INSTITUTE OF DEVELOPING ECONOMIES

IDE Discussion Papers are preliminary materials circulated
to stimulate discussions and critical comments

IDE DISCUSSION PAPER No. 524

State-Business Relations in the Smaller Gulf Monarchies: The Role of Business Actors in the Decision-Making Process*

Marc VALERI**

Abstract

The Arab monarchies of the Gulf have been undergoing striking socio-economic changes caused by the ending of the rent-based welfare state model on which they had largely relied since the 1950s. In this perspective, this paper aims at examining the comparative role of local business communities in affecting the orientations and the outcomes of the policies implemented during the period of high oil prices in the 2000s. This paper pays a special attention to the impact of the Arab Spring on the state-business relations in two of the smaller Gulf monarchies (Bahrain and Oman).

Keywords: Persian Gulf, Middle East, political economy, business, Arab Spring.

JEL classification:

---

* This work was based on the presentation at the International Symposium of CMPS Utsunomiya University & IDE-JETRO entitled "Changing the Arab Gulf States: Monarchy, Expatriate, and Economic Outlook in the Gulf" on 17 September 2014 at JETRO, Tokyo, and supported by the UK Economic and Social Research Council [grant number ES/J012696/1]

** Senior Lecturer in Political Economy of the Middle East and Director of the Centre for Gulf Studies, University of Exeter. (m.valeri@exeter.ac.uk)

The Institute of Developing Economies (IDE) is a semigovernmental, nonpartisan, nonprofit research institute, founded in 1958. The Institute merged with the Japan External Trade Organization (JETRO) on July 1, 1998. The Institute conducts basic and comprehensive studies on economic and related affairs in all developing countries and regions, including Asia, the Middle East, Africa, Latin America, Oceania, and Eastern Europe.

INSTITUTE OF DEVELOPING ECONOMIES (IDE), JETRO
3-2-2, WAKABA, MIHAMA-KU, CHIBA-SHI
CHIBA 261-8545, JAPAN

State-Business Relations in the Smaller Gulf Monarchies:
The Role of Business Actors in the Decision-Making Process

Marc VALERI
Senior Lecturer in Political Economy of the Middle East
Director of the Centre for Gulf Studies
University of Exeter

Abstract:
The Arab monarchies of the Gulf have been undergoing striking socio-economic changes caused by the ending of the rent-based welfare state model on which they had largely relied since the 1950s. In this perspective, this paper aims at examining the comparative role of local business communities in affecting the orientations and the outcomes of the policies implemented during the period of high oil prices in the 2000s. This paper pays a special attention to the impact of the Arab Spring on the state-business relations in two of the smaller Gulf monarchies (Bahrain and Oman).

Key Words:
Persian Gulf, Middle East, political economy, business, Arab Spring

Introduction

The first decade of the 21st century has seen an unprecedented awareness by Gulf Cooperation Council (GCC) elites of the need to rethink their states' socio-economic structures, in order to address challenges of political and economic sustainability. Thus, while high oil prices arguably reduced the pressure to diversify in the 1970s, the period of high oil prices during the 2000s instead coincided with changes in the role of the state, economic diversification policies, and reforms in labour markets. This has had major implications for the whole social contract in these states, and more particularly for the relations of the business sector with the political authority. This paper focusses on the business elites' positions, perceptions and role in the economic, social and political decisions implemented by the regimes. In particular, it aims at shedding new light on the role of the business actors for the stability and legitimacy of the system and ruling elites (especially after the Arab Spring).

The state-business relationship in the Gulf monarchies

Prior to the influx of major oil revenues, domestic stability in the monarchies of the Arabian Peninsula was insured by an arrangement linking rulers and local merchant families, who helped provide the rulers' financial needs, receiving in return political influence and protection of their economic interests. The merchants remained key partners until the surge in oil revenues accruing directly to the rulers from the 1950s. The historical alliance between merchants and rulers was disrupted by the unexpected material sufficiency of the rulers, after oil was discovered. The rulers were thus freed from their economic dependence on the merchants. The state monopoly on managing expenditure and development allowed the creation of a welfare state which became the cornerstone of the ruling families' political legitimacy. In effect this created a new social contract. The state distributed oil rent through free education, free health care and high-salaried government jobs; granted key political and administrative positions to historically-important tribes or families and economic monopolies to nationals; and introduced practices and laws which gave nationals rights and privileges which were not enjoyed by non-nationals. In return, the ruling families expected the non-interference of nationals and civil society in domestic politics. Thus, in the Gulf, the terms of the famous formula ("no taxation without representation," raised during the United States' Independence war by supporters of political liberalisation) have been reversed to become: "no representation without taxation".

Jill Crystal explains that the development of oil production in Kuwait and Qatar forced the merchants to renounce their historical claim to participate in decision-making;[1] in exchange, the rulers granted them a large share of oil revenues. While in Kuwait the ruler was forced to promise to keep royal family members out of business, in Qatar, because the merchant community was weaker and smaller, the ruler allowed his relatives into the merchants' economic territory. If eventual confusion of political and economic actors can be seen in Qatar, it is explained by the intrusion of ruling family members into economy, but also by the exclusion of merchants from the decision-making sphere. The same situation can be observed to a large extent in the UAE. The interrelations between the business elite and ruling families did not result in

[1] Jill Crystal, Oil and Politics in the Gulf: Rulers and Merchants in Kuwait and Qatar (Cambridge: Cambridge University Press, 1995).

any demands for economic or political change. In fact, merchants were more concerned with their own economic interests, and their limited political interests were focused solely on the condition that ruling families should use their political power to stop foreign merchants from competing in the private sector. In return, members of the ruling families involved merchant families in the running and managing of their businesses.

In Bahrain the business elite has been heavily dependent both on the balance of power within the royal family (Al Khalifa) and on its good relationship with the most influential individuals among the royal family, who monopolizes the important and most sensitive ministries. If a number of Bahrani[2] merchant families were historical allies of the Al Khalifas (such as the al-Baharna, al-Urayyid, and Rajab families), the Bahraini business elite is mainly composed of Sunni families, either of Najdi background or Hawala.[3] Given that this merchant elite view themselves as a minority and that their influence is not based on deep social networks, they have never been powerful enough to force the ruling family to stay out of business—as is the case in Kuwait. As a result, the Al Khalifa family has never had to grant a substantial number of leading positions in the decision-making field to the economic elite, and it retains extensive political room for maneuver vis-à-vis the merchants. Moreover, the Al Khalifas themselves have always been substantially involved in business. Indeed, the Al Khalifa family was the first beneficiary of the oil wealth:

> The wealth of the state has been the Al Khalifas' to distribute as largesse to grateful citizens… Most of the land on the island belongs to the Al Khalifa family and there has been no institutional accountability of the family to the public…since the suspension of the parliament [in 1975].[4]

In the 1990s, Prime Minister Shaykh Khalifa "allegedly became the richest person in Bahrain with extensive holdings in land, hotels, commercial property, and

---

[2] The Baharina (sing. Bahrani) are the indigenous Shi'i Arabs in Bahrain. All Shi'a — both indigenous and of Persian origin— are considered to be 60 percent of the national population.

[33] The Hawala are Sunnis that migrated to Bahrain starting in the nineteenth century from the Iranian coast but claim Arab origins. An example of one of these merchant families historically close to the al-Khalifas is the Kanoo family, who moved to Bahrain from southern Persia in the mid-nineteenth century. Yusif Kanoo, who began as a small merchant in 1890 trading with India, became in the 1920s and 1930s the largest banker on the island and the Bahrain agent of companies such as the Anglo-Persian Oil Company and Ford. In the 1950s and 1960s, the House of Kanoo evolved into a conglomerate of companies, with headquarters in Bahrain, Dammam, and Dubai. The Kanoo group of companies is currently one of the largest family-owned groups of companies in the Gulf.

[4] Graham E. Fuller and Rend Rahim Francke, *The Arab Shi'a: The Forgotten Muslims* (New York: St. Martin's Press, 1999), 125.

profits on government contracts."[5]

The shaping of the labour market reform implemented in the 2000s is a superb illustration of the power struggle within the ruling family, between what a lot of observers labelled as the "old guard", around the Prime Minister Sheikh Khalifa, the Cabinet and the prominent business families and their arm (the Chamber of Commerce) on one hand, and the new generation of technocrats led by the Crown Prince Sheikh Salman and the unaccountable Economic Development Board (EDB), created by royal decree in 2001. In 2004 the American McKinsey consultant firm was commissioned by the Crown Prince to draft a comprehensive long-term economic programme for Bahrain. Following McKinsey's recommendations, the EDB was given the overall responsibility for outlining, proposing and managing the economic reforms for Bahrain in a comprehensive manner—including education, labour, tourism, industry and healthcare The philosophy of the reform was to deregulate and liberalize the job market and redress the imbalance between the local and cheap expatriate workforce[6] in order to address the structural causes of unemployment of nationals. It included gradually phasing out the Bahrainization quotas, allowing easier termination procedures of Bahraini employees and replacing them with a fee-based system under which employers pay a BD75 monthly fee per expatriate worker and a BD600 visa issuing and renewing fee per worker for each two-year period in order to bring the cost of local and expatriate labor force in line.

The private sector did not spare in its efforts to make its voice heard by the EDB—not only through informal channels and lobbying to the King and the Prime Minister, but also through repeated public demonstrations outside the Parliament to pressure the authorities and attract the support of the representatives. One of the "privileged" addressees of this lobbying was the Prime Minister, in whom the private sector knew it had an understanding interlocutor. The business community successfully pushed for cutting the fees so that an agreement was finally reached in 2007: BD10 per month per expatriate plus a BD200 visa renewing fee for each two-year period. Interestingly, the scope of action of the private sector in Bahrain was only indirect, as it responded and adapted to the evolution of the balance of power among the Al Khalifas.

In Oman, unlike the other Gulf monarchies, the country is not under the rule of a

---

[5] John E. Peterson, "Bahrain: Reform, Promise and Reality," *Political Liberalization in the Persian Gulf*, Joshua Teitelbaum, ed. (London: Hurst, 2009), 158.

[6] In 2006, 46 percent of expatriates working in the private sector, but only 1.1 percent of Bahrainis, earned less than BD100 per month (Personal calculation based on table 2.1.15.2 available at http://blmi.lmra.bh/otherdata/surveytables/mi_surveydata.xml; BD1 = USD2.66).

tribe or a family, but under that of a man, who has constantly shown his determination to keep control of all matters in the country. Because Sultan Qaboos has never been willing to rely on his small family, he has allied with the merchant elites, a practice in keeping with the pre-1970 period. Never, until the late 1990s, were the Omani merchants "forced to choose money over formal political influence,"[7] as in states like Kuwait and Qatar. Thus some of the pre-eminent merchant families' members have been given strategic positions to secure public contracts and control over the distribution of the oil wealth. To a certain extent, the ruler has been more dependent on the business elite for the stability of the regime than the merchants have been on the ruler for developing their economic assets.

At the same time, oil revenues profoundly changed the boundaries between politics and the economy, as many ministers whose families were previously not active in the economy become personally rich. Qaboos did not question this process, as it both increased the dependency of the elites on the state and the stability of his rule. The symbolic debts owed by Qaboos at the beginning of his rule to these key players who supported him after 1970 thus gradually turned into a weapon in his hands, forestalling any challenges to his reign by turning the most powerful societal forces into unfailing allies. On the eve of the 2011 Arab Spring, few members of the Omani Council of Ministers had not personally derived material profit from oil revenue. One of the most illustrative cases is the noble branch of the Khalili family—heirs to a prestigious lineage of Ibadi imams who opposed the Sultans of Muscat until the 1950s. Sa'ud al-Khalili, the nephew of the Imam of Oman Muhammad al-Khalili (1920-54), became one of the four members of Qaboos' first Cabinet appointed in August 1970. He is also the founder (1973) and owner of the powerful business group Al Taher, which is active in construction contracting (Caterpillar), food and drink (Sprite and Coke), and the distribution of Shell products. His nephew, Salim bin Hilal, Minister for Agriculture until 2011, was formerly chairman of the Chamber of Commerce, while another of his nephews, 'Abd al-Malik bin 'Abd Allah, who had previously held successively the positions of executive chairman of the Royal Court Pension Fund, of chairman of the first Omani banking group, Bank Muscat, and of Minister for Tourism (2011-2012), is currently Minister of Justice.

Political debates in Oman over the necessity to rethink the economic model of development based on oil revenue are not new. The economic slowdown in the 1980s,

[7] Jill Crystal, *Oil and Politics in the Gulf: Rulers and Merchants in Kuwait and Qatar* (Cambridge: Cambridge University Press, 1995), p. 195.

combined with the emergence of endemic unemployment among the younger generations, led to the implementation of Omanization policies favoring nationals in employment. In June 1995 a long-term program entitled "Oman 2020: Vision for Oman's Economy," was approved by Sultan Qaboos. Two series of objectives were set out. The first was economic diversification: the oil sector's share of GDP had to fall from 41 percent in 1996 to nine percent by 2020, while that of non-oil industries was to increase from 7.5 to 29 percent. The second objective had to do with human resources and employment. It planned to raise the proportion of nationals in the public and private sectors from 68 to 95 percent and from 7.5 to 75 percent, respectively, while the share of expatriates in the whole population would be reduced from 25 percent in 1995 to 15 percent by 2020. The new Labor Law, issued by royal decree on 26 April 2003, illustrated these priorities. Under this law, employers had to obtain permits from the Ministry of Manpower to bring in foreign workers only if there were not enough Omanis available for the post and if the company had complied with the prescribed percentage of Omanization in its branch (Article 18). Once the company was granted the permit, a non-Omani, to qualify for a job, could obtain a labor card issued by the Ministry (for a duration decided by the Ministry) on the condition that the worker had the professional skill or the qualifications required by the position and that the prescribed labor card fees had been paid by the company (Articles 18 and 19). Moreover, under this law nationals enjoy a set of social measures that expatriates do not, including a minimum wage (OR200 for a full-time unskilled job[8]) and strict protection against dismissal. Indeed, an employer can terminate the contract of an Omani only during the three-month probation period (Article 24) or under two other conditions—if the employee absents himself from work for more than seven consecutive days or more than ten days during one year without justification, or if the employee makes a major mistake (Article 40). Thus, the challenge of employing young Omanis, of whom 50,000 every year leave school and university (with or without degrees) and enter the labor market, led to national mobilization driven from above, with the Omanization policy being the main emphasis.

In comparison to similar policies in neighboring countries, the Sultanate can be proud of undeniable successes, at least quantitatively. By the end of 2005, the number of active expatriates in the private sector stabilized, while the rate of nationals in the private sector and the overall rate of Omanization (public and private sectors, excluding

[8] The minimum wage consists of OR180 as a basic salary plus OR20 as transport and housing fees (as of March 2011).

security and defense forces) increased from 15 percent and 28 percent, respectively, in 2003, to 19 percent and 32 percent two years later. In December 2009 the civil service sector showed an average Omanization rate of 85.6 percent, a figure that had consistently risen during the decade. Moreover, 91 percent of employees in the private banking sector were Omani. Nevertheless, these increases were not enough to hide structural difficulties due to the policy. In 2005, civil servants of the Ministry for Manpower spoke privately of 300,000 job seekers[9]—an unemployment rate around 25 per cent.

The fact that most cabinet members are involved directly or indirectly in business explains why the quota-based labour market policy could not be maintained in the long term. These decision-makers had to avoid questions about their supposed promotion of the nation's interests (such as the Omanization policy) versus the particular interests they were defending as businessmen. The major Omani business families who control the Chamber of Commerce and are represented in the Cabinet were strategically positioned to express their disagreement with the labor market policy to the ruler and thus to advocate for changes in long-term policy. But even more significantly, they were positioned to prevent the emergence of newcomers in business and alternative voices from the private sector. The Omani authorities focused on economic liberalization in the second half of the 2000s by giving prominence to national and foreign private capital, even if it meant the emergence of lasting inflation and an acceptance of a pause in the Omanization employment policy. For example, the new tax system that came into force in January 2010 cancelled the distinction between local and foreign companies by establishing a fixed tax rate on profits of 12 percent for all companies (both local and foreign) after an initial tax-free exemption of profits of OR30,000. In January 2006 Oman signed a bilateral free trade agreement with the United States, which came into effect in January 2009; many services are excluded from it in order to preserve the local network of small and medium-sized enterprises in the Sultanate, and Omanization requirements are still valid, even in the sectors covered by the agreement.

As a consequence of this strategic U-turn, the Omanization rate in the private sector decreased dramatically after 2006. This can be explained by the fact that the number of active expatriates exploded—particularly due to the need for foreign workers to labor on construction and infrastructure projects.

[9] Personal interview, Muscat, 30 August 2005.

The economic liberalisation policies implemented in the 2000s directly entered into conflict with simultaneous labour market reforms favouring employment of nationals in the private sector. Outcomes of concomitant policies of privatisation and economic liberalization (which mainly benefit already leading actors) and nationalisation of private sector jobs (which directly damages these interests) are reliable indicators of the nature of relationship between the state and the business elite, and especially of the different role that the business elite has played in shaping the reforms' outputs.

The business elite and the Arab Spring

Even if political grievances were crucial in the protests which took place in the GCC countries after 2011 (such as the implementation of constitutional monarchies in Kuwait, Bahrain or Oman, guaranteeing the separation of the three executive, legislative and judicial powers, or the end of sectarian discriminations in Saudi Arabia and Bahrain), social and economic demands have been at the top of the demonstrations' agenda in all GCC countries, revolving around job opportunities, pro-active measures to curb rising inequalities, and to fight corruption among top officials. In particular, official figures cannot hide endemic unemployment among young nationals (maybe except in Qatar and Abu Dhabi).

If anything, the 2011 protests in the Gulf are revealing of the economic resistance to change, i.e. the business elites' inclination to privilege the political status quo over any kind of reform debate, and the extent to which the interests of the main business actors are intrinsically linked to those of the authoritarian rule. The business elite, accused of corruption, unwarranted privileges and political and economic opposition to change, has been one of the main targets of the protesters. From this perspective, it is not insignificant that early attempts by the Omani ruler to show his supposed benevolence towards the protestors led to an extensive reshuffle of the cabinet in March 2011, with the removal of long-serving ministers widely perceived as embodying corruption and conflict of interests between business and politics (such as Ahmed Makki, the Minister for National Economy; and Maqbool Al-Sultan, the Minister for Commerce and Industry). The fact that demonstrations were particularly active in the town of Sohar, conceived as the international showcase of the economic liberalisation of the country, is highly symbolic too. The transition of Sohar within a few years from a small sleepy provincial town into the industrial capital of the country led to a disruption of the social structures. This badly-digested economic boom benefited above all a handful of local notables, who have taken advantage of the dramatic rise in land prices, as well as the Omani top business groups (Omar Zawawi Establishment, National Trading Co., Zubayr, WJ Towell, Bahwan, etc. in partnership with foreign investors) and members of the royal family (including the ruler's first cousin and Minister for Heritage and Culture *sayyid* Haytham, through the holding company for investment and project development *National Trading Co.* he owns and chairs) already embedded in the heart of the political-economic decision process—while the majority of the local population had no access to the fruits of economic development, and experienced a stagnation or a diminution of their living standards, due to increase of costs.[10] The dismantlement of the Ministry of National Economy in March 2011 and the announcement of social and economic measures (such as the creation of public sector jobs for nationals; the sharp increase of public allowances or of salaries in public and private sectors) that openly contradict the liberalisation policies implemented for a decade illustrates the dilemma in which the Omani leadership finds itself. The fundamental question regarding the regime's future relates to the political-economic conflict of interest at the top levels in the country, i.e. the fact that the business elite is in charge of economic policies. While this elite has held the levers of power since 1970 and has predominantly benefited from the oil rent, this oligarchic pact has become unacceptable for a new generation who are calling into question the whole economic structure on which authoritarian Oman has relied under Qaboos.

In Bahrain, except some isolated cases who sympathised with the protesters in 2011, business actors have constantly reasserted their proximity with the regime and the necessity to preserve the stability of the country – as an allusion to the protesters considered as troublemakers. In a statement on 11 May 2011 referring to the Peninsula Shield Force military intervention in Bahrain, the Chamber of Commerce and Industry (BCCI) explained that "due to the timely measures taken by the leadership and the support of neighbouring GCC countries to ensure security and stability in the country, the [national] economy is back on track."[11] A few days earlier, it had called on "all business enterprises and owners in Bahrain" for a complete boycott of trade with Iran to

[10] For more details on the Arab Spring in Oman, and the socio-economic unrest in Sohar since 2011, see Marc Valeri, "Simmering Unrest and Succession Challenges in Oman," *Carnegie Paper*, January 2015.

[11] Bahrain Chamber of Commerce, "BCCI's Call for Consolidated Efforts to Revive the Economy," 11 May 2011. Available at http://www.bahrainchamber.org.bh/en/ViewNews.aspx?nid=601.

protest against Tehran's alleged fuelling of unrest in Bahrain.[12] Even more, the massive crackdown that followed the protests in 2011 has once again changed the balance among the ruling family, and proven successful in marginalising the less uncompromising component of the Al Khalifa, around the Crown Prince and the EDB, in favour of the Prime Minister and his supporters, first among them the Chamber of Commerce and the business elite. Both the EDB-led reforms until 2011 and the new balance of power among the Al Khalifas since then have confirmed that the royal family is still the decisive economic and political force. Contrary to Oman, where the ruler cannot rely on his small family and has allied with the merchant elite, which has been given political positions to secure public contracts and determine long-term economic policies, the Bahraini business sector has to press for its interests in dealing carefully with the evolving balance of power among the ruling family. It has to make use of the divisions within it in a much more tactical and noisier way than it is the case in Oman, where the 2011 protests and the widespread social frustration have not put an end yet to the direct interference of the bourgeoisie in the decision-making process.

In the UAE, it was not surprising not to see any business elites signing the petition submitted in March 2011 to the government by 100 intellectuals demanding more legislative power to the elected Federal National Council. These elites sided with the government and, if anything, showed more support to the leadership than before. Business elite continue to benefit from the status quo, and support the government's economic and political policies. This pattern of state-business relations remains a prominent feature in the UAE – and to an even wider extent in Qatar, where the ruling family controls directly or indirectly the vast majority of the emirate's economy and where non-Al Thani business elite content themselves to adapt and jump on the bandwagon. In Kuwait, where members of the merchant families historically played a significant role in reform movements, especially before the independence, the business sector has unambiguously sided with the regime since 2011 to oppose any popular demands which could alter the political status quo, and as a consequence, damage their rent-seeking interests.

[12] Sandeep Singh Grewal, 'Boycott Iranian Products,' *Gulf Daily News* (1 May 2011). BCCI treasurer 'Uthman Sharif said this call "reflects an economic decision highlighting [the BCCI's] support to the Bahrain government and rulers."