Arab and Islamic cultures."

These countries all share a similar attribute as they are all dependent on hydrocarbons as large percentages of their GDP. This is largely due to the fact that their geographical location puts the countries in the GCC directly on some of the largest oil reserves in the world. Due to its consistent demand around the world, it has provided an easy method for these countries to trade internationally. These governments have invested heavily in technology and infrastructure to make it one of the most efficient in the world in regards to oil production in order to take advantage of this. With this focus from the top of the structure in the states, it consequently has given a minority of individuals in the region immense wealth leading to a cycle of reinvestment over the years into oil allowing these countries to become so largely dependent on their international trade of hydrocarbons. Various countries of the GCC region and their oil dependence can be exemplified through Saudi Arabia as they are the world's largest exporter of oil and having the second largest oil reserves and the world's largest production capacity due to its investment in the industry. It also holds a significant influence over the global petroleum market and its price dynamics. Qatar is also a very important country in the global energy market as the world's largest exporter of liquified natural gas and earns nearly all of its government revenue from oil and related products.

Due to this large dependence on hydrocarbons, their economies and country's politics have become largely intertwined with the volatility of global oil prices and global oil demand. Also, as countries around the world attempt to reduce their usage of oil overtime citing some plans by the UN to reduce carbon emissions, as part of the Paris agreement, they seek to reduce greenhouse gas emissions to limit warming to 1.5 degrees celsius by aiming for a peak of gas emissions before 2025, declining by 43% by 2030 and net zero by 2050. Whether this will come to fruition is yet to be seen; however, the thought is there and with that comes a risk for these GCC states whose entire economies and international politics have become so intertwined with global oil demand.

The solution to this for the GCC states has been discussed over the years and the common consensus is the need for economic diversification. Economic diversification is defined as the process in which an entity increases its range of markets, sources of income and range of products in order to reduce its reliance on any one industry, sector or geographic area thereby making an economy more resilient to shocks and changes in global demand. This is a sensible solution to the issue at hand.

However, with any large change for a country, especially relating to the economy will come a change in the politics. Domestic politics have been affected over the years by how their respective nations are greatly impacted by oil, consequently driving their dependency on resources and causing many states to focus on developing and upgrading their oil production capacity while neglecting other development initiatives. This has had negative effects on increasing other areas of life, overall security, health and socioeconomic development of citizens. The uneven distribution of resources enabled the ruling dynasties and autocrats to further control and adjust their political systems by tailoring them to their own benefit. This leads to many of these states becoming increasingly conservative and in some cases oppressive in their policymaking in many parts of the region to allow them to continue to rule and stay in their wealthy positions. Internationally, politics are also just as affected by any changes in the fundamentals of these countries. Other countries and for example, the United States benefit from the economic pressure given the GCC's states' reliance on oil exports as it allows them to influence foreign policy in the region. The United States has major interests in the region and these issues in some cases are oil dependent. An example of this may be how the US supplies weapons to the GCC states in effort to fight Iran and other potential threats, or their stationing of major US military forces to "protect" the GCC countries citing some of the strongest US-GCC

State alliances being with Saudi Arabia and UAE. Due to the politics in the region being so dependent on large importers of oil like the US, the US has been able to wield influence and control over decision-making and even sometimes to the extent of it working against their own national interests. One example of this can be cited from June 2017, where Saudi Arabia and several other GCC states severed diplomatic ties and imposed trade and travel sanctions against Qatar. In response, the United States attempted to mediate and encourage dialogue and was successful in helping broker a settlement in January 2018. An example of when the United States has imposed export control measures on GCC states is shown through the Iran Nuclear Deal which places stringent restrictions on the region's exports to Iran to restrict Tehran's nuclear ambitions. It also imposed sanctions on Qatar for its links to terrorist organizations and for its funding of extremist groups.

Furthermore, the GCC states' diplomatic efforts have increased as they seek to play an even larger role in the international arena. Some efforts are subliminal and some are very public such as Qatar hosting the World Cup. Their diversified economies have allowed them to leverage FDI and contribute to global economic security. Their locations have been used strategically and allowed them to exercise influence in multiple areas of the Middle East. Their increased prominence on the global trade economy can be demonstrated with deals like the free-trade agreement between GCC states and the European Union along with several bilateral investment treaties with countries such as Japan, India and the United States.

POLICY CHANGE AND ITS EFFECTS

Diversification is seen as a source of increased economic resilience as it reduces the risk of any single industry or sector declining suddenly which can create a negative financial shock wave through the economy. GCC states have all enacted plans to complete this economic diversification by sometime in the next 20 years. Saudi Arabia has the Saudi Vision 2030, putting a focus on construction project support programs which provides a range of incentives and finance options for companies undertaking projects in the country. The UAE has the Abu Dhabi Economic Vision which is seeking to reduce dependence on oil and create a diversified economy by investing in industries such as manufacturing, tourism, education and financial services. Qatar National Vision 2030 is set to promote economic diversification through industries such as education, finance and tourism. Bahrain has the Kingdom's Economic Vision 2030, which seeks to reduce Bahrain's reliance on oil production. Oman has an Oman 2040 Vision which cites four core pillars: economic prosperity, social development, environmental protection and regional integration promoting economic diversification, creating more jobs and businesses and improving education, healthcare and infrastructure. implementation of the value added tax helping to support GDP growth. Lastly, Kuwait has implemented a number of measures in its effort to diversify its economy including the Kuwait Vision 2035, seeking to economically diversify.

All of the countries in the GCC have set policies to change their economies and specifically to diversify away from oil dependence. I will explore the example of Saudi Arabia in detail as most of the policy is similar to Saudi Arabia's Vision 2030 plan.

Saudi Arabia in its Vision 2030 plan, plans to diversify its economy and reduce oil revenues. The plan aims to create new sources of non-oil income, encourage private sector investment and develop infrastructure related to tourism, telecommunications, healthcare, media and entertainment, education and industry. Within healthcare, they plan to invest in infrastructure and facilities, renewable energy sources such as wind and solar, technology startups, research and supporting establishment and growth of small and medium sized enterprises. They also have the Qafilah program which supports the application of innovative technologies to generate economic activity and create jobs.

The reason cited for this pivot by Saudi Arabian government officials is the fact that their oil dependence has had a significant impact on their economic stability over the past few decades. It is an ambitious plan aiming to make the country a more attractive destination for investors, businesses and tourists. World Bank data suggests the plan has had a significant impact on Saudi Arabia's economy. After the launch of the Saudi Arabia Vision 2030 in 2016, it has successfully encouraged foreign direct investment (FDI) which has been steadily increasing in quantity every year. The percentage increases in 2018 being 199.34% increase, in 2019 7.43% increase and in 2020 an 18.34% increase from the years prior. It has also helped boost entrepreneurship startups have established themselves in the sectors of technology, hospitality and renewable energy. In addition, they have also contributed to the development of public transport services such as the first mass transit project in Riyadh, and the first high-speed train between Makkah and Medina which makes it much easier for people to travel. This creates employment opportunities and makes the region more accessible to tourists. This can be directly seen to have had improvement from the number of visitors to Saudi Arabia reaching 17.7 million in 2019 up from 8.8 million in 2016 as cited by the Commission for Tourism and National Heritage. Some examples of the new technology startups include Freshouse, an online grocery delivery service; UrBox, an online marketplace; HoneyCuts, an online beauty service.

Domestically, Saudi Vision 2030 with these effects has had a positive impact on society. The plan to modernize the Saudi Arabian economy and reduce its dependence on oil revenues has initiated a number of reforms and initiatives to encourage private sector investment and job creation and has shown success in recent years. The investment in education should not be understated as it allows for the Saudi citizens to take higher paying jobs after a pursuit of higher education. This is beneficial to the country's politics long term as tightening the wealth gap would only make the political conversation within the country less based solely on single opinions of the oil-wealthy individuals. However this statistic has yet to be shown numerically in a drastic sense as educating a population and giving them more opportunity as a whole takes time to see in data. This has been proven in prior case studies such as Brazil's Bolsa Familia Program which studies have found that the program has increased school attendance, improved performance for students and reduced wealth inequality. According to the World Bank, since the program's 2003 launch it has contributed to 25% of Brazil's Reduction in inequality and 16% of the drop in extreme poverty. Extreme poverty has dropped from 7.7% in 2003 to 3.91% in 2018 and a low of 2.34% in 2014.

Broadening the scope once more, GCC states have attacked economic diversification through creation of investment opportunities. Some include infrastructure projects which are being funded through public-private partnerships and can also provide attractive opportunities in areas such as building transportation networks, renewable energy plants or water and sewage infrastructure.

To demonstrate growth of non-oil economies due to this, we can also look at growth correlated with FDI inflows. According to the United Nations Conference on Trade and Development, FDI inflows to the GCC grew from $37 billion in 2016 to $56 billion in 2019, an increase of 51%. This growth in FDI inflows demonstrates how economic diversification is paying off for the GCC states, helping to create more sustainable resilient economies

INDUSTRY DIVERSIFICATION AND JOB GROWTH

Job statistics from the World Bank say that economic diversification plans implemented by the GCC countries have had a positive impact on job growth in the region with a "significant increase" in employment over the past decade and more specifically, the unemployment rate was 7.8% across the six GCC countries in 2018, down from 8.6% just one year earlier in 2017. To add, the average job growth rate was 4.4% in 2018 in UAE and in 2019, they had a job growth rate of 5.6% in the non-oil sector with 207,000 jobs added.

Government spending from these plans have been the clear and obvious driver for these changes as the development of roads and airports for example, directly increase access to previously inaccessible markets and makes business more attractive prospects for investors. That in combination with the government's investments in education and training helps promote job growth by equipping workers with the skills required for specialized roles in newly diversified industries. Fiscal incentives such as tax breaks have encouraged both domestic and foreign direct investment in the region which has contributed to the job growth. 2.2 million new jobs have been added in the GCC states between 2016 and 2019 according to the IMF. This is an increase as between 2011 and 2015, taking into account an extra year of time, the total number of jobs created was only 1.7 million. 1.7 million of the 2.2 million jobs have been created through the private sector.

FUTURE TRENDS

When looking at future trends, we can assess through quantitative data measures the success of non-oil contribution to GDP and its projected feasibility in the future using Press Release Economic data, Bank data and Economic and Financial Review Data of all of the GCC countries. According to the Oxford Business Group, the average dependence of the six GCC states on oil as a percentage of their GDP has decreased from 42.9% in 2016 to 38.1% in 2019.

Some specific examples of this statistic can be shown through UAE and Saudi Arabia. For Saudi Arabia, a press release on Economic Data from the Saudi Press Agency showed that in the first year of the Saudi Vision 2030 implementation, non-oil contribution to GDP increased from 39.3% in 2016 to 40.2% in 2017.

To detail some of the correlations between the policy efforts and economic metrics, we can see that the Saudi Vision 2030 has directly contributed to a Construction Projects Support Program which provides a range of incentives and finance options for companies undertaking projects in the country.

According to the IMF, the UAE’s dependence on oil as a percent of GDP fell from 69.3% in 2016 to 50.6% in 2019, which is a drastic change in only 3 years. This can be directly attributed to the government's large scale investments in infrastructure projects such as expanding airports, ports, and transport links as well as the country encouraging FDI and other private sector initiatives. Although the Abu Dhabi Economic Vision 2030 being introduced back in 2008, these investments in initiatives take time to show direct effect on the economy and as the years continue to pass, the impact they have on the economic diversification for the UAE and other neighboring GCC states, will only accelerate as they create a feedback loop for growth with a more educated workforce, better infrastructure and more private sector growth.

Hvidt backs these ideas in his research paper, Economic Diversification in GCC Countries: Past and Future Trends further supporting this notion that future trends of these economically diversifying nations point to more success as some sectors are already showing success. He also notes that despite the strong contribution of finance, there is still more room for development in the sector and that Gulf states will need to focus on the value-added manufacturing and other service-oriented sectors as well for primary growth. This can be supported by the notion that when it comes to not only creating but sustaining economic change, it needs to be a long term effort. Many of these countries know this hence why many of the plans are titled the 2030, 2035, and 2040 Vision because the change will not and cannot occur quickly. However, having a long term mindset in this specific topic I believe will be prosperous for the region and help them achieve their goals in the future given their sustained efforts.

CONCLUSION

The economic diversification efforts of the GCC states will have a positive impact on their political power in the future. The development of renewable energy sources, the promotion of tourism, hospitality and other services, the development of new technologies and increased investment in education will help create new economic opportunities and reduce the reliance on oil and gas. This will help reduce the income inequality between the rich and poor within the countries in the region and create a more equitable economic system. Furthermore, the development of educational institutions will help create a skilled and educated workforce which will help the GCC states to remain competitive in the global economy and attract foreign direct investment. This will assist the GCC states to strengthen their political power in the region and improve their global standing.

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