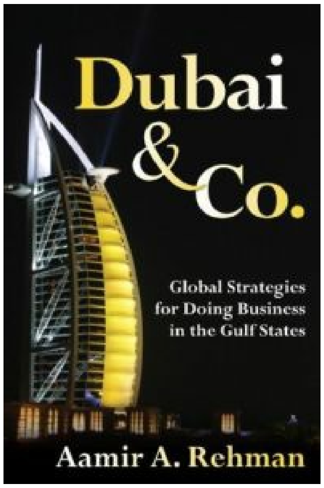

Book Dubai & Co.

Global Strategies for Doing Business in the Gulf States

Aamir A. Rehman
McGraw-Hill, 2007

Recommendation

Little heard-of, but increasingly important, the six nations known as the Gulf States are using their oil wealth to become global players in world finance. In turn, multinational corporations are recognizing that these nations should become integral parts of their expansion plans. All this makes author Aamir A. Rehman's work important to any business investigating this marketplace. He provides a cultural, economic, historical, political, demographic and geographic overview of this area, while spelling out the pros and cons of doing business there. Through this book repeats some key sections, Rehman keeps advancing his presentation, so any intrepid reader will have a strong foundation for future business plans. Think of this as a business guidebook to the region. If you are investigating an expansion in the Gulf States, *BooksInShort* would suggest that an investment in this book could generate large returns.

Take-Aways

- The Gulf Cooperation Council (GCC) nations are: the United Arab Emirates (U.A.E.), Saudi Arabia, Kuwait, Bahrain, Qatar and Oman.
- These states' combined 2006 budget surplus was $120 billion or $3,000 per person.
- GCC monarchies signed treaties with the British for political and military support.
- Multinational companies can enter the GCC market through a simple distribution arrangement, or a joint venture, or via direct ownership and management.
- Multinationals doing business in the GCC should understand how finance is conducted to comply with Islamic law.
- Cultural nuances distinguish Gulf States from each other.
- Saudi Arabia has two-thirds of the GCC's population and produces half of the region's economic output.
- The Abu Dhabi Investment Authority is a globally important institutional investor.
- The GCC's contribution to the global savings rate is larger than China's despite the fact that its population is only 3% that of China.
- Agreements that expressly put one of the parties at a disadvantage are not in compliance with Islamic law.

Summary

Oil Riches

The oil-rich countries of the Gulf Cooperation Council (GCC) – the United Arab Emirates (U.A.E.), Saudi Arabia, Kuwait, Bahrain, Qatar and Oman – may not be household names. But their global influence is shaping modern business and finance, in that these countries control 40% of the world's oil reserves. They are major investors in myriad companies around the world, from Caribou Coffee and Fairmont Hotels to Ferrari. The world's tallest building is planned for Dubai, as is the world's first "seven-star" hotel.

> "The economies of the GCC [Gulf Cooperation Council] countries represent the most attractive cluster of markets in the Middle East."

GCC countries had a *per capita* income in 2006 of almost $20,000, or triple that of China and five times that of India. The GCC's overall contribution to the global savings rate is larger than China's, though its population numbers only 3% of China's. Due mainly to oil revenues, GCC nations' gross domestic product increased 80% from 2001 to 2006.

"The GCC, however, does possess some significant risks and drawbacks. Chief among these risks is overdependence on oil."

Several factors link the nations of the GCC: oil wealth, small populations, relatively stable governments, desert locations and parallel histories. Politically, these nations have rulers whose lineages can be traced back to the days of tribal chieftains. In modern times, their monarchs signed exclusive treaties with the British in exchange for political and military support.

"Saudi Arabia is the core market of the GCC, and understanding it is critical to building a large-scale franchise in the Gulf."

GCC nations formed their own joint security pact in 1979 in response to the Iranian revolution. At that time, Iran established a radical Shiite theocracy that was too geographically close for the comfort of GCC nations, which are governed by Sunni monarchies. The same year, the Soviet Union's invasion of Afghanistan also showed the nonaligned GCC nations how important it was for them to have formal ties with each other to protect themselves against threats from the Soviets, and from Iran and Iraq as well.

"The Gulf...has been a magnet for Arab talent and represents the most attractive workplace in the Middle East region."

Using their vast oil wealth, GCC nations have launched an unprecedented infrastructure-building program. Their building projects involve roads, utilities, water facilities, public transportation and manufacturing. For example, an expansion of Dubai's airport is under way; more than 100 airlines are using it already. Dubai also intends to build the world's largest theme park, twice the size of Disneyland. Cooperative projects are helping the GCC nations advance as well. They have worked together to create a common customs protocol to facilitate shipping, and they aim to adopt a common currency by 2010.

The Importance of Women and Expatriates

Women also have a large role in GCC nations. Almost 60% of all first-year college students in GCC countries are women. Female professionals are moving into the workplace in larger numbers. To hire these women, provide jobs with duties they can balance with their family responsibilities. Public agencies are leading by example. In GCC nations, women play visible senior administrative roles. The U.A.E.'s Minister of the Economy is a woman, as is the head of Global Investment House, a Kuwaiti investment firm.

"A presence in the market often means more than just [having] a distributor or a small sales team."

While GCC countries are run primarily by Arabs, some 50% of the GCC states' population is made up of expatriates. Europeans, Australians and Americans have chosen to work in the region, especially in the U.A.E. This has helped make English the preferred language in most private-sector institutions. Many street signs are in both Arabic and English. Multinationals seeking a foothold in GCC nations should use the expatriate community to establish a local presence.

"Expect to see hot competition for market access in Iraq when it achieves some measure of stability."

The GCC nations are attractive to multinationals because of their bright growth prospects, attractive demographics and regulatory reforms. The drawback is that these nations are disproportionately dependent on oil revenues, and they are at risk of war (especially with Iran), extremism and terrorist threats.

Humble Origins

Most Gulf States began as isolated desert kingdoms, yet in the course of the past 10 years, the U.A.E. – especially its centerpiece, Dubai – has undergone a dramatic evolution. With a population comparable to that of New York City, the U.A.E. is comprised of seven states, which were incorporated in 1971. The U.A.E. began exporting oil in 1962 and by 2005, its oil exports totaled $50 billion. Today, the U.A.E.'s Abu Dhabi Investment Authority is the world's second largest institutional investor, as measured by assets under management, behind only the Bank of Japan.

"For years, global businesses and their executives have viewed prosperity in the GCC countries as a threat."

Abu Dhabi, the U.A.E. is remarkable because it has followed a deliberate diversification strategy; its revenues are not directly linked to oil. Instead, it developed through trade, commerce, real estate and the hospitality industry. To entice foreign investment, the U.A.E. has expanded infrastructure investment, endorsed liberal lifestyle policies (especially in Dubai), encouraged foreign ownership, and streamlined its bureaucracy to make it more business-friendly.

"Of all the Western nations, the U.K. has the deepest ties with the GCC and the U.A.E."

Saudi Arabia is the GCC's core market, so multinational corporations must understand its business dynamics. Saudi Arabia has two-thirds of the GCC's population, half of the region's total GDP and the world's largest oil reserves. In 1988, the Saudis took full control of the oil company Aramco. This was a key development in their nation's history.

"China's voracious thirst for petroleum makes it a natural partner for the GCC states, and its need for investments complements the Gulf's excess capital."

Saudi society is based on three key groups: the monarchy, the private business sector and the religious establishment. The Saudis consider the *Koran,* the basis of Islamic law, as their constitution. Other economically crucial GCC countries include Qatar, with its large domestic investment in water plants, gas pipelines, education and health care; and Bahrain, an island state that is known as a financial services center.

Getting Down to Business

Multinationals can enter the GCC market three different ways: through a simple distribution arrangement, in a joint venture, or via direct ownership and management. The most common method is a distribution arrangement, followed by joint ventures. Most multinationals entered this market via various "shallow-engagement strategies," such as distributorships, in order to minimize their financial risks while maximizing their income from revenue sharing, and fees for training and franchising.

"Without a doubt, ADIA [the Abu Dhabi Investment Authority] is one of the most important investors in the world."

The Al-Hokair group used this model in Saudi Arabia, where it distributes 50 international luxury brands to the domestic retail market. Carrefour, the world's second-largest department store operator (after Wal-Mart) opened four noncompany-owned stores in GCC states through joint franchise arrangements with local partners. Other companies that have entered the GCC market on a large scale include furniture dealer Ikea and computer maker Dell. In Saudi Arabia, local banks have formed joint ventures with Citigroup, Credit Agricole, HSBC and ABN Amro.

"Racism in the GCC countries is a real issue, especially for nonwhite expatriates."

While GCC countries have fostered joint ventures in the past, they are changing their regulatory structure to facilitate direct market entry by creating "free zones." These will be areas where international firms can completely own their businesses and repatriate all their profits, often on a tax-free basis, while receiving government support to comply with regulatory requirements.

"Corruption in the Gulf exists to a far smaller degree than in other emerging markets."

Once a multinational company decides to enter the GCC market, it must decide how to adapt its marketing to make it specific to the region. Most global firms customize their messages by translating their labels into Arabic. McDonald's and HSBC, for example, put Arabic translations in their ads. Beverage giants PepsiCo and Coca-Cola use locally recognized talent to promote their products. Choose advertising images with careful consideration of local tastes. An ad that is appropriate for a more liberal GCC state, such as the U.A.E., may be unacceptable in Saudi Arabia.

"Compromising a global reputation for a regional business is simply not an option, and standards must always be upheld."

Staffing a GCC office requires flexibility. Multinationals seeking experienced white-collar talent often will turn to the expatriate community. However, competition for expatriate talent is intense; recruiters are expected to offer competitive packages to attract and retain talent. The challenge is to keep the expatriate workforce professionally engaged while it clearly has guest status in the nation. Another talent-building technique is hiring local GCC professionals who are in the early stages of their careers and training them over time to become skilled, experienced employees.

Gulf Budget Surpluses

The Gulf States posted a combined budget surplus of $120 billion in 2006, or around $3,000 per person. The GCC nations are investing more of this money in public and private companies. Gulf States should continue to enjoy large budget surpluses thanks to their government-owned oil resources. An increase in the influence of Islamic financial institutions has accompanied this investment boom.

Expanded use of so-called "*Sharia*-compliant" investments is an important driver to GCC development. Such investments comply with Islamic law, particularly the way its financial code rules against making certain kinds of profits. In practice, the *Sharia* framework results in prohibitions against short sales of stock and against insurance contracts that put one party at greater risk than another. Many Western companies that do business in the Gulf States have become experienced participants in investments that are structured to conform to *Sharia* law.

Sharia business practices have produced a number of investments that are uniquely Islamic. One is *Murabaha*, a sale which covers the costs of goods plus a small profit linked to the asset's risk characteristics. Other common instruments are *Ijara*, or leases, and *Mudaraba*, that is, investment partnerships in which one partner is compensated for "sweat equity." Many of these principles are compatible with Western notions of ethical investment and corporate social responsibility. HSBC, Citibank and some 300 other major institutions offer investments based on *Sharia* law.

While Islamic law bars Muslim consumers from owning credit cards, larger-scale public borrowing exists in the Gulf States. Some countries have issued bond-like securities called *Sukuks* that comply with Islamic law. The City of London and the Bank of Japan are among the institutional investors making concerted efforts to trade in *Sukuks*.

Infrastructure and Protocols

GCC nations have emphasized constructing transportation, utilities and support systems to handle travel and trade. Dubai's sprawling Jebel Ali seaport has the world's largest man-made harbor. A major revamp is expected to make Dubai's airport larger than Chicago's O'Hare and London's Heathrow combined. These public works also serve GCC monarchies' political need to show how they are using the nation's oil wealth to benefit the population.

As a result of this major infrastructure development process, many multinationals, including Kraft, Nokia, Palmolive, Black and Decker, Hyundai, Adidas and Shell, are building new plants to take advantage of the GCC's improved logistical capabilities.

Multinationals doing business in the Gulf also must accommodate weekend schedules that are different from those in the West. Employees in Gulf States do not work on Fridays. For some, the weekend is Friday and Saturday, and for others, it is Thursday and Friday. Employees in Oman are off on Thursdays, Fridays and Sundays.

While the Gulf States are becoming more liberal, each has idiosyncratic regulatory protocols. To navigate the regulators, multinational corporate managers should work with a local public relations officer to ensure compliance. According to the World Bank, the time required to open a business is 39 days in Saudi Arabia and 34 days in Oman, compared with 18 days in the United Kindom and five days in the United States.

Once a corporation establishes a presence in the GCC, the team in charge of the branch must increase awareness of the region at the corporation's home office. Management can change reporting lines and resource allocations to improve home-office oversight of GCC operations.

About the Author

Aamir A. Rehman is an expert in global corporate strategy. He has worked as an advisor in the development of strategies for multinational companies based in the United States, Europe, the U.A.E., Saudi Arabia and the broader Middle East. A graduate of the Harvard Business School, he formerly served as global head of strategy for a business unit of the leading bank HSBC, and worked for the Boston Consulting Group.