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The Limits of Rentierism and the GCCs' Move toward "Greater"  
Liberalism

By

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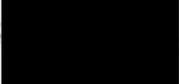
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*Dedicated to  
Noura, Jamal, and Mostapha*

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# The Limits of Rentierism and the GCCs' Move toward “Greater” Liberalism

Meryam Jamal Ramadan

## ABSTRACT

With radical transformations of the political economies of the Gulf in the past decade, conventional Rentier State Theory (RTS) fails to adequately explain many of the modern aspects of the GCC's politics. Through a theoretical and empirical assessment of the theory, this thesis will investigate the theory's shortcomings when applied to the dynamic economies of the Gulf countries. This will be conducted by undertaking an in-depth analysis of GCC macroeconomic performance with a focus on diversified economic challenges and its contemporary complications. Subsequently, the effect of natural gas revenues, states strategies, and the drift of foreign labor in relation to heightened liberalism in the gulf market will be delineated. Therefore, the paper will aim at deducing the theoretical modifications necessary in rendering RTS as pragmatically relatable to the present economics of the Gulf countries.

*Keywords:* Rentierism, Rentier States Theory, GCC Countries, Economic Diversification.

# Table of Contents

<b>List of Tables:</b> .....	<b>ix</b>
<b>List of Figures:</b> .....	<b>x</b>
<b>Chapter One</b> .....	<b>1</b>
<b>Introduction</b> .....	<b>1</b>
1.1 <i>Thesis Questions:</i> .....	5
1.2 <i>Overview of Chapters</i> .....	6
<b>Chapter Two</b> .....	<b>9</b>
<b>Literature Review: Theorizing Rentierism</b> .....	<b>9</b>
2.1 <i>Theory of rentier states</i> .....	9
2.2 <i>Late Rentierism</i> .....	17
<b>Chapter Three</b> .....	<b>24</b>
<b>GCC Countries as “Rentier States”</b> .....	<b>24</b>
<i>Rentierism in GCC Countries</i> .....	24
3.1 <i>The GCC labor market</i> .....	29
3.2    The Challenges of the GCC Labor Market: Localization and Nationalization.....	33
3.3 <i>The GCC Economies: Stepping up to Future Challenges</i> .....	38
3.3.1    Saudi Arabia.....	38
3.3.2    Bahrain .....	41
3.3.3    Qatar .....	44
3.3.4    Kuwait .....	47
3.3.5    United Arab Emirates .....	50
3.3.6    Oman .....	55
<b>Chapter Four</b> .....	<b>61</b>
<b>Conclusion</b> .....	<b>61</b>
4.1 <i>Contemporary Transformations of the Rentier Regime in the Gulf</i> .....	64
<b>Bibliography:</b> .....	<b>70</b>
<b>Appendix A: Oil Exporters: Oil and Non-Oil Real GDP Growth</b> .....	<b>76</b>

## List of Tables

Table 1: GCC Countries: Selected Economic Indicators, 2002.....	26
Table 2: Gulf Countries GDP per Capita.....	46
Table 3: Kuwait government revenue for fiscal years 2003/4 and 2007/8 (USD b).....	48
Table 4: Oman's Proven Oil Reserve.....	56
Table 5: Key Dimensions of the Vision for Oman's Economy 2020 Strategy.....	58

## List of Figures

Figure 1: The Rentier State- Society Relationship .....	12
Figure 2: GCC Countries: Oil Dependency ( <i>Average in 1998–2002; percent</i> ). .....	28
Figure 3: Trends in UAE government revenue.....	54

# Chapter One

## Introduction

One of the most popular phenomena in the twenty first century, occupying the day-to-day concern of the international monetary systems and stock markets, is natural oil and gas. Within a dynamic world order, the value and scarcity of such natural resources give its owners the capacity to stand out economically as the wealthiest states in the international arena. This reality in turn gives those states weight in the dynamics occurring on the international level economically and politically. Globalization and technological advancement are all factors introducing new mechanisms of foreign policies and therefore, states with more contribution in these fields will automatically occupy their places as major international players. In the last century, fossil fuels, oil, coal and natural gas were the world's main energy supply instruments, a reality that will not change in the near future<sup>1</sup>.

For most oil-dependent countries, the discovery of oil coexisted with the making of the modern states. Consequently, these countries continued to grow simultaneously alongside oil revenue growth. Thriving societies pose as threats to the influence and control of the ruling families, but in the gulf, these families operate as powers to protect their wealthy status, where oil serves to strengthen privileges and monopolies and astonishingly hold their growing society together. The result, as Luciani argues, was the creation of an allocation state and the politics of direct distribution.

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<sup>1</sup>Scientific and Technical Committee "Euratom". (2003).The Energy Challenge of the 21st century: the role of nuclear energy.

Iranian economist Hossein Mahdavy introduced the rentier state concept in the late 1960's. A general economic model of the emerging Gulf States was later elaborated by Luciani, based on the concept of rent. These countries are known to trade and base their wealth merely on their natural resources, and have structured their internal systems in such a way that the government is the sole provider for the country. This, reality in turn, gives the government the authority to control the social, political and economic sectors within the state. The government plays the role of the manipulator where it controls and uses the external rents it receives to buy the allegiance of its population and to secure its longevity<sup>2</sup>. Such behavior categorizes a state as rentier. Rentier state theory (RTS) indicates that such economies may have little reason to democratize, reform, or otherwise evolve. Rent is thus regarded as a kind of curse, where the states are in some ways trapped by God-given wealth, have no incentive to boost productivity and are (perhaps not explicitly) politically corrupted.

Over the last forty years, economic indicators of countries rich in natural resources in the Middle East and the North African region (MENA) showed that those states have actually maintained a persistently high income per capita, while marking low scales of economic growth domestically<sup>3</sup>. Beblawi asserts that the “oil phenomenon has cut across the whole of the Arab world, oil rich and oil poor”<sup>4</sup>, he continues “be it oil revenues or

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<sup>2</sup> Beblawi, H., &Giacomo, L. (1987). *The Rentier State: Nation, State, and Integration in the Arab World*. London: Croom Helm

<sup>3</sup>International Monetary Fund.(2012). *Natural Resources, Volatility, and Inclusive Growth: Perspective from the Middle East and North Africa*.

<sup>4</sup> Beblawi, H., &Giacomo, L. (1987). *The Rentier State: Nation, State, and Integration in the Arab World*. London: Croom Helm

workers' remittances, or strategic location, or *el-kafil*, or Soukh el Manakh, they are all consequences of the oil phenomenon, and have been accompanied by a serious blow to ethics of work. Income is no longer a reward of serious and hard work, it is very often related to special circumstances, chance, location, etc. In a word we are living in a rentier universe which has affected both the state and citizen.”<sup>5</sup>

Thomas Friedman states that “Petropolitics” is strictly correlated to authoritarianism. He argues that rentier states become more vulnerable when the oil prices decrease and more indifferent when the prices increase. But the resilience of the Gulf states and the evidence since oil prices started declining in August 2014 have not backed up that thesis.

Rent has a bad reputation (Ozyavuz& Schmidt, 2015), despite the four decades of the concept's circulation and radical economic transformations in the Arab Gulf States which challenge conventional rentier state theory. Falling oil prices are very likely to add further trouble in the future, and have already cause governments in authoritarian petro-states to question their ability to buy off citizens with subsidies, low taxes and other economic benefits. However, GCC countries (Saudi Arabia, UAE, Qatar, Kuwait, Bahrain, and Oman) are still pursuing some serious reforms by translating economic diversification plans into action and by rationalizing consumption habits in favor of sustainable growth. The discovery of oil and gas, as well as their development in the GCC countries, has resulted in rapid economic prosperity and in the overall improvement of the quality of life on both the micro and macro scale of the country.

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<sup>5</sup> Beblawi, H., &Giacomo, L. (1987). *The Rentier State: Nation, State, and Integration in the Arab World*. London: Croom Helm

The increasing complexity of the economic strategies of political and social relationships between rulers and citizens in the Gulf States reflects a noticeably more nuanced and dynamic picture than that of preceding scenarios. Obviously, the efforts put forth to surpass a sustainable rentier growth model reflect an essential objective for the region within the context of advanced globalization<sup>6</sup>. The GCC countries have definitely learnt from previous experiences and are assertively pushing for a more diversified economy and rapid growth. Certain institutions in the Gulf States have construction projects, energy subsidies and public sector wages, and have instead introduced new taxes and privatizations, and created free trade and investment zones where practices are actually taking place. Furthermore, Gulf rulers' are aware of their critical situation, and this is compelling some states towards implementing more aggressive regional policies, as portrayed by the Saudi war in Yemen. Nevertheless, many challenges are still restraining each nation's development processes. Thus, for the stability of the Middle East area to be attained, a change of governance and improvements in the governing systems of these countries is crucial.

The rentier state theory is essential for understanding the Gulf regimes, their resilience, their policies, and the nature of their relationship with society. However, as Gray claims, there is more to gulf politics than rents. The conventional RTS of early decades is no longer adequately detailed or adaptable enough to sufficiently explain the radical economic transformations in the Arab Gulf States.

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<sup>6</sup>Ozyavuz, A., &schmid D. (2015).Persistence and Evolutions of the Rentier State Model in Gulf Countries, Ifri.

## 1.1 Thesis Questions

While this thesis focuses mostly on the diversification strategies adopted by the Gulf Cooperation Council countries to counter the instability in global oil prices, it also embarks on evaluating the theoretical bases of rentierism. The below research questions are addressed in this thesis and are discussed in detail in the chapters to come. The questions aim at understanding the emergence of rentierism, the evolution of the theory, the shift in the political economies of the GCC states in the last two decades, and the contemporary transformations in the rentier system in the gulf in the light of the recent oil crisis. The problem is rooted in the fact that classical rentierism theory is no longer sufficient to explain the politics of the GCC States. Therefore, it's important to understand what rentierism is, how it has adapted to explain the dramatic changes in the political economies of rentier states in a globalized era, and what the shortcomings are of different rentierism approaches.

It is also important to understand the past record and future development trajectories of economic diversification efforts in the six Gulf cooperation council countries. The third chapter will address what steps have been taken by the Gulf States in recent years to diversify their economies, and what the remaining challenges are for the attainment of this diversification. In addition, it is vital to mention the contemporary transformations of the rentier regime in the Gulf in order to be able to make a conclusion about the capability of rentier state theory to explain the politics and state-society relations in GCC countries nowadays.

The last chapter will address how Gulf States no longer ideally fit the defining criteria of what qualifies as a classical rentier state, yet in spite of the changing dynamics on the

international system, Rentier State Theory still has utility in explaining the political dynamics of the six gulf countries.

## **1.2 Overview of Chapters**

The thesis is divided into four chapters. Following this introductory chapter, the second chapter will introduce Rentierism from its early definitions up until its modern applicability and will examine how different theorists have approached the study of rentier states.

The first contribution to the knowledge of rentier states theory was introduced by Mahdavy, who argued that rentier states are those which benefit from external rents by exploiting their natural resources to keep their economy prosperous. He considered that the Middle East region, specifically the Arabian Peninsula, reached an enormous amount of economic prosperity historically because they relied heavily on exporting their natural resources and benefitting from external rents<sup>7</sup>. Beblawi and Luciani refined the concept of the rentier state and argued that the availability of sufficient resources is the main prerequisite to ensure stability and political growth in a rentier state because it's the only source which prolongs its life-span. Luciani argues that rentier states are allocation rather than productive states because the governments support the population instead of having

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<sup>7</sup>Mahdavy, H. (1970). "The Pattern and Problems of Economic Development in Rentier States: the Case of Iran," in *Studies in the Economic History of the Middle East*, ed M.A. Cook. Oxford: Oxford University Press. p.428

citizens work and pay taxes. Eighteen out of the twenty two MENA states rely on revenues extracted from external rents for over a third of their GDP.<sup>8</sup>

The chapter discusses a variety of research on the theory of rentier states examining the relation between rentierism and the lack of democracy such as those brought forward by the scientist Michael Ross. In his research, he claimed that these states develop two reactions toward modernization: repression and immunity. Ensuring democratic rule within a state certainly affects other fields internally. For example, human rights, freedom of expression, and fair representation are some values among many that come with a democratic system. Such arguments are worth being discussed in this section in order to examine the effect of authoritarian practices taken by the Gulf governments on economic reforms and democratic transitions. In addition to the above, the second chapter features the arguments of scholars such as Gwenn Okruhlik, Thomas Richter and Christian Steiner and Thomas Friedman; all of whom have addressed later stages of rentierism.

The third chapter of the paper closely examines the practice of rentierism in GCC member states which have been resilient to the political and economic changes that took place during the civil uprisings in recent years. The chapter illustrates, through charts and figures, the level of oil dependency in GCC member states. The main emphasis in this section is on the recent positive initiatives taken by the Gulf States towards the construction of a non-oil economy. With regards to the classical rentier state theory, citizens of oil-dependent states prefer to strive for their wealth, prosperity and economic stability rather than engage in regime changing movements. However, the interplay between insurgency, terrorism, and civil war in the modern Middle East shows an obvious

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<sup>8</sup>Craig, J., Meyer, K., Costello M., & Aly, H. (2008). "International Rentierism in the Middle East and North Africa, Ohio State University.

contradiction with the main characteristics of the rentier state. This chapter will point out the main challenges rentier states face within a liberal economic and democratic political framework.

The last chapter in the paper marks the conclusion of the thesis and spells out its findings. The chapter will focus on the new politics of Gulf Arab States and the contemporary transformations of the rentier regime in light of decline in oil prices. The findings provide additional contributions that call for revising RTS toward greater liberal pragmatism.

# Chapter Two

## Literature Review: Theorizing Rentierism

It has become customary to view the MENA region through the prism of Rentier State Theory. Rentier State Theory is “a political economy theory that seeks to explain state-society relations in states that generate a large proportion of their income from rents, or externally-derived, unproductively-earned payments” (Gray, 2011). Mahdavy introduced the concept of rentierism in 1970; it was later elaborated by Luciani and Beblawi, and has since undergone some adjustments. This chapter will analyze the origin of the rentier model in the gulf and will subsequently examine how different scholars have approached the study of rentier states.

### 2.1 Theory of rentier states

The classic rentier state theory was first introduced and characterized by the economist Hossein Mahdavy who initiated the theory in 1970 and laid out the foundation of this concept after writing about pre-revolutionary Iran. His work is worth being mentioned as the first recognized scholarly research on this topic, adding significant value to the field of political science and international relations. Mahdavy characterized the rentier state as one which exploits its natural resources to export them to external clients; the state benefits from the revenues considered to be sufficient in keeping the state’s economy prosperous without the need to refer to other means for economic profit and development. He points out that the Middle East region -- specifically the Arabian Peninsula-- reached a significant

economic prosperity during the period extending from 1951 – 1956<sup>9</sup>. This was due to the influx of large amounts of revenue into the treasury of these states brought on by the trade of their natural resources<sup>10</sup>.

The concept of rentier states was further elaborated by Giacomo Luciani, one of rentierism's most prominent thinkers, who defined the rentier state by the following main characteristics as a state: its rent situations from abroad are predominate; its economy relies substantially on external rent and therefore does not require a strong domestic productive sector; only a small proportion of its working population is actually involved in the generation of the rent; and the state's government is the principal recipient of the external rent while the majority is only involved in the distribution or utilization of it<sup>11</sup>.

Luciani describes rentier states as "allocation states". In this regard he means that a state does not feel the necessity to reinvest in its domestic economy or to initiate economic plans to boost its economic growth which in turn becomes a "production state". Luciani claims that the availability of sufficient resources is the most important pre-condition for the stability of regime and state<sup>12</sup>. A production state is one where people derive their income from means other than the state such as revenues from a productive sector which generates wealth and imposes taxes to ensure economic growth which, as a result, affects the state's political sphere. Thus, political influence will be achieved due to having social disparity because of the competitive market, and consequently, different demands within

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<sup>9</sup> The Patterns and Problems of Economic Development in Rentier States: the Case of Iran H. Mahdavy

<sup>10</sup>Hosseini, M. (1970). "The Pattern and Problems of Economic Development in Rentier States: the Case of Iran," in Studies in the Economic History of the Middle East, ed M.A. Cook. Oxford: Oxford University Press. p.428

<sup>11</sup>Dunning, Thad. *Natural Resources and Democracy in Latin America*. Department of Political Science Yale University.

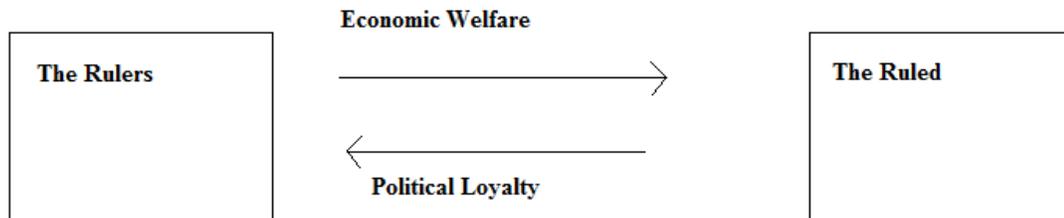
<sup>12</sup>Luciani, G. (1990). "Allocation vs. Production States: A Theoretical Framework", in G. Luciani (ed.) *The Arab State*, Kent: Routledge,

each social class will form different interest groups each lobbying for their demands and attempting to have a political influence on the decision making level. Those demands and attempts do not exist in rentier states.

Rentier states provide high welfare services to their people (i.e. healthcare, education, etc.). However, they do not ensure an ongoing sustainable economy which is based on economic growth and investments. Instead, they shift the economy into an expenditure mode where the state is the main source of income for the country. Such a system indicates that the broader section of the population of a rentier state is not benefiting equally with those who have direct involvement in rentierism. Hence, international rents reduce the state's need to collect taxes from the people. This bargain is derived from the policy applied by a rentier state where the latter ensures the well-being of its broad population, and the people in turn do not rebel or try to change the status quo in their country, especially in the political arena. Moreover, a prerequisite is required to undertake tax collection from a country's population, chiefly that of a Gulf's. Those states need the consent of the people and their willingness to pay in order for them to have the ability to affect economic policies; however, the overall mechanism required for that is democracy. Therefore, the debate in production states is "no taxation without representation" because the people will expect services for paying taxes unlike allocation states where the people are not expecting anything in return from their government.

Moore (2010) and Foley (2010) disagree with the notion that states become less accountable when they do not need to collect taxes from their citizens. They argue that the domestic conditions do not impose how the government will behave, but they do affect how the state is formed initially, whether it is a strong democracy or an authoritarian

regime. However, the overall consensus among scholars remains that oil diminishes democracy and allows a rentier state to act freely with minimal accountability. These states amend constitutions, reverse or introduce policies according to their interests, choose the country's foreign policy, and change their political loyalty and alliances as they deem appropriate for their benefits, and can do so with a high degree of flexibility.



**Figure 1: The Rentier State- Society Relationship**

This argument coincides with Luciani's theory. He argues that the relationship between rentier states and their people involves money flowing from the government to the people in the form of entitlements instead of the people to the government in the form of taxes. He reaches the conclusion that rentier regimes are financially independent of society<sup>13</sup> and are not accountable for their people; they enjoy a high degree of autonomy with the absence of appropriate frameworks to monitor the money inflows to the state's treasury. This

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<sup>13</sup>Elbadawi, I., &Makdisi, S..(2011). *“Democracy in the Arab World, Explaining the Deficit.”*Routledge.

promoted reality asserts that a population's political loyalty to the ruling monarchy can be easily manipulated and even bought. For example, the rentier states in the Arabian Peninsula which possess a high level of wealth due to their external rents allocate welfare services to their citizens in the form of an "implicit social contract", replacing their citizens' political rights for the services they are receiving from their governments. Even though this is a considerably informal contract, it can only be sustained by depending on enough resources to be allocated for both the state and the whole of society. This status quo might be threatened when a rentier state fails to abide by the 'implicit social contract' and consequently fails to sustain its autonomy due to increases in oppositional voices.<sup>14</sup>

As Beblawi(1987) argues, the rentier mentality is not based on production in turn for reward or other incentives. Rentier economy functions in a different way; reward in a rentier economy is related to connection with the ruling elite and with close ties to the government. This reality pushes the population to be totally reliant on a welfare system where the government is the sole allocator, and the production sector in the country is put in the hands of foreign labor. As a result, the government achieves legitimacy with time and sustains the status quo for a long time<sup>15</sup>.

Eighteen out of twenty two Middle Eastern and North African states, for over a third of their GDP, depend on revenues from rents extracted from international transactions<sup>16</sup>.

Although the states of the Arabian Peninsula reserved their places in the international capitalist market when their economies were assessed, they do not actually rely on a productive sector. Oil is not a sector which is produced; it is a natural resource which can

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<sup>14</sup>Schwarz, R. "State Formation Processes in Rentier States: The Middle Eastern Case." Graduate Institute of International Studies, Geneva. Web

<sup>15</sup>Beblawi, H. (1987). "The Rentier State in the Arab World". *Arab Studies Quarterly* 9.4 : 383–398. Web

<sup>16</sup>Craig, J., Meyer, K., Costello M., & Aly, H. (2008). "International Rentiersim in the Middle East and North Africa, *Ohio State University*.

be extracted and exported. For this reason, the Gulf States lack skilled man power when it comes to productive sector investment. Their citizens are merely reliant on the wealth generating sector without the skills to excel or develop other sectors. Therefore, Gulf States have a high number of expatriates working in their countries. Although these expatriates are rewarded according to the services they offer, they do not enjoy similar privileges like those of the Gulf's citizens. Once their presence in the labor market becomes a threat, they can easily be terminated.

The rentier state offers a minimal amount of its wealth to the society and gives itself the freedom to do as it wishes with the remaining amount. The rentier state convinces its people that they have shares in the state's wealth and doesn't concern itself with matters such as its legitimacy. Hence, by collecting revenues from oil rents, implementing welfare services domestically, purchasing public loyalty, they in turn achieving political and economic stability, and the continuity of the rentier state's is attained.

Luciani (1987) argues that rentierism is not only limited to oil exporting states but also to indirect forms of external rent revenues. These revenues could be made, for example, in bilateral or multilateral foreign aid payments, remittances, tourism, military and foreign development assistance, and access to water courses such as the Suez Canal.

Even advanced literature, which sought to be more precise than preceding research, further validated the correlation between rentierism and the absence of democracy<sup>17</sup>. Ross (2001) argues in "Does Oil Hinder Democracy?" that rentier states have little will to shift from non-rent dependent states because they do not have interest in supporting domestic

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<sup>17</sup>Herb, M. (2005). No Representation without Taxation? Rents, Development, and Democracy. JSTOR, Web

investments or to create taxation derived bargains with their people. He outlined three effects of rent that sustained or prolonged authoritarian and non-democratic governments in oil states. The no taxation policy commoditized the population and bought the state's "legitimacy" by bribing people for their allegiance to the state; a claim that he referred to as the "rentier effect". He also mentions the "repression effect" where the state tries to hinder and repress democratization attempts, and finally the "modernization effect" where rentier states develop immunity to democratic strategies and enhance socio-economic stagnation and underdevelopment<sup>18</sup>.

However, the last stage of research on rentierism acknowledges that rentier states are urged to consider long term plans to ensure a survival strategy in a global capitalist market. Beck and Schlumberger (2000), among others, argue that the type of rentiersim is the main determinant of the level of economic liberalization of a state. Luciani affirms this theory and adds that the economic and fiscal crises of a state are closely linked to the initiation of political liberalization. States which have significant revenues from oil rents impose a strong limiting factor on the democratization processes in these countries<sup>19</sup>.

An empirical cross national study using data from 113 states between 1971 and 1997 confirmed that oil exports are strongly associated with authoritarian rule.<sup>20</sup>Rentier states stand as a vital impediment to democratic rule, and ensuring a democratic rule within a state inevitably affects other internal fields. For example, human rights, freedom of

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<sup>18</sup>Ross, M. (2010) Replication Data for: Oil and Gas Production and Value, 1932-2009. Department of Political Science, UCLA

<sup>19</sup>Political Liberalization and Democratization in the Arab World : Theoretical Considerations

<sup>20</sup>Scwarz, R. (2004). "State Formation Processes in Rentier States: The Middle Eastern Case." Paper to Be Presented at the Fifth Pan-European Conference on International Relations, ECPR Standing Group on International Relation, Section 34 "International Relations Meet Area Studies", The Hague.

expression, and fair representation among many others are values enshrined within a democratic system. Subsequently, states which neglect the needs of their people to ensure their own sustainability will inescapably risk breaches in these fields.

The democratic state formation process in the Middle East has been hindered for several reasons, the most important of which is war. Hartmut Elsenhan and William Reno introduce the terms “state class” and “shadow state” which are linked to a self-ruling elite having control of a country’s external rents<sup>21</sup>. The level of rentierism in a state can be measured starting from how the state is actually generating wealth, how the revenues are being received from the external rents, the mechanisms of adding wealth to the state’s treasury, and how wealth is being distributed domestically. Certainly, several breaches can be recorded throughout this process due to the autonomy of a rentier state and due to the lack of proper monitoring mechanisms. Although the states of the Arabian Peninsula are considered to be rentier to a very large degree, they have still been able to ensure their durability because of their “gift from nature” as Beblawi describes it. These states do not invest in various productive sectors. Instead, their economy relies on one sector generating and exporting natural resources. This fact poses a serious threat to the future of these states due to their authoritarian rule, and due to the concentration on only one economic sector, and the lack of productivity in their societies. Most of the Arab states have failed to ensure a fair representation of their people which proves that the government formation in the Middle East is different from the government formation in Western countries.

However, Herb (1999) argues in “All in the Family: Absolutism, Revolution, and Democracy in the Middle Eastern Monarchies” that many problems are arising within

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<sup>21</sup>Laws, Glenda. *Annals of the Association of American Geographers* 82.4 (1992): 740–742. Web

rentier states, such as reducing returns in citizen gratitude for state benefits, popular discontent with the system caused by unfair rent distribution, and stimulation of public debates about the fact that governments shower their citizens with money to keep them silent. Notably, the traditional definition of rentierism is no longer sufficient for analyzing the dimensions of this dynamic theory. According to Gray (2011), a new phase of RTS, “Late Rentierism”, should be applied to rich Arab Gulf States, as classic RST is not modified enough to explain the significant changes in the political economies of the Gulf.

## **2.2 Late Rentierism**

RST has been successfully adapted by Gray’s “Late rentierism” theory which still embraces the same basic features of Beblawi and Luciani’s original model. Traditional RST asserts that Rentier States might be categorized as wealthy states that can, nevertheless, have weak structure. The lack of legitimacy of the government and the ruling elite, the limited productive sector, and the oppression of civil institutions and opposition movements ban the state from developing on the global level and hinder its capacity to cope with globalization. Therefore, as long as the loyalty of the citizens of a rentier state is purchased, such a state will have no incentive to democratization. Rotberg mentions in *State Failure and State Weakness in a Time of Terror*, that nation-states fail because they fall short of delivering positive political goods to their inhabitants, and thus lose legitimacy in the eyes of their citizens.<sup>22</sup>

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<sup>22</sup>Rotberg, Robert I. *State Failure and State Weakness in a Time of Terror*, Cambridge, Mass.: World Peace Foundation, 2003. Print

However, Gray's research on the late-stage of rentierism marks a different approach in the perspective of the state and its outlook both on rents and its own sustainability. The new rentier state is closely linked to what is termed as "state maturity" because rentier states have learned from the experiences of the past, especially the events of the 1970s and 80s, when oil prices were much lower than both earlier and later years. Due to globalization and increased global capitalist economy, rentier states now recognize that states with dynamic entrepreneurial activities are the ones that ensure longevity<sup>23</sup>.

Much scholarly research has emerged to further explain Rentier State Theory. For example, Okruhlik in his article "Comparative Politics" points out that wealth generated from oil rents serves as a catalyst for opposition to the state which stands in opposition to Luciani's argument which suggests that these states rely on its wealth to manipulate its people. Okruhlik elaborates her argument by saying that since the wealth is being distributed unequally, the chances of a revolution against the regime rises. It is once the rents are distributed equally to the "owners" of the oil that people will consent to the ruling regime<sup>24</sup>. However, the political stability of the Gulf States proves this theory to be inconsistent with the facts because the regimes in the Gulf have been able to exercise a large degree of authoritarianism through their rentier attitudes.

Richter & Steiner (2008) establish six main sources of international rents<sup>25</sup>:

- The rents derived from the export of natural resources such as oil and gas

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<sup>23</sup> Gray, M. (2011). "A Theory of "Late Rentiersim" in the Arab States of the Gulf." Center of Regional and International Studies, George Town University. Web.

<sup>24</sup>Okruhlik, G. (1999). "Rentier Wealth, Unruly Law, and the Rise of Opposition: The Political Economy of Oil States, in Comparative Politics. p. 295-315. Web.

<sup>25</sup>Craig, J., Meyer, K., Costello M., & Aly, H. (2008). "International Rentiersim in the Middle East and North Africa, Ohio State University.

- The rents derived from location facilities such as transit fees for providing transportation routes such as the Suez Canal
- The rents derived from strategic loans in forms of aid and assistance
- The rents derived from donations to a government, also known as political rents
- The rents derived from worker remittances
- The rents derived from international tourism revenues

Unlike Luciani, Jill Crystal, another rentier state theorist, in her article *Oil and Politics in the Gulf: Rulers and Merchants in Kuwait and Qatar* (1990), questions the stability of rentier states that redistribute wealth among their citizens, and claims that this distribution might be a potential cause of their instability, regardless the price of oil and revenues they are generating. She claims that central governments may divide their power centers and allocate representatives of the government for each center, such as an Emir or a governor. Accordingly, those central rulers can develop social and political relationships with the population in certain areas which reduce direct dependency of the population on the central government; this could cause a source of instability where the people might form interests with their direct governor, and as a result revolt against the main ruler. However, with time, the population of rentier states will realize that the distribution of the rent is not an act of “kindness” from the state, but rather a natural right entitled to them. Finally, in line with other rentier state theorists’ claims, Crystal also asserts that if oil revenues decrease state stability, they may be challenged by a revolt of the people against their allocating governments. Since oil exporting states are tied to one leading sector, they need to turn to

other economic means under fiscal pressures. Nevertheless, since rentier states have little alternatives, chaos is inevitable.

Okruhlik rejects the claim made by earlier rentier state theorists' that such states are able to control potential opposition by distributing oil wealth. She extracts examples from Saudi Arabia, Kuwait and Bahrain, and proves her claim by showing that opposition movements may emerge. Contrary to Luciani's claim that unequal distribution of rents has no important consequences in oil producing states, Okruhlik claims that unequal distribution of rents directly creates opposition<sup>26</sup>. Moreover, she mentions that oil is not a tool utilized by the government to silence opposition movements; oil is a tool gathering rebellious groups together to stand against the government. Okruhlik points out that instability and opposition take place due to the failed policies which are put into force by rentier states. She goes as far as to blame those states for their policies.

The last wave of rentier state theory is what is recognized as the revisionist theory which came to light in the beginning of the 21st century. Revisionist rentier state theory criticizes the previous literature of rentier state theories, and it refuses the claim that rents are structural variables with independent and uniform effects on the state type. Instead of this, revisionist literature does not see rent as an independent variable; they instead see it as an intervening one which is affected by the internal variables of a rentier state. Late rentierism provides a framework which contributes to the understanding of the Gulf's regimes and their dynamics and policies, given the circumstances in which they have found themselves at the different stages of their development.

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<sup>26</sup>Okruhlik, G. (1999). Rentier Wealth, Unruly Law, and the Rise of Opposition: The Political Economy of Oil States, *Comparative Politics*, Vol. 31, No.3.

Peters Moore, a revisionist theorist, commented in 2002 on the fiscal crisis and its effect on the regime's stability in the Gulf region. Contrary to the claim of previous rentier state theorists, such as Luciani, Moore believes that despite the fiscal crisis that emerged as a result of the decrease in oil prices, change in the state type in the Gulf region has not occurred.<sup>27</sup> He also argues that the interest of the private sector is similar to the interests of the state, and we shall see in the following chapter how the state is actually interested in private sector<sup>28</sup> activities in different Gulf States, and how it contributes to it in order for the private sector to give the state shares in their profit. Hence, Moore focuses on state-business relations and the sectors of productivity within a state.

In *Hard Times in the Lands of Plenty*, Smith writes that the state's reliance on oil depends on whether oil is the major commodity generating wealth of the state. Smith mainly claims that revenues from oil rents allow the rulers to develop strict means towards opposition movements which in return decrease the possibility of regime failure. Like Luciani, Smith claims that while oil wealth brings stability to the state, it ensures its longevity to a certain degree; however, it decreases the realization of democracy. In contrast to Luciani's claim, Smith asserts that this durability of the regimes is independent of the oil revenues because decrease in oil revenues does not cause regime crisis and instability to the oil exporting states<sup>29</sup>.

Given the literature review, the modern approach to rentier state theory proves that several errors exist while applying conventional theory to contemporary politics. Many

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<sup>27</sup>Moore P. W. (2002). Rentier Fiscal Crisis and Regime Stability: Business-State Relations in the Gulf, *Studies in Comparative International Development*, Vol. 37, No. 1

<sup>28</sup> Smith, B. (2007). *Hard Times in the Lands of Plenty: Oil Politics in Iran and Indonesia*, London: Cornell University Press.

<sup>29</sup> Ibid

aspects of rentier state-society relations remain ambiguous and need further research and examination.

In *No Representation without Taxation*, Herb asserts that wealth generated from external rents does not necessarily imply that a state is a rentier one. He claims that Ross's approach is inaccurate because it fails to distinguish between rent based wealth and wealth based on other factors. With reference to Ross' assessments, states which generate wealth because of oil and those which generate wealth through other sectors could have similar degrees of undemocratic systems without having links to being a rentier state<sup>30</sup>.

Recently, the impact of rentier state theory has become questionable due to several factors that might render it invalid with the rise of recent events. For example, many structures in the Gulf States can be analyzed by historical and social contexts rooted in ancient loyalty towards tribes; thus, this social interaction does not necessarily imply that the citizens are in favor of their governments, but seem so because they are playing the role of "allocation states" as Luciani claims. In fact, the citizens of Gulf States are seen to desire communal solidarity, allowing them to adhere to an autocratic ruler<sup>31</sup>.

The rentier state theory as explained by Luciani only describes such states as those which pursue "expenditure policies". These states rely heavily on rent generated from domestic economies and disregard other active sectors within the state. This approach, for example, fails to include the recent positive economic reforms which are being introduced by GCC member states. There have been many efforts to diversify their economies, impose economic reforms, and introduce development programs. For example, the United Arab

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<sup>30</sup> Alessandro, Zicchieri (2016). Is Rentier State Theory Sufficient to Explain the Politics of the UAE? *E-International Affairs Students*.

<sup>31</sup> Ibid.

Emirates is undergoing an Emiratisation program aimed at increasing the participation of native workers in the production of goods and services in the private sector. Recent attempts by the citizens of the Arab world have also proven the classical rentier state theory wrong. As a matter of fact, taking into consideration the example of Libya or Bahrain, their wealth based in oil rents did not keep the countries from maintaining the status quo. Different international political and internal sectarian factors played a role in the recent uprisings in the Middle East, and these factors are not thoroughly covered in traditional rentier state theory. The theory focuses mainly on measuring a rentier state by its domestic policies and fails to measure its social and political structure by not taking into consideration the state's foreign policy. Today, the GCC member states are in a position where they form a considerable weight in the politics of the Middle East as major players in regional alliances.

With the progression of the Gulf States, the Rentier State theory has progressed too. Not only does the theory attempt to explicate the absence of democracy in the region, but it also attempts to answer crucial questions about the interrelationship between society and state in oil exporting states.

UAE, KSA, Kuwait, Qatar, Oman, and Bahrain witnessed severe changes in their governments in the last ten years. The question today is: how does rentier theory stand in the current world? We will examine in the following chapter how rentier states still stand today in the Arabian Gulf by presenting data and figures from the economy of GCC member states and by measuring to what extent these states coincide with the theories we have previously discussed in this chapter.

## **Chapter Three**

### **GCC Countries as “Rentier States”**

Necessary reforms have been adopted to diversify the GCC economies and reduce their reliance on oil. Over the last few decades, the Arab Gulf States have increased public sector employment and spending on infrastructure, health and education. This chapter analyzes the diversification efforts in the six Gulf cooperation Council countries. Charts and figures are provided in this chapter to illustrate the level of oil dependency in each state, with an emphasis on the recent positive initiatives taken by the Gulf States to achieve a non-oil economy and encourage liberalism, and the structural constraints of these diversification initiatives. This will lead to a conclusion that reformations and economic transformations in the Gulf are clearly challenging conventional Rentier State Theory.

#### **Rentiersim in GCC Countries**

Self-ruling elites in the Middle East have proven to be more resilient to the political and economic changes that took place during the civil uprisings in recent years and which affected different countries of the Arab world more than predicted. Although several regimes were overthrown, the governments of the GCC member states such as the monarchies in Gulf areas like Kuwait, Qatar, UAE, Bahrain, Oman, and Saudi Arabia were not challenged brutally, and have actually stood steadily in the face of opposition movements. In fact, even though Bahrain and Saudi Arabia were subject to brief clashes

and protests by civilians, Al Kalifah and Al Saoud governments were only slightly affected and alternative plans to oppress such movements were immediately put into action.

Several countries in the Arabian Gulf, especially Bahrain, Kuwait, Saudi Arabia and Yemen, are considered to have unique socio political histories in the Arabian Peninsula. These states have achieved enormous amounts of economic wealth in a very short duration of time due to the availability of natural resources on their lands. As a matter of fact, western companies have positively increased their interest in investing in these countries and opened companies in the region in the 19<sup>th</sup> century, companies which continue to operate within these territories until this date.

The International Monetary Fund (IMF) states that oil proceeds in GCC member states have been used to modernize infrastructure, create employment, and improve social indicators. All these records were achieved while still being able to accumulate official reserves, maintain relatively low external debt, and maintain their role as important donors to poor states. Life expectancy in the GCC area increased by almost 10 - 14 years during 1980–2000, and literacy rates increased by 20 - 80 percent over the same period. Average per capita income in the GCC countries was estimated at about \$12,000 in 2002, with their combined nominal GDP reaching close to \$340 billion (more than half the GDP of all Middle Eastern countries).<sup>32</sup>The table below illustrates these figures.

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<sup>32</sup>MENA -- GCC Countries: From Oil Dependence to Diversification, Ugo Fasano and Zubair Iqbal, International Monetary Fund Publication, 2003

**Table 1: GCC Countries: Selected Economic Indicators, 2002**

Country	Nominal			Overall Fiscal Balance (Percent of GDP) <sup>2</sup>	Total Government Gross Debt (Percent of GDP)	Proven Oil Reserves (Years) <sup>3</sup>	Central Bank Foreign Assets (Months of Imports) <sup>4</sup>	Current Account Balance (Percent of GDP)
	Nominal GDP (Millions of U.S. dollars)	(Per capita dollars) <sup>1</sup>	Population (Millions) <sup>1</sup>					
Bahrain	8,506	11,619	0.7	0.8	30.3	15.0	2.7	0.3
Kuwait	33,215	15,098	2.2	20.6	32.9	134.0	10.7	20.9
Oman	20,290	7,515	2.7	3.7	16.0	16.0	4.8	10.0
Qatar	17,321	28,362	0.6	5.1	58.2	15.0	2.7	13.8
Saudi Arabia	188,960	8,567	22.1	-5.3	93.8	85.0	12.9	4.7
U.A.E.	71,187	19,613	3.6	-9.3	4.5	124.0	4.7	5.5
GCC	339,479	11,979 <sup>5</sup>	31.9	-2.7 <sup>5</sup>	66.6 <sup>5</sup>	83.7 <sup>5</sup>	7.6	6.9 <sup>5</sup>

Sources: National authorities; and IMF staff estimates.

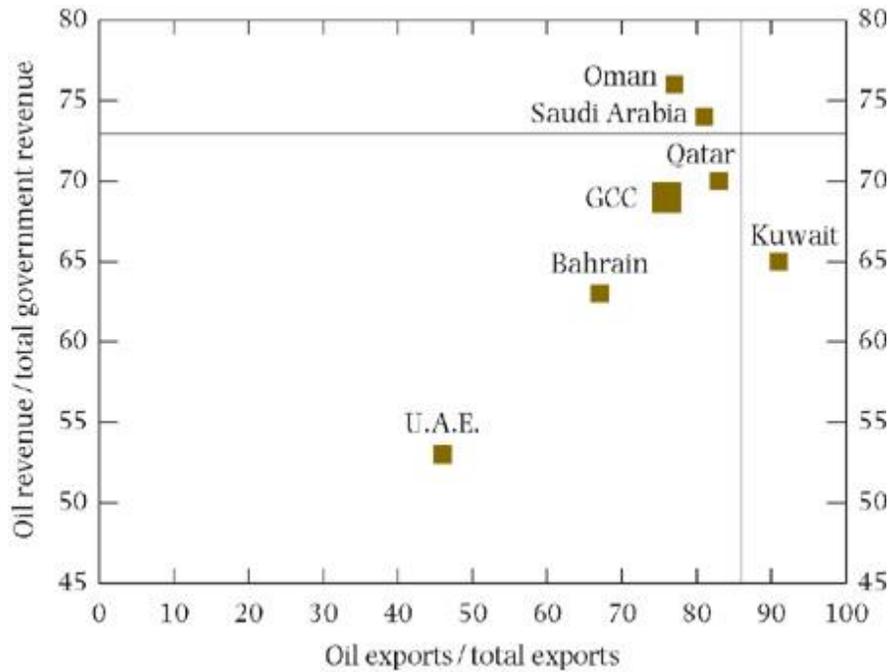
<sup>1</sup>Including expatriates.

<sup>2</sup>Including investment income of government foreign assets.

<sup>3</sup>Based on current production.

<sup>4</sup>These figures are not an accurate reflection of the country's foreign assets position because data on government foreign assets are partial in some GCC countries.

<sup>5</sup>Weighted average.



**Figure 2: GCC Countries: Oil Dependency (Average in 1998–2002; percent).**

Total government revenue includes investment income, and total exports include re-exports.

In addition to the above, data indicates that GCC countries share many economic characteristics. Oil contributes about one-third to their total GDP and three-fourths to annual government revenues and exports. Together, these countries account for about 45 percent of the world's proven oil reserves and 25 percent of crude oil exports (Saudi Arabia being the largest world oil exporter), and they possess at least 17 percent of the proven global natural gas reserves (Qatar becoming the fourth-largest exporter of liquefied natural

gas).<sup>33</sup> GCC countries are highly dependent on a large expatriate labor force, reflecting the small (but rapidly growing) size of the domestic workforce and the limited domestic supply of adequate skills. Expatriate workers now account in most GCC countries for about three-fourths of the total workforce. These countries have maintained an open-door policy to attract expatriate labor since the 1970s, and this has played an important role in the diversification of the production base and development of the service sector. The availability of imported skills at internationally competitive wages has been crucial to keeping the cost of production down. Most of the national labor force has been employed in the government sector with higher wage expectations than the expatriate workers. Thus, the labor market has remained segmented by sectors of employment, wages, non-wage benefits, and skills.<sup>34</sup> As a result, citizens of rentier states would prefer to strive for their wealth, prosperity, and economic stability rather than engage in regime changing movements. The challenges facing the labor market in the GCC countries are a crucial point we should thoroughly clarify before presenting the overall challenges that are faced by each of these country's economies.

### **3.1 The GCC labor market**

The main purpose of this section is to highlight the conditions and challenges of the GCC labor market. The text will explain how reforming the labor market will boost the employment and productivity, and subsequently, re-orient the GCC economies to become more varied.

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<sup>33</sup> Ibid.

<sup>34</sup> Ibid.

Labor markets in the member countries of the Cooperation Council for the Arab States of the Gulf are gradually becoming more complex, and unemployment pressures are developing among young nationals. Elevated growth in the national or local population throughout the last few years, coupled with the rising participation of women in the labor force, is turning into a rapidly growing supply of nationals seeking employment. Indeed, the national/local labor force has been growing at an average annual rate of 4 to 5 % over the past ten years and is most likely to continue at this rate over the next five years since more than 1/3<sup>rd</sup> of the national population in GCC countries is currently below fifteen years old.

Unemployment pressures among nationals have been undemonstrative until lately due to the fact that most GCC governments have been acting as employers of “first and last resort”. Consequently, nationals now establish the majority of the workforce of the public sector. This approach, however, has neared its limits since the wage bill has now become increasingly large, and continues to rise consistently in response to pressing need, in order to keep up with the demand for government services of the increasingly young population. The wage bill now represents over 10% of the GDP in most countries. For this reason, the responsibility of job creation in the coming years will most probably rest with the private non-oil sector. The task will not be an easy one though. Throughout the past 30 years, a liberal foreign labor policy has permitted the private non-oil sector to depend mostly on less expensive, better-trained, and more flexible foreign workers to support its development. The immediate result is segmented labor markets and a low pliability of substitution among both the national and foreign workers.

Based upon this, policymakers within the GCC countries must cast the appropriate balance between dealing with the pressures of an increasingly rising local labor force, and preserving a malleable policy toward the hiring of expatriate workers. Or else, unemployment of GCC nationals might increase, or the competitiveness of the non-oil economy might be at risk. The extent of this issue differs among these countries. Countries like Bahrain, Oman, and Saudi Arabia face a more immediate obstacle than the others because of their relatively huge national/local workforce. Policies are now shifted towards boosting the replacement of foreign workers with national workers within the realm of a combination between mandatory and market-based mechanisms, and the promotion of non-oil economic growth.

The general population of the GCC countries is quite small. The entire population, along with the expatriate community, was estimated at 32 million in the year 2000. The Kingdom of Saudi Arabia has the biggest population of 22 million, while countries like Bahrain and Qatar have the smallest. The expat population is about 1/4<sup>th</sup> of the entire population in Saudi Arabia but accounts for more than 70% of the entire population in the smaller countries. Elevated fertility rates across the past decades have transformed into elevated population growth. Despite these rates declining from 6.4 births per woman in 1980 to 3.5 births per woman in the year 2014, they remain elevated by international standards, especially in Oman and Saudi Arabia where they are considerably above the regional average. Based upon these facts and figures, the GCC population remains growing at over 3% per year. Also, a huge proportion of the general population is currently aged between 0 years and 14 years old, with the average general population age ranging between 26 years old and 30 years old. One more thing to note is the fact that the

dependency ratio has also remained elevated, reaching a staggering 96% in Saudi Arabia in the year 2000, as opposed to 72% among other Arab countries.

According to Kito de Boer, the Director in McKinsey & Company's Dubai office (2007), oil revenues are creating unprecedented wealth within the Gulf; however, elevated unemployment rates of youth are forcing countries to implement reforms to both their financial and educational systems on the national level. Pakkiasamy (2004) states that foreign workers constitute a major faction within the Saudi labor force – a reality the Saudi government is recently addressing in a more serious manner. Across the last 10 years, the government has prioritized “Saudiization”, an initiative that aims at increasing employment of Saudi nationals in every sector of the domestic economy, and reducing reliance on foreign workers. However, although Saudiization efforts are in high gear, the country continues to depend on foreign labor to be employed in both high and low leveled jobs. The government's premature initiatives safeguard the indigenization of the workforce, but will fail if they are not as quickly implemented as envisioned.

Fasano&Iqbal (2003) make it clear that over the past 30 years the countries of the GCC have witnessed an unparalleled economic and social boom. Oil revenues have been used to modernize infrastructure and create employment. The GCC area has become the major hub for regional economic growth. However, they state that we cannot generalize, because labor market challenges are contextual and unique across GCC countries. Anthony J. Figliolini summarizes the whole idea of this paragraph in his introduction which references the 2003 paper and states, that:

“The rapid expansion in the number of young nationals in the labor market, particularly in Bahrain, Oman, and Saudi Arabia, combined with downward rigidities in reservation wages—while expatriate workers are available at internationally competitive and flexible wages—has created the potential for strong unemployment pressures. The authorities are aware of the pitfalls of a quick "nationalization" of the labor force and are appropriately focusing on long-term structural solutions while taking interim steps to ease the transition to a market-based system in which wages reflect labor productivity.”

### **3.2 The Challenges of the GCC Labor Market: Localization and Nationalization**

The discovery of oil and gas, as well as their development in the GCC countries has brought a fast rise in economic prosperity and in the overall improvement of the quality of life on the individual and group levels of those countries. Because of the initial shortages in both skilled and unskilled labor, foreign workers were naturally hired to assist in the building of these rapidly booming economies. But as political, economic, and demographic challenges now make it more of an obstacle for countries to hire foreign nationals, while simultaneously a vast percentage of citizens remain unemployed, “Nationalization/Localization” programs were set up in order to assist in the replacement of foreign workers and establish new employment possibilities for locals/nationals, as well as to diversify the overall national economies of these developing states.

The matter of localization is one that perhaps presents the greatest challenges within these countries. For countries to replace foreign workers and create jobs of quality for their populaces, they also need to offer opportunity for foreign firms to expand in their region. For this reason, firms that are successful in their recruitment and development of

national/local talent are linked to the economic “fabric of the region” and have shown an obligation towards ensuring a more sustainable and long-term overall success. Most of these positive relationships underwent years of development. The fast-paced growth and high-performance of the global human resource management movement empowers firms working in the GCC region to develop close-knit ties and favorable reputations in order to eventually become “employers of choice.”

Localization has been on the table for the GCC leaders since oil was initially discovered and foreign businesses as well as expertise were both brought in in order to take advantage of the new discovery at the time. GCC countries wish to work on the increase of the percentage of locals/nationals employed in the private sector for reasons previously addressed, which are mainly rooted in the current demographic, political, and economic conditions under which they function.

With the rapid growth of the GCC economies as well as the elevated percentages of foreign workforces, the countries of the GCC have found themselves within an exceptional paradigm. Countries of the GCC experienced elevated economic growth in the era between the years 1960 and 2000. It ranged from 3.6% for Bahrain and 4.1% for the Kingdom of Saudi Arabia, to 6.5% for Qatar to 8.8% for the UAE. The population growth has since gradually decreased to about 4% per year ( Fasano & Iqbal, 2003 ). However, the economic growth is steady at about 3% per year – a figure estimated to increase steadily with the fluctuation in oil prices over the coming years. The population under the age of 15 years old is quite significant within the majority of these countries as stated previously, reaching 43% in the Kingdom of Saudi Arabia and Oman. This has a direct effect on the

number of young people arriving at the job market, and this percentage is either anticipated to stay constant, with a possibility of slight increase.

The number of foreign laborers within the GCC countries is currently estimated around 10 million individuals (Pakkiasamy, 2004), with percentages ranging from 26% of the national population in Oman to 82% of the overall population of the United Arab Emirates. Constituting 90% of the workers in the United Arab Emirates, foreigners constitute a major section of the workforce as well. This also applies to Qatar. The majority of the expatriates functions within low-level jobs and currently earns less than locals/nationals. Current economic growth has generated lower paid, low-skilled, and low-status jobs rather than the high-profile ones<sup>35</sup>that locals prefer (Harry, 2007). Moreover, migration to North American countries or neighboring European countries is usually for a short period of employment and not for more permanent settlement.

The demographic aspects which were previously addressed give great political motivation to localization programs within each GCC state. In his referral to the demographics within his own nation, United Arab Emirates nation builder and former, President Sheikh Zayed bin Sultan al-Nahyan stated in January of 2003, *“This imbalance continues to pose a grave problem which threatens the stability of our society and the prospects for future generations”* (Suliman, 2006). Rees, Mamman, and Braik (2007) state that the GCC nationalization is possibly directly linked to an aspiration to merge and preserve political independence and to manage internal affairs. Other less tangible factors cannot be ignored when tackling this issue. For instance, the Arab philosophical approach

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<sup>35</sup>These labels are rooted in jobs that are above and below the national poverty line, as well as above or below minimum wage within each state, and are roughly labeled so. There is no official label for these levels of jobs.

which states that the fortune of the entire Gulf region must be shared among all Arabs, along with the combination of regional conflicts (such as the Iraqi invasion of Kuwait), have elevated security fears concerning non-GCC Arab expats, and restricted their ability to stay within the region (Harry, 2007). These countries have concluded that the Arab expat community has been the easiest to supplant with local nationals, since several of the jobs they previously administered as well as the positions they held were Arabic-speaking, clerical, professional, and within the public sector (Abdalla, 2006). This labor force demonstrates convenient job characteristics which locals are often in search of. Moreover, having huge populations of low-paid, and at times ill-treated, workers may be a hazard and security concern, as a vast population of discontented as well as predominantly unemployed youth can be.<sup>36</sup>

The economic characteristics behind localization are of major concern to firms who currently do business within GCC countries, as they currently possess the most influence over current and aspired profitability. Localization is seen as an effort to terminate the reliance on foreign know-how, and particularly in the areas of development and within the oil/gas industries. The establishment of Saudi Aramco as well as its growth into the principal oil company across the globe may be seen as a model of localization and of self-reliance by several major players within the international community that up until recently, believed to have the sole know-how and expertise in the field of the oil industry. The decline in oil prices throughout the 1980s and 1990s, as well as the consequential debt of Saudi Arabia, coupled with the comprehension that oil is a natural resource that has its

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<sup>36</sup>The population discussed that is around 15 years of age.

limits, and not a permanent or sole fixation in the overall development process, raised concern among GCC countries regarding economic reliance on the oil industry.

Unofficial estimates of McKinsey & Company's Kito de Boer place the overall unemployment rate within the Kingdom of Saudi Arabia, Bahrain, and Oman at around 15%, with the overall rates of unemployment for persons aged between 16 years old and to 24 year old at a figure of 35% (Unemployment Drives GCC Reforms, 2007). The company believes that in order to tackle their obstacles of unemployment, the countries of the GCC must create approximately 300,000 high-quality private sector jobs each year, and double the current wages of these positions. Moreover, if these states wish to establish this number of positions, they need to reform everything, from the education system to what is seen as a suitable work ethic/environment within a host population. Also, a level of preparedness of the employers themselves needs to be procured (Harry, 2007). According to Harry, the GCC countries have a foundational problem of not formulating their youth properly to work within the private sector.

### **3.3 The GCC Economies: Stepping up to Future Challenges**

Reviewing economic indicators, official statements, actual investments and projects under implementation by the GCC countries (Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the United Arab Emirates), we can see that Arab Gulf States are turning diversifications plans into action.

#### **3.3.1 Saudi Arabia**

Saudi Arabia's wealth is based on oil trade to the rest of the world. Saudi Arabia possesses 25% of the world's oil reserves with a GDP of \$24.000 per capita.<sup>37</sup> Since Saudi Arabia's economy is reliant on oil trade, other sectors such as the service and industrial sector have been non profitable. The developed areas in Saudi Arabia involve real estate and stock market. Based on data from the U.S. Department of State, Saudi Arabia's state-owned enterprises (SOEs) play a leading role in its economy, particularly in water, power, oil, natural gas, and petrochemicals. Saudi Aramco, the world's largest producer and exporter of crude oil and a large-scale oil refiner and producer of natural gas, is solely owned by the Saudi Arabian Government, and its revenues typically account for around 85% of the government's budget. Aramco's board reports to the Supreme Council for Petroleum and Minerals Affairs which is chaired by the King. Likewise, 70% of Saudi Basic Industries Corporation (SABIC), the Kingdom's leading petrochemical company, is owned by the government with its Chairman also being a member of the royal family.

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<sup>37</sup>Aydin, A. (2013). "Hereditary Oil Monarchies: Why Arab Spring Fails in GCC Arabian States?" SDU Faculty of Arts and Sciences SosyalBilimlerDergisi Journal of Social Sciences.

These models serve as an exact example of a rentier state<sup>38</sup>. During the 1960s and 1970s, expatriate labor played an important role in developing the oil production in Saudi Arabia because the indigenous population in Saudi Arabia did not possess the oil production skills; only a few of them were involved in the part of the oil production process which was distributing and utilizing the production.

Oil exploration in Saudi Arabia started when King Abdul Aziz bin Saud granted Standard Oil of California concession to explore for oil. The country was previously reliant on tourism of people travelling to Saudi Arabia for pilgrimage, and the population was mostly nomadic. However, the year 1938 shifted the country's economic status when oil was discovered and the new Saudi Arabian governmental structure was established by the Al Saud family. Foreign workers expatriated some of the income from oil while the majority became the property of the new monarchy headed by Abdul Aziz bin Saud<sup>39</sup>.

The Saudi Arabian state owns an oil company called Aramco which is situated in Dhahran. Since the 1930s, this company has become the world's most significant company in exploring crude oil and natural gas and it is fully owned by the Al Saud family<sup>40</sup>.

The safe haven of Saudi Arabia's revenues is in the hands of an exclusive and authoritarian family. Saudi Arabia demonstrates all the characteristics of rentierism and prioritizes citizens who are affiliated to the ruling family by tribal loyalties; these families accumulate the greatest shares from the state's revenues. With vast oil revenues, there is no personal (individual) tax in Saudi Arabia; the government demands no taxes from its

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<sup>38</sup>“Executive Summary Saudi Arabia.” U.S Department of State

<sup>39</sup>“Oil Discovered in Saudi Arabia”. National Geographic Education. 12 Feb 2014. Web.

<sup>40</sup>“Who We Are”.Saudi Aramco. Web

citizens. The government puts into force a program to redistribute benefits to the whole population in the form of entitlements<sup>41</sup>. Not paying taxes weakened political participation in Saudi Arabia, resulting in the Al Saud dynasty monopolizing political power<sup>42</sup> who in turn paved the way for foreign, and especially American, companies that were responsible for launching infrastructure projects in Saudi Arabia such as airline industries and broadcast facilities and for overseeing the development of its defense industry.<sup>43</sup>

Internally, the long leadership of Saudi Arabia's elites divides the Saudi public into sectarian groups to avoid the population from following a unified trend. Several attempts have taken place in Saudi Arabia to overthrow the Al Saud rule but were repressed. The Saudi government is losing its Islamic credentials within the events happening in the Middle East today due to the emergence of new radical groups using religion as their main inspiration behind their cause. For instance, the 1979 extremist act which took place in Saudi Arabia targeting the Grand Mosque in Mecca planned to overthrow the Saudi regime. In this regard, the Saudi government has used its financial power for private gains; they have retaliated by putting into force strict religious codes and bringing an Islamic clergy to fulfill the role of counsel to the King<sup>44</sup>.

Rents from oil revenues in Saudi Arabia offer the population free healthcare, education, infrastructure, employment, as well as subsidized energy and water. If these social, cultural and economic services were removed, the new reality would force the population

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<sup>41</sup>"The Expatriate Financial Guide to Saudi Arabia." AILO. Web

<sup>42</sup>"Saudi Arabia Country Profile – BBC News." *BBC News*. Web

<sup>43</sup>"Executive Summary Saudi Arabia." U.S Department of State

<sup>44</sup> Wright, *Sacred Rage*, (2001), p. 155

of Saudi Arabia to seek their own means of profitable income, and consequently pay for energy, water, health care, and education.

The Saudi population is expanding at a very rapid rate, and with such rapid growth comes an increase in domestic demand for more oil. According to the BP Statistical Review of World Energy 2014, Saudi Arabia was the world's 12<sup>th</sup> largest consumer of energy in 2013. The oil reserves in Saudi Arabia, as everywhere else, are limited and even if they don't run out in the near future, it is an inevitable reality that they will eventually, and the government of Saudi Arabia must come to terms with this reality before it is too late. Hence, the need for alternative resources as a petroleum replacement has been part of a worldwide conversation since the early 1970s. Efforts have been made to expand on the discovery and utilization of alternative resources such as wind, solar power, and coal as a replacement for oil energy, but none have come close to the cleanliness, ease of extraction, transportability, and low price that petroleum has provided.

### **3.3.2 Bahrain**

Bahrain is an important case study in rentierism because it is the country in the Gulf which has experienced civil unrest due to the presence of its Shiite population, and it has actually served as an example for other Gulf countries of the fact that they are not immune from opposition movements. Bahrain also has internal socio-economic problems. The country's rulers are rich, and there is an economic disparity between them and the Shiite majority of the population which creates problems. In addition, the lack of democratic reform in the country bans a solution in the near future. Bahrain's state owned enterprises and sectorial limits on foreign investment distort the country's economy, and the events

that happened in Bahrain threatened Saudi Arabia from extending the unrest to its premises. With reference to these events, and as mentioned in A Theory of “Late Rentierism” in the Arab States of the Gulf, the Saudi King Abdullah on February 23, 2011, offered two packages of spending to quell popular unrest, which summed up US\$129 billion in overall costs with spending covering housing support, overseas study funds, and social security initiatives, among others<sup>45</sup>. Unlike other GCC member states, Bahrain’s mineral exports score less than 2 percent of GDP. Also, oil and mineral exports constitute between 20 to 50 percent of the GDP<sup>46</sup>. A rentier state such as Bahrain shifts its concentration from oil production into strengthening alternative economic sectors to ensure the country’s wealth growth. Today, Bahrain relies on financial services rather than oil and gas because its oil reserves are limited unlike its neighboring states. Clearly, shifting the economy in Bahrain doesn’t happen without a price. Bahrain focuses on aluminum exports which generate wealth for their treasury much more than oil exports<sup>47</sup>. Bahrain depends on Saudi Arabia economically, and this dependence has increased since 2011 after Bahrain became vulnerable following the 2011 uprising. In an article by Jane Kinninmont, the kingdom of Bahrain is reported to produce from its sole onshore field around 48,000 barrels per day. Furthermore, most of its oil revenue comes from a Bahraini share of an offshore field controlled by Saudi Arabia<sup>48</sup>. Data reveals that Bahrain’s economy has been drastically influenced since the 2011 uprisings and that the Bahraini budget has been in

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<sup>45</sup>Gray, M. (2011). “A Theory of “Late Rentierism” in the Arab States of the Gulf.” Center of Regional and International Studies, George Town University. Web.

<sup>46</sup>Craig, J., Meyer, K., Costello M., & Aly, H. (2008). “International Rentierism in the Middle East and North Africa, Ohio State University.

<sup>47</sup>“Analysis: Bahrain’s Economic Challenges.” *Middle East Eye*. Web.

<sup>48</sup> Ibid

deficit every year since 2011<sup>49</sup>. Bahrain has a \$4 billion budget deficit which accounts to 13% of the total GDP. It does not have too many options to cover this deficit because of its insufficient foreign assets. 86% of the revenues of Bahrain's treasury still come from oil despite the fact that the government has sought to diversify its economy and build communication and transport facilities with its neighboring Gulf States. One of the government's plans was developing a Free Trade Agreement with the United States. However, apart from the oil sector, Bahrain does have major economic activity in the production of aluminum and construction.

Moreover, the services sector in Bahrain, specifically the hotels and restaurants sector experienced a fast growth in 2012, growing by 13.6% over the year<sup>50</sup>. While regarded impressive, this growth rate in large part represented normalization from disruptions in 2011. Manufacturing, as well as social and personal services grew by a robust 5% and 13%, respectively<sup>51</sup>. The main drivers were expansion in the petrochemical and oil-related industry as well as private health care. As facts show in a report from the *Economic Yearbook of the Kingdom of Bahrain*, that the government provides services such as education and public health care. The sector has experienced strong growth over the past decade, expanding by 213% between 2002 and 2012. Although the historically strong growth in the government's health and education has been slightly lower in recent years, growth in output has been underpinned by a rise in other government services. This practice is an indicator that the Government of Bahrain still functions within a rentier mentality.

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<sup>49</sup> Ibid

<sup>50</sup>Economic Yearbook 2013, Kingdom of Bahrain.(n.d.). Retrieved from <http://www.bahrainedb.com/en/EDBDocuments/Bahrain-Economic-Yearbook.pdf>

<sup>51</sup> Ibid

Based on the Bahrain Economic Quarterly Report, records show that Bahrain's non-oil sector is growing whereas the oil production is stagnating<sup>52</sup>. In comparison to European standards, these numbers are considered to be low; however, they pose a serious concern for this small country because its wealthier neighbors were able to save money for harder times even when oil prices were high<sup>53</sup>. The example of Bahrain confirms Luciani's claim that rentier states are weak states, and the formation of such states is fragile. In response to the 2011 uprisings, the four richest of the Gulf States have promised \$10billion to Bahrain and Oman over 10 years. Despite that move, the country's reputation was damaged since the 2011 uprising, weakening its ability to compete with other Gulf countries for investment.

### 3.3.3 Qatar

Qatar differs slightly from its neighbors in the Arabian Peninsula, but also possesses all the characteristics of a rentier state. All the revenues from oil are transferred to the Qatari government's treasury. The government of Qatar enjoys full autonomy, it governs the political and economic branches, and it makes sole decisions on behalf of the population.

The political system in Qatar is based on a unitary parliamentary absolute monarchy where the head of the state, currently Tamim bin Hamad Al Thani, has absolute power. Luciani's claim that rentiersim and authoritarianism are closely linked cannot but come to mind when investigating this country. Although Qatar has a consultative assembly known as "Majlis El Shura", only 15 out of the 45 members of this assembly are appointed for

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<sup>52</sup>"Bahrain Economic Quarterly". June 2015. Web.

<sup>53</sup>"Analysis: Bahrain's Economic Challenges." *Middle East Eye*. Web.

authority, a clear indicator of a non-democratic practice<sup>54</sup>. The unelected assembly gives the impression of a democratic assembly, but in reality, this assembly's members are mostly related to or have ties with the ruling elite.

Qatar has become one of the wealthiest rentier states in the world because it has the highest economic growth of the GCC countries. Its economy rests largely on oil exports and all the revenues are received by the government. The country has 15 billion oil reserve barrels and gas fields that account for more than 5% of the global resource<sup>55</sup>. That amount of wealth can buy off critics, opposition voices and government legitimacy and leave no room for development. The government exploits its power to implement what it wishes and to ban what threatens its durability, yet another typical element of a rentier state. In addition, while discussing the links between a rentier state and human rights abuse, Qatar is a prime example. The rights of many migrant domestic workers who travel to work in Qatar as low skilled laborers are extremely violated, and they face many discriminatory acts and in many instances abuse of their basic rights, such as getting remunerated<sup>56</sup>.

Regardless of the above offenses, the economy of this wealthy Arab State remains promising. Qatar does not feel the necessity to expand or invest in other sectors to boost a diversified economy since the oil trade is generating sufficient wealth to the country and is estimated to stay as is for the next 23 years<sup>57</sup>.

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<sup>54</sup>Riaz S. (2014). "The Parliament of Qatar." Daily Parliament Files. Web.

<sup>55</sup>Lincoln, S. (2013). "Qatar Shows How Money Can Solve Most Problems." Business Day Live.

<sup>56</sup>Country Narratives.(2011). Human Trafficking Report, Office to Monitor and Combat Trafficking in Persons, US Department of State.

<sup>57</sup>Ozyavuz, A., & Schmid, D. (2015). "Persistence and Evolutions of the Rentier State Model in Gulf Countries." Institut Francais Des Relations Internationales. Web

The following table illustrates that Qatar, according to a 2012 report, records the GCC’s highest GDP per capita.

**Table 2: Gulf Countries GDP per Capita**

Qatar	93831.35118
Kuwait	56366.57008
United Arab Emirates	41691.67905
Saudi Arabia	24116.17763
Oman	23569.93653
Bahrain	23039.43912

Source: The World Bank Database

Qatar has a very low unemployment rate, and World Bank records illustrate that the overall unemployment rate in Qatar is less than 1%. This is due to the organized temporary residence permits of working visas for expatriates employed in the country<sup>58</sup>. Locals are expressing their frustration due to the competition with foreign labor forces. However, the majority of the wealth is in the hands of the population’s few rich elites while the rest is allocated to the population.

Recently, the government has been shifting an interest in economic diversification because of an important event due to be hosted in Qatar in 2022: the World Cup. Due to this international event which will shift international attention to this peninsular country,

<sup>58</sup> “Qatar: Unemployment, Total (% of Total Labor Force)(World Bank) – Data and Charts from Quandl.”

the government is spending a lot of its wealth on it and is considering eventually improving the service sector in the country in order to house people from all over the world. This in turn is compelling foreign investors to do business in Qatar; however, this interest has restrictions since Qatar remains to a large extent a rentier state. Hence, when the government is included in specific business shares, it will contribute more efficiently towards that business's interests and present more desirable opportunities and services, such as Qatar Airlines.<sup>59</sup>

### **3.3.4 Kuwait**

Kuwait is one of the front states in the Arabian Gulf which is also considered to be rentier. The ruling monarchy in Kuwait is in the hands of the Sabah family who took over the ruling in 1752 and have been in power ever since. The Al-Sabah family is the decision maker in all aspects related to foreign and domestic Kuwaiti affairs<sup>60</sup>. The system in Kuwait is a unitary constitutional monarchy, and the legislative branch is composed of a national assembly. The last elections took place in Kuwait on 27 July 2013, and the majority of legislatures who won were pro government.<sup>61</sup>

Kuwait is another vital case study when analyzing rentier state theory because in addition to the fact that it is a wealthy state, it also plays the strategic role of hosting U.S. military bases. Economically, it occupies the 5<sup>th</sup> rank among the global oil reserves<sup>62</sup>. The increase of the oil prices and the increase in demand of this scarce resource served the oil

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<sup>59</sup> Has Wealth Made Qatar Happy? *BBC News*. Web

<sup>60</sup> "Cultural Intelligence for Military Operation: Kuwait." Marine Corps Intelligence Activity, 2003. Web.

<sup>61</sup> "Kuwait." *The World Fact Book*. Central Intelligence Agency. Web.

<sup>62</sup> Ibid.

producing states in the Gulf and increased their wealth. The State of Kuwait has significantly benefited from this reality as the records show in the below figure.

**Table 3: Kuwait government revenue for fiscal years 2003/4 and 2007/8 (USD b)**

	2003/4	2007/8
Total	23.1	67.3
From oil	20.5	62.7
Non-oil revenue	2.6	4.6
Oil as % of total	88.7	93.2

*Source: calculated from Kuwaiti Ministry of Finance "Final Accounts 2007/8"*

Even though the revenues are increasing, facts and statistics still serve as a solid indicator that Kuwait persists as a rentier state. Unlike other rentier states, the people of Kuwait are supporters of democracy although they still have a long way to go before they can achieve correct democratization. Al Sabah family practiced some semi-democratic policies by agreeing to give vital powers to an elected parliament in 1961; however, they have suspended this decision twice since and once again imposed an absolute hegemony of their family in the state's political arena. Kuwait's members of parliament advocate for fair laws only to ensure another term in power, but when it comes to implementation none of the promises are delivered<sup>63</sup>. Just as any other rentier State, Kuwait is purchasing the

<sup>63</sup>Al Zumai, F. (2013). "Kuwait's Political Impasse and Rent- Seeking Behaviour: A Call for Institutional Reform." Gulf University for Science and Technology. Westminster University Law School.

loyalty of its citizens by establishing a welfare system which offers free education, interest free loans for citizens, and electricity<sup>64</sup>.

The Iraqi invasion in 1991 was another important event that shifted Kuwait's political status. This war actually restored a certain degree of democracy in the country after the intervention of U.S. led coalition to force Iraqi troops out of Kuwait<sup>65</sup>. Today, lawmakers actually question the executive branch and point out the corruption, but the degree of effectiveness still remains questionable<sup>66</sup>. An *Amnesty International* report in 2013 states that freedom of press in Kuwait is declining due to legal actions directed towards Kuwaiti activists; therefore, even though Kuwait might seem to be a country with more freedom than its neighbors, its institutions still maintain fundamentally rentier attitudes<sup>67</sup>. In an article published by Carnegie Institute, analysis showed that Kuwait might gradually produce better representation and participation in the international arena. While unruly, Kuwait's example offers an illustration of what could be a future model for politics in a rentier state.<sup>68</sup>

In addition, the Banking sector in Kuwait has been showing improvement in recent years, and this development offers a promising future for Kuwait's economic diversification and stock exchange. This is a very important sector because if it succeeds, it can shift the interest from oil to the service sector.

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<sup>64</sup> Ibid

<sup>65</sup> "Kuwait's Democracy Faces Turbulence." *The Wall Street Journal*. Web

<sup>66</sup> Elbadawi, I., & Kubirsi, A., (2014). "*Kuwaiti Democracy: Illusive or Resilient?*" Lecture and Working Paper Series No. 1, American University of Beirut Institute of Financial Economics. Web.

<sup>67</sup> Al Zumai, F. (2013). "*Kuwait's Political Impasse and Rent- Seeking Behaviour: A Call for Institutional Reform.*" Gulf University for Science and Technology. Westminster University Law School.

<sup>68</sup> Al Khouri, R. (2008). "Kuwait: Rentierism Revisited." Carnegie Endowment for International Peace, 28. Web.

### 3.3.5 United Arab Emirates

The United Arab Emirates is recognized today for attracting enormous numbers of foreign laborers to its market. The reason behind the stability of the United Arab Emirates is the rentier phenomena. Data reveals that 80% of the residents in the UAE are foreign residents, meaning the other 20% of the UAE nationals are benefitting from the state's welfare system. The United Arab Emirates is a unique state in the Arabian Gulf because it is the only model of a federation including seven monarchies. The political system is therefore based on having a president, who is currently Sheikh Khalifa bin Zayed Al Nahyan, and a Federal National Council composed of 40 members out of which only 20 members are elected by the people. An important achievement that took place during the last elections in UAE was the election of a female parliamentarian.

As previously mentioned, since UAE is a federal state, rentierism is practiced on the emirates level and on the higher federal governmental level. On the level of the various emirates, Abu Dhabi for example is a major contributor to the federal budget through oil rents. In turn, the federal government uses the revenues from the oil rents to finance central rulers who have no or little oil. By doing so, the central rulers' loyalties are being purchased by the federal government which in turn ensures the country's stability. Another example is Dubai, a region with a considerable contribution in oil rent, and a region simultaneously considered a modern city with revenues from tourism and commerce. Just like the trend of Abu Dhabi, Dubai follows suite in the process of rentierism in UAE<sup>69</sup>. In addition, the federal government follows a no tax policy as that is not necessary due to sufficient oil rent revenues.

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<sup>69</sup>Aartun, A. (2002). "The Political Economy of the United Arab Emirates An Analysis of the UAE as an Oil Rentier State." Department of Political Science, University of Oslo.

Alejandro Ortega, in his article *Dubai: The Case for Modern Tribalism* argues that Dubai is categorized by what academics term “vertical chains of relationship.” He argues that Dubai’s current political structure is based on a system of tribalist relationships whereby the sheikh is tied ‘vertically’ to various ruling families, business elites, loyal friends, all the way down to the lower classes of society<sup>70</sup>.

The following figures are factual records derived from the economy of the United Arab Emirates; data shows that the UAE is the second largest economy in the region, recording one of the highest economic growth rates in the Arab region because of its growing oil and gas exports. In the years 2004 to 2008, the UAE economy doubled because it was fueled by a strong growth of oil, hydrocarbon and non-oil sectors.<sup>71</sup>

Although the United Arab Emirates diversifies its economy, it still remains largely reliant on the main sector of wealth generation which is oil rents. UAE is yet another example of a rentier state where revenues from oil are hindering the democratization process in the country. Economic growth in the UAE is steady despite a short-lived interruption caused by the weakened global economy. Recovery was brought on by high oil prices, increased government spending, and boosts in tourism, transport and trade. In addition, successful restructuring of debt owed by high-profile companies, solidarity among the emirates and accommodative monetary and fiscal policies all played a role in bringing significant economic stability to the market.

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<sup>70</sup> Alejandro, O. (2009). “Dubai: The Case for Modern Tribalism.” *Stanford Journal of International Relations*..

<sup>71</sup> “United Arab Emirates – UAE.” *Gulf Base.Web*.

Although oil has been the backbone of the United Arab Emirate's economy and even though it continues to contribute significantly to economic prosperity of this country, a long term planning for UAE'S economy ensures economic diversification by allowing the oil sector to occupy less than 50% of the national GDP<sup>72</sup>. In the United Arab Emirates, the government has put together two main plans with the intention to diversify the Emirati economy and those two plans are the Abu Dhabi's Economic Vision 2030 and Dubai's Strategic Plan 2015. These plans aim to strategically maximize the business activities besides oil and gas service; that is to include the industrial and exports sector such as heavy industry, petrochemicals, and renewable energy. As a matter of fact, the government has already started performing well in such fields. Although the developments of these sectors are happening gradually, nobody can deny that they are strong alternatives to oil and will have a positive impact in the long term.

One of the main priorities of the Strategic Plan set by the Emirati government is ensuring a sustainable economy and the government knows that oil and gas are natural resources which will sooner or later impose a barrier in UAE's economy rather than a blessing. In order to implement this plan, the UAE government is replacing an oil based economy with an innovative, research based economy and is giving weight to highly knowledgeable experts. In so doing, the government is providing its citizens with an opportunity to experience a competitive economy instead of giving them the passive role only.

As evidence, tourism has played a large part in the success of the economic diversification in the Emirates. Facts show as recorded on the Embassy of UAE in the United States that Abu Dhabi's 156 hotels recorded their best year ever in terms of visitor

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<sup>72</sup>T. (n.d.).The Abu Dhabi Economic Vision 2030. Retrieved from <https://www.ecouncil.ae/PublicationsEn/economic-vision-2030-full-versionEn.pdf>

numbers, whilst Dubai's 634 establishments have also experienced a significant increase in guests. Other emirates are following suit<sup>73</sup>.

The United Arab Emirates is improving their business friendly environment for foreign investors, both to facilitate trade and attract inflows of foreign direct investment, which will help achieve balanced, sustainable development<sup>74</sup>. The government of the United Arab Emirates is facilitating a business environment with diplomatic cooperation, such as signing bilateral and multilateral cooperation agreements. This has also had a domestic impact in the UAE legislation on the federal level and has imposed reforms to introduce competitive business laws and attract foreign investors. The new law regulates economic activities and exploitation of intellectual property rights (IPR). This is expected to promote competition and contribute to efforts to meet the objectives of the Strategic Planning of the government.

According to the 2013 Global Investment Report published by UNCTAD, the UAE benefitted from inward FDI flows in 2013 of approximately US\$10.5 billion. Also, facts show that the UAE was the top Arab capital exporter over a 32-year period from 1980 to 2011: UNCTAD figures show that over this timeframe, the UAE pumped nearly US\$55.5 billion into global markets accounting for nearly 31 per cent of the total Arab FDI outflow of about US\$175.8 billion. Outward FDI in 2012 amounted to US\$2.5 billion and US\$2.9 billion in 2013.<sup>75</sup> Moreover, with assets worth US\$733 billion, the UAE's Abu Dhabi

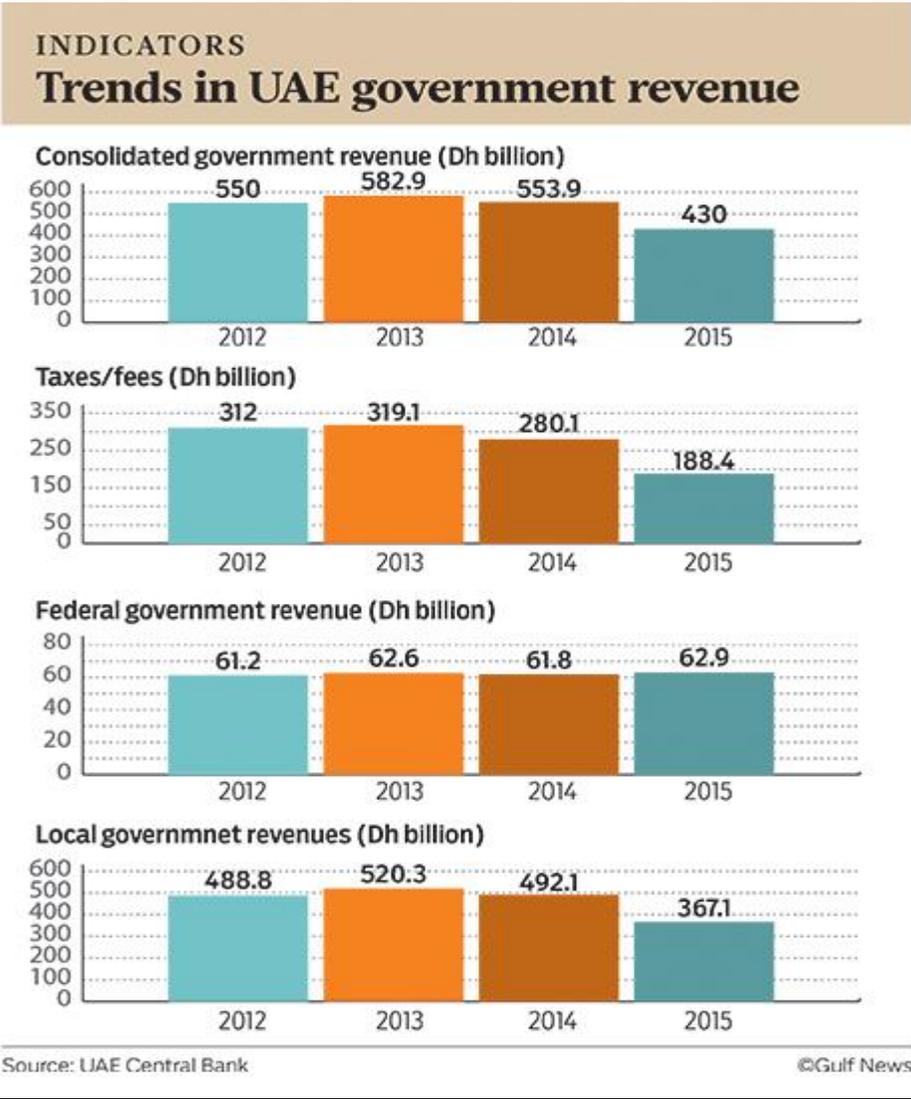
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<sup>73</sup>UAE Economy.(n.d.). Retrieved February 16, 2016, from <http://www.uae-embassy.org/about-uae/uae-economy>

<sup>74</sup>Ibid.

<sup>75</sup>UAE Interact (n.d.). THE ECONOMY. Retrieved from <http://www.uaeinteract.com/business/economy.asp>

Investment Authority (Adia) is factually the second richest SWF in the world, investing in a wide range of assets from equities and fixed-income securities to infrastructure. Other UAE SWFs, such as the Abu Dhabi Investment Council (US\$90 billion), International Petroleum Investment Company (US\$68.4 billion), Mubadala (US\$60.9 billion) and Emirates Investment Authority (US\$15 billion) play significant roles in investment<sup>76</sup>.



**Figure 3: Trends in UAE government revenue.**

<sup>76</sup> Ibid

### 3.3.6 Oman

Oman's economy is largely reliant on the oil and gas that contribute to 50% of the country's GDP, but it has increasingly improved its tourism sector, a sector now having a considerable contribution to the country's wealth<sup>77</sup>. The government of Oman is implementing new plans to diversify the state's economy, as estimates reveal that oil is not a sustainable resource, even though the life span of this natural resource is being extended as much as possible with the help of technological advancements. Oman's proven oil reserves have a limited time at current rates of extraction (15 years). The sultanate is not a member of the OPEC; however, its general policies are similar to its neighboring states and to GCC member states.

The below chart shows estimates of Oman's proven Oil Reserves and justifies why Oman is currently diversifying its economy. The Arab sultanate of Oman was the last to discover its possession of natural resources, and will in turn be the last to limit its production and export. Oil was first exported from Oman in 1967 and in turn this practice developed into designing a social contract system with the population, a simple practice of a rentier state. Similar to Kuwait, Oman has a certain degree of democracy, and this is evident via the recent Arab Spring in 2011 which challenged the government in Muscat to silence the population when they stood up for themselves in the face of unemployment and corruption, bringing to the government's awareness the fact that the welfare system is not a long term tool capable of repressing the voice of its people.<sup>78</sup>

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<sup>77</sup> "Oman 2015." Oxford Business Group, 25 Jan.2015. Web

<sup>78</sup> "Oman." Central Intelligence Agency. Web

**Table 4: Oman's Proven Oil Reserve**

Year	Millions of barrels	Years of production left (based on current production)
1977	5.7	46
2023		
1979	2.4	22
2001		
1993	4.7	16.5
2010		
1999	5.3	15.9
2015		
2003	5.6	19.6
2022		
2007	5.6	19
2026		

Sources: World Bank, World Economic Forum, BMI, Times of Oman.

Oman's governmental system is an absolute monarchy and the legislative branch is comprised of two houses: the upper and the lower. The consultative assembly (the lower

house) is comprised of 84 members who, unlike other GCC members, are elected democratically<sup>79</sup>.

The government is moving ahead with privatization of its utilities, the development of a body of commercial law to facilitate foreign investment, and increased budgetary outlays. The chart below illustrates Oman's strategic planning for a diversified and wealth-generating economy independent of oil production. These strategies show that the sultanate is shifting away from a rentier state to a more open economy integrating more of its citizens in the country's decision making process, consequently paving the way for a better democracy.

With the rise of the middle class within the region, Oman began implementing tourism, strengthening infrastructure, and ultimately modernizing the economy, privatizing government enterprises, and improving health services. This liberalization brought several improvements to the country's economy and to its citizens. The backdrop of political stability has ensured that there is consistency in economic reform because policies are implemented and legislation is enacted. Corruption has also been curbed considerably in recent years with improved governance structures and education systems. This is contrary to the experiences of other countries that rely on the export of natural resources for their national incomes.

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<sup>79</sup> Al-Farsi, S. H. (2014). "Democracy and Youth in the Middle East: Islam, Tribalism and the Rentier State in Oman." Volume XXI, Number 21.B. Tauris.

**Table 5: Key Dimensions of the Vision for Oman’s Economy 2020 Strategy<sup>80</sup>**

1. Stable macroeconomic framework
2. Increase the role of government in providing basic social service while decreasing its role in production and public service
3. Develop human resources
4. Economic diversification
5. Develop the private sector
6. Raising the standard of living equally
7. Integrate into the global market economy

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<sup>80</sup>Howk, J. C. “Lions in the Path of Stability and Security: Oman’s Response to Pressing Issues In The Middle East.” Naval Post Graduate School, Auburn University.

### **3.4 Between the Curse of the Resources and the Changing Global Context**

The above specific case studies show that GCC member states do practice rentier principles to a large extent. However, with the acknowledgement of the scarcity of their natural resources, countries such as Oman are shifting their economies into a more liberal and diversified one in order to maintain their economic wealth.

As long as the Gulf States work within the premises of economic monarchies<sup>81</sup>, no practical outcomes such as free trade and investment zones can be attained. And as long as there is no challenge to absolute power or the stability of the state, all attempts will remain futile. It is worth noting that those states entertain “reforms” aimed at restructuring economic sectors, changes that are restricted to only the sectors which are not responsible for generating the states’ wealth such as air transport, telecommunication, and security. The provision of services to private companies operating on geographically and socially sensitive grounds is another quasi-reform strategy adopted by the governments of such states in order to share revenues.

The international importance rentier states reach, as proved by the theory’s literature, is a result of their crucial international role. Therefore, these states do not resort to pressuring the international community by depending on their foreign policies. As a result, the theory nevertheless suffers from certain limitations because these states need to form an international alliance in order to enhance their economic sustainability in the international

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<sup>81</sup>Al Khouri, R. (2008). “EU and U.S Free Trade Agreements in the Middle East and North Africa.”Carnegie Endowment for International Peace, Web

arena, given their primary reliance on oil, a non-renewable source of energy and consequently, wealth. This strategy is implemented in the Gulf countries by their alliance formations with the West. This is due to the interest of Gulf elites to have access to arms and training in addition to other types of benefits that would be of vital use on the regional and domestic level<sup>82</sup>.

Moreover, with the sharp oil price decline of 2014, GCC economic stability was put into question. Following 5.8% average GDP growth from 2000 to 2011, the IMF project growth rates decreased from 2.4% in 2015 to 3.2% in 2016. In the same years, GDP fiscal deficits of 7.9% and 3.6% are projected after the 12.4% GDP surpluses recorded between 2000 and 2011.

With apparently weaker demand growth and oversupply in the oil market, the GCC countries realized that the oil price decline was not a temporal crisis, thus revealing the futility of their initial “wait and see” strategy.

Posing as a contemporary challenge, the fall in oil prices proved to be promising. The pressure for structural reform in the GCC economies was alleviated in reaction to huge inflow of export revenues generated by crude and natural gas between the year 2000 and 2010. This did not last long since by 2016 the pressure returned accompanied by far-fetched and drastic economic and subsidy reforms like those of domestic energy pricing. This positive effect on the GCC economies demonstrated protest-free strategies to other Middle Eastern countries aiming towards the attainment of economic reforms.

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<sup>82</sup>Wehrey, F., & Sokolsky, R. "Imagining a New Security Order in the Persian Gulf." Carnegie Endowment for International Peace. Web.

## Chapter Four

### Conclusion

Just as Lalu Prasad Yadav said that “*In a Democracy, Power is Not Permanent*”, rentier states will eventually have to acknowledge that democracy will not come without a price; moving towards democratization means giving up absolute power. Although the road to democratization is long, it is not impossible for the Gulf States; however, the direct reliance of the gulf cooperation council countries on oil revenues instead of citizens’ money is what hinders democracy in the region, the dilemma being that these countries do not rely on domestic taxation. The people have no interest in demanding political freedom and so can limit any opposition or political disagreement that may cause social insurgency. The rich government and the money distributed between citizens help preserve peace, and subsequently make resorting to force non-essential. However, in such an environment democracy can progress. As a matter of fact, recent civil uprisings in the Middle East will enforce some changes in the region because people are becoming more aware of their rights. Social media and modern technology have weighed in the changing regimes. Although the Gulf States have built fortresses using their wealth, this does not mean that they do not fear facing a fate like other states in the region. The only way Gulf States can avoid chaos in their countries is by making correct policies and implementing them efficiently. In the past, oil was a tool to strengthen authoritarian regimes. Today; it might be a tool to declare a state’s illegitimacy. Oil is a natural resource which sooner or later will come to an end, and in a globalized era, only the dynamics of the international interests will shift the Arabian Peninsula’s fate in the near future.

Currently, as the oil prices have been vastly decreasing, it is expected that Saudi Arabia will be the country which is going to be impacted the most. Even though data shows that the Saudis still have more than \$620 billion in reserves, which they can use to maintain stability for a short period of time, they have subsequently been profiting from this sector about \$100 billion less than they were last year and this imposes a serious threat to the Saudi Economy. The chairman of Saudi Aramco said at the World Economic Forum in Davos that the Saudis are able to withstand low oil prices for a long time; however, he did not explain how they were able to do so considering that the oil prices have significantly dropped in just 18 months. These facts imply that Saudi Arabia's income is going to drop considerably, and consequently its expenditure will grow yielding a large overspend against the Saudi budget. Some analyze that Saudi Arabia's decision in late 2014 to lead OPEC into not supporting the sliding price of oil with output cuts has had a number of consequences, especially on the country's own finances, and a reverse in this policy is still pending. The drop in oil prices is not only impacting the Saudi economy, it is also impacting Saudi Arabia's global and regional position in the OPEC, as well as in the geopolitics of the Middle East. Saudi Arabia has been in control of crude oil prices for a long time. The drop in these prices will cost the Saudi's proxy wars, its OPEC leadership and its alliances internationally especially with the United States of America. Representatives speaking in public forums on behalf of the Saudi Government are prone to show that the Saudi's economy is not affected. However, economists realize that Saudi Arabia is safe for only a short time if current oil prices stay as they are.

Internally, Prince Muhamed Ben Salman has introduced the "National Transformation Project 2020". This plan aims for a better management of expenditure, improving revenue

sources and debt capacity and limiting growth in bloated expenditure whilst channeling resources to key sectors, ensuring economic growth. The Saudi government is scrutinizing governmental allowances; Saudi Ministers now have limited expenditure on cars, furniture and showcase projects and soon enough the Saudis will start paying a 5% added value tax for the first time on non-essentials. This step is going to be implemented in coordination with other GCC member states.

It is apparent that the Saudi government is very determined to find alternatives to wealth generated solely from the oil sector, and is thus drastically cutting the public payments which have been serving as forms of unemployment benefits.

The Saudi government also believes that implementing economic liberalization policies will attract foreign investors. Minister of Defense Muhamed Bin Salman stated recently that the government is willing to sell stakes in state assets from telecoms to power stations and the national Saudi airline. Furthermore, the government is planning on selling government owned land to developers to foster its real-estate sector and form a new sector for wealth generation in Saudi Arabia. The kingdom is also focusing on developing Islamic tourism to the holy sites, as it hopes to boost the 18 million annual visitors to up to 45 million in the coming five years. Saudi Ministers also spoke of enhancing privatization in education and in social welfare through doubling private education to cover 30% of students, establishing charter schools, and transforming public health care into an insurance based system with expanded private provision.

Due to the economic and political unrest, KSA reported a 3.4% GDP deficit as a result of the financial benefits provided to its citizens in the year 2014. This fall was caused by

the plunge in oil revenues. Later in early 2015, and in consequence to the kingdom's participation in Yemen's war, the government reported a 15% deficit in its GDP. The deficit proved the notion that rentier states cannot sustain their economies by relying only on their oil revenue. Such realization caused the Kingdom to advocate reforms such as cutting fuel subsidies in half, raising oil prices, and introducing the VAT. All these steps were considered in order to outstretch the country's participation period in the war.

#### **4.1 Contemporary Transformations of the Rentier Regime in the Gulf**

Back in the 70's and 80's, the GCCs were upheld by oil and gas as their backbone. Today, energy is still a large percentage of GDP and export income in most of the countries, the royal families continue to control politics and business, and foreign workers still constitute a large base of the population in the gulf countries.

But while oil and gas revenues still dominate the economy, they are being utilized for more insightful policies and reforms that foster economic diversification. It appears that most Gulf States are abandoning complete rentierism and are moving towards a hybrid system. The states now acknowledge the scarcity of their natural resources and are taking that as an incentive to shift their economies into a more liberal and diversified state in order to maintain their economic wealth. Nevertheless, even though the Gulf States are competing to create free trade and investment zones, the centrality of authorities in these countries remains a significant issue. The relationships between these states and businesses are serving the political interests and the stability of one ruling family. Strengthening the private sector without direct intervention from the government is a concrete step towards

improvement. Not only would it serve the state economically, but it would also slowly implement a certain level of democracy<sup>83</sup>.

In fact, a rentier government doesn't need to micromanage investments, businesses, and the trade of the country to ensure its productivity. Instead, the government must establish a stable macroeconomic framework with clear guidelines and fair laws to ensure economic liberalization<sup>84</sup>.

The GCC countries have recently been shifting towards a diversified economy. The natural resources of rentier states are not permanent and this reality imposes a degree of responsibility on such governments to sustain their economic growth by strengthening other sectors. GCC governments have already started investing in entrepreneurship, basic research, innovation and infrastructure. Each state should pursue policies suited to its own political, economic and cultural institutions.

The necessity of developing skilled human resources in the countries is a crucial point here. As long as the people living in rentier states have no incentive to exert their skills other than in oil exportation, foreign labor will dominate the domestic market leaving no room for a rentier state's citizens to be productive. With the speedy growth of the GCC economies as well as the elevated percentages of foreign workforces, the countries of the GCC have found themselves in an exceptional paradigm.

The number of foreign workers within the GCC countries is currently estimated to be around 10 million laborers. The economic characteristics behind localization are of major

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<sup>83</sup>Howk, J. C. (2008). "Lions in the Path of Stability and Security: Oman's Response to Pressing Issues In The Middle East." Naval Post Graduate School, Auburn University.

<sup>84</sup>Ibid.

concern to firms who currently do business within the Gulf States, as they currently possess the most influence over current and aspired profitability. The GCC must create approximately 300,000 high-quality private sector jobs each year, and double the current wages of these positions. Moreover, if these states wish to establish this number of positions, they need to reform everything: from the education system, to work ethics and environment, as well as the preparedness of the employers themselves to make a sustained and consistent effort, to the contribution of various work related skills, and even attitudes and behaviors etc.

Nevertheless, the reform measurements rentier states are undertaking are promising. Data reveals that growth in sectors not related to oil in GCC member states averaged 6.8% between the years 2000 and 2013, and the share of the non-oil sector in total real GDP rose by 12 percentage points to 70 percent.<sup>85</sup> These policies have focused on providing a stable macroeconomic environment; strengthening the business incentives; investing in infrastructure and education as well as promoting entrepreneurship<sup>86</sup>.

Recently, GCC member states have implemented a wide range of policies and initiatives to improve their businesses. The reforms included the legal sector for facilitated business procedures, enhanced competition policies, and organized and developed investor and consumer rights<sup>87</sup>.

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<sup>85</sup>Callen, T.,Reda, C., Hasanov F., &Hegazy A. (2014). “Economic Diversification in the GCC: Past, Present, and Future.” International Monetary Fund.Web.

<sup>86</sup> Ibid

<sup>87</sup> Ibid

Moreover, liberal approaches have included efforts in creating free trade zones in the United Arab Emirates, and the establishment of the GCC Free Trade Area with a common external customs tariff in 2003<sup>88</sup>.

Other development projects include developing transportation services and reducing custom administration procedures and clearance requirements. They have also set up promotion entities to help companies export their products (for example, the Export Development Authority in Saudi Arabia and an Export Development Center in Bahrain)<sup>89</sup>.

The GCC has also showed some improvement in the trade network and transport-related infrastructure, in addition to developing oil-related industries, tourism, logistics, transportation, business, and financial services<sup>90</sup>.

However, managing change in a dynamic world is a prolonged complicated process. Oil prices have fallen to their lowest level since 2003 and analysts state that the drop was driven by oversupply coupled with a fall in demand. Oil producing nations have been affected the most; in Saudi Arabia, for example, the government put together economic transformation plans after analysts foresaw a serious threat to the Saudi economy. Classical rentier state theory suggests that rentier regimes would rely on oil rents to maintain their wealth and longevity; however, contemporary politics are proving otherwise. As a matter of fact, the Arab uprising and the recent low oil prices urged GCC member states to implement steps to diversify their economies to maintain stability and seek alternatives for wealth generation. These realities assert that the gulf countries have entered a period of unprecedented uncertainty and prove traditional rentier state theories wrong.

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<sup>88</sup>“EU Relations with the Gulf Cooperation Council (GCC).”European Union.Web.

<sup>89</sup> Ibid

<sup>90</sup> Ibid

This paper reveals the importance of the study of rentier states in economics and international relations because it explains the rentier governments' stances internationally, it measures the relationship between rentier regimes and societies, and it also examines the economic liberalization within a rentier state compared to other capitalist economies. The significance of this paper particularly lies in the data, theory, and recommendations of shifting GCC rentier states into more liberal economies. It introduces the theory of rentier states and explains how the theory itself has changed with the dynamics of international events. The paper also includes an in-depth examination of each GCC member state separately, and it briefly gives an individual account of each GCC member state's economic and political history. Additionally, it projects the challenges they are currently facing especially after contemporary events such as the Arab Spring and the drop in oil prices, while also presenting the positive measures they have undertaken to cope with these challenges. Due to the lack of exhaustive research involving all GCC member states in one essay, this paper contributes to the limitation of this academic work.

The presented material mostly relies on scientific analysis, academic research, books and recent international data from academic and credible online publications such as the OPEC, IMF, and World Bank; it has also relied on first hand interviews with governmental executives. The limitations to this research are that there have been no first hand accesses to GCC governmental records since the data retrieved has been reviewed by governmental publications only. Moreover, another evident limitation is the lack of first hand measurement of the effect and implementation of economic reforms in GCC member states; the data collected in this regard has been dependent on facts revealed in statistical charts published by each relevant government and by international organizations.

The study on rentier state theory is a continuous field of study because with changes in world order, states are being obliged to shift a lot of their policies towards more liberal economies and towards better democracies. The theory of rentier states alongside international events change, and future research must continuously develop methodologies to cope with the change in the study of this dynamic theory.

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## Appendix A: Oil Exporters: Oil and Non-Oil Real GDP Growth

*(Annual change; percent)*

	Average		2013	Projections		
	2000–11	2012		2014	2015	2016
	<b>Non-Oil</b>					
	<b>GDP</b>					
<b>MENAP Oil Exporters</b>	<b>7.3</b>	<b>5.2</b>	<b>4.9</b>	<b>3.8</b>	<b>3.6</b>	<b>4.2</b>
Algeria	6.4	7.1	7.1	5.5	4.9	4.6
Bahrain	8.0	6.6	3.0	4.7	3.5	3.5
Iran, I.R. of <sup>1</sup>	6.1	-0.7	-1.1	2.5	1.0	1.5
Iraq	...	8.4	7.3	-5.2	0.0	6.0
Kuwait	6.9	0.6	5.6	3.5	4.0	4.5
Libya	1.4	43.7	8.7	-1.0	3.5	5.0
Oman	7.4	7.7	6.5	6.5	5.5	5.5
Qatar	14.6	10.0	11.0	11.6	10.6	9.5
Saudi Arabia	7.1	5.5	6.4	5.1	4.3	4.1
United Arab Emirates	6.4	3.3	5.4	5.2	5.0	5.0
Yemen	3.5	4.0	4.0	1.5	3.0	4.5
<b>CCA Oil Exporters</b>	<b>9.3</b>	<b>8.8</b>	<b>8.2</b>	<b>6.8</b>	<b>5.5</b>	<b>6.2</b>

Azerbaijan	10.2	9.6	9.9	6.1	4.1	4.0
Kazakhstan	8.2	8.0	7.0	5.8	5.1	6.4
Turkmenistan	15.0	11.7	11.1	13.0	10.2	9.0
Uzbekistan	...	...	...	...	...	...
<i>Memorandum</i>						
<b>GCC</b>	<b>7.5</b>	<b>5.2</b>	<b>6.5</b>	<b>5.7</b>	<b>5.1</b>	<b>5.0</b>
<b>Non-GCC oil exporters</b>	<b>7.0</b>	<b>5.3</b>	<b>3.0</b>	<b>1.5</b>	<b>1.8</b>	<b>3.4</b>
<b>Oil GDP</b>						
<b>MENAP Oil Exporters</b>	<b>2.6</b>	<b>0.1</b>	<b>-2.8</b>	<b>1.8</b>	<b>1.5</b>	<b>2.2</b>
Algeria	0.2	-3.4	-5.5	2.3	1.8	1.6
Bahrain	-0.3	-8.5	15.3	5.0	2.5	1.6
Iran, I.R. of <sup>1</sup>	1.5	-37.2	-8.9	7.3	-2.7	-1.0
Iraq	...	12.8	0.3	5.9	5.7	9.3
Kuwait	4.5	10.3	-0.8	0.0	0.3	0.2
Libya	-2.9	211.4	-31.6	-51.2	44.1	42.9
Oman	1.5	4.1	3.1	0.4	3.4	0.9
Qatar	11.2	1.3	0.2	-2.1	1.0	1.0
Saudi Arabia	2.2	5.1	-1.6	1.7	0.9	0.9
United Arab Emirates	2.2	7.6	4.8	0.2	0.4	0.2
Yemen	0.8	-11.5	13.2	-11.3	4.1	4.5
<b>CCA Oil Exporters</b>	<b>11.0</b>	<b>-2.1</b>	<b>2.6</b>	<b>0.2</b>	<b>1.5</b>	<b>2.4</b>
Azerbaijan	16.3	-5.3	0.5	-2.4	-0.9	0.0
Kazakhstan	9.0	-2.2	3.2	0.1	0.0	1.5

Turkmenistan	10.9	6.1	3.6	6.1	13.1	10.8
Uzbekistan	...	...	...	...	...	...
<i>Memorandum</i>						
<b>GCC</b>	<b>3.1</b>	<b>5.4</b>	<b>0.5</b>	<b>0.8</b>	<b>0.9</b>	<b>0.7</b>
<b>Non-GCC oil exporters</b>	<b>2.2</b>	<b>-5.6</b>	<b>-6.6</b>	<b>3.0</b>	<b>2.2</b>	<b>4.0</b>

Source: National authorities; and IMF staff estimates and projections.