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Gulf Arab Financial Flows and Investment, 2000-2010: Promises, Process and Prospects in the MENA Region

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Abstract

The Gulf Arab countries were promoted as dynamic, rapidly growing and self-transforming economies in the boom years of the 2000s, and were praised for their purported leadership of the MENA regional economy. As of 2010, despite the severity of the financial crisis and recession of 2008-2009 in the Gulf and consequent impact on the rest of the region, the GCC countries were still promoted as potential leaders of both the recovery and future regional development. An examination of the evidence regarding the direction, magnitude and uses of GCC financial flows both domestically and internationally from 2000 to 2010 finds that the investment programs in place in the boom years provided outcomes that only weakly fulfilled these promises and that they barely fulfilled them at all during the economic crisis and recovery. The author's assessment is that GCC-sourced investment since 2008 mainly addressed the Gulf region's internal development project, although even that seemed dependent on continued high levels of hydrocarbon revenues, and did little to demonstrate the promised leadership of the regional economy by the GCC.

KEYWORDS: foreign direct investment, regional integration, political economy

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During the boom years of the 2000s, the six Arab countries of the Gulf Cooperation Council (GCC) gained a reputation as dynamic, rapidly growing and self-transforming economies. In contrast to the resource-curse cycle of the 1970s and 1980s, they invested relatively more, and consumed less, of their windfall hydrocarbon revenues. Investment entailed more internal diversification, with large infrastructure projects, downstream hydrocarbon spin offs, new non-hydrocarbon-dependent industries, and the nurturing of private sectors (Khamis and Senhadji 2010b: 50). By 2010, these private sectors appeared collectively to be dominated by an elite pan-GCC private capitalist class, a set of conglomerates that superseded traditional state-dependent commercial families, forming private equity funds and spreading investment over many sectors (Hanieh 2011: 2, 140-145).[1]

Gulf-based public and private funds were also credited with successfully diversifying their overseas portfolios to spread risk geographically in both Western and emerging markets, including the MENA region (Mohieldin 2008; Samba 2008; IIF 2007). Investment in the MENA region was elevated by some analysts, including those writing for the International Monetary Fund and the World Bank (IFIs), to the GCC's assumption of a "pace-setting" leadership role in the regional economy (e.g., Khoury and Wagner 2010: 23). Under the influence of what he dubbed "Khaleeji capital," even a more critical analyst concluded that, "The entire Middle East is increasingly moving to a single beat – inextricably linked to the rhythms of accumulation and class formation in the Gulf" (Hanieh 2011: 148). During the crisis and recovery of 2008-2010, authorities continued to praise GCC-based capital's purported leadership and beneficial impact and its potential for leading the regional recovery and future economic growth (e.g., World Bank 2010a: 1).[2]

This paper reviews the regional growth record for the 2000s, the sources of that growth, and the various streams of finance flowing into and out of the GCC through the boom, crisis and recovery, including both liquid capital and, most focally, foreign direct investment (FDI). The analysis finds that much more international capital, including FDI, flowed into the GCC than flowed out from the GCC to the region in the 2000s. The last two sections, on the financial crisis, recession and recovery, assess the impact of GCC-sourced public and private investment on the region's economies through 2010 and its potential to lead future regional growth. Were the emperor's new clothes just a passing fad or did they initiate an enduring trend in a newly-refashioned regional economy?

[1] See Tabet and de Saint-Laurent 2011 for a comprehensive review of Gulf-based and other private equity funds operating in the Mediterranean through 2010.
[2] See World Bank 2010b: 11-12, 144-145; IMF 2010a and 2010b; Khamis and Senhadji 2010a and 2010b; Burke and Bazoobandi 2010; Iradian 2009; Farrell and Lund 2008, Eid 2008 75, 77.

The Growth Era, 2000-2008

Between the 2001 recession and the 2008 financial crisis in the West, the global economy expanded rapidly, and, for the most part, MENA economies grew in tandem. Figure 1a portrays the real GDP growth rates of the GCC-6 economies in those years with projections to 2012. Qatar is an outlier from 2005 on due to rapid growth of its natural gas industry, but part of Qatar's growth, like that of the rest of the GCC, came from the use of surging hydrocarbon revenues to create large public domestic investment programs and to stimulate private sector development. Figure 1b compares the averages of GCC growth rates with the averages of two groups of "developing" (also called "diversified") Arab Mediterranean countries, those of the eastern and North African groups, and to Turkey and Israel, generally considered to be the two most "developed" of the regional economies. Especially after 2003, the growth rates appear to fluctuate in tandem.[3]

Strong regional growth in the 2003-2008 period was fed by export revenues, remittances, revenues from tourism and other services, and a surge of investment**.** Figure 2 indicates that the annual additions of international reserves to the developing countries of the region, such as Egypt and Jordan and not including the GCC, increased by a factor of about 3.8, while workers' remittances increased by a factor of 2.2. The build up in reserves came from the boom in hydrocarbon and other exports, including manufactured exports, and the rise in remittances was due to increased demand for emigré labor in the growing economies of host countries in the region and in the West. Furthermore, net equity inflow, mostly accounted for by foreign direct investment (FDI), rose by a factor of 6.2, from $4.2 billion in 2002 to $26 billion in 2006 (World Bank 2009a: 128, Table A10). From 2000 to 2007, according to World Bank calculations, MENA's investment to GDP ratio increased by five percentage points and capital deepening accounted for two-thirds of the growth in potential output in the region, placing MENA in the middle, as opposed to the bottom, of the developing country range for the first time (World Bank 2010b: 6-7).

In interpreting the data depicted in Figure 2, which includes net financial inflows from all sources, a World Bank document waxed enthusiastic about the origins and purposes of GCC investment, giving the impression that the GCC was primarily responsible for the inflow of FDI to these countries (World Bank 2009a: 128). However, this impression overstates the commitment of GCC capital to the region and the quality and sustainability of the GCC-sourced FDI that did materialize.

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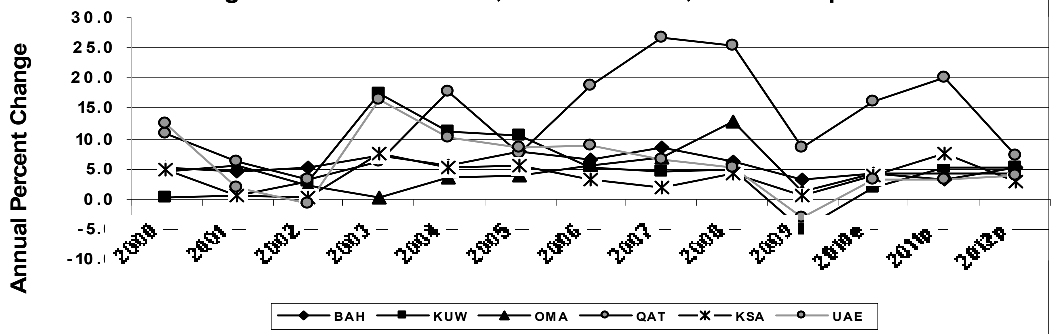
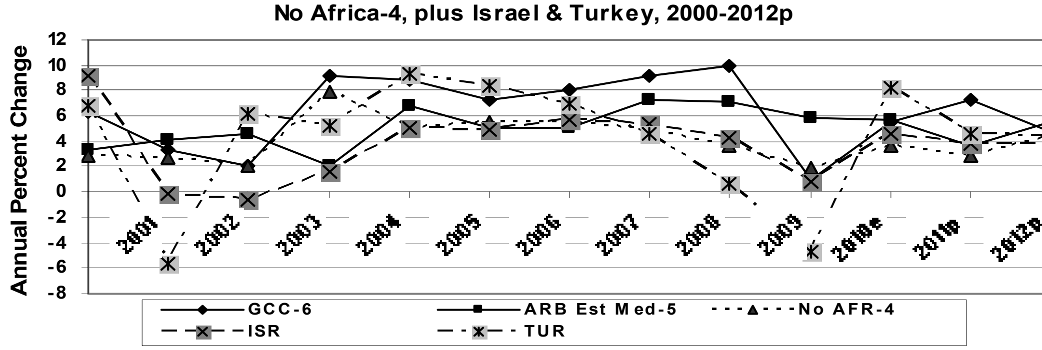
[3] Israel and Turkey were more integrated than other Mediterranean economies with both the financial and commodity sectors of the West, and so suffered more from the 2001 recession than did their neighbors.

Fig 1a. Real GDP Growth, GCC Countries, 2000-2012p



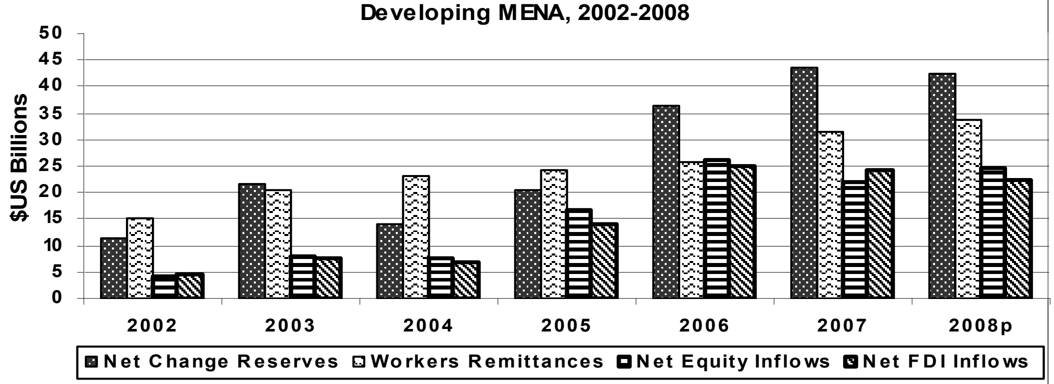
Source: International Monetary Fund, 2011b. World Economic Outlook Database

Fig 1b. Real GDP Growth Rates: Averages of GCC-6, Arab East Med-5, No Africa-4, plus Israel & Turkey, 2000-2012p



Source: International Monetary Fund, 2011b. World Economic Outlook Database
Note: GCC-6 includes Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and United Arab Emirates; Arab East Med-5 includes Egypt, Jordan, Lebanon, Syria and West Bank Gaza; North Africa-4 includes Algeria, Libya, Morocco and Tunisia

Fig 2. Net Capital Flows: Reserves, Remittances, Equity, FDI: Developing MENA, 2002-2008

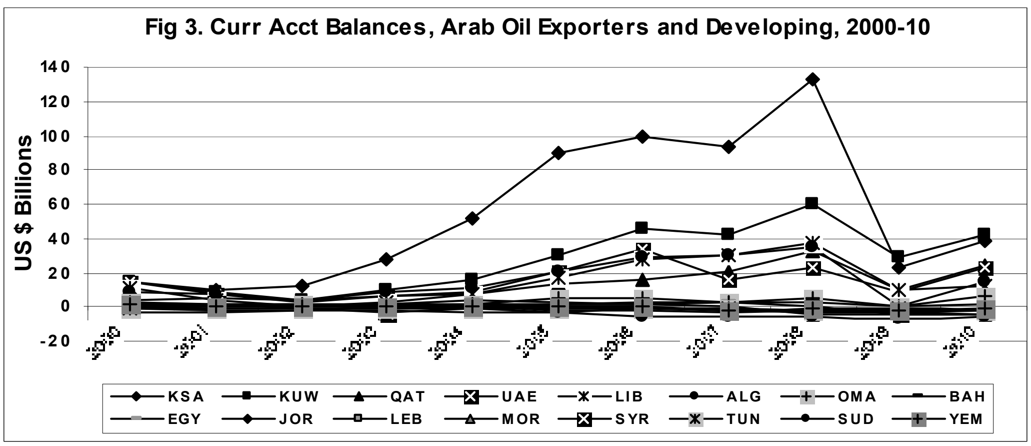


Source: World Bank 2009. Global Development Finance: 128, Tab A10
Note: Net FDI Inflow is Subset of Net Equity Inflow

Liquid Capital Flows

Changes in Current Account Balances (CAB) and Uses of Surpluses

All significant hydrocarbon exporters in the MENA region experienced rising current account surpluses in the 2000-2008 years, followed by a sharp drop in 2009 and a partial recovery in 2010. Figure 3 displays the CABs of 16 Arab countries, eight hydrocarbon exporters and eight "developing" or "diversified" economies, showing the great advantage of the former over the latter when hydrocarbon prices were high. The Top Four, namely Saudi Arabia, Kuwait, Qatar and the UAE, together had a cumulative surplus of over US$ one trillion from 2000 to 2008. One portion of these funds was used to service debt and augment domestic investment, much of which relied on imported inputs. A second portion was exported for overseas investment by both publicly owned sovereign wealth funds (SWFs) and private investment companies or individuals, including foreign direct investment outside and inside the region. A third portion was siphoned off into illicit financial outflows.



Source: International Monetary Fund, 2011b, World Economic Outlook Database

Net Changes in International Debt

Despite this unprecedented surge of surplus capital, the GCC countries borrowed on world capital markets. Figure 4a indicates that none of the GCC countries paid down debt, and, indeed, several added to it in those years in order to finance infrastructure and other projects that were among the largest in the world (IIF 2007: 6). In contrast, Figures 4b and 4c show Egypt, Jordan, Syria, and to a lesser degree Tunisia, Libya and Yemen, reducing their debt relative to GDP in those

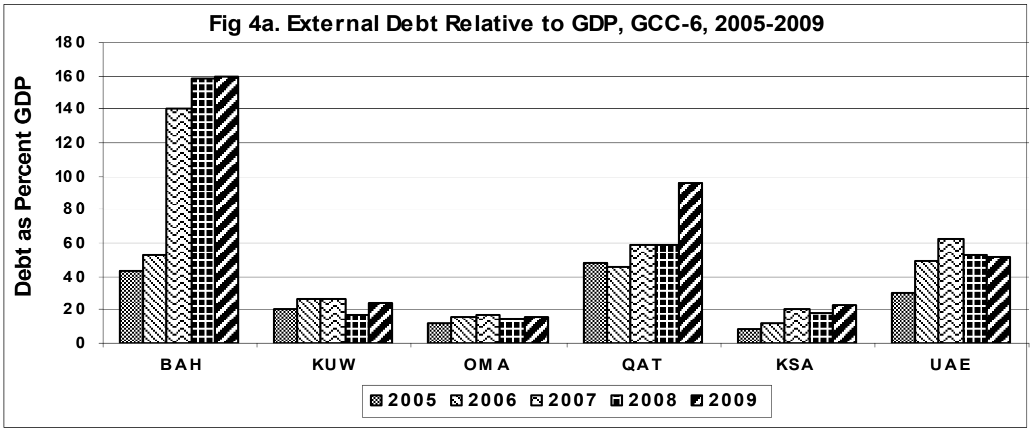


Fig 4a. External Debt Relative to GDP, GCC-6, 2005-2009

Source: Dhaman 2010: Country Fact Sheets

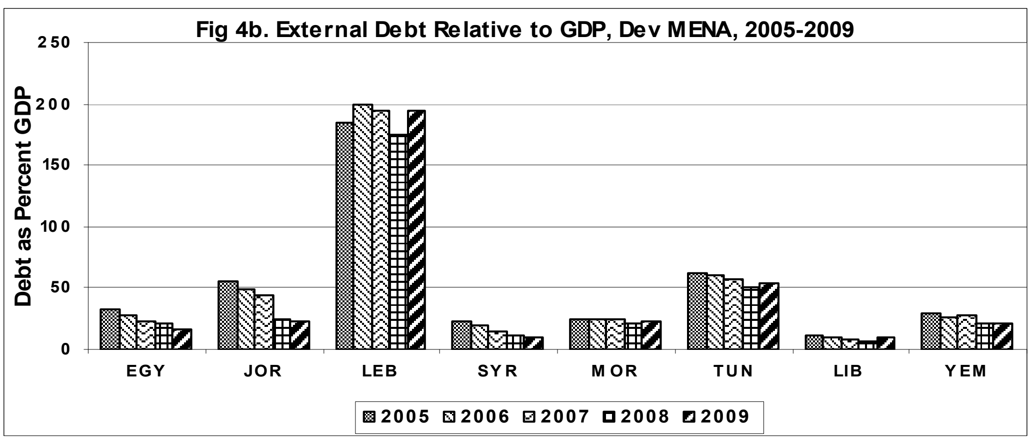


Fig 4b. External Debt Relative to GDP, Dev MENA, 2005-2009

Source: Dhaman 2010: Country Fact Sheets

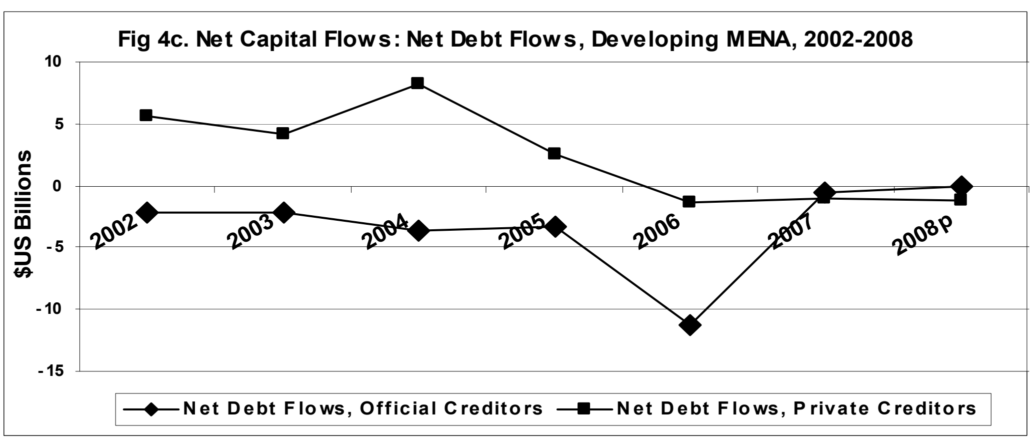


Fig 4c. Net Capital Flows: Net Debt Flows, Developing MENA, 2002-2008

Source: World Bank, Global Development Finance 2009: 128, Table A-10
Note: Negative Value Indicates Greater Outflow (repayment) than Inflow

years. Lebanon's external debt is overstated here because a large part of the debt was held locally in foreign currencies.[4]

Outflows of GCC Capital to the Rest of the World

A report by the Samba Financial Group[5] estimated the cumulative value of the GCC's current account surplus from 2003 to 2008 to be $US 911.6 billion, of which the traceable net asset holdings rose from $170 billion to $544 billion, leaving $368 billion unaccounted for (Samba 2008). The traceable funds were tracked into three types of foreign asset holdings each year: deposits with the Bank for International Settlements (BIS) used, for example, to pay for imports, U.S. financial claims such as Treasury bonds, and FDI. Over these years, the share to BIS deposits declined from 38 to 14 percent, while holdings of U.S. securities rose from half to two thirds, and FDI outflows rose from 7 percent to 20 percent. About $120 billion of the FDI went to other parts of the MENA region (Samba 2008: 11-12).

While $120 billion of GCC investment in the region was unprecedented and suitably heralded, it was small relative to the amount of petrodollars sent to the West, indeed two-thirds to the United States alone. The $450 million the GCC invested in U.S. securities from 2003 to 2008 was almost 60 percent greater than the $285 billion total FDI, from all sources put together, that was invested in the MED-13 economies in those years.[6] In one dramatic example, investors from Abu Dhabi and Qatar spent US$12 billion in a single transaction in October 2008 to purchase 16 percent ownership in Barclay's Bank, one of the U.K.'s crisis-stricken financial institutions (Samba 2008: 14), 20 percent more than the $9.5 billion in FDI that flowed into Egypt in the whole year 2008. This performance compares poorly to the standards for intraregional investment elsewhere. In 2003, for example, members of the EU invested 75 percent of total FDI in their own region and countries in the Integrating Asia Sixteen group (IA-16) invested 64 percent of their total FDI in their own region (Capannelli et al. 2009: 7-8).[7]

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[4] By 2007 the MENA region showed the second best performance of all developing regions (after East Asia and Pacific region) in terms of debt relative to GDP and current account balance relative to GDP and the lowest inflation rate of all developing regions (World Bank 2010b: 5). On Lebanon, thanks to Ghassan Dibeh for the clarification, and see IIF 2011: 27 for more detail

[5] The Samba Financial Group is located in Riyadh, Saudi Arabia. Besides its financial business operations, it gathers data and composes reports for the Institute of International Finance.

[6] The "MED 13" rubric includes the economies of the southern and eastern rim of the Mediterranean Sea: Morocco, Algeria, Tunisia, Libya, Egypt, Israel, Jordan, the Palestinian Territories, Lebanon, Syria, Turkey, Cyprus and Malta. When Cyrpus and Malta are excluded, because they joined the EU in 2004, the group is the "MED 11." When Turkey, which became a candidate to join the EU in 2004 is excluded, the group is the "MED 10." The "Med 10" is also sometimes used when Turkey is included but the Palestinian Authority or Libya is excluded.

[7] The "EU-15" were the members of the European Union at the end of 2003, namely Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, the

Capital Flight

The untraceable portion of the GCC's current account surpluses from 2003 to 2008, $368 billion, is surmised to have fled the region in favor of private bank accounts abroad, what the project for Global Financial Integrity (GFI)[8] labels "illicit financial flows" (IFF).[9] The total amount of IFF for a given year is estimated from discrepancies in balance of payments accounts and is suspected to be due to siphoning off of hydrocarbon export revenues and trade mis-pricing, meaning over-invoicing of imports and under-invoicing of exports (Kar and Curcio 2011: 3-7). Popularly known as "capital flight," illicit financial outflows represent a drain on the capital available for investment within a country and thus retard economic growth. A path breaking study on the MENA region found that capital flight was a significant problem for the resource-rich economies, where it was shown to "negatively and significantly affect economic growth" (Almonsour 2008: 33-35).

The amounts of IFF estimated for the world's developing regions add up to a staggering global total of US$6.5 trillion from 2000 to 2008. Of that amount, the MENA region accounted for almost 18 percent, about $1.2 trillion. MENA's illicit outflows grew at over 24 percent per year, the highest rate of growth of IFF among developing regions (Kar and Curcio 2011:14-15). While the rest of MENA countries were not innocent, the four outstanding generators of IFF were Saudi Arabia, the United Arab Emirates, Kuwait and Qatar, MENA's "Top Four." These countries placed as numbers 4, 6, 7 and 9, respectively, among all developing countries ranked by the amount of IFF in the 2000-2008 period. Together they accounted for $957 billion of the developing countries' cumulative IFF for 2000-2008, that is, 14.7 percentage points of the 17.9 percent from MENA as a whole. These funds were thus lost to local or intraregional investment.

Figures 5a and 5b show the cumulative totals and average per year, respectively, of current account surpluses and IFF for the Top Four in comparison

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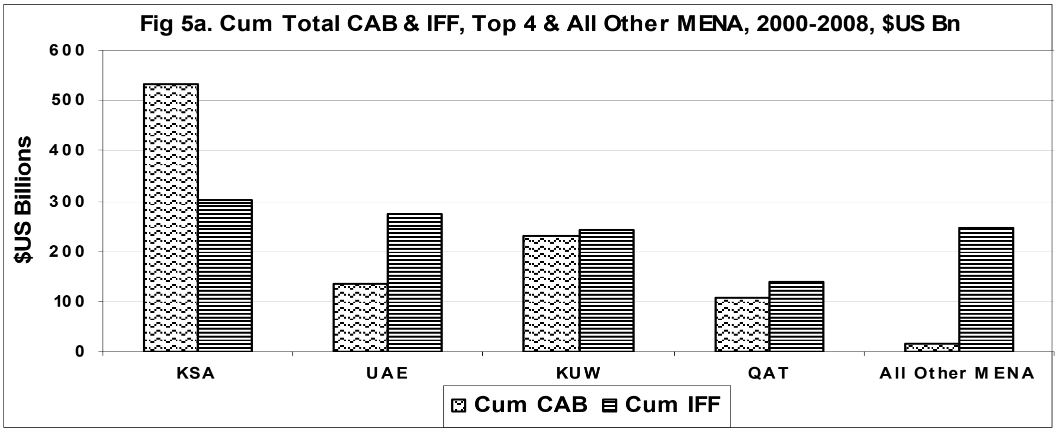
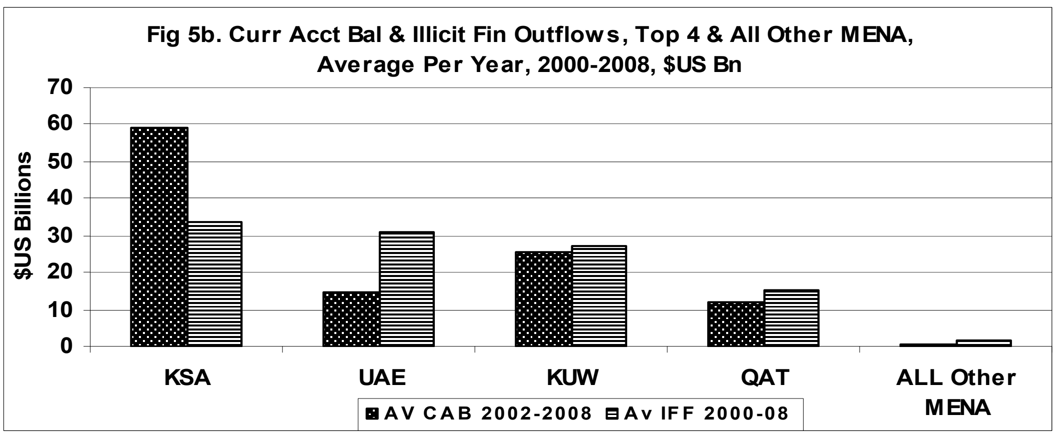
Netherlands, Portugal, Spain, Sweden and the United Kingdom, prior to the accession of Malta, Cyprus and eight central and eastern European countries in 2004. The "Integrating Asia 16" (IA-16), was composed of ASEAN nations (Brunei Darussalam, Cambodia, Lao PDR, Indonesia, Malaysia, Myanmar, Philippines, Singapore Thailand and Vietnam), plus China, Japan, South Korea, Hong Kong, India and Taipei (Capannelli et al. 2009: 1-2).

[8] The project for Global Financial Integrity is sponsored by the Center for International Policy in Washington DC, and the research was funded by the Ford Foundation.

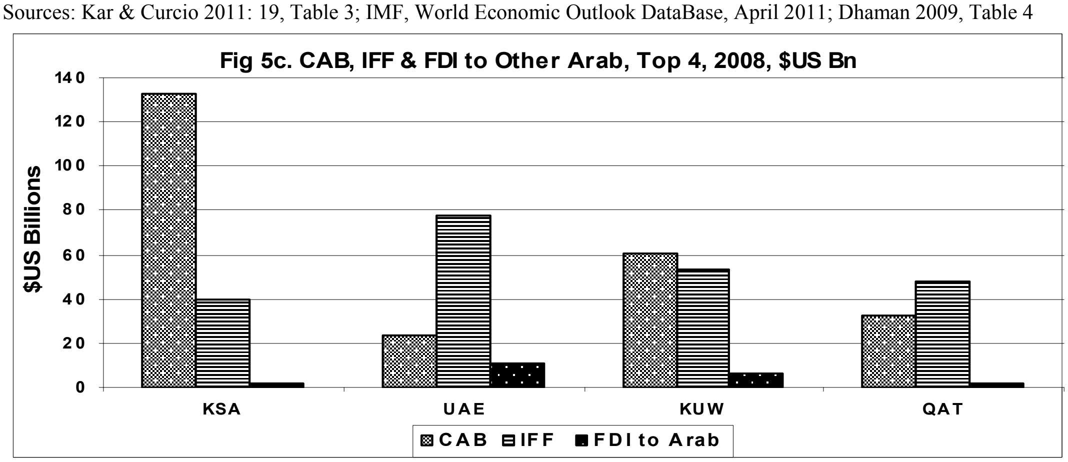
[9] "Illicit flows involve capital that is illegally earned, transferred or utilized and covers all unrecorded private financial outflows that drive the accumulation of foreign assets by residents in contravention of applicable capital controls and regulatory frameworks" (Kar and Curcio 2011: 3). The flows are not necessarily earned illegally; they are "illicit" if they are not recorded and thus enable the sender to avoid taxation or capital controls.



Sources: Kar and Curcio 2011: 19, Table 3; IMF, World Economic Outlook DataBase, April 2011



Sources: Kar & Curcio 2011: 19, Table 3; IMF, World Economic Outlook DataBase, April 2011; Dhaman 2009, Table 4



Sources: Kar & Curcio 2011: 19, Table 3; IMF, World Economic Outlook DataBase, April 2011; Dhaman 2009, Table 4

to the rest of MENA combined, illuminating the concentration in their hands of liquid capital flowing through the region. Figure 5c compares the amounts of

CAB, IFF, and Inter-Arab FDI outflow of the Top Four in 2008, illustrating how small their actual FDI was in proportion to the financial resources that could have been available for intraregional investment in that year.

Foreign Direct Investment

Why Focus on FDI

There was much excitement among both investors and international financial institutions in the 2000s boom about FDI to "emerging markets," mostly countries that had been defined previously as the underdeveloped or developing regions of the world. This excitement arose out of the conviction that FDI is more beneficial, and entails a deeper and longer-lasting commitment, to the development of these economies than other forms of capital transfer such as lending.

Policy makers in international organizations and many economists who study the MENA region (e.g. Dhaman 2010: 5; Eid 2008: 69; Iqbal and Nabli 2004) consider FDI to be especially desirable because it may introduce more sophisticated and efficient technology, bring higher productivity along with more jobs, increase the competitiveness of the host country's exports on world markets and boost absorptive capacity. While some econometric studies of regional economies support the theory that FDI leads growth (e.g., ESCWA 2011: 23-34; Bakardzhieva et al. 2010), other research has found that it is faster growth that attracts FDI (Institute of International Finance 2011: 8) or that there is an interactive or feedback effect between growth and FDI (Al-Iriani and Al-Shamsi 2007: 2; Metwally 2004: 381).

Some scholars suggested that FDI inflow to the MENA region, as compared to other developing regions, was discouraged by a set of country-level impediments, such as non-transparency, corruption, high risk due to political conflict, price inflation and remaining barriers to trade (e.g., Elafif 2009). Until these impediments could be overcome and multinational corporations began to invest in the region rather that just exporting to it, economists have suggested that the best medium-term development strategy for the region was to use its surplus capital to invest in itself, develop human resources to promote growth, and become more internally coherent and thus more attractive to foreign investors in the longer term (e.g., Khoury and Wagner 2010). Intraregional FDI would be the logical core of such a program.

The rub is that foreign investment in the MENA region is embedded in and constrained by political as well as economic relationships. Among others, the European Union (EU) and GCC both supplied FDI to the Mediterranean countries in the mid 2000s. However, European private investment was linked to the EU's several successive Euro-Mediterranean partnership projects, with complex agendas entailing security, migration-control, and cultural and political components in addition to aid and economic development (Schumacher 2010; Del Sarto and Schumacher 2005). In 2011, the Arab Spring inspired renewed efforts by the GCC to cooperate with the EU on the economic as well as the political front to "ensure that these countries [with new regimes] return to a forward path of economic and social progress" (i.e., neoliberal economic reform) and to underline that the GCC is "promoting security and stability both in its immediate neighborhood and the wider Middle East" with its political and strategic commitments (Sager 2012).

How exactly, then, did FDI into and within the region contribute to, or interact with, economic growth in the 2000s?

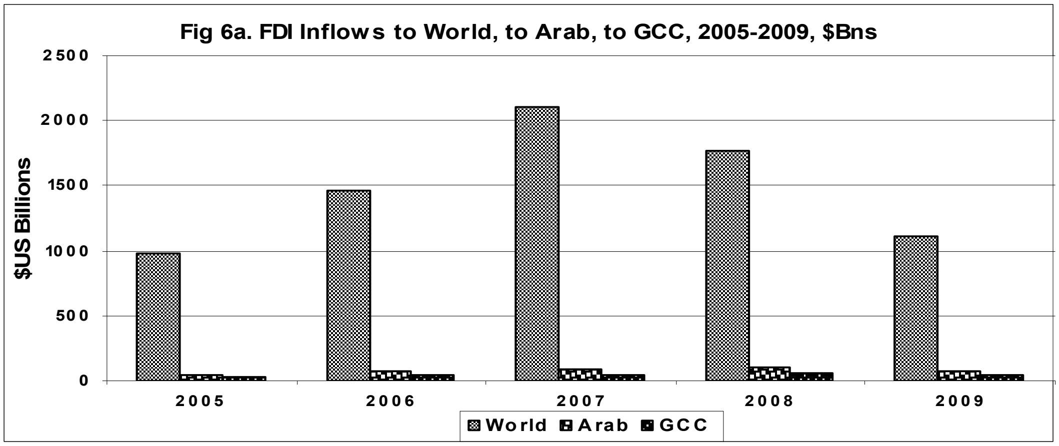
Global FDI Inflow to the Larger MENA Region and its Sub-regions

Foreign direct investment to MENA from the world as a whole rose in tandem with the global boom in FDI to emerging economies in the mid 2000s. ESCWA data indicate that these flows to the West Asia region[10] rose from US$ 40 billion in 2005 to over $84 billion in 2008. Through the crisis years, West Asia received a rising share of FDI to the world, from 3.3% in 2007 to 4.8% in 2008 to 6.5% in 2009. Its share of inflows to all developing regions also rose, from 12.4% in 2007 to 13.4% in 2008 and 15.2% in 2009 (ESCWA 2010: 2; 2009:2). Defining the "region" somewhat differently, as Dhaman does, yields a similar picture, with the Arab countries as a group[11] commanding a rising share of global FDI over the 2000s. FDI to the Arab region in 2007 was 4.1 percent of FDI to the world and 15.3 percent of FDI to developing regions, and in 2008 5.7 and 15.5 percent, respectively. Furthermore, when FDI to the world decreased by 38.7 percent from 2008 to 2009, FDI to the Arab region decreased by just 17.7 percent (Dhaman 2010: 12, 14).

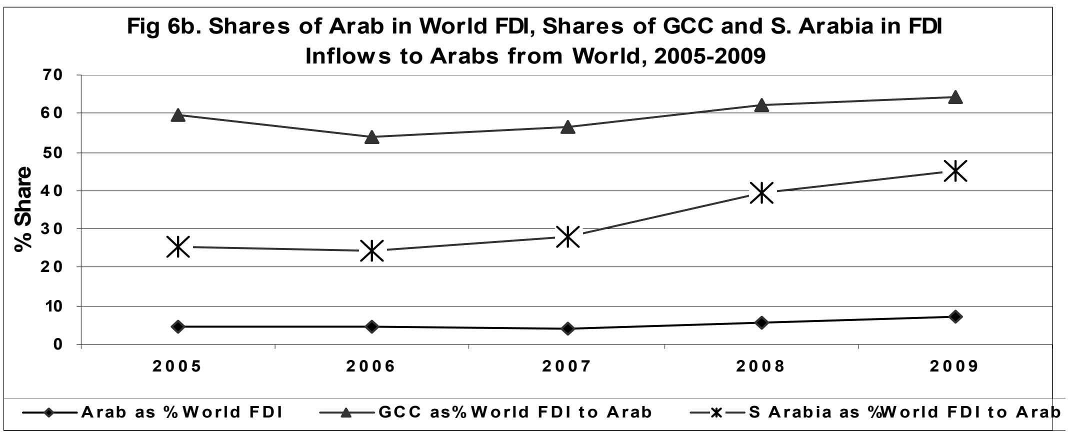
The major beneficiaries of this inflow were not the developing countries of the region, but rather the wealthiest hydrocarbon exporters. Figure 6a shows the growth of global FDI from 2005 to 2009, the share of global FDI that went to the Arab countries and the share that went to the GCC countries in particular. The GCC countries, with 10 percent of the Arab countries' population, about 40 million people including resident non-citizens, received around 60 percent of the global FDI that flowed into the Arab region from 2005 to 2009. As seen in Figure 6b, Saudi Arabia was by far the biggest single recipient, averaging about one-third of global FDI inflow per year (Dhaman 2010: Table 6).

[10] "West Asia" includes the GCC countries plus Lebanon, Syria, the Palestinian Territories, Egypt, Sudan, Jordan, Iraq and Yemen.

[11] For Dhaman's purposes, the Arab region includes all of the Arab countries of West Asia plus those of North Africa and other predominantly Arabic-speaking African nations, namely Morocco, Algeria, Tunisia, Libya, Mauritania, Djibouti and Somalia.



Dhaman 2010: Series "Direct Investment Inflows," http://www.iaigc.net/?id=7&sid=21



Source: Dhaman 2010: Series "Direct Investment Inflows," http://www.iaigc.net/?id=7&sid=21

Inter-Arab FDI

Saudi Arabia was also the leading recipient of one definition of intraregional investment, namely investment among the Arab countries. As shown in Figure 7a in dollar amounts, and Figure 7b in percentage shares, Saudi Arabia received the single largest share of inter-Arab flows of FDI from 2005 to 2009, even during the crisis. In 2009, total inter-Arab FDI dropped by 36 percent from its peak in 2008, but, of that smaller amount, more than half went to Saudi Arabia, allowing its dollar inflow to drop by just 9 percent (Dhaman 2011: Tables 3 and 4). It was also the single largest recipient of GCC flows. In 2008, 55 percent of UAE, 56 percent of Bahraini and 68 percent of Kuwaiti inter-Arab FDI went to Saudi Arabia. In 2009, these shares tended to be even larger, with 75 percent of UAE, 65 percent of Bahraini and 70 percent of Kuwaiti inter-Arab FDI going to Saudi Arabia (Dhaman 2010: Tables 3 and 4; 2009: Table 4).

Even among inter-Arab investors from the eastern Mediterranean, FDI flow favored Saudi Arabia, which won 44 percent of Syrian, 64 percent of Palestinian, and 68 percent of Jordanian inter-Arab investment in 2008.[12] Only Lebanese and Egyptian capital favored other developing countries in 2008, with 82 percent of Lebanese inter-Arab FDI going to Sudan (mostly banking) and 85 percent of Egyptian inter Arab FDI going to Algeria (a cement plant). In 2009, Saudi Arabia was even more favored, winning 98 percent of Syrian, 89 percent of Palestinian, 88 percent of Egyptian, 73 percent of Jordanian and 57 percent of Lebanese inter-Arab FDI (Dhaman 2010 and 2009: Table 4).

Furthermore, Saudi Arabia took in much more inter-Arab FDI than it put out. In 2008, it took in $13.0 billion but sent out just $2.1 billion. In 2009, it took in $11.6 billion, but sent out just $1 billion. Figure 8 shows the origins of inter-Arab FDI, in dollars, by source. In 2008 and 2009, the most important sources were Kuwait and the UAE, with Saudi Arabia ranked sixth. In 2008, it was surpassed by, surprisingly, Egypt, Oman and Lebanon, and, in 2009, by Bahrain, Qatar and, again surprisingly, Jordan (Dhaman 2010 and 2009, Table 4). Saudi Arabia in particular, as well as the GCC in general, had come to be a magnet for FDI from all sources.

The GCC and Saudi Arabia as Magnets for Extra- and Intra-Regional FDI

Given the shift of strategy toward productive investment of part of capital surpluses in the 2000s, the GCC had come to be treated by some enthusiastic analysts as a vibrant, rapidly developing and increasingly integrated single economy, expected to become an "economic powerhouse" by 2050 (Akarli 2008: 47-51, 57-58, 64). With a joint population of about 40 million and a collective GDP of more than a trillion dollars in 2010, as well as net assets of at least one trillion dollars, the GCC was portrayed as a "natural hub" for finance, commerce and transportation linking three continents, a beacon of progressive economic policies and political stability surrounded by a "natural economic hinterland" of 300 million people in a region "beset by political instability and low growth" (Toksov 2008: 81-87, 93-94).[13] In the late 2000s, both internal and pan-GCC investment plans entailed ambitious projects for heavy industry, physical infrastructure such as ports, highways, railroads, and whole new industrial and residential cities. By 2010-2011, proposals included alternative energy, such as wind and solar, a region-wide electricity grid that could be extended to other parts of MENA and beyond to Europe and Asia, telecommunications networks,

[12] Indeed, Jordan put out more inter-Arab FDI in 2008, $0.9 billion, than it took in, $0.4 billion, while Lebanon issued almost as much as it took in, $2.3 billion versus $2.6 billion.

[13] The IFIs also treated the GCC as a freestanding unit separate from the rest of the region. In their 68-page study, Khamis and Senhadji (2010a) did not once mention intraregional investment as part of the GCC's past activity, current program or future planning.

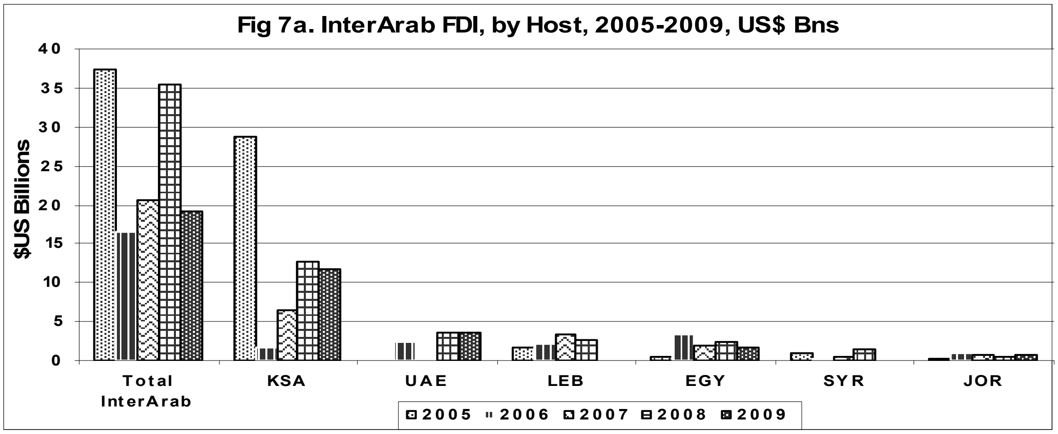


Fig 7a. InterArab FDI, by Host, 2005-2009, US$ Bns

Source: Dhaman 2010: Series "InterArab Direct Investment Inflows," http://www.iaigc.net/?id=7&sid=21

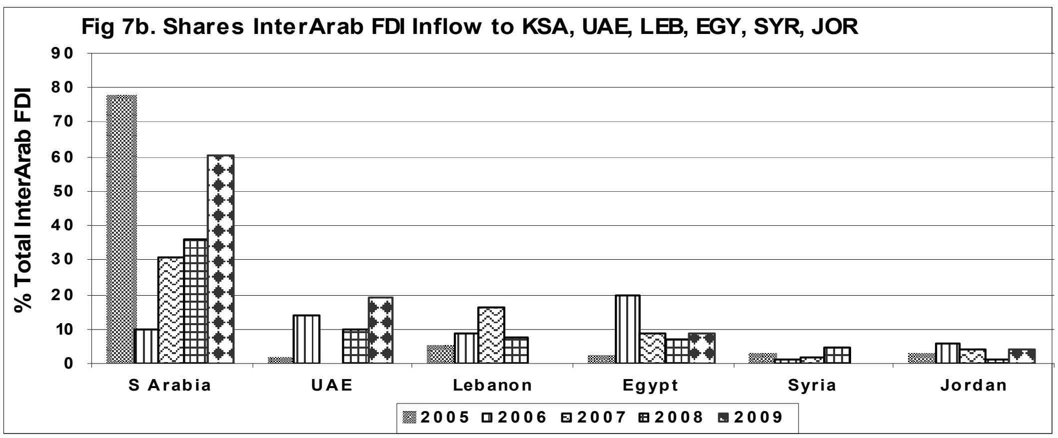


Fig 7b. Shares InterArab FDI Inflow to KSA, UAE, LEB, EGY, SYR, JOR

Source: Dhaman 2010: Series "InterArab Direct Investment Inflows," http://www.iaigc.net/?id=7&sid=21

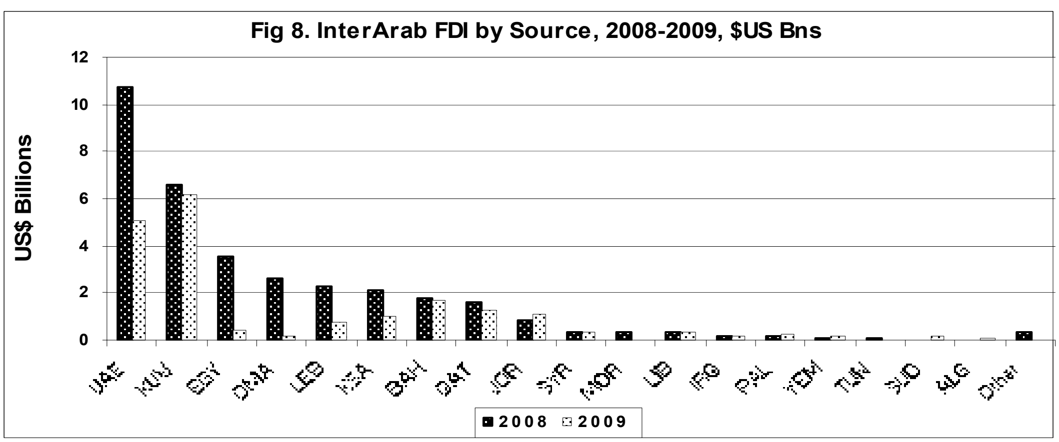


Fig 8. InterArab FDI by Source, 2008-2009, $US Bns

Source: Dhaman 2009: Table 4, 2010: Table 4; Note: Countries Ordered by Outflow 2008 residential construction, including affordable as well as luxury housing, social infrastructure and the subsidization of private enterprise initiatives in manufacturing, real estate and services (Toksov 2008: 84-87).[14]

As the biggest and leading economy in the GCC, Saudi Arabia became attractive for FDI from many sources in the 2000s. Whereas its outflows and inflows were more balanced in the 1990s, Saudi cumulative inflows in the 2005-2008 boom years totaled $US 93.2 billion, while outflows were just $US 15.5 billion (UNCTAD 2009: Country Fact Sheet, Saudi Arabia). In 2008 the sources of 44 percent of existing FDI stock were firms from the United States, Europe and Japan, while 13 percent had come from the UAE and 9 percent from Kuwait. These sources remained important for FDI inflow in 2009, but China, Russia and Malaysia all moved up in source ranking (SAGIA 2010b: 7-8), an indication of the expanding role of non-Western, non-Arab capital in the region. While real estate took 21 percent of FDI, reflecting internal diversification, energy-intense sectors remained a big draw, as hydrocarbon and related industries -- mining, oil, gas, refining, chemicals and petrochemicals -- accounted for 41 percent of FDI in 2008 (ESCWA 2009: 5). As one admirer claimed, "Saudi Arabia is set to become a heavy industry base for the region… Current plans… envisage that by 2020 the country will supply 15 percent of the world market for aluminum and plastics" (Toksov 2008: 81, 84- 87).

The Saudi Arabian Government Investment Authority (SAGIA) addressed its appeal to potential foreign investors in terms of such diversified opportunities and its accommodating environment. With rising scores on the World Bank's "competitiveness" and "doing business" indices (Dhaman 2010: 19-20), Saudi Arabia ranked eighth in the world for FDI inflow in 2009.[15] As SAGIA's website put it, "Saudi Arabia is undertaking aggressive reforms and investments to become one of the world's Top 10 most competitive economies by 2010… It's [also] about unfettered access to regional markets and financial services." This promotion offered investors easy credit, high consumer confidence and growing domestic demand, comprehensive public infrastructure investment, and low-cost access to fuel and feedstock for energy-intensive industries in four new planned cities. It also promised a high quality of life for expatriate families living in the country's "famous compounds," with "first-rate international schools" and "state of the art health facilities." Under "Key Benefits," SAGIA also compares Saudi Arabia favorably to other GCC countries and to Egypt, showing that, in 2008,

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[14] See http://corp.gulfinthemedia.com/gulf_media for many examples from Gulf news outlets.

[15] See, for example, Khalil Hanware, "Saudi Arabia's Ability to Attract FDI Becomes a Big Success Story," *Arab News*, Jan 25, 2011; and S.H. Moulana, "Saudi Arabia Breaks into Top 10 for FDI," *Asian Tribune*, July 24, 2010 (http://arabnews.com/economy/top_100_fdi/article242771.ece; http://www.asiantribune.com/news/2010/07/24/saudi-arabia-breaks-top-10-fdi)

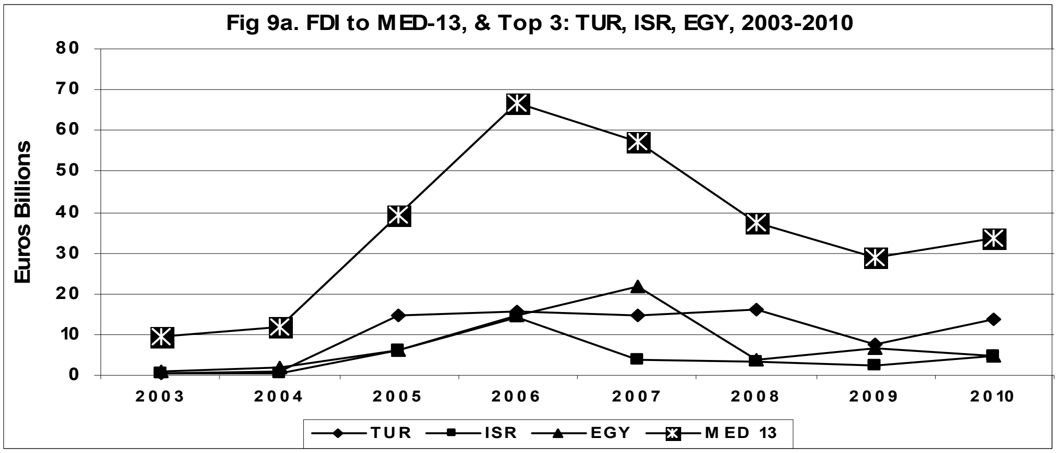
Saudi expenditure on education was 50 percent greater as a percent of GDP and its real aggregate GDP 2.4 times larger than were Egypt's (SAGIA 2010a).

There were two constraints that the SAGIA promotion did not mention. First, the core industries in Saudi Arabia were kept in the hands of state enterprises, usually in the form of joint ventures with transnational corporations or Khaleeji conglomerates, and were not open to independent foreign investment (Hertog 2010: 177-178). Second, the 2008-2009 crisis depressed both domestic and foreign investment, as about 23 percent of $2 trillion worth of domestic projects were suspended or cancelled (IIF 2009: 3; ESCWA 2009: 5). In the face of overcapacity in productive sectors and oversupply of real estate in Qatar and the UAE, as well as debt-servicing problems and some major defaults (see "Financial Crisis" below), Saudi and other GCC private sector investment remained subdued in 2010. FDI into Saudi Arabia decreased in 2009 and 2010, by a cumulative 26 percent from its peak in 2008 (Dhaman 2011: Country Fact Sheet Saudi Arabia). What FDI was flowing into Saudi Arabia in 2010 was not due to a booming private sector but rather a response to old familiar stimuli, namely, high prices and growing profits from the hydrocarbon and related sectors, and guarantees of sovereign backing and public partnerships for the reduced number of projects in which foreign firms were still likely to be interested.

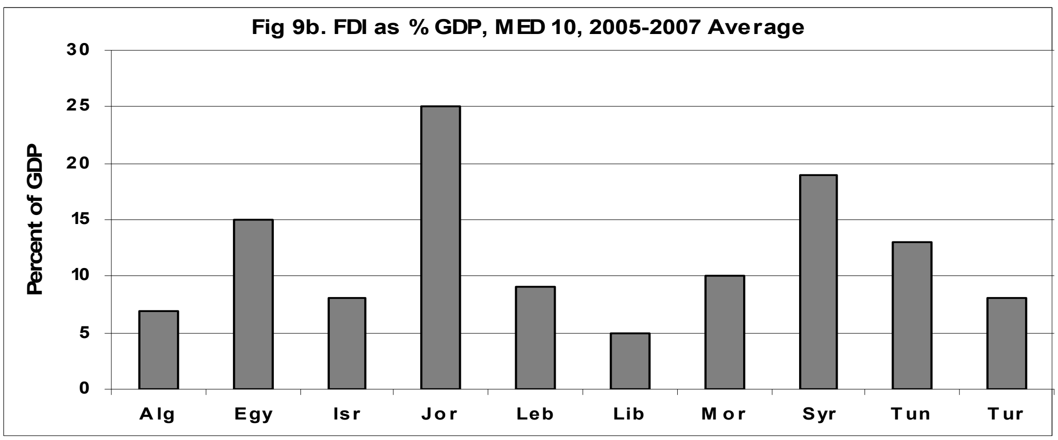
Magnitude of GCC FDI to the Mediterranean in Comparative Perspective

While FDI to the developing countries of the region in the 2000s, and especially GCC FDI, was widely celebrated, the magnitude, timing and distribution of these flows raised serious questions about their sustainability and their contribution to broad-based economic welfare. Figure 9a indicates that FDI to the 13 southern and eastern Mediterranean countries from all sources rose from Euros 10 billion in 2003 to an apogee of Euros 66.7 billion in 2006, about 4.5% of total world FDI that year (Henry et al. 2008: 10-11). Second only to China, the MED region took in more FDI in 2006 than other competing regions, including ASEAN, MERCOSUR, India and Russia (*Economist* 2008). However, FDI to the MED stopped rising two years before the onset of the 2008 financial crisis, and, by 2009, had crashed to less than half of its 2006 level.

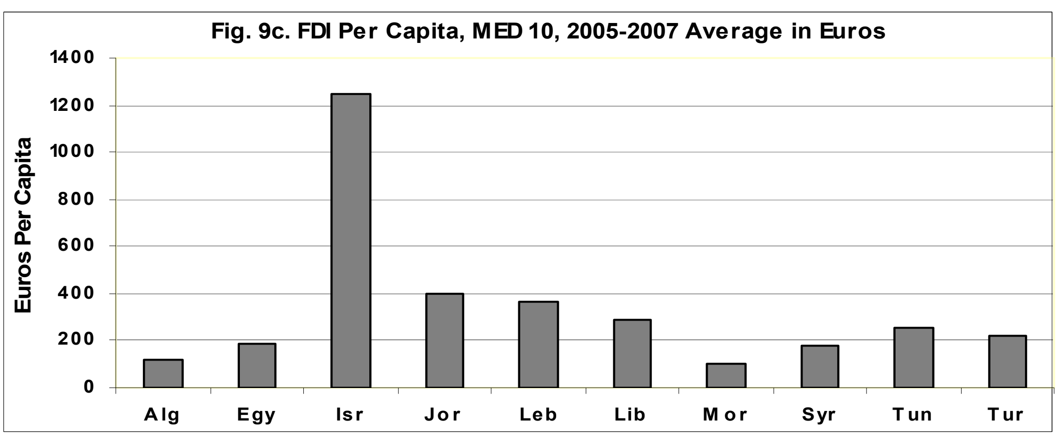
GCC-sourced investment in the Mediterranean through 2007 was less than Europe's but more than North America's. For the expansion period from 2003 to 2007, the Gulf countries provided 27.3 percent, favoring the Mashreq. The EU and other European countries provided 37.2 percent, favoring Turkey, the Maghreb, and Egypt, and North America provided 23.7 percent, strongly favoring Israel and, to a lesser extent, Turkey, Egypt and Algeria. About eight percent came from other regions of the world, with the MED countries suppling about four percent to one another (Henry et al. 2008: 153, Annex 2). The one year in which Gulf investment surpassed Europe's in both absolute and relative terms



Source: de Saint-Laurent 2011: 8, Fig 9



Source: Henry et al. 2008: 13, Fig 4



Source: Henry et al. 2008: 13, Fig 4

was 2006, the peak year for FDI to the MED from all sources, at 31 and 30 percent, respectively (de Saint Laurent et al. 2011: 10, 12).[16]

The destinations of this FDI and its magnitude relative to the host economies give some indication of its promise and limitations until the 2008 crisis. The three top recipients were Turkey 29 percent, Israel 20 percent, and Egypt 15 percent (Mishrif 2010: 135, Table 6.3). Figures 9b and 9c indicate the percentage of GDP and the per capita amounts, in Euros,[17] that FDI represented for the MED countries from 2005 to 2007. Most promising was that FDI averaged 5 percent of GDP or more for all countries in the group, with Jordan at the top, averaging 25 percent, followed by Syria at 19, and Egypt at 15. Israel received far and away the highest FDI per capita, at 1250 Euros. In this case, FDI flowed not to a needy developing country but to what was considered the most advanced economy in the region with the highest GDP per capita of the MED group,[18] illustrating that FDI was following, or at least interacting with, growth rather than leading it. GCC FDI could have helped the Arab Mediterranean economies to bring them into competitive range with Israel and to compensate for the United States' favoring of Israel. However, GCC investment was sometimes not developmentally sound and, in any case, declined in magnitude after 2008.

GCC FDI Projects in the Arab Mediterranean in Comparative Perspective

The impact of foreign direct investment can be evaluated by its contributions to development in the host country. Such contributions are the production of significant value and growth in the domestic market as well as for export, the creation of employment and linkages to related economic sectors, the spread of benefits in the population, the appropriateness of the scale of the project to the site and to the social community in which it is located, and the extent to which the announced investment is actually implemented (Luçon and Lapujade 2011: 20-28).

Led by the UAE with 52 percent, Gulf-sourced investment in the Mediterranean countries from 2003 to 2009 favored larger scale projects than did European investors and generally avoided higher-risk small and medium-size enterprises (SMEs). Gulf funds allocated 27 percent of total incoming FDI to just 16 percent of announced projects in those years, with the average amount invested per project about twice that of the European investors. Gulf investors were more likely than Europeans to undertake greenfield mega-projects in real estate (hotels,

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[16] Tabet and de Saint-Laurent 2011 Annex 1, provides a list that includes such firms, as does Hanieh 2011: 142-143, Table 5.8, and 187-202, Appendix A.

[17] When the Euro was formally inaugurated in 2000 as the common currency of most of the members of the European Union, it was set equal to the value of the US dollar. By 2008, however, its relative value had risen to a monthly average of about $1.45 per Euro.

[18] Israel's real GDP per capita in 2006 was US$ 20,792, with Cyprus a distant second at $ 14,718 and Malta third at $10,487 (http://data.worldbank.org/indicator/NY.GDP.PCAP.KD).

tourist resorts, high-end shopping malls), public works, transportation (ports and airports) and utilities (electricity, water supply). These projects created temporary jobs in construction, but, except for tourism, fewer permanent jobs and less technology transfer than the European-sponsored projects in manufacturing or in partnership with existing SMEs in, for example, the ITC sector. Furthermore, Gulf projects had an implementation rate of 43 percent, as compared to 71 percent for European investments (de Saint Laurent et al. 2009: 5-8, 10-11; Burke and Bazooandi 2010: 5-7).

Tunisia provided a case study of a proposed but never implemented mega-project, the "Mediterranean Gate" on the Lake of Tunis. This joint venture between the Tunisian government and the investment firm Sama Dubai, owned by Dubai Group Holding company, aimed to develop the southern shore of the lake into a vast commercial, residential and tourist center, taking 10 to 15 years to complete at a total cost of about $18 billion (Kerr and Wigglesworth 2011; *Wikipedia* 2011). Criticized for its grandiosity, elitism and social and ecological insensitivity, this proposal would have superimposed the Dubai urban development model on an ancient Mediterranean city with limited natural resources and absorptive capacity. Both the contract and its cancellation due to the financial crisis seem to "underline the fragility of a state such as Ben Ali's Tunisia [which was] unable to set a real strategy for its capital, but [was] eager for bribes and other forms of corruption" (Barthel 2011: 2, 10-14).[19]

GCC FDI in the region often took the form of mergers and acquisitions, as the GCC became a more important global purchaser of firms in other countries (Dhaman 2011 and 2010: Table 8). For example, two Dubai firms, including the deeply indebted Dubai Group Holding company, which had borrowed to finance its share, committed over $3 billion to purchase a 35 percent interest in Tunisie Telecom in 2006, accounting for 68 percent of total FDI from all sources to Tunisia in that year (UNCTAD 2012: 6-7). However, this entailed no investment in new productive capacity, and by early 2011 the Dubai Group was trying to liquidate its share in order to repay its creditors. Similarly, over the course of the 2000 to 2007 period, half of the incoming FDI to Egypt from the GCC went to acquisitions of existing firms rather than new projects. Some of these acquisitions were purely financial, such as that by the privately-owned National Bank of Kuwait of Al Watany Bank, one of Egypt's most successful private banks. Other acquisitions entailed purchases of privatized public sector enterprises, such as the 2007 takeover of the Egyptian Fertilizers Company by a firm from the UAE, and did not create new facilities or additional value (Henry et al. 2008).

[19] A few more positive examples had emerged by 2008, for example the Bab al-Bahr project near Rabat, also under the auspices of Sama Dubai. Although the investor had to withdraw in 2009, the Moroccan government had employed European technical advisors to negotiate a greater sensitivity to both the ecology and the social life of the community in which the project was to be sited (Barthel 2011: 14-15).

Both European and Gulf investors put a significant part of their funds into financial services like banking and insurance, 19 percent and 12 percent, respectively, and into telecommunications and the internet, each 15% (Saint Laurent et al. 2009: 5-8; *Economist* 2008; IIF 2007: 5-6) but Gulf investors also favored real estate and tourism. Lebanon, the premier example of these kinds of investment during the financial crisis, saw a rise in its intake of FDI in 2008, to $3.6 billion, almost one-third greater than in 2007. Real estate and construction together claimed over 56 percent of the total, with banking taking 20 percent and tourism 13 percent. ICT and industry came in significantly lower, at 7 percent and 3 percent, respectively. Virtually all of the FDI came to Lebanon from Gulf countries: Saudi Arabia 70 percent, Kuwait 22 percent, UAE four percent, and Qatar two percent (ESCWA 2009: 12-13), an example of exported capital alighting in what was considered to be a safe haven for bank deposits and real estate that would hold its value through a crisis.

Of total GCC-sourced inter-Arab FDI in 2008, 61 percent went to services, 28.5 percent to industry and 2.9 percent to agriculture (Dhaman 2009: Table 5). Much of the industry entailed investment that added value to the host economy, such as new infrastructure, cement and metallurgy factories, and specialized high-technology sectors like organic farming and logistics (Mohieldin 2008: 40-41). Much smaller proportions of GCC FDI were allocated to the manufacture of light industrial products and consumer goods for mass domestic consumption and to agriculture and ICT, contributing less to sustainable broad-based development than did European investors (Luçon and Lapujade 2011: 20-28; de Saint Laurent et al. 2011: 8-17; Henry et al. 2008).

Syria, Jordan and Egypt provided examples of investment in industry. Like Lebanon, Syria and Jordan experienced an increase in inflows of FDI from all sources in 2008, despite the financial crisis, and Syria saw an increase again in 2009. Industrial projects in Syria included refineries run as joint ventures with national petroleum companies from other countries, automobile assembly, and cement and paint factories, as well as services like banking, insurance, and communications. Besides Arab neighbors, including Saudi Arabia, Iraq and Jordan, and some European countries, investment came from Iran, Turkey, Malaysia, Venezuela, and, especially for petroleum refining, China (ESCWA 2011: 19-20; 2009: 17). This turned out to be part of the new growth trend in non-Western, non-Arab FDI to the region.

In 2008, 56 percent of FDI to Jordan went to manufacturing and 36 percent to tourism and hotels. Like Syria and Lebanon, but unlike Egypt, a major share of FDI in 2008, 53 percent, came from other Arab countries, in particular from the UAE at 26 percent, Kuwait 16 percent, and Saudi Arabia 11 percent, while a minor share came from the West, e.g. the United Kingdom with 29 percent (ESCWA 2009: 10-11). Unlike Syria, the manufacturing sector in Jordan that attracted the most FDI was in the enclave-style Qualified Industrial Zones

(QIZs), where most enterprises were owned by non-Jordanian firms employing non-Jordanian workers.[20] The firms produced goods like textiles and electronic components for duty-free export to the EU and the United States. In 2009, FDI from the UAE plunged, causing the share from Arab countries to fall to less than one-third, while the share from non-Western, non-Arab investors rose to 60 percent (ESCWA 2011: 16-18).[21] As in Syria and the MED countries in general, non-Western, non-Arab capital was growing as Gulf capital faded.

Named as one of the top ten global "reformers" in 2008, according to the World Bank's *Doing Business 2009*, Egypt was proclaimed the most successful of Arab Mediterranean countries in attracting FDI in general and Gulf investment in particular. FDI from all sources had risen by a dizzying factor of 26 in just a few years, from $450 million in 2003 to a peak of $11.6 billion in 2007. While more than half of Egypt's inflows of non-hydrocarbon FDI in 2007-2008 went into financial and other services, a third went to manufacturing, nine percent to real estate and construction, and the last four percent to tourism, agriculture and ICT (Mohieldin 2008: 40-41). According to one enthusiastic observer writing before the financial crisis of 2008, Egypt was "the most integrated with the GCC investment program," receiving about 40 percent of the GCC's FDI in the Mediterranean from 2003 to 2007, about $US 3.3 billion at its peak in 2006-2007.[22] During that year, Egypt also received $US 1 billion in remittances from the GCC, and Egypt's exports to the GCC rose to almost $550 million, including iron and steel, which made up 30% of Egypt's non-hydrocarbon exports (Eid 2008: 75-77).

Contrary to the impression given by these observers (Eid 2008; Mohieldin 2008), the bulk of total FDI to Egypt actually came from the West (see "Energy" below) and GCC FDI was not sustained. In 2008, for example, 33 percent came from the United States and 36 percent from the European Union. Only 18 percent came from other Arab Countries, mostly in finance, real estate and construction (ESCWA 2009: 9). In the later part of the calendar year 2008, the wave of FDI to Egypt began to ebb, in total decreasing by 18 percent from 2007 to 2008 and then by another 30 percent in 2009. Liberal reforms notwithstanding, the Arab share of FDI to Egypt fell to 15 percent of the total in 2009, then to 13 percent in 2010,

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[20] Most of the workers were from South Asia. The treatment of these workers and their unregulated working and living conditions were repeatedly and publicly criticized by a number of sources, including the United States State Department, from 2006 to 2011 (Institute for Global Labor and Human Rights. 2011. "Campaign: Jordan," 2006 to 2011 (http://www.globallabourrights.org/campaigns?id=0017).

[21] Main sources of non-Arab, non-Western investment were Israel, India, Sri Lanka and South Korea.

[22] Egypt's fiscal year brackets two calendar years, so statistics are often cited in this form. The IFIs adjust the incoming data to spread it over adjacent calendar years so that Egypt can be compared to other countries.

with the UAE's contribution declining most steeply (Dhaman 2011: Table 7 and Country Fact Sheet, Egypt).

Mixed Legacy of GCC FDI in Mediterranean

On one hand, real estate projects such as luxury apartment blocks, gated communities, shopping malls and tourist resorts were mostly targeted to wealthier social strata and contributed little to sustainable development. The focus on mergers and acquisitions, in which GCC purchasers became increasingly important on a world scale in the 2000s, and on financial and other services provided few developmental benefits unless the acquired enterprises were actually improved. Investment in manufacturing for export often took place in free-zone enclaves, creating too little of the forward and backward linkages and new jobs in the host economies that FDI theoretically generates. The evaporation of 50 percent of Egyptian firms from the stock market from 2007 to 2010 (see "Financial Crisis" below) may mean that privatization and mergers and acquisitions dampened competition and productive activity, contrary to predictions by proponents of liberalization.

On the other hand, many projects contributed to gross fixed capital formation (GFCF) in infrastructure, utilities, transportation and logistics, and Gulf investors were less interested in energy extraction than in practical downstream uses of hydrocarbon inputs for production of plastics, chemicals and fertilizers. The growth of manufactured exports in Egypt, Jordan, Tunisia and Morocco in the 2000s lends credence to the argument that FDI is endogenously and causally related to growth. Furthermore, FDI to the Med in the 2000s, from all sources, may have helped to raise productivity growth, from an annual rate of 0.6 percent in 1986-1990 to more than two percent per year from 2001 to 2008. This, in turn, may have stimulated more investment among MED countries themselves, as Turkish and Egyptian Trans-National Corporations (TNCs) in particular were praised for their contributions to intra-Mediterranean FDI from 2003 to 2010 (de Saint Laurent et al. 2011: 11-14, 18-28, 38-39).

Despite the steep decline in quantity after 2007, some qualitative changes in FDI from all sources to the MED gave promising signs for future development. First, after the cancellations or suspensions of many projects in 2009, the number of announced projects for 2010 rose by more than 50 percent, from 542 to 826. These were smaller, less costly, and more focused projects, including among Gulf-based investors, such as partnerships with local firms, franchise arrangements, joint ventures with SMEs, and the joining, and expanding or improving, of ongoing "brownfield" operations (de Saint Laurent et al. 2011: 9-11).[23] Second, post-crisis investors, from the Gulf as well as from Europe,

[23] Energy was again at the top with 19 percent of total FDI in 2010, followed by financial services with 15 percent, public works and real estate with 13 percent, and telecom/internet with 12

doubled the number of direct jobs created by their FDI between 2008 and 2010 as compared to previous years (de Saint Laurent et al. 2011: 40-41). Third, some GCC private equity firms maintained or restored their investments in the MED, or started new projects, on a more modest scale, open to innovation and making longer-run commitments that did not provide quick profits (Tabet and de Saint-Laurent 2011: 3-6). The UAE-based Abraaj Capital even formally committed itself to "socially responsible investment" (Luçon and Lapujade 2011: 74).

Continued Primacy of Energy Investment in MED and GCC Subregions

Investment in the energy sector in the region was important to both GCC and Western firms, as well as to rising non-Western, non-regional investors throughout the 2000s. Of their total FDI to the Mediterranean in the boom years, European investors allocated 23 percent to energy projects and investors from North America allocated 19 percent, while Gulf investors allocated six percent. As compared to Gulf investors, who focused on downstream industries like plastics and fertilizer,[24] Western firms put more resources into extracting, processing and exporting energy from the Mediterranean than in using it for manufacturing in the host economies (de Saint Laurent et al. 2011: 15-16). Western energy projects in the Mediterranean, unlike most other European-sponsored FDI, tended to be large-scale, expensive and capital-intensive rather than employment-generating.

Energy continued to be the single largest sector for FDI inflow to the Mediterranean through the crisis and recovery years as well, accounting for 24 percent in 2008, 39 percent in 2009, and 30 percent in 2010 (de Saint Laurent et al. 2011: 15-16). For example, European investors accounted for 89 to 90 percent of FDI to Tunisia in 2009 and 2010, with energy absorbing 54 percent of total FDI in 2009 and 62 percent in 2010 (Dhaman 2011: Country Fact Sheet Tunisia).[25] Similarly in Egypt, the hydrocarbon sector absorbed from 27 to 66 percent of FDI over the 2006 to 2010 years.[26] Among non-Arab sources of FDI, 59 percent came from Europe, with the UK alone supplying 38 percentage points,

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percent. Investment in tourism and chemicals/petrochemicals decreased, while wholesale and retail distribution, automobile assemblage, aerospace, engineering, public electronics and logistics shares grew (de Saint-Laurent et al 2011: 15-16).

[24] One exception was the privately owned Kuwait Energy plc firm, which worked three concession blocks in exploration and extraction of oil and gas in Egypt as of 2011 (http://www.arabtimesonline.com/NewsDetails/tabid/96/smid/414/ArticleID/179526/t/Kuwait-Energy-makes-new-oil-find/Default.aspx).

[25] As of 2011, the British Gas company controlled 60 percent of Tunisia's domestic market for natural gas, which was used to generate electricity among other things, and also exported natural gas through the pipeline to Sicily (www.investintunisia.tn).

[26] www.investment.gov.eg

and another 23 percent came from the United States, mostly targeted to energy (Dhaman 2011: Country Fact Sheet Egypt).[27]

In contrast to their FDI in the Mediterranean in the 2000s, Gulf investors devoted more resources to developing all stages of energy production, export and use in their own neighborhood. The growth of natural gas was expected to outpace that of oil, not only for export, especially by Qatar, but also for domestic manufacturing, as feedstock for petrochemicals and “clean” fuel for heavy industry such as aluminum, steel and cement (Samba 2011: 6). In a clear example of FDI leading growth, Yemen experienced an unprecedented burst of FDI from 2006 to 2008 (see Figure 10a below) from GCC neighbors, led by Saudi Arabia, to develop natural gas extraction and to complete an LNG production facility. While FDI in 2009 was less than one-tenth of that in 2008, mainly from Qatar to operate the new facilities, Yemen’s growth rate had doubled to between seven and eight percent by 2010 (ESCWA 2011: 21-22).

Sudan experienced surges of both FDI and growth starting in 2003 and peaking in 2006 with FDI at almost 10 percent of GDP and a GDP growth rate of 11.3 percent. In fact, Sudan ranked among the top five Arab FDI recipients every year, receiving a cumulative 4.4 percent of total FDI inflow to the Arab region and 14 percent of inter-Arab FDI in the 2000-2009 period (Dhaman 2011: Country Fact Sheet Sudan). In 2009, firms from Saudi Arabia, the UAE, Egypt and Lebanon invested in diverse sectors, including energy. However, in another important illustration of the growing role of non-Arab, non-Western FDI, Asian sources accounted for 65 percent of total FDI inflow, mostly for energy (ESCWA 2011: 20-21).

Oman and Bahrain were the least wealthy of the six GCC countries, in terms of both hydrocarbon resources and per capita income, but their economies were buoyed by energy-related FDI and other transfers. Oil and gas absorbed 65 percent of FDI to Oman in 2008. West Asian neighbors led by the UAE accounted for 32 percent, the UK 34 percent, and the US 30 percent, all focused primarily on hydrocarbons. For example, the Abu Dhabi IPIC fund was central to establishment of new refining and petrochemical plants (ESCWA 2011: 7-8). In contrast, FDI inflow to Bahrain during the 2000s boom had been concentrated in financial services, tourism and real estate. FDI peaked at a uniquely high 18.4 percent of GDP in 2006, but collapsed to about one percent in 2009 and 2010, causing Bahrain to incur the region’s second highest debt to GDP ratio, ranging from 139 to 155 percent from 2007 to 2010 (ESCWA 2011: 6; Dhaman 2011:

[27] Both UK and US investors were enthusiastically focused on energy, from upstream exploration and production of oil and gas, through transport via the Suez Canal, the SUMED pipeline and the natural gas grid, to downstream activities like oil refining and gas liquefaction, as well as distribution to both the domestic and export markets. See US Department of Energy, “Country Analysis Briefs: Egypt,” Feb 2011 (www.eia.doe.gov) and UK Organization of Trade and Investment, “Oil and Gas Opportunities in Egypt,” 2010 [both retrieved 8 April 2012].

Country Fact Sheet Bahrain). However, its growth rate did not fall below three percent in 2009, as Saudi-based companies continued to invest in Bahrain's aluminum and petrochemical industries and to augment the supply of subsidized crude oil to refine for export.[28]

Among the Top Four GCC hydrocarbon exporters themselves, Kuwait was the least attractive to foreign direct investment from any source. As measured by percent of GDP, its outflows routinely outweighed its inflows by a factor of up to 100 in the 2000s, but the bulk of Kuwait's inter-Arab investment was within the GCC, for example 70 percent to Saudi Arabia and 20 percent to the UAE in 2009 (Dhaman 2010: Table 4). In contrast to Kuwait, FDI to Qatar reached a peak of over 8 percent of GDP in 2009, even as GDP growth rose to almost 12 percent in that year. The most important source was the United States and the most important sector was natural gas extraction, liquefaction and associated downstream industries (ESCWA 2011: 9). The UAE may be unique in that its inflows and outflows of FDI netted to about zero in the 2000s, with much of the inflow going to Dubai, almost 90 percent to services, and much of the outflow coming from Abu Dhabi. These flows were largely intraregional and concentrated within the GCC. For example, in 2009, Arab sources accounted for over 90 percent of FDI to the UAE, one-third of which came from Kuwait, 17 percent from Qatar, and 13 percent from Saudi Arabia. In turn, 75 percent of UAE outward FDI to the Arab world in 2009 went to Saudi Arabia (Dhaman 2011: Table 4; and Country Fact Sheet UAE).

Financial Crisis, Recession and Recovery

Financial Crisis in the GCC

The global financial crisis and recession of 2008-2009 dealt the GCC economies a hard blow. It was inevitable that the deflation of the asset price bubble in the West would cause losses to GCC investment agencies and private funds, given the large proportion of their portfolios held abroad. The total net foreign assets of the GCC, including official reserves and holdings by financial institutions and SWFs, had risen from \$500 billion in 2002 to \$1.6 trillion by July of 2008, then fell by 19

[28] An estimated two-thirds of Bahrain's 2010 budget revenues came from sales of oil from the Saudi-owned Abu Saafa oil field. Another consistent source of foreign exchange is the US purchase of fuel for its Western Pacific military operations in informal exchange for Bahrain's hosting of the Fifth Fleet naval base (http://www.bahrainedb.com/aluminium-bahrain.aspx; http://uk.reuters.com/article/2011/10/06/uk-bahrain-budget-idUKTRE7952UY20111006; http://www.thedailybeast.com/newsweek/2011/06/26/pentagon-billions-are-flowing-to-middle-east-dictators.html).

percent to $1.3 trillion at the end of 2008. SWFs alone lost 12 percent of their capital value, from $724 billion in 2007 to $634 billion by end 2008 (IIF 2009: 2).

On the domestic front, imprudent local bank lending had fed a burgeoning demand in domestic asset markets, including consumer finance, securities, real estate and construction, where speculation had driven up prices. When these asset-price bubbles deflated in 2008, there began a “sharp correction” in GCC financial markets, generating an excessive level of non-performing loans and threats of default. In 2009, GCC banks faced high ratios for loans-to-assets and loans-to-deposits, of 60 and 120 percent respectively (NBK 2011: 32-33). Following a debt default by two private Saudi conglomerates and the UAE-based Dubai World, net private inflows collapsed (IIF 2010: 19) and local capital fled.[29]

In addition, GCC borrowers had built up significant debt in international capital markets during the boom years to finance large-scale investment in infrastructure and industry, accounting for about 60 percent of total commitments in 2007 (Hanieh 2011: 133, 138-139). However, the financial crisis of 2008 led to a “sustained withdrawal of foreign liquidity from GCC financial markets” as international lenders extracted their outstanding capital to protect themselves from the fall in value of their assets elsewhere, and portfolio investors flew to safety in the West, e.g. to US Treasury Bonds. Combined with the fall of export revenues in 2008 and 2009 due to falling oil prices, this drain on local financial markets left GCC investors without sufficient funds to service their debt (Carey 2008: 2).

As GDP growth rates plunged (refer to Figure 1a), GCC governments intervened to support their financial systems and stimulate domestic growth. Central banks expanded deposit guarantees, bailed out or took charge of weakened banks and investment companies, and loosened monetary policy, while large fiscal stimulus programs were put into place (Carey 2008: 2). Given the “huge infrastructure and energy projects that are already on course,” GCC governments hastened to provide sovereign backing for distressed financial institutions in order to restore their appeal to foreign investors (IIF 2010: 20). Their use of public finance in “cleaning up bank balance sheets” in 2009 and 2010 (NBK 2011: 32-33) enabled larger conglomerates and sovereign investment agencies to borrow $32 billion in 2009 and $26 billion in 2010 on international capital markets (Samba 2011: 5, 4, 16).

Crisis Transmission to the Developing MENA Economies

The developing MENA economies were not immediately affected by the financial crisis of 2008. While they had been criticized repeatedly by the international financial agencies for insufficient liberalization of their financial sectors, most

[29] In just five months, from August 2008 to January 2009, inflows of $2.7 billion were deposited in Lebanese banks, while official reserves in Lebanon rose from 39 percent of GDP at the end of 2007 to 60 percent at the end of 2008 (Kouame 2009: 6)

escaped the worst of the crisis for that very reason.[30] Except for Turkey, they were not well integrated into global financial markets and most local banks had not acquired the kind of "toxic assets" that brought down much bigger banks, investment companies and insurance companies in the West (Kouame 2009: 6). In contrast to GCC banks, Levant banks were more vested in government securities and central bank instruments bearing relatively low risk and had reasonable ratios of 40 percent for loans to assets and 70 percent for loans to deposits in 2009 (NBK 2011: 32-33).

However, the developing economies were affected indirectly via the GCC crisis by declines in regional stock markets and shifts in portfolio flows. GCC stock markets had been informally integrated by the cross-border investments of Khaleeji private firms (Hanieh 2011: 134-138) and affected performance in other regional markets. In general, GCC stock market indices peaked in July 2008, fell by half by March 2009, and were restored to just 75 percent of their peak value by end 2010 (NBK 2011: 10). Similarly, market capitalization had been at a peak of $1,300 billion at the end of 2007, fell by 40 percent in 2008, and ended 2010 still 24 percent below the peak. The markets that gained the most in capitalization were Saudi Arabia, Qatar and Kuwait, thanks to public infusions, as markets in Egypt, Jordan and Lebanon experienced losses.[31]

Among the shifts in the number and nationality of firms listed on the Arab stock markets, most countries showed small changes and some added a significant number of companies, especially Saudi Arabia with a total increase of 43. The stark exception was Egypt, where listings on the Cairo and Alexandria exchanges declined by over 50 percent, from 435 firms in 2007 to 212 in 2010 (Dhaman 2011, 2010, 2009: Table 10). In part reflecting the privatization of public sector enterprises, Egyptian companies' activities in mergers and acquisitions peaked in 2008, with $16 million worth of sales but just $4.6 million in purchases (UNCTAD 2011: Country Fact Sheet Egypt). As a group, the Arab countries reached a peak at 2.7 percent as sellers in global cross-border M&As in 2008, but accounted for a record 11.1 percent of global purchases in 2009 (Dhaman 2011: Table 8), led by GCC-based investors' export of capital.

Real Sector Effects on Developing MENA Economies

The developing economies were affected directly by the recession of 2009, with declines in hydrocarbon and other export revenues, tourism receipts, labor remittances, and, most dramatically, equity investment, especially FDI. As oil prices fell in 2009, oil exporters' current account surpluses shrank, and remained

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[30]See, for example, World Bank 2012: 95; World Bank 2010: 8; Sturm and Sauter 2010: 5; IMF 2009: 17.

[31] Nadim Kawach 2010. "Arab Bourses Gain $100 billion in 2010, but Trading tumbles by nearly $224 bn due to Global Crisis," *Emirates 24/7*. www.emirates247.com/.../arab-bourses-gain-100bn-in-2010-2010-12-28-1.334886

lower in 2010 than the pre-crisis levels of 2007. The Mediterranean-partner countries that export oil and gas mainly to Europe, namely Algeria, Libya and Mauritania, saw their exports to Europe drop by 45 percent, and the more diversified economies – from Morocco to Lebanon – saw their manufactured exports to Europe fall by 20 to 30 percent (Sturm and Sauter 2010: 10; World Bank 2010b: 142-144).

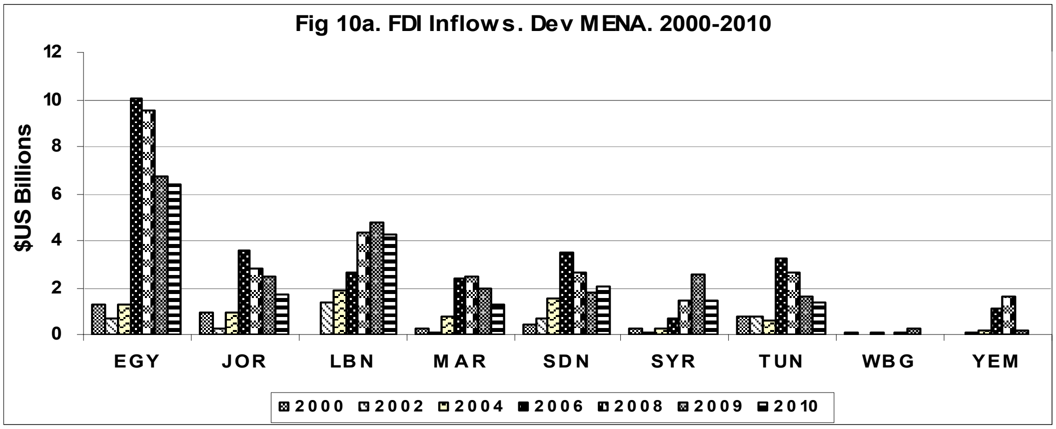
Inter-Arab trade served neither as a cushion in the recession of 2009 nor as a stimulus during the recovery of 2010. As world trade decreased by 12.2 percent from 2008 to 2009, total Arab exports to the world decreased by 34 percent, and total *inter-Arab exports* decreased by almost as much, 30%. In parallel, as total Arab imports from the world decreased by 16.5 percent, total *inter-Arab imports* decreased by almost as much, 15.8 percent, a surprise given the advantages that buying necessary imports from the region could have in a recession. In 2010, while total inter-Arab imports grew at the same 10 percent rate as total Arab imports from the world, and total Arab exports to the world increased by almost 29 percent, inter-Arab exports increased by only 6.5 percent (Dhaman 2011: 15 and Table 9). The aggregate Arab trade surplus had doubled from 2009 to 2010, but, as shown in Figure 3 above, most of the benefits went to the major hydrocarbon exporters, while everyone else's balance remained negative.

Other secondary effects, such as changes in remittances and tourist revenues, were varied in their impact on the developing countries in 2009. Remittances fell for almost all Mediterranean countries in 2009. Morocco and Egypt incurred the steepest losses, almost 17 percent and 10 percent, respectively. Some countries that routinely hosted more tourists from the Gulf, like Egypt and Jordan, lost share, while others, including Lebanon and Syria, gained (Sturm and Sauter 2010: 11), perhaps accompanying flight capital. In any case, remittances and tourism revenues would recover faster than FDI in 2009 and 2010.

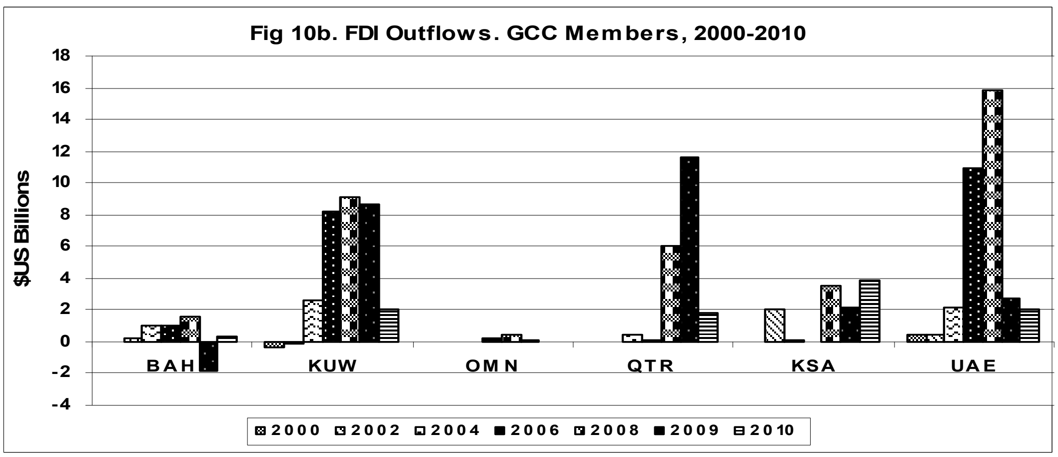
Impact of Crisis and Recovery on FDI

In 2010, both FDI to the MENA region and inter-Arab FDI continued to favor the GCC and Saudi Arabia in particular, while FDI to the developing countries, especially GCC-sourced FDI, remained low. Global FDI recovered slowly in 2009 and 2010, but MENA's share of world FDI inflow rose to 7.5% and FDI inflows to the Arab region in particular increased by about ten percent (Dhaman 2011b: 7-10). The leading Arab recipients of global inflow were Saudi Arabia, Qatar and the UAE, and despite their role in transmitting the financial crisis to the region, Saudi Arabia and the UAE together took in more than 85 percent of inter-Arab FDI in 2010 (NBK 2011: 15).

The prognosis for FDI to the MENA region after 2011 was most favorable for those countries that already received large doses of FDI in energy-related industries or that were considered regional hubs, Saudi Arabia, Qatar and the



Source: World Bank, World Development Indicators Online, 26apr12



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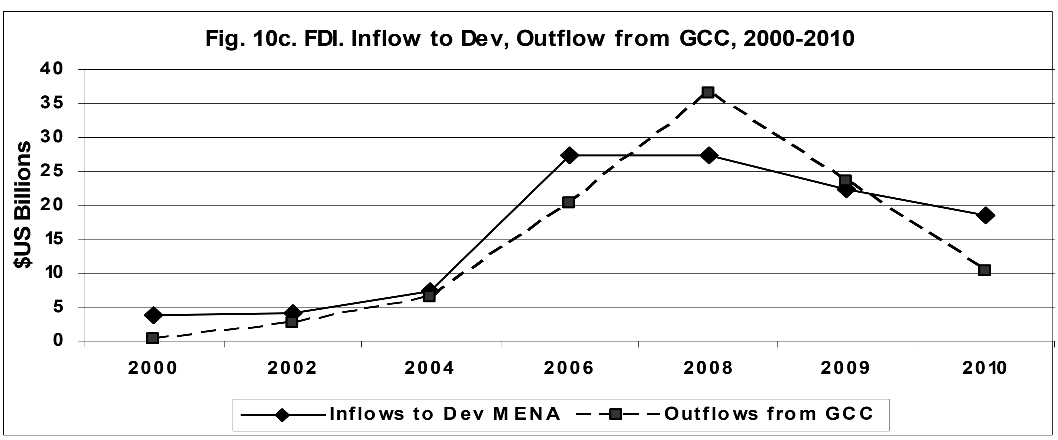

Source: World Bank, World Development Indicators Online, 26apr12
Note: Dev MENA =Egypt,Jordan.Lebanon,Morocco,Sudan,Syria,Tunisia,West Bank Gaza,Yemen

UAE in particular. UNCTAD's 2010 survey of transnational corporations (TNCs) predicted that global FDI in 2012 would remain below it peak in 2007, and that, while FDI would increase to every emerging region, MENA would see the smallest increase, with the prominent exception of investment in energy (UNCTAD 2010). Of the projected FDI inflows to Africa and the Middle East together, \$65 billion in 2011 and \$67 billion in 2012, 30 percent would go to Saudi Arabia and the UAE alone, \$25 billion and \$15 billion, respectively, mainly to "the energy sector and related industries" (IIF January 2011: 21). Another survey reported that multinational investors ranked the UAE 11th among desirable places to invest, and preferred Dubai to Cairo because of the quality of its infrastructure and logistics, its "ease of doing business," and its safe political environment. Comparing it to Hong Kong as the gateway to China, these investors considered Dubai to be a "hub for the region" connecting more than 500 million consumers from Morocco to Pakistan (Kearney 2010: 11, 20-21), while, in this view, economies like Egypt were left to languish in the hinterland.

The absolute quantity of FDI to Mediterranean developing countries fell much more sharply than other inflows, and there was a decided decline in the GCC's relative share in 2009 and 2010 as well. As shown in Figure 9a, total FDI to the MED-13 from all sources fell from its peak in 2006, at Euros 66.7 billion, to a low of Euros 28.4 billion in 2009. The subsequent increase to Euros 33.2 billion in 2010 was still significantly below the start of the boom in 2005. The Gulf's share of the provision had fallen to 16 percent by 2010, while Europe's share increased to 51 percent. Furthermore, FDI from "other countries" (that is, other than Europe, the Gulf, the United States/Canada, and the MED itself), came in at a record 16 percent, about equal to that from the Gulf. As can be seen in Figures 10a, 10b and 10c, FDI outflow from the GCC and inflows to the developing countries of the region were expected to remain subdued after 2010. The "experts" were quiet on this subject in 2011, as, for example, there is no mention of Gulf FDI to, or "pace-setting leadership" of, the developing countries of MENA during the recovery in what would have been the appropriate places in the IMF's projections in January 2011 (IMF 2011a: 5, 21, 28, 32, 50-53), while the World Bank offered a vague hope in January 2012 that GCC intraregional investment might be restored eventually (World Bank 2012: 125).

Assessment: FDI, Growth and Development in the MENA Region

Lending credence to the argument that growth "causes" FDI rather than the other way round, GCC-sourced investment in the developing countries of the region, especially to the Mediterranean Arab countries of Egypt, Jordan and Lebanon, rose only during the boom years of the mid-2000s, surpassing FDI from other regions briefly, when growth was high and liberalization was underway. The one clear exception was in the case of Yemen's natural gas industry, where FDI from the GCC, led by Saudi Arabia, rose from 2006 to 2008 and was then followed by a burst of growth. At the same time, GCC countries, Saudi Arabia in particular, absorbed much more financial inflow from the region and from the world than they provided to the region from 2000 to 2010, a pattern that was expected to continue in the subsequent decade. GCC countries exported large amounts of capital to the West, in the legal forms of private equity funds and public portfolios like sovereign wealth funds, and in the sub-legal form of illicit financial flows, in proportions that were many times greater than what was offered to the region as FDI. In the later 2000s, investors from the GCC preferred investment in themselves to investment in the developing countries of the region, spurred on by the emergence of pan-GCC private conglomerates with good connections to their respective home governments (Hanieh 2011: 172-177),

The revival of growth to GCC economies in 2010 was determined by a combination of rising hydrocarbon export revenues, including increased trade with the faster-growing Asian economies, public sector investment and government rescue of a stricken financial sector that had yet to recover as of the beginning of 2011 (IMF 2011a: 17). Growth in the GCC was expected to increase in 2011 and 2012 (see Fig 1a), led by rapid increases in natural gas production and export, but GCC private non-hydrocarbon sectors were expected to remain in the doldrums, and, contrary to the proud exposition by the Saudi Investment Authority of all the attractive non-hydrocarbon arenas for foreign investment, the largest portion of FDI would continue to flow to the hydrocarbon and affiliated sectors.

Contrary to the prognostications cited earlier by the IFIs and other economic experts about the GCC's positive leading role,[32] the GCC led the region into crisis in 2008 with spillovers from its own speculative boom and crash. It did not cushion the real-sector blows to the developing economies with trade or FDI during the 2009 recession, and it cannot be credited with leading the recovery in 2010, except for its role in the hydrocarbon industry in its immediate neighborhood. The GCC's contributions to the recovery of the developing economies came passively through traditional channels of tourism and remittances, both of which flowed as much as from outside the MENA region as from within it. Figure 11 indicates that FDI lagged behind the restoration of remittances and tourism revenues.

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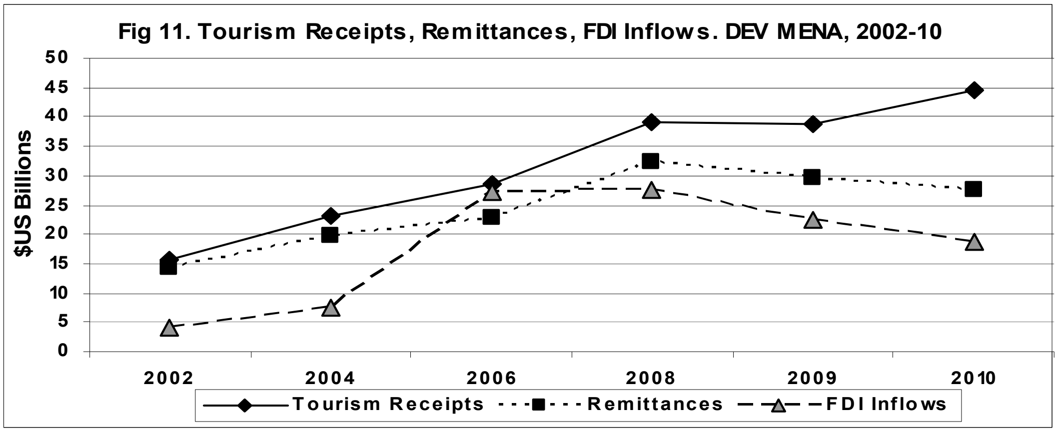
[32] For example, see Khamis and Senhadji 2010b; Sturm and Sauter 2010: 13; World Bank 2010a.; and Nadim Kawach : "GCC to Lead MENA Growth: World Bank," http://www.emirates247.com/eb247/economy/regional-economy/gcc-to-lead-mena-growth-world-bank-2010-05-19-1.245682



Source: World Bank, World Development Indicators Online, retrieved 26apr12
Note: Dev MENA =Egypt,Jordan.Lebanon,Morocco,Sudan,Syria,Tunisia,West Bank Gaza,Yemen

Before the Arab uprisings, growth in the developing economies of MENA was predicted to return to its long-term trend in 2010 to 2012, as seen in Figure 1b above, although this was below the high rates attained in the mid-2000s, and below the average for the developing regions as a group. The restoration of growth to the developing and diversified countries of the region in 2010 was determined by their own domestic investment, both public and private, fiscal stimulus packages, and growing internal demand by all strata of the population (Khamis and Senhadji 2010a: 145). It was also fed by renewed export revenues from trade with diverse sources, tourism revenues, remittances from émigré labor, and growing investment more from Europe and other emerging economies than from the GCC. As of the beginning of 2011, the emperor's clothes had become threadbare, and, instead of a single region running from the MED to the GULF, these two sub-regions seemed to be going their separate ways in a round of regional economic disintegration.

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